

RUSSIAN ECONOMY: TRENDS AND PERSPECTIVES
November 2002

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The State of the Federal Budget

According to the preliminary estimates of the Finance Ministry, the federal budget in January through September of 2002 was executed as follows: revenues – Rb. 1799.3 billion, expenditures (actual financing) – Rb. 1721.8 billion.

Table 1

The monthly execution of the federal budget of the Russian Federation (in % of GDP, in comparable prices).

	XII'01	I'02	II'02	III'02	IV'02	V'02	VI'02	VII'02	VIII'02	IX'02
Revenues										
Corporate profit tax	2,4%	1,4%	1,4%	1,5%	1,9%	1,9%	1,7%	1,7%	1,7%	1,6%
Personal income tax	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
VAT, special tax and excises	0,0%	4,9%	4,4%	4,0%	3,9%	3,6%	3,5%	3,5%	3,3%	3,2%
Tax on foreign trade and foreign trade operations	9,4%	9,3%	9,1%	9,3%	9,3%	9,3%	9,3%	9,3%	9,1%	9,0%
Other taxes, duties and payments	7,1%	6,9%	6,4%	6,8%	6,9%	7,0%	7,0%	7,0%	7,0%	6,9%
Total- taxes and charges	2,2%	2,4%	2,6%	2,5%	2,4%	2,3%	2,3%	2,2%	2,1%	2,0%
Non- tax revenues	3,7%	3,2%	3,3%	3,2%	3,0%	2,9%	2,9%	2,9%	2,8%	2,8%
Revenues, total	0,6%	9,7%	9,1%	8,7%	8,7%	8,4%	1,8%	2,0%	2,0%	2,0%
Expenditure	16,2%	20,4%	19,6%	19,6%	19,9%	19,6%	19,3%	19,4%	18,9%	18,5%
Public administration	1,4%	2,1%	1,6%	1,4%	1,3%	1,2%	1,3%	1,4%	1,4%	1,4%
National defense	17,6%	22,4%	21,2%	20,9%	21,2%	20,9%	20,6%	20,9%	20,4%	20,0%
International activities										
Judicial power	0,5%	0,1%	0,2%	0,3%	0,4%	0,4%	0,4%	0,4%	0,4%	0,4%
Law enforcement and security activities	2,7%	1,0%	1,5%	1,9%	2,3%	2,4%	2,5%	2,5%	2,5%	2,4%
Fundamental research	0,3%	0,4%	0,4%	0,4%	0,4%	0,4%	0,4%	0,4%	0,3%	0,3%
Services provided for the national economy	0,1%	0,0%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%
Social services	1,6%	0,6%	0,9%	1,0%	1,2%	1,2%	1,3%	1,4%	1,4%	1,4%
Servicing of public debt	0,3%	0,0%	0,1%	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%
Other expenditure	1,3%	0,1%	0,3%	0,4%	0,5%	0,6%	0,7%	0,8%	0,8%	0,8%
Expenditure, total	2,3%	3,7%	4,8%	4,8%	5,3%	5,2%	5,2%	5,2%	5,1%	4,9%
Loans, redemption exclusive	2,6%	2,0%	3,4%	3,4%	2,6%	2,5%	2,4%	2,3%	2,4%	2,4%
Expenditure and loans, redemption exclusive	3,0%	2,9%	3,3%	3,6%	3,9%	4,0%	4,0%	4,0%	3,9%	3,8%
Budget deficit (-)	14,7%	10,9%	15,0%	16,1%	16,9%	17,1%	17,2%	17,2%	17,1%	16,9%
Domestic financing	2,9%	11,5%	6,2%	4,8%	4,3%	3,8%	3,4%	3,7%	3,3%	3,1%
Other taxes, duties and payments	-0,1%	-11,2%	-4,6%	-2,7%	-2,0%	-1,8%	-1,6%	-1,8%	-1,3%	-1,2%
Total- taxes and charges	-2,8%	-0,4%	-1,6%	-2,1%	-2,3%	-1,9%	-1,8%	-1,9%	-1,9%	-1,9%
Non- tax revenues	-2,9%	-11,5%	-6,2%	-4,8%	-4,3%	-3,8%	-3,4%	-3,7%	-3,3%	-3,1%

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

Table 2

The monthly execution of the federal budget of the Russian Federation (in % GDP, actual financing).

	I'02	II'02	III'02	IV'02	V'02	VI'02	VII'02	VIII'02	IX'02	X'02
Total	22,2%	21,0%	20,9%	21,2%	20,8%	20,5%	20,5%	20,5%	20,0%	20,2%
Public administration	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%	0,5%
National defense	1,7%	2,4%	2,4%	2,7%	2,7%	2,7%	2,7%	2,7%	2,6%	2,7%
International activities	0,4%	0,2%	0,4%	0,5%	0,4%	0,4%	0,4%	0,3%	0,3%	0,4%
Judicial power	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%	0,2%
Law enforcement and security activities	1,6%	1,4%	1,4%	1,5%	1,5%	1,6%	1,9%	1,6%	1,6%	1,8%
Fundamental research	0,3%	0,3%	0,2%	0,3%	0,3%	0,3%	0,2%	0,3%	0,3%	0,3%
Services provided for the national economy	0,3%	0,6%	0,8%	0,9%	1,0%	1,0%	1,1%	1,1%	1,0%	1,5%
Social services	5,0%	5,7%	5,3%	5,9%	5,7%	5,5%	5,6%	5,4%	5,2%	5,8%
Servicing of public debt	1,9%	3,4%	3,4%	2,7%	2,5%	2,4%	2,6%	2,4%	2,4%	2,2%
Other expenditure	3,5%	4,0%	3,9%	4,0%	4,6%	4,2%	4,0%	4,0%	4,0%	4,0%
Total expenditure	15,5%	18,7%	18,6%	19,1%	19,4%	18,9%	19,1%	18,6%	18,2%	19,3%
Профицит (+) / дефицит (-)	6,8%	2,3%	2,3%	2,1%	1,4%	1,6%	1,4%	1,8%	1,7%	0,9%

The data on the cash execution of the federal budget up to September of 2002 are presented in Table 1¹, the data on fulfilled funding up to October of 2002 are presented in Table 2. As of October 1, 2002, the revenues of the federal budget accounted for 20.0 % of GDP, including tax revenues at 18.5 %, while expenditures made 16.9 % of GDP (18.2 % of GDP in terms of fulfilled funding²), including non-interest ones – 14.5 % of GDP (15.8 % of GDP in terms of fulfilled funding). The level of budget surplus accounted for 3.1 % of GDP (1.7 % of GDP in terms of fulfilled funding).

The indicators of revenues collected in January through September of 2002 somewhat decreased as compared with the figures registered in January through August. The tax revenues in January through August of 2002 made 15.3 % of GDP (without the single social tax).

The expenditures for the servicing of the public debt in January through September of 2002 made 2.4 % of GDP. As concerns the fulfilled funding, the expenditures in the first nine months of 2002 made 19.3 % of GDP.

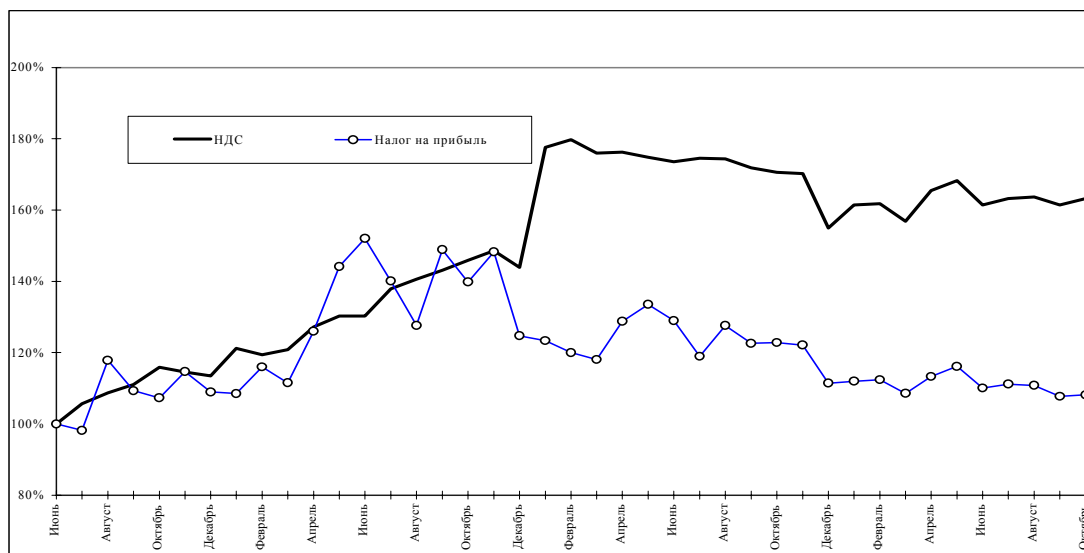
As of November 1, according to the preliminary estimates, the balances of accounts on accounting the federal budget funds (without regard to the funds accumulated on personal accounts of recipients of budget funds) grew up by Rb. 40.1 bln. since the beginning of the year.

Table 3

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

1999											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
100,0%	115,1%	122,0%	122,1%	104,5%	112,9%	127,0%	127,5%	124,3%	141,4%	160,8%	213,1%
2000											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
149,3%	160,5%	181,3%	205,8%	233,1%	186,9%	181,0%	186,4%	173,1%	181,1%	201,7%	254,1%
2001											
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
204,4%	198,4%	227,6%	267,5%	252,2%	233,3%	231,9%	235,6%	219,4%	237,5%	247,3%	360,6%
2002											
I	II	III	IV	V	VI	VII	VIII	IX	X		
218,7%	187,1%	234,8%	277,8%	239,6%	218,0%	284,4%	246,5%	254,8%	298,9%		

Figure 1. Rate of growth of the real tax arrears to the federal budget (in % to June of 1999)



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

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

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

The dynamics of actual tax debts to the federal budget is presented in Figure 1⁴. In September, no significant changes were registered.

Table 4

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

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

* Без учета ECH

Table 5.

The estimate of tax revenues

	Всего налоговых поступлений в консолидированный бюджет РФ	Всего поступлений налога на прибыль в консолидированный бюджет РФ	Всего поступлений НДС	Всего поступлений подоходного налога в консолидированный бюджет РФ	Всего налоговых поступлений в федеральный бюджет РФ	Всего поступлений налога на прибыль в федеральный бюджет РФ
ARIMA						
Октябрь	24,5%	4,2%	6,8%	3,1%	15,3%	1,5%
Ноябрь	24,9%	4,3%	6,9%	3,1%	15,4%	1,6%
Декабрь	25,4%	4,2%	7,3%	3,3%	15,8%	1,6%
Январь	25,2%	4,2%	7,3%	3,2%	15,7%	1,5%
REM						
Октябрь	24,7%	4,2%	6,8%	3,1%	15,5%	1,6%
Ноябрь	24,5%	4,2%	6,7%	3,1%	15,7%	1,5%
Декабрь	24,8%	4,2%	6,8%	3,1%	15,7%	1,5%
Январь	25,5%	4,1%	7,1%	3,2%	16,3%	1,5%

4 Since 2001 the form of the MTC's presentation of the respective statistical data has been changed, and the data on debts to the federal budget across all the taxes are no longer available. Since January of 2002 the practice of balancing the data on the arrears against the amount of tax surplus has been ceased. In this relation the figure presents the data on the gross unbalanced tax arrears for comparability purposes.

The level of tax revenues of the consolidated budget in January through September of 2002 somewhat decreased in comparison to the indicators observed in the period from January to August. The surplus of the consolidated budget was by 0.2 % of GDP below the level registered in the preceding year.

The estimate of tax revenues of the consolidated and federal budgets is presented in the table⁵. The estimate was revised as compared to the indicators presented in the preceding bulletin basing on the new data on the execution of the consolidated and federal budgets.

S. Batkibekov

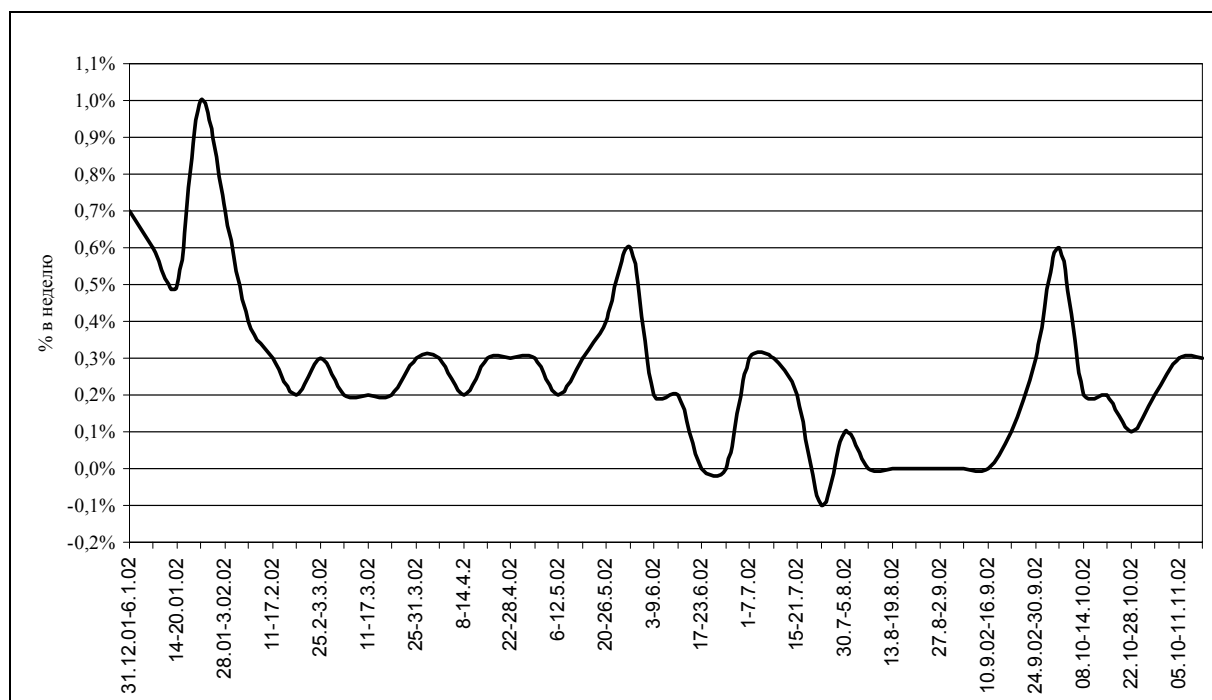
Monetary Policy

According to the State Committee for Statistics of the RF, in October the consumer price index amounted to 101.1 percent. The seasonal decline in prices for fruits and vegetables is practically over: the index for this commodity group was 98.9 percent in October.

The service price index grew 2.5 percent. The greatest rise in this group was observed in the public transportation sector: prices grew 4.6 percent. The increase occurred primarily owing to the municipal transport. Prices for housing and communal services are still growing: the increase amounts to 2.5 percent, or 43.7 percent as compared to December 2001. Prices for non-foods grew 0.9 percent.

In the course of the first ten months of year 2002 inflation in the Russian Federation (measured by the CPI) was 11.5 percent (15.2 percent in the respective period of 2001). According to preliminary estimates, in November the increase in consumer prices was 1.2 - 1.3 percent. In this connection it is quite probable that the annualized inflation would slightly exceed the upper limit of the 12-14 percent range set by the Government.

