



## RUSSIAN ECONOMY: TRENDS AND PROSPECTS

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## RUSSIA'S ECONOMY IN SEPTEMBER 2012: PRELIMINARY DATA AND MAJOR TRENDS

### ***The Political Background: Pensions in the Cross-Hairs***

*The beginning of the autumn was marked by an onset of fundamental conflicts in the ranks of the new Russian government and by some fresh signs of political reaction fomented in the State Duma by United Russia deputies. President Putin publicly expressed his dissatisfaction with the federal budget's draft for its failure to secure the achievement of the targets set by the President's executive orders, and also with the government's delay in producing a properly coordinated plan of pension reform. As a result, the plan of reform, which the RF Ministry of Labor and the other ministries constituting the government's economic block had failed to agree upon in August, was now, at last, submitted for government consideration. In the main, the new plan closely follows its initial version. According to the draft, the pension reform is aimed at reducing the pension fund's deficit in the medium-term perspective. The reform is clearly redistributive at the expense of the funded component of the pension system. The second conflict situation that emerged in September was manifested by the growing disagreements between the government and the head of Rosneft Igor Sechin, who is eager to maintain his grip on the dividends of the state-owned Rosneftegaz company and to use them for the purpose of further expansion in the oil and gas sphere. This conflict is being heated up by the personal rivalry between Sechin, believed to be one of the officials closest to Putin, and Prime Minister Dmitry Medvedev.*

*So far, the key highlights of the autumn 2012 session of the State Duma were the unseating of the deputy head of the Fair Russia faction, Gennady Gudkov, and the introduction into the State Duma of a draft law designed to make it a criminal offence "to offend religious feelings". The unseating of Gudkov, based on the decision of a State Duma commission, seems to have been politically motivated (Gudkov has taken an active part in the protest movement and clearly displays the ambition to become one of the leaders of the non-systemic opposition). Also, the legitimacy of Gudkov's dismissal is very questionable from the constitutional point of view, because his "guilt" as a parliamentarian was established in a non-judicial process. As far as the draft law designed to introduce greater accountability for "offending religious feelings" is concerned, it obviously follows the trend toward the clericalization of Russia's public life and toward the strengthening of the repressive character of her legislation. Apparently, the Kremlin is going to continue its onslaught on the opposition: the authorities have announced that more arrests will be made in the Bolotnaya Square case. The new tactics used by the authorities in persecuting the opposition involved relying on the mechanism of prejudice: one of the accused is enticed to strike a deal with the prosecution; once the deal has been struck, the court will deem his or her guilt to be proven on the basis of their own admission thereto; as a result, the objective fact of the criminal deed will be deemed to be established, thus making it possible for the court to convict the other co-defendants in the case. These tactics will apparently also be used against suspects in the Bolotnaya Square case, and against one of the opposition leaders, Aleksey Navalny, who is implicated in the far-fetched Kirovles case.*

*The political course of the Kremlin was further confirmed by the public refusal of State Duma Speaker Sergey Naryshkin to attend the October Session of the PACE, where a tough resolution on Russia's non-implementation of her obligations before the Council of Europe was to be discussed and adopted.*

### ***The Macroeconomic Background: Money Comes...And Goes***

*In September, the macroeconomic situation was determined by external events: the expectations of the Federal Reserve's decision to begin a third round of quantitative easing and then the decision itself caused a wave of hectic trading on the markets, which generated a sharp rise in*

raw materials prices and stock exchange indices. As a result, on 15 September the price of Brent crude oil hit a several-month high of \$ 116.9 per barrel. Over the course of the first two weeks of September, the MICEX and RTS indices rose 8% and 14% respectively. These same factors also determined a substantial strengthening of the ruble against the US dollar in the first half of September. However, a sharp drop in global oil prices in the next four days (the price of Brent crude plummeted by 9%) revealed the profiteering nature of the preceding rise in prices and indices. Russia's stock indices rapidly and radically descended, and the ruble weakened against the US dollar. As a result, by the end of September the value of the bi-currency basket had dropped from Rb 36.24 to Rb 35.25.

At the same time, oil prices remained high: in September, the average price of Urals crude amounted to \$ 111.56 per barrel, and its level over the period of January–September 2012 remained at \$ 111.02 per barrel, which practically corresponds to its last year's level of \$ 109.48 per barrel. However, this means that 2012 will be the first post-crisis year showing no increase in the price of oil in annual terms (in 2010 and 2011, it had grown by 30% and 40% respectively). It is noteworthy that this circumstance has already resulted in a considerable narrowing of Russia's trade surplus.

The most important trend in Russia's dynamics was the ongoing acceleration of inflation, which had begun in mid-summer. In August 2012, the monthly inflation rate amounted to 0.1%, while in August 2011 Russia experienced deflation of 0.2%. Over the period from 1 September to 24 September 2012, the Russian Consumer Price Index climbed up by 0.5% (vs. zero-rate inflation in September 2011). As a result, annual inflation in September rose above 6%, while the inflation rate since the beginning of the year amounted to 5.1%, which was considerably higher than last year's index (4.6%). Among the various driving factors behind this rise in prices, one should note the step-by-step increase in state-regulated tariffs and the growth in food prices. The latter trend is typical of global markets (many experts consider it to be one of the consequences of the excess liquidity created by the loose monetary policies pursued by the developed countries). It seems likely that this trend will continue to exert significant influence on the inflation situation during the whole autumn of 2012.

The rising threats of inflation were the most important reason for the Bank of Russia's decision to increase by 0.25 pp, from 14 September 2012, its refinancing rates and the other key interest rates on liquidity provision and absorption operations; the refinancing rate was set at 8.25%. Thus, after a nine-month interval, the regulator returned to the rate that existed from 3 May 2011 to 26 December 2011. Although the Bank of Russia's representatives expressed their confidence that the rate increase would have no negative consequences for economic growth, it should be admitted that the choice between inflation and economic growth was not made in favor of the latter, which is contrary to the practices of the developed countries but corresponds to those typical of a number of developing economies. Also, experts believe that one of the reasons for increasing the refinancing rate was the excessively high growth rates of consumer lending. According to First Deputy Chairman of the RF Central Bank Aleksey Simanovsky, consumer loan growth over the course of 2012 will amount to 20–25%. However, the rise in the interest rate on loans will undoubtedly have a notable impact on the behavior of consumer demand.

In August, the excess reserves of commercial banks continued to decline. By the end of that month, they amounted to Rb 889.8bn (-11%). The situation with bank liquidity did not change, and the banking sector continued to experience liquidity shortage, as was shown by the movement of the growth rate of borrowings from the Bank of Russia. In August 2012, banks' asset growth slowed down owing to a decline in the growth rates of the main types of attracted resources – foreign liabilities and the assets of enterprises and organizations. However, a considerable rise in government assistance and a reduction in investments in foreign assets made it possible to prevent a decline in the volume of lending to the economy.

According to the Bank of Russia's preliminary estimates, in Q3 2012 capital outflow from Russia amounted to \$ 13.6bn, which represented a moderate increase on Q2 2012 (\$ 9.7bn). On the whole, since the beginning of 2012, capital outflow from Russia has climbed up to \$ 58bn. The RF Government has already announced that it expects full-year capital outflow to be at the level of \$ 65bn. However, it should be noted that such forecasts (constantly failing to materialize) are

more therapeutic than analytical. For their part, analysts working for commercial banks (for example, Alfa Bank) predict that in Q4 2012 capital outflow from Russia will amount to \$ 20bn.

Thus, Russia's persistent macroeconomic stability looks very vulnerable, which makes it impossible to accumulate capital and to allocate it for economic development, as is apparent from capital outflow data, the rise in inflation risks, and the behavior of stock markets.

### ***The Real Sector: The Investment Passivity and the “New Normality”***

The main trend of the past few months was a notable decline in macroeconomic dynamics, brought about, in particular, by the ongoing slowdown in investment activity taking place against the background of contracting external demand and unstable internal demand.

Over the period of July–August 2012, the parameters of the basic types of economic activity continued to display further weakening. The industrial production index in August 2012 was 102.1% against 106.2% in August 2011, including for mineral resources extraction – 100.8% against 103.3%; and for processing industries – 104.1% against 107.1% respectively. GDP growth in the 2<sup>nd</sup> half-year 2012 is estimated to be at the level of 102.7% on the corresponding period of the previous year, and the 2012 full-year results against 2011 will amount to 103.5%.

From June 2012 onwards, there has been noted a slowdown in the per annum retail turnover rate. The retail turnover index in August 2012 was 104.3% on the corresponding period of the previous year, including 100.8% for foodstuffs and 107.4% for nonfood commodities. An alarming phenomenon in this situation is the accelerating rates of growth displayed by the population's real income and real wages, which increased by 7.2% and 7.8% respectively on August 2011. On the one hand, the rapid movement of these indices functions as one of the few available drivers of production growth. On the other hand, the upshot of the growth of production costs in response to rising wages is the deteriorating overall result of production activity. Increasing basic rates and the interest rates on consumer credits will have a negative effect on one of the most dynamic demand sectors – the demand for nonfood commodities.

The situation with regard to investment is also pessimistic. In June–August 2012, the movement of investment in fixed assets became weaker, production volume in the construction sector declined, and the housing construction indices demonstrated sharp fluctuations. The volume of investment in fixed assets over the period of January–August 2012 amounted to Rb 6,206.8bn, which represented a 8.8% increase on the corresponding period of the previous year. Meanwhile, in July the per annum rate of growth of investment in fixed assets dropped to 3.8%, and in August – to 2.3% against 107.0% in August 2011. In view of these developments, growth of investment in fixed assets in the 2<sup>nd</sup> half-year is expected to be at the level of 102.4%, and the 2012 full-year results against 2011 will be 105.5%. In the structure of investment funding sources, the downward trend displayed by the share of bank loans (including loans issued by foreign banks) and corporate borrowings became more prominent. The volume of production in the construction sector remained almost at the same level as in August 2011.

Foreign investment in the Russian economy in the 1<sup>st</sup> half-year 2012 amounted to \$ 74.8bn, which is 14.7% below the index for the 1<sup>st</sup> half-year 2011. As of 1 July 2012, the amount of accumulated foreign investment in Russia, including investment from the CIS countries, was \$ 334.7bn, which is 3.6% below the level achieved as of 1 January 2012. It should be reminded that in Q1 of the crisis year 2009 the accumulated investment volume dropped by 8.3%, then it began to increase throughout the entire pre-crisis period, and only in the 1<sup>st</sup> half-year 2010 this index demonstrated a decline by 2.08%.

However, the Gaidar Institute's surveys of industrial enterprises have demonstrated that in late summer their optimism somewhat increased, thus giving rise to hopes that the aforesaid trends may become weaker or altogether disappear. After several months in a row when demand estimates (both actual and expected) had been declining, they displayed an improvement. Nevertheless, these improvements should be interpreted with due regard for the ongoing adaptation of enterprises to the situation of reduced demand (‘a new norm’): thus, in late 2010 – early 2011 the level of demand was considered to be normal if it ensured capacity load at the level of 76–77%; at present, the level of 72–73% is estimated by industrialists to be satisfactory. As result, demand forecasts for Q3 2012 display a zero balance: growth expectations are equally balanced against

*the expected decline in sales. On the one hand, such a situation appears to be better than the increasing pessimism observed in Q2 2012, when the balance of expectation lost 13 points over the course of three months and reached a three-year low. On the other hand, it points to a high level of uncertainty, because enterprises give up their plans for replenishing their stocks, are very moderate in regard of increasing any further the prices of their products, and are more strongly orientated towards cutting their personnel number. The plans of enterprises give no indication of any changes in their human resources policies: in August, the initial balance of employment forecasts went down by another 6 points (or 4 points when cleared of seasonality), and so dismissals of workforce in industry will continue – more likely, with increasing intensity. ●*

## THE POLITICAL AND ECONOMIC RESULTS OF SEPTEMBER 2012

S.Zhavoronkov

*According to many experts, the main event on Russia's political scene in September was the public criticism, by RF President Vladimir Putin, of a number of government ministers, which immediately cast doubt on the future of Dmitry Medvedev's government. A number of conflicts within the RF Government have become more heated, especially those fueled by the reluctance of Ivan Sechin, head of Rosneft and Rosneftegaz, to transfer to the budget the enormous incomes of Rosneftegaz. Instead, he wants these incomes to be directed to finance the further expansion of his companies. Faced with opposition from most of the ministers, it is likely that Ivan Sechin will be forced to back down on this issue. Also, arguments flared up in the corridors of power with regard to the promised ban on government officials owning assets abroad – many top members of the United Russia party, including Dmitry Medvedev, have in fact called for putting the brakes on the new draft law. The endless reforming of criminal law continues unabated – after abolishing some dubious norms, the authorities have immediately introduced some new ones, no less dubious.*

According to many experts, the main event on Russia's political scene in September was the public criticism, by RF President Vladimir Putin, of a number of government ministers, which immediately cast doubt on the future of Dmitry Medvedev's government. The crux of the matter was as follows. Vladimir Putin announced that the current version of the draft budget for 2013 failed to make good on his presidential campaign promises. He also said that the timelines for preparing government documents on pension reform had been heavily disregarded: "What date is it today? The 18<sup>th</sup>. And what have we agreed? That by the end of September the Government will submit written proposals on the development of the pension system. We haven't received anything yet. How are you planning the budget for next year and the following years without addressing one of the key challenges facing the economy? [...] The Minister's job involves a personal responsibility for the sector. [...] I want you to know that this is nothing personal". In this respect, Vladimir Putin ordered that disciplinary measures in the form of a reprimand be taken against Regional Development Minister Oleg Govorun, Minister of Labor and Social Protection Maxim Topilin, and Minister of Education and Science Dmitry Livanov. It should be noted that, as far as pension reform and the draft budget are concerned, the said ministers are mere backbenchers with little say in these matters. Most likely, they have drawn the ire of the President because they are novices in their ministerial positions and, more importantly, cannot boast of any long-standing personal relations with Vladimir Putin. As regards the reprimands, Putin could have started with himself; for example, he could have applied this disciplinary measure against himself and Dmitry Medvedev – the sad fact being that, in violation of Article 170 of the RF Budget Code, the presidential budget messages have been published, for many years in a row, not in March but in the summer. Although the flaws of pension reform and the growing problems with maintaining the current pension system have been apparent for many years, Putin has not only refrained from taking any political decision on these matters, but he has repeatedly increased pensions for many categories of pensioners – even in excess of the requirements stipulated in legislation on the mandatory inflation adjustment of pensions.

The second conflict in the RF Government was concerned with the future of *Rosneftegaz*. Having been established in 2004 as the formal owner of state-owned shares in *Rosneft* and part of shares in *Gazprom*, *Rosneftegaz* paid (small) dividends only once – in 2007. As a result, *Rosneftegaz* accumulated no less than Rb 100bn, or maybe Rb 160bn (if the additional dividends already approved by the state companies are taken into account). The new head of *Rosneftegaz*, former vice prime minister Ivan Sechin (appointed this year), who simultaneously heads *Rosneft*, is one of the most powerful favorites of Vladimir Putin. As early as this spring, he lobbied a rather strange edict of the RF President stipulating that the above-mentioned funds could be spent on some mysterious

“*additional capitalization*” of enterprises of the fuel and energy complex for the purpose of their possible privatization. The meaning of the word ‘privatization’ as applied in this context is not absolutely clear. One of the most probable interpretations could be a take-over of some state enterprise by another such enterprise – in this case, *Rosneftegaz*. It should be noted, however, that the edict did not specify any concrete mechanisms – maybe because of the difficulty to invent them. The edict notwithstanding, in the summer and autumn of 2012 Prime Minister Dmitry Medvedev, Vice Prime Minister Arcady Dvorkovich, and a number of influential ministers began to demand that almost all the funds of *Neftegaz* should be transferred to the federal budget. The proponents of this move included RF Minister of Energy Alexander Novak and RF Minister of Finance Anton Siluanov, who called for 95% of *Rosneftegaz*’s capital to be transferred to the budget. The pro-budget politicians repeatedly made their voice heard on the public arena. Ivan Siluanov eagerly followed suit and publicly opposed the views of his ministerial colleagues. In so doing, Siluanov hinted that in that controversy he enjoyed personal support of Vladimir Putin – in particular, he announced that he was ready to implement the relevant decisions if they were to be taken by the RF President (although formally *Rosneftegaz* must also obey the RF Government’s orders).

A very broad coalition is being formed against Sechin who has also aired his plans that *Rosneft*, apart from the aforesaid assets, should also take over *TNK-BP*. This coalition against Sechin, who is known to control many top managers and officials representing a wide range of institutions from state-owned banks and state companies to ministries and departments, include some former Sechin’s loyalists – for example, big oil men from *TNK-BP*, *Bashneft* and *Surgutneftegaz*. In September, *Alfa-group*, a consortium of Russia’s private shareholders in *TNK-BP*, announced its readiness to buy out *BP*’s 50% stake in *TNK-BP*, and thus to become, in effect, *Rosneftegaz*’s bidding competitors. As *Alfa-group*’s move represents a direct challenge to Sechin, it is clear that its shareholders have carefully assessed all the possible risks involved in their initiative. Other oil men are displeased with *Rosneft*’s attempt to monopolize oil extraction on Russia’s continental shelf, especially in light of this company’ failure to achieve any real success in this field over the course of recent years. The ministers belonging to the ‘economic block’ of the RF government would like to resolve the existing problems of the federal budget at the expense of *Rosneftegaz*. So far, it seems that the anti-Sechin coalition has better chances to obtain Vladimir Putin’s support, if for no other reason than its numerical strength.

As far as the future of Prime Minister Dmitry Medvedev is concerned, this is a problem in its own right, and, frankly speaking, we do not believe that he will resign anytime in the near future. Firstly, his resignation would deliver yet another blow to the official propaganda campaign concerning the “tandem” etc. Secondly, Medvedev avoids direct conflict over the afore-said issue, and prefers to express the median point of view of many influential officials. Whenever he fails to gain their support, he simply keeps silent.

In September, the autumn 2012 session of the RF State Duma traditionally began with a series of repressive and liberal legislative acts. The latter had long been promised in the context of numerous declarations made by Russia’s leaders, while the aim of the new repressive measures was to scare both the existing political opposition and its potential participants, and especially sponsors. In particular, the State Duma stripped Gennady Gudkov, one of the leaders of the *Fair Russia* party, of his seat in parliament. Gudkov, formerly a member of Russia’s security services and then head of a number of private security firms that can be characterized as medium-sized businesses, was deprived of his mandate in accordance with an absurd and previously dormant legislative norm stipulating that members of parliament have the right to expel one another for his or her involvement in commercial activities, whereas the fact of this involvement should be established by themselves<sup>1</sup>. The actual reason for Gudkov’s expulsion was quite different – in the winter, Gudkov repeatedly called for his party to actively cooperate with the organizers of mass opposition rallies, while all the other leaders of *Fair Russia* preferred to keep silent. Also, in September 2012, a charge of “hooliganism motivated by political hatred” (which can carry a fine or deprivation of freedom) was brought against the owner of National Reserve Bank, Alexander

1 In Gennady Gudkov’s case, his detractors presented the minutes of a meeting of the board of directors of the enterprise in question, signed by Gudkov, who insists that the minutes were fraudulently forged. The authenticity of the minutes has never been tested.

Lebedev, known, among other things, for subsidizing the opposition, and, first of all, the opposition newspaper “Novaya Gazeta” (The New Gazette). The case in point was Lebedev’s having punched another businessman, Sergei Polonsky, during one of last year’s live debates on the NTV television channel. It should be added that the fight resulted in no injuries to Polonsky.

A new draft law was introduced in the State Duma, which proposed that the RF Criminal Code should be amended with a new article, 243.1, “*Offense of the Religious Beliefs and Feelings of Citizens and (or) the Desecration of Religious Buildings, Sites of Pilgrimage and Objects or Locations Used for Performance of Religious Rites and Ceremonies*”. On the pretext of the act of hooliganism (deeply disapproved in society), committed by three members of the Pussy Riot punk band, who were later sentenced to three years of deprivation of freedom (considered by many as too harsh a sentence), some political forces have been trying to introduce a new criminal code article for the purpose that was obviously not limited to protection of religious sites from performers of bawdy songs. In a nutshell, the draft law is aimed at criminalizing any religious utterances arising against the background of negative attitudes among the followers of different religions and the mutual hostility of atheists and religious believers. Some precedent has already been set towards criminal persecution of politicians for their views on religion (e.g. the trials, under the “anti-extremist” Article 282, of Yu. Samodurov and Igor Artemov – it is rather amusing that the former was charged with offending the Russian Orthodox Church, while the latter – with propagating the views of the Russian Orthodox Church). In addition to being ridiculous, these cases are extremely scandalous: they are initiated by the authorities; the prosecution cases are extremely unconvincing and unsubstantiated, etc. By contrast, the new draft law when passed will make it possible to represent such judicial cases as private disputes concerning the violation of one person’s right by another person. Moreover, the State Duma has adopted a number of amendments to the RF Criminal Code, making still more intricate the articles concerning high treason. Especially unhelpful are the amendments expanding the definition of high treason by such activities as “financial, material and technical, consultative or other assistance to a foreign state, a foreign or international organization, or to representatives thereof, in a way jeopardizing the RF’s security, including her constitutional order, sovereignty, and territorial and state integrity”. It should also be said for the sake of justice that the existing norms, which are likewise dubious enough, have so far never been applied against dissidents”.

At the same time as these legislative initiatives, the RF Ministry of Economic Development, in pursuance of Vladimir Putin’s May edict, introduced for consideration of the Russian Government a number of draft alterations to the RF Code of Criminal Procedure, changing the procedure for initiating criminal proceedings under the articles frequently used for the persecution of entrepreneurs. First of all, alterations are suggested to be made to Article 159 (fraud), Article 160 (appropriation or embezzlement), and Article 165 (infliction of damage on property by way of deceit). These articles are actively used, and each year tens of thousands of people are sentenced under them. Many of those sentenced are convicted in spite of absence of any victims – that is, the persons who could claim to have been defrauded. In particular, the proposed alterations would make it possible to initiate such proceedings on the basis of a statement submitted by a defrauded person. Such a solution can only be welcomed, although the prospects for these drafts to be approved by the Government are not completely clear. Moreover, there remains a second problem, equally serious: Russia’s legislative, law-enforcement and judicial practices make it possible for a person to be convicted of a crime in absence of any physical evidence of his or her guilt, merely on the basis of another person’s statement (for example, as in the notorious *Euroset* case, when ten people got prison sentences based on the evidence submitted by one individual). The case against the accused was later dropped, but by that time they had already spent several years behind bars, and the principle which made possible their imprisonment is still being used).

The afore-said legislative initiatives in the field of criminal law clearly indicate that the Russian authorities do not want any clear and strict legal norms to be established, while the net effect of all the hectic legislative activity of the State Duma has turned out to be close to zero – having improved and clarified one norm, the authorities immediately introduce a number of other vaguely formulated norms. Such a policy can only be explained by the ruling elite’s desire to preserve its ability to bring criminal charges against practically anybody and to create intense fear of the



State's repressive apparatus. However, bearing in mind the current growth in mass protest, the existing repressive services will simply be too understaffed and overworked to cope with the ever increasing flow of malcontents. And it should be added that, unlike in the provinces, feelings are still running high in Moscow. On September 15, the *March of Millions* protest rally, organized by the Opposition in Moscow, was attended by 20 to 30 thousand people – a very impressive figure, although it is several times lower than those recorded last December, at the peak of Russian protest activity. As regards the provinces, the culture of street protests has failed to emerge there as yet, although protests do take place there – for example, in the form of hunger strikes against *United Russia*. In this respect, the state of affairs will be clarified next month, when elections will be held in more than half a dozen Russian regions.

As expected, the summer lull was followed by an increasingly lively public discussion of the summer 2012 initiatives announced by *United Russia* and supported by Vladimir Putin – that it should be made illegal for Russian civil servants to own real estate abroad. The draft law put forth by *United Russia's* MP Vyacheslav Lysakov envisages that Russian civil servants should be deprived of the right to own real estate abroad and to hold foreign bank accounts. According to the draft law, civil servants should get rid of any such assets within six months after the date of entry into force of that law, and the failure to abide by it should be punishable, including by deprivation of freedom for five years. The aim of the draft law was to highjack the opposition's pet theme of fighting corruption and putting an end to transfer of assets abroad. Also, the draft law was intended to demonstrate Russia's readiness to the possible introduction of international sanctions against her leaders. The Russian opposition has long been calling for the developed countries of the world to impose entry bans on corrupt officials and human rights abusers. In recent years, Russian diplomacy has managed to successfully beat off most of those initiatives, which remain confined to parliamentary talk-show and never become binding. Even in the USA, where one of such bills (the "Magnitsky List") was frequently on the verge of passing into law, the Obama administration and various lobbyists have so far managed to block its adoption. However, the example of Belarus indicates that such a scenario is anything but implausible. Also, it should be reminded that, several years ago, on the initiative of tiny Estonia, EU entry bans were imposed on the then Russian minister Vasily Yakemenko and his team-mates, who were accused of having violated the inviolability of Estonian diplomats. These bans have not been lifted so far in spite of Russia's and Europe's diplomacy efforts to influence Estonia with regard to this issue. Prime Minister Dmitry Medvedev, following in the footsteps of a number of other influential members of *United Russia* (for example, head of the *United Russia* faction in the State Duma Andrei Vorobiev), has called for a serious revision of Lysakov's draft law. Medvedev said that a ban for civil servants to own real estate abroad would be "senseless": *"I do not think that if we scare businessmen with such laws and tell them: 'If you want to get a job in the civil service, you better hide everything somewhere, and then we'll employ you', this will improve our civil service and will ultimately help strengthen law and order in our country"*. According to Medvedev, the best alternative to the proposed ban would be declaration of income and certain expenses (it should be noted, however, that mandatory income declaration has already been introduced for Russian civil servants and parliamentarians, and it is only owing to this measure that the numerous overseas assets belonging to officials and MPs, and especially to those with a big-business background, have come to light) and a ban for civil servants to hold foreign bank accounts.

Although Dmitry Medvedev's personal opinion is not very important *per se*, in this particular instance he expressed a point of view shared by many other dignitaries. It is not by chance that the Press Secretary to the RF President, Dmitry Peskov has made a very conciliatory statement with regard to the controversy around the proposed ban: *"There are some arguments for it and some arguments against it. It has both proponents and opponents. Yes, there were United Russia activists at the Penza meeting, and United Russia holds a majority of seats in the State Duma. Let us see what approach to this issue they will take. There will be a second reading, there will be amendments; officials are a sensitive matter, when one should not leap before looking. The whole issue will be discussed in parliament"*. It is likely that the fate of "Lysakov's Draft Law" will be trivial – it will be radically altered and then passed into law, exactly as five or seven years ago the State Duma passed into law the once awe-inspiring legislative initiatives aimed at reigning in Russian offshore

companies and disclosing their beneficiaries (and very soon it became clear that their implementation was not in the best interests of Russia's leadership).

In September, the latest APEC summit held in Vladivostok reached its conclusion. In Russia, the main consequence of that summit was the discussion of its expense budget, which has grown more than six times since its approval in 2007 – to almost Rb 700bn. Apparently, the discussion was thought to be so important that even Vladimir Putin took an active part in it. He justified the expenses by emphasizing that half of the money went into building an underwater gas pipeline from Sakhalin to Vladivostok. However, he neglected to mention the fact that the feasibility of this project is far from being clear. These worries were once again reignited by Russia's having signed at the APEC Summit a number of declarative preliminary agreements with Japanese companies for the construction of a re-gasification terminal near Vladivostok. In the absence of any agreements with APEC countries for further natural gas exports, the current capacity of the pipeline is clearly excessive. It would have been much cheaper and more logical to build a re-gasification terminal for the reception of liquefied natural gas from Sakhalin. Moreover, bearing in mind the fact that the terminal will be built in any case, it is by no means evident why we should need the pipeline at all. Expenses on other projects have also soared enormously, and yet lots of them remain unaccomplished (the hotels are not finished and the water main to Russkii Island has not been built). The reasonability of some of these projects is open to question (for example, the newly constructed floor area of Far-Eastern University is comparable with that of Moscow State University, but the available number of students is clearly insufficient to make proper use of it). As far as the signed business agreements with any financial parameters are concerned (other agreements, like "Vladivostok-LNG", are simply non-binding declarations), only one of them, the agreement between the Japanese Mitsui company and the Russian IST group – which establishes a rail freight joint venture – is relatively noteworthy. However, the value of this contract is incomparable with Russia's expenditures on the Vladivostok Summit, the latter amounting to \$ 100m. ●

## INFLATION AND MONETARY POLICY

N.Luksha

*In August, the consumer price index was the lowest in the current year and amounted to 0.1% (against 0.2% decline in August 2011). The main inflation curbing factor was the inflation decline in food prices (-0.5%). The second phase of regulated tariffs indexation urged the acceleration of inflation in September, which made 0.4% within 17 days. As a result, cumulative inflation from the beginning of the year exceeded the relevant indicator of the previous year, amounting to 5% as of September 17 (vs. 4.6% in 2011). Foreign currency and gold reserves in mid-September reached the maximum peak of the four months and amounted to \$522.8bn. From September 14, the Bank of Russia has tightened the monetary and credit policy, having raised the interest rate by 0.25 p.p. to 8.25%. On September 21, the Bank of Russia decided to reduce the maximum interest rate on deposits from October 1.*

Belated seasonal decline in foodstuffs prices encouraged an expressed inflation decelerating in August: as per the month results, the consumer price index has reached 0.1%, which is the lowest indicator for this year (in August 2011, deflation by 0.2% was noted). Regardless price reduction for fruit and vegetable products, growth rate for other foodstuffs was positive and amounted to 0.8%. In view of grain crop wreckage, the utmost price growth was observed in bread and bakery products (+2.2%), as well as pasta (+1.8%). Sugar price was quickly growing as well (+1.8%).

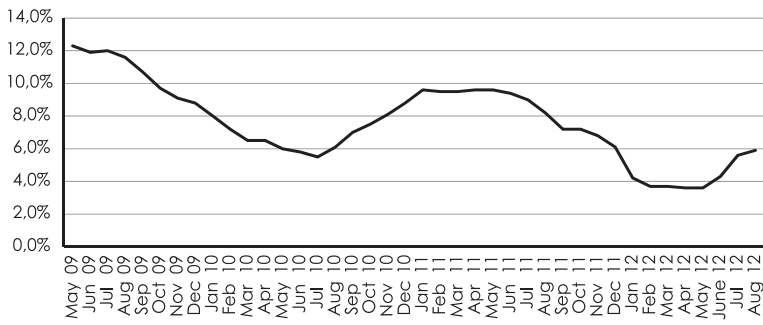
Growth rate of non-food items prices continued its growth, having increased from 0.3% to 0.4% (vs. 0.5% in August 2011). The greatest contribution to the rise in prices, as in previous months, was made by tobacco (+1.5%), which growth rate has increased more than two-fold (+3.5%). At the peak of construction season, prices have grown for construction materials (+0.6%). After a brief pause in August, gasoline prices rose again (+0.5%), which is provoked by the July increase in excise tax. Like in previous period, the only cheapening products were still video and audio appliances (-0.3%).

