

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
April 2004

MONTHLY BULLETIN

Moscow
2004

| | |
|--|----|
| On the progress of reforms in APRIL of 2004 | 3 |
| The State of the Federal Budget..... | 4 |
| Monetary Policy..... | 8 |
| Real Ruble exchange rate in 2003 and the 1 st quarter of 2004..... | 11 |
| Financial Markets | 12 |
| The Real Sector: Factors and Trends | 22 |
| IET Business Survey: Industry in April of 2004 | 25 |
| Foreign Trade..... | 27 |
| April of 2004: Political outcomes | 29 |
| State Individual Financial Obligation (SIFO): problems and prospects of development in the higher education system..... | 31 |
| Issues discussed at the meetings held by the Government of the Russian Federation on April 8, 15, and 21 of 2004 | 34 |
| Review of economic legislation: April of 2004..... | 40 |

On the progress of reforms in APRIL of 2004

In April, the “paralysis” of the Government after the dismissal of M. M. Kasyanov and restructuring of the Government continued. The law making activities and reviewing of legal and regulatory acts on the part of the Government has practically stopped.

However, the Government has discussed a number of important issues. First, there was discussed the draft of the new version of the Forestry Code, which introduced a whole number of most important innovations permitting to considerably improve the efficiency of the forestry activities and create real incentives for the development and improvement of wood working. These innovation included the requirements that forest plots should be provided exceptionally via auctions and the term of lease extended and make 99 years, at the same time, there were made radical changes in the process of approval of forestry related documents: the system of permissions was replaced with declarations. Besides, the system of management and control over forestry was divided and there was introduced a package of other measures.

Since the Prime Minister, the Speaker of the Federation Council, and a number of non-governmental organizations sharply opposed the introduction of private ownership principle in forestry, the initial draft Code, which envisaged that forest plots should be privatized after 15 years of conscientious use, was changed and only indirect references to private ownership were retained. At the same time, the draft Code still permits to privatize forests via a separate law, what is a positive factor.

The second important issue discussed at the meeting of the RF Government was the privatization program, for which the RF Ministry of Economic Development is responsible according to the new Government structure.

In April, the first draft laws out of the number of “national projects” developed at the Center of Strategic Research by the I. I. Shuvalov’s group were ready for the “zero reading.” The draft laws primarily embrace the problems of creation of a market of affordable housing and public health care reform. The most heated debate concerned the draft urban development code, which should remove numerous bureaucratic barriers on the construction market and decrease the respective market entry and business costs in the sphere of housing construction.

It was only natural that the Moscow Government, which completely controls the Moscow housing market and does not want to be deprived of any instruments of control over this market. The second subject of conflict has been the reform of the public health care sphere, where the interests of those satisfied with the present situation (give us more money and everything will be normal), mostly represented by Moscow medical establishment, clash with the interests of those who does not see the ways of development of medicine in the framework of the existing system. There is no doubt that the process of approval of the extremely sensitive issue of the reform of the public health care in the State Duma will be very difficult.

Among other, less significant developments in the sphere of social and economic reforms the following may be mentioned.

In April of 2004, there was approved the federal law on amendments to the federal law “On joint stock companies,” which more clearly defines the sources, from which dividends may be paid. The draft law is aimed at the improvement of investment activities of joint stock companies by implementing effective dividend policies, maintenance of transparency of decision making process as concerns the economic and financial aspects of the operations of Russian enterprises.

The State Duma of the Russian Federation has approved in the first reading the draft federal law on amendments to the federal law “On state regulation of the development of aviation,” which concerns the issue of broader participation of foreign partners in the authorized capitals of the aviation organization.

There was approved in the second reading the draft federal law “On state civil service in the Russian Federation.” Also, there was approved in the first reading the draft federal law on amendments to certain legislative acts in relation to the entry into force of the federal laws “On the state pensions in the Russian Federation” and “On labor pensions in the Russian Federation.”

Also in the first reading there was passed the draft federal law on amendments to articles 2 and 5 of the federal law “On the subsistence level in the Russian Federation,” which excluded the notion of “the minimal retirement pension amount” and the provision envisaging that there should be approved a special federal law setting forth the ratio between the size of the minimal wage and the amount of the subsistence level.

The State Duma of the Russian Federation has passed in the third reading the draft federal law on amendments to section 5 of article 133 of the RF Labor Code, which concerns the procedures governing the determination of the subsistence level.

In April, the Government of the Russian Federation approved the draft Concept of the reform of the budget process in the Russian Federation for years 2004 through 2006 and the draft regulations concerning the results and key guidelines of activities of the subjects of the budget planning.

O. Fomichev

The State of the Federal Budget

In January through February of 2004, the revenues of the federal budget (cash execution) made 19.6 per cent of GDP, while expenditures made 14.4 per cent of GDP (see Table 1). Therefore, the federal budget surplus made 5.2 per cent of GDP.

Table 1.

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

| | I'03 | II'03 | III'03 | IV'03 | V'03 | VI'03 | VII'03 | VIII'03 | IX'03 | X'03 | XI'03 | XII'03 | I'04 | II'04 |
|---|-------|-------|--------|-------|-------|-------|--------|---------|-------|-------|-------|--------|-------|-------|
| Revenues | | | | | | | | | | | | | | |
| Profits tax | 1.2% | 1.1% | 1.4% | 1.5% | 1.4% | 1.4% | 1.4% | 1.3% | 1.3% | 1.3% | 1.3% | 1.3% | 0.9% | 0.7% |
| Income tax | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| Unified social tax (UST) | 2.4% | 2.7% | 2.8% | 2.9% | 2.9% | 2.8% | 2.8% | 2.8% | 2.7% | 2.7% | 2.6% | 2.7% | 2.3% | 2.6% |
| Indirect taxes | 11.2% | 10.1% | 9.9% | 9.6% | 9.6% | 9.2% | 9.1% | 8.9% | 8.7% | 8.6% | 8.5% | 8.5% | 10.5% | 8.5% |
| VAT | 8.5% | 7.4% | 7.2% | 7.2% | 7.2% | 6.9% | 6.9% | 6.8% | 6.7% | 6.6% | 6.6% | 6.6% | 8.1% | 6.6% |
| Excises | 2.7% | 2.7% | 2.6% | 2.4% | 2.3% | 2.2% | 2.2% | 2.1% | 1.9% | 1.9% | 1.9% | 1.9% | 2.3% | 1.8% |
| Taxes on foreign trade and foreign economic transaction | 3.4% | 3.4% | 3.4% | 3.5% | 3.5% | 3.4% | 3.4% | 3.4% | 3.3% | 3.3% | 3.4% | 3.4% | 3.6% | 4.2% |
| Other taxes, fees and levies | 0.5% | 1.7% | 2.0% | 2.2% | 2.1% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.5% | 0.1% |
| Total taxes and other payments ** | 18.8% | 19.0% | 19.4% | 19.6% | 19.4% | 18.8% | 18.7% | 18.4% | 17.9% | 17.9% | 17.9% | 18.0% | 19.9% | 16.1% |
| Non-tax revenues | 17.5% | 8.5% | 1.3% | 1.2% | 1.7% | 1.6% | 1.5% | 1.5% | 1.4% | 1.4% | 1.3% | 1.3% | 0.9% | 0.8% |
| Total revenues | 20.8% | 20.6% | 20.9% | 21.0% | 21.3% | 20.6% | 20.4% | 20.0% | 19.5% | 19.4% | 19.3% | 19.4% | 20.9% | 19.6% |
| Expenditures | | | | | | | | | | | | | | |
| State administration | 0.3% | 0.3% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.4% | 0.5% | 0.2% | 0.3% |
| National defense | 1.5% | 2.1% | 2.6% | 2.7% | 2.7% | 2.6% | 2.6% | 2.6% | 2.5% | 2.5% | 2.5% | 2.7% | 1.8% | 2.2% |
| International activity | -0.3% | 0.0% | 0.2% | 0.2% | 0.3% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | -0.1% | 0.2% |
| Judicial authorities | 0.1% | 0.1% | 0.1% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.1% | 0.1% |
| Legal protection and security | 1.1% | 1.4% | 1.7% | 1.7% | 1.7% | 1.8% | 1.7% | 1.7% | 1.7% | 1.7% | 1.7% | 1.9% | 1.1% | 1.5% |
| Fundamental research | 0.1% | 0.2% | 0.2% | 0.2% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.1% | 0.1% |
| Services to national economy | 0.2% | 0.4% | 0.5% | 0.6% | 0.7% | 0.8% | 0.8% | 0.8% | 0.9% | 0.9% | 0.9% | 1.1% | 0.2% | 0.4% |
| Social services | 1.5% | 1.8% | 2.0% | 2.3% | 2.2% | 2.2% | 2.2% | 2.2% | 2.1% | 2.1% | 2.1% | 2.3% | 1.4% | 1.7% |
| Government debt servicing | 1.7% | 2.9% | 3.0% | 2.3% | 2.1% | 2.0% | 1.8% | 2.0% | 2.0% | 1.8% | 1.7% | 1.7% | 1.1% | 2.1% |
| Other expenditures | 6.6% | 7.1% | 7.0% | 7.0% | 7.1% | 7.1% | 7.1% | 7.0% | 6.9% | 6.8% | 6.8% | 6.9% | 5.3% | 5.8% |
| Total expenditures | 12.7% | 16.4% | 17.7% | 17.7% | 17.7% | 17.5% | 17.4% | 17.3% | 17.1% | 16.8% | 16.7% | 17.7% | 11.1% | 14.4% |
| Surplus (+) / deficit (-) | 8.1% | 4.2% | 3.2% | 3.3% | 3.6% | 3.0% | 3.0% | 2.7% | 2.5% | 2.6% | 2.6% | 1.7% | 9.8% | 5.2% |
| Internal financing | -6.6% | -1.7% | -1.0% | -1.0% | -0.5% | 0.3% | 0.0% | 0.3% | 0.2% | -0.1% | -0.3% | 0.5% | -8.8% | -3.1% |
| External financing | -1.4% | -2.5% | -2.2% | -2.3% | -3.1% | -3.3% | -3.0% | -2.9% | -2.7% | -2.5% | -2.3% | -2.2% | -1.0% | -2.1% |
| Overall financing | -8.1% | -4.2% | -3.2% | -3.3% | -3.6% | -3.0% | -3.0% | -2.7% | -2.5% | -2.6% | -2.6% | -1.7% | -9.8% | -5.2% |

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

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

As compared with the figures registered in the two first months of 2003, the budget revenues decreased by 1.0 p. p. of GDP in the respective period of 2004, while expenditures decreased by 2.0 p. p. and budget surplus respectively increased by 1.0 p. p. of GDP. At the same time, without SST the budgetary revenues decreased by 0.9 p. p. of GDP and made 17.0 per cent of GDP. As before, VAT accounted for the major share of federal tax revenues – 41.0 per cent of the total tax revenues what is practically at the level observed in the respective period of 2003.

According to preliminary estimates, the cash execution of federal budget revenues made 19.8 per cent of GDP in January through March of 2004, what was by 1.1 p. p of GDP below the level observed in the respective period of the preceding year. At the same time, the cash execution of expenditures made 16.1 per cent of GDP (17.7 per cent of GDP in January through March of 2004); therefore, in the first three months of this year, according to preliminary data, the surplus made 3.7 per cent of GDP.

According to the preliminary estimates of the Finance Ministry, in terms of fulfilled funding² the expenditures of the federal budget in January through March of 2004 made 18.0 per cent of GDP (see Table 2), while in the respective period of 2003 this indicator was at 20.9 per cent of GDP. In January through March of 2004, the amount of revenues of the federal budget decreased by 1.1 p. p. of GDP in comparison with the figures registered in the respective months of 2003 and made 19.8 per cent of GDP. Therefore, the surplus of the federal budget in terms of fulfilled funding in January through March of 2004 significantly increased in comparison with the figures registered in January through March of 2003 and made 1.8 per cent of GDP.

Table 2.

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

| | III'03 | IV'03 | V'03 | VI'03 | VII'03 | VIII'03 | IX'03 | X'03 | XI'03 | XII'03 | I'04 | II'04 | III'04 |
|-------------------------------|--------|-------|-------|-------|--------|---------|-------|-------|-------|--------|-------|-------|--------|
| Total expenditures | 20.9% | 21.0% | 21.3% | 20.6% | 20.4% | 20.0% | 19.6% | 19.5% | 19.4% | 19.4% | 20.9% | 20.2% | 19.8% |
| State administration | 0.6% | 0.6% | 0.6% | 0.5% | 0.5% | 0.5% | 0.5% | 0.5% | 0.5% | 0.5% | 0.6% | 0.7% | 0.6% |
| National defense | 3.3% | 3.2% | 3.1% | 3.0% | 2.9% | 2.8% | 2.7% | 2.8% | 2.9% | 2.7% | 2.7% | 4.0% | 2.9% |
| International activity | 0.2% | 0.3% | 0.3% | 0.3% | 0.3% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.0% | 0.2% | 0.2% |
| Judicial authority | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% | 0.2% |
| Legal protection and security | 2.3% | 2.2% | 2.2% | 2.1% | 2.0% | 1.9% | 1.9% | 1.9% | 1.9% | 1.9% | 2.1% | 2.5% | 2.3% |
| Fundamental research | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% | 0.3% |
| Services to national economy | 0.9% | 1.0% | 1.0% | 1.0% | 1.0% | 1.0% | 1.0% | 1.0% | 1.1% | 1.1% | 0.5% | 0.7% | 0.8% |
| Social services | 2.7% | 2.9% | 2.7% | 2.6% | 2.5% | 2.4% | 2.3% | 2.3% | 2.4% | 2.3% | 2.5% | 2.6% | 2.4% |
| Government debt servicing | 3.0% | 2.3% | 2.1% | 2.0% | 1.8% | 2.0% | 2.0% | 1.8% | 1.7% | 1.7% | 1.1% | 2.2% | 2.2% |
| Other expenditures | 7.3% | 7.2% | 7.4% | 7.3% | 7.2% | 7.2% | 7.0% | 6.9% | 6.9% | 7.0% | 5.7% | 6.8% | 6.1% |
| Total expenditures | 20.9% | 20.2% | 19.9% | 19.2% | 18.8% | 18.6% | 18.3% | 18.0% | 18.1% | 17.8% | 15.6% | 20.2% | 18.0% |
| Surplus (+) / deficit (-) | 0.0% | 0.8% | 1.4% | 1.3% | 1.6% | 1.3% | 1.3% | 1.5% | 1.3% | 1.6% | 5.3% | 0.0% | 1.8% |

According to the estimates of the Tax Ministry, in March of 2004 tax revenues of the federal budget made about Rb. 113.7 billion (without the single social tax). In real terms the revenues made 237.1 per cent of the level registered in January of 1999, while the respective indicator was at 265.5 per cent in March of 2003 and 134.8 per cent in March of 2002 (see Table 3).

At the same time, in March of 2004 the revenues generated by the single social tax made Rb. 38.4 billion. Thus, in March of 2004 the RF Tax Ministry transferred to the federal budget taxes and fees amounting to about Rb. 152.1 billion.

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

Table 3.

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

| 1999 | | | | | | | | | | | |
|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| 100,0% | 115,1% | 122,0% | 122,1% | 104,5% | 112,9% | 127,0% | 127,5% | 124,3% | 141,4% | 160,8% | 213,1% |
| 2000 | | | | | | | | | | | |
| I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| 149,3% | 160,5% | 181,3% | 205,8% | 233,1% | 186,9% | 181,0% | 186,4% | 173,1% | 181,1% | 201,7% | 254,1% |
| 2001 | | | | | | | | | | | |
| I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| 204,4% | 198,4% | 227,6% | 267,5% | 252,2% | 233,3% | 231,9% | 235,6% | 219,4% | 237,5% | 247,3% | 360,6% |
| 2002* | | | | | | | | | | | |
| I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| 218,7% | 187,1% | 234,8% | 277,8% | 239,6% | 218,0% | 284,4% | 246,5% | 254,8% | 299,7% | 241,0% | 250,2% |
| 2003* | | | | | | | | | | | |
| I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| 230,0% | 229,2% | 265,5% | 280,4% | 233,2% | 240,0% | 260,4% | 242,6% | 248,7% | 265,6% | 231,0% | 247,9% |
| 2004* | | | | | | | | | | | |
| I | | | | II | | | | III | | | |
| 266,5% | | | | 204,4% | | | | 237,1% | | | |

* Без учета ЕЧН.

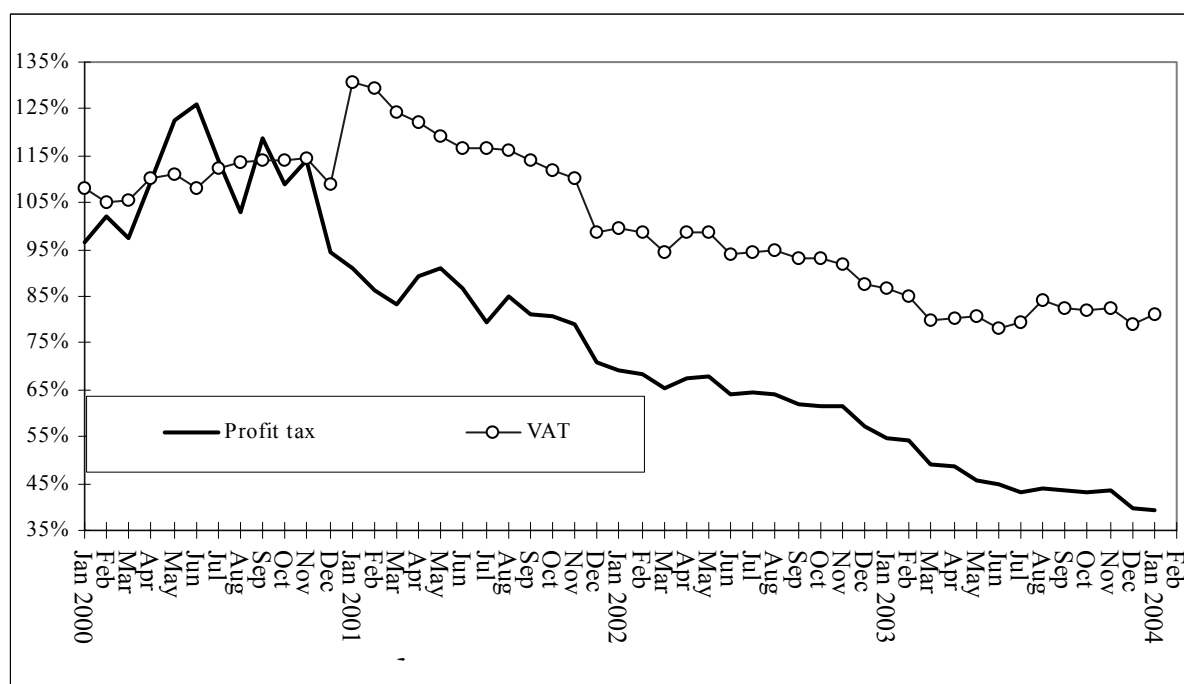


Figure 1. Real tax arrears to the federal budget (in % to July 1999)

The dynamics of real arrears relating to major taxes since January of 2000 are presented in Fig. 1. The debts related to the payments due to the federal budget made for VAT Rb. 256.3 billion as on March 1, 2004, increasing by Rub. 0.6 billion in February of 2004, while the arrears of the profit tax increased only by Rub. 1.6 billion and made Rb. 28.0 billion. On the whole, a gradual decrease in the

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

level of accumulated arrears observed since early 2001 to the second half of 2003 was replaced by the stabilization of the level of accumulated indebtedness as concerns both the profit tax, and VAT.

