THE RUSSIAN FEDERATION
THE IMPACT OF TRAVEL & TOURISM ON JOBS AND THE ECONOMY
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February 2006
WTTC is delighted to present this report, which provides the most comprehensive analysis of the Tourism Satellite Account for the Russian Federation ever undertaken.

Researched by WTTC, together with our partners Oxford Economic Forecasting, this report quantifies all aspects of Travel & Tourism Demand, from personal consumption to business purchases, capital investment, government spending and exports. It then translates this information into economic concepts of production, such as gross domestic product (GDP) and employment, which can be compared with other industries and the economy as a whole to provide credible statistical information that will assist in policy- and business decision-making.

Although economic growth since the late 1990s has been driven by energy exports, it is clear that sectors such as Travel & Tourism will have an increasingly important role to play in a diversified economy. Baseline forecasts for the Russian Federation’s Travel & Tourism are generally positive. In 2006, the wider Travel & Tourism Economy is expected to contribute 7.8 per cent of the country’s GDP and should account for 4.5 million jobs, representing 6.6 per cent of total employment. Furthermore, over the next ten years, Travel & Tourism in Russia is forecast to achieve annualized real growth of 6.4 per cent, in terms of GDP, compared with only 3.1 per cent in the EU, taking the share of Travel & Tourism GDP to 9.1 per cent in 2016.

Nevertheless, there is no room for complacency. As outlined in the Travel & Tourism Overview and Policy Framework sections of this report, significant challenges need to be overcome if Travel & Tourism’s full economic and social potential is to be realized in the Russian Federation. Recognition of the industry’s importance from the highest levels of government and throughout the population, combined with long-term planning at the national and regional levels and adequate funding for tourism development, marketing and promotions, are imperative moving forwards. The establishment in 2004 of the Federal Agency for Tourism reporting directly to the Prime Minister is an important step in the right direction.

The report also sets out WTTC’s recommendations on policies that we believe will help optimize the potential benefits of Travel & Tourism in the Russian Federation – for business and local communities, as well as for the environment. As long as certain factors are assured, Russia’s Travel & Tourism could well exceed baseline forecasts. WTTC stands ready to support the adoption and implementation of these policies.

Jean-Claude Baumgarten
President, World Travel & Tourism Council
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EXECUTIVE SUMMARY

THE RUSSIAN FEDERATION HAS THE POTENTIAL TO BECOME ONE OF THE WORLD’S LEADING TRAVEL & TOURISM ECONOMIES OVER THE NEXT DECADE. THIS VAST COUNTRY HAS AN UNPARALLELED RANGE OF NATURAL ATTRACTIONS, AND ITS TURBULENT HISTORY AND RICH CULTURAL AND ETHNIC DIVERSITY HAVE LONG FASCINATED THE OUTSIDE WORLD – EVEN MORE SO BECAUSE OF ITS MANY YEARS HIDDEN BEHIND THE IRON CURTAIN, SHROUDED IN MYSTERY.

Yet, since the collapse of the Soviet Union, the painful transition from a planned to a market-based economy has taken its toll on Travel & Tourism infrastructure, transport, communications and even such areas as statistical data collection and measurement. Despite enormous progress – not least Russia’s vastly improved economy and greater political stability – the country faces innumerable challenges that need to be addressed before it can hope to achieve its full Travel & Tourism potential.

One might of course question why Russia even needs Travel & Tourism at a time when the national economy is booming and prospects seem equally bullish. Although growth has been fuelled largely by energy exports – and this type of growth makes the national economy dangerously dependent on oil and natural gas exports – Russia does account for 5-6 per cent of the world’s oil reserves and one third of global natural gas reserves. And it is also one of the largest coal producers in the world. Moreover, the government’s stabilization fund – a rainy-day storage facility for windfall oil receipts that came into effect on 1 January 2004, and which currently stands at US$44 billion – can help to offset the oil market’s volatility, if needed.

However, the government’s decision in 2005 to develop special economic zones (SEZs) to help diversify the economy away from oil towards innovation sectors is a clear sign of its recognition that dependence on oil exports is not healthy in the long term. The first SEZs have been earmarked for technology and manufacturing, but a number of SEZs for tourism and leisure will be announced during 2006. Tax breaks and other benefits are offered to companies operating in the zones.

There are other positive signs, albeit modest for the time being, of an increased awareness on the part of the Russian Government of Travel & Tourism’s economic importance. These include the establishment, in November 2004, of the Federal Agency for Tourism (Rosturizm), whose director reports directly to Prime Minister.

There is no doubt, either, that Rosturizm fully recognizes the industry’s potential for diversification of the Russian economy and the creation of jobs, as well as having clear ideas as to how to address the weaknesses and inefficiencies of the system and reduce some of the many barriers to growth.

The next step is for government at the highest levels to make Travel & Tourism a strategic development priority and to factor it into mainstream policy- and decision-making. Federal funding for Travel & Tourism also needs to be increased, in particular for marketing and promotion.

Although the baseline forecasts developed by WTTC and its research partner, Oxford Economic Forecasting (OEF), are generally positive, there is no room for complacency. The last few years have demonstrated dramatically that the wider benefits of Travel & Tourism can no longer be left to chance. If Russia’s Travel & Tourism is to make its full contribution to job creation and wealth generation in the coming years, government must take the lead in unlocking the industry’s potential.
By recognizing Travel & Tourism’s valuable flow-through effects for all sectors of the economy and the population – and having the sense of leadership to act on that recognition – the Russian Government can help ensure benefits not only for those who travel, but also for the local communities they visit, and for their respective natural, social and cultural environments.

The responsibility does not lie only with government, either. In line with the recommendations drawn up in WTTC’s Blueprint for New Tourism, all stakeholders must assume their share of responsibility for the sustainable development of the country’s Travel & Tourism. What Russia needs is a new Travel & Tourism vision and strategy involving public–private sector partnership – between all levels and sectors of federal and local government, as well as between government and the Travel & Tourism industry, academia and other stakeholders. Only in this way can today’s challenges be turned into opportunities.

In order to address these challenges and achieve the vision, three fundamental conditions are required:

- The Russian Government must recognize Travel & Tourism as a top priority;
- Business must balance economics with people, culture and environment; and
- All stakeholders must share the pursuit of long-term growth and prosperity.

THE BASELINE FORECASTS: A REALITY CHECK

Despite some reservations, the baseline forecasts for Russia’s Travel & Tourism developed by WTTC/OEF are generally positive.

In 2006, the wider Travel & Tourism Economy is expected to contribute 7.8 per cent of Russia’s GDP – as against 11.8 per cent for Travel & Tourism in the European Union – and it should account for 4.5 million jobs, representing 6.6 per cent of total employment (11.8 per cent in the EU).

Over the next ten years, Travel & Tourism in Russia is forecast to achieve annualized real growth of 6.4 per cent, in terms of GDP, compared with only 3.1 per cent in the EU, taking the share of Travel & Tourism GDP in Russia to 9.1 per cent in 2016.

Nevertheless, the prognosis for employment is much less bullish. The share of Travel & Tourism Economy jobs will increase by a modest 1.5 per cent per annum, according to WTTC/OEF – only the same as in the developed EU markets – increasing their share by just 1.1 percentage points over the next ten years to 7.7 per cent in 2016. This compares with a 13.0 per cent share for Travel & Tourism in the EU in 2016.

Moreover, Travel & Tourism Industry GDP and employment – jobs directly within the industry – are projected at a low 1.5 per cent and 1.3 per cent respectively for 2006 and 2016. In terms of jobs in particular, this is clearly far too low to assure the level of employment required to meet the WTTC/OEF annual growth forecasts for total Travel & Tourism Demand of 6.5 per cent over the next decade.

Similarly, government expenditures on Travel & Tourism, which are currently estimated at just 2.7 per cent of total government expenditures – a share that is not expected to increase over the next ten years – will prove sorely inadequate to service the needs of a fast growing industry.

If optimistic forecasts for capital investment prove accurate, it is even more critical for government to allocate sufficient funding for support services to developers, travel companies, visitors and the public at large.
REALIZING THE POTENTIAL

WHILE THE BASELINE FORECASTS FOR THE RUSSIAN FEDERATION’S TRAVEL & TOURISM ARE GENERALLY POSITIVE – MORE POSITIVE IN SOME AREAS, IN FACT, THAN ANECDOTAL EVIDENCE MIGHT SUGGEST – THEY NONETHELESS HIGHLIGHT A NUMBER OF WEAKNESSES THAT COULD HINDER TRAVEL & TOURISM’S GROWTH. THESE MAY ALSO PREVENT RUSSIA FROM ATTAINING ITS TRUE TRAVEL & TOURISM POTENTIAL IN THE MEDIUM TO LONGER TERM.

At the same time, greater co-operation between all leading policy-makers, and between government and the private sector, as well as effective management of tourism growth, could help Russia do even better than the current forecasts suggest. This would help maximize the benefits and spread them equitably to all parts of the country and across all levels of the population.

The additional measures recommended in this report are intended to set the stage to help ensure the larger rewards that Travel & Tourism can bring to Russia over the short, medium and longer term. The following highlights the key areas in which government intervention is needed.

RAISING AWARENESS
Russia has the potential to become one of the world’s leading Travel & Tourism economies.

So greater priority needs to be accorded to Travel & Tourism by government, factoring it into mainstream policies and communicating the strategic importance of the industry to all levels of government, industry and local communities.

An industrial image campaign will help ensure that all public and private stakeholders recognize Travel & Tourism’s full impact across the national economy – not just on restaurants and cafes, or retail businesses, but also on construction, real estate and other sectors of the economy.

Most importantly, stakeholders should be made aware of Travel & Tourism’s untapped potential and of the spin-off benefits it can provide, which filter down through all levels of the community.

If it is to be successful, the industrial image campaign needs to be adequately funded, as does the Federal Agency for Tourism’s ongoing work to promote Travel & Tourism and drive the industry forwards.

TOURISM PLANNING
Long-term planning at the national level is a prerequisite for the successful development of Travel & Tourism in Russia since the industry is fragile and likely to be adversely affected by short-term political considerations.

The elaboration of a new action programme for tourism development, which is due to be completed by Rosturizm in 2006, should be incorporated into a formal National Tourism Policy, which should be communicated as widely as possible in order to ensure greater support and buy-in from all stakeholders.

The government should also initiate a more cohesive and co-operative approach to future tourism planning and development, involving all levels of government – federal and regional – the private sector and local communities.

The identification of special economic zones for tourism should be expedited as quickly as possible, so they help to guide the development of other regional plans and to instil confidence in potential investors as to the country’s tourism growth potential.
MARKETING & PROMOTION
Experience has shown that demand for any tourism destination grows sharply if marketing and promotions are well funded and effective.

A competitive, sustained promotional campaign in traditional and emerging foreign markets is critical for Russia, in order to clarify and enhance the country’s image as a tourism destination and generate new demand.

Domestic tourism promotion is also recommended to highlight the importance to local Russians of Travel & Tourism’s economic importance and its employment generation potential.

Considerable investment needs to be made to develop and promote the brand ‘Russia’, highlighting the country’s rich cultural and natural attractions.

This would ideally involve the appointment of marketing or PR representatives in key source countries, who could ensure a sustained promotional campaign throughout the year, rather than just at isolated Travel & Tourism trade fairs and other special events.

INDUSTRY MEASUREMENT
The transition from a centrally planned to a market-based economy severely disrupted the collection and analysis of data in Russia. In addition, because of tax avoidance, much private sector activity reportedly goes unrecorded.

So official statistics on trends in Russia’s Travel & Tourism are unreliable and can, in some cases, be confusing.

In order to plan ahead better and anticipate necessary changes to tourism supply, it is essential to monitor trends in past and current Travel & Tourism demand. This will help identify threats to growth, as well as new opportunities.

This new Tourism Satellite Account (TSA), developed by WTTC and OEF for Russia, provides a significant tool for planning and policy development. Updating the TSA on an annual basis will help ensure that adequate data is available to factor Travel & Tourism into economic and employment strategies.

HUMAN RESOURCES
Research by WTTC/OEF shows that, in 2006, Travel & Tourism in Russia will account for some 4.5 million jobs – around 863,000 directly within the industry and a further 3.6 million in sectors linked to Travel & Tourism, such as real estate, construction and retail.

For a country the size of Russia, which has the potential to increase Travel & Tourism Demand by 6.5 per cent a year over the next ten years, the WTTC/OEF employment growth forecasts are extremely modest.

Travel & Tourism Industry employment is expected to increase by only 0.3 per cent annually between 2006 and 2016, while Travel & Tourism Economy employment will rise by a projected 1.5 per cent. This low level of growth will simply not be sufficient to service the needs of the industry going forwards.

The Russian Government needs to work with the private sector and academia to develop the quality human capital required for Travel & Tourism growth and promote a positive image of the Travel & Tourism industry as a provider of jobs and careers.

Compensation also needs to be brought in line with that in other sectors of the economy, so that the value of the top-quality employees is not undermined.

INFRASTRUCTURE
Russia’s Travel & Tourism infrastructure has suffered over the past 14 years from neglect on the part of government and a lack of confidence on the part of both domestic and foreign investors.

Although investor confidence has picked up quite strongly since 2005, investment in Travel & Tourism projects has been lagging behind that of other sectors.

Potential investors need to be reassured that adequate investment is being made to improve basic infrastructure – such as airports, roads, communications, water and electricity supply. The Russian Government is on the right track but it needs to speed up its modernization programmes for airports, the railways and port facilities.

Quality infrastructure is essential to diversify the product base, remove bottlenecks, ensure good
service and distribute the benefits of tourism flows around the country. It is not only a question of planning for increased numbers of visitors, but also of making sure that the patterns of flow do not affect the natural or built heritage, nor run counter to local interests.

To stimulate and speed up privatization in the future, the government should consider setting up a tourism investment facilitation centre. Linked to the Federal Agency for Tourism, but also working in close co-operation with other relevant government ministries or agencies, this would act as a one-stop shop for private investors.

REGIONAL DEVELOPMENT
The Russian Government’s medium-to longer-term goal should be to ensure that the benefits of Travel & Tourism are spread as equitably as possible across all regions and to all levels of the population.

This can reduce disparities between urban and rural areas which, in turn, could bring improvements to Russians’ quality of life and well-being.

Opening up the regions will require increased investment in infrastructure – roads, railways and airports – as well as modernization and expansion of the hotel plant, plus the development of new attractions and facilities such as tourist information centres.

Most importantly, if Travel & Tourism is to be successful as a tool for rural development, it is critical to ensure the buy-in of those communities in which it is based.

BARRIERS TO GROWTH
Russia’s Travel & Tourism environment is still plagued with different examples of bureaucracy that require patience for anyone working in, or dealing with, Russia.

In addition to creating a competitive business environment that stimulates and facilitates investment, healthy Travel & Tourism will depend on an operating environment that is free of such bureaucracy and other barriers to growth.

The Russian Government must step up its financial sector reforms, introduce more intelligent taxation and address some of the serious issues hindering the industry’s development, such as excessively complicated visa requirements.

Measures also need to be stepped up to deal with increasing incidents of crime, which are a source of major complaints by tourists. Just as seriously, potential investors in Russia’s Travel & Tourism industry risk turning their backs on the country unless they are assured of a safe and secure operating environment.

BUSINESS ENVIRONMENT
Travel & Tourism growth can be inhibited by local market conditions – from incoherence in planning to unfair taxation, inadequate banking and financial services, uncertainties over land ownership issues and land lease regulations, and a lack of transparency in decision-making processes.

If Russia is to stimulate and sustain business and investor confidence, the Russian Government must try to create a competitive business environment that is conducive to investment.

This means addressing the different problems and weaknesses in the system, providing adequate state guarantees and incentives for investment, and ensuring that fiscal policies such as taxation are not harmful to investment.

PRODUCT & MARKET DIVERSIFICATION
Only 20 per cent of Russia’s vast land benefits from tourism, and 80 per cent of foreign tourists visit only Moscow and/or St Petersburg, either for business purposes or for city and/or cultural tourism.

It is clearly in the interests of both the public and private sectors – not to mention local communities and other stakeholders – to diversify Russia’s tourism product and market mix and try to tap new markets.

Diversification will help minimize the risk of over-dependence on a few key markets, as well as helping to reduce seasonality, spreading tourism demand more equitably throughout the year and away from Moscow and St Petersburg. In the longer
term, it could also help avoid excessive strains on valuable natural resources.

Sectors offering good growth potential include incentive travel, sea and river cruises, cultural tourism and city breaks – as long as visas do not remain a major deterrent – and all kinds of sports and adventure travel.

**TECHNOLOGY**

Adaptation to the ‘digital economy’ is essential for companies involved in all areas of Travel & Tourism to become and remain competitive.

An increasing share of Travel & Tourism operations – and virtually all distribution and sales transactions – flow through telecommunications circuits. Where telecommunications are monopoly controlled, there are often restrictions on access, high costs and unreasonable operating conditions. This in turn limits the potential of market-oriented expansion of Travel & Tourism, with negative impacts domestically and internationally in terms of cost, operational efficiency and customer service.

In today’s increasingly competitive global marketplace, there is also a real need for a strong national leadership branding. This will require a co-ordinated approach to internet marketing and distribution to optimize Russia’s visibility and image.

The Federal Agency for Tourism should take the lead in developing a user-friendly English-language website for potential foreign visitors to Russia. This will help improve the distribution of Russia’s tourism products – both through the travel trade and direct to consumers – and enhance the country’s image and the Russia brand generally in key markets.

**ECONOMIC VS THE ENVIRONMENT**

The Russian Government last year signed the Kyoto Protocol, but environmental problems remain one of the country’s major challenges, and one which no Kyoto agreement is likely to resolve in the short or medium term.

While Travel & Tourism is not currently directly affected by the widespread environmental degradation, the country’s future tourism success may depend on a rapid improvement of the situation, plus a visible effort on the part of government and the private sector to combat the problems.

It is critical for government to take the lead in promoting responsibility in natural, social and cultural environments and ensuring that business balances its commercial interests with these priorities.

The Russian Government has a special responsibility to ensure the sustainability of key tourism assets, such as the natural and cultural resources that preserve the attractiveness of the country and the competitiveness of tourism companies.
ECONOMIC IMPACT

IN 2006, THE RUSSIAN FEDERATION'S TRAVEL & TOURISM IS EXPECTED TO GENERATE RB2,731.5 BN (US$94.8 BN) OF ECONOMIC ACTIVITY (TOTAL DEMAND). THE INDUSTRY'S DIRECT IMPACT INCLUDES:

**863,162**

jobs representing 1.3% of total EMPLOYMENT.

**Rb357.1 bn**

(US$12.4 bn) of GROSS DOMESTIC PRODUCT (GDP) equivalent to 1.5% of total GDP.

HOWEVER, SINCE TRAVEL & TOURISM TOUCHES ALL SECTORS OF THE ECONOMY, ITS REAL IMPACT IS EVEN GREATER. THE RUSSIAN FEDERATION'S TRAVEL & TOURISM ECONOMY DIRECTLY AND INDIRECTLY ACCOUNTS FOR:

**4,515,170**

jobs representing 6.6% of total EMPLOYMENT.

**Rb1,910.7 bn**

(US$66.3 bn) of GROSS DOMESTIC PRODUCT (GDP) equivalent to 7.8% of total GDP.

**Rb 593.4 bn**

(US$20.6 bn) of EXPORTS, SERVICES & MERCHANDISE or 6.7% of total Exports.

**Rb 607.1 bn**

(US$21.1 bn) of CAPITAL INVESTMENT or 12.1% of total Investment.

**Rb 104.4 bn**

(US$3.6 bn) of GOVERNMENT EXPENDITURES or a 2.7% share.
GROWTH

In 2006 travel & tourism in the Russian Federation is forecast to see real growth of 1.9% in total travel & tourism demand to Rb2,731.5 bn (US$94.8 bn) and

10.0% in travel & tourism industry GDP to Rb357.1 bn (US$12.4 bn) for the industry directly and 0.4% to Rb1,910.7 bn (US$66.3 bn) for the Travel & Tourism Economy overall (direct and indirect expenditures).

4.8% in travel & tourism industry employment (direct impact only), 863,162 jobs, and -4.1% to 4,515,170 jobs in the Travel & Tourism Economy overall (direct and indirect).

Over the next ten years, the Russian Federation’s travel & tourism is expected to achieve annualized real growth of:

6.5% in total travel & tourism demand, to Rb9,137.7 bn (US$177.6 bn) in 2016.

5.1% in total travel & tourism GDP, to Rb1,049.4 bn (US$20.4 bn) in 2016 for the industry directly and to Rb6,319.0 bn (US$122.8 bn) for the Travel & Tourism Economy overall.

0.3% in travel & tourism employment, to 891,031 jobs directly in the industry, and 1.5% to 5,231,827 jobs in the Travel & Tourism Economy overall in 2016.

7.5% in visitor exports, rising to Rb918.0 bn (US$17.8 bn) by 2016.

9.3% in terms of capital investment, increasing to Rb2,621.1 bn (US$51.0 bn) in 2016.

3.2% in terms of government expenditures to Rb256.2 bn (US$5.0 bn) in 2016.
THE RUSSIAN FEDERATION’S TRAVEL & TOURISM
OVERVIEW OF CURRENT TRENDS AND DEVELOPMENTS

POTENTIALLY A WORLD-CLASS DESTINATION
A wealth of attractions…

“A riddle wrapped in a mystery inside an enigma” was the description coined by Sir Winston Churchill in 1939 when speaking of Russia, or the Soviet Union as it then was. And, if anything, the country has become even more mysterious after so many years hidden behind the Iron Curtain.

Such mystery always fascinates, of course, and since the collapse of the Soviet Union in 1991, curious tourists have ventured into the country in an effort to understand this vast multi-ethnic and geographically diverse country.

With a population of just under 144 million, comprising as many as 160 different nationalities, the Russian Federation – to use its official name – covers an area of more than 17 million km², and no less than eleven time zones. Train journeys in the country are measured in days rather than hours.

Russia offers tourists an amazing diversity of scenery and climates, plus a turbulent and fascinating history and a rich cultural heritage – from its art and music, to its literature and religion. Yet, its appeal also stems from the fact that, alongside this pre-Revolutionary cultural richness is the explosive energy of the new, unique culture that has emerged over the past 15 years, and which has made both Moscow and St Peters burg such vibrant modern cities.

…but that remain largely unexplored

Given its indisputable attractions as a tourism destination, Russia is still a long way from reaching its potential. In fact, the country has lost share over the past five years, in terms of international tourist arrivals, and 2005 is expected to have been one of the worst years for the country’s inbound tourism since before the unravelling of the Soviet Union.

The disappointing performance can be attributed to many different factors – all of which are addressed in this report – and it is fair to note that the decline has largely been from the Commonwealth of Independent States (CIS). But last year, reportedly, Russia also saw a sharp downturn from some important Western sources.
High prices are a major deterrent to growth – but not the only one.

From a tourist's point of view, the main complaints about their tourism experience in, or getting to, Russia concern the country's infamous red tape, the cost of a visa – and the time required to obtain one – the surly service, and fears over crime and terrorist attacks. Also a major deterrent is the skyrocketing cost of visiting Russia's top two tourism destinations, Moscow and St Petersburg. The price of a week-long visit to either city has almost tripled in the past four years and is now probably double what the equivalent stay would be in a city like Prague or Budapest.

As far as the rest of the country is concerned, price is also one of the factors discouraging tourism, because of the long distances involved, but a greater problem is lack of consistency in terms of product quality. This is due in no small part to poorly developed and/or maintained infrastructure – roads and transport infrastructure, as well as a shortage of suitable accommodation, and a lack of tourist facilities and services, such as tourist information centres.

All this goes some way to explaining why outbound travel has performed so much better than inbound or even domestic tourism since the birth of the Russian Federation.

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OVERALL TRENDS
A lack of reliable data on domestic tourism

Very little reliable data is available on domestic travel, but trip volume is variously estimated at between 75-100 million trips a year. Of these, less than 20 per cent involve air transport. The share of Russians taking an annual domestic holiday is probably only about 20 per cent, although anecdotal evidence suggests it may have picked up slightly since 2003. This is attributed to improved economic stability and living standards.

However, domestic trip volume is still well down on the numbers achieved during the Soviet era. In those days, social tourism was widespread. The government had a whole raft of economic measures designed to stimulate holiday taking and trade unions provided subsidies for employees who could not afford to go on holiday. Today, that kind of support is almost non-existent, except for some government sponsorship of summer camps for children.

There has also been a huge increase in the cost of domestic travel over the past few years – airline ticket prices increased by almost 20 per cent in 2004, according to the Russian Union of Travel Industry (RUTI) for the second or third consecutive year. And the cost of rail travel rose by over 30 per cent. As a result, more and more Russians who want to go on holiday are considering trips abroad.

Outbound travel outperforms inbound tourism

The following charts highlight the growth trends in Russia's inbound and outbound travel since the beginning of the decade. While inbound arrivals have fallen by more than 2 per cent per annum, with preliminary estimates for 2005 pointing to a 15 per cent annual decline, outbound trip volume has risen by an estimated 9 per cent a year. And the annual percentage growth for the last two years has been in double digits.

Inbound arrivals totalled 22 million in 2004. However, this figure included same-day visits and arrivals by a whole range of categories of travellers not officially termed 'tourists', such as airline crew, truck drivers and foreigners on long-term contracts to work in the country. The official outbound trip total, which is also inflated by same-day trips and Russians travelling for non-tourism purposes, was 24.5 million.

The growth in international tourism receipts and spending (visitor exports and imports minus spending on transport) has been more impressive, although real trends are distorted by exchange rate fluctuations. Receipts have risen by less than 9 per cent a year, while spending by Russian travellers abroad has increased by an annual average of 15 per cent.

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Sources: Russia’s State Statistics Committee (Goskomstat); World Tourism Organization (UNWTO)
that some 2,500 exhibitions were held in the country in 2003. These covered a total exhibition space of more than 2.8 million m² and attracted over 230,000 visitors – domestic and international. IUEF members accounted for around 45-50 per cent of the total exhibitions and probably a higher number of visitors and exhibitors.

INDIVIDUAL MARKETS
Non-CIS markets have generally shown good growth...

In 2004, the major sources of arrivals, excluding the CIS markets, were Poland, Finland, Lithuania, China and Germany which, between them, generated 21 per cent of the total arrivals count. As might be imagined, visits from neighbouring countries were primarily same-day shopping trips, or for cross-border shuttle trading.

