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The review provides a detailed analysis of main trends in Russia's economy in 2013. 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.

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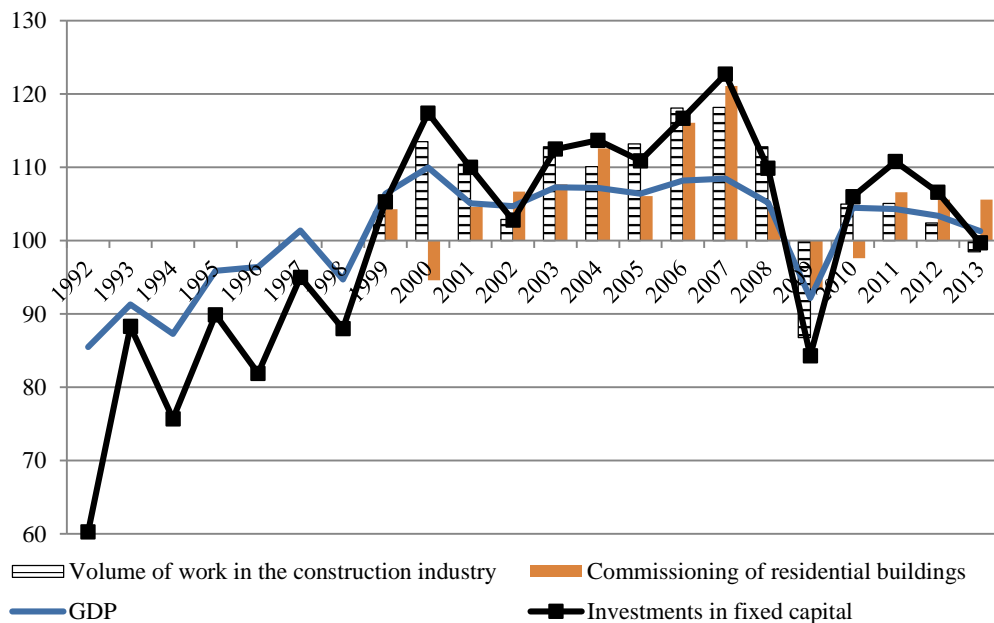
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Russia's Domestic Investments in Fixed Assets in 2013

Conditions and factors activities investment activities in 2009-2013

Transformational changes that have been taking place in the Russian economy over the past 15 years have had a substantial impact on the structural characteristics of the investment process. Comparative analysis of economic development between in 1999 and 2013 allows the identification of common and specific conditions, factors and risks, depending on the investment potential, demand for investment resources and the motivation for investment activities. In 2013, Russia's GDP increased 1.87 times, and investments in fixed capital by 2.89 times compared with 1999. The dynamics of the investment activities during the period under study were not uniform and were determined by the influence of changes in world market conditions, on the one hand, and the level of activity of Russian enterprises in the internal market, on the other (Fig. 27).



Source: Federal State Statistics Service (Rosstat).

Fig. 27. Dynamics of investments in fixed capital in 1992-2013, as % of the previous year,

When the level of potential investment demand in the domestic market was high, stabilisation of the share in the GDP of expenditure for investment purposes reflected the lack of mechanisms to transform savings into investments, which ultimately resulted in restraining of economic development. Development based on extensive use of primary factors, systematic growth of production costs and a high proportion of imports in domestic market resources led to low competitiveness of the Russian economy.

Under the influence of a sharp decline in income from foreign trade the share of gross saving in GDP in 2013 fell to 24.6% and exceeded the 1998 figure, which had been the minimum for the whole 20-year observation period, by less than 1%. It should be noted that, in the period from 2009 to 2013, despite the sharp decline in income, the anti-crisis measures taken helped to keep the share of investment in fixed capital at an average level of 19.9% of GDP. This was achieved by increasing the average ratio of transforming savings into investments to 73.7% during 2009-2013, in comparison with 53.8% for the previous 8 years. However, due to the undeveloped financial market, inter-industry floating of income and savings was not provided, in particular, between those of exporters, and the sectors serving domestic demand. The savings rate significantly exceeded the accumulation rate and the share of investments in fixed capital in GDP, with the Russian economy acting only as a net lender.

Table 9

Capital transactions account, based on current prices, RUR bn

	2008	2009	2010	2011	2012	2013*
Gross savings — total	12,459.5	7,810.7	12,201.64	16,495.63	17,729.92	18,661.5
Gross accumulation of fixed capital	9,200.8	8,535.7	10,014.4	11,950.5	13,603.7	14,316.4
Changes in inventories	1,325.3	-1,190.9	458.3	2,032.2	1,626.4	1,168
Net lending (+), net borrowing (-)	1,933.4	465.9	1,728.936	2,512.927	2,499.816	3,177.1
For reference: investment in fixed capital	8,781.6	7,976.0	9,152.1	10,776.8	12,568.8	13,255.5

*) preliminary data,

Source: Federal State Statistics Service (Rosstat).

