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The review provides a detailed analysis of main trends in Russia's economy in 2011. 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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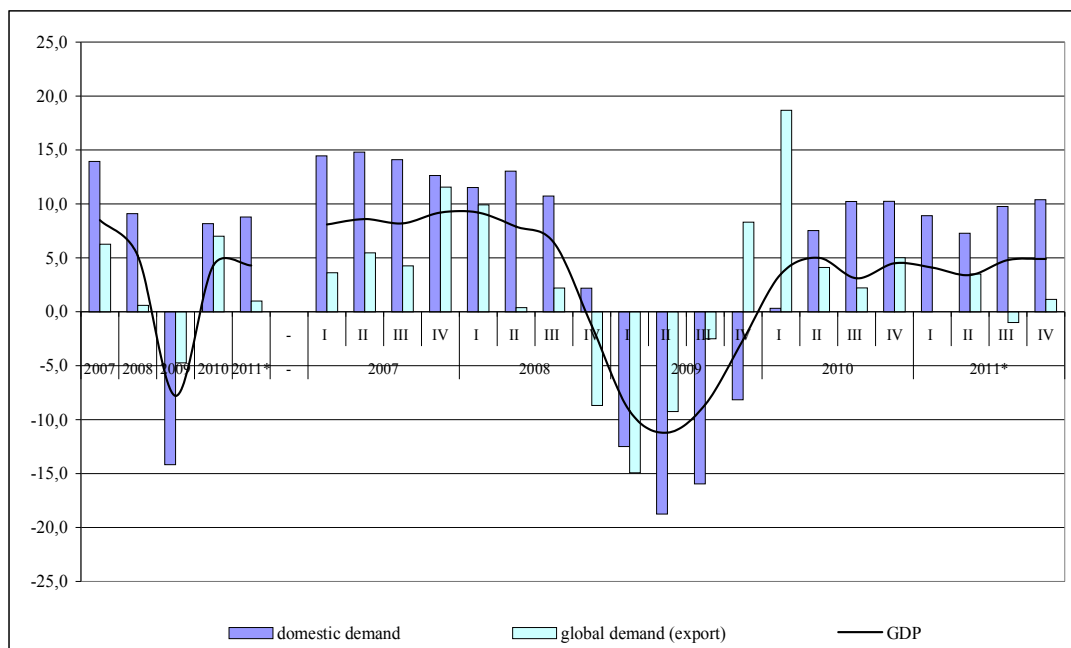
Olga Izryadnova

Production Macrostructure in Russia in 2011

Major trends and economic drivers in 2011

Macroeconomic trends of 2011 were determined by factors having formed during the preceding two years of post-crisis recovery. As an outcome of 2010–2011, average annual rate of GDP growth made 4.3%, and thus, judging by this development indicator, Russian economy has achieved the pre-crisis level of 2008.

The analysis of financial and economic recovery drivers and conditions allows for identifying special characteristics of economy rehabilitation in 2010–2011.



*preliminary estimates.

Source: Federal Statistics Service, RF Ministry of Economic Development.

Fig. 1. GDP dynamics by domestic and global demand components during 2007–2011, % to the respective period of the previous year

Low investment activity is a real characteristic feature of the recovering growth of the recent two years. In 2011 fixed capital investment constituted 96.7, the amount of work in construction constituted 94.4% and the amount of residential space commissioned – 97.1% of 2008 performance. In 1998 post-crisis recovery was completely based on dramatic business activity boom in the investment sector of the economy and was one of the key drivers for overcoming all the negative consequences of production shrinking. On the contrary, in 2010–2011

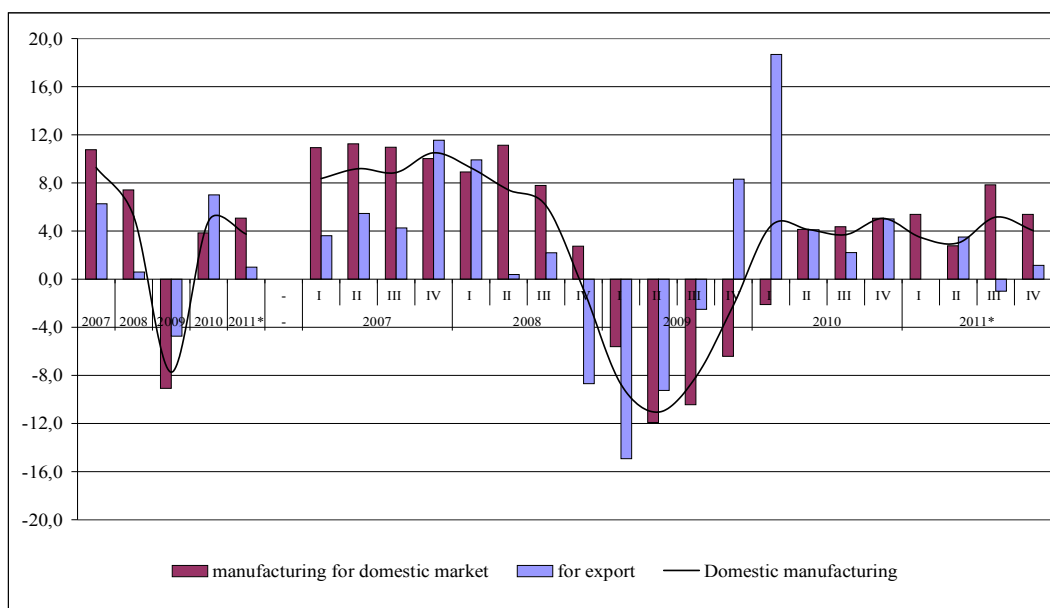
low investment activity during the recovery period was impeding the growth both in production and financial sectors of the economy.

Another special feature of 2010-2011 was pretty quick recovery of the consumer demand. Household demand in 2011 exceeded 2008 level by 6.1%. Contrary to the situation of 1998–2001 when low consumer demand limited the pace of domestic market expansion, 8.1% retail turnover growth in 2011 versus 2008 supported by approximately equal increase of the real income of the population became the dominating driver of economic recovery, including recovery of the financial sector at the expense of intensive growth of demand for cash loans.

When comparing the processes of post-crisis recovery in 1998 and in 2008, the impact of foreign trade should be noted. In the environment of rapid global economic recovery after 1998 crisis and favorable dynamics of global energy and raw materials markets, Russian economy was able to restore its export during one year. After long global economic recession in 2008 Russia was able to regain its export at the pre-crisis level only in 2010, and as of the end of 2011 its physical export volumes exceeded 2008 level by 3.0%.

Given GDP growth in 2011 at the level of 4.3%, the domestic demand grew by 8.8% (in 2010 – by 8.2%), including the domestic production – by 5.1% (3.8%), and the external demand – by 1.0% (7.1%) versus the preceding year.

The domestic market dynamics was defined by the ratio between the domestic production growth rates for domestic and foreign consumption, on one hand, and imports dynamics and structure – on the other hand. In 2010 the outrunning growth of the exporting sector defined the intensity of post-crisis recovery for domestic manufacturing targeted at the domestic market, but in 2011 acceleration of domestic production growth (5.1% versus 3.8% in the preceding year) obviously turned out to be insufficient to counteract the consequences of abrupt export slowdown. Eventually, in 2011 the domestic manufacturing growth rate made 103.7% and was 1.2 p.p. lower, than in 2010. Let us note, that slowdown of the growth rate was accompanied by maintaining high import dynamics.



