

ONLINE MONITORING OF RUSSIA'S ECONOMIC OUTLOOK

TRENDS AND CHALLENGES OF SOCIO-ECONOMIC DEVELOPMENT

№ 18 (December) 2015

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MAIN TRENDS AND CONCLUSIONS

The forecasts for 2016 represent a problem with multiple unknown variables, while those for 2015 were an equation where all the variables were unknown.

Thus, it is a well-known fact that oil prices in 2016 cannot plunge below zero. However, a year ago nobody knew if Russia was going to be subjected to the same embargo on oil exports as that introduced against Iran; if Russia's cut off from SWIFT was to become a reality; if it would be worthwhile to keep bank credit cards as financial relics; if the banking system might collapse while being raided by bank clients; if the rouble-to-euro exchange rate could double by the end of 2015, rising from Rb 100 to Rb 200; and if the flag of the so-called Novorossia would be raised over, say, Odessa – a development that would have indeed predetermined affirmative answers to all the previous questions. By comparing the initial conditions and facts of the two forecasts – which are divided by only a one-year period – we may come to the conclusion that they differ significantly, and even decisively in some of their fundamental aspects. This conclusion, in its turn, helps us to be more moderate in our estimates of the least certain prospects for the coming year 2016.

Among other things, we still do not know for certain if the current recession will finally be brought to a halt – and if so, when this may happen – in Q2 or Q4. We also do not know at what rate, 0.5% or 1.0%, GDP will then start to grow; how the inflation index is going to behave a year from now – if indeed it can decline to a one-digit figure; if the Reserve Fund will be fully spent over the course of next year, and if not – which budget expenditure items will be subject to cuts, and if the defence items are going to be left intact once again. The different answers to these questions vary significantly in terms of statistics rather than economics, because they imply the emergence of neither any fundamentally new conditions nor any important new trends.

Nevertheless, the measures designed to create some new preconditions for an improvement in the current situation or to prevent its further deterioration appear to be quite important. Among these, we may point to the RF Central Bank's decision to keep the key interest rate at its present level. This has been done with due regard for the current inflation expectations, which remain high as a result of the plummeting oil prices towards the year's end, followed by the downward movement of the rouble's exchange rate against world major currencies. However, no excessive volatility (let alone panic) can be observed in the FX market, it shows nothing at least remotely resembling the developments of last year. The low demand for foreign exchange displayed by banks (further smoothed down by the reintroduction of FX REPO auctions by the RF Central Bank) is an evidence of the continuing stable situation in that market. This does not mean, however, that the rouble is safe from any additional depreciation in response to a new plunge of the oil prices, but the decline of its exchange rate will be relatively slower and more gradual than the movement of oil quotes.

As before, one of the factors responsible for this relative stability in the foreign exchange market has been Russia's persistently positive foreign trade balance. Importantly, over the course of 2015, both exports and imports have been declining practically at the same pace. Moreover, in spite of some serious mac-

roeconomic shifts, the structure of foreign trade turnover has changed only insignificantly. Exports demonstrated a somewhat shrinking share of mineral resources, while imports displayed the same structure, with an increasing share of cheaper and poorer-quality versions of the same items. The pass-through effects of the rouble's exchange rate decline differed depending on specific groups of Russian exporters. Thus, while the prices denominated in USD for Russian mineral fertilizers, machinery and equipment, aluminium, and motor vehicles slightly declined, the suppliers of these commodities gained no less than 60% in terms of their rouble-denominated prices, which was a significant advantage because their main costs were denominated in the national currency. Meanwhile, the suppliers of ferrous metals, when faced with plunging prices denominated in foreign currencies, could not get an adequate compensation in rouble terms.

The pass-through effect of the rouble's exchange rate decline in Russia's metallurgy has been gradually receding. The declining world demand for metal products, largely determined by China's shrinking demand, pushed down their prices. Moreover, the domestic market also demonstrated a downward movement of both demand and prices. Russian metallurgy, which on the whole had been performing quite well, was now faced with a tricky situation. In response to the shrinking domestic demand (in machine-building and the construction sector), the producers had to increase their exports in terms of physical volume, while these had been dwindling significantly in terms of value.

General demand shrinkage can also be observed across Russian industry. As a consequence, production growth in November was also very weak, as testified by the results of a business survey of Russian companies. However, at the same time they report their rather optimistic production plans (in industry): this trend has been visible throughout all the recent months, having now reached its four-year high. As before, companies display a desire to depart from the bottom of the current crisis, and so they have even begun to change their pricing policies, now reducing the prices for their products, whereas over the previous months their prices were on the rise.

The data on the reasons for dismissals of employees as explained by the managers of industrial enterprises (these have been monitored annually since 2012) are rather interesting. The share of enterprises reporting no dismissals has hit its record high of 27%. Meanwhile, in 2015 the share of those who quit because of a low pay shrank to its four-year low. The share of those who estimated their salary size as 'normal' rose to its historic high of 70% (during the 2008–2009 crisis it had been as low as 37%). Besides, employees became less choosy with regard to their working conditions; in 2015, dissatisfaction with these conditions (as well as violations of employee discipline) are cited 1.5–2 times more rarely as a reason for quitting a job than back in 2012. By way of summing up, we may come to the following conclusion: people are now more afraid of losing their jobs.

This is by no means surprising: real incomes, wages and pensions have been on the decline for a year already. In particular, in 2015 incomes declined in 73 regions, while in 2009 this trend had been observed only in 48 regions. On the whole, the current income decline can largely be explained by the shrinkage of pensions in real terms, whereas in 2009, on the contrary, pensions had sharply increased, thus sustaining the overall personal income level. Neither consumption nor demand has been sustained by lending sources. People now borrow on a lower scale than they did last year, and they do so largely because they want to redeem their existing debts. If this had not been happening, the current share of outstanding debt (8% as of early October) would have been even more impressive. ●

1. RUSSIA'S FOREX MARKET: NO PANIC OUTLOOK

A.Bozhechkova, P.Trunin

The Bank of Russia on 11 December 2015 decided to keep the base interest rate unchanged at 11%, thus indicating that the bank will not move forward with easing monetary policy. Russia's Central Bank on 14 December resumed 12-month foreign exchange repo auctions with a view to pushing down demand for foreign currency. Thus, the Bank of Russia aims to avoid turbulence in Russia's financial markets, which may occur in response to a new downturn of oil prices amid raised Fed target rates.

Keeping the base interest rate unchanged, after stepwise cuts until August 2015, appears reasonable amid slower decline of inflation and higher risks to financial sustainability.

Inflation was declining at a very slow pace (15.7% in September, 15.6% in October, 15% in November compared to the same periods of 2014) after the year over year hike to 15.8% at end-August 2015. It would be unreasonable to cut the base rate amid high risks of inflation and further depreciation of the rouble, uncertain dynamics of oil prices, geopolitical tensions, investors' expectations that Fed's monetary policy would be further tightened. Nevertheless, the Bank of Russia has sent a signal to market participants that the monetary policy will be eased as long as inflation declines and the situation is stabilized.

The Consumers Price Index (CPI) in November 2015 gained 0.8% (1.3% in November 2014), 0.1 p.p. higher than the value seen in October 2015. Consumer prices during the first two weeks of December increased further 0.4%. Sluggish economy, moderate growth in money supply restrain inflation. However, the cumulative effect of the exchange rate pass-through to prices, as well as high risks of further depreciation of the rouble's exchange rate late in 2015 – early in 2016 are responsible for keeping inflation up, which may as well be higher than 13% at 2015 year-end.

