The Kaliningrad Oblast of the Russia Federation:
It’s Development Prospects on the Conceptual Baltic Main Street

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Resumo


Palavras-chave: Enclave de Kaliningrado, Federação Russa, Desenvolvimento Regional, Interacção Espacial, Fricção do Espaço, Decomposição da Distância,

1 An earlier draft can be seen as a discussion paper on the Viessmann Research Centre on Modern Europe at Laurier web site. The exact web location is: http://info.wlu.ca/~wwwgeog/special/viessman/Onlinepapers/2004/index_04.htm
Abstract

With the break up of the USSR in the early 1990s, the Kaliningrad Oblast on the Baltic, part of former East Prussia was, through the independence of Lithuania, geographically cut off from the main land body of Russia. As if this was not enough of a problem for the region, the 2004 expansion of the EU into Poland and the Baltic states increased the isolation aspect even more. In addition the recent expansion of NATO into the former USSR block countries, separated the region even more from the geographic core of the nation. The question must be raised what socio-economic impact have these events already have had on the development path of the Oblast or will have in the future. The first decay after the break up of the USSR where not kind for Kaliningrad's development. Hence, is its future tied to the EU, the Baltic States or Russia? It is proposed here that Kaliningrad's development future lies in large part with the Baltic region of Europe. Lying on the conceptual Baltic Main Street, a major highway circulating the Baltic Sea, is a substantial advantage for the region and should have a major influence on its regional development in the future.

Keywords: Kaliningrad Oblast, Russian Federation, Regional Development, Interaction Space, Friction of Space, Distance Decay, European Union (EU), NATO, USSR, European Kaliningrad Perspective, Centralist Perspective, and Regional Russian View.

Résumé

Avec le démembrement de l'URSS, au début des années 90, Kaliningrad Oblast dans la mer Baltique, partie de l'ancienne Prusse Orientale, a été géographiquement coupée du corps principal de la Russie, grâce à l'indépendance de la Lituanie. Comme si ça n'était déjà problème suffisant pour la région, l'expansion de l'UE, en 2004, pour la Pologne et les États Baltiques, a encore davantage augmenté l'isolement. En plus, la récente expansion de l'OTAN pour les pays de l'ancien bloc soviétique a encore plus séparée la région du centre géographique de la nation. On se demande quels impacts socio-économiques on déjà eu ces événements dans le processus de développement d'Oblast ou auront lieu dans le futur. La première décennie après la chute de l'URSS n'a pas été douce pour le
développement d'Oblast. Son futur est-il lié à l'UE, aux États Baltiques ou à la Russie? On propose ici que le futur du développement de Kaliningrad reste en grande partie avec la région baltique de l'Europe. La localisation dans le centre du Baltique, une autoroute majeure dans la mer Baltique est un avantage substantiel pour la région et devra avoir une influence majeure dans son développement régional futur.

Mots-clés: Kaliningrad Oblast ; Fédération Russe ; Développement Régional ; Espace d'Interaction ; Friction de l'Espace ; Décadence de la Distance ; Union Européenne ; OTAN ; USSR ; Perspective Européenne de Kaliningrad; Perspective Centraliste.

1. Introduction

When the Baltic States became independent in 1991, the Kaliningrad Region suddenly became an exclave separated from the rest of Russia with its own borders to independent countries (Figure 1). When NATO recently expanded and Poland and Lithuania joined this defence association the isolation was increased. The latest and probably the most severe barrier came when Poland and Lithuania joined the European Union on May 31, 2004. Not only did national political borders separate it from mainland Russia, but to it were added the barriers of the major trading block in the world, the EU, sometimes referred to as ‘fortress Europe’. These barriers are now frequently referred to as the ‘Paper Curtain’ around the Kaliningrad Oblast (MacKinnon, 2004). Given these developments the Kaliningrad Oblast has been seen either as “the forward military bastion of Russia, as a ‘second Cuba’ menacing its neighbours, or [as] a free trade area, a ‘Baltic Hong Kong’ contributing to peace and prosperity” for all of Russia. (Joenniemi & Parawitz, 1998, 1). What it actually is in large part determined from which geographic perspective an individual views the Kaliningrad region, from within the EU, from within Kaliningrad or from Moscow, the core of Russia. One can also examine the causes of its present underdeveloped status from these three perspectives and assign potential or actual problem issues appropriately.

But before we do a more detailed evaluation it is important to point out Kaliningrad’s relative and absolute location and conditions. It is one of 89 Oblast (or equivalent) territories of the Russian Federation. Its land mass comprises some 15,000 square kilometres, (about 170 by 90 km) which is part of the former German East Prussia territory. It was given to the USSR for administrative purpose after World War II until a final World War II peace treaty was to be signed.
The present population is about one million inhabitants, mostly of Russian ethnic background. The former German population had fled from the region towards the end of World War II or was asked to leave after the war. It has a northern border with Lithuania and a southern one with Poland. The most direct route from the Kaliningrad Oblast to mainland Russia is through Lithuania and Belarus, which were, until 1991, part of the USSR. If one looks at straight line distances, other countries like Latvia, Estonia, Belarus, Finland, Sweden, Denmark and Germany are all within 800 km of the city of Kaliningrad. In fact, Moscow is further away then many of the more heavily populated regions of these countries. Clearly the Oblast's geographic location is a major factor in its ties and relationships to the Baltic states as well as with the other EU countries.

2. The Moscow View and Perspective

The Kaliningrad region as seen from Moscow, the heart of Russian economic and political centre is very much influenced by Kaliningrad’s geographic periphery. Interaction over space, be it the movement of goods and services or people, is highly influenced by what geographers call the friction of space. Clearly more interaction takes place between two entities that are closer together then ones that are further apart, holding all other things constant. In fact this truism has led to the first law in Geography which states ‘that closer things are more related then further things’. The word related refers to physical as well as human socio-economic-
-cultural endeavours. Clearly, interactions within a household are greater than between different households, within a city they are greater than between cities and between adjacent regions (provinces in Canada and Oblasts in Russia) than with those that are further away. A great example from Canada relates to a strong decline in the trade of manufacturing goods between provinces the further they are apart (Kucsma, 1993). Clearly, many Canadian provinces have far greater economic interactions within themselves and the adjacent regions in the USA than with the other provinces further away. Spatial economic interactions have a clear analogy to the force of gravity between the mass of two objects and the distance between them.

