

GAIDAR INSTITUTE FOR ECONOMIC POLICY

**RUSSIAN ECONOMY IN 2010
TRENDS AND OUTLOOKS
(ISSUE 32)**

**Gaidar Institute
Publishers
Moscow
2011**

UDC 338.1(470+571)
BB 65.9(2Poc)-04
C

Agency CIP RSL

Editorial Board:

*S. Sinelnikov-Murylev (editor-in-chief),
A. Radygin,
N. Glavatskaya*

Russian Economy in 2010. Trends and Outlooks.
R95 (Issue 32) – Moscow. 2011. Gaidar Institute Publishers, 544 pp.

ISBN 978-5-93255-316-9

The review provides a detailed analysis of main trends in Russia's economy in 2010. The paper contains 6 big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit spheres; financial sphere; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts

This publication is made possible by the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the Gaidar Institute for Economic Policy and do not necessarily reflect the views of USAID or the United States Government.

**UDC 338.1(470+571)
BBC 65.9(2Poc)-04**

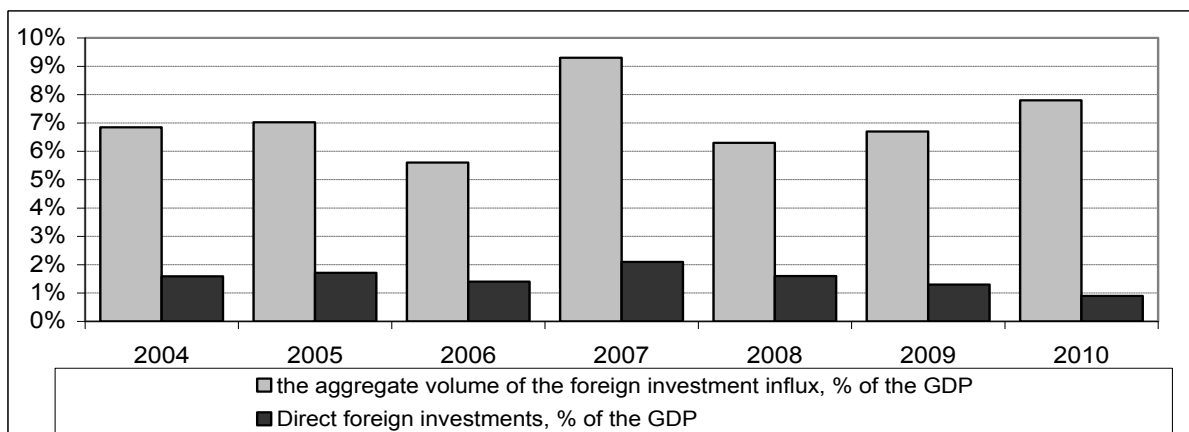
ISBN 978-5-93255-316-9
2011

© Gaidar Institute,

Russia’s Foreign Investments in 2010

Most of the year 2010 is characterized by a drop in foreign investors’ activities in the Russian Federation. In the investment sphere, crisis phenomena which were explicitly evident in 2009 kept prevailing in January-September 2010, while the influx of foreign investments in Russia decreased dramatically. In January-September 2010, the volume of foreign investments in the Russian economy fell by 13.2% as compared to that in the same period of 2009 and, by 46.0% as against the maximum level registered in January-September 2007. Due to substantial growth in foreign investments in the 4th quarter (a 150% increase as compared to the 4th quarter of 2009), the aggregate growth of 40.1% in foreign investments in the Russian economy as against the 2009 figure was registered (*Fig. 25*). At the same time, the outflow of the earlier invested capital continued. If in the 1st quarter of 2010 and the 4th quarter of 2010 the volume of the withdrawn funds (foreign investors’ income which was transferred abroad as well as interest payments on loans and loan repayments) was equal to the volume of foreign investments into the country in the same period, in the 2nd quarter of 2010 and the 3rd quarter of 2010 it exceeded the latter by 12.1% and 22.7%, respectively. Furthermore, in 2010 Russian investments abroad exceeded the volume of foreign investments into the Russian economy. Such trends were typical of the first half of 2010 where such an excess in the 1st quarter of 2010 and the 2nd quarter of 2010 amounted to 72.6% and 64.9%, respectively. In the 3rd quarter of 2010 and in the 4th quarter of 2010, Russian investments abroad amounted to 28.0% and 60.0% of the volume of foreign investments in Russia in the same periods, respectively. It remains to be seen if the above factor is the trend’s turning point.

