

DAILY REPORT ON RUSSIA

AND THE FORMER SOVIET REPUBLICS

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RUSSIAN FEDERATION

Politics

Russia-Germany Smooth Relations

• Russian President Vladimir PUTIN put his best foot forward to build his relations with German Chancellor Gerhard SCHROEDER during a visit to Moscow over the Orthodox Christmas holiday. The relationship with Germany is of critical importance on many fronts, including the Paris Club debt negotiations, expansion of NATO, and US plans to build a National Defense System breaking the Anti-ballistic Missile Treaty of 1972. Foremost on the agenda were discussions over Russia's willingness to pay the Paris Club of creditors on its Soviet-era debt of \$48 billion. Germany is Russia's biggest creditor, holding about \$20 billion of the total. Ahead of the visit, Russia said that it did not plan to pay \$1.5 billion that it owes the club of creditors in the first quarter. *Hermes*, the German Export credit guarantee group, confirmed that Russia had not paid the \$4.8 million due last week. Bankers said that a formal default could not be declared unless the money was not received within 90 days of the due date. Russia's First Deputy Finance Minister Alexei ULYUKAYEV said, "We have a state of consultations, a stage of negotiations, and this is considered as a technical deferment." Nonetheless, Jean-Pierre JOUYET, chairman of the Paris Club, sent a letter to Finance Minister Alexei KUDRIN warning Russia against non-payment. During the talks in Moscow, SCHROEDER confirmed the German position that it expects Russia, "to stand by its international debt service commitments in full," noting that Russia's economy was strong enough for it to meet its obligations. PUTIN insisted that Russia would pay its debts, but called for a restructuring that would not undermine the economic recovery. Russia is due to pay back \$3.4 billion in loans to the Paris Club this year. A joint Russian-German working groups will

meet in Berlin on January 15th to discuss the possibility of a "debt for equity" swap to settle some or all of the debt. Other Paris Club members are wary of this arrangement because Russia is reluctant to include blue-chip companies, like *Gazprom*, in the swap stock offer.

Putin Denies Kaliningrad Nuclear Movement

• Russian President Vladimir PUTIN on Saturday dismissed as "rubbish" a US intelligence report, confirmed by the CLINTON administration, citing the movement of tactical Russian nuclear weapons into a storage depot that serves the Baltic Fleet in Kaliningrad. Pentagon officials noted that the storage of tactical weapons in Kaliningrad did not violate any agreements with Russia. The Washington Times initially reported the story on January 3rd. The next day Kaliningrad governor Vladimir YEGOROV dismissed the newspaper report as a "dangerous joke" and emphasized that the Baltic region would remain nuclear free. Fears of the return of nuclear weapons raced through Kaliningrad's Baltic neighbors. Russia is believed to have withdrawn tactical nuclear weapons from all of its warships including those in the Baltic Fleet in 1991. Foreign Ministry spokesman Alexander YAKOVENKO stated, "There have been no tactical nuclear weapons [deployed in Kaliningrad] on naval objects, including at sea, on land and on the air force, and none have been taken there."

Economy

Putin Calls For 4 Percent GDP Growth

• On Wednesday, Russian President Vladimir PUTIN told his

team of economists to produce a plan that would lift the nation's economy above the government target of 4 percent growth of the gross domestic product (GDP). Finance Minister Alexei KUDRIN said PUTIN had told a Kremlin conference of senior ministers and officials that four percent growth in GDP should be seen as a minimum, the RIA news agency reported. Prime Minister Mikhail KASYANOV, Central Bank Chairman Viktor GERASHCHENKO, Kremlin economic adviser Andrei ILLARIONOV, PUTIN's chief of staff Alexander VOLOSHIN and Deputy Finance Minister Sergei IGNATYEV also attended the meeting. KUDRIN, who is also a deputy prime minister, said GDP growth in 2000 reached more than seven percent, adding that inflation for the year had been within expected limits at 20.2 percent. The Finance Minister said he was confident Russia had the tools to control inflation, the ruble and money supply.

Ruble = 28.43/\$1.00 (NY rate)

Ruble = 28.39/\$1.00 (CB rate)

Ruble = 26.94/1 euro (CB rate)

Business

Fedorov Accuses Kremlin Over Gazprom

- Former finance minister and now minority shareholder representative on the board of *Gazprom* Boris FEDOROV has accused Kremlin appointed Economics and Trade Minister German GREF of failing to address concerns of mismanagement within *Gazprom*. Minority shareholders are concerned over the relationship between *Gazprom* and a number of companies that have benefited from favorable contracts. This includes *Itera*, which has not revealed its close ties to *Gazprom*. GREF in December was charged with investigating investor concerns ahead of the next board meeting in January, which is now only two weeks away. In December, FEDOROV circulated a detailed list of questions expressing minority shareholders' concerns. He has received a three-page response from *Gazprom* and an eight-page letter from *Itera's* management, but neither answered most of the questions. FEDOROV said GREF, "never contacted us and is doing nothing." FEDOROV said that in absence of an adequate official response he plans to call for the appointment of an international accounting firm on behalf of minority shareholders to carry out an independent audit into a number of "big black holes" in *Gazprom's*

finances, the *Financial Times* reported. The Russian government holds a 38 percent stake in *Gazprom*. FEDOROV's campaign is being viewed as a test case over how seriously the government is willing to tackle corporate governing concerns, which are holding back foreign investment in Russia.