When viewed from Moscow, Kaliningrad is far away with limited interaction possibilities. Even in the USSR days, Kaliningrad was located distinctly in the periphery of the empire. Except for its military importance and its ‘historic’ conquest and acquisition by the USSR in 1945, in part as a reward for the suffering of the Russian population at the hands of the Nazis, it did not form a major component of the USSR. Its potential low place on the interaction scale with Moscow, as seen from the theoretical perspective in Figure 2a, is understandable and with the break-up of the USSR, Kaliningrad clearly moved even further into the periphery of central Russia. Its interaction space was now not only hindered by space itself but also by political boundaries like those of Lithuania, Poland and even Belarus (Figure 2b). Travel document requirements for people and goods increased the burden of interacting with the other part of Russia substantially after 1991. In order to avoid these, people have to fly or take a ship to get to Kaliningrad which means additional cost and greater inconveniences. When Lithuania and Poland joined NATO and the EU in 2004, these barriers increased from national to international (EU), making the isolation of the Kaliningrad Oblast from the main part of Russia even more severe (Figure 2c). All these developments, as seen from Moscow, created an island out of the Oblast with a sea of technical, political, economical and even environmental barriers.

3. The Kaliningrad Perspective

When these developments are seen from Kaliningrad’s perspective, they are similar in terms of barriers to interaction with Moscow and the remaining part of Russia. Even before the collapse of the USSR, Moscow, as the symbolic heart or core of the USSR, was rather far away. Most of the interaction took place over the closer adjacent geographical space (Figure 3a). With the collapse of the USSR much of Kaliningrad’s hinterland was cut off and its support structures decimated. When the adjacent regions became parts of the former competing western blocks
its isolation drastically increased. At the same time its geographic proximity does not allow it to disregard its physical neighbours. Even thought political, social, economic and linguistic barriers now exist, the region is bombarded with media information of all kind from the adjacent territories. And clearly Kaliningrad’s people want to interact with these desired economic and cultural spaces and its long term development perspectives depend on interaction with the EU (Figure 3b).
4. The EU Perspective

A different perspective on Kaliningrad’s interaction space comes from the core of the EU. Since the EU is basically a big trading block, with high external and low internal trade barriers, the Kaliningrad Oblast blocks in part its natural trading region on the eastern half of the Baltic (Figure 1). Especially overland transactions with the three new Baltic States of Lithuania, Latvia and Estonia are interrupted by foreign political entity. Even if favourable transit agreements are reached for goods, people and information channels, Kaliningrad nevertheless will hinder the EUs natural development of the eastern Baltic (Figure 5). In addition, the location of a poorer political region within in its geographic space, with different laws and regulations regarding commerce, property, trade, health and communication regulations, creates a sense of insecurity and potential lawlessness in the East. It is therefore in the EUs interest to remove such potential problems by having special trading, travel, law enforcement, environmental and other agreements with the Russian state for the Kaliningrad Oblast.

5. Changing Conditions in Kaliningrad after 1991

Since the break-up of the USSR in 1991 the socio-economic conditions in Kaliningrad have worsened. Given the interaction models above this is not surprising. With the introduction of a major barrier, the Lithuanian borders, and the decrease in importance of the military significance of Kaliningrad to Russia, it was bound to happen that Kaliningrad moved more into the periphery of the core
regions of Russia. The movement of goods and people became more difficult. At the same time Russia still retained much of its former centralized economic and socio-political structure over Kaliningrad. All this implied a lower level of significance of Kaliningrad for Russia despite the fact that it still retains a high emotional and political level of awareness in Russia, especially for the older people. It, after all, was in part a World War II reward for all the suffering of the Russian people caused by the Nazis. But with the decline of the Russian military presence in Kaliningrad after 1990, there also came a decline in the awareness and significance of the Oblast and with it its economic well being also started to decline. As the figure below shows, GDP per person, in terms of PPP, declined from 9,300 USD per person to only 4,400 in 2000, some 211%. In contrast the decline for the overall Russian federation was only 165% and that of the North-West Area of Russia, which Kaliningrad was highly integrated with before 1991, was only 153% (Figure 6).

By the year 2000 the Kaliningrad Region’s economy had only 75% of the income of the Russian Federation. In contrast, in 1990, it was above the Russian average! Presently it plays an insignificant role in Russia’s national economy comprising only a half percent of Russia’s overall GDP.

If one looks at absolute Rubles income per capita for these three regional entities we can see a slightly improving trend. The Kaliningrad Oblast goes from 26 thousand to 35,000 Rubles per year which was just under 60% of the income of that of the Russian Federation average in 1995 to 67% in 2003 (Table 1). In comparison to the North West region of Russia, Kaliningrad goes from 57% to 70%. Although the absolute income figures increase over the time period, if one converts the income to US dollars at the official average yearly rate, one can see that income went down from 5806 US dollars for Kaliningrad in 1995 to only
1143 in 2003. The devaluation of the Ruble in 1998 destroyed the income of the Russian people, as measured in US dollars, by a factor of nearly five!

Comparing Kaliningrad's development with that of its nearest neighbours Lithuania and Poland, brings also out a far worse situation then when it is compared to the Russian Federation. Lithuania only declined only 135% by 2000 after it left the USSR in 1990 and Poland, which was never part of the USSR, increased steadily its GDP per person by 71% over this time period (Figure 5). But, whereas Lithuania has recorded a gradual increase in GDP per person since 1994, only some four years after independence, clearly Kaliningrad has not been able to counter its decline. Only since 2000 has it experienced some positive grows, and one has to wonder if the one year increase is a new trend or just a temporary upturn. By the middle of 2004, its GDP per person in US Dollars was only 43.5% of that of Lithuania, 35% of Poland and only 7.1% of Canada's, a clearly disappointing situation. (http://www.spiegel.de/jahrbuch/0,1518,CAN,00.html).

