

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
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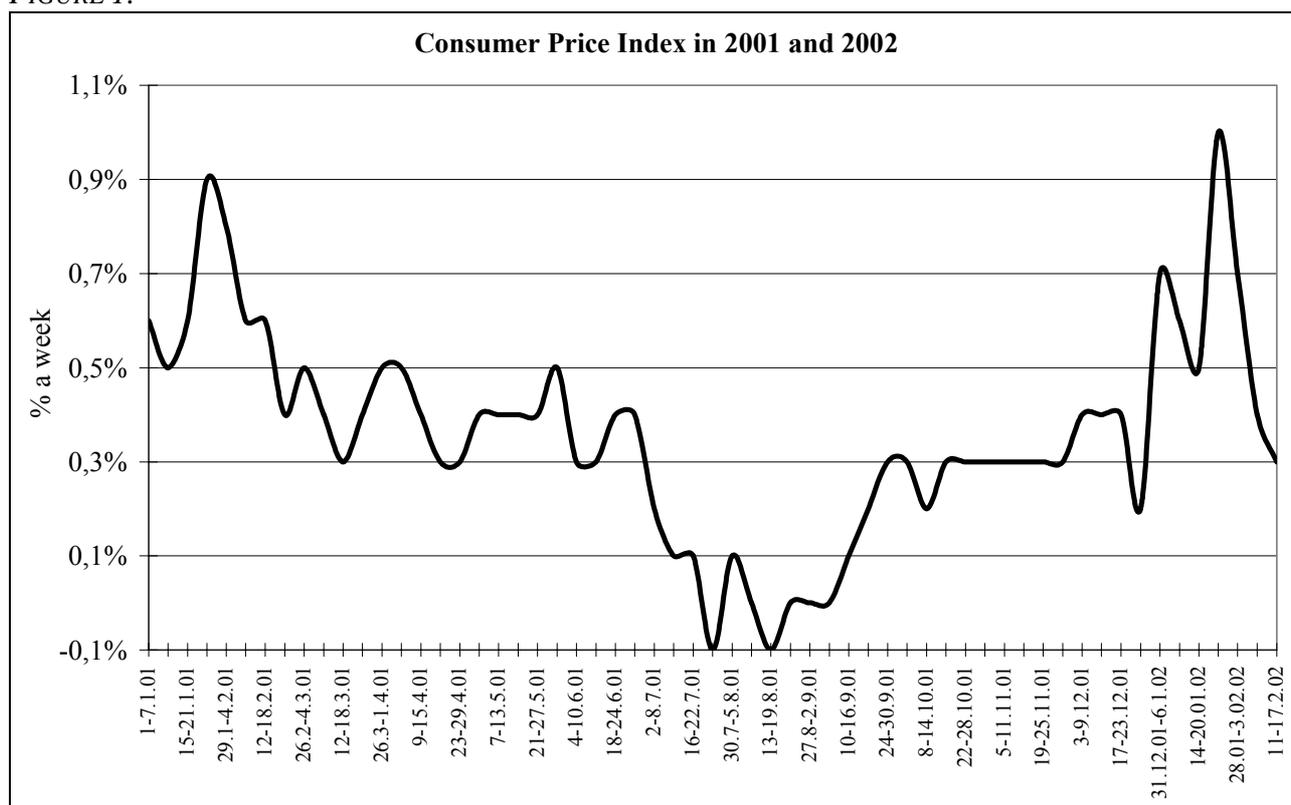
Monetary Policy

The final CPI growth values in January 2002 appeared to be much higher than we assessed in our previous report. The inflation rate in the first month of 2002 (based on CPI) reached 3.1% (about 44% annualised). That is the highest monthly price growth rate during last three years (since February 1999). It should be noted that price growth in January 2002 mostly fell on the last two weeks of the month, after the RF Government decided on limits of increase in natural monopolists' prices and tariffs. The commodity structure of the CPI growth proved the assumption on leading role played by administrative and seasonal factors in determining consumer price growth rate, while contribution of monetary factors appeared secondary in this regard. Specifically, the food stuff price index grew by 2.8% (at the same time prices for fruits and vegetables rose by 16.6%), the non-food goods price index – by 1.2% (prices for medicines grew by 5.2%, mainly because of abolition of their

exemption from VAT), prices for services – by 7.5%. The latter (the highest monthly rate of prices growth for services noted since January 1996) was caused primarily by the price rise for housing (by 8.8%), communications (18.0%), and railway transportation (18.9%).

However, yet in early February 2002 the weekly rates of CPI growth fell sharply (see Fig. 1). In our view, the inflation rate in February did not exceed 1.5%. Specifically, after two first months of 2002 the consumer price growth rate lags behind the respective value of 2001 (4.6% against 5.2%). Taking into account that the RF Government has no plans to renew increase in regulated prices until the end of the year and the rate of monetary expansion in 2002 will be slower because of smaller positive trade balance, we expect the year inflation rate in 2002 to be below the respective value of 2001. Namely, we forecast that consumer prices will grow by 15–16%.

FIGURE 1.



In February 2002 the Russian Central Bank renewed the policy of a slow accumulation of foreign reserves (see Fig. 2). By February 18 the foreign reserves increased by \$600 million as compared to late January 2002 and by \$100 million – as compared to the end of 2001. But, during the

third week of the month the reserves once again fell by \$600 million. In our opinion, that was explained by the sale of foreign exchange to the RF Ministry of Finance to repay on the foreign debt (Russia's payments on its debts to the Paris Club amounted up to \$1.3 billion). During the first three months of

February the increment of narrow monetary base amounted to 3.5%, but, taking into account the reduction in money supply in January, the monetary

base is currently at 2.5% smaller than it was as of January 1, 2002.

FIGURE 2.

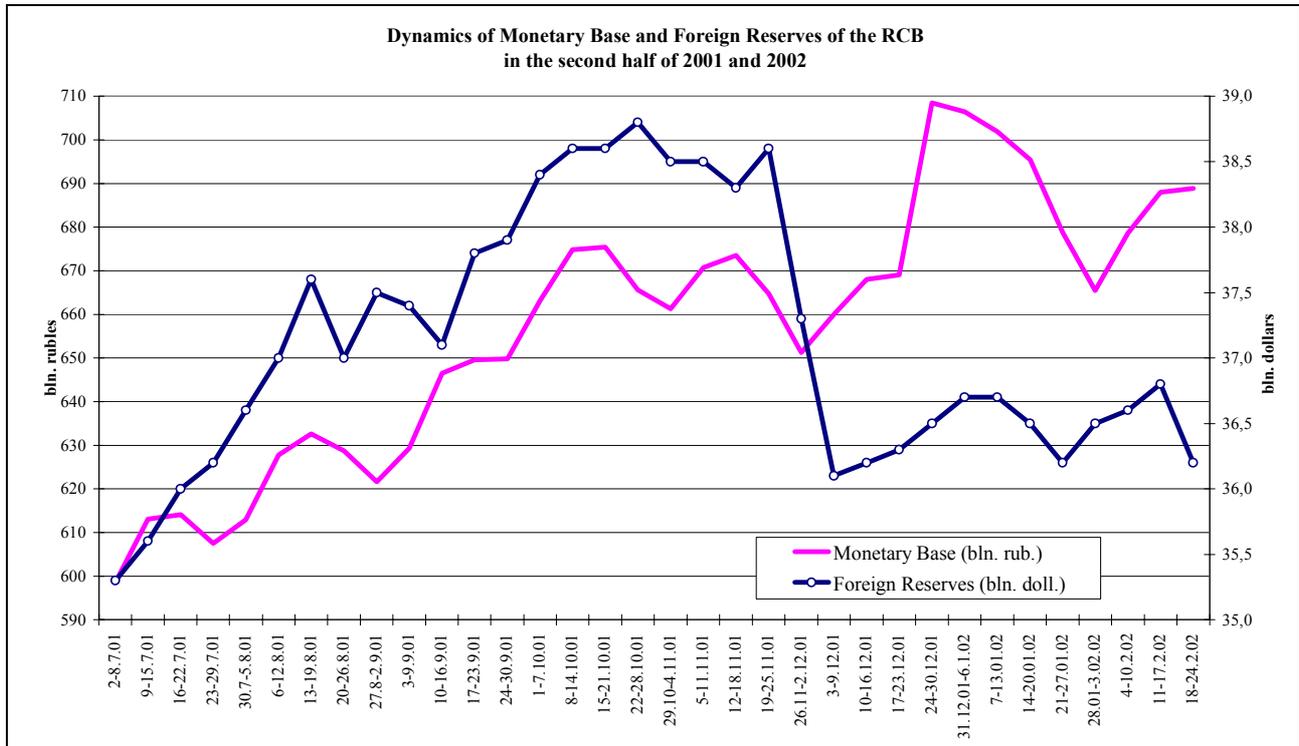
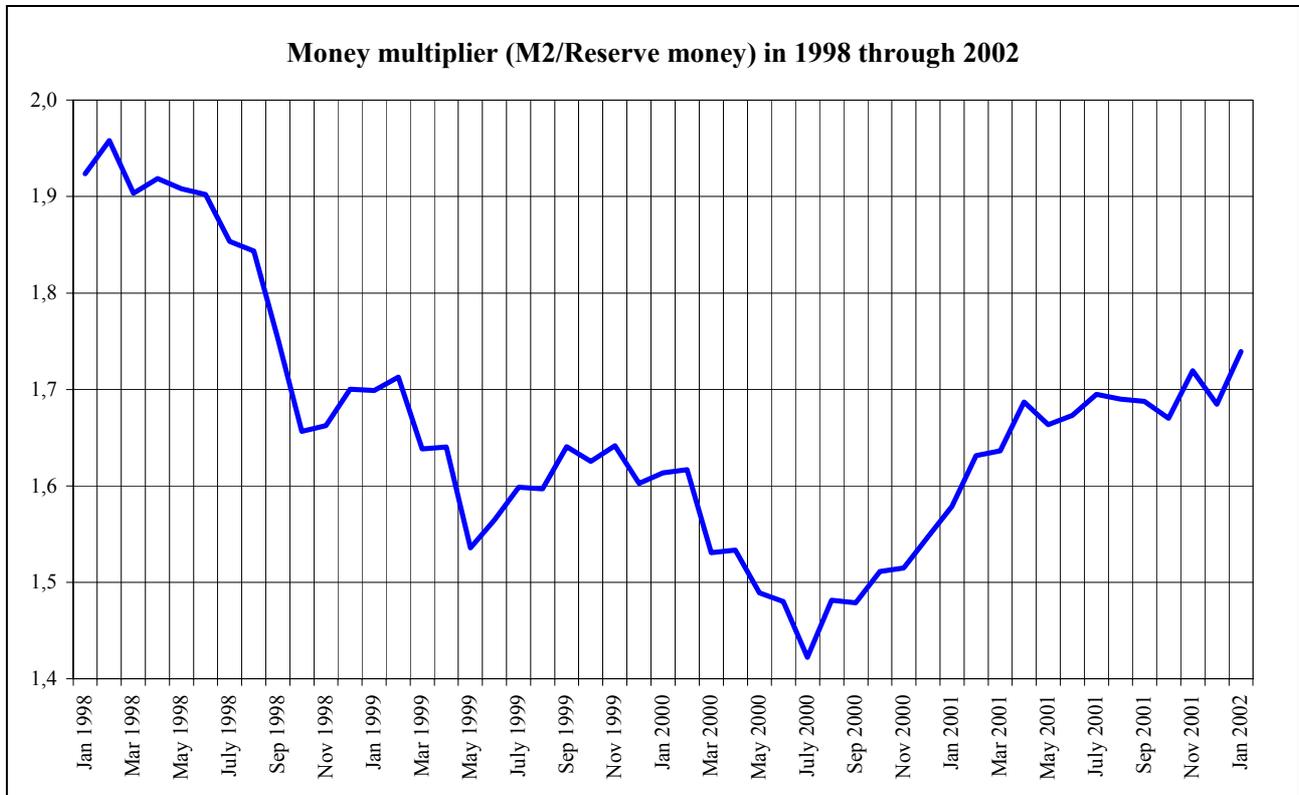


FIGURE 3.



In late 2001 and early 2002 the money multiplier renewed its growth after a half-year stabilisation at

the level of 1.67–1.69 (see Fig. 3). By the end of January 2002 the M_2 to reserve money ratio reached

the level of 1.74, i.e. the level of September 1998. Notably, the new period of larger money multiplication in the economy coincided with a recession in real sector (seasonally adjusted industrial production index has gone down since November 2001). Therefore, one can suppose the bank lending expansion matched mainly the real

sector's demand for additional financing for the sake of investing in the envisaged new period of economic growth. This assumption can be also proved by the stabilisation (and, even, some decline) of money multiplier on the eve of recession in 2001.

S. Drobyshesky.

Financial Markets

The market for government securities.

The tendency to growth in prices of all securities was still there in the market for the Russian foreign debt in February 2002 (see Figs. 1 and 2). By late February yields to maturity of the Russian debt liabilities peaked their historical maximums. Specifically, the yield rate on the fourth issue of Minfin bonds (maturity in 2003) fell to 6% annualised. Therefore, investors estimate the default risk premium price on this issue at the level of 1% annualised, as yield to maturity on the eurobonds of similar maturity is about 5% annualised. The yields on other Minfin issues have fell below 10% annualised, and the highest yield on eurobonds does not exceed 10.5% annualised. At

FIGURE 1.

the same time, it is worth noting, that in January and February 2002 the RF Ministry of Finance bought back a portion of Minfin 4th issue in the secondary market. That operation, along with pre-scheduled payments of the Bank of Russia to the IMF, somewhat lifted the burden of the "problem 2003": nowadays, the estimated amount of payments due on foreign debt in 2003 roughly accounts for \$15 billion, i.e. it is comparable with the amounts due in 2001 and in 2002. However, it is impossible now to analyse which proportion of yields' decrease was attributed to reduction in country risk and which – to the rise in demand for securities in the second market under buyback.

