



RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES

06'2011

MONTHLY BULLETIN:

RUSSIAN ECONOMY IN JUNE: TENTATIVE DATA AND BASIC TRENDS	2
POLITICAL AND ECONOMIC RESULTS OF JUNE 2011 (S.Zhavoronkov)	5
INFLATION AND MONETARY POLICY (N.Luksha)	10
FINANCIAL MARKET (N.Burkova, E.Hudko)	13
REAL ECONOMY SECTOR: TRENDS AND FACTORS (O.Izryadnova)	19
RUSSIAN INDUSTRY IN MAY 2011 (S.Tsukhlo)	24
INVESTMENTS IN REAL ECONOMY SECTOR (O.Izryadnova)	29
FOREIGN INVESTMENTS (E.Ilukhia)	35
FOREIGN TRADE (N.Volovik, K.Kharina)	40
STATE BUDGET (E.Fomina)	43
THE REAL-ESTATE MARKET OF THE RUSSIAN FEDERATION (G.Zadonsky)	48
REVIEW OF THE ECONOMIC LEGISLATION (I.Tolmacheva)	53
AN OVERVIEW OF THE RUSSIAN FEDERATION GOVERNMENT'S MEETINGS IN JUNE 2011 (M.Goldin)	55
AN OVERVIEW OF THE NORMATIVE DOCUMENTS ON TAXATION ISSUES ADOPTED IN MAY-JUNE 2011 (L.Anisimova)	57
CHANGES IN THE NORMATIVE BASE OF BUDGETING (M.Goldin)	62

RUSSIAN ECONOMY IN JUNE: TENTATIVE DATA AND BASIC TRENDS

Social and political background: reelection campaign

The budget message from the President, announced in June, despite a number of significant proposals, was obviously too late: this year it was again presented only in summer, rather than in March, as provided by law. Moreover, the message gives no clear guidance on the budget of the next year, but rather presents proposals for the medium term. However, it seems to be the next President, who is to decide whether to follow those proposals. The lack of influence of presidential initiatives was observed in the ongoing controversy between the president and the government in regard to reduction of insurance premiums.

Pre-election, or rather, re-election reconnaissance was observed on the party field. On the one hand, entire businesses and industries in accordance with Soviet tradition and contrary to the spirit of the law and the Constitution were joining Putin's Popular Front, on the other hand, and on the other hand, registration was rejected under false pretenses for "People's Freedom Party" of Mikhail Kasyanov, Vladimir Milov, B. Nemtsov and V. Ryzhkov (earlier refusal was received by the "Other Russia" of E. Limonov, "Rot Front" of S. Udaltsova, etc.).

Re-approval of the Prosecutor General Yuri Chaika in his position can be considered a significant event of June. It happened shortly after the scandal with the investigation of the case "backing of gambling business" in Moscow Region, in which subordinates of the Prosecutor General were involved and the name of his son was mentioned. Reassigning of Y. Chaika indicates that prior to the elections the key "political" authorities will maintain their status quo, formed on the eve of Medvedev's accession to the presidency. However, quite significant rearrangements have been made in the leadership of the Ministry of Internal Affairs: Deputy Ministers M. Sukhodolsky, E. Shkolov and A. Anichin have lost their positions. The latter, as we know, is involved in the "Cardin's list" – a list of persons involved in the death of Mr. Magnitsky, the lawyer, who revealed the scheme of the funds theft from the budget by officials of tax service and investigation department of the Ministry of Internal Affairs.

An important trend in the first half of 2011, which was continued in June, was an expressed deterioration in public opinion ratings of the country leadership, the government and the general situation. So, in answer to the question whether the country is moving in the right direction or events lead us to a dead end (put by "Levada-Center"), the balance in June fell down again to virtually zero (+1), to the level of the crisis peak in February 2009, while in the early summer of 2010 the balance stood at 20 points. The negative dynamics of this indicator in June is still more indicative, as it took place at the background of slowing inflation, traditionally making a significant adverse effect on the population. Estimates of Dmitry Medvedev, Vladimir Putin and the government actions in general lost as compared with June 2010 about 10 points, as compared with January–February – 3.4 points. The number of those ready to vote for the "United Russia" in June declined by 9 p.p. as compared with February 2010 ("Levada-Center" data). Fund "Public Opinion" surveys give a similar picture.

Macroeconomics and finance: cloudless and hopeless

The volatility of global financial and commodity markets in June was based on the events around Greece, as well as the decision of the International Energy Agency to supply oil from strategic reserves. However, due to the volatile dynamics in the US dollar and Euro rates, the value of the two-currency basket fluctuated in a narrow corridor of Rb33.38–33.67 and at the end of the month practically did not differ from the values of the late May. Oil quotations, which at first lost more than 10%, at the end of the month have quickly restored. The latter circumstance has supported confidence of the Russian stock market and as a result, the MICEX index in the last week of the month showed an increase from the level of 1608 points to 1666 points.

Extremely high oil prices ensured the record export revenues in April–June. The trade surplus remains very high (19.5 billion dollars in April), even despite the record growth of imports. In April 2011 the annual growth of imports was 45.1% (48.2% as per results of January–April), while in May, according to operative data of customs statistics (by non–CIS countries), the increase in imports against May of the last year almost came again to the indicator of 50% (49.1%). As a result, the rates of exports and imports came very close to pre–crisis peaks of 2008. Another consequence of record peak in oil prices was the actual federal budget surplus over January – April (+1% of GDP) and expanded government budget surplus, which amounted to 7% of GDP.

Inflation in Russia has declined in June to a minimum: the CPI made 0.2% (versus 0.4% in June of 2010). This was contributed by the stabilization and reduction of food prices in the global markets, seasonal depreciation of fruit and vegetable products, and finally, the relative stabilization of gasoline prices in the domestic market. However, rising costs of fuel and passenger transport services had the greatest impact on the overall price index. As a result, annual inflation fell down below the 9.5% rate since the beginning of the year and reached 5% (4.4% in June 2010). Reduction of monetary base in the first half of the year (on June 1 the monetary base in broad terms was Rb7,268.8 bn, i.e., –11.25% vs the beginning of the year) and a tightening of monetary policy by the Bank of Russia allow to expect a moderate inflation in the second half of the year.

In addition, tighter monetary policy led to a reduction in excessive reserves of commercial banks: in May, they declined by 4.9% to Rb1.2693 bn. Reduction of excessive liquidity has led to an increase in interbank rates: in May the interbank interest rate increased to 3.8% (vs 3.3% in April). On May 31, 2011, the Central Bank has raised interest rates for deposit operations by 0.25 percentage points. The narrowing gap between lending and deposit rates is promoting effectiveness of the interest rate policy. According to the Bank of Russia, the decision to raise deposit interest rates is based on the accelerating inflation. However, according to various estimates, the growth of lending to the industries has slowed down in late spring of 2011.

The main negative news on this nearly cloudless horizon is capital outflow, which is sustained for nine consecutive months. According to the tentative estimates of the Bank of Russia, the outflow has somewhat slowed down, from \$7.8 billion in April to \$5 billion in May. Nevertheless, as per results of five months of 2011, net capital outflow has almost reached the annual rate of 2010 (34.1 billion dollars in 2011 against 35.3 billion dollars in 2010). The Bank's management expects to halt the capital outflow from Russia in the second half of the year, predicting an annual outflow of \$35 billion. However, after the unfortunate first quarter, the Central Bank management was predicting an inflow of capital in the middle of the year and zero outflow as per its results.

Real sector: stop and go

The main trend of the first five months of 2011 was a significant slow–down of industrial production growth in comparison with the relevant period of the last year. Thus, the growth of January – May 2010 as compared with the same month of the previous year was 10.3%, while in January – May 2011, the industry has grown against the same period of the last year by 5.2%. Monthly growth slowed against the previous period approximately twice (excluding seasonal factors). In general, we can say that having demonstrated a strong upsurge from the bottom in early 2010, the industry slows down as it approaches the pre–crisis indicators.

Negative impact on the pace of the industry recovery and on the expectations of market participants had a slower growth of demand and stagnation in investment activity. Investment in fixed assets decreased in the first quarter (–0.8% compared to the last year indicator) and showed a rapid growth only in May (by 7.4% compared to May 2010), which resulted in a positive growth over five months (+2%). Significant role in reducing investment activity at the beginning of the year played a sharp decline in investment in fixed assets in the segment of small businesses. In terms of sources of investment, in early 2011 a decline continued in the share of investments through bank credits, as well as in the share of foreign investments, but the share of investment from regional budgets has been increased.

It should be noted that the structure of foreign investments in the Russian economy continues to deteriorate. If in the pre–crisis years the share of direct investment amounted to about 25% of total investments, in 2009 FDI amounted to 19.4%, in 2010 – 12.1%, and in the first quarter of 2011 – 8.8% of the total investment volume.

While in general the retail trade turnover shows a strong growth (by 5.2% in January–May, as compared with the same month in 2010), a negative trend that could affect the recovery rate of the domestic market remains the decrease in real incomes. Overall, in the January–May, the real incomes fell down by 3.7%, in May real disposable income was 93% of the 2010 indicator and as compared to April of this year, it decreased by 10.4%. Under these conditions, the growth of the retail market is supported by the reduction in the share of income savings (in the situation of negative interest rates on bank deposits), as well as credits growth. However, consumer expectations of the Russians (according to the Russian Statistical Service) showed a definitely negative trend in the first quarter.

Gaidar Institute business surveys also demonstrate contradictory trends in the industry. In May, a reduced demand for industrial products was recorded in all indicators. The data cleared from seasonal factors shows a decline by 8 points. As a result, the rate of sales growth from December 2010 lost 16 points. However, in the coming months, the companies look forward to overcome this negative trend. Growth rate of output continues to decline (although it is still positive). Clearance of seasonal factors showed the sustainability of April growth rate in May, which is the minimal rate for the last fourteen months.

In recent months the growth rate of prices of enterprises (according to their estimates) were declining, but this trend is gradually coming to zero. In May, enterprises revised their business policy in pricing: Russian manufacturers for the first time in 2011 expressed the desire to raise prices, or at least stop their decline. In May another trend of previous months has stopped, i.e., recruitment. After the March record growth rate of employment, over two months it lost 15 points and became zero, which means hiring is stopped, but dismissals in the industry is not started yet.

In general, the uncertain recovery of the Russian economy reflects inconsistency of the main factors: macro-economic well-being, based on external markets, on the one hand, and weak business and investment activity, provoked by the lack of confidence of market participants in the fundamental prospects of the Russian economy, on the other hand. ●

POLITICAL AND ECONOMIC RESULTS OF JUNE 2011

S.Zhavoronkov

*In June, the Government of the Russian Federation still failed to fulfill formal instructions of the President of the Russian Federation as regards making proposals on reduction of insurance contributions starting from 2012. In reality, the Government of the Russian Federation delays solution of that issue as it considers it to be an inappropriate one, while President D. Medvedev is not in a position to exert serious influence on the Government. As a result, in the regular Presidential Budget Message, the following option was proposed: insurance contributions should be reduced from 34% to 30%, while those for small enterprises and enterprises which use a simplified taxation system, to 20%. **June happened to be rich for personnel-related decisions:** Procurator General Y. Chaika and V. Yakunin, Head of OAO RZhD **kept their offices**, however, **V. Matvienko, Governor of St. Petersburg whose low rating was found unacceptable in the light of the forthcoming election campaign lost her office** (V. Matvienko is going to take a ceremonial office of the Speaker of the Council of Federation). Also, large-scale personnel changes took place in the Interior Ministry, but the resignation of three influential deputy ministers strengthened, on the contrary, the position of R. Nurgaliev, the Interior Minister. **After all the new parties have been refused registration, it has become apparent that only a set of the existing parties will be allowed to participate in the elections.***

In June 2011, the President of Russia made a number of political statements of which the most concrete one made at the St. Petersburg Economic Forum was an intention “not to exclude” the fact that the borders of Moscow might be expanded and a special “capital district” established. A bit later, A. Dvorkovich, Presidential Aide explained that it was meant to relocate a number of government agencies and, probably, commercial infrastructure facilities beyond MKAD (the Moscow Ring Motorway). S. Sabyanin, Mayor of Moscow and A. Gromov, Governor of the Moscow Region reacted to that proposal by setting up a commission which would study that issue with deliberation. It is believed that until March 2012 implementation of the above proposal is virtually impossible, while after March 2012 it will be decided in a new configuration. Anyway, it is highly unlikely that a new entity of the Federation will be established. Most probably, it may be such a specific decision similar to the transfer of the Constitution Court of the Russian Federation to St. Petersburg as would affect only a small number of government agencies. President Medvedev’s other statements which lacked any concrete message as well as his good wishes which have been numerous repeated in the past three years are not worth analyzing.

However, one undoubtedly useful initiative is worth mentioning. President D. Medvedev introduced to the State Duma of the Russian Federation such amendments to the Criminal Code as abolish the Criminal Code’s articles “offence” and “slander” and transfer them to the category of administrative violations. Though no particular abuse of the above articles was observed in enforcement practices in Moscow, initiation of criminal cases against journalists and public activists who criticized governors and other local authorities were wide-spread in Russian regions.¹ The existing practice of introduction of draft laws by the President or the Government of the Russian Federation suggests that they will be approved.

Quite the opposite situation took place with the debates on the tax reform. The announced draft law is still far away from being introduced. Despite the fact that in June 2011 President Medvedev announced the regular Budget Message, the issue of reduction of insurance contributions starting from 2012 (which reduction was promised by President Medvedev as early as this March) remains unclear. As a result, in his Budget Message he referred to the following option: insurance

¹ A typical example is the existing case against S. Mikhailov, journalist and deputy of the Parliament of the Republic of Altai who was accused of “slandering” A. Berdnikov, Head of the Republic in connection with an article in which S. Mikhailov wrote that A. Berdnikov abused alcohol.

contributions will be reduced generally from 34% to 30%, while those for small enterprises and enterprises which use a simplified taxation system, to 20%. However, it is proposed to exclude commercial enterprises (which account for a large portion of small enterprises) from the number of small enterprises. The government has still failed to work out its own proposals. In June, at a meeting in Rostov Premier V. Putin said: “...So far, I have no idea where to get the funds from to solve a number of issues, including subsidizing of the interest rate on loans to agricultural producers, the housing issue and other...The drop-out revenues amount to hundreds of billions rubles”. Officially, the deadline for implementation of President D. Medvedev’s instructions expired as early as June 1, however, Premier V. Putin who is actually in charge of the country may not worry much about it. After the Budget Message was announced, A. Kudrin, Vice-Premier and Minister of Finance of the Russian Federation evaluated the drop-out revenues to be in the amount of Rb400 bn, that is, he raised by 100% his previous forecasts. Actually, for political reasons the Government of the Russian Federation is unwilling to apply most measures which were considered to be used for compensation of the revenues, that is, raising of excise taxes (apart from unwillingness to make people angry by raising prices on alcohol and tobacco in the year of the election of the President of the Russian Federation, government experts point to the fact that the respective sectors may cease paying excises at all by turning their business into a shadow one, and in such a case budget revenues may even drop), carrying out of a large-scale privatization (it means diminishing of the influence and decrease in the amount of capital of top executives of large state-owned companies, which top executives are in most cases close friends of Premier V. Putin and have successfully resisted even a sale of the minority interest), cutting of expenses on R&D in the military and technical sphere (classified expenses are an ideal opportunity for administrative allotment), increasing of the profit tax (there are also concerns that it may reach the limits of the rate at which the profit tax may be actually collected), increasing of the income tax (in order not to make the middle class and wealthy people angry before the elections) and other.

Those measures which have been agreed upon to some extent -- like some increase in the tax burden on Gasprom – do not solve the problem completely. It seems the government will keep varying the terminology of the specially protected business – in the course of this year such terms as “small”, “social” and “industrial” business have been used – in order to minimize the number of enterprises which comply with those terms. It is highly probable that the government will delay approval of the respective draft laws in such a way that they come into effect after the elections in March 2012 when President D. Medvedev who gives the present advice on reduction of rates of insurance contributions leaves his office. If for some reasons it will be decided to execute legislatively those initiatives on reduction of contributions starting from January 2012 it is highly likely that such a law does not last long. Experts are unanimous that the final selection of the budgetary and fiscal policy will take place after the presidential elections in 2012.

In June 2011, V. Matvienko, the Head of St. Petersburg resigned, though her resignation was postponed for two months. At the meeting with heads of a number of constituent entities of the Federation, President D. Medvedev unexpectedly supported an “incidental” proposal by R. Hamitov, Head of Bashkiria to make V. Matvienko the Head of the Council of Federation (the office of the Head of the Senate is vacant since may after resignation of S. Mironov). V. Matvienko was not present at the meeting and she did not give a prompt answer. Five days later, having checked through her own channels that it was not only President Medvedev’s own opinion V. Matvienko accepted it and pointed out in particular that she “*met with Vladimir Putin who supported that decision and Boris Gruzlov. I am a team player and on the basis of the results of my consultations with other members of the team I made a positive decision in favor of that scenario*”. Under the law, at present for election to the Council of Federation one is required to be a deputy of a regional or municipal level. The most simple way to secure such a mandate for V. Matvienko would be a situation where most deputies of a St. Petersburg’s district divest themselves of authority and declare early elections. In such a case, V. Matvienko could become a municipal deputy in September and then be delegated to the Council of Federation. However, it is to be understood that as compared to the office of the Head of St. Petersburg V. Matvienko’s election as the Head of the Council of Federation is an explicit downgrading though, formally, it is a promotion. The Council of Federation has no authority or financial levers, nor has it an opportunity which deputies of the

State Duma may rarely have to introduce amendments into documents proposed by the President and the Government. The Council of Federation is kind of an elite club with parliamentary privilege and nothing more.

The reason behind V. Matvienko's resignation as well as that behind Yu. Luzhkov's one which took place less than a year ago is their low rating which had an adverse effect on the United Russia Party. It is to be noted that unlike Yu. Luzhkov who was earlier popular and appeared as an 'engine' V. Matvienko has never been popular in St. Petersburg – in 2003 at the election of the Governor of St. Petersburg she won the election only in the second round and in situation where she had no serious competitors, while at the elections in December 2007 the United Russia Party in St. Petersburg took the second lowest place among Russian regions leaving behind only the small Nenetsk Autonomous Region where a chaotic situation in the local government was observed. There is virtually the same set of complaints to V. Matvienko as it was to Yu. Luzhkov: barbaric commercial development, inefficient housing and public utilities, corrupt practices and clanism (V. Matvienko's son Sergei who was virtually unknown person before her election turned out to be one of the most prominent businessmen of St. Petersburg), high real-estate prices and expensiveness of urban living for low-income people (though the above factor was to a great extent an objective one it was nonetheless attributed by the discontented to the Governor). V. Matvienko maneuvered more successfully than Yu. Luzhkov among large business-structures, but it was not enough in the election year. It seems that the new Governor of St. Petersburg and the leader of the local list of the United Russia Party will become a federal leader of the United Russia Party with St. Petersburg roots.

In June, V. Yakunin, present Head of RZhD was reappointed to his office. There were many rumors about his resignation due to the fact that it was planned to carry out in the next few years privatization of large rail carriers – RZhD subsidiaries as well as a minority package of RZhD itself – and many questions arose with other contenders to that office as regards connection of the present management of RZhD with two prominent businessmen: I. Makhmudov and S. Generalov. Also, there were rumors that I. Levitin, powerful Minister of Transport who was supported by the famous St. Petersburg-based Rotenberg family had claims to that office. In addition to the above, the RZhD financial indices are far from those of the market leaders, while the conflicts with other government agencies as regards the limits to which the tariffs may be increased took place almost every year. However, V. Yakunin -- Premier V. Putin's main associate from the days of his work in St. Petersburg -- managed to keep his office.

Significant changes took place in the structure of the Interior Ministry. M. Sukhodolsky, First Deputy Interior Minister was appointed the Head of St. Petersburg GUVB instead of V. Piotrovsky who failed re-evaluation. V. Piotrovsky was in charge of the police of St. Petersburg for almost ten years. Such a transfer cannot be regarded as a serious downgrading as it is prestigious to be in charge of the police of St. Petersburg – one of the two business capitals of Russia – however, it is a downgrading as M. Sukhodolsky was considered for a long period of time as a likely successor of Interior Minister R. Nurgaliev. Also, E. Shkolov, Deputy Interior Minister and A. Anichin, Deputy Interior Minister and Head of the Investigation Committee at the Interior Ministry were dismissed. The former was considered for a long period of time to be close to President D. Medvedev whom he had worked with, but it seems his position was undermined by conceptual disagreement with the new Law on Police which he made numerous proposals to. Anichin -- who was Premier V. Putin's fellow-student – was vulnerable from the other point of view. Anichin's direct subordinates were the organizers of the notorious Heritage and Magnitsky case in the course of which over Rb 6bn were embezzled from the budget while Magnitsky who informed of the embezzlement died in prison. The European Parliament and the US Congress are discussing the prospect of introduction of sanctions against Anichin and his subordinates who for a long period of time used to receive rewards and promotions. Apart from diplomatic reasons, the above resignations could be kind of an "even score" in the framework of the balance of forces of different groups inside the Russian authorities. Generally, after the above resignations the position of R. Nurgaliev, the Interior Minister has strengthened – at least two resignees (Sukhodolsky and Shkolov) were considered as R. Nurgaliev's potential successors, while another Deputy Minister S. Bulavin who was not a member of the old team and supervised, in particular, the Law on

Police has worked at the Interior Ministry for less than a year¹ and probably still lacks the weight required for in that conservative structure.

In June, the President of the Russian Federation put forward in the Council of Federation the candidature of Prosecutor General Yu. Chaika for reappointment due to expiry of his term of office. The candidature of Yu. Chaika was approved by a majority vote. Yu. Chaika's fate was not affected by a notorious scandal related to the exposure of a large criminal group operating in the Moscow Region Prosecutor's Office. The above criminal group with senior officers of the Prosecutor's Office in charge of it used to extort money and protect illegal gambling business. Some senior officers were dismissed, while others were either arrested or declared in search². The above scandal is still going on as the Investigation Committee which is competing with the Prosecutor General's Office has been initiating cases against some or other persons within the frameworks of "the prosecutors" case, while the Prosecutor General's Office as a supervisory authority has overturned them. Earlier, it seemed that the public conflict went far beyond the limits of decency adopted in the circles of power, and many experts predicted an "even score", that is, simultaneous resignation of senior officers of both the Investigation Committee and the Prosecutor General's Office. However, it has turned out that that balance of forces suits the Russian authorities well.

In June 2011, the configuration of the parties which were allowed to participate in the parliamentary elections has finally become clear. The last of the five new parties -- the liberal opposition Party of People's Freedom led by M. Kasyanov, V. Milov, B. Nemtsov and V. Ryzhkov -- was denied registration of documents by the Ministry of Justice. Earlier, registration was denied to the left-wing opposition parties -- the Other Russia Party led by E. Limonov, the Rot Front Party led by S. Udaltsov and the Motherland -- Common Sense Party led by M. Delyagin -- as well as the Party of the Cause established by prominent businessman K. Babykin which party positioned itself as a centrist party. In reality, it can be stated that despite Russian leaders' statements about general liberalization, modernization and competition it is still impossible to have a political party registered for participation in the elections and Russian citizens are deprived of active voting rights, that is the right to be elected to the Parliament on the list of the party they want to establish. Apart from preventing the opposition from taking part in the elections (the existing set of the registered parties does not criticize V. Putin), such a policy by the authorities also pursues an indirect objective, that is, to reduce, primarily, in cities the voting turnout of those voters who do not want to go to polls because of absence of opposition candidates in voting bulletins and increase in the final results the share of national republics which usually demonstrate 99% turnout and voting for the United Russia party.

In June, the leadership of the Right Cause Party -- the last of the seven registered "system parties" -- was finally formed. As it was declared last month, M. Prokhorov, one of the wealthiest businessman was declared the leader of the party. Former Co-Chairman L. Gozman was removed from the party leadership, while A. Chubais, from the Supervisory Board. It can be stated that that group of liberal politicians from the former SPS party which put forward the idea of cooperation with the authorities in the 2000s was not eventually required. The leadership of the Right Cause party includes few former SPS party members now. As regards the party's personnel, it is a peculiar assembly of people with different political history ranging from the SPS Party to the United Russia Party and Rodina Party. A. Dunaev -- who is considered to be an appointee of V. Surkov, Deputy Chief of the Administration of the President of the Russian Federation -- has remained the Chief of the Party's Executive Committee. Also, it was declared that leaders of all the regional branches would keep their offices until the elections to the State Duma. The party's election campaign will be managed by the headquarters led by M. Prokhorov's long-term associates and PR and GR experts -- V. Kedrinsky and Yu. Slaschevoi -- who, however, lack election campaign experience. The party's congress received extensive TV coverage, while M. Prokhorov was received by President D. Medvedev whom M. Prokhorov told the key points of his program. Those key points represented a largely limited set of the opposition's long-standing demands, that is, a return of

1 Until 2010, Bulavin worked for a long period of time in the Administration of the President of the Russian Federation though he started his career in the Interior Ministry, but never occupied senior positions there.

2 For example, the prosecutor of the Moscow Region was dismissed from office, while his first deputy was declared in search. Also, dozens of regional prosecutors were involved in the scandal.

elections of the Heads of Moscow and St. Petersburg, re-establishment of 25% of single member constituencies, election of low-ranking administrative authority of the judicial system and the police and broadening of powers of the local self government. As usual, President D. Medvedev did not promise anything concrete, but advised “*all the parties to work in order to make the system of management less bureaucratic and more free*”. In our view, the prospect of passing by the Right Cause Party of the threshold barrier remains unclear – unlike its main contenders (the Communist Party of the Russian Federation, the Liberal-Democratic Party and the Just Russia Party) which exist in the federal parliament and most regional parliaments -- the party’s base rating is equal to zero, while the party’s regional structure has failed to produce any noticeable results in the past three years. The anti-rating of the party led by a billionaire does exist by definition. Theoretically, it can be assumed that by carrying out an expensive and successful election campaign, hiring new efficient executives in most regions, distributing dozens of millions of copies of election leaflets and ensuring supervision at least in cities the Right Cause Party might achieve the sought after result. However, the financial resource alone does not guarantee anything. For example, it is worth remembering the campaign of the Ivan Rybkin Block in 1995 and that of the People’s Party or the Civil Force Party in 2003 and 2007, respectively.

The start-up positions of participants in the elections will be determined in September with formation of party lists. It is not that important who takes the top three positions along with the party leader on the party lists, but who will lead the parties’ regional lists as it permits to assess to what extent the regions are prepared for an independent campaign and to what extent they have managed to raise funds from leaders of regional lists. ●

INFLATION AND MONETARY POLICY

N.Luksha

• *The month of May 2011 has seen zero growth rate in **prices of food stuffs** for the first time ever since October 2009. That notwithstanding, consumer **inflation as a whole accelerated, with CPI adding 0.1%** (from 0.4% to 0.5%). The main factor behind the acceleration of inflation became the price rise of fuel. The **inflation rate accumulated between January and May** accounted for **4.8%** vs. 4% in 2010. The decelerating growth rate of the price rise for gasoline and the seasonal cheapening of fruits and vegetables helped **slow down inflation in June**, with **consumer prices adding 0.2%** over nearly three weeks of the month. **The net capital outflow from the country has continued for nine months in a row already.** Preliminary estimates suggest that in May the process somewhat lost its steam – from \$7.8 bn to 5bn. **The Bank of Russia keeps tightening the monetary policy: since 31 May, the CBR raised interest rates on deposit operations by 0.25 p. p.***

By results of May 2011, inflation accounted for 0.5%. If not for the seasonal slowdown of food prices (0%), the inflation rate might have been even greater, for the pace of prices increases for non-food products and paid services was up roughly 1.5 times over the month. The major factors boosting inflation were the fuel crisis, which had started in April 2011, and the ensuing price rise for petrol and rising passenger transportation tariffs.