Other conditions, besides GDP per person also changed substantially in the Kaliningrad Oblast compared to conditions in the Russian Federation in the first eight years since the break-up of the USSR. Let me point out some of these, for selective years, with the help of different tables2.

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Table 1 – Gross Domestic Annual Income per Capita in Rubles and 2000 Prices (GDP deflator)

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Russia</td>
<td>45161</td>
<td>42838</td>
<td>42794</td>
<td>39386</td>
<td>39234</td>
<td>42902</td>
<td>46102</td>
<td>49048</td>
<td>52146</td>
</tr>
<tr>
<td>NW Region (average)</td>
<td>46285</td>
<td>38840</td>
<td>37795</td>
<td>37889</td>
<td>38635</td>
<td>40574</td>
<td>41971</td>
<td>44150</td>
<td>50102</td>
</tr>
<tr>
<td>Kaliningrad Oblast</td>
<td>26712</td>
<td>25985</td>
<td>24295</td>
<td>21841</td>
<td>23541</td>
<td>25931</td>
<td>30883</td>
<td>32369</td>
<td>35069</td>
</tr>
<tr>
<td>Kaliningrad Oblast as % of Russia</td>
<td>59.15</td>
<td>60.66</td>
<td>56.77</td>
<td>55.45</td>
<td>60.00</td>
<td>60.44</td>
<td>66.99</td>
<td>66.00</td>
<td>67.25</td>
</tr>
<tr>
<td>Kaliningrad Oblast as % of NW</td>
<td>57.71</td>
<td>66.90</td>
<td>64.28</td>
<td>57.64</td>
<td>60.93</td>
<td>63.91</td>
<td>73.58</td>
<td>73.32</td>
<td>70.00</td>
</tr>
<tr>
<td>Rubles per US $ (official rate – yearly)</td>
<td>4.60</td>
<td>5.17</td>
<td>5.84</td>
<td>9.71</td>
<td>24.62</td>
<td>28.13</td>
<td>29.17</td>
<td>31.35</td>
<td>30.69</td>
</tr>
<tr>
<td>Kaliningrad Oblast Income in US $</td>
<td>5806</td>
<td>5029</td>
<td>4162</td>
<td>2250</td>
<td>956</td>
<td>922</td>
<td>1059</td>
<td>1033</td>
<td>1143</td>
</tr>
</tbody>
</table>

Source: V. V. Dashkeyev, Institute for the Economy in Transition, Moscow, Rosstat, Nov. 7, 2005, email

Figure 5

**Comparison of Development Dynamics of the Kaliningrad Region, Lithuania and Poland (GRP/GDP per Capita, thousand USD)**

Source: Zhdanov, et. al. 2002, p. 8
Table 2 – Average Income per Capita in the Kaliningrad Oblast

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td>0.15</td>
<td>0.48</td>
<td>379</td>
<td>1063</td>
</tr>
<tr>
<td>Average of all Oblast</td>
<td>0.15</td>
<td>0.46</td>
<td>444</td>
<td>1262</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of Russian Regions</td>
<td>0.98</td>
<td>1.03</td>
<td>0.85</td>
<td>0.84</td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td>11</td>
<td>9</td>
<td>28</td>
<td>31</td>
</tr>
</tbody>
</table>

As can be seen from table 2 the relative average monthly income per capita did decline between 1985 and 1999 comparatively to the other Russian Regions. Kaliningrad had the 11th highest average income rank in 1985, which was equal to the average of all the Russian Regions and its ranking increased to ninth following the fall of Communism in 1991. However, the relative average income declined to 28th place by 1995 and 31st in 1999. The data under girds the graph data in Figure 4.

Table 3 presents data on the actual and registered unemployment rates for the Kaliningrad Oblast in 1992, 1995 and 1999. As can be seen the real unemployment rate increased substantially from 5.3 to 15.9 percent during this time period. Except for 1995 its actual rate is higher then the average of all Russian Regions, some 16% above the other entities. Actual unemployment rates in Kaliningrad began the period by being higher than the average Russian Regions rate, declined to below the average in the mid-90’s, but then increased again towards the end of the period.

Table 3 – Unemployment Rates in the Kaliningrad Oblast

<table>
<thead>
<tr>
<th>Kaliningrad Unemployment rates (end of the year; %)</th>
<th>1992</th>
<th>1995</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual unemployment rate</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kaliningrad Oblast</td>
<td>5.3</td>
<td>9.2</td>
<td>15.9</td>
</tr>
<tr>
<td>Average of all Russian Regions</td>
<td>4.9</td>
<td>9.31</td>
<td>13.68</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of Russian Regions</td>
<td>1.08</td>
<td>0.99</td>
<td>1.16</td>
</tr>
<tr>
<td>Registered unemployment rate</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kaliningrad Oblast</td>
<td>1.2</td>
<td>5.1</td>
<td>1.5</td>
</tr>
<tr>
<td>Average of all Russian Regions</td>
<td>0.88</td>
<td>3.91</td>
<td>1.89</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of Russian Regions</td>
<td>1.36</td>
<td>1.3</td>
<td>0.79</td>
</tr>
</tbody>
</table>

The second part of the table shows the official registered unemployment of the Kaliningrad Oblast in these years. Contrary to the actual unemployment rates,
the official registered unemployment rates increased substantially between 1992 and 1995, but by 1999 had declined and returned to near the 1992 rate. But the Kaliningrad/Average of Russian Regions ratio indicates that comparatively to the other Regions, the registered unemployment rate has been in steady decline between 1992 and 1999 going from 36% above the average to only 79% of the average. In comparison the actual ratio went from eight percent above to 16% above the Russian Average in these two years. Why would the difference in these unemployment rates be so high? One has to wonder about the reliability of the data, who collected it and for what purpose and what role of the black market economy may have played in the Region in these years:

Changing percentages in income received from wages and salaries, small business, transfer payments, property rents and other sources over the 1985 and 1999 period, can be seen in tables 4 and 5. Wages and salaries in Kaliningrad, much like all the other Regions of Russia, declined drastically in proportion of total income. But between 1985 and 1995, Kaliningrad’s proportion declined even more so then the other regions only to recuperate a little in 1999. Clearly the change in corporate structure in Russia, especially the decline in big Russian Enterprise probably accounted for this decline.