Table 4

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

| 1998 | | | | | | | | | | | | |
|--------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| Taxes | 16,2% | 17,4% | 18,1% | 19,3% | 19,7% | 19,8% | 19,8% | 19,4% | 18,8% | 18,5% | 18,6% | 19,6% |
| Revenues | 18,8% | 20,1% | 21,2% | 22,4% | 23,0% | 23,2% | 23,2% | 22,9% | 22,3% | 22,0% | 22,0% | 24,5% |
| Expenditures | 25,3% | 23,8% | 27,0% | 28,1% | 28,6% | 29,5% | 29,4% | 28,6% | 27,4% | 26,9% | 27,1% | 29,5% |
| Deficit | -6,5% | -3,7% | -5,8% | -5,7% | -5,7% | -6,3% | -6,2% | -5,7% | -5,2% | -5,0% | -5,0% | -5,1% |
| 1999 | | | | | | | | | | | | |
| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| Taxes | 16,8% | 16,6% | 18,1% | 19,9% | 20,1% | 20,5% | 20,8% | 20,8% | 20,3% | 20,2% | 20,9% | 22,1% |
| Revenues | 19,2% | 18,9% | 20,6% | 22,7% | 23,2% | 23,9% | 24,3% | 24,5% | 24,1% | 24,0% | 24,8% | 26,3% |
| Expenditures | 18,6% | 20,3% | 23,6% | 25,6% | 26,6% | 27,3% | 27,4% | 27,4% | 26,7% | 26,3% | 26,7% | 29,2% |
| Deficit | 0,6% | -1,5% | -3,1% | -3,0% | -3,4% | -3,4% | -3,1% | -2,9% | -2,7% | -2,3% | -1,9% | -2,9% |
| 2000 | | | | | | | | | | | | |
| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| Taxes | 20,8% | 21,4% | 22,6% | 24,2% | 25,5% | 25,4% | 24,9% | 24,8% | 24,1% | 23,7% | 24,0% | 24,6% |
| Revenues | 24,4% | 24,8% | 26,4% | 28,2% | 29,7% | 29,7% | 29,3% | 29,2% | 28,4% | 28,0% | 28,6% | 30,0% |
| Expenditures | 19,6% | 21,1% | 23,8% | 24,8% | 25,2% | 25,5% | 22,3% | 25,1% | 24,5% | 24,2% | 24,6% | 27,0% |
| Deficit | 4,7% | 3,7% | 2,6% | 3,4% | 4,5% | 4,3% | 7,0% | 4,1% | 3,9% | 3,8% | 4,0% | 3,0% |
| 2001 | | | | | | | | | | | | |
| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| Taxes | 22,7% | 23,6% | 23,9% | 25,4% | 26,4% | 26,0% | 26,1% | 25,9% | 25,0% | 24,8% | 25,4% | 27,1% |
| Revenues | 25,9% | 27,1% | 27,4% | 29,3% | 30,5% | 29,8% | 29,9% | 29,7% | 28,3% | 28,2% | 28,8% | 29,5% |
| Expenditures | 16,8% | 22,8% | 23,7% | 24,7% | 25,1% | 25,3% | 25,5% | 25,6% | 24,9% | 24,7% | 25,0% | 25,6% |
| Deficit | 9,1% | 4,2% | 3,7% | 4,7% | 5,4% | 4,4% | 4,4% | 4,1% | 3,5% | 3,5% | 3,8% | 3,9% |
| 2002 | | | | | | | | | | | | |
| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| Taxes | 28,7% | 23,6% | 24,3% | 26,5% | 26,6% | 25,9% | 26,4% | 25,9% | 25,2% | 25,4% | 25,4% | 25,5% |
| Revenues | 32,9% | 31,3% | 31,4% | 33,6% | 33,6% | 32,7% | 33,3% | 32,5% | 31,7% | 32,0% | 32,1% | 32,1% |
| Expenditures | 18,3% | 23,7% | 26,0% | 28,4% | 28,4% | 28,8% | 29,1% | 28,9% | 28,4% | 29,3% | 29,7% | 31,1% |
| Deficit | 14,6% | 7,7% | 5,4% | 5,3% | 5,2% | 3,8% | 4,2% | 3,7% | 3,3% | 2,7% | 2,4% | 1,0% |
| 2003 | | | | | | | | | | | | |
| | I | II | III | IV | V | VI | VII | VIII | IX | X | XI | XII |
| Taxes | 25,6% | 24,4% | 25,6% | 27,4% | 27,1% | 26,0% | 26,1% | 25,7% | 26,0% | 25,1% | 25,1% | 25,2% |
| Revenues | 32,0% | 30,3% | 31,5% | 33,4% | 33,6% | 32,2% | 32,2% | 31,6% | 29,9% | 29,8% | 29,7% | 31,1% |
| Expenditures | 20,7% | 25,3% | 27,7% | 28,8% | 28,8% | 28,6% | 28,7% | 28,5% | 28,2% | 27,8% | 27,9% | 29,7% |
| Deficit | 11,3% | 5,0% | 3,8% | 4,5% | 4,7% | 3,5% | 3,6% | 3,1% | 2,7% | 2,0% | 2,8% | 1,4% |
| 2004 | | | | | | | | | | | | |
| | I | | | | | | II | | | | | |
| Taxes | 25,6% | | | | | | 20,6% | | | | | |
| Revenues | 30,6% | | | | | | 28,2% | | | | | |
| Expenditures | 18,5% | | | | | | 22,8% | | | | | |
| Deficit | 12,1% | | | | | | 5,4% | | | | | |

* Без учета ECH

The revenues of the consolidated budget in January through February of 2004 made 28.2 per cent of GDP, including tax revenues (without SST) at 20.6 per cent of GDP (see Table 4). Expenditures of the consolidated budget decreased by 2.5 p. p. of GDP in comparison with the figures registered in January through February of 2003 and made 22.8 per cent of GDP. As on March 1, 2004, the surplus of the consolidated budget made 5.4 per cent of GDP, what is by 0.4 p. p. of GDP above the level observed in the respective period of 2003.

A. Razin

Monetary Policy

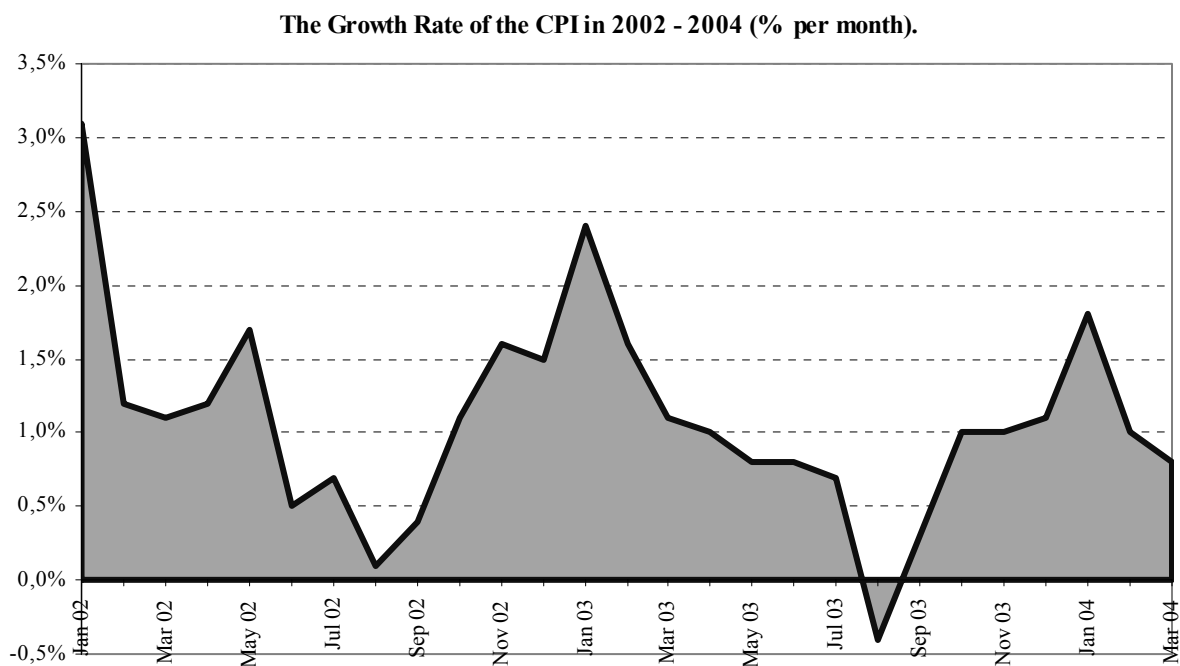
In March, the rates of growth in consumer prices continued to slow down and made 0.8 per cent by the end of the month (as compared with 1.8 per cent and 1.0 per cent registered in January and February respectively, see *Fig. 1*). So, in the 1st quarter of 2004 the rates of inflation were significantly below the levels observed in the last year (as compared with 2.4 per cent and 1.6 per cent registered in January and February of 2003 respectively). The factors behind the decline in the inflation rates were moderate rates of growth in the regulated tariffs, which were below the levels registered in the respective period of 2003 by 1.3 percentage points. At the same time, the base inflation rates was just slightly below the level observed in 2003 (0.8 per cent monthly in the 1st quarter as compared with 0.9 per cent a month in the last year). However, the base inflation rates also gradually continue to decline for the fourth month running (0.8 per cent and 0.7 per cent registered in February and March respectively).

The monetary pressure on the base inflation is mounting, what is the difference between the situations observed in March and April in comparison with the developments occurring in the first months of the year. While in the beginning of the year consumer prices were affected by the increase in the amount of cash registered in the 3rd quarter of the preceding year (1.4 per cent a month on the average), at present there is felt the impact of the sharp growth in the amount of cash observed in the 4th quarter (6.2 per cent a month on the average). Respectively, the major factor constraining the base inflation rates is the deceleration of turnover of cash, which is caused by the dedollarization of the economy persisting in spite of the stabilization of the US \$ exchange rate. According to the data published by the Bank of Russia, in the 1st quarter the balance of forex denominated cash declined by US \$ 3.5 billion (as compared with a decrease by US \$ 0.8 billion observed in the 1st quarter of 2003). As a result, the cash turnover rate registered in the 1st quarter reached its maximum over the last three years.

In March, the administratively regulated tariffs practically did not change (0.6 per cent as compared with 1.9 per cent registered in February). The major factor behind these developments was the stability of tariffs on housing and public utilities (0.4 per cent as compared with 2.8 per cent observed in February). This stability primarily resulted from the administrative factor at work in the regions. Additional constraint on the rise in prices of housing and public utilities services is the decision taken in a number of RF subjects to temporarily freeze tariffs on electrical power consumed by households (until May 1, 2004). In March, the prices of food products increased by 1.1 per cent and of non-food goods – by 0.4 per cent.

According to preliminary estimates, in March inflation rates were at or below 0.8 per cent to 1.0 per cent.

Figure 1.

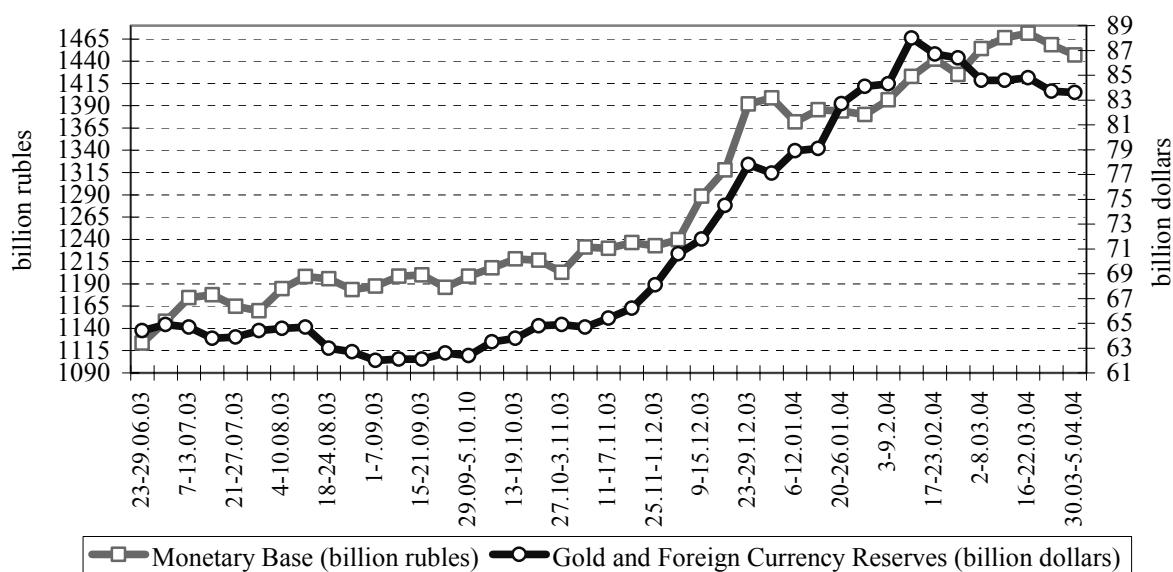


As on April 1, 2004, the amount of gold and foreign exchange reserves of the Russian monetary authorities made US \$ 83.4 billion (see *Figure 2*), what was by 3.4 per cent below the amount of gold and foreign exchange reserves registered on March 1 of this year. As on April 1, 2004, out of the total amount of international reserve assets at the disposal of the Russian monetary authorities the reserve assets denominated in foreign exchange made US \$ 79.6 billion, what was by 4 per cent below the level observed on March 1, 2004. In the second half of April, the amount of gold and foreign exchange reserves continued to decrease, what was primarily due to the considerable payments related to the external debt. As on January 1, 2004, the amount of international reserve assets made US \$ 76.9 billion.

As on April 1 of 2004, the monetary base of the Russian Federation in the broad definition⁴ increased by 1.2 per cent and made RUR 1936.6 billion as on April 1, 2004. The growth made 50.8 per cent as compared with the figures registered on the respective day of the preceding year. It should be noted that in the 1st quarter of 2003 there were observed higher rates of increase in the broadly defined monetary base (4.2 per cent). At the same time, over the period under observation the amount of cash in circulation declined by 1.9 per cent, while in 2004 it grew by 0.8 per cent. Therefore, for the first time in the few past years, in the 1st quarter of 2004 there was observed an increase in the amount of cash in circulation as a share of the monetary base. The rates of growth in the mandatory reserves in the 1st quarter of 2004 declined somewhat in comparison with the figures registered in the preceding year (from 8.9 per cent in 2003 to 7.9 per cent in 2004) what may be an evidence of a deceleration of accumulation of the non-cash monetary stock on the part of Russian banks.

Figure 2.

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



However, a more moderate increase in the broadly defined monetary base in the 1st quarter of 2004 in comparison with the figures registered in the respective period of the preceding year should not be seen as the unambiguous evidence of the lowering threat of inflation. The major factor behind these developments is the dynamics of the amounts of cash and mandatory reserves, therefore in this case the narrowly defined monetary base would be a better set of data for our analysis. In the 1st quarter of 2004, the narrow monetary base grew by 4.8 per cent (from RUR 1392.1 to RUR 1458.5, see *Fig. 2*). In the respective period of 2003, the narrowly defined monetary base increased by 1.1 per cent, while in the 4th quarter of the past year the growth made 17.4 per cent. The decline in the rates of growth in the monetary base appears to be caused

⁴ 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.

primarily by the decelerating rates of increase in the gold and foreign exchange reserves of the Bank of Russia.

In April of 2004, Russia paid about US \$ 698 million as disbursement of its public foreign debt, US \$ 236.8 were paid to the official creditor countries, what included US \$ 221.2 million transferred as debt repayment and US \$ 15.6 million as interest payments. The payments to international financial institutions made US \$ 461.2 million: 413.8 million as debt repayment and US \$ 47.4 million as interest payments respectively. In April, there were no payments relating to RF Eurobonds OVGZ and OGVZ of 1999.

In 2003, the public foreign debt of the RF to nonresidents in US \$ equivalent increased by 18.8 per cent and made US \$ 182 billion. As on January 1, 2004, the amount of the RF debt denominated in foreign exchange made US \$ 176 billion, what is by 18.3 per cent above the figures registered a year ago, while the Ruble denominated debt increased by 31.1 per cent over 2003 and made US \$ 5.9 billion. As on January 1, 2004, the short term liabilities made US \$ 37.3 billion (a 39.2 per cent growth in 2003), while long term liabilities made US \$ 126.5 billion (+ 14.4 per cent). As on January 1, 2004, the liabilities of the state administration sector made the bulk of the RF public foreign debt (over 54 per cent), the amount of these obligations increased by US \$ 1.3 billion over the past year making US \$ 99 billion. This amount includes the debt of the RF Government (US \$ 97.8 billion) and the debts of the RF subjects (US \$ 1.2 billion).

The structure of the foreign liabilities of the federal administration bodies was dominated by the debt accepted by Russia as the successor of the former Soviet Union, which made US \$ 57.9 billion as on January 1, 2004. This amount included the debt to the Paris Club member countries (US \$ 42.7 billion, this debt increased by US \$ 3.5 billion as compared with the figures registered as on January 1, 2003), liabilities relating to the former socialist countries (US \$ 3.6 billion, a decrease by US \$ 0.6 billion), OVGZ (III through V tranches, US \$ 1.4 billion, a decrease by US \$ 0.8 billion), other foreign liabilities including the debt to the countries not being the members of the Paris Club, International Investment Bank, International Bank for Economic Cooperation, and commercial debt (US \$ 10.3 billion).

As on January 1, 2004, the new Russia's debt was evaluated to make US \$ 39.8 billion (by US \$ 1.2 below the figures registered in the preceding year). The bulk of this debt made securities denominated in foreign exchange (US \$ 26.8 billion) and borrowings from international financial organizations (US \$ 6.6 billion).

In 2003, the debt of the RF monetary authorities to nonresidents increased insignificantly – from US \$ 7.5 billion to US \$ 7.8 billion. The foreign debt of the Russian banking system grew by 74.6 per cent making US \$ 24.8 billion by the end of 2003. The amount of foreign debt of the Russian banking system falling in two major categories increased: borrowings grew from US \$ 5.3 billion to US \$ 12.9 billion over 2003, while balances of current accounts and deposits increased from US \$ 6 billion to US \$ 9.6 billion. Debt liabilities of the sector of non-financial enterprises made US \$ 50.3 billion increasing by 48.8 per cent over 2003.

The total amount of the RF debt to the International Monetary Fund due in 2004 makes about US \$ 1.7 billion (SDR 1.2 billion). This amount includes US \$ 1.6 billion to be transferred as debt repayment (SDR 1.1 billion) and US \$ 94.8 million as interest payments (SDR 64 billion). It should be reminded that in 2003 Russia transferred to the IMF about US \$ 2.2 billion as debt repayment.

According to the statements made by the RF Central Bank management, in the nearest future the Bank of Russia is going to begin to use a new exchange rate benchmark. The Bank of Russia will use this operational benchmark in order to determine its goals in the sphere of exchange rate policy and elaboration of more flexible policies. The Bank of Russia plans to introduce this new benchmark in the few next weeks.

At present, the bank feels the need to introduce a new exchange rate benchmark, which would be reasonably transparent, easily used and evaluated, representative and sensitive. The new exchange rate benchmark will be a geometric weighted mean of exchange rates of foreign currencies against the Ruble. US dollar and Euro will be used as the major components of the new benchmark. Initially, the share of Euro in the benchmark composition should be about 10 to 20 per cent. At the same time, the Bank of Russia is aiming not to create new markets, but to keep the stability of the exchange rates. The RUR / US \$ and RUR / Euro should be preserved on the market, and the RF Central Bank has not powers to abolish these instruments. However, the new exchange rate benchmark will allow to better take into account the Euro exchange rates dynamics, while volatility of the US \$ exchange rate will become more volatile.

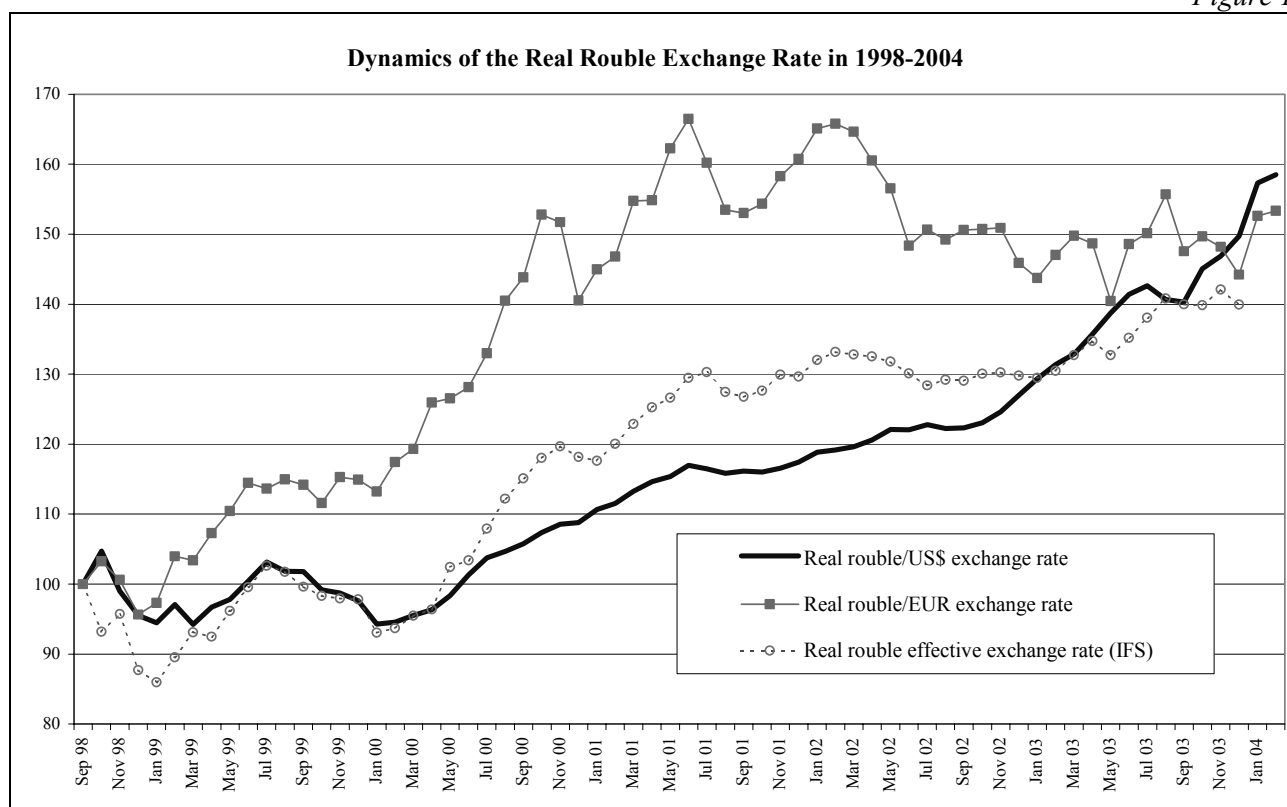
P. Trounin

Real Ruble exchange rate in 2003 and the 1st quarter of 2004

Over 2003, there was observed a rather rapid real Ruble exchange rate appreciation (see *Fig. 1*). Thus, the real Ruble exchange rate against the US Dollar calculated on the basis of changes in the nominal exchange rate and the data on the consumer price indices in Russian and the USA increased by 18.6 per cent, while the similar indicator calculated on the basis of the changes in the Euro / Ruble exchange rate and in the Euro zone has on the contrary declined by 1.25 per cent. The real effective Ruble exchange rate (against the currency basket of main trade partners) published by the IMF increased by 7.8 per cent in 2003, or by about 40 per cent as compared with the level registered in September of 1998. therefore, over 5.5 years (after the crisis and devaluation of the Ruble in August of 1998) the average real effective Ruble appreciation makes about 6.5 per cent a year, what is only slightly above the Ruble appreciation rates determined by the RF Government as acceptable (5 per cent to 6 per cent a year).

