Economies

On the move

TUESDAY, DECEMBER 17, 2002

SAKHALIN

SITUATED off the Russian Far East mainland in the Okhotsk Sea, north of Japan, lies Sakhalin, one of Russia's most promising locations for oil and gas development.

The 580-mile long island has flourishing fisheries and useful resources of timber and coal. However, it is the Sakhalin shelf to the northeast, in the waters known as the "ice kitchen", that interests the giant Western multinationals such as ExxonMobil and Royal Dutch/Shell. They are pouring millions of dollars into two of the biggest integrated oil and gas projects ever undertaken—known as Sakhalin-1 and Sakhalin-2.

Severe winter conditions have to be overcome—the sea freezes over for six to seven months each year—and there are ambitious plans to build pipelines, a huge liquefied natural gas (LNG) plant and export facilities.

Once the infrastructure is in place, however, the rewards could be huge. The energy-hungry economies of nearby Japan, China and South Korea are the primary target. And with the United States seeking to diversify its sources of energy, plus talk of a US/Russian energy alliance, the west coast of America is another potential market.

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MACEDONIA

OCCUPYING a strategic position on the Balkan peninsula, Macedonia is a small country that is naturally oriented toward the wider world. Integration with NATO and the European Union is seen as the key to its future.

Membership of the World Trade Organization and a series of free trade agreements with other countries in the region are important steps toward extending beyond the limited scope of its domestic economy. Progress made in building democratic structures in the 1990s has led to the country becoming the first of the western Balkan nations to be offered a definite prospect of accession to the EU through the signing of a Stabilization and Association Agreement.

With good transport and telecommunication links, both within Macedonia and with the rest of the world, a developed and efficient financial system, well educated work force and tax incentives, the country offers promising prospects for participation by foreign companies.

Notable sectors open for investment include tourism, food and beverages, textiles, tobacco, steel, chemicals and pharmaceuticals, infrastructure, telecommunications, energy and banking.

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Summit Communications partners with FDI Xchange

Summit Communications is proud to announce its partnership with the Multilateral Investment Guarantee Agency (MIGA) of the World Bank Group, in the FDI Xchange (www.fdixchange.com) initiative.

FDI Xchange is a web- and e-mail-based service that provides investors, advisors and financial institutions with customized investment information in a single, free package. FDI Xchange users can access a web-based archive of information on emerging economies, as well as receive periodic e-mail updates tailored to match the user's country, sector and topic interests. Through its partnership with FDI Xchange, Summit Communications will contribute to the goal of disseminating information on new investment incentives, industry sector analysis and market research on developing countries.

The FDI Xchange initiative was launched in April 2002, as part of the Agency's mandate to promote foreign direct investment in developing countries and economies in transition. MIGA also operates the Investment Promotion Network (www.ipanet.net), a portal website for the international investment community, and PrivatizationLink (www.privatizationlink.com) which provides information on upcoming privatization sales in developing countries, along with related legal and procedural information.

KRASNODAR

KRASNODAR Krai, the southernmost of Russia's 89 regions, is a place of extraordinary natural beauty, with a landscape that ranges from forests, wheat fields and sunny beaches to the snow-capped Caucasian mountains.

It is also an area of great economic importance to Russia and one of the country's most densely populated regions, with more than five million people and a well-developed consumer market. Krasnodar's agro-industrial complex is Russia's biggest producer and supplier of agricultural products and raw materials.

The region is a major crossroads along transportation routes linking Russia and Central Asia to the Mediterranean Sea and the Middle East. It is also one of Russia's most popular health resort and tourist areas.

Krasnodar's natural resources include marble, limestone, sandstone, gravel, ferrous ores and mineral waters, and it is one of the oldest petroleum extracting areas in the country.

It hosts two major energy projects. Investment totalling some $2 billion is being spent on the Krasnodar section of the Caspian pipeline, which will transport crude oil from Tengiz in Kazakhstan to a terminal at Novorossiysk. The other big project is the construction of the Russia-Turkey gas pipeline at the bottom of the Black Sea, running across 230 miles of Krasnodar's territory.

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Mega-projects will put island in the spotlight

ENERGY BOOST ALMOST UNKNOWN IN THE WEST, RUSSIA'S BIGGEST ISLAND WILL BE PUT ON THE MAP BY MAJOR PROJECTS TO EXPLOIT THE OIL AND GAS THAT LIES OFFSHORE. THE AUTHORITIES ARE DETERMINED TO ENSURE THE POPULATION RECEIVES MAXIMUM BENEFIT

THE REMOTE Russian island of Sakhalin is about to undergo a transformation. Development of offshore oil and gas is bringing jobs to the island and driving plans by the authorities and the oil companies for an improved transportation infrastructure, and construction of new offices and housing to accommodate workers.

Already among the leading Russian destinations for foreign direct investment (FDI), Sakhalin is forecast to receive some $45 billion over the next 40 years, with more than 70 percent coming from the United States.

