

**Russian-European Centre for Economic Policy**

**POLICY PAPER SERIES**

**«A NEW INVESTMENT POLICY IN THE  
KALININGRAD REGION»**

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The key issue of economic development is investments. The share of the region in aggregate investment into the Russian economy constituted only 0.36 % in 1999 (but its share in the RF population is 0.65 %). In spite of attempts to attract funds by setting up free economic and special economic zones in the region, the inflow of foreign investment is insignificant. Accumulated direct foreign investment at the beginning of 1999 amounted to only 46 million US dollars, and in 1999 an outflow of investment took place. The share of foreign investment in the total amount of investment in the 1990s constituted less than 10 %.

Investment per capita into fixed assets in the first quarter of 2000 is 636 roubles in Kaliningrad against 1120 roubles on average in the RF (and for the region this figure is half this amount). Foreign investment per capita amounts to 3.6 US dollars against 19 US dollars in Russia (about five times less). The total amount of foreign investment was only 3.4 million USD.

The new investment strategy suggested would ensure a favourable climate for private investment both Russian and foreign, firstly by the formation of a developed market economy in the region. Secondly, the Investment and Finance Corporation would support this process. Third, a more consistent realisation of the federal programme for the development of the special economic zone would be guaranteed through substantial financial support from the federal budget. Forth, an agreement between the RF and the EU would bring additional support from international programmes and would serve as a guarantee for foreign investors who invest into the Kaliningrad region.

The management of the federal programme for the development of the special economic zone would have the following functions:

- elaboration, monitoring, correction and execution of the federal programme for the development of the special economic zone, co-ordination of its provisions with other federal programmes;
- organisation of an IFC and participation in the management of its activities;
- co-operation with the regional administration in solving questions of regional development;
- substantiation, organisation and management of local free economic zones of federal significance (enjoying special status).

The federal programme on the development of the special economic zone should contain mainly infrastructural projects which cannot be financed by private business and social projects concerned with the development of non-commercial services.

That is why the existing programme for the period 1998 – 2005 (which is formally valid, but poorly financed due to various objective and subjective reasons), which does not meet this criterion, should be thoroughly revised. The necessity of revision is also due to the changed conditions of regional development, to the new federal policy and to the planned creation of an IFC, which would fulfil a number of functions previously resting with the federal programme.

At the same time a number of programmes are needed which would facilitate the development of a market economy, regulate issues of the economic security of the region or execute tasks strategically important for development of the Russian economy. In particular this would be the development of export-oriented or import-substituting productions, the support of local producers, the creation of the international trade-industrial complex “Europort Kaliningrad” and a system of local free economic zones, the development of the energy

and transport sectors, of the tourism and amber industries, the development of the fish resources of the Baltic Sea, the support of agriculture, etc.

With a view to activating the formation of a functioning market economy, the creation of an Investment and Finance Corporation (IFC) and of a number of relating elements, such as a Guarantee Fund and an Information and Consultation Centre is proposed.

The aim of creating an IFC is to guarantee conditions essential for the stable functioning of the financial market in the Kaliningrad region and above all, of the capital market. There are three main reasons for the non-existence of such a market:

1. insufficient information on the investment potential of the region, i.e. on the existence of lucrative investment projects;
2. the high level of investment risk of the region's economy;
3. the insufficient infrastructure the financial market.

The ICF's activity would allow:

first, to quickly find of projects worthy of investors' attention;

second, to reduce the risk of these projects by thorough prior examination, by increasing the financial transparency of the enterprises realising these projects, and by strictly monitoring the investment process;

third, the IFC will become the basis for the further development of the financial infrastructure, for the creation of powerful investment companies and of sources of information for the market (telecommunications, press, rating agency, reliable channels of profit transfer to investors etc.)

The ICF's tasks are to find attractive investment projects, the support enterprises draw up business plans for their investment projects and to reduce their risk, to finance these projects, to monitor their implementation and to guarantee profit transfer to investors.

These objectives and the ICF's philosophy determine the main functions that the ICF is to have:

- Examining the investment potential of the region and investment marketing;
- Examining and selecting the most attractive offers;
- Improving the financial management of corporate finance in the firms chosen;
- assisting enterprises in drawing up business plans for the investment projects;
- evaluating investment projects;
- finding funding for the projects;
- checking consequences concerning emissions;
- insuring risks of the projects;
- financing companies which carry out investment projects;
- monitoring project implementation and ensuring profit transfer.

It is assumed that the IFC - through fulfilling its functions - will turn into an effective financial and economic mechanism, which contributes to the realisation of the overall strategy of development of the Kaliningrad region as a pilot region of co-operation between Russia and the EU. At the same time, the IFC will be effectively protected from any attempts

by political leaders at interfering with its activities. It will become a powerful element of Kaliningrad's market structures, which will yield a profit, pay taxes and support the development of the financial markets in the Kaliningrad region and in Russia.

Setting up an IFC is useful even if no agreement between the RF and the EU is signed on the Kaliningrad region as a “pilot region” of co-operation. However, EU participation in the project would earn it authority in the West and would allow help to attract considerable private investment, in particular major investment banks, which Russia currently lacks.

Besides, the IFC would become a founder of the Guarantee Fund and the Information and Consultation Centre. In these circumstances, active participation of local enterprises in the IFC may be expected. These enterprises and their professional associations and consortia can also become founders of the IFC.

The pilot projects elaborated and realised with the active participation of the IFC also belong under this heading. We assume that among them there would be projects related to the telecommunications industry and the informatisation of the Kaliningrad region.

On the one hand it is impossible to imagine working in an open financial market without modern means of communication and high-powered computers. On the other hand, the availability of inexpensive, fast and reliable channels of communication would give an competitive advantage to the Kaliningrad enterprises active in the fields of “electronic” business, e-commerce, etc. It is quite likely that the near future will bring new options for attracting investment into the region.

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