

MONITORING OF RUSSIA'S ECONOMIC OUTLOOK:

TRENDS AND CHALLENGES OF SOCIO-ECONOMIC DEVELOPMENT

No. 13(51) July 2017

MAIN TRENDS AND CONCLUSIONS	3
1. INFLATION UPSURGE AMID BAD WEATHER (A.Bozhechkova, P.Trunin).....	5
2. PROPENSITY TO SAVE: STRENGTHENING AT THE EXPENSE OF LENDING GROWTH (M.Khromov)	8
3. DEMOGRAPHICS: THE NUMBER OF BIRTHS IS DECLINING (A.Makarentseva).....	11
4. AGGLOMERATIVE EFFECTS IN RUSSIAN INDUSTRY (V.Gordeev, R.Magomedov, T.Mikhailova).....	14
5. GERMANY' PRESIDENCY IN THE G20: TESTING BY TRUMP (M.Larionova)	16
AUTHORS.....	20

Monitoring has been written by experts of Gaidar Institute for Economic Policy (Gaidar Institute), Russian Presidential Academy of National Economy and Public Administration (RANEPA) and Russian Foreign Trade Academy of the Ministry of Economic Development of Russia.

Editorial board: Sergey Drobyshevsky, Pavel Kadochnikov, Vladimir Mau and Sergey Sinelnikov-Murylev

Editors: Vladimir Gurevich and Andrei Kolesnikov



Monitoring of Russia's Economic Outlook: trends and challenges of socio-economic development. 2017. № 13 (51). July / Bozhechkova A., Gordeev V., Larionova M., Magomedov P., Makarentseva A., Mikhailova T., Trunin P., Khromov M. Edited by: V. Gurevich, S. Drobyshevsky, P. Kadochnikov, A. Kolesnikov, V. Mau and S. Sinelnikov-Murylev; Gaidar Institute for Economic Policy, Russian Presidential Academy for National Economy and Public Administration, Russian Foreign Trade Academy. 20 p. URL: http://www.iep.ru/files/text/crisis_monitoring/2017_13-51_July_eng.pdf

The reference to this publication is mandatory if you intend to use this material in whole or in part.

MAIN TRENDS AND CONCLUSIONS

There are serious, albeit hypothetical, threats that are coupled with small but already-realized risks. The weight of the threats is so uncertain that it tempts one to treat it as a fake, whereas the risks are in the spotlight and debated a lot although they weight much less than the threats.

The former definitely refer to the lengthy U.S. congressional debates on a new package of sanctions against Russia. There are way more than zero chances that the package will be endorsed because things are messed up in the White House. The White House has decided to join the sanctions, seemingly in exchange for reserving the U.S. President's right to repel them (it's perhaps the first time congressmen have ever attempted to arrogate to themselves the right). The negative economic and political potential of the draft bill is very significant, albeit not well calibrated yet, because it does not seem to be inevitable so far.

Bad weather conditions in Russia's European regions seem pale beside the foregoing. However, the weather-related upsurge of prices (which is untypical of this season) has prompted further analysis of inflation risks. When evaluating the June spike in inflation, our experts have mentioned another key interest rate cut in mid-June which, according to the experts, seems to be an untimely measure of monetary policy easing, and the central bank will therefore have to slow the pace of key interest rate cuts.

Although the underlying inflation (excluding the price change driven by seasonal and administrative factors) continued to decline – from 5.5% in January 2017 (relative to January 2016) to 3.5% in June, there are high risks that inflation will accelerate: the bearish trend for the rouble's exchange rate, moderate crop yield forecasts for this year, Fed's monetary policy tightening, as well as consumer demand recovery. Real personal income in May 2017 did not fall on a May-to-May basis. Furthermore, the retail trade turnover in April and May 2017 increased by respectively 0.1% and 0.7% compared with the same periods last year – first time since December 2014, seemingly driven by the growth in consumer crediting.

The growth in consumer crediting has further drawn attention of experts who claim this also caused the increase in households' propensity to save in bank deposits, in cash and in securities in the first five months of 2017. Savings in that period increased by a total of Rb 970bn compared with Rb 777bn in the same period of 2016. The amount of cash in circulation and the propensity to purchase foreign currency in cash (foreign currency in hands increased approximately 10%) also increased. Amid stagnating real incomes, however, the growth in consumer crediting (individuals' credit outstanding increased Rb 264bn) is regarded as somewhat financial risk facing households.

Experts studying the demography in Russia have noted that Russia's economic stagnation had no effect on the fertility behaviour. The average fertility rate (births per woman) stood at 1.75–1.78 over a few years. However, the number of births in Russia continues to decline in 2017 because of a small size of the female generation at the peak of fertile age (the negative dynamics has been observed since the H2 2016). It has long been realized that

the sex-age structure of the Russian population will 'shrink' inevitably. Demographic holes of type as it is now have been occurred almost every quarter of a century since WWII. The latest small-size generation was born in the 1990s.

In the end, a certain decline in the death rate can no longer offset the decline in the number of births, and therefore Russia is again faced with a natural population decline (-112,000 persons in the first five months of 2017). And, the natural population growth in Russia in 2013–2015 was reduced to zero as early as in 2016. Since the number of births is declining, the birth/death rate can hardly be expected to become positive again if there is some possible decline in the death rate. According to Rosstat's "medium-case" forecast, the number of births will continue declining almost steadily over the decade to come, and it is not until nearly 2030 that the annual number of births is expected to stabilize at a level of 1.5 million (compared with almost 1.9 million in 2016) and to start growing for a long period of time.

The decline in the number of births shouldn't be confused with the decline in the fertility rate (births per woman) which is not the case: the fertility rate remains overall stable across the country. However, the fertility rate has indeed fallen in rural areas over the past three years, whereas the stability is accounted for by urban population.

