CENTRAL EUROPE & RUSSIA FUND INC
Form N-CSRS
July 05, 2006
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM N-CSRS

Investment Company Act file number 811-6041

Central Europe & Russia Fund, Inc.

(Exact Name of Registrant as Specified in Charter)

345 Park Avenue

New York, NY 10154

(Address of principal executive offices) (Zip code)

Registrant s Telephone Number, including Area Code: (212) 454-7190

Paul Schubert

345 Park Avenue

New York, NY 10154

(Name and Address of Agent for Service)

Date of fiscal year end: 10/31

Date of reporting period: 04/30/06

ITEM 1. REPORT TO STOCKHOLDERS

The Central Europe and Russia Fund, Inc.

LETTER TO THE SHAREHOLDERS

Dear Shareholder,

For the six months ended April 30, 2006, the Central Europe and Russia Fund's total return (based on its net asset value per share) was 46.26% in US dollar terms, while its total return based on share price was 27.15%. The fund's benchmark rose 53.28% during the same period.[1] (Past performance is no guarantee of future results. Please see page 3 for more complete performance information.)

During the first quarter of 2006, the Russian RTX index was among the top ten best performing markets in the world, boosted by soaring commodity prices, strong domestic liquidity, and inflows of foreign funds attracted by high oil prices and interest in Gazprom shares ahead of the implementation of the full liberalization of local shares. As the index continued to gain ground, concerns of an asset bubble began to increase. While the extensive IPO pipeline scheduled to come out of Russia over the next 12 to 18 months may provide new investment opportunities that could attract new global investors to the Russian market, some are concerned that there could be an excess supply of new shares flooding the market. As a result, stock selection will become increasingly important. Overall, the Fund's positioning in Russia contributed positively to performance as several holdings in the oil and gas sector posted strong gains, in-line with the Fund mana gement's view that higher commodity prices would persist through the first quarter of 2006. During the reporting period, the Fund initiated positions in natural gas company, Novatek, and cosmetics company Kalina while reducing its position in food retailer, Pyaterochka Holding.

In Turkey, strong fundamentals such as easing domestic interest rates, GNP growth, and rising corporate earnings have been supportive of equity markets. However, market performance continues to be affected by global liquidity concerns coupled with nervousness regarding Turkey's progress on negotiations with the EU and the IMF. Signs of rising foreign direct investment, spurred by the success in 2005 of several key privatizations after years of delay notably Turk Telekom, Tupras, Petkim and Erdemir could become a source of optimism for the market. Electricity distribution projects and state banks are on the privatization agenda, and almost all the banks that lack a major international partner are potential M&A targets. During the reporting period, Fund performance benefited from holdings in the Turkish financial sector, one of the Fund's main investment themes. Despite the existence of compelling valuations and investment th emes, the Turkish market continues to be subject to significant volatility related to political and macroeconomic developments. As a result, it will be important to monitor these developments closely.

The Czech equity market trades on an estimated P/E of 17.9x for 2005, and forecast P/Es of 19.2x for 2006, which not only places the Czech equity market on higher valuations than its Central European peers, Hungary and Poland, but also most Western European markets (though the limited number of stocks in the Czech benchmark means it is not necessarily representative of the broader market). Despite these rather lofty valuations, the market could still add to its total return figure over the balance of 2006 due to steady earnings growth and high dividends from a number of blue-chip stocks. Currently, the weighting of Czech stocks within the portfolio remains well below that of the Fund's benchmark, but the Fund may look to increase its exposure to Czech equities during periods of market turbulence. The good dividend yields offered by a few Czech stocks combined with the country's favorable macroeconomic environment and benign political situati on may allow some Czech equities to hold up better than other East European stocks in market downturns.

Hungarian blue-chips are reasonably valued, with some shares, if not overly attractive, offering good upside potential from either company-specific factors or from sector trends. However, due to growing concerns over the imbalances in the Hungarian economy, the Hungarian equity

LETTER TO THE SHAREHOLDERS (continued)

market is likely to find the going tougher than other markets across the region.