"Most of the investment is directed into the oil and gas sector," says Igor Farkhutdinov, the governor of the Sakhalin Region. "This year, FDI here will be twice that of last year, and we shall return to ranking second after Moscow in the all-Russia rating."

The island's authorities have done their best to attract foreign interest. "We had to create additional legislative tools to make it happen," says Mr. Farkhutdinov, "so the investors are sure they won't fail. Secondly, we offer projects attractive for investment. The third condition is a positive attitude toward investment on behalf of the authorities and the people, and we have both."

Revenues from the oil and gas projects already account for a third of total collected taxes on the island. "The indicators will grow with every year," adds the governor.

TREASURE ISLAND Sakhalin is among the top-ranking destinations for foreign investment

The Sakhalin Regional Administration has pioneered the Production Sharing Agreements (PSAs) that set the legal framework for cooperation between the island, the international oil giants and the Russian state.

"We are the party with the greatest interest," says Mr. Farkhutdinov. "Since the major operations are located on our territory, we are extremely interested, not only in the economic indicators but in the socio-political results and in ecological safety as well."

Development of Sakhalin's infrastructure is a key issue for the administration in its discussions with the oil companies. Mr. Farkhutdinov recently announced that $100 million will be invested in roads, bridges and airports by the Sakhalin Energy Investment Company, the operator for Sakhalin-2.

The administration's Department of Oil and Gas is at the heart of the Sakhalin-1 and Sakhalin-2 projects, working on all aspects and overseeing the execution of rights and responsibilities under the PSAs.

Galina Pavlova, its director, says, "We try to reach a consensus with the investors. We prioritize the Sakhalin infrastructure as it is important for the population."

The department keeps a database of all the companies available to work as subcontractors and pushes to ensure the companies keep to their commitment to 70 percent Russian content in the projects.

Ensuring a balance between production of hydrocarbons and conservation of valuable marine biological resources is a prime concern. "State authorities, production companies and public organizations have to cooperate in this work," says Mr. Farkhutdinov.

Fisheries are a major provider of employment on Sakhalin, as well as an important source of revenue and food for the island. Sakhalin sells high quality fish and seafood both on the internal Russian market and for export. Around 25 percent of the catch is exported, to Europe, Japan and Korea.

Until about seven years ago, Sakhalin fishermen were operating only around the Kuril Islands, which also make up the Sakhalin region, and the number of fish-processing facilities was limited. Since then many facilities have been built on the island of Sakhalin and the Kurils, and a large share of the fish and seafood catch is now processed. Sakhalin also has many fish hatchery plants, taking 600 million fish eggs for incubation annually.

> The Russian Far East is forecast to experience rapid growth in investment

In addition to oil, Sakhalin possesses large resources of coal—for which it has found a market in Japan—and timber. However, it needs to construct deep ports to accommodate larger vessels in order to fully expand its trade with neighboring countries. "This is why infrastructure development, especially of ports, has become a priority," says prime vice-governor Ivan Malakhov.

Insufficient infrastructural links with the rest of Russia have up to now limited the mainland's interest in Sakhalin as a supplier of goods, while high transportation costs on the mainland itself have encouraged Sakhalin to look to the foreign markets within its reach.

Cars and equipment are among the export deliveries currently made to 24 countries, including Japan, Korea, China, and the United States. Mr. Malakhov says, "It is easier for us to trade with Japan, Korea and China than with our own country because of the high railway tariffs on the mainland."

Governor Farkhutdinov says Sakhalin needs to become integrated into the Asia-Pacific region. "There is no regional growth without it. Sakhalin should be perceived as the territory of Russia closest to the United States and aiming at an active integration with the U.S. economy in supplying and processing hydrocarbons, fish and seafood," he argues.

Investment is expected to grow faster in the Russian Far East during the next three years than in Russia's other regions, according to the Russian Ministry of Economic Development and Trade. Konstantin Pulikovsky, presidential representative for the Far Eastern Federal District, within which Sakhalin falls, foresees increasing cooperation with U.S. companies in the Far East region as a whole.

He emphasizes its investment attractiveness and highlights three sectors in particular: energy, transport and information services. "We are making every effort to attract investors into the area," he says.

IGOR FARKHUTDINOV
Governor of the Sakhalin Region

GALINA PAVLOVA
Director of the Department of Oil and Gas

KONSTANTIN PULIKOVSKY
Presidential representative of the Far Eastern Federal District

Beer is best investment

THE BEST investment in Russia is not oil but beer, according to the country's largest foreign investor, the European Bank for Reconstruction and Development (EBRD).

Producing 10 million liters of beer per year, the JSC Kolos factory, based in Yuzhno-Sakhalinsk, is the leader in the regional market and recognized for the high quality of its products.

Last year the company bought new equipment to boost output by 30 percent. A new production line for glass-bottled beer is expected to raise total output by 70 percent by 2004.