Fig. 25. The level of the influx of foreign investments into the Russian economy in the 2004–2010 period (% of the GDP)



The source: Rosstat.

In 2010, international rating agencies left Russia's sovereign rating unchanged at the level below the pre-crisis one. At the same time, in December 2009 having registered some improvements in the Russian economy S&P, an international rating agency, raised Russia's rating forecast from the negative one to the stable one and preserved the rating at the "BBB" investment level. In September 2010, having confirmed the current rating level the Fitch Agency upgraded the rating forecast to the positive one. According to Fitch, "the Russian economy is recovering after being seriously affected by the global financial crisis. Such a change of the forecast to the positive one reflects Fitch confidence that a switchover to a more flexible foreign exchange policy, substantial repayment of the foreign debt of the private sector, stabilization of the banking sector and growth in foreign exchange reserves should contribute to a decrease in the number of factors behind the country's financial vulnerability".

According to Moody's, another rating agency the Russia's rating remains at the level of "Baa1", while the rating forecast is "stable" (in the 2008–2009 period, unlike S&P and Fitch Moody's did not downgrade Russia's rating, but cut only the rating forecast).

In 2010, foreign investments amounted to 140.1% and 105.8% as against the 2009 figure and the 2008 figure, respectively or USD 114.7 billion. (Table. 20).

In 2010, the largest growth in absolute indices (by USD 34.7 billion) was registered with the segment of other investments which were made on a return basis. Direct investments decreased by USD 2.1 billion. Such a drop took place due to a decrease in values of the following two components: contributions to the charter capital and loans from foreign co-owners of business entities. In 2010, the former fell by 3.7% to USD 7.7 billion, while the latter, by 28.4% to USD 4.6 billion. Thus, the unit weight of loans received from foreign co-owners in the structure of direct investments in the Russian Federation decreased from 40.5% in 2009 to 33.4% in 2010, while the share of contributions to the charter capital grew from 50.3% to 55.8%.

Table 20

The volume and structure of foreign investments in the non-financial sector of the Russian economy¹

	In million USD.				% of the previous year			
	Total	Direct	Portfolio	Other	Total	Direct	Portfolio	Other
2006	55 109	13 678	3 182	38 249	102.7	104.6	700.0	95.3
2007	120 941	27 797	4 194	88 950	219.5	203.2	131.8	232.6
2008	103 769	27 027	1 415	75 327	85.8	97.2	33.7	84.7
2009	81 927	15 906	882	65 139	79.0	58.9	62.3	86.5
2010	114 746	13 810	1 076	99 860	140.1	86.8	121.9	153.3