It is noted in the Bank of Russia's monetary policy report for November 2015 that, according to surveys conducted by OOO INFORM (a limited liability company), in November inflation expectations were up 0.5 p.p. to 15.8%, because individuals expected that the rouble would depreciate by the end of the year. High inflation expectations is an obstacle to softer monetary policy, restraining slowdown of real inflation.

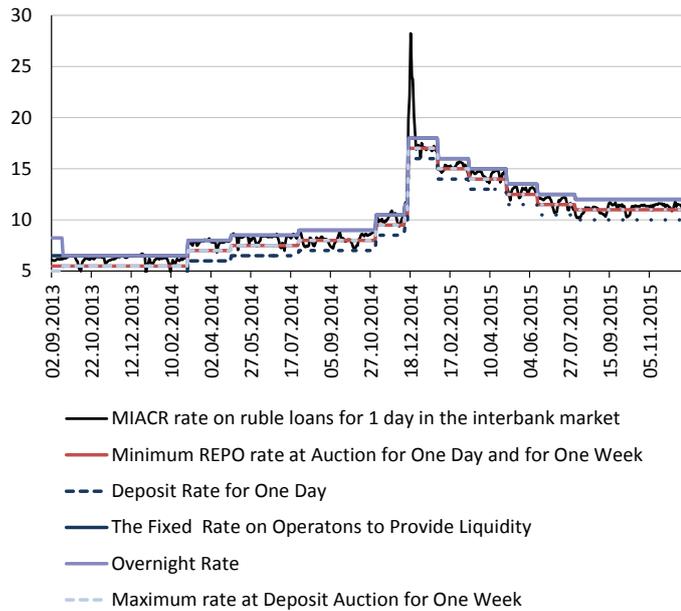
In the period between November and the first half of December 2015, the MIACR (Moscow InterBank Actual Credit Rate) on overnight interbank loans denominated in roubles didn't hit the interest rate band cap, staying at an average range of 11.3–11.4% (Fig. 1), thus evidencing that the Bank of Russia has been carrying out an efficient interest rate policy in terms of achieving the goal of converging interbank credit interest rates and the base interest rate.

At the same time, in the fall of 2015 credit institutions showed less demand for central bank's loans due to the fact that the monetary base increased as money of the Reserve Fund was spent. Banks' debt to the Bank

of Russia on rouble-denominated repos in November decreased by 12% to Rb 1.0 trillion. Additionally, banks' debt on loans secured by non-marketable assets contracted by 8.3% to Rb 2.3 trillion. Banks' foreign exchange debt to Russia's Central Bank in November – first half of December decreased too, by 16%. According to the data as of 21 December 2015, banks owed \$23.7bn to Russia's Central Bank on foreign exchange repos, including \$19.8bn on one-year repos and \$3.9bn on 28-day repos. The reduction in the debt on 12-month loans (down 23.9% in November – first half of December 2015) contributed most to the contraction of banks' foreign exchange debt to the Central Bank (Fig. 2).

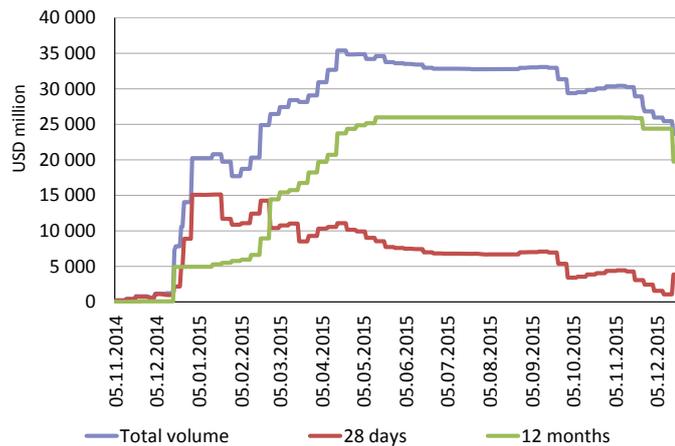
Hence, banks showed less demand for foreign exchange refinancing, despite a new weakening of the rouble's exchange rate, considerable foreign debt repayments in December (\$20.8bn of repayments of principal, \$2bn of interest payments according to the foreign debt repayment schedule) and a hike in Fed rates. It appears that credit institutions still have sufficient foreign exchange reserves, which were accumulated in the previous year. Furthermore, in an effort to push down demand in the forex market, Russia's central bank said on 27 November it would resume from 14 December 2015 foreign exchange repo auctions for a term of 12 months. Furthermore, the Bank of Russia increased the minimum rate for this type of actions by LIBOR plus 3 p.p. (previously, LIBOR plus 2.5 p.p.). As a reminder, the Bank of Russia on 18 May 2015 suspended one-year foreign exchange repos due to stable situation in the forex market.

Only \$201.3m was raised at 4.067%, with a limit of \$1bn, at a one-year repo auction held on 14 December. Note that low demand for the auction was determined by high value of funding. A foreign exchange repo auction for a term of 28 days was held on 14 December, which appealed more to commercial banks. Credit institutions raised \$2.9bn at 2.35%. With this interest rate policy in place, Russia's Central Bank will facilitate changes in favour of one-month repo auctions in the composition of the foreign exchange debt owed by banks to the Central Bank.



Source: The Central Bank of Russia.

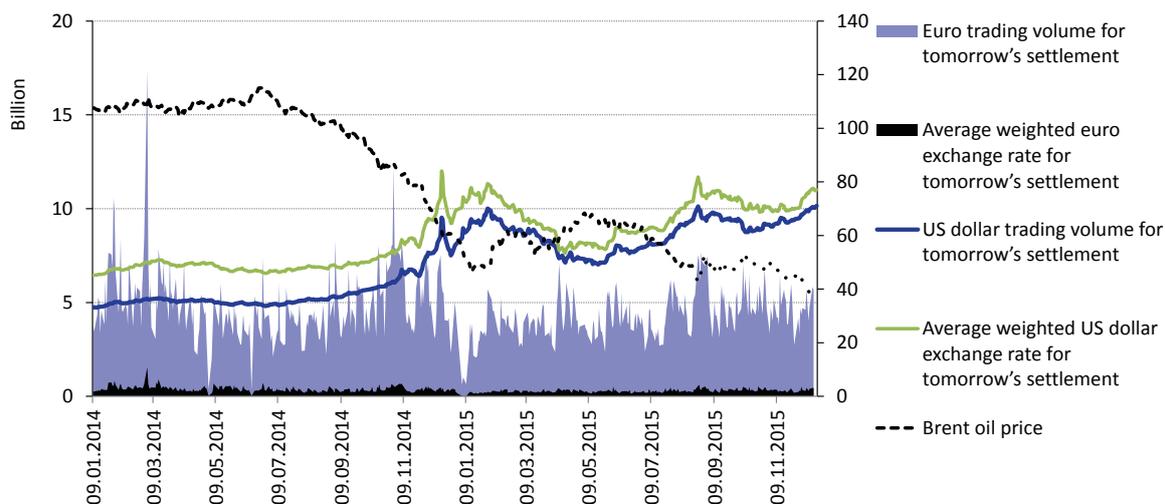
Fig. 1. The Bank of Russia interest rate band and the dynamics of the interbank lending market in 2012 to 2015, % p.a.



Source: the Bank of Russia.

Fig. 2. Banks' debt to Russia's Central Bank on foreign exchange repos in 2014–2015

1. RUSSIA'S FOREX MARKET: NO PANIC OUTLOOK



Sources: Russia's Central Bank, ICE.

