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Main Aspects of Regional Investment Climate Development in the Russian Federation

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Abstract

Significant regional differentiation by socioeconomic development levels is observed today, specifically, in terms of the volume of incoming investment determined by the investment attractiveness of a region.

Key-words: Investment Attractiveness, Investment Potential, Ranking Dynamics of The Russian Federation, Socioeconomic Development, Regional Investment Activity.

1. Introduction

Development of a favourable investment climate in Russia and across its regions relies on an optimal combination of mechanisms of market and government regulation to activate investment processes. The market mechanism is meant to create freedom of economic choice and action guided by the goals and objectives of the business structure. Government regulation serves to create a favourable environment for investment, so the main objective of government support for a favourable investment climate is to combine the advantages of government investment regulation and market advantages (Kurikov, Tashlanova: 2019b).

The problem set in this study is to work out and implement recommendations for developing the regional transportation sector in the Khanty-Mansi Autonomous Area — Yugra in line with socioeconomic sustainability principles and considering the planned diversification process in the region and economic prosperity for the population.

The goal of this study is to explore the aspects of the development of investment climate in Russian regions.

Objectives: 1) to analyse the key indicators of regional investment attractiveness; 2) to analyse the indicators of regional investment activity in Russia according to international rankings; 3) to explore the Russian system of investment climate practices.

Hypotheses: 1) investment attractiveness efforts require a stronger role of the government as the guarantor of a stable, predictable, and favourable legal regime of economic activities and a stronger role of regional authorities in addressing the regional investment attractiveness agenda; 2) the regions' standing in the ranking of investment attractiveness varies with time with economic crises.

2. Literature Review

The body of research focusing on the methodological aspects of territorial investment problems and setting up efficient investment management at the national, regional, and municipal levels comprises works by A. A. Smith, D. Ricardo, J. Keynes, J. Mill, P. Samuelson, A. Marshall, J. Schumpeter, J. Bailey, W. Sharpe, T. Alexander, J. Horne, R. Brealey, S. Myers, E. Brigham, F. Fabozzi, A. G. Granberg, B. M. Grinchel, E. A. Nazarova, A. A. Terentiev, and others.

Assessing and improving investment attractiveness of a regional economy is the topic of papers by I. V. Grishina, T. S. Kolmykova, A. A. Nikitin, T. E. Bragin, G. M. Drubetskaia, V. V. Avilova, V. M. Anshin, A. G. Babenko, E. V. Beliaev, V. V. Bocharov, N. Iu. Bryzgalova, N. Iu. Briukhovetskaia, O. B. Veretennikova, A. G. Giliarovskaia, M. G. Egorova, M. N. Kreinina, E. I. Krylov, V. A. Miliaev, V. A. Moskvin, N. N. Petukhova, N. V. Smirnov, L. S. Tishin, L. N. Chainikov, T. M. Smagliukova, V. M. Miakshin, O. V. Machulskaia, I. V. Bitkina, T. Rakhimov, A. Shakhnazarov, I. Roizman, V. Sekrekov, L. Gurieva, L. Semina, and others.

However, even with certain previous background research on territorial investment attractiveness, the theoretical and methodological foundations, socioeconomic development, and investment efforts diverge between regions and need to be adapted to meet the current developmental context of specific territorial entities. Further research should be concerned with ways to improve the investment attractiveness of a region based on the specific territorial profile and the development of specific steps to improve investment attractiveness. The acute nature and significance of these problems combined with the theoretical and methodological ambiguity and debate around potential solutions contributed to the choice of the topic and objectives of this study.

The review of background research on investment attractiveness, investment climate, and general economic growth suggests that investment processes in the country and specifically in the sectoral and spatial respect pour light on the overall state of the economy, on the one hand, and make it possible to conclude on the structural specifics of the economy, on the other.

3. Methods

Various tools and methods are used to analyse regional investment attractiveness. E. g., the techniques of comparative analysis of various scenarios of investment attractiveness have been actively developed. Such techniques help to identify priority industries for investment in different regions and eventually implement investment projects with the biggest potential return on invested capital with a moderate risk for investors.