Kolos was created in 1946 and privatized in 1993, when it became a joint stock company. Now 100 percent employee-owned, it produces 12 different brands of beer—draft, canned and in plastic bottles. It also bottles spring water and other beverages. The malt, barley, kegs, keg taps, shapes and caps for plastic bottles are imported.

Expansion into the Russian mainland is not envisaged due to high transportation costs, but local demand is limited. "The Sakhalin market capacity is 600,000 people, of whom only 200,000 to 250,000 drink beer," says general director Pavel Chusov.

Instead, Kolos is focusing on producing the best beer in the region and selling it abroad. It ships more than 5,000 cans of beer a year to Japan and is aiming to double that figure.

Part of the appeal of its beer to the Japanese is the low level of preservatives it contains. Kolos is considering penetrating other foreign markets and hopes to get a license for the production of international brands, including Bavarian beer.

"Foreign markets are our preference," says Mr. Chusov. "We have been working with our Japanese partner for two years now and we are increasing shipments every month."

Kolos is seeking a U.S. business partner to further build up capacity and to enhance quality through modern technology.

PAVEL CHUSOV
General director of JSC Kolos

Exploiting a 'world-class' energy resource

MARKET FORCE WITH OIL AND GAS RESERVES THAT COULD RIVAL THOSE OF THE NORTH SEA, SAKHALIN MAY BECOME AN IMPORTANT PRODUCER FOR WORLD MARKETS AS WELL AS PROVIDE FOR THE NEEDS OF NEIGHBORING ASIAN COUNTRIES

BOTH ExxonMobil and Royal Dutch/Shell, the two energy giants leading the Sakhalin-1 and Sakhalin-2 oil and gas projects, regard the island's offshore shelf as potentially a "world-class" resource.

Larry Smith, vice president of the ExxonMobil affiliate Exxon Neftgas, which is the operator for Sakhalin-1, envisages it making a significant contribution to the development of US/Russian economic partnership. "The Sakhalin-1 project is supported by both the Russian and U.S. governments, and during the recent visit of President Bush to Russia was praised as a success in US-Russian economic cooperation," he says. "It highlights the commitment that the United States and Russia have to making this type of venture a success."

SHIPSHAPE FEMCO specializes in providing services to offshore rigs

ExxonMobil holds a 30 percent stake in the Sakhalin-1 consortium. The other shareholders are the Japanese consortium SODECO (30 percent), India's ONGC Videsh (20 percent), Russia's SMNG Shelf (11.5 percent) and Rosneft-Astra (8.5 percent). Potential recoverable resources of the project are put at 2.3 billion barrels of oil and 17.3 trillion cubic feet of gas.

Sakhalin-1 comprises three offshore fields: Chayvo, Odoptu and Arkutun-Dagi, located on the northeast shelf of Sakhalin island. Oil production is expected to commence at Chayvo in late 2005, followed by Odoptu in 2007.

The oil will be exported via a 140-mile pipeline that will cross the island from Chayvo's onshore facility, and pass over the Tatar Strait to a marine tanker terminal at DeKastri on the Russian mainland. "This will offer year round tanker transportation opportunities, which opens up world markets and also offers the opportunity to use Russian infrastructure such as pipelines and refineries," says Mr. Smith.

Phase II of Sakhalin-1 envisages construction of an undersea natural gas pipeline link to Japan—initially connecting into the Hokkaido market in northern Japan and possibly with a pipeline spur into Yuzhno-Sakhalinsk, Sakhalin's largest population center. Gas sales to Japan are expected to commence in 2008. Phase 3 will see production at Arkutun-Dagi and Phase 4 will enable gas production to continue to beyond 2050.

Meanwhile, Phase I of Sakhalin-2 is already in operation. The Vityaz Production Complex, centered on the Molikpaq oil platform positioned nine miles offshore of northeast Sakhalin, began producing oil in July 1999—the first offshore oil production in Russia.

Phase II of the Sakhalin-2 project is an integrated oil and gas development involving installation of two new offshore platforms: an additional platform at the Piltun sector of the Piltun Astoskhskoye field and a large platform at the Lunskoye gas field.

Coupled with the new platforms will be an onshore processing facility to separate and treat the gas from the two fields, and 500-miles of pipelines to transport the oil and gas to the southern end of the island, where it is planned to build a liquefied natural gas (LNG) plant and oil and LNG export terminals. The location has been chosen because it remains largely ice-free during the winter, allowing for year-round export operations.

The LNG plant will be Russia's first, and will have an annual capacity of 9.6 million tons. The plant will have two trains with an annual capacity of 4.8 million tons, which will make it the largest ever built.

The operating company for the Sakhalin-2 project is Sakhalin Energy Investment Company (Sakhalin Energy), comprising Shell, the biggest shareholder with 55 percent, and Japan's Mitsui (25 percent) and Mitsubishi (20 percent). Shell describes it as the largest grassroots project it has undertaken as a major operator over the last 30 years.