After the July indexation of tariffs for housing and public utilities, price growth for public commercial services has substantially slowed down; in August they went up only by 0.6% (against +2.7% in July 2012 and 0.3% in August 2011). In August, the growth rate in tariffs for housing and public utilities by 0.4% was noted (vs. 5.7% in July of the current year). In the expectation of the forthcoming new school year, education prices went up (+2.7%), in particular, for higher education (+6.7%). High demand was observed for foreign hotel vouchers, and the ongoing summer vacations contributed to their cost upgrading by 1.7%. There was no reduction in any type of commercial services in August.

In August, the annual inflation (August 2012 against August 2011) has accelerated to 5.9% (*Fig. 1*), which is 1.5 times lower than in the relevant period of the last year. In early September the annual inflation indicator has exceeded the bottom threshold of the official estimates. The core consumer price index<sup>1</sup> went up again, having made 0.6% (vs. 0.4% in 2011).

In the first days of September the second stage of the government-regulated tariffs was implemented, which has spurred inflation again. As of 17 days of September, the index of consumer prices increased by 0.4% (against a decline in prices by 0.1% for the same period in 2011). As a result, the cumulative inflation since the beginning of the year has surpassed the indicator of the previous year (+4.6%), amounting to 5% as of September 17. In September, the seasonal reduction in prices for vegetables and fruits was observed. In addition, significant growth was noted in eggs (+5%) and wheat flour (+3.6%). Among industrial goods, accelerated growth rate of gasoline prices was noted (+1%).

<sup>1</sup> The core consumer price index reflects the level of inflation in the consumer market after adjustment for the seasonal (prices of vegetable and fruit products) and administrative (regulated tariffs for certain types of services, etc.) factors, which is also calculated by the RF Statistical Service (Rosstat).



Source: RF Statistical Service.

Fig. 1. The Growth Rate of the CPI in 2009–2012 (% year to year)

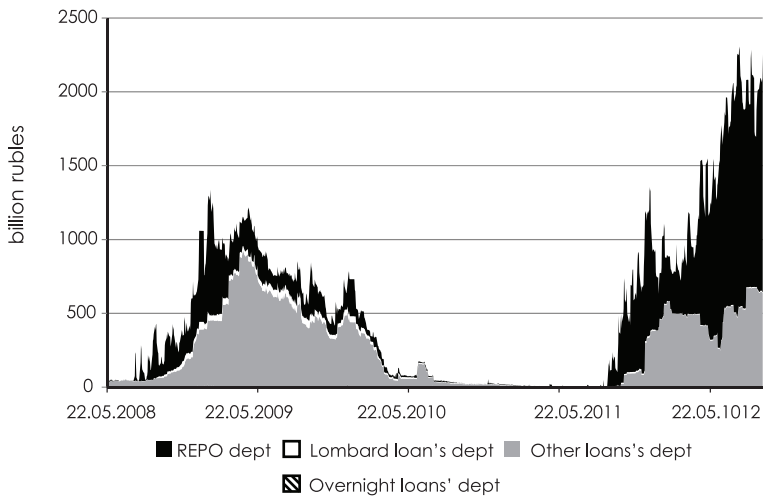


Fig.2. Arrears of commercial banks with the Bank of Russia in 2008–2012.

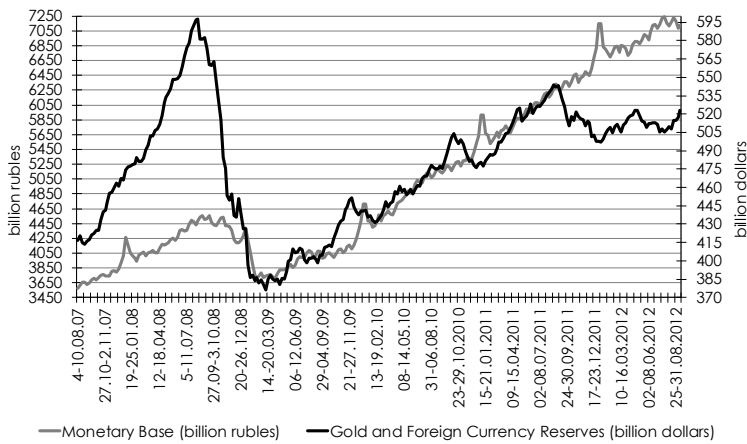


Fig.3. Dynamics of the RF monetary base (in narrow definition) and gold and foreign currency (international) reserves in 2007–2012

remained at the July level and amounted to about \$3bn. According to the Ministry of Economic Development of Russia, the capital flight was slightly lower – about \$1bn.

*In September, the Bank of Russia expects capital inflow from sales of 7.58% of Sberbank shares. It also does not rule out capital inflows in QIII and QIV. Nevertheless, as per the year performance, the*

After three months of growth, in August the monetary base in broad definition has decreased by 1.3% to Rb 8,107.8bn. The growth was based on the reduced commercial banks correspondent accounts with the Central Bank of Russia (–17.6%). Other components of the monetary base in broad definition were growing: the amount of cash in circulation (+0.1%), mandatory reserves (+1%), commercial banks deposits with the Central Bank of Russia (+26.6%).

In August, the excessive reserves<sup>1</sup> of commercial banks were still decreasing, having amounted to Rb 8898bn at the end of the month (-11.7%). The situation with the banks' liquidity has not changed: the banking sector continues to experience a shortage of liquidity, as evidenced by the growth in dynamics of borrowing from the Bank of Russia (Fig. 2).

In August the monetary base in narrow definition (cash plus mandatory reserves) has somewhat increased, having reached at the end of the month Rb 7,217.9bn (Fig. 3).

In August, the Bank of Russia has decreased the amount of foreign exchange intervention by 2.5 times. Like in the last three months, the Controller acted as a net seller of currencies: \$385.4m and Euro 47.5m were sold in the domestic market (Fig. 4).

Within month, from mid-August, international reserves were growing. On September 14, their volume amounted to \$ 522.8bn (+2.9%), having reached the maximum of the four months. It was contributed by the revaluation of foreign currency and gold reserves, which price has grown at the background of dollar decline in anticipation of the adoption of the US FRS decision to mitigate monetary policy.

In August an outflow of capital was observed again. According to tentative assessments of the Bank of Russia, it

<sup>1</sup> Under the excessive reserves of commercial banks with the RF Central Bank is understood the sum of correspondent accounts of commercial banks, their deposits with the RF CB and the RF CB bonds of commercial banks.

Regulator has increased the official forecast of capital outflow from July level of \$40bn to \$65bn. the Ministry of Economic Development gives a more optimistic assessment – \$60bn.

The ruble real effective exchange rate was strengthening. Within the month it has grown by 1%. As a result, index of the real effective exchange rate increased to 150.13 (Fig. 5).

The level of January 2002 is accepted as 100%.

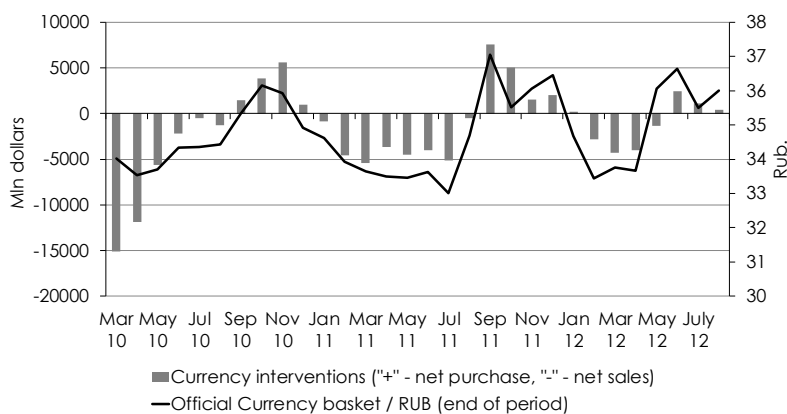
In early September, the dollar was weakening against the ruble: over 18 days of the month, it fell down by 6.1%, having decreased to the four-month minimum – 30.57 Rb / \$1. In the third week of the month US currency managed partially to gain the lost positions. As a result, within three weeks of September the ruble has strengthened against the dollar by 3.5%, i.e., Rb 31.17 / \$1 as of September 22.

In the first two weeks of September, the European currency against the ruble was relatively stable, fluctuating between Rb 40.48–40.72 / Euro 1. In the third week of the month Euro has initially weakened by about 1%, and then has grown by the same amount. As of three weeks of September, Rb exchange rate against Euro remained practically unchanged, amounting to Rb 40.45/ Euro 1 on September 22. As a result, the value of the two-currency basket has decreased by 1.8% to Rb 35.36.

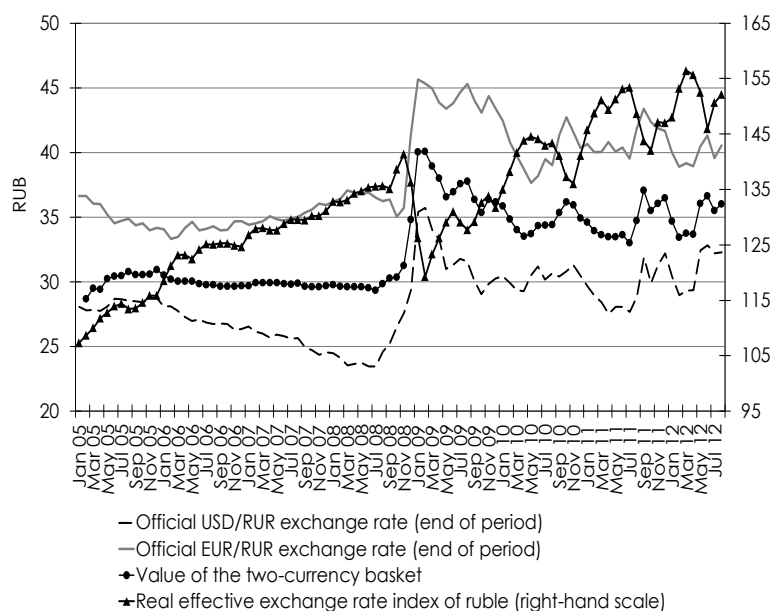
Strengthening of the Russian ruble against dollar and Euro in the middle of the month was encouraged by the FRS decision to hold a third round of quantitative mitigation of monetary policy, as well as by the decision of the Bank of Russia to raise the refinancing rate. In the third week of September, the depreciation of the ruble was due to the renewed downgrading in the global oil prices, following the publication of new data on oil reserves in the United States. In addition to external factors, the depreciation of the domestic currency was urged by the deterioration of the balance of payments current accounts. In QIII 2012, according to the HSE National Research University estimates, the current account balance of payments can amount to \$17bn, which is 20% less than in QII (\$21.2bn).

From September 14, 2012, the Bank of Russia raised the refinancing rate and the other key interest rates on providing and absorbing liquidity by 0.25 p.p. From that day, the refinancing rate is set at 8.25%. Thus, in nine months the Regulator has returned to the rate effective from May 3 to December 26, 2011.

This decision of the Bank of Russia is associated with the accelerated inflation in recent months, which annual rate of in early September has exceeded the government’s official forecast of 6%. The



Source: RF Central Bank, author’s estimates.  
Fig. 4. Central Bank Currency Interventions and Dynamics of Ruble Exchange Rate in March 2010 – August 2012



Note: The level of January 2002 is accepted as 100%.  
Source: RF Central Bank, author’s estimates.  
Fig. 5. Indicators of ruble exchange rate dynamics in January 2005–August 2012

main factors of inflation growth now are nonmonetary ones: upgrading of housing services and utilities tariffs, as well as an increase in the global prices for foodstuffs due to adverse weather conditions in some countries. In addition to this, base inflation started to accelerate in summer. It is also important to note that in addition to reducing inflation, another objective of the Regulator is to restrain the rapid pace of crediting growth. The credit boom, observed in the present time in Russia can involve bad loans' growth. According to Alexander Simanovsky, the RF CB First Vice-President, as of 2012 results, credit growth will make 20–25%.

On September 21, the Bank of Russia decided to reduce the maximum interest rate on deposits. From October 1, the Regulator will switch to the average rate assessment by a new method. The combined deposit products (pension funds or insurance funds) will be excluded from the assessment, which will reduce the interest rate by more than 1 p.p. This decision is aimed at reducing the risk of banks' default, resulting from the fact that credit institutions excessively increase interest rates on deposits to attract individuals' assets.

Currently, the average interest rate on ruble deposits amounts to 9–10%, except the top-10 banks. Herewith, the inflation rate estimate does not exceed 6–7%. Thus, the difference is at least 3%. A fair real interest rate on deposits should not exceed 1–2%. Taking this decision, the Bank of Russia pursues the objective to reduce interest rates to that level. ●

## FINANCIAL MARKETS

N.Burkova, E.Khudkova

Despite the willingness of the US Federal Reserve System and the ECB to adopt new measures of the US and the Eurozone economies encouragement, the deteriorated economic situation in Japan and China, as well as changes in Moody's Investors Service forecast for long-term credit rating of the European Union to "negative" has provoked high volatility in the Russian financial markets in September 2012. Futures Market for the month increased by 10%, turnover in the Russian stock market demonstrated an increase of 23%, and the average monthly turnover of the government securities market decreased by 15%.

In September, key indicators of corporate bonds domestic market stayed at a high level: the market volume, the trade performance indicators of the primary and secondary markets, as well as the activity of the emitters in registration of bonds issues. Market index and weighted average yield of securities demonstrated a positive trend. The situation with the emitters' performance of their current obligations to the bondholders has slightly deteriorated.

### Government securities market

In September, the lack of significant growth factors in the global financial markets, increase in the Bank of Russia refinancing rate and ruble volatility have led to the preservation of a slow development of the Russian market of government securities: the yield to maturity in the market of government securities continued to decline (by 1–11%) in line with a decline in the investors' activity in the sector (Fig. 1).

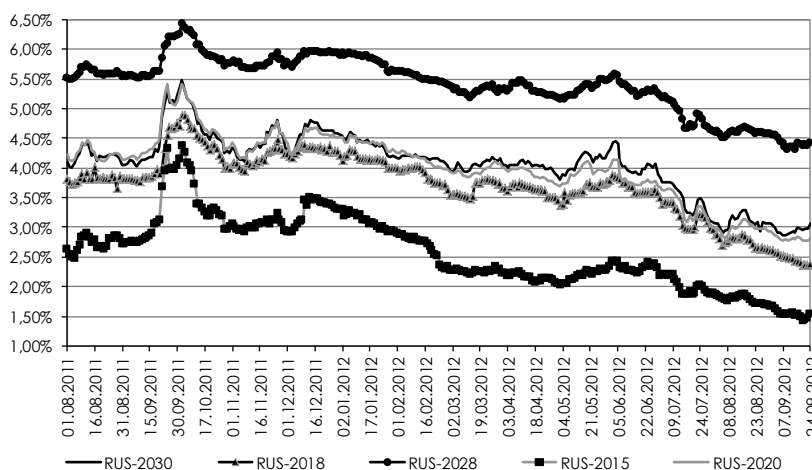
Within the period from August 27 to September 24, 2012, the total turnover in the secondary market of government bonds amounted to Rb 70.5bn with an average daily turnover at the level of Rb 3.36bn, which means the downfall of the average monthly turnover by 15% as compared with the preceding period.

From August 27 to September 24 of the current year there were held five auctions (vs. seven auctions a month earlier) in federal loan bonds (OFZ) placement in the primary market (Table 1). The total actual amount of placement made 56% of the planned volume (against 55% in the preceding month). There were no auctions on additional OFZ issues placement in the secondary market.

Table 1

## OFZ PLACEMENTS IN THE PRIMARY MARKET

Auction date	Emission	Emission volume, RB m	Emission volume at face value, RB m	Average weighted yield
29.08.2012	ОФЗ-25080-ПД	10 000.00	2 608.00	7,57
05.09.2012	ОФЗ-26209-ПД	25 000.00	23 970.63	8,01
12.09.2012	ОФЗ-26207-ПД	10 000.00	9 903.00	8,14



Source: "Finmarket" Information Agency data.  
Fig. 1. Yields to maturity of the Russian Eurobonds with maturity in 2015, 2018, 2020, 2028 and 2030

Table 1, cont'd

Auction date	Emission	Emission volume, RB m	Emission volume at face value, RB m	Average weighted yield
12.09.2012	ОФЗ-26208-ПД	20 000.00	3 064.00	7,68
19.09.2012	ОФЗ-26209-ПД	25 000.00	10 649.30	7,88
Total:		90 000,00	50 194.93	

Source: Russian Ministry of Finance.

## Stock market

### *Factors of the Russian stock market dynamics*

In general, from late August to early September 2012 there was a slight decline in the Russian stock market due to the volatility of the global oil prices and the continued holiday season. Preparedness for the US Federal Reserve Service to take new measures to support the national economy and launching of a new program by the ECB for buying government bonds of troubled countries, the publication of the US macroeconomic data on the improvement in the labor market, as well as return of investors to the Russian stock market have involved a gradual increase in the stock market since the middle of the first working week to the end of the second week of September. Reducing the forecast for GDP growth in China, the decline in oil prices, and the absence of significant positive economic data in the USA contributed to the corrective decline of the Russian stock market, starting from the third week of this month.

In general, over a month, the markets of developed and developing countries have grown by 1–6%, while since the beginning of the year the overall growth made 3–18%. The exceptions were a number of Asian countries. Thus, stock market indices in Japan and China under the influence of deterioration of economic development in these countries decreased in September by 1.3%. The basic Russian indices increased by 5.2% (Table 2 and Fig. 2).

Table 2

### DYNAMICS OF THE GLOBAL STOCK INDICES

Index	Value (as of 24.09.2012)	Dynamics within the month(%)*	Dynamics from the year beginning (%)
MICEX (Russia)	1 489.92	2.46	3.70
RTS (Russia)	1 509.58	5.06	3.98
Dow Jones Industrial Average (USA)	13 558.92	3.05	7.70
NASDAQ Composite (USA)	3 160.78	2.96	17.84
S&P 500 (USA)	1 456.89	3.24	12.21
FTSE 100 (UK)	5 838.84	1.08	3.67
DAX-30 (Germany)	7 413.16	6.34	18.19
CAC-40 (France)	3 497.22	1.86	8.65
Swiss Market (Switzerland)	6 597.22	1.87	9.09
Nikkei-225 (Japan)	9 069.29	-0.02	7.28
Bovespa (Brazil)	61 909.99	5.96	2.95
IPC (Mexico)	40 561.22	0.87	8.45
IPSA (Chile)	4 211.06	0.55	0.25
Straits Times (Singapore)	3 067.93	0.57	15.27
Seoul Composite (South Korea)	2 003.44	4.36	5.15
ISE National-100 (Turkey)	67 207.14	2.37	28.06
BSE 30 (India)	18 673.34	5.01	15.07
Shanghai Composite (China)	2 033.19	-2.82	-4.88
Morgan Stanley Emerging&Frontier Markets Index	793.05	4.03	5.13

\* Versus index values as of August 26, 2012.



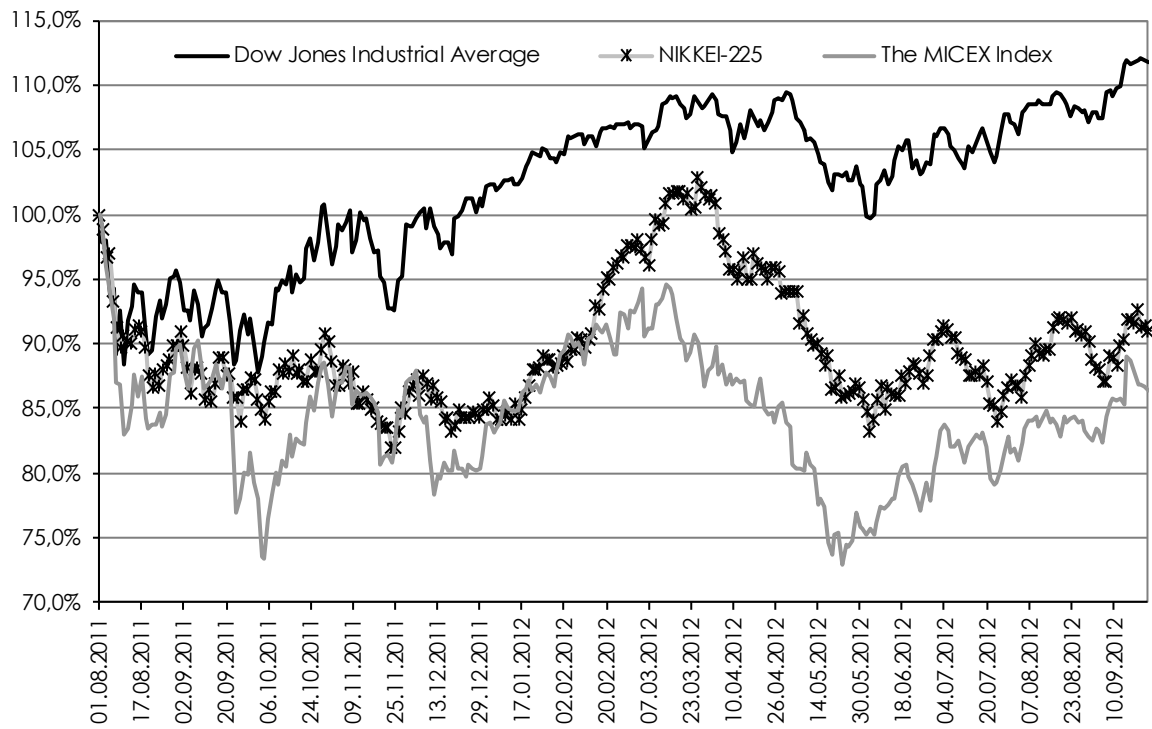
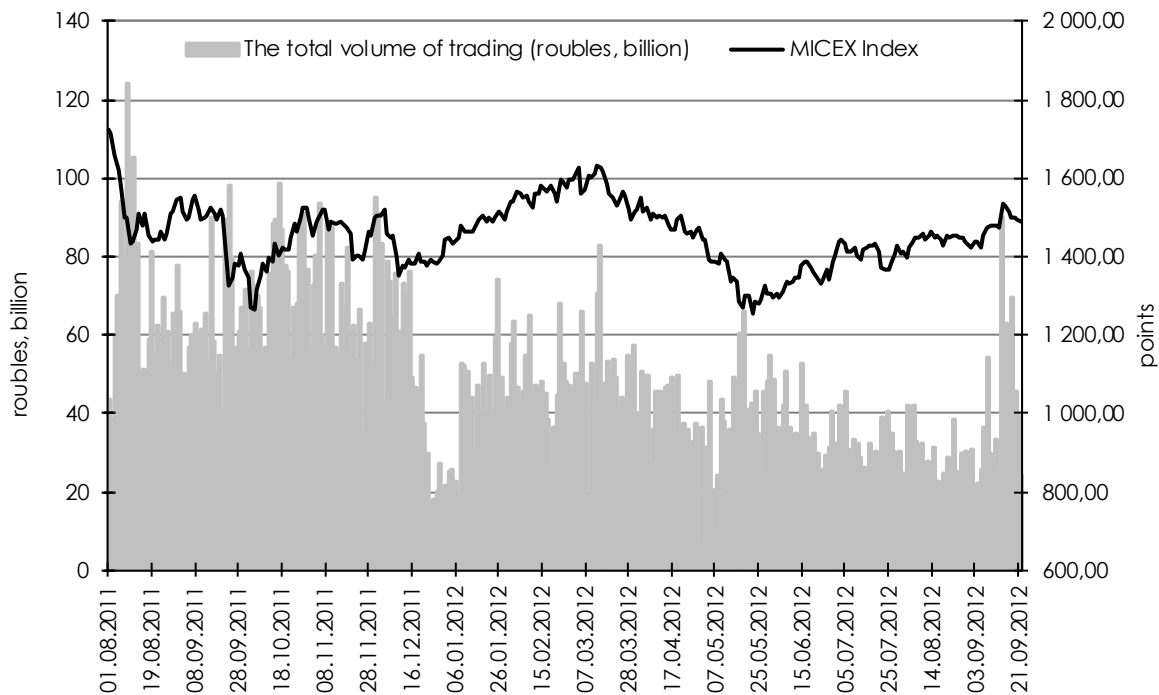


Fig. 2. Dynamics of the main USA, Japanese and Russian stock indexes (in % to the date 01.08.2012)

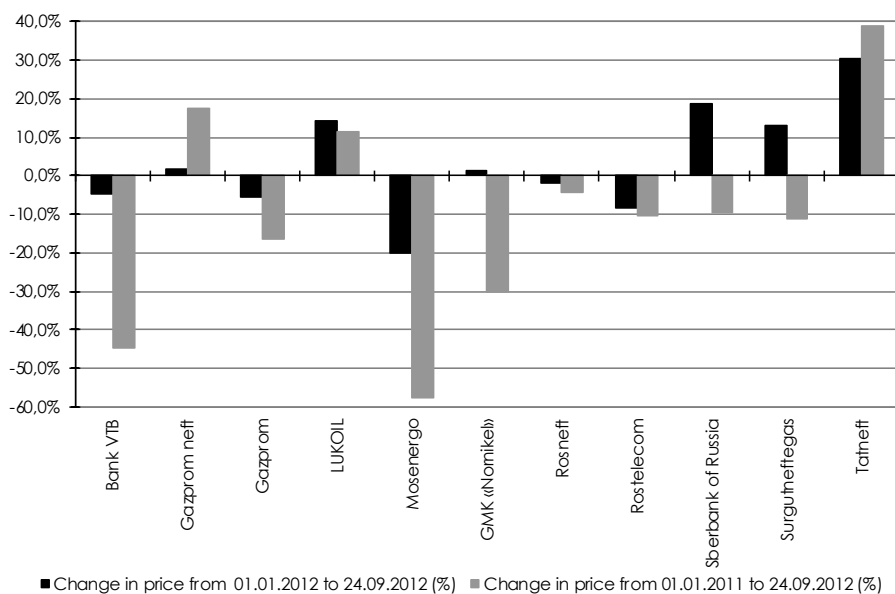
**Stock market situation development**

Within the month, the maximum value of the MICEX index was demonstrated on September 14, having reached 1,535,4 p. (versus 1,462.6 p. in the preceding month). The minimum value of the MICEX index of 1,397.1 p. has reached on September 5 (against 1,397.1 p. in the preceding month) (Fig. 3).



Source: OAO MICEX

Fig. 3. Dynamics of MICEX Index and trading volume



Source: OAO MICEX.

Fig. 4. Dynamics of the Russian Blue Chips

a month earlier were securities of Tatneft and Sberbank, which value has increased by 30.4% and 18.6%, accordingly, while the leaders of decline were Mosenergo and Rostelecom securities, downgraded by 19.9% and 8.4%, accordingly (Fig. 4).

According to the OAO MICEX, on September 24 of this year, five leaders of the domestic market in terms of capitalization were as follows: Gazprom – Rb 3,828bn (against Rb 3,708bn on August 26, 2012), Rosneft – Rb 2,203bn (against Rb 2,117bn), Sberbank of Russia – Rb 2,025bn (against Rb 20.02bn), LUKOIL – Rb 1,644bn (against Rb 1,595bn) and Sugrutneftegas – Rb 1,018bn (against Rb 1,007bn).

### Futures and Options Market

In FORTS market average daily activity of investors from August 27 to September 24, 2012 has increased by 10% as compared to the previous month. Herewith, the leaders in terms of trading in futures are contracts for the RTS index, followed with a significant lag by the contracts for Rb/\$ rate, for Rb/Euro rate, for the securities of Sberbank of Russia and Gazprom. Prices of the recent transactions, concluded for futures contracts for Rb/\$ with the date of execution on December 15, 2012 were mostly within 31–32.9 Rb/\$ (i.e., a depreciation of the ruble by 0–5.6% is expected as compared with the indicator of September 24, 2012 (31.17 Rb/USD), and with the date of execution on March 15, 2013 – within Rb/\$ 31.5–33.6. Prices of recent transactions concluded on futures contracts for Rb/Euro with the execution date on December 15, 2012 were mostly in the range of Rb/Euro 40.8–41.5, i.e., a depreciation of the ruble by 0.8–2.5% is expected as compared with the indicator of September 24, 2012 – 40.49 Rb/ Euro, and with the date of execution on March 15, 2013 – within 41.6–42 Rb/ Euro.

The value of the futures contract for RTS index (based on prices of recent transactions) with the execution date on December 15 was within 1,380–1,580 points, i.e., market participants expect a 0–8.6% decline against the indicator of September 24, 2012. By March 15, 2012 market participants expect the RTS index value to be in the range of 1,700–1,570 points. Prices of recent transactions in futures contracts for the MICEX index with the date of execution on December 15, 2012 were in the range of 1,440–1,550 points. Thus, expectations of a rather short-term MICEX index dynamics are variable as compared to the indicator of September 24, 2012 (Table 2), i.e., some market participants expect a decline of MICEX index (by 0.3%), and others, on the contrary, expect an increase of MICEX index (by 0.4%). Options enjoyed a far less demand, from August 27 to September 24, 2012 their trading turnover made about Rb 337.6bn (Rb 4,667.1bn in futures). The leaders in terms of trading turnover were the marginal options for futures contracts on the RTS index.

In general, within the period from August 27 to September 24, 2012, the MICEX index has increased by 2.5% (from September 25, 2011 to September 24, 2012 the MICEX index has increased by 12.3%), whereas the turnover of trades in securities included in the MICEX index has reached Rb 804.4bn. The average daily level of investor's activity in the stock market in September has grown by 23.2% as compared with the preceding month.

In the period from the beginning of the year through September 24, 2012, the leaders in the value growth among the “blue chips”, like

### Corporate bonds market

The volume of domestic corporate bonds market in Russia (at par value of circulating securities denominated in local currency) remained practically unchanged in September and at the end of the month made Rb 3,776.3bn, which is only by 0.2% more than its value at the end of August<sup>1</sup>. Therefore, the indicator is sustained at its historical maximum. The insignificant growth of the market capacity has been associated with an increased number of bond issues (828 issues of corporate bonds registered in the national currency against 823 emissions at the end of the previous month), while number of emitters registered in the debt sector has somewhat decreased (336 against 339 companies in August). In circulation there are still some emissions of bonds issued in US dollars and one bonds issue in Japanese yen.

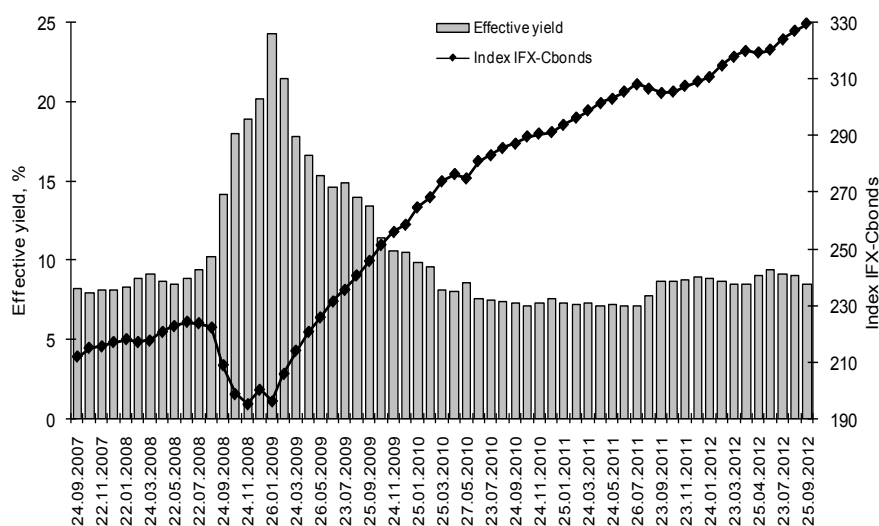
Investment activity in the secondary market of corporate bonds in September has also decreased to some extent, but still remained at a rather high level. Thus, from August 27 to September 24, the total volume of transactions in the MICEX amounted to Rb 110.3bn (for comparison, from July 2 to August 24, the turnover was equal to Rb 129.3bn), and the number of transactions for the period under review made 23.4 thousand (against 25.7 thousand in the previous period)<sup>2</sup>.

