

# **MONITORING OF RUSSIA'S ECONOMIC OUTLOOK:**

TRENDS AND CHALLENGES OF SOCIO-ECONOMIC DEVELOPMENT

**No. 19(37) December 2016**

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**РАНХиГС**  
РОССИЙСКАЯ АКАДЕМИЯ НАРОДНОГО ХОЗЯЙСТВА  
И ГОСУДАРСТВЕННОЙ СЛУЖБЫ  
ПРИ ПРЕЗИДЕНТЕ РОССИЙСКОЙ ФЕДЕРАЦИИ



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## MAIN TRENDS AND CONCLUSIONS

Crude oil prices are up significantly and oil export revenues are expected to face an uptrend after OPEC members have reached an unlikely agreement to curb oil production, in which Russia played an active part. However, only complete optimists could consider seriously that the emerged trend could be viewed as a reason for reviewing prospects of national economies.

First, there is no confidence whatsoever that agreements on curbing oil production would be observed over any longer-term period. Second, a rise in the crude price from, say, \$45 to \$55 a barrel is a good incentive for growth in oil production in the United States (not to mention US president-elect Donald Trump's intention to provide an extra boost to the US oil industry). Finally, these figures make no crucial difference whatsoever for, say, Russia's economy, which is facing issues of structural inefficiency and adverse business environment. In his recent Presidential Address to the Federal Assembly Russian President Putin had a good reason to stress the need for establishing appropriate arrangements to ensure that the federal budget is on a sustainable fiscal path, regardless of whatever external factors, including hydrocarbons prices, may be at play.

Our experts have analysed the execution of Russia's federal budget in the period between January and October 2016, and they note that the fall of federal budget revenues by 1.9 percentage points of GDP during that period compared to the same period last year was caused directly by the fall of oil and gas revenues. This could have been even worse, had the dynamics of non-oil and gas revenues not improved. Non-oil and gas deficit has been reducing. However, the experts' conclusion can only in part be viewed as optimistic one: in fact, what we are seeing is that the federal budget is becoming less reliant on the global energy market, which, however, is not the result of structural diversification of economy, but it rather is due to the decrease in terms of volume (and as a percentage share) of oil and gas revenues and to the decline in the percentage share of oil and gas industry of Russia's GDP.

Experts from the Gaidar Institute carried out business surveys of Russian enterprises in October 2016. The obtained results give more specific reasons for optimism with regard to Russia's industrial sector. Respondents noted a certain increase in demand for their products and expressed optimism, albeit with a dose of caution, about the prospects of the recent financial crisis coming to an end. One third of the respondents (the smallest share since the onset of the crisis) said uncertainty about the condition of the Russian economy – as it is now – is a factor that limits the industrial sector's ability to grow, whereas nearly a half of the respondents shared the same viewpoint in early 2016. As to the so-called "resource constraints", shortage of skilled personnel was ranked first by 23% of the respondents, shortage of working capital (a record low percentage throughout the entire survey period) was ranked second. Shortage of loans was mentioned by the smallest percentage (3%) of the respondents, with high loan rates being mentioned a bit more frequently (6%), the lowest percentage in the past 11 quarters of this year.

According to the experts, quite different are motives, assessments and dynamics in the retail bank lending whose conditions, among other indica-

tors, allow for assessing households' propensity to save. While assessing both change in bank loan delinquencies and in the dynamics of the bank deposits to income ratio, as well as in the dynamics of cash (roubles and foreign exchange), the experts have concluded that propensity to save still exists. Although growth in retail deposits and accounts in banks slowed down considerably in the first three quarters of this year, the "aggregate households' propensity to save is still at a high level". In contrast, households' savings exhibited negative values in recent years.

Curiously enough, migrants seem also to have gained confidence in savings in Russia despite crisis developments. According to our experts, it is highly likely that the 2016 year-end inbound migration growth in Russia will regain the level reached during the last few years. Furthermore, migration still contributes almost entirely to the population growth in the country. Temporary foreign migration shows that foreigners are getting "tolerant" to the economic situation in Russia, foreign migrants numbers started to rise again in summer season. However, foreign sojourners in Russia are still smaller in number than in previous years, including the last year. The issue of legalising migrants in the labour market seems to have become even more acute – the list of documents required for employment permit application is getting shorter, anyway. ●

## 1. THE EXECUTION OF THE FEDERAL BUDGET FOR JANUARY–OCTOBER 2016: SHRINKAGE OF THE OIL AND GAS DEFICIT

**A. Mamedov, E. Fomina**

*As demonstrated by reported monthly performance data, the RF federal budget for the first 10 months of 2016 was executed with a deficit of -2.3% of GDP (vs. -1.0% of GDP over the same period of 2015). By the year-end of 2016<sup>1</sup>, the plunge of total federal budget revenue is not expected to exceed 0.8 p.p. of GDP (as compared with 2015), this result to be secured by an increased non-oil and gas revenue component. The year-end movement pattern of expenditure in 2016 is going to be exactly reverse: its amount is expected to increase by 0.5 p.p. of GDP, due in the main to the additional allocation, in November, of Rb 739.7bn to national defense.*

### **Revenue and Expenditure: General Estimates**

In accordance with the RF Federal Treasury's monthly performance reports, RF federal budget revenue as of 1 November 2016 amounted to 15.4% of GDP (or Rb 10,440.6bn), which is 1.9 p.p. of GDP below the corresponding figure for the same period of 2015 (a drop by nearly 8% in nominal terms – see *Table 1*). The plunge of aggregate federal budget revenue in January–October 2016 was caused by the radical shrinkage of its oil and gas component. Over the first 10 months of 2016, the amount of oil and gas revenues shrank in nominal terms on the corresponding period of last year by 22.5%, or by nearly 2 p.p. of GDP.

At the same time, the amount of non-oil and gas revenues in terms of share of GDP remained at the previous level, while increasing in nominal terms by 3.5%. For 2016, the RF Ministry of Finance expects the year-end total federal budget revenue to decline by only 0.8 p.p. of GDP (as compared with 2015), which will be made possible by the non-oil and gas component's growth (by 0.8 p.p. of GDP).

