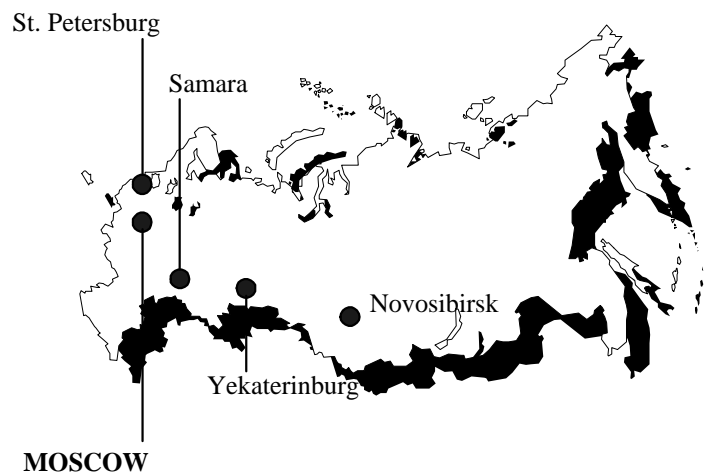


Russia

Key data

Area (sq km):	17,075,400
Population (million):	143.2
Population per sq km:	8.39
Capital:	Moscow
Population of capital (million):	8.31
Languages:	Russian
Exchange rate:	
- spot rate (17/07/03) RUR = EUR1	34.23
- annual average (2002) RUR = EUR1	29.71
GDP 2002 (EUR, billion):	324.1
GDP per capita 2002 (EUR, 000):	2.26

Sources: Bank of Russia, CIA, UN



Political profile

The Russian Federation is the largest country in the world by land mass, spanning ten time zones with a climate ranging from subarctic in the north to the more temperate south. Ethnic Russians account for 82% of the population, with Russian Orthodox Christianity being the dominant religion. Tatar, Ukrainian, Chuvash, Bashkir, Moldavian and Belorussian minorities are also present.

Russia's bicameral federal assembly is made up of a lower house, the State Duma, which has 450 deputies elected on a territorial basis, and an upper house, the 178-member Federation Council, composed of heads of regional executive and legislative bodies. The head of state is the president, elected for a four-year term. The title is currently held by former prime minister Vladimir Putin, who took office on 31 December 1999 when his predecessor, Boris Yeltsin, stepped down due to ill health. Putin subsequently won the March 2000 presidential elections, polling 52.9% of the first round vote to Communist Party candidate Gennady Zyuganov's 29.3%. The next parliamentary elections are scheduled for 21 December 2003 with presidential elections to follow in March 2004.

Putin enjoys considerable popularity amongst the Russian people, if not always abroad. His handling of the ongoing battle for Chechnya has attracted widespread international criticism, though relations with the West have improved in recent years, despite clashes over the US' 2003 invasion of Iraq. In May 2002 a NATO-Russia Council was established, intended to put Russia on an equal footing with NATO through the creation of a common anti-terrorism and security threats policy.

Economic development

The Russian economy has stabilised following the crisis of the late 1990s which was prompted by a slump in oil prices - the country's major export. GDP growth fell from 8.3% in 2000 to 4.5% a year on and 4.1% in 2002. Initial signs for 2003 are promising, with growth estimated to be 6.8% in the first quarter, whilst inflation fell to 5.3% over the same period and is predicted to be around 15% for the full year, level with 2002. Unemployment fell from 10.2% at end-2000 to 8.7% at end-2001 and 8% a year on.

Regulatory body

- State Committee of the Russian Federation on Communications and Information (Goskomsvyaz).

Date of liberalisation

- Local telephony: 1993
- Long-distance: 1993
- International: 1993

Key legislation

On 8 July 2003 Russian president Vladimir Putin signed the bill to put a new telecommunications act into law. The bill will set the legal basis for the telecoms sector in Russia and determine the authority that state bodies have, paying particular attention to the licensing process, which was not defined in detail in the previous telecommunications law. The new law states that licences can be issued via tenders, auctions or other competitions, the rules for which will be set by the government. It also defines the rules for allocating radio broadcasting frequencies which will be initially assigned for a term of ten years or less.

The new legislation will provide consumers greater choice in selecting fixed monthly or time billing payments. However, from 1 January 2005 privileged customers currently enjoying discounts will have to pay in full and apply for compensation from municipal, regional or the federal government.

Additional rules will give all telcos rights to use co-location facilities regardless of which operator owns the installation, with each operator assuming responsibility for its equipment. Furthermore the new law defines universal service obligations (USO) including terms and tariffs, public payphones and internet outlets - with prices to be set by the state - and allows for operators providing USO to receive compensation from a special fund to be created under the terms of the law; telecoms service providers will be required to pay into the fund.

Recent major regulatory activity

The new telecoms law has sparked controversy for containing a clause which requires profitable phone companies to subsidise their loss-making cousins. The so-called universal service fund that all operators of public networks will be required to pay into will be used to compensate telcos offering costly services to rural Russia. Critics naturally enough are not keen on the scheme which, they argue, penalises profitable ventures, adding that it should be the state's duty to subsidise such regions. It is also clear that in a country where corruption is still prevalent, operators fear the potential for abuse given the opaque nature of the new fund's creation. Added to this, the Duma has passed a series of amendments to the new law which have further angered the telecoms industry. Representatives of the telcos expressed concern that the changes overly favoured consumers at the expense of making the market more equal for different carriers and operators. The law was supposed to permit per-minute billing, but this has been dispensed with as a sop to voters in what is an election year. This decision, and a separate one to limit the tariff rises operators can impose, is, claim the operators, detrimental to long-term development as they will not have funds to replace antiquated equipment.

In August 2002 the Communications Ministry hinted that 'real' telecoms market liberalisation may take until 2010 to become reality. According to communications and IT minister Andrey Korotkov, Russia is bound by terms governing its acceptance into the WTO - as set by the Economic and Trade Ministry - which dictate that Rostelecom will continue to enjoy its *de facto* monopoly on the long-distance market until that date. It is hoped that the six-year period will allow the market to develop in a protected environment.

In December 2002 wholesale internet access providers Golden Telecom and MTU-Intel caused waves by changing the way they charged for data traffic. The companies, which provide access for many popular websites and smaller ISPs, decided to charge per-gigabyte rather than on a per-month basis, threatening to double the cost of www services and end the practice of free email. The move followed a similar step taken by RTKomm in mid-2002, and has wide ramifications considering the trio collectively control around 47% of the market.

Broadband

The broadband market in Russia is in its infancy with only 10% of the population currently using the internet on a regular basis as at May 2003. Nonetheless a market for broadband exists and is shaping itself along distinctly separate lines for residential and business users. The latter sector is growing quickly, with Moscow boasting internet penetration of 22%, 64,000 broadband users (i.e. those with connections greater than 64kbps) and a market estimated to be worth USD11.4 million. Russia lags behind other European countries in terms of broadband penetration. In the business market, leased line access is the principal means of obtaining high speed connection, although DSL over normal PSTN copper wires is growing in popularity.

