

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
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Politico-economical developments of October 2004

After “pregnant” September there was some calm in October 2004.

Expectations proved true of further escalation of tension at the Northern Caucasia. This time tragic events took place in the Karachayev-Cherkessian Republic. In fact, as compared to other Northern Caucasia republics, this region, which switched to direct head elections only in 1999, and elected (and reelected him, in 2003) in an atmosphere far from being quiet, was traditionally known for its weak regional power – not least because of strong confrontation of both national elites of Karachais and Circassians and their allied abasins, and also because of confrontation within Karachai community. In mid-October, a group of entrepreneurs disappeared which, together with regional deputy R. Bogatyrev, gathered for commercial talk at the President’s son-in-law’s cottage. The reaction of discontented was severe: calling for justice, the relatives of those lost captured the Government Building. As a result of the negotiations with participation of D. Kozak, M. Batyev had disavow his son-in-law, and the latter – surrendered to law bodies, following which, the Government Building was cleared and situation somewhat relieved. It should be said that (apart from Chechnya) this is, in fact, the third for the passed months more or less successful opposition actions at the Northern Caucasia. Most probable, the increased role of power methods will become evident with time in dialogue with official authorities, and as in the case considered, – without any sign of “international terrorism”.

The initiative of A. Veshnyakov on switching to a well-balanced voting system, which was originally presented in August in an analytical note, received further development. For this period of time, some changes have been introduced in a number of provisions of this document, and commentaries made by some members of the Central Electoral Commission and by its head. Moreover, last week, on the eve of Parliamentary hearings, Veshnyakov addressed with new initiatives he never mentioned before. Even so, no final wording of the draft law is available so far, though, the general trend, first mentioned even in August initiatives is obvious - to liquidate elections as a clear democratic procedure. Promise has been given to correct in some way an absurd idea of the priority of a relative number of voters, in regional groups, over the absolute¹, but how – is not yet clear. It has been announced of possibility of recalling a deputy upon the court order on such an unformalized pretext as “failure to perform duties before citizens”, or introducing an imperative mandate confining a deputy to a faction from which he is elected. It is indicative that the institutes of such kind are absent even in Belarus and are purely an example of “socialist parliamentarism” in the spirit of Cuba or Vietnam. It is offered that TV air channels be distributed among the parties based on their popularity data provided by three sociological services. An intention is confirmed to deprive poll-watchers of the right to make duplicates of minutes of the election commission, but, noble calls are not heard any more in declarations of officials to lower parliamentary barriers to 5% at a federal or even regional level.

Representatives of the “United Russia”, LDPR and “Rodina” introduced draft laws to the State Duma raising the demands for size of a political party from presently existing 10 to 50 thousand. It is interesting that just communists refused to support that demand, though of all today’s parties it is they who, alongside with the ruling parties, have better chance to match the criteria. Also interesting is the fact that, not wishing, apparently, to declare inadequate strength, being absolutely justified, though, in atmosphere of total distrust to the institute of political parties, the Russian political parties do not protest against the “United Russia”’s initiative which, undoubtedly will allow to exist only loyal for authorities parties .

It is likely that proposals to reform the electoral and party legislation will be corrected under the pressure of Russian and the World’s public opinion, as it was the case with the draft law of actual prohibition of mass actions. Another variant is also not excluded – such novelties stimulate opposition’s grouping for the sake of their own survival, which, again, may be considered as improper action.

The electoral cycle into the regional law enforcement bodies (The Tula, Chita, Sakhalin, Irkutsk regions, and Mariy-El), occurred in late September, gives some reason for party trends’ analysis.

¹ One should bear in his mind, even if secured 10% in multimillion Moscow, the party regional group concedes to that having 10.1%, despite the fact it is the Evenk Autonomous District with a population of less than 20000.

So, the “United Russia”’s indicators decreased everywhere, though considerably – only in the Sakhalin (30.13% - 17.7%) and Tula (29.86% - 22.31%) regions. In the four of five regions (except for Sakhalin) it occupied the first place. “Rodina” blocs also showed themselves reasonably good – a victory in Sakhalin (20.4%), almost the same number of votes collected D.Rogozin and S.Glaziev blocs in Tula. It is surprising that the lowest (9,06%) results were demonstrated by “Rodina” in Irkutsk – where it showed itself as federal political force unit. Communists slightly improved their positions (the highest result is Chita – 18.46%), the Right Forces Union showed a little above 6% in the Tula region, in alliance with populists the regional bloc was a success in Irkutsk (6.9%), but failed – in Sakhalin. In several locations (Chita, Sakhalin, Mariy-El) LDPR made a “step over the barrier”, but could not do it in the two other regions. “Yabloko” failed (or did not participate) everywhere. But crossing over the barrier by the Russian Pensioners Party in the four regions (with 12% of votes in Mariy-El) was a real wonder, in three regions the land-owning parties were elected to the Parliament, in fact, which actually played their the role of a reserve "ruling party".

The results of the regional elections show that, as before, pseudo parties are being called for. Though, in the absence of informational pressing of the federal TV channels, the chances are almost equal for communists and the “United Russia”. Both parties reliably achieved their parliamentary status.

When talking about regions, it should be noted that cases are observed of either rejecting the presidential initiatives by legislatures or amending them radically (Kaliningrad, Chuvashia, Primorije, Astrakhan).

Both chambers of the Russian Parliament predictably ratified Kyoto Protocol. So, the opponents of its approval, even with Fradkov’s support, could not either change or put off anything. Such step may be considered as potential approaching to WTO accession.

All remains uncertain about the future of seized (from Yukos) Yuganskneftegaz, or Gazprom. As concerns Yuganskneftegaz, juridically, the situation came to a deadlock caused by the decisions unprecedented for the jury system. No doubt that enactment of any decision taken by the Russian authorities will again damage its prestige, especially if the burden of evidence of a purchaser’s good faith and selling conditions is not placed on a large foreign company (for example, Exxon Mobile).

Sergey Zhavoronkov

On the Progress of Reforms in September and October of 2004

Contrary to expectations, in the autumn there was not observed an acceleration of reforms. All problems mentioned in the preceding survey still remain actual issues. The new medium term program is in the process of elaboration. The budget reports are still being discussed. As concerns economic news, the most important development is a smooth passing (as yet) of the budget for the next year, which is characterized by a radically increased component relating to armed forces and law enforcement agencies, in the State Duma. The economic scandal of the two last months was the false start of the reform of science, while the non-economic scandal was the introduction of “quasi-electivity” of regional authorities.

The first two months of the autumn have demonstrated that the Government, which is still stuck with the first stage of the administrative reform, could not regain its breath and turn to work yet. Judging by the procedures, under which the new Government operates, the restructuring of the system of executive authorities has not resulted in less red tape. However, at present the center of gravity of red tape shifted to the level of Ministries. It is already clear that the requirement to limit the number of Deputy Ministers posts to two per Minister is a “bottleneck,” since the planned measure to grant a higher real status of directors of departments has not been implemented yet, while the volume of documentary turnover remains at the same level contrary to expectations. Deputy Ministers became machines for signing documents, since they practically do not have time for substantive work on any issues.

In this situation, the most dangerous development would be if the Government begins to intensively adapt to the present situation in stead of taking next steps (and there are still very many such steps to take) in the sphere of administrative reform. No doubt, such a development will negatively affect not only the process of reforms, but the substantive work of the state authorities on the whole.

The outlines of the new medium term program of the Government elaborated by the RF Ministry of Economic Development and Trade became more clear. It still remains liberal and in comparison with the preceding program there have been introduced a number of important positive changes. In the new program, there have been incorporated sections concerning poverty reduction, support of institutions of the civil society, as well as provisions concerning the improvement of functioning of the judicial system and law enforcement agencies, which directly affects economic processes.

Unfortunately, it seems most probable that the version of the program existing at present will be subjected to significant changes in the process of passing of the document through several circles of approval on the part of the Ministries. Judging by the proposals presented by the Ministries, these changes may be rather significant. Therefore, it would be of interest to compare the original version of the program and its version approved as the final regulatory document.

A certain, although not significant, progress was observed with respect to the process of preparation and discussion of budget reports. Some of ideologists of performance budgeting in its Russian version began to understand that this type of budgeting is a more complex task than it seemed earlier. As it turned out, it is sometimes impossible to build a clear hierarchy of objectives: from work of each official to the twofold increase in GDP. At the moment, the work in this sphere seems to slow down somewhat; however this slowdown, in contradistinction to other reforms, is rather a positive than a negative factor. As concerns the intensity of work in this area, there may be mentioned the start of substantive discussion of the performance indicators of the block of armed and law enforcement agencies, what is especially important in the situation, where the amount of funds allocated for financing of these agencies is significantly increased. As the society is required to spend much more than before for defense and security, it would be not bad to know, what it receives in return.

As concerns not very pleasant news of September and October, there may be mentioned the scandal related to the preliminary draft of the Concept of state participation in scientific organizations elaborated by the Ministry of Science. The document, due to its preliminary nature, contained too many controversial provisions to be put for a public discussion. It should have been subjected to a further serious elaboration to avoid the criticism of its numerous insignificant flaws as a pretext for changes of its principal stipulations.

As concerns the developments in the spheres other than economic, which could have a significant impact on the economy, there may be mentioned the initiatives related to the de facto appointment of the heads of regions and the completion of switching to the party based system of formation of the State Duma.

Both the first and the second processes are rather dangerous not only as concerns the destruction of the base of democracy created over the last years, but also from the point of view of the economy. There exists a very high probability of creation of wrong incentives in the economy at large and in particular in the sphere of public finances.

In the present situation in Russia, the system of appointment of Governors will eliminate all political competition at the regional level, what is a sure way to reduce economic efficiency of activities of regional authorities. In the situation, where the personnel policy at the top echelons is lacking, it will result in a sharp shrinking of possibilities as concerns the ability of the Center to choose adequate candidates, while the attempt to develop a centralized personnel policy would only further aggravate the situation. In reality, this initiative may result in the fact that present heads of regions will keep their offices for an indefinite period of time on condition of personal loyalty to the Center, and not as a result of the effectiveness of their activities.

As concerns the documents reviewed in earlier surveys (in particular, the Forest and Water Codes, the law on mineral wealth), they remain in the same situation: the two former documents have not been submitted to the State Duma as yet. At the same time, the law on mineral wealth, although it is already in the public space, has not acquired the form of a bill and become the subject of a broad discussion yet.

O. V. Fomichev

Budgetary and Fiscal Policy

By the end of September of 2004, the level of revenues of the RF federal budget declined by 0.6 p. p. of GDP in comparison with the figures registered in the preceding month and made 20.0 per cent of

GDP. The level of expenditures of the federal budget increased by 0.1 p. p. in comparison with the figures registered last month and made 15.9 per cent of GDP by October 1, 2004. In January through August of 2004, the revenues of the RF consolidated budget made about 32.9 per cent of GDP, while the expenditures of the RF consolidated budget over the respective period made 26.9 per cent of GDP.

On October 12, the RF Government approved the amendments to the federal budget for year 2004, in accordance with which the revenues of the budget were increased by Rub. 531 billion and made Rub. 3273.8 billion, while the expenditures were raised by Rub. 108.6 billion up to Rub. 2768.1 billion.

The State of the Federal Budget

In January through August of 2004, the revenues of the federal budget (cash execution) made 20.6 per cent of GDP, while expenditures made 15.9 per cent of GDP (see Table 1). Therefore, the federal budget surplus made 4.7 per cent of GDP.

Table 1

The monthly execution of the federal budget of the Russian Federation (in % of GDP², cash execution)

	VIII'03	IX'03	X'03	XI'03	XII'03	I'04	II'04	III'04	IV'04	V'04	VI'04	VII'04	VIII'04
Revenues	1.3%	1.3%	1.3%	1.3%	1.3%	0.9%	0.7%	1.2%	1.4%	1.3%	1.3%	1.3%	1.3%
Profit tax .	2.8%	2.7%	2.7%	2.6%	2.7%	2.2%	2.6%	2.8%	2.9%	2.9%	2.8%	2.8%	2.8%
Income tax .	6.8%	6.7%	6.6%	6.6%	6.6%	7.9%	6.6%	6.2%	6.4%	6.5%	6.3%	6.5%	6.5%
Unified social tax .	2.1%	1.9%	1.9%	1.9%	1.9%	2.3%	1.8%	1.4%	1.2%	1.1%	1.0%	0.9%	0.8%
Taxes on goods and services. License and registration dues .	3.4%	3.3%	3.3%	3.4%	3.4%	3.6%	4.2%	4.4%	4.7%	5.0%	4.9%	4.9%	5.0%
VAT	1.8%	1.8%	1.8%	1.9%	1.9%	2.4%	2.6%	2.4%	2.5%	2.5%	2.5%	2.5%	2.5%
Excise taxes	3.0%	2.9%	2.9%	2.9%	3.0%	2.3%	0.1%	0.2%	0.2%	0.1%	0.1%	1.0%	0.2%
Taxes on foreign trade and foreign economic operations .	21.1%	20.6%	20.5%	20.5%	20.7%	21.6%	18.7%	18.6%	19.3%	19.5%	19.0%	20.1%	19.1%
Other taxes .	1.5%	1.4%	1.4%	1.3%	1.3%	0.9%	0.8%	0.9%	1.0%	1.1%	1.5%	1.4%	1.4%
Tax revenues .	20.0%	19.5%	19.4%	19.3%	19.4%	20.4%	19.6%	19.7%	20.4%	20.6%	20.6%	21.6%	20.6%
Non-tax revenues .	0.4%	0.4%	0.4%	0.4%	0.5%	0.2%	0.3%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%
Total revenues .	2.6%	2.5%	2.5%	2.5%	2.7%	1.7%	2.2%	2.6%	2.9%	2.7%	2.6%	2.6%	2.5%
Expenditures	0.2%	0.2%	0.2%	0.2%	0.2%	-0.1%	0.2%	0.2%	0.3%	0.3%	0.3%	0.3%	0.3%
Public administration .	0.2%	0.2%	0.2%	0.2%	0.2%	0.1%	0.1%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
National defense .	1.7%	1.7%	1.7%	1.7%	1.9%	1.0%	1.5%	1.7%	1.9%	1.8%	1.8%	1.8%	1.8%
International activity .	0.3%	0.3%	0.3%	0.3%	0.3%	0.1%	0.1%	0.2%	0.3%	0.3%	0.3%	0.2%	0.2%
Judicial power .	0.8%	0.9%	0.9%	0.9%	1.1%	0.2%	0.4%	0.5%	0.6%	0.6%	0.7%	0.7%	0.7%
Law enforcement and safety measures .	2.2%	2.1%	2.1%	2.1%	2.3%	1.4%	1.7%	1.9%	2.1%	2.1%	2.1%	2.1%	2.0%
Fundamental scientific research and technological development promotion .	2.0%	2.0%	1.8%	1.7%	1.7%	1.0%	2.1%	2.2%	1.7%	1.5%	1.4%	1.4%	0.3%
Public services rendered to national economy, including :	7.0%	6.9%	6.8%	6.8%	6.9%	5.2%	5.8%	5.9%	6.5%	6.4%	6.1%	6.1%	7.4%
Social services .	17.3%	17.1%	16.8%	16.7%	17.7%	10.8%	14.4%	15.8%	16.8%	16.3%	15.9%	15.8%	15.9%
National debt service	2.7%	2.5%	2.6%	2.6%	1.7%	9.6%	5.2%	3.8%	3.6%	4.3%	4.7%	5.8%	4.7%
Other expenditures	0.3%	0.2%	-0.1%	-0.3%	0.5%	-8.6%	-3.1%	-1.2%	-1.3%	-2.4%	-3.1%	-3.2%	-2.9%
Expenditures and loans less repaid loans	-2.9%	-2.7%	-2.5%	-2.3%	-2.2%	-1.0%	-2.1%	-2.6%	-2.3%	-1.9%	-1.6%	-1.7%	-1.8%
Surplus	-2.7%	-2.5%	-2.6%	-2.6%	-1.7%	-9.6%	-5.2%	-3.8%	-3.6%	-4.3%	-4.7%	-4.9%	-4.7%

в % ВВП; ** ECH включен в налоговые доходы

As compared with the figures registered in January through August of 2003, the budget revenues increased by 0.6 p. p. of GDP in the respective period of 2004, while expenditures decreased by 1.4 p. p. and budget surplus respectively increased by 2.0 p. p. of GDP. As before, VAT accounted for the major share of federal tax revenues – 34.1 per cent of the total tax revenues, what is by 0.2 p. p. above the level observed in the respective period of 2003.

² Because of the estimated data on GDP, the indices may be subject to revision.

According to preliminary estimates, the cash execution of federal budget revenues made 20.0 per cent of GDP in January through September of 2004, what was by 0.5 p. p of GDP above the level of revenues observed in the respective period of the preceding year. At the same time, the cash execution of expenditures made 15.2 per cent of GDP (17.1 per cent of GDP in January through August of 2004); therefore, in the first nine months of this year, according to preliminary data, the surplus made 4.9 per cent of GDP.

According to the preliminary estimates of the Finance Ministry, in terms of fulfilled funding³ the expenditures of the federal budget in January through September of 2004 made 16.1 per cent of GDP (see Table 2), while in the respective period of 2003 this indicator was at 18.2 per cent of GDP. In January through September of 2004, the amount of revenues of the federal budget increased by 0.5 p. p. of GDP in comparison with the figures registered in the respective months of 2003 and made 20.0 per cent of GDP. Therefore, the surplus of the federal budget in terms of fulfilled funding in January through September of 2004 increased by 2.6 p. p. in comparison with the figures registered in January through September of 2003 and made 3.9 per cent of GDP.

Table 2

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

	IX'03	X'03	XI'03	XII'03	I'04	II'04	III'04	IV'04	V'04	VI'04	VII'04	VIII'04	IX'04
Total revenues	19.5%	19.4%	19.3%	19.5%	20.4%	19.6%	19.7%	20.4%	20.6%	20.6%	20.7%	20.6%	20.0%
Public administration	0.5%	0.5%	0.5%	0.5%	0.5%	0.7%	0.6%	0.6%	0.6%	0.5%	0.6%	0.5%	0.5%
Judicial power	2.7%	2.8%	2.9%	2.7%	2.7%	3.9%	2.9%	3.7%	3.2%	2.8%	3.0%	2.8%	2.6%
International activity	0.2%	0.2%	0.2%	0.2%	0.0%	0.2%	0.2%	0.3%	0.3%	0.2%	0.3%	0.4%	0.4%
National defense	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Law enforcement and safety measures	1.9%	1.9%	1.9%	1.9%	2.1%	2.4%	2.3%	2.4%	2.3%	2.1%	2.1%	2.1%	2.0%
Fundamental scientific research and technological development promotion	0.3%	0.3%	0.3%	0.3%	0.2%	0.3%	0.3%	0.4%	0.3%	0.3%	0.3%	0.3%	0.2%
Public services rendered to national economy	1.0%	1.0%	1.1%	1.1%	0.5%	0.7%	0.8%	0.9%	0.9%	0.8%	0.8%	0.6%	0.7%
Social services	2.3%	2.3%	2.4%	2.3%	2.4%	2.5%	2.4%	3.0%	2.9%	2.5%	2.5%	2.4%	2.2%
National debt service	2.0%	1.8%	1.7%	1.7%	1.0%	2.1%	2.2%	1.7%	1.5%	1.4%	1.3%	1.5%	1.5%
Other expenditures	7.0%	6.9%	6.9%	7.0%	5.6%	6.6%	6.1%	6.6%	6.6%	6.2%	6.3%	6.3%	5.9%
Total expenditures	18.2%	17.9%	18.1%	17.8%	15.2%	19.7%	18.0%	19.7%	18.8%	17.1%	17.4%	17.1%	16.1%
Budgetary surplus (+) / deficit (-)	1.3%	1.5%	1.3%	1.6%	5.2%	0.0%	1.7%	0.7%	1.8%	3.5%	3.3%	3.4%	3.9%

According to the estimates of the Tax Ministry, in September of 2004 the tax revenues of the federal budget made about Rub. 144.16 billion (without the single social tax). In real terms the revenues made 288.4 per cent of the level registered in January of 1999, while the respective indicator was at 248.7 per cent in September of 2003 and 254.8 per cent in September of 2002 (see Table 3).

