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Russian Federation: Consolidated yet unspectacular recovery

Having spent nearly one year in a deep recession, the Russian economy started to recover from the crisis in late 2009. The link between energy prices and the fortunes of the Russian economy comes to the fore in both boom and bust. With a time lag of about two months, stabilization and an economic upswing followed the recovery of oil prices (the latter climbed to over USD 70 per barrel in August 2009). The GDP ceased to fall in November 2009, industrial production, the volume of goods transport and export revenues started to grow in November 2009 on an annual basis as well. Yet domestic demand still remained depressed as both retail trade and particularly investments continued to contract even in the final months of last year. The recovery in the autumn notwithstanding, GDP fell by 7.9% in 2009 – mainly due to the sharp reduction of fixed investment and a sizeable reduction of inventories. Consumer expenditures declined by more than 5% despite a modest (+2.3%) increase in real money incomes implying an increase in savings. Foreign trade, with falling exports and sharply reduced imports (in both nominal and real terms), mitigated the overall economic decline: the real contribution of foreign trade to GDP growth was positive in 2009, after several ‘negative’ years. CPI inflation slowed down (producer prices and the GDP deflator even fell) and the unemployment rate rose by about 2 percentage points.

Most trend features of the above-mentioned developments remained unchanged in early 2010 as the oil price continued to be above USD 70 per barrel: modest growth of GDP (+3%, year on year, in the first quarter of 2010), a stronger upswing of industry (+5.8%), goods transport (+11.5%) and, above all, export revenues (+60%). Domestic demand remained subdued with retail trade turnover and real expenditures on goods and services as a proxy for household consumption expanding by just 1% in the first quarter (despite robust growth of real disposable incomes in the same period). Most importantly, investment continued to fall while the export surplus expanded rapidly as the growth of imports was moderate. Among the positive features one has to mention the stabilization of the unemployment rate below 9% and continued disinflation (measured by the CPI; producer price inflation accelerated). Last but not least, as a by-product of rising export revenues, the rouble has been appreciating again after a short-lived depreciation during the peak of the crisis at the turn of 2008-2009.

Unfortunately, the crisis has not been used as a stimulus for a radical overhaul of economic policies; restructuring and modernization have so far been just slogans (see below). The various anti-crisis measures announced and implemented from late 2008 onwards resembled the standard rescue and fiscal packages adopted in the West. A large part of the earlier ambitious investment plans was discarded and the budget was thoroughly revised. The aim was to improve the liquidity of the banking sector and restore confidence, to support the exchange rate and domestic consumption. The costs of the various anti-crisis measures may add up to 10% of GDP; judging by the sharp fall in consumption and in investment in particular, the effects of the adopted measures have been rather disappointing. The steep decline in investments indicates not only tightened credit, but also a deterioration of business confidence and the correction of the previous housing bubble. The share of investment (gross capital formation) fell to 20% of GDP in 2009 – a rather low figure compared to other transition countries and definitely insufficient for the urgently needed development of infrastructure and modernization of capital stocks.

From this perspective, the government's long-term strategic target of economic diversification and modernization remains high on the agenda, yet it is obviously getting out of reach. President Medvedev's priority modernization areas include energy, nuclear technologies, global information technologies and services, medical equipment and pharmaceuticals. These modernization fields are allegedly backed by specific implementation plans which also count on the participation of foreign companies and researchers. Indeed, as one of the recent foreign policy breakthroughs,¹ the latest (31 May to 1 June 2010) EU–Russia summit in Rostov on Don adopted a joint statement on the Partnership for Modernization with both parties pledging to encourage the sectoral dialogue and the implementation of specific joint projects. Accession to WTO (postponed once again in June 2009 on the pretext of forming a Customs Union with Belarus and Kazakhstan) was put back on the agenda again.

The recent foreign policy advances are instrumental in consolidating the earlier fragile signs of recovery which had been visible already from late summer 2009. These include a modest increase in output, rising export revenues (thanks to higher oil prices), the stabilization of inflation and a strengthening of the exchange rate. GDP growth resumed in the fourth quarter of last year, not least thanks to statistical base effects, with modest (up to 4.5% per year) growth acceleration possible in 2010-2012. The current forecast (a slight upward revision) is based on the assumption of stabilized oil prices (Urals costing around

¹ Other breakthroughs include the signing of a new START Treaty by presidents Obama and Medvedev in Prague, as well as marked improvements in the relations with Ukraine and Poland. Currently, Georgia (and, paradoxically, Belarus) remain almost the only sore point in Russian external relations.

USD 70-80 per barrel) and no abrupt policy changes or external shocks. Both private consumption and investment are expected to grow faster than GDP (the latter in 2010 largely thanks to the build-up of replenished inventories). Real exports will continue to be sluggish at best since the volumes of exported oil and gas will hardly increase, while imports will grow at a faster rate, fuelled by an appreciating rouble. This implies a small negative contribution of real net exports to GDP growth in 2010 and, in nominal terms, a gradual reduction of the trade and current account surpluses. The current account surplus, expected to peak in 2010, will drop below 3% of GDP by 2012. Annual CPI inflation may remain in single digits and the budget deficit will gradually turn into a surplus again. The employment effects of the crisis have so far been rather modest. They are being mitigated by demography as the domestic labour supply is shrinking. Our previous assessment remains unchanged: labour shortages are likely to reappear soon and will definitely put a brake on economic growth already in the medium run. Chances for a successful modernization and restructuring are meagre. Needless to say, another wave of the crisis cannot be ruled out either should growth in the world economy slow down again and/or energy prices fall.

