INSTITUTE FOR THE ECONOMY IN TRANSITION

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RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES

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The economy and politics in August 2001

Despite numerous gloomy forecasts (regarding an alleged Rb.and USD depreciation), last August has proved to be a very calm month in the political and economic life of the country. The legislature and the high executive authorities went for their vacations.

Against such a background, the discussion in the government on the issue of establishment of a single tariff agency, the draft 2002 budget, measures on Russia's joining WTO can be considered as one of intermediary stages on the way to solving the noted problems.

The contents of the Decree on establishment of a single tariff regulatory agency on the basis of the Federal which specific price and tariffs would fall within the powers of the newly created agency and which not. The liberal hue of the economic policy currently pursued by the Cabinet allows no prophecies on transformation of the STA in Goskomtsen. However one should understand that the newly created agency will not be able to avoid a considerable lobbyist pressures on the part of certain regions (for example, Kuzbass). Clearly, the coordination of interests of natural monopolies and the whole economy mostly is a political problem. The real efficacy of STA operations mostly will be determined by the government's ability to effectively pursue a consistent liberal economic policy, so distancing itself from concrete business groups and having a clear vision of the purposes and priorities of the country's economic development.

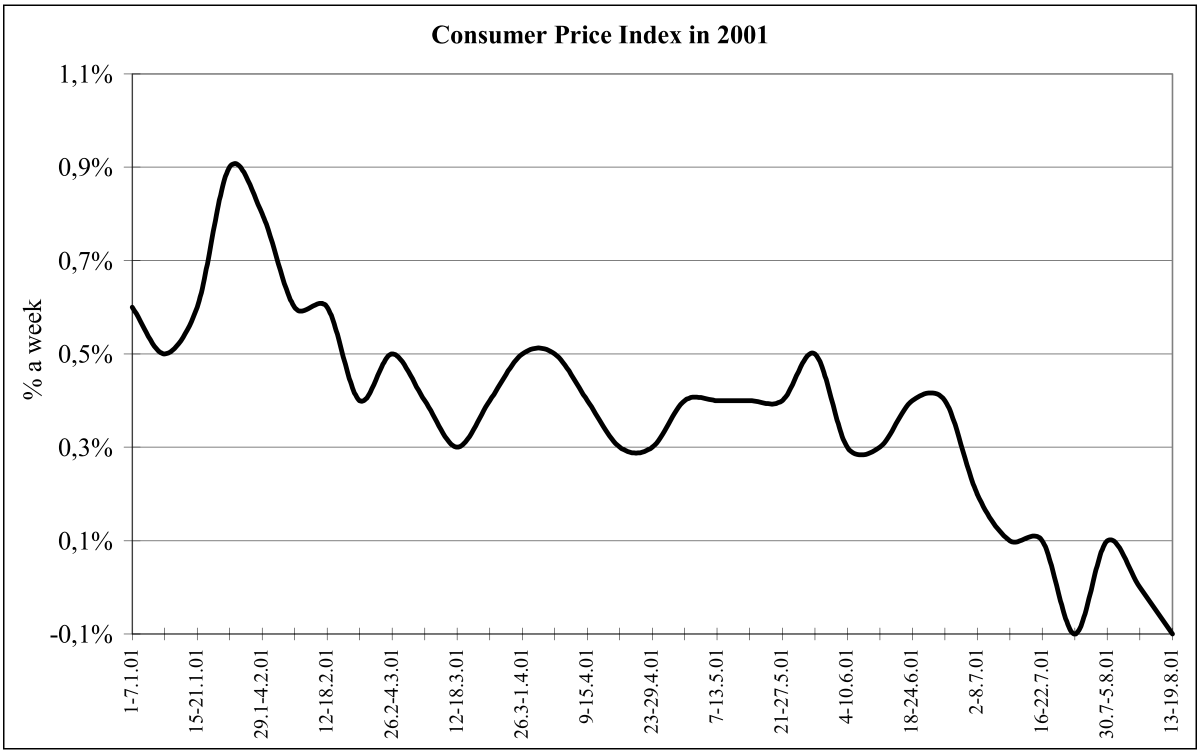
The active contribution of the Presidential Administration in establishing a Council of Small and Medium-Size Businesses alternative to the Russian Council of Industrialists and Entrepreneurs shows that the executive power realizes the specifics of and is ready for discussion with representatives of various strata of entrepreneurs. At the same time, similar to the attention paid to initiatives of the Union of Small Towns, such a support constitutes a logical component of the general strategy on dividing political and economic areas, establishment of a clear structure of the division of powers between the government, on the one hand, and economic agents (including territories among others), on the other.

T. Drobyshevskaya

Monetary Policy

In July 2001 the inflation rate fell considerably (see Fig. 1). The month ended up with the CPI rate being at the level of only 0.5%. Notably, it was summer 1998 that was the last time when a lower inflation rate was fixed. In July the prices for services once again outgrew prices for other commodity groups. Namely, the service price index increased by 2.9% (prices for housing – by 5.5%). The prices for non-food goods increased by 0.5%[1] , but prices for food stuffs declined due to seasonal factors (-0.3%).

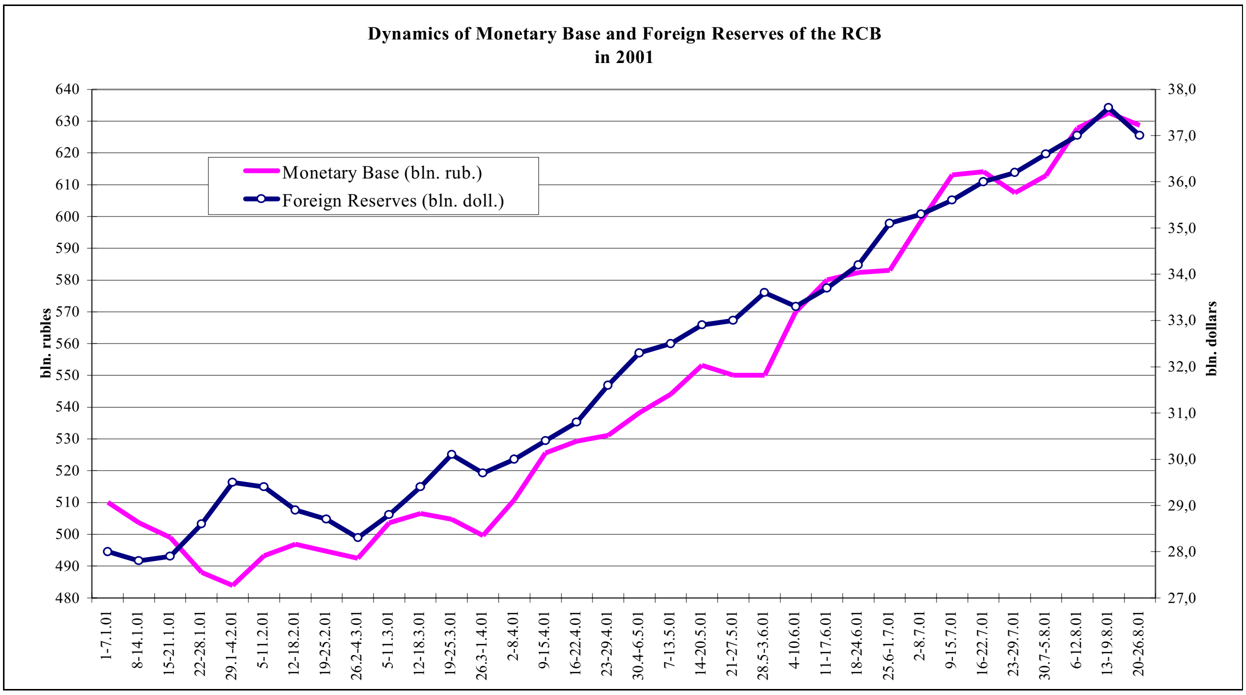
FIGURE 1.



[1] The petroleum prices decreased by 0.8%.

According to the preliminary data, in August zero inflation rate was observed. Thus, taking into account the summer decline in price rise rates the inflation forecast for 2001 can be adjusted to a lower value. In our view, in 2001 the CPI growth remains at the level of 2000, i.e. between 20% to 21%, though it is higher than the values projected in the Federal budget law.

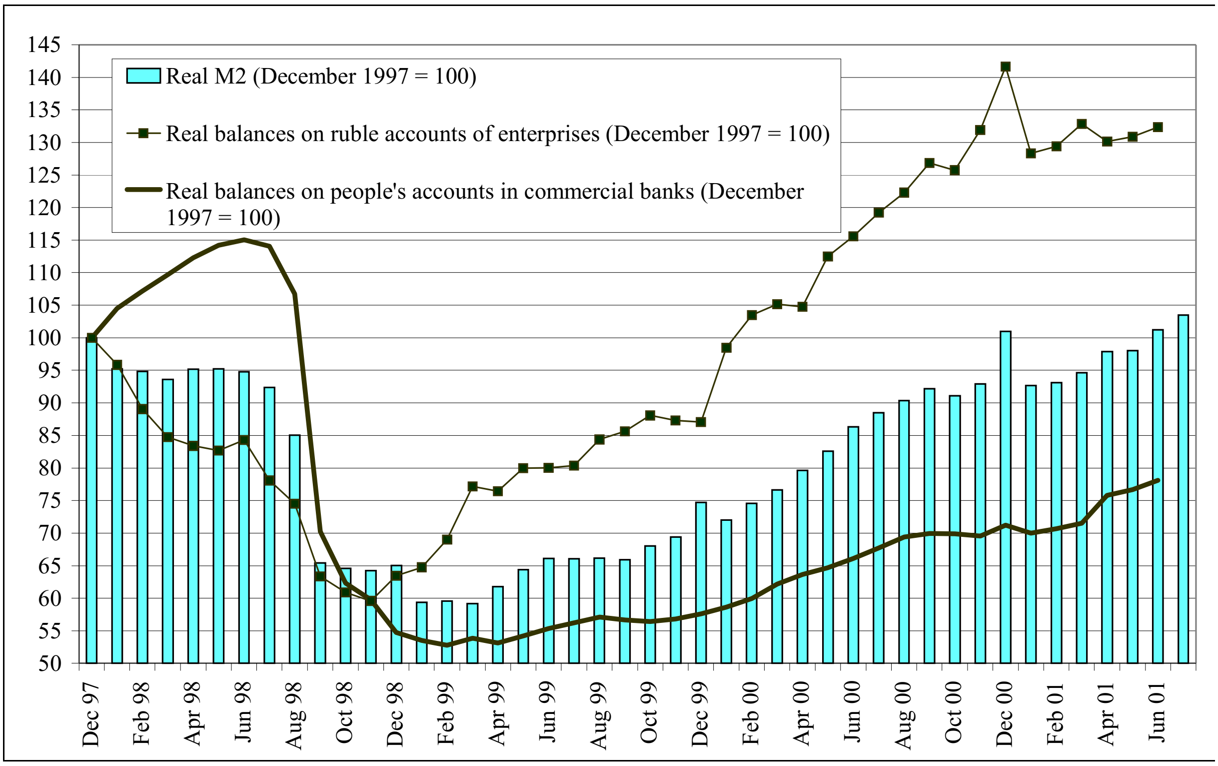
FIGURE 2.



After some deceleration in the second half of July, the rates of money supply growth once again accelerated in August (see Fig. 2). The increment of narrow monetary base made up 4.13% for the first three weeks of the month. At the same time, the Bank of Russia's foreign reserves grew by more than 1 billion USD and reached \$37.6 billion. However, in the second half of August the foreign reserves fell at \$600 million, because of selling foreign exchange to the RF Ministry of Finance to pay on the Russian foreign debt. Namely, in August 2001 about \$1.3 billion were paid to foreign creditors.

