Problems of attracting foreign direct investment into the regional economy

G MGaleeva1, E N Kadeeva2

1Kazan Federal University, 4, ButlerovaSt., Kazan, 420008, Russia
2Kazan State Technological University, 68, Karla MarksaAve., Kazan, 420015, Russia

E-mail: g.m.galeeva@mail.ru

Abstract. The article discusses topical issues of attracting foreign direct investment in the economy of the Republic of Tatarstan. The assessment of the factors affecting the investment attractiveness of Russian regions made it possible to determine the prospects for the implementation of projects with the participation of foreign investors. In conclusion, the authors highlight the successful practices of attracting foreign investment in the region's economy.

1. Introduction

Attracting foreign direct investment into the economy of the regions of the Volga Federal District has a significant impact on the economic indicators of their development. Let us emphasize the importance of foreign direct capital for the modernization and development of the regional economy of the Russian Federation. High-tech development of priority sectors of the region's economy contributes to an increase in the volume of production and services provided in the local market, which directly affects the rate of socio-economic development of Russian regions. The main factors in attracting foreign direct investment is access to markets and resources. The concentration of foreign capital only in certain regions and in certain industries restrains the development of the economy of other regions of Russia, primarily in which industry is not developed.

2. Materials and methods

The dynamics of attracting foreign direct investment in the economy of Russian regions is largely determined by macroeconomic factors. Thus, at the end of 2018, the Central Bank of Russia recorded the highest rate of outflow of foreign direct investment (FDI) from the capital of Russian companies in the entire history of statistical observations, amounting to $ 6.46 billion. The decrease in the inflow of foreign investment in Russia corresponds to the general global trend of reduction capital investments by 19% 1. Incentives for FDI inflows to Russia are diminishing due to the presence of political risks, including sanctions, in nature.

Table 1. Dynamics of foreign direct investment in the Russian economy, billion dollars

| Name of indicator               | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---------------------------------|------|------|------|------|------|------|
| Outbound Foreign Direct Investment | 86,5 | 57,1 | 22,1 | 22,3 | 36,8 | 31,9 |
During the economic crisis and its consequences, the actions of anti-Russian sanctions in the country by the Western countries and the United States, foreign investments in the Russian economy are undergoing a significant decline. The external oil shock that occurred in 2014–2016 and the recession in the Russian economy only exacerbated the overall situation with foreign investment in Russia. A similar situation occurred in 2020, therefore, forecasts of attracting foreign direct investment in the economy of Russian regions are pessimistic. Major investments of past years in industries such as power generation and communications have resulted in overcapacity in these industries. In other sectors of the economy (with the exception of extractive industries), the lingering problem of the “unfavorable investment climate” and the lack of capital inflows into them complicates the possibility of the Russian economy coming out of the current stagnation along the investment path. The outflow of foreign capital from the Russian Federation began back in 2014, when sanctions were imposed and many large foreign companies left the domestic market. In subsequent years, this trend only intensified, due to the fall in oil prices and the further deterioration of international relations.

According to Table 1, foreign direct investment in Russia in 2015 decreased by more than 3.5 times compared to the previous year. In 2014, investments of foreign investors in the Russian Federation exceeded $22.0 billion, and in 2015 they amounted to $4.8 billion, which was the lowest figure since 2002. In 2016, foreign investors invested $19 billion in the development of the Russian economy, which is 62% more than last year. At the same time, Russian investment abroad in 2015 reached its lowest level since 2005. Compared to the previous year, they fell more than 2.5 times - from 56.4 to 21.6 billion dollars.

At the same time, according to the data of the Bank of Russia, over the nine months of 2019, the volume of foreign direct investment in Russian companies increased fivefold. Such data, according to the agency "Prime", the regulator cited in the "Assessment of the balance of payments of the Russian Federation for the third quarter of 2019". At the same time, in the third quarter of 2019, an inflow of investments of $6.6 billion was recorded.

