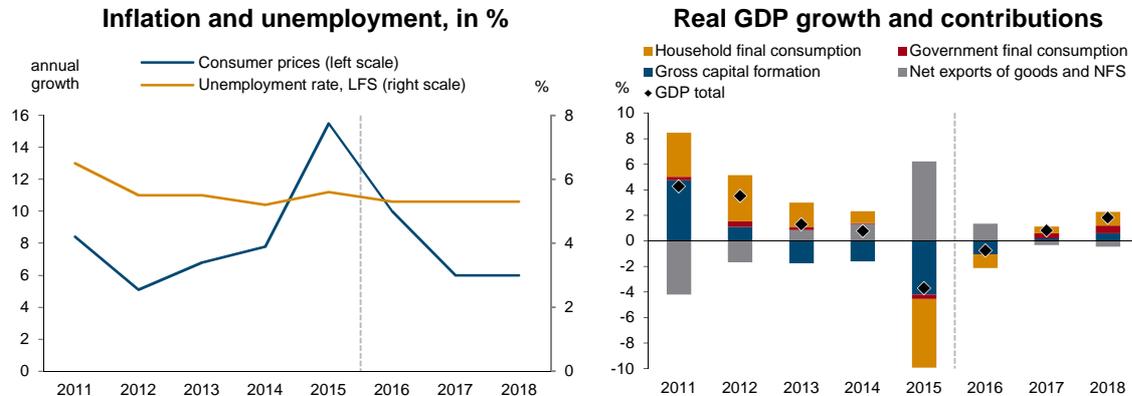


RUSSIAN FEDERATION: Recession not yet over

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Contrary to earlier expectations, the Russian economy will remain in recession in 2016. With oil prices having plunged anew at the beginning of 2016, export and budget revenues will drop. The envisaged cuts in expenditure will affect both consumption and investments; net exports will suffer as well. Barring additional external shocks, the economy may stabilise in 2017. Given the absence of reforms and investments, economic growth will remain sluggish – even in the medium term.

Figure 52 / Russian Federation: main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

The Russian economy plunged into recession in 2015. The combined effect of a prolonged reform stalemate, the collapse in oil prices and the subsequent devaluation of the rouble, as well as the imposition of Western sanctions and Russian counter-sanctions, has resulted in an unprecedented drop in Russian exports and – even more so – in imports.⁵⁵ Inflation shot up to double digits, the real effective exchange rate fell by 28% with respect to US dollar (and by 14% with respect to the euro) on annual average in 2015. Multiple shocks have hit domestic demand: real household consumption shrank by 10%, yet investments were cut even by 17% (inventories were sharply curtailed; gross fixed investments fell by ‘only’ 7.6%). The recession has not apparently affected the labour market so far; both employment and unemployment remain more or less flat and workers are sent on unpaid leave instead of being dismissed. However, the situation of migrant workers has markedly deteriorated. In addition to

⁵⁵ Both in nominal terms. Export volume (oil) increased by 3% and Russia suffered huge terms of trade losses.

heightened anti-migrant rhetoric and more restrictive registration rules, the economic crisis and rouble devaluation resulted in an exodus of migrants: while thousands have left for home, those who remain suffer severe income losses.⁵⁶

External shocks and related overall adjustments have been most spectacular in trade with the EU: already in 2014 EU exports to Russia had declined by 14% (German exports fell by 18%: all in current EUR terms). The trade decline accelerated dramatically in 2015 as the impact of collapsing oil prices, sanctions and the devaluation of the rouble struck home: preliminary data for 2015 indicate an additional huge drop not only in overall Russian exports (-19%), but especially in imports (-25%, again both in EUR terms).⁵⁷ Once again, trade with the EU suffered more than average: Russian imports from the EU fell by 35% in 2015, while those from Germany, Hungary, Poland and Slovakia dropped by close to 40%.⁵⁸

In addition, FDI inflows nearly dried out in the course of 2015 and FDI stocks were drastically reduced: inward FDI stocks fell by USD 186 billion (-33%), outward stocks by USD 100 billion (-20%) between January 2014 and July 2015. Simultaneously, the external debt was cut (by more than USD 200 billion during 2014-2015) as refinancing became more difficult due to the sanctions, and the outflow of capital diminished considerably last year. The reduction in FDI flows results from recession, the Western financial sanctions and the associated worsening of the investment climate; part of the disinvestment can also be attributed to the official 'de-offshorisation' campaign launched in 2014 and implemented since the beginning of 2015.⁵⁹

The year 2016 started with another plunge in the oil price and a complementary rouble devaluation. The Russian government, domestic and foreign think tanks and analysts reacted with another downward revision of economic forecasts. Scenarios which were considered pessimistic just a few months ago (based on an oil price below USD 40/bbl) represent now a baseline and the former crisis scenarios (with an oil price ranging between USD 20 and 30/bbl) have become more realistic. In either case, the bottoming-out of recession with subsequent stagnation in the course of 2016 – as was expected in wiiw's Autumn 2015 Forecast – will be delayed by at least one year. Moreover, the new external risks (Syria, the conflict with Turkey, further frictions with Ukraine, etc.) will lead to additional costs in terms of growth, investment and trade. The self-imposed ban on Turkish imports (food, textiles, construction and travel) will result in additional hardship for Russian consumers while prospects for import substitution from domestic or other sources are bleak due to the lack of investment resources and other bottlenecks – even in the medium term.⁶⁰

⁵⁶ The associated fall in remittances will have a severe impact on several countries, mainly Kyrgyzstan, Tajikistan, Uzbekistan, Moldova and Ukraine.