Figure 1. Consumer Price Index in 2002



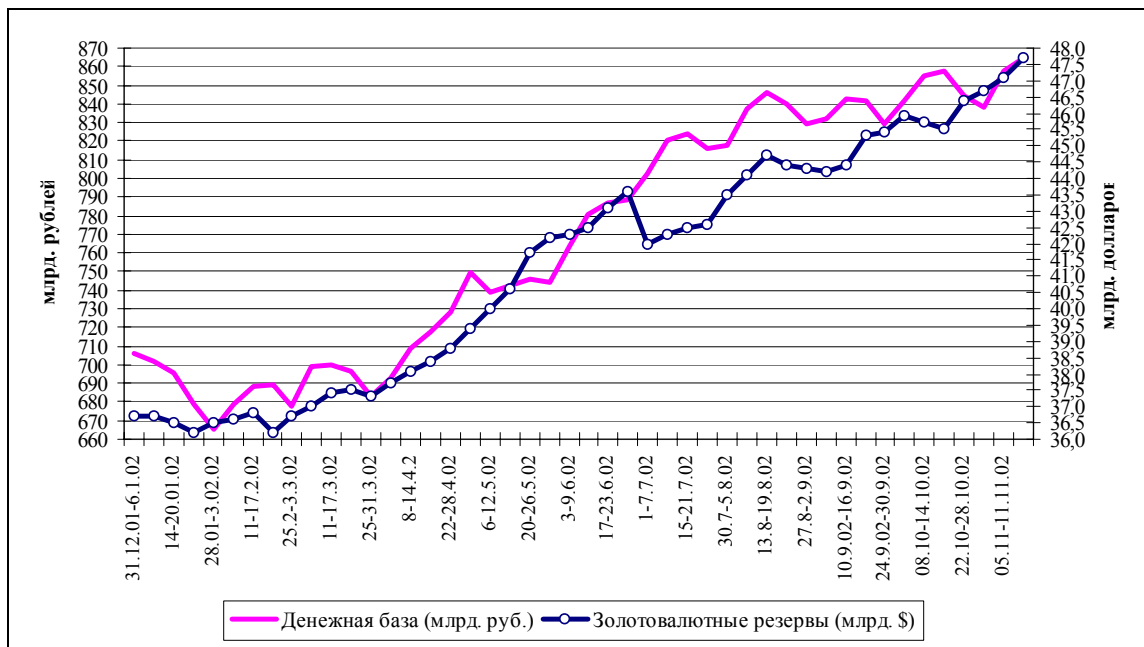
In November the gold and currency reserves continued to grow, reaching another historic high of US\$ 47.7 billion on 22 November 2002 (as opposed to US\$ 46.7 billion on 01 November 2002). The month of November cannot be regarded as strenuous in respect to external debt payments: the amount of the scheduled payments was US\$ 536.9 billion.

The guidelines of the currency legislation liberalization were more or less clarified. The draft law, adopted as a whole on 14 November, stipulates for mandatory repatriation of currency earnings within a period of up to 180 days. It also allows the Central Bank to impose certain limitations on capital transactions: the so-called account operation procedure (a list of permitted transactions) and mandatory reservation of up to 20 percent of the transaction amount for up to one year in case of importing currency and of up to 100 percent in

⁵ For the description of models see the preceding bulletins.

case of exporting it. The CB RF is also assigned a right to demand that residents pass a preliminary registration when opening currency accounts abroad. The upper limit of the norm for the mandatory currency earnings sale was established at the level of 30 percent. It is assumed that all the limitations, with the exception of the 100-percent repatriation, will be canceled starting with 01 January 2007.

Figure 2. Dynamics of the Monetary Base and Gold and Currency Reserves in 2002



D. Levchenko

Financial Markets

The Market for Government Securities

In November 2002 the trend towards a decrease in yields that was observed in the Russian market for foreign debt during previous months, continued. The main determining factor was the expected decision by the US Federal Reserve to lower the refinance rates, which in a natural way influenced the global level of interest rates. It is worth reminding that on 06 November 2002 the federal funds rate was lowered by 50 basis points (0.5 percent) down to 1.25 percent. Argentina's default on payments to the World Bank did not have any serious impact on the markets.

The announcement by the Russian Ministry of Finance of a restructuring of the former USSR's commercial debt worth US\$ 1.1 billion into Eurobonds with maturities in 2010 and 2030 was the most important occurrence in the Russian securities market.

The decrease in yields did not include short-term securities. On considering the trend dynamics, one could see that medium- and long-term securities regarded as an object of short-term investments brought impressive earnings to investors in November.

In November, the annualized yield of securities in the market of domestic debt was 14.1 percent. Based on preliminary data, the estimated turnover was circa RUR 13 billion, which is slightly lower than last month's figures (RUR 18.7 billion).

Figure 1. Yield to Maturity of Minfin Bonds in May to November 2002.

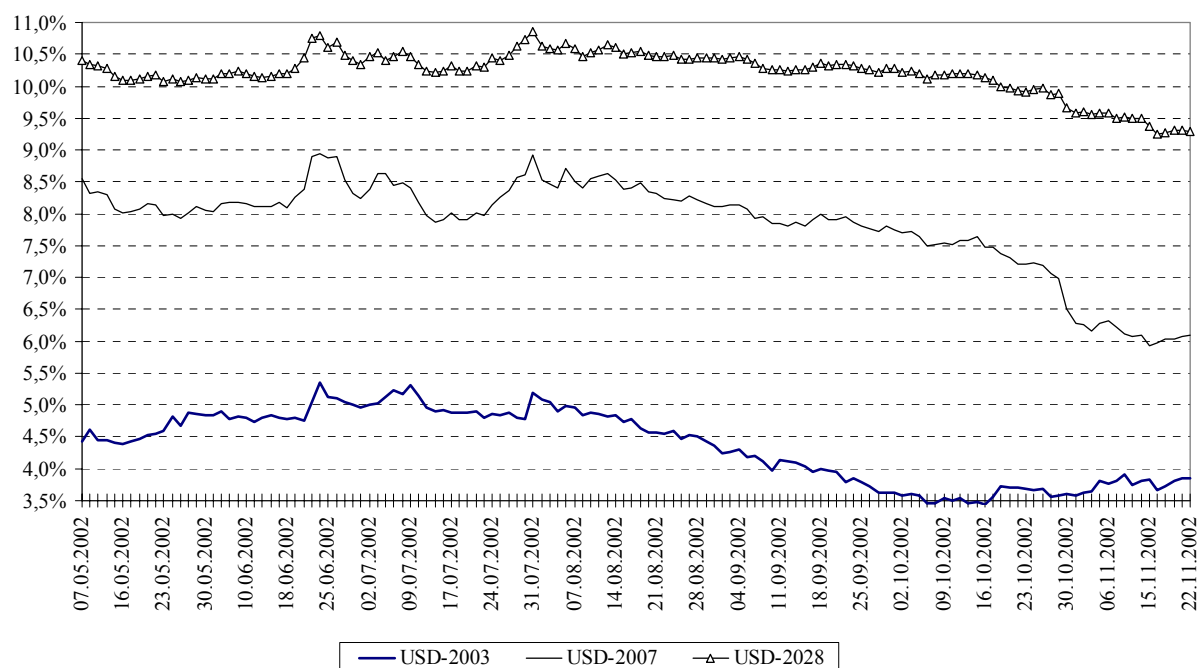
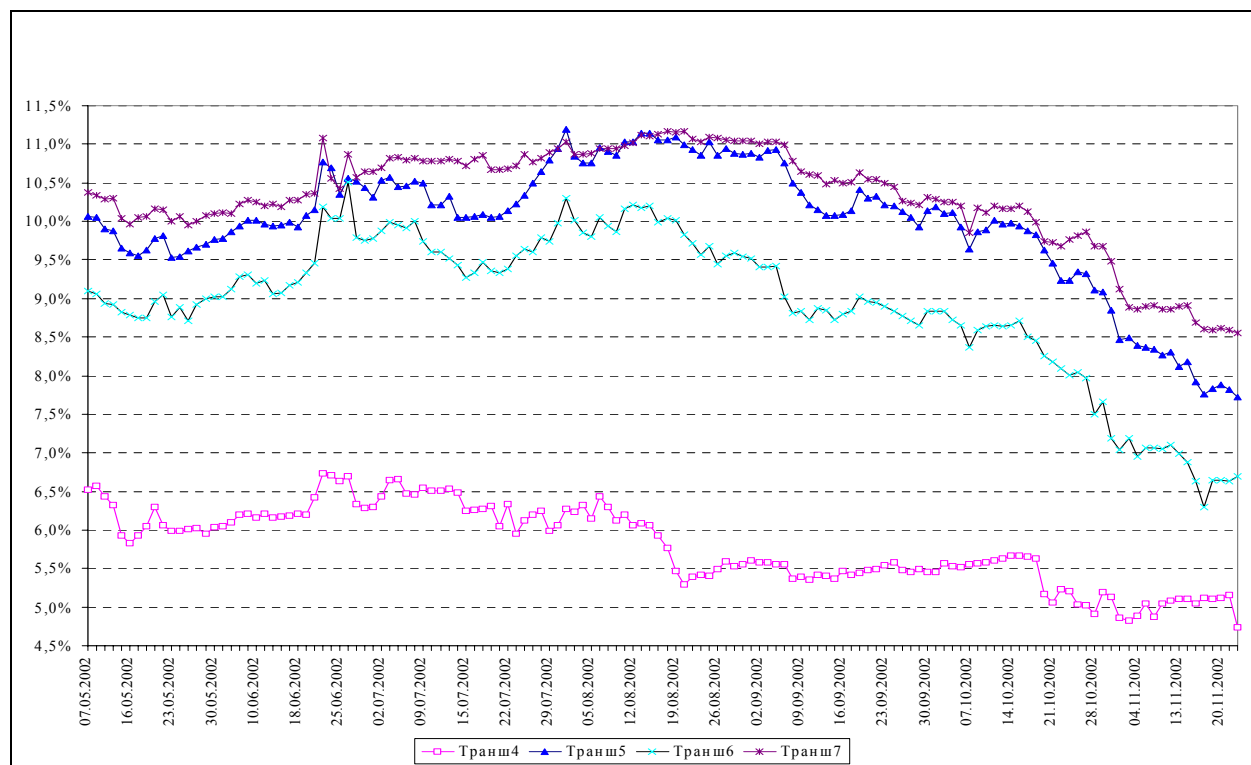


Figure 2 Yield to Maturity of Russian Eurobonds with Maturities in 2003, 2007 and 2008 in May to November 2002



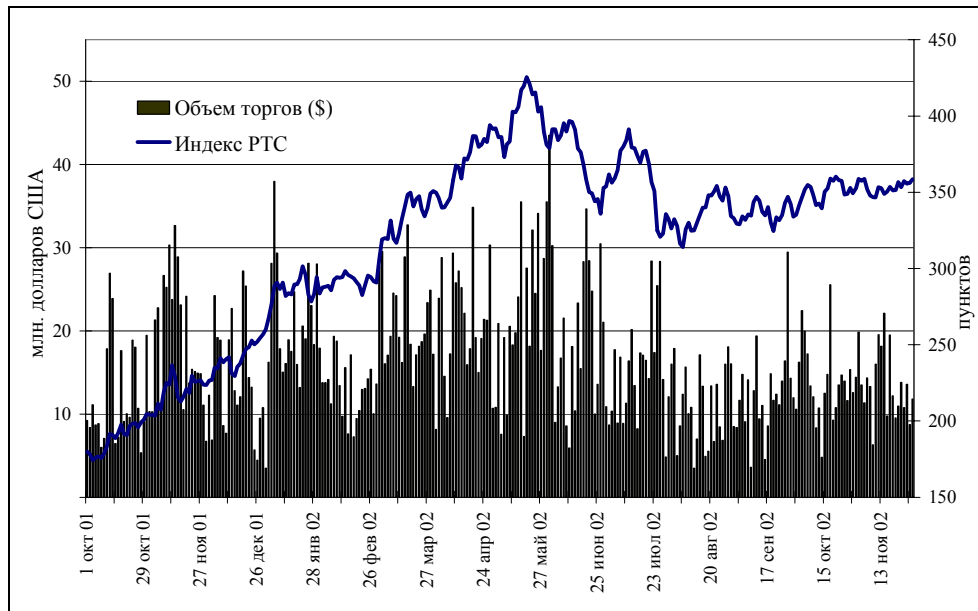
The Market for Corporate Securities

In November the Russian stock market was fairly quiet. On the one hand, corporate news resulted in positive changes in the prices of Russian securities; on the other hand, the external conditions remained adverse. The default by the Argentine government on the debt to the World Bank made investors treat the market of

the developing economies with greater caution. Despite the dramatic events in South America and if there are no severe shocks, in December one may expect a "New-Year rally" in the Russian market.

The Stock Market

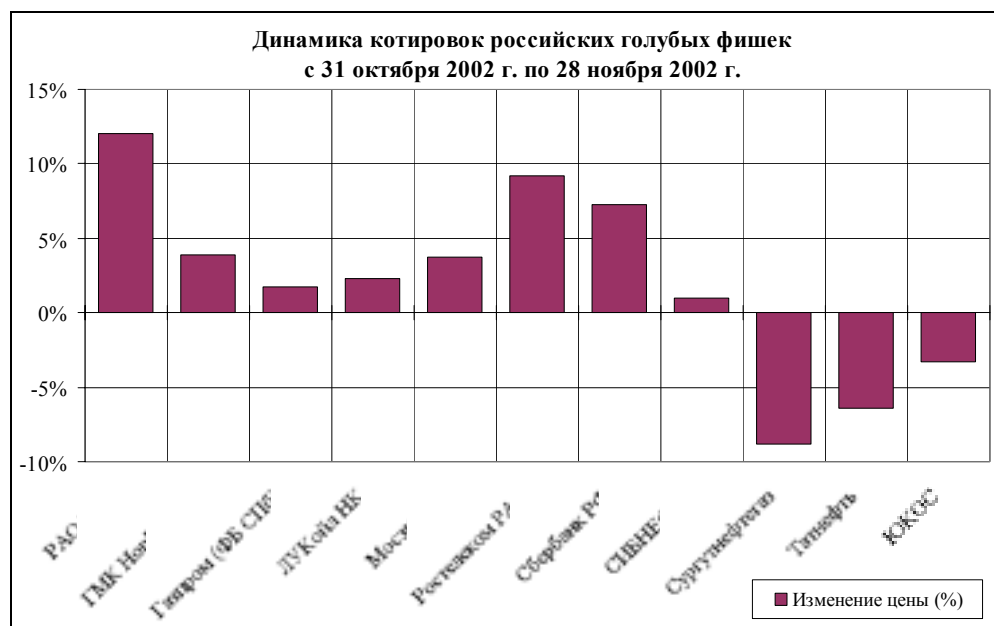
Figure 3.



In November the RTS index remained practically unchanged (-0.047 percent), reaching 358.48 points on 28 November. The trade volume reached US\$ 255 million, which is somewhat lower than in the previous month; the average daily volume was US\$ 13.4 million.

One could distinguish three periods in the RTS index dynamics. The index decreased from the beginning of the month till 11 November, reaching the lowest monthly mark of 346.52 points. This trend in the behavior of the stock market indicator was brought about by the fact that many market participants chose to close their "long" positions before the holidays because during the holidays significant events could occur on international markets (i.e., a change in the interest rates). Thereafter, the stock market indicator hovered at the level of 350 points; from 20 till 28 November the index regained the positions it had lost earlier during the month, reaching the level of late October. The lowest trade volume was observed on 10 November (US\$ 6.3 million), the greatest volume was observed on 14 November (US\$ 22 million).

