

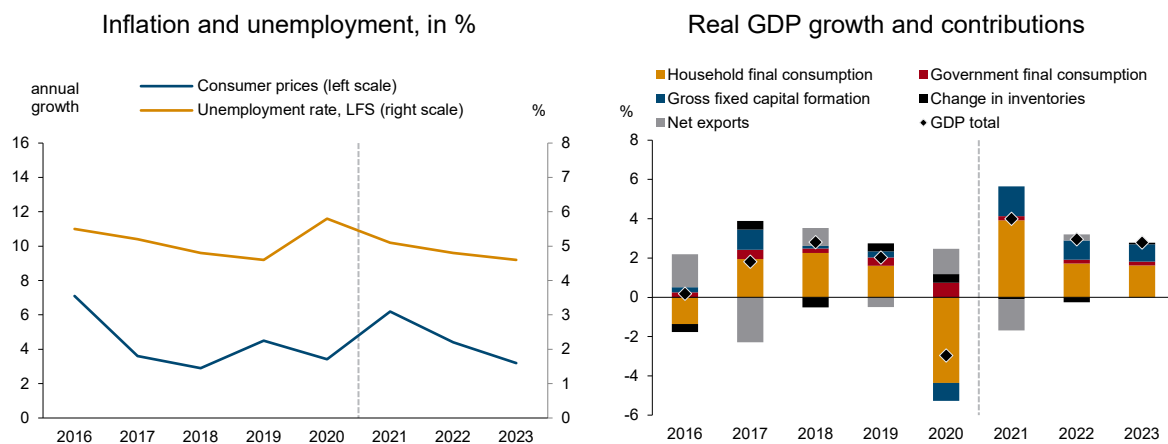


RUSSIA: Back to 'twin surpluses'

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Despite the persistently unfavourable COVID-19 situation, the economy has rebounded strongly and exceeded the pre-pandemic level in Q2 2021. But inflation has also accelerated markedly. In response, the policy interest rate has been hiked sharply, and more rises are likely to follow. Real GDP is projected to grow by 4% this year and by around 3% per year in 2022-23.

Figure 4.18 / Russia: Main macroeconomic indicators



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

Russia is on the brink of a fourth wave of the pandemic. This comes on top of the third wave, which started in June 2021 and has never really abated. Even prior to the fourth wave, the official statistics were recording around 800 COVID-related deaths and close to 20,000 new cases a day; on both counts, the situation has deteriorated further with the arrival of colder temperatures, bringing the daily number of deaths to nearly 1,000 at the time of writing. The true extent of the pandemic is likely much worse than the official data would suggest. As in many other CESEE countries, the rapid spread of the virus in Russia has been facilitated by the low inoculation rate (only 29% are fully vaccinated), which reflects primarily a low willingness to have the jab. Moreover, even if there were greater willingness, the inoculation rate would probably not increase all that much, given the vaccine production bottlenecks and problems with honouring export contracts.

On the face of it, the Russian economy has come through the COVID-19 pandemic relatively well. Last year, real GDP fell by only 3%, 1 percentage point (pp) of which was on account of the OPEC+ oil production cuts, rather than the pandemic itself. In Q1 2021, it still declined by 0.7% (year on year), but it surged by 10.5% in Q2. Although this is primarily explained by the low statistical basis (there were strict lockdowns in many Russian regions throughout much of spring 2020), it more than made up for the

slump in Q2 2019. As a result, real GDP in Q2 2021 was 1.9% higher than in Q2 2019, suggesting that the economic fallout from the pandemic has probably been left behind.

But this success is due in large part to policies that have prioritised the economy over public health. In contrast to the first wave of the pandemic, restrictions from the second wave onwards have been very mild: strict lockdowns are no longer imposed, and even the existing restrictions are generally observed only half-heartedly. These policies have also allowed the government to keep the fiscal stimulus to a bare minimum. Besides, this year has brought about a dramatic turnaround in the general government balance. While the recovery and surging energy prices boosted revenues by 21% in the first half of the year, expenditures picked up by only 8%, translating into a fiscal surplus of 2.4% of GDP. This is in stark contrast to most other CESEE countries, where budgets have remained in the red, despite the recovery.