In value terms, according to the Central Bank of the Russian Federation, foreign direct investment in Russian companies in January-September this year rose to $21.8 billion compared to $4.4 billion in the same period last year. Already in the first quarter of 2019, foreign direct investment grew by 34% compared to the same period in 2018, from $7 billion to $10.2 billion. Obviously, the money did not come from the CIS countries, they account for only 24 million dollars. The main inflow was from non-CIS countries - 10.18 billion dollars. Germany accounted for 1.1 billion dollars; Cyprus - 1.5 billion; Luxembourg - 1.5 billion; Switzerland - 2.1 billion; the rest of the amounts were insignificant, China - 115 million dollars.

By the type of economic activity, investments were divided almost equally: 4.3 billion were received in manufacturing, and 5.1 billion in mining. Foreign investments were divided into two types: participation in the capital of Russian companies ($6.8 billion) and the purchase of debt instruments (mainly, these were loans from co-owners - $4.7 billion).

Analysis of the structure of foreign direct investment based on statistics from the Central Bank of the Russian Federation shows that most of them do not lead to an increase in fixed assets (see Table 2).

Of great importance in the analysis of investment processes in Russia is the statistics of accumulated FDI in the context of investor countries (see Table 3). The first 7 leading countries account for 75.7% of FDI stock in Russia, and all of these countries are used to varying degrees as offshore zones, namely, such offshores as Cyprus, Luxembourg, Bahamas, Bermuda, and the British Virgin Islands.
Table 2 The structure of foreign direct investment by types of operations in the Russian Federation, according to the balance of payments

| Years   | Total (2 + 7) (according to the balance of payments) | Total (banks + other sectors) | Equity participation | Capital change investments | Mergers and Acquisitions | Debt instruments (14 + 23) |
|---------|------------------------------------------------------|-------------------------------|----------------------|----------------------------|----------------------------|----------------------------|
|         | Total (3 + 6)                                       | Total (4 + 5)                 | Purchase / sale of new shares (shares, units) (11 + 18) | Reinvestment of income (12 + 21) | | |
| 2011    | 55 084                                              | 33 157                        | 36 907               | 15 634                     | 21 273                     | -3 750                     | 21 926                     |
|         | 100%                                                | 60%                           | 67%                  | 28%                        | 39%                        | -7%                        | 40%                        |
| 2012    | 50 588                                              | 23 510                        | 28 684               | 5 146                      | 23 538                     | -5 173                     | 27 078                     |
|         | 100%                                                | 46%                           | 57%                  | 10%                        | 47%                        | -10%                       | 54%                        |
| 2013    | 69 219                                              | 32 358                        | 33 060               | 11 373                     | 21 687                     | -703                       | 36 862                     |
|         | 100%                                                | 47%                           | 48%                  | 16%                        | 31%                        | -1%                        | 53%                        |
| 2014    | 22 031                                              | 23 099                        | 33 907               | 12 173                     | 21 734                     | -10 808                    | -1 068                     |
| 2015    | 6 853                                               | 10 719                        | 21 754               | 10 566                     | 11 188                     | -11 035                    | -3 866                     |
| 2016    | 32 539                                              | 35 715                        | 26 321               | 9 083                      | 17 238                     | 9 394                      | -3 176                     |
| 2017    | 28 557                                              | 26 601                        | 25 119               | 8 409                      | 16 710                     | 1 482                      | 1 956                      |
|         | 100%                                                | 93%                           | 94%                  | 33%                        | 67%                        | 6%                         | 7%                         |
| 2018    | 8 785                                               | 9 913                         | 21 708               | 5 141                      | 16 567                     | -11 795                    | -1 128                     |
| 3 кв.   | 25 915                                              | 19 141                        | 19 514               | 5 552                      | 13 962                     | -373                       | 6 773                      |

