

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
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May of 2004: Political and economic outcomes

May witnessed a large number of events of national importance. However, it is difficult to single out the key event from the range including the annual address of the RF President to the chambers of the Federal Assembly, reappointment of the Government after the inauguration of the incumbent RF President as required by the RF Constitution and the respective reshuffling of the Cabinet, murder of the Chechen President A. Kadyrov, the decision of the Moscow Arbitration Court to exact US \$ 3.5 billion from the OAO NK YUKOS as repayment of the allegedly due taxes for year 2000, and a relative success of negotiations between Russia and the European Union concerning the support of the Russia's accession to WTO.

The address of the RF President to the Federal Assembly was the least interesting among the events listed above. According to V. Putin, "Our objectives are quite clear. They include high national living standards, safe, free, and comfortable life. They include developed democracy and developed civil society. They include consolidation of Russia's positions in the world. And, I repeat, the key objective is a significant increase in the welfare of citizens."

The address declared in general terms that human capital is the base for the development of the competitive capacity and the improvement of the quality of this capital "requires the settlement of the most urgent for the citizens problems in the country. These problems primarily include the quality and availability of housing, education, health care." It was promised that by 2010, alongside with the doubling of GDP, at least one third of the citizens would be able to purchase housing at the expense of their own savings and housing credits. Among the instruments required to achieve this goal there were named the elimination of the monopoly on construction markets and simplification of procedures governing construction.

The RF President noted the poor quality of the Russian health care system, low life span, and high rates of infant mortality. He advanced the slogan of "accessibility and quality of health care for broad strata of the population." According to V. Putin, in order to achieve these goals it is necessary to approve the standards of health care for each type of disease, what could permit to assess the actual costs of medical treatment and transit from budget financing of medical institutions to the payment for rendered services. However, the address fails to answer the key question: who should be the administrator of the mandatory medical insurance funds – insurance companies or medical institutions.

The President also believes that it is necessary to make higher education available for all and to create a transparent system allowing to evaluate the quality of school education. However, the address did not directly mentioned the problem of the single state examination. Therefore, there were not indicated concrete ways out of the present situation, where higher education establishments are free to recognize or reject the general system of testing. At the same time, President Putin advanced an original idea that students should make special agreements according to which they should either work according to their specialization for a certain term (in the public or private sector?! *S. Zh.*) or return the money spent for their education.

As concerns taxes, the address mentions that they should present no heavy burden on businesses. It should concern not only the levels of tax rates, but also procedures governing calculation and payment of taxes, streamlining of tax inspections and tax relating accounting. The address put forward the task of reduction of the single social tax and its withdrawal from wages and salaries, a further reduction of VAT and timely compensation of VAT relating to export operations and capital investment, it was also proposed to exempt advance payments from taxation.

The address sets forth the task to settle the problems encountered in creation of the transport infrastructure, transport networks, primarily as concerns transportation of energy resources. However, the address fails to mention what the state should do in order to create respective incentives for businesses in the case it is determined to keep state monopoly for pipelines.

The President again addressed the military reform, however, there were made no new proposals concerning this issue. However, this section of the address may be positively assessed, since it demonstrates that the top leadership of the country has not agreed to the ideas of general conscription advocated by certain officials (V. Filippov, V. Putilin and others).

However, the address fails to mention rights and liberties, inviolability of private property, equality of citizens before the law, the rule of law principle, independence of the judiciary system and mass media, destruction of the institution of elections, Chechnya, and so on. Instead, V. Putin addressed the issue of non-state sources of citizens' incomes, in particular, the organizations, whose "priority became to receive financing from influential foreign foundations and ... servicing of dubious groupings and commercial interests." It is

proposed to interpret any reproaches concerning the political system of Russia as manifestations of the “global competition struggle.” It should be also noted that in this address the usual package of difficult tasks and objectives is supplemented by the tasks absent in the real politics.

In May, there was published the Presidential decree “The issues pertaining to the structure of the federal executive authorities.” It should be reminded that according to the structure of the Government established in March, ministries were vested with normative and legal regulation, services were vested with supervisory functions, while agencies rendered services on behalf of the state. However, observers, first, noted that the mixing of supervision and control was wrong (since control, licensing, registration are in practice regulation), and, second, criticized the subjecting of agencies and services to the ministries. According to the new decree, federal executive authorities controlled by the RF Government should perform the functions relating to approval of normative and legal acts alongside with other functions. It is difficult to comment on changes which occurred over the two months in the framework of the administrative reform and in the framework of other paradigms. In fact this means that minimum eight services and agencies can, as before, issue any instructions.

As it was forecasted, the re-division of the spheres of influence in the Government continued. This time, in accordance with the new Presidential decree the services responsible for technological and atomic supervision, the federal tariff service, the federal space agency and the federal agency for atomic energy, as well as a number of less important services were subjected directly to the Prime Minister. There was reestablished the Ministry for communications and information technologies headed as before by L. Reiman (who was initially appointed as a deputy minister of transport and communications). The issues concerning the status and control over former State Customs Committee, Tax Ministry, and RFFI remain unresolved, since it requires amendments to the legislation.

The RF Government approved the draft law “On the accrual mortgage system of insurance of servicemen” (the draft law envisages the purchase of housing on installment basis, the state guarantees of bank credits, the contracts made for 20 years). However, the proposals of the Ministry for Economic Development concerning reduction of licensing and introduction instead of other types of control gave rise to disputes (the Ministry of Economic Development proposed to abolish more than 50 types of licensing). The question was not settled and the proposals were returned for further elaboration, however, the Ministers responsible for coordination of this work most actively protested against the reduction of licensing (S. Shoigu, the Minister for Emergencies, and V. Khristenko, the Minister of Industry and Power Engineering).

In May, M. Fradkov, the Prime Minister, declared new changes in the plans of the pension reform. Initially, it was envisaged that all citizens born after 1957 should be entitled to participate in the formation of the cumulative part of the pension. Later, due to the decision of the Government to reduce the single social tax in 2005, it was proposed to exclude citizens born before 1967 from the cumulative system in order to compensate for the revenues generated by the SST. The Government recommended citizens to accumulate pension savings on their own by making voluntary transfers of 4 per cent of wages and salaries to the cumulative segment of the pension. The Government promised to pay additional 2 per cent of wages and salaries (however, no more that Rub. 2 thousand) on behalf of such citizens. According to M. Fradkov’s statement, there should be taken balanced decisions aimed at improvement of pensioners’ living standards. However, according to the Prime Minister, it seems that the citizens born before 1967, who were initially included in the cumulative pension system and later excluded from it, may be entitled to participate in this system again.

On the whole, the new debates and significant reshuffling of the Government occurring only 2 months after its formation indicate that the Fradkov’s Cabinet is far from reaching internal unity and conceptual clarity.

On May 9 of 2004, A. Kadyrov, the President of the Chechen Republic died in the result of a terrorist attack. Kadyrov was an influential figure in the Republic, he disposed of his own military and financial resources. The successful attack clearly demonstrated that the situation in the Republic is far from stabilization even after four years of the “antiterrorist operation” and there arise new problems. The system of government in the Chechen Republic has been often changed in the period from the aggression against Dagestan and the peak of terrorist activities in 1999. However, no changes could create a clear and responsible government. In the civilian sphere the responsibility was divided among the Kadyrov administration and the Chechen Government consequently headed by non-Chechens, and numerous federal agencies and commissions for restoration of the Chechen economy. As concerns the military sphere, there the responsibility was divided among the 58th Army of the RF Defense Ministry controlled by the Staff for antiterrorist operation in Chechnya (in fact, FSB), special military units, the system of VOVD (formed from servicemen out of other regions), and

“Chechen” units, such as the Security Service of the President of the Chechen Republic (special brigades “East” and “West,” the Chechen Interior Ministry and other paramilitary units). By 2004, Kadyrov could form a semblance of hierarchy of Chechen authorities (the Moscow oriented Chechen leaders were expelled). However, the complicated system of military command remained. After his death, there is still no equal leader, since his relatives have no comparable authority and there may be expected conflicts between representatives of the pro-Moscow administration (expelled earlier) and local Chechen leaders. Naturally, this situation is favorable for Islamic extremism and separatism. For the time being, there was chosen the variant where Kadyrov’s son was appointed as the first vice prime minister of the Chechen government in stead of running for Chechen Presidency, what seems a good option. However, the issue of the real successor and the policy this successor would pursue remains open.

The Moscow Arbitration Court made an unprecedented decision to exact US \$ 3.4 billion in taxes, allegedly not paid by YUKOS (due to application of tax optimization schemes). Earlier, the Tax Ministry filed the respective claim with the Moscow City Arbitration Court, which arrested all YUKOS assets with the exception of oil and oil products in order to secure the claim. The RF Tax Ministry declared that YUKOS evaded taxes by creating 17 “fictitious” firms in regions with favorable tax regimes (Mordovia, Kalmykia, and the Evenk autonomous okrug). YUKOS allegedly carried its oil transactions via these companies and a number of closed administrative territorial entities. At the same time, it should be noted that the Russian legislation does not define the term “fictitious legal entity” and sets forth no applicable criteria.

Certain experts believe that finally there will be found a compromise which could settle the conflict by the way of negotiations and help both YUKOS and the state to “save face”. One of such ways may be participation in the announced competition for the improvement of the a new tax system. However, it seems that the Russian authorities on the contrary aim at the liquidation of the judiciary system and creation of a precedent allowing to expropriate businesses without any formal justification.

At the congress of the Agrarian Party held in April of 2004, M. Lapshin, the head of the Republic of Altai and the party leader was dismissed and at this post was appointed V. Plotnikov, a former member of the KPRF deputy group in the State Duma, presently a member of the United Russia party. G. Semigin, one of the most important sponsor of Communists, who expected to be nominated as the Communist candidate for Presidency, was expelled from the party on formal grounds (failed to register at this local party organization). The KPRF leadership disposed of a dangerous contender, who could attract support of almost half of the deputies of the last congress. However, Semigin took a strange position as concerns the personal composition of his organization “Patriots of Russia,” since it lacks the potential to become a serious party and is only one of the splinters of the Communist opposition alongside with agrarians, supporters of G. Seleznev, the Party of Social Justice, etc.

The negotiations between the RF Minister of Economic Development G. Gref and the EU trade commissioner P. Lami were unexpectedly short, however, there was signed a protocol determining the conditions on which European companies received access to the Russian markets of goods and services.

One of the key issues of the negotiations were Russian obligations relating to the “energy package”. EU recalled the majority of its initial requirements (abolishment of export duties on energy resources and the export monopoly of Gazprom, access of foreign companies to construction of Russian gas pipelines, increase in the domestic prices of natural gas, etc.). The signed protocol contains obligations to include in the domestic prices of natural gas all costs borne by natural gas extracting companies, including the investment component (however, this issue was not clarified, for instance the controversy about the growing debt of Gazprom remained open), as well as promise to refrain from increases in the export duties. Experts believe that the informal part of negotiation included Russia’s obligations to increase domestic prices of natural gas over US \$ 50 per 1000 cubic meters, i.e. 1.5 times. In its turn, EU recalled its demand to lift the ban on establishment of EU banks branches in Russia and abolishment of the restrictions on their participation in the aggregate capital of the Russian banking system.

Among the concessions of the Russian party of negotiations were the decrease in the import tariffs on civil aircraft, completing parts, and motor vehicles, abolishment of the Rostelekom monopoly for long distance communications, the promise to review the system of fees relating to EU companies as concerns trans-Siberian flights, as well as President Putin’s statement that “EU made a concession to Russia by signing the WTO protocol,” therefore Russia “will accelerate ratification of the Kyoto protocol.” Nor Russia, neither the USA have ratified the Kyoto protocol yet.

The agreement between Russia and EU is a significant step on the path of the Russia’s accession to WTO. It should be reminded that the negotiations took six years. However, this process is far from completion:

there are expected difficult negotiations with, for instance, China and Australia, while the EU – Russia protocol is only a framework agreement. However, the recall of absurd requirements that Russia should increase its domestic prices of certain commodity groups up to the “world” level is a significant success of the Russian external economic policy.

S. Zhavoronkov

On the Progress of Reforms in May of 2004

Russia has a new government again; the structure of state authorities has undergone certain changes. As concerns the progress of reforms over the month, there has been done practically nothing due both to the long May holidays (practically, 10 days this year), and changes in the Government. As concerns “national projects”, after reviewing the package of laws regulating health care and housing the Government started to discuss the package of regulatory and legislative acts aimed at creation of the cumulative mortgage system for servicemen of the Armed Forces. The draft law “On special economic zones” was once again removed from the agenda of the next Government meeting.

As concerns the social and economic policies pursued by the Government (or, more precisely, the lack thereof), the situation observed in May practically mirrored the situation in March and April. Objective factors had an additional negative impact on the rate of reform progress, such as ten days long holidays (as concerns the state authorities, although formally all ministries and departments should function between holidays, in practice there was done nothing over that time). The organizational restructuring in the ministries and departments relating to the redistribution of functions and personal changes continued.

In May, according to the RF Constitution, there was appointed the new Government of the Russian Federation. As expected, its composition remained the same as in March with one exception. The personal composition of Ministers now includes L. Reiman, who could insist on the separation of the Ministry of Communications from the Ministry of Transport and Communications, which had been created earlier. The very fact that lobbyist efforts of certain groups in the RF Government and the Presidential Administration could infringe upon the seemingly strict principles of the administrative reform raise certain doubts as concerns the further progress of the administrative reform.

In fact, the present situation is practically similar to that existing in the Government prior to the start of the administrative reform with the exception of the strictly enforced, although doubtful in terms of management, principle that each Minister should have no more than two deputies.

Until now, the administrative reform, which as it was hoped should serve as the most effective incentive for the “reanimation” of reforms, has brought no other results as turmoil and loss of most qualified and professional personnel at the medium level of government.

As concerns social and economic reforms *per se*, practically nothing was done in May. The only exception was the successful discussion of the package of regulatory and legislative acts aimed at creation of the cumulative mortgage system for servicemen of the Armed Forces worked out by the “Shuvalov group” at the Center for Strategic Research. The most important law underlying this system has all chances to be soon adopted by the State Duma, especially taking into account the consideration that the President has already indicated his approval of the principles underlying this law..

May can be also considered as the next qualitative stage of struggle between the Ministry of Economic Development and Trade and the Finance Ministry with respect to the issue of the law on free economic zones. The draft was set for discussion at the Government meeting scheduled for May 20, however, the discussion again did not take place. The reason of this was the letter of the Finance Ministry to the Government, which stated that although the Ministry acknowledged the approval of all amendments to the text it introduced, it was categorically against the approval of this law because of its principal considerations.

The situation seems to be insoluble: in its turn, the Ministry of Economic Development sent a letter to the Government informing it about the necessity to have a conciliatory meeting with participation of the Vice Prime Minister as concerns this issue. Taking into account the position taken by Zhukov (at present it is closer to the position of the Finance Ministry), it is very difficult to forecast the further development of the situation.

O. Fomichev

The State of the Federal Budget

In January through February of 2004, the revenues of the federal budget (cash execution) made 19.7 per cent of GDP, while expenditures made 15.8 per cent of GDP (see Table 1). Therefore, the federal budget surplus made 3.8 per cent of GDP.

Table 1

The monthly execution of the federal budget of the Russian Federation (in % of GDP¹, cash execution)

| | II'03 | III'03 | IV'03 | V'03 | VI'03 | VII'03 | VIII'03 | IX'03 | X'03 | XI'03 | XII'03 | I'04 | II'04 | III'04 |
|---|-------|--------|-------|-------|-------|--------|---------|-------|-------|-------|--------|-------|-------|--------|
| Revenues | | | | | | | | | | | | | | |
| Profits tax | 1.1% | 1.4% | 1.5% | 1.4% | 1.4% | 1.4% | 1.3% | 1.3% | 1.3% | 1.3% | 1.3% | 0.9% | 0.7% | 1.2% |
| 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) | 2.7% | 2.8% | 2.9% | 2.9% | 2.8% | 2.8% | 2.8% | 2.7% | 2.7% | 2.6% | 2.7% | 2.3% | 2.6% | 2.8% |
| Indirect taxes | 10.1% | 9.9% | 9.6% | 9.6% | 9.2% | 9.1% | 8.9% | 8.7% | 8.6% | 8.5% | 8.5% | 10.5% | 8.5% | 7.6% |
| VAT | 7.4% | 7.2% | 7.2% | 7.2% | 6.9% | 6.9% | 6.8% | 6.7% | 6.6% | 6.6% | 6.6% | 8.1% | 6.6% | 6.2% |
| Excises | 2.7% | 2.6% | 2.4% | 2.3% | 2.2% | 2.2% | 2.1% | 1.9% | 1.9% | 1.9% | 1.9% | 2.3% | 1.8% | 1.4% |
| Taxes on foreign trade and foreign economic transaction | 3.4% | 3.4% | 3.5% | 3.5% | 3.4% | 3.4% | 3.4% | 3.3% | 3.3% | 3.4% | 3.4% | 3.6% | 4.2% | 4.4% |
| Other taxes, fees and levies | 1.7% | 2.0% | 2.2% | 2.1% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.5% | 0.1% | -0.2% |
| Total taxes and other payments ** | 19.0% | 19.4% | 19.6% | 19.4% | 18.8% | 18.7% | 18.4% | 17.9% | 17.9% | 17.9% | 18.0% | 19.9% | 16.1% | 15.9% |
| Non-tax revenues | 8.5% | 1.3% | 1.2% | 1.7% | 1.6% | 1.5% | 1.5% | 1.4% | 1.4% | 1.3% | 1.3% | 0.9% | 0.8% | 0.9% |
| Total revenues | 20.6% | 20.9% | 21.0% | 21.3% | 20.6% | 20.4% | 20.0% | 19.5% | 19.4% | 19.3% | 19.4% | 20.9% | 19.6% | 19.7% |
| Expenditures | | | | | | | | | | | | | | |
| State administration | 0.3% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.5% | 0.2% | 0.3% | 0.4% |
| National defense | 2.1% | 2.6% | 2.7% | 2.7% | 2.6% | 2.6% | 2.6% | 2.5% | 2.5% | 2.5% | 2.7% | 1.8% | 2.2% | 2.6% |
| International activity | 0.0% | 0.2% | 0.2% | 0.3% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | -0.1% | 0.2% | 0.2% |
| Judicial authorities | 0.1% | 0.1% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.1% | 0.1% | 0.2% |
| Legal protection and security | 1.4% | 1.7% | 1.7% | 1.7% | 1.8% | 1.7% | 1.7% | 1.7% | 1.7% | 1.7% | 1.9% | 1.1% | 1.5% | 1.7% |
| Fundamental research | 0.2% | 0.2% | 0.2% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.1% | 0.1% | 0.2% |
| Services to national economy | 0.4% | 0.5% | 0.6% | 0.7% | 0.8% | 0.8% | 0.8% | 0.9% | 0.9% | 0.9% | 1.1% | 0.2% | 0.4% | 0.5% |
| Social services | 1.8% | 2.0% | 2.3% | 2.2% | 2.2% | 2.2% | 2.2% | 2.1% | 2.1% | 2.1% | 2.3% | 1.4% | 1.7% | 1.9% |
| Government debt servicing | 2.9% | 3.0% | 2.3% | 2.1% | 2.0% | 1.8% | 2.0% | 2.0% | 1.8% | 1.7% | 1.7% | 1.1% | 2.1% | 2.2% |
| Other expenditures | 7.1% | 7.0% | 7.0% | 7.1% | 7.1% | 7.1% | 7.0% | 6.9% | 6.8% | 6.8% | 6.9% | 5.3% | 5.8% | 5.9% |
| Total expenditures | 16.4% | 17.7% | 17.7% | 17.7% | 17.5% | 17.4% | 17.3% | 17.1% | 16.8% | 16.7% | 17.7% | 11.1% | 14.4% | 15.8% |
| Surplus (+) / deficit (-) | 4.2% | 3.2% | 3.3% | 3.6% | 3.0% | 3.0% | 2.7% | 2.5% | 2.6% | 2.6% | 1.7% | 9.8% | 5.2% | 3.8% |
| Internal financing | -1.7% | -1.0% | -1.0% | -0.5% | 0.3% | 0.0% | 0.3% | 0.2% | -0.1% | -0.3% | 0.5% | -8.8% | -3.1% | -1.2% |
| External financing | -2.5% | -2.2% | -2.3% | -3.1% | -3.3% | -3.0% | -2.9% | -2.7% | -2.5% | -2.3% | -2.2% | -1.0% | -2.1% | -2.6% |
| Overall financing | -4.2% | -3.2% | -3.3% | -3.6% | -3.0% | -3.0% | -2.7% | -2.5% | -2.6% | -2.6% | -1.7% | -9.8% | -5.2% | -3.8% |

* в % ВВП; ** ЕСН включен в налоговые доходы

As compared with the figures registered in the three first months of 2003, the budget revenues decreased by 1.2 p. p. of GDP in the respective period of 2004, while expenditures decreased by 1.8 p. p. and budget surplus respectively increased by 0.6 p. p. of GDP. At the same time, without SST the budgetary revenues decreased by 1.2 p. p. of GDP and made 16.9 per cent of GDP. As before, VAT accounted for the major share of federal tax revenues – 38.9 per cent of the total tax revenues what is practically at the level observed in the respective period of 2003.

According to preliminary estimates, the cash execution of federal budget revenues made 20.4 per cent of GDP in January through April of 2004, what was by 0.6 p. p of GDP below the level observed in the respective period of the preceding year. At the same time, the cash execution of expenditures made 17.2 per cent of GDP (17.7 per cent of GDP in January through April of 2004); therefore, in the first three months of this year, according to preliminary data, the surplus made 3.2 per cent of GDP.

According to the preliminary estimates of the Finance Ministry, in terms of fulfilled funding² the expenditures of the federal budget in January through April of 2004 made 19.7 per cent of GDP (see Table 2), while in the respective period of 2003 this indicator was at 20.2 per cent of GDP. In January through April of 2004,

¹ Because of the estimated data on GDP, the indices may be subject to revision.

² The execution of the budget in terms of fulfilled (actual) financing is equal to the sum of the funds transferred to managers of budget funds, while the cash execution of the budget is equal to the sum of funds spent by managers of funds (i.e. without account of funds remained on their accounts).

the amount of revenues of the federal budget decreased by 0.6 p. p. of GDP in comparison with the figures registered in the respective months of 2003 and made 20.4 per cent of GDP, what was partially caused by a 2.2 p. p. reduction of the VAT rate. Therefore, the surplus of the federal budget in terms of fulfilled funding in January through April of 2004 decreased by 0.1 p. p. in comparison with the figures registered in January through April of 2003 and made 0.7 per cent of GDP.

Table 2

**The monthly execution of the federal budget of the Russian Federation
(in % GDP, fulfilled funding)**

| | IV'03 | V'03 | VI'03 | VII'03 | VIII'03 | IX'03 | X'03 | XI'03 | XII'03 | I'04 | II'04 | III'04 | IV'04 |
|-------------------------------|-------|-------|-------|--------|---------|-------|-------|-------|--------|-------|-------|--------|-------|
| Total expenditures | 21.0% | 21.3% | 20.6% | 20.4% | 20.0% | 19.6% | 19.5% | 19.4% | 19.4% | 20.9% | 20.2% | 19.8% | 20.4% |
| State administration | 0.6% | 0.6% | 0.5% | 0.5% | 0.5% | 0.5% | 0.5% | 0.5% | 0.5% | 0.6% | 0.7% | 0.6% | 0.6% |
| National defense | 3.2% | 3.1% | 3.0% | 2.9% | 2.8% | 2.7% | 2.8% | 2.9% | 2.7% | 2.7% | 4.0% | 2.9% | 3.7% |
| International activity | 0.3% | 0.3% | 0.3% | 0.3% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.0% | 0.2% | 0.2% | 0.3% |
| 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 | 2.2% | 2.2% | 2.1% | 2.0% | 1.9% | 1.9% | 1.9% | 1.9% | 1.9% | 2.1% | 2.5% | 2.3% | 2.4% |
| 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% | 0.4% |
| Services to national economy | 1.0% | 1.0% | 1.0% | 1.0% | 1.0% | 1.0% | 1.0% | 1.1% | 1.1% | 0.5% | 0.7% | 0.8% | 0.9% |
| Social services | 2.9% | 2.7% | 2.6% | 2.5% | 2.4% | 2.3% | 2.3% | 2.4% | 2.3% | 2.5% | 2.6% | 2.4% | 3.0% |
| Government debt servicing | 2.3% | 2.1% | 2.0% | 1.8% | 2.0% | 2.0% | 1.8% | 1.7% | 1.7% | 1.1% | 2.2% | 2.2% | 1.7% |
| Other expenditures | 7.2% | 7.4% | 7.3% | 7.2% | 7.2% | 7.0% | 6.9% | 6.9% | 7.0% | 5.7% | 6.8% | 6.1% | 6.6% |
| Total expenditures | 20.2% | 19.9% | 19.2% | 18.8% | 18.6% | 18.3% | 18.0% | 18.1% | 17.8% | 15.6% | 20.2% | 18.0% | 19.7% |
| Surplus (+) / deficit (-) | 0.8% | 1.4% | 1.3% | 1.6% | 1.3% | 1.3% | 1.5% | 1.3% | 1.6% | 5.3% | 0.0% | 1.8% | 0.7% |

According to the estimates of the Tax Ministry, in April of 2004 tax revenues of the federal budget made about Rb. 130.2 billion (without the single social tax). In real terms the revenues made 266.3 per cent of the level registered in January of 1999, while the respective indicator was at 280.4 per cent in April of 2003 and 277.8 per cent in April of 2002 (see Table 3).