Mitsui and Mitsubishi are expected to deliver the Japanese market for LNG. "We look on this project as being anchored by Japanese LNG demand," says Steve McVeigh, Sakhalin Energy's chief executive officer.

"We believe that Japan, the world's largest LNG consumer, will experience additional energy demand growth through further economic recovery shortly. Korea is already growing very rapidly and increased demand for LNG is certain. China is another growth area and Taiwan continues to do well.

"In short, we are on the doorstep of the biggest LNG market in the world and our proximity and lower shipping costs allow us to be more market price competitive."

The west coast of North America is seen as a potential future market for LNG in light of the willingness of the United States to diversify its hydrocarbons sources. "Shipping gas to the west coast would take around 10 days—significantly less than it would take for our potential competitors," Mr. McVeigh points out.

STEVE MCVEIGH
Chief executive officer of Sakhalin Energy

Russian companies have benefited to the tune of hundreds of millions of dollars from the foreign investment in the Sakhalin-1 and Sakhalin-2 projects. Most of those companies have been Russian Far Eastern enterprises, carrying out some 2,000 associated contracts, in the course of which around 3,000 jobs have been created or conserved.

Among the firms contributing is the Far East Marine Company (FEMCO), the leading company

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servicing marine drilling installations and providing sea towing in the Russian Far East.

"Our company is expanding and in the process of development, but we continue to keep up the best traditions of our predecessors using the newest technologies," says FEMCO's director general, Andrey Aprelenko.

FEMCO is a subsidiary of SMNG. It provides a range of services in support of the development of the Sakhalin oil and gas projects, and has been granted an ISO 9002 certificate of quality by the Russian Registry of Shipping. It has aslo been classified by Det Norske Veritas, an independent marine safety foundation.

The company owns a modern fleet of 20 vessels for servicing offshore installations, deep-sea towing, fire fighting and ice-breaking rescue operations. Initially a drilling company, FEMCO plans at some stage to re-enter the drilling market and it has been working for more than a year on drilling rigs in the Persian Gulf. It operates four marine offshore drilling units, which can be used for exploration as well as for oil and gas drilling.

ANDREY APRELENKO
Director general of FEMCO

"Working with clients such as Exxon and Rosneft-Sakhalinmorneftgas demands the highest degree of professionalism," says Mr. Aprelenko. "We run our operations to comply with the highest safety and quality standards. Not many companies are capable of servicing offshore drilling rigs in ice conditions as we do," he adds. "We believe we are the uncontested leader in this area of Russia."

While its main focus remains on the Sakhalin projects, the company is also turning its attention to other areas of business. This includes extending its traditional fleet activities as well as mastering new opportunities.

"Femco is prepared to cooperate in any activity on Sakhalin—cargo delivery, cargo handling, supply base foundation, warehousing, acting as a ship agent, etc," says Mr. Aprelenko.

Leasing company targets foreign firms

THE leasing market in Russia has seen rapid development in recent years, but it began from a very low level. When Sakhalin Leasing Company (SALCO) was established in 1996, there was little understanding of the services it offered. "This type of business was absolutely new for Russia at the time," says Alexey Malashich, the company's general director.

Since then, however, SALCO has gone from strength to strength, experiencing an extraordinary growth in leasing contracts—from 13 in 1997 to 190 in 2002. Today, it ranks among the top 30 leasing companies in Russia, with clients ranging from small businesses to large enterprises.

"The general level of knowledge about leasing is very much higher now," says Mr. Malashich. "Practically all our clients consider leasing an alternative to banking loans for acquiring main assets, and we no longer find it necessary to engage in advertising and promotion."

Services offered by the company include finance leasing of equipment, machinery and means of transport, leaseback and cross-border leasing operations. The fishing industry, construction and the oil and gas industry are its biggest sources of clients.

SALCO's main goal is to capture all the opportunities presented by the Sakhalin shelf projects. There is great demand from contractors and subcontractors in the region for equipment, technologies and transport, Mr. Malashich says.

Having established itself firmly on the home market, however, SALCO is also turning its attention to spreading the word to foreign companies. These might include U.S. businesses involved in various kinds of operations in Russia and seeking a means of acquiring assets and increasing their production capability.

"Our task is to explain to the foreign companies that through the instrument of leasing we can lower the investment risks and the tax burdens for them in Sakhalin. When the leasing schemes are unfeasible, we tell clients they can do without us. We offer services only when they are feasible," says Mr. Malashich.

ALEXEY MALASHICH
General director of SALCO

Only a year ago, there was no demand for leasing services from the foreign companies. "They were simply studying the region to identify any areas of interest. Now many foreign companies are expressing an interest in Sakhalin," he adds.