Figure 4. The dynamics of russian blue chip quotations from 31 october till 28 november 2002



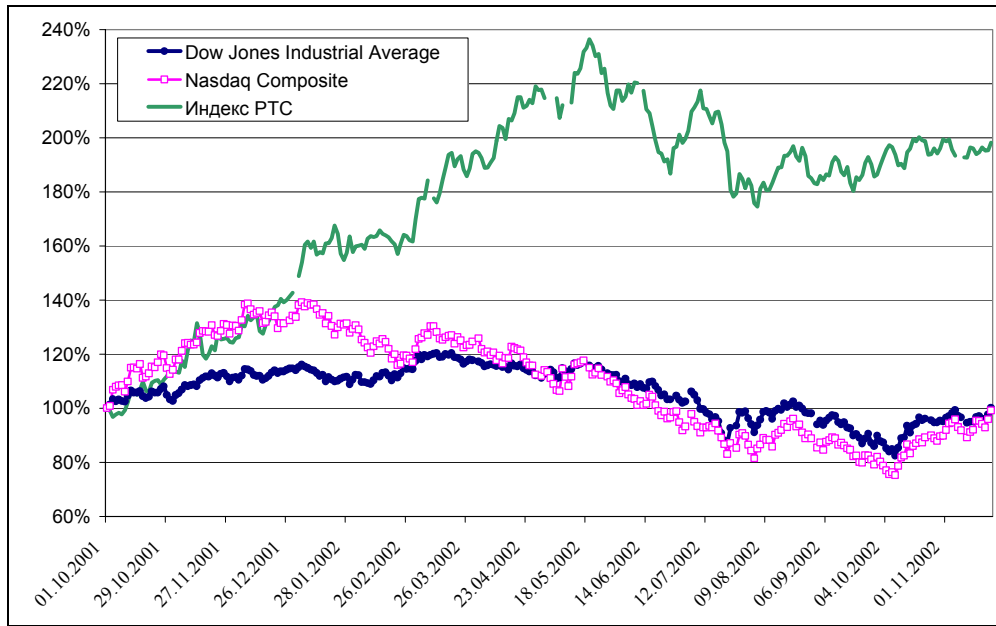
Securities of energy and telecom companies were in especially popular demand with investors in November. As 28 November, the shares of RAO UES were leading in growth (12.05 percent), followed by the securities of Rostelecom (9.18 percent), Sberbank (7.28 percent) and MMC Norilsk Nickel (3.88 percent). Lesser growth was demonstrated by the shares of Mosenergo (3.73 percent), Lukoil (2.32 percent), Gazprom (1.75 percent) and Sibneft (1.01 percent). The securities of large Russian oil companies were falling in price: Yukos, -3.30 percent; Tatneft: -6.41 percent, and Surgutneftegas: -8.82 percent. The distressing trends of the Russian oil industry resulted from a drop in world oil prices. Lukoil demonstrated greater growth results as compared with other oil companies due to the sale of a part of its Caspian assets (which include a 10 percent block of shares in the Azeri-Chirag-Gunashli Project). This transaction could bring circa US\$ 1 per share to Lukoil's shareholders; it is also a significant step towards restructuring the company. A rise in quotations of Norilsk Nickel and Rostelecom was also brought about by operations with assets. An increase in financial indicators (as compared with plan figures) resulted in growing investor interest towards the shares of RAO UES and Sberbank (see Corporate News). Ordinary shares of RAO UES accounted for the greatest proportion (29.64 percent) in the total volume of RTS turnover during the period under review (as compared to 29.22 percent in the previous month). The proportion of ordinary Lukoil shares fell to 17.97 percent (23.31 percent); Surgutneftegas: 13.12 percent (11.03 percent); Yukos: 10.51 percent (12.02 percent); the proportion of MMC Norilsk Nickel grew by more than 30 percent, reaching 6.31 percent (4.68 percent). The aggregate proportion of five most liquid shares in the overall RTS turnover somewhat diminished, reaching 77.55 percent (October: 80.79 percent). During the period from 01 till 28 November 2002 the volume of trade in Gazprom shares through RTS terminals grew 53 percent in comparison to the previous period, reaching US\$ 83.6 million (circa 103.5 million shares); a total of 11.8 thousand deals were concluded with the securities of the gas concern.

In November the list of the top five Russian companies by capitalization remained unchanged (RTS data): Yukos, US\$ 20.2 billion; Gazprom, US\$ 19.2 billion; Lukoil, US\$ 14.2 billion; Surgutneftegas, US\$ 11.8 billion; Sibneft, US\$ 9.5 billion

The Market for Term Contracts

The FORTS market reached new frontiers in November. On 26 November the trade volume was RUR 795.47 million (188.5 thousand contracts, 3,785 deals), which is the highest value in the entire history of this market. On the whole, during the period from 01 till 28 November the trade volume in the market for term contracts increased more than 20 percent as compared to last year's respective period, reaching RUR 9.69 billion (50.7 thousand deals, 2.34 million contracts). Futures contracts accounted for RUR 9.47 billion (48.7 thousand deals, 2.3 million contracts) in this amount. The average daily turnover was RUR 510 million, the number of deals: 2,670.

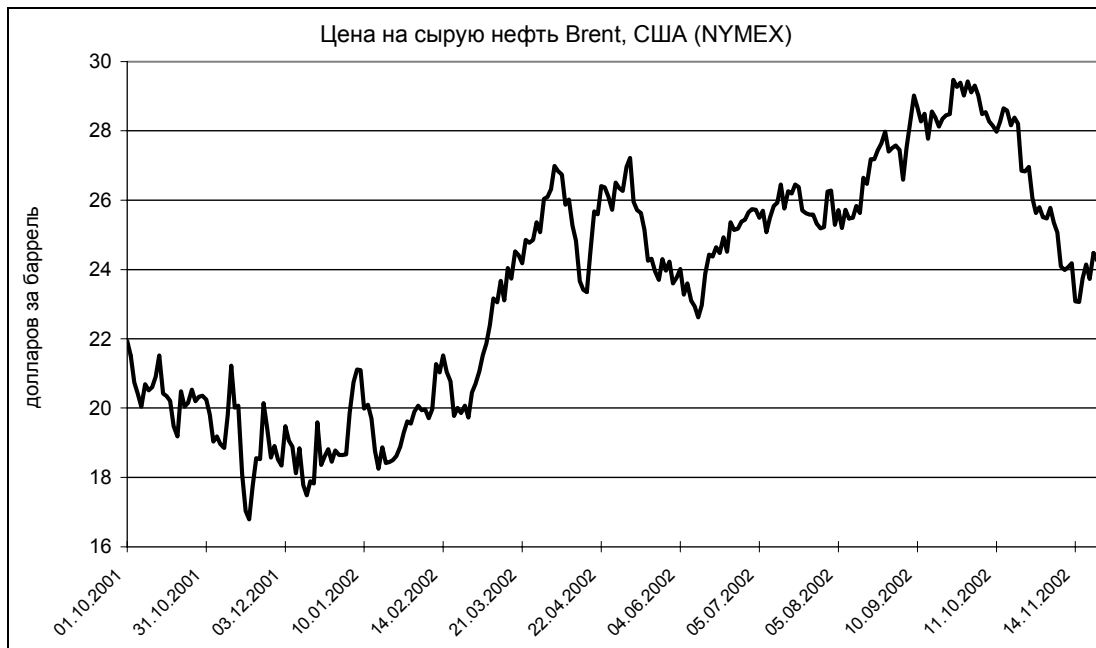
International News



The Federal Open Market Committee of the US Federal Reserve System announced a reduction of the re-finance rate by 50 basis points (the forecast was 25 basis points). Thus the rate reached 1.25 percent, which is the lowest value in 40 years. On the one hand, the management of the US Fed admitted that its previous measures aimed at helping the economy out of the recession were not efficient enough; on the other hand, it demonstrated it was bound to try and take the economy out of the crisis in any possible way. The US stock market reacted by increasing stock indicators because a lower re-finance rate would lead to greater consumption and investment volumes. US indices were also influenced by good reports presented by HP and General Electric. As at 22 November the DJIA index grew almost 5 percent and NASDAQ more than 10 percent.

After five consequent reductions, in October the Leading Index calculated by the Conference Board remained unchanged.

Figure 5. Price for brent crude oil, usa (nymex)



Constant transgressions by OPEC countries of the established quotas and a peaceful solution of the Iraq issue resulted in a significant reduction (down to the June level) of prices for the black gold. The minimum

price of the Brent mix (US\$ 23.06 per barrel) was observed on 15 November (-9.5 percent as compared to 31 October). Thereafter the prices grew again, and as at 22 November the total reduction of the price of a barrel was 4.8 percent.

According to the RF Ministry of Energy, oil production rates in Russia are growing. During the first eight months of the current year production grew 8.6 percent, during the first nine months production grew 8.7 percent and in the course of ten months the growth rate reached 8.8 percent.

Corporate News

OA0 North-West Telecom

Standard & Poors upgraded the operator's Corporate Governance Score from 5.0 to 5.6. The agency's analysts point out that the recent changes in the Board of Directors should lead to a development of more efficient control and management systems in future. However, at the present time, due to increased influence exerted by a single majority shareholder and its dominating role in the decision-making process, and also due to underdeveloped independent control mechanisms, the company's management process has certain drawbacks.

OA0 Surgutneftegas

The US GAAP report for the previous year published by the oil company demonstrates a deterioration of the company's main financial indicators: revenues fell to US\$ 5.23 billion (-9 percent), EBITDA fell down to US\$ 2.57 billion (-26 percent) and the adjusted net profit down to US\$ 1.57 billion (-16 percent).

OA0 Sberbank

Sberbank presented its mandatory financial reports for Quarter 3 of year 2002. Net profit grew 95 percent (as compared to the previous year) up to RUR 28.7 billion. Besides, according to Sberbank officials, the profit in 2002 may reach RUR 30 billion, which exceeds the earlier estimate of RUR 27.2 billion, and the dividends may increase twofold.

OA0 RAO UES of Russia

RAO UES also published its current year results in November. Its net profit grew up to RUR 39.98 billion during the first 9 months of the current year, and the IAS net profits in the first six months increased to RUR 17.8 billion. According to a statement by V. Sinyugin, Deputy Chairman of the Board, which he made at a meeting with investors in Boston, the energy holding is also planning to increase the dividends approximately twofold.

OA0 MMC Norilsk Nickel

MMC Norilsk Nickel acquired 100 percent of shares of Russia's largest gold production company Polyus. In 2002 Polyus is going to produce 25 tons of gold, which would bring it circa US\$ 250 in revenues and circa US\$ 75 in profit. The MMC paid US\$ 226 million in cash for the 100 percent of Polyus's shares.

In addition to purchasing domestic assets, Norilsk Nickel plays actively abroad: the MMC is acquiring for US\$ 341 million a controlling block of shares of Stillwater Mining Company, the only US producer of platinum group metals. US\$ 100 million will be paid in cash and the remaining US\$ 241 million in the form of 876,000 ounces of palladium.

OA0 Rostelecom

The telecom operator published its financial report for the 9 months of the current year. The revenues fell 1 percent down to US\$ 486.2 million, EBITDA grew 3 percent to US\$ 315 million. Owing to a sale of 50 percent of Sovintel shares, net profits grew more than half up to US\$ 156.9 million

Table 1

Dynamics of Foreign Stock Indexes

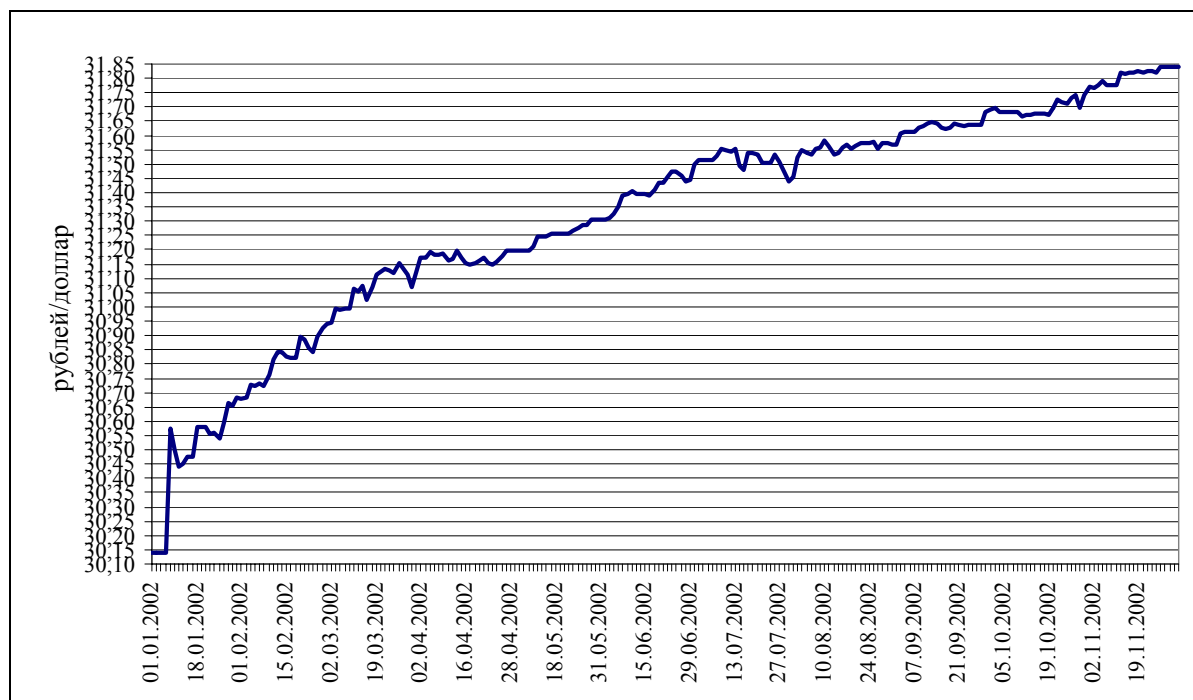
As of 23 October 2002	Value	Change During the Month (%)	Change Since the Beginning of the Year
RTS (Russia)	353.24	-1.51 %	35.84%
Dow Jones Industrial Average (USA)	8804.84	4.86%	-13.14%
NASDAQ Composite (USA)	1486.74	10.45%	-26.09%
S&P 500 (USA)	930.55	5.06%	-19.85%
FTSE 100 (UK)	4175.2	3.35%	-20.36%
DAX-30 (Germany)	3320.88	5.33%	-35.64%

As of 23 October 2002	Value	Change During the Month (%)	Change Since the Beginning of the Year
CAC-40 (France)	3305.78	4.94%	-28.52%
Swiss Market (Switzerland)	5160.8	4.28%	-19.59%
Nikkei-225 (Japan)	8772.56	1.53%	-16.79%
Bovespa (Brazil)	10289	1.19%	-24.22%
IPC (Mexico)	5818.43	-2.50%	010.03%
IPSA (Chile)	81.70	0.84%	-25.11%
Strait Times (Singapore)	1434.61	2.72%	-12.45%
Seoul Composite (Korea)	692.87	5.15%	-0.12%
ISE National-100 (Turkey)	13501.38	31.70%	-2.04%
Morgan Stanley Emerging Markets Free Index	297.334	5.01%	-6.32%

Foreign Exchange Market

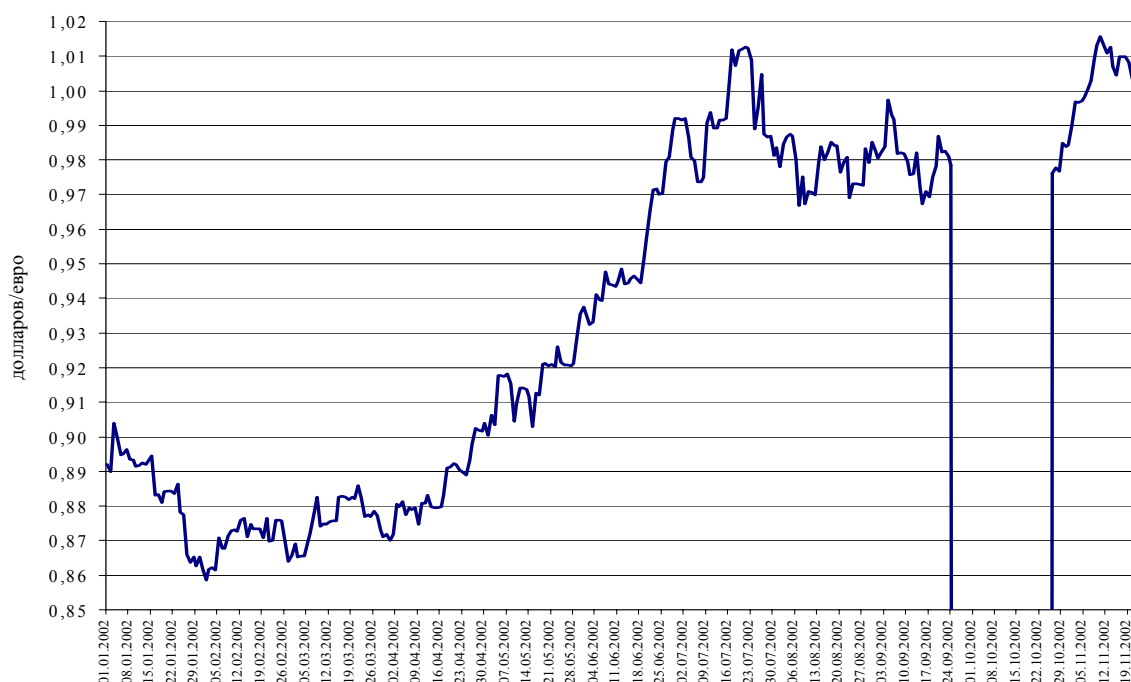
In October 2002 no significant fluctuations were observed in the RF foreign exchange market. The exchange rate passed the RUR/ US\$ 31.80 mark. The overall growth in the US Dollar exchange rate was 0.32 percent (from RUR/ US\$ 31.7408 at 31 October to RUR/ US\$ 31.8424 at 30 November 2002). According to preliminary estimates, the volume of trade in US Dollar in the SELT amounted to circa RUR 180 billion. In the previous bulletin we noted already that this value could lose its analytical sense once a new procedure for the mandatory sales of a part of foreign currency export revenues by legal entities is introduced by the Central Bank on 1 December 2002. (This document entitles banks to conduct mandatory sales of foreign currency over the counter). Facing a total loss of its monopoly, the MICEX decided in November to cut the commission for currency deals in the SELT dramatically. The fee for deals with US Dollars was cut from 0.06 percent down to 0.002 percent, i.e. one thirtieth of the previous value. The Exchange also canceled the mandatory cash deposit that was previously required to participate in the trade: now it is necessary to place with the Exchange only 1.5 percent of the plan transaction volume.

