

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
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The state budget

During January-November 2003 the federal budget revenues execution in cash terms amounted to 19.3% of GDP, expenditures – to 16.7% of GDP (Table 1). As a result, there was budget surplus of 2.6% of GDP.

Table 1.

Execution of federal budget of Russian Federation (as % of GDP¹, in cash terms).

	X'02	XI'02	XII'02	I'03	II'03	III'03	IV'03	V'03	VI'03	VII'03	VIII'03	IX'03	X'03	XI'03
Revenues														
Profits tax	1.7%	1.6%	1.6%	1.2%	1.1%	1.4%	1.5%	1.4%	1.4%	1.4%	1.3%	1.3%	1.3%	1.3%
Income tax	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Unified social tax (UST)	3.1%	3.1%	3.1%	2.4%	2.7%	2.8%	2.9%	2.9%	2.8%	2.8%	2.8%	2.7%	2.7%	2.6%
Indirect taxes	8.9%	8.9%	8.9%	11.2%	10.1%	9.9%	9.6%	9.6%	9.2%	9.1%	8.9%	8.7%	8.6%	8.5%
VAT	6.9%	6.9%	6.9%	8.5%	7.4%	7.2%	7.2%	7.2%	6.9%	6.9%	6.8%	6.7%	6.6%	6.6%
Excises	2.0%	1.9%	2.0%	2.7%	2.7%	2.6%	2.4%	2.3%	2.2%	2.2%	2.1%	1.9%	1.9%	1.9%
Taxes on foreign trade and foreign economic transaction	2.8%	2.9%	3.0%	3.4%	3.4%	3.4%	3.5%	3.5%	3.4%	3.4%	3.4%	3.3%	3.3%	3.4%
Other taxes, fees and levies	2.1%	2.1%	2.1%	0.5%	1.7%	2.0%	2.2%	2.1%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
Total taxes and other payments **	18.6%	18.5%	18.6%	18.8%	19.0%	19.4%	19.6%	19.4%	18.8%	18.7%	18.4%	17.9%	17.9%	17.9%
Non-tax revenues	1.5%	1.4%	1.4%	17.5%	8.5%	1.3%	1.2%	1.7%	1.6%	1.5%	1.5%	1.4%	1.4%	1.3%
Total revenues	20.2%	20.1%	20.1%	20.8%	20.6%	20.9%	21.0%	21.3%	20.6%	20.4%	20.0%	19.5%	19.4%	19.3%
Expenditures														
State administration	0.4%	0.4%	0.5%	0.3%	0.3%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%
National defense	2.4%	2.5%	2.7%	1.5%	2.1%	2.6%	2.7%	2.7%	2.6%	2.6%	2.6%	2.5%	2.5%	2.5%
International activity	0.3%	0.3%	0.3%	-0.3%	0.0%	0.2%	0.2%	0.3%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Judicial authorities	0.2%	0.2%	0.2%	0.1%	0.1%	0.1%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Legal protection and security	1.4%	1.5%	1.7%	1.1%	1.4%	1.7%	1.7%	1.7%	1.8%	1.7%	1.7%	1.7%	1.7%	1.7%
Fundamental research	0.2%	0.3%	0.3%	0.1%	0.2%	0.2%	0.2%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%
Services to national economy	1.3%	1.3%	1.5%	0.2%	0.4%	0.5%	0.6%	0.7%	0.8%	0.8%	0.8%	0.9%	0.9%	0.9%
Social services	5.5%	5.6%	5.6%	1.5%	1.8%	2.0%	2.3%	2.2%	2.2%	2.2%	2.2%	2.1%	2.1%	2.1%
Government debt servicing	2.2%	2.0%	2.0%	1.7%	2.9%	3.0%	2.3%	2.1%	2.0%	1.8%	2.0%	2.0%	1.8%	1.7%
Other expenditures	3.9%	3.9%	3.8%	6.6%	7.1%	7.0%	7.0%	7.1%	7.1%	7.1%	7.0%	6.9%	6.8%	6.8%
Total expenditures	17.8%	18.0%	18.7%	12.7%	16.4%	17.7%	17.7%	17.7%	17.5%	17.4%	17.3%	17.1%	16.8%	16.7%
Surplus (+) / deficit (-)	2.4%	2.1%	1.4%	8.1%	4.2%	3.2%	3.3%	3.6%	3.0%	3.0%	2.7%	2.5%	2.6%	2.6%
Internal financing	-0.5%	-0.2%	-0.6%	-6.6%	-1.7%	-1.0%	-1.0%	-0.5%	-0.3%	-0.0%	-0.3%	-0.2%	-0.1%	-0.3%
External financing	1.9%	1.9%	2.0%	1.4%	2.5%	2.2%	2.3%	3.1%	3.3%	3.0%	2.9%	-2.7%	-2.5%	-2.3%
Overall financing	2.4%	2.1%	1.4%	8.1%	4.2%	3.2%	3.3%	3.6%	3.0%	3.0%	2.7%	-2.5%	-2.6%	-2.6%

* as % of GDP; ** UST is included in tax revenues

¹ Due to the information on GDP being based on preliminary estimations, the indices may be reassessed later.

As compared to the same period of the year 2002, budget revenues in January-November 2003 went down by 0.8 p.p. of GDP; budget expenditures, in their turn, decreased by 1.3 p.p. of GDP; as a result, budget surplus increased accordingly by 0.5 p.p. of GDP. At the same time, if the UST is not taken into account, budget revenues decreased by 0.3 p.p. of GDP and amounted to 16.7% of GDP. The main bulk of federal tax revenues, as before, is represented by the VAT payments – 36.9% of total tax revenues, which is almost identical to the value of this budget item in 2002.

According to preliminary information, the execution of federal budget revenues in cash terms in the year 2003 amounted to 19.4% of GDP, which is by 0.6 p.p. of GDP less than the revenue level of the year 2002. At the same time, the execution of expenditures in cash terms amounted to 17.7% of GDP (in 2002 – 18.7% of GDP); thus, the 2003 budget surplus was equal to 1.7% of GDP.

Judging by the preliminary estimation of the Ministry of Finance, the federal budget financing² in the year 2003 in the part of expenditures was executed at the level of 17.8% of GDP (Table 2), whereas in the year 2002 this item amounted to 18.7% of GDP. Federal budget revenues in 2003 decreased, as compared to the year 2002, by 0.7 % of GDP and amounted to 19.4% of GDP. Thus, budget surplus in implemented financing in the year 2003 increased, as compared to the year 2002, by 0.2 % of GDP and became equal to 1.6% of GDP.

Table 2

**Execution of federal budget of Russian Federation
(as % of GDP, implemented financing).**

	XII'02	I'03	II'03	III'03	IV'03	V'03	VI'03	VII'03	VIII'03	IX'03	X'03	XI'03	XII'03
Total expenditures	20.1%	20.8%	20.6%	20.9%	21.0%	21.3%	20.6%	20.4%	20.0%	19.6%	19.5%	19.4%	19.4%
State administration	0.5%	0.5%	0.6%	0.6%	0.6%	0.6%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
National defense	2.6%	2.5%	3.1%	3.3%	3.2%	3.1%	3.0%	2.9%	2.8%	2.7%	2.8%	2.9%	2.7%
International activity	0.3%	-0.2%	0.1%	0.2%	0.3%	0.3%	0.3%	0.3%	0.2%	0.2%	0.2%	0.2%	0.2%
Judicial authority	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Legal protection and security	1.7%	1.9%	2.2%	2.3%	2.2%	2.2%	2.1%	2.0%	1.9%	1.9%	1.9%	1.9%	1.9%
Fundamental research	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%
Services to national economy	1.5%	0.6%	0.8%	0.9%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.1%	1.1%
Social services	5.7%	2.5%	2.7%	2.7%	2.9%	2.7%	2.6%	2.5%	2.4%	2.3%	2.3%	2.4%	2.3%
Government debt servicing	2.0%	1.7%	2.9%	3.0%	2.3%	2.1%	2.0%	1.8%	2.0%	2.0%	1.8%	1.7%	1.7%
Other expenditures	3.8%	6.8%	7.5%	7.3%	7.2%	7.4%	7.3%	7.2%	7.2%	7.0%	6.9%	6.9%	7.0%
Total expenditures	18.7%	16.8%	20.5%	20.9%	20.2%	19.9%	19.2%	18.8%	18.6%	18.3%	18.0%	18.1%	17.8%
Surplus (+) / deficit (-)	1.4%	4.0%	0.2%	0.0%	0.8%	1.4%	1.3%	1.6%	1.3%	1.3%	1.5%	1.3%	1.6%

According to the data of the MTL, in December 2003 total tax payments to the federal budget amounted to approximately 114.7 billion roubles (without the unified social tax). In real terms, these revenues constitute 247.9% of the level of January 1999, whereas this index in the year 2002 was 250.2%, and in the year 2001 – 360.6% (Table 3).

At the same time, the payments of the unified social tax to the federal budget in December 2003 amounted to 44.2 billion roubles. Thus, the RF MTL in December 2003 transferred to the federal budget a total of taxes and levies in the amount of about 159 billion roubles.

² Budget execution regarding the items of implemented financing is equal to the total funds transferred by the Federal Treasury to the accounts of budget recipients. Budget execution in cash terms is equal to the budget recipients' total expenditures from their accounts.

Table 3

**Real tax payments to federal budget, according to the data of MTL
(as percentage of the data of January 1999)³.**

1999											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
100.0%	115.1%	122.0%	122.1%	104.5%	112.9%	127.0%	127.5%	124.3%	141.4%	160.8%	213.1%
2000											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
149.3%	160.5%	181.3%	205.8%	233.1%	186.9%	181.0%	186.4%	173.1%	181.1%	201.7%	254.1%
2001											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
204.4%	198.4%	227.6%	267.5%	252.2%	233.3%	231.9%	235.6%	219.4%	237.5%	247.3%	360.6%
2002*											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
218.7%	187.1%	234.8%	277.8%	239.6%	218.0%	284.4%	246.5%	254.8%	299.7%	241.0%	250.2%
2003*											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
230.0%	229.2%	265.5%	280.4%	233.2%	240.0%	260.4%	242.6%	248.7%	265.6%	231.0%	247.9%

* Without UST.

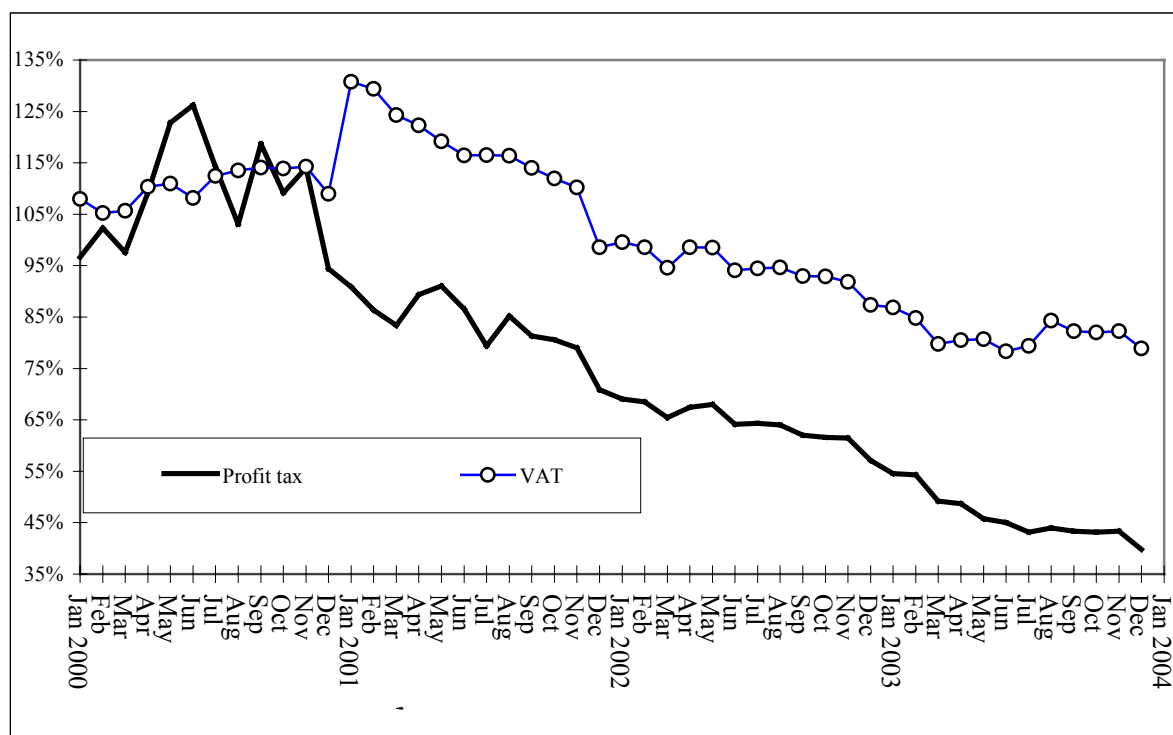


Fig. 1. Real tax arrears to the federal budget (in % to July 1999)

The changes in real arrears of basic taxes from January 2000 onward are shown in Figure 1. The arrears of payments of VAT to the federal budget in December 2003 went down by 7.6 billion roubles, and as of 1 January, 2004 amounted to 243.9 billion roubles. Similarly, the profits tax arrears decreased by 2.0 billion roubles and amounted to about 26.4 billion roubles. On the whole, the trend of the tax arrears being decreased, which was seen from early 2001 and until the second half of the year 2003, gave way to stabilization of the level of accrued arrears of both the profits tax and the value added tax.

³ The comparison to January 1999 was chosen in order to represent the most complete data available. From the point of view of tax revenues, January 1999 has nothing remarkable about it.

Table 4.

RF consolidated budget execution (as % of GDP).

1998												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes	16.2%	17.4%	18.1%	19.3%	19.7%	19.8%	19.8%	19.4%	18.8%	18.5%	18.6%	19.6%
Revenues	18.8%	20.1%	21.2%	22.4%	23.0%	23.2%	23.2%	22.9%	22.3%	22.0%	22.0%	24.5%
Expenditures	25.3%	23.8%	27.0%	28.1%	28.6%	29.5%	29.4%	28.6%	27.4%	26.9%	27.1%	29.5%
Deficit	-6.5%	-3.7%	-5.8%	-5.7%	-5.7%	-6.3%	-6.2%	-5.7%	-5.2%	-5.0%	-5.0%	-5.1%
1999												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes	16.8%	16.6%	18.1%	19.9%	20.1%	20.5%	20.8%	20.8%	20.3%	20.2%	20.9%	22.1%
Revenues	19.2%	18.9%	20.6%	22.7%	23.2%	23.9%	24.3%	24.5%	24.1%	24.0%	24.8%	26.3%
Expenditures	18.6%	20.3%	23.6%	25.6%	26.6%	27.3%	27.4%	27.4%	26.7%	26.3%	26.7%	29.2%
Deficit	0.6%	-1.5%	-3.1%	-3.0%	-3.4%	-3.4%	-3.1%	-2.9%	-2.7%	-2.3%	-1.9%	-2.9%
2000												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes	20.8%	21.4%	22.6%	24.2%	25.5%	25.4%	24.9%	24.8%	24.1%	23.7%	24.0%	24.6%
Revenues	24.4%	24.8%	26.4%	28.2%	29.7%	29.7%	29.3%	29.2%	28.4%	28.0%	28.6%	30.0%
Expenditures	19.6%	21.1%	23.8%	24.8%	25.2%	25.5%	22.3%	25.1%	24.5%	24.2%	24.6%	27.0%
Deficit	4.7%	3.7%	2.6%	3.4%	4.5%	4.3%	7.0%	4.1%	3.9%	3.8%	4.0%	3.0%
2001												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes	22.7%	23.6%	23.9%	25.4%	26.4%	26.0%	26.1%	25.9%	25.0%	24.8%	25.4%	27.1%
Revenues	25.9%	27.1%	27.4%	29.3%	30.5%	29.8%	29.9%	29.7%	28.3%	28.2%	28.8%	29.5%
Expenditures	16.8%	22.8%	23.7%	24.7%	25.1%	25.3%	25.5%	25.6%	24.9%	24.7%	25.0%	25.6%
Deficit / surplus	9.1%	4.2%	3.7%	4.7%	5.4%	4.4%	4.4%	4.1%	3.5%	3.5%	3.8%	3.9%
2002												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes*	28.7%	23.6%	24.3%	26.5%	26.6%	25.9%	26.4%	25.9%	25.2%	25.4%	25.4%	25.5%
Revenues	32.9%	31.3%	31.4%	33.6%	33.6%	32.7%	33.3%	32.5%	31.7%	32.0%	32.1%	32.1%
Expenditures	18.3%	23.7%	26.0%	28.4%	28.4%	28.8%	29.1%	28.9%	28.4%	29.3%	29.7%	31.1%
Deficit/surplus	14.6%	7.7%	5.4%	5.3%	5.2%	3.8%	4.2%	3.7%	3.3%	2.7%	2.4%	1.0%
2003												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes*	25.6%	24.4%	25.6%	27.4%	27.1%	26.0%	26.1%	25.7%	25.0%	25.0%	25.1%	
Revenues	32.0%	30.3%	31.5%	33.4%	33.6%	32.2%	32.2%	31.6%	30.9%	30.8%	30.7%	
Expenditures	20.7%	25.3%	27.7%	28.8%	28.8%	28.6%	28.7%	28.5%	28.2%	27.8%	27.9%	
Deficit/surplus	11.3%	5.0%	3.8%	4.5%	4.7%	3.5%	3.6%	3.1%	2.7%	3.0%	2.8%	

* without USC

The consolidated budget revenues in January through November 2003 amounted to 30.7% of GDP, of these tax revenues (without the USC) constituted 25.1% of GDP (Table 4). The consolidated budget expenditures went down, as compared to the level of January-through-November 2002, by 1.8 p.p. of GDP and amounted to 27.9% of GDP. The consolidated budget surplus as of 1 December, 2003 amounted to 2.8% of GDP, which is by 0.4 p.p. of GDP higher than the value of the same index during the same period of the year 2002.