In terms of small business income, Kaliningrad also did not fair well as its originally rank of 34th in 1985 declined to 44th by 1999. It also regressed in terms of the proportion of income that is made up of transfer payments. In 1985, Kaliningrad population received only 14% of its income through transfer payments which was 43rd worst out of 89 regions. However, by 1999, this regional dependency on transfer payment increased to 16% of income, and consequently, in comparison to the other Russian regions, its ranking rose to 33rd. The decrease in the military presence in the Oblast may account in part for this change.

<table>
<thead>
<tr>
<th>Year</th>
<th>Wages and salaries</th>
<th>Small business</th>
<th>Social Transfers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td>73.5 71.4 38 42.2</td>
<td>14.9 8.5 14.2 13.3 16.2 16.3</td>
<td></td>
</tr>
<tr>
<td>Average of all Regions</td>
<td>74.55 73.38 42.38 42.63</td>
<td>17.25 13.09 16.38 15.46 16.45 17.9</td>
<td></td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of all Regions</td>
<td>0.99 0.97 0.9 0.99</td>
<td>0.86 0.65 0.87 0.86 0.99 0.91</td>
<td></td>
</tr>
<tr>
<td>Kaliningrad Rank</td>
<td>23 29 34 23</td>
<td>34 44 43 41 29 33</td>
<td></td>
</tr>
</tbody>
</table>
Table 5 – Proportion of Income from Property Rent and Other Income

<table>
<thead>
<tr>
<th></th>
<th>Year</th>
<th>Property rents</th>
<th>Other incomes</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td>1.5</td>
<td>2.4</td>
<td>4.8</td>
<td>4.1</td>
<td>10.8</td>
<td>12.9</td>
<td>26.1</td>
<td>28.9</td>
</tr>
<tr>
<td>Average of all Regions</td>
<td>1.49</td>
<td>2.39</td>
<td>6.2</td>
<td>3.72</td>
<td>7.58</td>
<td>8.77</td>
<td>17.72</td>
<td>22.67</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of all Regions</td>
<td>1.01</td>
<td>1.01</td>
<td>0.77</td>
<td>1.1</td>
<td>1.42</td>
<td>1.47</td>
<td>1.47</td>
<td>1.28</td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td>28</td>
<td>28</td>
<td>35</td>
<td>16</td>
<td>7</td>
<td>4</td>
<td>6</td>
<td>11</td>
</tr>
</tbody>
</table>

Interestingly property rents became a more important source of income in Kaliningrad going from 1.5% to 4.1% over this time period. While initially increasing in proportion between 1985 and 1995 it decline slightly between 1995 and 1999, nevertheless Kaliningrad was able to improve its position in rent income, from 28th in 1985 to 16th in 1999. Rent income from EU tourists may have accounted for this improvement.

Other sources of income went from nearly 11% to nearly 28%. One can only speculate what kind of income this category covers. Black market income or rather the informal economy could be the source. Despite this increase, the relative importance of this income to the people in the Kaliningrad Oblast declined in comparison to the other Russian Regions as its ranking declined from its peak of fourth in 1990 to 11th in 1999.

Table 6 – Average Private Bank Deposits

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td>1.1</td>
<td>2</td>
<td>225</td>
<td>709</td>
<td></td>
</tr>
<tr>
<td>Average of all Russian Regions</td>
<td>1.3</td>
<td>2.1</td>
<td>193</td>
<td>683</td>
<td></td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of Russian Regions</td>
<td>0.86</td>
<td>0.95</td>
<td>1.16</td>
<td>1.04</td>
<td></td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td>45</td>
<td>36</td>
<td>8</td>
<td>17</td>
<td></td>
</tr>
</tbody>
</table>

Average private bank deposits, in the Sberbank of Russia, between 1985 and 1999, are presented in table 6. Overall, this table shows a substantial increase in the average private deposit in the Kaliningrad Oblast. In 1985, this region only ranked 45th but it increased its standing to 8th in 1995, only to decline to 17th in 1999. Still according to bank deposits the region is doing comparatively well.

If bank deposits increased relatively over the 1985 to 1999 period, as seen in table 6, one could expect that the proportion of people living below the property level should have decrease as well. Unfortunately, this is not the case as is seen in
table 7. It shows a substantial increase in poverty (21% to 37%) in the Kaliningrad Oblast for the 1994 to 1999 period.

Table 7 – Subsistence Level in the Kaliningrad Oblast

<table>
<thead>
<tr>
<th>Proportion of population with incomes below the subsistence level, in %</th>
<th>Year</th>
<th>1994</th>
<th>1996</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td></td>
<td>21.6</td>
<td>25.1</td>
<td>37.4</td>
</tr>
<tr>
<td>Average of all Regions</td>
<td></td>
<td>22.46</td>
<td>26.27</td>
<td>39.81</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of Russian Regions</td>
<td></td>
<td>0.96</td>
<td>0.96</td>
<td>0.94</td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td></td>
<td>22</td>
<td>25</td>
<td>23</td>
</tr>
</tbody>
</table>

The provision of accommodation in terms of square meters per capita between 1985 and 1999, is displayed in table 8. This table does indicate that there has been an increase in accommodations space, however, as shown by the ratio and the ranking, this increase has not been as rapid as in other regions of Russia. Kaliningrad's ranking slipped from 29th to 38th even though the average housing space increased by 3.3 square meters or 21%. In contrast, average housing space in the 89 regions of Russia increase by 29%.