Figure 6. The official rur/ us\$ exchange rate in 2002



In November, due to the influence of the negative news on US economy, the Euro rate exceeded the parity mark for a certain period of time. However, the trend towards rise in the price of the European currency did not hold, and in the end of November Euro again became slightly cheaper than the US Dollar. Obviously, it can be assumed that in the near future the exchange rate will fluctuate in the range of US\$/ Euro 0.99 - 1.01.

Figure 7. Dynamics of Euro/Dollar Exchange rate on the world forex markets



The changes in RUR/ Euro exchange rate followed the trends in the global market. The maximum value in November was RUR/ Euro 32.2268 (the historical high) on 11 November 2002, the lowest value was RUR/ Euro 31.3666 on 01 November 2002. The official RUR/ Euro exchange rate grew from RUR/ Euro 31.179 on 31 October 2002 to RUR/Euro 31.6736 on 30 November 2002, or 1.59 percent.

Figure 8. Dynamics of the official exchange rate of euro in 2002

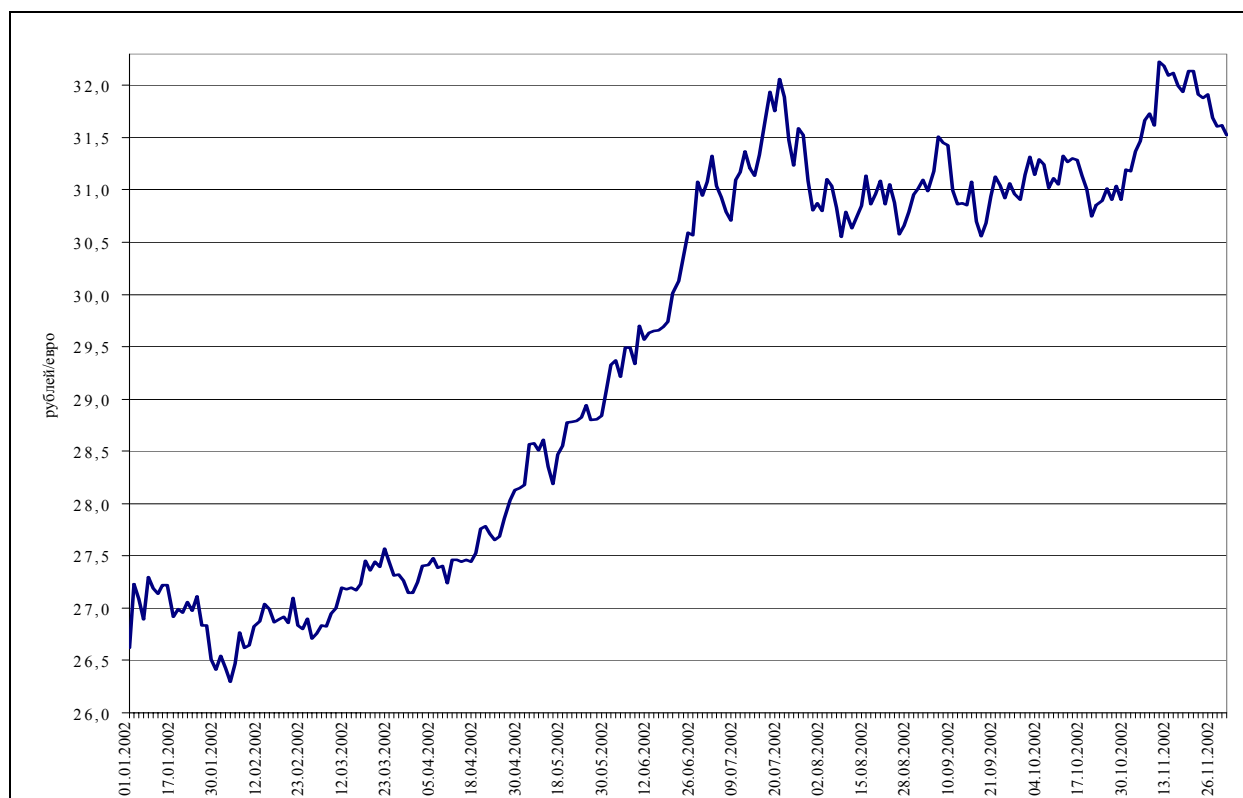


Table 2

Financial Market Indicators

Month	July	August	September	October	November
Monthly inflation rate	0,7%	0,1%	0,4%	1,1%	1,5%
Inflation rate annualized on the basis of this month's trend	8,7%	1,2%	4,9%	14,0%	19,6%
CB RF refinancing rate	23%	21%	21%	21%	21%
Annualized yield to maturity on OFZ issues	14,42%	14,45%	15,25%	14,98%	14,1%
Volume of trading in the secondary GKO-OFZ market for the month (RUR billion)	9,34	6,95	15,97	18,73	13
Yield to maturity on Minfin bonds at the end of the month (% p.a.)					
4 th tranche	6,27%	5,6%	5,46%	4,86%	4,74%
5 th tranche	11,19%	10,88%	10,13%	8,45%	7,72%
6 th tranche	10,3%	9,52%	8,84%	7,04%	6,70%
7 th tranche	11,03%	11,05%	10,31%	9,13%	8,55%
8 th tranche	9,72%	9,81%	9,24%	7,68%	6,71%
INSTAR-MIACR rate (% p.a.) on interbank loans at the end of the month:					
Overnight	29,06%	5,74%	17,79%	14,89%	10%
One week	8,08%	8,25%	2,85%	5,59%	10%
Official RUR / US\$ exchange rate at the end of the month	31,4401	31,5673	31,6358	31,7408	31,8424
Official RUR / Euro exchange rate at the end of the month	30,8019	31,0938	30,9082	31,1790	31,6736
Average annualized growth in RUR / US\$ exchange rate	-0,02%	0,4%	0,2%	0,33%	0,32%
Average annualized growth in RUR / Euro exchange rate	-0,89%	0,72%	-0,6%	0,88%	1,59%
Volume of trading at the stock market in the RTS for the month (US\$ million)	407	276,04	304,19	360,21	350
Value of RTS Index at the end of the month	326,23	332,9	334,06	358,65	359
Change in value of RTS Index during the month (%)	-9,22%	2,7%	0,35%	7,36%	0%

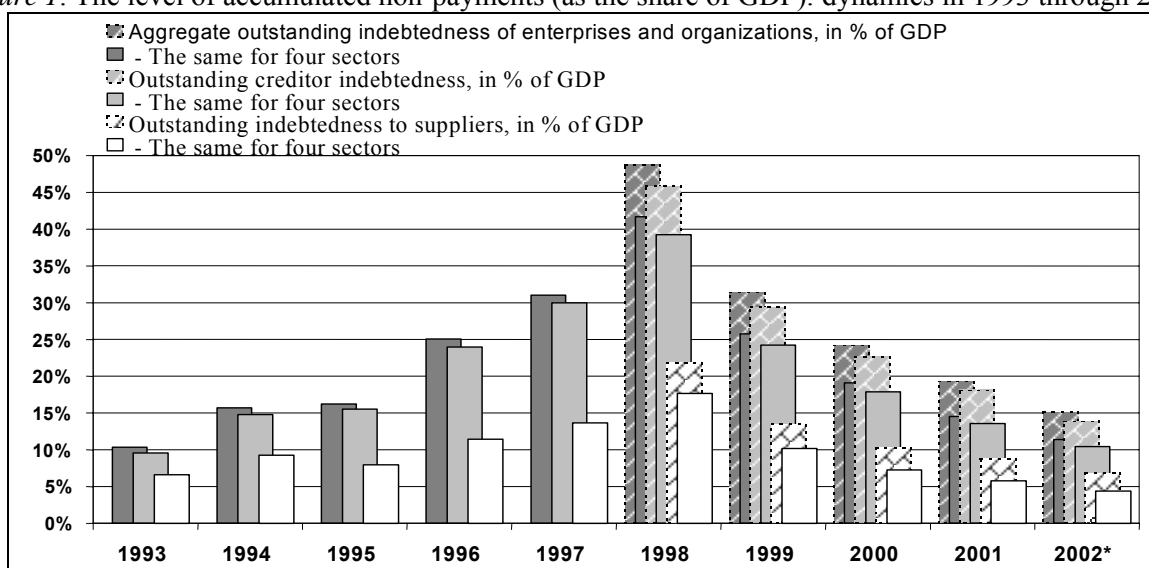
* Estimates

D. Levchenko, D. Skripkin

Enterprises and organizations: the state of payments

The trends observed in the sphere of payments in January through August of 2002 may be characterized as positive. The accumulated amount of outstanding indebtedness in the economy continued to decline both in real (share of GDP) and nominal terms (see Figures 1 and 2).

Figure 1. The level of accumulated non-payments (as the share of GDP): dynamics in 1993 through 2002.

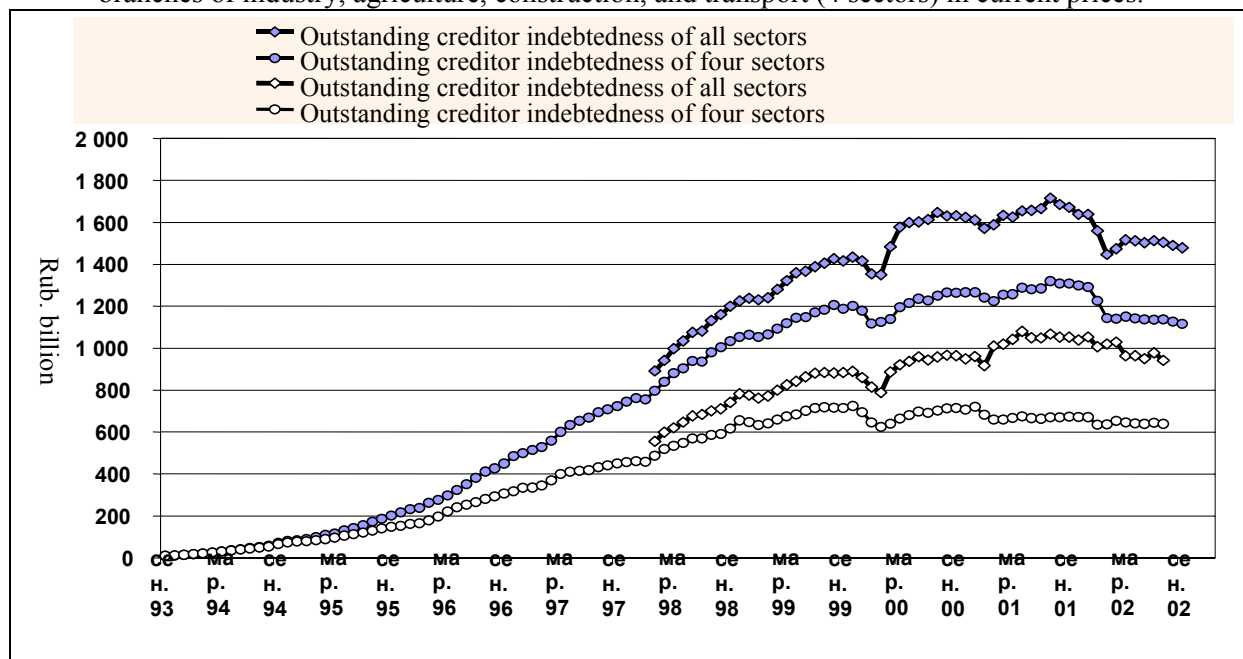


* - first six months of 2002.

Source: RF Goskomstat, calculations of the authors.

Note: the aggregate outstanding indebtedness of enterprises and organizations includes outstanding creditor indebtedness and the outstanding debts to the banking system. The creditor indebtedness is calculated as the sum of debts to suppliers, budgets of all levels, and extra-budgetary funds, indebtedness relating to wages and salaries, and debts to other creditors. Prior to 1998, the RF Goskomstat published payment arrears statistics for four sectors of the economy (industry, agriculture, transport, construction). Since 1998, the aggregate indebtedness in the economy has been calculated across all sectors of the economy.

Figure 2. Dynamics of outstanding creditor and debtor indebtedness across all sectors of the economy and branches of industry, agriculture, construction, and transport (4 sectors) in current prices.



Source: RF Goskomstat, calculations of the authors.

In the first 8 months of 2002, the amount of outstanding creditor indebtedness declined by 5.2 % (Rub. 81 billion) in comparison with the accumulated level, while outstanding debtor indebtedness decreased by 6.5 % (Rub. 66 billion) in January through July of 2002. In the first 8 months of 2002, the outstanding creditor indebtedness decreased by 5.2 % (Rub. 81 billion) in comparison with the accumulated level, while the outstanding debtor indebtedness declined by 6.5 % (Rub. 66 billion) in January through July of 2002. In the respective periods of 2001, there was observed a growth in the amounts of outstanding creditor and debtor indebtedness (7.2 % and 16.5 % respectively). The major decline in the outstanding creditor indebtedness occurred in January of this year and made Rub. 113 billion. It shall be noted that old debts (indebtedness overdue more than three months) accounted for 94 % (Rub. 106 billion) of decrease in indebtedness. Taking into account small amounts of debts written off to financial results (see Table 1), the decline in payment arrears is related to the restructuring and direct repayment of debts. The largest amounts of decline were registered in indebtedness to suppliers and extra-budgetary funds (Rub. 73 billion and Rub. 41 billion, or 9.6 % and 13.0 % of the accumulated level respectively). The indebtedness to the budget decreased by Rub. 14 billion (4.3 % of the accumulated level), while the overall amount of other types of indebtedness increased by Rub. 21 billion (11.7 % of the accumulated level).

Energy monopolies played a significant role in the decrease in payment arrears as they significantly diminished the use of all types of non-cash payments for shipped and purchased products. Even a greater decrease in barter operations in favor of offsets may be singled out among major changes in the structure of payments for shipped products of monopolistic enterprises⁶. In 2002, the share of cash payments increased and was maintained at about 80 % (see Fig. 3).

⁶ According to RF Government Resolution No. 10 of January 6, 1998, the RF Goskomstat conducts statistical monitoring of payments of largest Russia's taxpayers: "UES of Russia," "Gazprom," "Aeroflot – Russian international airlines," organizations of the federal railroad transport, and industrial monopolistic organizations.

Table 1.

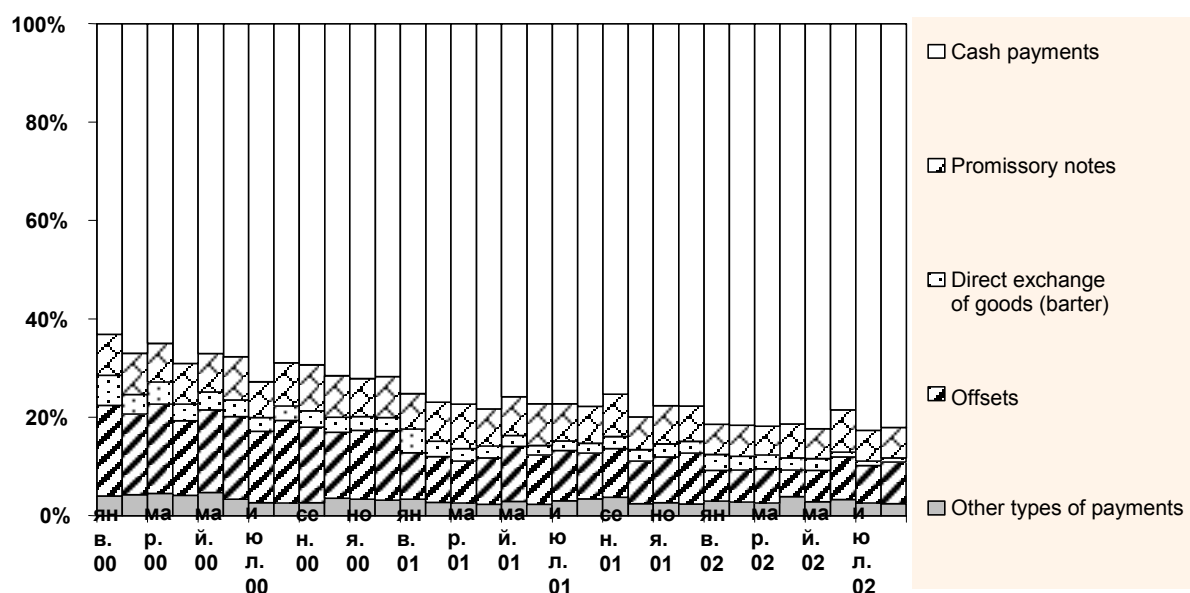
Amounts of outstanding indebtedness of economic agents written off to financial results.

