

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
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The State of the Federal Budget

In the first six months of 2003, the revenues of the state budget (cash execution) made 20.6 per cent of GDP, while expenditures made 17.5 per cent of GDP (see Table 1). Therefore, the federal budget surplus made 3.0 per cent of GDP.

Table 1.

The monthly execution of the federal budget of the Russian Federation (in % of GDP¹, in comparable prices).

	VI'02	VII'02	VIII'02	IX'02	X'02	XI'02	XII'02	I'03	II'03	III'03	IV'03	V'03	VI'03	VII'03
Revenues														
Corporate profit tax	1.7%	1.7%	1.7%	1.6%	1.7%	1.6%	1.6%	1.2%	1.1%	1.4%	1.5%	1.4%	1.4%	
Personal 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%	
VAT, special tax and excises	3.5%	3.5%	3.3%	3.2%	3.1%	3.1%	3.1%	2.4%	2.7%	2.8%	2.9%	2.9%	2.8%	
Tax on foreign trade and foreign trade operations	9.3%	9.2%	9.1%	9.0%	8.9%	8.9%	8.9%	11.2%	10.1%	9.9%	9.6%	9.6%	9.2%	
Other taxes, duties and payments	6.9%	7.0%	7.0%	6.9%	6.9%	6.9%	6.9%	8.5%	7.4%	7.2%	7.2%	7.2%	6.9%	
Total- taxes and charges	2.3%	2.2%	2.1%	2.0%	2.0%	1.9%	2.0%	2.7%	2.7%	2.6%	2.4%	2.3%	2.2%	
Non- tax revenues	2.9%	2.9%	2.8%	2.8%	2.8%	2.9%	3.0%	3.4%	3.4%	3.4%	3.5%	3.5%	3.4%	
Revenues, total	1.8%	2.0%	2.0%	2.0%	2.1%	2.1%	2.1%	0.5%	1.7%	2.0%	2.2%	2.1%	2.0%	
Expenditure	19.2%	19.3%	18.9%	18.5%	18.6%	18.5%	18.6%	18.8%	19.0%	19.4%	19.6%	19.4%	18.8%	
Public administration	1.3%	1.4%	1.4%	1.4%	1.5%	1.4%	1.4%	17.5%	8.5%	1.3%	1.2%	1.7%	1.6%	
National defense	20.5%	20.7%	20.4%	20.0%	20.2%	20.1%	20.1%	20.8%	20.6%	20.9%	21.0%	21.3%	20.6%	20.4%
International activities														
Judicial power	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.5%	0.3%	0.3%	0.4%	0.4%	0.4%	0.4%	
Law enforcement and security activities	2.5%	2.5%	2.5%	2.4%	2.4%	2.5%	2.7%	1.5%	2.1%	2.6%	2.7%	2.7%	2.6%	
Fundamental research	0.4%	0.4%	0.3%	0.3%	0.3%	0.3%	0.3%	-0.3%	0.0%	0.2%	0.2%	0.3%	0.2%	
Services provided for the national economy	0.1%	0.1%	0.1%	0.1%	0.2%	0.2%	0.2%	0.1%	0.1%	0.1%	0.2%	0.2%	0.2%	
Social services	1.3%	1.3%	1.4%	1.4%	1.4%	1.5%	1.7%	1.1%	1.4%	1.7%	1.7%	1.7%	1.8%	
Servicing of public debt	0.2%	0.2%	0.2%	0.2%	0.2%	0.3%	0.3%	0.1%	0.2%	0.2%	0.2%	0.3%	0.3%	
Other expenditure	0.7%	0.8%	0.8%	0.8%	1.3%	1.3%	1.5%	0.2%	0.4%	0.5%	0.6%	0.7%	0.8%	
Expenditure, total	5.1%	5.1%	5.1%	4.9%	5.5%	5.6%	5.6%	1.5%	1.8%	2.0%	2.3%	2.2%	2.2%	
Loans, redemption exclusive	2.3%	2.2%	2.4%	2.4%	2.2%	2.0%	2.0%	1.7%	2.9%	3.0%	2.3%	2.1%	2.0%	
Expenditure and loans, redemption exclusive	4.0%	4.0%	3.9%	3.8%	3.9%	3.9%	3.8%	6.6%	7.1%	7.0%	7.0%	7.1%	7.1%	
Budget deficit (-)	17.1%	17.1%	17.1%	16.9%	17.8%	18.0%	18.7%	12.7%	16.4%	17.7%	17.7%	17.7%	17.5%	17.6%
Domestic financing	3.4%	3.6%	3.3%	3.1%	2.4%	2.1%	1.4%	8.1%	4.2%	3.2%	3.3%	3.6%	3.0%	2.8%
Other taxes, duties and payments	-1.6%	-1.8%	-1.3%	-1.2%	-0.5%	-0.2%	0.6%	-6.6%	-1.7%	-1.0%	-1.0%	-0.5%	0.3%	0.2%
Total- taxes and charges	-1.8%	-1.9%	-1.9%	-1.9%	-1.9%	-1.9%	-2.0%	-1.4%	-2.5%	-2.2%	-2.3%	-3.1%	-3.3%	-3.0%
Non- tax revenues	-3.4%	-3.6%	-3.3%	-3.1%	-2.4%	-2.1%	-1.4%	-8.1%	-4.2%	-3.2%	-3.3%	-3.6%	-3.0%	-2.8%

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

As compared with the figures registered in January through June of 2002, the budget revenues increased by 0.1 p. p. of GDP in January through June of 2003, while expenditures increased by 0.4 p. p. and budget surplus respectively decreased by 0.4 p. p. of GDP. At the same time, without SST the budgetary revenues increased by 0.8 p. p. of GDP and made 17.8 per cent of GDP..

VAT accounted for the major share of federal tax revenues – 33.5 per cent of the total tax revenues what is by practically 0.2 p.p. of GDP above the level observed in the respective period of 2002.

According to preliminary estimates, the cash execution of federal budget revenues made 20.4 per cent of GDP in January through July of 2003, what is by 0.3 p. p of GDP below the respective level observed in January through July of 2002. At the same time the cash execution of expenditures made 17.6 per cent of GDP (17.1 % of GDP in 2002); therefore, the surplus made 2.8 per cent of GDP (3.6 per cent of GDP in 2002).

According to the preliminary estimates of the Finance Ministry, in terms of fulfilled funding² the expenditures of the federal budget in January through July of 2003 made 18.8 per cent of GDP (see Table 2),

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).

while on August 1 of 2002 this indicator was at 18.2 per cent of GDP. As a result, as the amount of aggregate revenues increased by 0.4 per cent of GDP (in January through July of 2003 the level of revenues made 20.4 per cent of GDP) the surplus of the federal budget in terms of fulfilled funding in the first seven months of 2003 has also decreased by 0.2 p. p. in comparison with the figures registered in the respective period of 2002 and made 1.6 per cent of GDP.

Table 2.

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

	VI'02	VII'02	VIII'02	IX'02	XI'02	I'03	II'03	III'03	IV'03	V'03	VI'03	VII'03
Total	20.4%	20.0%	20.2%	20.1%	20.1%	20.8%	20.5%	20.9%	21.0%	21.3%	20.5%	20.4%
Public administration	0.5%	0.5%	0.5%	0.6%	0.5%	0.5%	0.6%	0.6%	0.6%	0.6%	0.5%	0.5%
National defense	2.7%	2.6%	2.7%	2.9%	2.6%	2.5%	3.1%	3.3%	3.2%	3.1%	3.0%	2.9%
International activities	0.3%	0.3%	0.3%	0.3%	0.3%	-0.2%	0.1%	0.1%	0.3%	0.3%	0.3%	0.3%
Judicial power	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Law enforcement and security activities	1.6%	1.6%	1.7%	1.8%	1.7%	1.9%	2.2%	2.3%	2.2%	2.2%	2.0%	2.0%
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%
Services provided for the national economy	1.1%	1.0%	1.5%	1.5%	1.5%	0.6%	0.8%	0.9%	0.9%	1.0%	1.0%	1.0%
Social services	5.4%	5.2%	5.7%	5.8%	5.7%	2.5%	2.7%	2.7%	2.9%	2.7%	2.6%	2.5%
Servicing of public debt	2.4%	2.4%	2.2%	2.0%	2.0%	1.7%	2.9%	3.0%	2.3%	2.1%	2.0%	1.9%
Other expenditure	4.0%	3.9%	3.9%	4.0%	3.8%	6.8%	7.5%	7.3%	7.3%	7.4%	7.3%	7.3%
Total expenditure	18.6%	18.2%	19.2%	19.4%	18.7%	16.8%	20.5%	20.8%	20.2%	19.9%	19.2%	18.8%
Профицит (+) / дефицит (-)	1.8%	1.8%	1.0%	0.7%	1.4%	4.0%	0.1%	0.1%	0.8%	1.3%	1.3%	1.6%

According to the estimates of the Revenue Ministry, in July of 2003 tax revenues of the federal budget made Rb. 115.5 billion (without the single social tax). In real terms the revenues made 260.4 per cent of the level registered in January of 1999, while the respective indicator was at 284.4 per cent in 2002 and 231.9 per cent in 2001 (see Table 3).

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					
230,0%	229,2%	265,5%	280,4%	233,2%	240,0%	260,4%					

* Без учета ЕСН.

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.

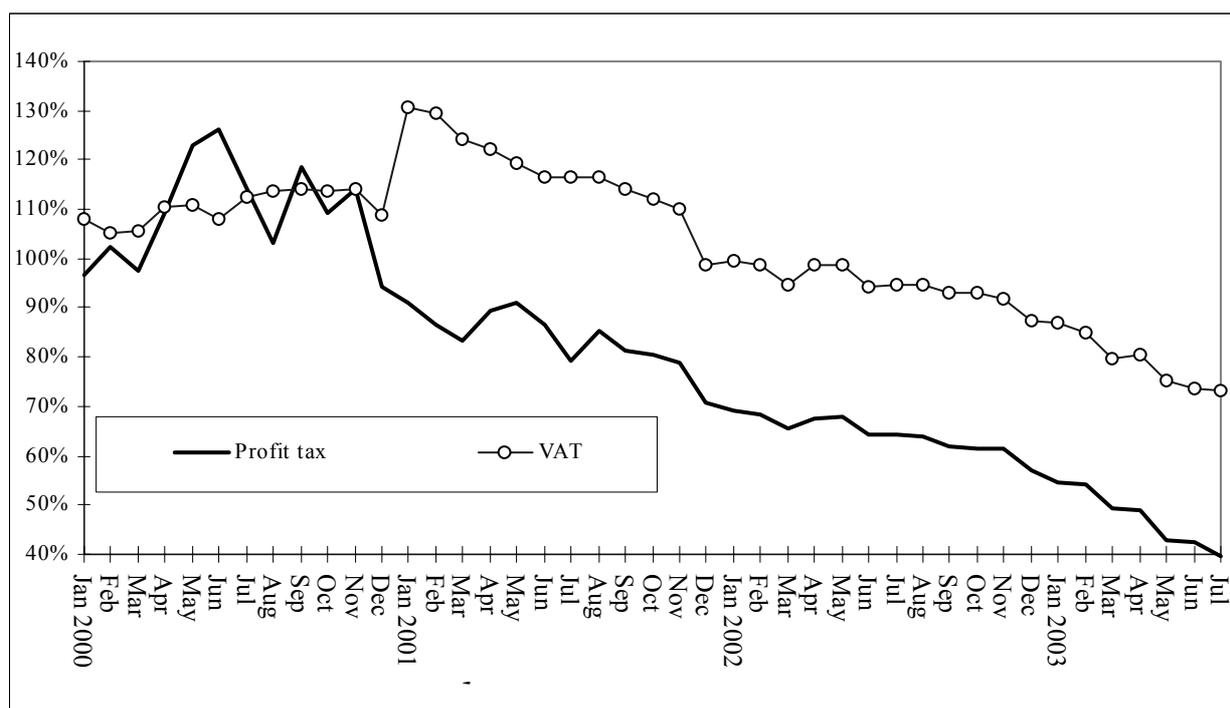


Fig. 1. Rate of growth of the real tax arrears to the federal budget (in % to June of 1999)

The dynamics of real arrears relating to major debts since January of 2000 is presented in Fig. 1. The debts related to the payments due to the federal budget made for VAT Rb. 238.0 billion as on August 1, 2003, increasing by almost Rub. 4.9 billion as compared with the figures registered in the preceding month, while the arrears of the profit tax decreased by practically Rb. 1 billion and made Rb. 27.7 billion. On the whole, the dynamics observed over the last 2 years still demonstrate a gradual decrease in the level of accumulated arrears as concerns not only the profit tax, but VAT as well.

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						
Taxes	25,6%	24,4%	25,6%	27,4%	27,1%	26,0%						
Revenues	32,0%	30,3%	31,5%	33,4%	33,6%	32,2%						
Expenditures	20,7%	25,3%	27,7%	28,8%	28,8%	28,6%						
Deficit	11,3%	5,0%	3,8%	4,5%	4,7%	3,5%						

* Без учета ЕЧН

The revenues of the consolidated budget in June of 2003 made 32.2 per cent of GDP, including tax revenues (without SST) at 26.0 per cent of GDP (see Table 4). Expenditures of the consolidated budget decreased by 0.2 p. p. in comparison with the figures registered in June of 2002 and made 28.6 per cent of GDP. As on August 1, 2003, the surplus of the consolidated budget made 3.5 per cent of GDP, what is by 0.3 p. p. of GDP below the level observed in the respective period of 2002.

