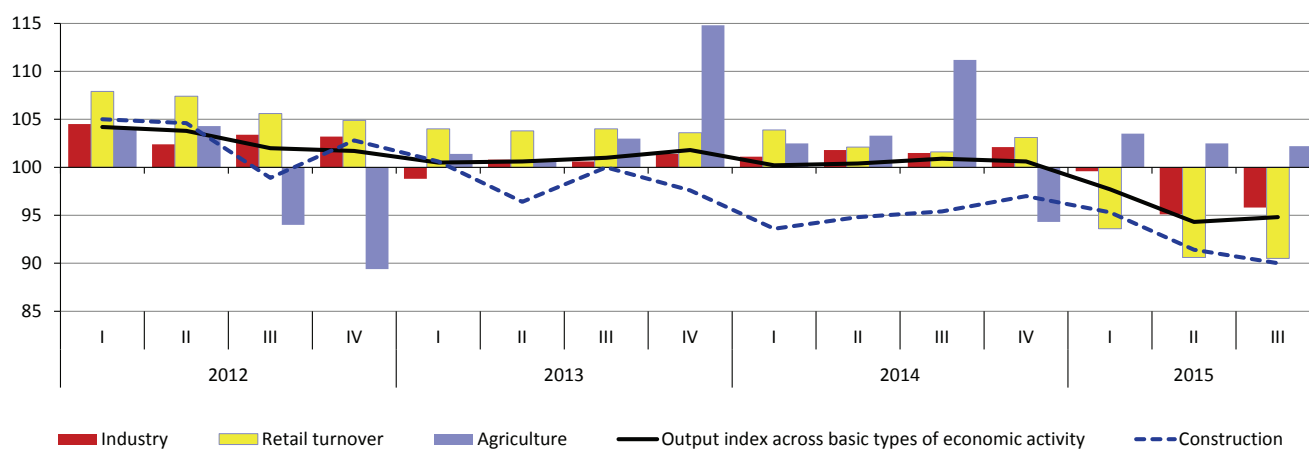


## THE REAL SECTOR OF THE RUSSIAN ECONOMY: FACTORS AND TRENDS IN JANUARY–SEPTEMBER 2015

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*In January–September 2015, the Russian economy posted shrinking domestic and external demand. In September 2015, the domestic market was negatively affected by decrease of investment in fixed assets by 5.6% and the fall of retail turnover by 10.4% against the corresponding period of the previous year. In Q3 2015, the situation was accentuated by the industrial slump by 4.3% including in processing industry by 5.4% against the same period last year.*

*Decrease of the real wages by 9.3% amid general unemployment growth by 6.8% and the registered one by 14.7% represented an alarming symptom in September 2015 against September 2014.*



Source: Rosstat.

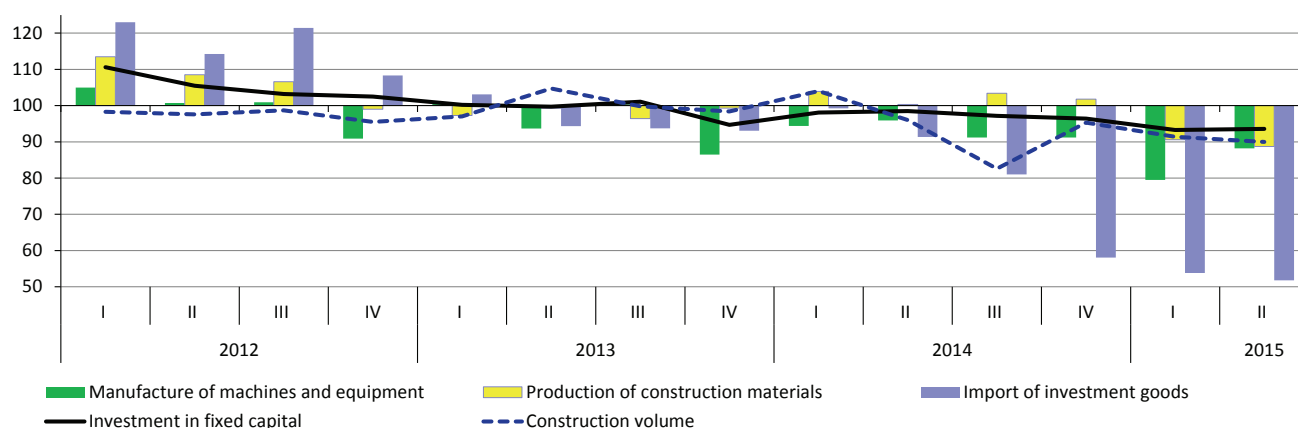
Fig. 1. Dynamics of basic types of economic activity in 2012–2015, in % to the corresponding period of the previous year