* preliminary estimates.

Source: Federal Statistics Service, RF Ministry of Economic Development.

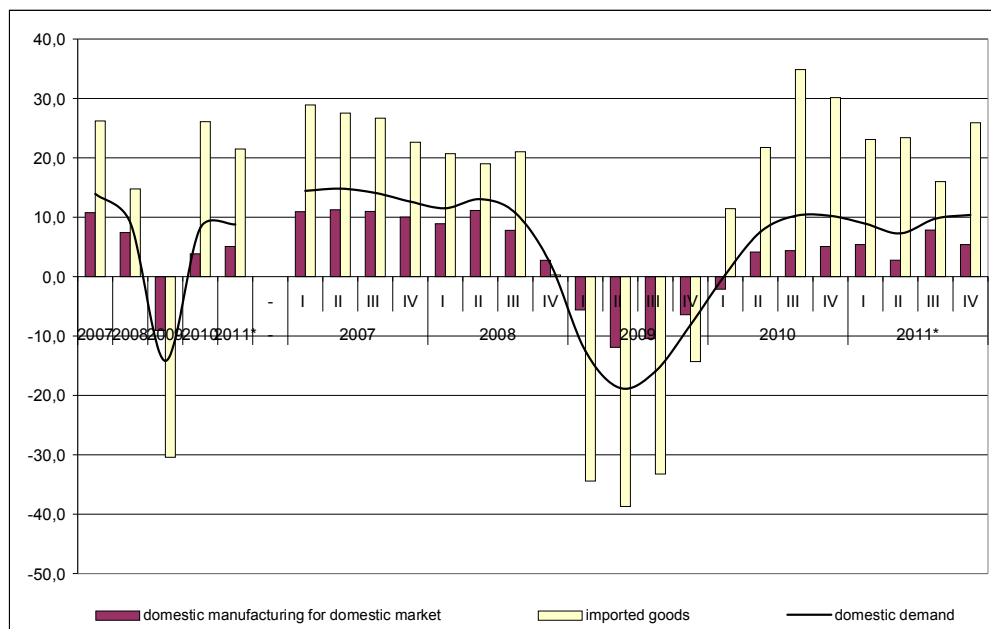
Fig. 2. Domestic manufacturing dynamics by components of usage in 2007–2011, % to the respective period in the preceding year

In terms of descending import, 2009 is comparable with 1998-1999; however, the recovery was completely different. 4.53 devaluation of ruble versus dollar in 1998–1999 resulted in dramatic fall of import efficiency in the domestic market and stimulated intense growth of import-substituting production and expansion of niches for domestically manufactured products (in that period domestic inflation was 251.7%). In 2008–2009 dollar versus ruble exchange rate went up only by 23.2% compared to 2007, which correlated with inflation growth rate. Quick recovery of global market demand starting from Q2 2009 and global prices change in favor of Russia throughout 2010 resulted in foreign trade price conditions index exceeding the post-crisis value.

In 2010–2011 the effective exchange rate of ruble got up and the domestic market situation was formed in the context of increased imports and pretty modest dynamics of domestic manufacturing of consumer goods. Besides, the recovery of demand for imported goods was supported by the maintained positive growth dynamics of the real income of population.

No large-scale import-substituting production growth was observed in 2009-2011 in the context of the ratio between ruble exchange rate and domestic inflation, as well as production dynamics and structure and lack of competitive back-up production capacities.

The out-running physical import growth rate versus export and GDP was a special characteristic in 2010–2011. As of the end of 2011, foreign trade turnover (physical volumes, as of SNA methodology) went up by 8.7%, including export – by 1.0% and import – by 21.5% versus the preceding year¹.



* preliminary estimates.

¹ Foreign trade turnover index value (balance of payments methodology) in 2011 versus the preceding year made 130.2%, export – 130.4% , import – 129.9%

Source: Federal Statistics Service, RF Ministry of Economic Development.

*Fig. 3. Internal demand dynamics by components
in 2007–2011, % to the respective period in the preceding year*

Domestic market expansion was an important dominating driver for post-crisis economic development in 2010–2011. In this context special attention needs to be paid to the following trend which is growing stronger: supplies of imported goods outgrow the domestic production dynamics. The domestic production targeted at domestic market needs was recovering very slowly despite the fact that during the acute phase of the crisis (2009) its fall had been not as deep as import shrinking.

The share of import in 2011 goods/materials retail circulation was 43%, including 33% for food products and 51% for non-foods.

Table 1

Retail trade resources structure in 2010–2011, %

	Retail trade resources	Including	
		domestically manufactured	imported
2010			
Q1	100	56	44
Q2	100	58	42
Q3	100	55	45
Q4	100	55	45
Annual	100	56	44
2011			
Q1	100	57	43
Q2	100	58	42
Q3	100	57	43
Q4	100	55	45
Annual	100	57	43

Source: Federal Statistics Service.

In the producer goods market gradual raise of imported goods share was also observed. The shifts in the overall structure of imported goods were defined by the trend for increased share of the intermediate demand goods. During H1 2011 the share of imported producer goods made 19.2% versus 17.8% in the preceding year, and the share of imported intermediate goods made 42.9% versus 40.7%. Despite the increase of imported producer goods share starting from Q3 2011, the share of intermediate goods continued to remain much higher than in 2008–2010.

The increase of producer and intermediate goods share in the import structure with simultaneous decrease of the consumer goods share was a qualitatively new process in the Russian economy, which may turn out to be the start of priority change and increased incentives to production development in the environment of limited domestic material and technical resources. It seems that further development of the real economy sector in such situation will be dependent on the intensity of fixed capital investment targeted at modernization and diversification of the production. Besides, adjustment of capital goods and associated goods volumes characteristic for the period 2007–2008 has led to changes in industrial sector recovery structure in 2010–2011.

In industrial sector the post-crisis recovery both in 2008 and in 1998 started with the recovery of the growth rates in mineral wealth extraction driven by changes both in the global and domestic markets. In 2011 the mineral wealth extraction index made 104.9% versus the pre-

crisis values of 2008. In processing crisis was more protracted during 2008–2009 compared to 1998 crisis, so getting back to the upward curve took twice as much time. Recovery of yields in processing and achieving the pre-crisis level of 2008 took place as late as in 2011.

The dependence of domestic production development dynamics, specifically – of enterprises operating under the industrial assembly regime, on the imported goods supplies was growing. In this context the import-replacing production and localization issues are becoming more and more relevant taking into account the special characteristics of development and modernization of certain processing industries of Russian economy. In the “Social and Economic Development Forecast for the RF in 2012 and for the Planned Period of 2013 and 2014” it is declared that the key economic growth driver in the mid-term perspective should be not just in increase of investment and consumption, but more – in increasing the level of competitiveness of domestic goods, which is to balance-off ruble exchange rate strengthening. However, the domestic market dynamics forecast for 2012–2014 is still based on import boom.