SALCO is one of the few leasing companies in Russia with experience in international leasing operations and is ready to offer competitive finance leasing services to foreign firms. "Working with foreign companies is more difficult and requires more responsibility on our part as we have to be competitive and keep up international standard quality," says Mr. Malashich.

SALCO's policy is to provide services at an international standard level and to offer "absolute care" for the interests of its clients, stockholders, investors and business partners. This is the second year in which the company is conducting international standard auditing with PricewaterhouseCoopers. It was recently awarded the ISO 9001:2000 certificate by the International Organization for Standardization for its quality management system.

SALCO is also interested in collaborating with strategic partners, such as U.S. leasing companies looking to expand their services into the Russian market.

"We are negotiating with the European Bank for Reconstruction and Development and the International Finance Corporation, and we are open for dialogue with other investors," says Mr. Malashich.

International backing for a fresh start

NEW ERA WITH THE HELP OF THE INTERNATIONAL COMMUNITY, AND UNDER A NEW MULTI-ETHNIC GOVERNMENT, MACEDONIA IS ON THE ROAD TO ECONOMIC RECOVERY WITH ITS SIGHTS FIRMLY SET ON TAKING ITS PLACE IN THE WIDER WORLD

MACEDONIA has been making significant progress toward its goal of integration into the wider international political and economic community, as the process of reform has continued this year.

September's election of a multi-ethnic government, was a clear indication of the country's desire to resolve the ethnic division that erupted into armed conflict between the Macedonian Slavs and Albanians last year.

The parliamentary elections—a key element of the subsequent EU-brokered peace settlement—saw overwhelming support for the winning Macedonia Together coalition and the ethnic Albania Democratic Union for Integration (DUI) party. The two parties subsequently struck a power-sharing deal to form the new administration.

The new prime minister, Branko Crvenkovski, has made clear the government's commitment to lasting peace, safety and stability, and to boosting the economy and attracting foreign investment.

Approval of Macedonia's accession to the World Trade Organization in October was another important step, committing the country to a multilateral trading system and enhancing its attraction as an environment for business.

WELL PLACED Macedonia offers investors a favorable geographical position and good transport and communications

Macedonia benefits from considerable financial support from both the United States and the EU, in addition to the World Bank and the International Monetary Fund. Earlier this year, Macedonia was promised $515 million by international donors to rebuild the country and for general economic development purposes. However, the longer term objective of the former Yugoslav republic is to stand on its own feet through trade rather than aid.

Macedonia's strategic location makes membership of NATO and the European Union the inevitable twin focus of its hopes and aspirations for the future.

The country's president, Boris Trajkovski, sees the United States and Macedonia as partners in the region. "We share a common interest. Both want to see the region become stable as soon as possible, in order to allow it to grow more prosperous and more attractive to foreign investors."

He points out that during the Kosovo crisis, there was close cooperation between Macedonia and the United States. Macedonia was a stationing area for NATO forces and provided shelter for 350,000 refugees at a significant cost to the country's economy. "We simply acted as if we were a NATO member country," says Mr. Trajkovski. "We opened our borders to NATO. We did that for the benefit of the region. It was a humanitarian mission, a mission to save thousands of lives."

During the Kosovo crisis, Macedonia acted as if it was a NATO country

The continuity of the reform process in Macedonia has remained unbroken, even throughout the crisis in 2001. "We worked in close cooperation with the IMF and the World Bank, and we reached all our objectives," says Mr. Trajkovski.

BORIS TRAJKOVSKI
President of Macedonia

The framework for Macedonia's progressive integration into the EU is provided by the Stabilization and Association Agreement it signed in April 2001. The agreement provides for the step-by-step dismantling of trade barriers over ten years. It sets political and economic conditions and stresses the need for regional cooperation. Macedonia has signed free trade

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Steel needs regional market

A PLAN is being prepared for the reconstruction and conversion of Macedonia's steel and metal sector. The project is also likely to focus on a regional strategy for the development of the industry in neighboring Macedonia, Yugoslavia and Bulgaria.

Steel is one of Macedonia's major export commodities, accounting for an average of $120 million per year, mainly from sales to European markets.

"Macedonia needs the steel industry to survive," says William Ernst, Chairman of the Board of Balkan Steel. He adds, however, that if the industry itself is to survive, it must build markets, and in particular it must rebuild the regional market.

"The steel industry was always very integrated with Yugoslavia, and until some economic interdependence is established within the region, we will have a difficult time. The relationship between Serbia, Kosovo, Bosnia, Croatia and Montenegro must grow," he adds. "For us, the business has to be the Balkans."

He sees a positive trend in bilateral agreements signed last year between Macedonia and Serbia, Bosnia and Croatia.

Roughly 40 percent of Balkan Steel's products are exported to Balkan countries. "We are operating at a low level because all the ex-Yugoslav republics, except maybe Slovenia, are struggling with their economies," says Mr. Ernst.

WILLIAM ERNST
Chairman of the Board of Balkan Steel

"This has put us in a position where we have to establish new markets while struggling to stay in the old ones."