Table RU

Russia: Selected Economic Indicators

	2006	2007	2008	2009 ¹⁾	2009	2010	2010	2011	2012
					1st quarter		Forecast		
Population, th pers., average ²⁾	142487	142115	141956	141902	141900	.	140000	139500	139000
Gross domestic product, RUB bn, nom.	26903.5	33258.1	41444.7	39063.6	8397.0	9862.0	43500	48500	53500
annual change in % (real)	7.7	8.1	5.6	-7.9	-9.4	2.9	4.0	4.2	4.4
GDP/capita (EUR at exchange rate)	5500	6700	8000	6200	.	.	.	.	.
GDP/capita (EUR at PPP - wiiw)	11100	12400	13200	12000	.	.	.	.	.
Consumption of households, RUB bn, nom.	12887.9	16006.8	20009.6	21084.4	4876.5	.	.	.	.
annual change in % (real)	11.4	13.9	10.8	-7.7	-2.6	.	4.5	5	4
Gross fixed capital form., RUB bn, nom.	4980.6	6984.0	9182.6	8387.5	1345.0	.	.	.	.
annual change in % (real)	18.0	21.1	10.4	-15.7	-16.2	.	-6	6	10
Gross industrial production									
annual change in % (real)	6.3	6.3	2.1	-10.8	-14.3	5.8	5	5	5
Gross agricultural production									
annual change in % (real)	3.6	3.4	10.8	1.2	2.3	3.6	.	.	.
Construction industry									
annual change in % (real)	18.1	18.2	12.8	-16.0	-19.2	-8.5	.	.	.
Employed persons - LFS, th, average	68855.0	70570.5	70965.1	69284.9	67760.0	68028.0	69000	69000	68700
annual change in %	1.0	2.5	0.6	-2.4	-2.5	0.4	-0.4	0	-0.4
Unemployed persons - LFS, th, average	5312.0	4589.0	4791.5	6372.8	7056.0	6436.0	6400	6000	6000
Unemployment rate - LFS, in %, average	7.2	6.1	6.3	8.4	9.4	8.6	8.5	8	8
Reg. unemployment rate, in %, end of period	2.3	2.0	2.0	2.9	2.9	3.0	.	.	.
Average gross monthly wages, RUB	10633.9	13593.4	17226.3	18785.0	17448.7	19371.0	.	.	.
annual change in % (real, gross)	13.3	17.0	10.3	-2.8	-0.8	2.2	.	.	.
Consumer prices, % p.a.	9.8	9.1	14.1	11.8	13.9	7.2	6.5	7	7
Producer prices in industry, % p.a. ³⁾	12.4	14.1	21.4	-7.2	-8.3	13.8	10	10	10
General governm.budget, nat.def., % GDP									
Revenues	39.5	40.2	38.6	34.8	36.1	35.1	.	.	.
Expenditures	31.1	34.2	33.8	41.1	33.4	32.7	.	.	.
Deficit (-) / surplus (+), % GDP	8.4	6.0	4.9	-6.3	2.7	2.5	-5	-3	0
Public debt, nat.def., in % of GDP ⁴⁾	8.6	6.7	5.7	8.3	6.2	7.2	10	10	10
Base rate of NB % p.a., end of per.	11.0	10.0	13.0	8.8	13.0	8.3	.	.	.
Current account, EUR mn ⁵⁾	75474	56818	70773	35224	7391	25034	50000	40000	35000
Current account in % of GDP	9.6	6.0	6.2	4.0	3.9	10.5	4.5	3.3	2.7
Exports of goods, BOP, EUR mn ⁵⁾	241960	258930	321793	218221	43779	67421	250000	260000	270000
annual growth rate in %	23.7	7.0	24.3	-32.2	-40.5	54.0	15	4	4
Imports of goods, BOP, EUR mn ⁵⁾	130948	163282	199148	137960	29420	33452	170000	190000	220000
annual growth rate in %	30.2	24.7	22.0	-30.7	-26.9	13.7	23	12	16
Exports of services, BOP, EUR mn ⁵⁾	24791	28681	34905	30010	6389	6572	35000	38000	42000
annual growth rate in %	23.8	15.7	21.7	-14.0	-7.1	2.9	17	9	11
Imports of services, BOP, EUR mn ⁵⁾	35643	42481	51495	44306	9364	9748	55000	65000	70000
annual growth rate in %	14.7	19.2	21.2	-14.0	-5.9	4.1	24	18	8
FDI inflow, EUR mn ⁵⁾	23675	40237	51490	27852	7214	.	35000	45000	50000
FDI outflow, EUR mn ⁵⁾	18454	33547	38273	33128	10414	.	35000	40000	45000
Gross reserves of NB, excl. gold, EUR mn	224306	318840	292483	290431	278624	313084	.	.	.
Gross external debt, EUR mn	237687	316893	339879	328733	351472	350344	.	.	.
Gross external debt in % of GDP	30.7	34.4	34.1	36.6	39.0	31.4	.	.	.
Average exchange rate RUB/EUR	34.11	35.01	36.43	44.14	44.46	41.41	39	40	41
Purchasing power parity RUB/EUR, wiiw ⁶⁾	16.99	18.88	22.19	23.04	.	.	.	.	.

1) Preliminary. - 2) Resident population. - 3) Domestic output prices. - 4) wiiw estimate. - 5) Converted from USD with the average exchange rate. - 6) wiiw estimates based on the 2005 International Comparison Project benchmark.

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