A. Razin

Major events in the sphere of tax and budgetary policy in January 2004

As follows from the communication of the RF Minister of Finance Aleksey Kudrin, in the next years to come, the growth of wages, and the overall growth of the economy is going to be generally stable. This will be due, among other factors, to the decreasing tax burden. In particular, the rate of the VAT, lowered from the year 2004 onward by two per cent will result in the economy having at its disposal an additional 100 billion roubles. According to the RF Minister of Finance, this will mean that enterprises will have at their disposal bigger circulating assets, that wages will be raised, that investments in capital assets will grow, and as a result higher rates of economic growth will be seen.

At the RF Government's meeting on February 26, 2004 it is planned to discuss the issue dealing with the measures designed to complete the tax reform in this country. In particular, according to the head of the Tax Policy Department of the RF Ministry of Finance Aleksandr Ivanteev, it is intended to consider, as a separate issue, that of the measures designed to improve the administration of the value added tax, including the introduction of special bank accounts for VAT payments.

Previously it was announced that the Ministry of Finance had been delegated with the task in February to submit to the government the draft laws addressing the issues of further improvement of taxation of the profits of organizations and better VAT administration, as well as amendments to the second reading of the draft law on lowering the UST.

It has been recommended to the Ministry of Finance, when elaborating the draft law concerning the improvement of the profits tax, to enhance the stimulating function of this tax and to increase the similarities between accounting and taxation procedures, which must result in simpler tax administration. The draft law aimed at improving the VAT administration must eliminate the principle of the taxpayers crediting the state. Besides, the Ministry of Finance was delegated with the task to submit to the government, in January 2004, the new drafts of the chapters of the RF TC that regulate the personal property tax and the tax on land.

According to the Government's Chairman Mikhail Kasianov, in 2004-2005 the tax reform will be generally completed.

According to the communication of the Public Relations Administration of the Ministry of Finance of Russia, the financing for the federal budget expenditures on servicing state and municipal debt in the year 2003 was 88.3% of annual budget allocation, or 90.3% of adjusted budget revenue and expenditure.

The financing of servicing state and municipal internal debt in January-December amounted to 45.1 billion roubles, or 95.4% of annual budget allocation. The expenditures on servicing government external debt in 2003 were 175.8 billion roubles, or 86.7% of annual budget allocation, and 89.1% of adjusted budget revenue and expenditure.

In this connection, the Ministry of Finance noted that economy of the resources was achieved due to the fact that the previously planned exchange of the commercial debts of the former USSR, as well as of the debts of the former USSR to the International Investment Bank and to the International Bank for Economic Cooperation, for the eurobonds of the Russian Federation was not effected; and the other factor was the higher actual rouble-to-USD exchange rate.

S. Ponomarenko

On the progress of reforms in the year 2003 and January 2004

Despite the misgivings of experts in respect to a certain lull in the sphere of reforms owing to the impending parliamentary and presidential elections, in the year 2003 the Government managed to achieve a lot in a number of directions; there was a reform of electric power engineering, a reform of railway transport, a pension reform, and a number of others. At the same time, some new important reforms planned to be started last year (the administrative reform etc.) were postponed until after the presidential elections. Active work was started at the Center for Strategic Developments as regards such spheres of reforming as education, health care, the structure of the military machine, and the housing market, as well as the development of Kaliningrad Oblast'.

Economic reforms in the year 2003

As far as the conduct of socio-economic reforms is concerned, the results of the year 2003 are rather dubious. The year was started with a number of loud declarations on the part of the Government which stressed the necessity to spur the process of transformation in a wide range of spheres so as to guarantee the

desired stability of economic growth. As early as February 2003, the RF Ministry of Economic Development submitted a new draft of the Government's medium-term program aimed at fulfilling this task. There was a number of political statements promising that the pre-electoral character of the year 2003 would have no serious effect on the intensity of reforming activity on the part of the Government.

The message of the President voiced in the spring of that year dispatched an even stronger "political impulse", stating the aim of "doubling the GDP" in the next ten years. However, the work of the Government did not significantly intensify, maybe because the economic indices were becoming better by the month. As a result, a new medium-term program for the years 2003-2005 was approved only in August, while all the relatively radical measures specified in it as regards the administrative reform, the transformation of the mechanisms of the social sphere's budgetary financing, etc. - in fact, everything that had survived the "editorship" of the Government Apparatus - was postponed till the year 2004.

The hopes were seriously boosted by the October reanimation of the Center for Strategic Developments, once (in 1999 and 2000) a venue for discussion and development of a long-term strategy, which became an unofficial economic doctrine for four years. Submitted for expert elaboration at the Center were the most important themes of reforms which had remained practically unattended for during the four previous years - the reforms of health care and education, the formation of the market of affordable housing, the reform of the Army, and the development of Kaliningrad Oblast.

The development of the conceptual bases for reforming these spheres - as well as for drafting concrete normative and legal acts - were put under the supervision of the former First Deputy Minister of Economic Development and Trade of the Russian Federation E. S. Nabiullina, while the post of the "top" curator of this work was given to the deputy-head of the President's Administration I. I. Shuvalov. The intensity of the Center's work during the three final months of 2003 gives certain reasons to hope that the approved deadline for the preparation of the legislative base (by April 2004) would be complied with, which means that there are all chances to adopt the key laws as early as the spring session of the State Duma.

Also, it should be admitted that despite a relative lull and the absence of any significant progress in the key directions of reforms, the year 2003 was marked with a number of important decisions. Here are some of them:

In January 2003,

the Federal Law "On the introduction of alterations and amendments in the Federal Law 'On non-government pension funds'" was adopted; the following three federal laws from the reform package concerning the railway transport: "On the railway transport in the Russian Federation"; "The statute of the railway transport of the Russian Federation"; "On the introduction of alterations and amendments in the Federal Law 'On natural monopolies'". The Federal Law "On the specific features of control and management of the railway transport property" was signed by the President of the Russian Federation in February 2003.

In February 2003,

the Government of the Russian Federation issued a regulation, authorizing the list of data on the activity of the Government of the Russian Federation and the federal organs of executive power, obligatory for publishing by the information systems of general use.

In March 2003,

a number of laws from the reform package concerning electric power engineering were adopted, including the Federal Law "On electric power engineering", and certain alterations were introduced in Part Two of the Civil Code of the Russian Federation, in the Federal Law "On natural monopolies" and in the Federal Law "On State regulation of electric-power and thermal-energy rates in the Russian Federation".

In April 2003,

the Law "On the introduction of alterations in the Federal Law 'On energy conservation'" was adopted.

In May 2003,

the Government of the Russian Federation issued a regulation authorizing the plan of measures for the realization of the Program of structural reform of the railway transport for the years 2003-2005;

the Federal Law "On the system of public service in the Russian Federation" was adopted. The Law specifies the legal and organizational bases of the system of public service in the Russian Federation;

the Customs Code of the Russian Federation corresponding to the norms and regulations of the WTO was adopted.

In June 2003,

the Government of the Russian Federation issued a regulation authorizing the plan of measures for reforming the system of electric power engineering for the years 2003-2005. To substantiate the plan, a number of normative and legal acts were adopted. In particular, in September 2003 the Government of the Russian Federation issued a resolution in respect to the formation of generating companies on the wholesale market of electric power. In October 2003, the Government of the Russian Federation issued a regulation authorizing the principles of the wholesale market of electric power for the period of transition.

In July 2003,

the Government of the Russian Federation issued a resolution authorizing the Concept of the development of the market of liquefied gas for domestic use, aimed at liberalizing the abovesaid market;

the Federal Law “On the introduction of alterations and amendments in the Federal Law ‘On the general principles of organization of legislative (representative) organs of state power of the Russian Federation’s subjects’”;

the President of the Russian Federation signed an edict specifying the priority directions of the administrative reform;

the federal laws envisaging a reduction in the VAT rate and certain changes in fiscal control over the expenses incurred by physical persons were adopted. Also in July 2003, the Federal Law “On the introduction of alterations in Articles 219 and 220 of Part Two of the Tax Code of the Russian Federation” envisaging an increase in the general amount of the property tax deduction to 1 million roubles, was adopted.

In August 2003,

the Government of the Russian Federation issued a resolution authorizing the Programme of the socio-economic development of the Russian Federation in the medium-term outlook (2003-2005);

the Government of the Russian Federation issued a regulation authorizing the target program “Transition to manning a number of detachments and military units by military personnel performing military service under a contract” for the years 2004-2007;

the Government of the Russian Federation issued a resolution authorizing the Energy Strategy of Russia for the period up to the year 2020;

the Government of the Russian Federation issued a resolution authorizing the Plan of measures for the years 2003-2005 in respect to stimulation of innovations and development of venture investment.

In September 2003,

the Presidents of the Republic of Belarus, the Republic of Kazakhstan, the Russian Federation and Ukraine signed the Agreement on the formation of a joint economic space;

the Government of the Russian Federation issued a regulation establishing the open joint-stock company “Russian Railways”.

In October 2003,

the federal law envisaging the imposition of a moratorium on planned inspections during the first three years of existence of a small-scale enterprise was adopted;

the Federal Law “On the general principles of organization of local self-government in the Russian Federation” was adopted;

the Government of the Russian Federation issued a resolution authorizing the Concept of development of state financial (guaranteed) support of industrial exports in the Russian Federation,

In November 2003,

the Government of the Russian Federation issued a resolution authorizing the Rules for the provision of services as regards the usage of the infrastructure of the railway transport of general use and the Rules for non-discriminative access of transporters to the infrastructure of the railway transport of general use;

the federal law envisaging the introduction in the RF Tax Code of a Chapter concerning the charges for using the objects of the animal world and for using objects of the aquatic biological resources, submitted by the Government of the Russian Federation, was adopted;

the federal law augmenting Part Two of the Tax Code with Chapter 30 “Organization assets tax” was adopted.

In December 2003,

the President of the Russian Federation signed the Federal Law “On the insurance of deposits hold by physical persons in the banks of the Russian Federation”. In November 2003, the federal law on mortgage debentures was adopted;

also in December 2003, the Government issued a resolution authorizing the decision to create seven inter-regional long-distance network companies in the form of open joint-stock companies with participation of the Russian Federation and the open joint-stock company “The Federal Network Company of the Joint Energy System”;

the Federal Laws “On currency regulation and currency control” (revised edition), “On the basic principles of state regulation of foreign-trade activity” and “On the special protective, anti-dumping and compensatory measures concerning import of commodities”;

there were adopted a number of resolutions issued by the Government of the Russian Federation in order to promote the realization of the pension reform in accordance with the Federal Laws “On the investment of resources for financing a funded component of labor pension in the Russian Federation” and “On the introduction of alterations and amendments in the Federal Law “On non-government pension funds”;

the President of the Russian Federation approved the draft Federal Law “On the introduction of amendments in the Budgetary Code of the Russian Federation as regards the creation of a Stabilization Fund of the Russian Federation”;

the Government of the Russian Federation issued a resolution authorizing the plan of actions to be taken in the years 2004-2005 in order to realize the Program of development of budgetary federalism in the Russian Federation for the period up to the year 2005.

Reforms in January 2004

Although the first two weeks of January were, in fact, holidays, the Government was back to work already on the 3rd - and issued Resolutions No 1-r and 55-r authorizing the Plan of actions of the Government for the year 2004 and the Plan of law-drafting activity.

In accordance with the resolution of the Government of the Russian Federation from 15 January 2004, No 11, the President of the Russian Federation received, for the further submission for ratification by the State Duma of the Federal Assembly of the Russian Federation, the Agreement on the formation of a joint economic space concluded in Yalta on 19 September 2003.

In January, there was a continuation of work on updating the legislative base of the pension reform - the draft Federal Law “On the introduction of alterations in certain legislative acts of the Russian Federation in order to guarantee the realization of citizens’ rights to a funded component of labor pension”.

The Regulation of the Government of the Russian Federation from 19 January 2004, No 19 authorizes the Rules for coordination of investment programs of the subjects of natural monopolies in the sphere of power engineering, specifying the order of consideration and coordination of investment programs of the subjects of natural monopolies in the sphere of electric-power engineering, as well as the order of control to monitor their implementation.

The submitted investment program and the materials justifying it should include: a list of investment projects comprising the investment program; the information on the sources of financing of the investment program; a justification of the necessity to realize the specified investment projects, the deadlines for their realization and the volumes of the required financial resources; a financing plan of the subject of a natural monopoly, composed for a three-years period with a subdivision by the types of activity and in accordance with the program of reformation of the said subject of a natural monopoly (in case it is to be reformed); an explanatory note containing the analytic information including the expected and actual indicators of the investment program’s realization in the previous and current years, as well as a number of other documents.

The norm canceling the 5% sales tax is with effect from 1 January 2004. The expected result, at least in the form of absence of the traditional January acceleration of inflation, has not materialized - largely because the regional authorities have significantly increased the public utilities rates in order to compensate for the loss in revenues, thus influencing the rate of inflation both directly and via the growth of prices of consumer goods.

O. Fomichiov

Monetary policy

The consumer price index, according to the results of the year 2003, was 12%, which corresponds to the targets plotted by the RF Government and the Bank of Russia for the past year. In early 2004, the country’s gold-and-foreign-currency reserves have continued to grow. The Bank of Russia, in January, lowered the refinancing rate to 14%.

The inflation rate in Russia, according to the results of the year 2003, struck the upper margin of the RF Government's forecast (12%). According to the official forecast of the RF Government, the level of inflation in Russia in the year 2003 was going to be 10-12%. Thus, the inflation level in Russia in the year 2003, for the first time since 1997, did not exceed the target index set by the RF Government (in the year 1997, the inflation rate was 11%, the limit envisaged by the Law of the federal budget being 11.8%).

In December 2003, the growth of consumer prices in Russia was 1.1% (see. *Fig. 1*), in November – 1%. In December, the prices of foodstuffs grew by 1.5%, of nonfood items – by 0.6%, of paid-for services rendered to the population – by 0.9%. In Moscow and St. Petersburg, the monthly index of consumer prices never exceeded 100.9% (from the year's beginning – 110.4% and 112.2%, respectively).

According to preliminary estimations, in January the prices in the RF will go up by 2.2–2.4%.

The Growth Rate of the CPI in 2002 - 2003 (% per month).

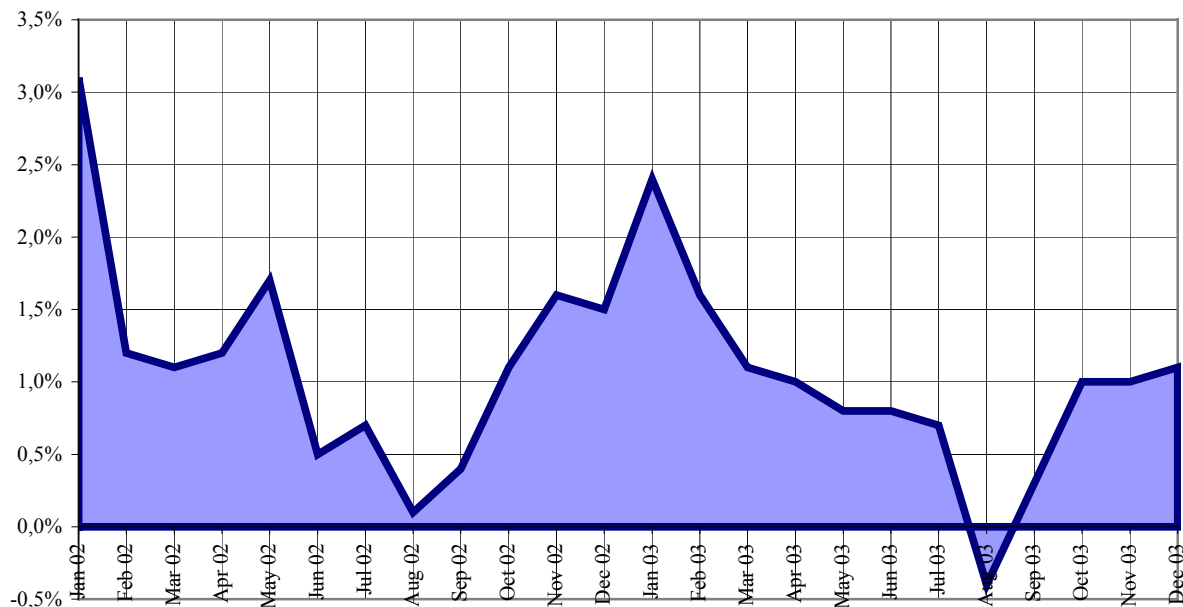


Fig. 1. Growth rate of CPI in years 2002 – 2003 (monthly %).

Russia's gold-and-foreign-currency reserves in 2003 grew by 29.1 billion USD (from 47.8 billion USD to 76.9 billion USD as of 1 January, 2004), or by 61% (see *Fig. 2*). Interestingly, 30% of this growth occurred in December, when the reserves increased by 8.8 billion USD. Such an increase in this index during one month, as well as the overall annual growth of the reserves, has hit Russia's historical maximum peak. Within the structure of the reserves, the foreign-currency component grew during the year from 44.1 billion USD to 73.2 billion USD, or by 66%. At the same time, the monetary gold volume increased from 3.7 billion USD to 3.8 billion USD, or by 0.7%. During December's last week, the gold-and-foreign-currency reserves decreased by 700 million USD and as of 2 January amounted to 77.1 billion USD, as compared to 77.8 billion USD as of 26 December. However, in the next two weeks of January the reserves once again grew by 2 billion USD (+2.6%), and on 16 January reached an eventual peak of 79.1 billion USD. At the same time, the changes in the narrow monetary base followed the changes in the amount of gold-and-foreign-currency reserves.

