



**THE CENTRAL BANK  
OF THE RUSSIAN FEDERATION  
(BANK OF RUSSIA)**

**Quarterly  
Inflation  
Review**

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**2005 Q2**

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**Research and Information Department**



## Introduction

Consumer price inflation was higher in the first half of 2005 than in the same period last year. Consumer price growth acceleration was attributable to factors outside the sphere of influence of the Bank of Russia's short-term monetary policy. This acceleration was largely due to a rapid growth in the prices of some foodstuffs (meat and fish products), the continued rise of world energy prices and a considerable increase in the prices of paid services to households, especially federally and regionally regulated prices. Another factor was a significant rise in vegetable and fruit prices.

As in the same period last year, household consumer spending continued to grow rapidly in January-June 2005. As employment grew, demand exerted upward pressure on consumer prices.

The prices of meat (especially beef and pork prices) continued to rise significantly in 2005. The same situation was observed in 2004. In the first half of 2005, the growth of poultry, fish and seafood prices accelerated considerably. Some foreign countries, for example, the USA, also registered an accelerated growth of meat prices on the consumer market.

Despite growth in world energy prices in the first half of 2005, domestic petrol prices rose insignificantly as compared with the previous year.

The Bank of Russia's exchange rate policy had a positive effect on core inflation. As the dollar appreciated against the euro on the international forex market, the ruble's nominal effective rate against the currencies of Russia's major trade partners rose 2.7% in June 2005 as compared with December 2004.

The growth of money supply accelerated in annual terms from March 2005. But the existing lags prevented this factor from exerting extra pressure on core inflation in 2005 Q2. However, if this trend continues to persist in money supply dynamics, monetary inflation will intensify and this factor can worsen the start conditions of the year 2006. That is why, it is extremely important for ruble supply growth to slow down to achieve the desired level of core inflation both this year and next year.

In the second half of 2005, core inflation will be affected (other conditions being unchanged) by the unsteady money supply observed in the last months of the previous year and in the first half of the year, foreign exchange rate dynamics and large budget non-interest expenditures compared to the first half of the year. At the same time, the budget will keep its sterilising function.

The monetary accommodation measures along with the stronger role of the Stabilisation Fund of the Russian Federation (hereinafter referred to as the Stabilisation Fund) sterilised a considerable part of free liquidity. In addition, low-liquidity ruble components (time deposits) prevailed in the structure of ruble supply growth, which was important from the viewpoint of weakening the inflationary consequences of monetary growth. At the same time, the trend of the declining share of cash in the M2 aggregate largely persisted in the first half of the year and had a positive effect (along with other factors) on inflation dynamics and the velocity of money.

In the conditions of a considerable inflow of foreign exchange to the domestic market and the policy of the managed floating of the exchange rate, the Bank of Russia took measures to contain money supply growth and its monetary policy aimed to restrain the expansion of the monetary base and absorb excess liquidity. The value of funds absorbed in the accounts of the general government with the Bank of Russia (largely through the expansion of the Stabilisation Fund) exceeded money supply growth from the Bank of Russia's operations on the domestic foreign exchange market.

The Bank of Russia conducted operations with its own bonds (OBR bonds) and daily fixed rate deposit operations on standard terms and also held deposit auctions as major sterilisation instruments. At the same time, as the level of banking liquidity fell in 2005 Q2, such operations relating to the provision of liquidity as repo operations and also intraday credits and overnight loans were most popular with banks.



## Major Inflation Indicators

According to the Federal Statistics Service, consumer prices rose 8.0% in the first half of 2005 (6.1% in January-June 2004).

Inflation equalled 2.5% in 2005 Q2 as against 5.3% in 2005 Q1. Consumer prices rose 1.1% in April month on month, 0.8% in May and 0.6% in June. Consumer price inflation in the moving 12-month period stood at 13.7% in June 2005 (13.6% in March 2005).

**Core inflation** equalled 4.4% in June 2005 as compared with December of the previous year (it was 4.3% in the first half of 2004). The prices of goods and services included in the core inflation calculation grew 1.9% in 2005 Q2 (2.4% in 2005 Q1). The prices of this group of goods and services increased 0.9% month on month in April, 0.6% in May and 0.5% in June. Core inflation in the moving 12-month period stood at an estimated 10.6% in June 2005.

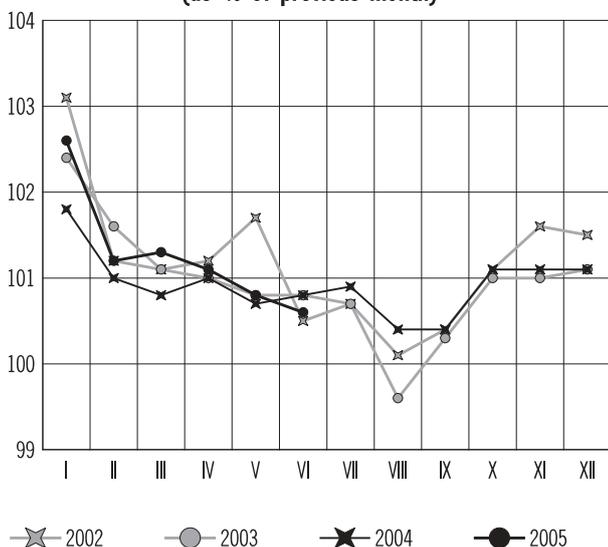
Estimates show that growth in the prices of goods and services included in the core inflation calculation in January-June 2005 accounted for 3.5 percentage points, or 44.1% of overall consumer price growth as against 3.5 percentage points, or 57.2%, in January-June 2004.

The relatively high level of core inflation registered in the past two years is largely due to volatile, local and short-term factors.

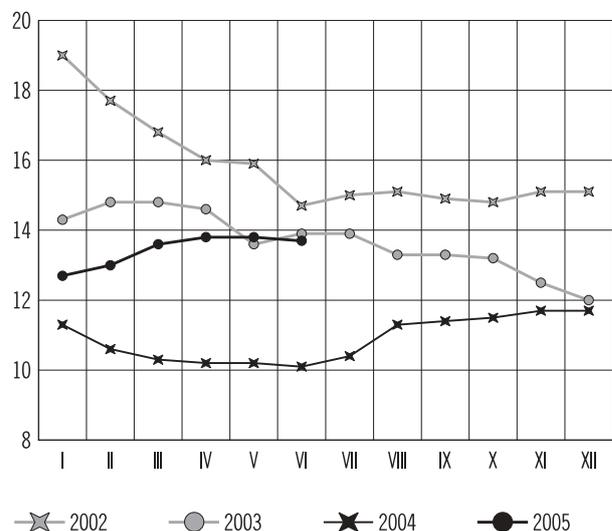
**Food prices, excluding vegetable and fruit prices**, gained 5.5% in January-June 2005 as against 5.2% in the same period last year. They rose 3.1% in 2005 Q1 and 2.4% in 2005 Q2. In the first half of 2005, growth in food prices, excluding vegetable and fruit prices, accounted for an estimated 2.5 percentage points, or 31.3%, of overall consumer price growth as against 2.6 percentage points, or 42.3%, in the same period of 2004.

The most significant growth in the first half of 2005 was registered in the prices of meat and poultry, which increased 14.6% as compared with 6.9% in the same period last year. This year, the growth of poultry prices accelerated considerably as compared with the same period of 2004 (they rose 18.9% in the first six months of 2005 as compared with 0.4% in January-June 2004). This year, poultry prices grew faster than beef and pork prices apparently due to stronger consumer demand for cheaper poultry. Meat and poultry prices grew amid the expansion of meat imports (beef, pork and poultry). The share of beef (fresh, cooled and frozen beef) imported under quotas increased from 63.7% in January-June 2004 to 71.3% in the same period of 2005 and the share of pork went up from 89.9% to 92.7%. The domestic beef and pork output declined in the first half of 2005 year

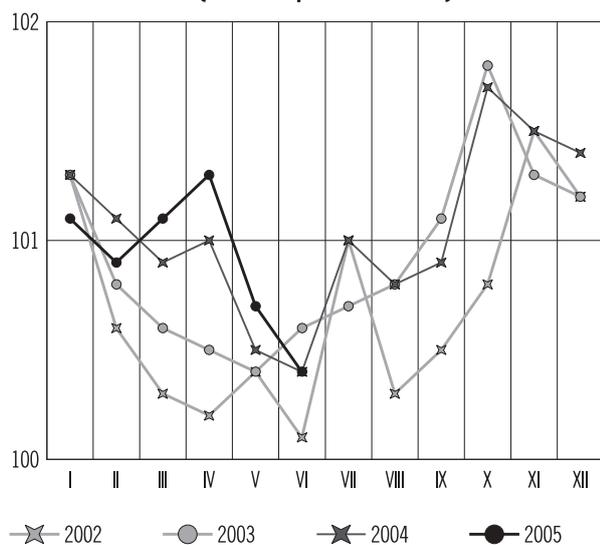
Consumer prices  
(as % of previous month)



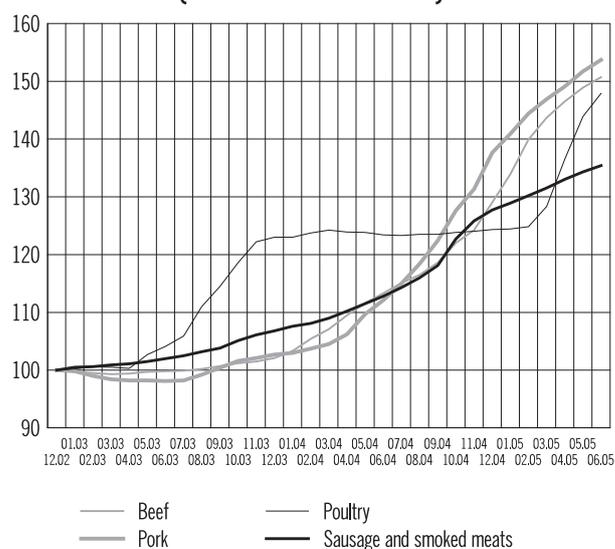
Inflation in the moving 12-month period  
(as % of corresponding month of previous year)



**Food prices, excluding vegetable and fruit prices  
(as % of previous month)**



**Meat and meat product prices  
(December 2002 = 100%)**



**Inflation rates on the consumer goods market as a whole (%)**

	Growth (June 2005 on December 2004)	Growth (June 2004 on December 2003)	Outcome
Prices of goods and services included in core inflation calculation	4.4	4.3	Some acceleration
Including:			
Food prices, excluding vegetable and fruit prices	5.5	5.2	Acceleration by 1.1 times
Non-food prices	2.4	3.4	Retardation by 1.4 times
Prices of paid services provided to households	15.4	11.0	Acceleration by 1.4 times
Including:			
Prices of goods and services regulated at federal or regional levels	19.3	13.3	Acceleration by 1.5 times
Vegetable and fruit prices	40.6	13.9	Acceleration by 2.9 times

**Food price inflation rates (%)**

	Growth (June 2005 on December 2004)	Growth (June 2004 on December 2003)	Outcome
Bread and bakery products	1.6	13.6	Retardation by 8.5 times
Cereals and legumes	-1.6	7.3	
Pasta	1.7	10.6	Retardation by 6.2 times
Meat and poultry	14.6	6.9	Acceleration by 2.1 times
Fish and seafood	10.7	2.1	Acceleration by 5.1 times
Milk and dairy products	2.7	1.6	Acceleration by 1.7 times
Butter	2.4	-0.9	
Sunflower oil	2.0	-0.8	
Granulated sugar	1.4	4.4	Retardation by 3.1 times
Alcoholic beverages	4.4	5.4	Retardation by 1.2 times

on year while the domestic poultry production expanded. The accelerated growth of meat prices affected the dynamics of fish and seafood prices. In the first half of the year, fish and seafood prices rose 10.7% (2.1% in the same period of 2004).

Year on year, the most significant slowdown in the first half of 2005 was registered in the prices of bread and bakery products (by 8.5 times) and pasta (by 6.2 times) due to the expectations of a good grain harvest this year.

The prices of cereals and legumes dropped 1.6%.

**Non-food prices** rose 2.4% in the first half of 2005 as against 3.4% in the same period of 2004. The last time non-food price growth was so small in the first half-year was registered in 1998. The prices of non-food products increased 1.1% in 2005 Q1 and 1.3% in 2005 Q2. In January-June 2005, the most significant increase in non-food prices was registered in the prices of knitwear (by 3.6%) and detergents (by 3.4%).

Petrol went up 2.6% in the first half of 2005 (14.2% in the same period last year).

The prices of knitwear, footwear, clothes and underwear grew slower than in the first half of 2004. Television and radio prices were observed to decline by 0.9%.

Estimates show that non-food price growth accounted for 0.7 percentage points, or 8.9%, of overall consumer price growth in January-June 2005 as against 0.9 percentage points, or 15.3%, in January-June 2004.

Overall, in the first half of 2005, as last year, food prices, excluding vegetable and fruit prices, grew faster than non-food prices.

**Vegetable and fruit prices** grew 40.6% in January-June 2005 or almost three times faster than in the same period of 2004 (13.9%) but this growth was below the average growth figure in the first half of 2001-2003 (47.5%). According to estimates, as a result of growth in vegetable and fruit prices in January-June 2005 headline inflation accelerated by 1.6 percentage points, or 19.5%. In January-June 2004, the contribution of vegetable and fruit price increase to consumer price growth stood at 0.7 percentage points, or 11.8%.

Consequently, the considerable growth in vegetable and fruit prices affected **food prices** as a whole: they grew 8.6% in the first half of 2005 as against 6.0% in the same period last year. Food prices increased 4.9% in 2005 Q1 and 3.5% in 2005 Q2.

**The prices of paid services provided to households** rose 15.4% in January-June 2005 (11.0% in January-June 2004). The prices of paid services grew 12.6% in 2005 Q1 and 2.6% in 2005 Q2. The most significant increase over that period was registered in rent and amenities prices (by 29.1% as against 18.6% a year ago) and pre-school tuition fees (by 21.9% as against 12.5% in the same period last year).

Growth in paid service prices in January-June 2005 was considerably faster than growth in the

Major meat and poultry market indicators (% growth)

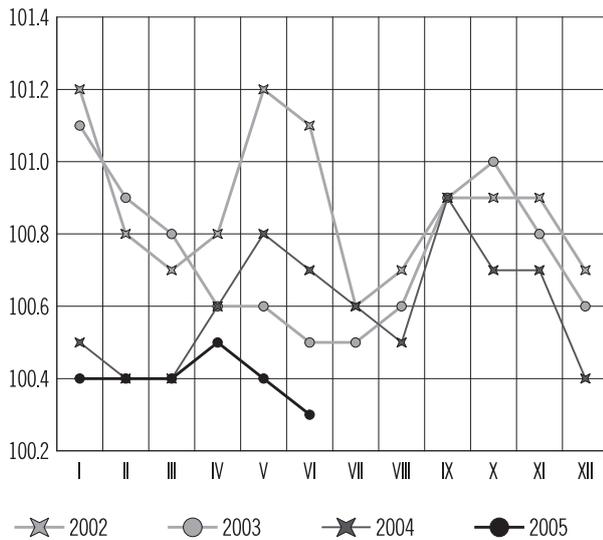
	Meat and poultry		Beef		Pork		Poultry	
	2005	2004	2005	2004	2005	2004	2005	2004
Food production (January-June as % of January-June of previous year)	1.1	10.2						
Livestock* and poultry production (January-June as % of January-June of previous year)								
- by farms of all categories	-2.2	-0.3						
- by agricultural enterprises	0.8	2.7	-12.6	-8.1	-6.5	0.1	18.2	18.5
Imports** (January-June as % of January-June of previous year)								
- volume	23.6	-21.7	22.1	3.5	3.7	-21.1	33.2	-24.7
- value	25.6	-10.4	25.9	26.7	11.2	-8.2	39.7	-22.8
Prices (June as % of December of previous year)								
- producer prices	10.4	8.8	14.7	21.2	0.0	9.2	18.0	-0.3
- livestock and poultry selling prices	13.4	10.6						
- consumer prices	14.6	6.9	16.8***	10.9***	11.7***	9.2***	18.9	0.4
- import prices**	4.1	5.0	6.2	15.2	3.3	9.3	3.9	-2.4
Livestock population* as of the end of month (June as % of June of previous year)			-7.3	-6.4	-10.1	-11.5		

\* Cattle and swine.

\*\* The estimate is based on Rosstat's figures.

\*\*\* Except boneless meat.

**Non-food prices  
(as % of previous month)**



prices of goods, which stood at 6.0%. Estimates indicate that growth in paid service prices in the first half of 2005 accounted for 3.2 percentage points, or 40.3%, of overall consumer price growth as against 1.9 percentage points, or 30.6%, in January-June 2004.

**The analysis of the distribution of increases in the prices of goods and services** in 2002-2005 (June on December of the previous year) was based on a selection of more than 400 consumer goods and services and conducted without taking account of their weight coefficients in consumer expenses.

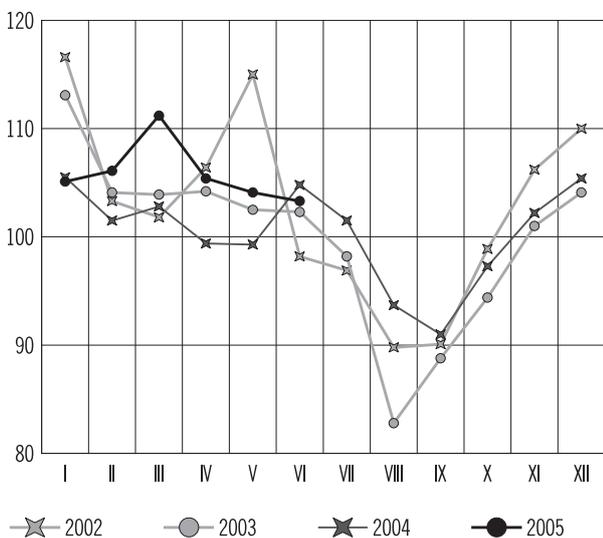
In the past four years, the prices of the bulk of consumer goods and services (over two thirds)

grew within the 0-8% range in January-June. In 2004-2005, price growth distribution was observed to slightly shift towards smaller values. In 2005, as in the previous year, major growth (45%) in the prices of goods and services was within the 0-4% range or 1.7 and 1.9 times more than in 2002 and 2003 respectively.

