MONITORING OF RUSSIA'S ECONOMIC OUTLOOK:

TRENDS AND CHALLENGES OF SOCIO-ECONOMIC DEVELOPMENT

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TRENDS AND CHALLENGES OF SOCIO-ECONOMIC DEVELOPMENT

The zigzag path of trade negotiations between the USA and China has clearly become a fundamental aspect of the global economy. Judging by the response of both financial and raw material markets, this aspect has already become a dominant one by having evolved into the principal determinant of market expectations. The duration of this factor's dominance, which ultimately depends on the results of those negotiations, will be limited only by the next US presidential election.

Apparently, such a situation tends to increase the risks faced by countries that produce and export raw materials, and especially by those of them who are trying to reduce their reliance on the US market. The main characteristic feature of this situation is the newly emerged dependence of the raw material exporters on US policies both in the field of raw materials supply and the field of raw materials demand. As everybody is aware, US oil companies are capable of massively and rapidly increasing oil production, thus determining the level of supply, while US politicians are clearly capable of extinguishing and rekindling international economic conflicts, thus determining the level of demand.

In order to properly respond to these (and other) risks, a country at risk should not resort to putting forth some half-baked initiatives in order to reduce its import dependency, because such initiatives are, first of all, fraught with danger for the competitiveness of its domestically produced goods. It is logical that a draft law imposing an almost total ban on all new types of industrial imports, introduced into the RF State Duma by a number of most active business lobbyists, has encountered very strong consumer resistance. It is equally logical that the RF Government is now eager to formulate its import substitution policies in a more orderly and rational fashion.

The RANEPA experts who have analyzed industrial production dynamics in Russia in Q2 and H1 2019 note, among other things, that by the middle of this year Russia's processing industries had registered zero growth. According to their estimates, the trend component reveals near-zero growth rates both in the manufacturing and extracting industries. Retail trade, provision of paid services to the population and building construction have slumped into stagnation. Our analysts warn that Russia's prospects for exports growth have become alarmingly grim: having faced a continual reduction in their economic growth rates, both the EU and China are busily erecting tariff barriers to trade in Russian goods, while the competitive ability of such goods is generally rather low. The aforesaid experts believe that due to Russia's weak domestic demand and the ongoing decline in private investment there is no reason to suggest that the period of stagnation in Russian industry is approaching its end.

Having assessed the progress of the implementation of the Safe and High-Quality Roads national project, our experts have come to the conclusion that this project is behind schedule, including with regard to multiple important contracts that should be concluded with the regions. Moreover, a number of regions have failed to properly assess the condition of their motor roads.

Distorted statistics have had a negative impact on the quality of decision-making, including with regard to the distribution of financial resources. As far as the reliability of statistics is concerned, our experts recommend that the activities of the regional statistics services should be randomly assessed on a regular basis.

Having paid attention to the fact that the shrinking of Russia's workforce has notably precipitated, by almost 0.8m persons in Q1 2019 relative to the same period of past year, while during the entire year 2018 it had declined by a mere 0.1m, the aforesaid analysts point out that the basic reason for this fact is the aging of all the main age groups of the working-age population. In principle, the decline in Russia's workforce has been going on since 2016, but recently this process has notably accelerated. Moreover, by now the expansion of the economic activity of the main working-age groups of the population has already reached its peak. Although a further rise in the economic activity of the population is possible, it could be achieved, first of all, if the senior age groups of the population notably increase their presence in the labor market.

A thorough research carried out at the RANEPA in 2018 has permitted our experts to assess the availability of the so-called development resources to various groups of the population, as well as their need for such resources, which include employment, the wage rate, social status, etc. More than two-thirds of respondents characterized their employment as stable, although one out of every five respondents admitted being afraid of losing his or her job. One third of the respondents believed that they would be able to find a job not worse than their current one. More than half of the respondents had received a mediocre or low-quality education, a factor that significantly hampered their social development. Our experts believe that the research has shed light on yet another highly important characteristic, the level of interpersonal trust. Sadly, the behavior of that index was clearly negative: more respondents than before affirmed that the number of trustworthy people had decreased. Nevertheless, our experts have come to the conclusion that the social moods of the population are characterized by optimism rather than pessimism, and the percentage of the population expecting to experience upward social mobility is notably larger than the percentage of those expecting to experience downward social mobility.

