

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES 08'2009

MONTHLY BULLETIN:

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BASIC DEVELOPMENTS AND TRENDS

In August there was a massive accident at the Sayan-Shushenskaya power plant with numerous human victims. In Ingushetia, a suicide terrorist blew up the building of the Nazran police department, which caused numerous casualties. Mr D. Medvedev has admitted that the situation in the Caucasus is deteriorating, and proposed as a specific measures to reduce the authority of the jury trial (to withdraw cases committed by criminal groups from its competence). A discussion is started in government circles on the public corporations, though it is more HR, rather than institutional in nature - no one talks about the liquidation of the institution as it is. A new version of "Basic trends of budgetary policy", developed by the Ministry of Finance is disclosed. A high level of public expenditures and budget deficits are planned for the nearest years.

Reduced capital investments in capital assets during January-July 2009 by 18.8% against the relevant period of the preceding year, industrial production - by 14.2% and the turnover in retail trade - by 3.8% had a significant impact on the domestic market. Stagnant consumer market in the current year was provoked by the reduction in real disposable monetary incomes by 0.9%, as compared to January-July 2008, and real wages - by 3.0%. The tension was sustained in the labor market: the total number of unemployed persons increased (by ILO methodology) in July 2009 to 6.3 million people, or 8.5% of the economically active population.

Results of the survey of industrial enterprises conducted by IET, showed that after some positive changes in July, August trends in the industry are not so good. Nevertheless, there was no return to expressed negative results of the first six months of the year. Schedules and estimates of manufacturing companies are getting improved, and it seems the problem of surplus stocks of finished goods in the industry has been already solved. However, a strong desire significantly to reduce the staff of enterprises. Assessment of credit availability to large enterprises is greatly improved.

As of July results, the consumer price index was slightly higher than the indicator of preceding year (0.6% against 0.5%). Nevertheless, the inflation, accumulated since the beginning of the year (8.1%) remains lower than it was in 2008 (9.3%). The real effective ruble rate weakened within the month by 1.5%, while international reserves of the Bank of Russia decreased by 2.6% to USD 401.98 billion. On August 7, 2009 the Board of Directors of the Bank of Russia decided to arrange the second issue of short-term zero-coupon bonds. Since August 10 the Bank of Russia once again lowered the refinancing rate by 0.25 percentage points up to 10.75% per annum.

In the first half of 2009 the basic indicators of the Russian foreign trade were formed under conditions of significant reduction of the external and domestic demand, and characterized by negative dynamics. The trade balance remains positive, though its volume has decreased more than twice, from USD 101.1 to USD 43.6 billion. Due to increased import duties, within six months of the year the domestic automakers managed to extend their share in the total volume of vehicle sales up to 61%, from 43% in January 2009.

In August, positive trends were dominating in the dynamics of the Russian financial market. Positive trends are particularly clearly observe in the government securities market, where the activity of investors increased by 177%. Volatile trends were observed in the domestic market of corporate bonds. On the one hand, the market volume was rapidly growing, the number and volume of registered issues has been significantly increased,

trading volumes in the secondary market has increased. Nevertheless, the number of actual defaults remains at a record level and the lack of trust among the investors in securities of small companies is sustained. International rating agencies Fitch and Moody's keep up «negative» estimates of Russia rating.

At the background of relative stability of the global economy, some improvement was observed in the basic macroeconomic indicators of the domestic economy in late second - early third quarters of 2009. At the same time, the RF public financial sector continues to face with the growing imbalance in the budget system. A key factor in the growth of the imbalance is the beginning of a large-scale funding of the RF Government anti-crisis program in June-August of this year. Herewith, within seven months of 2009, resources redistributed through the budget system have declined again.

Presidium of the RF Government has reviewed the issue of amending the budget legislation. The key proposed amendment is further centralization of oil revenues in the federal budget.

Indicators of mortgage creditting have demonstrated stable results in the II quarter. OAO «Agency for Housing Mortgage Lending» has lowered the interest rate in August to 10.8% and retains its refinancing rate close to pre-crisis levels.

As per results of the first quarter of 2009, the volume of assets in the accumulative share of the mandatory pension system (regardless the insurance premiums to the Russian Pension Fund (RPF) continued to decline. The share of the state management company (SMC) in the total assets of the accumulative mandatory pension system has decreased from 88.5% to 85.3% within the year quarter. RPF share has increased by 9.2 to 12.3% over the same term. According to the results of the first quarter of 2009, the yield on pension savings, invested in SMC was deficient (-7.2%). However, over the 3-year term the yield on pension savings invested in SMC, remained positive and amounted to 2.9%.

In late July and early August amendments were introduced in economic legislation and regulatory framework have been made, including the following:

- universities and research institutions were granted the right to create business entities;*
- procedure for the government regulation of prices for medicines is amended;*
- subsistence level in Russia was upgraded;*
- regulations on accumulating, allocation and distribution of the funds among the subsidies from the federal budget to the budgets of the RF Subjects are revised;*
- the decision is adopted on the transfer to the budget the "Fund for reforming housing and communal services" public company assets, valued at RUR 65 billion.*

THE POLITICAL AND ECONOMIC RESULTS OF AUGUST 2009

S.Zhavoronkov

In August there was a massive accident at the Sayan-Shushenskaya power plant with numerous human victims. In Ingushetia, a suicide bomber blew up the building of the Nazran police department, which caused numerous casualties. Mr. D. Medvedev admitted that the situation in the Caucasus is deteriorating, and suggested further to restrict the authority of the jury trial as a specific measure (to withdraw from its competence the cases committed by criminal groups). In government circles (after the order of D. Medvedev to the prosecutor's office to review the activities of public corporations), a discussion has been started on public corporations, though it is rather HR, than institutional measure - no one talks about the liquidation of the institution as it is. One more version of "Major trends of budget policy" is disclosed, prepared by the Ministry of Finance. A high level of public expenditures and budget deficit in the coming years is sustained.

August 2009 confirmed the reputation of «the month of disasters». The main event of the month was an accident at the Sayan-Shushenskaya hydropower plant. Major damage occurred in the turbine hall of the power plant, the walls of which were destroyed. The exact cause of the accident is not identified yet, the authorities exclude only version of the terrorist attack. Water could be blocked only in an hour due to the failure of the major part of the equipment, designed to combat such emergency. More than 70 people were killed – practically the entire night shift, several people managed to survive in the water. According to official information, the dam itself was not destroyed. As a result of the accident, energy consumption in Siberia is limited, what is a serious problem to the Sayan Aluminum Plant, located near the power plant. According to official estimates, it will take about two years to run the power plant to the full capacity: one hydraulic generating unit is completely destroyed and three more need serious repairs.

The controlling shareholder the power plant is the government, represented by JSC "RusHydro". After the accident, the Head of the power plant N. Nevolko was relieved of his position (though the dismissal was made on an honorary basis - at the same time, he was appointed as Advisor to the Chairman of the Board of JSC "RusHydro"). V. Kyari, the new appointed Director, who previously the Head of JSC "Sayan-Shushensky hidroenergoremont", an associated enterprise with the power plant.

Due to the accident, prices in the open electricity market rose sharply (although in a couple of days after the accident NP "ATS", the trading system management company has introduced a scheme of smoothing fluctuations, basing on the performance of the last year, adjusted for inflation). In view of the meetings with Prime Minister Vladimir Putin, Federal Tariff Service should develop by September 10 a policy for temporary government regulation of prices. "... Such a policy will be in effect in the following cases: in the event of a temporary shortage of power-generating capacity in some regions, in the absence of competition among suppliers due to technological reasons, as well as in case of force majeure," Putin said. It is not clear whether it is direct government regulation of prices, and with what level of price deviation from the pre-crisis period they will be applied. A. Klepach, Deputy Minister of Economic Development has stated, that the Government may increase the electricity tariffs for 2010 in excess of the estimated level (about 5 per cent), although in general, the Government of Russia promises to provide "non-tariff sources" for rehabilitation of the Sayan-Shushenskaya power plant.

Actually, the accident at the Sayan-Shushenskaya power plant provides new incentives to discussions on reforming the electric power industry – both, institutional and technical. First, the fact comes under notice, that this accident, as another accident at the Moscow substation Chagino in 2005, occurred in the energy segment, which is still in government ownership, and which is apparently less financed than power generating units under the control of private capital. Secondly, there arises a need to build large hydropower plants in general - because of the potential danger of a large-scale calamity in the event of the existing capacities failure (which does not seem impossible today), and an issue of the high cost of such construction. “RusHydro” stated, that the accident in Khakassia stresses the need for completion of Boguchansk power plant, which could provide surplus source of energy and bring market price down; there is a long-term discussion on the issue of construction funding between “RusHydro” and “Russian Aluminum”.

The second outstanding disaster, though with a few victims (2 persons) was the clash of aircrafts at the annual International Air Show in Zhukovsky. Herewith, it was found out, that a few years ago the deceased pilot in a public interview has expressed skepticism about the technical state of Russian aviation. The day after the accident, Prime Minister Vladimir Putin gave a negative assessment of the Joint Aircraft Corporation activity: “... It is strange enough, that a number of military contracts for aircraft sales to other countries and domestically has brought to JAC, losses, rather than profit...” There are also losses in civil aviation. ... I would like to warn against the illusion that the state will continue to correct corporate mistakes ... “. As a result, Putin has allocated a month term for the development of a national program with a limited funding for the aviation industry recovery.

In August there was a major terrorist attack in Ingushetia. The terrorist in a car with a large quantity of explosives attacked a building of Nazran police unit during the morning line-up. The building was severely damaged, more than 20 people were killed (the majority of them are police officers), more than 150 were injured. This is the biggest loss in Ingushetia after the terrorist attack on Nazran in 2004, and the second serious attack in one summer (in June, at the assassination attempt YU.-B. Yevkurov, the Head of Ingushetia was badly wounded). After the explosion the Minister of internal affairs of Ingushetia R. Meira, who spent his post less than a year was dismissed. Herewith, the new Head of the Minister of internal affairs has not been appointed, currently only a “curator” is appointed in the person of Deputy Minister of internal affairs Alexander Edelev. Dmitry Medvedev shortly after the incident said: “... In regard to the situation in the Caucasus. Of course, I do not believe sufficient measures are being taken. If they were sufficient, the situation there would have been peaceful, it is far from quiet. Moreover, to speak frankly and face the truth, in recent months there is a tendency to deterioration. It is clear, this is the outcome increased terrorists and criminal underground activity on the one hand, and some wrong actions on the part of law enforcement authorities on the other hand.

However, only one failure was specified, i.e., the existence of the trial jury, which, according to D. Medvedev, “release bandits to freedom.” Medvedev called for withdrawal the right to judge crimes, committed by criminal organizations, from trial juries. We would like to remind in this connection, under initiative of D. Medvedev, cases against terrorists were already withdrawn from the authority of trial juries. Meanwhile the relevant legislative initiatives have not been made yet, but there is a general trend for many years - under the pretext of the terrorist threat in the North Caucasus to abolish public institutions, independent from the government, throughout Russia. Regarding the courts, there are only few cases, when persons, acquitted by trial juries the North Caucasus, subsequently happened to be militants. There is more common practice, when captured militants are set free by law enforcement authorities, for whatever reasons, from corruption to the emissary

actions. And, of course, the level of terrorism in the North Caucasus is directly affected by extremely extensive corruption, even in comparison with the total Russian level, abuse of power, and there is no possibility of peaceful dialogue with the authorities, and the same persons are elected for many terms in succession.

In August, Dmitry Medvedev has authorized Prosecutor General Yuri Chaika and the Chief Control Department K. Chuychenko before November 10 to conduct a comprehensive review of public corporations. It was stated in the official reports to Kremlin on this occasion that "... as per the audit results it will be proposed to the President, if further use of such legal form as a public corporation is reasonable." Currently there are seven of them: "Deposit Insurance Agency", "Fund for Housing Reform Assistance", "Olympstroy", "VEB," Rosnano", "Rosatom" and "Rostechologies". In spring the Fund for Housing Reform Assistance was audited. As a result, the Fund management returned to the budget of several tens of millions rubles, paid as bonuses, but retained their positions. Public corporations, have been criticized for a variety of issues: from the megalomaniac association of hundreds of unrelated assets under the leadership of one entity, to the lack of proper accountability and transparency (public corporations are exempt from the effect of a large number of legal provisions, in particular, bankruptcy law, public procurement regulations, etc.) Particular concern has always been caused by the work of the public corporation Rostechologies, headed by S. Chemezov, a close ally of Putin. The corporation started its activities with the voluntary-compulsory purchase of private enterprises (Avtovaz, VSMPO-Avisma, etc.). Concurrently with the statements about the audit, it was informed that S. Chemezov is withdrawn from the presidential commission on modernization and technological development of the economy.

A number of analysts rated these events as a significant trend, but this can be hardly accepted. First, the withdrawal of an individual from an advisory committee only points to the status of S. Chemezov, which he kept and which more significant. Secondly, the statements on tentative reduction of government participation in the economy are so often and so inconclusive, the idea is badly devalued. However, some reassessment of the role of "Rostechologies" is in progress - in August it was announced about resignation of Boris Aleshin, the company Head, for the most scandalous results of management one the public corporation objects, Avtovaz.

He was replaced by I.Komarov, appointed Avtovaz Executive Vice-President in spring (which resulted in a significant reshuffling in management), and Aleshin received an honorary, but insignificant title of S. Chemezov Adviser. In August Moscow City Government has rejected to join Aviation Corporation with Rostechologies (tentative brand - "Rosavia"). The grounds are that the asset of the Government of Moscow - the airline "Atlant-union"(it was supposed to be exchanged for 49 per cent share in Rosavia") is in difficult financial position: there are more than RUR 11 billion of debt and negative profitability. In theory, it would seem advantageous to the Government of Moscow to get rid of this problem assets, but this is only theoretically. In practice, in terms of government ownership it is important keep operational control over financial flows, and the Moscow city government would be deprived of such control in the new company. As opposed to that, for the leadership of Rostechologies for the same reason it would be beneficial. At the same time, Luzhkov applied to the government of Russia with a request to provide of direct monetary compensation for the costs of "Atlant-union" for the passengers carriage, and to repay obligations of AirUnion alliance, which turned bankrupt last year.

Thus, we can talk about some management failures of S. Chemezov, but not the idea of public corporations as such.

In the financial sector struggle is going on between "thrifty" declarations of the Russian authorities and political economic practice of lobbying. Currently the latter is more

successful. Minister of Finance Kudrin, speaking in August about the state of Russian economy, said that public funding of its sectors has to be terminated. Otherwise, there is a threat of extended budget deficit and growing interest rates. “Financing of the economy is sufficient; it should not be done any more... This is comparable to the surplus emission into the economy that can boost inflation and lead to an increase in interest rates”. Ministry of Finance has also presented the amended after approval draft of the Government project “Basic trends of budgetary policy”. This document, however, is far from total compliance from the reasonable statements of the Minister of Finance: thus, the return of budget expenditures in terms of GDP (18.5 per cent) to the pre-crisis level is expected only by 2012, and there is still a significant planned increase in pensions (higher expenses by 40 per cent), the level of spending on “economic policy” (in fact, for financial assistance to enterprises) is not reduced, but increased, as well as expenses for “especially significant international projects” like the Sochi Olympics complex or APEC summit in Vladivostok, on the defense projects. The deficit is expected to be covered, as before, through extensive internal and external loans. However, Prime Minister Vladimir Putin has stressed in one of the August presentations, that Russia would not apply to the IMF, i.e., country’s leadership prefers the more expensive loans to avoid IMF standard requirements to the financial policy.

In August, the Head of the Federal Penitentiary Service was replaced. Yuri Kalinin, who was leading the FPS over 15 years, was appointed Deputy Minister of Justice. In fact, this is a descent, because the FPS is the only more or less influential unit in the structure of the Ministry of Justice, controlling the lives of nearly a million prisoners. The Head of Internal Affairs of the Samara region A. Reimer was appointed to that position. He is considered a protege of the current Minister of Justice Alexander Konovalov. From a political point of view, these rearrangements are equivalent; both officials were sharply criticized by the supporters of human rights. ●

INFLATION AND MONETARY POLICY

N.Luksha

As of July results, the CPI in the RF was somewhat higher than in the relevant period of preceding year (0,6 per cent against 0,5per cent). Nevertheless, the accumulated inflation since the beginning of the year (8.1per cent) remains lower than the indicator of 2008 (9.3per cent). The real effective ruble exchange rate has declined by 1.5per cent, while the foreign currency reserves of the Bank of Russia decreased by 2.6 per cent to USD 401.98 billion dollars as of August 7, 2009. The Board of Directors of the Bank of Russia has decided to hold a second issue of short-term zero-coupon bonds. Since 10 August, the Bank of Russia has once again lowered the refinancing rate by 0.25 percentage points up to 10.75 per cent per annum.

The consumer price index growth rate remained unchanged in comparison to June level and made 0.6 per cent in monthly terms (see Figure 1.). The greatest input in prices growth in July was made by commercial public services (+ 0.8 per cent).

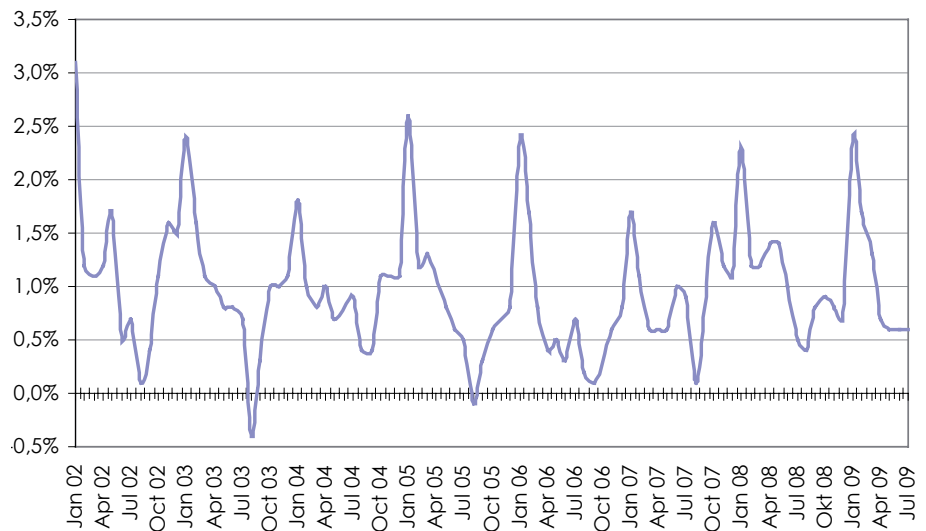
The growth rate of prices for public commercial services has accelerated again. Gas supply tariffs in housing and utilities service have been increased (+4.1 per cent). In the midst of the summer holidays season prices have continued to rise for health resort services and international tourism, prices growth for which amounted to 2.6 per cent and 2.5 per cent, accordingly. Growth was noted also in ticket prices for long-distance trains, which has affected the average prices for any passenger transport (+1.8%). The growth rates in healthcare services have somewhat decreased (+0.8 per cent). There was no reduction in prices for any type of services.

In July the growth rate for food prices was 0.6 per cent, which is slightly higher than the last month indicator. The major impact over the global price growth, as in the previous month, has been made by fruit and vegetable products, which went up by 3,2 per cent (against prices decline by 6.7 per cent in July of preceding year). The June decline in prices for eggs (-9.2 per cent) was replaced by some increase (1.3 per cent). Reduced prices have been observed in a number of products: pasta, milk and dairy products, butter among them, which become somewhat cheaper (by 0,5-0,3 per cent). Prices downgrading for sunflower oil, grits and beans was more expressed – by 3.1 per cent and 2.1 per cent respectively.

The growth rate of prices for non-food goods in July has somewhat decreased, having reached 0,6 per cent as of month results. Like in preceding month, the highest price growth in this group of products was observed for gasoline (+7.1 per cent). There was continued a downfall in medicines prices (-0.8 per cent). Video-and-audio goods have ceased the growth in price: price downgrading amounted to 0.4 per cent.

Therefore, in July for the first time since March, inflation has exceeded the same indicator of the last year. The main contribution to accelerating the growth rate of consumer prices has made the jump-up in prices for gasoline. A certain role has been also played by a continuing increase in prices for fruit and vegetables (contrary to the traditional seasonal decrease in prices), higher tariffs for gas, as well as increased costs for tourism and recreation. As a result, the increase in food prices and for commercial services have exceeded the level of previous month. Nevertheless, meanwhile the increase in consumer prices within January-July remains lower than the relevant indicator of the last year.

In particular, it is worth noting the unusual growth in prices for fruit and vegetables in summer. On the one hand, it was associated with a late delivery of the new crop products to a trading network as a result of adverse weather conditions in southern parts of the country. On the other hand, the RUR devaluation has led to the fact that food imports were purchased at a higher rate. As a result, domestic manufacturers have brought up their prices to the prices of imports. However, in late summer - early fall one can expect some decline in prices for vegetables in regard to the new crop and the purchase of imported products under the new contracts.



Source: Russian Statistical Agency

Fig. 1. The Growth Rate of the CPI in 2002–2009 (% per month)

As in previous months, in August the factors, restraining inflation, will be the downfall in consumer demand and the downgrading of monetary supply. However, in July it was demonstrated, that the necessary conditions for reducing inflation are insufficient yet. Manufacturers, contrary to the theory, were raising the prices to offset the losses from lower sales volumes. We can assume that in August the inflation will somewhat slow down in comparison with July, in view of lower prices for fruit and vegetables. We would like to remind, that the official estimates for the annual inflation, made by the Ministry of Economic Development is 12 per cent.

The base consumer price index¹ in July 2009 has amounted to 0.3 per cent (versus 0.8 per cent for the same period of the last year).

As of July 2009 results, the monetary base (in broad definition²) has declined by 2.4 per cent and amounted to RUR 4,850.5 bln. As of July 1, 2009, the volume of the monetary base in a broad definition has reached RUR 4497.6 bln. Let us consider the dynamics of the monetary base in broad definition by components.

On August 2009, with regard to the fund balances in credit organizations, cash in circulation made RUR 3.9 trln (growth by less than 0.7 per cent within the month), correspondent accounts of credit organizations with the Bank of Russia made RUR 417.8 bln (-11.4 per cent), mandatory reserves made RUR 93.2 bln (increased by 1.5-fold), banks' deposits in the Bank of Russia made RUR 385.4 bln (-24.3 per cent), and the value of shares of the Bank of Russia with credit organizations made RUR 19.4 bln (+10.9 per cent).

1 Basic index of consumer prices is an indicator of the inflation level without regard to seasonal price reduction (fruit and vegetable products) and to administrative measures (tariffs for government-regulated services, etc.). It is estimated by the RF Statistics Service.

2 The RF monetary base in broad terms with no regard to the cash issued by the Bank of Russia and the balance of Compulsory Reserve Accounts on credit organizations in national currency, deposited in the Bank of Russia, taking into account the assets of correspondent accounts and bank deposits, allocated in the Bank of Russia.

Within July 2009, excessive reserves of commercial banks¹ have significantly decreased²: as of the month results, this decline made RUR 174.8 bln, or 17.5 per cent. Herewith, the reduction was demonstrated by both, correspondent accounts and the banks' deposits with the Central Bank of Russia. The reduction of funds in correspondent accounts was the result of the abolished limit of foreign currency assets. According to the Bank of Russia, in July 30 largest national banks have withdrawn from the foreign currency accounts of the Central Bank about 75% of total assets. We should note, that on July 2 the Bank of Russia announced its intention not to extend to the III quarter of 2009 the regulation on maintaining a monthly average volume of foreign assets and the average aggregate net foreign currency volume in the balance sheets of credit institutions. After the removal of the restrictions, commercial banks began to reduce the foreign currency at their accounts in the Central Bank, which did not bring them income, and began to transfer them in foreign assets to earn a percentage.

The reduction of liquidity in the banking sector also urged by the scheduled increase of the required reserves threshold: on August 1, 2009 they have grown by another 0.5 percentage points to 2.5 per cent. We would like to remind, that this was the third and last planned extension of that limit, which was introduced on May 1. Nevertheless, the situation with ruble liquidity remains quite favorable. Interest rate in the interbank market in July averaged 6.5 per cent, which is fairly moderate rate. Demand for refinancing by the Bank of Russia is also fully fit within the limits of the regulator. The situation in the stock market and the ruble stock market, where the activity is rather low, can not serve as an indicator of the lack of liquidity, as apparently, the investors are preparing for the autumn, when, as expected, there might be a deterioration in the financial sector, associated with the growth of «bad» debts.

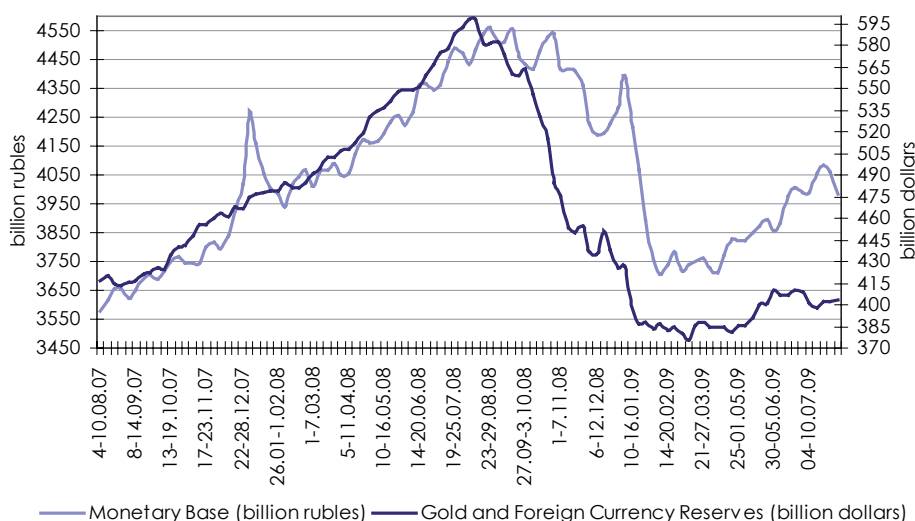
According to the Central Bank, the share of the debts of the fifth category of quality - bad debts – in the national banks portfolio on July 1, 2009 has made for retail loans 10.1 per cent (increased 1.6 times in comparison with the beginning of 2009), for corporate loans – 8.3 per cent (increased 2.3 times). Meanwhile, the level of «bad» credits is even more, as in addition to evidently bad debts, there are overdue loans. Thus, according to the Bank of Russia, as of July 1, the share of arrears in the total debt of the 30 largest banks in Russia amounted to 4 per cent. However, apparently, in the second half of the year the situation will be changed. Credits from other categories can go to the category of bad debts. On average, experts of the Bank of Russia estimate the growth of the «overdue debts» by the end of 2009 to the level of 12-13 per cent, although the earlier estimates did not exceed 10-12 per cent. The higher growth of the bank overdue arrears is possible in the event oil prices fall below 60 dollars per barrel. The growth of «bad» debts of banks will first of all result in reducing credits in the real sector. Banks are accumulating reserve funds in view of tentative losses.

We'd like to remind, that in June, to support of the real sector, Prime Minister Vladimir Putin demanded that public banks should reduce credit interest rates. VTB and Sberbank were the first to respond to that requirement and announced their intention to reduce rates. VTB reported on the decrease credit rates on credits for strategic enterprises by 2-3 p.p. The overall decline in credit rates of Sberbank in the last three months amounted to 2 percentage points. According to First Deputy Chairman of the Central Bank A.G. Ulyukayev, currently the stabilization of loan portfolio is in progress now. Since June, private banks have stopped the reduction of crediting. To date, their loan portfolio is not growing, whereas

1 The excessive reserves of commercial banks with the RF CB refers is the amount of correspondent accounts of commercial banks, their deposits with the RF CB and the CB bonds of commercial banks.

