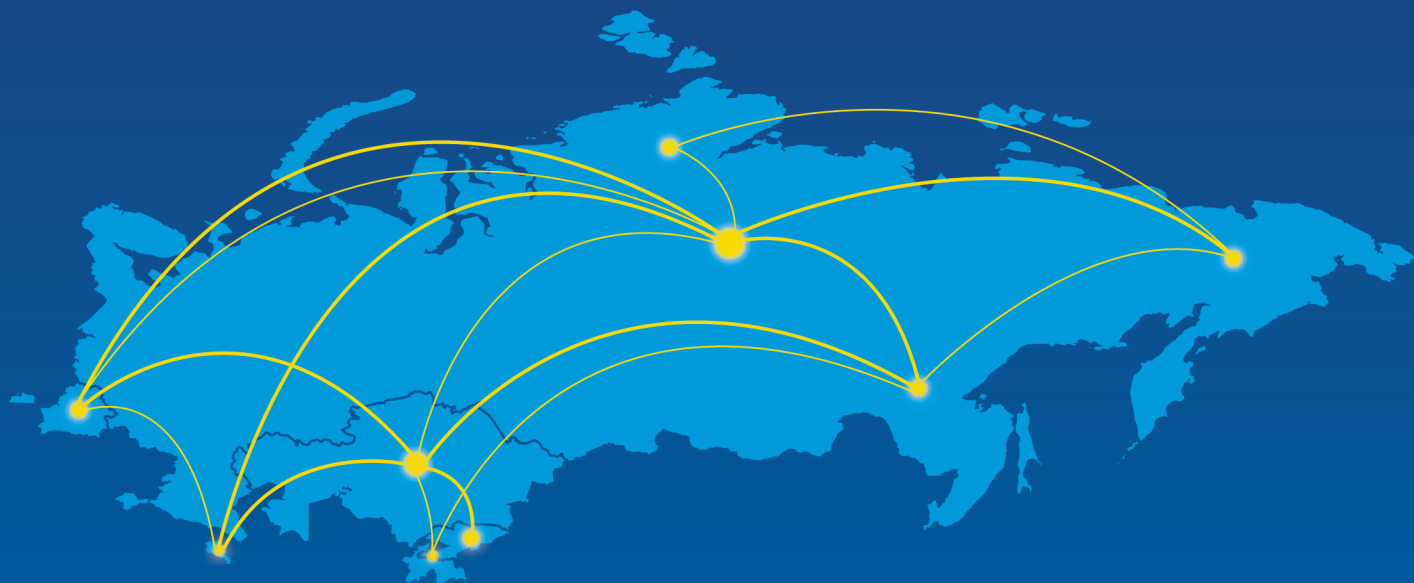


# EDB MACRO REVIEW



09'2020

**Russian Federation**



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# INFORMATION DISCLOSURE

This Review includes a detailed description of the current internal and external macroeconomic setting and an agreed set of forecasts that takes into account the interrelationships between the economies of the EDB operating region and the external sector.

The forecasts of the main macroeconomic indicators were prepared by the EDB jointly with the EEC using an integrated system of models based on a multi-country structural dynamic macroeconomic general equilibrium model. More detailed information about the structure of the integrated system of models, its main components, and its use for analysis of the macroeconomic situation and forecasting is contained in a joint EDB and EEC report entitled “Forecasting System for the Eurasian Economic Union”.

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# LIST OF ABBREVIATIONS

<b>BEA</b> — Bureau of Economic Analysis	<b>PCE</b> — Personal consumption expenditures inflation
<b>CDS</b> — Credit default swaps	<b>PMI</b> — Purchasing Managers' Index
<b>COVID-19</b> — Respiratory infection caused by the SARS-CoV-2 coronavirus	<b>pp</b> — percentage point
<b>CPI</b> — Consumer Price Index	<b>RF</b> — Russian Federation
<b>ECB</b> — European Central Bank	<b>RF CB</b> — Central Bank of the Russian Federation
<b>EDB</b> — Eurasian Development Bank	<b>RF MED</b> — Ministry of Economic Development of the Russian Federation
<b>EEC</b> — Eurasian Economic Commission	<b>RF MF</b> — Ministry of Finance of the Russian Federation
<b>EEU, Union</b> — Eurasian Economic Union	<b>Rosstat</b> — Federal State Statistics Service of the Russian Federation
<b>ENIA</b> — Euro Overnight Index Average	<b>U.S., USA</b> — United States of America
<b>EU</b> — European Union	<b>VAT</b> — Value Added Tax
<b>EURIBOR</b> — Euro Interbank Offered Rate	% — per cent
<b>FCS</b> — Federal Customs Service of the Russian Federation	<b>% YoY</b> — Year-on-Year growth rate
<b>FLBs</b> — Federal Loan Bonds	
<b>FRS</b> — U.S. Federal Reserve System	
<b>GDP</b> — Gross Domestic Product	
<b>h/h</b> — Household	
<b>IRA</b> — International reserve assets	
<b>ISM</b> — Integrated System of Models	
<b>LIBOR</b> — London Interbank Offered Rate	
<b>MIACR</b> — Moscow Interbank Actual Credit Rate	
<b>NFO</b> — Non-financial organization	
<b>OECD</b> — Organization for Economic Co-operation and Development	
<b>OPEC</b> — Organization of Petroleum Exporting Countries	

## SUMMARY

The Russian economy faced challenging external economic conditions in the first half of this year. The COVID-19 pandemic resulted in an unprecedented decline in global economic activity and volume of international trade. Lockdown restrictions considerably weakened consumer and investment demand and fostered a slowdown in inflation along with a fall in energy prices. These conditions compelled monetary regulators in both developed and developing countries to ease their monetary policy, while fiscal bodies unveiled large-scale anti-crisis packages to help the population and business.

June–July 2020 performance indicators communicated the beginning of a recovery in global economic activity amid an easing of lockdown restrictions and companies resuming work, primarily in the service sector. Due to differences in the epidemiological situation and government support amongst countries, this process has been gradual and varied. The EDB's base case assumes a slow recovery of the world's largest economies with unused capacity at production facilities in 2020–2022 to drive only moderate external demand for Russian exports in the medium term. Under such conditions, inflationary pressure from abroad will remain weak.

Oil prices were influenced by weakened global demand in the first half of the year and, therefore, were at reduced levels, while the OPEC+ agreement to reduce the extraction of raw materials reached in April was instrumental in limiting their fall. The EDB's projections assume that oil prices will grow moderately as global economic activity gets back on its feet.

The Russian economy contracted by 3.4% YoY in January–June 2020 in such circumstances. Among the key factors influencing economic trends were the domestic health restrictions, reduced external demand and difficulties with transportation, falling oil prices and production volumes under the OPEC+ agreements, increased uncertainty and a deterioration in business sentiment. These resulted in a significant reduction in consumption, investment and real income, as well as a rise in unemployment. The aftermath of the coronavirus pandemic is now mostly embodied in a cyclical economic recession, although potential GDP growth rates have also decreased. We believe that the negative output gap amounted to some 10–11% in 2Q2020.

According to the EDB's base case, the easing of lockdown measures in the second half of this year and support from expansionary monetary and fiscal policies will generate conditions fostering economic recovery. However, the process is going to be a slow one due to the increased uncertainty, social distancing, moderate external demand, weakened investment and depressed employment market; a return to the pre-crisis production levels is expected in 2021–2022, while the output gap will remain negative throughout the entire forecast period. The GDP contraction is estimated at 4.2% in 2020; its growth rate in 2021–2022 at about 3% on average per year.

In the first half of 2020, the Russian ruble weakened against the world's key currencies. The highest pressure was seen in the second half of March: the coronavirus outbreak grew into a pandemic, while the OPEC+ countries failed to reach an agreement regarding the extension of oil production restrictions. In May–June, the ruble regained some of the lost ground and traded at about 70 rubles per U.S. dollar, which was encouraged by the beginning of economic recovery at home and abroad, as well as by oil price growth. In the second half of August–early September 2020 pressure on the ruble grew due to increasing geopolitical risks; should these risks remain, the national currency is unlikely to strengthen by as much as its potential. The exchange rate is expected to adjust to an equilibrium level during 2021 as the coronavirus spread slows and geopolitical situation normalizes.

Consumer price growth rates somewhat increased in the first half of this year due to the exchange rate pass-through effect, temporary feverish demand for certain products and increases in prices of fruit and vegetables. We expect the inflation rate to grow to 3.9% YoY by the end of 2020, mainly through the low base effect of the previous year, which witnessed a significant slowdown in price growth. Restrained domestic and external consumer demand are expected to limit inflationary processes significantly in the medium term. Provided that exchange rates stabilize, the consumer prices growth rate will slow down to 3.5% YoY in 2021 and will commence a gradual recovery towards the Bank of Russia's target (4%), as disinflationary factors weaken.

Since inflation is quite likely to fall below the target in the medium term, it is imperative that domestic economic activity be supported; in light of this, the Bank of Russia lowered its key rate from 6.25% to 4.25%. We believe that the indicator has already been reduced almost as far as possible, and it will remain at 4–4.25% till the end of this year. The key rate is expected to increase gradually to the neutral level from the second half of 2021 onwards; however, monetary policy will be of a moderately stimulative nature in 2021–22.

The federal budget recorded a deficit of 1.7% of GDP in the first half of this year. Expenditures increased significantly, mainly due to anti-crisis economic support packages totaling some 4 trillion rubles (about 3.8% of GDP). Income fell in January–June 2020, primarily owing to the fall in hydrocarbon prices, their reduced extraction and exports, as well as reduced domestic economic activity. As a whole, fiscal policy was of a stimulative nature, thus limiting the scale of decline in production and demand. We expect a gradual weakening of the fiscal momentum as support for the economy decreases.

Heightened and negatively skewed risks to our forecasts remain, since the anticipated economic recovery is not of a stable nature, on the back of a potential second wave of the pandemic, increased tensions between the USA and China, and additional sanctions rhetoric regarding Russia.

# EXTERNAL CONDITIONS

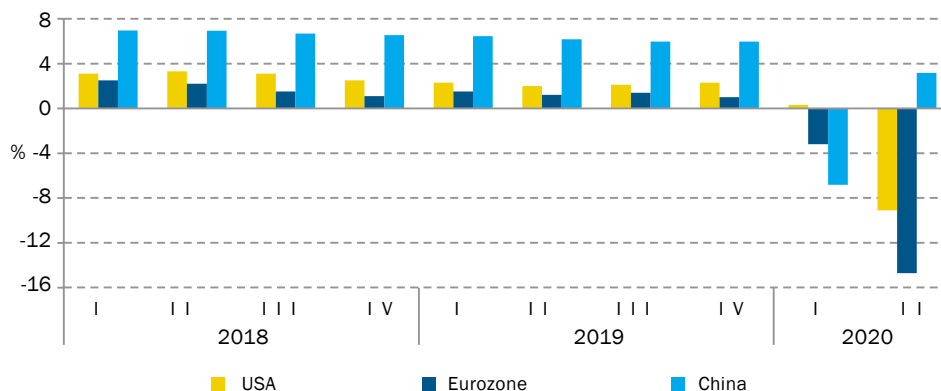
## Economic Activity

### Unprecedented decline in global economic activity

The first half of this year was marked by a huge challenge — the COVID-19 pandemic. As the disease spread, government bodies in the majority of countries responded by taking measures intended to contain it, which then led to a disruption in global supplies and increased volatility in the financial and commodity markets and exerted an overall negative impact on a great number of key economic sectors. Lockdown measures resulted in a reduction of consumer and investment activity, real and business incomes, and increased unemployment.