S. Batkibekov

Monetary Policy

In July 2003 the rate of consumer price growth continued to decline. The consumer price index did not exceed 0.7 percent during the month. In mid-August foreign reserves returned to the level observed in the early summer of 2003. In August the RF Government approved the draft main guidelines of the monetary policy for 2004.

According to the State Committee for Statistics, inflation in the Russian consumer market was 0.7 percent in July, which is similar to last year's inflation level. In the period from January to July 2003 inflation was 8.7 percent, as opposed to 9.8 percent in January-July of 2002. The basic consumer price index (which leaves out short-term irregular price changes due to individual factors of administrative, occasional or seasonal nature) was 100.7 percent in July (year to month: 105.4 percent). In July, 2003, the average daily price growth in the RF was 0.023 percent against 0.027 percent in June. Foodstuffs grew in price 0.4 percent on average (June: 0.8 percent), and, without taking the fruit and vegetables into consideration, the growth of foodstuff prices amounted to 0.7 percent (June: 0.6 percent). In July, like in June, the prices of non-foods increased 0.5 percent. Service prices grew 1.9 percent in July as opposed to 1.2 percent in June.

According to preliminary estimates, the consumer price index was 0 to 0.2 percent in August.

In July, 2003, the foreign reserves remained unchanged, amounting to US\$ 64.4 billion on 1 August, 2003. In August the trend towards reserve growth resumed, and during the first two weeks of August the reserves reached the level of early June, 2003 (US\$ 64.7 billion). In the course of July, the narrow monetary base grew from RUR 1123.6 to RUR 1159.7 billion (+3.2 percent) (see Fig. 2). During the first two weeks of August the monetary base increased another 3.3 percent.

The broad monetary base, for the first time since January, 2003, decreased in July by 1.5 percent, going down from RUR 1,534 billion to RUR 1,511 billion on 1 August. Taking into account the cash in the vaults of credit institutions, the amount of cash in circulation grew from RUR 904.3 billion to 971.9 billion, or 7.48 percent. Funds held by banks in correspondent accounts with the Bank of Russia were RUR 165.4 billion on 1 July as opposed to RUR 180.2 billion in early June.

In June, 2003, for the first time during the entire period that the currency market has been monitored by the Bank of Russia, the exports of foreign currency cash by the authorised banks exceeded the imports.

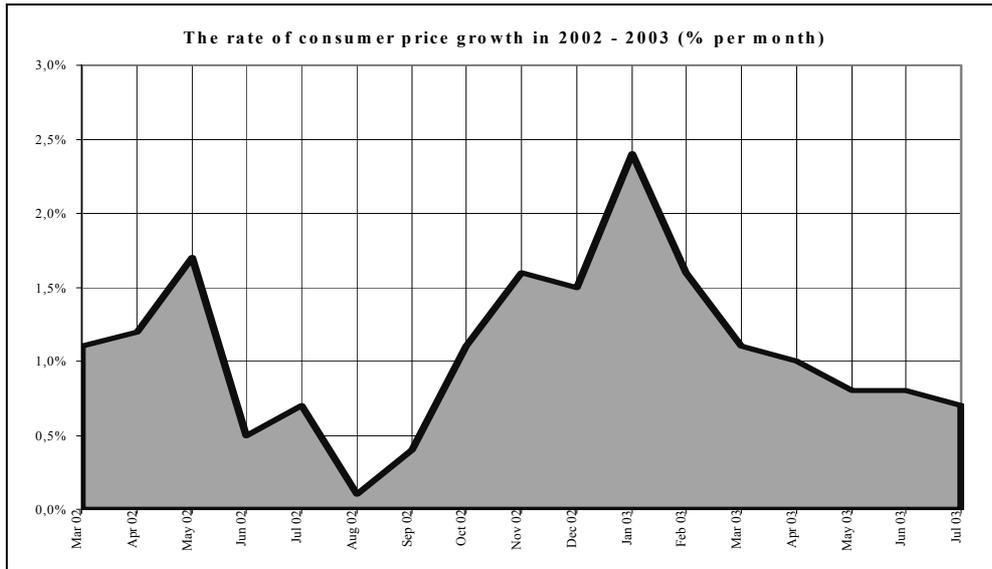


Fig. 1.

Changes in the Monetary Base and in the Gold and Foreign Currency Reserves in 2002 - 2003.

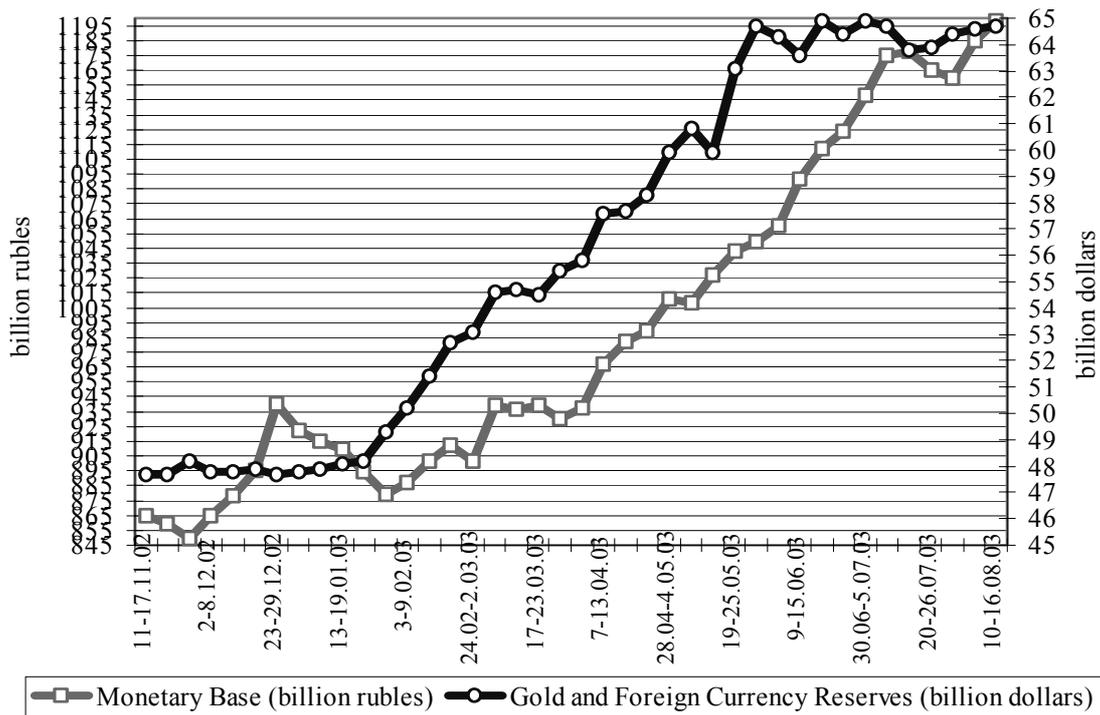


Fig. 2.

Russian external debt payments amounted to US\$ 2.098 billion in August. This includes payments to official creditor countries, banks and companies that reached US\$ 1.926 billion (US\$ 923 as debt repayment and US\$ 1.003 billion as interest payments). Russia's payments to international financial institutions were US\$ 171,5 million in August, including US\$ 126 million transferred as debt repayment and US\$ 44.9 million as interest payments. No RF Eurobond or Minfin bond payments were made in August. Thus, the amount of

payments made in terms of the Russian national external debt repayment and servicing reached RUR 339 billion in the period from January to July. This amount includes RUR 227.1 billion transferred on account of the RF external debt repayment and RUR 111.9 billion transferred on account of interest payments.

In August the RF Government approved the draft main guidelines of monetary policy in 2004 as a whole. The main target set forth in these guidelines is to reduce inflation to 8-10 percent in 2004. Says Chairman of the Central Bank Sergei Ignatiev: "In doing so, the Central Bank will strive to prevent the strengthening over seven percent of the real effective exchange rate of the Rouble in the event oil prices turn out to exceed the projected level".

Two versions of the Programme have been prepared for year 2004; Version One is based on the estimated price of US\$ 18.5 per barrel bbl for Urals oil in 2004, and Version Two proposes that the price will be US\$ 22 / bbl.

In addition, the Bank of Russia leaves without changes the target projected inflation indicator, which was fixed at the 12 percent level for year 2003. Moreover, the RF Central Bank has not revised the projected indicator of the Rouble's real effective exchange rate strengthening that was fixed at the six percent for 2003. It should be noted that over the first seven months of 2003 the real effective exchange rate of the Rouble grew approximately four percent stronger.

As a result of its meeting, the RF Government instructed the Ministry of Finance, Ministry for Economic Development and Central Bank to present proposals on the sterilisation of money supply and prevention of excessive strengthening of the Rouble.

Trounin P.

Money supply and money demand in the first half year of 2003

In the first half year of 2003, the situation observed in the monetary sphere was characterized by contradictory trends. On the one hand, as it is seen in Fig. 1, there was observed a sharp increase in real cash balances both on the accounts of enterprises and households, what indicated a growth in disposable funds on hand of all categories of economic agents.

By end of July, 2003, the real money supply (M_2) has reached 155 per cent of the level registered in December of 1997 increasing threefold over the post-crisis period. The real cash balances on the Ruble denominated enterprises' accounts have exceeded the pre-crisis level almost two times, while since the moment when there was registered their minimal values (the autumn of 1988) this figure increased more than threefold. In February of 2003, the balances on household accounts with commercial banks exceeded the pre-crisis maximum (in real terms) and as on July 1 make about 127 per cent of the December level (+ 20 per cent over 6 months of 2003). Monetization of GDP made 21.5 per cent by the end of the first half year of 2003.

On the other hand, the dynamics of the money multiplier (the ratio between M_2 and the reserve money) demonstrate that the mechanisms of money creation in the economy work very inefficiently (see Fig. 2). Practically over the whole first half year there were observed a rather sharp downfall of this indicator.

A preliminary analysis of the observed trends reveals that current situation in the monetary sphere is similar to the processes observed in late 1999 through 2000, i.e. a rapid growth in money supply at the background of a moderate inflation (over six months M_2 increased by 22.9 per cent, while the CPI grew by 7.9 per cent), at the same time, the multiplier declined. In other words, similar to 2000, the increase in disposable funds predominantly occurs at the expense of export proceeds, which transform in Ruble emission via operations conducted by the Central Bank of the Russian Federation. At the same time, the role played by commercial banks, which actively expanded the amounts and forms of their activities in 2001 and 2002, shrinks again. Therefore, it becomes possible to arrive to the conclusion that in a favorable situation the Russia's financial (banking) system to a considerable extent stops to move in the direction of the formation of a structure similar to financial sectors observed in developed countries, probably due to, among other reasons, the lack of demand for new possibilities and services on the part of the real sector.

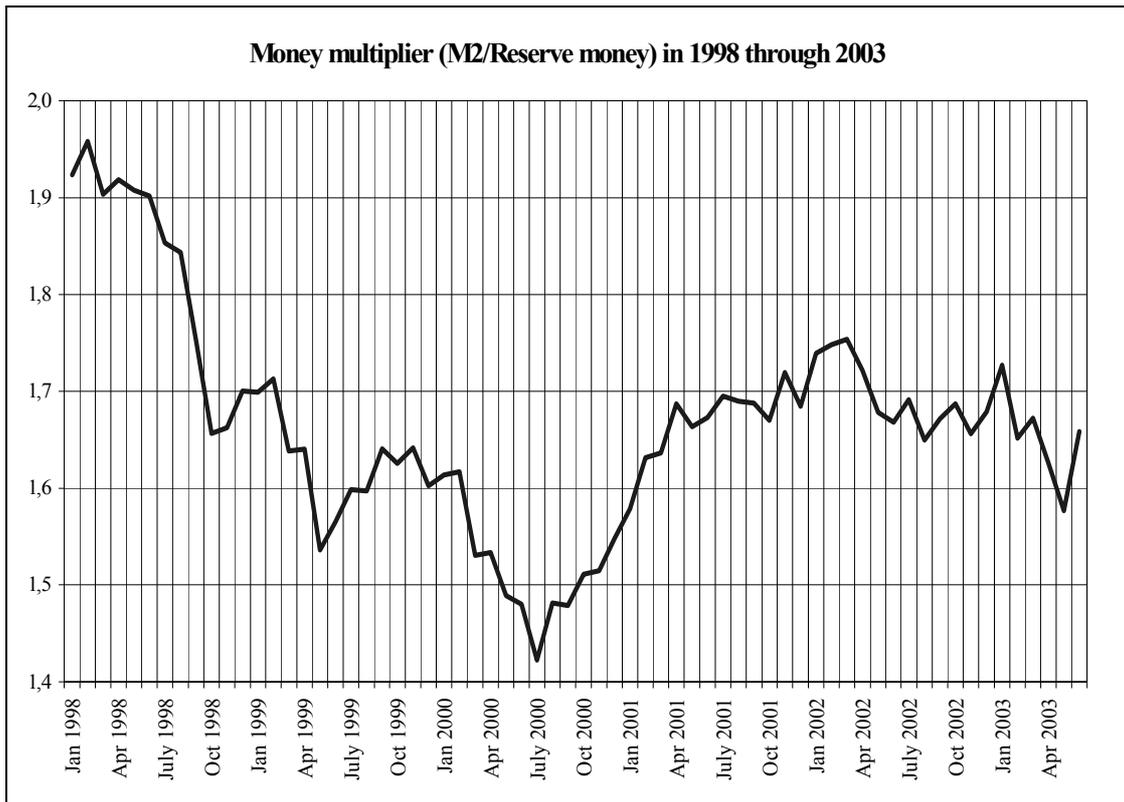


Fig. 1.