Index of the Russian corporate bond market IFX-Cbonds continued its growth trend. By the end of September its value increased by 2.5 points (or 0.8%) as compared with the value of late August. The average weighted yield for September has declined from 9.06% to 8.47% (See Fig. 5). Herewith, a sharp decline in corporate bond yields began immediately after the refinancing rate of the Central Bank upgrading on September 14 to the level of 8.25%. Reduction of domestic interest rates in mid-September was induced by rather favorable external market situation. However, further significant decline in the yield in the short term is unlikely. Prospective estimates of inflation in Russia for the year excess of the planned level of 6%, and a deterioration of worsening forecasts for the global economy growth can slow down the positive dynamics<sup>3</sup>.

The portfolio duration of corporate bonds indicator has sharply decreased again and at the end of September amounted to 600 days, which is by 61 days less than at the end of previous month. The declining trend of portfolio duration reflects the reduction in the term of maturity of bonds in the corporate sector.

Despite the average weighted yield in the bonds market has expressly decreased, the most liquid bond issues did not show a similar reduction trend in the yield. Maximum downfall in the rates (more than 1 p.p.) was recorded only in respect of OAO "AFK System" securities (03 series issue). Most major issuers of the financial and industrial sectors showed the opposite trends<sup>4</sup>.

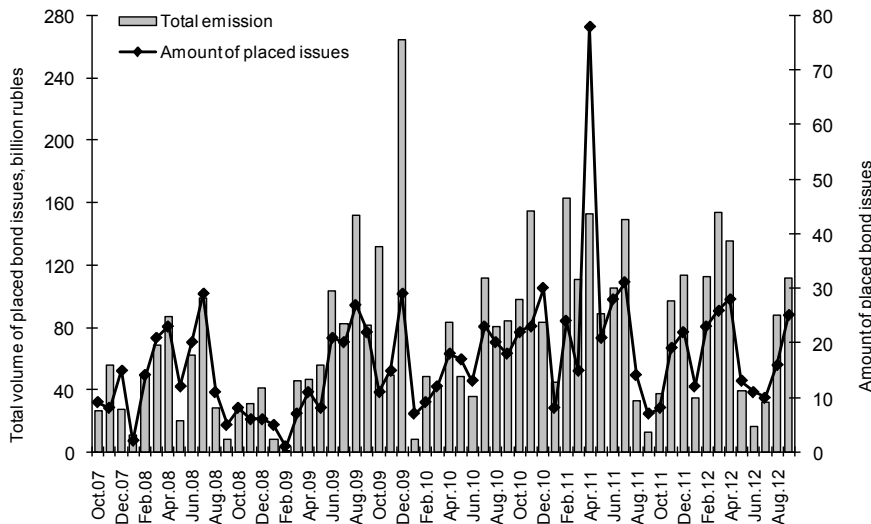
In September, rather high investors' activity remained in the debt market sector, though the volume of issues registration indicators were still far from the record indicators of July. Thus, from August 28 to September 25, twelve emitters have placed 37 stock bonds series with the total nominal value of Rb 172.0bn (for comparison, from July 24 to



Source: Cbonds data.

Fig. 5. Dynamics of the Russian corporate bonds market index and average weighted yield

- 1 Rusbonds Information Agency data.
- 2 Finmarket Information Agency data.
- 3 Cbonds Information Agency data.
- 4 Finmarket Information Agency data.



Source: Rusbonds data.

Fig. 6. Dynamics of primary placement of corporate bonds, denominated in national currency

August 27 there were registered 32 bond issues with the nominal value of Rb 254.5bn). Exchange bonds again made one third of registered issues.

Investor activity in the primary market was also quite high, thanks to the favorable market situation. From August 28 to September 25, twenty emitters have placed 25 bonds with a total face value of Rb 111.4bn (whereas from July 24 to August 27, there were placed 19 bonds with a total face value of Rb 87.5bn (Fig. 6). The largest bond issues were placed by OAO NLMK (two

series of bonds worth Rb 15bn), Insurance Company “RESO-Guarantee” (2 series bonds worth Rb 15bn), OAO “Bank VTB” a series of bonds worth Rb10bn), OAO “Rosbank” JSCB (a series of bonds worth Rb 10bn), ZAO “Reserve Trust company” (a series of bonds worth Rb 10bn)<sup>1</sup>. Emitters “Reserve Trust Company”, “NLMK”, “RESO-Guarantee” managed to attract funding with maturity term of 10 to 15 years, and ZAO “VTB Bank 24” has placed mortgage bonds with maturity of 30 years .

In September this year, like a month before, FFMS of Russia has not recognized as invalid any of the bond issues due to the non-placement of securities (earlier 2–4 bonds issues were recognized as invalid monthly). This is further evidence of the high investor interest in the Russian corporate bonds.

From August 28 to September 25 twelve emitters should have paid off their issues for the total amount of Rb 59.3bn. Herewith, one emitter failed to fulfill its liabilities to the bondholders in due time and announced a technical default (in the previous months, 2–3 emitters have announced a technical default). In October 2012, seven corporate bond issues totaling to Rb 17.0bn are expected to be paid off<sup>2</sup>.

The situation with the announcement of actual default (when the issuer is unable to pay income securities holders even in a few days after the due date of meeting liabilities) has somewhat deteriorated against the previous month. From August 28 to September 25, two emitters announced a real default in coupon yield payment (from July 24 to August 27, all issuers have performed their current liabilities). Herewith, all emitters have paid the bonds loan value and made early redemption of the securities on offer in due time<sup>3</sup>. ●

1 Rusbonds data.  
2 Rusbonds data.  
3 Cbonds data.

**REAL ECONOMY: TRENDS AND FACTORS**

O.Izryadnova

*In July-August of the current year the economic dynamics by the basic types of economic activities continued to weaken. Starting with June of the current year the retail trade turnover and investments in fixed assets growth rates in annual terms have been observed to slow down. In such a situation the acceleration of the real incomes of the population growth rates by 7.2% and real wages – by 7.8% versus August 2011 is worrying. The increase in the production costs due to the growth of expenses for labor remuneration leads to the worsening of the enterprises' financial results.*

This year the macroeconomic situation is characterized by a gradual decrease of the growth rates. In Q1 2012 the GDP physical volume index made 104.9%, in Q2 2012 – 104.0% and as a result of H1 2012 – 104.5% versus the corresponding periods of 2011. It is the slackening of the investments in fixed assets dynamics, retail trade and foreign trade turnover as compared with the corresponding period of the previous year that act as the main factors determining the conditions for the economic development starting with Q2 2012.

The changes in the situation at the world markets have resulted in the contraction of the Russian export growth rates both in the terms of physical and value volume, the exhaustion of the low base effect and starting ruble exchange rate weakening resulted in the slowdown of the import growth rates. In August 2012 as compared with the corresponding period of 2011 the foreign trade turnover reduced by 1.7%, export –by 0.9%, import – by 3.0%.

The situation at the consumer and investment markets is complex. Starting with June of the current year the retail trade turnover growth rates have been decelerating. In August 2012 the index of retail trade turnover made 104.3% versus the corresponding level of the previous year, being 100.8% for foodstuffs and 107.4% for non-food goods.

In June–August 2012 the dynamics of the investments in fixed assets and the workload in construction was observed to weaken, the indices in the sphere of housing construction were subject to sudden fluctuations. In August 2012 the growth rates of the investments in fixed assets made 102.3% in annual terms as compared with 107.0% in August 2011. The workload in construction remained practically at the level of August of the previous year.

The inertial development of the processes in July–August of the current year resulted in further weakening of the economic dynamics as broken by the basic types of economic activities. In August 2012 the industrial production index made 102.1% versus August 2011 as compared with 106.2% a year ago, being 100.8% versus 103.3% in minerals extraction, 104.1% versus 107.1% in manufacturing industry.

The existing situation made it necessary to specify main parameters for the development of the Russian economy till the end of 2012, which served as the basis for socio-economic development forecast for 2013 and for the planning period of 2014-2015. In accordance with the estimations of the RF Ministry of Economic Development the slackening of the economic development is to be expected as a result of consumer and investment demand growth rates slowdown and the decrease in the net export as compared with the corresponding period of the previous year. The acceleration of the industrial production growth forecast for H2 2012 as compared with H2 2011 does not compensate for the weakening of the demand in the construction complex and recession in the agriculture. In H2 2012 the growth of the GDP is estimated to be at the level of 102.7% versus the corresponding period of the previous year, making 103.5% on the whole over 2012.

Up to the end of 2012 the estimation of social parameter of the development are fairly optimistic. The situation at the labor market is stabilizing: the number of the unemployed in the economy will recover to the pre-crisis level of 2007, the general unemployment will lower to the decade minimum of 4.3m or 5.9% of the total number of the economically active population.

According to the forecast of the RF Ministry of Economic Development, as compared with the previous year in 2012 the growth of the real incomes will accelerate to 3.0%, of real wages – to 9.1%. The anticipating growth of the real wages versus labor productivity will result in the expansion of the labor remuneration proportion in the GDP to 24.3%.

Table 1

ESTIMATION OF THE MAIN INDICES OF ECONOMIC DEVELOPMENT IN 2012, AS % VERSUS THE CORRESPONDING PERIOD OF THE PREVIOUS YEAR

	2011			2012		
	Year	H1	H2	Year	H1	H2
GDP	104.3	103.7	104.9	103.5	104.5	102.7
Industrial production index	104.7	105.3	104.1	103.6	103.1	104.1
Manufacturing industry index	106.5	108	105	104.9	104.5	105.3
Agriculture production index	122.1	100.7	129	95.6	104.2	92.4
Investments in fixed assets	108.3	102.7	111.3	105.5	111.6	102.4
Workload in construction	106.0	101.2	110.8	-	105.4	-
Implementation of residential floor area	106.6	96.3	112.6	106.3	101.9	108.5
Retail trade turnover	107	105.4	108.4	106.1	107.1	105.1
Volume of paid services rendered to the population	103	103.4	102.6	103.6	104.2	103.1
Foreign trade turnover	130.3	134.7	126.9	103.7	105.7	101.9
Export	130.3	130.2	130.7	102.3	106.7	98.4
Import	130.2	142.8	121.3	105.8	104.1	107.3
Real disposable incomes of the population	100.8	99.4	102	103	103	103
Real wages	102.8	102.1	105	109.1	110.7	107.5
Consumer prices index at the end of the period, over the period	106.1	105	101.1	107	103.2	103.7
Average price for oil grade Urals, \$/barrel	109.3	108.2	110.5	109.0	111.8	106.2

Source: RF Ministry of Economic Development “Forecast for socio-economic development of the Russian Federation for 2012 and for the planning period of 2013 and 2014”.

For the purposes of the parameters for the federal budget for 2013–2015 development the moderately optimistic scenario (2) is suggested; it is based on the factors increasing the competitive ability of the Russian economy, strengthening of the import substitution trend, improvement of the investment climate together with moderate growth of the state expenditures for infrastructure and human capital development. In spite of the gradual increase in the quality of the economic growth the general dynamics is expected to be considerably below the pre-crisis period. In 2013–2015 the growth of the GDP is estimated to be at the level of 3.7–4.5% and investments in fixed assets – at 7.2–7.9%<sup>1</sup>.

The hypothesis of the acceleration of the internal demand versus the GDP dynamics is fundamental for the forecast for 2013–2015. The structural changes in the investments in fixed assets are directed to the gradual expansion of the investment in manufacturing industries and types of economic activities connected with services rendering. Even though the proportion of the investments in fixed assets in the GDP will rise to 22.3% by 2015 and exceed the pre-crisis level, these funds, according to the forecast, are insufficient to thoroughly modernize the economy. The struc-

<sup>1</sup> Conservative scenario (1) suggests retention of low competitive ability as compared with the import and reserved recovery of the investment activity, the real state expenditure for the development decreasing. The scenario assumes stagnation of the state investment demand and real wages of public sector employees and monetary allowance for the military. In 2013–2015 annual economy growth rates are estimated to be at 2.7–3.3%, investment in fixed assets growth rate – at 5.0–5.9%.

Accelerated growth scenario (3) suggests intensification of production factors and increase in labor productivity by 1.5 times by 2018 versus the level of 2011. Average annual economy growth rates in 2013 are in the range of 4.6–6.4%, investments in fixed assets – 8.5–13.1%. The scenario is characterized by macroeconomic imbalance and high vulnerability to the external shocks.

tural shifts and economy growth rates being as forecast in 2013–2015 the saturation of the investment demand will still be supported by the anticipating growth rates of investment goods import as compared with the domestic production. Besides, the domestic production will still be dependent on the import of intermediate goods.

Table 2

MAIN INDICES OF THE FORECAST ACCORDING TO THE MODERATELY OPTIMISTIC SCENARIO (2), AS PERCENTAGE VERSUS THE PREVIOUS YEAR

	2011	2012	2013	2014	2015	2015 versus 2011
Consumer prices index, growth rates	106.1	107	105–105	104–105	104–105	
Gross domestic product, growth rate	104.3	103.5	103.7	104.3	104.5	117
Industrial production index	104.7	103.6	103.7	103.7	103.7	115.5
Agriculture production index	122.1	95.6	106.4	102.4	102.8	107.1
Investments in fixed assets	108.3	105.5	107.2	107.3	107.9	130.9
Volume of retail trade, growth rate	107.0	106.1	105.4	105.8	105.8	125.2
Volume of paid services rendered to the population, growth rate	103	103.6	104.7	105.6	105.9	121.3
Real disposable incomes of the population	100.8	103	103.7	105.2	105.3	118.2
Real wages	102.8	109.1	103.7	105.5	105.9	126.3
Foreign trade turnover	130.3	103.7	99.8	106.1	106.0	116.6
Export	130.3	102.3	93.6	104.3	104.5	104.4
Import	130.2	105.8	109.5	108.5	108.0	135.8
Economically active population	99.5	99.7	99.7	99.6	99.4	98.5
Employed in the economy	100.1	100.9	99.7	99.6	99.4	99.4
Level of the unemployment versus the economically active population	6.9	5.9	5.9	5.9	5.9	
Labor efficiency	104.1	102.6	104.0	104.7	105.1	117.5

Source: RF Ministry of Economic Development.

The prospects of the Russian economy development in the mid-term run will be determined by the parameters for the improvement of the competitive ability, increase in the efficiency of factors of production use and the lowering of the costs. In the environment of the expected employment contraction the growth of the economy is possible when the factors of production are used more efficiently. However, the forecast still maintains the trend for the anticipating growth of labor remuneration versus labor efficiency and the increase of the expenses for labor remuneration proportion in the GDP. ●

## RUSSIAN INDUSTRY IN AUGUST 2012

S.Tsukhlo

According to the surveys of the Gaidar Institute<sup>1</sup>, in August the situation in Russian industry sooner improved than got worse. Slowdown of a drop in the demand permitted enterprises to avoid cuts in output, introduce positive adjustments in production plans and reduce the rate at which workers were laid off with complete control over finished goods stocks exercised. However, uncertainty about the future makes the industry minimize its investment plans and go ahead with lay-offs of workers.

### Industrial Optimism Index

The latest calculation of the industrial optimism index showed that the situation in Russian industry improved and, notably, by means of all the components of that composite index.

Enterprises' aggregate plans and forecasts got better as well, however, by virtue of output plans.

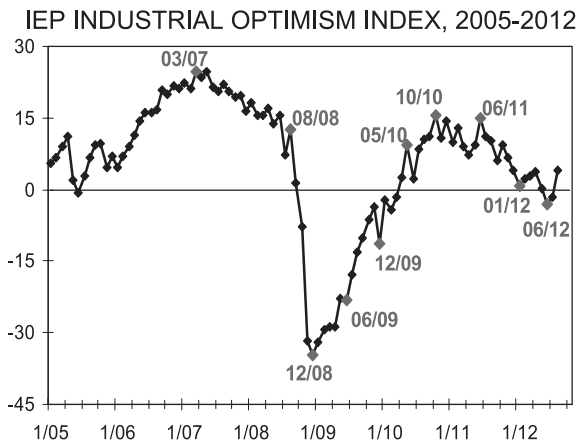


Fig. 1

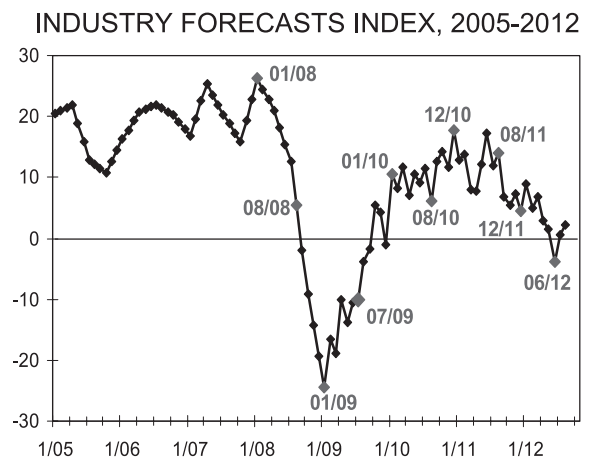


Fig. 2

### Demand on industrial products

CHANGES IN THE SOLVENT DEMAND  
CLEARED OF SEASONAL FACTOR  
(BALANCE=%GROWTH-%DECREASE)

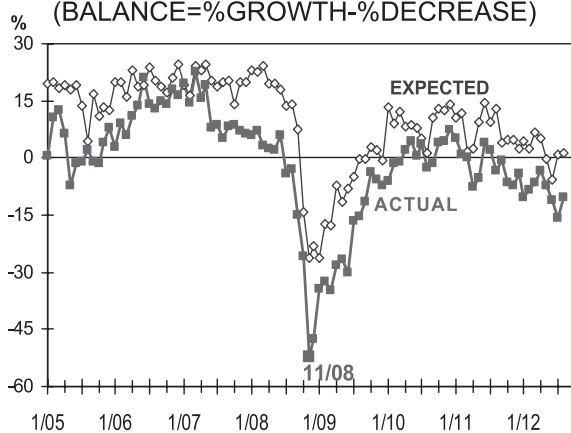


Fig. 3

In August, dynamics of the demand in industrial products underwent positive changes. Both the initial data and that cleared of the seasonal factor showed growth of six points, though it still remained in the negative zone; the above factor is evidence of the fact that a drop in sales slowed down (Fig. 3). Though a drop in the demand continued in August, it was not that intense as in July. As a result, July 2012 turned out to be the worst month as regards dynamics of the demand from July 2009.

The above situation permitted industry to “take breath” and improved satisfaction with sales volumes. Within a month, the difference in evaluations of the demand increased by eight points and, thus, all the losses of June and July were recovered. At present, only 42% of enterprises are not satisfied with sales of their products (Fig. 4). That is the minimum (best)

1 Surveys of managers of industrial enterprises are carried out by the Gaidar Institute in accordance with the European harmonized methods on a monthly basis from September 1992 and cover the entire territory of the Russian Federation. The size of the panel includes about 1,100 enterprises with workforce exceeding 15% of workers employed in industry. The panel is shifted towards large enterprises by each sub-industry. The return of queries amounts to 65–70%.



value in the past nine months. However long (protracted?) expectation of the second wave of the crisis which analysts spoke much about made enterprises reduce their requirements to normal volumes of the demand. If late in 2010 and early in 2011 the demand was considered normal with a capacity utilization at the level of 76–77%, at present Russian industry is satisfied with that of 72%–73%.

In the 3<sup>rd</sup> quarter, forecasts of the demand still preserve a zero balance: expectations of growth are balanced completely by those of a decrease in sales. On one hand, such an uncertainty in forecasts looks better than growth in pessimism of forecasts in the 2<sup>nd</sup> quarter of 2012 when within three months the balance of expectations lost 13 points and hit the three-year lowest level. On the other hand, the industry cannot determine the behavior of the demand in the near future.

**Stocks of Finished Products**

In a situation of continued decrease in the demand and uncertainty about the prospect of changes in it, the industry starts minimizing risks related to accumulation and maintenance of a reasonable surplus of stocks of finished products. During the summer, the balance of evaluations lost 8 points after it hit the 33-month maximum in May (*Fig. 5*). In August the share of answers “normal” reached the historic maximum (of all the 243 surveys!): as never before industry was careful about its policy of stock management. The latter leaves no hope either to the government which already tried to declare the need to replenish stocks as a driver of industrial growth, nor new buyers who will have to wait for new products to be made, rather than receive finished products from manufacturers’ warehouses right away.

**Output**

In August, the dynamics of the output underwent positive changes. The initial growth rate increased by 11 points after a drop of 26 points in the 2<sup>nd</sup> quarter and stabilization at a zero level in June and July. Clearing of the seasonal factor smoothed the August spike to four points. As a result, according to surveys growth in industrial output stopped in summer (the growth rates were within the range of –2 to +2 points, that is, zero ones). The fact that the expected recessionary drop (or the one close to it) did not materialize adds optimism to the above results. However, the pessimism of the June–August data cleared of the seasonal factor consisted in absence of signs of growth (*Fig. 6*). Those signs could only be seen in enterprises’ plans. In the 3<sup>rd</sup> quarter, the optimism increased by 11 points after a drop to the three-year minimum in

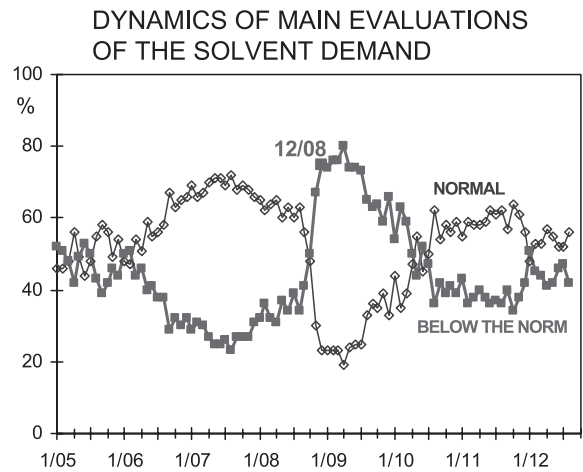


Fig. 4

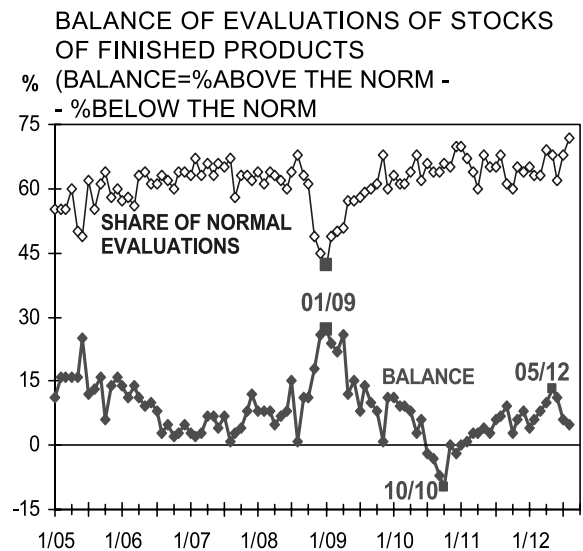


Fig. 5

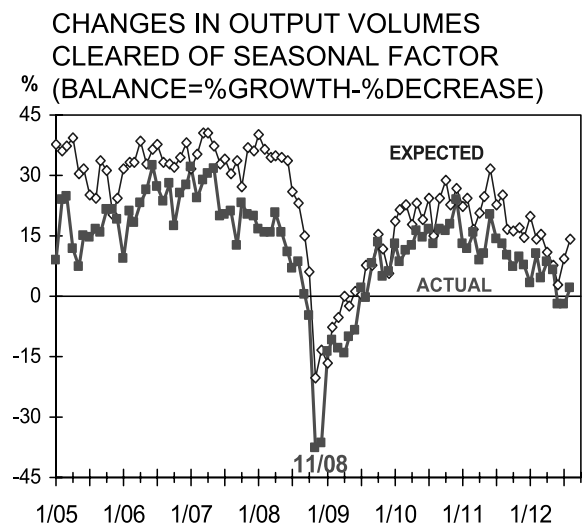


Fig. 6

June. Absence of a recessionary drop in the output gave enterprises a hope that production may revive.

### Prices of enterprises

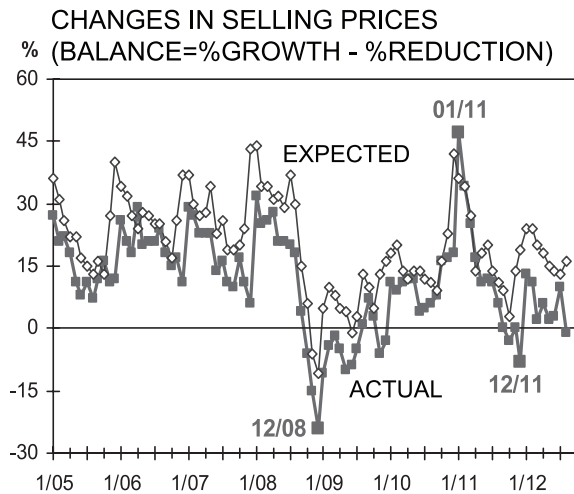


Fig. 7

noted that in May–June industry did not plan a price review in July and intended to stick to the former pricing policy which consisted in a slow reduction of prices' growth rates. It is another story that in March–June enterprises actually had to reduce growth in prices to the minimum.

### Actual dynamics and lay-off plans

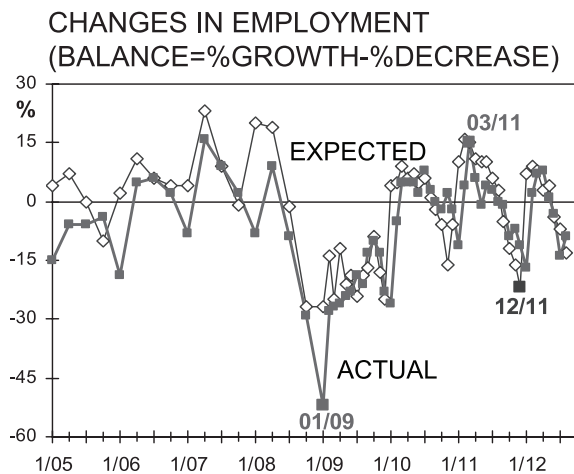


Fig. 8

In August, pricing policy of industrial enterprises underwent changes again. If in July the first half of the annual growth in tariffs had to be regained, at present enterprises returned to modesty in that area. The balance (rate of intensity) of actual growth in prices lost 11 points within a month and became a zero one; growth in selling prices in industry in general stopped again (*Fig. 7*). It is to be noted that 81% (almost the post-default maximum value) of enterprises reported directly that they did not change their prices, while in the remaining 19% of enterprises 9% and 10% of them reported about price rises and price cuts, respectively. As a result, the most moderate growth in selling prices in 2012 was registered.

Pricing plans of enterprises do not promise a change in the trend in that area. In August the balance of forecasts grew by symbolic two points after five months of an uninterrupted decline. It is to be

In August, industry kept laying off workers, however, at a lower rate of intensity than in July when the balance (rate) of a change in the number of the employed dropped to  $-14$  points according to the initial data and, to  $-17$  points, according to the data cleared of the seasonal factor (*Fig. 8*). At present, it amounts to  $-9$  points and  $-10$  points, respectively.

Enterprises' plans do not promise changes in the HR policy in industry. In August, the initial balance of forecasts decreased by another six points, while that cleared of a seasonal factor, by another four points. A reduction of the number of workers in industry continues and, most probably, at a higher rate of intensity. ●

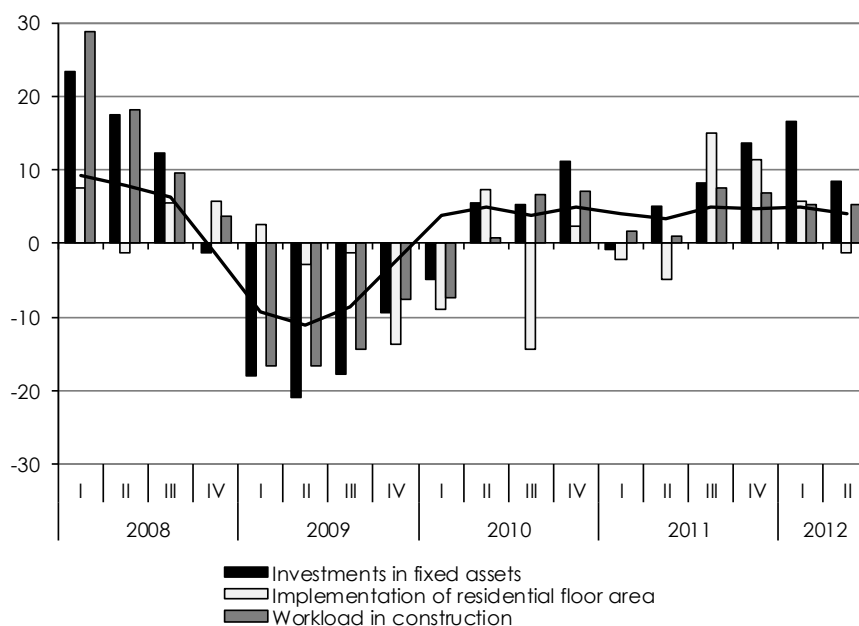
## INVESTMENTS IN REAL ECONOMY SECTOR

O.Izryadnova

*In January–August 2012 investments in fixed assets made Rb 6206.8bn, having increased by 8.8% versus the corresponding period of the previous year. In July the increase in the investments in fixed assets decreased to 3.8% in annual terms, and in August – to 2.3%. Under the existing dynamics the expected growth of the investments in fixed assets will make 102.4% in H2 2012, and 105.5% on the whole as a result of 2012. The structure of the investments financing sources is characterized by the contraction of the bank loans and borrowings from other organizations.*

In H1 2012 the investments in fixed assets made Rb 4299.8bn having increased by 11.6% as compared with H1 2011. The increase in the investments in fixed assets versus the previous year was determined by the overcoming of three-year trend towards the contraction of the investments in Q1 of the year. However, starting with Q2 2012 the business activity in construction complex was observed to weaken gradually, which was accompanied by the enterprises' profits decreasing and the interest rates for credits in rubles with the term below one year starting to grow again. In July–August 2012 the investments in fixed assets ceased having dominating impact on the dynamics of the economic growth. In July the growth of the investments in fixed assets decelerated to 3.8% in annual terms and in August – to 2.3%. Over January–August 2012 investments in fixed assets went up by 8.8% versus the corresponding period of the previous year and made Rb 6206.8bn. The changes in the dynamics of the investments is partially accounted for by the effect of the high base of the corresponding months of 2011 when the business activity level was observed to rise dramatically, but the fundamental reasons of the investment process instability are accounted for by the internal factors of economy functioning.