Table 3 Foreign direct investment in Russia (equity participation and debt instruments) from some countries (balance at the end of the year), billion dollars

| State from which received investments in the Russian Federation | 2013    | 2014    | 2015    | 2016    | 2017    | 2018    | 01.10.2019 |
|---------------------------------------------------------------|---------|---------|---------|---------|---------|---------|------------|
| Cyprus                                                        | 193,6   | 110,3   | 94,6    | 148,5   | 174,0   | 136,1   | 157,8      |
| Luxembourg                                                    | 42,9    | 39,4    | 41,1    | 44,7    | 54,2    | 49,5    | 41,7       |
| Netherlands                                                   | 64,5    | 53,3    | 40,4    | 47,6    | 45,7    | 49,9    | 57,8       |
| Ireland                                                       | 29,1    | 26,4    | 31,7    | 30,0    | 31,4    | 26,8    | 28,1       |
| Bahamas                                                       | 32      | 21      | 21,6    | 33,6    | 25,8    | 39,1    | 24,4       |
| Brit Virgin Islands                                           | 26,3    | 14,7    | 15,3    | 14,5    | 11,9    | 12,2    | 12,7       |
Thus, the main feature of the structure of foreign direct investment accumulated in the Russian Federation by investing country is the significant role of offshore investment. According to the information provided in the Table, by 01.10.2019, the leading investing countries in the Russian economy are Cyprus, Luxembourg, the Netherlands, Ireland, the Bahamas, British Virgin Islands, Bermuda and Germany. In total, by the end of the 3rd quarter of 2019, Russia had accumulated 550.2 billion US dollars of foreign direct investment, and the share of these countries in the total volume of accumulated foreign investment is 87%.

Next, it is necessary to analyze the distribution and dynamics of attracting foreign direct investment by federal districts.

Table 4 Dynamics of foreign direct investment in the Russian Federation by district, mln.

| District Name                          | 2016  | 2017  | 2018  | 01.10.2019 |
|----------------------------------------|-------|-------|-------|------------|
| The Russian Federation, including      | 477,670 | 529,644 | 497,366 | 550,209    |
| Central Federal District               | 46,250 | 45,905 | 40,035 | 46,545     |
| Northwestern Federal District          | 6,606  | 8,753  | 7,341  | 7,531      |
| Southern Federal District              | 696    | 806    | 475    | 524        |
| North Caucasian Federal District       | 17,116 | 15,210 | 13,724 | 12,185     |
| Volga Federal District                 | 46,576 | 59,589 | 57,863 | 72,328     |
| Ural federal district                  | 28,190 | 34,307 | 34,468 | 42,629     |
| Siberian Federal District              | 62,345 | 64,421 | 77,354 | 69,726     |
| Far Eastern Federal District           | -      | -      | -      | -          |

As can be seen from Table 4, foreign direct investment is distributed extremely unevenly across federal districts. There is a sharp polarization in the concentration of investments in the Central, Ural, Far Eastern and Northwestern Federal Districts. The shares of federal districts in the total volume of foreign direct investment are presented more clearly in Table 5.

Table 5 Share of federal districts in the total volume of direct foreign investments in the Russian Federation, %

| District Name                      | 2016 | 2017 | 2018 | 01.10.2019 |
|-----------------------------------|------|------|------|------------|
| The Russian Federation, including | 100% | 100% | 100% | 100%       |
including

| Region                          | 2015 | 2016 | 2017 | 2018 |
|---------------------------------|------|------|------|------|
| Central Federal District        | 56%  | 57%  | 53%  | 54%  |
| Northwestern Federal District   | 10%  | 9%   | 8%   | 8%   |
| Southern Federal District       | 1%   | 2%   | 1%   | 1%   |
| North Caucasian Federal District| 0%   | 0%   | 0%   | 0%   |
| Volga Federal District          | 4%   | 3%   | 3%   | 2%   |
| Ural federal district           | 10%  | 11%  | 12%  | 13%  |
| Siberian Federal District       | 6%   | 6%   | 7%   | 8%   |
|                                | 13%  | 12%  | 16%  | 13%  |

Thus, the regions of the Central Federal District account for more than half of the direct foreign investment in the Russian economy. This trend has continued over the past four years. The share of other federal districts remains practically unchanged. This indicates that the economic interests of foreign investors are concentrated mainly in the central part of Russia, the financial sector remains a priority, while there is a shortage of investments in the real sector of the economy of the Russian regions.