Table 2

**Russian Federation Import Structure (balance of payments methodology),
% to the outcome**

	Goods		
	consumer	producer	intermediate
2006	46.2	17.0	36.8
2007	44.4	18.9	36.7
2008	41.8	23.8	34.4
2009	44.3	19.7	36.0
2010	40.7	19.5	39.8
Q1	43.5	16.8	39.7
Q2	39.6	18.7	41.7
Q3	40.6	19.7	39.7
Q4	40.0	21.5	38.5
2011	36.6	21.4	42.0
Q1	40.2	18.2	41.6
Q2	35.2	20.3	44.5
Q3	35.0	23.0	42.0
Q4	37.0	23.0	40.0

Source: Federal Statistics Service.

As of the end of 2011 the GDP growth rate made 104.3% versus the preceding year. During H1 2011 this growth was mainly associated with favorable situation in the global market for raw materials and with consumer market expansion. Capital investment in H1 2011 grew by 2.7% with GDP growing by 3.7% versus the similar period of the preceding year.

In H2 of 2011 the accelerated GDP dynamics is connected with the structural specifics of the economic growth: capital investment growth rates were speeding up, as well as construction and agricultural production volumes, versus the similar period of the preceding year. In the end of 2011 capital investment grew by 6.2%, construction volumes – by 5.1%, and agricultural production – by 22.1%. As a result, 2011 domestic market dynamics was determined by simultaneous growth of the demand both for consumer goods and for investment. Retail trade turnover made 107.2% versus 2010, and the level of fee-based public services made 102.9%. The cumulative impact of these factors was enough to weaken the trend for slowing down the domestic demand for industrial products and infrastructure services.

In 2011 the industrial production growth was that of a recovery nature targeting the pre-crisis development trajectory. As of the year end, the industrial production index made 104.7%

versus 2010. The outrunning growth rate in processing had the dominating impact on the whole industrial sector dynamics and structure. In processing production index made 106.5%, and in mining – 101.9% versus the same indicators of 2010.

Table 3

**Major macroeconomic indicators indices in 2010–2011,
% to the preceding year**

	2010	Quarters				2011	Quarters			
		Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4
Gross domestic product	104.3	103.5	105.0	103.1	104.5	104.3	104.1	103.4	104.8	104.9*
Capital investment	106.0	95.2	105.6	105.3	111.1	108.3	99.2	105.0	108.2	113.6
Construction	103.5	92.7	100.8	106.6	107.1	105.1	101.6	101.0	107.6	106.9
Residential space commissioning	97.6	91.1	107.3	85.7	102.3	106.6	97.8	95.1	115.0	111.4
Industrial output	108.2	109.5	110.9	106.4	106.5	104.7	105.9	104.8	105.1	103.3
Extraction of mineral resources	103.6	106.7	104.8	101.3	102.0	101.9	103.3	101.7	102.2	101.3
Processing / manufacturing	111.8	112.1	116.3	109.5	109.9	106.5	110.6	105.8	105.7	104.6
Production of electric energy, gas and water	104.1	107.7	102.6	103.9	101.6	100.1	99.0	101.9	101.4	98.5
Agricultural output	88.7	100.5	98.6	79.2	96.2	122.1	100.7	100.6	116.9	132.6
Freight turnover	106.9	111.6	113.0	101.7	102.5	103.4	103.9	105.2	102.4	102.3
Retail turnover	106.3	102.2	106.9	108.4	107.4	107.2	105.2	106.1	107.9	109.1
-food products	105.1	103.7	105.7	107.3	103.7	103.6	101.4	101.3	103.8	107.1
-non-food products	107.6	100.9	108.1	109.5	111.0	110.7	109.0	111.0	111.8	110.9
-fee-based public services	101.5	99.9	101.6	101.5	102.6	103.0	102.9	103.8	102.4	102.8
Foreign trade turnover	131.1	144.1	139.0	126.3	121.4	130.2	129.8	139.5	130.0	124.1
-export	132.0	161.1	143.4	118.4	118.1	130.4	123.8	138.4	134.2	128.2
-import	129.7	118.8	132.4	139.5	126.7	129.9	141.9	141.5	124.1	118.0
Real disposable cash income	104.2	107.3	103.7	104.5	102.1	100.8	100.0	99.0	101.6	102.7
Real wages	105.2	103.1	106.1	105.1	104.2	104.2	101.6	102.7	103.8	108.5
Total number of unemployed	88.9	96.2	86.6	86.8	85.2	89.1	85.7	88.1	91.8	91.6
Number of officially registered unemployed	90.0	114.2	91.1	81	74.9	76.9	73.1	75.4	78.0	80.2

* preliminary estimates.

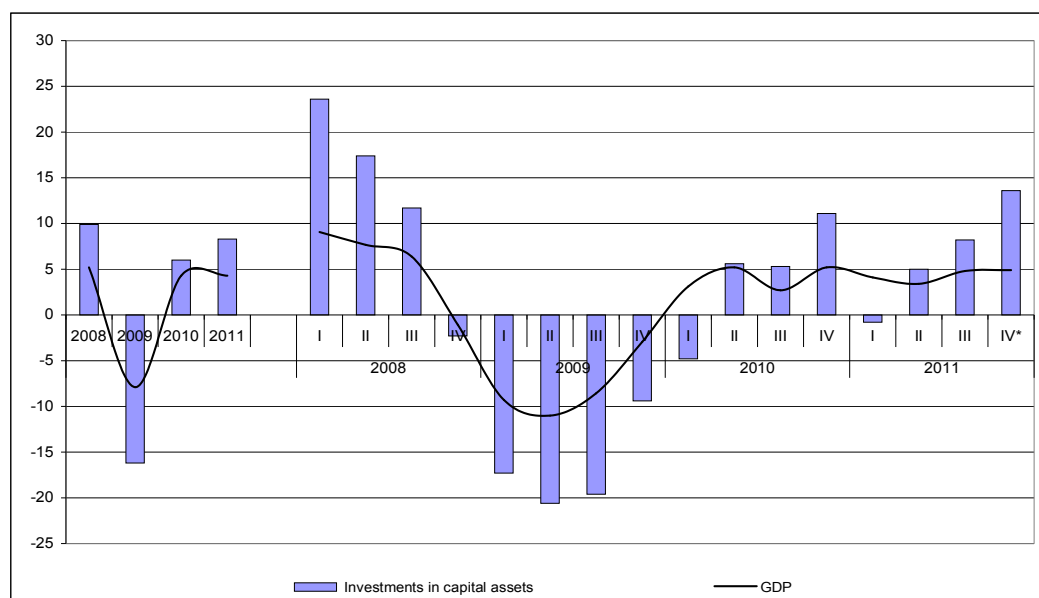
Source: Federal Statistics Service, RF Ministry of Economic Development.

Last year's domestic market expansion was taking place in the context of changes in the structure of the demand for domestic goods. Special feature of 2011 situation was growth of stock in the second half of the year. Dynamic growth of stock remained one of the key drivers for higher GDP growth rates in the second half of the year despite the fact that production growth in industry overall was slowing down. Let us note, that the forecast for 2012 by the RF Ministry of economic development assumes some slowdown of the economic growth to 103.7%, including – due to exhaustion of the stock contribution into the recovery growth of the economy.