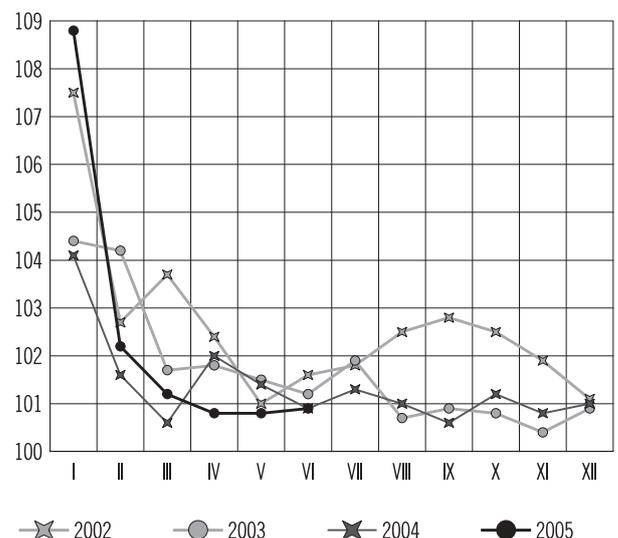
The distribution median characterising the range of growth in the prices of the bulk of goods and services was unchanged in January-June 2005 (3.8%) as compared with the same period last year. The distribution average increased by 1.2 percentage points year on year and stood at 6.4% (7.2% in the same period last year). The standard deviation, which characterises the extent of price growth difference from the average, rose to 12.4% from 6.3% a year ago and was larger than in the previous three years. This situation was attributable to a considerable increase in the share of goods and services with a high rate of price growth. It was typical for the past two years that some goods and services registered deflation.

In the first half of 2005, services registered the largest and non-food products the smallest price growth in the sample average. The median values reflecting increases in the prices of the bulk of food and non-food products did not differ significantly compared to average values. In the first half of 2005, the standard deviation for food products increased by 2.5 times year on year. The standard deviation for non-food products decreased compared to the first half of 2004 as the

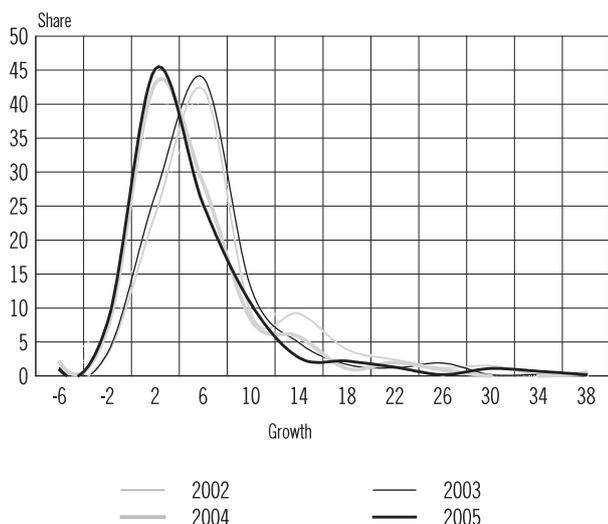
**Vegetable and fruit prices  
(as % of previous month)**



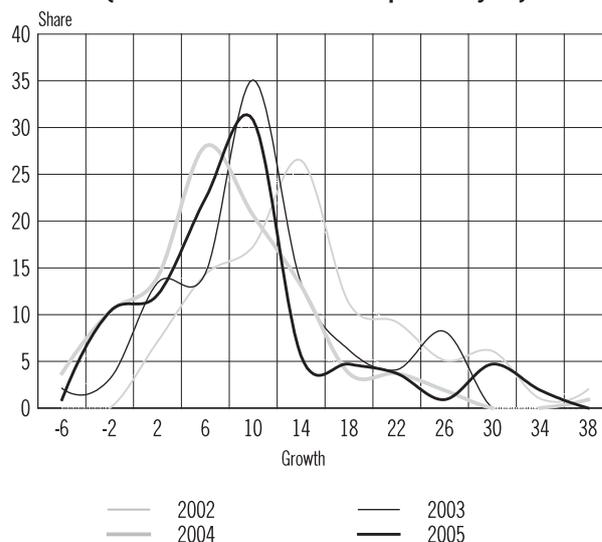
**Service prices  
(as % of previous month)**



**Consumer goods and services price growth distribution  
(June as % of December of previous year)**



**Service price growth distribution  
(June as % of December of previous year)**



price dynamics of some components of this group of goods evened out.

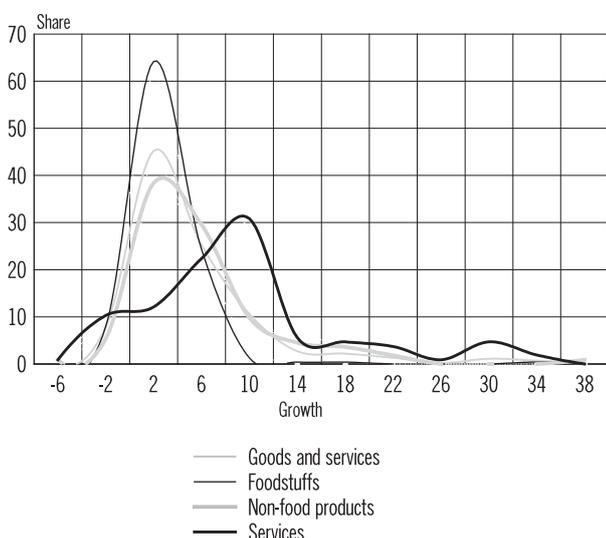
A statistical analysis of food price increases indicated that the distribution average and median values had grown in the first half of 2005 year on year. The standard deviation increased due to a considerable growth in the prices of vegetables and fruit and meat products.

The distribution of non-food price increases has a pronounced maximum and small dispersion reflecting the extent of growth deviation from the average. Consequently, the increases in the prices of most goods in this group remained within a narrow range. Thus, in the first half of 2005,

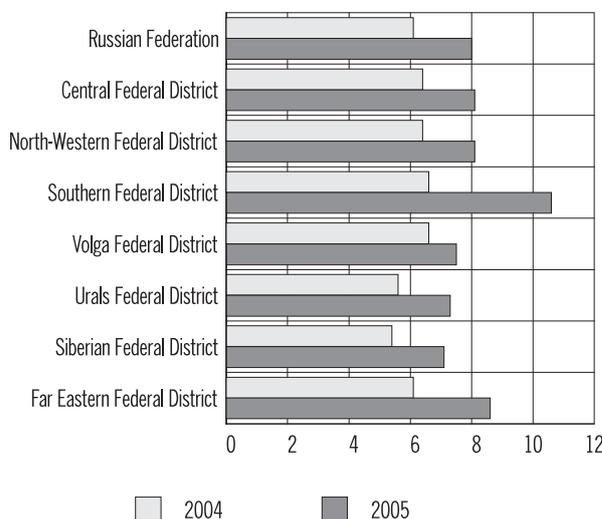
goods in the 0-8% price growth range accounted for 88.5% of all non-food products. In the same period of 2004, this price growth range accounted for 87.2% of goods.

The distribution of service price increases in the first half of 2005 was characterised by a peak corresponding to the 4-12% growth range. The range of increases in the prices of the bulk of paid services shifted towards higher price growth. In 2005, there was a relatively large share of services with the price growth of over 28%. The share of services, which registered lower prices, declined from 14% to 11% in the first half of 2005 year on year.

**Price growth distribution by kind of consumer goods and services (June 2005 as % of December of 2004)**



**Consumer price growth by federal district  
(June as % of December of previous year)**



According to Rosstat's data, in the first six months of 2005, consumer prices in **all federal districts of Russia** grew faster than last year. Consumer prices in the Central, North-Western, Southern and Far Eastern Federal Districts grew faster than in Russia as a whole by 0.1 percentage points, 0.1 points, 2.6 points and 0.6 points respectively.

According to estimates, the differences between the constituent entities of the Russian Federation with respect to the cost of a fixed set of goods and services used by the Federal Statistics Service for interregional comparisons of household purchasing power narrowed in 2004. In 2005, this tendency changed. The regional difference ratio<sup>1</sup> increased to 43.1% in the first half of 2005 from 42.6% a year ago. These dynamics are largely attributable to the fact that unlike the situation in 2004, there was no slowing of consumer price growth in the Far Eastern Federal District, which has the most expensive consumer basket.

As in 2004, vegetable and fruit prices demonstrated the most significant differences in growth rates by region in January-June 2005. Thus, vegetable and fruit prices grew 73.2% in the Southern Federal District and 18.3% in the Far Eastern Federal District. Growth in the prices of non-food products and foodstuffs, excluding vegetables and fruit, was, on the contrary, roughly the same in all federal districts.

In the first half of 2005, growth in the prices of paid services provided to households accelerated considerably in all federal districts as compared with the same period last year. The largest increase was registered in the Far Eastern and Southern Federal Districts where the prices of paid services grew by 9.4 and 8.4 percentage points respectively (in Russia as a whole, service prices rose by 4.4 percentage points).

## External Conditions

### **World Economy and International Financial Markets**

**US economic growth** continued in the first half of 2005 but it was slower than in the first half of 2004. Economic growth rates were observed

to fall in the leading developed countries, the group of new industrial countries of Asia, Latin American states, developing Asian countries (including China) and the group of Central European and Baltic states that have been the EU members since 2004. The growth of oil prices, relatively low US dollar rate and higher interest rates in the USA were the factors that restricted world economic growth in the first half of 2005.

According to preliminary estimates, US real GDP grew 3.6% in January-June 2005 year on year (4.7% in January-June 2004). Real GDP rose by an estimated 1.3% in the eurozone countries in the first half of 2005 as against 1.8% in the same period last year, by 1.3% in Japan (3.6%) and by 9.5% in China (9.7%). Fixed capital investment growth tended to slow down in these countries; in some countries (the USA and Japan), the slower growth of individual consumption also played a significant role.

The growing demand in the USA continued to considerably stimulate the economies of its trade partners. **The US trade deficit** widened by almost \$60 billion in the first half of 2005 year on year as imports grew faster than exports. In particular, the US deficit in trade with China increased by 1.3 times to almost 25% of the US total trade deficit. The growing imbalance in the US-Chinese trade adversely affected the trade balances and economies of the United States' other leading partners, including the eurozone countries and Japan. Their currencies (as compared to the yuan) appreciated considerably in nominal terms against the US dollar and made their goods less competitive.

The growth of the imports of goods into China slowed down sharply in the first half of 2005 as compared with the first half of 2004, suggesting that the increase of China's domestic demand started to play a less significant role in world economic growth. On the contrary, the accelerated growth of the imports of goods into the group of eurozone countries and Japan suggested that the rising domestic demand in these countries has a positive effect on the economies of their trade partners (in particular, regional trade partners in Europe and Asia).

<sup>1</sup> The regional difference ratio is calculated as the difference between the cost of a fixed set of goods and services in the most expensive and the cheapest regions relative to the national value of the same set.

**US inflation** equalled 2.2% in June 2005 on December 2004 (2.9% in June 2004). Food prices grew 1% (1.5% in June 2004). The slower growth was largely due to a fall in vegetable and fruit prices (by 4.9%). The prices of animal products, excluding milk and dairy products, rose 1.1% (0.7% in June 2004). In particular, poultry prices grew much faster in June 2005 on December 2004 (4.4%) than in June 2004 on December 2003 (1%); beef prices rose 3.1% (they fell 5.2% in June 2004 on December 2003). Higher prices of motor fuel were a considerable inflationary factor; however, this growth slowed down significantly (from 35.6% in June 2004 on December 2003 to 15.1% in June 2005 on December 2004). The prices of energy products used in the housing and utilities sector<sup>2</sup> increased 8% in June 2005 on December 2004 (8.8% in June 2004).

**US core inflation**<sup>3</sup> stood at 1.4% in June 2005 on December 2004 (1.5% in June 2004). The higher rent charges, which grew by an average 2.1% (2.4% in June 2004), were a decisive factor contributing to the general increase in consumer prices. Medical service charges and the prices of medicine-related goods rose by an average 2.5% (2.6% in June 2004). Lower core inflation suggests that the fundamental economic factors related to stronger consumer demand for goods and services had a less significant effect on the price growth rates in the USA from December 2004 to June 2005 than in the same period last year. The US Federal Reserve's tight monetary policy (from June 2004 to June 2005, US short-term interest rates were raised by 2.25 percentage points) helped the monetary authorities to curb inflation. Reduced core inflation and the slower growth of energy prices contributed to a lower headline inflation in the USA.

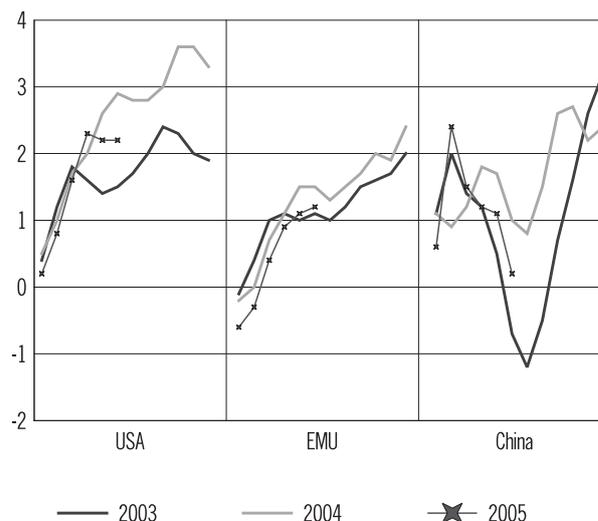
**Inflation in the eurozone countries** equalled 1.2% in June 2005 on December 2004 (1.5% in June 2004). The growth of energy prices, which rose 7.5% (5.1% in June 2004), was the principal inflationary factor in the eurozone

<sup>2</sup> Heating oil, boiler fuel, coal, town gas and electricity.

<sup>3</sup> Core inflation in the USA is understood as growth in the prices of goods and services included in the consumer goods basket, excluding foodstuffs and energy products.

<sup>4</sup> Core inflation in the eurozone countries is understood as growth in the prices of goods and services included in the consumer goods basket, excluding foodstuffs, alcoholic beverages, tobacco and energy products.

Inflation by country (%) \*

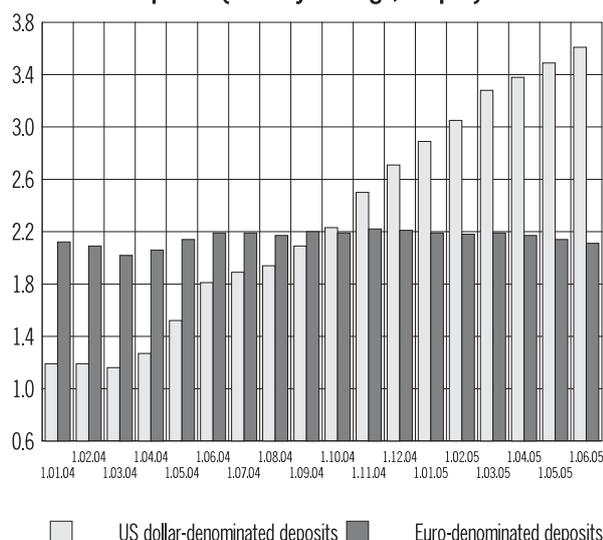


\* Consumer price growth on December of previous year.

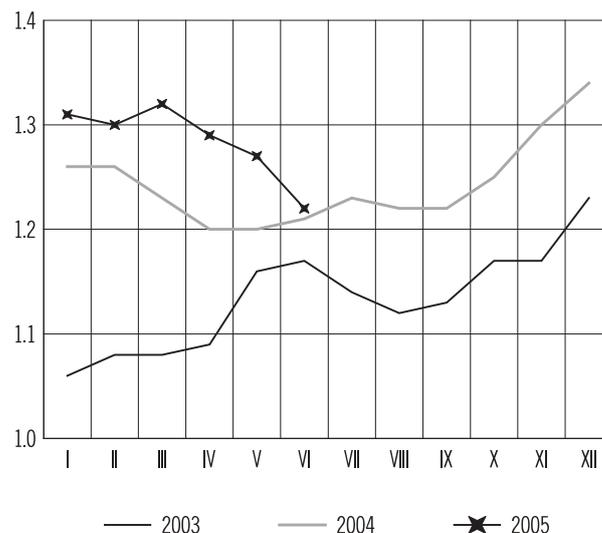
economies. In particular, the prices of fuels and lubricants for transport vehicles rose 9.1% (as in June 2004); the prices of energy products used in the housing and utilities sector grew 6% (1.8% in June 2004). The growth of food prices slowed down: they rose by an average 1.2% in June 2005 on December 2004 (1.4% in June 2004). Vegetable and fruit prices grew by an estimated 5% (4.1%), meat and meat product prices by 0.4% (0.4%).

**Core inflation in the eurozone countries**<sup>4</sup> stood at 0.4% in June 2005 on December 2004 (1% in June 2004). Therefore, fundamental economic factors had a less significant effect on the consumer price growth in December 2004-June 2005 than in December 2003-June 2004. However, market-determined factors related to the growth of energy prices restrained a fall in inflation in the eurozone countries (as compared with the USA, where the slower increase in energy product prices contributed to lower inflation). The exchange rate dynamics in the first half of 2005 did not restrict eurozone inflation (the euro depreciated against the dollar in June 2005 on December 2004, whereas year on year the euro/dollar rate was actually unchanged). Therefore, in-

**LIBOR rates on 6-month US dollar- and euro-denominated deposits (monthly average, % p.a.)**



**Euro versus US dollar (monthly average, dollars per euro)**



sufficient economic activity was the principal factor that led to lower inflation in the eurozone countries.