The effect of cities or rather agglomerative effects are also studied in terms of the extent to which they can affect productivity in the industrial sector. Some researchers show that the effects in the manufacturing industry of West European countries comprise about 5% of the total factor productivity, if a city doubles in size. Our authors assume that the effect in Russia is twice as much as that in West European countries: if a city has a population twice as large as the population of another city, then the firms operating in the former would be by 8–10% more productive than the firms operating in the latter. For example, the average productivity in the vicinity of Moscow and St. Petersburg decreases steadily with a distance from the cities (productivity at a distance of 200 kilometres is 40% below the productivity in the centre of agglomerations). Considering various factors that create the agglomerative effect (ranging from the level of competition to the convenient geographical location of a city), experts assume that this also may be associated with migration of workers seeking to realize their potential in large cities.

A completely different type of migration (first of all, a mass inflow of refugees) was considered among the three new key issues – along with digital economy and healthcare issues – which were raised at the recent G20 Summit. Germany's G20 Presidency amid the effect of "the Trump factor" is the topic of an expert review. ●

1. INFLATION UPSURGE AMID BAD WEATHER

A.Bozhechkova, P.Trunin

The Russian consumer price inflation gained speed in June 2017, up 4.4% from June 2016, which is 0.4 p.p.s above the Bank of Russia's target inflation rate for 2017 and 0.3 p.p.s above the rate seen in May 2017. The price rise was driven basically by the increase, due to adverse weather conditions, in food prices which appears to be temporal. However, the current inflation dynamics may force the Russian central bank to slow its easy monetary policy in an environment of continuing high inflation risks including a lean crop yields, rouble depreciation, consumer demand rally, as well as uncertainty about the fiscal policy.

The Bank of Russia cut the key interest rate in mid-June by 0.25 p.p.s to 9% p.a. – for the third time in a year. However, given the inflation data for June that were published early in July, this monetary easing seems to be somewhat untimely.

As a reminder, the January–May inflation rate dropped to 4.1% in April and May (relative to April and May 2016) from 5% in January (relative to January 2016), thus getting much closer to the Bank of Russia's target inflation rate. Inflation slowed in the first five months of 2017 in response to sluggish recovery of aggregate demand, as well as because of the rouble depreciation. However, consumer prices picked up sharply to hit 0.6% in June, an increase of 4.4% from June 2016 (Fig. 1).

The increase in consumer price inflation was first of all driven by the upsurge of food prices in response to adverse weather conditions. Food prices in June increased by an overall of 1.0% (+0.1% in June 2016), and prices of fresh fruits and vegetables were up to 8.3% from May (-1.1% in June 2016). Some food price inflation started up as early as April 2017 as the previous-year's harvest stocks depleted, with food prices hiking by 0.6% (0.1% in March 2017).

Despite the growth in food price inflation, the underlying inflation rate (the price change driven by seasonal and administrative factors is excluded) continued to fall since January 2017. For instance, while in January the underlying inflation rate stood at 5.5% (from January 2016), in June it reached 3.5% (from June 2016) – an argument in favour of the assumption of one-time seasonal inflationary shock in June. However, given the fact that the Russian Ministry of Agriculture downgraded in June its wheat crop forecast for 2017 from 110 to 100–105 million tonnes as a result of unfavourable weather conditions, there are high enough risks that food prices will continue to grow.

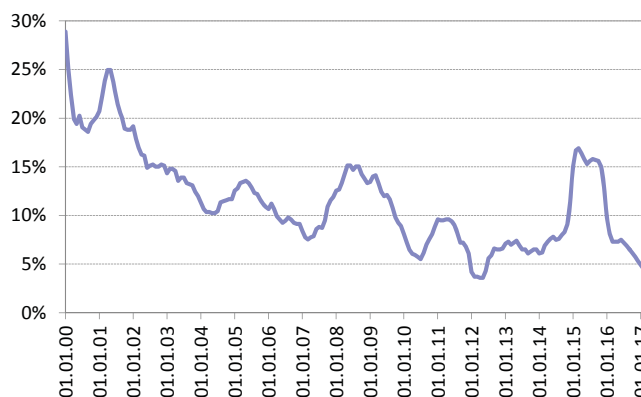


Fig. 1. CPI growth rate in 2011–2017, % change from the previous 12 months

Source: Rosstat.

A survey by InFOM (a sociological and marketing research firm) shows that median inflation expectations among individuals remained unchanged in June after declining to 10.3% in May from 11% in April 2017, which was seemingly driven by the above time factors associated with the food price rise. Furthermore, the Bank of Russia's estimates based on surveys of anticipated inflation movements give evidence of declining inflation expectations among individuals. For instance, the Bank of Russia's probabilistic estimate obtained through "overlapping" respondents' estimates on the current inflation rate was 3.8%, which is lower than the current inflation rate¹.

Non-food prices in June increased 0.1% (0.5% in June 2016). Price inflation of non-food products slowed at a faster pace than other items (0.2% in May 2017 compared with 0.4% in May 2016), seemingly driven by, among other things, the rouble appreciation in January–May 2017. Prices and rates of paid services to individuals in June 2017 increased 0.7% (0.6% in June 2016) mostly in response to a seasonal rise of prices of passenger transport services, health and leisure services, and outbound travel services.

