

Current crisis and its impact on Russia's foreign trade¹

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Abstract

Current economic crisis regardless of its obvious peculiarities clearly supports a trend which already revealed itself during several previous decades. Namely, in most cases volatility of foreign trade tended to be substantially higher in comparison with that of general macroeconomic indicators like GDP or industrial production. Russian Federation being characterized by relatively high level of functional foreign trade openness appears to be very sensitive to abovementioned trend. The paper attempts to assess the scale and scope of influence the crisis has on current state of Russian foreign trade as well as certain aspects of foreign trade developments' influence upon the national economy.

Key words: Economic crisis, foreign trade, Russian economy

1. Introduction

Crisis in general might be defined as a reaction of the particular system on imbalances (violation of some key proportions) between its elements when these imbalances exceed certain affordable limits. Reaction under review in most cases tends to be a) relatively fast and b) pretty painful. The crisis could result either in a restoration of previously violated balance (some key proportions) and hence renewal of what might be called a "regular" operation of the system, or in a collapse of the system.

Abovementioned definition is totally applicable to current economic crisis. In this case enormous scale and scope of various speculative transactions largely influencing performance of global financial system constitute one of the most significant evidences of imbalance. In his famous book J.M. Keynes analyzing dramatic experience of 1929-1933 Great Depression paid attention to this very type of a threat. He wrote: "Speculators may do no harm as bubbles on a steady stream of enterprise. But the position is serious when enterprise becomes the bubble on a whirlpool of speculation. When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill-done." (*J.M. Keynes*, p.159)

From the point of view of international trade at least two points should be emphasized. Firstly, different commodities traditionally circulating via international trade channels during previous decade were included by speculators in the domain of their operations that generated extreme volatility of respective commodity prices. According to recent report of UNCTAD, the number of futures and options contracts outstanding on commodity exchanges all over the world grew more than fivefold, while notional value of over-the-counter commodity derivatives increased

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more than 20-fold to \$ 13 trillion between 2002 and the mid-2008 (*The Global Economic Crisis*, p. 24-25).

Secondly, international trade nowadays is predominantly based upon activities of various financial middlemen. Their direct involvement measured by total value of foreign trade credits and insurance contracts accounted for 80%-90% of world export. Financial crisis seriously hit these operations. By the end of 2009 – beginning of 2010 estimated deficit of respective financial resources experienced by leading commercial banks equaled to \$ 25 billion monthly. (*M. Auboin*, p.10)

All this helps to understand why at least for last couple of decades volatility of foreign trade flows has substantially exceeded fluctuations of such macroeconomic indicators as GDP or industrial production. Both national and global statistical data illustrate the trend vividly enough. In particular, according to calculations of the WTO Secretariat "...world trade responds strongly to variations in global economic activity... Income elasticity – how much trade responds to change in income – has been between 1.5 and 2 over the last decade" (*WTO 2008*. p.2).

When the economy is on the rise above-mentioned dynamics logically enough tends to provide extra opportunities and to create additional incentives for the companies to expand their export and import operations. At the same time, for the periods of disturbances pendulum swings to an opposite direction. Already in case of mere deceleration of economic growth foreign trade can experience serious problems. It actually happened at the very beginning of a current millennium. Contraction of world GDP growth rate from 4.1% in 2000 down to 1.5% in 2001 was accompanied by respective contraction of world merchandise export growth from 10.7% down to -0.5%. (*WTO 2008*. p.3).

As for the time of real recession the situation appears to be even worse and more threatening. Current economic crisis provides a convincing proof of that. In 2009 international community experienced 2.2% reduction of world gross product (*United Nations*, p.2). As for world merchandise export, it contracted 12% in volume and 23% in value terms (*WTO 2010*). Under the circumstances it is not by chance that just after first evidences of global economic contraction world leaders at September 2008 G-20 summit clearly expressed both their common concerns on possible reduction of international trade flows and interest in avoiding of a new wave of protectionism.

Let's try to assess the scale and scope of influence the crisis might have on current state of Russian foreign trade as well as certain aspects of foreign trade developments' influence on the national economy.

