

AUSTERITY: A TREND ACROSS RUSSIA'S REGION¹

N.Zubarevich

The year of 2015 was marked by a few troublesome trends in the crisis unfolding in Russia's regions. The overwhelming majority of Russia's territories ran a budget deficit while regional and municipal debts were piling up. A new trend towards drastic shrinking of consumption took hold. Furthermore, investment continued to decline for three consecutive years. On the other hand, the industrial sector downturn was moderate and geographically localized, and the unemployment rate continued to grow at slowest pace. The outlook for 2016 is negative: the adverse trends are expected to worsen.

Budget disequilibrium and huge debts remained the principal (unaddressed) problem facing Russia's regions: 77 regions ran a budget deficit in 2013, 75 in 2014, 76 in 2015. Most of the top-ranked oil-and-gas producing regions and federal-status cities ran a budget surplus (*Fig. 1*). The total amount of regional budget deficit in 2015 dropped to Rb 171bn (Rb 642bn in 2013, Rb 448bn in 2014) mostly due to a huge surplus of Moscow's budget (Rb 144bn in 2015). Excluding the nine regions with budget surplus, the rest of the regions ran a total of Rb 370bn in budget deficit. Many regions endeavoured towards thrifting: consolidated budget expenditure increased mere 1%, income raised 6%.

The total amount of regional and municipal debts in 2015 increased 11% to Rb 2.66 trillion as of 1 January 2016 (3.3% of GDP), accounting for 35% of the regional tax and non-tax consolidated budget revenues (excluding transfers). The debt problem remained unaddressed while the Finance Ministry nearly doubled (from Rb 160bn to Rb 310bn) the amount of super cheap budget loans for regions, but failed to make a serious contribution to improving the debt structure which continued to have a large share of expensive loans from commercial banks (44% as of 1 January 2016).

The budget system saw further destabilization because the 2015 federal budget ran a deficit (nearly Rb 2 trillion or 2.5% of GDP). Risks worsened, especially for the regions, which depend heavily on government grants, making up almost 2/3 of Russia's regions. In 2015, transfers to regions contracted by about 3% (although excluding Crimea, they remained unchanged), and the federal support to the regions in 2016 may weaken substantially.

The **drastic consumption downturn** was the second major problem in 2015, which was determined by a decline in personal income and wages by 4% and 9.5% respectively. A new trend towards drastic contraction in retail sales emerged in 2015, consumption was declining two times faster than personal income. The Russians in 2015 switched to an "austerity mode" after realizing the crisis could continue for long. Geographical differences in the retail sales dynamics between the regions can be explained mostly by statistics drawbacks, especially for the North Caucasus Republics, Zabaykalskiy Territory and

¹ This paper was originally published in Online Monitoring of Russia's Economic Outlook No.3(21).