Table 3

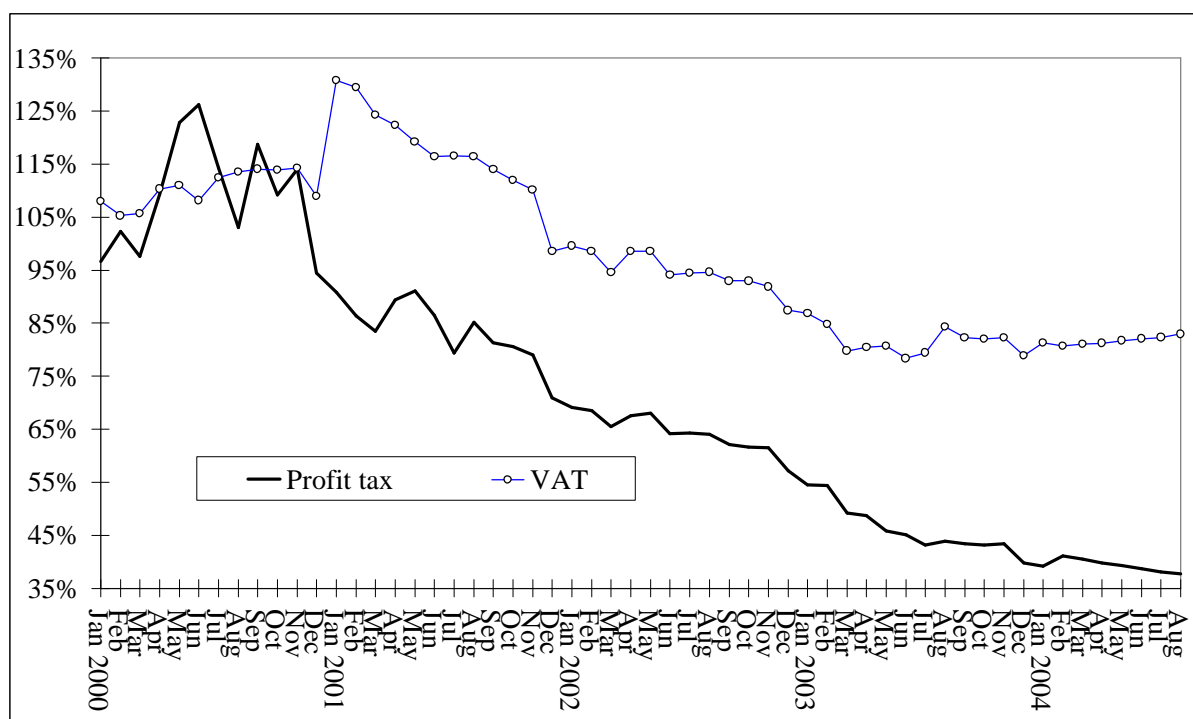
**Actual tax revenues to the federal budget, according to the data of the MTC
(in % of the data for January of 1999)⁴.**

2002*											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
218,7%	187,1%	234,8%	277,8%	239,6%	218,0%	284,4%	246,5%	254,8%	299,7%	241,0%	250,2%
2003*											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
230,0%	229,2%	265,5%	280,4%	233,2%	240,0%	260,4%	242,6%	248,7%	265,6%	231,0%	247,9%
2004*											
I	II	III	IV	V	VI	VII	VIII	IX			
266,5%	204,4%	238,0%	261,4%	241,0%	243,6%	288,9%	246,0%	288,4%			

* Без учета ЕЧН.

³ The execution of the budget in terms of fulfilled (actual) financing is equal to the sum of the funds transferred to managers of budget funds, while the cash execution of the budget is equal to the sum of funds spent by managers of funds (i.e. without account of funds remained on their accounts).

⁴ It was decided to choose January of 1999 as the benchmark in order to render the comparison more reliable. January of 1999 is not a remarkable date in terms of tax revenues.



* There are no data available as concerns the indebtedness relating to the profit tax and VAT in the period from March of 2004 till July of 2004, therefore, the dynamics of indebtedness over this period presented in the Figure above was calculated proceeding from the linear trend between February of 2004 and August of 2004.

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

Table 4

Execution of the RF consolidated budget (in % of GDP)

2002												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes*	28,7%	23,6%	24,3%	26,5%	26,6%	25,9%	26,4%	25,9%	25,2%	25,4%	25,4%	25,5%
Revenues	32,9%	31,3%	31,4%	33,6%	33,6%	32,7%	33,3%	32,5%	31,7%	32,0%	32,1%	32,1%
Expenditures	18,3%	23,7%	26,0%	28,4%	28,4%	28,8%	29,1%	28,9%	28,4%	29,3%	29,7%	31,1%
Budgetary deficit/surplus	14,6%	7,7%	5,4%	5,3%	5,2%	3,8%	4,2%	3,7%	3,3%	2,7%	2,4%	1,0%
2003												
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Taxes*	25,6%	24,4%	25,6%	27,4%	27,1%	26,0%	26,1%	25,7%	3,0%	5,0%	5,1%	25,2%
Revenues	32,0%	30,3%	31,5%	33,4%	33,6%	32,2%	32,2%	31,6%	9,9%	0,8%	0,7%	31,1%
Expenditures	20,7%	25,3%	27,7%	28,8%	28,8%	28,6%	28,7%	28,5%	8,2%	7,8%	7,9%	29,7%
Budgetary deficit/surplus	11,3%	5,0%	3,8%	4,5%	4,7%	3,5%	3,6%	3,1%	7%	0%	8%	1,4%
2004												
	I	II	III	IV	V	VI	VII	VIII				
Taxes*	6,1%		21,8%	27,4%	27,4%	26,6%	27,2%	27,1%				
Revenues	30,6%	28,2%	29,8%	32,9%	32,9%	32,5%	33,1%	32,9%				
Expenditures	18,5%	22,8%	25,4%	27,3%	26,9%	27,0%	27,0%	26,9%				
Budgetary deficit/surplus	12,1%	5,4%	4,4%	5,6%	6,0%	5,5%	6,1%	6,0%				

* Без учета ЕЧН

The revenues of the consolidated budget in January through August of 2004 made 32.9 per cent of GDP, including tax revenues (without SST) at 27.1 per cent of GDP (see Table 4). The expenditures of the consolidated budget decreased by 1.4 p. p. of GDP in comparison with the figures registered in January through August of 2003 and made 26.9 per cent of GDP. As on September 1, 2004, the surplus of the consolidated budget made 6.0 per cent of GDP, what is by 2.9 p. p. of GDP above the level observed in the respective period of 2003.

Main Developments in the Public Sector

In the framework of the reform of the tax legislation with respect to the value added tax, the RF Ministry of Finance proposed to make a number of amendments to the tax legislation. In particular, it is planned to introduce the procedure of value added tax collection on the country of destination basis in relations with Byelorussia already in 2004. In its turn, Russia will switch to collection of the value added tax and excise taxes on the country of destination principle in relations with all member countries of the Commonwealth of Independent States in 2005. Besides, in 2005 the RF Ministry of Finance is planning to discuss the issue of reduction of the base VAT rate from 18 per cent to 16 per cent and the simultaneous abolishment of the privileged 10 per cent VAT rate starting from 2006. In 2006, it is also planned to start the transition from the cash basis method of accounting to the accrual basis method of accounting with respect to VAT payments with the only exceptions permitted for small businesses. As concerns export operations and investments, there will be discussed options of accelerated refund of VAT. At last, the RF Ministry of Finance is considering the possibility to vest banks with the function of collection of information on the payment of the value added tax. At the same time, according to official statements of representatives of the RF Ministry of Finance, the Government has completely abandoned the idea of introduction of special VAT accounts.

This November, the RF Ministry of Finance intends to submit to the Government the draft law with respect to amendments to the Tax Code as concerns the transfer pricing. In particular, principal changes will be related to drawing up of a more precise list of interdependent persons and its expansion by inclusion of companies with different structures of ownership. Besides, in order to justify the price of the transaction, upon request of the tax authorities the taxpayer will have to present a number of documents in accordance with a clearly defined list, which would include marketing research. At the same time, the RF Ministry of Finance opposes the preliminary reconciliation of the price of the transaction between the taxpayer and the tax authorities.

As it follows from the statement made by Sergey Shatalov, a Deputy Finance Minister, in the end of October or beginning of November the RF State Duma may discuss the amendments to Article 25 of the RF Tax Code (as concerns the profit tax). These amendments concern the taxation of mergers, takeovers, and other transformations of companies. The principal concept of the amendments is that there should be no tax consequences in the case of reorganization of companies. At the same time, earnings of shareholders should be subjected to taxation only in the cases of sales of shares, but not in the cases of reorganization of companies.

On October 12, the RF Government approved the amendments to the federal budget for year 2004, in accordance with which the revenues of the budget were increased by Rub. 531 billion and made Rub. 3273.8 billion, while the expenditures were raised by Rub. 108.6 billion up to Rub. 2768.1 billion. It is expected that the Parliament will approve these amendments by the end of November of 2004.

In the framework of improvement of tax administration and tax control, the RF Ministry of Finance proposes to implement a significant modernization of the tax authorities. For instance, it is proposed to create specialized inspectorates in different spheres of business, what may help to more efficiently evaluate the activities of individual taxpayers. It is also proposed to enlarge inter-district tax inspectorates. At the same time, it is planned that the requirements with respect to the tax authorities will be tightened and there will be elaborated standards and official instructions and regulations for all inspectors.

S. Ponomarenko

Monetary Policy

In August and September of this year, there was not observed the traditional seasonal slowdown in the rates of growth in consumer prices as the increase in CPI made 0.4 per cent in each of these months. In October, the gold and foreign exchange reserves of the Russian Federation exceeded the level of US \$ 100 billion increasing by 12.3 per cent since the beginning of September. At this background, the growth in money supply made only 0.1 per cent in September. On September 16, 2004, there took place the first issue of Bank of Russia bonds (OBR) since 2001.

According to the data published by the RF Statistics Service, in September of 2004 the increase in the consumer price index made 0.4 per cent (0.3 per cent in September of 2003, see Fig. 1). Therefore, the rise in consumer prices in comparison with the figures observed in December of 2003 made 8.0 per cent (8.6 per cent in September of 2003 as compared with the level registered in December of 2002).

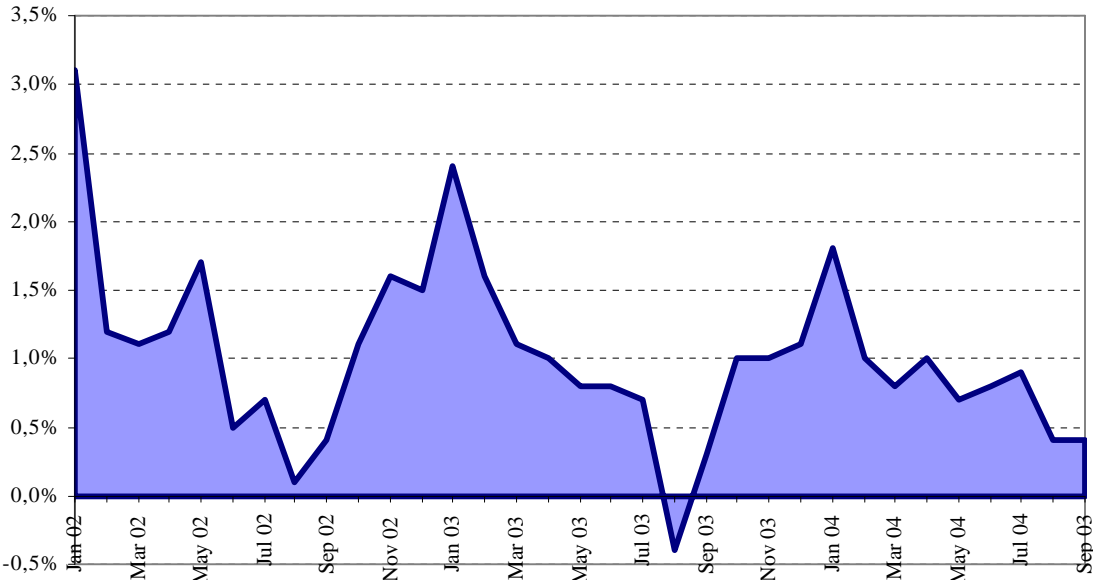
In September, the prices of food products did not grow (7.2 per cent since the beginning of the year). It should be noted that already in August, when there were observed positive rates of growth in food prices with respect to the levels registered in July, the increase in prices since the beginning of the year was above the indicators observed over the last two years. In September, this trend persisted, there was not registered the autumn decline in the prices of this group. At the same time, the prices of nonfood goods increased since the beginning of the year by 5.5 per cent (6.6 per cent in 2003), while in September the growth in prices made 0.9 per cent (0.9 per cent in September of 2003). Across all subgroups of nonfood goods the rates of growth in prices were more moderate as compared with preceding years. This September, the increase in tariffs on paid consumer services made 0.6 per cent as compared with the figures registered this August (0.9 per cent in September of 2003) and 14.3 per cent since the beginning of the year (19.7 per cent). As concerns this subgroup, only prices of services relating to preschool education increased at the rate exceeding the indicators registered last year (by 6.9 p. p.). In September, the growth in the Base Consumer Price Index (BCPI)⁵ made 0.9 per cent (6.8 per cent since the beginning of the year).

Therefore, basing on the results registered in September, it may be ascertained that in August there occurred no significant seasonal slowdown of growth (not to mention a decline) in consumer prices.

At the same time, it should be noted that the situation with respect to inflation in Russia is at the present time rather mixed. On the one hand, monetary factors (primarily the dynamics of the narrowly defined monetary base, which increased by 5.1 per cent over the nine months of this year as compared with 26.1 per cent over the nine months of the last year) facilitated a curb on the base inflation. On the other hand, a rapid increase in prices of manufacturers of industrial products, a significant growth in gasoline prices and the prices of a number of base food products had an additional inflationary impact on the economy.

According to preliminary estimates, in October the value of CPI made from 0.8 per cent to 1.0 per cent.

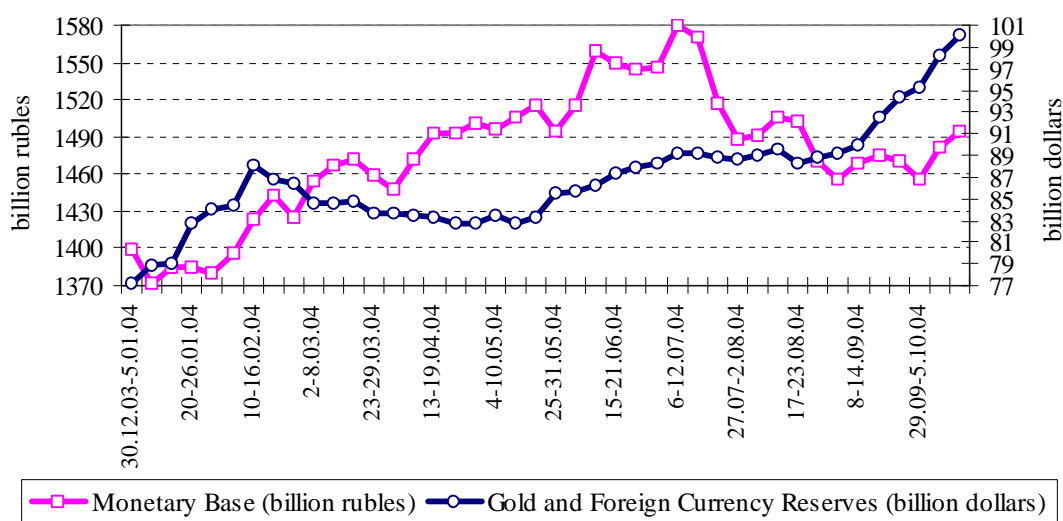
The Growth Rate of the CPI in 2002 - 2004 (% per month).



⁵ The Base Consumer Price Index (BCPI) is an indicator reflecting the inflation rate on the consumer market. It leaves out of account the seasonal (prices of fruits and vegetables) and administrative (tariffs on regulated types of services etc.) factors, calculated by the Statistics Service of the RF.

In the 3rd quarter of this year, the monetary base of the Russian Federation (in the broad definition⁶) decreased by 4.8 per cent and as on October 1 of 2004 made RUR 1.83 trillion. In comparison with the indicator's value observed as on January 1, 2004, the amount of the monetary base decreased by 4.5 per cent. It should be noted that an insignificant growth in the monetary base was observed only in September (+ 0.1 per cent), while in July and August the monetary base contracted. It should be reminded that in the 3rd quarter of the last year the monetary base decreased by 3.2 per cent. Below, the dynamics of the monetary base will be analyzed across its components.

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



The amount of cash in circulation (as adjusted for cash balances of crediting organizations) made RUR 1.37 trillion as on October 1 (by 1.6 per cent above the level registered on July 1 of this year). Over the 3rd quarter of 2004, the amount of accounts of crediting organizations with the Central Bank of Russia practically did not change and made RUR 223.4 billion by the end of the quarter. In July through September, the amount of mandatory reserves sharply declined and made RUR 116.1 billion (-53.8 per cent). At the same time, the amount of banks' deposits in the Bank of Russia increased to RUR 45.4 billion over the 3rd quarter (+ 18.2 per cent). As on October 1, the amount of the Central Bank's liabilities related to the reverse repurchase of securities was by 21.4 per cent above the respective figures registered as on July 1 and made RUR 68 billion. Therefore, the downward trend observed with respect to the dynamics of the monetary base in the 3rd quarter may be primarily explained by the decline in the amount of the fund of mandatory reserves resulted from a significant lowering of the mandatory reserves standards by the RF Central Bank. At the same time, the normalization of the situation in the banking sector resulted in a growth in deposits of banks with the Bank of Russia and the amount of the RF Central Bank liabilities related to the reverse repurchase of securities.

The changes in the narrowly defined monetary base (cash and mandatory reserves) observed in the 3rd quarter of 2004 were also mainly determined by a sharp contraction of the fund of mandatory reserves at the background of an insignificant increase in the amount of cash in circulation: as a result, this aggregate declined by 4.8 per cent in July through September (see Fig. 2). At the same time, in spite of significant growth in gold and foreign exchange reserves registered in the 3rd quarter (+ 7.8 per cent), the substantial withdrawal of liquidity to the budget system (only in July and August the increase in the deposits of the state authorities with the RF Central Bank exceeded RUR 125 billion) prevented a growth in the monetary base. This trend also persisted in October – in the first three weeks of the month the amount of gold and foreign exchange reserves demonstrated a significant growth (+

⁶ The RF Monetary Base in broad definition includes cash in circulation, the Ruble denominated funds in mandatory reserves relating to the borrowings of credit organizations, and funds in credit organizations' correspondent accounts and commercial banks' deposits with the Bank of Russia.

6.2 per cent) and exceeded the level of US \$ 100 billion, while over the same period the monetary base increased by only 1.6 per cent and made RUR 1493.7 billion as on October 18.

As on July 1, 2004, the total amount of the external public debt made US \$ 192 billion⁷ increasing by US \$ 6.3 billion (or by 3.4 per cent) since the beginning of the year. The amount of short term liabilities declined and made US \$ 30.5 billion (as compared with US \$ 36 billion as on January 1 of this year), while long term liabilities increased and made US \$ 161.5 billion (US \$ 149.7 billion). As before, 94 per cent of the external public debt is denominated in foreign currency. As on July 1, 2004, the governmental debt made about one half of the Russian external debt (49 per cent or US \$ 93.5 billion), of which the liabilities relating to the foreign debt of the former Soviet Union made 57 per cent (US \$ 53.2 billion), the amount of the new Russian debt was at 42 per cent (US \$ 39 billion), and the foreign debt of RF subjects made about 1 per cent (US \$ 1.4 billion).

Therefore, while the specific weight of the liabilities of the banks and the monetary authorities in the aggregate foreign debt persisted, this year the share of indebtedness of non-financial enterprises in the total amount of the RF debt continued to grow. Over the first six months of the year, the amount of this debt increased by US \$ 10.5 billion, or 19.1 per cent, and made US \$ 65.6 billion as on July 1, 2004. Over the period under observation, the amount of accumulated foreign liabilities of the state authorities declined by 4.5 per cent (US \$ 4.4 billion). In other words, there persisted the trend observed over the recent years: the amount of foreign liabilities of the public sector of the economy has been decreasing, while the debt of the private sector has continued to grow. It should be noted that in 2004 the increase in the amount of foreign debt of the Russian banking system was rather moderate, primarily due to the banking crisis. To a certain extent, the growth in the foreign debt was also checked by the general outflow of capital of foreign investors from emerging markets, which occurred in the first six months of this year.

