

UDC 33

Economic Situation in Post-Crisis Russia

¹Galina Bodrova²Tatiana N. Ogneva

¹Sochi State University, Russia
Sovetskaya st. 26a, Sochi 354000
Student

E-mail: galochka2211@yandex.ru

²Sochi State University, Russia
Sovetskaya st. 26a, Sochi 354000
PhD (Linguistics), Associate Professor
E-mail: tatyanaogneva@mail.ru

ABSTRACT. The global economy was slowing as well as the eurozone countries. Though Russia's economy held steady with the reported current account surplus, the large non-oil fiscal deficit requires concerted fiscal adjustment to reduce vulnerability in the face of new shocks. According to Mr. Putin emphasis has to be shifted away from the energy sector and toward new investments and infrastructure. A framework for creating and developing new sectors of the economy is to be provided for modernizing production units, mastering advanced production management methods and developing human assets.

Keywords: recession; fiscal adjustment; to reduce vulnerability; the balance of trade; economic development model; modernizing production units; developing human assets; upgrading production facilities; cooperation with foreign companies; access to global markets; strong government support.

INTRODUCTION

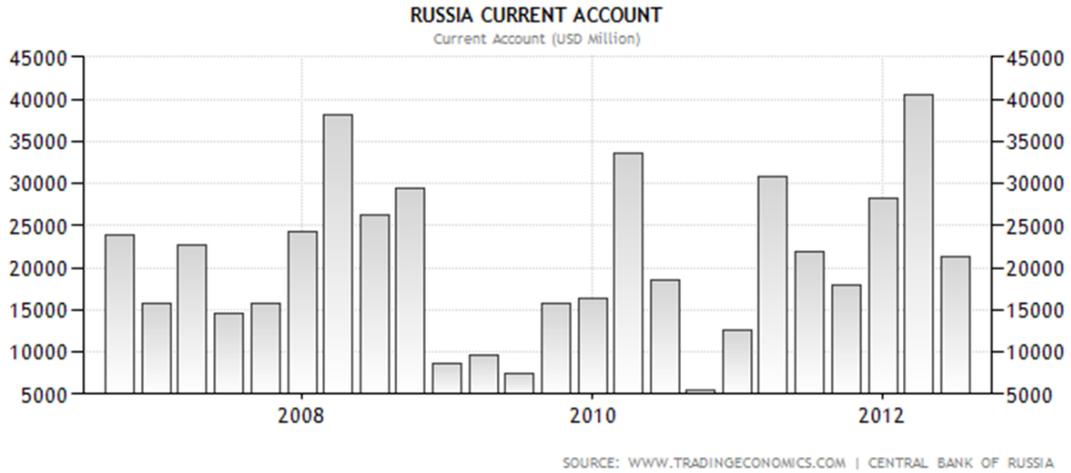
By the end of 2012 Russia's economy held steady and shows signs of sustainable growth. The Russian government should not miss opportunities provided by additional oil and gas revenues to improve long-term fiscal sustainability, to further reduce inflation, thus providing a stable base for a sustained and strong economic growth in the future. At the same time Russia's economy requires restructuring and reinvigorating, government must make major changes to economic development model. It is only possible by means of creating new production, modernizing currently operating production units and developing human assets. For these measures large-scale investments are required. So let's start with recent economic developments, then we'll go to investment climate in Russia and investment statistics.

Recent economic developments

Early this year, the global economy was slowing and the eurozone entered a recession. But Russia's economy held steady. By now, as 2012 is entering its final quarter, growth is slowing, even though oil prices have stayed high. But let's start with the strong points.