The RF's monetary base in a broad sense⁴ in December grew by 374.3 billion roubles – from 1.54 trillion roubles to 1.914 trillion roubles, or by 24.3%. The growth of this index in December was the highest ever seen, having by 23% exceeded its total increment during the year 2002 (by 304.3 billion roubles – from 928.3 billion roubles to 1.232 trillion roubles), and almost by 22% - the growth seen in January through November of the year 2003 (by 307.4 billion roubles - from 1,232 trillion roubles to 1,54 trillion roubles). The cash-in-circulation volume was 1.225 trillion roubles (+15%, as compared to November). The total

⁴ The RF's monetary base in a broad sense, in addition to the cash-in-circulation issued by the Bank of Russia, and the residuals on the accounts of mandatory reserves of the funds in the national currency attracted by credit institutions and deposited with the Bank of Russia, includes the funds in corresponding accounts with credit institutions and bank deposits placed with the Bank of Russia.

funds in the accounts of credit institutions with the Bank of Russia during December more than doubled and amounted to 304.9 billion roubles, while the mandatory reserves amounted to 267.4 billion roubles. The amount of banks' deposits with the Bank of Russia increased by 80.9 billion roubles – to 87,3 billion roubles. The amount of the Bank of Russia's liabilities on repurchase of securities as of 1 January, 2004 went down by 25.4 billion roubles – to 30.1 billion roubles. In January through November the broad monetary base grew by 24.9%, throughout the whole year 2003 – by 55.3%. The growth of this index in 2002 was 32.8%. It should be noted, however, that these changes of the monetary indices late in the year are associated with the seasonal fluctuations in liquidity demand and are compatible with the changes seen in the previous years. Obviously, early in the year the Bank of Russia will traditionally resort to decreasing the money supply.

Changes in the Monetary Base and in the Gold and Foreign Currency Reserves in 2003 - 2004.

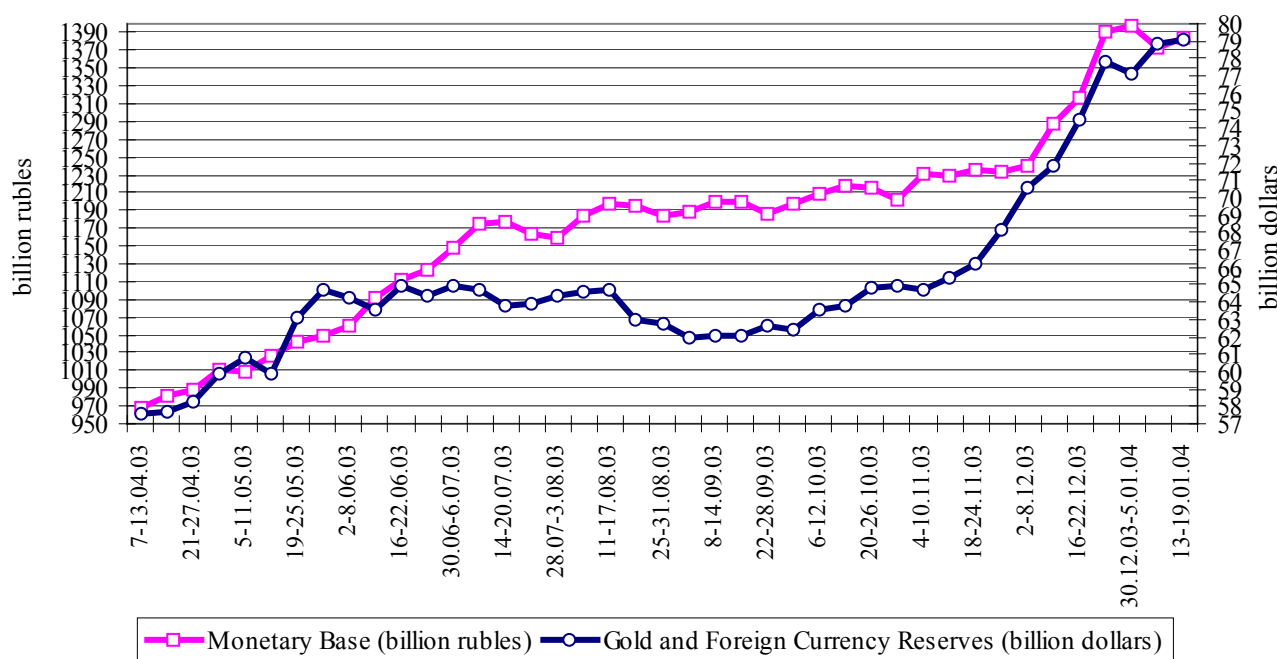


Fig. 2. Changes in (narrow) monetary base and gold-and-foreign-currency reserves of RF in years 2003 – 2004.

In January, Russia paid 1018.1 million USD to redeem the government external debt. Within this amount, total payments to redeem the actual debts amounted to 523.3 million USD, the payments of interest - to 494.8 million USD. The transfers to repay the RF's debts to official creditor countries, banks and companies in January amounted to 206.6 million USD as debt repayment, and 47.2 million USD – as interest payment. To repay the debts to international financial organizations, in January 303.8 million USD was transferred as debt repayment, and 9.1 million USD – as interest payment. The payments on RF eurobonds in January amounted to a total of 451.4 million USD, including 12.9 million USD – as debt repayment, and 438,5 million USD as interest payment. The total payments against the RF's external debt in the year 2004 are estimated to be equal to about 16.1 billion USD, including 9 billion USD as debt repayment, and 7.1 billion USD – as debt servicing.

The RF CB from 15 January lowered the refinancing rate to 14%. The decision to this effect was made by the CB's Board of Directors. The Bank of Russia had changed the refinancing rate for the last time on 21 June, 2003. At that time, the rate was lowered from 18% to 16%. Besides, at the Board's meeting it was also decided that the RF CB during the current year may sell on the open markets the securities from its portfolio in a total amount of 60 billion roubles. The limit on the operations with government securities in the year 2004, as far as REPO transactions are concerned, is established in the amount of 250 billion roubles.

Trunin P.

The government securities market

Throughout January 2004, a certain decline in the yields of tradable instruments was generally observed at the government currency-debt market, as compared with the level of December 2003. This tendency had been dominant until the third week of the month, when there emerged the information on the date of the next meeting of the shareholders. Despite the fact that this news has mostly affected the behavior of eurobonds of the corporate sector, the state segment has also been influenced by it. Against the background of a significant decline in the investors' interest, the quotations of the majority of RF currency bonds also went down. Moreover, one of the factors still determining the behavior of the eurobond markets of all developing markets including Russia is the market of US treasury bills - and throughout the month the yield of American bonds was steadily going down.

According to the data from January 23, the yields to maturity of Russian eurobonds RUS-30 amounted to 6.88% in yearly interest (7.28% by the end of December), RUS-18 - 6.62% in yearly interest (6.97% by the end of December). At the same date, the yield of Russian eurobonds amounted to: Tranche 7, internal currency bonds (6.08%), Tranche 6, internal currency bonds (3.77%), Tranche 5, internal currency bonds (5.28%) and RUS-07 (4.07%). Thus, during the first three weeks of January the yields of Russian eurobonds declined in comparison with the levels of late December 2003.

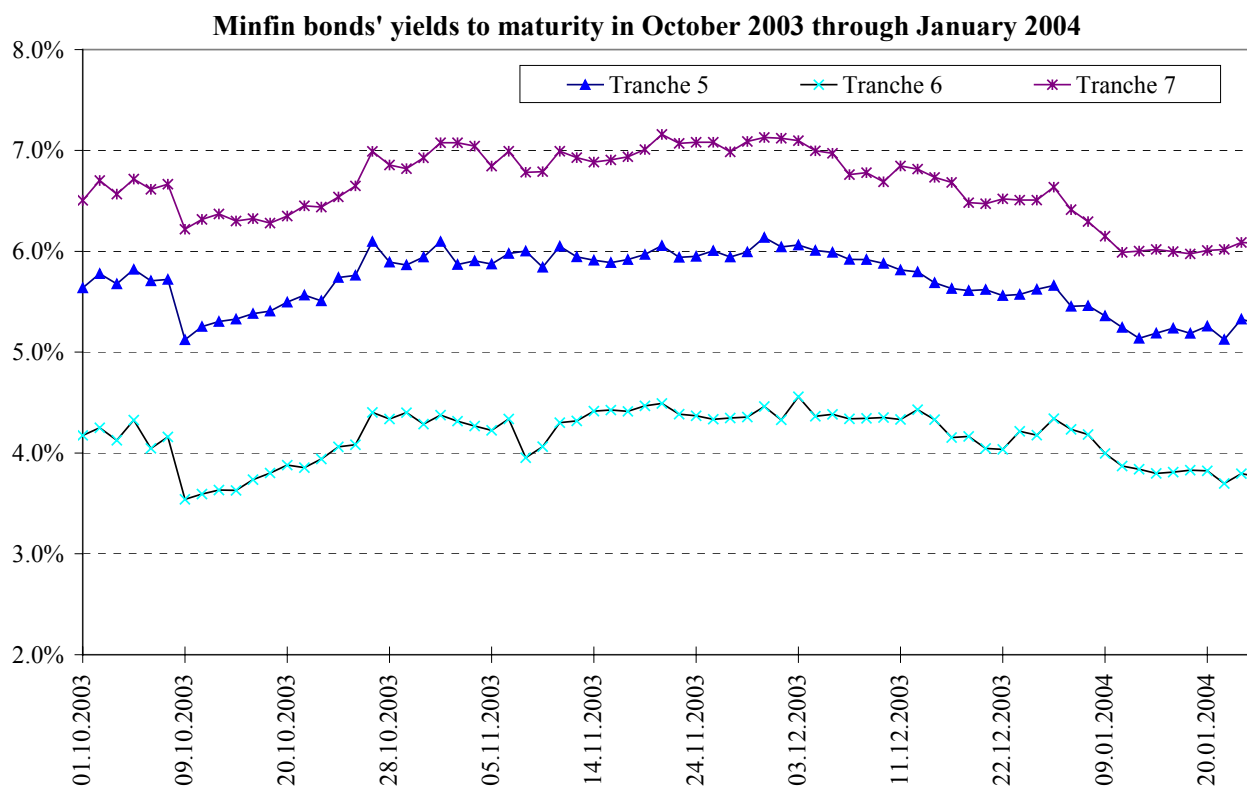


Fig. 1.

Yields to maturity of the Russian eurobonds with maturity in 2030, 2018 and 2007 in October 2003 through January 2004

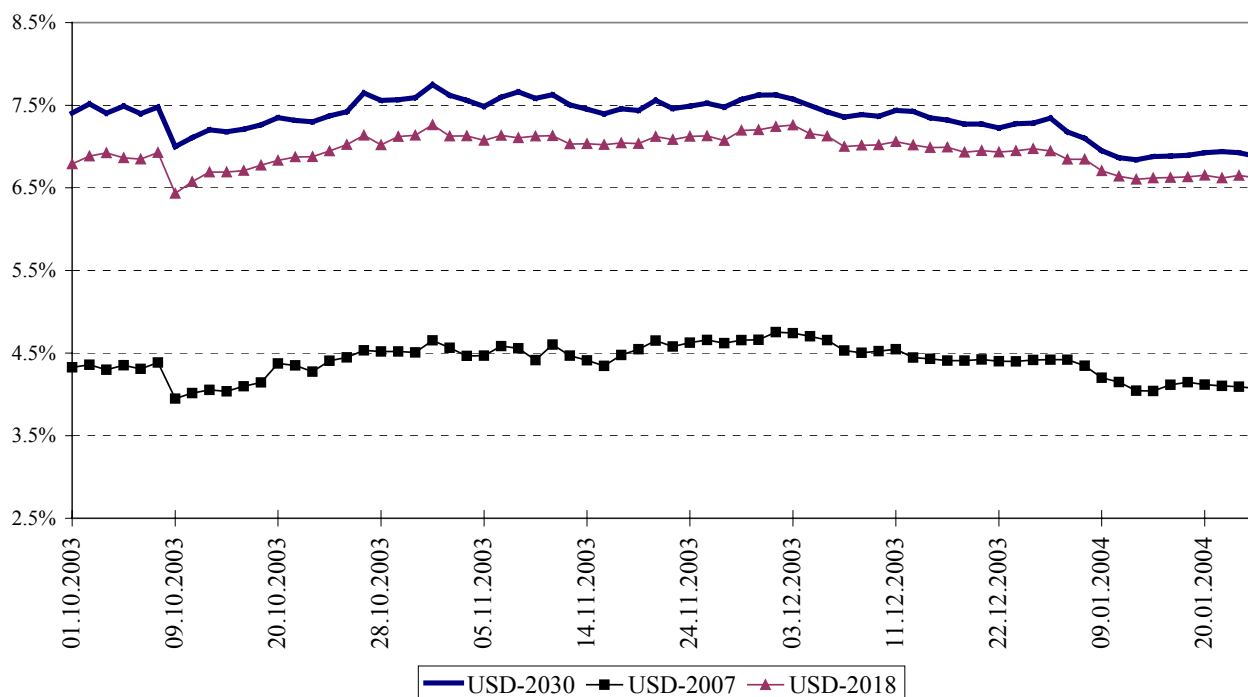


Fig. 2.

The behavior of the government rouble-debt market also pointed to an increase in quotations of government bonds. The major factors of the market behavior were the significant increase in liquidity in the banking sector and the continuing strengthening of the rouble against the dollar, enhancing the attractiveness of rouble assets. Also, another important factor positive for the future of the market was the approval by the RF Ministry of Finance of a program of internal borrowings envisaging a more than five-fold increase in the volume of loans in comparison with the level of 2003; according to representatives of the Ministry of Finance, the yields of government bounds would practically remain at the existing level.

During the period under consideration, there were two auctions for additional placement of OFZ-AD. In particular, on 21 January there were auctions for placement of OFZ-AD 46001, the nominal value 10 billion roubles, and OFZ-AD 46002, the nominal value 8 billion roubles. Issue OFZ 46001 was placed to the amount of 6.4 billion roubles at the nominal value with the weighted average yield of 7.82% in yearly interest (by 0.08 point higher that at the secondary distribution by tender). Issue OFZ 46002 was placed to the amount of 6.7 billion roubles at the nominal value with the weighted average yield of 7.97% in yearly interest (also by 0.08 point higher than the level of the yield of this instrument at the secondary distribution by tender).

As of 26 January, the volume of the GKO-OFZ market amounted to 320.58 billion roubles at the nominal value, and 348.85 billion roubles at the market value. The duration of a market portfolio of GKO-OFZ amounted to 1030.66 days.

By the end of 2003, the RF internal debt placed in government securities had increased by approximately 9 billion roubles, and on 1 January 2004 it amounted to 665.55 billion roubles at the nominal value. In 2003, the Ministry of Finance, by placing GKO and OFZ at the government internal-debt market, attracted 152 billion roubles. Last year, the volume of redemptions of GKO-OFZ amounted to 106.4 billion roubles, and therefore the balance of the Ministry of Finance's transactions in the GKO-OFZ market was 25.6 billion roubles.

On 16 January, the RF Government authorized the volumes of emission of government securities for the current year. The planned volume of GKO to be issued in the year 2004 amounts to 41 billion roubles, and it is planned to place OFZ to the amount of 220 billion roubles, while GSO are planned to be placed to the amount of 50 billion roubles. Government savings bonds should become a state instrument for investment of

a funded component of labour pension. Thus, the aggregate volume of the attracted resources would amount to 291 billion roubles. The redemption of government securities is planned to the amount of 118 billion roubles, and therefore the net attracted resources would exceed 140 billion roubles.

The corporate securities market

The state of the stock market

In January, the Russian stock market demonstrated a continuation of the steady rise in quotations. On the first Market day of the year 2004, the RTS index immediately rose by 18.83 points and stopped at the mark of 586.08 points. After some adjustment observed at the end of the first week of January, the market began to grow again. Among the major causes of the favorable behavior of the stock market, one could point out the extremely high level of liquidity in the banking sector which was steadily going up throughout the month, thus conducing to an increase in the volume of spare cash at the disposal of the investors, and – at least partially - conducing to the growth in demand for shares. The second most significant factor of the stock market's growth was the continuing strengthening of the rouble against the US dollar. In general, during the period between the 5th and the 27th of January, the RTS stock exchange index rose by 32.67 points, which corresponds to its growth by 5.57%.

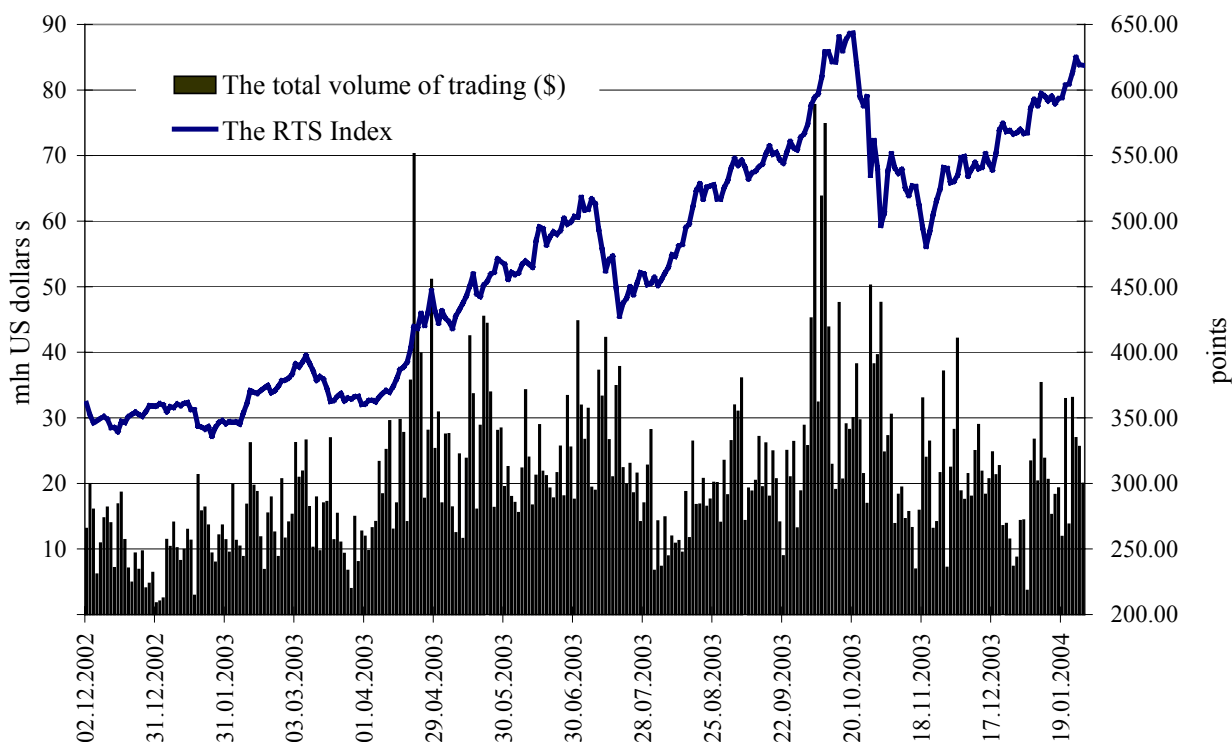


Fig. 3.