The dynamics of the investments in fixed assets is different for large and small enterprises. In H1 2012 in the segment of large and medium-sized enterprises investments in fixed assets went up by 9.6% versus the corresponding period of the previous year, exceeding by 5.0% the figure of the corresponding period of 2008. Changes in the situation at the internal market emphasized the contribution of small enterprises into the dynamics of the investment activity recovery. The proportion of small enterprises accounted for about 27% of the total volume of investments throughout the economy in H1 2012. In H1 2012 the growth of the investments in the segment of small enterprises has not only compensated for the low investment activity of the corresponding period of the previous year, but also secured the recovery of the volumes in this segment at the level of H1 2008. In H1 2012 the structure of invest-



Source: Federal State Statistics Service.

Fig. 1. Dynamics of Investments in Fixed Assets and GDP in 2008–2012, as percentage to the corresponding quarter of the previous year

ments in fixed assets was transformed fur to a considerable expansion of volumes and proportions of investments in machinery, equipment and transport vehicles, while the proportion of the investments in housing, buildings and constructions contracted. As compared with H1 2011, investments in machinery and equipment went up by Rb 274.7bn, in domestically produced models – by Rb 252.1bn. Over the last three years the proportion of investments for the purchase of imported machinery, equipment and transport vehicles in the total volume of investments into this group of commodities has been registered to decrease gradually from 23.3% in 2009 to 20.9% in 2011 and 17.9% in H1 2012. The formation of the trend occurs against unsteady dynamics of internal machine-building capital goods production development and the shift of the import structure towards the goods of intermediate demand. In this connection it is rational to analyze the characteristics of the replenishment and technological structures of investments in fixed assets.

Table 1

STRUCTURE OF INVESTMENTS IN FIXED ASSETS AS BROKEN BY TYPES OF FIXED ASSETS IN H1 2008-2012, AS % TO THE TOTAL (EXCLUDING THE SUBJECTS OF SMALL-SCALE ENTREPRENEURSHIP AND PARAMETERS OF INFORMAL ACTIVITIES)

	Rb bn					As % to the total				
	2008	2009	2010	2011	2012	2008	2009	2010	2011	2012
Investments in fixed assets	2205.8	2188.7	2108.1	2650.9	3135.0		100	100	100	100
including:										
housing	170.7	131.7	122.8	121.8	133.7	7.8	6.0	5.8	4.6	4.3
buildings (excluding housing) and constructions	1101.6	1190.2	1108.2	1419.0	1601.9	49.9	54.4	52.6	53.5	51.1
machinery, equipment and transport vehicles	751.6	671.2	692.1	872.2	1146.9	34.1	30.7	32.8	32.9	36.6
of which: purchase of imported machinery, equipment, transport vehicles	146.1	156.3	138.8	182.2	204.8	6.6	7.1	6.6	6.9	6.5
other	181.9	195.6	185.5	237.9	252.5	8.2	8.9	8.8	9.0	8.0

Source: Federal State Statistics Service.

An extremely reserved recovery of the investments in the housing construction is another characteristic of the construction and investment complex in recent year. In H1 2012 the volumes of investments in housing remained Rb 37.0bn below the corresponding figure of 2008, and their share in the total volume of investments in fixed assets was lower by 3.5%. Starting with H2 2011 the dynamics of residential floor area implementation has been observed to be positive, which was determined by some improvement of the financing situation. In H1 2012 the organizations of all the ownership forms constructed 242,800 apartments of the total floor area of 21.0 sq m, exceeding by 1.9% the figure of the corresponding period of the previous year. Individual contractors built 11.1m sq m of the residential floor area, or 53.00% of the total volume of housing that was put into implementation in 2012.

Analyzing the trend for the change in the absolute volumes of investments in housing construction in 2010–2012, the structural characteristics of financing connected with the increase in volumes and proportion of the funds of the population in share housing construction financing should be taken into account together with the intensifying dynamics of the contraction of organizations' funds. In H1 2012 funds received for share participation in construction went up by Rb 18.2bn, including the funds of population – by Rb 13.8bn as compared with H1 2011. The upsurge in the investment activity of the population was supported by the expansion of crediting scale. In H1 2012 issued mortgages volume made Rb 423.1bn, having grown by 1.63 times versus the previous year.

The changes in the structure of the investments financing was determined by the intensification of the orientation towards the use of own funds. In H1 2012 the proportion of the investments

made at the expense of the own funds of the enterprises expanded by 3.2% as compared with H1 2011 and by 9.2% as compared with H1 2009. Despite the fact that in H1 2012 the profitability on the whole throughout the economy made 10.0% and decreased by 1.6% versus the corresponding period of the previous year, the proportion of the investments financed from the organization's profit went up to 19.4% versus 18.0% in H1 2011.

Table 2

STRUCTURE OF INVESTMENTS IN FIXED ASSETS AS BROKEN BY THE SOURCES OF FINANCING  
IN H1 2009–2012, AS % TO THE TOTAL (EXCLUDING THE SUBJECTS OF SMALL-SCALE  
ENTREPRENEURSHIP AND PARAMETERS FOR INFORMAL ACTIVITIES)

	Rb billion				As % to the total			
	2009	2010	2011	2012	2009	2010	2011	2012
Investments in fixed assets	2188.7	2108.1	2650.9	3155.0	100	100	100	100
of which by sources of financing: own funds	878.5	947.4	1222.4	1544.0	40.1	44.9	46.1	49.3
of which: profit remaining in the organization	369.3	342.8	476.6	608.7	16.9	16.3	18.0	19.4
amortization	437.2	516.0	621.4	771.9	20.0	24.5	23.4	24.6
borrowings	1310.2	1160.7	1428.5	1591.0	59.9	55.1	53.9	50.7
of which: bank loans	263.2	193.0	224.4	262.8	12.0	9.2	8.5	8.4
of which loans from foreign banks	80.9	60.0	46.5	49.3	3.7	2.8	1.8	1.6
borrowings from other organizations	179.3	139.3	129.6	165.4	8.2	6.6	4.9	5.3
budget funds	364.7	327.3	382.7	412.3	16.7	15.5	14.4	13.2
of which: from the federal budget	142.5	159.6	174.2	199.5	6.5	7.6	6.6	6.4
from the budgets of subjects of the Russian Federation	200.5	148.9	185.7	187.0	9.2	7.1	7.0	6.0
off-budget funds	4.7	8.8	6.1	6.9	0.2	0.4	0.2	0.2
other	498.3	492.3	685.7	743.0	22.8	23.4	25.9	23.6
of which: funds from overhead organizations	371.3	355.6	547.6	583.6	17.0	16.9	20.7	18.6
funds for share participation in con- struction (from the population and organizations)	50.6	46.0	45.8	64.0	2.3	2.2	1.7	2.0
of which funds of the population	20.8	23.1	29.1	42.9	1.0	1.1	1.1	1.4
funds from corporate bonds emission	0.2	0.9	0.01	0.0	0.01	0.04	0.00	0.0
funds from stocks emission	10.4	34.8	27.7	38.7	0.5	1.7	1.0	1.2
Foreign investments in the total volume of the investments in fixed assets	124.6	111.3	95.2	100.1	5.7	5.3	3.6	3.2

Source: Federal State Statistics Service.

The banking sector has reacted to the program for investment activity financing support in a reserved manner. In H1 2012 only Rb 262.8bn or 16.2% of Rb 1591.0bn of attracted funds to be directed towards investments in fixed assets were accounted for by the banking credits. The volumes of the banking credits in H1 2012 roughly corresponded to the figure of H1 2009 while ratios of the share of participation of home and foreign banks differed considerably. As a result of H1 2012 the proportion of Russian banks' credits made 81.2%, of foreign banks' credits – 18.8%, the figure for H1 2009 being 69.3% and 30.7%, correspondingly.

In H1 2012 the level of the investment program financing by Russian and foreign banks was negatively influenced by a considerable outflow of the capital. According to the preliminary estimation of the RF Central Bank the net export of the capital by the private sector reached \$43.4bn in January-June of the current year as compared with \$27.1bn a year ago. Besides, in H1 2012 foreign investments in the Russian economy reduced by 14.7% compared with the corresponding period of the previous year and made \$74.8bn. As a result in H1 2012 the volume of foreign investments in fixed assets remained below the figures of 2009–2010 and their proportion in the total volume of the investments in the Russian economy reduced by 3.2% versus 5.5% on average over the period.

The proportion of the budget funds was observed to change in the structure of borrowings for investments in fixed assets financing. In H1 2012 Rb 412.3bn of investments in fixed assets was financed at the expense of the budget funds (13.2% of the total volume of the investments in the economy). The expansion of the investments financing at the expense of the federal budget funds supported the development of the investment and construction complex and compensated for the contraction of the Russian Federation subjects' budgets participation. In January–June 2012 the use of funds at the objects included in FTIP made Rb 122.6bn or 16.9% of the annual limit of budget allotments.

During 2009–2012 the structure of investments in fixed assets as broken by types of economic activities was subject to considerable changes. During the acute phase of the crisis investment activity recession rates in the industry were not as deep as on the whole throughout the economy. The recovery of the positive dynamics of investments in fixed assets has been observed starting with Q1 2011 and was accounted for by the simultaneous growth of the investment demand in both the extractive and manufacturing industries. In H1 2012 the increase in the investments in fixed assets in the industry made 18.1% versus the figure of the previous year, thus exceeding the level of pre-crisis H1 2008 by 21%. The volumes of investments in fixed assets in fossil fuels extraction exceeded the pre-crisis level in H1 2011 due to dynamic growth of the demand for investments.

It is the upsurge in the investment activity in the manufacturing sector that was a characteristic feature in H1 2012. The growth of the investments in fixed assets in manufacturing industries reached 21.5% in H1 2012 which allowed for 11% margin over pre-crisis figure of 2008. It should be noted at the same time that the proportion of the investments in machine-building complex remained within the range 2.2–2.4% of the total volume of investments in fixed assets in the economy. Low investment activity in machine-building complex constraints the fulfillment of the program for the accelerated renovation of the fixed assets.

Another positive trend of H1 2012 is the growth of investments in fixed assets in health care by 22.5%. Such types of activity as education, wholesale and retail trade made a negative contribution in the investments dynamics; the slowdown of investments growing rates in transportation development is also worrying.

The RF Ministry of Economic Development taking into account the dynamics of H1 2012 estimates the growth rates of the investments in fixed assets at the level of 105.5%, of the GDP – at 103.5% in 2012. It should be noted that in H2 2012 the growth rates of the investments in fixed assets are forecast to slow down to 102.4% versus the corresponding period of the previous year, and the GDP – to 102.7%. The situation in the investment sphere is aggravated by the expected by the RF Ministry of Economic Development expansion of the capital outflow to \$60bn and the decrease in the proportion of the gross national savings in the GDP to 27.3% (the average value for the index being 33.4% in 2004–2007).

According to “The Forecast of Socio-Economic Development of the Russian Federation in 2013 and the Planning Period of 2014 and 2015” a considerable improvement of the business environment and the expansion of the investments in fixed assets from 19.7% of the GDP in 2011 to 22.3% in 2015 is expected. According to the moderately optimistic variant, in 2013–2015 average annual growth rates of the investments in fixed assets are estimated at the level of 107.5%, GDP growth rates – at the level of 104.1%.

Table 3  
 INVESTMENTS IN FIXED ASSETS AS BROKEN BY TYPES OF ECONOMIC ACTIVITIES IN H1 2009–2012 (EXCLUDING THE SUBJECTS OF SMALL-SCALE ENTREPRENEURSHIP NOT OBSERVED BY DIRECT STATISTICAL METHODS)

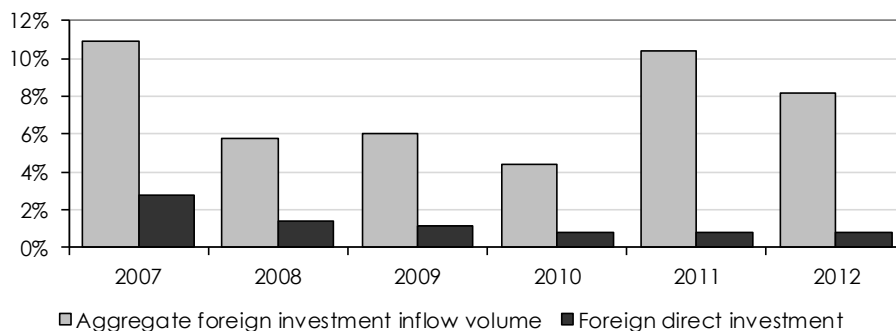
	Rb bn					As percentage to the total					Growth rates versus the corresponding period of the previous year				
	2009	2010	2011	2012	2012	2009	2010	2011	2012	2012	2009	2010	2011	2012	
Total	2188.7	2108.1	2650.9	3155.0	3155.0	100	100	100	100	100	95	89.8	112.3	109.6	
agriculture, hunting and forestry	75.7	70.9	88.5	106.6	106.6	3.5	3.4	3.3	3.4	3.4	74.8	96.3	117.3	106.9	
fishing and fish breeding	1.1	1.5	1.6	4.5	4.5	0.1	0.1	0.1	0.1	0.1	85.8	117.2	105.2	240.0	
industry	987.6	1019.6	1268.3	1597.5	1597.5	45.7	48.3	47.8	51.1	51.1	95.3	98.3	109.4	118.1	
minerals extraction	416.5	429.1	555.1	697.6	697.6	19.0	20.4	20.9	22.3	22.3	90.7	98.5	116.9	117.8	
manufacturing industries	375.5	344.7	439.7	557.3	557.3	17.8	16.3	16.6	17.8	17.8	97.8	84.9	110.5	121.5	
electricity, gas and water production and distribution	195.6	245.8	273.5	342.6	342.6	8.9	11.6	10.3	11.0	11.0	100.6	123.5	95.9	113.4	
construction	78.7	61.0	64.6	73.2	73.2	3.6	2.9	2.4	2.3	2.3	97.5	98.4	93.9	97.4	
wholesale and retail trade	44.9	46.9	54.7	59.8	59.8	2.1	2.2	2.1	1.9	1.9	96.2	89.3	102.9	99.0	
hotels and restaurants	8.6	9.9	10.5	10.9	10.9	0.4	0.5	0.4	0.3	0.3	89.9	111.7	97.1	81.1	
transportation and communication	558.5	537.4	729.9	793.5	793.5	25.5	25.5	27.5	25.3	25.3	105.4	92.0	121.4	99.6	
railway transportation	90.4	140.4	135.6	132.6	132.6	4.1	6.7	5.1	4.2	4.2	61.4	121.4	90.0	86.8	
pipelines transportation	232.5	197.2	313.5	313.4	313.4	10.6	9.4	11.8	10.0	10.0	147.4	87.3	143.3	92.0	
communication	66.6	67.6	92.3	105.5	105.5	3.0	3.2	3.5	3.4	3.4	75	104.0	135.3	112.2	
financial activity	32.1	24.7	33.3	48.9	48.9	1.5	1.2	1.3	1.6	1.6	135.3	78.6	121.3	141.0	
operations with real estate	233.0	188.5	208.3	216.2	216.2	10.6	8.9	7.9	6.9	6.9	76	74.0	99.1	102.7	
state management and military security; social insurance	33.7	26.9	26.1	42.4	42.4	1.5	1.3	1.0	1.4	1.4	106.7	77.2	99.9	99.6	
education	32.8	32.0	46.0	48.6	48.6	1.5	1.5	1.7	1.5	1.5	80.9	94.4	135.8	99.0	
health care and social services	38.7	41.3	41.3	53.7	53.7	1.8	2.0	1.6	1.7	1.7	93.2	107.9	97.8	122.5	
other utilities, social and personal services rendering	48.8	47.5	77.8	79.2	79.2	2.2	2.2	2.9	1.9	1.9	98.4	146.9	146.9	121.5	

Source: Federal State Statistics Service.

## FOREIGN INVESTMENT IN THE RUSSIAN ECONOMY

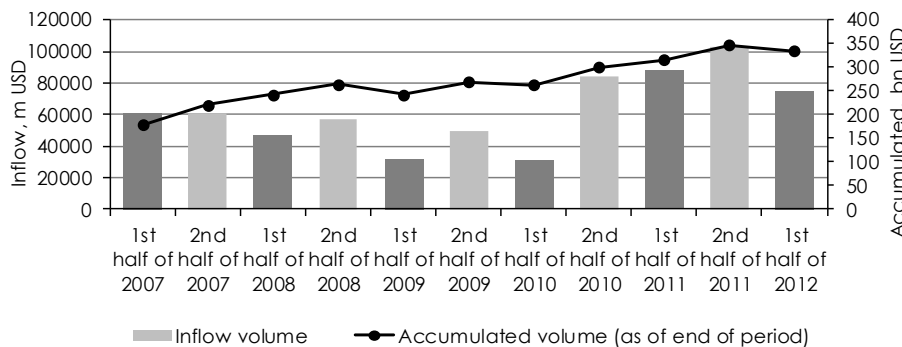
E.Lukhina

In the first half-year of 2012, the inflow of foreign investment in the Russian economy declined. This decline was produced by the shrinking 'other' investments, whose share in the overall foreign investment structure dropped to 88.2%. The share of direct investment increased to 10.2%. The volume of capital withdrawn amounted to 90.2% of that of foreign investment inflow over the same period. Industry is the most attractive field for foreign investors, followed by financial operations and trade. In terms of geographical structure, the highest share of investment inflow in the RF over the 1<sup>st</sup> half-year of 2012 was taken up by Switzerland – 41.1% of the total volume of foreign investment in the Russian economy.



Source: Rosstat.

Fig. 1. Foreign Investment Inflow in the Russian Economy in the First Half-year of 2007–2012 (as % of GDP)



Source: Rosstat.

Fig. 2. Foreign Investment Volume in the Russian Economy (Without Adjustment by Monetary Regulation Measures in the Banking Sector)

In the first half-year of 2012, foreign investment in the Russian economy amounted to \$ 74.8bn, which is by 14.7% lower than the same index for the 1<sup>st</sup> half-year of 2011. The level of foreign investment inflow (as % of GDP) declined on the previous year.

As of 1 July 2012, accumulated foreign investment in Russia, including investment flows from the CIS, amounted to \$ 334.7bn, which is 6.2% above the index registered as of 1 July 2011 and 3.6% below the level achieved as of 1 January 2012.

In the first half-year of 2012, the volume of capital outflow in the form of incomes of foreign investors transferred abroad and the interest on loans and loan redemption amounted to \$ 67.5bn, which is by 17.4% less than the same index for the 1<sup>st</sup> half-year of 2011. This year, the volume

of capital outflow will amount to 90.2% of the foreign investment inflow volume (over the 1<sup>st</sup> half-year of 2011, investment outflow amounted to 93.2% of the foreign investment inflow volume).

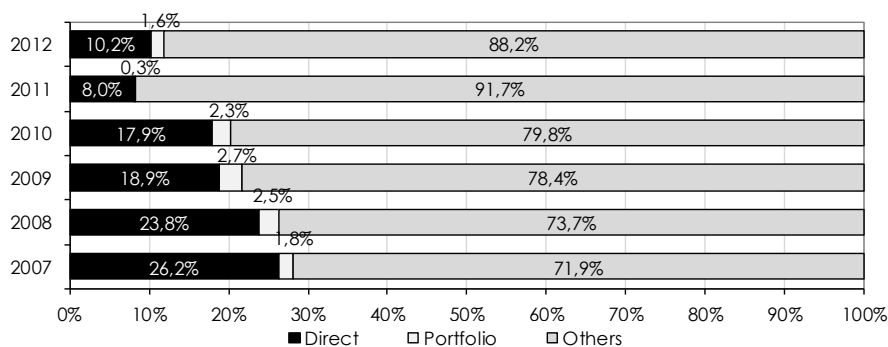
The bulk of foreign investment inflow in the Russian economy is represented by "other" investment<sup>1</sup>.

Over the first half-year of 2012, Russia experienced growth of foreign direct investment, taking place against the backdrop of declining indices of "other" and aggregate foreign investment, which resulted in an increased share of direct investment in the overall investment structure

<sup>1</sup> Direct investments are investments in real assets, acquisition of a controlling stake or a stake with the right of participation in management; portfolio investments are investments in securities solely for deriving income; "other" investments are returnable investments (credits issued by international financial organizations, commercial credits, etc.).



(to 10.2%). By the results of the 1<sup>st</sup> half-year of 2012, foreign direct investment amounted to \$ 7.6bn, which is 8.0% above the level recorded over the period of January–June 2011. Similarly to last year's situation, in Q2 2012 the foreign direct investment inflow declined on the previous quarter by 3.3% (in Q2 2011 the decline amounted to 6.7%). At the same time, in Q2 2012 this index increased by 18.6% on



Source: Rosstat.

Fig. 3. Structure of Foreign Investment Volume in the Russian Economy in the First Half-year of 2007 – 2012

the same period of the previous year. The by-sector structure of foreign investment attracted into the Russian economy over the 1<sup>st</sup> half-year of 2012 is characterized by a significant shrinkage of investment in financial activities (by 34.7% on the 1<sup>st</sup> half-year of 2011). Thus, the leading position in the structure of foreign investment formerly belonging to that sector was taken over by industry.

Table 1

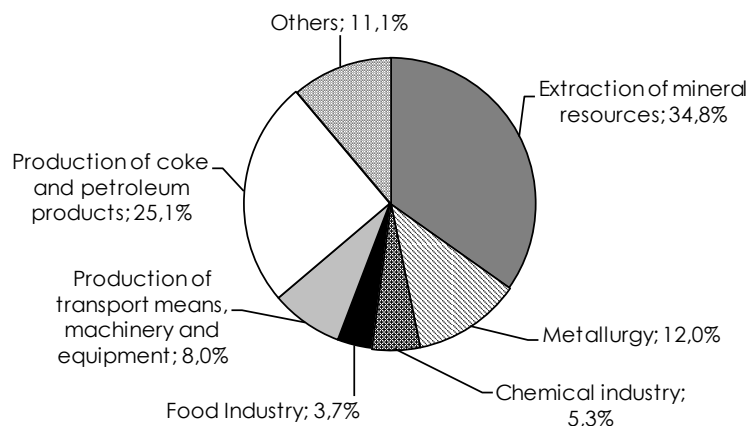
BY SECTOR STRUCTURE OF FOREIGN INVESTMENT IN THE RUSSIAN ECONOMY IN THE FIRST HALF-YEAR OF 2009–2011

	In m USD				As % of total			
	2009	2010	2011	2012	2009	2010	2011	2012
Industry	13,230	18,047	28,149	29,959	41.1	59.4	32.1	40.1
Transport and communications	6,511	3,082	4,751	2,634	20.2	10.1	5.4	3.5
Trade and public catering	7,995	4,620	6,788	8,723	24.9	15.2	7.7	11.6
Operations with real estate, renting and service rendering	2,670	2,553	2,956	3,705	8.3	8.4	3.4	5.0
Finance, credit, insurance, pension	1,025	1,321	44,432	29,004	3.2	4.4	50.7	38.8
Other sectors	732	761	622	764	2.3	2.5	0.7	1.0

Source: Rosstat.

This year, the volume of foreign investment in industry rose on the 1<sup>st</sup> half-year of 2011 by 6.4%. The amount of foreign money invested in trade and public catering increased by 28.5%; and that invested in operations with real estate – by 15.8% respectively. The volume of investment in the transport and communications sector declined by 44.6%.

In industry, over the 1<sup>st</sup> half-year of 2012, as before, the most attractive were the processing sectors, which received a total of \$ 18.5bn, or 61.8% of the aggregate money invested in industry (in the 1<sup>st</sup> half-year of 2011 – \$ 16.3bn or 58.0%). Investment in the extraction of mineral resources over that period declined by 9.0% to \$ 10.4bn; in metallurgy – by 10.6%, to \$ 3.6bn. Investment in the production of coke and petroleum products increased by 22.6%, to \$ 7.5bn; in the food industry – by 6.1%, to \$ 1.12bn. Over the 1st half-year of 2012, the share



Source: Rosstat.

Fig. 4. Structure of Foreign Investment in Industry in the First Half-year of 2012

of foreign direct investment in the overall structure of investment in industry dropped on the 1<sup>st</sup> half-year of 2011 from 16.2% to 14.6%. The shares of “other” and portfolio investment in industry over the period under consideration is estimated to be 81.8% and 3.6% respectively (in 1<sup>st</sup> half-year of 2011 – 83.3% and 0.5%).

Table 1

## FOREIGN INVESTMENT IN INDUSTRY IN THE FIRST HALF-YEAR OF 2012

	m USD			As % of 1 <sup>st</sup> half-year of 2011		
	direct	portfolio	other	direct	portfolio	other
Industry	4,378	1,080	24,501	96.1	739.7	104.5
Including:						
Extraction of mineral resources	1,338	5	9,087	47.8	15.2	105.3
Metallurgy	52	953	2,596	59.8	incr. 317.7 times.	65.9
Chemical	146	1	1,443	96.1	50.0	115.1
Food	505	1	617	200.4	100.0	76.6
Other sectors	2,337	120	10,758	184.7	112.1	122.0

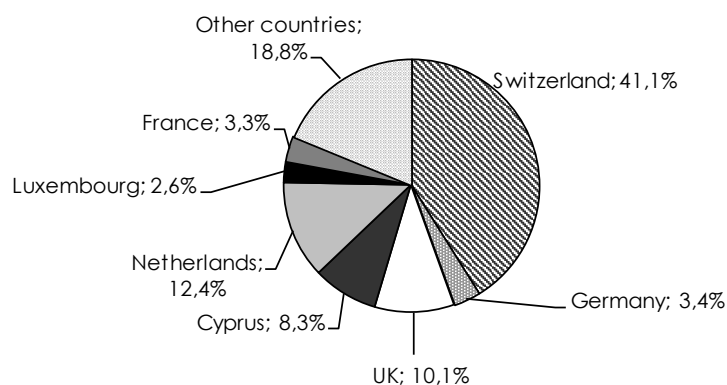
Source: Rosstat.

Over the 1<sup>st</sup> half-year of 2012, the extracting industry received 17.6% of foreign investment from direct investors (over the 1<sup>st</sup> half-year of 2011 – 39.8%). The processing industry received 37.4% of the aggregate foreign direct investment inflow in the Russian economy (over the 1<sup>st</sup> half-year of 2011 – 23.1%); trade and public catering – 11.3% (over the 1<sup>st</sup> half-year of 2011 – 7.0%); operations with real estate and services – 17.9% (over the 1<sup>st</sup> half-year of 2011 – 17.5%).

The priority target for portfolio investors in the 1<sup>st</sup> half-year of 2012 became the processing industry, which received 81.4% of the aggregate foreign direct investment inflow in the Russian economy (in the 1<sup>st</sup> half-year of 2011 – 11.6%); the production of electric energy, gas and water supply received 8.7% of foreign portfolio investment (in the 1<sup>st</sup> half-year of 2011 – 35.3%).

The highest volume of ‘other’ investment in the 1<sup>st</sup> half-year of 2012 went to financial activities – 43.2% of the aggregate foreign direct investment inflow in the Russian economy (in the 1<sup>st</sup> half-year of 2011 – 55.0%). Investment in the processing industry amounted to 22.3% of the aggregate volume of ‘other’ investment (in the 1<sup>st</sup> half-year of 2011 – to 18.2%); investment in the extraction of mineral resources – to 13.8% (in the 1<sup>st</sup> half-year of 2011 – to 10.7%); investment in trade – to 11.9% (in the 1<sup>st</sup> half-year of 2011 – to 7.8%), and investment in the transport and communications sector amounted to 3.6% of ‘other’ foreign investment (in the 1<sup>st</sup> half-year of 2011 – to 5.6%).

The leading position in the geographical structure of the foreign investment inflow in the Russian economy over the 1<sup>st</sup> half-year of 2012, as before, was occupied by Switzerland, whose investment in Russia amounted to \$ 30.7bn, or 41.1% of the aggregate foreign investment inflow in the Russian economy. Out of that amount, 89.4% was invested in financial activities.



Source: Rosstat.

Fig. 5. Geographical Structure of Foreign Investment Inflow in the Russian Economy in the First Half-year of 2012

In the 1<sup>st</sup> half-year of 2012, The Netherlands increased the amount of its investment in Russia by 18.6% – to \$ 9.3bn; the UK – by 91.9% to \$ 7.5bn; Luxemburg – by 38.3% to \$ 1.9bn. On the other hand, the results of the 1<sup>st</sup> half-year of 2012 demonstrated that Germany over that period decreased its investment in the Russian economy by 54.2% on the same period of 2011 – to \$ 2.6bn; Cyprus – by 17.9%, to \$ 6.2bn. Over that period, a decline in the level of investment was also displayed by Switzerland – the leader among the investor countries (by 33.8%).

Over the 1<sup>st</sup> half-year of 2012, the share of 10 topmost investor countries in the

Russian economy amounted to 84.7% of the aggregate volume of accumulated foreign investment as of 1 July (the same index for the 1<sup>st</sup> half-year of 2011 is 83.8%), including: 78.1% of accumulated direct investment (in the 1<sup>st</sup> half-year of 2011 – 78.6%), 82.2% (87.1%) and 89.4% (87.2%) of accumulated portfolio and “other” investment respectively.

Table 2

MOVEMENT OF ACCUMULATED FOREIGN INVESTMENT, BY MAJOR INVESTOR COUNTRY,  
AS OF 1 JULY 2012

	As % of amount as of 1 July 2011				As % of amount as of 1 January 2012			
	Total	Direct	Portfolio	Other	Total	Direct	Portfolio	Other
Ireland	83.0	55.4	80.0	84.3	83.4	52.2	400.0	85.0
Germany	85.3	100.8	100.0	76.1	87.0	96.5	100.0	80.8
Japan	107.4	100.3	133.3	108.2	101.0	86.4	66.7	102.9
UK	121.1	88.7	64.8	149.7	96.0	90.7	64.5	104.7
Cyprus	101.9	102.3	121.1	99.3	91.0	89.4	94.1	95.0
The Netherlands	129.5	94.8	82.8	172.1	113.4	94.9	104.3	130.6
Luxembourg	106.7	187.5	83.6	105.4	99.3	115.9	79.9	99.0
China	102.2	107.8	8.3	101.9	100.3	92.0	100.0	100.7
Other countries	106.1	112.8	150.7	95.6	93.5	94.8	106.2	90.7
Total	106.2	103.5	97.6	108.6	96.4	92.5	84.0	99.7

Source: Rosstat.

Against the backdrop of declining foreign investment in the Russian economy, the amount of investment outflow from Russia increased over the 1<sup>st</sup> half-year of 2012 by 3.4%, to \$ 69.5bn, thus amounting to 92.9% of the total volume of foreign investment in the Russian economy in January-June 2012 (in the 1<sup>st</sup> half-year of 2011 – 76.6%). The bulk of that amount – \$ 26.5bn (or 38.1% of the aggregate investment outflow from Russia in the 1<sup>st</sup> half-year of 2012) – went to Switzerland; 14.4% or \$ 10.0bn to Austria; 6.0% or \$ 4.1bn – to The Netherlands; and 9.5% (or \$ 6.6bn) and 5.9% (or \$ 4.1bn) to Cyprus and Belarus. ●

## THE FOREIGN TRADE

N.Volovik, K.kharina

*In a situation of slowdown of global trade growth, growth in the Russian foreign trade turnover is declining, as well. It is to be noted that though during seven months of this year trade with far abroad countries showed positive dynamics there was a recession in relations with CIS states. The Eurasian Economic Commission stepped up its activities to protect the domestic market of the Customs Union in a situation of Russia's accession to the World Trade Organization.*

In September 2012, the World Trade Organization (WTO) revised downward the forecast as regards global trade growth in 2012 to 2.5% from the April forecast of 3.7%. The 2013 forecast was revised downward from 5.6% to 4.5%. From the date of the previous evaluation of the global trade development, the problems of the global economy have aggravated: economic growth in China is slowing down, the data on the rate of unemployment and manufacturing in the US is worse than expected and the debt crisis in the euro area still prevails.