⁵⁷ Owing to EUR/USD fluctuations the decline in trade was more pronounced in USD terms.

⁵⁸ The number of imported passenger cars fell by half in 2015, imports of trucks by two thirds. Russia de facto stopped importing meat, fish, milk, fruits and vegetables from the EU. Export losses suffered by many EU countries are already close to the 'extreme' scenario elaborated in November 2014 (which reckoned with a 50% export drop).

⁵⁹ The lion's part of disinvestment was recorded vis-à-vis offshore tax havens (Cyprus: -USD 80 bn, British Virgin Islands: -USD 12 bn, Bermuda: -USD 14 bn, Bahamas: -USD 8bn, United Kingdom: - USD 12bn and USA: - USD 15 bn). For more details on the 'de-offshorisation' law, which has been in force since April 2015, see <http://www.step.org/russia%E2%80%99s-duma-passes-de-offshoring-bill>.

⁶⁰ Turkey accounted for 5.7% of Russian exports but just 2.2% of imports in 2015. Russian exports (mostly gas) are not (yet) affected by the conflict while import restrictions will have some (minor) adverse impact on Russian consumers, holiday makers and the construction industry.

Government anti-crisis plans for 2016 are largely pro-cyclical; budget expenditures will be cut by at least 10% and some taxes will increase. In February 2016, the Ministry of Economy elaborated its baseline GDP growth forecast (a drop by 0.8%) on the basis of an oil price of USD 40/bbl. It reckons with a deficit of the federal budget at 5.1% of GDP, a drop in investments by 6% and in real incomes by 4%. In a 'conservative' scenario (with an oil price of USD 25/bbl) there would be a higher budget deficit (6-7%) and a steeper fall in GDP. In both scenarios, the expected revenue shortfall should be partly offset by the imposition of new or higher taxes, additional privatisation revenues (RUB 1,000 billion), tapping the Reserve Fund (RUB 2,100 billion) and issuing new government debt (RUB 400 billion). Needless to say, each of these measures is controversial and will be subject to adjustments in the course of the forthcoming budgetary hearings in April.

In view of the new external shocks and the associated worsening of investment prospects, the revised wiiw forecast reckons with another fall of GDP in 2016 and stabilisation cum stagnation in the course of 2017 and thereafter. More than is usually the case, this baseline forecast is subject to significant downward risks, not only due to uncertain developments in the oil price and heightened geopolitical tensions. In alternative scenarios, the 2016 recession may be deeper and last longer. On the other hand, the recent alleged deal with Saudi Arabia to freeze oil production at the January 2016 level may push up the oil price and perhaps also prop up Russian economic growth. Nevertheless, there seems to be a consensus that Russia is facing a prolonged period of stagnation in both economic and societal developments. Turning inwards and continuing with more assertive policies is not helpful. Changing the pivot to China cannot substitute for trade with and investments from the EU, and the damaged links with most of the near neighbourhood both west and south (Ukraine and Turkey in particular) will be hard to restore. Moreover, even the Eurasian Economic Union flagship project has been adversely affected by these policies and other ill-considered unilateral steps on the part of Russia.