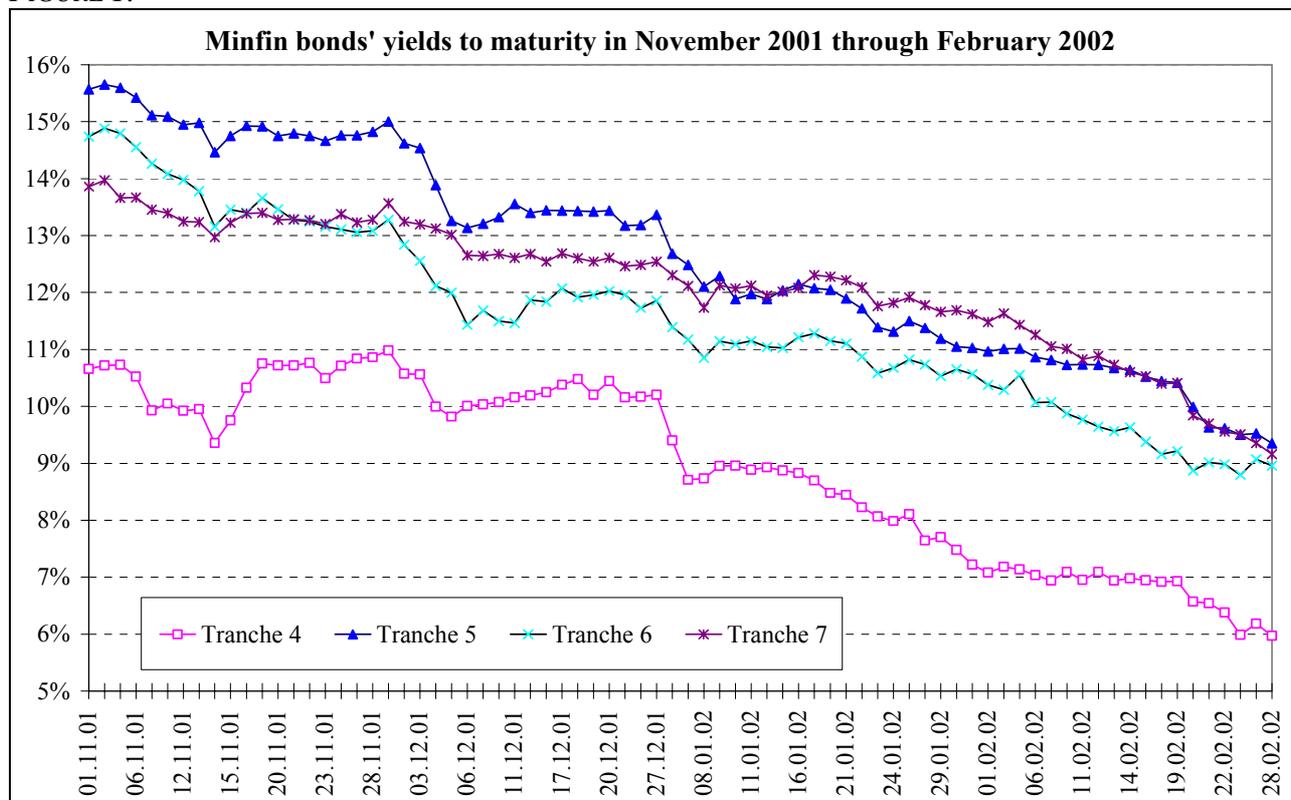
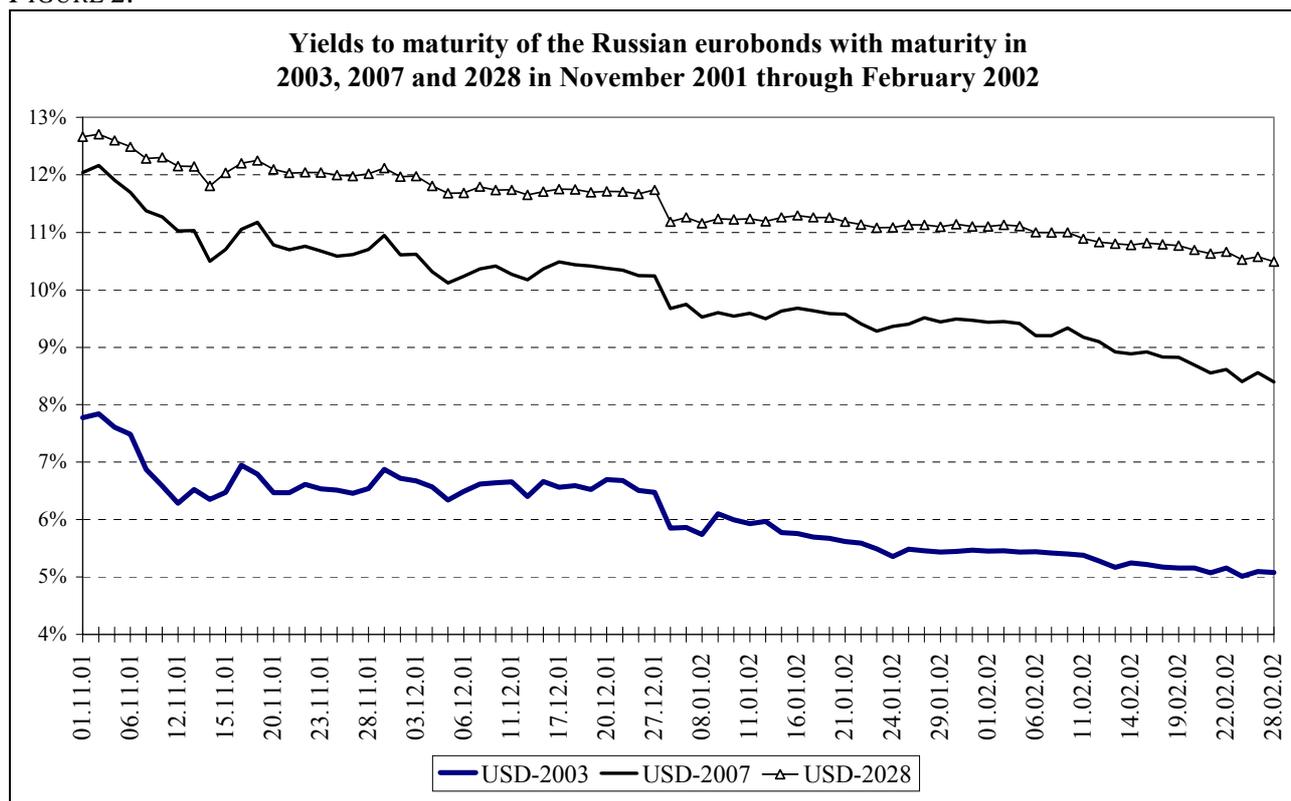


FIGURE 2.



In January and February 2002 one can see an unprecedented fall in yields along with extremely low trade volumes in the GKO-OFZ market. Specifically, despite of higher inflation rates, in some weeks the nominal average-weighted GKO-OFZ yield to maturity slid to 13.5–14.0% annualised, while the turnover in the secondary market dropped below one billion roubles. Hence, the monthly trade volumes in 2002 are the lowest one since spring 1999, when the market just reopened after the 1998 crisis.

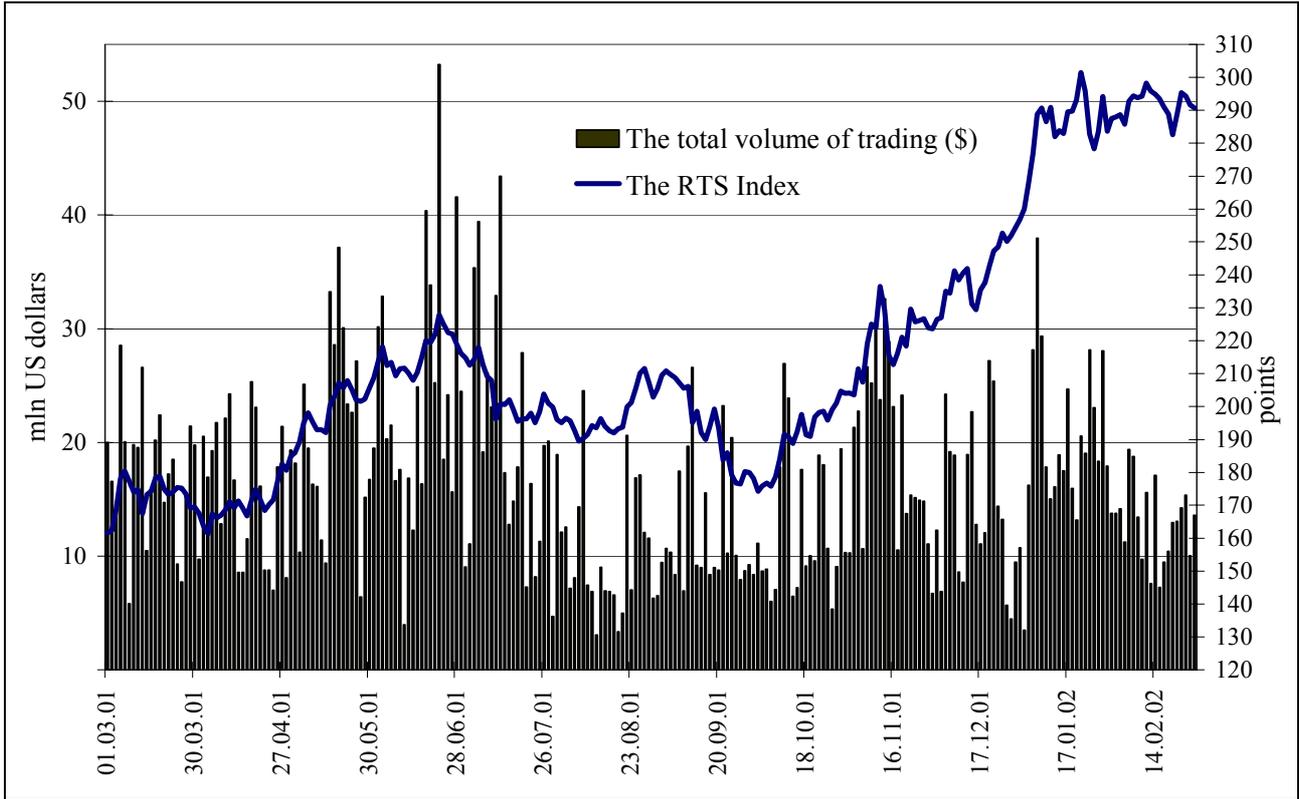
Stock market.

The side trend, which sprang up in the Russian stock market as early as in late January, lasted until late February. The absence of a clear tendency and any important events encouraged a rise in the number of speculative “intraday” deals, and the RTS Index shimmied within a narrow band. However, positive news from the S&P in late February and growing investors’ hopes for recovering of the world economy induce

expectations of a further upsurge in the Russian stock market.

In total, in February the RTS Index grew by 3.22 points (1.12%) with trade volumes accounting for about \$247 million. The fall in trade volume amounted up to 40% compared to the previous month, the average daily turnover in the RTS made up \$13 million. On February 15, the trade volume came down to its annual minimum – \$7.25 million. The stock index fluctuated within a narrow range of 282 to 299 points. Though it was twice over the month – on February 12 and February 26 – that the Index was dangerously close to the psychological level of 300 points, it failed to overstep it though. During the first decade of the month the stock index gained 10.8 points and on February 12 reached the highest level noted in February – 298.32 points. It fell consequently in mid-February to the month’s minimum value – 282.56 points (February 20). The month ended up with the side trend around the level of 292 points.

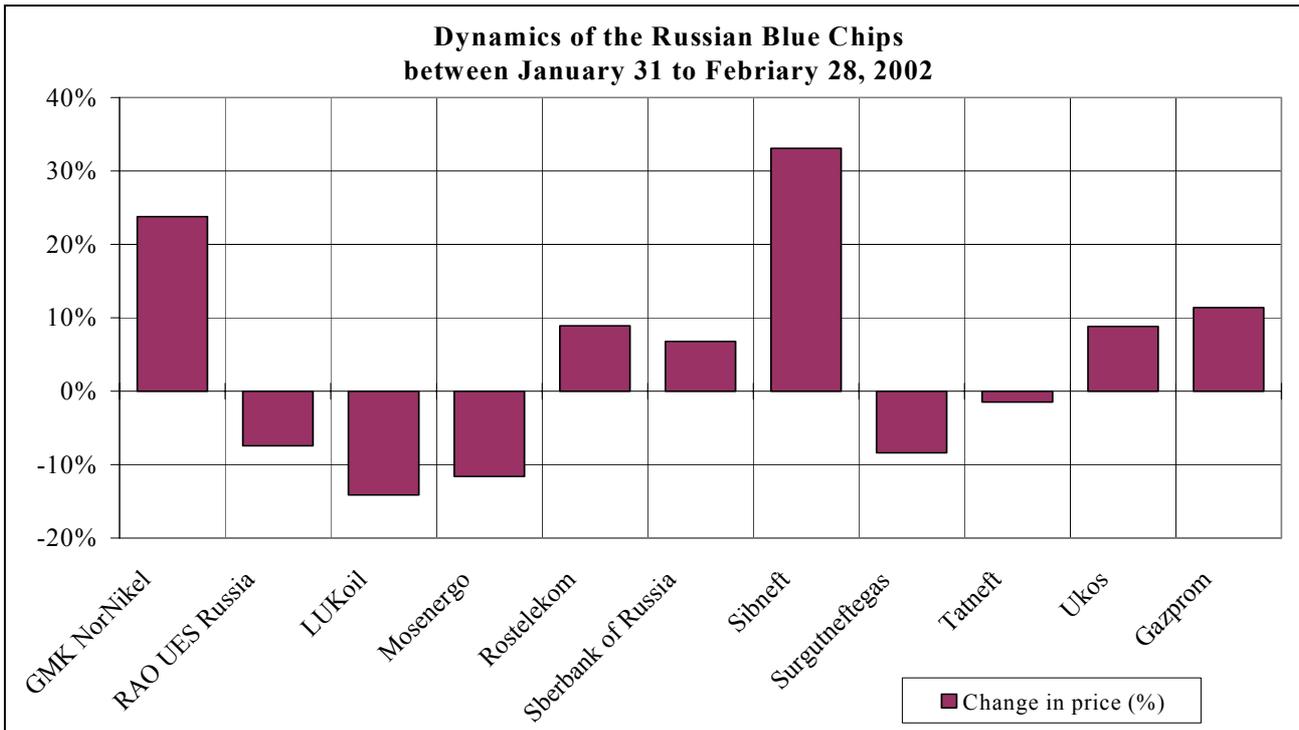
FIGURE 3.