However, in the 1st quarter of 2004, the rate of the real Ruble appreciation accelerated significantly. Thus, in January through March of 2004, the real Ruble exchange rate against the US Dollar increased by 5.9 per cent and against Euro – by 6.3 per cent. Therefore, in the annual terms the Ruble appreciation (including against the currency basket) may make over 25 per cent. It is apparent that these rates of appreciation of the Russian national currency may pose a threat to the competitive capacity of Russian producers. In order to check the Ruble appreciation, the RF Central Bank will probably increase its Ruble interventions on the foreign exchange market to support the nominal exchange rate of the Ruble. Therefore, the gold and foreign exchange reserves of the RF Central Bank should grow. At the same time, due to the time lag between the expansion of money supply and acceleration of inflation it may be expected that the real Ruble appreciation will slow down over 2004.

Figure 1



Source: International Financial Statistics, IET calculations basing on the data presented by RF Goskomstat and RF Central Bank.

For the purposes of more thorough analysis of the structure of growth in the real effective Ruble exchange rate, in the few last years we have calculated relative changes in the nominal and bilateral real Ruble exchange rate against major world currencies (US \$, Euro, British Pound, Japan Yen, and Swiss Franc) and national currencies of the Russian major CIS trading partners and competitors (Ukraine and Kazakhstan).

The positive sign of the change means Ruble appreciation (nominal or real), while negative sign means Ruble devaluation. For the results of these calculations in 2001 through 2003, see *Table 1*.

As the Table demonstrates, the most intensive Ruble appreciation against the majority of currencies (with the exception of the US Dollar and the Ukraine Hryvna) was observed not in 2002 through 2003, but in 2001. According to the results of the period from 2002 to 2003, in real terms the Ruble depreciated not only against the Euro, but also against the Swiss Franc, while the Ruble / British Pound exchange rate practically did not change. In other words, although it is impossible to single out the relative impact of each factor, the Ruble appreciation against the US Dollar observed in 2003 might be to a considerable extent caused by the US Dollar depreciation against other world currencies and should not be explained only in terms of the RF balance of trade situation. In the course of analysis of the dynamics of the Ruble exchange rates against other leading world currencies over the last 2 to 3 years, it becomes apparent that in spite of the excess of supply of foreign exchange over demand on the domestic market, the changes in the nominal Ruble exchange rates in this period approximately answers the PPP condition, i.e. the nominal change in the exchange rate of a national currency is equal to the ratio between the rates of inflation in the country and abroad. Annual increments in the real bilateral Ruble exchange rates against foreign currencies do not exceed 2 per cent to 4 per cent.

Table 1

Relative changes in the Ruble exchange rates against major world currencies and currencies of certain CIS member countries in 2001 through 2003

| | 2001 – 2003 | | 2002 – 2003 | |
|-----------------------|-----------------------|-------------------------|-----------------------|-------------------------|
| | Nominal exchange rate | Bilateral exchange rate | Nominal exchange rate | Bilateral exchange rate |
| US Dollar | -4,60% | +26,56% | +2,27% | +20,73% |
| Euro | -40,87% | +1,27% | -39,01% | -13,35% |
| British Pound | -24,46% | +12,70% | -19,84% | +1,92% |
| Japan Yen | -12,16% | +28,00% | -20,40% | +7,49% |
| Swiss Franc | -37,12% | +8,21% | -32,14% | -4,07% |
| Ukraine Hryvna | -7,31% | +9,65% | +2,83% | +13,22% |
| Kazakh Tenge | -5,69% | +12,25% | -2,46% | +6,73% |

Source: IET calculations basing on the data presented by RF Goskomstat, RF Central Bank, and International Financial Statistics.

The only exceptions are Ukraine and, probably, China (the latter was not included in the Table because of the unavailability of the data on the Ruble / Yuan exchange rates and inflation in China). We believe that this situation may be explained by the fact that these currencies are pegged to the US Dollar (openly in China) and the changes in the respective exchange rates just follow the dynamics of the Ruble / US Dollar exchange rate.

In this connection, it may be assumed that in the case the US Dollar appreciates on the world currency markets in 2004, the trend observed on the Russian domestic market may reverse, i.e. the Ruble will depreciate against both the Euro and other currencies, and the US Dollar in spite of persisting considerable current account surplus. For instance, in the case the US Dollar appreciates to US \$ 1.10 to 1.15 per Euro by the end of the year (as compared to US \$ 1.25 per Euro exchange rate registered in December of 2003 through January of 2004), the nominal Ruble / US Dollar exchange rate may make Rub. 30.5 to 31.0 per US Dollar in the last quarter of 2004, i.e. return to the levels observed in the first six months of 2003.

S.. Drobyshevsky

Financial Markets

In April, a significant adjustment was observed on the Russian stock market. By the end of the third week of the month, the RTS index declined by about 100 points as compared with the maximum observed on April 12. A certain decline in prices was observed also on the debt market. The major factors behind the dynamics of the stock market in April were the deteriorating liquidity situation in the banking sector, US Dollar appreciation against Ruble, and the further development of the YUKOS affair.

The Market for Government Securities

In April, on the market of foreign public debt there was observed a growth in the yields of government forex denominated bonds. The increasing volatility on the world forex market, as well as significant fluctuations of prices of base assets (US Treasury Bills) facilitated the increase in the yields of Russian forex denominated bonds.

Thus, as on April 23 the yield to maturity of Russian Eurobonds RUS-30 was 7.48 per cent p.a. (end of March: 6.88 per cent); RUS-18: 7.13 per cent p.a. (end of March: 6.86 per cent). Besides, on the same date the yield to maturity of the Russian Eurobonds was: Minfin bonds, 7th tranche: 6.59 per cent; Minfin bonds, 6th tranche: 4.08 per cent; Minfin bonds, 5th tranche: 5.69 per cent; RUS-07: 4.45 per cent.

Figure 1.

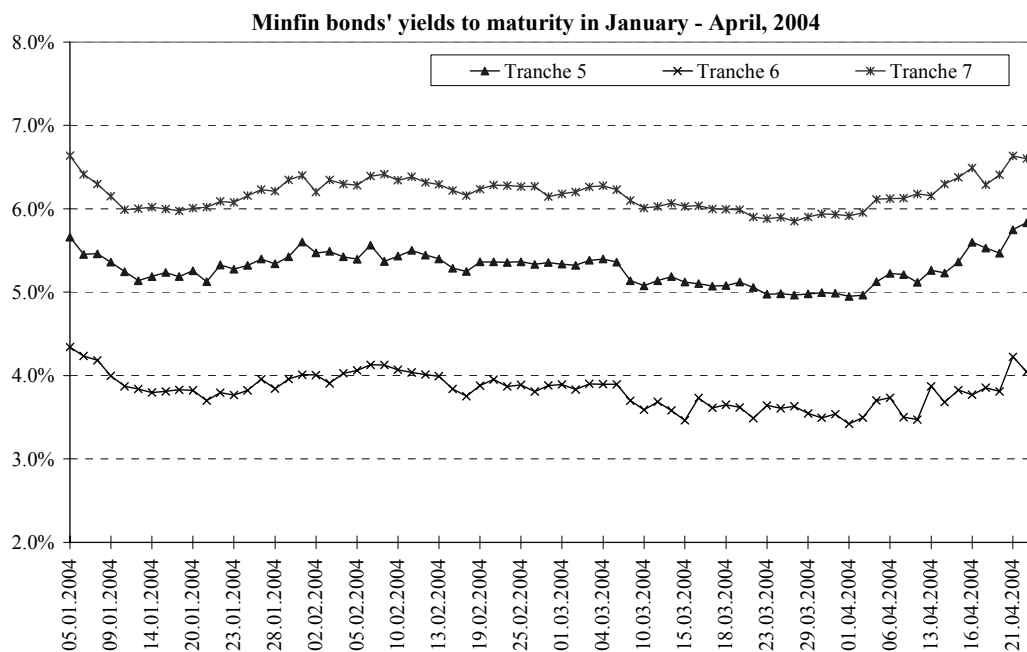
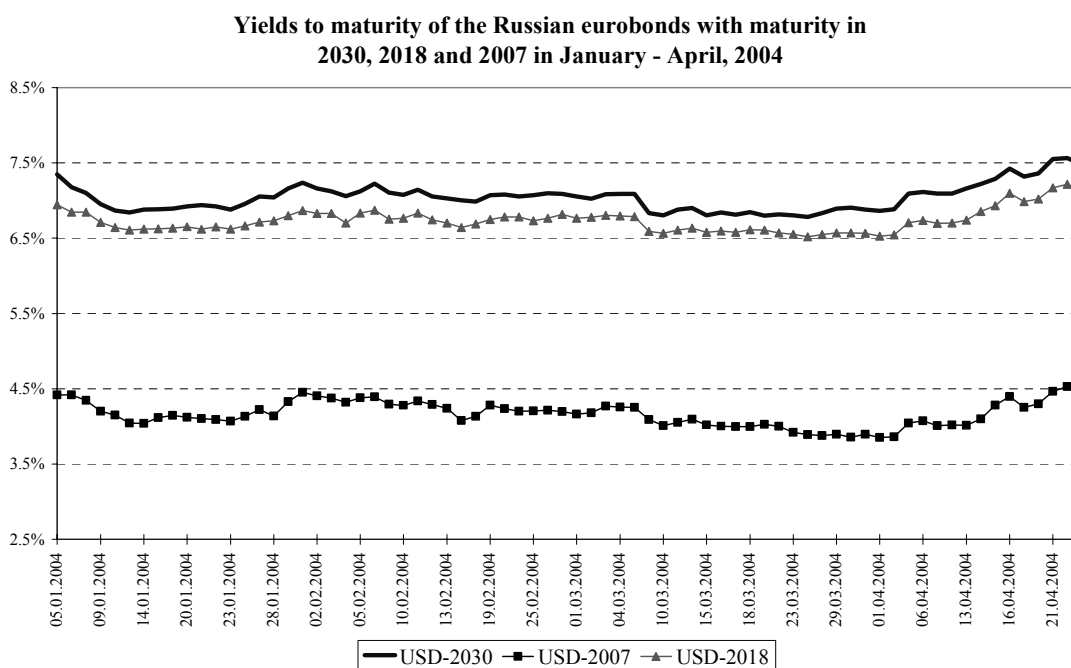


Figure 2.



Over the month, the situation on the market of Ruble denominated public debt was also characterized by the adjustment. On the whole, the dynamics of quotations were determined by the situation on the foreign and domestic forex markets, as well as a significant growth in the amount of primary placements. The deteriorating liquidity situation in the banking sector resulted in the domination of sellers on the market over the whole month.

Over the period from April 1 to 23, the aggregate turnover of the secondary GKO OFZ market made about RUR 30.6 billion, while the average daily turnover was at RUR 1.8 billion (in March, the respective indicators were registered at RUR 58.6 billion and RUR 3.45 billion). In the same period, there took place only one auction for the placement of OFZ AD 46001, the nominal value of which made RUR 5 billion. The amount of the placements made RUR 4.97 billion, while the weighed average yields of the placements were at 5.96 per cent per annum. As on April 2e, the amount of the GKO – OFZ market made RUR 460.71 billion at par and RUR 445.74 billion at the market value. The duration of the GKO-OFZ market portfolio was 1656.66 days.

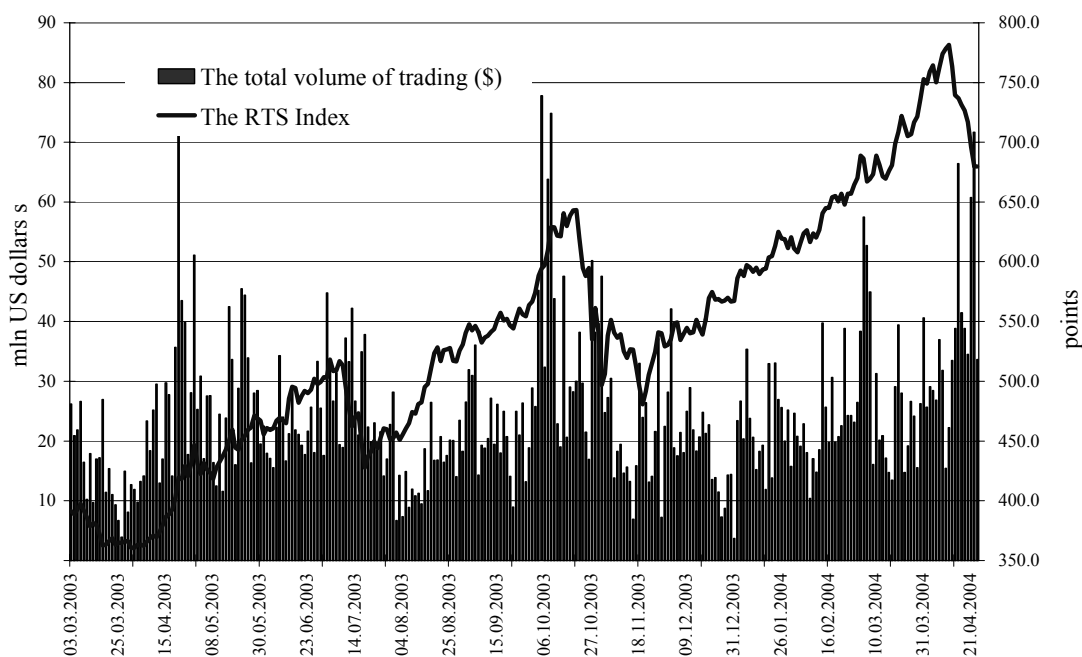
The Market for Corporate Securities

Situation on the stock market.

In April of 2004, after a long period of growth there was observed a significant decrease in market indices on the Russian stock market. However, early in the month the RTS index began to rise again reaching its historical maximum of 781.55 points on April 12. The major factors behind the positive dynamics of market quotations were as before a rather high level of liquidity in the banking sector, growing oil prices, and the generally favorable situation on the world stock markets. An additional factor supporting the market growth was the inflow of non-resident investors on the Russian market.

However, after reaching this high point the market stagnated and later significantly fell: in the period from April 12 to April 23, the RTS stock index declined by 101.96 points to the level of 679.59 points, i.e. by about 15 per cent. There may be pointed out several factors behind this sharp reverse in the market trend. First, there were new developments concerning the YUKOS affair. The fact that all assets of the YUKOS oil company were arrested by the court ruling made the ranking agency Standard & Poor's make a statement that it reduced the long term ranking of the oil company. Second, the liquidity situation in the banking sector has significantly deteriorated, while it should be noted that this factor played the key role on the market over the last few months. Third, the Russian market reacted to the statements made by the US monetary authorities that they might rise the base interest rate in the future, what affected the operations of non-resident investors. At last, an important factor behind the market downfall was the Ruble depreciation against the US Dollar.

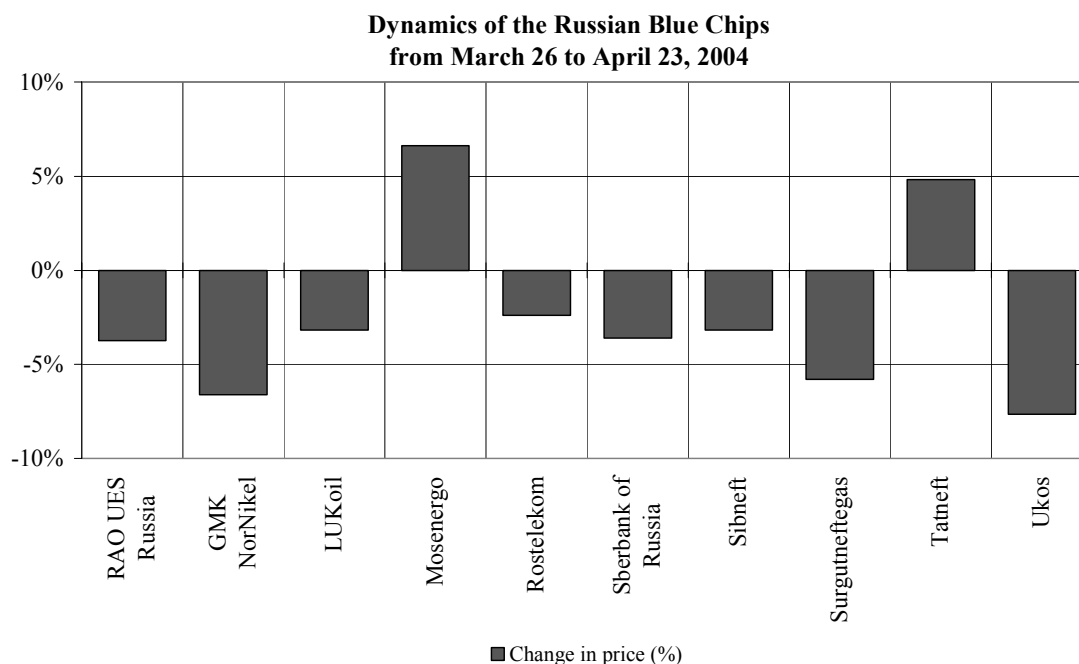
Figure 3.



On the whole, in the period from April 1 till 23, the RTS stock index declined by 69.36 points, what made about 10.21 per cent. Over the same period of time, the turnover of the RTS trading amounted to US \$ 635.96 million, while the average daily turnover at the RTS made about US \$ 37.4 million (US \$ 534.74 million and US \$ 28.14 million respectively in March). The highest volume of trade at the RTS (US \$ 71.6 million) was observed on April 22. The lowest trade volume (US \$ 15.5 million) was observed on April 9. These figures were above the respective levels registered in March (US \$ 57.5 million and US \$ 13.4 million respectively). Therefore, there was observed a growth in investors' activity on the market in April.

Over the last month (from March 26 till April 23), all "blue chips" with the exception of Tatneft (a 4.81 per cent growth) and Mosenergo (a 6.63 per cent growth) demonstrated a downfall in prices. As concerns the decline in prices, shares in the YUKOS fell by 7.64 per cent as a reaction to the court ruling arresting its assets and, later, the news about the reduction of its ranking. The YUKOS shares were followed by the stocks of the GMK Norilsk Nickel (-6.61 per cent) and Surgutneftegaz, which fell by 5.79 per cent. Further, the RAO UES stocks declined by 3.73 per cent apparently as a result of the decrease in the company's net profits and the statement of V. Khristenko, who had said that money may be acceptable for the participation in the auctions for wholesale generating companies alongside with the shares. The securities of the RF Sberbank fell by 3.59 per cent in the first three weeks of April, while LUKoil and Sibneft stocks demonstrated the same rate of decline (-3.17 per cent). The minimal downfall of prices was observed as concerns the shares in Rostelekom (-2.39 per cent).

Figure 4.



According to the authors' estimates, in the period from March 29 till April 23, the LUKoil shares took the top position in terms of the volume of turnover in the RTS⁵: the share of respective transactions amounted to about 21.85 per cent of the total turnover. The amount of transactions with the shares in the RAO UES of Russia was somewhat lower (21.37 per cent). The shares of the MMC Norilsk Nickel and YUKOS followed: the volume of transactions with these companies' shares made 12.99 percent and 10.72 per cent of the total turnover respectively. Thus, the aggregate percentage of transactions with the shares of only these four companies made about 66.93 per cent of the total traded turnover over the period of time under observation.

As on April 23, the top five leaders of the national stock market by capitalization looked as follows⁶: YUKOS: US \$ 33.22 billion; Surgutneftegaz: US \$ 24.36 billion; LUKoil: US \$ 24.18 billion; Sibneft: US \$ 14.94 billion; MMC Norilsk Nickel: US \$ 14.88 billion.

⁵ On the classical stock market.

⁶ According to the RTS.

The market for fixed term contracts. In April, the activity of investors on the RTS market for fixed term contracts (FORTS) increased in comparison with the preceding month. Thus, in the period from April 1 till 23 the volume of trade in futures and options at the RTS amounted to about RUR 23.28 billion (98.9 thousand transactions; 2.67 million contracts), what was somewhat below the respective indicators registered in the preceding month (turnover - RUR 24.5 billion, 110.6 thousand transactions; 3.02 million contracts).

