

Business perspective of the current macroeconomic environment and forecast scenarios: implications for Russia

Slide 1

Good afternoon!

Slide 2

During the course of the last year it became evident that the forecasts predicting Russia's economic development were overly optimistic.

The World Bank forecast was the most accurate (although it was updated in December, when economic trends became evident). Bank of Russia forecast should also be noted as well grounded. It predicted zero growth in base scenario, and a 4.6 percent recession in the negative one.

Slide 3

Decline of investment growth rate, which began in 2012, was the first sign of the approaching crisis, and in 2013 this indicator showed negative dynamics for the first time. According to the base scenario of the Russian Ministry of Economic Development a further 1.6 percent fall is expected in 2016, which will mark the fourth consecutive year of investment decline.

Peak inflation rates were registered in January 2015, when it amounted to 3.9 percent against the previous month. The total annual inflation rate in 2015 will exceed 12 percent (Russian Ministry of Economic Development – 12.2 percent), whereas in 2014 it already went double digit (11.4 percent).

A full-fledged industrial recession began only in 2015. Before that annual growth rate was positive, despite slumping to negatives in certain months.

Slide 4

The monthly RSPP Index of Business Environment provides a different perspective. A sharp downward trend of the key economic indicators was registered as early as in September 2014 – the Index acted as a leading indicator. However, after the peak of the crisis in December 2014 – January 2015 business started to quickly adapt to high loan interest rates, sanctions, ruble devaluation, as well as to declining demand.

It does not mean, however, that business does not have problems – there are plenty of them. But overall, the Russian business proved its ability to work under the pressure of crisis.

Slide 5

What can be a driver of growth in the crisis situation aggravated by sanctions and tough international environment? Current discussions within the government and wider community suggest that strategic development vision is shaped solely by oil price forecasts and energy sector performance.

Over the past few years the share of energy sector in the Russian exports has grown by 3.5 percent, it also accounts for around one third of the total amount of fixed capital investment and more than 20 percent of GDP.

However the Draft Energy Strategy provides for the reduction of the fuel and energy complex share in exports to 33 percent, which implies a significant growth in non-energy sectors.

Slide 6

Significant restructuring of the economy requires growth of investment. Currently access to loan capital remains limited. In August an average annual interest rate exceeded 14 percent. It is an improvement as compared to the 20 percent registered in January 2015, but still forbiddingly high for implementing investment programs.

The tension between the industry and the banking sector is rising. Some business owners argue that Russian financial system is “usurious”. The head of one of the largest banks said that “there is no use to lend money to small and medium business as there is no demand for it in the country”. The problem is that, without providing SMEs with loan capital, there will be no structural change in the Russian economy.

Attractive and strong industrial companies grew up from small and medium businesses. Currently, however, they have to turn not to the bank but to development institutions, such as Industrial Development Fund, which provides 5 percent per annum loans.

Slide 7

Development institutions can address local issues, but they can not cope with systemic problems. Since 2007, the RSPP has been conducting a survey on the state of the business climate in Russia and a shortage of skilled workforce has always been mentioned among top three major constraints to business development.

The business community is actively involved in addressing this problem at the systemic level (*the development of professional standards, an independent evaluation of qualifications*), and the level of individual companies (*the establishment of corporate universities, equipping laboratories and transfer of equipment to educational institutions, scholarships*).

This problem is far from being solved. It is one of the reasons for low unemployment in Russia – 5.3% in August 2015 – as after the crisis it would be difficult for a company which fired employees to find the necessary staff in the market. A similar situation was observed during the last crisis.

Other issues – inflation, high taxes and mandatory social insurance payments, administrative barriers – are also categorized as the standard systemic problems. An exception is the concern over the unavailability of financing that grew dramatically in late 2014 and early 2015.

Slide 8

The unavailability of borrowed funds and shortage of working capital have started to negatively affect settlements – in September the concern about non-payments by counterparties increased sharply.

Business is also concerned about instability of exchange rates. Even the companies that have benefited from the devaluation of the rouble purchase equipment, raw materials and components abroad, and have to service debts nominated in foreign currencies.

The level of concern about the low demand has increased slightly, but the problem still affects only a third of the companies. This fact is supported by comparatively optimistic estimates of demand in the RSPP Index.

Slide 9

The list of measures implemented by companies to minimize the negative effects of the crisis is broad. Some companies are cutting costs of personnel, raw materials and services at any sacrifice. Others implement systemic measures – maintain or even increase the volume of investment programs and launch programs to introduce energy-saving technologies.

Slide 10

In general, the situation with investments is not ideal, especially when compared to that of key competitors. The level of gross fixed capital formation in Russia is lower than in China and India. Comparisons of other macroeconomic indicators are also unfavourable for our country.

Slide 11

The Russian share in global exports is higher than in other BRICS and Eurasian Economic Union (EAEU) countries except China, but Russia's exports primarily consists of fuel and energy products.

Slide 12

In terms of the share in global imports, Russia lags behind both India and China, although seriously outperforming the EAEU countries.

Slide 13

The situation with the economic growth forecast is even worse – Russia lags behind all BRICS and EAEU countries except Belarus with its similarly negative outlook. Even in Brazil, with its suboptimal economic situation, the growth rate in 2020 is forecast to be by 1 percentage point higher than that in Russia. In general, the Russian growth rates will be lower than in developed and, especially, developing countries.

Slide 14

As for the consensus forecast for 2016, the fall of GDP, continuing fall of investment and relatively high inflation are expected. The optimism of the Russian Ministry of economic Development is not justified because it is based solely on the increase in stocks.

As usual Business is more optimistic. The period of the economic crisis is an opportunity for the most active companies to make a breakthrough in their development, and for the state – to take up structural reforms and finally change the ineffective structure of the economy.