Not surprisingly operators are gearing up to provide advanced high speed services. In October 2002 Svyazinvest's regional carrier for Moscow, Center Telecom, announced it was launching the first phase of its broadband network using equipment supplied by Lucent. Since late 2001 the company has deployed 400km of fibre-optic cable and hopes its multiservice network will offer a full spectrum of data services to two million prospective subscribers in 25 cities. The following February, high speed network operator TransTeleCom and Tandberg Television successfully concluded tests to transmit high quality MPEG-2 video over the former's IP-based fibre network. The trans-Siberian trial involved sending the packet on a 15,000 mile round trip, which has boosted confidence that services can be offered commercially on a nationwide basis. Then in June 2003 Tattelcom, a regional operator for Tatarstan, announced that it had established a network covering all 43 counties using equipment supplied from Cisco. It hopes to offer broadband access and VoIP services and completed the project as part of the state's Electronic Russia initiative to connect rural regions.

Since 2001 the Russian government has also been promoting Cyberpost, a project designed to provide public internet access in state post offices for lower income users. The project is proving beneficial, with more than 250,000 people using the service in October 2002 alone.

Unbundling

Local loop unbundling is still very much in its infancy and Russian CLECs and alternative telcos have yet to wrestle with such issues. Moreover many alternative telcos are forced to roll out their own networks anyway, excepting those which were spun off from local incumbents such as Moscow City Telephone (MGTS).

Timeline of market development

- 1993 State embarks upon the restructuring of the country's fixed line market by creating local operators or regional telecoms operators (RTOs) in each of the nation's 89 regions. At the same time it created dominant DLD and ILD service provider Rostelecom
- 1993 Local, long-distance and international markets opened to competition
- 1995 Svyazinvest established as a holding company for the government's stakes in each RTO
- March 1997 Foundation of the State Committee on Communications and Informatics
- July 1997 25% plus one share of Svyazinvest sold to Cyprus-based consortium Mustcom for USD1.88 billion
- April 1998 A further restructuring plan announced to consolidate Svyazinvest's RTOs into seven mega-regional operators by 2004
- 1999 IP telephony market opened up to competition
- February 2001 Svyazinvest begins reorganisation with seven telcos in the Urals and Siberia
- October 2001 It is announced that St Petersburg Telephone Network (PTN) will incorporate all the regional operators in the northwest, with the exception of MGTS
- July 2003 New Law on Telecommunications passed.

Market commentary

Slowly, but surely, the telecoms landscape is changing in Russia. In November 2002 a report on the nation's telecoms industry concluded that despite the global slump, the total value of telecoms services sold had mushroomed by 45.2% in the course of just twelve months thanks in part to general growth in the economy. The encouraging results were also attributed to telcos improving their ability to provide access for all users - not just fiscally well-off users - and the report also linked improvements to an increase in foreign direct investment in the sector. It is hoped that the introduction of a new Telecoms Law (July 2003) will speed up improvements by reducing state intervention and allowing better coordination with international law, in turn producing a more welcoming climate with transparent and open tenders.

Whilst most of the population lumber on with antiquated analogue exchanges, the business sector at least is turning on to the prospect of state-of-the-art communications networks. A number of high profile companies have hooked up to advanced digital networks and the benefits of dedicated internet access, and in the urban centres of Moscow and St Petersburg digital connections are booming - there were some 20,000 dedicated internet lines in Moscow alone by the start of 2003 - and competition from alternative telcos is on the rise.

Traditional operators are facing an increasing challenge, especially in the urban hubs of Moscow and St Petersburg. By February 2003 it was clear that alternative operators were making a dent in MGTS's traditional Moscow stronghold. According to official statistics from the Communications Ministry, the market for newcomers - including MTU-Inform, Golden Telecom, Komstar and Combella - reached USD625 million in 2002, almost 13% of the country total. Newcomers have consolidated their businesses, ramped up efforts to steal market share from traditional operators and have begun offering next-generation services to maintain their positions. The government's stranglehold over sector pricing policy for state-run telcos combined with the poor quality and range of services available has contributed to the alternative operators' success and the corporate sector in particular has seized upon them with enthusiasm. In 2002 Golden Telecom shifted its focus, dumping its Cityline brand in favour of offering internet services under the ROL brand. In the summer it acquired Sovintel, having also bought shares in DLD operator Rostelecom. The company's brands - which include TeleRoss - have now all been merged under the Golden Telecom banner to create a unified vehicle.

In October 2002 Yury Pavlenko, the First Deputy Telecoms Minister, announced that USD3 billion would be invested in the country's underdeveloped telecoms market in 2003, with much of the money invested by Russians themselves, compared with the USD2.2 billion poured in during 2002. The need for investment in the fixed line market is urgent. In 2002, although money trickled into specific telecoms projects and individual companies, the shortfall proved to be a major headache. To raise cash

Facilities-based licensees

Operator	Date licensed	Operating licence	Network	Local telephone subscribers
Svyazinvest Regional Operators	1995	Local	PSTN	28,228,000
Comstar	1989	Local, long-distance, international	PSTN	48,000*
Telmos	1992	Local, long-distance, international	PSTN	na
PeterStar	1994	Local, long-distance, international	PSTN	100,000
MTU-Inform	1995	Local, long-distance, international	PSTN	360,000*
Smart	1998	Local, long-distance, international	PSTN	na
Golden Telecom	1999	Local, long-distance, international	PSTN	na
Rostelecom	1994	Long-distance, international	PSTN	23,000

Total number of telephone subscribers (end 2002): ~31.05 million

Teledensity (end 2002): 21.7%

* - end 2001

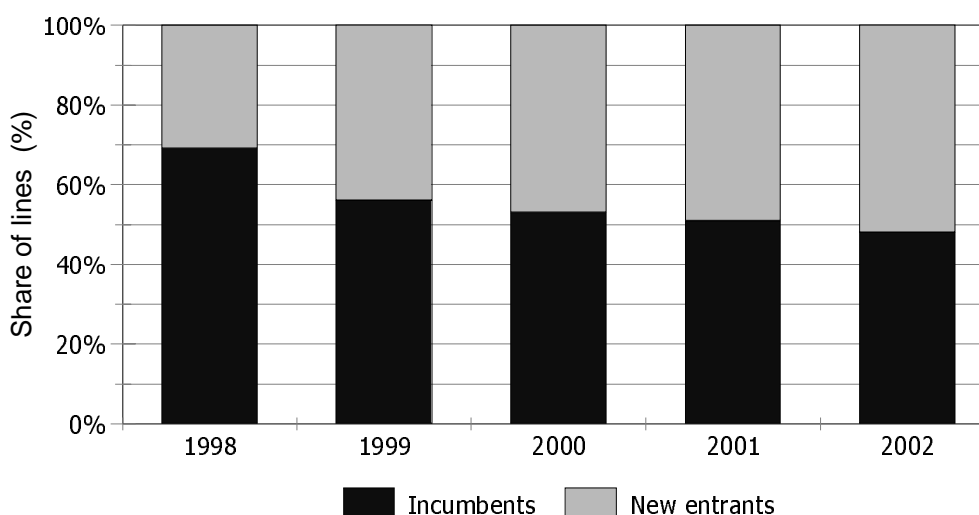
for development, telcos preferred to enter the western capital markets (via ADRs) and those which do not have the luxury of this route have opted for placing bonds domestically. Moscow City Telephone Network and Center Telecom both placed a total of RUR600 million. A number of regional operators also followed this path.