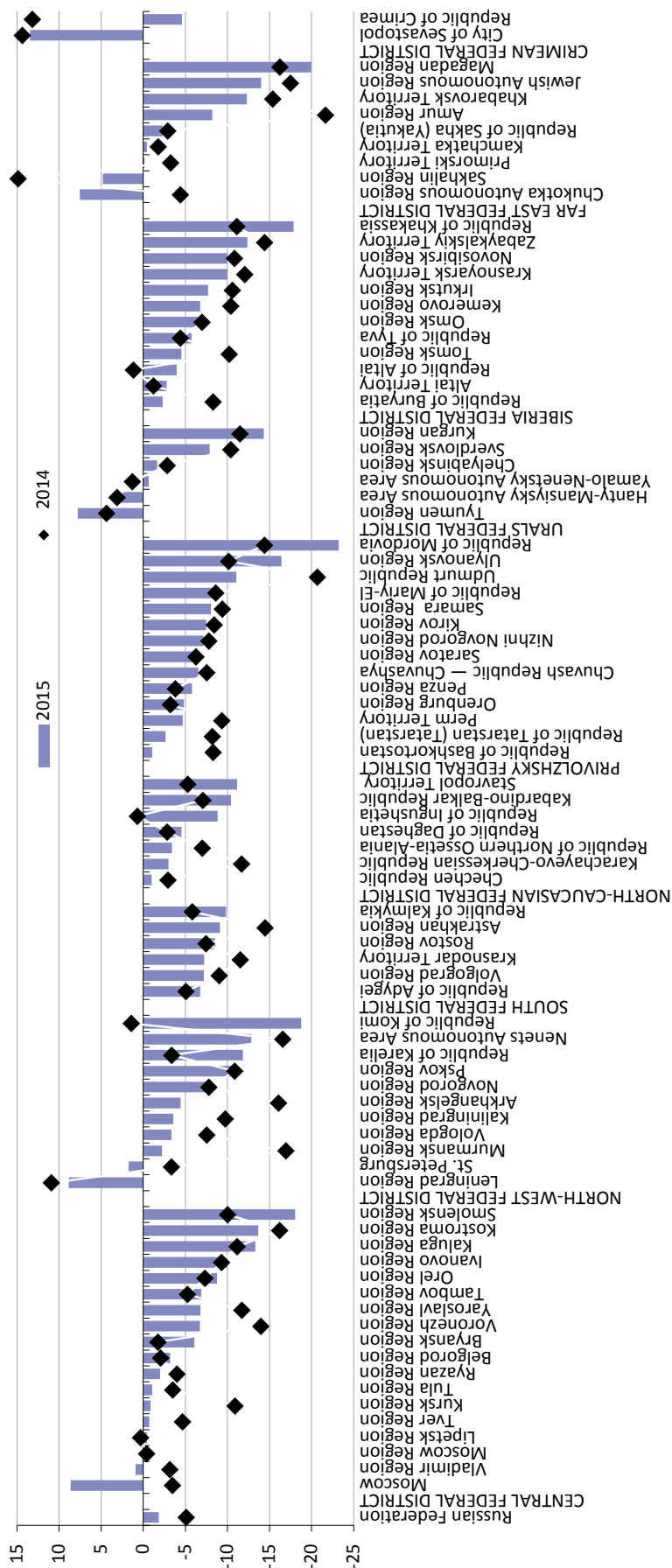


Fig 1. Budget deficit, as a percentage of a region's consolidated budget revenue

Far East Federal District, where bazaars make up a larger share of the overall sales. The Central, North-western, Southern, Volga, Urals Federal Districts, as well as most of the Siberian Federal District, saw a sweeping and severe decline in consumption (*Fig. 2*). The regional dynamics of personal income (according to the data for 11M 2015) is mostly similar to the consumption dynamics: with an average decline in personal income by 5%, the dynamics fell more steeply in the Central, North-western, Volga, Urals and Siberian Federal Districts. Only seven regions were reported to face no decline in personal income, which is most likely due to statistics drawbacks.

The **growing investment downturn** (for three consecutive years) is the third severe problem. The data for the three quarters of 2015 show that investment fell nearly 6% at a wide range of enterprises and organizations of 51 regions including many advanced regions, except new oil and gas areas (Sakhalin Region, Krasnoyarsk Territory, Nenets Autonomous Area), Hanty-Mansiysky Autonomous Area (the key oil producing region), as well as Moscow, Tatarstan, Bashkortostan, Belgorod, Voronezh, Novgorod, Orenburg, Ulyanovsk regions, and some other regions. The data for 11M 2015 (for large and medium-sized enterprises and organizations) show investment dropping even worse (9.5%) in 60 regions. Positive dynamics were reported basically in the same regions as before, except Moscow with zero dynamics. Economically advanced regions such as Kemerovo, Nizhniy Novgorod, Kaluga, Yaroslavl, Sverdlovsk and Chelyabinsk faced the deepest decline in investment (down 24–37%). The investment dynamics also reveals the failure to “go eastward”: investment continued to decline in half of the regions of the Far East Federal District, including all the major areas, namely the Khabarovsk Territory (down 33%), Primorsky Territory (down 5%), Yakutiya (down 2%).

Typical trends, such as industrial production downturn and rising unemployment rate, were less or even feebly marked in the course of this crisis. The **industrial production downturn** was not only moderate (3.4% in 2015) but also geographically localized, hitting only 36 regions. Although the manufacturing industry saw a deeper decline (5.4%), it faced only half of the 43 regions. The differences in the industrial production dynamics between regions developed in H1 2015 and continued till the end of the year, because they are determined by industry's sector-specific specialization.

An increase by one-third of federal defence spending contributed to the growth in defence industry regions (Bryansk, Tula, Yaroslavl, Penza and Kirov regions, Republic of Mari-El, etc.), although growth rates were slower than those seen in H1 2015. Industrial production increased in advanced agricultural regions, especially in the Black Earth Region and the South Federal District, because foreign competitors had left the market. Industrial growth continued in the key oil and gas producing regions, especially new ones (Sakhalin Region, Nenets Autonomous Area, Irkutsk Region, Yakutia), except the Hanty-Mansiysky Autonomous Area (down 2.5%) facing the downturn for two consecutive years. It is difficult to explain fantastic industrial growth rates in the Rostov Region (55%) even by a combination of all the three advantages deriving from its specialization (a new oil refinery kicked off, adding to defence enterprises and advanced food industry).

The regions facing the deepest economic slump were the same as in H1 2015, namely automotive industry regions (Kaluga and Kaliningrad regions, down 7–9%), semi-depressed regions with non-competitive industries that tend to be hit hardest by any crisis (Ivanovo, Kostroma, Tver