Table 8 – Size of Average Resident Space

<table>
<thead>
<tr>
<th>Housing space at the end of each year, in square meters per capita</th>
<th>Year</th>
<th>1985</th>
<th>1991</th>
<th>1995</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td></td>
<td>15</td>
<td>16.1</td>
<td>17.8</td>
<td>18.3</td>
</tr>
<tr>
<td>Average of all Russian Regions</td>
<td></td>
<td>15.06</td>
<td>16.83</td>
<td>18.49</td>
<td>19.44</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of Russian Regions</td>
<td></td>
<td>0.99</td>
<td>0.96</td>
<td>0.96</td>
<td>0.94</td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td></td>
<td>29</td>
<td>33</td>
<td>32</td>
<td>38</td>
</tr>
</tbody>
</table>

If people where able to increase their living space during this period one can also expect that they would have funds to increase their purchases of retail goods. Table 9 shows the changing retail turnover per capita, in 1998 Rubles, between 1985 and 1999. Kaliningrad clearly had above average retail purchases during this time period when compared to the rest of Russia. Nevertheless, its overall retail sales ranking fell from 10th in 1985, to 5th in 1991, to 18th in 1995 and to 16th in 1999.

Table 9 – Retail Sales

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td></td>
<td>1065</td>
<td>3527</td>
<td>3055</td>
<td>9370</td>
</tr>
<tr>
<td>Average of all Russian Regions</td>
<td></td>
<td>1024</td>
<td>2995</td>
<td>2890</td>
<td>8588</td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average of All Regions</td>
<td></td>
<td>1.04</td>
<td>1.18</td>
<td>1.06</td>
<td>1.09</td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td></td>
<td>10</td>
<td>5</td>
<td>18</td>
<td>16</td>
</tr>
</tbody>
</table>
Table 10 - Fixed Capital Investments in the Kaliningrad Oblast

<table>
<thead>
<tr>
<th>Investments (‘000) in fixed assets per capita (after 1995 in straight Rubles)</th>
<th>Year</th>
<th>1985</th>
<th>1991</th>
<th>1995</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kaliningrad Oblast</td>
<td>1.1</td>
<td>1.2</td>
<td>1058</td>
<td>2370</td>
<td></td>
</tr>
<tr>
<td>Average for all Russian Regions</td>
<td>1.4</td>
<td>1.6</td>
<td>1565</td>
<td>4210</td>
<td></td>
</tr>
<tr>
<td>Ratio: Kaliningrad/Average Russian Regions</td>
<td>0.77</td>
<td>0.74</td>
<td>0.68</td>
<td>0.56</td>
<td></td>
</tr>
<tr>
<td>Kaliningrad Oblast Rank</td>
<td>25</td>
<td>31</td>
<td>32</td>
<td>34</td>
<td></td>
</tr>
</tbody>
</table>

A rather depressing development picture for the Kaliningrad Oblast emerges from the data in table 10. Investment in fixed assets per capita, between 1985 and 1999 declined strongly in relative terms with the other regions of Russia. In 1985 the region invested 77% of the average of all regions but by 1999 it was only 56%. The decline was constantly downward for each year. The result was that Kaliningrad declined from 25th place to 34th. Such a declined clearly implies production problems in the future and with it a decline in the standard of living of the region.

In the next sections a closer examination of development prospects and geographic orientations will be examined to possibly counter to the development trends in the 1990’s as shown in the above 10 tables.

6. Field Perspective from the Kaliningrad Region

In March of 2002 I visited the Kaliningrad Oblast from the 12th to the 17th. The visit related to the CEPRA project “Problems of economic development of a region isolated from main economic centres of a country (with Kaliningrad oblast and a single Canadian provinces (territories) as an examples)” and its resulting publication3. This project was one of a number, which are part of a larger project entitled Economic Policy and Economic Development of the Regions in Russia. The aim of the visit was to speak to people in ministries responsible for development in the region as well as with some private firms and individuals about issues and problems in the region. In part the visit also was to determine how the region viewed its present isolation from the main part of Russia. Secondly, it was to determine the attitude of the local officials and people towards possible further isolation when Poland and Lithuania would join the EU on May 1st, 2004.

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Alexei Shekhovtsov, a member of the research team on this project and a member of the Institute for the Economy in Transition (IET) travelled with me. He did all the organising in Kaliningrad and the translation as needed. My sincere thanks go to him for his commitment and willingness to help in all the phases of the visit.

Before travelling to Kaliningrad I spent a couple of days in Moscow where I visited the IET and spoke to Alexei Altyntsev, the overall financial co-ordinator of the CEPRA projects and with Sergei Pridhodkov the co-ordinator of the Kaliningrad research team.

In Kaliningrad the following organisations were contacted and lengthy formal interviews were conducted. In nearly all instances a number of members of the organisation took part in the interviews. Translation was provided by the organisation being interviewed themselves or by Alexei Shekhovtsov. After the interview a discussion followed between Alexei and I in regards to what had been said. Formal interviews/consultations were conducted, with the following.

Three privates firm; an amber processing plant, a frozen food importer and an Austrian automotive parts producing subsidiary.

Four heads of governmental agencies were interviewed; the director of the Committee-Board of the Federal Program of Special Economic Zone development (Administration of Kaliningrad region) Mr. Mikhail Plyukhin, the head of the Investment activity Department of the Committee-Board of the Federal Program of Special Economic Zone development (Administration of Kaliningrad region) Svetlana Frolova, the head of the Committee of Economic Development and Trade of Kaliningrad region Administration, Mr. Vitaliy Zhdanov, and the ‘head’ and ‘vice head’ of the Baltic Fishery co-operative.

At the University of Kaliningrad, the Economic Geography Institute had organised workshop/ seminar for my visit. In total some 20 young people were present. Excellent direct translation was provided and a good discussion took place.

A full one day field trip was organised for Saturday, May 16th, 2002 to Bagationovsk on the Polish border and to Svetlogosk, the main recreational region on the Baltic. The trip also gave a good overview of the rural and small town landscape of the Oblast.