Period	Creditor indebtedness written off to profit			Дебиторская задолженность, списанная на убыток		
	Total, Rub mil	in % to overdue creditor indebtedness	in % of annual Increment in overdue creditor indebtedness (including write-offs)	Total, Rub mil.	in % of overdue debtor indebtedness	in % of annual Increment in overdue creditor indebtedness (including write-offs)
1997	874	0.1%	0.4%	1 921	0.4%	1.5%
1998	2 777	0.2%	0.7%	7 990	1.0%	3.2%
1999	5 597	0.4%	4.3%	12 420	1.5%	19.1%
2000	6 598	0.4%	3.0%	21 955	2.4%	17.8%
2001	10 185	0.6%	13.1%	25 783	2.6%	22.1%
2002*	5 108	0.3%	-4.2%	10 798	1.1%	-19.6%

* January through July of 2002

Source: RF Goskomstat, calculations of the authors.

Figure 3. Monopolistic enterprises: the structure of payments for shipped products



Source: RF Goskomstat, calculations of the authors.

At the same time, certain new trends are alarming. First of all, these concerns are related to the factors of growth in outstanding indebtedness revealed by economic examinations⁷. For instance, in 2002 there was observed a stable increase in the share of loss making enterprises in the economy (see Fig. 4). The share of loss making enterprises in the economy increased by 7 % to 10 % across the sectors of economy in comparison with the figures registered in the preceding year. In July of 2002, the share of loss making enterprises in industry made 46.5 % (as compared with 38.6 % registered in July of 2001), while in construction this indicator made 45.9 % (39 % in July of 2001), and in transport – 54.5 % (45.8 % in July of 2001).

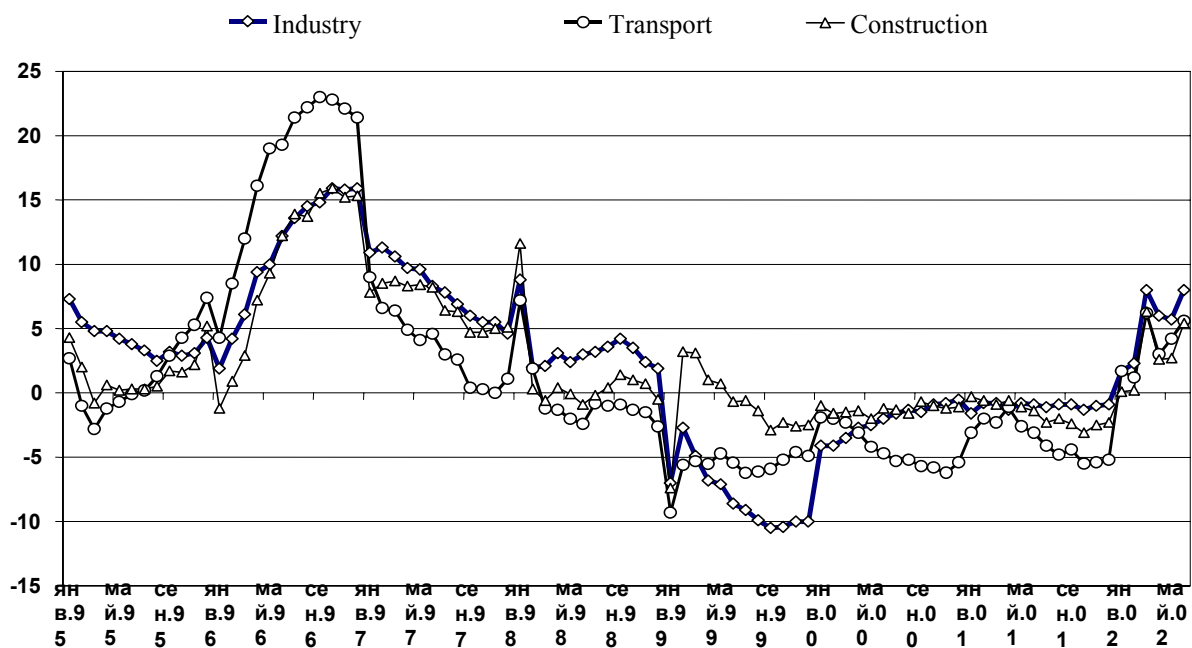
According to calculations⁸, ineffectiveness, financial insolvency of enterprises was a key factor behind the generation of payment arrears in the economy, which indicated the existence of a “channel of financing of bad firms.” This relationship was most characteristic for the period prior to 1998. After the crisis, the share

⁷ See, for instance, R. Entov, A. Radygin, V. Mau, S. Sinelnikov-Murylev et al. “Razvitiye rossiyskogo finansovogo rynka i novye instrumenty privlecheniya investitsiy (Development of the Russian financial market and new instruments attracting investment),” IET, 1998, pp. 96 – 149; O. Lugovoi, D. Semenov “Neplatezhi v Rossiyskoi Federatsii (Non-payments in the Russian Federation),” IET – USAID, 2000; R. Entov, L. Lederman, O. Lugovoi, A. Zolotareva ‘Non-payments in the Russian Economy and Regions’, CEPRA, 2001.

⁸ Ibidem.

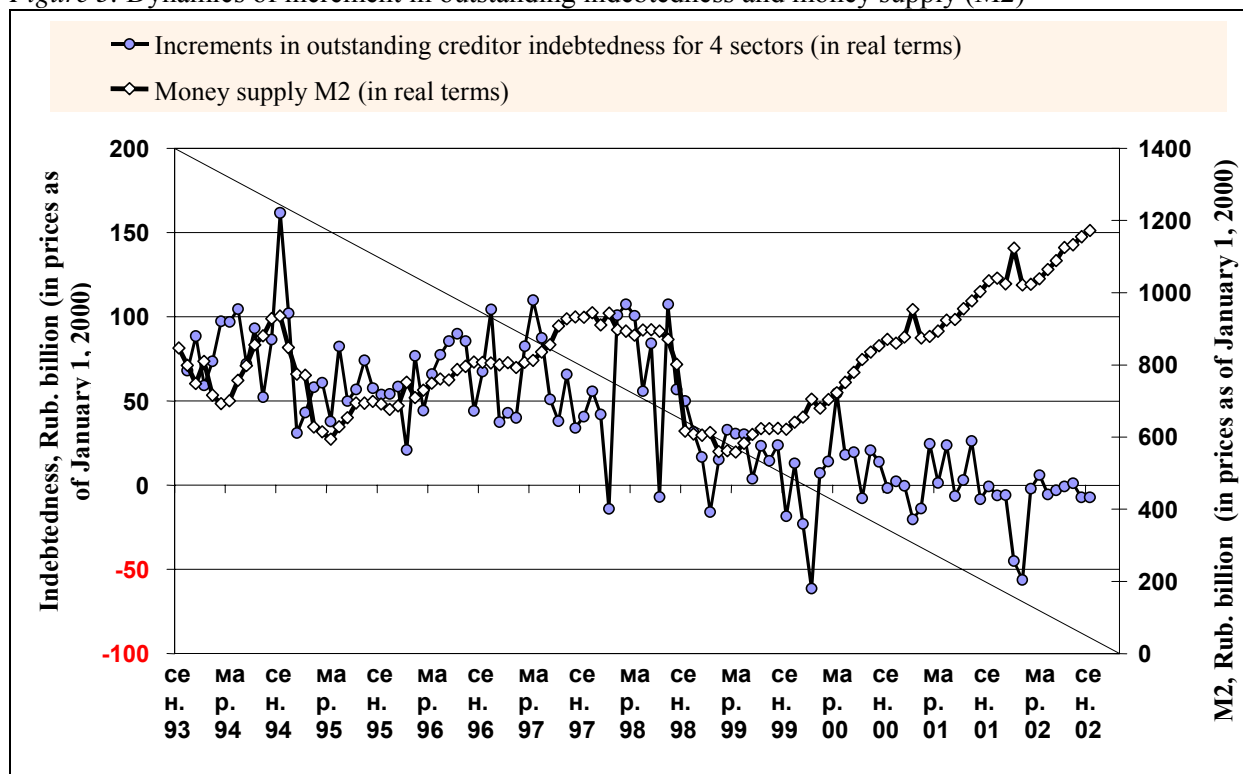
of ineffective enterprises constantly decreased, and the statistical significance of this factor diminished. Although no increase in payment arrears has been registered, this danger exists.

Figure 4. Changes in the share of loss making enterprises across industries (seasonal differences to respective periods of the preceding year)



Another important factor for the settlement of the problem of payment arrears is expansion of bank crediting. Transition to cash types of payments resulted in a growing cash demand, therefore, the money supply steadily increased over the last few years (see Fig. 5).

Figure 5. Dynamics of increment in outstanding indebtedness and money supply (M2)



Source: RF Goskomstat, CB of RF, calculations of the authors.

It seems that the factors, which prevented a surge in payment arrears in spite of a growth in the number of loss making enterprises and real Ruble appreciation, include, first, normalization of state finances, expansion of bank crediting, positive shifts in the area of contract law, in particular, bankruptcy laws.

Further developments in the sphere of payments will depend on the situation in the real sector of the economy and the stand of authorities primarily determined by the budget revenue situation. In the case the growth in the number of loss making enterprises continues, what is to a certain extent facilitated by a further real Ruble appreciation, there is a rather high probability of emergence of a new wave of increase in indebtedness. However, a surge in indebtedness may occur only under certain circumstances, i.e. in the situation where non-market relations develop due to ineffective enforcement of contract law. In such a situation, payment arrears are manifestation of ineffective, non-competitive production. Massive payment arrears switch off market mechanisms squeezing out loss making enterprises. Taking into account the positive experience accumulated in the last few years, a new large scale non-payment crisis becomes less and less probable, however, this danger can not be absolutely excluded in the case unfavorable economic trends prevail.

Investment in the Real Sector

In January through October of 2002, the positive dynamics of investment in the real sector of the economy persisted. The amount of investment in fixed assets from all sources of financing made Rub. 1234.6 billion, what is by 2.5 % above the level registered in the respective period of the preceding year. As compared with the figures observed in January through September of 2001, the share of investment in fixed assets in GDP decreased by 2.1 p. p. and made 13.6 %. In the first half-year of 2002,

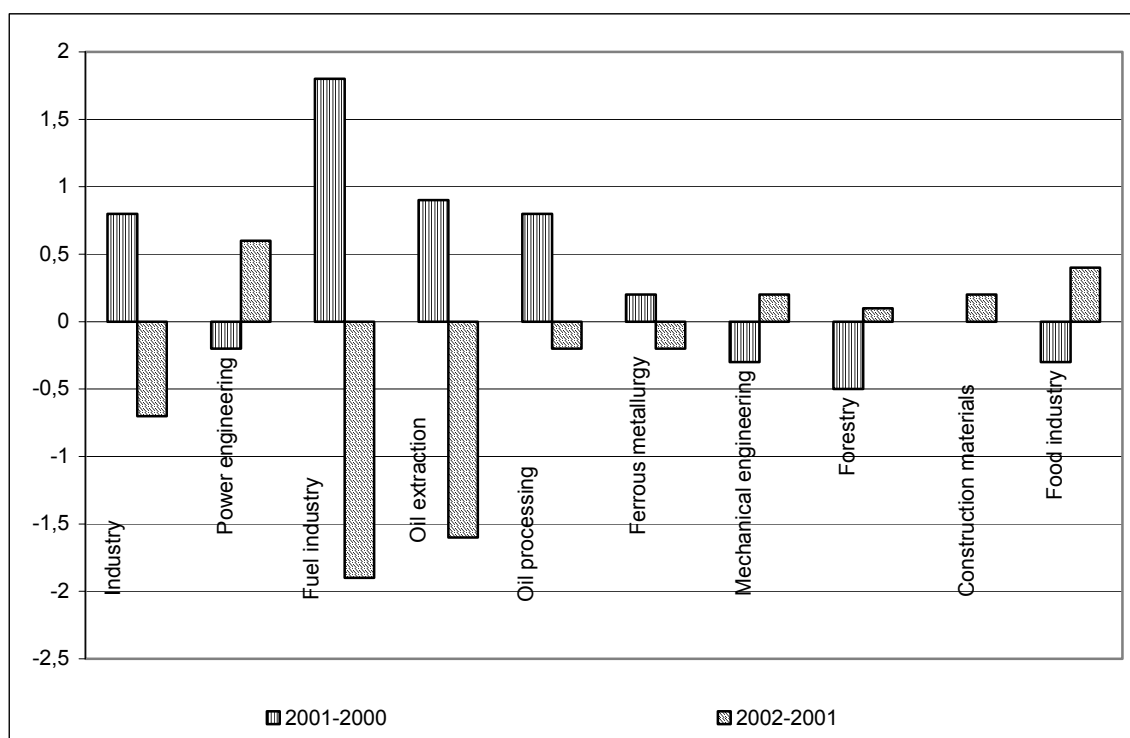
The lesser intensity of investment inflows in the real sector of the economy in 2002 was observed at the background of changes in the sectoral structure of investment. The share of investment in fixed assets of manufacturing industries has stabilized at about the level observed in the preceding year and made 49.2 %. The proportions of investment across the sectors of the economy was practically completely determined by the decrease of investment in industry and transport. As compared with the figures registered in January through October of 2001, the share of investment in industry decreased by 0.7 p. p., while the share of investment aimed at the development of transport fell by 3.2 p. p. At the same time, the share of investment expenditures for communications grew by 1.2 p. p., agriculture – by 0.5 p. p. and trade – by 0.3 p. p.

This year, the decreasing share of fuel complex in the total amount of investment in fixed assets in the economy on the whole and in industry is a significant factor behind the nature and dynamics of investment demand. Investment in the fuel complex made 26.1 % of the total amount of investment in fixed assets of all sectors of the economy in January through September of 2002 decreasing by 1.3 p. p. in comparison with the figures registered in the respective period of the preceding year. Taking into account the fact that transport, communications, and the fuel complex account for almost ½ of the total amount of investment in the national economy, it becomes evident that the financial and economic standing of these industries has the most strong impact on the dynamics and structure of investment demand.

Fuel industry maintains its dominating position in the structure of investment, its share makes 49.8 % of the total investment in industry; at the same time, almost 1/3 of investment flows in oil extracting industry. Over the last two years, the intensive expansion of demand for investment goods on the part of the oil and natural gas complex was a powerful factor behind the increase in business activity in mechanical engineering and the industry of construction materials. In 2002, as a result of cumulative impact of external and internal factors, profitability of production in oil industry fell almost twofold in comparison with the preceding period, what negatively affected the level of investment demand. Taking into account the traditionally high concentration of profits in the export oriented industries of the oil and raw materials sectors and the lack of mechanisms of inter-sectoral flow of capitals, it may be hardly expected that the rate of investment would increase and radical changes would occur in the nature of the reproduction of fixed capital. Fuel industry demonstrated deteriorating indicators of the reproduction of fixed capital at the background of decelerating rates of investment in this sector. In January through September of 2002, in fuel industry the commissioning of drilling wells decreased by 18.1 %, production drilling contracted by 17.7 %, and surveying drilling fell by 37.9 %. The decrease of investment in oil processing industries resulted in deteriorating technical and economic indicators of production. The output of oil products produced with the use of progressive processing technologies has decreased by 2.9 %, while the degree of processing of crude oil decreased from 71.1 % registered in January through September of 2001 to 70.3 % observed in the respective period of this year.

Decelerating rates of investment in industry observed in January through September of 2002 took place at the background of persisting sectoral proportions registered in the preceding year. The share of investment in fixed assets of natural gas industry remained at 5.0 %, chemistry and petro-chemistry – at 1.8 %, non-ferrous metallurgy – at 3.2 %, and light industry – at 0.2 %. In spite of the fact that in 2001 through 2002 there was observed an increase in the share of investment in the processing sector of the economy, it shall be taken into account that the share of investment intensive industries account for 4.8 % and industries of the consumer complex account for 4.6 % of the total investment in industry. Under the existing age, technology, and reproduction structure of fixed assets, low rates of investment in manufacturing industries are a factor slowing down the rates of economic growth.