Major characteristics of GDP utilization

The trend of investment growth acting across the whole period between 2000 and 2008 demonstrated a breaking point in 2009, so the decline of capital investment was registered for the first time after 1998 crisis. Recovery of capital investment in 2010–2011 was characterized by pretty slow pace and was taking shape under the inertial influence of the preceding three years and factors acting at that time. Starting from Q2 2010 investment started to grow. In 2010 capital investment growth rate made 106.0%, and in 2011 it was 108.3% в 2011. However, when evaluating the dynamics of this indicator, one needs to take into account that in

2009 the base line was very low. In 2009 capital investment fell by 15.7%, so the decline was much deeper than during 1998 crisis. As the result, capital investment in 2011 made 96.7% of 2008 level.



Source: Federal Statistics Service.

Fig. 4. GDP and capital investment dynamics in 2008–2011, % to the preceding year

In the context of the situation with capital markets and savings resources the capital investment share in GDP structure during 2009–2010 period went down to 20.4% (compare with 21.3% - the maximum value for the last decade registered in 2008). In 2011, despite the savings ratio going up to 31.9% GDP thus exceeding the average of the preceding two years by almost 3 p.p. GDP, the capital investment share in GDP structure made 19.4% and remained below the average of the preceding two years by 1 p.p. GDP.

Table 4

**Gross savings, gross capital formation and capital investment shares
in GDP structure during 1998–2010, % of total**

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Gross savings	30.8	31.4	32.6	33.2	33.8	33.9	33.3	24.6	29.0	31.9
Gross capital formation	20.0	20.7	20.8	20.0	21.2	24.4	25.1	18.6	22.3	24.9
including:										
gross fixed capital formation	17.9	18.3	18.3	17.7	18.5	21.2	22.0	21.6	21.3	20.5
Capital investment	16.3	16.6	16.8	16.7	17.6	20.2	21.3	20.6	20.3	19.4

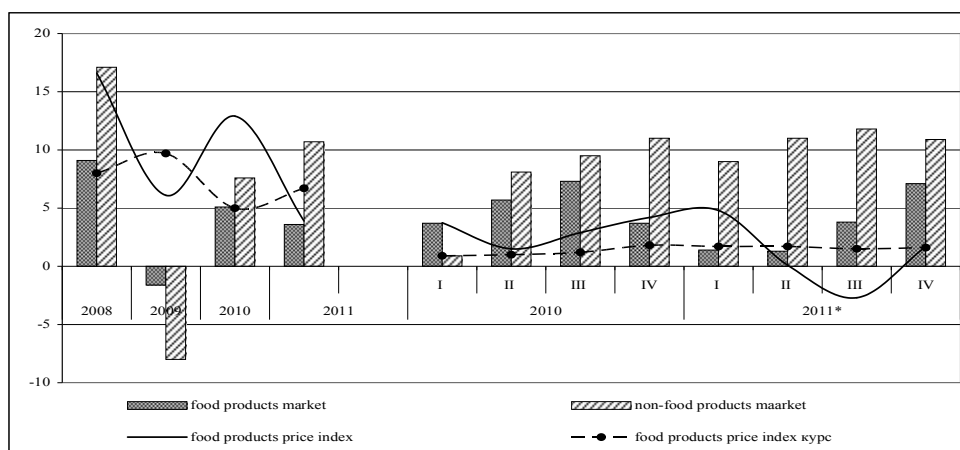
Source: Federal Statistics Service.

Consumer demand growth across the whole 2011 remained one of the main supporting economic growth drivers. In 2011 real income of the population made 100.8%, real wages – 104.2%, and real granted pension amounts – 101.2% to the respective 2010 values.

Overall, during the period of 2009-2011 real disposable income of the population went up by 9.8% versus the pre-crisis indicator of 2008. Let us note that structural specifics of real in-

come dynamics were determined by the growth of the granted pensions (161.1% to 2008) out-running the growth of the real wages (105.8%).

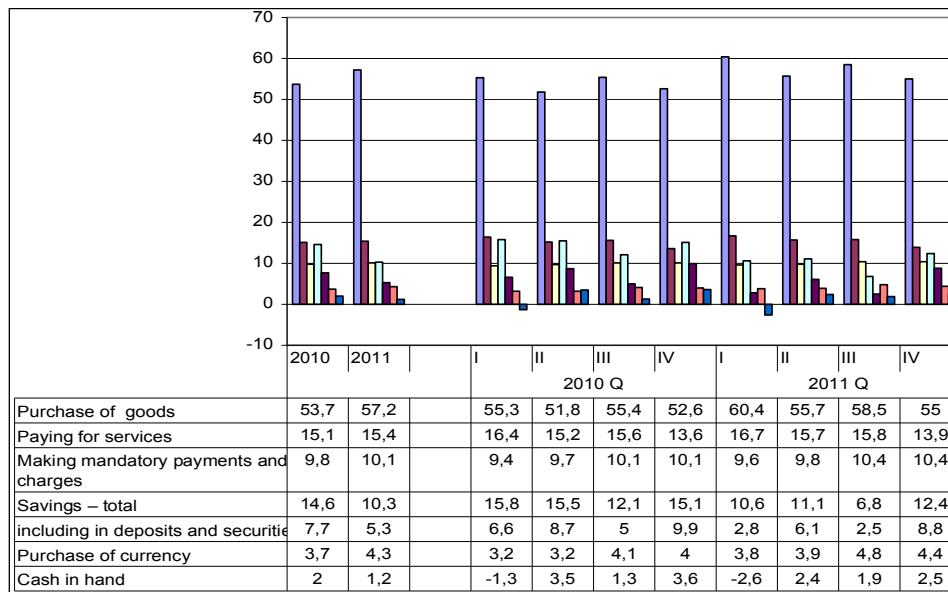
In the context of growth of the real income of population in 2010 the consumer market recovered at the pre-crisis level of 2008. Retail sales turnover in 2011 went up by 7.2% versus the preceding year. Snap acceleration of the non-food goods markets growth rate in the context of food products retail turnover rates slowdown became the characteristic feature of 2011. Non-food market turnover growth index made 110.7% versus 2010, and for food products it was 103.6%. At the same time, it is worth noting that while the food product market exceeded the pre-crisis level of 2008 by 3.3% in 2010 and by 7.1% in 2011, the non-food market was able to recover at the pre-crisis level only in 2011. Inflation rate slowdown in 2011 had a significant impact on forming of this trend: in food products market inflation rate went down to 103.9% (compare with 112.9% in the preceding year), and the price change was bigger in non-food market (106.7% in 2011 versus 105.7% in 2010) and fee-based public services market (108.7% versus 108.1%).



*preliminary estimates.

Source: Federal Statistics Service, RF Ministry of Economic Development.

Fig. 5. Consumer markets and prices growth rates in 2008–2011, % to the respective period of the preceding year



Source: Federal Statistics Service.

Fig. 6. Structure of using cash income of population in 2010–2011, % of total

Retail sales growth factors in 2011 remained based on savings ratio going down and consumer crediting going up. The share of savings in the income of population went down to 10.3% versus 14.6% in 2010, including savings in deposits and securities going down to 5.3% versus 7.7%. As of the end of December 2011 loans to individuals were issued for Rb 5,550.9bn and increased 1.36 times versus the same month of 2010.