Russia To Expand St. Petersburg Port

- The Russian government and private companies will invest \$105 million to build by 2003 a new sea fertilizer terminal and modernize rail and road links to the St. Petersburg port. The \$40 million fertilizer terminal will be able to handle as much as 5 million tons a year when it starts work in November. It will be half-owned by *Peterburgsky Morsky Port* and *Uralkaliy*, Russia's top fertilizer maker. *Sberbank*, Russia's state-run savings bank, has lent \$23 million for the project. The investment is part of plans to almost double the port's cargo volumes to 60 million tons a year by 2010. Lack of local capacity is one reason why Russia loses an estimated \$2 billion a year in lost duties on cargoes shipped in and out of Russia via ports in neighboring countries. Tangled laws are also a big problem. Lev SAVULKIN, senior analyst at the Leontieff Center for Economic and Social Research in St. Petersburg said, "With Russia's current customs and tax legislation situation, importers and exporters find it cheaper to do business with ports in Finland, Estonia, and Latvia." Since 1998, total cargo volumes—mostly exports such as timber, coal, metal, and oil products—rose 25 percent a year, reaching an expected 31.5 million tons this year, according to *Peterburgsky Morsky Port*, which handles 75 percent of all goods shipped through the port. The port is Russia's second largest, after Novorossiisk on the Black Sea, which handles about 58 million tons of cargo a year. Latvia's Ventspils is the largest port on the Baltic Sea, handling about 40 million tons a year, of which 30 million tons are oil and oil products, Bloomberg News reported.

EUROPEAN REPUBLICS

Lithuania To Sell Utilities

- The Lithuanian government announced on Friday it was committed to the restructuring and privatization of the state-run gas utility *Lietuvos*

Dujos and power utility *Lietuvos Energija*. "The government's strategic planning committee discussed energy sector strategic goals...Its aim to continue the reorganization and privatization of *Lietuvos Energija* and *Lietuvos Dujos* was approved," the government's press office said in a statement. Lithuania has pledged to sell between 34 and 51 percent, and possibly operational control, in monopoly *Lietuvos Dujos*. A public tender is expected to be launched in late spring Economy Minister Eugenijus MALDEIKIS told Reuters. He added the government is determined to complete restructuring of *Lietuvos Energija* over the next six to nine months. The previous administration planned to split 82.6 percent state-owned *Energija* into separate generation, transmission, and distribution companies. President Valdas ADAMKUS, who called for more transparency in the process, vetoed that plan. MALDEIKIS said, "All the legal groundwork has been presented to parliament. The company itself is working on restructuring and I think by autumn we should be ready to present privatization offers to potential investors."

Estonian Economic Statistics

- The Estonian Central Bank today said its gold and foreign currency reserves at the end of December were \$920.8 million, up 18.5 percent from the end-November figure of \$777.1 million. The Bank also said it had sold Estonian kroons worth of 3.44 billion EEK for foreign currency in December and bought 2.05 billion EEK for foreign currency. The Bank expected the country's inflation rate to rise by over five percent in the first half of 2001. "Annual growth of consumer prices will exceed 5 percent at least until the summer [amid] rising domestic demand [and] a planned increase in administratively regulated prices," the Central Bank said in a statement. Consumer prices—which grew 3.3 percent in 1999—rose 3.1 percent, year-on-year over the first and second quarters of last year. Estonian annual inflation quickened over 2000, peaking with a year-on-year rise in November of 5.7 percent amid rising fuel and transport costs before slowing to 5.0 percent in December, according to data from the statistics office today. The statistics office is due to release its full-2000 inflation data on January 22nd. Estonia's Economic Minister Mihkel PARNOJA on Friday said he expects the country's gross domestic product (GDP) to grow annually by six percent in

2001. Estonia's economy revived in 2000—with annual GDP growth of 6.9 percent in the third quarter and 7.5 percent in the second—after 1999's recession shrank the economy 1.1 percent in the wake of lost eastern markets following Russia's 1998 financial collapse. The Estonian Central Bank has said the country's annual economic growth could come in at 5.5 percent for 2000.