2 The excessive reserves of commercial banks with the RF CB refers is the amount of correspondent accounts of commercial banks, their deposits with the RF CB and the CB bonds of commercial banks.

the decline has already stopped. Before the end of the year, according to A. Ulyukaev, the growth of the loan portfolio for the total banking system may reach 7-8 per cent of the current level. In May the growth of the volume of cash in circulation by 0.7 per cent and mandatory reserves by 1.5-fold has led to expansion of the monetary base in narrow definition (cash plus mandatory reserves)¹ by 1.5 per cent (see Fig. 2). The volume of international reserves of the RF Central



Source: RF Central Bank

Fig. 2. Changes in the Monetary Base and in the Gold and Foreign Currency Reserves in 2007–2009

Bank has been reduced and made it the late July USD 401.98 bln. This indicator has declined for the first time since March; the decline made 2.6 per cent.

According to the estimates of A. Ulyukaev, within seven months of 2009, the net outflow of capital has reached nearly USD 26 bln. According to his words, the capital outflow in July was not so high, which resulted in the real effective RUR rate. Thus, nearly 5 per cent strengthening of the real effective RUR rate in the II quarter of 2009 has been replaced by a decline by 1.5 per cent. The index of real effective rate as of the month results made 129.03² (see Fig. 3).

As of July results, the official rates of USD and Euro against RUR have increased by 1.5 per cent and 2 per cent accordingly.

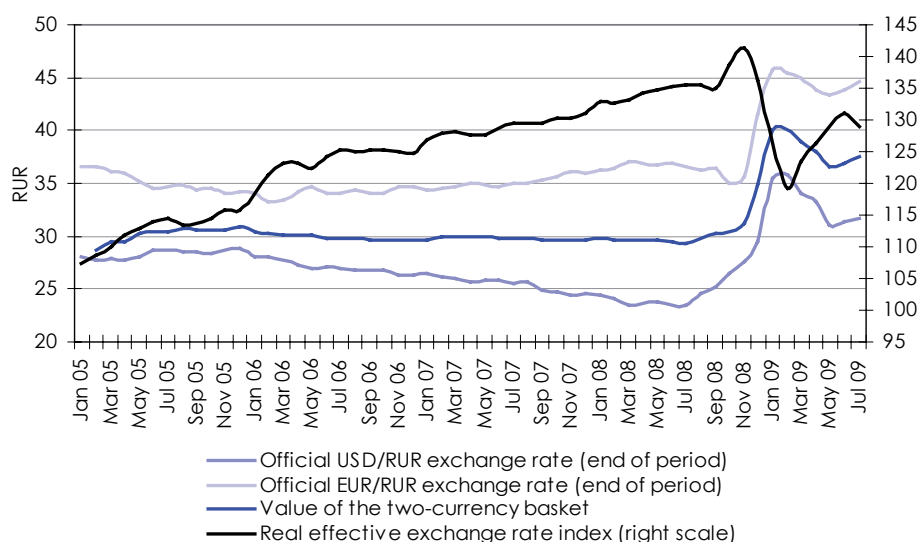
The USD rate has strengthened up to RUR 31.76, and Euro rate up to RUR 44.69. As a result, within the month, RUR has downgraded by RUR kopeks in regard to the two-currency basket, while the value of the two-currency basket³ has increased to RUR 37.58. Since the beginning of the current year it has decreased by 8.7 per cent. To avoid strong fluctuations in the ruble exchange rate, for the first time since January 2009 in the framework of foreign exchange intervention, the RF Central Bank has carried out net sales: there were sold USD 3.1 bln and Euro 0.6 bln. Earlier the Central Bank was performing net purchases of foreign currency.

Dynamics of the two-currency basket indicators, as always, was directly dependent on the dynamics of oil prices. Thus, according to Reuters, on July 1 the cost of a barrel of oil (Urals brand) was USD 68.17 dollars, and the two-currency basket value at the MICEX amounted to RUR 36.86. In mid-July (13.07.09) oil has declined to USD 58 per barrel, and the two-currency basket has risen in price to RUR 38.61. At the end of July (27.07.09) oil price went up to USD 69.18, and the two-currency basket has dropped down to RUR 36.56. Two days

1 We would like to remind, that the monetary base in the broad definition is not a monetary instrument, it reflects the obligations of the Bank of Russia in national currency. The monetary base in narrow definition is a monetary instrument (one of indicators of the volume of monetary offer), which is under total control of the CBR.

2 The level of 2002 is taken for 100.

3 Two-currency basket is the RF Central Bank operational indicator in its foreign currency policy. Currently the share of EURO in the currency basket makes 45 per cent, USD – 55 per cent.



Source: RF Central bank, author's estimates

Fig. 3. Indicators of Ruble's Exchange Rate Dynamics

deficit. Thus, in July, it has already reached RUR 202.1 billion. According to the Ministry of Finance, in 2009 the budget deficit will amount to RUR 3.6 trillion, or 9.4 per cent of GDP.

On August 7, 2009 the Board of Directors of the Bank of Russia has decided to issue in September, short-term zero-coupon bonds for the amount of RUR 100 billion (with the maturity in March 15, 2010). We would like to remind, that this is the second consecutive emission of short-term zero-coupon bonds. Thus, in the middle of May the Central Bank informed of placement of bonds for RUR 100 billion with the maturity in December 2009. The decision of the Bank is addressed at the sterilization of the excessive liquidity in the banking system. The bulk of the national budget expenditures is performed traditionally in the second half of the year. Excessive growth of monetary supply, based on the rapid growth of public expenditures, can affect the ruble and provoke it further weakening.

On August 20, 2009 the Bank of Russia has again decreased the rate of refinancing and other key interest rates. In particular, the refinancing rate was reduced by 0.25 percentage points and set up at 10.75 per cent per annum. Other interest rates of the Central Bank of Russia have been reduced as well (see Table 1.).

Table 1

RF CENTRAL BANK INTEREST RATE FOR CREDIT OPERATIONS

	Term	since 13.07.09	since 10.08.09
Lombard credits (at minimum rate)	14 days	8.5	8.25
	3 months	9.75	9.5
	6 months	10.25	10
	12 months	10.75	10.5
Direct REPO on the basis of an auction: Stock Exchange and OTC (minimum interest rate)	1 day	8	7.75
	7 days	8.5	8.25
	90 days	9.75	9.5
	6 months	10.25	10
	12 months	10.75	10.5
Overnight credit	Overnight	11	10.75
«Currency Swap» (ruble share)	1 day	11	10.75

later, oil price declined by 4.2 dollars per barrel to USD 64.98 per barrel, and the two-currency basket has grown by 72 kopecks to RUR 37.28. According to the estimates of JP Morgan, the cost of a barrel of oil (brand WTI) in the III quarter will be USD 60, and in the IV quarter - USD 65. Apparently, the value of the two-currency basket will stay within that range. Herewith, the volatility is likely to be substantial under the impact of the growing federal budget

	Term	since 13.07.09	since 10.08.09
Lombard credits (at fixed rate)	1 day	10	9.75
	7 days	10	9.75
	30 days	10	9.75
Direct REPO (at fixed rate)	1 day	10	9.75
	7 days	10	9.75
	12 months	10.75	10.5
Credits, secured by non-marketable assets or guarantees (at fixed interest rate)	Up to 90 days	10	9.75
	From 91 to 180 days	10,5	10,25
	From 181 to 365 days	11	10.75
Deposit operations (at fixed interest rate)	«Tom-next», «spot-next», «on demand»	5.75	5.5

Source: RF Central bank.

We would like to remind, this is already the fifth rate reduction, made since April of this year. Thus, the total reduction of the refinancing rate and the rates of the Russian Central bank operations made 2.25 p.p. The need for another rate reduction was urged by the persist low credit activity of the banks, hampering the recovery of economic growth. On the one hand, sustained low domestic demand and reduced ruble monetary supply allowed to pursue a consistent policy aimed at reducing the basic interest rates. However, on the other hand, due to an insignificant inflation growth in July allowed to limit the decline only a quarter of a percentage point, against half a percentage point, as it was in previous months. Further reduction of the interest rates will be possible in the event of inflation deceleration, as well as improvements in credit activity of banks and the state of financial markets. ●

FINANCIAL MARKET¹

N.Burkova, E.Khudko

In August, positive trends were dominating in the dynamics of the Russian financial market. The growth of the global market oil prices, the FRS and ECB statements on the improvement of the global economy, the positive macroeconomic news from the United States, stabilization of the national currency have contributed to positive expectations among investors and growth of the Russian stock market. Herewith, the decline of GDP the United States, Britain and Russia, the unemployment growth in the United States, information about the global losses of Japanese automakers, as well as negative financial reporting of the largest RF banks and the retention of the international rating agencies Fitch u Moody's «negative» credit rating of Russia were restricting the quotations. Positive trends were particularly expressed in the government securities market, where investors' activity has grown 177 per cent. Volatile trends were observed at the domestic market of corporate bonds. On the one hand, the market volume is rapidly expanding; the number and volume of the registered issues is increased, trading volume at the secondary market is extended. Emitters have again applied the mechanism of borrowing through the issuance of exchange-market bonds issuance. But still, the number of actual defaults remain at the record level and the lack of trust of investors to the securities of small companies is sustained.

Government securities market

Within August, growth of oil prices, the reduced risk of the national currency devaluation, stable situation with ruble liquidity, a significant increase in trading volumes in the OFZ market have resulted mainly in the downward trend in the market of government securities yields. Herewith, the growth in activity was observed at the both, primary and secondary federal loan (OFZ) market.

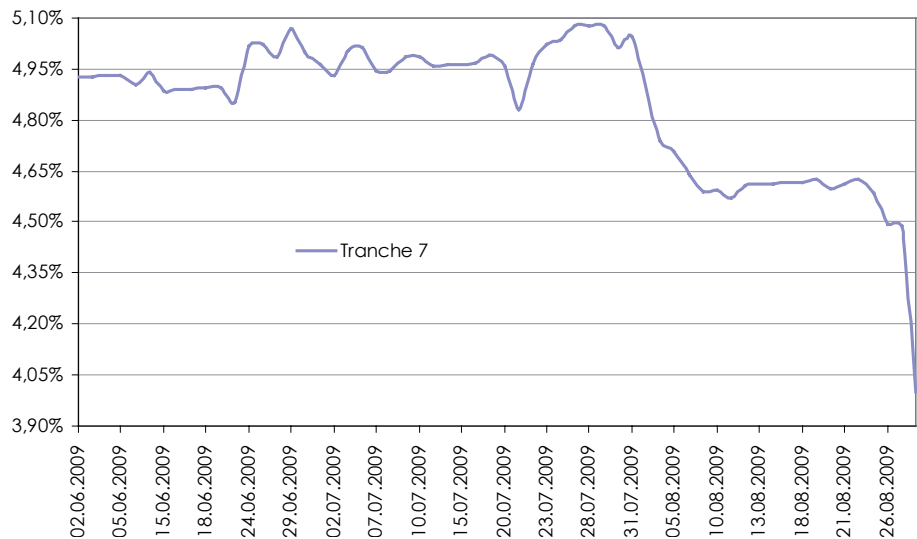
As of August 30, the Russian Eurobonds RUS-30 yield to maturity has decreased as compared with the level of July 22 from 8.05 to 7.03 per cent per annum (by 12.67 per cent), RUS-28 – from 8.24 per cent to 7.70 per cent per annum (by 6.5 per cent), RUS-10 – from 8.03 to 3.87 per cent per annum (by 2.1 per cent) and RUS-18, on the contrary, has grown from 5.07 per cent to 5.42 per cent per annum (by 6.90 per cent). As of the same date, the downgrading trend was also observed in the yields of external currency debt bonds. Thus, the yield to redemption of the seventh tranche of external currency debt bonds has decreased from 4.96 to 4.00 per cent per annum (by 19.35 per cent) (see Figs 1-2).

Within the period from July 23 to August 30, the total turnover of the OFZ secondary market amounted to approximately RUR 91.48 billion with an average daily turnover of RUR 3.39 billion (about RUR 40.29 billion with an average daily turnover of RUR 1.92

¹ In the course of preparation of the survey, there were used analytical materials and surveys published by the “Interfax”, MICEX, RTS, RF Central Bank and the materials presented at web sites of Russian issuing companies.

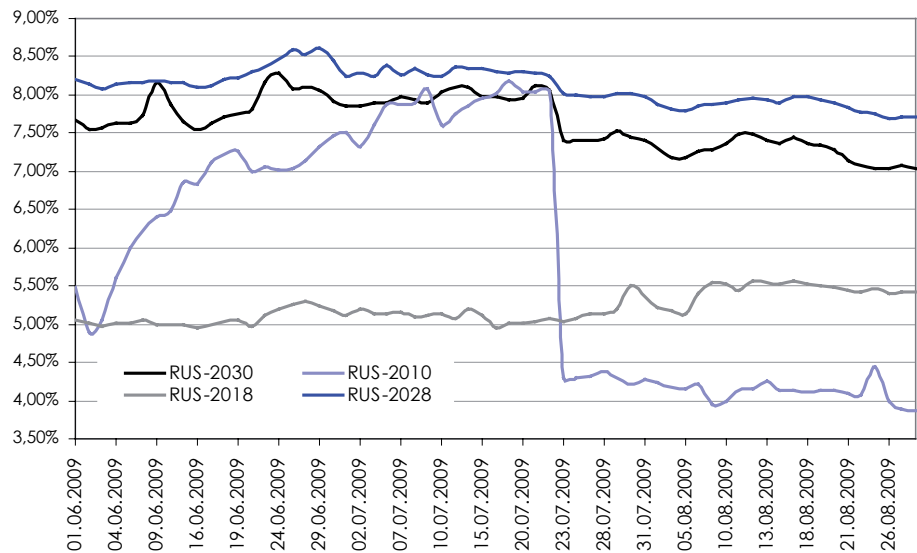
billion in July), what corresponds to the growth of an average monthly turnover nearly by 176.6 per cent.

Within July 22 – August 30, there were five auctions on OFZ additional placements (against four auctions a month before) at the primary OFZ market. Thus, on July 29, there was held an auction on OFZ placement, series 25065 for the amount of RUR 15 bln, actual placement volume was RUR 14.86 mln with an average weighted yield of 12.12 per cent per annum. On August 5, there was an auction on OFZ placement, series 25067 for the amount of RUR 15 bln, actual placement volume reached RUR 12.14 mln with an average weighted yield of 11.97 per cent per annum. On August 12 there was held an auction on additional OFZ placement, series 25006 for the amount of RUR 15 bln, the actual volume was RUR 3.21, actual placement volume reached RUR 3.21 bln with an average weighted yield of 11.39 per cent per annum. On August 19, there was an auction on additional OFZ placement, series 25065 for the amount of RUR 15 bln, actual placement volume reached RUR 3.05 mln with an average weighted yield of 12.10 per cent per annum. On August 26 there was held an auction on OFZ placement, series 25068 for the amount of RUR 5 bln, the actual volume was RUR 4.32 with an average weighted yield of 12.25 per cent per annum. Therefore, the total actual amount of placements within the period under review amounted to 57.8 per cent of the planned amount (versus 34 per cent a month earlier), what is a sign of significant increase in the investor’s interest in the primary OFZ market. Furthermore, in this period there were several auctions on OFZ additional placements in the secondary market (see Table. 1). The total actual placement in the secondary market for the period amounted to 21 per cent of the estimated volume (versus 4 per cent a month earlier). This trend reflects the overall upgrading dynamics in the market of government securities.



Source: “Finmarket information Agency data

Fig. 1. Minfin bonds' yields to maturity in June – August 2009



Source: “Finmarket” information Agency data

Fig.2 Yields to maturity of the Russian Eurobonds with maturity in 2010, 2018, 2028 and 2030 in June – August 2009

Table 1

AUCTIONS FOR OFZ ADDITIONAL PLACEMENTS IN THE SECONDARY MARKET

Auction date	Issue	Auction type	Issue volume, RUR, mln.	Nominal placement amount, RUR, mln	Average yield
23.07.2009	OFZ-25064-PD	Add. placement	165.63	5,00	11,60
23.07.2009	OFZ-25065-PD	Add. placement	456.86	456,86	12,13
23.07.2009	OFZ-25066-PD	Add. placement	7 196.01	256,60	11,41
24.07.2009	OFZ-25064-PD	Add. placement	160.63	14,30	11,62
24.07.2009	OFZ-25066-PD	Add. placement	6 939.41	815,00	11,36
27.07.2009	OFZ-25064-PD	Add. placement	146.33	146,33	11,62
27.07.2009	OFZ-25066-PD	Add. placement	6 124.41	1 710,00	11,31
28.07.2009	OFZ-25066-PD	Add. placement	4 414.41	2 361,81	11,36
30.07.2009	OFZ-25065-PD	Add. placement	141.12	141,12	12,10
30.07.2009	OFZ-25066-PD	Add. placement	2 052.60	650,00	11,35
31.07.2009	OFZ-25066-PD	Add. placement	1 402.60	51,00	11,35
03.08.2009	OFZ-25066-PD	Add. placement	1 351.60	535,01	11,35
04.08.2009	OFZ-25066-PD	Add. placement	816.59	612,56	11,35
05.08.2009	OFZ-25066-PD	Add. placement	204.03	204,03	11,31
05.08.2009	OFZ-25067-PD	Add. placement	2 857.44	159,83	11,92
06.08.2009	OFZ-25067-PD	Add. placement	2 697.61	145,00	11,93
07.08.2009	OFZ-25067-PD	Add. placement	2 552.61	500,00	11,91
10.08.2009	OFZ-25067-PD	Add. placement	2 052.61	1 600,00	11,92
11.08.2009	OFZ-25067-PD	Add. placement	452.61	8,99	11,91
13.08.2009	OFZ-25066-PD	Add. placement	11 786.63	973,71	11,37
13.08.2009	OFZ-25067-PD	Add. placement	443.62	443,62	11,97
14.08.2009	OFZ-25066-PD	Add. placement	10 812.92	70,00	11,36
17.08.2009	OFZ-25066-PD	Add. placement	10 742.92	370,00	11,38
18.08.2009	OFZ-25066-PD	Add. placement	10 372.92	267,00	11,38
19.08.2009	OFZ-25065-PD	Add. placement	10 948.18	1 866,90	12,07
19.08.2009	OFZ-25066-PD	Add. placement	10 105.92	1 945,00	11,37
20.08.2009	OFZ-25065-PD	Add. placement	10 081.28	1 299,00	12,05
20.08.2009	OFZ-25066-PD	Add. placement	8 160.92	1 745,00	11,33
21.08.2009	OFZ-25065-PD	Add. placement	8 782.28	951,00	12,05
21.08.2009	OFZ-25066-PD	Add. placement	6 415.92	1 081,00	11,31
24.08.2009	OFZ-25065-PD	Add. placement	7 831.28	3 180,30	12,04
24.08.2009	OFZ-25066-PD	Add. placement	5 334.92	775,00	11,31
25.08.2009	OFZ-25065-PD	Add. placement	4 650.98	3 095,00	12,03
25.08.2009	OFZ-25066-PD	Add. placement	4 559.92	3 194,50	11,31
26.08.2009	OFZ-25065-PD	Add. placement	1 555.98	1 555,98	12,00
26.08.2009	OFZ-25066-PD	Add. placement	1 365.42	1 365,42	11,30
26.08.2009	OΦ3-25068-PD	Add. placement	678.48	678,48	12,21
Total:			166 815,56	35 230,34	

Source: "Finmarket" information Agency data

As of August 30, the OFZ market has amounted to RUR 1,95.86 bln at face value and to RUR 1,022.1 bln at the market value. (RUR 1,123.93 bln and RUR 948.99 bln accordingly, as of July 22). The duration of the OFZ market portfolio has made 1,735.41 days, having decreased by 76.26 days as compared with the preceding month (as of July 22).

Stock market

Stock market situation

Improved rates of oil prices in the global market and stock indices, positive expectations in terms of global economic prospects, reduced refinancing rate of the RF Central Bank since August 10 (from 11 to 10.75 per cent per annum), information on the reduced unemployment rate and growth of the RF foreign currency and gold reserves on the one hand, in the background of the RF Ministry of Finance estimates of budget deficit in the amount of 9.4 per cent of GDP and its estimated growth up to 13.4 per cent of GDP as of 2009 results, negative financial results of the largest banks as per the first six months of the year (including Bank VTB net loss in the amount of RUR 9.71 bln, as well as decreased net proceeds of Sberbank of Russia), licenses revocation from a number of banks, GDP decrease by 10.2 per cent as of the results of seven months of 2009, confirmed rating of Russia by Fitch agency in early August at the level of BBB with the “negative” forecast, as well as Moody’s “negative” rating of the Russian banking system on the other hand made for a volatile dynamics in the Russian financial market within the month under review.

Thus, in August, a general volatile dynamics was observed in the MICEX index in the background of an upgrading market trend. (See Fig. 3). The minimum value the MICEX index has reached on August 19 - 1,034.08 points (against 871.33 points in the preceding month). The maximum value the MICEX index has reached on August 24, having reached 1,120.54 points (1,120.54 per cent points in the preceding month).

In general, within the period from July 23 to August 30, the MICEX index has increased by 13.32 per cent, what makes about 130.62 points in absolute terms (within the year, from August 31, 2008 to August 30, 2009, the MICEX index has downgraded by 17.6 per cent). Over the same period the turnover of trades in shares, included in the MICEX index, made about RUR 1,723.05 bln at an average daily turnover of RUR 63.83 bln (against RUR 1,197.86 billion with an average daily turnover of RUR 57.04 billion in the preceding period). Therefore, the investors’ average daily activity in the stock market in June has grown as compared with the preceding month by 12 per cent. The indicators of maximum and minimum daily turnover in the market trades in August made, accordingly, RUR 92.53 bln ((as of August 6), and RUR 42.62 bln (on August 17).

As of the month results (from July 23 through August 30), the “blue chips” securities have shown an upgrading trend. The leaders of the downgrading rates were “Mosenergo” (grown by 24.94 per cent, urged by the information on significant net profit extension as of the first six months of 2009, by 354 per cent), “Surgutneftegas” (by 17.94 per cent) and «Sberbank” (by 17.02 per cent). Some lower rates of growth were observed in the shares of “Tatneft” (14.74 per cent), “Bank VTB” (by 14.62 per cent), “Gazprom Neft” (by 11.99 per cent) and “Rosneft” (by 9.37 per cent). They were followed by GMK “Nornickel” (by 8.40 per

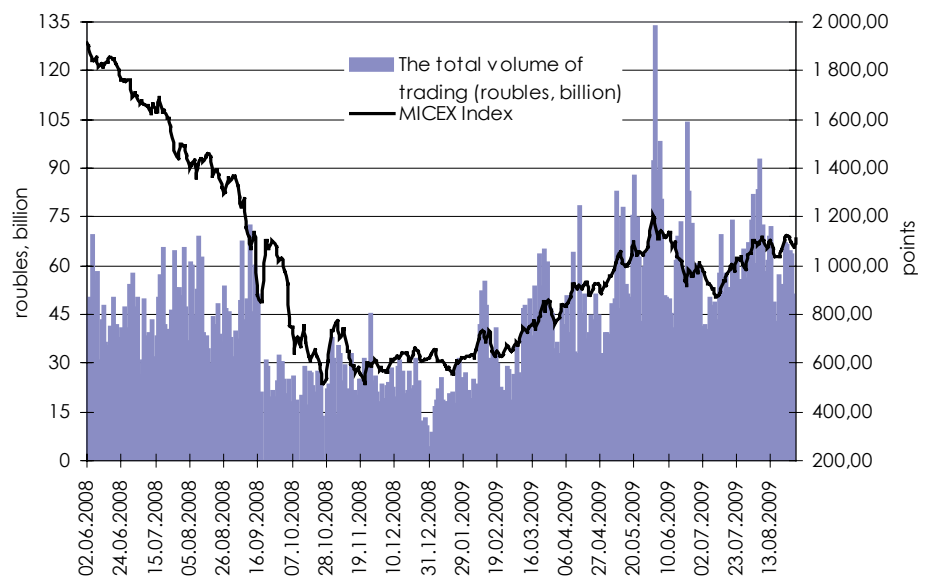


Fig. 3 Dynamics of MICEX Index and trading volume

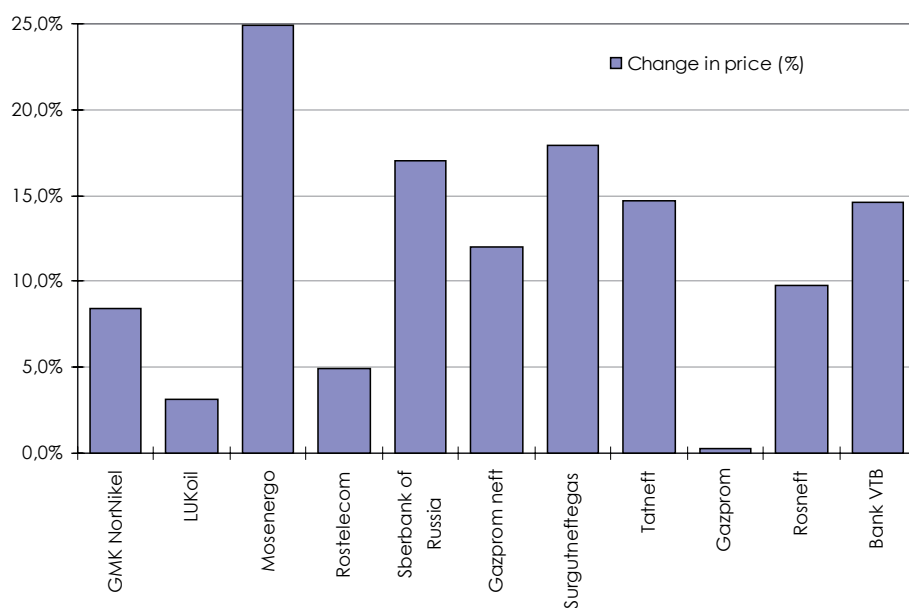


Fig. 4. Dynamics of the Russian Blue Chips from July 23 to August 30, 2009

cent), “Rostelecom” (by 4.94 per cent), LUKOIL (by 3.16 per cent) and Gazprom (by 0.31 per cent). (See Fig. 4).

In August the MICEX turnover leaders were: “Sberbank of Russia” (40.13 per cent of the total turnover), “Gazprom” (23.93 per cent of the total turnover), GMK “Nornickel” (8.31 per cent) “LUKOIL” (6.60 per cent), and “Rosneft” (4.50 per cent). The total share of transactions with the shares of the five «blue chips» was about 83 per cent (all «blue chips» - 89 per cent) of the total trades

in shares at the MICEX stock market during the period from July 23 to August 30.

According to MICEX information, as of August 30, the top five leaders of the domestic stock market in terms of capitalization were: “Gazprom” – RUR 3,965.60 bln (RUR 3,742.31 bln a month earlier), “Rosneft” – RUR 2,145.92 bln (RUR 3,742.31 bln in preceding month), “LUKOIL” - RUR 1,359.21 bln (RUR 1,269.30 bln in preceding month), “Sberbank of Russia” - RUR 1,047.18 bln (against RUR 859.59 bln) and “Surgutneftegas” - RUR 959.96 bln (RUR 786.36 bln in preceding month) .