According to the data published by the Russian Central Bank, by the end of July 2001 the broad monetary aggregate M_2 reached 1330.2 billion roubles, i.e. at 16.25% higher than its respective value as of January 1, 2001. In real terms, M_2 exceeded the previous post-crisis

FIGURE 3.



peak (December 2000) and presently amounts to 103.5% vs. the level of December 1997. The analysis of the M_2 structure (see Fig. 3) shows a recession in growth rates of balance on enterprises' rouble accounts, while balances on households' accounts in banks grew. Thus, by the end of July 2001 the real balances on enterprises' rouble accounts amounted to 132.4% relative to the level of December 1997 (141.6% in December 2000), i.e. they increased by 3.2% between January to July 2001. The households' real bank deposit balances grew by 11.5% over the same period and made up 78.1% against December 1997. In our view, this tendency testifies to an increase in households' disposable income as well as to some restoration of confidence in banking system. Since the shares of expenditure on foreign exchange purchases in 2000 and 2001 are almost equal (5.5–6.5% of expenditure), it is evident that the increase in savings was made in the form of bank deposits.

The recession in growth rates of balances on enterprises' accounts, in our view, can be explained by the achievement of a 'saturation' level in monetization under the present conditions. As the IET surveys showed (see the respective section of the IET monthly reports for May – July 2001), during the period in question the share of money in payments between enterprises was almost stable or even fell in some industries,. Hence, while the financial sector develops slowly and the interrelations between real and financial sectors are weak, one can expect stabilisation of the demand for real money balances.

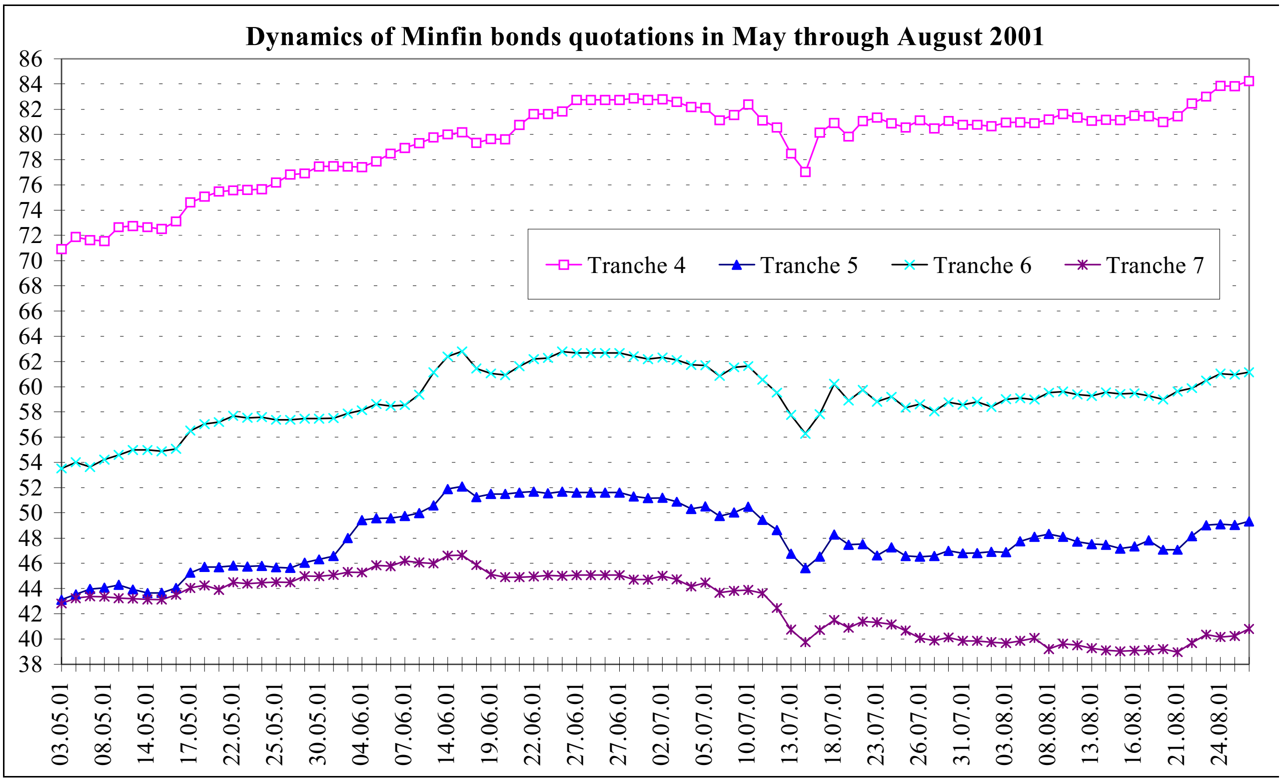
S. Drobyshevsky

Financial Markets

The government securities market

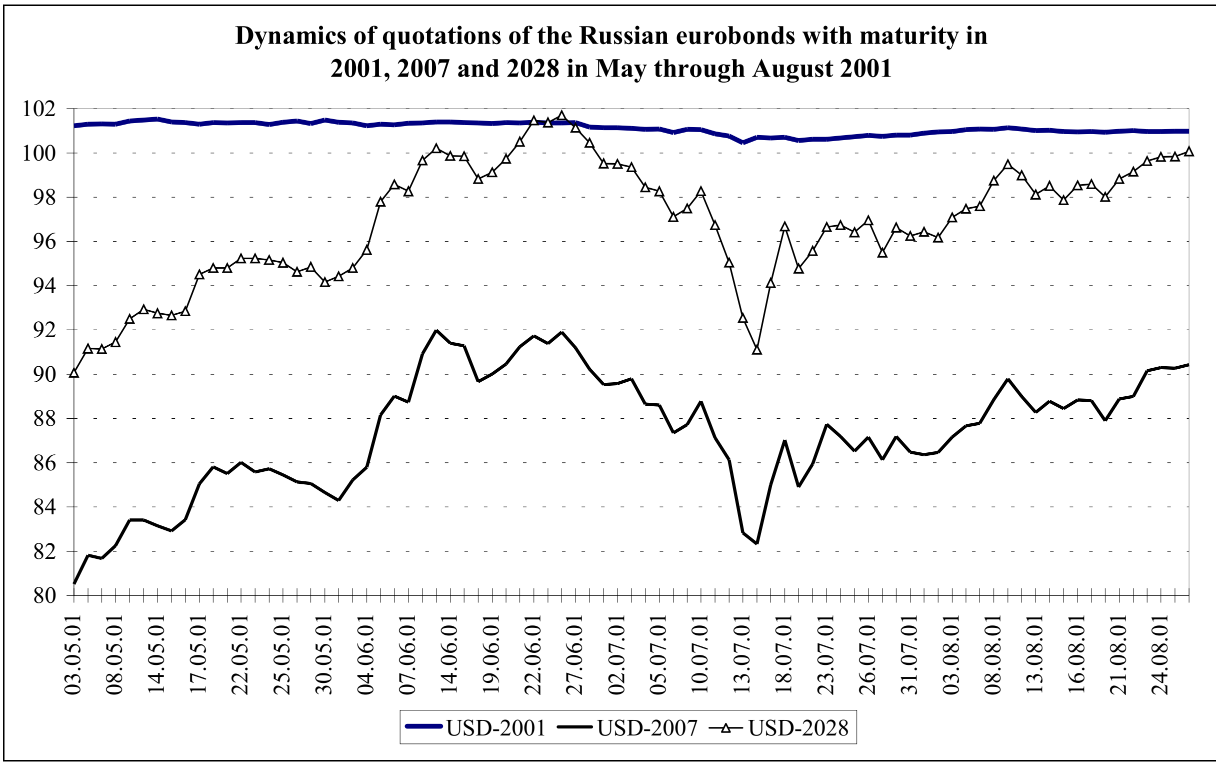
After some stagnation during the summer 2001, in late August the prices for the Russian foreign debt securities grew (see Figs. 1 and 2) and broke record values. The yields to maturity on the Minfin bonds decreased to 13.5–15.5% annualised, and the yields to maturity on eurobonds did not exceed 13% annualised. The yield on the shortest eurobonds matured in November 2001 fell to 4.6–4.7% annualised. Thus, the Russian debt liabilities remained practically unaffected by events at other emerging markets (in particular, in Argentina), and investors' confidence in the Russian securities is higher than the one in other countries' papers that have a similar international rating.

Figure 1.



In August 2001 the average-weighted GKO/OFZ yield dropped down to their minimal values – 15.6–16.0% annualised, while yields on the longest bonds did not exceed 19% annualised. Hence, taking into account the envisaged inflation rates, the real costs for borrowing at the domestic market are negative. In August, two new issues were placed – five-month GKO 21153 and three-year OFZ 27015. The auctions should be considered rather successful for the Ministry of Finance, because about 75% of the supplied volume was placed at market rates. In June and July only 50–60% of the issue volumes was placed at the auctions.

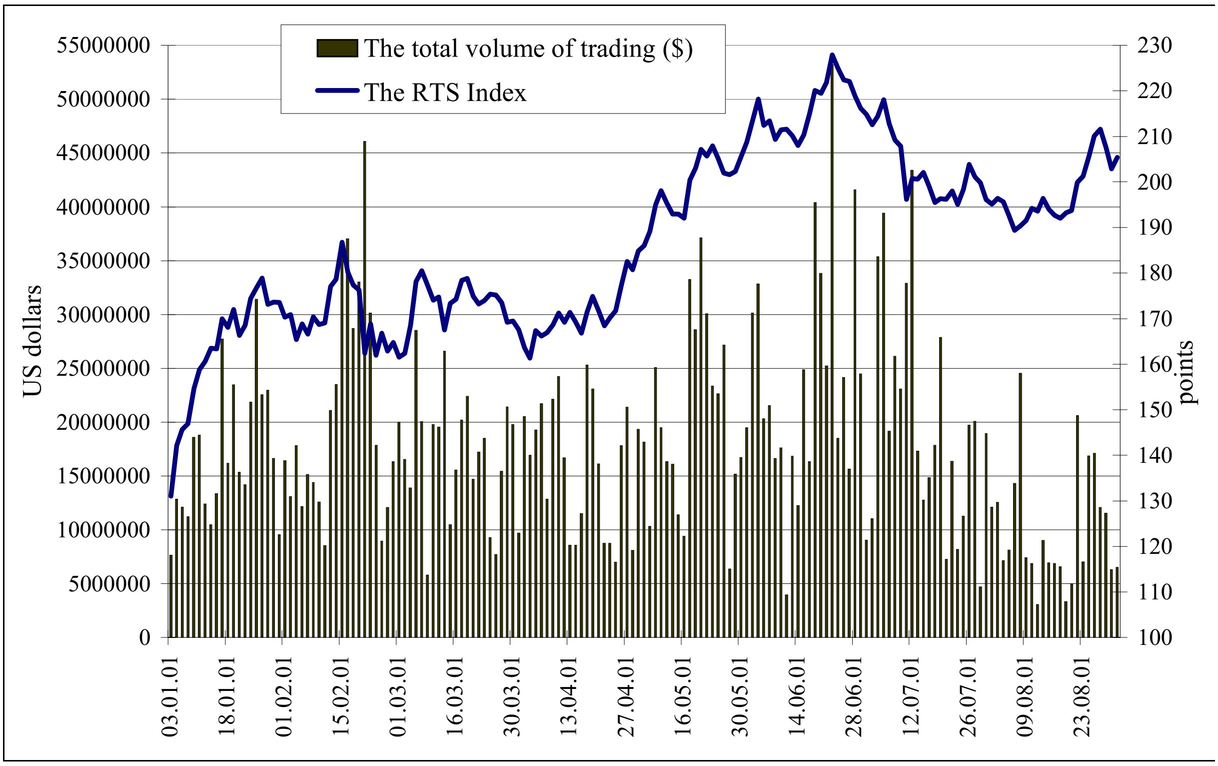
FIGURE 2



Stock market

In late August the Russian stock market revived. However, on the backdrop of a very low turnover a side trend prevailed over the month. The 'vacations' season, negative news from the emerging stock markets and expectations of economic crisis in the USA affected the market situation. Judicial inquiries involving the biggest Russian corporations also did not add optimism to investors.