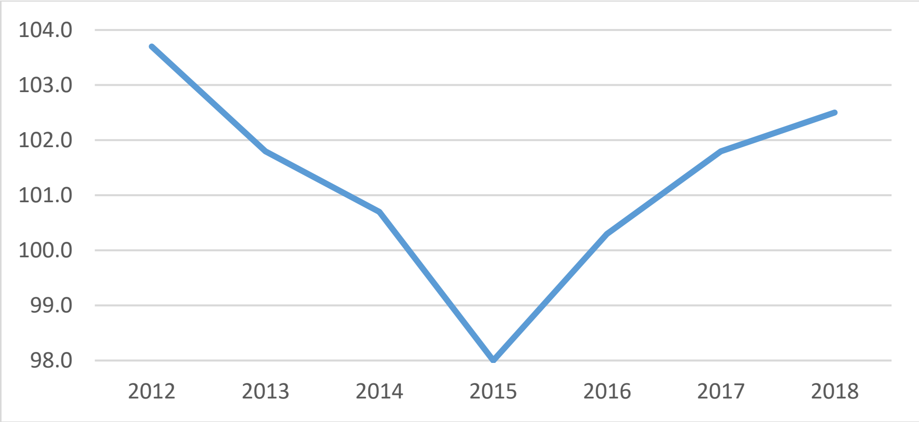
Meanwhile, existing methods of analysis and forecasting of investment attractiveness would not always provide investors with a reliable and comprehensive assessment of investment climate to inform an investment decision.

This setting creates the need for approaches to ensure a comprehensive integration of sectoral and territorial factors and their interaction. The combination of characteristics of investment attractiveness of a region should comprise sectoral assessments for certain most promising sectors and production spheres.

4. Results

GDP levels and growth are a key aspect of the analysis of economic development. According to the Institute of Economic Forecasting of the Russian Academy of Sciences (IEF RAS), the lower acceptable boundary of growth for the Russian economy is 2.5–3% in terms of annual GDP (Ivanter: 2013). The GDP trend for the period is shown in Fig. 1.

Figure 1 - Physical GDP index in Russia, % to the previous period [developed by the author]



This only constitutes growth rates sufficient to ensure simple reproduction of capital and absorption of losses caused by underinvestment during the previous periods. The lack of a significant increase of industrial production, tightening investment, and growing capital outflows from the country have brought to the foreground the only stabilising factor in the economy — the consumer sector helping to keep the Russian economy away from slipping into recession.

One of the reasons behind the declining indicators of economic growth is underinvestment in the economy. Fixed capital investment trends between 2012 and 2018 are shown in Table 1.

Table 1 - Analysis of fixed capital investment flows [developed by the author]

Year	2012	2013	2014	2015	2016	2017	2018
Investment, billion rubles	12,586.1	13.450.2	13,902.6	13,897.2	14,748.8	16,027.3	17,595.0
Growth rate (basis), %		106.87	110.46	110.42	117.18	127.34	139.80
Growth rate (chain), %		106.87	103.36	99.96	106.13	108.67	109.78

Fixed capital investment over the period also shows a mixed trend. In 2018 compared to 2012, fixed capital investment rose by 39.80%, which is a positive.

Experts point out that the economy is capable of growing at a pace of 6–7% per year over a long period. On average until 2030, economic growth can run at 5%. The rationale here is that there is room for quantitative and qualitative growth in modern Russia and there are no financial restrictions on the volume of investments. The first thesis is justified through the lens of domestic demand, and the second one reflects the high savings rate existing in the country.

Stronger growth in the Russian economy will require an increase in investment to support economic modernisation and structural transformation. Academician A. G. Aganbegian estimates that the investment ratio in the GDP including housing and municipal construction should rise to 40%, which is in line with the track record of countries demonstrating high growth rates in different periods.

According to experts, economic policies in Russia now should be primarily concerned with the rapid growth of fixed (non-cash) capital. Stronger economic growth would require structural transformations.

Fixed capital investment growth should occur on the back of new innovation-related business opportunities, stronger productivity, and the development of new competitive production operations. However, the idea of building a post-industrial economy faces much criticism given that the potential to implement it only exists in countries accumulating strong industrial capital and ensuring conditions for its ongoing renewal as the foundation to support service sector development.