At the same time, in April of 2004 the revenues generated by the single social tax made Rb. 36.9 billion. Thus, in April of 2004 the RF Tax Ministry transferred to the federal budget taxes and fees amounting to about Rb. 167.1 billion.

Table 3

**Actual tax revenues to the federal budget, according to the data of the MTC
(in % of the data for January of 1999)³.**

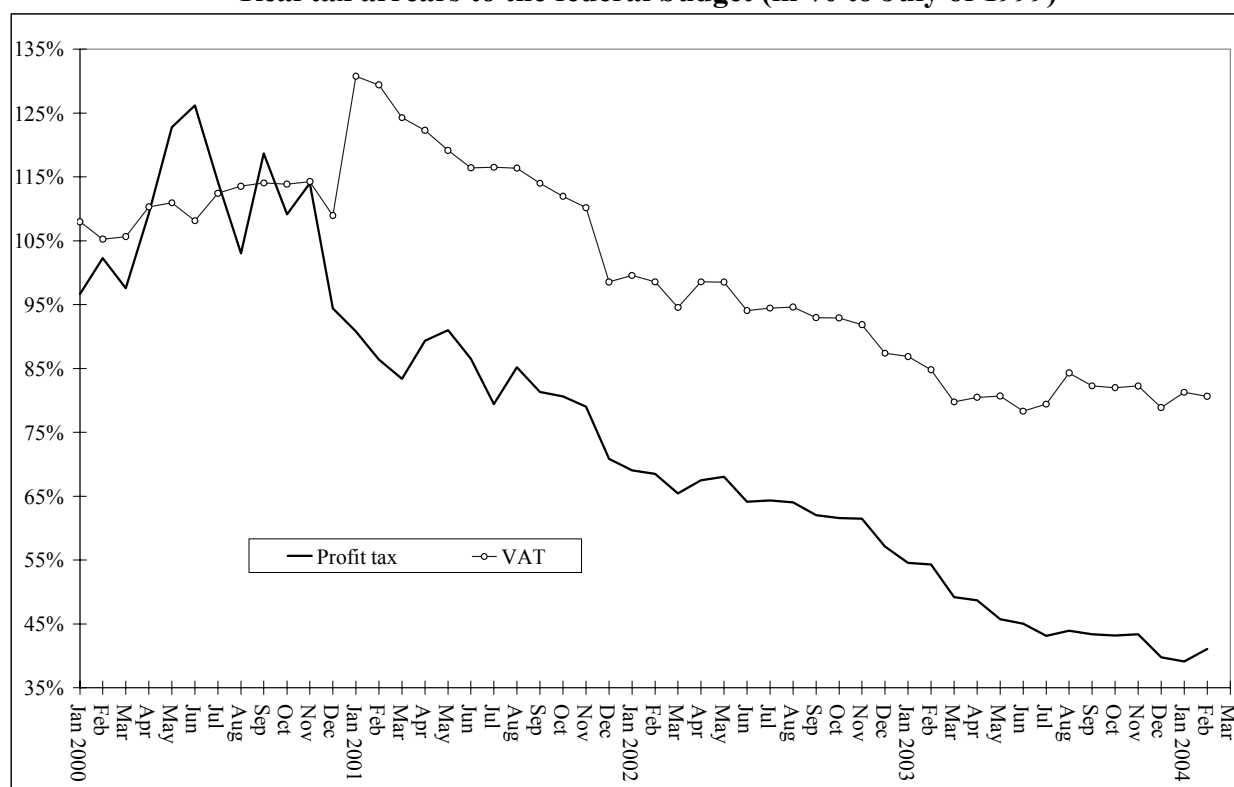
| 1999 | | | | | | | | | | | |
|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| 100,0% | 115,1% | 122,0% | 122,1% | 104,5% | 112,9% | 127,0% | 127,5% | 124,3% | 141,4% | 160,8% | 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% |
| 2004* | | | | | | | | | | | |
| I | | | II | | | III | | | IV | | |
| 266,5% | | | 204,4% | | | 237,1% | | | 266,3% | | |

* Без учета ЕЧН.

³ It was decided to choose January of 1999 as the benchmark in order to render the comparison more reliable. January of 1999 is not a remarkable date in terms of tax revenues.

Figure 1

Real tax arrears to the federal budget (in % to July of 1999)



The dynamics of real arrears relating to major taxes since January of 2000 are presented in Fig. 1. The debts related to the payments due to the federal budget made for VAT Rb. 256.3 billion as on March 1, 2004, increasing by Rub. 0.6 billion in February of 2004, while the arrears of the profit tax increased only by Rb. 1.6 billion and made Rb. 28.0 billion. On the whole, a gradual decrease in the level of accumulated arrears observed since early 2001 to the second half of 2003 was replaced by the stabilization of the level of accumulated indebtedness as concerns both the profit tax, and VAT.

Table 4

Execution of the RF consolidated budget (in % 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 | 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 | 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% | 25,2% |
| Revenues | 32,0% | 30,3% | 31,5% | 33,4% | 33,6% | 32,2% | 32,2% | 31,6% | 30,9% | 30,8% | 30,7% | 31,1% |
| Expenditures | 20,7% | 25,3% | 27,7% | 28,8% | 28,8% | 28,6% | 28,7% | 28,5% | 28,2% | 27,8% | 27,9% | 29,7% |
| Deficit | 11,3% | 5,0% | 3,8% | 4,5% | 4,7% | 3,5% | 3,6% | 3,1% | 2,7% | 3,0% | 2,8% | 1,4% |
| 2004 | | | | | | | | | | | | |
| | I | | | II | | | III | | | | | |
| Taxes | 25,6% | | | 20,6% | | | 21,8% | | | | | |
| Revenues | 30,6% | | | 28,2% | | | 29,8% | | | | | |
| Expenditures | 18,5% | | | 22,8% | | | 25,4% | | | | | |
| Deficit | 12,1% | | | 5,4% | | | 4,4% | | | | | |

* Без учета ECH

The revenues of the consolidated budget in January through March of 2004 made 29.8 per cent of GDP, including tax revenues (without SST) at 21.8 per cent of GDP (see Table 4). Expenditures of the consolidated budget decreased by 2.3 p. p. of GDP in comparison with the figures registered in January through March of 2003 and made 25.4 per cent of GDP. As on April 1, 2004, the surplus of the consolidated budget made 4.4 per cent of GDP, what is by 0.6 p. p. of GDP above the level observed in the respective period of 2003.

A. Razin

Monetary Policy

This April, the rates of growth in consumer prices somewhat increased in comparison with the figures registered last month and made 1 per cent by the end of the month. At the same time, the base inflation also increased. In April of this year, there was observed a decline in the amount of gold and foreign exchange reserves of the Russian Central Bank. In May, the RF Finance Ministry made payments relating to the external debt amounting to more than US \$ 2.5 billion.

In April of 2004, the growth in consumer price index made 1 per cent in comparison with the figures registered last month (4.6 per cent since the beginning of the year) (see *Figure 1*). It should be noted that in April of 2003 CPI also increased by 1 per cent, while inflation accumulated from the beginning of the year made 6.2 per cent. This April, the most significant growth in prices was observed in the group of paid consumer services (by 2 per cent in comparison to the figures registered in March of 2004 and 8.5 per cent since the beginning of the year). Last year, the increase in respective prices over four months made 12.6 per cent. As a year ago, the most significant growth in prices was observed in the sphere of prices of services relating to housing and public utilities (by 15.6 per cent). It should be noted that with the exception of services rendered by organizations of culture and preschool education, paid consumer services rose in prices slower than in 2003.

As it was expected, base inflation⁴ (0.8 per cent in April, 0.7 per cent in March) stopped to decline. It should be reminded that its level is determined primarily by the growth in money supply (with a certain lag) and the velocity of cash circulation depending on the exchange rate. The pressure on consumer prices on the part of money supply is increasing, since at present the consumer price index is affected by its expansion registered in the 4th quarter (by 5.2 per cent a month on the average). Accordingly, the main role in restraint of inflation is played by slowing velocity of cash circulation.

Over four months of 2004, the prices of food products increased at a slower rate than last year. In April of 2004, the growth in these prices was below 0.8 per cent in comparison with the figures registered in the last month, and since the beginning of the year CPI for this group of products increased by 4.7 per cent, while last year over the same period of time the growth in prices made 5.8 per cent. However, in 2004 the rates of rise in prices of a number of most important food products were significantly higher than the same indicators

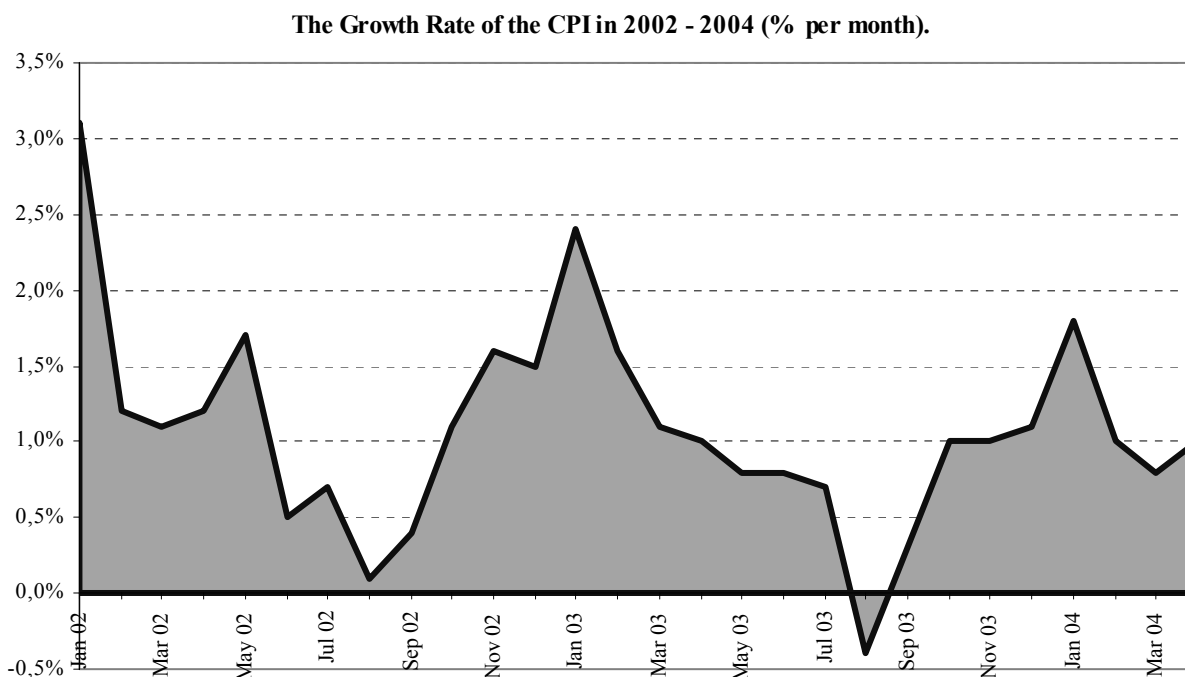
⁴ The Base Consumer Price Index (BCPI) is an indicator reflecting the inflation rate on the consumer market. It leaves out of account the seasonal (prices of fruits and vegetables) and administrative (tariffs on regulated types of services etc.) factors, calculated by the Statistics Service of the RF.

registered in the respective period of the last year. For instance, since the beginning of the year the growth in prices of bread and bread related products, which rose in prices by 2.2 per cent this April, made 11.5 per cent, while in the first four months of 2003 the respective prices decreased by 0.1 per cent. The deceleration of the general price index of food products is primarily explained by the dynamics of prices of fruits and vegetables, the average monthly rates of increase in prices of which this year were almost three times below the average monthly rates registered last year. Besides, a more moderate growth in comparison with the figures registered last year was observed with respect to the group of prices of fish and sea products, butter, and sunflower oil.

In spite of the fact that the changes in prices of nonfood products has a more moderate impact on the CPI dynamics than foodstuffs, it should be mentioned that the rates of growth in prices of these products over four months of 2004 are also below the indicators registered in the respective period of the last year. This April, they grew by 0.6 per cent, while the increase since the beginning of the year made 2 per cent (0.6 per cent and 3.4 per cent respectively in 2003).

According to preliminary estimates, in May inflation rates will be at or below 0.6 to 0.8 per cent.

Figure 1.



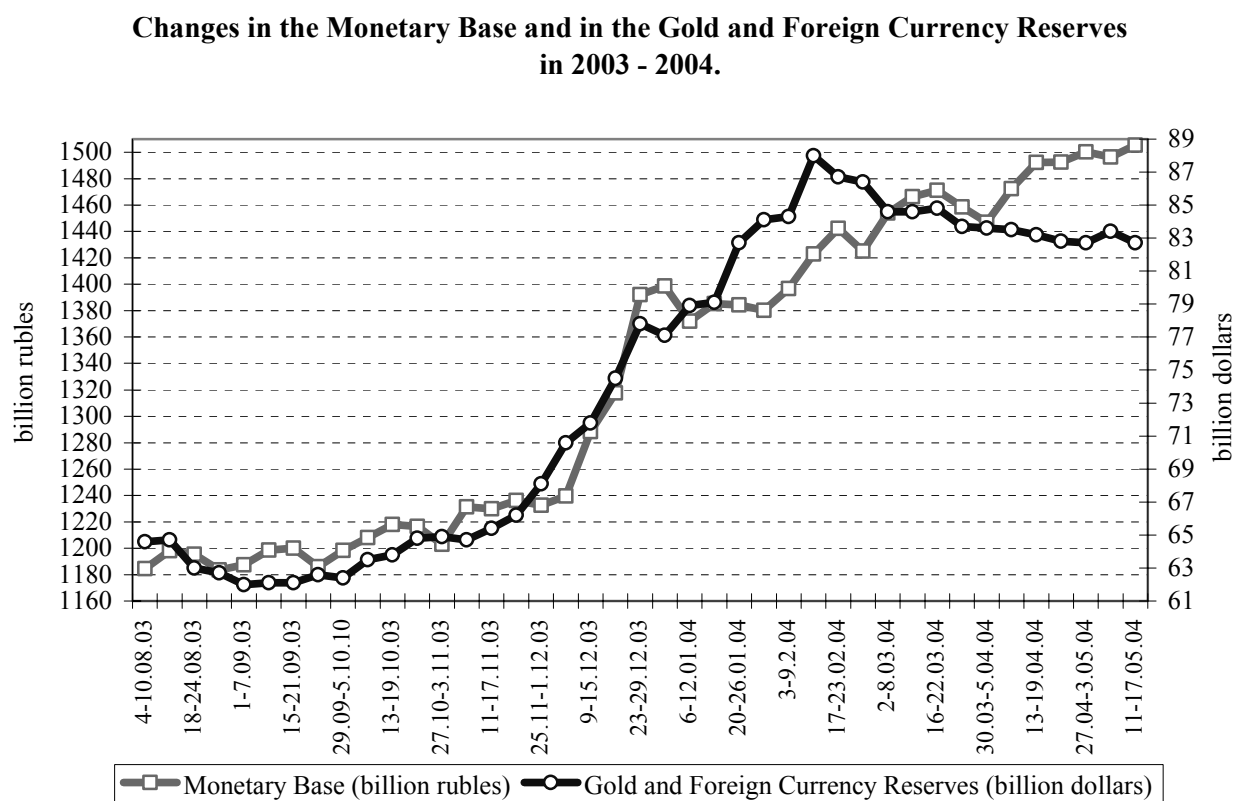
In the first four months of 2004, the amount of gold and foreign exchange reserves of the Bank of Russia increased by US \$ 5.8 billion (see Fig. 2). As on May 1, 2004, the amount of these reserves made US \$ 82.7 billion (+ 7.5 per cent since the beginning of the year). In the first two weeks of May, the amount of gold and foreign exchange reserves did not change. However, as on April 1, 2004, the amount of gold and foreign exchange reserves made US \$ 83.4 billion, i.e. over the month they decreased by US \$ 0.7 billion, or by 0.8 per cent. In April, the gold and foreign exchange reserves were declining, what is primarily related to the foreign debt related payments made by the RF Finance Ministry. It should be also noted that in spite of considerable forex denominated proceeds of oil exporters, the total amount of foreign exchange to the RF market could decrease, since, according to preliminary data, in the 2nd quarter the outflow of capital from Russia intensified. This fact is primarily related to the expectations that the discount rates in the USA would be increased.

In April of 2004, the monetary base of the Russian Federation in the broad definition⁵ decreased by 2.2 per cent, and as on May 1 made RUR 1.9 trillion (the process of decline was observed for the second month run-

⁵ The RF Monetary Base in broad definition includes cash in circulation, the Ruble denominated funds in mandatory reserves relating to the borrowings of credit organizations, and funds in credit organizations' correspondent accounts and commercial banks' deposits with the Bank of Russia.

ning). The opposite dynamics of the monetary base in broad definition and the narrowly defined monetary base, which increased by 2.9 per cent in April, is related to the fact that the amount of accounts of crediting organizations with the Central Bank of Russia diminished by 20.4 per cent to RUR 184.8 billion (-64.9 per cent as compared with the figures registered in the beginning of 2004), while the amount of banks' deposits in the Bank of Russia in April also decreased 2.2 times to RUR 49 billion. The main factors behind the decline in the level of liquidity in the banking sector were significant payments to budgets of all levels and further accumulation of funds in budget accounts not compensated by issue of money because of the amount of net sales of foreign exchange by the Bank of Russia on the forex market in March and April. At the same time, the amount of cash in circulation (as adjusted for cash balances of crediting organizations) made RUR 1.3 trillion as on May 1 (by 3.3 per cent above the level registered on April 1 of this year and by 6.9 per cent above the figures observed on January 1 of 2004), what predetermined a growth in the narrowly defined monetary base. The amount of mandatory reserves also declined by 4.2 per cent and made RUR 275.7 billion, partially due to the fact that the CB of RF reduced the rate of mandatory reservation concerning deposits of legal entities since April 1 of 2004.

Figure 2.



In May of 2004, the amount of payments pertaining to the public foreign debt of the Russian Federation was US \$ 2.5 billion. This, in turn, included US \$ 104.1 million paid to official creditor countries, banks, and firms as debt repayment and interest payments (including US \$ 90.4 as debt repayment and US \$ 13.7 as interest payments). In May, payments to international financial organizations made US \$ 107.3 million (including US \$ 102.6 as debt repayment and US \$ 4.7 as interest payments). Besides, in May more than US \$ 2 billion were transferred for repayment of bonds relating to the domestic public forex denominated loan (OVGVZ) and US \$ 265 as cashing of coupons. Russia paid about US \$ 5.6 billion in January through April, while the total amount of Russia's payments relating to the foreign debt should make about US \$ 17.3 billion this year.

P. Trounin

Financial Markets

In May of 2004, on the Russian financial market there was observed a general worsening of the business situation. The expected rise of interest rates in the USA not only affected the markets of public and corporate debts, but also facilitated a reduction of demand for Russian securities on the part of nonresidents. Political risks also increased (the further development of the situation relating to the YUKOS affair), although they did not influence the markets so much as earlier. High oil prices and favorable macroeconomic situation in the country have partially supported the quotations preventing their further decline.

The Market for Government Securities

As concerns the general situation in May, there was observed a decline in quotations of Russian forex denominated bonds. Nevertheless, the respective dynamics were unstable. Thus, the first week after the holidays was characterized by a decline in quotations of Russian bonds, which was to a considerable extent caused by the dynamics of US debt securities. The growth in the yields of US treasury bills occurring at the background of publication of employment situation data, which considerably differed from the forecasts and confirmed the apprehension of a soon increase in the discount rate, facilitated the rise in yields. However, the macroeconomic data published later in general corresponded to forecasts, what investors on the US market regarded as an evidence indicating the possibility of impending increase in the base rate (June – July) and resulted in the growth in prices. Accordingly, the quotations of Russian securities also increased. An additional factor of support of the Russian segment of Eurobonds was that S&P agency increased its ranking of Kazakhstan to the investment level, what was appraised by the market as an evidence of the soon increase in the Russia's ranking.

Thus, as on May 21 the yield to maturity of Russian Eurobonds RUS-30 was 8.14 per cent p.a. (end of April: 7.97 per cent); RUS-18: 7.89 per cent p.a. (end of April: 7.53 per cent). Besides, on the same date the yield to maturity of the Russian Eurobonds was: Minfin bonds, 7th tranche: 7.39 per cent; Minfin bonds, 6th tranche: 5.04 per cent; Minfin bonds, 5th tranche: 6.57 per cent; RUS-07: 5.30 per cent.

Figure 1

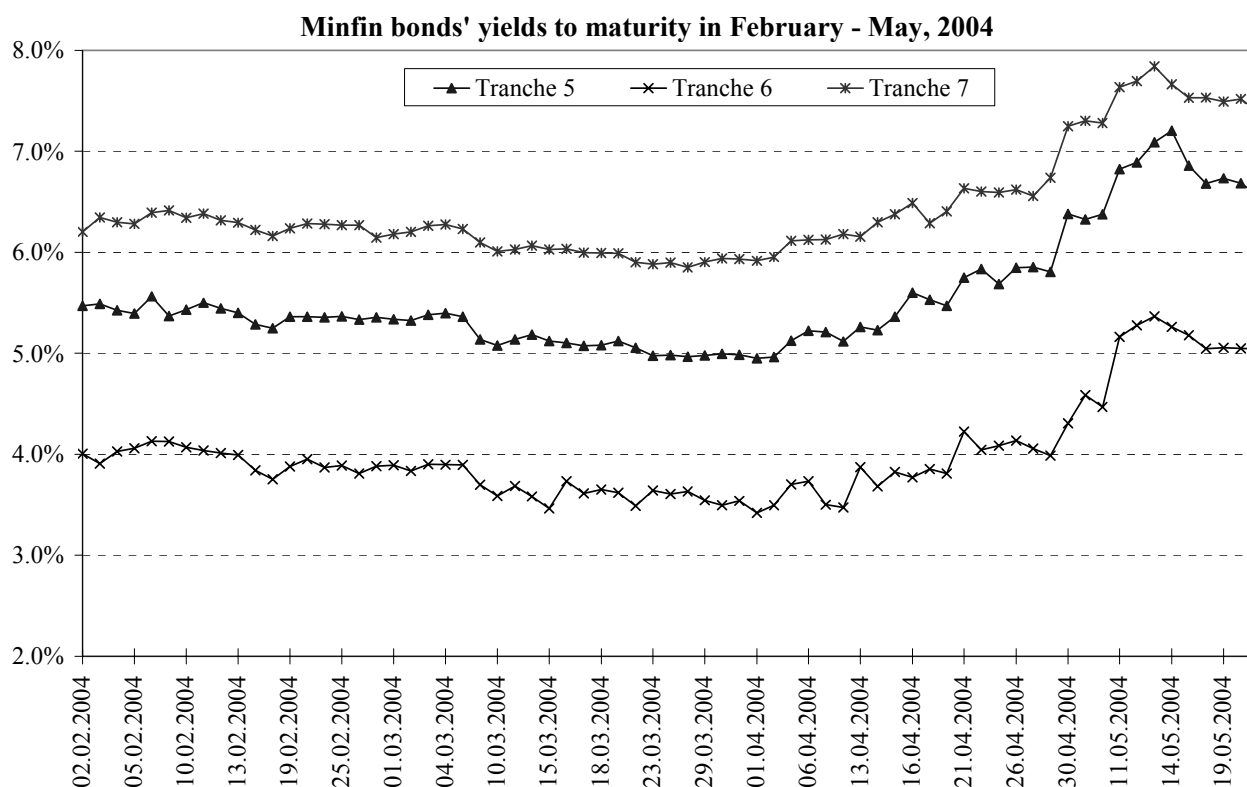
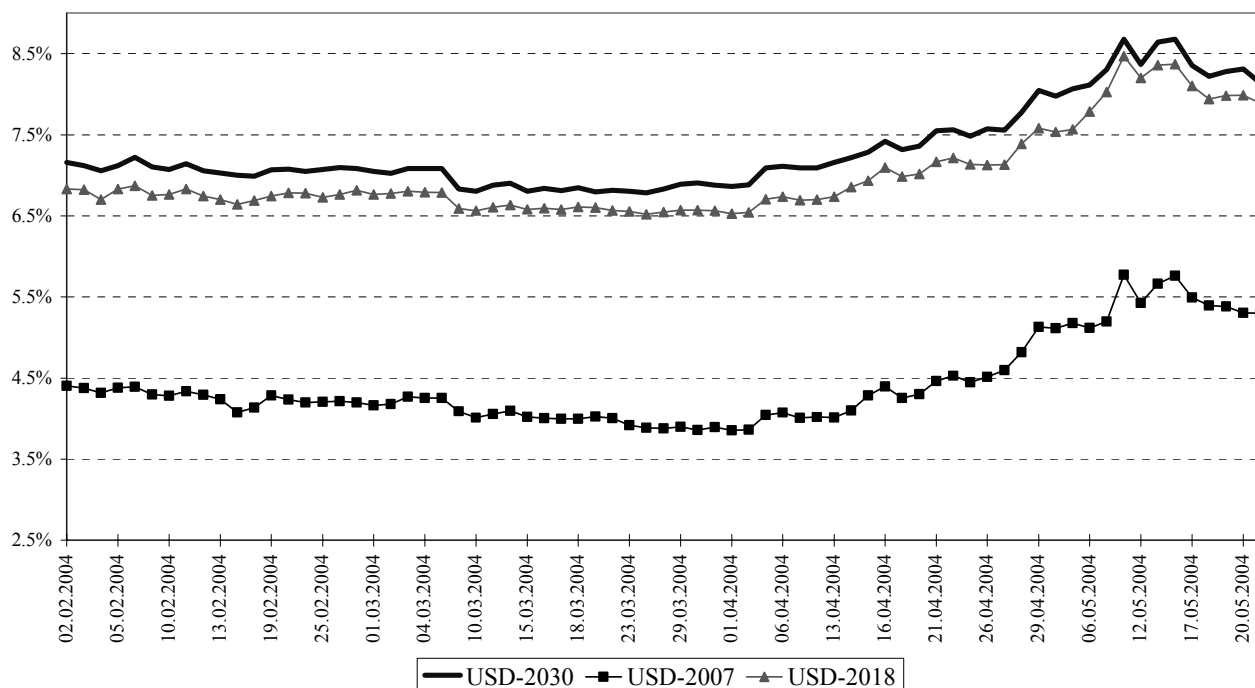


Figure 2.