Performances were very mixed across the different markets. However, the overall results highlight the fact that, with the exception of Poland and Finland – in first and second positions in the ranking – all key non-CIS sources achieved healthy increases in 2004. Non-CIS arrivals volume overall was 8.7 million, up 6 per cent on 2003. For some markets, 2003 arrivals were down on 2002, but this was attributed to external events such as worldwide terrorism and the Iraq war, which dampened tourism demand generally, not just to Russia.

MICE BUSINESS
Incentive travel is reported to be growing...

Although some hotels claim that they receive regular incentive travel groups – St Petersburg, for example, attracts companies wishing to reward their high-fliers with lavish entertainment in historic palaces – virtually no data is available to substantiate reported growth trends. The sector is still in its infancy but is certainly one to be watched closely in the future.

...as is the number of conferences and exhibitions

There are around 250 professional Russian exhibition organizers within Russia – 55 of whom, or 22 per cent, are members of the International Union of Exhibitions and Fairs (IUEF). The latest data available suggests

INBOUND TOURISM
PURPOSE OF TRIP
The statistics undermine business tourism’s importance

Of the total 22 million arrivals, as many as 65 per cent are classified under the heading ‘other private’ visits. This implies visits to friends and/or relations (VFR travel) but also same-day trips for various purposes such as shuttle trading and shopping. It is this category that has shown the sharpest decline in recent years, and particularly from CIS sources.

Holidays and business trips generate very modest shares of the official total, or 13 per cent and 12 per cent respectively, with the balance coming from visits by service staff, airline crew, etc – ie non-tourists, according to World Tourism Organization (UNWTO) definitions.

If arrivals from the CIS are excluded from the count, the breakdown by purpose of trip is rather different. ‘Other private’ visits still dominate, but holidays and business visits account for a much higher 30 per cent and 24 per cent shares respectively. The business share is almost certainly understated as well, since many travellers to Russia find it easier and cheaper to apply for a ‘tourist’ rather than a business visa. This trend is confirmed by hotel statistics.

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The best growth in 2004 for Russia came from Estonia – one of the three Baltic states, with Latvia and Lithuania, that were formerly part of the Soviet Union, and many of whose inhabitants are either Russian or still have close links with Russia. But, in addition, increases of over 20 per cent were achieved by the UK, Turkey, Spain, Austria and Switzerland. And other European markets also registered more modest
double-digit increases, reflecting the fact that there is growing interest in Russia as a tourism destination from the Western world, whether for business or leisure.

...until 2005

Arrivals data for 2005 is still incomplete. In fact, data on individual markets’ performance is only available for holiday/leisure visits, and only for the first six months of the year. But, coupled with anecdotal evidence from RUTI and other industry sources, the data shows clearly that demand took a dive last year, for many of the reasons already cited.

Many of Russia’s major sources, including the four leading holiday/leisure markets – Germany, Poland, China, Finland and Latvia – recorded declines from January through June 2005. In contrast, there were double-digit increases from the UK, Estonia and the USA, and arrivals from Italy also achieved healthy growth.

Visa-free travel for Chinese should stimulate demand

China, down nearly 21 per cent over the same period in 2004, was particularly disappointing, although preliminary estimates for the second half of the year look much better – due to a reciprocal agreement signed in mid-2005 between Russia and China for visa-free travel between the two countries. The agreement, which followed China’s granting of approved destination status (ADS) for Russia in 2003, means that Chinese tour groups with a minimum of five participants can now travel visa-free to any city in Russia that is open to foreigners.

<table>
<thead>
<tr>
<th>Leading holiday/leisure markets for Russia by nationality, January through June 2002-05 ('000)</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>% change 2005/04</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market</td>
<td>2002</td>
<td>2003</td>
<td>2004</td>
<td>2005</td>
<td>% change 2005/04</td>
</tr>
<tr>
<td>Germany</td>
<td>95.0</td>
<td>88.0</td>
<td>100.0</td>
<td>99.2</td>
<td>-0.8</td>
</tr>
<tr>
<td>Poland</td>
<td>325.0</td>
<td>357.0</td>
<td>110.7</td>
<td>76.8</td>
<td>-30.6</td>
</tr>
<tr>
<td>China</td>
<td>87.0</td>
<td>45.0</td>
<td>93.2</td>
<td>73.8</td>
<td>-20.8</td>
</tr>
<tr>
<td>Finland</td>
<td>48.0</td>
<td>98.0</td>
<td>83.3</td>
<td>66.9</td>
<td>-19.7</td>
</tr>
<tr>
<td>USA</td>
<td>34.0</td>
<td>37.0</td>
<td>52.1</td>
<td>60.9</td>
<td>16.9</td>
</tr>
<tr>
<td>Italy</td>
<td>21.0</td>
<td>24.0</td>
<td>46.6</td>
<td>50.9</td>
<td>9.2</td>
</tr>
<tr>
<td>France</td>
<td>34.0</td>
<td>43.0</td>
<td>63.1</td>
<td>49.5</td>
<td>-21.6</td>
</tr>
<tr>
<td>UK</td>
<td>20.0</td>
<td>30.0</td>
<td>38.6</td>
<td>48.3</td>
<td>25.1</td>
</tr>
<tr>
<td>Latvia</td>
<td>19.0</td>
<td>15.0</td>
<td>16.2</td>
<td>37.1</td>
<td>129.0</td>
</tr>
<tr>
<td>Estonia</td>
<td>19.0</td>
<td>18.0</td>
<td>26.6</td>
<td>32.5</td>
<td>22.2</td>
</tr>
</tbody>
</table>

But, in addition, arrivals in Russia include cruise passengers (this is contrary to the official UNWTO specifications), and both the US and UK markets, as shown below, have contributed strongly to the growth in cruise business for St Petersburg in recent years.

THE CRUISE MARKET

The cruise business is becoming big business

One sector of the inbound market that has performed well above average is the cruise market – both for river and sea cruises. The most popular river cruises, which primarily attract older Americans and Europeans, operate between St Petersburg in the north to Moscow, but it is possible to travel by boat from the Baltic Sea all the way south to Volgograd, Rostov-on-Don or Astrakhan on the Caspian Sea.

Although port facilities badly need upgrading – the St Petersburg Government plans for a major overhaul, as discussed in the Policy section of this report – the use of quality ships on cruises around the Baltic has helped to stimulate demand. St Petersburg is now the second most important port in the Baltic after Copenhagen, in terms of passenger numbers, attracting 253,000 in 2004, and it recorded the highest number of cruise ship calls of any Baltic port that year. The growth in passengers and ship calls is estimated at 39 per cent and 16 per cent respectively for 2005.

| Cruise business for St Petersburg, 2000-05a |
|-------------------------------------------|-------------------------------------------|
| Year           | Passengers ('000) | % annual change | Ship calls | % annual change |
| 2000           | 147.1           | na                 | 238        | na                 |
| 2001           | 163.9           | 11.4               | 221        | -7.1               |
| 2002           | 142.6           | -13.0              | 212        | -4.1               |
| 2003           | 204.4           | 43.3               | 275        | 29.7               |
| 2004           | 252.6           | 23.6               | 303        | 10.2               |
| 2005a          | 350.0           | 38.6               | 350        | 15.5               |

Russian inbound travel from non-CIS countries by purpose of visit, 2004

<table>
<thead>
<tr>
<th>Source: St Petersburg Committee for Tourism &amp; Resort Development</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source: Goskomstat</td>
</tr>
</tbody>
</table>

Chinese citizens living near the Russian border – one of the world’s longest shared borders – have been able to enter neighbouring regions without visas, whether for leisure or business reasons, since 2000, accounting for most of the 813,000 Chinese who visited Russia in 2004. By dropping the visa requirement for more distant trips within Russia, the country hopes to attract more than 1 million Chinese in 2006.

As already indicated, a significant, if unidentifiable, share of visits from Western markets are probably for business rather than pure leisure.

The USA dominates Russia’s Baltic cruise business, accounting for a 30 per cent share of passengers, followed by the UK (19 per cent) and Germany (13 per cent).
LEADING TOURISM DESTINATIONS
Only 20 per cent of the country benefits from tourism…

The National Tourism Academy’s report on the status of Russia’s tourism industry indicated that less than 20 per cent of the country is used for tourism purposes. Up to 90 per cent of foreign visitors go to Moscow and St Petersburg, visiting the Golden Ring as a side trip – 14 ancient cities forming a ring around the capital. Some may possibly take a Volga River cruise, and the more adventurous may head for Lake Baikal, the deepest lake in the world, or the Caucasus mountains.

Residents of countries bordering Russia tend to visit the border areas. Thus Poles and Lithuanians traditionally head for the Kaliningrad enclave, and tourists from China or other parts of Northeast Asia are most likely to visit Russia’s Far East, including the cities of Vladivostok and Khabarovsk.

…largely due to poor tourism infrastructure

Russia has a total of 13 different official tourist zones, according to Russia’s State Statistics Committee (Goskomstat). These stretch from the West Tourist Zone, which includes Kaliningrad, in the extreme west-northwest of the country, to Russia’s North and Far East Tourist Zones bordering the Pacific, including Kamchatka, the Primorsky territory and the regions of Khabarovsk and Sakhalin.

The most popular tourism region is the Central Tourist Zone, where Moscow and the Golden Ring cities are located. Of its total 5.3 million visitors in 2003, some 1.5 million, or 28 per cent were foreign. The North-West Zone, meanwhile, which includes St Petersburg, recorded 2.2 million arrivals the same year, of whom 36 per cent came from abroad.

Foreigners accounted for only 11 per cent of arrivals in the Volga region, Russia’s third favourite destination region with 1.9 million tourist arrivals – business and leisure combined. In contrast, the Urals and the Ob & Altai regions of Siberia – which make up the fourth and fifth most important regions – rely heavily on tourists from abroad, albeit on a lower base. Foreigners make up 69 per cent and 67 per cent of their arrivals. Nevertheless, it should be noted that only a small percentage of foreigners are Westerners on holiday.

MOSCOW AND ST PETERSBURG
Vying for top place in the favourites’ ranking

As already indicated, data for 2005 is rather sketchy. However, the Moscow Committee for Tourism claims double-digit growth in arrivals over 2004’s 2.9 million. If proved accurate, which seems uncertain, this would take Moscow to first place in the favourite Russian destinations’ ranking since St Petersburg and the North-West region, which occupied the top spot in 2004 with 3.1 million international visitors, are reported to have suffered a sharp downturn in arrivals last year.

The reports could turn out to be a case of media hype, but it is clear that the city’s hotels did suffer – even during their traditional peak summer season.

It should be noted that the official data is anyway not very meaningful, and must therefore be interpreted with caution, since arrivals in Moscow and St Petersburg only relate to visitors arriving directly in those cities/regions from abroad. So a tourist who enters the country via Moscow and travels on to St Petersburg by whatever mode of domestic transport, is excluded from the official St Petersburg count.

Moscow boasts over 50 per cent of Russia’s hotel room capacity

Over 50 per cent of the country’s hotel capacity, or more than 36,000 rooms (65,000 beds), is concentrated in Moscow. However, since most of these rooms are in hotels dating back to the Soviet era, and have not been renovated, they fall well short of international standards in terms of product and service quality.

The total room count including newly opened and/or internationally branded hotels, plus certain renovated rooms in Soviet properties – such as the 70 rooms in the now renovated and upgraded Savoy hotel – is estimated at about 8,000. This is of course well below the 70,000-75,000 graded room stock in, say, London or Paris. Of the 8,000, over 4,300 (excluding a two-star Best Western) carry an international brand name.

International brand hotels in Moscow, 2005a

<table>
<thead>
<tr>
<th>Hotel</th>
<th>Rooms</th>
<th>Opened/ acquiredb</th>
<th>Current hotel chain affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Baltschug Kempinski</td>
<td>230</td>
<td>1988</td>
<td>Kempinski</td>
</tr>
<tr>
<td>Radisson Slavyanskaya</td>
<td>410</td>
<td>1990</td>
<td>Rezidor</td>
</tr>
<tr>
<td>Novotel Airport</td>
<td>472</td>
<td>1992</td>
<td>Accor</td>
</tr>
<tr>
<td>Sheraton Palace</td>
<td>204</td>
<td>1993</td>
<td>Starwood</td>
</tr>
<tr>
<td>Holiday Inn Vinogradovo</td>
<td>154</td>
<td>1995</td>
<td>IHG</td>
</tr>
<tr>
<td>Méridien Country Club</td>
<td>131</td>
<td>1995</td>
<td>Le Méridien</td>
</tr>
<tr>
<td>National Méridien</td>
<td>221</td>
<td>1995</td>
<td>Le Méridien</td>
</tr>
<tr>
<td>Renaissance</td>
<td>475</td>
<td>1997</td>
<td>Marriott</td>
</tr>
<tr>
<td>Marriott Grand</td>
<td>386</td>
<td>1997</td>
<td>Interstate</td>
</tr>
<tr>
<td>Marriott Tverskaya</td>
<td>162</td>
<td>1997</td>
<td>Interstate</td>
</tr>
<tr>
<td>Marriott Royal Aurora</td>
<td>230</td>
<td>1999</td>
<td>Interstate</td>
</tr>
<tr>
<td>Novotel Center</td>
<td>255</td>
<td>2002</td>
<td>Accor</td>
</tr>
<tr>
<td>Ararat Park Hyatt</td>
<td>220</td>
<td>2002</td>
<td>Hyatt</td>
</tr>
<tr>
<td>Holiday Inn Lesnaya</td>
<td>301</td>
<td>2004</td>
<td>IHG</td>
</tr>
<tr>
<td>Swissôtel Krasny Holm</td>
<td>235</td>
<td>2005</td>
<td>Raffles</td>
</tr>
<tr>
<td>Courtyard C</td>
<td>218</td>
<td>2005</td>
<td>Marriot</td>
</tr>
</tbody>
</table>

Source: Respective hotels

More new branded hotels coming on line

A new 332-room Ritz-Carlton is scheduled to open in mid-2006 on the site of the demolished Intourist hotel in Moscow’s Tverskaya Street. This will be the first Ritz-Carlton in Central or Eastern Europe and is a major boost for the group, which lost out to rival Four Seasons in a bid to run a new property on the site of the former Moskva Hotel – a prime site in front of the Kremlin. Meanwhile, the Four Seasons is expected to come on line in 2007 or 2008.
Although plans have a habit of changing quite frequently in Moscow, other new developments under construction or on the drawing board include the Holiday Inn Sokolniki, which is also due to open in mid-2006 – and will be the third Holiday Inn in the city – and a third Novotel, a 220-room property that will be located in the Gostiny Dvor exhibition complex. The Korean-owned Lotte group is reportedly building a 350-room hotel, and a number of locally managed properties are also due to come on line in 2006 and 2007.

The Ukraina hotel, one of the most famous landmarks in Moscow, was recently sold and will reportedly be upgraded to a four-star property. It is thought that the owners will look to sign a management contract with an international hotel chain.

Business travellers dominate hotel guest mix

Statistics from the Moscow Committee for Tourism suggest that business travellers account for as much as 78 per cent of the overall guest mix in Moscow’s four- and five-star properties – 67 per cent at corporate rates and 11 per cent at full business rates. And the business sector is estimated to generate some 80 per cent of total hotel roomnights.

Nevertheless, the share of arrivals for holidays, or short breaks, in Moscow is growing faster – officially, by 250 per cent from 1999 to 2004. This compared with a 96.5 per cent increase in arrivals overall. In Moscow’s top hotels, group leisure business generates a 12 per cent share and independent (FIT) leisure guests 10 per cent (2004 data). The Moscow Committee for Tourism says that 40 per cent of leisure tourists are on pre-paid package programmes.

Overall, the city’s quality hotels report an average length of stay of between two to three nights – down from 5.5 nights in 1995.

A source of easy money for hotel operators

Average occupancy in Moscow’s top 12 hotels exceeded 77 per cent in 2004 and is reported to have reached 80 per cent last year. Average daily room rate (ADR) and revenue per available room (revpar) have also risen sharply and should increase further this year. Each of the city’s quality rooms brought in US$56,323 in 2004, according to Ernst & Young, with the combined annual take for the leading 12 hotels totalling US$300 million.

Operating performance of Moscow’s upmarket branded hotels, 2001-04

<table>
<thead>
<tr>
<th>Year</th>
<th>Occupancy (%)</th>
<th>ADR (US$)</th>
<th>Revpar (US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>57.2</td>
<td>149.33</td>
<td>94.04</td>
</tr>
<tr>
<td>2002</td>
<td>64.8</td>
<td>152.37</td>
<td>105.67</td>
</tr>
<tr>
<td>2003</td>
<td>72.0</td>
<td>179.31</td>
<td>128.01</td>
</tr>
<tr>
<td>2004</td>
<td>77.3</td>
<td>198.93</td>
<td>155.00</td>
</tr>
</tbody>
</table>

Source: Ernst & Young

An acute shortage of mid-market hotels…

Over the past ten years, led by Moscow’s Mayor, Yuri Luzhkov, there have been big efforts to raise the Russian capital’s tourism profile and turn it into a major destination for leisure as well as business tourism. Although international arrivals more than doubled from 1999 to 2004 – increasing Moscow’s share of total international arrivals in Russia by five percentage points over the five years to 13 per cent – these efforts have not been particularly successful because of a shortage of accommodation, particularly in the mid-market categories.

As discussed in more detail in the Policy section of this report, the hotel capacity situation has been exacerbated by the demolition of many Soviet-built hotels. As a result, the Moscow Committee for Tourism’s 2010 target of 5 million foreign visitors, which it now claims will be reached by 2007, seems unrealistic. And the situation is expected to get even worse.

…which will get worse in 2006

A continued reduction in room capacity through demolitions will also undermine the city’s plans to triple existing room supply by 2010. The next Soviet icon to go will be the 2,700-room Rossiya, which closed at the end of 2005. The loss of so many rooms – bringing the total room capacity lost to date to around 6,000 – is expected to have a major impact on tourism in Moscow in 2006 and beyond.

The sprawling hotel, which was built in 1967, occupies a prime site at the foot of Red Square next to St Basil’s cathedral. Current rumours suggest that it is likely to be replaced by a deluxe hotel of only 200-300 rooms plus serviced apartments. So the shortage of capacity will still be significant, even when the replacement hotel is up and running.

St Petersburg, the leisure tourism capital of Russia

Although St Petersburg is the leisure tourism capital of Russia, and it attracts a higher number of holiday travellers – and, indeed, arrivals overall – its hotel operating performance falls well short of Moscow’s,
primarily because it suffers badly from seasonal imbalances. This makes the city less attractive for hotel investment although, if the number of international groups already in St Petersburg or looking to establish a presence there is anything to go by, it is still seen as a prime location.

The city has nine internationally branded hotels, including Best Western, which is the only one not in the four- or five-star category. In addition to the hotels listed in the following table, there is one other locally managed five-star hotel, the Emerald, and several locally run four-star properties. The city now has around 180 hotels with 17,000 rooms, with around 50 per cent of these in international standard hotels.

### International brand hotels in St Petersburg, 2005

<table>
<thead>
<tr>
<th>Hotel</th>
<th>Rooms</th>
<th>Opened/acquired</th>
<th>Current hotel chain affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corinthia Nevskij Palace</td>
<td>285</td>
<td>1993</td>
<td>Corinthia</td>
</tr>
<tr>
<td>Angleterre</td>
<td>192</td>
<td>1997</td>
<td>Rocco Forte</td>
</tr>
<tr>
<td>Astoria</td>
<td>240</td>
<td>2001</td>
<td>Rocco Forte</td>
</tr>
<tr>
<td>Radisson Royal</td>
<td>164</td>
<td>2001</td>
<td>Rezidor</td>
</tr>
<tr>
<td>Grand Hotel Europe</td>
<td>301</td>
<td>2004</td>
<td>Orient Express</td>
</tr>
<tr>
<td>Baltic Renaissance</td>
<td>102</td>
<td>2004</td>
<td>Marriott</td>
</tr>
<tr>
<td>Novotel Center</td>
<td>233</td>
<td>2005</td>
<td>Accor</td>
</tr>
<tr>
<td>Moika Kempinski</td>
<td>197</td>
<td>2005</td>
<td>Kempinski</td>
</tr>
</tbody>
</table>

* 4-5-star brands as at August 2005
* Data of current brand/chain affiliation

### Guest mix at St Petersburg hotels, 2004 (%)

- Leisure groups (41%)
- Conference delegates (11%)
- Full-rate business (9%)
- Incentives (2%)
- Corporate (17%)
- Individual leisure (20%)

Source: St Petersburg Committee for Tourism & Resort Development

St Petersburg does not have a hotel capacity shortage, but prices skyrocket during the peak summer months, known as the ‘white nights’ season.

Increased competition helps stem rate rises

Except during its summer peak, which did not materialize in 2005, St Petersburg does not have a hotel capacity shortage, but prices skyrocket during the peak summer months, known as the ‘white nights’ season. The room rate eased somewhat in summer 2005 as business reportedly dropped by around 20 per cent for the city’s leading hotels. But this was also partly due to the fact that a large number of boutique or mini-hotels have been developed in St Petersburg, and these are attracting growing numbers of independent tourists.

In the last two years, and especially since the much-publicized Orient Express purchase of St Petersburg’s top hotel, the Grand Hotel Europe, investor confidence has picked up strongly. This is also due to the local government’s efforts to facilitate investment and ease bureaucratic procedures. Russia’s hosting of the G8 Summit in St Petersburg in summer 2006 should further raise awareness of the city’s tourism and investment potential.

Leisure generates nearly two thirds of hotel guests

Data for 2005 is not available but, in 2004, leisure group business accounted for 41 per cent of hotel guests, with FIT leisure travellers generating a further 20 per cent. MICE business represented 13 per cent and the balance was from corporate or full-rate business travellers.

According to the St Petersburg Committee for Tourism & Resort Development, average occupancy overall in the city in 2004 was 59 per cent, although five-star hotels achieved a much higher 68 per cent. But monthly averages range from a low of 40 per cent to a high of 88 per cent.

### Several new projects are in the pipeline

New hotel projects currently under construction or on the drawing board include two three-star Ibis and one five-star Sofitel for the Accor Group and a five-star Swissôtel for Raffles. Another unnamed five-star property is reportedly being developed with Indonesian backing, an Estonian group Reval Hotels will open a four-star property in 2007, and Rezidor plans at least one more Radisson SAS, at least two Park Inns and a Missoni. Intercontinental, Ramada and Banyan Tree Hotels & Resorts have also announced their arrival on the St Petersburg market – whether this year or in 2007.

Looking to be a world-class city, but growth seems elusive

St Petersburg’s main problem has been a shortage of funding. As discussed in the Policy Recommendations of this report, the budget allocated by the city authorities to tourism promotion and marketing is negligible alongside that of Moscow, although there has reportedly been a significant increase for 2006.

The results of a US$300,000 study commissioned from the Boston Consulting Group in 2004 suggest that St Petersburg could become the fifth most popular city in Europe within five years. And there is no doubt that the city has the potential to become a world-class destination. But it still has a number of weaknesses to overcome before it can dream of achieving this status – eg perceived high prices, widespread crime, and a severe seasonality problem (see pages 50 and 62).
OUTBOUND TOURISM
Pent-up demand for travel…

The collapse of the Soviet Union in 1991 released a huge pent-up demand for travel to foreign countries. It was not that Russians had never travelled abroad – on the contrary, it was quite common practice under the Soviet regime for the average Russian to enjoy state-subsidized holidays in other Communist countries – whether on the Black Sea or, for the really privileged, as far away as India or Vietnam. But like their fellow East Europeans, Russians dreamed of visiting Paris or Rome, London or New York, as well as more exotic climes.

After the initial euphoria and burst of travel activity when the Iron Curtain fell, the majority of Russians came down to earth with a bump. Although annual trip volume continued to rise through most of the 1990s – that is, until the 1998 financial crisis – times were increasingly hard for all but the super rich. The impact of the country’s transition from a planned to a market-based economy was directly felt by the growing middle classes. The average Russian simply did not have enough disposable income to realize his or her dreams, especially as unemployment levels rocketed, and many saw their savings wiped out overnight in 1998.

As a result of this difficult transition period, pent-up demand for travel remains extremely strong, and those who can afford to travel want to take more and more trips every year. So the sight of intrepid Russian travellers in all four corners of the globe is increasingly common.

…boosted by rising incomes

Since the end of the 1990s, the political situation has more or less stabilized and GDP has shown renewed strong growth, fuelled by rising oil prices. Although Russian consumers have a long way to go before catching up with West Europeans, their incomes have surged over the past few years with the booming Russian economy. Estimates suggest that disposable income, adjusted for inflation, has risen by at least 9 per cent for each of the past 3-4 years.

Total outbound trip volume fell during the second half of the 1990s and reached a low of 17.9 million in 2001. Since then, it has recorded consistent annual increases, reaching 24.5 million in 2004. And preliminary estimates point to at least 11-12 per cent growth in 2005.

Although Russian consumers have a long way to go before catching up with West Europeans, their incomes have surged over the past few years with the booming Russian economy.

Almost ten years of consistent growth to non-CIS countries

If travel to CIS countries is excluded from the count, the recent trends have been even more positive. In fact, despite the 1998 financial crisis, trip volume to non-CIS destinations actually increased through the second half of the 1990s. And, by 2004, travel to non-CIS countries represented almost 54 per cent of total volume – 13.2 million trips, up 13 per cent on 2003.

Neighbouring countries, such as Finland, China, Poland and the Baltic States, attract a significant share of Russian outbound travellers although – as is the case with those travelling to CIS destinations – many of their trips are for shuttle trading or simply shopping.

Leading non-CIS destinations for Russian outbound travel, 2002-04

<table>
<thead>
<tr>
<th>Destination</th>
<th>Trips (000)</th>
<th>% change 2004/03</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2002</td>
<td>2003</td>
</tr>
<tr>
<td>Finland</td>
<td>1,889</td>
<td>2,029</td>
</tr>
<tr>
<td>China</td>
<td>1,232</td>
<td>1,372</td>
</tr>
<tr>
<td>Turkey</td>
<td>913</td>
<td>1,312</td>
</tr>
<tr>
<td>Estonia</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Germany</td>
<td>625</td>
<td>790</td>
</tr>
<tr>
<td>Lithuania</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Egypt</td>
<td>279</td>
<td>418</td>
</tr>
<tr>
<td>Poland</td>
<td>897</td>
<td>666</td>
</tr>
<tr>
<td>France</td>
<td>196</td>
<td>232</td>
</tr>
<tr>
<td>Italy</td>
<td>227</td>
<td>201</td>
</tr>
<tr>
<td>Spain</td>
<td>273</td>
<td>215</td>
</tr>
<tr>
<td>UAE</td>
<td>219</td>
<td>193</td>
</tr>
<tr>
<td>UK</td>
<td>139</td>
<td>170</td>
</tr>
<tr>
<td>Japan</td>
<td>188</td>
<td>177</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>94</td>
<td>89</td>
</tr>
</tbody>
</table>

Poland, for example – a favourite for small traders – has lost significant share, and the trend is likely to continue since Russians now need visas for Poland as it joined the European Union in May 2004.