The U.S. was once a market for Macedonian steel, but Balkan Steel ceased shipping there when prices fell in 2000. High U.S. tariffs introduced by the Bush administration have ruled out a resumption of shipments across the Atlantic.

Mr. Ernst argues that Macedonia should be added to the list of developing nations that are exempted from the tariffs. "Macedonia is a developing country by American and EU definition," he says. "We are also the second largest per capita recipient of U.S. aid, after Israel. Excluding Macedonia from the tariffs makes both economic and political sense for the United States," he says.

In the meantime, Balkan Steel's biggest national market is Spain, where galvanized steel is imported for building construction. It also ships products to Portugal, Italy, France, Belgium, Germany and Greece. However, transportation from landlocked Macedonia makes it costly to operate in markets outside the Balkans.

"It is expensive for us to ship steel to Europe and the United States because we have to transport steel to Thessaloniki by ship," says Mr. Ernst.

Balkan Steel's biggest need is funding to upgrade its plant, which is of mid-1970s to 1980s vintage. "That's not old," says Mr. Ernst, "but it needs more updating in automation, computerization and quality enhancing modern tools. It would be a sound investment, especially for an investor who was able to bring a reliable source of semi-finished steel."

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agreements, with Slovenia, Croatia, FR Yugoslavia, Bulgaria, Turkey, EFTA countries and Ukraine.

"The agreement is in the course of implementation," says President Trajkovski. "The transformation towards a market economy is nearing its end. In order to develop our commerce, we need to utilize domestic investments along with the help of foreign investors.

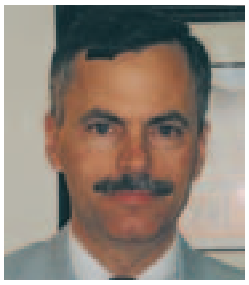
"We are a small country, but we have a great geographical position, good infrastructure and we can offer services to the region." he adds. "We play an important role in the development of the regional communications system—telecommunications, infrastructure, etc.

"We have well-educated youth and a very competitive labor force. We have enforced a set of laws that will encourage IT, e-banking and e-commerce development. Our goal is to produce more products on the market."

Maintaining stability in Macedonia is an important element of U.S. government efforts to reduce instability in the Balkans region and USAID has been a key bilateral donor, assisting the country with economic and democratic reforms. Aid has mostly been aimed at helping Macedonians to help themselves by backing projects aimed at making government structures more effective and supporting local business and economic development.

Sustainability is a key element. "A Macedonia that becomes dependent on foreign aid is in no one's interest," says Lawrence Butler, the U.S. ambassador.

He is in no doubt that it has advantages to offer U.S. investors, notably through its position as a major transportation corridor from western and central Europe to the Aegean Sea and from southern Europe to western Europe.



LAWRENCE BUTLER
U.S. ambassador to Macedonia

"Its strongest advantage is its position," Mr. Butler says. "Everywhere you go, you have to pass through this country. They have communications, railway tracks, roads and power plants in the right places—my cell phone works everywhere I go. It's an impressive structure."

Gligor Bishev, general manager of Stopanska Bank, the largest in the country, says, "We have economic, price, exchange rate and bank stability. The behavior of Macedonia in the economic area is predictable, which is something investors appreciate highly."

He points to the free trade agreements with neighboring countries and the good relationships with the markets of Turkey and Greece. "When you enter Macedonia, you are entering the regional market," he says.

New markets in neighboring states

A WELL-ESTABLISHED reputation for the quality of its products has led to important partnerships with foreign companies for Pivara Skopje, the largest brewery in Macedonia and one of the leading companies in the country.

The company brews and markets the Skopsko and Star Lisec brands and has captured an 80 percent share of the local market for beer. It also distributes Heineken and Amstel beers and a range of soft drinks, including Coca-Cola, Fanta, Sprite, Schweppes and also the BonAqua Water Portfolio.

Based in the Macedonian capital, Pivara Skopje has a production capacity of 1,100,000 hectoliters (220 million bottles) of beer and 948,000 hectoliters (94.8 million liters) of non-alcoholic beverages annually.

Originally founded as a joint-stock company, it has gone through several transformations in ownership in its 78-year history, including privatization in 1995. In 1998, Balkan Brew Holding Ltd of Greece, a joint venture by Athenian Brewery and the Hellenic Bottling Company, became the dominant shareholder with a 51 percent stake. Athenian Brewery is a fully owned subsidiary of Heineken.

Pivara Skopje's association with Coca-Cola goes back to 1991 when it began production as a licensed bottler for the company, for whom it has recently been installing new facilities.

"All our partners are satisfied with the present level of cooperation," says Svetozar Janevski, the company's general director. "We are one of the most successful and profitable companies in the region."