The leaders among *blue chips* (on February 28) were stocks of “Sibneft” (33.09%), MMC “Norilsky Nickel” (23.8%), “Rostelecom” (8.93%), “YUKOS” (8.83%) and Sberbank (6.8%). The list of stocks. prices of which fell down, is open with those of “LUKoil” (-14.12%), “Mosenergo” (-

11.62%) and “Surgutneftegas” (-8.39%). It is worth noting the highest growth of quotations was fixed among “second echelon” stocks. Thus, stocks of “Tulenergo” soared with 66.7%, common stocks of “AvtoVAZ” – 54.15%, preferred stocks of “AvtoVAZ” – 40.74%.

FIGURE 4.



In February the share of RAO "UES Russia" common stocks in the total RTS turnover was 24.81% (in January – 30.12%), the share of "LUKoil" stocks was 18.9% (19.89%), "YUKOS" – 9.98% (8.6%), MMC "Norilsky Nickel" – 7.21% (4.6%), "Surgutneftegas" – 7.41% (7.86%). Overall, in February, the total share of the top five most liquid stocks in RTS dropped to 69.2% (in January – 71.34%).

As far as the period between February 1 to February 28, 2002 is concerned, the trade volume on "Gazprom" stocks via RTS terminals exceeded \$33.6 million (54.6 million stocks). In total 3.7 thousand deals were struck. The quotations of "Gazprom" stocks grew by 11.4%.

Despite of stagnation of the spot stock market, the term stock market continued its growth. In February, the turnover in the FORTS amounted to 5.7 billion roubles (30 thousand deals, 1158.6 thousand contracts). These figures well outrun the January indicators: the number of deals surge by 24%, the turnover – by 46% (in roubles) and by 64.8% (in contracts). As of February 28 the total open interest peaked its historical maximum in the FORTS – 689.5 million roubles, i.e. 20% higher than in January (580 million roubles).

The futures section of the FORTS ended up with 29 thousand deals worth a total of 5.7 billion roubles, 1149 thousand contracts (January – 3.85 billion roubles, 23.8 thousand deals, 700.8 thousand contracts). The trade volume on futures grew by 48%, the number of deals – by 21.8%. On February 19 the maximum trade volume on futures was fixed – 451.3 million roubles (93.6 thousand contracts), on February 20 the number of deals on futures exceeded 2 thousand for the time and reached 2195.

The trade activity in FORTS on options doubled in February and amounted to 707 deals (January – 343 deals), the number of open interest tripled. Overall in February, the market participants stroke deals totalled 46 million roubles (9.3 thousand contracts)/ This was 3 times higher than in January (15 million roubles). On February 28 the open interest on options reached 55.7 million roubles (on January 31 – 17.5 million roubles).

It was futures on RAO "UES Russia's" stocks that enjoyed the greatest popularity in the term market were. The respective share in the FORTS turnover made up to 80% (4.6 billion roubles), the number of deals for the month – about 25 thousand.

Those were followed, though with a great gap, between them, by futures on "LUKoil" stocks – 8.5% (490 million roubles, 2.5 thousand deals) and futures on RUIX investment index – 7% (400 million roubles, 907 deals). The most traded options were those of RAO "UES Russia": the respective trade volume equalled 0.8% of the total turnover in the FORTS (46 million rouble, 707 deals).

In February the RTS listing reflected certain changes. The second level list was expected by stocks of "Lenenergo" and "Centrotelecom", while stocks of "Aeroflot" were downgraded from the first level list. Therefore, as of end of February, the total number of stocks in the RTS listing was 28, including 7 ones in the first level list and 21 – in the second level list).

In February the biggest top-5 (according to the NASMP data) Russian corporations in terms of market capitalisation were: "Gazprom" – \$15.5 billion, "YUKOS" – \$15.3 billion, "Surgutneftegas" – \$12.6 billion, "LUKoil" – \$10.6 billion and RAO "UES Russia" – \$6.45 billion.

External factors. On February 3, while addressing to the World Economic Forum in New York, Prime Minister M. Kasyanov stated that Russia could turn down restrictions on oil export.

Overall, hungry for important news, the oil market demonstrated the side trend within the range of 19.5–21.5 \$/bbl. In early February, the market was restrained by an increase in the US oil reserves and Kuwait's renewal of its oil export in full. The price growth in the mid of the month was partly generated by expectations of a new US military action against Iraq, which inevitably resulted in the cease of - the Iraqi oil export as well as in rumours about reduction in the US oil reserves. As of February 1, 2002, Iraq exported 13.5 million barrels a week, or 1.93 million barrels per day. In the very beginning of March the OPEC General Secretary A. Rodriguez visited Moscow and met the Russian officials, however, no final decisions on co-ordination of the Russian and the OPEC policies in the oil market were made.

The London Centre for Global Energy Research reported the situation in the world oil market was likely to normalise as early as in the second quarter of 2002, provided that OPEC retain the current oil production.

FIGURE 5.

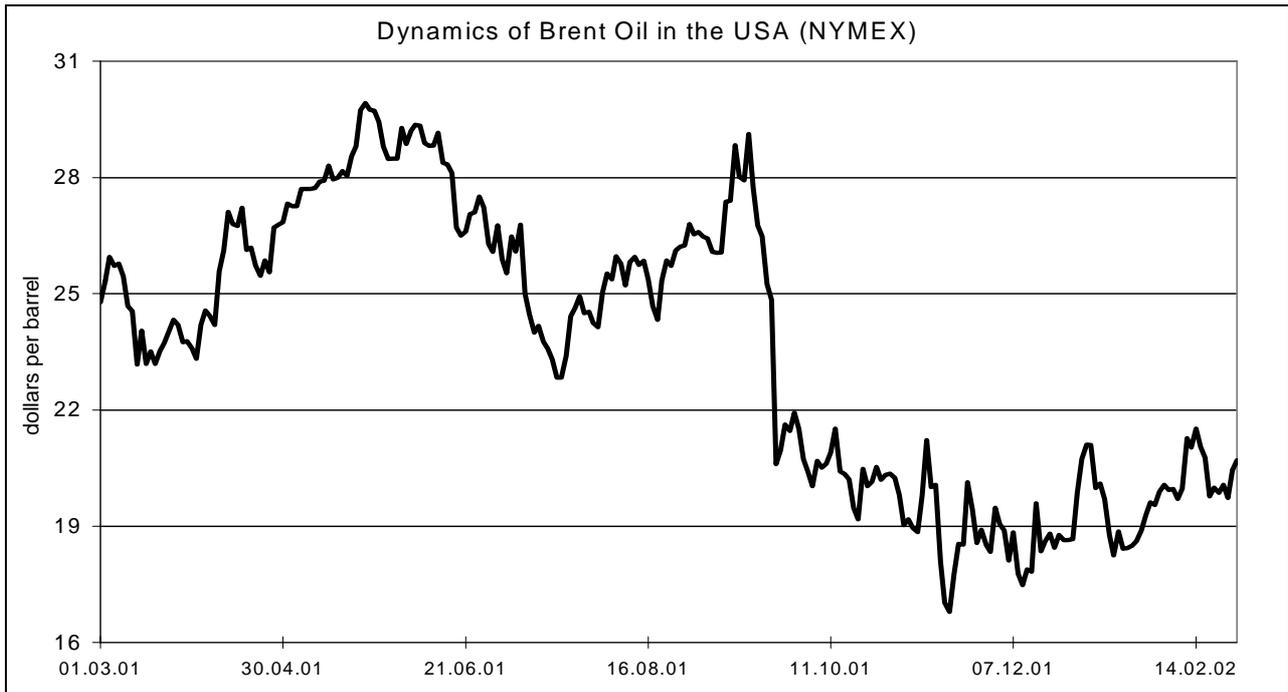
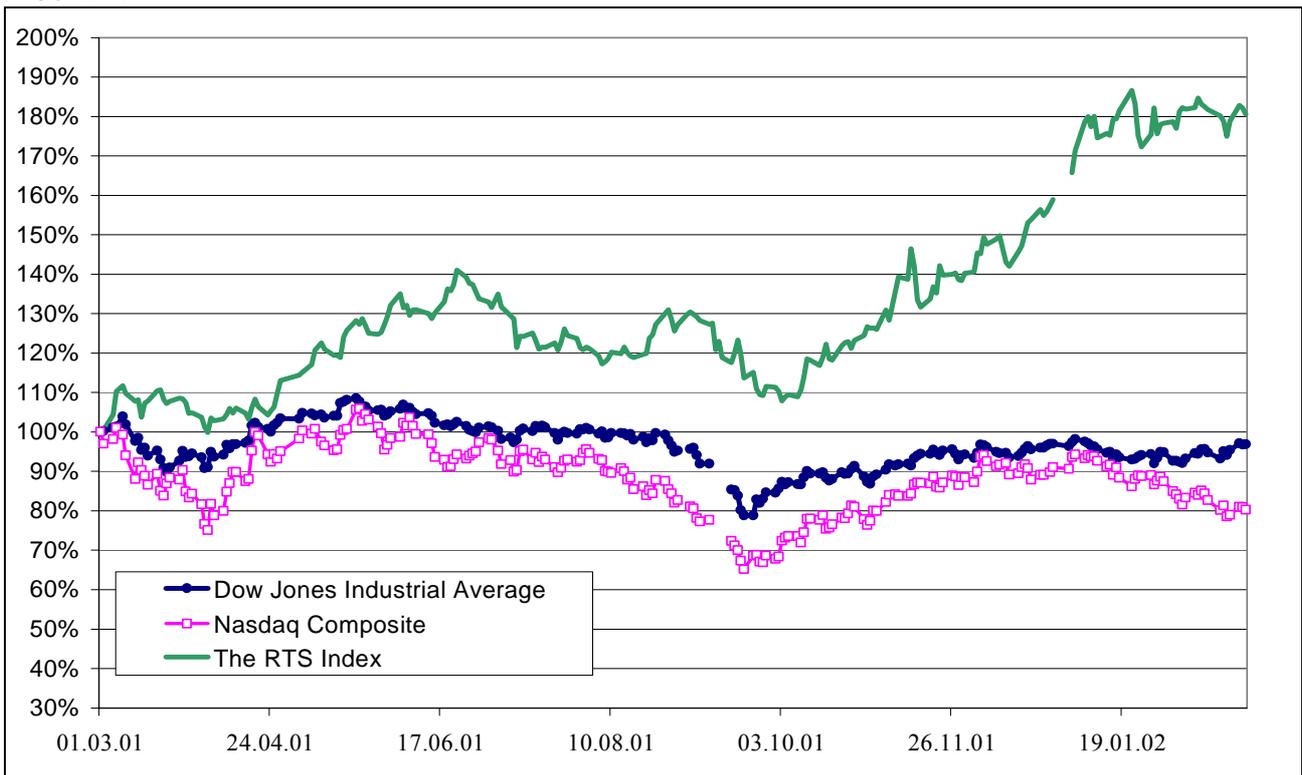


FIGURE 6.



Following the Fed, the central banks of economic developed countries left their key interest rates unchanged. The Bank of England decided to not change its refinancing rate, which is currently at 4.0%. The last time the Bank of England reduced its key interest, by 0.5% from 4.5% to 4.0% was on November 8, 2001 when, The European Central Bank also decided to leave the key euro interest rates unchanged.

Hence, the refinancing rate remained at the level of 3.25% annualised.

On Friday, February 22, the international rating agency Standard & Poor's reported the upgrade of the Russia's rating forecast from "stable" to "positive". One of the reasons for the forecast revision undoubtedly was the RF Ministry of Finance's statement that the volume of debt payments in 2003 would be at \$2.5 billion less than expected. The news

stimulated the rise of prices of the Russian “blue chips”. In one hour after the news was broken, the prices surged by 1-3% along with a rise in trade activity. We should note that presently the Russian rating set by S&P is at one grade behind the one by Moody’s, and so it is very likely that S&P grade. would soon catch up the latter

Corporate news.

The annual shareholders meeting of “Norilsky Nickel” will take place in Moscow on June 21. The meeting will elect a new Board of 17 directors to be approved by the present Board of Directors.

The Director General of “Lenenergo” A. Likhachev proved that that the company had consulted Standard & Poor’s concerning conferment a rating.

According to preliminary data, the net profit of “Gazprom” in 2001 amounted to 100 billion roubles, and it is envisaged to account for some 73 billion roubles in 2002. In 2001 “Gazprom” produced 512 billion cubic meters of gas and 10.2 million tons of condensate and oil. The volume of processed gas accounted for 34.6 billion cubic meters. Last year the gas concern supplied 317.5 billion cubic meters of gas to the domestic market, while another 126.9 billion cubic meters – to Europe and yet 39.8 billion cubic meters – to the Baltic states. The Board of Directors decided that the annual “Gazprom” shareholders meeting would take place on June 28, with registration of shareholders to be closed on May 13.

Over the three quarters of 2001 The net profit of “LUKoil” according to US GAAP slid to \$1937 billion compared to \$2458 billion for nine months of 2000. The net profit per share amounted to at most \$2.47 over the reported period. Such unfavourable news resulted in a 7% drop in “LUKoil” stock price, despite a 8% price rise for URALS oil (occurred between February

11 to February 15). That was why the RTS Index did not responded to the rise in oil prices.

“Surgutneftegas” informed that the annual shareholders meeting would take place on March 30, 2002. The shareholders should approve the annual report, divide the company’s profit for 2001, decide on dividends, and elect a new Board of Directors, auditing commission and company’s auditor. It is worth noting that the company managed to reduce dividends on the grounds of legislation weakness last years and investors have lost their interest in “Surgutneftegas” securities.

In early February the leading Russian dairy and juice producer “Wim-Bill-Dann” placed its ADS on the NYSE. In total, the company placed 10.62 million ADS at \$19.50, worth a total of \$207.1 million, the demand exceeded supply by five times. Thus, the market capitalisation of the company was evaluated by the US investors at \$828.4 million. That was for the first time that a Russian company operating in the market for consumer goods became listed at NYSE. Until recently it was only four Russian companies’ ADSs that have been listed on the NYSE (three of those were from telecommunication sector) – “Vypelcom”, “Rostelecom”, “MTS,” and “Tatneft”. Such a successful placement of ADS by “Wim-Bill-Dann” undoubtedly should have a positive impact on dynamics of the Russian stock market and give a positive signal to foreign investments inflow to the market.