The market for IP telephony and VoIP continues to expand quickly. By January 2003 it had reached an estimated value of USD70 million, up 33% year-on-year. Hinting at the possibilities to come, IP-switching equipment vendor Cisco Systems announced its Russian sales of IP-related equipment had mushroomed by 650% since 2001. Some 700 companies hold licences to offer IP services, although their operations are reportedly undermined by state-run operator Rostelecom. The dominant carrier in the long-distance segment is concerned at the erosion of its business: IP is far cheaper and calls to places such as the US or Asia can cost as little as a fifth of the price offered by Rostelecom. In response the telco has signed itself up to the market and is prepared to use its financial and political clout - including its control of the infrastructure which IP operators use to access the globe - to protect itself.

Future analysis

The process of consolidation has taken hold in the Russian fixed line sector and this period of flux, combined with the long-term ramifications of the newly adopted telecoms law of July 2003, make it difficult to predict the immediate prospects for the country's telcos. Alfa Group's telecoms holding arm AFK Sistema has successfully amalgamated its Moscow wireline networks and in October 2002 acquired the 50% stake held by Alcatel in fixed line operator Golden Line for EUR100,000 - along with the assumption of EUR3.2 million in debt. Then, in April 2003 struggling US media group Metromedia International sold its Russian assets to Adamant Advisory Services, another AFK Sistema subsidiary. Over the course of 2002 Adamant purchased Metromedia's corporate bonds for EUR197 million and more recently exchanged EUR55 million worth of bonds for the American company's 50% stake in Moscow alternative telco Comstar, satellite TV company Cosmos TV and two FM radio stations. Metromedia still maintains a presence in Russia through alternative telcos PeterStar and BSL and cable TV unit Teleplus. Elsewhere, Svyazinvest too has successfully collapsed its 82 regional telephony operators (RTOs) into seven mega-regional businesses with the specific aim of improving profitability and the level of services.

Telecom market breakdown by player 1998-2002



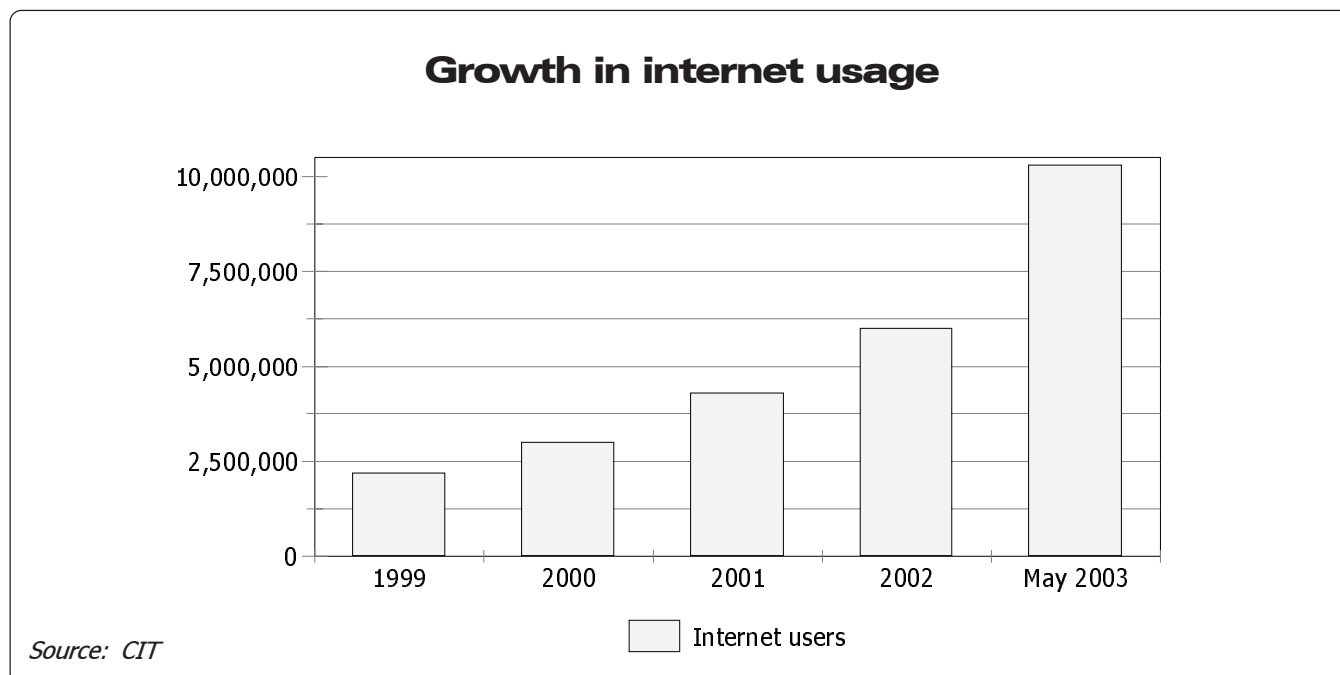
Source: State Statistics Committee

Residential market

Many Russians have been forced to endure a long wait for connection to the PSTN; by June 2002 some 5.5 million households were still waiting for a line. Svyazinvest to redress the situation progressively. It installed 1.9 million lines in 2001 and hoped to have commissioned 2.4 million lines by the end of 2002, rising to three million and four million lines in 2003 and 2004 respectively.

Despite these problems the market for internet services is beginning to take off and although only 10.2 million Russians, or 5% of the population, were online by May 2003, a Ministry report dated November 2002 predicted internet use would increase eight-fold by 2005. The Ministry believes that the proliferation of satellite-based systems will boost access in rural locations and new technology will halve the cost of access by that date. To this end the government hopes to launch no fewer than six satellites by 2005. In July 2002 the Communications Ministry ordered the Department of Information to hold a tender on forecasting the development of the country's internet segment through till 2010. Despite increases in internet uptake, Russia fell by three places to 45th in the list of 60 countries' e-readiness capability. Revenues from internet access services were estimated at EUR600 million in 2002.

Buoyed up by such enthusiasm, Russian ISPs such as RTKomm.RU are looking to spend heavily in order to capitalise in the long term. RTKomm.RU plans to invest over USD6 million in developing internet services in 2003, compared with USD2 million in 2002. According to its forecasts, the total market for internet services in Russia will increase from USD280 million in 2002 to USD350 million, split as follows: RTKomm.RU, USD35 million (USD26 million in 2002); Transtelecom, USD20 million (USD16 million), Golden Telecom, USD31 million (USD25 million), MTU-Intel, USD24 million (USD18 million), Svyazinvest regional companies, USD190 million (USD150 million), and other operators USD50 million (USD45 million). The volume of traffic handled is growing exponentially. In 2002 RTKomm.RU's internet traffic comprised 1,200 terabytes, double the amount of the previous year. It is forecast to increase by a further 50% in 2003.



Business market

The variable quality of the Russian telecoms infrastructure has impeded the development of voice, data and internet services for corporate customers. With patchy coverage of the fixed line network, Russian business services providers have generally opted to concentrate on selected cities rather than offering comprehensive coverage, so players present in St Petersburg do not necessarily have points of presence in Moscow or Nizhny Novgorod and vice versa.

Broadband services are in their infancy, with virtually all of the estimated 20,000 users at the end of 2002 being corporate customers in Moscow or St Petersburg; players looking to exploit the market include Sistema Telecom, Web Plus and Vesta Eurasia. Mir Telecom claims to have launched Russia's first DWDM-based network, although its exclusivity was short-lived, with

the launch of a similar network by Sonera Rus, the Russian arm of Scandinavian telco TeliaSonera, in October 2001. ADSL is similarly enjoying a period of unprecedented growth; as of July 2002 Moscow City Telephone (MGTS) had an installed capacity for 100,000 DSL lines, using equipment supplied by Cisco and Lucent.

