**Russia and the international economy**

**1. Russia and the international trade system**

According to a medium-term forecast for developments in the area of the international economy, business revival is cumulating momentum after the recession it experienced in early 1990s. It had a relevant effect on the world trade. In 1994 the average international trade turnover showed a 9.5 percent growth being a record figure in the last 20 years and by 3 times exceeding the increase in the international production. In 1995 the World Trade Organization estimated 8 percent increase in trade turnover as compared with a 3 percent growth in the world production. World Bank experts think that in the next 10 years an average increase in foreign trade will make 6 percent annually.

An economic run-up in most industrialized countries was followed by a growing demand for many products and a consecutive price hike on international markets.

Oil markets showed a balance of demand and supply in 1995. Average prices of Dubai oil were at $ 123 per metric ton, by 14.9 percent exceeding 1994 averages. Owning to small increase in the world oil consumption and practically unchanged supply situation no perceptible change of prices is expected.

A trend of natural gas prices on markets in Western Europe was practically the same as the oil price dynamics. In 1995 average prices were by 13.4 percent higher as compared with 1994.

Prices of nonferrous metals have risen dramatically. In 1995 average world prices were as follows: aluminum -- $ 1806 per metric ton (20.3 percent rise in comparison with 1994), copper -- $ 2933 (higher by 23.3 percent), nickel -- $ 8063 (19.3 percent growth).

As a result of the 1994-95 record price surge in the whole period after the World War II cellulose joined the leaders with a 50 percent price hike (up to more than $ 1000 per metric ton). According to a middle-range outlook price stabilization accompanied by a slight price rise is expected.

As market relations develop, process of internal price structure formation continues in Russia and it gradually closes to the price system existing on world markets. In 1995 contract prices grew perceptibly, however, prices of a majority of energy resources lagged behind those on the world trade markets in terms of rates of increase. The outcome was a worsening balance between contract and world prices.

An important role in development of the international trade is played by the GATT/WTO which for 48 years tried to work out the fundamentals of a future world trade basing on principles of observance of the Agreement's general regulations aimed to keep up non-discrimination of individual states and to a gradual elimination of barriers slowing down mutual exchange of commodities. Since 1950 the world trade turnover has increased by 13 times and eight rounds of multilateral trade negotiations held under the GATT's auspices have led to a ten-fold cut of average customs duties. At present it makes a bit less than 4 percent.

Russia's accession to the WTO will make it possible to tap all measures existing within the framework of this organization in order to protect Russia's economic interests. At present direct or concealed discrimination of Russian producers and traders on markets of certain countries is among factors affecting Russian exports dynamics. Thus, only the ban on Russian uranium exports to the USA has led to losses for Russia, as estimated by some experts, at $170 million a year. The total number of anti-dumping procedures imposed upon Russia has reached 41. More than a half of them (22) are qualified as openly discriminatory cases or unjustified claims by the Ministry of Foreign Economic Relations.

In the summer of 1995 the first round of negotiations between the Russian delegation and the WTO's Working Group on Russia took place in Geneva. Members of the Working Group apprised information on foreign trade regulations stated in the Russian Memorandum as exhaustive enough.

An outcome of the second round taking place from December 4 to 7 of 1995 was the completion of discussion of the Russian Memorandum on the foreign trade regime as concerns trade in goods. Besides, the first discussion on special annexes to the Memorandum embracing protection of intellectual property rights, trade in services and trade-related investment measures was held. At the same time, the WTO member countries have reserved the right to revert to a detailed discussion on three key issues: if state-owned trade organizations exist in Russia (Moscow denies this); import licensing; subsidizing of external operations. However, even now they agree in principle that the Russian legislation is in accordance with the WTO's rules and norms in these areas of the foreign trade regulation.

There are no apparent opponents to Russia's accession to the WTO, since the world trade, especially in the area of trade in raw materials, cannot be regulated without participation of Russia. However, the admission of Russia may be surrounded by a number of additional obligations not directly following from the WTO requirements. Bilateral consultations held in Geneva have shown that Russia will face some complications in the course of tariff negotiations.

On the whole, the outcome of the second round of Geneva talks has been successful for Russia.

**2. Regulation of External Economic Activities**

In 1995 certain changes were introduced to the mechanism of the state regulation of the foreign trade. In the first half of 1995 the state regulation of oil exports was substantially amended: quotas and licenses in oil exports were abolished alongside with preferences (with exclusion of supply pursuant to intergovernmental agreements) while export duties on oil and oil products were significantly reduced; certain oil products were excluded from the list of strategically important commodities. Producers' access to channels allowing transportation of oil to other countries (pipelines and terminals in sea ports) became a natural restraint on exports.

