GAIDAR INSTITUTE FOR ECONOMIC POLICY

RUSSIAN ECONOMY IN 2019

TRENDS AND OUTLOOKS

(*Issue 41*)

Gaidar Institute Publishers
Moscow / 2020

UDC 338.1(470+571)"2019"
BBC 65.9(2Рос)"

R95 **Russian Economy in 2019. Trends and outlooks. (Issue 41)** / [V. Mau et al; scientific editing by Kudrin A.L., Doctor of sciences (economics), Radygin A.D., Doctor of sciences (economics), Sinelnikov-Murylev S.G., Doctor of sciences (economics)]; Gaidar Institute. – Moscow: Gaidar Institute Publishers, 2020. – 596 pp.: illust.

ISBN 978-5-93255-587-3

The review “Russian Economy. Trends and Outlooks” has been published by the Gaidar Institute since 1991. This is the 41th issue. This publication provides a detailed analysis of main trends in Russian economy, global trends in social and economic development. The paper contains 6 big sections that highlight different aspects of Russia's economic development, which allow to monitor all angles of ongoing events over a prolonged period: global economic and political challenges and national responses, economic growth and economic crisis; the monetary and budget spheres; financial markets and institutions; the real sector; social sphere; institutional changes. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts confirming the conclusions.
By contrast to the previous publications the present issue includes also a short analysis of the first three months of 2020 from the perspective of the COVID-19 pandemic impact on the Russian economy development.

Reviewer: Faltsman V.K., Doctor of science (Economics), Professor, main researcher, Department of Institutional and Financial Markets Analysis, IAES RANEPA.

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ISBN 978-5-93255-587-3

Olga Izryadnova

4.4. Fixed investment in Russia in 2019[1]

4.4.1. Investment resources

In 2019, growth rates in fixed investments amounted to 1.7 percent relative to the previous year, while the corresponding indicator a year earlier reached the level of 5.4 percent. Despite certain success in the economic recovery growth in the previous two years, the dynamics of main components of the investment activity was negatively affected by persistence of crisis developments in the construction and investment sector, where fixed investments amounted to 99.2 percent in 2019, and the construction work volume was 97.2 percent against the indicator of 2013 (beginning of investment stagnation) (*Fig. 20*).

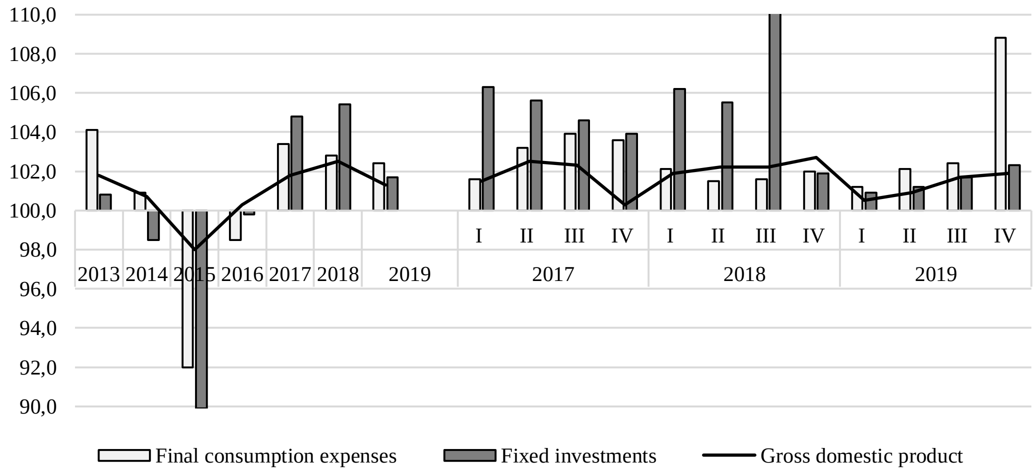

Fig. 20. Dynamics of GDP, fixed investments and volume of works in construction in 2013–2019, percent to the respective period of the previous year

Source: Rosstat.