The improved dynamics of the non-oil and gas revenues in the federal budget over recent months has had to do with the expected proceeds to be generated by the partial privatization of PAO *Rosneft*<sup>2</sup>. However, it is still doubtful if this deal can actually be closed before the year-end of 2016.

Federal budget expenditure executed over January–October 2016 amounted to 17.7% of GDP, which is 0.6 p.p. of GDP below the corresponding index for the first 10 months of 2015. The expenditure volume in nominal

<sup>1</sup> Hereinafter, the estimates for the year-end execution of the RF federal budget are based on the Explanatory Note for the Draft Federal Law 'On the Federal Budget for 2017 and Planning Period 2018 and 2019'.

<sup>2</sup> These revenues are not charged to the sources for covering budget deficit; instead, they are entered on the revenue side due to the multi-tiered public ownership structure of PAO *Rosneft* (through OJSC *Rosneftegaz*; once the transaction is completed, all the revenues generated by it must be transferred to the federal budget as early as 2016, to offset the dividends payable on shares in 2017 and the year-end dividends for 2016).

Table 1

## MAIN PARAMETERS OF THE FEDERAL BUDGET FOR JANUARY–OCTOBER 2015–2016

	2015		2016		Change over first 10 months of 2016 relative to first 10 months of 2015		Implementation of annual targets	
	10 months (actual)	Year (actual)	10 months (actual)	Year (estimated)	p.p. of GDP	nominal growth rate, %	10 months of 2015	10 months of 2016
	% of GDP						%	
<b>Revenue, including:</b>	17.3	16.9	15.4	16.1	-1.9	-7.9	83	78
oil and gas revenues	7.6	7.3	5.7	5.8	-1.9	-22.5	85	81
non-oil and gas revenues	9.7	9.6	9.7	10.4	0.0	+3.5	82	77
<b>Expenditure, including:</b>	18.3	19.3	17.7	19.8	-0.6	+0.3	77	73
interest	0.7	0.6	0.8	0.8	+0.2	+27.4	83	86
non-interest	17.6	18.7	16.9	19.0	-0.7	-0.7	77	73
<b>Federal budget surplus (deficit)</b>	-1.0	-2.4	-2.3	-3.7	+1.3	+144.6	33	52
non-oil and gas deficit	-8.6	-9.7	-8.0	-9.4	-0.6	-3.3	72	70
For reference: GDP at current prices	65,612	80,804	67,775	82,815	–	+3.3	–	–

Source: for 2015 and the first 10 months of 2016 – the RF Federal Treasury's reports; for 2016 – preliminary estimates released by the RF Ministry of Finance; own calculations.

terms increased by 0.3%, largely due to the significant rise in the amount of budgeted interest on public debt in the federal budget (by 27.4%).

The growth of expenditures related to public debt servicing resulted from the increased domestic debt servicing costs (by 43%) coupled with the slightly reduced foreign debt servicing costs (by 2%). One of the relevant factors was the accelerated debt growth rate in 2016: while over the entire year-long period of 2015 Russia's domestic debt had gained less than 1.8%, over the first 10 months of 2016 alone that index jumped by 6%.

The year-end result of 2016 is expected to demonstrate growth of total budget expenditure not only in nominal terms, but also in terms of share of GDP (by 0.5 p.p.), first of all due to the allocation of an additional Rb 739.7bn to national defense (mainly earmarked for the redemption of debts owed by defense enterprises against their loans). In the end, the execution of federal budget expenditure over the first 10 months of 2016 (as a percentage of the annual expenditure ceiling) turned out to be 4 p.p. below the corresponding index for the same period of 2015, thus pointing to the increasingly uneven expenditure distribution. For the last two months of the year 2016, there remains 27% of the annual expenditure target.

As shown by the period-end results for January–October 2016, the RF federal budget was executed with a deficit of 2.3% of GDP, which is 1.3 p.p. of GDP above the amount of deficit for the corresponding period of 2015. According to the RF Ministry of Finance's preliminary year-end estimates, the annual federal budget deficit growth in 2016 will not exceed 1.3 p.p. of GDP relative to its 2015 index. Meanwhile, the non-oil and gas deficit in 2016 is going to decline, both based on the period-end result of the first 10 months and in per annum terms.

So, the federal budget is becoming *de facto* less dependent on the situation in the world energy carriers markets, but this is happening not because of an increasing diversification of the Russian economy, but due to the significant shrinkage of the volume (and thus the budget share) of oil and gas revenues.

Table 2

## TAX RECEIPTS IN THE FEDERAL BUDGET OVER JANUARY–OCTOBER 2015–2016

	2015		2016		Change over first 10 months of 2016 relative to first 10 months of 2015		Implementation of annual targets	
	10 months (actual)	Year (actual)	10 months (actual)	Year (estimated)	p.p. of GDP	nominal growth rate, %	10 months of 2015	10 months of 2016
	% of GDP						%	
<b>Tax-generated revenues, total, including</b>	15.3	14.7	13.7	13.5	-1.5	-7.1	84	83
tax on profit of organizations	0.7	0.6	0.6	0.6	0.0	-3.5	90	92
VAT on goods produced in RF territory	3.3	3.0	3.4	3.2	+0.2	+8.6	87	88
VAT on goods imported into RF territory	2.2	2.2	2.3	2.3	+0.1	+7.9	80	81
Excises on goods produced in RF territory	0.7	0.7	0.8	3.2	+0.1	+19.4	82	83
Excises on goods imported into RF territory	0.1	0.1	0.1	0.1	0.0	+11.7	76	81
Tax on mineral resources extraction	4.1	3.9	3.4	3.4	-0.7	-14.1	85	81
Revenues generated by foreign trade (customs duties)	4.2	4.1	3.0	3.1	-1.1	-24.8	83	80

Source: for 2015 and the first 10 months of 2016 – the RF Federal Treasury's reports; for 2016 – preliminary estimates released by the RF Ministry of Finance; own calculations.

### Tax-generated Revenues

The parameters of the execution of the federal budget on its revenue side over the first 10 months of 2016 are presented in *Table 2*. When analyzing the movement of the actual amount of tax receipts over that period, we noted their plunge by 1.5 p.p. of GDP as compared with the same period of 2015.