During the period between the 5th and the 27th of January, the RTS trade turnover amounted to approximately 367.2 million USD, which is comparable with the index for the same period of December 2003. The RTS average daily turnover slightly rose in comparison with the corresponding figures for December, and amounted to approximately 22.9 million USD (22.3 million USD in December). The maximum volume of trade in the RTS system (35.4 million USD) was observed on 9 January. The minimum volume of trade was registered on 19 January when it amounted to 11.88 million USD. Thus, in January, the positive, behavior of the market was mainly determined by the influence of external factors without any considerable increase in the activity of investors.

When analyzing the behavior of the most liquid shares, it should be pointed out that practically all the “blue chips” have demonstrated positive behavior by the results of the month (January 5 - 27). The leader in respect to price increase were the shares of RAO “UES” which gained 15.3%. They are followed by the

shares of “Tatneft” (+14.74%), “Sberbank of Russia” (+14.11%) and “LUKoil” (+13.23%). A slightly lesser rate of growth was demonstrated by the shares of “Rostelekom” and “Mosenergo”: +10,7% and +10.43%, respectively. The rise in world prices of metals conduced to an increase in attractiveness of shares issued by Russian metallurgical companies. In particular, common shares of “NorNikel” rose in price by 9.83%. The development of the situation around “UKOS” and the cancellation of the agreement on the merger of “UKOS” and “Sibneft” had a negative effect on the behavior of shares issued by these companies - by the results of January, their losses in value were 1.82% and 1.57%, respectively.

**Dynamics of the Russian Blue Chips
from December 23, 2003 to January 27, 2004**

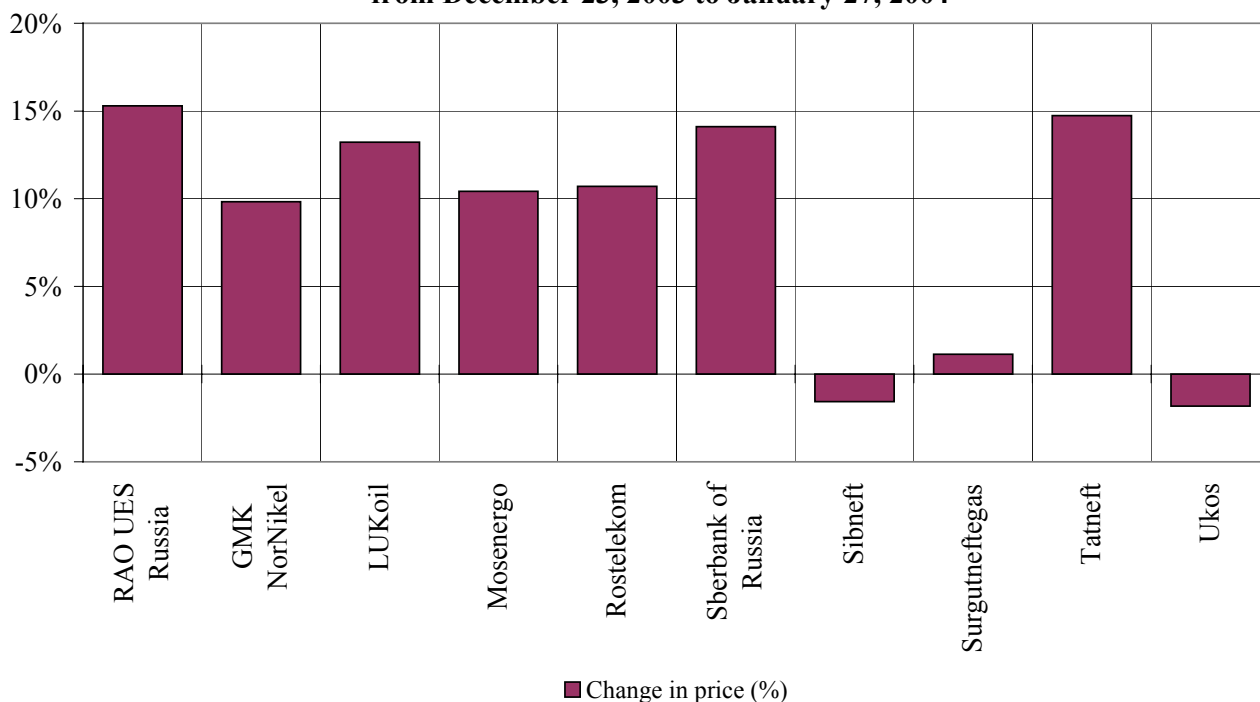


Fig. 4.

In the period between the 5th and the 27th of January, the leadership in RTS turnover⁵ was held by the shares of “LUKoil” with the aggregate volume of transactions amounting to 24,47%. A slightly lesser volume of transactions was reached by the shares of the RAO “UES of Russia” (23.99%). They are followed by the shares of “UKOS” (8.84%) and the GMK “NorNikel” with 7.31% of the total volume of trade at the Classical Market of Shares of the RTS. Thus, during the period under consideration, the aggregate share of transactions involving the stocks of just these four issuers in the total turnover of the RTS stock market amounted to 64.61% of the aggregate volume of trade and remained at practically the same level as in December 2003.

According to the data from 26 January, the Russian stock market has the following five leaders as regards capitalization⁶: “UKOS” – 28.74 billion USD, “LUKoil” - 22.18 billion USD, “Surgutneftegas”- 21.5 billion USD, GMK “NorNikel” - 15.29 billion USD and “Sibneft” - 14.22 billion USD.

The futures market. In January 2004, the investors’ activity at the RTS futures market (FORTS) practically did not change in comparison with the previous month. Thus, during the period between the 5th and the 27th of January, the aggregate turnover of the RTS futures and options market amounted to approximately 13.8 billion roubles (73.9 thousand transactions, 1.76 million contracts) which was slightly lower than the corresponding figures for December 2003 (15.9 billion roubles, 79.9 thousand transactions, 2.1 million contracts).

As in the past, the greatest demand among the participants was for futures; during the period between the 5th and the 27th of January, the volume of trade in futures amounted to 13.29 billion roubles (71.97 thousand

⁵ At the classical market of shares

⁶ According to the RTS data

transactions and 1.69 million contracts). Options were in much lesser demand - the volume of trade in them amounted to approximately 537 million roubles. The maximum volume of trade at the market was registered on 16 January when it amounted to 1.25 billion roubles; the minimum one was observed on 8 January, when it amounted to 504.7 million roubles.

The corporate bonds market. During the first three weeks of January, the rouble-denominated corporate bonds market demonstrated a generally positive behavior of quotations. Since the beginning of the month, the price index of corporate bonds tradable at Moscow International Stock Exchange⁷ had risen by 1.73 point (1.66%), while the index of the ten most liquid bonds of the corporate sector - by 1.92 point (1.66%). The major rise in quotations took place during the first market week of the month due to the extremely favorable situation with liquidity in the banking sector, as well as to the continuing strengthening of the rouble against the dollar. At the beginning of the second week of the month, the upsurge in growth continued; then there was a span of certain adjustment observed at the market. Nevertheless, starting from the second half of the week and up till 26 January, the investors preferred to fix their profits because of the general expectations of a relatively large volume of placements at the primary market. By the end of the third week of the month, the yields of the most liquid issues of corporate securities were at the level of 7%-10% in yearly interest, which was indicative of a negative actual profitability of investments in these securities, and hampered any further rise in quotations.

During the period between the 5th and the 27th of January, the aggregate turnover in the bonds section of Moscow International Stock Exchange amounted to slightly less than 6.2 billion roubles, which was relatively less than the similar figures for the corresponding period of December 2003 (6.9 billion roubles). The average daily volume of trade in January amounted to 441.7 million roubles (495.1 million roubles in December). Thus, according to the results of the first three weeks of the month, the investors' activity was relatively lower than in December 2003.

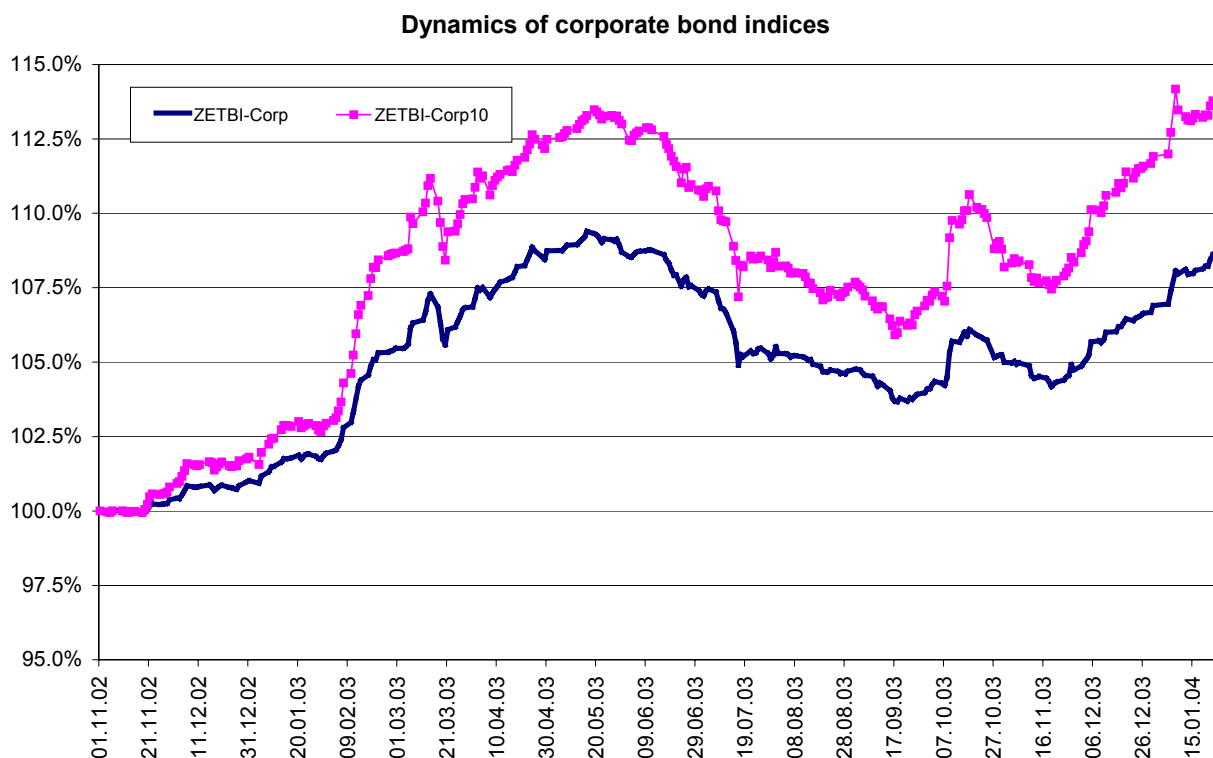


Fig. 5

The external factors of the behavior of the Russian stock market. Throughout January, prices at the world oil market continued to grow. Thus, during the period between the 30th of December 2003 and the 27th of January 2004, the price of Brent oil at the world market rose by 1.98 USD, or 6.79%. The market

⁷ The assessments were based on the indices of corporate bonds tradeable at the Moscow International Stock Exchange, as calculated by the bank "Zenith"

was favored by a number of factors including the low volume of oil reserves and reserves of oil products in the US, cold weather which determined the rise in demand for energy carriers, etc. Despite the fact that sometimes during the month oil prices exceeded 32 USD per barrel, official representatives of the OPEC are not planning any changes in the current policy pursued by the cartel in respect to oil quotas.

Dynamics of Brent Oil

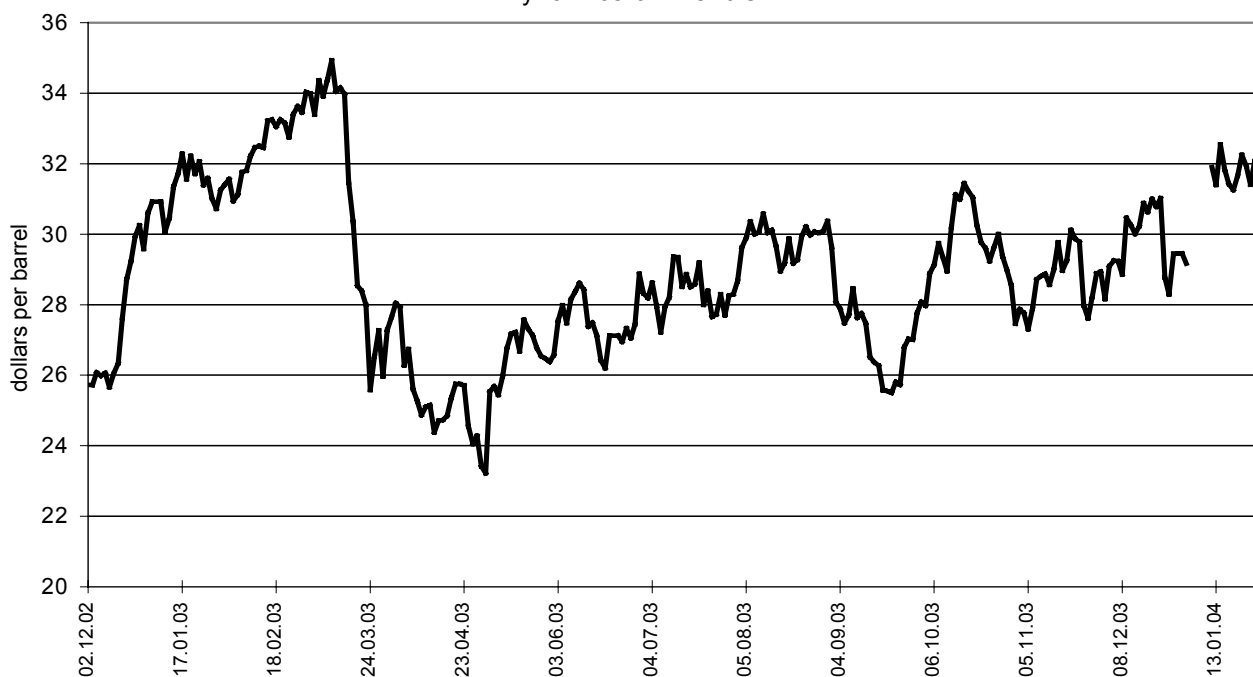


Fig. 6.

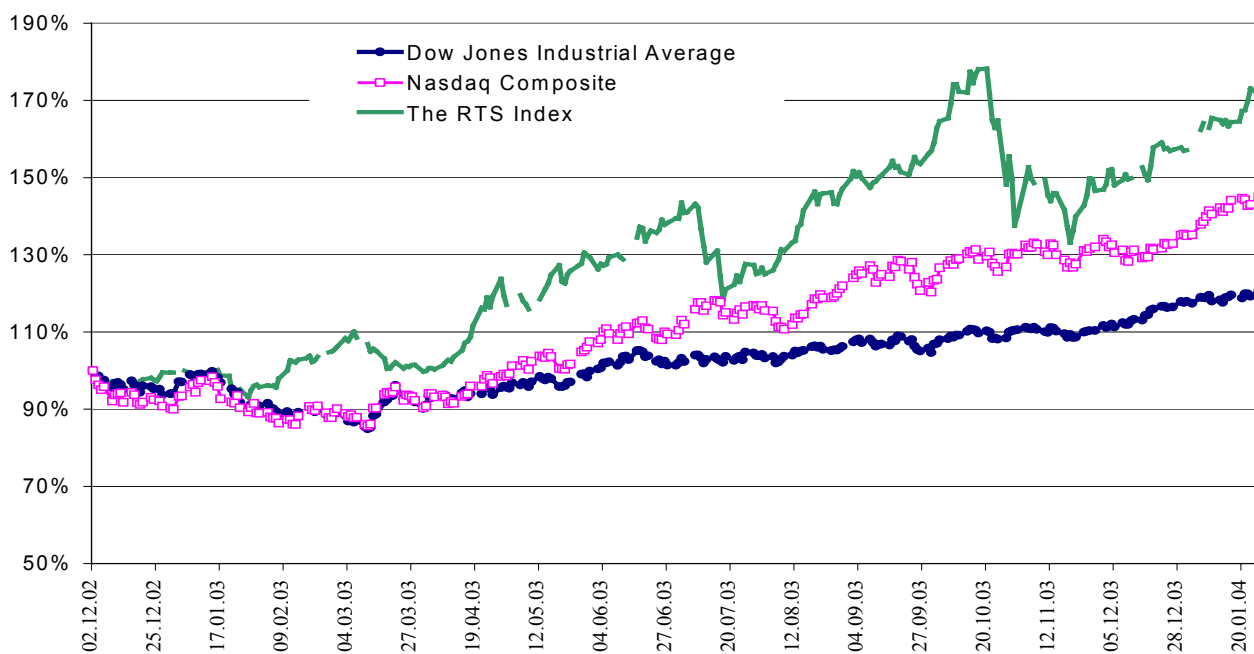


Fig. 7.

In January, the world stock markets were generally characterized by a rise in major stock exchange indices, which pointed to an improvement of the market situation. Thus, since the beginning of the year, the US stock exchange indices NASDAQ, and S&P500 have grown by 7.33% and 4.23%, respectively. A positive growth was also demonstrated by the DJIA index which has grown throughout the month by 2.81%. Practically all stock exchange indices of the European Union's member-countries have also demonstrated

positive rates of growth: DAX 30 (Germany) was up by 2.74%, CAC-40 (France) - by 2.19%. The only exception was FTSE 100 (UK) losing 1.43% by the results of the months. The stock exchange indices of Asian countries were also characterized, as regards the results of the month (year), by a positive behavior: Nikkei-225 (Japan) was up by 1.36%, Straits Times (Singapore) - by 6.06%. A positive trend continued to be prevalent in the behavior of the developing countries' markets, a testimony to which is the significant rise of the aggregated index of the MSCI agency throughout the period under consideration it has grown by 6.01%.