Fig. 3. Russia's forex market and crude oil prices in 2014–2015

Overall low foreign exchange demand by banks is indication that the forex market is being stable and there is low risk of panic similar to that seen late in 2015. This by no means indicates that the rouble's exchange rate may not depreciate if oil prices keep falling. In the period between November and the first half of December 2015, the rouble already lost 10.3% against the US dollar, from 63.8 to 70.4 roubles per US dollar, and the euro gained 9.4% against the rouble, up to 77.04 roubles per euro, while the value of the euro-dollar basket increased 10.5% to 73.9 roubles. As a result, the official rouble-dollar exchange rate on 19 December touched an all-time high of 71.32 roubles per US dollar (Fig. 3). The decline in oil prices (down 22.7% in the period between November – first half of December 2015) was the key factor responsible for the rouble's depreciation.

According to our estimates, the rouble's real effective exchange rate is currently being nearly equal to the equilibrium value, which is determined by fundamental factors (oil prices, economic growth rates, capital outflows and government spending). Additionally, because of high inflation in 2015, despite the rouble's depreciation in August and October–November, the rouble's real effective exchange rate is 6.5% higher than that in December 2014 and nearly equal to that seen in June 2005. Hence, we do not expect that Russia's national currency would keep depreciating substantially if prices of energy resources are stabilized. ●

2. EXPORT–IMPORT: ERA OF STAGNATION

A.Knobel

Preliminary results for 2015 have shown no substantial structural changes in both imports and non-energy exports. The import structure is most stable: the percentage share of chemical industry products, which are used basically as by-product in the domestic manufacturing industry, has seen some increase. This is indicative of similar response by various commodity groups to the depreciation of the national currency. The weakening of the rouble's nominal exchange rate by 65% has kept dollar prices of imported high conversion products at the same level and pushed down (by 20–40%) dollar prices of agricultural products, foods and low conversion products.

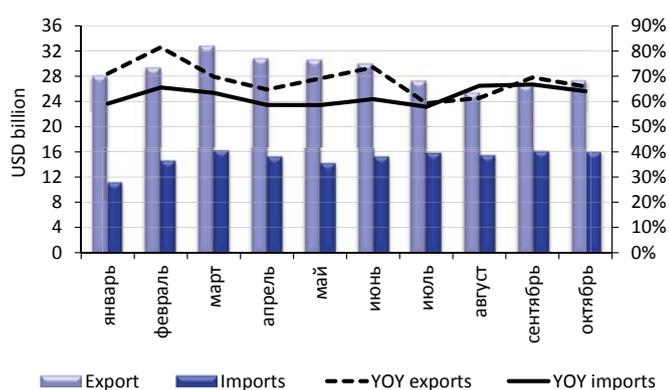
Export and import dynamics

Total exports and imports

In the first 10 months of 2015, the dynamics of exports and imports underwent almost simultaneous changes (Fig. 1). Foreign trade balance remained positive throughout the entire 2015. Exports, despite changes in global prices of energy resources, saw less decline (except in August) than imports which were influenced primarily by deteriorated purchasing power of the Russian rouble. Total imports in January–October 2015 amounted to \$150.4bn, or 62.0% on a year over year basis, and total exports ran at \$288.7bn or 68.2% y-o-y.

Exports as a percentage of the 2014 values showed a downtrend despite undulating changes. Imports were more stable, varying within a narrow range of 58% to 66% of the values seen last year.

Import volumes (expressed in US dollars) declined least for such commodity items as “Chemical products and mineral products” (FEACN 25-40) and “Food products” (FEACN 16-24), 71.6% and 65.1% of the previous year volumes, respectively, whereas the decline hit most such items as “Means of transport” (FEACN 86-89) and “Metals and articles thereof” (FEACN 71-83), 48.8% and 59.5%, respectively. Export volumes declined least for such commodity items as “Chemical products” (FEACN 28-40) and “Machinery, equipment, and means of transport” (FEACN 84-90), 88.3% and 87.6% of the previous year volumes, respectively, whereas the decline hit most such items as “Mineral products” (FEACN 25-27) and “Textiles and footwear” (FEACN 50-67), 61.8% and 77.2%, respectively.



Source: calculated using the data released by Russia's Federal Customs Service.

Fig. 1. Russia's foreign trade dynamics in 2015

Import and export structure

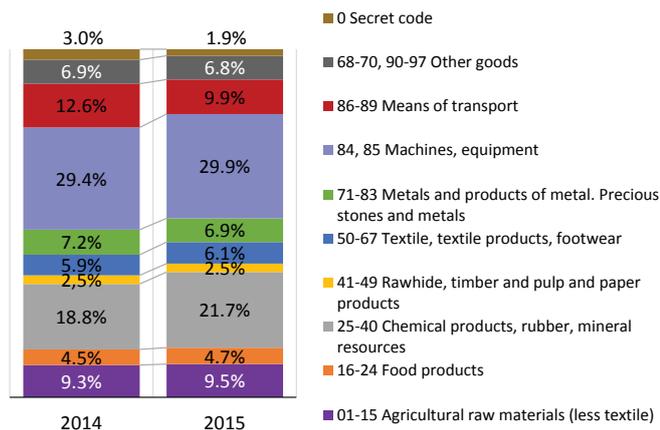
Russia’s import structure saw no drastic changes (Fig. 2). The share of means of transport shrank most (from 12.6% to 9.9%), whereas that of chemical products and minerals increased from 18.8% to 21.7%.

Most changes in Russia’s export structure (Fig. 3) were caused by a decrease in the share of mineral products (from 71.7% to 65.0%). This entailed an increase in the share of the rest of groups of commodities of total exports, although their relative proportions actually remained unchanged (Fig. 4).

Changes in the average price of some goods

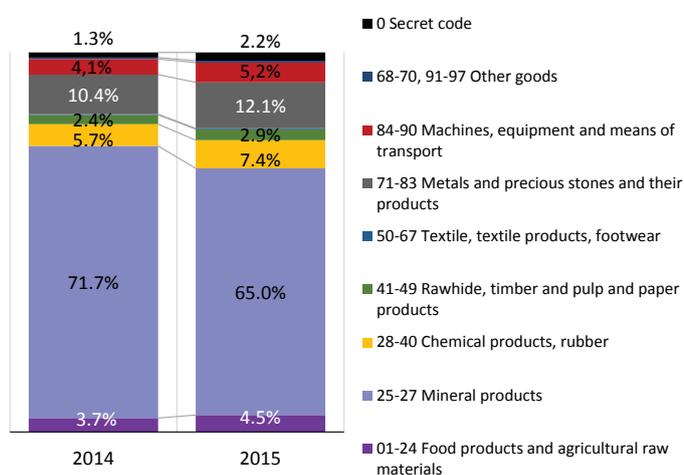
Judging from changes in average import prices (Table 1), dollar price declined for most of the commodities. For instance, the average price of all food products and footwear fell, except that the price of tea remained unchanged. Prices of the four of six commodity items saw a decline within a range of 9.5–19%. The decline can be explained by both importers (and consumers) refocusing toward cheaper imported commodities (decline in imports of expensive products, also because of a ban on specific products) and depreciation of the national currency of the key importing countries. For instance, the decline of average price of milk and cream was related primarily to devaluation of the Belorussian rouble (Belarus accounts for a major part of milk imported by Russia).

The decline of prices of imported metals reflects the dynamics of global prices of these commodities. Prices of steel pipes and passenger cars declined moderately. The considerable growth in prices of imported lorries can be explained by a decline in imports of low-end lorries which failed to compete with second-hand and domestically manufactured counterparts.



Source: calculated using the data released by Russia’s Federal Customs Service.

Fig. 2. Russia’s import structure in January–October 2014 and January–October 2015



Source: calculated using the data released by Russia’s Federal Customs Service.