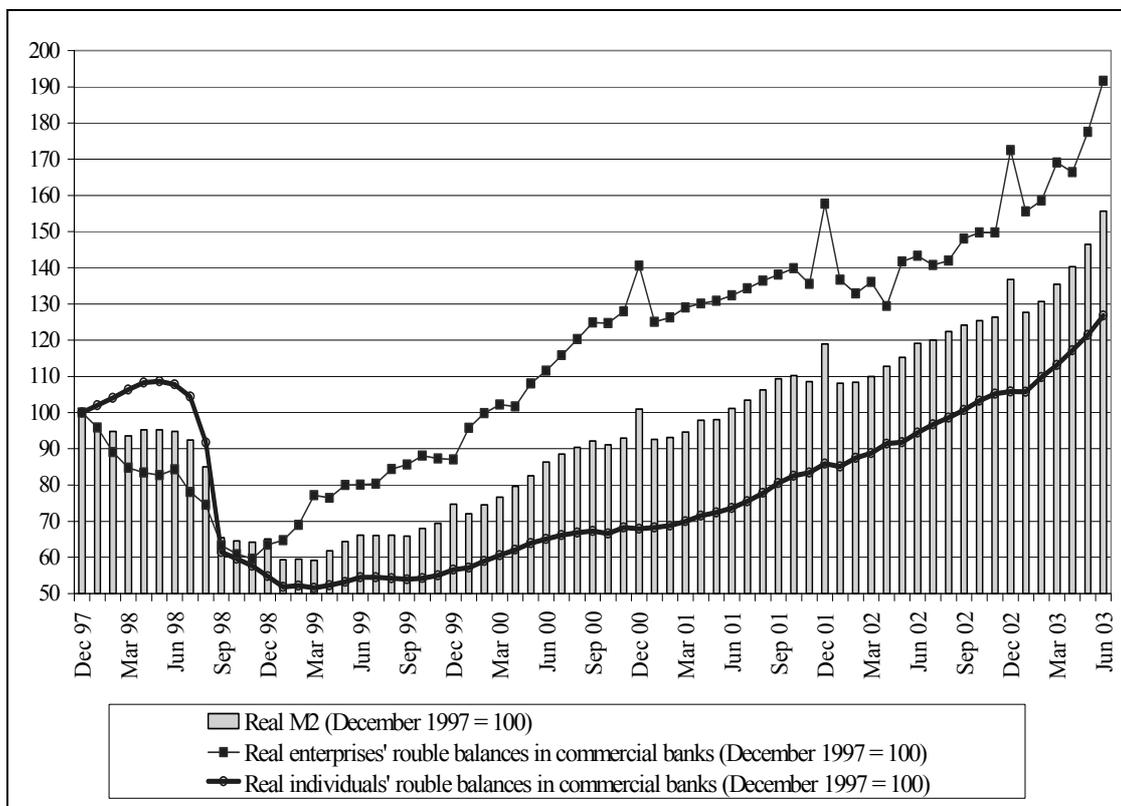


Fig. 2. Money multiplier (M2 / reserve money) in 1998 through 2003

S. Drobyshevsky

Financial Markets

Public Securities Market

This August, different trends were observed on the Russian market of forex denominated external debt. Although before the mid-month bond quotations continued to fall, by August 22 the prices of forex denominated bonds regained some of this decline. For instance, on August 22 the yield to maturity of RUS-30 made 7.90 per cent per annum, and of RUS-28 was at 7.84 per cent per annum, what was somewhat below the levels registered in early August of 2003. Besides, as of August 22, yields of Russian Euro bonds were as follows: 7th OVVZ tranche, 6.96 per cent; 6th OVVZ tranche, 4.52 per cent; 5th OVVZ tranche, 6.10 per cent; RUS-07, 4.86 per cent.

Over the period from July 21 to August 22, the total turnover of the GK0 – OFZ market made Rub. 28.5 billion, what corresponds to the average amount of trading of Rub. 1.19 billion. So, over the last week of July and three weeks of August the activity of operators on the market of the public bond market continued to abate.

Over the period under observation, two placements of government bonds took place. For instance, on August 3, there was held an auction for the placement of GKO 21170 maturing on July 21, 2004 and with nominal value of Rub. 5 billion. The nominal demand amounted to Rub. 4.9 billion, while the amount of placement made Rub. 1.015 billion. The cut off price was set at 94.115 per cent (income of 6.52 per cent per annum). On August 20, there was carried out the placement of OFZ - FD 27024 issue with maturity on April 19, 2006. The amount of placement made Rub. 7 billion, while the nominal demand amounted to Rub. 6.86 billion. The cutoff price was set at 99.92 per cent, what corresponded to the yield to maturity at 8 per cent per annum.

As of August 26, the nominal amount of the GKO OFZ market made Rub. 300.37, while in money terms it was at Rub. 319.32. The duration of the GKO OFZ market portfolio amounted to 837.51 days.

Minfin bonds' yields to maturity in May 2003 through August 2003

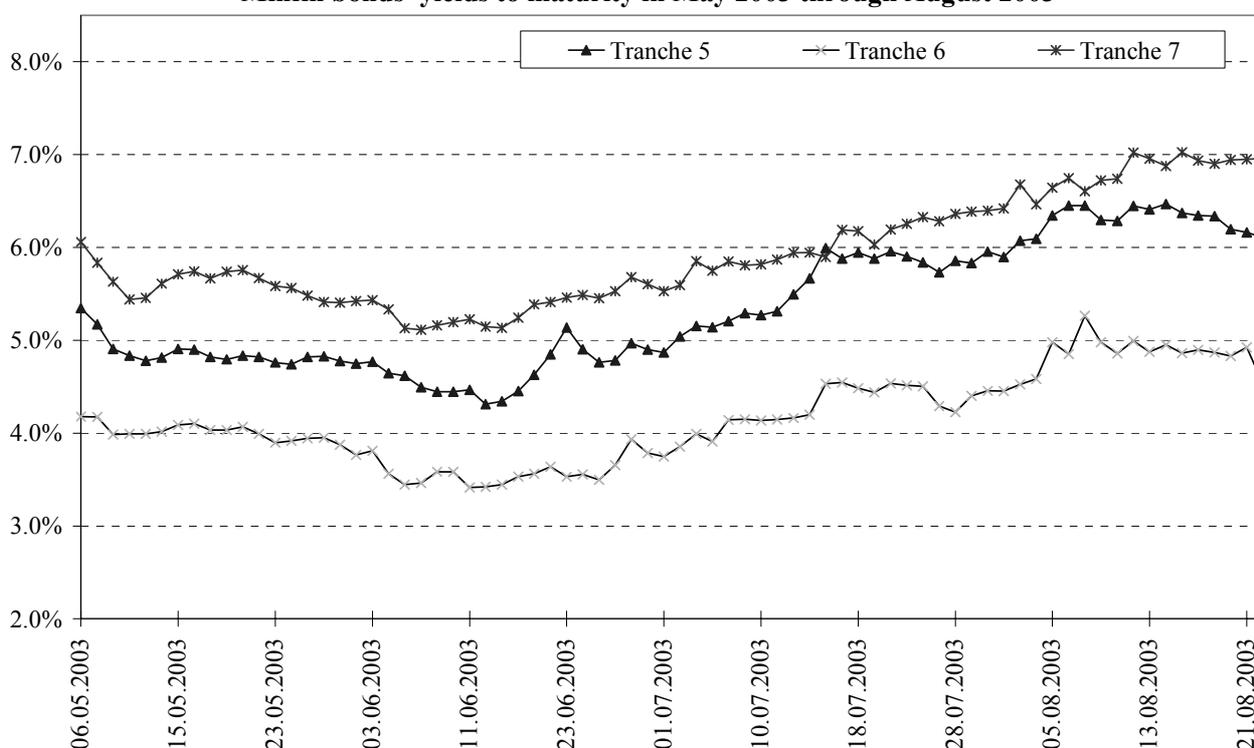


Fig. 1.

Yields to maturity of the Russian eurobonds with maturity in 2030, 2007 and 2028 in May 2003 through August 2003

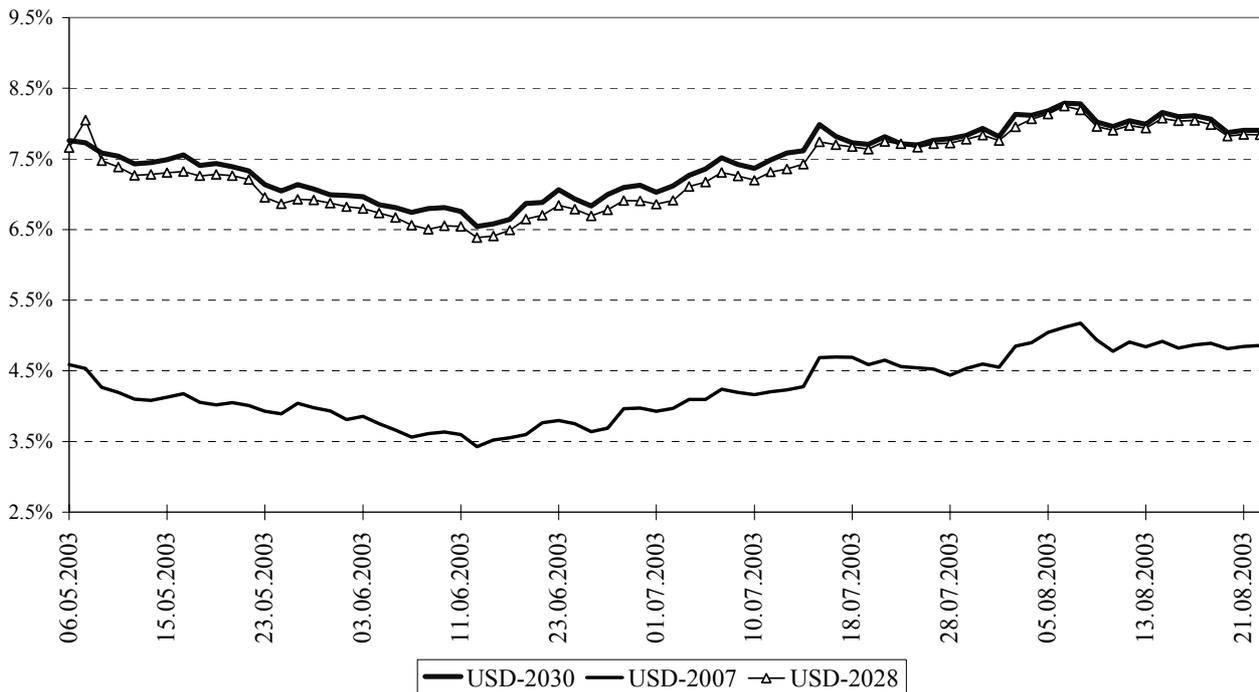


Fig. 2.

Corporate Securities Market

The market situation.

Throughout August of 2003, stock prices were steadily growing on the Russian stock market after a sharp decline observed in July. In the period from July 28 to August 27, the RTS Index rose by 56.04 points (+ 12 per cent). Over this period, that index reached another post-crisis maximum and made 528.33 points⁴ (closing of trades on August 19). The amount of trading in the above period from July 28 to August 27 made US \$ 362.8 million, while the average daily trade amount was at US \$ 15.78 million, what was by US \$ 11.2 million below the value of the respective indicator registered this July. In this period, the maximum daily trade volume (US \$ 28.15 million) was registered on July 30, while the minimum daily trade volume (US \$ 6.715 million) was registered on July 31. Therefore, it shall be noted that throughout August on the market there was observed a steady positive trend of quotations characterized by a relative decline in activity of the market operators.

Over this period, practically all blue chips demonstrated positive rates of growth in their respective market values. In August, the highest growth in prices was observed with shares of Yukos, which gained 21.39 per cent over this period, closely followed by shares of the RAO UES (a 14.81 per cent gain). The shares of these companies were followed by Tatneft shares, the market value of which increased by 14.07 per cent. Over the preceding month, the quotations of Mosenergo, Rostelekom, and Surgutneftegaz increased by 9.39 per cent, 8.87 per cent, and 5.53 per cent respectively. The quotations of Norilsk Nickel and Sibneft have changed practically identically – they increased by 4.34 per cent and 4.35 per cent respectively. The only company whose market value decreased was Sberbank of RF as the quotations of its shares fell by 3.96 per cent. Thus, in August the majority of blue chips regained some of the decline in quotations observed in July of 2003.

⁴ The last time the index reached a higher level was on October 23, 1997.