Thus, accelerating inflation in June was indeed driven by short-term factors. However, other risks may be realized before the end of the year. Consumer demand recovery can become a source of acceleration in inflation in addition to the weather-related depressed crop yields: in May 2017, for instance, real personal incomes saw no change compared with May 2016, whereas they were falling during the previous three months. Furthermore, real wages were on the rise since August 2016, with growth rates gaining 3.7% in May 2017 compared with the same period last year. Furthermore, the retail trade turnover in April and May 2017 increased by respectively 0.1% and 0.7% compared with the same periods last year – first time since December

1 The Bank of Russia Bulletin "Inflation Expectations and Consumer Sentiment", No. 6, June 2017.

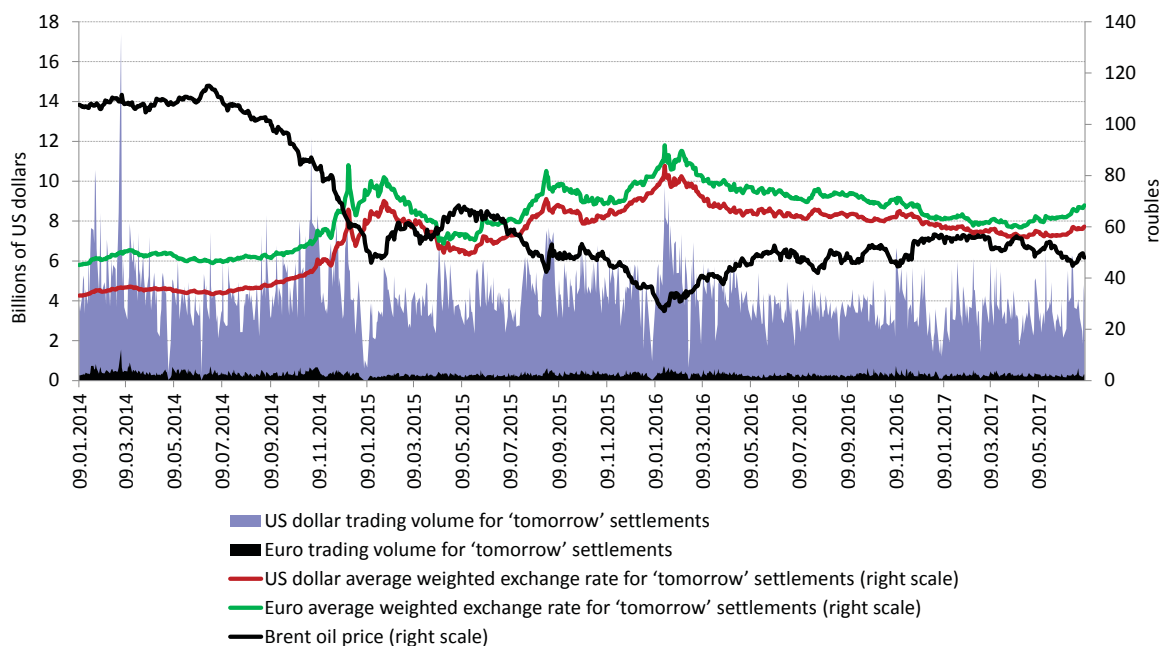


Fig. 2. Dynamics of the rouble's exchange rate to the US dollar and Euro, forex market trading volume, Brent oil price
Sources: Russian central bank, Finam.

2014, seemingly driven by the growth in consumer crediting. For instance, since March 2017, the growth in consumer credit outstanding, as adjusted for the exchange rate revaluation, reached a positive value of Rb 80.1bn in May – first time since October 2014 (excluding August 2016).

In the coming months, inflation will be accelerated by the rouble's exchange rate dynamics. The rouble-dollar exchange rate dropped 6.5% to 60.4 roubles in June/first week of July, which is bound to be reflected in the price dynamics given a big proportion of imported goods in the Russian consumer goods basket. The rouble's devaluation in question is primarily associated with a decline of 7.1% (to USD 46.7) in oil prices in June/early in July 2017 (a local low of USD 44.76 per barrel was reached on 21 June 2017) (*Fig. 2*). Over the longer term, the exchange rate dynamics can also be driven by further tightening of Fed's monetary policy coupled with falling interest rates in Russia, thus making US assets more attractive, triggering capital outflows from other markets, including from Russia.

Thus, the Bank of Russia, faced with possible risks of accelerating inflationary processes in 2017, will have to rethink the pace of lowering the key interest rate. Moreover, accelerating inflation is a challenge for reaching regulator's targets, particularly if the above risks are realized. ●

2. PROPENSITY TO SAVE: STRENGTHENING AT THE EXPENSE OF LENDING GROWTH

M.Khromov

In the course of the first five months of 2017, people tended to save in cash, bonds and in their bank accounts. One of the reasons could be retail lending growth, which increased households access to financial resources and resulted in larger assets savings.

In January–March 2017, the amount of household funds placed into bank accounts and deposits moved up by Rb 356bn¹, which constituted 2.0% of disposable household income over the period. Compared to the same period of 2016, growth of retail bank deposits has gone up by 22% against Rb 291bn or up 1.7% of disposable household income registered a year earlier. Growth rate has also gone up. During the first five months of 2017, the amount on deposits increased by 1.5% against 1.2% a year earlier.

Overall boost of savings dynamics in bank accounts was accompanied by a slowdown of growth of deposits on bank accounts denominated in rubles. Deposits denominated in national currency grew over five months of 2017 by Rb 472bn or by 2.6% compared to Rb 517bn or 3.2% registered a year earlier. The volume of household funds on bank accounts and deposits denominated in foreign currency on the contrary was shrinking both in the current and in previous year. However, the rates slowed down from 3.4 to 2.1%, which not only has offset the slowdown of ruble deposits growth but also ensured increase of the overall volume of household bank deposits.

Analysis of solely bank deposits dynamics is insufficient for assessment of households' propensity to saving. It is necessary to take into consideration changes in other households financial assets – cash and bonds. Moreover, it is paramount to keep in mind dynamics of financial obligations – credit indebtedness.

