

The Central Bank of the Russian Federation (Bank of Russia)

BANKING SUPERVISION REPORT 2002

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LIST OF ABBREVIATIONS USED IN THE REPORT

ARB	Association of Russian Banks
ARCO	Agency for the Restructuring of Credit Organisations
BCBS	Basel Committee on Banking Supervision
BSC	Bank of Russia's Banking Supervision Committee
EWS	Early Warning System
FATF	Financial Action Task Force on Money Laundering
FMC	Financial Monitoring Committee of the Russian Federation
FSAP	Financial Sector Assessment Programme
FSI	Financial Soundness Indicators
GDP	Gross Domestic Product
IAS/IFRS	International Accounting Standards/International Financial Reporting Standards
ILO	International Labour Organisation
IMF	International Monetary Fund
LLP	Loan Loss Provisions
MICEX	Moscow Interbank Currency Exchange
OCP	Open Currency Position
RTS	Russian Trading System

Foreword

The development of banking has received special attention quite lately. Sustainable economic growth depends greatly on how efficiently the banking sector operates. By improving the allocation of resources and decreasing entities' costs an efficient banking sector raises labour productivity and reduces the vulnerability of the economy. Stability in the banking sector is now a precondition of steady economic advancement and normal development of a society.

Rapid growth in the volume of banking operations, adoption of advanced technologies, the use of increasingly sophisticated banking products and financial instruments and changing profile of risks impose more stringent requirements on banking supervision.

While seeking to ensure banking sector stability and protect the interests of creditors and depositors of credit institutions, the Bank of Russia does its best to keep the public informed of the key issues and trends in the development of the banking industry and banking supervision.

Publication of banking supervision reports, which is common practice in many countries, is dictated by the importance of banking supervision as a means of ensuring stability of the banking sector and the national financial system at large. A new analytical publication of the Bank of Russia will discuss in more detail the issues of banking sector stability, including those not dealt with in the Bank of Russia's Annual Report.

This Report of the Bank of Russia is designed to inform both professionals and the general public of banking risks, the dynamics of banking sector macroprudential indicators, systemic stability of the banking sector and prospects for its development. The Report provides a comprehensive review of the system of banking regulation and supervision established in the Russian Federation, assessment of its compliance with internationally accepted standards and information on the principal areas of work of the Bank of Russia's supervisors during the past year. It also describes in some detail the measures the Bank of Russia has taken and plans to take to upgrade the system of banking regulation and supervision.

I would like to express the hope that the present Bank of Russia's Banking Supervision Report will become a useful source of information for all stakeholders, including representatives of the bodies of power, the business community and the public at large in Russia and elsewhere.

Sergei M. Ignatyev,

**Chairman
Bank of Russia**

I. THE BANKING REGULATION AND SUPERVISION IN RUSSIA

The contemporary banking sector in Russia has largely been formed in the past 15 years of market reforms. Today, it operates on market principles, providing the economy with basic banking services, and it is the basic element of financial intermediation. The commercial principles guiding the activities of credit institutions and a two-tier structure (the Central Bank of the Russian Federation is the first tier and credit institutions are the second) are crucial to the organisation of the Russian banking system, while a broad range of functions it fulfils, making banking in Russia a universal business, is its typical feature. Today the Russian banking sector is developing more rapidly and is closer to internationally accepted principles of market relations than any other sector of the Russian economy.

I.1. The banking regulation and supervision system: general characteristics

I.1.1. Legal framework of banking regulation and supervision

In most countries, the banking sector, as a financial intermediary, belongs to the sectors most subjected to state regulation. In Russia, banking regulation and supervision are organised by the Bank of Russia.

The principles of the present system of banking regulation and supervision were laid down by the Bank of Russia in the first half of the 1990s. The amendments to the banking legislation in 1995 and 1996 considerably strengthened the legal framework of banking and banking regulation and supervision. The amendments of 2001 and 2002 created additional opportunities for effective banking regulation and supervision implemented by the Bank of Russia.

A key element of the legal status of the Bank of Russia is its independence, a principle whereby the Bank of Russia fulfils its functions and exercises the powers granted to it by the applicable legislation independently from other federal and regional bodies of powers and local self-government. Another important characteristic of the legal status of the Bank of Russia is non-interference in the day-to-day activities of credit institutions.

The purposes of the Bank of Russia are set out in the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia).” In seeking to facilitate the development of and strengthen the banking system, the Bank of Russia, pursuant to Article 56 of the above Law, is a body of banking regulation and banking supervision, which constantly oversees the observance by credit institutions and banking groups of the banking legislation, anti-money-laundering laws and laws countering the financing of terrorism and Bank of Russia’s regulations and requirements.

Banking sector development and upgrading of the banking regulation and supervision system are constantly in the focus of attention of the National Banking Board (NBB), a collegiate body of the Bank of Russia comprised of representatives of the President, both chambers of the State Assembly (Parliament) and the Government of the Russian Federation as well as the Bank of Russia Chairman. The governing bodies of the Bank of Russia are the Board of Directors and Chairman of the Bank of

Russia. Information from the Board of Directors on issues relating to banking regulation and supervision is considered by the NBB on a quarterly basis.

Under Article 56 of the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia),” adopted in June 2002, the Bank of Russia performs its regulatory and supervisory functions through the Banking Supervision Committee (BSC), a permanent body within the Bank of Russia. A survey on issues pertaining to the development of banking regulation and supervision, including the analysis of the state of the Russian banking sector, is presented each year (as part of the Annual Report) to the State Duma of the Federal Assembly of the Russian Federation, to which the Bank of Russia is accountable.

The effectiveness of banking regulation and supervision depends, to a great extent, on whether it has an adequate legal framework. At present, Russia has a set of laws that regulate all principal aspects of functioning of the Bank of Russia and credit institutions (see Box 1).

Box 1. Key federal laws on banking regulation and supervision:

- ***Law No. 86-FZ “On the Central Bank of the Russian Federation (Bank of Russia)”, dated July 10, 2002 (as amended)***, establishes the status, purposes, functions and powers of the Bank of Russia.
- ***Law No. 17-FZ “On Banks and Banking Activities”, dated February 3, 1996 (as amended)***, defines a credit institution (bank and a non-banking credit institution) and the Russian banking system, contains a list of banking operations and transactions and formulates the principles of establishing, functioning and liquidating credit institutions in Russia.
- ***Law No. 40-FZ “On Insolvency (Bankruptcy) of Credit Institutions”, dated February 25, 1999 (as amended)***, establishes the procedure for implementing measures to prevent insolvency (bankruptcy) of credit institutions, declaring credit institutions insolvent (bankrupt) and liquidating them by initiating bankruptcy proceedings.
- ***Law No. 144-FZ “On the Restructuring of Credit Institutions”, dated July 8, 1999 (as amended)***, establishes the procedure for restructuring of credit institutions by implementing measures to overcome their financial instability and restore solvency or liquidate them in compliance with Russian legislation.
- ***Law No. 117-FZ “On Protecting Competition on the Financial Services Market”, dated June 23, 1999 (as amended)***, regulates relations that influence competition on the securities market, banking services market, insurance market and other financial services markets and are connected with the protection of competition on the financial services market.
- ***Law No. 115-FZ “On Countering the Legalisation (Laundering) of Criminally Gained Income and the Financing of Terrorism”, dated August 7, 2001 (as amended)***, is designed to protect the rights and legitimate interests of citizens, society and the state by creating a legal mechanism against money laundering and terrorist financing.

I.1.2. Purposes and tasks of the Bank of Russia in the field of banking regulation and supervision

The Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)” stipulates that the principal objectives of banking regulation and supervision are to maintain stability of the Russian banking system and protect the interests of its creditors and depositors. The Bank of Russia has consistently sought to achieve the objectives set in Chapter X of the Law and set out in the Banking Sector Development Strategy, adopted by the Government and Bank of Russia in December 2001. In the medium term, the Bank of Russia supervisors are to accomplish tasks that will help strengthen stability of the banking sector and increase its credibility in the eyes of creditors and depositors, reduce to a minimum the possibility of a systemic banking crisis, prevent any misuse of credit institutions for dishonest purposes and make banking more transparent. These tasks are as follows:

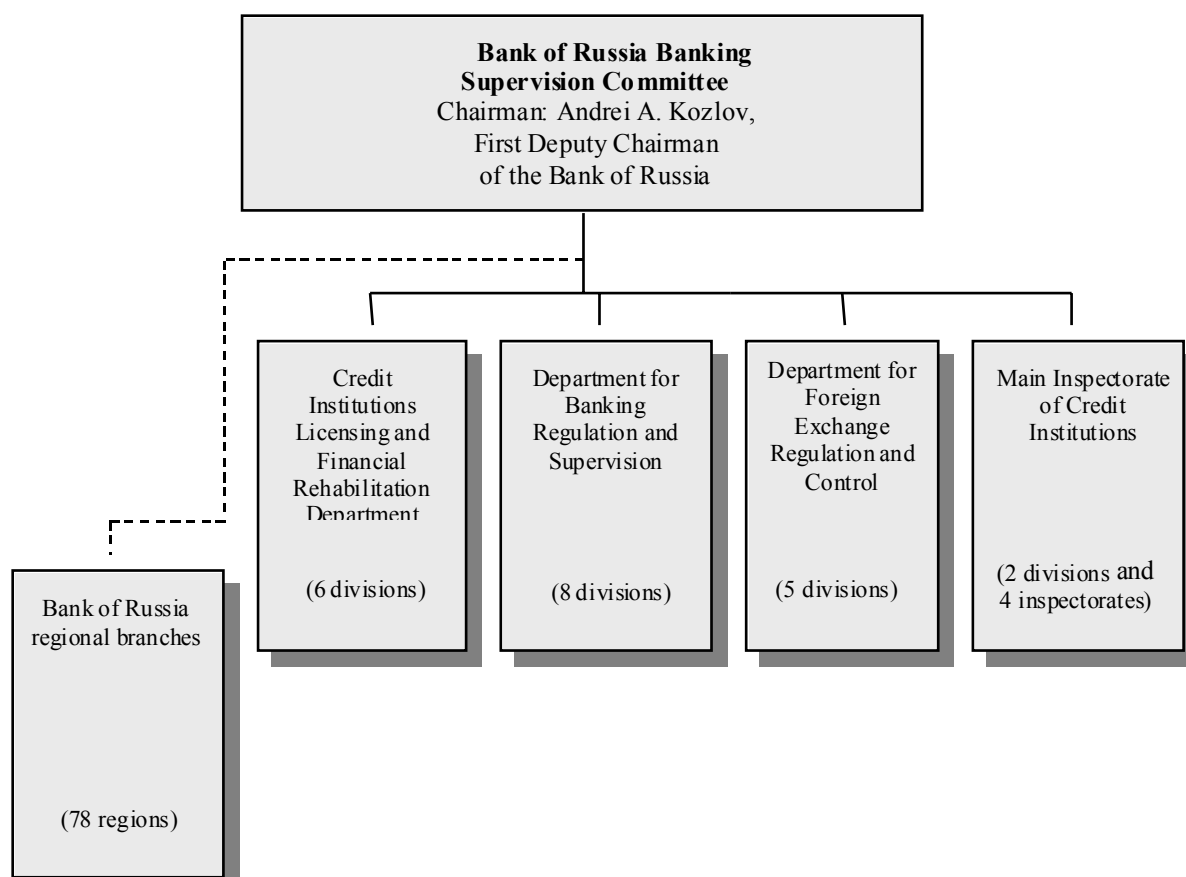
- developing the banking regulation system and implementing banking supervision by using internationally accepted standards, including the upgrading of the licensing procedures, on-going supervision, including the early warning system, and the licence revocation procedures;
- implementing the International Accounting Standards/International Financial Reporting Standards (IAS/IFRS) in the banking sector and using credit institutions' financial statements compiled according to the IAS/IFRS for analysis of credit institutions' activities when fulfilling supervisory functions;
- ensuring effective control over the legitimacy of the authorised capital formation and the origin of founders' (members') funds with the aim of preventing financially unsound persons from establishing control over credit institutions;
- preventing persons who fail to meet fitness and propriety requirements established by federal laws and the Bank of Russia's regulations and persons with a dubious business reputation from participating in managing credit institutions;
- creating conditions that will help raising the standard of corporate governance in credit institutions and expanding the role of internal control systems;
- enhancing the efficiency of bankruptcy and liquidation procedures in credit institutions;
- enhancing the efficiency and improving the quality of audits by introducing international audit, accounting and reporting standards;
- organising and conducting on-site inspections to evaluate the risks assumed and the quality of assets, the appropriateness of own funds (capital) formation and their adequacy, financial condition of credit institutions and their risk management and internal control systems;
- disclosing information on the state and development of the banking services market in Russia.

The Bank of Russia also regards as its strategic goal the creation of conditions providing for increased efficiency of the banking sector and its functional role in the economy. Implementation of this task requires to reduce risks of banking, prices of banking products and services, especially loans, lengthen maturity and lower credit institutions' costs of funding, improve the quality of capital (own funds) and cut credit institutions' expenses, including administrative costs.

I.1.3. Bank of Russia's banking supervisory structures

The activities of the supervisory divisions of the Bank of Russia are co-ordinated by the BSC, headed by the Bank of Russia's First Deputy Chairman. The BSC is responsible for drafting proposals on implementation of banking regulatory and supervisory policies. These proposals are put into practice by the following divisions of the Bank of Russia central office: the Department for Banking Regulation and Supervision, Credit Institutions Licensing and Financial Rehabilitation Department, Department for Foreign Exchange Regulation and Control and Main Inspectorate of Credit Institutions (see Box 2). The principal objectives of these divisions is methodological and organisational provision of the Bank of Russia's functions in the field of banking regulation and supervision during the entire "life-cycle" of a credit institution (from its emergence on the banking services market to orderly liquidation procedures). Specific tasks and functions of the departments are approved by the Board of Directors and formalised in Bank of Russia internal regulations.

Box 2. Bank of Russia's banking supervisory structures (as of January 1, 2003)



As part of single centralised system of the Bank of Russia, regional divisions, such as regional branches and national banks of the republics within the Russian Federation, also perform certain regulatory and supervisory functions. As of January 1, 2003, the Bank of Russia system comprised 59 regional branches and 19 national banks.

In the field of banking regulation and supervision, the regional divisions are responsible for analysing the activities and revealing true financial condition of credit institutions, carrying out practical measures to upgrade and strengthen the banking system in compliance with Bank of Russia instructions. They also prepare decisions on registration and liquidation of credit institutions. The Bank of Russia makes constant efforts to enhance the efficiency of its regional network. In November 2002 a national conference was held to discuss a wide range of issues relating to banking regulation and supervision. The Bank of Russia's regional branches received practical recommendations on improvement of co-operation between their supervisory divisions, detection of problems in credit institutions at early stages, implementation of risk-focused supervision of credit institutions and supervision on a consolidated basis, as well as introduction of the institute of curators of credit institutions.

I.1.4. Banking supervisory staff

The supervisory divisions of the Bank of Russia employ about 4,100 experts, of whom more than 90% work in the regional branches and about 10% in the central office. Most of them (93%) have a higher education and almost a quarter have worked in the banking system for 15 years and more (see Table 1 in the Statistical appendix).

One of the most important projects that requires substantial upgrading of Bank of Russia supervision staff is an experiment with the institute of curators of credit institutions. For this purpose, a group of experts of both central offices and regional divisions of the Bank of Russia began their training in curatorship and inspection in 2002 at leading financial and economic institutions of higher education, such as the Financial Academy and the Academy of National Economy.

I.2. The development of the banking regulation and supervision system in accordance with international standards

I.2.1. Compliance with the Basel Core Principles for Effective Banking Supervision

In 2002, the Bank of Russia continued to bring the banking regulation system into compliance with internationally accepted standards, especially those contained in the Basel Committee Papers.¹

This work was substantially supported by the International Monetary Fund (IMF) and the World Bank. The support was provided within the framework of the Financial Sector Assessment Programme (FSAP) (see I.10.1. Participation in the Financial Sector Assessment Programme). With the help of these organisations, the

¹ In April 1997, the Basel Committee published the Core Principles for Effective Banking Supervision, which contain 25 principles considered globally as the fundamentals for organising effective banking regulation and supervision.

Bank of Russia identified the areas of banking legislation, banking regulation and banking supervision that needed to be upgraded.

Specifically, while assessing the system of banking regulation and supervision from the viewpoint of its compliance with the capital adequacy principle (CP6), it was deemed expedient to place some limits on the excessively broad powers of credit institutions in revaluation of their property. This problem was resolved with the adoption of a new version of the Bank of Russia's Regulation "On the Methodology of Calculating Credit Institutions' Own Funds (Capital)", which stipulated that revaluation gains should not be included in the calculation of the additional sources of credit institutions' own funds (capital) more than once in three years.

In the course of assessment from the viewpoint of compliance with the lending policy principle (CP7), it was deemed necessary to advise management (boards of directors) of credit institutions to adopt and implement investment criteria. Reports on these criteria should be regularly reviewed in the future. In addition, credit institutions should take decisions on granting loans without pressure of any third party and conflicts of interest. Corresponding changes are to be made in the Bank of Russia regulations on internal controls in banks.

As for the observance of the loan valuation and loan loss provision principle (CP8), it has been found out that a fixed provisioning rate does not always meet credit institutions' needs from the viewpoint of adequate asset valuation. This assessment was taken into consideration in drafting a new version of the Bank of Russia Instruction "On the Procedure for Creating and Using a Loan Loss Provisions", which provides for the introduction of discretionary approach to provisioning within certain margin of rates.

In assessment of the system of banking regulation and supervision from the viewpoint of its compliance with the connected lending principle (CP10), it was deemed expedient to broaden the powers of the Bank of Russia, including the right to make requirements for credit institutions to comply with certain conditions and procedures while granting loans to connected parties. To this end, the Bank of Russia drafted the Operating Ordinance "On Connected Lending," which recommended banks to establish additional control over the risks involved in lending to connected parties.

Recommendations have been also worked out with regard to the internal control and audit principle (CP14), which regulates supervisors' internal control requirements for credit institutions. These recommendations were taken into account in drafting the Bank of Russia Regulation "On Organising Internal Control in Credit Institutions and Banking Groups."

Special attention was paid to studying issues related to the exchange of information between banking supervision authorities, including co-operation with bank supervisors in foreign countries (assessment of compliance with Basel principles CP1(6), CP24 and CP25). This work resulted in the adoption of amendments to the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)" in 2002. Article 51 of this Law grants to the Bank of Russia the right to pass to foreign supervisory authorities information and documents received from credit institutions in

the course of supervision. The Article provides, however, that such documents should not contain information about the operations conducted by credit institutions and their customers.

1.2.2. Upgrading laws and standards regulating activities of credit institutions

In conformity with the Banking Sector Development Strategy, the Bank of Russia in 2002 actively participated in the efforts to upgrade the legislation regulating the activities of credit institutions.

The most important decisions aimed at strengthening the legal basis of banking regulation were implemented in the new Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)” (see Box 3). In addition, the Bank of Russia was effectively involved in drafting laws on insurance of household deposits in banks of the Russian Federation and on the credit history bureau.

Box 3. New provisions of the new Bank of Russia Law pertaining to banking regulation and supervision

- The Bank of Russia is to supervise not only credit institutions, but also banking groups (part one of Article 56 and part two of Article 62);
- the Law stipulates that the Bank of Russia may set prudential requirements for banking groups (Articles 62, 64, 65, 67, 70 and 71);
- the procedure for fining credit institutions by the Bank of Russia for non-compliance with prudential requirements is specified;
- whenever the Bank of Russia introduces new rules, they apply to accounting and statistical reports compiled for the period beginning no sooner than the date on which the rules were published (Article 57);
- the Law extends authorities of the Bank of Russia to take corrective actions in case of various violations by credit institutions (Article 74): it stipulates that the Bank of Russia may prohibit reorganisation of a credit institution if its reorganisation may create grounds for the implementation of bankruptcy-prevention measures under the Federal Law “On Insolvency (Bankruptcy) of Credit Institutions”. The Bank of Russia is also empowered to recommend the founders (members) of a credit institution to take actions designed to increase its equity capital to the required level;
- the Law brings into conformity with the Federal Law “On Banks and Banking Activities” the standards relating to the establishment by the Bank of Russia of fitness and propriety requirements for persons nominated to managerial positions in a credit institution (Article 60), obtaining prior consent of the Bank of Russia for the acquisition of more than 20% of shares (stakes) in a credit institution and notification of the Bank of Russia about the acquisition of more than 5% of shares (stakes) in a credit institution (Article 61).

The changes and amendments that came into force in 2002 were of great importance for the development and upgrading of legal environment, as they helped significantly to improve the regulatory and supervisory framework of banking regulation and supervision in several major areas.

Registration of credit institutions and licensing banking activities. Bank of Russia Instruction No. 75-I, dated July 23, 1998, “On the Procedure for Applying Federal Laws Regulating the Procedure for Registering Credit Institutions and Licensing Banking Activities,” has taken account of the following changes made in federal legislation:

- the co-operation procedure between the Bank of Russia and a federal body of executive power concerning the state registration of credit institutions and state registration of changes in their founding documents;

- the enlarged list of persons who must comply with fitness and propriety requirements. At present, such requirements are imposed for an individual executive body and his deputies, members of a collegiate executive body of a credit institution, chief accountant and deputy chief accountants of a credit institution, chief executive officer and his deputies and chief accountant and deputy chief accountants of a branch of a credit institution and members of the board of directors (supervisory board) of a credit institution;

- an individual executive body and her deputies, members of a collegiate executive body and chief accountant of a credit institution, the head of a branch of a credit institution are prohibited from concurrently occupying positions in organisations whose list is established by law;

- the Bank of Russia may reject a request for the purchase of more than 20 percent of shares (stakes) in a credit institution if the person who intends to buy the shares (stakes) in a credit institution has been found guilty by a court of law of breaking the bankruptcy law or deliberately causing and (or) initiating a fictitious bankruptcy and in other cases stipulated by the federal laws;

- the Law has established the cases in which the Bank of Russia must reject the request for the purchase of more than 20 percent of shares (stakes) in a credit institution.

The Law has also tightened the requirement for the founders (members) of credit institutions to ensure transparency of the structure of founders (shareholders) and their groups when creating a new credit institution, expanding the range of activities by obtaining additional banking licences, changing the status of a credit institution (from a non-bank credit institution to a bank or from a bank to a non-bank credit institution) and reorganising a credit institution.

While implementing the provision of the Banking Sector Development Strategy that requires the creation of equal conditions for residents’ and non-residents’ access to the Russian banking services market, the Bank of Russia in 2002 lowered the minimum authorised capital requirement for a subsidiary credit institution established by a foreign bank from 10 to 5 million euros.

Business plan evaluation. The requirements for the content of business plans of credit institutions and the procedure for submitting them to the Bank of Russia are established in Bank of Russia Ordinance No. 1176-U, dated July 5, 2002, “On Business Plans of Credit Institutions”. The aim of the ordinance is to enable the Bank

of Russia to evaluate the ability of a credit institution to ensure financial stability, comply with prudential standards and reserve requirements and observe the legislation protecting the interests of creditors and depositors. The instruction is designed to help the Bank of Russia to evaluate the feasibility of a credit institution's commercial projects, make sure that a credit institution really intends to stay on the banking services market for a long time and that it has an effective risk management system.

Capital quality. In 2002, the Bank of Russia drafted a new version of its Regulation No. 215-P, "On the Procedure for Calculation of Credit Institution's Own Funds (Capital)"², which excluded from the capital calculation some sources of own funds, such as authorised capital, income from issuing securities, profit, etc. which are formed using inappropriate assets, especially property provided to the investor by the credit institution (directly or via third parties).

The Bank of Russia drafted the Ordinance "On Actions in Response to Instances (Evidence) of the Formation of Own Funds (Capital) or a Part Thereof Using Inappropriate Assets",³ which specified the procedure of imposing requirements on credit institutions to correct capital. The procedure of imposing requirements and the sequence of the Bank of Russia's actions in case of the formation of capital using inappropriate assets ensure that the decisions made on the matter are objective and balanced and offer an opportunity to discuss the problem with the bank concerned, allowing it to amend the situation. A final decision is to be taken by the BSC.

Loan-loss provisioning (LLP). In 2002, the Bank of Russia drafted and received the approval for the Regulations "On the Procedure for Making Allowances for Estimated Losses"⁴ and "On the Procedure for Making and Use of Allowances for Estimated Loan Losses". These documents elaborate on the principle of informed judgement in credit risk evaluation and introduce the following changes:

- they considerably broaden the range of risk factors that serve credit institutions as a basis for making informed judgements on the level of risk of estimated losses;
- they introduce the criterion of materiality, let credit institutions make allowances on a portfolio of similar claims, each of them being immaterial from the viewpoint of the volume of activity, without making an informed judgement on every claim;
- they specify the role of the collateral in the pattern of provisioning for estimated losses and stipulate that allowance should be reduced by the cost of highly liquid collateral;
- they establish five risk groups, allowing a credit institution not to provide an allowance for risk-free group 1 claims;
- they introduce discretionary approach to provisioning, within certain margin of rates, to enable banks and the supervising authority to make effective use of the informed judgement principle.