On September 16, 2004, there took place the first issue of Bank of Russia bonds (OBR) since 2001. The RF Central Bank placed bonds amounting to RUR 34.5 billion at 1.7 per cent rate of interest per annum for the term of 11 days. It is planned to place bonds in the amount of RUR 34 billion for a term up to 9 months at the next auction, which should take place in October of 2004. Prior to the issue of bonds, for the purposes of attraction of funds from the market the Bank of Russia used such instruments as deposit operations and the operations related to the reverse repurchase agreements (CBR crediting on the security of government bonds). As a result of the issue of OBR, the market instruments used by the Bank of Russia in order to tie up liquidity are now clearly classified in short term instruments (deposit operations), medium term instruments (reverse REPO operations), and long term instruments (Bank of Russia bonds).

The emergence of the new instrument of the RF Central Bank may increase the effectiveness of sterilization operations due to longer terms of attraction of funds from the market and a higher liquidity of bonds in comparison with the deposit operations and the operations relating to reverse repurchase agreements. In the case of deposit and REPO operations, the term of attraction of resources as a rule is at or below 3 and 6 months respectively. An additional factor in favor of the issue of Central Bank bonds is the fact that Russia lacks a benchmark for the market of corporate borrowings, which is usually represented by the rate of interest on the assets characterized by low risk levels (for instance, government securities). The extent, to which the bonds issued by the Bank of Russia may play this role, will depend on the policies pursued by the RF Central Bank with respect to the yields of the bonds at the moment of placement.

P. Trounin

⁷ It should be reminded that according to the international methodology used by the RF Central Bank for the determination of the amount of the foreign debt, this debt includes liabilities to nonresidents across all sectors of the economy notwithstanding the currency they are denominated in. Besides, a key characteristic of the debt is the debtor's obligation to make payments relating either to the principal or interest, i.e., the amount of the debt does not include conditional obligations, loan commitments, and guarantees, as well as participation in capital.

Financial Markets

Over the month, positive trends generally dominated on the financial markets. The quotations of Russian forex denominated bonds continued to grow at the background of falling yields of the base assets (US Treasury Bills). The market of Ruble denominated debt instruments, in its turn, was affected by such factors as the extremely high liquidity in the banking sector and the Ruble appreciation, what facilitated a growth in quotations both in the public and corporate sectors. By the end of the month, the stock market demonstrated positive results, however, in the middle of the month there was observed a significant adjustment. After the successful completion of the auction for the sale of LUKOIL shares, there continued the attack against YUKOS and its chief oil extracting asset Yuganskneftegaz. According to the statements made by the official representatives of the RF Ministry of Justice, the probability that this asset will be sold at an underestimated price is rather high. In spite of the already formed “immunity” of Russian stocks to the YUKOS affair, this news resulted in the changes in the ratio between demand and supply in favor of the latter.

The Market for Government Securities

In October, on the Russian market of Eurobonds there prevailed positive trends as concerns the dynamics of yields. In the beginning of the month, the quotations of Russian Eurobonds increased following the decline in yields of US Treasury Bills. The factor behind the decrease in yields of US and, later, Russia securities was the high level of oil prices, which may check a further rise of rates by the US FRS. The fact that the Moody's ranking agency raised the forecast of the Russia's ranking from stable to positive had a positive impact on quotations. As on October 22, the yield to maturity of Russian Eurobonds RUS-30 was 6.83 per cent p.a.; RUS-18: 7.23 per cent p.a. Besides, on the same date the yield to maturity of the Russian Eurobonds was: Minfin bonds, 7th tranche: 6.23 per cent; Minfin bonds, 6th tranche: 3.72 per cent; Minfin bonds, 5th tranche: 5.73 per cent; RUS-07: 5.33 per cent.

Figure 1.

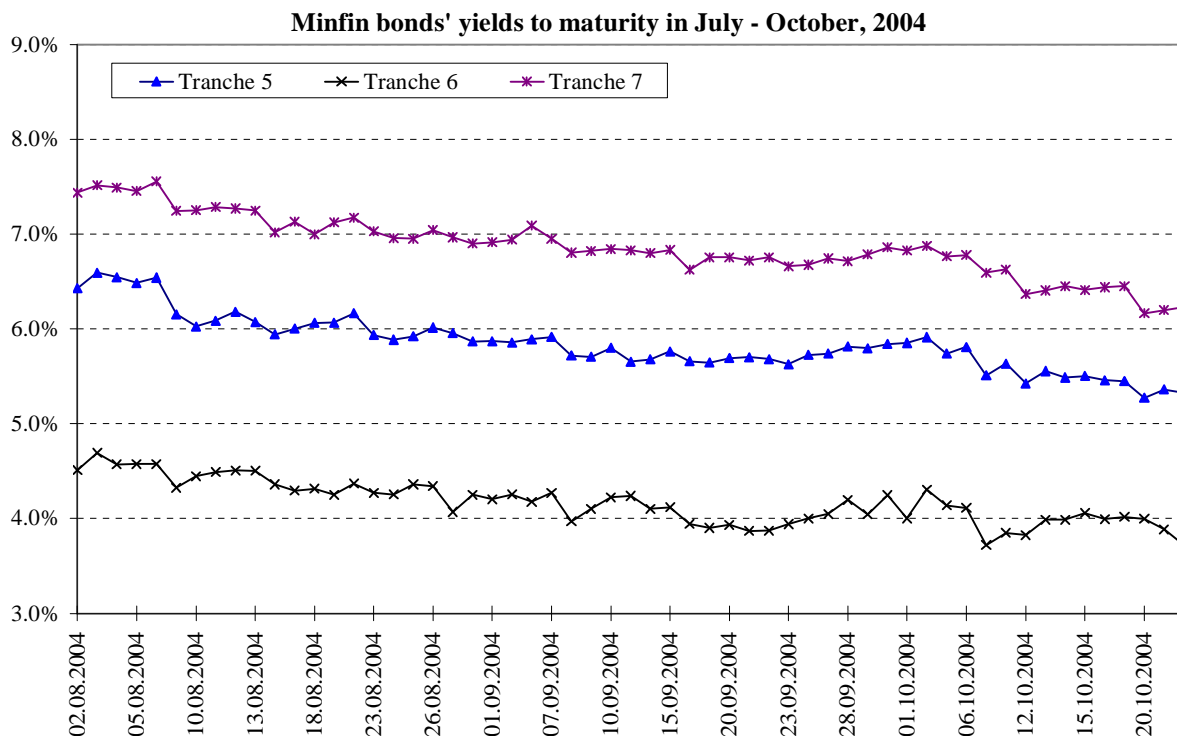
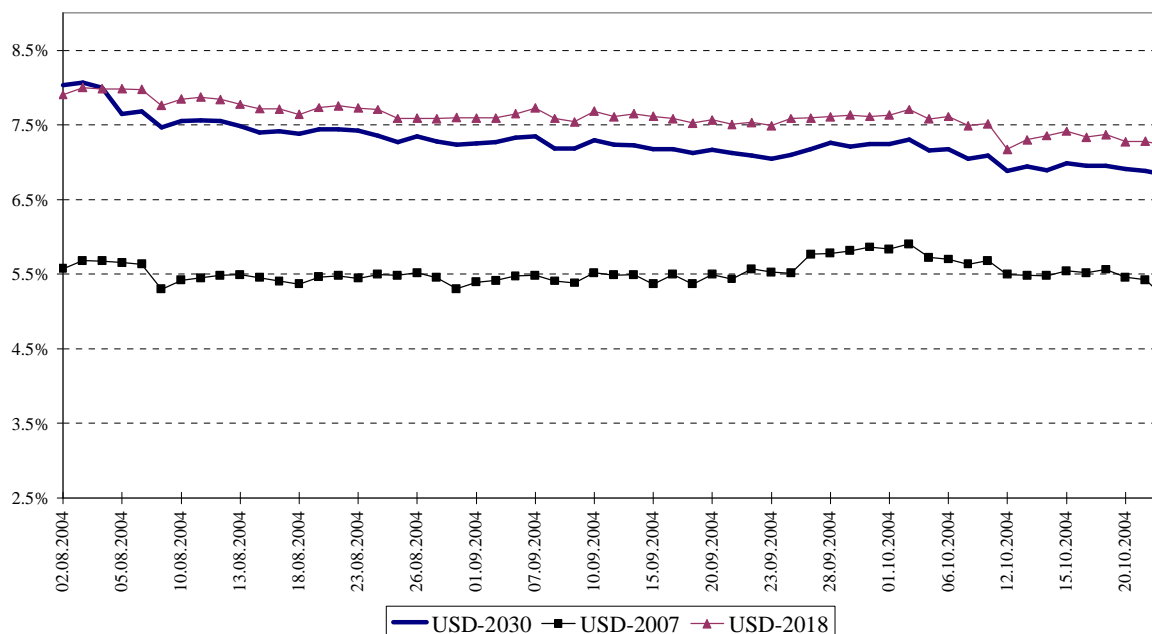


Figure 2.

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



As concerns the segment of Ruble denominated government debt, in the beginning of October there was registered the minimum amount of trading, mainly due to declining activity in the sector of OFZ FD and the significant amounts of placement of securities at the auctions, which took place over the preceding weeks. At this background, the demand at the BMR auction with respect to the bonds of the Bank of Russia demonstrated that the participants of the trading were interested in short term instruments. By the end of the month, there was observed an increase in the turnover and decline in yields of the majority of liquid issues. These developments were related to the business situation on the forex and financial markets: the average overnight MIBOR rates decreased, while the US \$ exchange rate persisted at a minimum level since the beginning of this June – RUR 29 per US \$. persisted a relative stability. On the one hand, the insignificant changes in quotations could be caused by the seasonal lull on the market. On the other hand, the low volatility of quotations may be an evidence of the high stability of the existing price levels.

Over the period from October 1 to 22, the aggregate turnover of the secondary GKO OFZ market made about RUR 63.8 billion (approximately RUR 103 billion over the respective period in September), while the average daily turnover was at RUR 3.86 billion (RUR 5.76 in September). Therefore, the activity of the market was significantly below the indicators observed in September. In the same period, there also took place several placements on the primary market of Ruble denominated debt instruments. Thus, on October 6, there took place two auctions for the placement of OFZ FK 27026 and OFZ AD 46002, the nominal value of which made RUR 4.8 and 4.0 billion respectively. The amount of these placements made RUR 2.6 billion and 3.9 billion respectively, while the weighed average yields of the placements were at 7.42 per cent p. a. for OFZ FK 27026 and 7.99 per cent p. a. for OFZ AD 46002. On September 20, there took place the auctions for the placement of OFZ AD 46001 and OFZ AD 46014, the nominal value of which made RUR 5.0 billion each. the amount of placement made RUR 249 million, while the weighed average yields of this placement was at 7.1 per cent. On the same day, there took place the auction for the additional placement of OFZ AD 46002, the nominal value of which made RUR 1 billion. The amount of these placements made RUR 1.7 billion and RUR 1.06 billion respectively, while the weighed average yields of the placements were at 7.62 per cent per annum and 7.91 per cent per annum.

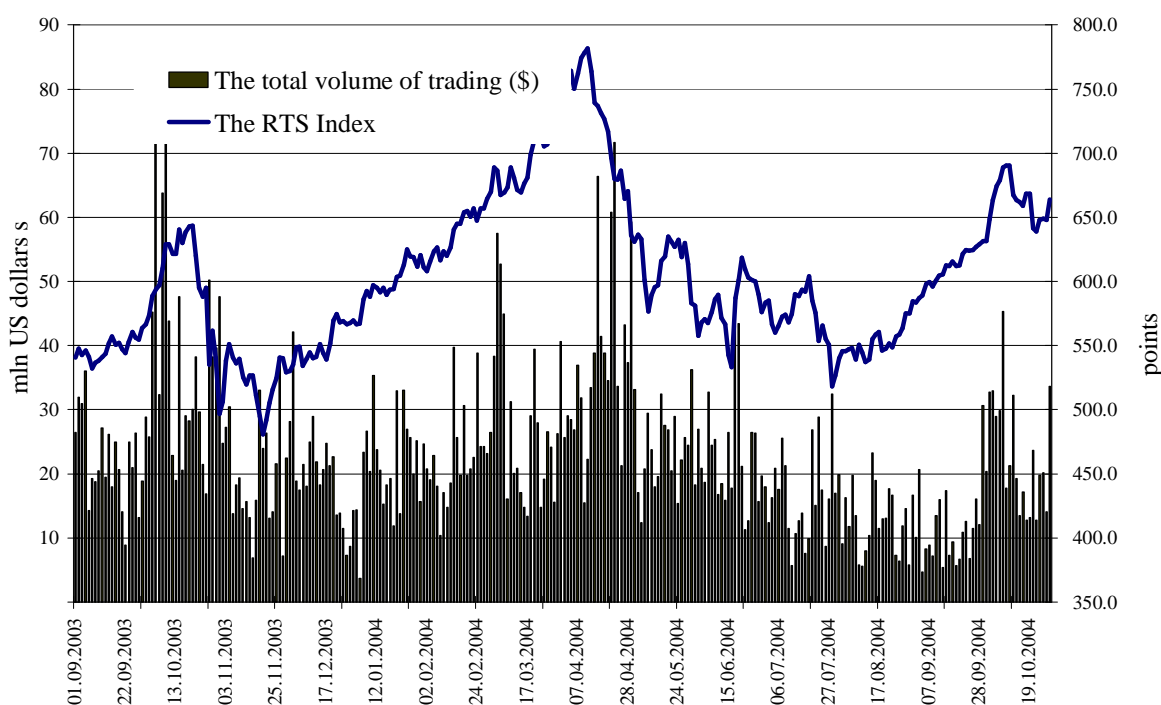
As on October 27, the amount of the GKO – OFZ market made RUR 492.01 billion at par and RUR 475.34 billion at the market value. The duration of the GKO-OFZ market portfolio was 1665.52 days.

The Market for Corporate Securities

The business situation on the stock market.

By the end of October, the Russian stock market demonstrated an insignificant increase in prices. At the same time, there may be singled out three stages in the dynamics of the RTS index. The first stage is characterized by positive dynamics of the stock market observed in the beginning of the month. The rise in prices was primarily determined by corporate news with respect to YUKOS, RAO UES of Russia, and LUKoil. For instance, in the first week of the month there was announced that YUKOS was highly evaluated by the investment bank Drezdner Kleinwort Wasserstein. The market positively reacted to the statement of the RF President that the Government should assist LUKoil in implementation of its plans. At the background of accelerating reform of electrical power engineering, the stocks of the energy sector enterprises, in particular, the RAO UES of Russia demonstrated positive dynamics, what facilitated a growth in the RTS index. An especially interesting situation formed with respect to the shares in Mosenergo: the increase in the market value of this company reached 70 per cent in one hour (on October 5). However, in the second week of the month, an adjustment occurred on the stock market. The adjustment was initiated by negative news about YUKOS: the RF Ministry of Justice announced that 100 per cent of Yuganskneftegaz shares were evaluated at US \$ 10.4 billion, what was significantly below the expectations dominating on the market. Moreover, later it became known that 77 per cent of shares in Yuganskneftegaz might be sold with a 60 per cent discount. By the end of the month, the adjustment stopped and the market dynamics were determined by the record high oil prices rather high amounts of liquidity in the banking sector, weak macroeconomic indicators of Russia, and negative news concerning YUKOS. On the whole, the situation at the end of the month was characterized by consolidation.

Figure 3.

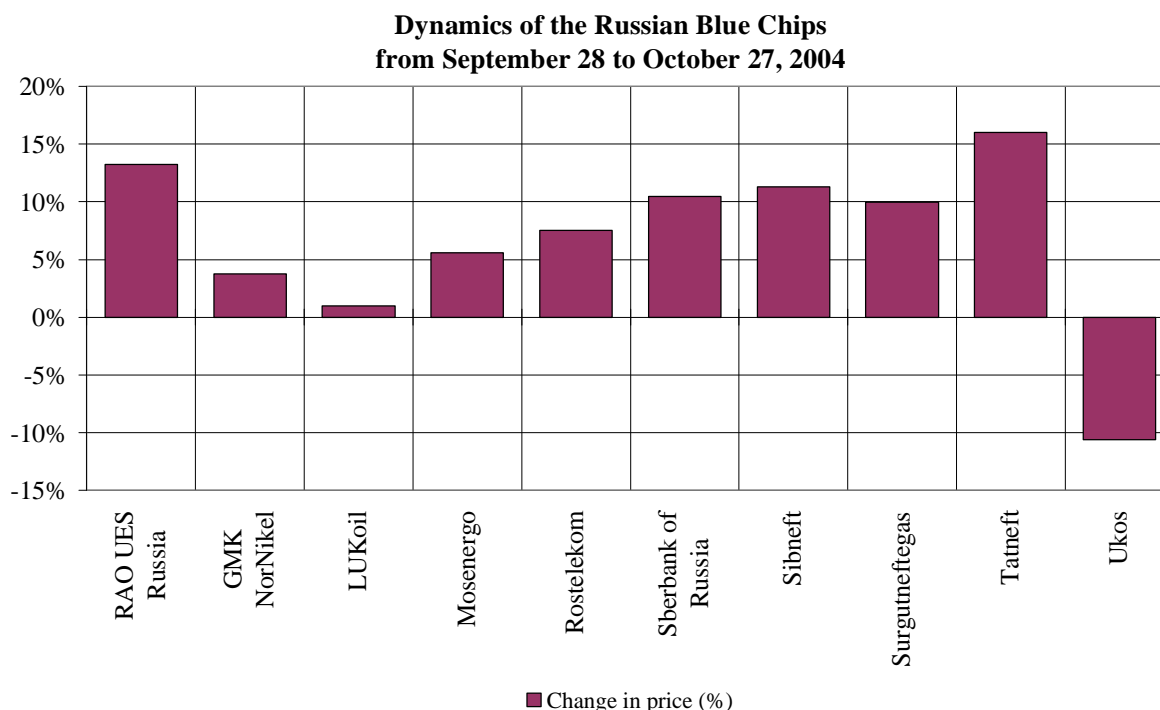


On the whole, in the period from September 30 till October 27, the RTS index increased by 5.12 per cent or by 32.31 points in absolute terms. Over the same period, the turnover of the RTS trading amounted to about US \$ 441.1 million (about US \$ 211.2 million in September), while the average daily turnover at the RTS made about US \$ 23.2 million (US \$ 10.5 million in September). The highest and the lowest volumes of trade at the RTS made US \$ 45.3 million (on October 7) and US \$ 12.7 million (on October 21) as compared with US \$ 20.68 million and US \$ 4.7 million respectively in September.

Over the last month (from September 28 till October 27), practically all “blue chips” with the exception of YUKOS demonstrated a growth in prices. Thus, shares in Tatneft, the price of which in-

creased by 16.01 per cent over the period under observation, became the leaders. These shares were followed by the stocks of the RAO UES of Russia (13.25 per cent), shares in Sibneft (11.28 per cent), and Sberbank of Russia (10.48 per cent). The stocks of Surgutneftegaz were also characterized by positive rates of growth (9.97 per cent) at the background of rumors about the possibility of the company's participation in the auction of Yuganskneftegaz in the case such an auction is held. Over the month, the price of shares in Rostelekom grew by 7.55 per cent, while the stocks of Mosenergo in spite of very significant volatility observed over the month demonstrated the rise in price by 5.57 per cent. At the same time, shares in the GMK Norilsk Nickel and LUKoil grew by 3.75 per cent and 0.99 per cent respectively. At the background of new negative information with respect to Yuganskneftegaz, YUKOS stocks fell by 10.63 per cent.

Figure 4.



In October, the list of leaders in terms of the volume of turnover at the RTS⁸ looked as follows: the shares in the RAO UES of Russia (28.20 per cent), LUKoil (15.67 per cent), the GMK Norilsk Nickel (8.86 per cent), and Surgutneftegaz (8.61 per cent). The aggregate share of transactions with shares in these four issuers made about 62 per cent of the total turnover of trade at the RTS.