SVETOZAR JANEVSKI
General director of Pivara Skopje

From its plant in Skopje, the company distributes its products through 12 distribution centers, located in Macedonia's largest trade and industrial areas. Each center is equipped with its own fleet of modern, specialized trucks, so the products find their way to customers quickly and efficiently—even in the remotest parts of the country.

Pivara Skopje also produces malt, wine, vinegar, dried brewers yeast and dried spent grains. The company is committed to the introduction of new technologies and improvement of existing ones, and to the on-going training of its employees. It was recently awarded an ISO 9002 quality certificate.

Given its dominance in the Macedonian market, it is not surprising that Pivara Skopje is looking to develop new markets in neighboring countries.

"We have been in southern Serbia for 75 years and currently have 24 percent of the market share there," says Mr. Janevski. "We plan to expand into central Serbia in the years to come.

"Our future strategy is to have around 75 percent of the local market and have the same level of sales in neighboring countries as on the domestic market, which means that in three years we will double our sales.

"We expect to become one of the 10 top players in the region of Bulgaria, Serbia, Macedonia and Croatia," he adds. "We plan to enter Albania also. This is the area in which we intend to grow."

Pipeline will boost production at refinery

SMOOTH FLOW COMPLETION OF A MAJOR PROJECT HAS GIVEN MACEDONIA CHEAPER OIL AND OPENS THE PROSPECT OF EXPORTING REFINED PRODUCTS WITHIN THE REGION

THE BIGGEST energy project in the Balkans, a pipeline linking the northern Greek port of Thessaloniki with the OKTA oil refinery outside Skopje, began full operations in September. The pipeline, which took three years to build, will provide Macedonia with a constant and reliable source of oil and, in the longer term, there are plans to export refined oil products to neighboring areas.

Macedonia has been paying a high price to move a million tons of oil and petroleum products a year from Thessaloniki by road and rail. The 130-mile pipeline will cut those costs by transporting 2.5 million tons of crude oil to the refinery per year.

OKTA, Macedonia's sole refinery, was established in 1982 as the regional facility for southern Yugoslavia. It was acquired in 1999 by Greece's state-owned oil refining group, Hellenic Petroleum, as part of its strategy to enter the Balkans energy market.

With an annual capacity of 4 million tons, OKTA is well able to meet Macedonia's own need for 1.25 million tons of refined products per year—expected to rise to 1.5 million tons by 2006. A ready, and cheaper, supply of crude oil means the spare capacity can be used to produce products for export to neighboring areas like Kosovo, where refining capacity was destroyed during the recent conflict.

Hellenic Petroleum is the main investor in the pipeline and the European Bank for Reconstruction and Development (EBRD) provided a loan of $50 million towards the $130 million cost. Hellenic Petroleum holds an 80 percent stake through its subsidiary El Pet Balkiniki, with the remaining 20 percent held by the Macedonian government.

Petros Karalis, OKTA's managing director, says Hellenic Petroleum expects to see a return on its investment within 10 years.

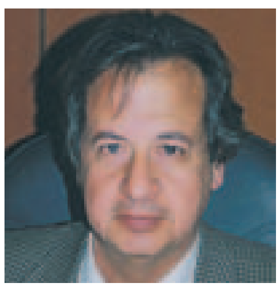
"OKTA is now where it was planned to be," he says. "We have finished a very big project in very difficult times, but this is not a static business. There are a lot of things going on and we have the capacity to do a lot more.

"We would like to see OKTA working within a network that covers Macedonia and Kosovo. We are looking to expand to other areas, like southern Serbia."

Plans to make OKTA part of a network extending to Kosovo and south Serbia

A new project, entirely Greek-funded, has been launched to build a $40 million pipeline to transport refined product from OKTA to the Kosovan capital, Pristina. Construction, which began in September, is expected to be completed within two years. Sixty miles long, the pipeline is designed to have the capacity to transport 300,000 tons of oil derivatives per year. There will be a second pipeline from OKTA to southern Serbia.

In the meantime, Hellenic Petroleum has started to modernize the refinery and bring it up to EU standards. "Refurbishment has already started," says Mr. Karalis.



PETROS KARALIS
Managing director of OKTA

"This is a fiber decentralization plan, worth $16-17 million, which is going to produce products of EU quality. We are going to reduce the sulphur content in products and there are some minor projects which will bring the total amount invested in the refinery to around $40 million."

Oil derivatives produced at OKTA include liquefied petroleum gas, naphtha, motor gasoline, diesel fuel and fuel oil.

Environmental protection is regarded as a priority. OKTA is the only company in Macedonia which has complete physical, chemical and biological waste water treatment. The refinery's power supply comes from its own power station. Surplus supply electricity is directed to the national distribution system.

Another of the strategic objectives of OKTA is to extend the distribution network by building around 30 modern petrol stations. "Our retail business is small at present, but we have plans to develop in that direction," says Mr. Karalis.