Reduction of growth rates of global trade in 2012 has been caused by a drop in developed countries' imports and, as a consequence, reduction in export volumes to developing countries. On the basis of the 2012 results, the WTO expects that the volume of import of developed countries will increase by the mere 0.4%, while that of developing countries, by 5.4% (according to the April forecast growth of 1.9% and 6.2%, respectively was anticipated). The forecast as regards the volume of export was revised downward in developed countries from 2% to 1.5%, while in developing countries, from 5.6% to 3.5%.

In July 2012, Russia's foreign trade turnover calculated on the basis of the methods of the balance of payments increased by 1.1% as compared to last July and amounted to \$70.2bn. The volume of the Russian export in the same period amounted to \$40.6bn which is 3.2% lower than in July 2011. In July 2012, the volume of import to the Russian Federation amounted to \$29.6bn which is 7.7% higher than the 2011 index. As a result, in July 2012 the foreign trade balance fell by 23.8% to \$11bn as compared to July 2011.

According to the data of the Central Bank of the Russian Federation, in January–July 2012

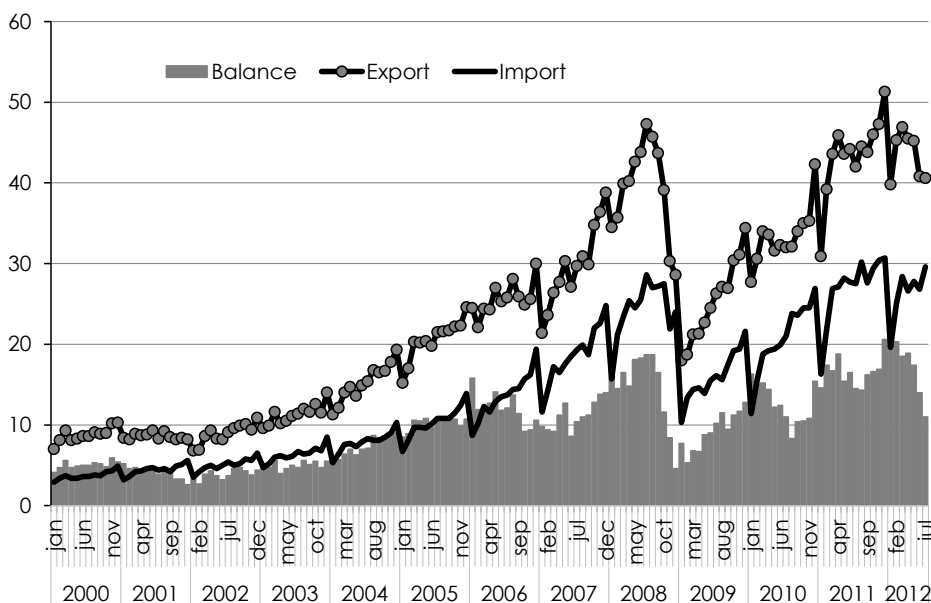


Fig. 1. The main indices of the Russian foreign trade, billion \$

Russia's foreign trade turnover amounted to \$487.9bn – which is 5.0% higher than the index of the last year – including \$304,0bn worth of export (growth of 5.2%) and \$183.8bn worth of import (growth of 4.7%). The export surplus remained positive and amounted to \$120.2bn (in January–July 2011 it was \$113.3bn).

Growth in foreign trade turnover took place as a result of expansion of trade relations with far abroad countries; during seven months of this year the trade turnover with

those countries increased by 6.2%, while that with CIS countries fell by 1.4% due to a reduction of 5.7% in import supplies.

In July 2012, though the foreign trade situation remained favorable, it became much worse as compared to last July (in July 2012 Russia's trade conditions index fell to 102.2 against 125.8 in July 2011). In July 2012, the index of trade conditions with far abroad countries amounted to 100.2 (in July 2011 it was 128.1), while that of trade conditions with CIS countries, to 115.1 (in July 2011 it was 112.9).

The dynamics of export is still dependent on fluctuations on the global commodities markets.

In July 2012, prices on Brent oil fluctuated in the range of \$96.82–107.76 a barrel, while in August 2012, in the range of \$106.05–116.2 a barrel.

On the basis of the results of the meeting on September 12–13, 2012, the US Federal Reserve System (FRS) announced its plans to buy-out government bonds with a 10-year maturity or US Treasuries within the frameworks of the QE3 quantitative mitigation program. The regulator left the base interest rate unchanged at the level of 0–0.25%. The FRS will buy-out \$40bn worth of mortgage securities a month starting from October. In September, the buy-out volume will amount to \$23bn.

The quantitative mitigation resulted in growth in oil prices: on September 15 Brent oil prices rose to \$116.92 a barrel which is the maximum level since May 2012. However, that effect happened to be short-lived. As early as September 19, oil prices went down to \$108.07 a barrel after the regular data on growth in the US oil and oil products reserves was made public. The negative effect on trading was caused by rumors that Saudi Arabia was going to increase production of oil.

In July 2012, Urals oil price on the global market amounted to \$102.6 a barrel which is 9.8% higher than in June 2012; as compared to July 2011 the price fell by 11.0%. In January–July 2012, the price on Urals oil amounted to \$110.6 a barrel which is 1.3% higher than in the respective period of 2011.

According to the monitoring of the Ministry of Finance of the Russian Federation, from August 15 till September 14 the average price on Urals oil amounted to \$113.98 a barrel. As a result, from October 1, 2012 the export duty on crude oil will grow by 6.4%, that is, from \$393.8 a ton in September 2012 to \$418.9 a ton (Resolution No. 954 of September 22, 2012 of the Government of the Russian Federation). From October 1, 2012, the single export duty rate on light and dark oil products, except for petroleum, calculated on the 60/66/90 method will amount to \$276.4 a ton against \$259.9 a ton in September. It is to be noted that in October the duty on petroleum preserved at the level of 90% of the oil duty will amount to \$377 a ton (\$354.4 a ton in September 2012).

In July 2012, global prices on non-ferrous metals on the London Metal Exchange (LME) were at a rather low level. Slowdown of the global economy has a negative effect on the balance between the global supply and demand of metals in physical terms. Seasonal factors do not support prices, either. In addition to that, metal quotations are falling due to large stock reserves at LME.

In July 2012, global prices on non-ferrous metals depreciated largely as compared to the same period of 2011. As compared to July 2011, prices on aluminium, copper and nickel fell by 25.7%, 21.4% and 32.4%, respectively. In January–July 2012, aluminium, copper and nickel were traded 19.6%, 15.0% and 28.7% lower, respectively, as compared to the same period of 2011.

Table 1

## AVERAGE MONTHLY PRICES IN JULY OF THE RESPECTIVE YEAR

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Oil (Brent), USD/barrel	25.7	28.25	38.2	56.4	72.5	75.09	139.23	65.74	75.6	116.46	103.14
Natural gas*, USD/1 million BTU	2.95	4.04	4.28	6.42	8.585	8.13	14.37	6.67	8.04	10.99	11.13
Petroleum, USD/gallon	0.804	0.896	1,306	1,601	2,271	2,182	3,313	1,771	2.06	3.13	3.18
Copper, USD/ton	1589.0	1730.3	2813.0	3614.0	7712	7962.7	8415.3	5215.5	6735.3	9650.5	7584.3

Table 1, cont'd

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Aluminium, USD/ton	1338.4	1434.9	1710.0	1779.0	2513	2730.7	3071.2	1668	1988.3	2525.4	1876.3
Nickel, USD/ton	7143.1	8790.6	15038	14581	26585	33373	20160	15985	19518	23848	16128

\* Market of Europe, average contractual price, franco border.

Source: calculated on the basis of the data of the London Metal Exchange and the Intercontinental Oil Exchange (London).

After a three months' decline, in July 2012 the FAO food price index rose by 6% gaining another 12 points from this June. Sharp growth in the Index was mainly justified by growth in prices on grain and sugar. In July 2012, the crops price index amounted to 260 points having appreciated by 17% or 38 points as compared to the June index. Also, in July the sugar price index grew sharply by 12% or 34 points from June to amount to the record-high level of 324 points. Such high growth which put an end to slow depreciation of prices from this March was justified by off-season rains in Brazil – the largest sugar exporter – which situation complicated harvesting of sugar cane in July. Global prices on meat and dairy products changed insignificantly.

In a situation of accession of the Russian Federation to the World Trade Organization, an important component of regulation of foreign trade of the Customs Union became application of instruments of domestic market protection – such as special protective antidumping and mitigation measures – against an unfavorable effect of foreign competition. In international trade practice, those instruments are used for effective neutralization of damage to industry from dumping, subsidized or increased import of goods from abroad.

From May 2012, the authorities to carry out antidumping and special protective investigations were transferred from national authorities of the Customs Union-member states to the Department of Protection of the Domestic Market of the Eurasian Economic Commission (EEC). Before that, the above authorities were carried out by the Ministry of Industry and Trade. During a few months, the Department carried out and accomplished two investigations in respect of import deliveries to the Customs Union of polymer rolled metal and cast-iron baths. As a result, antidumping duties and annual quotas have been imposed on those products.

Due to expiry of the term of the antidumping measure in September 2012, a repeated antidumping investigation was started in respect of antifriction bearings (except for needle ones) which were produced in China and brought to the single customs territory of the Customs Union. In accordance with the decision of June 22, 2011 of the Commission of the Customs Union, antidumping duties in the amount of 31.3% and 41.5% of the customs value were introduced for OOO “Podshipnik i Kachenia Usi” and other manufacturers, respectively. The above measure will be in effect till January 20, 2013.

Following antidumping investigations, EEC started to adopt a format of protective investigations: on July 6, 2012 a special protective investigation in respect of import of grain harvesters to the single customs territory of the Customs Union on the basis of the application submitted by OOO “Kombainovy Zavod Rostselmash” and OAO “Proizvodstvennoe Obyedinenie Krasnoyarsky Zavod Kombainov” was begun. The application was supported by RUP “Gomelsky Zavod Selskokhozyastvennogo Mashinostroeniya (Gomselmash)” and OAO “Lidagroprommash”. The applicants and enterprises which supported the above application account for 95.9% of the production volume of grain harvesters in the Customs Union.

In September 2012, a special protective investigation in respect of import of porcelain tableware and kitchenware to the single customs territory of the Customs Union was started. In the 2009–2011 period, applicant-enterprises and enterprises which supported the application (ZAO “Farfor Verbilok”, OAO “Imperatorsky Farforovy Zavod”, ZAO “Dobrushsky Farforovy Zavod” and PK “Dulevsky Farforovy Zavod”) accounted on average for 81.1% of the production volume of porcelain tableware and kitchenware in the single customs territory of the Customs Union. ●

## STATE BUDGET

T.Tishchenko

According to the Federal Treasury, in January–August 2012, federal budget revenues amounted to 22.0% of GDP, which is by 0.1 percentage points GDP higher than in the corresponding period of the last year. The federal budget expenditures over eight months of the year have increased by 1.0 p.p. of GDP against the same period of 2011, amounting to 20.6% of GDP. As of January–August 2012 results, the federal budget was executed with a surplus of 1.4% of GDP. The main growth of the federal budget was provided by the oil and gas revenues reached 11.2% of GDP, which exceeds the indicator of January–August 2011 by 1.4 p.p. The government domestic debt in August of this year has slightly decreased to Rb 4,427.4bn.

### Analysis of key indicators of the federal budget execution in January–August 2012

For January–August 2012, the revenues of the federal budget amounted to Rb 8353.8bn, which is by Rb 1133.4bn, or 0.1 p.p. of GDP higher than in the relevant period of the last year (Table 1). Oil and gas revenues for the same period increased to 11.2% of GDP, or 1.4 p.p. of GDP against eight months of 2011. The budget expenditure for January–August 2012 amounted to Rb 7822.7bn, i.e., Rb 1362.6bn (by 1.0 p.p. of GDP) higher as compared to the same period of the last year.

As of January–August 2012, federal budget was executed with a surplus of Rb 531.1bn (1.4% GDP), which is 0.9 p.p. of GDP lower against eight months of the past year. The volume of non-oil deficit has grown to 9.8% of GDP, which exceeds the indicator of the relevant period of the last year by 2.3 p.p. of GDP.

Table 1

#### KEY INDICATORS OF THE RF FEDERAL BUDGET IN JANUARY–AUGUST 2011–2012

	January–August 2012		January–August 2011		Change, p.p. of GDP
	Rb bn	GDP%	Rb bn	GDP%	
Revenues, including:	8353.8	22.0	7220.4	21.9	0.1
Oil and gas revenue	4237.6	11.2	3220.5	9.8	1.4
Expenditures, including:	7822.7	20.6	6460.1	19.6	1.0
Percentage expenditures	221.5	0.6	164.2	0.5	0.1
Non-percentage expenditures	7601.2	20.0	6295.9	19.1	0.9
Federal budget surplus (deficit)	531.1	1.4	760.3	2.3	–0.9
Non-oil and gas deficit	–3706.5	–9.8	–2460.2	–7.5	–2.3
GDP estimates	38057		33055		

Source: Federal Treasury, Gaidar Institute assessments.

Dynamics of the federal budget revenues within January–August 2012 (Table 2) shows the increase in revenues as compared to the same period of the last year in terms of MET by 0.3 p.p. of GDP, in customs duties – by 0.1 p.p. of GDP, in revenue from excise taxes on goods produced in the RF territory, and in VAT on imports – by 0.1 p.p. of GDP, respectively. One should note the reduction in federal revenues over 8 months of this year in domestic VAT by 0.2 p.p. of GDP against the relevant period in 2011.

In regard to the expenditures of the federal budget (Table 3), growth of expenses for January–August of this year as compared with the same period of the last year is observed under the budget lines “National security and law enforcement” – by 0.6 p.p. of GDP, “National Defense” – by 0.5 p.p. of GDP, “Healthcare” – by 0.2 p.p. of GDP, in each of the budget lines “Education”, “Social Policy”, “National Debt Service” – by 0.1 p.p. of GDP.

Table 2

## DYNAMICS OF FEDERAL BUDGET REVENUES FROM BASIC TAXES IN JANUARY–AUGUST 2011–2012, IN ABSOLUTE TERMS AND GDP P.P.

	January–August 2012		January–August 2011		Change, p.p. of GDP
	Rb bn	GDP%	Rb bn	GDP%	
1. Revenue, including:					
corporate profit tax	271.4	0.8	239.9	0.8	0.0
VAT on goods sold in the RF territory	1221.7	3.3	1150.1	3.5	–0.2
VAT on goods imported to the RF territory	1071.5	2.9	923.1	2.8	0.1
Excise duties on goods manufactured in the RF territory	218.7	0.6	148.0	0.5	0.1
Excise duties on goods imported to the RF territory	33.6	0.1	27.3	0.1	0.0
MET	1599.0	4.2	1284.0	3.9	0.3
2. Revenue from external economic activities	3248.3	8.6	2810.6	8.5	0.1

Source: Ministry of Finance of Russia, Russian Statistical Service, Gaidar Institute assessments.

Table 3

## FEDERAL BUDGET EXPENDITURES IN JANUARY–AUGUST 2011–2012

	January–August 2012		January–August 2011		Change, p.p. of GDP
	Rb bn	GDP%	Rb bn	GDP%	
Expenditures, total:	7822,7	20,6	6460,1	19,6	1,0
<i>Including</i>					
Federal issues	475.3	1.3	421.3	1.3	0.0
National defense	1186.2	3.2	868.4	2.7	0.5
National defense and law enforcement	995.2	2.7	696.1	2.1	0.6
National Economy	975.0	2.6	851.6	2.6	0.0
Housing and public utilities	53.5	0.2	137.6	0.5	–0.3
Environmental protection	14.0	0.1	9.0	0.1	0.0
Education	410.5	1.1	311.6	1.0	0.1
Culture and cinematography	50.5	0.2	41.7	0.2	0.0
Healthcare	356.2	1.0	263.2	0.8	0.2
Social policy	2620.5	6.9	2218.0	6.8	0.1
Physical training and sports	28.2	0.1	27.4	0.1	0.0
Mass media	47.4	0.2	38.0	0.2	0.0
Public and municipal debt servicing	221.5	0.6	164.2	0.5	0.1
Interbudgetary transfers	388.4	1.1	411.0	1.3	–0.2

Source: Federal Treasury, Gaidar Institute assessments.

In terms of GDP share, reduction in expenses over January–August 2012 was observed against the relevant period of the last year in the budget lines “Housing and Utilities” by 0.3 p.p. of GDP and “Intergovernmental transfers” by 0.2 p.p. of GDP. In other budget lines expenditures of the federal budget over eight months of this year in GDP share remained at the level of January–August 2011.

According to the Russian Ministry of Finance, at the end of August 2012 the Reserve Fund and the National Welfare Fund volumes have slightly grown due to exchange rate changes to Rb 1953.1 and Rb 2772.5 bn, respectively.

The structure of the federal budget reflects the increasing dependence of the budget on oil and gas revenues. In the 2012 budget forecast it was planned to increase the share of non-oil revenues in the total federal revenues from 50.7% in 2011 to 52.7% in 2012 due to the increased tax rev-



enue from VAT and excise duties, but these projections did not come true so far. As of September 1, 2012 the amount of the federal budget revenue from VAT and excise duties is recorded at 6.9% GDP (similar to the last year indicator). A higher-than-anticipated growth of federal revenues is noted in oil and gas revenues: if over eight months of this year the revenue of the federal budget amounted to 65.9% of the total estimated tax revenue, the share of oil and gas revenues of the budget execution for the same period amounted to 68.3% of the anticipated amount. It is worth noting that an increased share of revenues from foreign trade in the total federal revenues to 33.1% in January, 37.8% as of two and three months, 38.1% – as of four months and to 39.8% up to eight months of the year due to increased revenue from hydrocarbon exports.

Thus, with the forecasted reduction in the rate of economic growth, in the 2nd half of the current year there is a probability of the fiscal system stability deterioration in the short term, even at the background of continued growth of the global prices for hydrocarbons.

### RF Subjects consolidated budget execution in January–July 2012

According to the Federal Treasury, *the revenue of consolidated budget of the Russian Federation Subjects* in seven months 2012 amounted to 14.3% of GDP, which is by 1.0 p.p. of GDP lower than in the same period of 2011 (*Table 4*). Expenditures of the consolidated budget of the Russian Federation Subjects in January–July this year increased against the same period of the last year by 0.4 p.p. of GDP and accounted for 12.7% GDP. As of seven months of 2012 performance, the RF Subjects' consolidated budget is executed with a surplus of 1.6% of GDP (Rb 502.1bn), which is by 1.5 p.p. of GDP lower than in January–July 2011.

Table 4

#### KEY INDICATORS OF THE RF SUBJECTS CONSOLIDATED BUDGET IN JANUARY–JULY 2011–2012

	January–July 2012		January–July 2011		Change, p.p. of GDP
	Rb bn	GDP%	Rb bn	GDP%	
Revenues, including:	4678.0	14.3	4467.3	15.3	–1.0
– Corporate profit tax	1275.1	3.9	1230.0	4.2	–0.3
– Individual income tax	1231.5	3.8	1071.5	3.7	0.1
– Excise duties in the RF territory	253.9	0.8	209.4	0.8	0.0
– Aggregate income tax	193.4	0.6	146.8	0.5	0.1
– Property tax	482.3	1.5	419.4	1.5	0.0
– Non-repayable proceeds from other budgets of the RF fiscal system	895.5	2.8	933.7	3.2	–0.4
Expenditures,	4175.9	12.7	3580.7	12.3	0.4
Surplus/Deficit of the RF Subjects consolidated budget	502.1	1.6	886.6	3.1	–1.5
GDP estimates	32917		29 290		

Source: Federal Treasury, Gaidar Institute assessments.

The major decrease in the revenue proceeds of the consolidated budget of the RF Subjects in January–July this year versus seven months of the last year is noted in intergovernmental transfers – by 0.4 p.p. of GDP and corporate income tax – by 0.3 p.p. of GDP. According to the Rosstat operative data, the net financial result of organizations (except small businesses, banks, insurance companies and public institutions) in prices effective for seven months of 2012 amounted to Rb 4524.9bn, while over the same period of the last year – Rb 4664.3bn. It should be noted that the decrease in income tax revenue was observed only in the regional budgets, while the amount of this tax revenue of the federal budget in term of GDP share did not change against the same period of the last year. In part this can be explained by both, the immutability of the tax base on the grounds that revenue is addressed exclusively to the federal budget (for example, the corporate income tax on income earned in the form of dividends from Russian organizations to foreign ones), and the extension of local tax benefits granted at the expense of reducing the regional component of the tax rate.

Within January–July 2012 revenues of the consolidated budgets from personal income tax and tax on the total income have somewhat increased – by 0.1 p.p. of GDP against indicators thereof in

the same period of the last year. Proceeds from excise tax and property tax of the regional budgets in the last seven months of the year in terms of GDP share remained at the level of the relevant period in 2011.

RF Subjects consolidated budget execution in terms of expenditures (*Table 5*) in seven months of 2012 amounted to Rb 4175.9bn, or 12.7% of GDP, which exceeds the level of the relevant period of preceding year by 0.4% of GDP.

Table 5

RF SUBJECTS CONSOLIDATED BUDGET EXECUTION IN TERMS OF EXPENDITURES  
IN JANUARY–JULY 2011–2012

	January–July 2012		January–July 2011		Change, p.p. of GDP
	Rb bn	GDP%	Rb bn	GDP%	
Expenditures, total:	4175,9	12,7	3580,7	12,3	0,4
Including					
Federal issues	265.8	0.8	242.0	0.9	–0.1
National defense	1.9	0.0	1.6	0.0	0.0
National defense and law enforcement	42.9	0.2	135.1	0.5	–0.3
National Economy	681.2	2.1	526.9	1.8	0.3
Housing and public utilities	388.2	1.2	359.2	1.3	–0.1
Environmental protection	9.2	0.1	6.9	0.1	0.0
Education	1135.9	3.5	890.4	3.1	0.4
Culture and cinematography	136.4	0.5	111.9	0.4	0.1
Healthcare	690.4	2.1	556.0	1.9	0.2
Social policy	689.3	2.1	628.0	2.2	–0.1
Physical training and sports	69.6	0.2	63.5	0.3	–0.1
Mass media	19.2	0.1	15.6	0.1	0.0
Public and municipal debt servicing	36.1	0.1	34.1	0.2	–0.1
Interbudgetary transfers	9.8	0.1	9.0	0.1	0.0

Source: Federal Treasury, Gaidar Institute assessments.

The main growth of consolidated budget of the RF Subjects over seven months of the current year was noted under the budget lines “Education” – by 0.4 p.p. of GDP, “National economy” – by 0.3 p.p. of GDP, “Healthcare” – by 0.2 p.p. of GDP as compared to January–July 2011. Regional budget expenditures under the line “Culture and Cinematography” have grown by 0.1 p.p. of GDP over seven months of the current year against the relevant period of the last year.

As of January–July this year, there was noted an insignificant decline of expenditures under the budget lines “Federal issues” – by 0.1 p.p. of GDP, “National security and law enforcement” – by 0.3 p.p. of GDP, “Housing and communal services” – by 0.1 p.p. of GDP, “Social Policy” – by 0.1 p.p. of GDP, “Physical Training and Sports” – by 0.1 p.p. of GDP, “Public Debt Servicing” – by 0.1 p.p. of GDP against the same period of the last year. Reduction in expenditures of consolidated budgets of the RF Subjects under the line “National Security and Law Enforcement” in the current year is expected due to the transfer of responsibility for police financing from regional authorities to the federal level since the beginning of 2012. The expenditures volume of consolidated regional budgets of the RF Subjects within January–July 2012 under the lines “National Defense”, “Environmental Protection”, “Mass media and “Intergovernmental transfers” as GDP percentage remained unchanged. ●

## RUSSIAN BANKING SECTOR

M.Khromov

*In August 2012, the growth of bank assets has slowed down. The reason for this was the decreased growth rate of the main types of funds – foreign liabilities and assets of enterprises and organizations. However, the increased government support and reduced investments in foreign assets allowed to keep up the growth rate of the economy crediting.*

Growth rate of total banking sector assets in August 2012 was decelerated. Over the month, they increased by 0.7%<sup>1</sup>. Annual growth rates remained at the level of 22%. The basic contribution to slowing growth of the banking sector assets was made by assets reduction of medium and small banks, as well as foreign banks (1.0%). The leading positions were traditionally held by state-owned banks, whose assets increased by 1.7%.

Capital adequacy of the banking sector in August remained at about 13.3%, with the exception of Sberbank and VTB, the relevant indicator of which amounted to 13.8%. This confirms our assumptions, that the July decline in the capital adequacy by 0.5 p.p. was caused solely by the prudential innovations, namely by changes in the method of calculating own funds and capital adequacy indicator, introduced from July 1, 2012.

At the same time, the deceleration in growth rate of the banks' raised funds, which increased only by 0.8% in August, served as the main reason for the slowdown of aggregate assets growth.

The aggregate profit of the banking sector in August amounted to Rb 83bn, which corresponds to the return on assets at the level of 2.3% and return on equity at 20.3% in annual terms. Therefore, financial performance of banking sector remains quite stable in 2012. Since the year beginning, the return on assets (ROA) amounted to 20.4%, and return on equity (ROE) made 20.5%.

### Raised funds

*Funds in accounts and deposits of individuals* have resumed their growth. In August, they increased by 1.2%, while the annual growth rate increased over this month from 17.2 to 18.2%. Within the summer months, the total increase of deposits was even larger than last year – 4.0% (or Rb 503bn) vs. 3.8% (or Rb 396bn) for the same period in 2011. Thus, the July downfall in savings of individuals was fully compensated.

In regard to disposable income, savings rate with the bank accounts and deposits recorded in summer 2012 (5.7%) was also slightly higher than in the previous year (4.9%).

August deposit base growth was based on a more rapid growth of the volume of accounts in foreign currencies. If the ruble deposits rose less than by 1%, the deposits in foreign currency in \$ increased by 2.5%.

*The volume of corporate customers' assets* with the banks in August 2012 has reduced by 0.9%. The annual growth rate fell down to 18.9%. Just as in the case of funds in the accounts and deposits of individuals, the growth rate of accounts of enterprises in foreign currency was higher than that of ruble ones. While the volume of ruble accounts and deposits decreased by 1.2%, the value of foreign currency accounts increased by 0.5%.

The overall reduction of funds at the bank accounts of the corporate sector was accompanied by their overflow from current accounts to term deposits. As a result, the ratio between deposits and current accounts has shifted in favor of term deposits even more. As of September 1, their volume was by 21% greater than the value of the current accounts, which was the highest indicator in the total period under review. As back as in early 2011, the volume of assets on deposits amounted to only 80% against that of current accounts. This trend may be an indirect evidence of the economic

<sup>1</sup> Hereinafter growth rates of balance sheet are already adjusted for exchange rate revaluation of foreign currency component, unless otherwise indicated.

activity slowdown – assets not involved in the current economic turnover are withdrawn to term deposits.

In August, banks have sharply reduced fund raising from external capital markets. After two months of growth by 4–5% (\$7–8bn) per month, in August foreign liabilities of the banks increased by 0.3% (i.e., less than by \$0.5bn). However, state-owned banks continued their activity in the Eurobonds market. Sberbank, VTB and Rosselhozbank made five placements for the total amount exceeding \$5bn. The overall low growth of foreign loans is probably associated with the recovery of previously borrowed loans.

Table 1

## STRUCTURE OF THE RUSSIAN BANKING SYSTEM LIABILITIES (END OF MONTH), AS % OF TOTAL

	12.07	12.08	12.09	12.10	06.11	12.11	01.12	04.12	05.12	06.12	07.12	08.12
Liabilities, Rb bn	20125	28022	29430	33805	35237	41628	41150	42151	43225	44266	45090	45523
Own assets	15.3	14.1	19.3	18.7	18.5	16.9	17.3	17.3	17.0	16.8	16.8	16.9
Loans of the Bank of Russia	0.2	12.0	4.8	1.0	0.9	2.9	3.3	4.4	3.9	5.1	5.7	5.3
Interbank operations	4.1	4.4	4.8	5.5	5.2	5.7	5.7	4.9	4.7	4.8	4.8	5.0
Foreign liabilities	18.1	16.4	12.1	11.8	10.9	11.1	10.6	10.4	11.0	11.3	11.4	11.4
Private deposits	26.2	21.5	25.9	29.6	30.4	29.1	28.7	29.6	29.4	29.4	28.8	28.9
Corporate deposits	25.8	23.6	25.9	25.7	24.3	26.0	25.9	24.8	24.9	24.0	23.5	23.1
Deposits and balances of state agencies and local authorities	1.5	1.0	1.0	1.5	3.5	2.3	1.8	1.4	1.7	1.5	1.7	2.3
Securities issued	5.8	4.1	4.1	4.0	4.0	3.7	3.8	4.6	4.6	4.5	4.5	4.6

Source: Central Bank of Russia, IEP estimates.

### Investments

Credit debt of individuals to the banks increased in August 2012 by 3.5%, which has kept the annual growth rate of retail loan portfolio of banks at the level of 42%. Bank lending remains a significant factor supporting the volume of retail turnover. Since the beginning of the year the volume of loans to individuals amounted to about 25% of final consumption of households, which has reached 27-28% in summer months.

Key indicators of corporate loan portfolio quality did not change in August. The share of overdue debt loans remained at the same level of 4.6%, and the ratio of provisions for tentative losses on loans provided to individuals at 6.4%.

The volume of lending to corporate borrowers has increased by 2.0% over the month. Annual growth rate of lending to businesses and organizations remains at around 20%. Herewith, the growth in loan debt in the corporate sector of the market is comparable to the retail sector. Since the beginning of the year, the companies' debt to banks increased by Rb 1.7 trillion, whereas that of individuals – by Rb 1.5 trillion.

There were also no significant changes in the quality of loans to corporate borrowers in August. The share of overdue debt remained unchanged at the level of 4.9%. The ratio of tentative losses provisions to the value of loans has slightly decreased from 7.9 to 7.8%. Thus, the quality of loans to businesses and organizations remains worse than the quality of loans to individuals.

#### Liquidity and state support

The value of banks' debt to the RF Central Bank and the Russian Ministry of Finance in August continued its growth. On the one hand, banks have reduced the amount of liabilities to the Bank of Russia by Rb 174bn. However, as a compensation, they have attracted additional Rb 280bn of deposits with the Russian Ministry of Finance. Thus, the total volume of state support to the banks has increased by more than Rb 100bn.