The behavior of the US stock market was mainly predetermined by the favorable news from the corporate sector; the majority of US corporations have published the results of their activity which in most cases were better than expected by the analysts. In general, the macroeconomic statistics were of positive nature. It should be specifically emphasized that at the beginning of the month there appeared the information on a certain growth of unemployment, which had a negative effect on the indices. However, the statistics published later pointed to the fact that the authorities had managed to check this process, thus verifying the improvement of the situation with unemployment.

As in the past, the behavior of the European stock markets generally reflected the situation at US markets. Nevertheless, it is the situation at the financial markets that has become one of the most significant factors determining the behavior of the Euro zone's markets; when the dollar was weakening, the shares of export-oriented European companies were falling in price thus exerting a downward pressure on the indices. And on the contrary, when the dollar was strengthening, their shares always responded by starting to grow in price. Also, a significant influence on the behavior of stock exchange indices was exerted by the results of the activity of telecommunication and high-tech companies, which in a number of cases, were better than expected.

In general, when analyzing the influence exerted by the world stock markets on the Russian stock market, it should be noted that this influence remains positive, though it has recently been weakened in respect to such factors as the rise of world oil prices and the strengthening of the rouble.

Corporate news

Open Joint-Stock Company "LUKoil"

In the middle of the month, the Company published the results of its activity for 9 months of the year 2003 (in accordance with US GAAP). Thus, according to the published data, the specific operating costs, despite inflation and the continuing strengthening of the rouble, remained at the level of the year 2002; for the first nine months of 2003 the costs amounted to 2.6 USD per barrel of oil. During the period under consideration there was a significant rise in the export of oil, which rose to the level of 27.7 million tons thus exceeding the figures for the previous year by 9%. Due to the growth of world oil prices and a greater demand for oil and petroleum products, the Company has managed to increase its sales proceeds by 46%, as compared to the same period of the year 2002. The net profit of "LUKoil" for the nine months of the year 2003 (including the aggregate effect of the changes in its accounting policy and the net income from the sale of the Company's share in the production sharing agreement "Azeri, Chigar, Guneshli") amounted to 3.06 million USD, or 1.718 million USD more than for the same period of the year 2002.

Open Joint-Stock Company "Noril'skii Nikel"

The extraordinary meeting of the company's shareholders, which took place on 29 December 2003, made a decision to set the size of interim dividends at 42.1 rouble per share. As proposed by the Board of Directors, the interim dividends should be paid by the results of performance for the nine months of the year 2003. The net amount of dividends on registered book-entry equities should amount to 9 billion roubles.

Open Joint-Stock Company "Slavneft"

The extraordinary meeting of shareholders of the Open Joint-Stock Company "NGK Slavneft" which took place on 24 December 2003 made a decision to set the size of the dividend on one common share at 78 kopecks in accordance with the results of the nine months of the year 2003. Therefore, the net amount of dividend payments would be 3.7 million roubles.

Table 1.

Behavior of world stock exchange indices

Data as of 26 January 2004	Value	Change during month (%)	Change from beginning of year (%)
RTS (Russia)	586.08	5.67%	5.67%
Dow Jones Industrial Average (USA)	10409.85	2.81%	2.81%
Nasdaq Composite (USA)	2006.68	7.33%	7.33%
S&P 500 (USA)	1155.37	4.23%	4.23%
FTSE 100 (UK)	4445.5	-1.43%	-1.43%
DAX-30 (Germany)	4128.68	2.74%	2.74%
CAC-40 (France)	3675.72	2.19%	2.19%
Swiss Market (Switzerland)	5748.5	2.97%	2.97%
Nikkei-225 (Japan)	10972.6	1.36%	1.36%
Bovespa (Brazil)	24350.0	8.49%	8.49%
IPC (Mexico)	9563.91	17.81%	17.81%
IPSA (Chile)	1438.92	-3.08%	-3.08%
Straits Times (Singapore)	1899.98	6.06%	6.06%
Seoul Composite (South Korea)	869.04	5.82%	5.82%
ISE National-100 (Turkey)	18356.54	-4.13%	-4.13%
Morgan Stanley Emerging Markets Free Index	469.768	6.01%	6.01%

The currency market. Throughout January, there was a continuation of rapid strengthening of the rouble against the dollar on the internal currency market. During the period between the 1st and the 27th of January, the US currency has become cheaper by 95 kopecks (-3.25%), dropping to 28.49 roubles per dollar. The most influential factor determining this behavior is the high oil prices at the world market; as a result, the volume of currency earning becomes high, and there emerges an excessive currency supply at the market. A favorable macroeconomic situation in the country also conduces to the strengthening of the rouble. Moreover, the downward trend in the behavior of the dollar is also predetermined by the situation at the world currency market where the dollar has been likewise losing strength of late.

The total volume of trade in US dollars in the SELT electronic trading system for the period from the 5th to the 23rd of January amounted to approximately 13 billion USD, which exceeded the figures for the first three weeks of December 2003 (9.97 billion USD) by approximately 4 billion USD. For the same period, the average daily turnover amounted to 929.45 billion USD, which also exceeded the figures for December (712.2 billion USD). The maximum volume of trade in US dollars achieved during this period was registered on 21 January when it slightly exceeded the amount of 2 billion USD (2.057 billion USD vs. 1.6 billion USD in December); while the minimum volume - 261.47 million USD was registered on 19 January.

In January, the liquidity of the rouble in the banking sector remained at a relatively high level: according to the data from 27 January, the balances of credit institutions' correspondent accounts with the Bank of Russia amounted to 228.7 billion roubles, or relatively less than at the end of December 2003 (288.3 billion roubles on 31 December), but more than the average figure for December (197 billion roubles).

Dynamics of the Official USD/RUR and EUR/RUR Exchange Rates in 2003-2004

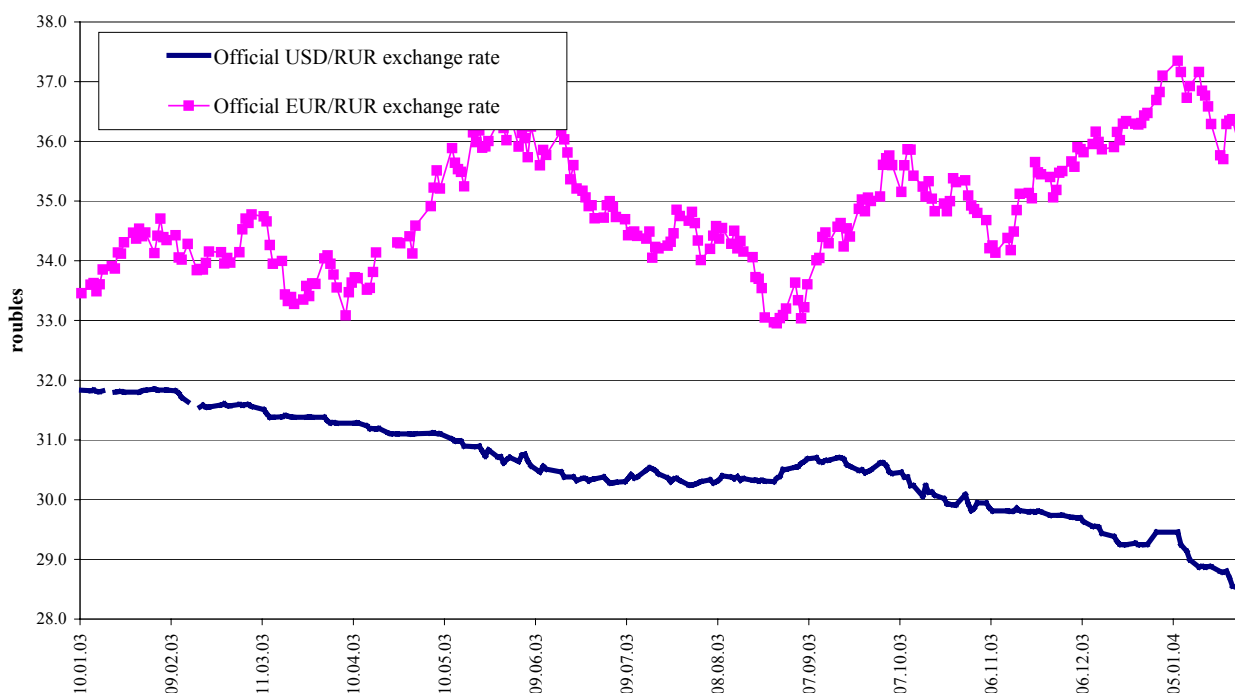


Fig. 8.

On the world currency market, by the results of the month, the dollar/euro exchange rate has remained practically unchanged - in the period between the 1st and the 27th of January the euro was traded at the level of 1.2539 USD/euro, or 0.4 cent below the figure at the end of the year 2003. Nevertheless, in the period under consideration the behavior of the exchange rate was characterized by high volatility. Thus, on 12 January the exchange rate reached a record height - 1.2833 USD for one euro. Then the market demonstrated a certain adjustment which took place against the background of a favorable influx of capital into the USA and a favorable balance of trade. Nevertheless, only a week later, the euro was traded for 1.2175 USD. During the following time-interval lasting until 27 January the euro was again gaining in strength, having reached the level observed at the beginning of the month. In general, the behavior of the euro / dollar exchange rate was determined by the current information on the situation in the US economy and the behavior of stock market indices. Also, the market responded to the remarks of high-ranking officials of the European Union in respect to the necessity to check the strengthening of the euro and to stabilize the currency market in order to sustain the economic growth in the countries of the Eurozone.

The behavior of the euro/rouble exchange rate was to a greater extent determined by the situation on the world market. A certain stabilization of this situation by the end of the month has resulted in the fact that in the period from the 1st to the 27th of January the euro/rouble exchange rate declined by 1.355 rouble (-3.65%). The total turnover of trading in euro in the SELT electronic trading system for the period from the 5th to the 23rd of January amounted to 108.56 million euro, thus exceeding the figures for December 2003 (91.7 million euro). The maximum volume of trade in the European currency for this period of time was registered on 14 January when it amounted to 12.708 million euro, while the minimum one - 1.89 million euro - was registered on 5 January.

Dynamics of the Dollar/Euro Exchange Rate on the International Markets



Fig. 9.

Table 2.

Indices of financial markets

Month	September	October	November	December	January*
monthly rate of inflation	0.3%	1.0%	1.0%	1.1%	2.3%
estimated, annual rate of inflation in accordance with the tendency in given month	3.66%	12.68%	12.68%	14.03%	31.37%
refinancing interest rate of RF CB	16%	16%	16%	16%	14%
average yield to maturity of OFZ, all issues (% per year)	6.15%	7.26%	6.74%	7.63%	6.5%
turnover of GKO-OFZ market for given month (bln. roubles)	12.87	14.60	5.02	20.58	30
yield to maturity of Minfin bonds by end of month (% per year):					
Tranche 5	5.68%	6.10%	5.99%	5.62%	5.3%
Tranche 6	4.26%	4.38%	4.36%	4.18%	3.8%
Tranche 7	6.55%	7.08%	7.09%	6.51%	6.1%
Tranche 8	4.96%	5.17%	5.09%	5.16%	4.4%
yield to maturity of eurobonds by end of month (% per year):					
2005	2.93%	3.22%	3.16%	3.05%	2.8%
2007	4.35%	4.65%	4.66%	4.42%	4.1%
2010	5.70%	5.98%	5.92%	5.80%	5.6%
2018	6.85%	7.26%	7.19%	6.97%	6.6%
2028	7.26%	7.57%	7.50%	7.34%	7.1%
2030	7.46%	7.75%	7.57%	7.28%	6.9%
MBK- MIACR rate (% per year by end of month) on credits for 1 day	22.0%	9.76%	7.75%	7.75%	1.5%
official rouble/USD exchange rate by end of month	30.6119	29.8584	29.7387	29.4545	28.50
official rouble/euro exchange rate by end of month	35.0751	34.8657	35.5021	36.8240	35.80

Month	September	October	November	December	January*
rise in official rouble /USD exchange rate during month (%)	0.36%	-2.46%	-0.40%	-0.96%	-3.24%
rise in official rouble / euro exchange rate during month (%)	5.65%	-0.60%	1.83%	3.72%	-2.78%
Turnover of stock market in RTS in given month (million USD for shares included in list for calculating RTS index)	490.78	867.33	374.55	416.89	430
value of RTS-1 index by the end of month	568.97	513.96	529.27	567.25	620
changes of RTS-1 index during given month (%)	7.15%	-9.67%	2.98%	7.18%	9.3%

* Estimates

D. Polevoi, P. Trunin

The real sector of the economy: factors and trends

In the year 2003, the growth of the GDP amounted to 7.0%, whereas that of investments in capital assets - to 12.5% and that of the gross output of industrial products - to 7.0%. The accelerated rise in investment demand exerted a considerable influence on the character of structural shifts in ultimate consumption and accumulation, as well as on the changes in the contributions made by the major branches of the economy and on the behavior of production of the GDP.

In the year 2003, while the growth of production in the export-oriented sector amounted to 7.7% in comparison with the results of the year 2002, the output of the investment complex rose by 8.9%. Despite the growing importance of the role played by the investment complex in accelerating the rate of industrial growth, the contribution of internal demand to the growth of output of Russian products in the year 2003 remained below the figures seen in 1999-2001. In the absence of any serious quantitative changes in the technology and structure of production, the complex of industries producing consumer goods was unable to maintain high rates of growth during a long period of time.

The period of 1999-2003 was characterized by a dynamic development of practically all sectors and branches of the economy. The economic growth was taking place against the background of a favorable external economic situation and internal socio-political stability. In the course of the last five years, the GDP increased by 37.1%, reaching in the year 2003 nearly 80% of the level achieved in 1990; its nadir was in the year 1998, when it fell to 57.7%. The scale of investments in capital assets as regards the economy in general increased nearly 1.55-fold, while ultimate consumption rose by 27.3%. The growth of investment demand exerted a significant influence on the character of structural shifts in ultimate consumption and accumulation, as well as on the changes of the influence exerted by the major branches of the economy on the behavior of production of the GDP.

Comparative analysis of the annual behavior of macroeconomic indices reveals rather significant fluctuations of rates from one sector to another. In 1999-2000, the average annual rate of growth of the GDP amounted to 8.5%, while in 2001-2002 it had declined to 4.3%. In 2003, the GDP rose by 7.0%, while the growth of investments in capital assets accelerated to 12.5%, and that of the output of industrial products - to 7.0%. According to the Ministry of Economic Development, nearly 60% of the GDP growth in the year 2003 was accounted for by internal factors - the increase of investments in capital assets and that of the incomes of the population, and only 30% were accounted for by the growth of the average annual price of Russian oil on the international market.

The economic upturn of 1999-2003 was taking place against the background of a simultaneous recovery of positive behavior both in the commodities-producing sector and in the services sector. The material-and-technical and labor potential created by the services sectors between the years 1999 and 1998 has all found its application at the market. The accelerated rate of production of commodities in the years 1999-2003 was supported by the infrastructure of the services market developed during the period of reforms. While in the last five years production of commodities grew by 44.3%, the volume of market services increased by 32.1%.

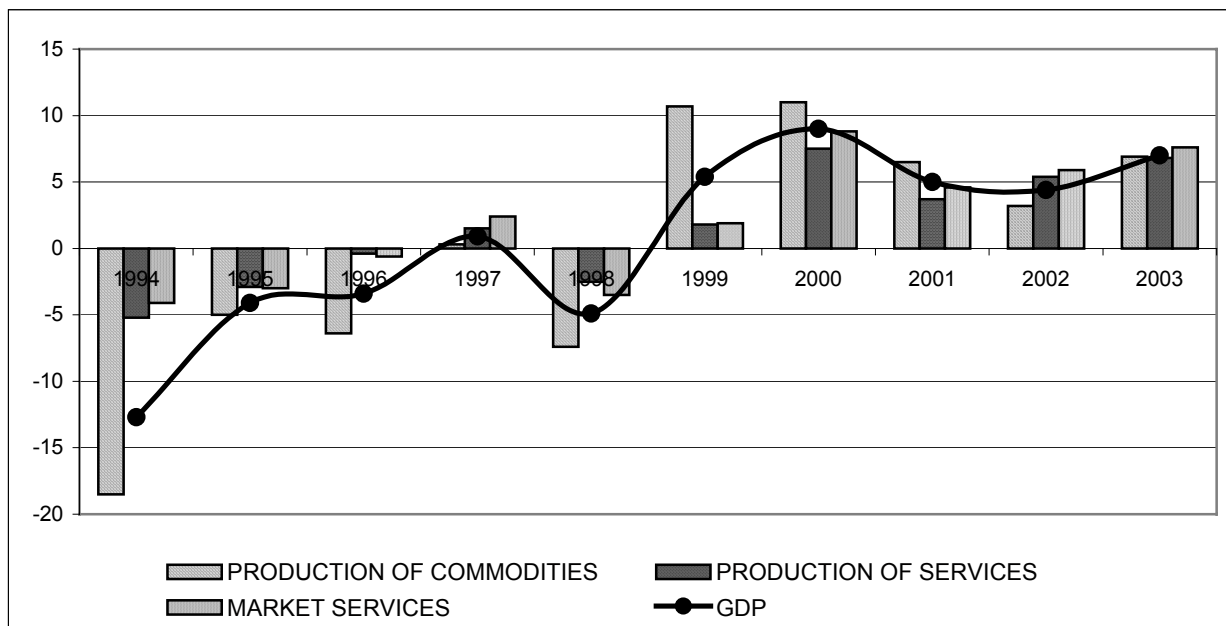


Figure 1. Sectoral changes in rate of production of commodities and services in period between 1994 and 2003, as a percentages of previous year

In the years 2002 and 2003, the Russian economy demonstrated a rise in the rate of growth of market services. With the increase of added value in the sector producing commodities by 6.9% observed in 2003, market services grew by 7.6%. The rise in the indices of the services sector closely corresponded to the level of business activity and the structural changes in the economy.