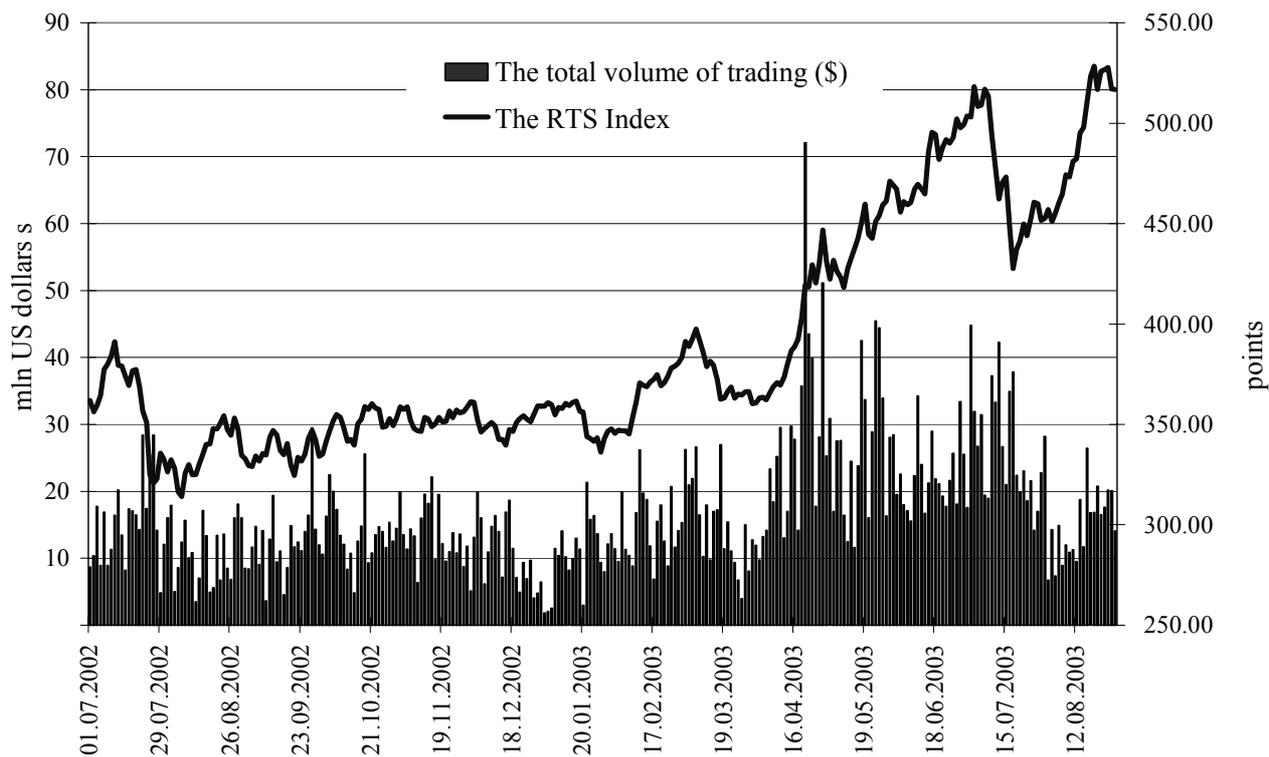


Fig. 3.

**Dynamics of the Russian Blue Chips
between July 25, 2003 to August 27**

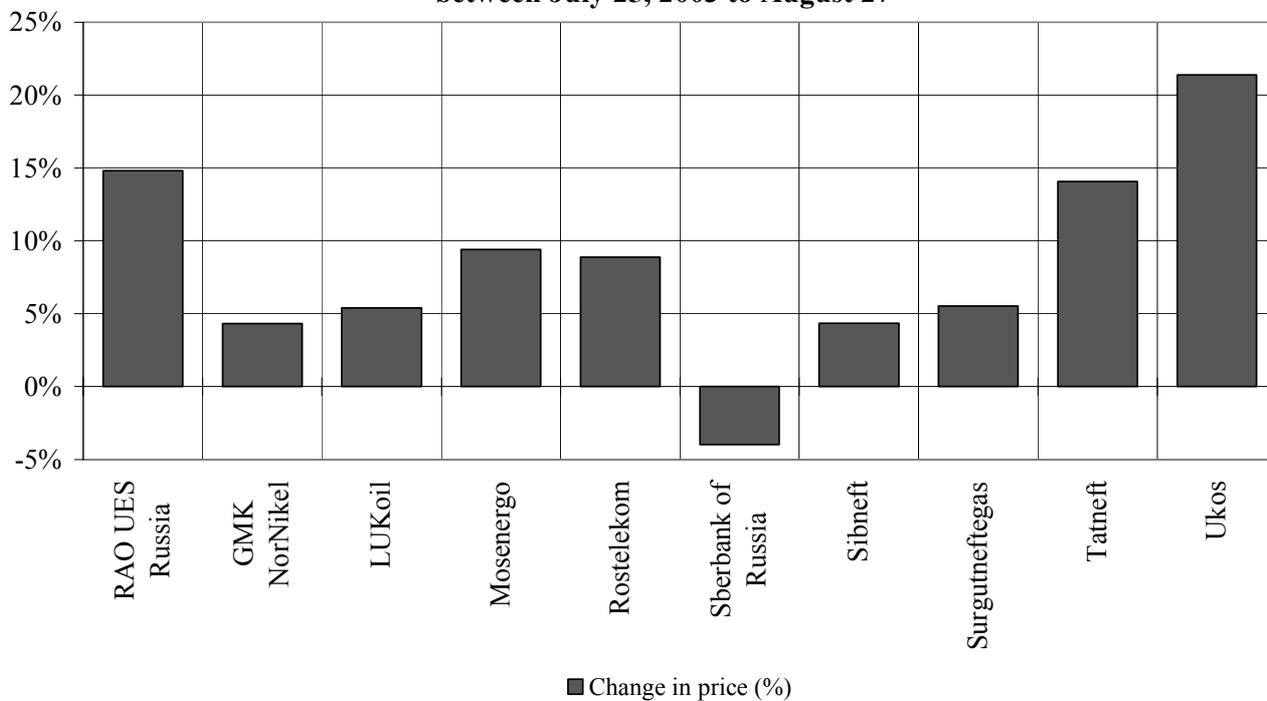


Fig. 4.

In August, shares of the RAO UES retained their leading position in the volume of trade; deals with shares of that power generation holding accounted for 35.70 per cent of the total volume of trades. This month, rating second and third in the volume of trades were, respectively, shares of LUKoil (14.52 per cent) and shares of Yukos (13.61 per cent), followed by shares of Surgutneftegaz and Nor Nickel (9.16 per cent and 4.78 per cent respectively). Therefore, in August of 2003 the aggregate share of the five most liquid papers accounted for 77.77 per cent of the total RTS volume.

As of August 27, according to RTS data, the five largest issuers as regards capitalization were as follows: Yukos (US \$ 31.1 billion, LUKoil (US \$ 16.4 billion), Surgutneftegas (US \$ 14.7 billion), RAO UES (US \$ 12.8 billion), and Sibneft (US \$ 12.1 billion).

The market for term contracts. In the July 28 – August 27 period, there was observed a decline in activity on the forward market. The volume of trading in FORTS forward contracts amounted to Rub. 17.3 billion (69.5 thousand deals and 2.26 million contracts), what was below the figures registered this July (at that time, the turnover made Rub. 21.2 billion, there were carried out 72.4 thousand transactions, and concluded 3.06 million contracts). The largest part of the aggregate turnover made futures contracts, the respective turnover accounted for Rub. 16.1 billion (2.1 million contracts, 67.3 thousand transactions). The maximum trading volume was observed on August 25 and made Rub. 1,379 billion, while the minimum trading volume (Rub. 312.625 million) on the forward market was registered on August 4.

Corporate bond market. In the first 3 weeks of August, on the whole the corporate bond market stagnated: by August 26 the amount of trading has already steadily contracted for the fourth week running, while prices predominantly declined. At the same time, over the whole summer period the least liquid instruments were among the most vulnerable ones on the market: organizers stopped to quote such instruments at the least sign of a contraction in business conditions. Over the period from August 1 to August 22, the turnover of the MICEX corporate bond section made Rub. 4.24 billion.

On August 5 and 6, the placement of Altaienergo bonds took place at MICEX and SMVB, amounting to Rub. 500 million and Rub 100 million respectively. Forty eight bids totaling to Rub. 545.5 million were registered at MICEX, the first coupon rate was set at 17.5 per cent per annum, what corresponded to the yield to maturity in one year (two years) at 18.54 per cent per annum (18.97 per cent per annum). Aeroflot has taken a decision to set the last coupon rate (the second bond tranche in the amount of Rub. 1 billion) at 0 per cent per annum, i.e. the issuer intends to redeem the total issue on the date of the next offer (September 15, 2003).

On August 19, MICEX held an auction for placement of the third bond issue of the Moscow oblast amounting to Rub. 4 billion. The bond maturity was set at 4 years, the coupon (11 per cent per annum) should be paid every six months.

Exogenous factors of the dynamics of the Russian stock market. Throughout August, an upward trend prevailed on the international oil market: over the month the prices of Brent oil were at or above US \$ 29 per barrel, what was caused by several factors. Firstly, on July 31 OPEC retained export quotas at the preceding level. Secondly, an important factor affecting price movement was the situation in Iraq: the instable operation of the largest oil processing plant in South Iraq (Basra) and Kirkuk - Ceyhan pipeline prevented the oil export from Iraq to resume in pre-war volumes. At last, a certain decline in gasoline reserves was registered in the USA, what determined a consequent rise in prices until the end of the month. For instance, as per data available on August 27, Brent oil prices on the world market were at US \$ 30.07 per barrel.

In August, on world stock markets there was also registered a growth in quotations indicated by the positive dynamics of the major world stock indices. For instance, American stock indices DJIA and NASDAQ grew from the beginning of the month to August 26 by 2.5 per cent and by 4.08 per cent respectively and from the beginning of the year to the same date by 8.59 per cent and by 27.65 per cent respectively. European and Asian stock indices were also characterized by positive growth rates: for example, the FTSE 100 (the UK) grew in a month (year) by 0.67 per cent (4.31 per cent), the DAX 30 (Germany), by 2.39 per cent (11.72 per cent), the CAC-40 (France), by 3.16 per cent (2.16 per cent), Nikkei-225 (Japan) – by 6.84 per cent (18.58 per cent), Seoul Composite (South Korea) – by 7.12 per cent (13.90 per cent), Straits Time (Singapore) – by 3.28 per cent (19.41 per cent). In August, a growth in stock indices was also observed on stock markets of developing countries. For instance, the Bovespa Index in Brazil grew by 8.12 per cent, while the gain of the MSCI developing countries index made 6.25 per cent.

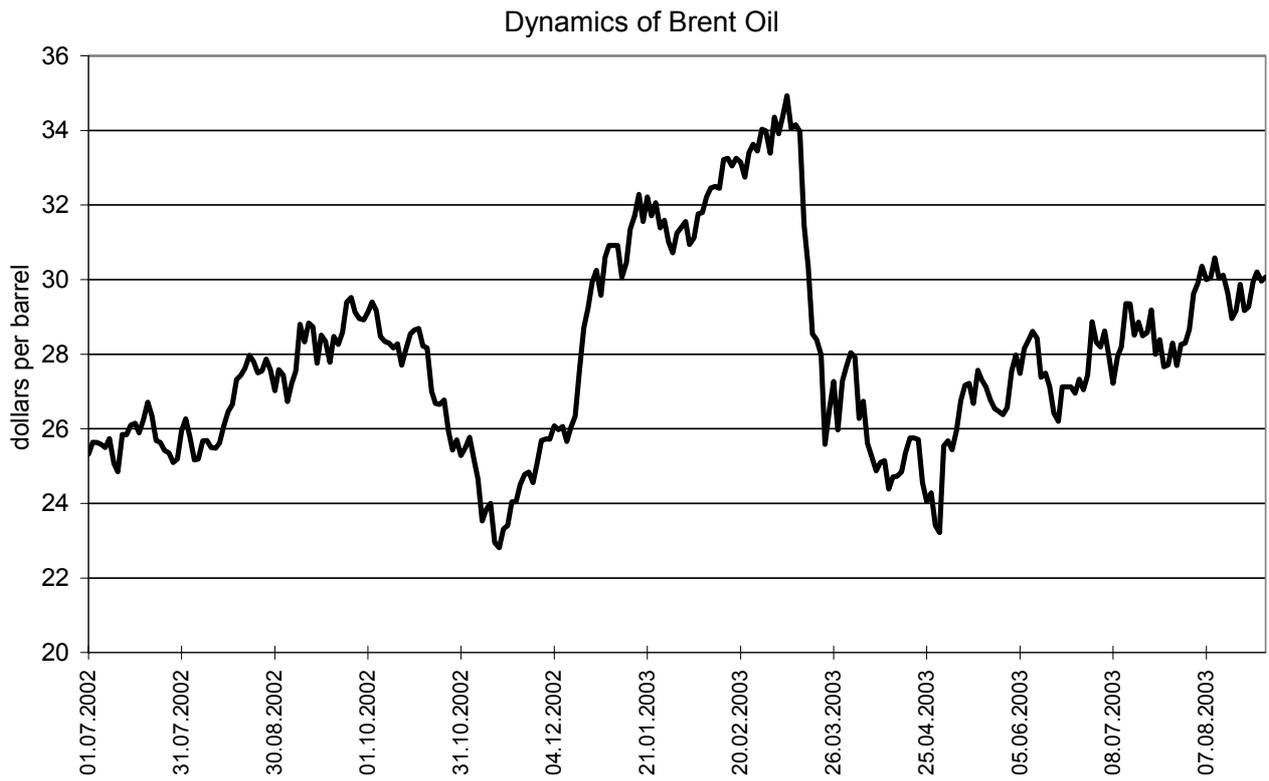


Fig. 5.