Among the world’s largest economies, the biggest decline in business activity in 2Q2020 was observed in the Eurozone, where GDP declined by 14.7% YoY<sup>1</sup> (down 3.2% YoY in January–March 2020), which is the highest drop since the indicator was first calculated in 1995. GDP of the USA decreased by 9.1% YoY<sup>2</sup> (0.3% growth in Q12020) over the same period, which had not been at this level since 1947. China’s GDP showed a positive trend in Q2: it increased by 3.2% YoY (down 6.8% YoY in January–March) upon the restrictions being eased in the spring.

**Figure 1.**  
GDP of the world’s largest economies (YoY)



Source: CEIC Data, BEA, Eurostat

<sup>1</sup> Seasonally adjusted data. As per our estimates, the year-on-year decrease compared to the previous quarter (seasonally adjusted) amounted to some 40%.

<sup>2</sup> Seasonally adjusted data. The year-on-year decrease compared to the previous quarter (seasonally adjusted) amounted to 31.7%.

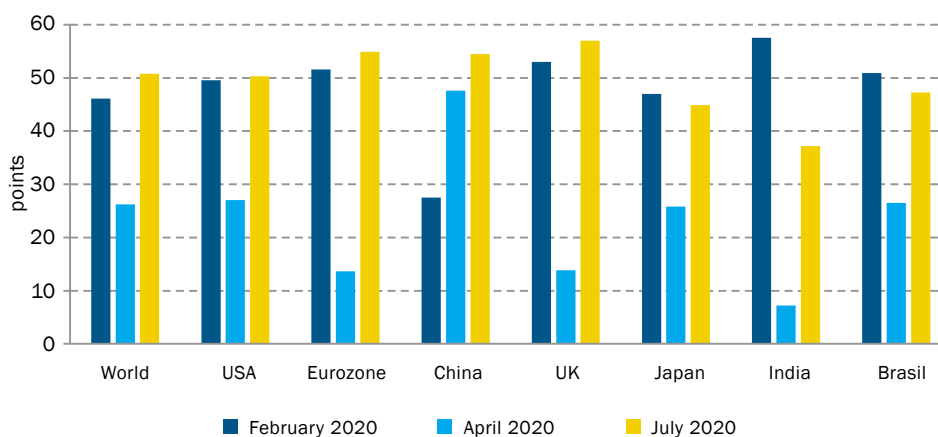
### Big losses in the service sector

In terms of industry, the largest losses were incurred by businesses providing consumer services. This follows from PMI survey results<sup>3</sup>, evidencing a significant decrease in business activity in the tourism and hotel industries, as well as in the transport and real estate sectors. A significant deterioration in business sentiment affected technology and financial firms, along with the telecommunications services segment. An output decline was also caused in the manufacturing industry, primarily in mechanical engineering and automobile production. There was a lesser impact of the pandemic on the food and pharmaceutical industries.

### Stabilization of the world economy at reduced levels in June–July

The maximum impact of the crisis (barring a second global wave of the disease or provided that its duration and consequences are not overly severe) is likely to have been passed in April–May, with the composite PMI at 26.2 (a record low) and 36.3 points, respectively. In June–July, the indicator increased to 47.7 and 50.8 points, respectively, which attests to a significant slowdown in the economic downturn after lockdown restrictions were eased. The composite PMI of the Eurozone reached 54.9 points in July (13.6 in April 2020), 50.3 in the U.S. (27 in April 2020), and 54.5 in China (27.5 in February 2020).

**Figure 2.**  
Composite PMI



**Source:** IHS Markit

Economic sentiment improved in June–July both in the service sector (real estate operations, banking products, telecommunications) and in the manufacturing industry (production of construction materials, automobiles, chemical products, etc.). There was a significant slowing in the decline of new orders volumes, including exports. However, the recovery in global

<sup>3</sup> PMI is an indicator describing changes in business activity and the operating conditions of private companies in the manufacturing and service industries. This indicator is based on monthly surveys of purchasing managers. A PMI index reading of over 50 points indicates an increase in economic activity, while readings below 50 indicate a decrease. For more information, please see: <https://www.markiteconomics.com/Public/Release/PressReleases>

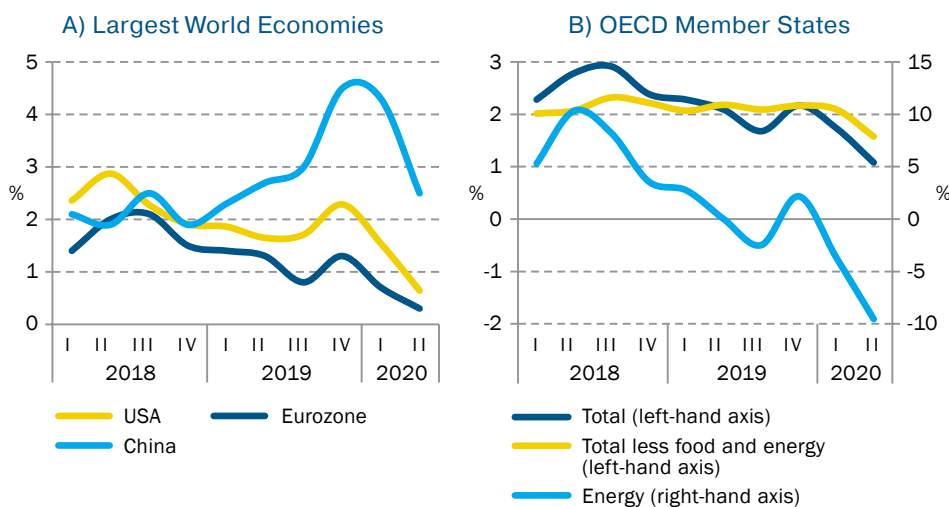
business activity is uneven due to differences in the epidemiological situation, and leading indicators overall signal the stabilization of global output at significantly lower levels than pre-crisis, which indicates the world economy is likely to be slow in returning to its “normal” state.

## Inflation

### Weak inflation background

The decline in global economic activity resulted in a slowdown in the world’s inflationary processes. Inflation in the OECD countries fell to 1.1% YoY in June from 2.2% in December 2019; in the U.S., it fell to 0.6% from 2.3%; in the Eurozone, it fell to 0.3% from 1.3%; and in China, it fell to 2.5% from 4.5%. The fall in energy costs due to decreased demand acted as an additional disinflationary factor. Accelerated food price growth had an impact on consumer prices despite their decrease in the international market, which might be driven by temporary difficulties relating to transportation and feverish demand for certain products in late March–early April.

**Figure 3.**  
**Foreign inflation**  
*(the last month in a quarter vs. the last month of the same quarter a year before)*



Source: OECD

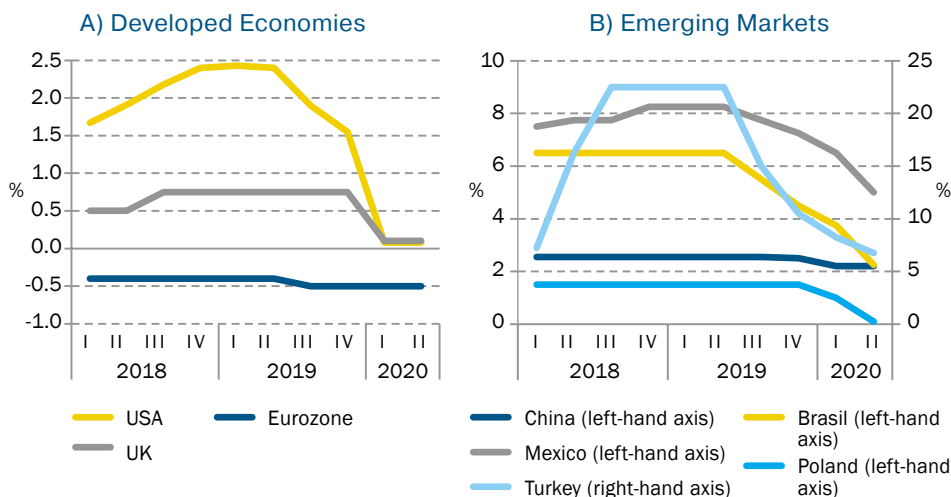
## Monetary and Fiscal Policy

### Easing of monetary policy

Active government measures taken to support the population, business and the financial sector were instrumental in limiting the scale of decline of the world’s largest economies. Monetary regulators eased monetary policy significantly in the first half of 2020 by lowering key interest rates and expanding asset purchase programs. In addition, top central banks

announced their intention to maintain a soft policy in the medium term. Monetary regulators in developing countries also lowered key rates, most actively in March–April 2020.

**Figure 4.**  
**Key interest rates of foreign countries**  
*(as at the end of period)*

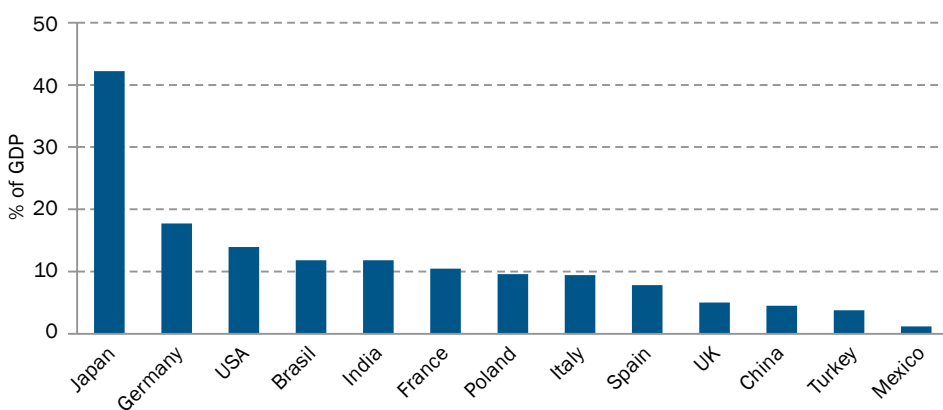


Source: CEIC Data

**Stimulative fiscal policy**

The volume of fiscal assistance was significantly expanded in the first half of 2020, since a need for anti-crisis measures arose, factoring in support for business and real incomes. According to the COVID-19 Economic Stimulus Index<sup>4</sup> as of August 25, the volume of fiscal stimulus in Japan amounted to 42.2% of GDP; in the U.S., 13.9% of GDP; in Germany, 17.7% of GDP; in France, 10.4% of GDP; in Italy, 9.4% of GDP; in the UK, 5% of GDP; and in China, 4.5% of GDP.

**Figure 5.**  
**Scope of fiscal support measures**



Source: COVID-19 Economic Stimulus Index

<sup>4</sup> For more information, see: Elgin C., Basbug G., Yalaman A. 2020. Economic Policy Responses to a Pandemic: Developing the Covid-19 Economic Stimulus Index. CEPR. Covid Economics, Vetted and Real-Time Papers. No 3. PP. 40–53.

## Commodity Markets

### Low oil prices

The prices of most key exchange-traded goods were driven largely by global demand and expectations of its recovery. After falling in March and April, prices for oil, metals and food began to recover in the face of a revival in economic activity. The OPEC+ agreement also had a positive impact on oil prices, providing for a large-scale reduction in raw materials extraction from May 2020. As a result, the price of Brent rose to USD 42.8 per barrel in July (Urals rose to USD 43.9) from a multi-year low of USD 23.3 in April (Urals: USD 18.2), but remained much lower than before the crisis.