The phenomenon of the Russian economy is that the growth of export earnings and a relative increase in the lending and investment attractiveness of the country has increased the transformation of capital into reserves. In 2004, in order to reduce the risks of adverse international economic conditions, and as an instrument to sterilise excess money supply in circulation, the Stabilization Fund had begun to form, and in 2008 it was transformed into the Reserve Fund and the National Welfare Fund (*Table 10*)

Table 10

Monetary values of the Reserve Fund and the National Welfare Fund in 2008-2013, (end of year)

	Reserve Fund	National Welfare Fund	Reserve Fund	National Welfare Fund
	RUR bn		as % of GDP	
2008	4,027.64	2,584.49	9.8	6.3
2009	1,830.51	2,769.02	4.7	7.1
2010	755.21	2,695.52	1.7	5.8
2011	811.52	2,794.43	1.5	5.0
2012	1,885.68	2,690.63	4.0	4.0
2013	2,859.72	2,900.64	4.3	4.3

Source: Federal State Statistics Service (Rosstat).

Due to the fact that just before the crisis, the aggregate volume of the Reserve Fund and National Welfare Fund had reached 16.1% of GDP, the implementation of an anti-crisis programme in 2009-2010 became possible. Not only did the accumulated volume of funds contribute to reduction of the negative effects of the crisis in the financial and real sectors of the economy, but it also ensured the implementation of state social obligations and stimulated growth of the economy and investment activities. In 2013 active discussions around the problem of the use of the National Welfare Fund to finance major infrastructure investment projects began.

The dynamics of GDP in the short term are more closely associated with such growth factors as inflation, surplus (deficit) of the state budget, the quality of the institutional environment and the restructuring of enterprises and companies in order to reduce costs, excessive labour forces and energy consumption as well as to close down inefficient industries.

In the context of the medium- and long-term development of the Russian Federation the role of investment activities increased dramatically in response to the need to address the problem of deep structural and reproduction imbalances, high energy production, inefficient location of enterprises, insufficient use of material and labour resources and a high proportion of non-competitive goods. At the corporate level, the need for solid investments is associated with a transition to strategic development, including the transition to new products, markets, management techniques and new patterns of corporate control.

Main trends in the financing of investment activities in 2009-2013

The principal aspect of economic development in the period 2009-2012 was the shift toward the increased funding of investments in fixed capital from the own funds of enterprises and organisations, whilst reducing the participation of borrowed funds. The proportion of these own funds in the financing of investments in fixed capital rose to 46.1% in 2013, as compared to 41.0% in 2010. The structure of use of equity funds of enterprises in investment activities closely corresponded with their financial condition. In 2013, the proportion of gross profits in GDP dropped to 28.8% in comparison with 29.6% in 2012, and 32.6% in 2010. The net financial results of enterprises and organisations in 2013 amounted to 87.2% of the same indicator in 2012, while the proportion of profitable enterprises declined by almost 1% compared to the previous year. Furthermore, in 2013, in line with the trend for a reduction in the rate of return existing over the previous decade, the share of profit in investment resources decreased, giving way to other sources.

Table 11

Monetary and financial resources of investment activities in 2008-2012

	2008	2009	2010	2011	2012	2013
Income of consolidated budget, RUR bn	16,003.9	13,599.7	16,031.9	20,853.7	23,435.1	24,082.4
Gross profit in the economy, including gross mixed income, RUR bn	13,498.7	11,921.1	15,093.7	17,172.5	18,255.3	19,142.1
Net financial result, RUR bn	3,801.2	4,431.6	6,330.6	7,252.7	7,716.5	6,650.5
Share of profit-making organisations, in %	71.7	68.0	70.1	71.9	74.1	73.2
Increase in financial assets of the population and real estate acquisition, RUR bn	2323	4,923	6,719	5,785	5,852	6,250.6*
Average per capita income (per month), RUR	14,940.6	16,838.3	18,958	20,780	22,880	25,522
Loans, deposits and other invested assets, provided by organisations, individuals and credit institutions, RUR bn	19,362.5	19,179.6	21,537.3	27,911.6	32,886.9	38,767.9

*) preliminary estimates.

Source: Federal State Statistics Service (Rosstat).

The main reduction of investments in respect of sources of funding was due to the sharp decline in finance for investment provided by parent entities – large holding companies, joint stock companies and financial-industrial groups with state participation. The proportion of investments of such controlling entities in the structure of funding sources had fallen to 12.6% in 2013, compared to 16.8% in 2012 and 19.0% in 2011.