As on October 27, the top five leaders of the national stock market by capitalization looked as follows⁹: Surgutneftegaz: US \$ 28.58 billion; LUKoil: US \$ 27.02 billion; Sibneft: US \$ 17.3 billion; GMK Norilsk Nickel: US \$ 13.8 billion, and the RAO UES of Russia: US \$ 13.04 billion.

The market for fixed term contracts. In October, the activity of investors on the RTS market for fixed term contracts (FORTS) somewhat increased in comparison with the September indicators. Thus, in the period from October 1 till October 27, the aggregate volume of trade in futures and options at the RTS amounted to about RUR 27.6 billion (115.3 thousand transactions; 3.06 million contracts), what was somewhat above the respective indicators registered in the preceding month (turnover - RUR 26.4 billion, 112.77 thousand transactions; 3.26 million contracts).

Futures contracts accounted for the greatest percentage of transactions: the volume of trade in these contracts made RUR 24.8 billion (2.75 million contracts, 110.8 thousand transactions) over the period under observation. As before, options were in a much lower demand: the respective amount of trading made about RUR 2.76 billion (315.7 thousand contracts, 4.5 thousand transactions). The maximum

⁸ On the classical stock market.

⁹ According to the RTS.

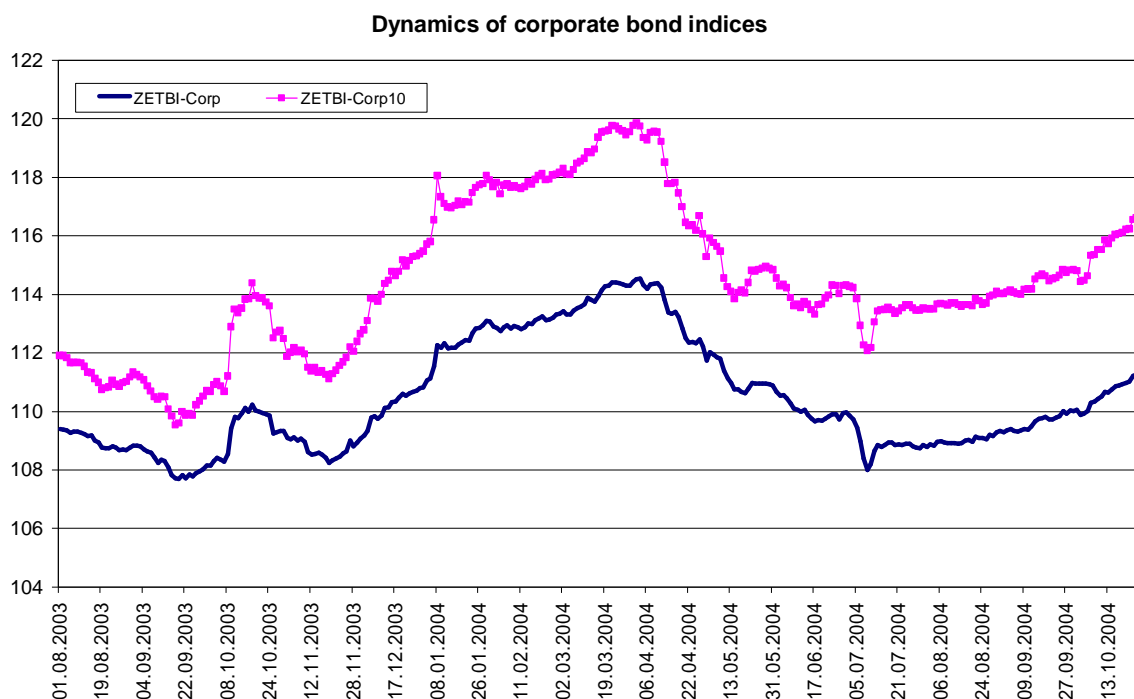
trading volume was observed on October 5 and made RUR 2.36 billion, while the minimum trading volume (RUR 854 million) was registered on October 25.

Corporate bond market.

At the end of September and in the beginning of October, the market of Ruble denominated corporate debt did not demonstrate any clearly directed trends. On the one hand, the inflow of forex denominated proceeds supported Ruble denominated securities. At the same time, the excessive liquidity alone was not enough to initiate a stable trend. A factor checking the activity of investors was the significant amount of supply on the primary market. During the second week of the month, the growth continued, what was also in part determined by the high level of liquidity. The dynamics of the forex market also significantly affected the sentiments of investors, since the US \$ exchange rate began to decline noticeably. The positive dynamics of the market was also supported by the decision of the ranking agency Moody's to increase rankings of Vneshtorgbank and Sberbank by 1 point above the sovereign ranking, as well as rising quotations of Eurobonds. Besides, the unsatisfied demand at the auction held with respect to placement of Gazprom bonds transformed into demand on the secondary market, what additionally supported the securities of the "top echelon." By the end of the month, the favorable situation with respect to liquidity facilitated the persistence of high prices in the sector of corporate and regional bonds. The dynamics demonstrated by the US debt market were also a factor behind the persistence of high prices: yields of 10 year US Treasury Bills was at or above 4 per cent.

From October 1 till October 27, the price index of corporate bonds traded at the MICEX¹⁰ increased by 1.31 points (1.20 per cent) and the index of ten most liquid corporate sector bonds increased by 2.06 points (by 1.80 per cent). In the period from October 1 till October 22, the total turnover in the bond sector of MICEX made about RUR 20.3 billion, while the average daily turnover was registered at RUR 1.27 million.

Figure 5



External factors affecting the dynamics of the Russian stock market.

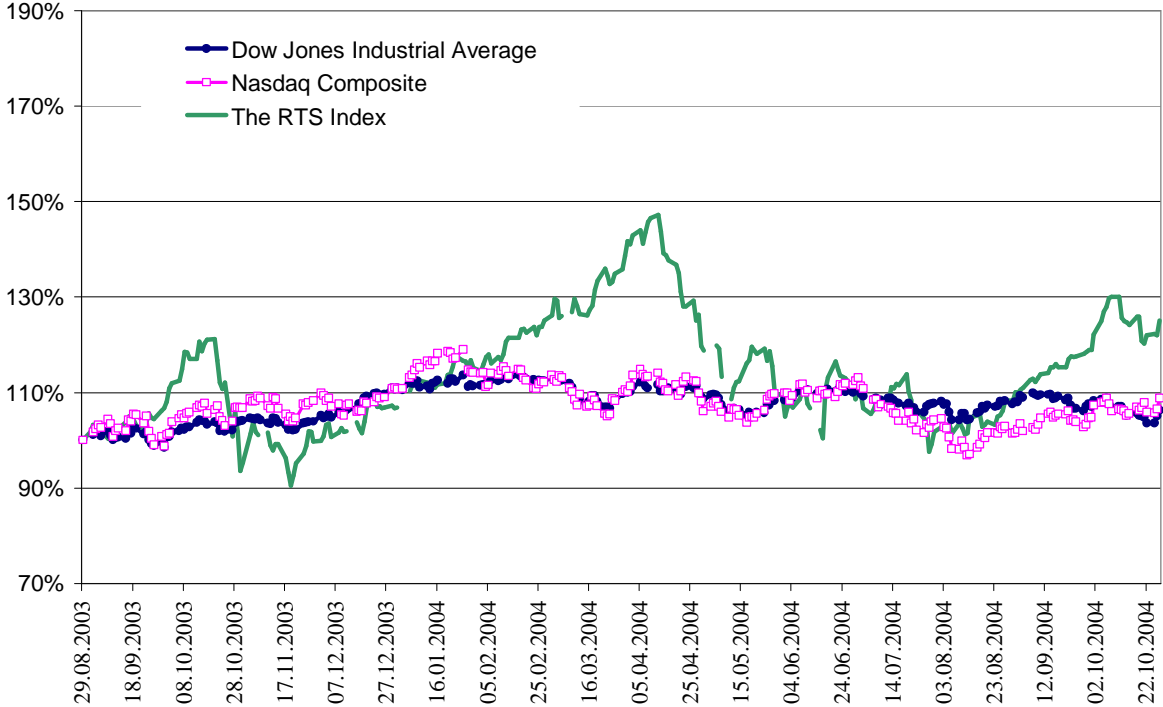
In the beginning of the month, the Brent oil prices, next to the North American WTI oil prices, exceeded the level of US \$ 50 per barrel. A factor behind these high prices of oil as before was the situation on the US fuel market, where because of the consequences of natural calamities taking place a month ago a part of oil extracting and processing capacities remained idle. The growth in prices was

¹⁰ The indices of corporate bonds traded at the MICEX that have been used for the calculations are calculated by Zenit Bank.

also facilitated by the persisting uncertainty in Nigeria, where the disagreement between trade unions and the government continued. Later, the growth in prices slowed down somewhat, and by the end of the third week of the month there was even observed an adjustment, which took place at the background of large funds closing out their long positions. On the whole, the week did not bring much important news. The only negative factor was the publication of the data on the reserves of crude oil and oil products in the USA. However, since recently the shortage of oil products on the eve of the winter season significantly affected the dynamics of quotations. Exactly this factor facilitated the recovery of growth in oil quotations during the second half of the third week of the month.

In September, on the world stock market there were observed mixed trends (see Table 1). In October, US stock indices demonstrated rather downward dynamics. The factors behind these developments were high oil prices, a flow of negative forecasts with respect to financial corporate results, growing trade deficit, cooling of the world economy, uncertainty of the outcome of the Presidential race, as well as mounting danger of new terrorist attacks. Among positive factors there may be perhaps noted only low yields of government bonds. As concerns macroeconomic news, there should be noted the growth in the consumer price index, which increased by 0.2 per cent after a 0.1 per cent growth registered in the preceding month. The same indicator, without adjustment for the volatility of food products and fuels increased by 0.3 per cent, while the forecast estimated it to grow by 0.1 per cent. The increase in base inflation at the background of cooling was a negative factor as concerns the stock market. In this connection, there is more chance that interest rates would increase further.

Figure 6.



As concerns the results of the month, it should be noted that the business situation on the markets of raw materials has no doubt favorably affected the dynamics of quotations of Russian stocks. Even a flow of negative corporate news could not significantly change the trends observed on the stock market in the situation of extremely high bank liquidity. At the same time, the negative situation on the US stock market could not fail to have an impact on the Russian market of securities and therefore in part reduced the potential of growth on the Russia's market.

Corporate news

The OAO LUKoil

On September 29, the NK LUKoil and the American company ConocoPhilips announced the creation of a large scale strategic alliance, in the framework of which the US company becomes a strategic investor in the capital of LUKoil. This statement was made after one of ConocoPhilips affiliates became the winner of the auction for purchase of 7.59 per cent of authorized and issued ordinary stocks

of LUKoil, up to that moment being in the federal ownership, for US \$ 1.988 billion (US \$ 30.76 per share).

The OAO Gazprom

In September of 2004, the Russian Government proposed to increase the share of the state in the authorized capital of the OAO Gazprom by the way of transfer to it of the state owned company Rosneft. In accordance with the Plan of measures aimed at the integration of the OAO NK Rosneft in the structure of the company, there were determined the consultants of the transaction concerning the affiliation of the assets of the NK Rosneft. Drezdner Kleinwort Wasserstein will be the financial consultant as concerns the structuring of the transaction and will assess the value of the Rosneft assets and the block of shares in Gazprom, which is entered in the balance sheets of the company's subsidiaries. Deutsche Bank and City Group will independently prepare statements concerning the fairness of the transaction with respect to its structure and evaluation of assets.

On October 12, the company placed Ruble denominated bonds in the amount of RUR 5 billion maturing in 3 years. The rate of the six month coupon was set at 7.58 per cent per annum. Investors submitted 120 bids amounting to more than RUR 9 billion. In the course of the auction, there were satisfied 73 bids. It is planned to use the attracted funds for the financing of investment necessary to maintain the existing production capacities, implement new prospective projects, as well as refinancing of the short term indebtedness of the company and optimization of the structure of its debt portfolio.

The OAO GMK Norilsk Nickel

In the middle of the month, the company placed its bonds in amount of US \$ 500 million with yields of 7.125 per cent at the moment of placement, which should mature on September 30, 2009. The demand for the issue was more than four times above the amount of supply.

At the meeting of the GMK Norilsk Nickel Board of Directors it was resolved to recommend the extraordinary general meeting of shareholders to pay interim dividends for 9 months of 2004 in amount of RUR 41.4 per share.

On October 20, 2004, the GMK Norilsk Nickel announced that in the nearest future it would implement the 3rd additional stage of exchange of shares in the RAO Norilsk Nickel for shares in the GMK Norilsk Nickel for the shareholders, who failed to utilize their right to carry out this operation in 2001 and 2002.

The OAO Sberbank of Russia

The international ranking agency Moody's has changed its forecast of the long term forex denominated ranking of Sberbank of Russia Ba1 from "stable" to "positive." The ranking of debt obligations of the bank was increased to Baa2 and is at the moment above the sovereign ranking of the Russian Federation. According to representatives of the agency, these decisions were taken with the view of a significant role the Sberbank of Russia played in the economy of Russia and the national banking system, especially in the sphere of private deposits.

The NK YUKOS

On October 8, the company instructed its registrar to transfer 57.5 per cent of shares in the OAO Sibneft to their former owners. This operation was carried out in connection with the fact that the ruling of the Moscow Arbitration Court of March 1, 2004, as concerns the nullification of the additional issue of shares in the OAO NK YUKOS, which was used in the framework of purchase of the OAO Sibneft, entered into force.

Table 1.

Dynamics of international stock market indices

Data as on October 30, 2004	Value	Change within the month (%) ¹¹	Change since the beginning of the year (%)
RTS (Russia)	663.96	5.53%	13.29%
Dow Jones Industrial Average (USA)	10002.03	-0.75%	-3.92%
Nasdaq Composite (USA)	1969.99	5.35%	-1.83%
S&P 500 (USA)	1111.09	0.09%	0.24%
FTSE 100 (UK)	4630.10	1.37%	2.66%
DAX-30 (Germany)	3929.03	1.20%	-2.23%
CAC-40 (France)	3678.39	0.30%	2.27%
Swiss Market (Switzerland)	5374.90	-2.27%	-3.72%
Nikkei-225 (Japan)	10691.95	-1.14%	-1.23%
Bovespa (Brazil)	23171.00	-0.26%	3.23%
IPC (Mexico)	11517.71	6.22%	41.88%
IPSA (Chile)		3.08%	17.19%
Straits Times (Singapore)	1959.05	-1.01%	9.36%
Seoul Composite (South Korea)	809.91	-2.67%	-1.38%
ISE National-100 (Turkey)	22565.77	1.22%	17.85%
Morgan Stanley Emerging Markets Free Index	469.74	2.01%	6.00%

The Foreign Exchange Market.

Throughout the most part of October, no significant fluctuations of the US \$ exchange rate were observed on the domestic foreign exchange market: the exchange rate was in the range from RUR 29.11 to RUR 29.12 per US dollar. The stability of the exchange rate as it seems was ensured by the statement of the Bank of Russia management that active speculations on the foreign exchange market had no prospects.

At the same time, by the end of the month the situation on the foreign exchange market changed: in the course of the trade session held on October 23, the US \$ exchange rate declined below the level of RUR 29 per US dollar and was at RUR 28.998 per US \$ dollar. It seemed that the RF Central Bank abandoned its policy of support of the Ruble in favor of stable inflation. The increase in turnover and the US \$ depreciation with respect to the Ruble was determined by an enormous inflow of forex denominated export proceeds. In January through August of 2004, the active balance of trade of Russia grew up to US \$ 51 billion, as compared with US \$ 39 billion registered in the respective period of the preceding year. The market oriented towards a further appreciation of the Ruble, since by the end of the third week of the month the price of Russian Urals oil exceeded the level of US \$ 44 per barrel, while the amount of gold and foreign exchange reserves reached US \$ 100.1 billion.

Thus, in the period from October 1 till October 22, the US \$ depreciated by RUR 0.45 (by 1.56 per cent) and made RUR 28.767 per US \$. The aggregate volume of trade in the US Dollar at the SELT in the period from October 1 till October 22 made about US \$ 18 billion (as compared with approximately US \$ 13.7 billion in the respective period of September). Over this period, the average daily turnover made US \$ 1.12 billion, what was also above the respective indicator registered in September. During the period under review, the highest volume of trade in the US Dollar, about US \$ 2.9

¹¹ As compared with the levels registered on September 28.

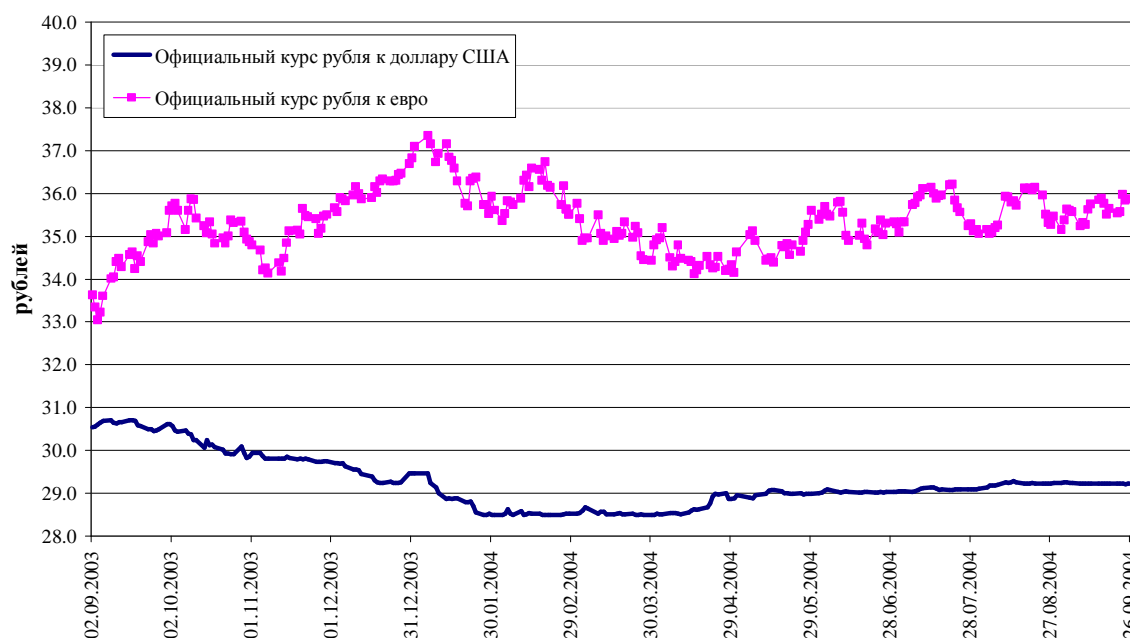
billion, was observed on October 22; the lowest volume, US \$ 445 million, was observed on October 7.

This October, the Ruble liquidity in the banking sector significantly increased in comparison with the figures registered in the preceding month: in October, the average balances of correspondent accounts of credit organizations with the Bank of Russia made RUR 231 billion as compared with RUR 198.4 billion registered in September of 2004.

Figure 7.

Dynamics of the official USD / RUR and EUR / RUR exchange rates in 2003 – 2004

Динамика официального обменного курса рубля к доллару США и евро в 2003-2004 гг.



In October, on the world foreign exchange market there was observed a sharp depreciation of the US dollar against the Euro. In the beginning of the month, the exchange rate was rather stable and was at the level of US \$ 1.23 to US \$ 1.24 per Euro. However, starting from the middle of the month, the exchange rate of the European currency began to stable rise against the US dollar, what was determined by negative, as compared to expectations, data on the trade balance and the level of unemployment in the USA. The downfall of the US stock indices also had a negative impact on the US \$ / Euro exchange rate. By the end of the month, the exchange rate of the US currency continued to decline. In August, the amount of purchases of the US securities by nonresidents fell to the minimum registered since October of 2003. in spite of the decline in this indicator, the inflow of capital remained at the level exceeding the necessary US \$ 55 billion a month to compensate for the deficit of the current account. An additional factor facilitating the sales of US currency was the statement made by the President of the Federal Reserve Bank of San Francisco G. Allen to the effect that the increase in the trade deficit presents a threat to the growth of the national economy.