Fig. 3. Russia’s export structure in January–October 2014 and January–October 2015

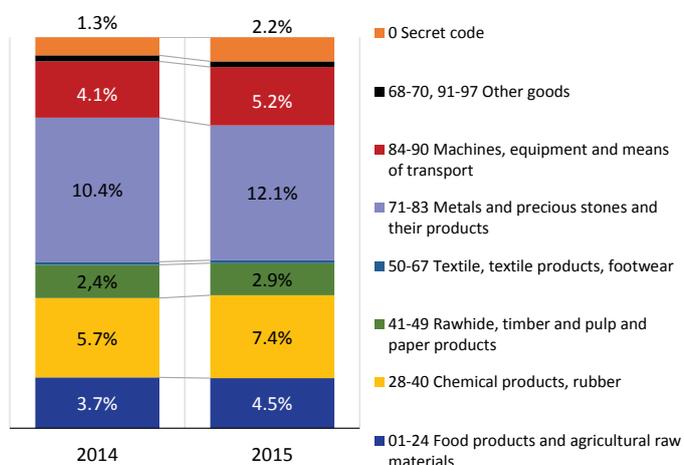


Fig. 4. Export structure, except mineral resources, in January–October 2014 and January–October 2015

Table 1

AVERAGE IMPORT PRICES OF SOME VITAL COMMODITIES

FEACN CODE	Commodity item (unit of measurement)	Price in 2015, US dollars	Price in 2014, US dollars	Price change in terms of US dollars	Price change in terms of roubles*
0201–0204	Fresh and frozen meat (kg)	3.39	4.17	-18.7%	35.4%
0302–0304	Fresh and frozen fish (kg)	2.56	2.94	-12.8%	45.1%
0402	Milk and concentrated cream (kg)	2.07	3.77	-45.1%	-8.6%
0805	Citrus fruits (kg)	0.81	0.99	-18.7%	35.3%
0902	Tea (kg)	3.70	3.66	1.0%	68.2%
6403	Leather footwear, (pairs)	23.50	25.95	-9.5%	50.7%
72	Ferrous metals (kg)	0.74	0.91	-18.7%	35.3%
7304–7306	Steel pipes (kg)	1.65	1.69	-2.4%	62.5%
84–90	Machinery and equipment (tons)	11,391	11,636	-2.1%	63.0%
8703	Passenger cars, (pieces)	18,667	19,457	-4.1%	59.7%
8704	Lorries, (pieces)	40,246	32,320	+24.5%	107.3%

* Rouble's average exchange rate in January–October 2014 was 36.07 roubles per US dollar; Rouble's average exchange rate in January–October 2015 was 60.03 roubles per US dollar.

Source: calculated using the data released by Russia's Federal Customs Service.

Similar to import prices, average dollar export prices (*Table 2*) dropped for all of the goods in question, except lorries. Additionally, even average rouble prices of crude oil and refined petroleum products fell 13.0% and 7.3%, respectively. Note that the decline in prices of wheat, coal, natural gas and metals stays within the dynamics of prices of the same goods in global markets.

Dollar prices of such commodity items as aluminium, fertilizers and motor vehicles declined least.

Also, note that the decline in dollar prices of imported goods also reflects the weakening of the national currency of Russia's major trade partners against the US dollar. For instance, in January–October 2015 the average US dollar exchange rate against SDR¹ (0.713 SDR = 1 dollar) was 9% higher than the value seen in the previous year (0.653). Consequently, the average weighted (in trade with Russia) weakening of trade partners' national currency against the US dollar was 15–17%.

Thus, commerce underwent no structural changes despite serious changes in macroeconomic conditions: the Russian economy shows demand for approximately the same imported goods basket as previously, and the structure of non-energy export supply remained the same, except for some changes in sales geography and refocusing, wherever possible, toward less expensive and lower quality products, namely low conversion products, agricultural products and food products. To date, no success has been achieved in refocusing toward sales at lower (dollar) prices of groups of commodities such as means of production, component parts, machinery and equipment.

1 Special Drawing Rights (SDR) refer to an artificial reserve and payment instrument issued by the International Monetary Fund, which provides a cashless form of bank account entries. SDR is calculated using dollar value of a basket comprised of the four key currencies, namely the US dollar (41.9% of the basket), the euro (37.4% of the basket), the Japanese Yen (9.4% of the basket) and the British Pound (11.3% of the basket);

Table 2

AVERAGE EXPORT PRICES OF SOME VITAL COMMODITIES

FEACN CODE	Commodity item (unit of measurement)	Price in 2015, US dollars	Price in 2014, US dollars	Price change in terms of US dollars	Price change in terms of roubles*
1001	Wheat and meslin (tons)	189.1	249.9	-24.3%	+25.9%
2701	Coal (tons)	64.0	78.1	-18.0%	+36.4%
2709	Crude oil (tons)	381.3	729.4	-47.7%	-13.0%
2710	Refined petroleum products (tons)	405.8	728.5	-44.3%	-7.3%
2711210000	Natural gas (thousand cub. m)	233.9	326.5	-28.3%	+19.3%
2716	Electric power (thousand kWh)	41.3	52.8	-21.8%	+30.2%
3102-3105	Fertilizers (tons)	283.4	290.1	-2.3%	+62.6%
72	Ferrous metals (tons)	375.0	530.0	-29.2%	+17.8%
7403	Refined copper (tons)	5,627	6,758	-16.7%	+38.6%
7502	Raw nickel (tons)	12,112	16,644	-27.2%	+21.1%
7601	Raw aluminium (tons)	1,840	1,874	-1.8%	+63.5%
84-90	Machinery and equipment (tons)	11,578	12,038	-3.8%	+60.1%
8703	Passenger cars (pieces)	11,093	11,539	-3.9%	+60.0%
8704	Lorries (pieces)	23,444	22,812	+2.8%	+71.1%

*Rouble's average exchange rate in January-October 2014 was 36.07 roubles per US dollar.

Source: calculated using the data released by Russia's Federal Customs Service.

3. RUSSIAN METALLURGY: THE ROUBLE WEAKNESS ALONE DOES NOT SUFFICE ANY LONGER

G.Idrisov, Yu.Ponomarev, S.Sudakov

The current change in expectations concerning the prospects of global economy development is reflected in weakening demand for metallurgy products, primarily in China. International and Russian domestic producer prices for the major types of metal goods continue to decline. The rouble weakness no longer suffices for the Russian metallurgical industry to sustainably overcome the slump, let alone to resume its development. The dwindling domestic demand has pushed up Russian metallurgy exports in physical terms, although they have significantly declined in money terms.

In 2015, world market prices for metallurgy products continue to decline (Tables 1 and 2). The major reason for their decline is the adjustment of the demand-supply balance to the changing expectations concerning the prospects of global economy development. In particular, there is a weakening of demand for metallurgy products¹, first of all in China², a country that has been playing the most important role on the world metal market during the past several decades.

Table 1

AVERAGE MONTHLY PRICES FOR THE MAJOR TYPES OF NON-FERROUS METALS AT LME IN DECEMBER 2014 – NOVEMBER 2015, USD / T

	Dec. 14	Jan. 15	Feb. 15	Mar.15	Apr. 15	May 15	Jun 15	July 15	Aug.15	Sep. 15	Oct. 15	Nov 15
Unalloyed aluminium	1,909	1,815	1,818	1,774	1,819	1,804	1,688	1,640	1,548	1,590	1,516	1,468
Refined copper	6,446	5,831	5,729	5,940	6,042	6,295	5,833	5,457	5,127	5,217	5,216	4,800
Unalloyed nickel	15,962	14,849	14,574	13,756	12,831	13,511	12,825	11,413	10,386	9,938	10,317	9,244

Source: World Bank data.