Based on the data of the Central Bank of the Russian Federation, we will illustrate the top 10 sectors of the economy to demonstrate the dynamics of attracted FDI in Russia by type of activity in 2015 and 2018. The most attractive for foreign direct investment in 2015 were wholesale and retail trade, manufacturing, finance and insurance, mining. These industries account for 80% of total FDI as of 2015. A high proportion of foreign direct investment in wholesale and retail trade was achieved thanks to the vigorous activity of international operators of retail chains (Auchan, IKEA, Metro, REWE). In recent years, the level of FDI inflows into the mining industry has been significantly influenced by the Federal Law of April 29, 2008, "On the procedure for foreign investment in business entities of strategic importance for ensuring the country's defense and state security", which limits the participation of foreign capital in the raw material industries. The share of manufacturing industries in the total volume of FDI was 23.9%. The interest of foreign investors in this industry is explained by the awareness of the prospects for its development, however, in the structure of processing industries, such activities as chemical, metallurgical production, production of oil products, coke, and nuclear materials are distinguished, which have an adverse effect on the environment. Investment in research and development has dropped significantly, from 3.4% in 2010 to 0.1% in 2015, and industries such as healthcare and education are not among Russia's priority sectors for foreign direct investment.

![Fig. 1. The structure of attracted foreign direct investment by type of economic activity for 2018](image-url)
As can be seen from Figure 1, in 2018, there were significant changes in the structure of foreign direct investment by type of activity. In particular, the share of the industry "mining" increased from 13 to 21%, the share of scientific and technical activities increased to 10%. The share of trade decreased significantly from 28% in 2015 to 16% in 2018.

3. Conclusion

The main investing country in the period under review, starting in 2013, was Cyprus. Moreover, the position of Cyprus as the main source of foreign direct investment in the Russian economy has significantly strengthened. So, according to the results of Q3. In 2019, 157.8 billion US dollars of direct investments were received from this offshore, which exceeded the indicator of 2015 by 1.6 times. According to experts, the bulk of these investments is capital of Russian origin. This situation is unfavorable, because Cyprus, combining UK legislation and local civil law, is included in the list of offshore zones. Therefore, such foreign investment is not a reliable indicator of the investment attractiveness of Russia, because as a result of unsatisfactory conditions for conducting economic activities, entrepreneurs register their organizations in offshore zones, from where they invest back in the Russian economy. The second, third and fourth places in terms of accumulated foreign investment in the Russian economy in 2019 were occupied by the Netherlands, Luxembourg and Bermuda, with a volume of 57.8; USD 41.7 and 35.4 billion, respectively. It should also be noted that these countries are actively used in the business schemes of Russian entrepreneurs. In particular, in these countries, special purpose companies are registered and parent companies are formed in order to carry out project financing, because they have transparent legislation and a favorable legal system. The Netherlands hosts the headquarters and production facilities of many multinational companies (Unilever, Campina, Heineken, RoyalDutch / Shell, RoyalPhilips, AkzoNobel, KPMG), which have invested in the Russian economy. In turn, the reasons for the close economic cooperation between Russia and Luxembourg were joint project cooperation in such types of economic activities as energy, metallurgy, automobile industry, finance, medicine and healthcare, new technologies, communications and informatization.

The dynamics of the volume of FDI stock in Russia in individual countries, which are not customarily classified as offshore, was multidirectional during the economic sanctions. The volume of stock of FDI from the United States in 2019 compared to 2013 decreased by 70%, while from China - by only 24%. One cannot fail to note the positive dynamics of attracting direct foreign investment from Germany, Switzerland, France, Great Britain and Finland. Thus, the share of these countries in the total volume of investments increased from 12% in 2013 to 18% in 2019. In general, the dynamics of FDI is influenced not only by anti-Russian sanctions, but also by the general problems of the regional economy.

It should be noted that most of all investments that come into the Russian economy from abroad are "Russian" in origin, despite the fact that they are officially considered foreign. About 90% of foreign investments attracted to the domestic economy are foreign loans and borrowings, which do not pursue for their own purposes the modernization of the economy and fixed assets of Russia. Only a small share of foreign resources is invested in fixed assets, most of it is allocated to the following areas of activity: reinvestment of previous loans and borrowings, the implementation of financial speculation, an increase in inventories, an expansion of working capital. Thus, we can conclude that the indicator “FDI attracted to the Russian economy” cannot be used as an assessment of the efficiency of the domestic economy.