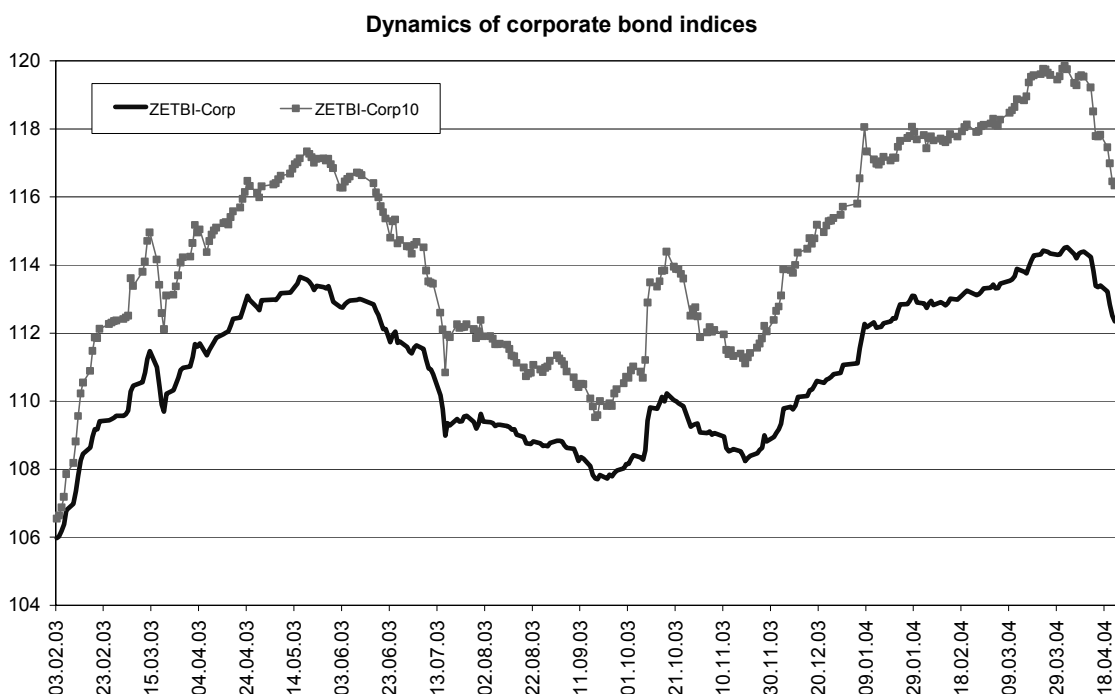
As usual, futures contracts account for the greatest percentage of transactions: the volume of trade in these contracts reached RUR 21.09 billion (2.4 million contracts, 95.56 thousand transactions) over the period under observation. As before, options were in a much lower demand: the respective amount of trading made about RUR 2.18 million, what, however, is above the figures registered in March. The maximum trading volume was observed on April 14 and made RUR 2.209 billion, while the minimum trading volume (RUR 233.55 million) was registered on April 23.

Corporate bond market. Over the month, the situation on the market of corporate bonds deteriorated. From April 1 till 23, the price index of corporate bonds traded at the MICEX⁷ decreased by 2.16 points (by 1.89 per cent) and the index of ten most liquid corporate sector bonds decreased by 3.51 points (by 2.93 per cent).

The market of corporate securities was affected by the same factors as the market of government bonds. The volatility of the world and domestic market, as well as the position taken by the Bank of Russia, which aimed to prevent an excessive real Ruble exchange rate appreciation (no more than 7 per cent over the year), had a negative impact on the quotations of corporate securities in the beginning of the month. Since mid-month, the adjustment processes had intensified at the background of increasing supply of blue chips. A factor behind the downfall of quotations was also the exceptionally high amount of primary placement and the deteriorating liquidity situation.

In the period from April 1 till 23, the total turnover in the bond sector of MICEX made about RUR 20.5 billion, while the average daily turnover was registered at RUR 1.2 million (RUR 11.3 billion and RUR 664.3 million respectively in the first three weeks of March). Therefore, in April the activity of investors was significantly above the levels observed in March.

Figure 5



⁷ The indices of corporate bonds traded at the MICEX that have been used for the calculations are calculated by Zenit Bank.

External factors affecting the dynamics of the Russian stock market. Throughout April of 2004, the prices on the world oil market remained high and did not decline below US \$ 31 per barrel. Thus, in the period from April 1 till 23 of 2004, the price of Brent oil on the world market increased by US \$ 0.95 (2.94 per cent) making US \$ 33.23 per barrel. There were several opposing factors behind the monthly dynamics of oil prices. In the beginning of the month, in spite of the OPEC decision to reduce quotas the prices somewhat declined because of the data about the growth in the US oil and gasoline reserves. However, later the expectations of the increase in the oil and oil products reserves proved to be wrong, the prices rose again. The deteriorating situation in Iraq, for instance, the attack on the export sea port in Basra also facilitated a growth in oil prices.

Figure 6.

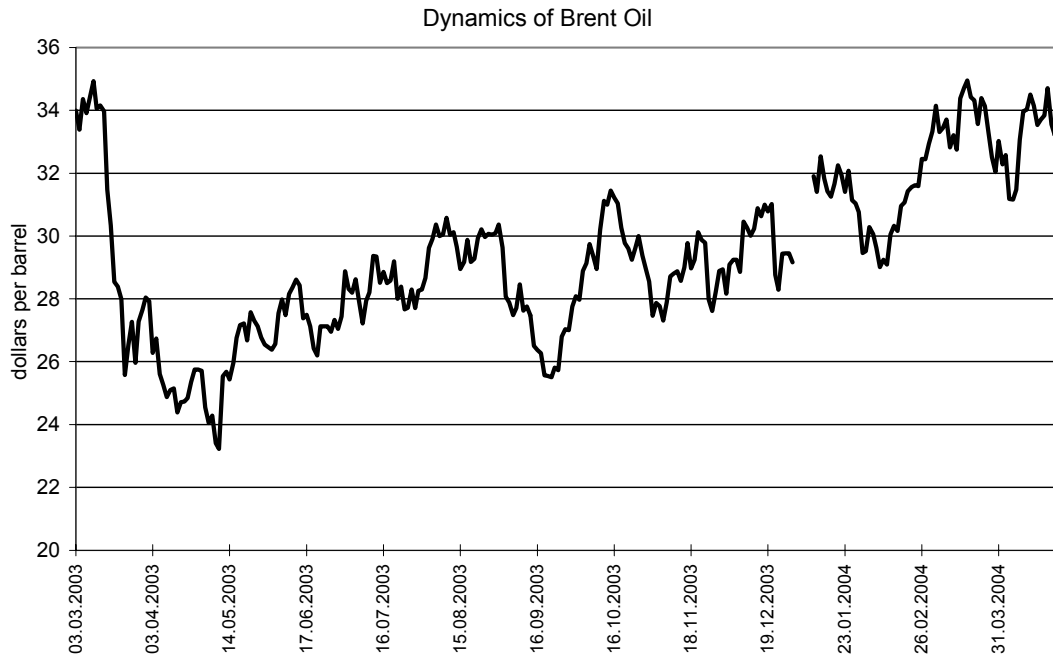
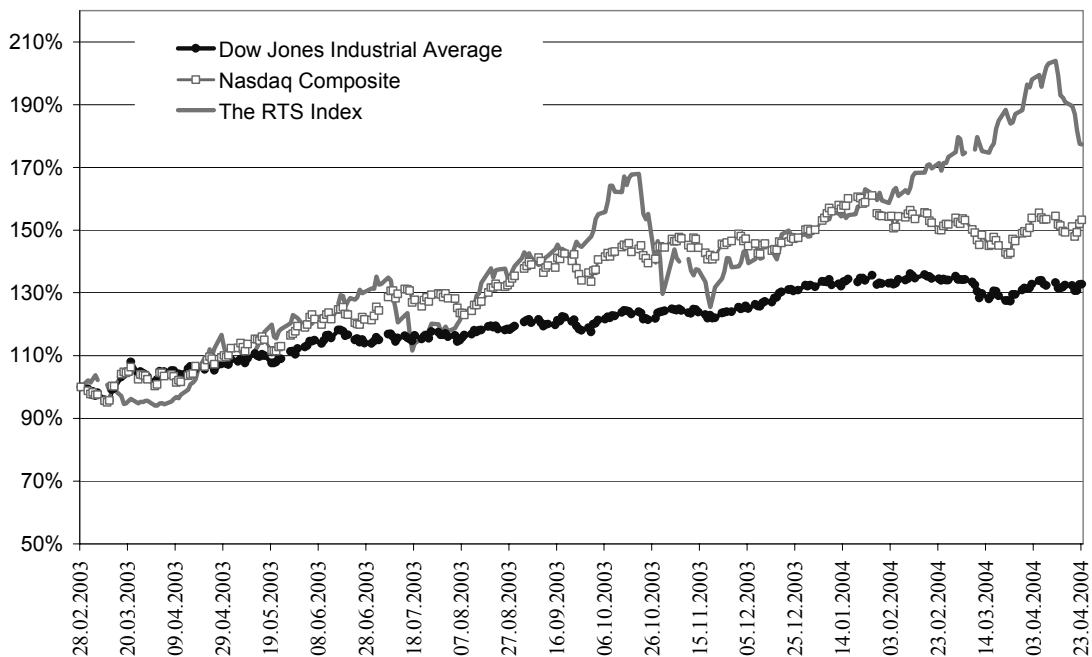


Figure 7.



In April, on the world stock markets there was observed an overall rise of the market indices (see Table 1). The US, European, and Asian stock indices were characterized by positive rates of growth by the end of the month. The only exception was stock index of Turkey, which fell by more than 6 per cent over the month. A certain improvement of the stock market situation was registered in developing countries, what was reflected by the positive dynamics of the stock index calculated by the agency MSCI.

In the first half of the month, the dynamics of the US stock market was determined by a number of factors. The positive macroeconomic statistics confirming the acceleration of the rates of economic growth in the USA and positive corporate news facilitated a rise in indices. However, the market had negatively reacted to the worsening of the geopolitical situation in Iraq. It is also important to note yet another negative factor determined by the growth in the US economy: possible rise of base interest rates, what may result in a decline of the current quotations on the stock market. Now, the US stock market will be under the influence of two opposing factors: the economic growth will facilitate a rise in prices, while the increasing inflation and possible rise in interest rates may result in a market downfall. The resulting effect will depend on the stability of the economic growth.

Summing up the impact of the different factors on the Russian stock market, it should be noted that it became more sensitive to the situation on developed stock markets and behavior of nonresidents, while continuing to be affected by the situation on the world raw material markets, which facilitates a growth of domestic securities. In particular, the fluctuations of demand for Russian depositary receipts on the markets of developed countries resulted in respective changes in prices on Russian trading floors. Besides, investors again strongly reacted to statements made by Russian public officials (for instance, as concerns the RAO USS of Russia), as well as the further development of the YUKOS affair (it should be reminded that its stocks are one of the most important factors determining the behavior of the index). At the same time, the US Dollar appreciation against the Ruble also affected the possibility of a further growth of the domestic stock market. Therefore, April witnesses the cessation of a rapid growth on the stock market and the start of adjustment.

Corporate news.

The NK LUKoil

In April, the company's management took the decision to sell its oil and natural gas assets situated in the Republic of Komi, Nenets AO, and the Perm krai. This decision was taken in the framework of the implementation of the Strategic Development Program till year 2013 aimed to reduce production costs, optimize the assets portfolio, and increase profitability of the invested capital.

On April 16, there took place a meeting of the LUKoil Board of Directors, which decided to hold an annual shareholders' meeting. The meeting was set for June 24, 2004. The Board of Directors intends to recommend the shareholders to approve the payment of dividends for 2003 at RUR 24 per one ordinary share. It was recommended to use the balance of the net profits for investment and loans to the LUKoil affiliated companies for investment purposes.

The OAO NK Sibneft

On April 15, 2004, the NK Sibneft discovered oil in the course of testing of a survey well at the Verkhne Telkaysk oil and gas condensate deposit located in the Chukotka AO. At present the proved extractable oil reserves at this deposit make 2.2 million metric tons of standard fuel. The Verkhne Telkaysk oil and gas condensate deposit has been developed since July of 2003.

The OAO Tatneft

On April 1, 2004, there was held the regular meeting of the OAO Tatneft Board of Directors, which discussed the issues related to the preparation for the annual shareholders' meeting. In particular, the Board of Directors recommended to pay dividends at 30 per cent of the par value of the company's ordinary shares (30 kopecks per share) and 100 per cent of the par value of preferred stocks (1 Ruble per share).

The OAO GMK Norilsk Nickel

The OAO GMK Norilsk Nickel has finalized the purchase of 20 per cent of shares in the gold mining company Gold Fields Ltd. The total amount of purchase has made about Rand 7.6 billion (US \$ 1.16 billion).

The RAO UES of Russia

On April 15, the company published its annual financial statement for 2003 in accordance with the Russian Accounting Standards (RAS). Over 12 months of 2003, the company's operating revenue decreased to RUR 51.6 billion as compared with RUR 52.5 billion earned in the respective period of the preceding year.

The sales profits declined by RUR 1.5 billion and made RUR 30.8 billion. In 2003, the net profit of the RAO UES of Russia made RUR 24.6 billion as compared with RUR 31.0 billion in 2002. The decline in the amount of net profits results from the fact that the RAO UES of Russia used its right (under Russian law) not to reflect the results of consequent evaluation and depreciation of investment in affiliated companies in its financial reports.

On April 23, 2004, there took place a meeting of the RAO UES of Russia Board of Directors. The Board set the date, on which the formation of the lists of persons entitled by the Russian legislation to take part in the annual shareholders' meeting of the RAO UES of Russia (April 12 of 2004). Besides the Board of Directors approved the configuration of the territorial generating companies (TGC) elaborated by the managers of the RAO UES of Russia and approved in the course of a series of meetings held by different Ministries and departments, which were attended also by minority shareholders and potential investors. According to the decision taken by the Board of Directors, there will be created 14 territorial generating companies on the basis of existing capacities. There was also approved the configuration of interregional distribution network companies and discussed the principles governing the management of these companies.

The OAO Rostelecom

On May 13, the company presented its financial statement for year 2003 made in accordance with the Russian Accounting Standards (RAS). The company's earnings increased by 17.8 per cent and made RUR 29.9 billion, sales profits increased by 17 per cent in comparison with the figures registered in 2002 and made RUR 9029 million. At the same time, the net profits increased by 155.2 per cent and made RUR 7899 million.

The OAO Sberbank Rossii

In April of 2004, the OAO Sberbank Rossii presented its financial statement for year 2003. The before tax profit of the company made RUR 38.8 billion, while the net profits were registered at RUR 33.7 billion. In 2003, the Sberbank's net assets reached RUR 1.5 trillion, while the bank's capital increased to RUR 184.4 billion.

Table 1.

Dynamics of International Stock Market Indices

| Data as of April 23, 2004 | Value | Change within the month (%)⁸ | Change since the beginning of the year (%) |
|--|--------------|--|---|
| RTS (Russia) | 679.59 | -5.16% | 15.96% |
| Dow Jones Industrial Average (USA) | 10472.84 | 2.54% | 0.61% |
| Nasdaq Composite (USA) | 2049.77 | 4.58% | 2.15% |
| S&P 500 (USA) | 1140.6 | 2.94% | 2.90% |
| FTSE 100 (UK) | 4570.0 | 4.88% | 1.33% |
| DAX-30 (Germany) | 4103.62 | 7.36% | 2.12% |
| CAC-40 (France) | 3811.43 | 6.10% | 5.97% |
| Swiss Market (Switzerland) | 5818.10 | 4.14% | 4.22% |
| Nikkei-225 (Japan) | 12120.66 | 2.97% | 11.97% |
| Bovespa (Brazil) | 21590.0 | 0.23% | -3.81% |
| IPC (Mexico) | 10721.62 | 2.78% | 32.07% |
| IPSA (Chile) | 1460.88 | 1.88% | -1.60% |
| Straits Times (Singapore) | 1867.64 | 2.22% | 4.26% |
| Seoul Composite (South Korea) | 936.06 | 8.35% | 19.98% |
| ISE National-100 (Turkey) | 19431.5 | -6.74% | 1.48% |
| Morgan Stanley Emerging Markets Free Index | 478.225 | 2.49% | 7.92% |

The Foreign Exchange Market. In the period from April 1 till 24, the US \$ / RUR exchange rate increased by about 45 kopecks to the level of RUR 28.97 per US \$, what made circa 1.59 per cent. On the whole, the exchange rate dynamics were determined by the impact of two oppositely directed trends: on the one hand, the growth in the world oil prices supported the supply of the US Dollars on the domestic market. On the other hand, the US Dollar appreciation on the world market was facilitated its strengthening against the Ruble. Besides, the statements made by the Central Bank representatives concerning the tightening of

⁸ As compared to the level registered on March 26.

control over the real Ruble appreciation and transition to the currency basket resulted in an increase in demand for foreign exchange on the part of banks. Therefore, starting since the second half of the month, the trends towards US Dollar appreciation outweighed the opposite factors, what resulted in a weaker Ruble and a stronger US Dollar.

Figure 8.

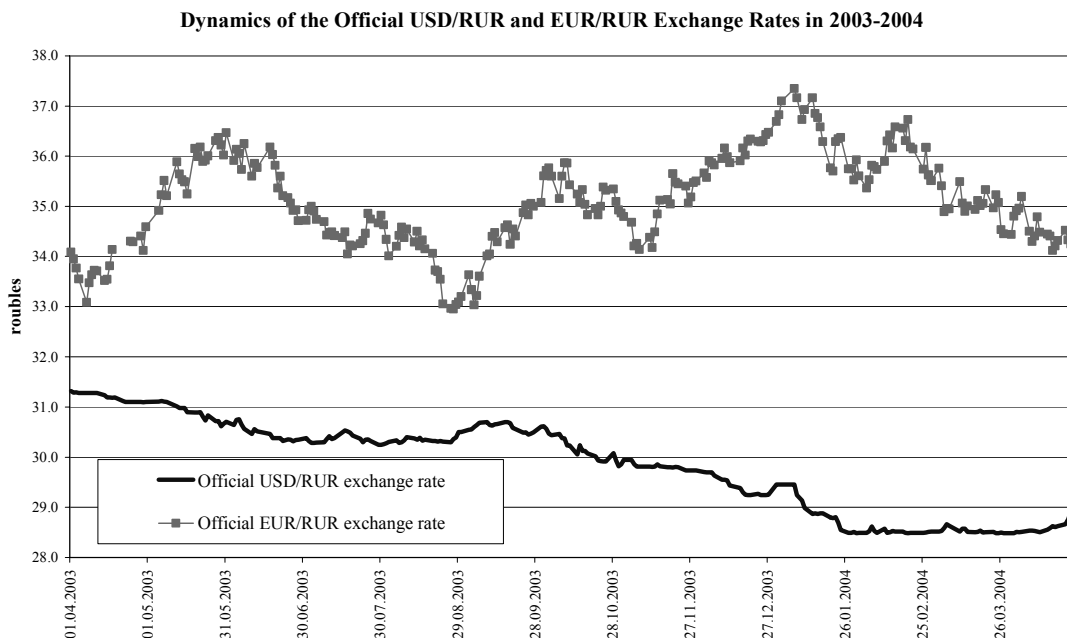
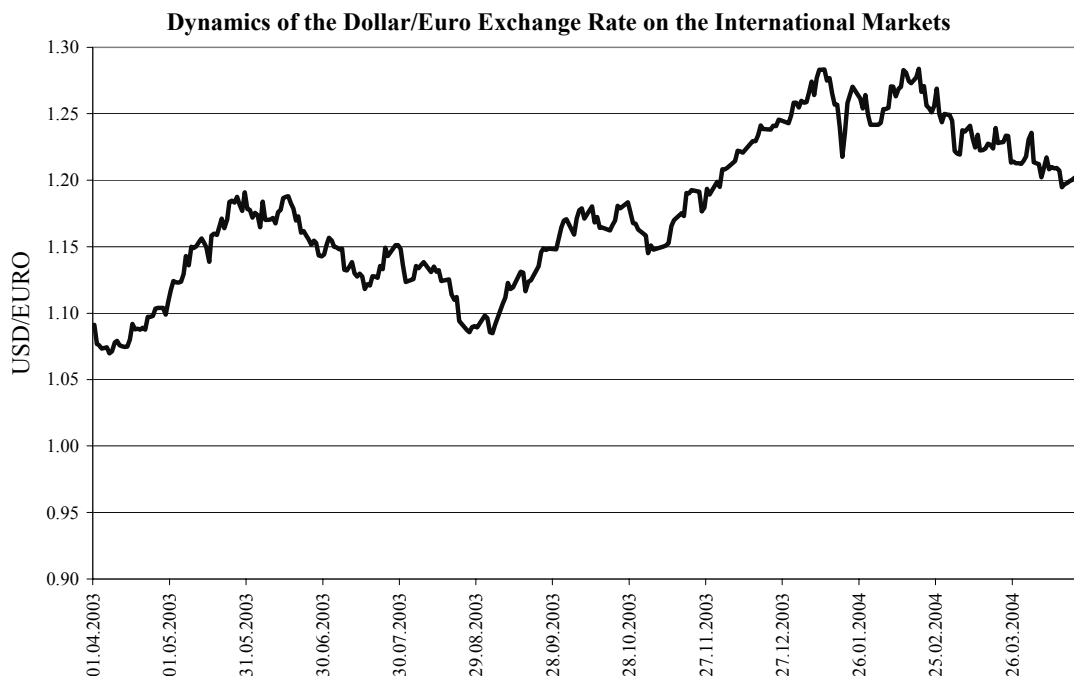


Figure 9.