Yields to maturity of the Russian eurobonds with maturity in 2030, 2018 and 2007 in February - May, 2004



A decline in prices was also observed on the market of Ruble denominated public debt. Over the first week after the holidays there was registered a downfall in prices across practically all issues of GKO OFZ. High MIBOR rates and the US dollar appreciation facilitated a decline in prices of Ruble denominated instruments. The second working week was characterized by a partial growth in quotations at the background of Ruble appreciation. However, the increase in the rates on the inter-bank credit market limited demand, what did not permit prices to significantly adjust upward.

Over the period from May 1 to 21, the aggregate turnover of the secondary GKO OFZ market made about RUR 18.3 billion, while the average daily turnover was at RUR 1.67 billion (in April, the respective indicator was registered at RUR 1.8 billion). In the same period, there took place only one auction for the placement of GKO – OFZ. On May 19, there took place the auction for the placement of OFZ AD 46003, the nominal value of which made RUR 5 billion. The amount of the placements made RUR 1.08 billion, while the weighed average yields of the placements were at 7.68 per cent per annum. As on May 26, the amount of the GKO – OFZ market made RUR 472.5 billion at par and RUR 453.41 billion at the market value. The duration of the GKO-OFZ market portfolio was 1621.42 days.

The Market for Corporate Securities

Situation on the stock market.

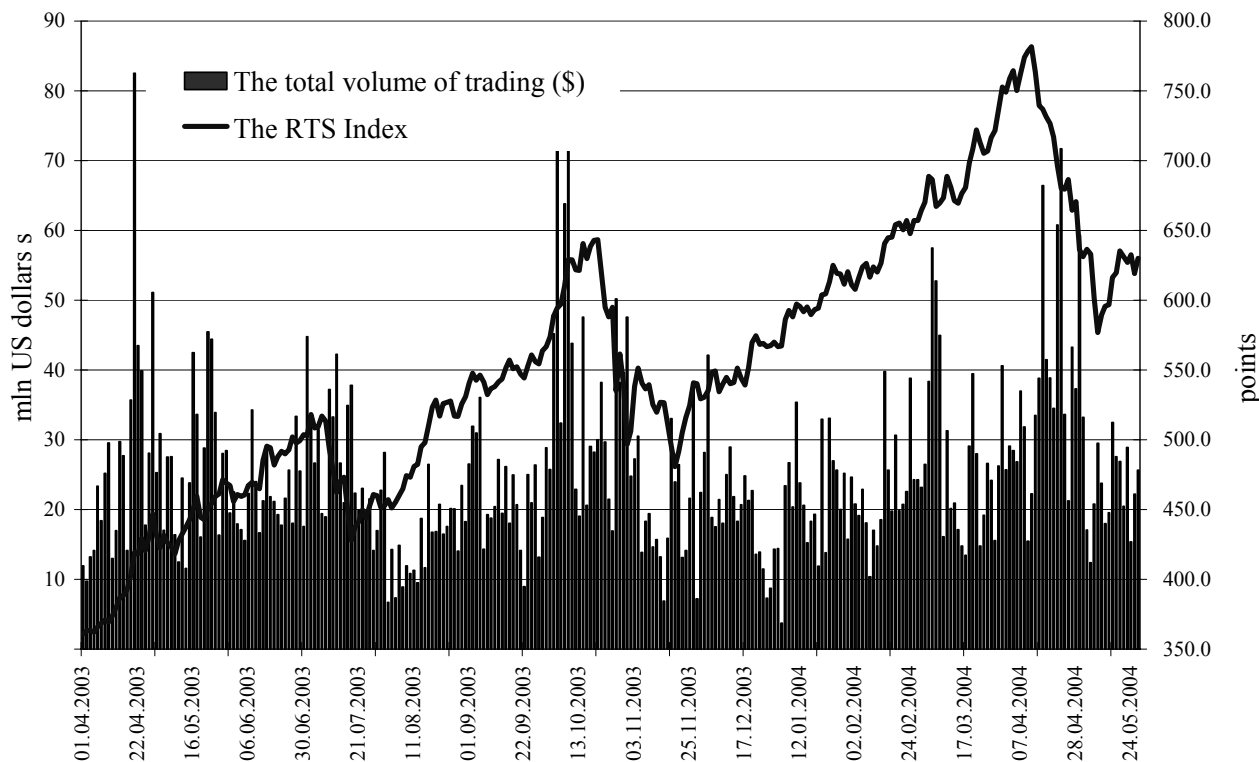
In May, on the Russian stock market there was observed opposite trends of quotations. In the beginning of the month, during the holiday trade week, the market continued its downward movement, and the RTS index made 576.63 points by May 11. The internal factors behind this downfall were the worsening of the liquidity situation in the banking sector and the further development of the situation concerning the YUKOS affair⁶, while external factors were the apprehension of the soon increase in the base rates in the USA and the dynamics of foreign quotations of Russian ADR and GDR. However, over the next two weeks the RTS index increased somewhat and

⁶ On May 19, the company received the second notification of the creditor concerning the possible default on the pre-export credit amounting to US \$ 1.6 billion. On May 26, the Moscow Arbitration Court ruled to recover from the NK YUKOS RUR 99 billion in taxes, penalties, and fines for year 2000. According to the statement made by the company, further similar actions on the part of the Tax Ministry may result in the company's bankruptcy by the end of 2004.

stabilized at 610 to 630 points. The positive adjustment was caused by low prices of the majority of blue chips, as well as a number of positive corporate news. In spite of numerous negative factors, record high oil prices continue to support the market preventing its further decline.

It should be also noted that in May creditors addressed YUKOS the second notification of possible default, the company's headquarters were searched, and the Arbitration Court ruled to exact the company's debt relating to tax payments. However, the development of the situation concerning YUKOS has much lesser impact on investors' intentions and, as a result, does not cause a significant downfall of quotations on the market.

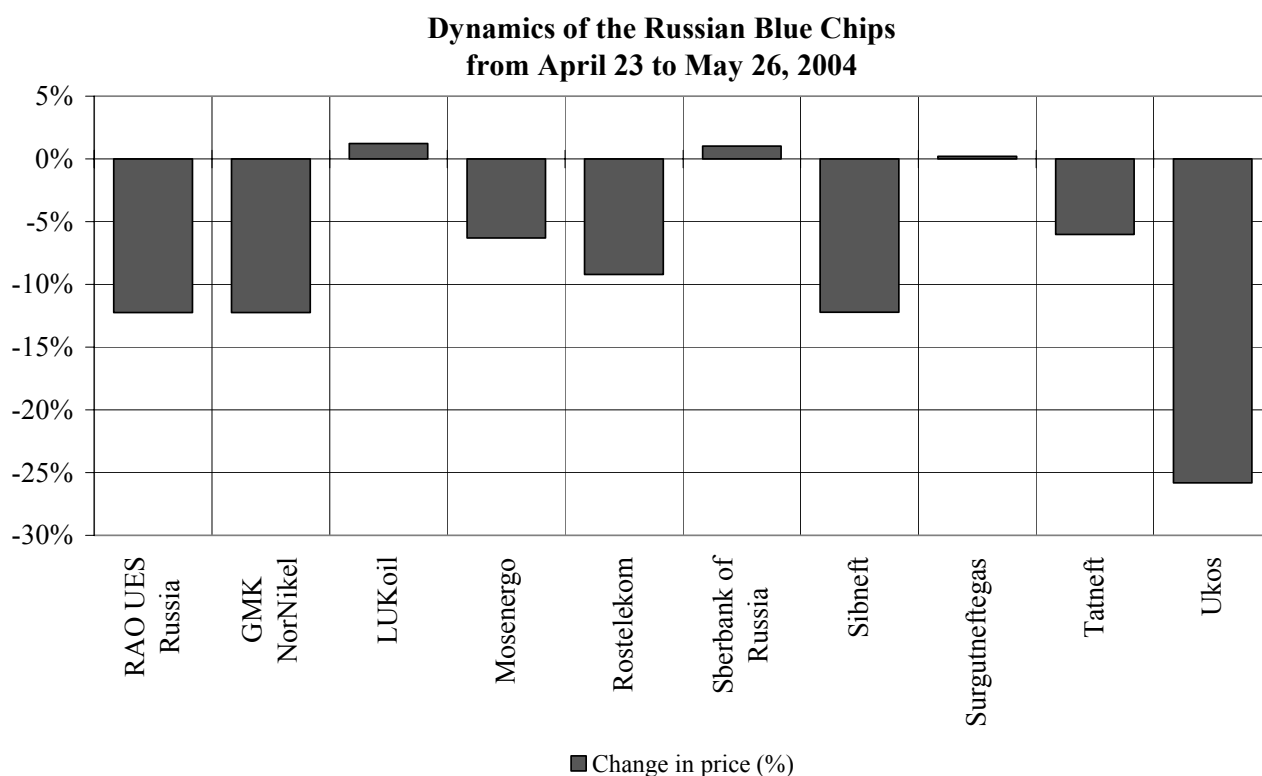
Figure 3.



According to the data as on May 26, the RTS index made 629.99 points, what was by 1.12 points (0.18 per cent) below the value of this indicator registered at the end of April. In the period from May 5 till 26, the turnover of the RTS trading amounted to about US \$ 340 million, while the average daily turnover at the RTS made about US \$ 22.69 million (about US \$ 37 million in April). The highest and the lowest volumes of trade at the RTS made US \$ 32.5 million (on May 17) and US \$ 12.4 million (on May 6), what was significantly below the figures registered in April (US \$ 71.6 million and US \$ 15.5 million respectively).

Over the last month (from April 23 till May 26), all "blue chips" with the exception of LUKoil (a 1.24 per cent growth), Sberbank of Russia (a 1.00 per cent growth), and Surgutneftegaz (a 0.2 per cent growth) demonstrated a significant downfall in prices. Thus, shares in NK YUKOS became leaders in terms of decrease in prices (-25.8 per cent) as a reaction to the further worsening of the company's situation. The YUKOS shares were followed by the stocks of the RAO UES of Russia and the GMK Norilsk Nickel (-12.25 per cent), and shares in Sibneft (-5.79 per cent). At the same time, the shares in Rostelekom, Mosenergo, and Tatneft fell by 9.21 per cent, 6.31 per cent, and 6.01 per cent respectively.

Figure 4.



In the period from May 5 till May 21, the RAO UES of Russia shares took the top position by the volume of turnover in the RTS⁷: the share of respective transactions amounted to about 30.92 per cent of the total turnover. The amount of transactions with the shares in the LUKoil was somewhat lower (23.23 per cent). The shares of YUKOS and Surgutneftegaz followed: the volume of transactions with these companies' shares made 11.47 per cent and 5.95 per cent of the total turnover respectively. Thus, the aggregate percentage of transactions with the shares of only these four companies made about 71.58 per cent of the total traded turnover over the period of time under observation.

As on May 26, the top five leaders of the national stock market by capitalization looked as follows⁸: YUKOS: US \$ 26.65 billion; LUKoil: US \$ 24.75 billion; Surgutneftegaz: US \$ 24.68 billion; Sibneft: US \$ 13.27 billion; MMC Norilsk Nickel: US \$ 13.16 billion.

The market for fixed term contracts. In May, the activity of investors on the RTS market for fixed term contracts (FORTS) practically did not change in comparison with the preceding month. Thus, in the period from May 5 till 26 the volume of trade in futures and options at the RTS amounted to about RUR 20.6 billion (102.1 thousand transactions; 2.77 million contracts), what was at the same level as the respective indicators registered in the preceding month (turnover - RUR 23.28 billion, 98.9 thousand transactions; 2.67 million contracts).

As usual, futures contracts account for the greatest percentage of transactions: the volume of trade in these contracts made RUR 18.65 billion (2.5 million contracts, 98.68 thousand transactions) over the period under observation. As before, options were in a much lower demand: the respective amount of trading made about RUR 1.96 billion (244 thousand contracts, 3.3 thousand transactions). The maximum trading volume was observed on May 19 and made RUR 1.95 billion, while the minimum trading volume (RUR 829.96 million) was registered on May 5.

Corporate bond market. Over the month, the downfall in prices on the market of corporate bonds continued. From April 30 till May 26, the price index of corporate bonds traded at the MICEX⁹ decreased by 1.08

⁷ On the classical stock market.

⁸ According to the RTS.

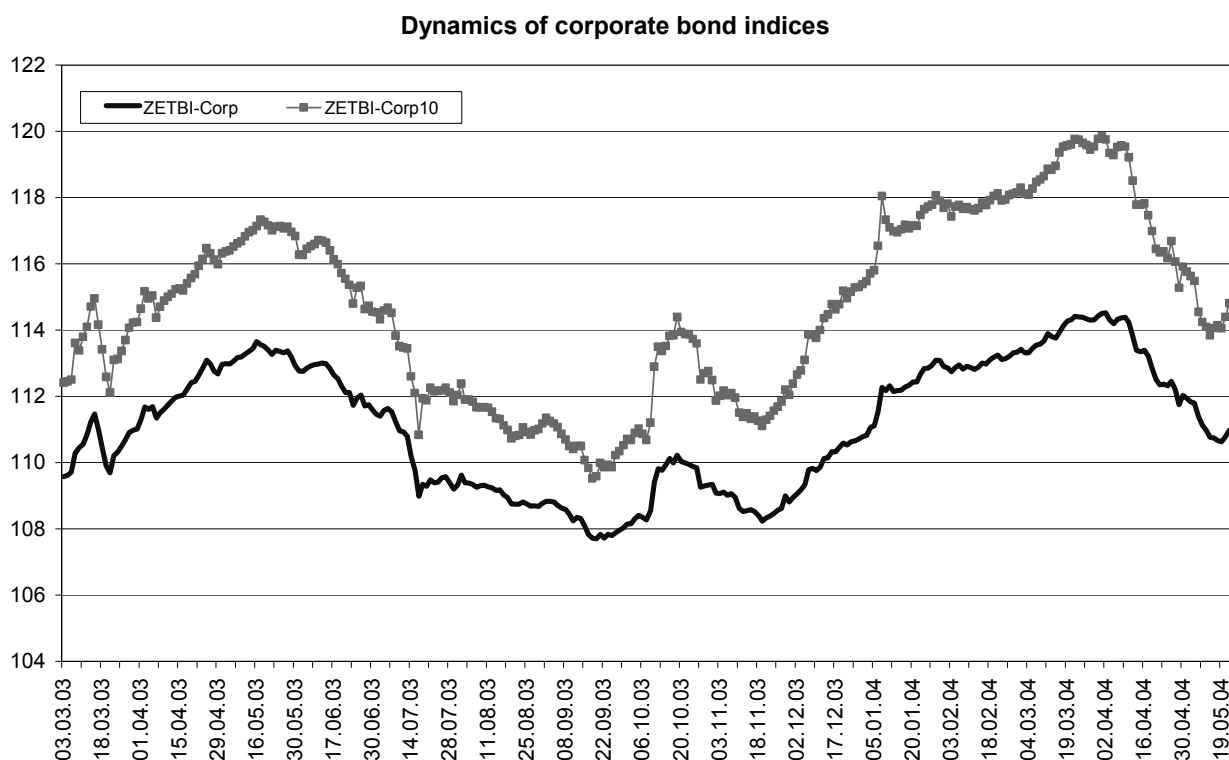
⁹ The indices of corporate bonds traded at the MICEX that have been used for the calculations are calculated by Zenit Bank.

points (by 0.96 per cent) and the index of ten most liquid corporate sector bonds decreased by 1.06 points (by 0.92 per cent).

The decrease in the prices of corporate bonds observed in the beginning of the month was mainly caused by the US dollar appreciation in comparison with the Ruble and low liquidity in the banking sector. However, the low price levels resulted in an increasing demand for corporate bonds. Among positive factors affecting the price dynamics, there should be also mentioned the decreasing yields of US bonds. At the same time, Russian bonds of the second echelon continued to fall, what was caused by the extremely low level of liquidity on the market.

In the period from May 5 till 21, the total turnover in the bond sector of MICEX made about RUR 3.5 billion, while the average daily turnover was registered at RUR 288 million, what was significantly below the indicators registered in April of this year.

Figure 5



External factors affecting the dynamics of the Russian stock market.

Throughout the month, the prices on the world oil markets continued to grow. Thus, in the period from April 30 till May 26 of 2004, the price of Brent oil on the world market increased by US \$ 3.82 (+ 11.02 per cent)¹⁰, from US \$ 34.65 per barrel to US \$ 38.47 per barrel. At the same time, the oil prices in the USA exceeded the level of US \$ 40 per barrel and reached the 20 year maximum. The major factors behind the positive dynamics of the world oil prices remained shortage of gasoline reserves in the USA, growing oil consumption in China, and instability in the Middle East.

¹⁰ The calculations were based on the data presented by the weekly newspaper *Vedomosti*.

Figure 6.

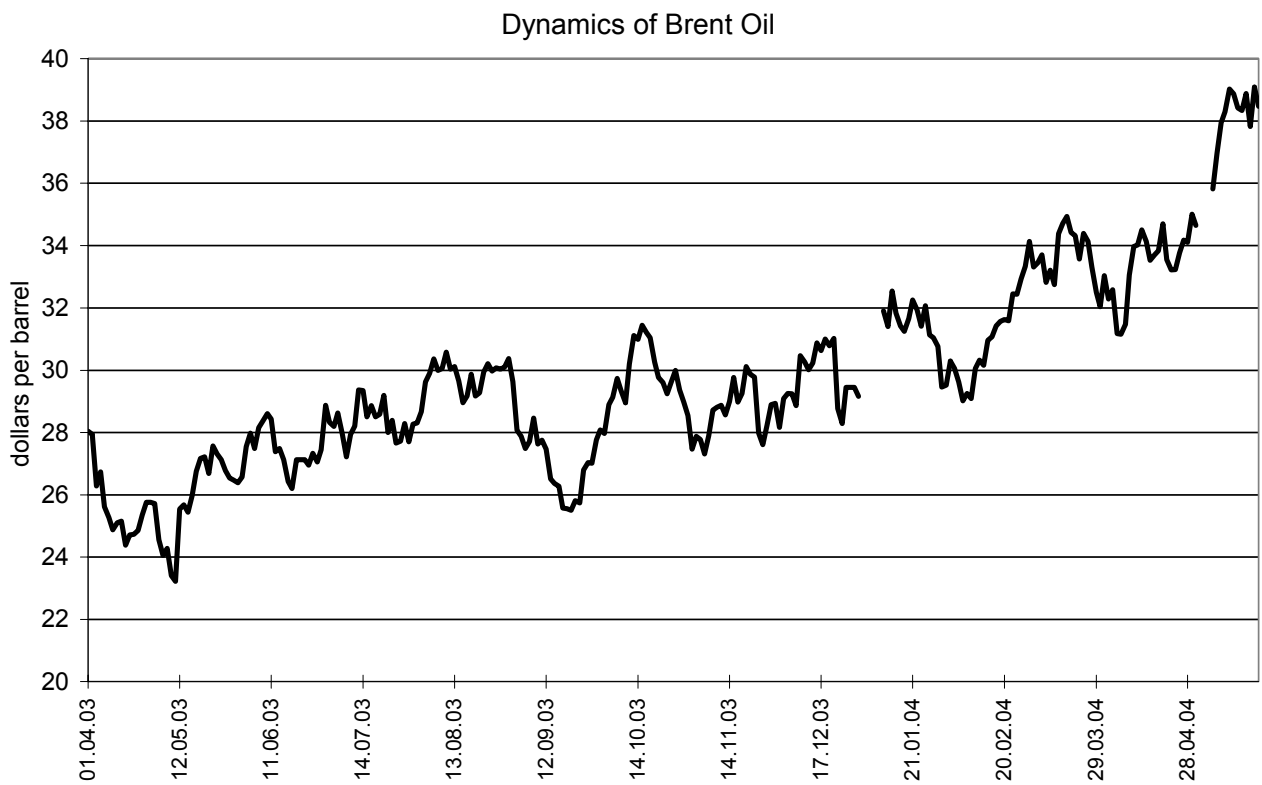
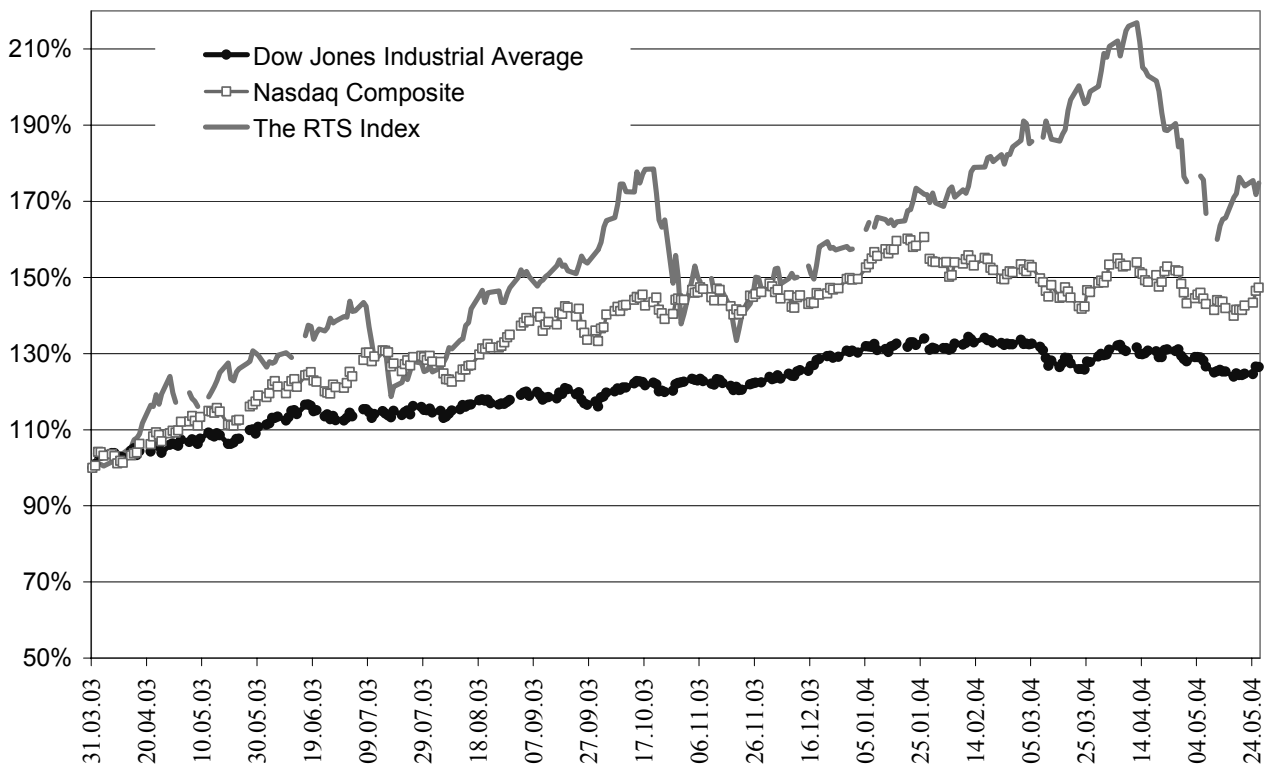


Figure 7.



In May, on the world stock markets there was observed a decrease of the market indices. At the same time, the levels registered as on May 26 caused the indicators of the dynamics since the beginning of the year to

assume negative values (see Table 1). The worsening business situation on the world stock markets was primarily caused by extremely high oil prices, which could negatively affect the rates of development of the world economy, as well as by the situation in the US economy (the possibility of increase in the base interest rate and the deteriorating situation in the Middle East, in particular, in Iraq).

In May, the impact of the business situation on the world oil market and stock markets on the Russian financial sector was mixed. High oil prices, which reached their historic maximums, are a favorable factor for the Russian economy and should automatically facilitate a growth in prices of oil companies' stocks. However, the positive impact of this factor on the dynamics of the domestic financial market was neutralized by a number of negative factors. Among these factors there should be noted the expected increase in the US interest rates, which determined the decline in demand for Russian ADR and outflow of funds from emerging markets, including Russia. Corporate developments in Russia also negatively affected the prices of securities. Limited liquidity of the Russian banking sector only increased the downward trend in spite of a certain adjustment of prices, which occurred later in the month.

Corporate news.

The OAO NGK Slavneft

The Board of Directors of the OAO NGK Slavneft made the decision to recommend the shareholders to distribute the company's net profit amounting to RUR 8 billion 324 million 897 thousand in the following way: RUR 8 billion 319 million 916 thousand 500 should be paid as dividends. The amount of dividends per ordinary share (nominal value 0.1 kopeck) will make RUR 1.75. The amount of RUR 4 million 980 thousand 500 was recommended for transfer for replenishment of the company's own capital. The results of 2003 are as follows: the total amount of dividends to be paid per one ordinary share in the OAO NGK Slavneft will make RUR 4.77 taking into account the previously paid (after the first 6 months and 9 months of operation) amount of dividends. The annual general meeting of the Slavneft shareholders will take place on June 30 of 2004. The list of shareholders entitled to take part in the meeting was formed basing on the data presented in the register of shareholders as on May 12, 2004.