In May 2002 US-based investment company Anderson Group said it was looking to buy Russian broadband provider ComCor-TV for around USD28 million in Anderson stock. It hopes to introduce new services such as IP telephony and high speed cable internet access in Moscow. The following August LLC TelecomInvest-XXI and Ericsson inked a EUR40 million contract for the supply of a multiservice network in Moscow and its environs, providing narrowband and broadband voice and data services for both private and business users. The following month Thuraya's partner in Russia, TM Sat, gained a licence from the Ministry to provide satellite services to undertake an 'experimental commercial operation of the Russian segment of the Thuraya network'. The word experimental will be dropped when TM Sat constructs an interlink station in Russia. TM Sat hopes to attract 70,000 users by the end of 2003.

Main players

Svyazinvest

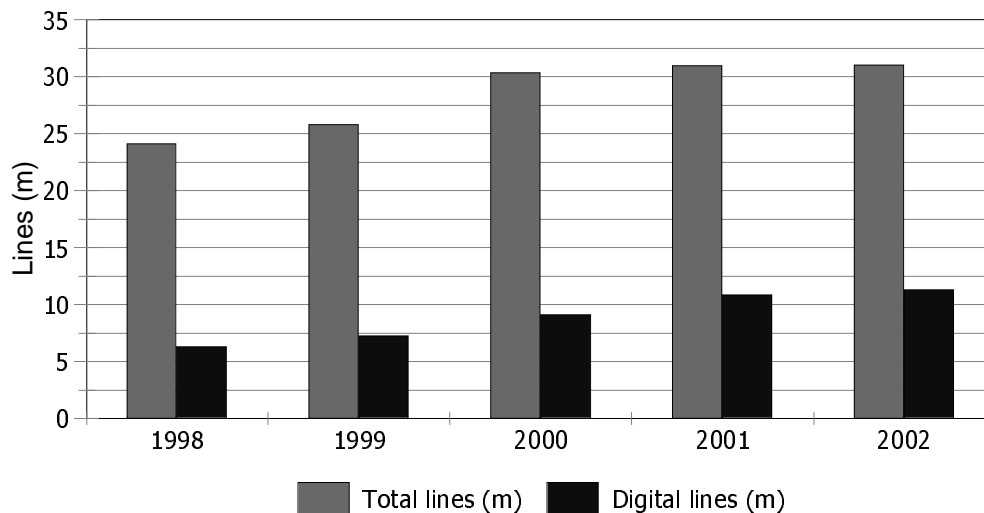
Svyazinvest was established in 1995 as a holding company for Russia's 80+ regional telecoms operators (RTOs). However, moves have been under way for several years to radically overhaul their structure and in 2002 the 82 RTOs in which Svyazinvest has a majority holding were collapsed into seven larger units. The holding company's self-stated aim is to improve the way the RTOs are managed and more importantly to increase profitability; at least 16 of the RTOs were reported to be making a loss in 2000. As a result of the restructuring, Svyazinvest now holds stakes of more than 50% in each of the seven mega-regional operators: CenterTelecom, North-Western Telecom, VolgaTelecom, Southern Telecom, Uralsvyazinform, SibirTelecom and Dalsvyaz. It also has minority stakes in Moscow Local Telephone Network MGTS (28%), Svyaz Komi Republic (25%), Ruslizinsvyaz (38%) and Kostroma GTS (37%), as well as a 51% interest in the country's national long-distance and international long-distance monopoly Rostelecom.

Svyazinvest's regional operators own licences to provide local, long-distance and international telephony, data transfer, internet, ISDN and wireless access services. The company also has concessions to offer mobile telephony in GSM, NMT-450, AMPS and D-AMPS standards. Its fixed line network covers nearly the whole of Russia and with an installed capacity of 30.16

Svyazinvest regional breakdown - 31 March 2003

	Installed capacity	Switched capacity	City digitalisation (%)
JSC Rostelecom	28,725	23,537	62.36
JSC MGTS	4,334,862	4,142,168	16.52
JSC Central Telecommunications	6,108,486	5,645,676	40.65
JSC North-Western Telecom	3,612,301	3,399,068	39.02
JSC VolgaTelecom	4,237,874	3,884,705	46.88
JSC South Telecommunications	3,545,008	3,311,848	47.00
JSC Sibirtelecom	3,781,316	3,437,228	50.89
JSC Dalnevostochnaya companya	1,191,227	1,086,939	44.40
JSC Uralsvyazinform	3,323,897	2,978,803	59.89
TOTAL	30,163,696	27,909,972	45.29

Growth of main lines December 2002



Source: Svyazinvest

million lines as at 31 March 2003, it made up over 90% of the country total. In the late nineties Svyazinvest's installed customer base has been falling, but in 2002 it rose from 27.22 million to 28.55 million and the company claimed a teledensity of 22.14%, up from 20.7%. In the first quarter of 2003 Svyazinvest posted revenues of RUR32.64 billion (USD1.07 billion) up 23.5% on the same period of 2002; profit rose by 15.8% to RUR8.93 billion.

Svyazinvest has been investing heavily in improving the quality and range of services. In October 2002 Center Telecom launched a USD10 million multiservice network based on equipment supplied by Lucent Technologies, covering 25 cities in the Moscow region. The network is capable of supporting both traditional telephony services and broadband data transmission, cable TV and other facilities. In 2003-04 Center Telecom plans to expand the reach to other regions of European Russia. Dalsvyaz, the fixed line services provider for the Far East Federal District, is to invest RUR15 million in 2003-04 in constructing a multiservice data transmission network in the Amur region. The Amur subsidiary of Dalsvyaz hopes to boost its client base by 10,000 to 135,000 in 2003. In mid-June 2003 Dalsvyaz said it was considering merging with Sibirtelecom. Its general director Igor Zabolotny stated that while no decision had been reached, instructions could be handed down directly from Svyazinvest. A month later Sibirtelecom said it expected to plough USD124 million into expanding its service coverage over the year. The company hopes to spend USD95 million on expanding its network by 362,000 fixed lines. Meanwhile Uralsvyazinform, the regional operator for the Urals, announced plans in July 2003 to offer bonds worth RUR3 billion on the Moscow Interbank Currency Exchange. In the same month Southern Telecom said it too was launching a bond issue worth RUR1.5 billion to finance investment projects related to upgrading old switches, increasing coverage and providing high speed internet access.

Svyazinvest is owned by Ministry of State Property of Russia (50% + one share), Russian Federal Property Fund (25% + two shares) and Mustcom (25% + one share).

Moscow City Telephone Network (MGTS)

2003 marks the 121st birthday of Moscow City Telephone Network (MGTS), the largest provider of local telecoms services in Moscow with 600 exchanges and 3.27 million subscribers at the end of 2002. It also produces five million payphone cards per annum at a cost of RUR15 million and owns and operates around 13,000 payphones in Moscow, St Petersburg, Sochi, Tver and other small towns in the Moscow region. The company came under the control of Svyazinvest in 1995 but looks set to loosen ties with the holding company during its ongoing restructuring. While Svyazinvest is keen to include it in its plans, analysts believe that the incentive is not there for MGTS and that it will decline the offer on the grounds that it already has a good market with profitable subsidiaries. The final decision, however, may rest on what is actually offered by Svyazinvest to the company's shareholders.