² Regulation No. 215-P, dated February 10, 2003, came into effect in March 2003.

³ Ordinance No. 1246-U, dated February 10, 2003, came into effect in March 2003.

⁴ Regulation No. 232-P, dated July 9, 2003, came into effect in July 2003.

In addition, in connection with the coming into force of Chapter 25 of the Tax Code of the Russian Federation, the Bank of Russia issued regulations explaining the specifics of the loan loss provisioning in connection with the changes in legislation, including the case of impaired loans recognised as such for the purpose of tax accounting.

Consolidated supervision. In accordance with the Banking Sector Development Strategy, the Bank of Russia in 2002 made every effort to upgrade the legislative framework of consolidated supervision.

As the new version of the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)” extended the supervisory powers of the Bank of Russia to banking groups, giving the Bank of Russia the right to set prudential standards for them and take supervisory action in response to a situation endangering the interests of creditors and depositors of credit institutions within banking groups, the Bank of Russia elaborated and put in force a number of regulations designed to improve consolidated supervision. Thus, Bank of Russia Regulation No. 191-P, dated July 30, 2002, “On Consolidated Reporting,” established the procedure for calculating own funds (capital) and prudential regulations for a banking/consolidated group and specified the procedure for compiling consolidated reports, especially from the viewpoint of accounting of transactions with securities. Bank of Russia Ordinance No. 1114-U, dated February 21, 2002, “On Amending Bank of Russia Regulation No. 85-P, dated August 5, 1999, “On the Procedure for Using Reported Data of Non-Credit Institutions Members of a Group in Compiling Consolidated Reports by Credit Institutions”, regulated the procedure for using data of non-credit institutions members of a banking/consolidated group in calculating required ratios for the banking/consolidated group and specified the procedure for including data of non-credit institutions members of banking/consolidated groups in consolidated statements.

To accomplish the tasks set in the Banking Sector Development Strategy, the Bank of Russia began to formulate the principles of evaluating consolidated risk assumed by credit institutions, directly and indirectly, that is, through related structures, taking into account the risks involved in the transactions conducted by non-credit institutions participating in a banking/consolidated group, in order to identify the areas where a credit institution has taken increased risks on a consolidated basis. Such risk evaluation practices will allow supervisors to conduct a comprehensive analysis of respective credit institutions, evaluating the standard of their governance, including risk management.

Lending to connected parties. In 2002, the Bank of Russia drafted the Operating Ordinance “On Connected Lending”,⁵ which recommended banks to establish additional controls over risks that arise when granting loans to persons connected with originating bank. Specifically, the document stipulated that a bank should not grant loans to borrowers related to it on more preferential terms than to an “ordinary” borrowers. Another requirement is that the decision to extend a loan to a borrower connected to a creditor bank in excess of the limits set by the bank’s internal documents should be approved by a shareholders’ (members’) meeting or the bank’s

⁵ Put into effect by Bank of Russia Operating Ordinance No. 68-T, dated May 5, 2003.

board of directors. Persons who are granted loans cannot participate in drafting proposals on extending loans or in making decisions on extending them.

Corporate governance. Many elements of the contemporary system of corporate governance are already used in Russian banking today. At the same time, the federal legislation does not regulate a number of key areas of corporate governance in credit institutions, such as setting requirements for managerial decision-making, preventing conflicts of interest in the management of credit institutions, ensuring the priority of the interests of a credit institution and its creditors and depositors over the interests of individual owners and managers of the credit institution, and establishing personal responsibility of the members of the board of directors (supervisory board) and executive bodies. In addition, a survey on corporate governance of a fairly large number of credit institutions conducted by the Bank of Russia in 2002 revealed quite a few common flaws in the organisation of boards of directors (supervisory boards). Specifically, there was not enough or no delimitation of powers, some boards of directors (supervisory boards) had no independent directors among their members, some credit institutions had no coherent long-term development strategy or short-term policy, others failed to work out a systemic approach to risk management, while still others disclosed information largely of promotional value.

In line with the Banking Sector Development Strategy, the Bank of Russia in 2002 took steps towards upgrading legislation on corporate governance in credit institutions. In drafting laws and regulations in this field, it attached great importance to the problem of the priority of the interests of a credit institution and its creditors and depositors over the interests of individual founders (members) and managers, the prevention of conflicts of interest in management of credit institutions and the establishment of the managerial decision-making system's requirements.

The opacity of the structure of property and management of credit institutions is one of the factors that have a negative effect on the quality of corporate governance in the banking sector. Aware of this, the Bank of Russia in 2002 tackled the task of increasing transparency of information on the owners (managers) of credit institutions, upgrading the system of requirements related to their founders (members).

Information provided by banks in compliance with Bank of Russia's regulations issued in 2002, such as Regulation No. 227-P, dated May 14, 2003, "On the Accounting Procedure and the Procedure for Providing Information on Persons Related to Credit Institutions" and Regulation No. 197-P, dated September 19, 2002, "On the Procedure for Providing Information on Bank Holding Companies," allowed Bank of Russia supervisors to analyse the structure of relations between members of credit institutions and enhance the efficiency of the procedure of giving Bank of Russia prior consent for the purchase by a group of people of more than 20% of shares (stakes) in a credit institution. This procedure helps to identify groups of people, banking groups and bank holding companies and to determine which people have a direct or indirect material influence on decisions made by the management of a credit institution.

Internal controls. In organising and implementing internal controls today, credit institutions are guided by Bank of Russia Regulation No. 509, dated August 28,

1997, “On Organising Internal Control in Banks” and Bank of Russia Ordinance No. 603-U, dated July 7, 1999, “On the Procedure for Implementing Internal Control over Compliance by Credit Institutions with the Financial Market Legislation” (with regard to the regulation of compliance control in credit institutions). These regulations need to be upgraded, however, because they fail to comply with all the requirements of the Basel Committee’s Core Principles with regard to the organisation of internal control in credit institutions. In addition, far from all credit institutions pay due attention to internal control. Some of them regard internal control and the organisation of internal control services as a mere formality.

Aware of this, the Bank of Russia in 2002 continued to work on the draft Regulation “On Organising Internal Control in Credit Institutions and Banking Groups,” which takes into account not only six years of experience in implementing the Regulation “On Organising Internal Control in Banks,” but also the Basel Committee’s new principles and recommendations on internal control in credit institutions.⁶ The essence of the new approaches is that the standards for determining the elements of internal control and the means (methods) of conducting inspections by the internal control service and some other hitherto non-binding standards are to be specified, expanded and presented in the form of regulatory requirements. The Bank of Russia is also to detail the procedure for organising internal control systems, establishing the objects and subjects of internal control and formulating their powers, rights and duties. In addition, the Bank of Russia is to extend the internal control requirements to banks as well as non-bank credit institutions and banking groups.

The need to create effective internal control systems also arises from the legislation against money laundering and the financing of terrorism (see also I.8).

Withdrawing insolvent credit institutions from the banking services market.

Amendments to the Federal Law “On Banks and Banking Activities” and the subsequent changes in Bank of Russia regulations require that the Bank of Russia should revoke the banking licence from a credit institution in the following cases:

- if a credit institution’s capital adequacy ratio falls below 2%;
- if a credit institution’s own funds (capital) are lower than the minimum amount of authorised capital, established by the Bank of Russia on the date of the state registration of the credit institution;
- if a credit institution fails to meet the Bank of Russia requirements to bring its authorised capital in compliance with its own funds (capital) by the deadline set by the Federal Law “On Insolvency (Bankruptcy) of Credit Institutions;”
- if a credit institution is incapable of meeting creditors’ claims on pecuniary obligations and (or) making compulsory payments within one month of the date on which they must be met and (or) paid. It is stipulated that the above

⁶ Basel Committee recommendations:

- Framework for internal control systems in banking organisations (September 1998);
- Internal audit in banks and supervisor’s relationship with auditors (August 2001);
- Customer due diligence for banks (October 2001);
- The relationship between banking supervisors and banks’ external auditors (January 2002).

claims should total no less than 1,000 times the minimum wage established by the federal law.

I.3. Regulating access to the banking services market

Under the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)” and Federal Law “On Banks and Banking Activities,” when making decisions on the state registration of new credit institutions and granting them a banking licence, the Bank of Russia must exercise control over compliance with the following requirements established by banking legislation and Bank of Russia regulations:

- the Bank of Russia must ensure that a credit institution meets the minimum authorised capital requirement;
- the Bank of Russia must prevent the establishment of credit institutions that are incapable of ensuring their own financial stability and have no clear prospects of further activities;
- the Bank of Russia must be certain that the funds of the founders (members) of a credit institution come from legitimate sources in order to prevent financially unsound and dishonest persons from establishing control over the credit institution;
- the Bank of Russia must ensure that the founders of a credit institution do not exceed the limit established for the amount of authorised capital that may be paid in with certain kinds of property other than money;
- the Bank of Russia must be certain that candidates for the position of members of the board of directors (supervisory board), individual executive body and her deputies, members of a collegiate executive body and chief accountant of a credit institution and her deputies meet the corresponding fitness and propriety and business reputation requirements established by the Bank of Russia.

Should a legal entity or private individual or a group of legal entities that are subsidiary to or dependent on one another or a group of persons bound by an agreement buy more than 20% of shares (stakes in the authorised capital) of a credit institution, the purchaser should obtain prior consent from the Bank of Russia for this transaction. The Bank of Russia may reject the request for the purchase of more than 20% of shares (stakes) in a credit institution if it is not satisfied with the purchaser's financial condition or if the purchaser has been previously found guilty by a court of law of causing a credit institution to sustain losses when fulfilling the duties of a member of its board of directors (supervisory board), individual executive body or his deputy and (or) a member of a collegiate executive body, and also in other cases stipulated by the federal laws and Bank of Russia regulations issued in pursuance of these laws.

When a newly created institution is being established, its founders must present to the Bank of Russia its business plan, approved by a founders' meeting,

which should contain general information on the credit institution being set up, its purposes and tasks, market policy for the next two years and management system, including internal controls.

The rate of creating credit institutions significantly accelerated in 2002 compared to 2000 and 2001: 35 new banks and six non-bank credit institutions were registered in 2002. The number of operating credit institutions rose from 1,319 to 1,329. It should be noted that the applicable legislation has given credit institutions universal opportunities for the development of the banking business and the following statistics bear this out:

- 90% of all credit institutions that were in operation at the beginning of 2003 had the right to take household deposits;
- 63% of the total number of operating credit institutions conducted banking operations in roubles and foreign currency;
- 22% of credit institutions had general licences;
- 13% of credit institutions had the right to conduct operations with precious metals.

The capital base of credit institutions was strengthened in 2002 in the interest of banking business development and the observance of Bank of Russia regulations by members (shareholders) of credit institutions. As of January 1, 2003, the aggregate registered authorised capital of credit institutions amounted to 300.4 billion roubles, an annual increase of 15.1%. The number of credit institutions with an authorised capital in excess of 300 million roubles increased 1.3 times to 170, or 12.8% of the total.

The strengthening of the capital base of Russian credit institutions was accompanied by their enlargement through mergers. Three mergers of credit institutions were registered in 2002.

I4. The capitalisation of credit institutions and the issue of securities by banks

Credit institutions tended to scale down their security issuing activity in 2002. Over the year, 330 credit institutions registered 355 security issues to the amount of 61 billion roubles (in 2001, 424 credit institutions registered 482 security issues to the amount of 110 billion roubles). The decrease may be attributable to the tightening of the procedure for credit institutions to increase their authorised capital using their property.

Credit institutions increased their authorised capital mainly by placing additional shares (240 credit institutions placed 262 share issues to the amount of 33.2 billion roubles). As before, the policy of increasing authorised capital by issuing additional shares was typical of credit institutions based in the Moscow Region, but in 2002 large regional banks also stepped up the share issuing activity.

During the year under review, 42 credit institutions with a total authorised capital of 9.2 billion roubles were transformed from limited liability companies into joint-stock companies against 67 credit institutions with an authorised capital of 63.9 billion roubles in 2001.

Although a large number of credit institutions operate as joint-stock companies (838, or 63% of the total), only a small part of credit institutions' shares are traded on the organised securities market and have any interest for potential investors. Most Russian banks are too small to be of any interest for major investors, so their shares are usually placed with former shareholders or investors selected in advance.

Unlike the situation on the stock market, banks' issuing activity on the corporate bond market increased in 2002: 19 credit institutions registered 20 bond issues to the amount of 9.56 billion roubles against 11 credit institutions that registered 15 bond issues to the amount of 4.60 billion roubles in 2001. There was a tendency towards issuing bonds against collateral and using underwriters, mainly on exchanges, such as MICEX, through direct trading at auctions. Such practices make bank bonds an increasingly attractive and safe financial instrument. Third party guarantees, such as irrevocable offers, serve as collateral, as a rule.

As for bank securities traded on the secondary market, they account for about 3% of the trade turnover of Russia's leading exchanges, MICEX and the RTS. The most traded Russian bank shares are those of the Savings Bank (Sberbank). There is stable demand for bank shares on the secondary market too: the most liquid of them are Vneshtorgbank bonds.

I.5. The off-site monitoring of credit institutions

The implementation of adequate decisions in the on-going supervision of credit institutions is a major factor of stability of the banking sector in Russia and protection of the legitimate interests of creditors and depositors of credit institutions. The principal objectives pursued by the Bank of Russia in the field of off-site monitoring in 2002 were to analyse the nature and level of the risks assumed by banks, assess their financial stability and optimise the supervisory regime. The Bank of Russia sought to use to the fullest possible extent the possibilities and powers granted to it by the effective legislation.

The number of sanctions applied to credit institutions in 2002 demonstrate a general fall in the cases of violations of the Bank of Russia's requirements with continued emphasis on preventive measures and reduced frequency of forced corrective actions taken against credit institutions.

Various legitimate measures based on the analysis of the banks' reports in 2002 were taken against violator banks. These measures included informing the management and/or boards of directors (supervisory boards) of 1,187 credit institutions about the shortcomings revealed in their work as well as conducting consultations with managers of 301 banks.

In 2002, the Bank of Russia imposed restrictions and bans on retail deposit taking of 28 banks (64 banks in 2001) and 83 banks were not allowed to open new

branches (131 banks in 2001), 473 banks were fined for violations of prudential standards and 150 banks were ordered to ensure compliance with Bank of Russia's prudential requirements (250 banks in 2001).

The institute of curators. To upgrade banking supervision and shift the emphasis from formal procedures to a substantive evaluation of the situation in a credit institution and implement the risk-focused supervision, in 2002 the Bank of Russia started an experiment to introduce the institute of curators in 10 of its regional branches. A legal framework for the project was provided by Bank of Russia Recommendations on the Experimental Use in Supervisory Practice of the Institute of Curators of Credit Institutions.

“Early warning system” (EWS). Efforts are being made to build a system that will provide for detection of problems in credit institutions at earliest stages. As part of this project different statistical models have been tested to determine the basic elements of the EWS: target and explanatory variables have been selected, planning horizons have been determined and the adequacy and accuracy of the models received have been analysed. Regression and cluster analysis methods were used in carrying out this work. The system is to be put into experimental operation in the second quarter of 2004.

Analysis of the financial condition of banks. To enhance the efficiency of supervision and standardise the procedures for assessing financial condition of credit institutions, the Bank of Russia continued to improve the methodology of analysing the financial condition of banks and upgrade a software system designed for this purpose (it has been installed in all Bank of Russia regional branches). In 2002, the Bank of Russia solved a number of problems including determination of trends of the indicators' analysis of the risks assumed by branches of credit institutions, which made it possible to evaluate the influence of such risks on the financial stability of the credit institutions as a whole.

Accuracy of reporting. To assess the accuracy and authenticity of credit institutions' reports and determine the main areas of credit institutions' activities to be inspected, the Bank of Russia has worked out draft methodology allowing to detect loan and bill schemes used by credit institutions to create a semblance of compliance with prudential standards, make their loan and bill portfolios look better and to reveal violations of payment rules. The Bank of Russia started to use this methodology in conducting inspections of credit institutions in 2002. The work was continued in 2003. In addition, the framework of this methodology has been implemented in the software system called the Analysis of the Financial Condition of a Bank, which is to be test operated in some regional branches of the Bank of Russia in 2003.

Bank performance assessment. When creating conditions for the implementation of the bank deposit insurance system, the Bank of Russia worked to establish criteria for evaluation of the performance of credit institutions, which could be used while giving or denying access of banks to the deposit insurance system. A draft Regulation “On the Assessment of a Bank's Compliance with the Criteria for Access to the Deposit Insurance System” was elaborated by the Bank of Russia and placed for discussion on its official website (www.cbr.ru). In addition to the existing

approaches to assessment of financial stability of credit institutions, the document introduces some new ones, such as relative indicators characterising capital adequacy, asset quality and liquidity and income levels, and also such criteria as transparency of the ownership structure and the quality of current management, including risk management, internal control systems, strategic management and business planning.

Internet-banking. To provide an information framework for the study of the dissemination of new information technologies in banking and their influence on banking, the Bank of Russia drafted the Ordinance “On the Procedure for Informing the Bank of Russia by Credit Institutions on the Introduction and Use of Internet Technologies in Banking.”

The document requires credit institutions to inform the Bank of Russia about opening their sites on the Internet (websites), making changes in the functional designation, capabilities and location of their websites, using websites of other organisations and ceasing using them.

Realising the need to raise significantly the level of disclosure of information on the activities and financial condition of credit institutions, the Bank of Russia drafted recommendations on the contents and management of the websites of credit institutions. The document aims to streamline the process of organising and using websites by credit institutions. The recommendations are designed to reduce banking risks involved in internet-banking, make credit institutions more transparent, and to help customers, including potential ones, receive a full and realistic picture of credit institutions and increase confidence in them.

I.6. The inspection of credit institutions

To maintain stability of the banking sector, protect the interests of creditors and depositors and adopt effective decisions in banking regulation and supervision, the Bank of Russia in 2002 conducted inspections of credit institutions, focusing on the assessment of their true financial condition, the level of risks they assumed, the effectiveness of their governance, including controlling and internal audit, credibility of the accounts and reports presented by credit institutions and their branches.

In 2002, the Bank of Russia conducted 4,600 inspections of credit institutions (1,953 inspections were conducted in main offices and 2,647 in branches of credit institutions). These included 565 comprehensive inspections of main offices and 275 comprehensive inspections of branches of credit institutions and 1,388 selective inspections of main offices and 2,372 selective inspections of branches of credit institutions (see Table 2 in the Statistical appendix).

Inspections of credit institutions whose branches are supervised by Bank of Russia regional branches were co-ordinated by the Bank of Russia regional branches that supervise the main offices of these credit institutions. In 2002 inter-regional inspections of 53 main offices and 107 branches of credit institutions were also conducted.

All main offices and all branches of credit institutions, except the branches of the Savings Bank (Sberbank), were inspected with regard to compliance with the

requirements of the Federal Law “On Countering the Legalisation (Laundering) of Criminally Obtained Incomes,” which came into force in 2002 (see also I.8).

In 2002, the Bank of Russia conducted 2,762 unscheduled inspections of main offices of credit institutions and their branches, or 60% of the total number of inspections. Such inspections were mainly conducted when it had been discovered that the legitimate interests of creditors and depositors could be infringed and when credit institutions intended to broaden the range of their activities and had applied for a general licence.

The principal objectives of the inspections were as follows:

- to assess credit institutions’ compliance with legislation of Russian Federation and regulations and standards of the Bank of Russia;
- to assess the state of accounting and accuracy credibility of the financial, statistical and accounting reports presented to the Bank of Russia;
- to assess credit institutions’ quality of assets and the adequacy of provisions made for possible losses;
- to assess the correctness of the formation of credit institutions’ own funds (capital).

The results of the inspections demonstrated that violations of legislation of Russian Federation and regulations and standards of Bank of Russia in 2002 were mostly committed by credit institutions when conducting lending, foreign exchange and cash operations and in accounting.

As a result of inspections, credit institutions found guilty of non-reporting, mis-reporting were ordered to take remedial action or subjected to other measures under Article 74 of the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia).”

In conformity with the decision made by its Board of Directors (Protocol No. 20 of September 4, 2002) and pursuant to Article 73 of the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)”. In 2002 the Bank of Russia began to implement new principles of inspections of credit institutions. For this purpose, it assigned the task of organising and providing methodological guidance for inspections of credit institutions in Russia to the Bank of Russia Main Inspectorate of Credit Institutions, formed by Bank of Russia Order No. OD-602, dated September 16, 2002. These changes were aimed at encouraging the substantive approach to on-site inspections of credit institutions, based on informed judgements about risk, loan loss provisioning and the effect of the violations and shortcomings detected on the financial condition of a credit institutions and its future.

I.7. The Financial rehabilitation, restructuring and liquidation of credit institutions

In seeking to ensure banking sector stability and protect the interests of creditors and depositors, the Bank of Russia attaches great importance to the detection of problem credit institutions, control over the implementation of measures to prevent their bankruptcy, including the work of the provisional administrations, the timely revocation of banking licences and the liquidation of credit institutions that could not be salvaged.

I.7.1. Financial rehabilitation and restructuring of credit institutions

The number of credit institutions subject to bankruptcy-prevention measures under Article 4 of the Federal Law “On Insolvency (Bankruptcy) of Credit Institutions” continued to decrease in 2002. Unlike the situation in the previous years, in 2002 more credit institutions sought to resolve their problems themselves, enlisting whenever necessary the resources of their members before the Bank of Russia’s regional branches issued their orders.

In 2002, the Bank of Russia controlled the implementation of the financial rehabilitation plans of 64 credit institutions, the majority of which (60%) have restored their financial stability.

The Bank of Russia actively worked with credit institutions whose own funds (capital) were smaller than their registered authorised capital. The number of such credit institutions declined in 2002. Forty-six credit institutions were ordered to match their own funds (capital) with their authorised capital and five credit institutions had their banking licence revoked for failing to fulfil these orders.

To protect the interests of creditors (depositors) of credit institutions, the Bank of Russia in 2002 controlled the activities of 37 provisional administrations appointed to credit institutions in accordance with the applicable legislation (24 of them were appointed in 2002). Provisional administrations were appointed to operating credit institutions and credit institutions whose banking licence had been revoked.

I.7.2. Liquidation of credit institutions

One way to strengthen the banking sector is to withdraw from the banking services market credit institutions that could not be salvaged.

In 2002, the Bank of Russia, guided by Article 74 of the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)” and Articles 20 and 23 of the Federal Law “On Banks and Banking Activities,” ordered the revocation (cancellation) of 26 credit institutions’ banking licences. The amendments made to banking legislation in 2001 broadened the powers of the Bank of Russia to withdraw financially unsound credit institutions from the market before their financial problems made them unable to meet their obligations to creditors (13 credit institutions had no backlogs of outstanding payments by the time their licence was recalled).

In the first half of 2002, 108 credit institutions that had their banking licence revoked were excluded from the State Register of Credit Institutions. In connection with the coming into force of Federal Law No. 129-FZ, dated August 8, 2001, "On the State Registration of Legal Entities," which changed the procedure for registering credit institutions, in the second half of 2002, the Bank of Russia made decisions on state registration of 133 credit institutions. In line with these decisions, the authorised registering agency excluded 104 credit institutions from the Single State Register of Legal Entities in 2002.

Seventy-one credit institutions were wound up in 2002 and liquidation commissions were set up or receivers (liquidators) were appointed in 111 credit institutions.

As of January 1, 2003, the average recovery ratio of creditors' claims during liquidation of credit institutions stood at 7.3%; of these, creditors ranked first to have their claims met had 49.5% of their claims met, creditors ranked second 65.7%, creditors ranked third 53.7%, creditors ranked fourth (debt on payments to the budget) 16.1% and creditors ranked fifth 2.4%.

The Bank of Russia continued to certify receivers (liquidators) of credit institutions and extend and cancel receivers' certificates that were issued earlier. Six credit institutions were transferred from the control of the governmental Agency for the Restructuring of Credit Organisations (ARCO) in 2002; one credit institution under ARCO's control was finally liquidated; one credit institution was restructured without being put under the control of ARCO in accordance with the decision of the ARCO Board of Directors; with regard to three credit institutions, the Bank of Russia decided to extend the term of their restructuring plans.

In 2002, the Bank of Russia implemented the provisions of Article 6 of the Federal Law "On Insolvency (Bankruptcy) of Credit Institutions," which stipulates that in the bankruptcy of an absent credit institution, a Bank of Russia employee may be appointed as the receiver. Bank of Russia employees were appointed by an arbitration court as receivers in five credit institutions declared absent debtors. In addition, the Bank of Russia formed a reserve team of employees who will be nominated as receivers in the bankruptcy of absent credit institutions.