In the period from October 1 till October 28, the exchange rate of Euro on the world market appreciated by US \$ 0.026 (2.15 per cent) and reached US \$ 1.2706 per Euro. At this background, there was also observed a significant appreciation of the Euro against the Ruble. In the period from October 1 till October 28, the European currency appreciated against the Ruble by RUR 0.67 (1.85 per cent) from RUR 36.03 per Euro to RUR 36.69 per Euro. It should be noted that on October 26, the exchange rate of the European currency was at RUR 36.86 per Euro. The aggregate turnover of trade at the SELT amounted to Euro 127.1 million in the period from October 1 till October 22, while the average daily turnover was registered at Euro 7.94 million. In this period, the highest volume of trade with Euro was registered on October 13 at Euro 12.68 million, and the lowest, Euro 5.69 million, was observed on October 11.

Figure 8

Dynamics of the Dollar / Euro exchange rate on the international markets

Динамика курса евро к доллару на мировых валютных рынках (\$ за евро)

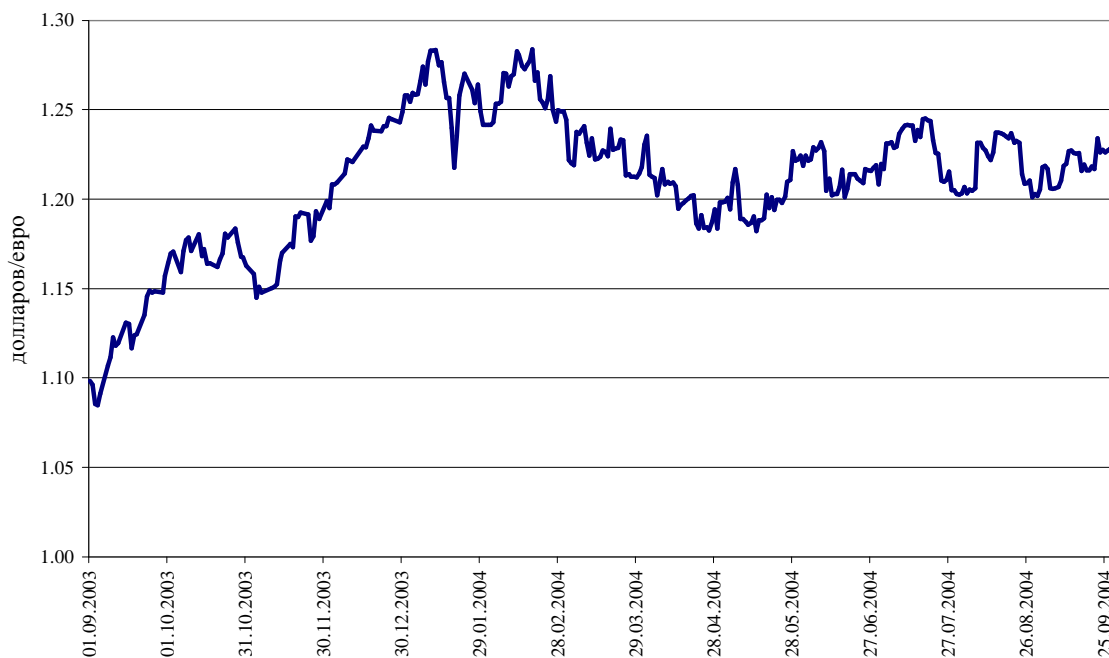


Table 2

Financial Markets Indicators

Month	June	July	August	September	October*
Monthly inflation rate	0,8%	0,9%	0,4%	0,4%	0,9%
Inflation rate annualized on the basis of this month's trend	10,03%	11,35%	4,91%	4,91%	11,3%
CB RF refinancing rate	13%	13%	13%	13%	13%
Annualized yield to maturity on OFZ issues (%)	6,48%	6,45%	6,64%	7,13%	6,0%
Volume of trading in the secondary GKO-OFZ market for the month (RUR billion)	12,03	6,41	20,61	33,59	30,0
Yield to maturity on Minfin bonds at the end of the month (% p.a.)					
5th tranche	6,71%	6,52%	5,87%	5,84%	5,3%
6th tranche	4,92%	4,78%	4,25%	4,25%	3,7%
7th tranche	7,68%	7,63%	6,90%	6,86%	6,2%
8th tranche	5,49%	5,33%	4,87%	4,76%	4,4%
Yield to maturity of Eurobonds at the end of the month (% p.a.)					
2005	3,39%	3,45%	3,92%	5,14%	6,0%
2007	5,28%	5,71%	5,30%	5,86%	5,1%
2010	6,52%	7,94%	6,76%	7,01%	6,6%
2018	7,87%	8,02%	7,60%	7,61%	7,2%
2028	8,29%	8,53%	8,22%	8,20%	7,8%
2030	8,09%	8,08%	7,23%	7,24%	6,9%
INSTAR-MIACR rate (% p.a.) on interbank overnight loans at the end of the month	11,38%	4,96%	9,86%	3,13%	1,5%
Official RUR / US\$ exchange rate at the end of the month	29,0274	29,1019	29,2447	29,2171	28,7655
Official RUR / Euro exchange rate at the end of the month	35,2915	35,0532	35,1463	35,9896	36,6472
Average annualized growth in RUR / US\$ exchange rate	0,15%	0,26%	0,49%	-0,09%	-1,55%
Average annualized growth in RUR / Euro exchange rate	-0,88%	-0,68%	0,27%	2,40%	1,83%
Volume of trading at the stock market in the RTS for the month (US\$ million)	482,07	368,25	277,15	262,27	475
Value of RTS-1 Index at the end of the month	584,63	540,27	584,65	635,57	660
Change in value of RTS-1 Index during the month (%)	0,54%	-7,59%	8,21%	8,71%	3,8%

* Estimate

D. Polevoy

The Real Sector of the Economy: Factors and Trends

According to the preliminary data, in January through September of 2004, GDP made Rub. 12047 and was by 6.9 per cent above the level registered in the respective period of the preceding year. This year, the dynamic expansion of domestic demand had a positive impact on dynamics of GDP. A specific feature is the outpacing rates of growth in investment in fixed assets in comparison with the dynamics of GDP, as well as of production and services of base sectors of the economy. The expansion of demand on the consumer and investment markets is observed at the background of outpacing rates of growth in import of final demand goods in comparison with the dynamics of domestic production.

According to the Regulations governing the elaboration and presentation of the data on the part of the Federal State Statistics Service, there was published the first assessment of the information relating to the production and utilization of GDP in the first six months of 2004. The amount of GDP in the first six months of 2004 made Rub. 7549.0 billion and increased by 7.4 per cent in comparison with the figures registered in the first six months of the preceding year. According to the preliminary data presented by the RF Ministry of Economic Development and Trade, in January through September of 2004, GDP made Rub. 12047.0 billion and exceeded the level registered in the respective period of the preceding year by 6.9 per cent. A specific feature of this year is the outpacing rates of growth in production of goods in comparison with the dynamics of services. The added value in industry increased by 7.3 per cent in real terms, while in construction it grew by 14.3 per cent. As concerns the sector of services, the sector of market services still developed most dynamically, and it should be noted that practically all increase in the respective added value was provided by communications, trade, and transport.

Table 1

The dynamics of the real amount of produced GDP and gross added value across individual industries in the first six months of 2003 and 2004, in per cent of the figures registered in the respective period of the preceding year.

	2003			2004		
	<i>Ist Q</i>	<i>2nd Q</i>	<i>Ist half year</i>	<i>Ist Q</i>	<i>2nd Q</i>	<i>Ist half year</i>
Gross Domestic Product	107,5	107,9	107,7	107,5	107,4	107,4
including:						
Production of goods	106,9	108,0	107,5	107,6	107,7	107,7
Of which:						
Industry	106,5	107,9	107,2	107,5	107,1	107,3
Construction	113,6	114,7	114,2	113,8	114,6	114,3
Agriculture	101,1	98,9	99,9	98,6	98,8	98,7
Production of services	108,0	107,8	107,9	107,1	107,1	107,1
Market services	109,0	108,8	108,9	107,9	107,9	107,9
Of which:						
Transport	106,4	106,5	106,4	106,8	106,2	106,5
Communications	117,8	122,2	120,2	121,5	123,6	122,7
Trade	112,8	111,2	112,0	108,2	109,2	108,7
Non-market services	102,4	102,3	102,4	102,2	102,5	102,4

Source: Federal Service of State Statistics

The outpacing rates of growth in gross accumulation in comparison with the dynamics of expenditures for final consumption had the dominating impact on the structure of GDP utilization in 2003 and 2004. By the end of the third quarter of 2004, investment in fixed assets increased by 11.6 per cent, while expenditures for final consumption grew by 10.1 per cent. At present, in Russia there exists a rather favorable situation for domestic and foreign investment. This situation is based on a balanced macroeconomic policy. No doubt, that certain risks persist, however, according to experts, these risks are at levels usual for other countries. The most attractive objectives of investment in the Russian economy were companies providing services relating to mobile communications, as well as oil extracting industry and largest steel producing enterprises. However, it should be noted that an intensive growth in revenues in the economy was not supported by adequate mechanism of transformation of household and public savings in investments. The share of investments in fixed assets in GDP remained at the level registered in January through September of 2003 and made 14.1 per cent, while the share of gross national savings increased by 2 p. p. over the same period.

Table 2

The dynamics of components of GDP utilization in 2003 through 2004, in per cent of the figures registered in the respective period of the preceding year.

	2003, by quarters			2004, by quarters		
	I	II	III	I	II	III*)
Gross Domestic Product	107,5	107,9	106,2	107,5	107,4	106,0
including:						
Expenditures for final consumption	106,5	106,6	105,7	109,7	110,3	110,1
Of households	107,8	107,9	107,0	112,0	112,7	112,4
Of state institutions	102,6	102,5	101,6	102,5	102,6	110,5
Of non-commercial organizations	102,3	101,3	98,3	100,6	99,8	99,8
Gross accumulation	115,4	119,5	112,5	113,5	115,6	110,5
Net exports	107,0	100,0	92,1	95,4	85,7	75,3

*) preliminary estimates of the RF Ministry of Economic Development and Trade

Source: Federal Service of State Statistics

In 2004, the trend towards an intensive expansion of production persisted across practically all sectors of economy and industries. In January through September of 2004, the increase in output of products and services of base sectors of economy made 6.9 per cent (6.5 per cent in industry). Over the same period, the freight turnover grew by 6.8 and retail trade turnover increased by 11.5 per cent as compared with the figures registered in January through September of 2003. In January through September of 2004, the average monthly rates of growth in communications services increased to 3.60 per cent, as compared with 2.25 per cent observed in the respective period of 2003.

In 2003 and 2004, there was observed an increasing influence of the export oriented sector of the economy. At the background of the exceptionally favorable price situation on the world markets of raw materials, exports grew across practically all range of goods. In January through August of 2004, exports increased by 27.4 per cent. The specific weight of staple fuel and energy resources in the total amount of exports made 54.5 per cent, while the share of ferrous and nonferrous metals was at 14.9 per cent. The growth in output of the industries oriented towards the domestic market affected the dynamics and structure of industry. In January through September of 2004, the indices of growth in fuel industry made 107.7 per cent, including 109.3 per cent in oil extraction industry, while the respective indicator of ferrous metallurgy was at 105.2 per cent. The dynamic growth of export oriented industries initiated an increase in revenues of the economy at large. As compared with the figures registered in January through August of 2004, the balanced financial result of fuel industry grew 1.95 times, and 2.3 times as concerns ferrous metallurgy, while in the economy at large this indicator increased 1.49 times and 1.68 times in industry.

The industries forming domestic demand were characterized by more intensive dynamics of development. As concerns the complex of investment industries, in January through September of 2004, the respective index of production made 111.3 per cent as compared with 106.9 per cent observed in the respective period of the preceding year. In January through September of 2004, the increase in production of mechanical engineering made 12.7 per cent, while this indicator in the industry of construction materials grew by 5.9 per cent.

The output significantly varied across branches of mechanical engineering. In 2003 and 2004, the persistence of rather high rates of growth in machinery and equipment was primarily facilitated by the expansion of demand for products of railroad mechanical engineering, instrument making, and the industry of communications equipment. Over the last four years, there persisted a stable increase in demand for equipment of the industries of the consumer complex. However, in spite of almost twofold acceleration of the rates of output of capital goods, this year there is observed an increasing gap between the dynamics of investment demand and supply of domestically produced equipment and machinery. The expansion of demand on both the investment and consumer markets takes place at the background of an outpacing rate of growth in import of goods of final consumption in comparison with the dynamics of domestic production. As compared with the figures registered in January through July of 2003, import of machinery and equipment increased by 44.0 per cent, while the share of imported equipment in the structure of investment in machinery and equipment made almost one fourth.

Table 3

The dynamics of output across industries of mechanical engineering in January through September of 2000 through 2004, in % of the figures registered in the respective period of the preceding year.

	2000	2001	2002	2003	2004
Mechanical engineering and metal working	116,0	107,7	103,1	108,1	112,7
Including by branch:					
Metallurgical mechanical engineering	144,1	90,8	70,1	104,8	115,2
Chemical and petrochemical mechanical engineering	123,0	125,6	87,8	87,0	111,1
Hoisting and transport mechanical engineering	148,1	123,5	92,3	80,8	107,0
Railroad mechanical engineering	105,2	121,1	123,4	132,0	120,9
Electrical engineering	139,3	113,7	94,4	102,7	103,2
Machine tool and tool industry	117,3	98,0	85,0	92,2	97,5
Instrument making	136,1	100,6	92,8	150,1	106,9
Motor industry	104,0	98,6	103,3	100,8	112,9
Tractor and agricultural mechanical engineering	153,8	134,9	82,2	71,8	135,6
Mechanical engineering for light and food industries	108,9	104,3	115,7	106,4	122,8
Communications equipment industry	430	85,6	169,2	128,8	191,0

Source: RF Goskomstat, Federal Service of State Statistics

The increasing impact of imports has significantly affected the dynamics of development of the consumer complex industries. The expansion of consumer demand was determined by an intensive growth in household incomes. In January through September of 2004, the increase in the real disposable cash household incomes made 9.8 per cent, while real wages and salaries grew by 13.3 per cent. In January through September of 2004, the turnover of retail trade exceeded the level registered in the respective period of the preceding year by 2.8 per cent. The saturation of the consumer market with goods mainly corresponded to the effective demand of households for major types of food and non-food goods. At the background of outpacing rates of growth in demand for nonfood goods, the state service of statistics registers a stable increase in the index of business confidence in the sectors of retail trade with radio devices and household appliances, furniture, household goods, pharmaceuticals, etc.

While in the first six months of 2002 domestically manufactured goods accounted for about 60 per cent of the structure of the commodity resources of the retail trade turnover, in 2004 their specific weight declined by 5 percentage points. As the growth rates in food industry decelerated to 4.4 per cent in January through September of 2004, the share of imports in the commodity resources of the food market demonstrated an upward trend. It should be noted that while non-competing imports make a considerable share in the structure of commodity resources of retail trade turnover with respect to food products, imports squeeze out domestically manufactured goods as concerns non-food commodities. According to some estimates, the share of imports in the structure of commodity resources of non-food goods has increased by 3.4 percentage points since the beginning of the year. While the downfall of output of light industry persists, the increase in import of jersey and textile apparel made 25.8 per cent as compared with the figures registered in January through July of 2003. A factor behind the declining competitiveness of Russian goods in comparison with similar imports has been the low technical and technological level of the production apparatus. The persisting trend towards the lower rates of renovation of fixed assets observed in light industry places it in the group of manufacturing industries characterized by critical levels of wear and tear of fixed assets. The low competitiveness of industries of final demand and the lack of a prospective strategy with respect to restructuring of the domestic business aimed at formation of new markets for Russian products facilitate the persistence of orientation towards traditional positions on the world markets of raw materials and fuels and determine the dependence of economic growth rates on the external economic situation.

The calculation of forecast values of macroeconomic indicators until end-2004, carried out by IET, demonstrates that at the current levels of prices of hydrocarbons and mineral products, as well as an increase in exports by 21.4 per cent, the expected growth in GDP will make 107.2 per cent, while the increase in investment in fixed assets may make 111.5 per cent.

O. Izryadnova

IET Business Survey: Industry in October of 2004

The up to date information concerning the state of Russian industry in October indicate that a hitch in economic growth will be overcome soon. This assumption is confirmed by the data on the actual dynamics of demand, output, obstacles to increase in output, and plans of enterprises.

The September official statistical data indicate that industrial recovery became less intensive. The average daily output increased by 0.2 per cent (as adjusted for the seasonal factors). According to the estimates presented by the Center for Macroeconomic Analysis and Short Term Prognostication (CMASTP), the average monthly rate of increase in the volumes of production made 0.2 per cent in the 3rd quarter as compared with 0.7 per cent registered in the 2nd quarter. In the 3rd quarter, the growth in the fuel and energy complex and the raw materials sector practically stopped. The persistence of the general trend towards an increase in industrial production was caused mainly by growing output in final industries based on the expansion of the domestic market.

In October, the intensity of growth in sales increased (as adjusted for the seasonal factors) by 7 p. p. and as a result exceeded the average level observed in the first six months of 2004. Surveys registered a more rapid growth in sales for money across all industries with the exception of the industry of construction materials, light industry, and food industry. However, the “negative developments” observed over the preceding months has not been permitting enterprises to revise their evaluations of demand (above norm – below norm) in a positive direction. The balance of evaluations remained without change at the level of -39 per cent after the absolute record registered in August (-37 per cent). However, the major part of enterprises assesses the level of demand for their products as normal. This indicator also has remained stable (58 per cent) over the last two months. The record figures across all 149 surveys (59 per cent) were also registered in August. For instance, in October 100 per cent of enterprises in fuel industry reported satisfaction with the demand for their products. The minimum value of this indicator was observed in mechanical engineering (44 per cent) and light industry (49 per cent).

The recovery of growth in demand (as compared with September figures) permitted enterprises to increase the rates of production. In October, the balance (intensity) of changes reached (after the adjustment for seasonal factors) the maximum in the last 5 months. However, there was not utilized the total potential of growth in production (ensured by demand, as it should be noted). Sales grew at an outpacing rate in comparison with output at 15 per cent of enterprises, while the usual level was observed to make 10 to 13 per cent. An especially significant ratio of the rate of growth in demand in comparison with the rate of growth in output was registered in October in the forestry complex (29 per cent), chemistry, and petrochemistry (24 per cent).

The monitoring of obstacles to the growth in production also demonstrated that the output of Russian enterprise could have increased more intensively. The frequency of reports about the majority of obstacles continued to diminish and some of them have reached record low values. At present, insufficient demand hinders to increase output to only 39 per cent of enterprises. This figure represents the best (minimum) value registered since the beginning of 1994. At present, the most frequently reported obstacle is the lack of working capital. However, this value is also almost the minimum value observed across all 149 surveys (the absolute minimum was registered in January of 2004). Now, only 16 per cent of enterprises mention payment arrears, which have once been destroying the economy. In 1995, payment arrears created obstacles for 74 per cent to 77 per cent of producers. The competing imports are considered to present an obstacle at only 17 per cent of Russian enterprises (in July of 2004 it hindered 26 per cent of enterprises). The lessening pressure of imports on domestic producers was observed across all industries with the exception of chemistry and petrochemistry. At present, the competing imports most often present an obstacle for enterprises of light industry (30 per cent as compared with 38 per cent registered in July). However, also in the food industry, which is considered to be most effectively protected, 19 per cent of enterprises suffer because of the competing imports.

A decline in the rates of growth in sales and output registered over the last months affected the dynamics of profits in October. There again became more enterprises in industry reporting a decrease in this indicator. A decline replacing growth or more intensive decline – these developments were registered across all industries with the exception of electrical power engineering, fuel industry, and metallurgy. The ceasing of a growth in profits affected the evaluations of the financial and economic standing of enterprises. In October, the balance of these assessments at once fell by 7 points, while in July there was observed the record high value of this indicator. However, the bulk of enterprises evaluate

their standing as satisfactory. In October, the share of such assessments increased to 75 per cent, what is the absolute record.

Over the last months, the forecasts of changes in demand (as adjusted for seasonal factors) practically have not changed. In industry at large and across all industries there is expected a rather intensive growth in sales. Especially high level of confidence was observed in electrical power engineering and fuel industry, while light industry was the third.