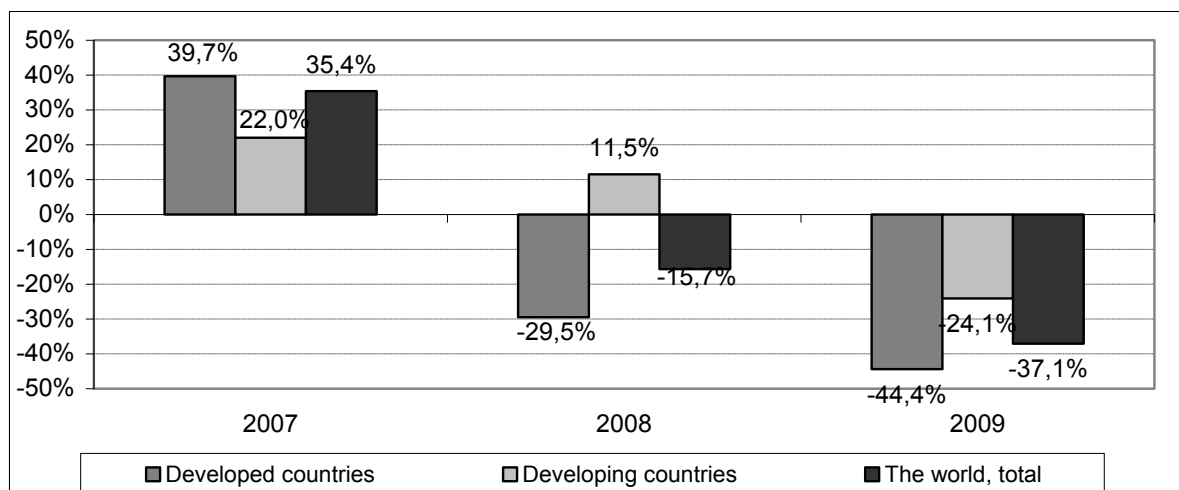
The source: Rosstat.

According to the UNCTAD World Investment Report 2010 which was published in July 2010, as regards the volume of direct foreign investments in 2009 Russia is rated 6th in the world (it was rated 5th in 2008, 9th in 2007, 10th in 2006 and 15th in 2005). As in the previous year, among the developing countries Russia is rated 2nd after China. According to the above

¹ Direct investments are investments in tangible assets and acquisition of a controlling interest or an interest which gives the investor the right to participate in management, while portfolio investments are investments in securities in order to receive income only; other investments are investments which are made on a return basis (loans of international financial institutions, trade loans and other).

report, in 2009 Russia accounted for 3.5% of the global foreign investments (4.1% in 2008) and, for 8.2% of the direct foreign investments in developing countries (11.9% in 2008).

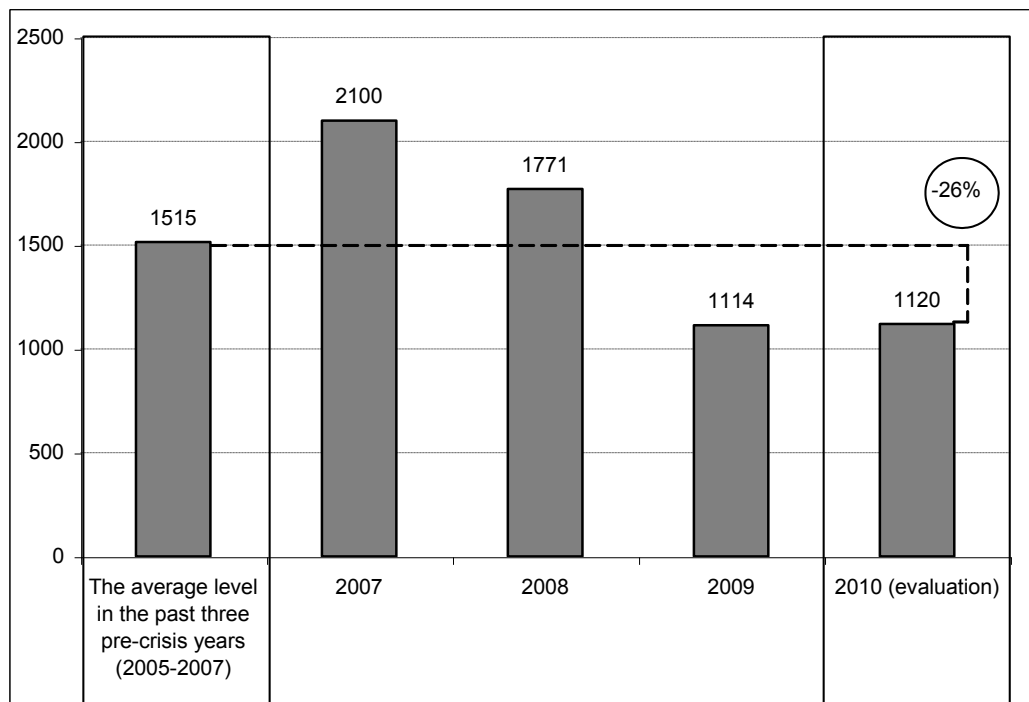
Fig. 26. Changes in the influx of direct foreign investments in the 2007–2009 period.