Futures and Options Market

In August the total turnover in the MICEX (futures) market has increased by 6 per cent as compared with the preceding month. Thus, in the period from July 23 through August 30 the total turnover in the MICEX (futures) market made approximately RUR 81.51 bln (4,196 of transactions, 2.4 mln of contracts), against approximately RUR 77.08 bln (3,123 transactions, 2.2 mln of contracts) in July. The largest volume of trading in August as a month earlier, was observed in foreign currency futures, amounting to RUR 75.29 billion (586 transactions, 2.33 mln of contracts). Herewith, contracts for the US dollar were in the first place in terms of trading in the MICEX futures market section, followed by futures contracts for Euro and for Euro/USD rate. Prices of futures contracts, concluded in August for RUR/USD futures in the short-term MICEX market were made within RUR/USD 31.4-32.7 for September, for RUR/USD 31.7-32.3 for October, RUR/USD 32.3-33.4 for December, RUR/USD 33.3-34 for March 2010 and RUR/USD 34,1–35,1 for June 2010.

The greatest number of transactions (2,627) within the month was made with commodity futures, the volume of trades in those transactions has reached RUR 5.06 billion (nearly 40 per cent more than in preceding month). Trading volume of transactions in futures the stock market instruments has grown within the period under review by 40 per cent (from RUR 827 mln to from RUR 1,156 mln). Herewith, futures for the MICEX index were leading in the short-term MICEX market, followed by futures for «Gazprom» and «Sberbank of Russia» shares. It should be noted, that the value of the MICEX index (the price of transactions) for September made on average 1 000–1 100 points. Therefore, the investors’ expectations regarding the MICEX quotations index have declined by 100 points

as compared with a month earlier. There were no transactions in futures on interest rates in August.

A similar situation was noted in RTS FORTS futures market, where the investors' activity has significantly increased as compared with the preceding month - by 61 per cent. Thus, throughout July 23 – August 30, the total turnover in the RTS futures and options market made approximately RUR 1,599.8 bln (8,186 thou. transactions, 54.57 mln contracts) against about RUR 992.05 bln (thou. transactions, 42.44 mln of contracts) in July. Like before, futures enjoyed the greatest demand: the volume of trades in the period under review made RUR 1,544,16 billion (8,091 thousand of transactions, 52.12 mln of contracts). Herewith, prices of futures contracts, concluded in RUR/USD in the RTS FORTS short-term market for September 15, 2009 were within the range of 31.4–32.5 RUR/USD, for December 15 – RUR/USD 32–33.3, for March 15, 2010 - RUR/USD 33-33.4.

The value of futures for the RTS index (based on the prices of recent contracts) for September 15, 2009 was estimated at 970-1,070 points, for December 15, 2009 – 1,000–1,100 points and within 960–1,100 points and for March 15, 2010 - 960–1,100 points. Options enjoyed far less demand, the turnover made about RUR 55.68 bln (92.25 thousand transactions and 2.44 mln of contracts). The maximum daily turnover in the short-term RTS futures market in August made RUR 74.76 billion (as of August 6), and minimum was RUR 45.42 bln. (on August 19).

External factors behind the Russian stock market dynamics

In August the Russian financial market dynamics, as a month earlier, was largely dependant on the situation in the global financial markets. Among the basic factors of positive global market indicators, affecting the Russian market in August, one should mention:

- upgrading global oil prices (up to USD 75 per barrel);
- optimistic expectations in regard to global economy, in particular, US FRS statement on the reduced funding for the support of national economy due to declined recession;
- the publication of positive macroeconomic news from the United States (in particular, the growth of the houses sales in primary and secondary markets);
- information on the net profit, raised by a number of the major international companies: the US automaker Ford Motor (USD 834 million in the first six months of 2009), the US mortgage agency Freddie Mac (USD 767 million for the II quarter of 2009), by MasterCard company (USD 349 million), the Swiss bank Credit Suisse (Euro 2,36 billion), the British bank Barclays (USD 3,16 billion);
- decision of the British central Bank to take supplementary measures for the support to the national bank sector; in particular, addressing GBP 50 bln for the purchase of bank assets;
- information on GDP growth in Germany by 0.3 per cent in II quarter of 2009;
- decision of Swedish government to allocate about Euro 83 mln for the improvement of the unemployment situation in the country;
- US FRS decision to keep up the basic interest within 0–0.25 per cent.

Along with the above, the following events were retraining the global markets growth within the month:

- Information on the reduction of the net profit of Microsoft Corp. by 18 per cent to USD 14.57 bln and French bank Soci t  G n rale S.A. to Euro 31 mln (56 times);
- publication of information on the net losses of the largest French airline Air France in the II Quarter of 2009 (about Euro 430 million), the Japanese auto manufacturers (Mazda Motor, Mitsubishi Motors Corp. and Nissan Motor Corp.), German bank Commerzbank AG (Euro 1,61 billion in the first quarter), British financial group Lloyds Banking Group (GBP 4 billion in the first six months of the year) and Royal Bank of Scotland (Euro 1,23 billion in the first six months of 2009)

- information of US GDP reduction in the II quarter 2009 by 1 per cent, as well as GDP of Great Britain by 0.7 per cent (as compared with the preceding quarter);
- increased level of unemployment and reduced demand for durable goods in USA;
- international rating agency Standard & Poor's downgraded rating of the French automaker PSA Peugeot Citroen.

All these factors have generally resulted in the volatile dynamics of the global stock indices in August, as compared with the indicators of early 2009, as well as of the preceding month results. Thus, as of results of August, the markets of individual developing countries have shown high volatility, but the upgrading trend was prevailing, what has resulted in the indices growth by 7-9 per cent. A similar trend was observed in the markets of European countries, where those indices were demonstrating growth rate by 5-12 per cent (See Table 1 and Fig. 5).

Table 2

DYNAMICS OF THE GLOBAL STOCK INDICES (AS OF AUGUST 30, 2009)

Index	Ticker	Value	Dynamics within the month(%)	Dynamics since the year beginning(%)
MICEX (Russia)	MICEXINDEXCF	1 111,33	13,32	79,38
RTS (Russia)	RTSI	1 089,46	13,12	72,41
Dow Jones Industrial (USA) Average (USA)	DJI	9 544,20	7,46	8,75
NASDAQ Composite (USA)	NASD	2 028,77	5,32	28,64
S&P 500 (USA)	SPX	1 028,93	7,85	13,91
FTSE 100 (UK)	FTSE	4 908,90	9,24	10,71
DAX-30 (Germany)	DAX	5 517,35	7,73	14,70
CAC-40 (France)	CAC	3 693,14	11,74	14,77
Swiss Market (Switzerland)	SSMI	6 211,58	10,19	12,23
Nikkei-225 (Japan)	NIKKEI	10 534,14	8,34	18,90
Bovespa (Brasil)	BUSP	57 700,57	8,72	53,66
IPC (Mexico)	IPC	28 599,92	8,79	27,79
IPSA (Chile)	IPSA	3 222,13	-0,08	35,59
Straits Times (Singapore)	STI	2 642,80	7,83	50,03
Seoul Composite (South Korea)	KS11	1 607,94	7,62	43,00
ISE National-100 (Turkey)	XU100	47 559,69	24,54	77,04
BSE 30 (India)	BSE	15 922,34	7,27	65,04
Shanghai Composite (China)	SSEC	2 860,69	-13,22	57,11
Morgan Stanley Emerging Markets Free Index	EFM	679,23	5,69	48,42

* – Versus index indicator valid on July 22, 2009.

Corporate news

OAO "Bank VTB"

In late July-August OAO «Bank VTB» in the framework of the national program for the support of the Russian economy was continuing to provide credits to domestic enterprises: on July 29, a loan was granted to OOO «Mariysky refinery» in the amount of RUR 3 425 billion for the period of 3 years, and on August 28 – credit to the Federal State Unitary Enterprise «GTK Russia» in the amount of RUR 700 million. Moreover, on August 27, OAO «Bank VTB» the first loans were provided under the state guarantees: to JSC «Kamaz» was granted the first credit tranche, amounting to RUR 2.9 billion (under the state guarantee of RUR 1.45 billion), to JSC «Sollers» - loan in the amount of RUR 1 billion (under the state

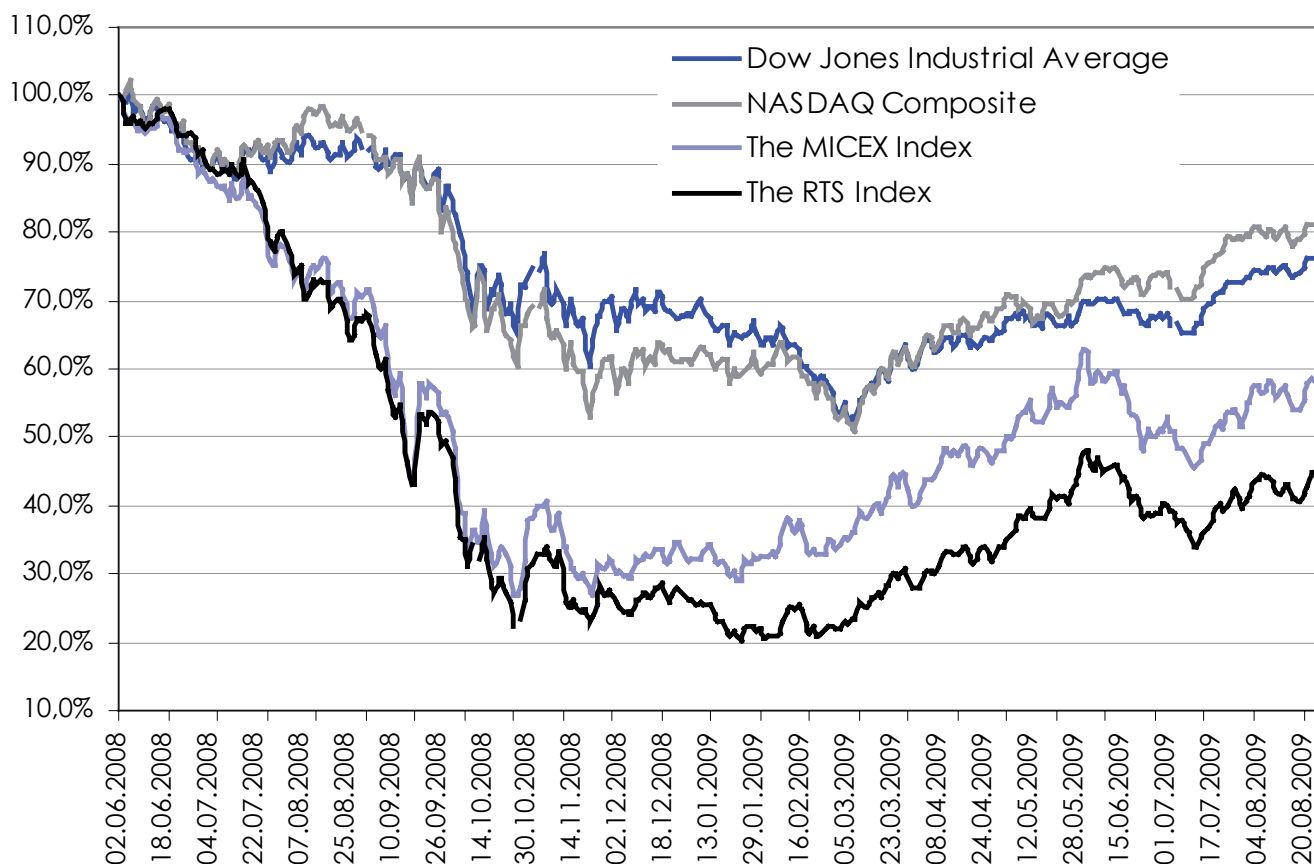


Fig. 5. Dynamics of the main USA and Russian stock indexes (in % to the date 01.06.2008)

guarantee of RUR 500 million), to OJSC «Sollers-Naberezhnye Chelny» - loan of RUR 700 million (under the state guarantee of RUR 350 million).

On July 30, OAO «Bank VTB», and the Export-Import Bank of Thailand Kingdom signed an agreement on the financing of trade transactions, providing for the granting of OAO «Bank VTB» credit line to purchase Thai goods by the importers from Russia for the amount of USD 30 million.

On July 31 OAO «Bank VTB» has placed a debut Eurobond issue for 750 million Swiss francs for the term of 2 years, the coupon rate was 7.5 % per annum.

On August 4, OAO «Bank VTB» has disclosed performance results for the I quarter of 2009, developed under IFRS: net losses amounted to UR 20.5 billion, capital-adequacy ratio has declined from 17.3 to 15 per cent. On August 5, OAO «Bank VTB» has disclosed non-consolidated reporting developed under RAS for July 2009: on August 1, the assets amounted to RUR 2,599 billion (against RUR 2,551 billion as of January 1, 2009), the net losses for the first 7 months of 2009 decreased to RUR 9.71 billion (in the first half of 2009 the losses were RUR 26.45 billion).

On August 25 a memorandum was signed between OAO «Bank VTB» and shareholders of «Don Stroy» group of companies on the transfer to the Bank a controlling block of shares in JSC «Don Stroy Invest» (50per cent plus one share) for the restructuring of the current Debt of PP «DON-Stroy», as well as for providing surplus funding for project financing.

OAO «Gazprom»

On July 31 OAO «Gazprom» in the framework of the national Eastern gas program for the organization of new gas centers has begun the construction of gas transmission system «Sakhalin - Khabarovsk - Vladivostok».

On August 26 OAO «Gazprom» has disclosed interim consolidated abbreviated performance reporting, developed under IFRS for the I quarter of 2009: the profit amounted to RUR 110 177 million, which is 2.6 times less than in the same period of 2008.

OAO «Gazprom neft»

On August 3, OAO «Gazprom neft» and Administration of Yamalo-Nenets autonomous region have signed a Framework Agreement on cooperation for 2009-2011, focused at the socio-economic development of the territory, supporting the investment and research and technological capacity of YAN region, as well as incentives for development of the oil industry.

On 17 August OAO «Gazprom neft» has acquired a network of gas stations in Chelyabinsk region, which includes 40 stations and 2 oil storage depots.

OAO «LUKOIL»

On August 24 OAO «LUKOIL» has attracted a syndicated loan in the amount of USD 1.2 billion for the term of 3 years for general corporate purposes, refinancing of the existing financial indebtedness and for financing operations related to oil exports, the interest rate was LIBOR plus 4 per cent per annum. The loan is secured by the sales under oil export contracts.

On August 28, OAO «LUKOIL» has disclosed consolidated financial reporting, developed under US GAAP for the first six months of 2009: net profit amounted to USD 3 229 million, EBITDA made USD 6 534 million, sales proceeds – USD 34 861 million.

OAO «Mosenergo»

On August 12, OAO «Mosenergo» has disclosed unaudited performance results under RAS for the first six months of 2009: net profit has grown by 354 per cent as compared with the first six months of 2008 and amounted to RUR 6 384 million.

OAO «Rostelecom»

On August 5, OAO «Rostelecom» has disclosed unaudited results for the first six months of 2009 according to RAS: net profit decreased by 52,6 per cent to RUR 2 364.4 million, the rate of OIBDA (total revenues less cost of core business activities before depreciation) amounted to RUR 5 778.3 million, OIBDA profit margin made 18.9 per cent.

Sberbank of Russia

In August, Sberbank of Russia continued to provide loans to domestic enterprises in the framework of the Program for the support to priority sectors of the Russian economy. In particular, Sberbank of Russia provided credit/credit lines to OOO «Gaztekhleasing» (amounting to RUR 1.4 billion), to SUE «Concern «Teplichny» (RUR 120 million), to ZAO «CENTER-CAPITAL» (RUR 500 million), to «Evraz» Group of companies (RUR 8,8 billion), to OAO «Mordovtsement» (RUR 250 million), to OOO «Shushenskaya Marka» (RUR 200 million), to OOO «Top-Kniga» (RUR 500 million), to OAO «Tumenenergo» (RUR 4,6 billion), to OOO «Communal Technologies» (RUR 200 million), to OAO NPO «Iskra» (RUR 370 million), to OAO «Hantymansiyskgeofizika» (RUR 600 million), to OAO Oil Company «Magma» (USD 200 million).

On August 3, OOO «Sberbank Capital» has concluded an agreement with Urals Energy on the ownership transfer to ZAO NC «Dulisma» as a settlement of the debt in the amount of USD 630 million.

On August 24, Sberbank of Russia has disclosed financial performance results for 7 months of 2009 developed under RAS: net profit amounted to RUR 6.8 billion against RUR

81.8 billion within 7 months of 2008, Russian companies were granted loans amounting to about RUR 2 700 billion.

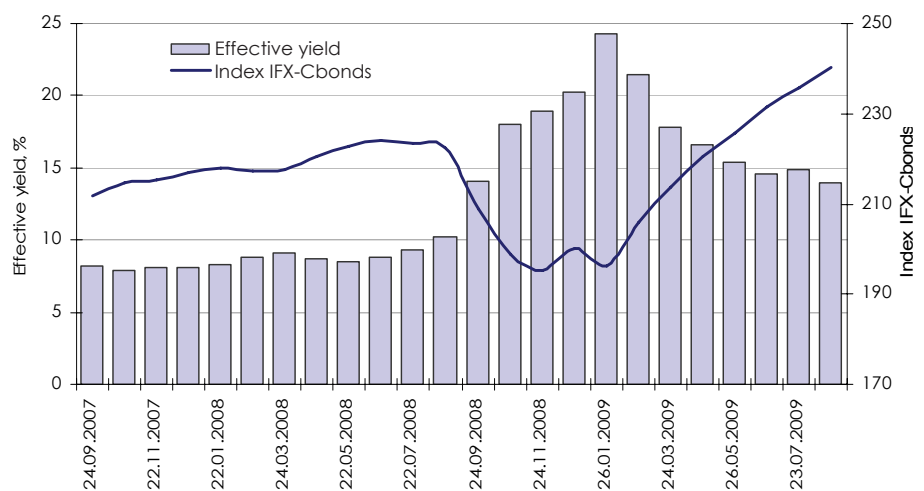
Corporate bonds market

The volume of the Russian domestic stock market (as per nominal value of shares in circulation, denominated in national currency) is continuously growing in the past months and in August it RUR 2,039.3 bln (711 emissions by 443 emitters), which exceeds the indicator of preceding month by RUR 6.6 per cent¹. The number of emissions has significantly increased, whereas the number emitters stayed the same (for comparison, in late July there were 693 emissions, made by 443 companies). Also currently there are two issues of bonds, nominated in US dollars and Japanese yens in circulation. There is sustained trend to expand the transactions scope with corporate bonds in the secondary market. In the background of the same number of transactions (25.4 thousand), the value of transactions within July 23 0 August 28 has grown nearly 1.5-fold as compared with the preceding relevant period and reached RUR 80.9 bln².

Since January of the current year the index of the Russian market of corporate bonds IFX-Cbonds is continuously growing. Within the period from July 24 to August 26, the index has grown more than by 4.8 points (or 2.0 per cent), having reached the highest level since the beginning of its assessments. After some growth, the effective yield, has decreased from 14.87 to 13.93 per cent during the period under review (see Fig. 6). The duration of corporate bonds market portfolio as of August 26 has made 393 days, what is by 25 days more as compared with the late July of the current year.

As compared with preceding months, in August of the current year a significant increase in the number and total amount of registered issues of corporate bonds was noted. In the period from July 24 to August 25 there were registered 18 of bond issues for the total amount of RUR 83.2 bln (for comparison, between June 26 and July 23 there were registered 13 issues of corporate bonds totaling to RUR 15.9 billion). The majority of the reported were issued by “Joint Stock Company for Oil Transport «Transneft” for RUR 35 bln, three series of bonds of ZAO “Raiffeizenbank”, totaling to RUR 20 billion, and one issue of OAO “Sedmoy Continent” bonds, totaling to RUR 5 billion⁴.

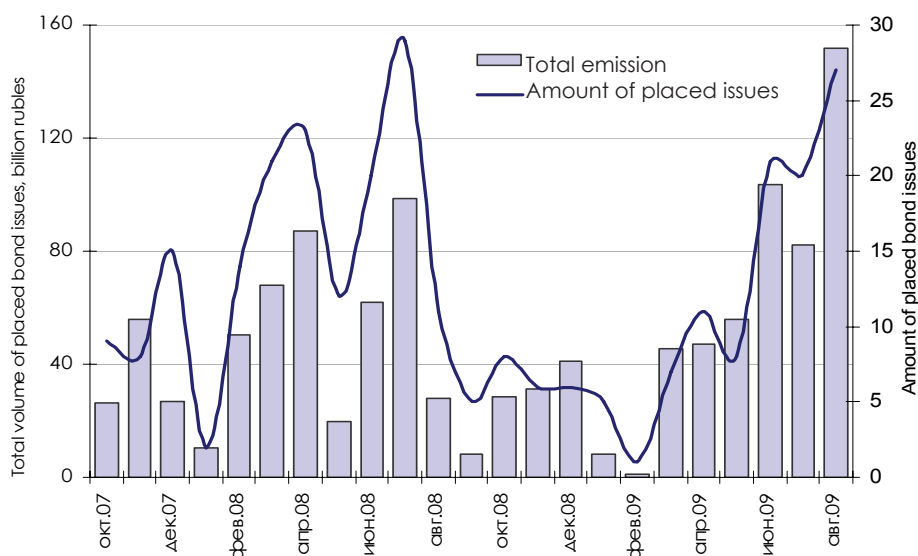
In August, there was observed a growth also in the total volume of corporate bonds placed issues. Thus, in the period from July 24 to August 26, there were 27 bonds issues, totaling to RUR 152.0 billion, which is the maximum indicator for the bonds, denominated in RUR, within the last



Source: Cbonds data.

Fig. 6. Russian corporate securities index and average weighted yield dynamics³

- 1 As per Rusbonds information
- 2 As per «Finmarket» information agency
- 3 As per Cbonds company data.
- 4 As per Rusbonds company.



Source: Rusbonds data.

Fig. 7. Corporate securities primary placement dynamics¹

two years (for comparison, from June 26 to July 23 there were placed 20 bond issues, totaling to RUR 82.0 billion (See Fig. 7). During the period under review the major bond issues were placed by OAO “Russian Railways” (two series of bonds amounting to RUR 40 billion), OAO “LUKOIL” (six series of bonds amounting to RUR 30 billion), OAO «Joint-Stock Financial Corporation «System» (one series of bonds for RUR 20 billion) and OAO «Mobile Telesystems» (one series of

bonds for RUR 15 billion). Herewith, OAO «The Fifth Power Generation Company of the Wholesale Electricity Market» has placed two debut issues of corporate bonds, totaling to RUR 4 billion.

In the period under review there was again a large number of issues, recognized invalid due to non-placement of any security. Thus, in the period from July 24 through August 26 the Federal Statistical Service for Financial Markets of Russia has recognized as invalid five issues of corporate bonds, offered for open placement (versus six bonds issues within June 26 – July 23)².

Within July 24 through August 26, 12 emitters had to redeem bonded loans totaling to RUR 24.6 billion. However, five emitters have announced a technical default on repayment of their bonds, totaling to RUR 6.0 bln. In September 2009, 15 issues of corporate bonds redemption for the total amount of RUR 21.2 bln are expected³.

In August there was maintained a negative trend for failure of the emitters to perform their liabilities in regard to the bonds holders. From July 24 to June 25 the default on offer (bonds redemption) was announced by 10 emitters (within April 24 to August 26 there were nine emitters) and 16 emitters have failed to repay the coupon yield (there were 18 of those in the preceding period)⁴.

Real default on failure to repay the nominal value of the bond loan within the period under review was announced by 7 emitters for the total amount of RUR 7.95 bln (5 emitters in preceding period, the scope of non-performed obligation was RUR 3.75 bln). On six bonds issues the emitters have reached an agreement with the bonds holders on the debt restructuring.

1 As per Rusbonds information.

2 По данным ФСФР России.

3 As per Rusbonds data.

4 As per Cbonds data.

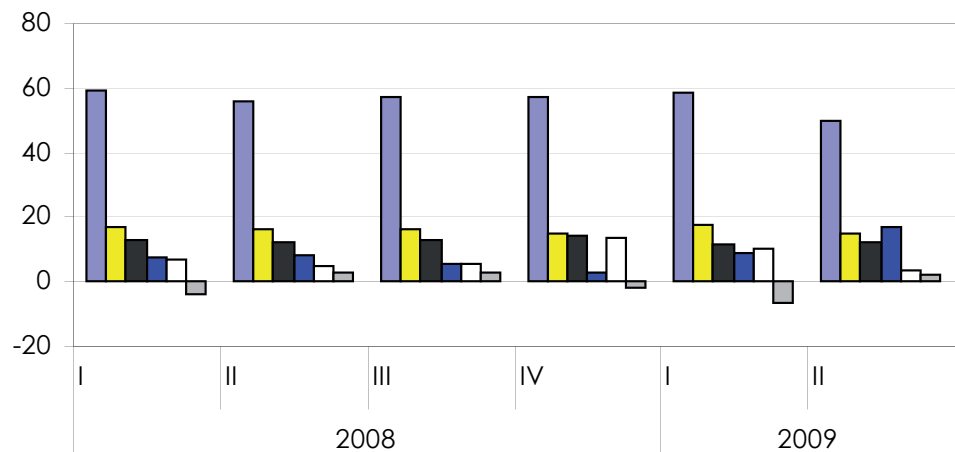
REAL ECONOMY: TRENDS AND FACTORS

O.Izryadnova

The reduction of investments in fixed assets by 18.8% in January–July 2009 of the level of the corresponding period of the previous year, of industrial production – by 14.2% and of the retail trade turnover – by 3.8% had a considerable effect on the internal market. Stagnant dynamics of the consumer market in the current year was defined by the decrease in the real disposable incomes of the population by 0.9% versus January–July 2008 and real wages – by 3.0%. the sustention of the tension at the labor market and the increase of the total number of the unemployed (calculated by the methodology of the International Labor Organization) up to 6.3 million of people in July 2009 or by 8.5% of the economically active population continued to make a negative effect. On the contrary, the increase in profitability of the processing industry had a positive effect, this, however, does not give any grounds for optimism when estimating the development in production till the end of the year, taking into account the aftermath of the catastrophe at Sayano–Shushenskaya hydro power plant.

In July of the current year the macroeconomic situation was defined by the influence of the factors and trends formed in the first half of 2009.

The internal market was severely affected by the decrease of investments in fixed assets by 18.8% in January–July 2009 versus the level of the previous year, in industrial produc-



	2008				2009	
	I	II	III	IV	I	II
purchase of goods	59,3	55,6	57,3	56,9	58,8	49,8
payments for services	17,2	16	16,1	14,8	17,5	15,2
compulsory payments	12,7	12,5	12,7	14,1	11,8	12,4
saving	7,7	8,2	5,8	2,5	8,7	17,1
purchase of foreign currency	6,9	4,7	5,6	13,3	10,3	3,5
change of the amount of cash	-3,8	3	2,5	-1,6	-6,6	2

Source: Federal State Statistics Service

Fig. 1. Structure of Use of Incomes of Population in 2008-2009, As Percentage to The Total

tion – by 14.2%, in the workload in construction – by 19.0%, in freight transportation turnover – by 16.3%, including at railway transportation – by 19.6%.