Let us analyze changes, which took place in the household preferences regarding financial instruments different to bank deposits. The volume of cash in circulation outside of the banking system (monetary aggregate M0) went up by Rb 98bn over 5 months of 2017. Purchases of foreign currency in cash by households have grown significantly. The amount of foreign cash in the hands of the population increased by around 10% (the ruble equivalent constituted Rb 280bn) over five months². This amount is much higher than the one posted a year earlier when growth rates of foreign cash in the hands of the population constituted around 3% (Rb 65bn in terms of national currency). This led to the aggregate amount of cash to growth over five months of 2017 by Rb 378bn, which came to 2.1% of disposable income of households. This is three time more than a year earlier when cash saving growth constituted barely 0.7% of disposable income (Rb 123bn).

1 Dynamics of deposits denominated in foreign currency was adjusted to the change of the ruble to dollar and euro exchange rate.

2 1st quarter – data released by the Bank of Russia, April–May – IEP estimates.

Thus, households tend to save in cash as well. Although the currency structure and its dynamics differ significantly from bank deposits.

A different picture is observed regarding savings dynamics in bonds. According to Rosstat, in January–May 2017, households spent Rb 235bn on bonds or 1.3% of their disposable income. This fact demonstrates a reduction of interest towards this type of asset by more than one third compared to the same period of 2016 when households' savings in bonds increased by Rb 363bn or by 2.1% of the disposable income.

At the same time, overall growth of savings on bank deposits, in cash and bonds for the first five months of 2017 exceeded the amount registered for the same period of 2016 – Rb 970bn against Rb 777bn or 5.3% of disposable income compared to 4.4% a year earlier.

Speaking about bank lending to households, which constitute a bulk of their financial liabilities, one can distinguish the following. Although retail debt on bank loans resumed an upward trend from April 2016, and on the whole for the period January–May 2016 its growth was negative – Rb 71bn. (0.4% of disposable income). Small contraction of the retail lending was due to the ongoing recession in consumer lending, which shrank by Rb 257bn and growing housing credit (+Rb 185bn). In 2017, downward trend of consumer lending halted and from March retail indebtedness on consumer lending has been growing steadily. Three months growth has exceeded contraction registered in January–February and on the whole, during five months consumer lending has increased by Rb 150bn. Growth of residential loans debt has slowed down to Rb 114bn. However, overall volume of retail credit exposure has gone up by Rb 264bn, which constitutes 1.4% of households' disposable income.

Table 1

DYNAMICS OF CHANGE OF HOUSEHOLDS' MAIN FINANCIAL ASSETS
AND OBLIGATIONS FOR JANUARY–MAY 2016 AND 2017

	January–May 2016		January–May 2017	
	Rb bn.	% of disposable income	Rb bn.	% of disposable income
Funds in bank accounts and deposits, total	291	1.7	356	2.0
Including in rubles	517	2.9	472	2.6
In foreign currency	-226	-1.3	-116	-0.6
Cash, total	123	0.7	378	2.1
Including foreign cash	58	0.3	98	0.5
Foreign cash	65	0.4	280	1.5
Savings in bonds	363	2.1	235	1.3
Total savings	777	4.4	970	5.3
Bank loans debt («-» – loans growth, «+» – reduction)	71	0.4	-264	-1.4
Including housing loans	-185	-1.1	-114	-0.6
Consumer loans	257	1.5	-150	-0.8
Balance on financial instruments	848	4.8	706	3.9

Table 1 provides a summary on households' transactions with financial instruments for the first five months of 2016 and 2017. The table demonstrates that growing households' propensity to save was accompanied by a robust recovery of retail credit activity. On the one hand, the real disposable income

stopped contracting in 2017, which indicated their growth in the nominal terms. This on its own led to increase of both nominal spending on final consumption and on investment in financial assets. On the other hand, resumption of consumer credit growth has expanded households' financial resources, which in the wake of close to zero growth rates of real income exposes additional risks for sustainable financial state of the population. ●

3. DEMOGRAPHICS: THE NUMBER OF BIRTHS IS DECLINING

A.Makarentseva

In 2017, the number of births began declining. This is due to the population makeup according to sex and age. To be more precise, it is due to small number of women at the peak of reproductive age. Another demographic hole is forecast for a period of at least 10 years. Despite the decline in the mortality rate, we will not manage to offset the decline of births – according to the results for 5 months of 2017, natural population decline totaled to 112,000 individuals.

The inevitability of sex and age group contraction that would eventually hit Russia was mentioned for several years. Such demographic gaps pop up around once in 25 years since 1945 (Fig. 1). The latest scanty generation was born in 1990s.

Growth and decline of the total number of births do not linearly depend on the number of women of reproductive age. This indicator is affected by birth-rate intensity in various age groups. At present, the peak of births accounts for women at 27 who were born in the 1990s. Mother's age when giving birth to the first child hits 25.5 years (up 3 full years in two recent decades). Due to this fact as well as to the fact that recently the birth rate in the range of reproductive age of 25–34 was high; the period of large generations lasted longer than was expected.

According to the Rosstat forecast, it is projected that in the coming decade there would be constant decline of births. Solely by around 2030, annual number of newborns will stabilize at 1.5 mn (for comparison: 2016 saw nearly 1.9 newborns) and will grow for a prolonged period.