The source: UNCTAD World Investment Report 2010, July 22, 2010

According to UNCTAD report, decrease in the aggregate volume of the global direct foreign investments was registered from 2008 (Fig. 26). According to preliminary estimates, in 2010 the aggregate volume of the direct foreign investments is virtually at the 2009 level, while in 2011 and 2012 it is expected to amount to USD 1.3–1.5 trillion and USD 1.6–2 trillion, respectively. (Fig. 27).

Fig. 27. The global influx of direct foreign investments, billion USD.



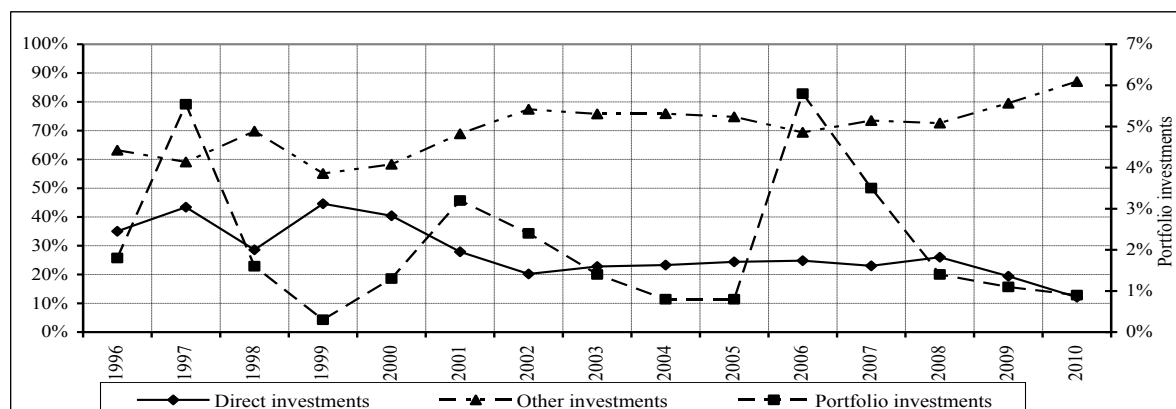
The source: UNCTAD Global Investment Trends Monitor, October 14, 2010.

As regards the segment of portfolio investments into the Russian economy in 2010, a 21.9% growth was registered as compared to that in 2009. At the same time, a decrease in the unit weight of investments in equities and shares from 42.9% in 2009 to 32.0% (against 95.5% of the volume of portfolio investments in 2007 and 79.6% in 2008) was observed.

In 2010, other investments grew by 53.3% as compared to the 2009 figure. The share of trade loans in the structure of other investments went down from 21.4% in 2009 to 17.6% in 2010 (against 21.5% in 2008). As regards the periods the investments were attracted for, the share of loans with a term of over six months fell to 38.0% as compared to 67.9% in 2009 (68.1% in 2008). The unit weight of loans with a term of less than six months increased up to 41.3% (against 10.1% in 2009 and 8.8% in 2008).

So, as compared to 2009 the structure of foreign investments into the Russian economy did not change much in 2010 (Fig. 28).

Fig. 28. The structure of foreign investments in the Russian economy in the 1996–2010 period



The source: Rosstat.

In 2010, priorities of foreign investors by the type of business changed dramatically; a concentration of foreign investments in industry and the financial sector was registered. In 2010, foreign investments in industry and the financial sector increased by 44.2% and 1,330%, respectively, as compared to 2009.

In 2010, investors took less interest in trade, transport and communications. In 2010, foreign investments in trade decreased by 41.2%, while those in transport and communications, by 52.4%.