The situation was aggravated by the negative dynamics of the consumers' demand. In July 2009 the inflation at the consumer market reached 8.1% since the beginning of the year the prices for foodstuffs growing by 7.6%, for non-food goods – by 7.0%, for paid services – by 3.7%. As compared with January–June 2008 the market of non-food goods was observed to contract by 5.9%, the market of foodstuffs – by 1.8%. The stagnant dynamics of the consumers' market was defined by the decrease of the real disposable monetary incomes of the population by 0.9% versus January–July 2008 and the real wages – by 3.0%.

Under the existing dynamics of prices and incomes in the 2nd quarter 2009 the trend for the decrease of expenditures for current consumption became more intensive – them going down to 65% of the total incomes of the population versus 76.3% in the preceding quarter of the current year. The uncertainty in the steadiness of monetary incomes predetermined the increase of the inclination of the population for saving, the volumes of the purchase of foreign currency decreasing gradually: the share of saving in the incomes of the population went up to 17.1% versus 8.7%, and the proportion of the currency purchase decreased, correspondingly, to 3.5% versus 10.3% in the analogous period of the previous year.

In the structure of monetary incomes of the population in the 2nd quarter 2009 the significance of the labor remuneration and social payments increased as compared with the corresponding period of the previous year, the proportion of the incomes from entrepreneurial activity and the incomes from property decreasing.

Table 1

STRUCTURE OF MONETARY INCOMES OF POPULATION, AS PERCENTAGE TO THE TOTAL

	Total of monetary incomes	Including				
		Profits from entrepreneurial activity	Labor remuneration, including the hidden wages	Social payments	Incomes from property	Other incomes
2008						
1 quarter	100	10.2	68.4	13.3	6.1	2.0
2 quarter	100	9.6	68.4	12.7	7.4	1.9
3 quarter	100	10.2	69.0	12.4	6.4	2.0
4 quarter	100	9.9	68.5	13.0	6.6	2.0
2009						
1 quarter	100	10.2	69.4	14.7	3.8	1.9
2 quarter	100	9.1	71.2	13.9	3.8	2.0

Source: federal State Statistics Service

There was a continuing tension at the labor market: in July 2009 the total number of the unemployed (calculated on the basis of the methodology of the International Labor Organization) increased up to 6.3 million of people or 8.5% of the economically active population, the number of the officially registered unemployed went up to 2.1 million of people, and the tension coefficient (the number of the unemployed registered in the state employment services per one vacant position) made 2.1 versus 1.0 in the corresponding period of the previous year.

The trend for the recession in the industry sustaining, the production index in minerals extraction made 96.9% in January–July 2009 versus the level of the corresponding period of the previous year, the index for fossil fuels being 97.6%. The production of oil, including gas condensate, made 284 million of tons in January–July 2009 or 100.3% versus the corresponding period of the previous year of 2008, and 41.8 million of tons (101.4%) in

July. The proportion of the processing of oil in its production made 47.9% versus 48.3% in January–July 2008. According to the data of the Ministry of Power of the Russian Federation the total export of oil in January–July 2009 is estimated to be 142.1 million of tons or 99.4% versus the corresponding period of 2008.

Since November 2008 the reduction of the investments necessary to maintain the current production and develop new fields was added to the exhaustion of the exploited oil fields and insufficient increase in the reserves of hydrocarbons which are the factors that traditionally account for the decrease in the production. According to the data of the Central Dispatcher of the Heat and Energy Complex of the Ministry of Power of the Russian Federation, in January–July 2009 the total amount of oil well drilling made 95.2% of the level of January–June 2008, the level of development drilling being 97.6%, and of exploratory boring – to 58.1%.

In January–July 2009 the gas production reduced by 20.2% of the level of the corresponding period of the previous year and made 315.3 billions of cu. m. The reduction in the volume of gas production was connected with the continuing decrease of the demand at the internal and primarily at the external markets. In January–July 2009 the consumption of the gas in Russia (according to the preliminary data of the Central Dispatcher of Power and Heat Complex) made 248.8 billion of cu.m. or 91.4% of the level of the corresponding period of 2008. The proportion of export in the total volume of gas production reduced to 24.3% in January–July 2009 versus 31.2% in January–July 2008, and the volume of export reduced by 36.6% versus January–July 2008 and made 78 billion of cu.m., export to non-CIS countries being 61.4 billion of cu.m.

Electricity, gas and water production and distribution reduced by 5.9% in January–July 2009 versus the corresponding period of the previous year.

Over January–July 2009 there were 567 billion of kWh of power produced which makes 93.8% versus January–July 2008, of which in July – 71.1 billion of kWh (93.2 versus July 2008). In January–July 2009 the production of energy at hydro power plants increased by 9.6% as compared with the corresponding period of 2008, at heat and nuclear power stations – by 10.4% and 4.5%. The proportion of the electric energy produced by hydro power plants in the total production of power went up from 16.1% in January–July 2008 to 18.8% in January–July 2009, that produced by nuclear power plants – from 15.8% to 16.1%, the proportion of the electric power produced by heat power plants reducing to 65.0% versus 68.1%.

A considerable increase in the production of electric power at hydro power plants was connected with the favorable hydrologic situation at the number of rivers of European part of Russia and Siberia. Thus, in January–July 2009 the production of electric power at Volga–Kama cascade went up by 11.3% (by 2.7 billion kWh), at Angara–Yenisei – by 14.0% (by 6.5 billion of kWh). Due to the catastrophe at Sayano–Shushenskaya hydro power plant the situation in the power industry will change fundamentally since the catastrophe affected about 15% of the production of the electric power in Siberia.

In January–July 2009 the consumption of electric power made 558.2 billion kWh, which is 6.0% lower than in the corresponding period of 2008, and in July 2009 – 70.3 billion kWh (by 4.8% lower). Over January–July 2009 the balance of export and import interchange of electric power is estimated to be at the volume of 9.3 billion kWh, which is 13.1% higher than the level of the previous year, which is accounted for by the increase of export to Baltic countries, republic of Belarus and non-CIS countries as well as the decrease in import supplies of electric power.

In the processing industries the output of goods over January–July 2009 reduced by 20.3% versus January–July 2008. The machine–building production oriented to the internal market of investment goods turned out to be vulnerable in the environment of crisis. The production of machinery and equipment reduced by 34.2% in January–July 2009 versus the corre-

sponding period of the previous year, production of electronic, electric and optic equipment reduced by 37.8% and the production of transport vehicles and equipment – by 39.6%.

A considerable decrease of promising projects in construction continues to have a negative effect on the production of machinery and equipment used in house and road construction – production of excavators reduced by 88.1% versus the level of January–July 2008, production of truck cranes – by 86.1%, production of construction loaders – by 77.2%.

As a result of the decrease of the investment programs of the industrial enterprises the decrease of machine tools production continues (by 65.5%), the same applies to the equipment used in metallurgy sector of the industry: equipment for blast and steel–melting furnaces – by 63.1%, shaft conveyor band – by 58.7%, rolling equipment – by 54.8%.

Production of machinery and equipment for agriculture and forestry reduced by 27.1% in January–July 2009 versus the level of January–July 2008. The main contribution to this drop was made by the reduction of production of wheel tractor – by 48.8%, of forage combine harvesters – by 42.9%, of combine harvesters – by 6.8%, which is also connected with the decrease of the demand from the producers of agriculture goods.

The production of household appliances continues to decrease (by 33.1%), which is accounted for by the decrease of consumer demand, connected with the decrease of the incomes of the population and the worsening of the conditions for crediting.

The contraction of the production of transport vehicles and equipment is observed for nearly all kinds of produced goods in January–July 2009. The decrease of the demand for the services of railway companies, decrease of the volumes of purchase and the delays with payments for orders by the OJSC Russian Railways still have a negative effect on the volumes of production of railway equipment. Thus, in January–July 2009 the production of freight and passenger cars reduced by 57.8% and 26.4%, correspondingly, and of mainline diesel locomotives – by 21.4%.

As compared with the corresponding period of 2008 in January–July 2009 the production of passenger cars reduced by 59.4%, and of trucks – by 71.2%.

The adopted measures for the government support of the automobile industry of the Russian Federation, including those aimed at the stimulating of the demand, has not so far enables to limit the development of the crisis trends in the domestic automobile industry.

In the sector of goods of the intermediate demand it is the production of construction materials (69.85 versus January–July 2009), chemistry industry (84.6%), production of rubber and plastic goods (84.2%), processing of timber and production of goods thereof (74.7%) and pulp–and–paper industry (83.8%) that are characterized by the deepest rates of the recession.

The dependence of the Russian timber industry complex on the situation at the external markets being deep, the demand and process for the production of timber processing lowering at the external markets were the factors aggravating the recession of the domestic industry. The share of export production being approximately at the level of 45% in timber processing complex, export of unprocessed timber reduced nearly by half in terms of value as compared with January–June 2008.

The index of chemistry production in January–July 2009 made 84.6% versus the corresponding perios of 2008. In the chemistry industry complex the recession of the production was also connected with the contraction of the external as well as the internal market. According to the data of the Federal State Statistics Service, export of goods belonging to the chemistry industry complex pver January–June 2009 reduced in terms of value down to 59.4% versus the corresponding period of the preivous year.

In January–July 2009 the production of mineral fertilizers made 78.1% cerssu January–July 2008, the output of soda ash making 75.95, of caustic soda – 83.1%, of sulphuric acid – 79.6%, of synthetic ammonia – 95.3%. the production of synthetic caoutchouc redced by 33.4% in

January–July 2009 as compared with the corresponding period of 2008, of synthetic resins and plastics – by 7.9%, of chemical fibers and filaments – by 20%.

Index of production of rubber and plastic goods in January–July 2009 made 84.2% versus the corresponding period of 2008. The world financial crisis had the most adverse effect on the automobile industry and the adjacent industries. In January–July 2009 the production of tires for trucks made 59.1% versus January–July 2008, tires for passenger cars – to 59.7%, tires for agriculture machinery – 57.8%.

The demand of the internal market for metal is provided by the growth rates of metal-consuming kinds of economic activity – machine-building, construction, defence and fuel and energy complexes. The index of metallurgical production and production of finished metal goods in January–July 2009 made 75.0% versus January–July 2008. In January–July 2009 there was 74.9% of cast iron and blast-furnace ferroalloys, 71.5% of steel, 75.0% of the finished rolled ferrous metals, 70.5% of steel pipes produced at metallurgical enterprises of Russia.

In January–June 2009 the physical volume of export of ferrous metals made 77.2% of the figure of January–June 2008, and import of ferrous metals reduced nearly by half.

Taking into account the dynamics of the production and demand of the main consumers the capacity of the internal market of rolled metal in January–June 2009 contracted to 55.7% versus the corresponding period of the previous year.

The contraction of the consumer demand, deficit of the liquid funds necessary to purchase the raw materials, high cost of the credit resources as the main factors for the sharp slowdown of the production in the consumer complex have been in effect since the second half of 2009. The aggravation of the recession of the domestic production of consumer goods which was not compensated by the import supplies that form 34% of the retail turnover of foodstuffs and 53% of the retail turnover of non-food goods can have a negative effect on the dynamics and the structure of the consumer market, taking into account the weak reaction of the producers to the expansion of the import-substituting productions. In January–June of the current year the index of foodstuffs production made 97.8% of the level of January–July 2008, of textile and sewing production – 77.9%, of leather, leather goods and footwear – 92.0%.

Index of textile production in January–July 2009 made 74.2% versus January–July 2008. The drop of the output of cotton fabrics by 32.2% versus January–July 2008 is mainly accounted for by the contraction of the demand for finished goods as well as shortage of monetary funds for purchase of the necessary volume of raw materials (cotton), which is testified by the drop of import volumes by 40% over January–June 2009. The decrease in the production of woolen fabrics by 23.8% over January–July the same as in the previous years was accounted for by the shortage and low quality of the domestic raw materials, absence of production of the demanded fabrics of new generation.

The decrease in the production of linen fabrics by nearly one third as compared with January–July 2008 is accounted for by both the reduction of export (89.4% versus January–June 2008) and by the decrease in the consumer demand for textile from linen as well as by the low quality of raw material (flax fiber).

The growth of the production of knitted goods of 1.4% versus January–July 2008 should be noted, which occurred against the background of the reduction of knitted goods import by 6.2% of the level of January–June 2008.

In January–July 2009 the decrease in production of leather, leather goods and footwear down to 92.0% of the level of January–July 2008 is accounted for by the reduction in leather tanning and dressing (80.0%) and footwear dressing (94.6%). The volumes of import supplies of footwear made 69.4% in terms of physical volume over January–June 2009. The contraction of the consumer demand primarily affected footwear import and not

the domestic production, which testifies that the processes of import substitution for these kinds of goods are being formed.

On the whole over the economy the dynamics of the financial results of the activity of the enterprises in the 1st half of 2009 was defined, on the one hand, by the decrease in production, and, on the other hand, by the increase of producers' prices in minerals extraction by 48.5%, in electricity, gas and water production and distribution – by 118.6% against the background of drop of prices for freight transportation by 0.8%. As a result of the diversified action of these factors the structural shifts in the distribution of incomes by kinds of activities have intensified.

In the 1st half of 2009, according to live data, the balance financial result (profit minus losses) of organizations (not taking into account the subjects of small-scale entrepreneurship, bank, insurance and budget organizations) made RUR +1634.4 billion in current prices. In the second quarter of the current year the balanced result on the whole throughout the economy made 66.0%, and 54.1% throughout the industry versus the level of the corresponding period of the previous year. It should be noted that the financial indices of the current year have been improving gradually as compared with the critical figures of the 4th quarter 2008. The positive moment of the second quarter was the increase of processing industry profitability, this, however, does not give grounds for optimism when estimating the development of the production till the end of the year, taking into account the aftermath of the catastrophe at Sayano–Shushenskaya hydro power plant.

Table 2

BALANCE FINANCIAL RESULT OF ORGANIZATIONS AS BROKEN BY KINDS OF ECONOMIC ACTIVITY IN 2008–2009, AS RUR BILLION

	2008				2009	
	I quarter	II quarter	III quarter	IV quarter	I quarter	II quarter
Total	1260	1979.9	1200.9	–442.2	366.5	1267.9
Minerals extraction	250.9	381.6	304.2	–64.2	130.6	252.9
Fossil fuels extraction	43.8	55.8	54.6	–69.6	149.1	227.1
Processing industries	451.3	775.2	583	–115.8	–67.3	347.8
Electricity, gas and water production and distribution	75.7	–3.4	–41.9	68.2	126.5	23.7
Construction	14.1	37.9	37.4	41	0.9	28.3
Wholesale and retail trade	296.2	401.3	245.1	–374.8	83.2	310.8
Transport	100.9	97.3	97.3	–8	10.3	122.9
Communication	66.3	99.9	90.4	30.1	41.2	88.8
Operations with real estate, rent and services rendering	97.1	131.1	19.9	44.7	16.3	77.8

RUSSIAN INDUSTRY IN AUGUST 2009

S.Tsukhlo

After definitely positive dynamics of July the August trends turned out to be not that good. However there was no return to the grave figures of the first half of the year. The enterprises' plans and forecasts continue to improve and the problem of the stocks of finished goods seems to have been solved already.

Official Statistics of July

In July industrial output, according to the data of the Federal State Statistics Service, reduced by 10.8% versus July 2008. This has been the best result since the beginning of 2009 (the worst – the reduction of 17.1% - was observed in May). Versus the previous month (June 2009) the output went up by 4.7%. According to the estimations of the Economic expert group¹ the growth against June after exclusion of calendar and seasonal factors made 1.5%. The experts' estimation for this limited number of figures of the official statistics can be divided in two groups. The first are optimistic ("The industry is reviving", "The second month in the row characterized definitely positively", "There are some positive signals", "The number of growing points is increasing"), the second are cautious ("it is too early for optimism", "The statistics of passenger cars production is alarming").

Demand for Industrial Goods

In August, according to the data of the survey among the enterprises conducted by the IET, the rates of the demand decrease went up (that is worsened) by 3 points after the improvement by 12 points in July. Thus, though the demand is still reducing and at the rates that are a bit higher than in July on the whole there is the sustention of the positive trend in the demand dynamics observed.

As a result the satisfaction with the volume of sales grew up. In August this figure finally left the trough (the surprisingly stable level of nearly all the months of the crisis), increasing by 3 points and reaching 28%. It is the foodstuff industry that is the leader in this respect, in which 52% of enterprises estimate the volumes of their sales as normal. The second place with the figure of 34% (the record-breaking figure for the months of crisis) is held by chemistry and petrochemistry. Non-ferrous metallurgy stepped back to the third place (32%). And the lowest satisfaction with the sales in August (8%) and on average over 10 months of the crisis (12%) is registered in the industry of construction materials. The situation in ferrous metallurgy is only slightly better (12% in August, 7% on average over the crisis).

After the drop in November the forecasts for the demand have been becoming better from month to month (if one removes the sudden changes in February and in April) by 2 points but are still negative upon exclusion of seasonality – the industry does not seriously count on the growth of the demand in September-October. Nevertheless in some branches of industry the expectations for the growth of sales in August reached 30% (timber and light industries) and even 40% (foodstuffs production) and obviously exceeded the expectations for its decrease.

Goods Output

1 <http://www.eeg.ru/>

The growth of the demand decrease rates by 3 points forced the industry to correct correspondingly the rates of output decrease: in August the production reduced 4 points more intensive than in July but less intensively than in all other crisis months. Thus, the positive shift in the dynamics of output in July was too good to be maintained in August.

The enterprises' production plans as well as the forecasts for the demand have been improved. It should be noted that the growth made 6 points at once, whereas since February they had been growing by 2 points once in two months. As a result they became definitely positive for the first time over all the months of the crisis. The plans for the increase of output are registered at 54% of enterprises in the foodstuffs production, at 41% of enterprises of ferrous metallurgy and at 36% of enterprises of the light industry.

In the 3rd quarter 2009 the load of facilities made 57% and remained practically unchanged as compared with the 2nd quarter (58%). A year ago this figure made 69% and the absolute maximum of 1993-2009 was equal to 74% and was registered in the 2nd quarter 2008.

Prices of Enterprises

The pricing policy of the enterprises could be described as the continuation of the previous months and testifies that the industry definitely has an intention to switch to the increase of prices. In August the real growth of prices was the most intensive since October 2008 for all the indices calculated. The prices grew most intensively in metallurgy, other branches of industry tried to switch to the stability of the prices from their decrease.

The plans for prices at enterprises went up by 6 points over the month and testify the second attempt to refuse from the deflation policy in the course of the current crisis. The first attempt (January-February) did not give any substantial results. The decrease of the prices was maintained only the industry of construction materials, and the most intensive growth is possible in ferrous metallurgy, foodstuffs production and chemistry industry.

Stocks of Finished Goods

The estimations of stocks of finished goods reacted quite adequately to the increase in the rates of the reduction of the demand. The balance of estimations worsened by 10 points over the month and returned to the normal level for crisis which was disturbed in July by too sudden changes in the dynamics of demand and output. The increase in the excessive stocks was characteristic for all the branches excluding foodstuffs production, where in the recent months there was a shortage of the stocks accumulations observed. The share of the estimations of normal estimations for the stocks has stabilized at the level of 57 since May which is quite acceptable for the period of crisis. Thus, the industry has solved the problem of stocks.

Redundancies: Real Dynamics and Plans

In August the scale of dismissals in the industry returned to the previous trend of slow attenuation. After the panic in January the balance of this index has changed by 1 point in a month, that is the intensity of the staff dismissals has been reducing slightly but steadily over each month of the crisis. The only exception was July which gave grounds for so many rosy hopes. In August the situation resumes its normal course. In August it was the machine-building industry (-32 b.p.), industry of construction materials (-23 b.p.), chemistry and petrochemistry (-21 b.p.) and even foodstuffs production (-14 b.p.) were characterized by the most intensive rates of dismissals.

There were no fundamental changes concerning the plans for dismissals in August. Over the last four months they stabilized in the range of -19...-24 balance points, which testifies steady and considerable desire of the enterprises to reduce the number of staff. In September-October the most numerous dismissals are possible in the industry of construction ma-

terials (balance of plans makes -47 b.p., which is a record-breaking figure for all the crisis), machine-building (-31 b.p., which is also a record) and chemistry industry (-18 b.p.).

Crediting of Industry

It seems that in August the Government managed to overcome the situation with the crediting of the real sector. The proportion of “normal” estimations for the availability of the credits went up by 11 points over the month and made 41%. The attitude of the banks to the metallurgy and timber industry has changed most considerably. Either that, or the enterprises reconsidered their attitude to their need in credits. In July only one fifth of the enterprises considered the shortage of credits as an obstacle for the growth of the production (sixth place out of 13 obstacles for the production).

However in August the growth of the availability on the whole throughout the industry was due only to the large-scale enterprises (more than 500 employees), 45% of which now consider the crediting conditions in banks as acceptable (32% in July). Normal attitude of the banks to small enterprises has not changes and remains at the level of 25%.

The ability of the enterprises to pay off the credits if there are any has not changed since July. The same as two months ago 60% of the producers consider themselves as able to serve their credits and 39% - as unable. The problems with the return of the credits are most likely in the light industry (the current level of the insolvency makes 69%), machine-building (63%) and the industry of construction materials (62%). ●

FOREIGN TRADE

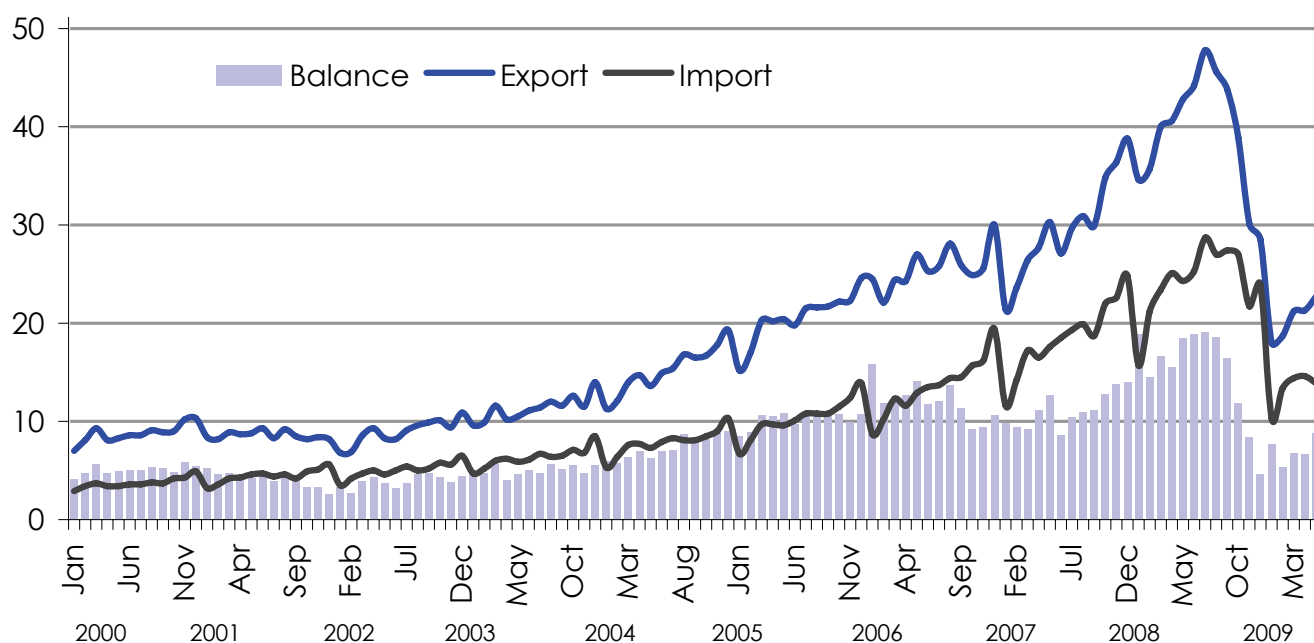
N.Volovik

In the first half of 2009 the main characteristics of the Russian foreign trade are formed in the environment of the considerable contraction of the external and internal demand and were characterized by negative dynamics. The foreign trade balance remains positive, although its volume has reduced by half – from USD 101.1 billion to USD 43.6 billion. The increase of the import duty rates allowed the domestic producers of passenger cars to increase their share in the total volume of sales of passenger cars up to 61% from 43% in January 2009.

In June 2009 the Russian foreign trade turnover calculated on the basis of the balance-of-payments methodology made USD 40 billion, which is by 42.3% lower than the corresponding figure of 2008. There were goods worth USD 24.5 billion supplied to export in June of the current year, which is by 44.1% lower than in June 2008. The value volume of import supplies made USD 15.5 billion, which is by 39.3% lower than the corresponding figure of the previous year (fig. 1).

The foreign trade balance made USD 9 billion in 2009, which is by nearly two times lower than the figure of the previous year.

Starting with the middle of February 2009 there evolved an upward trend in world prices for oil which is to a high extent connected with the expectations at the market for soon recovery of the world economy. The increase of the demand for the crude oil from oil processing factories in connection with the termination of the period of their spring servicing, increase in the demand for motor fuel with the coming of summer and considerable contraction of the reserves in floating storages are the factors that contributed to the growth of prices. The



Source: Central Bank of the Russian Federation

Fig. 1. Main Indices of Russian Foreign Trade (as USD billion)

decision of the OPEC adopted at the end of May on maintaining the volumes of sales at the previous level was of an additional support for the market.

In June 2009 the average price for oil grade Brent made USD 69.27 per barrel, having reduced by 51.4% versus June 2008. However versus May 2009 there was a growth of 18.1% observed.

As a result of monitoring from July 15 to August 14 the average price for oil grade Urals made USD 69.14 per barrel. In connection with the increased oil prices at the world market the export duty rates for oil was increased from USD 222 per ton to USD 238.6 per ton starting with September 1, 2009. The duty rate for light oil products went up by USD 12.8 up to USD 173.1 per ton, for dark oil products – by USD 5, up to USD 93.2 per ton.

Against the background of replenishing of stocks at the developed markets and the return of the investors to the market, the metals continue to increase in price. In June 2009 the average world prices for copper at London Metal Exchange went up by 55.7% since the beginning of the year, the prices for nickel – by 32.3%, for aluminum – by 11.4%. As compared with June 2008 the prices for aluminum went down by 46.8%, prices for copper – by 39.2%, prices for nickel by 33.7% (*table 1*).

Table 1

AVERAGE MONTHLY PRICES IN JUNE OF THE CORRESPONDING YEAR

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Oil (Brent), USD/barrel	13.83	15.99	29.41	27.14	24.66	27.06	35.2	53.9	68.3	70.13	135.2	65.74
Natural gas, USD/1 million BTU	2.159	2.358	4.245	3.704	3.254	5.891	6.409	7.12	8.99	7.62	12.8	3.914
Petroleum, USD/gallon	0.359	0.485	0.970	0.820	0.767	0.858	1.228	1.499	2.107	2.213	3.435	1.908
Copper, USD/ton	1665	1552.1	1752.0	1615.3	1686	1703	2669	3524	7198	7469	8263	5014
Aluminum, USD/ton	1316	1327.3	1510.2	1467.7	1355	1410	1676	1731	2477	2672	2957	1574
Nickel, USD/ton	4540	5241	8384.3	6629.2	7110	8761	13322	16160	20755	41407	22556	14960

Source: calculated on the basis of the data of London Metal Exchange (the UK, London), International Oil Exchange (London)

The world prices for most of foodstuffs and agriculture goods remain quite stable. The only exception is probably the increasing prices for beef, sugar and tea (*table 2*).