Zero rate of growth in food prices was fueled at most by the cheapening of a string of food stuffs: a drastic downfall in prices for eggs (-16.1%), declining prices for sugar (-3.9) and fruits and vegetables (-1.5%), while the continuous price rise for millet (+4%) led to some price increases for Gruels and legumes.

The pace of the price rise for non-food stuffs increased from 0.5% to 0.8% in May, with the major driver of the process being, unquestionably, growing gasoline prices (+6%). Prices for tobacco products were likewise on the upswing in May (+1.9%), while it was only prices of TV- and radio sets that were going down (-0.4%).

Meanwhile, the pace of increase in prices of paid services to the population likewise was up from 0.5% in April to 0.7% in May. The price rise for fuel resulted in increased passenger transportation tariffs (+3.1%). In addition, with the start of the period of summer holidays, prices for overseas touristic services were up by +2.6%, while those for sanatorium-and-rehabilitation services added 2.3%.

On a year-on-year basis (vis-a-vis the same period of the prior year), the May inflation rate did not change compared to the April one and accounted for 9.6% (see Fig. 1). In the same period of 2010, the price rise was 6%.

In May 2011, the basic Consumer Price Index ¹ continued to decline and ultimately made up 0.4% (0.1% in the respective period of 2010).

In June, inflation slowed down: CPI over slightly less than three weeks of the month accounted for 0.2% (0.3% over the respective period of 2010). Better still, the price increase over the second week of June has become zero one for the first time since the beginning of the year. Despite the Rospotrebnadzor's ban on import of vegetables from Europe effective since 2 June due to the outbreak of the enteric infection in Europe, prices for fruits and vegetables have been declining in the country. This can be explained by the fact that the share of the respective import from EU to Russia is relatively low in the summertime and accounts for some 5%, as suggested by Minselkhoz data. Deceleration of the pace of increase in consumer prices to yet a greater extent can be ascribed to a considerable lowering of the pace of increase in gasoline prices (+1.1% as of 20 June). It is worth noting that inflation traditionally slows down in Russia due to seasonal cheapening of food stuffs.

¹ Basic Consumer Price Index is an indicator mirroring the inflation level on the consumer market, less the seasonal (prices of fruits and vegetables) and administrative (tariffs for regulated kinds of services, etc.) factors, which is also calculated by Rosstat.

Additional factors taming inflation should become the appreciating Rb and decelerating rates of growth of money supply.

In the first half of 2011, the wide monetary base has been shrinking: on 1 June, it plummeted to Rb7268.8bn. (-11.25%). In May, its contraction accounted for 0.2% and was due to the continuous decline in the volume of credit institutions' deposits with the CBR to a value which became the minimum one since the beginning of the year (1.7 times, down to Rb158.3 bn.), as well as cash in circulation with account of credit organizations' cash balances (by 0.1%, down to Rb5664.1bn.).

Because of the Bank of Russia's tightening its monetary policy, the commercial banks' excessive reserves kept melting down¹: in May alone, they plunged by 4.9%, down to Rb1,269.3bn. The contraction in excessive liquidity resulted in rising interbank rates, with the IBL interest rate increasing to 3.8% in May vs. 3.3. in April.

A 0.2% decline in the volume of cash in circulation and the rise of mandatory reserves 1.2 times in May led to a 0.8% expansion of the monetary base in narrow terms (cash plus compulsory reserves)², up to 5999.5 (see Fig. 2).

In June, foreign reserves continued to grow and hit \$520.3 bn. on 17 June. In the first decade of June, their amount became record-breaking ever since October 2008 and accounted for \$528 bn. However, because of the plunge of the Euro on the global forex market and the ensuing currency re-valuation, the reserves momentarily dropped by \$7.7bn.

Overall, that Russia's foreign reserves were on the upsurge can be ascribed to a favorable state of affairs on external markets and high international oil prices in particular.

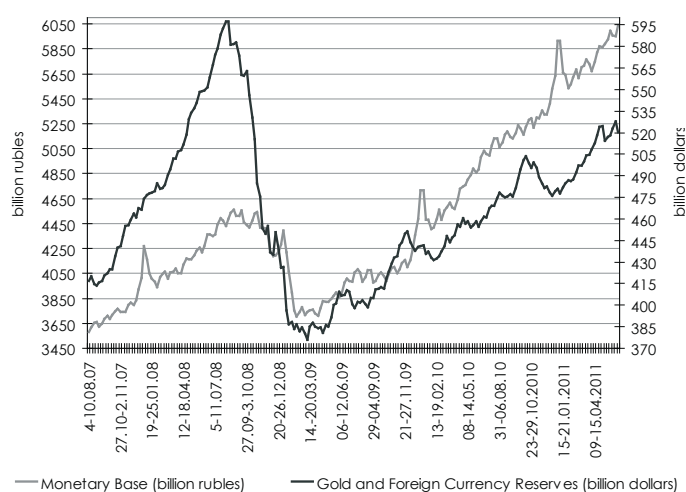
Since early 2011 the Rb monetary exchange rate calculated as the M_2 -to-foreign- reserves ratio has been gradually sliding down from 41.63 to 38.21 Rb/\$. That was taking place against the backdrop of an influx into the country of foreign currency from sales of more and more expensive oil and, as a consequence, of growth in foreign reserves. That said, the monetary rate of Russia's currency still is at nearly 40% lower than the market one. So, should the external state of affairs aggravate and oil prices tumble, there exists a substantial potential for a fall in the national currency's exchange rate.

The net capital outflow from Russia has been noted for nine straight months already. According to the CBR's preliminary estimates, the process somewhat decelerated: while in April the outflow accounted for \$7.8bn., in May it made up 5bn.³ That said, by results of the first five months of 2011,



Source: CBR

Fig. 1. Pace of Increase in CPI in 2009–2011 (as % annualized)



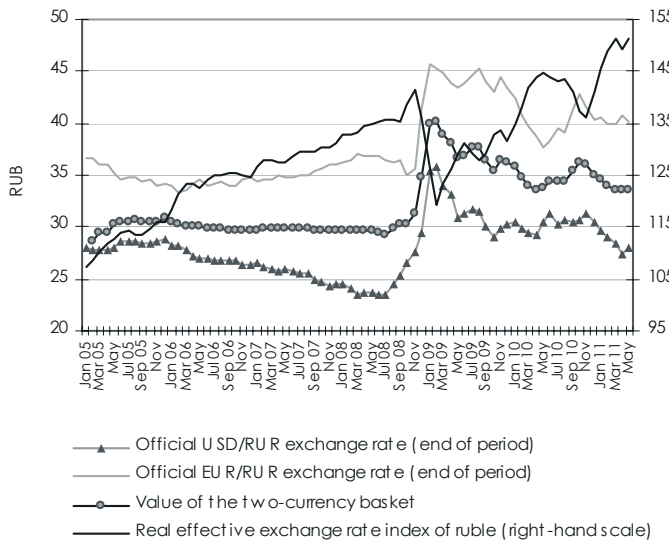
Source: CBR

Fig. 2. Dynamics of Monetary Base (in Narrow Terms) and Foreign Reserves of RF between 2007 and 2011

1 Commercial banks excessive reserves with CBR are understood as the total of the amount of commercial banks' corresponding accounts, their deposits with CBR, and CBR's bonds held by commercial banks.

2 As a reminder, wide monetary base does not constitute a money aggregate. Rather, it characterizes the Bank of Russia's denominated in the national currency liabilities. Meanwhile, monetary base in narrow terms does constitute a money aggregate (one of characteristics of the volume of money supply) and as such is fully controlled by the CBR.

3 RBK news (<http://top.rbc.ru/economics/06/06/2011/599085.shtml>), 06.06.2011.



Source: CBR, the author's calculations.

Fig. 3. Indicators of the Rb Exchange Rate between January 2005 and May 2011

to € and \$ was tumbling. In the course of the subsequent decade Rb has been appreciating against € on negative news from the Eurozone (S&P awarding a pre-default rating to Greece, a looming debt crisis in Slovenia, Moody's lowering its forecasts on the biggest French banks' ratings). Rb once again began depreciating against € after 17 June, once € picked the leading wind on the global forex market after European governments had agreed on the financial aid package for Greece. Such multidirectional fluctuations notwithstanding, the Rb/€ exchange rate has not practically changed over the first 25 days of the month and accounted for Rb40.12/ € (-0.1%).

Meanwhile, the June behavior of the other pair of currencies – that is, Rb and \$, was a reflection in the mirror to the Rb/€'s dynamic. In addition to the latter, the Rb exchange rate still found itself affected by oil prices, and over the 25 days of June Rb plunged by 0.4% vs. \$. As a result, the June value of the bicurrency basket was on the upsurge (+0.2%) and hit Rb33.55: as of 25 June.

On 30 May, the Bank of Russia ruled to leave unchanged the refinancing rate and interest rates on operations on provision of the CBR's liquidity. Meanwhile, since 31 May the CBR raised interest rates on deposit transactions by 0.25 p.p. So, the CBR kept tightening the monetary policy.

The banking sector currently enjoys a sizeable volume of excessive liquidity, which backs the growing role of deposit rates. Narrowing the gap between credit rates and deposit ones boosts efficacy of the current interest-rate policy.

While ruling to raise deposit rates, the CBR cited accelerating inflation as the reason behind its move. As noted above, inflationary expectations remain high, despite some slowdown of inflation in June. We believe that the task of keeping inflation in check may require further moves to tighten the monetary policy. As economic growth is losing steam, the regulator, however, is not going to revise the current state of interest rates in the close future. ●

the volume of net capital outflow practically matched the 2010 total (\$34.1bn in 2011 vs. 35.3bn. in 2010). While behind the April capital outflow were increases in banks' foreign assets, Sberbank's in particular (by \$5bn), it was companies that were taking capital away from Russia in May. The main cause for the capital outflow remained an unfavorable investment climate in the country and huge political risks in the pre-election year.

The real effective exchange rate resumed its growth in May, ultimately adding 1.3% by results of the month. Accordingly, the index of the real effective rate made up 151.28¹ (see. Fig. 3²).

Official exchange rate of \$ as of the end of the period Official exchange rate of Euro as of the end of the period. In June, the Rb exchange rate to € and \$ remained volatile. In the first week of the month, nominal Rb exchange rate

1 With the level registered in January 2002 accounting for 100

2 With the level registered in January 2002 accounting for 100

FINANCIAL MARKET

N.Burkova, E.Hudko

The public debt market was growing moderately in June. By contrast, the stock market exhibited a fall in turnover against the backdrop of main stock indices and Russian blue chips being on the upsurge. The volume and indices of the market for corporate bonds renewed their historic peaks, with the proportion of long-term borrowings being on the upswing in this particular segment. The situation with issuers meeting their current obligations to bondholders aggravated.

The Market for Government Papers

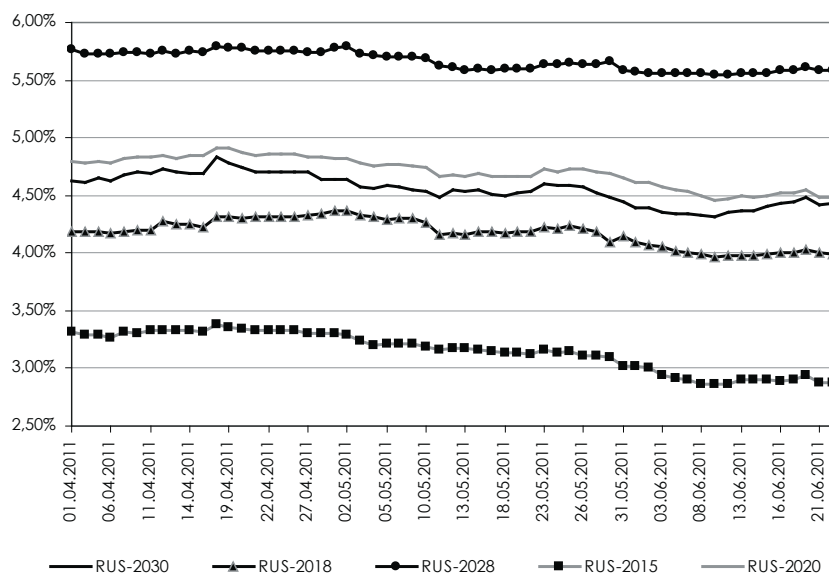
The yields rates of Russian public forex-denominated bonds were in decline in June. The increasingly gloomy prospects facing the Greek debt cast shadow on the Russian market for government bonds between late May and the first decade of June. Meanwhile, the sector for public debt saw existence of demand for Rb-denominated assets, as in June the Minfin revised its plans about borrowing towards its greater volumes and longer duration. Plus, the Bank of Russia retained the refinancing rate at the level of 8.25%, which also solidified stability of this particular segment of the debt market.

Between 9 and 21 June, the market for Rb- and forex-denominated public papers was pretty idle and saw an insignificant increase in yields rates triggered by the start of the tax period and the gloomy prospects for Greece's debt.

On 22 June, the Fed reported a temporary slowdown of the US economic recovery and signaled \$600bn bond-buying program to end by the end of June 2011. Besides, Rosstat reported that Russia's economy advanced by 3.8% on a year-on-year basis in May 2011, with the nation's foreign trade surplus being up by 32.4% (up to \$16.5bn.) and inflation adding 4.9% between the beginning of the year and 20 June. On that very day, the public segment of the Russian market for domestic debt displayed a side trend against huge turnover.

As of 22 June, maturity to date of Russian Eurobonds tumbled vs. 22 May, with RUS-15 posting the greatest fall (by 7.91%) (Fig. 1). Between 23 May and 22 June 2011 the aggregate turnover of the secondary market for OFZ accounted for Rb 197.11bn, with the average daily turnover being at the level of Rb 8.96bn., equivalent of a 4.2% growth in the daily average for a month.

Between 23 May and 22 June 2011, as many as 10 auctions on placement of OFZ on the primary market were held (vs. 4 auctions run the month before) (see Table. 1). The total actual volume of placement made up 69.93% of the planned one. No auctions were held on an additional placement of OFZ issues on the secondary market.



Source: by Finmarket data

Fig. 1. Redemption Yields of Russian Eurobonds with Maturity to Date in 2010, 2015, 2018, 2020, 2028 and 2030 between April and June 2011

Table 1

PLACEMENTS ON THE PRIMARY MARKET FOR OFZ

Date of the auction	Issue	Volume of the issue, as Rbm	The face-value volume of placement, as Rbm.	Average-weighted yield
25.05.2011	OFZ-25076-PD	20 000.00	2 152.91	6.60
25.05.2011	OFZ-25077-PD	20 000.00	18 174.37	7.55
01.06.2011	OFZ-25079-PD	10 000.00	9 993.59	7.25
01.06.2011	OFZ-26205-PD	20 000.00	15 539.46	8.18
08.06.2011	OFZ-25079-PD	20 000.00	19 491.75	7.18
08.06.2011	OFZ-26206-PD	20 000.00	11 735.56	7.75
15.06.2011	OFZ-26205-PD	10 000.00	4 042.50	8.20
15.06.2011	OFZ-26206-PD	20 000.00	8 930.11	7.80
22.06.2011	OFZ-25079-PD	10 000.00	9 089.34	7.13
22.06.2011	OFZ-26204-PD	20 000.00	19 729.32	7.99
Итого:		170 000,00	118 878.90	

Source: Minfin.

Stock market

External Factors behind the Dynamic of the Russian Stock Market

As a month ago, price fluctuations for oil, the US economic recovery running out of steam, uncertainties around the Eurozone nations climbing out of the debt crisis, Japan's economy in shambles, and China tightening its monetary policy likewise discouraged demand for risky assets around the globe. Meanwhile, the Bank of England and the European Central Bank holding their key rates unchanged in tandem with anticipation of a possible additional financial aid to Greece helped keep the Russian stock market's robustness.

By contrast, most developed nations' markets sank by 3–6% over the month, while those in emerging countries plunged by 2–7% (see *Table 2 and Fig. 2*), with China's Shanghai Composite suffering the strongest blow (-7,32%).

Table 2

DYNAMICS OF GLOBAL FINANCIAL INDICES (AS OF 22 JUNE 2011)

Index	Value	Change over the month (%)*	Change since the start of the year (%)
MICEX (Russia)	1 640.13	2.25	-2.84
RTS (Russia)	1 878.38	2.91	6.11
Dow Jones Industrial Average (USA)	12 109.67	-3.22	4.60
NASDAQ Composite (USA)	2 669.19	-4.78	0.62
S&P 500 (USA)	1 287.14	-3.46	2.35
FTSE 100 (UK)	5 772.99	-2.95	-2.15
DAX-30 (Germany)	7 278.19	0.16	5.26
CAC-40 (France)	3 871.37	-2.99	1.75
Swiss Market (Switzerland)	6 113.44	-6.39	-5.01
Nikkei-225 (Japan)	9 629.43	0.23	-5.86
Bovespa (Brasil)	61 194.09	-2.24	-11.70
IPC (Mexico)	35 399.44	0.29	-8.17
IPSA (Chile)	4 711.09	-2.24	-4.39
Straits Times (Singapore)	3 042.83	-3.97	-4.61
Seoul Composite (South Korea)	2 063.90	-2.25	0.63
ISE National-100 (Turkey)	61 217.96	-3.29	-7.25
BSE 30 (India)	17 550.63	-4.23	-14.43
Shanghai Composite (China)	2 649.32	-7.32	-5.65
Morgan Stanley Emerging&Frontier Markets Index	882.04	-2.13	-3.26

* – vis-a-vis the indices' values as of 22 May 2011

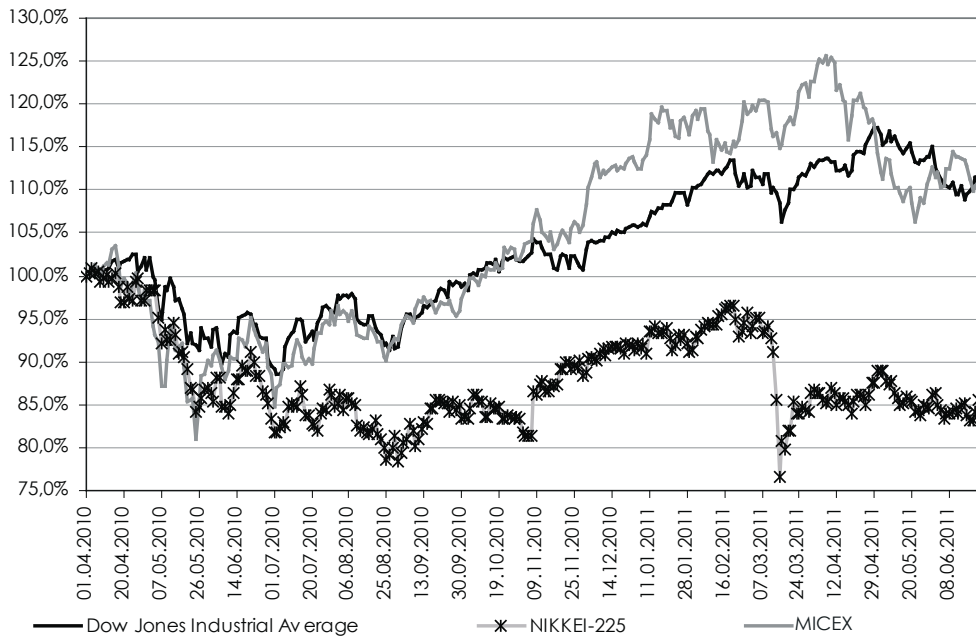
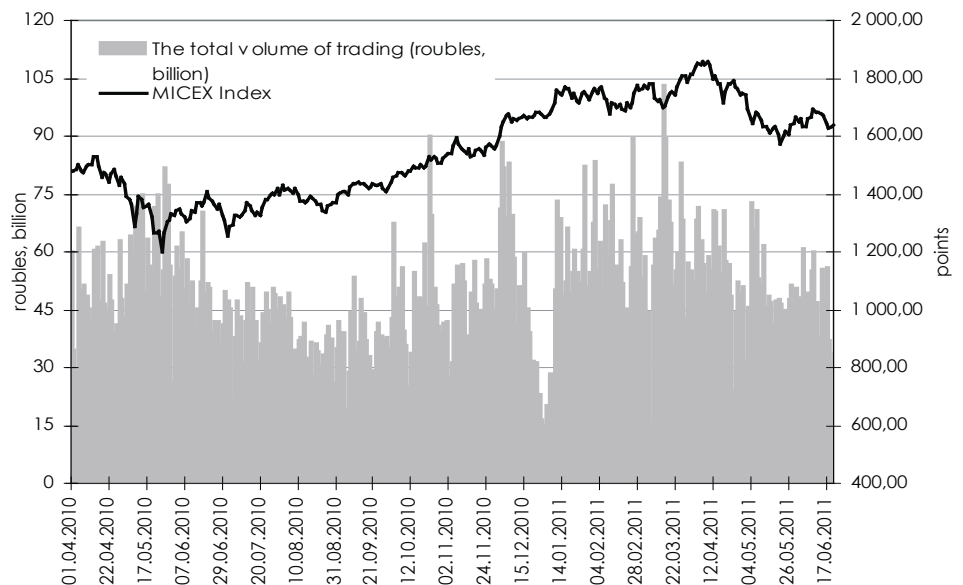


Fig. 2. Dynamics of Major US, Japanese and Russian Stock Indices (as % to Their Values as of 1 April 2010)

State of Affairs on the Stock Market

In June, the national stock market saw its state of affairs improve. Despite the debt crisis in Greece, the downgrade of Italy’s credit and Japan’s sovereign ratings, main Russian stock indices have been soaring between late May and early June, with volumes of trading remaining relatively stable. As to factors fueling the market’s surge, it is worth noting the G8 statement on acceleration of the pace of recovery of the global economy’s, good statistics from Germany, the Bank of England and the European Central Bank leaving their basic rates unchanged, and Goldman Sachs raising its forecast of Brent prices thru end-2011 up to \$120/b, and OECD raising its forecast of growth of Russia’s 2011 GDP from 4.2% up to 4.9%. That said, negative macroeconomic and employment statistics in the US published in the evening of 1 June and a possible downgrading of the US’s credit rating triggered a temporary (from 2 through 6 June) drop of the stock market. In mid-June (between 10 and 20 June), Russia’s

main stock indicators were down on Standard & Poor’s downgrading Greece’s sovereign credit rating to the lowest possible level (CCC) and negative statistics in China. But soaring oil prices and US indices and the EU’s move to beef up the lending capacity of the European Financial Stability Fund combined spurred on growth of the MICEX index on 21-22 June. In parallel with that, the uncertainty about the oil price levels and the pace of recovery of the global economy affected stock trading, nonetheless.



Source: MICEX

Fig. 3. Dynamic of the MICEX Index and Volume of Trading

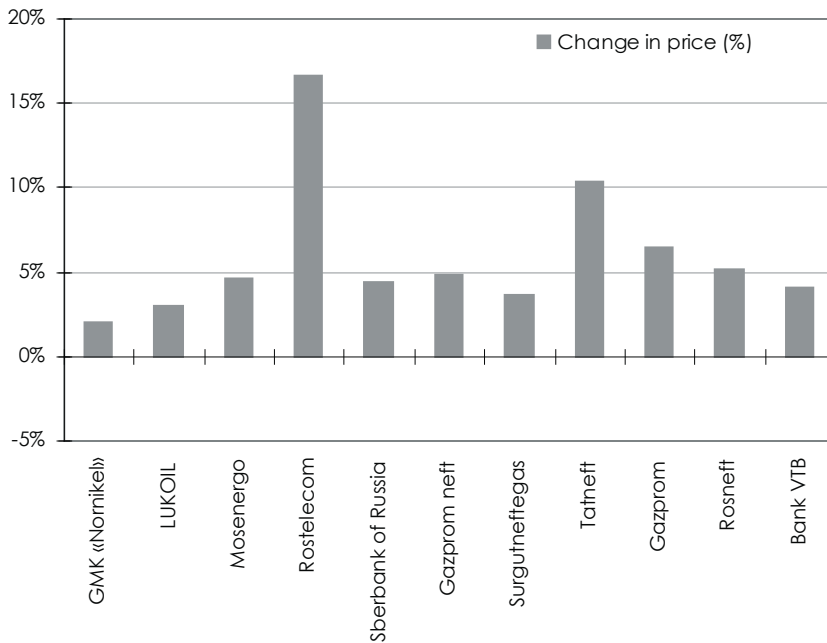


Fig. 4. Increase Rate in Quotations of Russian Blue Chips between 23 May and 22 June 2011

stock that were atop the list of blue chips price-wise: they added 16.68 and 10.39%, respectively (Fig. 4). According to MICEX data, as of 22 June, the TOP-5 Russian corporations by capitalization were: Gasprom – Rb4,753.4bn, Rosneft – 2,477.96bn, Sberbank of Russia – 2,064.36bn, LUKOIL – 1,484.49bn., and GMK Nornickel – 1,321.24bn.

The Spot Market

In June 2011 (between 23 May and 22 June), the average daily volume of trading on the MICEX spot market dwindled 40% compared to the prior month. As in May 2011, the biggest volume of trading in June fell likewise on futures on stock assets - Rb32.93bn (78,000 transactions). That said, trading volume-wise, in this section of the MICEX spot market settlement futures on the MICEX index are followed by supply futures on Gasprom, LUKOIL, Nornickel and Sberbank stock. It should be noted that the value of the MICEX index (the price of concluded deals) on September 2011 found itself on average within the range between 1,600–1,700 points, ie. most market participants anticipate the index to rise 0–3.65% against its value as of 22 May 2011.

Transactions with currency futures came in second in June (Rb7.86bn), followed by futures on interest-bearing instruments (Rb.4.3bn). Settlement futures on \$ are second to none in this section of the MICEX spot market, followed by futures on € against \$ and € exchange rate. Prices of futures on Rb/\$ concluded on the MICEX spot market in June with the date of execution in September 2011 were on average within the range 28–28.8 Rb/\$., ie. the market anticipates a 0–2.8% depreciation of Rb compared to the respective index as of 22 May 2011 (28.01 Rb/\$).

On RTS FORTS spot market, the investors' average daily activity dropped by 5.5% vs. the prior month, while trading volume-wise, atop the list were futures on the RTS index followed, with a substantial gap, by futures on Rb/\$ and €/ \$ exchange rate, on Sberbank and Gasprom stock. On the RTS FORTS spot market, prices of most recent deals concluded on futures on Rb/\$ with the closing date of 15 September 2011 were mostly within the range 28–28.8 Rb/\$., ie. the market anticipates a 0–2.8% depreciation of Rb. compared with the index as of 22 May 2011. The value of the futures on the RTS index (on the basis of the most recent deals) with the closing date of 15 September 2011 averaged 1,830–1,920 points, ie. the average value of the index is anticipated at the level of the index as of 22 June 2011. Options, meanwhile, enjoy a far lesser demand, with the volume of the respective trading accounting for Rb511.26bn (on futures – Rb4.59bn.). As to the FORTS market's novelties, it is worth noting the beginning of trading with futures on the Russian volatility index since 1 June 2011.