The aggregate volume of trade in the US Dollar at the SELT in the period from April 1 till April 23 made US \$ 9.9 billion (US \$ 12.07 in March). The average daily turnover made US \$ 582.8 million over this period, what was somewhat below the respective indicator registered in March of 2004 (US \$ 710.2 million). During the period under review, the highest volume of trade in the US Dollar, about US \$ 1.1 billion, was

observed on April 20 (about US \$ 1.9 billion in March of 2004); the lowest volume, US \$ 153.3 million, was observed on April 5.

This April, the Ruble liquidity in the banking sector significantly decreased in comparison with the figures registered in the preceding month: in April, the average balances of correspondent accounts of credit organizations with the Bank of Russia made RUR 184.3 billion, what was by about RUR 4.9 billion below the respective indicator registered in March of 2004 (RUR 189.2 billion).

In the period from March 31 till April 23, on the world forex markets there was observed a prevailing trend towards appreciation of US \$ against Euro. Thus, during this period of time the Euro exchange rate decreased by US \$ 0.034 making US \$ 1.184 per Euro. The major factor behind the continuing appreciation of the US Dollar on the world markets was the publication of favorable macroeconomic statistics in the USA notwithstanding the negative foreign trade indicators.

The dynamics of the Euro - Ruble rate were mainly determined by the trends on the world market. Following the appreciation of the US Dollar against Euro on the world forex markets, the exchange rate of the European currency against the Ruble also declined. In the period from April 1 till April 23, the European currency depreciated by RUR 0.38 (-1.1 per cent) from RUR 34.91 per Euro and made RUR 34.52 per Euro. The aggregate turnover of trade at the SELT amounted to Euro 115.6 million in the period from April 1 till April 23 (Euro 163.2 million in the first three weeks of March). In this period, the highest trade volume of Euro was registered on April 13 at Euro 14.9 million, and the lowest, Euro 3.02 million, on April 12.

Table 2.

Financial Markets Indicators

| Month | December | January | February | March | April* |
|---|----------|---------|----------|---------|--------|
| Monthly inflation rate | 1,1% | 1,8% | 1,0% | 0,8% | 0,9% |
| Inflation rate annualized on the basis of this month's trend | 14,03% | 23,87% | 12,68% | 10,03% | 11,5% |
| CB RF refinancing rate | 16% | 14% | 14% | 14% | 14% |
| Annualized yield to maturity on OFZ issues (%) | 7,63% | 6,48% | 6,15% | 6,78% | 7,0% |
| Volume of trading in the secondary GKO-OFZ market for the month (RUR billion) | 20,58 | 31,77 | 25,47 | 50,55 | 25,0 |
| Yield to maturity on Minfin bonds at the end of the month (% p.a.) | | | | | |
| 5th tranche | 5,62% | 5,60% | 5,36% | 4,99% | 5,8% |
| 6th tranche | 4,18% | 4,01% | 3,88% | 3,54% | 4,2% |
| 7th tranche | 6,51% | 6,40% | 6,15% | 5,93% | 6,6% |
| 8th tranche | 5,16% | 4,77% | 4,56% | 4,22% | 4,6% |
| Yield to maturity of Eurobonds at the end of the month (% p.a.) | | | | | |
| 2005 | 3,05% | 2,83% | 2,77% | 2,40% | 2,8% |
| 2007 | 4,42% | 4,45% | 4,20% | 3,90% | 4,5% |
| 2010 | 5,80% | 5,79% | 5,68% | 5,51% | 6,0% |
| 2018 | 6,97% | 6,86% | 6,82% | 6,56% | 7,2% |
| 2028 | 7,34% | 7,33% | 7,25% | 7,07% | 7,7% |
| 2030 | 7,28% | 7,24% | 7,08% | 6,88% | 7,6% |
| INSTAR-MIACR rate (% p.a.) on interbank overnight loans at the end of the month | 7,75% | 2,15% | 1,76% | 6,19% | 10% |
| Official RUR / US\$ exchange rate at the end of the month | 29,4545 | 28,4916 | 28,5156 | 28,4853 | 29,0 |
| Official RUR / Euro exchange rate at the end of the month | 36,8240 | 35,3635 | 35,5076 | 34,8005 | 34,3 |
| Average annualized growth in RUR / US\$ exchange rate | -0,96% | -3,27% | 0,08% | -0,11% | 1,8% |
| Average annualized growth in RUR / Euro exchange rate | 3,72% | -3,97% | 0,41% | -1,99% | -1,5% |
| Volume of trading at the stock market in the RTS for the month (US\$ million) | 416,89 | 432,75 | 433,12 | 613,91 | 800 |
| Value of RTS-I Index at the end of the month | 567,40 | 611,10 | 670,14 | 752,66 | 650 |
| Change in value of RTS-I Index during the month (%) | 4,33% | 7,70% | 9,66% | 12,31% | -13,5% |

* Estimate

D. Polevoy

The Real Sector: Factors and Trends

According to the preliminary data, in the 1st quarter of 2004, the gross domestic product made Rub. 3500 billion and increased by 8.0 per cent in comparison with the figures registered in the respective period of the preceding year. The accumulated potential of development has determined the adaptation to the changing external economic situation, Ruble exchange rate dynamics, growing costs of wages and salaries and payments for products and services provided by natural monopolies. Economic growth was supported by the persisting positive dynamics of production across practically all sectors of the economy. In April of 2004, output of products and services of the base sectors of the economy increased by 7.2 per cent as compared with the figures registered in January through March of 2003. The changes in the structure of production occurring in the 1st quarter of 2004 were primarily determined by the expanding demand for works and services rendered by construction by 13.8 per cent, and a 10.3 per cent growth in the retail trade turnover. The rates of growth in industrial output accelerated by 1.6 p. p. in comparison with the figures registered in the 1st quarter of 2003 and made 107.6 per cent.

A specific feature of 2003 through the 1st quarter of 2004 was reflected via changes in GDP utilization, which is forming at the background of the outpacing growth of the investment component. In the 1st quarter of 2004, the share of investment in fixed assets as the share of GDP made 11.8 per cent increasing by 2.5 p. p. in comparison with the figures observed in the respective period of the preceding year. Intensification of investment activity based on both a rapid growth in the output of mechanical engineering (by 17.5 per cent as compared with the level registered in the 1st quarter of 2003) and construction materials industry (11.8 per cent), and the expansion of the scale of import of machinery and equipment. The specific feature of the development of mechanical engineering was accelerating rates of growth in output of machinery and equipment not only for extracting industries, but for the industries of the consumer complex and the sphere of services as well. An intensive development of mechanical engineering sectors supplying light, food, and household appliance industries (a 125 per cent growth in comparison with the figures registered in the 1st quarter of 2003), communication equipment industry (143.3 per cent), and instrument making industry (130.0 per cent) was supported by the accelerating processes of modernization of fixed assets in respective industries, formation of new niches for domestic producers on the internal market, and changes in the competitive environment.

The consolidation of positions of Russian producers on the market of capital goods occurs at the background of a moderate growth in prices. In December of 2003 through March of 2004, the producer price index in mechanical engineering made 105.9 per cent as compared with 109.5 per cent registered in the industry on the whole. However, under the existing structure of and ratio between demand and supply import of machinery and equipment is growing at an outpacing rate in comparison with domestic production. In the first months of the year, the share of machinery, equipment, and vehicles in the total amount of imports increased by 3.1 p. p.

An analysis of the development of this trend should be focused on the price determination policy adopted by the motor industry. The analysis of long term trends of development of the motor industry demonstrates that the policy of increase in prices of cars as a rule results in a crisis of overproduction. The support rendered to the domestic motor industry over the last two years at the expense of systematic increase in customs duties did not bring the expected results either in terms of improvement of quality, or growth in the volumes of output.

As the situation developed according to this scenario, it again resulted in stagnation of production this April. In the beginning of this year, the prices of cars again rose by 5 to 6 per cent, what, even at the background of persisting high duties on cars of foreign manufacture imported in Russia resulted in the narrowing of the price gap between the domestic and foreign cars. The existing level of price proportions provokes the trend towards an increase of the delayed household demand at the expense of the consumer preferences shifting to the sector of foreign cars of better quality. In this connection, it appears that the Governmental proposal to reduce customs duties on imported foreign cars and completing parts used for domestic assembly of foreign cars in Russia was made in the right time. The implementation of this policy will permit to reduce the possibility of domestic car manufactures to uncontrollably rise prices of their products and change market conditions.

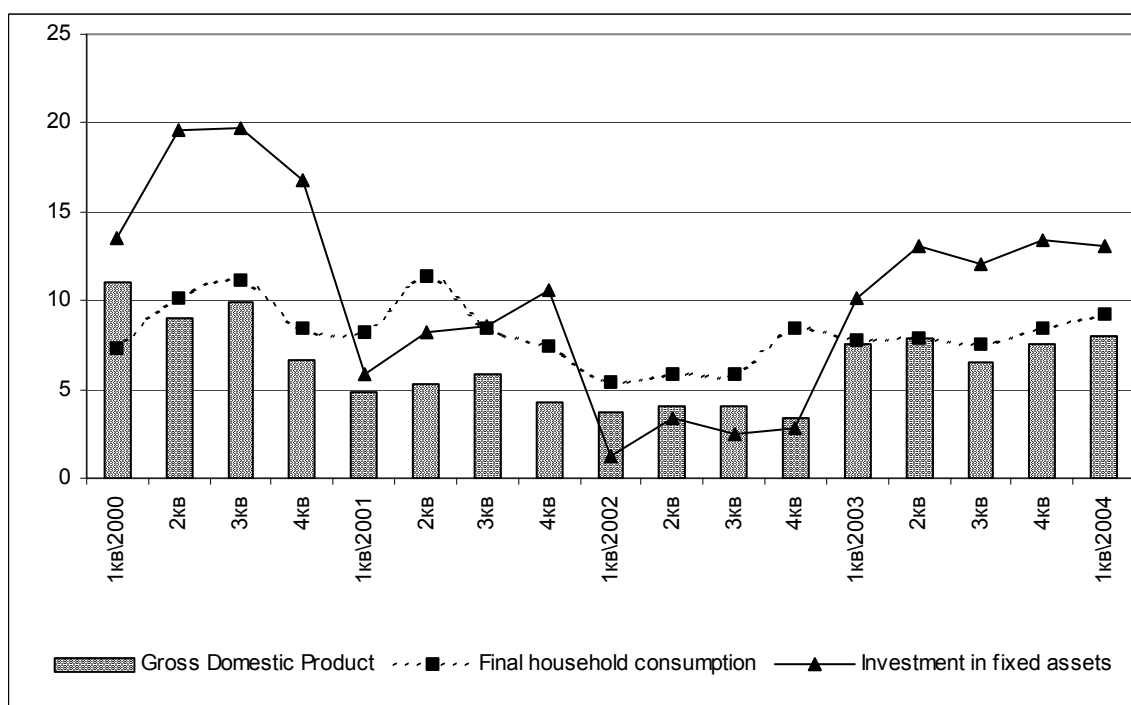


Figure 1. Changes in GDP dynamics as broken down by final use components in 2000 through 2004, in % of the respective period of the preceding year

The persisting intensive dynamics of expansion of household consumption was initiated by increasing household incomes. The major factor determining the growth in real incomes and consumption was the accelerating rates of rise in real wages and salaries. While in the 1st quarter of 2004 the real disposable household incomes grew by 13.9 per cent in comparison with the figures registered in the respective period of the preceding year, real wages and salaries increased by 15.8 per cent, what is by 6.1 p. p. exceeded the levels observed in the respective period of the past year.

The growth in household incomes occurring at the background of the widening gap between the dynamics of real wages and salaries and the productivity of labor results in the redistribution of added value from enterprises to households. In the economy, there is observed a growth in production costs and, respectively, diminishing profitability of the real sector. The reaction of supply to the changes in the Ruble exchange rate was a slowdown of the rate of increase in domestic production of consumer goods in comparison with the dynamics of final demand and accelerated growth in imports. The problem is aggravated by the persistence of high degree of differentiation of wages and salaries across the sectors of the economy, in particular, between the extracting and manufacturing industries. As a result, there is observed a decline in the factor remuneration of labor in manufacturing industries and the sector of services. Taking into account the fact that manufacturing industries and the sector of services employ almost 90 per cent of the total active labor resources in the country, while wages and salaries of the respective employees form over 75 per cent of the total household incomes. The low effective demand on the part of these categories households is a major factor determining the intensity of economic growth. In comparison with the figures registered in 2003, the share of domestically produced consumer goods in the retail trade resources has declined by 1 p. p. In the 1st quarter of 2004, the growth in output of consumer goods made 107.0 per cent, while the output of food industry increased by 7.2 per cent and the production of light industry continued to decline. This fact confirms the conclusion about the diminishing positive impact of consumer demand on the dynamics of output.

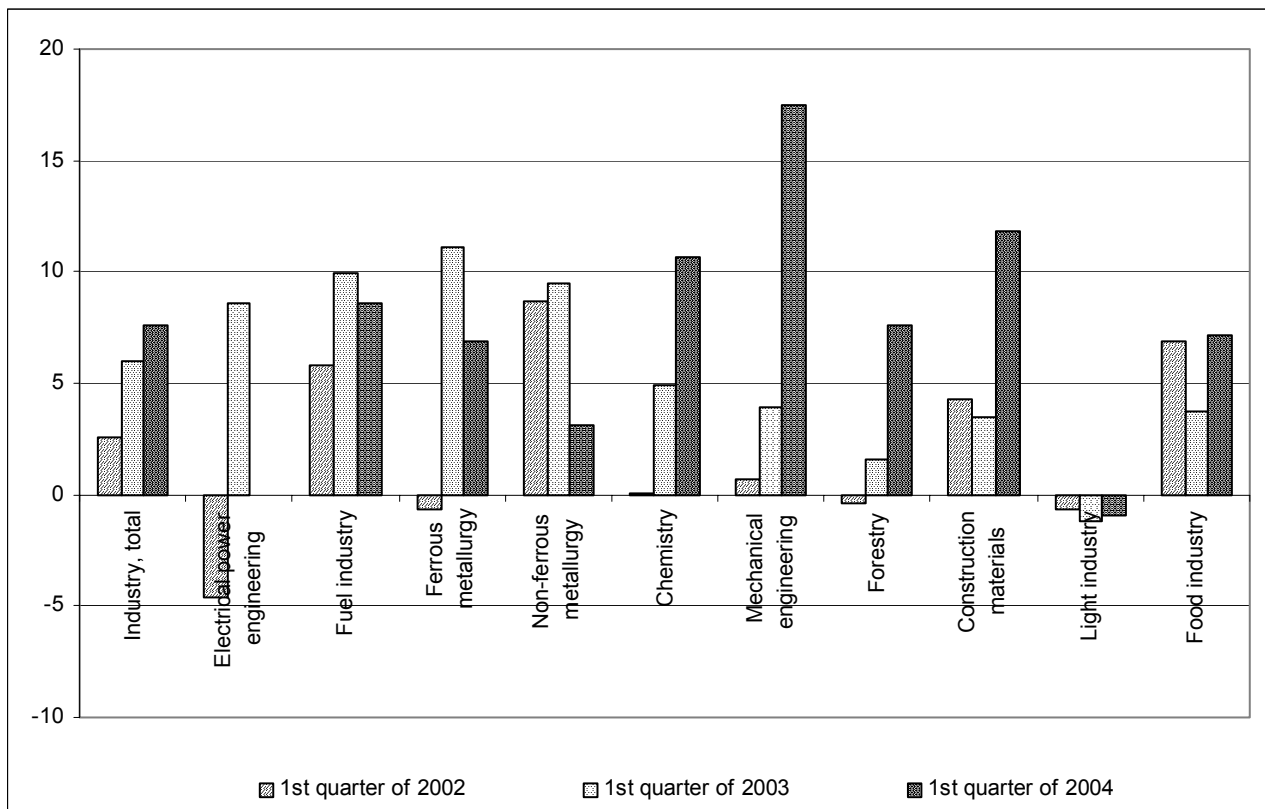


Figure 2 Changes in the dynamics of output across industries in the 1st quarter of 2001 through 2004, in % of the respective period of the preceding year

In early 2004, the structural shifts in industry were determined by the outpacing rates of growth in output of investment branches and persisting rather stable dynamics of development of export oriented industries in the exceptionally favorable situation on the world markets of hydrocarbons, mineral, and raw material resources. In the 1st quarter of 2004, there dynamically developed fuel industry (108.6 per cent), including oil processing industry (110.7 per cent), ferrous metallurgy (106.9 per cent), chemistry and petrochemistry (110.7 per cent). A stable increase in output was determined by both expansion of the export capacity of these industries, and the growing demand on the domestic market. As concerns oil industry, almost half of the total volume of extracted oil and about 35 per cent of the produced diesel fuel and furnace oil were exported. In nonferrous metallurgy, there persists the trend towards outpacing growth in imports as compared with the dynamics of domestic consumption. As concerns ferrous metallurgy, the increase in output of ferroalloys by 22.2 per cent was accompanied by an outpacing rate of increase in imports, while the 14.7 per cent growth in production of pipes was initiated by demand on the part of the oil and natural gas sector.

There is no doubt that the stable development of Russia's metallurgy observed in 2003 though early 2004 was favorably affected by the growing demand for metal products and ferrous ore raw materials on the world market. The weighed average world prices on the markets of ferrous metals increased by one third in the 1st quarter of 2004. As concerns the market of nonferrous metals, in the beginning of the year it was characterized by a rather favorable business situation: aluminum prices went up by 18 per cent, nickel prices grew by 77 per cent, and the price of copper increased by 64 per cent as compared with the figures registered in the 1st quarter of 2003. The impact of external factors on the dynamics of the metallurgical complex was also related to the cyclic nature of demand on the world market. In this situation, fluctuations in the external demand are compensated by changes in domestic demand and price levels. Exactly the expansion of the domestic market of metal products resulting from the high investment activity permitted to overcome the shrinking of output in ferrous metallurgy registered in the 4th quarter of 2003 and achieve the trajectory of growth.

At the same time, it should be noted that in the 1st quarter of 2004, on the domestic market there were observed accelerating rates of growth in prices of metal products. The producer price index registered this March in ferrous metallurgy and nonferrous metallurgy made 116.0 per cent and 106.9 per cent respectively in comparison with the figures observed in December of 2003. This developments were caused by the rise in

prices of ore materials, products of coke chemistry, and energy resources. Outpacing rates of growth in prices of metal products as compared with the price dynamics of major consumers of construction materials were observed at the background of gradually decelerating rates of growth in ferrous metallurgy. In a short time outlook, these developments may cause a price adjustment in mechanical engineering, construction complex, oil extraction, as well as tariffs on transport services.

A comparative analysis of dynamics and factors of economic growth revealed that the characteristic feature of the present situation is the stronger impact of the factors of domestic demand. In January through March of 2004, the increase in the output of industries primarily oriented towards the domestic market made about 9.0 per cent as compared with a 2.5 per cent growth registered in the respective period of the preceding year.

In the 1st quarter of 2004, the growth in production of chemistry and petrochemistry in Russia made 110.7 per cent as compared with 104.9 per cent observed in the respective period of the preceding year. The acceleration of the rates of increase in output occurred across all industries. Production of synthetic resins grew by 11.6 per cent, plastic products – by 14.8 per cent, core chemistry products – by 10.6 per cent, including a 13.7 per cent growth in the output of mineral fertilizers. While the dynamic expansion of the mineral fertilizers exports had rather significantly affected the dynamics of production of core chemistry products, the outpacing rates of increase in output of construction plastics and plastic products was determined by increasing demand on the part of the industries of the investment complex.

An intensive growth in production in the forestry complex was also supported by the outpacing rates of increase in domestic demand at the background of moderate dynamics of foreign trade with wood and paper products. In the 1st quarter of 2004, there were observed accelerating rates of growth in the forestry complex. As concerns lumber and wood working industries, there was registered recovery of the volumes of production after the slump of the end of 2003. In the 1st quarter of 2004, the output of pulp and paper industry increased by 12.5 per cent in comparison with the figures observed in the 1st quarter of 2003, at the same time, the rates of growth accelerated across practically all respective core industries.

On the whole, in the 1st quarter of 2004 domestic and external demand had practically equal impact on the growth in industrial output. Accordingly, the influence of the manufacturing industries determined by the outpacing rates of growth in the industries of the investment complex on the overall dynamics has somewhat increased in comparison with the preceding year..

O. I. Izryadnova

IET Business Survey: Industry in April of 2004

According to the Federal Statistics Service, in the 1st quarter of 2004 the growth in industrial output made 7.6 per cent as compared with the figures registered in the 1st quarter of the preceding year. In the 1st quarter of 2004, the most significant growth was observed in the glass, porcelain, and faience industry (21.5 per cent), mechanical engineering and metal working (17.5 per cent), construction materials industry (11.8 per cent), chemistry and petrochemistry (10.7 per cent), medical industry (8.9 per cent), fuel industry (8.6 per cent), and in forestry, woodworking, pulp and paper industry (7.6 per cent). In March of 2004, output grew by 9.2 per cent as compared with the figures registered in February.

First reports on the dynamics of sales, output, and finished stocks received in April rather demonstrate that the positive trends in the development of the Russian industry persist. However, it should be noted that surveys have registered certain negative phenomena.

The rates of growth in sales (evaluated in the terms of balance) decreased in April by 3 points (as adjusted for the seasonal factors). At present, the balance of changes in this indicator makes + 7 per cent, while in the preceding year its value was registered at + 2 per cent. The growth in effective demand continues. In April, a certain decline in the rates of growth of this indicator was observed only in electrical power engineering and light industry, the most intensive decrease was registered in chemistry, petrochemistry, and construction materials industry.