Table 2

DYNAMICS FOR AVERAGE WORLD PRICES FOR SOME AGRICULTURE GOODS

	2005	2006	2007	2008	2009					
					January	February	March	April	May	June
Wheat, USD/ton										
Canadian, WRS	197.6	216.8	300.4	454.6	340.2	318.5	306.9	315.4	334.6	326.6
American, HRW	152.4	192.0	255.2	326.0	239.1	224.7	230.9	234.2	262.3	255.1
American, SRW	135.7	159.0	238.6	271.5	195.1	183.4	183.7	182.6	202.5	201.7
American corn, USD/ton	98.7	122.9	163.0	223.1	172.8	163.4	164.6	168.5	179.9	179.5
Barley, USD/ton	95.0	117.0	172.0	200.5	121.4	112.5	114.8	111.3	128.7	148.5
Soybeans, USD/kg	274.4	268.4	384.0	523.0	413.0	390.0	379.0	414.0	465.0	502.0
Soy oil, USD/ton	545.1	598.6	881.0	1258	789.0	748.0	727.0	801.0	892.0	885.0
Thai rice, USD/ton		304.9	326.4	650.1	580.0	590.8	588.3	549.7	533.0	572.0

Source: World Bank.

In the forecast of the International Grain Council it is mentioned that the world market for wheat remains balanced and the expectations for the decrease of the crop due to unfavorable weather conditions proved to be wrong. It should be noted that the forecast for the production of wheat remained unchanged at the level of 652 million of tons.

In June the price for the wheat (American No 2) remained practically unchanged and was equal to USD 202 per ton. The price of corn also remained unchanged at the level of USD 180 per ton. In June the price for Thai rice went up by 7.3% - up to USD 572 per ton, which is USD 3 higher than in May. The prices for vegetable oils went down. Thus, palm oil (Malaysian), peanut oil and soybean oil (Holland) became 8.9%, 0.5% and 0.8% cheaper, correspondingly.

By June prices for beef had been observed to increase for the fourth month in a row. In June its price went up by 2.1% more – up to Cents 269.2 per kilo. At the same time the prices for poultry reached Cents 194.2 per kilo, which is only 0.7 cent per kilo lower than the maximum level registered in August of the previous year.

Prices for sugar reached record-breaking level: when the bids were opened on August 4 there was USD 505.9 offered per ton in London. Never before since the quotations at LIFFE started have prices for sugar reached such high figures. The direct reason for this was the drought that damaged the crops in India, Thailand and Mexico. The demand for sugar is additionally stimulated by the reports from Brazil, which is its largest producer. Due to heavy and incessant rains the government of Brazil has reconsidered the scales of forthcoming crop of sugar towards its decrease.

The prices for tea have also reached the historical maximum. The record was observed on August 27, when the price for 1 kilo of the best breed of tea known as BP1 reached USD 3.97. Never before has tea been so expensive. The world prices for tea are currently established as a result of biddings at the largest tea exchange in the Kenyan port, Mombasa. The reason for the growth of prices is the continuing drought in the leading tea producing countries: Kenya, India and Sri-Lanka. As a result the volumes of export from them dropped in the first half of the current year by 10%. At the same time the world demand for tea has increased.

The drop of prices for the goods exported from Russia and the growth of prices for imported goods at the world markets resulted to a considerable worsening of the conditions for trade of the Russian Federation with other countries.

Russia's foreign trade turnover in the 1st half year of 2009, according to the data of the bank of Russia, made USD 208.3 billion, having decreased by 44.1% versus the first half of 2008. Export made USD 126 billion (the decrease of 46.8%), import – USD 82.3 billion (decrease by 39.3%). The foreign trade balanced remained positive of USD 43.6 billion (USD 101.1 billion in the 1st half of 2008).

The reduction of the external demand and the drop of prices at the world goods markets affected the dynamics of the Russian export. In the 1st half of 2009 export to the countries of the European Union has decreased most significantly – by half (export to Germany has reduced by 2.4 third, to Italy and the Netherlands – by 2 times). Export to the main countries of Asia-Pacific Economic Cooperation – China, the USA, Japan - has reduced by more than one third regions. As to the CIS countries, it is the export to the Ukraine that has reduced most considerably – nearly by two thirds.

It was the fall of prices that contributed most to the reduction of export. The physical volumes of goods export have also reduced. In the 1st half of 2009 as compared with the 1st half of 2008 the volumes of supplies of the Russian natural gas to the external market reduced by 1.8 times, of production of timber and timber processing industries, chemistry production, mineral fertilizers and ferrous metals – by approximately 20-25%, export of oil went up by 0.2% and the supplies of oil products increased by 5.8%.

Export of foodstuffs demonstrated a spectacular growth – by 65.3% in terms of value due to the increase of the physical volumes of export of wheat and wheat and rye mix by 6.4 times, the average contract prices decreasing by 47.8%. It should be noted however that the proportion of foodstuffs in the total volume of the Russian export makes only 3.7%.

Over the 1st half of 2009 the rates for the decrease of goods import have accelerated. The reduction of import was connected with a considerable drop of physical volumes of import of goods to the country. In the 1st half of 2009 as compared with the 1st half of 2008 the index of physical volume reduced by 56.3% whereas the index of average prices made 96.7%.

Import of goods of investment purposes reduced more considerably than the consumers' import. The rates of reduction of the export of the production of machine-building industry accelerated in the 2nd quarter 2009 and as a result of the 1st half of 2009 its import reduced by 2.2 times. The rates of reduction of export of the production of chemistry industry and the productions connected with it somewhat increased in the 2nd quarter 2009, as for foodstuffs production and agriculture raw materials for their production – the rates were nearly the same as in the 1st quarter 2009. Import of this group of goods reduced, correspondingly, by 1.4 and 1.2 times in the 1st half of 2009.

In September the effect of the decree of the Government of the Russian Federation on the increase of customs duties for the used cars of foreign models expires. Import duty rates for the used cars of foreign models were introduced in January 2009 for the period of 9 months. Now the passenger cars of 3-5 years old are levied with the duty of 35% of the customs value and the cars older than 5 years – with 100% of the customs value.

Even if the increase of duty rates has not saved the Russian automobile industry, it has not allowed it to fall even lower. According to the data of the Ministry for Industry and Trade, in January 2009 import of all new cars of foreign models made 31.2 thousand, and the volume of the cars assembled in Russia – 18.2 thousand. In June the situation was quite different – there were 37.2 thousand of new cars imported to Russia and there were 58.8 thousand of cars produced in Russia. It should be noted that import of the used cars reduced to the minimum level of only 8 thousand of cars. If one takes into account that over all 2008 there were 300 thousand of used cars imported to Russia, this segment of the market ceased to exist.

At the meeting of the committee of the Government of the Russian Federation on protection measures in foreign trade and customs and tariffs policy the suggestion to prolong the existing regime of import of some kinds of motor vehicles on a temporary basis (for another 9 months) was considered to be well-grounded. ●

FEDERAL BUDGET

I.Sokolov, E.Fomina

In the background of relative stabilization of the world economy there has been some improvement in the basic macroeconomic indicators of the domestic economy in the late second and early third quarter of this year. At the same time, the RF public finance sector is still facing difficulties in retaining the positive balance of the budget system. The key incentive in the growing imbalance of the budget system are the funding of the Russian Government anti-crisis program in June and August this year, whereas within 7 months of 2009 a significant reduction of resources, distributed through the budget system was considerably reduced.

Review of basic indicators of the extended government budget execution with- in January-June 2009.

Taking into account the current needs of social support, as well as implementation of large-scale support to the real sector of economy, the key element of the national financial stability is the amount of resources, distributed through the budget system (see Table 1). As of 6 months of 2009 results, the volume of extended government budget revenues is reduced by 5.8 percentage points of GDP versus the relevant period of 2008, whereas the expenditures, by contrast, increased by 8 percentage points of GDP. As per tentative assessments, over 6 months of the current year, the budget deficit of the extended government was recorded in the amount of 3.2 per cent of GDP, whereas in the first half of 2008 the extended government budget was executed with a surplus, exceeding 10 per cent of GDP. It should be noted, that the growth of the budget deficit of the extended government for the first six months of this year as compared with its volume in January-May was more than 2 percentage points of GDP. In the second half of 2009 one should expect further imbalance in the budget of extended government.

Table 1
BASIC INDICATORS OF THE RF FEDERAL BUDGET EXECUTION AT ALL LEVELS IN 2008 – 2009
(% OF GDP)

	2009		2008		Imbalance, p.p. of GDP
	RUR, Bln	% of GDP	RUR, Bln	% of GDP	
Федеральный бюджет					
Revenues	3172,2	17,7	4370,7	22,9	-5,2
Expenditures	3893,8	21,7	2995,6	15,7	+6,0
Deficit (-)/ Surplus (+)	-721,7	-4,0	1375,1	7,2	-11,2
Consolidated budgets of the RF Subjects					
Revenues	2711,3	15,1	2880,8	15,1	0
Expenditures	2611,7	14,6	2407,5	12,6	+2,0
Deficit (-)/ Surplus (+)	99,6	0,6	473,3	2,5	-1,9
Extended government budget					
Revenues	6042,7	33,7	7543,7	39,5	-5,8
Expenditures	6619,7	36,9	5515,5	28,9	+8,0
Deficit (-)/ Surplus (+)	-577,0	-3,2	2028,1	10,6	-13,8
For reference: GDP, RUR, bln.	17927,8		19112,8		

Source: RF Ministry of finance, IET estimates.

In the first half of this year the global financial crisis and the weakening of the Russian economy as in general continued to provide an extremely adverse impact on the volume of the expanded government budget resources. Moreover, the strong dependence of the budget revenues from export prices of the Russian is sustained. Due to a significant reduction in the prices for primary energy resources in the global markets, in view of the reducing demand for oil and gas production from the importing countries, revenues from tax on extraction of mineral resources and income from foreign trade have been significantly reduced. Income from those taxes to the budget of enlarged government fell down by 2.2 percentage points of GDP and 3.5 percentage points GDP, respectively, as compared with the relevant period of 2008.

Herewith, it should be noted that in the first half of this year the contracts, concluded in late 2008 - early 2009, the peak of the crisis, at low prices, were subject to the execution. However, from the second quarter of 2009 the dynamics of energy prices started to improve, so the statistics of severance tax revenues from foreign economic activity in the July-August 2009 will be more optimistic (See Table 2). Moreover, following the improved pricing environment, the rates of export duty on crude oil have been increased. Thus, while in January - June 2009 the export duty fee was within 100-153 dollars per ton of crude oil, in July-August that rate was increased to 222 dollars per tonne. This measure, according to our estimates, would increase revenues from foreign economic activity, but not be able to reverse the trend of reduction of tax revenues to the budget system of the country, as compared with 2008.

In addition to energy sources price fluctuations in the world markets, the level of oil and gas revenues in the first half of 2009 had some impact in the administration of tax on extraction of mineral resources:

- the exempted rate of the severance tax is increased from USD; 9 to 15;
- since 2009 the amount of oil produced for tax purposes is estimated in terms of net weight;
- the list of sites, to which the zero severance tax rate is applied is increased;
- the procedure of cancellation of licenses for subsoil usage for all oil companies is changed.

The revenue reduction in oil and gas sector has provided an impact on reducing corporate income tax of organizations. Despite some stabilization of the enterprises of some economic sectors, the overall financial state of the Russian enterprises remains difficult because of the reduced investment activity and reduction of income from business activities. Within January-June 2009, revenues from corporate income tax of organizations to the budget of extended government amounted to 3.5 per cent of GDP against 6.5 per cent of GDP in January-June 2008 (See Table 2).

Significant reduction in corporate income tax happened due to further increase in the proportion of unprofitable organizations in the economy and reduction of the net financial performance of enterprises and organizations. Thus, within 6 months of 2009 the financial result of the real sector was in the amount of RUR 1,634 trillion, which is nearly 2 times lower than in the relevant period of 2008, whereas the share of unprofitable organizations in the total number of organizations in comparison with the corresponding period of previous year increased by 6 percentage points and amounted to about 35.5 per cent.

The amendments and supplements to the Chapter 25 of the Tax Code, came into effect since the beginning of 2009, continued to influence the narrowing of the tax base in terms of administration of the organizations corporate income tax and enhancement of taxpayers position, among which the greatest effect was provided by an increased depreciation refund (accounting a part of the original value of fixed assets as expenses in the current tax period) from 10 per cent to 30 per cent. Moreover, in 2009, the tax rate on corporate income has been reduced by 4 p.p. (previously 24 per cent). However, in the face of declining profits of

enterprises of real economic sector, this measure, designed to encourage the growth and expansion of companies, had a rather insignificant effect.

Against the background of significant reduction of corporate income tax and severance tax revenue, the budget revenue from VAT in January-June 2009 has demonstrated a significant increase in relative terms: the growth of this tax revenue to the budget of extended government reached 0.4 percentage points of GDP versus the revenue of January-June 2008 (Table 2). At the same time, in absolute terms, VAT receipts to the budget have grown insignificantly - about RUR 7 billion. When comparing the dynamics of VAT proceeds in 2008-2009, it should be taken into account, that VAT revenue base for the 6 months of 2008 and for the first half of 2009 are not comparable, because the VAT for the second quarter of 2008 was to be transferred in July and was not included in the statistics of budget execution for 6 months, while VAT revenues were included in the budget for the first half of 2009, including tax payments for transactions of the second quarter of this year. Further reasons that hindered the growth of VAT revenues in the budget, were measures aimed at improving the assessment and administration of this tax, among them: the abolition of duty to pay VAT in cash for non-cash settlements; VAT exemption on technological equipment, granting the right to deduct VAT on advance payments.

According to tentative assessments, the growth of income tax of individuals, recorded in the first months of this year, was sustained in the first half of 2009. The volume of personal income tax revenue in the budget of the extended government reached 4.1 per cent of GDP, which is 0.3 p.p. of GDP higher than the values of the relevant period of the last year (Table 2). The current dynamics of personal income tax revenue is based on faster GDP decline as compared with the dynamics of changes in disposable income. Thus, according to tentative estimates, real disposable monetary incomes (revenues less obligatory payments, adjusted for consumer price index) for 7 months of 2009 compared with the relevant period in 2008 decreased by 0.9 per cent, while the GDP volume over the same period demonstrates the decline by about 10 per cent against the corresponding period of 2008.

However, in 2009, a number of benefits have been entered into force on reduction personal income tax base: the amount of the deduction for the child is increased to RUR 1000 and the amount of income for the year is increased (up to RUR 280,000), below which such a deduction is available, derived from the taxation of the amount of education fees of employees and workers compensation costs paid on loans for housing facilities acquisition and construction. Expected in 2009 accelerated downfall of the level of personal income, together with those benefits should lead to the decline of the personal income tax base reduction.

Table 2

DYNAMICS OF TAX BURDEN AND REVENUES FROM BASIC TAXES TO THE BUDGET OF EXTENDED GOVERNMENT BUDGET IN JANUARY-JUNE 2008–2009, % IN GDP

	2009	2008	Deviation, p.p. I GDP
Tax burden (1+2+3)	32,8	39,6	-6,8
Tax revenues (1), among them:	24,2	27,8	-3,6
Corporate income tax	3,5	6,5	-3,0
Individual income tax	4,1	3,8	+0,3
Unified social tax*	2,2	2,1	+0,1
VAT	5,3	4,9	+0,4
Excise tax	0,9	0,9	0,0
Royalty	2,3	4,5	-2,2
Mandatory pension insurance (2)	3,4	3,1	+0,3

* regardless mandatory pension insurance.

Source: RF Ministry of finance, Russian Statistics Agency, IET estimates.

With the reduction of revenues within January-June of the current year, a rather restrained budget spending, observed in the first months of 2009 was replaced by active spending in June-August 2009. A massive and uneven budget spending can result in extended budget deficit and an accelerated rise in prices, whereas in January-May 2009 it was managed to keep it within the limits of 7 per cent (January-May 2008 – 8 per cent), including measures on restriction the budget expenditures.

Enlarged government budget expenditures within January-June 2009 amounted to 36.9 per cent of GDP against 28.8 per cent of GDP in 2008 (Table 3).

Table 3

EXTENDED GOVERNMENT BUDGET EXPENDITURES WITHIN JANUARY–JUNE 2009, % IN GDP

	January–June 2009		January–June 2008		Deviation, p.p. in GDP
	млрд руб.	в % ВВП	млрд руб.	в % ВВП	
Total budget expenditures	6619,7	36,9	5515,5	28,8	+8,1
Among them					
Federal issues	567,8	3,2	550,3	2,9	+0,3
Including expenditures associated with the servicing of federal and municipal debt	112,4	0,6	91,4	0,5	+0,1
National defense	527,3	2,9	417,9	2,2	+0,7
National defense and law enforcement	546,3	3,1	465,0	2,4	+0,6
National Economy	1034,5	5,8	694,0	3,6	+2,2
Housing and public utilities	329,2	1,8	318,4	1,7	+0,1
Environmental protection	11,6	0,1	10,4	0,05	+0,05
Education	817,1	4,6	723,7	3,8	+0,8
Culture, cinematography and mass media	132,1	0,7	121,4	0,6	+0,1
Health care and sports	680,1	3,8	623,6	3,3	+0,5
Social policy	1973,5	11,0	1590,7	8,3	+2,7

Source: Report on consolidated budget execution in January-June 2008–2009. RF Treasury, IET estimates.

The significant growth in funding was observed under «National Economy» budget line: 5.8 per cent of GDP in 2009 against 3.6 per cent of GDP in 2008. A record peak for the first half of this year was reached in funding for «Social Policy» - about 11 per cent of GDP against 8.3 per cent of GDP in 2008, significantly increased the volume of public funds annually is noted in financing of «National Defense», «National Security and Law Enforcement». Government liabilities under those purposes for 6 months of 2009 were performed in the amount of 6.0 per cent of GDP, which is 1.4 percentage points higher than the relevant indicator of 2008.

RF federal budget execution within January-July 2009

According to the information of the RF Ministry of Finance, federal budget revenues in 7 months of 2009 amounted to 17.8 per cent of GDP, which is 7.4 percentage points of GDP below the indicator of 2008, while expenditures exceeded the level of the last year to 6.3 percentage points of GDP and reached the level of 22.1 per cent of GDP.

A significant growth in expenditures over the period under review of the current year against the same period of 2008 is based on the large-scale financing of a wide range of anti-crisis measures to support the real sector of economy, accelerated indexation of social benefits, planned for execution in 2009, as well as significantly lower nominal volume of GDP in the current year. The indexation of pension payments is scheduled for the current year in four stages. The first stage of indexation in this year was held on March 1 - the basic

share of labor pension was increased by 8.7 per cent. From April 1 2009 the labor old-age pension is increased by 17.5 per cent. From August 1, the average size of the labor pension share has been increased by RUR 221 and amounted to RUR 5536. Herewith, the average level of the labor retirement pension has increased by RUR 236 to RUR 5855, a disability pension - by RUR 130 to 4048 rubles, pension for the loss of breadwinner - to RUR 161 to RUR 3323. Significant additional indexation is scheduled for December 1, 2009, when the base share of the labor pension will be increased by 31.4 per cent. In addition to pensions, an increase in other social payments include: salaries of public officers has been increased by 30 per cent from January 1, the maximum unemployment benefit has been increased 1.5-fold, up to RUR 4900. Allowance to military personnel from August 1, has been indexed by 8.5 per cent.

Irregular execution of the federal budget expenditures, observed over the last few years, against the background of the urgent need to support sectors of the economy in in 2009, can provide a disastrous effect on economic dynamics. Thus, over the first six months of the year there were spent only 40 per cent of the federal budget, whereas almost 10 per cent of them were supposed to be spent in June of the current year.

The reduction of the federal budget revenues in January-July 2009 both, in absolute and relative terms as compared with the relevant period of the last year occurred under the impact of both, external and internal factors. On the one hand, it was influenced by the decreasing share of oil and gas sector indicators, while revenues from the severance tax revenues and from foreign economic activity have declined; on the other hand, the impact of the global financial crisis had a negative impact on Russian economy and, consequently, led to a decrease in non-oil revenues of the federal budget.

Table 4

BASIC INDICATORS OF THE RF FEDERAL BUDGET IN JANUARY-JULY 2009

	January-July 2009		January-July 2008		% versus budget estimates	Отклонение	
	RUR bln	RUR bln	млрд руб.	% in GDP		RUR bln	p.p. of GDP
Revenues, including:	3801,2	17,8	5677,4	25,2	56,6	1876,2	-7,4
Oil and gas	1325,8	6,2	2562,8	11,4	64,4	1237,0	-5,2
Contributions to the Reserve Fund and National Welfare Fund (Stabilization Fund)	4,1	0,02	456,4	2,0	-	452,3	-1,9
Revenues, including:	4725,0	22,1	3557,9	15,8	48,3	1167,1	+6,3
Interest expenditures	102,9	0,5	87,7	0,4	43,8	15,2	+0,1
Noninterest expenditures	4622,0	21,6	3509,1	15,6	48,4	1112,9	+6,0
Deficit / Surplus of the federal budget	- 923,8	- 4,3	2119,5	9,4	31,0	-1195,7	-13,7
Non-oil deficit	-2249,6	-10,5	-443,3	-2,0%	44,7	-1806,3	-8,5
GDP estimates	21374,8		22537,0				

Source: RF Ministry of Finance (tentative estimates), IET estimates.

According to the tentative estimates of the federal budget for 6 months of 2009, the budget was executed with a deficit amounting to 4.3 per cent of GDP, with the amount of non-oil deficit of more than 10 per cent of GDP. Thus, in the situation of increasing the budget deficit in the second half of this year, there is a high probability that the federal budget deficit will exceed 7,4 per cent of GDP. Currently, the federal budget deficit is covered from the Reserve Fund: for half a year the Fund assets were addressed for the purposes of balancing the

federal budget, as well as to ensure oil and gas transfers, totaling nearly to RUR 1.8 trillion. As of July 1, the Reserve Fund assets amounted to nearly RUR 2.8 trillion.

Table 5 shows the dynamics of revenues and expenditures of oil and gas assets within January-July 2009. The total revenue for 7 months of 2009 to the Reserve Fund and National Welfare Fund amounted to RUR 490 billion. (2.7 per cent of GDP). Herewith, the volume of oil and gas transfers to the federal budget within 7 months of the current year amounted to RUR 1.749 trillion (8 per cent of GDP).

Table 5

DYNAMICS OF FEDERAL BUDGET OIL AND GAS REVENUE AND EXPENDITURE WITHIN
JANUARY-JULY 2009, RUR BLN

Indicator	Balance as of 2008	Estimated for 2009 budget	Revenue within January-July 2009	Использовано за январь-июль 2009 г.		Balance as of late July 2009
				Support of the federal budget balance	Support to oil and gas transfer	
Oil and gas revenue of the federal budget	x	2 057,2	1297,1			x
Areas of oil and gas revenues expenditure:	x	x				x
• Oil and gas transfers	x	2 531,1	1476,5			
• Reserve Fund	4 027,6	5 147,5	-	1615,6	179,4	2 811,3
• National Welfare Fund	2 584,5	x	4,1	-	-	2 858,7
Total	6612,1	x	1480,6	1615,6	179,4	5670,0

Source: Federal Treasury

In 2009 part of the budget deficit is expected to be replenished through domestic borrowings. The Ministry of Finance has allocated RUR 115 billion out of planned for the year RUR 530 billion in January – June.

The possibility of some increase of external public debt is considered to mitigate the dynamics of the rapid reduction of the accumulated assets of Reserve Fund.

Table. 6 shows the dynamics of the federal budget expenditures for 6 months of the current year, according to the break-down of budget expenditure lines. The majority of federal budget lines expenditures is carried out at lower rates in the last years, resulting in overall federal expenditures for the first half filled at a rate of about 40 per cent of the estimated budget against their execution by more than 43 per cent in the relevant period of the last year. Thus, the greatest gap in the the federal budget execution in the 6 months of the current year as compared with the relevant period of 2008 occurred under «Social policy» and «Intergovernmental transfers» budget lines. An exception is the budget execution under «National defense» lines The dynamics of those expenditures has exceeded the level of the last year by 1.1 p.p. Under such dynamics in the first half of 2009, it is clear that in the second half of this year expenditures will exceed the greater share of expenditures planned for the year, which can provoke a surge of inflation, an excessive pressure on the ruble and the fall thereof.

Table 6

CASH EXECUTION OF THE FEDERAL BUDGET WITHIN JANUARY-JUNE 2009 Г.
(% VERSUS BUDGET ESTIMATES FOR THE YEAR)

	January-June 2009	January-June 2008
Total Budget Expenditures	39,8	43,4
Including		
Federal issues	34,7	40,8

окончание Таблицы 6

	January-June 2009	January-June 2008
Including expenditures associated with the servicing of federal and municipal debt	36,8	39,9
National defense	43,3	42,2
National defense and law enforcement	43,3	44,3
National Economy	39,4	39,5
Housing and public utilities	23,3	24,4
Environmental protection	36,9	38,3
Education	39,9	40,1
Culture, cinematography and mass media	38,1	40,5
Health care and sports	32,5	39,8
Social policy	39,4	47,7
Interbudgetary transfers	40,7	46,6

Source: RF Ministry of Finance, IET estimates.

Despite the positive dynamics of some macroeconomic indicators, emerging in July and August of the current year, the overall state of the domestic economy can be regarded as unstable. On the way out of the economy from recession, in our opinion, it is extremely important to pursue a consistent and adequate policy, including a moderate build-up of public expenditure commitments. Otherwise, the commitments in the future may become a heavy burden to the national financial system. ●

MARKET OF MORTGAGES IN THE RUSSIAN FEDERATION

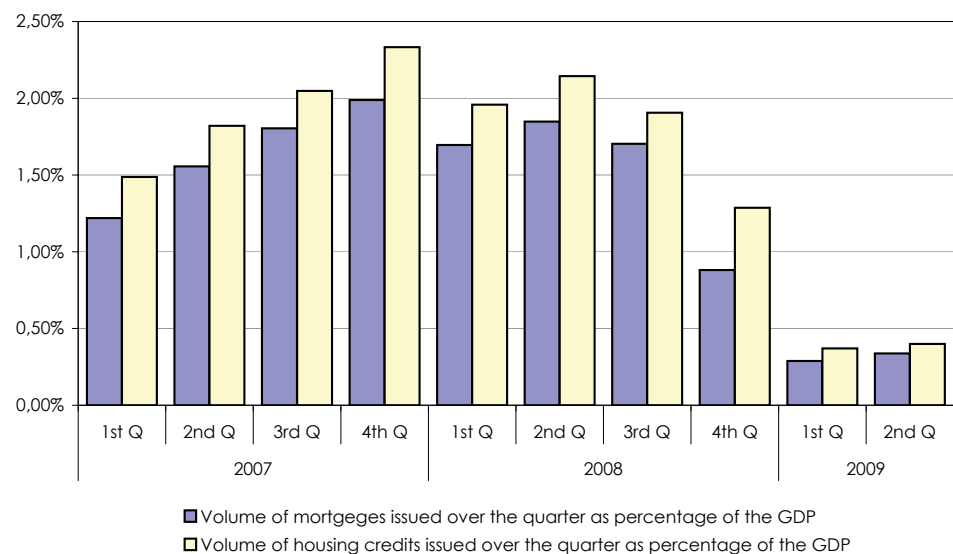
G.Zadonsky

The indices of housing credits in the 2nd quarter 2009 demonstrated some stability. In August open joint-stock company Agency for Home Mortgage Lending (AHML) reduced the rates for mortgage credits down to 10.8% and retains the volumes of refinancing that are near the pre-crisis level. Urals, Central and Privolzhsky federal okrugs are the leaders of the volumes of mortgage debt per capita of the population.