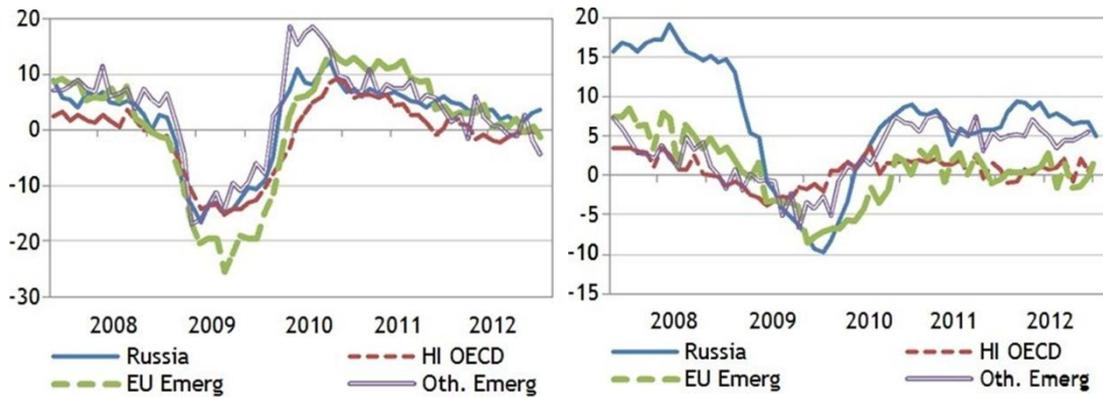
Russia reported a current account surplus equivalent to 21.2 Billion USD in the second quarter of 2012. Current Account is the sum of the balance of trade (exports minus imports of goods and services), net factor income (such as interest and dividends) and net transfer payments (such as foreign aid).

The improvement in the current account surplus, along with a moderation in capital outflows, allowed the Central Bank of Russia to increase its foreign reserves. The CBR added about US\$21 billion to its reserves, which increased to US\$530 billion by the end of September. [1]

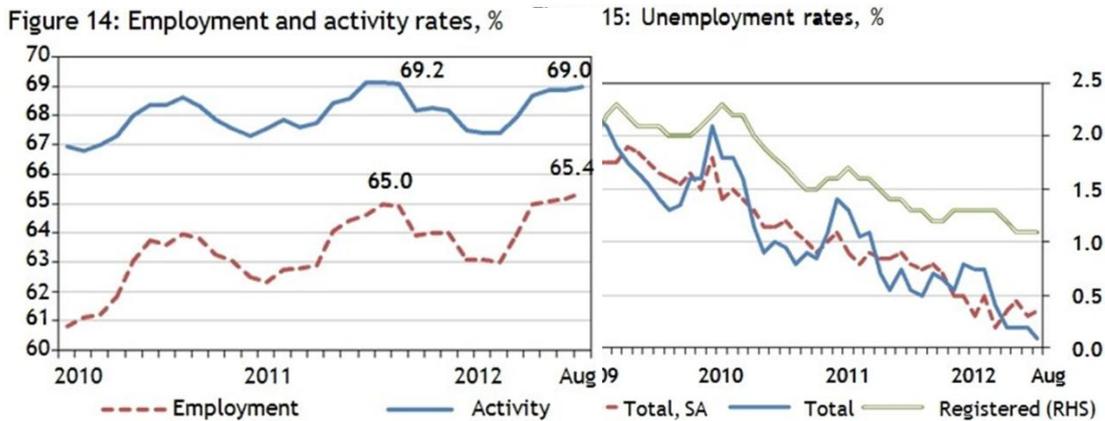


Russia's economy performed well relative to other regions this year:

- While growth of industrial production turned negative in recent months in other regions, it remained positive and even accelerated in Russia.
- Growth of retail sales in Russia exceeded the growth in other regions for the last year.
- Even with the recent slowdown, it remains growing



The labor market shows signs of overheating. The unemployment rate reached a record low, and the vacancy rate increased. The tight labor market led to rapid wage growth, also because public sector wages rose at a swift pace.