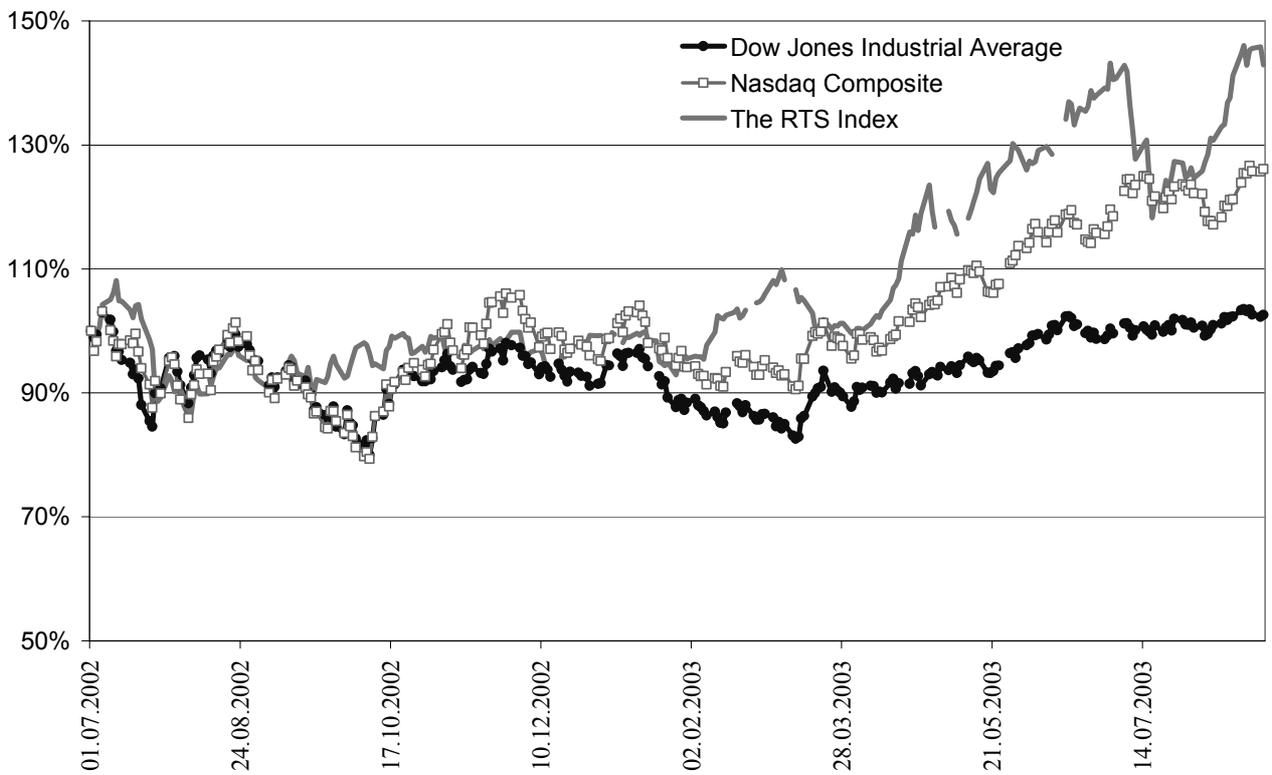


Fig. 6.

It is to be noted that among the factors which contributed to growth of the US stock market indices were publications of a number of statistical reports and corporate financial results for the 2nd quarter. The economic statistics data pointed to the fact that the economic situation was improving at a faster rate. For instance, in July there was registered an increase in retail sales, producer and consumer prices, and industrial output. The index of consumer confidence also remained at a high level. The number of new applications for the payment of the unemployment insurance made 386 thousand, what turned out to be considerably below the estimate (395 thousand). The positive trend of the market was also supported by the US FRS statement that the basic interest rate (currently at 1 per cent) would be kept at a low level for a long time.

The growth of European indices was somewhat less, what, in particular, was determined by slower rates of recovery of the European economy as compared with the economy in the USA. On the whole, the dynamics registered on European markets echoed the situation on the US stock market. At the same time, the positive dynamics of the European stock indicators were primarily determined by growth in market value of shares issued by export oriented companies, for which the growth in the USA was most favorable.

Corporate news.

The OAO GMK Norilsk Nickel

Early in August, the GMK Norilsk Nickel in the person of the Eurasian investment pool (Evroziatskiy investitsionny pul) company representing its interests won the auction for sale of the controlling interest in the gold mining OAO "Rudnik imeni Matrosova" previously owned by the state. The final value of the block of shares made Rub. 1 billion 033 million. According to the GMK management, in the future the company intends to increase its share in the OAO "Rudnik imeni Matrosova" to a level exceeding 75 per cent. The most valuable asset owned by the purchased company is the license for development of the Natalkinski gold deposit, where explored reserves make at the moment 250 metric tons. At the same time, according to Norilsk Nickel experts' evaluations, the reserves of this deposit have not been fully explored yet.

Besides, the GMK Norilsk Nickel and NK Rosneft have signed a memorandum on cooperation. The parties confirmed their interest in the development of the OAO Arkhangelskiy Morskoi Torgovy Port (Arkhangelsk Sea Trading Port) (AMPT, port district "Ekonomiya") and OAO NK Rosneft – Arkhangelsknefteprodukt (oil terminal "Talagi"). The parties intend to pursue common policies as relates to the settlement of issues pertaining to use and development of the North Sea Route infrastructure, effective usage of which is vital for both companies.

The NK LUKoil

In the beginning of August, in Aksai (the West Kazakhstan oblast) there was launched into operation the Karachaganakskiy processing complex, which shall ensure preparation of gas condensate directly at the deposit, what shall sharply enhance the project efficiency. There was also commissioned the 650 km long pipeline for transportation of liquid hydrocarbons, which connects the oil and gas condensate deposit Karachaganak and Atyrau, where the raw materials will enter the Caspian pipeline consortium (CPC) system.

OAO NGK Slavneft

In January through July of 2003, enterprises of the NGK Slavneft extracted 10.01 million metric tons of oil, what is by 21 per cent above the figures registered in the respective period of 2002. As concerns the major extracting enterprise of the holding – the OAO Slavneft – Megionneftegaz, its volume of extraction made 9.67 million metric tons over seven months and exceeded the figures registered in January through July of the preceding year by 21 per cent.

At the same time, this July the total volume of the company's oil production made 1.57 million metric tons, what is by 27 per cent above the respective indicator registered in July of 2002. The average daily oil output has also reached record highs since the date of the company's establishment: the volume of extraction made 50.57 million metric tons, while early this year this indicator was only slightly above 43 thousand metric tons.

Over seven months of this year, the enterprises of the company have processed 11.70 million metric tons of oil, what is by 3.7 per cent above the figures registered in the respective period of the preceding year. In July, the total amount of processing made 1.67 million metric tons of hydrocarbon raw materials and was by 7.3 per cent above the indicators observed in July of 2002.

The OAO NK YUKOS

In August, major shareholders of Sibneft and YUKOS reached an agreement as concerns a number of corporate governance issues. For instance, according to the arrangements, the Board of Directors of the YUKOSSibneft company shall be elected by cumulative vote. Besides, it is planned that the newly

established company shall pay quarter and annual dividends at no less than 40 per cent of its net profits calculated in accordance with the US GAAP.

Also in August, YUKOS and the Austrian company OMV signed a mutual understanding memorandum concerning the construction of a new pipeline connecting the city of Bratislava (Slovakia) and the oil processing plant owned by OMV in the town of Schwehat (Austria). It is planned to transport up to 5 million metric tons of oil a year via this pipeline in the framework of the long term agreement. The estimated cost of the project amounts to Euro 28 million.

The RAO UES of Russia

The RAO UES of Russia has prepared the financial statements for the first six months of 2003 in accordance with the RSBU requirements. The proceeds from core business of the RAO UES of Russia increased from Rub. 23.9 billion to Rub. 30.5 billion in the first six months of this year as compared with the figures registered in the respective period of the preceding year. In the first six months of the year, the RAO UES profits on sales grew by Rub. 0.9 billion as compared with the indicators observed in the respective period of 2002.

Over the reporting period, the creditor indebtedness of the RAO UES of Russia decreased more than two times: from Rub. 44.7 billion to Rub. 16.6 billion. As on June 30, 2003, the debtor indebtedness of the RAO UES of Russia was at Rub. 36.6 billion (Rub. 22.3 billion as in the beginning of 2003). The increase in the debtor indebtedness was caused by the redistribution of accounting records among the balance sheet items amounting to Rub. 12.7 billion, as well as reflection of dividends accruals in the reporting.

In the first six months of the year, the net profits of the RAO UES derived from its core business made Rub. 11.6 billion. The decrease in profits registered in the first six months of 2003 as compared with the figures registered in the respective period of the preceding year by Rub. 11.1 billion may be explained by the fact that in the financial results of 2002 there were reflected proceeds from the repayment of the Russian Federation debt to the Czech Republic in accordance with the RF Government resolution on the settlement of the RF public debt to the Czech Republic.

Table 1.

Dynamics of International Stock Market Indices

Data as of August 26, 2003	Value	Change within the month (%)	Change since the beginning of the year (%)
RTS (Russia)	517.01	12.23%	43.30%
Dow Jones Industrial Average (USA)	9340.45	2.50%	8.59%
Nasdaq Composite (USA)	1770.65	4.08%	27.65%
S&P 500 (USA)	996.73	1.54%	9.70%
FTSE 100 (UK)	4177.40	0.67%	4.31%
DAX-30 (Germany)	3455.48	2.39%	11.72%
CAC-40 France)	3256.69	3.16%	2.16%
Swiss Market Switzerland)	5156.70	3.74%	5.25%
Nikkei-225 (Japan)	10332.57	6.84%	18.58%
Bovespa (Brazil)	14878.00	8.12%	28.26%
IPC (Mexico)	7437.72	1.76%	18.94%
IPSA (Chile)	1343.39	5.04%	30.40%
Straits Times (Singapore)	1600.02	3.28%	19.41%
Seoul Composite (South Korea)	753.00	7.12%	13.90%
ISE National-100 (Turkey)	11735.19	12.03%	8.28%
Morgan Stanley Emerging Markets Free Index	369.318	6.25%	26.39%

The Foreign Exchange Market. Throughout August, there were observed no significant fluctuations of US \$ against RUR, nevertheless, US \$ appreciated somewhat against RUR: the official US \$ exchange rate increased by 10 kopeks (0.34 per cent) from Rub. 30.26 to Rub. 30.36 per US \$. The total US \$ trading volume at the Electronic Batch Trade Session (EBTS) amounted to US \$ 5.88 billion. In the August 1 - 21 period, the maximum high US \$ trading volume was observed on August 13 (US \$ 456 million), the minimum made US \$ 263.1 million on August 18. On the whole, it shall be noted that the EBTS US \$ trading volumes significantly declined over the month, what may be in part explained by the seasonal factors.

Ruble liquidity in the banking sector declined this August following the trend registered in July: as on August 27, correspondent account balances of crediting organizations made Rub. 112.8 billion (Rub. 126.4 billion in July).

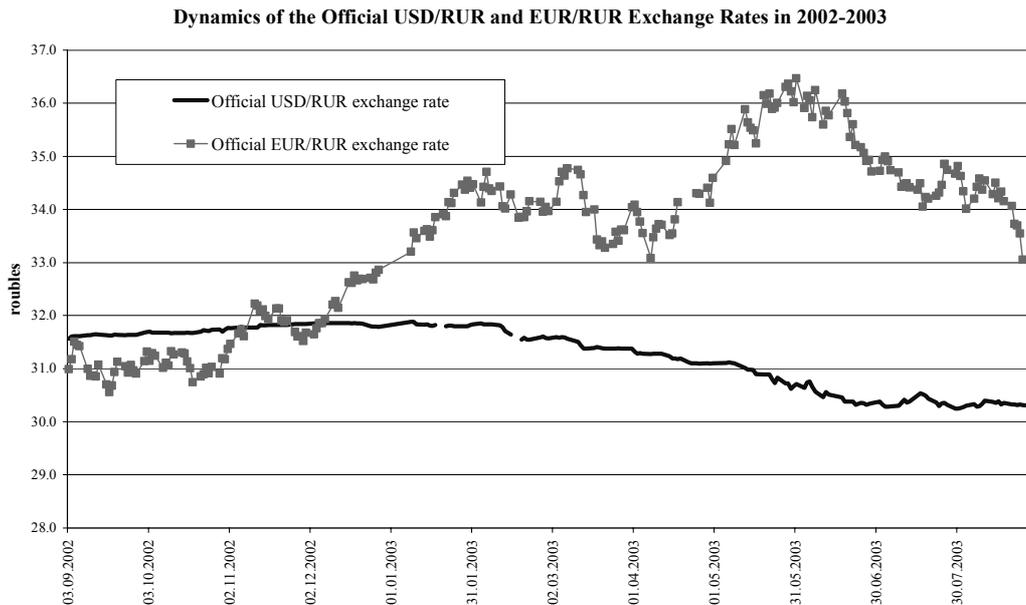


Fig. 7.