The shrinkage of tax receipts was caused in the main by the corresponding plunge of oil and gas revenues not only in terms of share of GDP, but also in absolute terms. The receipts of customs duties shrank by 25% in nominal terms, of by 1.1 p.p. of GDP (largely due to the reduced export duties on oil and petroleum products). The loss of tax on mineral resources extraction in nominal terms was as high as 14%, or 0.7 p.p. of GDP. Overall, the shrinkage of oil and gas revenues was caused by the significant plunge in oil prices<sup>1</sup>. However, these budget changes were partly offset by the ruble's weakening relative to the US dollar<sup>2</sup>.

It can also be noted that in 2016, the ceiling for the rate of export duty on oil was left at the level of 42%, while that of tax on mineral resources extraction for oil was raised from Rb 766 to Rb 857 per tonne. These legislative innovations, which actually went contrary to the logic of the ongoing tax maneuver, also helped prevent some of the potential federal budget loss that could result from the plummeting oil prices.

At the same time, the receipts of some other taxes increased both in nominal terms and in terms of share of GDP. Thus, the federal budget receipts

<sup>1</sup> Over the first 10 months of 2016, the average price of Urals was \$40.7 per barrel vs. \$53.6 per barrel over the corresponding period of 2015.

<sup>2</sup> The average ruble-to-USD exchange rate over the first 10 months of 2016 was Rb 67.7 vs. Rb 59.4 over the corresponding period of 2015.

of VAT on goods produced in RF territory gained 8.6% in nominal terms, or 0.2 p.p. of GDP; the revenues generated by VAT on imports increased by 7.9% in nominal terms, or by 0.1 p.p. of GDP; and the excises on goods produced in RF territory – by 19.4% or 0.1 p.p. of GDP respectively. The higher revenue inflow generated by these taxes could only in part compensate for the lost oil and gas revenues, and so it failed to reverse the overall downward trend displayed by the volume of tax receipts.

### **The Reliability of Planned Targets**

The significant deviation of the actual budget execution over the first 10 months of 2016 from its execution indices for the same period of 2015 may be indicative of the fact that the planned annual revenue targets for 2016 were insufficiently substantiated. If we compare the data in the last two columns in *Table 2*, no significant differences between 2015 and 2016 will be seen. At the same time, the level of budget execution over the first 10 months of 2016 for the majority of taxes pertaining to non-oil and gas revenues was somewhat higher than a year earlier. All other conditions being equal, this may point to the annual receipts targets set for these taxes being conservative (because if the budget execution indices for the first 10 months of 2016 remain at the same level as in 2015, the year-end result of 2016 can be expected to be above the target planned by the RF Ministry of Finance).

From this point of view, the greatest deviation from the planned target was displayed by the excises on goods imported into RF territory (5 p.p.). A reverse situation can be observed with regard to tax on mineral resources extraction and customs duties (revenues generated by foreign trade): our analysis of the actual receipts demonstrates that the annual targets set for 2016 were somewhat overestimated. However, bearing in mind that the key indicator in this case is the price of oil, which in H2 2016 moved over a higher trajectory than in H1, the estimates for the receipts of tax on mineral resources extraction and customs duties released by the RF Ministry of Finance appear to be quite realistic (due to the favorable trend displayed by prices of oil, the share of receipts over the last 2 months may well become higher than the corresponding index for last year).

*Table 3* demonstrates the by-function distribution of federal budget expenditure over the period 2015–2016 (10-month-period-end and year-end data). If we compare the movement of various budget functions as shown in *Table 3*, it will become obvious that the plunge in the total federal expenditure volume over the period of January–October 2016 was caused in the main by the shrinkage of allocations to national defense by 0.5 p.p. of GDP as a result of their slower implementation relative to the same period of 2015 (56% vs. 76% respectively). The upshot is that nearly 50% of the actually allocated expenditure will have to be implemented during the year's last 2 months. However, it must be remembered that such a situation emerged primarily due to the fact that an additional sum of Rb 739.7bn was allocated to national defense only after a number of relevant alterations had been made to the current budget law in November 2016 (earmarked in the main for the repayment of loans taken by companies belonging to the defense complex).

A similar trend, albeit on a lower scale, is also typical of the expenditures allocated to national security and law-enforcement activity, which shrank by 0.2 p.p. of GDP over the first 10 months of 2016 alongside a reduction of the degree of their actual implementation from 76% to 73%. For all the other ma-



Table 3

## FEDERAL BUDGET EXPENDITURE OVER JANUARY–OCTOBER 2015–2016

	2015		2016		Change over first 10 months of 2016 relative to first 10 months of 2015		Implementation of annual targets	
	10 months (actual)	Year (actual)	10 months (actual)	Year (estimated)	p.p. of GDP	nominal growth rate, %	10 months of 2015	10 months of 2016
	% of GDP						%	
<b>Expenditure, total, including:</b>	18.3	19.3	17.7	19.8	-0.6	+0.3	76.7	73.3
Nationwide issues	1.2	1.4	1.2	1.3	0.0	+5.5	71.6	76.9
National defense	3.7	3.9	3.2	4.7	-0.5	-10.1	76.3	56.1
National security and law-enforcement activity	2.3	2.4	2.1	2.3	-0.2	-4.9	76.1	73.2
National economy	2.4	2.9	2.3	2.6	-0.1	-2.7	68.3	71.4
Housing and utilities sector	0.1	0.2	0.1	0.1	-0.1	-41.4	59.0	87.4
Environment protection	0.1	0.1	0.1	0.1	0.0	+24.5	87.0	83.4
Education	0.8	0.8	0.7	0.7	-0.1	-4.0	85.5	89.8
Culture, cinematography	0.1	0.1	0.1	0.1	0.0	-7.9	78.5	70.7
Healthcare	0.6	0.6	0.6	0.6	0.0	+2.0	76.3	86.1
Social policy	5.3	5.3	5.6	5.6	+0.3	+9.1	81.2	81.6
Physical culture and sports	0.1	0.1	0.1	0.1	0.0	-36.3	77.3	54.1
Mass media	0.1	0.1	0.1	0.1	0.0	-22.6	88.5	74.1
Government debt servicing	0.7	0.6	0.8	0.8	+0.2	+27.4	83.2	86.0
Interbudgetary transfers	0.8	0.8	0.8	0.8	0.0	0.2	78.1	81.3

Source: for 2015 and the first 10 months of 2016 – the RF Federal Treasury's reports; for 2016 – preliminary estimates released by the RF Ministry of Finance; own calculations.