Structural transformations require an environment in place to facilitate market-driven capital flows between sectors. There is no such mechanism in place today, which means Russia shows a much bigger share of domestic trade turnover in the GDP. In other words, Russian businesses largely invest in sectors providing fast turnover and fast payback despite the unfavourable condition of the industrial sector (Kurikov, Tashlanova: 2019a).

Accordingly, apart from resource regions, investors are also most interested in regions with big consumer markets, which means competition is diminished in peripheral ones.

In 2018, Russia held the ninth place among the 20 most attractive investment destinations in Europe. In 2019, Russia ranked 31st among the 190 countries in the Doing Business index, up four places from 2017. As recently as in 2012, the country held a place in the middle of the ranking. Global experts cite improving investment climate and simplified legalisation procedures, less red tape and inspections, and wider use of electronic documents and "one-stop-shop" services.

A study of spatial investment distribution shows that Russian regions are diverse in terms of investment levels. This fact reflects the differences in regional investment attractiveness and reflects the established economic structure. Rankings and statistics suggest that the investment climate in Russian regions is generally unfavourable, but varies significantly. This uneven profile indicates that alongside federal lawmakers and government bodies, the responsibility for investment climate is also borne by regional authorities, and practices of leading regions could be helpful for less successful regions.

Analyses of territorial attractiveness show that a plausible way to drive structural modernisation is to diminish the territorial polarisation by consolidating investment potential in laggard regions.

Accordingly, there is an apparent need for capital movements not only between sectors but between regions, as well. In this respect, all regions can be grouped as either investment donors or investment recipients. The former show faster growth and face fixed capital investment shortages, while the latter have unutilised investment resources and channel them to other destinations (Tashlanova, Bogomolova: 2017).

Rational distribution of investment flows between regions and mobility of capital within the country are the conditions of socioeconomic cohesion. It requires a spatial projection of the national investment strategy indicating which investment projects could be implemented in which regions and guiding in terms of the expected fiscal, business, and social effects. Investment policies should observe the condition of consistency and should not be limited to macroeconomic regulation; this means, active participation of regional and municipal authorities is needed, as well as engagement of business structures operating in the territory.

Today, to drive investment climate objectives, regions in Russia adopt the Performance Standard for government authorities developed by the Agency for Strategic Initiatives and the NGO Delovaya Rossiya (Business Russia). The main target reference is Russia's accession into the top 20 of the World Bank's Doing Business ranking of countries by investment climate.

The core line of success is associated with raising innovation activity. Currently, Russian businesses' innovation activity is 3.7 times lower compared to the levels observed in Europe, China, or America. To change things, there needs to be a special focus on lawmaking, governance, and control efforts to shape a favourable investment climate. Such measures should be implemented by competent government agencies as direct or indirect government measures to influence the economy.

They should consider the principles of economic operation in a market economy to stimulate investment activity and subsequently economic growth (Romenskii, Kurikov: 2018).

The track record of investment climate-related efforts of regional governments indicates that this issue has become a priority.

Complex and aligned organisational transformations are now shaped along a sequence of investment climate management (Fig. 2), which creates a multi-level management system (federal, regional, and municipal levels) and a differentiation of tasks among government bodies in addressing investment climate problems (Kurikov, Porokhina: 2014). Such a multi-level support system for investment climate relies on mutual and synchronous interactions between levels. Disruptions in the government support mechanism at the federal level may send further destabilising impulses to the regional investment climate. Vice versa, a higher-level element of government support (federal mechanism) may consolidate stronger effects in the particular region. E. g., tax reliefs for certain businesses at the federal level can be coupled with additional regional efforts.

Figure 2 - Managerial decision-making process behind investment climate efforts [developed by the author]

National investment policies ⇨	Investment policies of the federal subject of the Russian Federation ⇨	Investment policies of the municipal entity ⇨	Investment policies of the company
⇩	⇩	⇩	⇩
Federal government bodies and developmental institutions	Government authorities of the federal subject	Local authorities	Company owners

Meanwhile, the current economic context further emphasises the role of the government as the guarantor of a predictable and favourable regulatory regime supporting the operation of local and foreign investors. It also highlights the power of regional authorities in addressing investment climate objectives in the regions. On the one hand, regional (in contrast to federal) authorities get closer to the specific setting in the region and have sufficient powers and resource capabilities. On the other, they appear at a distance from the direct influences of the managers and owners of local business structures (in contrast to the municipal level) (Kurikov, Sadykov: 2016).