As for emerging market economies, which account for a considerable proportion of Russia's trade turnover, **inflation was observed to slow considerably** in June 2005 as compared with December 2004 in Belarus (4% as against 8.3% in June 2004), in Slovakia (2.5% as against 6%), in Poland (0.6% as against 3.5%), in Hungary (3.6% as against 5.2%), in Estonia (2.4% as against 4.3%) and in Latvia (4.4% as against 5.5%). Inflation in China went down to 0.2% (1% in June 2004). Inflation accelerated to 6.4% from 4.4% in June 2004 in Ukraine and to 3.7% from 2.5% in Kazakhstan.

In January-June 2005, the US Federal Reserve **raised the target for the overnight inter-bank loan rate** (federal funds rate) four times: from 2.25% to 2.5% in February, to 2.75% in March, to 3% in May and to 3.25% in June. In 2004, this target was raised by 1.25 percentage points. Since December 2004, it has exceeded the European Central Bank's refinancing rate, which has not changed since July 2003.

**The LIBOR rates on US dollar-denominated deposits** with maturities from one month to one year rose by 0.8-0.9 percentage points in June 2005 on December 2004. The yields on US treasuries rose by 0.5-0.6 percentage points for securities with maturity from two to three years, by 0.2 percentage points for papers with five-year maturity and dropped by 0.2 percentage points for

papers with ten-year maturity. The LIBOR rates on US dollar-denominated deposits with all terms and the yields on US Federal Treasury bonds with all maturities in June 2005 were higher than the LIBOR rates on euro-denominated deposits and the yields on eurozone securities.

In the first half of 2005, **the dollar appreciated against the major international reserve currencies** on foreign financial markets due to US economic growth, the increased yields on US dollar-denominated financial assets and the negative results of the EU Constitution referendums in France and the Netherlands. The dollar gained 8.9% against the euro, 4.2% against the Japanese yen and 5.5% against the British pound in June 2005 on December 2004. The dollar also rallied against **some other currencies significant for the Russian economy** (the Swiss franc, Polish zloty, Kazakh tenge, Swedish krona, Hungarian forint, Czech koruna, Slovak koruna, Lithuanian litas, Latvian lat, Estonian kroon, Romanian leu and Israeli shekel). The dollar depreciated against the Belarussian ruble, Ukrainian hryvnia, Turkish lira, South Korean won, Indian rupee and Brazilian real.

**Foreign Trade**

In the first half of 2005, the terms of Russia's trade with foreign countries continued to improve. The growth of the terms of trade index accelerated as compared with the first half of 2004 due to a considerable rise in export prices and the moderate growth of import prices.

The world prices of Russia's major export commodities<sup>5</sup> continued to grow in the first half of 2005. According to Bank of Russia estimates, the world price composite index adjusted for the structure of Russian exports and calculated for commodities that account for nearly 70% of their value equalled 1.36 on average in the first half of 2005 year on year (1.15 in the first half of 2004). The price index was 1.26 in June 2005 on December 2004 (1.13 in June 2004).

The growth of energy prices accelerated in the first half of 2005. The average price of Urals crude rose 46.1% year on year to \$45.4 per barrel (15.3% in the first half of 2004). In late June 2005, the average price of Russian oil reached its record high on the world market for the entire history of exchange trade as it grew to \$55 per barrel<sup>6</sup>. The price of Urals crude equalled \$51.1 per barrel on average in June 2005 or 42.5% higher than in December of the previous year (13.3% higher in June 2004).

The prices of natural gas and petroleum products on the European market grew at about the same rates as oil prices in the first half of 2005.

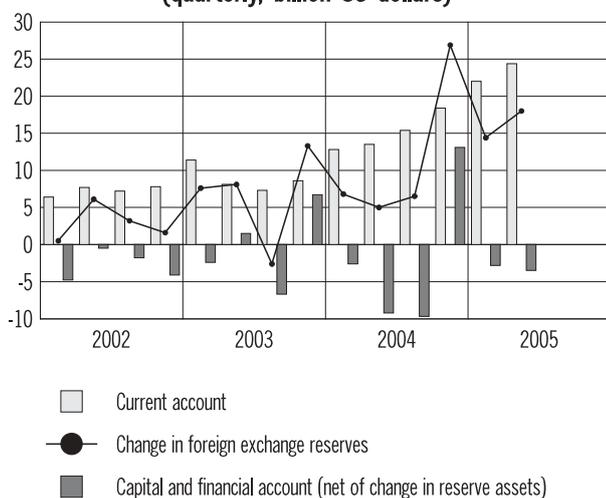
The prices of natural gas in Europe were 45% higher on average than in the first half of 2004 and the prices of petroleum products were up 45%. The price of diesel fuel rose 53%, fuel oil 37% and petrol 29%. In June 2005 as compared with December 2004, the prices of natural gas in Europe went up 18% and the prices of petroleum products increased 36% on average (the price of diesel fuel grew 28%, fuel oil 68% and petrol 14%).

The growth of world non-energy prices slowed down in the first half of 2005; however, they continued to register high growth rates. Ferrous metal prices rose 20% in the first half of 2005 year on year (52% in the first half of 2004). Non-ferrous metal prices increased 13% on average (33% in the first half of 2004). The price of aluminium rose 11% (20%), copper 21% (67%) and nickel 17% (63%). Ferrous metal prices grew 11% on average in June 2005 on December 2004 (54% in June 2004) and non-ferrous metal prices went up 1.7% (1.2%).

Food prices<sup>7</sup> remained high on world markets in the first half of 2005. The prices of beef went up 11.7% and pork 5.1% in January-June 2005 year on year. Poultry prices actually remained at the same level; the price of refined sugar rose 15.9% and raw sugar 33.1%. Meat and sugar prices tended to grow slower in the first half of 2005. The prices of beef rose 2.5% in June 2005 as compared with December 2004 (9.8% in June 2004) and poultry 1.2% (15.4%). Pork prices went down 6.5% in June 2005 on December 2004 (they rose 61% in June 2004). The price of refined sugar grew 12.2% over that period (16.7%) and raw sugar 3.6% (15.3%).

As the foreign trade situation continued to improve, Russia's **balance of payments** remained stable in the first half of the year. According to preliminary estimates, it was characterised by the following data.

Major balance of payments components  
(quarterly, billion US dollars)



\* 2005 Q2: estimate.

<sup>5</sup> Average prices are calculated on the basis of data provided daily by Reuters for oil, Petroleum Argus for petroleum products (petrol, diesel fuel and fuel oil), the London Metal Exchange for non-ferrous metals (aluminium, copper and nickel), the World Bank for average monthly prices of natural gas and ferrous metal price indices; prices of other commodities are based on data from the International Monetary Fund.

<sup>6</sup> Closing price of June 27, 2005 according to data provided by Reuters.

<sup>7</sup> The average prices of raw and granulated sugar are calculated on the basis of data provided daily by the London Commodity Exchange; the average monthly prices of beef, mutton, oranges and bananas are based on data from the World Bank; the prices of other commodities are based on data from the International Monetary Fund.

The current account surplus was estimated at \$46.4 billion in the first half of 2005 (\$26.3 billion in the same period last year) and trade surplus at \$58.9 billion or 1.5 times higher than in the first half of 2004. The exports of commodities increased 40% to \$112.5 billion, including the value of exported fuel and energy products (oil, petroleum products and natural gas), which rose by 1.5 times. The imports of goods totalled an estimated \$53.6 billion or 27% more than in the first half of 2004.

The deficit of operations with international services rose to an estimated \$6.2 billion (\$5.7 billion in the first half of 2004). As before, the growing deficit was attributable to a faster growth in the imports of services (they expanded to \$16.6 billion) than in their exports (they rose to \$10.4 billion).

The deficit of the balance of investment incomes narrowed from \$5.7 billion in the first half of 2004 to \$5.3 billion in the first half of 2005.

Residents' foreign liabilities increased by \$23.0 billion in the first half of 2005 as against \$13.2 billion in the same period last year. The liabilities of government sector and monetary authorities contracted by \$3.4 billion, while the liabilities of the private sector, which actively attracted foreign capital, expanded by \$26.4 billion. Credits and loans (\$11.9 billion) and also direct investments (\$9.3 billion) were the major forms to attract foreign capital to the sector of non-financial enterprises in the first half of 2005. Capital in the form of credits and loans accounted for 50% of foreign investment to the non-financial enterprise sector (56% in the first half of 2004) and capital in the form of foreign direct investment accounted for 39% (31% a year ago).

The intensified foreign capital inflow to the private sector was attributable to the improvement of investment climate in Russia, which did not pass unnoticed by international rating agencies. In January 2005, the international rating agency Standard & Poor's raised Russia's rating to the investment grade (Moody's Investors Service and Fitch Ratings raised Russia's rating to the investment grade in 2003 and 2004).

Accounting foreign assets (net of foreign exchange reserves) rose by \$29.1 billion in the first half of 2005 largely due to transactions of the private sector whose assets expanded by \$24.2 bil-

lion. Capital outflow from the banking sector stood at \$9.4 billion (\$5.9 billion in the first half of 2004), while capital outflow from the sector of non-financial enterprises and households totalled \$14.8 billion as against \$14.9 billion in the first half of 2004. Capital outflow from the government sector and monetary authorities increased to \$4.8 billion (\$2.2 billion in the first half of 2004).

The private sector's net capital outflow contracted considerably, from \$10.3 billion in the first half of 2004 to \$5.7 billion in the first half of 2005. Net capital outflow from the banking sector in the first half of 2005 was estimated actually at the level of the first half of 2004 (\$6.6 billion). Net capital outflow of \$3.9 billion from the sector of non-financial enterprises and households in the first half of 2004 gave way to its net inflow of \$0.9 billion in the first half of 2005.

The inflow of foreign currency into the country considerably exceeded demand for foreign exchange from businesses and led to an increase in Russia's international reserve assets. As of July 1, 2005, Russia's international reserves totalled \$151.6 billion and expanded by \$27.0 billion from the start of 2005 (in the first six months of 2004, they grew by \$11.3 billion). Their accrued amount would be enough to finance the imports of goods and services during 13 months (9.3 months in the first half of 2004).

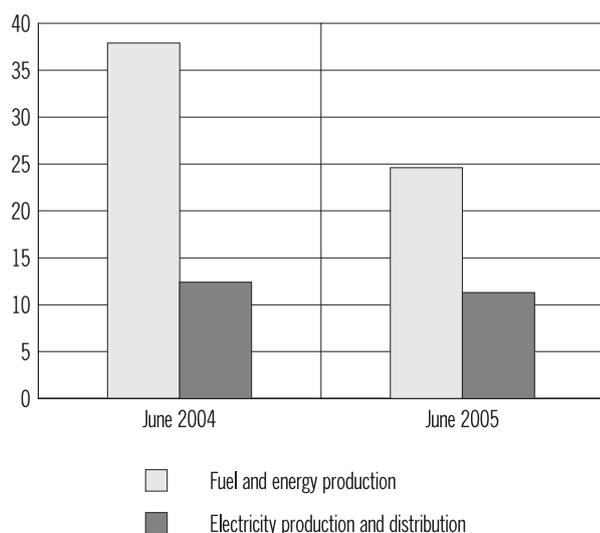
Russia's foreign debt was estimated at \$221.4 billion as of April 1, 2005 and rose by 2.9% (\$6.3 billion) as compared with January 1, 2005. The government and monetary authorities reduced their foreign debt by 4.5% (\$4.8 billion) whereas the private sector's debt rose by 10.2% (\$11.2 billion) largely due to an increase in the liabilities of the non-financial enterprise sector.

## Internal Conditions

Industrial production expanded 4.0% in the first half of 2005 (7.3% in the first half of 2004). The slowing of industrial output growth over that period was due to the year-on-year slowdown of production growth in the manufacturing sector (from 8.5% to 5.6%) and in mining (from 8.2% to 1.4%).

Agricultural output increased 0.2% in January-June 2005 year on year (it fell 1.2% in January-June 2004).

**Producer prices by type of activity**  
(growth as % of December of previous year)



Freight transport's turnover expanded 2.8% in January-June 2005 as compared with the same period last year (growth in 2004 stood at 7.4%). The freight turnover of railway transport increased 2.5%, automobile transport 9.6% and pipeline transport 3.1%.

In January-June 2005, household real disposable money income grew 8.3% year on year (8.9% in January-June 2004).

As was the case in the first half of 2004, consumer expenses tended to grow faster than household real money income in the first half of 2005. Amid the increased public propensity for consumption and the reduced share of expenses

on savings, this trend suggested insufficient living standards. Thus, according to an estimate, consumer spending increased 9.9% in real terms in January-June 2005 year on year or 0.8 percentage points less than in January-June 2004. Growing consumer demand contributed to price growth.

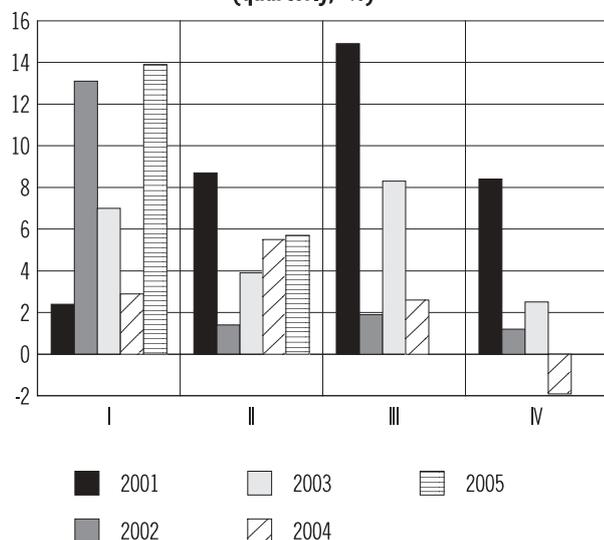
Despite the growth of household money income, the share of expenses on the purchase of goods and services continued to be considerable. Thus, according to preliminary data, this share was 72.5% in the first half of 2005 as against 70.6% in the same period last year. The share of expenses on services rose to 17.4% from 16.6% in the first half of 2004. The relatively high rates of growth in the prices of paid services provided to households contributed to the increase of this share.

The conditions stimulating corporate investment activity remained in the first half of 2005. The value of fixed capital investment rose 9.4% in January-June 2005 year on year (12.6% in January-June 2004).

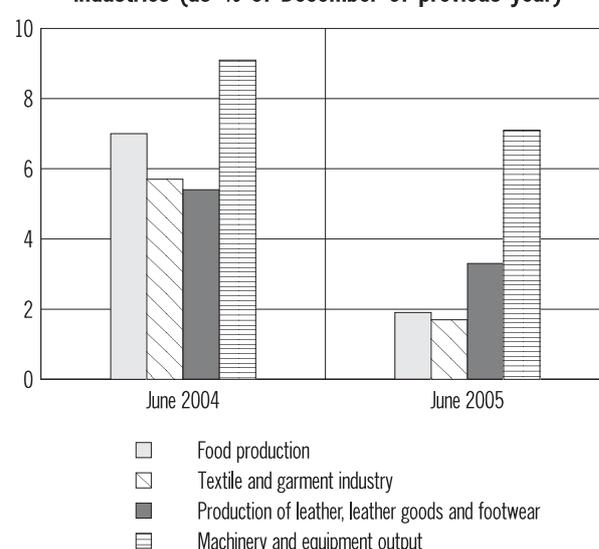
The situation on the labour market improved in the first half of 2005 as compared with the same period last year. Employment stood at 92.1% of the economically active population, while 7.9% were classified as unemployed according to ILO methodology (91.5% and 8.5% respectively in the first half of 2004).

Inflation was affected by price dynamics in industries whose output goes directly to the consumer goods market. According to estimates, pro-

**Growth in freight transportation charges**  
(quarterly, %)



**Producer price growth in some manufacturing industries**  
(as % of December of previous year)



ducer price growth in these industries accounted for 1.3 percentage points of growth in the prices of goods and services included in the core inflation calculation in January-June 2005 (3.1 percentage points in January-June 2004).

In the first half of 2005, the pressure put on consumer prices by costs (especially the costs of material resources) was less significant than in the first half of 2004. In particular, the increase in the mining price growth slowed down. Mining prices rose 22.5% in June 2005 on December 2004 (34.5% in June 2004) despite the rise in oil prices and the increase in basic tax rates for oil and gas production from January 1, 2005. However, as last year, producer prices in the mining sector grew faster than in the manufacturing industries. Manufacturing producer prices grew 5.3% as against 12.3% in June 2004.

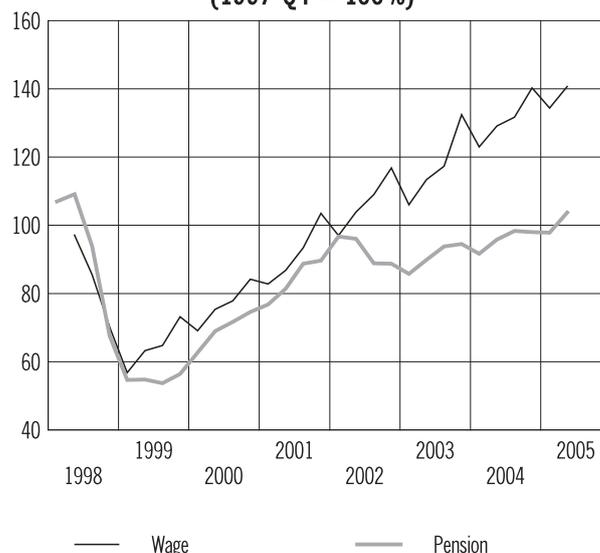
The prices of the production and distribution of electricity, gas and water grew 12.2% in June 2005 on December 2004 or by 0.1% slower than in the same period last year.

Freight transportation charges rose 20.3% in the first half of 2005 (8.5% in the same period of 2004). Railway transport fares increased 8.8% as against 12.6% in the same period last year.

According to Rosstat's updated figures, in January-May 2005, the growth rate in profit net of loss of companies in the mining sector stood at 177.6%, in manufacturing industries 125.6% and in the production and distribution of electricity, gas and water 118.7%.