Breakdown of foreign investments into the Russian economy by the type of business is shown in *Table 21*.

Table 21

**Breakdown of foreign investments into the Russian economy
by the type of business in the 2008–2010 period**

	In million USD			Change, % of the previous year			% of the total		
	2008	2009	2010	2008	2009	2010	2008	2009	2010
Industry	49 704	32 980	47 558	99.1	66.4	144.2	47.9	40.3	41.4
Transport and communications	4 861	13 749	6 576	72.5	282.8	47.8	4.7	16.8	5.7
Wholesale and retail trade; repair of motor vehicles, motor bikes, household appliances and personal items	23 905	22 792	13 334	50.5	95.3	58.5	23.0	27.8	11.6
Transactions with real property, rental and other services	15 378	7 937	7 341	182.8	51.6	92.5	14.8	9.7	6.4
Financial business	4 977	2 658	37 913	111.8	53.4	1426.3	4.8	3.2	33.0
Other industries	4 944	1 811	2 024	126.7	36.6	111.8	4.8	2.2	1.8

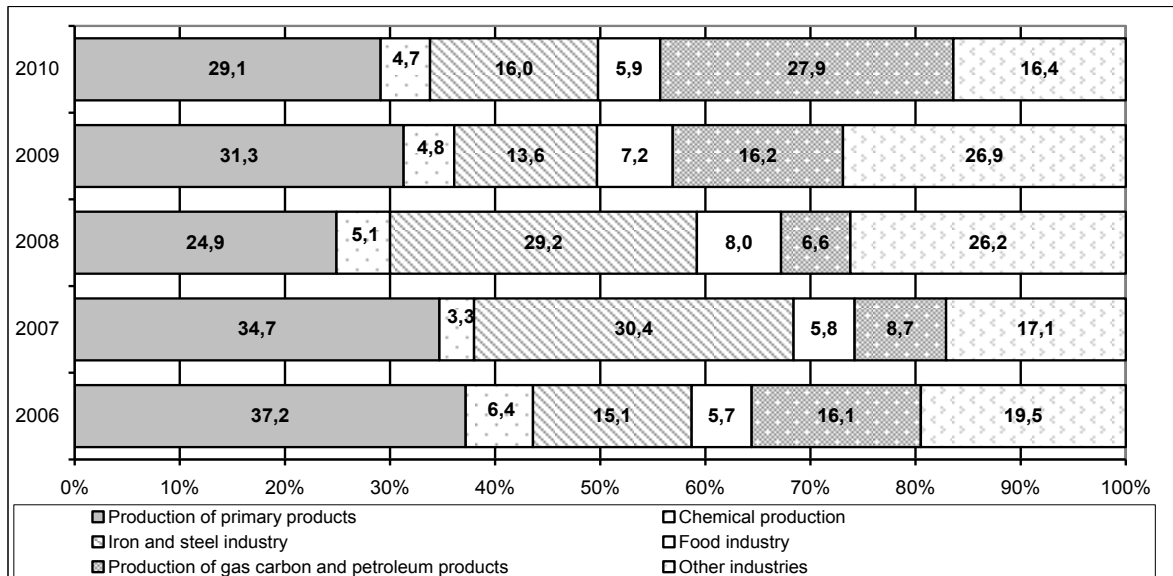
The source: Rosstat.

In 2010, in the structure of foreign investments in industry leaders of growth are manufacturing industries; as compared to 2009 investments in them grew by 49.2% (in 2009 a decrease amounted to 34.5%) (*Fig. 29*). Foreign investments in production of fuel and energy mineral resources increased by 43.2% (in 2009 a drop amounted to 16.0%).

In manufacturing industry, investments in production of gas carbon and petroleum products increased by 150%, while those in iron and steel industry, by 69.7%, thus amounting to USD 13.2 billion and USD 7.6 billion, respectively (in 2009 the growth in investments into production of gas carbon and petroleum products amounted to 63.7%, while investments in iron and steel industry fell by 68.8%). In 2010, foreign investments in chemical production increased by

41.3% to USD 2.2 billion as compared to 2009 (in 2009 a 37.6% drop in investments in that industry was registered).