The OAO Rostelecom

On May 17, the company presented its financial statement for the first quarter of 2004 made in accordance with the Russian Accounting Standards (RAS). In the 1st quarter, the company's total earnings made RUR 8.839 billion, what was by 38.9 per cent over the figures registered in the respective period of 2003. The EBITDA indicator made RUR 3.759 billion, increasing by 19.4 per cent in comparison with the figures registered in 2003. At the same time, the increase in net profits made by 125.1 per cent in comparison with the figures observed in the respective period of 2003, thus reaching RUR 2.809 billion.

The NK YUKOS

On May 26, the Moscow Arbitration Court ruled to recover from the NK YUKOS RUR 99 billion (US \$ 3.4 billion) in taxes, penalties, and fines for year 2000 with respect to the claim filed by the RF Tax Ministry. At present, the company lacks available funds to repay the this amount. In connection to the fact that the prohibition to sell the company's assets is still in force, and it is impossible to realize the assets in order to attract liquid funds, the company informed its shareholders and creditors about the possibility of the company's bankruptcy in the case the Tax Ministry continues to take similar measures.

Table 1.

Dynamics of International Stock Market Indices

| Data as of May 26, 2004 | Value | Change within the month (%) ¹¹ | Change since the beginning of the year (%) |
|--|----------|---|--|
| RTS (Russia) | 629.99 | -7.30% | 7.49% |
| Dow Jones Industrial Average (USA) | 10109.89 | -3.47% | -2.88% |
| Nasdaq Composite (USA) | 1976.15 | -3.59% | -1.52% |
| S&P 500 (USA) | 1114.94 | -2.25% | 0.58% |
| FTSE 100 (UK) | 4438.3 | -2.88% | -1.59% |
| DAX-30 (Germany) | 3867.3 | -5.75% | -3.76% |
| CAC-40 (France) | 3659.92 | -3.98% | 1.75% |
| Swiss Market (Switzerland) | 5671.7 | -2.52% | 1.59% |
| Nikkei-225 (Japan) | 11152.09 | -7.99% | 3.02% |
| Bovespa (Brazil) | 19069 | -11.68% | -15.04% |
| IPC (Mexico) | 10062.58 | -6.15% | 23.95% |
| IPSA (Chile) | 1417.97 | -2.94% | -4.49% |
| Straits Times (Singapore) | 1776.7 | -4.87% | -0.82% |
| Seoul Composite (South Korea) | 784.06 | -16.24% | -4.53% |
| ISE National-100 (Turkey) | 17235.48 | -11.30% | -9.99% |
| Morgan Stanley Emerging Markets Free Index | 426.191 | -10.88% | -3.83% |

The Foreign Exchange Market. In the period from April 30 till May 26, the US \$ / RUR exchange rate increased by about 9 kopecks to the level of RUR 28.97 per US \$, what made circa 0.32 per cent. On the whole, during the month the exchange rate dynamics were mixed and the overall exchange rate remained at the practically same level as compared with the figures registered in early April. On the one hand, the further Ruble appreciation was supported by the extremely high oil prices, while, on the other hand, the Ruble exchange rate was negatively affected by the US dollar appreciation on the world market at the background of positive macroeconomic data in the USA.

The aggregate volume of trade in the US Dollar at the SELT in the period from May 5 till May 21 made US \$ 7.4 billion, what was significantly below the figures registered in the respective period of April (about US \$ 9 billion). The average daily turnover made US \$ 618.33 million over this period as compared with US \$ 582.8 million observed in April. During the period under review, the highest volume of trade in the US Dollar, about US \$ 830 million, was observed on May 20; the lowest volume, US \$ 427.5 million, was observed on May 7.

This May, the Ruble liquidity in the banking sector significantly decreased in comparison with the figures registered in the preceding month: in May, the average balances of correspondent accounts of credit organizations with the Bank of Russia made RUR 154.6 billion, what was by about RUR 26.9 billion below the respective indicator registered in April of 2004 (RUR 181.6 billion).

¹¹ As compared to the level registered on April 23.

Figure 8.

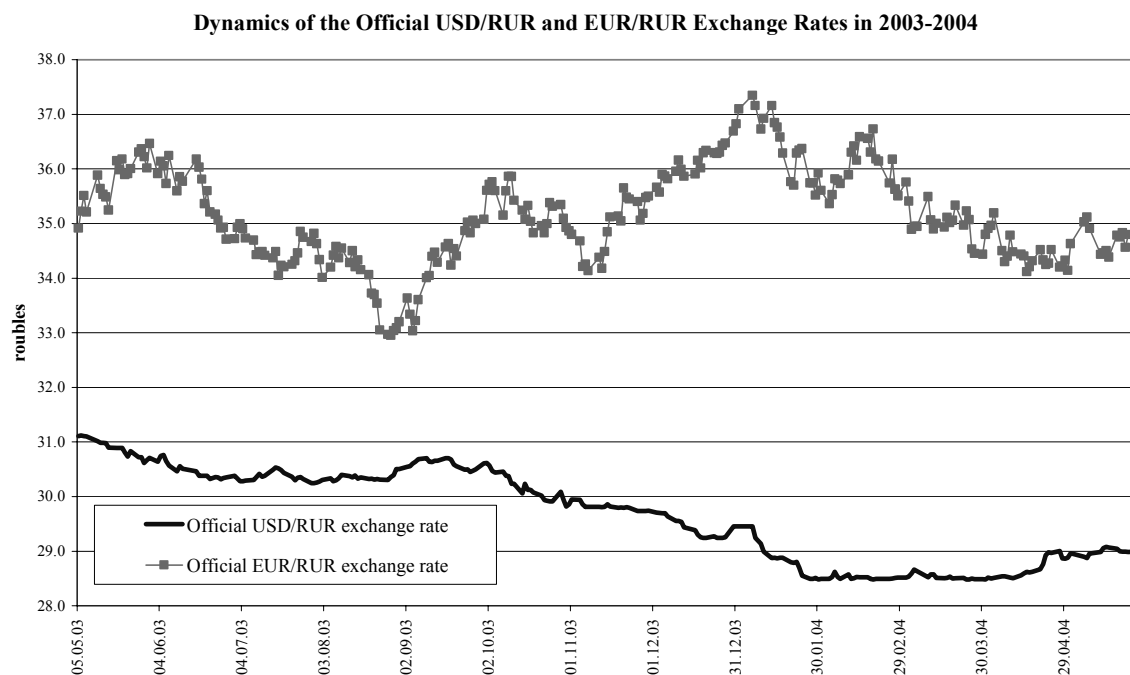
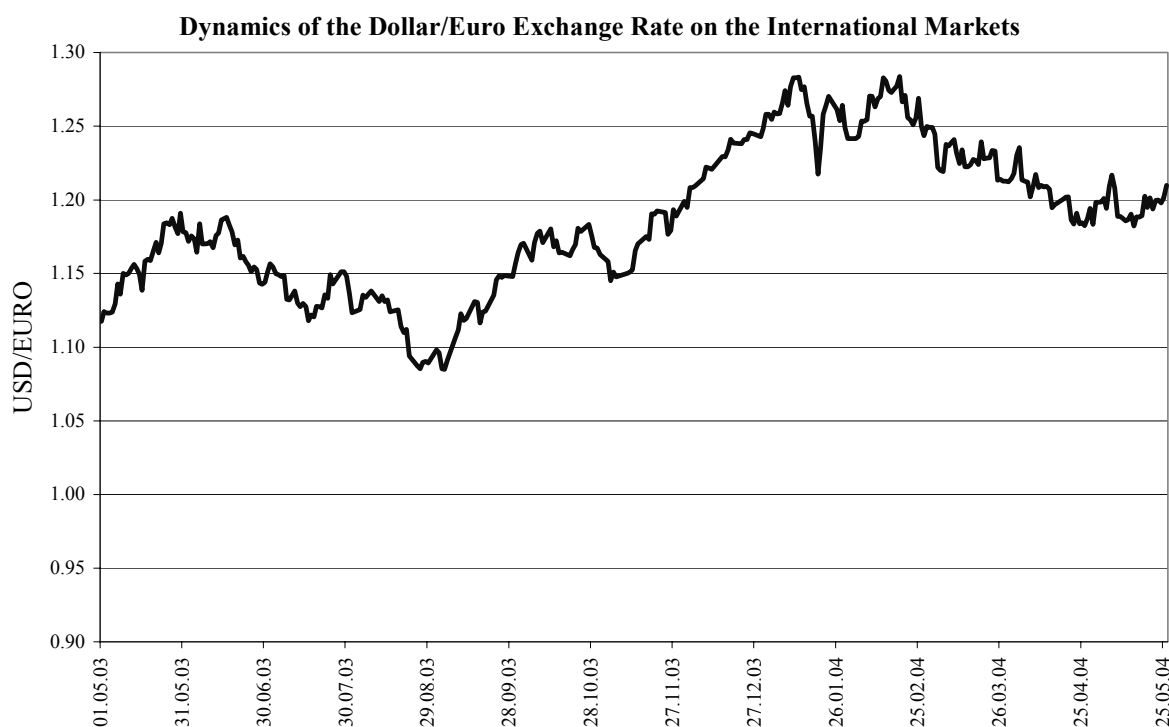


Figure 9.



In the period from April 31 till May 26, on the world forex markets there was observed no prevailing trend: in the beginning of the month there was observed a considerable appreciation of US \$ against Euro due to publication of positive macroeconomic statistics, however later the US \$ / Euro exchange rate returned to the band of about US \$ 1.2 per Euro because of the impact, among other factors, of high deficit of the US balance of payments. Thus, during this period of time the Euro exchange rate increased by US \$ 0.0124 making US \$ 1.209 per Euro.

The dynamics of the Euro - Ruble rate were mainly determined by the trends on the world market. In the period from April 30 till May 26, the European currency appreciated by RUR 0.75 (2.21 per cent) from RUR 34.14 per Euro and made RUR 34.89 per Euro. The aggregate turnover of trade at the SELT amounted to Euro 114.5 million in the period from May 5 till May 21 (Euro 115.6 million in April). In this period, the highest trade volume of Euro was registered on May 17 at Euro 16.9 million, and the lowest, Euro 3.89 million, on May 5.

Table 2

Financial Markets Indicators

| Month | January | February | March | April | May* |
|---|---------|----------|---------|---------|---------|
| Monthly inflation rate | 1,8% | 1,0% | 0,8% | 1,0% | 0,8% |
| Inflation rate annualized on the basis of this month's trend | 23,87% | 12,68% | 10,03% | 12,68% | 10% |
| CB RF refinancing rate | 14% | 14% | 14% | 14% | 14% |
| Annualized yield to maturity on OFZ issues (%) | 6,48% | 6,15% | 6,78% | 6,78% | 7,1% |
| Volume of trading in the secondary GKO-OFZ market for the month (RUR billion) | 31,77 | 25,47 | 50,55 | 21,72 | 20,0 |
| Yield to maturity on Minfin bonds at the end of the month (% p.a.) | | | | | |
| 5th tranche | 5,60% | 5,36% | 4,99% | 6,38% | 6,6% |
| 6th tranche | 4,01% | 3,88% | 3,54% | 4,31% | 5,1% |
| 7th tranche | 6,40% | 6,15% | 5,93% | 7,25% | 7,4% |
| 8th tranche | 4,77% | 4,56% | 4,22% | 4,58% | 5,6% |
| Yield to maturity of Eurobonds at the end of the month (% p.a.) | | | | | |
| 2005 | 2,83% | 2,77% | 2,40% | 3,00% | 3,4% |
| 2007 | 4,45% | 4,20% | 3,90% | 5,11% | 5,3% |
| 2010 | 5,79% | 5,68% | 5,51% | 6,34% | 6,6% |
| 2018 | 6,86% | 6,82% | 6,56% | 7,53% | 7,9% |
| 2028 | 7,33% | 7,25% | 7,07% | 8,10% | 8,5% |
| 2030 | 7,24% | 7,08% | 6,88% | 7,97% | 8,2% |
| INSTAR-MIACR rate (% p.a.) on interbank overnight loans at the end of the month | 2,15% | 1,76% | 6,19% | 17,54% | 10% |
| Official RUR / US\$ exchange rate at the end of the month | 28,4916 | 28,5156 | 28,4853 | 28,8834 | 28,9850 |
| Official RUR / Euro exchange rate at the end of the month | 35,3635 | 35,5076 | 34,8005 | 34,1431 | 35,6052 |
| Average annualized growth in RUR / US\$ exchange rate | -3,27% | 0,08% | -0,11% | 1,40% | 0,35% |
| Average annualized growth in RUR / Euro exchange rate | -3,97% | 0,41% | -1,99% | -1,89% | 4,28% |
| Volume of trading at the stock market in the RTS for the month (US\$ million) | 432,75 | 433,12 | 613,91 | 830,27 | 410 |
| Value of RTS-1 Index at the end of the month | 611,10 | 670,14 | 752,66 | 631,11 | 590 |
| Change in value of RTS-1 Index during the month (%) | 7,70% | 9,66% | 12,31% | -16,15% | -6,5% |

* Estimate

D. Polevoy

Enterprises and organizations: the state of payments

In the period from November of 2003 till January of 2004 the decline in outstanding and accumulated creditor indebtedness continued (see Figures 1 and 2). In January of 2004, the accumulated amount of outstanding indebtedness of organizations and enterprises in the economy made about 9.1 per cent of GDP (in 1998, in the period of the acute crisis, this indicator made 46 per cent (see Figure 1).

Figure 1.

**The level of accumulated payment arrears (as the share of GDP):
dynamics in 1993 through 2003.**



* - prior to (including) 1997 for four sectors.

** - estimate.

Source: RF Goskomstat, calculations of the authors.

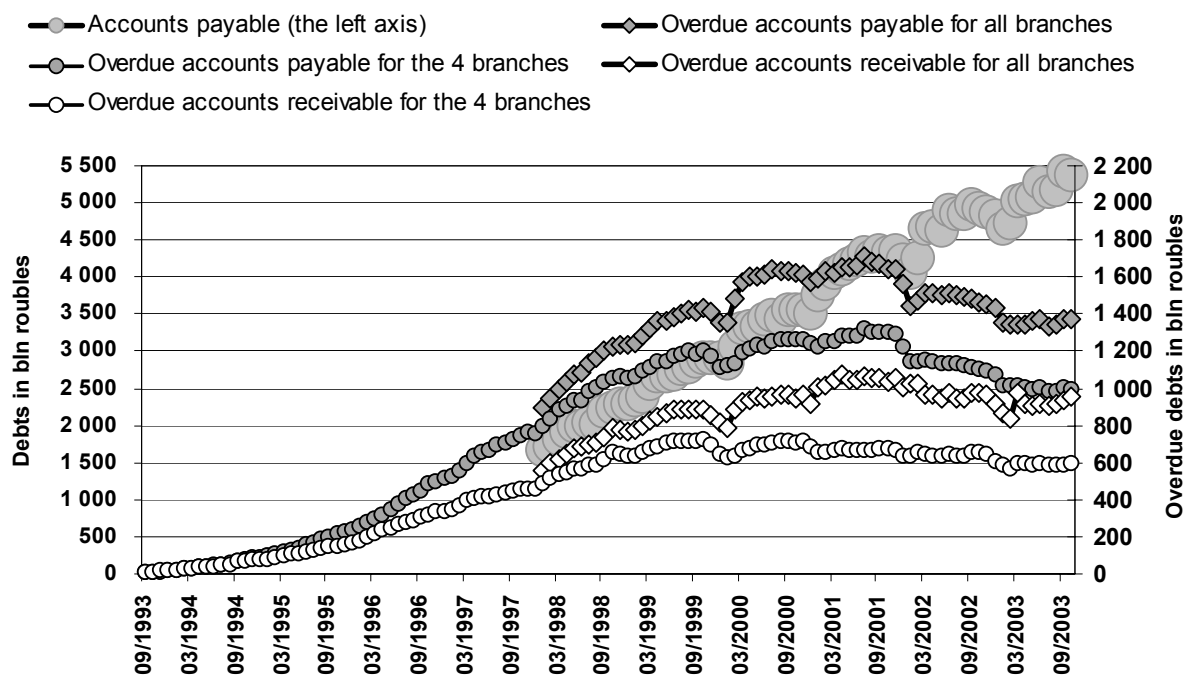
Note: the aggregate outstanding indebtedness of enterprises and organizations includes outstanding creditor indebtedness and the outstanding debts to the banking system. The creditor indebtedness is calculated as the sum of debts to suppliers, budgets of all levels, and extra-budgetary funds, indebtedness relating to wages and salaries, and debts to other creditors. Prior to 1998, the RF Goskomstat published payment arrears statistics for four sectors of the economy (industry, agriculture, transport, construction). Since 1998, the aggregate indebtedness in the economy has been calculated across all sectors of the economy.

The share of outstanding indebtedness in the total indebtedness continues to decline and makes about 25 per cent (the maximum – 55 per cent was observed in 1998, see Fig. 3).

In the first month of 2004, the amount of outstanding creditor indebtedness declined by 7.5 per cent (Rub. 98 billion). In the respective period of 2003, the outstanding creditor indebtedness decreased by 5.4 per cent, while the total decline in outstanding creditor indebtedness in 2003 made 8.9 per cent. There may be noted a certain increase in write off of outstanding indebtedness in 2003 in comparison with the figures registered in preceding periods, what indicates a certain intensification of processes of restructuring (see Table 1).

Figure 2

Dynamics of outstanding creditor and debtor indebtedness across all sectors of the economy and branches of industry, agriculture, construction, and transport (4 sectors) in current prices.



Source: RF Goskomstat, calculations of the authors.

Table 1

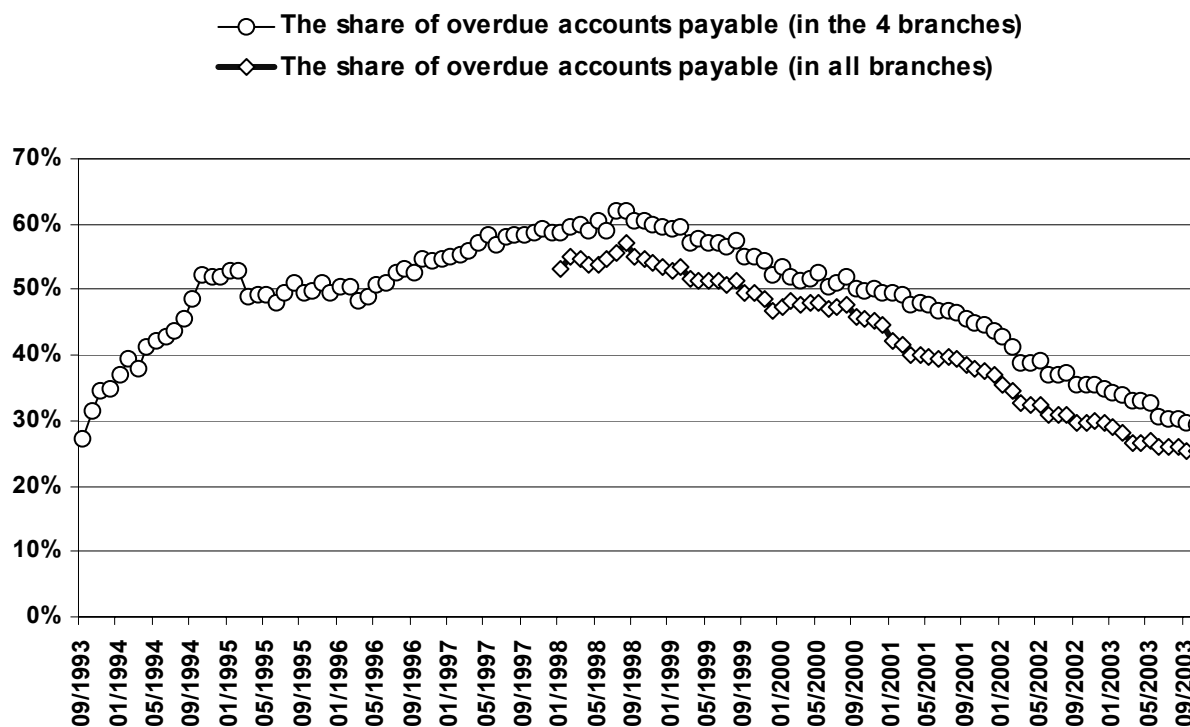
Amounts of outstanding indebtedness of economic agents written off to financial results.

| Period | Creditor indebtedness written off to profit | | Debtor indebtedness written off to losses | |
|---------------|---|---------------------------------------|---|-------------------------------------|
| | Total, Rub mil | in % to overdue creditor indebtedness | Total, Rub. mil. | in % of overdue debtor indebtedness |
| 1997 | 874 | 0,1% | 1 921 | 0,4% |
| 1998 | 2 777 | 0,2% | 7 990 | 1,0% |
| 1999 | 5 597 | 0,4% | 12 420 | 1,5% |
| 2000 | 6 598 | 0,4% | 21 955 | 2,4% |
| 2001 | 10 185 | 0,7% | 25 783 | 2,6% |
| 2002 | 12 861 | 0,9% | 24 000 | 2,6% |
| 2003 | 19 996 | 1,5% | 37 035 | 4,2% |
| 1/2004 | 337 | 0,0% | 548 | 0,1% |

Source: RF Goskomstat, calculations of the authors.

Figure 3

Dynamics of the share of outstanding creditor indebtedness in the total creditor indebtedness.



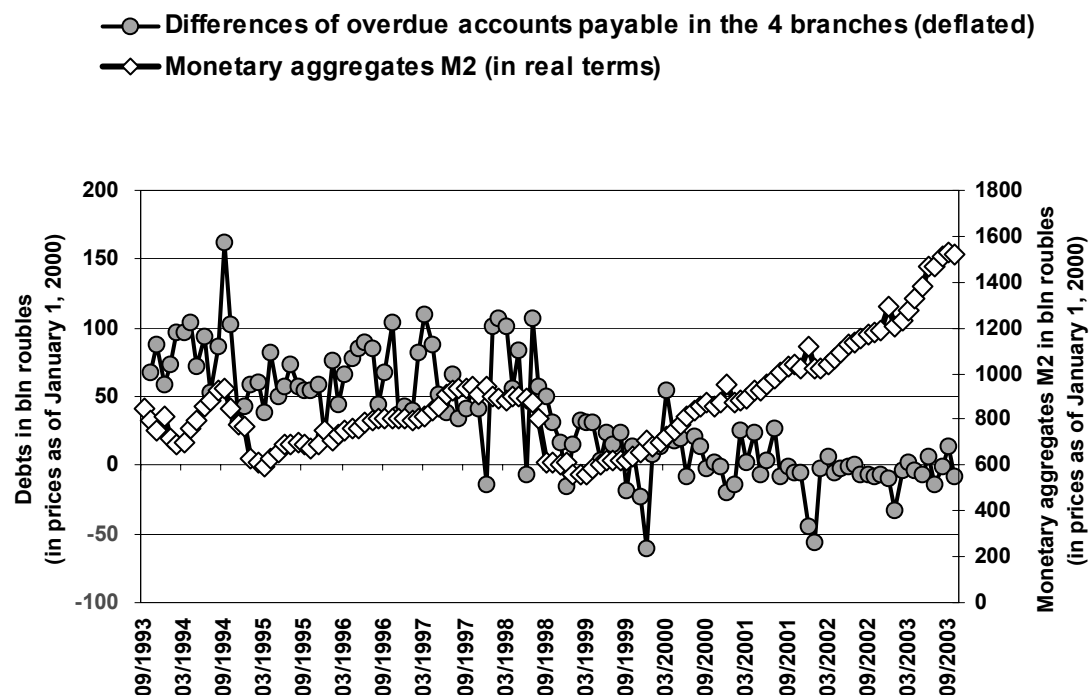
Source: RF Goskomstat, calculations of the authors.

Apparently, the growth in bank crediting and increase in demand for real cash balances played a positive role in normalization of payments. While before 1999 the dynamics of increase in non-payments mirrored the dynamics of money supply (see Figure 4), what to a certain extent characterized outstanding commercial credits as a substitute for bank crediting, since 2000 the dynamics of payment arrears and money supply diverge, what is an evidence of cash types of crediting squeezing out non-cash types. These trends are also observed in the structure of payments between monopolistic enterprises¹² (see Figure 5). The share of cash payments made by these enterprises continues to grow and makes more than 90 per cent according to the data for January of 2004.

¹² According to RF Government Resolution No. 10 of January 6, 1998, the RF Goskomstat conducts statistical monitoring of payments of largest Russia's taxpayers: "UES of Russia," "Gazprom," "Aeroflot – Russian international airlines," organizations of the federal railroad transport, and industrial monopolistic organizations.