For budget functions, the expenditure implementation index over the year's first 10 months either remained practically unchanged, or even increased. So, their movement (growth or decline) over January–October 2016 is on the whole compatible with their planned year-end targets.

### The Evenness of Budget Execution

A comparative analysis of the RF Federal Treasury's reports for the first 9 months of 2016 and 2015 from the point of view of by-department distribution of budget expenditure can demonstrate how evenly the budget funds are spent by each ministry and government department. *Table 4* shows the list of 10 chief budget funds managers (CBFMs) that achieved the least degree of expenditure implementation (relative to the annual target) over the first 9 months of 2016. In view of the low budget implementation rate demonstrated by these CBFMs over the financial year's first 9 months, it appears doubtful that budget funds can be spent with due efficiency in a situation where more than 50% of the total expenditure allocated to each of these departments is left for the year's last quarter.

It is noteworthy that, for a second year in a row, 8 out of the 10 CBFMs listed in *Table 4* have left more than half of the annual sum allocated to them to be spent over the year's last quarter. Another important phenomenon is that, by the year-end of 2015, only 2 out of these 8 agencies implemented significantly less than 100% of their budget allocations (the Federal Agency for Air Transport and the Federal Space Agency). As a result, the remaining 6 agencies were able to implement 50% or more of their annual allocations during the year's last quarter. In order to improve budgetary discipline and ensure

Table 4

THE CBFMS WITH THE LEAST DEGREE OF BUDGET EXPENDITURE IMPLEMENTATION  
OVER THE FIRST 9 MONTHS OF 2016 (RELATIVE TO ANNUAL TARGETS)

No	CBFMs	CBFM code	Budget execution, %		
			9 months of 2015	2015	9 months of 2016
1	Federal Agency for Ethnic Affairs	380	66.5	95.9	20.6
2	Federal Space Agency	259	39.3	91.7	21.9
3	RF Ministry of Economic Development of the Russian Federation	139	32.8	96.4	22.6
4	RF Ministry for the Development of the Russian Far East	350	6.6	98.8	26.7
5	RF Ministry of Communications and Mass Media	071	35.0	98.2	29.8
6	Federal Agency for Air Transport	107	35.2	76.3	33.5
7	Federal Guard Service	202	29.8	99.9	37.6
8	RF Ministry of Sport	777	70.8	97.9	40.7
9	RF Ministry of North Caucasus Affairs	370	13.0	99.0	41.0
10	Federal Service for Supervision in Education and Science	077	54.1	99.4	48.1

Source: the RF Federal Treasury's reports for 2015–2016; own calculations.

even spending of budget funds, in 2016 the rule was introduced whereby the CBFMs, after 30 September of each year, were no longer allowed to assume obligations associated with supplies of goods, performance of work, and delivery of services (with the exception of those executed in the framework of government defense orders and some other types of expenditure)<sup>1</sup>.

As follows from our analysis, in 2016 neither the budget execution pattern nor budget sustainability demonstrated an improvement, which casts doubt concerning the efficiency of the current measures designed to improve the quality of financial management practiced by the CBFMs. ●

1 Decree of the RF Government of April 4, 2016, No. 266 'On Introducing Alterations into Decree of the RF Government of the Russian Federation of December 28, 2015, No. 1456 "On Measures Designed to Implement the Federal Law 'On the Federal Budget for 2016'".

## 2. RUSSIAN INDUSTRY IN OCTOBER 2016: CAUTIOUS OPTIMISM INSPIRED BY SALES

**S. Tsykhlo**

*There are hopes for industrial recovery from stagnation in Russia, according to analysis of the results of a survey that was carried out by the Gaidar Institute in October 2016. A positive shift in real sales dynamics coupled with slowly upgraded forecasts for the same is supplemented by a moderate, albeit positive, recovery of industrial production growth rates and a likely upward revision in assessments of finished product stocks. No visible positive shifts in output plans have been seen to date.*

### **Demand for industrial products**

The initial dynamics (balance of changes) of demand in 2016 exhibits stability that was unusual for the past few years. Following the traditional collapse early in the year, the indicator reached near-zero values and has been staying within a range of -3...+2 points for eight months since then, still reluctant to decline (as it always did at year end), the balance value in October stood at +2 points.

It was for the first time that the seasonally and calendar adjusted demand balance reached a positive value regardless of the fact that enterprises tend to undervalue sales dynamics. November and December might yet see a decline in demand that was typical of previous years, although enterprises forecast the opposite. Manufacturers' seasonally adjusted expectations were slowly, albeit consistently, infused with optimism in the second half of the year, thereby reaching the highest value (amid recession) in October. Russia's industrial sector is explicitly exhibiting a cautious optimism regarding prospects of the economic recession coming to an end.

Enterprises' sales volume assessments show that the industrial sector is highly satisfied (which is unusual amid recession) with the demand as it is now. Fifty six percent of the respondents said the situation was "normal" in October, which is in line with the average value recorded in the preceding quarter. This is the highest value in the recent economic recession, while the lowest one (45%) was recorded in Q1 2016, that is, not at the peak of the recession. The lowest value stood at 23% during the recession of 2008–2009, and it was recorded appropriately at the onset of the recession.

### **Finished product stocks**

Enterprises' assessments of finished goods stocks in October were not as "normal" as they were in Q3 2016, which is rather due to respondents who didn't know the answer ("no answer"). However, the balance of responses describing the situation as "above normal" – "below normal" remained unchanged and negative. The latter indicates that the industrial sector is generally aware of being short of finished product stocks in terms of physical volume, however, the industry is yet not ready to increase them because it is not quite sure about consistency of the upward trends that apparently have been developing in recent months. This point is also supported by growth in the percentage of respondents who said they have "no answer" regarding

stock assessment. The industrial sector has started looking for a new physical volume that could be optimal for finished product stocks, which may even concern the recovery stage, and there are enterprises that have not yet made up their mind about what it could be.