FIGURE 3



On the whole, the RTS Index grew up at 9.29 points (4.74%) over the month at trade volumes dropping near twice against July (by 46.9%) and reaching the minimum value in 2001 – $232 million. The average daily trade volume in August roughly accounted for $10 million. Between August 13 to August 17 the trades were extremely sluggish, and the trade volume amounted to slightly over $32 million over the week, falling to $3.07 million on August 13, i.e. to the year minimum. During the other weeks of August the average weekly trade volume made up about $55 million. Between July 31 to August 21 the RTS Index fluctuated around 193.6 with the three-month minimum 189.38 registered on August 7[1]. Then it rose to 211.59 by August 28, and slid to 205.41 in the end of the month.

In August the prices for the biggest oil companies' stock were growing, but with a great variation in growth rates. The leader among *blue chips* was stocks of "Sibneft" (28.35%) following by "Surgutneftegaz" (11.21%). The quotations of other companies increased to a less degree: "Tatneft" – by 4.84%, "YUKOS" – by 3.35% and "LUKoil" – by 1.09%. Prices for stocks of non-oil corporations mainly fell. The leader was the stocks of "Norilsky Nickel" (-16.33%) and "Rostelecom" (-5.38%). The exception was the stocks of "Mosenergo", which increased almost by 7.1%.

Figure 4

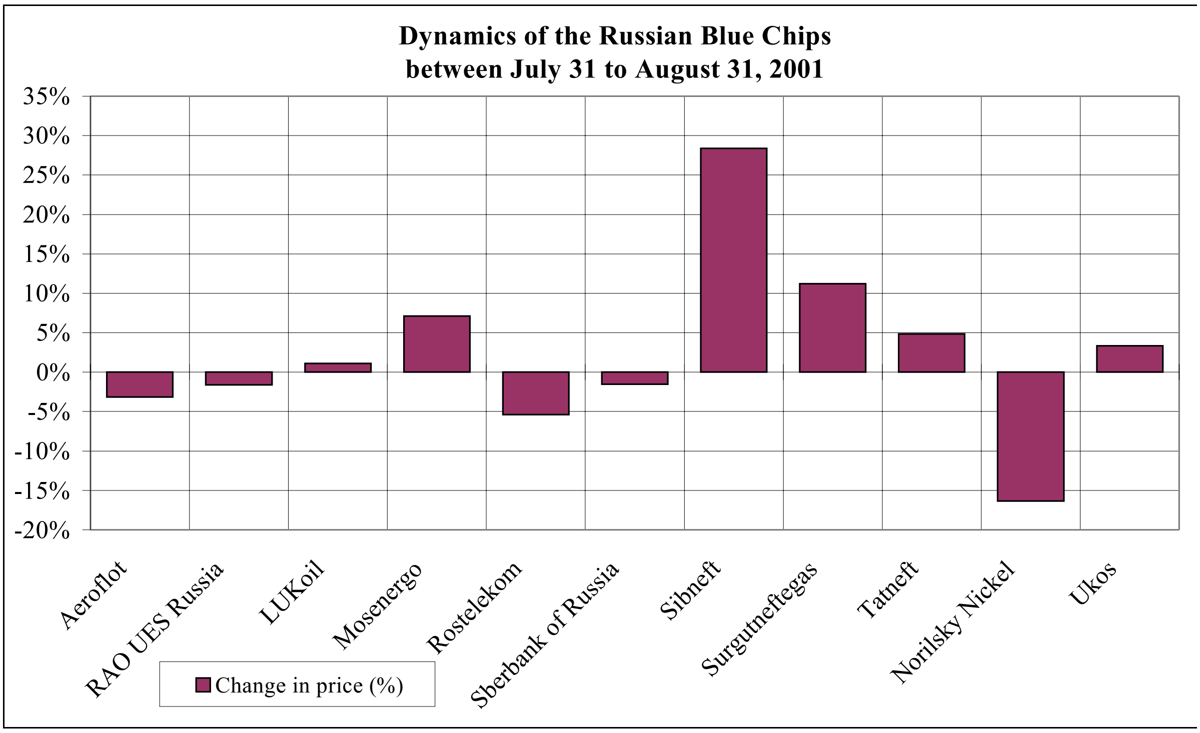
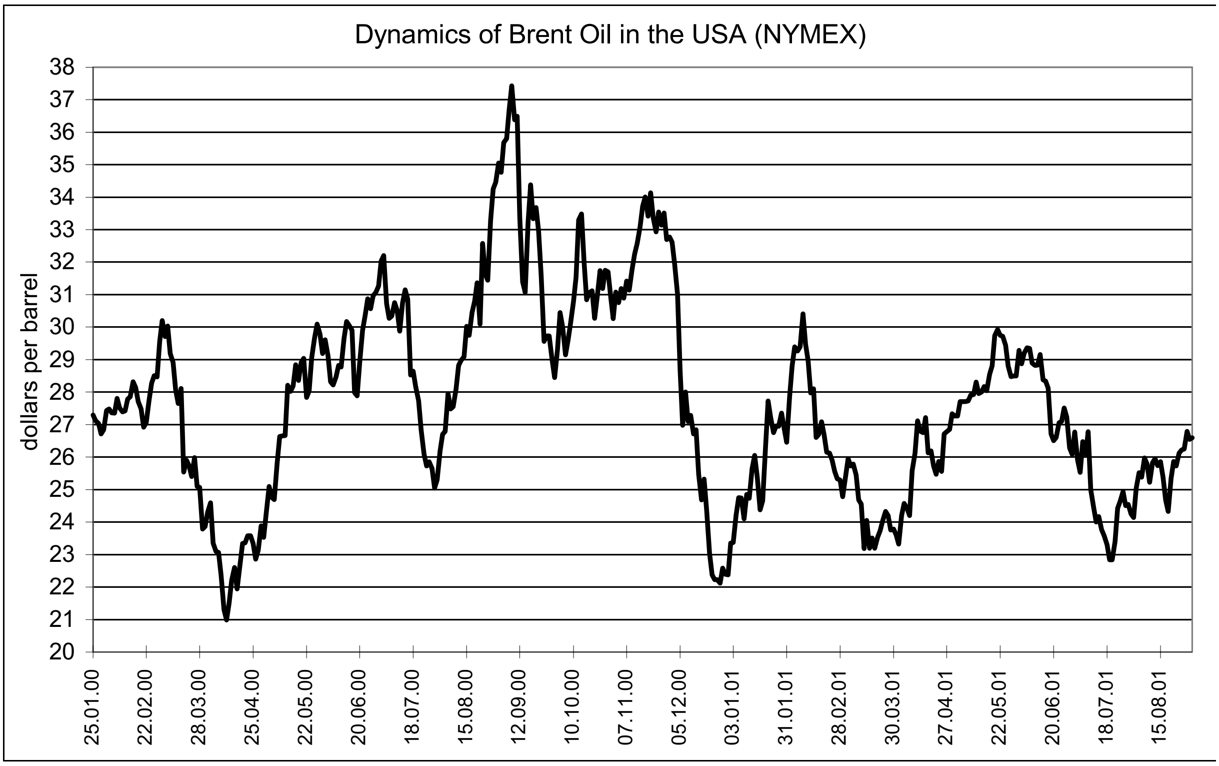


Figure 5.



The share of common stocks of RAO "UES Russia" in the total trade volume in the RTS was 25% (28.8% in July), the share of "YUKOS" – 25.1% (23.3%), "LUKoil" stocks – 15.2% (12.4%), "Surgutneftegaz" – 8.0% (8.1%), "Tatneft" – 6.3% (3.7%). Thus, in August the total share of the five most liquid stocks in the RTS was 79.6% (in July – 81.2%).

The main external factors influencing the prices for shares in the Russian stock market were as follows.

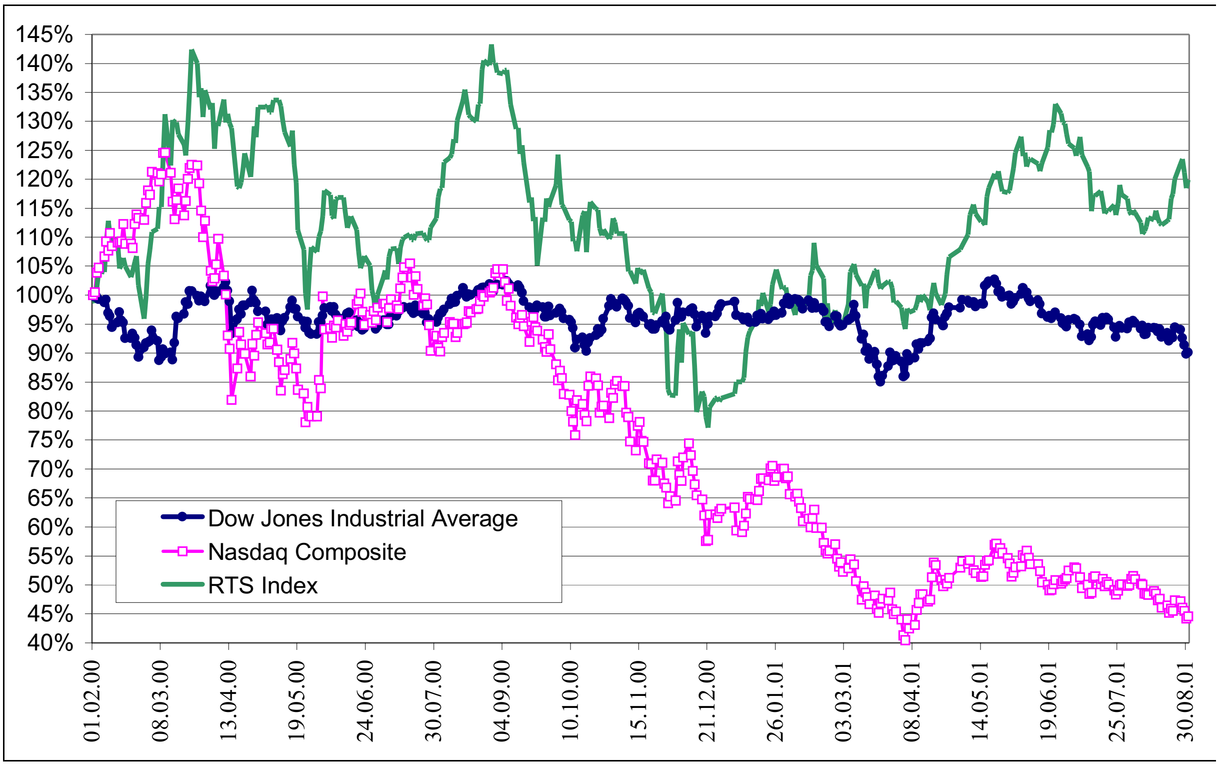
An unfavourable situation in stock markets of main developing countries, in particular in Argentina, discouraged investors' interest in all emerging markets. However, the IMF statement on its readiness to provide Argentina with a stabilisation loan up to $8 billion added optimism, and between August 17 to August 24the MSCI grew by 2.6%.

On August 21 the Fed Open Market Committee the sixth time this year decided on the next, , reduction in the Federal Funds rate. Presently, the rate was lowered by another 0.25% and, thus, dropped to 3.50%. This is the minimum value since April 1994.

The economic recession in the USA and many Western European countries induced a decline in demand for energy resources and, so some fall in oil prices. But, after the American Oil Institute lifted up its forecast for "black gold" price in 2002, the BRENT price rose by 5.8% between August 20 and August 24. Another contribution to the oil price growth was the data on the reduction in oil reserves in the USA and the Western Europe by 5.3 million barrels over last week.

August did not bring confidence into the US stock market, and the main indices fell there: in early August NASDAQ sank below 2000 points, and by the end of the month the DJIA slid below 10000 points. In total, the DJIA lost 573.1 points (-5.4%) and NASDAQ – 221.7 points (-10.9%) for the month. As before, the NASDAQ fall was determined by unfavourable corporate news from "new technologies" sector. CSFB downgraded stocks of some semiconductor produces, Cisco reported a lower expected profit for the current quarter. Dell Computers and Hewlett-Packard announced possible downsizing. Good news is that numerous bad external factors did not induced collapse in the Russian market. However, this conclusion can be questioned because of extremely low trade volumes.

Figure 6.