Newborns decline was already noticeable in the second half of 2016. The first five months of 2017 saw 83,300 less births than registered for the same period of last year (679,200 and 762,500 respectively) (Fig. 2). In modern Russia, the number of births does not significantly depend on seasonality, although during a year there are certain ups and downs. In particular, a decline in births is traditionally linked to a decline of marriages registered in May (in 2017, the number of marriages registered in May is half the number of marriages regis-

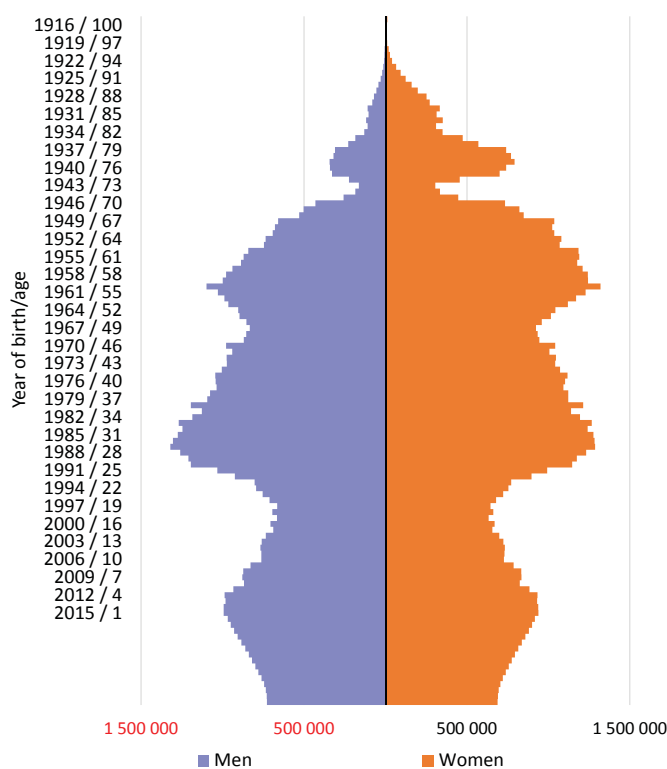


Fig. 1. Number of population according to gender and age for 01.2016, persons; forecast number of births in coming years
Source: data released by Rosstat, Rosstat average forecast.

tered in April and this is a customary situation). Despite a change in behavior in marital-reproductive sphere, provisional correlation between marriage registration and birth of a baby remains strong – at present more than half of mothers under 30 conception and marriage registration occur within a year. Recently, the peak of births fall for July and August.

As against 2016, decline of newborns has already affected all regions of the Russian Federation with solely 20 subjects registering such decline at less than 10 p.p.s (Fig. 3). There is no obvious social and regional component in this trend. Moreover, timely monthly statistics is rather volatile at the regional level. It is clear that neighboring and similar in social and economic profile regions this decline dynamics can differ. Decline in newborns “is lagging behind” in the regions where firstborns arrive at a later age – first, Moscow and Moscow region, certain northwestern regions. Regions with early reproductive age (North-Caucasus federal districts, Altai regions) register a reduction of the total number of birth earlier and there it goes unevenly.

Despite a gradual mortality decline, the number of deaths in the near future is unlikely to fall below the number of births. In the first five months of 2017, natural decline of population totaled to 111,800 persons (natural decline of population according to monthly data for 2017 is registered in 65 regions of Russia). In 2013–2015, natural growth of population was observed, which came to naught in 2016.

General birth rate coefficient (number of births per one thousand of population) totaled to 11.2 permille in January–May 2017. There are no reasons to speak about significant movement in birth rate intensity. The average number of babies per a woman has for several years been staying in the range of 1.75–1.78 babies.

The ongoing stagnation has not reflected on the reproductive behavior of the population. The birth rate is stable owing to the urban population, meanwhile the birth rate in the rural areas (around 30% of Russian population) in recent three years has been declining.

A number of long-term structural changes stand behind the birth rate dynamics. There is more and more evidence that among women born in the 1970s the level of final childlessness is growing compared to the previous generations. Our forecast of childlessness growth coincides with the estimates made for the entire Eastern and Western Europe – and stays around

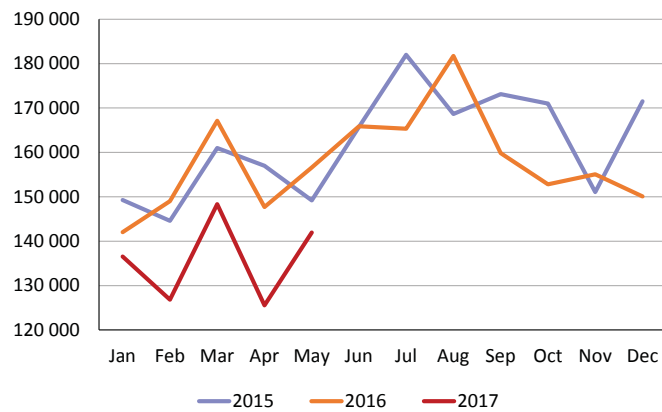


Fig. 2. Monthly number of births, babies

Source: The unified interdepartmental statistical information system (UISIS), timely information released by Rosstat.

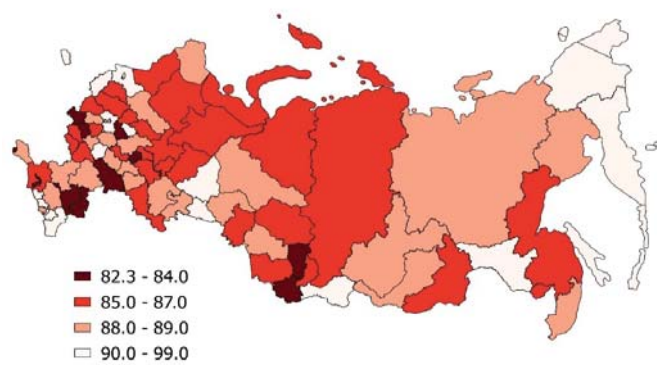


Fig. 3. Ratio of total birth coefficient in January–April 2017 to January–April 2016, in %

Source: timely information release by Rosstat.

15–20% (previously it stayed in the range of 6–8%).