In spite of a certain deceleration of the rates of growth in sales, the balance of respective assessments (above norm – below norm) has not deteriorated, while the share of evaluations of demand as “normal” even increased to 54 per cent. The absolute maximum of the latter indicator registered in the second six months of 2003 makes 55 per cent. Therefore, enterprises are not concerned about a slight decline in the rates of growth in sales as yet. In April, the maximal number of reports evaluating demand as “normal” were received in metallurgy (74 per cent), light (66 per cent) and food (61 per cent) industries, chemistry and petrochemistry

(60 per cent). For the first time since 1994, the value of this indicator in mechanical engineering has been registered at 50 per cent.

The dynamics of output also did not demonstrate negative trends in April. The last reported data (as adjusted for seasonal factors) showed an increase in the monthly rates of growth in output by additional 4 points. Fuel industry, metallurgy, mechanical engineering, and chemistry and petrochemistry accounted for these developments. The major constraints on the growth in industrial output remain insufficient domestic demand and shortage of working capital. In 2004, enterprises report about other obstacles at least two times less frequently (see the Table below).

Table 1

**Factors hindering Russian enterprises to increase their output
(in % of the total number of reports, annualized data)**

| | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|---------------------------------------|------|------|------|------|------|------|------|------|------|------|
| Nothing | 1 | 1 | 1 | 0 | 1 | 2 | 2 | 2 | 2 | 5 |
| Domestic effective demand | 56 | 64 | 61 | 63 | 51 | 45 | 47 | 62 | 58 | 50 |
| Low export demand | 8 | 12 | 17 | 16 | 17 | 16 | 21 | 23 | 26 | 24 |
| Competing imports | 8 | 14 | 13 | 12 | 5 | 6 | 11 | 13 | 19 | 20 |
| Non-payments on the part of customers | 72 | 69 | 66 | 61 | 39 | 31 | 27 | 32 | 26 | 18 |
| Shortage of working capital | 79 | 69 | 67 | 69 | 68 | 61 | 55 | 55 | 49 | 42 |
| Shortage of skilled labor | 14 | 8 | 8 | 7 | 12 | 20 | 23 | 20 | 23 | 22 |
| Shortage of equipment | 6 | 4 | 7 | 6 | 10 | 19 | 18 | 14 | 18 | 19 |
| Shortage of raw materials | 24 | 22 | 27 | 28 | 34 | 28 | 22 | 18 | 15 | 15 |
| Shortage of power | 4 | 5 | 7 | 7 | 7 | 8 | 8 | 6 | 6 | 2 |
| Other | 13 | 9 | 9 | 7 | 6 | 7 | 9 | 7 | 8 | 8 |

Note. 2004 r. – 1st and 2nd quarters

As concerns the dynamics of factors hindering the growth in output monitored by surveys, the obstacles to the growth in production may be classified in two groups. The importance of the first group of factors (domestic demand, non-payments, shortage of working capital, lack of raw materials) declines. On the contrary, as the period of recovery growth is nearing its completion, enterprises more often mention the second group of factors (lack of labor, equipment, insufficient export demand, competing imports). The most significant changes in comparison with the situation observed in 1999 (the first year after the default of 1998) occurred in the influence of competing imports. The use of such definition does not account for the impact of non-competing imports registered however by official statistics and permits to assess the influence of this factor on the development of domestic industry more correctly. According to enterprises' assessments, the constraining impact of imports in general has increased four times (from 5 per cent to 20 per cent). However, as it has turned out, the Russian industry was able to increase output even in the situation of more significant pressure of imports and the Ruble appreciation. The dynamics of output observed in 2003 through 2004 convincingly proves this fact. There have remained a considerable number of factors constraining the growth of output of manufacturing industries more significantly than the increasing imports and the Ruble exchange rates, which have been more and more often mentioned since recently. Even in the light industry, which has always been thought to most suffer because of imports, this factor was ranked only the fourth in 2004.

Since early 1999, the provision of enterprises with raw materials has improved two times. In 2004, 60 per cent of enterprises evaluated their stocks of raw materials as "normal," while in 1995 though 1998 this indicator was at or below 26 per cent. The majority of other enterprises assessed their stocks to be below the norm. However, the balance of evaluations (above norm – below the norm) increased from –69 per cent registered in 1995 to –24 per cent in 2004. The constraining impact of the shortage of raw materials on the output declined almost two times (see the Table above).

The balance of changes in the forecasts of demand (growth minus decline) has lost a few points of optimism before the national May holidays, mainly due to the fact that the share of expectation that demand would grow declined, while the share of "no changes" answers increased respectively. However, the forecasts of growth in sales still prevail over the reports stating their decline (the balance value was positive) both in the industry at large and across the majority of individual industries.

The forecasts of changes in output also became less optimistic since a number of enterprises decided not to increase output, but keep their present volumes of production. An absolute decline in output is expected only in metallurgy.

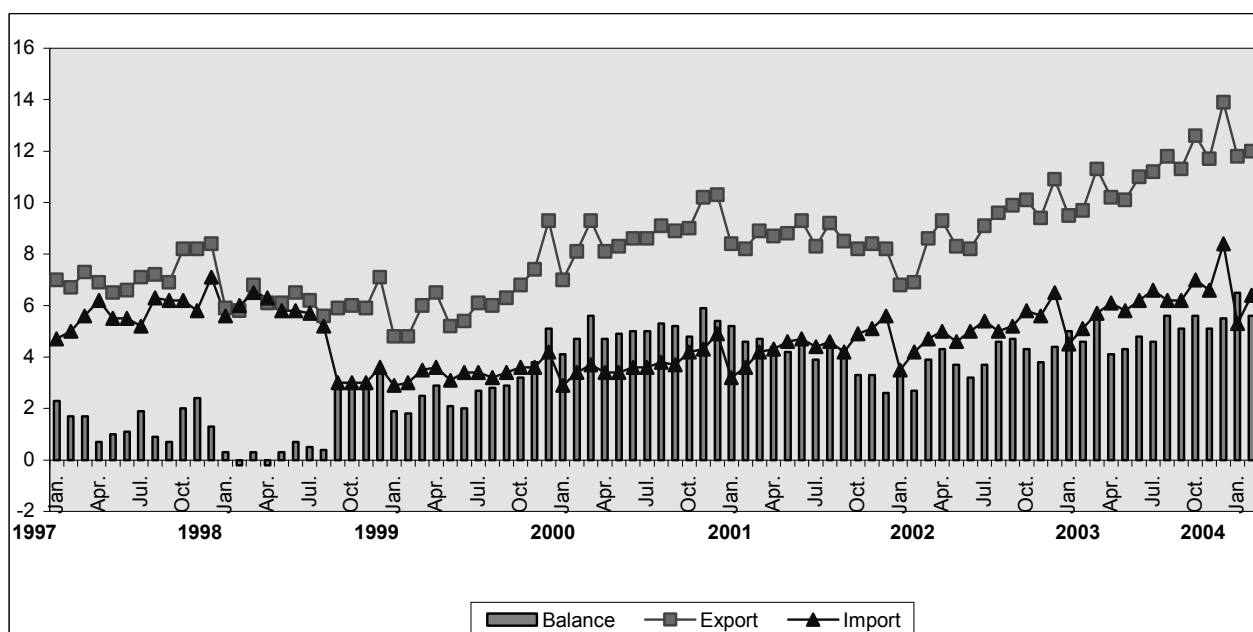
After the improvement registered in January, the assessments of changes in employment have declined again and became moderately pessimistic as it was observed over 2003. The majority of enterprises do not plan to change the strength of their personnel, while most of the others prefer to decrease the number of their employees. Since in April there was registered redundant employment (above the expected figures), these plans seem to be quite reasonable. A growth in employment is possible only in chemistry, petrochemistry, and mechanical engineering.

S. V. Tsukhlo

Foreign Trade

In February of 2004, the Russia's foreign trade turnover (according to the balance of trade methodology) reached US \$ 18.4 billion, what is by 21.9 per cent above the figures registered in February of 2003. In February of 2003, Russian exports made US \$ 12 billion (a 21.3 per cent growth), while imports were registered at US \$ 6.4 billion (a 23.1 per cent growth). In comparison with the figures observed in January of 2004, the Russian foreign trade turnover increased by 7.5 per cent as export of goods grew by 1.7 per cent and imports increased by 20.8 per cent.

In February of 2004, the Russia's active balance of trade made US \$ 5.6 billion, what was by 14 per cent below the level observed this January and by 19.3 per cent above the figures registered in February of 2003.



Source: RF Goskomstat

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

In February of 2004, export to countries outside NIS made US \$ 10.1 billion (by 20.9 per cent above the respective indicator of the preceding year). The business situation on the world market favorable for Russian exporters remained the major factor of growth.

In February of 2004, world oil prices remained at a high level, although demonstrating a slight downward trend. Thus, the average Urals price made US \$ 27.8 per barrel (a 3.8 per cent decrease as compared with the figures registered in January of 2004), while the average Brent price was at US \$ 30.8 per barrel (a 2.2 per cent decrease). The major factors behind the persisting high oil prices were the continuing turmoil in Iraq and Venezuela, as well as the uncertainty about further steps of the OPEC member countries concerning regulation of oil extraction.

Contract prices of Russian natural gas declined by 0.2 per cent in comparison with the figures observed in January of 2004.

In February of 2004, the prices of the majority non-ferrous metals continued to rise on the world market. The average monthly aluminum, copper, lead, zinc, tin, and nickel prices increased in comparison with the figures observed in the January of 2004 by 4.9 per cent (US \$ 1685.6 per metric ton), 13.9 per cent (US \$ 2759 per metric ton), 17.2 per cent (US \$ 888 per metric ton), 6.9 per cent (US \$ 1087.3 per metric ton), 2.9 per cent (US \$ 6668.3 per metric ton), and 0.5 per cent (US \$ 15178.3 per metric ton) respectively.

Aluminum prices demonstrated an upward trend due to the shortage of aluminum oxide. The continuing growth of nickel prices was determined by increasing demand on the part of China.

On the average, in February of 2004 the world prices of the staple Russian exports declined by 1.8 per cent in comparison with the figures registered in the preceding month.

Table 1.

The average monthly world prices in February of the respective year

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|---------------------------------|--------|--------|--------|--------|---------|--------|--------|---------|---------|
| Oil (Brent), USD / metric ton | 17,3 | 21,4 | 15,0 | 10,8 | 26,9 | 27,2 | 20,3 | 32,1 | 30,9 |
| Natural gas, USD / thous. c. m. | | 78,7 | 71,2 | 72,7 | 101,0 | 201,5 | 80,7 | 227,4 | 193,1 |
| Gasoline, USD / metric ton | 192,6 | 233,0 | 181,3 | 187,3 | 333,5 | 315,1 | 220,0 | 373,1 | 373,3 |
| Copper, USD / metric ton | 2552,9 | 2392,0 | 1673,3 | 1414,8 | 1779,1 | 1811,4 | 1601,5 | 1705,9 | 2759,0 |
| Aluminum, USD / metric ton | 1597,8 | 1567,7 | 1479 | 1188,1 | 1584,2 | 1602,1 | 1370,8 | 1428,04 | 1685,6 |
| Nickel, USD / metric ton | 8091,5 | 7670,8 | 5462,2 | 4629,4 | 10269,6 | 6544,6 | 6042,7 | 8619,64 | 15178,3 |

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

In February of 2004, the amount of Russian imports from countries outside NIS made US \$ 5.1 billion, what was by 22.5 per cent above the figures registered this January, and by 21.7 per cent above the level registered in February of 2003. The Ruble appreciation and increasing real cash household incomes still remain the major factors behind the growth in imports.

The continuing economic growth and relatively low inflation facilitated a growth in the real disposable cash household incomes. In January and February of 2004, they increased by 15.3 per cent as compared with the level registered in the respective period of the preceding year (in January through February of 2003 the growth made 15.7 per cent). As adjusted for the seasonal factors, this February the real disposable cash household incomes increased by 1.0 per cent in comparison with the figures registered in the preceding month.

The quotas on import of meat introduced last year bring their results. In January through February of 2004, import of frozen and refrigerated pork and beef from countries outside NIS diminished by 70.9 per cent in comparison with the figures registered in the respective period of 2003 and made 36200 million metric tons. The amount of pork and beef imports made US \$ 60.6 million as compared with last year US \$ 161.9 million. Import of poultry declined by 52 per cent and made 77800 metric tons.

At the same time, the policy aimed at support of domestic car manufacturers by introducing prohibitive duties on import of cars manufactured abroad failed. Over the two years the customs barrier have been in place, the domestic car producers were unable to improve the quality of their products or increase the output.

The customs measures also failed to check import of cars. In January through February of 2004, Russia's import of cars from countries outside NIS grew 2.4 times as compared with the figures registered in the respective period of the past year making 37.5 thousand cars. At the same time, 58 per cent of the cars imported by Russia are used cars manufactured 3 to 7 and more years ago. Import of foreign cars continues to grow even at the background of new restrictions set on foreign car imports last year. It should be reminded that in the summer and autumn of 2003, according to the concept of development of the Russian motor vehicle industry aimed to assist Russian car factories to be more competitive and attract foreign manufacturers to Russia, there were introduced more strict regulations concerning not only used, but also newer foreign cars. Thus, as concerns import of cars manufactured 7 and more years ago, at present the respective customs duties vary from Euro 2 to Euro 3 per 1 cubic cm. depending on motor capacity. Import duties on the cars aged 3 to 7 years made from Euro 0.85 to Euro 2.25 per 1 cubic cm. Besides, it should be reminded that on December 11, 2003, there were introduced import duties on newer cars with motor capacity from 1800 to 2300 cubic cm. making 25 per cent of their customs values, but not less than Euro 1.8 per 1 cubic cm.

The upward trend observed with respect to import of cars will most probably persist. The factors behind this trend are low quality of cars of Russian manufacture and as yet insufficient production of foreign cars assembled in Russia. Besides, in April Mikhail Fradkov, the new head of the Russian Government, promised Romano Prodi, the President of the European Commission to comply with one of the requirements the EU

set concerning Russia's accession to WTO, i.e. to reduce the maximal import duty on new foreign cars from 35 per cent to 20 per cent. At the same time, the RF Ministry of Industry and Power Engineering proposed to reduce import duties on completing parts imported by Russia for the purposes of assembly of foreign cars. Already this year, the respective customs duties may be reduced 10 times, from 30 per cent to 3 per cent. Therefore, the policy aimed at the protection of the domestic car manufacturers pursued by the former Cabinet of Ministers has in fact failed.

According to the available statistics, in February of 2004 Russian export to CIS member countries made US \$ 1.88 billion and increased by 23.8 per cent as compared with the figures registered in February of 2003, while imports made US \$ 1.29 billion growing by 28.8 per cent over the same period of time.

An actually functional free trade zone with Ukraine, the largest trading partner of Russia among the CIS member countries, could become a positive factor facilitating the development of mutual trade. This initiative was proposed by Ukraine in the course of recent negotiations between representatives of two countries. However, this initiative may fail because of the numerous trade conflicts in certain areas (for instance, pipes, oil, and natural gas) observed over the last three years.

Yet in July of 2001, Russia imposed VAT on the export of energy resources in retaliation to unsanctioned taking of natural gas transported via Ukraine. Therefore, Ukrainian exporters have to pay VAT twice, as Ukraine refuses to join EvrAzEs, where VAT has been since long paid on the destination country principle. As concerns natural gas exports, it should be mentioned that these exports only cover the payment for transit via Ukraine territory. This year, it is planned to export to Ukraine 24 billion cubic meters of natural gas at US \$ 50 per one thousand cubic meters. In spite of relatively small volumes of export of Russian oil to the CIS member countries (about 750 thousand barrels a year, while the total volume of oil exports makes more than 4 million barrels), the existing system of taxation of foreign trade in practice prevents an increase in the volume of mutual trade.

The customs authorities of Russia periodically carry out inspection campaigns as concerns Ukrainian imports, for instance, meat, in order to stop illegal import of meat produced in the countries outside NIS. This problem became especially urgent after Russia had introduced quotas on meat imports. In April, there was issued a special letter to the customs "On strengthening control over import of poultry, beef, and pork; and on the methodological recommendations concerning the assessment of the quality of meat," which informed that there might be made attempts to circumvent the meat quotas by declaring a wrong country of origin of the goods, or import meat in excess of the quotas.

N. Volovik, N. Leonova

April of 2004: Political outcomes

After the preceding month, which witnessed a large number of important events, in April there were observed much less administrative measures, appointments and dismissals. At the same time, important developments occurred in the sphere of ideology as after the new Russian Government had been formed it was of interest, what first statements this new Government would make to address the society. Naturally, after the completion of the Presidential elections the political forces should finalize their assessment of the outcomes of the election cycle of 2003 and 2004.

The restructuring of the RF Government and the Presidential Administration continued. It was announced that the Ministers would have only two deputies, however, the issue of armed forces and law enforcement agencies remained unresolved. As it could be expected, the preparation of recommendations concerning the new structure of ministries and departments was delayed until April 6, 2004, and brought about a number of conflicts, similarly to the problem of the announced reduction of officials employed by the executive authorities. However, the functions of regulation-making, control, and service remained undivided as concerns many key parameters⁹. Some key position remained vacant, primarily as concerns the sphere of armed and law enforcement ministries and departments, customs service, as well as state owned companies (or state representatives in the management of companies where the state has no controlling interest) and the stuff of the Government. It should be mentioned that the functions of the latter were not defined either in practical, or

⁹ Thus, the resolutions of the RF Government approving the new package of powers vested with the Ministries contain the typical wording that they should "coordinate and control the activities of subordinated..." (there follows the names of respective services and agencies), while the powers wielded by agencies are typically reduced to "licensing" and "issuance of individual legal acts."

legal terms. Only by the end of the month there were news about the long awaited appointments to the still vacant offices.

The formation of the structure of the Presidential Administration (with the exception of the Control Department, which, however, ceased to play an important role in the system of authorities) has been also completed. According to the new allocation of responsibilities, I. Sechin, appointed as the deputy head of the Administration was vested with the powers to appoint junior and medium ranked staff officials (starting with the heads of departments) and sign labor contracts; at the same time he retained his responsibilities concerning the flow of documents. The other deputy head of Administration, V. Surkov, continued to supervise domestic affairs (the State Duma, Federation Council, Central Election Commission, parties); however, at the same time he was vested with the right to sign financial documents alongside with the control over the most important sphere of regional policies. As concerns this new structure, it is apparent that the role played in it by the formal head of the Presidential Administration D. Medvedev becomes less important, since his powers relating to the interaction with the RF Government, courts, and the procurator's office in fact overlap with the functions of different advisors of the President.

Because of the restructuring of the Government, practically all measures planned to be taken in the sphere of announced priorities (the reform of the education system, public health care, mortgage, natural monopolies) have been delayed. The package of measures aimed to achieve an increase in taxation of profits of oil companies approved by the State Duma had been worked out a long time ago. The most clear illustration of the present situation is the sphere of electrical power engineering, where such key problems as the mechanism of purchase of shares in wholesale generating companies and abandoning of the system of cross subsidization, which had been already delayed for a year, have been delayed again for an undefined period, at least until June 30 of 2004, since the new Prime Minister said that he needed some time to "familiarize himself with the problem."

As concerns the sphere of public politics, in the past month (on March 29, 2004) the Vesti newspaper, one of the leading business publications, published a text signed by M. Khodorkovsky – "Crisis of Liberalism in Russia," which apparently was written in consultation with a publicist of the post-Soviet school of thought. The text puts the blame for the defeat of the liberal forces in the recent elections on the reformers responsible for the economic reforms undertaken in the country in the 1990s, personally naming Ye. Gaidar and A. Chubais, and the method of implementation of these reforms. According to the official ideology of the United Russia party¹⁰, the contrast to this tragic for the majority of citizens period is the rule of V. Putin, who is often favorably referred to in the document. President V. Putin and his administration are characterized as the chief defenders of business against the threat of the real populists like Rodina and LDPR. At the same time, the fault of entrepreneurs is that in the 1990s they supported the reformers, who implemented "wrong" reforms. However, the only recipe the party is ready to offer in order to put the end to the crisis is appeals to patriotism and so on, what can not be measured in qualitative or quantitative terms. Shortly after the publication of the article, L. Nevzlin, who was a Khodorkovsky's partner, stated that he is going to stop the financing of opposition parties, and it appears that B. Berezovsky will act in the same way according to his recent statements.

The politically significant consequences of the publication may include, first, that M. Khodorkovsky ceases to be a political figure, since the document signed by him confirms all real and imaginary allegations his critics made against him personally, including the clear allegations about his unlawful activities¹¹. Second, several major sponsors of any opposition projects abandon their activities in the sphere of public politics, what should render more difficult to rise funds basing on their personal antipathy to V. Putin. On the other hand, there shrink the possibilities to organize pseudo-opposition projects disposing of no other resources than the ability to please investors. A clear ideological program and skilled management becomes the must.

¹⁰ In contrast to the "reformers" of the 1980s and 1990s, who failed to achieve the main goal – a growth in well being of the majority of people, WE ACCEPT ONLY THOSE REFORMS, WHICH ENSURE WELL BEING OF THE PEOPLE... Market romanticism should be replaced with state pragmatism oriented towards the practical results. The major condition necessary to achieve this goal is the stable growth of the economy at a high rate, not less than 8 per cent a year. www.edin.ru

¹¹ An entrepreneur, I say it as a former head of a largest Russian oil company, may much more easy to make arrangements with a few moderately greedy officials than agree his or her actions with the dense and competent network of public institutions / see Khodorkovsky's article in: Vedomosti, March 29, 2004.