In 2003 MGTS plans to start the latest phase of its modernisation programme to replace old analogue exchanges with digital ones. The company intends to upgrade up to 200,000 numbers per annum and so double its digitalisation rate by 2006. As

a result of its efforts to direct major investments towards the repair of its network and new technologies, the number of lines to be installed in 2003 has been cut from 86,000 to 31,000. The volume of capital investments for the coming year will amount to RUR2.094 billion (USD65.8 million).

MGTS's main shareholders are Sistema (55.6%) and Svyazinvest (28%). The current capitalisation of MGTS is about USD626 million.

Comstar

Comstar was founded in 1989 as an equal joint venture between MGTS and Marconi (then known as GPT). Marconi sold out to US-based Metromedia International in June 2000 in a deal worth USD60 million, after MGTS waived its right of first refusal on the shares. In 2002 Metromedia declared itself bankrupt and began to sell its Russian assets. Its 50% stake in Comstar was sold to AFK Sistema.

Comstar was one of the first private companies in Russia to invest considerable funds - in its case USD75 million - in establishing a 1,240km advanced fibre-optic digital communications network. It has been operational in Moscow since April 1992 and today offers local, long-distance and international communications. Its primary focus is on the business services market, although it does have a portfolio of services for residential clients. By the end of 2001 (latest available figure - despite promises to provide end-2002 information) it had 48,000 lines in service, of which 85% were business connections - unchanged on the previous year. At the same date it reported 1,700 basic and 450 primary ISDN lines.

In May 2003 Comstar and Siemens signed a contract under which the German firm agreed to supply next-generation infrastructure equipment to run pilot tests for its new data network - NGN (new generation network). Once complete, NGN will be the country's first multiprotocol MPLS network capable of delivering VPN and VPLS services. The previous March Comstar

Svyazinvest: ownership breakdown (by regional telco)

	Svyazinvest holding	Other major shareholders
JSC Rostelecom	51%	Foreign investors (37%), Russian shareholders (10%), employees (2%)
JSC MGTS	28%	Sistema (55.6%)
JSC Central Telecommunications	50.69%	Foreign entities (6.37%) employees & other individuals (8.04%)
JSC North-West Telecom	39.89%	Brunswick UBS Warburg (13.17%), Depository Clearing Co (8.79%), ING Bank Eurasia (7.16%), Lindsell Enterprises (7.07%), Fractor Investments (2.84%) and JP Morgan Bank (1.61%)
JSC VolgaTelecom	50.67%	Foreign entities (6.68%), employees (6.55%)
JSC South Telecommunications	50.69%	Foreign entities (6.37%), employees & other individuals (8.04%)
JSC Sibirtelecom	50.67%	Foreign entities (5.35%), employees & other individuals (9.57%)
JSC Dalnevostochnaya Companya	50.56%	Foreign entities (18.56%), employees & other individuals (7.33%)
JSC Uralsvyazinform	51.42%	Foreign entities (3.02%), employees & other individuals (12.93%)

said it had begun offering ADSL-based services to all customers connected to its network at a cost of USD350. Internationally, Comstar's international capacity for carrying IP traffic was increased to 65Mbps in December 2002.

Comstar is owned by Sistema (50%) and MGTS (50%).

Rostelecom

Rostelecom began life as the USSR's national and international telecoms operator Sovtelecom before being restructured into its present incarnation in September 1993. It was granted operating licences for domestic long-distance (DLD) and international telephony in 1994 and remains Russia's dominant provider in those sectors. Rostelecom is the only Russian operator with contractual relationships with all of the country's PSTN operators, which are required by law to route their DLD and international traffic via Rostelecom's backbone network; it also operates Russia's ground network for TV and radio channels. In 2002 it claimed that the amount of domestic long-distance traffic it handled grew by 15.5% to 7.14 billion minutes; three years previously this figure stood at just 3.92 billion. Outgoing international traffic increased by 14.1% to 1.24 billion minutes, whilst the number of incoming international call minutes grew by 12% to 973 million.

Rostelecom's land network incorporates both analogue and digital transmission systems based on coaxial and fibre-optic cables and radio relay links. At the end of 2002 the network's analogue and digital plesiosynchronous transmission systems consisting of metal cables and radio relay links had a total length of 160,000km, whilst its fibre-optic links extended to 44,300km. The fibre-optic network utilises equipment principally from Alcatel, NEC and Siemens, although since 1999 Rostelecom has been using cables and equipment manufactured exclusively in Russia. The network is connected to Belarus, China, Denmark, Estonia, Finland, Japan, Italy, Kazakhstan, Korea, Turkey and Ukraine. Links are supplemented by the use of satellites; Rostelecom presides over eleven earth stations (3 hub stations and 8 peripheral stations) located in Siberia and the Far East regions, namely Gus-Khrustalny, Novosibirsk, Khabarovsk, Barnaul, Kirov, Gorno-Altai, Kyzyl, Yakutsk, Novokuznetsk, Juzhno-Sakhalinsk and Salekhard. By the end of 2002 the company claimed to have direct communication links with 75 operators from 72 countries. Its latest additions to the land-based network in late 2002 saw a fibre-optic line installed between Russia and Azerbaijan (200km in length) and an upgrade in the capacity of the existing 227km link between Kaliningrad and Kaunas to 34Mbps. In May 2003 Rostelecom signed an agreement with international carrier ITXC Corporation for the bilateral exchange of international voice traffic to and from Russia over ITXC's global VoIP network.

Rostelecom is owned by Svyazinvest (51%), foreign shareholders (37%), Russian shareholders (10%) and employees (2%).

North-Western Telecom

North-Western Telecom (formerly St Petersburg Telephone Network - PTN) is a provider of fixed line telephony services in St Petersburg and the areas of Kaliningrad, Pskov, Leningrad and Novgorod Region, Republic of Karelia, Nenets Autonomous District, Republic of Komi, Vologda, Archangel and Murmansk. It came into being in 2002 when regional telephone operators (RTOs) from eight territories merged into PTN to create an enlarged company with 3.5 million lines serving some 14.85 million people. Following ratification of the merger deal in March that year former PTN shareholders inherited a 63.8% stake in the new venture with the remainder split between Murmansk Elektrosvyaz (8.6%), Arkhangelsk Artelecom (7.5%), Kaliningrad Region (5.4%), Karelia Elektrosvyaz (4.8%), Novgorodtelecom (3.3%), Vologda Region Elektrosvyaz (2.3%), Pskovelektrosvyaz (2.2%) and Cherepovets Elektrosvyaz (2.1%). At the end of 2002 following the merger, North-Western Telecom reported 3,612,000 subscribers.

North-Western Telecom focuses on both the residential and business markets. It is developing its portfolio of ADSL services and working to improve digitalisation of its network by upgrading old switches. At the start of 2003 37% of the network was digitalised.

As at 1 July 2003 North-Western Telecom was owned by Svyazinvest (39.89%), Brunswick UBS Warburg (13.17%), Depository Clearing Co (8.79%), ING Bank Eurasia (7.16%), Lindsell Enterprises (7.07%), Fractor Investments (2.84%) and JP Morgan Bank (1.61%).