According to the data of the Central Bank of the Russian Federation, in the 1st half of 2009 there were 60894 housing loans issued of the sum of RUR 67.9 billion, out of which 44009 credits of the sum of RUR 55.25 billion were mortgage credits. As compared with the 1st half of 2008, the volume of issued mortgages reduced by 6.14 times, and the volume of the housing loans on the whole – by 5.78 times (fig. 1). The GDP of Russia over the 2nd quarter increased by 7.5% as compared with the 1st quarter 2009. The volume of the housing crediting has also somewhat grown in the 2nd quarter, also compared with the growth of the GDP.

In the 2nd quarter the trend for the decrease of the outstanding debt both for the housing loans and for mortgages that evolved in the 1st quarter persisted. According to the data of the Central Bank of the Russian federation, as on July 1, 2009 the outstanding debt for the housing loans made RUR 1195.0 billion, and for mortgages - RUR 1010.2 billion. According to the Central bank of the Russian Federation, as on 01.07.2009, the all-Russian level of the mortgage debt per capita of the population made RUR 7119 per person. The highest figure of this index was registered in Urals, Central and North-Western federal okrugs (RUR 11 354 per person, RUR 8732 per person and RUR 8630 per person, correspondingly). In terms of value, the central, Privolzhsky and Siberian federal okrugs are leaders of credit issuing.

Starting with August 10, 2009 the Bank of Russia lowered the refinancing rate down to 10.75%. In this connection open joint-stock company Agency for Home Mortgage Lending (AHML) reduced the basic interest rate for refinancing of standard mortgages from 11.05% to 10.8% per annum in rubles and practically returned the value of the rate to the pre-crisis level of 2007.



Source: according to the data of the Federal State Statistics Service and the Bank of Russia

Fig. 1. Dynamics of Housing Crediting (as percentage of the quarterly GDP)

The threshold value of the rate now makes from 10.805 to 12.76% when there is private insurance and from 11.50% to 13.46% if there is no insurance.

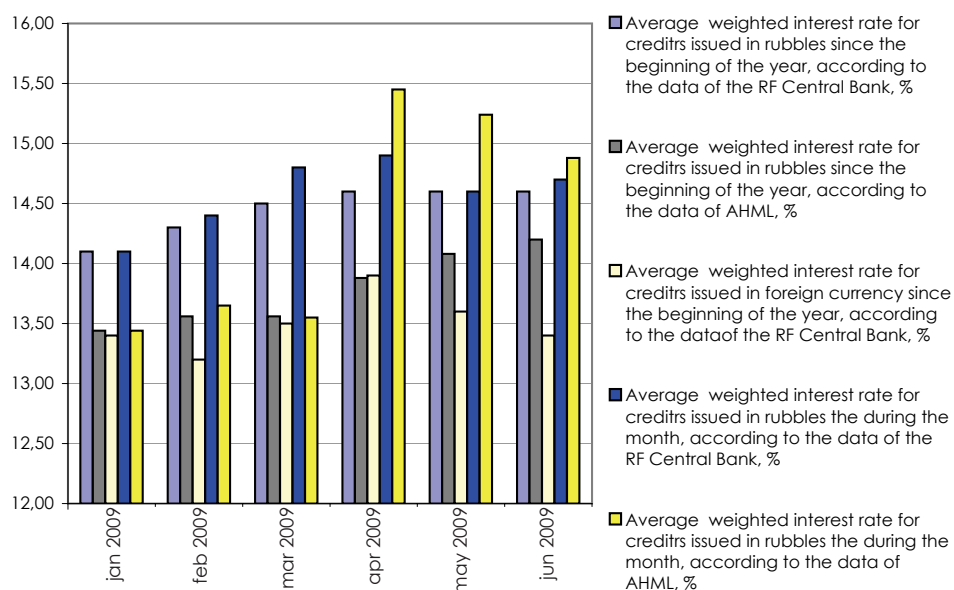
According to the data of the Central Bank of the Russian Federation, the average weighted interest rate for the mortgages in rubles issued exceed systematically from the beginning of the year the same rates for the credits refinanced by AHML. However whereas in the 1st quarter the average weighted interest rates for credits in rubles issued during the month, according to the data of the Central Bank of the Russian Federation, were also higher than the corresponding rates for the credits refinanced by AHML, in the 2nd quarter the situation was quite opposite. In April average weighted interest rate of AHML of 15.45% over the month exceeded the rate of AHML in March by 1.9 percentage points and the average rate for April (according to the data of the Central Bank of the Russian Federation) – by 0.55%. In May and June the average weighted interest rates over the month for the credits refinanced by AHML reduced in value, but, the same as in April, exceeded the March rate of AHML and the corresponding rates, according to the data of the Central Bank of the Russian Federation (fig. 2).

According to the data of Kreditmart the average market rate of mortgage credits increased versus June 2009 and made 20.32% for credits in rubles and 15.795 for credits in US dollars. The rates for mortgage products with floating rate reduced and made 19.75% for mortgages in rubles and 9.86% for mortgages in US dollars.

The proportion of mortgages in the volume of housing credits in the 2nd quarter 2009 increased and was equal to 81.37% as on July 1 (77.76% on April 1).

Average weighted crediting period for the mortgages in rubles has somewhat decreased as compared with the previous month, according to the data of the Central Bank of the Russian Federation, and made for credits issued since the beginning of the year 16.53 years, and for credits issued during the month – 15.77 years. On the contrary, the average weighted period of crediting for mortgages issued in foreign currency since the beginning of the year has increased, according to the data of the RF Central Bank, as on July 1, 2009 versus June 1, 2009 and made 10.59 years. Average weighted periods for housing loans demonstrate the similar trend and have close values.

The proportion of mortgages in foreign currency in the outstanding debt continued to



Source: on the basis of the data of the Central Bank of the Russian Federation and AHML

Fig. 2. Average Weighted Interest rates for Mortgages Issued in 2009

decrease and by 1 July made 21.9% (19.8% for housing loans). In the volume of the mortgages issued from the beginning of 2009 the proportion of the foreign currency in the 2nd quarter is varied around 6% - the same as for housing loans.

According to the data of Kreditmart, in the 2nd quarter 2009 the total number of 17 banks offered mortgages for purchase of housing at the secondary market. In July purposeful credits under security

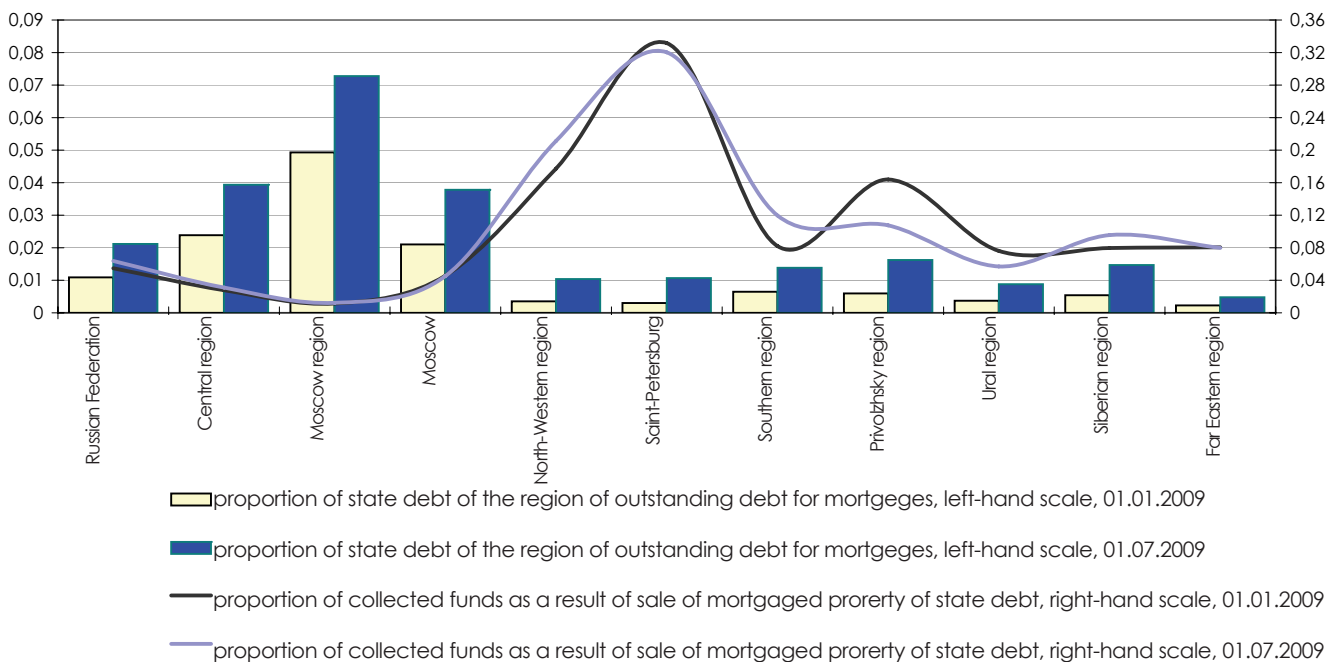
of the existing object of immovable property and credits for the purchase of a house with a land plot at the secondary market was offered by 10 banks.

According to the publication of the Central bank of the Russian Federation “Some indices characterizing the loaners in different regions of the Russian Federation” the volume of the funds collected from the borrowers as result of sale of the mortgaged property as on January 1, 2009 was equal to RUR 629.7 million, which makes 5.48% of the outstanding debt. As on July 1, 2009 the volume of the collected funds increased by RUR 737.2 million. The total volume of the funds collected as a result of the sale of the mortgaged property made 6.38% of outstanding debt as on July, 1st. The graph (fig. 3) demonstrates, that the volumes of collection of outstanding debt are increasing, with the exception of Privolzhsky and Urals federal okrugs, where the decrease in the volumes of collection is occurring.

The stale debt for mortgages increased over the 1st half of 2009: up to 1.46% of the outstanding debt for credits in rubles and up to 4.45% - for credits in foreign currency, whereas in the 1st half of 2008 it was equal to 0.29% of the outstanding debt in rubles and 0.38% of the outstanding debt in foreign currency

As on August 1, 2009 the open joint-stock company Agency for Home Mortgage Lending refinanced 13575 credits worth RUR 14.6 billion. Over the corresponding period of 2008 AHML refinance 16448 credits worth RUR 15.4 billion. The resulting figure of the volume of refinancing by August made RUR 119.92 billion. The proportion of the mortgages refinance by AHML in the total number of issued mortgages continues to increase. In April 2009 the proportion of AHML in the value volume of issued mortgages made 16.5%, and in physical volume – 17.4%, and by 01.07.09 it increased up to 16.9% and 19%, correspondingly.

According to the data of the Central Bank of the Russian Federation, the debt for the right of claims for mortgages purchased by organizations made RUR 100.89 billion as on July 1, 2009. According to the quarterly report of AHML, the arrears of credits that are serviced by the agency increased from 11.1% to 12.5% over the 2nd quarter 2009. The proportion of credits with arrears of payments of more than 180 days went up to 7% of



Source: according to the data of the Central Bank of the Russian Federation.

Fig. 3. Regional Dynamics of Outstanding Debt of Mortgages and Volumes of Collection of Funds from Borrowers as a result of Sale of Mortgaged Property

the AHML credit portfolio. The credits with such debt will most probably be repaid by the sale of mortgages. In case the prices for housing falls by 30%, 42.3% of AHML credits will partially be, according to the estimations of experts, unsecured with mortgages.

Federal Financial Markets Service registered mortgage bonds of the closed joint-stock company Mortgage Agency of the Moscow Bank for Reconstruction and Development of the total nominal value of RUR 2.216 billion. The bonds liabilities will be secured with the guarantee of AHML within the framework of agreement between it and the Moscow Bank for Reconstruction and Development. Absolut Bank is also planning to issue mortgage securities with the guarantee of AHML.

The President of Russia commissioned the Government with the participation of the Central Bank to elaborate a long-term strategy for the development of the mortgage crediting in Russia by December 20. They are also commissioned to prepare and approve the complex of measures for the development of mortgage crediting in Russia for the period of up to 2011, that are aimed at the “increase of mortgage accessibility for citizens by the development of mortgage crediting, formation of special mortgage programs for construction and purchase of the housing of economic class, stimulation of the purchase of housing constructed within the frameworks of projects of complex development of territories by the citizens”, as well as at “the reduction of the period for charging orders for mortgages property” up to October, 1.

At the beginning of August the Government of the Russian Federation submitted to the State Duma the amendments to the laws “On state registration of rights for immovable property and deals with it” and “On mortgages (the mortgage of immovable property)” aimed at the reduction for the period of registration of mortgages of land plots, buildings and constructions.

The Ministry for Economic Development prepared a bill “On collector activity” that describe in detail the activity of collectors, their rights and duties, the group of deputies submitted for the consideration of the State Duma the amendments to the law “On mortgages (mortgage of immovable property)” concerning the procedure for sale of property pledged in accordance with mortgage agreement. ●

INVESTING RETIREMENT SAVINGS IN THE SYSTEM OF MANDATORY PENSION INSURANCE IN THE FIRST QUARTER OF 2009

L.Mikhailov, L.Sycheva

As per the first quarter of 2009 results, the value of the assets in the mandatory accumulative pension system (regardless the funds of insurance contributions to the consolidated Russian Pension Fund (RPF) regression, started in the fall of preceding year has continued. The share of the state management company (SMC) in the total assets of the accumulative mandatory pension system has decreased from 88.5 per cent to 85.3 per cent within the year quarter. RPF share has increased by 9.2 to 12.3 per cent over the same term. The main reason is the transition of the insured persons from the RPF to the accumulative pension system (APS). According to the results of the first quarter of 2009, the yield on pension savings, invested in SMC was deficient (-7.2 per cent). However, over the 3-year term the yield on pension savings invested by SMC, remained positive and amounted to 2.9 per cent. Higher performance within that term was demonstrated only by 6 private management companies portfolios (PMCs).

As per the first quarter of 2009 results, the value of the assets in the mandatory accumulative pension system (regardless the funds of insurance contributions to the consolidated Russian Pension Fund (RPF) regression, started in the fall of preceding year has continued. As one can see from Table 1, the regression reached 1.7 per cent¹ (RUR 381.6 bln versus 387.8 bln).

Table 1

THE VALUE OF THE ASSETS IN THE ACCUMULATIVE MANDATORY PENSION SYSTEM,
2007-2009, RUR BLN.

Date	The value of assets invested in pension savings, allocated in management companies			Retirement savings in RPF	Total
	всего	Including RPF	Including PMC		
01.01.2007	276,2	267,1	9,2	9,96	286,2
01.04.2007	270,0	260,7	9,4	19,85	289,85
01.07.2007	274,5	265,1	9,4	19,25	293,75
01.10.2007	340,1	329,0	11,1	25,55	365,65
01.01.2008	375,1	362,9	12,2	26,8	401,9
01.04.2008	360,7	348,7	12,1	42,6	403,3
01.07.2008	366,0	353,7	12,3	43,1	409,1
01.10.2008	360,6	350,1	10,6	39,9	400,5
01.01.2009	352,2	343,1	9,1	35,5	387,8
01.04.2009	334,8	325,7	9,1	46,9	381,6

Note: – regardless insurance contributions to the accumulative share of RPF;

– management companies' performance indicators – net assets value, displayed at RPF web-site pprf.ru;

– RPF indicators – accumulated pension assets as per consolidated data on RPF performance, displayed by Federal Service for Financial Markets on the web-site fsmc.ru.

1 Hereinafter, RPF and Federal Service for Financial Markets (FSFV) data.

The share of the state management company (SMC), whose functions are performed by Vnesheconombank (VEB), in the assets of the mandatory pension system (regardless insurance contributions to the RPF) within the quarter decreased from 88.5 to 85.3 per cent. At the same time, in view of the statements of the insured persons on the transition to the accumulative pension fund (APS) or the choice of investment management company, VEB has transferred to RPF RUR 11.3 billion. The balance had been utilized to reduce the market value of assets that are invested in retirement savings. The share of APS over the same period increased from 9.2 to 12.3 per cent (see Table 2). The main reason is the transfer of the insured persons from RPF in the APS. Despite the financial crisis, the rate of this process decreased only slightly: in the Ist quarter of 2008, the share of APS accumulated assets in the of the mandatory pension system increased by 3.9 percentage points (from 6.7 to 10.6 per cent).

Table 2

DISTRIBUTION OF THE PENSION SAVINGS IN THE ACCUMULATIVE MANDATORY PENSIONS SYSTEM BETWEEN MC AND RPF, 2006-2009, IN %

	1.1.2006	1.1.2007	1.1.2008	1.1.2009	1.4.2009
Share in SMC	95,9	93,3	90,3	88,5	85,3
Share in PMC	3,0	3,2	3,0	2,3	2,4
Share in APS	1,1	3,5	6,7	9,2	12,3
Total	100	100	100	100	100
Including share in PMC and APS	4,1	6,7	9,7	11,5	14,7

Note. See note to Table 1.

Structure of the pension savings by private management companies

The structure of SMC and aggregate portfolios of PMC, investing pension assets under agreements with RPF as of late 2008 and I quarter of 2009 is provided in Figs 1-4.

SMC investments

The 4-fold growth of the share in the balance of accounts with credit institutions in the structure of the investment portfolio SMCs is striking (growth from 0.9 to 3.6 per cent), but in absolute terms, it is not too noticeable value to the banking system (RUR

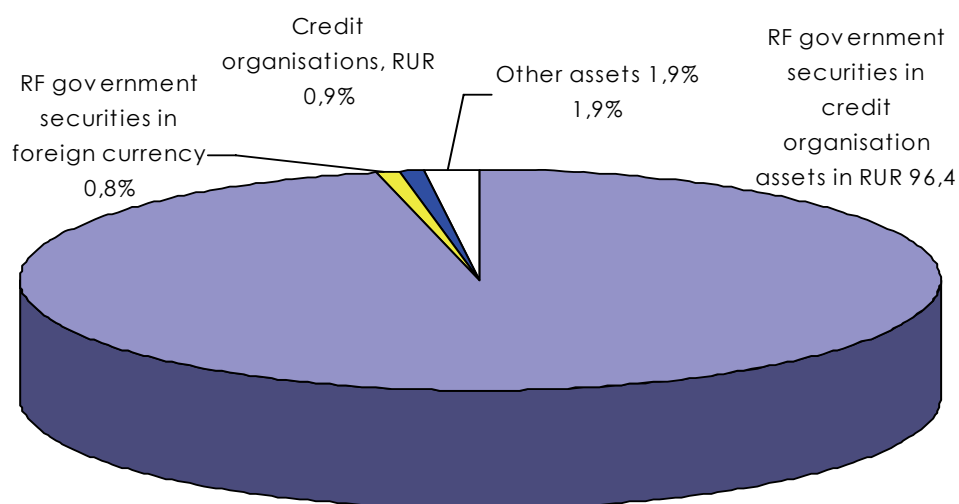


Fig. 1. Structure of the investment portfolio of state management company (Vnesheconombank) at the end of 2008

11.8 billion at the end of I quarter 2009). The share of investments in bonds of the RF foreign loans rose from 0.8 to 1.1 per cent. The share of the main instrument in which the SMC investing retirement savings, i.e., the bonds of the RF Government has downgraded from 96.4 to 94 per cent.

PMC investments

In the Ist quarter of 2009 growth of the

stock market in terms of MICEX index-10 amounted to 6,7 per cent (see Fig. 5), which should have had a positive impact on the dynamics of the assets value of the PMCs, which had a relatively high share in the investment portfolios and decided not to maintain the damages. However, in the aggregate PMCs' investment portfolio the share of securities has grown much less than if it were in the portfolios. A comparison of data in Fig. 3 and 4 demonstrates a growth of the securities shares in PMCs aggregate investment portfolio within the period, amounted to only 1.3 p.p. Among the instruments with a stable yield the proportion of corporate bonds has reduced to the greatest extent (from 43.2 to 40.8 per cent); the proportion of sub-federal bonds has also dropped down. At the same time, PMC increased the investments in ruble-denominated RF government securities, which share has increased from 4.8 to 5.2 per cent. However, the greatest share of investments has been made in "other assets" (see Fig. 3

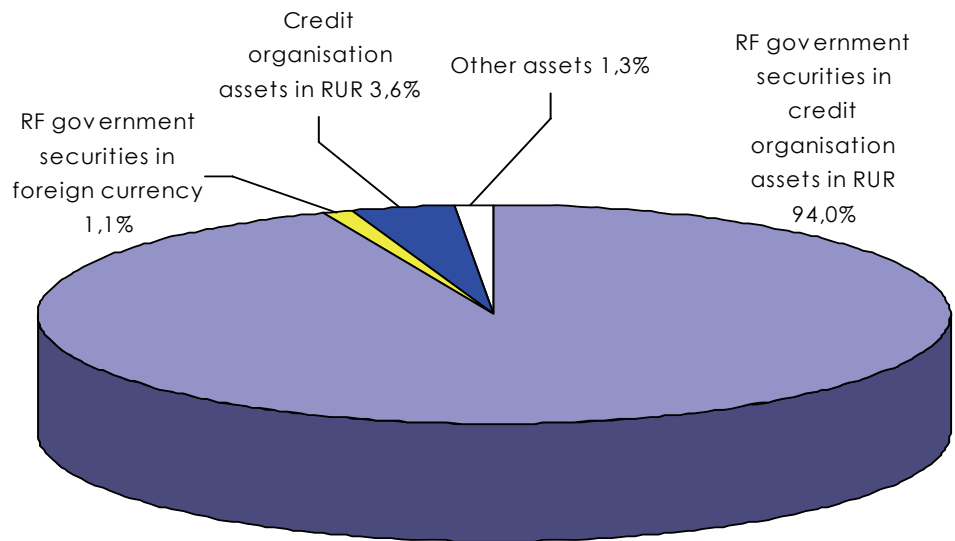


Fig. 2. Structure of the investment portfolio of public management company (Vnesheconombank) at the end of the 1st quarter of 2009

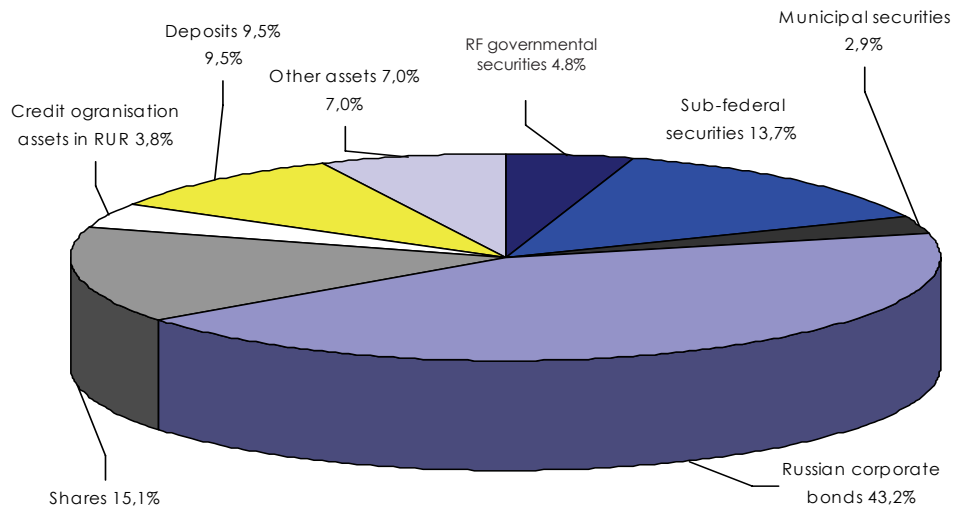


Fig. 3. Structure of the investment portfolios of private management companies at the end of 2008

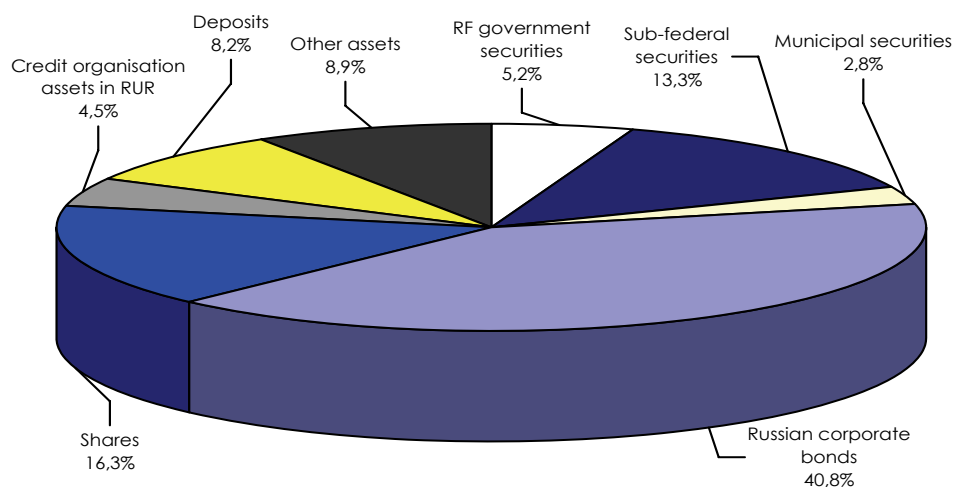
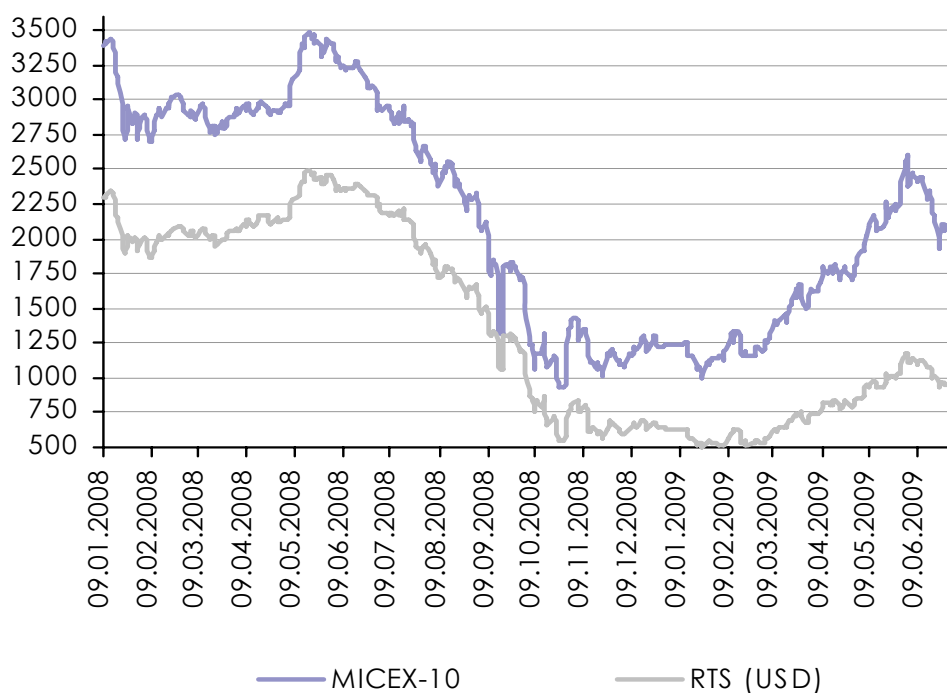


Fig. 4. Structure of the investment portfolios of private management companies at the end of the 1st quarter of 2009



Source: MISEX, RTS.

