

**RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
SEPTEMBER 2001**

MONTHLY BULLETIN

**Moscow
2001**

The economy and politics in September 2001	3
The state of the federal budget	3
Monetary Policy	6
Financial Markets	8
The Russian banks on the market for government bonds denominated in foreign exchange (OVVZ)	17
Investment in the real sector.....	20
Foreign Investment in Russian economy	22
The real sector: factors and trends.....	24
IET Monthly Trends Survey: September 2001	27
The oil and gas sector	28
Russian Agrifood Sector in 6 months 2001.....	31
Foreign trade.....	36

The economy and politics in September 2001

Russia's economic and political life in September was full of events that may have a substantial effect on the country's further development.

The parameters and the structure of the national economy in the short run will find themselves under a great impact of the 2002 federal budget law, the draft of which currently is under consideration of the State Duma, and the renewal of the Single Tariff Agency (STA).

Obviously, the rise of tension in the world in the wake of terrorists' attack on the US and the envisaged strike back should not be painless for the Russian economy as well. However the impact of these factors is ambiguous both from the viewpoint of prospects for maintenance of the consistently liberal vector of the governmental economic policy and in view of investment attractiveness of the Russian economy.

A long-lasting downfall in oil prices in medium run forecasted by some analysts is pregnant with difficulties in regard to the execution of the planned indices of the draft 2002 federal budget and possible deterioration of the situation with repaying the external debt. Such a danger becomes especially evident against the background of

contraction in budget revenues due to the worsening economic situation worldwide and growth in the defense expenditure. At the same time, in the short run such a fall in budget revenues may be compensated with utilization of a substantial amount of balances on budget recipients' accounts, which should preclude from arise in domestic prices and deterioration of the financial situation by the end of the year.

The envisaged long recession of the US economy and the world economy on the whole, along with a sharp leap of investment risks may increasingly undermine investors' confidence in emerging markets. At the same time the current political and economic situation (with internal political stability, budget profit back-upped by the ongoing economic growth, liberalization of tax and financial law, adoption of the Land Code as its key characteristics) allows estimate Russia's position as relatively favorable. With other conditions being equal, Russia's course towards supporting the US also increases Russia's investment attractiveness to the West, including international financial institutions.

T. Drobyshevskaya

The state of the federal budget

TABLE 1. THE MONTHLY EXECUTION OF THE FEDERAL BUDGET OF THE RUSSIAN FEDERATION (IN COMPARABLE PRICES)

	III '00	VII'00	00	I'01	II'01	III'01	IV'01	V'01	VI'01	VII'01
Revenues										
Corporate profit tax	2,0%	2,4%	2,6%	1,4%	1,5%	1,9%	2,4%	2,6%	2,5%	2,5%
Personal income tax	0,3%	0,4%	0,4%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
VAT, special tax and excises	8,0%	8,0%	7,3%	9,1%	9,4%	9,0%	9,2%	9,3%	9,2%	9,0%
Tax on foreign trade and foreign trade operations	3,5%	3,4%	3,3%	3,6%	4,2%	4,1%	4,0%	3,9%	3,9%	3,9%
Other taxes, duties and payments	0,3%	0,3%	0,4%	1,1%	0,9%	0,8%	0,8%	0,7%	0,7%	0,7%
Total- taxes and charges	14,1%	14,6%	13,9%	15,3%	16,0%	15,8%	16,3%	16,6%	16,3%	16,2%
Non- tax revenues	1,8%	2,1%	2,3%	1,0%	1,2%	1,1%	1,2%	1,2%	1,3%	1,3%
Revenues, total	16,0%	16,7%	16,2%	16,0%	17,1%	16,9%	17,5%	17,8%	17,6%	17,5%
Expenditure										
Public administration	0,3%	0,3%	0,4%	0,1%	0,2%	0,3%	0,4%	0,4%	0,4%	0,4%
National defense	3,0%	2,6%	2,7%	1,3%	2,0%	2,2%	2,5%	2,7%	2,6%	2,6%
International activities	0,8%	0,2%	0,3%	0,3%	0,3%	0,2%	0,2%	0,2%	0,2%	0,2%
Judicial power	0,1%	0,1%	0,1%	0,0%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%
Law enforcement and security activities	1,3%	1,4%	1,5%	0,7%	1,1%	1,3%	1,4%	1,4%	1,4%	1,4%

**TABLE 1. THE MONTHLY EXECUTION OF THE FEDERAL BUDGET OF THE RUSSIAN FEDERATION
(IN COMPARABLE PRICES)**

Fundamental research	0,1%	0,2%	0,3%	0,0%	0,1%	0,2%	0,2%	0,2%	0,2%	0,2%
Services provided for the national economy	0,5%	0,6%	0,9%	0,1%	0,3%	0,6%	0,7%	0,8%	0,9%	1,0%
Social services	1,8%	1,9%	1,9%	1,2%	1,7%	1,9%	2,1%	2,0%	2,1%	2,1%
Servicing of public debt	2,9%	3,0%	2,5%	3,2%	5,6%	4,7%	3,7%	3,4%	3,1%	2,9%
Other expenditure	3,0%	2,9%	3,1%	3,3%	3,2%	2,9%	3,0%	3,1%	3,2%	3,1%
Expenditure, total	13,8%	13,3%	13,7%	10,4%	14,6%	14,3%	14,2%	14,2%	14,3%	14,0%
Loans, redemption exclusive	2,2%	3,4%	2,5%	5,8%	2,5%	2,6%	3,4%	3,7%	3,3%	3,5%
Expenditure and loans, redemption exclusive	-0,3%	-0,6%	0,0%	-3,7%	-0,8%	-0,6%	-1,1%	-1,7%	-1,3%	-1,1%
Budget deficit (-)	-1,9%	-2,9%	-2,5%	-2,1%	-1,7%	-2,1%	-2,3%	-2,0%	-2,0%	-2,4%
Domestic financing	-2,2%	-3,4%	-2,5%	-5,7%	-2,5%	-2,6%	-3,4%	-3,7%	-3,3%	-3,5%

**TABLE 2. THE MONTHLY EXECUTION OF THE FEDERAL BUDGET OF THE RUSSIAN FEDERATION
(IN % GDP, ACTUAL FINANCING)**

	I'01	II'01	III'01	IV'01	V'01	VI'01	VII'01	VIII'01
Total	16,0%	16,7%	16,8%	17,4%	17,7%	17,6%	17,5%	17,4%
Public administration	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%
National defense	2,4%	2,5%	2,8%	2,8%	2,8%	2,9%	2,8%	2,9%
International activities	0,5%	0,4%	0,2%	0,2%	0,2%	0,2%	0,3%	0,2%
Judicial power	0,2%	0,2%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%
Law enforcement and security activities	1,7%	1,9%	1,9%	1,8%	1,8%	1,8%	1,7%	1,7%
Fundamental research	0,3%	0,3%	0,3%	0,3%	0,3%	0,3%	0,3%	0,3%
Services provided for the national economy	0,5%	0,9%	1,0%	1,0%	1,1%	1,3%	1,2%	1,3%
Social services	2,4%	2,6%	2,5%	2,7%	2,5%	2,6%	2,5%	2,5%
Servicing of public debt	3,2%	5,5%	4,7%	4,3%	3,9%	3,1%	2,9%	3,2%
Other expenditure	3,7%	3,4%	3,1%	2,5%	2,7%	3,3%	3,2%	3,2%
Total expenditure	15,1%	18,1%	17,1%	16,3%	16,0%	16,0%	15,5%	15,9%
Profit (+) / deficit (-)	0,9%	-1,4%	-0,3%	1,1%	1,6%	1,6%	2,0%	1,5%

The data on the execution of the federal budget over the seven months of 2001 is given in Table 1¹. As of August 1, the revenues to the federal budget 2001 accounted for 17.5% of GDP, including tax revenues – 16.2%, while expenditure made up 14.0% of GDP (15.7% of GDP in terms of fulfilled funding), including non-interest ones 11.1% of GDP (12.7% in terms of fulfilled financing). The level of budget profit accounted for 3.5% of GDP (1.9% of GDP in terms of fulfilled funding).

Between January through July 2001 the execution of the federal budget was characterized with the 1.6 per cent points excess of the level of tax revenues over the respective index of 2000, which again can be attributed to the rise in collection of indirect taxes, primarily VAT and excises (at 1 p.p.), and taxes on foreign trade (0.5 p.p.).

The execution of the expenditure part of the federal budget between January through July in terms of fulfilled financing accounted for 14.0%, while in cash execution equivalent- 15.7% of GDP. That testified to some lowering of the expenditure level (roughly at 0.3 p.p.) compared to the average annual index. Such a lowering can be attributed to seasonality, and last year there was an analogous lowering of expenditure.

The estimate of the execution of the expenditure part of the federal budget over the period concerned varies due to the methodology of the accounting of operations- whether it is calculated in terms of fulfilled funding or cash execution. In the former case the volume of expenditure accounted for 14.2% of GDP, while in the latter- 16.1% of GDP.

The comparison of the federal budget execution indices over the first seven months 2001 with the analogous indices of the prior year allows noting the following changes: whilst the spending on

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

servicing the public debt during the seven months of 2001 was roughly equal to the respective index of 2000 (2.9% of GDP and 3.0% of GDP, respectively), during the former period the government has succeeded to repay as much as Rb. 91 bln. of principal body of its external debt and interest payments on that totaled Rb. 116 bln., as well as 30 bln. Rb. –worth domestic debt and 24.5 bln. –worth interest payments on that. At the same time the expenditure on supporting the national industry branches nearly doubled when compared wit 2000 (from 0.6% of GDP to 1% of GDP).

The main difference between the cash execution of expenditure and the fulfilled funding falls under such outlays as “national defense” (0.2 p.p.), “law enforcement“ (0.3 p.p.), “ services to industry branches” (0.2 p.p.), and “the social sphere” (0.4 p.p.).

As of early August, the balances of accounts on accounting the federal budget funds (without regard to the funds accumulated on personal accounts of recipients of budget funds) dropped to Rb. 94 bln. . Overall, since early 2001 the aforementioned funds (including the moneys of the Road and Ecological Funds) grew by Rb. 13.8 bln.

TABLE 3. ACTUAL TAX REVENUES TO THE FEDERAL BUDGET, ACCORDING TO THE DATA OF THE MTC (IN PRICES OF JANUARY 1998).

1999											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
10067	11586	12281	12287	10524	11369	12785	12838	12514	14238	16190	21455
2000											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
15030	16161	18247	20714	23469	18817	18219	18762	17422	18232	20306	25579
2001											
I	II	III	IV	V	VI	VII					
20580	19978	22917	26959	25311	23491	23342					

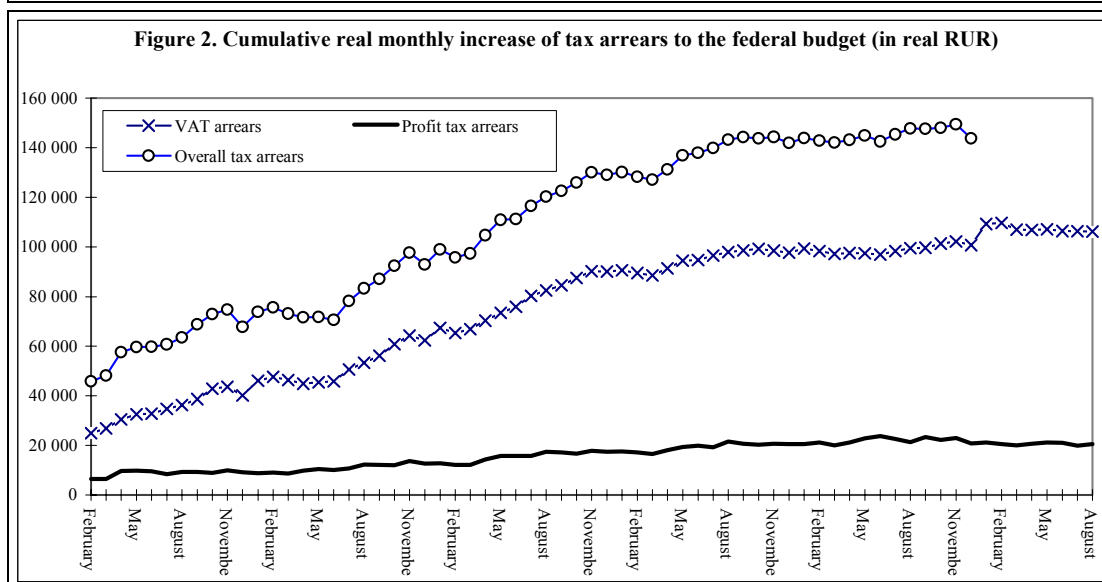
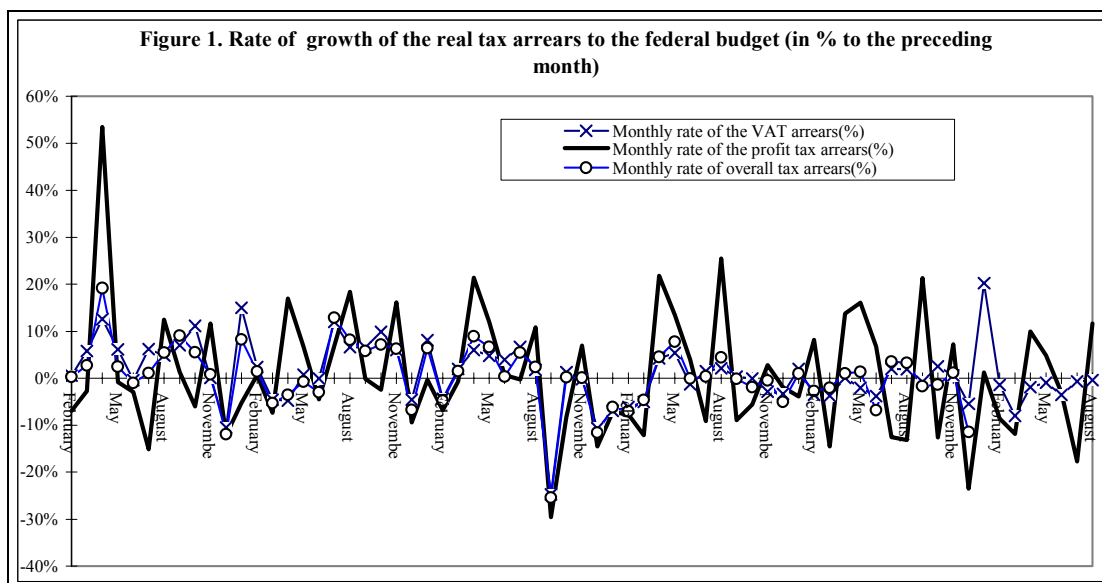
The dynamics of actual tax debts to the federal budget is given in Fig. 1. Since 2001 the form of the MTC’s presentation of the respective statistical

data has been changed, and the debts to the federal budget by all the taxes are no longer singled out.

The execution of the consolidated budget between 1998 through 2001 is represented in Table 4.

TABLE 4.

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					
Taxes	22,7%	23,6%	23,9%	25,4%	26,4%	26,0%	25,7%					
Revenues	25,9%	27,1%	27,4%	29,3%	30,5%	29,8%	29,5%					
Expenditures	16,8%	22,8%	23,7%	24,7%	25,1%	25,3%	25,2%					
Deficit	9,1%	4,2%	3,7%	4,7%	5,4%	4,4%	4,3%					



S. Batkibekov

Monetary Policy

In August 2001 the CPI growth rate fell to zero point. That occurred mainly due to seasonal factors, namely, the some 14.8% price fall for fruits and vegetables over the month. Thus, in August the increment of the food stuffs price index was negative and accounted for -1,0%. The prices for non-food goods rose by 0.8%, and for services – by 2.3%. It is worth noting that in August (for the first time this year) the growth in petroleum prices was noted (by 0.2%). The highest inflation rate was recorded in housing sector – the prices went up by 3.6% there.

In September the tendency to the decline in CPI growth rates still was in place (see Fig. 1), and inflation rate did not exceed 0.2–0.3%. Thus, the price growth for three quarters of 2001 turned to be

less than the one over the respective period of 2000 (13.6–13.7% against 14.1%)². However, in view of the forthcoming price rise for gas and rail transportation as well as discontinuance of seasonal factors' effect, we still forecast the annual inflation rate at 20–21%, i.e. at the level of 2000.

² In August, according to results of 8 months, the correlation was 12,6% to 13,4% в in favor of 2000.

FIGURE 1.