At the same time, competition, including one put up by importers, continued to affect price formation in the manufacturing sector oriented to consumer demand. Thus, producer prices in the production of foodstuffs (including beverages) and tobacco, textiles and clothing, leather, leather goods and footwear grew slower in January-June 2005 than in the manufacturing sector as a whole. In the first half of 2005, output in the textile and garment industry and the production of leather, leather goods and footwear was smaller than in the same period last year. According to Rosstat's data, in January-April 2005, profits (profit net of loss) of companies producing foodstuffs (including beverages) and tobacco contracted by 1.2 times year on year and profits of companies manufacturing leather, leather goods and footwear fell by 3.4 times. The textile and garment

**Real wage and real pension  
(1997 Q4 = 100%)**



industry operated at a loss unlike the situation in January-April 2004.

The growth of prices in some manufacturing industries, whose output goes to the consumer goods market, did not accelerate in the first half of 2005 as compared with the same period last year. Thus, the growth of producer prices slowed down from 7.0% in January-June 2004 to 1.9% in January-June 2005 in the food industry, from 5.7% to 1.7% in the textile and garment industry and from 5.4% to 3.3% in the production of leather, leather goods and footwear.

The growth of nominal and real wage, typical of the past two years, continued in 2005. This growth was facilitated by the increase of the minimum pay from 600 rubles to 720 rubles from January 1, 2005. According to preliminary data, the average monthly nominal imputed wage stood at 7,943 rubles in January-June 2005, an increase of 8% in real terms (14.2% in January-June 2004).

The average monthly pension was 2,225 rubles in January-June 2005, according to preliminary estimates, a 7.4% increase in real terms year on year (6.8% in January-June 2004). Pensions grew as their basic part increased by 240 rubles from March 1, 2005 to 900 rubles.

According to data of the Institute for the Economy in Transition, the inflationary expectations of managers of leading industrial enterprises were somewhat lower on average in the first half of 2005 than in the same period last year. Thus, in January-June 2005, 22-38% of respondents ex-

pected selling prices to grow as against 31-40% in the first half of 2004. In January-June 2005, a trend towards lower inflationary expectations was observed (from 38% in January to 19% in June) as prices mostly grew in the first months of 2005 and most producers do not expect the prices of their products to rise in the near future. It is sig-

nificant that in the past twelve months, enterprises expected the most significant growth of their selling prices in December 2004 (40% of respondents, according to data of the Institute for the Economy in Transition). High inflationary expectations preceded a considerable price leap in January-March 2005.



## Quantitative and Qualitative Monetary Indicators

### Exchange Rate

The situation on the domestic forex market in 2005 Q2 was characterised by the continued dollar's strengthening against the ruble. Despite a considerable inflow of foreign currency earnings to the Russian market amid the favourable foreign economic conditions, exchange rates were especially influenced by the expectations of the dollar's appreciation against the euro on international markets.

These trends caused the Bank of Russia to reduce its ruble interventions on the forex market in May-June and this contributed to slower growth in money supply.

The bi-currency basket introduced by the Bank of Russia in February 2005 as the target of its exchange rate policy continued to contribute to lower speculative activity of forex market players in 2005 Q2. Considering the rising role of the euro in trade turnover, the Bank of Russia changed the structure of its bi-currency basket from May 16, 2005. The euro share went up to 30% and the dollar share went down to 70%.

After the dollar's considerable appreciation against the ruble at the end of Q1, its changes in April were insignificant. However, the expectations of forex market players were linked with the dollar's further growth amid favourable economic

news coming from the USA. The average monthly dollar/ruble rate stood at 27.82 rubles to the dollar, an increase of 0.7% as compared with March.

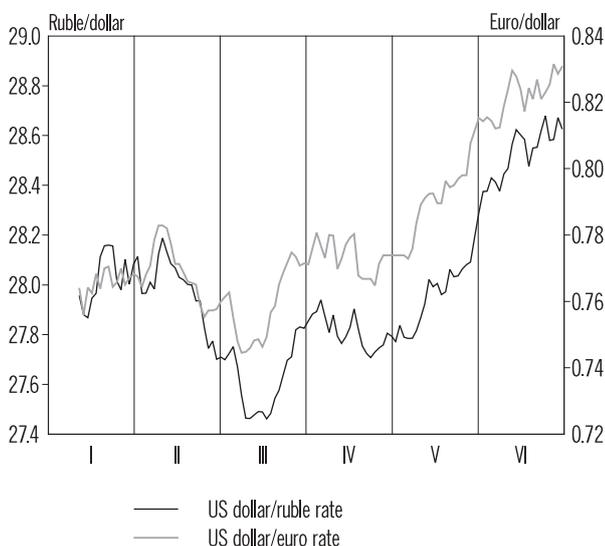
Political debates in EU countries influenced considerably the sentiments of market players in 2005 Q2. In May-June, these debates prompted the accelerated appreciation of the dollar against the euro and, therefore, against the ruble. In May 2005, the average monthly dollar/ruble rate was 27.92 rubles to the dollar, an increase of 0.4%. In June, the US currency gained more considerably (2%) and the average monthly dollar/ruble rate equalled 28.50 rubles to the dollar.

As a result, the dollar appreciated noticeably against the ruble in Q2 (0.9%). The average quarterly dollar/ruble rate was 28.08 rubles to the dollar.

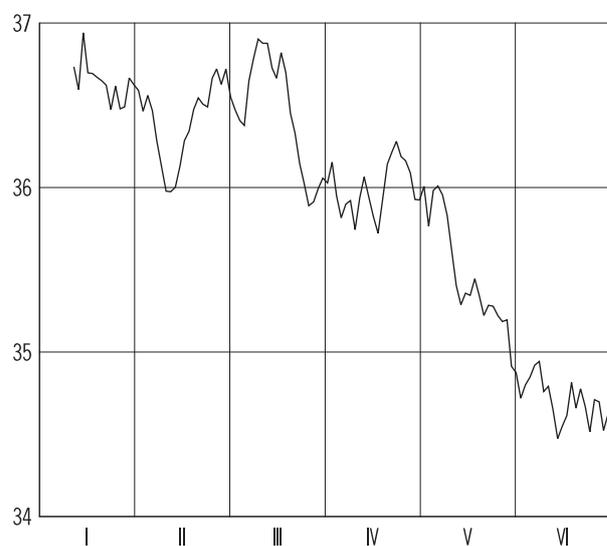
The European currency registered downward dynamics in Q2: the average euro rate dropped 3.3% to 35.42 rubles to the euro. The average monthly euro/ruble rate depreciated 1.4% in April month on month and 1.2% in May. In June, the weakening of the European currency accelerated to 2.4%.

In 2005 Q2, the ruble's real effective rate appreciated 3.7% against foreign currencies (7.7% since the start of the year). The ruble's real rate gained 1% against the dollar (4.3% since the start

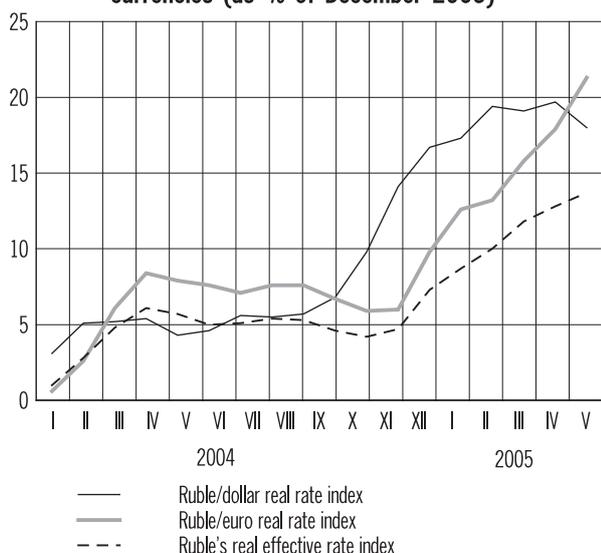
**US dollar/ruble and US dollar/euro rate  
in the first half of 2005**



**Euro/ruble nominal rate  
in the first half of 2005**



**Ruble's real and real effective rate indices against foreign currencies (as % of December 2003)**



of the year) and 5.8% against the euro (11.7% since the start of the year).

In 2005 Q2, as the Bank of Russia conducted its operations on the forex market and took measures to smooth over the dollar's sharp fluctuations against the ruble, Russia's international reserve assets grew by \$14.2 billion or 10.3% as compared with 2005 Q1. The largest growth was registered in April (by 5% month on month), when international reserve assets increased by \$6.9 billion. They grew by \$3.1 billion (2.2%) in May and by \$4.2 billion (2.9%) in June. The growth of international reserves slowed down in May-June as the Bank of Russia reduced the amount of its ruble interventions on the domestic forex market during the period of the dollar's appreciation against the ruble. Since the beginning of the year, Russia's international reserve assets have expanded by more than \$27 billion or 21.7%.

### Interest Rates

The average price level of short-term funds determined by the Bank of Russia interest rate band slightly increased in 2005 Q2 as compared with the previous quarter. Commercial banks' ruble liquidity declined and the ruble's nominal rate against the dollar weakened in 2005 Q2. As a result, financial market players were less interested in investing in ruble-denominated assets. As inflation ran at fairly rapid rates in April-May, there was no single trend in interest rate dynamics and the volumes of operations in the major segments of the financial market.

The Bank of Russia made no changes in interest rates on the deposit operations conducted on standard terms in 2005 Q2. The interest rate on tom-next deposits accounting for the largest share of credit institutions' funds placed on deposit shaped the lower limit of the interest rate band (it equalled 0.5% p.a.). The Bank of Russia overnight loan rate, the upper limit of the band, remained also unchanged at 13% p.a. The average-weighted interest rates on deposit auctions were slightly higher in 2005 Q2 quarter on quarter at 2.0% p.a. on 4-week deposits and 3.4% p.a. on 3-month deposits. The average-weighted yield on Bank of Russia bonds (OBR), which were used to attract banks' funds, ranged from 3.5% p.a. to 4.36% p.a.

The average rate on repo operations as the major market instrument of liquidity provision equalled 6.3% in 2005 Q2.

Money market interest rates and rates on commercial banks' operations were within the Bank of Russia interest rate band in 2005 Q2. As the banking sector's liquidity declined, the volatility and the average level of short-term interbank loan rates increased. The MIACR on overnight ruble loans ranged from 0.8% p.a. to 9.7% p.a. in April-June (from 0.65% p.a. to 2.0% p.a. in the previous quarter).

The market interest rate on loans extended to non-financial enterprises with all maturities dropped by 0.3 percentage points in April month on month to 10.4% p.a. In the subsequent months, this interest rate was observed to rise and stood at 11.2% p.a. in June. As for the structure of interest rates by maturity, loans with a maturity of 6 to 12 months were the most expensive credit resources for enterprises in April-May 2005 and in June it was loans extended for 1 to 3 years. The price of loans with all maturities rose by an average 0.03 percentage points in 2005 Q2 quarter on quarter, while the price of 6 to 12-month loans and 1 to 3-year loans dropped by 0.06 and 1.59 percentage points respectively.

The growing demand for loans from households, along with high cost of consumer lending and easier competition, enables banks to keep interest rates on loans to individuals higher than on loans to enterprises. In June, the interest rates on loans to households with all maturities dropped to 19.6% p.a. from 20.0% p.a. in March. As com-

Rates on Bank of Russia operations and overnight MIACR (%)



pared with Q1, the average interest rate on loans to households with all maturities dropped by 0.2 percentage points in Q2 to 19.7% p.a. The largest decline was registered in interest rates on 1 to 3-year loans (by 0.6 percentage points to 19.8% p.a.).

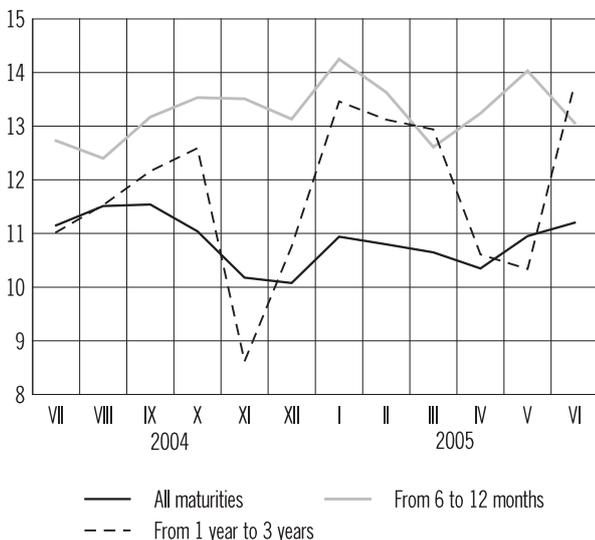
The interest rate on household time deposits rose by 0.23 percentage points in May-June but was lower than in March. The average interest rate on household time deposits was 8.2% p.a. in 2005 Q2 or 0.7 percentage points less than in 2005 Q1. As in the previous quarter, deposits for a term of 6 to 12 months registered the highest interest rates in 2005 Q2, while their average quarterly values

fell by 0.4 percentage points. As compared with Q1, deposits for a term of 8-30 days registered the largest fall of average quarterly rates (by 2.8 percentage points) in Q2.

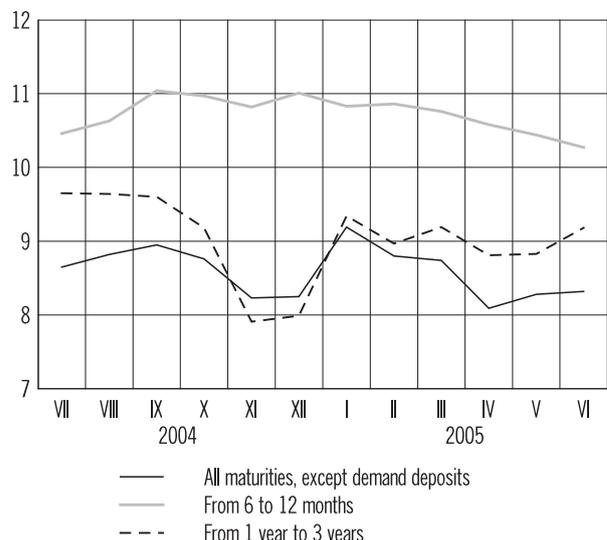
The yield curve on banks' lending operations retained its rising slope in 2005 Q2. The curve's positive incline in the up to 90 days sector slightly narrowed and increased for terms of over 3 years. The term structure of interest rates on banks' lending operations shows that market participants' inflationary expectations remain moderate.

A weak downward yield trend prevailed on the OFZ bond market from April to the first ten-day period of May. From this period and up to the

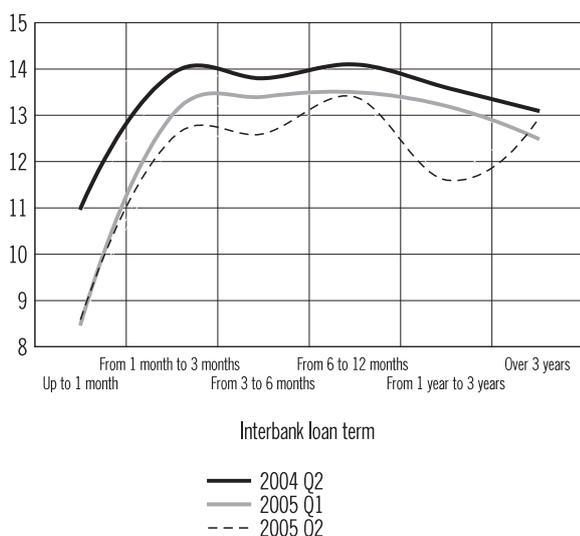
Interest rates on ruble loans to non-financial enterprises (% p.a.)



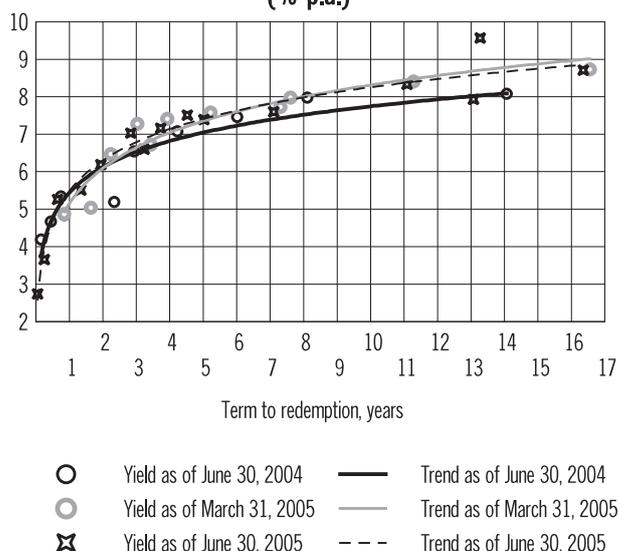
Interest rates on household ruble deposits (% p.a.)



**Bank lending yield curve  
(loans to corporate borrowers, % p.a.)**



**GKO-OFZ effective yield curve  
(% p.a.)**

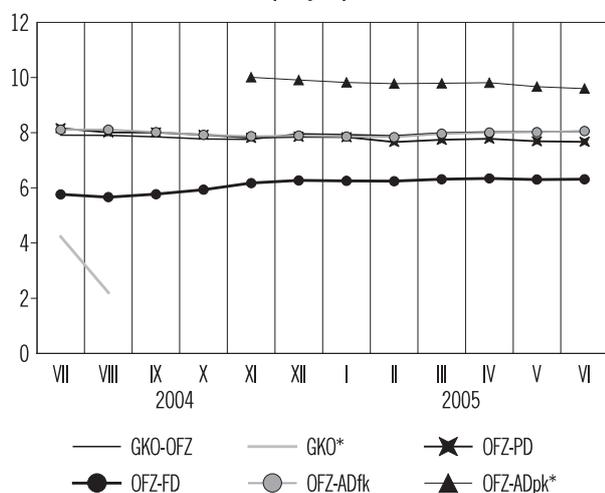


last week of June, a weak upward yield trend was registered. The yields of OFZ bonds fluctuated within the range of 0.17 percentage points in April-June. The effective indicator of the government bond market portfolio dropped by 0.02 percentage points by the end of the period as compared with the end of March to 8.02% p.a. As compared with Q1, the average quarterly effective indicator of the market portfolio rose in Q2 by 0.1 percentage points to 8.04% p.a.