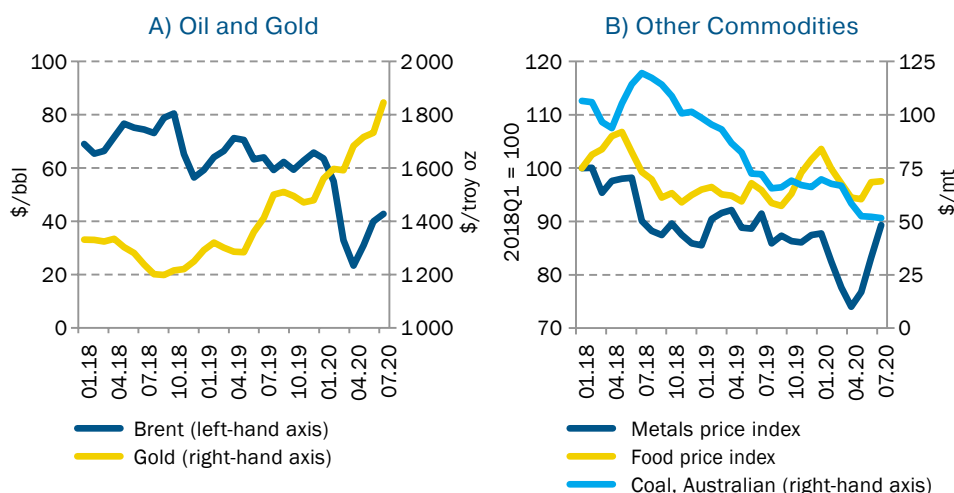
### Rapid recovery of metal prices

The metal price index increased by 20.7% in July versus the April minimum, and exceeded the level of December 2019. This was largely influenced by the revival of economic activity in China. The weakening of the U.S. dollar against key world currencies, as well as the risk of reduced supply of industrial metals, including copper, caused by the spread of coronavirus in Latin America, also affected the rapid growth of the indicator in June–July. The food price index showed a similar trend: after falling in April–May, there was a recovery in June–July. The market for potash fertilizers and coal remains just as weak in terms of prices.

### Increase in gold prices

Amid increasing global uncertainty in the first half of this year, there was a significant increase in demand for protective assets such as gold, with its prices reaching an all-time high in July 2020, being almost 25% higher than in last December. The soft policy maintained by major central banks furthered the increase, accompanied by large-scale injections of liquidity.

**Figure 6.**  
**Commodity prices**



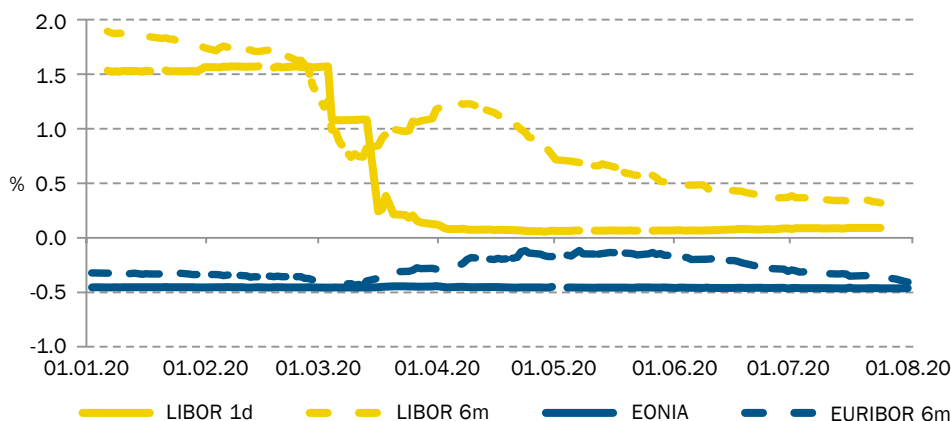
Source: World Bank

## Financial Markets

### Lowering of interbank market rates

LIBOR rates in U.S. dollars, as well as indicators of the Eurozone money market, decreased in 2Q2020 after monetary regulators opted to ease monetary policy. Central banks' efforts to maintain financial markets liquidity and somewhat improved business sentiment amid stabilizing economic activity were instrumental in reducing spreads between rates on one-day and longer interbank loans, which had returned to pre-crisis levels after an upsurge in March.

**Figure 7.**  
Money market rates in developed countries

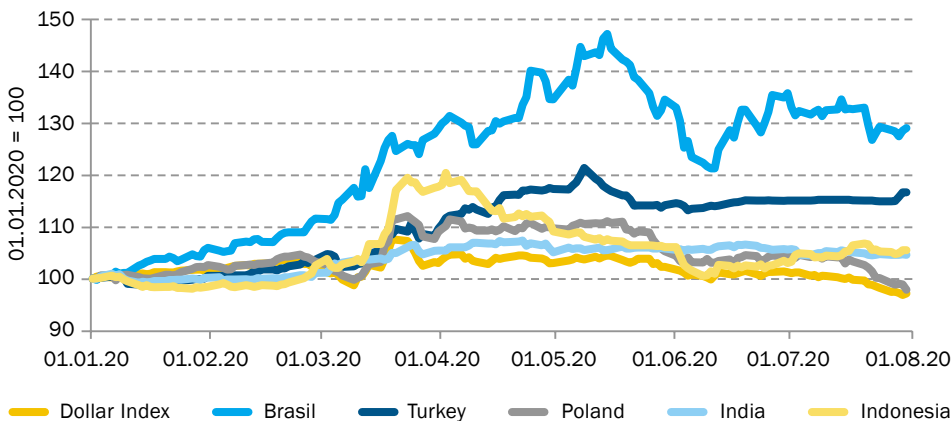


Source: CEIC Data

### Weakening of the U.S. dollar against the currencies of developed countries

The U.S. dollar exchange rate against key world currencies weakened markedly in June–July after strengthening in March–April, when investors were exiting from risky assets. The decline in the value of the U.S. currency was caused by a number of factors, including the FRS's statements about its intention to support an extremely soft monetary policy in the medium term, a still high rate of coronavirus disease spread in the USA, and the EU countries' agreement to issue common bonds in July.

**Figure 8.**  
Exchange rates against the U.S. dollar



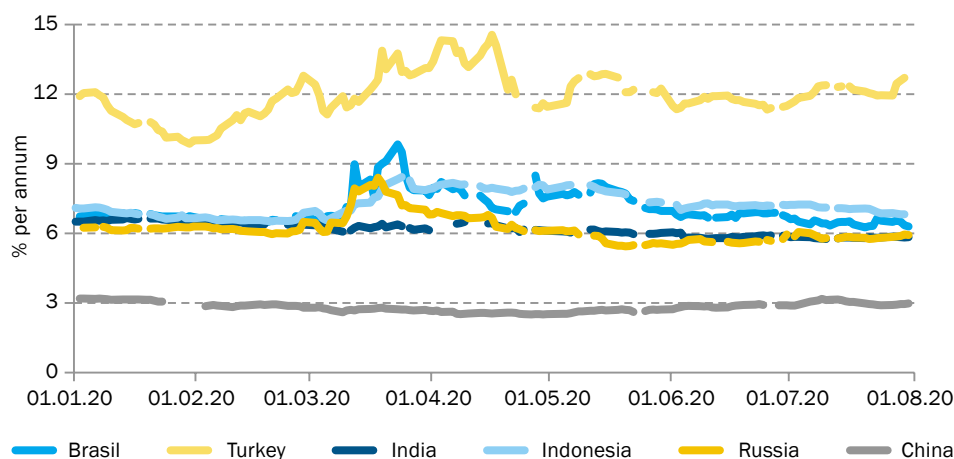
Source: CEIC Data, Investing.com

### Volatility in emerging market currencies

The currencies of emerging market countries regained in 2Q2020 some of the ground lost against the U.S. dollar in March, largely driven by signs of recovery in economic activity. In addition, these movements were largely corrective, since the currencies were oversold amid the March panic. However, exchange rates remain volatile. In the wake of new COVID-19 outbreaks in late June and July and a deterioration in China–United States relations, emerging market currencies were again pressurized by increased concerns about a second wave of the pandemic and a decrease in investor interest in risky assets.

The yield on long-term government bonds of emerging market countries decreased in April–July after a significant increase in March; it basically returned to the levels observed prior to the start of the pandemic, if not lower. Both the reduction in key interest rates of central banks and the beginning of recovery processes across economies played a crucial role in this.

**Figure 9.**  
Ten-year government bond profitability in emerging markets

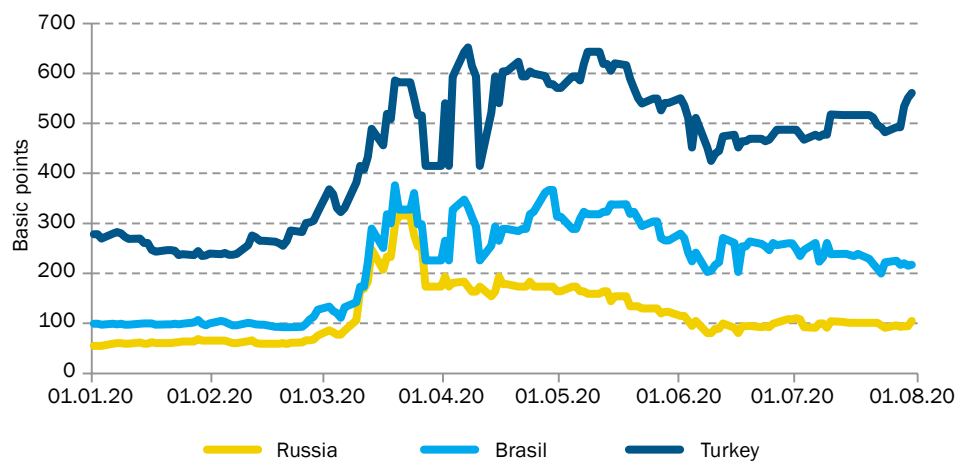


Source: Investing.com

### Risk premium has stabilized at a heightened level

Risk premiums for developing economies in 2Q2020 decreased against the highs of March–April, as indicated by the CDS trends. Nevertheless, their indicators stabilized in June–July, at levels higher than those before the crisis, which might be driven by the remaining high uncertainty about the global economic outlook. Country risk premiums will likely remain high until the spread of coronavirus slows in a sustained fashion.

**Figure 10.**  
**Five-year CDS in**  
**emerging markets**



**Source:** Investing.com

# STATE OF THE ECONOMY OF THE RUSSIAN FEDERATION

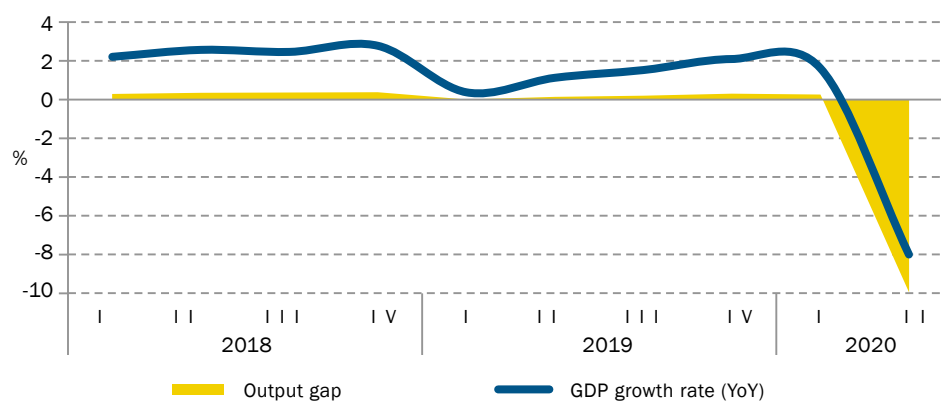
## Economic Activity

**Widespread decline in economic activity** In the first half of 2020, the economy of the Russian Federation took a big hit caused by the COVID-19 pandemic. The country's GDP decreased by 3.4% YoY in January–June 2020. The outbreak has affected economic activity in the country via two main channels.

- ← A deterioration in external economic conditions driven by lower demand for Russian exports, decreased budget and company incomes from sales of raw materials abroad due to falling prices and production volumes, the disruption of global value chains, and a deterioration in business sentiment.
- ← Health measures introduced in the country, primarily the declaration of non-working days from the end of March to mid-May 2020, resulted in consumer and investment demand shrinking on a large scale.