### **Output**

Output dynamics in October exhibited positive changes after the collapse in September that was registered during our surveys. However, the changes will be as minor as they always were, that is, the industrial production growth rate will remain nearly zero, sending no signals of entering a recovery phase. No clear hopes for higher output in the coming months can be seen from enterprises' plans.

Seasonally adjusted balances in recent months are still positive, albeit extremely moderate in terms of magnitude. Moreover, production plans current balances are less optimistic than those of the same months of 2015. It appears that then industry's expectations were "cheered up" by very nearly official statements (promises) of an upcoming "rebound from the bottom of recession" that eventually did not happen. In early 2016, this was apparently the beginning of projecting the most pessimistic output plans ever in the course of the recession, even more pessimistic than those in Q1 2015, that is, at the onset of the recent recession.

### **Industrial growth constraints**

Enterprises' moderately optimistic plans and forecasts coupled with the acknowledgment of being short of finished product stocks can be complemented with analysis of constraints to industrial growth, as enterprises see them.

Fifty percent of the enterprises still consider inadequate domestic demand as the principal constraint. For now, all the other factors are ranked much inferior to this constraint despite the fact that the majority of enterprises have managed to adapt to the volumes of their products that are in demand.

"Uncertainty about the condition and prospects of the Russian economy as it is now" is, as always, ranked second. This factor has been considered a constraint to a meaningful output strategy since the mid-2016, according to one third of Russian enterprises. However, 33% of the respondents mentioned "uncertainties", which is the lowest percentage ever in the course of the recent recession. This factor produced the strongest adverse effect on the Russian industrial sector in early 2016, when nearly a half of the respondents (enterprises) said it is a constraint, which resulted from, among other things, statements about reaching the bottom of recession and of an upcoming growth. The fact that government officials dropped giving promises of "rebounding from the bottom" and shifted to a more low-key rhetoric in 2016 did work in favour of the industrial sector, and enterprises have recently begun to seek ways towards recovery, having hunted down the specifics of the recent recession.

They also consider external demand, as they can hardly count on any growth in domestic demand. Therefore, 30% of the respondents (enterprises) pointed to low export demand, ranking it as the third most important factor. A strengthening rouble might have become another reason for growing issues of external demand.

However, the dynamics of references to other constraints allows one to be doubtful about a strengthening rouble having a truly adverse effect on

the Russian industrial sector in late 2016. Indeed, the constrain influence of such factor as “overdepreciated rouble exchange rate and appreciation of imported equipment and commodities” weakened by Q4 to its pre-recession level due to both a stronger rouble and two-year adaptation of the Russian industrial sector to a new exchange rate policy of the Bank of Russia. At the same time, an adverse effect on Russia’s industrial output by such factor as “competition with imports” weakened to a 16-year low(!), that is, it became the most moderate since the impact of 14-fold devaluation of the rouble in the aftermath of the Russian default of 1998.

Shortage of qualified personnel (that is still gaining momentum), especially regular labour force, was ranked first among the “resource constraints” to industrial growth in 2016. Twenty three percent of the respondents pointed to this factor. Nineteen percent of respondents who pointed to this factor was registered a year ago, the smallest percentage since the onset of the recession. Shortage of working capital has recently reached an all-time record in the entire period of monitoring (1993–2016) and is ranked second among the resource constraints. Shortage of machinery and equipment (“capacity shortage”) and shortage of commodities and materials are ranked third and fourth respectively, 8–9% of the respondents (enterprises) pointed to these factors. Finally, shortage of loans was mentioned by the smallest percentage (3%) of the respondents. However, high loan rates were mentioned a bit more frequently (by 6% of the respondents). The result obtained in Q4 2016 reflects the lowest percentage in the past 11 quarters of this year. ●

### 3. GROWTH OF THE RETAIL BANK DEPOSITS HAS SLOWED DOWN, HOWEVER CASH SAVINGS TREND REMAINS

M. Khromov

*During the first three quarters of 2016, growth rate of the retail bank deposits and accounts has slowed down twofold in comparison with the same period of 2015. However, it is still premature to talk about the dismantling of the savings model. Cash dynamics demonstrate increment of the households' propensity for cash savings. Slow growth of the population's loan debt retains positive net increment of retail assets.*

Over three quarters of 2016, retail bank accounts have moved up by Rb 1,054bn<sup>1</sup>. This is 40% less than a year earlier (Rb 1.776bn). Increase of the assets on the retail bank accounts and deposits over 9 months of 2016 has come to 4.7%, which is half the amount registered for the same period of 2015 (9.8%). In relation to the household's income<sup>2</sup> retail savings on the bank deposits have also gone down from 4.9 to 2.8%.

At a first glance, these trends demonstrate a reduction of propensity to save on part of Russian households. This is correct if we understand propensity to saving in the narrow sense of the word – bank deposits to income ratio. However, if we take into consideration the fact that deposits are not a single instrument of savings then a more complicated picture pops up.

In addition to dynamics of bank deposits, dynamics of cash denominated in national and foreign currencies also reflect the retail savings activity. Moreover, change on bank loans debt is also an important indicator. The loan debt growth demonstrates current contraction of net financial assets<sup>3</sup> of households and, vice versa, reduction of loan debt together with traditional saving instruments increases net assets of the population.

In what way households' preferences regarding financial instruments (besides bank deposits) have changed in comparison with last year. During 9 months of 2016, the volume of cash has gone up by Rb 383bn. Of which Rb 173bn accounts for cash and Rb 210bn accrue to the ruble equivalent of growing foreign cash. Its dollar volume went up by UDS 3.1bn over 3 months. Thus, total volume of money (cash and non-cash) in possession of Russian households has moved up for January–September 2016 by Rb 1,437bn, which comes to 3.9% of their income.