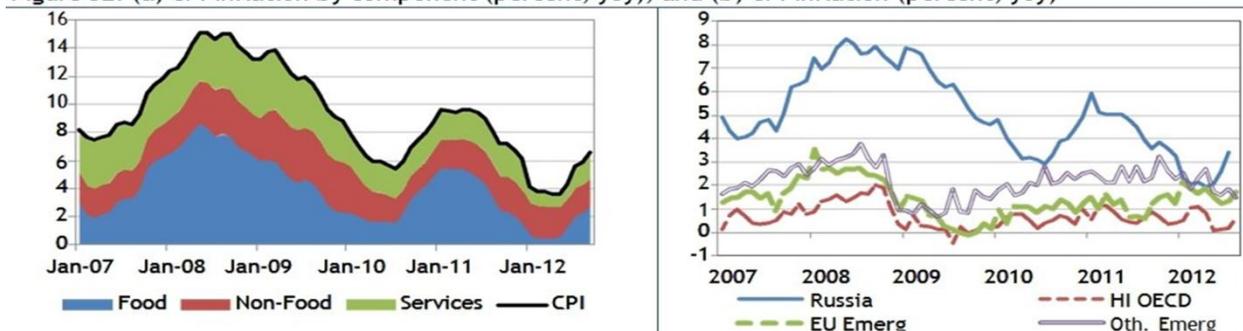


Since reaching record lows in April 2012, inflation increased mainly due to higher food and administrative prices. With inflation exceeding its end-year target, the CBR increased interest rates to anchor inflation expectations in response to concerns about large credit and wage growth.

While these achievements of the twin-surplus economy are impressive, the recent economic news is less encouraging.

- Whereas early in the year, growth was rising and inflation declining, now growth is declining and inflation rising.

Figure 32: (a) CPI inflation by component (percent, yoy); and (b) CPI inflation (percent, yoy)



- Domestic demand, the main driver of growth in Russia, is weakening.
- In addition, companies are no longer restocking and not yet stepping up investment.
- Elevated volatility in global financial markets slows global trade, industrial production and as a result economic growth. [2]

New model for economic growth

Russian President Vladimir Putin takes solutions for development in a new direction. He proposes shifting emphasis away from the energy sector and toward new investments and infrastructure.

According to Putin, Russia's GDP growth is now of "better quality" and "better balanced," but the country still needs to make major changes to its economic development model.

Further growth is only possible by means of large-scale investment in creating new production, modernizing currently operating production units and developing human assets. As such, the foremost task for Russian authorities is to provide a framework for creating and developing new sectors of the economy. [3]

Putin has also put high hopes in the Direct Investment Fund. According to him, almost 8 billion rubles (\$257.5 million) from the federal budget have been injected into investment projects, and 25 billion rubles (\$805 million) in private investor funds have been raised. Putin appears confident that the Fund will provide substantial support for newly-created sectors of the economy, particularly in the area of raising capital. All of this is expected to boost investment up to 25 percent of GDP by 2015 and create 25 million jobs by 2020. [4]

The Role of Foreign Investments in Russia

Attracting foreign capital is amongst the main strategic priorities for the development of Russian economy.

Russia views **foreign investments as a driver** for:

1. Accelerating economic and technical progress
2. Revamping and upgrading production facilities
3. Mastering advanced production management methods
4. Ensuring employment, training personnel capable of responding to the challenges of a market economy

Russia is interested in an inflow of enterprise capital over borrowed capital because in this case:

1. the country's external debt does not grow
2. cooperation with foreign companies provides Russian businesses with new technologies, management methods and direct access to global markets with competitive products real investments are the impulse the economy needs to overcome depression and ensure healthy economic growth.

What are Advantages of Investing in Russia:

- **Dynamic Economic Growth.** Russia is one of the most dynamically developing and attractive economies in the world. Thanks to the strengthening ruble, in dollar terms the 1999-2007 GDP growth was an astounding 26% per year, far outstripping international growth rates.

- **Favorable Geographic Position.** Russia links Europe with Asia and also borders the North American continent, offering the following advantages:

- Worldwide sea routes
- Major airport hubs
- Rail and road transit routes (leads the world in length of electrified railroads)
- Other transport and logistics infrastructure.

- **Vast Natural Resources.** Russia takes 1st place in the world in per capita resources. It is well placed amongst the richest countries in terms of natural gas, oil, coal, minerals, metals and energy. With its forest resources being the largest in the world, Russia also has tremendous reserves of drinking and fresh water.