I.8. The countering the legalisation of the criminally gained income (anti-money laundering)

The Federal Law "On Countering the Legalisation (Laundering) of Criminally Gained Income,"⁷ which came into force on February 1, 2002, laid the basis for the construction of an anti-money laundering system in the Russian Federation. The Law assigned to the Bank of Russia, as a supervisory authority, a number of functions designed to ensure the establishment of anti-money laundering system in the banking sector and its effective work, including establishment of specialised internal control; submission of information to the authorised body by credit institutions on transactions

⁷ In connection with the adoption of Federal Law No. 131-FZ, dated October 30, 2002 "On amendments to the Federal Law on Countering the Legalisation (Laundering) of Criminally Gained Income," which came into force on January 3, 2003, the name of the federal law mentioned in the text has been changed as follows: "On Countering the Legalisation (Laundering) of Criminally Gained Income and the Financing of Terrorism."

with money or other property subject to mandatory control and other transactions that may be linked with money laundering; supervision of credit institutions' compliance with the legal requirements in this area.

The Bank of Russia adopted Recommendations for credit institutions to develop internal controls with a view to countering legalisation (laundering) of criminally gained income. Besides, the Bank of Russia made a decision to use its own information and telecommunications networks for passing information received from credit institutions in pursuance of the applicable law to the Financial Monitoring Committee of the Russian Federation (FMC).

In exercising the powers granted to it by legislation to supervise credit institutions' compliance with the amended anti-money laundering law, the Bank of Russia established the corresponding monitoring procedure and worked out standard methods to organise and conduct inspections of credit institutions for the purpose of establishing their compliance with anti-money laundering requirements.

During the year 2002, 1,328 main offices and 2,077 branches of credit institutions were inspected from the viewpoint of their compliance with anti-money laundering legislation. The inspections showed that most credit institutions understood the requirements imposed on them by the law and complied with them in good faith. They have carried out the necessary organisational and technical measures to establish specialised internal controls to prevent money laundering and met the deadlines set for submission of information to the FMC on transactions with money and other property subject to mandatory control.

At the same time, the inspection showed that 9% of the inspected main offices of credit institutions and 11.7% of the total number of inspected branches committed violations of the anti-money laundering legislation. The measures taken against credit institutions that committed such violations ranged from prescriptions to take remedial action to the revocation of banking licences.

The Bank of Russia paid special attention to training experts with credit institutions and employees of the Bank of Russia's regional branches, especially at the initial stage of the system's operation. In 2002, the Bank of Russia organised 22 specialised seminars, which were attended by experts from 1,164 credit institutions, or nearly 90% of all operating credit institutions, and more than 450 employees of the corresponding divisions of Bank of Russia regional branches.

In addition to providing regular training, the Bank of Russia developed a comprehensive system of continuous training of executives and experts of anti-money laundering divisions of its regional branches. In September 2002, it approved the Standard Seminar Training Plan for Bank of Russia employees, which was included in the Bank of Russia personnel training catalogue for 2003.

The Bank of Russia attached great significance to co-operation with the FMC. In January 2002, the two organisations signed an agreement on co-operation in the information sphere and formed an inter-agency working group to tackle day-to-day problems arising in relations between credit institutions, the Bank of Russia and the

FMC. The Bank of Russia also actively co-operated with international and foreign organisations counteracting money laundering and the financing of terrorism.

The efforts made by the Bank of Russia to build an anti-money laundering system in the Russian banking sector were welcomed by international financial and economic organisations and it is largely thanks to them that in October 2002 FATF decided to remove Russia from the list of non-cooperative countries and territories⁸.

I.9. The co-operation with the Russian banking community

Ties with the banking associations are the basis and a time-tested form of co-operation between the Bank of Russia and the banking community in the most important areas of banking. In 2002, the Bank of Russia adopted a new form of co-operation with the banking community, placing the drafts of the most important methodological documents on banking regulation on its website for public discussion.

In 2002, the Bank of Russia sent for consideration of to the Association of Russian Banks (ARB) and the Association of regional banks "Russia" the following draft regulations related to conversion of Russian credit institutions to IAS/IFRS, after January 1, 2004: "On Consolidated Reporting", "On the Procedure for Accounting for Investments in Dependent Organisations in Consolidated Reports" and "On the Procedure for Compiling and Disclosing Financial Statements by Credit Institutions."

The opinions of the banking associations were taken into consideration in drafting regulations in such new area of regulation and supervision as internet-banking. The Regulation "On the Assessment of Banks' Compliance with the Criteria of Access to the Deposit Insurance System" was also discussed by the ARB and Association of regional banks "Russia".

The Bank of Russia, for its part, prepared its opinion on the ARB-drafted Code of Banking Ethics. The importance of the Code was emphasized in the Banking Sector Development Strategy: this document is expected to provide a strong impetus for building-up the culture of banking ethics and closer co-operation within the banking community.

Bank audit. In tackling issues relating to auditing activity the Bank of Russia constantly co-operates with the Government audit regulation body (Ministry of Finance) and audit firms. In 2002, Bank of Russia representatives took part in the work of the Finance Ministry's Audit Council and its commissions, which discussed issues pertaining to audit regulation, notably, draft laws and regulations on audit, prepared by the Finance Ministry in pursuance of the Federal Law "On Audit."

⁸ Russia became a full member of FATF in June 2003.

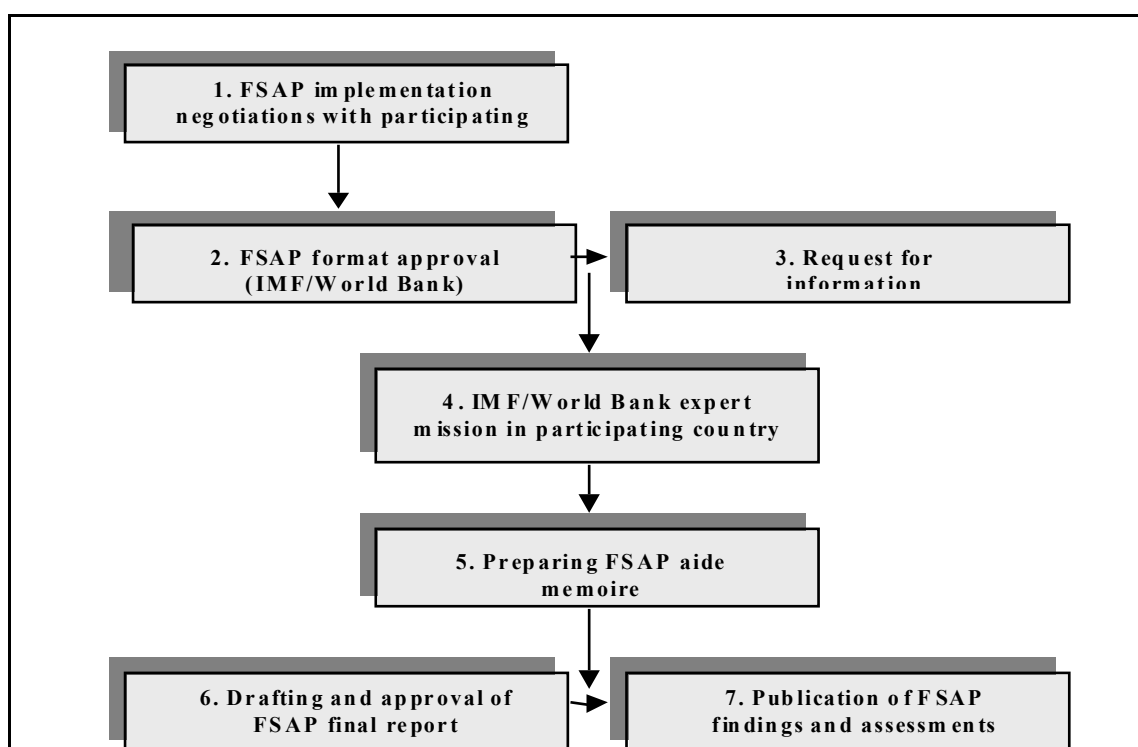
I.10. The co-operation with international financial organisations and foreign central banks and regulatory authorities in the field of banking supervision

Due to increased mobility of capital and internationalisation of banking, the development of financial innovations and the expansion of the cross-border banking international co-operation in the field of banking regulation and supervision is gaining importance. The above challenges can only be met through close ties between the supervisory authorities of different countries and the initiatives of international financial organisations aimed at stability of the world financial system.

I.10.1 Participation in the Financial Sector Assessment Programme (FSAP)

The Financial Sector Assessment Programme (FSAP), a joint international project developed by the IMF and the World Bank and designed to enhance the efficiency of the efforts to strengthen the national financial systems of member countries. In Russia the FSAP was largely completed in 2002 with the participation of the Bank of Russia. Initially FSAPs were launched in the late 1990s when the IMF and the World Bank became seriously concerned over the instability of the world financial system. At present, FSAPs have been completed or are being implemented in more than 60 countries, including industrialised, developing and economies in transition. The FSAP is carried out by concerted efforts of representatives of international financial organisations and national supervisory authorities with the aim of identifying the strengths and vulnerabilities of the financial systems of member countries, evaluating systemic risks and identifying macroeconomic policy priorities. The project also helps to pinpoint areas of possible co-operation between the international financial organisations and participating countries concerned. The main stages of the

Box 4. FSAP: main stages



FSAP are shown in Box 4.

The principal elements of the FSAP are as follows: assessment of stability of the financial system and compliance of the national regulatory practices with international standards and the extent to which the financial sector needs reform and development. FSAP results are available on the IMF website in the form of the Reports on Observance of Standards and Codes (ROSCs) and Financial System Stability Assessments (FSSAs).

In Russia, the FSAP was implemented by a working group, which comprised Bank of Russia, IMF and World Bank experts and enlisted the co-operation of representatives of the Bank of England, the German Bundesbank, the Bank of Finland, the Financial Supervision Agency of South Africa and the Financial Supervision Agency of Hungary. Taking into consideration that the banking sector is a major element of the Russian financial system, the FSAP for Russia focused on:

1) assessment of compliance of the banking regulation and supervision system with international standards, including the Basel Committee's Core Principles for Effective Banking Supervision;

2) calculation and analysis of financial soundness indicators (FSIs) for the banking sector;

3) stress testing of the banking sector.

In 2002, experts of the working group conducted a comprehensive assessment of the Russian banking sector, including risk concentration, banking sector capitalisation, capital quality, transparency, competition and prospects of introducing the deposit insurance scheme .

Russian banking regulation and supervision practices were analysed from the viewpoint of their compliance with the Basel Core Principles for Effective Banking Supervision in the following areas:

- preconditions for effective banking supervision;
- bank licensing procedures;
- prudential regulation and requirements ;
- methods of ongoing supervision;
- requirements to information provided by banks;
- remedial measures and exit;
- cross-border banking and supervision.

The experts' conclusions and recommendations provided a basis for discussing a series of measures aimed at upgrading banking regulation and supervision (see 1.2.1).

The calculation and analysis of the IMF-compiled financial soundness indicators (FSIs) are supposed to play a major role in the banking sector assessment, including assessments undertaken within the framework of co-operation with international financial institutions. The FSIs allow to evaluate the current state and stability of a country's financial institutions and their counterparts (the government, corporations and households). These indicators include both aggregated data on financial institutions and data relating to the markets on which these institutions operate. They are calculated and disseminated to make a more accurate assessments and monitoring of the strengths and vulnerabilities of financial systems. The FSIs are based upon the methodology of national accounts⁹, which makes them internationally comparable.

It should be noted that since December 2002 the Bank of Russia has published an internet version (at www.cbr.ru) of its monthly Review of the Russian banking sector, which contains all core internationally accepted FSIs, including capital adequacy, credit and market risk, liquidity and financial performance indicators.

An important part of the FSAP was stress testing of the Russian banking sector. A stress test evaluates the banking sector stability under unfavourable external influences, such as macroeconomic shocks, sharp deterioration of loan portfolio quality, increased volatility of the financial markets, banking sector liquidity drain and a rise in interest and exchange rate volatility. Reports of Russian banks were analysed as part of this work, including reports compiled according to international standards, to find out fundamental and specific risks, notably, off-balance asset risks, loan portfolio concentration and connected parties lending. The results of the stress testing exercise demonstrate that the Russian banking sector by and large would retain stability even in a distress comparable to the 1998 events.

I.10.2. Participation in other international projects

A major aspect of international co-operation maintained of the Bank of Russia is the signing of memorandums of understanding with foreign central banks and supervisory authorities.

The procedure for exchange of information between the Bank of Russia and foreign central banks and supervisory authorities is established by Article 51 of the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)." Measures to improve conditions and forms of co-operation with foreign central banks and supervisors were implemented by the Bank of Russia, given the amendments made to the Law in 2002. During this year, the Bank of Russia:

- signed the Agreement on Co-operation in Supervising Credit Institutions and Memorandum of Understanding in the Field of Banking Supervision with the Financial and Capital Market Commission of the Republic of Latvia;

⁹ In future, the FSIs will be calculated according to the Compilation Guide on Financial Soundness Indicators updated by IMF experts. The Guide is based on international expertise of calculating and assessing financial system stability indicators of more than 100 IMF member countries. At present, the FSIs consist of two sets of indicators (core and encouraged)

- drafted a new version of the Agreement on Co-operation in Supervising Credit Institutions with the Central Bank of Armenia (signed in January 2003).

The Bank of Russia continues to negotiate draft memorandums of understanding and statements of co-operation with the supervisory authorities of Switzerland, Turkey, Kazakhstan and some other countries.

In 2002, the Government of the Republic of Belarus, the National Bank of the Republic of Belarus, the Government of the Russian Federation and the Central Bank of the Russian Federation continued to implement the Joint Action Plan for the Introduction of a Single Currency in the Russia-Belarus Union State for the period of 2001 to 2005 and the National Bank of the Republic of Belarus and the Central Bank of the Russian Federation continued to implement the programme for harmonising supervisory requirements for registration and licensing, creating equal conditions for

Box 5. Participation in QIS-3

Within the framework of international Quantitative Impact Study-3 (QIS-3) the Basel Committee analysed the expedience and readiness for the Basel II proposals implementation. The principal objective of the study was to evaluate the quantitative effect of Basel II capital requirements, taking into account credit institutions' credit, market and operational risks.

Six Russian banks that were involved in the study in the period from October 2002 to April 2003 calculated on the basis of their balance sheet data capital adequacy ratios in accordance with the proposals of Standardised Approach to credit risk assessment of the Basel II). The results of the study demonstrated that the participating Russian banks met the capital adequacy requirements for covering credit and market risks under both the current and new Accords.

As for the capital requirements to cover operational risk imposed for the first time by the Basel II proposals the results of the study confirmed the need to make additional capital provisions to cover this risk.

mutual investment of funds in the authorised capital of Russian and Belarussian banks and for opening bank branches in Russia and Belarus, and elaborating a concept of transition to and the use of the Russian rouble as the single currency in the Russia-Belarus Union State.

Participation in projects of international organisations. In 2002, Bank of Russia experts participated in the work of the following working groups of the Basel Committee: the Core Principles Liaison Group, the Core Principles Working Group on Capital and the Task Force for the Basel Committee Guide on Dealing with Weak Banks¹⁰. The discussions held within these groups focused on crucial issues of effective banking supervision, the New Capital Accord (Basel II), supervision of weak banks, etc. At the request of the Basel Committee's Secretariat, the Bank of Russia took part in the Quantitative Impact Study, QIS-3 (see Box 5). This international study was conducted worldwide to evaluate the effect of the New Capital Accord proposals on the overall capital requirements for individual banks and banking system as a whole

¹⁰ The discussion held within the framework of the Task Force led to the publication in March 2002 of an updated draft of the Basel Committee's Guide for Dealing with Weak Banks.

In 2002, the Bank of Russia actively participated in the work of expert groups, conferences and seminars organised by international organisations:

- the Global Bank Insolvency Initiative, organised by the World Bank, IMF and Financial Stability Institute (Basel, October 2002);
- the 15th Conference of the Basel Committee Regional Group of Banking Supervisors from Central and Eastern Europe (Bratislava, October 2002);
- the Regional Seminar of the Basel Committee Bank Supervision Group for Central and Eastern Europe (Vilnius, September 2002);
- the 12th Conference of the Basel Committee Regional Group for the Caucasus and Central Asia (Bishkek, September 2002).

Organisation of international conferences and seminars. The Bank of Russia took part in organising and holding the 11th International Banking Congress (IBC-2002), which took place in St. Petersburg on June 5 to 8, 2002. Held under the title “Market Discipline and Transparency: Accounting, Reporting and Audit,” the Congress discussed key issues of the modernisation of the Russian banking sector, the transparency and discipline requirements for the banking services market, upgrading bank accounting and reporting procedures and conversion to IAS/IFRS. Representatives of Russian and foreign business and political circles, international organisations, foreign central (national) banks and supervisory authorities and the banking community took part in the Congress.

In 2002, the Bank of Russia in collaboration with international financial institutions organised and held the following seminars in Moscow with the participation of representatives of the Parliament and the Government, banking and financial institutions, academia and foreign experts:

- the discussion of the World Bank Report “Building Trust: Developing the Russian Financial Sector” (April 2002);
- the seminar on “Risk Management and Internal Controls,” held in Moscow with the assistance of the Financial Services Volunteer Corps Mission in Russia and the US Federal Reserve System (May 2002).

I.11. Prospects for the development of the banking regulation and supervisory system

Ensuring banking sector stability and protecting creditors and depositors’ interests will remain the principal objective of the upgrading of the Russian banking regulation and supervision system in the short and medium term. The Bank of Russia will implement these tasks in all major areas of banking supervision.

Registration and licensing. The efforts to improve the procedure for accessing credit institutions to the banking services market pursue two objectives. First, Russia intends to achieve an adequate level of requirements (from the viewpoint of the best international practice of banking supervision and the nature of the development of

market relations in the economy in general and the banking sector in particular) that will guarantee access to the market and the expansion of financially sound credit institutions only and prevent managers and owners with questionable business reputations and financial condition from managing credit institutions. To achieve this objective, it is very important to tighten banking legislation with regard to disclosure of information about the real owners of credit institutions and to empower the Bank of Russia to evaluate their financial condition and business reputation.

Second, to create conditions conducive to the expansion of banking infrastructure, the Bank of Russia will remove excessive administrative barriers and optimise bank registration and licensing procedures. In this context, it is important to upgrade laws and standards that regulate mergers and acquisitions in the banking sector. Specifically, the Bank of Russia is going to issue a new version of its Instruction No. 75-I, dated July 23, 1998, "On the Procedure for Applying Federal Laws Regulating the Procedure for Registering Credit Institutions and Licensing Banking Activities". The new document is expected to settle problems that arise in the process of applying existing regulations and to optimise registration procedures and decision-making within the Bank of Russia.

The efforts to upgrade the regulation of reorganisation of credit institutions, make them transparent and create favourable conditions for the expansion of the banking services market will be made taking into consideration the tasks involved in the implementation of the Banking Sector Development Strategy in the 2003-2005 period. Specifically, the Bank of Russia plans to carry out the following measures:

- create equal conditions for the participation of residents and non-residents in the Russian banking sector;
- improve bank reorganisation procedures;
- increase the transparency of the ownership structure (stakes in authorised capital) in credit institutions;
- identify the real owners of credit institutions and ensure that the Bank of Russia has the right to control their financial condition;
- grant credit institutions the right to issue unsecured bonds;
- increase the capital adequacy requirements whose non-fulfilment will entail the revocation of banking licences.

To facilitate the expansion of banks with foreign interest, the Bank of Russia plans to propose amendments to the Federal Law "On Banks and Banking Activities" and the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)", stipulating that residents and non-residents who intend to purchase up to 1% of shares (stakes) in the credit institution's authorised capital should notify the Bank of Russia of the purchase in advance and those who intend to buy more than 10% of shares should obtain Bank of Russia permission (a corresponding document was drafted by the Bank of Russia and the Ministry of Finance in 2002).

Off-site monitoring of credit institutions. As regards the methodology and practice of current supervision, the Bank of Russia will continue to focus on the conversion of the existing bank regulation system to internationally accepted principles including the Basel Committee's Core Principles for Effective Banking Supervision.

Bank asset valuation practices will be increasingly oriented to the principle of informed judgement, which implies, above all, the evaluation of the financial condition of the borrower and the borrower's debt service performance.

The Bank of Russia will continue to encourage the use of substance-over-form principles while evaluating bank performance and establish the regime of banking supervision and take supervisory action when necessary, taking into consideration, above all, the nature of risks assumed by credit institutions and the effectiveness of their risk management practices, evaluating the potential effect of such risks on the stability of credit institutions and the threat they pose to the interests of a bank's creditors and customers. Formal compliance procedures will be increasingly replaced with realistic evaluation of risks (introduction in supervisory practice of risk-focused principles assumes the development of the institute of credit institutions curators).

The Bank of Russia will continue to take steps to improve the qualitative parameters of banking capital by preventing the use by credit institutions of fictitious capitalisation schemes. A credit institution found or suspected of using inappropriate assets to form its own funds (capital), will be required to correct the value of their capital. To create better conditions for the Bank of Russia's supervision of credit institutions, banking groups and bank holding companies the Bank of Russia will put forward new proposals to amend federal legislation and participate in drafting new laws.

Consolidated supervision procedures are to be upgraded. The Bank of Russia is currently working on methodological recommendations on the analysis of reports by banking/consolidated groups (bank holding companies) and the evaluation of the impact of operations conducted by members of groups (holding companies), other than credit institutions, on the financial condition of member credit institutions.

The Bank of Russia believes that it is necessary to continue improving corporate governance in credit institutions from the viewpoint of optimising it, increasing the responsibility of affiliated persons of credit institutions and strengthening the role of internal controls. The Bank of Russia intends to propose amendments to the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)" and the Federal Law "On Banks and Banking Activities", taking into account the internationally accepted principles of regulating corporate governance in credit institutions. In addition, the Bank of Russia is to draft regulations on managing legal risk and the risk of losing business reputation in credit institutions and banking groups, on organising corporate governance in credit institutions.

To harmonise national practices with internationally accepted standards of supervision over currency risk levels, the Bank of Russia intends to revise the methodology of calculating open currency positions by expanding the range of

instruments included in the calculation, such as revocable and irrevocable sureties, guarantees as well as revocable bank guarantees. Taking into consideration internationally accepted practices, the Bank of Russia also intends to grant credit institutions the right to manage their own currency risks assumed by their branches and thus manage currency risks of a credit institution as a whole. As part of current efforts to optimise bank reporting procedures and with due account of the effective stabilisation of the Russian rouble foreign exchange market the Bank of Russia is going to give credit institutions the right to report their open currency positions on a monthly basis.

As regards the evaluation of risks assumed by a credit institution, the Bank of Russia plans to work out recommendations on stress testing in credit institutions.

To make the banking sector more transparent and enhance market discipline, the Bank of Russia will continue to take steps towards the disclosure of information to the public, including the reporting on a monthly basis of the current state of the banking sector and providing a list of banks that disclose information on the Bank of Russia's website.

The Bank of Russia will continue to develop methodologies to control the use of internet-banking and other advanced banking technologies by credit institutions. With due account of international experience, the work will be continued to optimise and improve the reports filed by credit institutions with the Bank of Russia, including the use of advanced information reporting technologies.

In 2004, credit institutions will have to compile their financial statements in accordance with internationally accepted standards. To do so, they will have to transform the statements compiled according to the Russian accounting rules, using the informed judgement method and making the necessary corrections (referred to below as the transformation method). In 2004 and 2005 financial statements compiled by using the transformation method will not be used for determining supervisory regime and corrective actions. They will be used only to assess the possible impact of comprehensive implementation of IAS/IFRS principles.

Inspection. The Bank of Russia will upgrade the methodology and organisation of inspections in accordance with its programme for a gradual transition to the territorial principle of organising and conducting inspections of credit institutions and their branches. The implementation of this principle will help optimise forms and methods of conducting inspections of credit institutions and their branches and make them more effective through better use of the Bank of Russia inspectors and inspection facilities.

While inspecting credit institutions, the Bank of Russia intends to focus on evaluating the observance of own funds (capital) formation and risk evaluation rules and assessing risk management systems, including risk classification and the creation of provisions for possible losses. It will continue to attach great importance to assessing the effectiveness of credit institutions' internal control systems, making sure that credit institutions accurately disclose the risks they assume in their statements and

analysing the impact of the violations and shortcomings detected on the financial performance of credit institutions and prospects for their future.

To provide a better use of information on inspection results, the Bank of Russia plans to develop and install in its inspection divisions a software system called the Automated System of an Inspection Division. The aim of this project is to build an effective system of collecting and processing information received during inspections, which will help enhance the efficiency of the Bank of Russia inspection divisions.

In connection with the transition of the Russian banking system to IAS/IFRS in 2004, the Bank of Russia is currently working on regulations and methodological recommendations on inspections of credit institutions and their branches. It has elaborated and is implementing now training and advanced training programmes for inspectors and heads of the inspection divisions of the central office and regional branches.

Financial rehabilitation and liquidation procedures. It is necessary to create conditions that will prompt managers and owners of credit institutions to take necessary and timely actions on financial rehabilitation of their credit institutions. Problem credit institutions that have no chance of financial recovery and whose further existence may jeopardise the interests of their creditors and depositors will have their banking licences revoked.

It is also important to make bank liquidation procedures more transparent and ensure that a greater number of creditors have their claims met to a fuller extent. Exercising the powers given to it by the law, the Bank of Russia will participate in supervising bank liquidations and upgrading the legislation that regulates bank's bankruptcies. It is necessary, therefore, to make amendments to legislation that will give ARCO the powers of a corporate liquidator.