The MICEX index climbed to its peak monthly value of 1,692.34 points on 9 June (the month before it hit 1,691.45 points), while its bottom value was registered on 20 June– 1,626.14 points (1,603.97 points the month before) (Fig. 3).

Volume of trading (RB.bn)

In all, between 23 May and 22 June 2011 the MICEX index added 2.25%, or 36.16 points in absolute terms (between 23 June 2010 and 22 June 2011 it rose by 19.03%), while the turnover of trading with shares included in the MICEX index hit Rb1,044.26bn. The average daily level of activity of investors in stock market in June was down by 10.25% compared with the previous period.

During the period in question, it was Rostelecom and Tatneft's

The Corporate bonds market

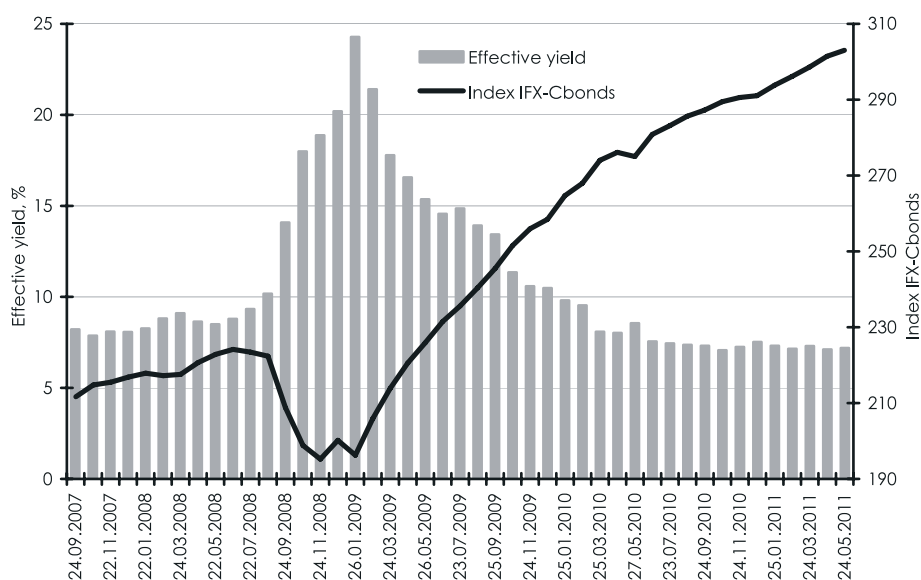
As of end-June, the volume of the domestic market for corporate bonds in Russia (by face-value of papers in circulation issued in the national currency) hit the level of Rb 3,212.3bn, thus having added over 2% when compared with its value as of end-May¹. As a result, the volume of the bond market once again renewed its historic peak. Meanwhile, the number of issuances registered in the national currency remained practically unchanged— 742 (741 in May). The number of issuers presented in the debt segment of the securities market slid slightly and accounted for 343 vs. 347 ones as of end-May. Out of issuances denominated in foreign exchange, it is just the one denominated in € which has remained in circulation.

The turnover of trading with corporate bonds on the stock market posted a substantial growth. Specifically, between 23 May and 22 June the aggregate volume of transactions on MICEX made up Rb172.4bn (for reference, between 25 April and 20 May it was Rb110.3bn.), while the number of transactions accounted for 26,700 (22,100 over the previous period)². But, while comparing to the May performance indicators, it is worth noting the presence of seasonality at the time, and investment activity was on a low level. That said, the June indicators fell short of catching up with record-breaking values of this year's period of March-April.

IFX-Cbonds, the index of the national market for corporate bonds, kept climbing up at a stable pace (2.2 points, or 0.7% over the month in question), and the index has once again renewed its maximum value since the beginning of its calculation. The average-weighted effective yields over the period in question slid insignificantly from 7.21% in late May down to 7.15% in late June. So, overall, it has been for a year already that the average yields in the corporate bond segment remained within the range of fluctuations between 7.0–7.6% (Fig. 5). The duration index of the corporate bond portfolio broke off the tendency to contraction and posted a drastic growth vis-a-vis the prior month – by 151 day - and made up 694 days. This evidences an increase of the proportion of long-term obligations in the corporate segment of the market.

In contrast with the previous month, the yields rates of the most liquid bond issues exhibited an insignificant downward dynamic in June. There was no strong volatility of interest rates, and, while in most cases, the yields rates added no more than 0.1–0.3 p.p. between 23 May and 22 June, it was JSC Rostlecom bonds whose yields rates suffered the most (series 07 and 09 - by 2.2 p.p. and 0.8 p.p., respectively). Meanwhile, industrial corporations exhibited no uniform dynamic of interest rates. Yields rates of papers issued by such corporations as ALROSA, Atomenergoprom, Bashneft, gasprom, Gasprom neft, LUKOIL, Magnitogorsky Mining Plant, GMK Norilsky Nickel, Severstal lost 0.5–0.6 p.p., while yields rates of a string of bond issues of Russian railways, Evraz Holding Finans and Mechel were on the rise.

This month saw a record-breaking for the recent months number of bond issuances. Specifically, between 25 May and 23 June, there were registered as many as 31 issuances of corporate bonds with the aggregate face-value of Rb235.7bn (for reference, between 23 April and 24 May there were registered 32 bond

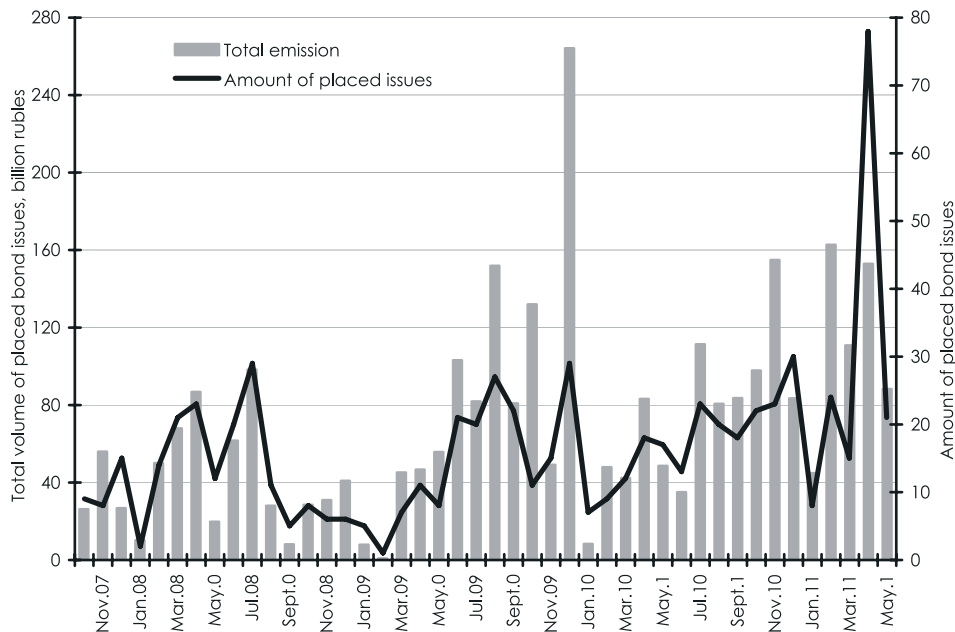


Source: by data of Cbonds.

Fig. 5. Dynamic of the Index of the Russian Market for Corporate Bonds and Average-Weighted Yields

1 By Rusbonds data.

2 By Finmarket data



Source: by Rusbonds data.

Fig 6. Dynamics of the Primary Placement of Issues of Corporate Bonds Denominated in the National Currency

issuances worth a total of Rb61bn). By contrast to May, however, it was mostly huge issuers whose bond issuances passed the public registration. More specifically, the biggest issues were registered by JSC FSK EES (nine series of bonds with the aggregate face-value of Rb125bn), JSC Vympel-Kommunikatsii (five series, 60bn), ZAO Ipotechny agent AIZHK 2011-2 (three series, Rb16.6bn)¹.

After a certain decline in investors' activity in May, the primary placement indices once again picked growth: between 25 May and 23 June as many as

28 series of bonds worth a total of Rb105.6bn. were placed on the market (21 issues with the aggregate face-value of Rb84.4bn between 23 April and 24 May) (Fig. 6). As the month before, the primary market likewise saw a relatively small number of commercial papers (just 7 issuances), while it used to be commercial papers registered following a simplified procedure which had earlier been popular with veteran issuers on the stock market. The bulk of placed issuances fell on two series of bonds of Evraz Holding Finans, Ltd, with the aggregate face-value of Rb20bn, three series of JSC Mechel's bonds with the face-value of Rb15bn, two series of JSC Oil Company Allians (12bn), and two series of bonds issued by JSC Zapadny Skorostnoy Diameter (10bn).

A distinctive feature of primary placements in June became long-term floating of issues. More specifically, five corporations attracted capital for the term of 10 years (TransFin-M, Mechel, Oil Company Allians, and Evraz Holding Finans), while Mekhprachechnaya SvZhD, Ltd. and JSC Zapadny Skorostnoy Diameter placed two *dăbut* bond issues each, for 15 and 20 years, respectively.² Numerous issuers failed to place any paper while entering the primary market. Thus, in the period between 25 May and 23 June, the FSFM of Russia recognized 6 bond issues failed and revoked their state registration, as not a single paper was placed (between 23 April and 24 May there were 12 such bond issues)³.

Between 25 May and 23 June twenty-two issuers were to redeem 23 bonded debts worth a total of Rb30.1bn. However, six of them failed to meet their obligations and defaulted in the performance of bonded debts worth a total of Rb8.7bn (during the previous period, there were five such issuers). It is anticipated that July 2011 will see redemption of 20 issues of corporate bonds worth a total of Rb68.8bn.⁴

The situation with issuers meeting their obligations deteriorated in June. Between 25 May and 23 June six of them failed to pay coupon yields to bond holders (between 23 April and 24 May there were two such issuers), and only one issuer succeeded in reaching an agreement on debt restructuring with bond holders. As in May, there were three issuers who failed to redeem the face-value of their bonded debt, even in the frame of a technical default. As to puttable bonds, all the issuers met their obligations in time.⁵

1 By Rusbonds's data.

2 By Rusbonds data

3 По данным ФСФР России.

4 By Rusbonds data.

5 By Cbonds data.

REAL ECONOMY SECTOR: TRENDS AND FACTORS

O.Izryadnova

Recovery growth of the Russian Economy in May 2011 was determined by the decrease in investment and consumer demand growth rates versus the corresponding period of the previous year, which is accounted for by both a relatively high base of May 2010 and by specific features of the current situation.

The trend towards the decrease in real incomes of the population and the slow-down of wages growth has intensified. The results of the Federal State Statics Service survey give evidence for the decrease in consumer confidence of the population, the retail trade volumes expansion being supported by the decrease of savings norm of the population and growth of consumer crediting.

In January-May 2011 investments in fixed assets made approximately 2/5 of the corresponding figure of 2008. Although weak investment activity of the 1st quarter 2011 gave way to investments in fixed assets growth rates acceleration in April-May 2011, there no sufficient reasons to expect this positive trend to become steady.

If one compares the current situation of recovery from the crisis with the processes of 1999-2001, **the decrease in consumption level that is not compensated by the intensive expansion of investment activity and resulted in slow-down of economy growth rates** is of notice.

The formation of the trend towards the decrease in real incomes of the population and the slow-down of wages growth is worrying.

In January-May 2011 the dynamics of the internal market was defined by the simultaneous growth of both the consumer and the investment demand. The retail trade turnover over the period made 105.2% versus January-May 2010 and 105.5% versus May 2010; volume of the paid services rendered to population – 102.9% and 101.6%, correspondingly.

The increase in retail trade volume is still based on the decrease of savings norm and the expansion of consumer crediting. Credits issued to natural persons made RYR 4192.8bn in April 2011, having increased by 1.2 times as compared with the corresponding month of 2010. The proportion of savings in the incomes of the population reduced to 11.2% versus 16.8% in January-April 2010, savings in the form of deposits and securities reducing to 4.4% versus 7.8%.

The decrease in real incomes of the population and the slow-down of wages growth persists as a negative trend. On the whole over January-May real incomes of the population decreased by 3.7% and real wages went up by only 2.0% versus the corresponding period of the previous year. In May real disposable incomes made 93% of the figure of 2010, reducing by 10.4% versus this April. In May 2011 real wages went up by 2.6% as compared with May 2010, reducing by 0.5% versus April 2011¹.

The situation in the investment sphere has somewhat increased due to the increase of investments in fixed assets by 22.% in April and by 7.4% in May as compared with the figures of the corresponding months of the previous year. On the whole over January-May the increase in investments in fixed assets made 2% versus the level of the corresponding period of the previous year. Recovery of the investments demand is exceptionally slow, and the recovery of the pre-crisis investments in fixed assets level cannot be expected sooner than in 2012 on condition of their average annual increase of 6%.

The specific features of industrial production dynamics this year are mainly determined by the effect of the base (*fig.2*). Industrial production index made 105.2% versus January-May 2010 and 104.1% versus May 2010. It is the manufacturing industries that had a prevailing impact on the industry dynamics and structure. Manufacturing production index was equal to 108.1% versus

¹ In May 2011 report the Federal State Statistics Service increased the estimation of real wages in 2010 versus 2009 up to 5.2% versus 4.9%. The data on the wages growth rates for April 2011 versus April 2010 were corrected – 2.4% as compared with 2.7% published earlier.

January-May 2010 and 105.0% versus May 2010, extractive industries indices being 102.7% and 102.1%, correspondingly.

The dynamics of the manufacturing sector remains considerably differentiated by types of economic activities and depend on such factors as the level of facilities load, structure and dynamics of internal solvent demand, orientation towards external market, expenses and prices dynamics.

It should be noted that the change in the structure of demand for both domestic and import goods is observed at the internal market. In the 1st quarter 2011 the proportion of investment goods import made 18.1%, exceeding by 1.3 percentage points the corresponding figure of the 1st quarter 2010. It is of notice that this year the trend towards the increase of the proportion of intermediate goods has intensified while the supplies of consumer goods have decreased. Consequently, the proportion of import in the retail trade resources decreased by 1 percentage point as a result of the 1st quarter and made 43%. The proportion of import good in retail trade turnover stabilizing at the level of 35%, the import share at the market of non-food goods reduced by 2.2 percentage points as compared with the 1st quarter 2010 and made 50.4%. This is accounted for by the recovery of domestic production of household appliances, passenger cars, furniture, sewing goods and footwear and leather goods.

Table 1

PROPORTION OF CONSUMER, INTERMEDIATE AND INVESTMENT GOODS IN THE TOTAL VOLUME OF IMPORT IN THE RUSSIAN FEDERATION (BASED ON BALANCE-OF-PAYMENTS METHODOLOGY), AS PERCENTAGE TO TOTAL

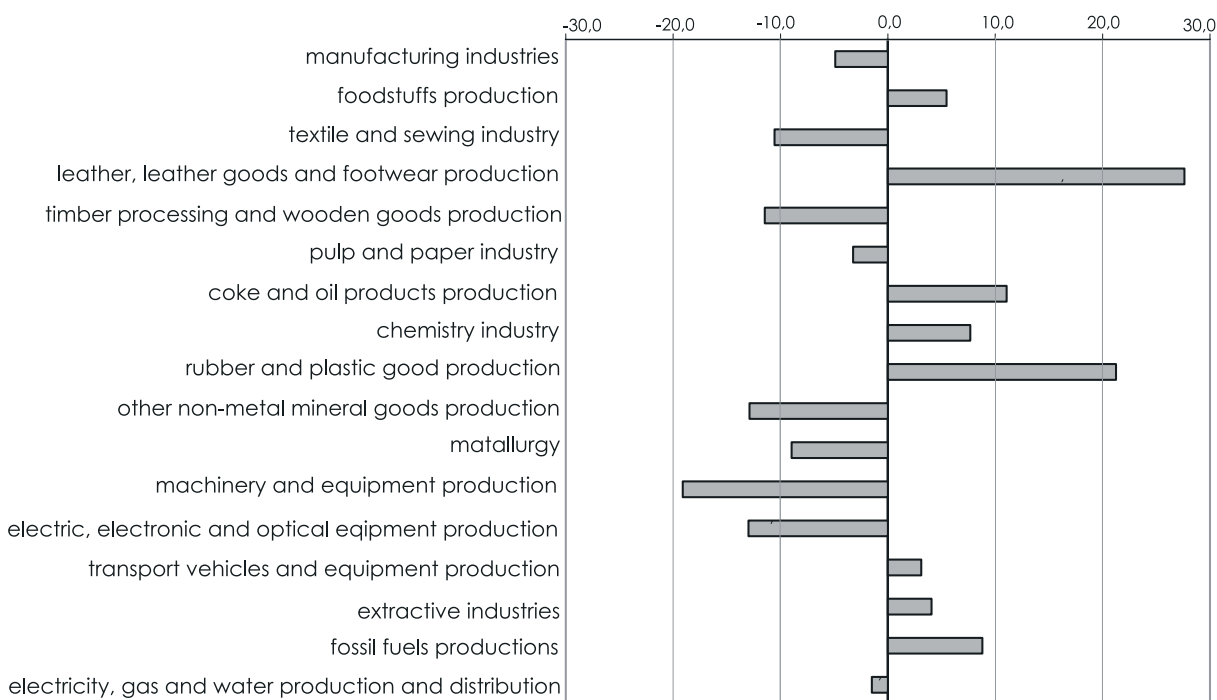
	Goods		
	Consumer	Investment	Intermediate
2009			
1 quarter	46.8	18.6	34.9
2 quarter	44.0	18.1	38.4
3 quarter	42.9	20.6	36.5
4 quarter	43.9	19.5	36.6
Year	44.3	19.7	36.0
2010			
1 quarter	43.5	16.8	39.7
2 quarter	39.6	18.7	41.7
3 quarter	40.6	19.7	39.7
4 quarter	40.0	21.5	38.5
Year	40.7	19.5	39.8
2011			
1 quarter	40.5	18.1	41.4

Source: Federal State Statistics Service

The complex of machine-building productions, chemistry industry, timber processing, leather, leather goods and footwear production make the major contribution into the increase in manufacturing industries output. The rate of overcoming the aftermaths of 2008 crisis and return to the growth trajectory are defined by internal problems in functioning of the specific sectors of economy. On the whole the structure of 2009-2011 growth reproduces the scheme of post-crisis development in 1998-2000, when the growth started with the increase in foodstuffs production and minerals extraction and the acceleration of development of manufacturing industries connected with hydrocarbons and other mineral raw materials processing.

The rates of recovery in chemistry industry, timber processing, pulp-and-paper and industry and metallurgy are highly dependent on the changes in foreign economic situation since the proportion of export supplies in the production of some goods in these types of economic activities is in the range of 45-80%. The rates and structure of recovery in machine-building complex, rubber and plastic goods production as well as in the complex of consumer goods oriented to the internal market is defined by the level of solvent demand and their competitiveness versus the import goods.

In January-May 2011 machinery and equipment production index made 108.4% versus January-May 2010, the volumes of production in all the trade nomenclature subclasses of this group growing with exclusion of mechanical equipment production (96.6%). The solvent demand for technological



Source: Federal State Statistics Service

Fig. 2. Industrial Production Growth Rates as Broken by Types of Economic Activities in May 2011, as percentage (May 2008 = 100.0%)

equipment increasing in January-May 2011 versus the corresponding period of 2010 the volume of machine tools production went up by 23%, production of forge-and-pressing machines increasing by 47.1%, of metal-cutting tools – by 46.3%. Financial and economic situation at agriculture enterprises stabilizing, the volumes of machinery and equipment production for agriculture and forestry grew by 15.5%. For instance, production of tractors for agriculture and forestry increased by 2.1 times, of field forage harvesters - by 40.7%, of reaping threshers - by 2%.

In January-May 2011 the index of electronic, electric and optical equipment production made 107.4% versus January-May 2010. The production dynamics was considerably influenced by the improvement of the situation in the sectors that consume the produced goods due to the increase in demand for components and final goods. As compared with the corresponding period of 2010 in January-May 2011 the production of office equipment and ADP equipment went up by 24.9%, electronic components, equipment for radio, television and communication – by 20.9%, electric machines and equipment – by 13.4%.

In January-May 2011 the index of transportation vehicles and equipment production was 140.2% versus the level of the corresponding period of 2010. The increase in railway transportation freight turnover by 6.9% in January-May 2011 versus the corresponding period of the previous year contributed into the increase of shunting and industrial locomotives by 63.0%, of mainline freight cars – by 43.4%, of main-line locomotives – by 8.3%.

As compared with January-May 2010 in January-May 2011 the production of passenger cars went up by 85.8%, which is mainly connected with the fulfillment of programs for stimulation of the demand for cars (utilization of cars, subsidies for credits' interest rates for purchase of new passenger cars).

In January-May 2011 production of trucks went up by 63.1% versus the corresponding period of the previous year, which was mainly aided by leasing mechanism of sale of this type of Russian equipment.

The growth recovery in the industry takes place against the background of increase in risks connected with the growth of production expenses, caused by inflation. As compared with the beginning of the year industrial producers' prices went up by 110.4% in May 2011 (by 8.9% over the corresponding period of 2010). In January-May 2011 the prices growth dynamics is observed to weaken in the manufacturing industries to 106.0% versus 108.8% in the corresponding period of

2010. This is connected with slower growth of tariffs for freight transportation (111.0% in January-May 2011 versus 130.4% in May 2010 versus December of the previous year) and producers' prices in electricity, gas and water production and distribution (109.0% versus 112.0%, correspondingly).

Dynamics of financial results of the Russian industry is accounted for by both the demand recovery and correction of production volumes and level of prices taking into account the competitive environment at the internal market.

Favorable situation at the world market of energy carriers allowed the enterprises involved in minerals extraction to get the balanced financial result of RUR 476.6bn in the 1st quarter 2011, which is by 87.7% more than the corresponding figure of January-March 2010. The financial situation in manufacturing industries somewhat improved: over the same period their balanced financial result was equal to RUR 504.9bn, which exceeded by 48.0% the level of the corresponding period of 2010. Under existing dynamics off prices products profitability in extractive industries reached 41.7%, in fossil fuels production – 39.5%. In the 1st quarter 2011 profitability of manufacturing industries made 14.1% remaining, however, 3.3 percentage points below the level of pre-crisis 1st quarter 2008. The pricing policy being reserved, the growth of financial results and gradual increase in profitability in the majority of processing industries was secured mainly by the increase in production and load of facilities. Besides, the level and dynamics of financial results were influenced by the growth of wages, which allowed maintaining labor potential decreasing at the same time the excessive number of the employed. It is quite possible that in this situation the prices in manufacturing sector can grow which will serve for securing stable growth of profitability. However adoption of such a decision implies thorough analysis of domestic goods competitive ability versus foreign goods in the environment of import cheapening.

Table 2

PROFITABILITY OF SOLD GOODS, PRODUCTS, WORKS, SERVICES, ASSETS AS BROKEN BY TYPES OF ECONOMIC ACTIVITIES IN THE 1ST QUARTER 2008-2011, %

	Profitability of sold goods, works, services				For reference		
					1 st quarter 2011 versus 1 st quarter 2010		March 2011 versus December 2010
					financial results growth rates	physical volume indices	Prices index
	2008	2009	2010	2011			
Total	15.5	11.0	12.7	12.6	133.1		
minerals extraction	34.7	19.3	31.5	41.7	183.7	103.3	113.1
fossil fuels extraction	32.8	18.9	31.3	39.5	176.4	100.3	113.3
minerals extraction excluding fossil fuels	51.4	22.5	33.5	61.2	240.0	107.7	111.6
manufacturing industries	17.4	10.8	12.9	14.1	148.0	110.6	103.8
foodstuffs, including beverages and tobacco production	8.7	11.9	9.5	9.4	90.5	101.7	102.8
textile and sewing industries	3.7	3.3	3.2	4.6	145.6	107.7	111.3
leather, leather goods and footwear production	4.1	8.3	6.5	6.3	115.2	112.8	102.2
timber processing and production of wooden goods	6.2	-1.5	-1.3	7.5	210.0	106.9	103.4
pulp-and-paper industry	9.0	7.3	6.9	12.1	182.3	99.5	103.6
coke and oil products production	30.1	23.8	22.7	22.7	152.2	104.6	99.0
coke production	16.1	-11.0	13.2	14.4	310.0	-	111.5
oil products production	30.5	24.4	22.9	22.9	150.6	-	99.6
chemistry industry	30.1	15.0	17.2	24.3	183.6	108.0	106.3
rubber and plastic goods production	6.8	2.3	3.8	6.7	78.6	120.6	102.5
production of other non-metal mineral goods	23.3	3.9	1.1	3.3	-	112.7	103.3
metallurgy and production of finished metal goods	25.0	7.2	18.0	18.5	126.7	109.1	108.5

Table 2, cont'd

	Profitability of sold goods, works, services				For reference			
					1 st quarter 2011 versus 1 st quarter 2010		March 2011 versus December 2010	
					financial results growth rates	physical volume indices	Prices index	
metallurgy	27.7	7.5	20.1	20.6	126.7	105.7	110.2	
production of finished metal goods	8.3	5.3	3.2	3.2	47.2	116.5	101.6	
machinery and equipment production	4.9	6.5	6.0	5.1	142.3	111.6	103.5	
electric, electronic and optical equipment production	7.4	3.2	6.3	5.8	134.3	106.3	103.5	
transportation equipment and vehicles production	5.4	-0.3	0.6	4.4	-	159.6	105.0	
electricity, gas and water production and distribution	7.7	13.3	11.5	12.7	107.6	99.0	111.1	

Source: Federal State Statistics Service

It should be noted that the growth of manufacturing industries is accompanied with the increase in the wages as compared with the average Russian level and is not supported by the adequate growth of labor efficiency. In this connection modernization and diversification of the production is of key importance for the increase in recovery growth. ●

RUSSIAN INDUSTRY IN MAY 2011

S.Tsukhlo

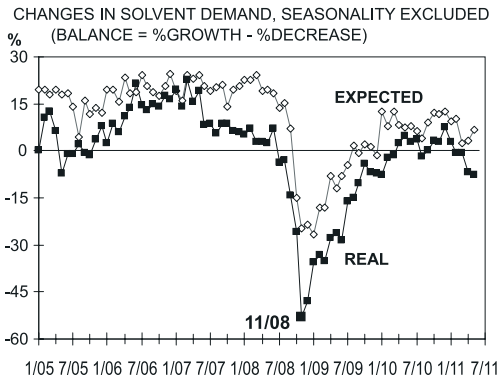


Fig. 1

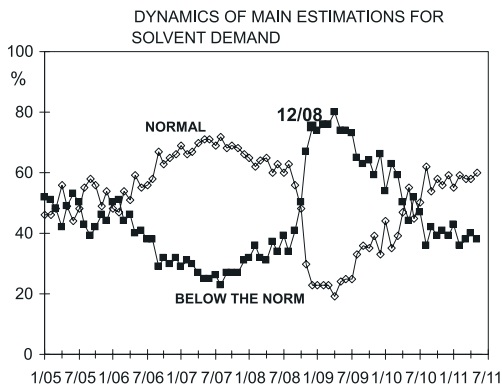


Fig. 2

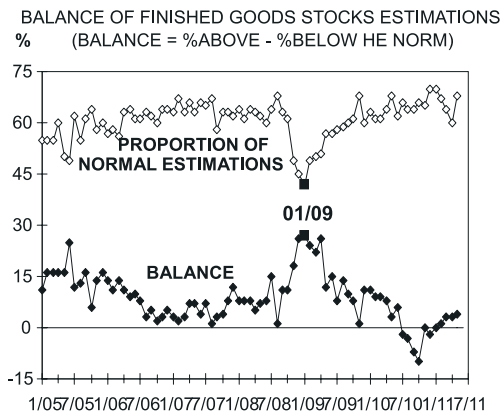


Fig. 3

According to the data of the Gaidar Institute surveys¹, the demand having started to contract the enterprises are constraining the output growth, allow warehouses to be filled with the finished goods and stop hiring employees. However the maintaining satisfaction with the sales demonstrate that the producers have adapted to the existing situation, while the improvement in demand forecasts, output plans and absence of the intention to dismiss any more employees give evidence for a possibility of a new forthcoming upsurge in the industry.