- **Fast Growing and Technologically Advanced Economy.** Strong Russian scientific knowledge provides excellent opportunities for research and development partnerships with Russian research institutes and universities. Critical technological areas eligible for government co-financing on a competitive basis are Aerospace, Aviation, Shipbuilding, Automotive, Machinery, Metallurgy, Chemistry and pharmaceuticals, Nuclear physics and many more.

- **Large Consumer Market.** With a population of over 140 million people and constantly increasing income per capita, Russia provides a large and booming internal market offering attractive growth potential.

- **Strong Government Support.** Investment in the Russian economy is strongly supported by federal and regional authorities. Such federal initiatives as the Investment Fund, Foreign Investment Advisory Council and Special Economic Zones as well as public-private partnership opportunities and large investment and development programs serve to accelerate the investment inflow and to further enhance the Russian investment climate.

- **Attractive Taxation System.** With a personal income tax rate of 13% for residents, corporate tax rate of 24%, and VAT rate of 18%, Russia has one of the most generous non-offshore tax regimes in the world, aimed at promoting investment and further developing the economy.

- **Highly Skilled and Well-Educated Human Capital.** Russia has one of the most highly skilled workforces in the world. Excellent educational background, extensive R&D and engineering practice allows Russian professionals to take up leading positions in areas such as natural and applied sciences, programming, R&D, engineering, etc.

- **State Bodies and Legislation**

The Government of the Russian Federation devotes significant attention to foreign investments in Russia as a tool of socio-economic and innovative development of the country. A broad network of institutions established in the recent years aims at simplifying investment procedures and providing comprehensive assistance to foreign investors. [5]

The following table 1 includes the most recent data from indices measuring the investment and business climate in Russia:

Measure	Year	Index/Ranking
TI Corruption Index	2011	2.4 – 143 of 183 countries
Heritage Economic Freedom	2011	50.5 – 143 of 183 countries
World Bank Doing Business	2012	120 of 183 economies
Gov't Effectiveness (Worldwide Governance Indicators)	2010	-0.39 – Percentile rank: 41.6
Rule of Law (Worldwide Governance Indicators)	2010	-0.78 – Percentile rank: 26.1

Control of Corruption (Worldwide Governance Indicators)	2010	-1.07 – Percentile rank: 12.9
Fiscal Policy (IMF World Economic Outlook)	2011 (est.)	Government net annual borrowing: 1.11% of GDP
Trade Policy (Heritage Economic Freedom)	2011	68.2 (moderately free)
Regulatory Quality (Worldwide Governance Indicators)	2010	-0.39 – Percentile rank: 38.3
Business Start Up (World Bank Doing Business)	2012	111 of 183 economies
Land Rights Access (World Bank Doing Business)	2012	Construction Permits: 178 of 183 economies Registering Property: 45 of 183 economies
Natural Resource Mgmt (Natural Resource Management Index)	2011	90.3 on a 0 – 100 scale (100 is best)

Foreign Direct Investment Statistics

Table 2 shows flows of foreign investment by country for the first nine months of 2011, compared to the same period in 2010. Total foreign investment increased sharply in 2011, rising by 182% year-on-year. FDI flows into Russia also increased in 2011. This year, the largest share of foreign investment came from Switzerland. FDI from the Netherlands and Cyprus is consistently high because most FDI coming from these countries is either returning or reinvested Russian capital through subsidiaries or off-shore vehicles.

Table 2: Top Investors - By Year (in USD million)

Country	Jan-Sep 2011		Jan-Sep 2010	
	Total	FDI	Total	FDI
Switzerland	69,115	70.1	3,398	64.5
Netherlands	13,218	3,023	7,507	943
Cyprus	12,972	2,758	5,635	1,912
Germany	8,169	1,480	7,520	1,095
UK	6,336	176	4,240	430
All Others	23,976	4,228	19,189	3,751
Total	133,784	11,736	47,488	8,196

Table 3 shows total foreign investment by region over the first nine months of 2011, compared to the same period in 2010. Moscow continues to attract the largest volume of investments (63.4 % of total foreign investment), mainly due to the concentration of companies' headquarters and consumers with high purchasing power.