Fig. 5. : MISEX-10 and RTS indices in 2008–2009

remained positive. The maximum term, covered SMC statistics is 3 years. During this time, the average yield on SMC investments per annum was 2.9 per cent (see Table 3). The highest result for this period were demonstrated only by 6 PMC portfolios.

According to the results of the I quarter, a negative yield was observed only among 3 PMCs, one of which (FB AUGUST MC) has just started the trust management of pension savings. The yield of the others varied in the range from 7 to 88.7 per cent in annual terms. The average indicator amounted to 32.2 per cent in annual terms (against the average net assets value, assessed in accordance with the requirements of Art. 16 of the Federal Law «On investment funds for the accumulated share of labor pensions in the Russian Federation»). As per the three-year term, 3 private management companies have again demonstrated nominal yield.

Table 3
MANAGEMENT COMPANIES – LEADERS THE YIELD OF INVESTMENTS OF PENSION FUNDS WITHIN 3 YEARS

Management companies	Yield of investments of pension funds		
	For 3 years (Q II, 2006 – Q I, 2009), % per annum	Q I, 2009, % per annum	For (Q II, 2008 – Q I, 2009), % per annum
OTKRYTIYE	9,13	32,98	10,65
PH-TRUST	7,21	14,97	2,16
UM	6,00	29,79	-11,42
VIKA	5,86	13,76	4,75

and 4), in which the bulk is invested in the brokers accounts. The share of bank deposits is decreased by 1.3 percentage points.

Investment Yield

According to the results of I quarter 2009, the yield of pension savings, invested in SMC, was negative (-7.2 per cent) mainly due to unfavorable dynamics in the prices for the RF government bonds in this period

However, for a longer period the yield of pension savings, invested by SMC,

Table 3 cont'd

Management companies	Yield of investments of pension funds		
	For 3 years (Q II, 2006 – Q I, 2009), % per annum	Q I, 2009, % per annum	For (Q II, 2008 – Q I, 2009), % per annum
TRINF (IP*conservative capital saving)	5,77	30,06	6,31
PROMSVYAZ	4,25	22,17	-3,82
SMC (VEB)	2,93	-7,23	-3,09

* – IP–investment portfolio.

REVIEW OF MEETINGS OF THE GOVERNMENT OF THE RF IN AUGUST 2009

M.Goldin

In August at the meetings of the Presidium of the Government of the Russian Federation the important issue on making a number of amendments to the budgetary legislation was considered.

On August, 27 at the meeting of the Presidium of the Russian Federation the project of the Federal Law “On making amendments to some legislative acts of the Russian Federation and invalidation of separate statements of legislative acts of the Russian Federation” submitted by the Ministry of Finance of the Russian Federation was considered (further referred to as the bill).

Among other measures the bill envisages the adoption of the following amendments to the Budgetary Code of the Russian Federation:

- according to the first amendment it is suggested to establish the norm for the transfer of 100% earnings from the severance tax on hydrocarbons production (excluding the natural combustible gas) to the federal budget. At present, in concordance with the Budget Code 5% of payments of the tax mentioned is to be paid into the budgets of the subjects of the Russian Federation. At present this tax is paid to the budgets of 32 regions. It is explained that such an amendment is necessary due to the reduction of earnings from oil and gas revenues in the federal budget owing to the drop of prices and the export volumes of the natural resources.

It is expected that the centralization of the revenues from payment of severance tax on hydrocarbons (oil and gas condensate) in the federal budget will result in the increase of the revenues of the federal budget as the following: in 2010 – by no less than RUR 46.5 billion, in 2011- by no less than RUR 50.9 billion, in 2012 – by no less than RUR 55 billion.

It should be noted that in 2008 the total sum of the payments to the regional budgets made RUR 79.0 billion, which on average throughout the country makes 2% of fiscal and non-fiscal earnings of the budgets of the subjects of the Russian Federation.

The biggest volume of payments was registered in Tyumen oblast (more than 60% of the total volume), considerable inpayments of the tax are made to the budgets of the Republic of Tatarstan (6% of the total volume), Orenburg oblast (4%) and Republic of Komi, Perm krai, Arkhangelsk and Samara oblasts (3% each).

Since the establishment of the norm for the transfer of 100% earnings from the severance tax on hydrocarbons production to the federal budget will cause a reduction in the revenues of the subjects of the Russian Federation it is envisaged to compensate for them partially in the form of subsidies for the support of the measures to ensure the balance of the regional budgets (excluding Tyumen oblast) as the following: at the rate of 0% of the forecast revenues in 2010, 40% - in 2011, 20% in 2012.

In connection with a considerable proportion of the severance tax on the hydrocarbon resources production in the budget of Tyumen oblast (more than 40%) it is suggested to give subsidies during 4 years according to the following procedure: 100% of the forecast revenues in 2010, 75% in 2011, 50% in 2012, 25% in 2013;

- according to the second amendment it is suggested to suspend the direction of revenues from the management of the Reserve Fund and the Fund for the National Welfare

for the purposes of formation of the corresponding funds from January 1, 2010 to February 1, 2012.

At present the means of the Reserve Fund are deposited in the Bank of Russia, and the means of the Fund for National Welfare – in Bank of Russia and Vnesheconombank.

In concordance with the agreements with the banks mentions, the Bank of Russia transfers the revenues from the management of the means to the federal budget annually at the rate fixed as on January 15th of the year following the year of depositing. Vnesheconombank transfers the revenues from the management of the means quarterly to the federal budget in the quarter following the quarter of depositing. Then the revenues mentioned are directed to the formation of the corresponding Funds.

It is suggested to suspend the effect of the norm of the Budget Code according to which the revenues from the management of means are transferred for the formation of the corresponding Funds, from January 1, 2010 until the revenues for the 4th quarter 2011 from the management of the means of the Fund of the National Welfare deposited in Vnesheconombank and for 2011 from the management of the means of the Funds deposited in the Bank of Russia are transferred;

– according to the third amendment it is suggested to increase the profit share directed to the Bank of Russia to the federal budget, which was established by the Federal Law from July 10, 2002 No 86-FZ “On the Central Bank of the Russian Federation (Bank of Russia)” from 50% to 75%, which will allow attracting to the federal budget no less than additional RUR 20 billion annually. ●

REVIEW OF ECONOMIC LEGISLATION

I.Tolmacheva

In August the following important changes were made to the economic legislation: the higher education institutions and the scientific organizations have been granted the right to form economic entities; the procedure connected with the state regulation of prices for medicines; the procedure for definition of the kinds of especially valuable movable property of an autonomous organizations was specified; the volume of the minimum of subsistence in the Russian Federation was increased; the refinancing rate of the bank of Russia was lowered.

I. Federal Laws of the Russian Federation

1. "ON MAKING CHANGES TO SOME LEGISLATIVE ACTS OF THE RUSSIAN FEDERATION CONCERNING THE ISSUES OF FORMATION OF ECONOMIC ENTITIES BY BUDGETARY SCIENTIFIC AND EDUCATIONAL INSTITUTIONS WITH THE PURPOSES OF PRACTICAL APPLICATION (IMPLEMENTATION) OF THE RESULTS OF PRACTICAL ACTIVITY" from 02.08.2009 No 217-FZ

Comes into effect in 10 days after its official promulgation

Higher educational institutions and scientific organizations have received the right to form economic entities to apply in practice the results of intellectual activity. It is established that the budgetary scientific organizations and higher educational institutions as well as scientific organizations and higher educational institutions created by the state academies of science without the permission of their owner have a right to act as founders (also together with other persons) of economic entities the activity of which consists in the practical application (implementation) of the results of intellectual activity (programs for computers, databases, inventions, useful models, industrial samples, results of selections, integrated circuit layout, know-how's), exclusive rights for which belong to these scientific organizations and higher educational institutions. The scientific organizations and higher educational institutions make a contribution in the authorized capital of such economic entities in the form of the right to use the results of the intellectual activity and may contribute monetary funds, equipment and other property they manage on day-to-day basis. Higher educational institutions and scientific organizations have a right to attract other persons as co-founders (participants) of an economic entity if the share of this scientific organization or higher educational institution makes more than 25% in the authorized capital of a joint-stock company or more than one third of the authorized capital of a limited company. The profits from managements of shares (stocks) in the authorized capital of economic entities, whose founders (participants) are scientific organizations or higher educational institutions, a part of the profit of the economic entities received by these higher educational institutions or scientific organizations (dividends), are transferred for independent use, taken into account on a separate balance and are directed only for the protection of rights for results of intellectual property, paying royalties to authors and conducting statutory activity of these scientific organizations and higher educational institutions.

II. Decrees of the Government of the Russian federation

1. “ON MAKING CHANGES TO THE DECREE OF THE GOVERNMENT OF THE RUSSIAN FEDERATION FROM MAY 31, 2009 NO 337” from 05.08.2009 No 639

The procedure for definition of the kinds of especially valuable movable property of an autonomous organization was specified. According to the changes made to the Decree of the Government of the Russian Federation from 31.05.2007 No 337 “On procedure for determination of the types of especially valuable movable property of an autonomous institution”, it is envisaged, for instance, that when defining the kinds of especially valuable movable property of autonomous federal organizations among others the movable property the balance value of which exceeds RUR 500 thousand is to be included in the list (earlier the value was RUR 50 thousand).

2. “ON IMPROVEMENT OF THE STATE REGULATION OF PRICES FOR VITAL AND IMPORTANT MEDICATIONS” from 08.08.2009 No 654

Comes into effect on January 1, 2010

The decree makes amendments to the decrees of the Government of the Russian Federation establishing the procedure for the state regulation of prices and tariffs including the prices for medication, to the decree, defining the procedure for import and export of medications as well as in the decrees that envisages the authority of the federal executive bodies in the part concerning the establishing of prices for medications. This decree regulates in further detail the procedure of the state regulation of prices for medications included in the list of vital and most important medications established by the Government of the Russian Federation. The government regulation of prices for medications is conducted via compulsory state registration of maximum sales prices of producing organizations as well as establishing the maximum wholesale and retail increments for the real sales prices of producers. The changes were also made to the procedure of the state registration of the maximum sales prices for medications of foreign producers.

The maximum sales prices of producers will be defined according to the method that is to be approved by the Ministry of Health Care and Social Development of the Russian Federation together with the Federal Tariff Service. The method mentioned should include the forms according to which the producer gives grounds for the maximum sales price when applying to the Federal State Service for Surveillance in the Sphere of Health Care and Social Development in order to make the state registration of the price. At present all the forms according to which the producer substantiates the maximum sales prices are to be approved by the Federal State Service for Surveillance in the Sphere of Health Care and Social Development on agreement with the Federal Tariff Service of the Russian Federation.

It is established that the maximum wholesale and retail increments to the medications established by executive bodies of subjects of the Russian Federation regarding the organizations of wholesale of medications and pharmacies are to be expressed as percentage and be differentiated depending on the cost of the medications taking into account the geographical remoteness, transport availability and other specific features. It is also established that the maximum wholesale and retail increments to the real prices of producers should be established by executive bodies of subjects of the Russian Federation in accordance with the method approved by the Federal tariff Service.

3. “ON ESTABLISHING THE AMOUNT OF THE MINIMUM SUBSISTENCE PER CAPITA AND FOR THE MAIN SOCIAL AND DEMOGRAPHIC GROUP OF THE POPULATION ON THE WHOLE THROUGHOUT THE RUSSIAN FEDERATION OVER THE 1ST QUARTER 2009” from 19.08.2009 No 666

The sum of the minimum subsistence level on the whole throughout the Russian Federation over the 1st quarter 2009 per capita is established at the rate of RUR 5083 (RUR

4693 for the 4th quarter), for able-bodied population – RUR 5497, for pensioners – RUR 4044, for children – RUR 4857 (for able-bodied population – RUR 5086, for pensioners – RUR 3712, for children – RUR 4472, correspondingly, in the 4th quarter 2008).

III. Instructions, Letters, Orders

1. Order of the Central bank of the Russian federation “ON REFINANCING RATE OF THE BANK OF RUSSIA” from 07.08.2009 No 2270-U

Starting from August 10, 2009 the refinancing rate of the Bank of Russia is established to be 10.75% per annum. Earlier, starting from July 13, 2009 the refinancing rate of 11% per annum was in effect. ●

REVIEW OF REGULATORY DOCUMENTS CONCERNING TAXATION OVER JULY–AUGUST 2009

L.Anisimova

1. According to the letter of the Federal Tax Service of the Russian Federation from July 23, 2009 No 3-1-10/529 the question about the filling of the tax declaration for VAT was clarified. For instance it was recommended that: - the sum that is presented to the buyer when transferring the means for payment, partial payment of the forthcoming delivery of the goods (execution of works, services rendering), transfer of property rights that is to be deduced from the buyer should be reflected in line 220 section 3 of the declaration;

– the sum of VAT that was earlier deduced by the taxpayer in case the buyer transferred the means for payment, partial payment of the forthcoming delivery of the goods (execution of works, services rendering), transfer of property rights that is to be recovered should be reflected in line 190 of the same section.

2. According to the letter of the Federal Tax Service of the Russian Federation from July 27, 2009 No 3-2-09/150 it is elucidated that if the object exploited for a long time was originally erroneously included in the amortization group the taxpayer should independently calculate the sum of the profit tax that is to be paid over the taxation period on the assumption of the taxation base, tax rate and tax privileges. If errors (falsification) in calculating the taxation base are discovered, the taxpayer in concordance with the article 54 of the Tax Code of the Russian Federation must recalculate the taxation base, that is, correct the mistake that he made himself. The taxpayer can recalculate the taxation base for the profit tax both for the current and for the preceding taxation (accounting) periods, submitting the corrected tax declaration to the taxation body.

When it concerns the property tax, the organization must correct the tax liabilities from the moment the mistake was made (since due to different amortization norms the average annual value of property changes) and submit the corrected tax declaration to the taxation body.

3. According to the letter of the Ministry of Finance of the Russian Federation and the Federal Tax Service of the Russian Federation from August 10, 2009 ShS -22-3/626@ the question on the filling of the declarations for the profit tax is clarified which arose in connection with the changes introduced in articles 258 and 259 of the Tax Code of the Russian Federation by the Federal Law from 26.11.2008 No 224-FZ and introduction of the amortization premium – the right to include the expenses for investments (completion of construction, equipment, modernization) in the number of expenses of the account (taxation) period at the rate of no more than 10% (no more than 30% regarding fixed assets belonging to the third-seventh groups of amortization) of the initial value of the fixed assets (excluding the fixed assets received gratuitously). Before the changes to the declaration were made such expenditures were recommended to be reflected in the list of extraordinary expenses in line 044 of the Appendix No 2 to List 02.

4. According to the decision of the plenary session of the Supreme Arbitrary Court of the Russian Federation from July 23, 2009 No 54 some questions connected with levying of the land tax were elucidated.

For instance, the plenary session of the Supreme Arbitrary Court explained that the payers of the land tax refers to the persons whose rights are registered according to the procedure established by the Federal Law “On the state registration of the rights for immovable property and the deals with it” and the persons that though being unregistered retain such a right. According to paragraph 1 article 6 of the Law the rights for the immovable property if they emerged before the Law came into effect are recognized as legally effective even if there is no state registration of the property which is made upon the desire of the rightholders.

The consequence of paragraph 9 article 3 of the Federal Law “On enactment of the Land Code of the Russian Federation” should be noted, according to which the state acts, certificates and other documents testifying the rights for land and issue before the Federal Law “On the state registration of the rights for immovable property and deals with it” came into effect have the same legal force as the records in the register.

The same rights are enjoyed by the universal legal successors when reorganizing the legal entities (excluding reorganization in the form of the segregation) and their heirs. The proprietary interest for the land plots mention in paragraph 1 article 388 of the tax Code of the Russian Federation are transferred to them directly on the basis of the law, and that is why the legal successors become taxpayers of the land tax irrespectively of whether the transfer of corresponding rights is registered.

5. According to the latter of Federal Tax Service of the Russian Federation from August 12, 2009 No ShS-22-3/634@ the question on the procedure for submission of invoices by the tax agents is elucidated.

In concordance with paragraph 3 article 168 when paying for goods (works, services, property rights), and namely at the moment of advance payment for them (made fully or partially) or at the moment of payment for really delivered goods (works, services) that are taken on balance the invoices are filled in the period of no later than 5 calendar days counting from the day of goods shipping (execution of works, services rendering) or from the day the property rights were transferred or from the date the advance payment for the further delivery was received.

In concordance with article 161 of the Tax Code of the Russian Federation when the goods (works, services) are sold in the territory of the Russian Federation by foreigners, these foreigners are recognized to be taxpayers that are not registered in the taxation bodies of the Russian Federation as such. However the VAT taxation base for such operations is defined as a sum of the profit from the sale of goods (works, services) taking VAT into account. Concerning such operations of foreigners the organizations and individual entrepreneurs registered in the taxation bodies of the Russian Federation and purchasing in the territory of the Russian Federation the goods (works, services) from the foreign persons are recognized to be the tax agents that must deduct and pay VAT. The tax agents should calculate, deduct from the taxpayer and pay to the budget the corresponding sum of the tax irrespectively of whether the tax agents themselves pay VAT on their own operations.

Similarly, the question concerning recognition of the leaseholder of the federal property, property of subjects of the Russian Federation and municipal property as tax agents was solved. In this case the taxation base is defined as a sum of the rent taking VAT into account.

The above-mentioned tax agents must make out invoices when calculating VAT according to the procedure established by paragraphs 5 and 5 article 169 of the Tax Code of the Russian Federation, register these invoices in sales book (when making payment or partial

payment including with the use of the non-monetary operations for the forthcoming delivery of goods (execution of works, services rendering) or when purchasing goods (works, services)).

The letter of the Federal Tax Service of the Russian Federation elucidates the procedure for filling the form of an invoice by tax agents.

The Federal Tax Service clarifies that the regulations that came into effect and allow the taxpayers-buyers to apply tax deductions for VAT to the advance payments for forthcoming delivery (in case the VAT taxpayer has an invoice drawn by the VAT payer that sells on receipt of payments, partial payment for forthcoming delivery of goods (execution of works, services rendering)) are not applied to the tax agents that purchase the goods from the mentioned foreign persons. Though the Tax Code of the Russian Federation contains the rights of the tax agents to deduct the withheld taxes, which is envisaged by the separate article 171 of the Tax Code of the Russian Federation, the text of the article has an explicit restriction for the deduction of such sums for tax agents that purchase goods from foreign persons not registered as VAT payers in the Russian Federation.

6. According to the decree of the Supreme Arbitrary Court of the Russian Federation from July 23, 2009 No 60 some question on taxation arose as a result of changes made by the federal Law from 31.12.2008 No 296 to the Federal Law “On insolvency (bankruptcy)” (further referred to as the law on bankruptcy) were clarified.

For instance, the plenary session of the Supreme Arbitrary Court explained (paragraph 41) that the application of the regime of requirements on compulsory payments claimed after the register of creditors’ requirements had been closed was excluded in the new version of the Law on bankruptcy.

In connection with this requirement of compulsory payments evolving after the contest production had been opened in concordance with indention 5 paragraph 2 article 134 of the Law on bankruptcy are referred to the current payments of the fourth turn. In order to collect these payments the taxation body has a right according to article 46 of the Tax Code of the Russian federation to submit a collection letter to the bank which is to be fulfilled by the bank taking into account the order established by the Law on bankruptcy for current payments. At the same time the taxation body has not got the right to make a decision envisaged by article 76 of the Tax Code of the Russian Federation on suspension of the operation of the debtor’s account, since in the period of bankruptcy another person manages it externally, that is the court procedure is going on.

7. According to the Decree of the Government of the Russian Federation from July 30, 2009 No 628 in concordance with subparagraph 13 paragraph 1 article 264 and subparagraph 22.1 article 346.5 of the Tax Code of the Russian Federation the diet and the norm for catering of the crews of sea and river vessels of the fishing fleet (calculation of a norm per one person a day) were approved. The expenditures mentioned are included into the list of other expenses connected with the goods production and sale for the purposes of profit taxation.

8. According to the Decree of the Government of the Russian Federation from July 30, 2009 No 630 changes were made to the list of international, foreign and Russian awards for outstanding achievements in the field of science and technology, education, culture, literature, arts and mass media, which sums received by taxpayers are not subject to taxation, approved by the Decree of the Government of the Russian Federation from February 6, 2001 No 89.

9. According to the Federal Law from July 19, 2009 No 202-FZ changes were made to chapter 23 of the Tax code of the Russian Federation (“Tax on incomes of natural persons”) and chapter 25 (“Tax on profit”) of the Tax code of the Russian Federation.

The notion of lucre from the economy on interest rates for the use of borrowed funds to purchase the individual housing is enhanced within the framework of payment of the tax on natural person’s income. Besides, the text of the chapter is supplemented with the information on purchasing the land plots on borrowed funds for individual housing construction, and the land plots on which the purchased houses are situated and the share in them. As to the notion of interests for credits, now the interests for use of borrowed funds (credit) provided by the banks in the territory of the Russian Federation for the purposes of refinancing (re-crediting) of loans (credits) also belong to such interests.

The lucre can be exempted from taxation in case a taxpayer has a right for tax deduction (expenses for these purposes testified by documents), approved by a taxation body.

Not only were the incomes in the form of the financial aid to the members of family of the deceased employee or the financial aid to the employee in the connection of the death of his members of family included in the list of incomes not taxed with the tax on income, but also the incomes in the form of financial aid to the retired organization’s employee in connection with the death of a member of family and to the family of the deceased retiree employee of the organization.

The incomes of individual persons derived from the sale of passenger cars are also exempted from taxation on condition that before the passenger car was taken off the register, it had been registered in concordance with the legislation of the Russian Federation for the individual persons mentioned for the period of three years and more.

Property tax deduction when selling other property in the ownership of a taxpayer was increased from RUR 125 thousand to RUR 250 thousand.

The procedure for notification of the taxation bodies by banks on the incomes of a client-taxpayer in the form of lucre from interests for the credit provided by the bank is specified. For instance, the bank should submit the data on impossibility to collect the tax and on the sum of the debt to the taxation body of the place of its registration in one month after the date of the end of the taxation period in which the client received the incomes mentioned.

Temporarily (before 31.12.2009) the norms for ascription of the paid interest rate to the expenditures of the organization have been increased: from 15% to 22% for credits in foreign currency and at the rate of the double refinancing rate of the Bank of Russia for credits issued in rubles.

10. According to the letter of the Ministry of Finance of the Russian Federation and the Federal Tax Service of the Russian Federation from August 10, 2009 No ShS-22-6/627@ the issue of the notion of a representative for individual entrepreneurs within the framework of the Tax Code of the Russian Federation was elucidated. To promote orderliness in organization of the submission of tax accountancy and other data presented by taxpayer that is an individual entrepreneur in the taxation bodies it should be noted that the authorized representative of a taxpayer that is an individual entrepreneur carries his authority on submission of accountancy and other data to the taxation body on the basis of warrant issued in concordance with the requirements of paragraph 5 article 185 of the Civil Code of the Russian Federation. The warrant is needed to present the accountancy both in paper and in the electronic form.

11. According to the letter of the Ministry of Finance of the Russian Federation from July 24, 2009 No 03-07-09/33 the question on the procedure for deduction of VAT for advanced

payments transferred with several payment orders according to the agreement that envisages 100% pre-payment of the purchased goods is clarified.

According to paragraph 9 article 172 of the Tax Code of the Russian Federation the deductions of sums of VAT are made by buyer on the basis of invoices drawn by seller upon receipt of the payment (partial payment) for the forthcoming delivery of goods. That is why if a buyer according to the agreement is to make 100% pre-payment to the seller the sums of VAT that are drawn by the seller to the buyer in invoices for advance payment can be deducted. In order to avoid double taxation the sums of VAT that were deducted when making advance payments should be recovered in tax liabilities in the taxation period when the sums of Vat for actually purchased goods are to be deducted.

12. According to the letter of the Ministry of Finance of the Russian Federation from July 31, 2009 No 03-11-09/270 the question on the possibility of application of the single social tax for the imputed income by an individual entrepreneur in case he uses for his activity his own transport vehicles and at the same time uses the transport vehicles of other persons upon agreement with them and the total number of transport vehicles operated by the entrepreneur for rendering services of transportation does not exceed 20 is clarified.

13. According to the letter of the Ministry of Finance of the Russian Federation from July 30, 2009 No 03-07-11/189 it is clarified that the purchase by the organization of the services for providing it with the place in the building that is in the municipal ownership for the purposes of advertising placement fits the situation considered in the Informational letter of the Presidium of Supreme Arbitrary Court of the Russian Federation from 11.01.2002 No 66 "Review of the practice settling the arguments concerning rent", according to which the agreement between the owner of the building and the other person on which basis the latter uses separate constructive element of the building for the purposes of advertising is not the agreement of rent. Because of this, the persons purchasing the services on placement the advertisement on the building of municipal ownership are not the lessees of municipal property, the payment for such services is not the rent, and, correspondingly, such persons should not act as tax agents for payment.

14. According to the letter of the Ministry of Finance of the Russian Federation from June 22, 2009 No 58n the form for the tax declaration for the tax paid in connection with the simplified system of taxation and the Procedure for its filling is approved.

15. According to the letter of the Ministry of Finance of the Russian Federation from 24.07.2009 No 03-05-04-02/50 and the Federal Tax Service of the Russian Federation from August 17, 2009 No ShS-17-3/157@ the question on payment of the land tax is clarified.

For instance, it is clarified that the land plots given on the basis for the permanent (indefinite) use to the federal budgetary enterprises and the federal state unitary enterprises conducting in concordance with their statutory the development, production, repair of armaments and military equipment are not recognized as the objects of taxation with the land tax in concordance with subparagraph 3 paragraph 2 article 380 of the Tax Code of the Russian Federation. If the land plots given to the above-mentioned enterprises are occupied only by the objects that are not connected with the conduction of the statutory activity such as shops, after-work sanatoriums, clubs, kindergartens, residential buildings, sport complexes etc., they are not subject to subparagraph 3

paragraph 2 article 380 of the Tax Code of the Russian Federation and land tax for them should be paid.

Abandonment of Single System of Compulsory Payments – Consequences for Russian Business

In concordance with the federal law from July 24, 2009 No 213-FZ chapter 24 of the Tax code of the Russian Federation “Single Social Tax” becomes invalid on 1.01.2010.

The notion of the organization operating in the field of information technologies for which the Tax Code of the Russian Federation recognizes the expenditures for see purchase of computers as material expenses for the purposes of taxation.