The government bond yield curve kept its normal shape in the reporting period. A slight increase in yields in Q2 caused the curve to move slightly upwards. The rising slope of the yield curve

extended to the up to 11 years section in the reporting period (it was limited to the 8 years section in Q1). The OFZ bond yield curve deviated noticeably from the flattened line in the over 11 years section due to debt depreciation of these issues (their yields are directly proportional to duration instead of their term to redemption). The yield curve slope fluctuations were insignificant in April-June. No inflation risk premium was included in the prices of short-term government bonds. The medium- and long-term inflationary expectations of market players were unchanged from the previous quarter. The risk of investing in papers with terms to redemption longer than five years was determined by market players by evaluating the risk involved in investing in medium-term issues. Investors kept their assessments of the reliability and liquidity of ruble-denominated government bonds for all terms.

**GKO-OFZ portfolio average monthly yield  
(% p.a.)**



\* GKO bonds were redeemed in August 2004, OFZ-ADpk bonds were floated in November 2004.

In 2005 Q2, the interest rate structure by instrument remained balanced enough. The yield curves of key financial instruments had a normal shape suggesting that the yield on financial instruments was in direct proportion to their maturity periods amid stable short- and medium-term inflationary expectations of Russian financial market players.

Long-term inflationary expectations cannot be evaluated accurately owing to the small scale of operations with long-term financial instruments. In 2005 Q2, the yield curve of the various longest-term instruments changed its negative

slope for the rising slope. This testifies to differentiated medium- and long-term price expectations.

### Money Supply

In 2005 Q2, annualised M2 growth increased to 33.6% from 30.8% as of April 1, 2005. In April-June 2005, the M2 growth was seasonally faster than in the first quarter and equalled 10.1%. This growth exceeded the M2 increase in the same period last year but was slightly lower than the second-quarter average growth since 1999.

In March 2005, the trend towards the lower annualised growth in money supply gave way to the opposite one. Annualised M2 growth registered as of July 1, 2004 continued in the short-term perspective and slightly exceeded demand for ruble supply projected for 2005 (28-32%). At the same time, the long-term trajectory of money supply growth continued to have a descending slope (40.4% as of July 1, 2004). With the continued seasonal specifics of money supply dynamics and the budget's considerable role in liquidity sterilisation, the M2 growth may slow down at the end of 2005 Q3.

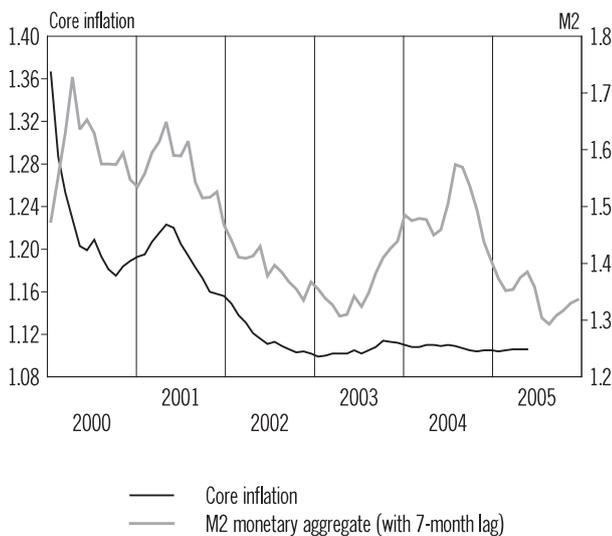
Unstable demand for the domestic currency that determines the M2 dynamics brings about an additional factor of uncertainty in assessing core inflation in late 2005 and early 2006.

The gap between M2 and GDP growth rates<sup>1</sup>, which sharply narrowed in the previous year, was actually unchanged in 2005 Q2 as compared with the first quarter. The dynamics of money velocity are essential to evaluate the influence of this gap on inflation. In 2005 Q2, money velocity fell 2% (3.7% in 2004 Q2). Therefore, the slowing of fall in money velocity observed from the second quarter of 2004 continued, and some factors, especially unstable demand for the domestic currency, the slowing of the process of de-dollarisation and money supply structural changes caused the dynamics of money velocity to deviate from the medium-term trend. This can be interpreted as increased inflationary pressure, given that the annualised money supply growth stays at the current level.

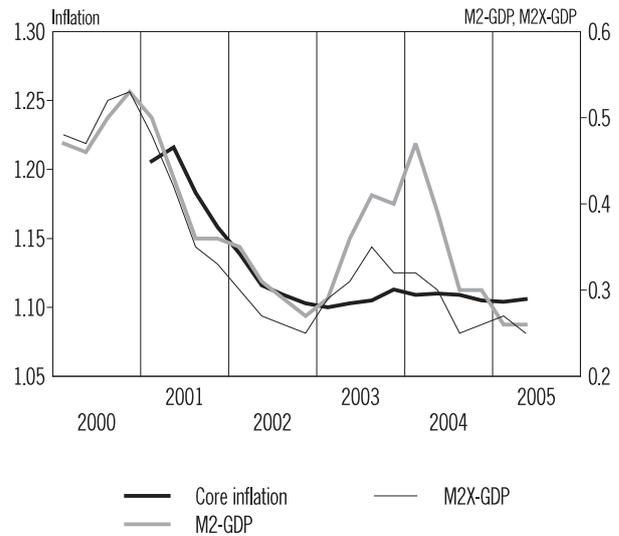
The gap between the growth rates of GDP and the broader monetary aggregate M2X comprising economic agents' foreign currency non-cash funds insignificantly narrowed in 2005 Q2. Since 2003, the M2-GDP and M2X-GDP trajectories were similar but the M2X-GDP gap was at a lower level.

The money aggregate in the monetary survey definition (similar to the M1 aggregate), which includes the most liquid transactional components of money supply, reflects economic conditions and liquidity preferences. In 2005 Q2, its dynamics were mainly affected by the accelerated

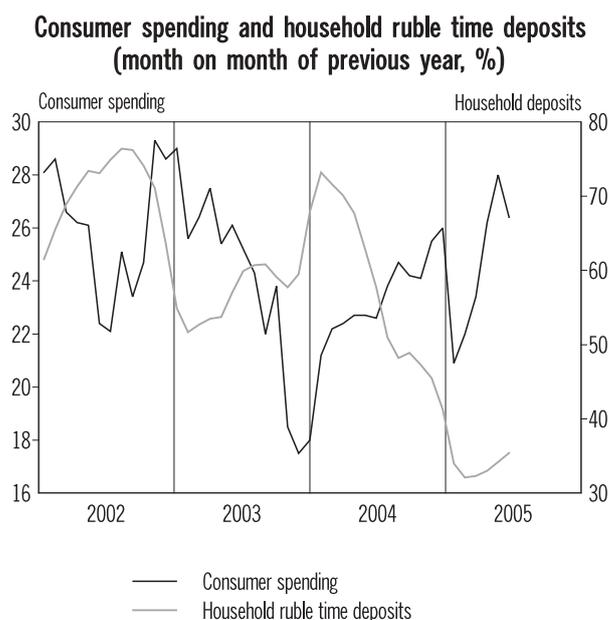
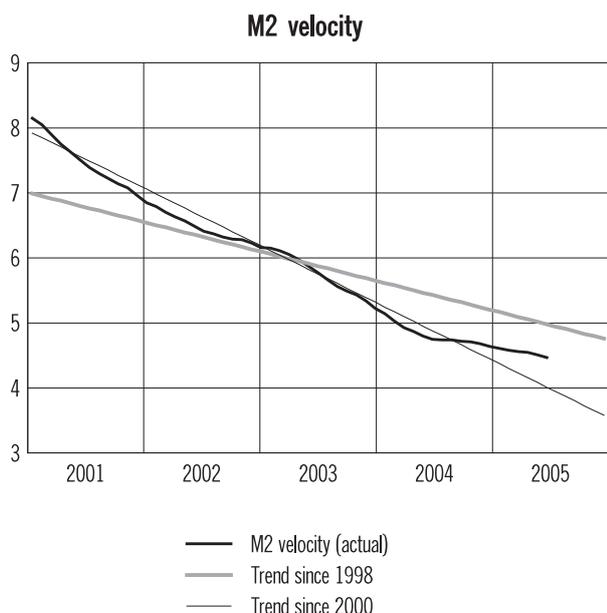
**Core inflation and M2 (month on month of previous year)**



**Core inflation and gap between money supply and GDP growth rates (quarter on quarter of previous year)**



<sup>1</sup> This gap characterises the part of monetary growth that exceeds the amount necessary to finance the expanded volume of transactions. Its increase can testify to the inflationary pressure of money supply growth on price dynamics.



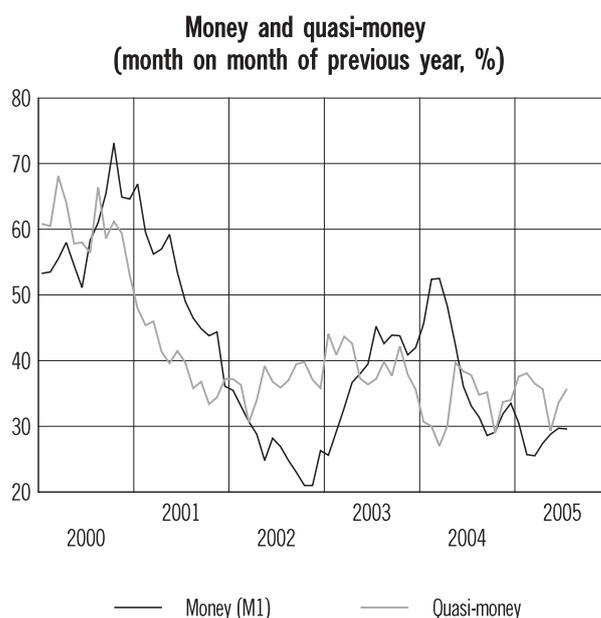
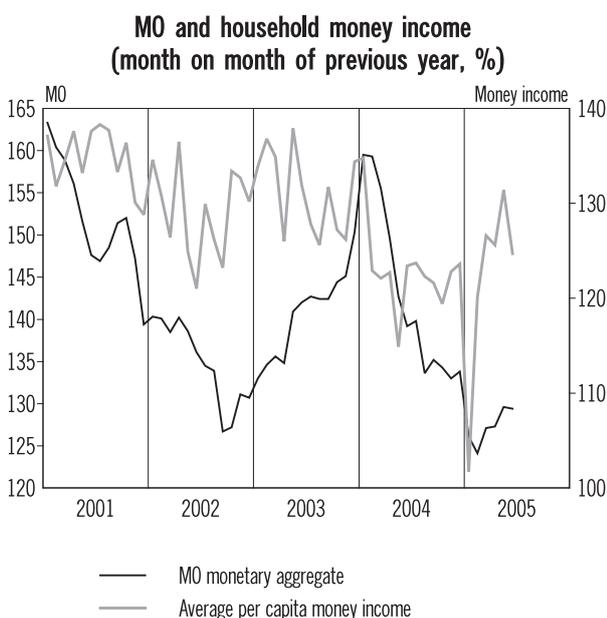
growth of the aggregate's cash component (M0 cash growth increased from an annualised 27.1% to 29.4% in April-June 2005 and was lower than in the same period last year).

Following seasonal trends, cash grew more considerably in 2005 Q2 (11.4%) as compared with 2005 Q1 and this growth was faster than in the second quarter of the previous year (9.5%). The M0 dynamics in 2005 Q2 were especially affected by the fluctuations of household demand for foreign currency cash and dynamics of household real money income.

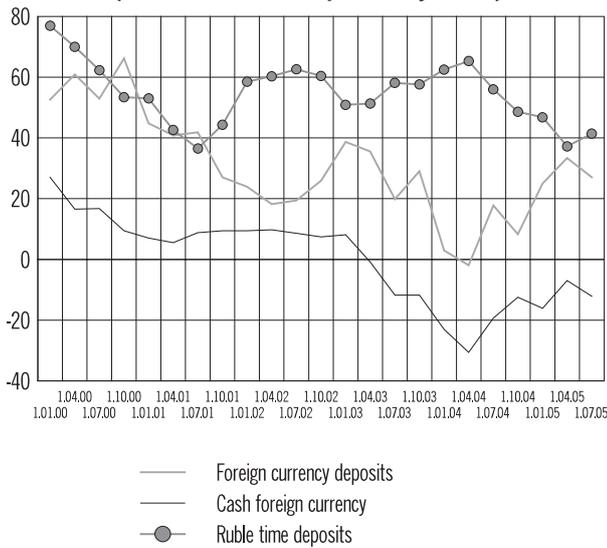
The M1 non-cash component is comprised by about 80% of non-financial enterprise sector

funds and its increase reflects economic agents' rising demand for money to conduct transactions and service the payment turnover. The annualised rates of growth (month on month of previous year) in non-cash transaction money slightly increased, from 27.8% to 29.8%, and were higher than in the same period last year.

As cash and funds in transactional accounts somewhat accelerated, the rates of growth in the money aggregate in the monetary survey definition grew from an annualised 27.4% as of April 1, 2005 to 29.6% as of July 1, 2005. The rates of growth in quasi-money (the aggregate comprising less liquid components of the money supply



**Individual components of notional broad M2Y aggregate  
(month on month of previous year, %)**



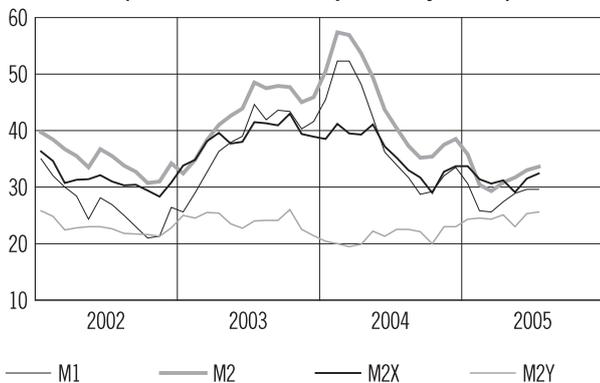
used by economic agents as savings) were slightly slower in 2005 Q2 than in the same period last year but considerably faster than the rates of growth in the money aggregate. The quasi-money dynamics that emerged by the beginning of July (the annualised growth rates remained at the level of the beginning of Q2, equalling about 35% as against 37.6% at the beginning of 2005) were determined by the faster growth in time deposits representing the ruble component of quasi-money. In April-June, the annualised rates of growth in time deposits accelerated by 4.2 percentage points to 41.4% but failed to exceed the growth rates as of the beginning of the year and

as of the same date in 2004. The rates of growth in foreign currency deposits representing the other component of quasi-money slowed as compared with Q1 and were also slower than in April-June last year. In 2005 Q2, the trend towards acceleration in the annualised rates of growth in foreign currency deposits, observed in the previous year, came to a halt and cannot be interpreted unambiguously.

Economic agents' unsteady currency preferences and the respective change in demand for the national currency and foreign exchange causing the reciprocal flow of ruble and foreign currency funds were among the factors that determined the monetary aggregate dynamics in 2005 Q2. The rates of growth in the ruble monetary aggregates (M0, M1 and M2) accelerated more considerably as compared with the dynamics of the M2X and M2Y aggregates, which include non-financial agents' foreign currency assets. Thus, the rates of growth in M2X increased from an annualised 31.2% as of April 1, 2005 to 32.4% as of July 1, 2005, while the rates of growth in M2Y accelerated by 0.5 percentage points in annual terms in April-June.

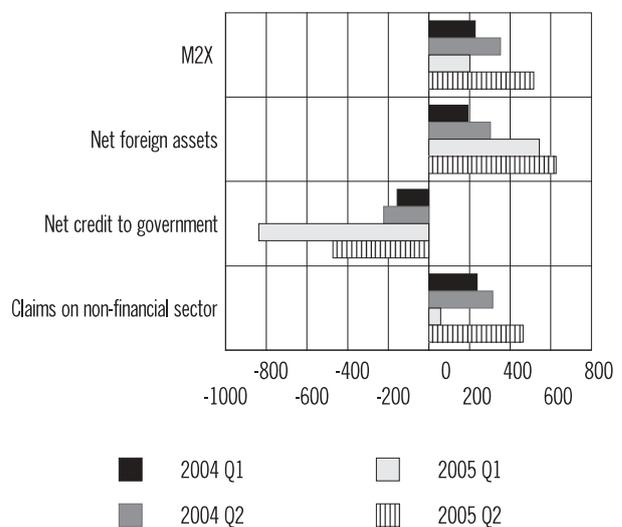
Despite the slowing of growth in foreign currency deposits in 2005 Q2 and a decline in the value of cash foreign currency, the dynamics of the notional broad M2Y aggregate demonstrated an upward long-term trend. The annualised M2Y growth rates were faster as of July 1, 2005 (25.6%) than as of the beginning of the year

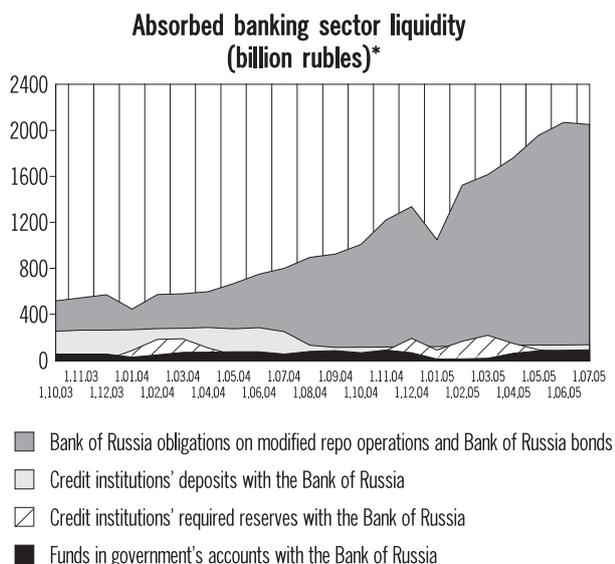
**Monetary aggregates  
(month on month of previous year, %)**



*Definitions of aggregates:*  
 M1 = M0 + current accounts and demand deposits;  
 M2 = M1 + ruble time deposits;  
 M2X (money supply in the monetary survey definition) = M2 + foreign currency deposits;  
 M2Y (notional broad monetary aggregate) = M2X + an estimated amount of cash foreign exchange in the non-banking sector.