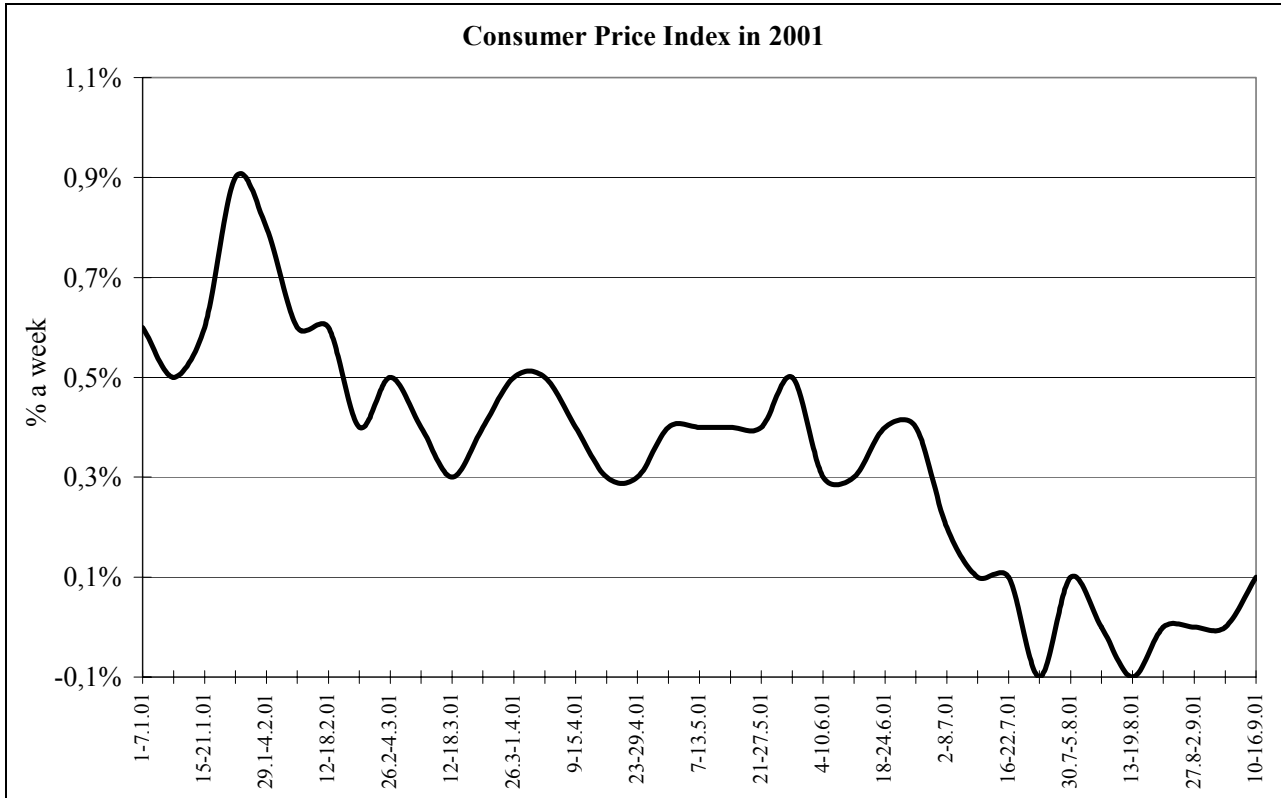
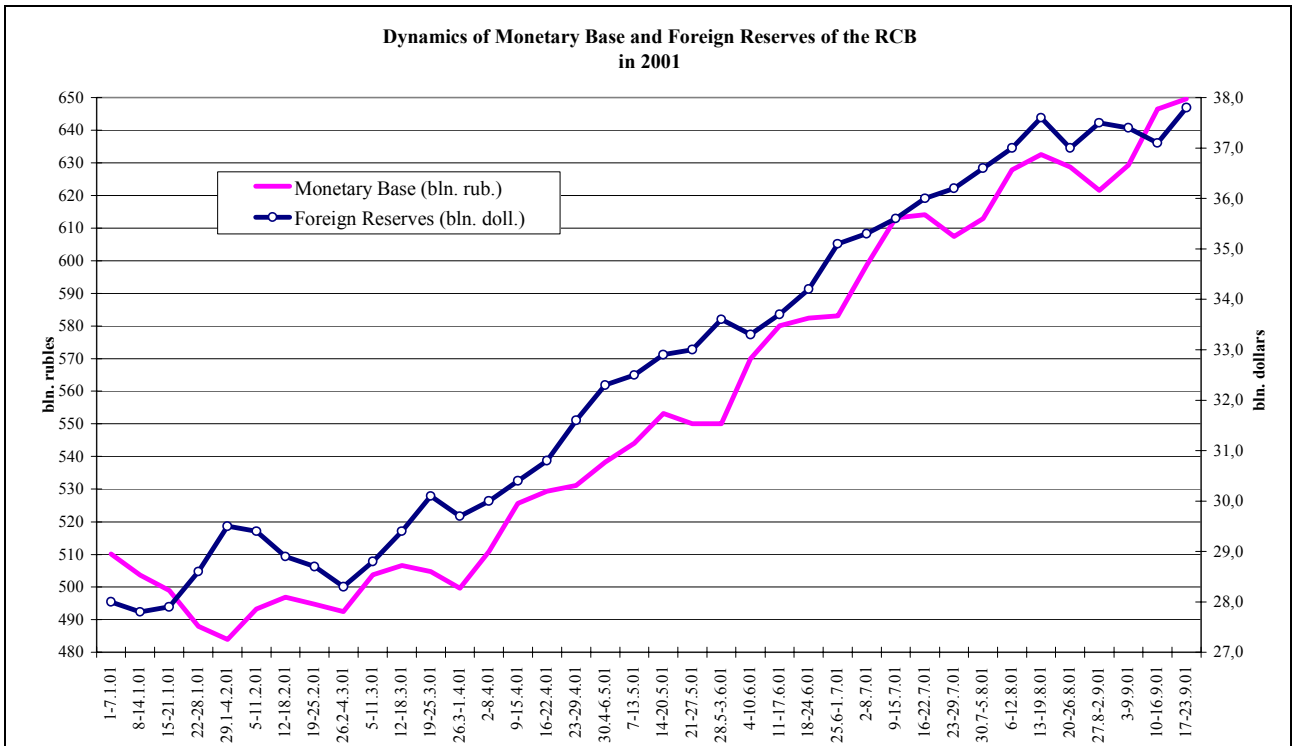


FIGURE 2.



As we predicted, the reduction in the compulsory export receipts sales rate did not affect the dynamics of foreign reserves (see Fig. 2). In particular, for the third week of September the

foreign reserves grew by \$700 million. However the total increase in foreign reserves of the Bank of Russia during three weeks of September was rather modest (about \$300 million). The external factors

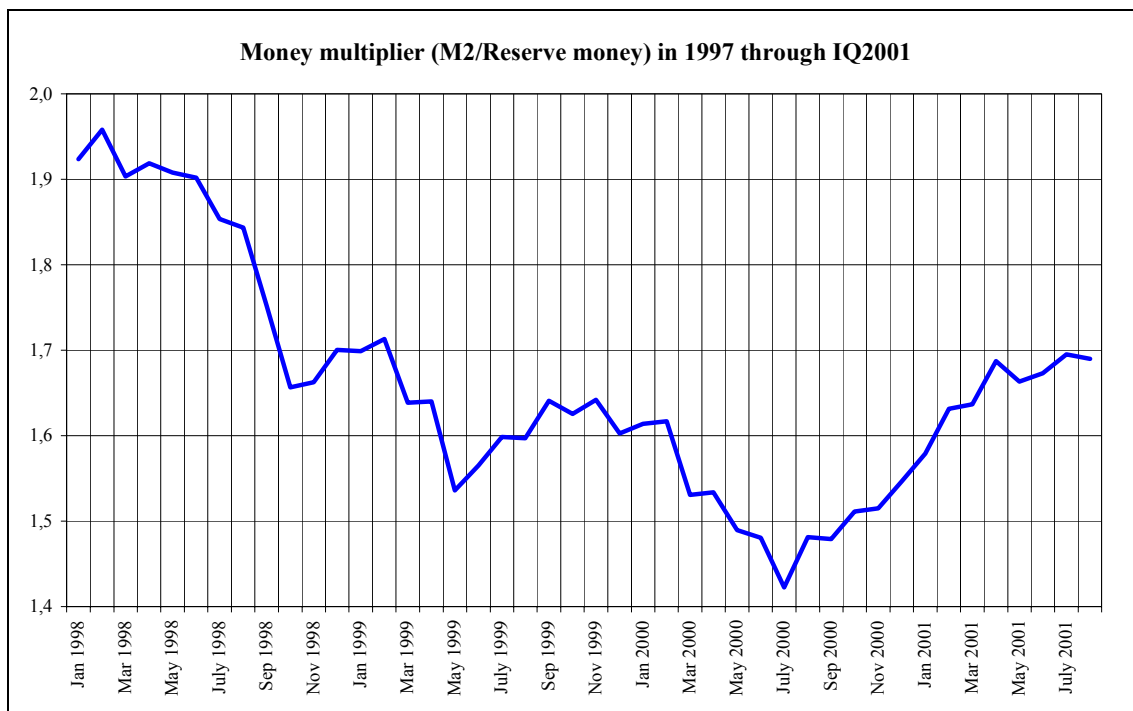
played their role: after the terrorist attacks against the US and turbulence in the world financial system the Bank of Russia was compelled to spend up to \$500 million to ensure liquidity in the market.

On September 6, 2001, the Bank of Russia held auctions to place two issues of the CBR bonds totalled up 4 billion roubles. However presently these securities have not enjoyed an actual demanded. Only some 21% of supplied bonds was placed at the average yield about 9.8% annualised.

In September 2001 the Bank of Russia published the data on dynamics of monetary aggregates over the eight months 2001. The money multiplier (M_2 to reserve money ratio) rose approximately by 10% vs. the beginning of the year (from 1.55 to 1.70) and by 19.5% as to its minimum (July 2000). The current level (about 1.7) corresponds to values noted between late-1998 – early-1999. Nevertheless, it is worth noting that during the last

half year (since April 2001) the multiplier actually discontinued its growth. In our view, this fact is related to a ‘maximum monetization level’, mentioned in our review in August (See *Russian Economy in August 2001. Trends and Outlooks*. M.: IET, 2001. Section *Monetary policy*.). At the same time the share of non-borrowed reserves of commercial banks in the reserve money continued to decline. Thus, in summer 2001 the balances on correspondent and deposit accounts of commercial banks with the Bank of Russia fell to 22–23% of the reserve money compared to 27.5–28.5% reported in the first and second quarters of 2001. The cash to compulsory reserves ratio remains stable (cash accounts for about 80% of the money base). Thus, despite growing crediting the economy, the credits to a great extent are still converted into cash (e.g., in wages and salaries), and multiplication chains in the Russian economy are short.

FIGURE 3.



S. Drobyshevsky.

Financial Markets

The government securities market

The development of prices for the Russian foreign debt securities in September 2001 could be divided into two periods, due to the acts of terrorism in the USA (see Figs. 1 and 2). During the first decade of September the quotations grew, supported by the increase of the Russia sovereign rating by Moody's from B3 to B2 (positive). By September 10 the

maximum yield on eurobonds dropped to 12.5% annualised. The minimum yield on the Minfin bonds was fixed on September 6 – from 11.9% to 14.6% annualised.

The shocks in the world financial system during the second week of the month (interruption in trades in the USA and in London, fall of many stock indices), as one could expect, had negative

impact, and prices for the Russian liabilities were going down until late-September. By the end of the month the yields on the Minfin bonds grew up to 13.5–16% annualised, and on eurobonds – up to 9–

13.25% annualised. The yield on eurobonds matured in late-November 2001 have found themselves within the range of 3.1–3,7% annualised.

FIGURE 1.

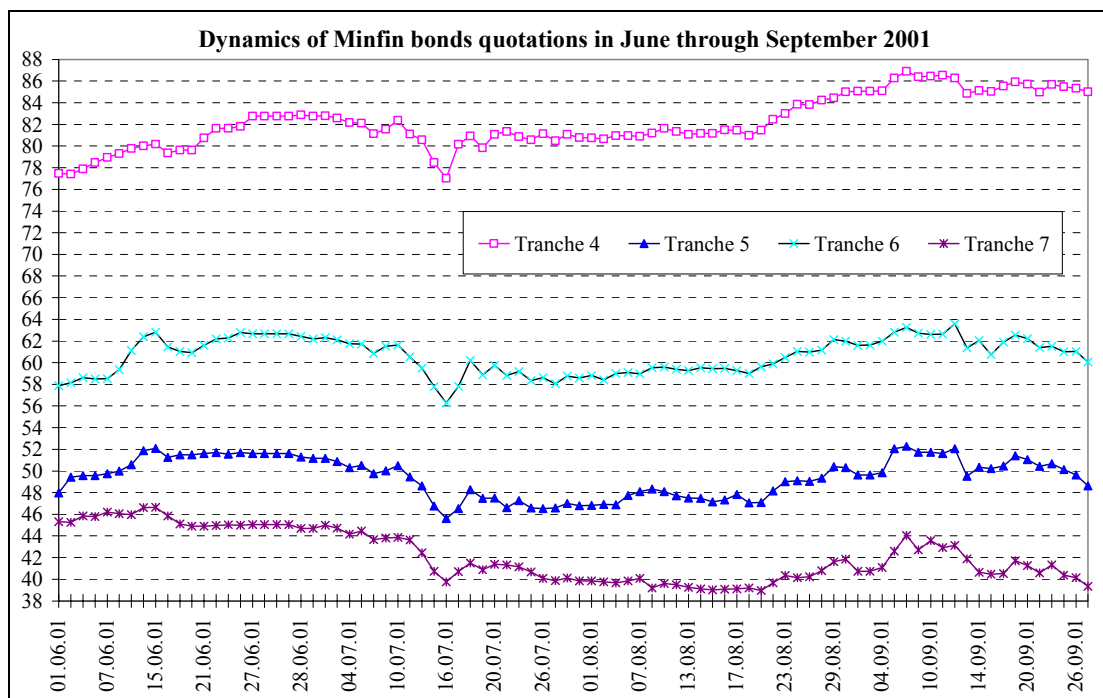


FIGURE 2.



The market for domestic debt in September 2001 showed its independence of external factors. The GKO and OFZ yields continued to decline during the whole month, and by the 20s of the month the average-weighted GKO/OFZ yield to maturity fell to 15% annualised. At the same time, in September the RF Ministry of Finance failed with a successful

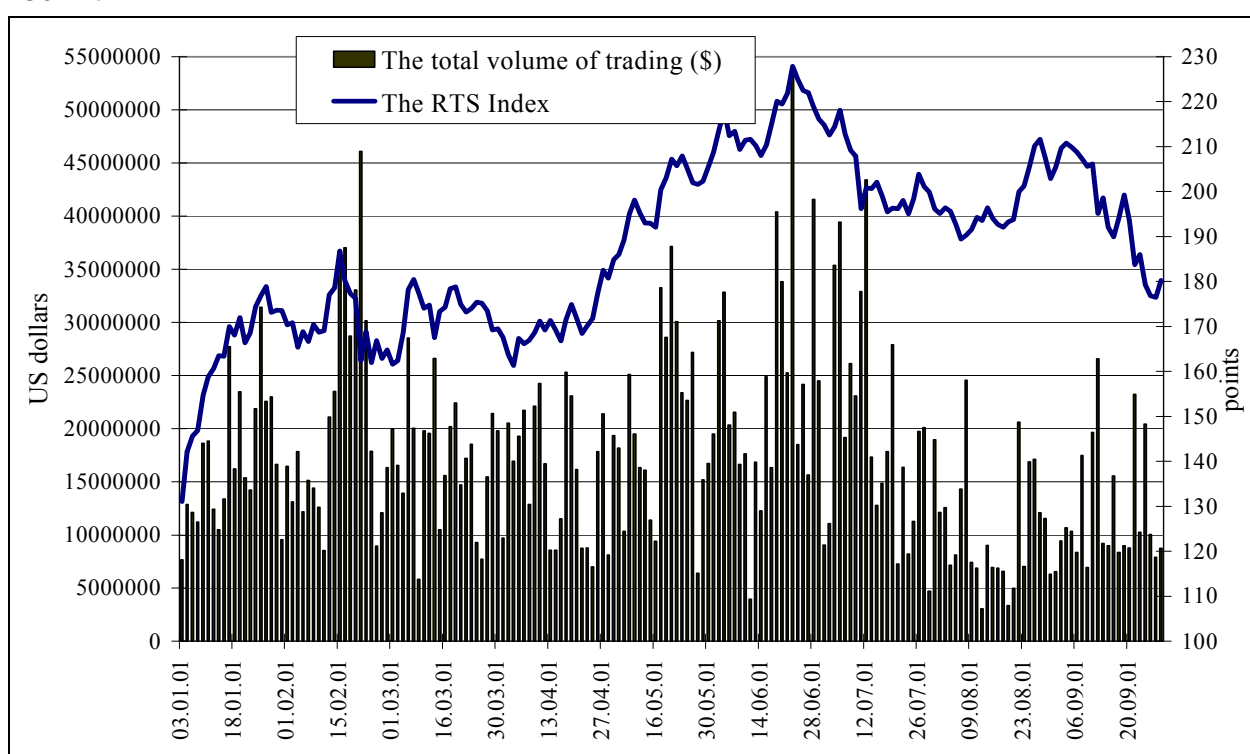
placement of new securities (five-month GKO and four-year OFZ) totalled up to 10 billion roubles. Thus, the auction on placement of OFZ was declared abortive, since the investors' bids seemed to the RF Ministry of Finance very high, and only 48% of the supply were placed at 13.9% annualised average-weighted yield.

Stock market

The boom on the Russian stock market, which had started in late August, came to an end with the events in the USA and subsequent fall in the world financial markets. The absence of large foreign investors ensured a relative independence of domestic market of the price decline abroad. However a sharp downfall in oil prices induced a loading-off of stocks of oil companies and the fall of the RTS index.

Overall, the RS index went down by 25.6 points (12.01%) over the month, the trade volumes remained negligible growing by 7.3% at the most relative to August. Thus, the turnover made up

FIGURE 3



As noted above, in September the prices for the Russian stocks found themselves affected by external factors. The leader among *blue chips* became the stocks of “Rostelecom” (-28.19%), followed by MMC “Norilsky Nickel” (-19.20%) and RAO “UES Russia” (-18.75%). The quotations of stocks of oil companies declined to a less extent: “Surgutneftegas” – by 14.98%, “Tatneft” – by 13.53%, “LUKoil” – by 13.21%, “YUKOS” – by 11.19%. The last was stocks of “Sibneft” – minus 5.61%. Despite the general bearish pattern, the “Aeroflot” stocks appreciated by 4.33%, however, their trade volume was the least among all blue chips.