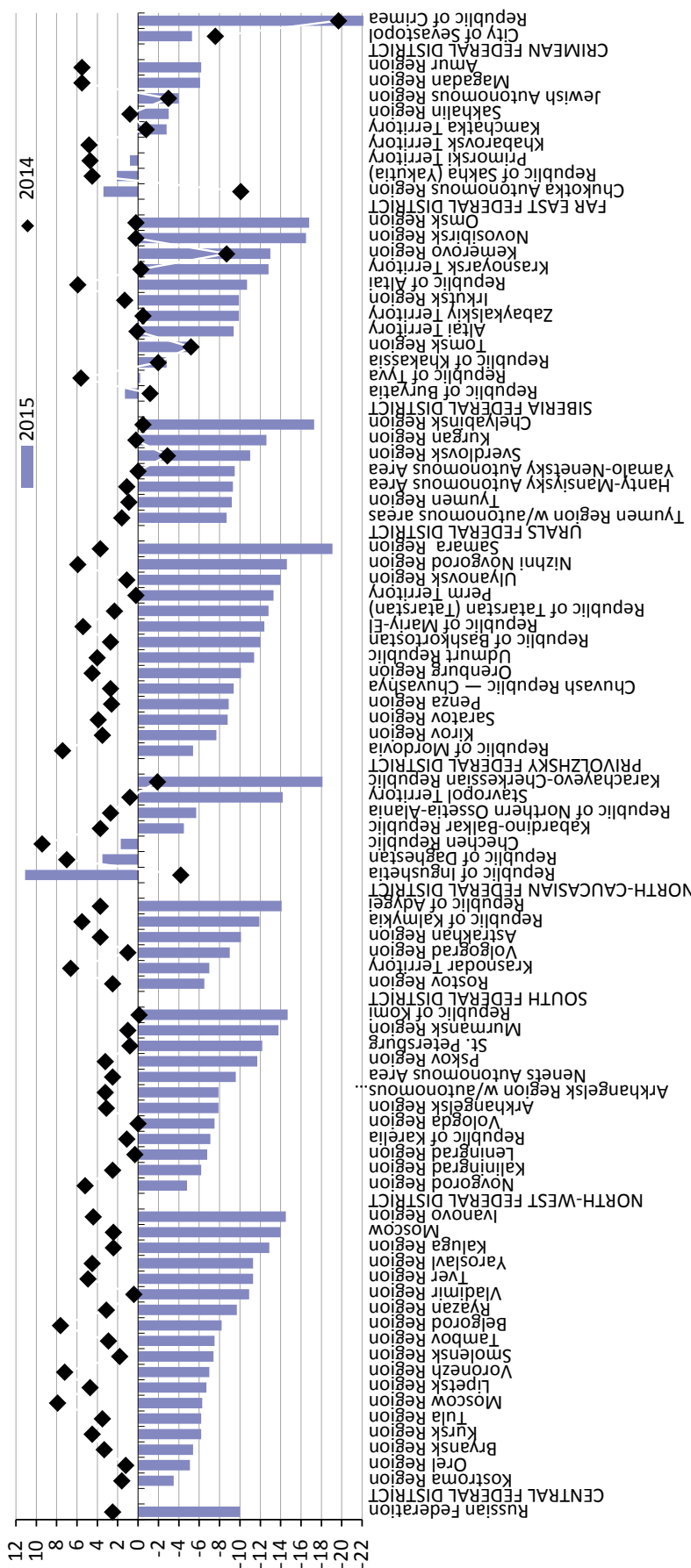


Fig. 2. Retail sales dynamics, % year-over-year

regions, Republic of Mordovia, Chuvash Republic, Amur Region and Jewish Autonomous Region, down 6–9%), as well as federal status cities (5–7%), where the crisis tends to boost deindustrialization processes. The slump of the Orenburg Region (8%) was partially determined by a tax manoeuvre in the oil industry, which rendered oil refiners loss-making, and the slump of the Primorsky Territory (down 12%) was caused by the downturn in the car assembly industry. 2016 faces high risks of the industrial downturn spreading out geographically in response to the decline in investment and effective demand.

Unemployment saw the slowest pace of growing in 2015, from 5.2% in October–November 2014 to 5.7% in October–November 2015. Furthermore, regional unemployment underwent small changes, except Vladimir, Yaroslavl, Vologda regions, Republic of Komi, Udmurt Republic, Republic of Buryatia and Republic of Khakasia, where it increased markedly (2–3 percentage points) but still remained relatively low. The crisis in regional labour markets has so far been following the pattern of slowly growing unemployment. According to the data for the three quarters of 2015, the regions facing the sharpest industrial downturn, namely Kaluga, Tver and Ivanovo regions (5–6% of the workforce), showed a bigger share of underemployment, forced downtime, or leaves without pay. Industrial regions such as Chelyabinsk and Sverdlovsk regions (10–12% of the workforce), as well as Republic of Buryatia, showed a bigger than normal share of leaves of absence without pay.

The unemployment issues are alleviated not only by using widely the underemployment mechanism but also the demographic factor – the low-numbered generation born in the 90s have been entering the labour market. Another mitigating factor is the reducing number and partial outflow of labour migrants of post-Soviet states, who were employed mostly in the construction and retail sectors. It is this factor that contributed to taming unemployment amid the sharp slump in these industries.

Overall, 2015 can be divided into two periods – the crisis-driven decline in the first 5–6 months and the following stagnation at a lower level until the end of the year, although the situation in the regions and the dynamics are more complex. The outlook for 2016 is negative, investment and personal income are expected to decline further due to, among other things, a new round of the rouble devaluation in January 2016, more regional economies are anticipated to decline further or stagnate at a lower level, the growth in the defence industry regions is foreseen to come to an end because of growing federal budget problems, and budget spending is expected to be streamlined even faster. Austerity is going to be a nationwide trend regardless of geographical differences. ●