The biggest shock from the pandemic was felt in Q2, with output dropping by 8% YoY. We believe that the negative impact was mostly embodied in a cyclical decline, although the growth rate of potential GDP also decreased (according to the EDB's estimates: by 0.4–0.8pp versus pre-crisis indicators to reach 0.7–1% YoY) (*Box 1*). State fiscal, monetary and macroprudential support measures were instrumental in mitigating the negative economic and social impact of the worsening epidemiological situation.

**Figure 11.**  
**Economic Activity**



**Source:** Rosstat, calculations by the authors, EEC

## Box 1. Impact of the COVID-19 pandemic on Russia's potential and cyclical economic growth

The fallout from the COVID-19 pandemic may have a significant impact on trends in unobservable macroeconomic variables, such as potential GDP and the output gap. Whether monetary and fiscal policies will be effective is largely determined by several aspects: the correct identification of the state of the business cycle, the nature of monetary and fiscal policies, and the drivers of economic processes.

The EDB uses its ISM as the main tool for analyzing and forecasting the macroeconomic situation in the Bank's operating region<sup>5</sup>. The system uses semi-structural models with monetary and fiscal sectors that permit an assessment of non-observable variables.

The Bank has developed a semi-structural macroeconomic model (SSM)<sup>6</sup> in order to verify ISM-based findings for every operating region of the Bank. It is distinguished from the SSM mainly by the method of determining the equilibrium interest rate: the level (instead of the ISM-based uncovered interest rate parity) is linked to the growth of potential GDP, which is adjusted for the change in the real equilibrium effective exchange rate. This makes it possible to directly factor in how the impact of the production profit rate on the equilibrium rate, the impact of the economic convergence process and the return on foreign currency investments influence its movements.

The findings obtained showed that the COVID-19 pandemic resulted in an unprecedented cyclical downturn in the Russian economy: the negative output gap, which shows the deviation of actual real GDP from the equilibrium (potential) level, was some 10–11% in 2Q2020, the lowest in the last 15 years. This trend can be attributed to such key factors as the reduction in external demand and the effect of domestic restrictive measures aimed at containing the coronavirus disease. The influence of the latter on the decompositions shown (*Figure B.1*) is indicated in the contribution of other factors (demand shock). The fall in oil prices and reduction in energy raw materials production under the OPEC+ agreement (translating, like the health measures, into a demand shock) had a significant impact on the economic cycle. Easing the monetary conditions and fiscal policy was crucial in limiting the scale of the downturn in business activity.

The growth rate of potential output decreased by 0.4–0.8 pp to 0.7–1% YoY, which can be attributed to some enterprises closing down, to a decline in investment activity and increased uncertainty, as well as the impact of the OPEC+ agreements on limiting oil production. It should be noted that

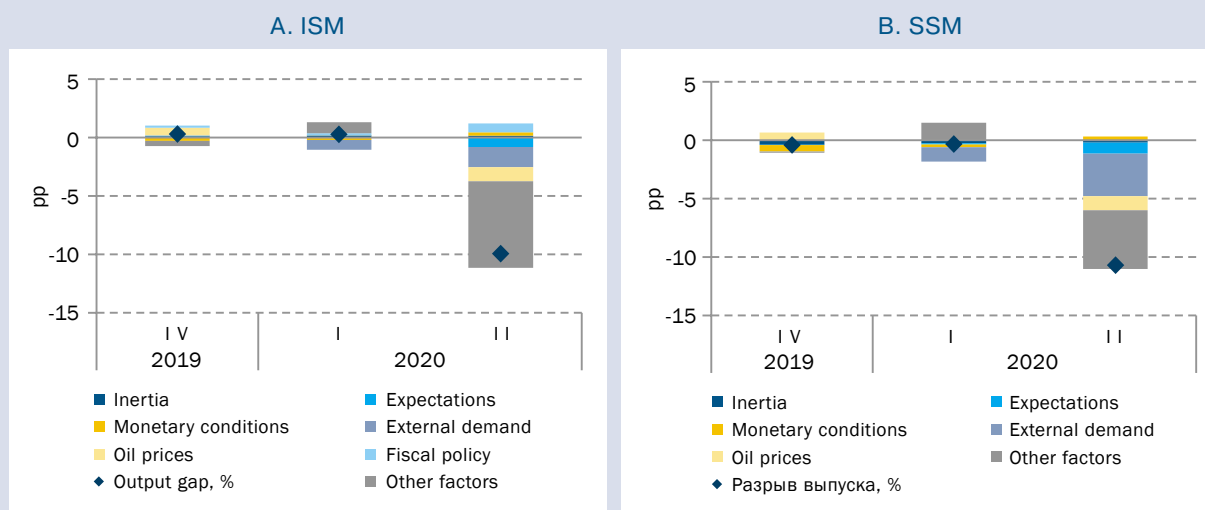


<sup>5</sup> For more information, please see the Joint EEC and EDB Report entitled 'Forecasting System for the Eurasian Economic Union' (2016).

<sup>6</sup> For more information, please see the EDB special report entitled 'Estimation of Non-Observable Economic Variables in EDB Member Countries' (August 2020).

the COVID-19 pandemic may affect potential Russian economic growth significantly more than the findings show, which will much depend on how the epidemiological situation further develops.

**Figure B.1. Decomposition of the output gap in Russia**



Source: calculations by the authors, EEC

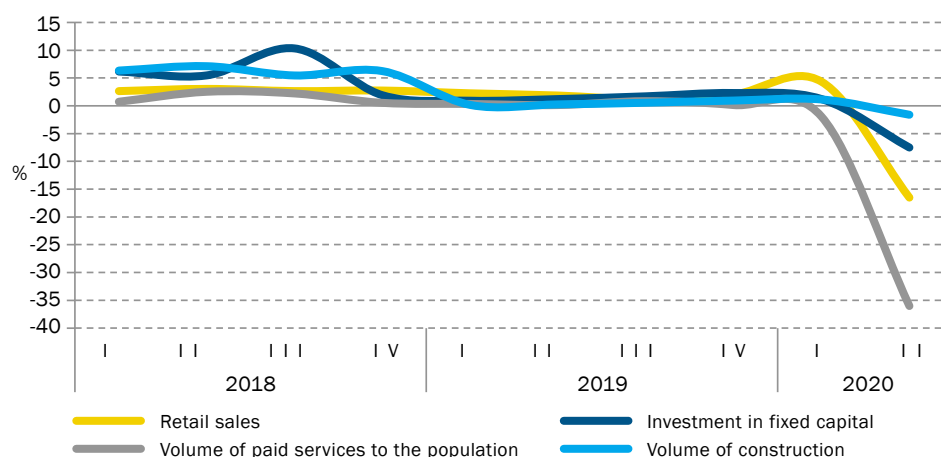
## Consumer demand declines

In terms of industry, consumer-oriented service sectors incurred the largest losses in the first half of 2020. Retail trade turnover decreased by 6.4% YoY; the volume of paid services to the population declined by 19.9% YoY. Consumer demand was negatively affected by lockdown measures and the suspension of work by some companies providing services to the population. Changes in the labor market caused by the COVID-19 pandemic were an additional driver, with rising unemployment and declining household incomes. April–May observed the largest drop in consumer activity, owing to the strict lockdown restrictions imposed. As these were eased, consumer demand commenced its recovery, and the PMI indicator<sup>7</sup> of the Russian services sector rose beyond 50 points in July, for the first time since February 2020 (58.5), indicating an increase in business activity in the sector. However, the recovery, especially in the paid services sector (down 25.5% YoY in July after being down 31.4% YoY in June and 38.9% YoY in May), is slow. It might take a long time to recover in the wake of a significant drop in income and rising unemployment.

<sup>7</sup> For more information, please see: <https://www.markiteconomics.com/Public/Release/PressReleases>

**Figure 12.**  
**Indicators of Domestic Demand**

*(period's growth rate year-on-year)*



**Source:** Rosstat

### **Weakening of investment activity**

Fixed investments decreased by 7.6% YoY in 2Q after an increase of 1.2% YoY in 1Q. The decline in activity was driven by a deterioration of financial conditions and economic sentiment across businesses, a reduction of external demand and domestic consumption, and a disruption in supply chains. The weakening of the national currency and stricter non-price bank lending conditions may also have helped restrain capital investments amid the increased risk of failed payments. The pandemic had a lower impact on the construction industry, with its output being 1.7% less in 2Q2020 than that in the corresponding period of the previous year. Overall, fiscal, monetary and macroprudential policies, including a deferral and reduction in tax and insurance payments, the reduced administrative burden on enterprises, support for banking sector liquidity and the easing of regulatory requirements, together with financial support for businesses, mitigated the decline in investments.

### **Pandemic severely affected industrial production**

Production activity in January–June 2020 decreased considerably due to lockdown restrictions and weak domestic and external demand. Industrial output decreased by 3.5% YoY in the first half of the year. However, in 2Q2020, the decline reached 8.5% YoY after experiencing an increase of 1.5% YoY in January–March.

### **Weak demand and OPEC+ agreement resulted in drop in raw materials extraction**

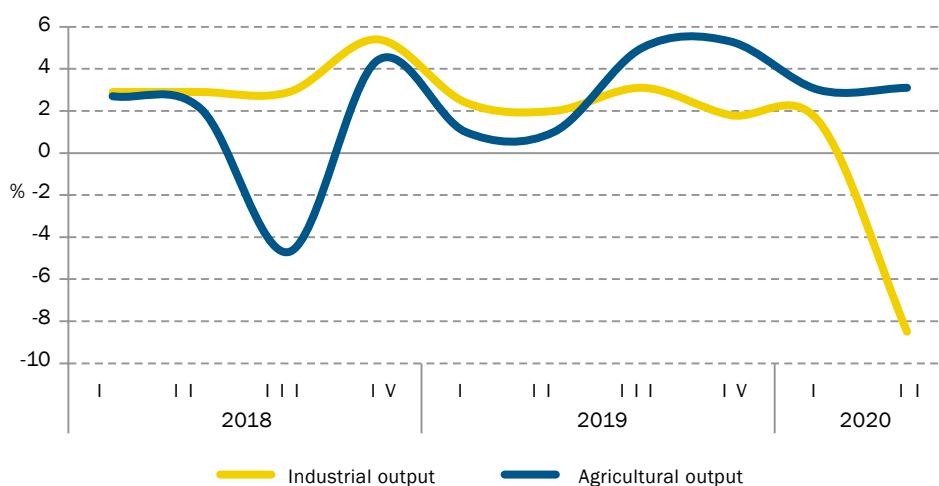
Worsening production indicators were observed in both the extractive and manufacturing industries. Extraction output in January–June decreased by 5.2% YoY, including oil and associated gas by 4.8% YoY; natural gas and condensate by 5.7% YoY; and coal by 7.4% YoY. Russia's implementation of the OPEC+ agreements on limiting oil production in May–June, weak external demand, and challenging transportation and logistics were the drivers of the sector trend. The coronavirus pandemic had a lower impact on the extraction of metals and construction materials (stone, sand, and clay), with positive growth rates remaining in the first half of the year at 0.6% and 2.7% YoY, respectively.

### Weak trend in manufacturing

Production declined by 2.3% YoY in the manufacturing industry in January–June 2020 in the wake of an unprecedented drop in domestic and foreign business activity. A large decline was observed in industries focused on investment demand and the production of non-food consumer goods (the production of vehicles, computers, electronic and electrical devices, cars and equipment, clothing, shoes and other leather goods, jewelry and furniture). The COVID-19 pandemic has had the least impact on the food, pharmaceutical and chemical industries.

When it comes to June–July, leading indicators point to a consolidation of production activity at reduced levels. The manufacturing PMI index amounted to 49.4 and 48.4 points respectively, experiencing a significant increase from April–May (31.3 and 36.2 points, respectively). Output expanded with enterprises resuming their work as lockdown restrictions eased. However, demand for products, including exports, remained weak; this clearly indicates that recovery in production activity will most likely be slow.