2. Overview of recent developments in RF foreign trade

One might sensibly argue that foreign trade represents one of important spheres of Russian economy. For example, during last several years it generated on average more than 20% of total RF consolidated budget revenues. From global perspective Russia is among 20 major trading nations. Taking under consideration historical background, huge territory largely located in the

North, size of population, general level of economic development this ranking should not be underestimated. Table 1 shows that in relative terms being assessed by initial indicator of functional economic openness the country is ahead of USA as well as Brazil and India. Even in comparison with China the gap exists only if measured in current USD.

Table 1. Foreign trade quotas for selected countries in 2008
(%%)

| | Merchandise (X + M)/GDP(current USD) | Merchandise (X + M)/GDP(PPP USD) |
|---------|--------------------------------------|----------------------------------|
| Brazil | 24 | 19 |
| PRC | 66 | 32 |
| Germany | 73 | 91 |
| India | 39 | 14 |
| Japan | 32 | 36 |
| RF | 48 | 33 |
| USA | 24 | 24 |

Source: WTO 2009-b, pp. 26, 38, 68, 81, 89, 138, 177.

At the same time one should not totally ignore existence of different approaches. In particular, KOF Index of Globalization in its economic component puts Russia remarkably low. Table 2 provides relevant data.

Table 2. Russia in 2010 KOF Index of Globalization

| Globalization index* | | Economic globalization | | Social globalization | | Political globalization | |
|----------------------|----------------|------------------------|-------------|----------------------|-------------|-------------------------|-------------|
| Index** | Global rank*** | Index | Global rank | Index | Global rank | Index | Global rank |
| 68.91 | 42 | 58.0 | 98 | 68.82 | 39 | 85.38 | 42 |

Source: <http://globalization.kof.ethz.ch/>

*The overall index covers the economic, social and political dimensions of globalization. Overall index is calculated as an average with weight of economic component equaling to 38%, social – to 37%, political – to 25% of the total.

** The index is calculated on a scale of one to hundred, where hundred is the maximum value for a specific variable and one is the minimum value.

*** Rankings set among 208 countries are based on data for the year 2007.

In general, this means that perception of Russia economy as one with high level of economic openness might be challenged. In fact, this perception is mainly based upon functional openness (actual involvement of the country in various forms of international economic cooperation). In contrast to that KOF Index takes under consideration both functional and institutional openness. The later relates to existing restrictions on trade and capital mobility (various import barriers, mean tariff rates, taxes on international trade as a share of current revenue, etc.). Given a certain level of trade, a country with higher revenues from tariffs is less globalized.

All aforementioned should be taken under consideration while assessing changes of some basic Russian macroeconomic indicators during current crisis. Respective information presented in Table 3 suggests that the country similarly to many other national economies has experienced higher volatility of foreign trade in comparison with fluctuations of GDP or industrial production. It is interesting to note that number of unemployed increased dramatically. This contrasts to the

period of 1990s when labour market (at least according to the official statistics) appeared to be very rigid with respect to severe contraction of domestic production².

Table 3. Selected RF macroeconomic indicators in 2008-2009
(%% in comparison with the previous year)

| | 2008 | 2009 |
|--------------------------------|------|-------|
| GDP | 5.6 | -7.9 |
| Industrial production | 2.1 | -10.8 |
| Unemployment (end of the year) | -2.0 | +41.1 |
| Foreign trade turnover | 33.2 | -36.2 |
| RF-EU trade turnover | 35.1 | -38.3 |
| RF-China trade turnover | 38.7 | -29.4 |

Source: Rosstat, www.gks.ru

Several aspects should be mentioned for proper assessment of changes in Russian foreign trade turnover. In particular, implemented monetary policy hampered for economic agents (including direct participants of foreign trade) access to financial resources they drastically needed. During second half of 2008 (the period of constant contraction in both industrial production and foreign trade turnover) Bank of Russia (CBR) – directly in opposite to the pattern followed by its counterparts in overwhelming majority of developed countries in Europe, Asia, North America – gradually increased main refinancing rate starting from 10.75% up to 13% (www.gks.ru). Doing that Russia joined the company of Argentina, Brazil, Chili, Hungary, Iceland, Pakistan, and Serbia which made their choice in favour of “expensive money” policy³ (*UNCTAD 2009, p.27.*)

In addition to that one should not forget that Table 3 foreign trade data are calculated on the basis of actual current value of the contracts. In other words, the data have been strongly influenced by sharp contraction of world oil prices (crude oil accounted in 2009 for 33.3% of total RF export) during second half of 2008 – beginning of 2009. Table 4 depicts this contraction clearly enough.