However, at the other end of the scale, in terms of growth trends – reflecting the boom in travel to sun & beach destinations – Turkey and Egypt have gained significant share.

Some former East European capitals, like Prague and Budapest, have also become increasingly popular city-break destinations. And the capitals and beaches of Western Europe – notably France, Italy, Spain and the UK – remain well up the ranking of favourites, despite visa issues.

Holiday travel dominates…

The official Goskomstat data for Russian travel to non-CIS countries overall points to a 44 per cent share for holiday trips, 32 per cent for other private travel and 13 per cent for business.

…and demand is mainly for sun & beach…

The following table highlights the top ten holiday destinations, as well as their respective growth in 2004 and the first half of 2005 – the latest data available. Turkey has been the firm favourite for a number of years already, ahead of China and Egypt. It should nonetheless be noted that
Some 65 per cent of trips to China are same-day cross-border trips from Russia’s Far East.

There has been little change in the overall ranking since 2004 although Poland has slipped from sixth to ninth position – due to the visa issue, as already indicated – and Italy has risen two places.

**Russian outbound travel to non-CIS destinations, by purpose of trip, 2004 (Total 13,196,000)**

<table>
<thead>
<tr>
<th>Trips ('000)</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>% change 2004/03</th>
<th>% change Jan-Jun 2005/04</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turkey</td>
<td>686</td>
<td>1,039</td>
<td>1,446</td>
<td>39.2</td>
<td>7.7</td>
</tr>
<tr>
<td>China</td>
<td>617</td>
<td>688</td>
<td>941</td>
<td>36.8</td>
<td>16.4</td>
</tr>
<tr>
<td>Egypt</td>
<td>240</td>
<td>368</td>
<td>586</td>
<td>59.2</td>
<td>7.0</td>
</tr>
<tr>
<td>Finland</td>
<td>406</td>
<td>327</td>
<td>377</td>
<td>15.3</td>
<td>0.8</td>
</tr>
<tr>
<td>Poland</td>
<td>635</td>
<td>422</td>
<td>322</td>
<td>-23.7</td>
<td>-61.7</td>
</tr>
<tr>
<td>Germany</td>
<td>209</td>
<td>278</td>
<td>256</td>
<td>-7.9</td>
<td>2.1</td>
</tr>
<tr>
<td>Spain</td>
<td>229</td>
<td>168</td>
<td>191</td>
<td>13.7</td>
<td>7.4</td>
</tr>
<tr>
<td>UAE</td>
<td>170</td>
<td>146</td>
<td>175</td>
<td>19.9</td>
<td>-3.1</td>
</tr>
<tr>
<td>Italy</td>
<td>148</td>
<td>119</td>
<td>156</td>
<td>31.1</td>
<td>30.2</td>
</tr>
<tr>
<td>France</td>
<td>87</td>
<td>112</td>
<td>138</td>
<td>23.2</td>
<td>4.8</td>
</tr>
</tbody>
</table>

**Top 20 destinations for Russian outbound holiday travel, 2002-05**

Most of the growth out of Russia in the last four to five years has been for sun & beach destinations, notably Turkey and Egypt, both of which are increasingly sold on a year-round basis. At the same time, destinations that have attracted consistent growth are those for which no visas are necessary, or which offer visas on arrival. Turkey, Egypt, Dubai, Tunisia and Thailand are good examples. A lot of trips are decided, and booked, at the last minute so Russians prefer to avoid the possible hassle of applying for visas.

**Growing incentive travel**

Apart from holiday travel, one sector offering good growth opportunities is corporate sponsored leisure travel, or incentives. Although most interest seems to be coming from foreign firms established in Russia, such as Panasonic and Pepsi-Cola, the trend is spreading to Russian businesses – and not just those operating out of the major centres of Moscow and St Petersburg. Yekaterinburg, for example, is an important centre of mineral wealth and there are key centres of industry – from oil and gas to aluminium, etc – across the country, employing large numbers of Russians.

The attraction of incentive travel is because it is new and exciting for the beneficiaries. Foreign travel was beyond the budgets of much of the population for so many years, and everyone is now eager to visit as many destinations as possible. So travel is a very popular form of reward or motivation.

While China, the Baltic States, the western CIS, Germany and Finland are the leading destinations for business travel, the main growth in demand for incentive travel last year was for the favourite holiday destinations – notably Turkey and Egypt – because of ease of access. Destinations which either do not require visas, or for which visas can be obtained on arrival, have the best chance of success in the short term.

**EXPERIMENT ON TRAVEL**

**Big spenders, especially on retail**

UNWTO statistics suggest that Russia is the ninth largest market, in terms of expenditure on travel (excluding spending before departure in Russia and all spending on transport). And they are expected to climb up the ranking fairly rapidly.

Russian tourists have a growing reputation as big spenders, whether in airports and downtown shops on retail goods, or on extras during their hotel stays. This is reflected in data released by the different charge/credit card companies, as well as by Global Refund and other stakeholders in the duty and tax refund business.

Research by RFH Consumer Insight – which surveys spending at airports and other retail outlets in key tourism destinations around the world – says that Russians are more brand aware than even the Chinese, willing to pay a premium for things they cannot find at home. At least 97 per cent of them buy at airports on their travels.

**RUSSIA’S TRAVEL TRADE**

**A fragmented industry**

Under the Soviet Union, there were only three travel agencies in the country, and these were all state-owned, but now there are reportedly 12,715 travel agencies and 5,137 tour operators – all privately owned. However, the actual number of companies tends to be lower than the official counts. This is because the licensing system allows one company to be a holder of both a tour operator and travel agent’s licence. As a result, many companies are simultaneously registered as both, allowing them to deal directly with customers and through other retail agents.
They are also allowed to handle all kinds of tourism – domestic, inbound and outbound.

The majority of travel agents are based in Moscow and St Petersburg, although six other cities have more than 40 each, excluding pure retail agencies, according to official data from Rosturizm. These are Vladivostok (78), Rostov-on-Don (66), Kaliningrad (53), Irkutsk (45), Yekaterinburg (42) and Novosibirsk (41). Moscow controls about 65 per cent of the market, in terms of sales, but growth over the next decade is expected to come mainly from the regions.

Regions growing as a source

The fastest growing sources of Travel & Tourism demand within Russia are the cities of over 1 million inhabitants, plus Vladivostok and Khabarovsk in Russia’s Far East. An increasing number of direct flights operate to foreign countries from cities such as Novosibirsk, Yekaterinburg and Krasnoyarsk. But these cities are also growing centres of business, attracting increasing corporate travel and investment.

**Russia’s largest cities, 2005**

<table>
<thead>
<tr>
<th>City</th>
<th>Region</th>
<th>Population (’000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Moscow</td>
<td>Central</td>
<td>10,126</td>
</tr>
<tr>
<td>St Petersburg</td>
<td>North-West</td>
<td>4,160</td>
</tr>
<tr>
<td>Novosibirsk</td>
<td>Siberia</td>
<td>1,426</td>
</tr>
<tr>
<td>Nizhny Novgorod</td>
<td>Volga</td>
<td>1,311</td>
</tr>
<tr>
<td>Yekaterinburg</td>
<td>Urals</td>
<td>1,294</td>
</tr>
<tr>
<td>Samara</td>
<td>Volga</td>
<td>1,158</td>
</tr>
<tr>
<td>Omsk</td>
<td>Siberia</td>
<td>1,134</td>
</tr>
<tr>
<td>Kazan</td>
<td>Tatarstan</td>
<td>1,105</td>
</tr>
<tr>
<td>Chelyabinsk</td>
<td>Urals</td>
<td>1,077</td>
</tr>
<tr>
<td>Rostov-on-Don</td>
<td>Caucasus</td>
<td>1,068</td>
</tr>
<tr>
<td>Ufa</td>
<td>Volga</td>
<td>1,042</td>
</tr>
<tr>
<td>Volgograd</td>
<td>Volga</td>
<td>1,011</td>
</tr>
<tr>
<td>Perm</td>
<td>Volga</td>
<td>1,002</td>
</tr>
<tr>
<td>Krasnoyarsk</td>
<td>Siberia</td>
<td>909</td>
</tr>
<tr>
<td>Saratov</td>
<td>Volga</td>
<td>873</td>
</tr>
<tr>
<td>Voronezh</td>
<td>South Russia</td>
<td>849</td>
</tr>
<tr>
<td>Vladivostok</td>
<td>Far East</td>
<td>595</td>
</tr>
<tr>
<td>Khabarovsk</td>
<td>Far East</td>
<td>583</td>
</tr>
</tbody>
</table>

Source: Goskomstat

Last-minute decisions

In 2004, an estimated 2 million package tours were sold in Russia and an astonishing 75 per cent of bookings were made within two weeks of departure. Of the 20 or so leading tour operators in the country, the biggest in terms of turnover and number of sales are Tez Tour, Inna Tour (which has merged with VIP-Service), Pegas Touristik, Natalie Tours, VAO Intourist and Neva. Most have their own agency network – for some, this can include several thousand retail travel agents across the country – but also deal directly with consumers.

**AIR TRANSPORT**

**Fuelled primarily by outbound demand**

A 20 per cent increase in outbound trips, as well as increased demand for domestic airline travel, resulted in a 17 per cent increase in Russia’s air traffic in 2004 to 83 billion revenue passenger-km (RPK). Thanks to the increase, coupled with higher airfares, Russian airlines achieved US$6 billion in operating revenues – an additional US$1 billion over 2003.

Just under 50 per cent of all trips to non-CIS countries made by Russians in 2004 were by plane, and preliminary estimates for 2005 suggest that the airline share is now well over 50 per cent.

**A growing choice of foreign airlines**

The last 18-20 months have seen a huge increase in the number of foreign airlines operating to Russia, particularly to Moscow, as well as the inauguration of new international routes by Russian airlines. Among the newcomers – or airlines operating new routes – have been Iberia from Madrid, Delta Airlines from Atlanta, and SkyNet from New York and Shannon. Germania Express (from Berlin and Munich) and Germanwings (from Berlin and Cologne-Bonn) are the first two low-cost carriers to operate to the country.

In addition, Royal Jordanian started a route in 2004 from Amman, Mongolian from Ulan-Bator, Pakistan International from Karachi via Dubai, China Eastern from Shanghai, and China Southern from Manzhouli (to Irkutsk).

Japan Airlines and Emirates increased frequencies from Japan and Dubai respectively, Korean Airlines started a service from Seoul to St Petersburg in July 2004, and Thai Airways International launched a Moscow-Bangkok service in November 2005. A whole host of carriers have started, or are starting, new services this winter. These include Cathay Pacific Airways, which originally signed a code-share agreement with Aeroflot on its Moscow-Hong Kong route in 2004, but which will now operate a new Hong Kong-Manchester service via Moscow later in 2006. And Singapore Airlines started flying to Moscow via Dubai in March this year.

**RUSSIAN AIRLINES**

Russia has some 200 airlines of its own, although mergers and acquisitions are resulting in increased consolidation. In 2004, they...
carried 33.7 million passengers, up 14 per cent over the previous year, and international passenger traffic grew much faster than domestic traffic. The top five airlines, which accounted for 50 per cent of total passengers carried, were Aeroflot, Sibir/S7, Pulkovo, KrasAir and UTair.

In sixth position was Transaero, which has added the greatest number of foreign destinations to its route network over the past 12 months.

All six recorded double-digit growth in passenger numbers in 2004 and the trend appears to have continued through 2005. Preliminary estimates point to an increase in passengers of 13 per cent for Aeroflot and 12 per cent for Sibir – of whom 36 per cent were on international routes.

**New Western aircraft**

Oil price rises and crippling import duties on foreign aircraft were expected to stunt growth last year, but the only thing that appears to have been negatively impacted is earnings and, despite this, at least 40 Western jet aircraft were bought by Russian airlines in 2005, including 35 Boeings and four Airbuses. The number of foreign aircraft purchases or leases is expected to exceed 60 in 2006, which of course does not augur well for Russia’s own aircraft manufacturing industry.

**MAJOR AIRPORTS**

Another year of good growth

Russia’s leading airports are the three rivals in Moscow – Domodedovo, Sheremetyevo and Vnukovo – plus St Petersburg’s Pulkovo. Yekaterinburg and Novosibirsk are also showing healthy annual growth, according to results filed with Airports Council International (ACI), and there are several smaller airports that are similarly gaining share. But most of these are not members of ACI, so do not report their traffic results on a regular basis.

**Passenger throughout at selected Russian airports**, 2003-04 and Jan through Oct 2005

<table>
<thead>
<tr>
<th>Airport</th>
<th>Code</th>
<th>Passengers ('000) 2003</th>
<th>Passengers ('000) 2004</th>
<th>% change 2003/02</th>
<th>% change 2004/03</th>
<th>Jan-Oct 2005 ('000)</th>
<th>% change Jan-Oct 2005/04</th>
</tr>
</thead>
<tbody>
<tr>
<td>Moscow Domodedovo</td>
<td>DME</td>
<td>9,375</td>
<td>12,095</td>
<td>40.3</td>
<td>28.9</td>
<td>11,962</td>
<td>14.5</td>
</tr>
<tr>
<td>Moscow Sheremetyevo</td>
<td>SVO</td>
<td>11,541</td>
<td>12,865</td>
<td>5.9</td>
<td>11.5</td>
<td>10,418</td>
<td>-6.6</td>
</tr>
<tr>
<td>Moscow Vnukovo</td>
<td>VKO</td>
<td>2,796</td>
<td>2,490</td>
<td>-10.4</td>
<td>-10.9</td>
<td>3,036</td>
<td>46.7</td>
</tr>
<tr>
<td>St Petersburg</td>
<td>LED</td>
<td>3,794</td>
<td>4,385</td>
<td>18.8</td>
<td>15.6</td>
<td>4,083</td>
<td>5.8</td>
</tr>
<tr>
<td>Yekaterinburg</td>
<td>SVX</td>
<td>1,336</td>
<td>1,552</td>
<td>12.9</td>
<td>21.4</td>
<td>na</td>
<td>na</td>
</tr>
<tr>
<td>Novosibirsk</td>
<td>OVB</td>
<td>1,364</td>
<td>1,500</td>
<td>9.9</td>
<td>8.0</td>
<td>1,428</td>
<td>7.5</td>
</tr>
<tr>
<td>Samara</td>
<td>KUF</td>
<td>914</td>
<td>1,002</td>
<td>4.4</td>
<td>9.6</td>
<td>876</td>
<td>2.0</td>
</tr>
<tr>
<td>Rostov</td>
<td>ROV</td>
<td>na</td>
<td>637</td>
<td>na</td>
<td>10.8</td>
<td>217</td>
<td>4.8</td>
</tr>
</tbody>
</table>

* Airports filing traffic data with ACI  
  b Estimated  

Source: Airports Council International (ACI)

**CURRENT OUTLOOK**

Given the many challenges facing Russia’s Travel & Tourism industry and the constraints to growth in the short term, there is little doubt that the growth in outbound travel will continue to outpace that of inbound or domestic tourism – at least over the remainder of this decade.

Russians are arguably among the most enthusiastic travellers in the world, and are rated by tourism destinations as having the same kind of growth potential as China or India. More and more national tourism organizations are entering the market to ensure their share of the expanding business. Most importantly, it is no longer just the elite of Russian society who can afford to travel, although these 5 million or so elite travellers are clearly the most sought after segment. But the middle Muscovite classes now go on holiday once a year – primarily in search of sun and beach – or even two or three times annually, while 5-10 per cent of the population travel abroad every couple of months, including at Christmas and/or the New Year.

Left to its own devices, Russia’s inbound tourism will struggle to compete against the growing competition – in Eastern Europe and other parts of the world. But if the Russian Government takes the lead in making Travel & Tourism a strategic development priority, working with the private sector to ensure a high-quality, well-marketed tourism product and providing the necessary infrastructure to support sustainable growth, the prospects are extremely bullish.
Over the last three decades, countries have estimated the economic impact of Travel & Tourism through a range of measures using a variety of definitions and methodologies. Such approaches have prevented meaningful comparisons among nations. Even for the same nation over different periods of time, they have frustrated business and government attempts to draw valid conclusions about the nature and course of Travel & Tourism Demand in national economies. This regime has obscured the substantial, positive role the industry plays in national economies and has thwarted business and government attempts to optimize economic programmes and policies.

The World Travel & Tourism Council (WTTC) recognized the dearth of crucial Travel & Tourism intelligence from the time of its establishment in 1990 and it published the first detailed estimates of world tourism’s economic impact that same year.

Since then WTTC has worked to improve its methodologies and to encourage individual countries to enhance their measurement and understanding of tourism’s impact on their national economies. Furthermore, in the spirit of joining forces to enhance world comprehension of the role of Travel & Tourism in national economies, WTTC has strongly supported the programmes of the World Tourism Organization (UNWTO) to improve tourism statistics worldwide.

WTTC’S RESEARCH

WTTC and its economic/research partners – Oxford Economic Forecasting, (OEF), since 1999, and Global Insight (previously known as DRP•WEFA), from 1990-1999 – have developed and published research on the economic contribution of Travel & Tourism to the world, regional and national economies.

Starting in 1990, WTTC’s research team has been working to develop practical, real-world models to illustrate Travel & Tourism’s economic contribution based on the needs of private sector leaders, public sector policy-makers and industry researchers, and on the interpretation of the system of national accounts. The research is now firmly anchored in the international standard for tourism satellite accounting that was developed by UNWTO, OECD and Eurostat, and approved by the United Nations Statistical Commission in 2000. It was launched at the TSA Conference held in Vancouver in May 2001 and published as the Tourism Satellite Account: Recommended Methodological Framework (TSA:RMF) in 2001.

Since 1999, WTTC’s research has assumed the conceptual framework of the UN-approved standard with a number of discretionary extensions, and it combines the most sophisticated economic modelling and forecasts available with the most up-to-date, publicly available data to generate a comprehensive implementation of Travel & Tourism satellite accounting.

This simulated TSA has been prepared for the benefit of all stakeholders involved in the future of Travel & Tourism in the Russian Federation – from both the public and private sectors. In carrying out the work, OEF has drawn extensively on the methodology developed over the years by WTTC to develop TSAs as operational tools.
WTTC’S APPROACH TO TOURISM SATELLITE ACCOUNTING

WTTC has endeavoured to implement and produce the most comprehensive TSA provided for within the TSA:RMF – by developing the narrow concept of the ‘Travel & Tourism Industry’ in addition to the broader concept of the ‘Travel & Tourism Economy’. WTTC advocates full implementation of the TSA as defined in the TSA:RMF in order to achieve the highest level of benefits for industry and governments. These include:

- A wealth of customer and consumer information on tourism-related purchases (before, during and after trips – whether domestic or international, imported or exported – as well as services, durables and non-durables) that has never been identified until now;
- Comprehensive documentation and analysis of the full tourism-product service chain and government’s ability to deliver quality and timely service to visitors;
- Linkages between Travel & Tourism and other sectors of the economy, such as agriculture and manufacturing, to illustrate the flow-through of spending;
- Complete outlook for public works that benefit visitors and Travel & Tourism companies in order to leverage public sector plans and priorities for growth;
- Focused opportunities for domestic production, as well as incentives from the public sector, to aid in the growth of businesses that help alleviate trade balance issues;
- Demand- and supply-side information on employment that allows for human resource planning and development.

WTTC has worked towards developing a comprehensive TSA – not because it is eager to exaggerate the size of Travel & Tourism’s impact, but because the information that can be garnered from the exercise by governments and industry is crucial for making intelligent and informed policy and business decisions. WTTC believes that history will document its pioneering implementation of the simulated TSA as one of the most important turning points for Travel & Tourism’s long overdue economic recognition.

In the WTTC research, no country receives special treatment or favours. WTTC uses internationally available data sources and the same scope of tourism satellite accounting for all countries, as well as the same basic assumptions through the same system of models. WTTC’s TSA research utilizes a universal and internally consistent modelling framework and generates harmonized results and forecasts for 175 countries around the world. Details of the methodology used by WTTC/OEF in its TSA research are available on WTTC’s website (www.wttc.org).

THE RUSSIAN FEDERATION
**TSA CONCEPTS & STRUCTURE**

**Demand Side Accounts**

**PERSONAL TRAVEL & TOURISM**
More formally known as Travel & Tourism Personal Consumption, this category includes all personal spending by an economy’s residents on Travel & Tourism services (lodging, transportation, entertainment, meals, financial services, etc) and goods (durable and nondurable) used for Travel & Tourism activities. Spending may occur before, during or after a trip. Spending covers all Travel & Tourism, outbound and domestic.

**BUSINESS TRAVEL**
Formally known as Intermediate Consumption of Travel & Tourism or more simply business travel, this category of expenditures by government and industry includes spending on goods and services (transportation, accommodation, meals, entertainment, etc) for employee business travel purposes.

**GOVERNMENT EXPENDITURES (INDIVIDUAL)**
Formally known as Non-Market Services (Individual), this category includes expenditures (transfers or subsidies) made by government agencies to provide Travel & Tourism services such as cultural (eg art museums), recreational (eg national park) or clearance (eg immigration/customs) etc to visitors.

**VISITOR EXPORTS**
Expenditures by international visitors on goods and services within the resident economy.

**GOVERNMENT EXPENDITURES (COLLECTIVE)**
Formally known as Non-Market Services (Collective), this category includes operating expenditures made by government agencies on services associated with Travel & Tourism, but not directly linked to any individual visitor, instead, these expenditures are generally made on behalf of the ‘community at large’, such as tourism promotion, aviation administration, security services and resort area sanitation services, etc.

**CAPITAL INVESTMENT**
Formally known as Capital Formation, this category includes capital expenditures by direct Travel & Tourism industry service providers and government agencies to provide facilities, equipment and infrastructure to visitors.

**EXPORTS (NON-VISITOR)**
Consumer goods (such as clothing, electronics or petrol) exported for ultimate sale to visitors, or Capital goods (such as aircraft or cruise ships) exported for use by Travel & Tourism industry providers.

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**TRAVEL & TOURISM CONSUMPTION**
Total Travel & Tourism expenditures made by and on behalf of visitors (goods and services) in the resident economy

**TRAVEL & TOURISM DEMAND**
The nominal aggregate of tourism activity in the resident economy

- **PERSONAL TRAVEL & TOURISM**: 1,076.9
- **BUSINESS TRAVEL**: 349.8
- **GOVERNMENT EXPENDITURES (INDIVIDUAL)**: 31.7
- **VISITOR EXPORTS**: 249.9
- **GOVERNMENT EXPENDITURES (COLLECTIVE)**: 72.7
- **CAPITAL INVESTMENT**: 607.1
- **EXPORTS (NON-VISITOR)**: 343.5

**Total**: 1,708.2

**Total**: 2,731.5
The Travel & Tourism Satellite Account is based on a ‘demand-side’ concept of economic activity, because the industry does not produce or supply a homogeneous product or service like traditional industries (agriculture, electronics, steel, etc). Instead, Travel & Tourism is an industrial activity defined by the diverse collection of products (durables and non-durables) and services (transportation, accommodation, food and beverage, entertainment, government services, etc) that are delivered to visitors. There are two basic aggregates of Demand (Travel & Tourism Consumption and Total Demand) and by employing input/output modelling separately (blue/green arrows) to these two aggregates the Satellite Account is able to produce two different and complementary aggregates of Travel & Tourism Supply: the Travel & Tourism Industry and the Travel & Tourism Economy. The former captures the explicitly defined production-side ‘industry’ contribution (i.e. direct impact only), for comparison with all other industries, while the latter captures the broader ‘economy-wide’ impact, direct and indirect, of Travel & Tourism.

### Supply Side Accounts

<table>
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<tr>
<th>Description</th>
<th>Rb bn</th>
<th>'000s of Jobs</th>
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<tbody>
<tr>
<td><strong>TRAVEL &amp; TOURISM INDUSTRY GDP (DIRECT)</strong></td>
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<tr>
<td><strong>TRAVEL &amp; TOURISM ECONOMY GDP (DIRECT AND INDIRECT)</strong></td>
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<tr>
<td><strong>TRAVEL &amp; TOURISM ECONOMY IMPORTS</strong></td>
<td>820.8</td>
<td></td>
</tr>
</tbody>
</table>
DEMAND
Worldwide in 2006, it is expected to post US$6,477 billion of economic activity (Total Demand) and this is forecast to grow to US$12,119 billion by 2016. Travel & Tourism Demand in the European Union is expected to reach US$2,149.4 billion in 2006, growing to US$3,529.0 billion in 2016. In Russia, in 2006, Travel & Tourism is expected to post Rb2,731.5 billion (US$94.8 billion) of economic activity (Total Demand), growing to Rb9,137.7 billion (US$177.6 billion) by 2016.

GDP
In 2006, the Travel & Tourism Industry should contribute 3.6 per cent to worldwide GDP. The broader Travel & Tourism Economy should contribute 10.3 per cent to world GDP in 2006. In the European Union, the Travel & Tourism Industry is expected to post a GDP contribution of 3.9 per cent in 2006, while the Travel & Tourism Economy contribution will be 10.9 per cent. Russia’s Travel & Tourism Industry is expected to contribute 1.5 per cent to Gross Domestic Product (GDP) in 2006 (Rb357.1 billion or US$12.4 billion), rising in nominal terms to Rb1,049.4 billion or US$20.4 billion (1.5 per cent of total) by 2016. The Travel & Tourism Economy contribution (percentage of total) should rise from 7.8 per cent (Rb1,910.7 billion or US$66.3 billion) to 9.1 per cent (Rb6,319.0 billion or US$122.8 billion) in this same period.

GROWTH
Travel & Tourism is a high-growth activity, which is forecast to increase its total economic activity by 4.2 per cent per annum worldwide in real terms over the next ten years. In the European Union, Travel & Tourism is expected to post average annualized gains of 3.5 per cent between 2007 and 2016. For Russia, Travel & Tourism activity is expected to grow by 6.5 per cent per annum in real terms between 2007 and 2016.