**Figure 13.**  
**Production Activity**  
(period's growth rate year-on-year)



Source: Rosstat

### Continued strong agriculture

Agricultural output increased by 3% YoY in the first half of 2020 (4% in 2019). This industry proved to be much less affected by the COVID-19 pandemic. Cattle numbers from key species have increased, and the relatively high growth rates of cattle products, primarily slaughter cattle and poultry (4% YoY in January–June 2020) and milk (3.6% YoY) have been maintained.

### Decrease in cargo and passenger traffic

Reduced domestic consumption and external demand, as well as restrictions on transportation, resulted in deteriorated output in the transport sector. Under such conditions, passenger turnover dropped in January–June 2020 by 47.4% YoY. Cargo turnover fell by 6.1% YoY. The largest decrease in the volume of railway transport loads was observed for ferrous metals and their scrap, and for coal, oil and petroleum products. Positive growth rates were

maintained in the transportation of construction goods, grain and milling products, chemical and mineral fertilizers among others.

## The Labor Market

**Rising unemployment** The unemployment rate in June 2020 amounted to 6.2%, an increase from 4.4% the previous year. The deterioration in the labor market was due to some organizations suspending work owing to measures introduced to contain the coronavirus disease. The number of persons employed decreased by 2.6% YoY in June 2020. It should be noted that unemployment increased mostly in April–May, during the non-working period. In June, the situation began to stabilize as the lockdown restrictions were eased.

Government aid provided to enterprises was successful in limiting the employment decline in 2Q2020; the aid included the provision of loans to support wages under special programs. According to the Ministry of Economic Development of Russia<sup>8</sup>, banks have signed loan agreements worth about 935 billion rubles to implement the aid.

**Households’  
disposable incomes  
decreased**

Real disposable income decreased by 3.7% YoY in the first half of 2020. A large drop in the indicator was observed in 2Q (by 8% YoY) due to the increased unemployment and underemployment and overall drop in economic activity. Government measures to increase payments to medical personnel and social service workers, to increase the maximum amount of unemployment benefits, to provide additional payments for children, and to grant repayment holidays provided considerable support for incomes. As per the Bank of Russia estimates<sup>9</sup>, such anti-crisis payments from the budget amounted to about 0.8 trillion rubles, or 6% of all incomes.

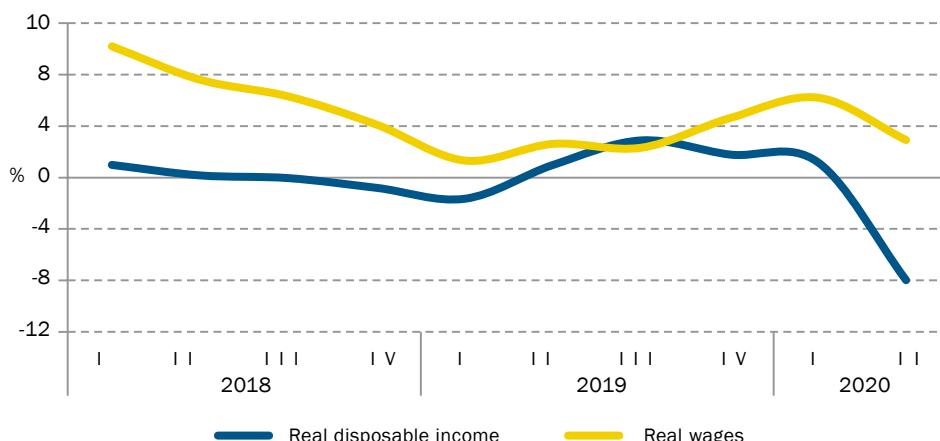
Wages continued to rise in real terms in the first half of this year (2.9% YoY after 4.8% YoY in 2019), facilitated by financial assistance from the authorities to enterprises, as well as an increase in the remuneration of medical workers. The largest reduction in nominal wages in January–June of this year was observed in the sectors most affected by the crisis (air transport, the hotel business, sports, recreation and entertainment).

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<sup>8</sup> For more information, please see: [https://economy.gov.ru/material/news/ekonomika\\_bez\\_virusa/biznesu\\_okazali\\_podderzhku\\_na\\_zarplaty\\_pochti\\_na\\_1\\_trln\\_rublej.html](https://economy.gov.ru/material/news/ekonomika_bez_virusa/biznesu_okazali_podderzhku_na_zarplaty_pochti_na_1_trln_rublej.html)

<sup>9</sup> For more information, please see: <http://cbr.ru/press/event/?id=7964> (in Russian).

**Figure 14.**  
**Labor Market Indicators**  
*(period's growth rate year-on-year)*



Source: Rosstat

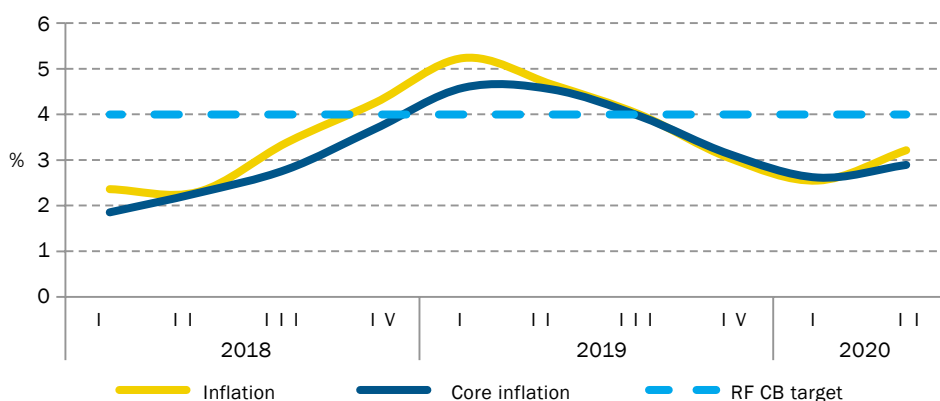
## Inflation

### Inflation remains below target

CPI inflation was 3.2% YoY in June 2020, up from 3% YoY in December 2019. The increase in the indicator mainly stems from the rise in the cost of food products due to the weakening of the national currency, challenging transportation and logistics, as well as the effect of a low base in the fruit and vegetables segment. Core inflation amounted to 2.9% YoY in June, down from 3.1% YoY in December 2019. The weakening domestic consumer demand and weak price conditions abroad mitigated its growth.

It should be noted that the maintenance of annual inflation rates below the Bank of Russia's target (4%) in the first half of 2020 may be largely attributed to the base effect: the VAT increase affected prices in early 2019. Average monthly CPI (seasonally adjusted) saw a significant acceleration in March–April during increased turbulence in the foreign exchange market, but it subsequently returned to lower values.

**Figure 15.**  
**Inflation**  
*(the last month in a quarter vs. the last month of the same quarter a year before)*



Source: RF CB

### Acceleration of food inflation

Food prices grew by 3.6% YoY in June 2020 after 3.1% YoY in December 2019. Late March–early April observed a significant acceleration of inflation in this segment; it was driven by ruble depreciation affecting prices and temporary high demand for certain products. Later on, the monthly trend in the indicator slowed down significantly. However, annual food inflation increased in June, caused by a low base in the fruit and vegetables segment from the early harvest reaped in 2019.

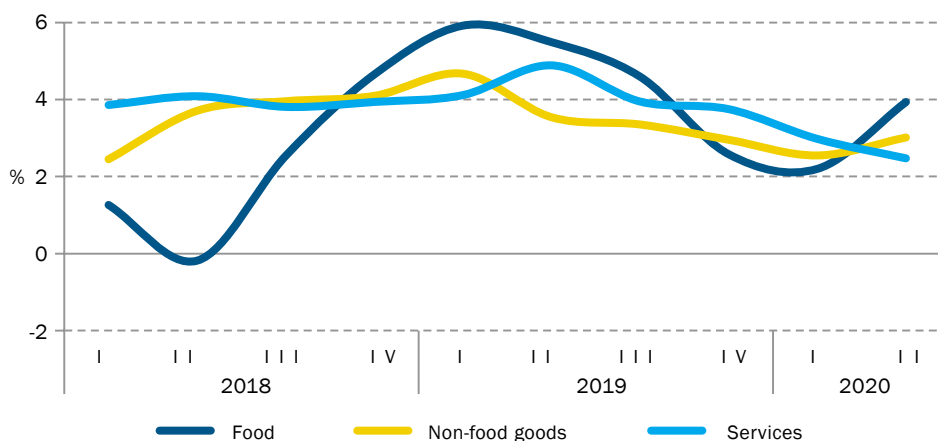
### Weak consumer activity served to hold back non-food inflation

Non-food product prices increased in June 2020 by 3% YoY and remained close to the level of last December (2.95% YoY). Inflation in this segment of the consumer basket accelerated in March–June, which may be due to exchange rate pass-through. However, the significant weakening of domestic consumer demand limited the change in non-food product prices.

The growth rate of services prices amounted to 2.5% YoY in June 2020: that marked a significant decrease compared to December 2019 (3.75% YoY). Moderate demand was a key factor in this trend in the wake of social distancing and lockdown measures. Given this, the cost of air travel and travel industry services has dropped dramatically, with these industries being among the most affected by the pandemic.

### Figure 16. Inflation Components

*(the last month in a quarter vs. the last month of the same quarter a year before)*



Source: RF CB

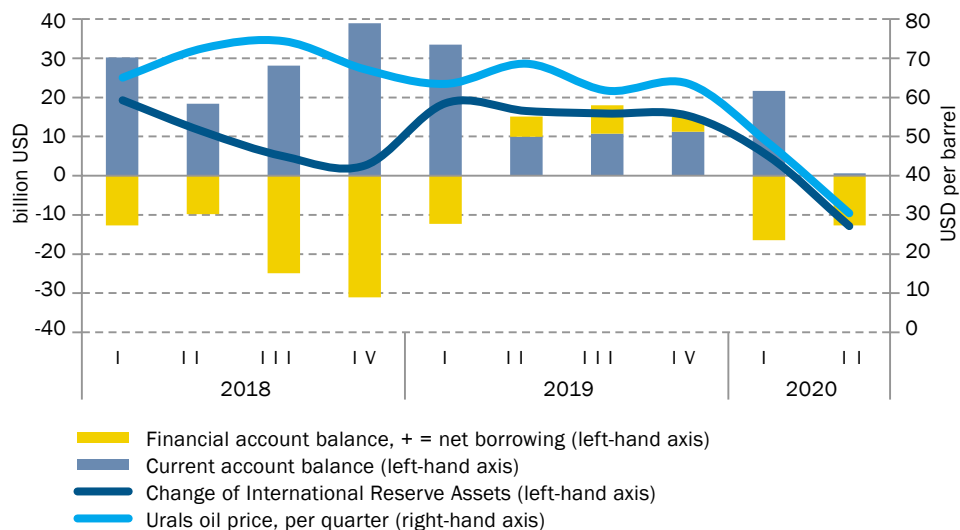
### The External Sector

#### Smaller surplus on current account of balance of payments

As per Bank of Russia estimates, the current account surplus amounted to USD 22.3 billion (3.2% of GDP) in the first half of the year, which is USD 21.1 billion (2.4% of GDP) less than that in the corresponding period of the previous year. The indicator was driven by the decrease in the trade

surplus as the services deficit and primary income balance declined. Net lending by Russia to other countries was recorded in the financial transactions account (IRA excluded) in January–June 2020 in the amount of USD 29.2 billion (USD 7.1 billion in January–June 2019).