Table 12

**Structure of investments in fixed assets by sources of funding
(excluding small businesses and investments,
which cannot be observed by statistical methods), % of total for 2007-2013**

	2007	2008	2009	2010	2011	2012	2013
1	2	3	4	5	6	7	8
Investments in fixed capital — total	100	100	100	100	100	100	100
including by sources of financing:							

Cont'd

1	2	3	4	5	6	7	8
own funds	40.4	39.5	37.1	41.0	41.9	44.5	46.1
borrowed funds	59.6	60.5	62.9	59.0	58.1	54.6	53.9
of which:							
bank loans	10.4	11.8	10.3	9.0	8.6	8.4	9.3
including loans from foreign banks	1.7	3.0	3.2	2.3	1.8	1.2	0.9
borrowings from other organisations	7.1	6.2	7.4	6.1	5.8	6.1	6.2
budgetary funds	21.5	20.9	21.9	19.5	19.2	17.9	18.8
including:							
federal budgetary funds	8.3	8.0	11.5	10.0	10.1	9.7	9.8
budgetary funds of constituent entities of the Russian Federation	11.7	11.3	9.2	8.2	7.9	7.1	7.7
non-budgetary funds	0.4	0.3	0.3	0.3	0.2	0.4	0.3
funds raised in connection with participation interest in construction (organisations and individuals)	3.7	3.5	2.6	2.2	2.0	2.7	3.0
including: population funds	1.5	1.9	1.3	1.2	1.3	1.3	2.3
other	16.4	17.7	20.4	21.9	22.3	20.0	16.3
including:							
funds of controlling entities	11.3	13.8	15.9	18.0	19.0	16.8	12.6
funds from the issue of corporate bonds	0.1	0.1	0.1	0.01	0.01	0.04	0.1
funds from issue of shares	1.8	0.8	1.0	1.4	1.0	1.0	1.0
Out of the total volume of fixed capital investment from abroad	5.4	4.3	4.3	3.8	3.1	3.0	2.2

Source: Federal State Statistics Service (Rosstat).

The change in volume and proportion of borrowed funds in these sources was accompanied by a change in their structure. The proportion of budgetary sources for financing investments in fixed capital in 2010-2013 was generally at a level of 18.9% and remained below pre-crisis levels, however, the proportions of funds used, according to budget system levels, did change (Table 13). The implementation of the programme of anti-crisis measures in 2009-2010 was accompanied by an increase in the financing of investment activities from the federal budget, and this compensated for the reduction of expenditure on investment objectives of subjects of the Russian Federation. State investments from the federal budget were implemented through the Investment Fund, the Federal Targeted Investment Programme (FTIP) and Federal Target Programme (FTP). Over the next three years state participation in financing investment activities was decreasing. In 2013, the share of budgetary funds to finance investments in fixed capital amounted to 2.68% of GDP, including, by means of the federal budget: 1.40% of GDP. In 2013, we noted a decline in spending on the Federal Targeted Investment Programme to 1.06% of GDP in comparison with an average over the previous two years of 1.43%. In absolute terms, the budgetary funds provided in 2013 to finance investments in fixed capital increased by RUR 86.0bn compared with the previous year, and amounted to RUR 1,790.1bn. It should be noted that, unlike 2010-2012, the greatest growth, RUR 62bn, was associated with increased investments of subjects of the Russian Federation in the budget investment programmes.

Table 13

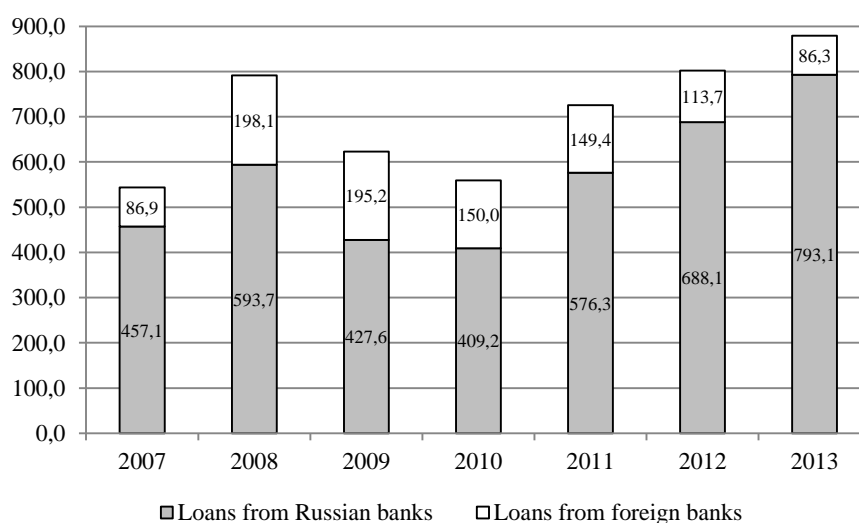
The share of expenditure on fixed assets investments in 2007-2013, % of GDP