The Bank of Russia plans to issue a new version of its Instruction "On the Procedure for Preventing Insolvency (Bankruptcy) of Credit Institutions," which will take into account the Basel Committee's recommendations on dealing with weak banks. A redrafted Instruction will also stipulate in what cases a credit institution must be required to take measures to rehabilitate itself financially and/or reorganise itself and in what cases it should be given the opportunity to eliminate the grounds for being required to do so on its own or enlisting the participation of its shareholders (members), creditors and other persons. In addition, the new document will formulate the principles of forming an informed judgement by Bank of Russia regional branches on the possibility of the financial rehabilitation of a credit institution in accordance with the rehabilitation plan it has drafted.

To improve the regulation of provisional administrations by the Bank of Russia, taking into account the established procedure for appointing them and their practices, including provisional administrations appointed after the revocation of banking licence, the Bank of Russia intends to issue a new version of the Regulation "On the Provisional Administration of a Credit Institution."

Enhancing banking sector efficiency and the effectiveness of banking infrastructure. The Bank of Russia will implement its tasks set in Chapter X of the

Federal Law “On the Central Bank of the Russian Federation (Bank of Russia),” taking into account the measures planned in the Banking Sector Development Strategy to create conditions that will help enhance the efficiency of the banking sector and strengthen its functional role in the economy. The creation of favourable conditions for the expansion of the activities of credit institutions in extending loans and providing settlement services to the real economy will require the Bank of Russia supervisory divisions to keep these activities under close scrutiny.

The most important task in this area will be strengthening the mortgage system by providing a legal framework for credit institutions to originate asset securitisation, especially regarding mortgage loans and encouraging credit institutions to conduct trust operations, including granting to credit institutions of the right to deal with a wider range of property (credit claims, property owned by non-residents, etc.).

Taking into consideration the proposals put forward by the banking community, which were dictated by the needs of the market, the Bank of Russia agreed that mobile offices might be one of the possible solutions to the problem of providing banking services to the public, especially in areas with underdeveloped banking infrastructure, remote and sparsely populated regions, where the construction of permanent bank offices would be unprofitable and the provision of banking services - inadequate and difficult. There is a good reason to believe that the idea of creating mobile offices will be favourably perceived by legislators.

II. THE STATE OF THE RUSSIAN BANKING SECTOR

II.1. General economic conditions of banking sector development

The future of banking is inseparably connected with the general thrust of economic development. Russia is no exception to this rule: a sustained growth of the Russian economy had a favourable effect on indicators of bank performance in 2002.

II.1.1. Macroeconomic conditions

The macroeconomic situation in 2002 was characterised by further reduction of inflation, growth of GDP and fixed capital investment, a federal budget surplus and growth in real wages. (see Table 3 in the Statistical appendix).

Judging by indicators of 2002, Russia joined the group of fast growing countries. Russia's GDP real growth on annual basis was 4.3% in 2002 (in 2001 - 5%). The principal factors of growth in production were a favourable situation in the world commodity markets which contributed to the increase of exports, and a rise in domestic demand.

Due to real incomes growth, the household sector's spending on final consumption increased by an estimated 8.6% in 2002, accounting for 4.1 percentage points of GDP growth. A rise in non-interest federal budget expenditures in 2002 brought about an increase in the government sector's expenditures on final consumption, which grew 2.4% compared to 2001, whereas in 2001 they fell by an estimated 1.7%. In 2002, the rate of growth in gross accumulation slowed to an estimated 1.7% as against 16.5% in 2001. The slowdown can be largely attributed to low corporate investment activity registered throughout 2002. Fixed capital investment rose by 2.6% in 2002 year on year, a significant decline from 2001 (10%). Net exports contracted by an estimated 4.5% in 2002 as against 13.6% in 2001 and as a result, the negative effect of net exports on GDP was less significantly as compared to 2001.

Industrial output expanded by 3.7% in 2002 year on year. Estimates show that the energy sector, steel and food industry contributed at most to the industrial production growth in 2002.

Favourable macroeconomic developments in 2002 were largely a result of the monetary policy, aimed at reducing inflation. Consumer price growth slowed significantly in 2002. In December 2002, consumer prices rose by 15.1% year on year (in December 2001, consumer prices were up 18.6% year on year). However, consumer price inflation in 2002 exceeded by more than 1 percentage point the target set for the year. Core inflation stood at 10.2% in 2002 as against 15.6% in 2001.

Actual consumer price growth was faster than planned mainly because of the rapid rates of growth in the tariffs for services rendered to households. In 2002, these tariffs rose by 36.2% as against 36.9% in 2001.

Due to economic growth, the employment continued to rise and the unemployment level continued to fall. In 2002, 92.0% of Russia's economically active population was employed in the economy and 8.0% was classified as unemployed,

according to the ILO calculation methods. In 2001, the respective percentages were 91.0% and 9.0%. The employment rose by 2.4% year on year, while the total number of those seeking work fell by 10.5%.

The fact that the production of goods and services grew faster than employment demonstrates that there were intensive factors which contributed to growth. Labour productivity rose by an estimated 1.8% in 2002.

In 2002, Russia had a stable balance of payments.

A favourable price situation and significant growth in physical volumes of exports caused exports to expand in 2002. Oil and petroleum product prices were 3% higher than in 2001. The average price of Urals crude stood at \$23.7 per barrel (in 2001, it was \$23.0 per barrel). Compared to 2001, exports expanded by 5.3% to \$107.2 billion and imports grew by 13.4% to \$61.0 billion. Russia's trade surplus in 2002 amounted to \$46.3 billion as against \$48.1 billion in 2001.

The current account surplus contracted to \$31.1 billion (9% of GDP) in 2002 from \$35.0 billion (11.3% of GDP) in 2001. At the same time, net capital outflow decreased in 2002 compared to 2001 with growth in foreign investment being one of the reasons.

Russia's international reserves amounted to \$47.8 billion as of January 1, 2003. Growth in international reserves created conditions for greater external and internal stability. In December 2002, the rouble gained 6.2% against the dollar in real terms compared to December 2001, while it lost 6.9% of its value against the euro. The real effective rate of the rouble fell 3.1% over that period.

The state of government finance was a major factor of macroeconomic stability. In 2002, the federal budget surplus stood at 1.5% of GDP. The Russian Government met all its foreign and domestic debt obligations in full.

Compared to 2001, the financial condition of Russian enterprises deteriorated slightly in 2002. Corporate profits (net) amounted to 905.8 billion roubles, a decrease of 18.9% from 2001. The share of profit-making companies contracted by 5 percentage points to 56.6% of the total number of companies as of January 1, 2003. The deterioration of companies' performance amid the expansion of output resulted from a rise in costs, caused by the accelerated growth in the prices of products manufactured by high-cost industries as well as growing wages and salaries. In addition, unit costs increased owing to the lifting of restrictions on taxpayers' practice of treating as cost the expenses involved in retaining profit (advertising expenses, property and health insurance expenses, etc).

The continued economic growth and increased employment in 2002 led to a rise in households money incomes. Compared to 2001, real households money income rose by 10.3% in 2002 and real disposable money income grew by 9.9%. The real imputed average monthly wage increased by 16.2% and real imputed monthly pension rose by 16.3%.

Household expenditures on goods and services accounted for 73.2% of household money income in 2002 as against 74.6% in 2001. The share of household savings in the form of bank deposits and securities remained unchanged since 2001 at 3.7% of household money income use.

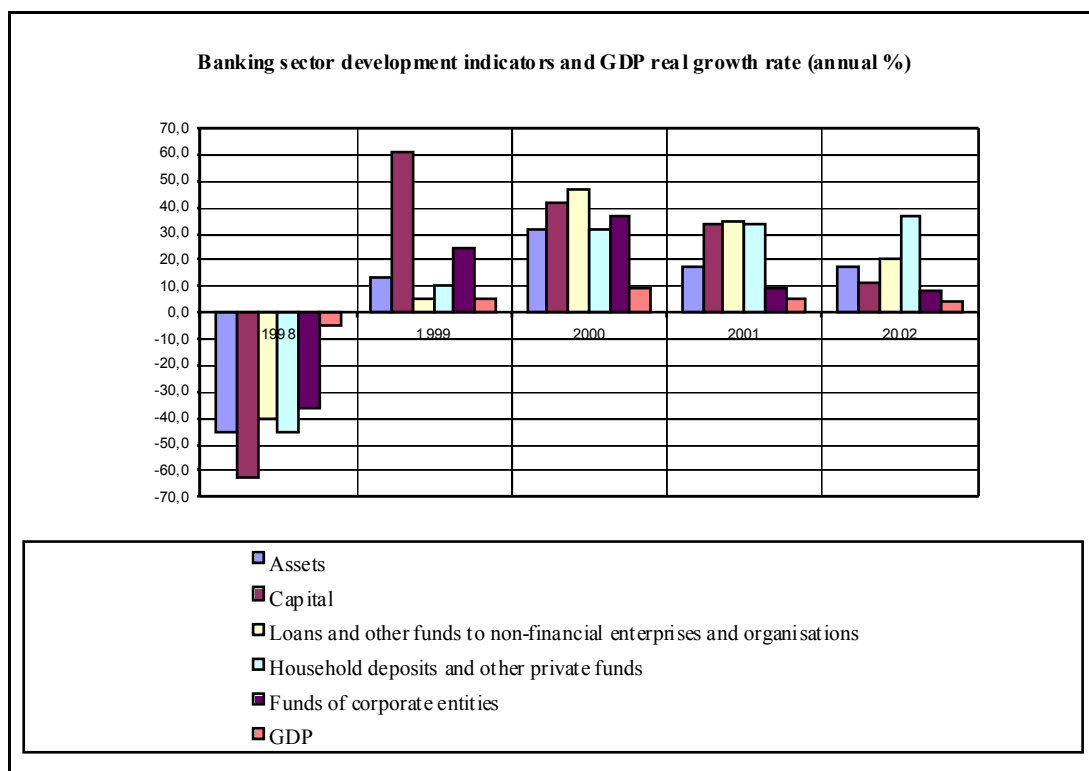
II.1.2. Banking sector performance indicators relative to key macroeconomic indicators

In 2002, the Russian banking sector continued to expand more rapidly than the economy as a whole. Banking capital grew 2.6 times faster than GDP, banking assets were overleaping GDP four times, lending to the non-financial sector¹¹ – five times and household deposits – nine times (see Chart 2.1). As a result, as of January 1, 2003, banking sector assets relative to GDP stood at 38.2% (34.9% as of January 1, 2002), loans to resident non-financial companies 14.6% (13.0%) and funds drawn from corporate borrowers and households 19.5% (17.5%).

The 2002 movement of major banking sector indicators show that the quantitative targets set for 2007 by the Banking Sector Development Strategy and its projections updated late in 2002 (assets to GDP are projected at 44%, capital to GDP at 6% and loans to the non-financial sector to GDP at 19%) may be achieved. Major preconditions of the success include implementation of measures envisaged by the Strategy to upgrade legal environment of banking regulation and increased attention to the structural aspects of banking reform.

In 2002 the banking sector developed in a favourable macroeconomic environment. Over the year, banking sector assets expanded by 31.2%. More importantly, sustained assets growth was demonstrated by more than 80% of all credit institutions operating at the end of 2002. In real terms, banking sector assets increased by 17.8%, exceeding the pre-crisis (July 1, 1998) level by 25%. The share of rouble assets in aggregate banking sector assets expanded slightly in 2002, from 62% to 64% (as of July 1, 1998, rouble assets accounted for almost 73% of aggregate banking sector assets).

¹¹For the purposes of this Report, the non-financial sector comprises resident commercial and non-commercial enterprises and organisations, both state-owned and private, and non-resident corporate entities.

Chart 2.1.

II.2. Institutional aspects of banking sector development

II.2.1. Quantitative characteristics

In 2002, the number of credit institutions rose by 10 (in 2001, by eight) to 1,329 (see Table 4 in the Statistical appendix). Twenty-six credit institutions, mostly small ones in terms of assets, had their banking licences revoked (cancelled) in 2002 (20 in 2001). The number of credit institutions with own funds (capital) in excess of 5 million euros rose by 5.5% to 423 as of January 1, 2003 (the aggregate capital of this group of banks expanded almost by a quarter).

The tendency of credit institutions to broaden the scope of their activities continued in 2002. As of January 1, 2003, 22% of all operating credit institutions had a general licence (20% as of January 1, 2002) and 63% (61%) conducted banking operations with roubles and foreign currency. At the same time, the number of credit institutions licensed to take household deposit fell from 1,223 to 1,202 (90% of the total) over the year.

It should be noted that growth in the number of credit institutions mainly resulted from banking sector development in the Central Federal District, where the number of operating credit institutions rose by 24 in 2002. In other districts the number of operating credit institutions was either unchanged or declined. As a result, there were 663 credit institutions in Moscow and the Moscow Region as of January 1, 2003, or half the total number of credit institutions in Russia. Credit institutions based in Moscow and the Moscow Region accounted for 84.5% of banking sector assets,

82.2% of capital and 85.4% of loans and other funds placed with non-financial enterprises and organisations.

At the same time, 14 regions of the Russian Federation (Bryansk, Kursk, Lipetsk, Orel, Tambov, Novgorod, Penza and Chita Regions, Republics of Karelia, Buryatia, Ingushetia and Marii El, the Taimyr and Koryak Autonomous Areas) had no more than two locally-based credit institutions (12 regions and territories as of January 1, 2002). As of January 1, 2003 there were no operating credit institutions, in eight regions of the Russian Federation (the Chechen Republic, Jewish Autonomous Region and Chukchee, Nenets, Komi-Permyak, Evenk, Ust-Aga Buryat and Aga-Buryat Autonomous Areas).

In 2002 regional banks¹², just as the banking sector as a whole, demonstrated a persistent tendency towards expansion. However, as assets of the regional banks grew more slowly (22.3%), their share in aggregate banking sector assets diminished from 16.7% to 15.5%.

The aggregate capital of regional banks increased by 26.5 billion roubles, or 34.4%, in 2002. As a result, the share of regional banks in aggregate banking sector assets expanded slightly: from 17.0% as of January 1, 2002, to 17.8% as of January 1, 2003.

The number of branches of credit institutions continued to decline in 2002: over the year, it fell from 3,433 to 3,326, or by 3.1% as against 9.5% decrease in 2001. The main reason for the decline was the continued optimisation of the Savings Bank (Sberbank) network: Sberbank closed 71 branches in 2002. At the same time, a rise in the number of additional offices established by banks (from 5,718 to 6,387, a growth of 11.7%) was a major trend of 2002. This tendency is largely the result of a relatively low cost of this kind of geographical expansion.

II.2.2. Concentration of banking sector activities

The level of asset concentration in the banking sector as a whole was unchanged in 2002: as of January 1, 2003, the top 200 banks (in terms of assets) accounted for 88.5% of aggregate banking sector assets. The top five banks expanded their share over that period from 42.8% to 44.2% and Sberbank's share increased from 26.5% to 28.4%.

As the banking sector capitalisation increased in 2002, large banks retained the level of capital concentration they had achieved earlier. The share of banks with a capital of more than 5 million euros in the aggregate capital of operating credit institutions with positive capital remained virtually unchanged over the year and stood at 93.1% as of January 1, 2003.

The Herfindahl-Hirschman Index (HHI)¹³ displays a relatively low, by international standards, level of banking capital concentration in Russia. However, in

¹² Regional banks are banks registered outside Moscow and the Moscow Region.

¹³ The Herfindahl-Hirschman Index is a measure of concentration of operations in the banking sector. It is calculated as a sum of squared unit weights of banks' assets, loans, deposits or capital in the banking sector's

the last two years the HHI calculated for banking sector assets rose by almost 20% (See Chart 2.2). If growth continues at the same rate, the level of asset concentration will increase dramatically in the next two years.

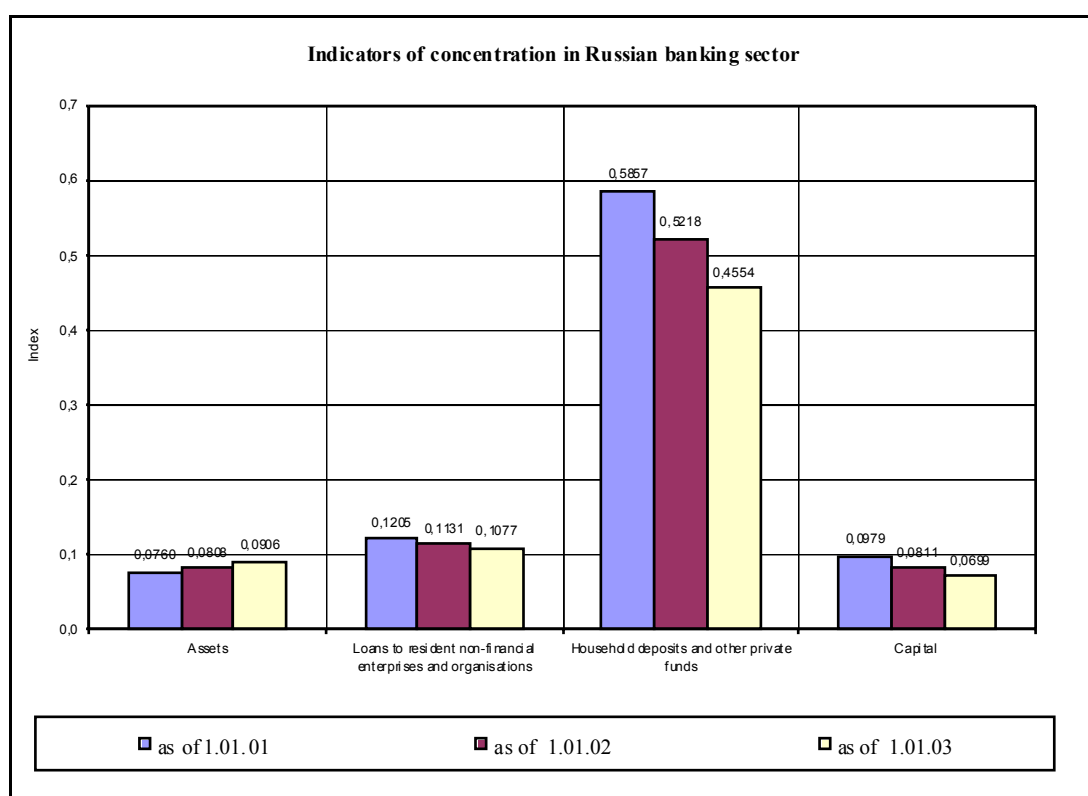
Geographically, the region that follows the Central Federal District in terms of bank asset concentration is the North-Western Federal District, where the level of asset concentration is close to average (HHI equals 0.12). In other federal districts asset concentration levels are lower with the lowest being in the Siberian Federal District.

A level of capital concentration also remains low; moreover, it has declined in the past two years.

As for the lending to the real sector of the economy¹⁴, here the level is average (HHI equalled 0.11 as of January 1, 2003), but this indicator tends to decline (in the past two years, it has fallen by almost 11%).

A very high level of concentration was registered in the household deposit market (as of January 1, 2003 HHI was 0.46). At the same time, the index fall by more than 22% shows that the situation in this segment of the banking services market is changing as banks are competing more aggressively for household deposits.

Chart 2.2.



total. HHI has the value of $0 < \text{HHI} < 1$. A value smaller than 0.10 indicates a low level of concentration, a value from 0.10 to 0.18 indicates an average level and a value larger than 0.18 means a high level of concentration.

¹⁴ For the purposes of this Report, the real sector of the economy signifies only resident non-financial (commercial and non-commercial) enterprises and organisations, both state-owned and private.

II.2.3. Development of banking activities at the regional level

There were no significant changes in the provision of banking services in the Russian regions¹⁵ in 2002, while the differences that remained between different regions in this sense were attributable to their different levels of economic development. The provision of banking services in the industrialised regions was, as a rule, above average¹⁶ (see Table 5 in the Statistical appendix). In addition, a number of banks and bank branches in a region was important from the viewpoint of the availability of banking services. The regions that were best provided with banking services were St. Petersburg and the Magadan, Kaliningrad and Nizhni Novgorod Regions.

Fifty-four out of the 77 regions of the Russian Federation (70% of the total) that were taken into account¹⁷ were provided with banking services below the national average. The worst provided regions in 2002 were the Republics of Ingushetia, Tyva, Khakassia and Dagestan and the Chita Region.

As for the federal districts, best provided with banking services was the North-Western federal district, where the respective composite index was 1.3 times higher than the national average (excluding Moscow and the Moscow Region). As of January 1, 2003 three federal districts - the Urals, Siberia and the Far East - were provided with banking services on a level below the national average. The region with the lowest level of banking services provision is the Siberian federal district.

II.2.4. Government participation in the banking sector

As of January 1, 2003 there were 23 state-controlled banks (banks in which the state had a 50%-plus stake¹⁸) in Russia. Five of them were controlled by federal structures unrelated to the Government (the Bank of Russia holds a controlling block of shares in Sberbank and Vneshtorgbank¹⁹, while the Federal Property Fund controls the Russian Development Bank, Roseximbank and Rosselkhozbank).

As of January 1, 2003, the above 23 credit institutions accounted for 34.4% of aggregate own funds (capital) of operating credit institutions, 37.5% of assets, 39.2% of loans to the real sector, 72.1% of household deposits and 77.6% of investments in the Russian Government debt instruments. State-controlled banks play an important role in conducting operations with Government budget funds and off-budget funds. As of January 1, 2003, they accounted for 46.1% of such funds deposited with operating credit institutions.

¹⁵ The indicator (composite index) of availability, or in other words density, of banking services in a region used as a measure of the provision of a region with banking services takes into account the ratio between the major aggregate bank performance indicators in an economic region (the number of banks, the value of assets, loans to the real economy, household deposits) and the region's social and economic indicators (regional product, population and per capita income).

¹⁶ Excluding Moscow and the Moscow Region.

¹⁷ Regions of the Russian Federation, excluding nine autonomous areas, which are part of larger constituent territories of the Russian Federation, the Chechen Republic and Moscow and the Moscow Region.

¹⁸ Organisations that immediately represent the government are the federal and regional executive bodies of power and state unitary enterprises.

¹⁹ Throughout 2002, the Bank of Russia stake in Vneshtorgbank was nearly 100%. At the beginning of 2003, Vneshtorgbank shares were transferred to the Government.

The Savings Bank (Sberbank) is a state-controlled bank that plays a special role in the banking services market. In 2002, its share in aggregate banking sector assets expanded from 26.5% to 28.4%, while the share in aggregate banking sector capital contracted slightly, from 21.1% to 20.4%. Sberbank continues to dominate the retail banking services market, accounting for more than 79% of household deposits denominated in roubles and over 48% of household deposits denominated in foreign currency. Sberbank's share in the total amount of household deposits, however, continued to decline: from 72.1% as of January 1, 2002, to 67.3% as of January 1, 2003 (as of January 1, 2001, it was 76.5%).

Sberbank's share in total banking sector investments in Russian Government debt instruments expanded from 62.7% as of January 1, 2002, to 68.0% as of January 1, 2003. Sberbank continues to play a leading role in extending loans to the non-financial sector of the economy, although its share in the total amount of loans extended by the banking sector to non-financial enterprises and organisations somewhat contracted (from 30.6% as of January 1, 2002, to 29.8% as of January 1, 2003). At the same time, Sberbank expanded its activities on the interbank market: in 2002, its share in interbank loans extended by all credit institutions increased from 4.6% as of January 1, 2002, to 10.8% as of January 1, 2003.

II.2.5. Participation of foreign capital in the Russian banking sector

In 2002, foreign capital slightly strengthened its presence in the Russian banking system. The value of non-residents' registered stakes in the aggregate authorised capital of operating credit institutions in 2002 increased from 13.8 billion roubles to 15.88 billion roubles, or by 14.8%.

At the end of the year under review 37 foreign-controlled banks (banks with a foreign stake in excess of 50%) were operating in the Russian banking sector. Nine of them were among Russia's top 50 banks in terms of assets.

Most of foreign banks holding stakes in Russian credit institutions or established are from Germany, the United States, France, the Netherlands and Austria.

In 2002, the assets of foreign-controlled banks increased by 20.8% (11.9% in real terms²⁰) to 334.5 billion roubles. However, the role of foreign capital in the Russian banking sector remains small and has even decreased a little. As of January 1, 2003, foreign-controlled banks accounted for 8.1% of Russian banking sector assets, 7.1% of own funds (capital) (as of January 1, 2002, the respective percentages were 8.8% and 7.7% (see Table 6 in the Statistical appendix). Foreign-controlled banks are located in different regions, most of them in Moscow and the Moscow Region (34 banks), the rest in St. Petersburg (2) in Krasnodar Territory (1).

In 2002 foreign-controlled banks mainly provided credit and settlement services to their customers. It should be noted that these banks have stepped up their activity on the Russian banking services market, especially retail banking.

²⁰ Here and below percentages are given taking into account the changes in the exchange rate of the rouble and consumer price index.