Demand for industrial goods

In May the decrease in the demand for industrial goods was registered by all the indicators. The initial data demonstrated the sales dropping at the rate of -5 points. Such an intensive contraction of demand in May has not been observed since 2005 (not taking into account the crisis 2009, certainly). In May the sales contracted in all the sectors excluding metallurgy, production of construction materials and foodstuffs production. Exclusion of seasonality made the decrease even more intense – to -8 points. As a result the sales growth rate lost 16 points as compared with December 2010. The definite increase in demand gave way to the no less definite decrease. May indicator values turned out to be the worst since autumn 2009 (!). However, in forthcoming months the enterprises expect this negative trend to be overcome (fig. 1). At least, such are their forecasts. The sales are expected to grow in all the sectors of industry. In 2011 the satisfaction of the enterprises with the demand is relatively stable and reflects their adaptation to the slacken dynamics of the Russian economy in the recent months. The proportion of normal estimations of the demand make on average 59% throughout the industry in April-May (fig. 2). In fuel and energy sector normal estimations make 100%, in metallurgy – 80%, in chemistry and machine-building – 70%. The worst results were observed in the industry of construction materials (43%) and light industry (37%).

Finished Goods Stocks

In the last seven months the balance of estimations of finished goods stocks demonstrates an amazing stability, changing from -2 to +4 points (fig. 3). The formal increase of 6 points took place mainly because of the negative trends in the demand dynamics and not due to the enterprises

1 Surveys of industrial enterprises directors have been conducted by the Gaidar Institute according to the European harmonized methodology monthly since September 1992 and encompass all the territory of the Russian Federation. Panel size makes about 1100 enterprises, at which more than 15% of the employed in the economy work. The panel is shifted towards large enterprises in each of the sectors allocated. Questionnaires recovery makes 65-70%.

conscientiously filling the finished goods stocks expecting the sales revival. Little absolute value of the indicator, however, testifies that the producers confidently manage their stocks.

Production Output

According to the initial data the output growth rates continue to decrease after they reached the crisis maximum in March 2011, remaining though positive, i.e. the production volume is continuing to grow. In May growth intensity dropped to the minimum of the previous 16 months (not taking into account January 2011). Exclusion of seasonality demonstrated that April growth rates which have been the minimum of the previous 14 months were maintained in May.

After the drop to twelve-month minimum in March 2011 the output plans have been improving for the second month in the row. However at the moment they are based only on May forecasts for the demand. Neither the real sales dynamics nor the preceding forecasts for the demand give any grounds for such a growth in production plans optimism. However, in pre-election 2011 the government may provide more support to the domestic industry.

The industry is well-equipped to manage possible (and so desired, certainly) growth of the demand for the goods produced. First, facilities load reached only 68% in 2011, whereas the maximum level of the facilities load in the period between the crises made 74% (2007). Second, only 19% of enterprises consider the shortage of facilities as an obstacle to production. The pre-crisis maximum for this obstacle citation made 32%. Third, in industry, according to the estimations of the producers there is excess of facilities in the industry (as compared with the expected changes in the demand) at 14% of enterprises (fig. 5). The prevailing majority of the producers hold the existing facilities as “sufficient” for the forthcoming changes in demand. It should be noted that this indicator has reached the absolute maximum value of 1993-2011. In other words, in 2011 the industry is better equipped with machinery and equipment for the demand growth than ever before.

Producers’ prices

In May the prices growth has again become less intensive but only by 4 points. After a leap in January, in February the indicator has lost 13 points, in March and April – 9 points. As a result over the last four months the intensity of prices growth in industry has decreased by three and half times (according to the balance of changes) (fig.6). The least intensive growth of prices in recent months is registered in the wood processing industry, industry of construction materials and foodstuffs production. Further decrease in prices growth rates is however doubtful. In May the enterprises plans demonstrated a U-turn in their price policies. Whereas from January to April the plans for prices changes decreased consecutively, in May this process was stopped and Russian producers for the first time in 2011 declared the intentions to increase prices growth rates or at least to stop their fall (fig. 7).

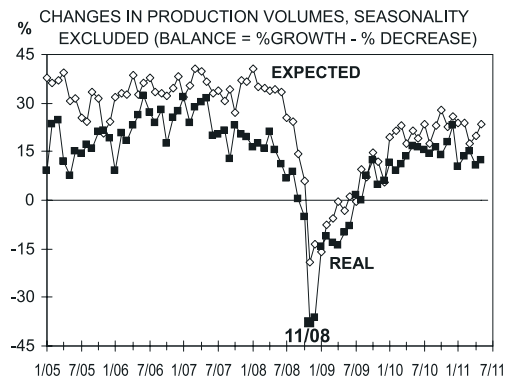


Fig. 4

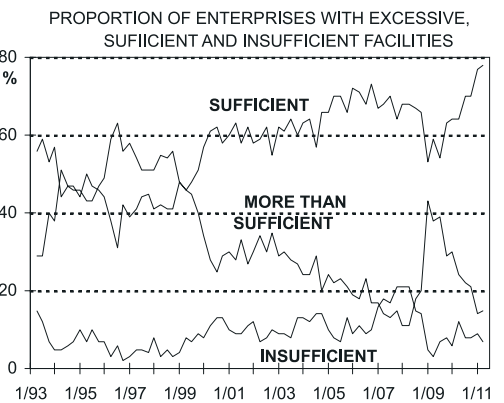


Fig. 5

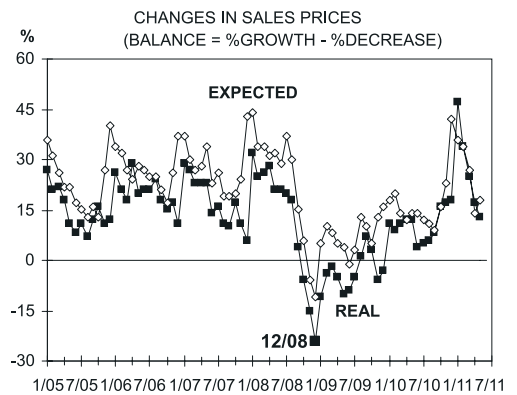


Fig. 6

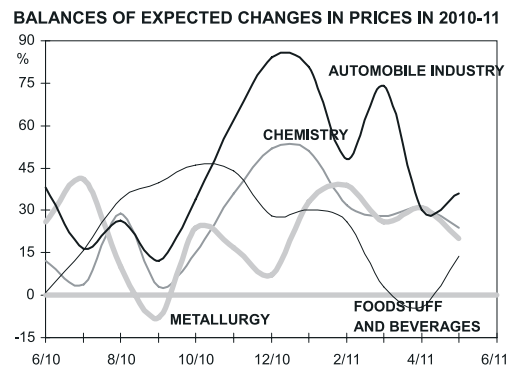


Fig. 7

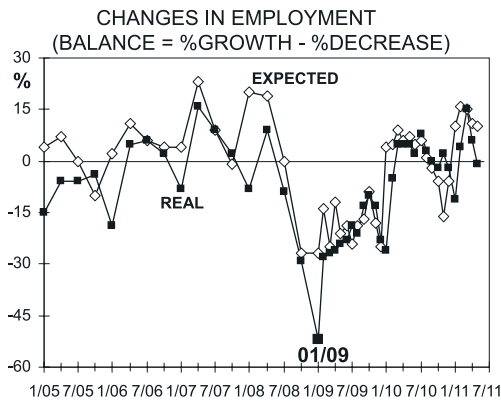


Fig. 8

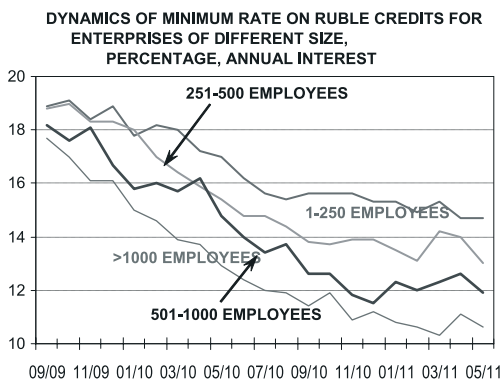


Fig. 9

Dismissals: Real Dynamics and Plans

In May industry stopped hiring the staff breaking the trend of three previous months. After record-breaking figures of March (the record-breaking figures for the whole period of monitoring of the indicator since 2003) the employment growth rate lost 15 points and became zero. That is, the hiring has stopped but the dismissals have not started throughout the industry yet. It seems that the Russian enterprises are not ready to resort to them at the moment. The enterprises' plans testify that. In May the balance of plans for the changes in staff number remained practically at the level of April, a bit below the crisis record of February 2011 (*fig. 8*). In the forthcoming months the dismissals are possible only in the sectors of non-ferrous metallurgy, chemistry and petrochemistry.

Crediting of Industry

Since the beginning of 2011 the accessibility of bank credits for industrial enterprises makes on average 72% (according to the sum of estimations "above the norm" and "normal"). The banks' priorities have not changed: metallurgical enterprises are offered the most preferential crediting conditions (83% of the enterprises is satisfied or more than satisfied with the conditions in 2011), chemistry and petrochemistry enterprises (82%), foodstuffs production (78%) and machine-building enterprises (76%). Timber processing sector (46%) and light industry (39%) are at the other end of the spectrum. Average minimum per annum rate offered by

the banks has sunk to 12.4% in May throughout the industry. However small and medium-scale enterprises are offered the credits for 14.7% per annum at best, and very large enterprises – for 10.6% per annum (*fig. 9*). The ability of enterprises to serve the credits they already have has started to decrease in 2011. In May the figure dropped to 81% (of the number of enterprises that have credits) after record-breaking 87% in December 2010. Such a negative trend is accounted for by the obvious worsening of the financial situation at enterprises registered in the 2nd quarter 2011.

Worsening of the financial situation together with the absolute decrease in sales and uncertain future makes the enterprises correct the borrowing plans. In the 2nd quarter 2011 the indicator decreased to +10 balance points after +18 balance points in the 4th quarter 2010. In the forthcoming months the highest demand for credits will be characteristic for electric power industry (+32 balance points), timber processing (+18 balance points) and light industry (+16 balance points). The contraction of the demand for credits is possible in metallurgy and industry of construction materials.

Reaction of Industrial Enterprises to the Increase in the Rates of Insurance (Single Social Tax)

A year ago (in May 2010) we supplemented the regular questionnaire with a question on how the enterprises INTENDED to react to the increase in the rate of compulsory pension, social and health insurance (single social tax) from 26% to 34% in 2011. In May 2011 we again asked the same question but this time it was about the REAL reaction of the enterprises to this tax novation. The obtained data allow getting clear and the most reliable reaction of enterprises to the increase in tax burden straight from the source (*fig. 10*). This is especially important in view of heated discussion about the cancellation of the novation.

Prices, profit, investments

It was the increase in prices that was the most frequent reaction to the increase in the single social tax (we will use this old denomination) during active debates about it in 2010. This was

INTENDED (2010) AND REAL (2011) REACTION OF ENTERPRISES TO THE INCREASE IN RATE OF INSURANCE, AS PERCENTAGE TO THE NUMBER OF RESPONDENTS

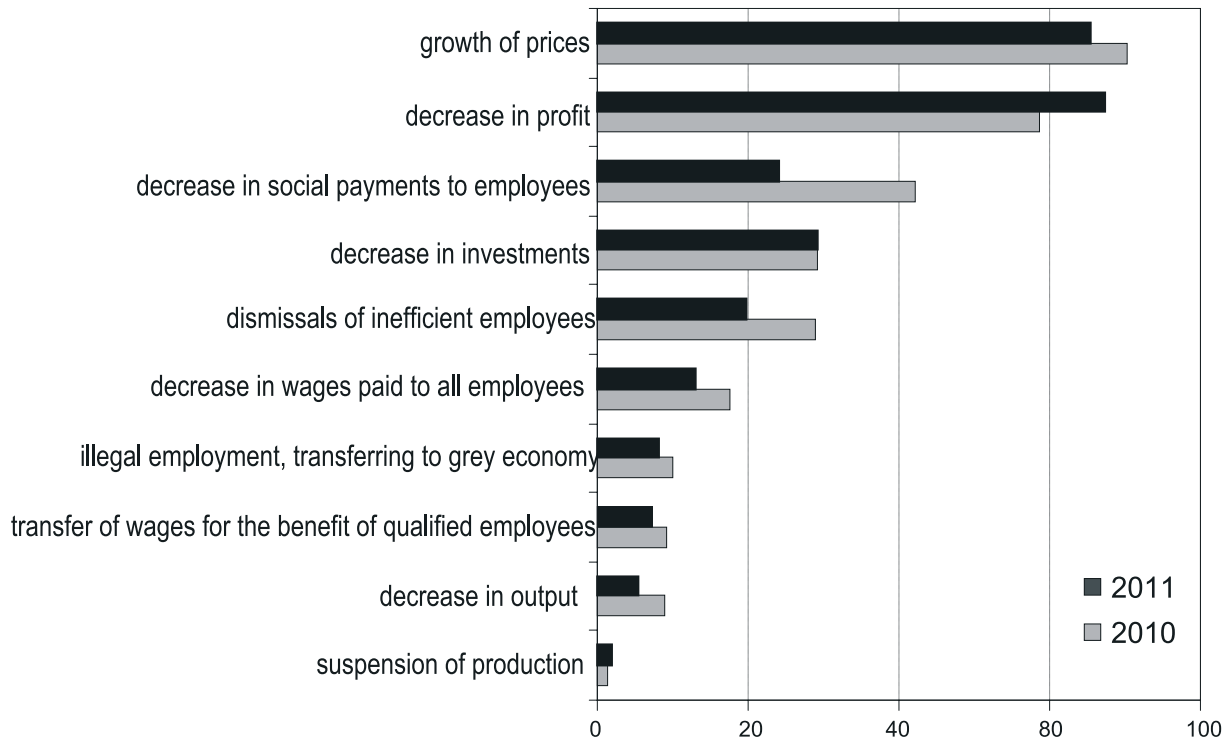


Fig. 9

forecast by 70% of enterprises a year ago. The small enterprises (below 100 employees) were more likely to plan the increase prices, 82% of them reporting such plans. Breaking by the sectors of industry demonstrated that the prices growth is most probable in light industry, machine-building, chemistry and petrochemistry. 80% of the state-owned enterprises, 68% of open joint-stock companies, 73% of closed joint-stock companies and 80% of limited liability companies reported the intention to increase the prices in 2010.

In 2011 65% reported the real increase in prices as a response to single social tax increase. Small enterprises were ready to increase the prices only in 65% of cases, the enterprises with 251-500 employees being the leaders in prices growth. Light industry, as it was forecast, resorted to prices growth as a protection against new single social tax more often (85%) than other sectors of industry, second place being held by machine-building industry (78%) and chemistry industry (71%). Only 42% of foodstuffs producers reported the increase in prices while 64% intended to use such a measure. It seems that the fact that foodstuffs became more expensive in autumn and winter allowed to salve difficulties with new single social tax for the industry. State-owned enterprises increased their prices in full accordance with their plans in 80% of cases. However it was limited liabilities companies that became the leaders with respect of prices growing.

The decrease in profit held the second place in the list of most frequent reactions, which means the willingness to cover increase in rates at enterprises' expense. In 2010 59% of enterprises reported it. This measure was acceptable for nearly all the enterprises of fuel industry and ferrous metallurgy, three quarters of enterprises of timber processing industry and about 60% of enterprises in non-ferrous metallurgy and machine-building industries. Light industry occupied the other end of the spectrum, only 30% of enterprises being able to use profit for the payment for the increased rates.

As the survey of 2011 demonstrated the use of the profit was the most popular source for payments to the government. 67% of enterprises used it. In foodstuffs production, timber processing and metallurgy more than 80% of enterprises resorted to it. This circumstance seems to make the estimations of financial and economic situation at enterprises graver in the 2nd quarter 2011, when the situation definitely worsened. The balance of estimations decreased for the first time since Jan-

uary 200, and quite considerably - from -5 to -13 balance points. This resulted from the expansion of estimations “bad” from 15 to 21% and contraction of estimations “satisfactory” from 71% to 65%. At the time of crisis overcoming the indicators cited did not demonstrate the negative trend.

29% of industrial enterprises reported the intention to decrease investments in the environment of the growth of the tax burden. And this was accurate. In 2011 29% of enterprises reported this reaction. It was the enterprises of non-ferrous metallurgy (49% planned to refuse from investments, 39% refused de facto in 2011), timber processing (46%, 39% de facto) and light industry (40%, 34% de facto) most frequently cited the willingness to refuse from investments a year ago. Machine-building industry also belongs to the group of leaders of investments decrease due to the rates of insurance growth: 31% of enterprises planning the decrease, 36% made the actual decision.

Dismissals, wages, social payments

In 2010 decrease in social payments to employees (voluntary health care, other social payments to employees, privileged crediting) held the third place by frequency of citation in the list of 10 possible reactions to the increase in rates of insurance. Large enterprises were more likely to plan this measure (which is understandable since such expenses are more characteristic for them), non-ferrous metallurgy plants and industry of construction materials production.

However, the real economy due to the social support of the employees was less frequent. In 2011 this “source of financing” for the grown expenses for the single social tax was reported by only 24% of enterprises. The accuracy of enterprises’ forecasts in this direction resulted to be the lowest. The frequency of the protective measure in question sank to the fourth place. Small-scale enterprises resorted to it more often than large ones. Foodstuffs production, timber processing and non-ferrous metallurgy applied it most frequently.

Dismissals of inefficient employees due to the increase in rates of insurance were planned by 29% of enterprises in 2010. They were especially wide-spread in non-ferrous metallurgy and light industry. In fact only 20% of industrial enterprises could (were willing to) resort to this measure. These included primarily small and very large enterprises, primarily in machine-building and light industries.

The general contraction of wages to decrease the volume of rates of insurance was planned by 18% of enterprises in 2010. Small enterprises were more prone to this measure, factory size increasing possibility of wages decrease lowering. The willingness to resort to such unpopular measures reached 25% in ferrous metallurgy and industry of construction materials production. However, in 2011 only 13% of enterprises reduced wages. As it was forecast, small enterprises used this measure more often. Only foodstuffs production stands out from other industries, the percentage of enterprises using such a measure being 24%.

Low popularity of the reactions connected with employment and labor remuneration is, in our opinion, connected with big problems that enterprises face and will face at the labor market. Before the crisis of 2008 the qualified staff became a considerable obstacle for the production growth in the Russian industry. In July 2008 it was cited by half of enterprises. At the stage of crisis overcoming the enterprises start realizing that the staff can soon again become the most critical resource. The shortage of staff in connection with the “expected changes in demand” has been observed in the industry for the fourth quarter in the row. So, the enterprises try to solve their problems at the expense of employees only as a last resort.

Application of “criminal” protective measures (transfer of wages to the most qualified staff with further redistribution by backdoor salaries, decrease of the payments by illegal employment, general shift towards grey economy) was planned by only 9-10% of enterprises in 2010. 7-8% of factories fulfilled such measures. ●

INVESTMENTS IN REAL ECONOMY SECTOR

O.Izryadnova

*In April and May 2011 the increase in scale of investment expenses as compared with the corresponding months of the previous year and preceding months of the current year had a positive effect on the dynamics of investments in fixed assets. **Over January-May 2011 investments in fixed assets growth rates made 102.0% versus the corresponding period of the previous year. At the same time the decrease of investments in fixed assets at small enterprises can be regarded as a negative trend.***

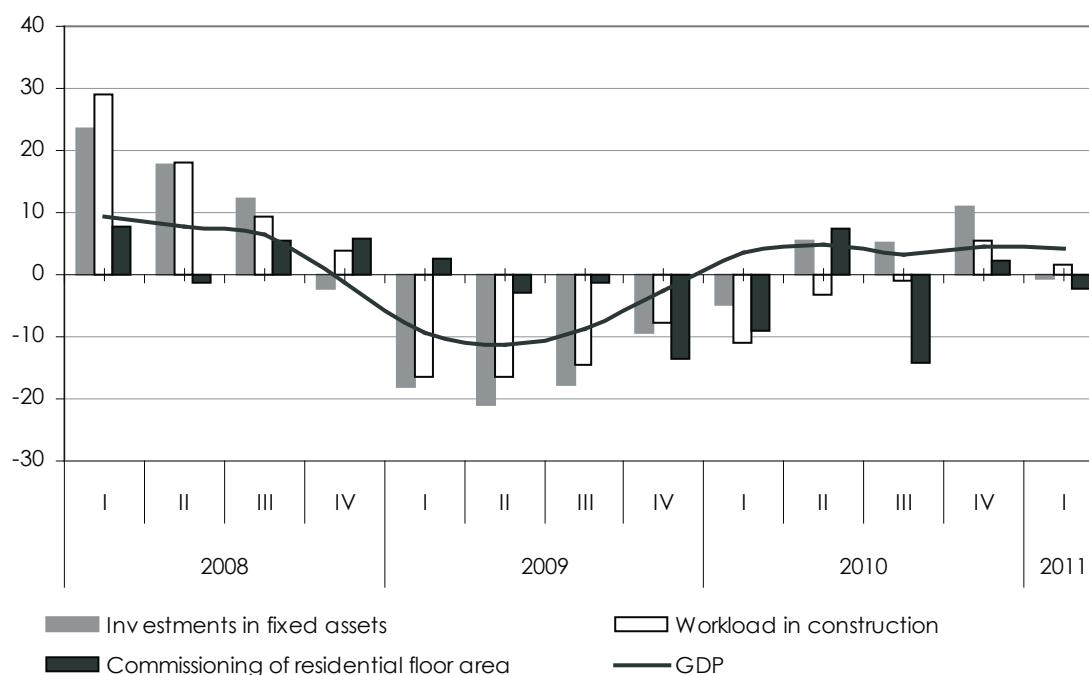
The trend towards the decrease in banks' credits and organizations' borrowed funds in the structure of investments financing sources has become more pronounced. It should be noted that simultaneous decrease in the volume of the credits issued by Russian and foreign banks and the increase in private capital export is a signal of necessity of fundamental changes in investment climate.

Analyzing the dynamics of investments the specific features of business activity post-crisis recovery should be taken into account. The peak of the investment crisis was passed in the 1st half of 2009, and starting with the 3rd quarter 2009 the trend towards the slow-down of investments decrease has been observed that was supported by the improvement in financial situation at enterprises. On the whole over 2010 the increase in investments in fixed assets was at the level of 6% while GDP went up by 4% versus 2009.

Over January-May 2011 investments in fixed assets reached RUR 2696.0bn having increased by 2% in real terms versus the corresponding period of the previous year. The start of the investments growth is connected with the increase by 7.4% in May 2011 versus the corresponding period of the previous year. It should be noted that in 2010 the recovery of investment activity was also first registered in April-May.

It should be remembered that in the 1st quarter 2011 while GDP increased by 4.1% versus the corresponding period of the previous year, investments in fixed assets decreased by 0.8% and the workload in construction went up by 1.6%. The volume of executed works in construction made 100.8% in January-May 2011 versus January-May 2010, housing area implementation – 93.1%. Low business activity in construction is accounted for by both underinvestment in construction works in the 1st quarter and the absence of sufficient groundwork. The index of provision of construction organizations with contracts and orders that is high this year as compared with the previous year is a positive factor, which allows optimistic forecasts of acceleration of investments in construction growth rates.

The dynamics of investment in fixed assets is considerably different for small and large enterprises. Whereas 2008 crisis at its initial stages resulted in critically low indicators of investment activity at small-scale enterprises, in 2009-2010 the positive dynamics of investment activity in the segment of small-scale enterprises was the factor that reserved the decrease in the scales of investments into the economy as a whole. In 2010 financial support of the small- and medium-scale enterprises was one of the priorities for the government bodies. In 2010 the total volume of budget allotments allocated for the government support of small- and medium-scale enterprises made RUR 7.97bn. In 2010 investments in fixed assets in the segment of small enterprises went up by 8% (reduction of 13.5% in 2009), their share in the total volume of investments in economy increasing to 32.1% versus 27.2% in 2009. However these structural changes were of momentary nature since they were not supported by the fundamental changes in the investment climate. Thus, as soon as the 1st quarter 2011 the volumes of investments in fixed assets decreasing by 0.8% versus the corresponding period of the previous year, the drop of investment activity in the segment of small enterprises made 5.5%, their share in the total volume of the investments in the economy reducing to 29.2%.



Source: Federal State Statistics Service
 Fig. 1. GDP, Investments in Fixed Assets, Workload in Construction and Residential Area Implementation Growth Rates by Quarters in 2008-2011, as percentage to the corresponding period of the previous year

In the segment of large and medium enterprises the investments in fixed assets increased by 1.9% in the 1st quarter 2011 versus the corresponding period of the previous year, the growth being less spectacular taking into account the investments decrease of 21.1% in the 1st quarter 2010. In the 1st quarter 2011 investments at large and medium-scale enterprises made 73.6% versus the corresponding period of pre-crisis 2008.

It should be noted that in the 1st quarter 2011 the absolute increase in investments in fixed assets scale is observed for all kinds of fixed assets. Investments in machinery and equipment went up by RUR 59.4bn as compared with the 1st quarter 2010, including by 50.2bn into domestically produced models. Investments for purchase of import machinery, equipment, transport vehicles (not taking into account small business and volume of investments not registered by direct statistical methods) in the 1st quarter 2011 or 19.5% of the total volume of investments in this type of fixed assets (RUR 54.4bn or 20.4% in the 1st quarter 2010, RUR 76.7bn or 25.5% in the 1st quarter 2009).

Table 1

STRUCTURE OF INVESTMENTS IN FIXED ASSETS AS BROKEN BY TYPES OF FIXED ASSETS IN THE 1ST QUARTER 2009-2011 (NOT TAKING INTO ACCOUNT SMALL BUSINESS AND PARAMETERS OF INFORMAL ACTIVITY), AS PERCENTAGE TO THE TOTAL

	RUR billion			As percentage to the total		
	2009	2010	2011	2009	2010	2011
Investments in fixed assets	933.3	802.1	956.8	100	100	100
including: housing	56.4	44.3	47.6	6.0	5.5	5.0
buildings (excluding residential) and constructions	481.8	410.5	499.2	51.6	51.2	52.2
machinery, equipment and transport vehicles	300.6	266.7	326.1	32.2	33.2	34.1
other	94.5	80.6	83.9	10.2	10.1	8.7

Source: Federal State Statistics Service

The trend towards the decrease in residential area implementation against the background of exceptionally low investments in housing construction recovery is characteristics for 2009-2011. The reduction of the implementation of residential area has been observed since the 2nd quarter 2009. In 2010 the implementation of residential floor area decreased by 2.4% as compared with the previous year. The situation of 2010-2011 is adversely affected by the contraction of the

groundwork for housing construction volume. In April-May 2011 implementation of residential floor area reduced by 13% versus the corresponding period of the previous year. This trend in construction is developing against the background of some improvement in situation with financing. In the 1st quarter 2011 the funds received for participation in shared housing construction went up by RUR 1.2bn, funds of population – by RUR 2.8bn. In 2010-2011 the volumes and shares of funds of population in shared construction financing, the organizations' funds continuing to decrease at higher rates.