As concerns the activities of the United Russia party, there were observed no significant developments in April.

Party formation processes continue on the right flank. For instance, a group of opposition minded journalists and politicians named “Committee 2008” is going to take part in organization of May Day demonstrations in stead of writing articles. There was established the “Democratic Alternative” club, however, all these structures still lack the necessary backbone, i.e. clear ideology and plans of development.

Restructuring processes continue on the left flank. After losing the Rodina brand, S. Glaziev has registered the public organization “For a Decent Life.” However, judging by his address to the party congress, he thought that the most suitable strategy for the next two years would be the abandon of involvement in “federal politics” due to the party organizational structure development considerations and the generally unfavorable period. The issue of political allies was not on the agenda. As concerns KPRF, the party continues to prepare for its congress to be held in the summer. The vote for the candidacy of N. Kharitonov and the failure of S. Glaziev in the Presidential elections have strengthened the position of G. Zyuganov. In this situation, the leader of the major competing group, G. Semigin, initiated the establishment of the next (after the NPSR) umbrella structure – the “Patriots of Russia” movement, although not canceling his formal membership in the KPRF. These hectic activities appear to be an evidence that the left wing forces focus on the struggle among themselves (against “moles”), while the authorities in fact in turn support the weaker left wing groups against the stronger ones. For instance, Glaziev was used to campaign against the KPRF, however, in the course of the election campaign Kharitonov, who stressed his sympathy to the executive authorities, was used in order to weaken Glaziev. An illustrative fact is also the started buying up of left wing media, which at the moment state that Putin is “the most left politician in Russia.” The processes underway on the left flank very much resemble the fierce mutual criticism between SPS and Yabloko parties.

At present, the conglomerate of left populist pro-Government forces headed by D. Rogozin’s Rodina conducts negotiations about creation of a union of smaller groups of the similar political orientation; however, it is too early to make any forecasts about the success of these activities.

It is possible that the forthcoming congress of the Agrarian Party will witness a radical change: the old party leader M. Lapshin, the head of the Republic of Altai, will be dismissed to be replaced by a large investor (for instance, A. Chepa, or someone from representatives of the RF Agriculture Ministry) intending to further develop this project along the lines of building a left paternalist party.

S. Zhavoronkov

State Individual Financial Obligation (SIFO): problems and prospects of development in the higher education system

In 2002, there was started the experimental approbation of the new mechanism of financing of higher education establishments based on the State Individual Financial Obligations (SIFO) system. The state announced that the priorities behind the SIFO introduction were:

- (1) creation of a more flexible system of state support of the higher education system resulting in an easier access of different categories of university entrants;
- (2) improved efficiency of utilization of financial resources allocated to the higher education system resulting from the development of the competitive environment for higher education establishments, more transparent financial flows in the higher education system.

The RF Government resolution No. 6 of January 14, 2002, “On carrying out an experiment on transition to financing of certain higher vocational education establishments via state individual financial obligations” approved the Regulations on the terms and procedure of the experiment in 2002 and 2003.

The Regulations set forth that the experiment on transition to financing of certain higher education institutions via state individual financial obligations should be carried out in interaction with the experiment on the introduction of the Unified State Exam (USE). SIFO is defined as a “certificate showing the results of the Unified State Examination passed by a citizen and the category of the financial obligation on the basis of which a higher education institution will be granted the budget funds aimed to finance the education of this citizen during the whole educational period in accordance with the state educational standard.”

As concerns the persons who did not pass the USE (those who had graduated before USE was introduced, graduates of educational establishment located in the regions, which do not participate in the experiment, etc.) or those who had not passed the USE components required to enter the concrete higher education institution, the state examination commissions for USE should organize the required USE examination.

Upon the completion of the experiment, the students who entered state higher education establishments on the basis of SIFO should continue their education on the same terms as during the experiment.

Higher education institutions in the jurisdiction of federal, regional, local executive authorities, which have the state accreditation and taking part in the USE experiment should be entitled to participate in the SIFO testing.

The higher education establishments going to take part in the experiment should determine and announce the cost of education for each specialization, direction, and form of education provided by them three months prior to the period set for the reception of the applications for entry. Such a higher education institution should enroll all first year students across all specializations only on the SIFO basis.

The number of students taught exclusively at the expense of the funds allocated on the SIFO basis should be not less than 50 per cent of the total number of students enrolled in the higher education institution, and not less than 25 per cent in each specialization.

In the case a citizen was not entitled to be taught exclusively at the expense of the budget funds and the cost of education exceeds the amount of his or her SIFO, such a citizen should make an agreement with the higher education institution and pay the difference between the cost of education and the amount of his or her SIFO according to the procedure set forth in such an agreement.

The Regulations stress that all higher education establishments taking part in the experiment should be financed from the federal budget in accordance with the regulatory and legal acts in the framework of treasury execution of the federal budget. At the same time, executive authorities of RF subjects and local governments should be responsible for the budget financing of the participant higher education establishments, which are in their respective jurisdictions, from their respective budgets.

In 2002, the RF Ministry of Education and the RF Finance Ministry issued their joint resolution No. 1597 / 39n "On approval of the methods pertaining to the planning and financing of expenditures of the federal budget for higher vocational education made on the basis of state individual financial obligations as concerns the higher education institutions taking part in the experiment." According to these methods, five categories of SIFO should be introduced for the period of the experiment. These 5 categories should correspond to the respective number of points citizens were given as they passed USE component examinations (see Table 1).

Table 1.

Correspondence between the sum of USE points, SIFO category, and its amount

| SIFO category | USE points |
|---------------|--------------------|
| Category 1 | More than 80 - 100 |
| Category 2 | More than 68 -80 |
| Category 3 | More than 52 -68 |
| Category 4 | More than 43 - 52 |
| Category 5 | More than 35 - 43 |

The list of higher education establishments taking part in the experiment as approved by the resolution RF Ministry of Education No. 1013 of March 25, 2002, included 6 higher education institutions from 3 RF subjects, namely: Mari State Technical University; Mari State Pedagogical Institute named after N. K. Krupskaya; Mari State University; Chuvash State University named after I. N. Ulyanov; Chuvash State Pedagogical University named after I. Ya. Yakovlev; Yakut State University. It should be noted that the higher education institutions situated in the Republic of Mari El and the Chuvash Republic also took part in the USE experiment.

It should be also noted that no private higher education institutions or regional branches of central state universities situated in the Republic of Mari El and the Chuvash Republic did not take part in the experiment. Besides, higher education establishments run by various departments also did not agree to participate in the SIFO experiment, what had significantly deteriorated representative qualities of the experiment in the selected territories.

In the course of the enrollment campaign of 2002 / 2003 carried out by 6 higher education establishments taking part in the experiment, more than 14.3 thousand persons out of 35 thousand applicants became first year students, of which more than 8.4 thousand, or 58 per cent of the total number of the first year students, were enrolled basing on SIFO.

For the distribution of budget resources and first year students across SIFO categories and higher education establishments see the Table below:

Table 2.

Distribution of budget resources and first year students across SIFO categories and higher education establishments in 2002 and 2003 (across all forms of education, in %)

| SIFO category | Distribution of first year students | | Distribution of budget funds basing on SIFO | |
|---------------|-------------------------------------|------|---|------|
| | 2002 | 2003 | 2002 | 2003 |
| Category 1 | 8 | 11,6 | 20 | 28 |
| Category 2 | 39 | 27,5 | 49 | 38 |
| Category 3 | 37,6 | 42,7 | 25 | 28 |
| Category 4 | 10,8 | 12,5 | 5 | 5 |
| Category 5 | 4,7 | 5,7 | 1 | 1 |

Source: the data presented by State University – Higher School of Economics (GU – VshE)

The amounts of SIFO in each category should be determined by the RF Ministry of Education for each financial year.

Therefore, SIFO entitles the student to be taught at a higher vocational education institution at the expense of budget resources, however, the amount of these funds would depend on the USE results of this student and the amount of budget resources allocated by the state for higher education in the annual budget. The share of first year students being taught at the expense of the federal budget funds, and those who had to make additional payments (full time students), made 58.8 per cent and 41.2 per cent respectively in 2002 and 58.6 per cent and 41.4 per cent respectively in 2003.

It should be noted that higher education institutions have the right to use the SIFO funds for such expenditure items as wages, salaries, and other current expenditures. Higher education institutions should cover other expenditure items using the funds they receive in the framework of the present estimate-based financing system. The planning of expenditures for the next years should take into account the number of students advanced to the next year level, changes in SIFO amounts per category, and the amount of federal budget funds allocated for the current year. For instance, the amount of SIFO across all categories diminished significantly in 2003 as compared with the figures registered in 2002 (see Table 3 below).

Table 3.

SIFO amounts as broken down by category in 2002 and 2003

| SIFO category | Amount of SIFO budget financing, Rub. | | |
|---------------|---------------------------------------|----------------------------|------------------------------|
| | Approved amount of SIFO * | Approved amount of SIFO ** | Increased amount of SIFO *** |
| | 2002 | 2003 | 2003 |
| Category 1 | 14500 | 12500 | 17500 |
| Category 2 | 7500 | 7200 | 12200 |
| Category 3 | 3900 | 3000 | 8000 |
| Category 4 | 2800 | 2000 | 2000 |
| Category 5 | 1200 | 700 | 700 |

* approved by order of the RF Minister of Education No. 1013 of March 25, 2002

** approved by order of the RF Minister of Education No. 1193 of March 26, 2003

*** approved by order of the RF Minister of Education No. 2376 of June 3, 2003

This situation may to a considerable degree explain the wish of the RF Ministry of Education to create such a mechanism of financing of higher education establishments, which could more adequately and flexibly ensure the budget support of education of specialists primarily needed by regions. Thus, resolution of the RF Ministry of Education No. 2376 of June 3, 2003, “On the development of the experiment on transition to financing of certain higher vocational education establishments via SIFO” envisages that in 2003, RF subjects and higher education institutions taking part in the experiment should jointly set forth lists of professions especially important for the social and economic development of regions, where the number of enrolled students is insufficient.

According to the list of professions, the amount of SIFO (categories 1, 2 and 3) financing should be increased. However, the total number of persons enrolled to be taught the listed profession should be at or below 300 persons per region, while in the case a student abandons a specialization put on the list and takes some other profession, the increased financing is not retained.

The complexity and multi-aspect nature of the experiment on financing of higher education institutions on the base of SIFO have unavoidable demonstrated both positive and negative financial, economic, and social consequences of the introduction of new approaches to the issues of current financing of higher education establishments.

On the whole, it appears that positive aspects of the SIFO mechanism include the following:

First, the development of per capita financing principles in relation to higher education institutions, i.e. budget financing based on the number of enrolled students and not any other arbitrary decisions.

Second, it permits to avoid the present situation, where the student either enters the budget department of a higher education establishment and is taught free of charge, or has to pay the full price of education because of the poor results of his or her entry examinations. The SIFO system permits to mix budget and private funds in order to pay for education.

Third, the SIFO system is naturally related to another institutional innovation, namely the institution of the unified state examination (USE), in a way linking the amount of funds allocated by the state for financing of students with the USE results (in fact, the single graduate / entry examination). In other words, SIFO creates economic incentives to learn better when in school.

Fourth, the SIFO institution should carry out a natural reorganization and restructuring of the system of higher education establishments. The main regulator of the system is the demand on the part of the population and not administrative measures. The students with the highest USE levels will receive more budget money via higher SIFO categories and, therefore, higher education establishments where such students concentrate will receive more budget funds. In other words, this system enhances competition in this sector. Competition should become one of the major factors ensuring the improvement of the quality of higher education system and an indicator of its real public and market evaluation.

Since the SIFO mechanism is a new mechanism of *financing* of higher education establishments, the problems encountered in the process of the experiment are primarily of financial nature.

First, it is instability of the amount of SIFO financing related to the current budget situation in a given year.

Second, it was revealed that in the case SIFO amounts are insufficient to cover the full costs of education of a student, it creates additional problems. In fact, this problem may result in the situation, where the whole higher education system is made "paid" *de facto*. Therefore, the problem of access to education will persist.

Third, the amount of SIFO is not differentiated across professions, although it is clear that the costs of education of a nuclear physicist are different from the expenditures for economists or jurists.

It is apparent that respective answers can not be found in the current framework of the experiment.

The transformation of the mechanism of financing of higher education establishments based on SIFO should be supplemented with the mechanism of state procurement concerning socially important professions necessary to develop fundamental science and new technologies in the country. Such a mechanism should create effective economic incentives for students demonstrating best results to choose the respective specializations. Otherwise, the fundamental component of the domestic higher education system may collapse in the nearest future.

I. A. Rozhdestvenskaya

Issues discussed at the meetings held by the Government of the Russian Federation on April 8, 15, and 21 of 2004

In the period from April 1 to April 26 of 2004, the RF Government held four meetings, in the course of which there were examined various issues..

The most interesting issues include the report of the RF Finance Minister A. L. Kudrin "On the measures aimed at the completion of the tax reform in 2004 through 2005 and draft federal laws aimed at the improvement of the RF legislation on taxes and fees" presented at the RF Government meeting held on April 8, 2004; the report of the RF Finance Minister A. L. Kudrin "On measures aimed to enhance the effectiveness of budget expenditures and reform of the budget process in the Russian Federation" presented at the RF Government meeting held on April 15, 2004; and the report of the RF Minister of Health Care and Social Development M. Yu. Zurabov "On the progress of the pension reform" presented at the meeting held on April 21, 2004.

At the meeting of the RF Government held on **April 8 of 2004**, A. L. Kudrin, the RF Finance Minister, presented his report “On the measures aimed at the completion of the tax reform in 2004 through 2005 and draft federal laws aimed at the improvement of the RF legislation on taxes and fees.”

In his report, the Minister noted that in April of 2003 the RF Government approved the key guidelines of the tax reform for years 2004 through 2006. The guidelines in particular envisaged that the course towards further reduction of the tax burden, simplification of the tax system in general, and improvement of tax administration should be continued. The report also noted the necessity to somewhat adjust the priorities of the tax policy, in particular correct the imbalances in the level of tax burden on the raw material sector and the rest of the economy.

The RF Government has approved in general the *draft federal law “On amendments to article 22 “Excises” of the second part of the RF Tax Code.”* The draft law envisages certain measures aimed to retain relative levels of budget revenues generated by excises imposed on excisable goods subject to specific (set in absolute amounts per measurement unit) tax rates in the situation where the average level of prices of consumer goods increase and taking into account the estimated inflation rates in 2005.

It is proposed to carry out the indexation of the specific excise rates on excisable goods with the exception of cigarettes by 8 per cent. As concerns cigarettes, taking into account the decision taken in the course of introduction of combined excise rates it is proposed to index the specific components of the tax to a higher degree. It is proposed to set the specific excise rate at Rub. 70 per 1000 pcs. on filtered cigarettes and Rub. 30 per 1000 pcs. on non-filtered cigarettes. The ad valorem component should be retained at 5 per cent of the producers’ prices. At this rate of indexing, the share of excises in the price of cigarettes will make about 25 per cent on the average.

The RF Finance Ministry and the RF Ministry of Economic Development were instructed to elaborate this draft law in coordination with the RF Ministry of Agriculture as concerns the proposed indexing of excises on tobacco and alcohol beverages.

The RF Government has also approved in general the draft federal law “On amendments to article 3 of the law of the Russian Federation “On customs tariff” and article 5 of the federal law “On amendments to the second part of the RF Tax Code and certain other legislative acts of the RF, as well as invalidation of certain legislative acts of the Russian Federation.”

This draft law is aimed to improve the taxation of the oil industry and permits to increase the rent component of taxation of oil companies and ensures an additional withdrawal of proceeds notwithstanding the type of activities oil companies are engaged in.

It is planned to withdraw only the profits which are not efficiently used from the point of view of the state, for instance, excessive amounts of dividends and investment in non-related assets.

The review of different variants of changes in the mineral extraction tax rates and export duties showed that the mixed variant in the framework of which both rates of export duties on oil and oil products and the formula of the mineral extraction tax rate are changed is most feasible.

It is proposed to change the current scale of the export oil duties and introduce an additional price interval: at oil prices from US \$ 20 to US \$ 25 per barrel the rate of the duty should make 45 per cent. In the case the oil price is above US \$ 25 per barrel, the export duty rate should be at 65 per cent, the base mineral extraction tax rate for oil should be increased from Rub. 347 to Rub. 400 per metric ton. At the same time, there should be changed the adjustment coefficient (Kts) calculated as the ratio between the current US \$ exchange rate and the average forecasted exchange rate, the latter should be reduced from Rub. 31.5 to Rub. 29.

In the case these proposals are implemented and oil prices are at US \$ 24 per barrel, the federal budget revenues will increase by about US \$ 1.2 billion and by US \$ 2.6 billion in the case oil prices will be at US \$ 27 pr barrel.

At the meeting, the RF Finance Ministry was instructed to elaborate this draft law in coordination with the RF Ministry of Industry and Power Engineering, including the issue of financial and economic feasibility study of the decision.

According to IET experts, the proposed measures concerning the export duty scale will allow, first, to more precisely take into account the amounts of additional natural rent related to the rise of the world oil prices and, second, focus the efforts on withdrawal of natural rent primarily as concerns the exported oil.

As concerns the draft law, a few comments should be made about the entry into force of proposed changes in the mineral extraction tax rates and the Kts coefficient. According to the new version of article 5 of the

draft law “On amendments to the second part of the RF Tax Code and certain other legislative acts of the RF, as well as invalidation of certain legislative acts of the Russian Federation,” the new rate of the mineral extraction tax (Rub. 400 per metric ton) and the new formula, according to which the Kts coefficient is calculated, should be in force from January 1, 2002 till December 31, 2006. Due to the fact that this version of the law may be interpreted as a worsening of the taxpayer’s situation (changes in the past obligations), it appears to be more feasible to concretize the amendments to article 5 of the draft law mentioned above.

The RF Government has approved in general the *draft federal law “On amendments to article 25 of the RF Tax Code and certain other legislative acts concerning taxes and fees”* aimed to more precisely define certain regulations pertaining to taxpayers, harmonize fiscal and general accounting principles, and resolve a number of other problems encountered in the course of implementation of this article.

In particular, the following measures are proposed to harmonize the principles of general and fiscal accounting:

- Introduction of an open list of direct costs;
- Recognition of the taxpayer’s right to independently determine the procedure governing the attribution of direct costs to uncompleted construction and finished stocks;
- Actual abolishment of the LIFO method of evaluation of finished stocks;
- Recognition of capital investment in leased fixed assets as depreciable property;
- Determination of the cost and terms of the beneficial use of property received as a contribution to the authorized capital on the basis of the accounting data presented by the transferor;
- Determination of the purchase prices and income on forex denominated securities in accordance with the CB RF exchange rate on the day of entering of the security in the books or on the day the respective transaction was performed.

It should be pointed out that the introduced measures will entail both positive and negative consequences..

The regulation concerning the classification of direct costs as expenditures for taxation purposes at the moment of sale of goods (item 35, article 1 of the draft law) may result in inconsistencies in the case the tax earnings and expenditures are determined in accordance with the cash basis method of accounting, especially for enterprises with longer production cycles.

The wording “In the case it is impossible to attribute direct costs to a concrete production process related to the production of this type of products... in the framework of accounting policies, the taxpayer should determine the mechanism of distribution of the said expenditures basing on the indicators substantiated in economic terms” (item 36 of article 1 of the draft law) is inconsistent. First, it is doubtful if it is necessary to take into account individual production processes for taxation purposes. Second, even in the case this degree of detailing is recognized as necessary, the expenditures mentioned in the law can not be defined as direct costs in this context, since direct costs are expenditures directly attributable to a concrete accounting item (in this case it is a production process). In the case such expenditures can not be attributed to a concrete production process, they can not be recognized as direct costs. .

According to item 23, article 1 of the draft law, the market revaluation of securities should be prohibited. In this connection, since Russian enterprises are introducing the IAS it would be feasible to account for securities according to their fair (market) price and therefore take into account the differences arising due to revaluation as proceeds or expenditures of the respective period.

According to the draft law, in the course of evaluation of forex denominated securities the exchange rate differences are not reflected in the composition of respective proceeds and expenditures not related to production and sales (item 12, article 1 of the draft law). At the same time, the exchange rate differences should be reflected in the composition of respective proceeds and expenditures not related to production and sales as concerns forex denominated claims and liabilities. The advantages of this measure remain unclear and require some explanation. Moreover, it is unclear why securities are excluded from this list. Besides, the generally accepted principles of accounting for securities in accordance with their current market value should not be rejected.

In the case the proposed amendment is approved, the procedure of reflection of exchange rate differences concerning forex denominated convertible bonds also remains unclear..

The regulation that property received as a contribution to the authorized capital should be entered in the books at the value determined on the basis of tax accounting data on the transferor (item 21, article 1 of the draft law) ensures the continuity of the tax accounting data and facilitates the prevention of setting too high the amounts of amortization aimed to minimize the amount of the profit tax in the case the transferred prop-

erty is unjustifiably overvalued by the parties engaged in the transaction. At the same time, it should be noted that evaluation of the market value of such property at the moment of its transfer to the authorized capital, in spite of all its merits, may be too difficult under the present conditions in Russia. In the case the information about the market price of such property is unavailable (in the absence of the respective market), evaluation may be rendered too difficult, since in Russia there is no tradition to use estimates in the framework of fiscal accounting. Moreover, the concept of market (fair) value as a component of IAS is still disputable.