The Polish equity market is causing a bit of debate due to the conflicting outlooks it presents from a top-down versus bottom-up perspective. The top-down story for Poland remains appealing and may even be improving. GDP estimates have been raised, interest rates have been reduced, and funds continue to flow into both pension and mutual funds. Counterbalancing these positives, though, are some more fundamental bottom-up negatives including lofty valuations, and modest earnings growth estimates.

However, there are signs that investor risk tolerance may be substantially declining, which could ultimately make Poland a more attractive market compared to higher beta markets such as Turkey and Russia. During the reporting period, the Fund initiated positions in two Polish banks PKO Bank Polski and Bank PBK (Bank Prezemyslowo-Handlowy PBK).

The Fund's discount to net asset value averaged 4.25% during the six months ended April 30, 2006.

The sources, opinions and forecasts expressed herein are as of May 2006. There is no guarantee that the views, opinions and forecasts expressed in this report will come to pass. This information is subject to change at any time based on market and other conditions and should not be construed as a recommendation for any specific security. Past performance does not guarantee future results.

[1] A custom blend of 45% in Central Europe (CECE-Index), 45% Russia (RTX-Index) and 10% in Turkey (ISE National 30).The CECE is a regional capitalization-weighted index, including stocks from the Czech Republic, Hungary, Poland and Slovakia and is published daily by the Vienna Stock Exchange. The RTX is a capitalization-weighted index of Russian blue chip stocks and published daily by the Vienna Stock Exchange. The ISE National 30 is a capitalization-weighted index composed of National Market companies except investment trusts and will also be used for trading in the Derivatives Market. Index returns assume reinvestment of dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly in an index.

Sincerely,

Christian Strenger
Chairman

For additional information about the Fund including performance, dividends, presentations, press releases, daily NAV and shareholder reports, please visit www.ceefund.com

ECONOMIC OUTLOOK

Czech Republic:

Economic activity appears to be at the top of the cycle, with GDP growth reported at 6.9% year-over-year (y-o-y) in the fourth quarter of 2005. The structure of GDP looked healthy, as exports remained the key driver. Most recent indicators on industrial output and retail sales have confirmed the positive trend in these data points into Q1 2006 and are likely to be sustained through the first half of the year. Currently many forecasters have the full-2006 pace of GDP growth penciled in at above 5% y-o-y, and expect a slight shift in the GDP structure away from exports towards private consumption and capital formation. Wage growth is set to stay moderate and unemployment is set to decline only marginally, leaving little scope for demand-led inflationary pressures. The CPI level was elevated by energy prices at the start of 2006. While some second-round impacts are to be expected in coming months, the core CPI will likely be little affected.

Hungary:

Exports supported by a weak Hungarian Forint (HUF) and stronger European Union (EU) demand together with a slight pick-up in household consumption should broadly counterbalance the possible sharp slowdown of investments (zero/slightly negative y-o-y investment growth) and keep GDP growth rate around 4.2% y-o-y in 2006. The current account is projected to deteriorate by about EUR 1 billion from the 2005 level, which would place it at 8.2% of GDP in 2006. The cashflow-based government budget deficit has reached 45% of the year-end target and will likely overshoot the HUF 1,500 billion target by around HUF 250 billion without any modification in the budget bill. A higher Q1 2006 CPI figure - up 3.5% over Q1 2005 - means that further monetary easing is unlikely over the near term. The potential increase in the discount VAT rate, a weaker HUF and slightly accelerating household demand all point to upside inflation risks.

Poland:

Growth prospects remain very favorable, and consensus GDP growth forecasts have been raised for 2006 from 4.5% to 5%. Industrial production grew by 9.6% year-on-year in January, 9.8% year-on-year in February and 10.2% year-on-year in March, driven by even higher manufacturing due to continuously strong export demand. Exports grew by 19.8% in March 2006, enabling the current account deficit to narrow to around 1.4% of GDP. This positive trend in exports is likely to continue as Western Europe's economy is gaining speed. Poland's economy is closely integrated into the German investment cycle and both capital goods industries and construction should benefit substantially from this year's investment-driven pick-up in Germany. So far, Polish growth has been mainly supported by external demand and investment. However, with employment growing at close to 2.5% plus wages growing at 2-3% in real terms, aggregate real household income is now rising by 5-6%. Therefore, private consumption growth should pick up, as reflected by nominal retail sales which show growth of 8.6% in January, 10.2% in February, and 9% in March.