The structure of investments in fixed assets as broken by sources of financing was subject to considerable changes. In the 1st quarter 2011 the proportion of investments made at the own expenses of enterprises went up by 3.5 percentage points, the proportion of borrowed funds decreasing correspondingly. It should be noted that in the 1st quarter 2011 profitability throughout the economy made 12.6% and remained practically at the level of the corresponding period of the previous year, but the proportion of investments financed from the organization's profit went up to 18.0% versus 15.0% in the 1st quarter 2010.

The scantiness of own funds was not compensated by attraction of banks' credits and borrowed funds. In the 1st quarter 2011 RUR 66.5bn or 13.5% of RUR 492.0bn of attracted funds was accounted for by banking credits (17.3% in the 1st quarter 2010, 22.6% in the 1st quarter 2009). As compared with the 1st quarter 2010 the credits issued by Russian banks contracted by RUR 1.6bn, and credits issued by foreign banks – by RUR 7.9bn.

The role of the budget funds in the structure of attracted funds for investments financing has been changing as well. In the 1st quarter 2011 RUR 127.6bn of investments in fixed assets was financed at the expense of budget funds (13.3% of the total investments in the economy), RUR 51.9bn (5.4%) was financed from the federal budget and RUR 69.0bn (7.2%) – from the budgets of the subjects of the Federation.

Besides, while in the 1st quarter 2011 foreign investments in the Russian economy went up by 3.4 ties as compared with the level of the corresponding period of the previous year and made \$44.3bn, their structure did not contribute into the revival of investment activity in the real economy sector. Direct investments made 8.8% of the total volume of the foreign investments received by the Russian economy as compared with 20% in the 1st quarter 2010. As a result the proportion of foreign investments in fixed assets in the structure of investments made 3.8% in the 1st quarter 2011 and was 2 percentage points below the corresponding figure of the previous year.

Table 2

STRUCTURE OF INVESTMENTS IN FIXED ASSETS AS BROKEN BY SOURCES OF FINANCING, IN THE 1ST QUARTER 2009-2011, AS PERCENTAGE TO THE TOTAL (NOT TAKING INTO ACCOUNT THE SUBJECTS OF SMALL-SCALE ENTREPRENEURSHIP AND PARAMETERS OF INFORMAL ACTIVITY)

	RUR billion			As percentage to the total		
	2009	2010	2011	2009	2010	2011
Investments in fixed assets	933.3	802.1	956.8	100	100	100
of which by sources of financing:						
own funds	381.3	362.1	464.8	40.9	45.1	48.6
of which: profit available to organizations	168.7	120.7	172.5	18.1	15.0	18.0
amortization	184.5	199.3	244.4	19.8	24.8	25.5
attracted funds	552.0	440.0	492.0	59.1	54.9	51.4
including: banking credits	125.0	76.0	66.5	13.4	9.5	7.0
of which foreign banks credits	40.0	25.3	17.4	4.3	3.2	1.8
funds borrowed from other organizations	85.9	51.3	47.0	9.2	6.4	4.9
budget funds	121.5	103.3	127.6	13.0	12.9	13.3
of which: from the federal budget	37.9	44.2	51.9	4.1	5.5	5.4
from budgets of subjects of the Russian Federation	75.9	52.8	69.0	8.1	6.6	7.2
off-budget funds	2.1	1.6	3.4	0.2	0.2	0.3
other	217.5	207.8	247.5	23.3	25.9	25.9
of which: funds of overhead organizations	164.2	154.5	200.7	17.6	19.3	21.0
funds for participation in shared construction (from organizations and population)	20.3	16.1	17.3	2.2	2.0	1.8
of funds of population	8.4	7.8	10.6	0.9	1.0	1.1

Table 2, cont'd

	RUR billion			As percentage to the total		
	2009	2010	2011	2009	2010	2011
earnings from corporate bonds emission	0.1	0.02		0.01	0.0	
earnings from stocks emission	5.2	14.9	10.0	0.6	1.9	1.0
Foreign investments in the total volume of investments in fixed assets	62.9	46.2	36.4	6.7	5.8	3.8

Source: Federal State Statistics Service

The government demand for production and services of the Russian enterprises was supported through fulfillment of the planned investment projects in the sphere of transportation, telecommunication etc., realized within FTP and FTIP framework as well as through large-scale infrastructure projects.

In 2011 the construction, reconstruction, technical re-equipment and purchase of objects as well as fulfillment of measures (consolidated investment projects) (further referred to as objects) included in FTIP RUR 895bn of the federal budget was allocated, which is RUR 131bn more than in 2010, of which budget investments make RUR 769.6bn (RUR 726.7bn for financing of objects in federal ownership, RUR 42.9bn for financing of objects in the ownership of open joint-stock companies), and subsidies make RUR 125.4bn.¹

The funds envisaged for FTIP fulfillment in 2011 in part of financing the objects included in federal target programs RUR 551.1bn is envisaged (61.6% of the total FTIP volume), of which budget investments make RUR 461.0bn, subsidies – RUR -90.1bn, the sum of the state defense order being RUR 65.1bn. In 2011 the construction of objects not included in federal target programs is allotted with RUR 343.9bn, which makes 38.4% of the total FTIP volume, budget investments being RUR 308.6bn, subsidies – 35.3bn. The volume of the state defense order within the non-program part is equal to RUR 89.4bn.

In concordance with the federal targeted investment program for 2011 taking into account corrections as on May 1st, 2011 budget allotments for construction and purchase of 2569 objects were envisaged, 1390 objects were planned for commissioning. In January-April of this year 4 objects were commissioned, one of which – to the full extent, 3 objects - partially, 2 of which are envisaged for commissioning in forthcoming years. As on May 1, 2011 638 objects were financed to the full extent, 348 objects were characterized by extent of technical readiness within 51.0% to 99.9%.

Table 3

OBJECTS ENVISAGED FOR TARGETED INVESTMENT PROGRAM AND OBJECTS OF STATE INVESTMENTS IN 2011 (EXCLUDING CONSTRUCTION SIGHTS AND OBJECTS INCLUDED IN STATE DEFENSE ORDER)

	Number of objects in 2011		Put into commission in January-April 2011		Limit of state investments in 2011		Financed from the federal budget in April-May 2011	Investments used at the expense of all sources of financing in April-May 2011
	total	with the deadline of implementation in 2011	to full extent	partially	total	from the federal budget		
	Units				RUR billion			
Total	2569	1390	1	3	731.7	671.4	230.9	61.5
including: transportation complex	536	314	1	-	287.2	246.6	132.2	33.4

¹ Starting with 2011 FTIP includes not only the objects of state-owned property of the Russian Federation and property of legal entities that are not government or municipal bodies but also capital constructions objects in the property of subjects of the Russian Federation and in the municipal property the construction of which are co-financed by the subsidies from the federal budget

Table 3, cont'd

	Number of objects in 2011		Put into commission in January-April 2011		Limit of state investments in 2011		Financed from the federal budget in April-May 2011	Investments used at the expense of all sources of financing in April-May 2011
	total	with the deadline of implementation in 2011	to full extent	partially	total	from the federal budget		
	Units				RUR billion			
agriculture complex	181	96	-	-	8.3	8.0	3.6	0.4
special complex	558	357	-	-	50.7	48.7	8.2	2.1
social complex	1126	568	-	3	336.3	325.3	83.0	22.8
other objects	168	55	-	-	49.2	42.8	3.9	2.9

Source: Federal State Statistics Service

In January-April 2011 RUR 230.9bn (34.4% of the total volume of funds envisaged for the year) of the year limit was financed from the federal budget and RUR 10.1bn – from the budgets of subjects of the Russian Federation and other sources. The government customers used RUR 61.5bn from all the sources of financing or 8.4% of the annual limit of funds envisaged for construction.

The annual limit of state investments in transportation (53.6%) and agriculture (45.0%) complexes is financed at a considerably higher level than the average for construction sights and objects for government purposes. Budget allotments to the special complex are financed at the level of 16.8% and to the social complex- at the level of 25.5%. low indices of the use budget allotments envisaged for FTIP fulfillment in January-April 2011 are accounted for by the fact that at the beginning of the year the works connected with contests and agreements signing with the contractors were still in progress. The structure of investments in fixed assets as broken by the types of economic activities was subject to considerable changes in 2009-2011.

Table 4

INVESTMENTS IN FIXED ASSETS (NOT TAKING INTO ACCOUNT SUBJECTS OF SMALL-SCALE ENTREPRENEURSHIP AND THE VOLUME OF INVESTMENTS NO DETECTED BY DIRECT STATISTICAL METHODS) IN THE 1ST QUARTER 2009-2011

	RUR billion			As percentage to the total			Growth rates versus the corresponding period of the previous year		
	2009	2010	2011	2009	2010	2011	2009	2010	2011
Total	933.3	802.1	956.8	100	100	100	95	78.9	101.9
agriculture, hunting and forestry	26.7	26.9	29.1	2.9	3.4	3.0	74.8	100.8	107.8
fishing, fish breeding	0.4	0.4	1.0	0.04	0.1	0.1	85.8	107.3	194.4
industry	439	415	473.9	47.1	51.7	49.5			
minerals extraction	192.9	180.4	211.5	20.7	22.4	22.1	90.7	89.9	107.5
manufacturing industries	178.2	141.8	170.8	19.1	17.7	17.9	97.8	78.6	104.7
electricity production and distribution	67.9	92.8	91.6	7.3	11.6	9.6	100.6	122.6	87.2
construction	29.5	19.8	22.3	3.2	2.5	2.3	97.5	70.3	96.7
wholesale and retail trade	25.9	15.7	26.4	2.7	2.0	2.7	96.2	84.2	129.7
hotels and restaurants	2.8	4.2	4.5	0.3	0.5	0.5	89.9	141.2	94.7
transportation and communication	238.6	194.4	252.0	25.6	24.2	26.3	105.4	76.5	113.0
railway transportation	28.3	54.6	51.0	3	6.8	5.3	61.4	130.7	87.8
pipelines transportation	124	69	106.0	13.3	8.6	11.1	147.4	55.1	125.8
communication	28.3	24.9	28.8	3	3.1	3.0	75	82.8	107.9

Table 4, cont'd

	RUR billion			As percentage to the total			Growth rates versus the corresponding period of the previous year		
	2009	2010	2011	2009	2010	2011	2009	2010	2011
financial activity	14.2	8.6	12.8	1.5	1.1	1.3	135.3	61.4	129.6
operations with real estate	95.3	70.6	70.5	10.2	8.8	7.4	76	66.7	87.5
state management	10.2	10.1	7.5	1.1	1.2	0.8	106.7	81.5	85.7
education	10.6	10.4	14.2	1.1	1.3	1.5	80.9	97	124.3
health care and social services rendering	14	12.1	14.8	1.5	1.5	1.6	93.2	83.8	115.8

Source: Federal State Statistics Service

In the 1st quarter 2011 the proportion of investment resources in the industry made 49.5% of the total volume of the investments in fixed assets in the economy. The change in the structure of the investments in industry in the current year was accompanied with the anticipating growth of investments in minerals extraction as compared with manufacturing industries (*table 4*). In contrast to the corresponding periods of the previous two years the growth rates of investments in electricity, gas and water production and distribution reduced, exceeding however by 7.5% the figures of favorable pre-crisis period of 2008. Among the manufacturing industries it is metallurgy and machine-building complexes, which have not overcome the aftermath of the acute crisis of 2008-2009 yet, that are characterized by the highest growth rates of investments in fixed assets.

In the 1st quarter 2011 the proportion of transportation and communication accounted for 23.3% and 3.0% of the total volume of investments, correspondingly. The absolute volumes of transportation financing in the 1st quarter 2011 went up by RUR 53.7bn versus the corresponding period of the previous year. In the 1st quarter 2011 it was the growth of investments in pipeline transportation by 25.8% that had a prevailing influence on the recovery of the positive dynamics of investments in transportation development.

In concordance with scenario conditions of Russia's socio and economic development for 2012-2014 the expected growth of investments will make 106.0% and of GDP – 104.2% in 2011. The revival of investment activity is expected to start in 2012: investments growth rates are forecast at the level of 108.8% in 2012 and 109.6% in 2013, gross capital formation in the GDP is expected to grow from 21.4% in 2010 to 25%.

It is expected at the same time that the improvement of investment climate and fulfillment of the government policy measures aimed at the increase of business efficiency will result in proportion of own funds of private-owned organization directed to investments will not sink to pre-crisis level and the investments in technical re-equipment and production development will still have high priority in the strategic development of companies. It should be noted that the forecast anticipating growth of investment import as compared with the dynamics of investments in fixed assets is a logical continuation of the recent years' trends and testifies that the domestic production of investment goods has been developing at insufficiently high rates.

In 2012-2014 it is oil and gas complex and infrastructure industries that will make a determining contribution into the growth of investments in fixed assets. In 2011-2013 investments in transportation complex (excluding pipeline transportation) are estimated to grow at 4.9%-6.1% per year, increasing by more than 10% in 2014 in case the corresponding budget decisions are adopted. By 2013 and 2013 the growth in manufacturing industries will intensify. The investments in fixed assets growth rates in the sphere of services (financial sphere, trade, real estate) will not reach pre-crisis level in 2011, but by the end of the forecast period they may increase by 12-18% a year. In the social sphere the proportion of off-budget sources in the investments in fixed assets will expand, their growth rates possibly accelerating to 5.5-6.5% a year by 2014. ●

FOREIGN INVESTMENTS

E.Ilukhia

• **At the beginning of 2011 foreign investments into the Russian Federation increased. A considerable growth of the segment of other investments, made on a repayable basis, has resulted in the decrease of direct investments proportion in the aggregated structure of foreign investments to 8.8%.**

• **The same as in the previous year, the volume of the exported capital in January– March of the current year was nearly equal to the volume of the foreign investments attracted over the period.**

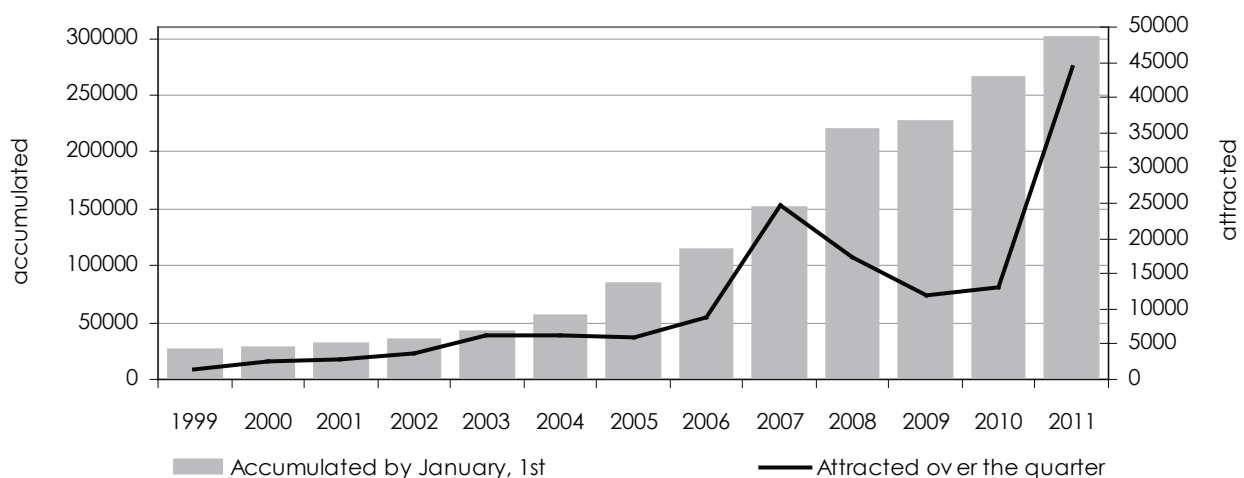
• **Financial activity became the most attractive sphere for foreign investors. The second place is now occupied by the industry, which forced transportation and communication back to the third position. Foreign investments in fossil fuels production grew at anticipating rates as compared with the processing industries.**

• **As to geographical structure, the largest volume of investment that was received by the Russian Federation in the 1st quarter 2011 was directed from Switzerland, which accounted for 54.2% of the total foreign investments in the Russian economy.**

The volume of foreign investments attracted in the 1st quarter 2011 by non– financial sector of the Russian economy not taking into account monetary and crediting regulating institutions, commercial and savings banks, including ruble investments recalculated in US dollars made \$44.3bn, which is by 3.4 times more than the figure of the 1st quarter 2010 (fig. 1).

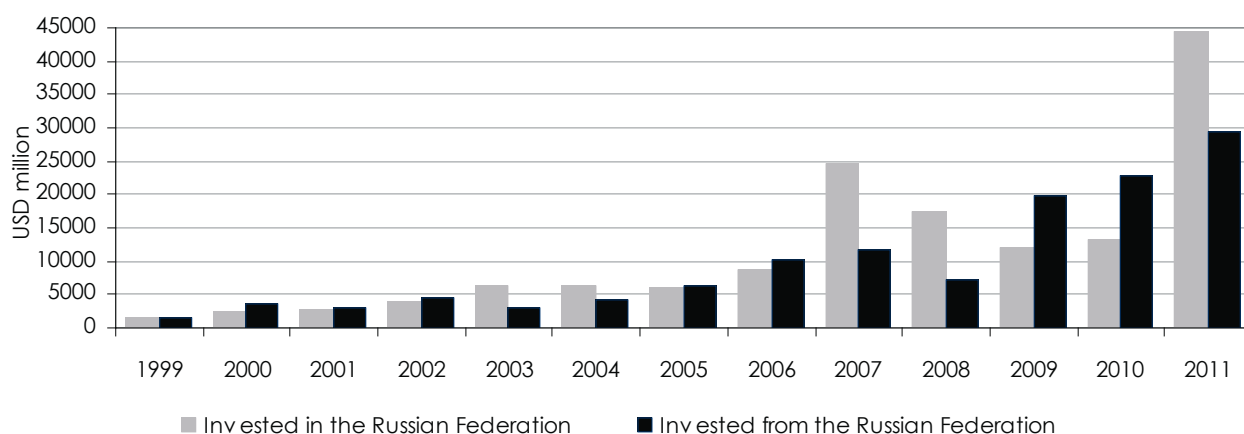
In the 1st quarter 2011 \$41.0b was exported from the Russian Federation in the form of profits of foreign investors transferred abroad as well as interest rates for credits and credit repayments, which is 3.1 times higher than the corresponding figure of 2010. Investments to foreign countries from Russia made 66.2% of the total volume of foreign investments in the Russian economy (in the 1st quarter 2010 the investments abroad were estimated to exceed foreign investments in the Russian economy by 74.2%).

In the 1st quarter of the current year the segment of the received direct investments was observed to grow by 48.3% versus the 1st quarter 2010 (up to \$3.9bn). IN the 1st quarter 2010 the decrease was estimated to be 17.6%. Portfolio investments as a result of January– March 2011 reduced by 58.3% (to \$122m), while in the 1st quarter 2010 their volume doubled. The segment of other investments expanded by 3.9 times up to \$40.3bn, the growth of other investments in the 1st quarter 2010 being 17.1%.



Source: Federal State Statistics Service

Fig. 1. Foreign Investments in the Russian Economy in the 1st Quarter 1999-2011, USD m



Source: Federal State Statistics Service

Fig. 2. Foreign Investments in the Russian Federation and Investments Abroad from the Russian Federation in the 1st Quarter 1999-2011

Decrease of portfolio investments and considerable growth of other foreign investments in the 1st quarter of the current year the growth rates of direct investments being lower resulted in a considerable change in the structure of aggregated investments in the Russian economy (table 1).

Table 1

STRUCTURE OF FOREIGN INVESTMENTS IN THE RUSSIAN FEDERATION
IN THE 1ST QUARTER 2005– 2011, AS PERCENTAGE

	2005	2006	2007	2008	2009	2010	2011
Direct investments	31.9	43.7	39.5	32.4	26.4	20.0	8.8
Portfolio investments	1.3	2.6	0.8	0.7	1.0	2.2	0.3
Other investments	66.8	53.6	59.6	66.9	72.6	77.8	90.9

Source: Federal State Statistics Service

Speaking about direct investments it should be noted that after two– year fall in contributions to the statutory capital of enterprises in the territory of the Russian Federation in the first quarters of the year, in January– March of the current year the contributions went up by 37.6% versus the corresponding period of the previous year. Their proportion in the structure of direct foreign investments decreased to 47.4% (51.0% in the 1st quarter 2010). Credit component of direct investments expanded by 77.5% (up to \$1.7bn). The proportion of credits received from the organizations' foreign co– owners increased to 44.8% (37.4% in the 1st quarter 2010).

The volume of trade credits went up to 47.0%. Their proportion in the total volume of other investments decreased to 12.3% (33.0% in the 1st quarter 2010). The volume of other credits, which made 85.6% of the total volume of other foreign investments in the Russian economy (58.0% in the 1st quarter 2010), increased by 5.8 times as compared with the 1st quarter 2010. The sum of short– term credits granted for the period of less than 180 days in their structure increased by 16.3 times.

As to the sector structure of foreign investments, the largest volume of them is directed into financial activity, whose share in the aggregated structure went up to 56.5%, the absolute values of foreign investments in the sphere increasing by \$24.1bn. The second place according to attraction to foreign investors was occupied by the industry in which foreign investors invested by 27.6% more funds than in the 1st quarter 2010. In absolute terms the growth made \$2.2bn. Investments in trade, transportation and communication increased by \$2.1bn. In the 1st quarter of the current year the most profound relative decrease of foreign investments was observed in construction, in which sector the volume of foreign investments is estimated to be \$96m (table 2).

In the industrial sector this year a considerable growth of investments in fossil fuels extraction was observed. As a result of the 1st quarter 2011 they made \$4.5bn, which is 80.6% above the level of the 1st quarter 2010. On the whole foreign investments in extractive industry went up by 81.5% versus the 1st quarter 2010 up to \$4.7bn.

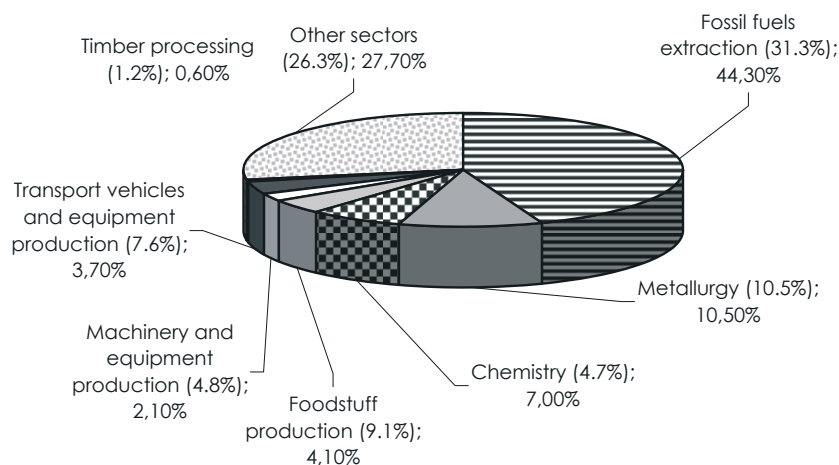
Table 2

STRUCTURE OF FOREIGN INVESTMENTS IN THE RUSSIAN ECONOMY AS BROKEN BY SECTORS
IN THE 1ST QUARTER 2009– 2011

	As USD million			As percentage to the total			Change versus the corresponding period of the previous year, %		
	2009	2010	2011	2009	2010	2011	2009	2010	2011
Industry	6 297	8 025	10 240	52.3	61.0	23.1	74.6	127.4	127.6
Construction	176	228	96	1.5	1.7	0.2	37.1	129.5	42.1
Transportation and communication	1 276	1 513	3 632	10.6	11.5	8.2	Б 3.5 p.	118.6	240.1
Wholesale and retail trade	2 605	1 407	3 503	21.7	10.7	7.9	47.6	54.0	249.0
Operations with real estate, rent and services rendering	1 124	922	1 585	9.3	7.0	3.6	63.2	82.0	171.9
Financial activity	332	925	25 072	2.8	7.0	56.5	64.7	278.6	2710.5
Other sectors	221	126	221	1.8	1.1	0.5	105.2	57.0	175.4

Source: Federal State Statistics Service

The volume of foreign investments in the Russian manufacturing industries in January– March of the current year increased as compared with the 1st quarter 2010 by 2.8% (up to \$5.5bn). As to manufacturing industries, in the 1st quarter 2011 investments directed in coke and oil products production went up by 28.6% versus the corresponding period of 2010 (up to \$1.7bn), in chemistry—by 88.2% (up to \$717m). The volume of foreign investments in metallurgy, foodstuffs production, machine building, and transportation vehicles and equipment construction decrease by cocorrespondingly 0.7%, 4.7%, 43.5% and 36.9%. Diversified dynamics of foreign investments as broken by sectors of industry affected the structure foreign investments in the industry (*fig. 3*).



Source: Federal State Statistics Service

Fig. 3. Structure of Foreign Investments in Industry in the 1st quarter 2011 as Broken by Sectors (data for the 1st quarter 2011 are given in parentheses)

Against the background of a considerable growth of the total volumes of foreign investments in extractive industry direct investments in this sector increased by 4.4 times as compared with the 1st quarter 2010 making \$2.1bn. Other investments in this sector over the period under consideration went up by 24.0%, which resulted in the expansion of direct investments proportion in total investments in extractive industry from 17.9% to 43.4% and reduction of the proportion of other investments from 82.1% to 56.1%.

In the 1st quarter 2011 the direct investments in manufacturing industries reduced by 25.8% as compared with the corresponding figure of the previous year, other investments increasing by 12.5%, which resulted in the decrease in the proportion of the direct investments in the structure of foreign investments in manufacturing industries from 19.9% to 14.4% and expansion of the share of other investments from 77.7% to 85.0%. Portfolio foreign investments in the sector reduced by 74.2% (from \$ 128m to \$33m), their share in the aggregated structure of foreign

investments in manufacturing industries remaining insignificant – 0.6% (2.4% in January–March 2010).

Structure of foreign investments directed into the industry differs from the corresponding structure of foreign investments in the Russian economy by a considerably higher proportion of direct investments. In January– March of the current year direct investments in the industry increased by 86.2%, while other investments in the industry went up by only 15.2%, which resulted in the expansion of the share of direct investments in the structure of foreign investments in the industry (*table 3*).