**Sources of money supply growth  
(quarterly change, billion rubles)**





(24.3%) and as of the same date last year (22.5%).

The dollarisation coefficient, the share of the foreign currency component of the money supply in the monetary survey definition (M2X), dropped in 2005 Q2 by 0.5 percentage points to 18.1% (it increased by about the same figure in the respective period of 2004). At the same time, the ruble component of quasi-money continued to predominate in M2X (29.6% as of July 1, 2005, as against 29.4% as of April 1, 2005).

The slowing of the Russian economy's de-dollarisation is also characterised by the changes in the structure of the M2Y aggregate. Thus, the share of the foreign currency component of this notional broad aggregate dropped by 1.5 percentage points in 2005 Q2 largely due to a contraction in the share of cash foreign currency. The share of all foreign currency funds in the broad M2Y aggregate was smaller in 2005 Q2 than in the same period last year.

The dynamics of enterprise and household funds attracted by banks in rubles and foreign currency (an annualised 33.6% as of July 1, 2005), which serve as the basis for the expansion of lending volumes, were slower than the increase in

loans to the real sector (43.2% as of July 1, 2005). In 2005 Q2, the increase of the banking sector's claims on the non-financial sector of the economy was much higher than in the previous quarter (it totalled 463.8 billion rubles in April-June) and also exceeded the 2004 Q2 figures. The role of credit to non-financial enterprises and households as a source of aggregate money supply expansion increased in 2005 Q2. However, the external source continued to be a major source of growth in money supply. The growth of banking sector net foreign assets (by 626.4 billion rubles), mainly caused by the Bank of Russia's purchase of foreign exchange on the domestic forex market, was two times larger in 2005 Q2 than in 2004 Q2.

The large-scale accumulation of funds in the general government's accounts, caused by the expansion of the Stabilisation Fund, had a significant restraining effect on money supply growth in the first half of 2005. The Stabilisation Fund totalled 617.9 billion rubles as of July 1, 2005. In 2005 Q2, its volume declined, however, the rates of growth in monthly transfers of tax revenues to the Stabilisation Fund continued to rise, while some funds charged off from it to make early foreign debt payments had no inflationary consequences.

The monetary base contracted 3.2% in the first half of 2005, while the government's balances with the Bank of Russia expanded by almost two times. In April-June 2005, the monetary base (broad definition) grew 2.3% (it declined by almost 1% in 2004 Q2). The share of credit institutions' funds in correspondent accounts with the Bank of Russia decreased from 14.5% to 12.2% in April-June 2005 (it was actually unchanged in the same period last year). The share of credit institutions' funds absorbed by the Bank of Russia through its deposits, operations with its bonds and repo operations dropped from 9.6% to 5.8% in the monetary base during the quarter and from 15.5% to 11.7% taking into account the credit institutions' required reserves.

# Statistical Addendum

## Consumer prices by group of goods and services (month on month, %)

	Monthly inflation	Core inflation	Food price growth	Growth in food prices net of vegetable prices	Vegetable and fruit price growth	Non-food price growth	Service price growth
<b>2003</b>							
January	2.4	1.2	2.5	1.3	13.1	1.1	4.4
February	1.6	0.9	1.2	0.8	4.1	0.9	4.2
March	1.1	0.7	1.0	0.6	3.9	0.8	1.7
April	1.0	0.6	1.0	0.5	4.2	0.6	1.8
May	0.8	0.6	0.7	0.4	2.5	0.6	1.5
June	0.8	0.6	0.8	0.6	2.3	0.5	1.2
July	0.7	0.7	0.4	0.7	-1.8	0.5	1.9
August	-0.4	0.7	-1.4	0.8	-17.2	0.6	0.7
September	0.3	1.1	-0.2	1.1	-11.2	0.9	0.9
October	1.0	1.4	1.1	1.8	-5.6	1.0	0.8
November	1.0	1.1	1.2	1.3	1.0	0.8	0.4
December	1.1	1.0	1.5	1.2	4.1	0.6	0.9
Full year (December on December)	12.0	11.2	10.2	11.8	-4.2	9.2	22.3
<b>2004</b>							
January	1.8	0.9	1.6	1.3	5.5	0.5	4.1
February	1.0	0.8	1.1	1.1	1.5	0.4	1.6
March	0.8	0.7	1.1	0.9	2.8	0.4	0.6
April	1.0	0.8	0.8	1.0	-0.6	0.6	2.0
May	0.7	0.6	0.4	0.5	-0.7	0.8	1.4
June	0.8	0.5	0.8	0.4	4.8	0.7	0.9
July	0.9	0.8	1.0	1.0	1.5	0.6	1.3
August	0.4	0.7	0.1	0.8	-6.3	0.5	1.0
September	0.4	0.9	0.0	0.9	-9.0	0.9	0.6
October	1.1	1.3	1.4	1.7	-2.7	0.7	1.2
November	1.1	1.1	1.5	1.5	2.2	0.7	0.8
December	1.1	1.0	1.7	1.4	5.4	0.4	1.0
Full year (December on December)	11.7	10.5	12.3	13.1	3.3	7.4	17.7
<b>2005</b>							
January	2.6	0.9	1.4	1.1	5.1	0.4	8.8
February	1.2	0.7	1.4	0.9	6.1	0.4	2.2
March	1.3	0.8	2.1	1.1	11.2	0.4	1.2
April	1.1	0.9	1.7	1.3	5.4	0.5	0.8
May	0.8	0.6	1.1	0.7	4.1	0.4	0.8
June	0.6	0.5	0.7	0.4	3.3	0.3	0.9

**Consumer prices by group of goods and services  
(since start of year on accrual basis, %)**

	Monthly inflation	Core inflation	Food price growth	Growth in food prices net of vegetable prices	Vegetable and fruit price growth	Non-food price growth	Service price growth
<b>2003</b>							
January	2.4	1.2	2.5	1.3	13.1	1.1	4.4
February	4.1	2.1	3.7	2.2	17.8	2.0	8.8
March	5.2	2.8	4.8	2.8	22.4	2.8	10.6
April	6.2	3.4	5.8	3.3	27.6	3.5	12.6
May	7.1	4.0	6.5	3.8	30.8	4.1	14.2
June	7.9	4.7	7.4	4.4	33.7	4.6	15.6
July	8.7	5.4	7.8	5.1	31.4	5.1	17.8
August	8.3	6.2	6.3	6.0	8.7	5.7	18.7
September	8.6	7.3	6.1	7.1	-3.4	6.6	19.7
October	9.7	8.9	7.3	9.1	-8.9	7.7	20.7
November	10.8	10.1	8.6	10.4	-7.9	8.6	21.2
December	12.0	11.2	10.2	11.8	-4.2	9.2	22.3
<b>2004</b>							
January	1.8	0.9	1.6	1.3	5.5	0.5	4.1
February	2.8	1.7	2.8	2.3	7.1	0.9	5.8
March	3.5	2.4	3.8	3.2	10.1	1.4	6.4
April	4.6	3.2	4.7	4.2	9.5	2.0	8.5
May	5.3	3.8	5.2	4.8	8.7	2.8	10.0
June	6.1	4.3	6.0	5.2	13.9	3.4	11.0
July	7.1	5.1	7.1	6.2	15.6	4.0	12.5
August	7.6	5.8	7.2	7.1	8.3	4.6	13.6
September	8.0	6.8	7.2	8.0	-1.4	5.5	14.3
October	9.3	8.1	8.7	9.9	-4.0	6.3	15.7
November	10.5	9.3	10.4	11.5	-1.9	7.0	16.6
December	11.7	10.5	12.3	13.1	3.3	7.4	17.7
<b>2005</b>							
January	2.6	0.9	1.4	1.1	5.1	0.4	8.8
February	3.9	1.7	2.8	2.0	11.5	0.7	11.2
March	5.3	2.4	4.9	3.1	24.0	1.1	12.6
April	6.5	3.3	6.7	4.4	30.8	1.6	13.5
May	7.3	4.0	7.9	5.1	36.1	2.1	14.4
June	8.0	4.4	8.6	5.5	40.6	2.4	15.4

**Consumer prices by group of goods and services  
(total for quarter, %)**

	Inflation	Core inflation	Food price growth	Growth in food prices net of vegetable prices	Vegetable and fruit price growth	Non-food price growth	Service price growth
<b>2002</b>							
I	5.4	2.8	4.2	2.1	22.6	2.7	14.5
II	3.4	1.5	3.0	0.7	20.1	3.1	5.1
III	1.2	2.3	-1.4	1.8	-21.6	2.1	7.3
IV	4.3	3.2	4.9	3.6	15.5	2.5	5.5
<b>2003</b>							
I	5.2	2.8	4.8	2.8	22.4	2.8	10.6
II	2.6	1.8	2.5	1.6	9.3	1.8	4.5
III	0.6	2.5	-1.2	2.6	-27.8	1.9	3.6
IV	3.1	3.6	3.9	4.3	-0.8	2.4	2.1
<b>2004</b>							
I	3.5	2.4	3.8	3.2	10.1	1.4	6.4
II	2.5	1.8	2.1	1.9	3.5	2.0	4.3
III	1.8	2.4	1.2	2.7	-13.4	2.0	3.0
IV	3.4	3.5	4.7	4.7	4.8	1.8	3.0
<b>2005</b>							
I	5.3	2.4	4.9	3.1	24.0	1.1	12.6
II	2.5	1.9	3.5	2.4	13.4	1.3	2.6

## Inflation Growth Structure (percentage points)

### Inflation growth over period since start of year due to changes in prices by group of goods and services

	Foodstuffs*	Non-food products	Paid services	Vegetables and fruit	Inflation over period, %	Core inflation	Non-core inflation**
<b>2003</b>							
January	0.7	0.3	0.8	0.7	<b>2.4</b>	1.0	1.4
February	1.1	0.5	1.5	0.9	<b>4.1</b>	1.7	2.4
March	1.4	0.8	1.8	1.2	<b>5.2</b>	2.3	2.9
April	1.7	1.0	2.2	1.4	<b>6.2</b>	2.8	3.4
May	1.9	1.1	2.4	1.6	<b>7.1</b>	3.3	3.8
June	2.2	1.3	2.7	1.8	<b>7.9</b>	3.8	4.1
July	2.6	1.4	3.1	1.6	<b>8.7</b>	4.4	4.3
August	3.0	1.6	3.2	0.5	<b>8.3</b>	5.0	3.2
September	3.6	1.8	3.4	-0.2	<b>8.6</b>	6.0	2.7
October	4.5	2.1	3.5	-0.5	<b>9.7</b>	7.2	2.5
November	5.2	2.4	3.6	-0.4	<b>10.8</b>	8.2	2.6
December	5.9	2.5	3.8	-0.2	<b>12.0</b>	9.1	2.9
<b>2004</b>							
January	0.6	0.1	0.7	0.3	<b>1.8</b>	0.8	1.0
February	1.2	0.2	1.0	0.4	<b>2.8</b>	1.4	1.4
March	1.6	0.4	1.1	0.5	<b>3.5</b>	2.0	1.6
April	2.1	0.5	1.4	0.5	<b>4.6</b>	2.6	1.9
May	2.4	0.8	1.7	0.4	<b>5.3</b>	3.1	2.2
June	2.6	0.9	1.9	0.7	<b>6.1</b>	3.5	2.6
July	3.1	1.1	2.1	0.8	<b>7.1</b>	4.2	2.9
August	3.5	1.3	2.3	0.4	<b>7.6</b>	4.7	2.8
September	4.1	1.5	2.5	-0.1	<b>8.0</b>	5.5	2.5
October	5.0	1.7	2.7	-0.2	<b>9.3</b>	6.6	2.7
November	5.8	1.9	2.9	-0.1	<b>10.5</b>	7.6	2.9
December	6.5	2.0	3.0	0.2	<b>11.7</b>	8.5	3.3
<b>2005</b>							
January	0.5	0.1	1.8	0.2	<b>2.6</b>	0.7	1.9
February	0.9	0.2	2.3	0.4	<b>3.9</b>	1.3	2.6
March	1.4	0.3	2.6	0.9	<b>5.3</b>	1.9	3.3
April	2.0	0.5	2.8	1.2	<b>6.5</b>	2.7	3.8
May	2.3	0.6	3.0	1.4	<b>7.3</b>	3.1	4.1
June	2.5	0.7	3.2	1.6	<b>8.0</b>	3.5	4.4

\* Excluding vegetables and fruit.

\*\* Growth in the prices of goods and paid services excluded from the core inflation calculation.

**Monthly inflation growth due to changes  
in prices by group of goods and services**

	Foodstuffs*	Non-food products	Paid services	Vegetables and fruit	Inflation over period, %	Core inflation	Non-core inflation**
<b>2003</b>							
January	0.7	0.3	0.8	0.7	2.4	1.0	1.4
February	0.4	0.2	0.7	0.2	1.6	0.7	0.9
March	0.3	0.2	0.3	0.2	1.1	0.6	0.5
April	0.3	0.2	0.3	0.3	1.0	0.5	0.5
May	0.2	0.2	0.3	0.2	0.8	0.4	0.4
June	0.3	0.1	0.2	0.1	0.8	0.5	0.3
July	0.3	0.1	0.4	-0.1	0.7	0.5	0.2
August	0.4	0.1	0.1	-1.1	-0.4	0.6	-1.0
September	0.5	0.2	0.2	-0.6	0.3	0.9	-0.6
October	0.9	0.3	0.1	-0.3	1.0	1.2	-0.1
November	0.6	0.2	0.1	0.0	1.0	0.9	0.1
December	0.6	0.2	0.2	0.2	1.1	0.8	0.3
<b>2004</b>							
January	0.6	0.1	0.7	0.3	1.8	0.8	1.0
February	0.5	0.1	0.3	0.1	1.0	0.6	0.4
March	0.4	0.1	0.1	0.1	0.8	0.6	0.2
April	0.5	0.2	0.4	0.0	1.0	0.6	0.3
May	0.3	0.2	0.2	0.0	0.7	0.5	0.2
June	0.2	0.2	0.2	0.3	0.8	0.4	0.4
July	0.5	0.1	0.2	0.1	0.9	0.6	0.3
August	0.4	0.2	0.2	-0.4	0.4	0.5	-0.1
September	0.5	0.3	0.1	-0.5	0.4	0.7	-0.3
October	0.9	0.2	0.2	-0.1	1.1	1.0	0.2
November	0.7	0.2	0.1	0.1	1.1	0.9	0.2
December	0.6	0.1	0.1	0.3	1.1	0.8	0.3
<b>2005</b>							
January	0.5	0.1	1.8	0.2	2.6	0.7	1.9
February	0.4	0.1	0.5	0.2	1.2	0.6	0.7
March	0.5	0.1	0.3	0.5	1.3	0.6	0.7
April	0.6	0.1	0.2	0.2	1.1	0.7	0.4
May	0.3	0.1	0.2	0.2	0.8	0.5	0.3
June	0.2	0.1	0.2	0.2	0.6	0.3	0.3

\* Excluding vegetables and fruit.

\*\* Growth in the prices of goods and paid services excluded from the core inflation calculation.

## Contribution to Inflation Growth (%)

### Contribution to inflation growth over period since start of year by group of goods and services

	Foodstuffs*	Non-food products	Paid services	Vegetables and fruit	Core inflation	Non-core inflation**
<b>2003</b>						
January	27.5	12.4	31.6	28.5	40.6	59.4
February	26.7	13.4	37.1	22.8	41.8	58.2
March	27.3	14.9	35.3	22.5	44.2	55.8
April	27.0	15.3	34.7	23.1	44.9	55.1
May	26.9	15.9	34.5	22.7	46.1	53.9
June	28.1	16.0	33.7	22.2	47.9	52.1
July	29.7	16.2	35.2	18.8	50.2	49.8
August	36.5	19.1	38.9	5.5	60.7	39.3
September	41.6	21.2	39.3	-2.1	69.1	30.9
October	46.7	21.6	36.4	-4.7	74.3	25.7
November	48.5	21.7	33.6	-3.8	76.3	23.7
December	49.1	21.0	31.7	-1.8	75.9	24.1
<b>2004</b>						
January	35.8	7.6	40.3	16.3	43.2	56.8
February	42.3	9.0	35.4	13.3	50.0	50.0
March	45.0	10.3	30.2	14.5	55.3	44.7
April	46.1	11.7	31.5	10.7	57.5	42.5
May	45.3	14.2	32.1	8.5	58.5	41.5
June	42.3	15.3	30.6	11.8	57.2	42.8
July	43.5	15.3	29.9	11.3	58.8	41.2
August	47.0	16.5	30.8	5.7	62.6	37.4
September	50.9	19.1	30.9	-0.9	68.4	31.6
October	54.2	18.7	29.3	-2.3	70.9	29.1
November	55.4	18.3	27.2	-1.0	72.0	28.0
December	55.7	17.1	25.7	1.5	72.0	28.0
<b>2005</b>						
January	18.3	4.4	69.9	7.4	27.1	72.9
February	22.9	5.7	60.1	11.4	33.4	66.6
March	26.4	6.2	49.9	17.5	36.6	63.4
April	30.8	7.4	43.5	18.3	41.0	59.0
May	31.6	8.4	41.1	19.0	43.1	56.9
June	31.3	8.9	40.3	19.5	44.1	55.9

\* Excluding vegetables and fruit.

\*\* Growth in the prices of goods and paid services excluded from the core inflation calculation.

