

RUSSIAN REAL SECTOR OF ECONOMY: FACTORS AND TRENDS IN APRIL 2015

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Russia's GDP in Q1 2015 stood at 98.1% compared to that for Q1 2014, according to the data provided by the Russian Federal Statistics Service (Rosstat). The economic dynamics in 2015 are affected by weakening domestic demand and the increased downturn in the consumer market. The retail turnover index in April 2015 stood at 90.2% and fixed investments at 95.2% compared with that for the corresponding period last year. The economic situation has been deteriorating through a 13.2% decline in real wages and a 8.4% increase of unemployment rate compared to that for April 2014.

According to the Rosstat data, Russia's GDP in Q1 2015 saw a 1.9% decline compared with that for the corresponding period last year. This is the first time since 2009 that GDP has declined synchronous with a contraction in retail turnover and fixed investments. In April 2015, retail turnover stood at 90.2% (92.5% in January–April same year) while fixed investments were 95.2% (96.3%) compared to that for the corresponding period last year.

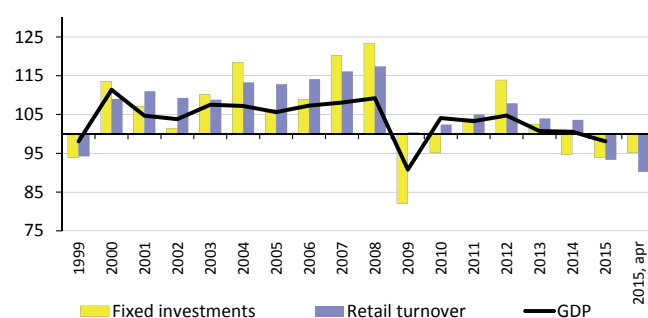
It is worthwhile noting that the current situation is characterized by a deeper than investment demand downturn in the consumer market. Such a ratio of the dynamics of investment and consumer demand was observed only at the acute phase of the crisis in the first half of 1999, when an unprecedented decline in personal income and consumption constriction turned to be the key constraining factor for economic growth, despite gradual recovery in the construction and investment sector. During the crisis developments facing Russian economy in Q1 2009, as distinguished from the crisis situation a decade ago, GDP fell chiefly by a contraction in fixed investments. Positive dynamics of real personal disposed income kept up a timid growth in the consumer market at the onset of the crisis and gave some extra push-up to economic recovery growth in 2010.

In Q1 2015, the implications of drastic devaluation of the ruble in November–December 2014 and still high inflations rates resulted in a slump of personal income and household consumption. The retail turnover downturn by market segment has been increasing since January 2015. In April 2015, the food market turnover saw a decline of 8.9% while that of nonfood market dropped 10.7% compared to that for April 2014. The Consumer Price Index in April 2015 stood at 116.4% on an annualized basis, real personal income at 96.0% and real wages at 86.8%. The real amount of accrued pensions in Q1 2015 dropped 4.1% compared to that for the previous year. The share of wages of the personal income structure increased, whereas that of social payments and property income declined, with personal

income as a whole declining. The developed dynamics of living standard parameters may lead to higher risks of deteriorating poverty headcount, which may turn to be the first since the crisis of 1998–1999 substantial boost in the poverty rate, because the anti-crisis measures adopted in 2008–2009 resulted in some growth of disposed personal income and allowed an adverse scenario of social developments to be avoided.

In 2015, the situation in the domestic market is deteriorated by the increased downtrend in fixed investments which has been prevailing for the recent five quarters. Alarming in particular is the contraction in January–April 2015 of fixed investments by 3.8% and scope of works in construction by 4.8% compared to the corresponding period last year, because negative dynamics of the foregoing indices developed at that time. The lowering of the central bank key interest rate to 14% in March 2015 and then to 12.5% in May is likely to have an effect on construction and investment early in the second half of the year¹.

A positive factor supporting the Russian economy in 2014 – early in 2015 was net exports whose dynamics were determined by a deeper decline in imports than



Source: Rosstat.

Fig. 1. The dynamics of GDP, fixed investments and retail turnover in Q1 1999–2015, by percentage compared to the corresponding period last year

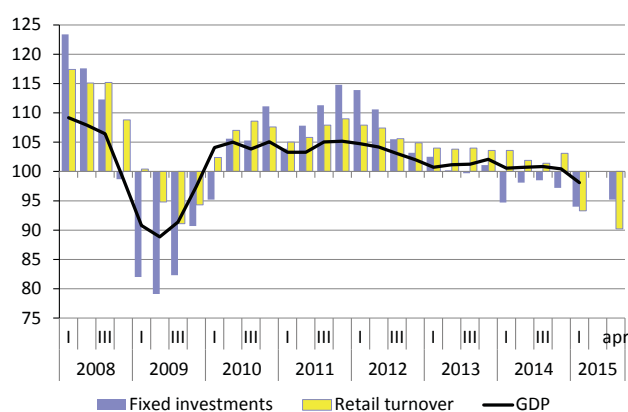
1 Model calculations of short-term forecasts for socio-economic figures of the Russian Federation. "Gaidar Institute Newsletter.ru" No.(86). P. 3–7.

exports, which was typical of the crisis situation in 2009.