Corporate news

In addition to positive oil price dynamics, another factor contributing to the increase in prices of "Sibneft" stocks was the news on intermediate dividends for 2001 at a rate of 3.79 roubles per share (in all about 17.97 billion roubles): so high dividends have been never paid by a Russian oil company. However, such a high dividend sum (which is comparable with the company's net profit for 2000) raises questions about the company's prospects.

Moody's ranked Tyumen Oil Company (TNK) at Ba2, i.e. higher than the Russia's sovereign rating. Nevertheless, the TNK stocks are not traded yet on stock exchanges, and the news will have a certain impact on quotations of other biggest oil companies.

On August 14 "LUKoil" finally published its financial accounts for 2000 in accordance with GAAP procedures. The net profit amounted to $3312 million, profit per share – $4.8. The market actually did respond to this news, as the publication was heavily postponed and the results did not outperform the foreseen ones.

The Price Waterhouse Coopers' examination showed that the relations between "Gazprom" and "Itera", the biggest domestic gas companies, are consistent with the Russian legislation.

The performance of "Aeroflot in 2000 measured in accordance with GAAP procedures turned to be higher than expected, but the corporate governance risk restrains the prices for the stocks. Investors are waiting for an early meeting of shareholders, due to August 6.

In August prices for “Mosenergo” shares were affected by two factors: the conflict between RAO “UES Russia” and its affiliate entity, which arose around shareholder’s meeting aimed at the dismissal of “Mosenergo” Head A. Remizov. The conflict had a certain negative effect. However perfect fundamentals pushed up the quotations. Thus, the net profit of “Mosenergo” in the first half of 2001 (according to the Russian accounting standards) increased nearly by 6 times compared to the respective period of last year and amounted to about 2.7 billion roubles.

The Russian FCSM licensed the OAO “Petersburg telephone network” to issue the first - level ADR. The number of possibly converted shares, with 1 Rb/-worth face-value, amounts to 350062150 with. One ADR represents 50 common shares of “PTS”. The expected timing of their entry to the US and European markets falls within the end of the 4Q, 2001.

On August 21 RAO “Norilsky Nickel ” finished the exchange of its shares of into the shares of AO MMC (Mine-metallurgical Company) “Norilsky Nickel”, which was implemented under the restructuring of the company. In total, 97% of shares was exchanged. After the exchange the RAO will become a 100% affiliated entity under the MMC. It is expected that the MMC “Norilsky Nickel” shares will be traded in RTS in early-October.

We should also note that another court examination related to restructuring, which paralysed trades on the RAO “Norilsky Nickel” shares on main stock markets. A district court in Kemerovo region took a suit (applied by a shareholder possessing three stocks) and forbade the MMC using the name “Norilsky Nickel” and implementing any actions aimed at listing shares of OAO MMC “Norilsky Nickel” at the Russian and foreign stock exchanges. The next corporate blackmail once again highlighted the lack of legal protection of the domestic companies and affected the Russian company’s image.

The Swiss banking group USB AG placed three-year converted bonds, which are collated by “YUKOS” shares. The demand for these securities exceeded the supply and, probably, the underwriter had to buy additional shares to collate bonds. This fact explains the record turnover of “YUKOS” shares on August 8, which amounted to over $19 million. However, the operation brings potential pressure on “YUKOS” stock prices, as the bond holders will gain profits converting bonds to stocks under a low coupon rate.

Table 1.Dynamics of the Foreign Stock Indexes

as of August 31, 2001	Value	change for last week (%)	change for last month (%)
RTS (Russia)	205.41	4.74%	44.5%
Dow Jones Industrial Average (USA)	9949.75	-5.4%	-8.8%
Nasdaq Composite (USA)	1805.43	-10.9%	-29.7%
S&P 500 (USA)	1133.58	-6.41%	-14.98%
FTSE 100 (UK)	5345.00	-3.33%	-13.59%
DAX-30 (Germany)	5188.17	-11.48%	-18.64%
CAC-40 (France)	4689.34	-7.79%	-19.37%
Swiss Market (Switzerland)	6582.40	-3.87%	-18.90%
Nikkei-225 (Japan)	10713.51	-9.67%	-21.75%
Bovespa (Brazil)	12840.60	-6.64%	-22.99%
IPC (Mexico)	6310.700	-2.53%	4.34%
IPSA (Chile)	114.28	3.17%	13.38%
Straits Times (Singapore)	1619.12	-2.82%	-17.02%
Seoul Composite(Korea)	545.11	0.66%	-2.31%
ISE National-100 (Turkey)	9878.88	-0.36%	-3.13%
Morgan Stanley Emerging Markets Index	230.845	-1.19%	-10.80%

Foreign exchange market

In August 2001 the rates of official rouble nominal exchange rate devaluation slowed down despite an increase in the demand for foreign exchange on the part of the RF Ministry of Finance and the Bank of Russia (see section *Monetary policy*). The reduction in the compulsory export receipts sales rate from 75% to 50% had practically no effect on the exchange rate dynamics, but turnovers at the morning session fell nearly one and a half times, i.e. in proportion to the reduction in the compulsory sales rate.

In August 2001, the official dollar exchange rate grew from 29.27 roubles/$ to 29.37 roubles/$, i.e. by 0.34% (4.16% annualised, see Fig. 7). The 'today' dollar exchange rate in the SELT declined from 29.337 roubles/$ to 29.3613 roubles/$ (as of August 27), i.e. by 0.08%. The 'tomorrow' dollar exchange rate grew from 29.3472 rubles/$ to 29.3625 rubles/$ (as of August 27), i.e. by 0.05%. According to preliminary estimates, in August the trading volumes by dollar in the SELT amounted to 90 billion roubles at most.

FIGURE 7.

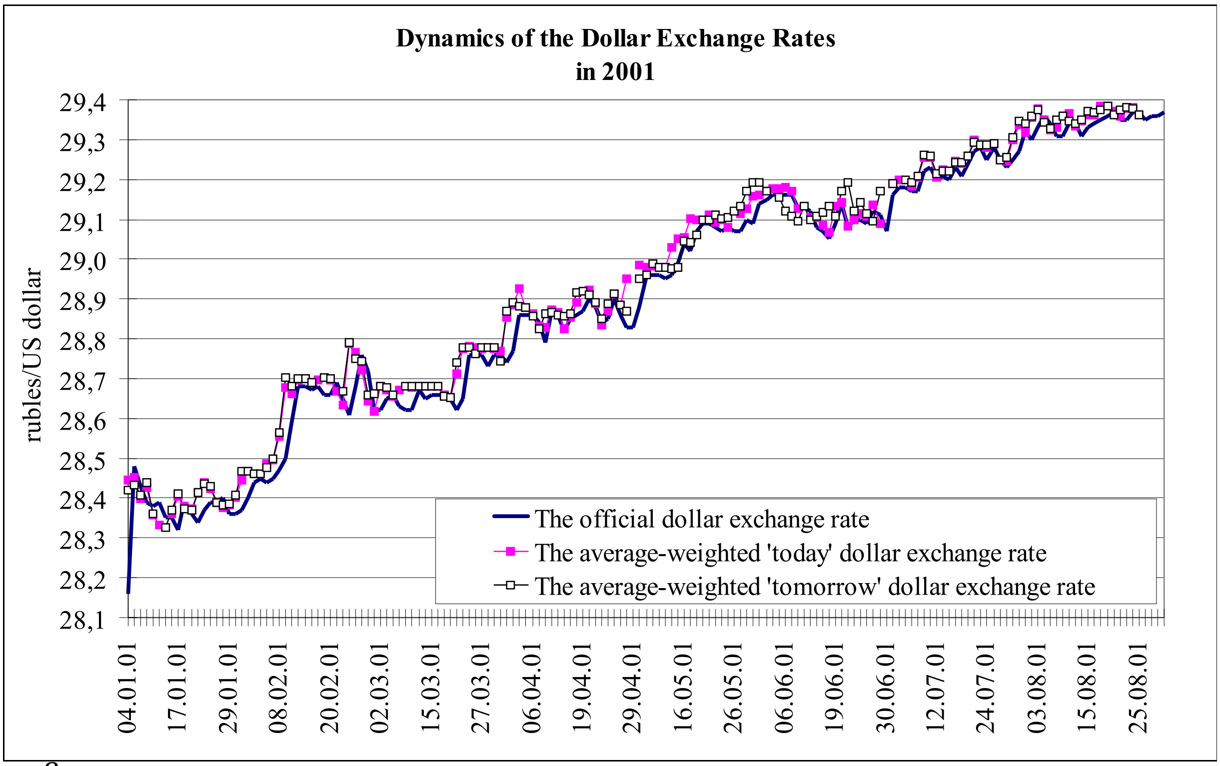
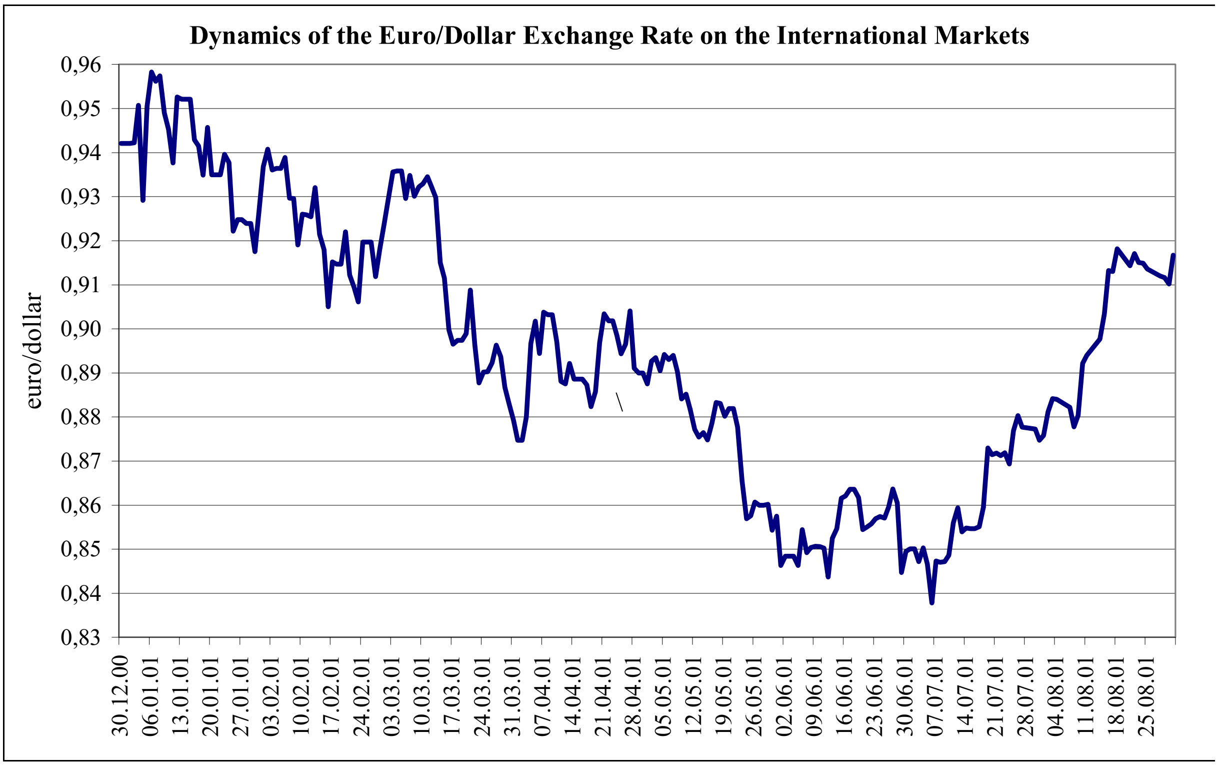


FIGURE 8.



In August 2001 the euro continued its strengthening against the US dollar (see Fig. 8). By the third decade of the month the "euro/dollar" exchange rate reached its five-month maximum – 0.917 $/euro. In the late August the exchange rate remained stable. The fundamentals both in the USA and the EC are weak and show no signs of overcoming the recession, and the further dynamics of the euro exchange rate is determined by economic agents' expectations., One can consider the presentation of euro notes and coins made by the ECB in early-September in Germany a positive factor effecting the expectations.