Fig. 29. The breakdown of foreign investments in industry in the 2006–2010 period, %



The source: Rosstat.

In 2010, both direct investments and portfolio investments in industry decreased by 7.9% and 41.6%, respectively, as compared to 2009 (in 2009 they fell by 44.1% and 41.2%, respectively). As compared to 2009, other investments in industry grew by 62.0% (in 2009 a drop of 29.5% was registered). Thus, the unit weight of all other investments in industry grew from 75.6% in 2009 to 84.9% in 2010, while in the same period the share of the direct investments and that of portfolio investments fell from 22.4% and 2.0% to 14.3% and 0.8%, respectively.

Changes in the structure of foreign investments by the type of economic activities in industry were registered. In production of primary products, direct investments kept falling and decreased by 35.9% to USD 2.0 billion. As a result, in 2010 the share of such investments in the aggregate investments in that industry fell to 14.7% (against 30.7% in 2009 and 40.2% in 2008). The share of other investments in production of primary products (in 2010 other investments grew by 70% to USD 11.8 billion) increased up to 85.0% (against 65.8% in 2009 and 59.0% in 2008).

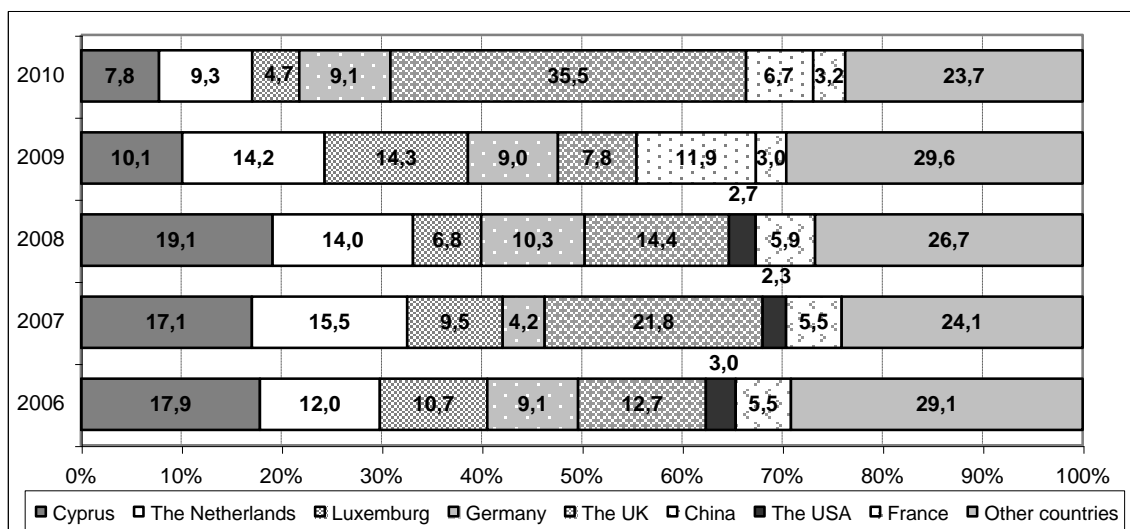
In 2010, in manufacturing industry other investments accounted for a larger part of investments, too. As compared to 2009, such investments increased by 60% and amounted to 85.4% of all the investments in manufacturing industry in 2010 (against 80.6% in 2009). In 2010, direct foreign investments in manufacturing industry increased by 13.3%, while the unit weight of direct investments in manufacturing industry fell to 14.0% (against 18.5% in 2009).

As regards the geographic structure of foreign investments into the Russian economy in 2010, changes have taken place in the list of states which are the main exporters of the capital to the Russian Federation. In 2010, the largest volume of investments, that is, USD 40.8 billion

(35.5% of the total volume of foreign investments into the Russian economy in the above period) was received from Britain and USD 10.7 billion worth of investments, from the Netherlands. In 2010, the top three leaders as regards investments in the Russian Federation included Germany as well, which country invested USD 10.4 billion in to the Russian economy.