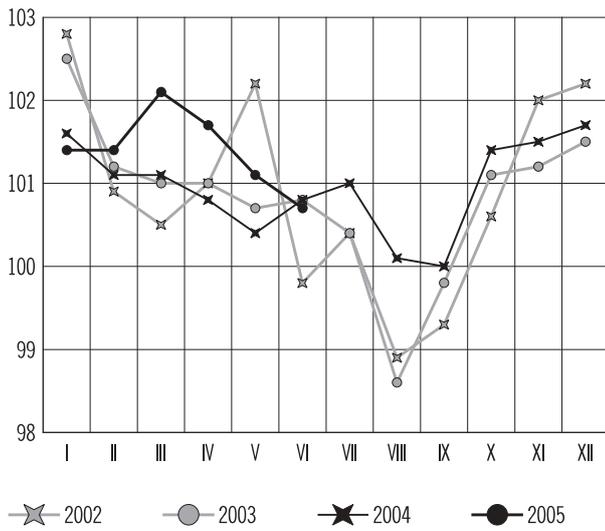
**Contribution to monthly inflation growth by group of goods and services**

	Foodstuffs*	Non-food products	Paid services	Vegetables and fruit	Core inflation	Non-core inflation**
<b>2003</b>						
January	27.5	12.4	31.6	28.5	40.6	59.4
February	25.5	15.0	45.0	14.6	43.7	56.3
March	29.7	20.3	28.3	21.7	53.0	47.0
April	25.5	17.2	31.6	25.7	48.7	51.3
May	25.9	21.2	33.1	19.8	55.3	44.7
June	38.4	16.6	26.9	18.1	62.7	37.3
July	46.8	18.9	50.7	-16.4	74.7	25.3
August	<i>Estimate impossible for negative value</i>					
September	164.8	72.9	50.5	-188.3	270.6	-170.6
October	86.6	25.6	14.2	-26.4	114.6	-14.6
November	63.8	23.3	8.4	4.5	94.1	5.9
December	53.8	14.2	15.1	16.9	71.7	28.3
<b>2004</b>						
January	35.8	7.6	40.3	16.3	43.2	56.8
February	53.5	11.5	26.8	8.1	61.8	38.2
March	54.6	14.8	11.5	19.2	74.2	25.8
April	49.6	17.1	36.3	-2.9	65.1	34.9
May	40.1	29.6	35.6	-5.2	64.9	35.1
June	22.7	22.7	21.0	33.7	48.2	51.8
July	50.3	15.6	25.3	8.7	68.1	31.9
August	101.5	35.8	46.0	-83.3	122.3	-22.3
September	117.0	63.9	34.1	-115.0	164.9	-64.9
October	75.6	16.9	19.0	-11.5	86.8	13.2
November	63.4	15.6	12.0	9.0	79.4	20.6
December	56.7	7.1	13.1	23.1	71.7	28.3
<b>2005</b>						
January	18.3	4.4	69.9	7.4	27.1	72.9
February	32.3	8.4	39.8	19.5	46.4	53.6
March	36.4	7.7	21.1	34.8	46.1	53.9
April	50.0	12.8	15.3	21.8	60.9	39.1
May	37.7	16.9	20.9	24.6	60.0	40.0
June	28.0	14.4	32.3	25.3	54.7	45.3

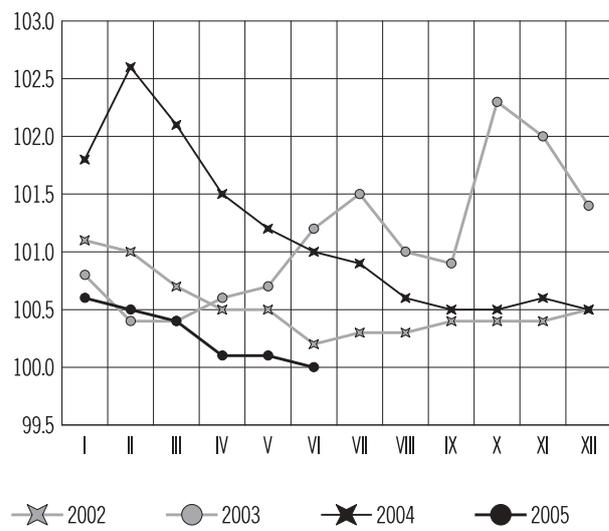
\* Excluding vegetables and fruit.

\*\* Growth in the prices of goods and paid services excluded from the core inflation calculation.

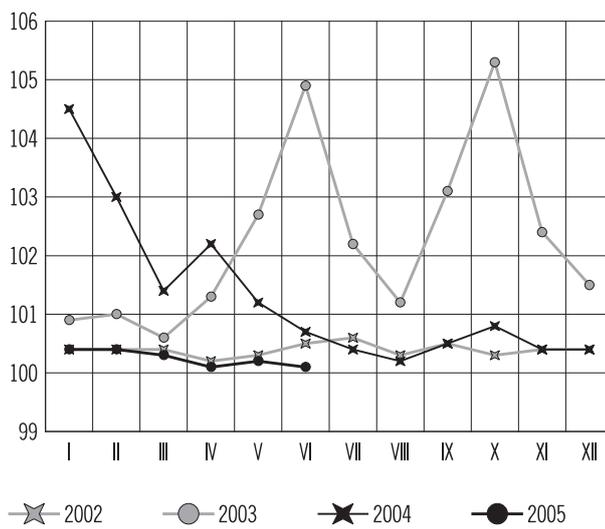
**Food prices, total**  
(as % of previous month)



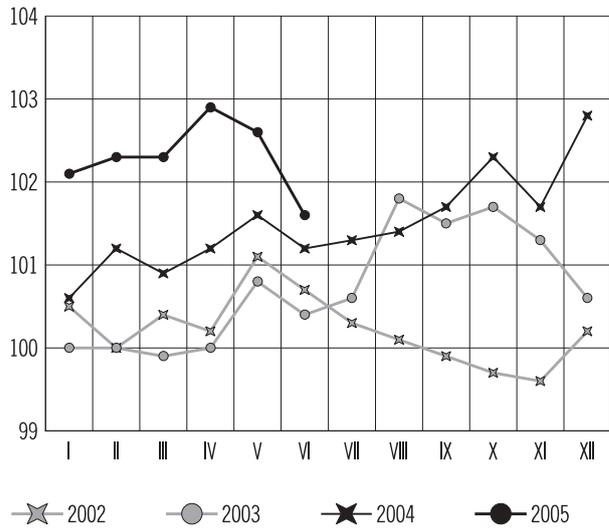
**Pasta prices**  
(as % of previous month)



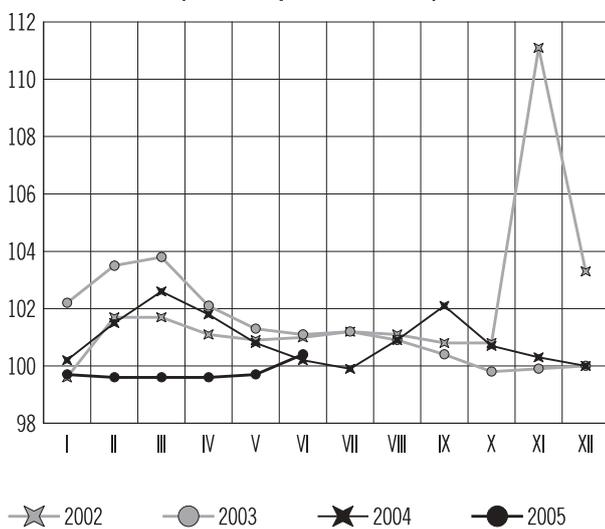
**Bread and bakery product prices**  
(as % of previous month)



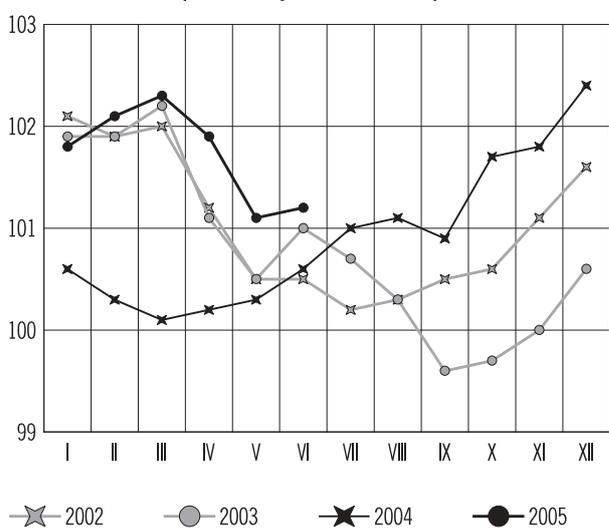
**Meat and poultry prices**  
(as % of previous month)



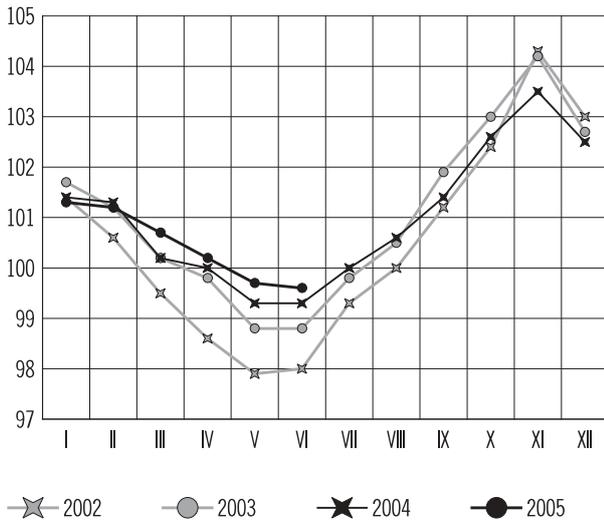
**Cereal and legume prices**  
(as % of previous month)



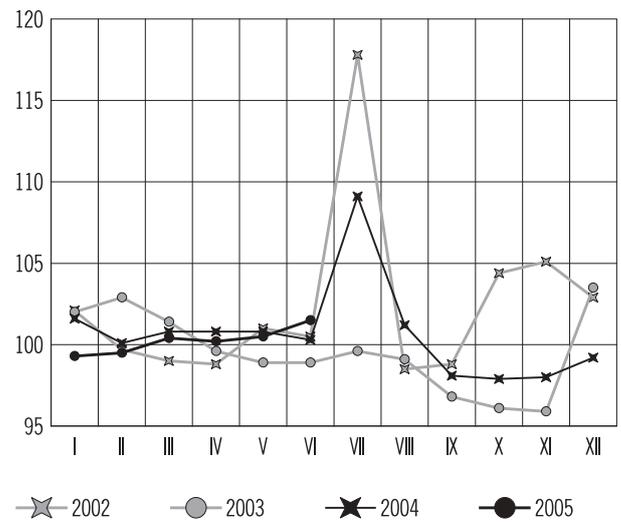
**Fish and seafood prices**  
(as % of previous month)



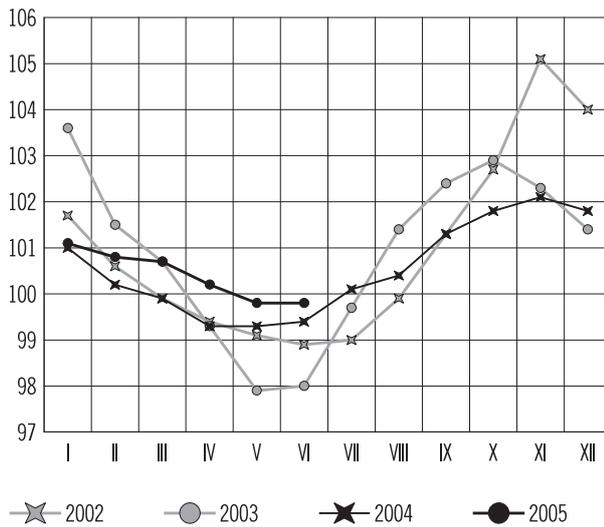
**Milk and dairy product prices  
(as % of previous month)**



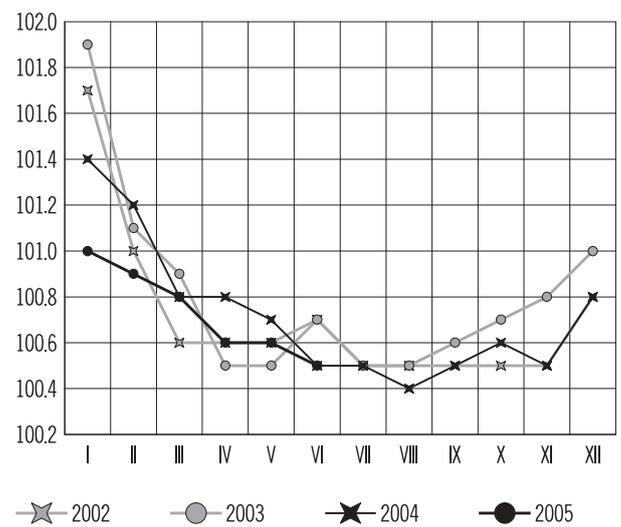
**Granulated sugar prices  
(as % of previous month)**



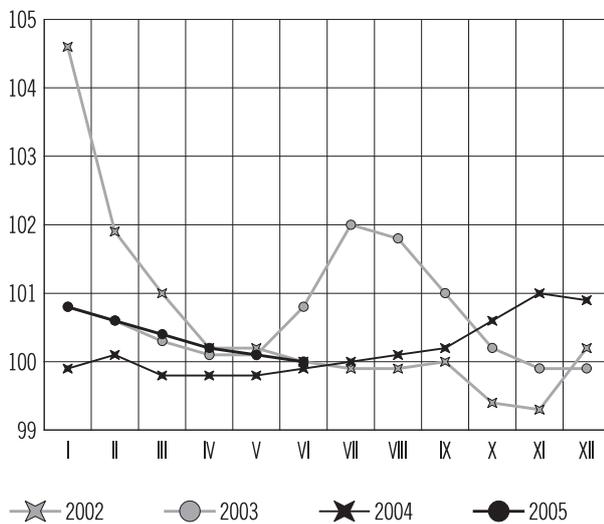
**Butter prices  
(as % of previous month)**



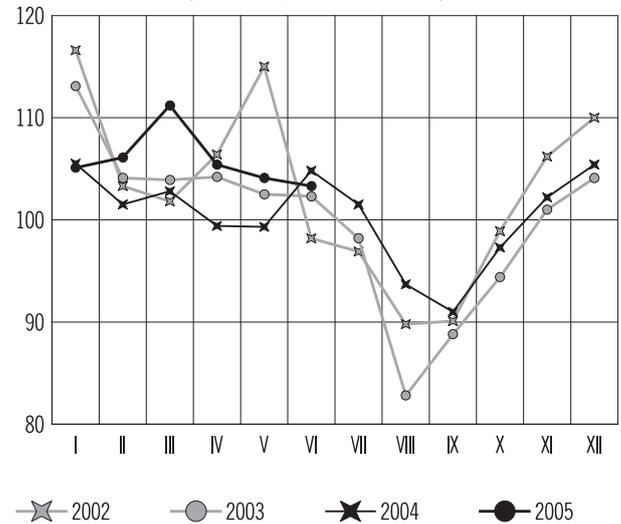
**Alcoholic beverage prices  
(as % of previous month)**



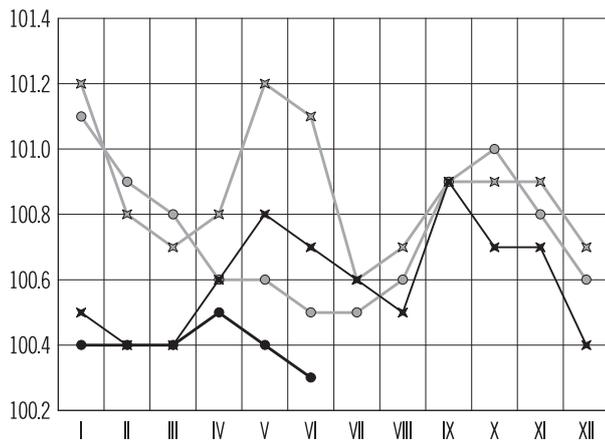
**Sunflower oil prices  
(as % of previous month)**



**Vegetable and fruit prices  
(as % of previous month)**

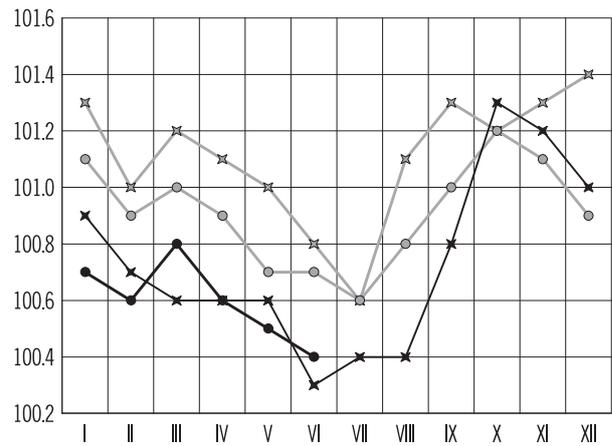


**Non-food prices, total**  
(as % of previous month)



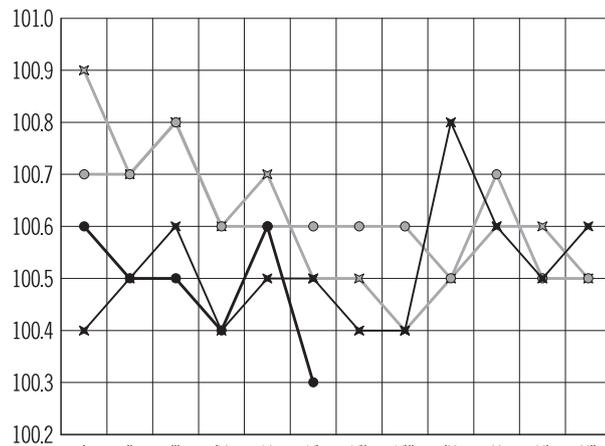
—x— 2002    —●— 2003    —x— 2004    —●— 2005