Balances in clients' accounts form a large part of foreign-controlled banks' liabilities (43.8% as of January 1, 2002, and 41.1% as of January 1, 2003). At the same time, these resources account for a little more than 6% of the total amount of clients' funds deposited in the Russian banking sector.

In 2002, foreign-controlled banks increased by 1.5 times the total amount of household deposits and other private funds and the share of this source in their liabilities expanded from 5.6% to 7.0%. However, foreign-controlled banks still accounted for a small part of the retail market and their share of this market remained unchanged during the year 2002 (2.3% as of January 1, 2003).

Foreign-controlled banks retain important positions on the market for interbank loans and deposits received from non-residents. As of January 1, 2003, they accounted for 45.8% of the total amount of funds attracted by credit institutions from non-resident banks. As of January 1, 2003, these funds accounted for 26.7% of the foreign-controlled banks' liabilities as against 22.7% as of January 1, 2002.

In 2002 the share of operations with non-residents in the structure of foreign-controlled banks' assets contracted slightly. As of January 1, 2003, funds deposited with non-residents accounted for 34.7% of foreign-controlled banks' assets as against 38.1% as of January 1, 2002.

Lending is one of the principal activities conducted by foreign-controlled banks. Loans and other funds extended to non-financial enterprises and organisations rose by 33.6% in 2002 and their share in the assets of foreign-controlled banks expanded from 31.8% as of January 1, 2002, to 35.2% as of January 1, 2003. It is significant that loans extended to the real sector increased by 34.6% (they accounted for 97% of all loans extended to non-financial enterprises and organisations) and loans extended to non-resident enterprises by 7.7%. Nevertheless, 85% of loans from this group of banks were denominated in foreign currencies, and this reflects the specificity of these banks' customers base. The share of foreign-controlled banks in total loans extended by the banking sector to non-financial enterprises and organisations remained virtually unchanged in 2002 at 7.1% (as of January 1, 2002, it stood at 7.2%).

The share of foreign-controlled banks' investments in Russian Government securities continued to contract (from 6.1% as of January 1, 2002, to 5.8% as of January 1, 2003).

Balances of funds kept by foreign-controlled banks in correspondent accounts in other banks decreased by 4.2% in 2002 (by 3.8% in non-resident banks), while the share of this item in foreign-controlled banks' assets contracted from 17.5% as of January 1, 2002, to 13.9% as of January 1, 2003.

The role played by foreign-controlled banks in redistributing resources between the Russian and international financial markets changed in 2002. While generally there was a net outflow of capital from Russia²¹ (even though it declined by 37.5%, from 149.3 billion roubles to 93.4 billion roubles), the direction of capital flow from foreign-controlled banks changed its direction (from an outflow to an inflow) and

²¹ The excess of the funds extended to non-residents over the funds borrowed from them.

as of January 1, 2003, the funds brought to the Russian financial market exceeded the funds deposited with non-residents by 22.6 billion roubles.

The results of the activities of foreign-controlled banks in 2002 demonstrate further improvement of their financial condition. Current profit of these banks increased by almost a half (from 6.7 billion roubles as of January 1, 2002, to 10.0 billion roubles as of January 1, 2003). The number of profit-making banks rose from 25 to 31 and their profits grew from 7.1 billion roubles and 10.2 billion roubles. In the meantime, the number of banks incurring losses fell from 10 to six and the losses they incurred went down from 400 million roubles to 100 million roubles.

A rise in profits recorded by foreign-controlled banks in 2002 allowed them to improve their financial results significantly as compared to their performance in the previous years. As of January 1, 2003, their profits, including the financial results of previous years, amounted to 8.2 billion roubles compared to 900 million roubles as of January 1, 2002. All foreign-controlled banks are financially sound.

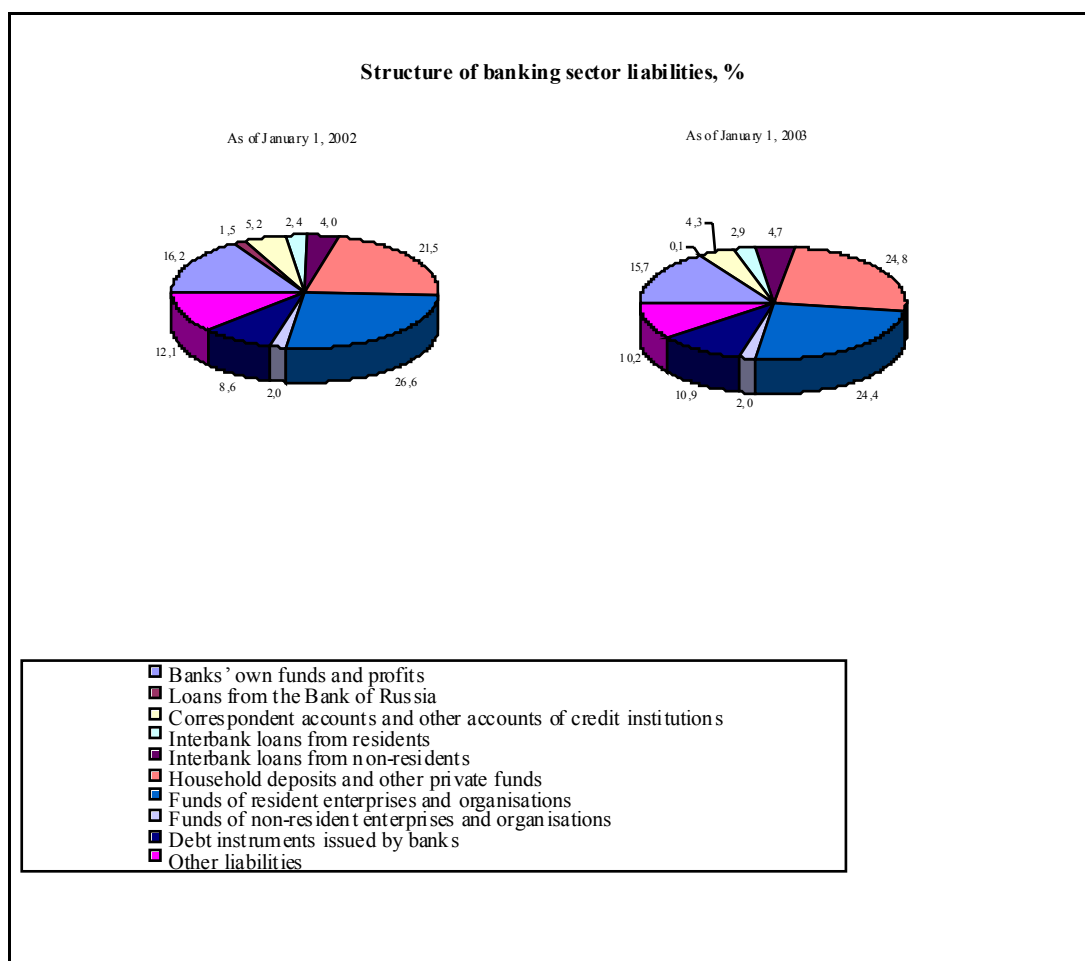
II.3. The development of banks' operations

II.3.1. Dynamics and structure of sources of funds

Development of the main banking sector parameters in 2002 indicate that the Russian banking system has overcome the aftermath of the financial and economic crisis of 1998 and continues to demonstrate an expansionary tendency. Household deposits were the last of the key quantitative banking sector indicators to reach the pre-crisis level in real terms: that happened in the middle of 2002. By the end of 2002 they had surpassed the pre-crisis level by 22.4%.

In 2002, the Russian banking sector continued to build up its credibility in the eyes of creditors and depositors and that helped credit institutions to expand their resource base (see Table 7 in the Statistical appendix).

The principal source of expansion of the banks resource base in 2002 was growth in customers' accounts: this item accounted for 36.7% of the overall increase in banking sector liabilities. As of January 1, 2003, household deposits and other private funds aggregated 1,029.6 billion roubles, or 24.8% of banking sector liabilities (see Chart 2.3).

Chart 2.3.

Foreign currency deposits grew most rapidly: while the amount of rouble denominated deposits rose by 45.6% in 2002 foreign currency deposits increased by 54.6%²². Nevertheless, rouble deposits continued to dominate and accounted for 61.5% of total deposits as of January 1, 2003. As for Sberbank, the leader of the retail deposit market, the ratio between its rouble and foreign currency deposits was 72% to 28% (with other Russian banks it was 39% to 61%).

The increased share of personal deposits with maturity over 1 year which expanded from 24.4% as of January 1, 2002, to 35.5% as of January 1, 2003 also indicates that the Russian banking sector has restored private customers' credibility.

Competition between banks on the household deposit market intensified considerably in 2002. Household deposits attracted by banks (excluding Sberbank) rose by 78%, while Sberbank increased the amount of these deposits by just 42%. Seventy-four percent of credit institutions that were in operation at the beginning of this year had a rise in household deposits.

However, Sberbank has retained its leadership on the household deposit market. As of January 1, 2002 it held a market share of 72.1% (489.0 billion roubles) and during the year its share reduced to 67.3% (693.0 billion roubles). Household

²² Here and below foreign currency is recalculated in US dollars terms.

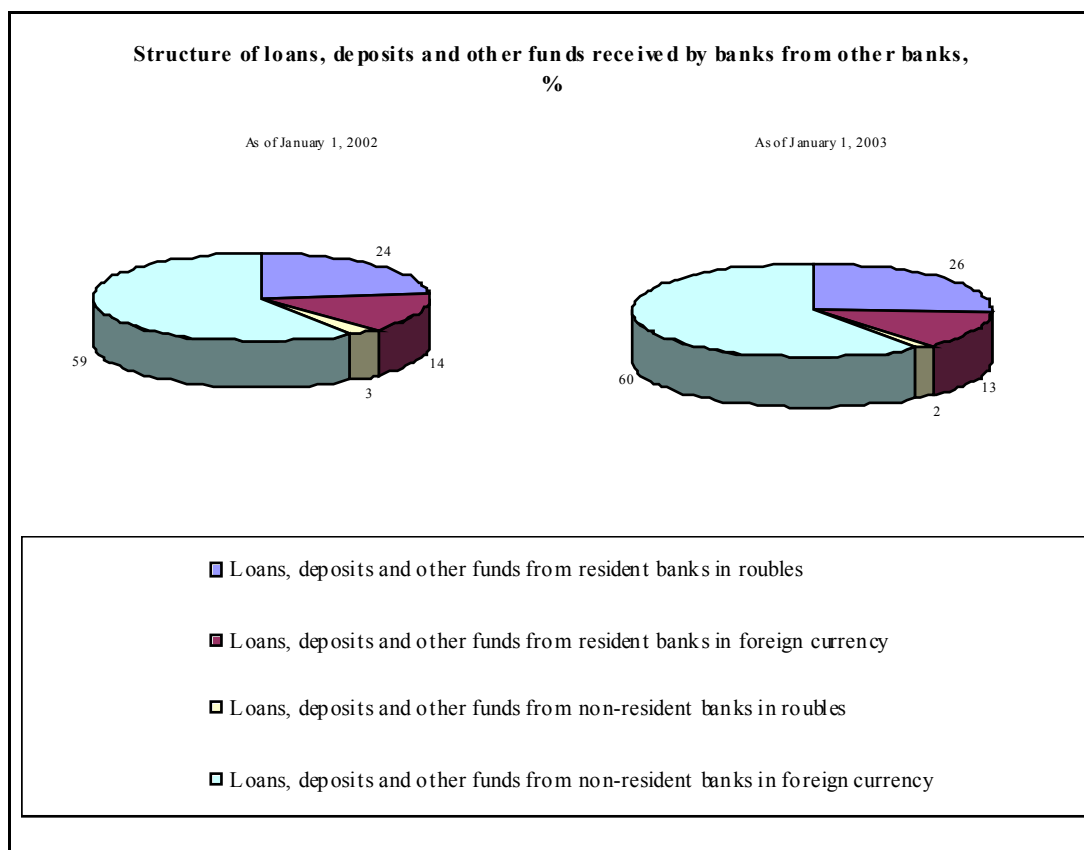
deposits accounted for 59% of Sberbank's liabilities as of January 1, 2003. Despite the 2002 expansion other banks' share of the household deposit market remains small.

The second largest source of expansion of credit institutions' resource base in 2002 were funds taken from enterprises and organisations, which increased by 20.9% (8.4% in real terms) to 1,091.4 billion roubles. Though their share in aggregate banking sector liabilities contracted from 28.6% as of January 1, 2002, to 26.3% as of January 1, 2003. Of the total amount of funds drawn from enterprises and organisations, 71% were deposited in settlement and current accounts. A similar trend was observed in the previous two years.

Overall growth in corporate deposits was 9.6%, while their share in aggregate banking sector liabilities contracted from 8.0% as of January 1, 2002, to 6.7% as of January 1, 2003. As for the foreign currency corporate deposits, their amount decreased by 9.7% in 2002. At the same time, the structure of deposits improved: deposits with longer maturities (over 1 year) rose by 60.1% in 2002 and their share in the total amount of deposits expanded during the year from 21.8% to 31.8%. Demand deposits and deposits with maturity up to 30 days decreased by 25.0% and their share in the total amount of deposits declined to 21.0% from 30.7% as of January 1, 2002.

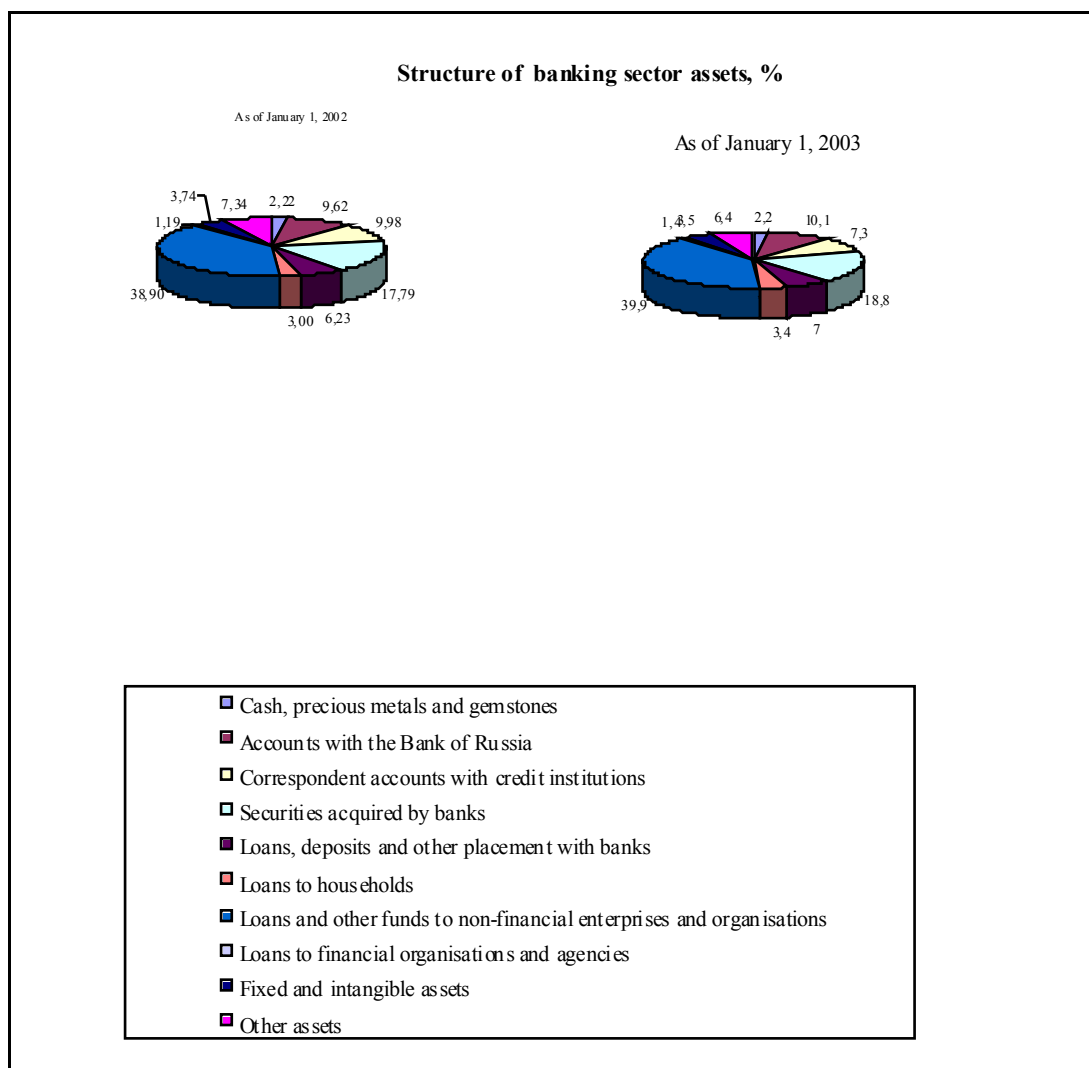
In 2002 there was an appreciable growth (65.3%) in the value of debt instruments issued by banks. As of January 1, 2003, their value amounted to 450.6 billion roubles. That growth largely resulted from the issue of bills of exchange - their value rose by 55.9%. As of January 1, 2003, the value of bills issued by banks amounted to 372.4 billion roubles and their share in banking sector liabilities stood at 9.0%. In 2002, the value of bonds, certificates of deposit and savings certificates increased by 2.4 times, but these debt instruments still play an insignificant role as a source of funds. As of January 1, 2003, these securities accounted for 1.8% of banking sector liabilities (as of January 1, 2002, their share stood at 1.0%).

Banks were rather active in conducting activities on the interbank market in 2002. Loans, deposits and other funds received by banks from other banks increased by 55.3% to 315.4 billion roubles and their share in banking sector liabilities expanded from 6.4% as of January 1, 2002, to 7.6% as of January 1, 2003. Like in previous years, about 60% of interbank loans were foreign currency loans received from non-resident banks (see Chart 2.4).

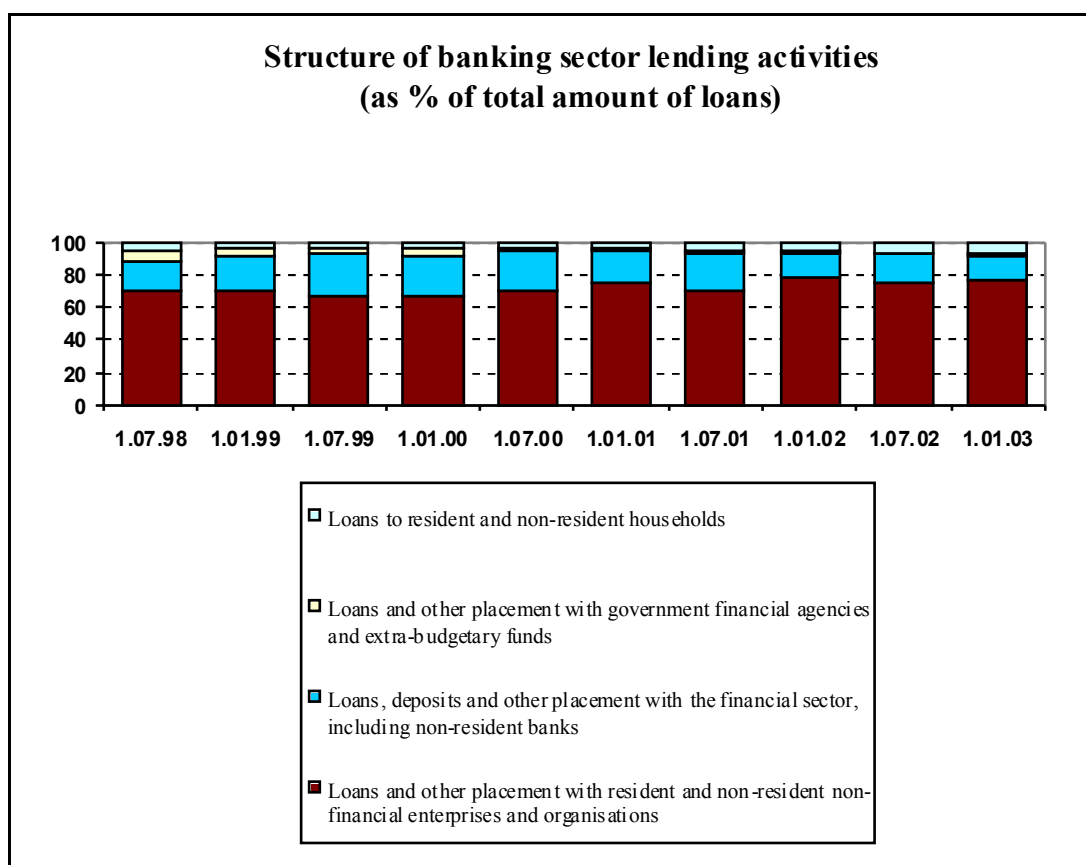
Chart 2.4.

II.3.2 Dynamics and structure of assets

In 2002 aggregate banking sector assets grew by 31.2% (17.8% in real terms) to 4,145.3 billion roubles as of January 1, 2003 (see Table 8 in the Statistical appendix). There was an marked expansion in the share of loans, deposits and other funds extended to non-financial enterprises and organisations in aggregate banking sector assets (39.9% as of January 1, 2003, against 38.9% as of January 1, 2002) (see Chart 2.5). Rouble denominated assets expanded by 34.8% (compared with inflation rate of 15.1%) while foreign currency denominated assets rose by 18.9%. There was a slight contraction in the foreign currency part of banking sector assets (from 37.9% to 36.2%). More than 4/5 of credit institutions operating at the end of 2002 registered an increase in their assets.

Chart 2.5.

Expansion of lending activities by banks made the biggest contribution to growth in banking sector assets. Despite a slight year-on-year fall in the rate of growth, the overall trend in lending was upward: in 2002 banks loans extended to the real sector rose by 35.2% (21.2% in real terms) to 1,591.4 billion roubles as of January 1, 2003 (see Table 9 in the Statistical appendix) and their share in aggregate assets of operating credit institutions expanded from 37.2% as of January 1, 2002, to 38.4% as of January 1, 2003. Seventy percent of operating credit institutions expanded lending to the real sector.

Chart 2.6.

This growth was caused by a combination of factors: on the one hand, it was a rise in companies' demand for loans to finance production, especially working assets, and a nascent tendency towards a fall in the price of bank loans amid a general reduction of interest rates in the economy. On the other hand, credit institutions were increasingly willing to lend as yields in the major segments of the financial market (Government securities and interbank loans) fell, the volumes and maturities of credit institutions' funds increased and the systemic risk of lending to non-financial enterprises declined due to macroeconomic stability.

Some changes were noted in the structure of bank loans²³ to different sectors of the economy. In 2002 the amount of outstanding loans rose very rapidly: to agriculture (68.6%), to the construction sector (45.1%), to trade and public catering (49.2%) and to transportation and communications (42.8%). The outstanding loans extended to industrial enterprises increased by 20.7% (including a 86.1% loan growth to machine-building enterprises). As a result, the share of loans extended to industrial enterprises dropped from 44.3% to 40.1% (the share of loans extended to machine-building enterprises increased from 5.4% to 7.5%), while the outstanding debt of agriculture rose from 1.9% to 2.4%, of the construction sector - from 4.4% to 4.8%, trade and public catering from 21.0% to 23.4% and transport and communications from 4.7% to 5.0%.

Loans extended to non-resident non-financial enterprises and organisations rose by 19.9%, while their share in total assets contracted from 1.7% to 1.5%.

²³ Information relating to various sectors of the economy is based on data reported by banks (Form No. 302).

Considerable growth in the volume of lending to the household sector was a noticeable trend in the development of banks' investment. Loans extended to households rose from 93.3 billion roubles to 141.2 billion roubles, an increase of 50%, while the share of these loans in aggregate assets expanded from 3.0% as of January 1, 2002, to 3.4% as of January 1, 2003. Most of this growth was ensured by a small number of banks specialising in consumer lending. Despite the dynamic development of this segment of the market, its further growth is inhibited by inadequate legislation (it is necessary to enhance the efficiency of the mortgage mechanism and encourage the development of the mortgage business) and the lack of mechanisms to protect consumers' interests.

There was a slight expansion in the scale of operations conducted on the interbank and securities markets in 2002.

Claims on interbank loans, deposits and other borrowed funds rose by 48.0% in 2002 and their share in banking sector assets expanded from 6.2% to 7.0%. At the same time, rouble loans, deposits and other funds placed by banks on the domestic interbank market increased by 68.2% and the amount of foreign currency funds placed with non-resident credit institutions expanded by 34.8%.

Banks' investments in Government securities rose faster in 2002 than 2001. Over the year, bank investments in these financial instruments rose by 22.0% as against 9.0% in 2001 and amounted to 412.8 billion roubles as of January 1, 2003. However, as the overall expansion of banks' active operations, especially lending, was far more significant, the share of Government securities in aggregate banking sector assets contracted from 10.7% as of January 1, 2002, to 10.0% as of January 1, 2003. At the same time, banks' speculative operations with securities demonstrated even more significant growth. In the May-December period alone²⁴, banks' investment portfolio expanded by 1.6 times.