The persisting external demand has made it possible to take advantage of the deep devaluation of the ruble, which is not the case with the domestic market, where such advantages were limited by drastic contraction of domestic demand. Export-focused industrial enterprises increased physical volumes of their exports while retrenching internal production costs, thereby boosting the return on exports even amid substantial fall of external prices. In Q1 2015, this also supported production growth of mineral extracting and manufacturing enterprises operating in the energy, metallurgic and chemical complexes, compared to the corresponding period last year.

However, with the weakening effect of devaluation and dynamics of foreign trade turnover, the situation in the manufacturing sector began to gradually deteriorate while the output in April dropped to 7.2% compared to that for April 2014, reaching the highest value since 2010. It can be assumed that the dynamics were caused by the strengthened real effective ruble exchange rate against foreign currencies, by 8% in March and 22% in April compared to that for December 2014. Although the ruble appreciation weakened the advantages of mineral extracting enterprises in external markets, it resulted in a domestic market upturn¹. The nature of economic downturn in 2015 differs substantially from that in 2009 as to the basic types of economic activity. While 2009 saw a deep decline in the industrial sector, transport turnaround and scope of construction works, in 2015, the industrial sector was found to be more responsive to new trends, whereas wholesale/retail sales and construction turned to be the key guides towards lower output of the basic types of economic activity. What is more, the situation in these sectors was deteriorating since the beginning of the year. As a result, in March 2015, the output index on the basic types of economic activity went out beyond 99–102%, the range it was throughout the period of 2013–2014, and decreased 2.3%².

The contraction of domestic demand determined the industrial production dynamics. Industrial production dropped 4.5% in April 2015, 1.5% in January–April, compared to that for the corresponding period last year. While the industrial sector's operating features in January–March 2015 were determined by the



Source: Rosstat.

Fig. 2. Industrial production indices by type of economic activity in 2012–2015, by percentage compared to the corresponding month last year

persisting positive dynamics in mineral extraction, the trend changed in April: for the first time over the past two years the sector saw a 0.8% decline compared to that for the corresponding month last year.

It is worthwhile noting that the production of fossil fuels showed a 0.1% increase in April 2015, as well as the production of crude oil increased 1.2%, whereas other segments of mineral extraction saw a 1.4% decline for the first time over the recent 13 months. The decline resulted chiefly from almost a ¼ decline in the production of minerals used for manufacturing construction materials, which was caused by weaker demand from the construction and investment complex.

Only two types of economic activity in the manufacturing sector saw positive dynamics in April 2015: the production index was 101.8% on an annualized basis for the manufacture of coke and petrochemical products and 103.6% for the manufacture of chemicals and chemical products. The manufacturing sector was governed by domestic factors. The downtrend towards investment resulted in further decline in production in the machine-building sector, by type of economic activity. Manufacture of machinery and equipment stood at 85.1% compared to that for April 2014, manufacture of means of transport at 77.8% compared to the same period. It is worthwhile noting that the dynamics of manufacture of means of transport and transport equipment were adversely affected by a 22.3% decline of output in the manufacture of motor vehicles and 21.0% in the manufacture of vessels, aircraft, compared to that for the corresponding month last year. The decline in output of final demand products determined a decline in output of intermediate consumption products – manufacture of electric, electronic and optical equipment dropped 0.7%.

The manufacture of consumer goods in April 2015 also saw the continuing downtrend in production.

1 Rogov K. Real sector has no more advantages from the devaluation. OMES No. 8, 2015. <http://www.iep.ru/ru/publikacii/7497/publication.html>

2 Izryadnova O., Rogov K. The economy enters a crisis the other way around. OMES No. 6, 2015. <http://www.iep.ru/ru/publikacii/7423/publication.html>

For example, the manufacture of food products in April 2015 stood at 99.4% compared to that for the previous year, while growth rates were at 103.5% throughout the entire first quarter. While 2015 shows a higher positive contribution of an increase in the manufacture of agricultural products (up 3.5% in April 2015 over that for the previous year¹), it should be taken into account that the dynamics of agricultural processing plants weakened not only because of weaker domestic demand, but also the appreciation of imported materials, equipment and raw materials which are not produced by Russian industrial enterprises, and may interfere with further development.

Having encountered effective demand constraints, manufacturers of industrial products adjusted their pricing policy. The producer price index in the manufacturing sector in April 2015 was 100.7% compared to that for the previous month, with a 103% average

¹ For more details on the dynamics of agricultural production see OMES No. 8, 2015. <http://www.iep.ru/ru/publikacii/7497/publication.html>

monthly price rate change in the period between January and March 2015.

The labor market was facing a greater stress as a result of declining production rate in the economy. The unemployment rate (calculated using the ILO method) in April 2015 increased 8.8% to 4,5 million persons (5.8% of the economically active population) compared to that for the corresponding period last year; employment agencies registered 1,0 million of unemployed persons, up 1.5% compared to that for March 2015. The employment issues have come to the forefront, given that salaries of employees make up the income of almost 80% of the population. According to public employment agencies, however, the demand for labor force in March 2015 was 1,212,000 persons, 472,000 less than that for March 2014. At the same time, the load of the unemployed registered with public employment agencies upon 100 vacancies for the same period increased by 1.5 times to 100,7 persons in March 2015. ●