**Knitwear prices**  
(as % of previous month)



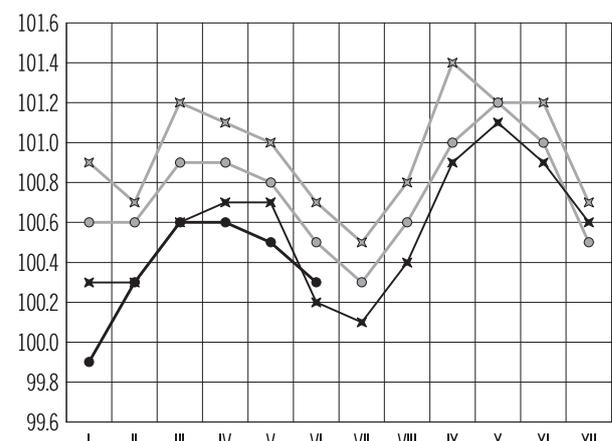
—x— 2002    —●— 2003    —x— 2004    —●— 2005

**Fabrics prices**  
(as % of previous month)



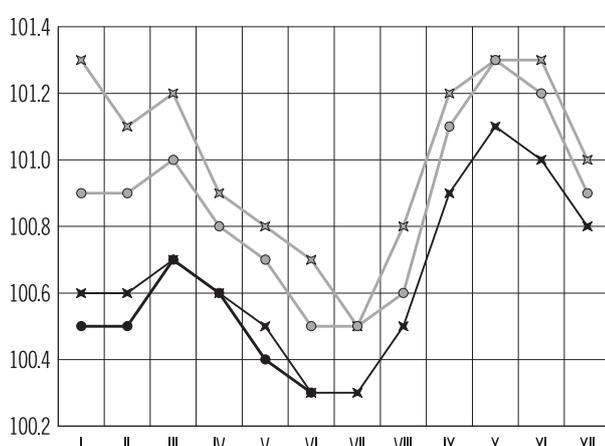
—x— 2002    —●— 2003    —x— 2004    —●— 2005

**Footwear prices**  
(as % of previous month)



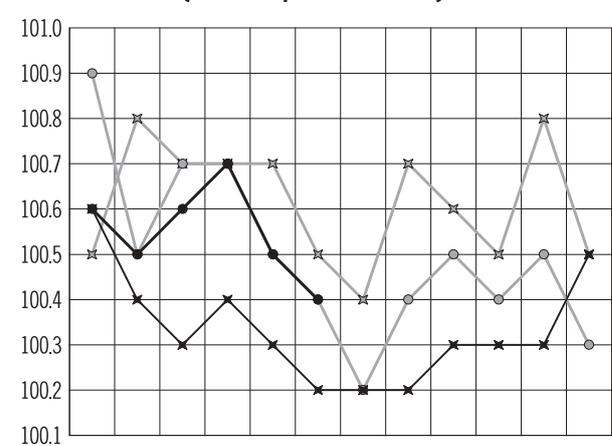
—x— 2002    —●— 2003    —x— 2004    —●— 2005

**Clothing and underwear prices**  
(as % of previous month)



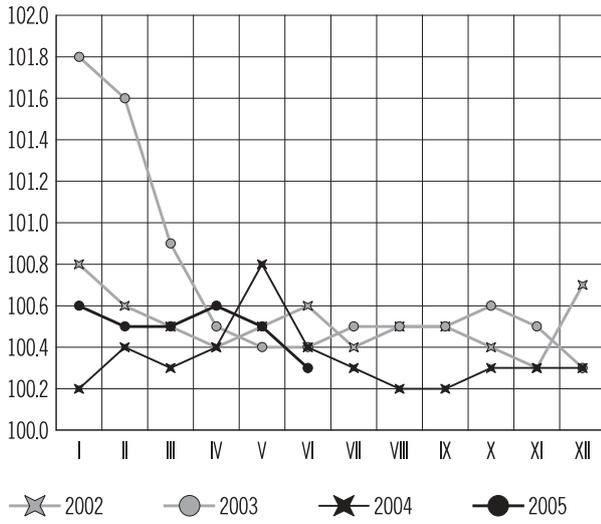
—x— 2002    —●— 2003    —x— 2004    —●— 2005

**Detergent prices**  
(as % of previous month)

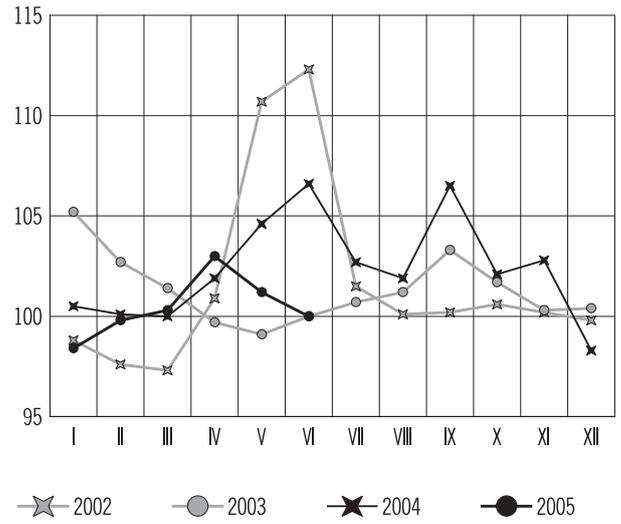


—x— 2002    —●— 2003    —x— 2004    —●— 2005

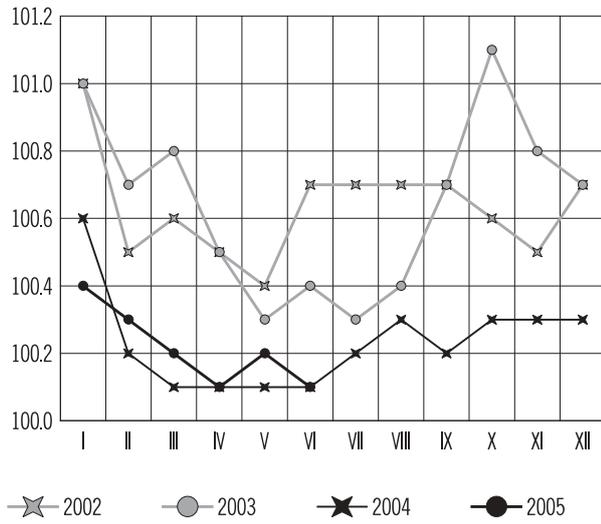
**Tobacco prices**  
(as % of previous month)



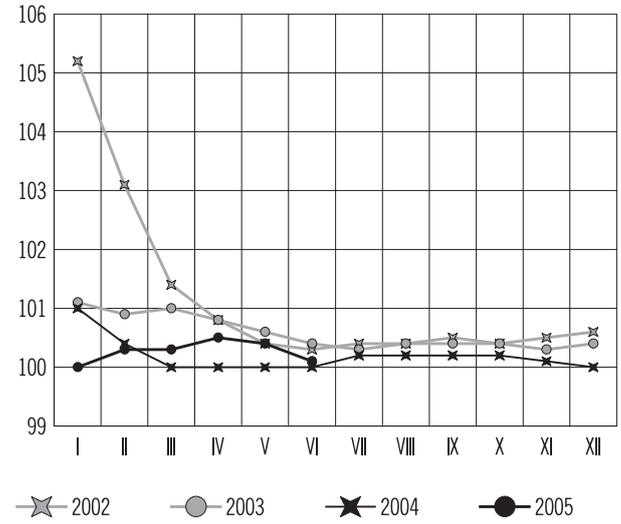
**Petrol prices**  
(as % of previous month)



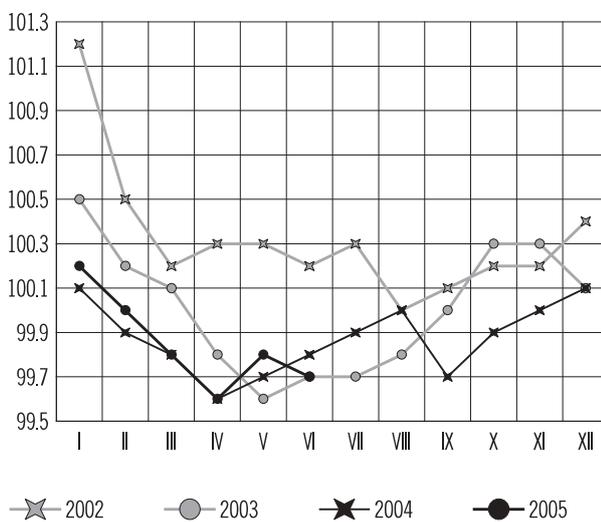
**Household electric appliances prices**  
(as % of previous month)



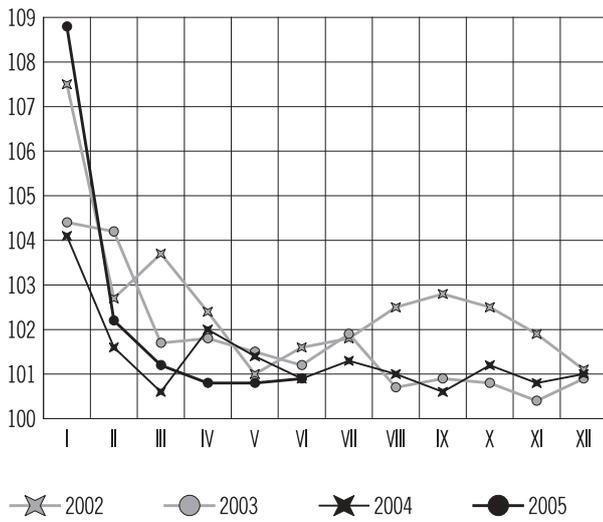
**Medicine prices**  
(as % of previous month)



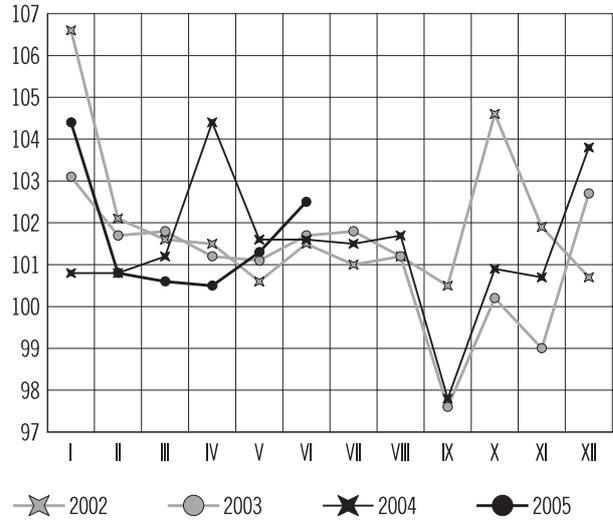
**TV and radio set prices**  
(as % of previous month)



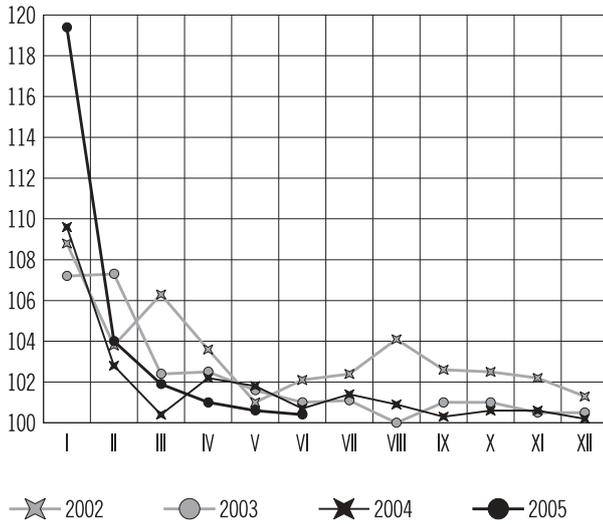
**Paid service prices  
(as % of previous month)**



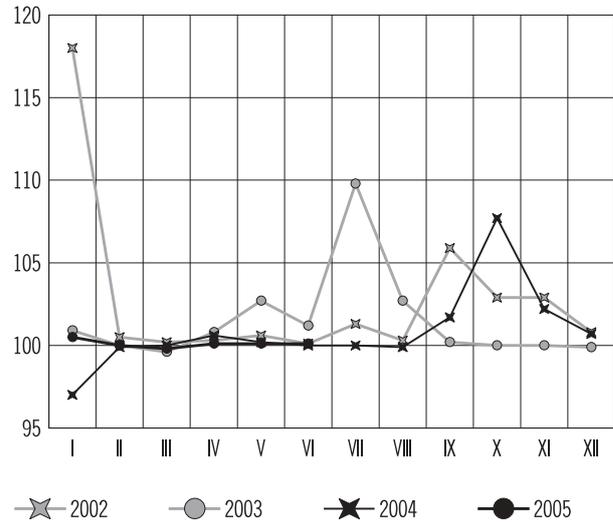
**Passenger transport fares  
(as % of previous month)**



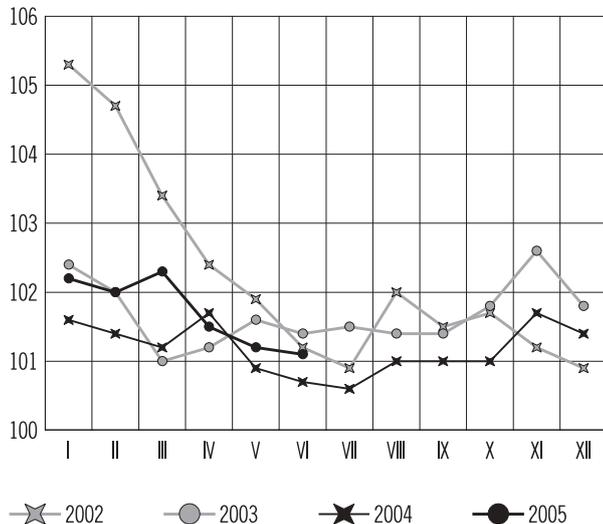
**Rent and amenities prices  
(as % of previous month)**



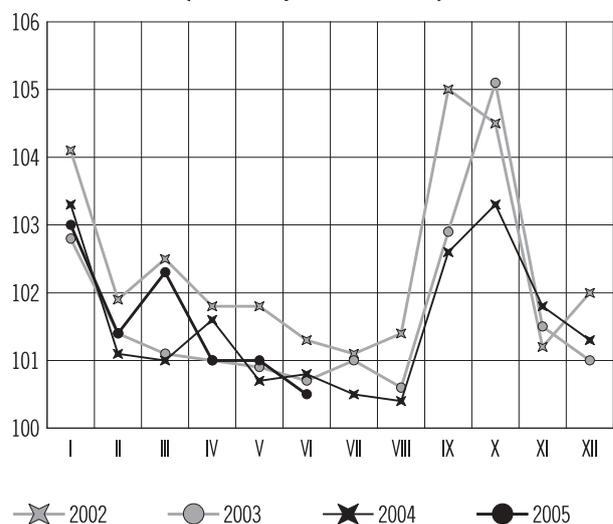
**Communication fees  
(as % of previous month)**



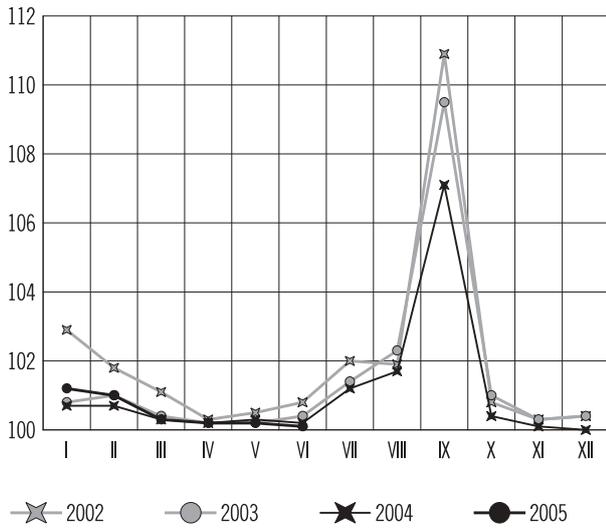
**Healthcare prices  
(as % of previous month)**



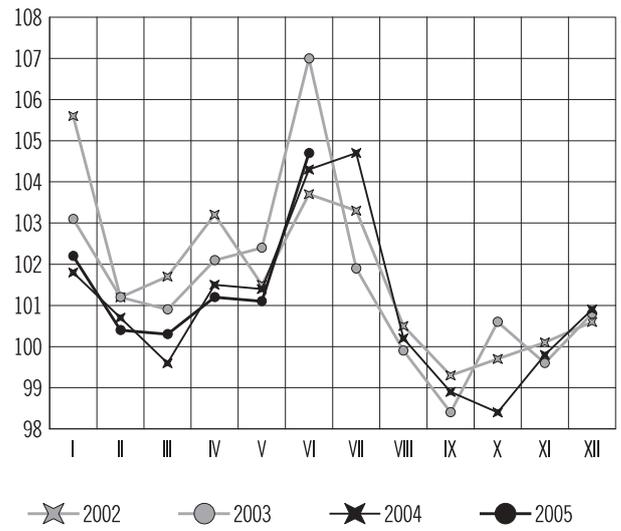
**Cultural service prices  
(as % of previous month)**



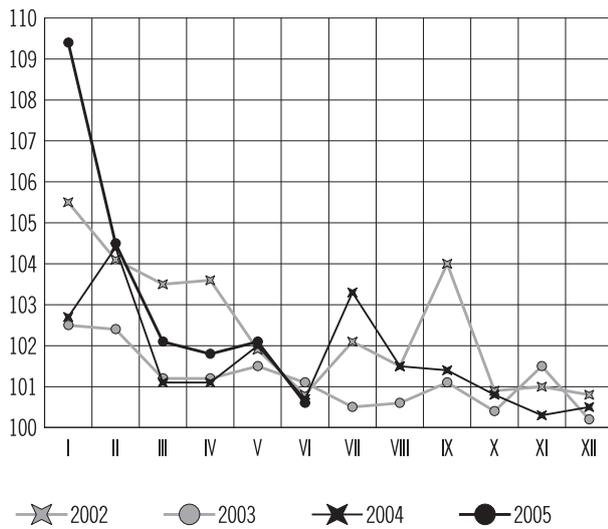
**Education fees  
(as % of previous month)**



**Sanatorium and health resort accommodation prices  
(as % of previous month)**



**Pre-school tuition fees  
(as % of previous month)**



**Everyday service prices  
(as % of previous month)**