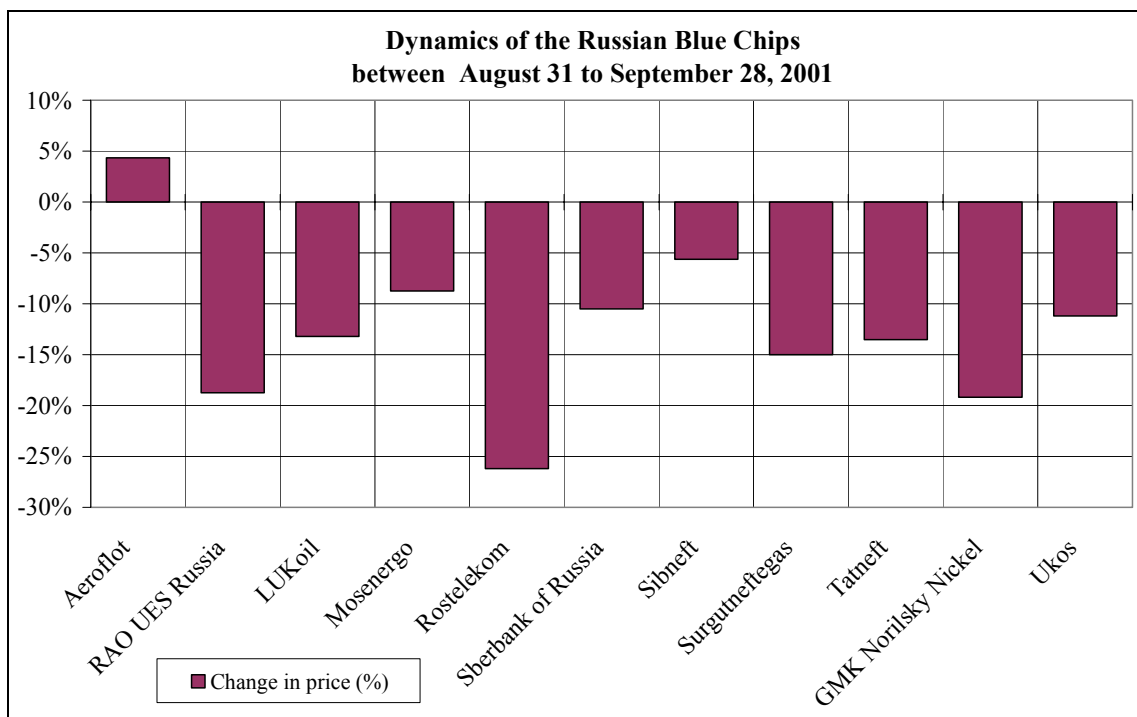
In September the RTS trade volume consisted of common stocks of RAO “UES Russia” – 29.95%

\$249.9 million. In September, the daily average trade volume rose by nearly 24% compared to August and amounted to \$12.5 million. The weekly average trade volume was about \$62.5 million. Between August 31 to September 11 the RTS index fluctuated within the range of 205-210 points. It is worth noting that the monthly maximum - 210.79 - was reached on September 4. Further, being influenced by the situation in world markets, the Index dropped, and on September 27 it reached 176.79 points, which is the minimum value since April 25, 2001. During the last day of the month the Russian stock index went up to 180.25.

(25%, correspondingly, in August), “LUKoil” – 20.90% (15.2%), “Surgutneftegas” – 10.59% (8%), “YUKOS” – 10.43% (25.1%), “Mosenergo” – 4.70% (3.49%). Thus, in September the total share of the five most liquid stocks in RTS declined to 76.58% (in August – 79.6%).

During last month, the trade volume on “Gazprom” stocks in RTS amounted to \$36.3 million (76.5 million stocks), with 3581 deals on them concluded. Between September 17 to September 21 1050 deals with “Gazprom” stocks were concluded, which became the maximum amount for the whole time of “Gazprom” trading in the RTS. The peak was recorded on September 17 – 334 deals.

FIGURE 4



On September 19 the RTS forward market (FORTS) was opened under the agreement on establishment of united market for futures and options between the RTS and the “Saint-Petersburg” stock exchange. Meanwhile, the futures on RAO “UES Russia”, “Gazprom”, “LUKoil” and Surgutneftegas” stocks and options on RAO “UES Russia” and “Gazprom” stocks are traded in FORTS. For the first hour of trades the turnover exceeded 15 million roubles (147 deals, 5206 contracts). For one and a half weeks the trade volume exceeded 500 million roubles. Notably, on September 25 the maximum amount of contracts on the “Saint-Petersburg” stock exchange (7-year life) was fixed – 38590.

Since October 1, the list of stocks used for the RTS index calculation was changed. Because of company restructuring, the common and preferred stocks of RAO “Norilsky Nickel” were replaced by the stocks of MMC “Norilsky Nickel”.

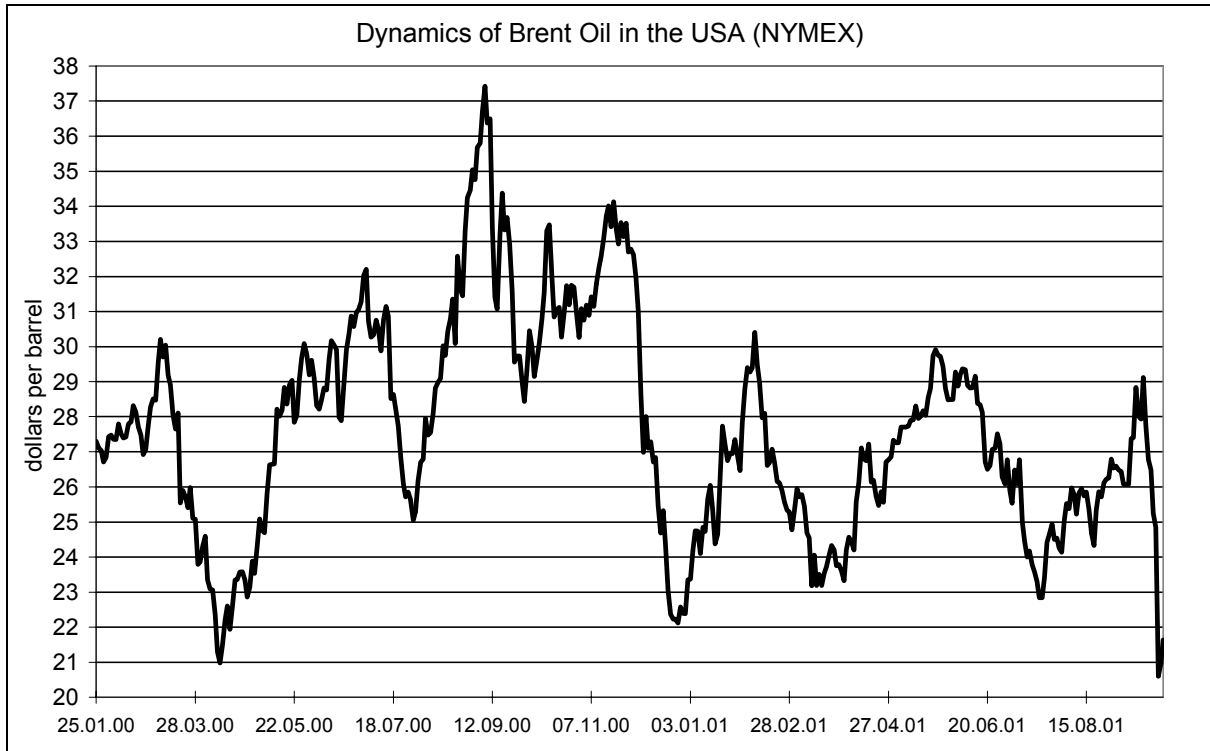
The external factors that affected the Russian stock market were mainly those related to the accident in the USA. The destruction of the World Trade Centre and expectations of the US striking back provoked a collapse in main world markets. The trades on the NYSE were stopped between September 11 to September 17. For the week of 17.09–21.09 the US stock indices fell considerably: the DJ lost 7.68%, Nasdaq – 9.9%, and S&P – 7%. On September 20 the S&P closed at below 1000 points. Interestingly, the RTS index slid by only 3.3% against such a background.

However the sharp decline in oil prices observed during the last week of September heavily affected the Russian stock market dominated by oil companies. On September 25, the oil price went down by \$4.25 (-17.1%) at once and reached the minimum value of 20.6 \$/bbl. That day the RTS index dropped by -6.82 points (-3.7%). The largest fall was recorded with regard to the stocks of “Sibneft” – 7.9%, followed by “Surgutneftegas” – 6.5%, “LUKoil” and “Tatneft” – 5.9%. The smallest fall was fixed with respect to “YUKOS” stocks – 4.2%.

On September 19, the American Oil Institute reported an increase in oil reserves in the USA. The reserves of jet fuel grew at the most, because of the suspension of flights. At the same time, the closing down of several oil terminals induced ceases in oil delivery, and the crude oil reserves declined. On September 26-27, the situation in the oil market was discussed on the OPEC Conference. The countries – OPEC members decided on remaining quotes unchanged, but this decision is subject to revision, should the situation worsen. In general, the state of the world oil market is determined by expectations on world recession and decline in the demand for fuel³.

³ Details see in section *Oil and gas sector*.

FIGURE 5.

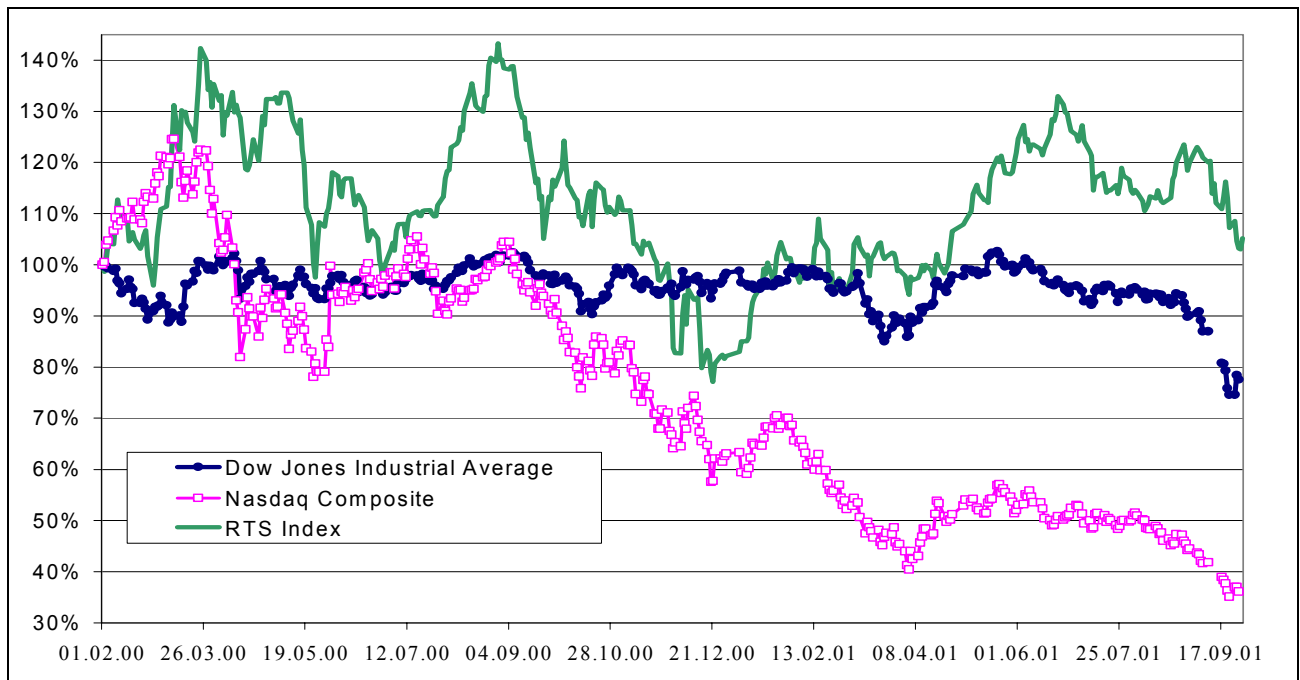


Without waiting for the Open Market Committee meeting scheduled for October 2, on September 17, the FRS reduced the federal funds rate once again by 50 basic points to 3.0%. On October 2, the rate was reduced to 2.5%. This decision was dictated by an aspiration to support a stable functioning of financial markets after September 11. The FRS demonstrated its commitment to

reduce interest rate, declaring that in the long run the American economy was subject to the risk of recession risk, rather than inflation.

To support the Eurozone economies, on September 17 the ECB dropped its interest rate by 0.5 percentage point - to the level of 3.75%. The Central Banks of many other countries also lowered their key rates.

FIGURE 6.



Corporate news

Further steps on the way of the “Gazprom” stock market liberalisation were made. President Vladimir Putin approved the plan, worked out by the task force. Now foreign investors are allowed to purchase “domestic” stocks and to convert them into ADR. We should note, however, that the share of foreign capital in the company is still limited by 20%, the trading and settlement procedures are rather cumbersome, and the separation of the markets for the company shares actually still is in place, although getting a softer from.

“LUKoil” started placing of 16,568.939 common stocks at a market price plus 15 cents. The market price is calculated by the RTS on the day preceding to the bidding one. The “LUKoil” net profit, calculated in compliance with the US GAAP standards, amount to \$690 million in the first quarter of 2001. The “Standard&Poors” rating agency increased long-term credit ratings of “LUKoil” and “Tataneft” to B and B-, respectively. “LUKoil” also holds the top line in the annual rating of the biggest trans-national companies in the Central and Eastern Europe published by the UN.

In the first half year the MMC “Norilsky Nickel” net profit amounted to 22,754 million roubles, i.e. by 0.6% below the respective index of last year.

The net profit of the RAO “UES Russia” in the first half - year accounted for 14.7 billion roubles (according to the Russian accounting rules), i.e. 3 billion higher plus vs. 2000.

The list of securities traded in the RTS was joined by common and preferred stocks of “Baltika” brewery.

The completion of the scandal around the position of “Mosenergo” Director General and the appointment of an acting Director General led to an increase in company’s stock prices in early-September.

The “Petersburg Telephone” intends to change its name for “North-West Telecom”. Under the “Svyazinvest” restructuring program, the “Petersburg Telephone” issued 262.896.773 common stocks and 87.646.542 preferred stocks. The securities of eight regional telecommunication companies were consolidated. In late-September – early-October the “Petersburg Telecom” will issued the first - level ADR. Also we should note that in September the “Petersburg Telecom” became the leader in the RTS, quotations of its stocks grew by almost 30%.

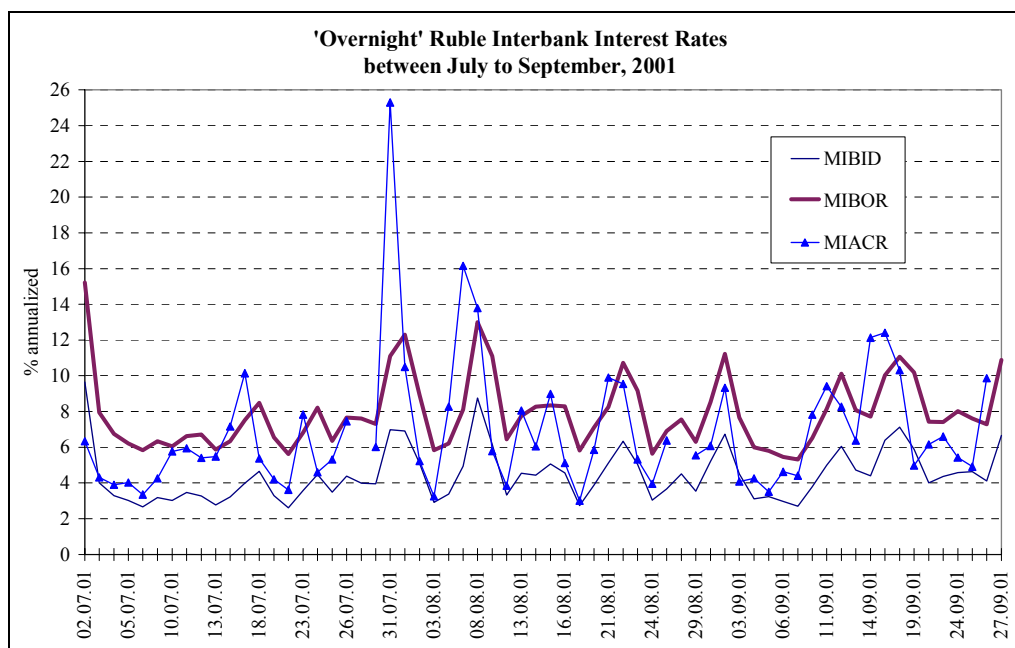
TABLE 1. DYNAMICS OF THE FOREIGN STOCK INDEXES

as of September 26, 2001	Value	change for last week (%)	change for last month (%)
RTS (Russia)	176.79	-13.93%	34.93%
Dow Jones Industrial Average (USA)	8567.39	-13.89%	-19.53%
Nasdaq Composite (USA)	1464.04	-18.91%	-36.12%
S&P 500 (USA)	1007.04	-11.16%	-21.53%
FTSE 100 (UK)	4696.1	-12.14%	-23.95%
DAX-30 (Germany)	4095.32	-21.06%	-34.89%
CAC-40 (France)	3975.53	-15.22%	-31.44%
Swiss Market (Switzerland)	5725.4	-13.02%	-29.48%
Nikkei-225 (Japan)	9641.7	-10.00%	-29.58%
Bovespa (Brazil)	10006	-22.08%	-35.13%
IPC (Mexico)	5324.84	-15.62%	-4.17%
IPSA (Chile)	100.75	-11.84%	1.38%
Straits Times (Singapore)	1277.71	-21.09%	-33.48%
Seoul Composite(Korea)	472.85	-13.26%	-9.23%
ISE National-100 (Turkey)	7477.42	-24.31%	-21.02%
Morgan Stanley Emerging Markets Index	194.409	-15.78%	-24.88%

Interbank credit market

In August and September 2001 the market for rouble interbank credits was rather calm (see Fig. 7). The “overnight” rate fluctuated between 4% to 10% annualised. It is an evident fact that in August we did not see even the traditional end-of-month effect, when the credit rates went up in the end of the month because of an increase in demand for roubles to settle payments and tax payments. The

FIGURE 7.