Golden Telecom (including Sovintel)

Headquartered in Moscow, Golden Telecom lays claim to being the largest independent facilities-based provider of telecoms and internet services to business users and telecoms operators in Russia and the Commonwealth of Independent States (CIS). It was incorporated in 1999 when US-based Global TeleSystems (GTS) brought its Russian and Ukrainian ventures under one roof. In October of that year GTS completed an IPO of Golden Telecom, raising USD128 million in the process, and then undertook a private share issue two months later which diluted its shareholding to around 62%.

Golden Telecom operates in more than 90 cities, offering the business community a range of local, long-distance, international and mobile telephony, internet access, leased line and call centre services. It also provides cellular operators with connection to the PSTN, and international carriers with voice traffic termination services, capacity resale and voice over internet protocol (VoIP) services. Although its portfolio is aimed primarily at the corporate community, Golden Telecom also provides dial-up internet access and pre-paid calling cards to the consumer segment. In Moscow in mid-2003 the company held 33% of the business voice telephony market, 24% of the corporate data services market and 25% of the residential dial-up internet sector in mid-2003, whilst in Russia's second city, St Petersburg, it claims to be the second largest supplier of voice and data services to the business market. Its other main markets are Nizhny Novgorod, Russia's third city, and the Ukraine capital Kiev, in both of which it claims to be the largest corporate services provider.

Golden Telecom's network infrastructure spans eight countries across the CIS, incorporating 149 points of presence at the end of 2002. At the same date it had over 300,000 digital lines in service, served by 22 switches and 808 private branch exchanges (PBXs). The company provides competitive local exchange carrier (CLEC) services via its overlay network in Moscow, St Petersburg, Kiev and Nizhny Novgorod and data and internet access services over a 2,000km fibre-optic and satellite network. It also offers internet content services through its Russia-On-Line (ROL) brand and operates mobile networks in Kiev, Odessa and Tajikistan.

In September 2002 Golden Telecom completed the purchase of the 50% of Moscow-based CLEC Sovintel it did not already own. It paid its partner in the venture, Rostelecom, USD56 million in cash for the stake in addition to 15% of Golden Telecom's shares and a representation on the board of directors. The company then merged Sovintel with existing subsidiary TeleRoss, hitherto active mainly in the provision of long-distance telephony services. Sovintel provides telephony, fax and data communication services principally in the capital and the metropolitan area of St Petersburg, in addition to local, long-distance and international phone services in Pskov, Kaliningrad, Novgorod, Perm, Yekaterinburg, Krasnodar, Kaluga and Karelia.

In June 2003 Golden Telecom said it was planning on increasing the company's liquidity by upping the number of publicly traded shares from 15% to 25%-30%. According to president and CEO Alexander Vinogradov, Golden Telecom aims to list itself on the Russian bourse although this is not a priority for 2003. The telco had USD24 million in cash for investment projects and network development at the start of the year and is also looking at bank loans if these funds prove inadequate. Also in June 2003 Golden Telecom confirmed its interest in acquiring Comincom-Combella, a rival carrier owned by Norwegian operator Telenor, in exchange for Golden Telecom shares. Telenor bought out the minority shareholders' combined 25% holding for USD30 million, suggesting that its equity swap stake would be worth just under USD600 million. Alfa Group, the oil-to-banking consortium which owns 39% of Golden Telecom, has confirmed it is keen to complete the equity swap.

Golden Telecom is owned by the Alfa Group (39%), Rostelecom (15%), Barings Vostok (9%), Capital Research International (8%), EBRD (11%) and management (3%); the remainder is in free float.

PeterStar

Formed in October 1992 through an initiative of the Leningrad City Telephone Network, PeterStar is one of the largest alternative operators in North West Russia and at the end of 2002 served around 100,000 people, unchanged from the previous year. Its primary customer base is the business market which accounts for 70% of all users. PeterStar provides local, long-distance and international telecoms voice and data transmission services across its 1,100km fibre-optic network consisting of ten SDH rings with transmission speeds of 2.4Gbps. The network has been integrated with the existing city telephone system and since its launch the company has invested more than USD100 million in network construction.

In 2002 PeterStar modernised some 35,000 lines on Vasilevskogo Island and the following July said it planned to invest USD500,000 in 2003 on installing WiFi hotspots in and around St Petersburg. By the end of the year it hopes to have deployed 15 terminals at Pulkovo airport, the sea port and in cafes, and hopes to have a further twelve broadband access points installed in local schools. The company offers a full portfolio of services based on ATM, frame relay, IP and DSL technologies.

PeterStar is owned by Metromedia (71%) and Telecominvest (29%).

Telmos

Closed joint stock company Telmos was created in April 1993 by MGTS and AT&T. Two years later Rostelecom purchased 10% from each founder member and in spring 2001 bought out AT&T to up its holding to 60%. In September 2001 Russian holding company AFK Sistema, which also has stakes in telecoms operators MTU-Infom and, indirectly, Comstar (via its controlling interest in MGTS), bought 40% back from Rostelecom for a consideration of USD17 million (EUR18.6 million). Sistema has

indicated its intention to merge all its telecoms assets and to this end has also merged two of its ISP assets, MTU-Intel and PTT-Teleport.

Telmos offers a full range of telecoms services to mainly corporate clients in Moscow and across Russia. It owns and operates a fibre-optic digital network which provides ISDN switching, and offers data transmission, voicemail and VPN services. The architecture uses SDH-rings for increased reliability.

Telmos is owned by Sistema (40%), MGTS (40%) and Rostelecom (20%).

MTU-Inform

Moscow-based MTU-Inform has been in operation in the capital since 1995 and holds concessions to provide local, long-distance and inter-regional telephony, data transmission and telematic services, as well as cable television. Its SDH fibre-optic network covers the entire city and environs. At the end of 2001 (latest available figure) MTU-Inform presided over 360,000 local telephony subscribers.

In 2002 MTU-Inform completed the modernisation of its peripheral SDH ring at a cost of USD1.8 million, connecting north west Russia and raising traffic capacity to 2.5Gbps. The company's strategic focus is on increasing its broadband provision and in July 2002 it completed tests of a new high speed cable network supplied by Motorola. The system will provide internet access at speeds of up to 10Mbps, based on the existing cable TV network. The upgrade project is part of the company's multiservice network development strategy. It has also introduced a new service, MAXIcard, which provides customers with access to high quality international and domestic communications. MTU-Inform's major clients include the Ministry for Emergency Monitoring, the Central Bank of Russia, US Embassy, Chevron, IBM, Shell and Pepsi.

ComCor

Moscow Telecommunication Corp (ComCor) was created in June 1992 as part of a project to create an advanced citywide data network. In September 1995 the company commenced phase one of construction of its network, comprising two rings, and by the start of 2003 its fibre-optic network spanned 10,000km, with 1,300km added in 2002 alone. The telco provides a broad range of services including dedicated lines, high speed internet access and systems integration for over 5,000 corporate clients.

Regulatory body

- State Committee of the Russian Federation on Communications and Information (Goskomsvyaz).

Key legislation

On 8 July 2003 Russian president Vladimir Putin signed the bill to put a new telecommunications act into law. The bill will set the legal basis for the telecoms sector in Russia and determine the authority that state bodies have, paying particular attention to the licensing process, which was not defined in detail in the previous law. The new law states that licences can be issued via tenders, auctions or other competitions, the rules for which will be set by the government. It also defines the rules for allocating radio broadcasting frequencies which will be initially assigned for a term of ten years or less.