Latvia To Sell More Ventspils Nafta Stakes

- The Latvian government plans to sell another stake in *Ventspils Nafta*, the national oil company. The government, which now owns 43.62 percent of *Ventspils Nafta*, could begin the process of selling another 38.62 percent during the first half of this year. The remaining 5 percent would be reserved as an option until July 1st for *Latvijas Naftas Tranzits*, the major shareholder. Privatization Agency spokeswoman Viktorija JAKOBSONE said, "We are negotiating with the privatization consultant now and believe that the privatization regulations, or at least conditions, will be prepared in about three months." Austria's *Raiffeisen Zentralbank Oesterreich* is leading a group that was chosen to advise the government on the sale. A final agreement is expected to be signed within a month, said JAKOBSONE. She said it still is not known exactly how the shares will be sold, though a public offering would be the most appropriate method. "It could be done even internationally, but while it is not decided, it is difficult to say." *Ventspils Nafta* earned a net income of 16.2 million lats (\$26.1 million) in the first nine months, up from 15.2 million lats in the same period of 1999. *Latvijas Naftas Tranzits*, Latvia's largest oil transporter, owns 47.06 percent of *Ventspils Nafta*.

SOUTH CAUCASUS & CENTRAL ASIA

Georgia Protests Against Travel Warning

- Georgia's Foreign Ministry dismissed a Russian government report today, which warned Russian citizens to avoid traveling to Georgia because of rising crime and kidnappings by Chechen fighters. The warning highlighted the Pankisi Gorge and Akhmeta District. The statement recommended to Russian citizens staying in Georgia to take safety measures and restrict movement in dark hours. "They are manipulating the facts of certain criminal actions artificially to heighten tensions and worsen Georgia's international image," according to the

Georgian Foreign Ministry statement. Tensions between Georgia and Russia have worsened in the past year due to many issues including the on-going war in Chechnya, a new visa regime, the withdrawal of Russian bases, and energy cut-offs. Foreign Minister Irakly MENAGARISHVILI said Russia's warning, issued on Saturday, was "disinformation." He said, "Any country, including Russia, naturally has the right to make some or other recommendations to its citizens about advisability of trips to some or other countries," however, the Russian ministry's statement has, "elements of disinformation about the crime situation in Georgia." Georgian President Eduard SHEVARDNADZE said only that the situation was calm and added, "Any tension with our large neighbor is unacceptable for both Georgia and Russia." Analysts believe Russia is anxious about Georgia's efforts to boost ties with the West, undermining links with Moscow.

"Zero Variant" Presented To Parliament

- Georgian President Eduard SHEVARDNADZE on Friday presented a "zero variant" draft proposal to parliament. The agreement would allow Georgia to have its debts to Russia rescheduled in exchange for the refusal to lay claims to the Soviet property inherited by Russia. Some of the politicians immediately branded it as "SHEVARDNADZE's surrender to Russia" and ridiculed the prospect of giving up claims to the republic's \$5 billion chunk in the former Soviet property, given that the Georgian debts to Russia are estimated at \$179 million, Itar-Tass reported. SHEVARDNADZE had previously insisted that a "zero variant" agreement is inevitable, as "every country of the former USSR, except Georgia and Ukraine, has accepted it. We have to submit [the draft agreement] to the country's parliament so that it can find the relevant solution." **Intercon** sources report that the "zero variant" has the full support of the US government.

Aliyev Establishes Oil Fund

- Azeri President Geidar ALIYEV issued a decree on December 29th establishing the Oil Fund of the

Republic of Azerbaijan. The Oil Fund is an independent extra-budgetary entity responsible to the Head of State. The Azerbaijan Newsletter reported that the Fund can finance some investment projects of national significance upon a special decision, but its funds cannot be used for loans or covering expenses of government structures. Funding for such investment projects will come primarily from interest earned on Oil Fund's deposits in international banks. The Fund's income will be based on profits from sales of crude and gas, oil bonuses, various other payments within the framework of oil contacts, and earning from the Fund's investments. A total of \$270 million has been allocated for the Oil Fund's account. ALIYEV appointed Samir SHARIFOV, formerly a top level official in the Azerbaijan Central Bank, to be the Oil Fund's Executive Director.

China Delivers Military Supplies To Kyrgyzstan

- China on Saturday delivered 40 tons of military supplies worth five million yuan (\$600,000) to Kyrgyzstan as part of joint efforts to combat "extremist" groups in Central Asia. Military officials say the gift will provide uniforms and boots for more than half Kyrgyzstan's 10,000-strong armed forces. Last year, China donated 70 pre-fabricated buildings for border guard troops, on top of a five million yuan grant in April, 1999. The two sides, which will start on delineating their common border this spring, have been drawn toward closer military cooperation in recent years as they confront the perceived threat from separatist and religious radical groups. China has become increasingly concerned about the activities of ethnic Uighur separatists in its Xinjiang province, which borders Kyrgyzstan. Uighurs based in Central Asia have been active in supporting the province's secessionist bid.

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