Table 2

AVERAGE MONTHLY WORLD MARKET PRICES FOR STEEL PRODUCTS IN DECEMBER 2014 – AUGUST 2015, USD/T

	Dec.14	Jan.15	Feb.15	Mar.15	Apr. 15	May 15	June 15	July 15	Aug. 15
Hot-rolled coil	576	548	519	495	471	479	469	463	452
Rolled sheet	685	658	617	586	556	552	541	533	523

1 According to the forecasts released by the World Steel Association, in 2015 demand for steel will fall by 1.7% relative to 2014. See 'Worldsteel Short Range Outlook 2015–2016', URL: [<https://www.worldsteel.org/dms/internetDocumentList/press-release-downloads/2015/Short-Range-Outlook-2015-2016/document/Short%20Range%20Outlook%202015-2016.pdf>].

2 In September 2015, demand for steel in China declined by 8.7% relative to September 2014. At the same time, it is expected that during the next 10 years steel production in China will fall by at least 10%. See URL: [<http://www.afr.com/business/mining/iron-ore/steel-output-drops-in-china-as-maize-flags-iron-ore-mismatch-20151111-gkwru3>]; [<http://www.vedomosti.ru/business/articles/2015/12/08/620023-stali-snizhat-tseni>].

3. RUSSIAN METALLURGY: THE ROUBLE WEAKNESS ALONE DOES NOT SUFFICE ANY LONGER

	Dec.14	Jan.15	Feb.15	Mar.15	Apr. 15	May 15	June 15	July 15	Aug. 15
Cold-rolled coil	663	632	601	582	554	563	550	548	540
Hot-galvanized coil	758	730	701	682	649	658	646	645	627
Wire rod	593	576	553	521	515	511	503	512	494
Rebar	580	562	538	516	508	508	498	497	484

Source: the independent information agency MEPS (International) Ltd.

The rouble's considerable weakening that compensated Russian metallurgists for their losses from the decline in world market prices in late 2014-early 2015 has come to an end, thus resulting in a steady decrease of domestic prices in roubles for most of the types of metallurgy products in the second half of 2015 (*Table 3*).

Table 3

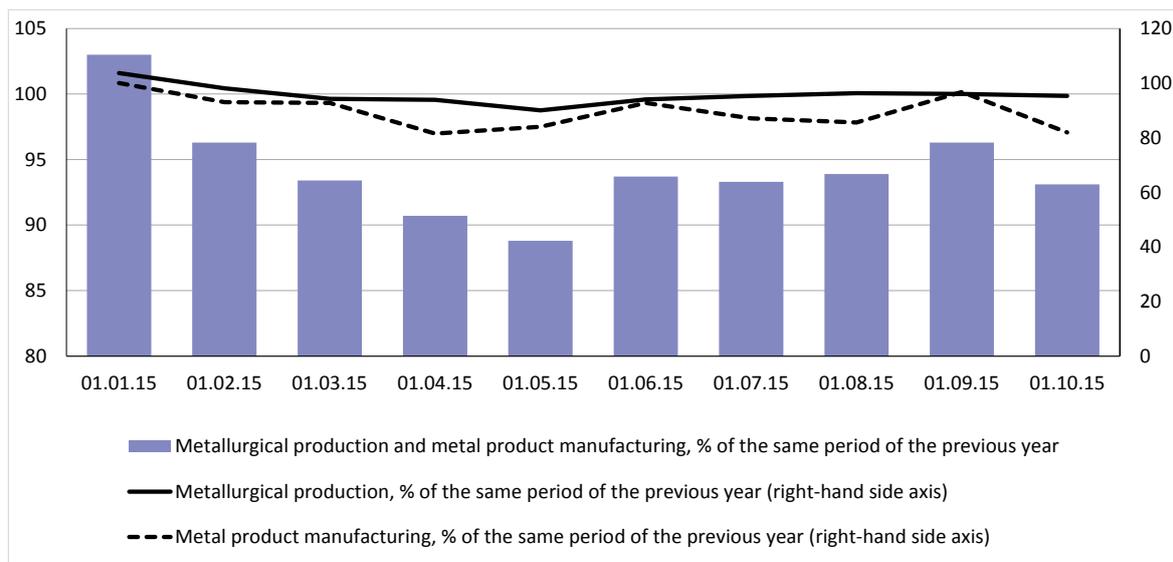
RUSSIAN DOMESTIC PRODUCER PRICES FOR THE MAJOR TYPES OF METALLURGY PRODUCTS

	Ratio of prices in October 2015 to prices in January 2015	Ratio of prices in October 2015 to prices in October 2014	Average monthly growth rate of prices (relative to previous period) over January–October 2015
Unprocessed aluminium, t	92%	141%	-0.6%
Refined unalloyed unprocessed copper, t	97%	134%	-0.2%
Unalloyed nickel, t	74%	97%	-3.1%
semi-finished steel products, t	72%	93%	-3.3%
Hot-rolled steel sheet (except stainless and high-speed steel), t	108%	120%	1.0%
Cold-rolled steel-plated sheet (except stainless and high-speed steel), not less than 600 mm in width, t	115%	121%	1.7%
Merchantable crude iron ore, t	91%	105%	-0.8%
Steel tubes, t	103%	115%	0.5%
Cast iron, t	64%	85%	-4.3%

Source: Rosstat, the authors' calculations.

In 2015, Russian metallurgy has shown a notable decline in production volumes: over the period January 2015 – October 2015, the Index of Metallurgical Production amounted to 94.2% relative to the same period of the previous year (the month-on-month movement of production volumes is shown in *Fig. 1*); in particular, there was also a fall in production of the major types of non-ferrous metals: primary aluminum – 96.4%, refined unalloyed unprocessed copper – 99.4%, and unprocessed nickel – 96.8%. The main factors behind the drop in metallurgy production volumes were as follows:

- decline in the prices of metals and metallurgical products;
- rise in transportation costs (for example, the introduction of an extra charge to railway tariffs for exporting metals; although from 1 January 2016 this extra fee will be cancelled, its cancellation cannot have a



Source: Rosstat.

Fig. 1. The Index of Metallurgical Production in January–October 2015, Relative to the Same Period of the Previous Year

significant impact on the authors' conclusions, because it has already played some role in 2015¹);

- erection of trade barriers by third countries (for example, Canada introduced antidumping duties on Russian thin hot-rolled carbon steel plates and thin high-strength low-alloy steel plates²; at the end of 2015, the European Union also introduced minimum-import prices on electrical steel produced by the Novolipetsk Iron and Steel Works³ and prolonged its antidumping duties on welded pipes from Russia until 2020⁴; the USA has begun to revise its antidumping measure regarding Russian hot-rolled steel for the delivery period 19 December 2014–30 November 2015⁵, and has initiated an antidumping investigation regarding the export of cold-rolled steel from Russia⁶);
- decline in domestic demand for metallurgical products on the part of major consumer branches (machine-building, building construction⁷ etc.) due to the rise of crisis phenomena in the economy.

1 The charge to railway tariffs for exporting metals amounts to 13.4%, see URL: [<http://www.vedomosti.ru/business/articles/2015/11/25/618213-metallurgii-prosyat-otmenit-eksportnuyu-nadbavku-rzhd>].

2 These duties are also extended to products from India, see also URL: [<http://www.metalinfo.ru/ru/news/81075>].

3 See URL: [<http://www.kommersant.ru/doc/2868443>].

4 See URL: [<http://www.vedomosti.ru/business/articles/2015/06/10/595878-kak-rossiiskie-metallurgi-boryutsya-za-klienta>].

5 See URL: [<http://economy.gov.ru/minec/about/structure/depsvod/20151207>].

6 See URL: [<http://www.interfax.ru/business/457635>].

7 Over the period January 2015 – October 2015, the Construction Production Index and the Machinery and Equipment Production Index amounted to 89.7% and 87.7% respectively, relative to the same period of 2014.