Table 3

STRUCTURE OF FOREIGN INVESTMENTS IN INDUSTRY IN THE 1ST QUARTER 2005– 2011, %

	2005	2006	2007	2008	2009	2010	2011
Direct investments	43.2	56.2	70.3	46.0	30.4	19.1	27.9
Portfolio investments	2.2	3.5	1.0	1.2	0.1	1.6	0.5
Other investments	54.5	40.3	28.7	52.8	69.5	79.3	71.6

Source: Federal State Statistics Service

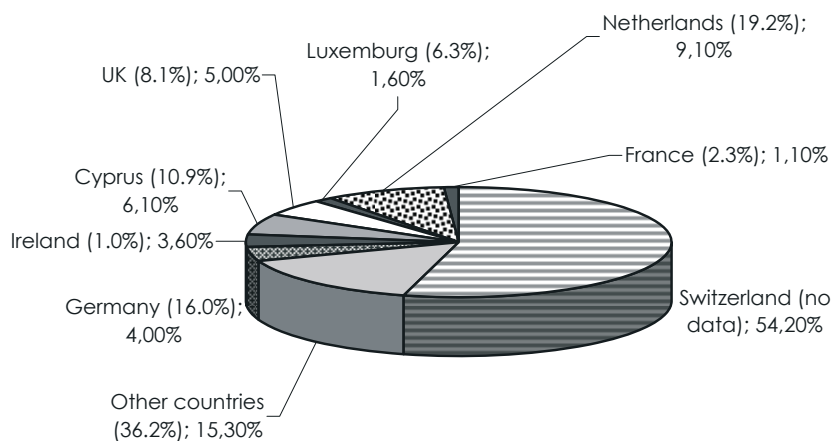
Direct investments in the industry in the 1st quarter 2011 made 73.4% of the total direct foreign investments in the Russian economy (58.5% in the 1st quarter 2010). The proportion of portfolio and other investments in the industry the corresponding total investments figure is estimated to be 46.0% and 18.2% (43.7% and 62.2%, correspondingly, in the 1st quarter 2010). In the 1st quarter 2011 five leading countries investing in the Russian economy include Switzerland, Netherlands, Cyprus and Germany, which accounted for 78.4% of the foreign investments received by the Russian Federation (in the 1st quarter 2010 five leading investing countries investments accounted for 60.5%) (*fig. 4*).

It is Switzerland that holds the leading position among the countries investing in the Russian Federation – its investments in the Russian economy made more than \$24bn. The investors from Switzerland are mainly interested in financial activity. Switzerland accounted for 95.9% of the total foreign investments in this sector I the 1st quarter 2011.

In January– March of the current year investments from the Netherlands in the Russian Federation went up by 59.5% (up to \$4.0bn) as compared with the corresponding period of 2010. Fossil fuels production received \$1.7bn of Netherland investments (43.6% of the total investments of the country in the Russian economy and 38.7% of the total foreign investments in the sector), communication – \$1.5bn

(37.7% and 44.7%). In the 1st quarter 2010 the major part of investments from the Netherlands (about \$1.0 bn or 41.1% of the total investments from the Netherlands into the Russian Federation) was directed into communication, making 69.3% of the total foreign investments in the sector.

The highest rates of investments growth in the 1st quarter 2011 are characteristic for Ireland (by 11.8 times as compared with the 1st quarter 2010). In the current year the prevailing part of the investments from Ireland into the economy of the Russian Federation, which made \$1.6bn, was directed into communication – \$1.5bn (95.1% of the total investments of the country into the Russian Federation).



Source: Federal State Statistics Service (data for Switzerland investments were not cited by the Federal State Statistics Service in the 1st quarter 2010 and were included in “other countries”).

Fig. 4. Geographic structure of Foreign Investments Attracted into the Russian Federation in the 1st Quarter 2011 (data for the 1st quarter 2010 are given in parentheses).

Investors from the Cyprus have increased the volume of investments in the Russian economy to \$2.7bn in January– March 2011 (+88.9% versus the corresponding figure of the 1st quarter 2010), the main sphere of attraction being the trade, in which \$1.3bn was directed (49.1% of country's investments in the Russian Federation), operations with real estate – \$533m (19.7%) and metallurgy – \$119m (4.4%).

The UK has increased its investments in the Russian Federation by 2.1 times (up to \$2.2bn), giving preference to fossil fuel extraction. This industry accounted for 39.2% of investments in the Russian economy from the UK. Besides, UK investors showed interest to coke and oil products production (\$780m, or 34.9% of the total investments in the Russian Federation from the country) and operations with real estate (\$469m, or 21.0%).

In January– March 2011 the most pronounced decrease of investments from the leading investing countries into the Russian economy was observed from Japan, Germany and Luxemburg: reduction versus the same period of the previous year made, correspondingly, 32.0%, 16.3% and 12.8%. The absolute figure of investments in the Russian economy from these countries was at the level of \$215m, \$1.76bn and \$726m, correspondingly as a result of the 1st quarter of the current year.

Thus year investors from Germany showed particular interest to fossil fuels extraction, investing \$667m in this sector (37.8% of Germany's investments in the Russian Federation), trade – \$42m (24.3%) and metallurgy – \$212m (12.0%).

On the whole, at the end of March 2011, the volume of accumulated foreign investments in the Russian economy reached \$301.1bn, which is by 13.3% above the figure of the end of March 2010 and by 0.3% above the level of inflation, registered on January, 1st of the current year.

Table 4

STRUCTURE OF ACCUMULATED FOREIGN INVESTMENTS AS BROKEN BY MAIN INVESTING COUNTRIES

	Accumulated by 01.04.2011, USD m				Change by 01.01.2011, %			
	Total	Direct	Portfolio	Other	Total	Direct	Portfolio	Other
Ireland	12775	564	5	12206	111.2	99.3	125.0	111.8
Germany	27852	11096	27	16729	100.1	119.9	245.5	90.1
Japan	9190	887	4	8299	101.9	107.6	200.0	101.3
UK	20744	2879	4502	13363	96.1	82.2	100.5	98.3
Cyprus	64205	46899	1618	15688	103.6	104.8	93.4	101.3
Netherlands	41706	24540	27	17139	103.3	109.5	337.5	95.4
Luxemburg	34031	578	155	33298	96.8	87.4	76.4	97.1
China	26735	1135	1	25599	95.7	120.5	1000.0	94.8
Other countries	63874	31685	2552	29637	98.7	95.1	102.9	102.4
Total	301112	120263	8891	171958	100.3	103.5	99.7	98.3

Source: Federal State Statistics Service.

FOREIGN TRADE

N.Volovik, K.Kharina

The main volume-wise indicators of Russia's foreign trade kept growing in April 2011 vis-a-vis respective indicators of 2010. Since July 1, 2011, Russia has lifted the ban on grain export. In June, the Government imposed a series of bans on import of food products.

In April 2011, Russia's foreign trade turnover calculated by the balance-of-payments methodology accounted for \$72.9bn, or up by 38.5% vs. April 2010. Exports grew by 37.6% on a year-on-year basis, while imports added 39.9%. The nation's balance of foreign trade hits its peak value for the whole period of observations and accounted for \$19.3bn, or up by 34% on a year-on-year basis. As export prices were increasing faster than those of import supplies, the nation enjoyed favorable foreign trade conditions in April 2011. The trade conditions index hit 117.3.

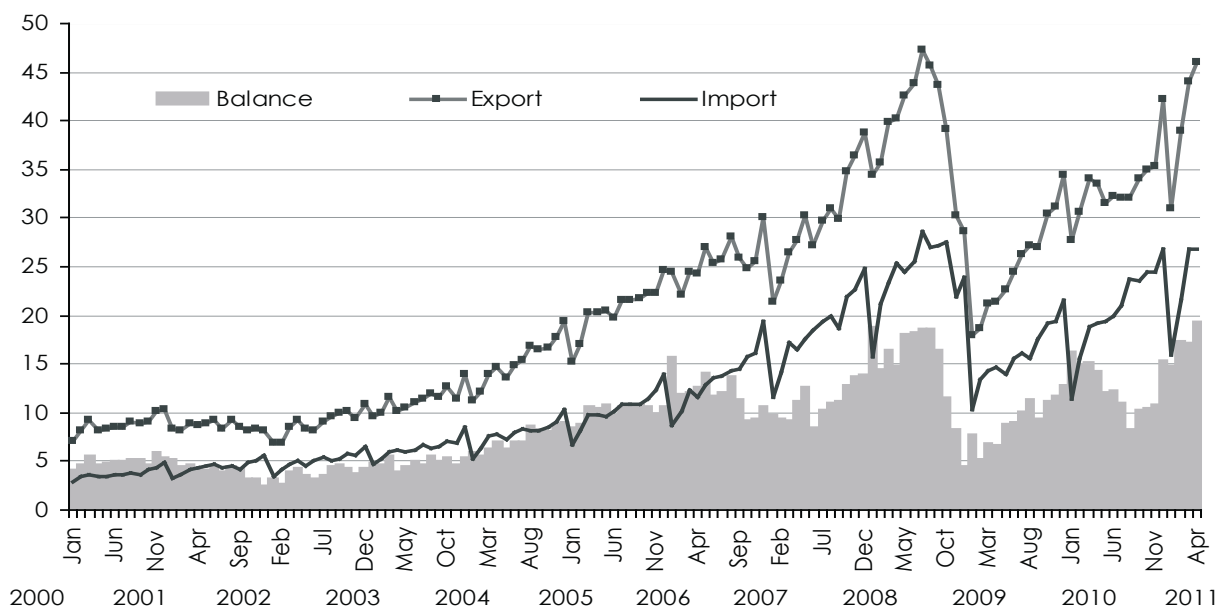
Table 1

AVERAGE WORLD PRICES IN APRIL OF RESPECTIVE YEARS

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Oil (Brent), USD/bbl	22.97	26.26	25.81	24.79	33.5	50.6	68	68.32	108.26	51.51	85.67	122.30
Natural gas, USD/MMBTU	3.052	5.200	3.408	5.390	5.785	7.422	7.964	7.67	10.32	3.604	5.23	4.91
Gasoline, USD /gall	0.808	0.999	0.814	0.855	1.152	1.603	2.016	2.13	2.884	1.459	2.321	3.24
Copper, USD/t	1710.1	1689.4	1620.8	1598.5	2950	3395	6370	7766.5	8684.9	4406.6	7745.1	9483.3
Aluminum, USD/t	1448.0	1493.7	1370.3	1332.8	1734	1894	2620	2814.8	2959.3	1420.9	2316.7	2662.6
Nickel, USD/t	9657.1	6303.1	6940.6	7915.3	12872	16142	17935	50267	28763	11166	26031	26329

Source: calculated on the basis of the LME and IOE data (London).

The global markets for food products and minerals saw the price rally continue in April 2011: specifically, the price of Urals made \$119.4/ b., or up by 44.7% vs. April 2010 and up by 7.4% vs. March 2011. The Urals price between January and April 2011 averaged \$106.3/b. and beat the record-breaking index of the first four months of the pre-crisis 2008.



Source: CBR

Fig. 1. Main Indicators of Russia's Foreign Trade (as \$bn)

The average oil price over the period of monitoring between 15 May and 14 June 2011 accounted for \$112.65 /b. Consequently, in compliance with Resolution of the RF Government of 22 June 2011 №94 the export duty on oil should be lowered by \$17 (3.68%) – from \$462.1/t to \$445.1/t., effective as of 1 July 2011, while the preferential duty will make up USD 205./t vs. 217.5/t in the prior month. This lowering of the duties became the first one this year, as it was in July 2010 when the export duty rate for oil and oil products was lowered the last time. After that, following oil prices, it has been raised permanently, and increased roughly by \$200 over the past 12 months.

The export duty on black oil products will make up \$207.8/t (\$215.8 t in June), while that on light oil products will be \$298.2/t (vs. \$309.6/t in June). The increased duty on gasoline will be retained and since 1 July 2011 will make up \$400.5/t.

In late June, the leadership of the IEA in coordination with the US Administration ruled to release 60m barrels of oil out of its reserves. The oil will be supplied onto the market in an amount of 2m barrels a day, including 30m barrels of oil supplied out of the US's strategic reserves. According to IEA, since the beginning of the civil war in Libya, the global economy has been short of some 132m barrels of oil, which triggered the price rise for crude. The IEA's move aims to stop the global price rise for oil, which continued after OPEC, at its Summit on 8 June 2011, failed to come to terms on an increase in quotas on oil production, as championed by Saudis and some other nations of the Persian Gulf. As a result, having hit its monthly peak of \$120/b on 14 June, Brent prices slid on 27 June to their 4-month low - down to \$104.09/b.

The world prices for non-ferrous metals still were on a high level. In April 2011, aluminum was traded at LME at 14.9% higher than in April 2010, while copper added 22.4% and nickel – 1.1%.

The CBR data suggest that between January and April 2011 Russia's foreign trade turnover stood at \$251.5bn (up by 131.9% on a year-on-year basis), including exports – \$160.2bn (up by 127.4%) and imports– \$91.4bn (up by 140.8%). The balance of foreign trade remained positive and accounted for \$68.8bn (\$60.9bn in January-April 2010; \$64.7bn in January-April 2008).

Because of imposition of embargo on grain export last summer, the proportion of food products and agricultural raw materials in the structure of Russia's export tumbled from 2.7% reported over the period between January and April 2010 down to 1.4% in the same period this year. The ban was lifted on July 1. In the 2009–2010 season, Russia's grain export accounted for over 21m t.n, while in this marketing season of 2010-2011 it will make up a. 4m t. Such a dramatic fall should be ascribed to the last year's draught, which compelled the Government to temporarily ban export of wheat, barley, rye, corn and flour effective as of 15 August 2010. The ban was first effective through 31 December 2010, but it was subsequently extended until 30 June 2011, with just flour having been crossed out of the list. The global grain market sees a significant price rise: specifically, in April 2011, global prices of Canadian wheat soared by 74.1%, while the ones for the US HRW – by 84.2% on a year-on-year basis.

The FAO projects the 2011 global wheat harvest to be at 3.2% greater than last year, in large part due to good prospects of the Russian harvest vis-a-vis the last year's poor one. The global production of feeding grain should surge by 3.9%, thus beating the record-breaking 2008 figures.

The RF Ministry of Agriculture's forecasts suggest that this year Russia should harvest some 85m ton of grain. Given the carry-over grain inventories of 17m t., not only will the country meet the domestic demand (69m ton), but it will be able to export grain, for its traditional customers – that is, Middle East and North African nations and Egypt in particular, -have retained their interest in Russian grain. In the short run, grain supplies from Russia can make up 2-2.5m t. and by the end of the year hit the level of 15m t.

Between January and April 2011 the import pattern kept seeing an increase in the proportion of machinery, equipment and means of transportation against a plunge in the share of other groups of imports. While import of food products and agricultural raw materials posted a 33.5% increase over the first 4 months 2011 compared to the same period of 2010, the proportion of this specific group of goods slid from 17.8% in January-April 2010 down to 16% in the respective period 2011. The pace of increase of import of these goods should slow down in the near future, as various prohibitive measures are going to take effect shortly.

On 2 June, Rospotrebnadzor imposed a ban on import of all vegetables from EU, due to the outbreak of an enteric infection first in Northern Germany and then throughout Europe. On 22

June, Russia and EU agreed on a special regime of granting access to European vegetables to the Russian market – namely until the ban is lifted, European laboratories will be running safety tests before shipping vegetables to Russia. The special regime will remain effective until there are no new cases of the enteric infection.

On results of monitoring of microbiological safety of meat products imported into Russia in the 1st half 2011, Rosselkhoznadzor imposed restrictions on certain supplies into the country. Because of an unduly control over compliance with veterinary and sanitary requirements, since 15 June Russia banned import of meat products from 80 Brazilian companies. Rosselkhoznadzor experts conducted a selective inspection of 29 local meat-processing plants back in April and found out that none of them met standards and requirements set by Russia and the Customs Union. Brazil is one of the largest exporters of meat products to Russia: between January and April 2011 the aggregate import of deep-frozen beef in Russia accounted for 153,000 tons, pork- 182,000 tons and poultry – 72,000 tons, and Brazil's share therein accounted for 40, 28.4 and 27.9%, respectively. Rosselkhoznadzor also imposed a temporary ban on supplies of meat products from certain facilities in Germany, Belgium, Spain, Holland, and Sweden, for after testing for E.coli they all proved positive.

The temporary ban on meat import, which came in effect after exposing infected shipments of meat from a series of meat-processing plants in 19 countries worldwide, including 10 EU nations, is still there. The authorities explained their move to extend the ban by the fact that animal products are more prone to catching microbes in the course of slaughtering and butchering and thus fall under the category of high-risk products.

The inspection Rosselkhoznadzor experts ran together with representatives of the German veterinary authority between 10 and 22 April 2011 failed to prove that local companies complied in full with veterinary and sanitary standards and requirements of RF and the Customs Union. Because of that, Rosselkhoznadzor considered it necessary to undertake urgent measures to prevent importation of potentially perilous products in RF. Since 27 June, Rosselkhoznadzor imposed a temporary ban on shipments in Russia of products from 10 dairy and 3 meat-processing plants in Germany. In addition, there still are temporary restrictions on import of poultry from yet another poultry ranch. The bans were imposed because of an exposure at a number of German facilities of systemic drawbacks in ensuring control over safety of products exported in Russia and the Customs Union.

With its Resolution of 3 June 2011 №445 the RF Government ruled to introduce a special import duty on hard boiling since 8 July 2011 in an amount of \$294.1/t. The protective import duty will remain in effect for three years on, and it will be applied to candy glasses, toffee and other kinds of hard boiling from all the countries but the Custom Union member states (Belarus and Kazakhstan) and countries enjoying Russia's national system of preferences (except for China and Turkey).

The ban followed an investigation by the RF Ministry of Industry and Trade back in 2010. The investigation revealed a drastic increase in the proportion of import hard boiling: between 2006 and 2009 import supplies of hard boiling rose 3.1 times against a 8.8% contraction in the national market for hard boiling, a 15.1% fall in the volume of its production and a 16.1% plunge in its sales. These negative tendencies led to domestic producers being driven away from the national market: between 2006 and 2009 the proportion of domestically produced hard boiling plummeted 7.8 p. p. The domestic production-to-import ratio dwindled 3.6 times.

In 2006, it was EU nations which held a lion's share of hard boiling supplies. In 2009, Ukraine boosted its domestic production more than 17-fold and became a major supplier of hard boiling to Russia – its share in the total volume of import in Russia increased from 10.8% in 2006 to 60.7% in 2009. It is planned that the special duty should practically close the Russian market for Ukrainian hard boiling. This is the third time Russia introduces a special duty on Ukrainian hard boiling, after the same moves in 2001 and 2005. ●

STATE BUDGET

E.Fomina

• **Adoption of new decisions on the expansion of the budget for social obligations make the task of reducing the budget deficit more difficult, increasing pressure on the budget system.** The scope of federal spending in 2011 was increased by 364 bn rubles. (in June relevant amendments were adopted to the Budget Law), the major part of them will be addressed to social needs. With worsening of macroeconomic situation, a significant amount of budget spending, already extended in the crisis period of 2008-2009 will become a heavy burden for the national budgetary system in future.

• **The debt policy adjustment in the direction of borrowing growth will inevitably be the next step in expansion of the budget expenditures, whereas the amount of domestic debt is already estimated at about 10 per cent of GDP.**

Analysis of the main parameters

of the expanded government budget execution in January – April 2011.

In June 2011, preliminary results of the execution of the expanded government were assessed for January-April of 2011 of the current year. The volume of the revenues of the budget has decreased against the level of the relevant period of 2010 by 1.3 percentage points of GDP¹. Herewith, the expenditure part of the budget in relative terms has been reduced by 2.9 p.p. of GDP, whereas in absolute terms the expenditures have grown by approximately Rb70.3 bn. As a result, the budget of the expanded government has been executed with a significant surplus of 7.4 of GDP, which is by 0.1 p.p. of GDP lower than in the relevant period of 2010 (See *Table 1*).

Table 1

EXECUTION OF THE BUDGETS OF ALL GOVERNMENT LEVELS IN TERMS OF REVENUE AND EXPENDITURES IN JANUARY-APRIL 2010-2011

	January– April 2011		January– April 2010		Change, against GDP, p.p.
	Rb, bn	GDP, %	Rb, bn	GDP, %	
Federal budget					
Revenues	3 339.7	21.3	2 618.3	20.0	+1.3
Expenditures	3 176.6	20.3	3 030.5	23.1	–2.8
Deficit (–) /Surplus (+)	163.1	+1.0	–412.2	–3.1	+4.1
Consolidated budgets of the RF Subjects					
Revenues	2 511.7	16.0	2 177.8	16.6	–0.6
Expenditures	1 808.0	11.5	1 664.4	12.7	–1.2
Deficit (–) /Surplus (+)	+703.7	+4.5	+513.4	+3.9	+0.6
Budget of expanded government					
Revenues	6 326.0	40.3	4 998.9	38.1	+2.2
Expenditures	5 153.7	32.9	4 689.9	35.8	–2.9
Deficit (–) /Surplus (+)	+1 172.4	+7.4*	+30909	+2.3	+5.1
For reference: GDP, Rb, bn	15 682.0		13 115.9		

* A significant surplus of the budget of the expanded government as against the surplus of the federal budget and budgets of the RF Subjects can be explained by the change since 2001 in the procedure for crediting of funds to extra-budgetary funds, bypassing the federal budget as it was done before.

Source: The Ministry of Finance of the Russian Federation, assessments of Gaidar Institute

1 When analyzing the volume of revenues to the budget of the country one should consider revenue from investment income from funds management of oil and gas assets in 2009-2010 in the amount of 275.2 billion rubles and 134 billion rubles, respectively.

Consolidated budget of the Subjects of the Russian Federation over the first four months of 2011 was also executed with a surplus of 4.5 per cent of GDP against 3.9 per cent of GDP over the relevant period of 2010. Growth of the budget surpluses of the RF subjects in both, relative terms and in absolute value was due to a lower expenditure rate of the budget funds against available resources. Thus, on May 1, there were expended about 24.6 per cent (against 26.8 per cent in 2010) against the expenditures approved by the consolidated budgetary estimates for 2011.

Sustained consolidated budget surplus of the RF subjects allows to start with the formation of regional reserve funds, which analogs are successfully operating in separate administrative territorial units of the US and Canada. In Russia, the establishment of reserve funds in the subjects of the Russian Federation was introduced in 2009 (the Budget Code was supplemented with Art. 81.1). The purpose of such fund, as well as the Federal Reserve Fund is smoothing of adverse volatility in the period of significant growth in the budget balance. However, in conditions of instability of income expenditure components and unpredictability of regional budgets in a crisis of direction of the formation of such a fund would be extremely difficult. In the current climate of budget surpluses in the execution of regional budgets it would be appropriate to address this problem.

The growth of expanded government budget revenue (Table 2) largely depend on the increased oil and gas revenues.

Revenue from mineral extraction tax (MET) and income from foreign economic activity over January-April 2011 increased by 0.4-0.5 percentage points of GDP for each of those taxes. The basic grounds for higher tax collection level in both, absolute and relative terms were provided by the growth of global oil prices against the relevant period of 2010 (\$108 per barrel against \$76 per barrel). According to experts, at present oil prices are approaching their historic peak, and it is extremely dangerous to be guided by the current favorable conditions for the choice of strategy for fiscal policy. In the medium term, one should expect more moderate prices. Thus, under the baseline scenario of the Ministry of Economic Development of Russia in 2012 - 2014 oil price in international commodity markets should not exceed \$93-97 / barrel¹. At the same time, assessments of other oil-producing countries are more conservative; when planning their budgets, they adhere to the prices of \$50-70 / barrel².

Table 2

THE DYNAMICS OF THE BASIC TAX REVENUES TO THE BUDGET OF EXPANDED GOVERNMENT OF THE RUSSIAN FEDERATION IN JANUARY-APRIL 2010–2011, PER CENT OF GDP

	January- April 2011	January- April 2010	Change, p.p.of GDP
Level of tax burden (1+2+3)	37.8	35.2	+2.6
1. Revenues from taxes (1), including:	23.1	22.5	+0.6
Corporate profits tax	5.5	5.1	+0.4
Single social tax	3.6	3.9	-0.3
VAT	6.5	6.0	+0.5
Excise duties	1.2	1.1	+0.1
Severance tax	4.0	3.5	+0.5
2. Insurance contributions for compulsory social insurance	6.7	5.1	+1.6
3. Revenues from foreign economic activity	8.0	7.6	+0.4

Source: Ministry of Finance of the Russian Federation and Rosstat; Gaidar Institute assessments.

Following a tangible increase of oil and gas revenues, *other than oil industries* also demonstrate a trend of revenue growth in nominal and in relative terms. The exception is personal income tax, the income of which in relative terms show a slight decrease (See *Table 2*)

The revenue from *individual profit tax* to the expanded government budget in relative terms made 3.6 per cent of GDP, which is by 0.3 percentage points of GDP lower than the level of the

1 Scenario conditions for the formation of social and economic development options in 2012-2014.

2 <http://bujet.ru/article/140500.php>

relevant indicator of 2010. In nominal terms, the growth of budget revenues in the first four months of 2011 made over 10 per cent and was based mainly on the extended tax base: the dynamics of average monthly gross wage increase shows an increase of 2010 level in both nominal and real terms (by 11.2 and 1.6 per cent, respectively)¹.

The revenue from *corporate profit tax* to the expanded government budget within January-April of 2011 as compared with the relevant period of 2010 has increased by 0.4 percentage points of GDP, which was based on the growth of the tax base. In January-April of the current year the real sector has received the financial surplus in the amount of Rb 2,726.3 bn, which is by 31 per cent higher than its value for the corresponding period in 2010, whereas the share of profitable organizations in the total number of organizations in comparison with the relevant period of preceding year increased by 0.5 percentage points and amounted to about 63.4 per cent².

In general, it can be noted that the level of the *tax burden* on the economy in the first four months of 2011 has increased by 2.6 percentage points of GDP as compared with the same period in 2010 and reached 37.8 per cent of GDP.

Against the background of increased revenues of the budget of expanded government, relative level of expenditures also demonstrated a reduction: budget expenditures decreased by 2.9 percentage points of GDP as compared with the relevant period of 2010 (*Table 3*).

Table 3

EXECUTION OF THE BUDGET OF THE EXPANDED GOVERNMENT IN TERMS OF EXPENDITURES
IN JANUARY-APRIL 2011–2010, % OF THE GDP

	January-April 2011		January-April 2010		Change, p.p. of GDP
	Rb, bn	% of GDP	Rb, bn	% of GDP	
Expenditures, total:	5 153.7	32.9	4 689.9	35.8	-2.9
Including					
Federal issues	442.4	2.8	403.4	3.1	-0.3
Contributions to the service of federal and municipal debt	108.5	0.7	96.7	0.7	0.0
National defense	436.2	2.8	414.0	3.2	-0.4
National defense and law enforcement	392.0	2.5	377.5	2.9	-0.4
National Economy	565.1	3.6	527.0	4.0	-0.4
Housing and public utilities	209.5	1.3	176.3	1.3	0.0
Environmental protection	6.6	0.04	6.3	0.05	-0.01
Education	557.0	3.6	502.7	3.8	-0.2
Culture, cinematography and mass media*	100.9	0.6	87.2	0.7	-0.1
Health care and sports**	494.6	3.2	441.1	3.4	-0.2
Social policy	1 949.5	12.4	1 754.3	13.4	-1.0

* In the functional classification of budget expenditures for 2011 there were changes: the article "Culture, "Film Industry", "Media" and "Healthcare" and "Physical Culture and Sport" are presented as separate budget lines.

Source: RF Treasury, Gaidar Institute estimates.

In relative terms, all budget lines of expanded government were reduced. The worst decline in public expenditures was based on the low rate of funding for «Social policy», which has reduced by about 1.1 p.p. GDP. In addition, reduction of budget expenditures is noted in the lines "National Economy", "National Defense", "National Defense and Law Enforcement", - by 0.4 percentage points of GDP for each budget line.

The marked underinvestment in certain budget lines should be regarded as deferred expenses, rather than budget savings. Execution of the majority of spending commitments will occur in the second half of this year.

In particular, in June we became aware of the indexation of salaries to state employees, expected before the end of the year. The salaries are planned to be raised in two phases: in summer and

1 http://www.gks.ru/bgd/free/B11_00/IssWWW.exe/Stg/dk05/6-0.htm

2 According to the Federal State Statistics Service "On the financial performance of organizations in the I Quarter 2011"

in fall. This decision is a very “popular” measure in an election period, but at the same time it is cumbersome in the situation of a limited budget.