Compared to the previous year, the pattern of investment activity in 2019 was significantly affected by a decrease in interest rates, a slowdown in the dynamics of prices for machinery and equipment, and an increase in international credit ratings to the investment level of the Russian economy. According to advance estimates by the RF Central Bank, the volume of direct foreign investments in the Russian economy amounted to $ 26.9 billion in 2019, and net private capital outflows fell to $ 26.7 billion against $ 63.0 billion a year earlier (*Table 12*).

[1] This section was written by *Izryadnova O.I.*, Head of the Structural Policy Department, Gaidar Institute, Leading Researcher of the Structural Policy Department, IAES RANEPA.

Table 12

Financial conditions for investment activity in 2014–2019

	2014	2015	2016	2017	2018	2019
Key rate (year- end), percent	17.00	11.00	10.00	7.75	7.75	6.25
International reserves of the Russian Federation (year- end), USD billion	385.5	368.0	376.3	432.1	468.5	549.8
Private sector transactions (net lending (+) / net borrowing (-)), USD billion	152.1	57.1	18.5	24.3	63.0	26.7
Direct foreign investments in Russian economy, USD billion.	22.0	6.9	32.5	28.6	8,8	26.9
Direct Russian investment abroad, USD billion	57.1	22.1	22.3	36.8	31.4	16.9*
Price index for investment purposes goods, December to December of previous year, percent	107.2	110.3	103.2	103.1	107.3	106.0
Including:						
Producers of construction products	104.6	104.1	106.6	104.9	106.5	106.6
Purchase of machinery and equipment	112.3	120.1	97.8	101.1	108.9	107.1
Official Ruble USD exchange rate (year-end), RUB/USD	56.26	72.88	60.66	57.60	69.47	61.91

* January-September 2019.
Sources: Rosstat; Central Bank of Russia.

ncome growth seen in 2016–2019, the structure of GDP registered increase of the share of gross national savings. However, the current ratio of interest rates, inflation and earning record as a whole for the period have not significantly affected the investment decision making. The share of fixed investments amounted to 17.7 percent of GDP in 2019. The share of attracted by credit institutions corporate funds in 2019 amounted to 19.8 percent of GDP and households deposits to 27.9 percent of GDP under continued high interest rates (*Table 13*).

Table 13

Main characteristics of investment sources in 2015–2019, as percent of GDP

	2015	2016	2017	2018	2019
Gross savings	27.6	26.2	26.8	31.1	31.3*
Fixed investment	16.7	17.2	17.4	17.0	17.7
Gross income and other mixed revenues	47.8	48.2	47.8	46.1	46.9
Consolidated budget revenues	32.3	32.8	33.3	35.8	35.8
Budget funds for investment	2.3	2.2	2.1	2.1	2.1
Including federal budget funds	1.4	1.2	1.1	0.6	0.97
Deposits of individuals	27.8	28.2	28.2	27.5	27.9
Corporate deposits	22.,8	19.0	19.4	20.9	19.8

* Advance estimates.
Source: Rosstat.

Resource potential of investment activity was determined by reserves and capital stock. Coefficient of renewal of fixed assets has gone up amid reduction of depreciation degree and contraction of proportion of outspent fixed assets for the whole of economy, while maintaining positive dynamics of capital stock commissioning in 2016–2018. However, this was not kept up with increased return on assets and significant change in the investment structure in fixed assets by source and by type of activity.

4.4.2. Fixed investment financing by source and by type of ownership

In 2019, financing of investment resources was dominated by own funds of enterprises and organizations. The share of investment from own funds of organizations hit maximum for twenty years monitoring period of 57.1 percent of the total fixed investment volume. The long-term financial investments decreased to 9.1 percent in the pattern of financial fixed assets against the indicator of 13.2 percent in 2018. Growing rate of own funds in financial resources of enterprises and organizations in 2019 was entailed by slowdown in increase of financial performance results for the whole of economy to 17.5 percent (66.4 percent a year earlier) and rate of return to 11.4 percent against 12.3 percent in 2018).

