

RUSSIAN INDUSTRY IN H1 2016: ZERO DYNAMICS¹

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The trend that first became visible in early 2016 – decline giving way to zero rates of growth – towards the end of H1 had spread across a majority of segments of the economy's real sector. The lack of a noticeable domestic demand and dependence upon foreign equipment supplies coupled with the persistently low relative income generated by exports of raw materials make it impossible to expect any significant domestic production growth in the near future².

In spite of the temporary deterioration of the terms of trade in late 2015 – early 2016, no significant decline in the main sectors of Russian industry could be observed over the course of H1, in contrast to the situation in late 2014³. Rather, the statistical data for early 2016 indicated that the period of a relatively high output volatility in the real sector was over, possibly to give way to the period of a near-zero growth rate⁴. This change was caused by the absence of additional negative factors – in 2014 these had been the introduction of economic sanctions against Russia and Russia's retaliatory sanctions, the events in Ukraine, and the expectations of further deteriorating terms of trade. Besides, late 2015 was a period of gradual stabilization in the economy and adaptation of businesses to the new realities – among other things, by adjusting their business plans and investment projects.

The currently available Rosstat's data⁵ applied by the Gaidar Institute for the purpose of decomposition and removal of the trend component in its by-sector time series analysis⁶ have provided an answer to the question as to how sustainable the trend that first became visible in Q1 actually is (output stabilization and zero growth rates in the majority of segments of the real sector).

The results of our calculations demonstrate (*Fig. 1*) that on the whole, the situation in industry over Q2 2016 remained stable, while at the same time a slow decline of the Industrial Production Index (IPI) could be observed (99.5% in July on March 2016).

Similarly to the situation in Q1, the production indices in different sectors still vary across Russian industry, but their values are becoming increasingly uniform and starting to display zero growth rates (*Table 1* and *Fig. 2*).

Among the sectors that over recent months have been displaying positive growth rates, however small, we may point to mineral extraction; textiles and

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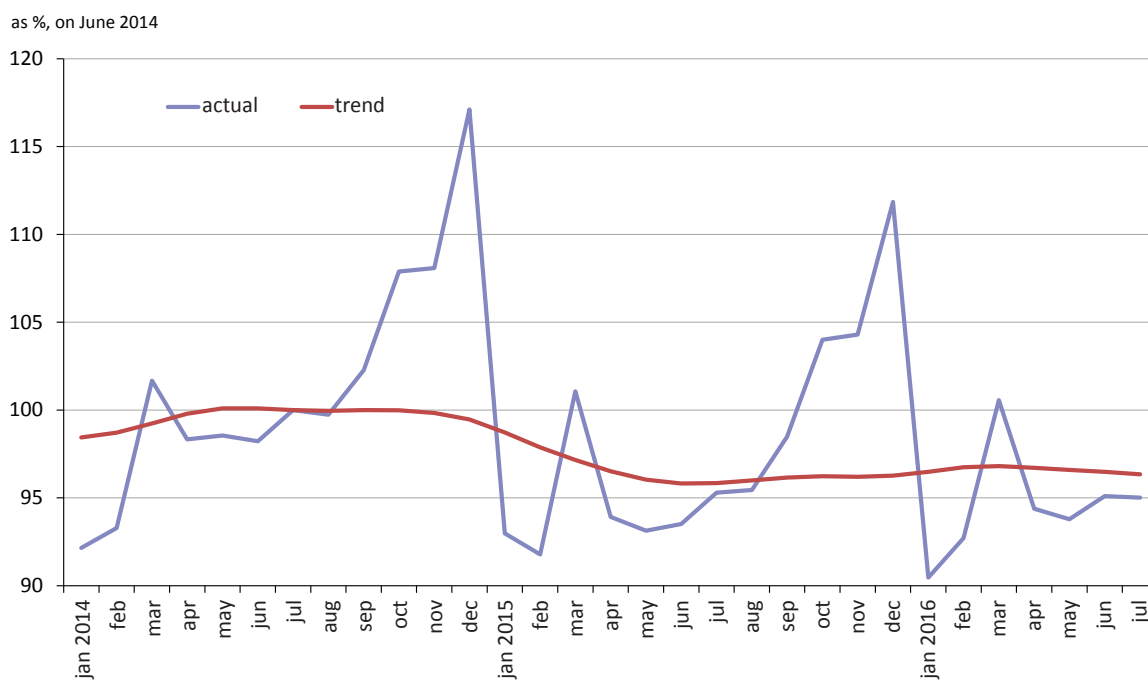
2 This paper was originally published in *Online Monitoring of Russia's Economic Outlook* No.14(32).

3 Russian Economy in 2015. Trends and Outlooks (Issue 37). M., IEP. 2016.

4 A. Kaukin, G. Idrisov. Russian industry in Q1 2016: the onset of stagnation? // *Online Monitoring of Russia's Economic Outlook. Trends and Challenges of Socioeconomic Development*, No. 7 (25), April 2016.

5 Information on the social and economic situation in Russia, January–July 2016, Rosstat.

6 The trend component was removed by using Demetra software package based on X12-ARIMA.



Sources: Rosstat; own calculations.

Fig. 1. The movement of the Industrial Production Index (IPI) in 2014–2016, actual data and trend components

textile products manufacturing; manufacturing of rubber and plastic products; and machinery and equipment manufacturing.

The aftereffects of the 2014 crisis have turned out to be comparatively mild in the manufacturing industry (Fig. 2). Although the implementation of several investment projects was suspended, a certain revival of the investment activity has recently been observed and conducted to slight growth.