Russia:

January through March was characterized by exceptionally cold weather conditions, which had a temporary impact on almost all economic performance indicators: investment growth turned into the red, industrial production growth fell at 1% y-o-y despite good momentum in business confidence indicators, and household consumption "slowed" to circa 10% y-o-y. The impact on fiscal and foreign trade balances was counter-balanced by higher-than-expected oil prices, as both the fiscal balance and the trade balance reached all-time high surpluses. However, the structure of GDP growth continues to deteriorate (i.e., more driven by household demand fuelled by a looser fiscal policy), resulting in potentially higher inflation (core YTD inflation is up 3.2% through April) and a worsening ex-oil trade balance. Key risks to the economy remain the lack of reforms, capacity constraints, inflation and a weak long-term political outlook, but with net debt to GDP negative, structural risks are likely to remain in the back seat for now.

Turkey:

GNP surprised on the upside in Q4, pushing the full-year growth to 7.6% compared to expectations of 6%. Private investment spending, up 42% y-o-y, remains strong, with corporates continuing to show confidence in the government's reform program, and the start of EU accession talks clearly playing their part. Private consumption spending rose 16.7% y-o-y in Q4, while the lack of growth in government spending provides some comfort and support in discussions with the IMF. As of April, CPI is up 8.2% year-on-year and will need to be monitored as EU negotiations progress. We expect a budget deficit below the 2% of GDP seen in 2005 and debt to GDP heading under the Maastricht target of 60% by the end of 2007. The current account (C/A) deficit remains a significant risk with a C/A deficit to GNP ratio of 7% possible this year. FDI covering at least 60% of this year's C/A deficit is expected, with potential to the upside (depending on M&A activit y). Foreign exchange reserves are close to six months of imported goods and services, above the Emerging Market average of around five months.

FUND HISTORY AS OF APRIL 30, 2006

All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when sold, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please visit www.ceefund.com for the Fund's most recent performance.

TOTAL RETURNS:

	For the six months ended April 30, 2006(c)	For the years ended October 31,				
		2005	2004	2003	2002	2001
Net Asset Value(a)	46.26%(d)	48.74%	35.20%(b)	44.88%	17.05%	(14.31)%
Market Value(a)	27.15%	80.71%	18.73%	60.38%	23.43%	(7.79)%
Benchmark	53.28%(1)	37.81%(1)	32.73%(2)	40.65%(3)	14.68%(4)	(20.40)%(5)

(a) Total return based on net asset value reflects changes in the Fund's net asset value during the period. Total return based on market value reflects changes in market value. Each figure includes reinvestments of distributions. These figures will differ depending upon the level of any discount from or premium to net asset value at which the Fund's shares trade during the period.

(b) Return excludes the effect of the $2.15 per share dilution associated with the Fund's rights offering.

(c) Total returns shown for the six month period are not annualized.

(d) Return excludes the effect of the $3.25 per share dilution associated with the Fund's rights offering.

(1) Represents an arithmetic composite consisting of 45% CECE*/45% RTX**/10% ISE National 30***.

(2) Represents an arithmetic composite consisting of 70% CECE/30% RTX for the 5 months ended 3/31/04 and 45% CECE/45% RTX/10% ISE National 30 for the seven months ended 10/31/04. The Fund changed its benchmark from 70% CECE/30% RTX to 45% CECE/45% RTX/10% ISE National 30 on April 1, 2004.

(3) Represents an arithmetic composite consisting of 85% CECE/15% RTX for the 9 months ended 7/31/03 and 70% CECE/30% RTX for the 3 months ended 10/31/03. The Fund changed its benchmark from 85% CECE/15% RTX to 70% CECE/30% RTX on August 1, 2003.

(4) Represents the CECE Index.

(5) Represents an arithmetic composite consisting of a customized MSCI index for the 2 months ended 12/31/00 and the CECE Index for the 10 months ended 10/31/01. The customized MSCI index consists of 35% Germany, 20% Poland, 15% Hungary, 10% Czech Republic, 10% Russia and 10% Austria. The Fund changed its benchmark from a customized MSCI Index to the CECE Index on January 1, 2001.