Table 4. Actual export prices for Russian oil
(USD per ton)

| | |
|---------------|-------|
| July 2008 | 887.4 |
| December 2008 | 325.2 |
| January 2009 | 291.6 |
| April 2009 | 322.4 |
| August 2009 | 467.0 |
| December 2009 | 508.7 |

Source: Rosstat, www.gks.ru

Other commodity prices behaved similarly also contributing to deterioration of Russian export statistics. Under the circumstances it looks sensible to argue that in case of several commodity groups dramatic reduction of 2009 outward deliveries in a way balanced their previous year impressive expansion. The latter in its turn was largely supported by growing world prices. Table 5 vividly illustrates the point.

Table 5. Changes in value of RF exports

² This phenomenon deserves special analysis which would go far beyond both size and focus of a present paper.

³ It's worth noting that CBR aimed at keeping the process of devaluation carried out during the end of 2008 – beginning of 2009 under control and mostly succeeded. Starting from April 2009 main refinancing rate has been gradually reduced down to 8.25% in March 2010 (http://www.cbr.ru/print.asp?file=/statistics/credit_statistics/refinancing_rates.htm).

(in %% to previous year)

| | 2008 | 2009 |
|-----------------------------------|-------|-------|
| Total exports | 32.9 | -35. |
| Mineral products | 42.2 | -37.5 |
| Ferrous metals | 35.5 | -44.6 |
| Non-ferrous metals | -16.2 | -26.7 |
| Machines & transport units | 15.7 | -21.2 |
| Chemicals | 45.3 | -38.2 |
| Wood & pulp products | 7.0 | -27.0 |
| Food & Agricultural raw materials | 2.1 | 7.3 |

Source: Rosstat, www.gks.ru

Finally, with respect to Russian import exchange rate fluctuations played their role. On the one hand, they pushed statistical data down. The point is that payments in trade between RF and its main trading partner – EU are mainly made in euro. At the same time Russian foreign trade statistics is traditionally calculated in USD. During 2009 euro on average lost 5.2% of its value against USD (www.ecb.int). On the other hand, depreciation of RUR *vis-à-vis* USD and euro (respectively 21.7% and 17.5% for 2009 - www.cbr.ru) made imported goods less attractive for Russian consumers. Despite the fact that their real income in 2009 according to official statistics increased 1.9% in comparison with a previous year, overall demand for foreign goods and services contracted.

In terms of geographical composition of RF foreign trade current crisis didn't generate any dramatic changes. 2009 continued (with exception of Chinese export) same trends three major Russian trading partners already demonstrated previously. Table 6 presents relevant data.

Table 6. Share of major trading partners in RF foreign trade (%%)

| | 2005 | | 2006 | | 2007 | | 2008 | | 2009* | |
|-------------|------|------|------|------|------|------|------|------|-------|------|
| | X | M | X | M | X | M | X | M | X | M |
| Germany | 8.1 | 13.4 | 8.1 | 13.4 | 7.5 | 13.3 | 7.1 | 12.8 | 6.1 | 12.6 |
| Netherlands | 10.2 | 2.0 | 11.9 | 1.9 | 12.2 | 1.9 | 12.2 | 1.8 | 12.0 | 2.1 |
| PRC | 5.4 | 7.4 | 5.2 | 9.4 | 4.5 | 12.2 | 4.5 | 13.0 | 5.5 | 13.5 |

*- January-November 2009.

Source: Calculated on the basis of Rosstat, www.gks.ru

Fluctuations in reduction of Russian trade turnover with country's 15 main trading partners (see Table 7) around average -37.7% are relatively large (-22.8 in case of France, - 49.8% in case of Japan). At the same time no definite conclusion can be made regarding correlation between magnitude of foreign trade turnover and its contraction. Trade with France and China performed better than with the others. The former was supported by intensive political interaction. The latter resulted from the fact that PRC managed to secure in 2009 impressive economic growth.