1. INDUSTRIAL PRODUCTION DYNAMICS IN H1 2019[1]

A.Kaukin, E.Miller

In Q2 2019, the extractive industry and production of electric energy, gas and water continued to display a near-zero growth pattern. The manufacturing sectors, after demonstrating some growth at year beginning, likewise demonstrated zero growth by the period-end results for Q2. The aggregate output index for industry points, overall, to a slow growth.

According to statistics recently issued by Rosstat (the Russian Federal State Statistics Service), in June 2019 the Industrial Production Index grew by 3.3% relative to the same period of the past year. This growth was primarily caused by an improvement in the dynamics of manufacturing production (+3.4%), while growth in mineral resources extraction amounted to +2.3% relative to the same period of the past year and therefore was more modest than in May.

In order to provide a detailed analysis of the by-sector dynamics of industrial production indices across Russian industry, the Gaidar Institute's experts decomposed the corresponding time series and obtained the trend component of the industrial production indices for each industry[2]. The results of processing the time series for the Industrial Production Index are shown in *Fig.1*. They indicate that during Q2 2019 its growth was slow. The dynamics of the trend components of the extractive and manufacturing industries, as well as those of electric energy, gas and water production, displayed near-zero growth rates (*Table 1*).

The extractive sector continues to be influenced by the existing OPEC Plus Agreement to cut oil production at around current levels, which was prolonged until April 2020 (and cut oil production in Russia by 228,000 barrels per diem). Russia's extractive sector is also negatively impacted by the unfavorable price situation in the global coal market, which has forced Russian enterprises to downwardly adjust their production plans: to cut extraction and to redirect supplies to the Asian market[3].

The only exception of the general downward trend in extractive industries production was the natural gas industry: in the course of preparing themselves to the next heating season, European countries had begun to actively stockpile natural gas in their underground storage reservoirs, purchasing it at prices lower than 'winter' futures

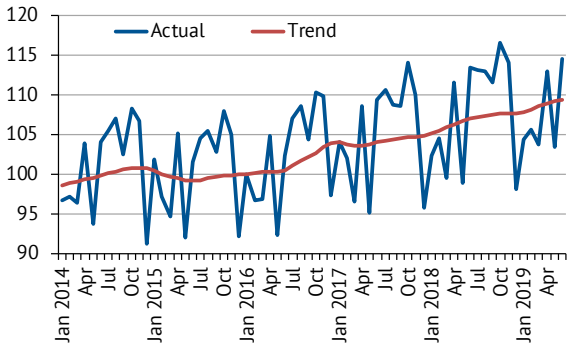

Fig. 1. The movement pattern of the industrial production index in 2014–2019 (actual data and trend components), as % relative to January 2016

Source: Rosstat; own calculations.

1 The authors should like to thank M. Turuntseva and T. Gorshkova for their assistance and expertise in the preparation of this statistical analysis.

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

3 Coal extraction in Kuzbass has dropped by 7% due to the fall in prices in Europe [in Russian] // RBC, 22 July 2019. [https://www.rbc.ru/business/22/07/2019/5d-35dc409a7947aa069fe85f?from=newsfeed].