Paving the way for investment in the region

OPEN DOOR U.S. COMPANIES LEAD FOREIGN INVESTMENT IN KRASNODAR. THE GOVERNOR WOULD LIKE TO SEE MORE AMERICAN FIRMS COMING TO THE REGION

ATTRACTING INVESTMENT is a key issue in the development of Krasnodar's economy and regional authorities pay considerable attention to creating a favorable climate for doing business.

Krasnodar is rated among the top ten destinations in Russia for investment potential. It also rates highly in terms of legislative activity to encourage investment.

The state provides support with tax privileges and credit arrangements. Investors are also eligible for preferential conditions for use of land and other natural resources.

"We have to convince businessmen to put their money here," says the governor of the region, Alexander Tkachev. "We understand that a firm legal basis is very important. In general, we have no laws that prevent foreign investors from working here successfully.

"It is also very important to create an atmosphere of political stability in the region. We have done that, and investors are responding."

ALEXANDER TKACHEV
Governor of the Krasnodar Region

Last year investment in Krasnodar exceeded $2 billion, almost twice as much as the figure for 1998. Since 1991, when the region started to attract foreign firms, the number of joint ventures has risen to more than 800. These involve partners from 72 countries, including more than 70 companies from the United States.

Judged by the amount of capital invested, the U.S. leads with investment volume totalling more than $62 million.

"I think we can be proud of Krasnodar-US business cooperation," says Mr. Tkachev. "We would like to see more activity on the part of American companies."

The sectors attracting the greatest investment are manufacturing (30 percent), commerce (20 percent), construction (15 percent) and agriculture (8 percent).

Tourism is another sector the authorities want to promote. The governor pinpoints the development of the Krasnaya Plyana Recreation Complex, considered by the National Olympic Committee of Russia as a possible location for the Olympic Games.

"It is a very attractive project for investors," says Mr. Tkachev. "The landscape, high mountains and climate provide all the conditions for the creation of a mountaintop resort of European standards—one that will function in winter and in summer as well."

Charting a steady course

KRASNODAR'S well-developed transport network makes it the southern gateway to Russia and an important hub for trade. More than 26 percent of international Russian cargo, and a third of Russian oil exports, pass through the region.

There are eight ice-free ports offering year-round access, including Russia's biggest port at Novorossiysk on the Black Sea. Based there is Novorossiysk Shipping Company (Novoship), one of the largest shipping companies in Russia and among the 10 largest in the world.

The company is an effective competitor on the world market, with 97 percent of its cargo transported to other countries, and two-thirds of its tankers passing to and from the United States.

"We are fully busy, which shows how competitive we are," says Novoship's president, Tagir Izmailov. "We have received $456 million in credit facilities from various Western banks, so we are well accepted in the market."

Mr. Izmailov attributes the company's success to its long experience doing international business and to its well-qualified and well-paid crews. The company employs 7,000 people and its crews are all-Russian.

Novoship's current financial position is very healthy and the company is trading profitably. It was inevitably affected by the Russian economic crisis of August 1998 and by the depression of the world freight market that caused problems for all major shipping companies in 1998/99. However, determination and strength of purpose saw the company progress satisfactorily through this difficult period and the long-awaited upturn in freight values in mid-2000 saw increased profits for its principal areas of activity.

Novoship's basic strategy of concentrating on its "wet" bulk shipping operations proved correct. While dry-cargo earnings remained static, oil products and chemical tanker operating profits increased by 115 percent.

TAGIR IZMAILOV
President of Novorossiysk Shipping Company

"Most of our business is with the major companies, such as Shell, BP, Chevron and Texaco," says Mr. Izmailov.

Novoship's fleet is divided into two main groups: larger-sized vessels, ranging from 55,000 to 150,000 tons, for crude oil and smaller sized ones, ranging from 30,000 to 47,000 tons, for transporting products.

Systematic fleet renewal and modernization are a key element of the company's strategy. January 2000 saw the completion of the company's fleet renewal and modernization program, which began in 1995 and was maintained throughout the subsequent difficult years. During the five-year period to 2000, 22 new ships were built and brought into service, giving Novoship a modern competitive merchant marine fleet with which to expand its commercial activities.

It enabled the company to take advantage of the rise in tanker earnings in the second half of 2000, which increased its operating profit by 300 percent in comparison with 1999. Since then, the company has focused on the continuing development and expansion of its tanker carrying capacity. In terms of deadweight tonnage, tankers represent 78 percent of the Novoship fleet.

Further fleet renewal projects are planned up to 2005. "Our total assets are $1,100 million. In addition to that, we have ordered another ten vessels for nearly $320 million," says Mr. Izmailov. "These vessels will come in September 2003, in 2004 and 2005. It is important to substitute new vessels for those that are ageing. Our vessels range from three to 20 years old. The average is 12.7 years."

The third part of the company's business is on-shore activity, which it plans to consolidate and develop. This includes small facilities for loading and unloading, a ship repair service and training facilities.

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