	2007	2008	2009	2010	2011	2012	2013
Budgetary funds — total	3.37	3.40	3.41	2.80	2.91	2.76	2.68
including:							
from federal budget	1.30	1.30	1.78	1.43	1.54	1.49	1.40
from budgets of the constituent entities of the Russian Federation	1.84	1.84	1.42	1.17	1.20	1.09	1.10
Federal Targeted Investment Programme — total	1.41	1.02	1.28	1.23	1.40	1.45	1.06

including:							
programme part	0.88	0.70	0.77	0.71	0.93	0.97	0.76
non-programme part	0.32	0.38	0.53	0.31	0.51	0.48	0.30

Source: Federal State Statistics Service (Rosstat); <http://faip.economy.gov.ru> .

The general trend is towards a greater participation of the banking sector in financing investment activities during the post-crisis period, but the figure for this is still below the pre-crisis level of 2007-2008. (Table 12). In 2013, the share of bank loans in the structure of funding sources was 9.3% having increased by 0.9% compared with the previous year. Changes in the structure of bank lending in the last three years are defined by the increasing volume and share of loans from Russian banks, which replaced loans from foreign banks. Compared to 2012, the loans from Russian banks increased by RUR 105.0bn, whilst loans from foreign banks decreased by RUR 27.4bn. (Fig. 28).



Source: Federal State Statistics Service.

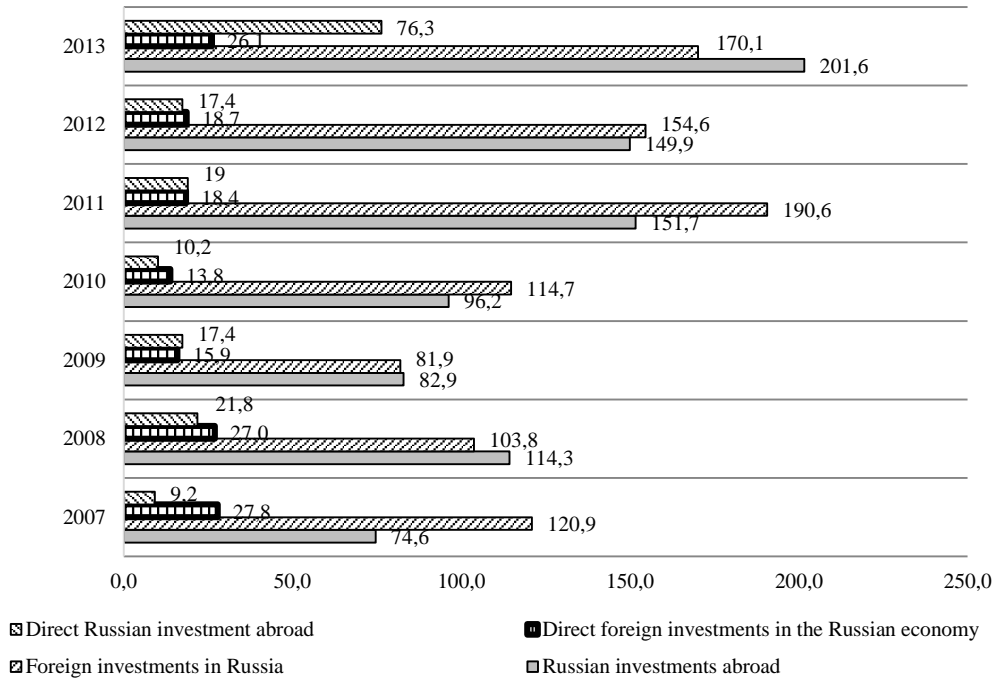
Fig. 28. Bank loans to finance investments in fixed capital in 2007-2013, Rb bn

The crisis of 2008 was characterised by even more rapidly falling rates of foreign investments into the Russian economy compared with the dynamics of domestic investment activities. The decline in foreign loans, while reducing the extent of foreign direct investments, has led to a steady fall in the share of total investments coming from abroad and in the structure of investments in fixed capital to its lowest level for the last 13 years – 2.2% in 2013, even though the volume of direct foreign investments into the Russian economy in 2013 had risen by nearly 40% over the previous year. The change in dynamics of the investment activities of Russian and foreign capital in Russia took place against a background of a sharp increase in net capital outflow. In 2011, the volume of capital exports reached \$81.4bn, which roughly corresponded to the sum of the previous two years. In 2012-2013 net capital outflow was in the range of \$54.6-60bn per year.

In 2013, the total volume of Russian investments abroad exceeded the volume of foreign investments in Russia by \$31.5bn (Fig. 29).