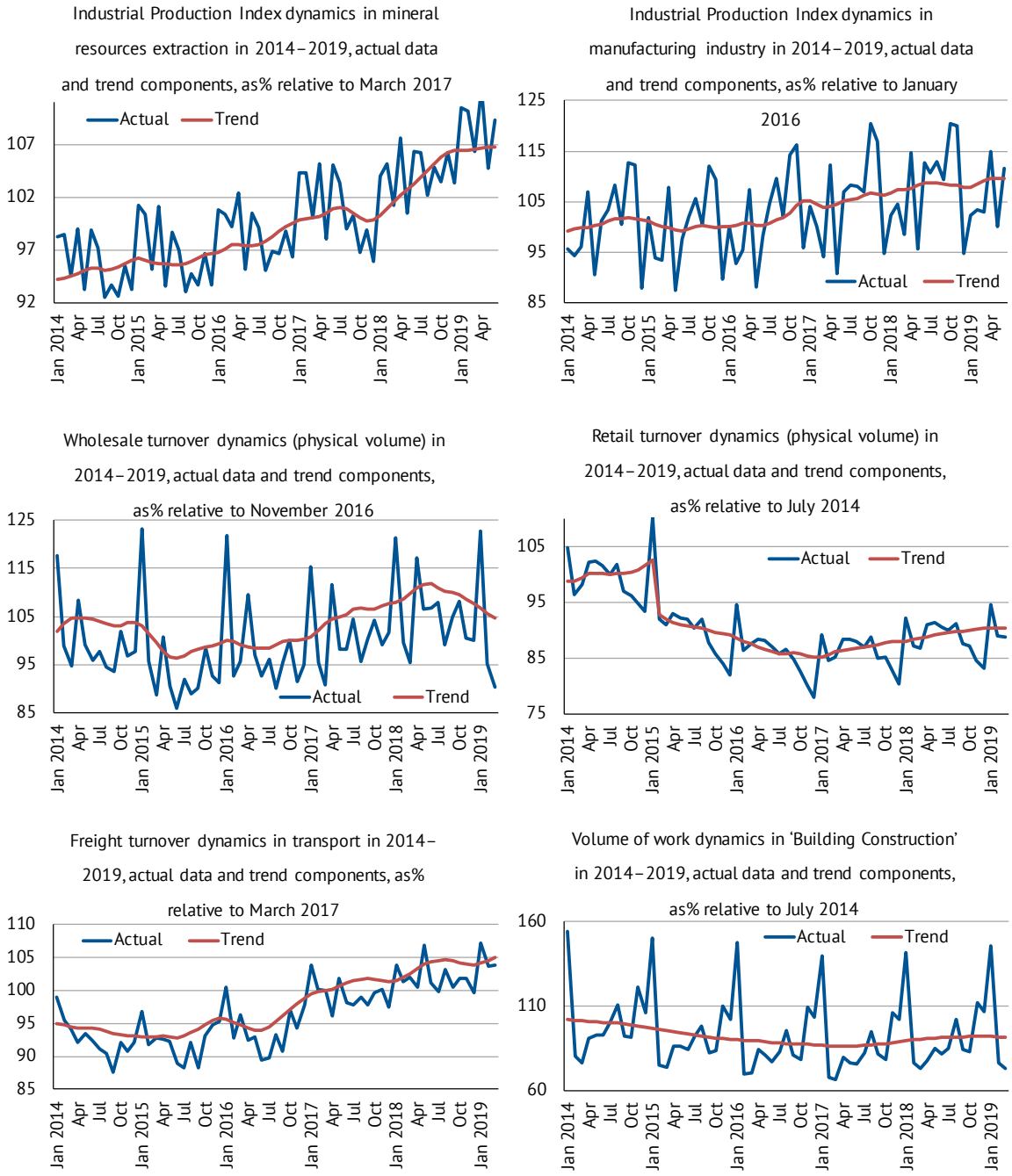

Fig. 2. The by-industry movement patterns of the industrial production index in 2014–2019, actual data and trend components.

Source: Rosstat; own calculations.

prices[1]. By the beginning of June 2019, the volume of natural gas stored in these reservoirs was almost twice as high as in June 2018. Nevertheless, in Q2 2019 the cumulative output of the extractive industry displayed near-zero growth rates.

[1] As of the beginning of July 2019, 'winter' natural gas futures quotes on the European hubs were twice as high as the spot price and the natural gas price for next month's deliveries. See Gazprom has taken advantage of the sharp fall in natural gas prices in Europe [in Russian] // Vedomosti, 2 July 2019. [https://www.vedomosti.ru/business/articles/2019/07/02/805558-gazprom-vospolzovalsya-vospolzovalsya

1. Industrial Production Dynamics in H1 2019

In Q2 2019, a continuation of growth in manufacturing industries was observed in the foodstuffs production, timber and wood products processing, chemical production, metallurgical production, and transportation equipment manufacturing. The causes of growth were the same as before – government support and a favorable market situation. The other industries, which had registered a positive dynamics in Q1 2019, returned to near-zero growth rates or a gradual slowdown in production[1].