Changes in GDP structure formation – by revenue sources

Domestic market growth support in 2011 was based on redistribution of income from enterprises to the population. The share of wages in GDP in 2011 made 49.9% versus the average of 46.1% in the period between 2002 and 2008. The insurance premiums increase impacted the structure of GDP formation from the revenues point of view. It resulted in decrease of the gross profit of the economy as GDP share in 2011 by 1.2 p.p. versus the preceding year remaining below the pre-crisis level of 2008¹.

Table 5

Structure of GDP formation by revenue sources in 2008–2011, % of total, on current basis

	2008	2009	2010	2011	2011			
					Q1	Q2	Q3	Q4
Gross domestic product	100	100	100	100	100.0	100.0	100.0	100.0
including:								

¹As per the RF Ministry of Finance, in 2009 at 26% rate insurance premiums revenues made 5.93% of GDP and in 2011 at 34% rate – 6.49% of GDP. In 2009 Individual Income Tax made 4.29% of GDP, in 2010 – 3.96%, and in 2011 – 3.67%. Aggregate IIT + insurance premiums revenues decreased from 10.22% of GDP down to 10.16%. It may be assumed, that the insurance premiums increase has led to increase in the latent salaries and mixed income.

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Wages of hired employees, including latent salaries and mixed income	47.4	52.6	49.9	49.3	53.8	51.7	47.5	45.4
Net production and import taxes	20.0	16.7	18.2	20	19.4	20.8	19.6	20.3
Gross profit in economics and gross mixed income	32.6	30.7	31.9	30.7	26.8	27.5	32.9	34.2

Source: Federal Statistics Service.

Within the structure of employed population employers providing for full-time employment of their hires and the self-employed make 8%. This is the factor determining the specific characteristics of GDP and population income structure. Almost 66% of population income in 2011 was formed at the expense of hired employees' wages.

High level of salary differentiation by types of business is a characteristic feature of Russian economy. In industrial production the degree of differentiation is determined by the growing gap in manufacturing and in sectors associated with mineral resources extraction. In the latter the nominal gross payroll in 2011 was 1.88 times higher the average level of wages across the economy. As for fuel-and-energy sector, the wages there were 2.2 times above the average. In manufacturing wages were 93% of the average level and only 45% of the wages at producing facilities. Gross payroll on petroleum products production and transportation of fuel and energy resources, as well as in financial sector was 2.3 higher than average level across the economy. In education and healthcare average wages got down to 65–74% of average level across the economy. The specifics of wages by types of business significantly impacted the structure of both revenue and expenditure formation, on consumer demand, on employment profile and distribution of resources across the economy.

Mitigation of labor market tension and recovery of demand for labor force in 2011 were the major outcomes of 2009–2010 anti-crisis program. The number of economically active population in 2011 was 75.7m persons, including 70.7m of gainfully employed and 5.0m of unemployed (using ILO methodology). The level of employment in 2011 made 63.8% exceeding the preceding year level by 1.1 p.p. in the context of the overall unemployment rates going down to 6.6% (by 0.9 p.p. versus 2010).

The total number of unemployed as of the end of 2011 exceeded the number of unemployed registered with government employment agencies 3.6 times in December 2011. 1,286,000 people were registered as unemployed with government employment agencies. The tension coefficient (the number of registered unemployed per 100 vacancies) in December 2011 was 175.9 (compare with 120.7 persons in January of the same year).

Table 6

Labor market fundamentals dynamics in 2009–2011

	2009	2010	Quarters				2011	Quarters			
			Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4
Number of employed in economy, m pers.	69.4	69.8	68.0	70.0	71.1	70.1	70.7	69.4	70.7	71.9	70.9
Number of unemployed, m pers.	6.3	5.6	6.6	5.6	5.2	5.2	5.0	5.6	5.0	4.8	4.7
Unemployment level, % to economically active population	8.4	7.5	8.8	7.4	6.8	6.9	6.6	7.5	6.6	6.2	6.3
Number of unemployed registered with government employment agencies, m pers.	2.1	2.2	2.2	2.0	1.7	1.5	1.4	1.6	1.5	1.3	1.2
Registered unemployment level, % to economically active population	2.8	2.5	3.0	2.7	2.2	2.1	1.9	2.2	2.0	1.7	1.6
Average monthly accrued nominal wages, Rb	18,785	21,090	19,485	20,809	21,031	23,045	23,532	21,354	23,154	23,352	26,202
% to the same period of the preceding year											
Number of employed in the economy	97.8	100.6	99.6	101.0	101.0	100.9	101.3	102.1	101.0	101.1	101.1
Number of unemployed	131.1	89.1	96.3	86.7	87.2	85.2	89.1	87.5	88.1	91.8	91.6
Number of unemployed registered with government employment agencies	148.0	90.0	114.2	91.1	81.0	74.9	73.6	73.1	75.4	78.0	80.2
Average monthly accrued nominal wages, RB	108.5	112.4	110.5	112.4	111.6	112.7	112.2	111.2	112.5	112.2	113.1

Average monthly accrued real wages, RB	97.2	105.2	103.1	105.1	104.2	102.4	104.2	101.6	102.7	103.8	105.9*
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* preliminary estimates.

Source: Federal Statistics Service.

During 2000–2011 deviations in the demand for labor force were based on shifting the majority of employed to the services sector. Employment decrease was registered in the industrial sector practically for all types of business. This decrease of employment was especially intensive in the manufacturing sector. During the last three years the situation became even more complicated due to 2008 crisis which caused abrupt decrease in number of jobs in trade and construction.

Comparing the dynamics of employment, wages and GDP one can see that outrunning growth of wages versus labor productivity resulted in increased load on the economy and impacted financial performance of companies.

In 2011 positive balanced financial result of companies' performance was obtained in the amount of Rb 7,252.7bn, which is 20.0% above the preceding year performance. However, despite certain positive trends, overall in the economy the pre-crisis profitability level was not achieved. Profitability of goods sold, production output and work done as of the end of 2011 made 11.0% and were 2.0 p.p. below 2008 level. Extraction of mineral resources continued to remain the most profitable business activity in 2011.

Table 7

Labor productivity in Russia, % to the preceding year

	Code of business activity by All-Russian Classifier	2003	2004	2005	2006	2007	2008	2009	2010
Total for the economy		107.0	106.5	105.5	107.5	107.5	104.8	95.9	102.7
including:									
Agriculture, hunting and forestry	A	105.6	102.9	101.8	104.3	105.0	110.0	104.4	89.3
Fishery and fish-breeding	B	102.1	104.3	96.5	101.6	103.2	95.4	106.2	101.4
Extraction of commercial minerals	C	109.2	107.3	106.3	103.3	103.1	100.9	108.5	101.3
Processing and manufacturing	D	108.8	109.8	106.0	108.5	108.4	102.6	95.9	109.0
Production and distribution of electric energy, gas and water	E	103.7	100.7	103.7	101.9	97.5	102.1	96.3	98.9
Construction	F	105.3	106.8	105.9	115.8	112.8	109.1	94.4	94.8
Wholesale and retail	G	109.8	110.5	105.1	110.8	104.8	108.1	99.0	98.5
Hotels and restaurants	H	100.3	103.1	108.5	109.2	108.0	109.2	86.7	93.7
Transport and communications	I	107.5	108.7	102.1	110.7	107.5	106.4	95.5	103.9
Real estate transactions, leasing and provision of services	K	102.5	101.3	112.4	106.2	117.1	107.5	95.3	94.2
For reference: real accrued wages		110.9	110.6	112.6	113.3	117.2	111.5	96.5	105.2

Source: Federal Statistics Service.