When analysing the sources of financing for investments in fixed assets, it should be noted that, in 2009, there was a turning point in the trend for residential construction. In 2010, after a steady increase in housing construction between 2001 and 2008, the commissioning of residential buildings decreased by 8.9%, moreover, the commissioning of residential buildings paid for by the public and with borrowed funds decreased by 6.9% compared with the pre-crisis

level of 2008. The situation changed in the third quarter of 2011, when the commissioning of residential buildings increased. As a result, by the end of 2011 the growth in terms of commissioning of residential buildings was 6.6%, for 2012 and in 2013 was 5.6% in comparison with the previous year. The proportion of individual house construction to overall residential construction in 2013 reached 43.8%, exceeding the pre-crisis level of 2008 by 1.1%.

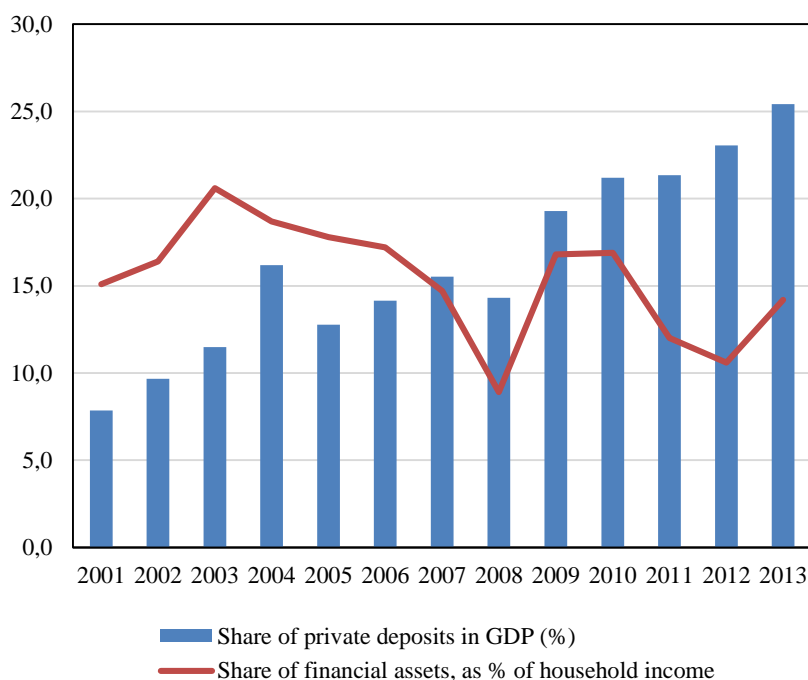


Source: Federal State Statistics Service (Rosstat).

Fig. 29. Volumes of Russian investments abroad and foreign investment into the Russian economy in 2007-2013, in \$ bn

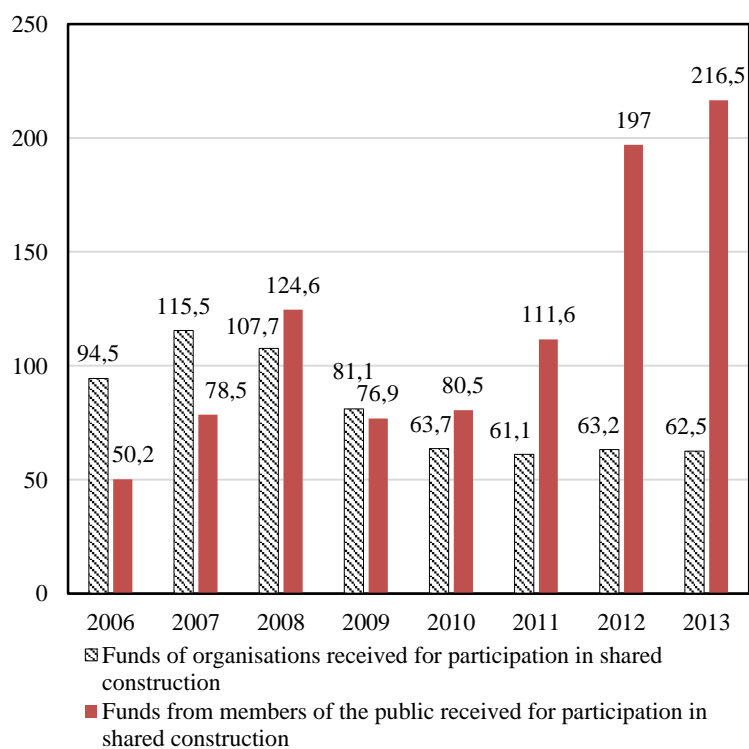
When analysing the dynamics and structure of sources of funding for investment, it is necessary to assess the investment potential of the population. As a result of the population's income growth over the past 10 years, both the volume of investments (deposits) from individuals in financial and credit organisations increased as did the volumes and share of financial asset in the growth of total income. It should be noted, however, that the growth of household savings and the increase in the proportion of savings in income was accompanied by the growth of organised forms of savings, and led to greater participation of households in the formation of investment resources. In 2008, the potential investment resources of households accounted for 14.3%, while in 2012 it was 23.1%, and in 2013, 25.4% of GDP (Fig. 30).