The CD-Rom, Region of Cooperation, Special Economic Zone in the Kaliningrad Region by “Media-Company XXI VEK”, 2002 was given to me and thoroughly analysed.

Interviews were conducted with the following basic questions in mind but it should also be stated that a deviation or expansion on their basic enquiry was more the norm then the exception.
Questions for a manager/owner of a firm in Kaliningrad

What is the nature of your business? How did you get your education/training to run this business?

When were you established? Why in Kaliningrad and how many employees do you have now?

Who and from where come your customers? How can you get new ones?

From where do you receive your raw materials (or support services)?

How are economic conditions for your firm now? Are you operating at capacity?

What are your firm’s economic prospects for the next 1-3 years?

To what extend do you need government help and support to run your business?

What are the major hurdles that government puts in your way to run your business efficiently?

Are these local/regional or central government constraints?

Do you make any use of the “Free Trade Status” of the Kaliningrad region in your business?

What do you think of the overall economic chances for development in the Kaliningrad Region over the next 5 years?

Question for local Kaliningrad governmental officials

What are the present economic development conditions like in Kaliningrad for old and new firms? Why?

Is there a difference between privately owned firms and firms owned by the government? Why?

What are the economic development prospects for Kaliningrad for the next 5 years in terms of real growth (decline)?

What are the basic reasons for this outlook?

Which of the following three entities might most help development in the future in the Kaliningrad Region, the local/regional governments, the Russian Federation or foreign investors/institutions?

If growth in economic development will take place in the future from which economic sector will it come, primary, secondary, tertiary or quaternary?

What are the strength and weakness of the Kaliningrad labour market?

Which are the major complaints of the Kaliningrad people about the conditions in Kaliningrad?

What are the advantages and the disadvantages of the “Free Trade Zone” of Kaliningrad?

If you had the final say in what development should take place in Kaliningrad what would you do and why?
These questions had been translated into Russian by Alexei and the organisation/people being interviewed received these questions at the start of the interview. The following represent the overall findings of the discussions.

**Overall Impressions and Main Concerns in Kaliningrad**

As was implied above, the originally proposed format of an interview, which would follow the order of the proposed question, had to be frequently abandoned during the interviews. In some instances the questions were irrelevant in other instances related issue were of greater concern. Also because of the small number of interviews the findings are presented under major headings only and not question by question.

1. **Financial problems in the Region**

   In nearly every interview, but especially in governmental offices, the financial difficulties of the region were brought to the foreground. Many related to transferring payments from the federal government to the region, city and municipal offices. These potential monies are meant to cover compulsory social expenditures, to improve the infrastructure of the region, and in some instances were to be used as matching funds in attracting investors. Over the years these transfer payments have not been met by the federal government, resulting in major disruptions in local programs especially since the ability of local governments to raise money locally is limited and legally restricted. The result was a rather depressing picture in the local landscape. Very poor infrastructure conditions like those of roads, public transport, public buildings, educational facilities (e.g. University), Airport, etc. are the norm. Most private entities in the landscape like housing did not fair much better, although a few, like cars, some churches and recreational properties did show substantial investment of capital.

   On the other hand private businesses did not complain about money issues. Loan applications if they could be backed by assets, seemed to encounter no problems in being granted by banks. Getting governmental grants for expansion by businesses, on the other hand, encountered major bureaucratic hurdles and required substantial administrative efforts. Consequently some firms gave up applying for government funds and withdraw their application to conserve energy.

   Since people in the Region have substantial interaction with Lithuania and Poland they naturally compare their conditions, during the interviews, with those of the adjacent countries. Clearly there is a substantial lower standard of living in
Kaliningrad when compared to these neighbours (http://www.hkhamb-ahk-kaliningrad.com/en/chap05.html). Wages for instance are substantially lower.

That socio-economic conditions were substantially poorer in Kaliningrad then in mainland Russia, was frequently brought up in the discussions. Wages and salaries are clearly below, as is its GDP per person as shown in the above tables. Furthermore, conditions varied substantially from year to year in the region which increased uncertainty.

2. EU expansion and its impact on the Kaliningrad Oblast

A major concern of the people in the region related to what would happen once Poland and Lithuania have joined the EU. Their well being would depend to a large extent on developments in these two countries. But to take advantage of their location certain political, socio-economic conditions would have to be met. The main problem for the Oblast, as seen from the local perspective is the issue of visa, transit conditions, trade restrictions, etc. both to the adjacent countries and to the main territory of Russia. In 2002 local residents did not need visas to enter Poland and Lithuania. With the admission of these two countries to the EU this could became no longer the case after 2004. Tighter border controls conditions would slowdown cross border interactions. Clearly, it depends on the relative ease of movement between the Oblast and the neighbouring countries. That Russians in Kaliningrad might need a visa to go to the main territory of their country by train or road, also brought out major consternations during the interviews. If this should happen, it certainly would certainly slow down substantially local economic ties to the Russian Federation. What further annoyed the local residents was the impression that the federal government (frequently only referred to as just Moscow) as well as the EU bureaucracy, seemed not to care about their forthcoming predicament. The posturing of these two power blocks over the local situations, yet seemingly not involving them, was leading to anger and frustration. An article in The Moscow Times by Peter Pomernzef clearly captured this frustration in Kaliningrad. However, my challenge to the people in the region that they (local governments or citizen groups) should make some proposals themselves to both bodies seem to be incomprehensible to them. Kaliningrad’s present and future condition of isolation was considered to be purely a Russian government international affair. That local suggestions might help the supper blocks out of a rigid/traditional response corner did not seem to enter their minds.

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5 “EU and Russia: Actors in Search of a Policy”, The Moscow Times, March 11, 2002
3. The status of the Kaliningrad Free Trade Zone

In 1991 Kaliningrad was given, by presidential decree, the status of a free trade zone. In 1996 a law was passed that basically substantiated this status. The main advantage to Kaliningrad is that goods can be imported duty free if some form of further manufacturing occurs in the region. But this additional processing has to result in a new or different product with a new product code and one which has a value added component of at least 15% in the electronic sector and 30% for all other manufactured goods. Such goods can then be exported or sold to the main Russian Federation or locally, duty free, except for customs handling fees.