Figure. Changes in the structure of investment across industries in January through September of 2002, in % of the respective period of the preceding year



Deteriorating financial standing of enterprises in the real sector of the economy is a major factor initiating a slowdown of rates of investment activity.

Since the beginning of the year, the dynamics of balanced profits have been characterized by the gradual deceleration of the quarterly rates of decrease in balanced profits in comparison with the respective periods of 2001. The industries of the service sector had a positive impact on the character of formation of balanced profits in the economy. In January through September of 2002, the amounts of balanced profits were above the respective indicators observed in the preceding year: in communications - by 33.0 %, in transport – by 20.8 %, and in trade and public catering – by 8.7 %. However, the increase in profits registered in the service sector did not compensate for the negative impact of decline in profits observed in industry (by 37.1 %) and construction (by 36.7 %). As a result, the balanced financial results of enterprises and organizations across all sectors of the economy made 83.1 % in January through September of 2002 as compared with the level registered in January through September of 2001.

As the financial results of operations of industrial organizations deteriorated in January through September of 2002, their share in the sectoral structure of the balanced profits of the economy decreased by 14.1 p. p. in comparison with the figures registered in the respective period of the preceding year and made 39.8 %. The deterioration of this indicator across the industry at large occurred at the expense of export oriented industries – by 10.6 p. p., while fuel industry accounted for 6.4 % of decrease in this indicator.

The decrease in the profitability of production in the fuel and metallurgical complexes forming more than ¼ of the total investment demand in the national economy has negatively affected the business activity in construction. In the first six months of 2002, the share of profits in the structure of the sources of financing

of investment in fixed assets decreased by 2.5 p. p. in comparison with the figures registered in the respective period of 2001. The situation is aggravated by the impact of such factors, as high costs of commercial credits, insignificant amounts of financing from budgetary funds and other financial institutions, high level of investment risks due to insufficient legal protection of domestic and foreign investors, and the lack of effective mechanisms ensuring transformation of household savings into investment.

In this situation, it is rather problematic to expect that investment recovery, which in essence is the major potential source of growth, will persist.

O. Izryadnova

The Real Sector: Factors and Trends

According to the preliminary data, in January through September of 2002, GDP made Rub. 7896 billion and increased by 4.0 % in comparison with the figures registered in the respective period of the preceding year. The dynamic expansion of final demand has positively affected the dynamics of GDP and output of base sectors of the economy since the 2nd quarter of this year. According to the estimates of the Ministry for Economic Development, on the whole in 2002 GDP will make about Rub. 10950 billion and increase by 4.0 % as compared with the preceding year figures.

A growth in output is observed across practically all industries and sectors of the economy since February of 2000. The output of products and services of the base economic sectors increased by 3.8 % as compared with the figures observed in January through October of 2002. While the output of manufactured goods grew by 4.0 % in January through October of 2002, the production of construction industry increased by 2.5 %. On the whole, service sectors developed more dynamically. In January through October of 2002, the retail trade turnover grew by 9.0 %, freight turnover – by 5.1 %, and communication services – by 12.0 % as compared with the figures registered in the respective period of the preceding year.

An analysis of changes in the structure of industry reveals that practically all growth in production was generated by the outpacing development of industries oriented towards the domestic market. The index of production related to the consumer complex made 106.5 % in January through October of 2002. As concerns the branches of investment complex, a rather significant slowdown in the rates of growth was a characteristic feature of this year. On the whole, in January through October of 2002, the index of production related to the investment made 103.3 % as compared to the figures registered in January through September of 2001. In January through October of 2002, the output of mechanical engineering increased by 3.1 % as compared with 8.0 % and 17.5 % registered in 2001 and 2000 respectively. While in 2000 and 2001 the characteristic features of the economy were outpacing rates of growth of investment sectors as compared with export oriented sectors and fuel industry, in 2002 the situation is changing.

Therefore, in 2002 there was observed a more strong impact of export oriented sector of the economy, and as a result, dependence of the Russia's economy on the business situation on world raw materials markets. As the external business situation gradually improved, the rates of growth in production of export oriented industries reached 105.5 % in January through October of 2002. Non-ferrous metallurgy (108.9 %) and fuel industry (106.6 %) demonstrated the most rapid rates of growth among the industries of this complex.

A specific feature of the 3rd quarter of 2002 was favorable shifts in the world business situation, which stimulated export and supported the economy at large. However, even in this case the growing influence of competing imports significantly affected the dynamics of development of domestically oriented industries. While the total industrial output increased by 3.7 % in comparison with the figures registered in January through September of 2001, imports grew by 12.1 %. The intensive growth in imports has most significantly affected the dynamics of development of the investment complex. While the output of mechanical engineering increased by 3.1 % in comparison with the figures observed in January through September of 2001, import of machinery, equipment, and vehicles grew by 20.5 %, at the same time, the share of imported equipment in the structure of investment in machinery and equipment made almost one fourth.

Stagnation of production of light industry was accompanied by an increase in import of jersey and textile wear, which made 67.1 % in comparison with the figures registered in January through August of 2001, while import of footwear increased by 28.2 %. A gap between the rates of growth in domestic production of consumer goods and imports resulted in a shift of the situation on the retail market. According to estimates, the share of imports in the structure of commodity resources of non-food products has increased by 3.3 percentage points since the beginning of the year. At the same time, it is necessary to stress that while non-competing imports make a significant share of the structure of commodity resources of retail trade in food

products, imports squeeze out domestic products in the sphere of retail trade in non-food items. Further development of these trends makes problematic expansion of domestic production of consumer goods. In this connection, it seems feasible and timely to take a decision on the reduction of import duties on certain types of technological equipment in order to increase competitiveness of goods made in Russia.

In 2002, growing consumer demand is a factor compensating for a slowdown in rates of investment demand. As compared with the figures registered in January through October of 2001, the increase in the retail trade turnover made 9.0 %. It shall be noted that in the 3rd quarter there was observed an outpacing rate of growth in demand for non-food products as compared with foods. At the same time, the demand for non-food goods significantly outpaces real household incomes.

An intensive growth in household incomes was a major factor behind the expansion of consumer demand. At the same time, on the one hand, the continuing intensive growth in wages and salaries supports the positive dynamics of real incomes. In January through October of 2002, the increase in real disposable household incomes made 8.9 % as compared with figures registered in January through October of 2001, while real wages and salaries grew by 17.4 %. On the other hand, the widening gap between wages and salaries and productivity of labor initiates a growth in production costs and decrease in profitability. This year, the share of gross profits in GDP decreased from 40.7 % registered in the 1st quarter to 37.7 % observed in the 2nd quarter.

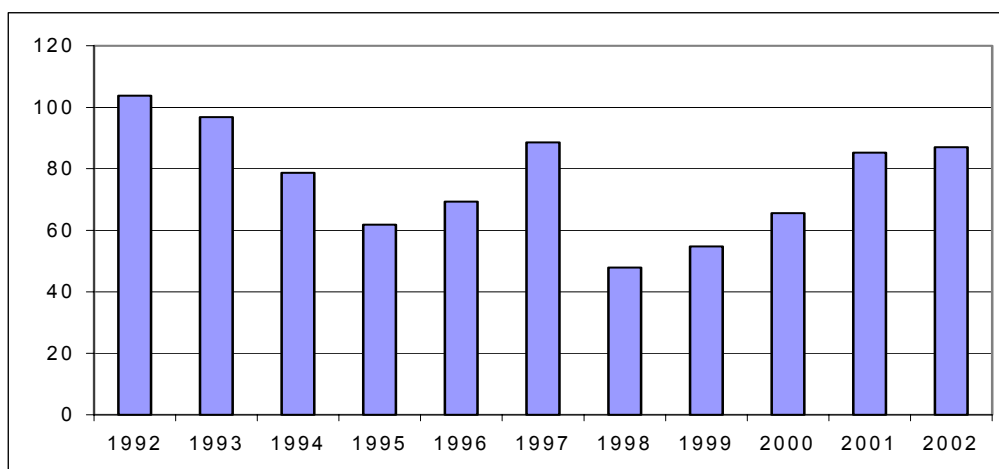
In the case the rates of growth in proceeds of enterprises decelerate further, the existing trends will persist. In the situation, where the internal funds in the real sector of the economy are limited and it is impossible to borrow funds for a long term, the Russia's economy reproduces the conditions provoking the shrinking of investment demand. An analysis of major trends of development of the Russian economy over the last three years demonstrates that cardinal changes in the structure of investment in the real sector oriented towards a large scale modernization of fixed assets, increase in productivity of labor and competitiveness of domestic products on the internal and external markets is a key factor behind further economic growth.

O. Izryadnova

Grain Interventions in 2002

The new grain crop in Russia is rather good although not record high as it's sometimes declared in the home press (Picture 1). Large beginning stocks, scarce increase of domestic demand and complicated export exert strong pressure on the domestic grain market: its prices fell far below the world ones. By the end of October prices for soft wheat FOB Novorossiysk port ranged from \$90 to \$100 per ton while in Europe they amounted to \$120, in the US Gulf – to about \$160. Grain prices were sliding down during harvesting and right after it. In Siberia they fell very low – to \$50 per ton of wheat #3, FCA.

Picture 1. Grain production in Russia, million tons



Source: Data of the RF State Committee for Statistics.

In this situation the government for the second year round decided to carry out grain interventions. For this purpose “Sberbank”⁹ grants a 6 billion rubles loan guaranteed by the federal government that is to be used for purchasing and storing grain (40 rubles per ton monthly), for paying commission (2,7% of the grain value) and for servicing the credit.

Maximum prices to be paid in the course of state purchase interventions were set as follows:

- soft food wheat #3 – 2300 rubles per ton;
- soft food wheat #4 – 1800 rubles per ton;
- food rye group A – 1400 rubles per ton.

These prices include costs of delivering grain to elevator, its acceptance, primary processing, drying and insurance.

As different from 2001, intervention purchases are made in 6 other sites in addition to Moscow. This is a *de facto* recognition of grain market decentralization in the country: bigger demand in the Central region does not result in the corresponding rise of prices in other regions. The state unitary enterprise “Federal Agency for Regulating Food Market” is hors concours authorized to be the state’s grain purchasing agent, while in 2001 the choice was made by tender. This simplifies the procedure and, to our mind, does not infringe upon market operators’ interests. Some other procedures of the intervention mechanism are simplified as well (e.g. security deposit becomes smaller and easier to call back). Besides, the amount of budget funds to be spent on interventions is notably enlarged. Given that the most over-saturated markets are those of feed wheat and rye, in 2002 these crops will also be subject to interventions in addition to wheat #3 purchased in 2001. Interventions are combined with temporary duties on import of respective grains. Their rate is set at 12 EUR per ton seeming to be a sufficient protection against substitution of imports for the sterilized domestic grain¹⁰. In all other respects the 2002 intervention mechanism copies the 2001 one.

Trading sessions in the framework of state purchase interventions started only on November 13, and those for rye even later – on November 20. The delivery period under signed contracts is 45-90 days (depending on the terms of delivery). Due to that it’s still hard to assess the interventions’ impact on prices for grain on the primary and secondary markets. Besides, one cannot judge how beneficial they are for market operators basing only on price rise during or just after purchases. The costs of storing grain till the spring-summer 2003 price peak should be compared with grain prices during this peak. It may turn out that even though prices have grown as the result of interventions, it’s more profitable to store grain till spring and to sell it at the end of marketing year rather than to do it right now.

Nevertheless, some conclusions can already be made.

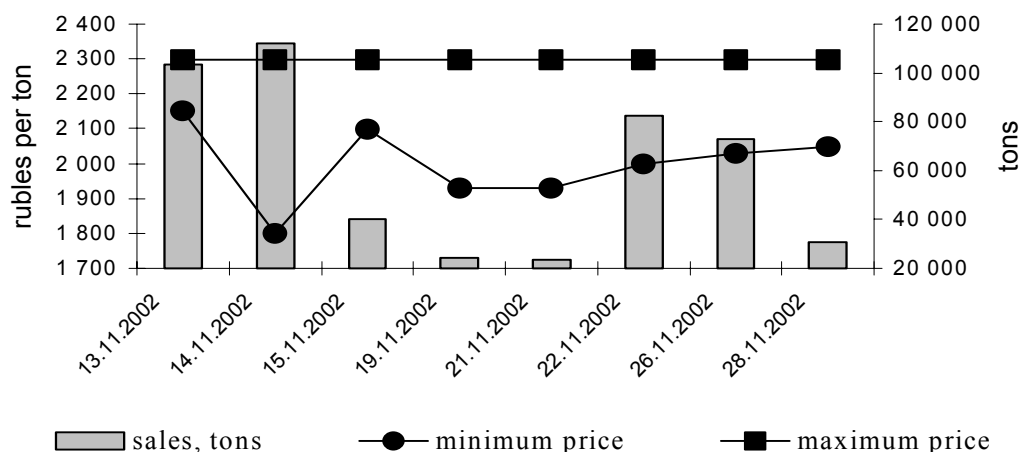
First of all, it should be noted that in 2002 prices for basic grains began to rise several weeks before trading sessions started but already after the intervention intentions had been announced. Experts point out that purchases of grain from agricultural producers grew as well. Still, one cannot assert that this growth is entirely the result of announced interventions since at the same time exports of grain notably expanded and might have also led to higher prices on the domestic grain market. From the beginning of harvesting till the end of November over 5 million tons of grain were exported, from January 1, 2002 – almost 11 million tons.

Grain with South of Russia delivery terms is traded far less intensely than in Siberia while the price for it is generally higher. This fact evidences that the Russian grain market has at least two relatively independent segments: before and after the Urals. Operators in the Central part of the country, and first of all in the South, have an opportunity to export grain (Rostov oblast is the major grain exporting region of Russia), and, besides, the demand for their feed grain is higher since livestock production here is growing. The supply of grain on the Siberian market is excessive due to the good crop and low demand inside the region. Accordingly, the market situation in which intervention purchases are made in these two regions is shaped by different alternative traders’ costs. Besides, this is an evidence of relatively high transportation barriers to delivery of grain from the eastern part of the country. Such barriers are posed not only and not so much by railroad tariffs as by availability of vans and by other factors (the fact needs a more detailed examination).

⁹ The Savings Bank.

¹⁰ The Russian Customs Code does not allow to introduce a variable import tariff. Since purchases are projected for two years, the rate of 12 EUR per ton may at some moment turn out to be too high or too low depending on the world grain market situation.

Picture 2. Statistics of trading sessions for soft wheat #3 in November 2002 (volumes purchased and minimum/maximum prices)



Source: trade information (<http://www.birja.ru/session.html>).

The prices received at trading sessions are about 200-500 rubles per ton (10-30%) higher than the average purchase prices in corresponding regions. It would be a mistake to conclude that this is the amount of real prices' growth. First of all, the auction price includes costs of delivering and primary processing of purchased grain, and so the difference in prices is approximately 5% smaller. Besides, the above described intervention mechanism with maximum prices and the total amount to be spent both fixed by the state determines Dutch auction – the one with lowering bids. The world experience shows that in case of applying the Dutch type of auction prices are usually higher than in case of applying the English one (with elevating bids). Second, given the selected mechanism the auction price is not directly translated into the market price. The offered for auction sale volumes are not entirely determined by supply of grain in the region – they also depends on local traders' ability to register as trading sessions' participants. In case the competition thereat is not strong, the price settles at the level that is not much below the upper limit announced by the government. Meanwhile, when brokers that signed contracts on delivery of grain to the state enter the cash market for buying it, the supply may be so large that the actual purchase price will be far below the trading sessions' rates. In this case brokers will be the ones who benefit from the price margin. It's important that such a situation is possible even without the brokers' collusion at auction (this year large number of market operators participating in trading sessions helps to diminish the possibility of such collusions). Some traders sign contracts on delivering grain that they have already bought and stored in elevators. For instance, one can guess that brokers participating in trading sessions in Russia's South offer to state the grain that is already stored in elevators since the auction prices are close to the actual purchase prices in the region (otherwise purchases for future deliveries become non-profitable given that auction prices are to be reduced by costs of delivering and primary processing of grain). In this case auction prices won't affect primary market (purchase) prices at all: the only result of trading sessions will be guaranteed marketing of some traders' grain and the corresponding lowering of their risks.