The decline in domestic demand for metals¹ resulted in a rise in the physical volume of the major types of metallurgical exports during the first 9 months of 2015 relative to the same period of 2014, although with a rather significant loss in value due to the drop in world market prices:

ferrous metals	+5.6% in terms of weight, -25.2% in terms of value
cast iron	+15.8% in terms of weight, -17.0% in terms of value
refined copper	+104.5% in terms of weight, +71.0% in terms of value;
unprocessed nickel	-5.4% in terms of weight, -30.6% in terms of value;
hot-rolled products ²	+2.2% in terms of weight, -26.2% in terms of value;
cold-rolled products ³	-10.7% in terms of weight, -31.5% in terms of value.

All these circumstances have resulted in a decline of the income and profitability of Russian metallurgical enterprises both in the domestic market (during the first 9 months of 2015, the incomes of the Novolipetsk Metallurgical Plant, *Severstal*, and the Magnitogorsk Iron and Steel Works dropped by 21%, 22.1% and 25%, respectively) and in the export-oriented segment⁴. At the same time, the government's initiatives⁵ (such as the requalification of metallurgical wastes, the construction of wastewater treatment plants, the introduction of payments for electric supply reserve capacity, the obligatory purchases of products from small and medium-size enterprises etc) are exerting additional pressure on the metallurgical industry.

The current situation in the Russian economy as a whole and in the metallurgical industry in particular further increases the existing challenges for the sustainable development of the domestic market of metals and metallurgical products: first, the challenge for the improvement of wastewater treatment at the existing iron and steel works and for the modernization thereof, as well as for the creation of new iron and steel works capable of producing high value-added products in the course of implementing the metallurgical industry's plan for imports substitution; second, the challenge for the optimization of logistics and market outlets – the share of the logistics component in the cost of domestically produced metallurgical products is rather high, which is especially important because of the accelerated growth of prices for goods and services in conditions of a dynamically developing economic situation; third, the challenge for the quest for a new demand-supply balance both in the domestic and external markets, that would bring about, as a consequence, the achievement of an agreement between the largest producers and consumers of metallurgical products. ●

1 The drop in domestic demand for non-ferrous metal in October 2015 amounted to 17.7% relative to the same period of 2014 (or to 19.8% since the beginning of the year), while the drop in demand for ferrous metals amounted to 3.4% relative to October 2014 (vs. 4.3% over the period January 2015 – October 2015 relative to the same period of 2014). See URL: [http://ipem.ru/files/files/index_archive/2015_10_ipem_index.pdf].

2 Commodity group 7208. In October 2015, the drop in this commodity group's exports in terms of weight amounted to 29% relative to October 2014.

3 Commodity group 7209.

4 See URL: [<http://www.vedomosti.ru/business/articles/2015/11/19/617459-metallurg-ne-hotyat-velichivat-nagruzku-197-mlrd-roublei>].

5 Ibid.

4. RUSSIAN INDUSTRY: OPTIMISTIC TRAGEDY

S.TSukhlo

Amid slack demand, Russian industrial production growth keeps on low. So far, enterprises remain optimistic regarding output plans. They do not revise stock of finished goods projections. Despite increase of costs, enterprises start slash prices on their products.

Industrial products demand

In November, the initial data on industrial products sales has not changed much compared to October and remained in the red. When seasonally adjusted, it has demonstrated a slight improvement but missed transition from 'minus' side to 'plus' side. Thus, demand continues moving down, however, not so fast as over the recent months. Nevertheless, improvement of the seasonally adjusted balance of sales movement constitutes just 2 p.p., which is obviously insufficient for sustainable trends in the output dynamic to take shape.

In October, satisfaction of enterprises with sales volume fell by 8 p.p. and went up 2 p.p. in November. As before, industry remains discontent with the low volumes of demand. However, the level of frustration with slack demand is far from the classical crisis one (2008–2009 template) when the share of 'below norm' responses hit 80%. At present, this indicator comes to modest 48%. To note, in 2011, it's values fell to 36-40%.

Demand forecasts do not express optimism. Over entire H2, they have remained (seasonally adjusted) around 'zero', in other words, sales growth projections are offset by expectations of their reduction, which sums up economic outlook quite properly.

Industrial output

Flat demand forced industry to revise output volumes. According to enterprises' assessments, seasonally adjusted November industrial growth rate is significantly below the September-October values. However, according to official statistics, one should not expect essentially negative values of the indicator. Industrial production growth rate will remain zero, provoke next cycle of contest for improvement of indicators by way of time series adjustment from seasonal, and calendar factors. Nevertheless, any result will not tell on the substantive assessments of the situation: industry is undecided about its output growth in statistically indisputable (or distinct) volumes.

Users of less informative set of indicators released by official statistics are forced to analyse sectoral and subsectoral data on output in the hope of revealing "crisis bottom" even at the sectoral level likewise it was fashionable to search for "point of growth" or "points of crisis". However, detection of the sectoral "bottom" with the help of statistical microscope will not add to understanding of Russian industry's state specifics for 2015. An extended set of indicators is required for a balanced understanding of the current situation. These include enterprises' plans and forecasts.

In spite of slack demand and zero forecast balance for its reverse, industrial production plans following July slump are getting momentum. Principal surge of the indicator was in August (5 p.p.). Then, its values were growing by 1–2 point per month and by November reached +22 balance points, which is a four-year high. Thus, industry retains its wish to leave behind the present crisis.

Stock of finished goods

Industry is not only ready to leave behind slow-rolling crisis but believes in the feasibility of this way out. Estimates of stock of finished goods represent an example. Since May 2015, responses “above norm” retain moderate (and by far from crisis!) predominance over “below norm” responses. In 1999–2000, the situation was developing far otherwise. Thereafter, industry amid an obvious growth of effective (not barter) demand continued keeping stock of finished products primarily at “below norm” level purposefully. Then, the share of such responses hit 40% and retained pre-eminence over other estimates of stocks from October 1998 to December 1999. Industry started to sustain reasonable excess (positive balance “above norm” – “below norm”) just in early 2001, in other words, two years after the post-default demand growth.

Business pricing policy

Enterprises not only retain faith in the feasibility of leaving 2015 crisis behind but also take practical steps in that direction. For example, by introducing substantial changes in their pricing policy. For instance, according to November survey, industry started slashing prices on its products following four months of their rather intensive and stable growth. Subsequently, indicator’s balance (growth rate) has moved down during the month from +8 to -3 points.

Herewith, costs of enterprises in Q4 continued growing at a greater pace than in Q3 2015. Indicator’s balance up from +30 to +39 points. In Q2 (May) enterprises estimated growth rate of their costs with balance of +13 points. Forecasts of changes in production costs show that Russian industry relies on just retaining the current growth rate, but in no way on slowing down and all the more on their absolute reduction.

Consequently, financial indicators can deteriorate. And sure enough, the latest (October) balance of expected changes of financial and economic situation in industry moved to ‘minus’ side, although in July (true, prior to the second devaluation) stayed in ‘plus’.

Assessment of industrial capacities

In 2015, data on capacity utilization has not undergone any fundamental changes compared to 2014. The latest indicator metering (October) demonstrated that industry uses available capacities up to 667% of maximum potential.

Therewith, Russian enterprises consider 81–82% as a normal maximum potential of capacity utilization. The latter indicator envisages observance of the following terms (restrictions): a) all operating procedures regarding equipment maintenance are observed; b) competitive goods are produced (currently in demand on the market); c) no fixed investment is required.