**Figure 17.**  
**Balance of Payments**



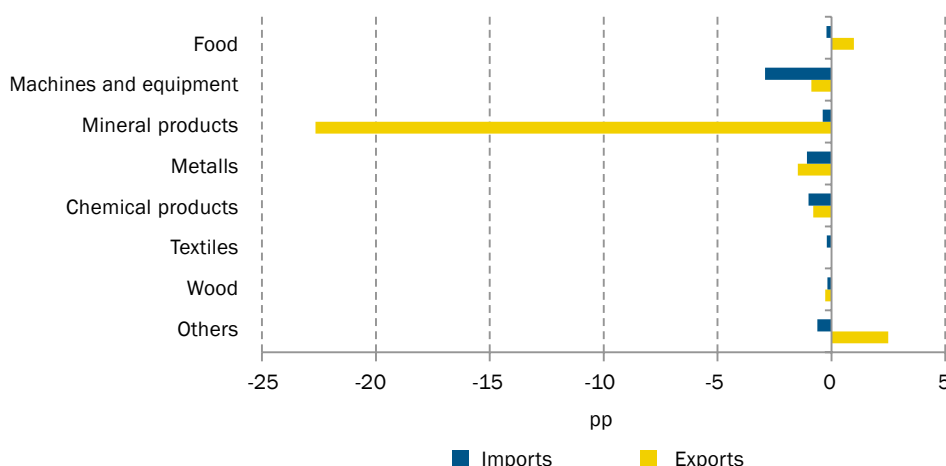
**Source:** RF CB, RF MF, Thomson Reuters, calculations by the authors

### Goods exports decrease

The trade surplus equaled USD 47.3 billion in January to June 2020, USD 39 billion less than in the same period last year. The reduction in exports of Russian goods (by USD 46.8 billion or 22.9% YoY) was the key factor in the decline in the foreign trade balance. The decrease in monetary value of oil and gas product exports was the main driver behind the indicator; that was mostly due to the weakening external demand, the decrease in oil production under the OPEC+ agreement and the drop in hydrocarbon prices.

Exports of most other key commodity groups, including machinery and equipment, metals and products made from them, and chemical products, also declined in the first half of 2020. The deterioration in the trade balance was held back by the expansion of food sales abroad amid strong indicators of the agro-industrial complex and gold, the latter due to the suspension of purchases of metal in the domestic market by the Bank of Russia from April 1, 2020, as well as a significant increase in demand for it among investors.

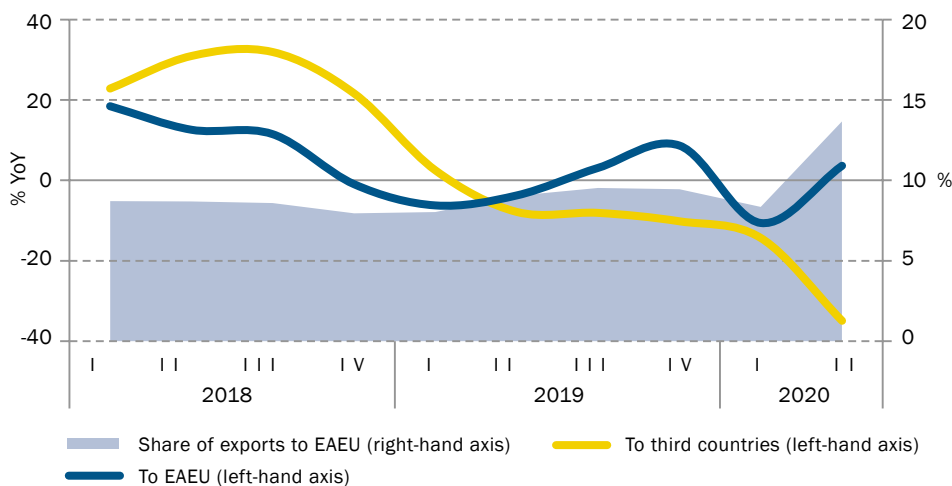
**Figure 18. Product Groups' Contribution to Goods Export and Import Changes**  
(January–June 2020 vs. January–June 2019)



**Source:** Federal Customs Service, calculations by the authors

Exports of Russian goods both to the EEU states and third countries decreased in January–June 2020. Moreover, the decrease in sales to markets outside the Union turned out to be much larger, which may be attributed to the predominance of energy products. The share of exports of Russian products to the EEU countries amounted to 10.7% in the first half of the year (9% in 2019).

**Figure 19. Goods Exports by the Russian Federation**



**Source:** Federal Customs Service, calculations by the authors

**Reduced imports in the wake of decreased domestic demand**

The decline in domestic economic activity, challenging transportation situation and weakening of the ruble resulted in an adjustment in imports of goods, which experienced a 7.8 billion-ruble decrease (or 6.6% YoY) in January–June 2020. There was a drop in sales of all enlarged commodity

groups to the country, with the peak occurring during the April non-working period. According to the RF FCS, the decline in imports saw a significant slowdown in June, which may be due to renewed domestic demand after the easing of the lockdown.

### Improved foreign trade in services

The services balance in the first half of 2020 posted a deficit of USD 9 billion, USD 5.9 billion less than in the corresponding period of 2019. This improvement is attributed to a faster decline in imports of services compared to their exports, mainly due to restrictions imposed on international transport.

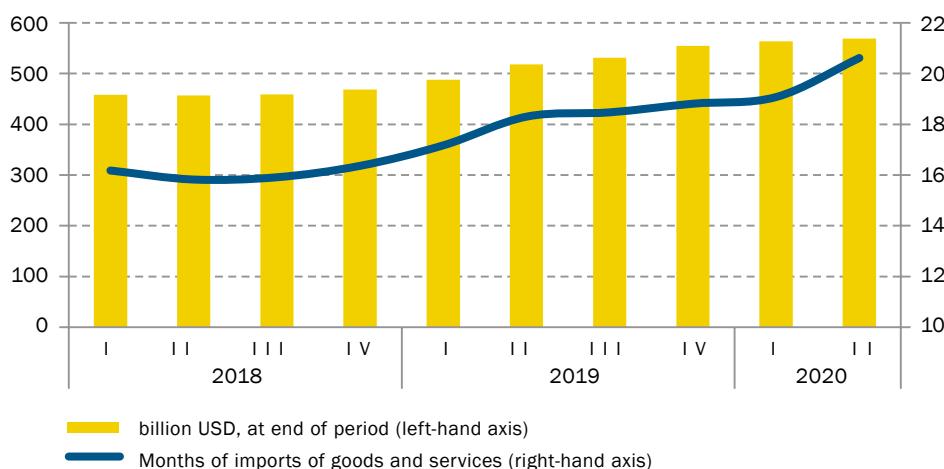
### Capital outflow accelerates

According to Bank of Russia estimates, private sector capital outflow from Russia was USD 28.9 billion in January to June 2020, USD 5.6 billion more than in the same period last year. The share of non-residents holding FLBs amounted to 30.6% as of July 1, 2020, a drop from the peak of 34.9% reached as of March 1, 2020. A significant reduction in investments made by foreign investors holding FLBs occurred in March: investors limited the amount of their investments in risky assets amid a dramatically deteriorating global economic outlook and increased volatility in the global financial and commodity markets.

### Gold and foreign exchange reserves high

The Russian Federation's international reserve assets amounted to USD 568.9 billion as of July 1, 2020, a USD 14.5 billion increase since the beginning of the year. The increase in the value of monetary gold due to a revaluation resulting from the price increase in the international market boosted the growth of gold and foreign exchange reserves. On account of the Central Bank selling foreign currency under the fiscal rule amid falling oil prices, the change in the reserves was mitigated. The volume of international reserves was above the traditional adequacy criteria.

**Figure 20.**  
International Reserve Assets of the Russian Federation



**Source:** RF CB, calculations by the authors

## The Fiscal Sector

### **Pandemic resulted in a budget deficit**

The federal budget posted a deficit of 0.8 trillion rubles (1.7% of GDP) in January–June 2020 after a surplus of 1.7 trillion rubles (3.3% of GDP) a year earlier. Both the reduced income and the expansion of expense items affected the indicator. The federal budget's revenue fell by 4.8% YoY in the first half of the year. The fall stems from a 35.4% YoY decrease in oil and gas revenues due to a collapse in energy prices and reduced production of raw materials. Non-oil and gas revenues increased by 18.5% YoY due to Sberbank being sold in April and the funds being remitted to the budget (over 1 trillion rubles). In the wake of economic recession, import-related revenues and corporate taxes declined considerably (by 5.1% YoY and by 8.4% YoY, respectively). Domestic VAT revenues began to decline in 2Q2020; however, this indicator will be more affected by the pandemic in the second half of 2020.

### **Increase in budget expenditures has smoothed out negative effects of pandemic**

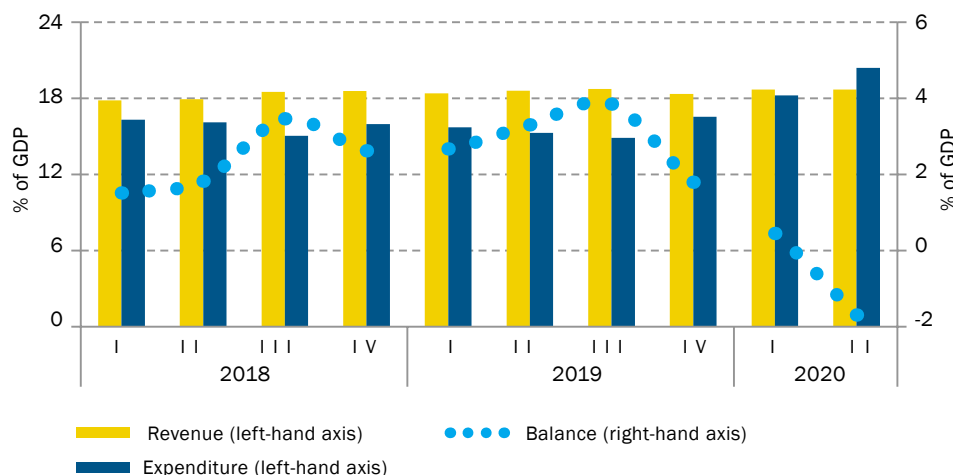
The federal budget's expenditures rose by 26.2% YoY in the first half of the year. An increase in allocations was registered for all categories (excluding debt servicing). We believe that social policy spending (an increase of 30.5% YoY), healthcare (up 109.5% YoY) and inter-budget transfers (up 63.7% YoY) were key in the growth of expenditures, which can be mainly attributed to measures introduced to mitigate the negative consequences of the COVID-19 pandemic. According to Deputy Finance Minister V. Kolychev<sup>10</sup>, the authorities' anti-crisis package is estimated at about 4 trillion rubles of direct additional budgetary expenditures (based on our calculations, this is about 3.8% of GDP), of which approximately 0.5 trillion rubles were planned to be allocated to support the health system; 0.8 trillion rubles for real incomes of the population; 2 trillion rubles for the most affected sectors of the economy (financial assistance and loans to businesses, deferrals and a reduction of tax and insurance payments, etc.); 0.7–0.8 trillion rubles for the federal subjects of Russia and the budgets of state extra-budgetary funds.

### **Public debt remains low**

According to our estimates, the Russian Federation's public debt increased to 13.6% of GDP as of July 1, 2020, from 12.5% of GDP as of the beginning of this year. The increase is accounted for by domestic debt obligations amid the budget deficit. Thus, the volume of FLBs placed amounted to 1.6 trillion rubles in January–June 2020 (versus 1.4 trillion rubles in the first half of 2019). Overall, the debt burden remains low, providing leeway for fiscal support of the economy should negative shocks occur.

