

## RUSSIA'S REAL SECTOR OF THE ECONOMY: FACTORS AND TRENDS IN AUGUST 2014

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*In August 2014, the dynamics of baseline types of economic activities weakened. With stagnation of industrial production at the level of August 2013, manufacturing industries fell by 0.6%. Investments in capital assets fell by 2.7% against August 2014 and irregularities in fulfillment of jobs in the building industry became higher. Reduction of growth in households' real income and higher inflationary expectations have resulted in slowdown of the dynamics of households' consumer demand.*

In 2014, the macroeconomic situation is characterized by gradual weakening of development dynamics. In H1 2014, the GDP physical volume index amounted to 100.8%, having fallen by 0.1 p.p. as compared to the same period of the previous year. According to the estimate of the Ministry of Economic Development of the Russian Federation, in Q3 and Q4 2014 with the expected dynamics of GDP growth in the range of 0.1–0.2% the result index of 2014 will amount to 100.5% on the previous year. Slowdown of growth rates of the Russian economy is justified by a simultaneous effect of macroeconomic, institutional and geopolitical factors. Limitations justified by introduction of sanctions determined slowdown of growth in demand on goods of the Russian export and structural shifts in the import which provoked a decrease in foreign investments and a large-scale outflow of capital which situation had a negative effect on the dynamics of the ruble exchange rate and eventually resulted in growth in the rate of inflation. However, the effect of the internal factors justified by the structural specifics of the Russian economy is still more important.

The dynamics of internal demand is greatly affected by a 2.5% reduction of investments in capital assets as compared to January–August 2013. In August 2014, due to growth in the cost of credit recourses, limitation of companies' access to borrowing of funds on global financial markets and prevalence of high geopolitical risks a higher year-on-year slump in investment activities to 2.7% was registered. According to the estimate of the Ministry of Economic Development of the Russian Federation, in 2014 a decrease in investments in capital assets amounted to 2.4% as compared to the previous year.

In the 2013–2014 period, a drop in investments in capital assets has determined rather tough conditions of functioning of the building and investment complex in 2015. The forecasted growth rates of investments in capital assets at the level of 102.0% in 2015 ensures at best preservation of their physical volume at the level of the previous year, while acceleration of the

economic dynamics is possible only in case of higher efficiency in utilization of investment funds.

The main factor which underpins a positive trend of development of the Russian economy is still demand on the part of households, however, contribution of households and state management into the GDP dynamics is getting much weaker as compared to the 2012–2013 period. In the pattern of households' cash income, in January–July 2014 the share of savings amounted to 6.1%, which is 3.6 p.p. lower than a year before with growth in the share of expenditures on purchasing of foreign currency amounts to 5.5% in 2014 against 4.0% in 2013. Slowdown of income growth rates with prevailing high irregularities in distribution of income has resulted in some growth in the level of poverty.

In January–August 2014, growth in the turnover of the retail trade volume and paid services to households amounted to 2.3% and 1.0%, respectively, as compared to the same period of the previous year. From June 2014, indices of the retail trade turnover and paid services have been at the minimum level since March 2010. In August 2014, year-on-year growth rates of retail trade and paid services to households amounted to 101.4% (104.2% in August 2013) and 101.0% (103.9%), respectively. In 2014, slowdown of the retail trade turnover takes place simultaneously both in the segment of food products and nonfood products. In January–August 2014, as compared to December 2013 the consumer inflation index amounted to 105.6% and exceeded by 1.1 p.p. the same index of the previous year. In 2014, a 7.3% growth in food prices in January–August against growth of 4.4% in the same period a year before had a dominating effect on the rate of inflation. In January–August 2014, the index of prices on nonfood products and paid services to households grew at a moderate rate: 103.8% and 105.9%, respectively. The level of consumer confidence is at a record low level which situation justifies the estimate of a 1.9% growth in retail trade turnover on the basis of the results of 2014, that is, 50% of the 2013 index.

Changes in consumer demand took place in the situation of slowdown of growth rates of real income, growth in the level of households' debt on loans and acceleration of the inflation rate. In August 2014, households' real disposable cash income on a year-on-year basis grew by 3.9% (3.6% in August 2013) with an increase in the share of social payments and revenues from property in households' cash income. Real wages and salaries which account for a larger portion of households' income increased by the mere 1.4% (6.8% a year before). The effect of the budget sector on income growth weakened considerably as compared to the previous year. With a decrease in the rate of growth in real wages, there is narrowing of the gap with the dynamics of labor efficiency. According to the estimate of the Ministry of Economic Development of the Russian Federation, in 2014 real wages and salaries and labor efficiency increased by 1.5% (4.8% in 2013) and 0.9% (1.4%), respectively, as compared to the previous year.