The list of strategically important raw commodities was shortened and the institution of special exporters was abolished altogether. The system of contracts' registration became the main instrument of control over exports. Individual preferences granted to participants of external economic activities were abolished, excluding those issued in accordance with the laws of the Russian Federation.

The law "On State Regulation of Foreign Trade" adopted in July came into force in October. The law stipulated what authority in this area shall be with the President, the Government and the Ministry of Foreign Economic Relations. The exclusiveness of the MFER's position was emphasized by the fact that only it was vested with the right to license import and export transactions subject to quantitative restrictions or to approval procedures.

As pursuant to the law, the Russian Government shall submit a program of foreign trade development together with a draft of the Federal budget for the Parliament's approval. Alongside with other provisions this program shall embrace customs tariff rates planned for the year in question as well as the band of their possible fluctuation, thus making the foreign trade more predictable. The Government has the right to introduce export and import quantitative restrictions on national security grounds, to comply with international agreements or to protect the domestic market, however, these measures shall be announced not less than 3 months prior to their actual introduction. The law envisages a possibility to introduce state monopoly for trade in certain products. In this case a special procedure of licensing import and export operations exclusively to state-owned enterprises shall be applied.

As the above mentioned law was effectuated, the Commission of the RF Government on Safeguard Measures in Foreign Trade became fully legitimate and in December it received "Procedures of Investigation Prior to Application of Safeguard Measures" approved by the MFER (Russ.abbr. MVES). A possibility to apply safeguard measures against competitive imported products complies with usual practices applicable in the world trade. In this area Russia is late in working out and application of such measures, especially taking into account that Russian exports are often and in most cases unjustifiably subject to discrimination on foreign markets. So, the RF import regime loses its exceptional liberalism which has been characteristic of it until recently.

Tariff regulation. From September through December export duties levels were gradually lowered until their complete abolition since January 1, 1996, with an exception of a small group of goods including oil, natural gas and some other raw commodities.

In June and in October, 1996 import duty rates were changed. On the whole, changes were made in direction of an increase in tariffs. Earlier goods taxable at 1 percent have constituted a rather significant part of the list, at present this rate is only applicable to certain goods within Group 10 of the External Economic Activity commodity nomenclature (grain) and 1701 (cane sugar, beet firm sugar and sucrose). A 10 percent tariff is now applied to medicines which earlier have been exempt from duties while fish and fish products are subject to a double rise of duties (from 5 to 10 percent) and duties on vegetables were tripled (from 5 to 15 percent). For foodstuffs earlier exempted from duties new tariffs made 5 percent on bananas and citrus fruits, 10 percent on tee and coffee, 15 percent on fresh cucumbers, however, rates of import duties in Russia still remain considerably lower than in the EU countries (16 percent against 21 percent). There were effectuated provisions stipulating a 30 percent duty on goods such as luxuries, tobacco products, alcoholic beverages and weapons.

Tax regulation. As before, close attention was paid to products subject to excise taxation. In July and in December, 1996 a price difference between excise stamps and special stamps designated for imported tobacco and alcohol products were adjusted. There were created equal conditions for importers of these products both from countries within and outside of the former Soviet Union (ECU 0.1 per unit of an alcohol beverage and ECU 0.01 per unit of a tobacco product). In December the rate of excise tax on tobacco products was increased from ECU 1.2 to ECU 2 per 1000 pieces.

In June the list of products subject to a preferential 10 percent value added tax was shortened; it was again examined in detail in November and some new products were added to it. In December works and services, both produced domestically and purchased, being exported to countries outside the CIS alongside with services concerning the transit of foreign cargo through Russian territory were exempted from the value added tax.

Preferences in External Economic Activities. In October, 1996 the Government abolished previously applicable preferential taxation of alcoholic beverages imported from abroad by certain legal entities which were exempt from customs duties (for instance, the National Fund of Sports and the All-Russian Society of Invalids). Since December, pursuant to the Presidential Decree "On Customs Preferences" of November 30, 1995, it is inadmissible for Federal agencies to adopt decisions which would provide prolongation of preferences in terms of customs duty exempts and receipts of additional compensations.

In August, 1996 the control mechanism over incoming export proceeds denominated in foreign exchange was adjusted. All proceeds in foreign currencies shall be entered into accounts with authorized banks--that became a requirement of the customs regime. Customs service now enjoys the right to control all capital flows and apply relevant sanctions if necessary.

In September, 1996 the control over exports and imports of military-purposed products, works and services, subject to licensing, was tightened.