Thus far the status has not created an economic boom in the region as acknowledge by the local government. "Despite various legal preparatory activities, the Special Economic Zone has not become "Hong Kong on the Baltic Sea" as it was lately called again by Mr Chernomyrdin, former prime minister". In fact it seemingly has only created envy in other regions of Russia. Manufacturing continues to decline in the region and the special zone status has had no effect on other sectors of the economy. Local manufacturers using local resources, like amber jewellery producers, seem to get no benefit from it either. One might even hypothesise that the bureaucracy involved (and potential corruption practices) in enforcing the special status may absorb any benefits that might flow to the region. Secondly, it should be noted that import/export duties on manufactured products have been declining rapidly world wide under the guidance of the WTO. When Russia joins the WTO it will have to meet these norms as well and a special status for one of its regions may only cause an administrative nightmare. Secondly, a minimum increase of 15% in the electronic and related industries and 30% for other goods is high in terms of local value added. Clearly in the present world of manufacturing outsourcing, such added value requirements are substantial especially if one adds the additional transport and transhipment cost to and from Kaliningrad to the final product. From personal information on visiting a television assembly plant in the free trade zone on the Mexican/US border in spring of 2001, it was found that their value-added percentage was only 5%.

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6 Media-Company XXI VEK, 2002
7 See the following web site http://www.hkhamb-ahk-kaliningrad.com/en/chap03.html
8 In a recent Transparency International Corruption Perception Index 2004 table on “Facts on Corruption” in the Journal of Development Policy and Practice, Vol. 1, No. 1, December, 2004 Russia is tied with seven other countries for the 90-97th rank of 146 counties. During my visit to Kaliningrad corruption problems were frequently mentioned as a major issue.
4. Future competition from the EU

An interesting concern emerged from the Kaliningrad business world which related to possible competition for their businesses from the EU should Kaliningrad, after an EU expansion into Poland and Lithuania, become an integrated economic part of the EU. Presently much of the economic activities in the region are oriented towards providing for the needs of the one million people in the Oblast. This means that the firms are relative small and inefficient. They could not possibly compete with the large conglomerates from the EU should these receive free market access to the Oblast. Yet there seems to be little opportunities for local firms to grow as their main major Russian market is too far away over rough roads and across international borders. Shipment by sea to St. Petersburg and then into the interior of Russia, seems not to be a viable alternative either for a modern economy.

Expansion into the EU market by Kaliningrad finns, in contrast, would have to overcome major import hurdles put in place over years by the EU. Secondly, most products and services by Russian entrepreneurs are still of substantial poorer quality then those available in the EU. Most Kaliningrad finns are under capitalised and not geared to supply a large and sophisticated market. In fact Russia has problems supplying its own population with reliable consumer goods. Hence building economies of scale by Kaliningrad finns seems highly unlikely. Integration of producers, suppliers and sellers into large-scale operations are not yet established in the new Russian economy. For the relative small Kaliningrad region this is even truer since “at present, about 68% of goods are imported”\(^9\). Most come from Europe and Russian proper.

5. Labour and working conditions in Kaliningrad

Over the last 10 years the labour market in Kaliningrad has changed dramatically. The military has reduced its presence in Kaliningrad substantially and with it have gone many of the supporting industries. The fishing and canning industry is down to a fraction of what it was earlier. Even the agricultural economy seems to have contracted greatly as the many abandoned fields in the rural areas of Kaliningrad Oblast showed. There is little hope that either sectors will come back. In addition overall employment in manufacturing is continuously declining\(^10\), similar to the world trend. Blue collar labour is therefore not in a good bargaining position to improve its economic well-being.


In the manufacturing sector getting paid on the basis of output (piecework) seems now to be the norm in the region. Training is frequently done on the job since no good job training institutes exists in the region. Capitalistic or market oriented thinking is based upon intuition and basic common logic. New entrepreneurs frequently have been trained in traditional academic disciplines, which stress reasoning abilities starting from reasonable assumptions. Such training is applied to the new situation of being a business person. According to one interviewee new employees are hired on the basis of brightness (as seen in the interview), commitment (how frequently has he/she applied for work) and youth. Advanced formal training plays a lower role except for additional language requirements (e.g. English, German, Lithuanian and Polish).

6. Mentality perspectives of Kaliningrad citizen regarding the EU and Russia

It was surprising to see that there were a number of perspectives of the local population regarding their place in Europe. The first view one could label a Centralist Perspective. Clearly many government officials, at different levels, have a strong, greater Russian perspective. They see Kaliningrad and themselves as an integral part of the Russian Federation. Any future status of the region should not challenge this association. In part, the Kaliningrad territory is seen as a reward for the many lives lost in Russia during WWII. Just because the region is now isolated and may become more remote in the future, does not challenge this viewpoint. People with these views also look to Moscow for all directions and support. In Canada one would label them clearly federalists first and foremost.

A second perspective may be labelled a Regional Russian View. The people see themselves as part of the Kaliningrad region but which in turn is part of greater Russia. They in part look for local dynamics to get them going. Again in Canada these people would put their province first except on travelling abroad when they would have a Canadian flag on their knapsack.