The balances of changes in the plans of output have also stabilized. However, they are not as close to the record values as forecasts of demand. Growth in production will persist across all industries with the exception (due to the seasonal factors) of the industry of construction materials.

S. V. Tsukhlo

Foreign trade

In August 2004, record indicators of the volumes of Russian foreign trade were achieved. As before, the main factors contributing to this situation are high world prices of the Russian basic export goods and continuation of Russian rouble strengthening.

Work is continued on improving the Russian legislation in the sphere of economy and regulation of the foreign economic activity. In October 2004, investigations began to determine the presence of dumping import of nickel-containing corrosion-resistant (stainless) flat-rolled stock of the UN countries. The State Duma passed the Draft Law in the third reading "On Introduction Changes in the Customs Code of the RF", adding the Code with a new Chapter "Customs Duties".

Since November 2004, a new mechanism of establishing export duties for oil products comes into effect.

According to WTO forecast, the world trade growth for 2004 will make 8,5% in real price. The growth of oil prices will not substantially affect the world trade, as the powerful growth of trade and gross domestic product is observed in China, Latin America and Africa. Moreover, the recovery of Japanese economy proceeds in quicker rates than expected. According to WTO data, in 2003 the volume of trade in commodities rose by 16% - to 7.3 bln dollars in nominal prices. In real prices, the world trade growth in 2003 was 4,5%, in comparison with 3% in 2002 and the recession of 2001.

In August 2004, major indicators of the Russian foreign trade reached record results for the past 15 years. The Russia's foreign trade turnover, calculated according to balance of payments methodology, rose to 24.3 bln dollars, which by 32,8% exceeds this indicator of last year. As compared to August 2003, the volume of export of goods in August 2004 rose to 35,0% - to 16.2 bln dollars, import - by 28,8% - to 8.1 bln dollars. The trade balance reached 8.1 bln dollars. Among other things, the volume of exports abroad increased by 32% - to 13.2 bln dollars. The import deliveries from abroad made in August 2004 6.4 bln dollars, having increased, in comparison with July 2003, by 28,3%.

Figure 1

As before, the growth of export is largely determined for Russian exporters by favourable conjuncture of the world market. For several months already the world prices of oil are maintained on the record level, which can be explained by peak (for the last 24 years) oil demand against the background of unstable situation in a number of source countries (Iraq, Russia and Venezuela).

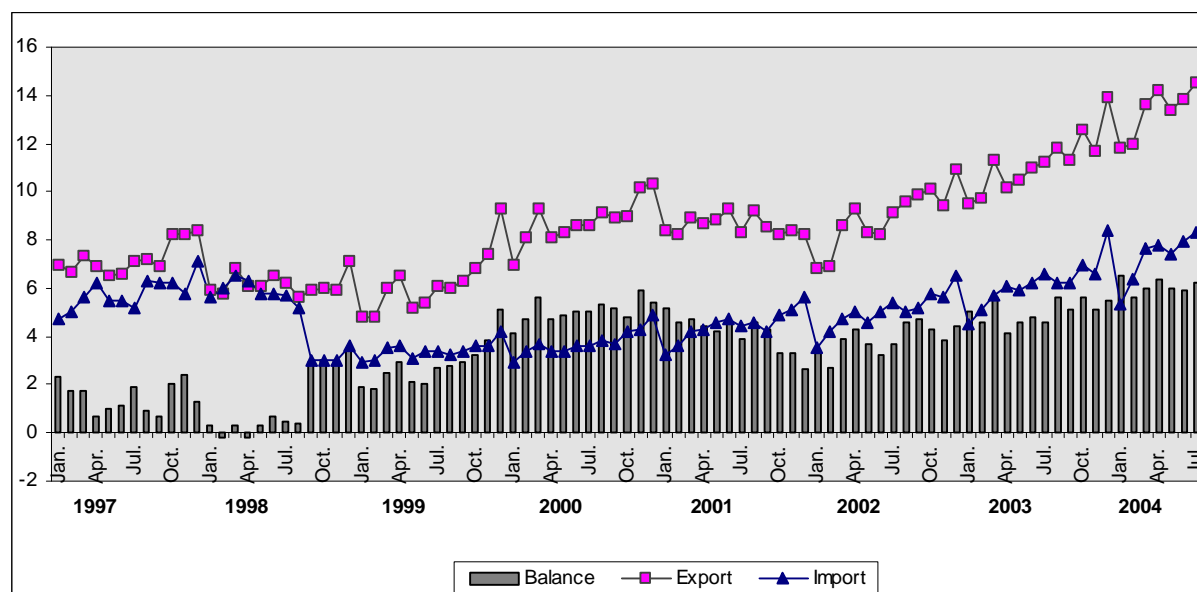
In August, the oil price of Brent was USD 42.8/barrel, which by 12,1% exceeds the same indicator of last month, and by 43,2% - the August of 2003.

In January-August 2004, the average oil price of Urals was USD 32.5/barrel and increased, in comparison with the same period of last year, by 20,1%. It should be noted that, in August, the average price made USD 39.3/barrel, (growth by 10,5%, in comparison with July 2004).

The increased difference between oil prices of Brent and Urals can also be explained by the fact that, recently, Saudi Arabia considerably increased the deliveries of high-sulfur oil to the European market, causing, thereby, decrease in price of Russian oil Urals, comparable with it by characteristics.

As compared to July this year, the average August contract price of Russian natural gas, supplied abroad, increased by 3,3%.

Over the passed months, the world prices of non-ferrous metals have not changed substantially (except for nickel price, which reached its peak in July, and started to come down afterwards), but still noticeably exceed the last year indicators.



Source: Central Bank of Russia

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

Table 1.

August Average Monthly World Prices (by year)

	1996	1997	1998	1999	2000	2001	2002	2003	2004
Oil (Brent), USD/barrel	21.04	18.25	12.5	20.2	29.4	25.7	27.2	29.9	42.8
Natural gas, USD/1 mln. BTU	2.856	2.121	1.858	2.8	4.437	2.91	2.999	4.888	5.212
Gasoline, USD/gallon	0.6299	0.5941	0.4128	0.6476	0.9021	0.776	0.834	0.935	1.152
Copper, USD/t	2001.4	2481.7	1627.4	1646.6	1941.7	1499.4	1480.0	1731.0	2835.8
Aluminum, USD/t	1480.1	1563.7	1345.4	1421.1	1546.4	1374.9	1292.0	1457.0	1694.3
Nickel, USD/t	7100.4	6737.3	4137.1	6430.8	8092.9	5554	6720.0	9365.0	13723

Source: based on the data of the London Metal Exchange (Great Britain, London), International Oil Exchange (London)

The growth of import is favored by a continuing (in the last months) tendency of strengthening the real dollar-to-rouble rate and income growth in the Russian economy. According to the Ministry of Economic Development, strengthening (in January-August) of the real dollar-to-rouble rate was 5,5%, which is considerably less than a year ago (11,4%). In conditions of dollar strengthening relative to euro, the real effective rouble rate is strengthened somewhat quicker than in previous years. According to the Ministry of Economic Development, for the 8 months strengthening of the real effective rouble rate made 5,3% (5% for January-August 2003). In so doing, in the 2d quarter, as in July-August, the real effective rouble rate was strengthened only by 0,2%. As compared to the same period of 2003, the real incomes of the population in January-August 2004, increased by 9,2% (including in August - by 7%).

The activities of the RF government are continuing to improve the Russian legislation in the sphere of economy and regulation of foreign economic activity.

Since November 2004, the rates of oil products export duties will be differentiated. From now on they will be calculated proceeding from the world oil prices and will make, on average, about 65% of the export tariff of oil itself. However, within the "oil products basket" transportation of fuel oil will be two times cheaper than export of light oils. For example, at the general duty rate for the oil products

basket amounting 15% of export cost, the fuel oil duty will come 10%, and for the rest of products manufactured from oil, - 20%.

In this connection, on October 18 the Government established a new rate of customs export duties for products manufactured from oil, brought out from the Russian Federation beyond the boundaries of the states – members of the Customs Union agreements. The export duty rate of USD 57/t (65% of oil duty, which, since October 1 is USD 87.9/t) is established for benzene, toluene, xylene, oil lubricants, used oil products, propane, butane, and other liquefied gases. Also according to that rate, beginning from November 20, the following products will be brought out from the RF: xylene, distillates, gas oils, residues of crude oil or oil products refining, obtained from bituminous rocks. Crude oil products and calcinated petroleum coke will be transported duty free.

At present in exporting oil products the customs duty of USD 45.4/t is effective. It came into force from August 30. Prior to that date, the rates of export customs duties for oil products were USD 37.5/t. Tariff for fuel oil exporting is not changed so far and will make USD 45.4/t.

In October 2004, the Ministry of Economic Development and Trade of the RF starts investigations in order to determine the presence of dumping import of nickel-containing corrosion-resistant (stainless) flat-rolled stock from the UN, which caused financial damage to that sector of the Russian economy.

Decision on the start of investigations was taken according to statutory requirements and based on the results of examination of the proposal filed by the OJSC “Chelyabinsk integrated iron-and-steel works” on behalf of Russian manufacturers.

For the share of the applicant party, together with the OJSC Moscow Metallurgical Plant “Serp i Molot” that supported it, came, in the period of 2001 – 2003, on average 78,7% of the total volume of production of the nickel-containing flat-rolled stock in Russia.

The fair value of the nickel-containing flat-rolled stock from the EU, made in the EU market, on average USD 1657/t, export price of the same stock from the EU, imported to the customs area of the RF – is on average USD 708/t, margin of dumping for deliveries - 134%.

The financial damage to this sector of the Russian economy characterized as worsening of a number of financial and economic indicators. In particular, the sales of domestic nickel-containing flat-rolled stock in the internal market decreased by 16,1%, which led to reduction of the share of domestic producers of nickel-containing flat-rolled stock in the internal market from 54,2% to 52,9%.

The profitability of sales lowered to the point of 30,4%. In addition, the gross profit decreased of sales in the internal market, which reached negative value in 2003. Use of production capacities is at a low level, while the number of manufacturing staff at the enterprise of the applicant party lowered by 5,8%.

A number of facts give evidence to the cause-and-effect relation between dumping import and the financial damage of this sector of Russian economy. Like that, increasing of the share of import from the EU in consumption (by 7 percent in 2003, as compared to 2002) occurred with lowering of the share of Russian nickel-containing flat-rolled stock in the internal market (by 6,2 percent).

Supplies of nickel-containing flat-rolled stock from the EU in the period of the 1st to 3^d quarters of 2003 by dumping prices lower than in the world market, made a negative effect on pricing of the Russian manufacturers, which, in turn, was attended with worsening of the indicators characterizing the sector of the Russian economy.

Besides, dumping batches of nickel-containing flat-rolled stock from the EU to the Russian market and infliction of damage to Russian producers synchronize. Thus, in accordance with the Federal Law “On Special Protective, Antidumping, and Countervailing Measures in Importing Goods” the above conditions provide a basis for making a decision on the start of investigations for recognition of the presence of dumping import of nickel-containing flat-rolled stock from the EU to the RF customs area and the financial damage to the sector of the Russian economy determined by that.

In October, the State Duma passed the Draft Law in the third reading “On Introduction of Changes in the Customs Code of the RF”, adding the Code with a new Chapter “Customs Duties”.

Introduction of changes in the current wording of the Customs Code is caused by necessity of carrying out the law-making procedure of levying customs dues. The Draft Law expands the sphere of the Customs Code regulation by adding it with a new Chapter 33.1 “Customs Duties”. This Chapter defines the notion - Customs Duties and offers a qualificatory list of their types: for customs clearance, escort and storage. The Draft Law fixes a maximum of the customs duty rate for the customs clearing -

100 thousand roubles. Also, fixed rates are established for the escort and goods storage at the temporary storage warehouses and the customs storage warehouses. The fact that the fixed rates for several types of dues are stated right in the text of the Draft Law, makes it a directly applicable law.

For example, for carrying out the customs escort of a motor vehicle or railway vehicle for a distance less than 50 km, dues are paid in the amount of 2 thousand roubles, 51 - 100 km - 3 thousand roubles, 101 - 200 km - 4 thousand roubles. At distances above 200 km, dues will make up 1 thousand roubles for each 100 km of railway, but never less than 6 thousand roubles. For carrying out the customs escort of a sea, river or airborne vehicle, dues are assigned in the amount of 20 thousand roubles, regardless of a haulage distance.

Introduction of changes in the Code will allow to fulfill the obligations of the RF with regard to customs duties in the negotiation process for entry into WTO – pursuant to Article VIII GATT, the customs dues are levied not for fiscal purposes, but as refund of the customs authorities' charges.

N.Volovik

Reforming the Public Sector of Science: New Government Approach

The two draft Concepts are considered for reforming the public sector of science: the first prepared by the Ministry of Education and Science, and second – revised with the participation of RAS. The contrastive study shows the tasks, goals and major provisions of the two draft Concepts. The drawbacks are analyzed and the results of changes made in the draft Concepts are assessed. The list of problems is formulated which may arise in the case the final wording of the Concept is adopted.

In September 2004, the excerpts of a new document “**A Concept of the RF Participation in Administrating Public Institutions Engaged in Science Activities**”, developed by the Ministry of Education and Science of the RF, had been made public. The Concept was developed behind-the-scenes and was published only after it had gone through hot debates in the Presidium of RAS. Among the expressed criticism the most essential was that RAS was not engaged in preparation of the text of Concept, and thus, the role of fundamental science became underestimated. After the Concept has been published it aroused a stormy and negative reaction on the part of the scientific community itself, as it also has participated neither in development nor in discussing of any of its drafts. On the initiative of RAS, a Working Group was formed comprising representatives of the Ministry of Education and Science, RAS, and the Union of Rectors of Russia. As a consequence of its activity, a revised and signed (by the three parties) draft Concept was prepared entitled “**Concept of the RF Participation in Administrating the Real Estate of Public Institutions Engaged in Research Activities**”.

What is the essence of the draft Concept and why did it cause such an outburst?

In its original version the Concept contained the ways, and most important – the scope of reforming the public sector of research and developments. Following the results of reforming, by the year 2008, as many as 400-700 organizations will remain in federal ownership, including 100-200 public research institutions and 300-500 organizations representing “infrastructural component” of the public sector of science. This is substantial reduction because now, more than 450 are only RAS institutions, not to mention departmental research organizations, academic institutions functioning at the higher education establishments, and State Unitary enterprises – in all, over 2.8 thousand organizations being in public ownership. It is just those figures of reduction, as well as unclear criteria of institution selection caused protests against the Concept among the ordinary scientists and heads of research institutions.

Moreover, The Academy took the Concept as a new attack on RAS status because, in fact, the substantial reduction of academic institutions within jurisdiction of RAS meant that the the Presidium of RAS actually loses its chances to possess public ownership. At the same time, it is a long time already that the problem of RAS legal status needs to be solved. Being, so far, a self-governing organization, the Academy enjoys privileges of a public office.

The draft Concept for reforming the public sector comprises six sections. The first is intended for analyzing the state of the public sector of science. In so doing, the inventory figures of 2001 are used here. No doubt that this is somewhat outdated information, but, unfortunately, only this information can be used, because only thanks to non-recurrent inventory that the data were first obtained about the scientific organizations depending on their legal form. The annually collected data of the system of State statistics concerning the state of science do not contain the information of legal form of research organizations.

In the second section of the Concept, the tasks, goals and principles of the RF participation are defined in administration of the public research institutions. It should be said that the goals of the original Concept version differ considerably from those stated in the new Concept version. So, the following goals were projected in the first version: (1) achieving breakthrough on the priority directions of science, technology and engineering; (2) securing competitiveness; (3) developing human potential of science; (4) optimization of the organizational and financial costs of the State for administration of the research institutions; (5) enhancing the budgetary efficiency of use of state ownership. As is seen from the list, the last two goals explained, to some extent, why it is planned to reform the public sector of science. On the whole, the list of goals added no new information, in comparison with similar precursor-documents (like “The RF Policy Basics in the Field of Science and Technology for a Period until the year 2010 and for Future Periods” adopted in 2002).

However, the second version is by far retires from the idea of the public sector reformation and focuses on the need of government support of science on the whole, increase of the research potential, and the development of fundamental science, in particular. In this case, the five new goals taken together look all the more eclectic: (1) increasing the role of science for solving the national task of doubling the gross domestic product; (2) enhancing the quality of basic research; (3) maintaining and increasing the science and technology potential of the country; (4) complex development of the national innovation system; (5) creating conditions for development and increasing the competitiveness of “human capital”. And though the new Concept focuses just on administration of the real estate, the goal of enhancing budget efficiency of use of state ownership, formulated in the first version of the Concept, was removed in the last version.

The third section defines a set of criteria for keeping an organization as part of the public sector of science. Such criteria are subdivided into basic and additional, stated in most general terms. Here the most considerable oversight is that a number of criteria are declarative (for example, one of them runs like this: “the institution property in the mid-term outlook is planned to use within the limits of sector restructuring”), also, it is not defined who and how will use these criteria in assessment and the choice of institution.

The fourth section is completely different in the original and new Concept versions. In the primary version (the fourth section) the list of mechanisms is provided reducing the State involvement in organizations’ activities and 11 main methods of reforming considered, while in the new Concept version this section is, in fact, given in Annex 2 as auxiliary information. It is notable that there will be fewer variants for institutions’ reforming: if earlier they were intended to be transformed into funds, autonomous non-commercial organizations, joint-stock companies, or sell the institutions real estate as a whole, the new version suggests that State-owned institutions will be transformed only to a fund or an autonomous non-commercial organization.

In the new Concept version the fourth section is radically new. It is entitled “Specifics of Administration of the Real Estate of the Russian Academy of Sciences and Governmental Branch Academies Having Public Status”. As is evident from this section that RAS not only reserves all its functions, but also acquires new powers. Today, the Academy is not only “the main basic research center of the country”, but it also maintains high standards of those directions of the applied science “which progress is assumed by the State”. In addition, RAS becomes a coordinator of basic research performed elsewhere: in higher education establishments, state research centers, governmental branch academies. In accordance with its grown (even in comparison with the Charter of RAS) powers, RAS will itself optimize the composition of the institutions and organizations (within its jurisdiction), develop the criteria of institutions’ effective work, as well as “specific actions plan to administrate the real estate”.

In the fifth section, the terms (reasons) are defined for taking decisions by the Federal Bodies of Executive Power on stopping the RF involvement in administration of public research institutions. Here it is described, in sufficient detail (the first version) or in outline, with details given in Annex 3 (the second version), what exactly are the terms to be taken into account in deciding on transformation of an institution or a State unitary enterprise into a new legal form.

The six and final section is entitled “Basic Trends of Transformation of the Public Sector of Science and Its Future “Appearance””. Six directions of transformation of the Public Sector of Science were reviewed in the first version of the concept: reduction of the number of federal research institutions and their integration; rationalization of the public sector of science at the levels of the budgetary

system (transfer of a part of state research institutions from federal ownership into possession of the RF subjects); optimization of the legal forms of public research institutions (i.e., transformation of institutions and FGUP(s) into those legal forms which description underlies the first Concept version); optimization of the extent of government involvement in the capital of public research institutions; optimization and restructuring of the real estate of public research organizations; functional restructuring. The last direction suggested creation of a system of base institutions and universities, development of college sciences based on integration of the educational and research organizations, creation of federal centers of science and high technologies, development of elements of innovation infrastructure, including creation of federal "Fund of Funds".

The new Concept version numbers five directions (the direction is omitted relating to "reduction of the number of federal research institutions and their integration" and changed their order). The first direction is now a functional restructuring suggesting the development of universities and academic institutions engaged in basis research, creation of integration structures, the federal centers of science and high technologies, as well as elements of innovation infrastructure (including creation of federal "Fund of Funds").

It is to be noted that in both versions of the Concept all the directions are given in outline. For example, it is absolutely not clear –who a research organizations will be subordinate to - federal center or the RF subjects. Also, the list of new forms of organizations is also questionable, as some of them (namely, the federal centers of science and high technologies)¹² have failed and their creation was stopped for this reason. Suggestion to establish a Fund of funds is also strange, as such a Fund (called Venture Innovation Fund) was already established in 2000 and so far is inefficient (the reason also includes inadequate public funding at the initial stage).