Table 21 / Russia: selected economic indicators

	2011	2012	2013	2014	2015 ¹⁾	2016	2017 Forecast	2018
Population, th pers., average	142,961	143,202	143,507	146,091	146,394	146,500	146,500	146,500
Gross domestic product, RUB bn, nom. ²⁾	55,967	66,927	71,055	77,893	80,413	87,000	93,000	100,000
annual change in % (real)	4.3	3.5	1.3	0.8	-3.7	-0.8	0.8	1.8
GDP/capita (EUR at exchange rate) ²⁾	9,600	11,700	11,700	10,500	8,100	7,700	7,700	7,800
GDP/capita (EUR at PPP) ²⁾	17,000	19,100	17,800	18,700	18,400	.	.	.
Consumption of households, RUB bn, nom. ²⁾	27,193	34,334	38,068	41,436	43,301	.	.	.
annual change in % (real)	6.8	7.4	3.7	1.7	-10.1	-2.0	1.0	2.0
Gross fixed capital form., RUB bn, nom. ²⁾	11,950	13,522	14,357	16,652	17,696	.	.	.
annual change in % (real)	9.1	6.0	0.9	-0.6	-7.6	-5.0	1.0	3.0
Gross industrial production ³⁾								
annual change in % (real)	5.0	3.4	0.4	1.7	-3.4	3.0	4.0	5.0
Gross agricultural production								
annual change in % (real)	23.0	-4.8	5.8	3.5	3.0	.	.	.
Construction output								
annual change in % (real)	5.1	2.5	0.1	-2.3	-7.0	.	.	.
Employed persons, LFS, th, average	70,857	71,545	71,391	71,524	72,324	72,500	73,000	73,500
annual change in %	1.3	1.0	-0.2	0.2	-0.4	0.2	0.7	0.7
Unemployed persons, LFS, th, average	4,922	4,131	4,138	3,889	4,264	4,100	4,100	4,100
Unemployment rate, LFS, in %, average	6.5	5.5	5.5	5.2	5.6	5.3	5.3	5.3
Reg. unemployment rate, in %, end of period ⁴⁾	1.7	1.4	1.2	1.2	1.2	.	.	.
Average monthly gross wages, RUB	23,369	26,629	29,792	32,495	33,925	36,200	39,500	44,000
annual change in % (real, gross)	2.8	8.4	4.8	1.2	-9.5	-3.0	3.0	5.0
Consumer prices, % p.a.	8.4	5.1	6.8	7.8	15.5	10.0	6.0	6.0
Producer prices in industry, % p.a. ⁵⁾	17.3	6.8	3.4	6.1	12.4	8.0	5.0	5.0
General government budget, nat. def., % of GDP								
Revenues	37.3	34.5	34.4	34.4	32.9	30.0	33.0	35.0
Expenditures	35.7	34.1	35.6	35.4	36.4	35.0	36.0	38.0
Deficit (-) / surplus (+)	1.5	0.4	-1.2	-1.1	-3.5	-5.0	-3.0	-3.0
Public debt, nat. def., % of GDP ⁶⁾	9.0	9.3	9.8	10.8	10.8	14.0	15.0	15.0
Central bank policy rate, % p.a., end of period ⁷⁾	8.00	8.25	5.50	17.00	11.00	8.0	6.0	5.0
Current account, EUR mn ⁸⁾	69,855	55,452	26,197	44,171	59,174	54,200	48,200	55,300
Current account, % of GDP ⁸⁾	5.1	3.3	1.6	2.9	5.0	4.8	4.2	4.9
Exports of goods, BOP, EUR mn ⁸⁾	370,131	410,300	393,911	376,284	305,404	293,300	309,800	338,800
annual change in %	25.0	10.9	-4.0	-4.5	-18.8	-4.0	5.6	9.4
Imports of goods, BOP, EUR mn ⁸⁾	228,764	261,202	256,951	232,852	174,465	167,500	178,700	191,800
annual change in %	23.5	14.2	-1.6	-9.4	-25.1	-4.0	6.7	7.3
Exports of services, BOP, EUR mn ⁸⁾	41,680	48,495	52,787	49,700	44,695	46,100	48,700	50,800
annual change in %	12.5	16.4	8.8	-5.8	-10.1	3.1	5.6	4.3
Imports of services, BOP, EUR mn ⁸⁾	65,706	84,736	96,643	91,487	78,060	81,300	85,900	87,900
annual change in %	15.8	29.0	14.1	-5.3	-14.7	4.2	5.7	2.3
FDI liabilities (inflow), EUR mn ⁸⁾	39,557	39,353	52,107	17,304	1,500	1,000	.	.
FDI assets (outflow), EUR mn ⁸⁾	48,008	37,980	65,120	42,630	15,000	10,000	.	.
Gross reserves of CB, excl. gold, EUR mn ⁹⁾	350,786	367,323	341,787	279,383	292,467	.	.	.
Gross external debt, EUR mn ⁸⁾	416,416	480,440	530,481	493,153	471,163	451,900	374,300	340,900
Gross external debt, % of GDP ⁸⁾	30.4	28.7	31.6	32.1	39.7	40.0	33.0	30.0
Exchange rate RUB/EUR, average	40.9	39.9	42.3	50.8	67.8	77.0	82.0	88.0
Purchasing power parity RUB/EUR ¹⁰⁾	23.0	24.4	27.8	28.6	29.8	.	.	.

Note: From 2014 including Crimean Federal District (for LFS and wages from 2015, growth rates for employment and real wages from 2016).

- 1) Preliminary and wiiw estimates. - 2) From 2012 according to SNA'08. - 3) Excluding small enterprises. - 4) In % of labour force (LFS). - 5) Domestic output prices. - 6) wiiw estimate. - 7) From 2013 one-week repo rate, refinancing rate before. - 8) Converted from USD. - 9) Including part of resources of the Reserve Fund and the National Wealth Fund of the Russian Federation. - 10) wiiw estimates based on the 2011 International Comparison Project benchmark.

Source: wiiw Databases incorporating national statistics. Forecasts by wiiw.