The situation in the textiles and textile products manufacturing sector is somewhat more interesting. Traditionally, wages take up a substantial share in the cost structure of textiles and final goods (alongside depreciation and technical upgrading costs). The soaring USD-to-ruble exchange rate after 2014 made the transfer of foreign production entities into Russia's territory¹ and cooperation of domestic producers with their foreign partners² very attractive; besides, it boosted the demand for Russian exports of these products³. In fact, these are examples of inclusion into international value chains, which translates into domestic output growth reflected by an increasing industrial production index in a given sector.

A movement in the opposite direction over the entire period of H1 2016 was demonstrated by metallurgical production. The output plunge in that industry, according to experts⁴, was caused primarily by the shrinking domes-

1 SC ELIS will build a new factory in Rostov to the value of Rb 200m // RBC, 18 June 2016. [<http://rostov.rbc.ru/rostov/18/07/2016/578ccb5b9a7947109655868c>]

2 Pierre Cardin is considering the possibility of clothes manufacturing in the Kuban region // RBC, 23 June 2016. [<http://kuban.rbc.ru/krasnodar/23/06/2016/576b89039a79471299fae7fb>]

3 BTKTextile signed contracts for fabric supplies to Italy // RBC, 24 May 2016. [<http://rostov.rbc.ru/rostov/freenews/574455a09a7947585491afda>]; Recently, we have been observing demand growth // RBC+, 15 June 2016. [<http://www.rbcplus.ru/news/575e1dd77a8aa97007fb7e1d>]

4 Metallurgical crisis. Problems in Russia // Pro nedra, 3 March 2016. [<http://pronedra.ru/mining/2016/03/03/metallurgicheskij-krizis-v-rossii/>]

Table 1

THE BY-SECTOR MOVEMENT OF OUTPUT INDICES

	Share in total industrial production index, %	July 2016 on December 2015, %	July 2016 on March 2016, %	July 2016 on June 2016, %	Changes over recent months
Industrial production index		100.09	99.52	99.86	stagnation
Mineral extraction	33.99	100.25	100.37	100.26	slow growth
Manufacturing industry	52.50	99.88	99.59	99.78	stagnation
including					
Production of foodstuffs, including beverages, and tobacco products	17.05	100.83	100.22	100.06	stagnation
Textiles & textile products manufacturing	1.43	108.48	103.25	99.84	slow growth
Leather production and leather products & footwear manufacturing	0.32	102.00	98.58	99.31	slow decline
Timber & wood product processing	2.20	100.34	99.78	99.20	stagnation
Cellulose & paper production	3.92	100.76	99.78	99.79	stagnation
Production of coke & petroleum products	18.78	99.38	99.75	100.05	stagnation
Chemical production	7.46	100.55	99.10	99.60	decline
Manufacturing of rubber & plastic products	2.26	104.10	103.49	100.00	growth
Manufacturing of other non-metallic mineral products	4.41	96.07	98.87	98.96	slow decline
Metallurgical production & finished metal products	17.23	97.95	97.05	98.91	decline
Machinery & equipment manufacturing	6.24	98.71	99.43	100.94	slow growth
Electrical, electronic and optical equipment manufacturing	6.05	97.81	98.54	99.63	decline
Production of means of transport and transportation equipment	7.06	99.35	99.24	99.41	decline
Other industries	5.59	91.09	94.63	98.32	decline
Electricity, natural gas & water	13.51	99.97	100.00	100.00	stagnation
Retail trade		97.37	98.58	99.75	decline
Wholesale trade*		100.43	99.31	99.75	stagnation
Transport		99.70	100.65	100.49	slow growth
Construction		96.97	98.16	99.78	decline
Commercial services rendered to population*		99.60	99.52	99.77	slow decline

* for these sectors, calculations were done as of June 2016.

Sources: Rosstat; own calculations.

tic demand (a declining construction volume coupled with a general industrial production decline), as well as by the introduction of antidumping duties and economic sanctions by the European Union¹, which prevented Russian metallurgists from taking advantage of their new competitive opportunities that had arisen as a result of the shrinking ruble-denominated component of their costs in the final price of their products (denominated in US dollars) after the ruble's weakening (as it happened in the case of textiles and textile products manufacturing).

1 Russian metallurgists have come under the European Union's sanctions // RBC, 4 August 2016. [<http://www.rbc.ru/business/04/08/2016/57a311779a79475ea5c2fd91>]



Sources: Rosstat; own calculations.

Fig. 2. The by-sector movement of production indices in 2014–2016, actual data and trend components

On the whole in the machinery and equipment manufacturing sectors, including the production of electrical and transportation equipment, output continues its decline caused both by the general shrinkage of demand for their products and their rather high dependence on foreign equipment and spare parts, which have become significantly more expensive due to the ruble's plunge. Slight output growth over recent months has been observed only in the machinery and equipment manufacturing sector, but this is obviously only a manifestation of recovery growth¹. The government support measures for the production of means of transport and transportation equipment² have not yielded any results as yet, judging by the movement of the production indices.

1 Some branches of the Russian economy are entering the new year with optimism // Vzgl'yad, 5 January 2016. [<http://vz.ru/economy/2016/1/5/786502.html>]

2 Program of transport machine-building for 2016 (Directive of the Government of the Russian Federation of 21 January 2016, No. 57-r).

Other important sectors have been displaying practically no growth: the decline in the retail and construction sectors is continuing; the wholesale sector is stagnating; and slight growth can be observed only in freight turnover (*Table 1* and *Fig. 2*). ●