The only concrete milestone in the new Concept version is as follows: it is planned that by the year 2006 that the number of budget-funded research institutions will be cut/decreased to 800 (55%). In which case, the data contained in the first concept version that 100-200 organizations will be left as federal property, which caused the most stormy reaction, were removed from the new version. Instead, the data appeared of the planned (in 2008) specific finance indexation of federal science: the minimum budgetary spending for one research worker will be 700-750 thousand rubles per annum (prices of 2004). Here the number of research personnel of budgetary organizations will be determined with due regard for the necessity of observing this index. This may be considered as the only oversight of RAS in its struggle for keeping its all authorities and privileges: given that now, according to the Ministry of Education and Science, the budgetary spending of a research worker is 133 thousand rubles per year¹³, even if the planned growth of science budgetary allocation (to 110 bln roubles by 2008 vs 46.2 bln roubles in 2004) has been taken into account, achieving the budgetary spending index, specified in the Concept, will require at least twice as much to cut the scientific personnel in the federal science.

On the whole, transformation of the Concept may be regarded as RAS political victory in the struggle of maintaining a status quo. If the first Concept version deserves criticism as being not thoroughly studied? but still a variant of reforming the public sector, then, in reality, the second version leads the reform to only transformation of FGUP(s), and to "cosmetic" (not affecting the interests of the Academy) integration of the academic and college sciences, which criteria are not clear. As regards the State research centers, forming in the prior version at least a part of the "core" of science, in the new version no special intention of the government are known in this regard. It is characteristic that just the State research centers are today the organizations engaged in priority applied research for the State, which, according to the Concept new version, are to be (to some extent) in possession of RAS.

Though, there are more general problems underlying both Concepts.

1. It is not clear, what is the purpose of optimization of the administration of the real estate of public institutions. No government document clearly stated its position relative to the model of science it would like to have in the new economic situation. To what extent the science plans to focus on researches in the field of national security and defence? How far will it be innovation-oriented? Answer-

¹² See in more detail Dezhina I., Saltykov B. Incentive mechanisms of R&D Commercialization. Monography. M.: IET, nauchnye trudy No.72R, 2004, pp. 87-88.

¹³ Poisk, No.№40, October 1, 2004., p.c.2.

ing these important questions will determine the extent and manner in which transformations are to be conducted in the public sector.

2. The offered directions and methods of transformation of the institutions and FGUP(s) into other legal forms do not take into account the possibility of introducing two new forms of public organizations – autonomous institution and government (municipal) autonomous non-commercial organization. Currently, a package of respective draft laws is discussed in the government. Such forms of organizations are very actual for the sphere of science and their introduction may substantially optimize the organizational transformations of research organizations. In this case, all the transformation schemes, described in the concept, will have to be revised, as the Concept is a document for the future, and not a guideline for immediate action, it must take into account the possibility of introduction of new legal forms.

3. All amendments made to the Concept, goes to prove that real reforms are put off to an indefinite period. First, an academic sector will be maintained – and this is a dominating segment of a “base”, that is – organizations having budgetary funding regardless of the type and results of their activities. Second, according to explanations of the leadership of the Ministry of Education and Science, none of existing institutions will be closed. They will be enlarged through integration with the educational and industrial organizations. Such an approach is not promising, because large research institutions are not an optimal form of institution’s effective functioning in the current scientific sphere. They are not flexible and practise a bureaucratic style of activity, possessing excessively inflated staffs of various auxiliary and servicing subdivisions. So, an “epidemic” enlargement of institutions will keep unsolved the previous problems and will give rise to new ones. In particular, enlargement does not solve the problem of optimization of the staff of research organizations.

I.Dezhina

Issues Reviewed at the Sessions of the RF Government on October 7, 12 and 21, 2004

Of all issues reviewed by the Government in October the most interesting are as follows. At October 7 session, the Minister of Transport of the RF, Levitin I.E. rendered a report “On Improving the Funding Mechanisms of Large Nationwide Projects in the Field of Transport Infrastructure Development”, related to major development trends of the country’s transport infrastructure. At the session of the Government of the RF of October 12, the draft federal law was considered “On Introducing Changes in the Federal Law “On the Federal Budget for 2004” and Recognizing Inoperative Some Provisions of the RF Acts of Law”. The project’s primary intent was to render financial support to measures aimed to adoption in the current year of new federal statutes, and adjusting the structure of federal bodies of executive power in accordance with the RF President’s Decrees No. 314 of March 9, 2004, and No. 649 of May 20, 2004. At the session of the Government of the RF of October 21, 2004, the Deputy Chairman of the RF Government, Zhukov A.D. rendered a report “On the Course of the Administrative Reform”, concerning optimization of the system of federal public institutions and the federal state unitary enterprises being within jurisdiction of federal bodies of executive power.

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At the session of the Government of the RF of October 7, 2004, the Minister of Transport of the RF, Levitin I.E. read a paper “On Improving Funding Mechanisms of Large Nationwide Projects in the Field of Transport Infrastructure Development”, in which he emphasized that the current state of Russia’s transport infrastructure does not match the demands of rising economy and creates considerable risks.

In this connection, activities have been performed in the Ministry of Transport of the RF to develop Russia’s Transport Strategy for the period until the year 2020, in which the following strategic goals were defined:

- “enhancing commuting services”: development of up-to-date, extended and efficient transport infrastructure ensuring the acceleration of commodity and passenger flows, and lowering transportation costs in the economy;
- “mobility”: raising servicability of the transport complex for population;

- “transit and export”: enhancing competitiveness of the transport system of Russia and implementing the country’s transit potential;
- “safety”: enhancing comprehensive safety and stability of the transport system;
- “investment”: improving the investment climate and developing market relations in the transport complex.

In the context of strategic goals a number of priority projects have been defined in the field of transport infrastructure development, in particular, construction of a new highway and high-speed “Moscow - Saint-Petersburg” railway system, creation of a national system of modern hub airports, etc. Calculations show that the total cost of realization of such projects is around tens billion dollars.

It is noted in the report that work is under way currently to upgrade the the funding mechanisms of large infrastructure projects at the cost of budgetary funds (basically, such projects are government funded).

Transition to mid-term targeting and flexible three-year budget, being introduced currently, will allow to considerably improve the efficiency of budgetary funds, owing to which it would be possible to provide steadiness of funding and short time project commissioning, as well as to cut the volume of funds “blocked” in incomplete construction. At the same time, the mechanisms are corrected of tender holding, carrying out purchases and contract activities aimed at enhancing openness, price optimization and protecting the government interests acting as customer. Control is intensified to observe agreements with the RF subjects on joint funding of investment projects.

Special attention is attached in the report to the issue of attraction of extra-budgetary funds in funding of the transport complex. Proceeding from the Transport strategy, an increase of the share of private investment is intended in this sphere.

In many countries, the main form of funds attraction to infrastructure projects is mechanism of public-private partnerships, which provides the reduction of burdens put on the budget, possibility of implementing socially important projects, which are scarcely interesting for the traditional forms of private financing, and also more quick project realization, as well as their better effectiveness due to business involvement, less public risks, etc.

However, for effective public-private partnership, the more active participation of government is needed, in comparison with other sectors.

In the report, the main distinguishing features are outlined of the institute of public-private partnership:

- integration of the state and private industry for joint provision of socially important services and implementation of socially important projects;
- an alternative decision in comparison with a total hundred-per-cent public servicing or complete privatization;
- maintenance a partnership object in public ownership;
- direct regulation of the only operator activities where it is impossible or inappropriate competitive environment development;
- no secrets in relations with private sector, and selection of commercial counterparties on a competitive basis.

The development of the institute of public-private partnership in the transport system of Russia is encumbered by absence of mechanisms of estimation, approval, and control over implementation of respective agreements; the absence of organs, specifically authorized to fulfill such functions at inter-departmental level; moreover, the “single-window procedure” is not adhered to in conclusion of agreements, while the lease and contract forms of partnership, provided for in the legislation, allow to involve private capital only for the solution of confined scope of tasks.

The report reviews variants of use of an institute of public-private partnership at different types of transport.

In particular, construction and operation of paid automobile roads are defined as the main sphere of use of such partnership mechanisms. In this connection, the draft federal law “On Paid Automobile Roads”, has been elaborated in the Ministry of Transport, which is planned to be submitted soon to the RF Government, for consideration. In order to fulfill the RF President’s instructions concerning implementation of projects for building of paid automobile roads and creation of investment attractiveness of the road facilities, a Working Group for development of paid automobile roads and other infrastructure facilities has been organized in the Ministry of Transport. The Ministry has prepared and

included in the subprogram “Automobile Roads” the Federal Target Program “Modernization of Russia’s Transport Program (2002 - 2010)” an additional section “Public-private Partnership in Construction of Automobile Roads and the Objects of Road Infrastructure”. The section describes priority projects with paid passage to be introduced until the year 2013. At present, the largest and most nationally important project, which is to be funded with participation of extra-budgetary funds, is a project of building a new highway Moscow - Saint-Petersburg (from MKAD (Moscow Ring Road) to KAD (St.-Petersburg Ring Road)).

In addition, examples were given of involving the extra-budgetary funds on the sea and railway transport, civil aviation, and also on the domestic water ways.

At the session of the Government of the RF of **October 12, 2004** the draft federal law “On Introducing Changes in the Federal Law “On the Federal Budget for 2004” and recognizing inoperative some provisions of the acts of law of the Russian Federation”, was considered, which primary intent is finance measures related to adoption in the current year of new federal statutes, other normative legal acts, decrees of the President of the RF, and the decisions of the RF Government not stated in the Federal Law of December 23, 2003 “On the Federal Budget for 2004”, and also adjusting the structure of federal bodies of executive power in accordance with the RF President’s Decrees No. 314 of March 9, 2004, and No. 649 of May 20, 2004.

The draft law parameters are based on indices of previous estimation of the federal budget execution for 9 months of 2004 and its execution forecast made till the end of the year. Within the 9 months of 2004 the federal budget expenditures were specified as based on the data set in Sections 35, 67, 86, 93, 94, 129, 133, 134 and 147 of the law on federal budget for 2004, totaling Rb. 39.77 bn.

An analysis of the execution of revenue side of the federal budget for the 9 months of 2004 and its execution estimates till the end of 2004 gives reason to expect that 2004 will see additional budget revenues worth Rb. 531.0 bn. Such an estimate was made proceeding from the specified forecast of basic indices of Russia’s socio-economic development in the current year, and also the actual revenue collection in January-August, as well as the federal budget revenue estimates for September-October this year.

The favorable foreign economic conjuncture was the major reason for increase of the expected federal budget revenues. Thus, of Rb. 541.6 bn of excess of tax revenues in 2004 over the forecasted tax revenues adopted in the federal budget for 2004, Rb. 429.1 bn account for the tax on extraction of mineral resources and the export customs duty (Rb. 142.6 bn and Rb. 286.5 bn accordingly). As regards taxes depending on the volume of import, increase of tax revenues by Rb. 57.5 bn is expected (VAT - by Rb. 34 bn, import customs duties - by Rb. 22.2 bn, as regards excisable goods and products brought into the RF - Rb. 1.3 bn). At the same time, the favorable foreign economic conjuncture will negatively affect the federal budget revenues. As estimated, VAT compensation will be increased by Rb. 64 bn, as compared to the figure approved at the federal budget for 2004,.

The favorable, in general, macroeconomic situation affected the increase of the taxable profit and, hence, growth of revenues from profit tax of organizations (boosting revenues of Rb. 22.6 bn.-worth is projected). Revenues collection of Rb. 19 bn.-worth is projected from natural gas excise. In addition, in estimation of tax revenues accounts are made for Rb. 16.5 bn.-worth revenues collected from the fuels and lubricants sales tax. It is expected that revenues from levies for use of objects of water biological resources will be by Rb. 2.8 bn less vs. the indicator stipulated in the federal budget for 2004. Decrease of expected sales of excisable motor petrol, compared to the figure computed in the 2004 budget as excise revenues from motor petrol, lowered the revenue collector for this tax by Rb. 2.5 bn, relative to amount introduced as per the law. As regards deviations of expected tax revenues from those stipulated in the federal budget – they are minor and increase tax revenues by Rb. 2.3 bn in absolute terms.

The projected changing of the volume of non-tax revenues of the federal budget in 2004 vs. that enacted as per the law, basically occurred for the following reasons:

- lowering the volume of revenues transferred by the Central Bank of the RF by Rb. 2.2 bn;
- lowering the volume of royalty, including in fulfilling agreements for production sharing by Rb. 19.0 bn, because of lessening the number of issued licenses for the development of the fields according to the results of held tenders;
- boosting revenues from delivery of services or compensation for state expenditures worth a total of Rb. 112 bn. and associated largely with collection from the revenue sources as per the enacted law,-

revenues from commodity interventions from the stock of the Federal Agricultural Produce, Minerals and Food Stuffs Intervention Fund worth a total of Rb. 6.0 bn. (Section 86), and the Rb.1.7 bn.- worth revenues from deductions provided by communication operators (Section 67).

The projection of targeted revenues to the RF Stabilization Fund should make up Rb. 397.4 bn., or at Rb. 313.9 bn. more vs. the respective parameters stipulated in the law. Of them, at the cost of the tax on extraction of mineral resources – Rb. 141.5 bn, export customs oil duties – Rb. 172.4 bn.

The total volume of increase of expenditure of the federal budget for 2004 (without taking into account the “targeted” balances, the need for substitutes of inadequate return of credits and loans, increase of the expenditures because of attraction of additional targeted credits, as well as taking into account the created savings and difference in rates of exchange within the approved budget parameters) worth Rb. 48.6 bn.

Key changes have been made for the following sections of functional classification:

“International Activity” – Rb. 14.9 bn. Major increase in the expenditures under the section is concerned with introduction of corrections into parameters of the Program of State Foreign Loans.

An analysis of the course of the Program for January-August 2004, shows that the use of credits granted domestically made USD 188.0 million, which 11 % exceeds the planned budgetary targets for indicated period. Thus, putting corrections in the Program will allow to accelerate the implementation of priorities, defined by the program of social and economic development of the RF, which require in the shortest possible time to complete funding of projects in the social sphere and those related to ensuring security of the State.

In accordance with the agreement achieved by the heads of the governments of the Republic Belarus and the RF it is necessary to take a decision on granting a public credit, for USD 175 million, to the Republic Belarus for financing a part of deliveries of the Russian natural gas to this republic and provision of balanced mutual trade between the two republics. According to the Budgetary Code of the RF, such an agreement can be concluded only after introducing respective changes in the federal law of the federal budget, i.e. – increase of maximum rate of public credits granted by the RF, and introducing changes in the Program of granting credit.

“Agriculture and Fishery” – Rb. 5.0 bn. These allocations will be directed to increasing of the RF contribution to the authorized fund of the JSC “Rosagrolizin” to supply agricultural manufacturers with farm equipment, by its timely ordering from the manufacturing works.

“Culture, Art and Cinematography” – Rb. 0.39 bn.

“Mass Media” – Rb. 0.54 bn, including for the repayment of credit granted to the All-Russian State Broadcasting Company by Sberbank (Savings Bank) of Russia in accordance with the credit agreement of December 7, 2001 – Rb. 0.5 bn.

“Public Health” – 1.68 bn roubles. Additional expenditures are also provided for in the section for purchasing expensive medicines for treatment of haematological and oncological diseases with children and for children’s liver and kidney transplantation – Rb. 0.5 bn; for purchasing reanimobiles for war veteran’s hospitals – Rb. 0.16 bn; for purchasing medical equipment for war veteran’s hospitals – Rb. 0.82 bn, etc.

The source of such an increase, worth a total of Rb. 1.5 bn roubles, will be funds returned to the federal budget of the Central Electoral Commission of Russia because of savings created after the presidential election campaign (President of the RF).

“Financial Assistance to Other Budgets of the Budgetary System” – 17.86 bn roubles.

Additional allocations provided for in this section are planned for realization of the federal law “On Social Protection of Disabled Persons in the Russian Federation” – Rb. 6.3 bn; increase of the share of the federal budget in the the Fund for Co-financing of Social Expenditures – 3.0 bn roubles; increase of for the RF subjects’ budgets for provision of their budgets’ balance – Rb. 6.6 bn; granting additional subventions and subsidies to the budgets of the RF subjects for road facilities – Rb. 1.39 bn; measures to provide judges and public prosecutors, as well as the participators of the subprogram “Granting Accommodation to Participants of the Radiation Accidents’ and Catastrophes’ Aftereffects” with dwelling space – Rb. 0.57 bn.

“Road Facility” – Rb. 4.75 bn. Additional allocations are assigned for financing the construction and timely commissioning of the federal automobile roads and road infrastructure objects, including KAD (St.-Petersburg Ring Road). For provision of the construction and timely commissioning of pro-

jects having important social and economic importance, additional public capital investments for Rb. 11.86 bn are provided for by the draft law.

Proceeding from the above, the parameters of federal budget for 2004 were made by revenues Rb. 3273.8 bn, expenditures – Rb. 2768.1 bn. The federal budget surplus for 2004 is projected Rb. 505.7 bn.-worth.

At the session of the RF Government of **October 21, 2004**, the paper of the deputy Chairman of the Government of the RF Zhukov A.D. “On the Course of the Administrative reform” **was reviewed related to optimization of a system of federal public institutions and the federal state unitary enterprises within jurisdiction of federal bodies of executive power.**

The work on optimization was organized within the framework of the government commission for carrying out the administrative reform according to the criteria set by commission for **optimization of a system of federal public institutions and the federal state unitary enterprises within jurisdiction of federal bodies of executive power**, and also the shares (interests, deposits) of organizations being in possession of the RF.

The prepared by federal bodies of executive power in collaboration with the Ministry of Economic Development of Russia and the Ministry of Finance of Russia lists have been studied by created at the Commission working groups for optimization of the structure and functions of public organizations performing activities in the spheres of public health and social development, ecology, culture, education and science, economy and finance, industry, energy, transport and communications, defence and security, agriculture and natural resources.

According to the results of the study the lists of the above organizations have been approved by appropriate protocols of the Government Commission for carrying out the administrative reform.

Bolshakova E.A.

A review of regulatory documents concerning taxation, which were made public in August through October of 2004

AUGUST

1. Letter of the RF Tax Ministry No. 21-3-05/367 of August 13, 2004, “On the tax on the property of organizations and the land tax”

This document informs about letter of the RF Ministry of Economic Development and Trade No. D16-665 of July 23, 2004, providing instructions with respect to registration and filing of documents confirming the rights of organizations having mobilization responsibilities as concerns the privileges related to the tax on the property of organizations and the land tax in 2004.

2. Letter of the RF Tax Ministry No. 03-06-04-04/01 of August 25, 2004,

“On the procedures governing the enforcement of provisions of Article 28 of the RF Tax Code “Transportation tax”

This letter explains that for the taxation purposes the term “transport vehicle” as defined in the RF Tax Code is more broad term than the definition set forth in the All-Russian Classifier of fixed assets. Such objects as, for instance, tractors and self-propelled harvesters registered exceptionally with agricultural producers should be not subjected to the transport tax. However, tractors and harvesters registered with other categories of individuals and legal entities should be defined as transport vehicles for taxation purposes.

SEPTEMBER

1. Letter of the RF Tax Ministry No. 04-4-09/1195 of September 1, 2004, “On the stamp tax”

The letter explains that the following amendments set forth by federal law No. 104 FZ of August 20, 2004, “On amendments to Article 4 of the law of the Russian Federation “On the stamp tax” should enter into force since October 26, 2004:

1) there were set forth the rates of the stamp tax exacted by public notaries of state notary offices for certification of agreements concerning mortgages concluded in order to ensure the repayment of credits (loans) granted for purchase of housing at Rub. 200 and other real estate at 0.3 per cent of the amount of the agreement, but no more than Rub. 3000;

2) there were abolished the rates of the stamp tax with respect to state registration of contracts of pledge of real property (mortgage agreements) and the issue of documents about such a registration to

citizens in the amount of 2 minimum wages for each act and to legal entities in the amount of 5 minimum wages for each act;

3) there were abolished the rates of the stamp tax with respect to the issuance of excerpts from the register of state registration of mortgage agreements.