This is a new phenomenon for Russia in contrast with, for example, widely discussed issue of delaying births. During recent two decades, the average age of first time moms has grown significantly. However, it grows not so fast and still is significantly less than in many European countries. Urban population represents the driving force in this respect. In addition, it is not a “new demographics reality” – if we compare with early 1960s increment of this indicator constituted around one year.

Delaying to give a birth does not lead to a decline of the final number of births in a generation and to a high rate of childlessness. There are countries where despite the high age of first-time mothers childlessness stays at a low rate (for example, Portugal) and the fertility rate, the number of children per woman – stays high (for example, Ireland).

Finally, the growth rate of third and more births per woman attracts attention. Now, they constitute around 18%, which roughly is similar to the situation seen in mid-1980s but is still far from the level posted in the 1960s (Fig. 4). Cumulatively, these factors demonstrate that the dominant during couple of decades’ model of a single child family has stopped being wide-scale.

Despite the fact that demographic “hole” represents a common phenomenon for Russia, it poses a challenge for social infrastructure. State system of preschool education faces it first. One should hope that there are no mass closures of institutions for kids and a promise of accessibility of nurseries will be carried out. Discussions about stimulating the fertility take a new round. Had the program known as “mother’s capital” not been implemented in 2007, it should have been invented now. Additional measures for material incentives are been widely discussed, however their impact is not very high. On the whole, one should acknowledge that we will not be able to avoid the effect of small number of mothers and consequently of a serious decline of births in the near future. ●

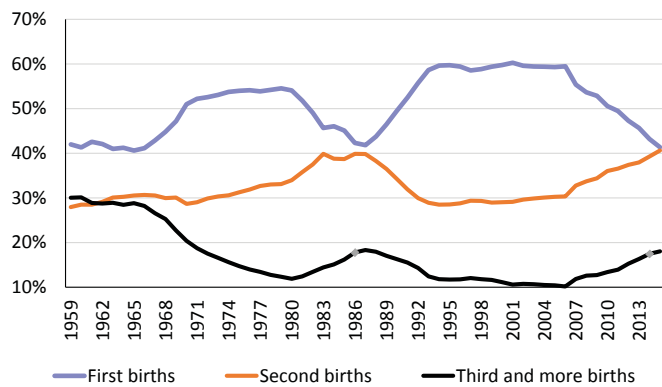


Fig. 4. Share of first, second, third and more births in the total number of births, 1960–2015, %

4. AGGLOMERATIVE EFFECTS IN RUSSIAN INDUSTRY

V.Gordeev, R.Magomedov, T.Mikhailova

Agglomerative effects in the Russian manufacturing industry are significant and higher on average than in West European countries. Also, there is a marked “agglomeration shadow effect”, that is, firms’ productivity tends to grow in the vicinity of large cities and to decline with distance from an agglomeration centre. With the Russian economic development as it is now, the growth in industrial employment in large cities is a reserve productivity-enhancing tool.

The modern economy is driven by cities where there is high concentration of population, firms, market transactions. Indeed, most of the value added is created by cities. The larger a city and the density of its population is, the higher is the labour and capital productivity in the city.

The agglomerative effects observed in the manufacturing industry of West European countries account for about 5% of the total factor productivity, if a city doubles in size. These results have been obtained by some researchers¹.

What are the mechanisms driving agglomerative effects? Large cities are on the winning side in terms of productivity due to their convenient geographical locations such as intersections of convenient transport routes, seashores and navigable waterways. Large cities are attractive to most ambitious and efficient labour migrants. In addition, large cities offer strong competition which only the most efficient firms can meet.

Of practical interest is to measure the size of agglomerative effects for a wide range of firms, geographic locations and branches of the Russian manufacturing industry. Knowing and understanding the relation of the indicators of geographical distribution of economic activity in the Russian Federation and the economic effectiveness at the level of small economic entities such as firms and enterprises can enable us to increase the effectiveness of the evolution of the spatial pattern of the Russian economy, to realize its economic implications, and to develop a regional policy built on the above factors.

When sampling out of more than 70,000 manufacturing industry enterprises employing 10 or more workers across the country, we evaluated the extent to which firms’ productivity depends on the size of their location. On average, if a city has a population twice as large as the population of another city, then the firms operating in the former would be by 8–10% more productive than the firms operating in the latter. In Russia this proportion is higher than in western countries.

However, the cause-effect relationship can be reversed, too. For example, it is not particularly the size of a city but cities themselves that are build and

¹ See Sveikauskas L. “The productivity of cities” (The Quarterly Journal of Economics, 1975. pp. 393–413), Combes P.P., Duranton G., Gobillon L., and Roux S. “Estimating agglomeration economies with history, geology, and worker effects” (“Agglomeration Economics”, University of Chicago Press, 2010. P. 15–66) and Combes P.P., Duranton G., Gobillon L., Puga D., and Roux S. “The productivity advantages of large cities: Distinguishing agglomeration from firm selection” (Econometrica, Vol. 80, No. 6, 2012. P. 2543–2594).

grow in locations geographically favourable for economic activity that make firms more productive. Or there is another explanation: it is not agglomerative effects but the inherent advantages of geographical location that affect the productivity.

Alternatively, agglomerative effects are created through the self-selection of workers and producers: the most enterprising businessmen and competent workers tend to realize their potential in large cities. Thus, migration tends to increase the productivity in larger cities and to decrease it in small and medium-size cities from where best workers migrate to larger cities.

We have studied these possible alternative explanations using instrumental variables, that is, the data on urban population in 1897 and in 1959. The economic pattern and the technological level at that time differ to the extent that the history of population density can be assumed as having no direct effect on modern productivity. Migration today is even far less dependent on heritage.

There is another explanation of the agglomerative effects in question – fierce competition in large markets. There are many consumers and firms in large cities. Competition gets tougher with increasing number of firms in the market. Least efficient producers fail to compete and go bust, and such a rigorous selection boosts the average productivity. We have tested the hypothesis according to which the competition effect tends to force the worst (of the survived) firms to catch up with average firms in large cities.