In August 2001 the euro/rouble exchange rate also rose sharply. The rouble/euro official exchange rate decreased from 25.6 roubles/euro to 26.67 roubles/euro, i.e. by 4.18%, over the month (see Fig. 9). According to preliminary estimates, in August 2001, the total trading volume on euro in the SELT made up about 2.8 billion roubles.

FIGURE 9.

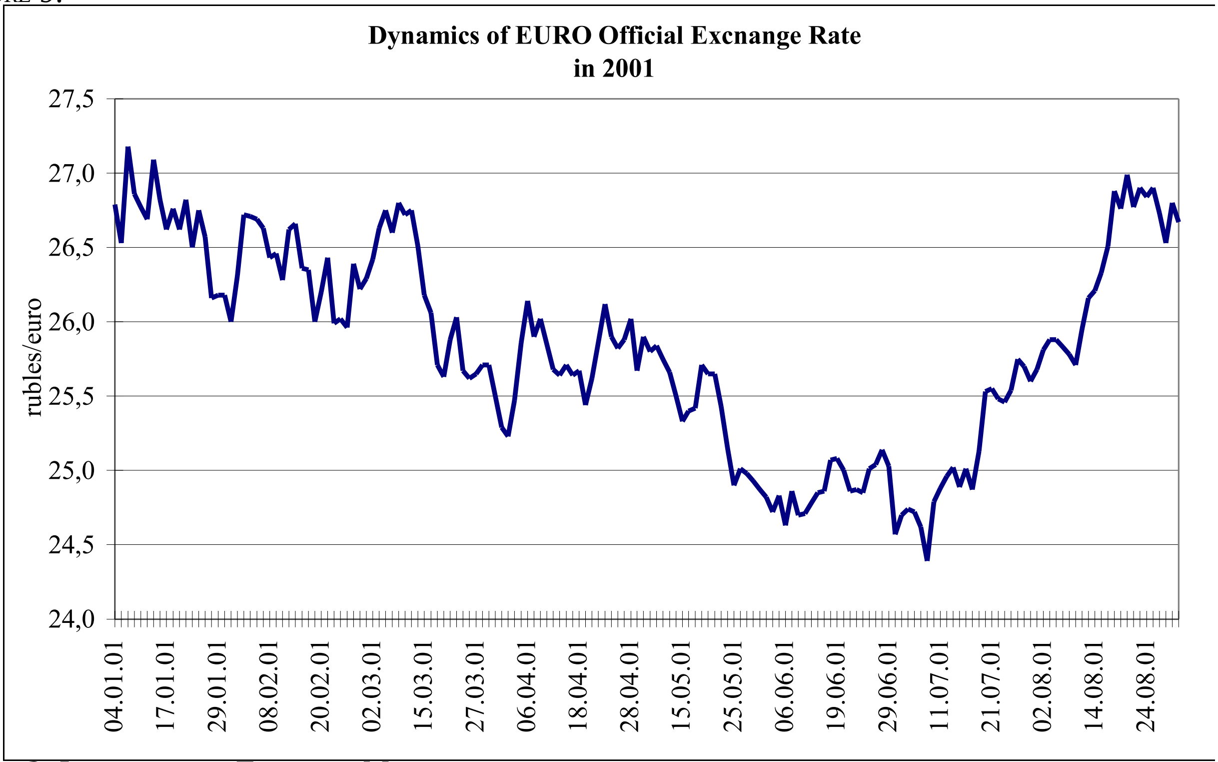


TABLE 2. INDICATORS OF FINANCIAL MARKETS

	April	May	June	July	August*
inflation rate (monthly)	1.8%	1.8%	1.6%	0.5%	0.0%
annualised inflation rate by the month's tendency	23.87%	23.87%	20.98%	6.17%	0%
the RCB refinancing rate	25%	25%	25%	25%	25%
annualized yield to maturity on OFZ issues	16.33%	17.11%	17.03%	17.19%	16.5%
volume of trading in the secondary GKO-OFZ market a month (billion rubles)	15.14	7.98	7.92	11.67	8.5
yield to maturity on Minfin bonds by the end of the month (% a year):					
4th tranche	22.12%	17.37%	13.91%	15.90%	13.7%
5th tranche	17.55%	16.34%	14.59%	16.29%	15.5%
6th tranche	17.71%	15.88%	14.01%	15.54%	14.8%
7th tranche	13.83%	13.09%	13.26%	14.79%	14.6%
8th tranche	17.57%	15.71%	13.93%	14.76%	14.3%
INSTAR – MIACR rate (annual %) on interbank loans by the end of the month:					
overnight	24.50%	13.87%	29.95%	25.3%	8%
1 week	28.06%	8.52%	29.49%	14.0%	12%
official exchange rate of ruble per US dollar by the end of the month	28.83	29.09	29.07	29.27	29.37
official exchange rate of ruble per Euro by the end of the month	25.67	24.87	24.57	25.60	26.67
average annualized exchange rate of ruble per US dollar growth	0.31%	0.90%	-0.07%	0.69%	0.34%
average annualized exchange rate of ruble per euro growth	1.50%	-3.12%	-1.21%	4.19%	4.18%
volume of trading at the stock market in the RTS for the month (millions of USD)	329.1	405.7	490.4	436.8	232.0
the value of the RTS Index by the end of the month	180.68	208.80	216.11	196.12	205.41
growth in the RTS Index (% a month)	6.62%	15.56%	3.50%	-9.25%	4.74%

S. Drobyshevsky, D. Skripkin

The real sector: factors and trends

The current macroeconomic situation in the country is determined by the ongoing trends to production expansion in all the sectors of the economy and particularly in the industrial sector. Between January through July relative to the respective period of 2000 the increment in industrial output accounted for 5.4%, construction- 6/4%, and agriculture – 6.1%. The dynamics of economic growth finds itself under practically equal impact of both domestic and external demand. However, since the second quarter 2001 the investment component has strengthened its positive impact on dynamics of GDP and output of goods and services in the basic sectors.

According to the RF Ministry of Economic Development and Trade, it was investment sectors that demonstrated the highest growth rates, with the index of industrial output across the sector accounting for 109.8% over the first half 2001. In particular the growth in investment machine engineering sector impacted the dynamics of output in the machine engineering sector and the industry of construction materials. In the conditions of stabilization of socio-economic and political situation in Russia and improvement of the business environment, banks, enterprises and foreign investors alike intensified their operations related to financing investment projects in the real sector. Between January through July 2001 the increment of investment in capital assets accounted for 7.3% vs. the respective period of the prior year, however the components of domestic demand and primarily investment activity in the economy requires governmental support.

Despite some changes noted in the beginning of the year, there is a remaining substantial gap between export-oriented and domestically- centered sectors. According to some experts, roughly a half of hidden capital export is related to the export of energy sources, a. 1/3 – to the export of ferrous and non-ferrous metals, while the hidden capital export is estimated being at the level of a. 40% relative to the official sectoral export of metallurgical products, a. 25% - of the output in the sector for chemicals and petrochemicals, and under 20% - of the output in the fuel sector, which objectively experiences a sharp need in investing in Russia. The solution to this problem is directly related to the development of the system of investment institutions that could manage financial resources created by the national economy as well as external investors' resources that could be accumulated in Russia.

The urgent necessity of a practical resolution of the problem is also dictated by the fact that the possibilities for meeting the growing consumer demand and production expansion are constrained by a low capacity of domestic processing sectors compared to import as well as by the lack of enterprises' own resources for a qualitative renewal of their machinery and equipment stock.

During the period in question the growth rate across the consumer sectors accounted for 106.5%, while in the light industry the respective index accounted for 105.7%. However the situation is not ambiguous, because in the course of a gradual comeback of imports to the domestic consumer market many enterprises cannot survive competition: the sewing and footwear sectors once again have reported production decline. The advanced growth in output in the light industry compared with the development rates of the industrial output on the whole has been supported by the textile industry and the production of fur clothes.

At the same time the food-processing sector has proved to be fairly successful in retaining its position in the market. During the period in question the increment in its output accounted for 7.2% vs. the respective period of 2000, and since February this year the sector showed a regular positive dynamics of production development. It was the meat-processing, butter, confectionery, tea and tobacco sub-sectors that were especially successful in terms of expansion of their domestic markets, while some gaps between demand and offer naturally are filled in with import supplies.

According to the RF Ministry of Trade and economic development, the proportion of import goods in the volume of consumer resources tradable on the market in the Ist half 2001 accounts for 40%. A low competitiveness of domestic goods compared to imports did not allow a flexible reaction to the growing consumer demand. The price factor that impacts the gowth in the population's demand for domestic goods has come to its exhaustion, because the suppliers of import goods increased the volume of their supplies of relatively inexpensive consumer goods to the country.

The positive trends in the dynamics of households' consumption were based upon a positive dynamics of real disposable incomes of the population. When compared with the time period between January to July 2000 the latter grew by 5.4% and the real salaries and wages showed a 18.0% growth, however they are still substantially lower than the respective indices of the ist half 1998. The dynamics of retail trade turnover showed much higher growth rates compared to the population's incomes which allowed an excess of the maximal level of retail trade turnover registered in late 1997. That was determined by a shift in the population's structure of purchases in the post-crisis period towards cheaper goods and the contraction in the population'' monetary savings. In the short run this encourages the domestic demand and creates prerequisites for production growth, however it would lead to slowdown in growth and the consequent decline in the savings rate in the economy in the longer run.

The change in the share of savings in 2001 found itself under a substantial impact of the lowering profitability rate in the production area. The level of enterprises and organizations' receipts across the economy on the whole fell roughly by 3.7 per cent points compared with the 1st half 2000. There is a remaining structural distortion in income distribution across sectors of the economy: the proportion of industrial entities' profits in the overall balance-sheet profit roughly accounts for 53%. The export-oriented sectors show a growing profit rate against the backdrop of general stabilization of profit rate in the industrial sector. It is the fuel and energy sub-sector and other export –oriented sectors that still contribute considerably to the formation of the overall financial performance as well as to results of the industrial sector's financial performance (with their proportions accounting for 27.3% and 15.3%, respectively). Under a fairly favorable situation in the foreign trade area for the products of the fuel sector and the non-ferrous metallurgy they both report profit rates exceeding the average sectoral level across the whole industrial sector. At the same time between January to May 2001, under the effect of the growing domestic demand some sectors, including machine engineering and metal processing and food processing sector have improved their financial performance and their balance sheet profit grew 1.3 and 1.5 times, respectively. With the demand for investment goods rising, the profit rates in the machine engineering sector grew considerably, due to an advanced price rise for machinery and equipment compared to price dynamics for construction materials.