The growth of demand for industrial products both within the country and at the international level was accompanied by a widening of the scope of activity of the transport system. In comparison with the year 1998, the cargo turnover of the transport system has increased by 29.0%, while the volume of communication services has grown nearly 2.56-fold. After the volumes of retail trade had fallen in the years 1998-1999 by more than 10% in comparison with the year 1997, in the following four years, as the effective demand on the part of the population was gradually restored due to an active policy aimed at increasing the real earnings of the population, the turnover of retail trade grew at the rate outstripping that of the growth of the GDP. The index of retail-trade turnover in the year 2003 amounted to 145.1% of the level achieved in 1999, while the GDP rose by 28.9%.

In the year 2003, the transport system's commercial cargo turnover increased by 7.4%, while industrial output grew by 7.0%. The largest contribution to the growth of demand for services was made by the export-oriented branches. The increase in cargo turnover of pipeline transport amounted to 8.1% in comparison with January-November 2002, while the volume of transported oil rose by 12.3%, of petroleum products - by 8.6%, and that of gas - by 7.2%. The capacity for oil export was increased by the implementation of the second stage of the Baltic Pipeline System (capacity -18 million tons). In terms of the volumes of loaded cargo in the railway system, leadership belongs, as in the past, to oil and petroleum products, ores of ferrous and nonferrous metals and products of ferrous metallurgy.

Nowadays, communications represent one of the most promising and rapidly developing industries. The volume of gross added value of communications amounted, in the year 2003, to 241.9 billion roubles, or 1.8% of the GDP.

The growth rate of the volumes of communications services provided in the year 2003 amounted to 22.9%. Nearly 3/5 of the general volume of communication services and more than one half of the volume of communications services provided to the population is accounted for by the new operators. Telephone communication is the most widely used type of electric communication. It yields two thirds of all earnings gained by the industry through the provision of services, and one third of them is accounted for by mobile electric communication. As of 1 October 2003, the total number of users of mobile radio-link communication

amounted to 28.8 million. In January-September 2003, the increase in the number of users amounted to more than 11.1 million.

In the year 2003, the share of trade in the produced GDP amounted to 23.0%, which corresponds to the average index for the past five years. It should be noted that the development of this branch of the economy was accompanied by dynamic structural shifts. Firstly, the favorable situation on the international market has determined an accelerated growth and an increase in the share of external trade in the structure of trade turnover. Secondly, it is typical of the Russian economy that the volume of wholesale trade is nearly two times larger than the retail-trade turnover. With the increase of business activity, the intensive growth of wholesale trade is sustained by the expansion of the internal market's demand for material and technical resources. The index of growth of the retail-trade turnover amounted to 110.4% (as a percentage of the previous year), while its share in the GDP rose to 8,1% in comparison with 7.6% in the year 2000. There was an increase in the share of small business in respect to retail trade; in the year 2003, small enterprises accounted for 49.8% of retail-trade turnover, in comparison with 48.7% in the year 2001, and 46.1% in the year 2000.

In the years 1999-2003, the development of the Russian economy was taking place against the background of intensive growth of the industries oriented to the internal market. While the average annual growth rate of output in the raw-materials sector predominantly oriented to the external market was at the level of 105.4%, this rate in the investment complex amounted to 107.2%, and in the consumer complex it amounted to 106.5%.

In the year 2002, a decline in the growth rate was registered in the investment branches where it dropped to the level of 102.2%, significantly changing the structure of the internal market. The decrease in the growth rate of demand for construction materials on the part of mechanical engineering and the construction-materials producing industry determined more modest growth rates in the associated branches of the metallurgical and chemical & timber complexes. It should be pointed out that the narrowing of the demand at the internal market was not compensated by the expansion of production in the export-oriented sector - and therefore, it has ultimately resulted in a decrease in the growth rate in industry to the lowest level in five years.

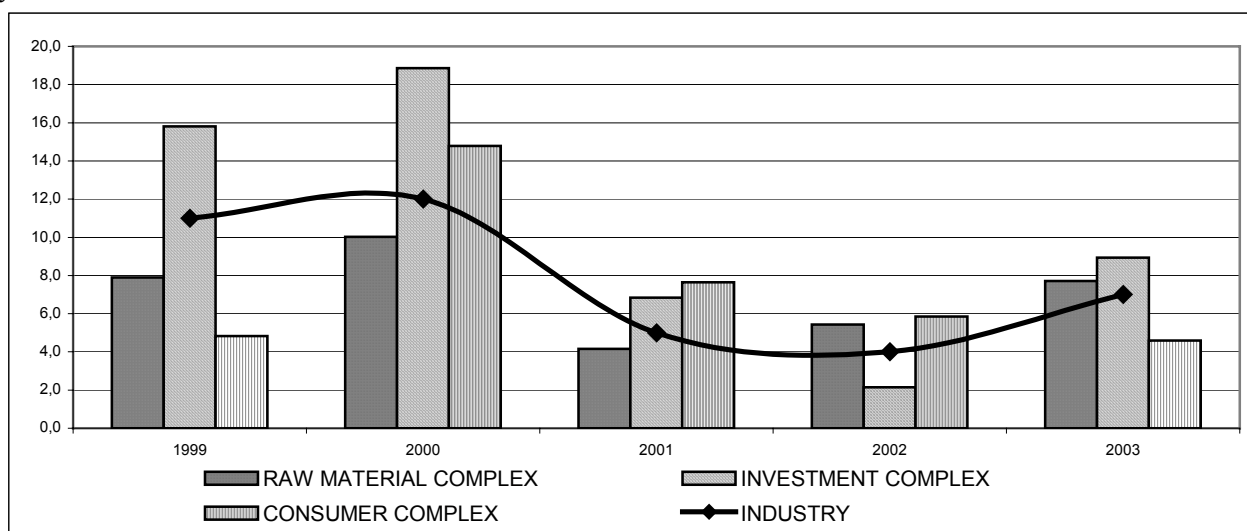


Figure 2. The growth rates in industrial and production complexes in 1999-2003, as a percentage of the previous year

In the year 2003, the situation radically changed. While production in the export-oriented sector grew approximately by 7.7% in comparison with the year 2002, the growth of output in the investment complex amounted to 8.9%, thus exceeding the level of the previous year by nearly 7.6 percentage points. Despite the increase in the importance of the investment complex in respect to acceleration of the industrial-growth rate, the share of internal demand for Russian products was lower in the year 2003 than in the years 1999-2001. It can be explained by the response of the branches of the consumer complex and, first of all, of the light industry to the changes in the exchange rate of the rouble and the increase in the efficiency of import

transactions. In the absence of any serious quantitative changes in the technology and the structure of production, the complex of industries producing consumer goods was unable to sustain high rates of growth during a long period of time. In the year 2003, the light industry was characterized by a continuation of the downward tendency in production, first registered in the previous year, and also by a decline of growth rate in the food industry. With the growth rate of the population's earnings accelerated in comparison with the general behavior of production in Russia, the consumer-goods market became more dependent on imports. This situation is not surprising: a slow rate of modernization and the lack of any sound strategy of development, which could get over the crisis in certain branches and complexes of the manufacturing industry have undoubtedly had a negative impact on the compatibility of domestic consumer goods and on the character of recovery-oriented growth of the Russian economy.

O.Izriadnova

The situation in industry in January 2004

The traditional January holidays have resulted in a sharp decline in sales and output in Russian industry, while the rate of decrease in profit has gone up. However, the forecasts of changes in the sphere of major indices (demand, output, employment) point to the possibility of a rather intensive industrial growth in the months to come. Analysis of the behavior of obstacles to production indicates an onset of the formation of a new structure of barriers to growth.

As it should have been expected, in January the volumes of sales of industrial products underwent a sharp seasonal decline. It overlapped with the negative tendency which had emerged as early as last September. As a result, the intensity of growth of effective demand has decreased in the course of the past six months by 45 balance points: from +19% (the best result for the whole post-default period) to -24% (the worst result for the whole post-default period). However, it should be remembered that in January 2003 the "drop" had been of the same magnitude. As a year ago, the volume of sales declined in all branches excepting electric-power engineering. Naturally, all these circumstances have resulted in a lower satisfaction with the volumes of demand. In January, the balance of assessments of demand went down, on the average in industry, by 7 points. The declines of such sharpness had never been observed in the previous years. Maybe, this phenomenon can be explained by the fact that in September - December 2003 enterprises still preserved a relatively high level of satisfaction with sales, despite the deceleration of their growth and their subsequent absolute reduction. The January seasonal drop in sales was the last straw - the assessments, after all, went down.

The sharp drop in sales has also resulted in the acceleration of the rate of profit decline. The balance of this index has fallen to -27% from -12% in December. A stable growth of profits has been registered in the last few months only in the sphere of electric-power engineering (+55 in January).

The two-months-long decline in demand forced the enterprises to reduce their volumes of production as well. In January, the balance, for the first time since January 2003, became negative - in industry, the responses stating the decline in output were now prevalent. But not to the extent observed a year ago. Then the balance (the difference between the responses stating the growth of output and those stating its decline) reached -18%, while now it is only -4%. As a year ago, the growth of output is preserved in electric-power engineering, non-ferrous metallurgy and the timber complex. Apart from these industries, in the year 2004 the January slump was avoided by mechanical engineering. The most intensive decline in production took place in the construction-materials-producing industry and in the food branch. The decline in production, though not so intensive as the decline in demand, made it possible for the enterprises to achieve a greater synchronization of the output and the sales in comparison with the previous month. In December 2003, the production behavior outstripped the sales behavior among 32% of enterprises, while now this can be seen in 27% of enterprises, which does not differ significantly from the average figures for the first 11 months of the year 2003 (25%). The largest numbers of enterprises whose output outstrips demand is registered in the light industry (34%), the timber complex (32%), and mechanical engineering (31%).

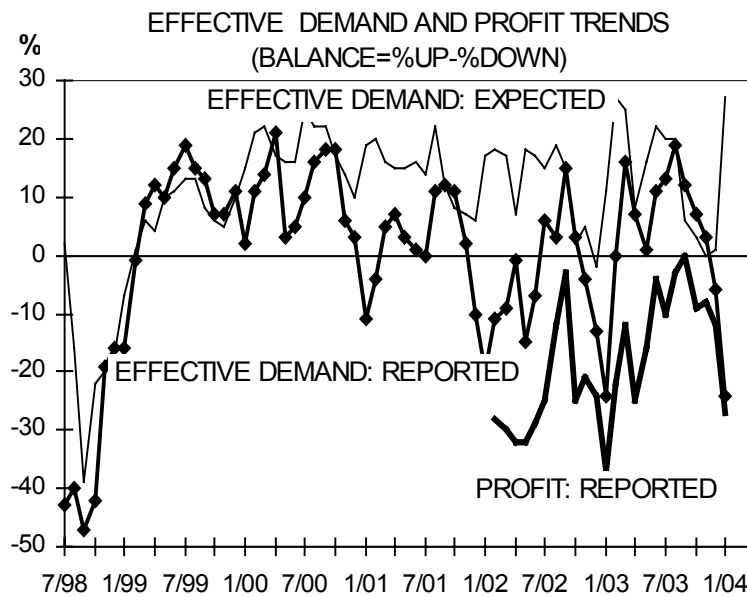


Fig. 1. CHANGES IN EFFECTIVE DEMAND AND PROFIT
(BALANCE = GROWTH - % DECLINE)

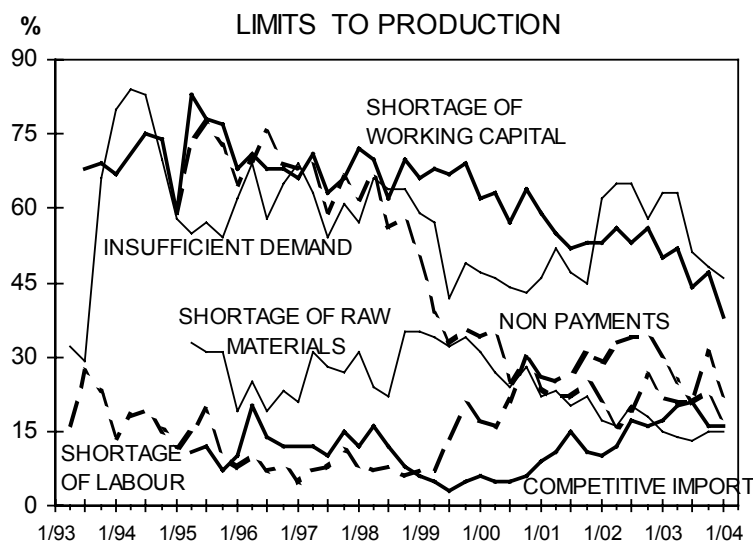


Fig. 2. OBSTACLES TO PRODUCTION GROWTH

At the beginning of 2004, polling revealed a clear reduction in the frequency of references to the factors impeding the growth of production in Russian industry. The leading factors - the lack of working capital and low demand - lost in January 9 and 2 points, respectively. Nonpayments, once one of the leaders, are troubling only 16% of all enterprises, “outstripped” by the lack of qualified personnel (22%) and low export demand (22%). Among the obstacles to production growth, the lack of raw materials, competition of imports and the lack of equipment are at the same level as nonpayments (15-16%). It looks as if Russian industry is acquiring a new structure of barriers to growth.

In January 2004, polling registered an intensive increase in the volumes of stocks of finished products. During one quarter, the balance has grown by 11 points, and reached the value of +6%. Such an intensive growth of the physical volume of stocks has not been observed since early 1996. In the pre-default period, the stocks had either been on the decrease, or had been growing with a minimal intensity (+1..+2%). Nowadays, the absolute growth of their volumes is registered in the chemical and petrochemical industries (+31%), the timber complex (+45%), the construction industry (+32%), and the light industry (+27%). In

other branches, the stocks continued to decline, but with a lesser intensity. Nevertheless, the negative (at first glance) tendencies have net resulted in overstocking of the stores. On the contrary, they have resulted in the increase in the share of enterprises with normal volumes of stocks to an unprecedentedly high level (62%). Such a high number of producers satisfied with the volume of their stock reserves have not been registered since March 1992. The balance of assessments of stocks (above-below the norm) remained in January practically unchanged. As a result, during the last three months, only a small surplus of stocks could have been spotted in industry, which is normal for the counties with developed market economies. Russian industrial enterprises are becoming more and more expert in finding a proper balance between demand and output.

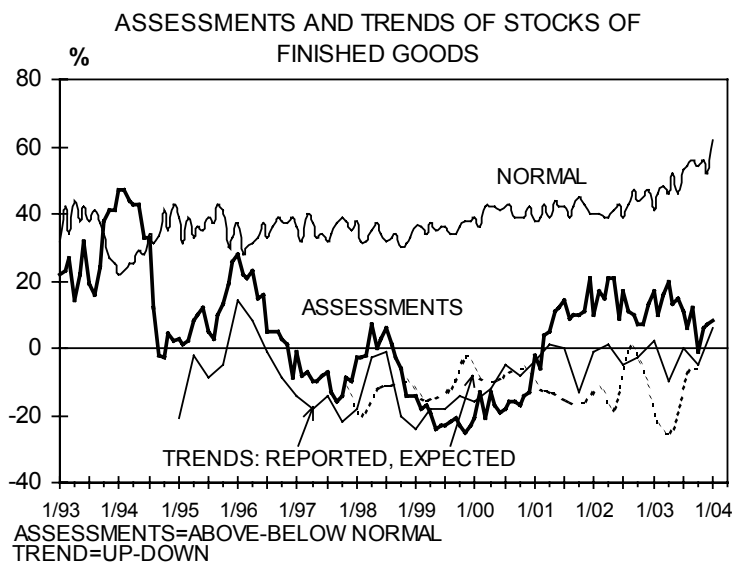


Fig. 3. BALANCES OF ASSESSMENTS AND CHANGES
OF STOCKS OF FINISHED PRODUCTS

The forecasts of changes in major indices (demand, output, employment) point to the possibility of a rather intensive industrial growth in the months immediately ahead.

Firstly, the balance of forecasts of effective demands have soared by 26 points in a very short period of time. It is only for the second time since March 1992 that such optimistic forecasts have been registered in Russian industry. Only 7% of enterprises are expecting the volume of sales of their products to fall in the nearest future. These enterprises are mainly concentrated in the food industry (15% of the total), the light, chemical, petrochemical and construction industries (9% in each industry).

Secondly, the balance of output forecasts has jumped up (the best possible expression) in one month by 32 points to +48 % at the present time. Neither such a significant change of the balance nor such a value of the latter has ever been registered since March 1992. Only 4% of enterprises, mainly in the electric-power engineering industry and in the food industry, are planning to reduce their output. The most intensive growth of production is possible in the chemical, petrochemical, mechanical engineering and construction industries.

Thirdly, the balance of employment forecasts has risen during the quarter by 10 points reaching the value of +8%. It is the best value of this index in the past three years. In the immediate months ahead, redundancies are possible only in electric-power engineering, nonferrous metallurgy, the food industry and the petrochemical branch.

S. Tsukhio

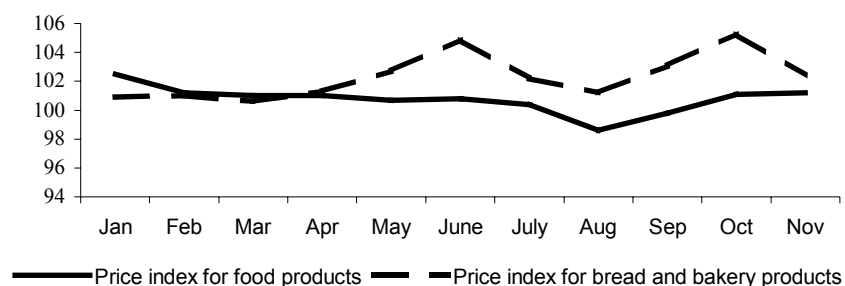
Russia: Export duties on grain

In compliance with Government Regulation No.749 of December 11, 2003 export duties on grain came into force in Russia beginning from January 2004. The Government decided to levy a temporary 25 EUR per ton duty on export of rye, wheat and their mix to countries not being members of the Customs Union. The

duty will be effective from January 1 till May 1, 2004. Its ad valorem ratio to the current domestic price for grain is about 15-20%.