Regarding bank lending, in April 2016, reduction of the retail debt before banks terminated, which lasted for 16 months in a row. In Q2 and Q3, retail lending portfolio began expanding. However, total growth since the turn of the year was insignificant – barely Rb 15bn.

<sup>1</sup> Hereinafter, dynamics of balance indices is given with adjustment to revaluation of assets denominated in foreign currency according to dynamics of dollar ruble exchange rate.

<sup>2</sup> Hereinafter, household income is a measure of cash income according to the Rosstat methodology adjusted to the income volume generated from the sale of cash foreign currency because this transaction is not income of an individual and solely means a change in the structure of their financial assets.

<sup>3</sup> Hereinafter, net assets of households are a sum of cash and non-cash assets of individuals minus retail debt on bank loans.

### 3. GROWTH OF THE RETAIL BANK DEPOSITS HAS SLOWED DOWN

Consequently, net increment of households' assets for the first 9 months of the current year has constituted Rb 1,422bn, which amounts to 3.8% of income.

Last year's dynamics of the corresponding financial balance items of households was completely different. For the first three quarters of 2015, the volume of cash has shrunk by Rb 1,051bn. This amount resulted from a reduction of cash rubles by Rb 427bn and a decrease of cash foreign currency by USD 10.5bn or by Rb 624bn in ruble equivalent. This signifies that despite a rather healthy growth of assets on retail bank accounts and deposits, total volume of cash in hand moved up for the first 9 months of 2015 rather moderately – merely Rb 726bn or by 2.0% of the households income.

Furthermore, as was noted above, the entire last year a reduction of retail bank loans debt was observed. Repayment of bank loans was an alternative to money savings taking into account net assets of households. During Q1–Q3 2015, retail lending portfolio shrank by Rb 732bn. Thuswise, for the first three quarters of 2015, increment of net assets of households totaled to Rb 1,458bn or 4.0% of income.

Comparison of this data shows that net increment of assets of the population for the first three quarters of 2016 in comparison with the corresponding period of 2015 really decreased, but barely by 0.2 p.p. from 4.0 to 3.8% of households.

*Table 1*

#### DYNAMICS OF MAIN COMPONENTS OF NET ASSETS OF HOUSEHOLDS IN Q1–Q3

	Average for 2011–2013	2014	2015	2016
	Bn Rb			
Growth of assets on accounts and deposits	1185	-254	1776	1054
Growth of foreign currency in cash	-42	520	-624	210
Growth of domestic currency in cash	124	-26	-427	173
Total growth of money assets	1267	239	726	1437
Debt change on bank loans («-» – growth of loans, «+» – decrease)	-1501	-1108	732	-15
Total change in net assets	-234	-868	1458	1422
	% to income			
Growth of assets on bank accounts and deposits	4.3	-0.8	4.9	2.8
Growth of foreign currency in cash	-0.2	1.6	-1.7	0.6
Growth of domestic currency in cash	0.5	-0.1	-1.2	0.5
Total growth of cash assets	4.6	0.7	2.0	3.9
Debt change on bank loans	-5.5	-3.4	2.0	0.0
Total change in net assets	-0.9	-2.6	4.0	3.8

Moreover, despite an insignificant reduction registered in 2016, growth of net assets to income ratio of households remains on a high level. During previous several years, as well as during first three quarters of the current year net assets of households were falling. This was owing partly to a strong growth of debt on bank loans in volumes, which exceed growth of cash resources (such situation was observed in 2011–2013).

In 2014, outflow of bank deposits together with savings of foreign currency in cash was observed with simultaneous retention of credit debt increase. Cash income demonstrates seasonality effect when the increment of money assets in Q4 of the calendar year significantly exceeds the one registered in Q1–Q3. As a result, by the year-end growth of net retail assets is typically

observed. Solely 2014 was an exception, when even by the year-end households assets decreased on the whole.

The situation with the saving behavior of households in Q1–Q3 2015–2016 to a certain extent is similar to the same period of 2009–2010, when the population boasted of a saving model in the wake of contraction of credit debt in 2009 and gradual its resumption in 2010. During 2009–2010, over first three quarters of the calendar year growth of net assets of households exceeded 5.0% of their income, which was by 1 p.p. more than in 2015–2016.

Lower values of net assets of the population during current period in comparison with 2009–2010 was explained, most likely, by a negative dynamics of households cash income in real terms. Their nominal volume in Q1–Q3 2016 moved up by 2.8% in comparison with the corresponding period of 2015 and by 13.3% – to 2014. At the same time, the average level of consumer prices for Q1–Q3 2016 was higher than for the same period of 2015 by 7.7% and by 24.9% against 2014. Meanwhile in 2009–2010, there was no reduction of household income in real terms. ●



## 4. MIGRATION IN RUSSIA: OLD TRENDS AND NEW PROBLEMS

Yu. Florinskaya, N. Mkrtchyan

According to the 2016 results, in Russia migration growth is likely to return from lower rates to the level of the past few years. As before, migration virtually ensures completely population growth in Russia. The two largest metropolitan areas (Moscow together with the Moscow Region and St. Petersburg together with the Leningrad Region) and the Krasnodar Territory are the main centers which attract migrants.

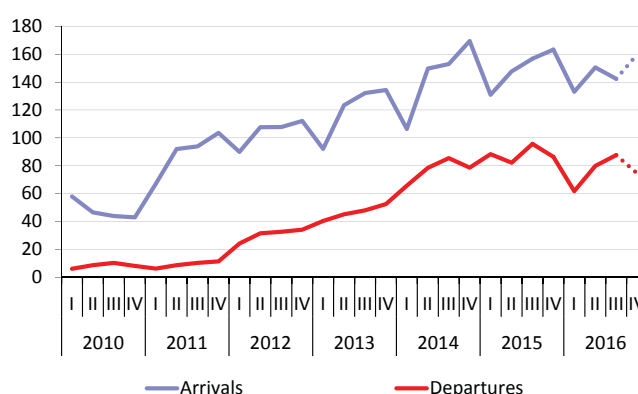
Also, there is a renewal of growth in temporary foreign migration (season migrants) in a summer period. The number of season foreign migrants is below the level of 2013–2014 and even that of 2015. In 2016, the issues related to regulation of labor migration have become more topical: the number of work permits required for employment keeps falling.