Figure 4

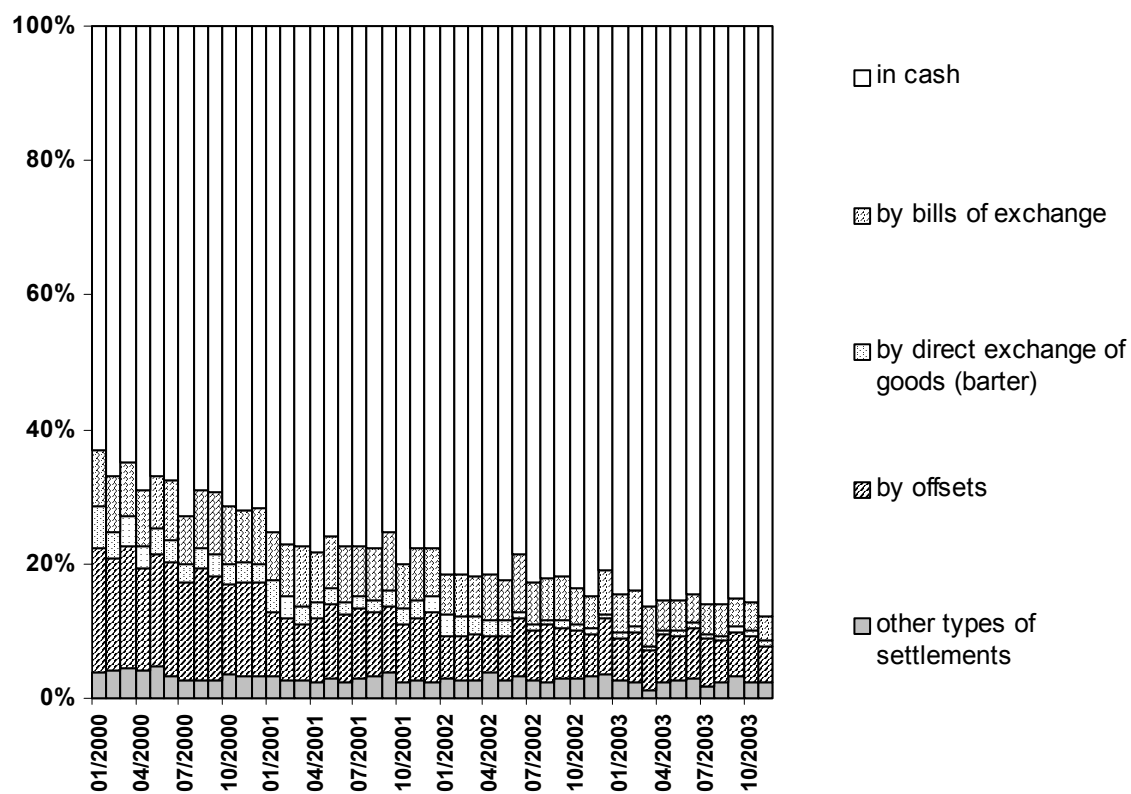
Dynamics of increment in outstanding indebtedness and money supply (M2).



Source: RF Goskomstat, CB of RF, calculations of the authors.

Figure 5

Monopolistic enterprises: the structure of payments for shipped products.

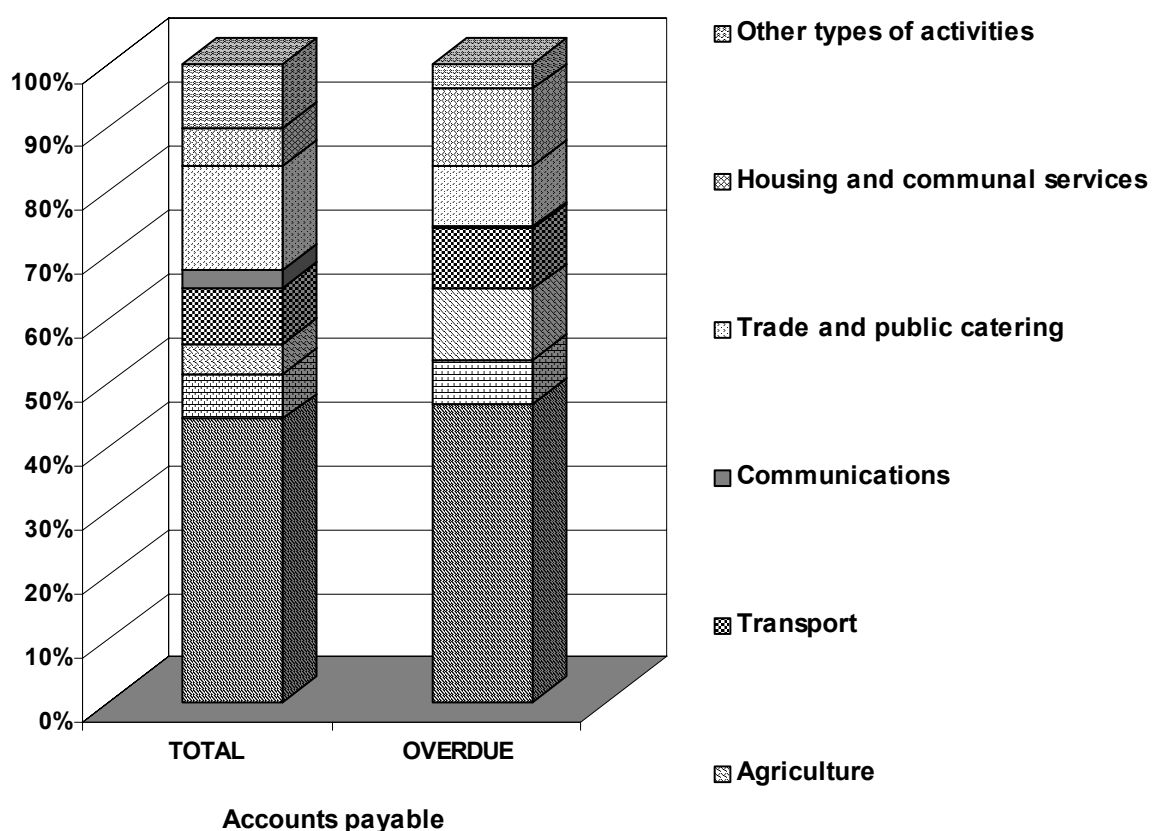


Source: RF Goskomstat, calculations of the authors.

As concerns the sectoral structure, debts of industry stable make the major share of the total and outstanding indebtedness (see Figure 6). At the same time, while the share of the industrial sector makes about 42.1 per cent in the total amount of creditor indebtedness, it makes 46.1 per cent in the total outstanding indebtedness (the figures as in January of 2004). It shall be noted that the share of industry in outstanding creditor indebtedness has somewhat increased in comparison with the figures registered in October of 2003. Similarly, housing and public utilities, agriculture, and transport (since January of 2002) have accounted for a larger share in the outstanding creditor indebtedness than in the total amount of indebtedness. This ratio indicates that repayment of commercial credits in these sectors is more often delayed as compared with other sectors. For instance, outstanding debts make 59.3 per cent in creditor indebtedness of agriculture and 52.1 per cent of indebtedness of housing and public utilities. On the average, this indicator makes 24.7 per cent in Russia.

Figure 6

Structure of creditor indebtedness across base sectors of the economy by the end of February, 2003.



Source: RF Goskomstat, calculations of the authors.

Among industries, the leaders in terms of their share of outstanding indebtedness in the aggregate creditor indebtedness are coal industry (67 per cent, see Table 2), electrical power engineering (40 per cent), light industry (41.3 per cent), and microbiological industry (77 per cent). However, while the amounts of indebtedness of two latter industries are relatively small, debts of electrical power engineering and branches of fuel industry total to about one third of the total indebtedness in the economy on the whole. The largest consumer of commercial credits in absolute terms are branches of mechanical engineering and metal working, as well as fuel industry. It shall be noted that there was observed a significant decrease in the amount of outstanding debts of natural gas industry and ferrous metallurgy in 2003.

Table 2

Structure of creditor indebtedness across industries as in end of February of 2003

| Industries | Creditor indebtedness | | Share of outstanding indebtedness in the total indebtedness, % | | Share of creditor indebtedness of the industry in the aggregate indebtedness of the industry on the whole, % | Share of outstanding creditor indebtedness of the industry in the aggregate indebtedness of the industry on the whole, % |
|---|-----------------------|---|--|-----------------------------|--|--|
| | Total, Rub. billion | Including outstanding debts, Rub. billion | Jan. 2004 | Memorandum, October of 2003 | | |
| Industry, total | 2060000 | 556800 | 27,03% | 26,02% | 100,00% | 100,00% |
| Including, electrical power engineering | 237600 | 95200 | 40,07% | 42,04% | 11,53% | 17,10% |
| Fuel industry | 527900 | 117400 | 22,24% | 16,17% | 25,63% | 21,08% |
| Including | | | | | | 0,00% |
| Oil extracting industry | 233300 | 12500 | 5,36% | 3,75% | 11,33% | 2,24% |
| Oil processing industry | 59700 | 17800 | 29,82% | 21,88% | 2,90% | 3,20% |
| Natural gas (extraction and processing or natural and casing head gas) | 149600 | 29700 | 19,85% | 15,15% | 7,26% | 5,33% |
| Coal industry | 84400 | 56700 | 67,18% | 67,87% | 4,10% | 10,18% |
| Ferrous metallurgy | 108500 | 18300 | 16,87% | 21,60% | 5,27% | 3,29% |
| Non-ferrous metallurgy | 120800 | 34000 | 28,15% | 29,52% | 5,86% | 6,11% |
| Chemistry and petrochemistry (without chemical pharmaceutical industry) | 107600 | 29500 | 27,42% | 34,68% | 5,22% | 5,30% |
| Mechanical engineering and metal working | 583400 | 164700 | 28,23% | 28,60% | 28,32% | 29,58% |
| Forestry, woodworking, and pulp and paper industry | 54800 | 18400 | 33,58% | 37,99% | 2,66% | 3,30% |
| Industry of construction materials | 53900 | 19100 | 35,44% | 38,21% | 2,62% | 3,43% |
| Glass, porcelain, and faience industry | 8200 | 2000 | 24,39% | 28,92% | 0,40% | 0,36% |
| Light industry | 30000 | 12400 | 41,33% | 42,74% | 1,46% | 2,23% |
| Food industry | 170100 | 22500 | 13,23% | 15,16% | 8,26% | 4,04% |
| Including fish industry | 23100 | 4300 | 18,61% | 20,90% | 1,12% | 0,77% |

| Industries | Creditor indebtedness | | Share of outstanding indebtedness in the total indebtedness, % | | Share of creditor indebtedness of the industry in the aggregate indebtedness of the industry on the whole, % | Share of outstanding creditor indebtedness of the industry in the aggregate indebtedness of the industry on the whole, % |
|--|-----------------------|---|--|-----------------------------|--|--|
| | Total, Rub. billion | Including outstanding debts, Rub. billion | Jan. 2004 | Memorandum, October of 2003 | | |
| Microbiological industry | 3000 | 2300 | 76,67% | 70,00% | 0,15% | 0,41% |
| Flour, grits, and combined fodder industries | 15600 | 3000 | 19,23% | 22,42% | 0,76% | 0,54% |
| Medical industry | 9000 | 1700 | 18,89% | 19,78% | 0,44% | 0,31% |
| Printing industry | 6700 | 200 | 2,99% | 2,99% | 0,33% | 0,04% |

Source: RF Goskomstat, calculations of the authors.

The further developments in the sphere of payments will depend on the situation in the real sector of the economy and the level of budget revenues. It should be noted that the most acute danger for softening of budgetary constraints (weaker enforcement) is a budget crisis. However, at present the persistence of positive rates of growth in spite of certain negative trends as concerns the recovery of growth in payments arrears, such as Ruble appreciation, provide grounds for positive expectations in the sphere of inter-enterprise payments.

O. Lugovoi

The Real Sector: Factors and Trends

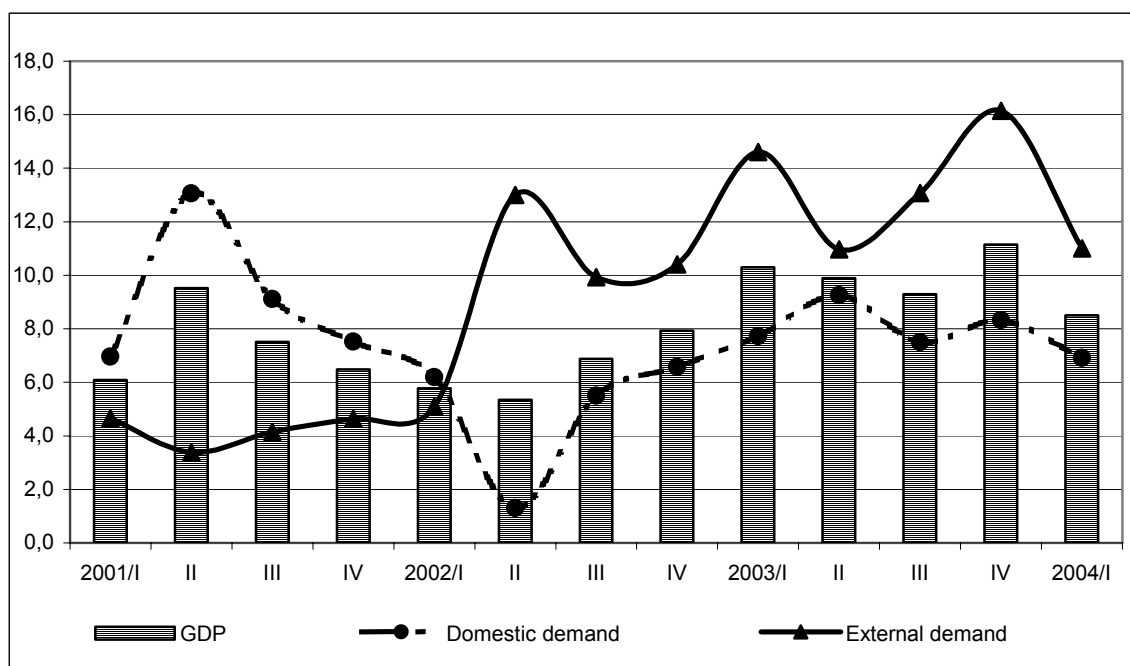
According to the preliminary data for the 1st quarter of 2004 published by the RF Ministry of Economic Development, GDP increased by 8.0 per cent in comparison with the respective period of the preceding year. In the Russian economy, there persists the trend towards an outpacing rate of growth in investment as compared with GDP dynamics and expenditures for final consumption.

As concerns the sector of production of goods, there dominating influence has the expanding business activity in construction. The amount of works in construction increased by 13.8 per cent, while the industrial output grew by 7.4 per cent. In the sector of services, the increase in the turnover of retail trade made 10.7 per cent in comparison with the figures registered in the 1st quarter of 2003 due to an intensive expansion of the effective household demand.

According to the preliminary data for the 1st quarter of 2004 published by the RF Ministry of Economic Development, GDP increased by 8.0 per cent in comparison with the respective period of the preceding year. The dynamic development of the national economy was supported by the persisting high rates of growth in production across practically all sectors of the economy. The output of products and services of the base economic sectors increased by 7.9 per cent as compared with the figures registered in January through April of 2003. The expanding amount of works in construction (by 13.8 per cent) and turnover of retail trade (by 10.7 per cent) had the dominating influence on the changes in the structure of production. In January through April of 2004, the rates of growth in industrial output made 107.4 per cent as compared with 106.3 per cent observed in the respective period of the last year. This ratio between the rates of development in different sectors reflects the specific nature of the factors of economic dynamics observed in the 1st quarter.

Figure 1

Changes in the dynamics of GDP, domestic and external demand in 2001 through 2004, in % of the figures registered in the respective quarter of the preceding year.



The acceleration of the dynamics of the development of the Russian economy took place at the background of expansion of both domestic and external demand. Due to the exceptionally favorable world business situation on the markets of hydrocarbon raw materials and metals, in the 1st quarter of 2004, the amount of Russian export of goods, according to the estimates made by the RF Ministry of Economic Development made US \$ 37.3 billion and increased by 20.0 per cent in comparison with the figures registered in the preceding year. More favorable conditions of trade with export goods resulted in an increase in the positive balance of trade in the 1st quarter of 2004 up to US \$ 18.1 billion as compared with US \$ 15.3 billion registered in the 1st quarter of 2003 and was a factor behind the expanding domestic revenues in the economy.

The comparison of dynamics of the amounts and volumes of exports, as well as the rates of production demonstrates that intensity of production of export oriented industries gradually decrease at the background of growing influence of the business situation on the world market. The possibilities to further expand exports are limited due to both production capacities of producers, and delivery capacity of transport communications. Besides, while at present the market of hydrocarbon products is characterized by a rather stable expansion of supply determined primarily by the revival of the world economy, the specifics of the market of metals, which has the cyclic nature of demand, were restrained reaction of producers to the changes in the scale of output. As a result, this year there was observed a declining rate of growth in fuel industry and metallurgy. In January through April of 2004, the increase in production of fuel industry made 8.5 per cent, including oil extracting industry, where the growth in output was registered at 10.7 per cent, what was by 1.4 and 2.8 p. p. below the respective indicators registered last year. As concerns ferrous metallurgy, in January through April the growth in production there made 106.0 per cent in comparison with 109.7 per cent registered in the respective period of the last year, while in non-ferrous metallurgy the increase in output made 104.3 per cent as compared with 108.6 per cent.

The slowing down of the rates of growth in output observed in the fuel and metallurgy complex occurred at the background of an intensive increase in average actual export and domestic prices of the products of export oriented industries. As domestic prices of production of export oriented industries of the raw materials sector grew, the pressure of these prices on manufacturing industries increased. In April of 2004, the growth in producer prices of manufacturers of industrial products outpaced the changes in consumer prices by almost 8 p. p. Thus, only in the first four months of this year, the increase in prices of products of mechanical engineering made 7.2 per cent, while in the construction materials industry and food industry the respective indicators were at 7.5 per cent and 5.9 per cent.

Table 1

Price indices of producers of industrial output in January through April of 2004.

| | As compared with the figures registered in the preceding month | | | | As compared with the figures registered in December of the preceding year | |
|-------------------------------------|--|----------|-------|-------|---|---------------|
| | January | February | March | April | April of 2004 | April of 2003 |
| Industry, total | 104,2 | 103,4 | 101,7 | 102,7 | 112,5 | 104,6 |
| Electrical power engineering | 104,0 | 106,5 | 100,2 | 100,1 | 111,0 | 112,4 |
| Fuel industry | 110,9 | 104,1 | 101,5 | 103,8 | 121,6 | 95,2 |
| Oil extracting industry | 106,0 | 105,0 | 101,5 | 103,7 | 117,1 | 89,1 |
| Ferrous metallurgy | 102,9 | 105,3 | 107,5 | 115,1 | 134,0 | 115,0 |
| Non-ferrous metallurgy | 103,7 | 103,0 | 100,1 | 100,5 | 107,4 | 111,9 |
| Mechanical engineering | 102,4 | 102,1 | 101,4 | 101,3 | 107,2 | 103,8 |
| Industry of construction materials | 101,1 | 102,4 | 100,9 | 102,9 | 107,5 | 105,6 |
| Light industry | 101,8 | 101,9 | 100,5 | 100,7 | 104,9 | 104,8 |
| Food industry | 101,6 | 101,6 | 101,1 | 101,5 | 105,9 | 102,4 |
| Memorandum: Consumer price index | 101,8 | 101,0 | 100,8 | 101,0 | 104,6 | 106,2 |

Source: Federal Service of State Statistics

Simultaneously, a significant impact on the domestic market had the relative reduction in prices of imported products caused by the changes in the Ruble exchange rate. In the 1st quarter of 2004, import of goods made US \$ 17.2 billion, what was by 21.3 per cent above the level registered in 2003. The situation was aggravated by the fact that the scale of supply of domestic goods did not correspond to the scale of expansion of domestic demand. The increase in import of consumer and investment products was accompanied by the changes in the competitive environment and gradual squeezing of Russian producers out of markets. As compared with the figures registered in 2003, the share of domestically produced goods in the total amount of available resources decreased by almost 2 p. p. (as compared with the figures observed in the 1st quarter of 2003). This circumstance may explain the unexpectedly low contribution of industry in the dynamics of economic growth observed in the 1st quarter of 2004.

At the same time, in the beginning of this year there persisted the trend towards a gradual improvement of the structure of industrial growth. While the export oriented sector of industry kept its leading position, it to a certain degree transformed the growth in external demand in an expansion of the domestic market. The positive conditions of growth in production in final industries were, first, expansion of consumer demand for nonfood products basing on increasing real household incomes and real wages and salaries, and, second, increase in investment demand initiated by growing profitability of production and net capital inflow in the sector of non-financial corporations. In January through April of 2004, the growth in production of mechanical engineering made 15.3 per cent, in the industry of construction materials – 10.4 per cent, in food industry – 8.8 per cent, while the output of intermediate goods increased by about 6.8 per cent to 7.0 per cent. These dynamics of industrial growth was significantly different from the situation observed in the 1st quarter of 2003, when the increase in production of final industries was at 3.5 per cent, and industries of the raw materials sector made about 10 per cent.

The changes in proportions of industrial growth illustrates a gradual development of the processes of transformation of export revenues of the economy in the expansion of the domestic market. As the experience accumulated over the last five years demonstrates, exactly the prevailing influence of the dynamics and structure of domestic demand has the decisive impact on the rates of the recovery growth.

O. Izryadnova

IET Business Survey: Industry in May of 2004

The first results of May demonstrate the persistence of positive trends in the dynamics of Russia's industry. The increasing rates of growth in demand occurring at the background of slightly decelerating rates of increase in output made producers to use their finished stocks. In a few next months, a decline in the volumes of finished stocks should result in an intensification of growth in output aimed at the replenishment of stocks and satisfaction of current demand.

According to the Federal Statistics Service, in April of 2004 the upward trend in the growth in industrial output resumed. After the pause observed in March, according to the evaluations of the Center for Macroeconomic Analysis and Short Term Prognostication (CMASTP), in April the average daily output increased by 0.8 per cent, what was twice as much as the average rate of growth registered in the 1st quarter. In the case the present trend persists, the CMASTP estimates that the index of industrial production in 2004 will be at 106.5 per cent to 106.7 per cent. According to the data presented by the Ministry of Economic Development and Trade, in January through April of 2004 industrial output increased by 7.4 per cent in comparison with the figures registered in the respective period of 2003. In April of 2004, the growth made 6.7 per cent. Developments in April of 2004 were characterized by intensifying growth across all sectors of the economy. Powerful growth was observed in mechanical engineering and production of construction materials; at the same time, in light industry there was registered a certain stagnation. Over four months, exports made US \$ 51 billion (a 23 per cent increase in comparison with the figures observed in January through April of 2003), while imports increased by 21 per cent and made US \$ 27 billion.

The first results of May demonstrate the persistence of positive trends in the dynamics of Russia's industry. The dynamics of effective demand were very stable in May. In spite of traditional long holiday period, the results of surveys did not registered any growth in cash sales both in the industry at large, and in the majority of individual industries. The only exceptions were light industry and the forestry complex. However, the results of surveys adjusted for seasonal factors demonstrated an intensive increase in demand at the rates last registered in 2000.

However, enterprises were not satisfied with even such positive dynamics. Evaluations of demand demonstrated that enterprises expected even more intensive growth. In May, the share of "normal" evaluations of demand again declined and were below 50 per cent, while the share of evaluations "below norm" increased. The most significant downward reevaluation of demand occurred in mechanical engineering and light industry.

In May, the rates of growth in industrial output decreased by several balance points in comparison with April figures in spite of persisting rates of growth in sales. However, taking into account the fact that in April both IET surveys and official statistics registered high rates of growth, a slight decline in May results is not alarming. It is not surprising that these developments resulted in the phenomenon, which has been rarely observed over the last years, i.e., the growth in the share of enterprises where changes in output lagged behind changes in demand. In May, there were registered 23 per cent of such enterprises, while in the last few months there were registered from 9 per cent to 13 per cent of such enterprises. This indicator was most significant in electrical power engineering and fuel industry (62 per cent), as well as in metallurgy and food industry (33 per cent each).

The outpacing rates of growth in sales made enterprises to resort to their finished stocks. These developments resulted in a further decline in the balance of evaluations by 5 points. As a result, in April through May the redundancy of finished stocks decreased by 11 points. At the same time, a shortage of finished stocks was already registered in chemistry, petrochemistry, and construction industry.

The post-default industrial growth allowed enterprises to put idle capacities in operation. In 1996, redundant capacities were registered at 63 per cent of enterprises. However, by 2004 this reserve for expansion of production appeared to be exhausted. In the last 2 quarters, the share of enterprises reporting about idle capacities because of insufficient demand has stabilized at 24 per cent level, while the share of enterprises with a lack of capacities on the contrary increased and made 12 per cent to 13 per cent.

The of the most recent (April of 2004) survey of competition and the share of competitive markets characterized by competition with producers from countries outside the NIS did not show growth in these indicators. Since October of 2003, the share of competitive markets has declined by 2 p. p. (see the Figure below). At present, the share of such markets according to enterprises' assessments is at 60 per cent, while the respective maximum was registered in April of 1998. The share of competitive markets characterized by domestic Russian competition remained at the same level (91 per cent).

As a result, the index of competition against producers from countries outside the NIS declined from 3.13 to 3.10. Therefore, the stable increase in this indicator registered in April of 2002 through October of 2003 has stopped. The index of domestic Russian competition continues to grow. In April of 2004 its value exceeded the "moderate" level for the first time since the start of monitoring.

The decline in the values of indicators characterizing competition with producers from countries outside the NIS at the background of increasing volumes of import may be explained by the growing gap in quality between domestic and imported products. This fact is demonstrated by enterprises' evaluations of factors

behind the non-competitiveness of their products. Obsolete equipment (1st place, 71 per cent), high energy consumption (high (!) prices of energy resources were ranked 2nd, 54 per cent), and low level of research and development of new products (3rd place, 45 per cent) result in low quality of domestic products in comparison with imported analogues (4th place, 30 per cent). In this situation, operations involving Ruble exchange rate factors may help only 8 per cent of Russian enterprises. Exactly this number of enterprises believe that Ruble appreciation against the US dollar negatively affects the competitiveness of their products.