Foreign exchange market

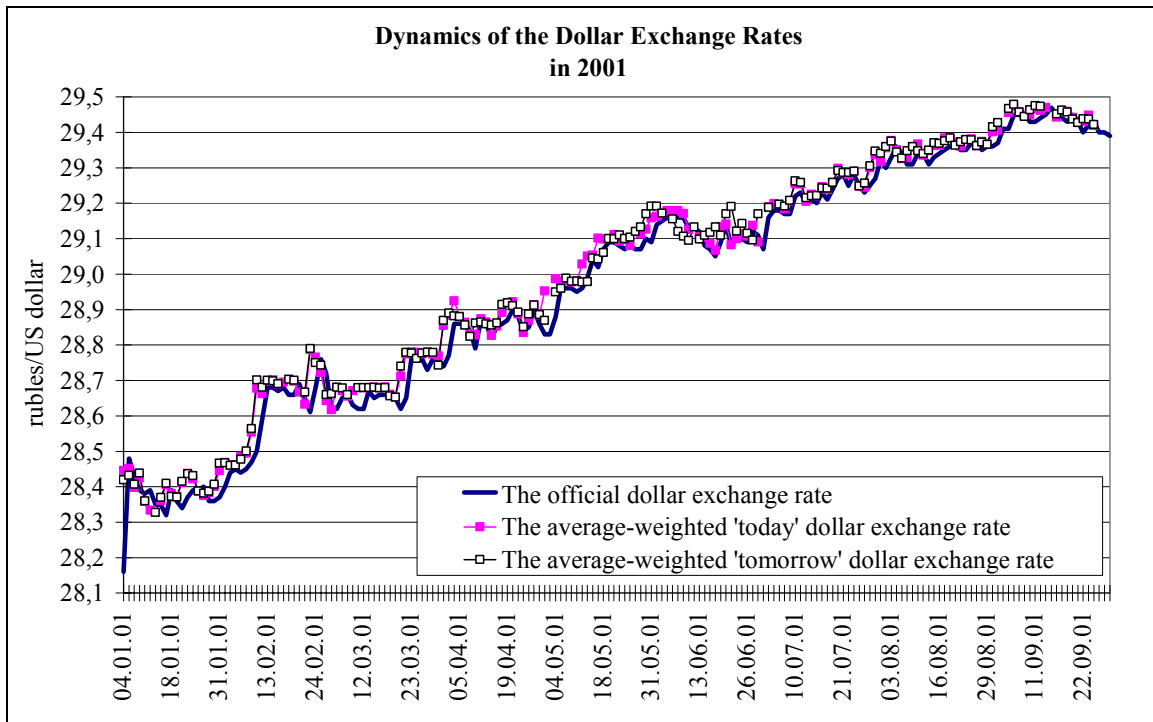
During early autumn, the foreign exchange market experienced some disturbances due to external shocks (after acts of terrorism in the USA to ensure regularity of trades the MICEX changed its clearing bank in US dollars – the new one became Chase Manhattan Bank). However the Bank of Russia maintained its control over the situation. Thus, the main effect of the temporary rise of uncertainty was a decline in the CBR’s foreign reserves, while the dollar exchange rate actually did not varied (the exchange rate increase did not exceeded 10 kopeck, or about 0.3%). Just within two or three days the dollar exchange rate arrived to the level of 29.4 roubles/USD. Notably, in the first hours after the information on events in the USA arrived, the sale of foreign exchange in the streets increased, and the street exchange points quoted cash USD for to 20–22 roubles/\$. However at the same time there was no serious increase in the demand for other foreign currencies (e.g., German marks or British pounds). This fact

balances on correspondent accounts of commercial banks with the Bank of Russia for the respective period experienced strong variations between 70 to 98 billion roubles. However, even a temporary liquidity shrinkage (e.g., on the eve of GKO auction in the beginning of the third decade the balances decreased to 70 billion roubles) did not evoke a rise in interest rates.

testified to Russians’ confidence in rouble as a more liquid and reliable (at least in the short run) asset in case of economic shocks in the USA. As well, there was no withdrawal of dollar-denominated deposits, i.e. the transaction costs associated with deposit withdrawal and “dollar–rouble” conversion were estimated as higher than possible gains on shifting to roubles even under unfavourable for the USD scenario. However the market for cash dollar stabilised the next day, and the buy/sell spread became narrow.

In September 2001, the official dollar exchange rate grew from 29.37 roubles/\$ to 29.39 roubles/\$, i.e. by 0.07% (0.82% annualised, see Fig. 8). The ‘today’ dollar exchange rate in the SELT increased from 29.4057 roubles/\$ to 29.419 roubles/\$ (as of September 27), i.e. by 0.05%. The ‘tomorrow’ dollar exchange rate grew from 29.416 roubles/\$ to 29.4218 roubles/\$ (as of September 26), i.e. by 0.02%. According to preliminary estimates, in September the trading volumes by dollar in the SELT amounted to 82 billion roubles at the most.

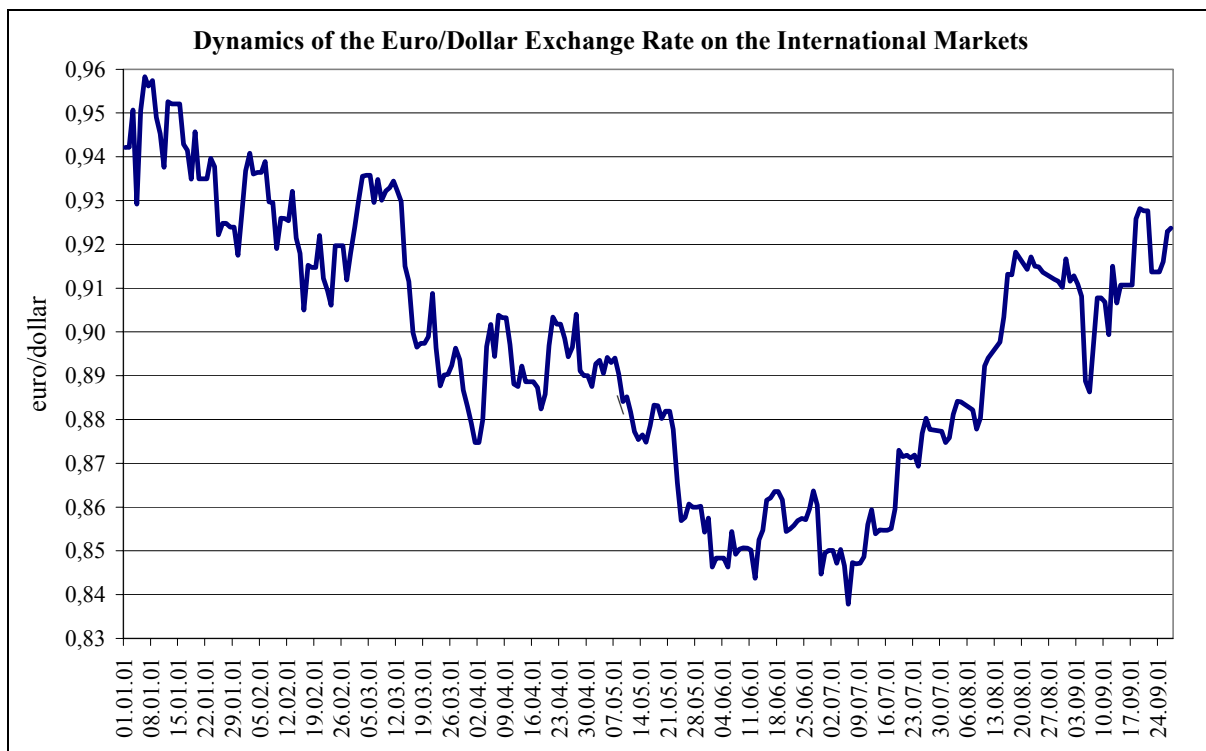
FIGURE 8.



In September 2001 the euro/dollar exchange rate reached its maximum since early-March 2001 (see Fig. 9). After the initial fall from 0.9068 to 0.8994 \$/euro on September 11, the euro/dollar exchange rate got the level of 0.922–0.923 \$/euro by the end of month. An interesting fact is that the euro/USD exchange rate dynamics in 2001 looks like well known in technical analysis of financial markets

inverted “head and shoulders” pattern. In particular, the “head” (0.84–0.86 \$/euro) fell on the period of the maximum slump in the euro exchange rate (June) and “shoulders” were at the level of 0.91–0.93 \$/euro (February and September). Thus, as early as in October one could expect a further growth in the euro exchange rate up to 0.95–0.96 \$/euro.

FIGURE 9.



In September 2001 the euro/ruble exchange rate reached its historical maximum. The ruble/euro official exchange rate decreased from 26.67 roubles/euro to 26.86 roubles/euro, i.e. by 0.71%,

FIGURE 10.

over the month (see Fig. 10). According to preliminary estimates, in September 2001, the total trading volume on euro in the SELT made up about 3 billion roubles.

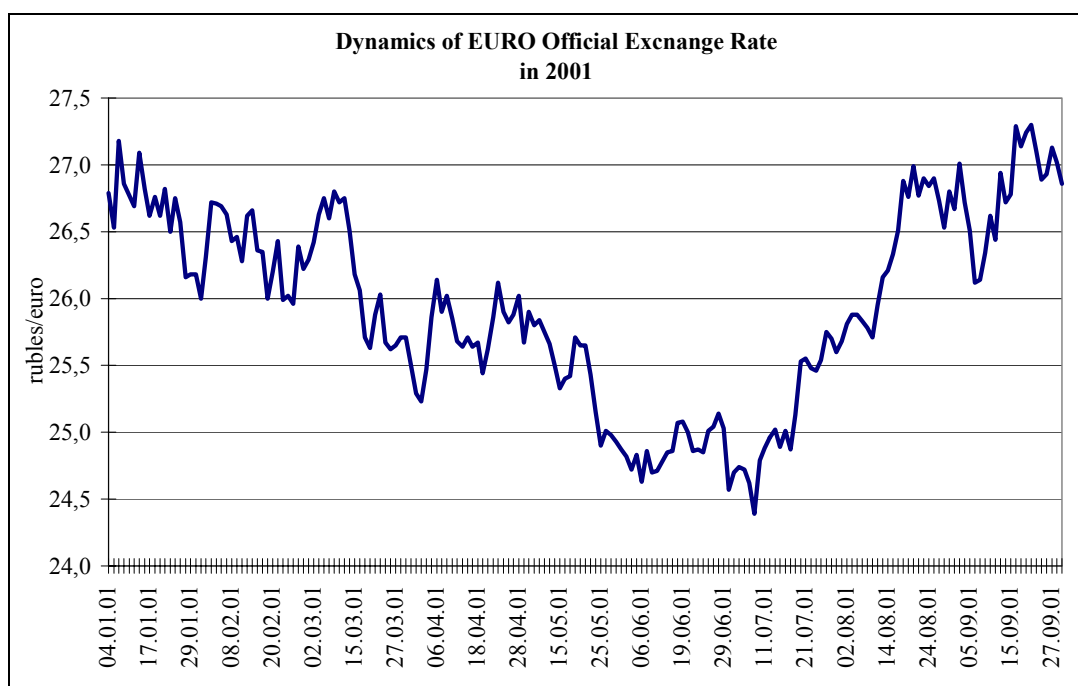


TABLE 2. INDICATORS OF FINANCIAL MARKETS.

	May	June	July	August	September*
inflation rate (monthly)	1.8%	1.6%	0.5%	0.0%	0.2%
annualised inflation rate by the month's tendency	23.87%	20.98%	6.17%	0.0%	2.43%
the RCB refinancing rate	25%	25%	25%	25%	25%
annualized yield to maturity on OFZ issues	17.11%	17.03%	17.19%	16.13%	15.5%
volume of trading in the secondary GKO-OFZ market a month (billion roubles)	7.98	7.92	11.67	7.44	8.3
yield to maturity on Minfin bonds by the end of the month (% a year):					
4th tranche	17.37%	13.91%	15.90%	13.05%	13.6%
5th tranche	16.34%	14.59%	16.29%	15.53%	16.1%
6th tranche	15.88%	14.01%	15.54%	14.78%	15.7%
7th tranche	13.09%	13.26%	14.79%	14.70%	15.4%
8th tranche	15.71%	13.93%	14.76%	14.21%	15.1%
INSTAR – MIACR rate (annual %) on interbank loans by the end of the month:					
overnight	13.87%	29.95%	25.3%	9.33%	10%
1 week	8.52%	29.49%	14.0%	10.28%	13%
official exchange rate of ruble per US dollar by the end of the month	29.09	29.07	29.27	29.37	29.39
official exchange rate of ruble per Euro by the end of the month	24.87	24.57	25.60	26.67	26.86
average annualized exchange rate of ruble per US dollar growth	0.90%	-0.07%	0.69%	0.34%	0.07%
average annualized exchange rate of ruble per euro growth	-3.12%	-1.21%	4.19%	4.18%	0.71%
volume of trading at the stock market in the RTS for the month (millions of USD)	405.7	490.4	436.8	232.0	249.9
the value of the RTS Index by the end of the month	208.80	216.11	196.12	205.41	180.25
growth in the RTS Index (% a month)	15.56%	3.50%	-9.25%	13.96%	-12.25%

* Estimates

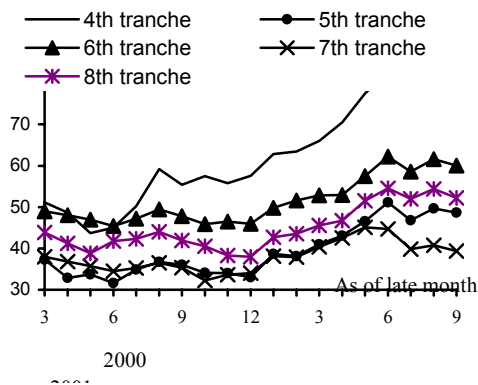
S. Drobyshevsky, D. Skripkin

The Russian banks on the market for government bonds denominated in foreign exchange (OVVZ)

The first half this year was characterized with a price rise for OVVZ. Of the five currently circulating tranches with the maturity between 2003 through 2011, it was the quotations of the fourth, the shortest tranche that experienced the highest price rise. Given that in late December 2000 the average price for them was 57.6%, it climbed up to 82.75% by late July.

By mid 2001 the OVVZ quotations found themselves ranging between 40 to 80% of their face-value, depending on the tranche (Fig.1).

FIG.1 THE AVERAGE PRICES FOR OVVZ IN 2000-01

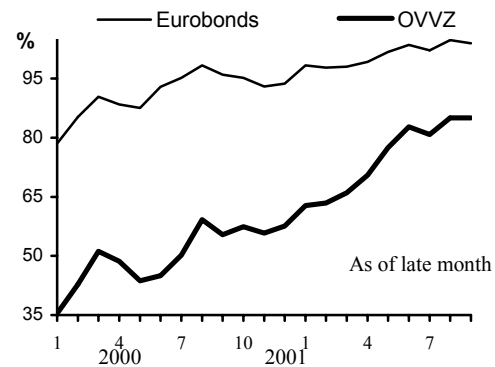


Calculated on the basis of the data of IA "Finmarket"
At the same time in the first half 2001 the proportion of OVVZ slid from 9.7 to 8.7%. This can be attributed to the fact that the average assets of Russian banks in absolute equivalent were growing faster than the Government federal debt obligations of the Russian Federation denominated in foreign exchange (FDO RF) in the banks' portfolios and their prices. Thus, the assets of the average Russian bank showed a 17.7% rise over the past half-year, while the amount of the noted FDO RF in Rb. terms grew just by 5%. That is, the banks would find more attractive investment instruments than the OVVZ, which is also proved by the fact that the prices for OVVZ and Russian Eurobonds were rising faster than the volume of the FDO RF in the Russian banks' portfolios. Thus, during the period in question the price rise rate for OVVZ accounted for 4.4.... 28.6%, depending on the tranche, while for Eurobonds-between 1 to 11%, depending on the tranche, while the portfolio of the FDO RF of the average Russian bank grew by 2.2% in USD equivalent.

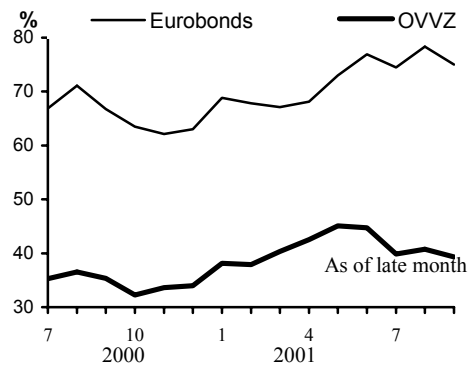
The investment characteristics of OVVZ tranches in 2001 continued to differ greatly from RF Government's Eurobonds. Whilst comparing the

prices for the latter and for OVVZ with similar maturity dates, the Eurobonds appear significantly more expensive. The difference is nearly two-fold, as far as the tranches with the most remote maturity dates are concerned. Thus, as of late July, the quotations of the tranches of both Eurobonds and OVVZ with the dates of maturity set for 2003 were 102 and 81%, respectively, while considering the longer-term tranches (with the maturity dates between 2010-11) the gap widens substantially (74% vs. 40%), given that the trend to shrinkage of the price spread is noted only for the tranches with the shortest term to maturity (see Fig. 2 and 3)

FIG. 2 THE AVERAGE PRICES FOR THE TRANCHES OF EUROBONDS AND OVVZ WITH THE MATURITY DATES IN 2003



Рассчитано по данным ИА «Финмаркет»
FIG. 3 THE AVERAGE PRICES FOR THE TRANCHES OF EUROBONDS AND OVVZ WITH THE MATURITY DATES IN 2010-11



As of late month
Calculated upon the data of IA "Finmarket"
The lower prices for OVVZ secured higher yields compared with Eurobonds, despite the latter showed a higher coupon yield. Whilst investing in OVVZ with an intention to hold them right until

the maturity date, despite a seemingly great price difference, the banks may have counted on 17 to 30% interest at the beginning, and 15-16% in the middle of the year (between 40 to 80%, depending on the tranche).

Yet another characteristic feature of the market for OVVZ is a higher margin rate between the purchase and sales prices (between 0.6 to 2.3% depending on the tranche vs. 0.2- 1.6% the one for Eurobonds noted in mid 2001).