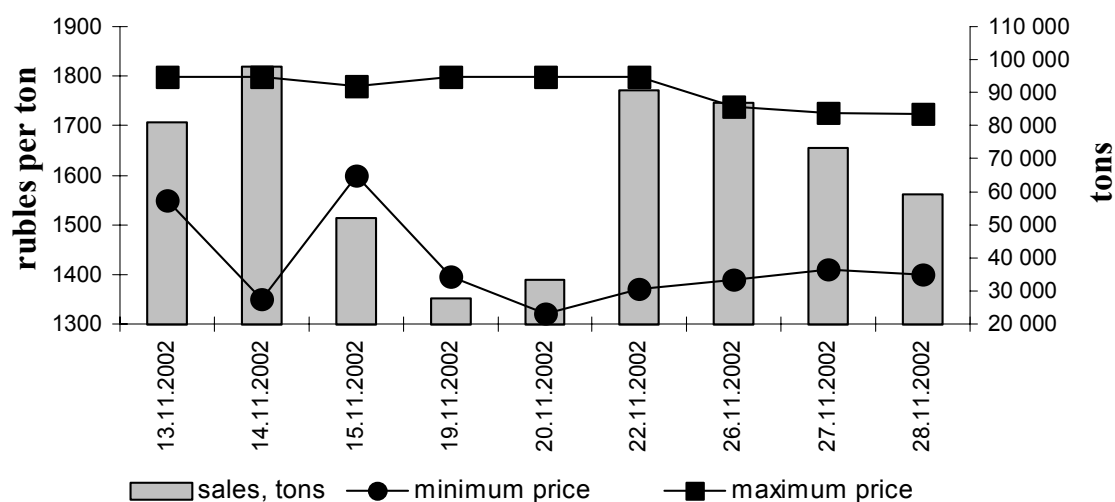
The adopted intervention mechanism has one more unclear provision complicating market operators' business planning. The state has fixed the total amount of purchases and the maximum purchase prices. It's also envisaged in government resolutions that interventions will be conducted in 2002-2003. However, there are no indications under what circumstances these purchases will begin and stop. Will the 2002 trading sessions be held until all the 6 billion rubles are spent or will they be halted and regained later? Who and how takes the decision? In this situation market operators cannot estimate their risks and choose the proper moment for entering the market. In other words, the state's actions increase uncertainty on the market and accordingly the risks of its operators.

And finally, the government decisions do not contain a clear mechanism of control over non-penetration of intervention stocks into the domestic market. In case it happens, the excessive grain won't be sterilized and intervention purchases will become senseless. In the US intervention grain stocks are sometimes colored

with food dyes in order to control their movement since inspection of elevators is found non-sufficient. Instead such mechanism in Russia we have only promises of the Ministry of Agriculture officials.

Although the impact of 2002 interventions on grain prices is not yet clear, their importance for development of exchange trade in grain is evident: despite all imperfections the currently held sessions make their participants used to public auction, to an open price quotation and basic procedures and organization of exchange trade. In this respect the positive role of 2002 interventions is doubtless.

Picture 3. Statistics of trading sessions for soft wheat #4 in November 2002 (volumes purchased and minimum/maximum prices)



Source: trade information (<http://www.birja.ru/session.html>).

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E. Serova, I. Khramova

Introduction of Grain Quotas by the EU

The European Union plans to alter the regime of grain market regulation. In June the Agricultural Commissioner Mr. Fishler announced quite an ambitious program of further liberalization of the EU Common Agricultural Policy (see www.iet.ru/afe/news) that looked even more liberal when compared with the new US Farm Bill (Ibid.). Nevertheless, the sharply growing import of cheap grain from Eastern Europe includ-

ing Russia and protests of local grain producers entailed shifting to new policies that envisage the introduction of tariff quotas on import of food wheat.

Beginning from January 1, 2003 the EU enforces the tariff quota on import of low and average quality food wheat totaling 2 981 600 tons. Within this quota the customs duty will equal 12 EUR per ton, in excess of it – 95 EUR per ton. Quotas will also regulate the import of brewer's barley (50 000 tons with 8 EUR per ton duty within the quota) and other barley (300 000 tons with 16 EUR per ton duty within the quota). The effective duty (93 EUR per ton) will be applied to all barley in excess of the quotas.

The EU has already signed agreements with the US and Canada on granting them a quota for import of about 600 000 tons of grain, meaning that only 2 300 000 tons remain for the East European countries.

Let's first examine whether this measure complies with the WTO Uruguay Round Agricultural Agreement (1994). According to this agreement all non-tariff import restrictions should be tariffed (i.e. transferred into an ad valorem form) and their further application is principally not permitted. In developed countries the initial rates of coupled tariffs had to be reduced by 36% within 6 years (till 2000), in developing countries – by 24% within 10 years. 4 countries (none of which is European) were allowed to temporarily preserve quotas. Besides, members of WTO had to set quotas for products the import of which during the base period (1986-1988) was below 5% of the domestic consumption. When enacted these quotas had to equal at least 3% of the domestic consumption and by the end of 6-year period – 5%.

As we see, quotas were supposed to be a mechanism of expanding access to domestic markets rather than a mechanism of constraining import. In late 80's the EC grain imports were very small and thus when Uruguay Round agreements were initially implemented, grain quotas could serve as a tool of easing penetration into the Community's market. However, today the European Union imports over one fourth of all the consumed wheat. The introduced in 2003 quota is very small – less than 3% of the domestic production. In other words, the new regime contradicts the spirit of Agricultural Agreement since one of its three basic principles is easier access to domestic markets of WTO countries.

What does this imply for Russia? In the current marketing year the country actively exports wheat (and even rye!) to the European market. The major buyers of Russian wheat in recent months were Italy, Greece and Spain. In July-October Russian grain was imported by 11 of the 15 EU countries. Within 4 months the volume of new crop grain supplied to the region totaled almost 3 million tons of which over one third was wheat. Since during all these months exports to Europe continued to grow, one can expect that by the end of the year Russia will additionally supply 1 million tons of grain to the EU. Thus, already now Russian exports almost equal the annual quota for all East European countries. In other words, the introduced by the EU new trade regime dramatically restricts our access to this market. The 2003 grain crop in Russia is likely to be smaller but the drop won't be very deep since even given the current technical level our grain output is far from being the largest possible. Domestic consumption will hardly show noticeable growth. All this means that in the coming year the country's grain sector will preserve its export potential. So the new grain trade regime introduced by the EU countries significantly limits Russia's export opportunities.

E. Serova

2003 Agricultural Budget

The State Duma passed the Law "On 2003 Federal Budget" in the third reading. In the coming year the expenditures on agriculture will total 37,7 billion rubles (Table 1). This is 18% (or about 7% in real terms) more than in 2002. Expenditures on agriculture grow slower than the total budget expenditures (up 9% in real terms). Still, this growth is quite noticeable when compared with the preceding year (1,15% in real terms). The share of agriculture in the total budget expenditures remains at approximately the same level – 1,61% (in 2002 – 1,64%).

The efficiency of budget support to the agrarian sector is determined by the way funds are distributed among items and goals rather than by the total amount of budget allocations. The structure of agrarian budget remains actually unchanged as compared with the previous year. As before, 64% of funds will be spent on various subsidies and programs of support to agricultural producers. The financing of budget services (the most important and efficient part of the agrarian budget including expenditures on control and inspection institutions, on education and science, on providing market information to producers) remains at the previous year level. While in 2002 expenditures on science and education started to grow, the 2003 budget envisages nothing of the kind.

Subsidies to agricultural producers are of the greatest interest from the point of view of next year's agricultural policies. The structure of federal budget expenditures on these subsidies does not change since early 90's (Table 2). That's where two basic problems of the 2003 agricultural budget originate. On the one hand, the draft budget preserves all the programs of support to agricultural producers, the inefficiency of which has long been spoken about. On the other hand, it does not envisage programs and regulation tools that the Government and the Ministry of Agriculture declare to be the most important ones for the sector's development.

For instance, purchase interventions aimed to support grain prices are conducted for the second year round. Regardless of their efficiency, they need financing since they take place. Still, neither 2001 nor 2002 budget allocated funds for this purpose and had to be amended right before the interventions started. The 2003 budget item "Agriculture and fishery" specifies that 1 billion rubles will be spent on financing interventions. These funds are intended for servicing the "Sberbank" credit on conducting grain purchases in 2002/2003. It's not clear from what sources the principal debt will be paid back. In case next year similar interventions are needed, there is again no corresponding allocation in the budget.

In order to stabilize the domestic grain market the government plans to take several rational (from our point of view) steps: to alter state grain standards, to favor export including compensation of transport tariffs and development of ports' infrastructure. Out of all these measures only one gets financing from the 2003 budget: 130 thousand rubles are allocated to compensation of interest on long-term credits used for construction of port elevators.

On the other hand, the budget contains programs of support to agricultural producers, the efficiency of which is very doubtful: subsidies to utilization plants, support to flax and hemp growers, subsidies for wool, etc.

Given high profitability of crop production in recent years, seed growing becomes profitable as well and no longer needs state support. Nevertheless, the expenditures on this program in the past two years grew at a high rate.

Federal subsidies for seed growing as well as some of the above mentioned subsidies look even more irrational given that similar programs exist at the regional level. Allocations from the federal budget are often so minor as compared with regional expenditures that they do not have a stimulating effect.

The novelty of 2003 budget are expenditures on implementation of the recently adopted Target program of rural development. One of its positive features is the allocation of budget funds to completion of social infrastructure's transfer from agricultural enterprises' to municipal balances and its technical updating.

The financing of leasing programs is more than halved. Before 2002 leasing was the only program facilitating agriculture's technical re-equipment. However, the applied leasing scheme proved to be inefficient as we have continuously noted in our publications. Thus, the cutting of expenses thereon should be welcomed. In 2002 the program of compensating agricultural producers for interest paid on medium-term credits of commercial banks was initiated. In 2003 it's likely to substitute for the leasing program since its terms are much more beneficial for farms. The financing of medium-term credits' program will be almost doubled as compared with 2002 and one can suppose that the demand for such subsidized credits will be high.

In 2003 1,2 billion budget rubles will be invested in "Rosagroleasing" authorized capital. Large funds continue to be used for strengthening monopoly operating at the budget expense. Its effective margin is well above the leasing market average (not only in agriculture but in economy as a whole) thus burdening agricultural producers and hindering the development of normal market of leasing services in the agrifood sector.

Expenditures on partial compensation of insurance costs are increased 3,5 fold. The fast progress of agricultural debt restructuring allows to suggest that farms may have enough funds to insure against risks, and the corresponding government program will foster the spread of insurance practices in the agrifood sector. Still, today it's hard to assess how these allocations will be actually used in 2003.

The expenditures on maintaining subordinate institutions will grow by 1/3 since the financing of veterinary inspections, seed inspections and melioration organizations is transferred from the regional to the federal level.

The 2002 budget envisages that "Rosselkhozbank" and "Rosagroleasing" will be the government's agents collecting debts on previously granted credits and leasing payments. Their remuneration for performing this function is 20 million rubles. In the draft 2003 budget the amount is raised to 40 million rubles (Clauses 76-78) though it's not clear what is this rise due to – the success of debt recovery campaign in 2002 or the change of agents' functions. Besides, there is again no provision as to whether the remuneration is to be paid in case debts are collected in full or just partially. To our mind, it should be set as a percent rate of recovered

sums. In any case, these allocations mean strengthening of commercial institutions at the budget expense and favoring of selected market agents.

Table 1.

Structure of federal budget expenditures on the agrifood sector in 2001-2003, thousand rubles

	2001			2002	2003	% of change
	plan	execution	% of execution	plan	draft	
Agricultural production	9 627 700,0	12 468 099,2	<u>130%</u>	20 444 700	24 010 800	<u>117%</u>
Land resources	6 912 000,00	6 959 204,10	<u>101%</u>	1 937 000	1 801 300	<u>93%</u>
State support to grain inspection institutions	55 000,00	56 894,50	<u>103%</u>	97 614	108 300	<u>111%</u>
Budget investments in the leasing company authorized capital					1 270 000	
Forming of Russian Agricultural Bank's ("Rosselkhozbank") authorized capital	2 000 000,00	2 000 000,00	<u>100%</u>	1 420 000	1 150 000	<u>81%</u>
Science	140 199,70	186 777,90	<u>133%</u>	171 562,30	181 179,5	<u>106%</u>
Russian Academy of Agricultural Sciences	879 641,60	1 056 049,20	<u>120%</u>	1 496 327,90	1 650 717,1	<u>110%</u>
Education	3 280 498,20	3 751 271,60	<u>114%</u>	5 350 106,10	6 452 482,3	<u>121%</u>
Capital investments	440 498,30	577 914,90	<u>131%</u>	246 850	864 500	<u>100%</u>
Ministry's staff	94 536,80	129 197,80	<u>137%</u>	142 029,10	152 229,8	<u>107%</u>
International contacts		16293,8			10 544	
Medical service					12 100	
Social policies		4071			5 386,9	
Financial assistance to regional and local budgets		374545		1 600	72 400	<u>4525%</u>
Other expenditures		33184				
Total expenditures on agriculture	23 430 075	27 580 319	<u>118%</u>	31 307 789	37 741 940	<u>118%</u>

Source: Draft Law "On execution of 2001 federal budget", Law "On 2002 federal budget", draft Law "On 2003 federal budget", www.agrodat.ru.

Table 2.

Subsidies to agriculture in 2001-2003, thousand rubles

	2001			2002	2003	% of change
	plan	execution	% of execution	plan	draft	
Support to livestock production	960 000,0	944 522,7	<u>98%</u>	1 060 000	1 195 000	113%
including						
Pure stock breeding	620 000,0	618 639,3	<u>100%</u>	670 000	745 000	<u>111%</u>
Subsidies for wool	270 000,0	255 996,7	<u>95%</u>	320 000	350 000	<u>109%</u>
Reindeer breeding	70 000,0	69 886,7	<u>100%</u>	70 000	100 000	<u>143%</u>
Support to crop production	550 000,0	554 274,3	<u>101%</u>	650 000	1 350 000	<u>208%</u>
including						
Elite seed growing	250 000,0	247 812,9	<u>99%</u>	270 000	270 000	<u>100%</u>
Subsidies for production of flax and hemp	70 000,0	84 533,8	<u>121%</u>	100 000	100 000	<u>100%</u>
Partial compensation of expenses on crop insurance	230 000,0	221 927,6	<u>96%</u>	280 000	980 000	<u>350%</u>
Other expenditures						
Building of federal reserve of veterinary drugs	150 000,0		<u>0%</u>			
Subsidies to utilization plants	40 000,0	38 869,6	<u>97%</u>	40 000	45 000	<u>113%</u>
Centralized supply of seeds to northern and high mountain regions				150 000	200 000	<u>133%</u>
Support to horticulture and viticulture				300 000	400 000	<u>133%</u>
Building of pesticide reserve	450 000,0			300 000	300 000	<u>100%</u>
Building of leasing fund	3 000 000,0	5 500 000,0	<u>183%</u>	2 780 000		<u>0%</u>
Building of federal seed reserve	150 000,0	150 000,0	<u>100%</u>	150 000		<u>0%</u>
Maintenance of subordinate institutions	2 570 000,0	2 887 690,2	<u>112%</u>	6 144 200	8 162 900	<u>133%</u>

	2001			2002	2003	% of change
	plan	execution	% of execution	plan	draft	
Other expenditures	300 000,0	1 038 928,9		1 819 500	2 027 500	111%
including						
Capital expenditures				864 500,0	864 500,0	100%
Other				955 000,0	1 163 000,0	122%
Expenditures on environment protection	59 400,0	59 372,2	100%	100 000		0%
Subsidizing of interest on received credits	1 398 300,0	1 293 880,1	93%	2 200 000	3 200 000	145%
including						
Short-term credits				1 400 000	2 000 000	143%
Long-term credits				800 000	1 200 000	150%
of them: subsidized crediting of port elevators' construction					130 000	
Soil fertility improvement program				4 751 000	4 533 400	95%
including partial compensation of mineral fertilizers' cost				2 600 000	2 082 400	80%
Program "Social development in rural areas"					1 470 000	
Grain market regulation subventions					1 027 000	
Total subsidies	9 627 700,0	12 468 099,2	130%	20 444 700	24 038 850	118%

Source: Draft Law "On execution of 2001 federal budget", Law "On 2002 federal budget", draft Law "On 2003 federal budget", www.agrodat.ru.