In December the set of instruments of the state control mechanism over imports was supplemented. The system of foreign exchange control over imports introduced on January 1, 1996, is basing on the same principles as the export control existing since 1994 and envisages the same chain of relations: an importer--an authorized bank--customs. The key document fundamental for the whole control system is a registration certificate for import transactions.

**3. Foreign Trade Pattern**

In 1995 Russian foreign trade was influenced by differently directed factors. A favorable state of the world market and the governmental policy of stimulating exports via regular lowering of export duties provided for a further increase in volumes of trade with countries outside the former Soviet Union and a stable active balance of the foreign trade.

Estimating Russian foreign trade the following adverse factors shall be taken into account: a decline in production, small amounts of investment, rather high inflation rates, insufficient level of state assistance for development of the country's export potential, poor competitiveness of many Russian-made manufactured products, especially of machines and equipment, lack of positive shifts in development of Russia's external relations with countries of the former CMEA, huge external debt, discriminatory barriers banning a number of Russian-made products from external markets. In connection with accession of Finland, Sweden and Austria to the EU Russia automatically became subject to anti-dumping and quantitative restrictions concerning trade with these countries in steel, textiles, mineral fertilizers, uranium.

Introduction of the "ruble corridor (fluctuation band)" alongside with a relatively high internal price dynamics caused deterioration of export transactions' effectiveness. However, due to liberalization of energy resources exports, the export sector reacted to the introduction of the "corridor" slower and not so sharply as critics of a fixed exchange rate had believed. At the same time, stabilization of ruble exchange rate created a sufficiently favorable transaction climate for importers allowing them to compensate a part of the loss inflicted by an increase in import tariffs.

Goskomstat reports that the Russian foreign trade turnover, unorganized trade including, made $ 135.7 billion in 1995, or by 16 percent more in comparison with 1994 figures. Exports were at $ 77.8 billion (a 18 percent increase) and imports at $ 57.9 billion (by 15 percent more).

The results of external economic activities in 1992 through 1995 are indicative of the fact that Russia re-oriented its trade towards industrialized countries and that the share of countries outside the former Soviet Union in the total foreign trade turnover has grown. In 1995 countries outside the former USSR accounted for 78 percent of it. In 1992 through 1995 exports to these countries increased at a record rate in the last 20 years with exports showing a 25 percent growth ($ 64.3 billion) and imports (together with unorganized trade) increasing by 12 percent ($ 41.6 billion).

In 1995 growth rates slowed down considerably. Thus, while in the first quarter exports grew by 45 percent as compared with the same period in the last year, in the second quarter it made only 29 percent and showed a modest 15 percent increase in the third quarter. Undoubtedly, export growth rates were affected by the "currency corridor (fluctuation band)" introduced in the second half of the year.

As before, the bulk of Russian exports consists of raw materials. Fuel and energy resources account for the biggest share (41 percent) of exports, while the Fuel-and-Energy Complex production (oil, natural gas, oil products) becomes more and more oriented towards external markets.

In 1995 a decline in export growth rates in real terms was observed as natural gas exports increased by 11 percent (14 percent in 1994), oil products grew by 8 percent (11 percent), oil--by only 1 percent (11 percent).

Growth of exports as calculated in value terms was primarily caused by a favorable situation on the world market. Average contract oil prices of exports in the countries outside the former Soviet Union increased by about 7 percent as compared with 1994 figures, natural gas exports grew by 10 percent while oil products showed a 6.6 percent increase.

Metal exports accounted for a 20 percent share in the Russian exports. Nickel and ferrous metals exports grew most rapidly at 37 and 26 percent accordingly. Average export prices of key metals surged, thus, price of nickel increased by 33.1 percent, of aluminum--by 36.9 percent, of copper--by 24.2 percent, of ferrous alloys--by 24.7 percent, of pig iron--by 14.6 percent. The pattern of metal exports has somewhat changed. Customs statistics reveal a growing number of contracts on export of finished metal articles, however, their share in the total export volumes is still insignificant. These articles are being made according to designs of foreign companies (mostly in aircraft and engineering industries) under a binding condition that they shall be manufactured in accordance with the West European standards and certified by a foreign firm. It is too early to suggest the end of an age of raw exports conducted in their most primitive form, however, the Russian metal industry is given an opportunity to participate in the international division of labor on equal basis and to reach a qualitatively new level of production.

The share of chemicals made 9.6 percent. Mineral fertilizers still remain a key export item in the industry. Export volumes of mineral fertilizers increased by 14 percent in comparison with 1994 figures. Simultaneously, average contract prices also grew (by 24 percent).