The forecasts of changes in demand increased by 4 p. p. in May after two months of decline. In the few next months, a growth is possible in all industries with the exception of electrical power engineering, non-ferrous metallurgy, and light industry.

As concerns the plans of changes in output, there is also observed the recovery of optimism (which declined before the May holidays). Again, more than half of enterprises intend to increase their output. A decline in production is possible only in timber, wood working, and pulp and paper industry.

S. V. Tsukhlo

Russia: Draft Law on Regulating Agriculture

A group of RF State Duma deputies headed by G.V.Kulik has introduced a draft Law on regulating agriculture.

At present there are some agricultural development issues in Russia that are not regulated by the effective legislation. In particular as different from most other countries there is no legal definition of an agricultural producer: each normative act contains its own definition and this is not convenient for laws' execution. The competence of federal and regional authorities in supporting agriculture is not delineated. As a result regions implement support programs that disrupt the country's common market space and actually launch trade wars between regions. There is also no clear delineation of agricultural regulation competence between federal agencies leading to long-lasting coordination of efforts and as a result – to their being late, to the loss of regulation flexibility and to poorer responsibility for agrifood policies carried out in the country. The applying for humanitarian aid in 1998 caused serious damage to the Russian agrifood sector demonstrating that this issue is non-elaborated as well. The lack of legally guaranteed equal access to market information becomes a factor of unfair competition on the agricultural and food markets: large companies able to collect their own market information or companies having access to official information get market advantage over the rest. Besides, non-equal access to official information becomes a factor of corruption in agencies administering the agrifood sector.

The second factor necessitating a Law on agricultural development and agrifood policies is the need for longer termed budget planning in the sector. On the average in the current macroeconomic situation farm and food sector entities plan their operation for 3-4 years ahead while the state agrarian policy is formulated only for one year. This destabilizes business environment in the sector. In view of the above it's urgent to elaborate regular laws on state support to the agrifood sector for 3-4-year term encompassing approximate budget projections that could be revised in the framework of annual budget procedure but would still enable market agents to make medium-term business plans.

The introduced draft law consists of two parts. The first part includes permanent statutes while the second establishes the actual regime for agrifood sector regulation in 2005-2007.

The key novelties of the first part of the Law are:

1. Definition of an agricultural producer.

For the first time the Law gives a uniform definition of an agricultural producer irrespective of its organizational and legal status, size and registration.

2. State programs for regulating agriculture and agrifood market.

It's specified that federal agrifood policies are carried out through State programs. The Law defines the State program for regulating agriculture and agrifood market as a complex of measures targeted at the solution of specific social and economic problems in the agrifood sector, consistent with the goals of state agrifood policies, having time limits, discontinued after the proclaimed goals are attained and executed by state governing bodies.

Each program should contain specified goals, basic measures for attaining them, the amount and sources of financing in each year, requirements to program participants, mechanisms of budget funds' distribution between participants, qualitative and quantitative indicators of attained goals. Such programs make the es-

sence of the second part of the Law. They substantiate expenditures on the agrifood sector in the Budget Law.

3. Medium-term planning of agrifood policies.

The second part of the Law is adopted for the period not shorter than three years enabling market agents to adjust their operation to medium-term policies of the federal government.

Besides, the legal adoption of State programs enables to expand the competence of authorized federal executive bodies in taking decisions under the implemented programs. Many measures of market regulation require prompt response of the regulating body. Under the current legal system an authorized body has to coordinate its actions with other agencies and as a result the taken measures are not enough prompt and efficient. On the other hand, more freedom in decision-taking raises the authorized body's responsibility for the conducted agrifood policies.

4. Examination of results of implementing State programs for regulating agriculture and agrifood market.

The Law envisages an independent examination of agrifood policy results. On the basis of this examination State programs for the following period are worked out, the decisions are taken for each program whether to prolong, to modify or to discontinue it, other programs are adopted.

Such an examination should be done by an Independent commission including representatives of federal executive bodies, regional authorities, independent experts, associations of agricultural producers and consumers of agricultural and food products, other non-commercial organizations. The share of state officials in the Independent commission should not exceed thirty percent. Such a composition of the commission is to ensure its real independence and due respect to opinions of all market agents and experts.

Until now the efficiency of support measures was actually evaluated by their elaborators and executors that is surely not optimal.

5. National report on results of agrifood policies and performance of the agrifood sector.

Each year the Minister of Agriculture presents a National report on results of agrifood policies and performance of the agrifood sector, giving a public account of execution of all programs for supporting the sector in the past year.

The National report should contain the description of agrifood policies' general results as well as the assessment of effect of specific programs implemented in compliance with the Federal Law on regulating agriculture and agrifood market, and proposals for modifying agricultural policies.

The National report is examined and adopted by the Russian Federation's Government and then is introduced to the RF Federal Assembly.

6. Competence of the authorized executive body.

The adoption of regular Law "On regulating agriculture and agrifood market" makes the authorized executive body fully responsible for the implementation thereof endowing it with certain competence. Besides, in order to prevent the disruption of common agrifood markets in the country the federal governing bodies are granted the exclusive right to regulate them.

7. The state system of informational support to the agrifood sector.

The Law principally changes the role of informational support to the agrifood sector. It is declared one of the priorities of state agrifood policies aimed to ensure fair competition between agrifood market agents. The Law creates legal pre-requisites for equal access to information for all of them.

The Law establishes a list of data that the state undertakes to gather and disseminate among market agents and guarantees to them equal and single-moment access to information.

8. Food Code of the Russian Federation.

Russia joined the International Food Code (adopted by the UN Food and Agricultural Organization and the World Health Organization) but as yet has no national Food Code of its own. The Law urges the Government to work out and to adopt such a Code as a complex of national technical norms in the agrifood sector in compliance with the law on technical regulation.

9. State regulation of agrifood market in case of emergency.

The Law establishes the pattern for RF Government's actions in case of emergency caused by natural calamities (liquidation of damage done by them), economic situation (compensation of agriculture's losses in case of extreme worsening of price parity) or in case of threat to the population's food security.

10. Sustainable development of rural areas.

Measures supporting sustainable development of rural areas are an integral part of agrifood policies. They should be targeted at the diversification of rural economy, expansion of employment opportunities and

growth of rural residents' incomes, development of social and engineer infrastructure, safeguarding of rural landscapes and natural environment.

These measures should be financed not only from funds of federal and regional budgets allocated to agriculture but also from budget funds allocated to development of other branches of economy (education, health care, culture, transport, etc.).

The second part of the Law consists of 15 programs divided in three groups. The first group contains programs rendering general support to agricultural producers. Some of the currently effective programs that proved to be successful were retained therein, e.g. the subsidizing of interest on short- and medium-term credits, subsidies to pedigree stock breeders and elite seed growers, subsidies for melioration works and planting of perennial plantations.

The mechanism of supporting technical re-equipment of agriculture was notably changed. Instead of the state leasing program effective since 1994, a new mechanism is proposed that is free from the basic drawbacks of the previous one. For instance, agricultural producers are supposed to get subsidies equaling 70% of their initial installment under the leasing agreement irrespective of who is the lessor. The state will no longer set the list of eligible purchased machinery. The Law also provides for higher subsidies in case of purchasing new machinery.

Programs for supporting rural credit cooperation and newly formed family farms are envisaged as well.

Two new programs – the one for subsidizing purchase of fuels and oils and the other for supporting credits to agricultural producers with low financial stability – raise serious doubts. The first program is fraught with outflow of subsidized fuels and oils from agriculture to other markets and low efficiency for primary agricultural production. The second program attempts to solve the problem of credit availability for loss-making farms that seems to be a wrong idea.

The second group of programs is targeted at the regulation of agrifood markets. Three major markets are selected – those of grain, meat and sugar. Two basic mechanisms are proposed for regulating grain market aimed to mitigate seasonal price fluctuations. First of all, this is the establishing of price corridor (the upper and the lower guaranteed prices). In case the actual grain prices fall below the minimal level, the state undertakes to buy grain until price for it rises to the guaranteed level. In case prices exceed the upper limit market interventions will be carried out. The above operations are proposed for wheat #3 and #4, feed barley and rye.

Besides, the mechanism is worked out for compensating to agricultural producers a part of expenditures on seasonal storage of grain. Producers can use this grain as a security for subsidized (on common terms) credit. Banks that issued credits under such a security are guaranteed the purchase of this grain at minimal price.

The experience of some Central and East European countries demonstrated that this mechanism will most likely lead to the spread of warehouse receipts on the grain market but won't require real interventions.

For regulating meat market it was proposed to preserve quantitative quotas for import of poultry meat but to abandon them for import of beef and pork (these two food items will be subject to combined import tariffs).

On the market of sugar the currently effective regulating mechanism (introduced in December 2003) is preserved.

Besides, the government promises not to constrain export of agrifood products (except cases when grain market interventions are carried out) and to apply quantitative limits on import of regulated products from the CIS countries until their trade regimes are harmonized.

The tools for fostering rural social development actually pattern the mechanism of currently effective special program of the same name.

The basic virtue of the introduced mechanisms is their direct action excluding the distributive procedure in allotting subsidies that was effective up till now. Actually the Law lifts the subsidizing limit that left a large field for voluntarism and corruption and did not guarantee agricultural producers an access to promised state support. Second, a limit is set on the amount of subsidies granted to one producer ensuring their more socially fair distribution.

Despite some serious (from our point of view) imperfections of the draft Law it still signifies a notable progress in the legislative agricultural policy making in the country.

E. Serova, O. Shick

Foreign Trade

The favorable business situation on the world markets, Ruble appreciation and increasing effective domestic demand still facilitate the growth in the Russian foreign trade turnover. The key indicators characterizing the development of foreign trade in the 1st quarter of 2004 are at record highs over the last 10 years.

In May, the European Union agreed to the Russia's accession to WTO. Russia could defend its relatively low domestic prices of natural gas, which, however, will gradually increase. EU may expect a reduction in import customs duties on motor vehicles and aircraft, as well as access to new insurance and long distance communications services.

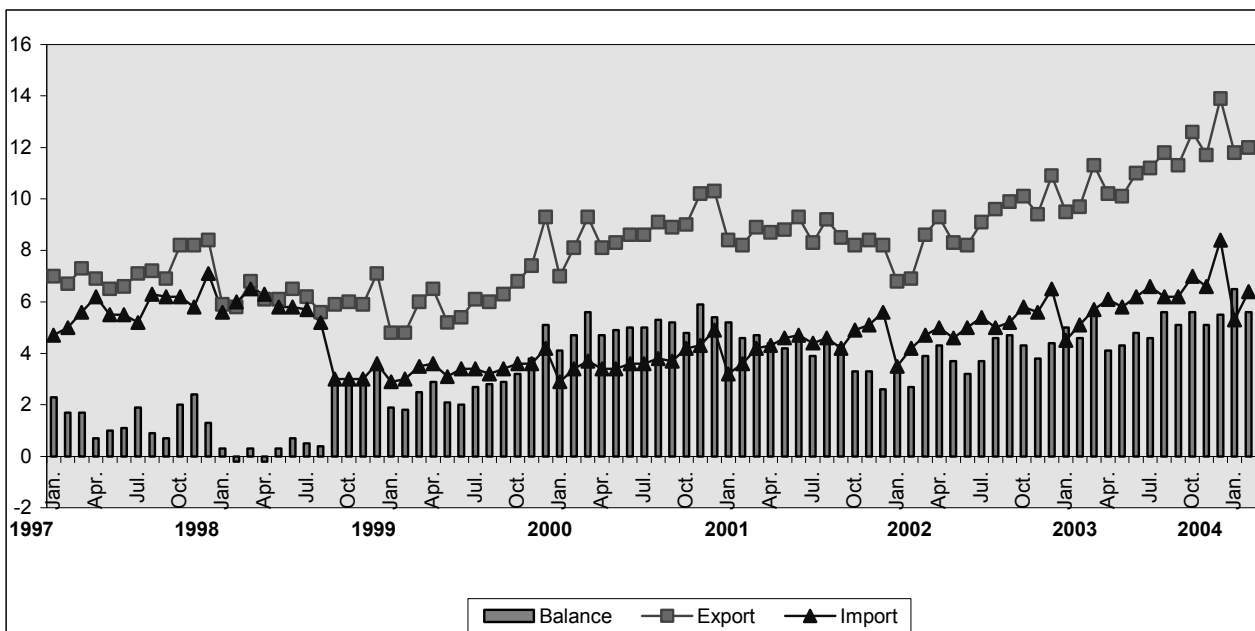
In March of 2004, the Russia's foreign trade turnover reached US \$ 21.1 billion, what is by 20.3 per cent above the figures registered in March of 2003. This March, Russian exports made US \$ 13.6 billion (a 16.9 per cent growth), while imports were registered at US \$ 7.6 billion (a 26.7 per cent growth). In March of 2004, the Russia's active balance of trade made US \$ 7.7 billion, what was at about the level observed in March of 2003 (US \$ 7 billion).

In the 1st quarter of 2004, Russian exports made US \$ 35.8 billion, what was by 15.2 per cent above the figures registered in the 1st quarter of 2003 (the record high as concerns the first quarters figures registered the period from 1994 till 2004). The highest results were observed not only with respect to fuel and energy, but also other commodity groups. The latter circumstance was related to the growth in export prices (according to the Bank of Russia, the respective index was at 1.079) and the expanding volume of exports (the volume index was registered at 1.071).

The amounts of import of commodities in the 1st quarter of 2004 also grew and made US \$ 18.8 billion (a 18.6 per cent growth), what also was above all previously registered volumes of import in the 1st quarters. The increase in imports was facilitated the Ruble appreciation in real effective terms.

Figure 1.

Main indicators of Russia's foreign trade (in US \$ bln.).



Source: RF Goskomstat, RF CB

The high rates of growth in the Russian exports are still to a considerable degree determined by the favorable business situation on the world market.

In the 1st quarter of 2004, the world oil prices were at a high level. After an insignificant decrease in February and March, there was observed a considerable rise in prices. Thus, the quotations of the "Light" oil prices at the New York exchange made US \$ 38 per barrel by the end of the month. The average Urals price made US \$ 30.9 per barrel (a 9.4 per cent increase as compared with the figures registered in March of 2003), while the average Brent price was at US \$ 33.6 per barrel (a 9 per cent growth). As compared with the figures registered in the 1st quarter of 2003, average monthly oil prices practically did not change.

The major factors behind the persisting high oil prices were the growing demand for oil in relation to economic growth in the USA and China (in the 1st quarter of this year, the demand for oil in China increased by 18 per cent in comparison with the figures registered in the respective period of the preceding year, while Chinese imports increased by 9 per cent), the threat of terrorist attacks, and the policy of the OPEC aimed at the real reduction in extraction of oil.

The persistence of high oil prices was predetermined by the recent turmoil in Iraq, which prevent a stable increase in extraction of oil and its export from this country. Besides, the global demand for oil in 2004 may increase by 1.7 per cent to 2.2 per cent and make 80.3 to 80.7 million barrels a day. According to the recent forecasts of the International Energy Agency, the average annual oil price (“Light”) can make US \$ 33 per barrel in 2004.

The average Russian oil prices made US \$ 30.53 per barrel (US \$ 222.88 per metric ton) according to the results of the monitoring conducted in March and April, as compared with US \$ 28.32 per barrel registered in January and February. Proceeding from the formula set forth by the law, on June 1 the rates of export duties on oil should make US \$ 41.6 per metric ton (currently US \$ 35.2 per metric ton). This rate of export duty is the record high in the period from February of 2002, when the export duties pegged to the prices observed on the world markets were first introduced.

In March, the contract prices of Russian natural gas declined by 2.6 per cent in comparison with the figures observed in February of 2004. in the 1st quarter of 2004, the average monthly price of natural gas increased by 10.6 per cent in comparison with the figures observed in the respective period of 2003.

In 2004, the significant growth in demand for ferrous metals in Europe, USA, and a number of Asian countries resulted in a considerable increase of the respective world prices. In March of 2004, the European export prices of major types of merchant rolled shapes and flat rolled products grew by about 18 per cent in comparison with the figures registered in February.

The exceptionally good price situation persists on the market of non-ferrous metals, what may be explained by economic growth observed in Asian countries and USA. In the 1st quarter of 2004, the average monthly nickel, copper, and aluminum prices increased in comparison with the figures observed in the respective period of 2003 1.7 times, 1.6 times, and by 18.2 per cent respectively. The average nickel price in March of 2004 made US \$ 13730 per metric ton (a 9.8 per cent decline in comparison with the February figures), the aluminum price made US \$ 1660 per metric ton (a 1.4 per cent decline), and copper price made US \$ 3018 per metric ton (a 8.5 per cent growth).

Table 1

The average monthly world prices in March of the respective year

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|---------------------------------|--------|--------|--------|--------|---------|--------|---------|--------|---------|
| Oil (Brent), USD / metric ton | 19,1 | 19,2 | 13,0 | 13,7 | 26,9 | 25,5 | 24,1 | 29,1 | 33,6 |
| Natural gas, USD / thous. c. m. | | 1,870 | 2,170 | 2,120 | 2,828 | 5,200 | 2,996 | 5,757 | 5,267 |
| Gasoline, USD / metric ton | 0,603 | 0,645 | 0,467 | 0,527 | 0,934 | 0,890 | 0,783 | 1,005 | 1,12 |
| Copper, USD / metric ton | 2584,7 | 2424,8 | 1772 | 1477,1 | 1779,1 | 1780,3 | 1605 | 1681,6 | 3018,0 |
| Aluminum, USD / metric ton | 1600,8 | 1635,5 | 1441,3 | 1251,1 | 1584,2 | 1511,2 | 1403,17 | 1393,1 | 1660,0 |
| Nickel, USD / metric ton | 7955,7 | 7929,5 | 5380 | 4934,5 | 10269,6 | 6140,3 | 6503,33 | 8402,4 | 13730,0 |

Source: calculated in accordance to the data presented by London Metal Exchange (UK), International Oil Exchange (London)

In the 1st quarter of 2004, the amount of export transactions vis-à-vis the countries outside CIS made Rub. 31.4 billion, what was by 18.4 per cent above the figures registered in the respective period of the preceding year; in March the amount of exports made US \$ 11.24 billion (13.7 per cent). On the whole, imports from these countries demonstrated intensive dynamics – in the 1st quarter of 2004 the respective imports made US \$ 15.3 billion, what was by 18.6 per cent above the figures registered in the 1st quarter of 2003. this March, the import of goods accounted for US \$ 6.0 billion (a 24.4 per cent increase in comparison with the figures observed in March of 2003).

In March, the amount of Russian trade vis-à-vis CIS member countries made US \$ 3.85 billion, the exports and imports grew by 35 per cent in comparison with the figures registered in March of 2003; the amounts of import and export made US \$ 2.31 billion and US \$ 1.54 billion respectively.

In May of 2004, the government of Belorussia forwarded to the governments of Russia, Ukraine, and Kazakhstan a package of documents, proposing to create a single fuel and energy complex in the framework of the single economic space (SES) and work out a joint perspective fuel and energy balance of four states up to year 2015. Belorussia is not content with the situation, where it has to sign a new agreement with Gazprom each year. The Gazprom management extremely negatively apprised the Belorussian proposal. As a matter of fact, Belorussia categorically refuses to create a joint venture between the Belorussian state gas company "Beltransgaz" and the Russian Gazprom. The joint venture should manage the Belorussian natural gas transportation system, and Russian natural monopoly hoped to obtain control over its export channel, thus reducing the risks of its European consumers and compensate its losses caused by payment arrears of Belorussia. As a result, Beltransgaz and Gazprom have not signed contracts for supply of Russian natural gas to Belorussia and transit of Russian natural gas to Europe until the end of 2004 as yet. This situation even made Gazprom to stop the transportation of natural gas via Belorussia in February of this year.

In the end of May, there was held a meeting of heads of states participating in the single economic space (SES) – Russia, Belorussia, Kazakhstan, and Ukraine. They put forward the major objective – the creation of the single customs space and a free trade zone. In order to implement SES in practice, it was decided to work out more than 60 joint legislative acts.

However, even at this first stage of approval of the package of documents the parties had serious disputes. Thus, the creation of a free trade zone with the Ukrainian participation means that certain changes should be made in the procedures governing VAT collection. As concerns the trade relations between Russian and its CIS partners, this tax is practically everywhere collected basing on the country of destination principle. Ukraine is a rare exception: the export of energy resources to Ukraine generates almost US \$ 700 million in tax revenues due to the Russian budget; Ukraine protests against this situation. Besides, Russia and Belorussia could not resolve their dispute concerning natural gas exports.

The negotiations on the Russia's accession to WTO continue. In May, Russian and EU signed the protocol of completion of negotiations concerning market access in the framework of Russia's accession to the World Trade Organization. The protocol contains the agreements between the parties relating to the reduction of import tariffs, conditions of access to the Russian market of banking, insurance, and telecommunication services.

The average maximal level of tariffs was set at 7.6 per cent as concerns manufactured goods, 11 per cent – for fish products, and 13 per cent – for agricultural produce in addition to the tariff quotas on meat and poultry amounting to Euro 600 million a year (15 per cent of the total EU agricultural exports to Russia).

As concerns import duties on cars, the reduction of these prices should be started after the transitional period and they will be reduced only by 2012. The EU recalled its requirement to set a zero rate customs duties on aircraft and respective completing parts. In its turn, Russia agreed to meet the requirements of European aircraft manufacturers and reduce the customs duty on aircraft in 7 years.

The highest rates of customs tariffs will remain as concerns textiles, cloths, footwear, furniture, and toys, the lowest tariffs were set on imported technological equipment necessary for Russian industry.

As concerns the sphere of services, Russia should assume a broad range of obligations including telecommunications, transport, financial services, mail and courier services, trade, ecology, news agencies, and tourism. The obligations include the cross-border rendering of services and commercial institutions.

Besides, the agreement could settle a number of energy problems related to trade, in particular, the issue of the domestic prices on natural gas for industrial consumers. Russia assumed the obligation that the domestic price of natural gas for industrial consumers should include self-cost, profit, and investments necessary for prospecting of new deposits. Russian prices of natural gas for industrial consumers will be gradually increased up to US \$ 27 - US \$ 28 by 2004, US \$ 37 to US \$ 42 by 2006, and to US \$ 49 – US \$ 57 by 2010, what is in line with the Russia's energy strategy.

There was also reached an agreement concerning the revision of the system of fees currently applied to EU air companies flying via Siberia. It was decided that not later than in 2013 this system should base on actual costs, be transparent and non-discriminatory.

There were also achieved other compromises.

However, the negotiations with other WTO members have not been completed as yet. USA and Canada strongly react to the issues of low Russian domestic natural gas prices and the problem of protection of intellectual property. China insists on liberalization of Russian legislation regulating access of foreign labor force to the Russian labor market and requires a reduction in customs tariffs on imported textiles, footwear, and furniture. Negotiations with Australia progress slowly, as that country is viewed as a prospective trade part-

ner, however, it requires a reduction of customs duties on goods it does not produce at the moment, but is going to organize respective production and import these goods in Russia.

By this time, Russia has signed WTO accession protocols with Kyrgyzia, New Zealand, Hungary, Czech Republic, Bulgaria, and Israel. This month it is planned to complete the tariff negotiations with Japan and South Korea.

N. Volovik, N. Leonova

Organizational changes in the sphere of science

The new Ministry of Education intends to create research universities and launch a pilot project in Novosibirsk. The concept of “leading higher education establishments” elaborated over two last years is not abandoned yet. However, simultaneously there was proposed a number of measures aimed at the integration of science and education. The new Ministry is planning to continue to support innovative activities. Since the beginning of the year, the situation relating to the state of the budget of the Russian Fund of Technological Development engaged in financing of intersectoral applied and innovative projects has aggravated.

The most noticeable event, which took place in the science and technology sphere in the first six months of 2004 was the creation of the new Ministry of Education and Science, which replaced the former Ministry of Education and the section of the Ministry of Industry, Science, and Technologies managing the issues of scientific and technological development. The integration of science and education may be viewed as a step forward in comparison with the former administrative structure, which confirms the intent of the state to more consistently pursue the policy aimed at the integration of these two spheres. This conclusion is confirmed by the fact that the new Ministry will be formed not on the sectoral principle (science and education), but on the problem principle assuming that science and education are inseparably related. It was also decided not single scientific sphere of higher education establishments out of other scientific sectors. Prior to this organization, the sphere of scientific projects carried out by higher education institutions was supervised by the former Ministry of Education, while the Ministry of Industry and Science was responsible for the development of departmental organizations, state scientific centers (SCC), and was oriented towards applied research and innovation activities.

Although different governmental documents stated the necessity to integrate science and education for almost 10 years, and in 1996 there was launched the Presidential program “Integration,¹³” a number of regulatory and legal barriers continues to prevent the real integration. The academic personnel of higher education establishments is formally separated from research and development personnel, while cooperation between higher education institutions and scientific organizations is carried out on the basis of special agreements primarily in the form of part time work. Financing is still based on the departmental principle, and there are no exceptions in the case of cooperation.

The new Ministry has already put forward a number of initiatives indicating a search for new ways of integration of the scientific and educational spheres. These measures include, first, the intent to abandon the procedure of accreditation of scientific organizations (the respective amendments should be made to the federal law “On science and the state science and technology policies”), as well as removal of restrictions on educational activities of specialists engaged in scientific researches. Second, the Ministry develops the idea of creation of integrated structures, or “research universities” (the respective amendments should be made to the federal law “On higher and postgraduate education”). At last, third, the Ministry works out the package of documents concerning the introduction of the status of “leading universities.”