Thus, enterprises have in store industrial capacities, which can be used in case of demand growth and in import substitution. To note, that “import substitution scenario” of capacities utilization relates solely to those production operations, which already exist in the country and are unable to resolve main, according to enterprises, issue of import substitution: “common lack of domestic analogues of any quality”. The majority of enterprises point to this issue – 62% in January and in August 2015. Capital investments in new facilities are required in order to overcome this shortage.

Personnel problems of industry

Employment in industry continues falling. Over two months of Q4 2015, the pace of this process increased by 6 points and reversed positive trend, which started to take shape in August-September when the pace of dismissals shrank by 10 points. From the point of view of employment, the only positive months of ‘crisis’ 2015 were March and April when the scale of dismissals in industry gave in to recruitment scale. This situation emerged for the first time since May 2012. In the wake of the crisis and dismissals, Russian industry managed to resolve partially its personnel problems, which relate mainly to qualified workers and bring normal provision of personnel to 78%.

Results of the annual (2012–2015) monitoring of reasons for workers’ dismissal represent improved positions of industrial enterprises on the labour market. Two recent probes of these reasons were taken in July 2014 and October 2015.

As a consequence of apparent positive (for the industry) trend on the labour market, the share of enterprises reporting no dismissals has hit its four-year high of 27%. At the same time, in 2014, there were just 15% of such enterprises. The main reason for resignation was the pension age and it fell to its minimum of 40% in industry. The latter is explained not only by economic reasons (unwillingness to be a pensioner in the wake of the crisis sweeping the Russian pension system), but by natural causes (reduction of the number of working pensioners).

The share of those who quit jobs due to low pay speaks about the attractiveness of remuneration in industry. In 2015, this factor of resignations has hit its low for 4 years of monitoring and the share of those who estimated their pay size as “normal” has risen to its historic high of 70% in October 2015. During 2008–2009 crisis, it had been as low as 37%. However, monitoring of these estimates commences just from April 2007. Nevertheless, eight years period is an ample period for revealing regularities and specifics of formation of such type of estimates in Russian industry.

Workers became less choosy with regard to their work conditions in Russian industry. In 2015, dissatisfaction with these conditions are cited by merely 9% of enterprises. Although in 2012–2013, 16% of respondents indicated this reason.

Data on administrative dismissals of violators of labour (shop floor) discipline speaks about growing attractiveness of employment in Russian industry in the wake of the crisis. In 2015, this cause for dismissal is cited by merely 17% of enterprises (26% in 2013). Thus, workers give fewer causes for an administrative dismissal. ●

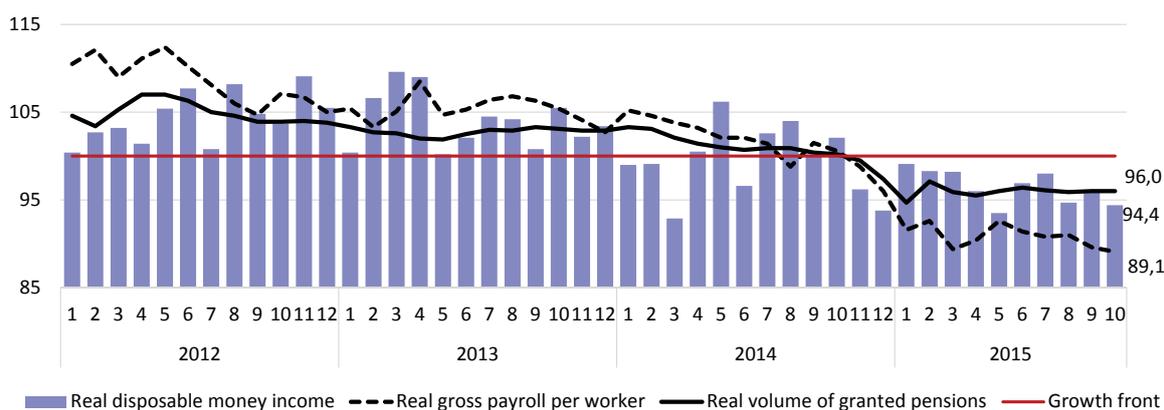
5. POPULATION'S INCOME AND CONSUMER CREDITING IS IN THE RED

A.Burdyak, E.Grishina

Real disposable income of population, real wages and salaries and pensions have been falling during the year. The territory of real income reduction (73 regions) has noticeably expanded in comparison with 2009 and 2014 (48 and 26 regions, respectively). Nearly half of population highlights deterioration of economic situation in the country. One third of surveyed in the framework of the socio-economic monitoring expect the situation to retain for at least one or two years. Consumer crediting is unlikely to sustain demand at the same level: in 2015, retail loan origination fell sharply.

In October 2015, money income of population averaged per capita Rb 31,014, monthly average nominal gross payroll per worker came to Rb 33,240 and pension averaged Rb 12,098¹. Real disposable money income of population (income less mandatory payments adjusted to the consumer price index) fell in January–October 2015 in comparison with the same period 2014 by 3.5% and real wages – by 9.3%. On the whole, reduction of these indices as well as pensions is being observed since November 2014 (Fig. 1). In November 2014 compared to November 2013, income fell by 3.8% and wages – by 1.2%. In October 2015 compared to October 2014, income and pensions fell by 5.6% and 10.9%, respectively. Granted pension volume also shrank by 4% and this fact represents *main difference of the current situation from 2009 crisis*. Then, the government managed to avoid reduction of population's income by sharp increase of pensions.

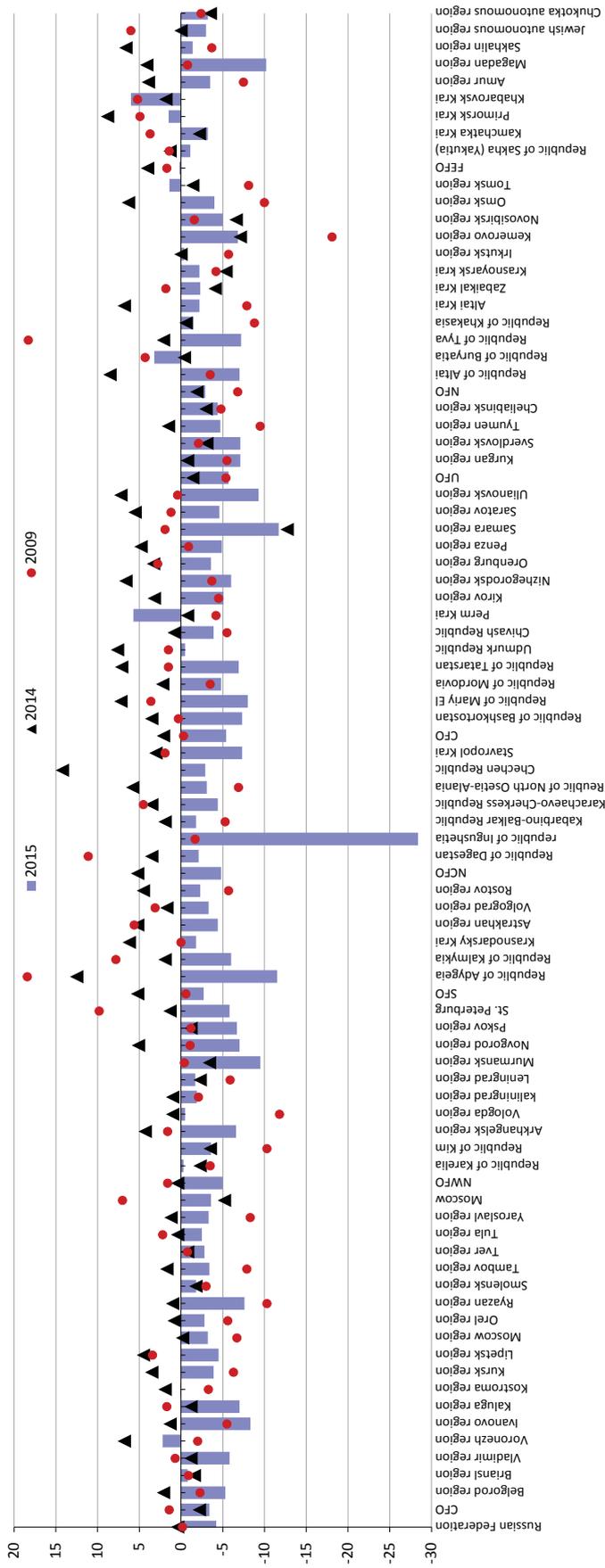
Geographically, these trends are being observed nearly everywhere both regarding population's income and consumption estimated by the volume of



Source: Rosstat, Socio-economic situation in Ruussia, January–October 2015.