Recent major regulatory activity

Russia's first national mobile operator MegaFon was formed when Sonera, Telia and Telecominvest merged their mobile assets in the country. It was licensed in early 2002 and holds concessions in 68 Russian regions covering 80% of the population. Since then, however, Moscow-based operators MTS, Tele2 and Moscow Cellular Communications (MCC) have all expanded their reach to cover the north west of the country - an area that covers St Petersburg and the surrounding area and in March 2003 Vimpelcom was given permission to launch a GSM-900 network there, the last cellco to do so. It launched commercial services the following month.

In January 2002 telecoms minister Leonid Reiman revealed that third-generation (3G) licences would be awarded on the basis of tenders and a commission would be established to oversee the process. In April 2003 he announced that the licences would be issued before the end of the year, as long as 3G handsets and infrastructure are available. At that date the government had yet to decide how many licences will be awarded and whether they will be issued on a regional or national basis. Likely bidders include market leader Mobile TeleSystems (MTS), Vimpelcom, MCC, Delta Telecom and MegaFon.

As part of the migration to 3G technology, in April 2003 the government upgraded the networks of six NMT-450 operators - MCC, Kusbass Cellular Communications, Cellular Communications of Bashkortostan, Rostov Cellular Telephone, Uralvestcom and Novosibirsk Cellular Communications - to CDMA-450. This solution is based on the 2.5G CDMA2000 1X technology, but operates in the 450MHz band and features smooth evolution towards 1xEV-DO and 1xEV-DV technology. The regulator hopes that the move will provide the market with an indication of the future popularity of 3G services.

Timeline of market development

August 1991	Moscow Cellular Communications launches Russia's first NMT-450 service in the Moscow region
1994	Vimpelcom licensed to provide D-AMPS service; MTS launches services over GSM-900 network, both in Moscow
1997	Vimpelcom receives DCS-1800 licence to operate in the Moscow region
2001	Tele2 enters Russian market through the acquisition of Fora Telecom; MegaFon enters Moscow market
January 2002	MegaFon licensed to provide GSM-900 services nationwide; telecoms minister announces plans to auction 3G licences via a tender
March 2003	Vimpelcom receives permission to launch GSM-900 services in the St Petersburg region, the last of the main operators to do so
April 2003	Government claims that 3G licences will be awarded before the end of the year; six NMT-450 operators have their licences upgraded to digital CDMA-450 technology as a stepping stone to 3G; Tele2 announces plans to launch GSM networks in Irkutsk, Rostov and St Petersburg.

Market commentary

The Russian mobile market is centred around the major cities of Moscow and St Petersburg, with the vast size of the country, the lack of roaming agreements between operators and the fact that the cellcos are licensed on a regional basis meaning that development in the more rural areas has been severely hampered. In early 2002, however, the market saw the creation of its first nationwide operator when MegaFon was awarded licences to operate in all seven of the country's regions. By the end of June 2003 MegaFon had rolled out commercial networks in four of these - Central, North West, Volga and Southern - and had revealed plans to launch in Siberia and the Eastern region before the end of the year. The move encouraged the regulator to award additional regional licences to the other main players in the market; during 2002 Sweden's Tele2 won licences to operate in Novgorod, Chelyabinsk and St Petersburg, giving it a total of twelve GSM licences in the country. It launched services in Irkutsk in the south in April 2003, Rostov in the south west in May and St Petersburg in the north west in June. In July it launched its fourth GSM network, in the Kemerovo region. MTS too has been expanding its reach during 2002/03, launching in the Kuban, North West and Siberia regions during the year; it also holds licences in the Republic of Tuva, Sakhalin, Chukotka and the Republic of Kalmykia through its wholly owned subsidiary Bit LLC. Vimpelcom was the most recent cellco to increase its coverage to the north west of the country, when it was given regulatory permission to launch a network in the St Petersburg region in March 2003.

In the year to March 2003 the total number of mobile subscribers in Russia grew from around 8.8 million to 23.7 million, with the cellular penetration rate shooting up to 16.6% from 6.1%. MTS managed to hold on to its number one position, but only just, with a 40.6% share, down from 46% the previous year. Its main rival Vimpelcom, on the other hand, managed to increase its share from 30.3% to 36.97% thanks to the expansion of its networks beyond Moscow. The other principal operators, MegaFon and MCC, hold market shares of 21.37% and 1.06% respectively.

One company which is keen to take on the might of MTS and Vimpelcom is Swedish alternative operator Tele2, which entered the Russian market at the end of 2001 when it took on the mobile assets of MIC and launched GSM services in Irkutsk, Rostov and St Petersburg during the second quarter of 2003. Although Tele2 does not release separate subscriber figures for its Russian operations, it claims to have already gained a significant number of customers. However, analysts are sceptical about its future success as cellular penetration in St Petersburg has already reached 30% and is relatively high in its other operating regions. Also Tele2 does not have a strong brand presence in Russia.

Future analysis

The Russian mobile market witnessed a year of unprecedented growth in the twelve months to the end of March 2003 with the total number of subscribers growing by 14.94 million. The spurt was mainly due to a regulatory decision taken during the year to allow Moscow-based operators to expand their coverage to other parts of the country. This growth looks set to continue with the overall penetration rate of 16.6% in March 2003 leaving plenty of room for further expansion - welcome news for all the operators which are currently competing with each other in the areas of highest penetration and are looking to expand their networks to more rural areas.

The government's intention to award 3G licences before the end of 2003 could encourage growth to accelerate at an even faster rate. The regulator is keeping a watchful eye on the progress made by western European 3G operators before it makes a definite decision: the low penetration rate has cast doubts as to whether the technology will take off to any great extent. In April 2002 the regulator upgraded six NMT-450 networks to CDMA-450 to create a stepping stone to 3G and to enable it to assess the future popularity of the technology.

Main players

Mobile TeleSystems (MTS)

Russia's largest mobile operator MTS entered the market in 1994 and is now active in all seven of the country's 'super regions'. After announcing that 2002/03 would be characterised by expansion, the cellco has stuck to its word. Following its launch in Tambov, Altai and Karelia in late 2001, at the beginning of 2002 it expanded to St Petersburg and the Leningrad region. In July that year, however, it decided against purchasing Samara-based operator SMARTS, despite being regarded as the most

likely buyer given that SMARTS operates in the Volga region where MTS had been looking to establish a presence. This issue was solved in March 2003, however, when the Ministry of Communications issued MTS with a licence to provide GSM-900/1800 services in the Samara region. MTS has continued with its expansion strategy throughout late 2002 and early 2003 with the acquisition of several smaller cellcos. In October 2002 it completed the purchase of a 100% stake in GSM operator Dontelecom, which provides services in the southern Rostov region, and later that month purchased a 100% stake in Bit LCC, which holds licences in the Republic of Tyva, Sakhalin, Chukotka and the Republic of Kalmykia. In April 2003 the cellco completed an agreement to acquire a controlling stake in Tatarstan-based operator TAIF-TELKOM.

At the end of March 2003 MTS claimed a national market share of 40.6% and a customer base of 7.6 million, a significant increase on the 4.05 million it reported at the same time in 2002. It says the strong growth is mainly down to its aggressive expansion programme which has given it access to a completely new customer base. In November 2002 MTS introduced its first pre-paid offering, launched under the banner 'Jeans'; at the end of March 2003 around 11% of its total customer base were 'Jeans' subscribers. The cellco has also been rolling out multimedia messaging services (MMS); in May 2003 it teamed up with Nokia to bring the service to customers in the Kuban, North West and Siberia regions and the following month selected LogicaCMG to deploy the offering in Moscow.