The recovery has been driven exclusively by domestic demand. In the first half of 2021, private consumption surged by 11%, bringing it to pre-pandemic levels. The strong growth in consumption was fuelled by improved consumer sentiment, the release of accumulated savings and rapid credit expansion. By August, the pace of credit expansion to households had accelerated to 24% year on year, giving rise to sustainability concerns, especially against the background of nearly stagnant real incomes. Continued restrictions on foreign travel have also strengthened domestic spending. Travel to some traditional destinations has been hampered by COVID-19, while recognition by the EU of the Russian vaccines is still pending. Gross fixed capital formation also performed strongly, growing by 7% and far outpacing the decline in the first half of last year.

Foreign trade has rebounded impressively in nominal terms, but has been a drag on real growth. In the first half of the year, merchandise exports and imports alike soared by 27-28% in US dollar terms, reflecting the recovery in the Russian and global economies and in global energy demand. More recently, import growth has slowed somewhat, contributing to a surge in the current account surplus: in January-August, it almost tripled on an annual basis, to USD 70bn. However, the high growth of nominal exports in the first half was entirely due to the price effect, reflecting the recovery in energy prices from last year's dip; meanwhile export volumes declined by 2.5%. In contrast, real imports surged by 12.4% in the first half (mostly on account of machinery, equipment and textiles), so that the contribution of real net exports to GDP growth turned negative (-3.2 pp).

Despite the recent signs of a growth slowdown, the forecast for 2021 has been revised upwards. High-frequency indicators suggest that the economic recovery has lost some of its momentum in recent months, with the effect of the low statistical basis gradually fading, the release of accumulated savings largely exhausted, and with unfavourable weather conditions (rains and floods) affecting the harvest. Still, on the strength of economic performance in Q2, our growth forecast for the whole year has been revised to 4% (from 3.5%), whereas for 2022-2023 we project a minor slowdown to around 3% per year.

Defying earlier predictions, annual inflation has been accelerating, and reached 7.4% in September. As in many parts of the world, it has been predominantly supply-side driven, fuelled by disruptions in supply chains, rising energy prices and specific factors in selected food product markets (such as poultry). Therefore, we view the current spike in inflation as largely transitory, requiring little monetary policy response. However, demand-side factors have increasingly played a role as well, prompting the central bank to tighten policy. Overall, the policy rate has been raised by 2.5 pp since the

start of the year, to 6.75% at the time of writing. With inflation hovering well above the central bank target (4%) and the real policy rate still around zero, further hikes are likely in the months to come. This will likely slow the pace of lending and suppress both inflation and economic growth next year and in 2023. For 2022-2023, we expect growth of around 3% per year, also on account of the fading statistical basis effect and the usual structural constraints (unfavourable business climate and low investment rate) again increasingly making their presence felt.

The parliamentary election in September 2021 preserved the constitutional majority of the ruling United Russia party. However, the Communist Party came a strong second, with 18.9% of the votes, according to the official results (and almost certainly far more in reality). This should come as no surprise, given the recent rise in poverty in the wake of the pandemic and the protracted stagnation in living standards over the past decade. Between 2014 and 2020, real disposable incomes declined by 11%; though they picked up by 1.7% in the first half of this year, that did little to reverse the trend. Depressed living standards may become a political problem for the authorities, potentially forcing them to switch to rather more socially oriented economic policies, above all fiscal policy. The latest government proposal to substantially increase state spending next year may well be the first sign of a forthcoming policy shift.