The total receipts of “Mosenergo” in 2001 made up 46 billion roubles. The company has reduced its accounts payable by 4,055 million roubles (from 11,263 million roubles as of beginning of 2001 to 7208 million roubles as of early January 2002). The company’s representatives argued the profits enough financial resources (336 million roubles) to pay dividends for 2001.

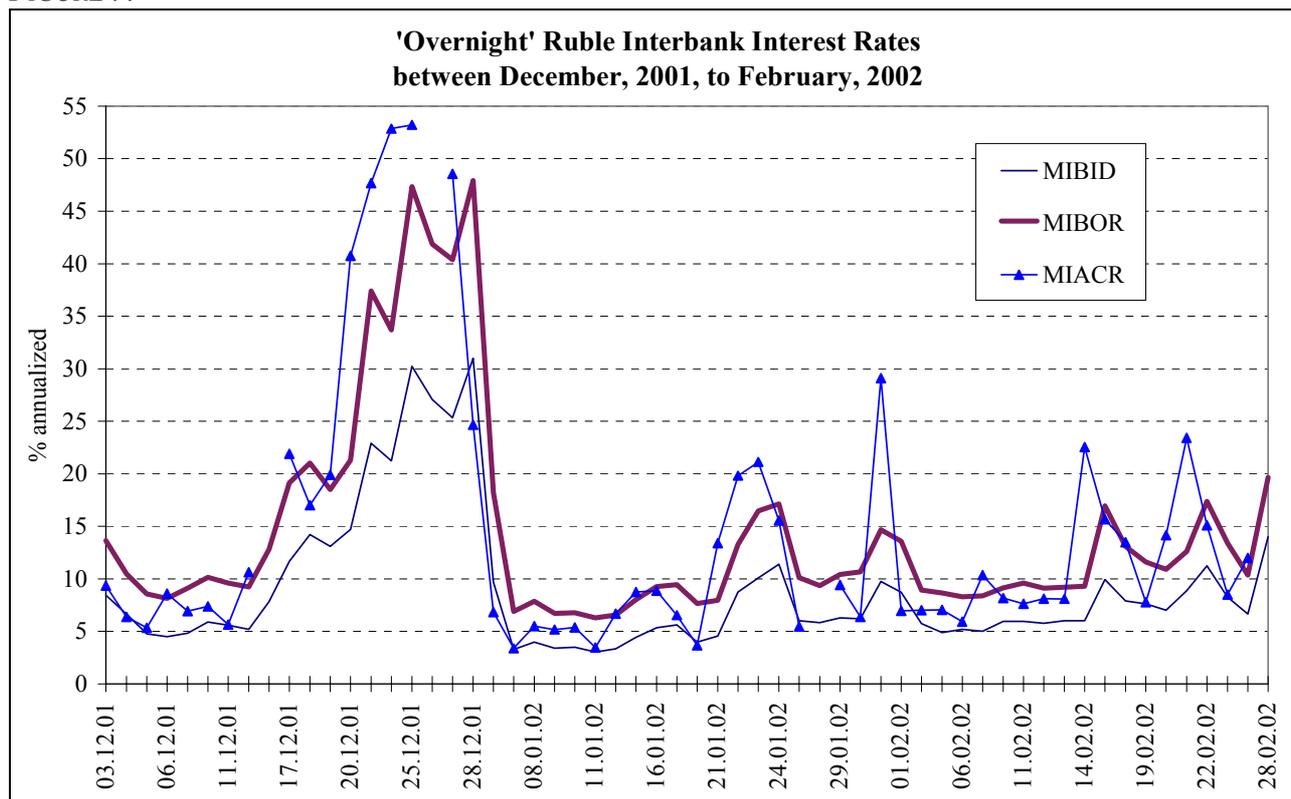
TABLE 1. DYNAMICS OF THE FOREIGN STOCK INDEXES

as of February 27, 2002	value	change for last month (%)	change since beginning of the year (%)
RTS (Russia)	291.64	1.43%	13.59%
Dow Jones Industrial Average (USA)	10127.58	2.09%	-0.09%
Nasdaq Composite (USA)	1751.88	-9.42%	-11.84%
S&P 500 (USA)	1109.89	-1.80%	-4.40%
FTSE 100 (UK)	5178.4	0.26%	-1.22%
DAX-30 (Germany)	4960.22	-2.89%	-3.87%
CAC-40 (France)	4424.71	-0.83%	-4.32%
Swiss Market (Switzerland)	6319.9	1.32%	-1.53%
Nikkei-225 (Japan)	10573.09	5.75%	0.29%
Bovespa (Brazil)	14212	11.72%	4.67%
IPC (Mexico)	6795.9	-1.90%	5.08%
IPSA (Chile)	96.22	-1.27%	-11.81%
Straits Times (Singapore)	1702.37	-4.73%	4.70%
Seoul Composite (Korea)	822.11	9.90%	18.51%
ISE National-100 (Turkey)	11186	-15.59%	-18.84%
Morgan Stanley Emerging Markets Index	335.038	2.22%	6.29%

Interbank credit market.

The situation in the rouble interbank credit market between late 2001 to early 2002 was characterised by a smooth upward trend of interest rates (see Fig. 7). After the peak in the second half of December 2001 (up to 50–55% annualised), when banks attacked the rouble exchange rate, in January 2002 the rates came back to the level of 5–7% annualised, which was typical for the most part

FIGURE 7.



of 2001. However, as liquidity within the banking system fell (because of rouble withdrawals by the Bank of Russia the balances on correspondent accounts of commercial banks in the Russian Central Bank shrank from 100–120 to 70 billion roubles), the rates on interbank loans went up, and by late February they reached the level of 10–20% annualised.

Foreign exchange market.

In February 2002 the tendency to growth of dollar/rouble exchange rate continued, but the pace of devaluation slowed down substantially. In our opinion, the Bank of Russia played a passive role in the market, it did not intervene with selling foreign exchange, but also restricted purchasing of foreign exchange supplied by exporters. At the same time, taking into account seasonal fluctuations of trade balance, we suppose the supply of foreign exchange on the part of exporters grew in February compared to December and January, while demand for foreign exchange for import remained at the level noted in December. Hence, the participation of the Bank of Russia in the market as well as increment of its foreign reserves appeared to be modest, while

rouble exchange rate dynamics were determined mainly by the demand on the part of commercial banks, which was restricted by volume of liquidity within the banking system.

In total, in February 2002, the official dollar exchange rate grew from 30.685 roubles/\$ to 30.9404 roubles/\$, i.e. by 0.83% (10.4% annualised, see Fig. 8). The ‘today’ dollar exchange rate in the SELT increased from 30.7100 roubles/\$ to 30.9483 roubles/\$ (as of February 27), i.e. by 0.78%. The ‘tomorrow’ dollar exchange rate grew from 30.7248 roubles/\$ to 30.9564 roubles/\$ (as of February 27), i.e. by 0.75%. According to preliminary estimates, in February the trading volumes by dollar in the SELT did not exceed 110 billion roubles.

FIGURE 8.

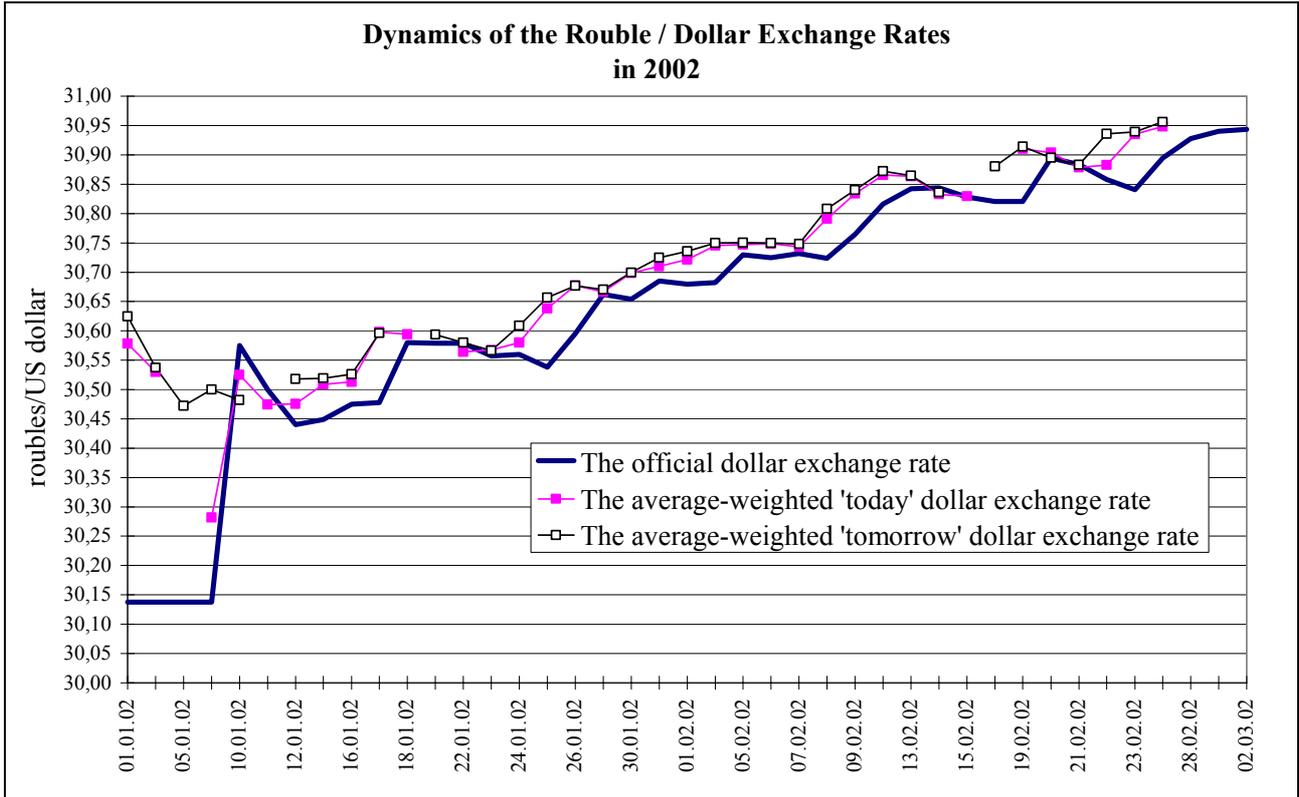
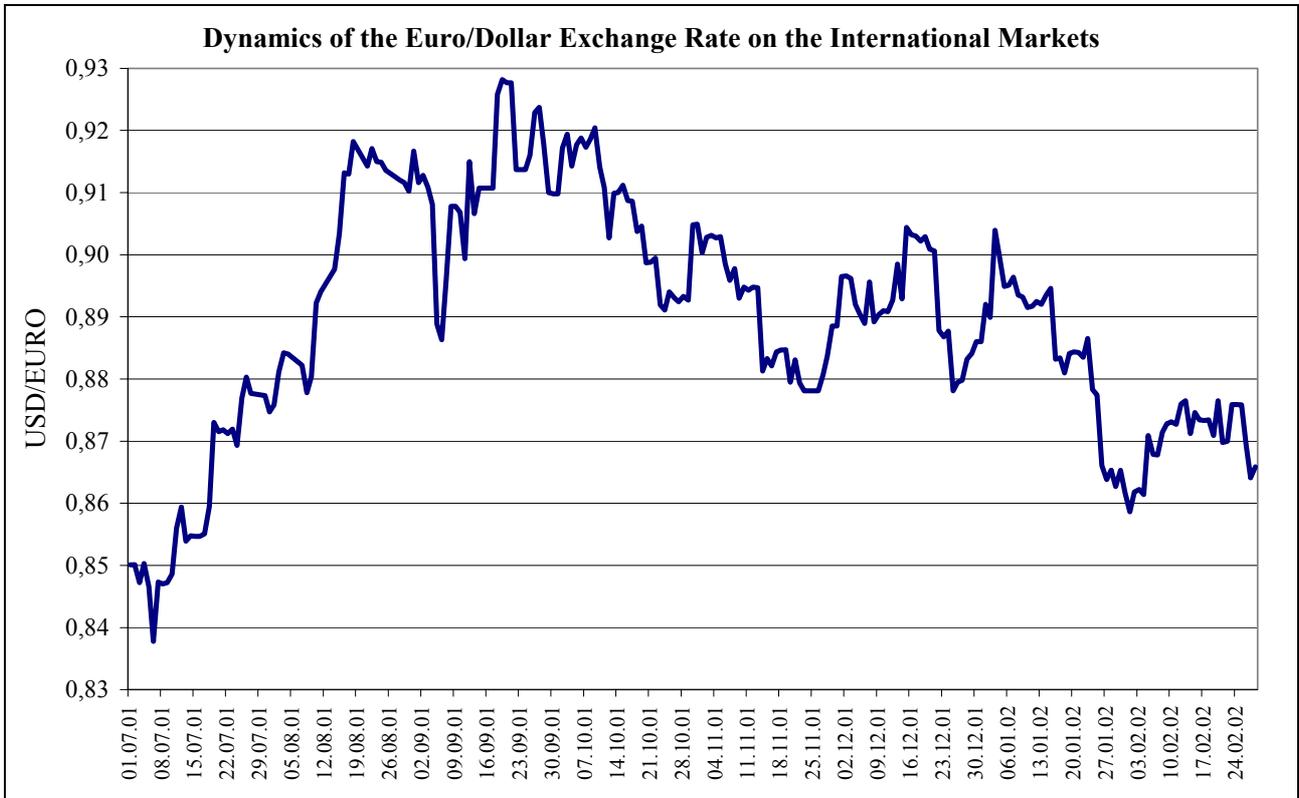


FIGURE 9.