Table 3 – Foreign Investment – Top Regions (in USD million)

	Jan-Sep 2011			Jan-Sep 2010		
	Amount	%	Rank	Amount	%	Rank
Moscow (city)	84,878	63.4%	1	15,816	33.3%	1
Tyumen Region	9,821	7.3%	2	701	1.5%	11
Sakhalin Region	6,570	4.9%	3	3,611	7.6%	4
St. Petersburg	3,972	3.0%	4	3,723	7.8%	3
Belgorod Region	3,171	2.4%	5	24.7	0.1%	58
Others	25,371	19.0%		23,612	49.7%	
Total	133,784	100%		47,488	100.0%	

Table 4 shows investment by sector over the first nine months of 2011, compared to the same period in 2010. Total investment rose in each of the top ten sectors, with the largest jump occurring in the financial sector. Foreign investment into the financial sector rose from 3.7% to nearly half of all foreign investment in Russia. [6]

Table 4: Foreign Investment: Top Sectors (in USD million)

	Jan-Sep 2011		Jan-Sep 2010	
	%	Amount	%	Amount
Finance	49.1%	65,711	3.7%	1,764
Extraction of Fuel	9.6%	12,850	17.1%	8,115
Wholesale and Retail Trade	9.2%	12,363	18.3%	8,688
Production of coke and oil products	7.5%	9,997	10.5%	4,980
Metallurgy	4.4%	5,902	10.4%	4,950
Transport and Communications	4.1%	5,494	8.3%	3,952
Real Estate and Related Services	3.6%	4,782	8.1%	3,843
Chemical Industry	2.7%	3,636	3.5%	1,679
Food Industry	1.5%	1,964	3.9%	1,866
Production of vehicles	1.4%	1,845	3.3%	1,569
All Others	6.9%	9,240	12.8%	6,082
Total	100.0%	133,784	100.0%	47,488

CONCLUSION

Three-aimed policy action is essential to reinvigorate the economy:

- First, economic policies have to ensure stability. The recent tightening in monetary policy was an important step in this direction.
- Second, Russia has to build buffers against the external volatility. This means replenishing the reserve fund, moving towards inflation targeting and strengthening banking supervision.
- Finally, the government has to lift the growth potential of the economy. This means raising productivity and competitiveness, diversifying the economy in line with its longer-term goals. Making headway on this agenda will enable Russia to lift growth above 4 percent and more.

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Экономическое положение России в пост – кризисный период¹ Галина Бодрова² Татьяна Николаевна Огнева

¹ Сочинский государственный университет, Россия
354000, г. Сочи, ул. Советская, 26а

Студент

E-mail: galochka2211@yandex.ru

² Сочинский государственный университет, Россия
354000, г. Сочи, ул. Советская, 26а

Кандидат филологических наук, доцент

E-mail: tatyanaogneva@mail.ru

Аннотация. Отмечается замедление темпов глобальной экономики, включая страны еврозоны. Хотя по показателям профицита текущих операций экономическая ситуация России остается неизменной, перед лицом новых потрясений для уменьшения уязвимости экономики требуются согласованные усилия для корректировки бюджетного дефицита тех отраслей экономики, которые не связаны с нефтяной отраслью. По мнению г-на Путина акцент должен быть смещен в сторону от энергетического сектора к новым инвестициям и развитию инфраструктуры. Должна быть сформирована основа для создания и развития новых секторов экономики, чтобы модернизировать производственные мощности, освоить передовые методы управления производством и развить трудовые ресурсы.

Ключевые слова: кризис; бюджетная корректировка; уменьшить уязвимость; сальдо торгового баланса; модель экономического развития; модернизации производственных мощностей; развитие трудовых ресурсов; обновление технологии производства; сотрудничество с иностранными компаниями; доступ к глобальным рынкам; значительная поддержка государства.