Participation of Russian banks in financing investment projects in 2019 was marked by reduction of the contraction of loans share by 2.5 percentage points relative to the previous year. Moreover, share of foreign loans and investments from abroad contracted to 2.1 percent (-2.3 pp against 2018) and 0.5 percent (-0.1 pp) respectively in the structure of fixed investments sources. Loans of Russian banks did not compensate the reduction of foreign loans within investment resources.

In 2019, volumes of budget funds for investment spending have insignificantly increased against reduction of the federal budget and increase of budgets of the RF subjects and local budgets (*Table 14*). At the end of 2019, financing of the federal targeted investment program from the federal budget appropriations amounted to 66 percent compared to 70.1 percent a year earlier. The federal budget expenditures for national projects in 2019 amounted to 91.4 percent (89.3 percent according to data of the “Electronic Budget” portal) or RUB 1.6 trillion vs planned indicator RUB 1.75 trillion.

This is due to the low rhythm of funding: in H1, exercising of the federal budget spending on the implementation of national projects and the comprehensive plan amounted to 32.4 percent at the end of September, with 52 percent, the major part, used in December 2019.

Table 14

Structure of fixed investments by sources of financing in 2016–2019 (less small businesses and informal activity)

	2016	2017	2018	2019
Fixed investment	100	100	100	100
Including by sources of financing: Own funds	51.0	51.3	53.0	57.1
Attracted funds	49.0	48.7	47.0	42.0
Including: Bank loans	10.4	11.2	11.2	8.7
Of which: Foreign banks loans	2.9	5.4	4.4	2.1
Russian banks loans	7.5	5.8	6.8	6.6
Borrowed funds from other institutions	6.0	5.4	4.3	4.1
Foreign investments	0.8	0.8	0.6	0.5
Budget funds	16.4	16.3	15.3	15.8
including: Federal budget	9.3	8.5	7.0	6.6
RF subjects budget funds	6.0	6.7	5.6	6.0
Local budget funds	1.1	1.1	1.1	1.3
Extrabudgetary funds	0.2	0.2	0.2	0.2
Funds obtained from shared construction (organization and population)	3.0	3.3	3.5	3.7
Including funds of population	237	2.5	2.5	2.9
Other	12.2	11.5	11.9	9.5

Source: Rosstat.

The share of Russian ownership investments in 2019 increased to 82.8 percent (in investments without small businesses and the parameters of informal activity), mainly due to an increase in the share of private Russian ownership to 50.5 percent and state ownership to 19.8 percent (*Table 15*).

The positive role of private sector in 2017–2018 was determined by dynamic growth of fixed investments, which compensated the reduction of public, mixed Russian forms of ownership and ownership of state corporations. In 2019, the situation has changed: private investments gave way to the state investments (*Table 15*). Herewith, it should be noted that structural shifts in fixed investments by forms of ownership were developed amid reduction of share of mixed Russian, foreign, and joint Russian and foreign forms of ownership.

Таблица 15

Structure of fixed investments by forms of ownership in current prices in 2015–2019

	On full range of businesses				Without small businesses and parameters of informal activity	
	2015	2016	2017	2018	2018	2019
Fixed investment, total	100	100	100	100	100	100
Including form of ownership						
Russian	84.3	83.1	83.8	85.6	81.3	82.8
State	14.8	15.2	14.4	13.8	18.3	19.8
Municipal	3	2.7	2.5	2.2	2.9	3.5
Private	56.8	55.9	58.1	60.9	49.0	50.5
Mixed Russian	8.2	7.8	7.5	7.4	9.5	7.6
State corporations	1.4	1.4	1.2	1.2	1.5	1.3
Foreign	8.3	7.4	7.4	6.2	8.0	7.9
Joint Russian and foreign	7.4	9.5	8.8	8.2	10.7	9.3

4.4.3. Fixed investments by type of capital stock

Short – term acceleration of the indicators dynamics in construction-investment activity in 2018 did not compensate the impact of the 4-years investment crisis. In 2019, the growth of construction volume constituted 0.6 percent against the previous year after 6.3 percent a year earlier. The investment structure by types of fixed assets was influenced by factors of renewal of capital stock, modernization and reconstruction of fixed assets. With a general tendency to weaken financing of construction works and services, their structure by types of fixed assets showed a steady increase in the share of costs for machinery and equipment. The increase in demand for new equipment in the majority of cases is due to critical aspects of physical depreciation and economic inefficiency in the operation of the old types of equipment.