The findings show no effect of self-selection. Inefficient producers are not forced out from large markets, but rather, large markets make it easier for firms to stay in business: producers are even more efficient in large markets than in small cities. At the same time, however, large markets create leaders of industry: highly productive firms are more typical of agglomerations.

Thus, the market size in modern Russia is not related to a tougher competition. Rather markets in large cities are not saturated enough, competition is weak, and even inefficient producers have an opportunity to find a distribution area.

Furthermore, in the geographical vicinity of large agglomerations the average productivity declines steadily with distance from an agglomeration centre. For example, the average productivity in the vicinity of Moscow and St. Petersburg decreases steadily all the way up to 200 kilometres from the cities. Productivity at a distance of 200 kilometres is 40% below the productivity in the centre of agglomerations.

Agglomerative effects in the Russian manufacturing industry are strong and direct, thus increasing the productivity of all the firms in locations with higher population density. Therefore, the potential of redistribution of economic activity toward Russia's large cities is substantial and yet to be fully implemented. ●

5. GERMANY' PRESIDENCY IN THE G20: TESTING BY TRUMP

M.Larionova

For nearly a decade, the G20 has united leaders of developed and developing countries to deal with common challenges. There are different assessments of its role in handling the crisis and solving global management issues. But it is obvious that amid the changing situation in the world, worsening of the environment and growing hostility to the globalization¹ the G20 remains a major economic cooperation forum. In 2017, Germany chairs the G20 and it is possible to sum up the preliminary results.

Challenges and Expectations

With the 45th US President taking the office – Donald Trump is known for his tough rhetoric in respect of the multilateral trade policy and the Paris Climate Change Agreement – the G20's chances to advance cooperation in problem lines (fight with protectionism, negotiations on the outstanding issues of the Doha agenda and timely implementation of the Paris Agreement) are thrown into question. Further uncertainties were related to participation in the G20 summit of new leaders of Brazil, France, the US, Korea and Italy. The results of the referendum on the UK membership in the EU, the June elections in the UK and the start of the Brexit negotiations required mobilization of efforts to develop domestic and pan-European positions on the parameters of “the agreement on the orderly exit” and future cooperation².

There are other factors which limit the potential of Germany's presidency in the G20. Germany's permanent and large current account surplus is regarded by the international community as a factor which may give rise to global imbalances. Also, partners are critical of the fact that the German government does not utilize the available large fiscal space to stimulate domestic demand and economic growth in Europe and other countries. Germany's efforts to implement the agenda of sustainable development till 2030 were criticized at the national level³. In addition, the September parliamentary elections, emergence of Martin Schultz, a new prominent figure who is running for the office of the German Chancellor from the German Social-Democratic Party, and the growing popularity of the populist *German Alternative* party have added up tensions to the domestic politics.

At the same time, there were high expectations from Germany's presidency due to both external and internal factors. Firstly, the need to respond to growing challenges of deglobalization, economic inequality and climate

1 Cheng, Shuaihua (2017) When it comes to 'saving globalization' world leaders are still missing the point. 3 January. Geneva: World Economic Forum. https://www.weforum.org/agenda/2017/01/when-it-comes-to-saving-globalization-world-leaders-are-still-missing-the-point?utm_content=buffer47b7b&utm_medium=social&utm_source=twitter.com&utm_campaign=buffer

2 European Council (Art. 50) guidelines for Brexit negotiations. <http://www.consilium.europa.eu/en/press/press-releases/2017/04/29-euco-brexite-guidelines/>

3 T. Fues (2017) The Priorities of Sustainable Development in G20's Activities: Opportunities and Challenges for Germany's Presidency // Bulletin of International Organizations: Education, Science and New Economy. V. 12, No. 2.

change is forming a request for resolute collective actions which Germany could stimulate. Secondly, having both a significant economic and diplomatic influence and intent to promote multilateral cooperation, Germany is able to upgrade the efficiency of the G20 and consolidate the role of the forum as a general wellbeing guarantor^{1,2}.

The Priorities

The priorities of the presidency presented by Angela Merkel on 30 November 2016 were divided into three groups of issues united by the slogan: "Building Resilience – Improving Sustainability – Assuming Responsibility". "Building of Resilience" includes issues typical of the G20 agenda issues, such as promotion of economic growth through structural reforms, monetary and fiscal policy measures, consolidation of the financial architecture and development of financial markets; prevention of a tax base dilution and tax evasion, fighting protectionism and consolidation of multilateral trade and investment regimes, creation of quality jobs and promotion of labor efficiency.

Cooperation within the "Improving Sustainability" group is focused on protection of the climate, promotion of energy stability, creation of incentives for investment into a viable infrastructure and technological innovations. Carrying out of the agenda of the sustainable development till 2030 and handling of digital technology promotion issues, development of digital infrastructure and creation of norms, standards and international regulation rules in digital trade and economy have become central issues of cooperation within the frameworks of the presidency. For the first time in the G20 history, the meeting of ministers responsible for the digital economy was held. The meeting set the lines of collective activities under the digitalization road map.

The need of collective efforts to prevent pandemics, create sustainable healthcare systems and overcome the risks of resistance to antimicrobials was on the agenda of the meeting of healthcare ministers held for the first time in history and aimed at rendering political support to international initiatives and the leading role of the World Healthcare Organization (WTO) and the UN in dealing with global healthcare problems.

Along with such traditional issues for the G20 as fight against terrorism, corruption and food security, Germany's presidency set the goal of solving the problems of refugee protection and root causes of displacement and illegal immigration.

The Summit Decisions

What will be the legacy of Germany's presidency for the partners?