Slowdown of quarterly economic development dynamic during last three years was accompanied by slow rates of industrial production, retail turnover and construction-and-investment complex. In January–September 2015, for the first time since 2008–2009 crisis, the fall of output volume index was registered across basic types of economic activity compared to the previous year, meanwhile quarterly output dynamics was falling. If in 2014, unstable indicators of the investment activity was partly compensated by positive dynamics of retail turnover, industrial and agricultural production, than in January–September 2015, consumer and investment demand were falling simultaneously with industrial production recession. In January–September 2015, the Industrial Production Index constituted 96.8%, construction work – 91.7% and retail turnover – 91.5% against the corresponding period of the previous year. Output reduction in the real sector of the economy has resulted in the contraction of demand for infrastructure services: freight turnover fell by 1.1%, volume of paid services rendered to the population – by 1.9% in comparison with January–September 2014. Agricultural output

growth by 2.4% was the only one positively affecting the economic outlook this year compared to January–September 2014.

Rube depreciation, households' high level of indebtedness and inflation spiral have led to the reduction of households' income and consumption contraction. Contraction of gross fixed capital formation and reduction of stocks have negatively affected the decrease of the GDP reduction rates. In January–September 2015, investment in fixed capital came to 94.2% against this indicator a year before amid growing decrease in the construction-and-investment complex quarter-on-quarter.

Restrictions on borrowing assets from abroad and domestic high interest rates have remained major factors of slowing down the investment processes. Investment into fixed assets mainly happens at the expense of proper assets of enterprises and state financing. Despite growth of financial results of enterprise activity by 1.23 times compared to January–September 2014 and increased share of gross revenues to GDP by 2.1 p.p. against H1 2014, enterprises and the banking sector highly reservedly implement



Source: Rosstat.

Fig. 2. Dynamics of indices in construction-and-investment complex in 2012-2015, % to corresponding period of last year

and finance investment programs due to unstable outlook of domestic market. Share of investment in fixed capital as of the period-end for H1 2015 amounted to 14.6% of GDP.

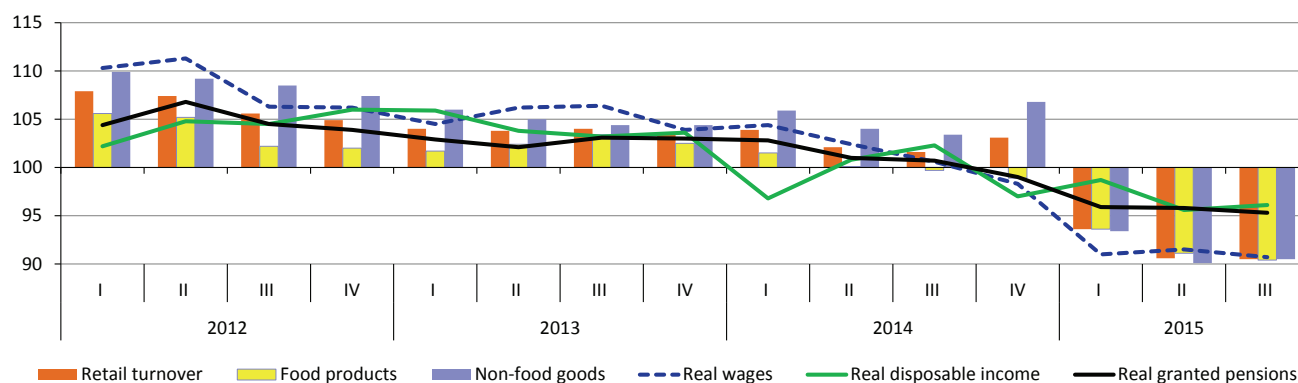
The fall in the investment demand has been observed since mid-2012 and has been accompanied by a contraction of manufacture of domestic machines and equipment, import of investment goods as well as construction materials. In January–September 2015, manufacture of machines and equipment shrank by 14.4%, manufacture of construction materials down 6.5% against the corresponding period of the previous year. Simultaneous contraction of manufacture and import of machines and equipment highly negatively affects the implementation of investment projects on modernization, in particular in the oil and gas extraction.

Contraction of industrial facilities construction since Q3 2014 have resulted in the fall of the overall volume of construction. Meanwhile, in Q3 2015, additional factor for a reduction of business activity in the construction sector for the first time in last ten quarters was a

decline of the new housing supply by 6.2% against the corresponding period of the previous year.