In addition, banks managed again to extend the maturity of loans with monetary authorities. The debts to the Bank of Russia have been decreased in volume primarily in regard to one-day repo operations, while the loans for the term over 90 days have increased. The majority of the Russian Ministry of Finance deposits was placed in the banks in August with maturity of 91 days, that is,

they are to be returned in December, when liquidity problems are usually resolved through the budget expenditures growth.

Thus, banks are demonstrating a greater demand for short-term (up to one month) loans from the monetary authorities, rather than for the long-term resources, which is an evidence of the systematic tendency of growth of the state support to the banking system.

The volume of the banking sector liquidity has somewhat declined in August: the share of liquid assets decreased from 4.85% to 4.6%.

Table 2

## STRUCTURE OF THE RUSSIAN BANKING SYSTEM ASSETS (END OF MONTH), AS% OF TOTAL

	12.07	12.08	12.09	12.10	06.11	12.11	03.12	04.12	05.12	06.12	07.12	08.12
Assets, Rb bn	20125	28022	29430	33805	35237	41628	41533	42151	43225	44266	45090	45523
Cash and precious metals	2.5	3.0	2.7	2.7	2.2	2.9	2.4	2.5	2.4	2.5	2.5	2.5
Deposits with the Bank of Russia	6.9	7.5	6.9	7.1	4.5	4.2	3.2	2.6	2.6	3.0	3.2	2.9
Interbank operations	5.4	5.2	5.4	6.5	6.4	6.4	6.2	6.0	5.7	5.8	5.7	5.9
Foreign assets	9.8	13.8	14.1	13.4	13.8	14.3	14.2	14.3	14.6	14.2	14.5	14.0
Individuals	16.1	15.5	13.1	13.0	14.0	14.4	15.3	15.6	15.8	16.0	16.1	16.5
Corporate sector	47.2	44.5	44.5	43.6	45.3	44.0	44.4	44.6	44.1	43.6	42.7	43.7
Government	4.1	2.0	4.2	5.1	5.8	5.0	4.9	4.1	4.5	3.8	3.4	3.4
Property	2.2	1.9	2.7	2.6	2.5	2.3	2.4	2.4	2.3	2.3	2.3	2.3

Source: Central Bank of Russia, IEP estimates.

## REAL ESTATE IN THE RUSSIAN FEDERATION

G.Zadonsky

In July 2012, entities of all the forms of ownership built 52,600 new apartments with the total floorspace of 4.21m sq. meters which is 13.8% more than in July 2011. In the 2<sup>nd</sup> quarter of 2012, the ratio between the price of a sq. meter of housing on the primary market and the cost of building of a sq. meter of housing amounted to 147.42% against 138.9% in the 1<sup>st</sup> quarter of 2012. The growth in the outstanding debt on MHL in rubles continued, and as of August 1, 2012 it amounted to Rb 1,572,685bn which is 41.28% more than in August 1, 2011. As regards loans in foreign currency, as of August 1, 2012 the debt on MHL amounted to Rb 137,728bn which is 11.7% less than that as of August 1, 2011.

According to the Rosstat's data, in the first six months of 2012 entities of all the forms of ownership built 242,800 apartments with the total floorspace of 21.04m sq. meters which figure was equal to 101.9% on the respective period of last year. Individual developers built 11.1m sq. meters of housing or 53% of the total volume of housing commissioned in the first six months of 2012.

In July 2012, entities of all the forms of ownership built 52,600 new apartments with the total floorspace of 4,21m sq. meters which is 13.8% more than in July 2011, while in January–July, 295,400 apartments with the total floorspace of 25.25m sq. meters which is 3.5% more than in the respective period of 2011.

In the first six months of 2012 and 2011, the largest volume of housing per thousand persons (347.9 sq. meters) was commissioned in Krasnodar Territory (*Table 1*). Among federal districts, as in the first six months of 2011 the highest result (221.0 sq. meters per thousand persons) was registered with the Southern Federal District, while the lowest one (85.2 sq. meters per thousand persons), with the Far East Federal District (*Table 1*). As regards that index, Moscow was downgraded to the 85<sup>th</sup> place. As regards the volume of housing commissioned by individual developers per thousand persons of the population, the top three leaders have consistently been the Belgorod Region, the Lipetsk Region and the Tambov Region.

Table 1

DISTRIBUTION OF THE REGIONS OF THE RUSSIAN FEDERATION AS REGARDS THE VOLUME OF HOUSING COMMISSIONED IN JANUARY–JUNE 2012 PER THOUSAND PERSONS OF THE POPULATION

Region	Total housing commissioned		Housing commissioned by individual developers	
	% of H1 2011	Sq. meters per thousand persons	% of H1 2011	Sq. meters per thousand persons
The Russian Federation	101,9	147,1	106,1	77,9
Krasnodar Territory	113.3	347.9	97.8	157.0
Tyumen Region	111.5	302.1	69.3	64.8
Belgorod Region	131.1	301.5	122.8	249.1
Republic of Tatarstan	93.6	288.2	103.6	132.3
Moscow Region	113.0	279.3	94.4	148.2
Republic of Altai	145.2	247.1	88.3	146.3
Leningrad Region	112.1	235.5	122.3	141.4
Lipetsk Region	110.2	232.0	146.0	204.7
Including Nenetsk Autonomous Region	128.0	228.6	227.2	122.5
Kaliningrad Region	101.3	227.8	119.7	62.6
Republic of Chuvashia	105.1	219.2	102.4	171.6
Republic of Bashkortostan	109.4	210.4	108.1	163.6

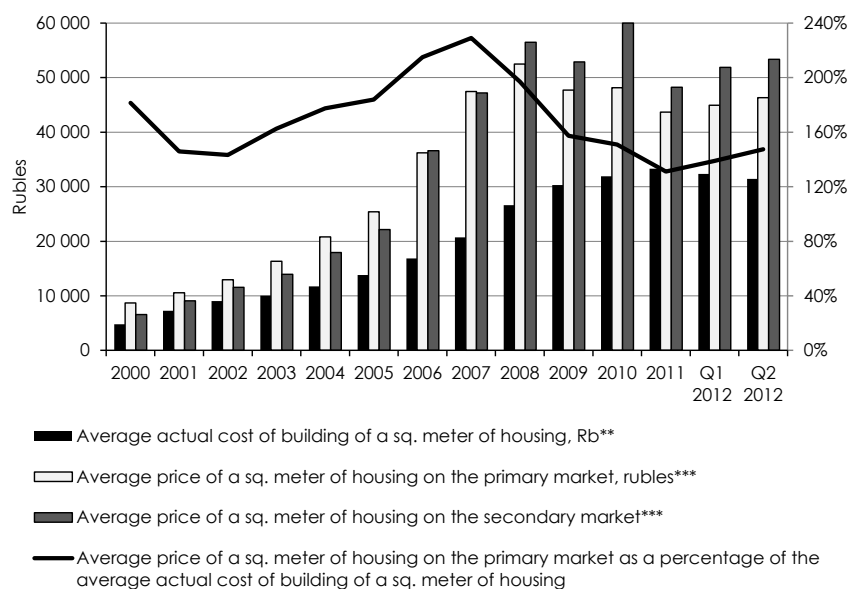
Table 1, cont'd

Region	Total housing commissioned		Housing commissioned by individual developers	
	% of H1 2011	Sq. meters per thousand persons	% of H1 2011	Sq. meters per thousand persons
Republic of Mariy El	106.0	207.0	102.9	137.2
Ulyanov Region	129.0	202.2	140.7	164.7
Tambov Region	106.9	197.2	145.4	174.0
City of St. Petersburg	62.1	109.3	117.8	8.1
City of Moscow	66.4	53.9	34.8	0.4
Southern Federal District	107.7	221.0	97.6	125.4
Ural Federal District	110.8	169.5	85.3	55.6
Privolzhsky Federal District	98.9	161.4	106.9	104.5
North Caucasian Federal District	131.8	141.6	123.4	81.7
Central Federal District	102.8	139.3	112.0	74.7
North Western Federal District	86.6	118.5	118.0	43.2
Siberian Federal District	89.3	114.6	102.0	57.0
Far East Federal District	113.5	85.2	122.9	44.1

Source: on the basis of the data of Rosstat.

According to the data of Rosstat, in the 2<sup>nd</sup> quarter 2012 the average actual cost of building of a sq. meter of housing fell by 2,86% on the 1<sup>st</sup> quarter of 2012 and amounted to Rb 31,441 (Fig. 2). In the first six months of 2012, the average actual cost of building of a sq. meter of housing amounted to Rb 31,870 (Fig. 2) having decreased by 0.81% as compared to the first six months of 2011. In the first six months of 2012, the highest cost of building which exceeded by 50% and more the national average level was registered with the Khabarovsk Territory (Rb 50,557), the Chechen Republic (Rb 49,580) and the Sakhalin Region (Rb 48,265). In 51 constituent entities of the Russian Federation that cost is lower than Russia's average with the lowest one registered in the Republic of Adygeya (Rb 17,493), the Republic of Dagestan (Rb 19,213) and the Ivanovo Region (Rb 20,840).

In the 2<sup>nd</sup> quarter of 2012, the average price of a sq. meter of housing on the primary market (according to the preliminary data – Rb 46,349) increased by 3.1% as compared to the 1<sup>st</sup> quarter of 2012 (Fig. 1) exceeding by 9.83% the average price of a sq. meter of housing in the 2<sup>nd</sup> quarter of 2011. In the 2<sup>nd</sup> quarter of 2012, the average price of a sq. meter of housing amounted to 86.86% of the average price of a sq. me-



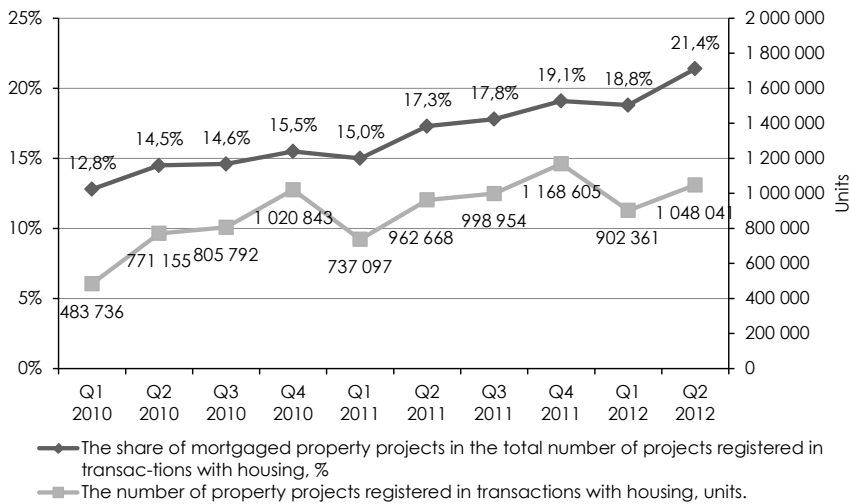
\* Preliminary prices in the 2<sup>nd</sup> quarter of 2012.

\*\* Average actual cost of building of a sq. meter of housing of detached houses (all the apartments) without additional buildings, overstories and built-in premises in the Russian Federation (without those built by people at their own account and by means of borrowed funds).

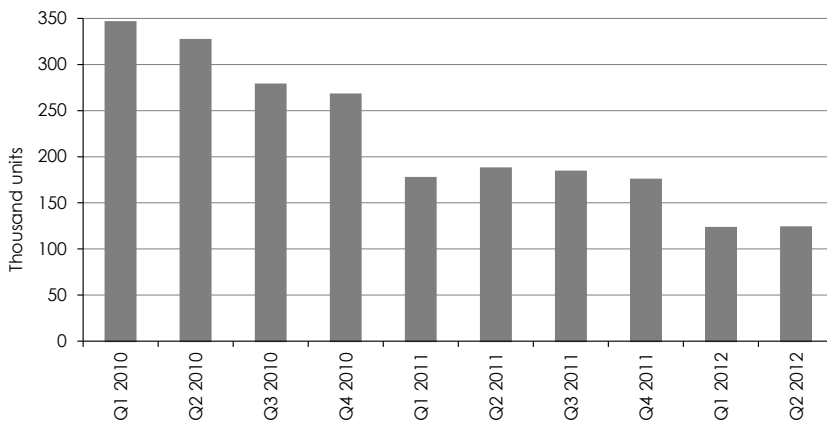
\*\*\* All the apartments.

Source: according to the data of Rosstat.

Fig. 1. Dynamics of the cost of building of housing and housing prices on the primary and secondary markets



Source: OAO AHML on the basis of the Rosreestr's data.  
Fig. 2. Dynamics of transactions with housing



Source: on the basis of the data of the Rosreestr.  
Fig. 3. Dynamics of registration of individuals' titles to land plots in accordance with a simplified procedure

of land plots (37,761 certificates) decreased by 52.24% as compared to the first six months of 2011, while that by legal entities (14,715 certificates), by 5.21%.

As compared to the first six months of 2011, in the first six months of 2012 the number of registered land mortgages for individuals (190,283 certificates) rose by 57.43%, while that for legal entities (62,813 registered certificates), by 8.15%.

According to the Rosreestr, the volume of registration in accordance with a simplified procedure ("summer cottage amnesty") of individuals' titles to land plots provided prior to approval of the Land Code of the Russian Federation for personal subsidiary husbandry, summer house, orcharding, gardening and garage or individual housing building keeps decreasing and in the first six months of 2012 amounted to 246,323 certificates which is 32.44% lower than in the first six months of 2011 (Fig. 3).

According to the data of the Central Bank of the Russian Federation, in January–July 2012 382,571 housing loans (HL) for the total amount of Rb 540.41bn were provided, including 353,252 mortgage housing loans (MHL) for the amount of Rb 516.89bn which exceeded by 55% the monetary volume of MHL extended in January–July 2011. Extended in July 2012 were Rb 86,102m worth of MHL which figure is 48% higher than in July 2011 (Fig. 4) and Rb 1,281m worth of MHL in foreign currency which is 12.32% lower than in July 2011.

In the 2<sup>nd</sup> quarter and July 2012, the outstanding debt on MHL in rubles kept growing and as of August 1, 2012 amounted to Rb 1,572,685bn which is 41.28% more than that as of Au-

ter of housing on the secondary market which figure is 3.57 p.p. lower than that in the 2<sup>nd</sup> quarter of 2011. In the 2<sup>nd</sup> quarter of 2012, the ratio between the price of a sq. meter of housing on the primary housing market and the cost of building of a sq. meter of housing amounted to 147.42% against 138.9% in the 1<sup>st</sup> quarter of 2012 (Fig. 1).

According to the Rosreestr's data provided by OAO AHML (Fig. 2), in the 2<sup>nd</sup> quarter of 2012 the share of mortgaged property projects in the total number of projects registered in transactions with housing increased by 4.1 p.p. on the 2<sup>nd</sup> quarter of 2011 and amounted to 21.4%.

According to the data of the Rosreestr, in the first six months of 2012 the volume of registration of individuals' titles to land plots (2,597,274 certificates) decreased by 3.77% as compared to the first six months of 2011. The number of legal entities' registered titles to land plots rose by 11.82% and in the first six months of 2012 amounted to 135,922 certificates. In the first six months of 2012, leasing by individuals



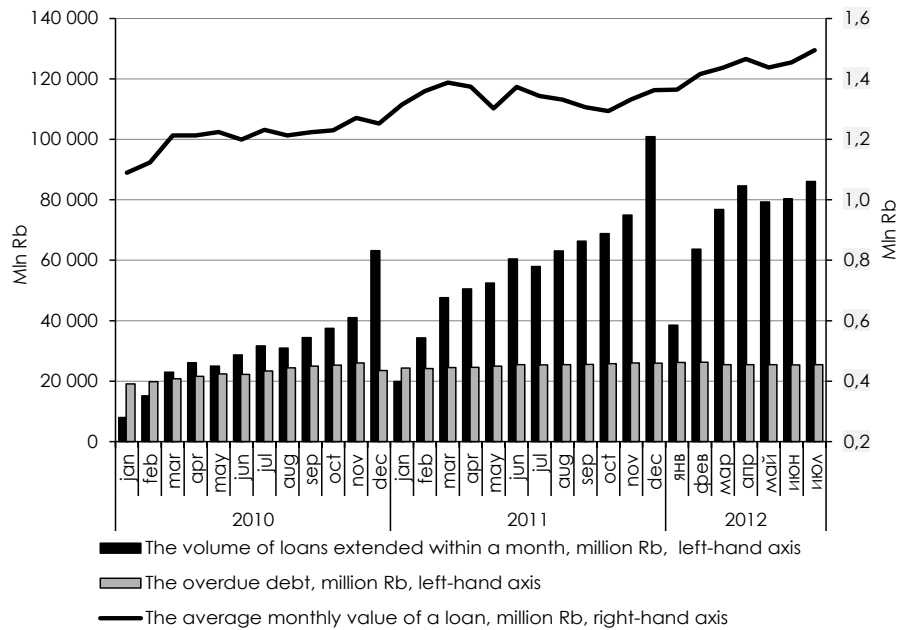
gust 1, 2011. As regards loans in foreign currency, as of August 1, 2012 the debt on MHL amounted to Rb 137,728bn which is 11.7% lower than that as of August 1, 2011.

As of August 1, 2012, the overdue debt on MHL in rubles grew to Rb 25.5bn, while its share in the debt kept falling and as of August 1 amounted to 1.62% which is 0.66 p.p. lower than that as of August 1, 2011 (Fig. 4). As of August 1, 2012, the overdue debt on MHL in foreign currency amounted to Rb 20.1bn or 14.6% of the outstanding debt which figure is 3.45 p.p. higher as compared to that as of August 1, 2011. As compared to the minimum value of October 2011, the average value of MHL in rubles increased by 15.58% and amounted to Rb 1.49m (Fig. 4).

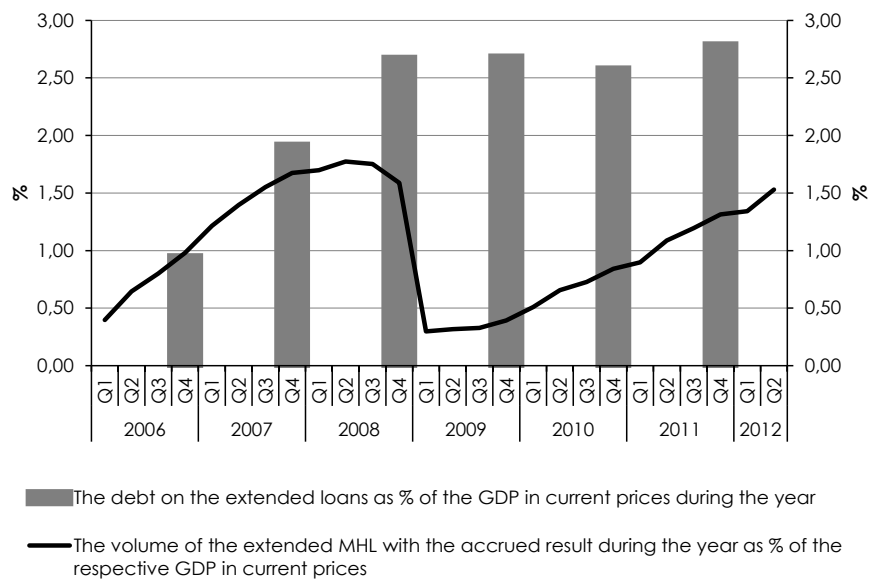
In 2012, the role of MHL in foreign currency in housing lending keeps decreasing. As of August 1, the share of MHL in foreign currency as regards the number of loans, the volume of loans and the debt amounted to 0.27%, 1.47% and 8.05%, respectively. At the same time, the share of the overdue debt on loans in foreign currency in the total outstanding debt remains substantial and exceeds 40%.

In 2011 and the first six months of 2012, the volume of the extended MHL as a share of GDP in current prices kept growing (Fig. 5). However, the volume of MHL extended in the first six months of 2012 (1.53% of GDP) was 0.24 p.p. lower than the maximum value of the first six months of 2008.

According to the data of the Central Bank of the Russian Federation, as of August 1, 2012 the debt on defaulted mortgage housing loans (with an overdue period of over 180 days) amounted to Rb 50,457bn or 2.95% of the total amount of the debt which figure is 0.11 p.p. lower than in the previous month. As of August 1, 2012, the share of debt on MHL without overdue payments increased in money terms, but diminished as a percentage of the total amount of the debt by 0.25 p.p. during the month (Table 2).



Source: on the basis of the data of the Central Bank of the Russian Federation. Fig. 4. Dynamics of mortgage housing loans



Source: on the basis of the data of the Rosstat. Fig. 5. The volume of and the debt on the extended MHL as a share of GDP in current prices

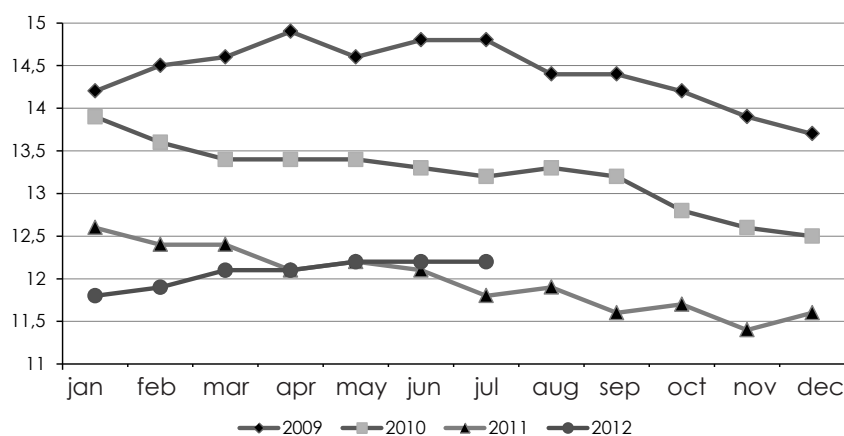
Table 2

## DEBT ON MORTGAGE HOUSING LOANS BY THE PERIOD OF DELAY IN PAYMENTS IN 2012

	The total amount of the debt on MHL	Without overdue payments		With overdue payments					
				from 1 to 30 days		from 31 to 180 days		over 180 days	
		Million Rb.	%*	Million Rb	% *	Million Rb	%*	Million Rb	%*
01.Jan.	1 478 982	1 391 130	94.06	19 079	1.29	14 642	0.99	54 131	3.66
01 Feb	1 477 252	1 377 537	93.25	30 875	2.09	16 102	1.09	52 738	3.57
01Mar	1 499 657	1 398 579	93.26	32 693	2.18	15 147	1.01	53 238	3.55
01.Apr	1 538 270	1 449 359	94.22	21 843	1.42	16 151	1.05	50 917	3.31
01May	1 574 238	1 489 072	94.59	19 993	1.27	14 010	0.89	51 163	3.25
01Jun	1 627 289	1 527 048	93.84	31 569	1.94	13 344	0.82	55 328	3.4
01.Jul	1 672 968	1 581 289	94.52	25 764	1.54	14 722	0.88	51 193	3.06
01.Aug	1 710 413	1 612 407	94.27	33 353	1.95	14 196	0.83	50 457	2.95

\* % of the total amount of the debt.

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



Source: on the basis of the data of the Central Bank of the Russian Federation.

Fig. 6. Average weighted interest rates on MHL in rubles extended within a month

According to the data of the Central Bank of the Russian Federation, as of August 1, 2012, the average weighted rate on MHL in rubles extended within a month remains at the level of 12.2% (Fig. 6), while that on HL in rubles extended within a month fell by 0.1 p.p. and amounted to 12.2%, as well. As of August 1, 2012, the average weighted rate on MHL in foreign currency extended from the beginning of the year came to a halt at the level of 9.6%, while that on HL, at the level of 9.8%.

The average weighted period of lending on MHL in rubles extended within a month increased by 0.2 years during July 2012 and amounted to 15.14 years, while that on HL, decreased by 0.03 years to 14.65 years. As of August 1, 2012, the average weighted period of lending as regards MHL in foreign currency extended from the beginning of the year amounted to 11.95 years, while that as regards HL in foreign currency, to 10.25 years.

According to the results of operations of the leading mortgage banks in the first six months of 2012 (Table 3), Sberbank, Gazprombank and Deltacredit increased by 50% the volume of mortgage loans as compared to the respective period of 2011, while VTB, by 120%. Sberbank and VTB24 account for more than a half of the mortgage market as regards the volume of mortgage loans (58.7%).

Table 3

## OPERATION RESULTS OF THE LEADING MORTGAGE BANKS

H1 2012		2011		H1 2011	
Bank	Volume, million Rb	Bank	Volume, million Rb	Bank	Volume, million Rb
1.Sberbank	192 296	1.Sberbank	320 712	1. Sberbank	129 000
2.VTB24	59 615	2. VTB24	80 382	2. VTB24	27 043
3.Gazprombank	26 736	3. Gazprombank	45 690	3. Gazprombank	16 386

Table 3, cont'd

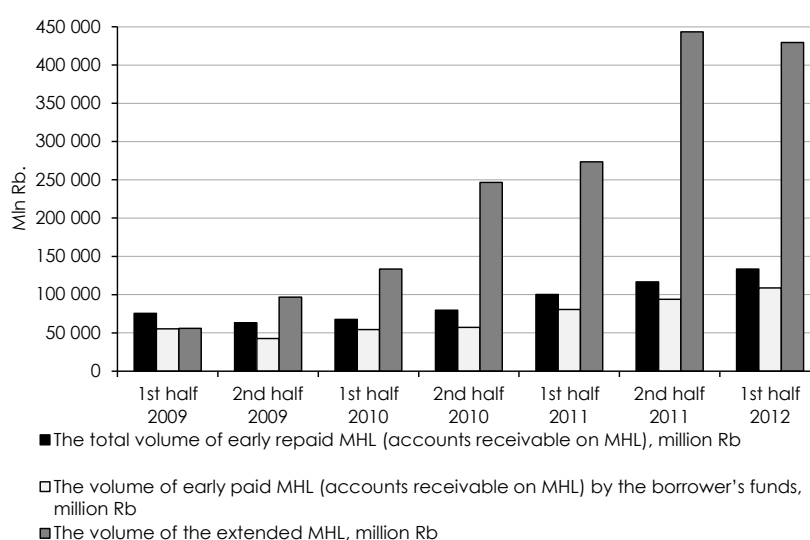
H1 2012		2011		H1 2011	
Bank	Volume, million Rb	Bank	Volume, million Rb	Bank	Volume, million Rb
4.Deltacredit	10 238	4. Deltacredit	18 144	4. Deltacredit	7 157
5.Rosbank	7 288	5. Rosbank	13 084	5. Absolut Bank	4 292
6.Uralsib	7 286	6. Uralsib	9 619	6. Zapsibkombankнк	4 092
7.Svyaz-Bank	5 607	7.Raiffeizenbank	9 612	7. Raiffeizenbank банк	3 933
8.AK Bars	5 496	8. Vozrozhdenie	9 150	8. Vozrozhdeniенe	3 850
9.Vozrozhdenie	5 357	9. Zapsibkombank	8 792	9.BSGV	3 679
10.Zapsibkombank	4 813	10. Absolut Bank	8 581	10.Khanty-Mansiisky Bank	3 375

Source: the data of Rusipoteka

In the 2010–2012 period, the volume of early repaid MHL (accounts receivable on MHL) increased (*Fig. 7*). At the same time, after a decline in the 2009–2010 period the share of early repaid MHL in the volume of the extended MHL is at the level of 30%. In the first six months of 2012, that value amounted to 31.08% having exceeded by 4.82 p.p. the share of H2 2011.

According to the data of the Central Bank of the Russian Federation, in the first six months of 2012 149 credit institutions refinanced MHL for the amount of Rb 30.7bn which is 18.23% more than in the first six months of 2011. In the first six months of 2012, the share of OAO AHML amounted to 85.13%; generally 7.2% of the volume of loans granted was refinanced.

In the letter to the Ministry of Finance of the Russian Federation, the Central Bank of the Russian Federation formulated its position as regards establishment of a single regulator of the banking and financial markets by means of assignment to the Central Bank of the Russian Federation of a function of the Federal Financial Markets Service (FFMS). ●



Source: on the basis of the data of the Central Bank of the Russian Federation.  
 Fig. 7. Dynamics of the volume of provision and early repayment of MHL (accounts receivable)

## THE OIL AND GAS SECTION

Yu.Bobylev

Since the beginning of 2012, the situation in the oil and gas sector has been characterized by the persistence of high global oil and natural gas prices. According to preliminary estimates, the average price of Brent crude oil in January–September 2012 amounted to \$ 112.4 per barrel, which translated into high profits of Russian oil and gas companies and considerable revenues of the state budget. Oil production and petroleum products exports have significantly increased. Russia's authorities are planning to introduce additional tax measures designed to stimulate the development of new oil fields. At the same time, the tax burden on the gas sector is expected to be increased in order to enhance the capture of natural gas rent and to augment the revenues of the state budget.

In 2012, the situation on the global oil market so far has been characterized by the persistence of high oil prices. According to preliminary estimates, the average price of Brent crude oil in January–September 2012 amounted to \$ 112.4 per barrel, which exceeded last year's average (*Table 1, Fig. 1*).

In the European market, prices for Russian natural gas were also impressively high, well in excess of their last year's level. At the same time, they experienced a downward influence of the changing situation in the European natural gas market, caused by a considerable increase in natural gas supplies from other producers and a lower level of natural gas spot prices in comparison with prices for long-term contracts where the price of natural gas is pegged to petroleum product prices.

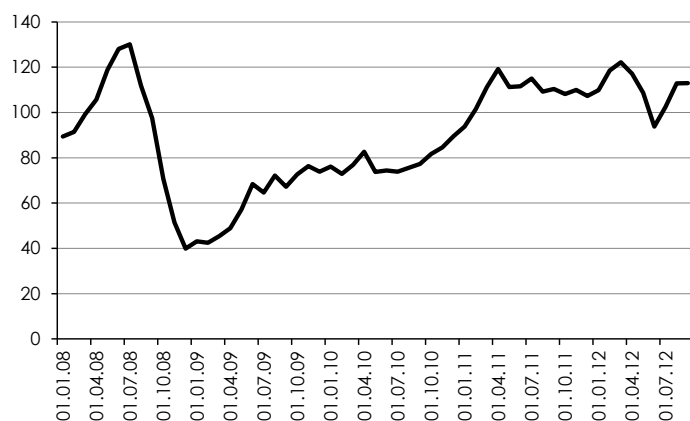
Table 1

INTERNATIONAL PRICES OF OIL AND NATURAL GAS IN 2008–2012

	2008	2009	2010	2011	1Q 2012	2Q 2012	2012 July	2012 August	2012 September*
Price of Brent (UK), USD/barrel	97.7	61.9	79.6	111.0	118.5	108.9	103.1	113.3	113.1
Price of Urals (Russia), USD/barrel	94.5	61.0	78.3	109.1	116.9	106.5	102.5	112.9	112.0
Price of Russian gas on the European market, USD/1,000 m <sup>3</sup>	473.0	318.8	296.0	381.5	444.7	452.4	409.7	410.4	н/д

\* Preliminary estimate.

Source: IMF, OECD/IEA.



Source: OECD/IEA.