The issue of investment climate was instituted as a separate direction bestowed on the Russian Ministry of Economic Development in 2010. In the following 9 years, a system of measures was developed and introduced at the national level to build investment climate institutions in the country (Table 2) and develop the regulatory framework (Table 3).

Table 2 - Development of investment climate institutions in Russia [developed by the author]

Year	Institution, purpose
2010	Investment ombudsman; out-of-court settlement support on projects of foreign investors
2010	Advisory council for foreign investment in Russia (new format); prompt resolution of issues arising for foreign investors in Russia and development of recommendations on business conditions in the Russian Federation
2011	Russian Direct Investment Fund (RDIF); ensuring maximum returns on capital invested by the Fund and co-investors
2011	Agency for Strategic Initiatives (ASI); assistance with administrative barriers and attracting co-funding for high-potential business and social and infrastructure projects
2011	Russian Agency for Export Credit and Investment Insurance (EXIAR)

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Table 3 - Development of regulatory framework on major aspects of investment climate [developed by the author]

Direction	Principal measures
Simplification of construction procedures	Time requirements and costs involved in obtaining construction permits for investors are diminished, etc.
Development of the business environment	Regional standards of developing business environment are developed, setting uniform rules of business support in federal subjects of the Russian Federation
Elimination of infrastructural constraints	Template utility connection agreements between users and power grid companies are adopted; supplier responsibility is established; negotiation burdens are eliminated on connections; connection costs in power grids are cut down; the procedure of mutual settlements is refined for power grid companies and businesses; application processing time limits are set within 30 days, etc.
Simplification of migration procedures	Application processing times on working permits and entry visas are cut down; the maximum validity periods are extended for visas and working permits; the resident status is available and income tax of 13% (instead of 30%) is applicable from the first day of work given an agreement in place; residential permits can be obtained under a simplified procedure, etc.
Improvement of customs administration	The Customs Union' Customs Code became effective on July 1, 2010. It sets forth the main regulations of customs administration which are elaborated further in Law "On customs regulation in the Russian Federation"
Tax stimulus	Tax burdens are relieved on certain categories of taxpayers and payrolls; taxation mechanism is refined in special taxation regimes and for certain types of taxes; specific measures of tax stimulation are offered for some types of innovation activities;

	tax administration is improved in several dimensions
Criminal law liberalisation	Some economic wrongdoings are decriminalised with lighter punishment; possibilities are cut down for exerting illegal pressures on businessmen through falsification of criminal cases
Relief of administrative barriers	Some economic objects are transferred from the license-based to the notification-based domain; online notification procedure is introduced; the number of licensed activity types is cut down; a restriction is introduced to limit inspections to not more than one in three years; inspections of small and medium businesses by control authorities are only allowed subject to the approval of the prosecutor's office; time allowed for inspections is limited; the Federal Service for Accreditation is established, etc.
Refinement of the corporate legal framework	The list of material facts subject to obligatory disclosure by the issuers of securities is expanded; the procedure of self-initiated audits is established
Establishment of performance criteria for top officials of federal government authorities	Performance criteria are proposed reflecting the attainment of qualitative and quantitative results in investment climate improvement
Cooperation with international developmental institutions	2011 was marked by a historical maximum level of EBRD funding provided for projects in Russia; the volume of investment in the industrial sector, commerce, and agriculture first outpaced the financial sector; a new strategy of cooperation between the World Bank and Russia was approved for the following five years
Facilitation of operations of the Russian Federation Government Commission for Humanitarian Aid	Engagement of international technical aid; the percentage of procurement of foreign equipment is brought down and almost fully substituted by local equipment

The efforts on the investment climate in Russia have followed several principal lines since 2011 (Table 4).

Table 4 - Change of Russia's standing in the Doing Business ranking [developed by the author]

Key conditions of business operations	Position in 2012	Position in 2019	Absolute change in ranking
starting a business	28	32	-4
dealing with construction permits	115	48	67
getting electricity	10	12	-2
registering property	12	12	0
getting credit	29	22	7
protecting minority investors	51	57	-6
paying taxes	52	53	-1
trading across borders	100	99	1
enforcing contracts	18	18	0
resolving insolvency (bankruptcy)	54	55	-1
Overall rank	120	31	89

An analysis of the ranking paints a mixed picture, as 50% of the items are trending negatively. However, Russia's overall rank rose by 89 points over the analysed period. Accordingly, Russia holds the 31st place in the global ranking of investment attractiveness.