In fact the mentioned Federal Law means that the policy of accumulation within the framework of a single Law (Tax Code of the Russian Federation) of the system of compulsory payments levied in the territory of the Russian Federation, standardization and unification of tax bases, reaching of the maximum possible neutrality of the compulsory payments with regard to all taxpayers (that is the leveling of the maximum load for the aggregated incomes of taxpayers simultaneously along two directions: for incomes received in the territory of the Russian Federation regardless of whether the taxpayer is a resident of Russia or a foreign organization, and for the incomes of the Russian taxpayer regardless of whether they are in the territory of the Russian Federation or abroad) is abandoned. According to this (old) system single social tax was considered as a forced measure that is retained only for the period of transfer to the market economy. This tax due to its compulsory nature distorted market conditions for Russian producers of goods and was to be gradually transformed into a system of agreements and the sort of suspended income. It was envisaged that the competitiveness of Russian goods rising, such social payments made on the basis of the agreements with the state social funds will be considered as a special form of labor remuneration (suspended in time) that is to serve as an additional stimulus for attraction of highly-qualified specialists to the Russian enterprises.

The main tasks that were to be solved with the reform of taxation were: (1) to define the whole list of compulsory payments, bases and rates within the framework of one Law in order to be able to establish maximum tax load for each producer and exclude the introduction of additional compulsory payments by any other laws; (2) to concentrate all the earnings in one fund – State budget, abandoning allotment of purposeful payments for solution of any particular tasks, thus excluding the possibility for atomization of the State budget, its transformation in the aggregation of many surrogate funds, achieve the maximum transparency of the formation of the revenue part of the budget and distribution of expenses. These two tasks are the fundamental principles for the formation of anti-corruption financial system of any state functioning in the environment of open market.

At present the logic of the social contributions in Russia it transferred to directly opposite one: separate Laws regulate compulsory payments to particular funds with all the characteristics of taxes. Though such payments are called insurance contributions, this is not the insurance but compulsory taxation (the payment is made for the able-bodied citizens and the funds received are directed to pay pensions to the previous generations). In this respect the single social tax accurately reflected the essence of the problem (shortage of funds), while the current system of “insurance” contributions distorts and disguises it.

The abandonment of the system of compulsory payments accumulated within the framework of the tax Code of the Russian Federation will soon revive all the problems that existed earlier, which were the reason for consolidation of many compulsory payments and contributions to the single (social) tax: dissatisfaction of goods producers connected with existence of many controlling bodies (the number of checks will increase dramatically – each fund will have a right to check that the contributions were accrues correctly), multiplicity of

separate systems of fines and penalties, existing disagreements of bases for the calculation of sums of compulsory social payments and the tax on incomes of natural persons since they are regulated by different legislation (at present there is no such problem since when dividing the contributions the base similar to that of the single social tax which was unified as much as possible within the framework of the Tax code of the Russian Federation with the tax on incomes of natural persons was retained) – all the factors that had depressing effect on the business and were replaced with the single social tax. Besides, due to the expected increase in the total rate of insurance fees low profitable enterprises are likely to transfer to the shadow economy the criminal control over them recovering etc.

It is difficult to agree that the replacement of the single social tax with the system of compulsory payments (fixing a separate compulsory source for each fund) is an effective economic solution in the present situation of shortage of means in social funds. Not going into analysis of the reasons for such shortage we should note that the increase of VAT rate will allow to solve this problem more effectively. On the one hand, this would allow attracting to the formation of the additional sources (which could be directed to social funds through the budget) of the foreign participants of the Russian market as well as the Russian producers of goods. Taking into account that in the end Vat is paid by the consumers – that is the citizens of the Russian Federation, the total tax load on the Russian economy would not decrease but would be redistributed in proportion with the incomes of citizens and above all it would not distort the proportions of Russian and foreign goods at the market that was formed as a result of the competition. The decision on abandonment of the single social tax with further increase of the rates of compulsory contributions to the social funds that was adopted is fraught with a dangerous distortion of the tax load towards Russian producers of goods. As a matter of fact, in contrast to VAT (with which any goods are levied) the decision on the increase of the social contributions will result in artificial increase of the expenses of Russian business which will inevitably lead to the decreased competitiveness of the Russian goods as compared with the import analogues due to the forced growth of prices. Other taxes that are established as a markup to the price – excises, VAT - will grow inevitably. And all this conglomeration of the additional tax load will affect only the Russian producers of goods since it is only than that should pay increased social contributions and as a result will not be able to sell the goods that were “forced to become more expensive”. The Russian business that is connected with high labor input – and this is primarily innovation, IT-business, science and education, culture, where the intellectual component in the expenses is high – will face substantial additional problems.

It should also be noted that such atomization of the former single social tax will inevitably lead to the excessive increase in the number of administrative and management personnel of social funds, since in each of them a separate staff for registration of contributions will be recovered (earlier this was the task of tax officers).

In our opinion, in the environment of crisis such a reform may have extremely grave consequences for the Russian business. ●

SOME ISSUES OF CORPORATE INCOME TAXATION: APPLICATION PROCEDURE OF ART. 269, RF TAX CODE

T.Malinina

Article 269 of the Tax Code stipulates the specifics of accounting the interest on debt liabilities as expenditures, as well as the rules, hindering the practice of thin capitalization¹. Federal law № 202-FZ of July 19, 2009 has suspended the effect of the fourth paragraph of Section 1 of Art. 269 of the Tax Code, which establishes the threshold of interest rate accounted as expenses for the tax purposes till December 31, 2009; this provision is applicable to legal relationships, arising since September 1, 2008. Herewith, the provisions 2-4. of Article 269 of the Tax Code have not undergone any changes.

Paragraph 4, Item 1 of Art. 269 in the currently effective version of the Tax Code establishes the following limit for the accounting of interest rate as an expense for tax purposes in regard to corporate income tax: in case of absence of debt liabilities to the Russian entities, issued in the same quarter in comparable circumstances, with regard to the choice of a taxpayer, the threshold of the interest rate is recognized as expense shall be assessed as the refinancing rate of Central Bank of Russia, multiplied be 1.1 times for the RUR debt liabilities and equal to 15 per cent for the debt liabilities, denominated in foreign currency.

In accordance with Art. 5 of the Federal Law № 202-FZ, before December 31, 2009 the threshold the interest rate, recognized for the tax purposes in accordance with Paragraph four, Item 1 of Art. 269 of the Tax Code, shall be equal to the refinancing rate of the Central Bank of Russia, multiplied by 2 - on debt in rubles and equal to 22 per cent - on the debt in foreign currency. Therefore, the provisions of Art. 5 of the Federal Law № 202-FZ mitigate the standards for the recognition of interest rate as expenses for tax purposes.

It should be noted, that the expansion of the above threshold of the debt liabilities in rubles was made gradually. Article 8 of the Federal Law № 224-FZ, dated November 26, 2008 stipulated the limit value of interest on debt liabilities in rubles, recognized as expense for tax purposes in accordance with Paragraph four of Item 1 Art. 269 of the Tax Code, set up the refinancing rate of Central Bank of Russia, multiplies by 1.5 times. With the adoption of the Federal Law № 202-FZ that provision became invalid. It was replaced by Art. 4 of the Federal law, which established the restriction of 1.5 of the Central Bank refinancing rate for the period until July 31, 2009. From August 1, 2009 the Art. 5 of the Federal Law, is valid, i.e., the limit is further mitigated.

The increased threshold of interest on debt liabilities, recognized as expenses for the tax purposes in regard to corporate income tax of organizations, can be regarded as a measure bringing the restrictions, imposed by the tax legislation, in line with interest rates, under which one can involve borrowed funds in practice in the situation of financial crisis². However, the legal regulations, reviewed here do not affect the effective Item 2-4 of Article 269 of the Tax Code, i.e., the provisions, counteracting the practice of thin capitalization.

¹ Substitution of funding organizations through participation in equity financing through the provision of loan funds is understood as the practice of thin capitalization.

² In "Guidelines for the Tax Policy of the Russian Federation in 2010 and the planned term for 2011 and 2012" (approved by the RF Government on May 25, 2009), this measure is called "operational" (see p. 21).

Currently, if a Russian entity has a debt on the last day of the reporting (tax) period, which exceeds 3 times (12.5 times for banks and organizations engaged exclusively in leasing activity) the balance between the amount of assets (equity) and the value of liabilities of the organization, the threshold of the interest to be recognized as expenses for tax purposes of corporate income tax is assessed accordance with Paragraph 2 of Art. 269 of the Tax Code. If the accrued interest exceeds the limit, it is accounted in accordance with Paragraph 2 of Art. 269 of the Tax Code, and the balance is recognized for tax purposes as dividends, paid by the Russian Organization to a foreign entity, in respect to which there is a controlled debt.

According to Item 2, Article 269 of the Tax Code, the indebtedness of the organization is regarded as controlled in the presence of outstanding debt: to a foreign organization, directly or indirectly owing more than 20 per cent of the authorized (equity) capital of that organization; or to the Russian agency recognized in accordance with Russian laws as an affiliate entity of the organization, as well as in case of the debt liabilities, in respect to which such affiliate entity and (or) such foreign organization acts as a guarantor, underwriter or otherwise undertakes to ensure the debt repayment of the Russian organization.

Therefore, the regulations, counterfeiting the practice of thin capitalization, in accordance with Russia's tax laws apply only to affiliated (related) entities.

In the situation of economic crisis, which involves the lack of liquidity and tightened conditions for obtaining credits, it is suggested that the rules of Art. 269 of the Tax Code, which oppose the practice of thin capitalization, are in contradiction with the objective of facilitating access to credits for businesses and promotion of the monetary inflow to the economy. Moreover, in view of the devaluation of the ruble in the category of controlled debt, on which in accordance with Paragraph 2 of Art. 269 of the Tax Code shall be accounted as a threshold of the interest to be accepted for tax purposes, a greater number of loans was accepted, since the devaluation affected the ratio of controlled debt and equity of organizations.

In these circumstances, the provisions of Art. 269 of the Tax Code, which oppose the practice of thin capitalization, have been criticized, whereas some arguments seem to be quite reasonable. For example, provisions of the effective Art. 269 of the Tax Code, based on the approach of interdependence (affiliation) of entities, cause serious difficulties in administration of the relevant provisions of tax laws, which can not be regarded as sufficiently effective, in particular in counterfeiting the practice of compensatory loans¹. Moreover, the effective Art. 269 of the Tax Code discriminates the taxpayers on the basis of foreign participation in equity, as the rules against thin capitalization are not applied in respect of the debts of the Russian organizations, not affiliated with foreign organizations.

Along with the criticisms, there expressed proposals to amend Art. 269 of the Tax Code, which can fairly be broken down into those that set up specific conditions of application of the article in the financial crisis, and those that are proposed to be permanent. In the first group, it is proposed, in particular, to suspend the effect of Item 2.4 of Art. 269 of the Tax Code from September 1, 2008 to December 31, 2009 with a possibility of extension the suspension², i.e., to follow the same path that was proposed in Item 1 subsection 1 of this Article. It appears that this approach should not be widely implemented in practice, at least because in the crisis situation fiscal discipline does not lose its relevance.

1 Loans, provided by affiliate entities indirectly, but through an independent bank and understood as back-to-back loans.

2 Such a proposal, in particular, was expressed in a letter of the American Chamber of Commerce in Russia to the RF Ministry of Finance

The second group of proposals involves, as a rule, the introduction of targeted amendments to Article 269 of the Tax Code, aimed primarily at reducing the list of situations in which the debt of a Russian organization will be regarded as a controlled debt. For example, there are proposals not to apply the provisions for thin capitalization counterfeiting in cases where no payment the Russian borrower to foreign shareholders took place, as well as when a guarantee of foreign affiliated companies has resulted in a more favorable credit conditions¹.

It should be noted that the introduction of targeted amendments to the Article 269 of the RF Tax Code will complicate the administration of relevant regulations, since the surplus requirements to identification of the controlled debt and/or affiliated (related) entities will further complicate the structure of Art. 269 of the Tax Code, and will also bring new risks in application of the rules that work against the practice of thin capitalization. These risks are involve, among other things, with the definitions, which are difficult to describe in thee tax law wording and, accordingly, complicated in administration and enforcement. In particular, it is not clear how to define to administer the “preferable conditions for obtaining credit”.

However, there can be proposed an approach, based on the amendment to Art. 269 of the Tax Code, which allows to avoid the definition of affiliation (interdependence) of entities, discrimination of organizations with foreign participation in equity, as well as the assessment of the shares of the borrowed found versus his equity for the app provisions on thin capitalization counterfeiting. To this end, an alternative version of Art. 269 of the Tax Code should foresee a deduction of expenditures for interest payments (net interest²) for tax purposes should be limited to a fixed threshold of taxable income within the actual amount of such cost. Herewith, the interest, not accepted for deduction in the current period, under certain circumstances can be taken for deduction in future periods. This approach is included in «The main trends of tax policy of Russia for 2010 and the planned period 2011 and 2012”.

1 See, eg., Proposals of the American Chamber of Commerce in Russia.

2 Under the pure interest is understood an excess of the interest payments made during the period, versus the revenue in the form of interest received in this period.

REVIEW OF BUDGETARY LEGISLATION

M.Goldin

A number of important events in the field of the budgetary legislation took place in August: the Regulations on the formation, provision and distribution of subsidies from the federal budget to the budgets of the RF subjects were supplemented; the rate of subsidies granted to the RF subjects to co-finance the objects of capital construction of the state property of RF subjects and of the municipal property that were not included in the federal targeted programs were defined; it was decided to transfer of the means of the State Corporation “Fund for Assistance of the Reforms in Housing and Communal Services”.

According to the decree of the Government of the Russian Federation from 20.08.2009 No 693 “On making changes to the regulations of formation, granting and distribution of subsidies from the federal budget to the budgets of subjects of the Russian Federation” the Regulations of formation, granting and distribution of subsidies from the federal budget to the budgets of subjects of the Russian Federation (further referred to as the Regulations) were supplemented.

The following addenda were made to the Regulations mentioned:

1. As to the subsidies envisaged within the framework of long-term (federal) targeted programs, whose action is terminated by January 1, 2011, the state clients that coordinate long-term (federal) targeted programs have a right to be guided by the targeted distribution of subsidies established earlier and their distribution among the subjects of the Russian Federation within the limit of the budget allotments envisaged by the Federal Law “On the federal budget for 2009 and for the planning period of 2010 and 2011” and (or) by the regulatory legislative acts adopted in concordance with it by the Government of the Russian Federation;

2. It was established that in 2009 when granting and distributing the subsidies the level of co-financing of a expenditure liability of a subject of the Russian Federation envisaged by paragraph 13 of the Regulations for the subjects of the Russian Federation which level of the calculated provision with budget funds after the distribution of the subsidies for 2009 exceeds by less than three times the average level of the calculated provision with the budget funds of subjects of the Russian Federation (envisaged by the Decree of the Government of the Russian Federation from November 22, 2004 No 670 “On distribution of subsidies for leveling the provision with budget funds of the subjects for the Russian Federation”) could not be stated to be less than 40% and more than 95% of the expense liability;

3. In case the corresponding long-term (federal) targeted programs envisage co-financing of the objects of capital construction of the state property of subjects of the Russian Federation and (or) granting the corresponding subsidies from the budgets of subjects of the Russian Federation to the local budgets to co-finance the objects of capital construction of municipal property when defining the purpose of subsidies the targeted distribution of subsidies with specification of their amount for each object of capital construction included in long-term (federal) targeted program and (or) distribution of subsidies among the categories of the objects mentioned that belong to the spheres of operation of the state clients of long-term (federal) targeted programs should be given.

It should be noted that targeted distribution of subsidies must be specified for the objects of capital construction included in long-term (federal) targeted programs without which the implementation and (or) functioning of the objects of capital construction of the state property of the Russian Federation is impossible or which are necessary to construct because of the international liabilities of Russia.

The Decree of the Government of the Russian Federation from 08.08.2009 No 650 “On granting subsidies to the budgets of subjects of the Russian Federation for co-financing of the objects of capital construction of the state property of the subjects to the Russian Federation not included in the federal targeted programs, budget investments for which are made from the budgets of subjects of the Russian Federation , and (or) for granting corresponding subsidies from the budgets of subjects of the Russian Federation to co-finance the objects of the capital construction of municipal property not included in the federal targeted programs, the budget investments for which are made from the local budgets, at the expense of allocations from the federal budget for which the Ministry of the Regional Development of the Russian Federation is the chief superintendant” defines the rate of subsidies given to the budgets of subjects of the Russian Federation in 2009 to co-finance the objects of capital construction of the state property of subjects of the Russian Federation and of municipal property, not included in the federal targeted programs.

The Government of the Russian Federation established the distribution of the budget allocations from the federal budget (for which the Ministry for Regional Development of the Russian Federation is the chief superintendant) to the budgets of subjects of the Russian Federation. The Ministry for regional development of the Russian Federation is commissioned to secure the conclusion of the agreements on granting the subsidies with the supreme executive bodies of the Russian Federation within 30 days.

According to paragraph 1 article 5 of the Federal Law from 21.07.2007 No 185-FZ “On the Fund for assistance to the reforms of housing and communal services” the property of the Funds is formed at the expense of the property contribution of the Russian Federation at the rate of two hundred and forth billion of rubles, as well as from the profits received by the Fund from the placement of temporary surplus funds and other contributions not prohibited by the law. In concordance with this norm of the law it was established by the Decree of the Government of the Russian Federation from 30.07.2009 No 631 “On transferring of the funds of the state corporation – the fund for assistance to the reforms of housing and communal services to the property of the Russian Federation”, that in 2009 the funds of the state corporation – the fund for assistance to the reforms of housing and communal services will be transferred to the property of the Russian Federation at the amount of RUR 65 billion. It should be noted that the dates for transfer of the means of the Fund are established by its supervisory board on the suggestion by its board of directors upon agreement with the Ministry of Finance of the Russian Federation after the board of directors of the Fund has made the corresponding changes to the financial plan of revenues and expenditures of the Fund (budget). The means transferred to the federal budget are registered by the Fund as the decrease of the property contribution of the Russian Federation. ●

FACTORS OF ECONOMIC GROWTH IN 2008 AND IN THE FIRST HALF OF 2009¹

E.Astafieva

The dynamics of oil prices defines the biggest part of the total factor productivity (TFE) and the GDP. On average in the period under consideration excluding the end of 2008 the changes in the price factor defined about 85% of the output growth rates, whereas the technological productivity accounted for 30%. However on the whole over the period under consideration the dynamics of the “technological” component demonstrates the reduction of the decrease rates by 0.5 percentage points on average over the quarter.

According to the data of the Federal State Statistics Service, the year of 2008 was characterized by more than sevenfold drop of quarterly growth of the GDP: whereas in the 1st quarter the increase of the GDP versus the corresponding period of the previous year made 8.7%, in the 4th – it made only 1.2%. In the 1st half of 2009 for the first time over the last 10 years the growth rates of the real GDP went to the field of negative values, making -10.1%², moreover the rates of the decrease grow from quarter to quarter: from -9.8% in the 1st quarter to -10.4% in the 2nd quarter 2009.

The changes of the volume of the GDP and the input of the main factors, excluding the 4th quarter 2008, when the positive rates of the GDP growth were observed against the background of the decrease of labor and capital input characterized by unidirectional dynamics: the increase of the output is accompanied by the growth of the main extensive factors (1st-3rd quarters 2008), and the reduction of the output – by their decrease (1st-2nd quarter 2009).

According to the results of the decomposition (*table 1, fig. 1*) in the period under consideration excluding the end of 2008 the GDP growth rates of the average of 10% were accounted for by the changes in labor input, and it should be noted that the input of this component increased by nearly threefold (from 5.3% in the 1st quarter 2008 to 15.1%³ in the 2nd quarter 2009). The changes in the capital involved in the production process making on average 36% were characterized by a more considerable input to the GDP growth rates. However the main factor defining the dynamics of the output growth rates in this period is TFE, whose changes account for on average 54% of the output growth rates.

Table 1

STRUCTURE OF GDP GROWTH RATES (AS COMPARED WITH THE CORRESPONDING PERIOD OF THE PREVIOUS YEAR)

	I quarter 2008	II quarter 2008	III quarter 2008	IV quarter 2008	I quarter 2009	II quarter 2009
Growth rates						
GDP	8.70	7.50	6.00	1.20	-9.80	-10.40

1 The results of the decomposition of the growth of the output index (GDP) in 2008-the first half of 2009, obtained as in concordance with the method, described in IET's work (“factors of Economic Growth”, series of Scientific Works, No 70, IET, Moscow, 2003) is presented in this section. The basis of the decomposition is the breakdown of the economic growth into extensive and intensive components, which allows estimating the quality of the growth and forecasting of forthcoming trends of the economic growth.

2 The estimation made by the Ministry of Economic Development of the Russian Federation

3 There being no data on changes in the worked hours, the estimation of the input of the input of labor in the GDP growth rates in the 1st half of 2009 is somewhat understated.

Table 1 cont'd

	I quarter 2008	II quarter 2008	III quarter 2008	IV quarter 2008	I quarter 2009	II quarter 2009
I. Input of factors	4.76	3.13	4.85	-0.70	-2.51	-2.83
I.1 Labor	0.46	0.32	0.59	-1.05	-1.37	-1.57
Employment	0.35	0.53	0.30	-0.26	-1.37	-1.57
Hours of work	0.11	-0.21	0.29	-0.79	-	-
I.2 Capital	4.30	2.81	4.27	0.35	-1.14	-1.25
Fixed assets	1.51	1.61	1.81	1.70	1.33	1.26
Extent of facilities load	2.80	1.20	2.46	-1.35	-2.47	-2.51
II. TFE	3.94	4.37	1.15	1.90	-7.29	-7.57
As percentage of the GDP growth rates						
GDP	100.0	100.0	100.0	100.0	100.0	100.0
I. Input of factors	54.7	41.7	80.9	-58.6	25.6	27.2
I.1 Labor	5.3	4.2	9.8	-87.6	14.0	15.1
Employment	4.0	7.1	4.9	-21.6	14.0	15.1
Hours of work	1.3	-2.8	4.9	-66.0	-	-
I.2 Capital	49.4	37.5	71.1	29.0	11.6	12.1
Fixed assets	17.3	21.5	30.1	141.3	-13.6	-12.1
Extent of facilities load	32.1	16.0	41.0	-112.4	25.2	24.1
II. TFE	45.3	58.3	19.1	158.6	74.4	72.8

In the first half of 2008 the most considerable component of labor input that defined its contribution in GDP growth rates was the changes in the labor reserves, that is in the number of the employed. The negative trends at the labor market connected with the developing financial crisis emerged in the 4th quarter 2008 which was characterized by the reduction in the number of the employed by 0.6% and became more intensive in the 1st half of 2009: the value of the figure was -2.4% in the 1st quarter and -2.8% in the 2nd quarter. The negative growth rates of the number of the employed are mainly accounted for by the decrease in the proportion of the employed population in the number of the economically active population, the proportion of the able-bodied population in the total number of the population and the proportion of the economically active population in the number of the able-bodied population being nearly constant.

The analysis of the change in the structure of labor input as a response to the spread of the crisis phenomena testifies that it is the manipulation with the length of a working day that is the main instrument for the adaptation of the labor market to the changes in the labor situation. In the 3rd quarter 2008 the growth rates of the labor and the intensity of its use became equal, and in the 4th quarter the input of of the hours worked by the employed in the growth rates of the GDP increased the input accounted fro by the changes in the number of the employed by nearly three times. There are no data on the average length of the working hours in the 1st half of 2009, however, taking into account the fact that the number of part-time workers increased by nearly one and a half times it can be assumed that the specification of the decomposition for the first half of 2009 taking into account the number of working hours will result in the negative input of labor in GDP growth rates.

Starting with 1999 the capital input has been the more significant factor for the GDO growth rates than labor input. This situation has persisted till the 3rd quarter 2008 however if in the 1st quarter 2008 the input of capital exceeded labor input by more than 9 times, in the 2nd quarter the excess was only twofold. The crisis affected the rates of the input of capital in the same way as the labor input, the former also transferring to the

field of negative values, though in this case the rates of the capital input it happened in the 1st quarter 2009 and not at the end of 2008.

According to the method of the estimation¹, the dynamics of the reserves of capital is defined by the changes in the volume of investments in fixed assets, whose growth rates are in the period under consideration decreased on average by 8.7 percentage points quarterly (from 23.6% in the 1st quarter 2008 to 20.0% in the 2nd quarter 2009). As a result, the reduction of the funds directed for renovation and recovery of the fixed assets taking into account a considerable extent of their wear and tear which reached the level of 46.3% by the beginning of 2008 has resulted in the quarterly reduction in the growth rates of the stocks of capital of 0.01 percentage points.

In the period under consideration the changes in the capital input are mainly accounted for by the changes in the extent of its load, and it should be noted that whereas in the 1st quarter 2008 the input of this component exceeded the input of stocks of the capital by nearly 2 times, starting with 2009 the volatility of the intensity of the capital use defines the direction of the changes in capital input.

The prevailing factor in the GDP growth rates in the period under consideration is the total factor efficiency: in the first three quarters of 2008 and in the first half of 2009 it accounts for on average 54% of the production growth rates, and in the 4th quarter 2008 it is the main factor defining the positive rates of the GDP growth. It should be noted that the same as all the considered components the dynamics of the TFE demonstrates the decrease in the growth rates: on average over the quarter the reduction of the efficiency growth rates made 2.3 percentage points (2.6 percentage points in concordance with the linear trend²).

The obtained estimation for the TFE should be regarded as purely “technological” component, characterizing the change in efficiency of factors. It reflects the effect of the indices that have not been taken into account when estimating the main costs, as well as the shifts connected with the method for estimation. Thus, the use of cost indices of output and capital can result in the shift of the “physical” estimation of TFE due to unevenness of the dynamics of price, GDP and the main factors³. At the same time, the conditions of the Russian economic system are characterized by this very unevenness that define high volatility of prices for oil, so that in the short term period the factors of the economic situation may have a more considerable effect on the growth than the technological ones.

In concordance with the obtained results⁴, the dynamics of prices for oil (with the exception of the 4th quarter 2008) define the biggest part of TFE and GDP growth rates. On average in the period under consideration, excluding the end of 2008, the changes of the

1 There being no quarter to quarter statistics, the estimation of the growth of the fixed assets is based on the supposition that the coefficient of the retirement of fixed assets is constant and so is the proportion of the investments directed for their renewal. It should be noted that the estimation received in this way can be shifted since it does not take into account the time lag between the moment of the receipt of the investments and the moment of their use.

2 The estimations of the growth rates in concordance with the linear trend are considered to decrease the dependence of the results of the estimation from the choice of the initial and final year of the period under consideration.

3 The “value” estimation of the efficiency coincides with the “physical” in case the economy is in long-term equilibrium and there is perfect competition or, in other words, when all the possible exogenous shocks are taken into account in the current equilibrium of the system.

4 The apportionment of the situational component in the structure of the TFE and the conduction of further decomposition of the production growth rates is based on the existing statistical dependence between the TFE growth rates and the growth rates of world oil prices, which is estimated with the help of regression on the basis of the annual data in the period from 1993 to 2008. The “final residue” obtained in the end, cleared from the influence of the changes at the world markets of raw materials is a more correct characteristic for technological efficiency, that is the intensive component of the growth.

factor of price defined about 85% of the production growth rates, whereas the technological component (“final residue”) - -30%. The changes in the growth rates of the technological component which were obtained as a result of apportioning of the price situation at the world markets of raw materials as a separate factor are somewhat different from the TFE dynamics. The growth rates of the “residue” are negative not only in the first half of 2009 but also in January-September 2008. However on the whole over the period under consideration the dynamics of the technological component demonstrates the decrease of the reduction rates by the average of 0.5 percentage points by quarter (by 0.9 percentage points in concordance with the linear trend).