As the macroeconomic situation gradually stabilised, the corporate securities market grew more active. Banks' investments in stocks and shares rose by 43.4%, although their share in banking sector assets only expanded slightly: from 1.5% as of January 1, 2002, to 1.7% as of January 1, 2003.

The value of bills discounted by banks rose by 41.5% in 2002 and as of January 1, 2003, it amounted to 208.5 billion roubles, while their share in banking sector assets slightly expanded (from 4.7% as of January 1, 2002, to 5.0% as of January 1, 2003). Bills issued by Russian enterprises and organisations accounted for 73.9% of the bills discounted by banks, bank bills accounted for 20.1% and bills issued by non-residents 5.2%. Special mentions should be made here of extremely rapid growth in investments in bank bills, which expanded by 4.9 times. A rise in the demand for bank bills is attributable to growth in the value of bills issued by financially sound banks.

²⁴ The changes in the principles of accounting for securities, which were put into effect on May 1, 2002, by Bank of Russia Ordinance No. 1054-U, dated November 20, 2001, only allow this trend to be monitored from May 2002.

The expansion of lending operations by banks and bank operations on the securities market caused the balances in banks' correspondent accounts in other banks to contract by 4.6%. As a result, their share in aggregate banking sector assets decreased from 10.0% as of January 1, 2002, to 7.3% as of January 1, 2003 from 7.3% to 4.7% in accounts with non-resident banks.

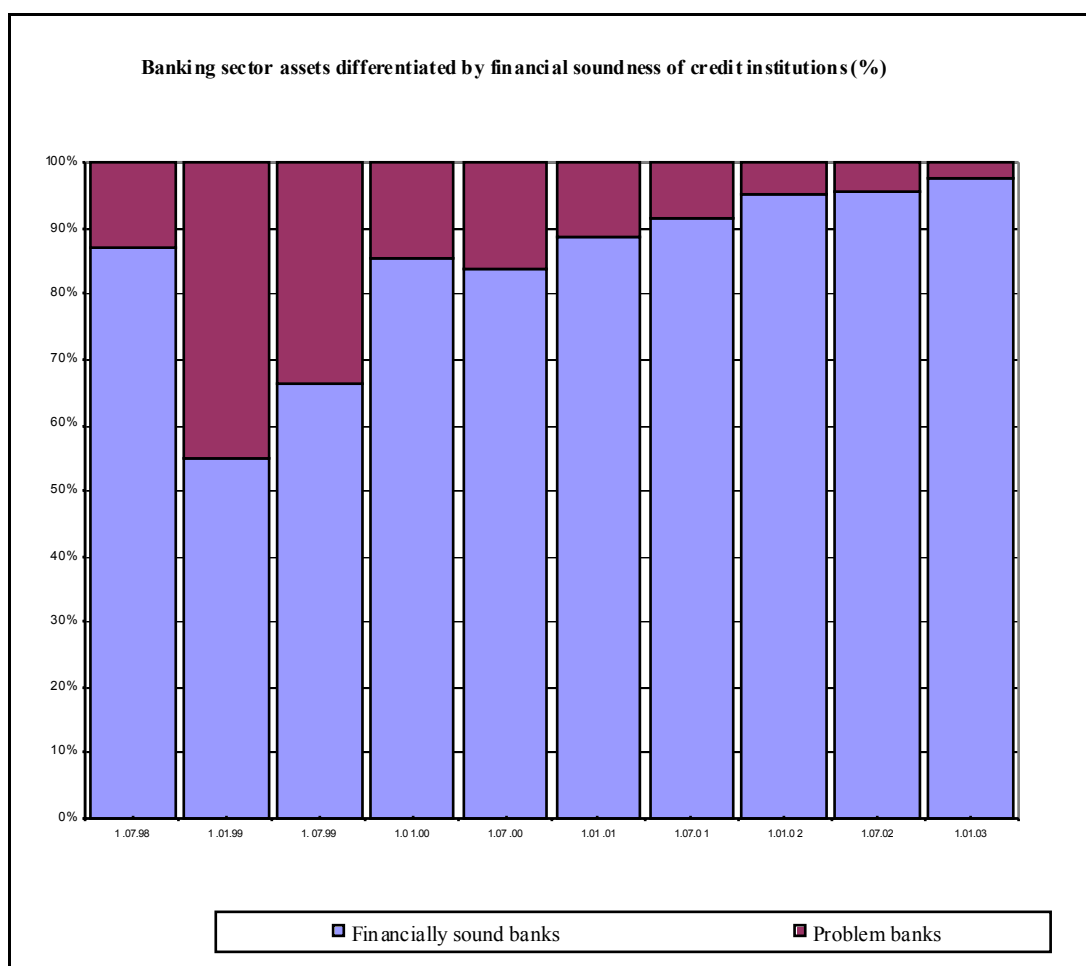
The share of the balances in banks' correspondent accounts, deposits and other placement with the Bank of Russia expanded from 4.6% of aggregate banking sector assets as of January 1, 2002, to 5.1% as of January 1, 2003.

II.4. The financial condition of credit institutions

II.4.1. Financial results

The analysis of the financial results of operating credit institutions in 2002 shows that their financial condition is, by and large, stable.

Chart 2.7.



The number of financially sound credit institutions, which include two groups of credit institutions, such as “credit institutions without shortcomings in their activity” and “credit institutions with certain shortcomings in their activity”²⁵, amounted to 1,269 as of January 1, 2003 (there were 1,227 as of January 1, 2002) and their share in

²⁵ According to Bank of Russia Ordinance No. 766-U, dated March 31, 2000.

the total number of operating credit institutions grew from 93.1% as of January 1, 2002, to 95.4% as of January 1, 2003. The share of the assets of financially sound credit institutions in aggregate banking sector assets continued to expand: as of January 1, 2003, it stood at 97.6% against 95.1% as of January 1, 2002 (see Chart 2.7). These credit institutions accounted for 97.4% of all funds drawn from enterprises and organisations (95.9% in 2001), 99.1% of household deposits (98.5% in 2001), 94.4% of budget funds (92.2% in 2001) and 94.1% of interbank loans (83.5% in 2001).

In 2002, operating credit institutions recorded a profit of 93 billion roubles, an increase of 40% over 2001 (67.6 billion roubles). The number of profit-making banks amounted to 1,279 as of January 1, 2003, a slight rise over the beginning of the year (1,257). At the same time, the number credit institutions which incurred losses was 58 as of January 1, 2002 compared to 46 as of January 1, 2003²⁶.

There was a slight increase in the return on banking sector assets²⁷: 2.6% in 2002 against 2.5% in 2001. The return on capital²⁸ was 18.1% in 2002, that is remained high, but a little lower than in 2001 (19.4%). These dynamics of profitability are the result of movement of its various factors, such as financial results, assets and capital²⁹.

Unlike the situation in the previous years, in 2002 it was banks with a capital in excess of 5 million euros that demonstrated the highest profitability levels. In 2002, their return on assets was 3.0% and return on capital 18.1% (the respective percentages for the banking sector as a whole were 2.6% and 18.1%). Other credit institutions with smaller capital in 2002 registered lower returns on assets and capital than in the previous years.

Compared to other branches of the economy, the banking sector has the highest return on capital, while the average figure for the economy as a whole was less than 8%³⁰, according to the State Statistics Committee, or Goskomstat (see Table 10 in the Statistical appendix).

The profits received by operating credit institutions in 2002 covered all the losses they made in the previous years, mostly incurred as a result of the 1998 crisis. As of January 1, 2003, profit, calculated taking account of the results of the previous years, amounted to 27.4 billion roubles.

II.4.2. Structure of income and expenses

The change in the structure of banking operations had a telling effect on the structure of bank income and expenses. As lending to the real sector expanded and the

²⁶ Four credit institutions failed to submit their reports as of January 1, 2003.

²⁷ The return on assets is calculated as the ratio of profit to assets. Annual pre-tax earnings (profit-and-loss balance) and the chronological average value of assets are used for calculation.

²⁸ The return on capital is calculated as the ratio of profit to capital. Full-year pre-tax earnings (profit-and-loss balance) and the average annual (average chronological) amount of capital are used for calculation.

²⁹ 2002 earnings (profit) rose by 38%, banks' assets (annual averages) expanded by 30% and capital increased by 48%.

³⁰ According to Goskomstat methodology, the return on capital is calculated as the ratio of profit before taxation to end-of-period capital. Calculated according to this methodology, the Russian banking sector's return on capital in 2002 was 16%.

quality of loans remained stable, interest income from loans grew throughout the period under review. As a result, the share of interest income in the total amount of income expanded from 13.1% as of January 1, 2002, to 18% as of January 1, 2003.

Income received from non-financial enterprises and organisations accounted for 73.6% of interest income from loans. The role of interest income received from lending to the household sector has also been growing: this income are the second most important source of interest income from loans (9%).

Interest received under loan agreements accounted for most of interest income (90%). At the same time, the share of interest received for overdue loans and overdue interest received remained virtually unchanged.

As banks expanded their trade operations on the securities market, their income from transactions with securities increased. In 2002, income from operations with securities rose faster than interest income from loans (58% as against 40%). As a result, the share of income from operations with securities expanded from 6.5% of the total amount of income as of January 1, 2002, to 10.1% as of January 1, 2003. Mention should be made of the considerable growth in the share of income from resale of securities, which expanded from 24.6% of total income from operations with securities as of January 1, 2002, to 37.0% as of January 1, 2003, while the share of interest income from investments in debt instruments contracted from 46.5% to 32.2% respectively.

As banks found it increasingly difficult to make profits on the foreign exchange market, the share of income from operations with foreign exchange contracted from 32.7% of aggregate banking sector income as of January 1, 2002, to 27.8% as of January 1, 2003.

Commission income continued to rise. In 2002, they expanded by 28% and their share in total banking sector income increased from 2.9% as of January 1, 2002, to 3.7% as of January 1, 2003.

The share of expenses on operations with foreign exchange continued to contract in the structure of expenses of operating credit institutions in 2002. At the same time, there was an expansion in the share of interest expenses, mainly due to interest paid to households on deposits. A similar situation applied to the share of expenses on operations with securities: as of January 1, 2003, it reached 5.4% against 3.2% a year earlier.

The above changes in the structure of income and expenses impacted the structure of net income³¹ and profit of credit institutions. Net interest income made up the largest part of credit institutions' net income in 2002 (61.9% as of January 1, 2002, and 60.5% as of January 1, 2003). The share of net income from operations with securities expanded significantly (from 11.9% as of January 1, 2002, to 16.1% as of January 1, 2003).

³¹ Financial result before the formation (recovery) of provisions, maintenance and administrative costs excluded.

The share of net commission income contracted from 20% as of January 1, 2002, to 17% as of January 1, 2003 and the share of net income from operations with foreign exchange narrowed from 11.2% to 8.8% respectively. There was a reduction by more than a quarter in net other expenses (losses), formed mainly due to the banks' balance of income and expenses on fines, penalties, operations with precious metals and futures transactions. These losses accounted for 2.4% of total net income as of January 1, 2003, against 4.8% as of January 1, 2002.

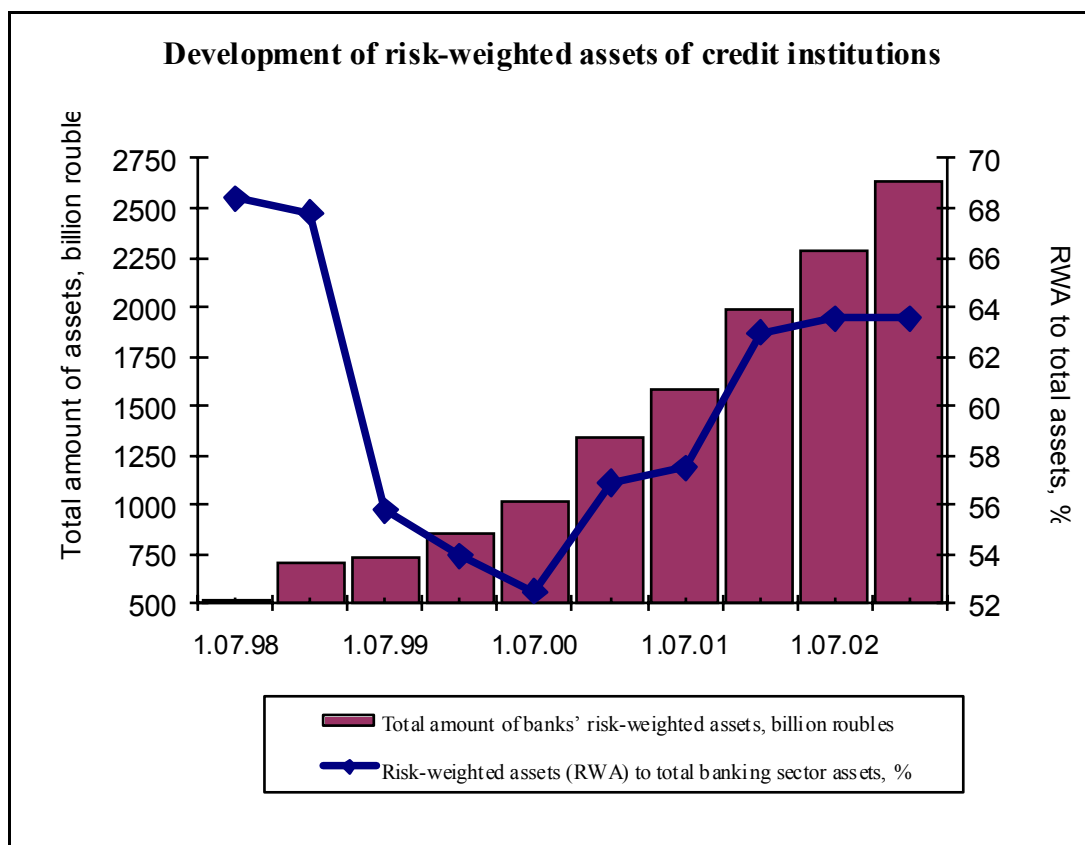
At the same time, provisions for possible losses (net of recovered provisions) increased in absolute terms from 29.4 billion roubles as of January 1, 2002, to 43.5 billion roubles as of January 1, 2003 (the share of net income allocated for the creation of such provisions was practically unchanged). The share of net income allocated for the formation of taxable profit expanded from 34.5% as of January 1, 2002, to 36.3% as of January 1, 2003.

II.5. Banking sector risks

II.5.1. Capital adequacy

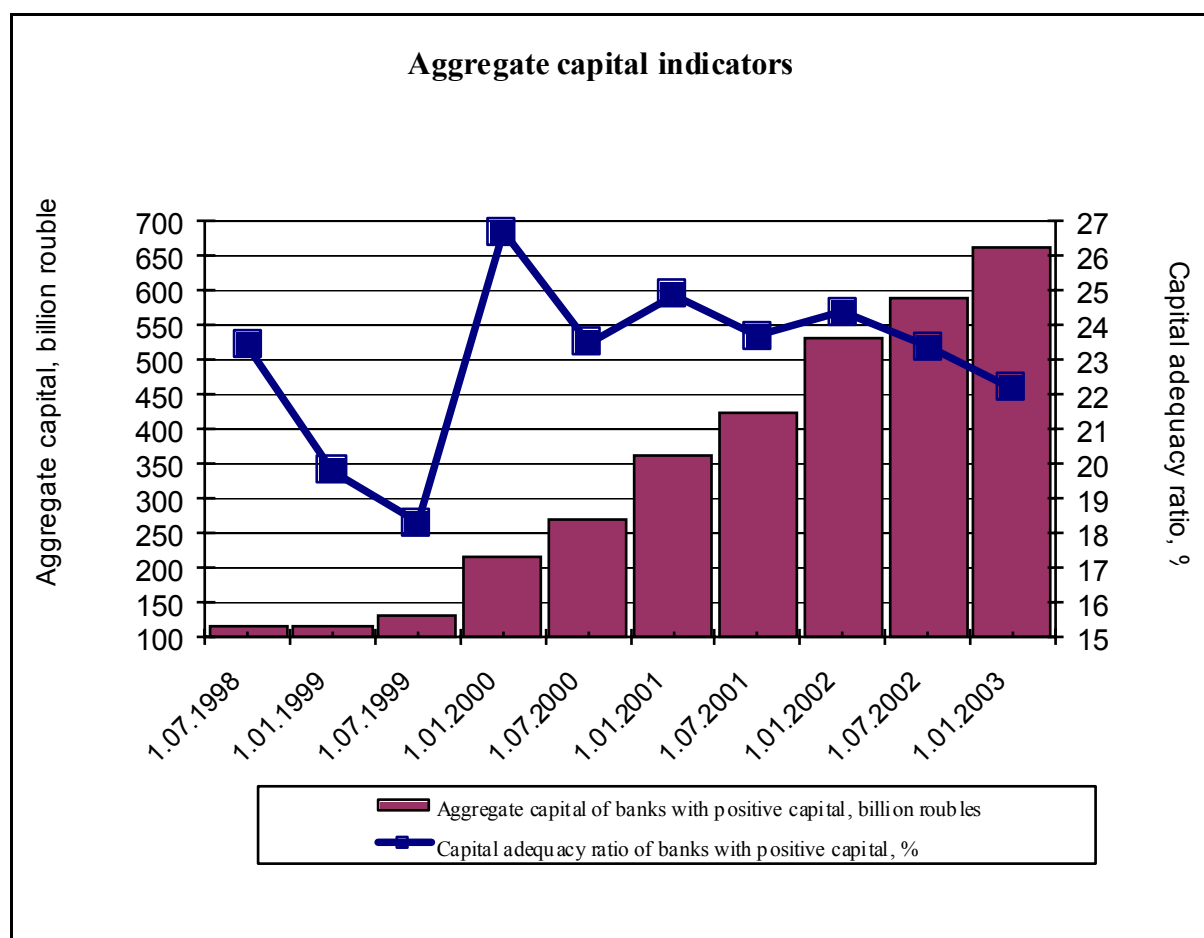
Capital adequacy registered 22.2% in 2002 against 24.4% in 2001³². The fall occurred because aggregate risk of credit institutions rose faster (36.9%) than their capital (24.8%). Nevertheless, the general level of capital adequacy was rather high in nominal terms.

³² Calculated for banks with positive capital.

Chart 2.8.

There were practically no credit institutions in 2002 that failed to comply with the N1 (capital adequacy) ratio established by the Bank of Russia: as of January 1, 2003, only three banks failed to comply with this ratio with their share in aggregate banking sector assets being 0.9%.

Chart 2.9.



The level of capitalisation of largest banks is a major indicator of stability of the banking sector. The average capital adequacy of top 20 largest (in terms of assets) banks was 17.9% as of January 1, 2003, as against 20.2% as of January 1, 2002.

II.5.2. Liquidity risk

The improved macroeconomic indicators and increased confidence in the banking sector have an overall favourable influence on the formation of the resource base of Russian banks. Although a shortage of medium- and long-term obligations remains a problem for the Russian banking sector, there is a tendency for maturities of banks' debt obligations to increase.

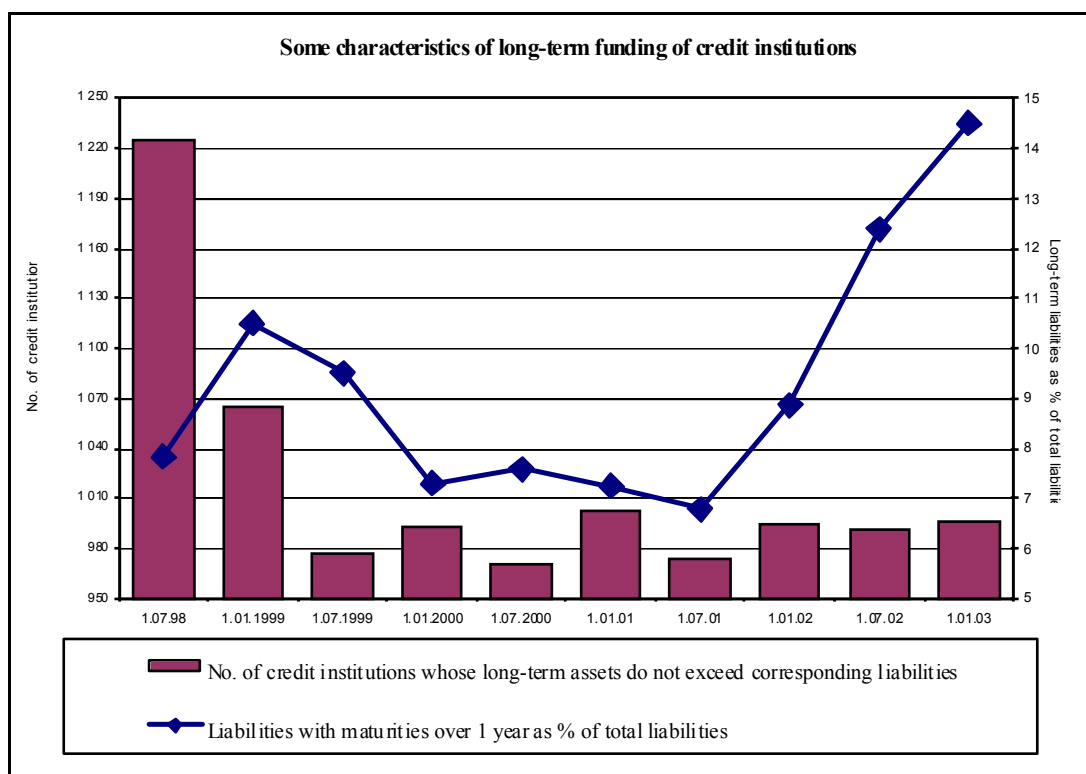
In 2002, the share of liabilities with maturities less than 1 month slightly contracted and as of January 1, 2003, these liabilities accounted for 46.0% of their total amount against 49.6% as of January 1, 2002. Most of the liabilities with maturities shorter than 1 month were call obligations: these accounted for 73% as of January 1, 2003, as against 76% a year earlier.

The share of liabilities with maturities from 1 month to 1 year was practically unchanged at 24.9% (25.1% as of January 1, 2002).

Special mention should be made of significant growth in the share of liabilities with maturities over 1 year: in 2002, their share expanded from 25.0% to 28.8%. As for the net borrowed funds of credit institutions, that is, liabilities net of the sources of

own funds, the share of liabilities with maturities over 1 year expanded to almost 15% as of January 1, 2003, from 9% as of January 1, 2002. This means almost doubling over the pre-crisis level (7.8% as of July 1, 1998; see Chart 2.10).

Chart 2.10.



While the average maturity of bank liabilities lengthened, the maturity structure of bank assets remained virtually unchanged during 2002. As of January 1, 2003, assets with terms shorter than 1 month accounted for 36.3% of aggregate banking sector assets, assets with maturities from 1 month to 1 year 32.9% and assets with maturities over 1 year 30.5% (at the beginning of 2002, the respective percentages stood at 37.0%, 32.0% and 30.6%).

As a result of the above changes, banks significantly scaled down the use of short-term obligations as a source of long-term assets³³. As of January 1, 2003, respective relation contracted to 2.8%, that is, it decreased by almost 3 times compared to the beginning of 2002 (8.1%). As of January 1, 2003, 999 credit institutions did not use short-term obligations as a source of long-term assets (see Chart 2.10). The distribution of credit institutions according to the deficit of liquidity coverage³⁴ (see Table 11 in the Statistical appendix) remained unchanged.

Extended maturity of the banks' funds and the formation of sustained long-term liabilities are a major prerequisite for the development of long-term lending. The reduction of the deficit of liquidity coverage and the use of short-term obligations as a

³³ Calculated as the ratio of the excess of long-term (longer than 1 year) assets over corresponding liabilities to short-term liabilities (shorter than 1 year).

³⁴ The deficit of liquidity coverage is the ratio of the excess of call obligations and obligations with terms up to 30 days over assets of same maturities to the total amount of these obligations.

source of long-term assets testify to positive dynamics of long-term banking sector liquidity.

Banks' overdue liabilities declined by 3.4% to 10.6 billion roubles. Most of them (66%) were owed by banks under the control of ARCO (61% as of January 1, 2002). As of January 1, 2003, the share of overdue liabilities accounted for 0.33% of aggregate banking sector liabilities.

In 2002, the number of banks that had overdue liabilities in their books somewhat grew (from 99 to 107), while the share of their assets in aggregate banking sector assets diminished from 14.6% as of the beginning of 2002 to 12.0% as of January 1, 2003. Of the top 20 banks in terms of assets, two had overdue balance sheet liabilities (three at the beginning of 2002).

II.5.3. Credit risk

According to data reported by credit institutions in 2002, the quality of loan portfolios remained high. Standard loans accounted for 90.1% of loans as of January 1, 2003 (89.4% a year before), doubtful loans accounted for 1.8% (2.1%) and bad loans stood at 3.8% (4.2%)³⁵.

The number of banks with more than 90% of standard loans in their loan portfolios rose from 895 to 959 in 2002 and their assets represented more than 70% of aggregate banking sector assets.

The number of credit institutions that failed to comply with the large loans ratio (N7) fell from 10 to 1 in 2002 and their share in banking sector assets contracted from 1.6% to 0.17%.