EMPLOYMENT
Travel & Tourism is human resource intensive, creating quality jobs across the full employment spectrum. In 2006, one in 11.5 jobs will be generated by the Travel & Tourism Economy. The Travel & Tourism Economy accounts for 8.7 per cent of global employment. Today there are 76.7 million Travel & Tourism Industry jobs and 234.3 million jobs in the Travel & Tourism Economy, and these will rise to 89.5 million Travel & Tourism Industry jobs and 279.3 million Travel & Tourism Economy jobs by 2016. The European Union Travel & Tourism Industry is expected to generate 8,605,615 jobs in 2006 (4.2 per cent of total employment), while the broader Travel & Tourism Economy will account for 23,820,340 jobs (11.8 per cent of total employment). Russia’s Travel & Tourism Economy employment is estimated at 4,515,170 jobs in 2006, 6.6 per cent of total employment, or one in every 15.1 jobs. By 2016, this should total 5,231,827 jobs, 7.7 per cent of total employment or one in every 12.9 jobs. The 863,162 Travel & Tourism Industry jobs account for 1.3 per cent of total employment in 2006 and are forecast to total 891,031 jobs or 1.3 per cent of the total by 2016.

VISITOR EXPORTS
Travel & Tourism is a major exporter, with inbound visitors injecting foreign exchange directly into the economy. Travel & Tourism exports in the European Union are expected to represent 13.0 per cent of total exports in 2006. In Russia, exports make up a very important share of Travel & Tourism’s contribution to GDP. Of Russia’s total exports, Travel & Tourism is expected to generate 6.7 per cent (Rb593.4 billion or US$20.6 billion) in 2006, increasing to Rb1,886.6 billion, or US$36.7 billion (10.1 per cent of the total), in 2016.

CAPITAL INVESTMENT
Travel & Tourism is a catalyst for construction and manufacturing. In 2006, the public and private sectors combined are expected to spend US$1,010.7 billion on new Travel & Tourism Capital Investment worldwide - 9.3 per cent of total investment - rising to US$2,059.8 billion, or 9.6 per cent of the total, in 2016. In the European Union, Travel & Tourism Capital Investment is expected to total US$241.4 billion in 2006, or 8.6 per cent of total regional capital investment. Russia’s Travel & Tourism Capital Investment is estimated at Rb607.1 billion, US$21.1 billion or 12.1 per cent of total investment in 2006. By 2016, this should reach Rb2,621.1 billion, US$51.0 billion or 12.1 per cent of the total.

GOVERNMENT
Travel & Tourism is both a generator and receiver of government funds. Globally, in 2006, Travel & Tourism is expected to garner US$300.2 billion of government expenditures, or 3.8 per cent of total expenditures. By 2016, government spending on Travel & Tourism should increase to US$480.9 billion - 4.0 per cent of total government expenditure. Government Travel & Tourism operating expenditures in Russia in 2006 are expected to total Rb104.4 billion (US$3.6 billion) or 2.7 per cent of total government spending. In 2016, this spending is forecast to total Rb256.2 billion (US$5.0 billion), or 2.7 per cent of total government spending.
### RUSSIAN FEDERATION ESTIMATES AND FORECASTS

<table>
<thead>
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<th></th>
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12006 Real Growth Adjusted for Inflation (%); 22007-2016 Annualized Real Growth Adjusted for Inflation (%);'000 of Jobs

### EUROPEAN UNION ESTIMATES AND FORECASTS

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12006 Real Growth Adjusted for Inflation (%); 22007-2016 Annualized Real Growth Adjusted for Inflation (%);'000 of Jobs

### WORLD ESTIMATES AND FORECASTS

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<td>% of Total</td>
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<td>279,346.7</td>
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12006 Real Growth Adjusted for Inflation (%); 22007-2016 Annualized Real Growth Adjusted for Inflation (%);'000 of Jobs
TOTAL DEMAND

TRAVEL & TOURISM IN RUSSIA IS EXPECTED TO GENERATE RUB2.7 TRILLION (US$94.8 BILLION) OF TOTAL DEMAND IN 2006, INCLUDING:

- RUB1.1 trillion (US$37.4 billion) of Personal Travel & Tourism consumption by residents of Russia (7.8 per cent of total personal consumption);
- RUB349.8 billion (US$12.1 billion) of Business and Government Travel by resident companies and government employees;
- RUB104.4 billion (US$3.6 billion) of Government Expenditures, or 2.7 per cent of total government spending in Russia, to provide individual and collective services to the country’s Travel & Tourism Industry and its visitors;
- RUB607.1 billion (US$21.1 billion) of Capital Investment, or 12.1 per cent of total capital investment in Russia, in personal, commercial and public Travel & Tourism facilities, equipment and infrastructure by residents, Travel & Tourism companies and government agencies;
- RUB249.9 billion (US$8.7 billion) of Visitor Exports generated from international visitor markets, or 2.8 per cent of Russia’s total exports; and
- RUB343.5 billion (US$11.9 billion) of Merchandise Trade Exports, or 3.9 per cent of total exports.

This breakdown of demand shows that Personal and Business Travel & Tourism accounts for nearly 50 per cent of the nation’s Travel & Tourism Economy. Given how important Travel & Tourism is already, the sector must be accorded the highest priority by government so as to ensure sustainable growth in the future.

Over the past 15 years (1990-2005), Russia’s Travel & Tourism activity has experienced a series of strong and weak years followed by a steadier performance (since 1998). But growth in Travel & Tourism activity has nonetheless exceeded 128 per cent since 1988. This compares with 41 per cent cumulative growth over the same period for the European Union, and with 57 per cent for the world overall.

Although Russia suffered like the rest of the world from the impact of 11 September 2001, tourism demand has continued to increase since the start of the recovery in 2002. Russia now looks poised for a period of healthy growth in terms of Travel & Tourism Demand, especially in the medium term.

In 2006, Russia’s Travel & Tourism is expected to grow by 1.9 per cent overall. In the longer term – ie to 2016 – Travel & Tourism Demand in Russia is forecast to average 6.5 per cent per annum. This would comfortably exceed expected worldwide growth of 4.2 per cent per annum, as well as the 3.5 per cent annual average growth forecast for the European Union.

WTTC/OEF expect strong growth in capital investment and visitor exports (9.3 and 7.5 per cent per annum respectively) for the foreseeable future, providing necessary support for business travel and government expenditures – which are expected to post similarly consistent, albeit slightly slower growth.
EMPLOYMENT

THE TRAVEL & TOURISM INDUSTRY IN RUSSIA IS EXPECTED TO GENERATE DIRECTLY 863,000 JOBS IN 2006.

A total of 4.5 million jobs (direct and indirect) are expected to be generated across the broader spectrum of the Travel & Tourism Economy, encompassing:

- travel company employment,
- government agency employment, and
- supplier company employment.

The first category represents Travel & Tourism Industry jobs, while all three categories together represent Travel & Tourism Economy jobs.

Travel & Tourism Industry jobs in Russia, which are expected to total 863,000 in 2006, represent 1.3 per cent of the country’s workforce. By 2016, Travel & Tourism Industry employment is forecast to increase by 28,000 jobs to 1.3 per cent of total employment in Russia.

The 4.5 million Travel & Tourism Economy jobs in Russia in 2006 represent 6.6 per cent of the total workforce. By 2016, Travel & Tourism Economy employment is expected to increase by 717,000 jobs in Russia to 7.7 per cent of total employment.

Over the past ten years, Travel & Tourism employment in Russia has steadily increased – by more than three quarters of a million jobs. In 2006, due to continued strong growth in personal and business Travel & Tourism the employment outlook for Travel & Tourism is quite positive, with employment gains expected to exceed 39,000 jobs.

Assuming that growth in the economy remains positive and visitor exports strengthens over the next few years, there is strong potential over the next decade to create 75,000 new jobs a year. This would mean that the total number of jobs in Travel & Tourism would increase by just over 1.5 per cent per annum between 2007 and 2016.

The charts opposite highlight a few points of interest. First, Russia’s Travel & Tourism employment growth has been mostly positive since the late 1990s.

Second, if Travel & Tourism employment in Russia as a percentage of total employment is compared with the respective shares of neighbouring and competing destinations, Russia comes fairly low down the ranking at number 127. More disappointing, though, it still ranks unfavourably – in 126th position – among the list of 174 countries whose future growth performances are assessed by WTTC/OEF.
GROSS DOMESTIC PRODUCT

THE TRAVEL & TOURISM INDUSTRY IN RUSSIA IS EXPECTED TO PRODUCE DIRECTLY RB357.1 BILLION (US$12.4 BILLION), OR 1.5 PER CENT OF TOTAL GDP, IN 2006.

The broader Travel & Tourism Economy (direct and indirect) is forecast to contribute Rb1.9 trillion (US$66.3 billion), or 7.8 per cent, to total GDP. The long-term expectations for Travel & Tourism GDP growth are positive, exceeding 6.4 per cent annualized real growth to 2016. Over the same period, Travel & Tourism Economy GDP is forecast to gain 1.3 percentage points to reach a 9.1 per cent share of total GDP, or Rb6.3 trillion (US$122.8 billion).

The Travel & Tourism results and forecasts illustrate the significant and sometimes massive economic stimulus of Travel & Tourism, especially for a developing country. The first set of charts (stacked bar) for Russia illustrates how the tourism industry acts as a leading economic catalyst as its contribution permeates through Russia’s Travel & Tourism Economy.

For the European Union, there is less leverage between both parts of the value added and they tend to move more in step. In general, these charts illustrate how small yet positive changes in the Travel & Tourism Industry, especially visible in the Russian charts, result in a much greater impact on the broader Travel & Tourism Economy.

In the second set of charts (Cumulative Real Growth), Russia’s Travel & Tourism Economy shows significant growth in the 1990s after the collapse of the Soviet Union, with an understandable short-term hangover following the surge. Also evident is the strongly positive outlook for growth over the next ten years. Overall, this level of growth is much stronger than for the European Union overall, which continues to post positive, but more modest gains.

The third set of charts (left) compares WTTC/OEFl’s estimates for Russia and its neighbouring and competing destinations, showing respective Travel & Tourism Economy GDP as a percentage of total GDP. Ranked in 124th place among 174 countries – ahead of Latvia in 153rd position and below Ukraine in 110th place – Russia is currently among the lower-tier, tourism-intensive countries of the region and the world. However, the second league table extract illustrates how Russia’s prospects for GDP growth are also better than for most of its neighbours and competitors within the regional and world ranking – in fourth and 17th position respectively.
The largest component of capital investment originates from the private sector in new plant and equipment, while the public sector invests in new Travel & Tourism infrastructure.

This represents the continuation of significant capital investment growth in the Russian Travel & Tourism economy since the mid-1990s. Over the next ten years (2007-16), the contribution of Travel & Tourism to Russia's capital investment account is expected to increase at an average rate of 9.3 per cent per annum in real terms.

Examination of Travel & Tourism Capital Investment results and forecasts lends greater insight into the market forces at work in a given economy and the expectations by the public and private sectors to meet the challenges and opportunities in the years ahead. For the most part, Travel & Tourism Capital Investment tends to be cyclical, with strong links to major public policy initiatives, the business/market cycle, major events (such as natural disasters) and significant socio-political changes.

Worldwide, Travel & Tourism Capital Investment is expected to generate 9.3 per cent of total investment in 2006. The expectation for global growth from 2007-16 is 4.6 per cent per year (in constant US dollars). In the European Union, the respective figures are 8.6 per cent of total capital investment in 2006 and 4.2 per cent real growth over the coming decade.

The charts on the right illustrate several interesting points. First, Russia’s Travel & Tourism Capital Investment is expected to show steady significant growth following its early 1990s’ jump and retrenchment. Second, when compared with neighbouring and competing countries, Russia’s ranking is favourable if not modest – as it is in the broader listing of 174 countries in investment percentage terms for 2006. With Travel & Tourism estimated at 12.1 per cent of total investment, Russia ranks 77th in the world listing, behind Ukraine (35th place).

However, Russia’s Travel & Tourism Capital Investment growth prospects for 2007-16 place it at the absolute top of the WTTC league tables – in first position in the regional and second position in the world listings. This ranking sends a positive message to Travel & Tourism operators at home and abroad that Russia is well positioned and absolutely expects to attract significant new business ventures over the coming decade.
In 2006, Russia is expected to generate RB1.1 trillion (US$37.4 billion) of personal travel & tourism consumption by residents, or 7.8 per cent of total personal consumption.

In Russia, business travel in 2006 is expected to total Rb49.8 billion, or US$12.1 billion (88 per cent corporate, 12 per cent government).

Unlike visitor exports, which depend on international markets for consumers, the business generated in these two categories depends on Russia’s economy itself. As the national economy grows, Russia’s consumer and business travel tends to follow suit. In the early 1990s, Russia’s Personal Travel & Tourism enjoyed a rapid period of growth following the change of government. Over the next decade (2007-16), Personal Travel & Tourism in Russia is expected to grow at an annual rate of 5.8 per cent, while Business/Government Travel is forecast to grow by 4.9 per cent a year.

Although most of this Travel & Tourism occurs domestically within Russia, a part of it takes place outside the country. When the spending does take place abroad, the satellite account generates a corresponding ‘import credit’, providing for an accurate assessment of Travel & Tourism ‘produced’ in Russia and Travel & Tourism ‘produced’ by the rest of the world.

Analysis of Russia’s results highlights a few interesting points. First, Russia’s residents have recently been allocating only about 7.8 per cent of their personal expenditures on Travel & Tourism. This percentage is only slightly below the world average of 9.5 per cent, yet much lower than the European Union average of 11.3 per cent. Generally, the level of personal Travel & Tourism spending is directly linked to the development of the resident economy. As per capita income increases, so does Travel & Tourism spending.

Russia’s overall macroeconomic situation since the mid-1990s has been reflected by the strongly positive trend of Russian residents’ spending on Travel & Tourism, as illustrated by the stacked bar and cumulative growth charts on the left.

Nevertheless, even discounting the early 1990s’ surge, the cumulative growth charts for Russia and the European Union illustrate the strong future growth outlook for Russia – well above that for European Union Travel & Tourism spending. If, as expected, the economy continues to show positive growth, Russia’s residents’ spending on personal and business Travel & Tourism is also likely to accelerate.

Finally, the league table extracts also suggest that, while Russia ranks in the upper to middle tier of countries (70th position in the ranking) in terms of current Travel & Tourism spending on a relative basis, it ranks much more favourably in the worldwide listing (38th) in respect of future forecast growth of personal Travel & Tourism. This suggests there is significant opportunity for generating and producing Travel & Tourism services in Russia for Russians in the years to come.
In 2006, Travel & Tourism Services and Merchandise Exports for Russia are expected to total Rb593.4 billion, or US$20.6 billion – 42 per cent from visitors and 58 per cent from exported consumer and capital goods – representing some 22 per cent of total Travel & Tourism Demand. Without question, as this category grows, it will enhance the health and vitality of Russia’s Travel & Tourism sector.

Over the past 15 years, the gains for Travel & Tourism Visitor Exports in Russia have been impressive, while only a couple years of decline have tempered this march forwards. Over the next ten years, Russia’s Visitor Exports are expected to grow by a strong 7.5 per cent per annum, while Travel & Tourism Merchandise Exports (non-visitor exports) are forecast to record healthy growth of 4.7 per cent per annum.

Globally, and for the European Union, Visitor Exports are projected to grow by 4.9 and 4.3 per cent per annum respectively over the next ten years (2007-2016).

Clearly, based on these forecasts, Russia’s Travel & Tourism Visitor Exports’ growth is excellent and well ahead of its regional and global peers.

Although long-term expectations for Russia’s Travel & Tourism export growth (2007-2016) are positive, these forecasts – like any others – depend on future events and can therefore not be guaranteed. Hurricane Katrina in 2005, for example, which had a major negative impact on tourism in the Gulf Coast of the USA, is a perfect illustration of the uncertainty inherent in forecasting.

Examination of the WTTC league tables reveals that Russia is lower on the scale of current Visitor Exports measured as a percentage of total exports. In the second league table, Russia’s Visitor Exports’ growth illustrates the positive outlook ahead, since it ranks in 19th position globally. This ranking implies there is a need for the public and private sectors to pay significant attention to maintaining international visitor growth at these high levels.
IN 2006, GOVERNMENT AGENCIES IN RUSSIA ARE EXPECTED TO SPEND RB104.4 BILLION (US$3.6 BILLION) OF CURRENT OPERATING FUNDS ON TRAVEL & TOURISM.

This represents 2.7 per cent of total government expenditures, which are allocated to providing individual and collective government Travel & Tourism services to visitors, travel companies and the community at large. Over the next ten years (2007-16), Travel & Tourism Government Expenditures in Russia are expected to increase by an average of 3.2 per cent per year in real terms.

Globally, governments are forecast to allocate an average of 3.8 per cent of their expenditures to Travel & Tourism-related functions, and to increase this spending by 2.6 per cent per annum over the next ten years. The corresponding figures for the European Union are 3.2 per cent of total government spending and 1.7 per cent real growth for the coming decade. Based on these results, Russia’s 2006 government contribution of 2.7 per cent is currently well below the level of its regional competitors and global average in terms of Travel & Tourism support and services.

In this WTTC report, 2006 government expenditures include individual expenditures of Rb31.7 billion (US$1.1 billion) that can be linked to individual visitors, such as immigration services. But they also include collective expenditures of Rb72.7 billion (US$2.5 billion) that are undertaken for the community at large – such as on airport administration – but which have a logical service connection to Travel & Tourism.

One would naturally assume there should be a direct link between the impact of an industry/sector like Travel & Tourism on the economy (in terms of GDP) and the amount of funding allocated by governments towards that industry/sector. In Russia, the 2006 ratio of Travel & Tourism GDP (percentage of total GDP) to government expenditures is 2.9:1.0. Worldwide, and in the European Union, this ratio is 2.7:1.0 and 3.4:1.0 respectively. This would suggest that Russia is approximately on par with the world average while the European Union government authorities generally, are giving significantly less back to Travel & Tourism than governments in the rest of the world.

The league tables opposite reinforces this particular point. First, Russia’s government expenditures for Travel & Tourism are more in line with developed countries than developing countries, ranking the country 116th out of 174 worldwide. However, more disappointing is the outlook for growth. In this measure Russia ranks fifth among its regional neighbours and 100th worldwide.
While outbound travel from Russia has flourished, the events of the past 14 years have not provided a favourable environment for developing a new style of inbound Travel & Tourism industry, and liberalization has brought with it confusion, operational difficulties and, in many areas, lower standards of service.

As a result, Russia’s share of world Travel & Tourism Demand is currently only 1.4 per cent, and Travel & Tourism Industry jobs account for a mere 1.3 per cent of total employment in the country – or 2.4 per cent, if jobs in all sectors related to Travel & Tourism are included in the count. This confirms that Russia is punching well below its industry weight for a country of its size, location and history.

During the communist era, the government did not consider the Travel & Tourism industry an important or effective means of generating hard currency. Successive governments of the Russian Federation have had many more pressing concerns than Travel & Tourism and have therefore offered the industry negligible support. Meanwhile, although the economy has shown strong growth over the last 6-7 years – ie since the financial crisis of 1998 – the business environment in Russia is still not very conducive to growth in Travel & Tourism.

The taxation and legal framework has been very slow to develop and taxes are complex and punitive. Legislation governing foreign investment and property ownership remains confused and confusing, and there has been a lot of negative publicity about the high cost of Travel & Tourism in Russia, as well as about widespread crime and a breakdown in law and order.

Russia’s visitor arrivals plummeted in the early 1990s, but began to regain previous levels by 1995. Most of the growth in the second half of the 1990s was from former USSR member countries, now the Commonwealth of Independent States (CIS), and under the category ‘other private’ visits, which comprise visits to friends and/or relations and trips (even same-day trips) for shopping and shuttle trading. However, many of these markets have shown steady declines since 2000.

International business traffic from Western markets and Asia has generated the highest yields over the past ten years, and the strong operating performances of four- and five-star hotels in Moscow reflect the sustained buoyancy of this segment of the market.

However, except to St Petersburg, it is arguable as to whether real holiday/leisure travel from non-CIS markets has shown much growth at all since 1991, or even recovered its level of the late-1980s. (Many of the arrivals officially termed holiday/leisure are in fact business travellers in disguise since it is easier and quicker to obtain a leisure visa.)

Travel & Tourism infrastructure has suffered from a lack of confidence on the part of both domestic and foreign investors during much of the 1990s and early 2000s, with capital flight continuing to be a serious concern. But infrastructure weaknesses have also been a major deterrent to Travel & Tourism growth. Strategic investment by government for improving airports, roads, museums and historic sites is still sorely inadequate.

In the hospitality sector, while there has been strong interest from international hotel groups to establish a presence in Moscow and St Petersburg, in terms of management or franchise contracts – and even in a growing number of secondary cities – joint-venture projects have been relatively few and far between. Foreign investor confidence has improved significantly since 2004, but many potential foreign investors say the
partner, Oxford Economic Forecasting (OEF), are fairly bullish about Russia’s Travel & Tourism prospects, but with reservations. Travel & Tourism Demand is forecast to grow by 6.5 per cent annually from 2007 to 2016 and Travel & Tourism GDP should rise by 6.4 per cent a year over the period, increasing its share of total GDP from 7.8 per cent in 2006 to 9.1 per cent ten years later. Meanwhile, capital investment in Travel & Tourism is projected to increase by 9.3 per cent annually, although its share of total capital investment in Russia will remain unchanged at 12.1 per cent.

Much less optimistic are WTTC/OEF’s forecasts for Travel & Tourism employment. Employment in the wider Travel & Tourism Economy, which is estimated at 6.6 per cent of total employment in Russia in 2006, is expected to rise by 1.5 per cent annually over the next ten years, taking its share to 7.7 per cent. But direct Travel & Tourism Industry employment, which currently accounts for a mere 1.3 per cent of total jobs in the country, is projected to stagnate.

The challenge for the Russian Government is to prove that it is capable not only of achieving these growth forecasts, but also of exceeding them. The private sector can and must play an increasingly proactive role in developing quality products and services geared to international and domestic demand. But it is up to the federal government to show leadership by encouraging and facilitating investment, building infrastructure, and streamlining and co-ordinating tourism-related policies and activities with regional governments and local authorities. This will help ensure an integrated approach to tourism development and management.

Against this background, WTTC recommends that the Russian Government:
RECOGNIZE TRAVEL & TOURISM AS A STRATEGIC DEVELOPMENT PRIORITY

Not only must the Russian Government factor Travel & Tourism into mainstream policies, it must also ensure that all public and private sector stakeholders recognize Travel & Tourism’s full impact across the national economy. This will involve an industrial image campaign and the implementation of tourism satellite accounting as a tool for planning and policy development.

Give greater priority to Travel & Tourism…

The lack of priority accorded to Travel & Tourism by successive governments over the past 14 years may be understandable. Yet it highlights the fact that the potential of the industry as a catalyst for the development of other areas of economic activity, such as agriculture, manufacturing and financial services, has been seriously underestimated. There are signs of change, such as the establishment of the Federal Agency for Tourism in November 2004, reporting directly to the Prime Minister. But progress in creating the right operating environment to stimulate tourism growth is still very slow.

Travel & Tourism has the potential to diversify Russia’s economy which, while seemingly unnecessary today, may prove very welcome in the future. It can stimulate entrepreneurship – particularly among small and medium-sized enterprises (SMEs) – catalyse investment and create large numbers of sustainable jobs. It can also help social development in local communities by reducing the disparities between urban and rural areas which, in turn, could bring major improvements to poorer Russians’ quality of life and well-being.

…and factor it into mainstream policies

Travel & Tourism should be factored into mainstream policies for employment, trade, investment, education and environmental protection. The strategic importance of Travel & Tourism should be communicated to all levels of government, industry and local communities. All government departments impacted by, or impacting on, Travel & Tourism development should be closely involved in drawing up a National Tourism Policy and in planning and co-ordinating individual programmes.

Undertake an image campaign to promote its economic importance

The government should undertake an industrial image campaign to ensure that all public and private stakeholders recognize Travel & Tourism’s full impact across the national economy – not just on eating and drinking places and retail business, but also on construction, real estate and other sectors of the economy. Even more importantly, stakeholders should be made aware of its untapped potential and of the spin-off benefits of tourism that filter down through all levels of the community.
The government should also consider convening a National Tourism Congress, which would bring domestic and foreign stakeholders together to discuss Travel & Tourism challenges and opportunities for Russia. This would be an effective way of promoting the importance of the industry to public and private sector decision-makers.

**Implement tourism satellite accounting on an annual basis**

Travel & Tourism needs to be effectively measured in order to understand its full impact throughout the economy. As a new industry, it is not discretely identified in charts of national or state accounts – its component parts are scattered throughout the accounts. Public sector analysis and related policies tend to overlook, or understate, the impact of the industry, or deal with its smaller individual components.

The technique of satellite accounting is designed to measure the new service sectors, and this Tourism Satellite Account (TSA) developed by WTTC and its research partner OEF, should prove to be a significant tool for planning and policy development. WTTC urges the Russian Government to assume responsibility for developing a TSA on an annual basis to ensure that adequate data is available to factor Travel & Tourism into economic and employment strategies.

**EMPOWER THE NATIONAL TOURISM ADMINISTRATION TO DRIVE FORWARD TRAVEL & TOURISM DEVELOPMENT**

Although the Federal Agency for Tourism has a certain autonomy, reporting directly to the Prime Minister, it has such a small budget that it cannot be as effective as it needs to be, especially in terms of marketing and promotions and in coordinating Travel & Tourism development at national, regional and local levels. This situation needs to be resolved urgently.

**Create a national tourism administration with teeth**

The national tourism administration (NTA) during the Soviet era was split between three bodies: the State Committee for Foreign Tourism (Goskominturist), with Intourist as its operating arm; the Tourism Committee of the Central Council of Trade Unions; and the International Youth Travel Bureau, with Sputnik as its operator. This structure was quickly dismantled after the collapse of the Soviet Union, and a new framework, on more familiar international lines, was gradually built up.

In 1995, presidential approval was given to a document elaborating a concept of tourism development in Russia. The document provided a detailed assessment of tourism in and to the country, identified areas requiring state support, and drafted a legal framework in line with legislation considered common practice in other countries for the development and management of a modern and competitive tourism industry.