<sup>10</sup> For more information, please see: [https://1prime.ru/state\\_regulation/20200702/831717944.html](https://1prime.ru/state_regulation/20200702/831717944.html)

**Figure 21.**  
**The Federal Budget**  
*(the period's cumulative balance since the beginning of the year)*

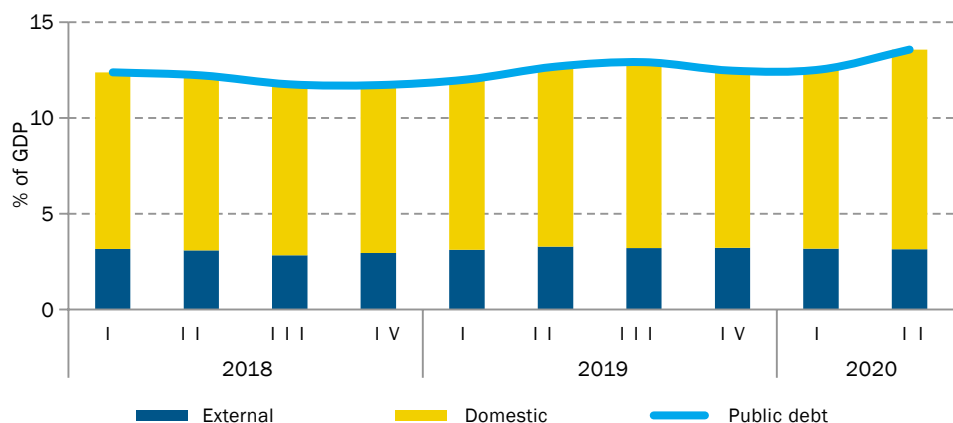


Source: RF MF, calculations by the authors

**Sovereign credit ratings confirmed**

Fitch and Standard & Poor's kept Russia's sovereign credit ratings at investment levels of BBB and BBB-, respectively. A balanced domestic economic policy and debt sustainability were drivers behind the Russian economy adapting to negative external impacts.

**Figure 22.**  
**Public debt**  
*(as at the end of period)*



Source: RF MF, calculations by the authors

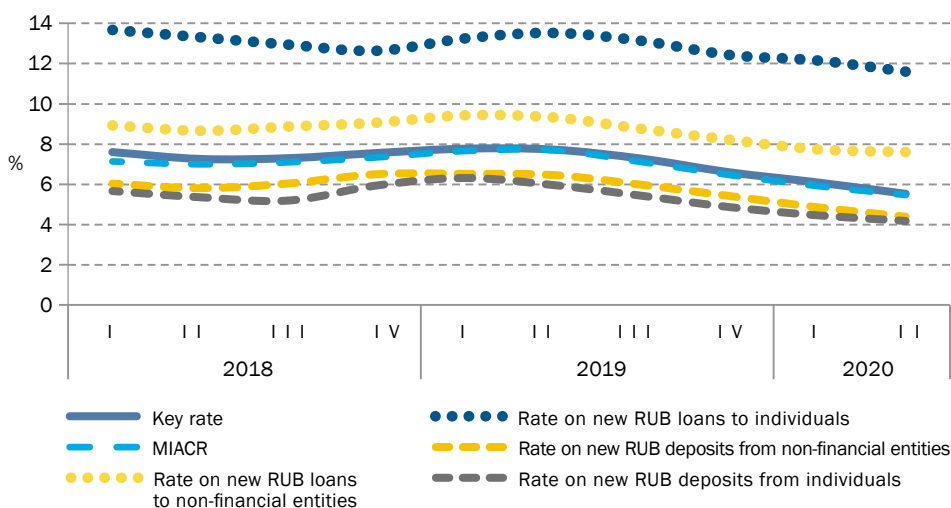
**Monetary Conditions**

**Transition to a soft monetary policy**

As of the end of August 2020, the Bank of Russia's key rate amounted to 4.25%, 2 percentage points lower compared to its level at the beginning of the year. The regulator's actions are explained by a shift in the balance of risks in 2Q towards disinflationary ones due to a deep drop in both domestic and external demand, which might cause inflation to drop below the 4%

target in the medium term. Since the inflationary processes trend has proven to be rather moderate, we believe that the Bank of Russia monetary policy adheres to a stimulative nature.

**Figure 23.**  
**Interest Rates**  
(period's average)



**Source:** RF CB, calculations by the authors

### Financial market rates decreasing

The short-term interbank loan rates stayed near the policy rate over January–June 2020, with a small negative spread resulting from a structural surplus of liquidity remaining in the banking sector. The yield on ruble FLBs also decreased visibly in April–July, propelled by the expectation of a key rate adjustment and the stabilization of the financial market after a period of increased turbulence around the middle of March.

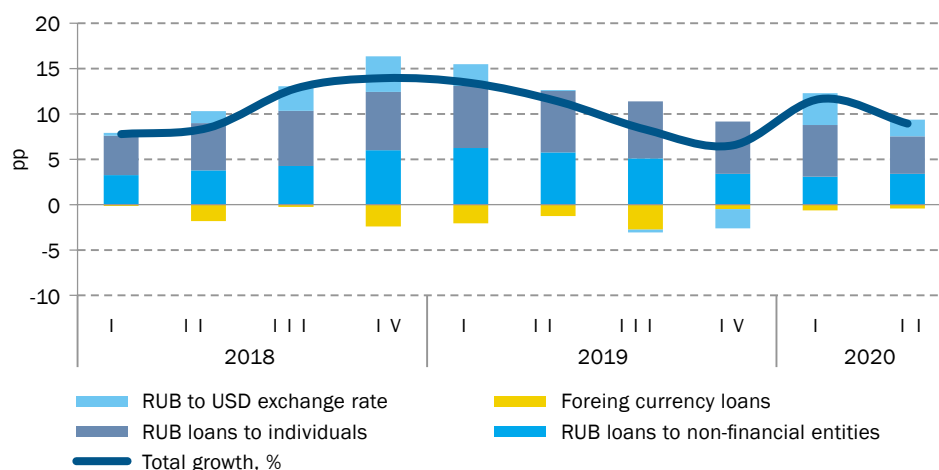
Credit risk increased due to the deterioration of the economic situation, and this limited the decline in the cost of bank lending in the first half of 2020. During the crisis, banks imposed stricter non-price borrowing requirements, including those related to the maximum size and term of loans, as well as requirements for the financial standing of recipients and securing of obligations.

### Lending activity decreasing

The weakening of business activity both domestically and abroad led to a noticeable reduction in the economy's demand for new bank loans in 2Q2020. According to the survey of banks conducted by the RF CB, such a trend was recorded for all categories of borrowers, and the largest drop was noted in retail customers. Further, amid a large-scale drop in the incomes of economic agents and the measures taken by the Bank of Russia and the government, deposit organizations indicated a significant increase in demand for loan restructuring. Due to these factors combined, the growth rate of loans to non-financial corporations and individuals (excluding currency revaluation) slowed down to 7.1% YoY as of July 1, 2020 (8.7% YoY in 2019).

**Figure 24.**  
**Factors' Contribution**  
**to the Growth**  
**of Banks' Credit**  
**Portfolio**

*(end of quarter vs. end  
of the same quarter the  
year before)*



**Source:** RF CB, calculations by the authors

**Increase in**  
**dollarization of loans**  
**and deposits**

Due to the revaluation of the currency in the first half of the year, the share of foreign currency bank loans and deposits increased, amounting to 25.5% and 25% respectively as of July 1, 2020 (24.8% and 23.4% as at the beginning of the year). The stabilization of the domestic currency market and economic activity in general are key factors for continuing with the devaluation trend in the second half of 2020.

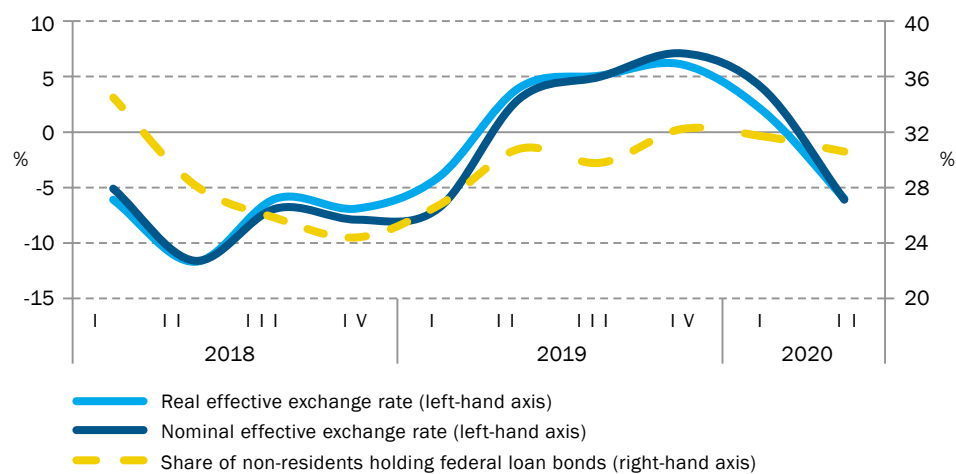
**Russian ruble**  
**weakens**

The Russian ruble weakened significantly against the world's major currencies in the first half of 2020. The main blow was seen in the second half of March: the coronavirus outbreak turned into a pandemic, while the OPEC+ countries failed to reach an agreement on extending oil production restrictions. These conditions led to panic dominating the market given the rising uncertainty and collapse in oil prices, which drove the ruble to around 80 against the U.S. dollar. The scale of the fall in the value of the national currency in this period was limited by the RF MF and Bank of Russia selling foreign currency under the fiscal rule. In May–June, the Russian ruble regained some of the ground lost and traded about 70 rubles per U.S. dollar, which was encouraged by the beginning of economic recovery both at home and abroad, as well as oil prices growth upon reaching new OPEC+ agreements on the production reduction.

**National currency**  
**undervalued**

The ruble's real effective exchange rate weakened following the nominal rate in the first half of the year. We believe that this resulted in the undervaluation of the national currency. On the one hand, inflation was affected, but on the other, the price competitiveness of domestic producers was maintained. According to our calculations, the coronavirus pandemic has led to faster weakening of the equilibrium real effective exchange rate of the Russian ruble.

**Figure 25.**  
**Russian Ruble**  
**Exchange Rates**  
*(period's growth rate*  
*year-on-year, + = ruble*  
*strengthening)*



**Source:** RF CB, calculations by the authors

# ECONOMIC OUTLOOK: RUSSIAN FEDERATION

## Background

### **Gradual recovery of major economies in the mid term**

The base case involves a further easing of lockdown restrictions in the world's largest economies (the US, the Eurozone and China) in the second half of 2020, that, along with stimulative fiscal and monetary policies, will be instrumental in a gradual recovery in consumer and investment activity, as well as international trade. However, due to the increased uncertainty, deterioration of the labor market, disruption of existing value chains, and anticipated changes in consumer habits (social distancing, higher savings rates, etc.), the return to pre-crisis production levels will be slow and is unlikely to be over until 2022.

### **External demand constrained**

Negative output gaps in the countries under review will gradually close, remaining in the negative area over the entire projection horizon (2020–2022) owing to the restrained economic activity recovery. It is expected to result in low external demand for Russian exports in the medium term.

### **Moderate oil price growth**

Under the EDB base case, oil prices will grow at a moderate pace in 2020–2022, encouraged by a recovery in global economic activity. Nevertheless, we are quite conservative in our expectations of the increase in energy commodity prices, which will continue to be affected by the uncertain global outlook.

### **Low foreign inflation**

External inflation will remain weak in the medium term. We expect the growth rate of the consumer price index in the Eurozone and the United States to remain below the ECB and FRS targets in the wake of moderate demand, lowered inflation expectations and low energy prices.

The country risk premium for Russia will remain heightened in 2020–early 2021 due to high uncertainty about the development of the pandemic and the global economic recovery, as well as a geopolitical factor (the threat of anti-Russian sanctions expanding). In the future, as the situation normalizes, we expect it to return to pre-crisis indicators.