2. Letter of the RF Tax Ministry No. 02-5-11/158 of September 13, 2004,

“On registration of taxpayers’ expenditures relating to the servicing of credit facilities by banks”

A credit facility is a legally registered obligation of a bank (or a similar entity) to the borrower to grant such a borrower credits up to the agreed amount within a certain period of time.

The payment for the possibility to receive financial resources on conditions of credit facility should be defined as expenditures taken into account for the purposes of taxation of profits. At the same time, in accordance with Article 272 of the RF Tax Code, such expenditures should be included in the composition of current expenditures evenly for the period set forth by the conditions of the transaction with respect to the granting of the credit facility.

The said considerations should be not related to the situations where in accordance with the agreement between the parties in the case of granting of credit facilities there is envisaged an increase in the payment for the use of borrowed resources, or the payment for the granting of a credit facility is set forth as a percentage of the total amount of non-repaid credits received by an organization in the framework of a credit facility. In such cases, there should be applied provisions of Article 269 of the RF Tax Code.

3. Letter of the RF Tax Ministry No. 02-5-10/53 of September 15, 2004,

“On the procedures governing the write-off of bad debts with expired periods of limitation for the purposes of taxation of profits”

The letter explains that the writ of execution should be returned to the claimant (in the cases where sanction was not based on the grounds stipulated by sub-items 3 and 4 of paragraph 1 of Article 26 of federal law No. 119 FZ of July 21, 1997 “On executive proceedings,” in particular, in the cases where it proves impossible to find out the address of the debtor organization or place of residence of the debtor individual, the place of location of the debtor’s property, or obtain information about money and other valuables of the debtor being in bank accounts, on deposit in banks, in custody of banks or other credit organizations in the case the debtor has no property or earnings, against which the execution may be levied, while all measures permitted by the law taken by the officer of the law in order to find the debtor’s property or earnings brought no results) does not deprive the claimant of the right to use the writ of execution repeatedly until the date of expiration of its term of validity.

In this connection, the RF Tax Ministry clarifies that the act of the officer of law about the impossibility of exaction and the ruling about the completion of executive proceedings and return of the writ of execution concerning the exaction of tax indebtedness could not be the grounds for recognition of the amount of debtor indebtedness as a bad debt for the purposes of enforcement of the RF Tax Code.

The cases where organizations fail to repeat the submissions of writs of executions in the framework of civil legislation also can not be reviewed in the regime of the expiration of the period of limitation.

Therefore, the amount of debtor indebtedness not exacted in connection to the failure to turn to the officer of law within the period of limitation can not be used in order to diminish the tax base for taxation purposes, since this ground is not mentioned in the list of reasons according to which an indebtedness may be recognized as a bad debt as set forth by item 2 of Article 266 of the RF Tax Code.

The only ground for diminishing of the tax base with respect to such amounts may be a document confirming the fact of exclusion of the debtor from the register of legal entities or liquidation of the claim upon entry into force of a court ruling as concerns the completion of bankruptcy proceedings with respect to the debtor.

4. Letter of the RF Tax Ministry No. 05-1-05/501 of September 22, 2004, “On application of arbitration practices”

The RF Tax Ministry explains that in accordance with the RF Tax Code the payments to employees of organizations financed from the budget should not be subjected to the single social tax in the case such payments were at or below Rub. 2000 per individual in the respective tax period.

The letter defines the term “extra budgetary fund” as state extra budgetary funds formed outside the state budget and budgets of the subjects of the Russian Federation. Therefore, for taxation purposes,

the terms “funds of the budgets” and “funds of the budgets of state extra budgetary funds” should not be similar.

The aforesaid privilege with respect to the taxation of payments made to employees from budgets with the single social tax should not be extended to the payments to employees of agencies of state extra budgetary funds, for instance, the Pension Fund of the Russian Federation (hereinafter referred to as PFR).

In the course of arbitration proceedings concerning the respective disputes, the tax agencies are recommended to support their positions with explanations of the Supreme Court of the Russian Federation No. 2122-1 made public on December 27, 1991, as concerns the formation of the PFR funds, as well as the structure of the revenue and expenditure items of the PFR budget for the respective year as concerns the financing of money salaries of the staff of the Fund at the expense of extra budgetary sources. The attention of the courts should be also called to the fact that the funds transferred to the revenues of the PFR from the federal budget are transferred in accordance with the legislation of the Russian Federation on the strict condition that they should be expended only for the payment of pensions and allowances and should not be expended for the maintenance of the PRF agencies.

5. Letter of the RF Tax Ministry No. 10-0-07/4565 of September 23, 2004, determines the procedures, which should ensure the correct drawing up of accounting documents as concerns the transfer of taxes (fees) and other payments to the budget in connection with order of the RF Ministry of Finance No. 72n of August 27, 2004, which approved the Instructions on the procedures governing the application of the budget classification of the Russian Federation in the course of drawing up and administration of budgets of all levels starting since 2005.

According to these Instructions, the number of symbols in the code of taxes (fees) taxpayers should enter in the field 104 of accounting documents, which relate to transfer of payments to the accounts of revenues and funds of the budgets of all levels of the budget system, should make 20 symbols. The RF Tax Ministry envisages that there should be handed out the respective instructions on the filling in of accounting documents drawn up individually for each taxpayer.

According to Instruction of the Bank of Russia No. 1493 U of August 25, 2004, “On specifics of application of the formats of accounting documents in the course of electronic payments via the payment network of the Bank of Russia,” the maximal length of field 104 of the accounting document was increased to 20 symbols.

Therefore, since January 1, 2005, crediting organizations will not accept the accounting documents, which were filled in incorrectly, since Instruction of the Bank of Russia No. 2 P of December 23, 2002, “On non-cash payments in the Russian Federation” sets forth that accounting documents drawn up not in accordance with the established rules should not be accepted.

6. Letter of the RF Ministry of Finance No. 03-04-08/73 of September 24, 2004, clarifies the procedures governing the refund of penalties arising in connection with the failure to timely submit the documents confirming the lawfulness of application of the zero VAT rate to exported goods.

According to the procedures currently in force, the date, on which in the course of realization of goods for export there originates the right to apply the zero rate of the value added tax should be the date of the stamp of a regional customs office “export permitted” on the freight customs declaration.

In the case of the failure to submit the documents justifying the application of the zero rate of the value added tax during the established period of 180 days and the submission of such documents after the deadline established by the law, the taxpayer should be refunded only the paid amount of the value added tax. The provisions of the Code do not stipulate the refund of the previously paid amounts of penalties.

7. Letter of the RF Tax Ministry No. 22-1-14/1558 of September 27, 2004, “On simplified system of taxation”

The letter explains that in accordance with to federal law No. 129 FZ of November 21, 1996, “On accounting,” the organizations which used the system of taxation in the form of the single tax on imputed income for certain types of activities prior to switching to the simplified system of taxation should be not exempted from the responsibility to keep records in accordance with the standard procedures.

Proceeding from this stipulation, as concerns the organizations using the system of taxation in the form of the single tax on imputed income for certain types of activities, the residual value of fixed

assets at the moment of switching to the simplified system of taxation should be determined basing on the accounting data.

8. Letter of the RF Tax Ministry No. 02-5-11/162 of September 27, 2004,
“On enforcement of the legislation of the Russian Federation”

The letter clarifies that in accordance with the legislation of the Russian Federation, expenditures are defined as any costs on condition that such costs were borne for performance of operations aimed at deriving of proceeds.

Therefore, the costs borne in the framework of operations, which organizations perform in order to derive proceeds, including the costs not resulting in proceeds but necessary for operations resulting in proceeds should be defined as expenditures for the purposes of the RF Tax Code.

Since repairs are a component of the technological process in the framework of operations and is aimed at maintenance of fixed assets in working order, therefore, the amount of depreciation originated during the period of repair of a fixed asset should be also considered as expenditures related to operations aimed at deriving of proceeds.

In the course of performance of operations of seasonal nature, the organization should have the right to include the amount of depreciation of fixed assets originating during the period, in which services were rendered and the period, in which the rendering of services was ceased because of a seasonal factor, in the composition of its expenditures for the purposes of taxation.

9. Order of the RF Tax Ministry No. SAE-3-09/508 of September 29, 2004,

“On establishment of a mass medium for publication of information in accordance with the legislation of the Russian Federation with respect to registration of legal entities”

For the purposes of publication of information contained in the Single state register of legal entities, in accordance with Resolution of the RF Government No. 438 of June 19, 2002, there was established a journal Bulletin of State Registration, which should publish information related to the state registration of legal entities.

10. Resolution of the RF Government No. 506 of September 30, 2004, approved the Regulations concerning the Federal Tax Service

According to the Regulations, the Federal Tax Service (hereinafter referred to as FTS of Russia) is a federal executive authority performing the functions relating to control and supervision of the compliance with the RF legislation on taxes and fees, the correctness of calculation, the fullness and promptitude of other payments to the respective budgets, as well as production and turnover of ethyl alcohol, alcohol containing products, alcoholic beverages, and tobacco products and compliance with the foreign exchange legislation of the Russian Federation within the terms of reference of the tax authorities.

The Tax Service is an authorized federal executive body carrying out state registration of legal entities, individuals as individual entrepreneurs and farmers, as well as an authorized federal executive body representing the Russian Federation as concerns the mandatory payments and state claims relating to money liabilities in the cases of bankruptcy and bankruptcy proceedings.

The Regulations set forth the list of documents, the forms of which are determined by the FTS.

The Federal Tax Service is under the authority of the Ministry of Finance of the Russian Federation.

OCTOBER

1. Letter of the RF Ministry of Finance No. 07-05-14/250 of October 4, 2004, explains that the issues of depreciation of fixed assets purchased for budgetary financial resources should be governed by Accounting Regulations “Accounting related to state aid” No. PBU 13/2000 approved by Order of the RF Ministry of Finance No. 92 n of October 16, 2000.

According to these Regulations, fixed assets purchased for budgetary financial resources should be depreciated in accordance with the standard procedures currently in force.

At the same time, the clarification presented by the RF Ministry of Finance fails to explicitly and unambiguously settle the problem if these regulations are applicable to the fixed assets purchased by budgetary entities for extra budgetary financial resources. Budgetary entities do not use Account 02 referred to in the letter of the RF Ministry of Finance, since for budgetary entities there is set forth a different system of accounts.

2. Letter of the RF Tax Ministry No. 02-3-07/161 of October 12, 2004, explains certain issues related to enforcement of the RF Tax Code.

In accordance with Article 275.1 of the RF Tax Code, the taxpayers, in the composition of which there are separate units engaged in activities relating to the use of auxiliary types of production and

auxiliary businesses should determine their tax bases as concerns the aforesaid activities separately from tax bases pertaining to “other” types of activities.

Comparisons with respect to activities carried out by taxpayers with respect to the use of objects of auxiliary types of production and auxiliary businesses with the operations of organizations created in relation to carrying out of activities pertaining to the use of objects of auxiliary farms, housing and public utilities, social and cultural amenities, training facilities, etc should be conducted for each service.

Expenditures borne with respect to separate units of organizations should be taken into account for the purposes of taxation of profits in amounts of expenditures borne by specialized businesses. At the same time, it should be noted that the tax legislation does not set forth any limitations to the effect that such comparisons should be carried out only with respect to the objects located in the same territory.

3. Letter of the RF Tax Ministry No. 04-5-05/153 of October 12, 2004, clarifies the issues of taxation of earnings of individuals.

In accordance with the provisions of Article 211 of the RF Tax Code, the cases where individuals receive services they pay for at prices below the respective market prices may be viewed as their earnings in kind.

In the cases where payments for education received by individuals at educational establishments are at the market prices of similar services, in the cases where education is paid for at prices below the indicators set forth for the purposes of determination of incomes in kind, the tax base should be calculated as the difference between the established price of education and the actually paid price.

4. Decree of the RF President No. 1315 of October 13, 2004, approves the Regulations concerning the Federal Registration Service.

The Federal Registration Service (Rosregistratsiya) is a federal executive authority performing functions pertaining to the sphere of registration of rights for real estate and respective transactions, registration of public associations and political parties, as well as enforcement functions and functions relating to control and supervision in the sphere of legal profession and notary public.

Rosregistratsiya is under authority of the RF Ministry of Justice.

5. Resolution of the RF Government No. 546 of October 13, 2004, approves the Rules of calculation of the amount of specific subsidies of a foreign state (a union of foreign states).

The rules set forth the procedures governing the calculation of the amount of specific subsidies of a foreign state for the purposes of determination of the amount of the countervailing duty. The calculation of the amount of subsidy is carried out per unit of goods (metric ton, cubic meter, piece, etc) exported to the Russian Federation.

The amount of subsidy per unit of goods is determined proceeding from the amount of expenditures borne by the foreign state for these purposes.

In the course of calculation of the amount of subsidy per unit of goods, the value of the goods is determined as the total value of sales made by the legal entity receiving the subsidy within 12 months, which preceded the reception of the subsidy; at the same time, there should be taken into account the share of subsidized imported good in the total amount of production, sales, or export of such a good.

In the case the subsidy is granted in the form of tax privileges, the value of the goods is determined proceeding from the calculation of the total value of the respective sales within the last 12 months of application of tax privileges.

The subsidies granted by different subsidizing agencies and (or) for implementation of different programs within a year should be summed up.

6. Resolution of the RF Government No. 562 of October 15, 2004, approves the Standard rules of trust management of mortgage coverage. The application of these Rules is necessary for correct determination of the tax base with respect to operations involving property and securities.

L. Anisimova

Review of economic legislation: October of 2004

In October, there were introduced the following changes in the legislation currently in force: amendments pertaining to the regulation of turnover of land owned by religious organization and the rights of these organizations as concerns their participation in the settlement of land related issues; there were approved the Rules governing the management of the RF Stabilization Fund; there were approved the Rules governing the issuance and repayment of state housing certificates in the framework of implementation of the subprogram "State Housing Certificates" in 2004 through 2010; there were presented the new data to be used for the calculation of the mineral extraction tax on oil in September of 2004.

I. FEDERAL LAWS of the Russian Federation

1. "ON AMENDMENTS TO THE LAND CODE OF THE RUSSIAN FEDERATION, THE FEDERAL LAW "ON PUTTING INTO EFFECT OF THE LAND CODE OF THE RUSSIAN FEDERATION" AND THE FEDERAL LAW "ON TURNOVER OF FARM LANDS" No. 123 FZ of October 3, 2004

The said amendments concern the regulation of turnover of land owned by religious organization and the rights of these organizations as concerns their participation in the settlement of land related issues. The law stipulated that in the case a religious organization owns buildings or structures used for religious or charitable purposes situated on the land plots being in the state or municipal ownership, these plots of land should be transferred in the ownership of such a religious organization free of charge. In the case a religious organization has in accordance with federal laws buildings or structures used for religious or charitable purposes basing on the right to use such buildings and structures on a gratis basis, which are situated on the land plots being in the state or municipal ownership, these plots of land should be assigned to such a religious organization basing on the right of limited term free use of these buildings or structures. The re-registration should be completed prior to January 1, 2006. It is stipulated that religious organizations should have the right to take part in the preparation of decisions, implementation of which may affect the state of the land plots in the course of their use and protection, as well as those relating to withdrawals, including buy out of such land plots for state and municipal needs and in the case of issuance of building permits with respect to such plots of land.

2. "ON AMENDMENTS TO ARTICLE 277 OF SECTION TWO OF THE TAX CODE OF THE RUSSIAN FEDERATION" No. 124 FZ of October 4, 2004

Enters into force in one month since the day of promulgation and pertains to legal relationships originated on and after January 1, 2003.

As concerns the title of Article 277 of the second section of the RF Tax Code "Specifics of determination of the tax base with respect to proceeds derived in the course of transfer of property in the authorized (joint) capital (fund) of the organization" the words "(fund) of the organization" should be replaced with words "(fund, property of the fund)." As a result of the introduction of these amendments, the partners in investment funds should be subjected to the same procedure of taxation as is in force with respect to shareholders in joint stock companies, participants of limited liability companies, and partners of production cooperatives, because at present the title of Article 277 of the version of the RF Tax Code currently in force unlawfully limits its enforcement only to the cases of transfer of property within organizations and does not embrace all forms of investment stipulated by the legislation.

II. RESOLUTIONS OF THE GOVERNMENT of the Russian Federation

1. "ON THE PROCEDURES GOVERNING THE MANAGEMENT OF THE STABILIZATION FUND OF THE RUSSIAN FEDERATION" No. 508 of September 30, 2004

In accordance with Article 96.4 of the RF Budget Code, the RF Government approved the Procedures governing the management of the RF Stabilization Fund, which set forth the rules of management of these financial reserves and the list of foreign organizations, whose debt liabilities are eligible for investment of the financial reserves of the RF Stabilization Fund. The management of the financial resources of the Fund should be vested with the RF Ministry of Finance, while certain powers relating to the management of these financial reserves may be delegated to the RF Central Bank acting in ac-

cordance with the agreement on the management of the financial resources of the Fund. The management of the financial reserves of the Fund should include the following operations:

- to purchase permitted foreign exchange (US dollars, Euro, Pound Sterling) at the expense of the financial resources of the Fund denominated in the currency of the Russian Federation;
- to carry out transactions aimed at formation of the investment portfolio and change its structure in compliance with the requirements set forth by the Rules on the part of the RF Central Bank;
- to enter proceeds denominated in permitted foreign exchange derived from the placement of financial resources of the Fund to the accounts formed for the keeping of the record of the financial resources of the Fund.

For the purposes of management of the financial resources of the Fund, the RF Ministry of Finance should form an investment portfolio from the financial resources of the Fund (including proceeds derived from the placement of the Fund's financial resources), which should include cash funds denominated in permitted foreign exchange and debt liabilities of foreign countries (debt liabilities in the form of securities issued by the governments of such countries as Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Luxemburg, the Netherlands, Portugal, Spain, Great Britain, and USA). The resolution also sets forth the requirements pertaining to debt obligations and procedures governing the disclosure of information about the results of investment of the Fund's financial resources, which should in particular include the quarterly reports of the Ministry of Finance submitted to the RF Government as concerns the results of investment of the financial resources of the Fund. The respective reports should be submitted to the RF Government within one month after the end of a quarter.

2. ON CERTAIN ISSUES CONCERNING THE IMPLEMENTATION OF THE SUBPROGRAM "STATE HOUSING CERTIFICATES" IN 2004 THROUGH 2010, BEING A PART OF THE FEDERAL TARGETED PROGRAM "HOUSE" FOR 2002 – 2010" No. 522 of October 7, 2004

The Resolution approved the Rules governing the issuance and repayment of state housing certificates in the framework of implementation of the subprogram "State Housing Certificates" in 2004 through 2010. It sets forth the categories of RF citizens eligible for reception of such certificates and set forth the procedures governing the participation of citizens in this subprogram, determines the list of documents necessary for participation in the program and reception of housing certificates.

The subsidy is granted in an amount equivalent to the estimated cost of the residential space in accordance with the social standard with respect to the total space of residential premises specified for families with different numbers of family members. Since January 1, 2005, the standard cost of 1 square meter of residential space should be determined by the RF Ministry of Industry and Energy once each half year basing on the information presented by the Federal Service of State Statistics and the executive authorities of RF subjects. Prior to January 1, 2005, in the course of calculation of the amount of subsidies, there should be used the indicator of the average market value of 1 square meter of residential space in the Russian Federation determined in accordance with a certain procedure. The Rules also set forth the raising coefficient to be applied to the standard value of 1 square meter of residential space in the Russian Federation in the course of calculation of the amount of the subsidy granted for purchase of residential housing in the territory of individual RF subjects.

The social standard of the total space of residential premises used for the calculation of the amount of the subsidy is set forth as follows: 33 square meters for single citizens; 42 square meters for a family of 2 persons; 18 square meters per person for families consisting of 3 and more persons.

III. INSTRUCTIONS, REGULATIONS, AND ORDERS

1. Informational letter of the RF Tax Ministry No. 21-2-05/122@ of October 20, 2004 "ON CALCULATION OF THE MINERAL EXTRACTION TAX RATE IN SEPTEMBER OF 2004"

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

- the average level of Urals oil prices on the Mediterranean and Rotterdam markets (US \$ 38.21 per barrel);
- value of the Kts coefficient (3.5031);
- tax rate adjusted for the Kts coefficient (Rub. 1215.5757 per metric ton).

I. V. Tolmacheva