The investment activity of the population in 2010-2013 was supported by a growth in demand for loans at lower interest rates. Funds from the public received for use in shared construction have steadily increased over the last three years, and have compensated for the weakening investment activities of organisations (Fig. 30). The public remains active in the real estate market. The share of expenditures on the acquisition of real estate in 2013 amounted to 4.4% of household income, while the total amount of funds used to purchase real estate increased by 1.54 times in comparison with 2008.



Source: Federal State Statistics Service (Rosstat).

Fig. 30. Private investments (deposits) in financial and credit organisations and financial assets of the population in the period 2001-2013



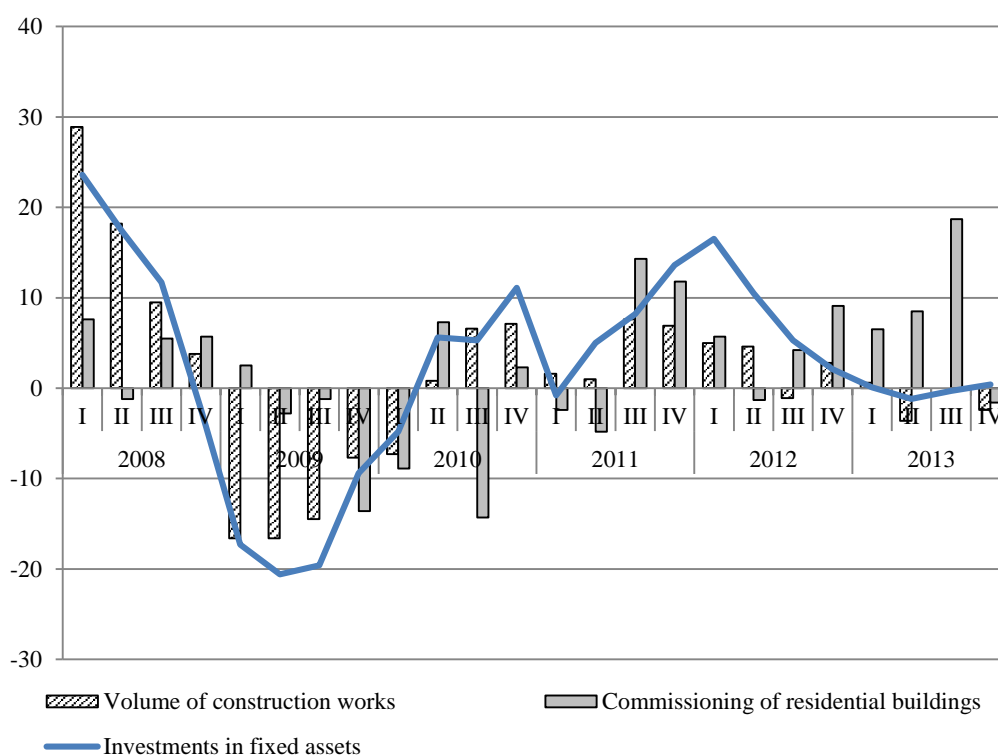
Source: Federal State Statistics Service (Rosstat).

Fig. 31. Funds received for participation in shared construction in 2006-2013, Rb bn

Investments in fixed capital by types of fixed asset and economic activity

The crisis of 2008-2009 radically changed the situation in the investment sphere. In 2009, there was a decrease in the rate of actual volume of investments in fixed assets by 15.7%, which significantly exceeded the decrease in output in basic economic activities (by 9.8%) compared with the previous year. The peak of the investment crisis passed in the first half of 2009, and, since the third quarter, there was a tendency towards a weakening of the decline of investments in fixed assets. However, by 2012, investments in fixed assets exceeded that of 2008 (by 3.2%). The dynamics of business activity in 2012 were extremely diverse, and after the investment growth in the first half of the year, its pace in the third and fourth quarters sharply decreased (Fig. 32).

In 2013, the downward trend of investments in fixed assets was quite predictable and was determined by the extremely low level of business activity in the second half of 2012. The stabilisation of investments in fixed capital in the first quarter of 2013, at the level of the previous year, gave way to a decline by 1.2% in the second quarter and by 0.3% in the third quarter (in comparison to the corresponding quarters of 2012). At the end of 2013, investments in fixed assets were at 99.8%, and the volume of works in the construction industry at 98.5% of those of the previous year.