Let us focus on operations of Moscow banks in the market for OVVZ. According to the data of information agencies 'Finmarket', 'MFD-Infocenter', 'RosbusinessConsulting', OVVZ are quoted by the Moscow banks presented in Table 1. Interestingly, all of them, except Metalinvest also are operators in the market for Russian Eurobonds, however, the group of the banks quoting Eurobonds also includes Akfa-bank, Impexbank, and Russky Generalny Bank.

TABLE 1. THE BANKS PROVIDING THEIR QUOTATIONS OF OVVZ TO INFORMATION AGENCIES*

Финмаркет	МФД-Инфоцентр	РосБизнесКонсалтинг
Sberbank RF	Sberbank RF	Sberbank RF
Guta-Bank	Bank of Moscow	Bank of Moscow
Eurofinance	Guta-Bank	Vneshtorgbank
Zenit	Metalinvestbank	Sovfintrade
MDM-Bank	MDM-Bank	Alba Alliance
Novikombank	Alba-Alliance	Eurofinance
Rosbank		Zenit
Roseximbank		Guta-Bank
Vozrozhdenie		MDM-Bank
Sobinbank		Монтажспецбанк
Expobank		Novikombank
		Sobinbank
		Rosbank
		Roseximbank
		ING Bank

It should be noted that the above list is not a complete list of financial institutions that quote OVVZ, nor it covers all the banks that conduct operations with or hold in their portfolio federal debt obligations of the Russian Federation denominated in foreign exchange (FDO RF).

Overall, as of mid-2001 the banks whose balances showed the presence of FDO RF denominated in foreign exchange outnumbered 140, however, it is the banks that provide their quotations to information agencies that can be regarded as the most active operators on this market.

To compare them with the average Moscow bank, the two biggest banks- Sberbank RF and Vneshtorgbank- were excluded from the both samples. As well, Montazhspeetsbank was excluded from the sample of banks-operators on the market for OVVZ, because as of the dates in question (January 1, 2001 and July 1, 2001), it did not have its own portfolio of OVVZ. Thus, the sample of the most active operators in the OVVZ market was

comprised of 15 banks. As for the group of Moscow banks, additionally, the banks run by ARCO were excluded, too.

The proportions of FDO RF denominated in foreign exchange in the assets of the banks that provide their quotations of OVVZ showed an upward trend. Thus, as of late 2000 the respective index accounted for 6%, by the end of the 1st quarter 2001- 6.5%, and by the beginning of the 3rd quarter- 7.2%. Interestingly, as concerns the group of Moscow banks, their respective index slid from 4.1 to 3.8% over the period in question.

The growth in FDO RF denominated in foreign exchange in absolute terms over the half-year in USD equivalent for the banks providing their OVVZ quotations accounted for 36%, while there was a practical absence of that for all the Russian banks, while as for the Moscow banks, the respective rate made up just 14%.

As of mid-2001, the overall assets of the Moscow banks- operators in the OVVZ market accounted

* Commercial banks of the Russian Federation

for Rb. 220.8 bln., or 17% of the assets of the operating Moscow banks (without regard to Sberbank and Vneshtorgbank). At the same time by mid-2001, the banks-operators in the OVVZ market appeared on average 7-fold bigger than a Moscow bank.

Interestingly, in the 2nd quarter the growth rate of the banks-operators in the OVVZ market accelerated sharply vs. the 1st quarter (12.1% vs. 3.9%, respectively). Thus, given that in the 1st quarter it was the average Moscow bank's assets that showed a faster rise (8.1 and 11.25% in the 1st and 2nd quarters, respectively), in the 2nd quarter it was the banks-operators in the OVVZ market that showed a greater growth pace of their assets.

Table 2 presents some indices of the structure of the balance of the two groups of banks as of the beginning 2001 and mid-2001. The comparison

demonstrates that the banks that are active in the market for FDO RF denominated in foreign exchange, are more reluctant to place their capital in the banking sector compared with the average Moscow bank, while at the same time they hold a more pro-active stand in regard to extending credits outside the banking sector.

One should pay a special attention to the dynamics of the profit to assets ratio. The ROA index of the average Moscow bank for 2000 accounted for 0.95%, while it grew up to 1.7% over the first half 2001 in annual terms.

The respective index for the group of banks that provide their quotations of OVVZ was positive between 2000 to 2001, however with a downward trend (2.9% over 2000 and 0.8% annualized over the 1st half 2001).

TABLE 2. SOME INDICES OF THE STRUCTURE OF THE BALANCE AS % TO ASSETS, AS OF THE END-MONTH

Indices as % to assets	Moscow banks		Banks- active operators in the market for OVVZ	
	12.2000	06.2001	12.2000	06.2001
The data of the balance	12.2000	06.2001	12.2000	06.2001
Assets denominated in foreign	48.7	47.9	43	39.4
Capital in the banking sector	41.4	41.7	32.6	26
Including in foreign exchange	22.8	23.9	12.7	8.6
Loans extended to the non-banking	38.1	39.5	43.3	48
Including in foreign exchange	18	17.5	17.6	16.7
Promissory notes (excluding banks')	7.2	7.2	12.9	11.4
Including in foreign exchange	1	0.9	5.6	4.9
Obligations and shares	9.1	7.8	9.2	10.8
Including in foreign exchange	5.6	4.5	6.9	8
FDO=s	6.5	5.6	7.4	8.3
Including in foreign exchange	4.1	3.8	6	7.2
Deposits	17.2	17.8	22.4	21
Including in foreign exchange	12.9	13.5	13.1	13.4
Deposits placed by legal entities	12.3	12.1	17.3	15
Including in foreign exchange	9.2	9.1	9.3	9
Deposits placed by private	4.9	5.7	5.1	6
Including in foreign exchange	3.7	4.4	3.8	4.4
Balance-sheet capital	21.3	20	14.6	12.9
<i>For reference:</i>				
<i>The average assets as Rb.blm.</i>	<i>1.74</i>	<i>2.05</i>	<i>12.6</i>	<i>14.7</i>

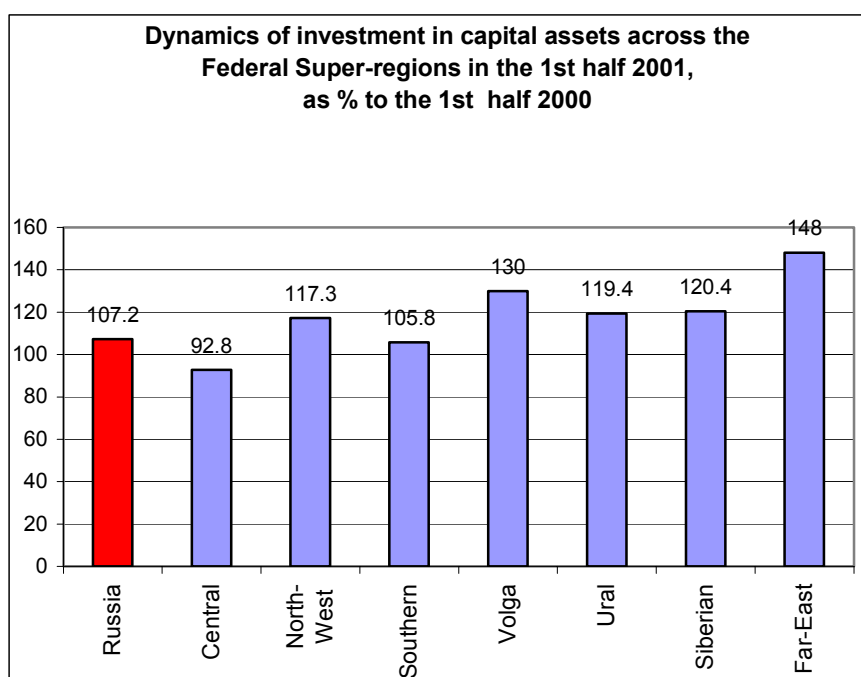
Calculated on the data of CBR and STiK company

E.Marushkina, E. Timofeev

Investment in the real sector

The positive dynamics of growth in investment in the real sector was in place between January through August 2001. During this period the volume of investment in capital assets from all the sources of financing accounted for Rb. 827.7 bln., or at 7.5% more than the one reported over the period between January through August 2000. The investment demand rises at an advanced pace

compared to dynamics of GDP. When compared with the 1st half 2000, the share of investment in capital assets grew by 1.7 per cent points and accounted for 14.6%. According to results of the 1st half 2001, the growth in investment in capital assets compared with the respective period of the prior year was registered in all the federal Super-region except the Central one.



The growth in investment demand is accompanied by an intense increase in output in all the sectors of the investment complex. During the period in question (January- August 2001), the increment in the machine- engineering output accounted for 8.5%, while the one in the industry of construction materials – 5.9%, and services and works in the construction sector- 7.6%.

The growing demand for new kinds of machinery and equipment is related to the activation of the process of renewal of machinery stock in main sectors of the economy and production reconstruction. That determines major changes in the technological structure of investment. The trend to systematic increase in the share of spending on machinery and equipment has been in place over the past two years. In the 1st half 2001 the share of investment in machinery and equipment accounted for 35.7% vs. 34.8% reported over the respective period of the prior year. However, on the whole, the domestic machine engineering sector does not satisfy the sharply growing demand for technical means, and the import of machinery and equipment nearly doubled

compared with the prior year. In the 1st half 2001 enterprises and organizations invested as much as Rb. 45 bln. in purchasing import equipment, or 24.6% of the overall volume of investment in machinery and equipment (with no account for the share of small businesses).

The characteristic feature of the change in the structure of investment in capital assets across the sources of funding in the 1st half 2001 is a trend to decline in enterprises' own funds from 49.3% vs. 53.3% reported over the respective period of the prior year. Despite a slowdown in the profit growth rates, the enterprises proceed with increasing their investing in production modernization and expansion. When compared with the 1st half 2001, the share of profit in the structure of enterprises' spending on investment grew by 8.3 per cent points.

At the same time the share of banking credit in the composition of attracted funds continues to decline, especially the one of credits extended by foreign banks and loans from other organizations. The fall in the share of budget capital- from 20.6% in the 1st half 2000 to 19.2% over the respective

period this year can be attributed to the contraction in the volume of funds attracted from the budgets of the Federation's Subjects from 14.3 to 12.9%. When compared with the prior year, the share of

off-budget funds in the structure of the sources of investment funding in the real sector rose by 1.2 per cent points.

TABLE. STRUCTURE OF INVESTMENT IN CAPITAL ASSETS BY SOURCES OF FINANCING, AS % TO RESULT

	1998	1999	2000	1 st half	
				2000	2001
Investment in capital assets	100,0	100,0	100,0		100,0
Including					
1. <i>Own capital</i>	53,2	52,4	46,1	53,5	49,3
Of which profit	13,2	15,9	23,4	21,7	24,1
2. <i>Attracted capital</i>	46,8	47,6	53,9	46,5	50,7
Of which					
Budget funds	19,1	17,0	21,2	20,6	19,2
Including from:					
Federal budget	6,5	6,4	5,8	5,2	5,3
Budgets of the Federation's Subjects	12,6	9,6	14,4	14,3	12,9
Banking credits	4,8	4,2	2,9	4,0	3,3
Borrowed funds	4,3	5,6	7,2	9,4	6,0
Resources of off-budget funds	10,7	8,6	4,8	3,8	4,6
Others	7,8	12,2	17,8	8,7	17,6
Of the overall volume of investment in capital assets from abroad	3,4	6,6	4,6	4,9	4,7

Source: Goskomstat of RF

In the 2001 federal budget Rb. 282. Bln was allocated to finance government capital investment, including Rb. 23.8 bln.- to fund the Federal Targeted Investment Program. In 2001, the financing of public investment is carried out more evenly than in the past: between January through August the government has funded some 65% of the annual limit of public capital investment, while the Federal targeted investment program was funded at 60.7% of its annual limit (Rb. 14.4 bln.), and Rb. 3.7 bln. was spent to repay the credit liability for earlier complete works.

According to the 2002 federal budget law, it is envisaged that the state investment should reach Rb. 42.27 bln, which should make up 0.35% GDP and 2.2% of the overall projected volume of investment in capital assets, thus allowing the 30% increment in public investment vs. 2001.

According to the draft 2002 federal budget law, the funding of the Federal targeted investment program should amount to Rb. 34.46 bln., or at 33.3% more than the respective sum allocated for the Program implementation in 2001. The main part of government capital investment is designated for funding the social sector – 61.2% (a

15.5% more than in 2001). Rb. 5.82 bln. should be spent on maintenance and development of the production complex (16% of the overall amount of spending on the Program). When compared with 2001, the increment in public capital investment in the production complex should make up 73%, with a special emphasis put on solving the problems of development of infrastructure branches and increasing the reliability of the country's energy sufficiency.

Overall, the dynamics and nature of the use of public capital investment by major directions match the proclaimed goals of political and economic and social development in 2002.

According to FITCH's estimates, Russia appears one of the most successfully developing economies in terms of macroeconomic indicators. Analysts believe that the RF government was efficient in using additional revenues generated thanks to high oil prices. Standard and Poor's confirmed all Russia's ratings – the long-run 'B' and short-run 'B' alike, and changed their forecast of the country's long-run sovereign credit ratings from 'stable' for 'positive'.

O. Izryadnova

Foreign Investment in Russian economy

As of July 1, 2001, the foreign capital accumulated in Russian economy, including investments from the CIS states accounted for USD 33.84 bln.

The increment in the overall volume of foreign investment in the Russian economy in the first half 2001 vs. the respective period of 2000, without

regard to the monetary and credit regulatory bodies, commercial and savings banks, inclusive of Rb.- denominated investment, in USD equivalent, accounted for 39.9%. This year is characterized with the growth in the capital exportation volume compared with the respective period of 2000.

	Ist half year, as USD mln. (as of July 1)			Change vs. the respective period of the prior year	
	1999	2000	2001	2000	2001
Investment accumulated as of the beginning of the period Накоплено инвестиций на начало периода	35 338	29 253	32 005	-17,2%	9,4%
Investment inflow over the period	4 271	4 778	6 684	11,9%	39,9%
Investment accumulated as of the end of the period	27 820	30 679	33 839	10,3%	10,3%
Total: investment withdrawn (repaid) over the period	11 789	3 352	4 850	-71,6%	44,7%

It was portfolio investment that showed the highest growth rate vs. other kind of investment in the first half 2001 (4.7-fold). The growth in the volume of direct and other foreign investment in the national economy over the period in question accounted for

40.5% and 33.9%, respectively. At the same time the structure of foreign investment in the Ist half 2001 remained practically unchanged vs. the respective period of 2000

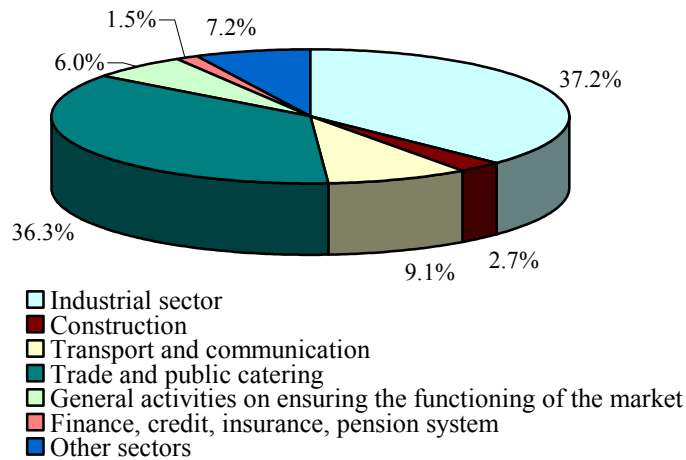
	Foreign investment inflow in the 1 st half year							
	1998		1999		2000		2001	
	As USD mln.	Share as %	As USD mln.	Share as %	As USD mln.	Share as %	As USD mln.	Share as %
Total	7697,9	100	4271	100	4778	100	6684	100
including:								
- direct	1509,4	19,6	2429	56,9	1786	37,4	2509	37,5
- portfolio	32,4	0,4	7	0,2	51	1,1	238	3,6
- others*	6156,1	80	1835	43	2941	61,5	3937	58,9

*Investment mostly formed at the expense of credits received not from direct investors- World Bank, IMF, EBRD, and the resources investors spend on purchasing government bonds, primarily GKO-OFZ.

As concerns the sectoral structure of foreign investment attracted in the national economy in the 1st half 2001, their major part (although a smaller one) still falls within the industrial sector. The volume of foreign investment in the national

industrial sector over the period in question accounted for USD 2,487 mln., or at 9.4% more than in the Ist half 2000 (2,273 mln., or 45.6% of the aggregate volume of attracted investment).

The sectoral structure of foreign investment in RF in the 1st half 2001



This year, one notes a substantial growth in investment in trade and public catering (over 3-fold one compared with the 1st half 2000), which reflects changes in foreign investors' sectoral

preferences that have taken place over recent years and attributed to the lowering attractiveness of Russian fuel and energy complex.

	Foreign investment attracted over the 1 st half year, as USD mln.					
	1996	1997	1998	1999	2000	2001
Fuel sector	153	588	1147	1434	286	298
Торговля и Trade and public catering	375	313	519	583	766	2426

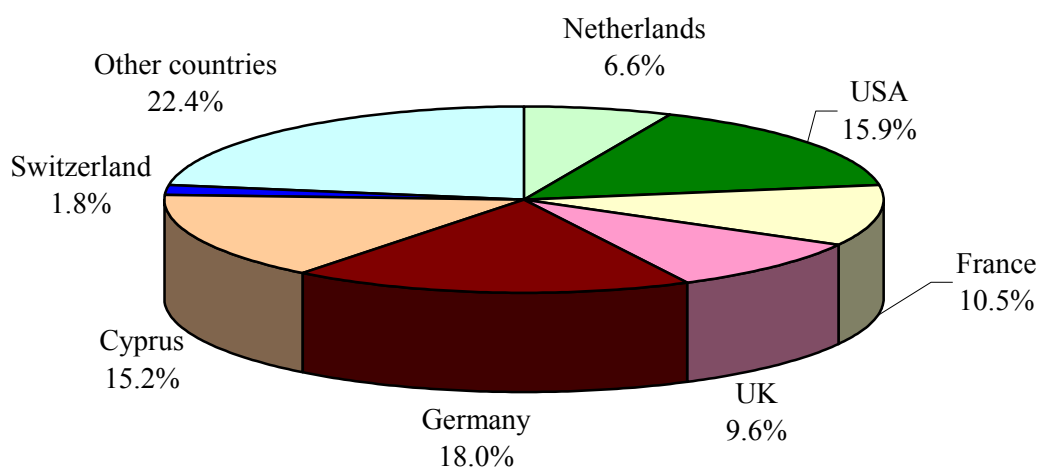
The foreign capital gradually increases its participation in the national banking system. During 7 months of 2001 the number of banks with foreign participation grew up to 35 (as of January 1, 2001, there were 33 ones), of which 21 bank are at 100% owned by foreign capital.