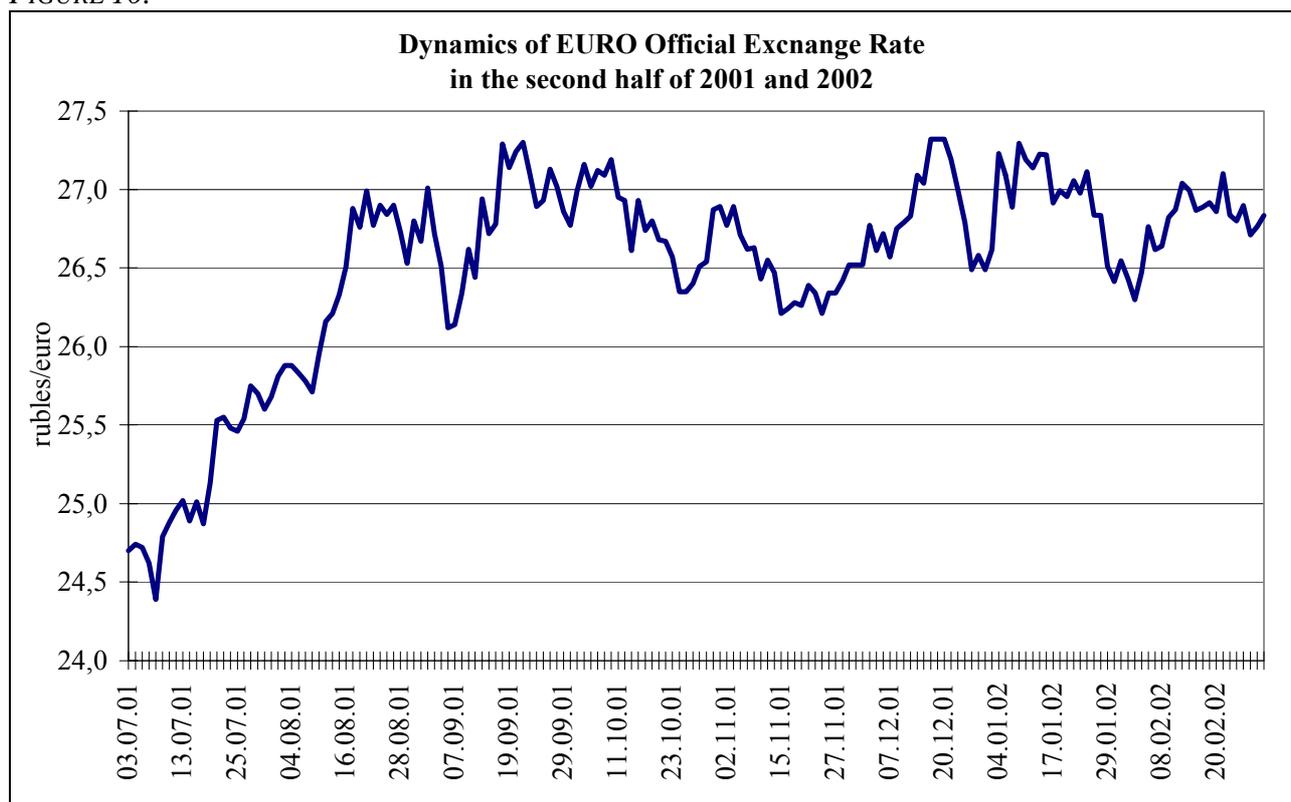
In February the euro / dollar exchange rate in the international foreign exchange market went down, and it fluctuated around the level of 0.87 \$/euro during the whole month (see Fig. 9). The main

reason for further decline in the euro exchange rate was the difference in forecasts on the USA and the euro-zone economic perspectives for 2002. The preliminary data testify the recession in the US

economy stopped already in January 2002, and it is likely to renew its growth as early as in mid-2002. At the same time, in February 2002 the data available indicated negative rates of real growth in the biggest European economy (Germany) for two quarters running, and, therefore, the position of the European economies within the business cycle remained shaky.

In February 2002 the euro/ruble exchange rate still fluctuated around the level of 26.5 to 27.5 roubles per euro (see Fig. 10). Actually, the rouble and euro devalue against the US dollar with the

FIGURE 10.



same pace during the past half-year, and the rouble/euro exchange rate remained practically constant. In February, the rouble/euro official exchange rate decreased from 26.5456 roubles/euro to 26.712 roubles/euro, i.e. by 0.63% over the month. At the same time, one should note a growth of interest in the European currency in the Russian foreign exchange market. According to preliminary estimates, in February 2002, the total trading volume on euro in the SELT made up to 3 billion roubles.

TABLE 2. INDICATORS OF FINANCIAL MARKETS.

	October	November	December	January	February*
inflation rate (monthly)	1.1%	1.4%	1.6%	3.1%	1.5%
annualised inflation rate by the month's tendency	14.03%	18.16%	20.98%	44.25%	19.56%
the RCB refinancing rate	25%	25%	25%	25%	25%
annualised yield to maturity on OFZ issues	15.07%	14.91%	15.84%	14.08%	13.8%
volume of trading in the secondary GKO-OFZ market a month (billion roubles)	9.14	12.56	10.20	4.51	6.0
yield to maturity on Minfin bonds by the end of the month (% a year):					
4th tranche	10.61%	10.57%	10.20%	7.22%	6.0%
5th tranche	15.53%	14.62%	13.36%	11.03%	9.4%
6th tranche	14.76%	12.84%	11.86%	10.57%	9.0%
7th tranche	13.92%	13.24%	12.54%	11.62%	9.2%
8th tranche	14.29%	12.88%	11.93%	10.41%	8.8%
INSTAR – MIACR rate (annual %) on interbank loans by the end of the month:					

	October	November	December	January	February*
overnight	24.76%	19.80%	24.66%	29.09%	12%
1 week	19.03%	16.24%	23.97%	8.24%	17%
official exchange rate of ruble per US dollar by the end of the month	29.70	29.93	30.14	30.6850	30.9404
official exchange rate of ruble per Euro by the end of the month	26.87	26.52	26.617	26.5456	26.7120
average annualized exchange rate of ruble per US dollar growth	1.05%	0.77%	0.70%	1.81%	0.83%
average annualized exchange rate of ruble per euro growth	0.04%	-1.30%	0.37%	-0.27%	0.63%
volume of trading at the stock market in the RTS for the month (millions of USD)	279.0	394.2	277.0	419.7	247.1
the value of the RTS Index by the end of the month	204.04	226.49	260.05	287.53	290.75
growth in the RTS Index (% a month)	13.20%	11.00%	14.82%	10.57%	1.12%

* Estimates

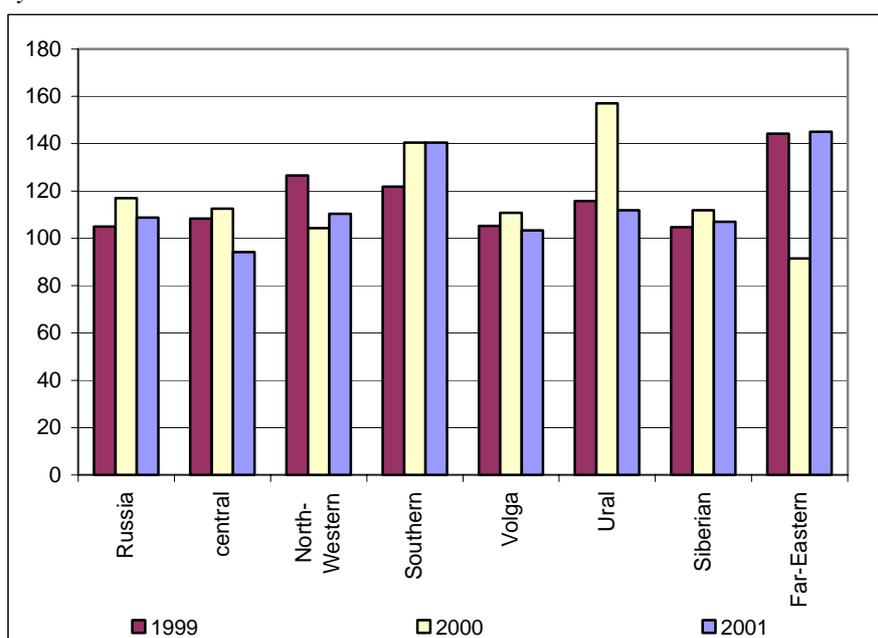
S. Drobyshevsky, D. Skripkin

Investment in the real sector

It is an intense rise in investment demand that becomes a notable feature of the national economy's development. During past years one noted a steady trend to advanced growth in investment in capital assets vs. dynamics of GDP and output of basic sectors of the economy. In 1991 the share of investment in GDP grew up to 17.7% vs. 16.8% reported over the prior year. This trend was encouraged by expanding domestic demand generated by the growth in enterprises' own and borrowed capital for investment purposes and the slowdown in producer prices in the industrial and construction sector.

In 2001 the volume of investment in capital assets by means of all the sources of financing accounted for Rb. 1,599.5 bln., or at 8.7% more than in the prior year. The renewal of investment activity in 2001 was accompanied with the rise in demand for construction services and capital goods. When compared with 2000 the volume of works accomplished by construction companies grew by 9.9%, increment in gross output in the machine engineering sector rose by 7.2% and that in the industry of construction materials – by 5.5%. Rise in investment in capital assets was registered in all the federal Super-regions, but Central one.

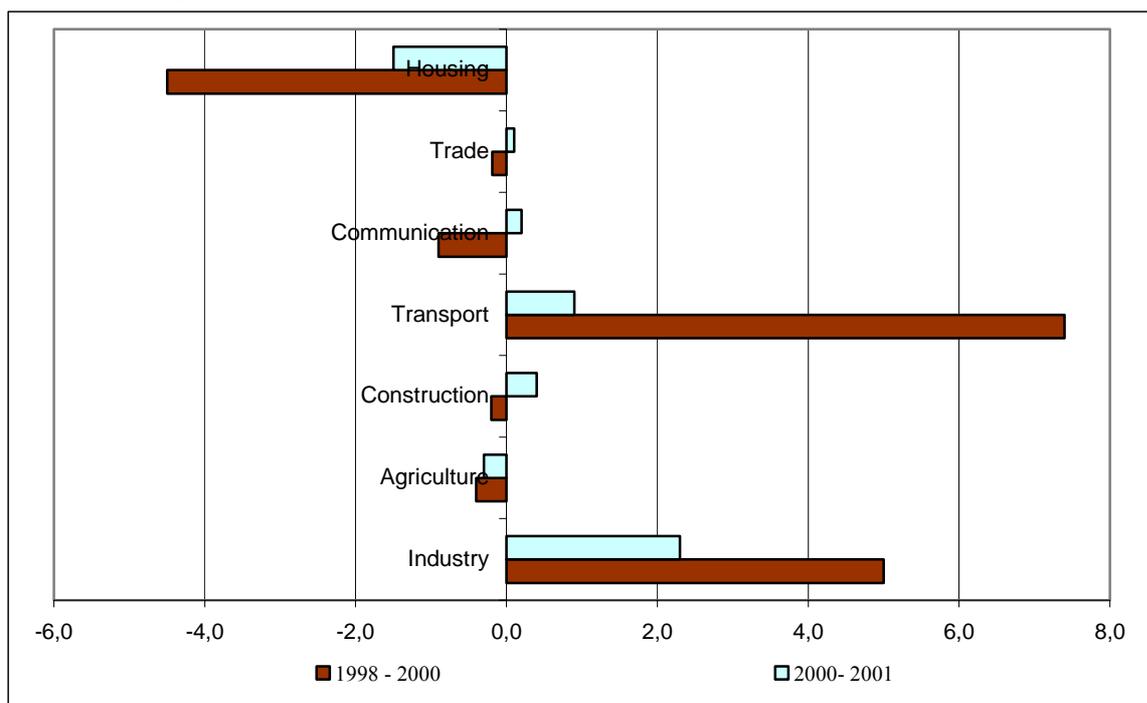
Fig. Dynamics of investment in capital assets across federal Super-regions between 1999 through 2001, as % to the prior year



The investment surge of 2000-2001 was structural by its essence and appeared determined by an aggregate impact of factors of changes in sectoral, technological and reproduction shifts in the national economy.

The reallocation of investment flows was taking place along with the rise in the share of infrastructure sectors and the growth in demand for

Fig. Change in the structure of investment across sectors of the economy between 1998 through 2001, as % over the respective period



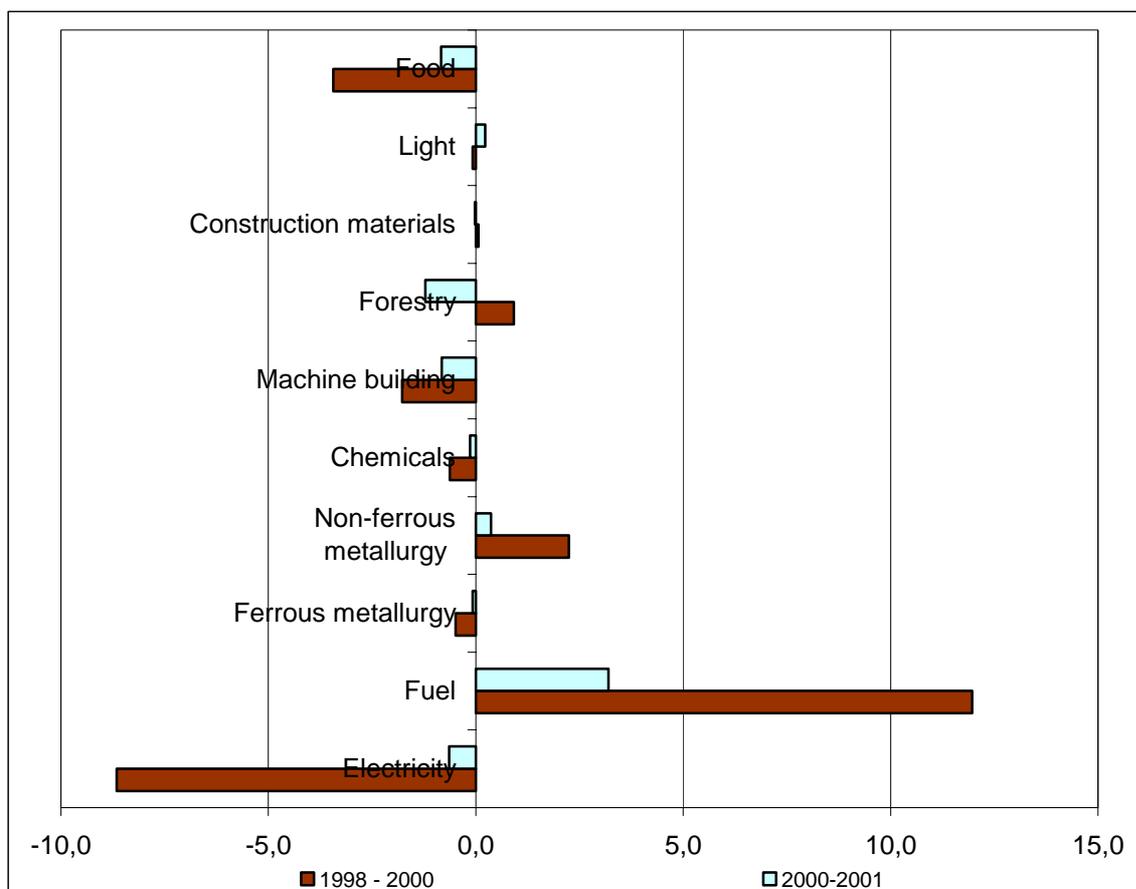
While evaluating the state of and prospects for the national economy's development, one should take into account the fact that the surge of investment activity to a considerable extent should be attributed to market situation. Against the background of changing priorities the investment structure mutated influenced by the growing demand on the part of the fuel and energy and metallurgical complexes. Changes in the structure of output in the sector for machine engineering were determined primarily by the growth in demand on the part of oil sub-sectors, transport, and communication. It was these sectors that reported the highest growth rates in investment in production over 2001.