Based on this concept, the government drew up a kind of national tourism strategy, *The Development of Tourism in the Russian Federation*, which laid the foundations for state regulation of tourism activity and determined the main directions of its development. However, this strategy gave little space to the role of the NTA. Six years later, in 2002 – very little actually happened to turn the strategy into an action plan in the intervening period – *The Concept of Tourism Development in the Russian Federation* up to 2005 was approved by government. This was followed by the current federal law *On the Foundations of the Tourism Industry in the Russian Federation*.

One of the reasons that Travel & Tourism suffered over the 1990s and early years of this decade was that it was not rated a priority by government, and the NTA was constantly shunted around from one ministry to another. Finally, in November 2004, in a move that was seen as very positive for tourism, Russia’s Federal Agency for Physical Culture, Sports and Tourism – the NTA at the time, which came under the aegis of the Health and Social Development Ministry – was split into two independent agencies: the Federal Agency for Physical Culture & Sport (Rossport) and the Federal Agency for Tourism (Rosturizm). Rosturizm was taken over by Vladimir Strzhalkovsky, the former Deputy Minister for Economic Development & Trade, within which ministry tourism had been located in an even earlier incarnation.

Most importantly, both agencies report directly to Prime Minister, Mikhail Fradkov. Also good news for the industry is the fact that Strzhalkovsky has both public and private sector experience in Travel & Tourism. In addition to being responsible for tourism when it came under the Minister for Economic Development and Trade, he was also the founder of St Petersburg’s leading tour operator, Neva, which is the sixth biggest in the country in terms of turnover. So he is already very familiar with the industry, as well as fully recognizing its potential for diversification of the Russian economy.

In addition, he and his 92-strong team have firm ideas on how to address the weaknesses and inefficiencies of the system and reduce some of the many barriers to growth.

Sadly, this does not appear to be the case in the upper echelons of the Russian Government, and especially not with those holding the purse strings. Rosturizm has an estimated budget of just Rb110 million for 2006 (US$3.9 million) – only a modest increase on 2005’s annual budget which, itself, was virtually unchanged over its level of the previous three years. As detailed below, this is less than 20 per cent of the budget for the city of Moscow. Moreover, most of the marketing and promotional spend goes on participation in travel trade fairs, or even travel generally, with little money left over for promotional campaigns or advertising.

Clearly, if Russia’s Travel & Tourism is to make any real impact in the global marketplace, a far greater investment needs to be made into raising the profile of Rosturizm and establishing the brand ‘Russia’ abroad.
The weaknesses of Russia's Travel & Tourism structure and the challenges facing the industry are well documented in a report entitled *The Current Status and Problems of Tourism in the Russian Federation*, which was published by the National Tourism Academy in mid-2004. The report, which was approved by the Presidium of the National Academy, covers — in addition to legislation (or lack of) — key issues of interest and/or concern to the Russian Travel & Tourism industry, such as social tourism, consumer protection, etc.

The two most important bodies responsible for tourism in Russia are the Federal Agency for Tourism (Rosturizm) and the Committee for Economy and Tourism in the Duma, or State Parliament.

Most of the existing laws applying to tourism activity — such as the licensing of tour operators and travel agents, or the classification of hotels and other accommodation — are archaic and badly need revising. Moreover, they do not cover transport, gaming or attractions, for example, which come under different legal systems. Laws are being updated on an ongoing basis, although little progress in implementing these new laws, or even getting them past the Duma, appears to have been made to date.

The perception is that the government has been more concerned with focusing on laws that require changing in line with Russia's application for membership of the World Trade Organization. All legislation comes under the Ministry of Economy and the Duma deals with approval of laws.

**Role and responsibilities of the Federal Agency for Tourism**

Rosturizm has a staff of 92 who are spread across five departments with three deputy heads responsible for:

- Legislation, including the licensing of tourism activities and other administrative issues;
- The development of domestic tourism, state tourism projects, regional co-ordination and investment policy; and
- Analysis and forecasting, the organization of hotels and the travel trade, quality standards, marketing and promotions and international co-operation.

In 2006 a new action programme for tourism development is expected to be implemented by Rosturizm. An intrinsic part of this programme will be an ongoing dialogue with the regions through the establishment of a permanent committee.

**Regional tourism authorities**

Tourism administration at regional level is handled by regional committees supported by regional governments. Small districts have local tourism officers. The regional committees vary considerably in prestige and effectiveness, with Moscow and St Petersburg possessing the highest profile organizations. But, while the Moscow Committee for Tourism claims to have an annual budget of over US$20 million, the North-West Russian capital's tourism authorities are almost impoverished by comparison.

St Petersburg's 300th anniversary may have resonated all over the world, but the initial city budget for tourism development and marketing in 2004 was cut by more than 80 per cent, leaving just Rb6 million (US$230,000) for promotions. There was no increase in 2005, but industry reports suggest that a significant increase has been approved for 2006.

Moscow, meanwhile, enjoys a very privileged situation due to its direct link to the office of the city's powerful Mayor, Yury Luzhkov. Through its joint-stock company, GAO Moskva, the latter is also responsible for the building and renovation of hotels in the city, the handling of the municipality's stake in some properties, the certification of hotel and tourism services, the training of tourism personnel, the development and management of tourism transport companies in the city, managing the municipal interests in a number of the city's hotels, and co-ordinating Moscow's presence in exhibitions and promotion of the city.

Some believe there is a conflict of interest between GAO Moskva's own commercial activities and its administrative or regulatory roles, which is also a cause of concern among the city's other tourism-related enterprises.

In 2003, the Moscow Committee for Tourism set up its own committee for co-ordination of regional activities and policy. It currently has about 50 regional/local tourism administrations as members and is aiming to increase this number to over 80. While the committee appears to carry out some useful activities on behalf of the regions, such as joint promotions abroad, and support in regional tourism development, it appears to duplicate an important role of Rosturizm.

In St Petersburg, the Committee of Tourism and Resort Development outlines its responsibilities as regulating and promoting the tourism industry in the city and region, as well as drawing up a development plan. It controls the activities of tourism-related companies in the city and region, and issues licences and certificates to operators, agents and hotels. It has the power to halt a company's operations until arbitration takes place. It is also involved to varying degrees with hotel development, transport, tourism training and in tourism exhibitions both in St Petersburg and abroad.

The lack of funding over the last few years from the local authorities has prompted a number of the city's hotels and cultural attractions to jointly fund some promotional campaigns abroad. The most prominent has been the White Days' campaign — promoting tour packages during the less popular winter months.

**Industry associations and organizations**

The first international-style tourism associations started to emerge in Russia in the early 1990s. The institutional principles of tourism public
organizations, tour operators’ and tour agents’ associations, as well as tourist unions, were laid down in the federal law On the Fundamentals of the Tourism Industry in the Russian Federation. Among those created in 1993–94 and functioning today are:

The National Tourism Academy, which comprises over 450 members – researchers, university lecturers, members of tourism administrations, deputies of all levels, heads of tourism companies, etc – from practically all Russia’s regions. The Academy takes an active part in the life of the tourism community, contributing ideas for the shaping of state policy, carrying out legal work, studies and research projects, as well as publishing research and other reports.

The Russian Union of Travel Industry (RUTI) was founded in 1993 as the Russian Association of Travel Agencies (RATA), but changed its name to reflect its growing membership from all sectors of Travel & Tourism. It is a voluntary non-commercial association headquartered in Moscow with some 900 members nationwide and a growing network of regional divisions. The North-West division, set up in 1995 in St Petersburg, is the most influential of these. It also has representation in seven countries abroad.

RUTI takes an active role in helping Rosturizm and other government ministries and departments draft the basic laws on tourism, as well as contributing to federal and regional programmes of tourism development. It collates and publishes statistics on tourism to and from Russia, in co-operation with the State Statistics Committee (Goskomstat), as well as publishing an e-newsletter and other tourism promotional material.

Among the other organizations and associations in the field of tourism the most important is the Russian Hotel Association. Other active bodies include the St Petersburg Association of Tourism and Excursions Workers, the National Tourism Administration (which groups Moscow companies operating in the Travel & Tourism industry, and the Association of Travel Exhibition Companies.

Tourist Information Centres

One of the few examples of public-private sector partnership are tourist information centres (TICs), which offer assistance to tourists – e.g. distributing multilingual maps and guides, or helping translate signs and giving advice in foreign languages. Although they are few and far between, especially outside Moscow and St Petersburg, EU funding has helped set up TICs in a number of cities, including Petrozavodsk, Murmansk, Archangelsk and Great Novgorod. The funding has come through programmes such as TACIS (Technical Assistance to the Commonwealth of Independent States) and INTER REG. In line with regulations, these are generally non-commercial partnerships with the participation of interested local or regional organizations and companies.

Ensure more effective marketing and promotion

Annual spending on marketing and promotion by Rosturizm is negligible. This does not augur well for Russia’s Travel & Tourism growth, and funding should be increased to allow Rosturizm to drive forwards the development of Travel & Tourism in Russia. Advertising and media marketing are important to enhance the image of the destination, to generate demand and to promote new products. It can help reduce the concentration of demand in time and space and spread the benefits of tourism more equitably across the country.

Due to existing federal government legislation on competition, there is reportedly no possibility of a public-private sector national tourism organization (NTO) being set up in Russia, along similar lines to existing public-private sector partnerships in most West European countries. This is a pity.

However, as a minimum step, it is important for Rosturizm to work in close co-operation with the private sector, as well as with regional tourism authorities, to improve marketing and promotion – not least e-marketing, at which the private sector is generally much more competent – and to stretch advertising dollars.

Private sector contributions to advertising and promotional spending are also important. But there are many different ways of supplementing government funding with contributions from the private sector in addition to direct contributions, such as through bednight taxes in hotels and similar establishments. However, Rosturizm should take full responsibility for advertising and media marketing spend to promote tourism in the less developed rural regions in an effort to kick-start tourism growth.

Establish foreign offices or marketing representation abroad

In pre-perestroika USSR, the NTA – through its operating arm, Intourist – had more than 30 offices in key foreign source markets. Today, although some private companies assume some of the activities of an NTO, such as brochure distribution, advice on visas, etc, Rosturizm has no official representation abroad. There has been talk of establishing a presence in some markets and, whether this took the form of an official Rosturizm office or marketing and PR representation, this would be a very important step in driving the industry forward and in raising awareness of Russia as a tourism destination.

Due to existing federal government legislation on competition, there is reportedly no possibility of a public-private sector national tourism organization (NTO) being set up in Russia, along similar lines to existing public-private sector partnerships in most West European countries. This is a pity.
PLAN FOR THE FUTURE

Long-term planning is critical for the sustainable development of Travel & Tourism, and this should include the elaboration of a National Tourism Policy, or Masterplan, in consultation with the industry and other stakeholders. It is also essential to monitor Travel & Tourism trends, for example, by implementing international and domestic visitor surveys, to ensure that quality statistics and information feed into policy- and decision-making processes.

Look to the long term

Long-term planning at the national level is a prerequisite for the successful development of Travel & Tourism in Russia. The industry is fragile and likely to be adversely affected by short-term political considerations. The development of a Tourism Masterplan, which is due to be completed by Rosturizm in 2006, should be incorporated into a formal National Tourism Policy. This Policy must start from a vision of what kind of Travel & Tourism Russians wish to develop – in physical and marketing terms. The Policy must include certain basic elements:

- Clearly defined goals, objectives and responsibilities;
- Indications of best practice in tourism development;
- Measures to support existing industry, as well as for the promotion of new developments;
- An articulated strategy for product diversification;
- A long-term strategy for tourism marketing and promotion in line with the Policy’s long-term goals and objectives; and
- Clear branding that reinforces the basic vision for Russia’s Travel & Tourism development.

In order to ensure greater support and commitment from all stakeholders, the government should also initiate a more cohesive and co-operative approach to longer-term tourism planning and development, involving all levels of government, the private sector and local communities.

Meanwhile, the government should commit to using money generated from the privatization of hotels and other tourism assets for re-investment into rural areas of the country. This will not only be an important step towards spreading the benefits of tourism more equitably across the country, but will also help diversify the destination’s tourism appeal.

DEVELOP THE HUMAN CAPITAL REQUIRED FOR GROWTH

The Russian Government needs to work with the private sector and academia to develop the human capital required for Travel & Tourism growth and promote a positive image of the Travel & Tourism industry as a provider of jobs and careers. Compensation also needs to be brought in line with that in other sectors of the economy, so that the value of the top-quality employees is not undermined.

Monitor trends in Travel & Tourism demand

The transition from a centrally planned to a market-based economy severely disrupted the collection and analysis of data in Russia. In addition, because of tax avoidance, much private sector activity reportedly goes unrecorded. So official statistics on trends in Russia’s Travel & Tourism are unreliable and can, in some cases, be confusing.

In order to plan ahead better and anticipate necessary changes to tourism supply, it is essential to monitor trends in past and current Travel & Tourism demand. This will help identify threats to growth, as well as new opportunities.

Monitoring demand trends on a regular basis implies the provision of good quality statistical data on Russia’s Travel & Tourism, including data on international visitor arrivals and departures, domestic tourism, hotel operating performance, expenditure patterns, attitudes and preferences, as well as on the overall economic contribution of Travel & Tourism.

A national Tourism Forecasting Council (TFC) – established along the same lines as Australia’s successful TFC, in which all stakeholders are well represented – could be a useful tool for ensuring the credibility of historical results and future demand forecasts. It could also help to anticipate future capital investment and infrastructure needs, mitigating serious supply shortages or oversupply.

Rosturizm needs to work closely with industry organizations and associations such as the Russia Union of Travel Industry (see box on page 44) to encourage the private sector to share data and other information on operating performance and market trends. It is important to build up the trust and confidence of hotels, tour operators, travel agents, etc, so that they share their data, which is vital to the successful future of the country’s tourism business. In more general terms there is a need throughout the country for a new approach to using statistical research for business development and the government should take steps to encourage this.

Adapt the growth in jobs to that of Travel & Tourism Demand

Research by WTTC/OEF shows that, in 2006, Travel & Tourism in Russia will account for some 4.5 million jobs – around 863,000 directly within the industry and a further 3.6 million in sectors linked to Travel & Tourism, such as real estate, construction and retail. For a country the...
size of Russia, which has the potential to increase Travel & Tourism Demand by 6.5 per cent a year over the next ten years, the WTTC/ OEF employment growth forecasts are extremely modest.

Travel & Tourism Industry employment is expected to increase by only 0.3 per cent annually between 2006 and 2016, while Travel & Tourism Economy employment will rise by a projected 1.5 per cent. This low level of growth will simply not be sufficient to service the needs of the industry going forward.

Although well down on target in terms of performance, Travel & Tourism in Russia over the past decade has nonetheless grown in terms of hotel capacity – admittedly, mainly in Moscow and St Petersburg – as well as in the number of travel agencies and tour operators, ground handlers and attractions. And this has highlighted the severe shortage of trained personnel in all sectors of the industry.

There are approximately 275 colleges or other educational establishments offering higher education in Travel & Tourism in Russia, specializing in subjects as diverse as management, business economics, social services, history and geography. Among the best is the International Institute of Hotel Management and Tourism (MIGMT), which has received the ‘TedQual Audit’ certification from the World Tourism Organization.

However, there are only a few state-owned institutions that offer tourism-related courses. All others are either privately run, or are technical universities providing training as part of the course. And the biggest problem is the absence of training for staff at tourism establishments. At the moment, there is no prescribed training for hotel staff, tour operators or travel agencies. This is clearly a problem, and one that will be exacerbated as demand for inbound tourism grows.

**Educational reform needs to go further**

Although educational reform is underway generally in Russia, foreign hotel groups and some local companies, such as Aeroflot and Intourist, are finding that they have to organize their own on-the-job training courses to ensure that their staff are up to scratch. For foreign companies, this adds to the day-to-day difficulties of operating in the country.

Most travel companies in Russia are also small businesses, with between 2-15 employees, so they have neither the time nor the financial means to train their staff. They therefore need employees with a minimum basic knowledge and practical experience. Yet the level of education and training given by the existing colleges and institutes is considered totally inadequate.

There has been some support in terms of practical tourism training of staff, particularly in the North-West region, through the European Union’s TACIS programme, but this represents a drop in the ocean.

Some new undergraduate and post-graduate courses are being developed, but there is now increasing concern in the industry that, since demand is so high for such courses, universities and colleges with unqualified teaching staff will decide to offer these courses, undermining the level of the degrees and diplomas awarded.
Beat the ‘brain drain’

Another issue of concern is that universities are increasingly introducing charges for certain courses. In 2002 more than 50 per cent of university students in Russia paid for their education. And the percentage paying in professional training schools and colleges is over 40 per cent. This could have a negative impact on the number of students entering the industry with the minimum qualifications required.

At the same time, potential students who can afford to pay are going abroad to study, where the qualifications are more valuable, and companies are worried that this will encourage the brightest students to look for work abroad after their studies where salaries are currently higher and opportunities more attractive.

Ensure the right kind of supply to match demand

If Russia is to develop the right calibre of human resources within its Travel & Tourism industry, the Ministry of Education needs to work closely with the Federal Agency for Tourism, academia and the industry to ensure that courses at higher educational establishments are relevant to the needs of the industry.

While there is a need for broad-based training, which helps develop a variety of skills and customer service skills, there is also a need for higher academic skills and increased technological know-how. The government must ensure that further education in Travel & Tourism is available at no cost to a much larger number of young Russians.

Promote Travel & Tourism as a positive career choice

The Russian Government should help to promote a positive image of the industry as a key future employer to young people finishing secondary school education, or graduates. Career opportunities in Travel & Tourism can be extremely varied – with upstream suppliers such as hotel designers or airport engineers, or with downstream service companies like retail shops, gas stations, clothing manufacturers and food suppliers. The former depend on travel company purchases, the latter are driven by visitors’ expenditures. There are also jobs in the public sector catering to visitors – such as border inspectors, air traffic controllers and museum attendants.

Contrary to conventional wisdom, jobs created by Travel & Tourism – both directly in and outside the industry – also range across the entire employment spectrum and, in many cases, have characteristics that fit model employment patterns:

As the local industry becomes more sophisticated and more international brands enter the market, there will be a growing number of high-level jobs in different sectors. They will provide an impetus to regeneration and social cohesion by counter-balancing the flow of people to the cities from disadvantaged rural areas. They will provide significant opportunities for women and they will be ideal for young or first-time employees. Most importantly, they should offer widespread opportunities for long-term careers rather than mere jobs.

MAKE SURE THAT PUBLIC AND PRIVATE INFRASTRUCTURE DEVELOPMENT SUPPORTS TRAVEL & TOURISM

Infrastructure is one of the main weaknesses of Russia’s Travel & Tourism industry today and a major deterrent to growth. The Russian Government needs to earmark public and private infrastructure development as a priority to stimulate Travel & Tourism demand and open up the more remote areas of the country.

Infrastructure development should be a priority

Travel & Tourism infrastructure has suffered over the past 14 years from neglect on the part of government and a lack of confidence on the part of both domestic and foreign investors. Although investor confidence has picked up quite strongly, investment in Travel & Tourism projects has been lagging behind that of other sectors.

In terms of major infrastructure projects – on which Travel & Tourism growth also depends – the government set to work in 2004 on a number of initiatives to attract private investment, including setting up the State Infrastructure Fund. Due to become operational in 2006, the fund is aimed at key projects like roads, bridges and runways. Up to 60 per cent of financing can come from the private sector. The Russian Government’s contribution will be funded by oil revenues and money saved on foreign debt servicing through early repayment.

Travel & Tourism infrastructure has suffered over the past 14 years from neglect on the part of government and a lack of confidence on the part of both domestic and foreign investors.

Interestingly, China is one of the major investors currently involved in infrastructure projects. Chinese Telco Huawei Technologies is investing US$3 billion in St Petersburg’s telecoms industry, for example. And Beijing, looking to improve trade ties with St Petersburg, approved a proposal from five Shanghai developers in 2004 to build a Chinatown in Russia’s northern capital – a project estimated at US$1.2 billion.

More recently, Chinese investors have announced that they plan to pour up to US$1 billion in a high-speed toll road between St Petersburg and Moscow. Construction of the four-lane, 650-kilometre motorway was scheduled to start last year and take up to five years to complete. The government said it would cover half the estimated US$6.2 billion project with the other half coming from private investors.
Expand and modernize Russia’s transport infrastructure

Transport infrastructure is undoubtedly the most serious concern at present. Research by the National Academy of Tourism shows that, during the 1990s, the total volume of passenger transport decreased by more than 30 per cent. Although the last few years have seen a reversal of the trend, existing transport infrastructure is not geared to Travel & Tourism and continues to act as a deterrent to growth. Perhaps most serious is the condition of Russia’s roads, even those connecting main tourist centres. But the railways are also badly in need of upgrading, as are Russia’s waterways.

Most of the country’s airports are also not up to world standards although (as is illustrated in the report on page 53), major airports have undergone, or are undergoing massive renovation and expansion. Nevertheless, many of the aircraft flown by Russia’s 200 or so airlines are so old that they no longer meet minimum technical and noise-level norms, so they are not allowed into airports in other European countries.

Modernize Russia’s railways…

Although the idea of a trip on the Trans-Siberian Railway conjures up the image of an epic adventure, the experience is not always as positive as one would expect it to be – simply because so much investment is required to upgrade the product and related service. There are a few isolated exceptions, but Russia’s railways are generally in a very poor condition as a result of years of neglect and under-investment.

The launch of a new luxury rail service between Moscow and St Petersburg in 2005 – the Grand Express – was good news for the tourism industry. The first privately owned luxury passenger train is operated by Grand Service Express but uses the Russian Railways’ (RZD) infrastructure. Meanwhile, there is also talk of developing the infrastructure for a high-speed railway line between the two cities and between St Petersburg and Helsinki.

The Spanish Government reportedly allocated €1.3 million (US$1.6 million) to conducting a feasibility study and the German Siemens was due to develop the trains in a joint venture with RZD – with Siemens designing the trains and RZD being responsible for production. However, the US$1.8 billion project appears to be on hold as RZD is concerned about its lack of rights to the trains’ design.

Also launched last year was a new luxury rail link between Moscow and Kiev, which has reduced journey time from 12 to 9.5 hours. For tourists travelling between Moscow’s airports and the city centre, there are plans to add new rail links. For the time being, only passengers leaving from/travelling to Domodedovo can make the journey by train – and they can check in their baggage at Paveletsky station before taking the 40-50 minute ride.

Now, Sheremetyevo Airport is set to get a direct rail link to central Moscow by summer 2006. The US$100 million project envisions connecting Savolyovsky Station to the airport by extending existing track by seven kilometres. The capital’s third airport, Vnukovo, is also expected to complete a rail link to Kievsy station by August this year.

HOTEL DEVELOPMENT IN RUSSIA

Shortage of hotel capacity is a major bottleneck

The serious shortage of hotel accommodation in Russia’s main tourism centres – particularly of international standard mid-market hotels – is one of the main factors hampering development. Official statistics from Goskomstat suggest that Russia has a total of 177,200 hotel rooms, or 364,000 beds – 50 per cent of which in Moscow – which achieved a countrywide average occupancy of just 34 per cent in 2004.

Moscow attracts primarily upmarket hotels

The majority of new builds and reconstructions in Moscow since the late-1980s have been four- or five-star internationally branded properties (see table on page 19). The preference for upmarket hotels can be explained by the higher economic returns achievable.

Nevertheless, even these are not considered high enough by some developers. A number of projects in Moscow that started out as hotels have been converted in mid-construction to commercial properties because of the faster return on investment expected. And the Canadian-managed Aerostar was closed down for the same reason in 2004 when it was already operating as a hotel.

Simple mathematics explain why development of a two- to three-star hotel is just not economically viable for investors. According to Moscow-based Hotel Development Consultants, a 300-room development for an average cost of US$50 million – US$165,000 per room – must be capable of achieving and average daily room rate (ADR) of US$164. So a 200-room mid-priced hotel, which averages an ADR of US$100, cannot have a development cost of more than US$100,000 per room, or a total of US$20 million. This is not possible in Moscow today.

One of the most long-delayed hotel projects in the capital, the 218-room Courtyard by Marriott, which finally opened in late-2005 – although it was ready to open 18 months earlier – almost never opened as a hotel. Due to reasons that were never made public, builder and owner Baltic Construction Company offered it up for sale for a huge US$73 million, having paid only US$35 million to develop it. Few ever doubted that a buyer for a prime piece of property in central Moscow would be found, although many suspected it would never operate as a hotel. They turned out to be wrong but, at more than US$300,000 per room, ADR and occupancy will have to be much higher than normal for a three-star hotel.

New scheme could further boost investor confidence

City Hall announced plans at the beginning of 2006 to take its first cautious steps toward allowing private ownership of land in the capital. Under federal law, it has been legal to buy and sell land since 2001, but City Hall has yet to extend the law to Moscow, apparently reluctant to surrender dues paid from the leasing of land, one of its major sources of income. As a result, investors are forced to buy buildings with leases on the land for only 49 years – a major deterrent to investors.

The price of land lease payments is one of the biggest variables in investors’ long-term planning. If a building’s owner has land ownership, he has less risk. Under the new trial scheme, applications
to buy the land under 25 residential properties are to be considered in the coming weeks. However, to receive the right to buy the land, the applicant should be the owner of the building and have a perpetual lease. This requirement will severely restrict the number of building owners who can take part.

The first decisions on the privatization of land plots under enterprises are due before April 2006 – but “only for those with socially beneficial activities”. There are now reportedly about 300 applications from enterprises under consideration.

St Petersburg: the leisure capital of Russia
St Petersburg is widely seen as the leisure tourism capital of Russia, but its operating performance falls well short of Moscow’s – primarily because it suffers badly from seasonal imbalances. This makes the city less attractive for hotel investment although, if the number of international groups already in St Petersburg or looking to establish a presence there is anything to go by, it is still seen as a prime location.

The city has nine internationally branded hotels and more are under construction or on the drawing board. In addition, it has attracted a large number of small, deluxe boutique hotels, such as the Casa Leto around the corner from Rocco Forte’s Astoria and Anglettere hotels. Thanks in no small part to the local authority’s efforts to facilitate investment and ease bureaucratic procedures, St Petersburg is also attracting growing investment interest in a whole range of tourism-related projects in the city.

New Holland Island project
One of the latest projects to be launched is the New Holland Island redevelopment, for which British architect Sir Norman Foster will be responsible for the design. A competition, announced by City Hall in November 2005, invited tenders requiring participants to invest over US$300 million and complete the project within seven years.