Export patterns within the forestry and paper industry tended to be oriented towards raw materials in recent years affecting the structure of currency proceeds accordingly. A third of foreign exchange proceeds was derived from raw timber (logs) exports while semi-finished timber (lumber) accounted for 25 percent of proceeds and processing-intensive products brought only 32 percent.

A considerable increase in physical volumes of exports in the countries outside the former Soviet Union as compared with the previous year figures was reported for logs (37 percent) and cellulose (38 percent). At the same time, average export prices of logs grew by 2.8 percent and of cellulose -- by 96.6 percent.

One of the ways to increase export revenues is an expansion of sales markets for Russian-made weapons and military equipment. Export volumes of military production made $ 2.6 billion in 1995, that being by 1.7 times more than in 1994.

The share of machines and equipment in Russian exports to countries outside the former Soviet Union contracted to 3.8 percent as compared with 5.3 percent in 1994. Development of new competitive and technologically-intensive products relevant to modern level of requirements on external markets demands large investment and is time-consuming.

An increase in internal productional costs, first of all at the expense of energy and raw materials, more expensive loans, growing transport expenses, aging production assets in extractive and processing branches, deteriorating productional situation contributed to diminishing effectiveness of export transactions. At present only export of natural gas, oil, nickel, timber and lumber are profitable. Export of oil products, ferrous and nonferrous metals, chemicals begins to bring losses. However, due to worsening financial situation of Russian enterprises and growing payment arrears exporters prefer to have hard currencies even at declining or altogether negative profitability of exports.

The most dynamic and growing market of the Russian Federation are industrialized Western countries. The largest share of Russian exports goes to Germany (9.1 percent). The USA account for 6.9 percent, Switzerland--for 5.8 percent, Italy--for 5.6 percent, Japan--for 5.5 percent, Netherlands -- for 4.9 percent, Great Britain -- for 4.7 percent and Finland--for 4 percent of Russian exports.

The pattern of Russian imports has not been changed considerably. As before, machines and equipment were ranked first and accounted for a 38 percent share of the total imports which grew by 23 percent in comparison with 1994. It was caused by a necessity to provide key branches of the national economy with modern technologies and equipment.

A decline in agriculture followed by deteriorating provision of the populace with domestic-made foodstuffs has led to an expansion of food imports. Such measures as a rise of import duty rates, introduction of excises and of value added tax, abolition of preferences concerning import tariffs, which have been taken lately, contributed to an increase in internal prices of imported goods thus creating prerequisites to restrain imports. However, stabilization of ruble somewhat compensated for the negative impact of growing import duties and excises and helped to increase imports.

In 1995 imports grew considerably, especially of such products as sunflower oil (a 232 percent increase), poultry (by 70 percent more), alcoholic and non-alcoholic beverages (a 67 percent increase), butter (an increase by 65 percent), frozen meat (by 43 percent more).

In the nearest future dynamics and pattern of the country's foreign trade will be first of all determined by the internal economic situation, i.e. whether it shows signs of business revival or not, by changes in the structure of supply and solvent demand on the domestic market, as well as by exchange rate policies. The regulatory mechanism of the external economic activities may also change due to political factors.

In 1996 exports grew somewhat slower (at about 1--3 percent rates). It was expected that export of major fuel and energy resources would remain at the same level while such products as metals, chemicals, timber, pulp and paper would be exported in increasing quantities.

Oil and natural gas exports remained profitable because estimated rates of internal price growth prevailed.

Imports pattern changed impacted by a growth of the share of technological equipment and manufactured consumer goods. Growing imports of key foodstuffs and non-food consumer goods led to application of certain measures aimed to tighten protectionist regime in order to safeguard domestic industries in 1996 (import quotas introduced).

In 1995 Russian foreign trade turnover with the CIS countries made $ 29.8 billion, increasing by 5 percent in comparison with 1994 figures, it is due, first of all, to a price rise concerning fuel and energy products (14 -- 28 percent on the average). Exports made $ 13.5 billion, or by 9 percent less than in 1994 while imports reached $ 16.3 billion (a 21 percent increase). The share of the CIS countries in the Russian foreign trade turnover diminished by 2 percent as compared with the previous year figures and made 22 percent.

For the first time in the years of the CIS existence Russia had a negative trade balance with these countries ($ -2.8 billion) while in 1994 it had a trade surplus of $ 1.2 billion. Starting from the end of the last year imports from the CIS grew at a fast rate while exports gradually shrank.