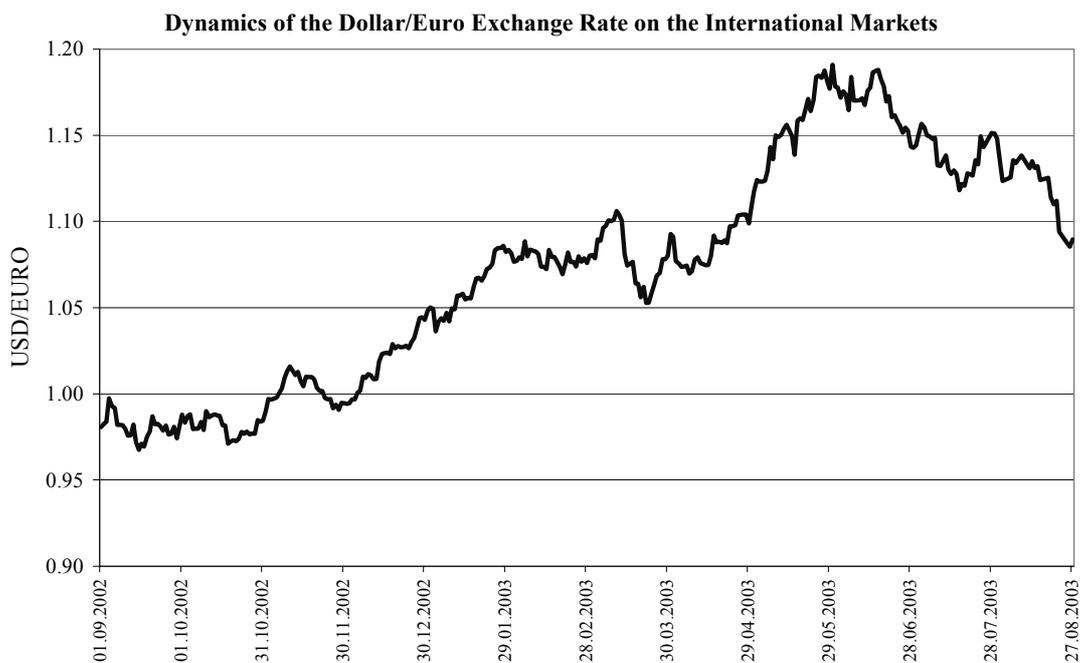


Fig. 8.

The US \$ / Euro exchange rate on the international market went down by 4.6 cents (- 4.1 per cent) to 1.089 US \$ / Euro. It shall be noted that the downward trend was observed throughout the whole month. The major factor behind the dynamics of the US \$ / Euro exchange rate remained the long term expectations of economic growth in the US economy exceeding growth rates in the EU economy.

Following the decline registered on international currency markets, in August there was registered a significant downfall of Euro to Ruble: Euro exchange rate fell by Rub. 1.67 (- 4.84 per cent) in July 31 through August 27 – from Rub. 34.63 per Euro to Rub. 32.95 per Euro. In the August 1 to August 22 period, the total Euro trading volume at the EBTS made Euro 108.69 million. In the above period, the maximum Euro trading volume was registered on August 12 at Euro 9.364 million, while the minimum volume was Euro 4.76 million (as on August 11).

Table 2.

Financial Markets Indicators

Month	April	May	June	July	August*
Monthly inflation	1,0%	0,8%	0,8%	0,7%	0,2%
Inflation rate for the year estimated on the basis of inflation rate in the month	12,68%	10,03%	10,03%	8,73%	2,43%
Rate of refinancing of the Central Bank of Russia	18%	18%	16%	16%	16%
Average yield to maturity on all issues of OFZ securities (% per annum)	8,03%	6,44%	5,31%	7,11%	6,5%
Volume of the GKO-OFZ securities market per month (billion rubles.)	20,83	20,68	40,12	17,08	12,5
Yield to maturity of OFZ securities as of the end of the month (% per annum):					
5 tranche	5,57%	4,78%	4,90%	5,90%	6,2%
6 tranche	4,18%	3,87%	3,79%	4,45%	4,6%
7 tranche	6,19%	5,40%	5,61%	6,42%	7,0%
8 tranche	4,78%	4,17%	4,20%	5,32%	5,7%
Yield to maturity of eurobonds as of the end of the month (% per annum):					
2003	3,22%	2,74%	2,74%	3,13%	3,4%
2005	4,68%	3,93%	3,97%	4,55%	4,9%
2007	5,85%	5,27%	5,37%	5,86%	6,2%
2010	7,20%	6,43%	6,35%	7,24%	7,5%
2018	7,78%	6,88%	6,91%	7,76%	7,9%
2028	7,94%	6,99%	7,13%	7,82%	8,0%
Inter-Bank Lending-MIACR rate (% per annum as of the end of the month) on overnight loans	3,46%	1,81%	3,17%	11,52%	8,18%
Official USD exchange rate as of the end of the month (RUR/USD)	31,1000	30,7090	30,3483	30,2596	30,5036
Official EURO exchange rate as of the end of the month (RUR/EURO)	34,1447	36,4669	34,7124	34,6291	33,2001
Gain of the official USD exchange rate in the month (%)	-0,89%	-1,26%	-1,17%	-0,29%	0,81%
Gain of the official EURO exchange rate in the month (%)	1,66%	6,80%	-4,81%	-0,24%	-4,13%
Stock market volume in RTS in the month (mil USD):	601,40	497,74	442,10	600,12	329,97
Value of the RTS-1 Index as of the end of the month	429,16	469,93	503,51	457,02	530,94
Change in the RTS-1 Index in the month (%)	18,00%	9,50%	7,15%	-9,23%	16,17%

* Estimation

D. Polevoi

The Real Sector: Factors and Trends

The macroeconomic situation is determined by persisting trends towards expansion of production across all sectors of the economy and industry. According to the preliminary estimates published by the Ministry of Economic Development, in the 2nd quarter of 2003 the increase in GDP made 7.4 per cent as compared with the figures registered in the respective period of the preceding year, while the output of base sectors of the economy increased by 7.8 per cent. The positive dynamics of the key economic indicators was determined by a favorable combination of internal and external factors. In the 2nd quarter of 2003, the amount of export proceeds increased, at the same time there grew the net inflow of capital from abroad. In the first six months of 2003, foreign investment in the Russia's economy made US \$ 12.7 billion, while Russian investment abroad amounted to US \$ 9.7 billion. Domestic and foreign investment in fixed assets increased at an outpacing rate in comparison with the GDP dynamics and the output of products and services of the base sectors of the economy. Investment in fixed assets increased by 11.9 per cent as compared with the figures registered in the respective period of the preceding year, including a growth by 51.3 per cent in foreign investment, while GDP increased by 7.2 per cent. In January through July of 2003, the amount of investment in fixed assets reached Rub. 985.4 billion and made 13.2 per cent of GDP.

The progressive trend towards an increase in investment in fixed assets, which had been forming since early 2003, was determined by the cumulative impact of a number of general economic factors and factors relating to changes in the business situation. The growth in proceeds of the economy as a result of the exceptionally favorable business situation on the world markets permits to support the profitability level of production and investment attractiveness of sectors and enterprises. In January through June of 2003, the balanced financial results of the economy at large increased 1.76 times as compared with the figures registered in the respective period of the preceding year. An increase in the balanced financial results were registered across all sectors of the economy. The highest rates of growth in the balanced profits were observed in foreign trade and communications. As concerns industry, there the profits made Rub. 316.9 billion, while fuel industries and the metallurgical complex accounted for more than a half of this amount. The persisting high profitability rates registered in the export oriented sector of the economy positively affect the rates of economic growth.

It shall be noted that in the first six months of 2003, GDP grew primarily at the expense of accelerating rates of development of construction, trade, transport, communications, and other market services. The role of industry in GDP growth has become somewhat less important. The increase in the industrial output in January through July of 2003 made 6.8 per cent, while the amount of construction works grew by 14.4 per cent, communication were up by 34.8 per cent, and trade grew by 8.7 per cent.

In January through July of 2003, industries of the fuel and energy complex made the most important contribution in the dynamics of industrial output. The increase of output of the fuel and energy complex made 8.6 per cent, including 9.9 per cent contributed by the fuel industry. Growing profitability of the export oriented sector of the economy had a positive impact on the recovery of production and enhancing effectiveness of related industries. The rates of growth registered in the industries producing raw materials made 6.2 per cent. Growth in ferrous metallurgy (109.4 per cent) and non-ferrous metallurgy (106.5 per cent) was the major factor behind the dynamics of production of intermediate products. Structural shifts in industry are determined by the outpacing rates of development of the raw materials complex. The development of the industries of the investment and consumer complexes primarily oriented towards the domestic market is characterized by more modest dynamics. In January through July of 2003, the rates of growth in manufacturing industries made 105.9 per cent (including: mechanical engineering and metal working – 107.5 per cent, food industry – 104.6 per cent) in comparison with the figures registered in the respective period of the preceding year, while the trend towards a decrease in output of light industry (by 1.0 per cent) persisted. It shall be noted that in June and July of 2003 the trend towards an increase in output of mechanical engineering became significantly less pronounced.

In the 2nd quarter of 2003, the positive quarterly dynamics of indicators characterizing household living standards recovered. In comparison with the figures registered in the 1st quarter of 2003, real household incomes increased by 10.0 per cent, real wages and salaries – by 7.0 per cent, and real gross pensions – by 4.8 per cent. The size of the population whose incomes were below the poverty line decreased by 6.5 million as compared with the figures observed in the 2nd quarter of 2002 and made 24.6 per cent of the total population as compared with 29.0 per cent registered in the respective period of the preceding year.

In July of 2003, cash household incomes totaled to Rub. 745.5 billion increasing by 27.0 per cent in comparison with the figures registered in July of 2002. The structure of cash household incomes was dominated by remuneration of labor (68.2 per cent) and the influence of this component has been increasing over the last 3 years. As concerns the employment structure, 92.1 per cent of the population are wage workers and only 7.9 per cent may be defined either as employers of wage laborers for work at their enterprises on the permanent basis, or self-employed persons. The share of proceeds from entrepreneurial activities and property remain at a level below the pre-crisis figures observed in 1998. in the 2nd quarter of 2003, the aggregate share of wages, salaries, and property related incomes increased by 1.9 percentage points as compared with the figures registered in the preceding period, while the share of entrepreneurship related incomes and social transfers decreased by 0.7 p. p. and 1.5 p. p. respectively.

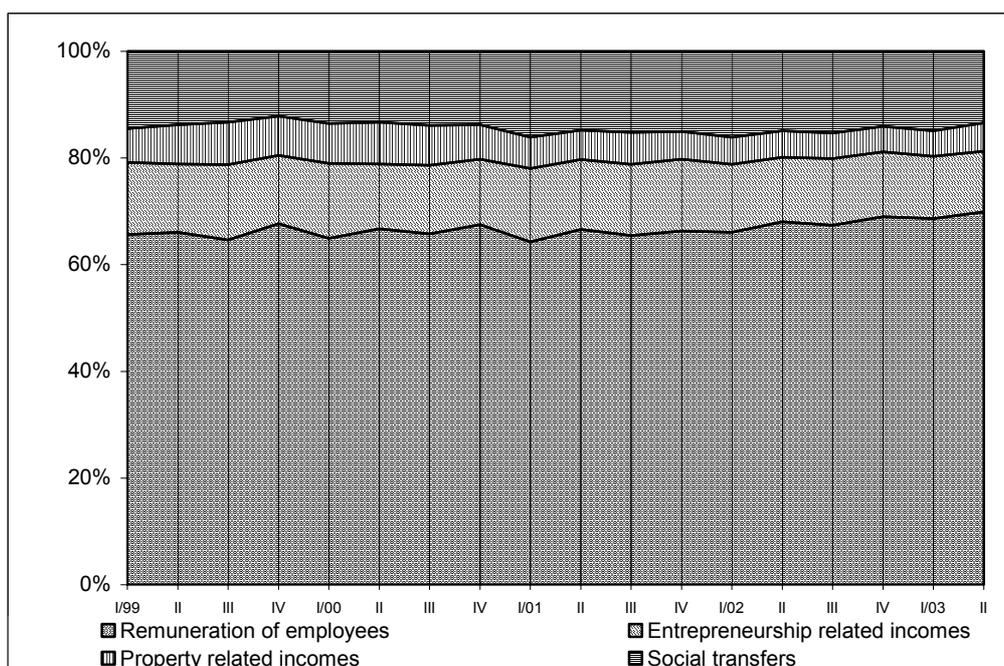


Fig. 1. Structure of cash household incomes as broken down by quarters in 1999 through 2003, in % of the total

A comparative analysis of distribution of the population as broken down by per capita incomes demonstrate that the share of households with incomes exceeding Rub. 3,000 has increased by almost 15 p. p. in comparison with the figures registered in the first six months of 2002. The favorable economic situation, positive dynamics of base macroeconomic indicators, and a considerable growth of household incomes positively affected the recovery on the market of consumer goods and paid services. Purchasing power of households has increased as concerns base products. In the 2nd quarter of 2003, the increase in retail trade turnover made 4.3 per cent as compared with the figures registered in the respective period of the preceding year. An analysis of the monthly dynamics reveals that this July the rates of growth of the market of consumer goods and services accelerated. The increase in turnover of retail trade made 2.7 per cent, while paid services grew by 3.1 per cent. In contradistinction to the figures registered in the preceding year, in 2003 there was observed a certain equalization of the rates of growth in the amount of paid services rendered to the population and the turnover of the retail trade in spite of the fact that the rates of increase in prices of and tariffs on paid services significantly outpaced prices of goods. In January through July of 2003, in comparison with the figures registered in the preceding period, the retail trade turnover increased by 8.7 per cent (in January through July of 2002 – 9.6 per cent) and the amount of paid services – by 5.1 per cent (0.9 per cent), while real household incomes grew by 14.4 per cent (7.8 per cent).