* *The CECE is a regional capitalization-weighted index including stocks from the Czech Republic, Hungary and Poland and is published daily by the Vienna Stock Exchange.*

** *The RTX is a capitalization-weighted index of Russian blue chip stocks and published daily by the Vienna Stock Exchange.*

*** *The ISE National 30 is a capitalization-weighted index composed of National Market companies except investment trusts and will also be used for trading in the Derivatives Market.*

Index returns assume reinvestment of dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly in an index.

Investments in funds involve risks including the loss of principal.

This Fund is not diversified and may focus its investments in certain geographical regions, thereby increasing its vulnerability to developments in that region. Investing in foreign securities presents certain unique risks not associated with domestic investments, such as currency fluctuation and political and economic changes and market risks. This may result in greater share price volatility.

Shares of closed-end funds frequently trade at a discount to net asset value. The price of the Fund's shares is determined by a number of factors, several of which are beyond the control of the Fund. Therefore, the Fund cannot predict whether its shares will trade at, below or above net asset value. Closed-end funds, unlike open-end funds, are not continuously offered. There is a one-time public offering, and once issued, shares of closed-end funds are sold in the open market through a stock exchange.

The Fund is complying with the German tax transparency rules for the current fiscal year that ends on October 31, 2006 and therefore qualifies as a transparent fund within the meaning of the German fund tax law (InvStG 2004).

FUND HISTORY AS OF APRIL 30, 2006 (continued)

STATISTICS:

Net Assets	$ 809,084,113
Shares Outstanding	14,002,505
NAV Per Share	$ 57.78

DIVIDEND AND CAPITAL GAIN DISTRIBUTIONS:

Record Date	Payable Date	Ordinary Income	ST Capital Gains	LT Capital Gains	Total
12/20/05	12/30/05	$ 0.33	$ 0.215	$ 2.507	$ 3.05
12/22/04	12/31/04	$ 0.17	$	$	$ 0.17
12/22/03	12/31/03	$ 0.22	$	$	$ 0.22
11/19/01	11/29/01	$ 0.10	$ 0.13	$	$ 0.23

OTHER INFORMATION:

NYSE Ticker Symbol	CEE
NASDAQ Symbol	XCEEX
Dividend Reinvestment Plan	Yes
Voluntary Cash Purchase Program	Yes
Annualized Expense Ratio (4/30/06)*	1.04%

* Represents expense ratio before custody credits. Please see "Financial Highlights" section of this report.

10 LARGEST EQUITY HOLDINGS AS OF APRIL 30, 2006 (As a % of Portfolio's Market Value*)

1.	Surgutneftegaz	11.3
2.	Lukoil	10.7
3.	OAO Gazprom	9.8
4.	Unified Energy System	5.5
5.	JSC MMC Norilsk Nickel	4.5
6.	Polski Koncern Naftowy	4.4
7.	Tatneft	3.9
8.	Ceske Energeticke Zavody	3.2
9.	Telekomunikacja Polska	3.1
10.	Mol Magyar Olaj-ES Gazipari	2.5

*Percentage (%) of market value refers to all securities in the portfolio, except cash and equivalents.

GEOGRAPHICAL REPRESENTATION OF HOLDINGS BY COUNTRY

10 Largest Equity Holdings and Country Breakdown are subject to change and may not be indicative of future portfolio composition.

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling 1-800-SEC-0330.