As concerns the structure of investment in the industrial sector, 53.3% falls on the fuel complex,

services provided by the noted sectors forms an indicator of growth economic potential. Furthermore in this sector the investment policy is aimed mostly at solving perspective problems. The infrastructure formed in the course of reforms proved to be fully engaged by market in the conditions of economic growth.

of which 34.8% on oil output. In 2001, there were 4,203 oil wells put into operation which made up a 18.6% increase compared with the prior year. In addition, the placement into operation of earlier idle wells allowed an additional output accounting for 5.7 mln.t. of oil, or 23.5% of the overall increment in the Russian oil output. When compared with 2000, the share of investment in the oil-refining industry grew by 2.2 per cent points. However, the proportion of allocation of investment between oil-extracting and oil refining subsectors have been changing in favor of the former ones. The more moderate dynamics of investment in the oil - refining sector this year has led to stavilization of the proportional weight of technologies of an intense oil refinery at the level of 2000.

Fig. Change in the structure of investment across industrial sub-sectors over 1998 to 2001, as % over the respective period.



The investment demand of 200-01 by its essence was fully generated by the oil industry, whose share in the overall volume of investment in the industrial sector accounted up to 30%. Though exporters have increased their investment expenditure on development of their profile production, however, they still are very cautious to invest the rest of their

available funds in the national economy, thus increasing the gap between themselves and the major part of the economy. Low investment activity in the processing sub-sectors have remained one of the factors inhibiting economic growth rates.

O. Izryadnova

Loan disbursement to the real sector in 2001

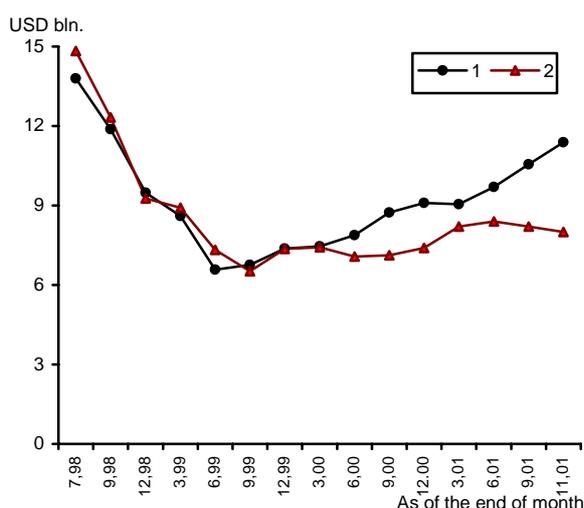
It was a relative rise in loan disbursement to the non-banking sector (NBS) that appeared the most notable positive shift in the trends of the national banking system's development over 2001. The growth in aggregate credit portfolio in constant prices accounted for 25.4 % over the 11 months of last year. That was less than in 2000 - 34.6%, however in 2001 the rise in loans disbursement to the real sector was taking place at a rate outrunning the overall growth in banks' assets. As a result, the share of loans disbursed among NBS grew from 40.8 as of early 2001 to 45.4% as of early December (the growth rate accounted for 11%). At the same time so far analysts' forecasts have not justified, as the share of outstanding loans in banks' credit portfolios has not experienced any notable

changes (3.0% as of early 2001 v. 2.9% as of early December). If we exclude Sberbank and banks run by ARKO, the trend to growth in the share of loans to NBS in assets would still be there – it accounted for 36.8% as of early 2001 and 42.7% as of early December (the growth rate accounting for 16%), while the share of outstanding loans in their overall amount disbursed to NBS accounted for 2.1% both as of early 2001 and early December 2001.

It is the rise in the share of Rb.-denominated loans which still appear a characteristic feature of the currency structure of the banks' credit portfolios. Given that as of early 2001 their share in loans to NBS accounted for 64.5%, it reached 68.1% in December (exclusive of Sberbank and banks run by ARKO – 58.7 and 61.5%,

respectively). At the same time changes in the correlation between Rb.-denominated loans and those denominated in foreign exchange were taking place against the backdrop of a vigorous expansion of the both kinds of loan disbursement. Given that over 2000 the rise in crediting in forex equivalent notably was lagging behind the growth in assets, over the 11 months of 2001 both indexes grew by 24%. While extending such loans, banks to a greater extent had to focus on domestic enterprises' and private individuals' resources (see Fig.1)

Fig.1 Russian banks' loans to enterprises-residents in forex equivalent and obligations to non-residents



1. loans to enterprises-residents
2. obligations to non-residents

Table 1. Time structure of loans to the non-banking sector*

Type of loans	Structure of loans to NBS, as a %		
	01.01.00	01.01.01	01.12.01
Loans to NBS for the term up to 90 days	17.8	16.9	20.0
Loans to NBS for the term between 90 to 180 days	10.8	15.7	15.3
Loans to NBS for the between 180 days and 1 year	33.2	34.4	35.0
Loans to NBS for the period over 1 year	38.2	33.0	29.6
Forex-denominated loans			
Loans to NBS for the term up to 90 days	9.5	8.0	10.1
Loans to NBS for the term between 90 to 180 days	9.0	8.4	11.8
Loans to NBS for the between 180 days and 1 year	25.1	28.1	30.5
Loans to NBS for the period over 1 year	56.3	55.4	47.6
Rb.-denominated loans			
Loans to NBS for the term up to 90 days	24.5	21.7	24.5
Loans to NBS for the term between 90 to 180 days	12.2	19.6	17.0
Loans to NBS for the between 180 days and 1 year	39.8	37.7	37.1
Loans to NBS for the period over 1 year	23.5	20.9	21.5

Non-outstanding loans without account of banks run by ARKO
Calculated on the basis of the data of CBR and STIiK company

The share of private individuals grew in the structure of borrowers: given that in 2000 the share of loans to private individuals was slightly over 5% of the overall amount of loans extended, by December 2001 it grew up to 7.6% (see Table 2). This was mostly thanks to Sberbank that increased

Given that on the eve of the 1998 crisis the overall volume of banks' obligations towards non-residents exceeded the volume of forex-denominated loans they disbursed among residents-non-banks, these indexes became equal by late 1999, while by late 2001 the banks' forex-denominated obligations towards non-residents accounted just for 70% of the volume of forex-denominated loans to residents-non-banks. In 2001 it was the growth in deposits with fixed period and primarily private individuals' deposits that formed the factors allowing the banking system to expand forex-denominated crediting. The amount of private individuals' deposits grew by over 47% in USD equivalent over the noted 11 months.

As far as the time structure of the Russian banks' aggregate credit portfolio is concerned, one could note a rise in the share of the most short-term loans at the expense of the fall in the share of loans extended for the term over 1 year. As it can be seen from the data of Table 1, such a trend formed primarily due to the decrease in the share of forex-denominated loans that banks extended for the term over 1 year. The provision of credits for the period under 3 months to a great extent expanded in the case of Rb.-denominated loans (the respective share of loans extended for the term under 3 months in the overall amount of Rb.-denominated loans grew from 21.7% to 24.5%). However, as long as the structure of forex-denominated loans is concerned, the share of short-term credits grew from 8.0 up to 10.1%.

the volume of credits to private individuals over 6.5 times over the 11 months 2001. At the same time the share of public enterprises fell notably (from 8.1% as of January 1, 2001, to 5.7% as of December 1, 2001). It is most likely that this trend should be regarded as a general result of

improvement of the state of public finance. In 2000, the government authorities' need in banking credits

fall drastically, while in 2001 the same was noted with regard to public enterprises.

Table 2. The structure of loans to NBS by counterparts

Type of loan	Structure of loans, as %*		
	01.01.00	01.01.01	01.12.01
Loans to budgets and extrabudgetary funds	5.8	1.7	1.2
Loans to enterprises	82.8	88.1	87.0
Including public	8.4	8.1	5.7
Non-governmental	74.4	80.0	81.3
Loans to enterprises-non-residents	6.1	5.0	4.2
Loans to private individuals	5.3	5.2	7.6

Note: exclusive of banks run by ARKO

*including outstanding loans

Calculated on the basis of the data of STIiK company

The advanced rise in credits to the non-banking sector was accompanied by a *relative decrease in the share of capital placed with the banking sector*. The share of funds placed in the banking sector in assets slid from 35.8% to 31.8% (from 43 to 39%, if without regard to Sberbank) over the 11 months. Such a decline mostly took place due to decrease in

the share of capital on corresponding accounts with CBR (from 5.9% as of early 2001 to 2.9% as of December 1). At the same time the share of funds placed with commercial banks experienced just insignificant changes – from 21.4% as of early 2001 to 20.7% as of early December.

L. Sycheva, L. Mikhailov, E. Timofeev

The real sector: factors and trends

In compliance with the Data Development and Presentation Procedures, the Goskomstat of RF has completed preliminary estimate of the nation's GDP for 2001 and specified the respective indicators over 1999 and 2000. The adjustment of GDP indicators was held on the basis of enterprises and organizations' annual reports, the account of the RF Ministry of Finance on execution of consolidated budget and the Balance of Payments developed by the Bank of Russia. The 1999 GDP changed by 0.2% relative to earlier available data, which did not impact the estimate of its dynamics over the prior year. It was the data on 2000 that became subject to specifications. The volume of GDP in 2000 accounted for Rb. 730.2, and considering the deflator index making up 140.5%

relative to the prices of 1999, the real increment in GDP accounts for 9.0% vs. earlier computed 8.3%. Proceeding from a new level of the base, the volume of Russia's GDP in 2001 was estimated at the level of Rb. 9,040.8 bln., which is substantially greater than the indicators that formed the basis of the 2001 budget. The rising activity of the domestic businesses allowed to assume that given other conditions equal, in 2001 the growth in GDP should account for 103 to 104%. However, a dynamic expansion of domestic demand ensured an additional impulse to the growth in the national economy. In 2001 the share of domestic demand in GDP grew up to 86.7% vs. 79.6% noted over the prior year.

Table 1 Change in dynamics of consumption of GDP across its components, as % to the prior year

	1998.	1999.	2000	2001
GDP	-4,9	5,4	9,0	5,0
Spending on final consumption by	-1,5	-2,4	7,4	6,2
households	-2,4	-4,4	9,3	8,7
Public institutions	0,6	3,0	1,4	-1,0
Gross savings	-28,7	8,5	31,9	17,0
Accumulation of capital assets	-11,2	2,4	15,0	6,5
Чистый экспорт	111,0	72,3	-6,2	-10,1
export	-0,3	9,4	8,7	2,0
import	-11,0	-15,6	12,7	8,6

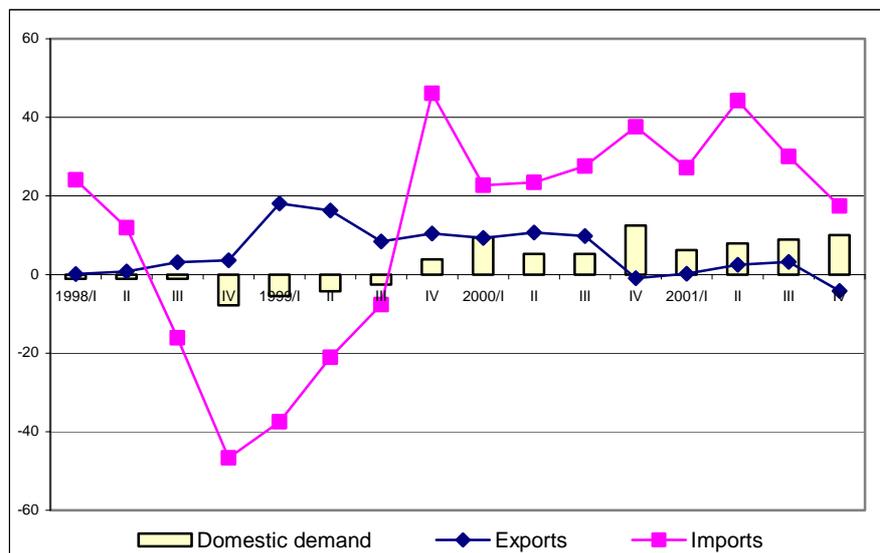
Source; the Ministry of Economic Development and Trade, the Customs Statistics of Foreign Trade of RF

The rise in revenues in the economy has had a substantial impact on proportions of final consumption in GDP. It was gross accumulation of capital assets that showed the highest growth rate compared with other noted components. With the

level of business activity in Russian economy growing, the rise in investment demand secured some ¼ of the increment in physical volume of GDP.

The growth potential accumulated via increase of business's income and vigorous investment activity allowed resolution of the earlier accumulated social problems. One can attribute almost 3/5 of the increment in GDP in 2001 to the rise in expenditure on final consumption. In 2001, with rather a regular trend to rise in salaries and wages, and pensions, the population's real incomes grew by 5.9%. The share of spending on final consumption grew by 3.7 per cent points vs. 2000, and this is fully related to the advanced rise in households' spending. It should be emphasized that the analysis of the national economy's development over the past decade shows that the volume of households' spending on final consumption has reached the level of the pre-reform 1991.

Fig. Change in dynamics of physical volume of exports, imports and domestic demand between 1998 through 2001, as % to the respective quarter of the prior year.



The analysis of the trade sector's development allows arguing that the national economy has not created new niches for the domestic products in the world and domestic markets. The expansion of domestic demand between 2000 through 2001 generated by the export-oriented sectors was ensured by the inertia-driven rise in output in rather a narrow segment of sectors.