Table 7. RF trade with major trading partners
(billion USD, %%)

| | Foreign trade turnover | 2009 in comparison with 2008 |
|--|------------------------|------------------------------|
| | | |

| | | |
|--|------|--------------|
| Germany | 39.9 | -40.6 |
| Netherlands | 39.8 | -35.5 |
| China | 39.5 | -29.4 |
| Italy | 32.9 | -37.8 |
| Belarus' | 23.4 | -31.2 |
| Ukraine | 22.9 | -42.5 |
| Turkey | 19.6 | -42.0 |
| USA | 18.4 | -32.2 |
| France | 17.2 | -22.8 |
| Poland | 16.7 | -38.7 |
| Japan | 14.5 | -49.8 |
| Finland | 13.1 | -41.4 |
| Kazakhstan | 12.8 | -34.8 |
| UK | 12.6 | -44.0 |
| R.Korea | 10.5 | -42.6 |
| Average for 15 largest trading partners | | -37,7 |

Source: Rosstat, www.gks.ru

3. Does foreign trade help to survive the crisis?

Taking all aforementioned under consideration it looks pretty sensible to ask this type of question. Due to complexity of the processes under review no straightforward answer is possible both globally and with respect to Russian economy in particular. Nevertheless, at least several aspects appear to be relevant. Let's start with some general results presented in Table 8.

Table 8. RF Foreign Trade in 2009

| | |
|--------------------------|-------|
| X bln. USD | 304.0 |
| M bln. USD | 191.9 |
| X-M bln. USD | 112.1 |
| X 2009/2008 in value %% | 64.5 |
| X 2009/2008 in volume %% | 97.0 |
| M 2009/2008 in value %% | 65.7 |
| M 2009/2008 in volume %% | 63.3 |

Source: Rosstat, www.gks.ru

On the basis of these data one might first of all argue that in spite of certain pessimistic forecasts the country still has significant foreign trade surplus. *Paribus ceteris* it tends to support individual economic agents as well as total national economy providing additional financial resources to resist the crisis. In addition to that, relatively modest contraction in volume of export means that regardless of external shocks respective industries managed to maintain their production. By doing that they not only constituted some kind of "stability islands" but also, at least partially, disseminated stability impulses towards the rest of economic system.

On a flip side, Russia in comparison with many other global players experienced more dramatic reduction in trade value. In 2009 it has 13th rank among leading exporters and 17th one among leading importers, against 9th and 16th respective ranks in 2008 (*WTO 2010*). More than that, Table 6 clearly indicates that RF terms of trade deteriorated substantially. This development being normally perceived as something “bad” for national economy in time of crisis could generate additional negative effects. At last but not least, existing Russian foreign trade pattern so far failed to stimulate any serious positive changes in the level of RF oil & gas dependency. Under the circumstances prospects for the country’s quest for modernization and “innovation-based” economy look pretty problematic.

From the point of view of individual industries one might ask whether those of them more deeply involved in export operations are better equipped to resist current crisis comparing to mostly domestically oriented counterparts. Comparison of recent developments experienced by two enlarged industrial sectors extractive and processing ones - might provide some clue. The former contributes to RF export much more than the latter. Relevant data are presented in Table 9.

Table 9. Monthly changes in Russian industrial production
(%% in comparison with the previous month)

| Month | Total industrial output | Extraction of mineral resources | Processing industry |
|----------------|-------------------------|---------------------------------|---------------------|
| September 2008 | 101.4 | 98.3 | 102.0 |
| October 2008 | 102.8 | 99.7 | 100.4 |
| November 2008 | 89.2 | 94.2 | 84.7 |
| December 2008 | 103.8 | 102.3 | 101.6 |
| January 2009 | 80.1 | 97.0 | 67.3 |
| February 2009 | 106.4 | 91.3 | 119.7 |
| March 2009 | 111.1 | 111.6 | 114.7 |
| April 2009 | 91.9 | 97.1 | 91.9 |
| May 2009 | 97.9 | 102.1 | 100.7 |
| June 2009 | 104.5 | 99.9 | 109.9 |
| July 2009 | 104.7 | 105.0 | 104.9 |
| August 2009 | 97.0 | 99.2 | 95.7 |
| September 2009 | 105.1 | 101.2 | 106.0 |
| October 2009 | 100.8 | 102.9 | 95.7 |
| November 2009 | 102.0 | 96.7 | 101.9 |
| December 2009 | 105.0 | 102.3 | 103.2 |
| January 2010 | 79.6 | 97.2 | 73.1 |

| | | | |
|---------------|-------|------|-------|
| February 2010 | 104.8 | 92.7 | 108.3 |
|---------------|-------|------|-------|

Source: www.gks.ru

The Table 9 all in all covers 18 months. In terms of relative results of extracting and processing industries each of them surpassed “a rival” in 50% of cases (9 months). Nevertheless, at the annual basis 2009 index for extracting industry equalled to 98.8% in comparison with 84.0% for processing one.