With the implementation of projects on modernization, reconstruction and technical re-equipment, the priority area is the comprehensive re-instrumentation of production, purchasing of electronic computer technology, mechanical equipment and automation of engineering and administrative work.

Positive factor was seen in the increase of investment rate in information technology, computer and telecommunications equipment, which create conditions for further development of digital technologies. In the structure of investments by type of capital stock the share of investment in machinery and equipment in 2019 moved up to 38.5 percent in the context of exceptionally low for twenty years of statistical monitoring indicator of 31.5 percent in 2016 (*Table 16*).

Table 16

Structure of fixed investments by type of capital stock in 2016–2019, in percent to total	On full range of businesses			Without small businesses and parameters of informal activity	
	2016	2017	2018	2018	2019
Fixed investments, total	100.0	100	100	100	100
Including:					
Residential buildings and facilities	14.7	13.6	12.7	5.5	5.5
Buildings (minus housing) and facilities	44.7	43.8	43.3	48.7	44.5
Spending on land improvement				0.1	0.03
Machinery, equipment, transportation	31,5	33,7	34,6	35,4	38,5
Of which: information, computer and TV communication equipment (ICT)				3.6	4.0
Intellectual property items		2.8	3.1	41	4.3
Other	9.1	6.1	6.3	6.2	7.2

Source: Rosstat.

The slowdown in domestic production and imports of investment goods in 2019 hindered the renewal of fixed assets, introduction of new technologies, cost saving and creating new jobs.

Change in the performance of construction activity was followed by structural shifts in the use of investments by type of capital goods. The 2019 distinctive feature was the reduction of fixed investments aggregate share in housing buildings and non-housing facilities.

Following the peak of spending on housing construction seen in 2015, subsequent three years registered gradual contraction of investment percentage by this type of capital goods. In 2019, the ratio of investment in construction of buildings and facilities remained at the previous year level and constituted 5.5 percent of the total volume of investment in the economy (without small businesses and parameters of informal activity).

The development of housing construction and housing services in state and program documents is determined by priority trend for improving the quality of life and prerequisite for modernization of the social sphere and economy.

The dynamics of expenditures and their structure for housing construction is affected by both the growing demand of households and the need to reconstruct the housing stock, while reducing the share of dilapidated and substandard housing having poor chances for improvement.

In accordance with the budget parameters of the national project "Housing and urban environment for the period 2019–2024" almost half of the allocated funds are planned to be used to ensure sustainable reduction of unsuitable housing stock.

Despite the positive dynamics in resettlement of dilapidated housing and the overhaul of apartment buildings in recent years, the existing rates remain insufficient to finally resolve these problems. Important in this regard is the attraction of private and institutional investors in housing construction and the formation of effective regional overhaul systems.

A positive impact on the development of housing construction was secured by measures to promote competition and reduce administrative barriers, simplify the preparation of planning projects, develop and hold state examination of project documents, issue building permits and provide land for housing construction.

Business activity in housing construction was supported by such measures as the implementation of the program of subsidizing the interest rate on loans for purchasing housing in new buildings, the reduction of interest rates on mortgages, the implementation of mortgage programs for certain social groups at a reduced rate. Given the current level and structure of households' incomes and expenditures, the low availability to purchase housing at market prices remains the principal issue for popular majority.

In 2019, for the first time after a three-year drop, the rate of commissioning of housing climbed positive and amounted to 104.9 percent compared to the previous year indicator. At the same time, housing construction was most dynamically expanded due to own funds and loans attracted by households. In 2019, the share of living space paid by household funds reached a historic maximum of 45.2 percent of the total volume of commissioning (*Table 17*).