Table 4.18 / Russia: Selected economic indicators

	2018	2019	2020 ¹⁾	2020	2021	2021	2022	2023
				January-June			Forecast	
Population, th pers., average	146,831	146,765	146,460	146,640	146,017	145,850	145,800	145,800
Gross domestic product, RUB bn, nom.	103,862	109,242	106,967	48,419	57,624	122,400	131,900	140,500
annual change in % (real)	2.8	2.0	-3.0	-3.4	4.9	4.0	3.0	2.8
GDP/capita (EUR at PPP)	19,450	19,610	20,120
Consumption of households, RUB bn, nom.	51,884	55,448	52,425	24,399	29,113	.	.	.
annual change in % (real)	4.3	3.2	-8.6	-10.0	11.0	8.0	3.5	3.3
Gross fixed capital form., RUB bn, nom.	21,452	23,087	23,273	8,497	9,463	.	.	.
annual change in % (real)	0.6	1.5	-4.3	-4.1	7.0	7.0	4.5	4.0
Gross industrial production ²⁾								
annual change in % (real)	3.5	3.4	-2.2	-1.7	4.0	4.2	3.0	2.5
Gross agricultural production								
annual change in % (real)	-0.2	4.3	1.5	3.0	0.2	.	.	.
Construction output								
annual change in % (real)	6.3	2.1	0.1	-1.2	6.4	.	.	.
Employed persons, LFS, th, average	72,532	71,933	70,601	70,700	71,169	71,310	71,310	71,310
annual change in %	0.3	-0.8	-1.9	-1.1	0.7	1.0	0.0	0.0
Unemployed persons, LFS, th, average	3,658	3,465	4,321	3,966	3,969	3,600	3,400	3,300
Unemployment rate, LFS, in %, average	4.8	4.6	5.8	5.4	5.3	5.1	4.8	4.6
Reg. unemployment rate, in %, eop ³⁾	0.9	0.9	3.7	3.7	1.6	.	.	.
Average monthly gross wages, RUB	43,724	47,867	51,344	49,509	54,587	56,700	61,000	64,500
annual change in % (real, gross)	8.5	4.8	3.8	4.3	4.2	4.0	3.0	2.5
Consumer prices, % p.a.	2.9	4.5	3.4	2.8	5.8	6.2	4.4	3.2
Producer prices in industry, % p.a. ⁴⁾	12.1	2.0	-3.8	-7.3	20.4	15.0	5.0	4.0
General governm.budget, nat.def., % of GDP								
Revenues	35.9	36.2	35.7	36.9	37.5	37.5	37.5	37.5
Expenditures	33.0	34.2	39.7	38.7	35.0	36.5	36.0	36.0
Deficit (-) / surplus (+)	2.9	1.9	-4.0	-1.8	2.4	1.0	1.5	1.5
General gov.gross debt, nat.def., % of GDP	12.1	12.4	17.7	13.8	16.7	15.5	12.5	10.0
Stock of loans of non-fin.private sector, % p.a.	13.9	6.5	12.4	8.9	17.4	.	.	.
Non-performing loans (NPL), in %, eop ⁵⁾	5.3	6.0	6.1	6.0	5.7	.	.	.
Central bank policy rate, % p.a., eop ⁶⁾	7.75	6.25	4.25	4.50	5.50	7.00	7.50	7.00
Current account, EUR m ⁷⁾	98,142	58,390	31,510	22,777	34,354	78,100	89,900	93,500
Current account, % of GDP	7.0	3.9	2.4	3.6	5.3	5.6	5.9	5.7
Exports of goods, BOP, EUR m ⁷⁾	376,612	374,738	291,760	144,983	172,777	372,900	412,100	432,700
annual change in %	20.5	-0.5	-22.1	-19.7	19.2	27.8	10.5	5.0
Imports of goods, BOP, EUR m ⁷⁾	211,127	226,668	209,726	99,607	116,880	253,900	279,200	293,200
annual change in %	0.0	7.4	-7.5	-4.0	17.3	21.1	10.0	5.0
Exports of services, BOP, EUR m ⁷⁾	54,845	55,275	41,165	21,399	19,719	41,900	43,900	46,100
annual change in %	7.6	0.8	-25.5	-17.5	-7.8	1.8	4.8	5.0
Imports of services, BOP, EUR m ⁷⁾	80,366	88,081	56,082	28,856	25,028	48,900	51,300	53,900
annual change in %	2.1	9.6	-36.3	-26.4	-13.3	-12.8	4.9	5.1
FDI liabilities, EUR m ⁷⁾	7,453	28,548	8,296	2,266	8,724	11,000	.	.
FDI assets, EUR m ⁷⁾	26,620	19,574	5,117	4,770	14,191	25,400	.	.
Gross reserves of CB excl. gold, EUR m ⁷⁾⁸⁾	333,617	396,378	372,318	389,476	387,293	.	.	.
Gross external debt, EUR m ⁷⁾	397,860	438,645	380,738	429,814	396,482	391,700	414,100	432,900
Gross external debt, % of GDP	28.3	29.1	29.3	33.1	28.3	28.0	27.0	26.5
Average exchange rate RUB/EUR	73.87	72.51	82.39	76.38	89.54	87.5	86.0	86.0

Note: Including Crimean Federal District.

1) Preliminary. - 2) Excluding small enterprises. - 3) In % of labour force (LFS). - 4) Domestic output prices. - 5) According to Russian Accounting Standards overdue debt is defined as debt service overdue, therefore the data are not fully comparable with other countries. - 6) One-week repo rate. - 7) Converted from USD. - 8) Including part of resources of the National Wealth Fund of the Russian Federation.

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