The other most important sectors of the economy have not demonstrated considerable growth: there is a continuation of decline in retail trade and the ongoing stagnation in the provision of paid services to the population and building construction. The largest growth has been registered in cargo turnover, due mainly to the contribution made by road transport. As far as its contribution is concerned, the following factors are worth mentioning.

- Increase in the average length of haul due to the commissioning of new high-speed motor roads;
- Accelerated renewal of vehicle stock. By comparison with the same period of the past year, the volumes of commercial auto leasing and purchase loans made by road haulage firms in order to buy new vehicles went up (which means that the firms that had postponed the renewal of their vehicle stock began to actively renovate it). An increase in the use of new vehicles inevitably results in a decrease in the number of breakages and long stays of empty vehicles, and therefore in an increase in the number of long-distance hauls (exceeding 300 km)[2];
- Increase in the number of small deliveries due to the traditional tonnage reduction introduced in springtime in most of the regions of the Central Federal District, the Northwestern Federal District, and the Maritime Federal District[3].

Under current conditions, the drop in exports seems especially worrisome for a number of reasons[4]. These reasons are as follows: firstly, the OPEC Plus Agreement and a very high proportion (more than 60%) of the fuel and energy complex's products in Russia's exports; secondly, the protectionist tariff policies exercised by the top consumers of Russian exports, such as metallic products etc., and a decline in the economic growth rates in a number of regions (the EU, China); and thirdly, the poor quality of goods produced by Russian enterprises, which make them incapable of succeeding in price competition when the ruble strengthens.

At the present moment, the weakness of domestic demand, the ongoing drop in private investment, and the huge capital outflow from Russia do not suggest that the period of stagnation of Russian industry will soon be over. Proper monitoring of by-sector output dynamics over the course of future periods, including the emergence of more accurate statistics, will make it possible to more confidently interpret the results of investigating the trends discernable in the by-sector output of Russian industry.

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1 Kaukin, A. S., Miller, E. M. Industrial Production Dynamics in Q1 2019: Manufacturing Sector on the Rise // Russian Economic Developments. 2019. No 5. P. 14–19.

2 Traft: Cargo turnover increases, among other things, due to the increase in the length of hauls [in Russian] // The Unified Transport Portal, 28 May 2019. [https://trans.ru/news/traft-gruzooborot-rastet-v-tom-chisle-i-za-schet-uvelicheniya-dalnosti-perevozok].

3 The springtime tonnage limitations of 2019: where, when, and to how many tons [in Russian] / The Unified Transport Portal, 7 February 2019. [https://trans.ru/news/vesennie-ogranicheniya-2019-gde-kogda-i-na-skolko-tonn].

4 A. Bashkatova, The exports curse of Russia is beginning to come true [in Russian] // The Independent Newspaper, 13 June 2019. [http://www.ng.ru/economics/2019–06–13/4_7597_export.html].

Table 1

By-industry movement of the industrial production index,%

	Share in industrial production index	June 2019 on June 2018	June 2019 on May 2019	Changes over recent months
Industrial production index		102.21	100.14	slow growth
Extraction of mineral resources	34.54	103.39	100.03	stagnation
Manufacturing industries,	54.91	100.86	99.95	stagnation
including:				
production of foodstuffs, including beverages, and tobacco products	16.34	104.24	100.23	slow growth
textiles & textile products manufacturing	1.14	104.86	99.94	stagnation
leather production and leather products & footwear manufacturing	0.27	98.81	99.55	stagnation
timber & wood product processing	2.02	106.72	100.74	growth
cellulose & paper production	3.35	77.19	97.57	decline
production of coke & petroleum products	17.25	100.61	99.98	stagnation
chemical production	7.56	109.68	100.29	slow growth
manufacturing of rubber & plastic products	2.14	98.42	98.82	decline
manufacturing of other non-metallic mineral products	4.02	105.92	99.74	stagnation
metallurgical production & finished products	17.42	113.54	101.36	growth
machinery & equipment manufacturing	6.97	94.43	98.88	decline
electric, electronic & optical equipment manufacturing	6.27	97.21	99.35	decline
transportation equipment manufacturing	6.75	79.23	102.18	growth
other industries	2.42	98.87	99.51	decline
Electric energy, gas and water	13.51	100.08	100.00	stagnation
Wholesale trade		94.24	100.15	stagnation
Retail trade		101.44	100.08	stagnation
Cargo turnover		101.62	100.12	slow growth
Building construction		100.52	100.01	stagnation
Provision of paid services		100.20	100.01	stagnation

Source: Rosstat; own calculations.