Table 17

Size, structure and dynamics of commissioned residential housing by developers in 2013–2019

Year	Housing commissioning, mln sq.m	Including		Structure of housing commissioning, percent to total		Rate of commissioning, percent to previous year		
		By organizations	By populations	By organizations	By population	Total	By organizations	By population

2013	70.5	39.3	28.4	55.8	43.5	107.3	106.2	106.0
2014	84.2	47.6	30.7	56.6	43.0	119.4	121.1	108.1
2015	85.3	49.5	36.2	58.1	41.2	101.3	104.0	117.9
2016	80.2	47.4	31.8	59.2	39.6	94.0	95.8	87.8
2017	79.2	45.4	33.0	57.4	41.6	98.8	95.8	103.8
2018	75.7	42.9	32.	56.6	42.9	95.6	94.5	98.2
2019	79.4	43.5	35.9	54.8	45.2	104.9	101.4	110.8

Source: Rosstat.

Changes in the living-standard-criteria, the national currency exchange rate, consumer prices and prices for construction and assemblage works as well as government measures related to supporting household incomes and the mortgage market will improve the situation in the housing market in 2020.

4.4.4. Investment activity by type of economic activity

A sharp slowdown in construction and investment activity in 2019 was registered for almost all basic types of economic activity. Fixed investments by large businesses, which account for almost 3/4 of capital investments in the national economy, amounted to 97.8 percent in 2019 compared to the indicator of the previous year. The largest decline in investment activity was registered in mining industries: 92.8 percent relative to 2018.

Structural shifts in the mining industry in 2019 were determined by the renewal of growth of investments in the extraction of crude oil and natural gas and maintaining high investment activity in coal mining. The share of fixed investments in the extraction of fuel and energy resources increased in the structure of investments for the whole to 15.5 percent (+1.1 percentage points relative to 2018) and up to 70.8 percent (+7.1 percentage points) in fixed investments and mining operations (*Fig. 21*).

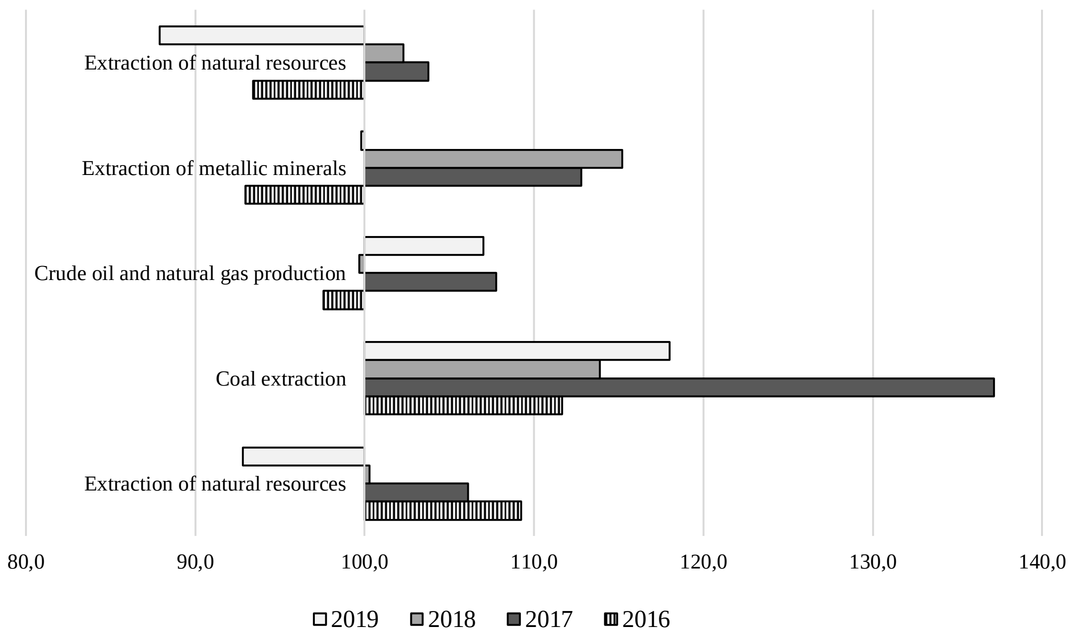

Fig. 21. Fixed investments dynamics in natural resources extraction during 2016–2019, percent to previous year

Source: Rosstat.