The British architect’s winning proposal was part of a bid by ST Novaya Gollandia, which has promised to invest US$319 million and complete construction within 30 months. Shalva Shigirinsky, a Moscow-based developer behind ST Novaya Gollandia, says the company will finance 30 per cent of the project’s costs with the rest to be borrowed from various sources.

The triangular-shaped self-sustaining island will provide 7.6 hectares of mixed-use cultural development including an indoor theatre, conference facilities, galleries, a hotel, shops, apartments and restaurants, with a flexible outdoor arena at its heart. The project will regenerate the 18th century New Holland Island, presenting a unique opportunity to transform the city of St Petersburg into the foremost venue for performance and visual arts in the world.

The winning proposal does not include any residential buildings. But offices, a hotel and museum will be located at former military warehouses, while a former navy prison will be converted into a concert hall for 400 people. The project also includes the construction of a House of Festivals for 2,000 people, an open amphitheatre for 3,000, three hotels with 542 rooms and eight bridges.

Growing interest in the regions...
Until now, there has been very little capital investment by foreign companies in hotel development in Russia. A lack of transparency in terms of regulations and procedures, not to mention the other factors cited on page 55, have had a negative impact on investor confidence. As a result, several international hotel groups decided they would rather put their money elsewhere and just look for management contracts.

But the situation is changing as investor confidence returns. The Accor Group now says that Russia is now one of its top three priority development countries, with China and India, for the foreseeable future. It says it likes the idea of taking equity as it believes that joint ventures with Russian companies will have the advantage of allowing the group to influence the nature of the product and location. Accor is currently tripling its staff in the country to help support the regional rollout of Ibis.

...with some mid-market groups planning properties across Russia
Major mid-market hotel chains such as Ibis, Best Western and Holiday Inn, say they are planning significant pushes into smaller provincial cities in bids to become the country’s dominant domestic chain. And still more deluxe and five-star brands, such as Westin, are looking for opportunities.

Best Western signed a franchise agreement in 2005 for a dozen Russian locations, mainly in the regions. In total, it plans 50,000 rooms by 2025 at a cost of US$250 million for its partner, the Bonita Group (30 per cent), with the balance of the investment coming from banks.

In late 2004, USA-based Cendant Corporation signed a deal with Hermitage Hospitality, the local operator of the Days Inn brand, to develop 45 midlevel Days Inn hotels in Russia and 14 former Soviet republics over the next five years.

Delta Capital Management and the operator of Radisson are launching a chain of up to 50 hotels to capitalize on the country’s nascent three-star market. Two European investment funds – Sweden’s Swedfund and Denmark’s The Investment Fund for Central and Eastern Europe – are participating in the project with Delta and Rezidor SAS Hospitality to set up the Country Inn brand hotels. The group intends to own its first hotels in order to ensure their success and build up to 50 hotels throughout Russia by 2012. It has exclusive rights in Russia to the Country Inn brand, which belongs to the US Carlson group.

The first eight hotels will be built in the next two to three years. Each hotel will cost US$5-$12 million and have 80-120 rooms charging US$90 per room per night in Moscow and US$70 in the regions.

Meanwhile, Park Inn was due to open its first hotel in January 2006 in Yekaterinburg, with the brand’s owner, Rezidor, planning to open up to 50 hotels in the CIS by 2012, mostly under the Park Inn Brand. Intercontinental is also planning on putting a Holiday Inn in every town in Russia. A 178-room Holiday Inn opened in central Samara in late 2005, and the 512-room Holiday Inn Sokolniki is slated to open by mid-2006 in northeastern Moscow.

Russian Hotels, a company close to metals conglomerate Basic Element, announced plans last year to invest between US$200 million and US$250 million into a chain of 20-30 mid-market hotels and office centres. They will be located chiefly in the Russian regions and CIS capitals, such as Kiev, Tbilisi, Georgia, and Yerevan, Armenia. The company is negotiating with South Africa’s Protea Hotels to operate its property in Novosibirsk, scheduled for a 2007 opening.
The good news for the rail sector is that, with orders for new aircraft plummeting (see box on page 54), some Russian aircraft manufacturers are looking to beef up their order books by refitting their production facilities to move into a more lucrative market – trains. Aviastar, for example, which once rolled out more than 50 jets a year, produced only two in 2005.

…expand and upgrade port facilities
In terms of port facilities, the Russian Government announced plans last year to build a US$1 billion new port at St Petersburg, capable of receiving and servicing large cruise ships. Current facilities can only service ships less than 200 metres long. The new port will comprise a passenger terminal, hotels, a museum and residential area, and the government has earmarked US$222 million in funds for the project. Private investors are also set to contribute to the development.

Although this cannot be confirmed, the Federal Seaports Management Agency (Rosmorport) was due to invest Rb5.3 billion (US$190 million) in port infrastructure development across the country in 2005 after spending Rb4 billion (US$144 million) in 2004. Of course, the decision is not only about stimulating tourism development; it is more a question of Russia’s competitiveness in terms of cargo transport. In addition to increasing competition from Baltic and Scandinavian ports, Rosmorport is concerned that protectionist tariffs will have to end on Russia’s entry into the World Trade Organization.

Port facilities are also being upgraded in Murmansk, which has opened up for sea cruising. In 2005 it handled six cruise ships taking mostly foreign tourists to the North Pole.

Improve land-use planning and protection
Infrastructure remains a critical component in Travel & Tourism development if the full potential of employment generation, export earnings and regional development effects are to be achieved. And public infrastructure that supports Travel & Tourism expansion will also serve other urban and regional development purposes.

Quality infrastructure is also essential to diversify the product base, remove bottlenecks, ensure good service and distribute the benefits of tourism flows around the economy. It is not only a question of coping with increasing numbers of visitors, but also of making sure that the patterns of flow do not affect the natural or built heritage, nor run counter to local interests.

The Russian Government and the private sector can influence the development of new tourism infrastructure to protect and promote the character of the local environment, developing authentic tourism products that are unique to the country and its culture. Land-use planning should as far as possible remain the responsibility of the federal government so as to avoid the risk of local authorities turning a blind eye to illegal construction, as has already occurred around Lake Baikal (see page 66).

TRY TO GENERATE AN EQUITABLE SPREAD OF TOURISM BENEFITS
The Russian Government’s medium- to longer-term goal should be to ensure that the benefits of Travel & Tourism are spread as equitably as possible across all regions and to all levels of the population since this can reduce disparities between urban and rural areas which, in turn, could bring improvements to Russians’ quality of life and well-being.

Step up investment in the regions to advance community development
According to a report entitled The Current Status and Problems of Tourism in the Russian Federation, which was published by National Tourism Academy in mid-2004, less than 20 per cent of the country is used for tourism purposes. It is hardly surprising, therefore, that recognition of Travel & Tourism’s contribution, or potential contribution, to the national and regional economies is confined to a relatively tiny sector of the population – those living in the big cities and a few other significant tourism destination regions such as the Black sea coast.

Opening up the regions will require increased investment in infrastructure – roads, railways and airports – as well as modernization and expansion of the hotel plant, plus the development of new attractions and facilities such as tourist information centres.

If Travel & Tourism is to be successful as a tool for rural development, it is critical to ensure the buy-in of those communities in which it is based. The Russian Government must incorporate sustainable tourism into the national social and economic policy framework with a focus on:
- local engagement with the industry;
- start up support and technical assistance for entrepreneurs and small and medium-sized enterprises (SMEs);
- ensuring that money from Travel & Tourism benefits all stakeholders in local communities, rather than remaining in the hands of a few major players; and
- partnership with the private sector so that developments, new and old, fulfil the governments targets for social and economic development.

There are already projects throughout Europe that reflect a community-based approach. Examples of best practice from inside and outside the country should be identified, so as to produce models on which to base the further development of such projects in Russia.

Continue to favour the development of special economic zones
The Russian Government and the presidential administration placed increasing emphasis on regional issues during the second half of 2005 and, since the beginning of 2006, they have made this a top policy priority. Prime Minister Mikhail Fradkov has chaired a commission on improving co-operation between the federal and regional governments.
RUSSIA’S AVIATION INDUSTRY

Despite the lack of investment by government over the years, Russia’s air transport industry appears to be thriving, thanks largely to the growth in outbound travel. Russia’s airline traffic increased by 17 per cent in 2004 to 83 billion revenue passenger-km (RPK) and this, coupled with higher airfares, helped Russian airlines achieve US$6 billion in operating revenues – an additional US$1 billion over 2003. Moreover, preliminary estimates point to another year of double-digit growth in 2005.

Major Russian airlines

Aeroflot, which has been designated by government as a “strategic national company”, has existed in various guises for several decades. However, it was established in a new form in 1994, and became a public company in 1995, with the Russian Government owning 51 per cent of the firm’s stock. The remainder is held by Western institutional investors and Russian private shareholders. There are plans for full privatization but this seems to have been delayed.

In 2005, Aeroflot carried an estimated 7.8 million passengers, up 13 per cent, following a 16 per cent rise in 2004. Aeroflot is looking to increase passenger numbers to 12 million by 2010. Profit for the first nine months of 2005 fell 13 per cent due to the soaring cost of fuel (an increase of 52 per cent for the airline) and the fact that some of its aircraft were grounded last year over safety concerns. Net profit in 2004 (an increase of 52 per cent for the airline) and the fact that some of its nine months of 2005 fell 13 per cent due to the soaring cost of fuel (a 16 per cent rise in 2004). Aeroflot is looking for full privatization but this seems to have been delayed.

In mid-January 2006, Aeroflot announced plans to establish a charter flight subsidiary. The structure and business plan of the new company will be finalized by summer, and the company will be launched in late 2006. Contrary to its original plan to take over an existing charter carrier, this airline will be created from scratch, and will be 100 per cent owned by Aeroflot.

The thinking behind the decision seems to be that charter airlines are performing in a market that is growing by 10-15 per cent a year. So Aeroflot wants to ensure it captures a slice of the market. It is also believed to be a way of offloading inefficient aircraft – the new charter carrier will operate six of Aeroflot’s Ilyushin Il-86 planes – so that Aeroflot can acquire more modern Western aircraft and improve its operating performance.

Sibir, Russia’s second largest airline in terms of passenger numbers, with 3.8 million in 2004 (+11 per cent), was recently renamed S7 as part of a rebranding exercise. Sibir/S7 was founded in 1992 as the successor of the Tolmachevo United Avia Squadron, the local subsidiary of Aeroflot, whose first international flight was to Harbin, China in 1991. The airline, which is based at Tolmachevo airport in Novosibirsk but also operates out of two other hubs in Moscow and Irkutsk, recorded a 12 per cent increase in passengers in 2005 to 4.2 million, of whom 36 per cent were flown on international routes. It operates a mixture of Western and Russian aircraft.

Pulkovo Airlines is due to be split from St Petersburg’s airport of the same name this year and merged with Rossiya, the presidential airline. It operates mainly to Europe, but has one service to Asia, to Beijing. In 2005 it recorded a 5 per cent increase in passengers, although international passenger traffic was up less than 4 per cent, following a 12 per cent rise the previous year. Pulkovo operates five Boeing 737s.

Krasnoyarsk Airlines, better known as KrasAir, is the fourth largest domestic carrier in Russia, based in Krasnoyarsk, Siberia. In 2004 it carried just under 2 million passengers on international scheduled and charter services. The airline sprang from the Yenisei airwing (set up in 1934) of the Soviet Aeroflot, the only airline of the USSR. It is owned by Boris and Mikhail Abramovich, two brothers (no relation to Roman Abramovich), whose aggressive expansion campaign led to the creation of AirUnion alliance in 2005, the first airline alliance in Russia. This includes KrasAir, Domodedovo Airlines, Samara Airlines, Omskavia and Siberiatrans, and is the third largest domestic carrier in Russia.

In 2005 KrasAir also attempted to acquire Malev Hungarian Airlines. But the bid was rejected by the Hungarian Government. KrasAir has two Boeing 767s as well as a large number of Russian-built planes, and is planning on expanding its foreign fleet of aircraft.

UTAir is a totally privately owned airline controlled by the oil major, Surgutneftegaz, which bought a stake in 2004. It operates mainly helicopter flights.

Transaero, launched in 1991, and which carried over 1 million passengers on international services in 2004 to more than 150 airports in around 60 countries, is Russia’s sixth biggest airline and gaining in importance as an international carrier. It is an exception among
Russian carriers in having a 100 per cent foreign-built fleet. In 2003 it finished in fourth place in terms of its ranking among Russian carriers, after rising rapidly from a low base in recent years. But it lost share in 2004 due to a decline in domestic traffic, although international passengers increased by 53 per cent to over 1 million.

Transaero operates scheduled services to different countries in Europe, North America and Asia – including Bangkok, Singapore, Manila and Kuala Lumpur (the last three being relatively new additions to its route network).

Leading airports
Russia’s leading airports achieved another year of good growth, according to preliminary estimates – as discussed in the Travel & Tourism Overview section of this report. The most important airports in the country, in terms of passenger throughput, are Moscow’s Domodedovo, Sheremetyevo and Vnukovo airports and St Petersburg’s Pulkovo.

Like Moscow’s Sheremetyevo and Irkutsk airports, St Petersburg’s Pulkovo has been benefiting from EU funding through the TACIS programme. Much of this was related to the planned privatization of the airport, which has not yet taken place, and the separation of the airport and airline of the same name.

Last year, in preparation for the July 2006 G8 summit that will take place in the city, the federal government allocated nearly Rb3 billion (US$105 million) for the reconstruction of St Petersburg’s Pulkovo 2 airport. The work mainly involves replacing the cover of the second landing strip, plus adjacent tracks, as well as providing new lighting, signals, and radio equipment. The federal budget allocated for the project was Rb1.8 billion (US$70 million) in 2005 and another Rb1 billion (US$34 million) in 2006. The work is being carried out by local construction firm Transtroi.

The unusually high investment has been justified by the Russian Aviation Agency in order to upgrade Pulkovo 2’s landing strip to the III ICAO category – a standard rated by the International Civil Aviation Organization as reliable for aircraft take-offs and landings in complicated weather conditions. The upgrade will also allow all types of aircraft, including the Airbus 380 and Boeing 787, to land at the airport. At the moment, only one lane at Moscow’s Sheremetyevo airport is classified as meeting the III ICAO standard, although Domodedovo is due to be granted the certification imminently.

With air travel booming in Russia for the sixth successive year, Moscow’s three main airports – Sheremetyevo, Domodedovo and Vnukovo – have been developing plans to meet growing demand as far ahead as 2020. The three airports are planning on becoming bigger, sleeker and user-friendlier as the competition heats up for the millions of extra passengers per year expected to fly to and from the city. But while the country’s pre-eminent hub for decades, state-owned Sheremetyevo, has been mired in bureaucratic delays, its rivals have been forging ahead with ambitious plans involving large-scale private sector investments.

Experts predict traffic of between 60-65 million passengers by 2020 as against about 30 million in 2005, so there will be enough demand to fill all three airports.

Moscow’s oldest airport is Sheremetyevo, whose existing terminals, Sheremetyevo 1 and Sheremetyevo 2, were built in 1959 and 1980 respectively, and have been operating at overcapacity for years. Aeroflot first announced its intention to build the new terminal 3 in 2000 and originally planned to have it completed by the end of 2004. But infighting between the airport, the airline and various government bodies and officials halted the project after a groundbreaking ceremony in February 2001.

In January 2005, Alfa-Sheremetyevo – a unit of the powerful Alfa conglomerate – won a government tender to manage the airport, but Aeroflot was adamantly opposed to having Alfa run its hub and the tender was never ratified. Meanwhile, Sheremetyevo’s board decided last year to move ahead with a US$70 million overhaul of Sheremetyevo 2, the international terminal, to increase capacity. But the airport has been losing share to the privately owned Domodedovo, since inadequate operating conditions at Sheremetyevo 2 have encouraged an increasing number of international airlines to switch their operations to its rival.

At the same time, last year, it was realized that the new terminal was also crucial to Aeroflot’s development. It would significantly ease congestion at the two existing terminals, while making Moscow a more attractive hub for transit flights between Asia and Europe. The interested stakeholders finally agreed to put aside years of disputes. The third terminal, which will have a capacity of 9 million passengers a year, is due to be built at a cost of US$830 million, and completed in 2007. As with other state airport development plans, it may still not materialize.

However, under the new agreement, Aeroflot will hold 30 per cent in Sheremetyevo 3, the airport will have 25 per cent plus one share, and the rest will go to banks, primarily to state-owned Vneshtorgbank. The construction project will also include a US$310 million upgrade of the Sheremetyevo 2 terminal and the construction of a gallery that will connect it to Sheremetyevo 3. Sheremetyevo 1, which handles primarily domestic traffic, will also be upgraded to handle 5 million passengers a year.

The fastest growing of the three airports, Domodedovo, saw passenger traffic throughput increase by 40 per cent in 2003, 29 per cent in 2004 and 16 per cent in 2005. Passenger traffic on international routes last year totalled 7.8 million, up 23 per cent – or nearly 50 per cent more than growth overall – while domestic traffic, at 6.1 million passengers, increased by just over 7 per cent over 2004’s level.

This strong performance confirms that Domodedovo – which is owned by a private group of diversified companies, East Line – is now Moscow’s major airport by a wide margin, having ousted Sheremetyevo from first place in 2004.

The history of the East Line group dates back to 1993, when the initial company of the future group entered the international air cargo market. It later launched the airline of the same name. Today, the group’s core business is airport management and airport services. These include aircraft maintenance and repair, inflight catering, a jet service fuel facility, East Line ground handling, aviation security and an airport hotel.
With East Line’s investment into facilities of US$500 million, Domodedovo is widely viewed as the best airport in Russia. By the end of 2006 East Line plans to increase the airport’s size to 215,000 square metres, including an all-glass multilevel plaza with parking for 4,500 cars, a hotel and even a supermarket and a cinema, while capacity will increase to 16 million passengers per year.

The first airport to become accessible by rail, Domodedovo is also in talks with Russian Railways (RZD) to build rail links to most of Moscow’s train stations. It currently has one rail link, to Paveletsky Station in central Moscow.

The airport predicts it will serve anywhere between 23 million and 40 million passengers per year by 2020, and is planning to construct three new terminals to meet this demand. Eventually, Domodedovo is scheduled to grow into a miniature city, including a business area with office buildings and warehouses, plus entertainment theme parks and shopping centres for the whole airport catchment area.

East Line’s ambitious plans, not to mention its heavy investments to date, have helped it woo several new domestic and international carriers to Domodedovo, with a number of other airlines, such as Transaero and British Airways, switching from Sheremetyevo. Among foreign carriers, Thai Airways International and Vietnam Airlines operate to Domodedovo from Asia and Emirates links Domodedovo to Dubai.

Vnukovo, the smallest of Moscow’s three airports, is looking to catch up with its two big rivals and is a rare example of successful cooperation in Russia between the public authorities and the private sector. Controlled by Moscow’s City Hall, Vnukovo has profited from the city’s continued construction and development spree under Mayor Luzhkov. In April 2004, the airport completed construction of a second terminal next to its Soviet-era one, taking annual passenger capacity to 4 million, and it opened a third terminal in 2005, raising capacity again to 8 million. From November 2006, Vnukovo plans to begin construction of a fourth terminal at a cost of US$200 million.

In 2004, Vnukovo’s traffic fell 11 per cent to 2.5 million passengers. Until the third terminal was built last year, traffic at the airport overall was limited to 15 daily flights, serving mainly the CIS and top tourism destinations such as Turkey and Egypt. However, things have changed significantly since then. Preliminary results point to 47 per cent growth for the first ten months of 2005, or an additional 1 million passengers.

Two of Vnukovo’s terminals are owned by AO Airport Vnukovo, 61 per cent of which is owned by the Moscow City government and 36.5 per cent by Vnukovo-Invest, which is controlled by management. The third terminal is owned by Vnukovo International Airport, 20 per cent of which is owned by the city and 75 per cent by Vnukovo Invest.

The new terminal, for which the tender has not yet been announced, should be completed by the end of 2007, and will double the airport’s current capacity. Vnukovo also plans to extend one of its two runways and complete its rail link to Kievsky Station with an underground platform at the airport by this August.

**Aircraft manufacturing**

Unlike the country’s airlines, Russia's civil aircraft manufacturing industry is in the doldrums. In Soviet times, domestic aircraft manufacturers such as Tupolev, Illyushin and Yakovlev accounted for more than a quarter of global aerospace production and were a force to be reckoned with by Western manufacturers like Boeing. Now, production and research levels are only a fraction of what they used to be during the Cold War years.

President Putin hopes that opening up the sector (which is still tightly regulated by the state) to private investment will stimulate production by discouraging Russian airlines from switching their fleets totally to Western-built aircraft. But full privatization seems some way off.

One hopeful sign is the planned launch of the Russian Regional Jet (RRJ), the biggest venture in domestic aviation, which lies at the heart of Putin’s ambition to breathe new life into the moribund industry. But the launch will not actually take place until 2008 at least, so it is too early to talk of a change in fortunes for the industry. The decision by Alenia Aeronautica, part of Italian aerospace company Finmeccanica, to buy up to 25 per cent of the Sukhoi-led RRJ venture, has nonetheless given the project global recognition.

Meanwhile, in a move aimed at strengthening the ailing sector, the country’s most famous brands – Sukhoi, MiG, Tupolev and Illyushin – will also be merged into an umbrella company, OAK, at the end of 2006. The government will initially hold between 60-70 percent of the corporation.

Russia’s airlines have also joined forces with the domestic aircraft industry to come up with a plan to rescue the sector, benefiting airlines at the same time. High tariffs on foreign aircraft – leases as well as aircraft purchased – have been hurting business, and Russian airlines complain that they are particularly unfair given the fact that Russian aircraft manufacturers cannot produce suitable similar aircraft.

As a result, they have appealed to the government to lower import duties on foreign aircraft, which add approximately 40 per cent to the price. And, in return for allowing foreign planes to flood the market, domestic manufacturers are willing to boost their share in the production of Boeing and Airbus planes.

Over the past decade, Boeing has invested US$1.3 billion into Russia, employing more than 1,000 engineers and designers who have contributed to the development of jets like the Boeing 787 Dreamliner.

Airbus has a smaller presence, running an engineering centre with a local partner who employs 100 people. But there have been discussions about bringing Russian manufacturers into the production of the new Airbus A350 and making Russia a competence centre for conversion of A320 passenger airliners into cargo planes. The work could generate around US$400 million in revenues for Russian plants over the next 20 years.
The commission has been working on the transfer of powers from the federal government to the regions, as outlined at recent State Council meetings in Kaliningrad and Kazan. It also oversees the progress of administrative reform in the regions.

Whatever the reasons for Fradkov’s increased emphasis on regional affairs (some observers believe that he is being promoted in the regions as a successor to President Putin), WTTC commends the move as it augurs well for Travel & Tourism. In January alone, the government approved plans for six new special economic zones (SEZs) – for technology and manufacturing – and launched a federal programme aimed at developing the city of Sochi (see box on page 58). This was in addition to two federal programmes recently outlined by Putin for the south of Russia and the Far East.

The government has promised to create another three to five SEZs at major ports in the near future. And in April or May the announcement of a competition for a new SEZ aimed at boosting tourism is expected. These and many other indicators make it clear that the regions are once more on the political map.

Some US$1.8 billion has reportedly been earmarked for the development of SEZs in 2006. The main objective of SEZs is to help diversify the economy away from oil towards innovation sectors. Tax breaks and other benefits are offered to companies operating in the zones.

As far as the tourism SEZs are concerned, there are no firm details as to where they will be, but likely candidates are Sochi, given the big investments already taking place there, the Lake Baikal region and Kaliningrad – because of its particular geographical location. Officially an ‘oblast’ (province or administrative region), and a Russian enclave between Poland and Lithuania on the Baltic Sea, Kaliningrad has a seaport city of the same name. Under its previous name, Königsberg, it was the capital of the German province of East Prussia.

**CREATE A COMPETITIVE BUSINESS ENVIRONMENT THAT ENCOURAGES AND FACILITATES INVESTMENT**

Travel & Tourism growth can be inhibited by local market conditions – from incoherence in planning to unfair taxation, inadequate banking and financial services, uncertainties over ownership and land lease regulations, and a lack of transparency in terms of procedures. If Russia is to stimulate and sustain business and investor confidence, the Russian Government must try to create an operating environment that is conducive to investment.

**Encourage and stimulate foreign investment**

As already indicated, there are several challenges that continue to hamper Russia’s attractiveness for both domestic and foreign investors – not least in terms of hotel development. According to WTTC/OEF’s latest economic research, investment in Travel & Tourism accounts for 12.1 per cent of total capital investment, which is more than 50 per cent higher than for member countries of the European Union.

However, for a tourism destination re-emerging onto the world stage after a decade and a half of painful transition to a market-based economy, the level should be much higher. Moreover, the WTTC/OEF forecast 9.3 per cent a year growth in capital investment over the next ten years will not be sufficient to increase Travel & Tourism’s share of total investment in the country, which itself is critical to capacity growth.

Although the mood has lifted significantly since 2004, a number of factors have contributed to damaging business and investor confidence in Russia’s Travel & Tourism over the past few years. Among these, the most important have been concerns over the perceived centralization economy (Boris Yeltsin, had ceded a lot of powers to the regions) and the implications of highly visible corporate sagas.

But local market conditions have also had a very negative impact. These include inadequate state guarantees and incentives for investment, the absence of a clear legal framework, a lack of transparency in decision-making processes, high levels of bureaucracy, and increasing prices for fuel, electricity, water, rent, services, etc – all leading to higher prices for tourism products and services.

The situation in Russia is completely in contrast to, say, China, where bureaucracy is much more supportive, geared to welcoming and guiding foreign investors through the regulatory swamp.

Recognizing the power of international brands to attract high-yield markets and, thereby, to stimulate wealth and job creation, the Russian Government should make strong efforts to address these problems, so as to reassure potential high-profile investors. Care should also be taken to ensure increased transparency in the privatization process, a rapid resolution of land ownership issues and the removal of red tape, as well as to ensure that fiscal policies such as taxation are not harmful to investment.

To stimulate and speed up privatization in the future, the government should consider setting up a tourism investment facilitation centre. Linked to the Federal Agency for Tourism, but also working in close co-operation with other relevant government ministries or agencies, this would act as a one-stop shop for private investors.