2. THE CAUSES OF WORKFORCE DECLINE

V.Liashok

In 2019, the rate of decline in the workforce soared: in Q1, it shrank by nearly 0.8m on the corresponding quarter of the previous year, while over the entire year 2018, that index had declined by only 0.1m. As a result, the number of individuals involved in economic activities (without taking into account the Republic of Crimea and the city of Sevastopol) returned to its 2005 level.

In Q1 2019, Russia's workforce dropped by nearly 0.8m on the corresponding quarter of the previous year, to 75.0m. This index is calculated by Rosstat on the basis of the ILO methodology as the total number of employed persons (those who work for pay or profit) and unemployed persons (those without work for pay or profit, who are seeking and available to start working for pay or profit). By that definition, workforce also includes persons involved in forms of work other than employment, as well as individual entrepreneurs; and unemployed persons are all those who do not have a job, and not only those registered with public employment services. As a result, the index reflects the degree of the population's involvement in labor relations. In this connection, workforce (or the number of economically active persons), in contrast to the number of employed persons and that of unemployed persons, becomes an acyclic economic indicator. Its plunge translates into a limited economic growth potential for a country.

Workforce decline per se is not an unexpected phenomenon, because it has been going on since 2016, and this dynamics is in sync with Russia's general demographic trends (*Fig. 1*). Since the Soviet period, Russian statistics traditionally divided the total population into the total working-age population (aged 15 to 59 years for men and 15 to 54 years for women), those younger, and those older than that age cohort. The working-age cohort has been shrinking in this country since 2006, and over 12 years it fell by 9%. However, at present this age span only weakly reflects the age profile of the Russian population involved in the labor force.

On the one hand, in face of the widespread higher and secondary professional education, only 7.7% of all young people aged 15 to 19 years were participating, in 2018, in the labor market — that is, were part of the workforce. On the other, 55% of women aged 55 to 59 years continue to work. Under the modern conditions, a more accurate definition of the age span encompassing the main working-age cohort (more than 50% of men and women involved in labor relations) should be that of 20 to 59 years. Due to the retirement age raise, the upper threshold will be pushed a little further.

If we should look at the population dynamics within this age range, it will be close to that of the workforce: the index was actively on the rise during the previous decade, and has been slowly declining over the past 9 years. While the working-age population has been shrinking since 2006, the number of persons aged 20 to 59 years began to fall only since 2011, having shrunk by 5.2%.

The workforce growth in the noughties, and the unchanged value of its index over the period 2011–2018, could become possible not only thanks

to the relatively favorable demographic situation during these periods, but also to the increasing involvement of the population in the labor market. Among the characteristic features of the 1990s was not only the high (by Russian standards) unemployment rate, but also a withdrawal from the workforce into economic inactivity; after 2000, the trend was reversed. The aggregate economic activity level (the number of economically active persons as a percentage of all individuals aged 15–72 years) gained 3.8 pp., but the movement patterns of that indicator varied significantly between age groups (*Fig. 2*): for those aged 15 to 24 years, it lost 10–12 p.p., while increasing for all the other age groups. As a result, by 2018 the rate of involvement in labor relations for persons aged 25 to 54 years in Russia was higher than in the OECD member states, with the exception of Sweden and Slovenia. At the same time, in spite of the significant increase of economic activity in the 55–59 age group, by 2018 the economic activity level in the senior age group has been still below the corresponding average index in the developed countries.

