

# Russia's Growing Middle Class in for a Scare

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A group of office workers, which largely comprise Russia's middle class.

Russia's middle class is about to go through the mill of a sharp economic slowdown.

The group that emerges in a few years will be more complex in structure and differentiated in income, but would remain a major fixture of the socioeconomic landscape as the country ambles toward a postindustrial economy, according to analysts polled by The Moscow Times.

The immediate impact of the economic turmoil on the consumer class will be cushioned by the fact that many of them are on the state's payroll, experts said.

The approaching economic downturn and the long-term global trends toward income diversification will see many of these downgraded in social status. But the economy has a strategic need for highly qualified — and hence well-paid — professionals, said Alexander Safonov, deputy principal at the Russian Presidential Academy of National Economy

and Public Administration in Moscow, or RANEPA.

The middle class is "here to stay, and there is no stopping their rise," Safonov said.

## **Russia Specific**

What exactly constitutes the Russian middle class has been a subject of a two-decade-long debate, with estimates ranging from 2 percent to 80 percent based on criteria used.

It is definitely not the same people as in the West: A Russian's average monthly wage was 29,900 rubles (\$860) in 2013, compared to \$4,300 in the U.S.

Still, the World Bank said last March that 60 percent of the Russian population belonged to middle class in 2010, up from 27 percent in 2001. This year, the bank classified Russia for the first time as a high-income economy.

Russians themselves are less optimistic — in poll held in April by headhunting agency Superjob.ru, 37 percent of respondents identified themselves as middle class. The nationwide poll covered 3,000 economically active respondents and did not give a margin of error.

Recent economic problems and policies, however, have raised concerns that the social group — the cornerstone of most developed economies — is in for a punishing period.

Russia's economic growth rate has plummeted from 4.3 percent in 2011 to 1.3 percent last year. Official forecasts for 2014 have been slashed repeatedly in recent months and now hover around 0.5 percent, while independent experts talk of zero growth.

The government has reacted by ramping up pressure on businesses. The powerful Investigative Committee is on track to regain the right to open probes into tax crimes — which entrepreneurs said will lead to a drastic increase in tax cases, including fabricated ones designed for extorting bribes. Meanwhile, the government has come up with an arsenal of policies designed to force businessmen with assets overseas to bring those assets back into the Russian jurisdiction — where they can pay more tax. A commercial property tax hit business last year, and social security payments for small businesses have been hiked to 30 percent from 14 percent in 2011.

At least 650,000 registered businessmen disappeared from the state roster in the first half of 2013 alone, according to business lobby group Delovaya Rossia, though experts noted many of those either were de facto defunct companies that their owners never bothered to formally close or continued operating without official registration.

Russia also faces economic sanctions from the West over its alleged support of separatist militants in eastern Ukraine and the annexation of the Crimean peninsula in March. Sanctions remain limited to specific individuals and companies for now, but Western leaders have threatened to expand them to whole sectors of the Russian economy, including the oil and gas industry, which accounts for more than 50 percent of Russia's budget revenues and feeds a vast class of well-paid state employees.

All of which means households are faced with shrinking income in 2014 and will continue to struggle in the next few years, said analyst Maxim Klyagin of investment firm Finam

Management.

Indicating consumer trends, car sales in Russia have slumped 4 percent year-on-year since the beginning of 2014, according to the Association of European Businesses. The real estate market is meanwhile grinding to a halt after a short upsurge earlier this year caused by anxious buyers looking to invest money in depreciation-proof assets in the face of geopolitical turmoil and the weakening ruble.

But no foreign retail and food chains — businesses that target primarily the middle class — planned to pull out of Russia in the long term, confirming that global companies had faith in the long-term perspectives of the country's economy, Klyagin said.

Turnover in Russia's retail sector stood at 23.6 trillion rubles (\$680 billion) in 2013, according to official statistics. More than 1,000 new stores were opened nationwide by foreign retailers last year, retail consultancy Magazin Magazinov reported in February.

"The [consumer] market will shrink in 2014, but ... business activity is going on, with new players emerging constantly," Klyagin said.

### **What Next?**

The current trends do not good for the economic well-being of the Russian population. But analysts interviewed by the Moscow Times unanimously said that the Russian middle class would weather the downturn without a serious thinning of the ranks.

People working in the private sector — particularly employees of globalized companies — face the highest risks as business activity slows and sanctions loom, said RANEPA's Safonov.

But in Russia's middle class, he said, such people are a minority — Safonov put the business-related middle class at 4.5 million and state-employed wealthy consumers at 14 million people. Russia's total population stands at 143 million, of which 75 million people are economically active, according to official figures.

Longer-term prospects may be more worrying for the state-employed segment of the middle class, with mass job cuts on the cards if the oil prices plummets the government has to cut expenditure, said Nikolai Kashcheyev, head of analysis at Promsvyazbank — "Some of these people are unproductive, lack experience and skills and may struggle finding good jobs outside the public sector."

But state employees will remain the backbone of the Russian middle class for a long time, analysts said. And even if this or any other sector of the middle class shrinks, global trends still favor this social group, even as it becomes more complex and more widely differentiated by income.

The middle class is the staple of both industrial and postindustrial economies, which need millions of skilled professionals who require relatively high salaries, and Russia is an industrial economy, said Safonov of RANEPA.

"The middle class is transforming and differentiating, but it will remain the most important social group in foreseeable future," he said.

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