In 2010, investments from Britain showed the highest growth of 530% as compared to that in 2009, while investments from Ireland increased by 240%. Investments from Germany and France rose by 41.7% and 48.6%, respectively. However, investments from Luxemburg, China, Japan and the Netherlands decreased by 54.2%, 21.8%, 63.3% and 8.1%, respectively. Differences in the dynamics of investments have resulted in changes in the geographic structure of foreign investments into the Russian economy (*Fig. 30*).

Fig. 30. The geographic structure of foreign investments into the Russian Economy in the 2006–2010 period, %



The Source: Rosstat. The data on investments from the USA in the 2009–2010 period and those from China in the 2006–2008 period is unavailable.

As of the end of December 2010, the accumulated foreign capital (without monetary regulation authorities, commercial banks and savings banks taken into account) including RUR investments calculated into US dollars amounted to USD 300.1 billion, which figure is 11.9% higher than the respective value as of the beginning of the year. From the beginning of the year, direct accumulated investments grew by 6.6% (*Table 22*).

In 2010, Cyprus, the Netherlands, Luxemburg, China and Germany account for a larger portion of the total volume of the accumulated foreign investments. The total share of the above countries amounted to 64.4% (against 66.3% in 2009). At the same time, the share of the above five leaders in the segment of other investments increased to 64.8% (against 62.9% in 2009), while in the segments of direct investments and the portfolio investments it is estimated to amount to 67.1% and 21.9%, respectively (against 69.0% and 85.1% in 2009).

Table 22

The accumulated foreign investments by the investor-country

	Accumulated as of January 1, 2011, million USD.			
	Total	Direct investments	Portfolio investments	Other investments
Ireland	11 488	568	4	10 916
Germany	27 825	9 254	11	18 560
Japan	9 022	824	2	8 196
Britain	21 578	3 501	4 481	13 596
Cyprus	61 961	44 737	1 732	15 492
The Netherlands	40 383	22 401	8	17 974
Luxemburg	35 167	661	203	34 303
China	27 940	942	0.1	26 998
Other countries	64 742	33 311	2 479	28 952
Total	300 106	116 199	8 920	174 987

The source: Rosstat

Other investments prevail in the structure of foreign investments accumulated as of the end of December 2010. They accounted for 58.3%. A similar index as regards direct foreign investments amounted to 38.7%.

Considering the above, it may be concluded that the situation with investments in Russia started to improve by the end of 2010. Discernable growth in the volume of the accumulated foreign capital was registered. At the same time, a drop in the influx of the direct foreign investments in the Russian economy is a negative factor. Growth in foreign investments took place due to the segment of other investments which are made on a return basis. Thanks to lower interest rates and capital injection in the economy of countries which are the main investors in the Russian Federation, foreign businessmen took greater interest in the financial business in Russia.

In 2010, growth in profits of corporations was observed which factor according to UNCTAD “along with improvements of the situation on the stock markets will create a basis for financing direct foreign investments”. Interest of global investors in developing countries is constantly growing. “In particular, Brazil, the Russian Federation, India and China (BRIC countries) have good prospects of attracting direct foreign investments. In developing countries and countries with transition economy, apart from the most labor-intensive segments of the chain of creation of value, foreign investments will also be made far and wide into activities with a greater technological component”¹. Thus, with taking into account the registered growth in the foreign investments in the 4th quarter of 2010 a renewal of investments flows to the Russian economy may be expected in 2011.

Taking into account a considerable growth in prices on energy carriers late in 2009 and early in 2011, a substantial volume of investments into the fuel and energy complex can be expected. In addition to the above, both the ongoing liberalization of the legislation regulating foreign investments and measures aimed at making long-term projects more attractive may motivate foreign investors to make investments in other sectors of the Russian economy as well.

¹ UNCTAD World Investment Report 2010.