In manufacturing, fixed investments increased by 0.9 percent in 2019 compared to 3.6 percent in the previous year. In contrast to 2018, the positive dynamics was maintained due to the increase in construction and investment activity in the oil refining complex with the simultaneous increase in coke production (210.0 percent by 2018) and in the production of petroleum products (128.1 percent). The continued growth of fixed investments in the metallurgical complex in 2019 was supported by a change in the proportions between metallurgical production and production of finished metal products.

Amid slowdown of dynamics of the fixed investments and the volume of construction work for the whole of economy, a drop in capital investments in the machine-building complex and in the production of construction materials was recorded in 2019. In the machine-building complex, a drop of fixed investments in the production of motor vehicles by 24.3 percent, in the production of computers and electronic-optical products by 14.2 percent and electrical equipment by 17.2 percent relative to 2018, led to curbing the technical and technological renovation of these industries, as well as of other types of economic activity.

In the chemical/pharmaceutical sector, in 2019, in contrast with growth in capital investments for all sub-productions in 2018, the positive dynamics of investment demand maintained only in production of medicines (112.7 percent relative to 2018). Decline in investments in production of chemicals, rubber and plastic articles, which account for 3.3 percent of investments in economy, exceeded 10 percent (*Fig. 22*). Reduction of fixed investments in the consumer complex amid concurrent decline of investments in agriculture, is disturbing.

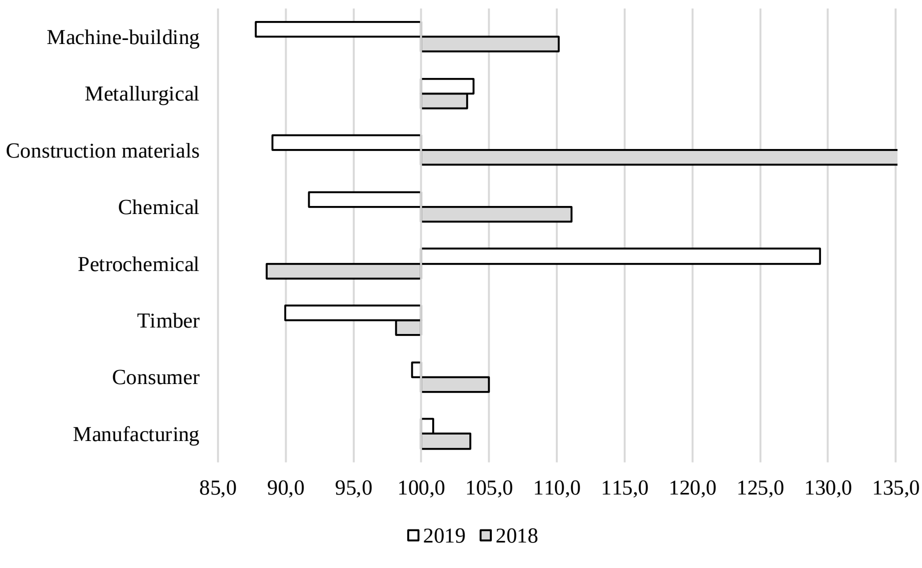

Fig. 22. Fixed investment dynamic in manufacturing industry
in 2018–2019, in percent to previous year

Source: Rosstat.

The growth of fixed investments in education activities (119.6 percent), healthcare (115.0 percent) continued in the sector of services under strengthening of social profile of investment policy in 2019. Such positive aspects as the outstripping growth of investments in the field of information and communication (115.6 percent against 2018), in professional and scientific-technical activities (115.6 percent) should also be noted. However, the decrease in investments in the development of transport and logistics (97.1 percent) and trade and marketing services (87.9 percent), especially in the context of the implementation of a comprehensive plan for modernization and expansion of the main infrastructure, is particularly alarming.

Low investment activity in 2019 and new challenges early in the year 2020, associated with an extremely unfavorable factor combination, i.e. Ruble depreciation, decline in oil prices and the need to finance emergency measures in the health sector and related economic activities, will have a significant impact on the dynamics and structure of public investment and determine the structural changes in investment activity in 2020.