Fig. 1. Price of Urals Crude Oil in 2008–2012, USD/barrel

Against this background, oil production continued its upward trend. In January–August 2012, oil production rose by 1.0% on the corresponding period of 2011 (*Table 2*). Among other things, crude oil output was pushed up by the beginning of exploitation of several major new oil fields in the north of European Russia and in eastern Siberia and by a number of changes in taxation, designed to reduce the tax burden on the oil sector, to stimulate the efficiency of oil production at the depleted resource base of Russia's traditional oil fields and to give impetus to the development of new oil areas. At the same time, the volume of oil refining continued to grow at a faster rate than that of oil extraction, mainly due to a

substantial rise in RF petroleum product exports. In January–August 2012, Russia’s oil refining efficiency amounted to 71.6% (vs. 71.0% in January–August 2011). Thus, in this respect Russia significantly lags behind the leading industrially developed countries, where oil refining efficiency amounts to 90–95%.

Table 2

PRODUCTION OF OIL, PETROLEUM PRODUCTS AND NATURAL GAS IN 2005–2012,  
AS A PERCENTAGE OF THE PREVIOUS YEAR

	2005	2006	2007	2008	2009	2010	2011	2012 January–August*
Oil, including natural gas condensate	102.2	102.1	102.1	99.3	101.2	102.1	100.8	101.0
Primary crude oil distillation	106.2	105.7	103.8	103.2	99.6	105.5	103.3	104.1
Motor gasoline	104.8	107.4	102.1	101.8	100.5	100.5	102.0	103.4
Diesel fuel	108.5	107.0	103.4	104.1	97.7	104.2	100.3	96.3
Furnace fuel oil	105.8	104.5	105.2	101.9	100.8	108.5	104.6	101.5
Natural gas	100.5	102.4	99.2	101.7	87.9	111.4	102.9	96.4

\* As % of January–August 2011.

Source: RF Federal State Statistics Service.

The year 2012 saw a considerable rise in petroleum product exports: in January–June they grew by 8.5% on the corresponding period of 2011 (*Table 3*). As previously, the largest share of petroleum product exports consisted of fuel oil, which is used in Europe as a raw material for further reprocessing into diesel fuel. In January–July 2012, the share of exports in the total volumes of fuel oil and motor gasoline resources amounted to 59% and 8.6% respectively (in 2011, the share of exports in motor gasoline output was 10.6%). At the same time, petroleum product imports and their share in the coverage of domestic demand significantly declined. In January–July 2012, motor gasoline imports dropped more than twofold, thus reducing their share in the total volume of motor gasoline resources to a mere 0.9%.

Table 3

EXPORT OF OIL, PETROLEUM PRODUCTS AND NATURAL GAS IN 2005–2012,  
AS A PERCENTAGE OF THE PREVIOUS YEAR

	2005	2006	2007	2008	2009	2010	2011	2012 January–June*
Oil, total	98.4	98.0	104.0	94.0	101.8	101.2	97.6	97.5
including: to non-CIS countries	99.1	98.0	104.8	92.6	102.9	106.1	95.7	97.2
Petroleum products, total	117.9	106.3	108.0	105.0	105.3	106.2	98.5	108.5
including: to non-CIS countries	119.1	104.5	107.6	102.0	107.1	109.6	94.6	101.9
Gas, total	103.7	97.6	94.6	101.8	86.2	105.6	104.0	90.4

\* As % of January–June 2011.

Source: RF Federal State Statistics Service.

Against the background of high global oil and natural gas prices, in January–July 2012 the share of fuel and energy products in Russian exports amounted to 71.0%, including crude oil exports – to 35% (*Table 4*). In Russia, the domestic pricing of crude oil and petroleum products is directly linked to their international prices in accordance with the equal profitability principle for their sales on the domestic and foreign markets. This means that the prices of crude oil and petroleum products are set as netback prices, equal to the international price of a product less the amount of export customs duty and export freight costs. In this connection, the behavior of producer prices for crude oil and petroleum products reflects the behavior of their international prices (*Table 5, Fig. 2*). As regards Russian domestic natural gas prices, they are still subject to state regulation. Over the course of the current year, domestic natural gas prices have significantly increased in response to

their latest adjustments within the framework of price indexation designed to eventually equalize the profitability of Russian natural gas sales on the domestic and foreign markets.

Table 4

## VALUE OF PETROLEUM PRODUCT EXPORTS AND THEIR SHARE IN THE TOTAL VOLUME OF RUSSIAN EXPORTS IN 2005–2012

	2005		2010		2011		2012 January–July	
	bn USD	%*	bn USD	%*	bn USD	%*	bn USD	%*
Fuel and energy products, total	154.7	64.1	267.7	67.5	357.2	69.2	214.6	71.0
including: crude oil	83.8	34.7	134.6	34.0	179.1	34.7	105.8	35.0
natural gas	31.4	13.0	47.6	12.0	63.8	12.4	36.9	12.2

\* As % of the total volume of Russian exports.

Source: RF Federal State Statistics Service.

Table 5

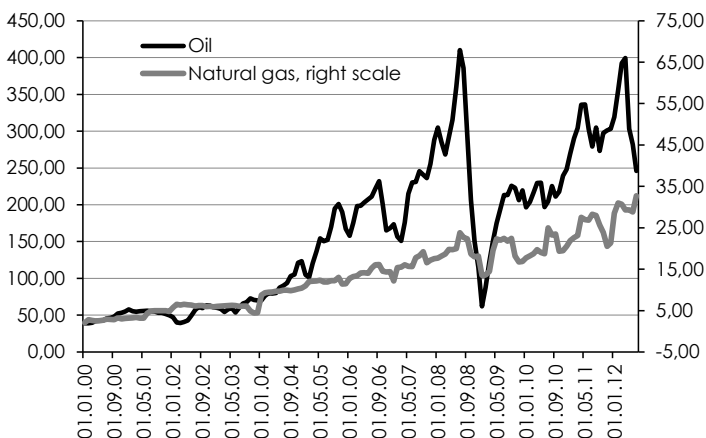
## DOMESTIC PRICES OF OIL, PETROLEUM PRODUCTS AND NATURAL GAS EXPRESSED IN USD IN 2005–2012 (AVERAGE PRODUCER PRICES, USD/TON)

	2005 December	2006 December	2007 December	2008 December	2009 December
Oil	167.2	168.4	288.2	114.9	219.3
Motor gasoline	318.2	416.5	581.2	305.1	457.4
Diesel fuel	417.0	426.1	692.5	346.5	394.8
Furnace fuel oil	142.7	148.8	276.5	125.0	250.8
Natural gas, USD/1,000 m <sup>3</sup>	11.5	14.4	17.6	18.1	16.9

	2010 December	2011 December	2012 January	2012 June	2012 July	2012 August
Oil	248.2	303.3	319.3	281.8	245.9	313.1
Motor gasoline	547.9	576.9	544.4	542.3	565.0	591.8
Diesel fuel	536.1	644.9	674.9	597.1	625.9	674.2
Furnace fuel oil	246.3	274.6	300.2	276.8	286.0	307.6
Natural gas, USD/1,000 m <sup>3</sup>	20.5	21.3	28.5	28.8	32.7	32.6

Source: based on data published by the RF Federal State Statistics Service.



Source: based on data published by the RF Federal State Statistics Service.

Fig. 2. Mean Producer Prices of Oil and Natural Gas, Expressed in US Dollars, in 2000–2012, in USD per Ton and USD per Thousand Cubic Meters

A positive influence on Russia's oil sector was also produced by a number of alterations in the system of taxation. In recent years, in order to stimulate the development of untapped basin provinces, Russia established tax holidays with regard to Mineral Resources Extraction Tax (MRET). From the beginning of 2012 onwards, the MRET tax holidays regime is established for the new oil fields situated in Yamalo-Nenets Autonomous Okrug north of 65°N and for the oil fields in the Back Sea and the Sea of Okhotsk. In order to create incentives for developing small oil fields with initial producible oil reserves of up to 5m tons, Russia's fiscal authorities have introduced a downward coefficient to be applied to the rate of MRET levied on oil extraction, which specifies the size of oil reserves in a given oil field.

In the nearest future, Russia is expected to adopt the following additional measures designed to stimulate oil production: to extend the MRET tax holidays for new oil fields in eastern Siberia from 2017 to 2022; to reduce the rate of export duty on oil from new oil field in eastern Siberia, Yamalo-Nenets AO and Nenets AO; and to introduce reduced MRET rates for 'hard to recover' fields.

At the same time, Russia is planning to increase the tax burden on the gas sector by raising the rate of MRET on natural gas. The proposals to that effect prepared in September 2012 by the RF Ministry of Finance are presented in Table 6. According to the proposals, independent natural gas producers should be entitled to the following downward coefficients to the MRET rate on natural gas production: 0.646 in 2013; 0.673 in 2014; and 0.701 from 2015 onwards.

Table 6

MRET RATE FOR NATURAL GAS IN 2010–2015, RB/1,000 M<sup>3</sup>

	2010	2011	2012	2013	2014	2015
MRET established rate for natural gas extraction	147	237	509	582	622	
Rate suggested by RF Ministry of Finance, September 2012				602	700	788

Source: RF Tax Code (2010–2012 wording); RF Ministry of Finance.

In conditions of the expected rise in domestic natural gas prices, such an increase in the MRET rate should enhance the capture of natural gas rent and to substantially augment the revenues of the state budget. ●

**MIGRATION PROCESS<sup>1</sup>**

L.Karachurina, NRU HSE

*In early July 2012, the RF President signed Russia's State Migration Policy Concept. Two months later, the RF Government considered a draft plan of measures aimed at implementing that concept. The plan sets timelines for the new laws on migration designed to implement the Concept to be presented for consideration – 2012 and 2013. It should be noted that the plan spells out only the timelines for presenting the laws to the RF Government and the State Duma, and not the timeline for their adoption. Bearing in mind that sometimes it takes years for a bill to pass through the State Duma, and taking into account the Russian penchant for emergency changes to law enforcement (for example, in time of crisis), the actual implementation of the Concept may either be indefinitely postponed or even fail to materialize.*

The current State Migration Policy Concept is the second concept elaborated in order to deal with migration issues in Russia's contemporary history. Its predecessor, "The Concept of Regulation of Migration Processes in the Russian Federation" dating back to 2003, mostly remained on paper because, firstly, "the severity of the Russian laws is mitigated by the arbitrariness of their application", and secondly, due to the evident impracticability of some major points of that analytically ill-conceived document.

In the entry under the heading "Conditions for the Formation and Implementation of State Migration Policy", the new Concept honestly and shamefacedly enumerates all the challenges faced by contemporary migration processes in Russia. Thus, the Concept acknowledges Russia's low attractiveness as a destination for permanent migration from other countries, except the CIS member states, and the fact that the presence of 3 to 5 million illegal labor migrants is beneficial to the shadow sector of the Russian economy. Also, the Concept positively characterizes the experience of the countries pursuing active migration policies, which has indicated that migration processes accelerate socio-economic development and improve the welfare of the population. The very fact that these acknowledgements are included in an official state document makes it look realistic (at least in part) and originally based on actual data.

However, the Concept's main section under the heading "The Goals, Principles, Tasks and Main Directions of the State Migration Policy of the Russian Federation" leaves an impression of vagueness, probably reflecting the months-long struggle between the RF Federal Migration Service and the RF Ministry of Healthcare and Social Development. In particular, these two government bodies clashed over the proposals that, from 2015 onwards, the quotas for labor migrants should be abolished, and temporary residential permits cancelled. As a result, these proposals of the RF Federal Migration Service were not approved. The adopted innovations include the development of differentiated mechanisms for the attraction, selection and employment of migrants, including through special programs of long-term and short-term labor migration; the creation of a points-based migrant selection system; a simplification of entry and exit procedures for some categories of migrants – for example, for migrants taking part in investment and entrepreneurial activities, etc. As regards the most corruption-prone mechanisms for quota-setting and the issuance of temporary residential permits, the Concept goes only as far as to suggest that they should be "modernized" and "improved".

However, some questions remain unanswered not only due to the vagueness of some of the Concept's major points. Bureaucratic "mechanisms" and law enforcement are capable of rendering worthless even the most precise and effective document. The State Migration Policy Concept was signed by the RF President in early July 2012, and two months later the RF Government considered a draft plan of measures aimed at implementing this concept. The plan sets the timeline for the new laws on migration designed to implement the Concept to be presented for consideration –

<sup>1</sup> The next issue of 'Migration Processes' will include materials based on labor migration statistics.



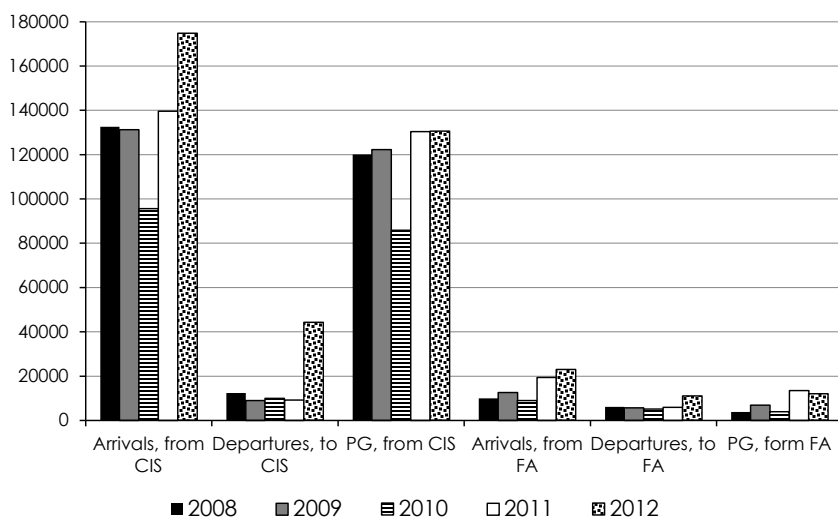
2012 and 2013. It should be noted that the plan spells out only the timeline for presenting the laws to the RF Government and the State Duma, and not the timeline for their adoption. Considering the fact that sometimes it takes years for a bill to pass through the State Duma, and also that emergency changes are often made to law enforcement at a later date (for example, in response to a crisis), the implementation of the Concept can either be indefinitely postponed or ultimately fail to materialize.

One of the examples of this eternal penchant for innovations is the incessantly changing procedure for keeping statistical records of migrants. The latest change of that kind took place in 2011. In accordance with this innovation, the statistical registration of long-term migration (one of the main participants in natural population loss replacement) should include migrants registered at the place of residence and persons registered at the place of stay for a period of 9 months or more (previously, these statistics included migrants registered at the place of residence and persons registered at the place of stay for a period of more than 12 months). The methodological differences between the two approaches can apparently be explained by the fact that during the period of 90 days (the three-month period that represents the difference between 9 months and one year) migrants are allowed to stay without registration at their place of dwelling<sup>1</sup>. As a result, the duration of their stay amounts to one year, which corresponds to the international recommendations concerning long-term migrants' statistical registration. On the one hand, the logic of these changes is based entirely on mercantile considerations: the authorities have found a method for demonstrating that Russia's population is either not declining at all, or is declining very slightly (it should be reminded that still earlier, the category of migrants shaping Russia's net migration exclusively included migrants registered at the place of residence, while migrants registered at the place of stay for any period of time did not count in net migration statistics). On the other hand, any rise in the official net migration figure definitely brings it closer to the actual figure approximated by researchers.

*Fig. 1* shows the impact of the recent changes in the statistical registration of migrants on the statistically registered parameters of migrant flows. Firstly, almost all indicators sharply rose in 2011, when the procedure for statistical registration of migrants was altered. This rise was especially pronounced with regard to the internal migration trend and the number of arrivals from far-abroad countries. This is yet another confirmation of the opinion that migration without changing the officially registered place of residence is really an important factor of economic life in Russia. This indicator continued to grow in the first half of 2012. Its net growth over the first months of 2012 by comparison with the corresponding period of 2011 was almost twofold. If this upward trend continues through the rest of the current year, the number of internal migrants in Russia, for the first time since 1992, will exceed 3m. However, it should be noted that the 3.2m migrants recorded in 1992 did not include the migrants who changed their place of stay, for this category of migrants simply did not exist "officially" at the time. This also explains the significant differences in the number of population reflected in current population estimates and in the 2002 and 2010 population censuses. These censuses established that the population of a number of Siberian and Far-Eastern region was notably less numerous than that reflected in current population estimates. The demographic situation in the central regions of European Russia was diametrically opposite<sup>2</sup>. Firstly, the net immigration numbers, which the authorities had been eager to increase by changing the rules of statistical migrant registration, did not respond as expected. The net immigration numbers grew considerably on the crisis year 2010, but only slightly on 2008 and 2009. The root cause of this sluggish growth in net immigration numbers was a sharp increase in departures from Russia, including to "far-abroad" countries, and especially to CIS countries. Previously, when only really "permanent" migration was taken into account, the number of departures from Russia to other states was negligible. When the official notion of migration was extended to persons changing the place of stay, the number of departures from

1 However, no changes were introduced to Federal Law of 16 July 2006, No 109-FZ, "On the Statistical Migrant Registration of Foreign Nationals and Stateless Persons in the Russian Federation".

2 For more details, see N. V. Mkrtychyan, *Migratsiia kak component dinamiki naseleniia regionov Rossii: otsenka na osnove dannykh perepisi naseleniia 2010 goda* [Migration as a component of the population dynamics of Russia's regions: an estimate based on the 2010 Population Census // *Izvestiia RAN. Seriiia geographicheskaiia* [News of the Russian Academy of Sciences. Geography Series]. 2011, No 5. Pp. 28–41.



Note: FA – far-abroad countries. Apart from the countries traditionally classified as far-abroad ones, this category now includes Georgia and the Baltic States. PG – population growth linked to migration.

Fig. 1. General Parameters of Migration Flows Between Russia and CIS Countries and Between Russia and Far-Aboard Countries (FA) in the First Half-Year of 2008-2012

to 25% of illegal migrants are persons who have been staying in the territory of Russia for a long time and are intending to remain in Russia permanently.

Owing to the newly-established procedure for statistical registration of migrants, Russia's migration-linked population growth has not only compensated for natural population loss (in the first half-year of 2012 it amounted to 57 thousand persons vs. almost 139 thousand persons in the corresponding period of 2011), but has exceeded it by almost 2.5%. In the first few months of 2012, Russia's natural population loss was at its lowest since 2000, which makes it possible to assume that even if the statistical registration procedure had not been changed, the migration-linked population growth would have been strong enough to compensate for natural population loss.

For the first time in many years, Russia showed some migration-linked population growth not only in her migrant exchange with CIS countries but also with far-abroad countries (which now also include the Baltic States and Georgia). For example, Russia registered a migration surplus vis-à-vis her major emigration partners of the 1990s and 2000s, Germany and Israel. Migrants from China, Georgia and the Baltic States accounted for 13%, 29% and 10% of Russia's population growth linked to migration from far-abroad countries, respectively. Russia had a negative migration balance only with Canada, the USA and Finland. However, this negative migration balance as registered by Russian statistics agencies is so small, and the current trends in this respect are so promising, that it is reasonable to expect that as early as the second half of 2012, or in the course of next year, the traditionally negative migration balance with these countries will be replaced by a positive one. Although, by all appearances, these developments seem to favor the hypothesis that Russia's migration attractiveness is increasing, even the new Concept states something directly opposite to that optimistic point of view. But, most importantly, the lack of serious progress in eliminating the defects of Russia's migrant exchange with many of the far-abroad countries is also testified to by the migration statistics of European countries. Some of these statistics may be summarized as follows: "[...] in 2009, net migration from Russia to Germany amounted to 3 thousand persons, including 1 thousand Russian Germans and

Russia to CIS countries in the first half of 2012 soared almost fivefold on the corresponding period of 2011. The above statistics bear witness to the fact that Russia's net migration now includes a "short-term" component, and that natural population loss is partly compensated for by migrants coming into Russia for the purpose of permanent residence (although the amount of this compensation definitely does not match official statistics). Quite another matter is illegal migration, whose numbers can be estimated only approximately (the Concept puts the number of illegal migrants in Russia at 3 to 5 million). According to recent surveys<sup>1</sup>, 20

1 The surveys carried out by the Center for Migration Studies within the framework of the following projects: Migration Management in Conditions of Demographic Crisis (2007-2010 funded by the McArthur Foundation, Head of Project Zh. A. Zaionchkovskaya); and Strategic Partnership in the Promotion of Rights and Enhancing Opportunities for Migrant Women in Russia (2010-2011, funded by the UN Women's Fund for Gender Equality, Head of Project Ye. V. Tiurukanova).

2 thousand other migrants. In contrast to Russian statistics, German statistics indicates the continuation of emigration to Germany, however small it might be. According to [public opinion] surveys<sup>1</sup>, Russia's emigration potential to Germany exceeds these figures<sup>2</sup>. Similar conclusions are made concerning Russian emigration to Israel: "The flow of emigrants from Russia to Israel is currently relatively small (2–4 thousand persons per year), which reflects the emigration potential of Russia's [Jewish] community. However, this flow considerably exceeds the Russian estimate of the size of emigration to Israel: 973 persons in 2011"<sup>3</sup>. Emigration from Russia is going on. It is caused by Russia's current political and socio-economic realities. On the other hand, the course of events gives every reason to believe that the population of Russia is rapidly getting involved in globalization processes, including through migration.

The development of the outstanding features of Russia's migrant exchange with CIS countries was perhaps most heavily influenced by the de facto shelving of the procedure for acquisition of Russian citizenship (established in accordance with Russia's international agreements with Kazakhstan, Kyrgyzstan and Belarus<sup>4</sup>). According to the RF Federal Migration Service, the number of persons who obtained Russian citizenship under this procedure in January–August 2012 amounted to 59,600, which represented an impressive (almost one-third) drop on the corresponding period of 2011. In this respect, Russia's 2012 full-year results will, most likely, be even lower than those recorded in the disastrous 2010, when Russian citizenship was acquired by 111,400 persons. At the same time, Russia's positive migration balance with the republics of Central Asia either dropped or stabilized, while her positive migration balance with Belarus and the number of arrivals from that country sharply increased (Fig. 2).

As had been expected, the vanished opportunity for citizens of some CIS countries to obtain Russian citizenship under a simplified procedure resulted in their increasing interest in the moribund state program of assistance to the voluntary resettlement to Russia of compatriots residing abroad. Over the course of the first eight months of 2012, the number of this program's participants and their accompanying family members increased by 1.8 times on January–August 2011 – to 18,200<sup>5</sup>. However, Russia's 2012 full-year results in this field will certainly fall short even of the program's initial target of 50,000 resettled persons, set for 2007. ●

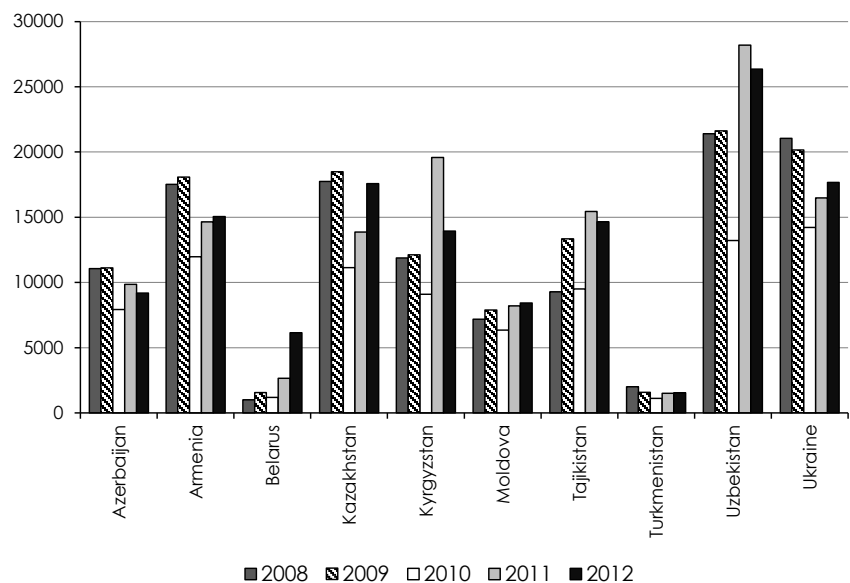


Fig. 2. Russia' Population Growth Linked to Migration from CIS Countries in the First Half-Year of 2008–2012, Number of Persons.

1 VtsIOM Rossiia, *Amerika i Zapadnaia Evropa – gde lutshe zhit', rabotat' i uchit'sia?* [VtsIOM Russia, America and Western Europe – where is it better to live, work and study?] / Press-vypusk [press release] No 1793. 6 July 2011; Levada-Tsentr: *mnogie rossiiane gotovy navegda pokinut' Rodinu* [The Levada-Center: Many Russians are ready to leave their motherland for ever] // Novaia Gazeta [The New Gazette]. 12 July 2011.

2 For more details, see M. B. Denisenko, *Emigratsiia iz Rossii v strany Dal'nego Zarubez'ia* [Emigration from Russia to far-abroad countries] // Demoscope Weekly. 2012. No 513-514. <http://demoscope.ru/weekly/2012/0513/tema05.php>

3 Ibid.

4 For more details, see L. B. Karachurina, *Migration Processes* // Russian Economy in 2011. Trends and Outlooks (Issue 33). Moscow: The Gaidar Institute for Economic Policy, Gaidar Institute Publishers, 2012. Section 5.2. P. 319.

5 Form 1-RD data. This new form of statistical administrative report is being developed by the RF Federal Migration Service.

**REVIEW OF ECONOMIC LEGISLATION<sup>1</sup>**

I.Tolmacheva

*In September, the following amendments were introduced in the legislation: the rules of registration of people for the purpose of a search of an appropriate job and the unemployed, as well as requirements to selection of an appropriate job have been approved; a procedure for public discussion of state purchases for the amount of over Rb 1bn – which procedure is mandatory in placement of orders for federal needs – has been developed; the rate of refinancing of the Central Bank of Russia has been raised.*

**I. Resolutions of the Government of the Russian Federation****1. Resolution No.891 of September 7, 2012 “ON THE PROCEDURE FOR REGISTRATION OF PEOPLE FOR THE PURPOSE OF A SEARCH OF AN APPROPRIATE JOB AND THE UNEMPLOYED AS WELL AS REQUIREMENTS TO SELECTION OF AN APPROPRIATE JOB”**

In accordance with the Law of the Russian Federation on Employment in the Russian Federation, the following documents have been approved:

- The Rules of Registration of People for the Purpose of a Search of an Appropriate Job;
- The Rules of Registration of the Unemployed;
- Requirements to Selection of an Appropriate Job.

In particular, the Rules of Registration of the Unemployed set the procedures for registration, keeping of a register and discarding from registration by the employment service public agencies and determine the list of documents required for registration, the instances of denial in registration to the unemployed registered for the purpose of a search of an appropriate job, as well as instances of discarding from registration of the unemployed.

In search of an appropriate job for the unemployed, the following should be taken into account among other things: experience and job skills, the amount of the average pay in the past three months at the last work place, the specifics and conditions of work, transport accessibility to the work place and the employer’s requirements to a job applicant.

**II. Instructions, Letters and Orders****1. Letter No. AD-P13-4450 of August 2, 2012 of the Government of the Russian Federation.**

The procedure for public discussion of state purchases for the amount of over Rb 1bn – which procedure is mandatory in placement of orders for federal needs – has been developed. In public discussion, any legal entities irregardless of the their form of incorporation and ownership, location and the place of origin of capital, any individuals, including individual entrepreneurs, as well as public authorities and local government bodies may participate on an equal basis. The discussion is to be carried out in the two stages: on the official Internet site meant for placement of information on public purchases and in the form of open public hearings.

All the comments submitted to the Internet site undergo pre-moderation in order to exclude comments with statements which violate generally accepted norms of public discussion (that is, slang words, uncontrolled vocabulary and other) and comments which have nothing to do with the topic of the public discussion. Answers to the comments are to be sent by the customer to their authors by e-mail and published on the Internet site.

The information on the date, time and location of the meeting of the second stage of the discussion and public hearings, as well as the procedure for participation in them, including the information on the access mode are to be published by the customer on the Internet site, as well. Public hearings are open ones; the customer (the authorized body) does not have the right to limit access of interested parties to such a meeting. The customer has to send by e-mail an invitation for participation in open public hearings.

<sup>1</sup> The review was prepared with assistance of the KonsultantPlus legal system.

All the comments and proposals by participants in public hearings, the customer's answers to them, as well as intermediary and final minutes of public hearing are to be published on the official site.

2. Instructions No. 2873-U of September 13, 2012 "ON THE LEVEL OF THE RATE OF REFINANCING OF THE CENTRAL BANK OF RUSSIA"

From September 14, 2012, the rate of refinancing of the Central Bank of Russia is set at the level of 8.25% per annum. The rate of refinancing did not change from December 26, 2011 when it was fixed at the level of 8% per annum. ●

## REVIEW OF THE MEETINGS OF THE GOVERNMENT OF THE RF IN SEPTEMBER 2012

M. Goldin

*In September 2012, at the meetings of the Presidium of the Government of the Russian Federation, the following issues were discussed: determination of the federal executive authority which sets the procedure for calculation of the amount of the fee for participation in tenders (auctions) on utilization of the mineral wealth; such draft amendments to the Tax Code of the Russian Federation as provide for exemption of payment of a sale tax on cultural valuables purchased by means of extra-budgetary funds and brought to the territory of the Russian Federation and other territories within its jurisdiction..*

**On September 5**, at the meeting of the Government of the Russian Federation the draft Federal Law “On Amendment of Article 42 of Law No.2395-1 of February 21, 1992 of the Russian Federation on the Mineral Wealth (hereinafter, the Law on the Mineral Wealth)” was discussed. In Article 42 of the Law on the Mineral Wealth, a fee for participation in a tender (auction) is set. It is to be reminded that a fee for participation in a tender (auction) on securing of the title to utilization of the mineral wealth is to be paid by all the participants and constitutes a condition for a bid to be registered. The bid is considered to be submitted after payment was made by the bidder of a fee for participation in the tender or auction on securing of the title to utilization of sections of mineral wealth and registration.

However, neither the methods of calculation of that fee, nor the person responsible for approval of those methods have been approved so far.

Until recently, the Temporary Guidelines for Determination of the Amount of the Fee for Participation in Tenders (Auctions) on Securing of the Title to Utilization of Sections of the Mineral Wealth approved by Order No.688 of June 17, 2005 of the Federal Agency for Utilization of the Mineral Wealth (hereinafter, Rosnedr) were in effect. However, the above statutory act lost effect from September 1, 2009 as Order No. 791 of August 25, 2009 of Rosnedr “On Cancellation of Orders of the Federal Agency for Utilization of the Mineral Wealth” – Order No. 688 of June 17, 2005 “On Approval of Temporary Guidelines for Determination of the Amount of the Fee for Participation in a Tender (Auction) on Securing of the Title to Utilization of Sections of the Mineral Wealth” and Order No. 729 of June 28, 2005 “On Approval of the Temporary Guidelines for Determination of the Amount of the Fee for Issuing of a License to Utilization of the Mineral Wealth” – was issued.

It is proposed in the draft law to determine that the procedure for calculation of the amount of the fee for participation in tenders (auctions) on securing of the title to utilization of sections of the mineral wealth (except for mineral wealth sections of local importance for exploration and production of generally known minerals or geological research, exploration and production of generally known minerals) is set by the federal authority in charge of management of the mineral wealth (Rosnedr), while as regards mineral wealth sections of local importance granted in utilization for exploration and production of popular minerals, by a public authority of constituent entities of the Russian Federation.

The draft law was approved by the Government of the Russian Federation and submitted to the State Duma of the Russian Federation.