### The Long-Term Migration

In 2016, the international migration to Russia (its *long-term* component) was at a stable level in the past few years. By our estimate, on the basis of the results of the year the number of migrants who arrived will not exceed 600,000 people, while departures are expected at the level of over 300,000 people. As a result, within a year migration growth will remain at the level of the past few years: according to our estimates it amounts to about 280,000 people. The extent of statistically registered arrivals more than doubled, while departures increased by times; it is to be noted that migration growth stabilized at the level of 250,000–300,000 a year (Fig. 1), that is, the level it was at in the late 2000s.

Migration makes a decisive contribution to the dynamics of the number of population in Russia and ensures completely its growth. The role of the long-term migration in making up for a decrease in the number of active working age population is not quite significant; in the past few years it covered only 15% of losses of that age group.

As compared to 2016, migration growth increased, but it happened on the back of a drop in the last year's index; generally, the values remain at the level of the past few years (Table 1). The above growth was ensured by renewal both of a migration increase in the exchange of migrants with Uzbekistan and standard volumes of growth in the exchange of migrants with Tajikistan. It is to be noted that Ukraine is still Russia's main migration donor: in 2016 it ensured almost 50% of migration growth in the international migration. As compared to the previous years, the net influx of



**Note.** The 4Q 2016 data were calculated on the basis of distribution of numbers of arrivals and departures by quarter in 2015.

Source: The Rosstat and the authors' calculations.

Fig. 1. International migration to Russia, the 2010–2016 period, quarterly data, thousand persons

migrants from most CIS states decreased, while growth in the exchange of migrants with Kazakhstan remains at a stable level.

*Table 1*

THE NET-MIGRATION OF RUSSIA'S POPULATION WITH FOREIGN STATES,  
JANUARY–SEPTEMBER 2012–2016, THOUSAND PERSONS

	2012	2013	2014	2015	2016
International migration, total	217.5	214.0	185.1	169.1	196.5
Including that with CIS states	197.6	199.3	179.6	165.1	191.9
Azerbaijan	13.7	12.8	10.0	8.1	7.9
Armenia	23.6	25.2	18.6	15.7	8.9
Belarus	8.7	2.1	5.1	3.2	1.6
Kazakhstan	25.9	29.5	28.8	24.9	25.6
Kirgizia	19.2	14.2	11.7	5.6	9.3
Moldova	13.1	15.0	12.3	12.5	10.6
Tajikistan	22.9	24.2	13.7	5.8	19.4
Turkmenia	2.5	2.3	1.4	1.3	0.8
Uzbekistan	41.7	47.0	30.7	-17.2	14.2
Ukraine	26.4	26.9	47.3	105.2	93.6
With far abroad countries	20.0	14.8	5.5	4.0	4.5

Source: The Rosstat.

After substantial growth due to aggravation of the situation in Ukraine in the 2014–2015 period<sup>1</sup>, forced migration to Russia stopped growing. As of the beginning of 2015, in Russia 237,800 people were registered as temporary refugees, while as of the beginning of 2016 their number amounted to 313,700 people and as of 1 October 2016 – 249,300 people. In January–September, the number of people who received temporary refuge in Russia amounted to 17,200 people, while in the respective period of the previous year it was equal to 130,300. In future, if no aggravation of the situation happens the number of such people will decrease as they settle in the territory of Russia or return to Ukraine.

As regards far abroad countries, there is still small migration growth, but one can trust the Rosstat's data on emigration from Russia with some reservations: if it is judged on the basis of recipient countries' statistical data, emigration from Russia is highly underestimated.

In 2016, the extent of the **domestic** migration did not virtually change having increased by 42,900 people or 1.4% as compared to January–September 2015. It means that on the basis of the results of the year the number of domestic migrants will exceed 4 million people and be at the level of 1980–1990 which situation was largely contributed to by changes in the methods of accounting of migration in 2011.

The two largest metropolitan areas (Moscow together with the Moscow region and St. Petersburg together with the Leningrad Region) and the Krasnodar Territory are still the main centers which attract migrants. Considerable migration growth is registered in the Tyumen Region, Crimea, the city of Sevastopol, the Kaliningrad Region as well as individual regions of Central Russia.

<sup>1</sup> In 2014, hundreds of thousands of people from Ukraine started to come to Russia and apply for a temporary refuge. In 2015, after some stabilization of the situation in the Donetsk Region and the Lugansk Region the influx of people seeking temporary refuge largely decreased.

A general increase in migration growth of Russia's population, even such an insignificant one as in 2016, results in reduction of the number of regions which lose population due to migration as population growth based on international migration makes up for the losses caused by domestic migration. Also, the migration balance of Central Russia's regions was affected by the fact that in January–September 2016 as compared to the respective period of 2015 migration growth of Moscow which is formed up to one-third at the expense of regions bordering on the Moscow metropolitan area decreased.

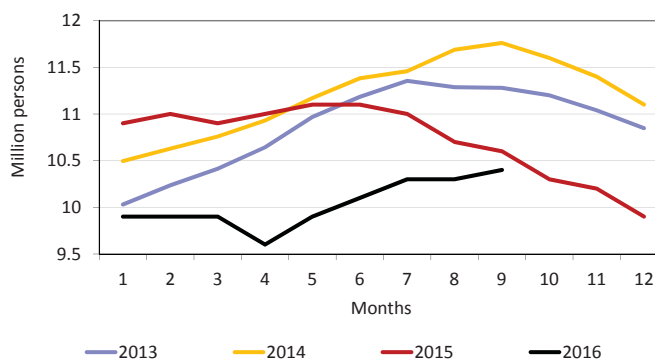
As before, migration leads to a loss of population by most regions of the Privolzhsky Federal District, the North-Caucasian Federal District and the Siberian Federal District, as well as all the regions of the Far Eastern Federal District, except for the Sakhalin Region. Early in 2016, reports came in that migration decreased in Far Eastern regions, however, according to the results of 9 months of 2016 it is not quite so. Migration fell from 16,100 people to 7,200 people, but on the basis of the results of this year it will not probably exceed 10,000 people. It is too early to speak about the breaking point of the trend.