As economic growth mostly was oriented to increase in the rate of utilization and introduction into production of spare production capacities, it formed one of the reasons for low competitiveness of domestic products. The absence of substantial shifts in regard to placement of new production capacities into operation practically did not allow

While analyzing the stability of the national economy's state, one should stress that the correlation of external factors influencing production rise over 2000 and 2001 appeared different. Given that in 2000 it was the price rise for energy sources and non-ferrous metals that formed the most important factor for production growth, in 2001 the effect of external factors was gradually weakening. Since 2000 the physical volume of imports has regain its advanced dynamics against dynamics of exports and GDP. The slowdown of the growth rate in physical volume of exports by late 2001 is explained by the situation in the world markets for minerals, while an intense rise in imports over 2001 was related to purely domestic problems.

the implementation of a consistent import-substitution policy and diversification of export flows. Since early 2000 the structure of commodity resources of consumer market and the market for material and technical products has demonstrated the intensification of the trend to growth in the share of imports. In addition, the latter was also encouraged by a real appreciation of the Rb. As a result, according to the RF Ministry for Economic development and trade, in 2001 next exports amounted to 89.1% of the prior year's level. It is a real alarm bell for the Russian economy, because the contraction in net exports, as role, leads to slowdown in economic growth pace.

O. Izryadnova.

The IET Industrial Survey: February 2002

Similar to February 2001, in February this year the national industrial sector experienced renewal of production growth, which has not been back-upped by a rise in sales as yet. All kinds of demand continue to fall, which led to growth in excessive stock of finished goods, drop in profits and purchases of equipment. Interestingly, the contraction of purchases of domestic equipment proved to be more intense than those of import one. For the first time since the 1st quarter 2001 enterprises have shared pessimistic mood with regard to their investment plans.

In February 2002 the sales of industrial products for cash continued to decline, though the decline rate was lower than in January. The respective balance grew by 13 points over the month, however remained negative i.e. reports on decrease in sales outran those on their growth. The decline in demand was noted in all the sectors, while it was most intense in the sectors for electricity and metallurgy. The non-cash kinds of demand (barter, promissory notes, and off-sets) lowered at a lower rate. So, for the third month in line the surveys registered decline in all kinds of demand in the national industrial sector.

Despite the continuous contraction in the volume of sales, last February showed production growth. After the January slump (the balance fell as low as -21%), the intensity of change in output became positive once again (+8%). Rise in output was registered in all the sectors, except the one for electricity and the light industry.

In February the Russian industry once again experienced excessive stocks of finished products. After some decline of the index in January, which could be attributed to hopes for an intense rise in demand between February through April, in the conditions of the continuous contraction in all kinds of demand and the beginning of production growth enterprises had to adjust their estimates. Their stock accounts for the same amount as in December 2001, while it was the forestry complex and food sector that reported shortages with regard to their stock.

The negative trends that manifested themselves clearly in the national industrial complex have determined decrease in real profits. According to enterprises' estimates, in February this index was falling in all the sectors, and most intensively – in the food sector and chemicals and petrochemicals. The analogous situation is noted with regard with purchases of machinery and equipment. Given that last year one noted prevalence of reports of growth

in such investment, in early 1992 enterprises clearly reported decrease in their purchases of both domestic and foreign equipment, while the contraction in purchases of the former proved to be more intense than the latter (-12% v. -3%). More accurate computations (at microlevel) show that the rise in purchases of import equipment with a simultaneous decrease of purchases of domestic equipment took place at 11% of enterprises, while the reverse situation was reported by 4% of enterprises.

The forecasts of change in output remained highly optimistic. All the sectors but electricity (due to seasonality) envisage rise in their output over the forthcoming months. It is the construction industry, chemicals and petrochemicals, and machine building that reported the most optimistic expectations. It was the prior actual changes in effective demand that appeared the factor determining shaping of enterprises' production plans over recent years. The enterprises are keen to extrapolate actual cash sales trends to their next production plans without account of changes in the volume of their barter, promissory note and off-set deals as well as previous changes of output itself. It means that the "planning from the reached level" has gone to the past.

For the first time since the 1st quarter 2001 (the beginning of monitoring of the respective index) enterprises' investment plans showed the prevalence of pessimism. Given that last year's survey registered just a decline in optimism (from +17 to +6%), in the 1st quarter 2002 enterprises mostly reported their plans to lower their purchases of both domestic and foreign equipment rather than their plans to increase such purchases (the balances of responses were -5% and -3%, respectively). Once again, the correlation was not in favor of the domestic investment sectors. At the same time microcomputations on vertex matrix of reports showed a rough parity of enterprises' plans. The supplanting of purchases of domestic equipment with foreign one in the 2nd quarter will be counterbalanced with a reverse process. However, the analysis of change in actual purchases in the 1st quarter and plans of their changes in the 2nd quarter once again are in favor of foreign equipment. After cutting down their purchases of domestic equipment in the 1st quarter 2002, over 20% of enterprises intend to increase their purchases of import equipment in the 2nd quarter, while the reverse intents are reported by 9% of enterprises.

So, the balance clearly is not in favor of import substitution.

According to Russian enterprises' estimates, in the 4th quarter 2001 they noted a fall in volumes of sales of both domestic and import goods on their markets. The most drastic fall in the volume of sales of Russian goods was noted on the sales markets of enterprises of the non-ferrous metallurgy and construction. It was only the forestry, food industry and machine engineering that reported rise in sales of domestic products. The volume of sales of import products on the market for domestic producers' sales was falling at a slower rate, with the most intense fall in sales of import products noted by chemical and petrochemical companies accounted for -11%. As well, the contraction of the volume of sales of import products took place on the markets for metallurgical and food products, while other sectors mostly reported the prevalence of rise in sales of import goods. According to heads of Russian enterprises, it is the light industry that experienced the most intense of increase in the volume of sales of import products (+8%).

The calculation indicators analogous to those we use to estimate interaction between effective and

non-cash kinds of demand allow a more accurate picture of the correlation between sales of domestic and import products. As long as various kinds of demand are concerned, we calculated the index of substitution for non-cash kinds of demand with effective one. Two new questions in our questionnaires allow to estimate import substitution itself in an analogous way. The computations testify that in the 4th quarter the process of import substitution was still there across the industrial sector on the whole. Over 12% of enterprises reported that on their sales markets sales of import goods decreased or remained unchanged under the rise in sales of domestic products, or they remained unchanged under the fall in sales of import goods. The substitution rate for domestic goods with import accounted for 9%. So, the overall balance ($9-12=-3$) was in favor of domestic producer. Let us note that at this point we considered both cases of a direct substitution for one producers by other ones and softer variants of rise in sales by a general expansion of demand. In the latter case sales of one group of producers were growing against the maintenance of other group's sales.

S. Tsoukhlo

Foreign trade

In December 2001 Russian exports fell by 3% compared with the prior months, while if compared with the respective period of the prior year the fall appeared dramatic - 20.2%, which became the most intense decline over the past 35 months. In December 2001 exports accounted for USD 103.04 bln. vs. 105.57 reported in December 2000.

In December 2001 imports made up USD 5.61 bln. vs. 5.07 bln. reported in November and 4.89 bln.- in December 2000. The import value noted in December 2001 appeared maximal since June 1998 (at that time, the respective index made up USD 5.7 bln.). By results of 2001 import accounted for USD 53.38 bln. vs. 43.86 bln. in 2000.

In December 2001 Russia's trade balance was USD 2.55 bln. vs. 3.34 bln. reported in November and 5.34 bln.- in December 2000. The trade balance reported in December 2001 appeared minimal since June 1999. So, Russia's 2001 trade balance made up USD 49.69 bln. vs. 61.71 bln. reported over 2000.

Russia's foreign trade indicators still remain strongly dependent on the situation in the world markets for minerals and change following world price fluctuations, mostly those of prices for energy sources. In December 2001 the world market for oil

and petroleum derivatives reached the bottom over the year, while the market for non-ferrous metals showed some renewal of activity. In late 2001 main producers of non-ferrous metals decided to decrease their output, and the prices for aluminum, copper and nickel started to rise.

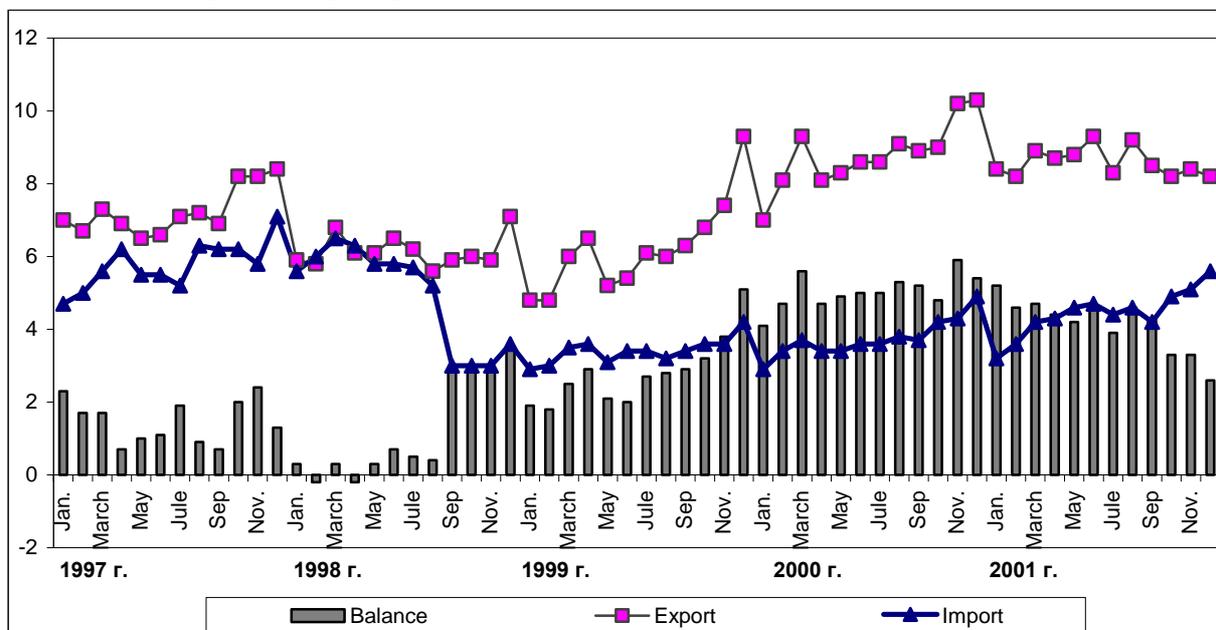
Russian import rises at a stable pace and reflects the growth in the population's real incomes and strengthening of a real exchange rate of the Rb., and the volume of imports practically has already reached the pre-default level. Most likely, the trend to growth in import would still be in place over the whole 2002, though the rate of this growth would drop due to a slowdown of the process of strengthening of the national currency's real exchange rate.

In December 2001 the volume of the trade between Russian and the CIS states accounted for USD 2.46 bln. Specifically, the volume of Russia's export stood at the level of USD 1.39 bln. and showed just an insignificant decline compared with the prior year- at 3.3%, while the drop in import supplies accounted for 21% vs. the noted period and totaled USD 1.07 bln. It was deep-frozen meat, grain crops, fuel and energy sources, and steel pipes that suffered the most notable fall. On February 22, 2002, the RF Customs Committee hosted the 15th Session

of the Council of Heads of customs agencies under the Integration Committee of the Eurasian Economic Community that unites Russia, Belarus, Kazakhstan, Kyrgyzia, and Tadjikistan. In 2001, Russia trade turnover with the above nations reached USD 14.3 bln. and accounted for 55% of the country's overall trade turnover with the Commonwealth states. The main efforts of the participants in the Session were

aimed at solving the problem of unification of national customs tariffs within the Integration Committee and at developing a single approach to exercising of customs control. By today the participants have already decided on unification of procedures of customs clearance of transit goods, customs accompanying, and transportation of goods by customs agents.

Fig.1 Main indices of Russia's foreign trade (as USD bln.)



Source: Goskomstat of RF

Table 1. The average world prices in November of the respective year

	1996	1997	1998	1999	2000	2001
Oil (Brent), USD/barrel	22,8	17,8	11,5	24,1	25,6	19,0
Gasoline, USD/gallon	3,093	2,393	2,251	2,558	8,713	2,694
Copper, USD/t	0,6691	0,5648	0,3739	0,6986	0,7649	0,5398
Aluminum, USD/t	2273,3	1834,7	1601,6	1748,1	1914,4	1528,7
Nickel, USD/t	1459,9	1535,45	1305	1470,7	1562,5	1346,3
Oil (Brent), USD/barrel	6920	6099	4202	7984,2	7315,4	5219,5

Sources: London Metal Exchange; International Oil Exchange (London).

In the course of the Session the parties agreed on a gradual transition to common measures on ensuring payments of customs duties that still are different due to substantial differences in national forex and tax regulation procedures. It was the problem of control over the customs value of transported goods that formed the hottest issue to debate on. In order to preclude an unjustified lowering of customs value of goods, the participants in the Session agreed that it would be expedient to form a single price information system between the countries-participants in the "Union of Five".

As for other documents considered and approved at the Session, it is worth noting such important ones as: the Action Plan on the reference data and software unification to ensure implementation of the Procedures of Declaration of Goods Transported via

External Borders of the Customs Union; a Draft Charter on the Union of Heads of Customs Agencies of the nations- members of the Union; a Draft Standard Bilateral Agreement between central customs bodies of the participants in the Union "On organization of information exchange on transportation of goods in the mutual trade".

Because of the deteriorating state of affairs in the world markets, the RF Government has had to work on lowering and cancellation of export duties. Specifically, effective as of February 5, 2002, the government set export customs duty rates for light and medium distillates and diesel fuel at the level of Euro 25 per 1000 kg. (earlier the rate was Euro 39).

In compliance with RF Government Resolution of January 14, 2002, # 17 "On non-exercising export customs duty rates to some goods", starting from

February 19, the customs authorities have not levied duties in the course of importation of some goods made from birch (until February 18 the respective rate was 5% of their customs value); paper and cardboard with the upper layer from or laminated with plastic, exclusive of adhesive substances (the previous rate was 10%), gold (5%); piezoelectric quartz (6.5%). Since February 1, 2002 oil and oil products from ... substances have become subject to export rate of USD 8 per 1000 kg. (until January 31, 2002 the rate was Euro 23.4/1000 kg).

At the same time, some export duties are regulative and levied to restrict exportation of some goods. Specifically, prohibitive rate have been set on export of leather, sunflower seeds, ferrous and non-ferrous scrap. Such duties may not be lowered.