The trend towards outpacing rates of growth in disposable cash household incomes in comparison with the dynamics of the retail trade turnover persists at the background of changes taking place in the structure of household expenditures. As household incomes grow, the gap between rates of increase in expenditures for purchase of goods and savings. In January through July of 2003, the share of expenditures for purchase of

goods made 53.9 per cent of household incomes as compared with 57.7 per cent registered in the respective period of 2002, while the share of savings increased by 2 p. p.

It shall be noted that the principal difference between the situation observed in 2003 and last year is determined by the gradual equalization of the dynamics of wages and salaries as compared with the productivity of labor. According to the estimates published by the Ministry of Economic Development, in January through July the growth in labor productivity in industry made 112.1 per cent and outpaced the output dynamics by 5.3 p. p.

A growth in productivity of labor is registered across practically all industries and is accompanied by changes in the dynamics and structure of demand for labor. As concerns the fuel and energy, metallurgical, and chemistry and forestry complexes, there the outpacing rate of labor productivity in comparison with wages and salaries is supported at the expense of improving efficiency of labor. Exactly in these industries there was registered the most massive reduction of jobs as compared with the figures observed in the respective month of 2002.

In the economy at large, the total number of unemployed increased by 568 thousand in comparison with the figures registered in the first six months of 2002. The coefficient of tension (the number of unemployed citizens registered with employment agencies per vacancy) increased from 1.3 to 1.7. At the same time, while the general trend towards decrease in the number of jobs persists, the demand for skilled labor grows. The share of persons dismissed due to redundancy, liquidation of organizations or own businesses decreases at the background of the growing share of inexperienced and untrained persons. Enterprises pursue rather active policies aimed at the restructuring of employment and enhancing of efficiency of labor time utilization. As compared with the figures registered in the first six months of 2002, the number of part time employees (working only a part of the working week or working day) decreased by 20 per cent, at the same time, the number of workers on mandatory administrative leaves declined by 360 thousand, or 26 per cent. The formation of this trend is extremely important for further economic growth.

O. Izryadnova

IET Business Survey: Industry

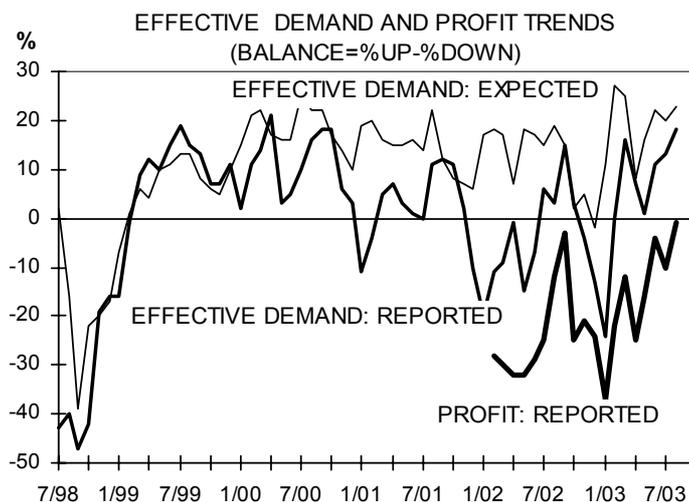
The official statistical data on the July dynamics of industrial output published by Goskomstat in the second half of August indicate that the recovery trend in the Russia's industry persists. The index of industrial output made 107.5 per cent as compared with the level registered in June (100.5 per cent as adjusted for exclusion of the labor time fund). According to the evaluations of the Center for Macroeconomic Analysis and Short Term Prognostication (CMASTP), the intensity of growth even increased somewhat in comparison with the figures registered in the 2nd quarter of 2003 as the average daily output in July grew by 0.7 per cent as compared with 0.5 per cent on the average in April through June. The major contribution to the increase in industrial output was made by raw materials industries. Fuel industry, chemistry and petrochemistry, as well as non-ferrous metallurgy accounted for about 2/3 of the total increase in output. As concerns mechanical engineering, light and food industries, the intensity of growth in these industries significantly decreased in July. These industries contributed only about 1/4 of the national industrial output growth in July.

On the whole, the positive results registered in the first seven months of 2003 may be undermined by less bright prospects for the end of the year. This conclusion is contained in the consensus forecast elaborated by the Development Center basing on the estimates presented by about 30 analytical centers. According to these experts, the economy would not be able to reach a GDP growth even close to that registered in January through July (7.2 per cent). As a result, by the end of the year this indicator would make only 5.8 per cent. The next year, the situation will be even worse: the GDP growth should make only 4.6 per cent. The experts state that the reason of the slowdown in the economy is that "the unique combination of external and internal factors" causing the economic boom in Russia in the first six months of 2003 will not occur again. Indeed, this situation was unique, mainly because of the fact that an anomaly high price of oil, a staple Russia's export item, was observed over many months.

However, the first results of the eighth month do not provide grounds for pessimistic moods. The August business survey registered not only an increase in the rates of growth in effective demand and output, but also increasing optimism of enterprises. As a result, the summary Russian industrial confidence index calculated by IET in accordance with the adjusted European methods has reached the record highs in 2001 through 2003.



The rates of growth in cash sales of industrial products increased by 5 balance points in August reaching the maximal value in the last 34 months. Sales have not grown so intensively since October of 2000. An increase in demand was registered across all industries with the exception of non-ferrous metallurgy and the forestry complex. The highest results were observed in chemistry and petrochemistry. As a result, evaluations of the amounts of sales also improved. About 52 per cent of enterprises already assess these amounts as normal (a 12 p.p. increase over the last 3 months). Such evaluations prevail in metallurgy (90 per cent), chemistry, petrochemistry, and construction industry (70 per cent), and light industry (60 per cent).



The intensity of output increases following the growth in demand. The rate of growth in output made 33 per cent (in terms of the balance), what is the record high over the last 40 months. Output increases across all Russia's industries with the exception of power engineering, where there was registered a moderate decline as compared with the figures observed in the summer months. Most intensively output grew in chemistry, petrochemistry, metallurgy, and mechanical engineering.

In spite of rather high rates of growth in output, no increase in finished stocks was registered in the industry. Moreover, in July through August the balance of evaluations (above norm – below norm) decreased by 8 points and is at present at the lowest level over the last 9 months (considerable excessive stocks were registered only in chemistry and petrochemistry). At the same time, the share of normal assessments of finished stocks remains at the absolute maximum. In other words, enterprises better control the ratio between demand and supply and do not expect deterioration of sales in a few next months.

The dynamics of real profits also indicates that the situation in industry improves. The balance of change in this indicator became almost zero after rather high negative values demonstrated in the first six months of the year. I.e., the decrease of real profits in industry has practically stopped. A certain growth was registered in ferrous metallurgy, light industry, and mechanical engineering.

To the contrary, the investment activity of enterprises abated. In the 3rd quarter, the balance of purchases of domestically produced machinery and equipment was at zero after a moderate growth registered in the

preceding month. An increase in purchases was observed only in power engineering, metallurgy, and construction industry. Purchases of imported equipment continue to fall with the previous minimal intensity.

The balance of estimates of changes in effective demand increased by several balance points in August. A growth in sales in a few next months is expected across all industries with the exception of construction industry. The most optimistic expectations were observed in power engineering, food industry, and mechanical engineering.

The plans of changes in output gather in optimism. In August, the balance in the industry at large increased by another 4 points and demonstrated the record high over the last 19 months. A decrease in optimism was registered only in non-ferrous metallurgy, construction materials industry, and food industry.

The forecasts of changes in real profits have retained positive values since May as enterprises hoping for a growth in this indicator prevail across industries. In August the balance was registered at + 20 per cent. Only forestry complex and industry of construction materials forecast a decrease in profits.

In the 3rd quarter, the forecasts of purchases of machinery and equipment came to zero as the share of enterprises intending to increase such purchases became equal to the share of enterprises planning to decrease purchases. In the 1st and 2nd quarters, the industry had more plans to increase purchases of both imported and domestically manufactured equipment. A growth in purchases of domestically produced equipment is probable only in the forestry complex, while food industry may account for an increase in purchases of imported equipment.

S. Tsukhlo

Regions: Dynamics of Industrial Output

The scope of interregional differences relating to the dynamics of industrial output observed in the first six months of 2003 remained at the practically same level as in the 1st quarter of this year. While the average national growth in industrial output in the first six months of 2003 made 6.8 per cent (as compared with the figures registered in the first six months of 2002), this indicator varied across individual regions from a growth by 37.5 per cent (in the Nenets AO) to a decline by 31.5 per cent (in the Koryak AO). At the same time, as compared with the figures registered in the 1st quarter, the number of RF subjects where there was observed a decline in industrial output has significantly diminished. While in the 1st quarter there were registered 21 such regions, in the first six months their number made 13. Beside the RF subjects indicated in Table 1, the amount of industrial output, as compared with the figures registered in the respective period of the preceding year, decreased in yet 6 autonomous okrugs – Komi Permyak, Taimyr, Ust Orda, Buryat, Aginsk Buryat, Koryak, and Chukotka okrugs (in all aforementioned autonomous okrugs, with the exception of the Koryak AO, a decline in industrial output was also registered by the end of the 1st quarter of this year).

The Republics of Komi and Yakutia, the Stavropol and Primorski kraises, the Murmansk, Novgorod, Rostov, and Ulyanovsk oblasts, and the Evenk AO were removed from the list of regions demonstrating a decline in industrial output as compared with the data registered in the 1st quarter of this year. In all these regions, the index of industrial output was below 103 per cent, with the exception of the Ulyanovsk oblast, which became a leader as concerns the rates of growth in industrial output. The amount of production of cars in this region was still below the figures registered in the preceding year (by 3.6 per cent); however, the rates of decline in the industry have sharply decelerated (in the 1st quarter of this year, the amount of production of cars was by 17.4 per cent below the indicator observed in the 1st quarter of the preceding year). At the same time, the production of trucks and buses in the Ulyanovsk oblast increased by 26.9 per cent and 16.1 per cent respectively in the first six months of 2003 as compared with the figures registered in the first six months of 2002. As concerns the Samara oblast, there the rates of decline in output of the motor industry decelerated much less (from 21.8 per cent in the 1st quarter to 12.2 per cent in the first six months of this year as compared with the figures registered in the respective periods of the preceding year), and this RF subject remains among outsiders as concerns the dynamics of industrial output (the national average decline in production of cars made 19.1 per cent in the 1st quarter and 9.9 per cent in the first six months of this year).

The only RF subject where industrial growth was reversed was the Khabarovsk krai. This region has a diversified structure of the economy, where the sectoral structure of industry is dominated by mechanical engineering and metal working (almost half of the amount of the regional industrial output according to the 2002 data), including the defense related industries. The Kamchatka oblast has lost its leading position as concerns the rates of growth in industrial output (the amount of industrial output in the region increased by 5.5 per cent, while in the 1st quarter it made almost 40 per cent). However, the favorable situation still exists

in the regional fish industry – fish and sea products catches have increased in comparison with the figures registered last year by 31.6 per cent (while on the national level there was observed a 6 per cent decline). The overall indicator of growth in the Kamchatka oblast was affected by the negative situation in other industries, including certain sub-industries pertaining to food industry and power engineering, which is the second (after the food industry) most important industry in the region.

In the first six months of 2003, similarly to the situation observed in the 1st quarter, among the leaders as concerns the rates of growth in industrial output there were regions where raw materials industries played a more important role (most often this role was played by fuel industry, as, for instance, in the Arkhangelsk oblast, the data on which, for reporting purposes, include oil extraction volumes of the Nenets AO, the Orenburg oblast, Kalmykia); however, the RF subjects with industries oriented towards the domestic market prevail (among the leaders are the cities of Moscow and St. Petersburg and their respective oblasts).

Table 1

Regions demonstrating the most and least favorable industrial output dynamics in the first six months of 2003*

Regions demonstrating most significant rates of growth in industrial output	IOI, first six months of 2003 in % of first six months of 2002	Regions demonstrating a decline in industrial output	IOI, first six months of 2003 in % of first six months of 2002
City of St. Petersburg	126,2	Republic of Karelia	99,7
Republic of Buryatia	121,4	Kirov oblast	99,3
Kursk oblast	121,0	Tula oblast	96,7
Leningrad oblast	120,9	Samara oblast	96,7
Republic of Mordovia	118,8	Republic of Altai	95,6
Orenburg oblast	118,2	Khabarovsk krai	93,4
Arkhangelsk oblast	117,8	Magadan oblast	77,0
Moscow oblast	117,1	Republic of Ingushetia	72,1
City of Moscow	117,0		
Chita oblast	116,9		
Tomsk oblast	116,3		
Kaliningrad oblast	114,4		
Ulyanovsk oblast	113,6		
Republic of Kalmykia	112,8		

* without autonomous okrugs

IOI – industrial output index

The shares of regions in the first six months of 2002 and 2003 were similar (see Table 2). The most significant change is the growth in the share of regions specializing in ferrous metallurgy, especially as concerns the Volgograd oblast. There also increased the share of the Chelyabinsk oblast, somewhat grew the share of the Sverdlovsk oblast and the Lipetsk oblast, which was up from the 23rd place (1st half year of 2002) to the 16th place (1st half year of 2003) in terms of their share in the national amount of industrial output (in the Sverdlovsk oblast, ferrous metallurgy accounts for about ¼ of the total industrial output, in three other regions this indicator makes more than half of the total industrial output).