Favorable situation at the global market of hydrocarbons and mineral resources allowed for producing companies quick recovery. Their profits continued to grow across the entire 2010 (151.7% versus the preceding year). This trend was maintained in 2011, the financial performance of these companies made Rb 1981.0bn (148.7% versus 2010), the drivers of which were such as producers' prices growth by 29.1% and global prices growth by 39.3% (Brent) in the context of production growth by 1.3% in 2011 versus the preceding year. The total profit

margin for mineral resources extraction sector made 35.7% having grown by 2.2 p.p. versus 2010. The cost-effectiveness of hydrocarbons production in 2011 made 32.1%, of other mineral resources extraction – 64.5%, which was the maximum level starting from 2005.

Financial performance of processing and manufacturing companies in 2011 made Rb 1904.1bn, thus exceeding 2010 level by 20.4%, and production output growth made 6.5%. Let us note that given unstable external demand in H2 2011, reduction of balanced financial result by 3.1% to the respective period of the preceding year was registered due to weaker dynamics of export-oriented enterprises operations. The balanced financial result of companies trading in foreign markets increased by 15.1% in 2011, and for companies oriented towards domestic markets – by 32.9%.

During the post-crisis period financial performance in oil refining were also gradually improving. As of the end of 2011, financial performance of oil refineries made Rb 735.0bn, which is 22.9% above the preceding year level. During 2011 oil refining output increased by 3.3%, and the producers' prices grew by 17.6% versus 2010. However, the refining margin in 2011 went down to 19.8% versus 23.1% in the preceding year due to the increase of production costs and lack of positive trends in upgrading the feedstock processing technology.

Chemical enterprises have been demonstrating improvement of financial metrics since 2010. In 2011 balanced financial result of such enterprises made Rb 274.4bn having increased by 65.1% versus the same period of the preceding year. Let us note that in chemical sector the producers' prices growth in 2011 was 110.3% and production output growth – 105.2% versus the preceding year. High level of machines and equipment wear-and-tear, poor product mix and poor quality of domestic supplies versus the exported products had a very negative impact on chemical enterprises performance. Profitability in chemical sector in 2011 made 24.9% and exceeded the level of 2010 by 5.1 p.p. at the expense of intensive reduction of production costs due to reduction of the employed people number.

Table 8

Profitability of goods sold, production output, work done, services rendered and assets of companies in 2008-2011 by types of business, %

	Profitability of goods/work/ services sold,				Profitability of assets				For reference		
	2008	2009	2010	2011	2008	2009	2010	2011	2011 versus 2010		December 2011 vs. December 2010
									Financial performance rate	Gross Value Added physical indices	Prices indices
Total	13.0	11.5	11.4	11.0	5.4	5.7	6.8	7.0	120.0	104.3	
including: Agriculture, hunting and forestry	10	8.4	10.3	10.3	4.8	3.1	3.4	4.2	144.5	116.1	94.9
Fishery and fish-breeding	7.4	21.4	20.8	22.0	1.0	14.5	13.9	13.8	129.2	113.2	
Extraction of commercial minerals	25.4	29.2	35.5	35.7	10.5	11.3	14.5	18.4	148.7	101.7	126.7
Processing and manufacturing	17.1	12.5	14.3	13.2	8.6	5.6	7.8	8.2	120.4	106.1	108.3
Production and distribution of electric energy, gas and water	4.9	7.6	7.2	6.7	2.3	3.6	5.3	1.4	33.3	100.4	105.1
Construction	5.6	6.6	5.7	6.6	3.1	2.9	2.2	2.4	102.9	104.8	108.0

Wholesale and retail; maintenance of motor vehicles, bikes, household appliances and individual supplies	10.8	8.3	9.2	8.9	5.3	7.9	6.9	10.4	178.0	105.0	
Transport and communications	14.2	14.1	13.8	12.8	5.4	4.5	5.0	4.7	107.6	102.9	108.4

Source: Federal Statistics Service.

In metal industry balanced financial result in 2011 made Rb 370.9bn meaning 8.1% decrease versus the preceding year. Starting from H2 2011 external demand for Russian metallurgic products was going down, which became the cause for deterioration of balanced financial result. Production profitability in metal industry decreased by 2.8 p.p. versus 2010 and made 15.9%. As of the end of 2011 the production output level in metal manufacturing and metal goods manufacturing grew only by 2.9% versus 12.4% growth in the preceding year, and producers' process growth went down from 122.4% to 104.7%.

In timber industry balanced financial result decreased by 12.3% versus 2010. In the environment of production rates slowing down in wood processing and in pulp-and-paper production the profitability level was maintained at the expense of increased producer's prices.

Currently the pre-crisis levels of production capacity utilization have been achieved in processing sector. Hitting the intensive growth limit at the expense of increasing the capacity utilization rates is accompanied by intensive import of foreign goods. Combination of these two factors leads to volatile dynamics of processing industries output.

Companies producing goods non-marketable in foreign markets are in the majority of cases inefficient. It is worth noting that despite financial performance improvement in business activities targeted at meeting the internal investment demand, the situation in these fields remains not quite favorable.

In construction materials production the profitability rate in 2011 was 11.8%, which is a 3.9 p.p. increase versus the preceding year. However, this indicator is still significantly lower than the pre-crisis level (18.9% in Q1 2008). Last year the profitability growth was driven by gradual growth of demand and by production output growth by 9.3% versus 2010, on one hand, and by facilitated growth of prices for products and services in this sector – by 113.5% versus 103.6% a year earlier.

In the mechanic engineering sector the balanced financial result of 2011 exceeded the level of the preceding year 1.86 times, but significant differentiation by types of business may be observed here. Given a pretty much restrained pricing policy, indicative for this sector, the dynamics of production yield and the level of production costs had the dominating impact on the profitability level. Also, performance of mechanical engineering companies was significantly impacted by the outrunning growth of production costs in this sector versus the economy in general and processing enterprises in particular at the expense of labor costs growth. The profitability of machines and equipment manufacturing in 2011 made 7.0% versus 7.3% in the preceding year, and the profitability of electric equipment, electronic and optical equipment manufacturing – 10.0% versus 10.1% respectively.

In 2010-2011 significant growth was observed in transportation vehicles and equipment manufacturing, which was related with implementation of car-manufacturing anti-crisis support programs. In 2011 transportation vehicles and equipment manufacturing maintained its leading position with regard to production output growth rates versus other areas of mechanical engi-

neering sector. As of the end of 2011 the balanced financial result in transportation vehicles and equipment manufacturing made Rb 86.4bn, and sales profitability exceeded the pre-crisis level making 7.5%, which was 2.7 p.p. versus the preceding year.