References

[1] Vlasenko R. D., Stroganova A. V. Foreign direct investment as a factor in the growth of the Russian economy // Young scientist. - 2015. - No. 21.1. - S. 116-121.
[2] Ponomareva IV. Foreign investment in the Russian economy: dynamics, analysis, problems // Young scientist. - 2014. - No. 12. - S. 172-173.
[3] Operations by type of direct investment [Electronic resource] / CBR. - The official website of the
Central Bank of the Russian Federation. - URL: http://www.cbr.ru/statistics/?PrtId=svs
[4] IMF, CoordinatedDirectInvestmentSurvey [Electronic resource] / Official website of the IMF. - URL: http://cdis.imf.org
[5] Bank of Russia. Direct investments in the Russian Federation by partner countries in 2007–2015 (participation in capital, reinvestment of income and debt instruments) [Electronic resource] / CBR. - The official website of the Central Bank of the Russian Federation. - URL: http: www.cbr.ru/statistics/?PrtId=svs
[6] Yanyuk E.N., Yafizova A.I. Problems of attracting foreign investment in the Russian economy // Problems of Economics and Management. - 2015. - No. 2 (42) - P.144.
[7] Federal Law of April 29, 2008 No. 57-ФЗ “On the Procedure for the Implementation of Foreign Investments in Business Companies of Strategic Importance for Ensuring the Defense of the Country and the Preservation of the Country”
[9] Galeeva, G.M., Fazlieva, E.P., Mingazova, R.K., Zinurova, R.I. Innovation as a part of strategic management and enterprise competitiveness of petrochemical cluster // Social Sciences and Interdisciplinary Behavior - Proceedings of the 4th International Congress on Interdisciplinary Behavior and Social Science, ICIBSOS 2015. pp. 213-216
[10] M. E. Ivanov, G. M. Galeeva Diversification of sources of external financing the real economy in terms of institutional transformation // Journal of economics and economic education research. Volume 17, Special Issue 2. 2016. – p. 415-422.
[11] Galeeva G.M., Zinurova R.I. Technological modernization of industry // Social Sciences and Interdisciplinary Behavior: The 4th International Congress on Interdisciplinary Behavior and Social Science (ICIBSoS 2015), pp.217-221
[12] Sayfudinova N.Z, Safiullin M.R, Safiullin A.R, Modeling of economic system of the development of the russian federation system//Journal of Economics and Economic Education Research. - 2016. - Vol.17, Is.SpecialIssue2. - P.334-346.
[13] Mgaleeva, G. Modeling the process of attracting foreign investment in the Russian economy// Journal of Physics: Conference Series. - 2019. - 1391(1),012154
[14] Kiselev, S.V., Chernyavskaya, Y.S., Bardasova, E.V., Galeeva, G.M., Fazlieva, E.P., Krokhina, J.A. Assessment of electronic banking service’s impact on the economic parameters of the bank activity // International Journal of Environmental and Science Education. 11(14), pp. 7226-7235
[15] GaleevaGM,Aktasheva O A 2017 Forecasting the Dynamics of Foreign Direct Investment in the Russian Economy Astra Salvensis2137-149
[16] Galeeva G M., Fazlieva E P., Mingazova R Kh., Zinurova R I. 2016 Innovation as a part of strategic management and enterprise competitiveness petrochemical cluster Social Sciences and Interdisciplinary Behavior: The 4th International Congress on Interdisciplinary Behavior and Social Science 216-216
[17] Mgaleeva, G. Modeling the process of attracting foreign investment in the Russian economy. 2019. Journal of Physics: Conference Series 1391(1),012154.
[18] Mgaleeva, G., Zagladina, E.N., Kadeeva, E.N., Kadeeva, Z.K. Model for assessing the influence of factors on a country's competitiveness in the global economy. 2019. Journal of Physics: Conference Series 1391(1),012153.