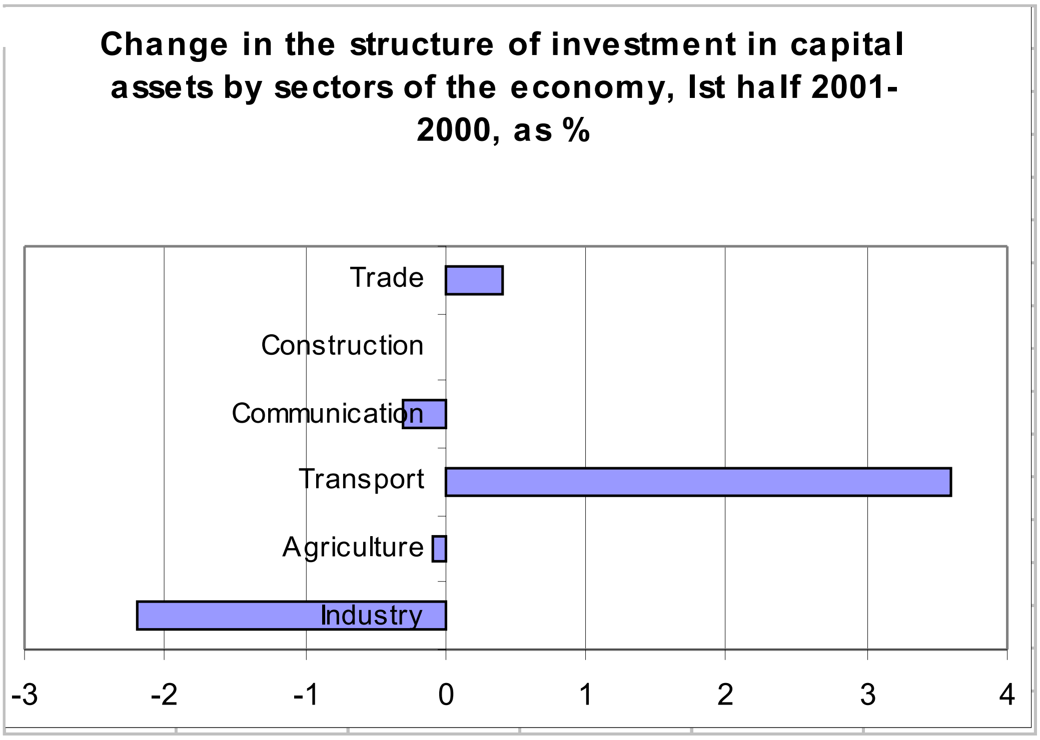
In addition, the change in enterprises' profitability rate and financial performance became affected by opposite trends. On the one hand, a relative drop in prices for import goods generated by the appreciation of Rb. vs. USD have constrained a rise in producer prices to the extent of the rise in their production costs. However, on the other hand, the rise in prices and tariffs for natural monopolies' services and products along with the growth in salaries and wages has formed conditions for price rise. Nonetheless, between June to July the negative effect of such factors has weakened substantially, and inflation rate accounted for 0.5% vs. the average index of 1.8% noted over the last six months, which allows positive estimates of the further growth in the economy.

O. Izryadnova

Investment in the real sector

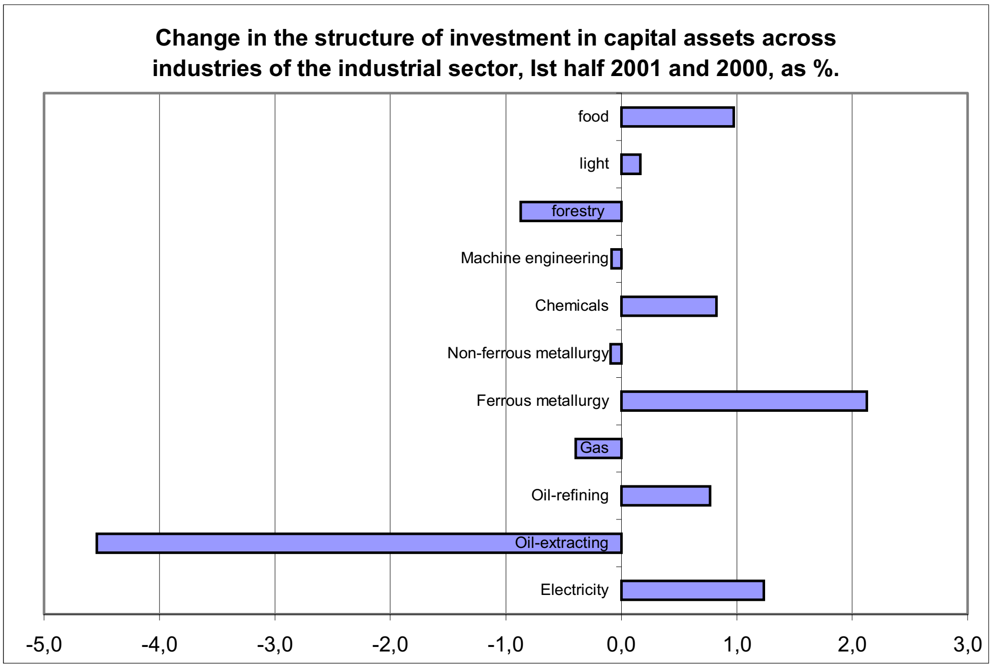
According to Standard &Poor's, due to positive changes in investment and business environment this year Russia's credit rating was increased up to "B+". In 2001there is an ongoing trend to growth in investment demand. Between January to July 2001 the volume of investment in capital assets from all the sources of financing accounted for Rb. 7000 bln. so exceeding the level noted in the respective period of the prior year. The Ist half 2001 was characterized with an advanced growth in investment demand in the sectors for services. When compared with the first half 2000, the proportion of investment in transport and communication in the overall volume of spending on capital assets reproduction in the real sector grew nearly by 3 per cent points, while in the trade sector – by 0.4 p.p.

Fig.1



The dynamics of investment demand in the sector producing goods has found itself under the most substantial impact of a slowdown in the investment growth rate in the industrial sector. During the period in question, the proportional weight of investment in capital assets in the industrial sector dropped by over 2 per cent points. The major part of investment to capital assets is still used to maintain the current production stock, while just an insignificant part of investment is forwarded to its renewal. The mining and export-oriented sector's free resources still partially serve as a source for capital exportation, while partially they are invested in the mineral sector in a form of import of technological equipment. Given that in 2000 a sharp intensity of investment activity in the industrial sector was fully initiated by the fuel sector, this year the proportion have changed in favor of manufacturing sub-sectors. However, such a redistribution of financial resources remains very insignificant and takes places within the corporate merger framework. As a result, one notes an ongoing trend to the drop in the share of investment in development of domestic machine engineering.

FIG.2



In the Ist half 2001 the positive phenomenon was an increase in the share of investment in the food-processing sector and the discontinuation of the decline of investment in the light industry.

During the past two years it was the sectors related to an intensive development of such segments of consumer market as confectionery, soft drinks, ice-cream, beer, and tobacco that showed the most substantial growth in investment activity.

The investment policy in the confectionery sector is determined both by the specifics of enterprises' locations throughout the country's territory and the market situation. In 2000, the national confectionery industry increased its output by 8%, while according to some forecasts for 2001, it is envisaged that it should rise roughly by another 9.0%. Given that experts of the RF Ministry for Agriculture and Food attribute the growth in output o single kinds of products (caramel) to the introduction of a special customs import duty rate (21%), the growth in output across other kinds of confectionery goods is closely related to the respective production and modernization.

The search for new institutional forms appears an example of diversification of diversification of investment spending. The output of enterprises located in the central European part of Russia accounts for more than 1/3 of the overall output of confectionery goods, while the share of the Northern territories and the Asian part of Russian in the overall output makes up under 3.0%. A high level of transportation costs leads to intensification of price differentiation for confectionery goods across the regions and determines the level and dynamics of consumer demand. In addition, with the volume of purchases of import raw materials being substantial, the production dynamics depends on changes in the situation in the markets for goods and foreign exchange. In order to overcome negative trends and stabilize the situation in the regional and nationwide markets, the confectionery companies attempt to carry out production expansion and introduce changes in the managerial structure. In particular, "SladCo" company that includes AO "Volzhanka (Ulyanovsk), AO "Konfi" (Ekaterinburg) and AO "Zarya" (Kazan) raised its output by 16.7% in the ist quarter this year only thanks to an introduction of a single production management and distribution system for all the noted plants.

Another direction is purchasing modern import technologies. Confectionery plant "Korkunov" (Moscow Oblast) completely attribute the growth in its output to implementation of investment projects aimed at production modernization. In particular, in February 2001 a new 3.5 mln USD-worth Italian line for the production of chocolate was put into operation, and in June the implementation of anew 7 mln. USD- worth project started: that is, the construction of a facility for chokolate production using an Italian equipment.

OAO “Krasny Oktyabr” reached an agreement with EBRD and Rabo Black Earth b.v. (the Netherlands) that manage a venture fund of EBRD on investing USD 1.5 mln.in Oktyabr’s daughter company OAO “Takf” (Tambov Oblast), providing that a modern technological equipment should be installed in newly built production facilities.

Given a high capacity of the national confectionery market, the involvement of foreign capital has intensified. Stollwerk (Germany) began to build a new production facility for Stollwerk Rus in Vladimir Oblast: the company intends to invest as much as DM 32 mln. in that which would allow a 40% increase of the production capacity. In addition, the company has already installed another two production lines at the palnt worth a total of 3.2 mln. DM.

According to the data as of the end of 2000, Netsle that holds control stakes in 6 Russian confectionery factories located in 5 regions invested in them USD 175 mln. Over past 6 years Nestle invested as much as USD 80 mln. in “Rossia” confectionery plant. Considering an intensive rise in demand for instant coffee, Nestle is anxious to hold a substantial niche in this segment of the market. In 2001 AO “Rossia” started producing mixed coffee in small packs, while the first packing line for instant coffee began to operate at AO “Khladopordukt” (Krasnodar Krai”. The total cost of the line accounts for USD 140 mln.

Foreign companies expand the scale of their operations through production diversification and development of the related sectors and production. Holding control stakes in AO “Severnoye Siyaniye” and AO “Moskovsly Margarinovy Zavod”, Unilever announced its intent to invest USD 8-10 mln. in the construction of the first facility of atea-producing factory. The factory should be built in the territory of AO “Severnoye Siyaniye” in early 2002 and will be the biggest production facility of Unilever worldwide.

The owner of two plants (in Tolyatti and in Moscow Oblast), Danon invested USD 4 mln. in the development of Russian diary farms to ensure supplies of raw materials for the factories. In the meantime the company’s suppliers are 10 farms in Tolyatty and 10- in Moscow Oblast. The company plans to proceed with investing in farms at a volume of USD 1 mln. annually.

The US-Russian joint venture “Elinar-Boiler” (Moscow Oblast” placed into operation 6 new poultry-producing lines in the 1st quarter 2001, worth a total of USD 500,000. This would allow the company to double its output. The US partner- UIPDP – plans to quit the joint venture in 8 years and to assign its share to the Russian side. The overall amount of the planned investment in the project accounts for USD 10 mln., of which 90% has been already spent.

There is also some growth in investment in tare-producing and packing enterprises, which, in particular, caused an intensive rise in output in the glass sector.

The “OST” group comprised of several plants producing soft drinks was to start the construction of the biggest (with the annual capacity of 600 – 700 mln. bottles) glass plant in Moscow Oblast in June 2001. The overall cost of the project is accounted for USD 100 mln..

Turkish company SiseCam established a company with foreign participation “Rustzham” in Vladimir Oblast, to produce beer bottles. The overall cost of the project accounts for USD 24 mln.

“Rostar” company – one of the biggest producers of aluminum cans pursues an active policy on promotion canned beer.

The modernization of the national economy is directly dependent on the dynamics of importation of equipment. In 2000, the share of investment in machinery and equipment in the overall volume of investment in capital assets roughly accounted for 20%. According to the RF Ministry of economic development and trade, in 2001 the import of machinery and equipment should rise at 25% compared to the prior year and by the end of the year should account for USD 12 bln. However, even with the advanced rate of the import of machinery and equipment relative to imports on the whole, the share of the former accounts for 21.9% vs. 23.3% reported in the pre-crisis period (1997). In order to encourage reconstruction of the economy, the Commission for protection measures in the foreign trade area has agreed upon a list of sophisticated technological equipment that should fall within a privilege customs regime. The individual customs duty rates should be diminished for such sectors as metallurgy, ship – building and car manufacturing, light and textile sectors, instrument making and food-processing sectors. The customs duty rate for importation of equipment for food, light and textile sectors should be lowered from 10 to 5%, while for the other sectors – from 15 to 10%. Should the economy retain a high rate of economic growth, such measures may help accelerate the production modernization processes.