As concerns federal okrugs, the indicators of the dynamics of industrial output in the first six months of this year significantly differ from the indicators registered in the 1st quarter. First, it shall be noted that the Central and North West federal okrugs characterized by the most favorable economic and geographical positions were included in the list of leaders in terms of rates of growth in industrial output (see Table 3), while the Ural federal okrug is ranking only third (in spite of the fact that in the first six months of the year the maximal rates of growth were again registered in fuel industry, which accounts for more than a half of the total industrial production manufactured in the Ural federal okrug). The rates of growth registered in the “central” federal okrugs of Russia – aforementioned Ural okrug, as well as the South and Privolzhski federal okrugs – remained at practically the same level as in the 1st quarter of 2003. The situation in the eastern part of the country – the Siberian and Far East federal okrugs has noticeably deteriorated. This situation

characterized by more rapid rates of growth observed in the Center and North West and lagging behind eastern provinces is much similar to that registered last year.

Table 2

Regions leading in terms of their share in the national volume of industrial output in the first six months of 2002 and 2003*

Regions	Share in industrial output, first six months of 2003, in %	Regions	Share in industrial output, first six months of 2003, in %
Tyumen obalst	11,26	Tyumen obalst	11,33
City of Moscow	5,51	City of Moscow	6,18
Sverdlovsk oblast	4,51	Sverdlovsk oblast	4,40
Moscow oblast	4,09	Samara oblast	4,39
Samara oblast	3,97	Moscow oblast	4,14
Chelyabinsk oblast	3,74	Republic of Tatarstan	3,76
City of St. Petersburg	3,73	Krasnoyarsk krai	3,44
Republic of Tatarstan	3,43	City of St. Petersburg	3,39
Krasnoyarsk krai	3,30	Chelyabinsk oblast	3,21
Republic of Bashkortostan	2,86	Republic of Bashkortostan	2,84
<i>Total top 10</i>	<i>46,40</i>	<i>Total top 10</i>	<i>47,07</i>
Kemerovo oblast	2,75	Nizhni Novgorod oblast	2,54
Perm oblast	2,59	Perm oblast	2,50
Nizhni Novgorod oblast	2,42	Kemerovo oblast	2,45
Vologda oblast	2,01	Irkutsk oblast	2,12
Irkutsk oblast	1,98	Vologda oblast	1,74
<i>Total top 15</i>	<i>58,16</i>	<i>Total top 15</i>	<i>58,41</i>

* without autonomous okrugs

The decrease in the share of Far East in the national industrial output was also clearly perceptible. While in all other federal okrugs the growth in amounts of industrial output (not adjusted for price dynamics) fluctuated from 20.1 per cent to 31.0 per cent (the maximal growth was registered in the North West okrug), in the Far East federal okrug the amount of industrial output increased by just 14.2 per cent (in the first six months of 2003 as compared with the figures registered in the respective period of 2002).

Table 3

Characteristics of industrial output across federal okrugs

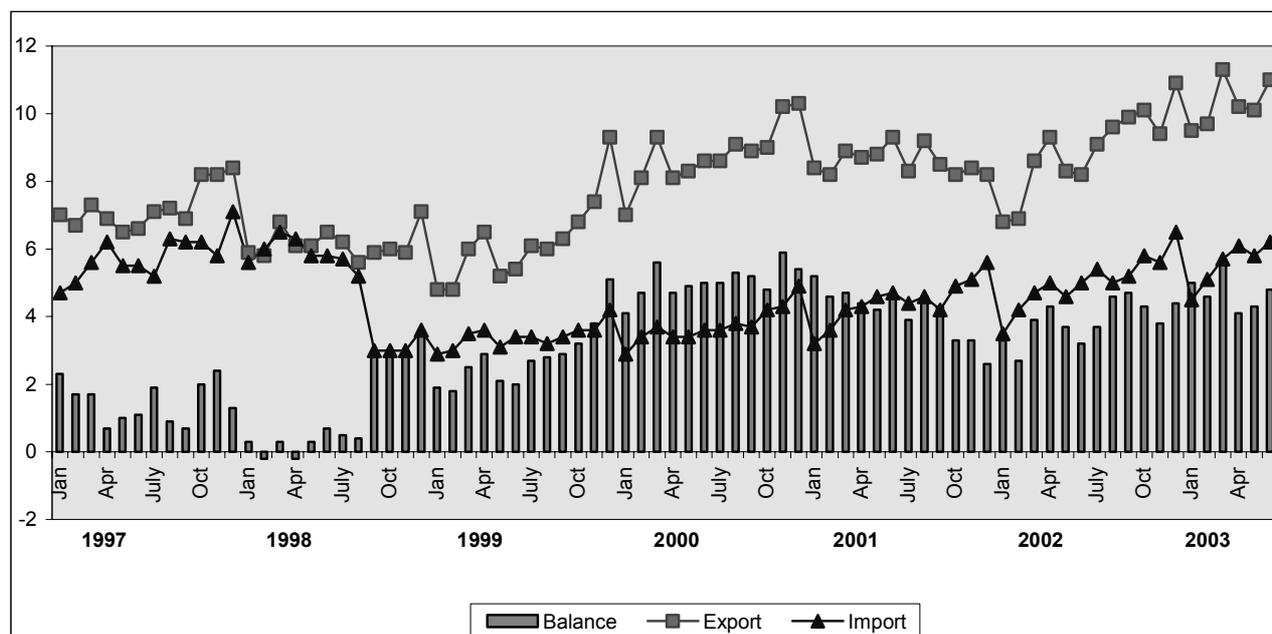
Federal okrugs	IOI, first six months of 2003 in % of first six months of 2002	Share in the national industrial output (in %)	
		first six months of 2003	first six months of 2002
Central federal okrug	112,0	22,27	22,29
North West federal okrug	114,4	12,16	11,56
Southern federal okrug	103,9	6,36	6,60
Privolzhski federal okrug	105,7	22,20	22,86
Ural federal okrug	109,9	19,81	19,26
Siberian federal okrug	107,6	12,36	12,17
Far East federal okrug	101,6	4,83	5,27
Russian Federation	106,8	100,00	100,00

O. Kuznetsova

Foreign Trade

In June of 2003, the Russia's foreign trade turnover reached the record high since the beginning of the year – US \$ 17.2 billion, what was by 30.3 per cent above the respective level registered in 2002. At the same time, the trend towards outpacing rates of growth in exports persisted, in comparison with the figures registered last June, exports grew by 33.6 per cent. The rates of growth in imports remained rather high and

made 24.9 per cent. Due to the fact that exports grew at an outpacing rate in comparison with imports, the balance of trade remained at a rather high level making US \$ 4.8 billion.



Source: RF Goskomstat

Fig.1 Main indicators of Russia's foreign trade (in US \$ bln.)

The growth in exports was to a considerable extent determined by rising world prices of staple raw materials. In the first six months, the volumes of export increased only insignificantly as the world economic situation stagnated.

On the whole, the business situation on the international oil and oil products markets remained rather stable and favorable for exporters. In June of 2003, world oil prices were moderately high. For instance, the average URALS oil price made US \$ 25.6 per barrel (a 2.8 per cent increase in comparison with the May figures) while the BRENT oil prices were at US \$ 27.1 per barrel (a 6.7 per cent growth).

In May and June, the average URALS oil price made US \$ 24.8 per barrel, or US \$ 181.45 per metric ton. In March and April this indicator was at US \$ 25.4 per barrel. As a result, since August 1, 2003, the export duties on oil and oil products were reduced to US \$ 25.1 per metric ton and US \$ 22.6 per metric ton respectively.

The situation on the world markets of non-ferrous metals was on the whole favorable for exporters. For instance, in the first six months of 2003 the average monthly prices of nickel grew by 27.8 per cent, price of copper increased by 4 per cent, while aluminum prices grew by 1.7 per cent in comparison with the figures registered in the respective period of the preceding year. The growth in prices of staple metals was caused by increasing demand related to the necessity to replenish the stock of goods. In June, the average prices of nickel increased by 4.98 per cent, copper – by 1.1 per cent, and aluminum – by 0.9 per cent in comparison with the figures registered this May.

Table 1.

The average monthly world prices in June of the respective year

	1996	1997	1998	1999	2000	2001	2002	2003
Oil (Brent), USD / metric ton	130,7	133,1	100,7	116,4	214,1	197,6	179,5	197,0
Natural gas, USD / thous. m ³	-	76,3	77,1	84,2	151,6	132,3	116,2	210,4
Gasoline, USD / metric ton	157,3	157,6	128,3	173,4	346,5	292,9	273,9	306,4
Copper, USD / metric ton	2202	2543	1665	1552,1	1752,0	1615,3	1686,2	1703,2
Aluminum, USD / metric ton	1490	1575	1316	1327,3	1510,2	1467,7	1354,9	1410,2
Nickel, USD / metric ton	7153,8	7054,6	4540	5241	8384,3	6629,2	7110,0	8761,1

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

The increase in the total amount of imports was primarily due to the growing volumes of import, while purchasing prices continued to decline. High positive dynamics of imports were stimulated by a stable increase in final consumption and investment.

In August of 2003, the RF Government changed the procedure governing the rising of import customs duties. The item, according to which the decisions of the RF Government concerning changes in import customs duties should come into force not sooner than after 180 days after their official publication with the exception of cases where such changes resulted in reduction of duty rates, was excluded from the RF Government resolution No. 1347 of October 22, 1997, "Issues pertaining to customs and tariff policies." In other words, while prior to the introduction of this change decisions on changes in the rates of import customs duties had come into force only after at least 3 months since the official publication date, now the terms of new duties shall be set forth for each type of goods.

This amendment permits to more actively use customs duties for protection of the domestic market from imported food products. Earlier, the resolution regulating terms of new duties was amended many times, however, the amendments primarily concerned foodstuffs. Only this year there were introduced exemptions concerning import of yeast, rice, meats (the last amendment concerning meat imports was introduced in early July).

These developments allow to arrive to the conclusion that the changes in the procedure governing the rising of import customs duties will primarily concern exactly the regulation of import of food products, where the existing protective measures, for instance, setting of quotas, has already become insufficient. For instance, the quotas relating to meat imports, which were introduced in the beginning of the year, proved inefficient as they do not concern NIS countries, while, for instance, Ukraine is a leading supplier of red meats to Russia.

According to the estimates provided by the Ministry of Agriculture, at present the customs and tariff protection covers 11.45 per cent of the Russia's agricultural market, while the respective international standard is at 62 per cent. The Russian Government intends to expand the list of protected foods. Thus, in the nearest future the Government shall discuss a resolution protecting domestic producers of rice, yeast, and soybeans. Besides, the Government discussed certain proposals concerning customs and tariff measures aimed at the limitation of grain, vegetable oil, milk, and milk products imports to Russia.

In this situation, the approval of the amendment concerning the terms of enactment of new customs duties may be viewed as a next step of the Government attempting to protect the domestic market from imported food products. This resolution will enable the Government more flexibly react to changes in the business situation on the world food markets, what was earlier impossible because of the longer terms of enactment of new customs duties.

In June of 2003, the amount of Russia's trade vis-à-vis CIS member countries made US \$ 2.93 billion. Russia still maintains an active balance of trade at US \$ 0.49 billion, at the same time, exports made US \$ 1.71 billion growing by 37.3 per cent as compared with the figures registered in the respective period of the preceding year, while imports grew by only 22.7 per cent in comparison with the figures registered last June.

In August, the RF Government approved the draft agreement concerning the creation of the common economic space (CES) including Russia, Belorussia, Kazakhstan, and Ukraine. Yet on February 23, in Moscow, the heads of these countries signed a statement concerning the creation of a new organization of regional integration. These countries account for 90 per cent of the total CIS GDP, about 90 per cent of mutual trade, and almost 80 per cent of the total CIS population. For the first time it is planned to set forth a supranational body to take decisions in the sphere of foreign trade regulation and tariffs. For Russia, the issue of utmost importance is the participation of Ukraine, as there are many disagreements with this country concerning trade policies, for instance, Ukrainian exports of pipes and sugar.

At the first stage, it is envisaged to harmonize customs tariff rates related to products imported by the participating countries, with the only exception being agricultural produce. A necessary condition should be unification of respective legislations in this sphere. The second stage poses even more difficult tasks, as at this stage there should be formed a customs union with common tariffs, what excludes protective and antidumping measures. At the third stage, there should be ensured free cross border movement of goods, services, labor, and capitals, and, probably, introduction of a common currency.

In the case all countries approve the draft agreement, there should begin work on elaboration of documents regulating concrete spheres of cooperation.

N. Volovik N. Leonova