As concerns main industries, it is metallurgy, the fuel and food-processing sectors that still appear most attractive to foreign investors. At the same time foreign investment in the metallurgical and fuel sectors grew by 46.1% and 4.2% compared with the 1st half 2000, thus accounting for USD 802 mln and 298 mln (32.2% and 12% of the aggregate investment in the industrial sector), while investments in the food sector fell by 13.1% and currently account for USD 701 mln.

The major part of FDI (69%) was forwarded mostly to trade and public catering (USD 782 mln.), followed by the fuel and food sectors (183 and 272 mln., respectively), machine building (118 mln.), transport (378 mln.). The share of FDI in the industrial sector in the 1st half 2001 accounted for 33% (USD 831 mln.) of the overall volume of direct investment in the national economy this year (in the 1st half 2000- 45%, 1st half 1999- 70.4%).

As concerns the geographic structure of foreign investment in the 1st half 2001, the clear leader is Cyprus (17%), USA (12.3%), France (10%), Switzerland (9.4%), and UK (8.8%). According to results of the 1st half 2001, the country structure of the accumulated capital differs substantially from the analogous structure of the investment inflow over the first half this year

Geographic structure of foreign investment accumulated in the Russian economy in the 1st half 2001



When compared with the respective period of 2000, the level of the US investment (as of July 1, 2001) fell by 36.2% relative to the one reported as of July 1, 2000 and by 23.7% relative to early 2001, while the respective indices for German investment inflow contraction accounted for 7.3% and 6.8%. At the same time among the major countries- investors in Russia that increased the volume of investing over the period in question, it is Netherlands (2.2 times relative to July 1, 2000 and at 55.2% to January 1, 2001), UK (35% and 42.3%), and Cyprus (2.7 times and at 21.7%). As for the Swiss investment, it showed a 1.5-fold growth relative to its respective index as of July 1, 2000 and currently account for USD 616 mln.

In the meantime, the Swiss public agency established in 1997 and dealing with encouragement of a long-term cooperation between Swiss companies and Russian private sector considers the possibility of expanding cooperation with small- and medium-size Russian businesses in the areas of car manufacturing, energy, biotechnology, clock, food, and other industries.

In the second half 2001 the investment climate in Russia may experience a positive impact of the recent increase by FITCH of the country's sovereign credit rating up to "B" level, however, the recent terrorist attacks on the US may entail a contraction in the investment inflow in Russia.

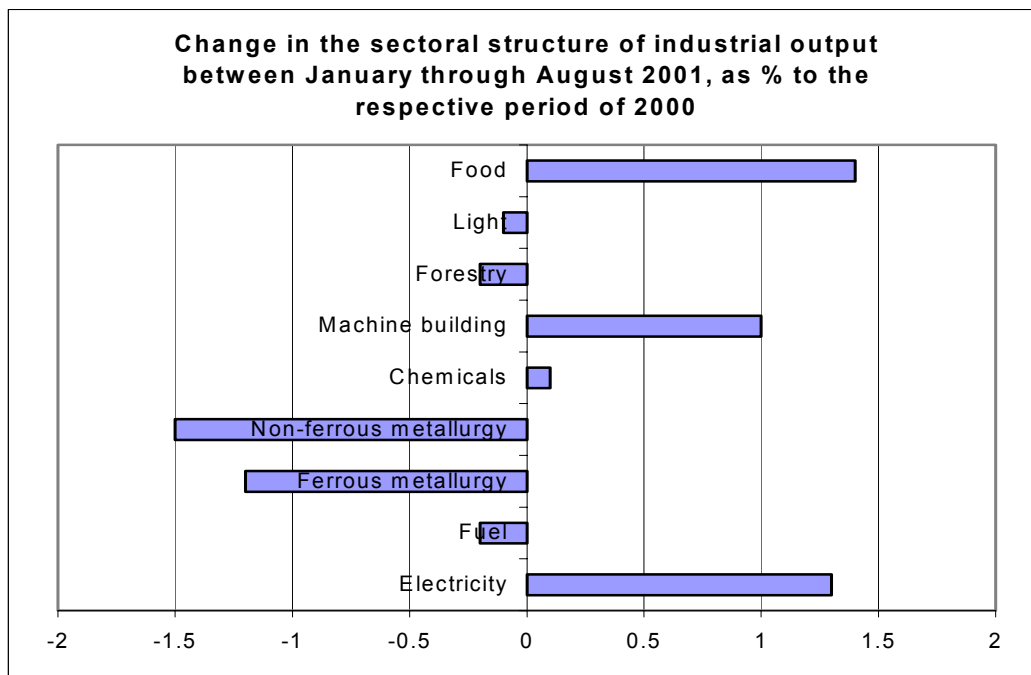
E. Ilykhina

The real sector: factors and trends

According to Goskomstat, in the first half 2001 GDP accounted for Rb. 3,994.5 bln., thus being at 5% in excess over its respective index of the prior year. It was the dynamic expansion of final demand that has had a positive impact on the dynamics of GDP and output of goods and services by the basic sectors of the economy alike since the IInd quarter this year. Given that in the 1st quarter 2001 GDP slid by 12.7% compared with the IVth quarter 2000, with the renewal of an intense growth in investment demand, the negative results of the production decline were overcome by May through August, and the economy once again found itself on the path of economic development. In the IInd quarter, the increment in GDP reached 8.1% compared with its respective index of the prior period of the year and 51.% - relative to the prior year.

The rise in output was noted practically in all the sectors; the output of goods and services by the basic sectors grew by 5.9% compared to the period between January to August 2000. With the growth in industrial output between January through August at 5.3%, the output in the construction sector rose at 7.6%, while the retail trade turnover – by 10%.

FIG.



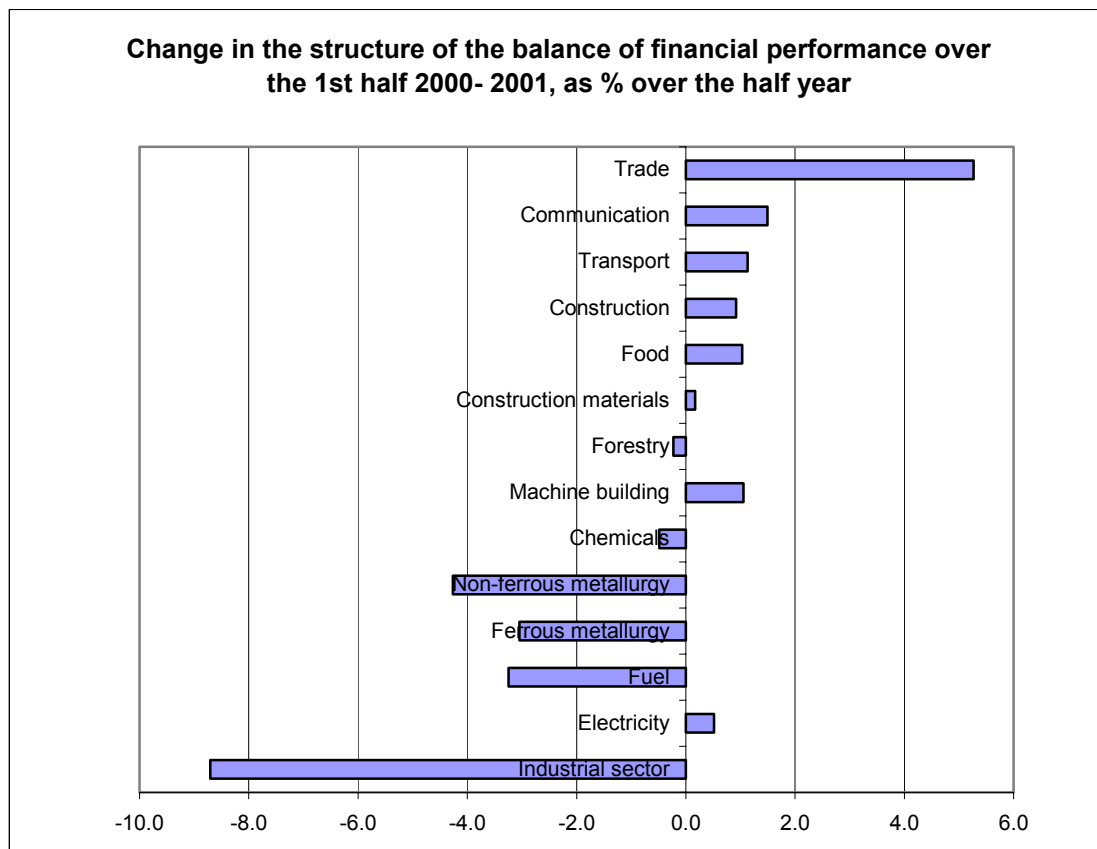
The analysis of the structure of the industrial rise shows that the growth in output practically completely was backed-up by an advanced growth in the sectors focused on the domestic market. While compared with the time period between January through August 2000, the index of output accounted for 108% across the complex of investment sectors and 107.7% across the complex of consumer industries. In particular, with its increment in output accounting for 8.5% vs. to the respective period of the prior year, the sector for machine engineering is one of the most dynamically developing industries, however, the situation in the sector still is very complex. The dynamics of output by single sub-sectors is subject to fairly substantial fluctuations. The decline in output in car manufacture, machine tool manufacture and metal machine engineering indeed is an alarm bell. With the well-developed inter-sectoral ties system, the contraction in output affects the dynamics of the production of construction materials in the metallurgical sector as well as the intensity of the processes of reproduction of the active part of capital assets in the economy.

Following some slowdown of the consumer demand growth rate over the 2nd quarter, it has renewed notably in August. The commodity saturation of the market is steady and fully matches the population's effective demand. When compared with July, the retail trade turnover grew

by 6.4%, with its average monthly growth rate over the 2nd quarter roughly accounting for 0.2%. The rise in consumer demand manifested itself in the production renewal in the food and light sectors. In August, the increment in output the light industry accounted for 10.1% and in the food industry-3.3% relative to July. Notably, the rise in output in the consumer complex between July to August undoubtedly can be attributed to the impact of the correction lowering of imports. However, even under such circumstances, the proportion of imports in the overall volume of commodity resources made up 29% in the 2nd quarter and showed the 1% growth compared with the 1st quarter.

The growth rates in the output of the oil and energy sub-sectors and export-oriented industries over the time period between January through August accounted for 104.9% and 103.6%, respectively. The slowdown of growth in mineral sectors shows the trend to decline in the physical volume of exports. As concerns the overall volume of sales of industrial goods, in June 2001 the proportion exports accounted for 28.4% of that vs. 32.4% reported over the respective period of 2000. The trend emerges on the background of an intense rise of competitive imports, which may affect the nature of economic development. Between January to July 2001 vs. the respective period of 2000 the increment in imports accounted for 20.1%, while the rise in industrial output made up 5.5%.

FIG.



Whilst estimating short-term prospects for industrial development, one should pay a special attention to the decline in industrial enterprises' incomes. Since early 2001 the dynamics of profits has been characterized with a consistent fall of its rate in all the sectors of the economy from 124.5% in January down to 96.3% between January to July, while the respective fall in the industrial sector was from 104.5% down to 83.0%. Between January to July the financial performance balance accounted for Rb. 652.7 bln., including the industrial sector Rb. 246.9 bln. The profit rate in the industrial sector fell from 18.0% between January to July 2000 to 10.0% over the respective period this year.

The reduction in the profit rate in the industrial sector is determined by rising production costs due to the growth in wholesale prices and tariffs for consumed material resources against a more gradual change in pricing of industrial producers, as well as because of an advanced growth rate of salaries and wages against the price dynamics for final products. In addition, the situation is affected by a relative worsening of the situation in external markets for some Russian exports. Should the trend intensify further on, it would be fairly problematic to count on investment growth that, in essence, is the main source of economic growth. At

the same time, it should be noted that according to results of the 1st half year, enterprises increased the share of profit spent on production expansion in the composition of their investment resources. That highlights the change in priorities and motivation of economic activity – the domestic producers link the prospects for expansion and maintenance of their positions in the national and external markets with an activation of technical modernization and renewal of their production.

Given that in 2000 the rise in investment demand was generated by the growth in revenues in the export-oriented industrial sector, this year it is the sub-sectors of investment and consumer complexes, and the sphere of services that induce the investment renewal process. While the profit rate in the fuel complex was down by 8.1% compared with the 1st half 2000 and in the metallurgical sector it fell almost twice, the sector for machine engineering increased its profit by 34.9%, in the industry of construction materials- by 62.1%, and in the construction sector- by 38.6%. The characteristic feature of investment demand over the period between April to August became the shift in its structure towards machine-engineering produce, which supported the production of technological equipment, along with

a simultaneous rise in the demand for construction services and works.

The positive factor supporting the level of business activity has become the trend to decline of inflation rate. Zero inflation in August appeared an additional factor of acceleration of the growth in final demand. In view of that, one should be

especially attentive towards the areas in which a generation of a new wave of inflation may become possible – that is, the price rise for gas, growth in tariffs for cargo transportation and paid services to the population, and seasonal price rise in the agrarian sector.

O. Izryadnova

IET Monthly Trends Survey: September 2001

The continuous rise in monetary sales allowed enterprises a further increase in their rate of output and getting rid of barter. However the stock of finished goods has remained excessive and forecasts of sales in the IVth quarter appeared the most moderate ones since early 2000.

In September, the growth rates of monetary sales of industrial products continued to grow. Their balance grew by another 4 points and reached the maximum value observed over the past 11 months. Effective demand grew in all the sectors except the non-ferrous metallurgy that reported an absolute fall in the index. As a result, according to preliminary estimates, overall, the share of industrial output paid for in cash reached 76%, while the volumes of barter deals continued their decline, with the contraction rate of such transactions growing for the third month running. It is the sectors for chemicals, petrochemicals, machine engineering and light industry that reported the most intensive decline in their barter deals, while none of the sectors has reported any growth in barter. As well, the volume of off-set and promissory note deals has slowed down in September, the surveys registered one of the slowest rates of decline if such deals since early 2000.

The renewal of the growth in effective demand allowed enterprises to proceed with the growth in their output. In September, the intensity of the growth in output rose by another balance points. Clearly, the production has not grown at such a rapid pace over the past 16 months. All the industry branches demonstrated a growth in their rate of output, except the metallurgical and construction sectors. A rapid growth in output has improved sharply the enterprises' estimates of their volumes of output: the share of reports "below norm" fell to 56%, which has become the best value ever registered by 112 surveys held since March 1992 (for reference: in "bad times", the share of such reports would be 91%).

A fast growth in output has ceased the contraction in the excessive stock of finished products. In September, the surveys once again registered a slight growth in the excessive stock, with the construction sector and the food-processing

industry lacking the stock for the fourth month running. In September, they were joined by the forestry, wood-working, and paper and pulp sectors.

The normal availability of credits for industrial enterprises from all the sources grew by 11 points over the year and currently accounts for 52%. It is the enterprises operating in the sectors for non-ferrous metallurgy and electric power that experiencing the least problems with obtaining credits, while those of the forestry and construction sector find it most difficult to get loans.

The forecasts of the change in effective demand deteriorated drastically in September – in the IVth quarter the enterprises envisage a substantial slowdown of the growth rate of their monetary sales. There has not been such a low optimism in the industrial sector since early 2000. The slowdown in the growth rate of monetary sales is forecasted by all the sectors, while the metallurgical sector and construction industry envisage their absolute decline.

The forecasts of barter deals "improved" by 4 points, i.e. the enterprises expect a more intensive contraction in such transactions at the end of the year. The growth in barter may become possible only in the food-processing sector. The forecasts of off-set and promissory note transactions remained unchanged in September, and the balance of these forecasts is slightly different from zero, which testifies to a probable stabilization of their volumes.

In September, the forecasts of changes in output remained unchanged – the industrial sector maintains fairly strong hopes for a growth in output that are especially great in the machine-engineering sector, chemicals, petrochemicals, and the light industry. Some fall in output may become possible only in the industry of construction materials.

Business surveys provide an unparalleled opportunity to evaluate the accuracy of enterprises' forecasts on microlevel. Let us employ a simple and clear indicator – the proportion (as %) of

enterprises whose forecasts have justified in the 1st, 2nd, or 3rd month following the month covered by the survey. As showed by calculations, over the time of holding the surveys the accuracy of enterprises' forecasts has undergone certain changes. The comparison of the forecasted and actual changes across all the indicators on microlevel shows that the forecasts appeared more accurate on the month that immediately followed the month covered by the survey, while the accuracy of forecasts for the 2nd and 3rd months slides by 2 and 4 points, respectively. Note that the questionnaire contains the questions on forecasts for 2-3 months. As concerns the indicators that are covered by the data both on forecasts and their further realization, it is the changes in producer prices that the enterprises succeed to predict most accurately. Considering all the surveys, the forecasts on changes in pricing would prove to be correct in 65% of cases on average. Between 1994

to 1995 and in 1997 the accuracy of these forecasts was over 70%, while during recent years it has accounted for 60%.