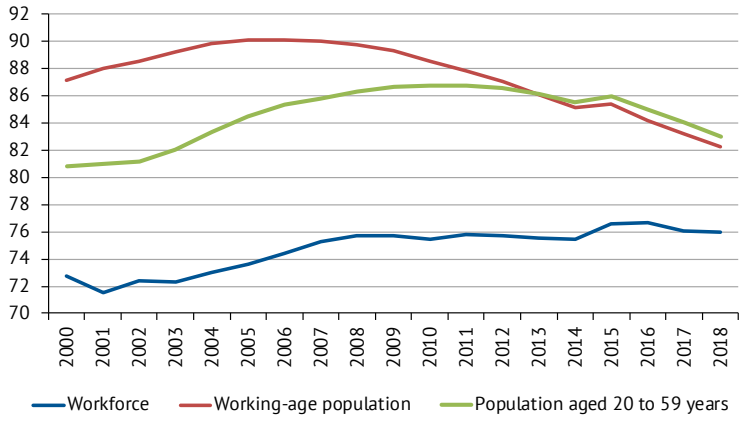

Fig. 1. The workforce, the working-age population, and the population aged 20 to 59 years, million

Source: Rosstat; own calculations.

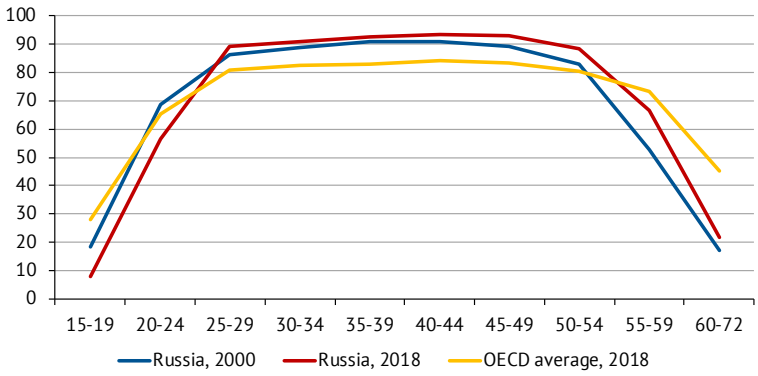

Fig. 2. The age profiles of the workforce in Russia in 2000 and 2018, and the OECD average for 2018, %

Source: Rosstat; OECD-stat; own calculations.

On the whole over the period 2000–2018, the workforce in Russia increased by 3.7m. Factor decomposition of the movement of that index points to the negative impact of the population aging on the workforce in Russia: if the economic activity level had remained unchanged, it would have shrunk by 0.5m. However, the demographic changes were offset by the additional involvement of the population in labor relations, and so the economically active population increased by 4.2m.

As for the situation in early 2019, the process of population aging continued, and the number of potential workers was on the decline – the number of persons aged 20 to 59 years had shrunk, over the course of one year, by 1m. Meanwhile, although Rosstat releases its workforce estimates on a monthly basis, the demographic changes are recorded on an annual basis[1]. Thus, the

1 The level of participation in the workforce is determined on the basis of monthly population surveys. The estimated share is spread to the entire population, determined as the total population as of 1 January of the previous year. Over 12 months, the general population remains constant. Thus, the monthly workforce fluctuations (except January on December) reflect only the input of economic activity fluctuations.

sharp workforce shrinkage in Q1 can be explained in part by the demographic factor and the specificity of procedure applied in calculating that index.

On the other hand, the economic activity level demonstrated a decline: from 62.6% in Q1 2018 to 62.0% in Q1 2019. This can be partly explained by structural effects – population aging translated into a plunge of the average economic activity level. Nevertheless, the activity increase among the working-age groups that had been observed for at least 10 years previously, in 2019 effectively halted[1].

It can be assumed that at present, the economic activity ceiling has already been hit for the main working-age groups. Any further growth can be possible only through more active involvement of the senior population in the labor market.

1 In 2019, Rosstat applied the 'old' working age threshold: up to 59 years for men and up to 54 years for women.

3. WHAT DO RUSSIANS NEED AND WHAT THEY HAVE

E.Avraamova

Socioeconomic development depends on different social groups having access to the so called «development resources». Research conducted by our experts shows that Russians' most scarce resources are education and high salary.

Research of availability of development resources for different socioeconomic groups is based on representative pool of 3000 people of age groups 25–65 (taken out in 2018). Main resources of development are considered to be: growth of occupational level (vertical labor mobility); increase in quality of education, increase in social status, development of social capital.