There is yet another important trade-related aspect of aforementioned modernization prospects. It is well-known that in time of economic troubles various trade barriers have been frequently used as a tool to support domestic economy at the expense of foreign countries. Regardless of widely recognized long-term inefficiency of beggar-thy-neighbor policy and substantial risks directly associated with it, current crisis gave birth to a new wave of same attempts (See *United Nations 2010*, p.69).

Under the circumstances from a certain point of view with respect to available anti-crisis strategies both national authorities and business community face an alternative – either to focus on modernization or to rely upon protectionism. In case of the former relocation of resources, investments, innovations should ultimately result in higher competitiveness of domestic companies and their products. In case of the latter pressure put upon on the authorities by producers in addition to threatening developments of a labour market would generate extra trade barriers artificially enhancing competitiveness.

In parallel with famous approach proposed by Gary Becker (*G.Becker*, p. 169–217) with respect to economic analysis of crime one might argue that for representatives of business community decision to lobby distorting protectionist measures is a function of the costs and benefits of lobbying. The latter is economically rational if the following equation is valid:

$$(1 - p)b > pfu, (1)$$

where p – probability of a lobbying to fail;

b – utility of protectionists measures;

u – utility of modernization aiming to promote competitiveness;

fu – share of modernization utility lost as a result of protectionists measures.

Being perceived from the point of view of expenses situation looks differently. Certain group of manufacturers would lobby distorting protectionist measures in case it is cost-efficient in line with the following equation:

$$C(\text{lob.})$$

$$\text{-----} < C(\text{modern.}), (2)$$

$$P$$

where $C(\text{lob.})$ – costs of lobbying;

$C(\text{modern.})$ – costs of modernization aiming to promote competitiveness;

P – probability of lobbying to succeed.

Generally speaking the crisis *ceteris paribus* would reduce parameter “ p ” in equation (1) and increase parameter “ P ” in equation (2) giving certain components of protectionist policy extra chances to be implemented. Probability of this scenario appears to be higher for more functionally open economies and less institutionally open ones.

Scale and scope of international commitments also might play significant role. Director-General Pascal Lamy, at the Round Table Centre for Public Studies in Santiago on 15 April 2010 claiming that “the trade rules have stood to the protectionist pressures” (*Lamy cites “vital role” of trade*) most likely was right. From that perspective for Russia the WTO accession should ultimately mean growth of “p” in equation (1) or contraction of “P” in equation (2). In other words, relative utilities/costs of lobbying and modernization aiming to promote competitiveness change making the latter more attractive for business community.

4. Conclusion

The author by no means pretends to provide comprehensive analysis of current economic crisis’ impact on Russian foreign trade as well as foreign trade developments’ influence on national economy. Nevertheless, already at a current stage of investigation one might conclude the following:

- Foreign trade represents one of important spheres of Russian economy. Being assessed by initial indicator of functional economic openness the country is ahead of USA as well as Brazil and India. Even in comparison with China the gap exists only if measured in current USD.
- Similarly to many other national economies during current crisis RF has experienced higher volatility of foreign trade in comparison with fluctuations of GDP or industrial production.
- Several aspects should be taken under consideration for proper assessment of contraction in Russian foreign trade turnover. Namely they are: implemented monetary policy; sharp contraction of world oil and some other commodity prices; RUR, USD and euro exchange rates fluctuations.
- In terms of geographical composition of RF foreign trade current crisis didn’t generate any dramatic changes. 2009 continued (with exception of Chinese export) same trends three major Russian trading partners already demonstrated.
- Russia’s foreign trade performance in 2008-2009 exerted ambivalent influence upon national economy. On the one hand foreign trade surplus provided additional financial resources to resist the crisis, some exporting companies constituted a kind of “stability islands” disseminating stability impulses towards the rest of economic system. On the other hand RF terms of trade deteriorated substantially, existing foreign trade pattern failed either to stimulate any serious positive changes in the level of RF oil & gas dependency or support country’s quest for modernization and “innovation-based” model of development.

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