Fig. 1. Dynamic of real disposable money income of the population, wages and pensions in 2012–2015, % to the corresponding period of the previous year

1 Rosstat. Socio-economic situation in Russia, January–October 2015.



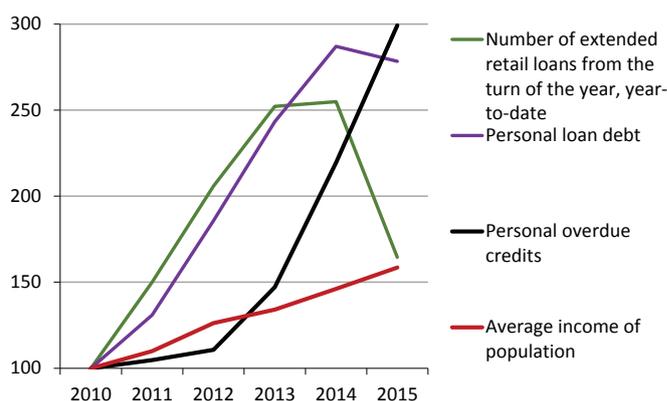
Source: Rosstat. Data for monitoring socio-economic situation of the RF subjects, January–October 2015.
 Fig. 2. Dynamic of real money income of population in January–September 2015, 2014 and 2009, % to the corresponding period of the previous year

retail trade¹. In January–September 2015, income decreased compared to the same period of the previous year in 73 regions. For comparison: in January–September 2009, real money income of population shrank in 48 regions, and in January–September 2014 – merely in 26 regions (Fig. 2). In January–September 2015, the most significant reduction of real money income of population is being observed in regions of Volga and North-Western federal districts. Compared to 2009, income reduction in January–September 2015 to a greater extent has revealed itself in regions of North-Western, Volga and Central federal districts with predominance of manufacturing industry as well as in Moscow and St. Petersburg. Meanwhile, for example, in regions of North federal district decrease of income of population in January–September 2015 turned out to be less important than in 2009.

Monitoring of socio-economic general state demonstrates that nearly half of population highlights deterioration of economic situation in the country. Herewith, one third of the surveyed expect that this deterioration will last for a year or two or even longer². By staying in sync with the prices, people began saving. Let us try to answer the question if consumer crediting will manage to sustain consumer demand or on the contrary it will contract it? How acute will be the issue of payments for retail credits for goods and services, which are being consumed but were bought on credit from income to come?

In 2015, retail loan origination fell sharply due to increased credit interest rates, tightening of extension procedures, volatility of currency rates, housing market slump as well as shortage of funds experienced by banks, which extend retail loans. Borrowers pay their debts and do not take new loans. That is why, on the one hand, retail debt before banks is contracting on the whole but, on the other hand, the share of outstanding debt is increasing. If we relate growth of nominal per capita average money income to the growth rate of lending indicator for five-year period then we will discover that income went up 1.6 times against January–September 2010. At the same time, the volume of extended loans increased by 2.5-fold in 2013–2014, during nine months of the current year has contracted 1.5-fold against last year and currently exceeds 2010 base indicator by 1.6-fold as well as income (Fig. 3). Movement of consumer expectations as well as the state of the banking sector give grounds to suppose the ratio to deteriorate.

The loan debt volume of population during recent four years as of 1 October has gone up by 2.8-fold, and shrank by 3 p.p. this year against last year. Subsequently, during five years, the volume of outstand-

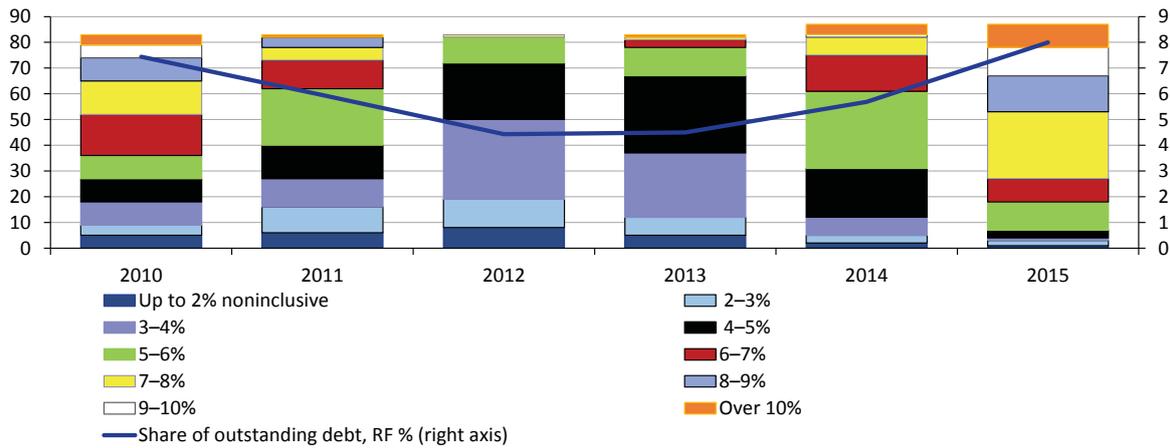


Sources: Rosstat data, authors' calculations.

Fig. 3. Volume of retail loans origination in January–September, volume of debt and outstanding debt of individuals as of 1 October and per capita average income in September 2011–2015, % to the same indicator in 2010

1 2014–2015: economic crisis – social dimension. Moscow, “Delo” Publishing house RANEPa, 2016.

2 Ibid, pp. 91–95.



Sources: CBR data, authors' calculations.

Fig. 4. Share of personal outstanding debt as of 1 October across Russian Federation as a whole and across regions, 2010–2015

ing debt has moved up three-fold. With relative measure, the share of outstanding debt in the overall loan debt of population as of September 2015 has reached the same mark where it started its descent five years ago – 7.5%. During the period under review, Q1 2013 was the best quarter with past-due share in personal loan debt amounting to 4.1%. As of 1 October 2015, the share of past-due debt has gone up to 8%. Such surge could be linked not only with dynamic of income of population but with individual insolvency law entering into force, which prompted non-performing loans to appear as past-due ones on banks' statistical reporting.

However, despite similar average indices across the Russian Federation as of 1 October 2010 and 2015, the regional scene became more diverse (Fig. 4). In 20 regions over 9% of the personal loan debt is pastdue including 9 regions with over 10% loans pastdue. Significant share of loans are mortgages (39% of the debt volume) and this type of loans due to their long-term character will play a bigger role against reduction of consumer loans origination. Where that share of mortgages in the total debt is higher, the situation with outstanding debt is better, for example, in Urals federal district. And, on the contrary, North-Caucasus federal district with 11% past-due payments is high;ighted by the lowest share of mortgages. Nighthter of the regions are distinguished by real money income of population. ●

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