In consumer goods manufacturing output growth rates slowdown was accompanied by facilitated dynamics of manufacturers' prices and gradual slowdown of wages growth rates. Profitability of textile and clothing manufacturing in 2011 grew up to 7.1% versus 5.4% in the preceding year, and in leather and leather garments manufacturing profitability went down to 7.5% versus 8.0%. In food products manufacturing profitability decreased by 4.1 p.p. versus 2010 and made 8.1%. Slowdown of foods products manufacturing growth rates (down to 101.0%) in 2011 with simultaneous growth of the manufacturers' prices by 1.8% became one of the key factors here determining poorer performance. Financial result in food products manufacturing in 2011 made Rb 147.0bn, which was 25.8% lower the result of 2010.

In general, the analysis of production dynamics and financial results allows for making a conclusion about gradual post-crisis recovery of the economy and overcoming of 2008–2009 phenomena. However, financial results were improving versus the preceding year mainly due to pricing factors. Given a slowdown in the economy growth rates, the production costs did not go down, and the efficiency of labor and capital utilization went down. Surely, the increase in labor costs and insurance premiums on salaries (from 26% up to 34% in 2011) impacted the financial performance of businesses and companies. In 2011 the financial result growth rate under the cumulative impact of all the above listed factors made 120.0% versus 142.8% in 2010, and profitability went down by 0.4 p.p. versus the preceding year.

Production dynamics and structure by types of economic activity

Overcoming the negative consequences of 2008–2009 crisis and hitting the growth trajectory is determined by specific features of operations in certain sectors of the national economy and certain types of business. In general, the structure of restored economic growth of 2009–2011 period mirrors the post-crisis development pattern of 1998–2000, when the growth emerged in food products manufacturing and in mineral resources extraction, as well as other processing enterprises associated with processing hydrocarbons and other mineral resources. Then this growth rolled-out to sectors of industrial production. Speaking of the basic sectors, the biggest decrease of production was registered in H1 2009, when the decline made 13.9% to the level of the respective period of the preceding year. Starting from H2 2009 due to recovery of external demand and due to government anti-crisis measures the situation began to improve and as of the end of the year the decline in industrial production was making only 9% of the preceding year level. Recovery of demand for energy in domestic and foreign markets resulted in mineral resources extraction growth in Q4 2009, which, in its turn, contributed to further development of processing manufacturing sectors. In H1 2010 the industrial output growth rate was 110.2%, including 105.8% for extraction and 141.3% for processing.

Starting from Q3 2010 some slowdown of the economic growth could be observed, caused by decline of export growth rate. In Q3 2010 industrial production index made 106.3%. However, in Q4 while rather high rates of investment growth and consumer market development were preserved, total industrial growth rate was 6.5%, including 9.9% in processing.

During 2011 the growth rates in industry slowed down, which was to a great extent determined by high base of the previous year. In 2011 industrial production index made 104.7%, including 101.9%, for mineral resources extraction, 106.5% in processing and 100.1% in pro-

ducing and distributing electric energy, gas and water. In 2011 situation in industrial sector was unique – contrary to the entire period of 2000th when the growth was supported mainly by mineral resources extraction, last year the growth in industrial production took place mainly at the expense of processing sectors output growth.

As of the end of 2011 processing industries achieved the level of 2008, but the growth rates differ significantly by certain types of business. The recovery growth of 2010–2011 identified structural misbalances of Russian industrial sector. On one hand, the sectors which are of strategic priority for Russian economy – i.e., mineral resources extraction; food products, leather and footwear manufacturing; coke and petroleum products production; chemical production; rubber and plastic goods manufacturing; transportation vehicles and equipment manufacturing – proved their sustainability and exceeded the pre-crisis output level in 2011. On the other hand, some serious lag still exists in the recovery dynamics of mechanical engineering, electrical equipment manufacturing, metallurgy, timber production and construction materials manufacturing, where 2008 level has not been achieved yet.

Slow recovery rates in mechanical engineering constituted the dominating factor negatively impacting the level of business activity in adjacent sectors of manufacturing of structural materials and other producers' goods.

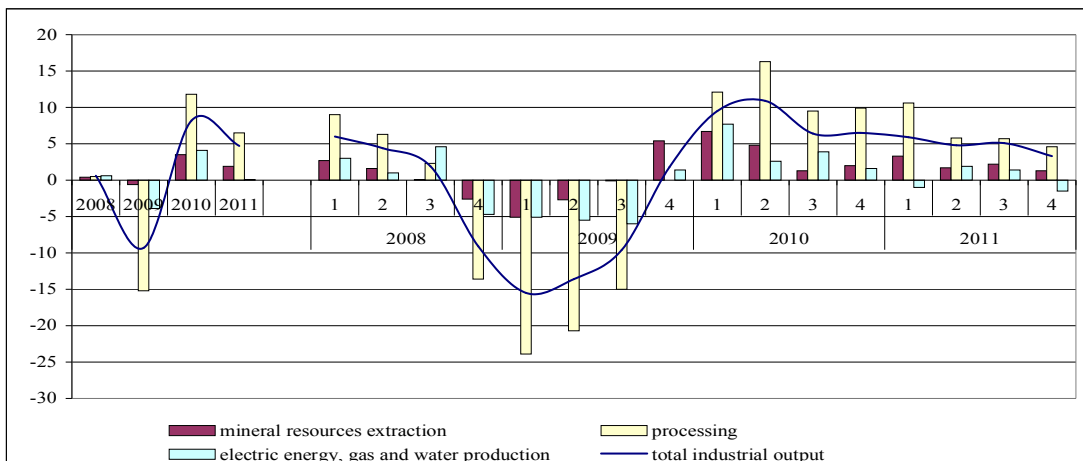
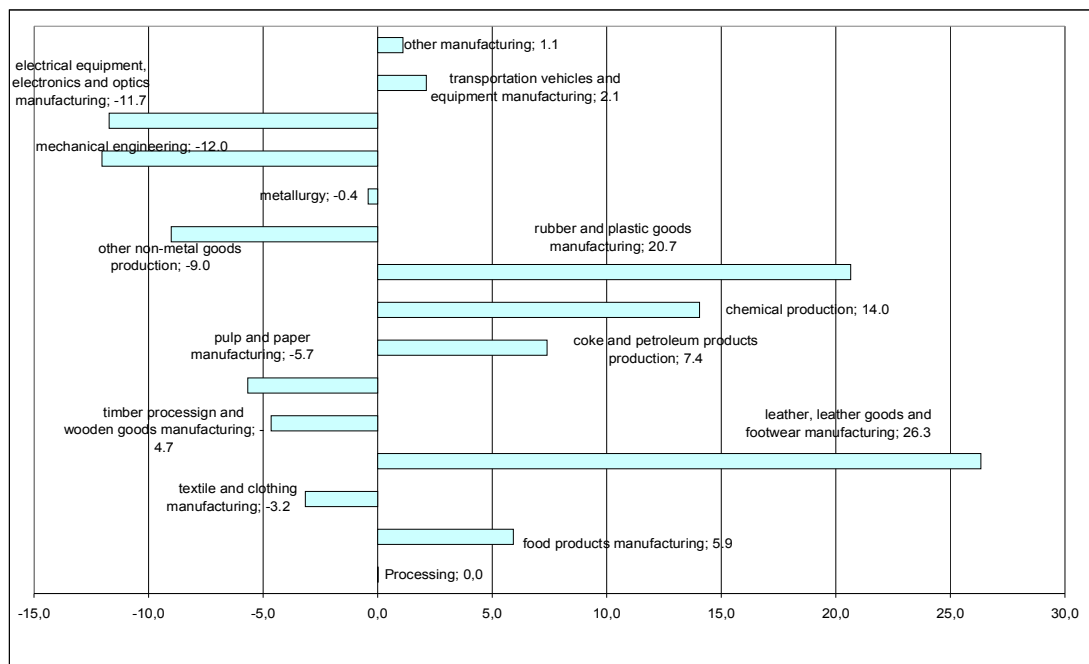