### Temporary Migration

It is noteworthy that H2 2015 and the entire 2016 demonstrate substantially lower quantitative indices of presence of foreign nationals in Russia as compared to the level of 2013–2014 (Fig. 2). In 2016, the number of temporary foreign migrants in Russia became even lower than in 2015. In some months, the difference amounted to 1.4m people. At the same time, the 2016 data point to the fact that foreigners get one way or another accustomed to the Russian economic situation as growth in the number of foreign migrants was registered in summer (it means that season migrants returned to Russia again). As of the end of September 2016, 10.4m foreign nationals stayed in Russia. By the end of the year, their number is likely to fall.

Most foreigners in the territory of the Russian Federation are still nationals of CIS states; their share is constantly within the range of 85–86%; as of the end of September 2016 that index in absolute figures amounted to 8.8m people (Table 2).

As compared to 2014, the number of CIS nationals became on average 7–10% lower, though as regards individual countries – the main donors of workforce to Russia – the reduction was more substantial: from 10–15% (Tajikistan) to 30% (Uzbekistan). At the same time, the number of nationals from member-states of the Eurasian Economic Union keeps growing; it is to be noted that in 2016 the number of Kyrgyz nationals grew at a particularly high rate. Employers seek to take advantage of the situation with such migrants as neither permit documents for employment are required, nor need any additional monthly patent payments be made, while migrants from other CIS states have to pay for it. It is to be noted that employment rules for such migrants are virtually the same as for Russian nationals.



Source: The Central Database of Accounting of Foreign Nationals and Stateless Persons (CDAFNSP).

Fig. 2. The number of foreign nationals in the territory of Russia as of the end of a month, million people, 2013–2016

Table 2

THE NUMBER OF FOREIGN NATIONALS FROM CIS STATES IN RUSSIA  
AS OF THE SPECIFIED DATE, PERSONS

	03.09.14	01.10.2015	01.10.2016
Azerbaijan	610159	537475	531471
Armenia	531691	518731	523124
Belarus	476187	622786	741453
Kazakhstan	581257	704535	613067
Kirgizia	550136	519487	582863
Moldova	582375	525903	490844
Tajikistan	1163199	967751	999035
Uzbekistan	2509666	2038155	1779002
Ukraine	2446123	2596092	2581380
CIS, total	9450793	9030915	8842239

Source: The Main Department on Migration of the RF Ministry of Internal Affairs, CDAFNPS.

The number of foreigners from developed western countries keeps falling: from 2014 their number decreased by nearly 60%, while by some countries, even more (Table 3). So, the number of foreigners from the US and Spain fell by 80%, while that from the UK, by 83%.

Table 3

THE NUMBER OF FOREIGNERS FROM SOME EU COUNTRIES  
AND THE US STAYING IN RUSSIA AS OF THE SPECIFIED DATE, PERSONS

	13.11.13	01.10.15	01.10.16
Germany	352335	148414	116948
Spain	77200	23144	16011
Italy	77193	34908	28114
The UK	174061	50478	29739
Finland	108312	47360	94557
France	65559	38645	29697
The EU as a whole	1177829	546341	513367
The US	220086	68367	53978

Source: The Main Department on Migration of the RF Ministry of Internal Affairs, CDAFNPS.

The average annual number of foreigners coming to the Russian Federation to work (the purpose of visit is specified in the migration card at arrival) amounts to about 4m people: about 3.8–3.9m labor migrants and 170,000–180,000 labor migrants from the CIS and far abroad countries, respectively.

At the same time, the number of work permits secured by migrants in the Russian Federation does not comply with the number of migrants arriving in Russia for employment purposes. So, the issues related to regulation of labor migration are still topical, the more so in 2016 they became more acute (Table 4).

As of the end of September 2016, only 1.8m foreigners had valid work permits, while 4m foreigners stayed in the Russian Federation then as labor migrants. Even if one deducts from 4m foreign migrants about 900,000 of those who had the right to work without permit documents, that is, nationals of the member-states of the Eurasian Economic Union – it appears that *about 1.3m people were illegal labor migrants* (it is to be noted that in addition to the above there is a large number of those migrants who came to Russia on a private trip, but stayed to work without securing any work permits). The

number of migrants who enter into official relations with Russian employers is even smaller. So, within 9 months of 2016 employers sent to the RF migration authorities about 800,000 notifications on entering into a contract with those migrants who had a work permit or a patent. So, over 55% migrants who initially were legal on the labor market maintained informal relations with their employers (both legal entities and individuals). It is to be noted that out of 900,000 migrants from member-states of the Eurasian Economic Union who arrive in the Russian Federation for employment purposes, over 60% worked on an informal basis.

Table 4

EXECUTION OF WORK PERMITS FOR MIGRANTS IN THE RUSSIAN FEDERATION,  
JANUARY–SEPTEMBER, PERSONS

	9 months 2014	9 months 2015	9 months 2016
Work permits for foreign nationals*	965856	172335	95158
Work permits for skilled* and high-skilled workers	121516	46376	29362
Patents**	1943810	1479673	1193811
Total	3031182	1698384	1318331

\*From 1 January 2015, work permits are issued only to foreign nationals from countries the Russian Federation maintains a visa regime with.

\*\*From 1 January 2015, patents are issued to foreign nationals from countries with a visa-free regime for employment both with individuals and legal entities.

Source: The RF Federal Migration Service, 1-RD form.

The number and share of illegal migrants are growing. It can be explained both by economic problems and legislative barriers (the cost of execution of contractual relations and monthly payments is rather high; in addition to that a large number of migrants are banned to enter the country, so they cannot have their contractual relations executed on a legal basis).

However, even with a lack of official contractual relations with employers migrants replenish regional budgets of the Russian Federation. So, within 9 months of 2016 monthly patent payments alone (advance payments on the individual income tax) amounted to Rb 34bn with over 80% of such payments ensured by migrants from Tajikistan and Uzbekistan. ●

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