The abolishment of state accreditation means the abolishment of the concept of “scientific organization” and, therefore, the adjustment of departmental regulations pertaining to science to the concepts set forth in the Civil Code. Besides, after the abolishment of accreditation higher education establishments will have equal rights with scientific institutions and will be able to participate in any tenders (at present they formally have no such a right). Informally, the higher education establishments having developed scientific bases could receive the necessary licenses and take orders: for instance, over the last 18 months the Ministry of Industry and Science issued accreditation certificates to about 20 – 25 higher education institutions. However, after the accreditation is abolished, higher education establishments will be able to participate in research projects not on the basis of exception, but on lawful grounds. Besides, the abolishment of accreditation creates incentives for the development of innovation activities, since according to the legislation cur-

¹³ At present this program is known as “Integration of science and higher education in Russia in 2002 through 2006”.

rently in force organizations having the status of “scientific” institutions should spend not less than 70 per cent of their aggregate expenditures for R & D purposes, therefore the enhancement of innovative activities is tightly constrained.

As concerns research universities and leading higher education institutions, the interpretation of these terms is still somewhat ambiguous, therefore rectors are reluctant with respect to such organizations.

The concept of “leading universities” has been discussed for more than 2 years. According to the latest plans, this status should be granted to 15 or 20 federal higher education institutions. Besides, 80 to 85 higher education establishments should be granted the status of “specialized leading higher education institution,” this category should include higher education establishments pursuing certain specific avenues of research¹⁴. According to the package of documents developed by the Ministry, the status of “leading university” should be granted on the contest basis for a 5 year period and bring additional financing from the state budget, as well as provide certain freedom as concerns the development of standards and methods of education, etc. Therefore, the introduction of the concept of “leading higher education establishment” is necessary to provide financial support to elite higher education institutions. However, it potentially deteriorates financing of other higher education establishments.

At the same time, it should be noted that higher education institutions in fact significantly differ in terms of their potentials. According to the RF Ministry of Education, only 38 per cent of accredited higher education establishments have funds for R & D activities, and only 20 per cent of the academic personnel are engaged in research.

The leading universities should differ from other higher education establishments by engagement in “effective” fundamental and applied research, carry out innovative activities, are integrated in the world educational, cultural, and informational environment. They also should differ in terms of the quality of their academic personnel, the level and scale of education of highly qualified specialists, scientific personnel, and educators. All the characteristics listed above were assessed basing on more than 50 formalized criteria, basing on the results of this assessment there were chosen the leading higher education establishments.

This system provoked significant discontent in the higher education community. Apparently, the apprehension was primarily caused by the fact that the introduction of “leading universities” would financially affect many higher education establishments, especially new and regional ones. A number of apprehensions is justified. First, the issue of the status: in the case there are “leading” institutions, other may be considered “obsolete” and loose part of their entrants. These developments may also result in social and inter-university conflicts. Second, it is doubtful if the criteria were objective enough. The category of the leading higher education establishment is not clearly defined. At many higher education institutions are weak and strong schools and chairs, therefore, many higher education establishments may apply for the status of “specialized leading higher education institution.” Third, a number of criteria used for the assessment deteriorates the chances of new higher education establishments and the universities situated in previously closed towns (for instance, it concerns the criterion relating to the share of foreign students). Fourth, according to the data presented by the former RF Ministry of Education, it was planned to use for the additional support of leading universities not the financial resources allocated for other higher education institutions, but the additional funds assigned for financing of the education from the excess budget revenues. It is clear that it is only hopes and not approved plans, therefore in the case leading universities are introduced it may result in the redistribution of budget funds. At the same time, many regional universities are not just educational establishments, but centers of social and cultural influence, therefore the lack of financing of such institutions may result in deterioration of the social situation in the respective city (region).

The concept of “leading higher education establishment” is the unique Russian phenomenon. International practices include the close, but not identical concept of “research university”. For instance, in the USA there is used the so called “Carnegie classification” according to which all universities and colleges are classified in 6 categories, the highest of which is “research university”. Research universities are characterized by a broad range of educational courses, have their postgraduate departments, award not less than 50 Ph. D. a year and receive state financing for research at or above a certain level (not less than US \$ 15.5 billion a year)¹⁵. At the same time, the status of research university is granted basing on the universities activities, and not by

¹⁴ Dezhina I. Sostoyaniye sfery issledovaniy i razrabotok // Rossiyskaya ekonomika v 2003 godu. Tendentsii i perspektivy. Issue 25: - M.: IET, 2004, p. 276.

¹⁵ Science and Engineering Indicators – 2002. Vol. 1. NSB. Arlington, VA: NSF, 2002, p.2-10.

a directive, it also does not include any preferences. The terms “research university” and “elite university” are synonyms. The concept of “elite university” was based on the notion of a close integration of education and research, including the use of research in education of students. The specifics of elite / research universities in the USA practically do not differ from the criteria of research universities in other countries of the world, and include the following:

- A broad range of specializations, including hard science, social and humanitarian sciences;
- Intensive orientation towards scientific R & D activities, primarily, fundamental research;
- Orientation towards modern scientific avenues and innovative activities;
- Availability of a system allowing to receive Ph. D. degree, often the number of postgraduates working on their master and doctor theses exceeds the number of students;
- High professional level of educators;
- Invitation of leading experts from other countries on temporary basis;
- Receptivity of the world practices and flexibility with respect to new avenues of research and education methods;
- Enrollment of students on the contest basis;
- Formation of a specific intellectual environment and specific science, technological, and economic space often filled by objects of innovative infrastructure;
- Corporate ethics based on democratic values and academic liberties.

The new Ministry of Education and Science also started to promote the concept of “research universities”. In this case the concept primarily includes the creation of new integrated structures basing on cooperation between universities and scientific institutes, as well as state scientific centers. It is envisaged that this integration should be carried out on the voluntary basis and the new structures can be formed both on the basis of universities, and research institutions and state scientific centers. In legal terms, the concept of “research university” is absent in Russia, therefore the creation of integrated structures in the form of research universities will require a considerable revision of the legislation currently in force. At the moment it is planned that the first integrated structures will be formed already this year, for instance, there is launched a pilot project on the base of the Novosibirsk state university. It should become the center of integration of a number of leading educational and research institutions¹⁶.

At the same time, the use of terms “leading” and “research” university resulted in considerable confusion. At present it is unclear if the intent to create research university presupposes the abandonment of the so much criticized concept of leading higher education establishments, and if the latter concept continues to exist, to what extent these two concepts are overlapping? For instance, will a research university at the same time (automatically) granted the status of the leading higher education institution? At present there are no clear criteria and even concept of research university, therefore it is difficult to answer these questions.

At the same time, in the scientific and educational community the notion of research university is similar to its foreign concept. For instance, representatives of rectors believe that the specific features of a research university should include orientation towards education of postgraduate students, expanded set of subjects, work with senior school pupils and selection of future entrants, inseparable integration of science and education, availability of modern equipment, developed links to the industry, and participation in commercialization of technologies, cooperation with other organizations, primarily the Russian Academy of Science, developed infrastructure (campus), and the infrastructure of work with alumni and donors¹⁷. However, at the moment both representatives of the Russian Academy of Science and higher education establishment are more oriented to closer cooperation than creation of integrated structures.

It would be feasible to review the research and education centers created in a number of Russian higher education institutions (16 centers in the field of hard sciences and 9 in the field of humanities) with the support of the Carnegie corporation and the McArthur foundation as a model for development of research universities. The experience accumulated by these centers includes different approaches to the development of research and education process, support of students, postgraduates, and young scientists, cooperation with

¹⁶ A. Fursenko: Gosudarstvo dolzhno sozdat sistemu finansirovaniya projektov // *Novye tekhnologii*, No. 17, April 28, 2004.

¹⁷ Compiled basing on the materials of the Russian – US conference “Research Universities” organized by the RF Ministry of Education, Russian Academy of Science, and the American Foundation for Civilian Research and Development. – M., April 4 – 6, 2004.

Russian and foreign organizations may be extended to the universities where such centers were established. It also seems that in case cooperative structures develop, joint scientific programs, joint scientific councils, parity financing, joint participation in international projects should become their important elements.

Although the creation of the Ministry of Education and Science somewhat shifted the focus from the scientific-industrial, innovative activities to scientific-educational types of activities, it is important to note that the issues of innovative development were also included in the sphere of responsibility of the new Ministry¹⁸. Therefore, there is hope that support of innovative and financial infrastructure, small innovative businesses will continue. Many problems are still encountered in this sphere, and in the first six months of this year one of them, concerning the conditions of activities of the extra-budgetary funds aimed at the support of R & D and the Russian Fund of Technological Development, has aggravated.

Extra-budgetary departmental funds were formed by ministries, departments, concerns, corporations, and associations at the expense of contributions made by enterprises (1.5 per cent of the self-cost of their products). In its turn, the Russian Fund of Technological Development was formed at the expense of these departmental funds (25 per cent). After article 25 of the second part of the RF Tax Code entered into force (as amended), extra-budgetary R & D funds should be formed at the expense of voluntary contributions of gross profits (0.5 per cent). The changes in the procedures governing contribution of financial resources in the R & D extra-budgetary funds resulted in fact in a twofold decline in contributions to the RFTD. As a result, in 2004 the RFTD had reserves sufficient only for financing of running projects, and insufficient to make new contracts.

At the same time, the composition and the number of extra-budgetary funds also changed, since there were introduced new criteria of granting organizations the status of extra-budgetary funds. While earlier extra-budgetary funds could be created only at federal executive authorities or commercial enterprises and associations of enterprises, in 2004, according to the new requirements, extra-budgetary funds may be only non-commercial organizations. These changes froze the activities of the RFTD, what may negatively affect the innovative activities and applied interdisciplinary research at the time, when interdisciplinary research is the key avenue of development of science in the world.

I. Dezhina

Municipal reform: the experience of the Leningrad oblast

In Russian regions, there began the work on implementation of the municipal reform in accordance with the law "On general principles of organization of local governments in the Russian Federation."

The first stage of this work is related to the reform of the territorial foundations of local government. According to the requirements set forth by the law, the RF subjects should establish the boundaries of municipal entities and grant them the status of urban or rural settlement, urban okrug, or municipal district before January 1 of 2005.

At present this work is at different stages in different regions of Russia. The reform of the territorial foundations is braked by the ambiguous situation concerning the assignment of sources of financing to local budgets (the respective amendments to the Tax and Budget Code passed only the first reading), and the contradictions and flaws in a number of provisions of the law. In particular, such criteria of formation of municipalities at the settlement level as accessibility of the center of the settlement by walk and population not less than 1000 residents in many cases contradict one another. The law, which requires to divide territories of all densely populated districts among settlements does not take into account the non uniform nature density of population within each region. The practice demonstrate that territories with sparse populations, where walking accessibility is difficult exist in the majority of administrative districts, even in the case the average density of population in these districts is above the national average.

At the same time, in certain regions the reform of their territorial structure progresses at a fast rate. For instance, in the Leningrad oblast the regional law "On boundaries and status of municipal entities Vsevolzhsky district and Vyborg district and municipal entities in their composition" was approved on March 9, 2004. According to this law, the municipal entities Vsevolzhsky district and Vyborg district were granted the status of municipal districts. Within the Vsevolzhsky district there were formed 20 municipalities at the settlement level (8 urban and 12 rural ones). In the Vyborg district there were created 14 settlements (8 urban and 6

¹⁸ Issues concerning the Ministry of Education and Science of the Russian Federation. Resolution of the RF Government No. 158 of April 6, 2004.

rural ones). The law contains the cartographic description of the boundaries of all municipal entities listed above.

It seems that the Leningrad oblast is the first subject of the Russian Federation, which could approve the official legislation concerning the issues of the territorial structure in the framework of the municipal reform. Therefore, the local practices should attract attention.

The initial conditions for the introduction of the two tier model of local government in the Leningrad oblast may be evaluated as relatively favorable. The oblast is characterized by high population density, developing economic potential, high level of education. Although the district based organization of local government is the prevailing territorial model, according to the regional legislation settlements were granted the possibility to form independent municipal entities. This right was primarily used by urban settlements with high levels of budget provision. The only rural settlement having municipal status is the Koltushskaya volost.

In the framework of the district model there were kept (although not in all districts) certain elements of decentralization with respect to the units at the settlement level. Since the settlement budgets in the oblast were liquidated only in 1996, in certain districts there persisted traditions to modify estimates with certain elements of interbudgetary relations. For instance, in the Gatchinsky district the accounting for tax revenues is still carried out at the volost level.

In 2001, in the district there was organized an experiment in fact envisaging the granting of a quasi-municipal status to the volosts¹⁹. The district administration transferred to its territorial units certain powers concerning the settlement of issues of local importance and assigned to them sources of financing on voluntary basis. At the same time, the base of revenue assignment were minimal guaranteed expenditures across key items calculated in accordance with the single formula for all territorial units. In practice, the experiment was conducted only in one volost (Pudostskaya volost) for several months. Practically all municipal functions with the exception of HPU were transferred to the volost level. The list of revenue sources included the income tax, single tax on imputed income, the tax on property of individuals, land tax, leasing fees, cleaning of territory fees, fees for the needs of educational establishments, and a part of the tax on property of enterprises.

In spite of the fact that the experiment was carried out only for a short time, its results could be evaluated as positive. The tax revenues in the territory grew significantly, while their utilization became more efficient. At the same time, the experiment revealed potential problems related to the formation of budgets at the settlement level. For instance, the Pudostskaya volost considerably depends on the revenues generated by one enterprise – the local poultry plant. In the period when the experiment was conducted the standing of the poultry farm was rather good, however, by this time it went bankrupt. Therefore, the volost administration has serious apprehensions concerning its financial independency.

Yet another positive factor facilitating the municipal reform in the Leningrad oblast is a rather high availability of management resources at the level of settlement and volosts. The number of employees at settlement and volost administrations is comparable to the personnel of municipal officers in the settlements located in the regions with the two tier structure. The share of expenditures for administration in the consolidated municipal budget is also at the level characteristic of regions with the two tier structure and is by almost one fourth above the national average. It means that the problem of growth in administrative expenditures in the course of implementation of the municipal reform in the oblast should not be urgent. At the same time, in a number of districts there were elaborated mechanisms allowing to achieve economy of scale in the sphere of administration: there were created joint administrations performing their functions in several volosts. For instance, there are two such administrations in the Gatchinsky district and 5 in the Vyborg district.

At the same time, certain specifics of local government in the Leningrad oblast created problems in the implementation of the municipal reform. For instance, the existence of several urban settlements (including rather small ones, such as towns of Svetlogorsk and Kommunar) as independent municipal entities was doubtful in the situation of the reform of the territorial structure. The uneven economic development of the territory made the political component a more important factor as concerns the issue of municipal boundaries.

¹⁹ Bobrov I. V., Lyubushkina Ye. V. Daite nam istochnik dokhodov... i Gatchina ne ustupit Versalyu // Munitsipalnaya vlast, 2002, No. 1.

In this situation, the administration of the Leningrad oblast demonstrated the following approaches to the problems of territorial organization of local governments.

First, the adopted decisions did not envisage any changes in the boundaries of the existing municipalities at the district level. According to a representative of the oblast administration, it is also going to follow this approach in the future. As concerns the boundaries of the existing territorial units (volosts, settlement, etc.), the approaches should be different. For instance, in the Vsevolzhsky district municipalities at the settlement level were created within the boundaries of existing volosts, while in the Vyborg district territories were enlarged: the number of settlement municipalities is by 8 less than the number of volosts. At the same time, in both cases the sizes of settlements are rather large: the average population of one settlement in the Vsevolzhsky district is 8 thousand, while in the Vyborg district – 13 thousand. Only in few settlements of the Vyborg district the size of the population is below 10 thousand, in the majority of settlements population makes from 10 to 20 thousand residents (80 thousand in the town of Vyborg).

Second, the new territorial structure was primarily formed “from the top.” Basing on the information provided by districts, the oblast administration worked out its own variant of the territorial structure and agreed it with district administrations. The representatives of settlements and public did not participate in this process. It may be assumed that this approach prevented optimization of the territorial structure, since the specifics of individual settlements were not taken into account. For instance, representatives of certain volost administrations proposed variants of enlargement of territories different from those envisaged in the law, however, they had no institutional possibilities to voice and support their opinions. Therefore, alternative variants were taken into account only in the case they were presented personally to the oblast leadership.

Third, in the two districts included in the law there were formed no urban okrugs. All previously independent municipal entities (towns of Svetlogorsk and Sertolovo, as well as the Koltushskaya volost) were included in the composition of districts as urban and rural settlements. At the same time, no effort was made to obtain their agreement. Moreover, according to representatives of the oblast administration, similar policies will be pursued with respect to larger towns – Gatchina, Volkhov, etc. This position seems rather doubtful, especially in the light of the legislation currently in force. Article 84 (3) of the law “On general principles of organization of local governments in the Russian Federation” envisages that urban settlements, which had the status of municipal entities on the day this article entered into force should be urban okrugs in the case the law of the RF subject (as established by the provisions of section 2 of article 11 and section 7 of article 13 of this federal law) did not set forth other arrangements as on February 1, 2005. At the same time, section 7 of article 13 envisages that the population should express its agreement with such changes. However, this approach was approved by the Leningrad oblast Procurator’s office, which did not find any infringement on the legislation in this case.

The similar approach to the towns also rises certain questions. In the modern world, exactly towns are the centers of economic growth and one of the objectives of the municipal reform should be the creation of conditions facilitating increase in towns’ competitive capacities. It seems doubtful if the inclusion of towns in the composition of districts answers this objective. These actions may negatively affect the investment climate in urban centers, since investors have to deal with an additional bureaucratic tier at the level of districts. Besides, this model may constrain introduction of innovative approaches to municipal administration which often (although not always) concentrates in towns. The real problem faced by the towns of the Leningrad oblast and deteriorating their investment attractiveness is the lack of free territories necessary for investment. However, it is still doubtful that this problem may be settled by inclusion of towns in the composition of districts.

As concerns the assessment of the financial consequences of the reform of the territorial structure of local government, this work is underway, however, already after the decision on formation of municipalities at the settlement level had been taken. In the process of decision making, financial consequences of different variants of territorial organization are not taken into account. At present, the financial assessment of the consequences of reforms is available only for the Vsevolzhsky and Vyborg districts.

The methodology of assessment of financial consequences of the reform is of considerable interest. The specifics of this methodology is that financial calculations are not strictly linked to the local budget standards set forth by draft Tax and Budget Codes, since these standards may be changed in the process of discussion of these drafts in the State Duma. Alongside with the assessment of consequences of assignment of these standards there is carried out the calculation of the so called revenue potential for each municipal entity. The revenue potential includes all tax revenues collected within a given territory with the exception of amounts due to the federal budget, i.e. the total amount of tax revenues, which may be divided between the oblast and

local budgets. This indicator demonstrates the maximal possible level of tax assignment, which may be achieved at the regional level.

Alongside with the calculation of the revenue potential, there was also carried out the evaluation of the average oblast per capita expenditures across municipalities of different types: settlement, municipal district, an urban okrug. The comparison of the consequences of assignment of sources of financing in accordance with the amendments made to the Tax and Budget Codes, the estimated potential per capita revenues, and the average oblast budget security level at the settlement level was carried out as concerns settlements in the Vyborg district (see Figure 1). The data for year 2003 were used for the calculations.

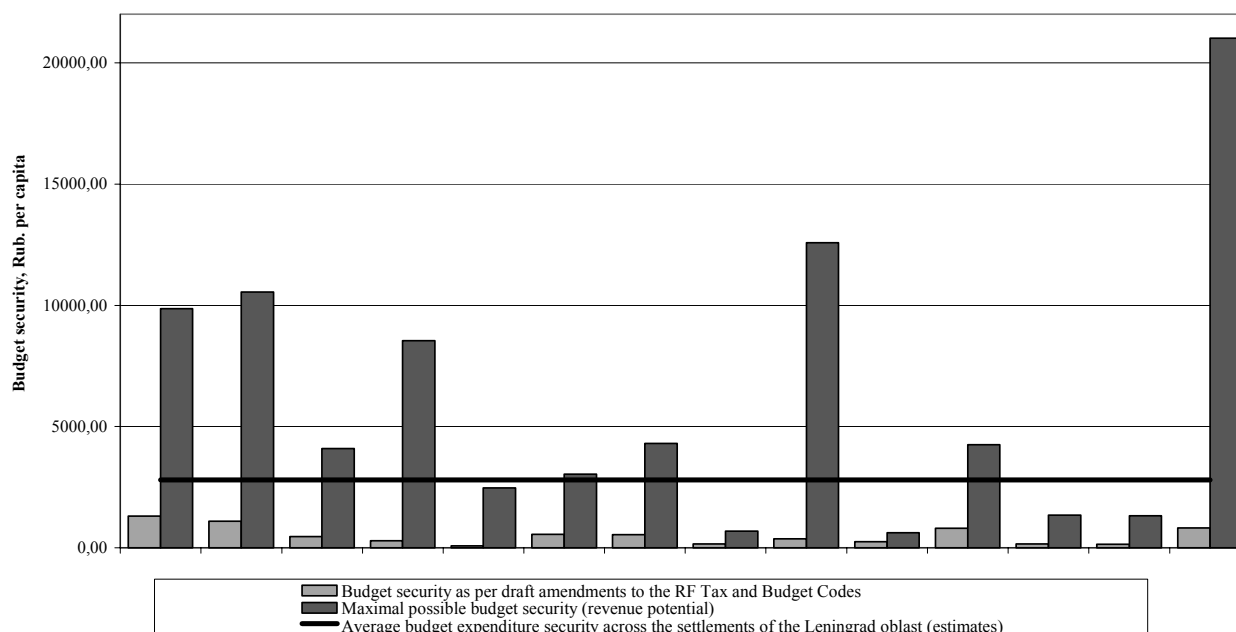
In the case the average oblast budget security level is assumed to be the level, to which the budget security of settlements should be equalized, a thorough analysis may be of considerable interest for the further formation of the system of interbudgetary relations. The analysis embracing all municipal entities in the oblast permits to answer a number of principal questions, i.e.:

- 1) What municipal entities will need subsidies at any level of assignment of sources of financing to local budgets (apparently, in the Vyborg district there will be 4 to 5 such settlements out of 14);
- 2) If there is the possibility to assign sources of financing of local budgets at the regional level in addition to those envisaged by the federal legislation (if we proceed from the data on the Vyborg district, this possibility is apparently available, however, in this case it is necessary to analyze the totality of settlement municipalities in the oblast).

At the same time, such an analysis (which is preliminary and not detailed) can not answer the question what concrete additional taxes should be assigned to municipal entities.

Figure 1.

Possible spread of budget revenue security levels of settlement municipal entities in the Vyborg district of the Leningrad oblast depending on the assignment of the sources of financing.



In the framework of the generally interesting approach used in the Leningrad oblast for assessment of financial consequences of the reform of the territorial structure of local government, there are certain controversies. For instance, it is difficult to understand why expenditures are compared only to tax revenues, and not all own revenues of municipal entities. The methods employed to find out the average oblast per capita expenditures of municipal entities of different types give rise to doubts, since in the result the expenditures of urban okrugs (Rub. 3971.3 per capita) are significantly below the amount of expenditures of settlements and districts (Rub. 2802.5 and Rub. 2137.3 per capita respectively). Moreover, the revenue potential is calculated basing on the indicator of marginal withdrawals – an analogue of a negative transfer, where the actual budget security of municipal entities is compared with the average oblast expenditure security, the economic nature of which is difficult to understand.

However, certain (mainly technical) flaws do not outweigh the significant advantages of the methodology, which ensures, first, an objective measurement of the revenue potential independent of the concrete standards (which have not been set forth as yet), and, second, orientation towards single average criteria and not specific expenditures of each municipality.

I. Starodubrovskaya, M. Slavgorodskaya, I. Bobrov

Issues discussed at the meetings held by the Government of the Russian Federation on May 13, 20, and 27 of 2004

The most interesting documents reviewed in the course of the meetings held by the RF Government in May were the draft law “On measures aimed at the establishment of accrual mortgage system ensuring provision of housing for servicemen and their family members” (the meeting held on May 20), the report of the RF Minister of Economic Development and Trade German Gref “On the forecast of the level of prices (tariffs) on the products (services) of natural monopolies in 2005” (the meeting held on May 27), and the draft federal law “On the placement of orders for procurement of goods, works, and services for state and municipal needs” presented at the meeting held on May 13. This draft law is aimed at the systematization of the RF legislation concerning the state and municipal procurement and its harmonization with the international legislation and international practices. Many recommendations worked out by the IET in the sphere of streamlining of the institute of state and municipal procurement, in particular those presented in the paper “Improvement of the system of procurement of goods, works, and services for state needs” (IET Working Papers Series, issue No. 66) were reflected in the final version of the draft law presented by the Ministry of Economic Development and Trade (MEDT).

The meeting of the RF Government held on May 13 of 2004.

At the meeting of the RF Government held on May 13, 2004, A. V. Sharonov, the acting RF Minister of Economic Development and Trade presented the draft federal law “On the placement of orders for procurement of goods, works, and services for state and municipal needs.”