INTERVIEW WITH THE LEAD PORTFOLIO MANAGER Ralf Oberbannscheidt

Question: **As this summer's G-8 summit approaches, the US has become increasingly critical of the Russian government. What are the reasons for this and what are the implications for the financial markets in Russia?**

Answer: Russia's chairmanship of the G-8 got off to a rocky start this year when state-controlled Gazprom cut off the gas supply to Ukraine amidst a pricing dispute, causing some to question Russia's reliability as an energy supplier for Europe and accuse President Putin of using energy supply as a policy tool. The US has been critical of the advancement of democracy under President Putin for some time, but recent developments including the Gazprom price increases and the Russian government's decision to ban imports of selected goods from Georgia, Moldova, and Ukraine have raised questions about the government's role in the economy. Although President Bush is expected to attend the G-8 summit, there is speculation that he will give President Putin a lukewarm reception. Nonetheless, in an environment of sustained high energy and commodity price s, the incentive to invest in commodity-rich markets, such as Russia, is likely to outweigh the impact of any negative political sentiment, though some short-term volatility is possible. However, investors will be closely monitoring the government's involvement in company affairs and are likely to favor those companies that have a strong relationship with the government.

Question: **Recent political, economic, and market developments in Turkey suggest that the stability of the past few years may be in question. Could you comment on the reasons for this and the prospects for a return to stability?**

Answer: Due to a variety of factors, 2006 is turning out to be a relatively turbulent year for Turkey. The current account deficit continues to be the most significant issue on the macroeconomic front, as the government struggles to contain spending. Amidst reports of higher-than-expected inflation and concerns that the current account deficit will reach 7% of GDP this year (compared to initial forecasts for 6% of GDP), Turkey's currency has depreciated sharply. In addition, the government has faced political difficulty over a variety of issues, leading to speculation that early elections may be necessary. From an economic perspective, the currency depreciation should boost Turkish exports, and GDP growth is still expected to remain strong. However, the recent instability underscores the importance of the IMF program as well as eventual European Union ("EU") membership as a real possibility for Turkey to work toward.

Question: Lithuania's application to adopt the euro next year was recently rejected. Meanwhile, Latvia and Estonia have postponed their timeline for adopting the euro. How does this impact plans for euro adoption by the CE-3 countries?

Answer: The EU recently accepted Slovenia's bid to adopt the euro in 2007 while rejecting Lithuania's application for failure to meet all of the Maastricht criteria. In particular, Lithuania's inflation, at 3.5%, is higher than the target rate. Several of the fifteen original EU countries were given leniency on meeting the Maastricht criteria when the euro was introduced in 1999, but amidst growing political opposition to enlargement, the EU is clearly sending a signal that it will not provide any leniency to new EU members. Because the Czech Republic, Hungary, and Poland are not planning to adopt the euro until at least 2010, the rejection of Lithuania's application has no immediate impact on their plans to adopt the euro. However, it will be important to monitor whether the EU continues to strictly enforce the Maastricht criteria, which some argue are out dated and fail to take into account the fact that higher inflation is a by-product of the current macroeconomic environment of high growth rates in the new EU countries, coupled with high oil prices.

Ralf Oberbannscheidt, Lead Portfolio Manager of the Central Europe and Russia Fund, Inc.

THE CENTRAL EUROPE AND RUSSIA FUND, INC.
SCHEDULE OF INVESTMENTS APRIL 30, 2006 (unaudited)

Shares	Description	Value
INVESTMENTS IN RUSSIAN SECURITIES 58.0%		
	COMMON STOCKS 55.9%	
	COMMERCIAL BANKS 0.7%	
3,000	Sberbank	$ 5,430,000
1,000	Sberbank RF-(GDR) Reg S	178,849
		5,608,849
	DIVERSIFIED TELECOMMUNICATION SERVICES 0.5%	
200,000	Rostelecom (ADR)	4,260,000
	FOOD PRODUCTS 1.0%	
116,319	Lebedyansky*	7,880,612
	METALS & MINING 7.6%	
281,000	JSC MMC Norilsk Nickel (ADR)	37,092,000
85,600	Mechel OAO-(GDR) Reg S	2,311,200
416,000	Polyus Gold Co Zao (ADR)	17,971,200
3,500	Vyksa Metallurgical Plant*	3,850,000
		61,224,400
	MULTI-UTILITIES 5.4%	
568,000	Unified Energy Systems (GDR)	43,736,000
	OIL, GAS & CONSUMABLE FUELS 38.7%	
1,400,000	Gazprom	15,960,000
943,000	Lukoil (ADR)	85,435,800
450,000	Novatek Oao-Spons (GDR)	19,125,000
1,375,000	OAO Gazprom (ADR)	62,425,000
1,040,000	Surgutneftegaz (ADR)	90,480,000
262,500	Tatneft (ADR)	30,843,750
1,143,800	Tnk-Bp	3,888,920
500,000	Ufimskij Npz	1,350,000
52,000	Vostok Nafta Investment (SDR)*	4,002,602
		313,511,072
	PERSONAL PRODUCTS 1.0%	
181,000	Kalina	8,145,000
	WIRELESS TELECOMMUNICATION SERVICES 1.0%	
140,000	Mobile Telesystems (GDR)	4,576,600
50,000	Mobile Telesystems-SP (ADR)	1,634,500
45,500	Vimpel Communications (ADR)*	2,119,845
		8,330,945
	Total Common Stocks (cost $186,560,404)	452,696,878