O. Izryadnov

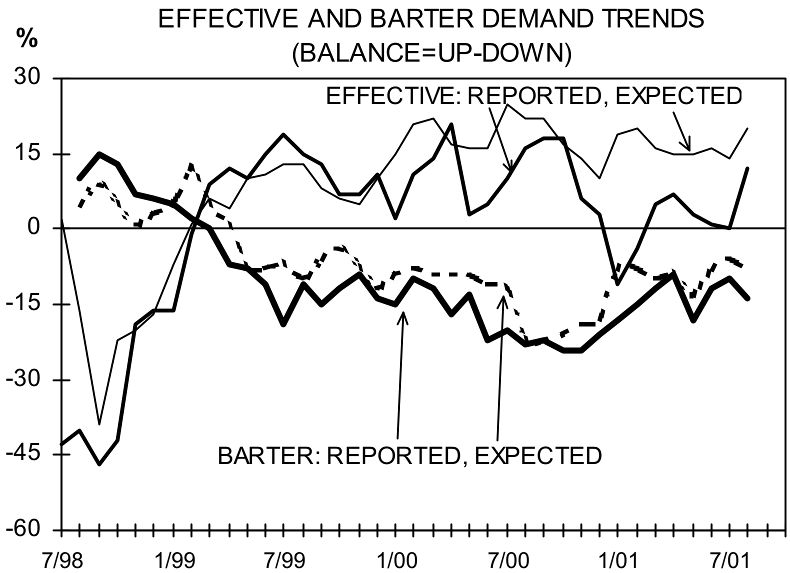
IET Monthly Trends Survey: August 2001

A sharp growth in effective demand along with a moderate price policy have stopped the growth in negative trends in the industrial sector. The growth excessive stock discontinued immediately and the production growth renewed. The enterprises' forecasts retain a strong optimism.

In August, the dynamics of effective demand experienced radical changes. After an actual stop in monetary sales in June to July the survey held in August registered a sharp rise in the intensity of sales, which has not been in place over the past nine months. The rise in the sales growth rate was noted in all the sectors but the non-ferrous metallurgy, however, the latter has reported just a slowdown of the growth, while none of sectors reported an absolute contraction in effective demand over the last month.

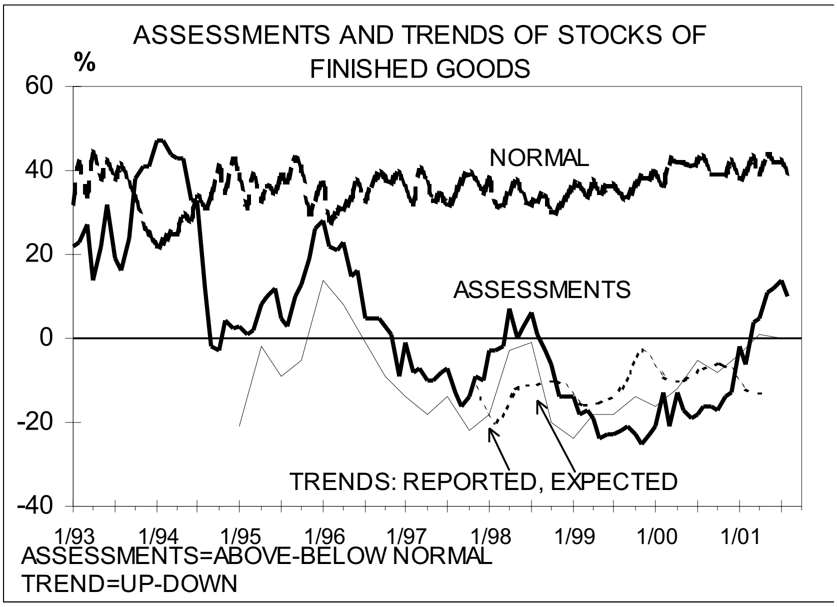
The increase in monetary sales allowed enterprises to get rid of barter more effectively. In August, the intensity of reduction of such operations grew by 4 points. It was the construction industry, machine engineering, the sector for chemicals and petrochemicals that provided the highest share of responses on the reduction in barter transactions. None of sectors reported a rise in barter, while the rate of reduction in promissory note and off-set schemes remained unchanged. Like in the past months, the surveys registered a moderate decline in such deals, at a rate being the slowest over the last 12 months. Except for the non-ferrous metallurgy and construction sector, there was no growth in the noted transaction in the industrial sector.

As a result, in August the national industrial sector renewed supplanting the non-monetary demand with effective one. The respective index values became the best over the past 10 months, i.e. once again, there were more enterprises reporting the growth in monetary sales along with a simultaneous decline in barter schemes that enterprises that reported the reverse correlation. In July, this index practically was at zero level – at that time, the dynamic correlation between monetary and non-monetary kinds of demand stabilized.



The renewal of the growth in effective demand has had an immediate impact on estimates of the stock of finished products. The growth in excessive stored stock registered over the last five months discontinued, and in August the balance of estimates of this index improved by 4 points. Nonetheless, the industrial sector still provides the prevalence of "above norm" reports, while the lack of stock (i.e. the prevalence of "below norm" reports) is still in place only in the industry of construction materials and the food - processing sector.

The dynamics of output reacted in the same fashion to the renewal of the growth in sales. The correlation between reports "up and "down" grew by 12 points at once and became one of the best in 2001. The intensity of output rise in all the sectors, but the forestry, wood-working and paper and pulp ones. An absolute production reduction remained only in the food-processing sector.



In August, the forecasts of change in effective demand reached the best value over the past 10 months. All the sectors shared more optimistic expectations, except the wood-working, light, and construction industries. Notably, the latter already forecasts a seasonal absolute decline in sales. The forecasts of barter, promissory-note and off-set schemes still remain unchanged - –he industrial sector on the whole expect the slowest decline in the volume of such deals.

The forecasts of change in output improved once again and became the most optimistic ones since March 2001. A more intensive growth in output may become possible in all the industries, except the metallurgical sector and the industry of construction materials.

The plans to purchase machinery and equipment in the IIIrd quarter proved to be most moderate over the whole 2001. When compared with the beginning of the year, the forecasted intensity of such purchases experienced nearly a two-fold drop. An absolute rise in purchases may become possible only in the sector for chemicals, petrochemicals, forestry, and light industry, while other sectors report a prevalence of plans to contract the purchases of machinery and equipment.

S. Tsoukhlo

Land Legislation Development in Russia

Summer 2001 was marked by energetic endeavours to develop Russian land legislation. The first thing to note is the passage of a new Land Code in two readings. The fate of this law is rather dramatic: its various versions were being discussed in the State Duma since 1996 but only now the adoption of a more or less sound document became possible. Contrary to the common notion there was a Land Code in the country adopted back in 1990. When the new Russian Constitution was enacted, this Code turned out to be quite obsolete and many of its provisions were annulled by the 1993 President Decree. Still, the Code remained in force and together with other normative acts regulated land relations in the country. And what's more, the then operative legislation declared the existence of private land ownership in the country (including agriculture) and permitted to conduct basic land transactions except for farmland mortgage (that was prohibited by the 1998 Law on mortgage). It's essential to keep all this in mind when assessing the true importance of the new Land Code being adopted: the document doesn't signify a revolutionary legitimisation of private land ownership in Russia but is a step towards comprehensive and complex land legislation adjusted to the new stage of the country's social and economic development.

In fact, three bills were proposed to the State Duma. First, the old version worked out by the Agrarian faction back in 1996 with multiple amendments introduced later. Once it has already been vetoed by the President. This version was obsolete at the very moment of its initial introduction. And these were not substantial limitations on agricultural lands' transferability that mattered - after all, they could have been abrogated in time, - but the imperfection of the document itself: it was poorly written in legal terms, didn't solve all the problems of land legislation, could not be reasonably amended afterwards and, thus, in time had to be replaced with a new Code. Second, the bill worked out by the Right Forces Alliance faction. By now, this Code is most complex and up-to-date, corresponding to the world trends and at the same time reflecting land transformations that took place in the country during the reform years. Finally, the third bill worked out by the Government. This is a compromise version, although the compromise is attained not by averaging the first two versions but by incorporating the basic provisions of the second version and by laying aside the most serious problems of the first one for further examination. In other words, the Government version accepted the logic of draft Code proposed by Right Forces Alliance but excluded from it issues relating to agricultural lands' transferability. It was the Government version that passed two readings in the State Duma in spring-summer 2001 and is most likely to pass the third reading in autumn. Besides, this autumn the Government plans to introduce to the Legislative Assembly a bill on agricultural lands' transferability.

The adoption of Land Code in its third version signifies a great progress in terms of politics. All the previous attempts to pass progressive land legislation failed voted down by the agrarian and communist opposition in the State Duma. The passage of the Code in two readings evidences a new balance of political forces in the country. Moreover, it sends a positive signal to economic agents. Though private land ownership in the country has long been legitimated (as we have mentioned above), virtually both business and officials were temporizing as continuous debates over land legislation made the situation unstable and acquired property rights were not guaranteed. So, this is the first important role of the adopted Code.

Its second role is purely legal: it creates a legal basis for regulating land relations and brings together numerous laws that served this purpose earlier. The procedure of acquiring and transferring land property rights is thus simplified, these rights become more guaranteed, the opportunities for rent seeking in land rights distribution are largely eliminated.

Lawyers and economists will later scrutinize the basic provisions of the passed Code as to their adequacy to social and economic needs of the country, legal perfection, etc. Here we would like to concentrate just on two principal problems arising from the Code's adoption.

As mentioned above, the Code is primarily targeted at regulating land relations outside agriculture. At present about 2/3 of farmlands and only 6% of urban lands have been privatized. Agricultural lands were subject to large-scale land reform (here we do not speak of its qualitative outcomes) while lands in cities and towns were not. The major part of urban land belongs to municipal authorities that withhold from selling it since land property is an important source of local budgets receipts and a good mechanism for manipulating economic entities, to say nothing of rent seeking in the process of allotting land plots. The new Code's adoption doesn't change the situation: the permission to sell and to buy land in cities (by the way, already being in force) will by no means make city authorities do it at their own will. Thus, the new Code just preserves the existing status quo in the urban land problem. In these circumstances the only way to solve the collision is to adopt an efficient law on enforcing the Code that will establish the procedure of privatizing land in cities.

The second problem unsolved by the Code is the determination of lands' category. Beginning from the Soviet period a category of land is determined by the fact of its allotment to some specific use. For example, agricultural lands are lands allotted to farming. Given the state land monopoly it was then logical and operational. But when land is privately owned, plots are no longer allotted - instead, they are acquired by means of civil transactions (purchase, inheritance, etc.). Formally, according to the above mentioned rule the fact of purchasing a plot of agricultural land discontinues its belonging to lands for farming category. But none of the three proposed versions of the Land Code revised the obsolete system of lands classification and this is going to be a notable hindrance to land relations development in the country. An up-to-date land zoning is needed and the solution of this problem could have become a subject of another, auxiliary law that was also passed this summer - the law on land management. But this law is far from being adequate to present requirements.

The actual fundamental lying behind the law's concept is that land management is an exclusive function of the state having monopoly over land. Land management is quite a technical procedure of forming and organizing land management units. The legal regulation of these activities was to become the subject of the law.

The law should have clearly stipulated that land management is an activity to be licensed and should have defined who, how and on what terms can get such licences, who is authorized to issue them and what is the corresponding procedure. It was necessary to clarify whether the state land management institutions are preserved or not, what units are to be managed at the budget account and what are to get funds only from private sources, who is to keep information on land management. The adopted law contains none of these norms. At the same time its Chapter III looks like a handbook for students - land managers and simply describes land management procedures that are not subjects of legal regulation.

It's also unfortunate, that the law on land management was adopted before the Land Code - a superior legal document. Even land management definitions in the two documents are not similar. Other contradictions may emerge as well, and then the recently adopted law will have to be revised.

On the whole, the adopted law in its present form looks to us not like a needed document but like one of departmental rules with the help of which state agencies demonstrate their usefulness.

So, the legislative process is very active this year. But what is actually happening to agricultural lands? And again contrary to the common notion, they are rather actively transferred. We continuously stress, that the driving force of this transfer is production growth that started in 1999 - as a result, agricultural land became valuable. Unfortunately, the national land statistics doesn't record all land transactions. It reflects only sale and rent of state owned lands while the bulk of transactions is conducted between private agents.

Studies carried out by different scientific centers show that at present there are three basic fields of land transfer activities. First, land is being concentrated in the sector of private farms. Successful and rapidly developing farmers rent or (and) buy land shares from their neighbours and thus enlarge cultivated areas. Second, agricultural enterprises also started to rent land shares in order to optimize their size. A small study in three Russian regions revealed that in 1993-2000 up to one third of farms changed the area planted from 3 to 7 times thus actively adjusting to the shifts in economic situation. Third, in the recent 2-3 years external operators (processors, traders, oil companies, etc.) became most active on the agricultural land market. Nowadays they intensely invest in agrarian production (grains and oilseeds growing, pig and poultry raising) renting therefor large land areas. The restructuring of agricultural enterprises' debts that started this summer accelerated the process.