**On September 13**, at the meeting of the Government of the Russian Federation the draft Federal Law “On Amendment of Article 150 of Part 2 of the Tax Code of the Russian Federation” (hereinafter, the draft law) was discussed. By development of the draft law, Item 19 of the Plan of Legislative Activities of the Government of the Russian Federation in 2012 approved by Instructions No. 2425-r of December 28, 2011 of the Government of the Russian Federation is realized.

In accordance with Article 150 (4) of Part 2 of the Tax Code of the Russian Federation, exempted from VAT payment are cultural valuables brought to the territory of the Russian Federation or other territories which are under its jurisdiction and purchased by means of federal budget funds,

budgets of constituent entities of the Russian Federation and local budgets. However, state and municipal entities buy cultural valuables abroad for replenishment of their funds not only by means of budget funds alone, but at the expense of extra-budgetary sources, as well. So, with cultural valuables brought to the territory of the Russian Federation and other territories which are under its jurisdiction and purchased at the expense of funds from extra-budgetary sources, state and municipal entities will have to pay VAT of 18% of the value of such cultural valuables.

It is proposed in the draft law to extend the VAT privilege to cultural valuables which are brought to the territory of the Russian Federation and other territories under its jurisdiction and purchased by state and municipal entities at the expense of extra-budgetary funds.

The above entities will be able to use that privilege after submitting to customs authorities of a statement confirming the fact that the specified condition has been met, and such a confirmation is to be issued by a federal executive authority carrying out functions of development of the state policy and legal regulation in the sphere of culture, art, cultural heritage (including archeological one), cinematography and archiving.

The draft law has been approved by the Government of the Russian Federation and submitted to the State Duma of the Russian Federation. ●

## AN OVERVIEW OF NORMATIVE DOCUMENT ON TAXATION ISSUES IN AUGUST–SEPTEMBER 2012

L.Anisimova

*The overall situation in the area of compulsory payments in August–September continues to reflect uncertainties in the domestic financial policy of Russia. The turbulence of its opponents' positions is high, and it does not seem possible to reach any clear agreement.*

At the meeting of September 18, 2012 the Russian President Vladimir Putin expressed his displeasure with the draft budget, presented by the Russian government, which, in his opinion, makes it impossible to implement the goals set out in the decrees adopted after the inauguration. The following tasks are set forth: development of agreed decisions on the pension system, improvement of living conditions of large families, funding of Siberia and Far East development<sup>1</sup>. The Russian government responded immediately to these comments: on the next day, at a meeting with the RF Prime Minister Dmitry Medvedev, the Head of the RF Ministry of Finance has offered to cover the deficit of the RF Pension Fund (PF) with 95% dividends of Rosneft, the Central Bank proceeds from the sale of Sberbank shares and also increase the effective rate of insurance contributions for self-employed individuals<sup>2</sup>, having raised the tax base from one to three minimum wages (SMIC) for 3 years, and to increase insurance rates on the list of hazardous occupations up to 6–9%. It is clear that even in this case the mobilized additional resources will not cover the trillion deficit of social funds, so the financing of election promises will be finally determined, apparently, closer to the completion of the budget draft. The objective of forming a balanced budget is complicated also by a forced adjustment of MET scheme, implemented by the Ministry of Finance at the last moment under a heavy pressure of OAO “Gazprom”<sup>3</sup>.

In September 2012 the Duma officials and trade union leaders, in turn, made some highly politicized proposals for finding resources for payments to pensioners (message from A.Isayeva, Chairman of the Duma Committee on Social Policy, and M. Shmakov, Chairman of the Independent Trade Unions Federation of (FNPR) to the government on the so-called “Countervauchers”). The issue in question is cancellation of the privatization that happened 20 years ago, withdrawal of dividends from the total budget revenues, and distribution thereof between pensioners (those who lived at that time and still live now after those 20 years) and some other proposals on the sources of pensions funding. Famous Russian market economists have commented on this proposal, explaining that the dividends of privatized mining companies, which are state corporations now, are paid to the federal budget anyway, so the government cannot get any additional revenue to cover the PF deficit. Our position<sup>4</sup> is based on a more detailed study of trends in labor relations and on a

1 “Putin’s promises were not included in the budget. Budget estimates for 2013–2015 will not allow Vladimir Putin to fulfill his election campaign promises”, website gazeta.ru, 18.09.2012.

2 D.Butrin, P.Netreba, O.Sapozhkov, “The budget is not revised, but extended”, website komsomol.ru, 21.12.2012 No. 177 (4962).

3 “National property shall be spared. “Gazprom” has regained from the Ministry of Finance \$6bn of annual tax liabilities on production”, website of “Kommersant » newspaper No. 177 (4962), 09/21/2012.

4 See “Three requests to Putin from Russia. Russian Federation of Independent Trade Unions (FNPR) Head Mikhail Shmakov and the “United Russia” member Andrey Isayev wrote an article for the “Moscow News”, website mn.ru, on 04/09/2012, the “In economists’ opinion, it will be difficult to implement the proposals of Shmakov Isayev”, website lprime.ru 09.05.2012.

Our position on the extensive debate is as follows. It is clear that privatization has split up the society to such extent that even the President was forced to return to this subject in the election campaign. However, an economically healthy society cannot be built at a constant debate on the privatization. It is necessary to look for acceptable solutions in current relationships: people are working now, they need to support their families, they are not interested in businesses to turn bankrupts and discontinue their operations, which is in line with the interests of employers. Perhaps, the best solution in this situation would be participation of representatives or authorized persons of employees in business management bodies. By the way, the FNPR and Duma Committee proposal on social policy in general is in line with our position, presented in previous reviews, although many prominent market economists consider it highly undesirable and believe that its adoption can provoke unnecessary conflicts and reduce production efficiency.



more extensive comparison of the dividends and taxes efficiency as a source of retirement benefits in today's market, because in our opinion, the discussion about the results of privatization needs to be consistently transferred from the artificially maintained political confrontation to the routine framework of economic analysis.

During the period under review, the Ministry of Finance has tightened the requirements to the regional fiscal policy<sup>1</sup>. At a meeting with the regional Governors, the RF Minister of Finance noted that a number of Russian regions pursues inadequate and irresponsible fiscal policy, which is why they have huge debts (now in 20 regions there recorded debts exceeding 50% of tax and non-tax regional revenues, whereas the upper limit of such debts set up by law is 100% of tax and non-tax regional revenue). According to the Minister, it is necessary to increase personal responsibility of governors, if the Subject of the Russian Federation fails to perform its liabilities or exceeds the tax burden as compared with the parameters specified in the Budget Code, including "initiating the process of the governor's dismissal due to the loss of the President's confidence". In turn, the heads of the regions have expressed dissatisfaction with the policy of the federal government, including that of the Ministry of Finance, as in their opinion, the debt is growing as a result of the adoption of the federal government decision to reduce the revenues of regional budgets with a simultaneous extension of spending commitments thereof.

Against this background, and given the tension in the formation of the budgets of various levels, the announced by the Ministry of Finance experts intent on granting tax benefits on the loans

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We will try to explain our position.

Income from dividends even on OAO "Gazprom" shares is unpredictable. Corporate profit tax (20%) is established by the law. The decision on dividends payment and the amount thereof is taken by company management after tax. According to the law, taxes are payable by everybody, but paying high dividends is impractical, because it immediately reduces the total capitalization of the company, as well as the market value of its shares (for the specifics of the problems of state corporations, see further in the text of the review). Shareholders are more interested in preserving and increasing the capital value - that is, in rising stock value of the company, as it provides grounds to the credits, which the company can attract for its operations, and therefore, its turnover. It is business solvency, which serves as an indicator of its high market value, because nowadays none of the shareholders invests their assets in production. If the company pays high dividends, the ability to get a good return on bank lending is reduced and, as a consequence, loans are decreased in line with production and profit. In this case, it is not clear what advantages the authors of the proposal see in re-privatization of shares in regard to the benefits of dividends as a source of financing pension costs in comparison with paying pensions from taxes deducted to the budget? High dividends are harmful to the organization. Subsoil user can be easily replaced (pursuant the law, ownership for subsoil is held by the federal and regional Subjects), and it will not affect budget revenues from taxes, including income taxes, but the liaison of retirement income to dividends with the shares of a particular company is a risky decision. Ownership of the shares does not guarantee of capital integrity - any company can suffer from bankruptcy, and then its shares will be worth nothing, and the property will go under the hammer.

At the current stage, the basic economic relations are the relations between the employees and the legal entity. The modern market is a complicated organizational structure, where continuous changes take place among both, capital owners in the stock trading (stocks, bonds, derivatives), and the cost of the production. The key issue for the capitalist is to catch a moment to transfer assets to the area, where the maximum return can be obtained. In other words, the capital owner is a much more uncertain subject of relationship now, than the team of employees. Thus, at this point one cannot seriously talk about labor disputes between the employees and the capital owner - if the stock is depreciated to zero, then the owners can instantly lose capital (the owner of the shares is not responsible for the debts of the company - the shares can be merely thrown away), and the employees and creditors are left with their requirements. Property of the bankrupt company will be sold by bankruptcy trustee. In other words, if the employees take a conflicting position, the company will be swept away from the market and get ruined very soon, the manager will receive a "golden parachute" and quit the business, and all claims of the employees will be eventually addressed to the state, rather than the capital owners. The competition between the cost of labor and the cost of the machinery, which can replace the labor force, is likely to be the key tool used to determine the actual number of employees in any specific industry. The Manager objective is to create competition within the employees' team to improve the quality of labor. Employees, in turn, must know in advance about plans for development and production and to be informed, under what circumstances and what jobs will be cut down; this information can mitigate social conflicts and should be reflected and regularly updated in the collective agreements with employees. Therefore, we believe that the participation of the employees in the management bodies of business companies will avoid major spontaneous disturbances, speed up the establishment of the modern labor market in Russia and finally, perhaps, to resolve the problem of privatization revision.

By the way, experts of the Center for American progress on its website (<http://www.americanprogress.org/>) also point to the fact that in our time, it is labor groups who generate middle class.

1 "Siluanov offered to dismiss regional leaders for budget debts. The Minister of Finance named the most troubled regions, whose heads, on the Agency opinion, should be made responsible for the budget debts", website [izvestia.ru](http://izvestia.ru), 13.09.2012.

released by the banks to the borrowers, look even more confusing<sup>1</sup>. Recall that the banks have the right to write off loans, including unearned interest from profit before tax – that is, cover their losses and lost revenue at the expense of the budget. If the government wants to help a citizen in a difficult financial situation, it should provide assistance in the form of targeted subsidies, along with other individuals in need: the disabled, pensioners, orphans, etc. The RF Ministry of Finance, once again appreciating the “generosity” of bankers, who repay the “forgiven” debt, including unearned interest (at the expense of the budget), demonstrated its willingness to decide on its own discretion, who is to pay taxes to the regional budget, and who is released from that liability (bearing in mind, that profits tax is one of the major sources of regional and local budgets), and then all claims will be laid against the governors, who fail to fund expenditures set up by law and go into debt. The State Duma, in turn, taking care of agricultural producers in view of the drought, has adopted the law granting them the right to apply zero-rate income tax for an unlimited term – in fact, at the expense of the regional budgets.

We have repeatedly pointed out that policy which replaces the lack of budget financing with the indirect tax benefits (although the Government of the Russian Federation has the right to provide tax credit in case of financial difficulties experienced by the taxpayers) is ineffective, since it provides an artificial support to the weak and uncompetitive manufacturers, damaging the revenue base of the state and hindering the formation of the regional own financial resources.

All the above is aggravated by external financial difficulties.

In the period under review Russia had to respond to the request of the US IRS to disclose the information on the accounts of the US residents, as well as to the financial claims of the EU to OAO “Gazprom”. Those two external requests are not accidental and reflect the style of relations between the state and business, which is typical for the open market. Let us try to compare the fiscal policy of the Russian authorities and that of the countries with developed market economies. We believe the policy of the Russian authorities should be more focused on the awareness of uniformity of market relations standards of the domestic and external markets. That is, there should be a clear understanding of what is acceptable and what is destructive to the state in the organization of the internal fiscal relationships. Apparently, there is no feeling of uniformity with the global market yet, which is the source of often incompliance of internal policy with the principles of fairness and neutrality in fiscal relations with the market participants, failure to maintain the competitive level of the tax burden on producers and provision of individual benefits, the use of taxes disguised in the form of fines and fees for public services, inconsistent with the upper limit burden on profits of individuals and legal entities, the desire to control the monopoly by maintaining a high share of state participation, etc. Apparently, the dominance of such approach is caused by the fact that the Russian government has virtually returned to the central planning system. The key planning points are funding the preset objectives; therefore the government should have a direct access to the main domestic revenue sources to meet declared commitments. In such circumstances, the market standards are allowed only to the extent that they do not interfere with the development program adopted by governmental authorities. Hence, there is an attitude to tax revenue not as to the main source of national revenue, but as an additional opportunity to increase proceeds from business activities of residents and non-residents of the country, because the first and foremost income, directly or indirectly controlled by the state is the profit of state-owned corporations (sale proceeds from raw materials, weapons, etc.).

In developed economies the government objectives are understood in a different way, which promotes different fiscal policy of high compliance, steadily pursued despite the crisis and the lack of funds. The bearing point of the developed markets is an absolutely firm principle of free competition and free capital circulation. Therefore, the government understands taxes as a major source of the national own funds and strictly controls neutrality, fair distribution of the tax burden and competitive tax system development. Analyzing the contents of the APEC agreements in regard to the free trade, the US experts highlight insufficient measures to prevent the capital export<sup>2</sup> by

1 T. Aleshkina, “Released debts without taxes”, website slon.ru on 09/18/2012.

2 The meaning of the phenomenon is as follows: e.g., there are two companies: one is a foreign corporation, the other one is a local company, forced to insure their commitments to counterparties in connection with the operations in the open market. Both of them sell refrigerators. The price for the local market is \$300 per piece. If due to a disguised state

companies with the state participation (in particular, such companies and policies are common in Asian countries) as one of the basic threats to the development of a free competitive market. This refers to the hidden subsidies received by such companies, which have an access to low-interest loans, taking advantage of recovering financial losses due to the government funding and other advantages, which make the products of such companies with state participation more affordable and attracts financial flows from the market in favor of these companies (and apparently, in favor of the relevant states – *author's note*)<sup>1</sup>. American experts, in particular, noted that entrepreneurs and trade unions are unanimous in the opinion that the benefits of the state-owned companies “distort the playing field and create disadvantageous conditions to the US companies and their employees”<sup>2</sup>.

Recently OAO “Gazprom” has faced the issue of free competition protection and forcing the state-owned companies to comply with the European market rules<sup>3</sup>. Herewith, this happened not due to someone’s wicked will. The rules are directly formulated in the Treaty on the Functioning of the European Union<sup>4</sup>. Let us refer to its text.

Pursuant Art. 101 of the Treaty: «1. The following shall be prohibited as incompatible with the internal market agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market, and in particular those which: (a) directly or indirectly fix purchase or selling prices or any other trading conditions; (b) limit or control production, markets, technical development, or investment; (c) share markets or sources of supply; (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this Article shall be *automatically void*» (the author’s *italic*).

The wording of the ban to benefit from a dominant position “in the domestic market or a substantial part thereof” is no less rigid (Art. 102).

The rules for the companies with state participation operations in the EU internal market are specified separately (Art.107): “...incompatible with the internal market in so far as it affects trade between Member States, the assistance provided by the states in any form or national resources, which distorts or threatens to distort competition by the benefits to individual companies or industries”. Herewith, in accordance with Art. 3, the EU has “exclusive competence in establishing the competition rules necessary for the functioning of the internal market”.

In this regard, the President’s Decree No. 1285 of September 11, 2012 “On measures to protect the interests of the Russian Federation in external trade activities of the Russian legal entities” should be regarded as an attempt to define some general rules of conduct for the Russian companies with the state participation in the European market, rather than protection of OAO “Gazprom” and other companies’ property interests, since blocking of the companies with state participation advantages in their operations in the open market is a general trend not only to the Russian companies, but to our Asian partners as well. Despite the possible sanctions, OAO “Gazprom”<sup>5</sup> is unlikely to withdraw from the European market; in fact, one can make profit in external markets only on the terms of fair competition, while doing so in the markets with foreign state monopoly is much more difficult.

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subsidies (for example, government support or government guarantee) a foreign state-owned company can lower the price to \$250, then (through its subsidiary) it will be able to take out \$200 (net of \$50 tax).

1 It is clear that no sovereign state will allow another state to pump out financial resources in a disguised form from the market, as it violates the principle of sovereignty..

2 Sabina Dewan, Director of Globalization and International Employment at the Center for American Progress; <http://www.americanprogress.org/issues/regulation/news/2012/02/23/11134/getting-state-owned-enterprises-right-in-the-trans-pacific-partnership/>

3 S.Kozlovsky, “Consumer is rebelling. EU may fine “Gazprom” for \$14bn”, the website lenta.ru 06.09.2012.

4 Treaty on the Functioning of the European Union, website eulaw.ru.

5 “Putin has protected the Russian companies from claims of foreigners. The President obligated the market leaders to coordinate their actions with the authorities in case of foreign buyers’ claims”, website izvestia.ru of 11.09.2012.

The result of the rigid protection of free competitive market is a similarly rigid enforcement of tax legislation compliance, because taxation is the key source of state revenue, and revenue base directly depends on the open market development.

In early September, Elvira Nabiullina, Assistant to the RF President held a meeting on implementation of FATCA (US Foreign Account Tax Compliance Act), coming into effect on 01.01.2013<sup>1</sup>. If an acceptable solution on the interaction of Russian banks with the US tax authorities is not found in a timely manner, it can result in tax law enforcement by the US government in regard to any transaction with the US counterparts and thus, complicate the business of Russian banks in external markets<sup>2</sup>. The issue of combating tax evasion is so pressing, that it gradually destroys the long-term traditions, for example, such as banking confidentiality. Global tax audit has also involved Swiss bankers. Reuters has published information on its website, that today the US tax authorities are accusing eleven Swiss private banks in tax evasion assistance to the US taxpayers, who made disguised funds transfers to offshore accounts. Credit Suisse, the largest Swiss bank has already informed that it will submit more details on cash flow management, including information on its employees involved in such operations, to the US official structures for the purpose of combating tax evasion. As a result, some of the Swiss bankers have abandoned their plans to go on holiday overseas in fear of being detained by the US official structures for specific investigations<sup>3</sup>.

Apparently, as soon as the economic activity of the state using such legal form as a state corporation, may happen to be inefficient and risky from the point of view of safety of capital and assets of these organizations in their activity in the open market.

The following technical documents on the application of the RF legislation on compulsory payments, adopted in the period under review should be highlighted.

1. We already mentioned before, that the judicial system of the Russian Federation does not include customs fees and duties in tax payments, if they are not specified in the RF Tax Code, and qualifies them as payment for public services, even if the RF government itself draws an analogy between some fees or duties with taxes. In particular, ambiguous positions in regard to the fees were demonstrated in the course of the Supreme Arbitration Court of the Russian Federation proceedings on recognition as discriminating in regard to non-resident entrepreneurs and abolition of a number of provisions of the Regulation "On patent and other fees for performance of legal actions related to the patent for the invention, utility model, production sample, with the state registration of the trademark and service mark, with the state registration and granting an exclusive right for the product origin, as well as with the state registration of the transfer of exclusive rights to other persons and agreements on disposal of those rights", approved by the Decree of the Government of the Russian Federation No. 941 of 10.12.2008. A foreign entrepreneur made a claim for cancellation the increased fee paid by non-residents of the Russian Federation, and the Supreme Arbitration Court supported it by the decision No. VAS-5123/12 made on August 28, 2012, confirming the equality of rights of the Russian and foreign copyright holders.

It is noteworthy, that during the court hearings the Russian government motivated differential approach to setting fees for residents and non-residents by the position of the RF Constitutional Court as expressed in its decision No. 5-P of 13.03.2008. According to the above decision of the RF Constitutional Court, the principle of equality before the law guarantees equal rights and responsibilities for entities belonging to the same category of taxpayers, but does not exclude a possibility of establishing different conditions for different categories of entities (in particular, residents and

1 "Nabiullina gave instructions to sort it out with the US tax authorities. Final proposals on American "anti-money laundering" law to be implemented in Russia will be submitted to her in two weeks. *izvestia.ru* of 5.09.2012. We are talking about agreements with IRS (U.S. tax authorities) submission of information on the customers – US tax residents' bank accounts. The US Internal Revenue Service transfers to the global control over taxpayers' execution of their tax liabilities. If this requirement is not fulfilled, the US tax authorities may enforce withholding 30% of the amount of transactions with US counterparties.

2 T.Aleshkina, "How much will the Russian bankers pay to the US tax authorities", website *slon.ru* of 14.09.2012. According to the experts, the tentative direct and indirect losses of banks due to a failure to comply with FATCA will exceed Rb 100bn. Bankers fear that after deduction of 30% tax, the US residents can demand compensation from Russian banks. Since the issue is not resolved in the Russian legislation, the client who has lost money during the payment, according to bankers, will have the right to do so.

3 Credit Suisse staff informed of the following objections, Reuters website of 17.09.2012 (See [in.reuters.com/article/2012/09/17/ubs-tax-idINL5E8KEH7820120917](http://in.reuters.com/article/2012/09/17/ubs-tax-idINL5E8KEH7820120917))

non-residents, according to the RF Government belong to different categories of taxpayers). The RF government considered permissible to apply the tax analogy to patent fees established by the challenged act.

The RF Constitutional Court did not support the Russian government and explained, that since the patent fees are regarded as fees, rather than taxes by legal nature, and therefore, an analogy with tax relations regulated by federal law and by-laws is inadmissible in their assessment.

The RF Constitutional Court has applied the following argument. Article 2 of the RF Civil Code provides for national tax regime to be applied to foreign entities. This means that the rules established by the RF Civil Code shall apply to relations with foreign citizens, stateless persons and foreign legal entities, so the Russian government was entitled to adopt Acts that restrict the rights of foreign individuals only in terms of retorsion, that is, if such restrictions are reciprocal (Article 1194 of the RF Civil Code). In addition, according to the RF Constitutional Court, the disputed provision is inconsistent not only with the national civil legislation of the Russian Federation, but also with the international treaty of the Russian Federation with the EU, which in view of Part 4, Art. 15 of the RF Constitution is a part of RF the legal system, having a higher legal force.

The above-reviewed services, which were referred by the RF Constitutional Court to commercial public services, are established as such by the RF government separate document and not included in the list of mandatory public services, approved by the RF Government Decree No. 352, version No. 874 of 30.08.2012 of May 6, 2011. All those issues provoke confusion in the legal mechanism for the recognition of the RF Government service provided for a fee, as a mandatory government service provided on a fee basis, or simply a function of the RF Government, which cannot be attributed to commercial services, which is paid directly from budget funds. We believe that in spite of the legal scheme applied by the RF Constitutional Court, payments for public services should not be regarded as taxes, only if the rights for their provision and getting payment are granted on a competitive basis or otherwise by an adequate market assessment.

2. A new phenomenon in tax administration is worth mentioning.

The letter of the Ministry of Finance of the Russian Federation and the RF Federal Tax Service No. OA-4-13/14433 of August 30, 2012 has communicated Recommendations on documents' preparation and filing for tax audit. The letter refers to the so-called controlled transactions between interrelated parties.

In particular, it is noted in the letter preamble that the RF Federal Tax Service "in order to implement Chapter 14.04 of the RF Tax Code, and in connection with the questions received from taxpayers, provides information on the preparation by taxpayers and filing with the RF FTS documents for tax audit". The liability of taxpayers to submit documents on controlled transactions is stipulated in Art.105.15 of the RF Tax Code. The Code defines the content of such documents and timeframes for audit – namely, six months after the reporting period. In the letter, the RF Federal Tax Service has provided detailed recommendations on the documents' structure.

In common understanding, the FTS recommendations require additional paperwork on the part of taxpayers, which in fact should be carried out by tax authorities in the course of audit. Most likely, there occurred a common mistake and the recommendation to tax authorities was presented as an advice to taxpayers. Let us review the text of the letter in more detail. Recommended content of documents is provided in Appendix 1 to the letter, preparation steps are enclosed in Appendix 2. According to those enclosures, the taxpayer is liable to provide: functional analysis, analysis of the economic circumstances of the parties in a controlled transaction, estimates of market prices or profitability range, include references "to the documents and other sources of information, which, if necessary, should be submitted at the request of the Federal Tax Service of Russia", etc.

Tax authorities recommend the taxpayers to prepare the following information: "description of goods (works, services), which are the subjects of a controlled transaction ... to assess the possibility of potential comparison with similar (identical) goods (works, services), the current level of competition in the relevant activity of the taxpayer (major competitors, customers of products, suppliers of raw materials) and the assessment of the competitive environment impact on the process of price formation, possible substitutes of manufactured goods ..." etc. (Appendix 1).

According to Appendix 2, it is recommended: to monitor prices in controlled transactions and the preparation of specific sections of the documentation at the time of transaction or price assessment

(Item 1, Para. 4); “...to provide more detail in the contract to determine the rights and liabilities of the parties. Herewith, it is important which party of the controlled transaction performs (fails to perform) the terms of the contract, and *what provisions do not reflect actual relationship of the parties and their real economic and financial performance*” (Item 4, Para. 8); “... to identify the parties to the transaction as a company carrying out basic functions or bearing key risks, and the companies carrying out “routine” functions ... *search for comparable independent companies performing routine functions is less complicated*” (Item 5, Para. 7)<sup>1</sup>.

As we see, in terms of both, the structure and the content, the recommended list of documents looks like a detailed analytical report, which a taxpayer must prepare for the RF FTS for free.

It is clear, why the tax authorities carefully presented their requirements and regulations as “recommendations”. In fact, such policy can lead to additional administrative pressure by shifting a part of workload to be performed by tax authorities to those involved in business activities. In any case, this is certainly a new phenomenon in the official administration of tax audits. In our view, the legitimacy of this type of recommendations on the documents to be filed by the taxpayers requires additional legal review. ●

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1 The author’s *italic*.

## CHANGES IN THE REGULATORY BASE OF THE BUDGETARY PROCESS

M.Goldin

*In September, the following changes were introduced in the regulatory base of the budgetary process: from October 1, 2012 the Government of the Russian Federation increased by 6% labor remuneration of workers of federal government, state-financed and autonomous institutions; the Rules of Formation of the Plan of Procurement of Goods (Work and Services), as well as requirements to the form of the plan of procurement of goods (work and services) were approved by a resolution of the Government .*

**By Instructions No. 1667-r of September 11, 2012 of the Government of the Russian Federation** “On Taking of Measures by Federal Executive Authorities which Carry Out Authorities of a Founder of Federal Government, State-Financed and Autonomous Institutions which are Within their Jurisdiction and Main Distributors of the Federal Budget Funds as Regards Raising” from October 1, 2012 of Labor Remuneration of Workers of the Specified Institutions labor remuneration of workers of federal government, state-financed and autonomous institutions was increased by 6% from October 1, 2012.

Labor remuneration was increased for the following categories of workers:

- Workers of federal government, state-financed and autonomous institutions;
- Workers of federal government authorities, as well as civil personnel of military units, entities and departments of federal executive authorities where military service as well as the one made equal to it are provided for by the law and remuneration for such services is carried out in accordance with Resolution No. 583 of August 5, 2008 of the Government of the Russian Federation “On Introduction of New Systems of Labor Remuneration of Workers of Federal State-Financed and Government Institutions and Federal Government Authorities, as well as the Civil Personnel of Military Units, Entities and Departments of Federal Executive Authorities where Military Service and the One Made Equal to it are Provided for by the Law and Remuneration for such Services is Carried out at Present on the Basis of the Single Wages Scale as Regards Labor Remuneration of Workers of Federal Government Institutions”;
- Workers of state academies of sciences and institutions which are subordinate to them.

**By Resolution No.932 of September 17, 2012 of the Government of the Russian Federation**, the following was approved:

The rules of formation of the plan of procurement of goods (work and services);

Requirements to the form of the plan of procurement of goods (work and services).

The rules determine the procedure for formation of the plan of procurement for the needs of legal entities specified in Article 1 of Federal Law No. 223-FZ of July 18, 2011 on Procurement of Goods, Work and Services by Individual Types of Legal Entities (hereinafter, Federal Law No.223-FZ).

It is to be reminded that such legal persons include:

1) state corporations, state companies, entities of natural monopolies, entities carrying out regulated types of activities in the sphere of power, gas, heat and water supply, water discharge, waste water treatment, reclamation (disposal) of urban ore, state unitary enterprises, municipal unitary enterprises, autonomous institutions, as well as economic entities in whose charter capital the share of participation of the Russian Federation, a constituent entity of the Russian Federation and a municipal entity exceeds aggregately 50%;

2) subsidiary economic entities in whose charter capital the above institutions own aggregately over 50%;

3) subsidiary economic entities in whose charter capital the above subsidiary economic entities own aggregately over 50%.

The plan of procurement includes information on purchasing of goods (work and services) which are required for the customer's needs to be met.

In accordance with Article 4 (15) of Federal Law No. 223-FZ, the plan of procurement does not include information on procurement of goods (work and services) which constitutes a state secret provided that such information is included in the notice on the procurement or draft agreement, as well as any other information on the procurement if a decision of the Government of the Russian Federation has been taken to that effect.

In accordance with Article 4 (15) of Federal Law No. 223-FZ, the plan of procurement may not include information on procurement of goods (work and services) provided that the cost of goods (work and services) does not exceed Rb 100,000, while in case the customer's annual revenues in the reporting fiscal year amount to over Rb 5bn, the information on procurement of goods (work and services) whose cost does not exceed Rb 500,000.

The plan of procurement is formed by the customer in accordance with the requirements set by statutory acts of the Russian Federation, domestic documents of the customer, as well as provisions on procurement approved in accordance with the established procedure with purchasing deadlines taken into account on the basis of the required date of delivery of goods (work and services).

The plan of procurement may be formed with taking into account such information as the exchange rate, market indices and other information on the basis of the following programs which determine the activities of the customer:

- a) production program (all the purchases which form the estimate of costs related to production and sales of goods (work and services);
- b) maintenance program (maintenance schedule);
- c) investment program (including technical re-equipment and modernization with those in the area of information technologies and new building included);
- d) other programs.

The plan of procurement of goods (work and services) is made up by the customer in accordance with the form as per annex as a single document in the electronic format which can be saved on the user's hardware, provides an option of a search and copy of a random extract of the text by means of the relevant program for viewing and includes the following information:

- 1) subject of the agreement with specification of the identification code of procurement in accordance with the National Industry Classification Standard (NICS) and National Classification Standard of Economic Activities, Produce and Services (NCSEAPS);
- 2) such minimum requirements to goods (work and services) to be purchased as are provided for in the agreement, including operating, technical and quality parameters and such performance specification of the subject of the agreement as permits to identify the subject of the agreement (if required);
- 3) the information on the initial (maximum) price of the agreement (price of the lot);
- 4) the expected date or the period of placement of a notice on procurement (year and month);
- 5) the term of the contract (year, month);
- 6) mode of purchasing.

In addition to the above, Resolution No. 932 of September 17, 2012 of the Government of the Russian Federation sets the requirements to the Plan of Procurement of Innovation Products, High-Tech Products and Pharmaceuticals. ●