Generally speaking export duties may pursue two goals – the fiscal and constraining ones. After 1994 export duties in Russia rarely serve as an export constraint mechanism. While in 1992 ad valorem export duties were imposed on all food products, in 1993-1995 they were effective only for wheat and corn (10-25%); in 1999 Russia limited export of oilseeds (the initial duty was 10% but not less than 15-20 ECU; afterwards it was lifted up to 20% but not less than 30-35 EUR). Throughout the transition period export of fish, fish products and alcohol was also subject to duties pursuing fiscal rather than constraining goal. In view of the above the current introduction of export duties on food grain is a novelty for Russian agricultural policies.

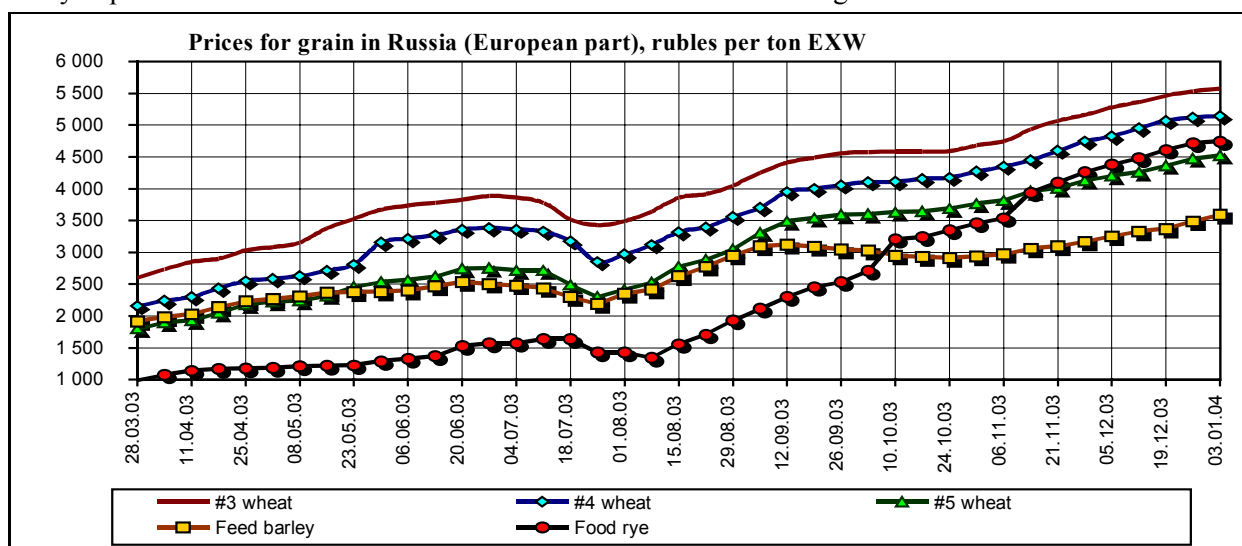
The declared basic reason for introducing this measure is the wish to constrain growth of domestic prices for bread due to poor grain crop in Russia in 2003/2004 season. Indeed, prices for bread in 2003 started to rise already in spring (Picture 1) and the harvest of grain was far below those of the two preceding years.



Source: RF State Committee for Statistics.

Fig. 1. Prices for bread and bakery products in 2003, as % of preceding month

Poor crop conditioned swift rise of grain prices (Picture 2) that in the previous bumper-crop year were heavily depressed and served as one of the causes of financial crisis in agriculture.



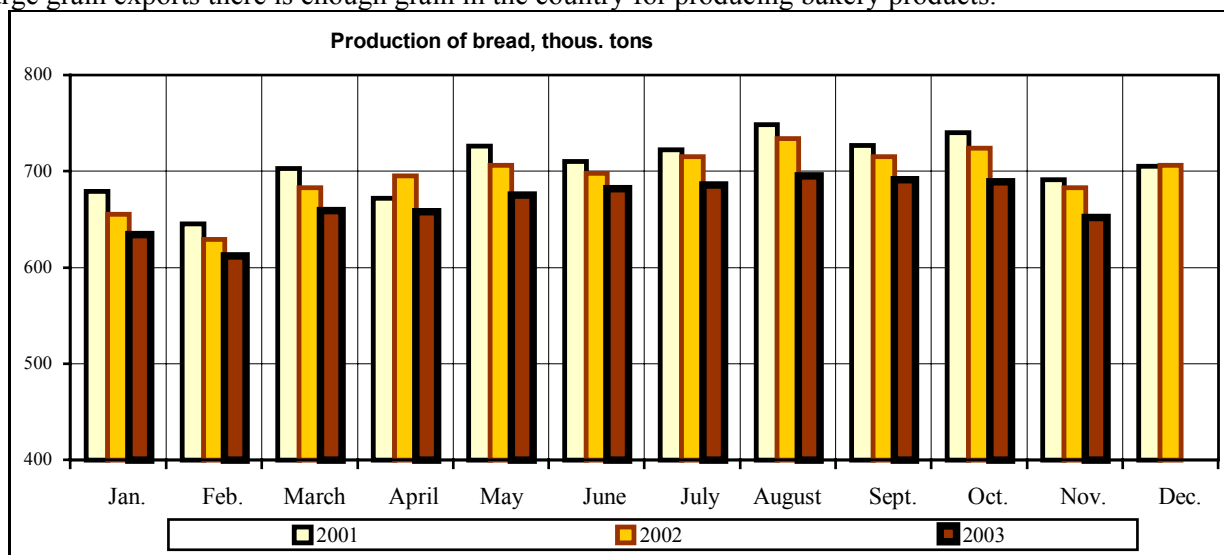
Source: Unidell group of companies.

Fig. 2. Prices for grain in Russia

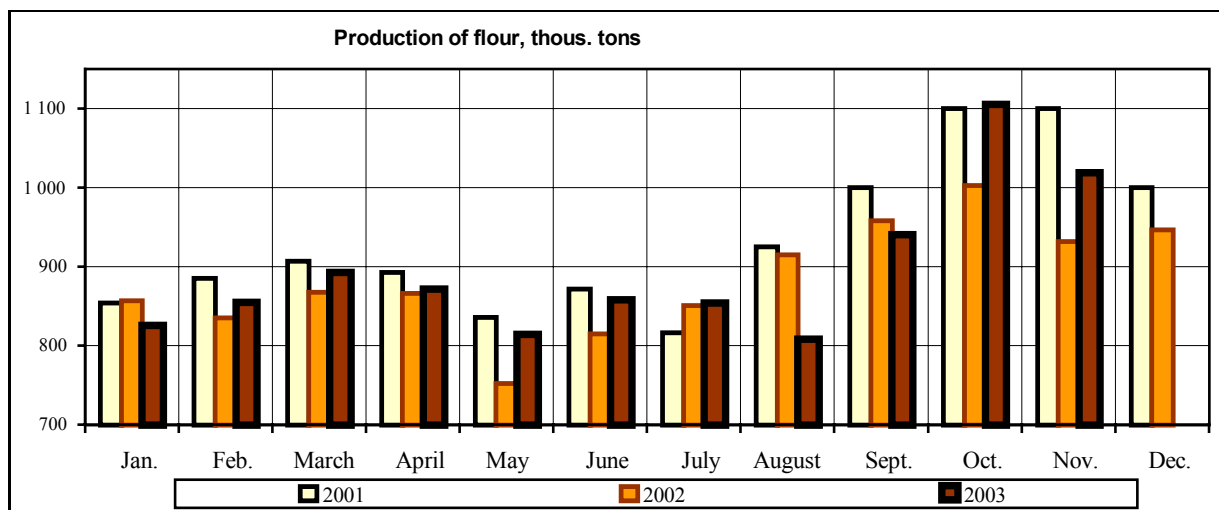
On the other hand the steady growth of real personal incomes beginning from 1998 resulted in smaller demand for bread, production of which reduces year after year (Picture 3). During the reform years prices for bread haven't been liberalized completely: first the federal government and later authorities in almost all regions continued to control rise of prices for this product being of particular social importance. As a result the spread between lower indices of price for bread and higher overall food price indices was growing. At

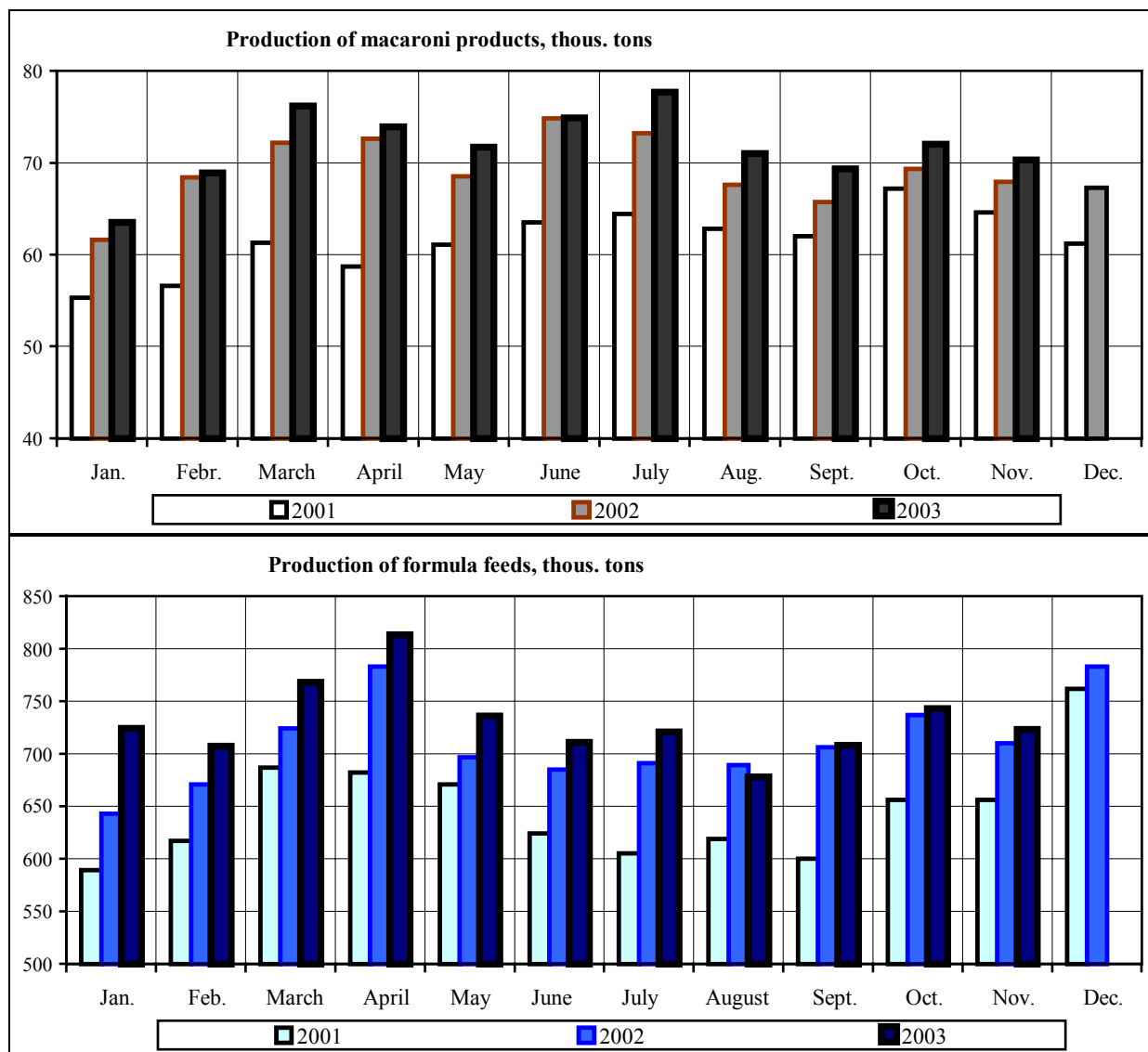
some moment this distortion had to be eliminated by a bounce, i.e. faster growth of price for bread. Indeed, beginning from 1999 retail prices for bread and bakery products steadily grew at a higher rate as compared with prices for food in general but then it hasn't resulted in their drastic upsurge due to, first, the strengthening of state regulation on the regional level after poor 1998 crop, and, later, to two successive years of abundant crop (2001 and 2002) that pulled grain prices down. Probably, it was just the combination of poor grain crop and smaller bread production in 2003 that made formerly lagging behind bread prices to soar.

This conclusion is supported by the fact that production of all other grain products (except bread) demonstrates quite a steady growth in recent years including 2003. In other words, in spite of poor crop and large grain exports there is enough grain in the country for producing bakery products.



Picture 3. Production of basic grain products in Russia in 2001-2003





Source: Unidell group of companies.

In view of the above export duties on food grain will hardly stop the rise of prices for bread since its causes are other than poor supply of grain.

At the same time higher prices (now including duties) are undermining grain export opportunities. Definitely, given the current domestic prices for grain its export becomes less attractive for exporters. Export of food grain started to shrink even before the government interference⁸. On the other hand, large traders are motivated not only by prices but also by the wish to preserve their image making them to remain on the world market even if price situation deteriorates. Besides, the introduction of export duties was announced only half a month before their enforcement and thus traders had no time to cancel contracts and will have to meet them despite the duty. This will lower the profitability of export transactions.

Summing up, the introduction of grain export duties fails to achieve its goal but can notably undermine positions of Russian grain traders on the world market that strengthened markedly in 2002/2003. These traders launched large investment projects aimed at creation of export port infrastructure and got support of the government that allocated funds from the federal budget to subsidize interest on credits for construction of port grain loading facilities⁹. Most likely this measure will have purely populist effect that is not surprising in a year of elections.

E.Serova, I.Khramova

⁸ It's noteworthy that rumors about the introduction of export duties, on the contrary, fostered grain export in last months 2003.

⁹ Supplement № 36 to Federal Law "On 2003 federal budget".

External trade

In November, 2003, the favorable conditions for the development of Russia's foreign trade remained as before. The situation on the world market was promoting export growth, while the consolidation of the rouble and real incomes growth had resulted in an expansion of import supplies.

A serious obstacle in the way of further export growth has been the limited access of Russian commodities to some foreign markets. In January 2004, China imposed anti-dumping duties on imported cold-rolled steel for suppliers from Russia and a number of other countries. The losses of the Russian steel suppliers on the Chinese market may become as high as \$ 80 million.

Russia's external trade turnover, as calculated by the balance-of-payment-method, in November, 2003 grew, in comparison with the same period of the previous year, by 22% - to \$18.3 billion. However, when compared to October 2003, a certain decrease in both export and import supplies could be seen, as a result of which the November volume of commodities turnover went down, as compared to the preceding month, by 6.6%.

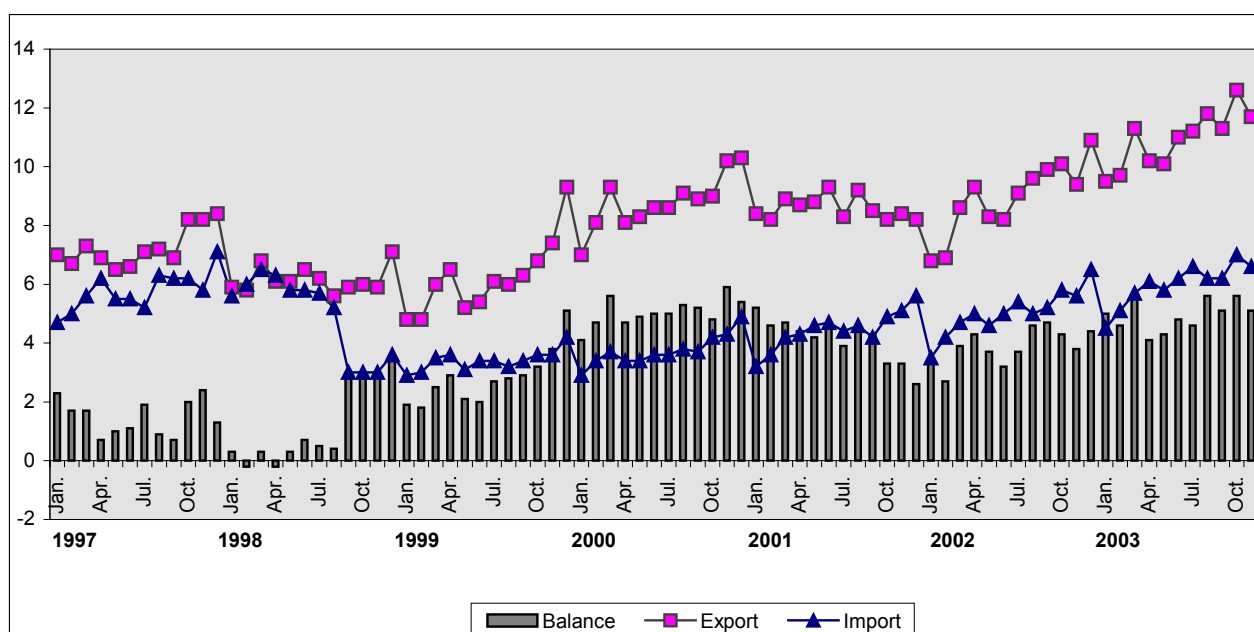


Fig. 1. Basic indices of Russia's foreign trade (billion USD)

Source: RF Goskomstat

The commodities export in November 2003 became as high as 11.7 billion USD, having exceeded the level of the same month of the year 2002 by 26.6%. The basic indices of Russian export were forming under the conditions of a maintained favorable situation on the world market.