Thus, land transfer became a noticeable phenomenon. The poor development of its normative basis is a hindrance for all the participants and necessitates adequate revisions of legislation. In this situation the continuing political debates about land transferability in the country become purely scholastic and the adoption of Law on agricultural land transfer is just a matter of time. Given a keen interest of almost all oil companies in land transactions the passage of such a law is doubtless.

E. Serova

Interventions on Grain Market

In 2000 in the Program of social and economic development of Russia till 2010 the Government declared its intention to begin interventions on the grain market. At the end of the year the conference headed by Prime Minister approved the program of developing grain production in the country that incorporated intervention provisions too. It was decided to use the receipts from selling raw sugar import quotas (the tender was held in November) for funding the interventions. In other words, grain market interventions no longer raise doubts and therefore since the corresponding Government Resolution was adopted in summer 2001, their procedure rather than expediency is being discussed.

Indeed, the crop is rather good this year and prices are consequently falling. It could seem that in this situation state interventions on the grain market are quite justified: it's reasonable to support grain producers when prices slide down. But this is so only at first glance. Grain was and continues to be one of the most profitable agricultural products. Profits of the Kuban grain producers mount to 300-400%. It's not easy to find another sector of the economy where an invested ruble brings 3-4 rubles of return. Lower prices will probably reduce profitability of grain production but not to the extent to make it low-profit and threatening the economic performance of grain producers (of course, in case they do not intend to grow grain to the north of polar circle).

One can argue that the problem is entirely due to the seasonal fluctuations of prices for grain. Farms usually have to sell it in autumn. Statistics show that by November most agricultural enterprises have no grain stocks. Traders are thus the ones who benefit from higher spring prices. An attempt to more equally distribute returns from marketing grain between producers and traders is quite an acceptable explanation for state purchase interventions. But already at the end of August we witnessed bulky sales of grain. Besides, regional authorities initiated the campaign of collecting grain in settlement of agricultural producers' former debts, thus accelerating grain marketing. Meanwhile, the procedure of state interventions has not yet been approved. In case a tender for selecting state agents is needed (and it's most likely to be needed), its organization according to the law will take 45 days. In other words, interventions can really begin only in November-December, when producers won't have any disposable stocks of grain. This means that the interventions being planned won't support agricultural producers but will benefit grain market operators that in no way can be considered a business urgently needing state support.

But that's not all. A purchase intervention irrespective of the way it's done supposes the purchase of all grain by the state at the intervention price. In case the market price is below the intervention one, these purchases help to raise it up to the set level (the level of intervention price). In case the market price is higher nobody will sell grain to the state. It's obvious that given such a system there should be a guarantee against an unconstrained inflow of imported grain to the domestic market. Otherwise, the grain purchased by the state will be replaced by the imported one, the desirable growth of price won't be attained and the whole operation will lose sense. That's the way the mechanism of minimal guaranteed prices worked in the EU: a variable import tariff on the regulated product was imposed in line with the intervention price. Nothing of the kind is being envisaged in Russia: the mechanism of grain interventions is worked out by the Ministry of agriculture, import tariffs are in charge of the Ministry of economic development and there are no coordinated tactics in this domain. In other words, the only result of the purchase interventions will be a simpler penetration of Kazakhstan and Ukrainian grain to the Russian market. They won't even benefit domestic traders.

In case the purchase interventions somehow help to raise domestic prices for grain, Russian grain exporters will suffer from it: their commodity will lose price competitiveness on the external markets. To tackle the problem the above mentioned European mechanism envisaged flexible export subsidies, not even spoken about in Russia. This means that while in 1998-1999 domestic exporters were ousted from the world grain market by humanitarian aid deliveries, in 2001 the same thing will be done by the purchase interventions policies.

Unfortunately, the decisions on grain market interventions have already been taken and are likely to be implemented. It could seem that such interventions in one season are not quite an awful mistake and next year they can be annulled. But the world experience evidences that subsidies are much like drugs - it's easy to introduce them and very hard to discontinue. Keen interests and lobbyists emerge whose resistance will be difficult to overcome.

E. Serova

The Russian banks in the market for European obligations of the Russian Federation

The Russian European obligations can be divided into three groups:

- The European obligations (*alias* Euro-obligations) of the RF Government (federal);
- European obligations of municipal entities (sub-federal), and
- Corporate European obligations .

Since November 1996 the RF Government has placed 9 issues of Euro-obligations worth a total of USD 13.59 bln., DM 3.25 bln., and 750 Italian Lire (IL). Of the nine tranches, 6 were denominated in USD, two – in DM, and 1- in IL. The maturity of all the issues falls within the period between 2001 through 2028.

In addition, in compliance with the conditions of the debt restructuring agreement with the London club of creditors the principal body of the debt towards foreign creditors and the debt on interest were converted into Euro-obligations, (so-called PRIN and IAN obligations, respectively) roughly accounted for USD 20 bln. with the maturity in 2010 and 2030. Therefore the capacity of this market is much bigger than the one for Eurobonds.

In the conditions of destabilization of Rb. exchange rate the instruments ensuring fixed income in foreign exchange appear fairly attractive for investors, and banks are not an exception. In the conditions of price rise for Euro-obligations and stabilization of Rb. rate the attractiveness of Euro-obligations as an instrument for short – term investing declines, however, it remains substantially attractive in light of longer-term considerations. In the meantime there are a number of significant impediments in a form of restrictions in the foreign exchange regulation area. The current law puts Russian investors in an unequal position. The banks licensed to carry out transactions with foreign exchange actually enjoy visible advantages in terms of their entry to the market for Euro-obligations.

By mid –2001 the prices for RF Euro-obligations were not lower than 76% of their face-value, while their yields accounted for 6 to 13% annualized, depending on the issue.

The market for Euro-obligations basically is an off-exchange one, even despite its inclusion, in the majority of cases, in the listing of the London or Luxembourg stock exchanges.

The market for Euro-obligations practically is not subject to any national forms of regulation, however its is regulated rather strictly by procedures and recommendations set by ISMA and the associated with that IPMA.

As concerns Russian participants in the market, it is Vnesheconombank, Vneshtorgbank, MFK, Sberbank RF, Doveritelny and Investitsionny Bank that hold membership in ISMA. Nonetheless, other Russian banks can also carry out transactions with Russian Euro-obligations in the international market – upon signing standard agreements with their foreign counterparts, i.e. de-facto following the procedures set by ISMA. In particular, MDM Bank operates under such conditions.

According to information agencies "Finmarket", "MFD-Infocenter", and "Rosbusinessconsulting", the following banks quote Russian Euro-obligations:

Table 1. The banks that provide quotations of Russian Euro-obligations to information agencies.

Finmarket	MFD-Infocenter	Rosbusinesconsulting
Zenit	Alba-Alliance	Alfa-Bank
MDM-bank	Bank Moskvy	MDM-bank
Rosbank	Vnesheconombank	Sberbank RF
Russly generalny bank	Impexbank	Zenit
Sobinbank	MDM-bank	Novikombank
Vozrozhdeniye	Sberbank RF	Guta- bank
Eurofinans	Guta-bank	Roseximbank
Novikombankк		Rosbank
Roseximbank		Eurofinans
Sberbank RF		Sovfintrade
Expo-bankк		Expo-bank
Guta-bank		Bank of Moscow
Krasbank		Vneshtorgbank
		Vnesheconombank
		Russky generalny bank
		ING-Eurasia
		Montazhspetsbank
		Sobinbank

It should be noted that the above list (22 banks) is not a complete list of financial institutions that quote Russian Euro-obligations, and it does not incorporate all the national banks that conduct operations with or hold in their protfolios federal debentures of the Russian Federation denominated in foreign exchange (FD RF).

The data on banks' balance sheets allow an estimation of just the amount of Eurobonds and Euro-obligations in their portfolios. Considering such a criterion as the presence of the bank's turnover in December 2000 or the balance sheet on FD RF as of January 1, 2000, 259 banks were selected. However 8 of them are managed by ARCO and are not active operators in the market for Euro-obligations, that is why they were excluded from the aforementioned sample.

Basin on the list of banks represented in Table 1 a sample of the most active operators in the market for Russian Euro-obligations was completed. The sample was comprised of 20 banks, including Sberbank RF, Vheshtorgbank, and Vnesheconombank. Two banks- Krasbank and Montazhspetsbank- were excluded from the sample, because over the period between April 2000 through April 2001 the non-zero values on the position of FD RF were fixed only twice.

To conduct a comparative analysis, we used the data on a sample of 613 Moscow banks, exclusive of Sberbank RF, Vneshtogbank and Vnesheconombank. It should be noted that the banks managed by ARCO have not been excluded from the smaple of Moscow banks.

As of beginning 2001, the average weighted share of FD RF in assets across the sample of Moscow banks accounted for 4.1%, and by the end of the quarter it fell to 3.8%[1]. At the same time the banks that provide their quotations of Russian Euro-obligations to the noted information agencies demonstrated a different trend: as of the beginning of the year, their respective index was 4.5% and by the end of the 1st quarter it grew up to 4.7%[2].

Ass of early 2001, the average assets of the banks that provide their quotations of Russian Euro-obligations to the noted information agencies, exclusive of Sberbank RF, Vneshtogbank and Vnesheconombank, accounted for Rb. 15.6 bln., which was much higher than the respective index identified across the sample of Moscow banks (1.8 bln.). The trend remained unchanged by the end of the 1st quarter: 16. 6 bln. vs. 1.9 bln.

It should be noted that 13 banks out of 17 ones comprising the list of the banks providing their quotations of Russian Euro-obligations to the noted information agencies (exclusive of Sberbank RF, Vneshtogbank and Vnesheconombank) possessed assets that were substantially bigger than the average index across Moscow banks.

The banks of this group has also become considerably more profitable when compared with the average statistical Moscow banks that showed a negative profitability rate as of early 2001. Thus, the average weighted profit-to-assets ratio across this group of banks accounted for 2.12% vs. –1.04 across the group of Moscow banks (as of the end of the 1st quarter: 2.05% vs. –1.06 annualized).

The banks that provide their quotations of Russian Euro-obligations to the noted information agencies also appeared more capitalized against the backdrop of Moscow banks. As of early 2001, the average weighted share of balance-sheet capital in their assets accounted for 19.35% vs. 14.67% of Moscow banks.

Hence financial indices of the banks that vigorously operate with Russian Euro-obligations are substantially higher than average ones, which may testify to the fact that currently it is only fairly big and stable banks that deal with this financial instrument. This assumption is also proved by the fact that as of beginning of 2001, the turnover or balance sheet on FD RF was shown only by 259 out of registered banks, i.e. less than one-fifth of them, and most likely some of them operated rather with Eurobonds than Euro-obligations.

In December 2000, the aggregate turnover of all the banks in terms of FD RF (except the banks managed by ARCO) accounted for Rb. 347 bln (roughly USD 12 bln.), while the share of Sberbank RF, Vnesheconombank and Vneshtorgbank made up Rb. 215 bln., or roughly as much as 62% of the aggregate turnover.

The turnover of the banks that were the most active players in this market in December 2000 accounted for Rb. 274 bln., while without regard to Sberbank RF, Vnesheconombank and Vneshtorgbank – 59 bln. Hence the share of the group of the most active players in the market for Euro-obligations of RF accounted slightly under 80% of the aggregate turnover of all the Russian banks - operators in the market. These results allows judgement of a fairly high level of concentration of operations in this particular segment of the market, which once again proves a low outspread of operations with Russian Euro-obligations across Russian banks.

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[1] As of August 1, 1998, the share of FD RF denominated in foreign exchange accounted for 5.3% of the national banks assets on average, exclusive of Sberbank RF

[2] exclusive of Sberbank RF, Vneshtogbank and Vnesheconombank