Source: Federal State Statistics Service (Rosstat).

Fig. 32. Dynamics of investments in fixed assets in 2008-2013, as % of the corresponding quarter of the previous year

The dynamics of investment into fixed capital varies between large and small enterprises. While the total volume of investments in fixed assets in 2013 was reduced by 0.2 % in comparison with the previous year, the investment in fixed capital by the large and medium-sized enterprise sectors decreased by 5.6% (Table 14).

Table 14

**Growth in the volume of investments in fixed capital
in 2009-2013, as % of the previous year**

	2009	2010	2011	2012	2013
Investments in fixed capital (for the full range of organisations, including adjustments for investments not observable by direct statistical methods)	84.3	106.0	108.3	106.6	99.8
Large and medium-sized organisations (investments in fixed assets, not including small businesses and investments, not observable by direct statistical methods)	82.56.7	105.1	110.4	100.7	94.4

Source: Federal State Statistics Service (Rosstat).

In 2013, the changes in the structure of investments in fixed assets, by type of economic activity, were determined by the sharp decline in construction and investment activity in the production and transportation sectors, the combined share of which accounted for nearly 70% of investments in the economy. Investments in transportation made up 88.5% of that in 2012, due, on one hand, to the completion of major investment projects in pipeline transport, and, on the other, to a reduction of investment in railway transport with the reduction in volume of freight turnover, and reduced financial performance.

Table 15

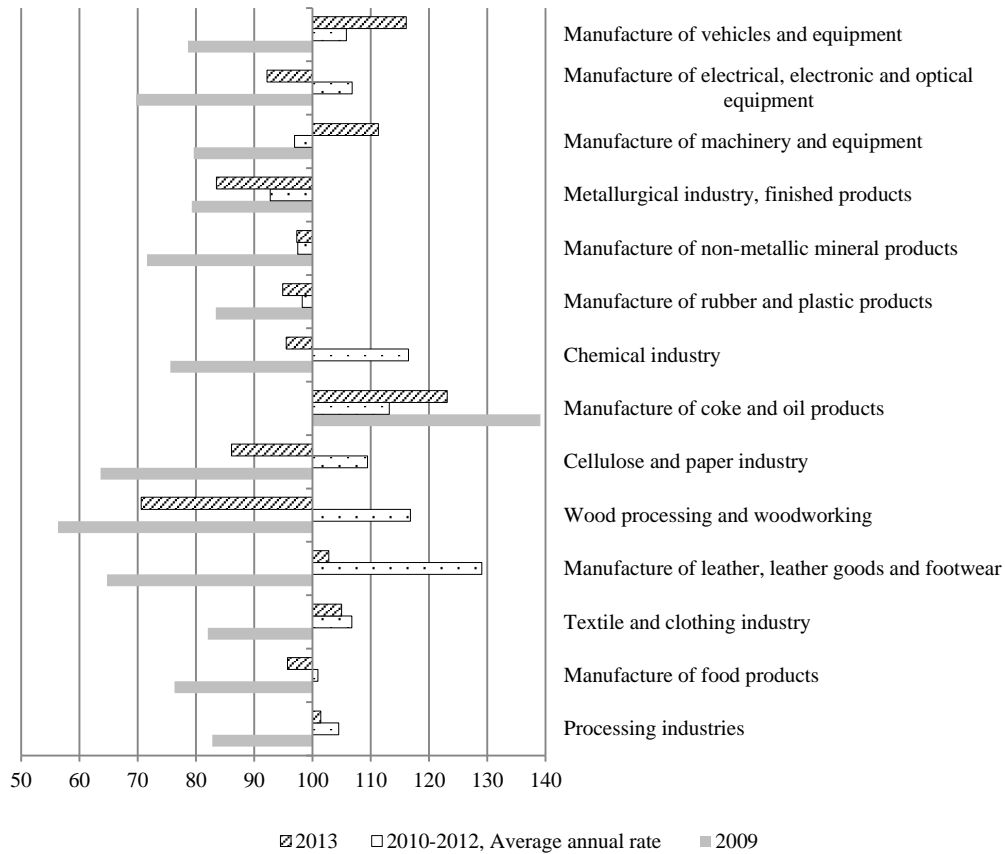
**Investments in fixed capital (excluding small businesses and investments,
not observable by direct statistical methods) in 2008-2013, as % of the previous year**