Fig. 7. Industrial growth rates by types of business and sectors in 2008–2011, % to similar period of the preceding year



Source: Federal Statistics Service.

Fig. 8. Industrial growth rates by types of business in 2011, % to 2008 level

We can discuss the specifics of post-crisis recovery in mechanical engineering only in connection with transportation vehicles manufacturing. This is determined by a big-scale government support of domestic passenger cars manufacturing and growth of foreign brands assembly lines output.

Situation with strategically important high-tech and mid-tech sectors (electrical equipment, electronics and optics manufacturing, as well as mechanical engineering) constituted one of the most serious problems. These sectors turned out to be the most vulnerable in the conditions of crisis, because the accumulated issues of poor compatibility of various types of engineering products versus imported foreign analogues judging by “value-for-money”, as well as due to lack of capacity for manufacturing state-of-the-art machinery. All of those factors significantly impeded the recovery of domestic mechanical engineering. At the same time abrupt import shrinkage took place in the crisis conditions, while as over the course of the last several years it was import which significantly impacted the pattern of mechanical engineering development and machines market.

Overestimated market positions of domestic construction and investment sector during the period of intensive growth in 2006–2008, when no adequate measures were taken to improve efficiency of capital investment, resulted in unprecedented decline in construction and structural materials manufacturing, as well as in adjacent mechanical engineering and metallurgical enterprises.

In 2011 index of machines and equipment production versus 2010 made 109.5%. Such growth is associated with implementation of measures supporting domestic manufacturers. Growth was observed for all sub-classes of this group of goods. Utilizing the resources of OJSC Rosselkhozbank and OJSC Rosagroleasing for incentivizing the demand for Russian machines and equipment for agriculture and timber husbandry, as well as increase of capital in-

vestment in agriculture resulted in accelerated production of machinery for these businesses: 37.6% versus 2010. Implementation of long-term projects in technical modernization of metallurgical, mining, oil-and-gas enterprises, high degree of depreciation and obsolescence of equipment, as well as growth of mineral resources production in 2011 contributed to 23.0% growth of machines and equipment production (versus 2010). Consistent implementation of investment programs for technology modernization of companies provided for increased effective demand for process equipment, thus determining the growth of machines production in 2011 by 14.6%, and for mechanical equipment – by 6.9% versus 2010. Incentivizing customer demand utilizing loan mechanisms went along with increase in household appliances production by 8.8% versus 2010.

In 2011 electrical equipment, electronics and optics manufacturing grew by 5.1% versus 2010. It was not sufficient to compensate for the downfall of the preceding two years. In 2011 transportation vehicles and equipment production index was 124.6% versus 2010. That was mainly determined by financial and economic stabilization of key manufacturers and customers transportation vehicles and equipment after 2008–2009 crisis.

The railway cargo turnover growth during 2011 made 5.7% versus 2010 and provided for growth of production of railway machinery used for cargoes transportation. At the same time with passenger turnover at 2011 level manufacturing of passenger railcars decreased by 2.6% during the year.

In 2011 production of passenger cars grew by 44.5% versus 2010, and trucks production grew by 33.4%. Implementation of programs to incentivize the demand for automobiles (including old cars utilization and concessional car loans programs) was a significant driver of passenger cars production growth. For trucks production similar role was played by development of mechanisms for domestic vehicles sales via leasing and loans schemes. Implementation of such programs accounted for 11.7% and 10% of total sales at passenger cars and light commercial vehicles markets respectively. However, in 2011 the share of imported passenger cars and truck in 2011 grew even more versus 2010 (51.9%, and 87.5% respectively).

The lag in recovery of production is concentrated in metallurgy, timber industry and production of construction materials. In 2011 metals and metal ware production index made 102.9% versus the preceding year including for metallurgy – 105.2%, for metal ware production – 98.2%. Non-ferrous metals production index in 2011 made 108.7% versus 2010. The growth of production yields in this sector is maintained due to growing final process stages output (118.9% versus 2010), utilized primarily in the domestic market.

In mid-2011 the overall situation in the non-ferrous metals markets got worse leading to suspension of export supplies, deterioration of financial and economic indicators of companies and enterprises' performance slide down. Despite all of that, some rehabilitation of investment activities was observed in non-ferrous metallurgy compared to 2010 – specifically in non-ferrous ores production and concentration.

Production index in timber processing and wooden goods manufacturing in 2011 made 104.0% versus 2010; in pulp-and-paper manufacturing, publishing and printing – 101.8%; for timber harvesting – 103.1%. Business activity in this sector was supported by the state. Thus, the following subsidies were granted from the federal budget in 2011: partial compensation of costs incurred by Russian exporters of industrial products when paying interest on loans received in Russian credit institutions; subsidizing interest rates on loans received by timber in-

dustry enterprises from Russian credit organizations in 2008–2009 to set-up inter-seasonal stock of timber, feedstock and fuel; subsidizing interest rates on loans which Russian companies operating in agricultural and tractor vehicles manufacturing and in timber industry received from Russian credit institutions and from Vnesheconombank in 2008–2011 for technical re-equipment for 5 years.

Construction materials production index in 2011 made 109.3% versus the preceding year. However, despite its high dynamics during the last two years, it remained 9% below the pre-crisis level of 2008. Simultaneously with expansion of scope of work in construction and growth of demand for construction materials in 2011 production growth for practically all types of goods of this sector was observed. Given the outrunning growth rates of construction materials domestic market capacity, the demand was satisfied at the expense of both re-routing cement supplies from external market to domestic market and import volumes growth.

The key macroeconomic trends analysis provides for the following conclusion: in 2011 Russian economy in general was able to recover from the crisis. In the environment of integration between Russian and global economy the 2009–2011 recovery growth illustrates the preserved dependency of growth rates on the global situation with commodities prices and demand for them in foreign markets. Respectively, quick recovery of production growth rates in export-oriented sector of mineral resources extraction provided incentives for development of domestic manufacturing sectors. However, the delayed response of domestic manufacturers to the domestic demand changes resulted in outrunning growth of import versus the domestic manufacturing recovery rates. The situation grew even more complicated due slow recovery of investment and financial crediting sectors. The inertial impact of these factors determines the system of growth limitations in the short-term perspective.