The third group is one with a European Kaliningrad Perspective. These people see themselves as Europeans who happen to live in Kaliningrad Oblast, which is one of the 89 regions of Russia. People with this view usually have grown up in Kaliningrad or have moved there to make a living and have, since 1990, interacted mainly with their European neighbours. Few have visited other regions of Russia. They see European television programs, have frequently traveled to Poland and Lithuania and are quite familiar with West European views. For them the eastward expansion of the EU will mentally contain them as well as Poland and Lithuania. They view themselves first as Europeans, especially North Europeans but normally not Russians. They are not against Russia but their geographic location and their
world interaction space is Central Europe, which produces in them a European image of themselves. Some are confident that an eastward expansion of the EU will impose privileges and conditions on them similar to those their neighbouring countries will receive. It may be under some special status regulation but the exact nature of this status is not that important. The important thing is that they will be part of the greater EU. Much of the private business world, owners and employees are part of it. People with such attitudes may be required to help formulate and establish the special relationship of Kaliningrad with the EU and mainland Russia in the future. A close Canadian counterpart viewpoint could come from a person living in a greater city in Canada, who is working for an international firm and basically sees his/her business turf as North America. He/she watches North American sports, news, movies and reads books and magazines produced for the North American market – both Canada and the USA. He/she has many friends and relatives that work in either the USA or in Canada and could have gone to either an American or Canadian university. In a sense he/she is part of a global economy. They may see themselves as a global citizen.

7. Other comments

In general, in 2002, there was an attitude of resignation in governmental institutions towards what Moscow may have in store for them. In the business world, on the other hand, there existed an even ‘cocky’ perspective. No overall desire to leave the region could be observed among them. It is this basic local commitment that probably will pull the region through its difficulties and uncertainties in the near future.

8. Summary and conclusion from the interviews

The trip to the Kaliningrad Oblast added substantial local knowledge of the conditions beyond that acquired from theoretical and empirical conditions for this peripheral Oblast of Russia. A large part of the local frustration was clearly related to the dismantling of a highly centralised and planed economy and the emergence of the new local oriented market economy. New conceptual development initiatives can come, in my view, only from the local European Kaliningrad Perspective. Unfortunately, any suggestions for developments that go counter to the Centralist Perspective (Moscow) may be challenged. Local government authorities with their Regional Russian View are not clear in their objectives and policies for development as they depend on Moscow for funds but are elected by the local population to
help with local development. This dual accountability leads to frustrations by the
new local entrepreneurial class as well as the local population. It has the power
relationships of modern colonialism. No wonder many Kaliningrad individuals
want as little of such government leadership as possible.

9. Possible Development Opportunities in Kaliningrad

The above review of theoretical and actual conditions in Kaliningrad
exemplifies the well-known characteristics of core-periphery relationships of two
or more regions\(^1\). Kaliningrad, unlike main land Russia, does not have the relevant,
wealth producing, natural resources. The presence of amber, although abundant,
is not enough. But what it does have is tremendous location advantages compared
to the rest of Russia. It is located near the heart of northern Europe and certainly
on the main pathway form Denmark through northern Germany and onto to Poland,
the Baltic States, Finland and Sweden. In fact it is located on the conceptual Baltic
Main Street highway that circulates the Baltic (Figure 6). In fact one could consider
it as the modern hanseatic transport link of the Baltic. Kaliningrad needs to take
advantage of this fact. Much commerce and people will want to path through its
territory on trucks, buses and cars that need to go to destinations all around the
Baltic. It must be on the forefront on promoting the awareness of such a Baltic
route for commerce as well as tourist reasons. And it needs to make sure this
highway passes through the Kaliningrad Oblast and has umpteen service, retail
and entertainment and even light manufacturing malls located on it. In other words
Kaliningrad needs to set up a number of specialized "malls" that would entice
potential businesses to stop in or come to Kaliningrad. Its cheap labour, energy
and living costs should give it an absolute comparative advantage over other EU
providers. Hence building and a good highway through Kaliningrad Oblast is the
first and foremost advantage. It is imperative that such a route does not go around
Kaliningrad!

In addition Kaliningrad is in the flight path of a number of European airlines
and is located not far from such major hubs as Frankfurt, Hamburg, London,
Copenhagen, Stockholm and Helsinki. It clearly needs to set up an aircraft service
sector to cater to the potential demand of servicing aircraft. Having an extended
duty free at such an aircraft service base may further enhance the attractiveness of
such trips to Kaliningrad.

In order to attract more investment from abroad the Oblast also needs to
change its land ownership laws. Selling to outsiders or providing long leases (99
\(^1\) See for instant D. J. A. Douglas' article "Community Economic Development in Rural Canada: A
years) could be one approach. Only then will outside capital view things as more stable and potentially attractive in the region. Land and buildings once in place cannot be moved. They will continue to be part and parcel of the physical assets of the territory even if owned in part by outsiders. In a sense they will always be part of the Russian territory. The buying of land and buildings assets means financial flows into the region. This money requires financial returns and hence will be used productively which means further investment in the region. Clearly the region has to create a positive cumulative causation cycle in the economy for its own and its citizen future well being.

Another possibility would be to create a mobile temporary labour pool (short term work employment agency) for Europe. If needed a car or bus full of labourers could go on weekly job task to Europe and return for the weekend. Seasonal work in the agricultural sector as well as in the construction and hospitality sectors may again give local Kaliningrad labour an advantage.

The region should expand its Free Trade Zone concepts to include industrial services. It should especially encourage the remanufacturing industry of machines of all kind, aircraft, trucks, ships, locomotive, etc. for it probably has great labour skills in these areas from its earlier USSR era.

Kaliningrad should consider making English a second official language. Besides providing educated trades with good trade and language abilities for the above mentioned opportunities, it could create education centres that would attract students from all over the world. Its comparative cost advantage would especially appeal to students from the developing world.

Another possibility relates to tourism both short and long term. The Oblast should consider leasing many of the rural not used farms and small town houses to people from the EU on a long term basis. In Canada recreational places can be leased from a few years up to 99 years. The longer the lease the higher is the possibility that foreigners will invest substantial sums in upgrading, reconstruction and even building facilities, in every case creating local demand.

In order to enhance such tourist potential, the Kaliningrad region needs to abolish all visa requirements for citizen from EU states.

It will not be easy to create viable economic development opportunities for Kaliningrad. But its location advantages in Europe are substantial! In addition for any development strategy to be implemented and to succeed, it will need to adopt an overall European Kaliningrad Perspective and that may be the most difficult first step, for a centralist state like Russia, even though in name it is a federation.
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