The considerable merit of the draft law is the fact that it embraces procurement of all products carried out in the RF territory at the expense of respective budgets and extra-budgetary sources of financing at the federal, regional, and municipal levels. We believe that this will allow to exclude gross infringements on the competitive principles of procurement at the level of RF subjects. Besides, the draft law introduces a number of positive innovations, for instance:

- closed tenders may be held only in the case the object of state or municipal contracts is procurement of goods, works, and services for state or municipal needs constitutes state secret, what expands the sphere for open tenders;
- the draft law establishes publicly accepted criteria of assessment of tender bids and determination of tender winners;
- it envisages the possibility to appeal against the actions (failures to act) on the part of the customer in the course of application of procedures governing the placement of orders for procurement of goods for the state and municipal needs to the authorized federal executive authority vested with the responsibility to control the procedures governing the placement of orders (in the course of placement of orders for procurement for federal needs), or the respective authorized agency of the RF subject (in the course of placement of orders for procurement for the needs of the RF subject), or the respective authorized agency of the local government (in the course of placement of orders for procurement for municipal needs). At the same time, the procedure governing the protection of rights does not exclude the possibility to take legal action. This provision of the draft law should employ more operative methods of protection of tender participants as compared with the court proceedings;
- the draft law envisages the state support for enterprises of the penal system and public associations of invalids in accordance with the international practices;
- it determines the price limits for small scale procurement below which the placement of orders for procurement of goods, works, and services for state and municipal needs may be carried out without organization of tenders (procurement from the single supplier (contractor). This limit corresponds to the cap set forth by the Central Bank of Russia as concerns cash payments made between legal entities in the framework of one transaction (at present this cap is at Rub. 60 thousand);

- the draft law ensures that agent organizations should have the access to participation in tenders for procurement of products for state and municipal needs on the condition they answer certain qualification requirements;

- it introduces a clear division of tender and non-tender methods of procurement (quotation analysis, purchases from the single supplier (contractor));

- the draft law more clearly defines the provisions regulating the placement of orders on the tender basis, among which are the procedures governing the formation of tender commissions, requirements concerning the contents of tender documents, interpretation and changes in the tender documentation, assessment and drawing up of tender offers, the procedures governing the drawing up of tender protocols.

The new draft law defines the terms "state and municipal needs" and the "state and municipal customer." The legislation currently in force fails to clearly define these terms in a number of cases.

Besides, we believe that the draft law justifiably removes the present tight constraints on attraction of foreign suppliers as concerns the procurement of products for state and municipal needs. According to the new draft law, in the course of placement of orders for procurement of goods, works, and services for state and municipal needs the goods (works, services) of foreign origin should be subject to national treatment with the exception of cases where the states or groups of states maintain any prohibitions or restrictions on goods (works, services) of Russian origin.

The draft law changes the minimal term set forth by customers with respect to presentation of tender offers for open tenders: in stead of 45 days this term is set at 30 days. The introduction of this term is related to the fact that in a number of cases longer terms are unpractical (for instance, as concerns tenders for placement of simple goods). From our point of view, this approach is not quite correct, since the term of presentation of tender offers in this case should be differentiated depending on the type of procured products.

It should be noted that in the case this draft law is approved, it will be a qualitative leap in the development of the Russian legislation concerning state procurement, since the provisions introduced by the draft law are based on the best international practices in this sphere.

The meeting of the RF Government held on May 20 of 2004.

At the meeting of the RF Government held on May 20, 2004, there was discussed the draft law "On measures aimed at the establishment of accrual mortgage system ensuring provision of housing for servicemen and their family members."

This draft law is aimed at the legal regulation of relations pertaining to the formation, specifics of investment, and utilization of funds for provision of servicemen and their family members with housing, state support of housing provision for servicemen by the method of accumulation of funds at the expense of the state budget and support of paying capacity of servicemen in the framework of mortgage based crediting.

The draft law determines the categories of persons entitled to participate in the cumulative mortgage system. It should be mentioned that the draft law regulates the most important issue of participation of graduates of vocational education establishments, who made contracts for military service prior to the beginning of the operation of the system, in the cumulative mortgage system.

The draft law envisages that in certain cases servicemen and their family members should be entitled to utilize their housing savings put on the personal cumulative account notwithstanding if they have permanent resident housing. This provision presents the possibility to equalize the social rights of servicemen and, according to the intent of the authors, should enhance the motivation for contract service in the armed forces by provision of the possibility to improve housing conditions of the servicemen already having permanent resident housing at the expense of additional funds provided to them in the framework of the system.

The possibility to purchase own housing by servicemen by the way of the use of the instruments of mortgage based crediting at any time after the expiration of a three year period of participation in the cumulative mortgage system prior to the discharge from the military service, as well as the possibility to choose the place of residence and the size of housing are a new form of realization of the servicemen' right for housing.

The advantages of the cumulative mortgage system in comparison with the present system of provision of servicemen with housing is that the funds allocated for the settlement of the housing problem are distributed on the target basis, and that quality of purchased housing depends on the length of service in stead of the need in housing. At the same time, the process of formation of the funds aimed for purchase of housing is controlled both by federal executive authorities employing servicemen and servicemen themselves.

The replacement of the present system of housing provision with the cumulative mortgage system will allow to abolish the in kind form of provision of housing by monetary payments to servicemen.

The basis for the creation of the cumulative mortgage system is the long term character of the military service (15 to 20 years on the average) and provided by the budget target assignments for accumulation of funds on personal cumulative accounts of servicemen specifically designed for the consequent purchase of housing. Taking into account the fact that the system shall begin to operate since 2005, the 17 year long period of participation in the cumulative mortgage system was set forth as the base period of accumulation of sufficient funds for purchase of housing.

Servicemen are entitled to choose between the mortgage based crediting and the cumulative system basing on the long term forecasts of growth in prices of housing and profitability of the placement of savings.

In the framework of the proposed cumulative mortgage system, the choice of the mortgage based crediting will be justified in the case the rate of interest on the mortgage credit will be below or at the rate of growth in prices of housing. In 2003, the rate of interest on mortgage credits made 15 per cent in Rubles, i.e. inflation plus 3 per cent per annum. In 2005 and later it is expected that this rate will be reduced in accordance with the reduction of inflation rates.

According to the authors of this draft law, the forecasted conditions of the social and economic development and at the estimated real profitability of investment (3 per cent), mortgage based crediting is a sufficiently effective instrument for the settlement of the housing problem in the framework of the recommended cumulative mortgage system both for servicemen and the federal budget.

For the purposes of optimization of the mechanism of utilization of budget funds and meeting of budget obligations, as well as minimization of organizational expenditures, it is proposed that the functions pertaining to realization of the cumulative mortgage system of housing provision for servicemen should be transferred from the federal executive authorities employing servicemen to the federal executive authority ensuring its functioning.

The meeting of the RF Government held on May 27 of 2004

At the meeting of the RF Government held on May 27, 2004, the RF Minister of Economic Development and Trade German Gref presented the report "On the forecast of the level of prices (tariffs) on the products (services) of natural monopolies in 2005."

The main aim of the state regulation of prices (tariffs) on the products (services) of natural monopolies for this period should be the pursuit of a balanced tariff policy, which could ensure:

- achievement of targeted inflation parameters and reduction of the negative impact of growth in prices (tariffs) of products (services) of natural monopolies on the rates of the economic growth;
- the level of tariffs (prices) sufficient for the operation of natural monopolies.

The parameters of the increase in the regulated prices (tariffs) for the period of forecast should create incentives not only for reduction of costs borne by natural monopolies, but also facilitate the optimization of the energy balance and create incentives for transparency and introduction of the principle of separate accounting depending on the types of activities, as well as stimulate producers to more efficiently utilize the products (services) of natural monopolies, reduce the volumes of consumption of these products (services) to the levels observed in developed economies.

Natural gas prices

The increase in natural gas prices at the rates, which in 1999 through 2004 outpaced the rate of inflation, permitted to make profitable the domestic natural gas prices. These measures allowed to partially cover the need for investments at the expense of profits derived on the domestic market. However, the domestic prices still do not allow to cover the full amount of investment necessary to meet the requirements pertaining to the maintenance and development of the infrastructure oriented towards the domestic market. The RF Ministry of Economic Development proposed to set forth the following marginal rates of increase in the average wholesale consumer prices of natural gas in 2005 and 2006: 20 per cent in 2005 and 11 per cent in 2006.

According to the preliminary estimates, the increase in the level of wholesale price of natural gas in 2005 and 2006 within the parameters indicated above will not result in a significant growth in costs borne by major consumers of natural gas, first of all, electrical power enterprises, what could permit to restrain the growth in energy tariffs, which have the most considerable impact on the growth in the costs borne by consumers. Thus, the increase in the natural gas prices in 2005 will result in the growth in costs in industry at large by 0.92 p. p. (in 2004 the increase in costs is estimated to make 0.77 p. p.). On the whole, the growth in the natural gas prices in 2005 will cause a rise in the costs borne by electrical power engineering by no more than 4.3 p. p. As concerns other industries, the growth in costs is expected to be rather insignificant – about 0.4 p. p. on the average.

Over this period, there should be continued the improvement of the mechanism of territorial differentiation of wholesale prices of natural gas and adjustment of the levels of wholesale prices in each price zone to the economically justified costs for extraction and transportation of natural gas from its deposits to consumers in the Russian Federation. In 2004, there should be taken a decision concerning an increase in the number of price zones, what may permit to reduce the scale of cross subsidizing of the zones situated in the European part of the Russian Federation at the expense of zones located closer to the deposits of natural gas.

Electrical power engineering

The growth in the tariffs in the electrical power engineering has the most significant impact on the costs borne by consumers, inflation rates, and the rates of economic growth. In order to ensure the reduction of inflation in 2005 through 2006 to the target values, the rates of growth in tariffs in electrical power engineering for end consumers should be at or below the inflation rates forecasted for the respective year. On the condition that the growth in tariffs on electrical power for end consumers in 2005 will outpace inflation rates (8.5 per cent) by no more than 1 per cent (due to the increase in the prices of natural gas in 2005), the prices of industrial products will increase by only 0.75 p. p. as compared to 0.9 – 1 per cent registered in 2004 and 1.7 per cent observed in 2003.

As concerns the most energy intensive industries, mostly export oriented ones (ferrous and non-ferrous metallurgy, a number of industries relating to chemistry and petrochemistry), there the increase in costs will be below 2 per cent to 3 per cent, therefore they remain competitive and the increase in costs will have no significant negative impact on the investment potential.

In this period, there should be continued the formation of a competitive market of electrical power. The development of the competitive environment in the electrical power engineering alongside with the caps on tariffs should ensure a reduction of costs borne by the industry.

Tariffs on railroad freight

Taking in account the fact that the contribution of tariffs on transportation in the prices of raw materials and intermediate products is rather significant, the growth in tariffs on railroad freight in the period of 2005 and 2006 should be moderate. This will allow to constrain the negative impact of increase in tariffs on consumer of railroad services, while ensuring the sufficient level of profitability in this sector. According to the estimates, the justified growth in tariffs should be at the target inflation rates for the respective period. In the period of 2005 and 2006, in the railroad transport there will be continued the creation of prerequisites for the development of a competitive environment by the method of separation of non-regulated types of activities, where tariffs should be formed in the market environment. Over the period included in the forecasts, the withdrawal from the structure of railroad transport and privatization of state owned enterprises not directly linked to organization of traffic and rendering of maintenance and repair services will continue. The objects pertaining to the social sphere should be transferred to the balances of RF subjects and municipal entities. In 2005, the increase in tariffs on railroad freight within the inflation rates will result in the aggregate growth in the costs borne by industrial consumers by 0.17 p. p. (0.25 p. p. in 2004).

The rates of growth in prices (tariffs) of the products (services) of natural monopolies presented in the report correspond to the macroeconomic indicators approved by the RF Government and permit to attain a number of key objectives set forth by the state, at the same time not infringing on the interests of natural monopolies. The main results of implementation of the proposals discussed above may be presented as follows:

1. The recommended parameters of the increase in prices (tariffs) of products (services) of natural monopolies do not result in significant increase in the amount of costs borne by consumers and do not have any significant impact on inflation rates. The estimates demonstrate that in 2005 inflation should decline to 6.5 per cent – 8.5 per cent (as compared with 10 per cent registered in 2004), while by 2007 it should make 4 per cent to 6 per cent. The contribution of the increase in regulated prices and tariffs in inflation should be below 2.6 to 2.7 p. p. in 2005, and in 2006 make 1.9 to 2 p. p. respectively.

2. The estimated rates of growth in prices (tariffs) of products (services) of natural monopolies significantly reduce the share of costs relating to the use of products and services of natural monopolies in the structure of costs of industrial products, what has a significant positive impact on the competitive capacity of domestic products on the internal and external markets.

3. The proposed program of changes in prices (tariffs) of electrical power reduces the gap between the prices paid by different categories of consumers, what permits to settle a key problem of the reform of the electrical power engineering – the reduction of cross subsidizing of electrical power tariffs on the part of

specific categories of consumers of electrical power (households, budget and agricultural consumers) at the expense of a lesser imbalance of increase in tariffs for industrial consumers, as well as reduction of subsidizing of production and transportation of heat energy at the expense of electrical power.

As concerns the natural gas industry, the amount of cross subsidizing in certain regions is not reduced and corresponds to the existing proportions, while in other regions it should be reduced at the expense of a more rapid rates of growth in natural gas prices for households than industrial consumers. The decision concerning the implementation of the territorial differentiation (i.e. the increase in the number of price zones from 7 to 11) will permit to significantly reduce the amount of cross subsidizing among price zones.

4. Implementation of the key principles of reform of the electrical power engineering, i.e. the separation of the types of operations (generation, transportation, and marketing) has already permitted to eliminate the internal cross subsidizing within the industry and increase the investment attractiveness and economic efficiency of production. This approach to the conduct of financial and economic operations should create incentives for other natural monopolies (OAO Gazprom, OAO RZhD) to introduce similar programs taking into account the specifics of their activities.

5. The approval of the program regulating the changes in prices (tariffs) of the products (services) of natural monopolies by the RF Government will permit the natural monopolies and consumers of their products to have more clear benchmarks for the planning of their own production and investment, at the same time creating the incentives for natural monopolies to reduce their costs.

E. A. Bolshakova

Review of economic legislation: May of 2004

In May, there were introduced the following changes in the legislation currently in force: there were changed the procedures governing the calculation of the tax rates on oil extraction and the procedures governing the calculation of the export customs duty on crude oil; there was changed the procedure governing the determination of the amount of long service pension provided to federal state officials; there was increased the amount of the average monthly salary basing on which there are calculated the amounts of the long service pensions due to federal state officials (from 1.8 salary to 2.3 salary). The RF Government took the decision to repurchase the USSR state treasury debentures and certificates of the USSR Sberbank (placed in the territory of the Russian Federation before January of 1992) owned by RF citizens.

I. FEDERAL LAWS of the Russian Federation

1. "ON AMENDMENTS TO ARTICLE 3 OF THE RUSSIAN FEDERATION LAW 'ON CUSTOMS TARIFF' AND ARTICLE 5 OF THE FEDERAL LAW 'ON AMENDMENTS TO SECTION 2 OF THE RF TAX CODE AND CERTAIN OTHER LEGISLATIVE ACTS OF THE RUSSIAN FEDERATION, AND ON ABOLISHMENT OF CERTAIN LEGISLATIVE ACTS OF THE RUSSIAN FEDERATION"

Enters into force in one month since the day of promulgation, with the exception of Article 2, which enters into force on January 1, 2005..

The law changes the procedure governing the calculation of the maximal rate of the export customs duty on crude oil established by the RF law "On the customs tariff" No. 5003-1 of May 21, 1993.

The rates of the export duty on crude oil set forth by the RF Government should not exceed the maximal amount of the duty rate calculated as follows:

In the case the average crude Urals oil prices on the world markets of crude oil (the Mediterranean and Rotterdam markets) in the period of monitoring are at or below US \$ 109.5 per 1 metric ton the rate of duty should be at 0 per cent;

In the case the average crude Urals oil prices on the world markets of crude oil (the Mediterranean and Rotterdam markets) in the period of monitoring exceed US \$ 109.5 per 1 metric ton, but is at or below US \$ 146 per 1 metric ton the rate of duty should be at or below 35 per cent of the difference between the average US \$ denominated price of 1 metric ton of this oil during the monitoring period and US \$ 109.5;

In the case the average crude Urals oil prices on the world markets of crude oil (the Mediterranean and Rotterdam markets) in the period of monitoring exceed US \$ 146 per 1 metric ton, but is at or below US \$ 182.5 per 1 metric ton the rate of duty should be at or below US \$ 12.78 per 1 metric ton and 45 per cent of the difference between the average US \$ denominated price of 1 metric ton of this oil during the monitoring period and US \$ 146;

In the case the average crude Urals oil prices on the world markets of crude oil (the Mediterranean and Rotterdam markets) in the period of monitoring exceed US \$ 182.5 per 1 metric ton, the rate of duty should be at or below US \$ 29.2 per 1 metric ton and 65 per cent of the difference between the average US \$ denominated price of 1 metric ton of this oil during the monitoring period and US \$ 182.5;

According to the amendments to the federal law No. 126 FZ of August 8, 2001, the tax rate on the extraction of oil should be increased from Rub. 347 to Rub. 400 per metric ton. The law introduces the changes in the formula determining the coefficient characterizing the dynamics of the world oil prices relating to the said tax rate: the formula $K_{ts} = (T_s - 8) \times R/252$ should be replaced with the formula $K_{ts} = (T_s - 9) \times R/261$.

2. "ON AMENDMENTS TO ARTICLES 14, 21, AND 25 OF THE FEDERAL LAW "ON STATE PENSIONS IN THE RUSSIAN FEDERATION" No. 34 FZ of May 8, 2004.

Enters into force on the day of promulgation.

Amendments to federal law «On state pensions in the Russian Federation» No. 166 FZ of December 15, 2001, concern the calculation and indexation of the amounts of the long service pension provided to federal state officials. The amendments envisage that the pensions of citizens residing in the regions of the Far North and regions with the similar status should be increased by the coefficient, for which are entitled employees on non-production sectors. In the case the citizen resettles from the said regions, the amount of pension should not include the respective coefficient. This regulation should be applicable to the legal relations established after January 1, 2002, i.e. before federal law No. 166 FZ entered into force. The amendments made by the law unify the indexation of pensions paid to federal state officials. From now on, the indexation depend not on increases in salaries of individual state officials, but on centralized increase in salaries of federal state officials in accordance with the procedure set forth by the RF Government. There was also increased the amount of the average monthly salary basing on which there are calculated the amounts of the long service pensions due to federal state officials (from 1.8 salary to 2.3 salary). Taking into account these changes, the long service pensions set for federal state officials before the entry in force of this federal law, but after July 1, 2002, should be recalculated.

II. RESOLUTIONS OF THE GOVERNMENT of the Russian Federation

1. "ON INTRODUCTION OF ADDITIONAL RESTRICTIONS ON THE INVESTMENT OF PENSION SAVINGS BY MANAGEMENT COMPANIES, WHICH CONCLUDED TRUST AGREEMENTS WITH THE RF PENSION FUND AND NON-STATE PENSION FUNDS ENGAGED IN MANDATORY PENSION INSURANCE, IN RUBLE DENOMINATED DEPOSITS WITH CREDITING ORGANIZATIONS" No. 247 of May 21, 2004

The resolution sets additional restrictions on the investment of pension savings in Ruble denominated deposits with crediting organizations by management companies, which made trust agreements with the RF Pension fund and non-state pension funds engaged in mandatory pension insurance. The resolution also sets forth the requirements concerning deposits and financial stability of crediting organizations. The former include the determination of the annual interest rates on deposits not less than yield to maturity of RF Ruble denominated state securities maturing on the date closest to the day of expiration of the deposit (in the case several issues of RF Ruble denominated securities mature on the day of expiration of the deposit, the interest rate on the deposit should be at or above the maximal yield of one of such issues), as well as the inclusion in the deposit agreement of a provision setting forth the terms on which the deposit and respective interest (taking into account the restrictions set forth by the resolution) should be returned. The latter include, for instance, the general license of the RF Central Bank for banking operations, positive financial results of operations in the last reporting year and the last reporting period of the current year, as well as the positive audit statement for the last year and absence of sanctions imposed by tax authorities and the RF Central Bank. Besides, the resolution determines the procedures governing the control over compliance with the additional restrictions, which should be vested with the federal executive authority supervising the sphere of formation and investment of pension savings.

2. "ON REPURCHASE OF THE USSR STATE TREASURY DEBENTURES AND CERTIFICATES OF THE USSR SBERBANK (PLACED IN THE TERRITORY OF THE RUSSIAN FEDERATION BEFORE JANUARY OF 1992) OWNED BY RF CITIZENS" No. 230 of May 6, 2004

This document was worked out in accordance with the federal law "On the federal budget for year 2004." Article 137 of the law envisages, in particular, the repurchase of the the USSR state treasury debentures and certificates of the USSR Sberbank (placed in the territory of the Russian Federation before January of 1992) owned by RF citizens, which are guaranteed savings in accordance with the federal law "On the restoration

and protection of savings of RF citizens” No. 73 FZ of May 10, 1995. The resolution of the RF Government approves the “Rules pertaining to the repurchase of the USSR state treasury debentures and certificates of the USSR Sberbank (placed in the territory of the Russian Federation before January of 1992) owned by RF citizens in 2004.” The resolution also establishes the amounts to be paid to the owners of these debentures and certificates. The rules determine the procedure of repurchase of the securities from the owners on the voluntary basis. The repurchase operations should be carried out by offices of the RF Sberbank on the presentation of the RF passport or other identification card confirming Russian citizenship of the owner. The amount to be paid should be determined proceeding from the face value of the respective security (in USSR Rubles) and include a compensation amounting to 40 per cent of the face value of the security and its yield. The procedure of calculation of the amount due to be paid for debentures and certificates is determined as follows: for each year after the end of circulation, including 2003, of these securities there should be paid a 10 per cent annual interest basing on the respective face value adjusted for the 40 per cent compensation. Coupons separated from the debentures should not be repaid. Repurchased debentures and certificates should be redeemed and no further payments related to these securities should be made. The RF Sberbank should present the data on repurchase of debentures and certificates to the RF Finance Ministry on the monthly basis separately for each type of securities. The expenditures of the RF Sberbank relating to the repurchase and redemption of the state treasury debentures and certificates should be compensated from the federal budget item envisaged for the servicing of the state domestic debt of the Russian Federation in 2004. The same funds should be used for the compensation of expenditures relating to the inspection and destruction of repurchased and redeemed debentures and certificates. The resolution sets forth concrete amounts to be paid for USSR state treasury debentures with 16 coupons and 8 coupons, as well as amounts to be paid to the owners of the USSR Sberbank certificates.

3. “ON AMENDMENTS OF THE RF GOVERNMENT RESOLUTION “ON APPROVAL OF THE RULES GOVERNING SUSPENSION OF OPERATIONS RELATING TO THE ACCOUNTS OF CHIEF ADMINISTRATORS, ADMINISTRATORS AND RECIPIENTS OF FEDERAL BUDGET FUNDS OPENED WITH THE FEDERAL TREASURY” No. 244 of May 17, 2004

The resolution amends item 2 of the Rules. The amendment envisages that the respective operations should be suspended in the case the federal institution failed to close its accounts opened with the RF Central Bank and (or) other crediting operations in order to conduct operations relating to funds derived from entrepreneurial or other types of commercial operations.

4. “ON AMENDMENTS TO THE REGULATIONS ON THE GOVERNMENTAL COMMISSION FOR ADMINISTRATIVE REFORM” No. 248 of May 21, 2004

Several amendments were made in the regulations on the governmental commission for administrative reform approved by the RF Government resolution No. 451 of July 31, 2003. These amendments concern the organization of activities of this governmental commission and its working groups. In particular, the amended regulations set forth that the governmental commission should analyze the function carried out by both federal executive authorities, and state institutions and federal state unitary enterprises in the jurisdiction of the federal executive authorities for their redundancy and overlapping. Besides, the governmental commission should be vested with the responsibilities relating to the analysis of proposals on optimization of the structure and functions of federal state institutions and federal state owned unitary enterprises in the jurisdiction of the federal executive authorities, as well as review of the said proposals and drafts of the respective regulatory and legal acts.

III. INSTRUCTIONS, REGULATIONS, AND ORDERS

1. Letter of the RF Central Bank No. 014-12-1040 “ON THE QUOTAS ON EXPORT OF CASH RF CURRENCY.”

The RF Central Bank more clearly defined the issues pertaining to the calculation of the quotas on import and export of cash RF currency by individuals (at present the respective maximal amount of cash RF currency is determined as 500 minimal wages). According to the letter, the amount of the minimal wage (as per articles 4 and 5 of the federal law “On minimal wage” No. 82 FZ of June 19, 2000, applicable in this case should make Rub. 100.

2. Letter of the RF Tax Ministry No. 33-0-11/285@ “ON THE USE OF CASH REGISTERES BY NOTARIES”

The letter explains that provisions of Article 2 of the federal law “On the use of cash registers in the course of cash payments and (or) payments made with the use of payment cards” No. 54 FZ of May 22,

2003, should not be applied to the legal relations pertaining to the payments for notary services. The primary accounting documents confirming the payment made for notary services should be the ledger registering notary actions. Private notaries should accept cash payments and register such payments in their respective ledgers.

3. Informational letter of the RF Tax Ministry No. 21-2-05/47@ of April 20, 2004 “ON CALCULATION OF THE MINERAL EXTRACTION TAX RATE IN MARCH OF 2003”

The letter informs about the data used for the calculation of the mineral extraction tax with respect to oil in March of 2004:

- the average level of Urals oil prices on the Mediterranean and Rotterdam markets (US \$ 31.20 per barrel);
- value of the Kts coefficient (2.6259);
- tax rate adjusted for the Kts coefficient (Rub. 911.5343 per metric ton).

I. V. Tolmacheva