**Progressively open up Russia’s skies**

The number of new airlines operating to Russia has grown significantly in the last couple of years, and Russia’s leading gateway airports are all undergoing massive renovations and expansion. WTTC commends the Russian Government’s forward-thinking approach to airport privatization, which has already proved beneficial to Moscow. Nevertheless, the country is still perceived as a tough negotiator when it comes to granting foreign airlines traffic and overflight rights.
RUSSIA’S TOURISM REGIONS

The longer-term potential for Travel & Tourism in Russia’s many regions is enormous. The country’s geographic diversity is extremely rich and its wealth of art, architecture and history place it among the world’s most important cultural destinations.

‘European’ Russia – the land which lies to the west of the Ural Mountains – is bigger than any other European country and is home to some 120 million people, or 83 per cent of the Russian population. The country contains within its borders destinations as varied as the magnificent European city of St Petersburg and the vibrant capital Moscow, the coastal Riviera of the Black Sea and a spectacular portion of the Caucasus Mountains. These contrast sharply with Siberia’s vast, largely uninhabited, lands, the outstanding natural beauty of Lake Baikal and the fast-growing Far Eastern cities of Khabarovsk, Irkutsk and Vladivostok.

Most international leisure travel interest is currently still centred on Moscow and the surrounding towns of the Golden Ring, as well as on St Petersburg, an increasingly popular port of call for cruise ships. Foreign tourists continue to cross the country on the Trans-Siberian railway, stopping at a handful of cities en route, and to cruise on the waterways of European Russia, but most of the rest of the country is unexplored.

International business travellers primarily visit Moscow, with St Petersburg in second position, although they are starting to venture further afield as more foreign companies establish a presence in the country and international trade grows. The capital is also increasingly acting as a hub for foreign business visitors to developing regional cities of European Russia such as Yekaterinburg, Nizhny Novgorod, Kazan and Samara, as well as the industrial centres of Siberia, eg Novosibirsk and Krasnoyarsk, and the Far East.

There are 89 subdivisions in Russia. These are republics (21), krays (6 administrative areas), federal cities (2) autonomous regions (1) and autonomous ‘okrugs’, or administrative subdivisions of republics, krays or regions (10). In terms of potential tourism interests, the Federal Agency for Tourism (Rosturizm) has divided the country into the following main tourism zones according to specialization by tourism type:

- The North – the White Sea, the Barents Sea, Arkhangelsk, Vologda, the Murmansk region, the Karelian Republic. Especially popular in this tourism zone are educational and ecological tourism, cruises, hunting, fishing, skiing, hiking and pilgrimages to the ancient centres of Russian Orthodox culture.
- The Northwest – St Petersburg, Pskov, the Novgorod region. Lovers of history and culture gravitate here, as well as tourists who enjoy historical surroundings for business meetings and conferences. These destinations also offer cruises and traditional touring options.
- The Baltic coast – the Kaliningrad region – specializes in business tourism, cruises, and medical tourism, ie treatment in traditional sanatoria.
- Moscow and the Moscow region – this is the prime destination in Russia for business but it is also the cultural centre, attracting tourists on both group and individually tailored tours.
- The Golden Ring – Vladimir, Yaroslavl, Ivanovo, Kostroma and Tver regions. This zone is ideal for those interested in early Slavic history and who want to combine tours with treatment in a sanatorium and/or relaxation. River cruises are also popular.
- The Povolzhye region – the banks of the Volga river, including the Nizhegorod, Astrakhan, Volgograd, Samara, Ulyanovsk regions, Chuvashia and Tatarstan. The region is usually visited for business, educational and leisure tourism, including fishing. Cruises down the Volga, Russia’s best-known river, are also popular.
- The Northern Caucasus – comprising three different regions. The first covers the Black Sea and Azov Sea coasts – Krasnodarsky Kray, Adygeya and the Rostov region – which appeal to sun & beach enthusiasts (see below), those looking for medical treatment – curative or preventative – and tourists who enjoy walking and hiking. The Caucasus mineral waters have curative powers that are reputed to heal a whole range of ailments and diseases. Finally, the Kabardino-Balkarsk Republic is one of the Russia’s best mountain resort regions for skiing.
- Siberia – which includes four distinct tourism regions. First, the mountainous Altai, where tourists can rest and recuperate, or opt for a more active holiday, mountain hiking and skiing. The mountainous Shoria (Kemerovo region) offers similar activities and facilities and is particularly good for skiing. Yakutia is an unique place for ecotourism.
- Finally, the Baikal region around the lake of the same name – with Irkutsk, the Chitinsk region and the Republic of Buryatia – is located near the Mongolian border, and surrounded by mountains, forests and wild rivers. It is an immense and breathtaking area of physical beauty. The lake holds 20 per cent of the earth’s fresh water and harbours more endemic species of plants and animals than any other lake in the world. The surrounding wild mountains and rivers make the region an ideal area for engaging in an array of outdoor pursuits including hiking, climbing, white-water sports, skiing and nature photography.
- The Far East comprises three tourism regions – Primorye, which is primarily a business centre; Sakhalin and the Kuril Islands, for relaxation, hunting and fishing; and Kamchatka, the peninsula for harder adventure holiday enthusiasts.

One of the city of Vladivostok’s main attractions are its numerous casinos where Chinese can indulge in gambling, which is banned in China. The Far East also has great potential as an ecotourism destination. More and more tourists are interested in sea and air tours to the Kamchatka peninsula and the Maritime territory, as well as the Amur River. However, the shortage of international standard accommodation and poor service levels remain a serious handicap to developing tourism demand in the region.

Kamchatka, a remote, sparsely populated, former military stronghold that was closed off to most Russians during Soviet times, is known by local Russians as the ‘land of fire and ice’. It is covered in volcanoes, geysers and hot springs, and it teems with brown bears, salmon, giant eagles and other exotic wildlife. For skiers and
Regions earmarked for development: from historic sites...

Rosturizm has earmarked at least 12 centres for tourism development and, of these, two have been personally recommended by President Putin. These are Krasnaya Polyana – a mountain ski resort in Krasnodar Territory (see below) – and Tobolsk in Western Siberia. In Tobolsk the focus will be on improving infrastructure, including developing new hotels, as well as restoring cultural monuments and important buildings.

Among the historic sites in Tobolsk is the Romanov House, where the last tsar’s family resided shortly before their death. And not far from Tobolsk is the village of Pokrovskoye, the birthplace of Grigory Rasputin, the monk who was for a long time an adviser to the Russian Royal family and who is often seen as a central reason for the overthrow of the Romanovs.

With abundant arable land – more than 5 million acres – Krasnodar is strategically located between the oil-rich area of the Caspian Sea and the resort areas of the Black and Azov Seas, and it boasts several of the biggest ports in Russia. It is already the recipient of plenty of foreign direct investment (FDI) from countries such as Germany and Italy.

Major foreign companies, including Nestlé, Phillip Morris, Coca-Cola, construction materials producer Knauf and agricultural equipment maker Claas, have already set up shop there – in all there are about 500 businesses that have established a presence in Krasnodar. In 2003 it ranked third for FDI in Russia, with US$250 million in total foreign investments – a 61 per cent increase over 2002 – and had total FDI of US$118 million.

...to beach resorts...

With 2 million or more tourists a year visiting the beaches of the Black and Azov Seas, the region is also one of Russia’s top tourism destinations – although the annual influx of visitors has dropped sharply from the levels achieved in the resorts’ heyday, in the 1980s.

The Black Sea city of Sochi has been a popular Russian resort area for nearly two centuries. Located approximately 2,400 kilometres due south of Moscow, the city is famous for its favourable climate, beautiful landscapes, beaches, parks, health resorts, spas, and hotels, as well as its mineral springs, which have prompted the development of spas, such as the renowned Matsesta. The city’s charm comes from its unique location, creating a sub-tropical climate for much of the year.

It is the warmest city in Russia, with year-round temperatures averaging over 14°C. Tourism is the leading industry of the city and provides growth for other sectors, such as health care, hotel services, construction, restaurants, and food processing.

During the 1990s, the popularity of Sochi waned as Russians, granted new travel freedoms, began holidaying abroad. However, as a result of the economic crisis that began in 1998, including the devaluation of the rouble, the destination regained some of its lost appeal. Rezidor has two Radisson SAS properties in Sochi. But the city generally does not offer an adequate supply of quality restaurants, hotels, and leisure attractions to meet demand.

...and new Olympic venues?

Although most tourists flock to the city in the summer, the winter season also attracts skiers to Krasnaya Polyana. Located on the Roza Khutor plateau, 70 kilometres from Sochi, Krasnaya Polyana is linked via underground tunnel to Sochi and is officially the snowiest place in Russia. It already has two failed Winter Olympic Games bids behind it but officials from the Russian Olympic Committee think that with proper planning, solid preparation and sufficient funding, the city would be the perfect choice for 2014.

The Kremlin has similar ambitions and is backing Krasnaya Polyana and Sochi for the 2014 Games. The government has approved a Rb327 billion rouble (US$11.7 billion) plan to turn Sochi into a year-round mountain and Black Sea resort.

More than half the money will come from federal and regional coffers and go toward infrastructure such as electricity, communication and transport. Private investment is expected to make up the balance and will be spent on sports and tourism facilities.

Among the proposed projects are a 50-kilometre mini-metro system, a bobsled track and 14 other sports facilities that will accommodate 200,000 fans, new hotels, and a reconstruction of the main airport serving the area, in Adler. The government believes that the annual flow of tourists to Sochi and the surrounding mountains could triple to 6 million by 2015.

If Russia wins the 2014 Winter Olympics bid, it could collect an additional US$1 billion to improve infrastructure from the International Olympic Committee and corporate sponsors of the Games. If the bid fails, the programme’s US$11.7 billion price tag would be halved.

Meanwhile, different projects are moving ahead regardless. The US$425 million Karusel resort, which is the brainchild of Nortgaz co-owner and Krasnodar Senator Farkhat Akhmedov, was due to open its first ski lift in February 2006. Gazprom, the state-controlled gas monopoly, is to open a resort with six ski lifts, more than a dozen slopes and several dozen cabins later this year. And Vladimir Potanin’s Interros holding is to start construction of a US$140 million ski centre called Roza Hutor in summer 2006.

Potanin agreed to build Roza Hutor together with Chelsea football owner and Chukotka Governor Roman Abramovich. But in 2003 the project nearly fell apart when Interros announced it was suspending the project indefinitely due to a conflict between its ideas for the resort and the government’s development plans. The project was rekindled a year later and is now the proposed site for the Olympics skiing competition.

Roza Hutor is currently holding a tender for a chief contractor, and a winner is to be selected in March. Construction on the 429-hectare site is to start this summer and last four years. When finished, the ski centre will offer 55 slopes and 15 ski lifts to up to 9,500 visitors per day. No accommodation is planned, but this may be reviewed once the centre’s capacity reaches 7,000.
BUSINESS REALITIES

State control versus privatization
The Russian economy has been dominated by power plays between central and regional governments, over-powerful corporations and their tycoons, the security forces, an often arbitrary judiciary and organized crime which has undermined domestic and international confidence in Russia as a place in which to invest safely.

Russia is also plagued with bureaucratic inefficiency and corruption. Much restructuring and recapitalization is still needed, especially in infrastructure and basic services. Some progress has been made with legislation covering, for instance, the legal, tax and financial systems, civil service administration, urban land tenures and housing, customs, business regulation, pensions and the labour code, but passing legislation is often easier than implementing it.

In 2002 the USA and the European Union recognized Russia as a market economy, easing business, trade and financial relations. Income tax is now levied at a flat rate of 13 per cent. The standard rate of value added tax (VAT) has been reduced from 20 per cent in 2003 to 18 per cent in 2004 and will be further reduced to 16 per cent in 2006. The unified social tax (UST) was reduced from four tiers with a top rate of 35.6 per cent to three tiers up to 26 per cent in January 2005. Oil and gas extraction and export duties are adjusted every two months. The foreign exchange surrender requirement for companies was reduced from 50 per cent to 30 per cent in 2003; there are proposals to abolish exchange controls entirely from 2007.

Tax burdens to be reduced…
New tax proposals approved by government late last year will cut companies’ tax burdens by an estimated US$7 billion a year. The proposals, which will simplify the collection of VAT and speed up refunds to exporters, will cost the government US$5 billion less than an alternative plan proposed by the Prime Minister in 2004 to slash the VAT rate to 13 per cent from 18 per cent. The changes will also allow companies to write off 10 per cent of equipment purchases as operating expenses, thus reducing their corporate tax bill.

…but bureaucratic inefficiencies continue to constrain the business environment
Nevertheless, Russia’s business environment will remain constrained for the foreseeable future by inadequate legislation, uncertain property rights, red tape, corruption, and the fear of government interference in business and the economy. The environment for small businesses is particularly difficult, given the paucity of lending by the unstructured banking sector. Yet for the hardy and experienced investor, Russia can offer enormous opportunities, especially given the size of the domestic market. This is probably more true for Travel & Tourism than for any other sector.

The country’s foreign reserve position looks strong, but capital flight continues to be a problem. The Russian Central Bank estimates that net illegal capital flight may have amounted to US$15.8 billion in 2003 and US$25.8 billion in 2004. The influence of the Yukos affair on capital flight and inwards investment is a hotly debated topic, but foreign investors seem to be returning to Russia. Foreign direct investment (FDI) inflows, according to the Russian Central Bank, were US$3.5 billion in 2002, US$8.9 billion in 2003, US$11.7 billion in 2004 and US$9.3 billion in the first half of 2005.

Diversification of investment
Investment is also becoming more diversified as it no longer concentrates solely on the oil and gas sector. Last year’s FDI recipients came from a variety of sectors, benefiting from the ongoing consumer spending boom, such as retail, financial services, media and automotive products. FDI in tourism projects such as hotels has been slow – attributable to the lack of clarity in legal procedures, ownership rules, expatriation of funds, etc – but the situation is improving.

In addition, Russia should be accepted as a member of the World Trade Organization (WTO) in 2006 or 2007 – a goal towards which it has been striving for a number of years – and this should open up new opportunities for foreign investment in tourism, as well as more traditional sectors.

Russia embarked on a very cautious trade liberalization process in preparation for WTO membership and gained approval from the EU for its application in 2003. However, final approval has still not been given, largely due to the USA’s apparent unwillingness to back Russian entry. Prior to the WTO Ministerial Conference that took place in Hong Kong in December 2005, the head of the US delegation said that some questions remained open.

Among the most contentious issues in the bilateral negotiations over US backing of Russian entry into the 149-member body is better access to the Russian market for foreign aircraft manufacturers, enforcement of intellectual property rights and sanitation for agricultural goods. Like the USA, other countries – primarily Switzerland – are unhappy with Russia’s refusal to allow banks and other financial institutions to open their own branches in the country – although this matter was expected to be addressed during planned discussions at the January 2006 World Economic Forum in Davos, Switzerland. If this is the case, and it also resolves its other differences with the USA, Russia could in theory be a member by this coming summer. But next year is more likely.

The Russian economy has been dominated by power plays between central and regional governments, over-powerful corporations and their tycoons, the security forces, an often arbitrary judiciary and organized crime which has undermined domestic and international confidence in Russia as a place in which to invest safely.
WTTC maintains that any form of protectionism is not in the longer-term tourism interests of the country, and that the government should progressively open up its air transport market and privatize all sectors of air transport. As tourism demand grows, an expansion of liberal aviation accords will attract an increased number of scheduled flights and charter activity from Russia’s main markets – as well as stimulating outbound travel – while low-cost carriers can help generate new markets from within Europe.

**REMOVE BARRIERS TO GROWTH**

In addition to creating a competitive business environment that stimulates and facilitates investment, healthy Travel & Tourism will depend on an operating environment that is free of bureaucratic hassles and other barriers to growth. The Russian Government must step up its financial sector reforms, introduce more intelligent taxation and address some of the serious issues hindering the industry’s development, such as visa requirements.

**Open markets and pursue aggressive reforms**

Travel & Tourism can only flourish and realize its full socio-economic potential within open and competitive markets. There is no room for protectionism in an industry that depends on the free movement of people and capital. On the contrary, there is a need to create rapid and transparent systems of interchange to deal with international trade and mobility.

The Russian Government clearly understands these needs and is, in fact, making progress towards harmonizing its policies and laws with those of its trading partners – an important step on the road to planned membership of the World Trade Organization. The government should pursue aggressive reform policies that are conducive to the sustainable growth of Travel & Tourism and that will, in turn, accelerate Russia’s attainment of economic targets.

Broadly speaking, these policies should include, in addition to attracting foreign direct investment:

- Reducing the level of direct state intervention;
- Balancing budgets, and implementing healthcare and pension reforms;
- Maintaining price stability;
- Accelerating privatization; and
- Streamlining regulation and reducing red tape.

**Tax intelligently**

Transaction (indirect) taxes are relatively high in Russia, and are certainly not conducive to increased foreign investment, or tourism growth generally. However, the progressive reduction in VAT and other tax reforms is commended by WTTC. Care must be taken to ensure

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**WTTC Principles of Intelligent Taxation**

A study of Travel & Tourism taxation policy by the London School of Economics for WTTC recommended five principles that public policy-makers should use to guide their review of tax policy proposals and legislation.

**Equity**

All economic sectors should be treated fairly with regard to taxation. Even-handed treatment of all sectors reduces imbalances that can result in political, social and economic difficulties.

**Efficiency**

Taxes must generate revenue without a significant impact on the demand for a good or service (unless the tax is designed to modify behaviour). At a certain threshold, the benefits of a tax become less significant than the costs of reduced demand. The decrease in demand sends a debilitating wave throughout the economy as linked suppliers are affected. This negative cycle swells because of the subsequent loss of tax revenue in many sectors.

**Simplicity**

Complicated taxation schemes eat up revenues through administrative costs. These costs include both those borne by government in the process of collecting and enforcing taxes, and those borne by taxpayers. An objective of good tax policy is to achieve the highest possible ratio of revenues generated per dollar invested in collecting the tax. Special note should be made to incorporate taxpayers’ costs of compliance in calculating this ratio. Simplicity in taxing also dictates that it is clear what the tax rates are, and what the revenues are intended to be used for.

**Fair revenue generation**

Fair revenue generation arises from the concept of equity. In the even-handed capturing of tax revenue, it is unreasonable to assess special fees or levies on specific goods or services. These taxes are often cloaked by language and terminology to hide their real intent. Special charges and fees may appear, on face value, to be modest. They aggregate, however, to become a cumulative and often unreasonable burden to a sector.

**Effective stimulus to growth**

Tax incentives and disincentives should be imposed with the underlying goal of stimulating growth. Taxes that support infrastructure will ideally result in the attraction of investment and subsequent employment. When taxes become excessive, economic growth often grinds to a halt.

Many taxes on Travel & Tourism violate some or all of these Intelligent Tax Principles. The practical reality of these principles provides that taxes can be imposed to generate revenue, increase competitiveness, or change consumptive behaviour. If taxes follow the criteria above, they will result in both increased revenues for governments and strong competitive economies.
that the level of VAT is not perceived as excessive, as this could have a long-term, negative impact on Travel & Tourism Demand.

While Travel & Tourism should pay its fair share of taxes, the growth and prosperity of the industry – including the investment necessary to generate these future revenue flows – will depend in no small part on the competitiveness of Russia’s Travel & Tourism. This will also depend on whether it receives equitable treatment relative to other industries and to competing destinations.

There is an increasing tendency worldwide for governments to target Travel & Tourism as a revenue generator to meet short-term budget objectives, with little thought to the longer-term consequences on demand and job creation. WTTC urges the Russian Government to ensure fiscal regimes that encourage tourism growth, exports, investment, infrastructure, business innovation and job creation. The ‘User Pays – User Benefits’ principle should be given priority, with funding collected earmarked for Travel & Tourism infrastructure and promotion.

**Ease the constraints to Travel & Tourism**

Russia’s Travel & Tourism environment is still plagued with different examples of bureaucracy that require patience for anyone working in, or dealing with, Russia. One example is the recent decision to place non-governmental organizations (NGOs) under strict state control and to close down NGOs that use foreign grants to finance political activities. While there may be justification for such a move, there are many NGOs involved in legitimate Travel & Tourism projects in Russia. So there is some concern that the move could have a negative impact on foreign aid for the industry.

A proposed requirement for frequent business travellers to register every time they enter the country was fortunately scrapped before it came into practice. But a new law, approved last autumn, which was intended to help monitor the import of valuable documents with security features such as watermarks, caused serious problems for airlines and travel agencies issuing airline tickets, which were covered by the term ‘valuable documents’ – even though a blank ticket has no value. This resulted in a shortage of ticket stock for airlines to issue to passengers.

Another piece of arcane legislation is holding domestic carriers back from joining the 21st century. The International Air Transport Association (IATA) has set a 2007 deadline for the world’s airlines to switch completely to e-tickets. However, Russian tax authorities are blocking e-tickets because their regulations require a paper coupon as proof of payment. Even users of private or corporate jets have to produce paper tickets for the tax authorities.

Yet another rule, typical of the ones with which airlines operating to/from Russia have to contend, was the decision to print immigration forms only in Russian. Initially a major headache, the airlines have fortunately got round the problem by all providing a detailed translation to passengers on which they can base their replies. But the decision seems to be totally illogical.

The Federal Agency for Tourism (Rosturizm) should work closely with other government ministries and departments to try to avoid this kind of bureaucratic hassle becoming a deterrent to Travel & Tourism growth.
Simplify visa requirements

The visa issue – both the high cost and the bureaucratic hassles involved in obtaining a visa – is the most frequently cited subject of concern to Russia’s inbound tourism industry. Rosturizm and the private sector, through the Russia Union of Travel Industry (RUTI), have called on government to ease rules as the delays and hassles clearly discourage visitors. Tourist visas cost a minimum of US$70 but, in most cases, the cost is much higher.

For those not travelling in groups, a hotel voucher confirming one’s stay is required, so this adds a further cost element – and it is even higher if a travel agency is involved in the visa application, or if the traveller applies for a business visa. Non-urgent visas can take up to three weeks to process, so most people also ask for quicker delivery times. It is therefore not surprising that many visitors pay upwards of US$200-$250, or even more for a multiple-entry visa.

Fortunately, efforts are now being made at intergovernmental level to address the visa problem. Russia and the European Union recently signed an agreement facilitating visa issuance for Russians travelling to EU countries in exchange for Russia agreeing to take back illegal immigrants.

There are reciprocal agreements between Russia and a number of countries, one of the latest being China. Russians and Chinese living close to the Sino-Russian border have been able to make local trips to each other’s countries without visas for some time. But the new agreement signed last year goes much further. Chinese can now travel to any city in Russia that is open to foreigners without the need for a visa, and vice-versa. This partly explains why there has been such a surge in demand from Russians for destinations like Hainan Island, which can be booked at the last minute.

Experience from other countries has shown that visa-free access for Russians, or visas on arrival, are a major stimulant to demand, while the imposition of visas can dampen demand overnight. This was the case for Poland and Cyprus, for example, when they joined the EU in May 2004 and were forced to impose visa requirements on Russian visitors.

Japan has now announced that it plans to simplify visas for Russian visitors and permit multiple entry valid up to three years bypassing the need for official invitations. Reciprocal arrangements will presumably be made available to Japanese travelling to Russia. Negotiations are due to start between the two countries in early 2006. It also plans to waive all consular fees involved in issuing visas.

The Russian Government should pursue these commendable efforts to simplify visa requirements through reciprocal agreements with other countries.

Improve safety and security

Safety and security concerns for foreign tourists in Russia are widespread. The level of crime is high – more than 2.7 million crimes were committed in Russia in 2004, over half of which fell into the category of theft, and the figure is reported to have risen in 2005. In St Petersburg alone, over 800 crimes against foreigners were committed between January and September 2005. Many of these received widespread media coverage, not least because law enforcement is very poor and few petty criminals are ever found, let alone prosecuted.

In response to intense lobbying by RUTI, the St Petersburg authorities have been looking at establishing a tourist police, who would try to reduce incidents of crime as well as handle complaints by tourists. It is too early

Tax service to issue gaming licenses

Russia’s gambling industry is well developed and there are a large number of casinos – more than 50 in Moscow and 20 in St Petersburg alone. Primorye in Russia’s Far East, for example, is very popular with Chinese gamblers and thus a main tourism draw. Yet, even though the country’s slots machine market alone is worth US$3.5 billion, Russia still does not have a federal law that regulates the gaming industry.

The market players in Russia’s booming gaming industry therefore welcomed the government’s recent move to bring more clarity to the sector’s regulation by appointing the Federal Tax Service to take responsibility for issuing licenses. The good news is that the move should resolve the long deadlock over gambling licensing.

All gambling licensing has been stalled since the State Sports Committee was disbanded in the early 2000s and its successor, the Federal Agency for Physical Culture, Sports and Tourism, did not inherit the committee’s powers to issue permits. This was then split into two separate agencies for sport and tourism respectively, as already indicated, but neither is allowed to issue permits.

The main concern within the industry now is that, having licensing, oversight and punishment all concentrated in one place, the tax body will have too much power. It will be able to decide who can and cannot work in the market and will also be able to decide unilaterally when and for whom to schedule back tax checks and levy fines.
to judge the success of this plan as it is only really expected to be put into force in summer 2006. But, interestingly, as few Russian policemen and women speak any foreign languages, the tourist police will be selected from among students during their summer vacations.

There are also moves to improve tourism signage in St Petersburg, as well as to oblige ground handlers and tour operators to operate new or, at least, safe tourist buses. Since most of those used are currently below standard and considered unsafe – they average about 20-30 years old – accidents are frequent, especially as the local roads are full of potholes and, therefore, dangerous. There is no bus manufacturing industry in Russia, so virtually all tourist buses have to be imported. The import duty on a new bus/coach, which costs around US$1 million, is 100 per cent.

PROMOTE GREATER PRODUCT AND MARKET DIVERSIFICATION

Only 20 per cent of Russia benefits from tourism, and 80 per cent of foreign tourists visit only Moscow and/or St Petersburg, either for business purposes or for city and/or cultural tourism. It is clearly in the interests of both the public and private sectors – not to mention local communities and other stakeholders – to diversify Russia’s tourism product mix and try to tap new markets.

Adapt products to meet the needs of the changing marketplace

Russia is perceived as an expensive destination. It faces particularly serious competition from all the emerging former East European countries that, like Russia, were half-hidden behind the Iron Curtain for so many years. These include the Baltic States, Hungary, the Czech Republic, Slovakia and Poland, which attract primarily demand for city breaks and cultural trips. But competition is also intense in the sun & beach and cruise sectors from new destinations like Croatia and Montenegro, and health and wellness tourism is enjoying a renaissance in countries like Hungary and the Czech Republic – once renowned for their world-famous spas like Marienbad and Carlsbad.