In 2015, a decline of the households' final consumption is registered against indicators of last year. Escalation of recession in consumer demand was determined by a fall of the population's income in the course of recent four quarters. In January–September 2015, real income of the population came to 96.7%, real wages – 91.0% and real granted pensions – 96.0% against the corresponding period of the previous year. The reaction of the population to the fall of their income was a contraction of demand of food products by 8.3% and on non-food goods – by 8.6% against January–September 2014. Amid uncertainty households' consumption behavior is undergoing a change: the population tends to save amid contraction of expenses on current consumption. In January–September 2015, a share of savings in the money income of the population constituted 13.2% against 6.4% a year earlier.

Decline of the real wages in real disposable income in 2015 has led to an increase in the poverty level: according to the estimated of the Ministry of Economic



Source: Rosstat.

Fig. 3. The Movement of Retail Turnover and real Income of Population in 2012–2015, % to the corresponding period of the previous year

Development in 2015 as a whole the poverty level went up to 13.2% of the overall number of population.

Dynamics of the domestic demand since the turn of 2014 was in the red, however, this year it complicated by simultaneous fall of domestic production of goods and services and imports. Import pattern has been changing under the impact of a far deeper fall of supplies of consumer and investment goods against commercial goods.

In January–September 2015, deeper recession in industry was determined by a contraction of manufacturing output by 6.4% against the same period of last year. To note, that by all types of activity in manufacturing production a deeper recession has been registered this year and in the most acute form it has affected hi-tech complex of machine building. In January–September 2015, extraction of natural resources up 0.3% against last year. Outstanding feature of 2015 was the fall of output both in tradable and non-tradable sectors of the economy.

During January–September 2015, total number of unemployed up 6.8%, and the number of officially registered unemployed up 7.9% of the corresponding indicators of 2014. Despite a fall of economic movement, the total level of unemployment barely moved away from the low bottom for the entire history of the indicator. In September 2015, the level of general unemployment amounted to 5.2% of the economically active population. Requirement of the employees in workers registered in the state employment service has remained below the indicators of the last year. Russian practice demonstrates the fact that in crisis situations labor market adjustment happens mainly in the form of wages reduction, part time employment and increased employment in the informal sector of the economy.

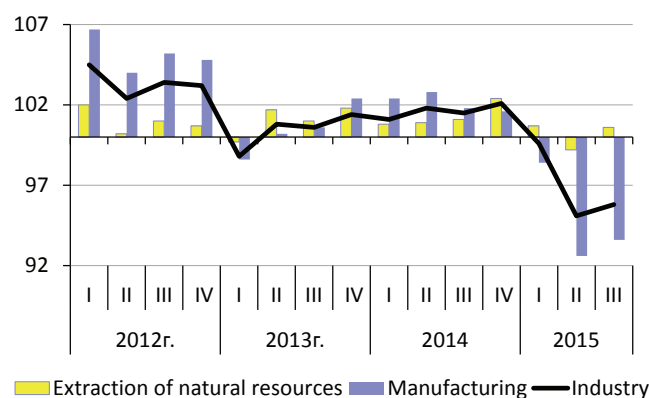
According to the Ministry of Economic Development estimates, expected GDP contraction in 2015 will come to 3.9%, investment in fixed capital – 9.9%, retail turnover – 8.5% and industrial production – 3.3% against last year. These projections have been put in the basis of “Forecast of Socio-economic Development of the Russian Federation for 2016 and for the planned period 2017–2018”. According to the forecast, the effect of the negative factors will remain. These negative factors are determined by low crude oil prices and restrictions in the import of goods and technologies. However, formation of compensating factors and con-



\*Estimate.

Source: Rosstat.

Fig. 4. Dynamics of domestic demand by components in 2012–2015, % to the corresponding period of the previous year



Source: Rosstat.

Fig. 5. The Movement of industrial production by type of economic activity in 2012–2015, % to corresponding quarter of previous year

ditions are projected: adaptation of the economy to the restrictions in import of goods, reduction of costs, release of inefficient capital and increase of domestic goods competitiveness. The effect of these factors should manifest itself in the positive GDP dynamic recovery. It is projected that in 2016 GDP growth will amount 100.7%. In the meantime, final consumption of the population will be growing at moderate rates on the back the reduction of main standard of living characteristics. Investment in fixed capital in 2016 will keep contracting and their share will come to 18% of GDP against 18.4% in 2015. In this situation as in 2015 net export will remain the factor which will support the economy. ●