Only 11% of respondents have high-level **education** and 34% of respondents received education which can be considered 'above average.' Therefore, when talking about opportunities gained by higher education, more than 40% of population are competitive on the labor market and can be actors of social development. However, more than a half of respondents have average-level education or even lower. Therefore, it is much harder for them to socially develop.

Demand is one of education's most important characteristics – among other factors, ability to apply one's professional skills on the labor market. 56.8% of respondents work by occupation or in areas close to the occupation. Inability for various reasons to apply according to gained education in the workplace decreases motivation to increase the quality of education.

Education of average or lower quality puts people in situation where they have to choose occupations that are not very demanding competence-wise.

Stable employment provides an opportunity to sustain and grow other resources of development. More than two thirds of workers describe their employment as stable. At the same time, every fifth person is afraid of loosing job.

Strongest employment stability show not managers, but highly trained specialists. Semiskilled personnel are below aforementioned groups while blue-collar workers and laborers, even those who are qualified, feel stronger danger of loosing job.

Age differences also matter when it comes to evaluating how stable their employment is. Danger of losing job is growing as a worker approaches 35 and then gets stronger, until it reaches the highest point in the age interval of 55–65 years, i.e. preretirement age.

Only one third of employed are looking forward to finding a job that is better than their current one. At the same time, 45% believe that it will be difficult, while 20.8% believe, that alternative employment is impossible.

The younger the respondents, the easier is the task of finding a job. So, in age gap of 25–35 forty percent believe that it will be easy for them to find a job which is not worse than the current one, while in the next age group 35–40 that index drops 6% and in the next one it decreases by 7%, reaching a minimum of 26% in the oldest age group.

Potential growth of **social professional status** depends on compatibility of mentioned status and education and qualification. Third of employed notes that

the level of their education and professional qualification is higher or even significantly higher than their job position. Workers with the highest compatibility are the ones who have the highest quality of education.

Overall, majority of respondents mention decrease of social status when compared to ones who talk about increase. Social self-esteem decreased in lower-status groups, stayed the same in the middle class and increased in upper class. Never the less, public mood is rather optimistic, as most of people are sure they will raise their social status.

Social capital was rated through categories of cohesion and trust. First category is mostly about help, which a person can get from their social surroundings. A person can get help through different channels, foremost from family and friends. Around 30% of respondents don't get any help and just above 20% can only expect help from one channel. In the same time, around a third have well developed social connections. Group size, which has low level of social cohesion, is growing because of older generations.

Trust is as important aspect of social capital as cohesion. Almost half of respondents, when asked how many people they trust, said that there were barely any or none. Dynamic of inter-individual trust has negative nature, as now, there are less people who can be trusted, as 30% of respondents say. Only 6% say the opposite.

Younger generation has high hopes regarding the number of people who can be trusted will grow. After the age of 55, views change and there is no hope. People of that age are reluctant to narrow the circle of trust. The number of respondents who are narrowing the circle of trust in that age are double compared to next youngest age group (45-54 years of age). Respondents say, that they have stopped trusting their colleagues (down 25%), friends (down 18.2%) and relatives (down 12.6%).

Overall, it can be said, that social capital in Russia is a deficit resource of development, as social cohesion is not high enough while interindividual and intergroup trust is reluctant to diminish.

Maximum satisfaction comes from quality and level of education, then – level of social support, further – socio-professional status. And, in the end, the last on the list of satisfaction is the level of material security which is dependent on salary. Blue-collar workers and laborers, qualified as well as less qualified are the ones who are more demanding when it comes to wages. When it comes to age, workers of 45–54 have the highest dissatisfaction with their pay. Blue-collar worker and laborers, especially the ones who are not qualified have the highest demand to raise socio-professional status. The highest demand for career growth has the youngest age groups – 25–34 years and 35–44 years.

Overall, highest demand for development resources have people in middle age groups without higher education and workers who are not working in a job for which they got a degree.

Around 40% of respondents consider economic situation in the country to be the main reason for growth of their prosperity and availability of other resources. When compared to this factor, all other, including effort, are on the second plan. Respondents often note that among restrictions of social development are mainly unavailability of education and low salary.

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