The geopolitical issues – North Korea's missile tests, the war in Syria and the diplomatic crisis between member-states of the Cooperation Council of Arab States of the Gulf – which dominated during the summit did not prevent the G20 to agree upon the key economic agenda issues and formulate obligations to increase employment, complete the financial sector reforms, promote efficiency and prominence of international economic and financial in-

1 Cooper, Andrew F. (2014) The G20 and Contested Global Governance: BRICS, Middle Powers and Small States. In: Caribbean Journal of International Relations & Diplomacy. Vol. 2(3), September 2014. P. 87–109.

2 Priorities of the 2017 G20 summit, p. 2. <http://www.ranepa.ru/images/media/g20/2017hamburg/2016-g20-praesidentschaftspapier-en.pdf>

stitutions, fulfill the plan on prevention of tax base dilution and withdrawal of profit from taxation and implementation of the G20 Anticorruption Plan. Also, the G20 summit launched the *Partnership with Africa* initiative, approved the G20's Hamburg Climate and Energy Plan and the Sea Litter Fighting Plan. The report on implementation by the G20 of obligations to facilitate development and the plan of collective actions to assist fulfilment of goals of sustainable development till 2030 were approved.

The Hamburg Plan defines a set of new measures aimed at promotion of resilience of the G20's economies to shocks and consolidation of social unity and trust. The leaders reaffirmed their readiness to carry out growth strategies, particularly, structural reforms to achieve the goal agreed upon in Brisbane to increase by additional 2% the aggregate growth of the G20' economies by 2018 as compared to the projected trajectory.

Angela Merkel's remarks at the meeting with the business circles that preservation of the achievements is sometimes an achievement¹ are evidence of the fact that G20 negotiations on climate and trade issues are difficult. Indeed, though in the G20's communique no mention was made of a traditional obligation not to use new protectionist measures and reduce the existing ones and the role of trade protection legitimate instruments was recognized for the first time, confirmation of the G20's commitment to open markets, nondiscrimination principles, fight against protectionism, transparency and compliance with the WTO's rules of bilateral and multilateral agreements can be regard as success. The leaders called for complete fulfilment of the WTO agreement on making trade simpler².

The G20's communique and the Hamburg roadmap on climate and energy reflect the specific US position on the Paris agreement and the declaration of 19 members of the G20 that the Paris agreement is irreversible. Thus, it demonstrates political will to implementation of the agreement. Recognition by the US of its intent to cooperate actively to facilitate cleaner and more effective utilization of fossil fuel and access to it, as well as apply renewable and other clean energy sources is a success³.

As regards the three new priorities: digitalization, healthcare and migration, the most concrete and ambitious objectives have been formulated in respect of the digital economy. The leaders set the lines of collective actions to ensure efficient competition in order to stimulate investments in innovations, promote development and utilization of market-based international standards of digital production, create predictable and transparent digital trade conditions, effectively protect consumer rights and intellectual property rights and ensure transparency and security in information and communication technologies (ICT)⁴.

In healthcare, it is worth mentioning a concrete arrangement to carry out in full national plans by the end of 2018 to prevent resistance to antimicro-

1 Speech by Federal Chancellor Angela Merkel at the G20 dialogue forum with business associations (B20) in Berlin on 3 May 2017. P. 3. https://www.g20.org/Content/EN/Reden/2017/2017-05-03-bk-merkel-b20_en.html?nn=2186566

2 The Communique of the G20 Leaders on the Summit in Hamburg (Germany) on July 7–8, 2017. P. 3–4. http://www.ranepa.ru/images/media/g20/2017hamburg/comm_2017.pdf

3 Ibid. P. 16

4 Ibid. P. 7.

bials and support the UN and WHO's activities to strengthen healthcare systems and build up the potential to respond to emergency situations¹.

Networking and cooperation arrangements as regards displacement and migration are more modest. General understanding of a country's sovereign rights to carry out management and control of its borders and develop national security measures and measures of humane and safe repatriation and reintegration of migrants was formalized. The G20 leaders agreed on coordinated actions to be taken in respect of root causes of displacement and approved a set of the G20's practical measures on fair and effective integration of legal migrants and persons with a refugee status into labor markets².

Thus, during Germany's presidency a foundation for cooperation in priorities set by its presidency was laid, some progress was achieved in the forum's key lines of activities, statements against protectionist trends in the international trade were made, the G20's commitment to the Paris Climate Change Agreement was reaffirmed and cooperation in sustainable energy and energy efficiency was promoted. The G20 reconfirmed its role as a key forum of economic cooperation. ●

1 The Communique of the G20 Leaders on the Summit in Hamburg (Germany) on July 7–8, 2017. P. 13–14. http://www.ranepa.ru/images/media/g20/2017hamburg/comm_2017.pdf

2 Ibid. P. 23–24.

AUTHORS

Alexandra Bozhechkova, Head of Monetary Policy Department, Gaidar Institute; senior researcher, IAES, RANEPA

Vladimir Gordeev, researcher, Industrial Organization and Infrastructure Economics Department, IAES, RANEPA

Marina Larionova, Director of the Center for International Institutions Research, RANEPA

Rustam Magomedov, researcher, Industrial Organization and Infrastructure Economics Department, IAES, RANEPA

Alla Makarentseva, Head of Demography, Migration and Labor Market Studies Department, Institute of Social Analysis and Forecasting, RANEPA

Tatiana Mikhailova, senior researcher, Industrial Organization and Infrastructure Economics Department, IAES, RANEPA

Pavel Trunin, Director of Center for Macroeconomics and Finance, Gaidar Institute; leading researcher, Center for Central Banks Issues, IAES, RANEPA

Mikhail Khromov, Head of the Financial Research Department, Gaidar Institute; senior researcher, Structural Research Department, IAES, RANEPA