	2008	2009	2010	2011	2012	2013
Total	109.9	84.3	106.0	108.3	106.6	99.8
agriculture	98.8	78.1	89.1	114.6	92.8	96.0
fishing, fish breeding	88.1	88.1	108.8	137.4	127.4	77.4
production sector	109.9	90.7	106.1	110.9	107.4	96.8
mining	106.5	89.9	106.6	113.8	111.8	93.6
processing industries	112.5	82.8	101.5	105.3	106.7	101.4
production and distribution of electricity, gas and water	111.6	108.9	112.5	114.7	101.7	95.8
construction	126.2	69.9	110.9	90.6	79.9	84.0
wholesale and retail	93.1	79.2	120.2	90.0	107.1	103.1
hotels and restaurants						
transport and communications	116.1	103.5	102.4	118.3	98.4	88.5
financial activity	94.9	99.7	112.9	136.8	111.4	80.8
real estate operations,	109.5	73.7	125.4	91.9	100.8	104.4
public administration	118.3	134.8	115.2	112.4	98.7	93.7
education	108.6	93.0	84.9	122.0	85.2	77.9
health and social services	102.5	79.4	109.7	113.0	93.6	98.8
provision of other services	108.1	83.8	103.6	103.5	111.8	75.0

Source: Federal State Statistics Service (Rosstat).

In the production sector, investment in fixed assets accounted for 96.8% of the 2012 value. One peculiar feature of the investment process in 2013 manifested itself in the maintenance of the positive dynamics of investments in fixed assets in the manufacturing sector (101.4% compared with 2012) while there was a decrease of investment activities in mining (93.6%) and in the production and distribution of electricity, gas and water (95.8%) (Table 15). In 2013, growth of investments in the fixed assets for vehicle production (116.1%), the manufacture of machinery and equipment (111.3%) and the manufacture of coke and oil products (123.1%) outstripped the average level for manufacturing. In line with the established model of reproduction of fixed asset investment demand, mining production in 2013 exceeded the pre-crisis level of 2008 by 14.1%. In manufacturing, instability and the reduction of investment in fixed assets over the previous five years (Fig. 33) were the consequences of the acute investment crisis of 2008, as well as a lack of motivation to modernise production. In general,

in manufacturing, investments in fixed assets in 2013 remained 4.2% below the pre-crisis level, with the exception of oil refining, the chemical industry and production of vehicles that made up almost half of the manufacturing investment demand.



Source: Federal State Statistics Service (Rosstat).

Fig. 33. Growth rate of fixed asset investments in the manufacturing industry in 2009-2013, as % of the previous year

In 2013, the structure of investments by type of fixed assets was transformed by means of increasing the volume and the share of investments in the construction of housing units, as well as machinery, equipment and vehicles whilst reducing the share of investments in non-residential buildings (Table 16). In the previous four years, there had been a gradual increase in the share of investment in the acquisition of domestic machines and equipment in the total volume of investments in fixed assets. In 2013, the share of imported machinery, equipment and vehicles in the total volume of investment in machinery, equipment, vehicles amounted to 16.1%. The growth of investment in imports compared to the dynamics of investment in fixed assets continued the trend of recent years and attests to the lack of development of the domestic production of capital goods.

Table 16

Structure of fixed asset investments by types of assets in 2009-2013 (excluding small businesses and informal activity performance)

	billion rubles	As % of the total
--	----------------	-------------------

	2009	2010	2011	2012	2013	2009	2010	2011	2012	2013
Investments in fixed assets	5,769.8	6,625	8445.2	8,446.2	9,493.4	100	100	100	100	100
including: housing	346.2	384.3	396.9	439.2	550.6	6	5.8	4.7	5.2	5.8
buildings (other than residential) and facilities	3,219.5	3,610.6	4,577.3	4,417.4	4,840.8	55.8	54.5	54.2	52.3	51
machinery, equipment, vehicles	1,800.2	2,179.6	2,896.7	3,006.8	3,366.5	31.2	32.9	34.3	35.6	35.5
of which:										
acquisition of domestically produced machinery, equipment and vehicles	1,427.5	1,787.3	2,357.9	2,519.7	2,825.2	24.7	27.0	27.9	29.8	29.8
acquisition of imported machinery, equipment and vehicles	372.6	392.3	538.8	487.1	541.3	6.5	5.9	6.4	5.8	5.7
Other	409.7	450.5	574.3	582.8	735.5	7.1	6.8	6.8	6.9	7.7

Source: Federal State Statistics Service (Rosstat).

The particular feature of the post-crisis development of the construction and investment complex manifests itself in the faster growth of investments in housing in 2012-2013 compared to the overall dynamics of investments in fixed assets and the construction of non-residential buildings. Positive dynamics of commissioning residential buildings were recorded in the second half of 2011 and evidenced some improvement of the situation with financing. In 2013, organisations of all types of ownership commissioned 69.4m sq m of residential space, which is 5.60% more than in the previous year. It should be noted, however, that the substantial gap which exists between the rates of putting buildings into service and the scope of construction work results from a reduction of required capacity, which will very probably lead to a further decline in the construction industry at the beginning of 2014.