The main reason determining the import surplus is an unbalanced, owning to a crisis situation existing in national economies, foreign trade within the CIS framework, that rendering difficulties in settlement of the CIS countries debts, especially those due for fuel and energy resources supply. According to current data, these debts as of January 1, 1996, made Rb 15.6 trillion, or two times more than in 1995. It is hardly justified to attribute Russian shrinking exports to neighboring countries to introduction of the "currency corridor (fluctuation band)" as their fall began as early as April while to the contrary in October some increase in export operations was observed. On the other hand, introduction of the "currency corridor (fluctuation band)" and stabilization of ruble exchange rates enhanced effectiveness of operations of exporters from countries within the former Soviet Union on the Russian market.

As before, the fuel and energy products accounted for the bulk of exports to the CIS member countries (about 50 percent). Total volumes of oil exports diminished by 22 percent as compared with the previous year while export of oil products shrank even more considerably -- by 60 percent, the fact caused not only by payment arrears in reciprocal transactions, but by growing export prices of Russian oil which increased by 28.3 percent in comparison with the last year figures and reached $ 74.9 per metric ton (that making roughly 70 percent of prices under export contracts with countries outside the former Soviet Union). However, now some CIS countries try to reduce their dependence on Russian energy supply. For instance, Moldavia has already signed an oil import agreement with Iran while Ukraine relies upon cooperation with countries of the Persian Gulf. At the same time, Russian oil exports to Byelorussia grew considerably as a result of creation of the common customs area, that allowing Byelorussian oil processing enterprises to purchase oil at prices quoted on the Russian domestic market.

The pattern of Russian exports somewhat changed in 1995 as compared with 1994, for instance coal exports grew by 32 percent, iron ore exports increased twofold and export of ferrous metals also showed signs of growth.

As concerns import operations, the role of the CIS member countries remains an important one in terms of providing Russia with foodstuffs. Thus, the share of white sugar imports from these countries reached 80 percent while their volumes increased by more than two times since the last year. There was also observed an increase in imports of grain, meat, butter. At the same time, a trend to purchase fewer consumer goods in countries within the former Soviet Union in connection to availability of cheaper similar products of quality made in the West manifests itself.

The Customs Union of Russia, Byelorussia and Kazakhstan which was established in 1995 and faces a number of objective difficulties and contradictions caused in the first turn by differences in levels of development and directions of reforms. The Intergovernmental Economic Committee which at last started to perform its functions in 1995 still lacks supranational authority; unsettled problems of mutual payment arrears prevent activities of the Payment Union.

Prospects of foreign trade developments within the CIS cannot be estimated in simple terms. The Commonwealth's objective orientation towards integration faces grave political and economic problems. It is probable that in the beginning of next year a negative trade balance with neighboring countries will remain, in particular due to further decline in export of fuel and energy products.

On the whole, the Commonwealth's future, undoubtedly, will depend on the political situation in Russia. However, the experience of the last few years demonstrates that Russia's partners within the CIS prefer to act according to their economic interests rather than to political rhetorics. The CIS member countries are interested in an economic cooperation with Russia exactly because it has progressed relatively further on the way of reforms. That is why slackening pace of the reform or a complete stop of the transformation may damage trends towards integration to such extent that any political declarations on closer unity and cooperation will be overweighed.

**Balance of Payments**

The balance of payments reflecting Russian residents' activities in the external sector reveals the following key facts.

In 1995, the strengthening ruble did not hold back the growth of trade surplus: exports increased at a greater rate than imports.

As during previous periods import of services exceeded their exports, that being primarily attributed to developing tourism to countries outside the former Soviet Union. Thus, import of tourist services exceeded imports by $ 5366 million. As a result, current accounts balance was by 43 percent less than the balance of foreign trade. Operations of governmental agencies prevailed in the capital account. External debt grew due both to new borrowing and deferments and arrears in debt servicing.

Non-state sector operations were mostly represented by commercial loans, both in terms of merchandise exports with deferred payments and advance payments. As concerns direct and portfolio investment, they remained at an insignificant level.

Growing reliance of residents on ruble was shown by somewhat decreasing amounts of cash foreign exchange.

As a rule, commercial structures accounted for loans granted to non-residents. The main form of such loans was export loans of enterprises.

Non-repatriation of export proceeds became an important factor destabilizing the financial sphere. In January through September of 1995 it reached $ 5.6 billion, as the State Customs Committee (GTK) reports. This figure is comparable to all foreign loans drawn by the state in the same period.

The amount of payments due to disburse the official external debt exerted more pressure on the Federal budget as compared with the same period of the last year. While in 9 months of 1994 96 percent of actual payments to disburse the official external debt were financed at the expense of external sources and only $ 134 million were received from internal sources, in 9 months of 1995 the figures made 89.5 percent and $ 590 million accordingly.