For this reason the Russian Government and the local Travel & Tourism industry should invest heavily in product diversification. Some steps in this direction have already been taken thanks to the availability of foreign aid – mainly European Union funding. But further diversification will help minimize the risk of over-reliance on a few key markets, and reduce seasonality, spreading tourism demand more equitably throughout the year and away from Moscow and St Peters burg. In the longer term, it could also help avoid excessive strains on valuable natural resources.

International markets from Europe, Asia and North America offer the greatest potential for tourism growth – whether in terms of volume or percentage growth. They are also especially attractive to Russia as they generate higher yields. However, the domestic and CIS markets should not be overlooked as they can provide a valuable source of revenues at a time when much of the country’s tourism infrastructure and facilities remain below internationally accepted standards.

The key market and product segments which Russia should develop and promote include:

Domestic tourism

The share of Russians taking an annual domestic holiday is probably only about 20 per cent, although anecdotal evidence suggests it may have picked up slightly since 2003. This is attributed to improved economic stability and living standards. But domestic tourism is still well down on its level achieved during the Soviet era. In those days, social tourism was widespread. The government had a whole raft of economic measures designed to stimulate holiday taking and trade unions provided subsidies for employees who could not afford to go on holiday. Today, that kind of support is almost non-existent, except for children going on summer
camps. Even then, the number of camps has reduced sharply – in the
Moscow region alone they have fallen from more than 700 prior to 1990
to less than 300 – subsidies have declined significantly and prices have
soared. At the same time, children from wealthy families can choose from
a variety of high-cost specialized camps offering sports, computer studies
and the like – similar to camps seen in Western countries.

Although details are not available, it seems that an increasing
number of large companies are recognizing their social responsibilities
to employees and are looking at financing vocational programmes and
holidays. And some kind of holiday cheque system – modelled on the
French chèque-vacances – may well emerge in due course.

MICE business

The meetings, exhibitions, conferences and exhibitions (MICE) business
is relatively undeveloped in Russia, given the size of the country. There
are around 250 professional Russian exhibition organizers within Russia
– 55 of whom, or 22 per cent, are members of the International Union
of Exhibitions and Fairs (IUEF). The latest data available suggests that
some 2,500 exhibitions were held in the country in 2003. These covered
a total exhibition space of more than 2.8 million square kilometres and
attracted over 230,000 visitors – domestic and international. IUEF
members accounted for around 45-50 per cent of the total exhibitions
and probably a higher number of visitors and exhibitors.

Nevertheless, the convention and exhibition business is not really
expected to grow significantly in Russia until the country has some
major centres meeting international norms. The potential for St
Petersburg is seen as possibly greater than for Moscow, but the city will
not have a major multi-purpose centre until 2008-09 at least – located
in the New Holland Island complex. Hotel capacity will also have to be
increased to cope with projected delegate numbers.

Meanwhile, incentive travel would seem to be a better bet to
generate high-yield tourism business in the short to medium term. But
the visa issue is a deterrent for demand of this type of business. St
Petersburg is nonetheless seen as a very upmarket destination offering
huge potential for lavish entertainment in historic palaces, so the
opportunities should be good.

Cultural tourism

Cultural tourism is already one of the best-selling tourism products to
foreigners and domestic travellers. But sales to foreigners could grow far
more quickly if the visa issue were eased and it were possible to spend,
say, 3-4 nights in the country visa free, or to obtain a visa for a short stay
on arrival. City breaks are the fastest growth sector in Europe at present,
due to the huge increase in availability of no-frills’ airlines offering low
fares. And the majority of city-break travellers book their trips a very
short time in advance of their departure. But Russia is more or less
closed to this market at present because of the time involved in
obtaining a visa.

The only type of tourists prepared to fight the system and pay
whatever is needed to speed up the visa process are the affluent Western
visitors who travel to Russia for special art exhibitions or cultural
events.

Sea and river cruising

One sector of the inbound market that has performed well above
average for Russia in recent years is the cruise market – both for river
and sea cruises. St Petersburg is now the second most important port in
the Baltic after Copenhagen, in terms of passenger numbers, attracting
253,000 in 2004, and it recorded the highest number of cruise ship calls
of any Baltic port that year. The growth in passengers and ship calls is
estimated at 39 per cent and 16 per cent respectively for 2005 and
future growth looks assured thanks to plans to upgrade and modernize
port facilities.

Regular cruises to Sakhalin Island and Kamchatka are offered by
Japanese and American cruise lines, and Russian ships provide tailor-
made cruise tour programmes between Russia’s Far East ports. The
Komandorskie islands are one of the most popular destinations for Far
East cruises.

The most popular river cruises, which primarily attract older
Americans and Europeans, operate between St Petersburg in the north
to Moscow – a 3-4 day trip – but it is possible to travel by boat from
the Baltic Sea all the way south to Volgograd, Rostov-on-Don or
Astrakhan on the Caspian Sea.

Cruises from Moscow to St Petersburg usually stop off at the island
of Kizhi in the north of Karelia, and there are also trips to the Valaam
archipelago and Arkhangelsk, Vologda, Novgorod and Pikov in the
north and northwest of Russia.

Valaam, for example, which is made up of 50 islands, is famous not
only for its rich history and ancient architecture, but also for its climate.
Fruit normally only found in southern climes grows in this northern
region. Another remarkable fact about Valaam is that trees grow directly
on rocks, and crossing Lake Ladoga, Europe’s largest lake, to reach the
archipelago is like being in the open sea.

The potential for future growth is nonetheless good since more
and more cruise routes are being revived, such as those on the Volga and
Siberian rivers Lena, Yenisei, Ob and Amur. Small boat tourism is also
being developed on Lake Baikal. But it is important to note that no new
river cruise boats have been built in Russia for 15 years.

Sports tourism and adventure travel

Russia has enormous tourism potential for niche markets such as
adventure travellers and nature enthusiasts. Russia has many wild places,
where animals have never encountered humans, and there are
fascinating polar regions, such as the island of Vrangal with its Arctic
tundra, polar bears and musk oxen.

One can raft down wild Siberian rivers, fish in the wonderfully
clean waters of Lake Baikal in southern Siberia, see the geysers and
giant depressions of Kamchatka, or walk in the virgin forests in the
Republic of Komi. Also popular are cycling around Karelia, climbing
the Ural and Caucasus mountains, horse riding in the Altai nature
reserves, and diving in polar waters.

The development of resorts in the Krasnodar region, and especially
in Krasnaya Polyana, will open up Russia to foreign ski enthusiasts.
Winter sports are extremely popular in Russia, but many of the ski
stations are badly in need of modernization and would not appeal to
typical foreign markets, with the exception of hard adventure travellers. This is certainly a market worth catering to as it generates high-yield business.

Fishing and hunting are two niche sectors in which Russia could excel. The Lower Volga and its delta are some of the best places to fish in the whole of Europe. Hunting and fishing are nonetheless prohibited in national parks and reserves, including the Astrakhan biosphere reserve, which is in the delta of the Volga. Fishing tourists are accommodated in small docks transformed into hotels and situated right by the water. Fishing is almost unrestricted in the lakes of Karelia and the Murmansk region.

Adventure travel programmes include a wide range of sporting activities such as hiking, skiing, water tourism, biking, mountain tourism, horse riding, auto- and moto- tourism and caving, and all the different sectors have bucked the general inbound trends, showing healthy growth in recent years – albeit from a very low base. So they clearly have strong potential for future growth. Also increasingly popular are the two extreme types of adventure travel – hang-gliding and para-planing.

Health/wellness tourism

Russia has a long tradition in health tourism and ‘cures’ are rather popular, at least among older Russians and neighbours from CIS markets. The industry is undergoing a massive, but relatively slow, restructuring similar to that in Eastern Europe over the past decade. The main problems are lack of funds for modernization, the non-commercial mindset of the sanatoria’s public or semi-public owners, and the resulting decline in numbers of clients.

The decline is primarily due to the fact that Russia’s public health service has cut back drastically on providing free spa treatment as a medical service. And few sanatoria – the traditional term is still widely used, reflecting the (rightful) image of ageing, clinical institutions. Only a few have been modernized – The Stein Group’s deluxe spa resort near Sochi, the Rodina, is one example – and are trying to tap the wellness market, but the potential for this type of business could be significant. The first step, of course, is to stop using the negative word ‘sanatorium’ and start talking about ‘spas’.

FAVOUR TECHNOLOGICAL ADVANCEMENT

Adaptation to the ‘digital economy’ is essential for companies involved in all areas of Travel & Tourism to become and remain competitive. In today’s increasingly competitive global marketplace, there is also a real need for a strong national leadership branding. This will require a co-ordinated approach to internet marketing and distribution to optimize Russia’s visibility and image.

Although the average figures mask wide discrepancies from one region of the country to another – and particularly between urban and rural areas – internet usage in Russia is still in the relatively early stages of development.

Adapt to the ‘digital economy’

Although the average figures mask wide discrepancies from one region of the country to another – and particularly between urban and rural areas – internet usage in Russia is still in the relatively early stages of development. The online population is variously estimated at between 24 million and 35 million – or 17-24 per cent of the total population. And the number of Russian Travel & Tourism companies with broadband access – let alone handling online transactions – is low. It is not surprising that Russia has not yet been able to embrace the full potential of technology. But it is important for government to recognize that, as a technology intensive industry, Travel & Tourism can help Russia obtain and apply information technology systems and telecommunications at a competitive pace.
One example is telecommunications. An increasing share of Travel & Tourism operations – and virtually all distribution and sales transactions – flow through telecommunications circuits. Where telecommunications are monopoly controlled, there are often restrictions on access, high costs and unreasonable operating conditions. This in turn limits the potential of market-oriented expansion of Travel & Tourism, with negative impacts domestically and internationally in terms of cost, operational efficiency and customer service.

WTTC recommends that the Russian Government pursue a policy of open telecommunications markets, which will help to lower costs and enhance services for travellers and tourism companies.

Meanwhile, WTTC commends the Russian Government’s earmarking of special economic zones to help diversify the economy away from oil toward innovation sectors. Four locations have been selected as special zones for technology research, including the Moscow region towns of Dubna and Zelenograd, St Petersburg and the Siberian city of Tomsk. Tax breaks and other benefits are being offered to technology companies that reside in the zones.

**Invest in e-marketing and distribution**

In today’s increasingly competitive global marketplace, there is a real need for a strong national leadership branding which optimizes resources, focuses the myriad of interests – public and private sector, national, regional and local – and attracts the attention of travellers. This will require particular emphasis on a co-ordinated approach to internet marketing and distribution to optimize Russia’s visibility and image.

The Federal Agency for Tourism (Rosturizm) should take the lead in developing a user-friendly English-language website for potential foreign visitors to Russia. This will help improve the distribution of Russia’s tourism products – both through the travel trade and direct to consumers – and enhance the country’s image and the Russia brand generally in key markets. However, experience in other countries around the world has shown that, while public sector support for national destination databases is critical, the operation and marketing of these databases are best left to the private sector.

The government should also promote the use of technology and the development of e-marketing skills in Travel & Tourism to achieve greater efficiencies and effectiveness, as well as to ensure the industry responds better to the needs of the changing marketplace. Business models are changing almost daily and the industry needs support to stay abreast of these changes, as well as to respond to the demand for online self-tailored programmes and dynamic packaging.

**BALANCE ECONOMICS WITH ENVIRONMENT, PEOPLE AND CULTURES**

**Environmental concerns**

The Russian Government last year signed the Kyoto Protocol, but environmental problems remain one of the country’s major challenges, and one which no Kyoto agreement is likely to resolve in the short or medium term. While Travel & Tourism is not currently directly affected by the widespread environmental degradation, the country’s future tourism success may depend on a rapid improvement of the situation, plus a visible effort on the part of government and the private sector to combat the problems.

The country has 25 national parks and 84 reserves, all of which need to be protected to maintain their tourism appeal. Lake Baikal is an example of a favourite tourism destination – for domestic visitors, if not yet foreigners – but in hundreds of spots around the lake’s 2,000-kilometre shoreline, new houses are coming up fast, with no regard for environmental protection laws, according to officials in the Natural Resources Ministry.

The housing construction, together with a planned oil pipeline to the north and a pulp and paper mill to the south, has set the stage for Lake Baikal to become the first ever UNESCO World Heritage Site to be designated “in danger” against a government’s wishes.

Other conservation issues concern Russia’s wildlife. The feeding ground of the Western grey whale, for example, of which there are only 100 left in the world, is in the middle of the oil production ground near Sakhalin Island. And there are other examples of wildlife not being adequately protected. These include the
Amur leopard – of which only 20-40 still exist in the southernmost tip of the Russian Far East – and the Amur tiger, which is the largest living cat in the world, living in Primorsky and Khabarovsk Kray.

Nevertheless, water pollution is the biggest environmental problem in Russia at present. Less than half of Russia’s population has access to safe drinking water. While water pollution from industrial sources has diminished because of the decline in manufacturing, municipal waste increasingly threatens key water supply sources, and nuclear contamination could leach into key water sources as well.

Air quality is almost as poor as water quality, with over 200 cities often exceeding Russian pollution limits, and the problem is likely to worsen. Solid waste generation has increased substantially due to the adoption of Western-style consumption patterns. Yet Russian municipalities lack management expertise and landfill capacity to cope with disposal problems.

US, Russian, and World Bank studies link an increase in respiratory and gastrointestinal illnesses and developmental problems among children in several Russian cities in part to environmental factors.

Pollution is adding to budgetary strains, reducing labour productivity through illness and absenteeism, and damaging natural resources. It also is deterring some domestic and foreign investors concerned about cleanup and liability issues. A team of Russian experts has pegged overall economic losses from environmental degradation at 10-12 per cent of GDP – similar to estimated losses in other East European countries and substantially higher than estimates of 1-2 per cent in the developed world.

**Government focus is on the economy at the expense of the environment**

Russia has a comprehensive legal and regulatory framework in the environmental area. Yet Russian political leaders and bureaucrats lack the commitment, resources, and organizational capabilities to address environmental issues effectively, according to a 1997 study by Demosthenes James Peterson written under the auspices of the National Council for Eurasian and East European Research.

Businesses or individuals that violate environmental codes typically avoid or minimize penalties, often by paying bribes. And some features of the government’s economic plan, such as its support for ailing and highly polluting state enterprises, will further complicate environmental cleanup if they are implemented.

Moreover, environmental activism has been on the wane since the break-up of the Soviet Union. Despite growing concerns about environmentally related health problems, the Russian public is preoccupied with economic survival and accords much less priority to environmental issues.

**The greening effect of foreign investment**

On the positive side, although Russia is not a candidate for European Union (EU) membership, and is therefore not under pressure to improve its environmental performance in preparation for EU membership, it is receiving considerable international advice and assistance on its environmental efforts. The World Bank, the European Bank for Reconstruction and Development (EBRD), the EU, and environmental non-government organizations (NGOs) have provided Russia with substantial aid, technical training, and assistance on policy priorities, reform, institution-building, and environmental legislation.

The World Bank has designed and implemented regional programmes for the Baltic and Black Seas and has provided environmental project loans to Russia amounting to several hundred million dollars for cleaning up major oil spills and other environmental reclamation and improvement projects.

The EBRD has provided Russia with financing for several major environmental projects, including one aimed at revamping St. Petersburg’s dilapidated water and sewerage network. These and other EBRD-supported projects must meet rigorous environmental impact criteria.

Although much of the US$10 billion invested in Russia from 1989 to 1997 focused on pollution-intensive sectors such as oil, logging, and consumer goods, most multinational corporations employ more efficient equipment and technology and generally use more environmentally friendly practices than Russian companies, according to another 1997 study by Peterson produced under the auspices of the National Council for Eurasian and East European Research. And this is undoubtedly true of more recent capital investment projects.
Establish clear procedures and guidelines
Since the Rio Earth Summit in 1992, it has been widely recognized that sustainability has to be at the core of all policy-making and development planning. This holds especially true for Travel & Tourism. With huge increases in the number of people travelling for tourism purposes over the next decade, there are evident implications for consumption, waste and resource utilization.

It is imperative to ensure that the economic and social benefits that the industry brings, as well as the investment that underpins it, are sustainable in the longer term.

WTTC recommends that:

■ Clear policies and guidelines are developed by the Russian Government – the Ministry of Natural Resources and the State Committee for Environmental Protection, together with Rosturizm and all other interested stakeholders – for planned and sustainable tourism expansion;

■ The government adopts the principles of ecological preservation as outlined in Agenda 21 for the Travel & Tourism industry, developed after the 1992 Rio Earth Summit by WTTC, the World Tourism Organization and the Earth Council;

■ The socio-economic, cultural and environmental benefits of Travel & Tourism are spread equitably across the population in all parts of the country; and

■ The need for local community engagement and empowerment is recognized.

Sustainability will need a balance of private initiative, economic instrument and regulation. Global principles should be reflected in local action and market-based delivery mechanisms should be encouraged. Microloans for local community-based sustainable tourism enterprises should be provided as incentives, and pilot projects used to evaluate and demonstrate local sustainability.

Preserve and promote cultural heritage and natural resources
Russia has an unparalleled wealth of cultural and natural attractions. Travel & Tourism is one of the few ways – if not the only way – in which heritage preservation can be carried out in a way which produces financial returns. The government should prioritize the development of cultural tourism as a way of preserving the country’s rich heritage and enhancing the country’s tourism product. However, it is very important to monitor restoration projects closely to ensure that high standards are maintained.

Meanwhile, the government should also look to increase branding through international and national heritage designations. The country already has 24 sites listed as World Heritage Sites by UNESCO – from cultural sites including the historic centre of St Petersburg and related groups of monuments and the Kremlin and Red Square in Moscow, to natural sites such as the virgin forests of Komi, Lake Baikal, the volcanoes of Kamchatka, Golden Mountains of Altai, and the Western Caucasus.

Now, the Kedrovaya Pad nature reserve in the Maritime territory has been included in the world network of UNESCO biosphere reserves. Kedrovaya Pad is the oldest nature reserve in Russia’s Far East, founded in 1916. It is located in the Khasansky district of the Maritime territory, on the Russian-Chinese border. Its area is small (only 179 square kilometres), but it has all remarkable features of the southern Ussuri taiga.

The Maritime territory already has two biosphere reserves, the Sikhote-Alin and Far-Eastern marine nature reserves. Unlike ordinary nature reserves, biosphere reserves are organized into three inter-related zones, known as the core area, the buffer zone and the transition area. A strict reservation regime is observed in the core area. Certain activities, including research, monitoring and ecological tourism, can be carried out in the buffer area. The transition area, or area of cooperation, has no exact boundaries. All economic activities, which do no harm to the environment, are permitted in this area.

Highlight tourism’s linkages with other parts of the economy
WTTC recommends that the Federal Agency for Tourism, in cooperation with all the other relevant ministries and government agencies, makes efforts to highlight the important linkages between Travel & Tourism and the rest of the economy. This will involve:

■ promoting public awareness of these linkages between Travel & Tourism and other sectors such as agriculture and construction;

■ educating those in other sectors of the needs of Travel & Tourism so that high-quality products can be sourced locally by the industry; and

■ encouraging the use of traditional skills and products in the development of Travel & Tourism products and services.

Russia has an unparalleled wealth of cultural and natural attractions. Travel & Tourism is one of the few ways – if not the only way – in which heritage preservation can be carried out in a way which produces financial returns.
## SATELLITE ACCOUNT
### THE RUSSIAN FEDERATION

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<tr>
<th>Travel &amp; Tourism - Rb billion</th>
<th>2001</th>
<th>2002</th>
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<th>2005E</th>
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<td>Personal Travel &amp; Tourism</td>
<td>378.25</td>
<td>478.54</td>
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<td>Travel &amp; Tourism Economy Aggregates (Direct and Indirect Impacts)</td>
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<td>4,872.52</td>
<td>4,492.11</td>
<td>4,665.73</td>
<td>4,710.40</td>
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<tr>
<td>Gross Domestic Product</td>
<td>727.76</td>
<td>943.46</td>
<td>1,064.35</td>
<td>1,369.66</td>
<td>1,691.45</td>
<td>1,910.68</td>
<td>6,319.03</td>
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<table>
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<tr>
<th>Travel &amp; Tourism Accounts as % of National Accounts</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005E</th>
<th>2006E</th>
<th>2016P</th>
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<tbody>
<tr>
<td>Personal Travel &amp; Tourism</td>
<td>8.46</td>
<td>8.57</td>
<td>8.41</td>
<td>7.98</td>
<td>7.88</td>
<td>7.83</td>
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<td>Gov’t Expenditures</td>
<td>2.56</td>
<td>2.57</td>
<td>2.60</td>
<td>2.64</td>
<td>2.67</td>
<td>2.66</td>
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<td>Capital Investment</td>
<td>11.44</td>
<td>11.65</td>
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<td>11.88</td>
<td>13.63</td>
<td>12.10</td>
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<tr>
<td>Exports</td>
<td>8.90</td>
<td>11.78</td>
<td>9.87</td>
<td>9.03</td>
<td>7.18</td>
<td>6.71</td>
<td>10.12</td>
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<td>T&amp;T Imports</td>
<td>16.02</td>
<td>16.78</td>
<td>15.81</td>
<td>15.12</td>
<td>15.50</td>
<td>16.79</td>
<td>17.52</td>
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<tr>
<td>Travel &amp; Tourism Industry Aggregates (Direct Impact Only)</td>
<td>1.29</td>
<td>1.23</td>
<td>1.10</td>
<td>1.16</td>
<td>1.21</td>
<td>1.26</td>
<td>1.32</td>
</tr>
<tr>
<td>Gross Domestic Product</td>
<td>1.48</td>
<td>1.42</td>
<td>1.27</td>
<td>1.33</td>
<td>1.39</td>
<td>1.45</td>
<td>1.52</td>
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<tr>
<td>Travel &amp; Tourism Economy Aggregates (Direct and Indirect Impacts)</td>
<td>6.90</td>
<td>7.38</td>
<td>6.80</td>
<td>6.92</td>
<td>6.90</td>
<td>6.61</td>
<td>7.74</td>
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<tr>
<td>Gross Domestic Product</td>
<td>8.14</td>
<td>8.72</td>
<td>8.04</td>
<td>8.18</td>
<td>8.15</td>
<td>7.78</td>
<td>9.15</td>
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<table>
<thead>
<tr>
<th>Travel &amp; Tourism Real Growth (per annum except 2015 = 10-year annualized)</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005E</th>
<th>2006E</th>
<th>2016P</th>
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<tbody>
<tr>
<td>Personal Travel &amp; Tourism</td>
<td>3.63</td>
<td>9.65</td>
<td>3.84</td>
<td>5.04</td>
<td>9.01</td>
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<td>Business Travel &amp; Tourism</td>
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<td>-10.77</td>
<td>-17.68</td>
<td>20.05</td>
<td>23.23</td>
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<tr>
<td>Gov’t Expenditures</td>
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<td>1.74</td>
<td>3.67</td>
<td>3.99</td>
<td>2.74</td>
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<tr>
<td>Capital Investment</td>
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<td>4.84</td>
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<td>9.27</td>
<td>7.32</td>
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<td>Visitor Exports</td>
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<td>-2.09</td>
<td>5.01</td>
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<td>8.51</td>
<td>6.38</td>
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<td>Travel &amp; Tourism Demand</td>
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<td>-0.47</td>
<td>4.98</td>
<td>4.89</td>
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<td>6.48</td>
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# Tables

## Travel & Tourism Industry Aggregates (Direct Impact Only)

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## Travel & Tourism Economy Aggregates (Direct and Indirect Impact)

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## Travel & Tourism - US$ billion

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<td>GDP</td>
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</table>

## Travel & Tourism - 2000 Constant US$ billion

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<tbody>
<tr>
<td>GDP</td>
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</tbody>
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The table above provides a detailed breakdown of travel and tourism aggregates and expenditures over various years, categorized by GDP, employment, and other economic indicators. The data includes personal travel, business travel, government expenditures, visitor exports, government expenditures - collective, capital investment, exports (non-visitor), travel and tourism demand, and the associated gross domestic product and employment figures.
WTTC would like to express its appreciation to the following organizations, government ministries and agencies that contributed their knowledge, insight and data/information to the policy review effort included in this report.

Accor Hotels Central & Eastern Europe
Aeroflot Russian Airlines
American Chamber of Commerce in Russia
Business Travel Agencies Association
Business Travel International
Branan – Carl Bro
Congress Bureau of St Petersburg
Consolidated Hospitality Consulting
DLA Piper Rudnick Gray Cary
Domodedovo International Airport
East Line Group
Ernst & Young
European Bank for Reconstruction & Development (EBRD)
Evrofinance Mosnarbank
Global Refund Group
Government of Moscow Joint Stock Company GAO Moskva
Government of St Petersburg
Gullivers Travel Associates
Hilton International
Hotel Consulting & Development Group
HVS International
Horwath Consulting Central & Eastern Europe
Intercontinental Hotels
International Finance Corporation (IFC)
International Institute of Hospitality & Tourism, Moscow
Interstate Hotels & Resorts
Intourist
Jones Lang Lasalle Moscow
Korston Hotels & Malls
Kuoni Travel Destination Management
Marriott International
Le Méridien Hotels

Ministry of Economic Development and Trade of the Russian Federation
Ministry of Transport of the Russian Federation
Monab Development
Monomax Meetings & Incentives
Moscow City Government Committee for Tourism
National Academy of Tourism of the Russian Federation
NERL JSC
Nevskij Fund
Orient Express Hotels
Pulkovo Aviation Enterprise
Rezidor SAS Hotel Management & Development
Russian Gold Group of Companies
RMHC – Russian Management Hotel Company
Rocco Forte Hotels
Russian Federation Federal Agency for Tourism
Russian Federation Federal Agency for Physical Culture, Sport & Tourism (defunct)
Russian Union of Travel Industry (RUTI)
State Duma of the Russian Federation, Committee for Economic Policy, Entrepreneurship and Tourism
St Petersburg Centre for International Co-operation
St Petersburg City Government City Tourist Information Centre
St Petersburg Express JSC
St Petersburg Government Committee for External Relations and Tourism
St Petersburg Government Committee for Investments and Strategic Projects
St Petersburg Technical University
Swissôtel – Raffles International
TMI Consultancy
Transaero
Transbusiness Line

The researchers/authors also consulted with a number of regional governments and individual hotels in Russia, as well as tour operators and travel agencies, foreign national tourism organizations and media groups.