In 2014, there is still a trend of growing demand on workforce which is measured by the number of job vacancies. In August 2014, the number of the gainfully employed population remained at the level of the previous year and amounted to 72.4m people. In May–August 2014, the number of the unemployed (according to the ILO methods) was estimated at the level of 3.7m persons, while the level of the rate of unemployment amounted to 4.8% in August 2014 and was 0.4 p.p. lower than the respective index of the previous year. Late in August 2014, 836,000 persons

were registered as unemployed with state employment agencies which figure is 2.2% and 9.6% lower as compared to July 2014 and August 2013, respectively. According to state employment agencies, employers' declared need in workers amounted to 2,198,000 persons as of the end of July 2014 and exceeded by 24% the index of 2013. As of the beginning of August 2014, the load of the unemployed population per 100 job vacancies amounted to 46.8% against 60.3% a year before. As regards the regional level, in a situation of a rather low mobility of the population the indices of unemployment are greatly diversified, but their dynamics is in line with the nationwide dynamics.

From 2012, dynamics of GDP has been greatly influenced by non-trading sectors of the economy (commerce, building, transport, market services and other) which were affected more than other sectors by slowdown of domestic demand. In that segment, stable positive dynamics was registered with the financial services sector. Also, positive dynamics prevails in the real-estate operations sector, healthcare and education.

The trading sectors (primary sector, manufacturing and agriculture) which account for nearly 50% of all the jobs and investments in capital assets remain the main sources which underpin economic growth, however, their aggregate contribution to GDP decreases gradually. In August 2014, growth in manufacturing stopped year-on-year, while as compared to January–August 2014 increased by the mere 1.3%. A positive contribution to the dynamics of economic development was made by agriculture: in August 2014 the

Table 1

**GDP DYNAMICS BY THE TYPE OF ECONOMIC ACTIVITIES IN THE 2013–2014 PERIOD  
AS % OF THE RESPECTIVE PERIOD OF THE PREVIOUS YEAR**

	2013					2014		
	Q		H1	Q		Q		H1
	I	II		III	IV	I	II	
GDP	100.8	101.0	100.9	101.3	102.0	100.9	100.8	100.8
Trading sectors								
Total	101.1	100.0	100.5	101.1	103.0	101.1	102.4	101.7
Agriculture	97.4	98.7	98.2	101.7	110.0	99.2	101.0	100.3
Fishing industry, fish farming	103.7	99.8	101.7	109.1	102.5	99.5	100.7	100.1
Primary sector	101.5	101.0	101.3	101.2	100.1	99.2	100.8	100
Manufacturing	101.2	99.6	100.4	100.7	103.0	102.5	103.6	103
Non-trading sectors								
Total	100.5	101.5	101.0	101.5	101.9	100.8	100.2	100.4
Production and distribution of power, gas and water	97.2	100.0	98.4	98.9	95.5	95.2	98.3	96.5
Building	99.7	95.7	97.2	99.2	96.9	94.7	99.6	97.7
Retail and wholesale trade	98.3	102.9	100.6	100.6	102.6	99.2	97.4	98.3
Transport and communications	101.1	100.6	100.8	100.3	102.0	99.7	101.4	100.6
Financial operations	111.0	111.4	111.2	111.9	111.8	112.7	108.7	110.7
Real-estate operations	100.8	100.6	100.7	102.5	103.5	104.3	101.0	102.6

Source: The Rosstat.

output of that sector increased by 4.6% year-on-year, which is 1.6 p.p. higher than the index of the previous year. According to the estimate of the Ministry of Economic Development of the Russian Federation, in H 2014<sup>2</sup> current trends are expected to prevail and in 2014 in general there will be growth in the volumes of industrial production (1.7%), manufacturing (2.6%) and agriculture (3.2%); as a result growth in added value in the trading sectors and non-trading sectors will amount to 1.8% and 0.2%, respectively as compared to 2013.

In H1 2014, contribution of the primary sector to GDP was 0.9 p.p. higher than the respective index of the previous year and amounted to 11.9%. Preservation of demand on the part of the primary sector industries, particularly, fuel and energy industries which form 23.4% of the volume of investments in capital assets and 28.3% of balanced financial result of enterprises and entities in the economy in general has influenced positively the dynamics of manufacturing industries and transport services. Prior to August 2014, positive year-on-year dynamics of manufacturing industries was registered.

The index of manufacturing amounted to 102.2% and 99.4% in January–August 2014 and August 2014, respectively, on the respective period of the previous year, while the index of production and distribu-

tion of power, gas and water, to 98.1% and 101.2%, respectively. Reduction of investment demand affects considerably the dynamics of functioning of machine-building and iron and steel sectors. In January–August 2014, output of machines and equipment and trucks fell by 7.9% and 20.6%, respectively, as compared to the respective period of the previous year. The situation in the machine-building sector is complicated by trends of reduction of the import of investment purpose products.

A complicated situation in manufacturing is justified by a long period of growth in production costs, too. The above situation is related both to the tariff policy of infrastructure monopolies and advanced growth in wages and salaries. In 2014, a decrease in financial results of manufacturing enterprises resulted in price changes. In January–August 2014, the index of prices in manufacturing rose by 6.4% against 1.8% a year before; it is to be noted that advanced growth as compared to average growth in manufacturing in general was registered in production of food products (109.0%), oil products (111.7%), the chemical industry (107.5%) and the iron and steel industry (108.4%).

There is modest growth in prices in the machine-building sector despite the fact that financial performance and profitability of enterprises of that sector are getting worse. ●