During the year the aggregate amount of large loans (large credit risks) in the banking sector rose by 35.3% from 982.3 to 1,328.9 billion roubles. As a result, the share of large loans in banking sector assets expanded by one percentage point to 32.1%. Like in the previous years, a high concentration of credit risks was predetermined by practice of connected lending, as well as insufficient creditworthiness and transparency of significant part of domestic companies.

The number of credit institutions that failed to comply with the N6 ratio (maximum risk per borrower or a group of connected borrowers) also declined: from 83 as of January 1, 2002, to 51 as of January 1, 2003. However, the share of such credit institutions in aggregate banking sector assets remained at a high level of 42% (45% as of January 1, 2002).

In 2002, the number of banks that failed to comply with the N9 ratio (maximum credit risk per shareholder/member) and N10 ratio (maximum amount of loans extended to insiders and guarantees and sureties issued for their benefit) declined and their share in aggregate banking sector assets contracted.

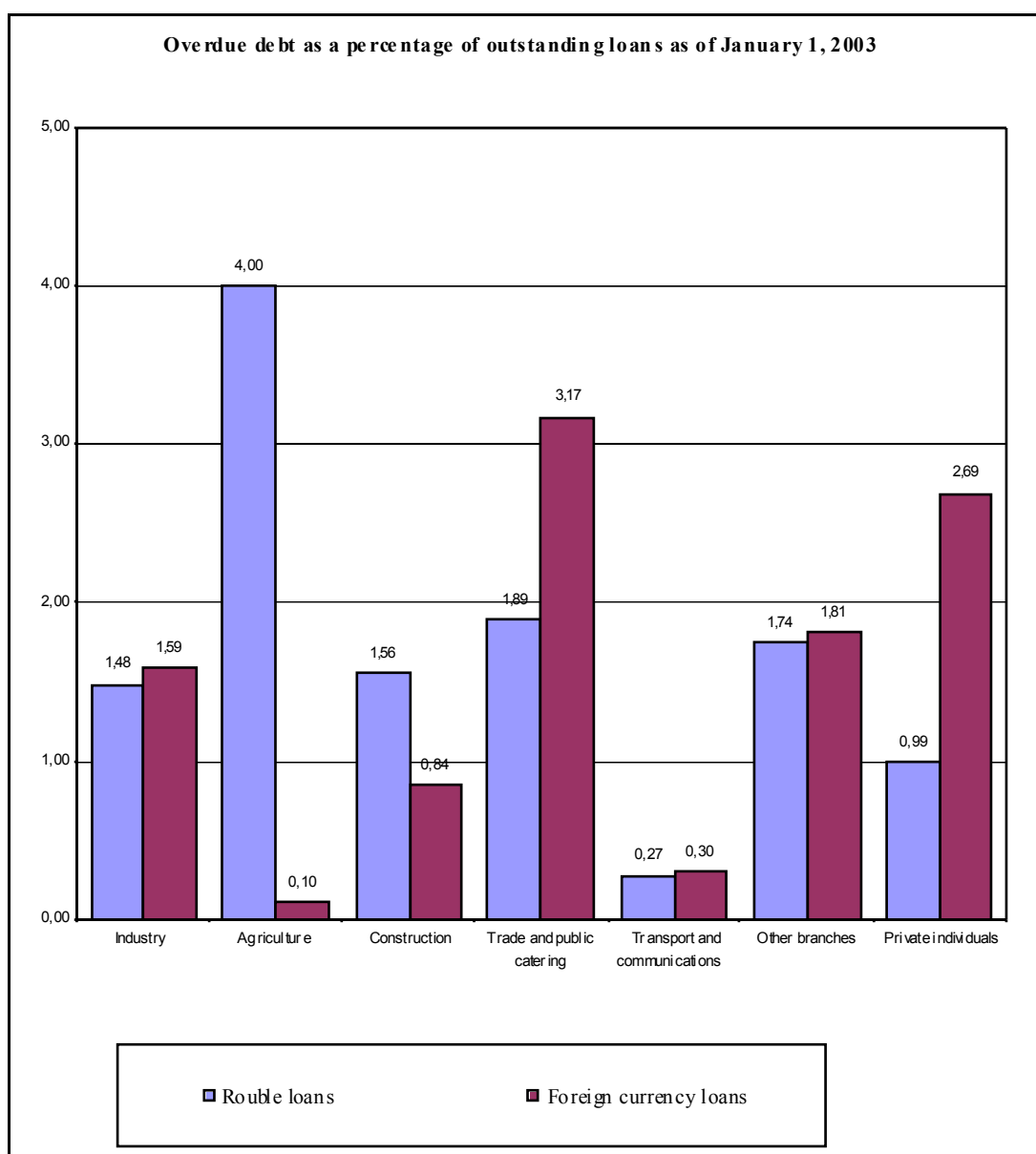
³⁵ By international banking supervision standards, credit risk is considered high if bad loans account for more than 10% of the aggregate loan portfolio.

The level of overdue loans, deposits and other funds placed by banks (hereinafter referred to as overdue debt) allows to evaluate the credit risk in the banking sector as moderate in 2002. Against the dynamic expansion of lending operations by banks (lending volumes expanded by more than 20% in real terms in 2002), the share of overdue debt in total loans went down from 2.6% to 1.9%, according to data reported by banks.

The share of overdue debt in loans to non-financial enterprises and organisations contracted to 1.8% as of January 1, 2003, from 2.3% at the beginning of 2002, of which the share of overdue debt on rouble denominated loans stood at 1.7% and foreign currency loans 1.9% (as of January 1, 2002, 1.6% and 4.0% respectively).

The highest share of overdue debt on rouble denominated loans was registered in agriculture (4%) (see Chart 2.11), but in general, the ratios of overdue debt on loans differ little from sector to sector and do not depend much on the loan currency.

Chart 2.11.



In 2002 the share of credit institutions with overdue debt less than 5% of their loan portfolios remained unchanged and was more than 80% of operating banks. They accounted for 91% of banking sector assets. In 157 credit institutions overdue debt exceeded 10% of their portfolios and these banks accounted for less than 9% of banking sector assets.

According to data reported by banks, throughout 2002 credit institutions on the whole complied with Bank of Russia loan loss provision (LLP) requirements. As of January 1, 2003, the number of banks that met in full the LLP requirements was 1,212 and they accounted for 92.3% of banking sector assets (1,199 banks and 95.6% of banking sector assets as of January 1, 2002).

According to data reported by banks, the LLP accounted for 6.3% of the total loans. As of January 1, 2003, the LLP accounted for 113% of loans classified by banks to credit risk groups 3 and 4.

As of January 1, 2003, 47 banks representing 1.3% of banking sector assets, had LLP that covered less than 75% of the aggregate amount of their doubtful and bad loans (there were 65 such banks and they accounted for 2.1% of aggregate assets at the beginning of 2002).

II.5.4. Market risk

From April 1, 2000, the evaluation of capital adequacy of Russian credit institutions takes into account market risk, which is calculated in accordance with the procedure set by Bank of Russia's Regulation No. 89-P, dated September 24, 1999. Between January 1, 2002, to January 1, 2003, the number of credit institutions that calculated market risk calculations increased from 808 to 848³⁶ and their share in banking sector assets expanded from 90% to 95%.

In the period under review the size of banking sector market risk increased by almost 1.5 times, but relative to the capital of the banks that calculated market risk it did not increase much (from 32% to 37%)³⁷. Nevertheless, market risk still accounts for 7% of aggregate banking risk.

The expansion of bank operations on the stock market brought about substantial changes in the structure of market risk: the share of interest risk³⁸ in banking sector market risk in 2002 expanded from 12.3% to 18.6% and that of the stock risk from 17.3% to 31.5%. Despite these changes, currency risk remains the main component of market risk: at the beginning of this year its share stood at 49.8% as against 70.4% at the beginning of last year.

As of January 1, 2003, 813 banks that accounted for 93% of banking sector assets included currency risk in calculation of capital adequacy ratios (as of January 1, 2002, 776 banks that accounted for 88% of banking sector assets did so). By comparison, 93 banks that accounted for 22% of banking sector assets included stock

³⁶ Excluding banks under the control of ARCO.

³⁷ The ratio of aggregate banking risk to capital (the inverse of the capital adequacy ratio) stood at 524% as of January 1, 2003.

³⁸ The Basel Committee regards interest risk as a separate kind of risk.

risk in their capital adequacy calculations as of January 1, 2003, and 145 banks that accounted for 25% of banking sector assets included interest risk in their calculations. Only 69 credit institutions that accounted for 20% of banking sector assets as of January 1, 2003, included all the three kinds of market risk in their calculations.

In 2002 the foreign currency component of banks' assets and liabilities remained, by and large, stable: the difference between the foreign currency ratios of assets and liabilities decreased from 5.8 percentage points to 4.4 percentage points. The ratio of off-balance sheet and balance sheet operations of credit institutions in foreign currency also remained stable at some 22-26%.

Minor changes were registered in banks' compliance with the open currency position requirements. Thirty-seven credit institutions violated OCP requirements on an average quarterly basis in 2002 (32 in 2001). As of January 1, 2003, banks that violated OCP limits accounted for 9.0% of banking sector assets (8.0% as of January 1, 2002).

III. THE STATISTICAL APPENDIX

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Table 1

Supervisory staff of the Bank of Russia as of January 1, 2003

DIVISION TITLE	Nominal number of jobs as of Jan. 1, 2003	Total number of employees as of Jan. 1, 2003 (excluding part-timers)	of whom							
			age			education		career in banking sector		women
			under 30 (born 1973 and later)	50 plus (born 1952 and earlier)	of whom women over 55 and men over 60	higher	vocational secondary	3 years and under	15 years and more	
Central Office										
Department for Banking Regulation and Supervision	165	149	29	38	10	145	4	16	69	106
Credit Institutions Licensing and Financial Rehabilitation Department	135	122	39	18	6	109	12	11	47	89
Department for Foreign Exchange Regulation and Control	120	99	38	17	3	90	5	21	19	63
Main Inspectorate of Credit Institutions	111	37	13	6	2	35	2	7	5	17
Total in the Central Office	531	407	119	79	21	379	23	55	140	275
Regional Branches										
Bank Supervision Division (Department)	1 426	1 403	284	212	45	1 318	77	72	427	1 180
Bank Inspection Division (Department)	1 073	1 048	188	183	40	1 008	34	48	194	582
Foreign Operations Division (Department)	686	673	162	63	15	649	18	57	114	450
Sectors of the Moscow Branch	587	582	211	81	22	484	84	88	72	409
Total of the Regional Branches/National Banks	3 772	3 706	845	539	122	3 459	213	265	807	2 621
Total of the Bank of Russia	4 303	4 113	964	618	143	3 838	236	320	947	2 896

Table 2

Number of inspections of main offices and branches of credit institutions conducted by the Bank of Russia in 2002

№	Bank of Russia Divisions (grouped by Federal District)	No. of credit institutions as of Jan. 1, 2002	No. of bank branches as of Jan. 1, 2002	No. of inspections by plan	Actual number of inspections			Examined through comprehensive inspections		Examined through thematic inspections	
					TOTAL	credit institutions	branches of credit institutions	credit institutions	branches of credit institutions	credit institutions	branches of credit institutions
1	2	3	4	5	6	7	8	9	10	11	12
1. Central federal district											
1.1.	Bank of Russia Regional Branch for the Belgorod Region	6	29	16	35	12	23	1	3	11	20
1.2.	Bank of Russia Regional Branch for the Braynsk Region	2	32	12	19	4	15	2	2	2	13
1.3.	Bank of Russia Regional Branch for the Vladimir Region	3	37	17	41	5	36	2	4	3	32
1.4.	Bank of Russia Regional Branch for the Voronezh Region	4	38	32	51	10	41	2	1	8	40
1.5.	Bank of Russia Regional Branch for the Ivanovo Region	5	17	8	29	12	17	3	2	9	15
1.6.	Bank of Russia Regional Branch for the Tver Region	8	30	15	28	14	14	6	4	8	10
1.7.	Bank of Russia Regional Branch for the Kaluga Region	6	31	29	55	16	39	3	1	13	38
1.8.	Bank of Russia Regional Branch for the Kostroma Region	6	13	20	37	11	26	2	0	9	26
1.9.	Bank of Russia Regional Branch for the Kursk Region	2	28	20	24	3	21	1	1	2	20
1.10.	Bank of Russia Regional Branch for the Lipetsk Region	2	22	17	17	4	13	1	1	3	12
1.11.	Bank of Russia Regional Branch for the Orel Region	2	20	10	35	4	31	1	2	3	29
1.12.	Bank of Russia Regional Branch for the Ryazan Region	6	27	19	24	12	12	4	0	8	12
1.13.	Bank of Russia Regional Branch for the Smolensk Region	4	29	10	39	5	34	2	3	3	31
1.14.	Bank of Russia Regional Branch for the Tambov Region	2	29	7	22	3	19	2	3	1	16
1.15.	Bank of Russia Regional Branch for the Tula Region	7	34	8	31	7	24	5	2	2	22
1.16.	Bank of Russia Regional Branch for the Yaroslavl Region	10	32	21	49	17	32	10	4	7	28
1.17.	Moscow Branch (Moscow and the Moscow Region)	639	320	266	1 068	814	254	186	10	628	244
TOTAL		714	768	527	1 604	953	651	233	43	720	608
2. North-Western federal district											
2.1.	Bank of Russia Regional Branch for the Arkhangelsk Region	5	30	13	31	7	24	3	0	4	24
2.2.	Bank of Russia Regional Branch for the Vologda Region	9	45	45	53	15	38	5	2	10	36
2.3.	Bank of Russia Regional Branch for the Kaliningrad Region	13	31	30	49	24	25	5	3	19	22
2.4.	St. Petersburg Branch	42	111	146	235	93	142	16	4	77	138
2.5.	Bank of Russia Regional Branch for the Leningrad Region	4	40	44	44	9	35	3	3	6	32
2.6.	Bank of Russia Regional Branch for the Murmansk Region	4	26	35	42	8	34	4	2	4	32
2.7.	Bank of Russia Regional Branch for the Novgorod Region	2	29	9	21	5	16	1	5	4	11
2.8.	Bank of Russia Regional Branch for the Pskov Region	5	14	13	22	10	12	4	1	6	11
2.9.	Bank of Russia National Bank of the Republic of Karelia	1	28	8	25	3	22	1	4	2	18
2.10.	Bank of Russia National Bank of the Komi Republic	6	42	16	42	14	28	4	4	10	24

1	2	3	4	5	6	7	8	9	10	11	12
TOTAL		91	396	359	564	188	376	46	28	142	348
3. Southern federal district											
3.1.	Bank of Russia Regional Branch for the Krasnodar Territory	28	106	25	102	40	62	17	7	23	55
3.2.	Bank of Russia Regional Branch for the Stavropol Territory	11	54	44	58	17	41	5	7	12	34
3.3.	Bank of Russia Regional Branch for the Astrakhan Region	4	29	50	50	6	44	3	6	3	38
3.4.	Bank of Russia Regional Branch for the Volgograd Region	6	57	24	63	11	52	5	7	6	45
3.5.	Bank of Russia National Bank of the Republic of Ingushetia	2	4	5	6	3	3	2	0	1	3
3.6.	Bank of Russia Regional Branch for the Rostov Region	25	104	48	109	38	71	17	21	21	50
3.7.	Bank of Russia National Bank of the Republic of Adygeya	5	10	12	18	10	8	2	1	8	7
3.8.	Bank of Russia National Bank of the Republic of Daghestan	40	76	47	167	70	97	19	0	51	97
3.9.	Bank of Russia National Bank of the Kabardino-Balkar Republic	6	16	11	35	16	19	4	1	12	18
3.10.	Bank of Russia National Bank of the Republic of Kalmykia	3	5	9	14	6	8	3	1	3	7
3.11.	Bank of Russia National Bank of the Republic of North Ossetia-Alaniya	6	19	9	28	11	17	3	1	8	16
3.12.	Bank of Russia National Bank of the Karachai-Circassian Republic	7	6	5	17	12	5	5	0	7	5
TOTAL		143	486	289	667	240	427	85	52	155	375
4. Volga federal district											
4.1.	Bank of Russia Regional Branch for the Nizhni Novgorod Region	21	85	42	110	27	83	10	13	17	70
4.2.	Bank of Russia Regional Branch for the Kirov Region	3	50	4	24	4	20	2	1	2	19
4.3.	Bank of Russia Regional Branch for the Samara Region	23	80	22	80	37	43	10	6	27	37
4.4.	Bank of Russia Regional Branch for the Orenburg Region	11	41	28	47	26	21	5	2	21	19
4.5.	Bank of Russia Regional Branch for the Penza Region	2	32	17	50	9	41	0	5	9	36
4.6.	Bank of Russia Regional Branch for the Perm Region	11	55	15	57	19	38	5	4	14	34
4.7.	Bank of Russia Regional Branch for the Saratov Region	18	73	22	95	41	54	11	11	30	43
4.8.	Bank of Russia Regional Branch for the Ulyanovsk Region	7	26	23	27	10	17	4	4	6	13
4.9.	Bank of Russia National Bank of the Republic of Bashkortostan	14	58	33	37	20	17	9	0	11	17
4.10.	Bank of Russia National Bank of the Republic of Marii El	1	24	11	23	1	22	1	2	0	20
4.11.	Bank of Russia National Bank of the Republic of Mordovia	5	21	15	28	7	21	2	4	5	17
4.12.	Bank of Russia National Bank of the Republic of Tatarstan	25	98	17	56	17	39	11	1	6	38
4.13.	Bank of Russia National Bank of the Udmurt Republic	11	44	19	40	19	21	7	6	12	15
4.14.	Bank of Russia National Bank of the Chuvash Republic	5	30	8	39	10	29	5	2	5	27

1	2	3	4	5	6	7	8	9	10	11	12
TOTAL		157	717	276	713	247	466	82	61	165	405
5. Ural federal district											
5.1.	Bank of Russia Regional Branch for the Kurgan Region	6	23	8	26	13	13	4	0	9	13
5.2.	Bank of Russia Regional Branch for the Sverdlovsk Region	30	141	43	146	43	103	11	2	32	101
5.3.	Bank of Russia Regional Branch for the Tyumen Region	33	159	32	88	24	64	18	14	6	50
5.4.	Bank of Russia Regional Branch for the Chelyabinsk Region	13	106	15	23	8	15	7	6	1	9
TOTAL		82	429	98	283	88	195	40	22	48	173
6. Siberian federal district											
6.1.	Bank of Russia Regional Branch for the Altai Territory	9	53	15	44	13	31	6	4	7	27
6.2.	Bank of Russia Regional Branch for the Krasnoyarsk Territory	10	76	17	89	13	76	5	9	8	67
6.3.	Bank of Russia Regional Branch for the Irkutsk Region	11	64	20	63	19	44	7	6	12	38
6.4.	Bank of Russia Regional Branch for the Kemerovo Region	12	45	19	52	22	30	7	6	15	24
6.5.	Bank of Russia Regional Branch for the Novosibirsk Region	15	46	19	41	19	22	7	0	12	22
6.6.	Bank of Russia Regional Branch for the Omsk Region	8	39	11	38	19	19	6	1	13	18
6.7.	Bank of Russia Regional Branch for the Tomsk Region	5	30	50	50	12	38	4	6	8	32
6.8.	Bank of Russia Regional Branch for the Chita Region	2	30	10	30	5	25	2	4	3	21
6.9.	Bank of Russia National Bank of the Republic of Buryatia	3	26	11	44	8	36	0	0	8	36
6.10.	Bank of Russia National Bank of the Republic of Altai	5	2	6	13	11	2	5	0	6	2
6.11.	Bank of Russia National Bank of the Republic of Tyva	3	4	8	8	4	4	1	0	3	4
6.12.	Bank of Russia National Bank of the Republic of Khakassia	3	12	7	13	4	9	1	1	3	8
TOTAL		86	427	193	485	149	336	51	37	98	299
7. Far Eastern federal district											
7.1.	Bank of Russia Regional Branch for the Primorskiy Territory	10	40	20	64	23	41	7	11	16	30
7.2.	Bank of Russia Regional Branch for the Khabarovsk Territory	6	27	20	34	9	25	4	3	5	22
7.3.	Bank of Russia Regional Branch for the Amur Region	5	20	14	17	8	9	2	4	6	5
7.4.	Bank of Russia Regional Branch for the Kamchatka Region	8	19	22	23	9	14	6	2	3	12
7.5.	Bank of Russia Regional Branch for the Magadan Region	3	20	24	34	10	24	2	2	8	22
7.6.	Bank of Russia Regional Branch for the Sakhalin Region	6	19	12	26	9	17	3	3	6	14
7.7.	Bank of Russia Regional Branch for the Chukchee Autonomous Area	0	7	3	8	0	8	0	1	0	7
7.8.	Bank of Russia National Bank of the Republic of Sakha (Yakutia)	8	51	17	41	14	27	4	6	10	21
7.9.	Bank of Russia National Bank of the Republic of Jewish Autonomous Region	0	6	30	30	0	30	0	0	0	30
TOTAL		46	209	162	277	82	195	28	32	54	163
8. Bank of Russia Central Office											
				0	7	6	1	0	0	6	1
The Russian Federation, total		1 319	3 432	1 904	4 600	1 953	2 647	565	275	1 388	2 372

Table 3**Key macroeconomic indicators in 2000-2002**

	2000	2001	2002
GDP, billion roubles	7 305,6	9 039,4	10 863,4
Real GDP (as % of previous year)	110,0	105,0	104,3
GDP deflator index, %	140,5	117,8	115,2
Federal budget surplus, % of GDP	1,4	2,9	1,4
Industrial output (as % of previous year)	111,9	104,9	103,7
Agricultural output (as % of previous year)	107,7	107,5	101,7
Retail trade turnover (as % of previous year)	108,8	110,7	109,2
Fixed capital investment (as % of previous year)	117,4	110,0	102,6
Labour productivity (as % of previous year)	105,9	104,7	101,8
Real disposable household income (as % of previous year)	112,0	108,7	109,9
Unemployment rate as % of economically active population (average for period)	10,5	9,0	8,0
Consumer price index (December to December previous), %	120,2	118,6	115,1
Rouble/US dollar market exchange rate (average for period)	28,12	29,18	31,36

Table 4

Quantitative characteristics of Russian credit institutions (numbers)

Indicator	01.01.02	01.04.02	01.07.02	01.10.02	01.01.03
Credit institutions registered by the Bank of Russia and other bodies	2 003	1 982	1 923	1 917	1 828
Operating credit institutions (credit institutions with banking licence)	1 319	1 327	1 328	1 334	1 329
Credit institutions that have been registered by the Bank of Russia but have not yet paid up authorised capital and have not received a licence (within time period set by law)	7	5	13	3	8
Credit institutions whose banking licence has been revoked (cancelled)	677	650	582	580	491
Credit institutions with a licence to conduct operations in foreign currency	810	822	824	835	839
Credit institutions with a general licence	262	270	279	284	293