O. Shick

IET Business Survey: Industry

In November, the growth in effective demand stopped completely, as it was the case a year ago. After the October decline in growth rates by 12 balance points, in November the balance dropped further by 4 points and at the moment makes -1 %. In November, cash sales declined across all industries with the exception of non-ferrous metallurgy (balance is + 15 %), forestry and woodworking (+ 10 %).

However, the halt of growth in sales does not trouble Russia's enterprises as yet. The share of responses evaluating cash demand as "normal" decreased only by 3 points and makes 39 %. The maximal values of this indicator are registered in power engineering (76 %), non-ferrous metallurgy (88 %), and the forestry complex (62 %).

In spite of the apparent problems related to effective demand, enterprises have not yet increased amounts of non-cash transactions. Moreover, in November the amounts of promissory note and offset payments declined most intensively since the beginning of the year. At present, this decline is registered across all Russia's industries. A similar situation is observed as concerns barter transactions. Since March of 2002, the intensity of decrease in barter operations has been relatively stable in an interval from -10.. to -7 %. No industry demonstrated a growth in barter transactions in November. The most active decline was registered in the forestry complex (-16 %), and chemistry and petrochemistry (-12 %). As a result, about 80 % of industrial output were sold via cash operations. The largest volumes of cash sales were observed in power engineering (93 %), while chemistry and petrochemistry accounted for the smallest volumes of such sales (74 %). This indicator makes 80 % for mechanical engineering, 89 % for light industry, and 86 % for food industry.

The rates of growth in output, similarly to demand indicators, continue to decline for the second month running. After the maximum registered in September, the balance dropped by 16 points in two months, however, it remains positive, mostly due to the situation in power engineering and ferrous metallurgy. Growth in output was also registered in mechanical engineering (+ 7 % in terms of the balance) and food industry (+ 3 %). Other industries demonstrated either zero or negative growth in output.

Enterprises consider low demand and lack of working capital as the main constraints on the growth in output. About 55 % of enterprises constantly reported the lack of working capital in 2000 through 2002. At the same time, insufficient demand, which in the beginning of the year went up to the pre-default 65 % declined to 58 % in the 4th quarter in terms of its constraining influence on output. The third most frequently reported constraint was payment arrears (mentioned by one third of enterprises). Among six major constraints on increase in output, competing imports are reported least frequently. Only 16 % to 17 % of enterprises men-

tioned this factor in the end of this year, while in early 1998 it was a constraint on output of 13 % of domestic producers.

Enterprises adjusted their output taking into account the dynamics of sales, what allowed them to prevent excessive increase in finished stocks. In the four last months, balances of evaluation of finished stocks made from + 9.. to + 11 %. It seems probable that this level is most acceptable for Russia's enterprises as it is the same as in 2001, when the necessity to work out a new policy of management of finished stocks became apparent. At present lack of finished stocks is registered only in the forestry complex and construction industry.

The rates of decline in profits were registered at a somewhat lower level, however, real profits continue to fall in the industry on the whole and across individual industries. The most intensive decline in profit rates was registered in construction industry, chemistry, petrochemistry, and light industry. Growth in profits was registered only in power engineering.

Purchases of domestically manufactured equipment began to decline again in the end of the year. Although in the 3rd quarter the decline in this type of investment seemed to stop (the balance stabilized at zero), at present the balance again became significantly negative, and what is more, across all industries. At the same time, no decline in purchases of imported machinery was registered for the second quarter running. Fuel energy is primarily responsible for the fact that the balance of this indicator remains at zero in the industry at large. A minimal increase has been registered in mechanical engineering.

Estimates of changes in effective demand gathered 7 points in terms of optimism after in October they fell by 2 %. Power engineering, mechanical engineering, and the forestry complex accounted for this growth. Estimates remain negative across other industries where expectations of decrease in cash sales prevail.

Estimates of trends in barter remain practically without change since August of 2002. Enterprises expect a decline in this type of transactions at about -10.. to - 7 % (in terms of balance). No industry anticipates a growth in barter. Estimates of change in promissory note and offset transactions have again become negative. In a few next months, enterprises expect the most intensive decline in these types of transactions in the last 18 months. A growth in the amount of promissory note and offset transactions is possible only in power engineering and food industry. At the same time, enterprises demonstrate propensity to more often use promissory notes and offsets than barter operations in order to compensate the declining cash sales. Compensation forecasts are determined as the share of reports on increase in barter, promissory notes, and offsets in response to actual decrease in effective demand. The average share of such forecasts related to promissory notes and offsets was at 18 % in 2000, while it was at 14 % for barter operations.

Estimates of changes in output continue to loose optimism. In the last three months the balance dropped by 16 points. A decrease in optimistic reports was registered across all industries with the exception of power engineering and ferrous metallurgy, while non-ferrous metallurgy, chemistry, petrochemistry, construction industry, and light industry already anticipate a drop in production.

In a few next months Russia's enterprises plan to decrease purchases of both domestically produced and imported equipment. However, the purchases of domestic machinery will decline more intensively. A growth in purchases of imported and domestic equipment is probable only in food industry.

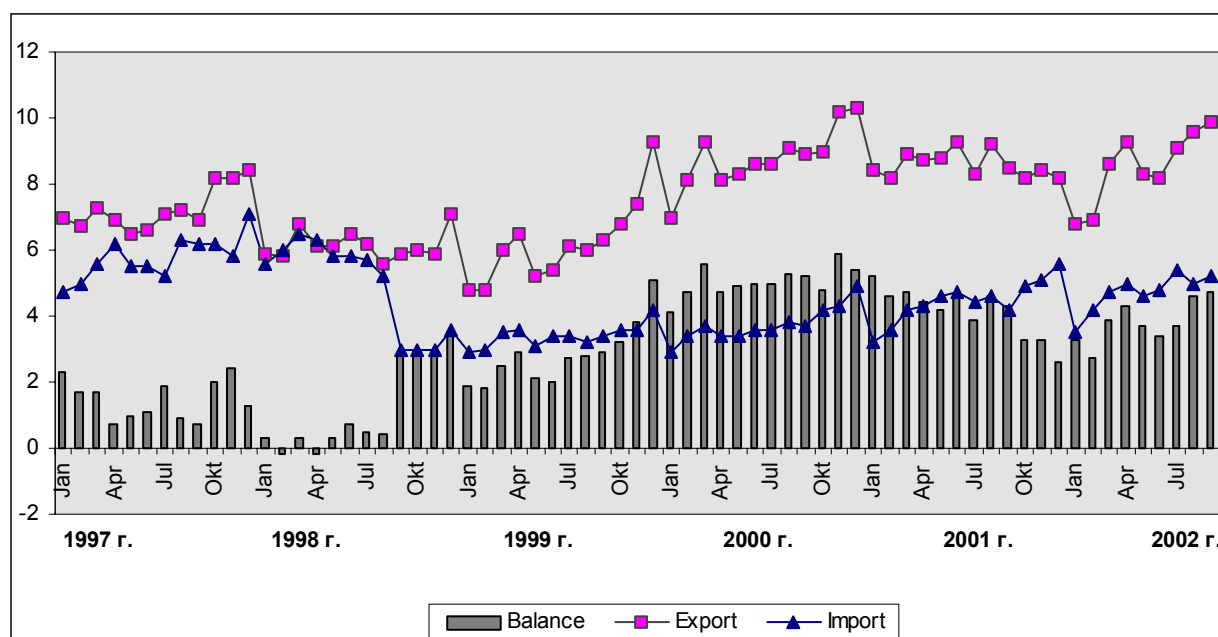
S. Tsukhlo

Foreign Trade

In September of 2002, the Russia's foreign trade turnover grew by 11 % in comparison with the figures registered in the respective period of the preceding year and made US \$ 15.1 billion (according to the balance of trade methodology). As compared with last August figures, this indicator increased by 3.4 %. In the situation of recovering world economy and improving world business situation observed since March of 2002 (especially, as concerns oil prices), in the few last months there was registered a recovery of the positive dynamics of export of goods. In September, exports made US \$ 9.9 billion (the record high in the last 20 months). The September imports also grew considerably and made US \$ 5.2 billion, what is by 23.8 % above the levels registered in the respective period of the preceding year.

The active balance of trade made US \$ 4.7 billion, what is by 9.3 % more than in the respective month of the preceding year. However, this indicator grew less considerably as compared with the figures observed in August of 2002 (by 2.2 %).

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



Source: RF Goskomstat

In September, the external business situation was rather favorable. The trend towards an increase in prices prevailed on the market of energy resources. For instance, the average world price of oil (Urals) made US \$ 18.3 per barrel in January, while in June it was at US \$ 23.0 per barrel (a growth by 25.7 %) and in September – US \$ 27.1 per barrel (a growth by 48 % in comparison with the January figures). However, in January through September of 2002, the average monthly price of this sort of oil was at US \$ 23.0 per barrel, what is by 5.7 % below the level registered in the respective period of 2001.

In September, a major factor behind the growth in oil prices was the refusal of OPEC member countries to increase oil extraction quotas. Besides, the danger of the US action against Iraq facilitated the growth in oil prices.

Russia has increased export customs duties on oil and oil products from US \$ 26.2 per metric ton to US \$ 29.8 per metric ton in connection with the growth in oil prices since December 1, 2002.

The price situation on the world market of non-ferrous metals only slightly differed from August figures, however, as concerns certain metals, it considerably improved in comparison with last September. For instance, in September of 2002, the average price of aluminum increased by 0.9 % in comparison with the August figures, while it decreased by 3.7 % as compared with the figures registered in September of 2001. At the same time, the average copper price did not change in comparison with the August figures, while it increased by 3.1 % as compared with prices observed in September of 2001. As concerns nickel, its average price decreased by 1.3 % in comparison with August prices, while growing by 30.8 % as compared with the figures registered in September of the preceding year. Therefore, the overall situation on the market of non-ferrous metals is better than in the preceding year, however, in the 3rd quarter there was observed its deterioration in comparison with the situation existing on the market in the past months of this year.

TABLE 1

The average monthly world prices in September of the respective year

	1996	1997	1998	1999	2000	2001	2002
Oil (Brent), USD / metric ton	22,9	18,12	13,1	22,6	32,15	26,18	28,26
Natural gas, USD / thous. m ³	2,743	2,251	1,858	2,62	5,118	2,204	3,6253
Gasoline, USD / metric ton	0,6484	0,579	0,4212	0,6825	0,9409	0,757	0,7969
Copper, USD / metric ton	1932,6	2032,7	1676,4	1876,8	2037,5	1452,9	1498,3
Aluminum, USD / metric ton	1428,3	1544,6	1391,3	1493,6	1600,2	1342,6	1294,7
Nickel, USD / metric ton	7426,4	6523,6	4229,8	6932	8654,3	5040,9	6592,5

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

The world market situation has favorably affected the Russia's foreign trade in the 3rd quarter of 2002. After a decline in exports observed in the first six months of this year, in the 3rd quarter exports grew by 12 % in comparison with the figures registered in the respective period of the preceding year.

The situation also improved as concerns imports. While in the first six months of 2002 rates of growth in imports were below those observed in the preceding year, in the 3rd quarter the dynamics of imports improved and they increased by 18.3 % in comparison with the figures registered in the respective period of the preceding year.

A factor behind the growth in imports was the real Ruble appreciation and, as a result, increased competitiveness of imports in terms of prices, as well as a growth in real disposable household incomes and investment demand on the part of enterprises and organizations, a part of which was satisfied at the expense of imports.

In September of 2002, imports from countries outside the former Soviet Union increased by 25.7 % in comparison with the figures registered in September of 2001. The increase in imports was observed across all major commodity groups: foods – by 29.5 %, chemicals – by 20.6 %, textile products and footwear – by 37.4 %, and products of mechanical engineering – by 32.4 %.

In September, the turnover of Russia's trade vis-à-vis CIS countries made US \$ 2.51 billion. Exports made US \$ 1.48 billion increasing by 19.3 % in comparison with the figures registered in September of 2001, while imports grew by 10.4 % and made US \$ 1.03 billion).

As concerns the sphere of exports, there was registered a growth in fuel and energy resources. Exports of crude oil and foodstuffs increased most significantly. At the same time, monthly exports of machinery and equipment continued to fall.

Imports from CIS countries were as before dominated by products of mechanical engineering, foods, and agricultural produce, which accounted for about 20 per cent of imported products. There was observed a growth in imports of quick frozen meats, quick frozen fish, and chocolate products.

At the same time, there was registered a decline in imports of dry and condensed milk, sunflower oil and butter from CIS member countries as a result of re-orientation towards Russia-produced goods.

In November, the RF State Duma ratified the agreements on the principles of collection of VAT and excises in bilateral trade Russia had made with Georgia, Moldavia, and Uzbekistan. The agreements envisage that participant states should use the principles of VAT collection in the country of destination. Goods, imported from the customs territories of participating states should be subject to excise taxes at zero rates. At the same time, natural gas, oil, and gas condensate should be excluded from this rule. Services related to freight and servicing of exported and transit goods, transport of passengers and baggage should be subject to zero VAT rates in the state whose taxpayers provide the respective services.

This year, the countries which are members of the Customs Union, for instance, Kazakhstan, completed the transition to collection of excise taxes on the country of destination principle. As a result, there was registered a natural decline in bilateral trade between Russia and Kazakhstan, which, it seems, is of a temporal nature. In the second half-year of 2002, there were already observed positive shifts in this sphere. However, in the first 9 months of 2002, the trade turnover of the two countries decreased by 15 % in comparison with the indicators registered in the preceding year and made US \$ 3.12 billion. It shall be noted that Russian exports to Kazakhstan declined more (almost by 20 %).

The staple Russia's exports to Kazakhstan are fuel and energy goods, machinery and equipment, chemical products. In its turn, Russia primarily imports machinery and equipment, which make one fourth of its total imports from Kazakhstan. Chemical products, metals, and metal products account for about 15 % Russia's imports from Kazakhstan.

As concerns customs regulations, there are certain differences between the legislation of two countries. For instance, in Kazakhstan exists only one rate of VAT (16 %), while export duties are practically absent (only 10 commodities, including scrape non-ferrous and ferrous metals, hides, and wool, are subject to export duties).

As concerns the levels of customs tariffs, it shall be noted that rates are similar only for about a half of goods included in the general commodity register. At the same time, in comparison with Russia, Kazakhstan maintains higher rates of customs duties on 60 % of goods.

Both Kazakhstan and Russia are planning to approve new customs codes soon, what may render more difficult the unification of rates of customs tariffs and excise taxes.

Customs authorities of Russia actively cooperate with their counterparts in Belorussia, which is also a member of the Customs Union. In November, there was held a meeting of representatives of customs agen-

cies of these countries, where the parties agreed to conduct random audits of export import transactions in order to prevent smuggling of a wide range of goods using Russian and Belorussian trade marks. The measure is primarily aimed at the prevention of illegal traffic in oil products and non-ferrous metals. It was also envisaged to work out model plans of joint actions with regard to external economic activities of the fuel and energy complex, turnover of tobacco and alcohol products, as well as smuggling of metals, timber, and oil and natural gas products.

On November 20, China introduces prohibitive customs duties on imported cold rolled metal products, which will affect exporters from Russia, Korea, Taiwan, and Japan. Chinese officials, who conducted an antidumping investigation, initiated in accordance with the claims submitted by the local association of entrepreneurs this May, set a 20 % duty on the exports from Russia. However, this protective measure will have only a little effect on the Russian producers in the short time perspective. Russian exporters will be granted a quota for cold rolled products. Exports within the quota should not be subject to import duties, and the amount of shipments from Russia will hardly exceed the respective maximum. For instance, the quota set for the period from May of 2003 to May of 2004 makes more than 800 thous. metric tons, and will be increased in the future. In 2001, Russian exports to China made only about 600 thous. metric tons of cold rolled metal products. Therefore, Russia will be able to export even more rolled products to China than before the introduction of these sanctions. China annually imports up to 25 million metric tons of rolled products and steel, and the demand of the Chinese market of metal products grows most constantly and dynamically. Therefore, in the future Russian exports may increase and exceed the quota, what may result in a significant decline in profitability of exports to China.

In November, Russia and the USA signed an amendment to the comprehensive agreement on steel concluded in 1999. According to the amendment, Russian producers have the right to export 1.2 million metric tons of steel slabs to the USA this year (previously the volume of respective exports was limited to 1 million metric tons). The agreement on thick sheets is also favorable for Russia: the agreement takes into account the market status of the country and abolishes the existing quotas and price limits. According to the agreement, Russian producers will have to submit quarterly reports on the production costs of their products to the US authorities. Our partners will set minimal prices basing on the respective information.

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