In February 2002 Russia attempted to develop a new agreement on trade with steel with the EU. The document is to be signed shortly and should be effective over three years after that or until Russia's accession to WTO.

The term of the previous agreement expired on December 31, 2001, and since January 1, 2002 the steel trade between Russia and EU is based upon autonomous quotas the EC had introduced for the period of 6 months. Notably, the volume of the

Russian metal exports falling under the quotas is equal to the half volume of Russian steel export to the European market, though it was envisaged initially that the quotas would be equal to the actual export volume.

According to a new agreement in 2002 Russia should increase its steel export to the EU at 28% compared with the prior year, while in 2003 and 2004 the quotas on Russian steel supplies would be increased annually by another 2.5% vs. the prior year.

Should Russia cancel export duties on scrap (currently accounting for 15%), then the quotas would be raised by another 12%. The RF Ministry of Economic Development and Trade has developed a proposal on lowering the noted duties, however, they will not be canceled at all.

In addition, the agreement provides that in 2002 the supplies of born-alloyed steel should account for 90 Thos. t., they also should be subject to the above 2.5% annual increase. In 2001, when alloyed steel was not included in the above Agreement, according to different estimates, Russian producers supplied to EU countries 200 to 300 Thos. t. of this product.

N. Volovik, N. Leonova.

Military Expenditures of Russia in 2002

The results of the analysis of Russia's military expenditures offered here continue the informational and analytical activities in this field the IET experts began a year ago. It shall be reminded that military-related economic problems were not subject of monthly IET publications until year 2001.

On the whole, it shall be noted that the justification of the amount and distribution of Russia's military expenditures for year 2002 was mainly based on the successful administration of the preceding year 2001. The target military expenditures were practically financed in full. There was liquidated a considerable portion of the state debts to the military organization accumulated over preceding years. At the same time, a number of promises given by the RF governments was not met, including those related to the increase in military salaries.

However, in case we review not only the financial side, but also the results of expenditures and the general efficiency of the economy related to the military security, it remains low. We understand this "branch" of economy as a system, which, utilizing a part of the budget, renders to the public, the society, and the state the most important service

– military security. There are no grounds to consider that the situation related to the provision of this service could be rid of problems. The counter-terrorist operation in Chechnya is far from being completed. The preparedness of the considerable part of troops (forces) can not be regarded even as satisfactory. The social status of servicemen continues to fall. The process of recruitment in the military organization faces considerable problems, while its provision with weapon systems meeting the standards of the 21st century is postponed for an indefinite future.

Other results of the military related economic activities in the RF also do not provide grounds of optimism. Considerable revenues derived from export sales of military equipment, technologies, and services, traditionally calculated in terms of "currency proceeds" still is not compared with the production costs related to these goods, moreover, these revenues are "split up" among middlemen and non-state joint stock companies belonging to MIC. Even auditors of the Accounting Chamber fail to identify the budgetary revenues related to these proceeds. The rendering of a number of other services (with the exception of military security), which may be clearly measured in economic terms,

is organized slower than it would be desirable. Mass media noted some negative facts related to fishery violations in the Russia's territorial waters and unlawful exports (jurisdiction of the Border Guards), national communications and informational security (Federal Agency for Government Communications and Information - FAGCI). There were also detected violations committed with the participation of the military components in economic activities, for instance, with regard to the construction and guarding of federal roads, freight of non-military cargoes carried out by the military transport aviation. Such economic activities as transfer of certain military technologies to civilian industries, sales and

utilization of surplus military equipment, etc. also failed to bring expected results in terms of economic effectiveness.

The definition of military expenditures for year 2002 analyzed below remains the same:

1. Expenditures related to the national military preparations, in general corresponding to the standard UN accounting.

Expenditures, sometimes defined as indirect expenditures, which are related to previous military activities of the state (military pensions, conversion of defense enterprises, utilization and liquidation of armaments, outlays for the military reform, etc.).

Table 1. Military Expenditures of the RF Military Organization in 2002

Item#	Expenditure	S(SS)/TEI/TE Codes	Agency Code	Amount Rub. mil	% of the RFB	% of GDP	Source of information
01	EXPENDITURES FOR "NATIONAL DEFENSE"	0400		284158	14,59	2,6	Sup. 5 FB
1	<i>Military expenditures for the military organization included in the expenditures for "national defense," including::</i>	0400		270697	13,9	2,47	Sum of lines 1.1, 1.2, 1.3
1.1	Development and maintenance of RF AF	0401		263864	13,55	2,41	
1.2	Ensuring of mobilization and extra-military preparations, including the expenditures for:	0403		3270	0,17	0,03	Sup. 5 FB
	Federal Railroad Troops Service		029	2395	0,12	0,02	Sup. 6 FB
1.3	Preparation for and participation in collective security and peacekeeping operations	0404		2728	0,14	0,02	Sup. 5 FB
02	EXPENDITURES FOR "LAW ENFORCEMENT AND NATIONAL SECURITY"	0500		173863	8,93	1,59	Sup. 5 FB
2	<i>Military expenditures for the military organization included in the expenditures for "law enforcement and national security" item, Including:</i>	0500		62972	3,23	0,58	Sum of lines 2.1, 2.2, 2.3)
2.1	Troops of RF Interior Ministry	0502	188	13571	0,7	0,12	Sup. 6 FB
2.2	State security agencies*	0505	189	31813	1,63	0,29	Sup. 6 FB
2.3	Border guard service agencies	0506	191	17588	0,9	0,16	Sup. 6 FB
3	<i>Other expenditures for the military organization</i>			4392	0,23	0,04	Sum of lines 3.1, 3.2, 3.3
3.1	Maintenance of special construction service, including:	0710		654	0,03	0,01	Sup. 5 FB
	Federal Special Construction Service		279	654	0,03	0,01	Sup. 6 FB
3.2	Maintenance and equipment of MES troops Including	1302	177	3716	0,19	0,03	Sum of lines a - e
a	Maintenance of personnel of troops (forces)	1302/601	177	1982	0,1	0,02	Sup. 6 FB
b	Combat training and material and technical maintenance of troops (forces)	1302/602	177	898	0,05	0,01	Sup. 6 FB
c	Procurement of VVT, PTN, and other stocks	1302/603	177	740	0,04	0,01	Sup. 6 FB
d	Repairs of VVT, PTN, and other stocks at enterprises	1302/604	177	71	0	0	Sup. 6 FB
e	Insurance guarantees for servicemen	1302/607	177	25	0	0	Sup. 6 FB
3.3	Civil defense	1303	177	22	0	0	Sup. 6 FB
4	TOTAL: general military expenditures of the RF military organization			338061	17,36	3,09	Sum of lines 1, 2, and 3

Note:

* It is assumed that the amount shown in item 2.2 includes the expenditures for the maintenance of agencies of the Federal Security Service (FSS), Foreign Intelligence Service (FIS), and some other structures ensuring RF national security.

Abbreviations: S – FB section; SS – subsection; TEI – targeted expenditure item; TE – type of expenditure; EFB – general amount of FB expenditures; Sup. – supplements to the law on FB.

Table 2. Military Expenditures outside of the Military Organization

Item#	Expenditure	S(SS)/TEI/T E Codes	Agency Code	Amount Rub. mil	% of the RFB	% of GDP	Source of information
<i>Contained in "National Defense" item (see line 01, Table 1)</i>							
1	Military program of Atomic Energy Ministry	0402		13994	0,72	0,13	Sup. 5 FB
2	Russian Defense Sports and Technical Organization (RDSTO)	0403	464	40	0	0	Sup. 6 FB
3	Ensuring of industries' activities for the national defense: Ministry of Industry, Science, and Technologies	0407	139	303	0,02	0	Sup. 6 FB
<i>Contained in other sections and subsections of FB</i>							
4	Mobilization preparedness of the economy	2300	-	500	0,03	0	Sup. 5 FB
5	Grants and subsidies to CATE budgets including:	2101/485		11 219	0,58	0,1	Sup. 6, 19 FB
a	Grants and subsidies to CATE budgets	*/*/350	092	10544	0,54	0,1	Sum of lines a-c Sup. 6,19 FB
b	Grants and subsidies for the maintenance of Baikonur town infrastructure	*/*/361	092	675	0,03	0,01	Sup. 6,19 FB
c	Grants for CATE budgets for financing CATE development programs	*/*/454	092	1000	0,05	0,01	Sup. 6,19 FB
6	TOTAL: general military expenditures outside the RF military organization			15067	0,77	0,14	Sum of lines 1-5

Note: a part of the expenditures shown in the table may hardly be identified as the military expenditures (for instance, the expenditures for the maintenance of Baikonur's infrastructure, since the population of the town mainly services commercial and national economy-related launches of cosmic vehicles.

Table 3. Expenditures Related to Previous Military Activities

Item#	Expenditure	S(SS)/TEI/T E Codes	Agency Code	Amount Rub. mil	% of the RFB	% of GDP	Source of information
1	Military pensions, including:	1804		40274	2,07	0,37	Sup. 5 FB
	- paid via the Defense Ministry		187	37291	1,91	0,34	Sup. 6 FB
	- paid via the Finance Ministry		092	2983	0,15	0,03	Sup. 6 FB
2	Pensions paid to servicemen of law enforcement agencies, including:	1805		18562	0,95	0,17	Sum of lines a - d
a	- paid via the Interior Ministry	*/447/326	188	12791	0,66	0,12	Sup. 6 FB
b	- paid via the FSS	*/447/326	189	4514	0,23	0,04	Sup. 6 FB
c	- paid via the Federal Tax Police Service	*/447/326	205	472	0,02	0	Sup. 6 FB
d	- paid via the Ministry of Justice	*/447/326	318	785	0,04	0,01	Sup. 6 FB
3	Utilization and liquidation of armaments	2200	-	10315	0,53	0,09	Sup. 5 FB
4	Conversion of the defense industry: Ministry of Industry, Science, and Technologies	0704	139	250	0,01	0	Sup. 5,6 FB
5	Implementation of the military reform, including:	2500		16545	0,85	0,15	Sup. 5 FB
	- via MES	2501/611	177	103	0,01	0	Sup. 6 FB
	- via the Defense Ministry	2501/611	187	14997	0,77	0,14	Sup. 6 FB
	- via the Interior Ministry	2501/611	188	916	0,05	0,01	Sup. 6 FB
	- via the FBS	2501/611	191	529	0,03	0	Sup. 6 FB
6	Program "State Housing Certificates (1998 – 2002)" In the framework of FTP "Housing" for 2002 – 2010	0707/ 633/758	092	5400	0,28	0,05	Sup. 6 FB
7	TOTAL: Expenditures related to the previous military activities of the RF			91346	4,69	0,83	Sum of lines 1-6

It shall be also noted that at present the RF military organization includes the following components: RF Armed Forces, other troops (border guards, Ministry of Interior troops, railroad troops, troops of the government communications and information agency, civil defense troops), military units (engineering technical troops and road construction troops), and agencies (Foreign Intelligence Service, security services, border guards, agencies for governmental communications and information, Federal Protection Service, Federal agency for ensuring mobilization preparedness). The structure of the RF military organization has not been finalized.

While analyzing the information on the RF military expenditures, the following shall be

remembered: in case of good organization of economic relations between the components of the military organization and other RF economic agents these expenditures are not the simple "deduction" from state revenues as some economists see this. It is also obvious that information about Russia's military expenditure may be of considerable interest for many subjects of the Russia's multifaceted economy, especially at the time of growth. It shall be noted that announcements about tenders and auctions for goods and services are regularly published in the "Krasnaya Zvezda" newspaper.

The data presented below were derived from the Federal budget for year 2002 (FB 2002) and structured across the budget recipients, which include, first, components of the **RF military**

organization (the Defense Ministry and subordinated to it Armed Forces (AF), and other ministries and agencies disposing of troops, military units, and agencies. Second, a part of RF military expenditures is directly disposed of by certain **non-military agencies and organizations**.

It shall be noted that the repayment of the state debt related to the defense state procurement order fulfilled up to year 2000 is also linked to the previous military activities of the RF. This debt,

Table 4. Aggregate Indicators of Military and Military-Related Expenditures of the Federal Budget for Year 2002

Item #	Expenditure	Amount, Rub. mil.	% of the RFB	% of GDP
1	General military expenditures (for the military organization and other related items) (the sum of line 4 of Table 1 and line 6 of Table 2)	353128	18,13	3,22
2	The amount of total military expenditures and expenditures related to the previous military activities of RF (the sum of line 1 of this Table and line 7 of Table 3)	444474	22,82	4,06
3	Aggregate expenditures for "national defense" and "law enforcement and national security" (the sum of lines 01 and 02 of Table 1)	458021	23,52	4,18

Therefore, the total military funds to be received by the financial agencies of the RF military organization in year 2002 in accordance with the budget for this year make more than 17 per cent of the expenditure items of the federal budgets, what makes it feasible for Russia's enterprises interested in profitable (and, after 2000, stable) orders to cooperate with the military. It shall be noted that the share of military expenditures due to the RF military organization in year 2002 was below the figures registered in the preceding year, when it was at 22 per cent of the federal budget expenditures.

The total military expenditures outside the RF military organization are much less significant.

The amount of total expenditures for national defense, law enforcement, and national security shown in item 3 of the last table are illustrative in terms of characterization of the expenditure level in year 2002 (4.18 per cent of GDP) as compared with

which (by estimates) exceeds Rub. 16 billion, was restructured and should be repaid before January 1, 2003 (as stipulated by the RF Government Decision No. 1020, of 29.12.00, "On the Repayment of Indebtedness Related to the State Defense Procurement Order"). However, the federal budget for year 2002 fails to clearly identify these expenditures and therefore they are excluded from the calculation of aggregate expenditures.

the conventional standard approved by the RF President in 1998 (5.1 per cent of GDP). Moreover, this level is not only below the "standard" level, but also below the level of the preceding year, when it was at 4.47 per cent.

The situation is similar for the evaluation of expenditures for national defense. The standard expenditure level was set at 3.5 per cent of GDP, i.e. considerably above the present 2.6 per cent. It shall be also noted that the present level is below the level registered in the preceding year (2.77 per cent of GDP).

The meagerness of RF military expenditures, moreover the fact that they are falling at the background of real military threats is in striking contrast with military preparations of a number of other countries, first of all, the USA. However, it is the subject of another analysis.

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