Table 5

Development of banking services in Russian regions as of January 1, 2003

Region	No. of credit institutions	No. of branches	Assets (net), million roubles	Loans and other placement with non-financial enterprises and organisations, million roubles	Household deposits and other private funds, million roubles	Gross Regional Product for 2002, billion roubles (estimate)	Population as of 01.01.03, thous. (estimate)	Per capita income (monthly average for 2002 Q4), roubles	Institutional saturation with banking services (by population)	Financial saturation with banking services (by assets)	Financial saturation with banking services (by credit volumes)	Savings business development index (per capita deposits to income)	Composite index of region's provision with banking services*
1	2	3	4	5	6	7	8	9	10	11	12	13	14
Central federal district (excluding Moscow and the Moscow Region)	75	434	177 383	74 858	92 957	808	21 311	2 905	0,83	1,00	1,09	1,09	1,00
Belgorod Region	6	27	14 439	9 049	7 756	66	1 499	3 187	0,76	1,00	1,62	1,18	1,10
Braynsk Region	2	32	7 642	2 194	4 271	39	1 395	2 727	0,84	0,89	0,66	0,82	0,80
Vladimir Region	3	32	11 385	7 491	6 932	53	1 558	2 434	0,78	0,98	1,67	1,33	1,14
Voronezh Region	4	35	33 372	12 485	12 602	78	2 393	2 903	0,56	1,96	1,90	1,32	1,29
Ivanovo Region	5	18	6 571	1 628	3 831	27	1 176	1 858	0,68	1,11	0,71	1,28	0,91
Kaluga Region	6	32	8 816	3 247	4 964	39	1 048	2 790	1,25	1,03	0,98	1,24	1,12
Kostroma Region	5	15	4 998	1 079	2 940	27	758	2 616	0,91	0,84	0,47	1,08	0,79
Kursk Region	2	26	7 979	4 070	4 697	48	1 269	2 868	0,76	0,76	1,01	0,94	0,86
Lipetsk Region	2	18	11 011	5 240	5 216	72	1 220	3 375	0,57	0,70	0,86	0,92	0,75
Orel Region	2	21	5 801	2 093	3 215	38	876	2 870	0,91	0,69	0,65	0,93	0,79
Ryazan Region	6	27	9 438	2 845	5 666	48	1 239	2 898	0,92	0,90	0,70	1,15	0,90
Smolensk Region	4	30	8 426	3 181	4 552	45	1 084	3 270	1,08	0,86	0,84	0,94	0,92
Tambov Region	2	25	6 527	2 790	4 118	39	1 224	3 238	0,76	0,77	0,85	0,76	0,78
Tver Region	8	31	8 693	1 952	5 047	58	1 531	2 576	0,88	0,69	0,40	0,93	0,69
Tula Region	7	35	13 278	6 852	8 531	65	1 665	2 927	0,87	0,93	1,24	1,28	1,06
Yaroslavl Region	11	30	19 010	8 661	8 620	70	1 373	3 858	1,03	1,24	1,46	1,19	1,22
North-Western federal district	88	382	299 598	115 166	107 614	915	14 147	4 451	1,15	1,49	1,48	1,25	1,33
Republic of Karelia	1	24	5 413	3 904	3 181	42	752	4 379	1,15	0,58	1,08	0,70	0,84
Komi Republic	6	41	14 696	4 323	8 719	108	1 107	6 259	1,47	0,62	0,47	0,92	0,79
Arkhangelsk Region	5	29	11 214	7 352	6 104	87	1 415	3 970	0,83	0,59	0,99	0,79	0,79
Vologda Region	8	37	17 859	6 417	7 899	102	1 291	3 950	1,21	0,80	0,74	1,13	0,95
Kaliningrad Region	12	30	13 597	4 313	6 156	39	940	3 262	1,54	1,58	1,30	1,46	1,47
Leningrad Region	3	40	10 609	2 949	6 712	88	1 642	2 779	0,91	0,55	0,39	1,07	0,68
Murmansk Region	4	27	14 118	3 862	8 990	87	966	5 979	1,11	0,74	0,52	1,13	0,83
Novgorod Region	2	29	4 552	1 919	2 611	31	703	3 267	1,53	0,67	0,73	0,83	0,88
Pskov Region	5	13	4 240	1 239	2 334	25	767	2 777	0,81	0,76	0,57	0,80	0,73
St. Petersburg	42	112	203 301	78 887	54 908	306	4 565	5 301	1,17	3,02	3,04	1,65	2,05
Southern federal district	142	480	168 147	60 616	82 266	726	20 785	3 083	1,03	1,05	0,98	0,94	1,00
Republic of Adygeya	5	6	2 134	422	1 369	9	444	2 664	0,86	1,12	0,58	0,84	0,83
Republic of Dagestan	39	76	4 586	463	1 312	32	2 200	2 218	1,81	0,66	0,17	0,20	0,45
Republic of Ingushetia	2	6	781	62	202	9	473	1 737	0,59	0,40	0,08	0,18	0,24

1	2	3	4	5	6	7	8	9	10	11	12	13	14
Kabardino-Balkar Republic	7	18	3 081	914	1 560	24	780	3 106	1,11	0,58	0,45	0,47	0,61
Republic of Kalmykia-Khalmg Tangch	3	5	2 644	2 133	314	13	304	2 003	0,91	0,92	1,92	0,37	0,88
Karachai-Circassian Republic	7	5	1 340	490	632	9	426	2 631	0,97	0,71	0,67	0,41	0,66
Republic of North Ossetia	6	19	3 946	1 121	1 897	17	676	2 905	1,28	1,03	0,76	0,70	0,92
Krasnodar Territory	26	102	49 185	19 377	28 574	225	4 970	3 527	0,89	0,99	1,01	1,19	1,02
Stavropol Territory	11	55	24 563	7 797	13 926	87	2 633	2 657	0,87	1,28	1,05	1,45	1,14
Astrakhan Region	4	28	8 257	1 814	4 357	48	1 006	3 524	1,10	0,78	0,44	0,90	0,76
Volgograd Region	6	55	20 717	7 979	11 116	110	2 616	2 966	0,81	0,86	0,85	1,04	0,89
Rostov Region	26	104	46 913	18 043	17 007	143	4 257	3 582	1,06	1,49	1,49	0,81	1,17
Volga federal district	156	682	394 214	162 306	155 150	1 667	31 440	3 392	0,92	1,07	1,15	1,06	1,05
Republic of Bashkortostan	13	52	59 419	17 553	17 111	239	4 080	3 517	0,55	1,13	0,86	0,87	0,83
Republic of Marii El	1	25	2 669	925	1 598	18	745	2 072	1,21	0,68	0,61	0,75	0,79
Republic of Mordovia	5	20	5 039	2 583	2 341	36	900	2 503	0,96	0,64	0,85	0,76	0,79
Republic of Tatarstan	25	99	71 310	28 754	21 098	302	3 761	3 687	1,14	1,07	1,12	1,11	1,11
Udmurt Republic	11	34	14 395	8 042	6 120	83	1 608	2 740	0,97	0,79	1,14	1,01	0,97
Chuvash Republic	5	29	7 048	3 727	3 868	37	1 339	2 412	0,88	0,85	1,17	0,87	0,94
Kirov Region	3	50	8 976	3 332	5 256	57	1 542	2 742	1,19	0,72	0,69	0,91	0,86
Nizhni Novgorod Region	21	88	53 274	22 538	24 729	155	3 562	3 624	1,06	1,56	1,71	1,40	1,41
Orenburg Region	11	40	16 637	5 274	8 244	123	2 186	2 855	0,81	0,62	0,51	0,96	0,70
Penza Region	2	24	9 308	2 598	5 415	41	1 490	2 519	0,60	1,04	0,75	1,05	0,84
Perm Region	11	55	38 399	17 232	16 444	195	2 904	4 502	0,79	0,89	1,04	0,92	0,90
Samara Region	24	73	75 003	34 181	25 483	232	3 242	4 823	1,03	1,47	1,74	1,19	1,33
Saratov Region	18	65	24 078	10 654	12 055	101	2 656	2 811	1,08	1,08	1,24	1,18	1,14
Ulyanovsk Region	6	28	8 662	4 913	5 388	49	1 425	2 592	0,82	0,80	1,18	1,06	0,96
Ural federal district	77	419	241 392	75 244	89 737	1 398	12 469	5 364	1,38	0,78	0,63	0,98	0,90
Kurgan Region	6	23	4 273	1 790	2 159	30	1 062	2 588	0,94	0,66	0,71	0,57	0,71
Sverdlovsk Region	30	143	77 908	34 120	28 851	247	4 511	4 357	1,33	1,43	1,63	1,07	1,35
Tyumen Region	28	159	121 782	24 060	41 969	919	3 291	9 884	1,96	0,60	0,31	0,94	0,76
Chelyabinsk Region	13	94	37 429	15 273	16 758	202	3 605	3 315	1,03	0,84	0,89	1,02	0,94
Siberian federal district	82	417	184 459	77 792	82 805	1 064	20 411	3 774	0,85	0,79	0,86	0,78	0,82
Republic of Altai	5	2	961	392	360	6	205	3 267	1,18	0,73	0,78	0,39	0,72
Republic of Buryatia	2	28	5 360	1 927	2 361	33	1 014	3 619	1,02	0,73	0,68	0,47	0,70
Republic of Tyva	3	4	539	74	314	6	311	2 838	0,78	0,43	0,15	0,26	0,34
Republic of Khakassia	3	11	2 524	274	1 442	26	572	3 354	0,85	0,44	0,12	0,55	0,40
Altai Territory	9	51	16 851	8 102	6 803	72	2 601	2 772	0,80	1,06	1,32	0,69	0,93
Krasnoyarsk Territory	9	76	33 452	9 156	16 084	323	2 997	4 745	0,98	0,47	0,33	0,82	0,60
Irkutsk Region	11	65	24 637	9 824	12 512	159	2 696	3 927	0,97	0,70	0,73	0,86	0,81
Kemerovo Region	11	33	24 068	10 418	12 430	139	2 919	4 595	0,52	0,79	0,88	0,68	0,70
Novosibirsk Region	15	46	38 183	17 712	11 939	114	2 702	3 118	0,78	1,52	1,82	1,03	1,22
Omsk Region	8	43	19 267	11 500	9 657	72	2 109	3 768	0,84	1,21	1,87	0,89	1,14
Tomsk Region	4	28	12 785	7 630	5 960	65	1 057	4 294	1,05	0,89	1,38	0,96	1,05

1	2	3	4	5	6	7	8	9	10	11	12	13	14
Chita Region	2	30	5 831	783	2 942	47	1 227	2 897	0,90	0,57	0,20	0,60	0,50
Far Eastern federal district	46	209	87 425	33 386	41 100	475	6 988	5 047	1,26	0,84	0,83	0,85	0,93
Republic of Sakha (Yakutia)	8	52	12 448	3 894	6 784	122	981	8 002	2,11	0,46	0,38	0,63	0,69
Primorskiy Territory	10	39	20 872	7 963	9 451	99	2 109	3 597	0,80	0,96	0,95	0,91	0,90
Khabarovsk Territory	6	27	22 148	9 938	10 210	102	1 476	5 322	0,77	0,98	1,14	0,95	0,95
Amur Region	5	19	5 814	2 654	2 892	40	975	3 031	0,85	0,66	0,78	0,71	0,75
Kamchatka Region	8	18	7 007	1 926	3 601	27	377	6 652	2,39	1,17	0,83	1,05	1,25
Magadan Region	3	20	7 815	3 131	2 364	19	226	6 782	3,52	1,86	1,93	1,13	1,94
Sakhalin Region	6	21	8 819	3 095	4 295	54	578	6 143	1,61	0,74	0,67	0,88	0,92
Jewish Autonomous Region	0	6	886	298	502	6	194	3 551	1,07	0,71	0,62	0,53	0,71
Chukchee Autonomous Area	0	7	1 617	485	1 001	6	72	10 268	3,35	1,20	0,94	0,98	1,39
Total (excluding Moscow and the Moscow Region)	666	3 023	1 552 619	599 367	651 630	7 053	127 551	3 722	1,00	1,00	1,00	1,00	1,00

*Calculated according to the methodology of the Bank of Russia Department for Banking Regulation and Supervision.

Table 6

Indicators of credit institutions with foreign ownership (% share in banking sector)

	1.07.98	1.01.00	1.01.01	1.01.02	1.07.02	1.01.03
Credit institutions with 50%-plus foreign ownership						
Assets	6,7	10,6	9,5	8,8	8,8	8,1
Equity capital	5,0	10,3	9,4	7,7	7,0	7,1
Correspondent accounts with non-resident banks	6,4	9,9	15,6	20,0	16,6	22,9
Loans and other placement with non-financial companies, including non-resident corporate entities	8,8	9,8	7,1	7,2	7,3	7,1
Loans, deposits and other placement with banks	14,6	31,8	33,0	31,3	32,4	25,9
Household deposits and other funds	0,7	1,8	1,7	2,3	2,3	2,3
Funds of enterprises and organisations*	7,1	14,7	13,8	11,5	13,2	10,3
of which subsidiaries of foreign banks						
Assets	4,7	6,0	5,1	5,2	5,8	5,6
Equity capital	3,4	6,2	6,2	5,2	5,5	5,4
Correspondent accounts with non-resident banks	3,2	4,2	9,0	10,5	13,4	19,2
Loans and other placement with non-financial companies, including non-resident corporate entities	6,9	7,6	5,5	5,2	5,7	5,5
Loans, deposits and other placement with banks	8,4	13,0	13,2	20,4	17,9	16,3
Houshold deposits and other private funds	0,2	0,7	1,0	1,5	1,5	1,5
Funds of enterprises and organisations*	3,3	6,5	5,3	5,1	6,6	5,4

*These include deposits, government extra-budgetary funds, funds of the Ministry of Finance, financial agencies and clients in factoring and forfeiting operations, funds in settlements, and funds transferred from clients' accounts, which have not passed through a credit institution's correspondent account.

Table 7

Structure of banking sector liabilities, by sources of funds (billion roubles)

	Liabilities	1.01.02	1.04.02	1.07.02	1.10.02	1.01.03
1.	Banks' own funds and profits, total	510,3	558,9	563,4	607,3	652,5
	of which					
1.1.	Banks' own funds	517,4	540,6	567,2	592,9	625,0
1.2.	Profit (loss), including financial results of previous years	-7,1	18,3	-3,8	14,4	27,4
	of which					
1.2.1.	Reporting year's profit (loss)	67,6	29,2	57,8	80,8	93,0
2.	Loans, deposits and other funds from the Bank of Russia	46,6	26,6	25,5	19,1	6,2
3.	Other banks' accounts, total	164,7	157,4	175,4	184,6	176,5
	of which					
3.1.	Correspondent accounts of credit institutions	84,3	83,1	87,9	95,8	111,0
3.2.	Correspondent accounts of non-resident banks	79,5	72,9	85,5	87,1	63,7
4.	Loans, deposits and other funds from other banks, total	203,1	247,9	239,8	260,4	315,4
	of which					
4.1.	Overdue debt	30,7	31,9	22,7	21,5	17,6
5.	Customers' funds, total	1 647,7	1 726,3	1 890,8	1 993,4	2 194,5
	of which					
5.1.	Budget funds in settlement and current accounts	45,0	58,1	74,8	76,9	42,3
5.2.	Government extra-budgetary funds in settlement and current accounts	22,0	22,8	24,4	25,0	27,0
5.3.	Corporate funds in settlement, current and other accounts	582,7	554,6	594,5	615,3	735,0
5.4.	Customer funds in settlements	14,8	36,0	42,8	43,0	11,8
5.5.	Corporate deposits	252,4	238,1	242,2	244,2	276,7
5.6.	Individual accounts	700,1	782,7	871,2	948,1	1 060,7
	of which					
5.6.1.	Household deposits and other private funds	677,9	757,3	843,1	921,1	1 029,6
5.7.	Other borrowed funds	29,6	32,8	39,9	39,4	39,7
5.8.	Customers' funds in factoring and forfeiting operations	0,0	0,1	0,1	0,1	0,2
5.9.	Funds transferred from customers' accounts, which have not passed through a credit institution's correspondent account	1,1	1,0	1,0	1,4	0,9
6.	Debt instruments issued by banks, total	272,5	285,6	328,1	363,1	450,6
	of which					
6.1.	Bonds	4,0	6,3	5,2	5,8	7,4
6.2.	Certificates of deposit	27,0	25,4	33,8	44,6	66,6
6.3.	Savings certificates	0,5	0,6	0,8	1,1	1,1
6.4.	Bills of exchange and bank acceptances	238,9	249,8	283,5	307,1	372,4
7.	Other liabilities, total	314,8	330,5	360,9	371,3	349,6
	of which					
7.1.	Reserves	135,2	153,0	163,8	172,2	168,3
7.2.	Funds in settlements	106,7	98,9	115,4	118,4	110,8
7.3.	Creditors	9,3	11,1	12,6	8,9	8,1
7.4.	Fixed and intangible asset depreciation	20,5	22,2	23,9	25,4	27,2
7.5.	Deferred income	32,0	33,7	32,8	34,3	27,3
Total liabilities		3 159,7	3 333,2	3 583,9	3 799,2	4 145,3

Table 8

Structure of banking sector assets, by form of investment (billion roubles)

	Assets	1.01.02	1.04.02	1.07.02	1.10.02	1.01.03
1.	Cash, precious metals and gemstones, total	70,3	64,5	70,2	78,5	91,2
1.1.	of which Cash	66,9	62,1	66,8	73,2	88,1
2.	Accounts with the Bank of Russia, total	303,9	275,0	334,3	350,0	416,8
2.1.	of which Credit institutions' correspondent accounts with the Bank of Russia	140,6	83,2	94,6	99,2	164,5
2.2.	Credit institutions' mandatory reserves held with the Bank of Russia	156,3	164,1	176,9	186,8	200,7
2.3.	Deposits with the Bank of Russia	3,7	24,1	59,5	58,4	47,4
3.	Correspondent accounts with credit institutions, total	315,3	289,3	266,6	258,6	300,9
3.1.	of which Correspondent accounts with credit institutions	83,3	82,3	81,3	86,9	106,7
3.2.	Correspondent accounts with non-resident banks	232,0	207,0	185,3	171,7	194,2
4.	Securities acquired by banks, total*	562,0	611,5	681,1	680,9	779,9
4.1.	of which Debt instruments	366,7	383,9	429,6	429,7	502,6
4.1.1.	of which Debt obligations of the Russian Federation	338,4	348,6	379,8	376,0	412,8
4.2.	Shares	47,9	50,8	62,9	63,9	68,7
4.2.1.	of which Controlling shareholdings	15,2	16,0	16,7	17,0	17,4
4.3.	Bills discounted	147,3	176,9	188,5	187,3	208,5
5.	Other participation in authorised capital	2,7	2,7	2,4	3,3	4,7
6.	Loan debt, total	1 561,7	1 711,2	1 849,4	2 017,3	2 148,8
6.1.	of which Loans, deposits and other placement including overdue debt	1 558,2 40,4	1 708,4 43,5	1 846,7 48,1	2 014,6 48,9	2 146,2 40,5
6.1.1.	of which Loans and other placement with non-financial enterprises and organisations including overdue debt	1 229,0 28,0	1 285,8 30,7	1 391,5 35,3	1 523,6 35,9	1 654,0 29,0
6.1.2.	Loans, deposits and other placement with banks including overdue debt	196,9 9,5	283,6 9,6	289,9 9,7	302,3 9,8	291,4 9,0
6.2.	Financing of government programmes and capital investment on a returnable basis	3,5	2,8	2,7	2,7	2,7
7.	Fixed assets, intangible assets and inventories	128,9	133,8	139,0	144,8	157,2
8.	Disposition of profit	41,9	54,6	30,6	43,7	55,1
9.	Other assets, total	172,8	190,5	210,4	222,2	190,7
9.1.	of which Funds in settlements	99,0	104,4	116,2	121,8	100,8
9.2.	Debtors	17,6	21,5	24,0	24,3	21,7
9.3.	Overdue interest on loans	7,4	8,6	9,0	10,9	3,4
9.4.	Deferred expenses	37,0	42,0	47,8	51,7	51,5
Total assets		3 159,7	3 333,2	3 583,9	3 799,2	4 145,3

* Including controlling shareholdings.

Table 9

Main characteristics of banking sector lending activities (billion roubles)

	Roubles					Foreign currency					Total				
	1.01.02	1.04.02	1.07.02	1.10.02	1.01.03	1.01.02	1.04.02	1.07.02	1.10.02	1.01.03	1.01.02	1.04.02	1.07.02	1.10.02	1.01.03
1. Loans, deposits and other placement, total	994,8	1 039,1	1 122,6	1 237,3	1 319,7	563,4	669,3	724,0	777,2	826,5	1 558,2	1 708,4	1 846,7	2 014,6	2 146,2
of which:															
- overdue debt	18,3	22,6	24,9	26,1	24,9	22,1	20,9	23,2	22,8	15,6	40,4	43,5	48,1	48,9	40,5
1.1 Loans and other placement with resident non-financial enterprises and organisations	810,1	826,2	889,6	974,0	1 044,2	366,7	406,7	449,7	490,2	547,2	1 176,8	1 233,0	1 339,3	1 464,1	1 591,4
of which:															
- overdue debt	12,8	17,1	17,9	18,8	18,0	14,7	13,0	16,4	15,8	10,5	27,5	30,1	34,2	34,7	28,4
1.2 Loans and other placement with non-resident corporate entities, except banks	3,9	3,4	4,0	3,6	3,4	48,2	49,5	48,2	55,9	59,2	52,2	52,9	52,2	59,5	62,6
of which:															
- overdue debt	0,15	0,19	0,19	0,24	0,24	0,36	0,42	0,85	1,00	0,33	0,51	0,61	1,04	1,25	0,58
1.3 Loans, deposits and other placement with the financial sector	66,2	85,8	83,3	98,3	103,5	28,1	36,7	36,3	33,7	45,0	94,3	122,5	119,6	131,9	148,4
of which															
- overdue debt	3,4	3,4	5,2	5,3	5,2	2,0	2,2	0,6	0,5	0,4	5,5	5,7	5,7	5,8	5,6
of which:															
1.3.1 Loans, deposits and other placement with resident organisations	50,6	73,3	69,4	81,6	85,1	23,7	31,9	30,8	26,3	34,7	74,3	105,2	100,1	108,0	119,9
of which															
- overdue debt	3,4	3,4	5,1	5,3	5,2	2,0	2,2	0,5	0,4	0,3	5,4	5,6	5,6	5,7	5,6
1.3.2. Loans, deposits and other placement with resident financial organisations of different forms of ownership	15,6	12,5	14,0	16,6	18,3	4,4	4,8	5,5	7,3	10,2	20,0	17,3	19,5	23,9	28,6
of which:															
- overdue debt	0,01	0,01	0,01	0,00	0,01	0,03	0,03	0,05	0,05	0,05	0,04	0,04	0,06	0,05	0,06
1.4 Loans, deposits and other placement with non-resident banks	19,6	19,6	19,9	20,3	25,0	103,0	158,8	169,8	174,1	146,6	122,6	178,4	189,7	194,4	171,5
of which:															
- overdue debt	0,01	0,01	0,01	0,01	0,01	4,07	3,96	4,03	4,10	3,45	4,07	3,97	4,03	4,10	3,46
1.5 Loans and other claims on government financial bodies and extra-budgetary funds	16,5	20,3	23,3	25,7	27,8	1,2	0,7	0,6	0,5	2,1	17,6	21,0	23,9	26,2	29,9
of which:															
- overdue debt	1,01	0,81	0,52	0,47	0,28	0,02	0,23	0,23	0,23	0,02	1,03	1,03	0,75	0,70	0,30
1.6 Loans to resident individuals	77,9	83,5	102,3	115,3	115,8	15,4	16,0	18,5	21,8	25,3	93,3	99,5	120,7	137,1	141,2
of which:															
- overdue debt	0,9	1,1	1,2	1,2	1,2	0,7	0,8	0,9	1,0	0,7	1,6	1,9	2,1	2,2	1,9
1.7. Loans to non-resident individuals	0,5	0,2	0,2	0,2	0,1	0,8	0,9	0,9	1,1	0,9	1,4	1,2	1,2	1,3	1,0
of which:															
- overdue debt	0,00	0,00	0,00	0,00	0,00	0,20	0,21	0,23	0,22	0,21	0,20	0,21	0,23	0,22	0,21
For the record:															
Overdue interest on loans, deposits and other placement with residents	2,1	2,5	2,5	2,9	1,8	5,2	6,0	6,3	7,8	1,6	7,3	8,5	8,8	10,7	3,4
Overdue interest on loans, deposits and other placement with non-residents	0,00	0,00	0,00	0,00	0,00	0,08	0,11	0,12	0,14	0,01	0,09	0,11	0,12	0,14	0,01
Bank investments in residents' bills	129,0	155,5	164,2	161,7	187,9	1,5	4,2	5,1	8,3	9,8	130,5	159,7	169,3	170,0	197,6
Bank investments in non-residents' bills	0,8	0,7	1,1	0,5	1,4	16,1	16,5	18,0	16,8	9,5	16,9	17,2	19,2	17,3	10,9

Table 10

Return on capital in key branches of the Russian economy in 2002

Sector	Return on capital*, %
Electric-power industry	1,2
Fuel sector	16,0
Trade and public catering	8,5
Communications	30,0
Transport	3,9
Ferrous metallurgy	18,6
Non-ferrous metallurgy	14,1
Food industry	21,1
Woodworking and pulp-and-paper industry	12,3
Building materials industry	13,0
Construction	9,6
Machine-building and metalworking	9,9
Chemical and petrochemical industry	5,6
Light industry	-3,3
Economy as a whole	7,9
Banking sector**	16,0

Source: data on branches have been compiled by Goskomstat and on the banking sector by the Bank of Russia.

* The return on capital is calculated as the net financial result to capital and reserves. Capital and reserves comprise authorised capital, additional capital, reserve capital, social security fund, targeted allocations and receipts, retained profit and uncovered loss of the previous years and reporting period.

** Calculated by the Bank of Russia according to Goskomstat methodology. The return on capital is calculated as the ratio of banking sector profit to equity capital as of the end of 2002.

Table 11

Credit institutions, by deficit of liquidity coverage*

Indicator	No. of credit institutions					% share in aggregate banking sector assets				
	1.01.02	1.04.01	1.07.02	1.10.02	1.01.03	1.01.02	1.04.01	1.07.02	1.10.02	1.01.03
Less than 0%	650	643	595	613	659	24,2	22,9	19,2	21,9	24,0
From 0% to 20%	422	427	414	409	422	22,7	24,8	22,7	25,0	22,0
More than 20%	243	252	314	308	244	53,2	52,4	58,0	53,2	54,1
Data unavailable	4	5	5	4	4	0,0	0,0	0,0	0,0	0,0
TOTAL	1 319	1 327	1 328	1 334	1 329	100,0	100,0	100,0	100,0	100,0

Calculated as prescribed by Form No.125 "Information on Assets and Liabilities by Call Date and Term of Payment" (Annex No. 17 to Bank of Russia Instruction No. 17, dated October 1, 1997, "On Compiling Financial Statements")

*The deficit of liquidity coverage is the ratio of the excess of demand liabilities and liabilities with maturity up to 30 days over assets with the same terms to the total value of the above mentioned liabilities.