In addition, the government’s plans are announced to increase in the medium term the state defense order nearly by 4 times, as well as to increase the allowance and pensions for military personnel¹; the cost of defense industry development will increase.

RF federal budget execution within January-April 2011

According to the tentative estimates of the RF Ministry of Finance, within 5 months of 2011 budget revenues amounted to 21.3 per cent of GDP, which is by 1.2 percentage points of GDP exceeds the indicator of the relevant period of 2010 (See *Table 4*). In absolute terms, the growth of federal budget revenues amounted to Rb one trillion.

In January-May 2011 revenues from oil and gas asset management funds for 2010 were enrolled in the budget in the amount of Rb54.1 bn. The total volume of oil and gas revenues over five months of the current year amounted to 10.5 per cent of GDP, which is by 1.7 percentage points of GDP higher than the values of the same period in the last year.

Table 4

BASIC INDICATORS OF THE RF FEDERAL BUDGET IN JANUARY-MAY OF 2010-2011

	January-May 2011		January-May 2010		Budget execution in % versus 2011 year estimates	Change	
	Rb, bn	% of GDP	Rb, bn	% of GDP		Rb, bn	p.p. of GDP
Revenues, including:	4 197.8	21.3	3 195.7	19.2	47,5	+1 002,1	+2,1
Oil and gas	2 067.0	10.5	1 469.3	8.8	50,5	+597,7	+1,7
Contributions to the Reserve Fund and National Welfare Fund (Stabilization Fund)	0.0	0.0	26.5	0.2	-	-26,5	-0,2
Revenues, including:	3 842.0	19.5	3 658.9	21.9	36,0	+183,1	-2,4
Interest expenditures	98.9	0.5	84.6	0.5	25,4	+14,3	+0,0
Non-interest expenditures	3 743.1	19.0	3574.3	21.4	36,5	+168,8	-2,4
Deficit / Surplus of the federal budget	+355.8	+1.8	-463.3	-2.8	-	+819,1	+4,6
Non-oil deficit	-1 711.2	-8.7	-1 932.5	-11.6	29,0	+221,3	+2,9
GDP estimates	19 723.3		16 677.9				

Source: RF Ministry of Finance (tentative assessments), Gaidar Institute estimates.

Preliminary estimates of the *federal budget execution in terms of expenditures* for January-May 2011 indicate a significant decrease in their volume - by 2.4 percentage points of GDP against the value of five months of 2010, which is mainly based on the low rate of budget expenditures.

Before the end of 2011, one can expect the federal budget expenditures increase. Thus, according to amendments to the Law on Federal budget for 2011, the growth will amount to Rb363.9 bn² over 80 per cent of which will be covered by the surplus oil and gas revenue. The major part of funding will be addressed to social objectives: in particular, about Rb43 bn will be allocated for the Fund of Direct Investments formation.

Consistent extension of budgetary commitments (mainly social ones) at the background of limited budget resources increases the dependence of the Russian financial system from the external environment and oil and gas sector (non-oil deficit of the federal budget in January-May amounted to about 9 per cent of GDP). This situation poses a threat to the stability of the national budget system in the medium term, particularly with the forecast for decline in oil prices in 2012-2014 (up to \$97-93/ bbl) against the estimates of 2011 (\$ 105 / bbl).

1 <http://www.interfax-russia.ru/main.asp?id=238294&p=6>

2 <http://www.minfin.ru/ru/press/speech/index.php?id4=13169>

According to the tentative data, within the first five months of 2011, *the federal budget was executed with a surplus* of 1.8 per cent of GDP against the deficit of 2.8 per cent of GDP in the same period of 2010; the volume of non-oil deficit has declined by 2.9 per cent of GDP as compared with the previous year and amounted to 8.7 per cent of GDP. However, its level is still rather high.

In general, in 2011 there is a high probability of achieving a balanced budget with some surplus. In the June amendments to the budget law for 2011, the fiscal balance remained positive, but with its significant reduction to 1.4 vs. 3.6 per cent of GDP. A significant adjustment is triggered by the revision of the expenditure part of the budget upward by 1.7 percentage points of GDP as compared with the initial indicators. The adopted amendments to the budget are based on an updated forecast of the socio-economic development, in particular on the revision of the estimated oil price (increase to 105 dollars / barrel against the initial estimate 75 dollars / barrel).

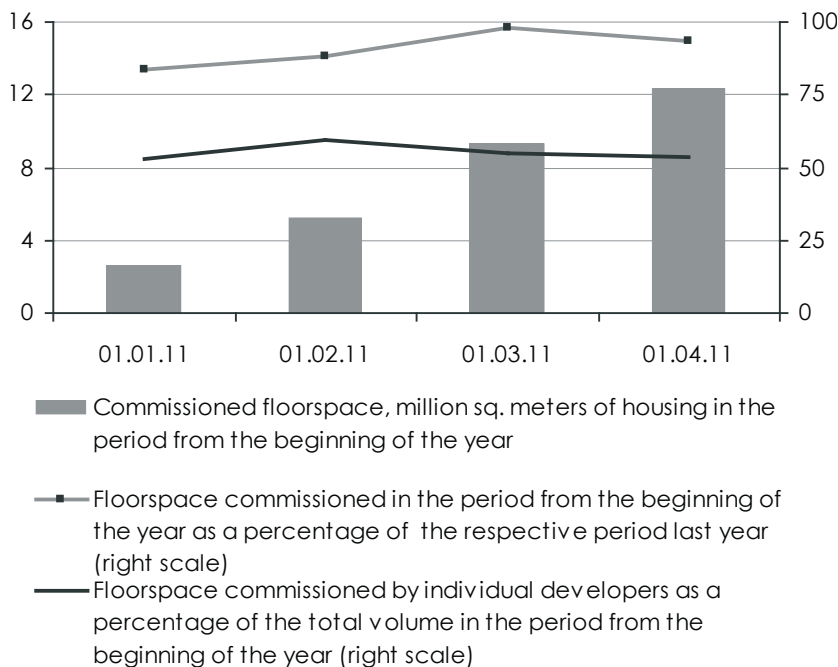
As of June 1, 2011, *the volume of Reserve Fund* amounted to Rb745.9 bn (Rb 775.2 bn on January 1, 2011); *the volume of the National Welfare Fund* has reached Rb2,597.6 bn (Rb2,695.5 bn on January 1, 2011). The government intends to renew the accumulation of funds in the Reserve Fund. According to preliminary estimates the RF Ministry of Finance, the amount of the Reserve Fund by the end of 2014 may exceed 2.2 trillion rubles¹. It is worth noting that the accumulation of funds against the background of an imminent the growth of government spending in the pre-election period may lead to increased internal government borrowing, which will increase government spending on debt service (in 2011 the upper limit of domestic government debt should not exceed 8.9 per cent of GDP). ●

1 <http://ria.ru/economy/20110602/383178253.html>

THE REAL-ESTATE MARKET OF THE RUSSIAN FEDERATION

G.Zadonsky

In January-April 2011, entities of all the forms of ownership built 145,600 apartments with the total floorspace of 12.4 m sq meters which figure amounted to **93.3%** against the respective period last year. **In the 1st quarter of 2011, the ratio between the price of a sq. meter of housing on the primary residential property market and the cost of building of a sq. meter of housing amounted to the minimum value of 130.2% since 2002.** By evaluations of OAO AMHL, in the first six months of 2011 181,000 to 195,000 mortgage housing loans for the total amount of Rb 253bn to Rb 273bn will be extended **with rates on mortgage housing loans in rubles being in the range of 12–12.5%**, while the share of the overdue debt in the total volume of the mortgage portfolio of the banking sector amounts to 3.2–3.6%.



Source: on the basis of the Rosstat's data.

Fig. 1. The Dynamics of commissioning of housing on an accrual basis from the beginning of the year

According to the data of Rosstat, in January-April 2011 entities of all the forms of ownership built 145,600 apartments with the total floorspace of 12.4 m sq. meters, which figure amounted to 93.3% against the respective period last year. The above volume also includes 6.6 m sq. meters of residential floorspace built by individual developers which figure amounts to 53.3% of the total volume of housing which was commissioned in that period (Fig. 1) and 94.1% against the respective period last year. In April 2011, 38,600 new apartments with the total floorspace of 3.1 m sq. meters were built.

According to the Rosstat's data, within the frameworks of the *Fulfillment of State Obligations as Regards Provision of Housing to the Categories of People Established by the Federal Legislation Sub-Program of the Housing Federal*

Purpose Program in the 2002–2010 period 327 apartments were bought for persons dismissed from the military service and law enforcement agencies as well as those made equal to the above categories of people through realization of state housing certificates in the 1st quarter of 2011. The total floorspace of the purchased housing amounted to 16,600 sq. meters which cost Rb 540.8m, including those bought by means of provided social payments in the amount of Rb 514.9m. In 2010, 3,100 apartments with the total floorspace of 160,400 sq. meters which cost Rb 5,196.5m, including those bought by means of provided social payments in the amount of Rb 4,909.4m were purchased.

Having increased by 2.4% as compared to the 1st quarter of 2010 (Rb 31,135), the average actual cost of building of a sq. meter of floorspace of apartment houses amounted to Rb 31,893 in the 1st quarter of 2011 (Fig. 2). The average price of a sq. meter of housing on the primary market went down to Rb 41,534 (Fig. 2) remaining below that of a sq. meter of housing on the secondary market

(Rb 46,162.). It is to be noted that in the first quarter 2011 the ratio between the price of a sq. meter of housing on the primary market and the cost of building a sq. meter of housing amounted to the minimum value of the mere 130.2%. The previous minimum of 143.4% was registered in 2002.

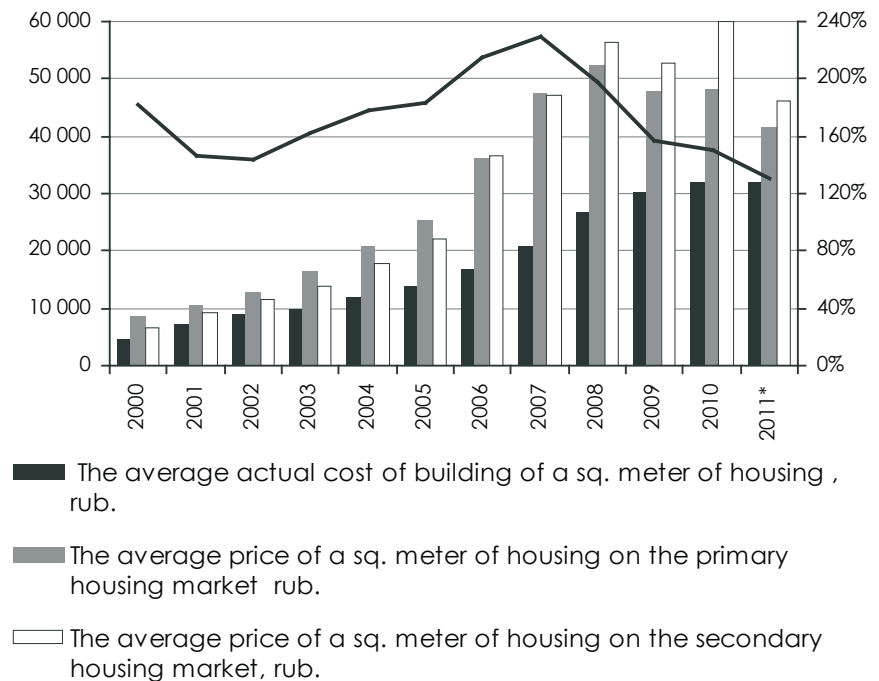
According to the Rosstat's data, in the 1st quarter of 2011 the average actual cost of building a sq. meter of housing was over 50% higher than the average national level in the Nenets Autonomous Region (Rb 61,154), the Salhalin Region (Rb 59,354) and the Archangelsk Region (Rb 52,002) and below the average national level in 48 constituent entities of the Russian Federation; the lowest indices were registered, in particular, in the Transbaikal

Territory (Rb 8,734), the Republic of Dagestan (Rb 17,957), the Kursk Region (Rb 19,280), the Astrakhan Region (Rb 19,311) and the Ivanovo Region (Rb 19,847).

According to the Rosreestr's data, in the 1st quarter of 2011 the number of the registered titles of individuals to dwelling premises (1 708 483 certificates) decreased by 22.92% as compared to the 1st quarter of 2010, while the number of registered titles of legal entities to dwelling premises (51 391 registered certificates), by 30.97%. The number of new agreements on leasehold of dwelling premises is insignificant as compared to the number of titles acquired to dwelling premises, and in the 1st quarter of 2011 the number of certificates of leasehold amounted to the mere 0.026% of the number of certificates of registration of the title to dwelling premises. In the 1st quarter of 2010, the number of housing mortgages increased by 75.59% (179 969 certificates) as compared to the 1st quarter of 2010. It is to be noted that in the 1st quarter of 2011 the number of mortgages of dwelling premises owned by people who bought (built) them with use of borrowed funds or purpose loan increased by 97.26% as compared to the 1st quarter of 2010 (93 127 mortgages in the 1st quarter of 2011).

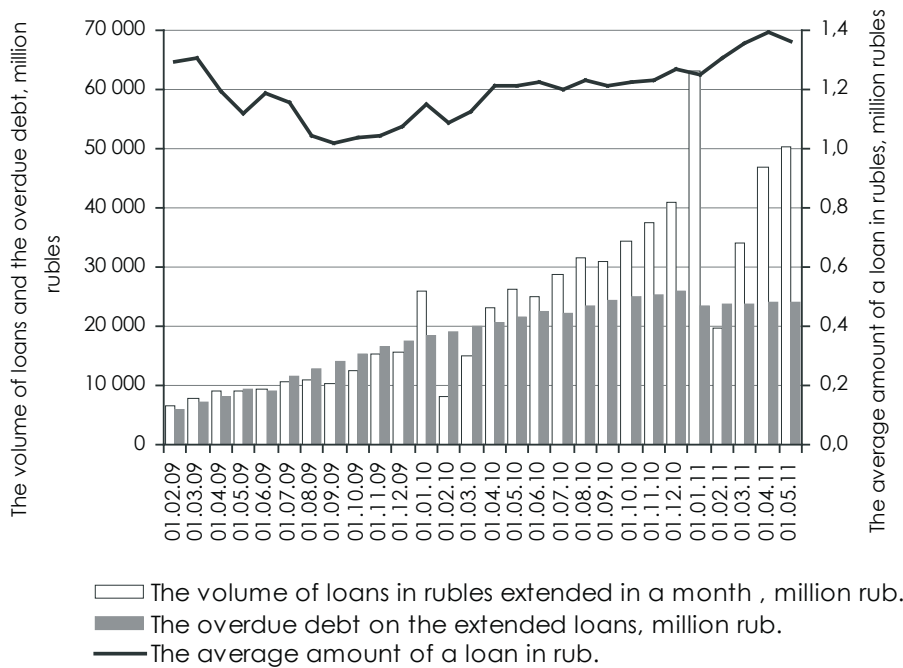
According to the Rosreestr's data, in the 1st quarter of 2011 the number of certificates of registration of titles of individuals and legal entities to land plots decreased as compared to the 1st quarter of 2010 (as regards individuals, such a reduction amounted to 16.85% with 1 211 705 certificates registered, while in case of legal entities, to 13.65% with 504 179 certificated registered). In the 1st quarter of 2011, the number of agreements on leasehold of land plots decreased in general by 42.51% as compared to the 1st quarter of 2010 due to a drop of 78% in the number of leasehold agreements by legal entities (62417 registered certificates the 1st quarter of 2011), however, the number of agreements by individuals on leasehold of land plots increased by 57.21% and amounted to 39 993 registered certificates in the 1st quarter of 2011 as against 25440 registered certificates last year. As compared to the 1st quarter of 2010, the number of registered mortgages of land plots for individuals increased by 131.5% (46 419 certificates in the 1st quarter of 2011), while that for legal entities, by 32.6% (26 273 registered certificates in the 1st quarter of 2011).

According to the data of the Central Bank of Russia, in January-April 2011 136 891 housing loans were extended for the total amount of Rb 173.13bn including 111 304 mortgage housing loans for the



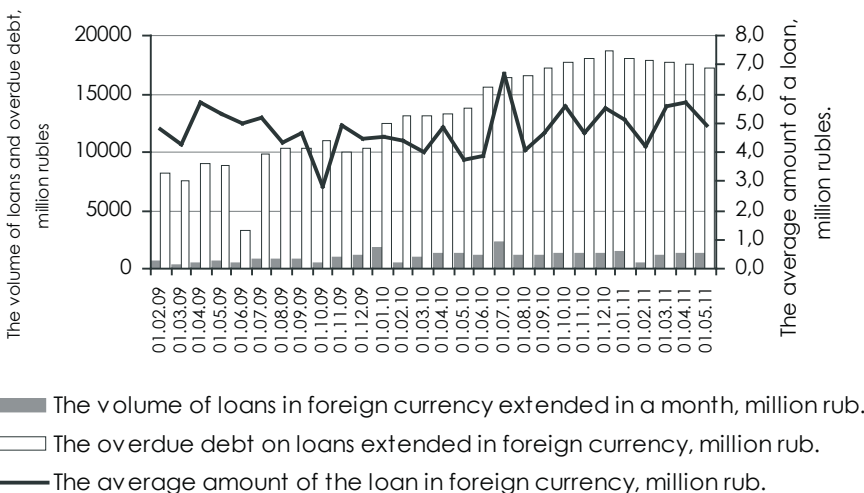
The source: on the basis of the Rosstat's data.

Fig. 2. The cost of building and price of a sq. meter of housing on the primary and secondary real-estate market



The source: on the basis of the data of the Central Bank of Russia.
 Fig.3. The dynamics of extension of mortgage housing loans in rubles

amount of Rb 154.9bn which figure exceeds 2.03 times over the total volume of mortgage housing loans extended in January-April 2010. In April 2011, the number of ruble mortgage housing loans for the total amount of Rb 50.25bn increased 1.93 times over as compared to that in April 2010 (Fig. 3), while the number of mortgage housing loans in foreign currency for the total amount of Rb 1.32bn, only by 7.3% as compared to April 2010 (Fig. 4). Growth in the average amount of mortgage housing loans in rubles in a month which took place in the 1st quarter of 2011, went down in April to Rb 1,365m (1.9% lower than in March 2011 (Fig.3), while as regards loans in foreign currency in the same period the average amount of mortgage housing loans dropped by 13.75% to Rb 4.92 m (Fig. 4). As of May 1, 2011, the outstanding debt on mortgage housing loans in rubles rose to Rb 1 011.21bn, while that on loans in foreign currency went down to Rb 157.83bn which figure is 3.72% lower than that as April 1, 2011.



The source: on the basis of the Central bank's data.
 Fig.4. The dynamics of extension of mortgage housing loans in foreign currency

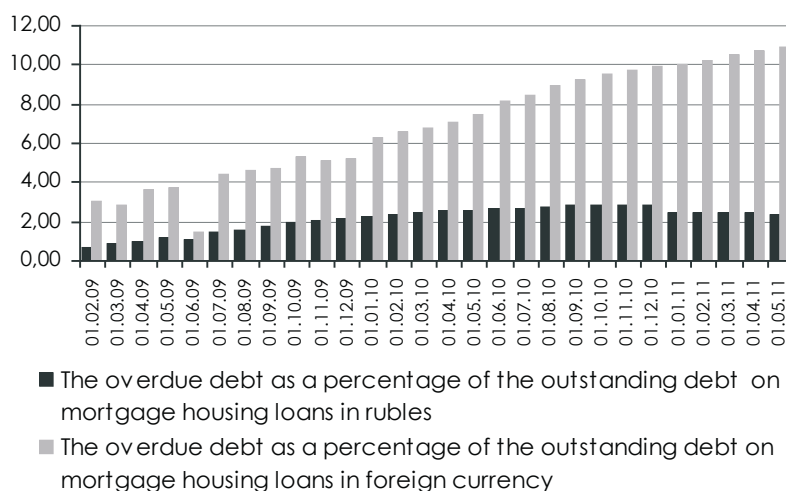
As of May 2011, the overdue debt on the mortgage housing loans amounted to Rb 41.23bn which figure is 0.55% lower than that as of April 1, 2011 (Rb 24.01bn as regards loans

in rubles (Fig. 3) and Rb 17.21bn as regards loans in foreign currency (Fig. 4). The overdue debt keeps decreasing against the outstanding debt on mortgage housing loans in rubles and as of May 1, 2011 it amounted to 2.37% (Fig. 5), while the overdue debt on mortgage housing loans in foreign currency keeps growing and as of May 1 amounted to 10.91% of the outstanding debt (Fig. 5).

According to the data of the Central Bank of Russia, as of May 1, 2011, the debt on the defaulted mortgage housing loans (with a period of delay of over 180 days) amounted to Rb 53,425bn and 4.57% of the total amount of the debt which figure is somewhat lower (by 0.05 percentage points) than that in the previous month (Table 1). As of May 1, 2011, the share of the debt on the mortgage housing loans without overdue payments increased as compared to that as of April 1, 2011 and amounted to 88.66%. Average weighted rates on housing loans in rubles extended within a month kept falling. In April 2011, the average weighted rates on mortgage housing loans and housing loans narrowed at the level of 12.1% (Fig. 6).

In 2011, average weighted rates on loans in foreign currency extended within a year tend to go down; in April 2011 the rates on mortgage housing loans fell to 9.8%, while those on housing loans, to 10.2%. However, in May 2011 the Central Bank of Russia raised the rate of refinancing from 8.0% to 8.25%, which situation, probably, results in subsequent growth in rates on housing loans.

In April 2011, the average weighted periods of lending as regards loans in rubles extended within a month decreased as compared to March to 16.07 years and 15.61 years for mortgage housing loans and housing loans, respectively (Fig. 6). In April 2011, the average weighted period of lending for mortgage housing loans in foreign currency extended from the beginning of the year amounted to 12.78 years, while that for housing loans in foreign currency, to 11.5 years.



The source: on the basis of the data of the Central Bank of Russia.
Fig. 5. The dynamics of the overdue debt

Table 1

GROUPING OF THE DEBT ON MORTGAGE HOUSING LOANS BY THE PERIOD OF DELAY
IN PAYMENTS IN 2011

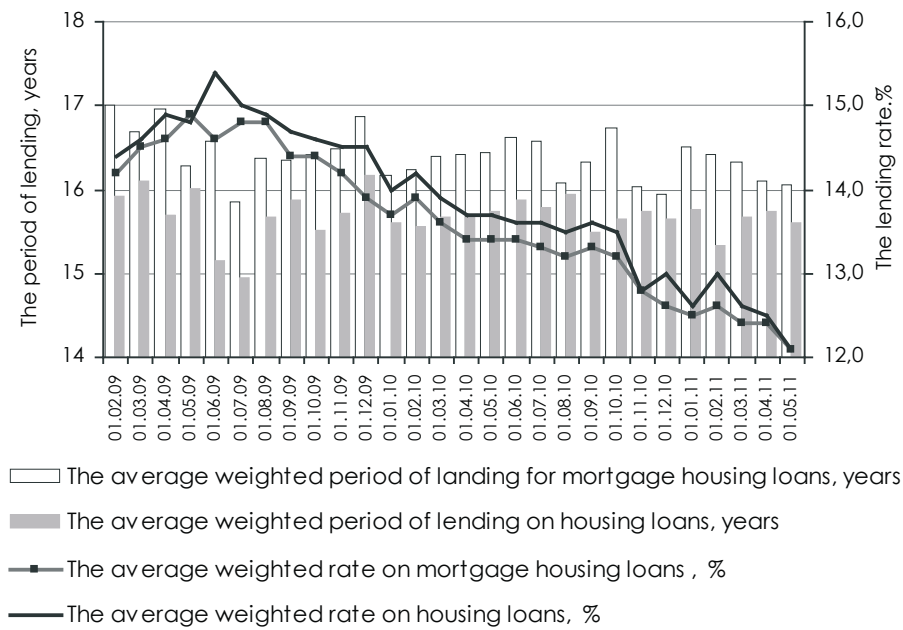
	The total amount of debt on mortgage housing loans, million rubles	Including							
		Without overdue payments		With payments overdue for 1 to 90 days		With payments overdue for 91 to 180 days		With payments overdue for over 180 days	
		Million rubles	% of the total amount of the debt	Million rubles	% of the total amount of the debt	Million rubles	% of the total amount of the debt	Million rubles	% of the total amount of the debt
Jan.01	1 129 373	991 928	87.83	66 859	5.92	12 875	1.14	57 711	5.11
Feb.01	1 127 753	977 311	86.66	84 581	7.50	12 293	1.09	53 568	4.75
March 01	1 134 097	982 922	86.67	86 758	7.65	11 908	1.05	52 509	4.63
Apr.01	1 152 654	1 013 874	87.96	73 309	6.36	12 218	1.06	53 253	4.62
May 01	1 169 045	1 036 476	88.66	68 155	5.83	10 989	0.94	53 425	4.57

The source: on the basis of the data of the Central Bank of Russia.

As of May 1, 2011, the share of mortgage housing loans in foreign currency in the total volume of the outstanding debt decreased and amounted to 13.5%, while in the volume of mortgage-housing loans extended in the same period it amounted to 2.8%.

In June 2011, the State Duma passed in the third reading amendments to the law on mortgage as regards restoration as participants in the funded mortgage system of provision with housing military servicemen who were earlier dismissed from service and then concluded a new contract with the Ministry of Defense. Family members of the perished participant in the funded mortgage system are granted the right to use the accumulated funds not only on improvement of their housing conditions, but also on other purposes.

According to the data of OAO Agency for Mortgage Housing Lending (AMHL), in the 1st quarter of 2011 the Agency refinanced 7 996 mortgage loans for the total amount of Rb 9.7 bn which figure amounts to 10.8% (in quantitative terms) and 9.4% (in money terms) of all the mortgage loans extended in that period. As compared to the 1st quarter of 2010, that figure is 5.2 % and 5% lower, respectively. According to the Agency, the reduction in the share of AMHL in a situation of growth



The source: on the basis of the data of the Central Bank of Russia.
 Fig.6. The average weighted periods and average weighted rates on loans in rubles extended within a month

in the mortgage market is the result of improvement of the liquidity situation in the mortgage sector which factor is evidence of recovery of the mortgage market.

AMHL intends to stimulate building of leasehold housing within the frameworks of the *Mortgage of Rent* program and for that purpose it proposes to buy out from banks loans extended to legal entities for building of commercial apartment houses after completion of building and transfer of the project to the balance of the legal entity.

AMHL is planning another program under which it intends to extend loans to the elderly against the real

property which they own. Such a loan – the reverse mortgage – is transferred by installments on a monthly basis as an additional pension. After the death of the borrower, the debt will be either repaid by the heirs, or the apartment is taken over by the creditor.

At present, there are 14 issues of OAO AMHL' bonds for the total amount of Rb 73.6bn in the market; the bonds are secured by state guarantees of the Russian Federation.

According to evaluations of the Agency, in the first six months of 2011 180,190,000 mortgage loans for the total amount of Rb 253bn to Rb 273bn will be provided; the rates on mortgage housing loans in rubles will be in the range of 12–12.5%, while the share of the overdue debt in the total volume of the mortgage portfolio of the banking sector amounts to 3.2%–3.6%. Analysts of the Agency say that in the mid-term prospect banks may lower requirements to borrowers and reduce the amount of the initial installment.