At the moment, by the volume of capital exports, the value of foreign assets, and their growth rates, the Russian Federation has risen close to the levels of many developed countries and other BRICS. The net capital outflow from the country in the analysed period equaled billion dollars, which, particularly, reflects foreign investments made by Russian companies and weaker activity of investors given the overall uncertainty in the markets across the globe and the situation in Europe (Baranov et al.: 2018).

Experts of the Gaidar Institute for Economic Policy associate the unfavourable capital outflow trend with the following principal factors:

- lack of political and economic stability in the Russian Federation. Add to that the steadily deteriorating relations with other countries (USA, UK, etc.) supplying a considerable flow of investment. E. g., the situation of 2014 caused the biggest capital outflow to the tune of $150 billion;
- lack of trust in the Russian banking system after the banking crisis of 2008;
- relatively high inflation compared to other countries, contributing to the devaluation of invested capital (Kurikov, Bessonova: 2012).

The main consequences of big capital outflows are primarily associated with lower budget revenues in Russia. The lack of external investment combined with cash exports by Russian businessmen results in business closures, reduced tax revenues, rising unemployment, and, as a consequence, diminished budget spending on social needs.

An important institutional factor influencing the state and potential of the investment climate is Russia's accession to the World Trade Organisation (WTO) in 2012. The implementation of fundamental principles of this international organisation creates the conditions for developing a favourable investment climate both at the national and international level (Skufina et al.: 2018). The mere fact of Russia's accession to the WTO contributes to its investment attractiveness as it helps to consolidate trust in the country's economic policies among foreign investors. However, there is no spontaneous activation of investment activities, which rather depend on the national economic model and a combination of sociopolitical factors indispensable for ensuring a stronger investment attractiveness profile for the country (Oder of the Department of Economic Development of the Khanty-Mansi Autonomous Area: 2013).

Meanwhile, besides positive effects, the development and implementation of government support measures on investment climate brought new problems slowing down the planned processes. Specifically, the main two of them are associated with missed implementation timelines and negative attitudes of the business community to the regulatory drafts being developed.

Consequently, despite the active engagement of the government, the investment climate in Russia has yet to improve and investment flows to the Russian economy remain subdued and fall short of the growing requirements. The main problems remaining on top of the agenda for government authorities include the regulatory framework, specifically in construction, the energy sector, customs, and property registration; the court system; the system of accounting and reporting in the Russian Federation that hinders clear impact valuations on invested capital for investors; limited access to credit; administrative barriers and arbitrary local rule; shortage of skilled talent competent in investment and related areas (Samarina, Illarionova: 2015).

However, the most complicated problem is still territorial unevenness, which generates significant contradictions in the management system of investment attractiveness. On the one hand, there is the decentralisation of management in the economy, which contributes to the growing role and significance of regional authorities in investment climate efforts. On the other, the increasing investment unevenness between regions exacerbates the disproportions in economic development, which makes it difficult for the underperforming territories to independently set up their development strategies and address existing problems. It weakens adaptation mechanisms and leaves regional authorities dependent on the federal authorities. This creates the need to analyse the modern trends of the investment climate in various regions of Russia (Illarionova: 2014).

5. Conclusion

The analysis of Russian regions in terms of investment profile confirms the findings of multiple studies on the unevenness of spatial development and strong differentiation of regional socioeconomic conditions. This significantly influences the indicators of regional investment attractiveness and suggests the framework of management should not only be refined but differentiated as well.

Consequently, the problem of investment attractiveness can be only addressed with in-depth analysis of the situation in the regional socioeconomic development helping to determine the key factors driving investment processes and accordingly work out and implement managerial decisions to improve the framework of managing regional investment attractiveness and bringing it to a trajectory of sustainable development (Kurikov, Bessonova: 2018).

Based on the above, hypothesis No. 1 and hypothesis No. 2 are deemed confirmed.

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