It is the forecasts of non-monetary kinds of demand that hold the second position in terms of accuracy: they are accurate at 64% on average, and this rate has not fluctuated substantially from year to year. The average accuracy of forecasts of changes in effective demand accounted for 55% over the 72 surveys that monitored this particular indicator. The accuracy of such forecasts tends to grow, with the best value reaching 65-66%. It is volumes of output which is the worst indicator in terms of planning and predictability: it was proved in 54% of cases, and there were no changes in the accuracy of forecasting this indicator over the time period between 1993 through 2001.

S. Tsoukhlo

The oil and gas sector

This year, the oil and gas sector maintained main positive trends in its development. Between January to August 2001 the overall oil output made up 107.4% vs. its respective period of the prior year, while the volume of primary oil processing accounted for 103.2%. The production of petroleum derivatives showed a substantial growth, too (see Table 1). During the period in question the volume of operational oil drilling grew by 15.5%, prospecting drilling – by 30.7%, and the placement

of new wells into operation – by 30.3%. The proportional weight of idle wells in the operational stock fell from 23.3% as of August 1, 2000, to 21.3% as of August 1, 2001. The intensity of oil refining remained roughly at the level noted last year – 70.5%, while there was some growth in the production of non-ethylated and high-octane gasoline: their shares in the overall output of gasoline reached 97.8% and 44.6%, respectively.

TABLE 1. PRODUCTION OF OIL, PETROLEUM DERIVATIVES AND NATURAL GAS, AS % TO THE RESPECTIVE PERIOD OF THE PRIOR YEAR

	1998	1999	2000	2001 January-August
Oil	99,0	100,3	105,9	107,4
Gas condensate	105,0	104,7	103,8	106,3
Primary oil processing	92,5	102,9	102,7	103,2
Gasoline	95,7	102,2	103,6	103,3
Diesel fuel	95,5	104,2	104,9	102,2
Black oil	89,0	94,8	98,3	102,7
Natural gas, bln. cub.m.	103,8	99,7	98,5	97,9
Oil gas, bln. cub.m.	99,1	103,2	102,5	101,5

Source: Goskomstat RF

This year, the domestic oil prices in USD equivalent stabilized at the level of USD 55-56/t., while the prices for gasoline and black oil slid notably against their maximum value noted in late 2000, while the gas prices have climbed up

substantially over recent months. However the prices for gas and black oil still remain substantially lower than those in the pre-crisis level (Table 2, Fig.1)

TABLE 2. THE DOMESTIC PRICES FOR OIL, PETROLEUM DERIVATIVES AND NATURAL GAS IN USD EQUIVALENT (AS ENTERPRISES' AVERAGE WHOLESALE PRICES, USD/T.)

	1997 December	1998. December	1999 December	2000 December	2001 July
Oil	63,1	16,4	37,0	54,9	55,4
Gasoline	169,6	63,4	171,9	199,3	170,0
Diesel fuel	170,0	52,9	125,0	185,0	184,1
Black oil	73,8	22,0	46,1	79,7	52,6
Gas, USD/tcm	6,6	2,2	2,2	3,1	4,9

Source: calculated on the basis of the data of Goskomstat

Between January to June 2001 Russian oil exports grew by 9.2% compared with their respective period of the prior year, while the export of petroleum derivatives demonstrated a 1.5% growth. In the 1st half 2001, the proportion of export in the commodity stock of diesel fuel accounted for 50.4% , black oil- 19.1%, and gasoline- 13.7%. The growth in physical volume of the exports allowed some compensation for the slight fall in world oil prices compared with the prior year. In the first half 2001, Russia's oil exports in value equivalent accounted for 105.4% compared with their respective period of the prior year (Fig.2), while there was a notable fall in gas exports (at 13% compared with the first half of the prior year) which can be attributed chiefly to a considerable drop in Russian oil supplies to the CIS countries (at 31.5%).

In contrast to the period between 1999 to 2000, with their characteristic feature being a significant decrease in the import of petroleum derivatives, this year demonstrated a growth in the import of gasoline and diesel fuel. At the same time the proportion of imports in the overall stock of oil products remains fairly low (0.6% by gasoline and 0.3% - by diesel fuel).

The current financial state of the national oil sector is characterized by the maintenance of the oil companies' high level of export proceeds and profit and a further decrease in the level of their credit liabilities. By late June the oil sector's outstanding debts to the budgets of all levels in USD equivalent fell to the value of USD 0.23 bln. being minimal over recent years. (Table 3).

TABLE 3. THE FINANCIAL INDICES OF THE OIL SECTOR BETWEEN 1997 TO 2001, AS USD BLN.

	1997	1998	1999	2000	2001 1st half
Proceeds from export of oil and petroleum derivatives	21,09	13,96	18,82	34,89	16,96
Profit (balance financial result)	3,52	0,60	6,32	10,42	4,37
Outstanding credit liability (as of the end of the period)	6,79	2,41	1,61	1,35	1,24
Including to the budget	2,53	0,66	0,43	0,27	0,23

Source: calculated on the basis of the data of Goskomstat of RF

The growth in output of and investment in the national oil sector noted over 2000 to 2001 can be attributed to the high level of world oil prices and the growth in domestic demand. According to the basic scenario designed by the US Department of Energy published in early September, the world oil price calculated as an average price for the US oil import should account for USD 24.66/barrel in 2002, or roughly should remain unchanged. The Economic Intelligence Unit produced the analogous report, too.

At the same time, as long as the time period following 2002 is concerned, the leading

international expert institutions forecast a notable downfall in the world oil prices: according to the basic scenario of the US Department of Energy, in 2005 they should make up roughly USD 20.83/b. (given that the high price margin variant should make up USD 26.04/b/, while the lower one- USD 15.10/b. Such a forecast is complemented by close price estimations of the International Energy Agency (USD 19.83/b.) and Standard & Poor's Platt's (19.47)

The latest developments in the US, however, have introduced a great deal of uncertainty in the aforementioned estimates. At the 117th Session of

OPEC held in late September the nation members have confirmed their intention to retain the oil prices within the earlier established price corridor of USD 22 to 28/b. Considering the fact that OPEC has been rather successful in maintaining the noted price margins, one should expect that should the Organization retain its current oil price policy, the oil prices should not leave the set price corridor, at least in the short run, and even if they leave that, it should happen just occasionally.

However under present conditions one cannot exclude that the US would effectively press the OPEC nations to retain a higher level of oil output and, consequently, to ensure lower world oil prices. In addition, a long-lasting maintenance of high prices for oil entails a growth in output in other oil-producing countries that do not hold membership in OPEC, which may lead to OPEC changing its price guidelines and shifting of the set price corridor margins towards smaller prices.

FIG.1

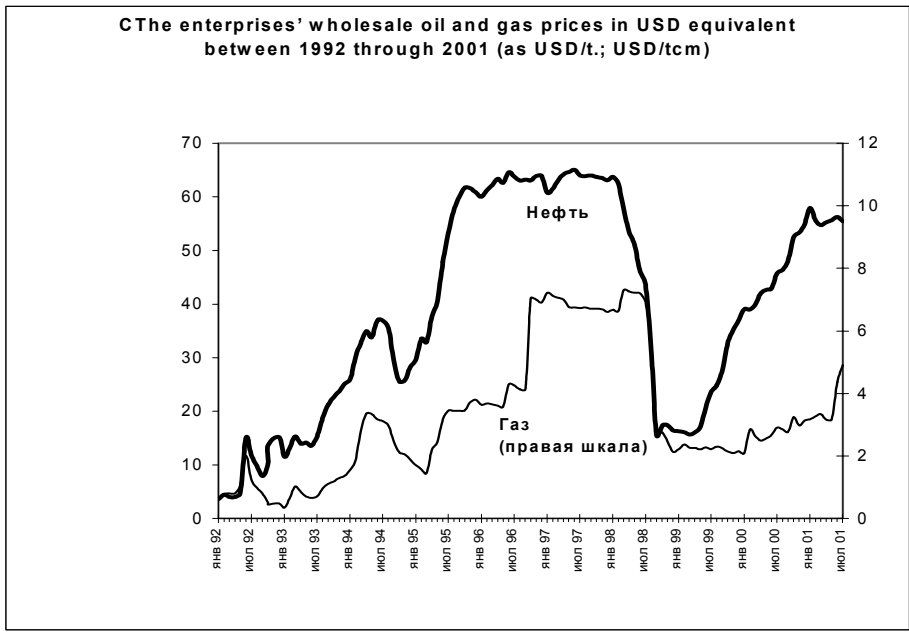
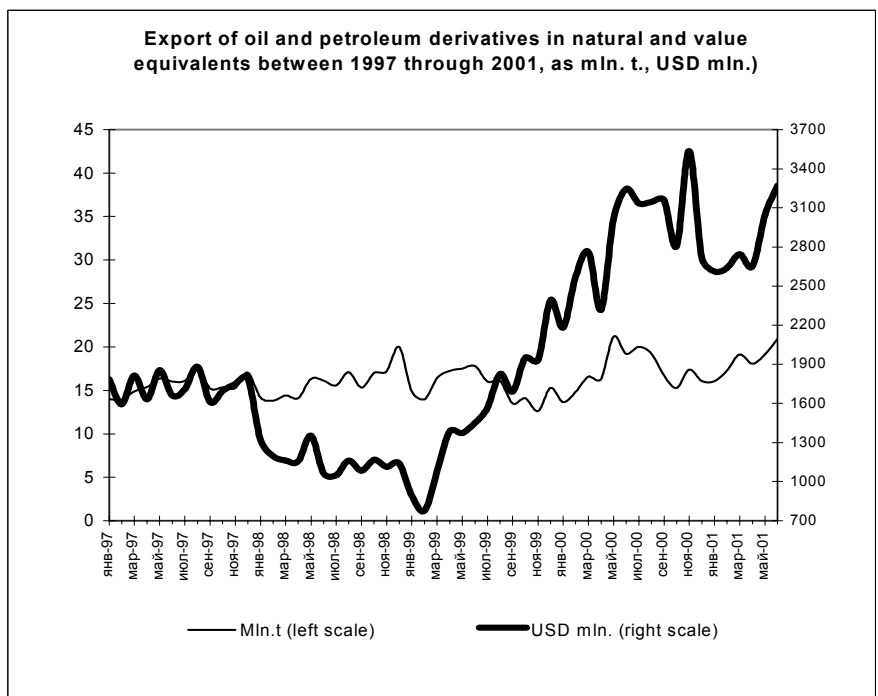


FIG.2



Yu. Bobilev

Russian Agrifood Sector in 6 months 2001

In the first half of 2001 growth in the Russian agricultural production continued. In January-July its index exceeded 106% (in 1999 the annual growth rate amounted to 4% while in 2000 - to 7%). The major contributor to this growth was crop production that in July (after the harvesting began) was up 14%. Favourable weather conditions have surely been an important but not the single factor thereof. The food production index in 6 months 2001 equalled 107.2% (107.1% in 2000).

In 2001 the crop structure of cultivated lands changed: larger areas were planted in grains and smaller - in sunflower. This is a natural result of higher grain profitability. The introduction of tariff quotas on raw sugar import didn't help to enlarge sugar beets plantings.

This year the grain crop will be larger than that of 2000: experts' estimates range from 78 to 80 million tons including 40 million tons of wheat. This volume is below the 1991-1995 average gross output but fully covers the country's demand for grain. According to the traditional balance about 5 million tons can potentially be sold to foreign buyers but experts fear that poor development of export and transport infrastructure (sea ports capacities, shortage of railroad cars, etc.) will constrain sales.

Despite all the government efforts to support sugar beets production, its volume is falling largely due to smaller planted areas.

Weather conditions favour harvesting of almost all crops. It progresses at a higher rate than in the previous year and this fact *ceteris paribus* can lead to larger gross output.

Livestock and poultry production performance is far less successful. Cattle and pig numbers continue to decrease even faster than in the previous year. Number of poultry grew by about 4% while that of sheep - only to a minor degree. The output of basic livestock products in 7 months 2001 remained at actually the same level. As marketing grows at a higher rate than production, one can assume that greater share of output is marketed while barter and shadow turnover are losing ground. Livestock productivity grows in line with decreasing number of animals.

Agricultural enterprises are the major contributors to growth in livestock and poultry production. Private farmers' engagement therein is minor while household farming is shrinking as economy

stabilizes. As a result the share of household plots in the gross agricultural output decreases.

Food industry continues to grow by somewhat over 7% for the third year round. Trends in production of selected food products change (Table 4). The production of sugar and vegetable oils fell after being record high in 2000. This drop can be a response to overproduction witnessing the still persisting extreme reaction of agrifood producers to market fluctuations. Besides, the drop is due to smaller areas planted in sunflower and sugar beets.

Production of basic meat and milk products continues to grow, and its pre-crisis⁴ level has been restored. Good grains crop triggered growth in flour and groats industry that was declining a year ago.

The growth in agricultural inputs production became slower and tractor building even dropped. This is a sign of shorter agrarian sector's demand for domestic inputs. There are several reasons for that. First, in 2001 the system of federal leasing was reorganized and purchases of agricultural machinery were notably reduced. Second, domestic agricultural machine building began to lose its price advantage over Western machinery, the import of which respectively grew. Besides, large external investors in the agrarian sector prefer imported machinery and equipment, have financial resources for buying it and don't need state leasing. The share of such vertically integrated agrarian holdings in the Russian agriculture steadily grows. Accordingly, the demand for domestic agricultural machinery declines. The post-devaluation price gap was not sufficient for reorganizing this sector as well as others.

The situation on domestic agrifood market was determined by higher population's real incomes and import trends. In the first half of the year incomes rose by 5.4%. However, growth of food expenditures was constrained by notably bigger spendings on services that were due to the reform of housing and communal services initiated in some of the country's regions (the share of services in the total population's expenditures more than doubled).

Higher population's incomes enlarged food consumption. In 7 months 2001 the turnover of retail food trade was up 6.9%, of food service - 7.9%. The growth of incomes resulted in bigger

⁴ August 1998 financial crisis.

demand for such income elastic items as meat and milk products whose consumption almost attained the pre-crisis level.

Meanwhile, larger supplies of home-produced meat and milk to the domestic market fail to cover demand. As a result import of these products grew and in the first half of 2001 nearly regained the pre-crisis volumes. So, in these two aggregated market segments the domestic agrifood sector failed to benefit from the competitive advantage it gained after the ruble devaluation.

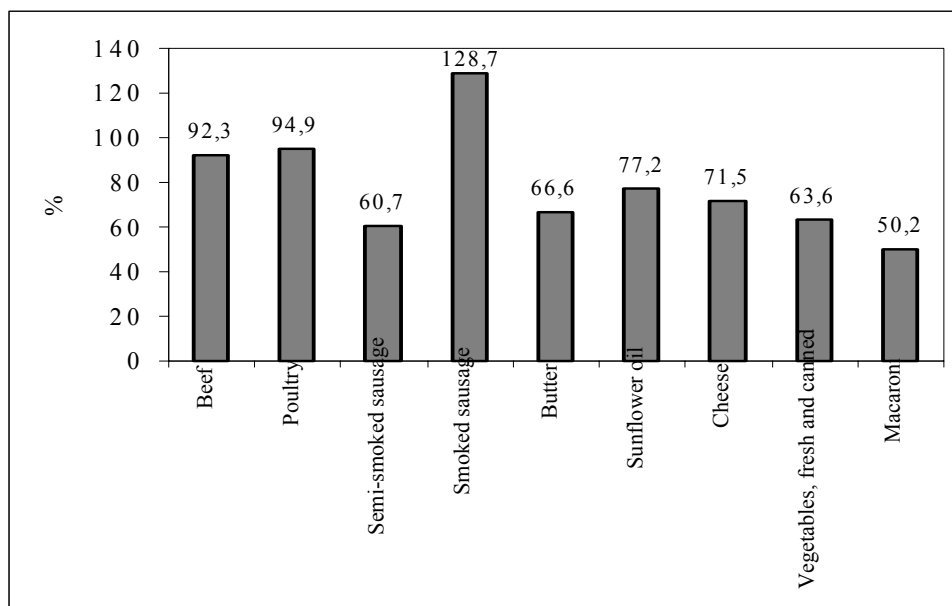
Despite the introduced restrictions on raw sugar import, the domestic sugar market remains saturated. The quota tender resulted in the reduction of raw sugar imports by 14.5%. Still, the price for sugar powder in 7 months 2001 actually didn't change (as compared to the 40% rise during the same period last year). The retail price for sugar didn't grow as well even in the months of peak demand (July-August). This is an evidence of large volumes of ending stocks that in 2001 are more than 1/3 over the 2000 level. Besides, an inaccurate foreign trade regulation of sugar

segment failed to prevent a sharp increase of white sugar imports in January-March that also contributed to the market over-saturation.

Situation on the grain market in the first half of the year was determined by the volume of ending stocks and the envisaged state interventions. During 7 months 2001 grain prices' growth equalled inflation rate. The expected good crop will pull prices down. At the same time, the announced state purchase interventions induce producers to hold grain back and thus constrain price drop. The growth of prices for food products manufactured out of grain (bread and bread products, groats, flour) during the examined period was far below the inflation rate. It can be explained by, first, regional regulation of prices for bread, and, second, by the fact that prices grew primarily for coarse grains.

The gap between prices for some domestic and imported products (i.e. meat and milk products) still persists to the benefit of domestic producers. However, it rapidly shrinks (Picture 1).

PICTURE 1. AVERAGE CONSUMER PRICES FOR SELECTED DOMESTIC PRODUCTS AS % OF PRICES FOR IMPORTED PRODUCTS, JUNE 2001



Source: Data of the RF State Committee for Statistics.

In the first half of 2001 the growth of some foods import that started in the previous year continued. The volumes of some items' import during the 6 months already exceed the 1999 and 2000 annual indicators though the 1997 record has not yet been attained.

The major contributors to import growth are meat, fish, butter and cacao products. The supplies of sunflower oil, citrus fruits, alcoholic and alcohol-free beverages grew less importantly (Table 1).