In 2011, Rosreestr is planning to complete a large-scale evaluation of property projects in 12 regions where it is expected to introduce for the first time the single tax on the real property. Those regions include Bashkortostan, Tatarstan, the Krasnodar Territory, the Krasnoyarsk Territory, the Irkutsk Region, the Kaliningrad Region, the Kaluga Region, the Kemerovo Region, the Nizhny Novgorod Region, the Rostov Region, the Samara Region and the Tver Region. Until the end of the year, it is expected to make calculations as regards the tax rate and introduce the tax from 2012. ●

REVIEW OF THE ECONOMIC LEGISLATION

I.Tolmacheva

In June, the following amendments were introduced into the legislation: from June 1, 2011 the minimum wages were increased from Rb 4,330 to Rb 4,611 a month; large families were granted the right to acquire free of charge land plots which are in a state or municipal property; at the federal level the maximum size of the area of land plots which can simultaneously be in ownership of people who engage in subsidiary husbandry or belong to them by other rights was established; the amount of the minimum subsistence level in Russia in the 1st quarter of 2011 was approved and new forms of sick lists were introduced from July 1, 2011.

I. Federal Laws of the Russian Federation

1. "ON INTRODUCTION OF AMENDMENT INTO ARTICLE 1 OF THE FEDERAL LAW ON THE MINIMUM WAGES" (Law No.106-FZ of June 1, 2011).

Amendment was introduced into Federal Law No.82-FZ of June 19, 2000 on The Minimum Wages. From June 1, 2011, the minimum amount of wages was increased from Rb 4,330 to Rb 4,611 a month. Under the Law, the minimum wages are applied only for the purpose of regulation of labor remuneration and determination of the amount of temporary disability benefits, maternity benefits, as well as for other purposes of mandatory social insurance. Under the Labor Code of the Russian Federation, the minimum wages are set simultaneously in the entire territory of the Russian Federation by a federal law, and they cannot be below the minimum subsistence level of the able-bodied citizens.

2. "ON INTRODUCTION OF AMENDMENTS INTO ARTICLE 16 OF THE FEDERAL LAW "ON ASSISTANCE IN DEVELOPMENT OF HOUSE BUILDING" AND THE LAND CODE OF THE RUSSIAN FEDERATION" (Law No. 138-FZ of June 14, 2011).

People with three or more children are granted the right to acquire free of charge land plots which are in a state or municipal ownership. The procedure for acquisition of such land plots and their size limits are set by the laws of a constituent member of the Russian Federation. Also, land plots may be acquired for individual house building without bargaining and preliminary approval of location of projects. The law specifies the procedure for cadastral accounting of some types of land plots.

3. "ON INTRODUCTION OF AMENDMENTS IN ARTICLE 217 OF PART TWO OF THE TAX CODE OF THE RUSSIAN FEDERATION AND ARTICLE 4 OF THE FEDERAL LAW ON "INDIVIDUAL SUBSIDIARY HUSBANDRY" (Law No. 147-FZ of June 21, 2011).

Amendments have established the maximum size of 0.5 ha of the entire land plot which can simultaneously be in ownership of or otherwise belong to people who engage in individual subsidiary husbandry. The maximum size can be increased by the law of a constituent member of the Russian Federation, but no more than fivefold. In the previous statutory wording, the maximum size of the entire area of such land plots was not determined and was set by the law of a constituent entity of the Russian Federation.

In addition to the above, it is established that the funds received by the taxpayer out of the budgets of the budget system of the Russian Federation for development of individual subsidiary husbandry are exempted from the individual income tax. The privilege in the form of exemption from taxation of the income received from sale of the livestock products and crop products grown by the taxpayer in individual subsidiary husbandry can be utilized only by those husbandries which do not use hired labor.

II. Resolutions of the Government of the Russian Federation

1. "ON ESTABLISHMENT OF THE AMOUNT OF THE MINIMUM SUBSISTENCE LEVEL PER CAPITA AND BY THE MAIN SOCIAL AND DEMOGRAPHIC GROUPS OF THE POPULATION

IN GENERAL IN THE 1ST QUARTER OF 2011 IN THE RUSSIAN FEDERATION” (Resolution No. 465 of June 14, 2011.

In the 1st quarter of 2011, the minimum subsistence level in Russia in general is established in the amount of Rb 6,473 per capita, while that for the able-bodied citizens, pensioners and children, in the amount of Rb 6,986, Rb 5,122 and Rb 6,265, respectively. As compared to the previous quarter, the minimum subsistence level has been increased. In the 4th quarter of 2010, it amounted to Rb 5,902 per capita, while for able-bodied citizens, pensioners and children, to Rb 6,367, Rb 4,683 and Rb 5,709, respectively.

The amount of the minimum subsistence level is determined quarterly on the basis of the consumer goods basket and Rosstat’s data on the level of consumer prices on food, non-food products and services, as well as expenditures related to mandatory payments and charges.

III. Instructions, Letters and Orders

1. Order No. 347n of April 26, 2011 of the Ministry of Health and Social Development of the Russian Federation “ON APPROVAL OF THE FORM OF THE SICK LIST ».

Registered with the Ministry of Justice of the Russian Federation on April 26, 2011, Registration No. 21026.

From July 1, 2011, in the territory of the Russian Federation the new form of sick lists will be introduced. The main difference from the previous one is that the new form of the sick list is machine-readable. All the entries are to be made in special sections. Some information included in the sick list will be encoded (the list of the necessary codes is given on the reverse side of the sick list). Relevant codes are to be entered into special margins provided for that purpose. Provision of medical institutions with the approved new forms of sick lists has been entrusted with the Fund of Social Insurance of the Russian Federation.

The form of the sick list is a protected printing product with “B”- level of protection ¹.

¹ In production of “B”- level protected printed product it is required to use paper with weight of 70-120 g per sq. m and such a water mark of limited distribution as has detectable sharpness which ensures reliable visual control. The paper should have no luminosity (visual luminescence) under effect of UV-light. The paper must contain at least two types of fibers which are controlled in the visual or other areas of the spectrum (Cl. 4.2 of the Technical Requirements and Specifications for Production of Protected Printed Products approved by Order No. 14n of February 7, 2003 of the Ministry of Finance of the Russian Federation).

AN OVERVIEW OF THE RUSSIAN FEDERATION GOVERNMENT'S MEETINGS IN JUNE 2011

M. Goldin

At its meetings in June 2011, the RF Government considered the following issues: a bill, which aims to improve the effective mechanism of appeal by citizens of actions and administrative dereliction of government agencies and local self-government bodies and their officials; a bill that provides for amendments to a series of legislative acts due to improvements made in the anti-monopoly law.

At its meeting on 9 June 2011, the Presidium of the RF Government considered a bill “On introducing amendments to individual legislative acts of Russian Federation” submitted by the RF Ministry of Economy.

Currently the issues stipulated in the bill fall under the federal act “On the procedure of consideration of claims of citizens of Russian Federation” of 2 May 2006 № 59-FZ (hereinafter referred to as Act № 56-FZ). In compliance with Act № 56-FZ, citizens’ claims that require prompt decision making and restoration of violated rights and legal interests are considered in general order, along with other submissions.

That said, the procedure of appeal most often falls short of helping receive a timely and adequate public or municipal service. Claims routinely bounce to respective government agencies and ultimately land on the desk of a public official who de-facto is not held responsible for a formal answer to or ignoring it.

The bill suggests granting a special (vis-a-vis other individual and corporate claims) status to claims on decisions and acts or administrative dereliction of government agencies and local self-government bodies in regard to provision of public and municipal services and making decisions in this respect. This would allow matching pre-set standards of provision of public and municipal services.

Plus, the bill introduced administrative responsibility of public officials of federal agencies of executive power for breaching the pre-set standards and procedures of provision of public services, and for an unjustified refusal of satisfying the claim.

At its meeting on 28 June 2011, the Presidium of the RF Government considered bills “On introducing amendments to the federal act “On protection of competition” and some other legislative acts of Russian Federation” and “On introducing amendments to the Administrative Offenses Code of Russian Federation”. The bills were submitted by the Federal Anti-Monopoly Service of Russian Federation.

The amendments in the federal act “On protection of competition” are based on the law-enforcement practice and provide for changes in anti-monopoly requirements, including:

- Setting more distinctive and transparent rules of recognition of prices being monopolistically high and, specifically, the impermissibility of recognition of a price to be monopolistically high, should it emerge in the course of exchange trading;
- Contraction in the list of bans on agreements and concerted actions of economic agents and, respectively, grounds of recognizing such agreements as cartels;
- Additional guarantees to entities with regard to whom proceedings have been instituted on cases of violation of the anti-monopoly law, including setting a minimum necessary period of analysis of the commodity market (no less than 1 year);
- Exercise of control over economic concentration with regard to operations of foreign entities only in the event the latter have shipped goods to the RF territory worth a total no less than Rb1bn over the year prior to the date of execution of the transaction;
- Conduct of the register of private individuals held administratively liable in order to exclude cases of an ungrounded holding one liable for one-time abuse of dominance;
- Specification of the procedure of institution and consideration of proceedings with regard to violation of the anti-monopoly law.

The bill also suggests introducing changes in the Criminal Code in regard to exclusion of criminal liability for concerted action and vertical agreements by economic agents. So, it will be cartels, as the most perilous for competition actions, which will become subject to prosecution.

As well, the bill provides for introducing amendments to federal acts “On electric power”, ‘On natural monopolies”, “On subsoil resources”, the Land, Urban Development, Water and Housing Codes of Russian Federation, and a string of other legislative acts. The proposed amendments to the Administrative Offenses Code provide for differentiation of economic agents’ liability for violation of the anti-trust law, including imposing a fixed fine in the amount of RUR 1m for abuse of dominance infringing upon counterparts’ interests albeit not limiting competition on the market. ●

AN OVERVIEW OF THE NORMATIVE DOCUMENTS ON TAXATION ISSUES ADOPTED IN MAY-JUNE 2011

L.Anisimova

1. *Federal Law No. 132-FZ of June 7, 2011* has introduced a number of important measures aimed at improvement of the investment climate for Russian manufacturers which engage in academic pursuits or carry out R&D.

The most important decision has become an opportunity to reserve funds out of the profit before tax for R&D for the period of maximum two years on the basis of work estimates.

The other important decision was related to acceptance of the costs within the frameworks of R&D for taxation purposes on the basis of the fact of recognition of those costs within the frameworks of the legislation on science (in respect of the list of jobs approved by the Government of the Russian Federation the right to appoint a scientific inquiry is granted to the tax authorities in accordance with the procedure provided for in Article 95 of the Tax Code of the Russian Federation). Earlier, R&D costs were qualified as a type of the manufacturer's production costs, that is, they used to be written off for reduction of the tax base depending on the fact whether they were recognized as investments in intangible assets used in activities on which the VAT was either charged or not, sold to the third parties or utilized in further research by the manufacturer. Those ambiguities related to posting of R&D costs incurred to production costs used to increase a great deal the manufacturers' risks if those costs for formal reasons were later qualified as payments out of the after-tax profit. (That situation largely prevented investments by Russian manufacturers in their own research and development). With introduction of amendments into the Tax Code of the Russian Federation the option of allocation of such costs in the full volume to lowering of the tax base has become much stronger, though on the face of it the amendments are executed by way of additions to the same articles which earlier regulated both R&D costs (Article 262) and other costs (Article 264). Briefly formulated, R&D costs are now recognized as costs related to carrying out of independent entrepreneurial activities irregardless of the obtained results, so losses related to the above activities can be charged within the frameworks of the Tax Code to the profit received from other types of business activities in accordance with the so-called "commingled method". An exception is expenses included in the cost of production of the intangible asset if the results of R&D are legally executed as intellectual property (see explanations below).

In accordance with new amendments, capital assets (except for the real property) used for R&D purposed are accounted for separately and depreciated (for that purpose it will be enough to declare items in which capital assets were used as R&D ones in accordance with the procedure set by the legislation on science); it is to be noted that non-linear depreciation is also provided for. Along with depreciation, material inputs and remuneration of the main workers, R&D costs include other expenses in the amount of 75% of the remuneration of the main workers; contributions for formation of such funds of support of scientific, research and innovation activities as are established in accordance with the Federal law on Science and State Research and Technical Policy in the amount of maximum 1.5% of the revenues from realization and other. Introduced into the text of the Tax Code of the Russian Federation is a general provision under which the above R&D costs of the taxpayer are recognized for taxation purposes irrespective of the results in accordance with the procedure provided for by the Tax Code of the Russian Federation not only after completion of the research (developments) in general, but, most importantly, after completion of individual stages thereof and (or) after signing by the parties of the acceptance certificate. The R&D costs recognized as such in accordance with the legislation on science are charged to expenses in the full volume irregardless of the fact whether they were included (fully or partially) in the cost of the intangible asset (in such a case they are written off through depreciation) or posted to other expenses (in such a case they are written off within two years).

If later the manufacturer has decided to execute a patent and a trademark or otherwise execute legally its title to intellectual property the amount of R&D costs which were earlier included in other

expenses is not subject to restoration and inclusion in the initial cost of the intangible asset. Such a measure has been introduced to make the accounting procedure for taxation purposes easier for entities which carry out R&D. The costs are simply written off as they arise in a calendar order and posted either to other expenses or -- if in the view of the designer the obtained result has turned out to be a promising one and a decision has been taken to execute an intellectual property title in respect of it -- the cost of the intangible asset in the amount of the expenses which were not written off before. At the same time, the adopted scheme permits to prevent unjustified reduction of taxes as in restoring of the costs which were earlier accounted for in other expenses and inclusion thereof in the cost of intangible assets the tax base is to be automatically increased for the previous periods and respective taxes and sanctions are to be charged additionally. Also, such a scheme permits to apply to R&D costs an officially accepted measure of protection of the budget interests: the text of the Tax Code includes a provision that in case of realization by the taxpayer of the intangible asset (which was obtained as a result of spendings on R&D) with a loss, such a loss is not accounted for for taxation purposes, that is, it does not reduce the tax base. It is believed that introduction of amendments into the procedure for taxation of R&D will largely eliminate the problems which prevented Russian entities from making the required volumes of investments in R&D.

2. *Federal Law No. 122-FZ of June 3, 2011* has established procedure for withholding and payment of taxes by a depositary which carries out accounting of owners' titles to securities with mandatory centralized safekeeping (for example, government securities). Such a depositary is obligated to render to the depositor (a nominal holder of securities) services related to receipt of income on securities in a cash form and other cash payments which are due to owners of such securities.

The central depositary renders the issuer services in the form of annual presentation of the list of persons who are owners of securities for a fee which does not exceed actual costs related to compilation of such a list and other services for a fee which amount is determined by agreement with the central depositary. The information on the owners of securities is provided by depositors to the central depositary within seven days from the day of inquiry.

Payments on securities of centralized safekeeping are carried out by the issuer by way of transfer of cash funds to the central depositary. Within one working day from the date of receipt of funds from the issuer, the central depositary transfers payments to depositaries which keep record of execution of obligations in respect of the securities; in its turn the above depositaries transfer them within ten days to depositors (nominal holders).

Within the frameworks of the above operations, the tax agent in respect of the income on federal government securities with mandatory centralized safekeeping is a depositary which carries out in the interests of the taxpayer transactions with securities of centralized safe-keeping. It is to be noted that as regards redemption of the par value of securities the depositary is not recognized as a tax agent and nor is it allowed to withhold tax on such amounts. The law will come into force from January 1, 2012.

3. *Federal Law No. 117-FZ of June 3, 2011* provides a tax privilege in respect of payment of insurance contributions to state social extrabudgetary funds under civil law contracts concluded with volunteers engaged in preparation, holding and servicing of the Olympic Games in Sochi in 2014 and the World Summer Universiade in Kazan in 2013 (hereinafter, referred to as the Games) in the form of payment of expenses on execution and issuing of visas, invitations and other similar documents, fares, accommodation, meals, training, communications services, transportation services, linguistic support, souvenirs bearing the emblem of the Games, as well as the amounts of insurance premiums (insurance contributions) under insurance agreements in favor of the specified persons, including premiums by the type of insurance provided for by the agreement concluded by the International Olympic Committee with the Russian Olympic Committee, the agreement between the International Federation of Student Sport and the Russian Student Sport Union and the agreement between the Government of the Republic of Tatarstan and the Mayor's Office of Kazan.

4. The analysis of documents as regards taxation issues has identified such an important problem in the work of tax authorities as insufficient credibility of evidence produced by tax authorities in courts in consideration of cases of tax violations.

So, in *Letter No. SA-4-9/8250 of the Federal Tax Service of May 24, 2011* for the purpose of raising efficiency of tax authorities' activities a large-scale analysis is carried out of the reasons for which

lawsuits brought by tax authorities in courts on the fact of receipt by taxpayers of unjustified tax benefits are dismissed (engagement of fly-by-night companies as counterparties to agreements, an artificial switch-over of tax obligations to companies which are in a bad financial situation and other), such negative financial and image consequences for the budget as are related to refusal by judicial authorities to support tax authorities' claims are investigated and methods of collection of evidence as regards detected instances of receipt by the taxpayer of unjustified tax benefits are proposed (tax authorities are advised to prove either the fact that the taxpayer intended to commit a violation, particularly, in case of use of fly-by-night companies, or indiscretion in the choice of the counterparty, or non-compliance with the rules of business intercourse and etc.). The above letter includes the opinion of the Presidium of the Supreme Arbitration Court of the Russian Federation as regards the issue of sufficiency of evidence of the taxpayer's unjustified tax benefit. (*Resolution No. 15574/09 of March 9, 2010 of the Presidium of the Supreme Arbitration Court of the Russian Federation, Resolution No. 15658/09 of May 25, 2010 of the Presidium of the Supreme Arbitration Court of the Russian Federation, Resolution No. 18162/09 of April 20, 2010 of the Presidium of the Supreme Arbitration Court of the Russian Federation, Resolution No. 17684/09 of June 8, 2010 of the Presidium of the Supreme Arbitration Court of the Russian Federation and Resolution No. 505/10 of July 27, 2010 of the Presidium of the Supreme Arbitration Court of the Russian Federation*). As tax violations are not supported by evidence submitted by tax authorities to courts, the VAT which is presented for refunding or setoff must be either paid to the taxpayer or taken into account in determination of the taxpayer's tax liabilities. It is to be noted that refusal by judicial authorities to accept lawsuits of tax authorities is evidence of the substandard quality of tax administration. In our opinion, there are two main factors behind that which are as follows: a) tax authorities are obligated to fulfill kind of a tax plan ensuring financing of the expenditure provided for by the budget; b) decisions taken by competent authorities as regards further development of the tax legislation and respective mechanisms of fulfillment thereof often fail in reality to ensure growth in tax revenues.

In our opinion, the issue of raising of credibility of evidence of tax violations due to a switch-over to electronic invoices used for VAT settlements will become particularly topical. (*The procedure was approved by Order No. 50n of April 25, 2011 of the Ministry of Finance of the Russian Federation*). In *Resolution No. 18162/09 of April 20, 2010*, the Presidium of the Supreme Arbitration Court explains that "the conclusion as regards unreliability of invoices signed by persons who are not specified in suppliers' founding documents as senior executives of those entities cannot be independently -- in case of absence of other factors and conditions -- regarded as evidence which permits to consider tax benefit unjustified. In case the counterparty complies with requirements set to execution of the required documents there are no grounds to conclude that the information included in the above invoices is unreliable or inconsistent one unless the evidence certifying the fact that the taxpayer was aware or had to be aware of provision by the seller of unreliable or inconsistent information has been found".

Order No.50n of April 25, 2011 of the Ministry of Finance of the Russian Federation in accordance with Article 169 (9) of the Tax Code of the Russian Federation approved the procedure for issuing and receipt of invoices in an electronic format through telecommunications channels due to application of the electronic digital signature (EDS).

Acceptance of VAT amounts for deduction can be carried out in respect of invoices which have been executed in accordance with the approved format and signed by means of EDS. Issuing and receipt of electronic invoices is carried out through one or a few entities which ensure exchange of both the open information and confidential information through telecommunications channels within the frameworks of electronic documents flow (Operators of the electronic documents flow, hereinafter referred to the Operators). The operators need be equipped both with technical devices which are compatible with those used by the Federal Tax Service of the Russian Federation for receipt and transfer of invoices in the approved electronic format and cryptographic facilities which are certified in accordance with the legislation of the Russian Federation and permit to identify the owner of the signature key certificate. Invoices can be issued through telecommunication channels either in an encrypted form or a plain form.

Invoices in electronic format are deemed issued if the seller has received a relevant confirmation from the operator and notification from the buyer of the receipt of the invoice signed by means of EDS of the buyer's authorized person.

For participation in the electronic flow of documents, the seller (the buyer) has to do the following: a) secure EDS key certificates; b) execute and submit to the operator an application for participation in the electronic document flow of invoices (along with other details it is necessary to specify in the application the taxpayer number and the tax authority which the taxpayer is registered with); c) receive from the operator an identification code of the participant in the electronic document flow, details of access and other.

In case of a change in the accounting data, it must be provided to the operator within three working days. In its turn, the operator is to inform within three working days the taxpayer's tax authority to that effect.

Despite all the advantages of the electronic document flow, it imposes on buyers (sellers) obligations to verify authenticity of EDS of operators which participate in the electronic document flow, while authenticity of EDS of participants in electronic document flow is to be verified by the operators.

It is to be noted that for operators economic consequences related to confirmation of signatures of such participants in the document flow as turned out later to be unauthorized ones are not regulated by the Tax Code. In case of a failure in the operators' activities, counterparties' tax obligations under agreements become ambiguous ones. On the one hand, taxpayers' obligations arise even in case of unscrupulous work of operators as no amendments regarding operators' tax obligations have been introduced into the Tax Code of the Russian Federation. On the other hand, under *Order No. 50n of May 25, 2011 of the Ministry of Finance of the Russian Federation* operators have been obligated to verify authenticity of such signatures. Therefore, it appears that litigations will definitely follow.

It is clear that in a situation of rapid development of foreign economic ties and the Customs Union electronic invoices can become the most efficient instrument in establishment of control by tax authorities over timely and complete payment of VAT to the budget. However, with introduction into the system of settlements with the budget of new participants, that is, operators which are responsible for confirmation of authenticity of EDS on tax documents there may be a repetition of the conflict similar to that which was once considered by the Constitution Court of the Russian Federation as regards responsibility of banks for a failure to transfer or untimely transfer of taxes to the budget due to a lack of balances in their correspondent accounts while funds in taxpayers' bank accounts were available. Consequently, the Order of the Ministry of Finance alone as regards the mechanism of settlements with the budget with the use of electronic invoices in order to ensure efficient utilization of electronic invoices is not enough. As courts have to decide all the disputes in favor of payers, difficulties may arise in formation of the revenue side of the federal budget until the issue of responsibility of the operators for a violation which resulted in a shortfall or delay in receipt of taxes by the budget has been resolved either in the text of the Tax Code of the Russian Federation or at the level of courts of last resort.

5. Another indirect evidence of insufficiently high quality of tax administration is an intention by some tax authorities to make arrangements with taxpayers as regards payment of concrete amounts to the federal budget. The above phenomenon is rather alarming as apart from a failure by tax authorities to ensure by legal methods execution of the tax legislation in full it points to the fact that tax authorities are prepared to give up execution of the legislation. The factors behind their intention to give up the norms of legislation may be different and range from determination to preserve by all means in the region entrepreneurial activities which for objective reasons (including high burdens in the form of different mandatory payments) are becoming loss-making and shrink -- which situation in its turn results in growth in the unemployment rate and social burden on the budget with the decreasing revenues base -- to (in an explicit form) corrupt practices.

As a result, the Federal Tax Service of the Russian Federation had to official notify the tax authorities of inadmissibility to conclude agreements with taxpayers on payment by the latter of concrete sums of money to the budget (*Letter No. ZN-4/1/8319 of May 25, 2011 of the Federal Tax Service of the Russian Federation*).

6. With establishment of the practice of making customs payments within the limits of the Customs Union, the Federal Tax Service of the Russian Federation explained in *Letter No. 01-11/25837 of June 2, 2011 and Letter No. 01-11/25837 of June 2, 2011* the procedure of making of customs payments for cars brought in by individuals to the Russian Federation.

It was explained in particular that in importing of cars by individuals (except for the cases where they are used for personal, family, households and other purposes which are not related to entrepreneurial activities and in respect of which full exemption of payment of customs duties and taxes is provided for by the Russian legislation) customs payments (duties and taxes) which were not paid to budgets of other countries of the Customs Union are subject to payment to the federal budget of the Russian Federation with customs declaration submitted to the customs authority of the Russian Federation. Applied in such situation are those types of rates of customs duties which have been set by the legislation of a member-state of the Customs Union (Article 72 (2) of the Customs Code of the Customs Union) in whose budget customs duties on imported cars are paid.

The rates of customs duties for customs clearance paid to the budget of the Russian Federation are set by *Resolution No. 863 of December 28, 2004 of the Government of the Russian Federation*. The Federal Customs Service of the Russian Federation draws taxpayers' attention to Cl. 7 of the Resolution which includes a special norm under which in case of repeated submission of the customs declaration on the same goods with declaration of the same customs regime customs duties for customs clearance are paid in the amount of Rb 500. However, if customs declaration was initially made to the customs authority of the Republic of Belarus or the Republic of Kazakhstan submission of the customs declaration to the customs authority of the Russian Federation is not deemed to be the second declaration, nor is Cl.7 of the Resolution applied to. In such a case, customs duties for customs operations are subject to payment at the rates set by Cl.1 of the above Resolution, that is, in the same way as it is done in case of the initial declaration.

It is believed that such a regulation actually compels individuals to bring in cars to the territory of the Russian Federation only through the Customs Union's external border which is controlled by the Russian customs service because otherwise double payment of customs duties cannot be excluded (both to the budget of the member-state of the Customs Union through which member-state the car was taken in and to the budget of the Russian Federation).

The above fact is evidence of insufficient development of the system of revenues transfer between the budgets of member-states of the Customs Union, lack of confidence with member-states of the Customs Union that budget revenues which are due to a respective member-state of the Customs Union are received in a timely manner, as well as the intention of the federal ministry to preserve its direct control over cash flows in order to maintain its current status and escape the fate of becoming an ordinary registrar of customs clearance documents whose exchange is carried out within the limits of the Customs Union if goods are imported through the territory of other member-states of the Customs Union. ●

CHANGES IN THE NORMATIVE BASE OF BUDGETING

M. Goldin

The procedure of identification of the volume of inefficient budget expenditures on managing cadres of medical staff and schoolteachers in RF Subjects was specified in June 2011.

With its Resolution of 14.06.2011 № 470 “On introducing amendments into the methodology of evaluation of efficiency of bodies of executive power of Subjects of Russian Federation” the RF Government specified the procedure of identification of the volume of inefficient budget expenditures on managing cadres of medical staff and schoolteachers in RF Subjects.

Instead of the value of the Uniform Social Tax abolished since 1 January 2011, the formula of calculation of the volume of inefficient expenditures now comprises insurance contributions. In addition, the RF Government set target values of the number of medical doctors and paramedical personnel per 10,000 local residents (41 and 114.3 people, respectively), which should be factored into in the course of calculation of inefficient expenditures on management of cadres instead of the previously used “average nationwide” values of numbers of medical doctors and paramedics per 10,000 residents. As well, it was established that optimization of the number of other personnel at medical institutions should be conducted, provided they outnumber 15% to run such optimizations, (previously, it was recommended to run such optimizations if “other” personnel outnumbered 40% of the average nationwide number of medical doctors and paramedics). ●