MTS is owned by AFK Sistema (42%) and Deutsche Telekom (36.27%). The remainder is traded on the New York stock exchange.

Vimpelcom

MTS's main rival Vimpelcom managed to gain considerable ground in the year to 31 March 2003 thanks to the expansion of its network to the St Petersburg area. It has always been within striking distance of MTS, but without a licence for the North West region, had found it hard to compete successfully. It had already begun expanding its network out of the Moscow region when it was given permission to launch in the north west; in December 2002 it completed the acquisition of Vostok-Zapad

Main operators

Mobile telephony

Operator	Network	Launch date	Subscribers (000)		% change	% pre-paid	WAP/GPRS launched?
			March 2002	March 2003			
Mobile TeleSystems	GSM-900	1994	4,050	7,600	88%	11%	WAP GPRS trial
Vimpelcom	DCS-1800	1997	2,662	6,920	160%	70%	both
MegaFon	GSM-900	2002	1,600*	4,000	150%	na	WAP HSCSD/ GPRS trial
Moscow Cellular Communications	NMT-450	1991	85**	200	18%	-	no
Others	-	-	~400	~5,020	-	-	-
Cellular penetration			6.14%	16.6%			
Total mobile subscribers:			~8,797,000	23,740,000			
*June 2002 **end 2001							

Telecom which holds a licence for the Ural region. By the end of March 2003 Vimpelcom had increased its market share to 36.97% from 30.3% at the same time in 2002, in the process stealing percentage points away from MTS. It had over 6.9 million customers at the same date, up from 2.66 million, boasting the largest increase - 160% - of all four of the main operators. According to its own figures, 4.22 million of its subscribers were in the Moscow licence area and 2.7 million elsewhere.

In addition to its expansion strategy, Vimpelcom has also launched a number of new offerings to keep up with its rivals. It was the first cellco to launch GPRS services commercially in April 2002 and in May 2003 it joined forces with French equipment supplier Alcatel to launch a 3G trial at the Svyas-Expocom trade fair, the first time that 3G had been demonstrated in Russia.

Vimpelcom is owned by Telenor (28.9%), Alfa (13% + 2 shares), free float (45.5%) and treasury shares (4.45%). The remaining 8.15% is floated.

MegaFon

MegaFon enjoyed a brief advantage over its competitors, when it was the only operator to have nationwide coverage. It was formed in mid-2001 when Telia and Sonera (now TeliaSonera) merged their Russian cellular holdings with those of Telekominvest and was awarded licences for all seven of the country's 'super regions'. However, this situation changed in 2002 when its rivals MTS, Vimpelcom and Tele2 were all granted regulatory permission to expand their networks outside their traditional operating regions. At the end of March 2003 MegaFon was the third largest cellco in the country, with a market share of 21.37% and a customer base of around four million, up from 18.3% and 1.6 million in June 2002.

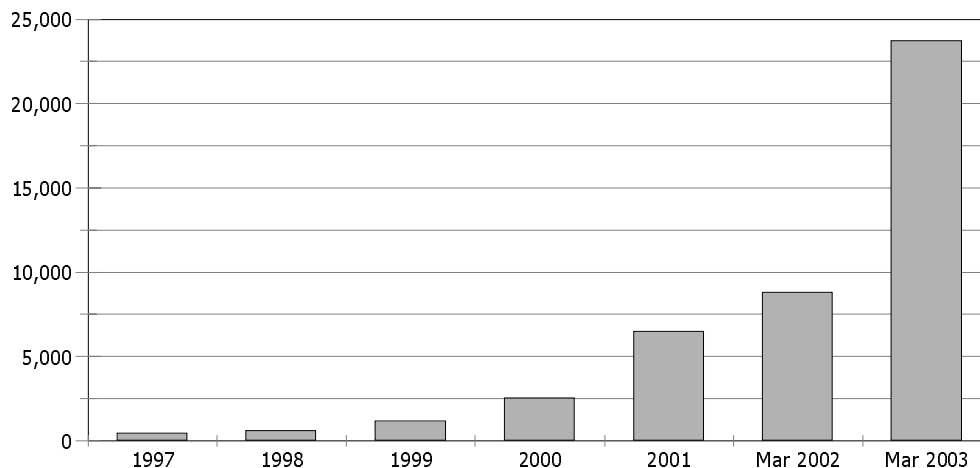
Like its rivals, Megafon has been rapidly expanding its portfolio of services. In December 2002 it launched trial GPRS and MMS services in the Moscow and St Petersburg areas and in February 2003 MMS was launched commercially on a nationwide basis. MegaFon has also revealed plans to launch mobile TV services over its GPRS network in the second half of 2003.

MegaFon's major shareholders are TeliaSonera, Telekominvest and CT-Mobile.

Moscow Cellular Communications (MCC)

MCC was the first cellco to launch in 1991 over its NMT-450 network and by the end of March 2003 offered services to around 200,000 people, a market share of 1.07%. It saw its customer base fall in 2001, ending the year with 85,000 subscribers compared with 98,000 the previous June, but during 2002 it managed to boost it considerably thanks to a modernisation scheme. MCC has been gradually encouraging its customers to switch from analogue to digital services and in April 2003 it was one of six cellcos to have its network upgraded to CDMA-450.

Growth of wireless services
Total number of subscribers (000)



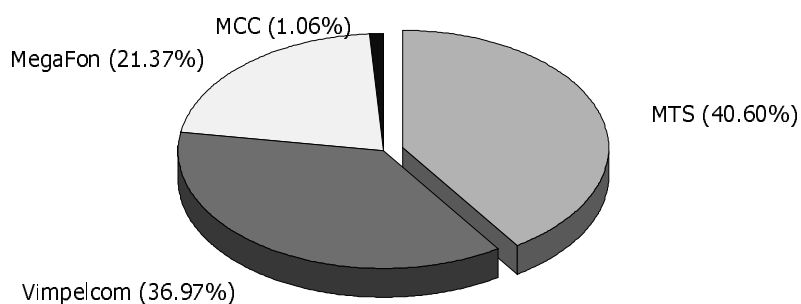
Source: operators

Tele2

Swedish alternative operator Tele2 entered the market in late 2001 via the acquisition of Fora Telecom, the holding company for the Russian mobile assets of Millicom International Cellular. Tele2 inherited Fora's twelve cellular operations in Belgorod, Chelyabinsk, Irkutsk, Kemerovo, Kursk, Moscow, Nizhny Novgorod, Omsk, Rostov-on-Don, Smolensk, St Petersburg and the Republic of Udmurtiya, and also holds five additional concessions. It does not provide operational statistics for its operations in Russia but regards the market as a good opportunity for substantial growth, particularly in the less well penetrated areas.

In the first seven months of 2003 Tele2 launched four GSM networks under the Tele2 brand name in Russia, beating its goal of rolling them out before the end of the year. The first was rolled out in April in Irkutsk, followed by one in Rostov later that month. In June it launched its third GSM network in St Petersburg and the fourth was rolled out on 12 July in the Kemerovo region of South West Siberia.

Tele2 owns 100% of Fora Telecom and its assets. It is itself owned by MIC (12.73%), Invik & Co (10.56%) and Brotherton Corporation (5.77%); no other shareholder holds more than 4%.

Wireless market share**September 2002**

Source: operators

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