Shares	Description	Value

	PREFERRED 2.1%	
	OIL, GAS & CONSUMABLE FUELS 2.1%	
7,750	Transneft Preferred (Cost $17,515,000)	$ 16,662,500
	Total Investments in Russian Securities (cost $204,075,404)	469,359,378
INVESTMENTS IN POLISH COMMON STOCKS 13.1%		
	BUILDING PRODUCTS 0.6%	
850,950	Cersanit-Krasnystaw SA	4,956,883
	COMMERCIAL BANKS 3.0%	
81,746	Bank Pekao SA	5,480,060
25,000	BK Prezemyslowo-Handlowy PBK	6,443,425
1,000,000	Pko Bank Polski SA	12,561,424
		24,484,909
	CONSTRUCTION & ENGINEERING 0.1%	
40,842	Budimex*	744,298
	DIVERSIFIED TELECOMMUNICATION SERVICES 3.1%	
2,920,207	Telekomunikacja Polska	21,381,971
490,000	Telekomunikacja Polska (GDR)	3,650,500
		25,032,471
	MEDIA 0.1%	
37,700	Tvn*	1,177,780
	METAL & MINING 0.7%	
147,029	KGHM Polska Miedz	5,382,786
	OIL, GAS & CONSUMABLE FUELS 4.3%	
1,036,102	Polski Koncern Naftowy	21,579,136
149,500	Polski Koncern Naftowy (GDR)	6,092,125
180,000	Polski Koncern Naftowy (GDR)	7,335,000
		35,006,261
	REAL ESTATE 1.2%	
109,018	Echo Investment*	9,472,422
	Total Investments in Polish Common Stocks (cost $50,091,954)	106,257,810

The accompanying notes are an integral part of the financial statements.

THE CENTRAL EUROPE AND RUSSIA FUND, INC.
SCHEDULE OF INVESTMENTS APRIL 30, 2006 (unaudited) (continued)

Shares	Description	Value
INVESTMENTS IN HUNGARIAN COMMON STOCKS 5.7%		
	COMMERCIAL BANKS 2.3%	
437,400	OTP Bank	$ 16,941,328
25,000	OTP Bank (GDR)	1,902,500
		18,843,828
	OIL, GAS & CONSUMABLE FUELS 2.5%	
110,000	Mol Magyar Olaj-Es Gazipari	13,070,817
61,000	Mol Magyar Olaj-Es Gazipari (GDR)	7,167,500
		20,238,317
	PHARMACEUTICALS .9%	
30,000	Gedeon Richter	6,455,315
4,300	Gedeon Richter (GDR)	918,050
		7,373,365
	Total Investments in Hungarian Common Stocks (cost $12,385,403)	46,455,510
INVESTMENTS IN CZECH REPUBLIC COMMON STOCKS 3.9%		
	COMMERCIAL BANKS 0.7%	
4,500	Komercni Banka	709,038
89,996	Komercni Banka (GDR)	4,724,790
		5,433,828
	MULTI-UTILITIES 3.2%	
750,000	Ceske Energeticke Zavody	25,775,648
	Total Investments in Czech Republic Common Stocks (cost $3,984,713)	31,209,476
INVESTMENTS IN TURKISH COMMON STOCKS 13.5%		
	AUTOMOBILES 0.6%	
1,500,000	Tofas Turk Oromobil Fabrika	