Therefore, the positive results of harmonization of general and fiscal accounting principles are reduced only to simplification of the calculation of the profit tax. It should be noted that harmonization of general and fiscal accounting should not be set as a goal *per se*, since these two systems of accounting were created for different purposes and, therefore, can not use the identical methods.

The amendments discussed above touch upon a number of problems, which as it seems were not sufficiently taken into account in the framework of proposed measures.

According to the draft law, the pension insurance payments made in accordance to the scheme envisaging that pension contributions will be accounted for after they are transferred to individual accounts with private pension funds should be defined as expenditures for wages and salaries and therefore should be deducted from the amounts subject to taxation. It should be noted that the introduction of this measure may create incentives for pension insurance of higher paid employees entailing deduction of respective expenditures from the profit tax base, i.e. the greater regressivity or lesser progressiveness of the tax system. Perhaps, in order to prevent this, it would be feasible to add a regulation stipulating that only the amounts exceeding certain limit per insured person should be deductible.

Proposed amendments to article 277 as concerns the determination of the purchase value of shares purchased in the course of reorganization of enterprises require a further discussion (item 21, article 1 of the draft law). First of all, it remains unclear for what article of the Code these amendments were proposed. Item 4, according to which the purchase value of shares in a newly created enterprise is recognized to be equal to the value of a converted share in a reorganized enterprise according to the fiscal accounting data raise no doubts only in the case the conversion is carried out at the 1 to 1 rate. It is necessary to introduce a special regulation for other proportions of conversion.

Item 5 also raises certain doubts. The determination of the value of shares received in the process of reorganization in proportion to the value of net assets of enterprises may be incorrect in the case even one enterprise have negative net assets, what at present is not always related to loss making. Therefore, it is seen that there exist factors which may influence the amount of net assets without deteriorating the standing of the enterprise.

As concerns amendments to item 5, article 283, according to which in the course of reorganization the succeeding taxpayer should have no right to deduct losses, which had taken place before the reorganization (item 25, article 1 of the draft law), it should be noted that under the existing limitations on the deduction of losses occurring in past years this regulation will have no significant impact beside introducing an additional limitation on write off of losses, which will be effective (especially as concerns small businesses).

At the same meeting of the RF Government there were approved in general the draft amendments to draft federal law No. 314634-3 “*On amendments to article 241 of the Tax Code of the Russian Federation*” aimed at improvement of the single social tax (SST).

The draft law “*On amendments to to article 241 of the Tax Code of the Russian Federation*” introduced by a number of State Duma deputies envisages a reduction of the SST rates for all categories of taxpayers pointed out in article 241 of the Tax Code of the Russian Federation with the exception of lawyers. It is proposed to set the following scale of tax rates as concerns employer organizations: the annual amount of payments per one employee below Rub. 50 thousand – 30 per cent, Rub. 50001 to Rub. 60 thousand – 15 per cent, over Rub. 600 thousand – 5 per cent.

It is proposed to abolish the regulation setting limits on the application of the SST regressive scale as concerns the exception of highly paid employees for the purposes of calculation of the average sales and wages in order to determine if the organization is entitled to apply the regressive scale of taxation.

The RF Government has discussed certain issues pertaining to the progress of the tax reform and there was taken a decision to reduce the effective rate of the single social tax (SST) in 2005, while implementing the related measures in the sphere of pension, health, and social insurance. After a discussion of different proposed approaches, it was decided to reduce the tax rate by setting the following SST rates as concerns employer organizations: the annual amount of payments per one employee below Rub. 300 thousand – 26 per

cent, Rub. 300001 to Rub. 600 thousand – 10 per cent, over Rub. 600 thousand – 2 per cent. It is envisaged that these regulations will be introduced on January 1, 2005.

For the purposes of implementation of this decision, the RF Finance Ministry has proposed draft amendments to the draft federal law introduced by the State Duma deputies.

There are also envisaged the respective amendments to the federal law “On mandatory pension insurance in the Russian Federation,” which concern the insurance contribution tariffs pertaining to the mandatory pension insurance.

The rate of tariffs on the mandatory pension insurance was retained at 14 per cent, while the rates are reduced as concerns the amounts due to the federal budget – from 14 per cent to 6 per cent, social insurance fund – from 4.0 per cent to 3.2 per cent, and mandatory health insurance funds – from 3.6 per cent to 2.8 per cent.

At the same time, it is assumed that only contributions for financing of the cumulative component of the labor pension for persons born in 1967 and later should be mandatory in the composition of contributions for mandatory pension insurance.

Along with mandatory contributions, it is also envisaged that employees of all ages should have the right to make voluntary contributions for financing of the cumulative part of their labor pensions since 2005. This issue was discussed at the RF Government meeting held on April 21, 2004 (see below).

According to IET experts, the proposed reduction of the SST effective rate will result in a reduced burden on taxpayers and under certain conditions may facilitate legalization of wages and salaries.

Yet another positive factor is that the draft law envisages a reduction in the number of SST related privileges and exemptions (it is proposed to abolish SST exemptions as concerns the amounts paid as cooperative membership fees, amounts paid from trade union funds, in kind remuneration for employees, compensations for purchased medicines, the exemptions from the federal share of SST as concerns cash remuneration of justices of peace, exemption of amounts paid in accordance with license agreements from the list of SST exempted payments).

Besides, the draft law is aimed to resolve a number of technical problems relating to the calculation and payment of the SST, which are encountered in the process of enforcement of the respective regulations set by the RF Tax Code, and the issues of SST collection pertaining to lawyers in connection with the approval of the federal law “On the legal profession.”

It appears that the transfer of the burden of formation of the base part of the labor pension to the federal budget is justified taking into account the fact that, first, the determination of the minimal pension notwithstanding its nature is rather an issue of social and not pension policy, and, second, it will reduce the share of redistributed component in the system of mandatory pension insurance.

However, the draft law is not free of flaws. For instance, a serious problem is the use of different schemes resulting in unjustified reduction of SST obligations via the use of services of organizations and individual entrepreneurs entitled to SST related privileges or subject to special taxation treatments (public organizations of invalids, as well as the small businesses, which have switched to the simplified system of taxation or the single tax on imputed income). A complex settlement of these problems should be envisaged in the framework of the current stage of the tax reform, however, it was not reflected in this draft law.

At the meeting of the RF Government held on **April 15 of 2004**, A. L. Kudrin, the RF Finance Minister, presented his report “On measures aimed to enhance the effectiveness of budget expenditures and reform of the budget process in the Russian Federation.”

The proposed *Concept of the reform of the budget process in 2004 through 2006* is to create conditions and prerequisites for the efficient management of the state (municipal) finances in accordance with the priorities of the state policies.

In the framework of the concept of “performance management,” the budget should be formed proceeding from the objectives and planned targets of state policies. Budget allocations should be closely linked to functions (services, types of activities), and in the process of planning of budget targets special attention should be paid to substantiation of final results in the framework of budget programs. The independency and responsibility of administrators of budget projects are enhanced: there are set long term carry forward allocations subject to annual adjustment in the framework of medium term financial plans, there is formed the total amount of allocations (a global budget) for certain functions and programs, in the framework of which administrators are free to determine the degree of breakdown of objectives for which budget funds should be used, there are created incentives for optimization of the use of resources (personnel, equipment, premises, etc.) with priority of internal control, decision making responsibilities are devolved. There should be carried

out monitoring and consequent external audit of finances and results of activities, evaluation of administrators of budget funds is carried out basing on performance indicators.

The gist of the reform is to shift accents of the budget process from management of budget resources (expenditures) to performance management via enhancement of responsibility and independency of participants of the budget process and administrators of budget funds in the framework of clear medium term targets.

It is envisaged that the reform of the budget process should be carried out along the following avenues:

- 1) Reform of the budget classification and budget accounting;
- 2) Singling out the budgets of “actual” and “assumed” obligations;
- 3) Improvement of the medium term financial planning;
- 4) Development and enhancement of the sphere, where performance budgeting is applied;
- 5) Streamlining of procedures governing the formation and approval of the budget.

The measures aimed at the enhancement of efficiency of expenditures in the framework of the complex reform of the budget system include, alongside with the reform of the budget process, also the reform of the budget network (which is composed of the measures aimed at the reform of the status of budget organizations and the principles of their functioning), transition to new forms of financing of state (municipal) services, improvement of the procedures governing budget execution, including the elements of management of liquidity of single accounts of budgets in the framework of the RF budget system, and the reform of inter-budgetary relations.

The proposed concept develops further the work in the framework of the “Principles of restructuring of the budget sector in the Russian Federation” approved by the RF Government. Earlier, in the framework of this program responsible Ministries have prepared draft documents aimed at the elaboration of the regulatory and legal base for creation of new organizational and legal forms of state and municipally owned organizations in which the existing state institutions are to be transformed, as well as the streamlining of procedures governing the transfer of a number of budget institutions to the sub-federal level in accordance with the principles of division of powers between the levels of authority in the framework of the federative reform.

The principles underlying the Concept meet the requirements of the reform of the budget process, i.e. the switch from expenditure oriented approach to budgeting to performance budgeting and transition to the full fledged medium term budget planning. The fulfillment of these tasks is the key factor allowing to achieve the main objectives of the reform, i.e. higher stability of the budget system and higher quality of (primarily social) services rendered to the population at the expense of budget funds.

It should be noted that the sequence of goals proposed in the Concept – from those which may be settled in the current regulatory and legislative framework to those envisaging more significant changes in the regulatory and legislative base should ensure that the goals of the reform are achieved. In particular, the proposed staged introduction of the principle of division of the budget in the budget of “actual” obligations and the budget of “assumed” obligations, what allows to concretize the amount of mandatory budget obligations, creates prerequisites for fine tuning of the new system even before the respective amendments are made to the budget legislation.

At the meeting of the RF Government held on **April 21 of 2004**, the RF Minister of Health Care and Social Development M. Yu. Zurabov presented his report “On the progress of the pension reform.”

In his report, the Minister noted that taking into account the approved decision to reduce the rate of the single social tax, the RF Ministry of Health Care and Social Development is planning to modernize the cumulative component of the pension system by introducing additional pension insurance.

For the purposes of implementation of this concept, the RF Ministry of Health Care and Social Development has prepared the draft federal law “On amendments to legislative acts of the Russian Federation in relation to the introduction of additional pension insurance.”

It is envisaged that individuals should make agreements concerning the additional pension insurance with insurers. The agreements on additional pension insurance should envisage the payment of additional insurance contributions (at 4 per cent of the amount of remuneration due to the employee) to be transferred to the cumulative component of the labor pension. The payment of these contribution should be made by the employer on behalf and at the expense of the respective employee simultaneously with the payment of insurance contributions for mandatory pension insurance.

The draft law envisages that the federal budget should transfer to the budget of the RF Pension Fund the double value of one insurance year (Rub. 1008 as approved for year 2004) for each person making the agreement on additional pension insurance.

The proposed mechanism of financing of the cumulative component of the labor pension will permit to significantly increase the ratio between the pensions of future pensioners and the amount of the current average wages and salaries. At present this indicator is slightly below 30 per cent. In the case these proposals are implemented, the replacement coefficient should make 50 to 60 per cent as concerns persons aged 65 (taking into account the base, insurance, mandatory, cumulative, and voluntary components of the pension). It is envisaged that this coefficient should be higher for the persons with lower wages and salaries.

As an additional incentive for making the new system attractive for citizens, it is proposed to deduct the amount of voluntary payments for the financing of the cumulative component of labor pensions from the base of the income tax on individuals.

E. A. Bolshakova

Review of economic legislation: April of 2004

I. FEDERAL LAWS of the Russian Federation

1. "ON AMENDMENTS TO ARTICLE 42 OF THE FEDERAL LAW "ON JOINT STOCK COMPANIES" of April 6, 2004, No. 17 – FZ

Enters into force on July 1, 2004

The article was amended as concerns the procedure governing the payment of dividends by joint stock companies. The amendments set forth that the source of dividends should be the after tax profit (net profit) of the joint stock company. The net profit of the joint stock company should be determined in accordance with the company's accounting data. Dividends on preferred stocks of certain types also may be paid from the special funds formed by the company for these purposes.

2. "ON AMENDMENTS TO SECTION TWO OF THE TAX CODE OF THE RUSSIAN FEDERATION AND THE FEDERAL LAW 'ON AMENDMENTS TO ARTICLE 26.1 OF SECTION 2 OF THE TAX CODE OF THE RUSSIAN FEDERATION AND CERTAIN OTHER LEGISLATIVE ACTS OF THE RUSSIAN FEDERATION'"

Enters into force in one month since the day of promulgation.

There were approved the amendments to article 26.1 of the second section of the RF Tax Code. The amendments concern more precise determination of the procedures governing the switching of agricultural producers to the payment of the single agricultural tax and return to the general tax treatment. In particular, after the switching to the payment of the single agricultural tax the amounts of the value added tax paid prior to the switching to the payment of the single agricultural tax should not be returned. The term of submission of application for the switching to the payment of the single agricultural tax in 2004 was prolonged until June 1, 2004.

Legal relations formed since January 1, 2004, should be subject to this law.

II. REGULATIONS OF THE GOVERNMENT of the Russian Federation

1. "ON ORGANIZATION AND IMPLEMENTATION OF THE CHILDREN HEALTH CAMPAIGN IN 2004" No. 320-r of March 5, 2004

For the purposes to organize recreation, rehabilitation, and employment of children in 2004, the federal executive authorities and regional executive authorities were given respective instructions. In accordance with the stipulations of federal law No. 166-FZ of December 8, 2003, "On the budget of the Social Insurance Fund of the Russian Federation for year 2004" it is planned to pay (in full and in part) the costs of stay of children (aged 15 and below) of insured citizens in children all year rehabilitation camps, country stationary rehabilitation camps, and sports and rehabilitation camps from the funds of mandatory social insurance. It is envisaged that the Social Insurance Fund should finance the costs of food for the children staying in day time rehabilitation camps situated on school premises, which are organized by the educational executive authorities of the RF subjects, and compensate travel expenses of the persons accompanying children to and from rehabilitation camps, as well as pay such persons daily allowances (up to 3 days) at the rates applicable to business trips.

III. RESOLUTIONS OF THE GOVERNMENT of the Russian Federation

1. "ON THE SUBSIDIZING OF CERTAIN SECTORS OF AGRICULTURAL PRODUCTION FROM THE FEDERAL BUDGET FUNDS IN 2004" No. 210 of April 14, 2004

The resolution establishes that subsidies from the federal budget for the state support of certain sectors of the agricultural production should be granted in 2004 in accordance with the procedures set forth by Resolution of the RF Government No. 272 of April 6, 2001. The subsidies are granted to support Northern reindeer breeding, pedigree livestock farming, domestic sheep farming, elite seed farming, flax and hemp farming. At the same time, veterinary utilization plants are not entitled to subsidies, while garden farming, grapevine farming, hop farming, and tea farming may be entitled to subsidies in the case there are respective funds in the federal budget for 2004.

IV. INSTRUCTIONS, REGULATIONS, AND ORDERS

1. Order of the RF Tax Ministry “ON ORGANIZATION OF TAX ADMINISTRATION OF LARGEST TAXPAYERS AND APPROVAL OF THE CRITERIA DETERMINING THE CLASSIFICATION OF RUSSIAN LEGAL ENTITIES AS LARGEST TAXPAYERS SUBJECTED TO TAX ADMINISTRATION AT THE FEDERAL AND THE REGIONAL LEVELS” No. SAE-3-30/290@ of April 16, 2004

Entered into force on April 16, 2004

The order approves the criteria determining the classification of Russian legal entities as largest taxpayers subjected to tax administration on the federal and the regional levels. The following criteria should be applied in order to determine the status of a largest taxpayer: financial and economic accounting data for the reporting year (any reporting year after 2000); dependency relationships between organizations to be determined in accordance with the regulations set forth by article 20 of the first section of the Tax Code of the Russian Federation. Administration of the largest taxpayers (legal entities) at the federal level should be vested with specialized branch interregional inspections for largest taxpayers of the RF Tax Ministry and with inter-district inspections for largest taxpayers created within the structure of the RF Tax Ministry departments across the subjects of the Russian Federation.

There was abolished order of the RF Tax Ministry No. BG-3-08/279 of August 10, 2001, which set forth the criteria determining the classification of Russian legal entities as largest taxpayers subjected to tax administration by the federal and the regional tax authorities as amended by orders of the RF Tax Ministry No. BG-3-30/117 of March 6, 2002, No. BG-3-07/302 of June 14, 2002, and BG-3-30/690 of December 16, 2003.

2. Order of the RF Tax Ministry “ON APPROVAL OF THE PROCEDURES AND TERMS PERTAINING TO THE ASSIGNMENT, USE, AND CHANGE OF THE TAXPAYER IDENTIFICATION NUMBER AND THE FORMS OF DOCUMENTS REQUIRED IN THE COURSE OF REGISTRATION AND DEREGISTRATION OF LEGAL ENTITIES AND INDIVIDUALS” No. BG-3-09/178 of March 3, 2004

Registered by the RF Justice Ministry on March 24, 2004, No. 5685.

In the course of improvement of the procedures governing the state registration of legal persons and individual entrepreneurs, there were approved the new Regulations and terms pertaining to the assignment, use, and change of the taxpayer identification number and the forms of documents required in the course of registration and deregistration of legal entities and individuals. There were determined the special terms, on which taxpayer identification number (TIN) should be assigned to organizations, individuals, and individual entrepreneurs. The document approves the list of documents and data necessary for the registration and assignment of TIN; in the course of registration organizations should be assigned not only TIN, but also the reason of registration code (RRC). The TIN assigned to organizations and individuals should not be changed with the exception of cases where the Russian legislation or the Regulations are amended or restructured. The TIN should not be changed in the case individuals or organizations change their places of residence or locations. There were determined, in what cases TIN may be invalidated. All taxpayers should indicate their TINs on the documents submitted to the tax authorities. The assigned TIN may be confirmed by a certificate, notification about registration by the tax authorities, the information from the Single state register of taxpayers (SSRT) received according to the established procedures, and the mark in the passport of the citizen of the Russian Federation. The tax authorities should use TIN as the number of the taxpayer’s file both for individuals and legal entities. The order approves new forms of documents required for registration and deregistration of legal entities and individuals. The applications for registration or deregistration of legal entities and applications of individuals requesting the issuance of a document confirming TIN assignment are supplemented with the procedures governing the filling in of such applications.

3. Order of the RF Tax Ministry “ON TRANSFER OF INFORMATION CONCERNING THE OPENING (CLOSING) OF BANK ACCOUNTS AND CHANGES OF THE BANK ACCOUNT NUMBERS BY LE-

GAL ENTITIES AND INDIVIDUAL ENTREPRENEURS BETWEEN BANKS AND TAX AUTHORITIES IN ELECTRONIC FORM VIA TELECOMMUNICATION CHANNELS”

The order approves and enacts the regulation governing the transfer of information concerning the opening (closing) of bank accounts and changes of the bank account numbers by legal entities and individual entrepreneurs between banks and tax authorities in electronic form via telecommunication channels. The data on opening (closing) of bank accounts and changes of the bank account numbers transferred via telecommunication channels should include the bank notification of the tax authorities about the opening (closing) of the account, change of the bank account number, information letter of the tax authorities informing the bank about the receipt of its notification about opening (closing) of the bank account and technical documents exchanged by software and equipment. The order sets forth the procedures governing the storage of information in electronic form and the interaction between the party of the information exchange.

4. Letter of the RF Tax Ministry “ON THE PROCEDURE GOVERNING TAX DEDUCTIONS” No. 03-5-09/847/54 of March 29, 2004.

The letter clarifies the procedures governing tax deductions pertaining to the excises on natural gas in 2004. Since starting with payments made in January of 2004 the excise was calculated and paid to the federal budget only as concerns the excisable raw materials extracted prior to January 1, 2004, the tax deductions of the amounts of excise charged on the amounts of advance and (or) other payments received as payments for future deliveries of excisable raw materials in 2004 should be made after they are reflected in the accounting for operations concerning the sale of natural gas (including dry gas) extracted prior to the date indicated above. Tax deductions pertaining to excises charged on advance payments made in 2003 for natural gas extracted and delivered in 2004 should not be made. Tax deductions of the amounts of excise charged on advance payments received for future deliveries of natural gas and respective sales operations should be simultaneously reflected in excise declarations for excisable raw materials (natural gas) for the same tax period.

5. Letter of the RF Tax Ministry “ON REGISTRATION OF SUBJECTS OF THE TAX ON GAMBLING BY TAX AUTHORITIES” No. 22-0-10/425@ of March 15, 2004.

The letter explains that in the case the organization is engaged in the gambling business outside its premises by equipping stationary premises for a term exceeding one month, such actions should be defined as creation of a separate unit and therefore the organization must obtain tax registration with the tax authorities of the jurisdiction, where such separate unit is located. The payment of the gambling tax should be made at the location of the separate unit. At the same time, slot machines located outside the organization premises (locations of separate units) should be registered with the tax authorities of the jurisdiction where the organization is located.

I. V. Tolmacheva