In November 2003, the international oil market saw a certain negligible fall in prices. The average price of Urals oil was 27.5 USD per barrel (a decrease by 2.5%, as compared to October of the same year), of Brent oil – by 28.8 USD per barrel (a decrease by 2.7%). As seen by the results of eleven months of the year 2003, the average price of Urals oil was higher than that during the same period of the year 2002 by 16.8%, and of Brent oil – by 17.5%. The high enough level of prices was due to the growing demand for oil (primarily, on the Asian market), as well as to the low reserves of liquid fuel in the OESD countries.

From February 1, 2004 the rate of import duty on crude oil was set at 33.9 USD per ton. The rate of import duty on liquid fuels, medium distillates, light distillates and oil products was set at 30.5 USD per ton. The rate of duty on crude oil products extracted from bituminous deposits now is 33.9 USD per ton. Until now, the rate of export duty on oil has been 31.2 USD per ton, on oil products – 28.1 USD per ton.

The prices on Russian natural gas have remained high. The average contractual price during November 2003 grew, as compared to October of the current year, by 0.7%.

The prices on the ferrous-metals market have become stabilized. The European average monthly export prices of the basic types of graded and lamellar rolled-steel stock in November 2003 remained at the October level.

The revival of the global economy had promoted further growth of prices on the world non-ferrous-metals market. In November, as compared to October 2003, the average prices of aluminum increased by 2.2%, of copper – by 7.1%, of nickel – by 9.6%. During eleven months of the year 2003, the average price of nickel grew, as compared to the same period of the previous year, by 37.2%, of copper – by 12%, of aluminum – by 5.5%.

Table 1.

Average world monthly price in November of each year under study

	1996	1997	1998	1999	2000	2001	2002	2003
Oil (Brent), USD/barrel	22.8	17.8	11.5	24.1	25.6	19.35	24.4	28.8
Natural gas, USD /1 mln. BTU	3.093	2.393	2.251	2.558	5.767	2.843	4.11	4.876
Petroleum, USD /gallon	0.6691	0.5648	0.3739	0.6986	0.7649	0.5454	0.7203	0.845
Copper, USD / ton	2273.3	1834.7	1601.6	1748.1	1914.4	1481.0	1610.0	2052.0
Aluminum, USD / ton	1459.9	1535.5	1305.0	1470.7	1562.5	1326.6	1373.4	1507.0
Nickel, USD / ton	6920.0	6099.0	4202.0	7984.2	7315.4	5159.7	7316.7	12090.0

Source: calculated by the data of the London Metals Exchange and the International Oil Exchange (London)

Any further growth of the rates of Russia's export is suppressed by the actual scope of external demand and the traffic capacity of transport channels. Also, a serious obstacle to export growth has been the limited access of the Russian commodities to foreign markets. Presently, there exist 93 restrictions on these commodities, which results in losses for this country's exporters in the amount of about 2 billion USD. The greatest number of restrictions were imposed by the European Union. The potential losses of the Russian economy that could result from the expansion of the EU may become as high as 150 million USD. This will be due to the introduction of higher import duties and applying anti-dumping measures to the Russian manufacturers by the EU members.

From 14 January, 2004 China has imposed anti-dumping duties on imported cold-rolled steel for suppliers from Russia, Ukraine, Kazakhstan, South Korea and Taiwan. The duty rates are 29%, 49%, 48%, 40% and 55%, respectively. The new rates are for the term of five years. Previously, China did not apply anti-dumping duties to rolled steel, because the supplies of this commodity were being regulated by means of quotas. In November, China took an unprecedented step and lifted all restrictions on steel import. However, quotas were soon replaced by anti-dumping duties. The losses of Magnitogorsk metallurgic combine and other suppliers of steel to the Chinese market may become as high as 80 million USD.

In November 2003, the Russian import of commodities was also characterized by high growth rates and amounted to 6.6 billion USD, having exceeded by 15% the level of the same period of the year 2002. This import growth was due mainly to the increased physical shipment volumes. The high import growth rates were due primarily to the growth of the population's incomes and the incomes of enterprises, as well as to consolidation of the rouble.

During January-through-November, the real strengthening of the rouble-to-USD exchange rate, as estimated by the Ministry of Economic Development, was 16.1%, and the real effective exchange rate of the rouble (as estimated by the "currency basket") grew by 5.1%. The negative impact of the rouble's consolidation on the competitive capacity of the Russian commodities, as compared to that of imported commodities, has been somewhat softened by the relatively more favorable changes in the rouble-to-euro rate – the real strengthening of the rouble-to-euro exchange rate during the eleven months amounted to about 1.1% (while the euro zone is the source of approximately one-third of total import to Russia).

The share of import within the structure of retail trade's commodities resources has also been growing. In Quarter III of 2003 it went up by 1 percent point, as compared to the same period of 2002, having amounted to 43%.

However, in January-through-November of 2003, the meat import volumes from the far abroad went down, as compared to the same period of the previous year. According to the SCC's information, the shipments of poultry amounted to 998,100 tons, or by 20.4% less than in eleven months of the year 2002.

The import of other kinds of meat was reduced by 15.6%, or to 743,800 tons. The reduction in shipments was due to Russia last year having introduced quotas on the import of beef, pork and poultry.

The shipments of canned meat were also decreased (by 24.1%), as well as those of sunflower oil (by 35.6%) and raw sugar (by 17.1%).

It should be remembered that from January 1, 2004 a new regulating regime for the import to Russia of raw sugar was introduced, based on the exchange price of this commodity. The duty rate is to be calculated on the basis of monitoring the prices of raw sugar of the New York Commodity Exchange. In January 2004, the import duty rate on raw sugar was 235 USD per ton. In February, the import duty rate on raw sugar is expected to be 250 USD per ton.

In November 2003, the two-way turnover between Russia and the CIS amounted to 3.30 billion USD. Russia maintained an active balance of trade in the amount of 0.52 billion USD. In contrast to the preceding months, in November 2003, as compared to November 2002, import growth was greater (by 27.2%) than export (the increment being 25.8%).

In January this year, an International Conference of Heads of Customs Services of the European Region of the World Customs Organization is to take place in Moscow, where the role of the customs services as a factor of economic growth will be discussed, as well as priority areas of customs regulation in Russia which have been given an impetus to develop after the new Customs Code was enacted from 1 January of this year.

In the sphere of customs regulation, the SCC of Russia has suggested that this year quotas should be introduced for the import to Russia of sugar from the CIS, in particular from Belarus and Kazakhstan. The introduction of quotas is not expected to result in lower volumes of planned shipments – its purpose is to control the level of sugar smuggling.

Besides, in connection with the growing illegal import of meat products from the CIS, in excess of the existing quotas, the RF SCC's Resolution of 16.12.2003 was enacted, concerning the organization of the discharge to shelters for customs inspection of the meat products shipped from neighboring regions.

From 1 January, 2004 the new RF Customs Code was enacted. During the first few weeks of operation under the new Code it has already become obvious that the customs-associated business in Russia has undergone substantial changes. The number of brokers went down more than twofold, that of shelters – by more than threefold, and that of customs carriers – by one-and-a-half times. Small-scale agents, which are unable to provide guarantees against their liabilities amounting to between 20 million roubles and 50 million roubles, are being ousted from the market. As of today, 30 large-scale brokers control already almost as much as 70% of total import in Moscow and in Moscow Oblast.

The number of regional shelters and broker companies went down by an order of ten. In some Russia's oblasts, the entire customs-associated business went into shadow. The former customs brokers whose license has expired are being hired by importer companies as consultants and advisers, while the former customs carriers are being merged with importer companies as transport-and-supply divisions. However, only large-scale participants of foreign economic activity can afford to keep the entire customs administrations. Small businesses whose monthly export-import turnover does not exceed the amount of 100,000 USD, are forced to make a choice of either being serviced by large customs entities (which would double or triple the cost of customs clearance) or directing all commodities flows through the so-called "gray schemes".

N.Volovik, N.Leonova

Mandatory medical insurance

January 2004 saw an important step forward in implementing the long-awaited modernization of the mandatory medical insurance system (MMI). The RF Government discussed this issue at the meeting on 15 January 2004 and approved the proposals of the Ministry of Economic Development of Russia concerning the reform of the MMI and the draft federal law "On mandatory medical insurance in the Russian Federation".

It should be reminded that the MMI system was initially introduced in this country in the first half of the 1990s; however, the planned reform of financing the health care system was implemented only partially and incompletely. The replacement of budgetary funding of medical organization by insurance funding has not been completed. The regional and local government agencies were not transferring sufficient amounts of funds to finance the MMI for non-working population. The MMI system concentrates within itself only one-third of state financing of health care, while about two-thirds is needed. This is the result of the lack of efficient regulation of the amounts of contributions to finance the MMI for non-working population.

Therefore the funds accumulated within the MMI system are enough only to cover a part of the cost of rendering medical care under the MMI program.

The insurance-based principles of organizing the financing of medical care provided to the population, in fact, found no place in the system of financing which is actually functioning under the name of mandatory medical insurance.

The patient care and prevention institutions receive funding for carrying out one and the same activity simultaneously from two sources: from the budget, in the form of allocations for the upkeep of the institutions in accordance with an estimate of revenues and expenses, and from the MMI system, in the form of payments for the medical care provided to insured persons. The budgetary funds are used to cover all expenditure items of an institution. The MMI funds are intended to cover the cost of wages, purchases of medications, small equipment, patients' nutrition. As a result, there exist two separate sources and two mechanisms of financing the activity of medical institutions, thus reproducing the cost-led mechanism of economic activity in health care system.

The existing MMI system provides no stimuli for its subjects to improve the efficiency of their functioning. The medical insurance organizations are assigned the role of a mere intermediary in the movement of financial resources. Insured persons have little opportunity to influence the insurers in any way. There is no adequate regulation of the choice of the method of payment to medical institutions.

Among the drawbacks of the existing system of health care financing is the existence of substantial discrepancies between the RF's subjects in the levels of financial backing for the state guarantees of medical services to be rendered to the population: there is a 14-fold difference between the highest and the lowest amounts of per capita state financing of the health care system. The MMI system has a mechanism for equalizing the levels of financial backing for the territorial MMI programs: a part of the social tax allocated to the MMI is concentrated in the Federal MMI Fund. However, this amount is too small to provide a solution to the problem in question: the base rate being equal to 3.6% of the wages fund, the centralized component constitutes 0.2 percent points.

The task of reforming the MMI system was envisaged in "The Main Directions of the Socio-Economic Policy of the Government of the Russian Federation in the Long-Term Perspective" approved by the Government of the Russian Federation on 28 June 2000. Initially, it was intended to achieve this task by means of transforming the systems of mandatory medical insurance and social insurance into a unified medico-social insurance system. In 2002 the idea of such a unification was abandoned, and it was decided to reform the MMI system as a separate entity.

The leading role in elaborating the concept of the reform and the draft law on mandatory medical insurance has been assigned to the Ministry of Economic Development of Russia. Also, the RF Pension Fund is very active in this sphere, and on its initiative in the year 2003 a pilot project was started in 13 RF subjects, under which the Fund was to co-finance the contributions designed to cover the MMI for non-working population.

The problem associated with the absence of any distinct rules for determining the amount of these contributions has turned out to be too complicated to be solved under the conditions of a federal state. Imposing on the RF subjects the obligation to pay from their budgets certain clearly defined amounts to finance the MMI for non-working population contradicts the contemporary understanding of the principles of federalism. This is regarded as the Federation imposing additional liabilities on its subjects, which must be substantiated by adequate sources of financing from the federal budget. However, the capacity of the federal budget is sufficient only to cover a smaller part on the actually needed contributions, and not to provide full coverage of all expenditures. The time-consuming analysis of possible variants, and the need to coordinate the standpoints regarding this key issue, has become the principal factor responsible for such a long delay in the preparation of the new draft law.

As a result, the mechanism that envisages making agreements between the RF Ministry of Finance, the RF Ministry Public Health Care, the Federal MMI Fund, the Pension Fund, the executive power agencies of the RF subjects, and the Territorial MMI Funds concerning the insurance of non-working population was selected. The subject of the agreements will constitute the mutual obligations of each of the parties to co-finance the payments on behalf of non-working population to be transferred to the Territorial MMI Funds. The federal budget will allocate appropriate funds to back such co-financing.

Those RF subjects who have not signed such an agreement will on their own determine the procedure of insuring non-working population and of rendering and paying for the medical care envisaged in a territorial MMI program.

The draft law approved by the RF Government also stipulates the following transformations to be carried out within the MMI system:

- elimination of the local budgets as the sources of financing the MMI payments on behalf of non-working population and effecting the payments to cover MMI services for non-working population only from the budgets of the Russian Federation's subjects;
- preservation of medical insurance organizations as insurers within the MMI system, with substantial toughening of the state requirements to their activity;
- granting to insured persons the right to select an insurer;
- unification of the mechanisms of price-making and payment for medical care within the MMI system.

A very significant role within the modernized MMI system is assigned to the RF Pension Fund. The Fund will keep records of all the persons insured within the MMI system, participate in multilateral agreements, and collect and verify the information needed to control the individual client accounts of insured persons.

It is intended to gradually concentrate within the Federal MMI Fund the greater bulk of the MMI funds, by means of changing the proportional distribution of the funds generated by the social tax payments between the Federal MMI Fund and the territorial MMI funds, thus augmenting the capacity of the Federal MMI Fund to equalize the financial backing for the implementation of the basic MMI program in different region.

Regretfully, the draft law did not reflect the widely discussed proposals concerning the possibility to voluntarily leave the MMI system, on the condition of making an agreement on voluntary medical insurance, and to use a part of the MMI payments to cover the contributions paid under the agreement on voluntary insurance.

Generally, the draft law offers acceptable solutions to the problems faced by the existing MMI system. The enactment of the new law will make it possible to effect a transition to a system that envisages one unified payer for the medical services rendered to citizens at the public expense, that is, to concentrate the main bulk of the budgetary funds in the MMI funds in the form of payments made on behalf of non-working citizens, as well as to make the transition toward paying for the services rendered by medical institutions on the basis of full tariffs that will cover the whole cost of medical care. All this will lay the foundation for achieving an adequate balance of financial liabilities within the MMI system and improving the efficiency of medical care provided to the population.

The RF Ministry of Economic Development by mid-February must revise and refine the draft law, with regard to the previous discussion, after which the draft will be submitted to the State Duma.

S.V. Shishkin

A forecast of some macroeconomic indices¹⁰

This section contains the results of forecasts of monthly indices of population's living standards, the indices of the population employed in the economy, and the indices of overall unemployment, plotted on the basis of time series models ARIMA(p, d, q). It should be noted that from November 2003 onward the IET has been issuing a monthly bulletin of modeled short-term forecasts of socio-economic indices of the RF (see www.iet.ru).

Changes in prices

This section presents the modeled forecasts of consumer price index and manufacturing price indices (of industry as a whole, as well as of some sectors) calculated on the basis of time series model based on the data

¹⁰ In this instance, a forecasted value is understood as an estimated future value of a given index obtained on the basis of a certain model with the best statistical properties. For more details on time series models, see: Entov R.M., Drobyshevskii V.P., Nosko S.M., Yudin A.D. (2001), *Ekonomicheskie analizy dinamicheskikh riadov osnovnykh makroekonomicheskikh pokazatelei (Econometric Analysis of Dynamic Series of Basic Macroeconomic Indices)*, Moscow, IET; R.M. Entov P.M.ЭНТОВ, V.P. Nosko, A.D. Yudin, P.A.Kadochnikov, S.S.Ponomarenko (2002), *Problemy prognozirovaniia nekotorykh makroekonomicheskikh pokazatelei (The Problems of Forecasting Some Macroeconomic Indices)*, Moscow, IET; Nosko, A. Buzayev, P. Kadochnikov, S.Ponomarenko (2003), *Analiz prognoznykh svoistv strukturnykh modelei i modelei s vklucheniem rezultatov oprosov predpriatii (An Analysis of Prognostic Properties of Structural Models and Models Including the Results of Polling Enterprises)*, Moscow, IET

of the RF Goskomstat in the interval from November 1998 through November 2003. Table 1 shows the resulting modeled forecasts of February, March and April indices of 2004.

Table 1

Resulting forecasts of price indices											
Month	Consumer price index	Manufacturing price indices:									
		Whole industry	Electric-power engineering	Fuel industry	Ferrous metallurgy	Non-ferrous metallurgy	Chemical industry	Petrochemical industry	Machine-building and metal-works	Light industry	Foodstuff industry
Forecasted indices, ARIMA models (as % of preceding month index)											
February 2004	101.5	101.0	102.0	100.9	101.6	102.9	102.4	101.3	101.0	100.6	100.8
March 2004	101.1	100.6	101.8	99.8	101.0	102.4	101.9	101.6	101.3	101.0	101.1
April 2004	101.0	100.2	101.6	99.9	101.3	94.1	103.0	101.8	101.3	101.4	101.2
Forecasted indices, ARIMA models (as % of December 2003 index)											
February 2004	103.1	102.2	104.4	103.6	103.5	102.0	105.0	102.8	102.1	101.8	101.9
March 2004	104.2	102.8	106.3	103.4	104.5	104.4	107.0	104.5	103.4	102.9	103.0
April 2004	105.2	103.1	108.0	103.2	105.9	98.3	110.2	106.4	104.7	104.3	104.3
Reference: actual indices of same periods of year 2003 (as % of December 2002 index)											
February 2003	104.0	101.8	106.7	96.5	105.1	103.9	103.0	101.2	101.9	102.7	101.6
March 2003	105.2	103.1	112.1	96.7	108.7	104.8	103.2	101.9	102.5	103.2	102.0
April 2003	106.2	104.6	112.5	95.2	115.2	111.9	104.9	103.3	103.8	104.9	102.5

The forecasted average monthly inflation rate in February through April 2004 is 1.2%. Thus, the inflation rate in the period of January through April is expected to be 5.2%.

The forecasted growth rates of manufacturing prices during the same period are as follows: 0.6% per month in industry as a whole, 1.8% per month in electric-power engineering, 0.2% per month in fuel industry, 1.3% per month in ferrous metallurgy, -0.2% per month in non-ferrous metallurgy, 2.4% per month in chemical industry, 1.6% per month in petrochemical industry, 1.2% per month in machine-building and metal-works, and 1% per month in light and foodstuff industries.

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