TABLE 1. IMPORT OF BASIC FOOD PRODUCTS IN 6 MONTHS 2001 AS COMPARED TO 6 MONTHS 2000, %

	Total	From the CIS countries	From the non-CIS countries
Red meat, fresh and frozen	2.1 fold	104.4	2.7 fold
Poultry meat	3.1 fold	n.a.	3.3 fold
Canned meat and meat products	87.3	62.8	137.6
Fish, fresh and frozen	2.1 fold	123.8	2.3 fold
Condensed milk and cream	99.7	n.a.	n.a.
Butter	3.2 fold	3.3 fold	3.1 fold
Sunflower oil	128.8	138.1	111.6
Raw sugar	85.5	n.a.	n.a.
White sugar	87.7	35.9	n.a.
Food grains	35.3	37.6	31.6
Cacao products	2.0 fold	2.5 fold	122.8
Coffee	98.9	n.a.	n.a.
Tea	94.2	80.7	94.7
Citrus fruits	105.7	n.a.	102.2
Alcoholic and alcohol-free beverages	138.6	142.3	132.4

Source: Data of the RF State Committee for Statistics.

Meat and poultry imports were rapidly restoring after the lifting of restrictions thereon connected with the unfavourable veterinary situation in some countries. Besides, duties on different poultry items were unified and the number of border customhouses through which they could be imported was restricted. As a result some part of poultry supplies could come out of shadow and thus elevate the statistically recorded imports.

While the import of livestock products in the first half of 2001 grew, that of grains, raw and white sugar noticeably fell.

The agriculture's financial performance was determined by the positive development trend in the past two years and the start of restructuring debts to the budget. Some segments of the agrarian sector became quite profitable (e.g. the profitability of grains in some regions amounts to 400%). Together with the substantial tax privileges it makes agriculture attractive for investors. Capital comes from external industries, e.g. fuel and energy. Vertical holdings continue to develop in the sector. Adoption of the new Land Code will

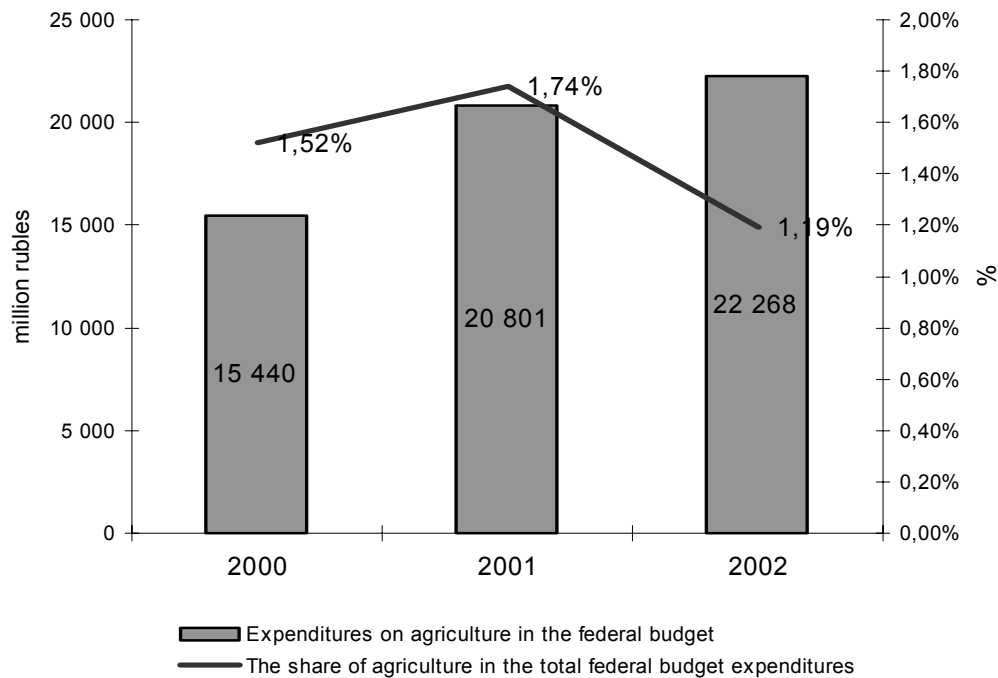
intensify this process and encourage further inflow of capital to agriculture in the near future.

In the first half of 2001 direct foreign investments in the primary agricultural production grew by 1/3 (i.e. by 5 million dollars). The major part of them came from Panama being actually a repatriation of Russian-origin capital rather than real foreign investments.

It's difficult to estimate agriculture's profits reinvestment in the first half of the year as due to the seasonal nature of production the bulk of investments is made after the crop is sold. But the initiated restructuring of debts with requirements to fulfil can make agricultural producers' budgets very tight and entail a cut of their investments in fixed capital.

Nominal budget outlays for the agrarian sector grow since 1999. However, in 2001 their share in the total federal expenditures fell (Picture 2). The share of agrifood sector in the consolidated budget shrank as well - from 2.75% to 2.13%. At the same time the contribution of federal budget to the sector's financing increased from 22% to 28%.

PICTURE 2. EXPENDITURES FOR AGRICULTURE IN THE FEDERAL BUDGET



Federal budget execution in the agrarian sector is only about 75% which is the lowest indicator in the first half of the year. Subsidies were financed much better - over 84%. In 2001 actually all subsidies to crop and livestock producers were preserved. We find that most of them are inefficient. Meantime, these items are the best financed ones. In the first half of the year the largest federal budget funds were allotted to the compensation of agricultural producers' spendings on purchase of mineral fertilizers, pesticides and elite seeds, and on soil fertility improvement (melioration). We continuously stress that compensation of expenses on mineral fertilizers has no radical effect and in the last season their application even dropped as compared to the previous year. Moreover, budget funds are still used to compensate the agricultural producers' spendings on seeds of grains and oilseeds despite their being the most profitable crops. The reasons for that are very doubtful since the marginal product in grains and oilseeds production fully covers marginal cost of purchasing elite seeds and thus producers are quite able to pay for them themselves.

Almost 1/3 of federal budget outlays for spring field works (1.7 billion rubles) was used to "render financial assistance on request in the form of interest-free budget subsidies intended to cover cash gaps in executing budgets of constituent

members of the Russian Federation⁵". These budget subsidies are not envisaged in the 2001 Federal Budget Law and actually continue the notorious practice of budget credits to agriculture known since 1992-1994. Then it resulted in building up of bad debts in the sector, financial irresponsibility of producers and corruption in the administrative bodies.

Agrifood sector's performance in 2001 will still be good, but already the next year will be much harder. First, given the current trends the effect of import substitution will be completely exhausted and it will become clear what Russian products have real comparative advantages on the world market. Second, the initiated restructuring of debts will induce a wave of bankruptcies in agriculture. The clearing of the sector of inefficient producers will eventually bring positive results. But at the initial stage it will rather entail production drop. Besides, the lack of more or less sound rural development policies is likely to increase social tension in regions where many agricultural producers go bankrupt.

The structure of agricultural production will shift to large holdings while household farming will gradually become less important as macroeconomic situation improves. The progress of vertical integration will imply capital inflow in

⁵ Data of the RF Ministry of Agriculture: <http://aris.ru>.

the agrifood sector although in the near future nominal investments in the primary production won't be large. Restructuring of agriculture's debts can lead to a somewhat deeper involvement of banks in financing the sector and a wider spread of financial leasing.

Despite the progress of negotiations on Russia's acceptance to WTO, the agrarian protectionism will strengthen. Due to errors in market regulation additional corrective practices will be introduced rather than inefficient ones will be discontinued. Thus, Russia can get into "a vicious circle of protectionism".

APPENDIX

TABLE 2. AREAS PLANTED IN BASIC AGRICULTURAL CROPS

	1995	1996	1997	1998	1999	2000	2001
Grains	54.7	53.4	53.6	50.8	46.8	45.9	47.6
Sunflower	4.1	3.9	3.6	4.1	5.5	4.6	3.8
Sugar beets	1.1	1.1	0.9	0.8	0.9	0.8	0.8
Potatoes	3.4	3.4	3.4	3.3	3.3	3.2	3.3
Vegetables	0.8	0.7	0.7	0.7	0.8	0.8	0.8

Source: Social and Economic Situation in Russia, corresponding years.

TABLE 3. TOTAL PRODUCTION AND MARKETING OF BASIC LIVESTOCK PRODUCTS IN JANUARY-JULY AS % OF THE CORRESPONDING PERIOD PREVIOUS YEAR

	1998		1999		2000		2001	
	Prod-n	Mark-ng	Prod-n	Mark-ng	Prod-n	Mark-ng	Prod-n	Mark-ng
Livestock and poultry for slaughter, live weight	94.4	92.6	92.1	87.5	102.9	103.6	99.3	100.2
Milk	98.4	100.4	95.5	97.1	99.7	99.2	100.9	103.1
Eggs, billion pieces	104.2	108.0	98.3	99.3	103.6	105.3	101.4	100.5

Source: Social and Economic Situation in Russia, corresponding years, January-July.

TABLE 4. PRODUCTION OF BASIC FOOD PRODUCTS IN JANUARY-JULY AS % OF THE CORRESPONDING PERIOD PREVIOUS YEAR

	1998	1999	2000	2001
Meat	96.4	87.9	112.9	110.3
Sausage	90.5	88.8	114.0	109.8
Butter	94.7	90.1	103.7	104.7
Whole milk products	105.2	100.1	110.5	107.6
Vegetable oils	2.0 fold	120.1	2.0 fold	95.6
Sugar	109.5	136.7	92.7	95.8
Flour	95.3	104.8	97.9	100.2
Groats	100.2	80.4	100.1	128.5
Macaroni	97.0	146.8	97.6	107.5
Margarine	84.0	24.5	12.3	115.5
Canned meat	n.a.	160.5	85.9	99.7

Source: Social and Economic Situation in Russia, corresponding years, January-July.

TABLE 5. PRODUCTION OF AGRICULTURAL INPUTS IN JANUARY-JULY AS % OF THE CORRESPONDING PERIOD PREVIOUS YEAR

	1998	1999	2000	2001
Tractors	78.0	137.9	146.1	80.5
Tractor ploughs	n.a.	75.2	162.9	121.1
Tractor seeders	n.a.	172.6	180.4	124.6
Tractor cultivators	n.a.	65.3	188.8	114.3
Grain harvesters	103.5	131.4	2.5 fold	2.0 fold
Tractor mowers	n.a.	121.6	99.2	64.2
Mineral fertilizers	98.6	123.0	109.9	104.2

Source: Social and Economic Situation in Russia, corresponding years, January-July.

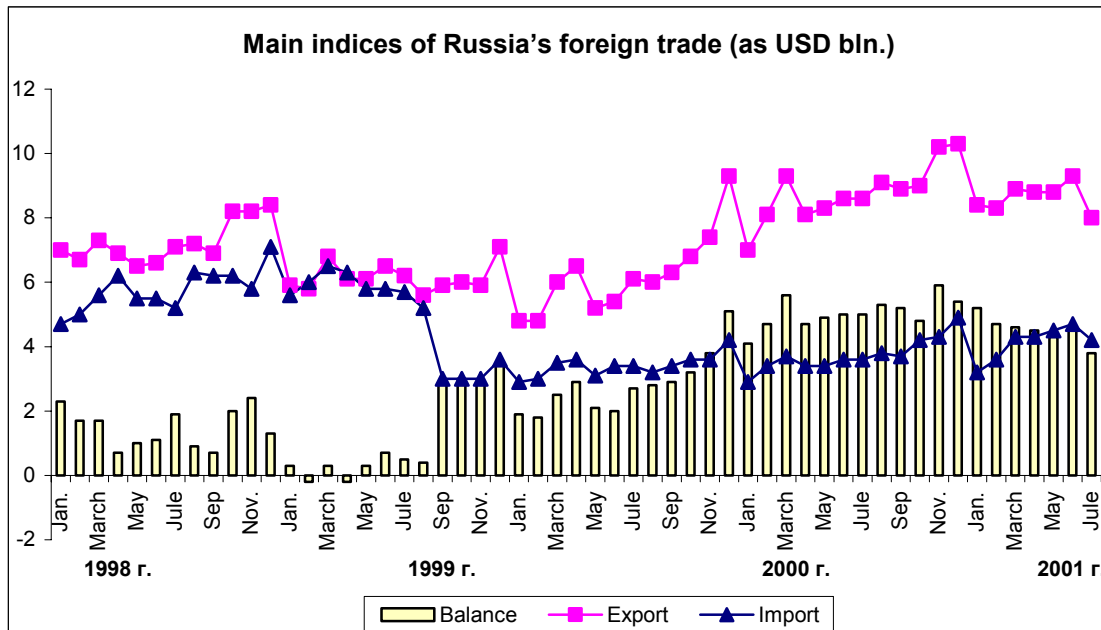
*E.Serova, I.Khramova, N.Karlova,
O.Shick, T.Tikhonova*

Foreign trade

In July 2001 Russia's foreign trade turnover dropped by 12.1% compared to the prior month and accounted for USD 12/2 bln. When compared to its respective period of the prior year, the foreign trade remained practically unchanged. Its growth accounted just for 0.6% which became the lowest rate over the past two years. Russia exports made up USD 8.0 bln. vs. 8.6 bln. reported in July

2000 (i.e. fell by 6.8%) while imports accounted for USD 4.2 bln. vs. 3.6 bln. registered in July 2000 (a 18.3% growth). Because of the decline in exports and imports, the balance of Russia's foreign trade slid to USD 3.8 bln., which also became the lowest value noted over the past two years.

FIG. 1



In July, the trend emerged to downfall in world oil prices – the average price for Brent accounted for USD 24.6/barrel (down at 11.5% compared with June), while Urals was quoted for USD 23/b. (down at 10.2%). The main reason for such a downfall is the recession noted in the major world economies, which traditionally is accompanied with lower oil consumption. In addition, the oil price fall was caused by the Iraq's decision to renew its oil supplies to the world market and the growth in oil and oil products stock in the US> In view of that, in late July the OPEC members made a decision on contracting the oil output by 1 mln. barrel daily since September 1, to maintain the price corridor within USD 22 to 28/b. Thus, between January through July 2001 the average

monthly price for Brent made up USD 26.3/b. (down at 3.3% against the respective period of the prior year), while Urals- USD 24.4% (- 6.2%). The situation in the world market for petroleum derivatives generally followed the one noted in the market for crude oil. At the same time, during the period in question the contracting price for the Russian natural gas supplies grew by 44.7%, however July showed the trend to its decline.

The world markets for ferrous metals were rather stable over the period concerned, with price fluctuations being insignificant. Between January to July 2001 the main non-ferrous markets were dominated by a bullsih trend induced by a low consumer demand

TABLE 1 THE AVERAGE WORLD PRICES IN MAY OF THE RESPECTIVE YEAR

	1996	1997	1998	1999	2000	2001
Oil (brent), USD/t	20,66	18,25	12,96	18,8	28,4	24,62
Natural gas, USD/mln.m ³	-	2,121	1,983	2,363	4,01	3,15
Petrol, USD/t	0,6338	0,5941	0,4234	0,6002	0,935	0,732
Copper USD/t	1935,9	2481,7	1754,3	1744,8	1864,2	1541,4
Aluminum, USD/t	1455,4	1563,7	1377,7	1403,5	1565,9	1412,2
Nickel, USD/t.	7350	6737,3	4620	5273	8202,0	5956,8

Since October 1, 2001, the new import customs duty rates approximately on 400 commodity positions have been introduced for the term of 9 months. In addition, the duty rates on almost 3.5 thousand goods lowered and unified as of January 1, 2001, will remain effective. It should be noted that the lowering and unification of import duty rates has encouraged the reduction in violations of the customs procedures and the transition of an increasing number of economic agents towards the legal sphere.

Whilst changing the import duty rates, the RF Government was willing to encourage an activation of the importation of technological equipment to Russia. It is a very urgent issue due to high deterioration rates of the production equipment noted at the majority of national enterprises. That is why the duty rates on the whole range of technological equipment were decreased, and on some kinds of that, particularly, the equipment not produced in the country and needed for technical modernization of domestic enterprises, the rates were lowered from 10-15% to 5-10%. The process of customs duty rates unification also covered paper, colorings, chemicals, machine-engineering equipment. In the past, different kinds of these goods were subject to rather a broad range of duties – between 5 to 15%, - which provoked indecent importers' fraudulent operations.

As well, the unified the duty rates on microchips, transistors, resistors and other element base components that previously were fluctuating within the range of 5 to 20%, while at present they have become subject to a single 10% rate. All the aforementioned decisions were made on the basis of a monitoring of changes in the domestic market for commodity goods since 2001. The monitoring showed that the introduction of the new rates has had a positive impact on the dynamics of import supplies and the collection of customs duties. According to the customs statistics, over 8 months of 2001 the customs authorities collected to the

federal budget Rb. 336.96 bln. in customs duties vs. 220.44 bln. reported over the same period of the prior year.

Before addressing the customs tariff system reform, the Russian authorities took into account both foreign and domestic experiences, which witnesses that high rates become efficient only if a government intends to limit the importation of a number of goods. However, if nowadays the mission is to increase the customs duty collection, such high rates are not effective, because they entail abuse and fraudulence and, finally, lead to a contraction in the amount of customs collection.

In order to protect national producers, since January 2002 the customs import duty on unrefined sugar should make up 40% of its customs value, but not less than Euro 0.12/kg., while the one on refined sugar should become 40%, too, but not less than Euro 0.14/kg. The noted seasonal import duty on unrefined sugar should be introduced for the period between July 1 through December 31 and would make up 50% of the product's customs value, but not less than Euro 0.15/kg, while the one for refined sugar should be 50%, too, but not less than Euro 0.18/kg.

As concerns the trade with the CIS countries, in July the respective export supplies remained at the average level reported over this year and accounted for USD 1.1 bln. which exceeds the analogous average annual level at 9.5%.

As to import supplies from the CIS countries to Russia, for the first time since early 2001 there has been noted a trend to their contraction, and in July the respective volumes accounted for USD 0.9 bln, or at 14.1% less than their respective index of the prior year.

Notably, the physical volumes of import supplies from the CIS countries fell significantly, while the average contracting prices for their imports grew by 12%.

N. Volovik, N. Leonova