**Weakening of fiscal impulse in the medium term** Domestic medium-term fiscal policy will see a gradual return to the fiscal rule. We expect the volume of anti-crisis support for the economy to decrease at the end of 2020–2021, resulting in a noticeable weakening of fiscal impulse.

Potential economic growth will begin to gradually recover in 2021–2022, which will be supported by the implementation of state development programs aimed, among other things, at increasing investment activity. The structural reforms' maximum effect is projected in the long term.

**Table 1. Forecast of Key Foreign Economic Indicators**

	Average annual Urals oil price (USD per barrel)	Eurozone real GDP growth rate, %	China real GDP growth rate, %	Inflation (CPI) in the Eurozone, % (period's average)	Inflation in U.S. (PCE), % (period's average)
<b>2020</b>	42.4	-8.4	1.5	0.4	1.0
<b>2021</b>	48.9	5.5	8.3	0.5	1.0
<b>2022</b>	52.7	3.7	5.6	1.3	1.6

**Source:** calculations by the authors, EEC

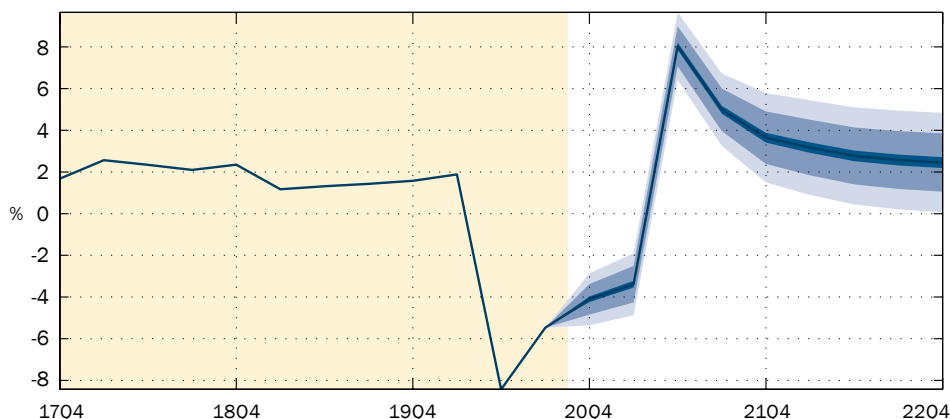
## Economic Activity

### Economic activity to recover gradually in second half of 2020

The easing of lockdown restrictions both in Russia and abroad since the end of the first half of this year is generating conditions for the recovery of economic activity in the country. We expect a gradual recovery in consumer and investment demand, which will continue to be supported by stimulative monetary and fiscal policies in 2020. Increased business activity abroad and the weakening of the national currency will help limit the decline in non-energy exports. The implementation of the OPEC+ agreements will continue to restrain oil production: according to our calculations, factoring in the impact on related industries, it may cost about 0.7% of the country's GDP this year.

We believe that quarterly GDP (seasonally adjusted) will begin to grow from 3Q2020, which will result in a slower decline in annual indicators (from down 8% YoY in April–June to down 4–5% YoY in the second half of the year) and a gradual reduction in the negative output gap. The GDP contraction rate over 2020 is estimated at 4.2%.

**Figure 26.11**  
**Real GDP**  
*(period's growth rate year-on-year)*



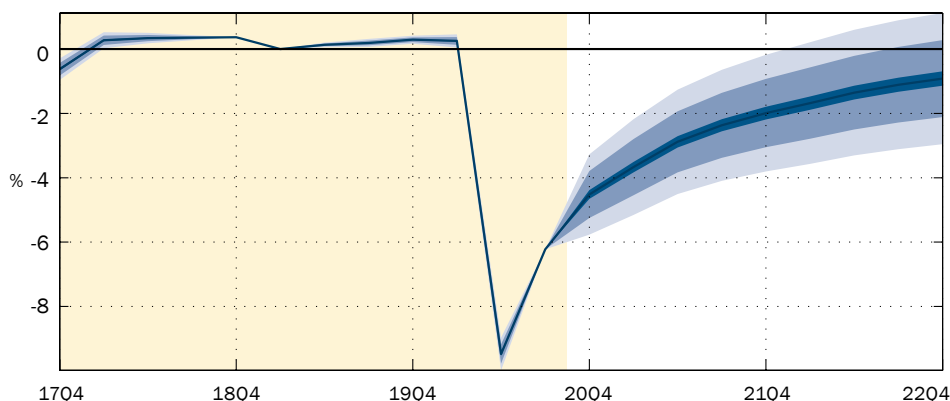
**Note:** seasonally adjusted data.  
**Source:** calculations by the authors, EEC

Compared to the previous projections, the assessment has been downgraded by 1.9 pp<sup>12</sup>, thus demonstrating the longer-term effect of lockdown measures and their slower easing than that expected in early April<sup>13</sup>, as well as the stronger negative impact of the pandemic on economic activity abroad.

**Risks of aggravation of economic situation**

The short-term risks are shifted towards a larger reduction in GDP due to the ongoing challenging epidemiological situation in the world and the risks of a large second wave of the pandemic in the fall and winter. Should they materialize, and should the authorities react as they did in 2Q2020, Russia's GDP may decrease by 6–7% in the year.

**Figure 27.**  
**Output Gap**



**Source:** calculations by the authors, EEC

<sup>11</sup> Here and elsewhere the chart ranges correspond to the 10%, 50% and 75% confidence intervals.

<sup>12</sup> Please see EDB Macroeview. April 2020. Updated Projections.

<sup>13</sup> The April projections assumed that the lockdown would last one month.

**Gradual recovery of economic activity in 2021–2022**

In the 2021–2022 base case, we expect GDP growth to continue to recover by an average of 3% per year as the situation in the global economy and commodity markets stabilizes, domestic structural reforms are implemented, and monetary policy support continues. However, the EDB forecasts assume that this will be a slow process due to the long-term weakening of investment activity amid the increased uncertainty, a number of service-related organizations closing down, rising unemployment and changing consumer habits (social distancing, a weak travel industry and air transportation). In addition, fiscal support is projected to decrease in 2021 as the fiscal impulse from the anti-crisis measures introduced weakens.

As a result, we believe that the pre-crisis level of GDP (4Q2019) will be reached only in the first half of 2022. A slow recovery will result in a negative output gap remaining throughout the forecast period, indicating that the economy will operate with excess production capacity.

**Lingering risks to economic growth**

The risks to the medium-term forecasts have shifted to the downside. The development of the epidemiological situation is still uncertain. Should it worsen, we might expect greater losses of potential economic growth than those built into the base case due to a continuous decline in investment and innovation activity. There is still a high chance of geopolitical tensions increasing and stricter anti-Russian sanctions being imposed; it might have a significant negative effect on the business climate. In addition, there is also an increased risk of global trade protectionism growing, which may hinder global economic recovery.

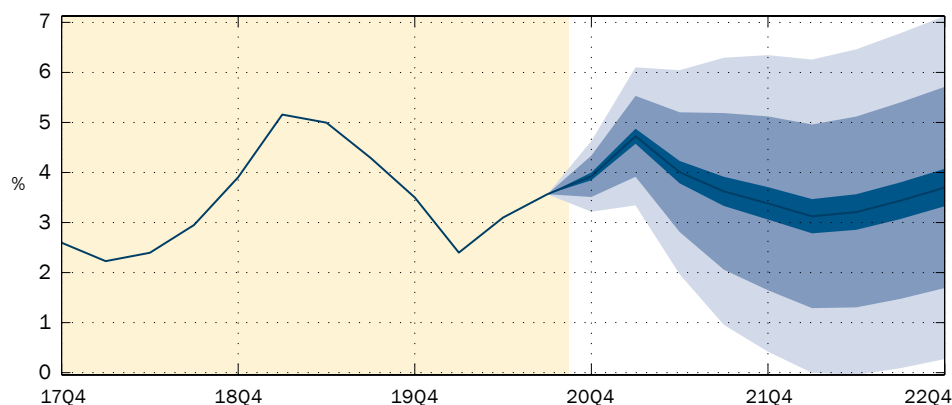
**Inflation****Inflation below target in medium term**

According to the EDB forecasts, inflation will amount to 3.9% YoY at the end of 2020. The increase in the indicator in the second half of this year will be due to the ruble's weakening influencing prices, as well as the effect of the low base of the previous year, with its price growth having slowed down significantly.

Restrained domestic demand will have a significant disinflationary impact. This factor is expected to exert its maximum impact on the consumer price index in 2021, which, along with the projected stabilization of the national currency, will result in a significant inflation slowdown — to 3.5% YoY in 2021 under the EDB base case.

A gradual recovery in economic activity will help reduce the disinflationary impact of domestic demand during 2022, which will increase the growth rate of the consumer price index to 3.7% YoY.

**Figure 28.**  
**Inflation**  
(period year-on-year)



**Note:** seasonally adjusted data.

**Source:** calculations by the authors, EEC

### Risks are shifted towards disinflation

Currently, disinflationary risks predominate. They are driven by a likely slower recovery of the Russian and global economies than that projected in the EDB base case.

Pro-inflationary risks are associated with the threat of long-term and serious disruption of supply chains and shortages of individual goods in the event of a widespread second wave of the pandemic. In addition, should an unfavorable scenario occur, volatility in the foreign exchange market may again experience a significant increase, which will affect the prices of imported goods and the expectations of economic agents.

## Monetary Conditions

### Stimulative monetary policy

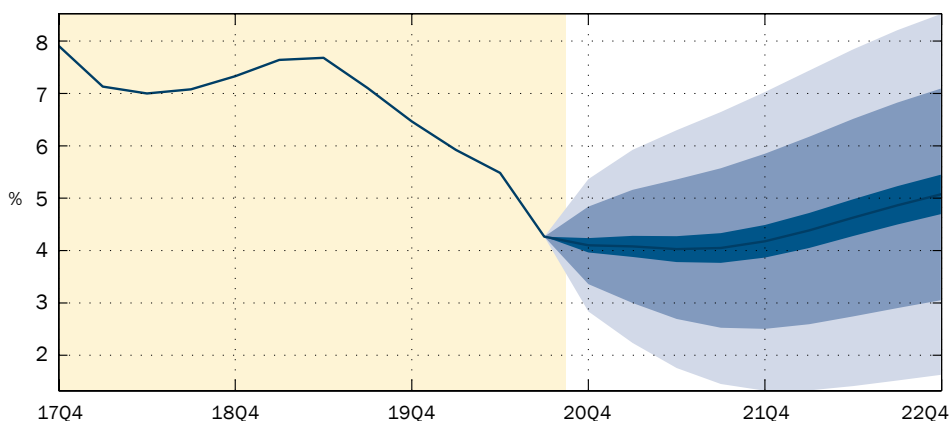
We believe that the key rate has already been reduced by nearly as much as possible; it will remain at 4–4.25% till the end of this year. This implies the maintenance of a moderately stimulative monetary policy in order to facilitate the recovery of economic activity and prevent inflation from deviating significantly below the 4% target.

Due to the completion of the cycle of monetary policy easing and barring any major shocks, the cost of resources in the interbank market and the yield on short-term FLBs will be almost on a par with the key rate level. We believe that the potential for a further lowering of interest rates on loans granted to

non-financial organizations and the population remains; it is due to both lags in the transmission of the key rate adjustment already implemented, and to a possible reduction in the credit premium as the situation in the Russian and global economies stabilizes.

Amid the prevalence of disinflationary risks, we expect soft monetary conditions to remain in the medium term. The base case assumes that a gradual increase in the key rate will commence in the second half of 2021 and that it will approach 5–5.5% by the end of the forecast period.

**Figure 29.**  
**MIACR**  
*(the period's average)*



**Source:** calculations by the authors, EEC

**Geopolitical risks limit leeway for ruble to strengthen in second half of 2020**

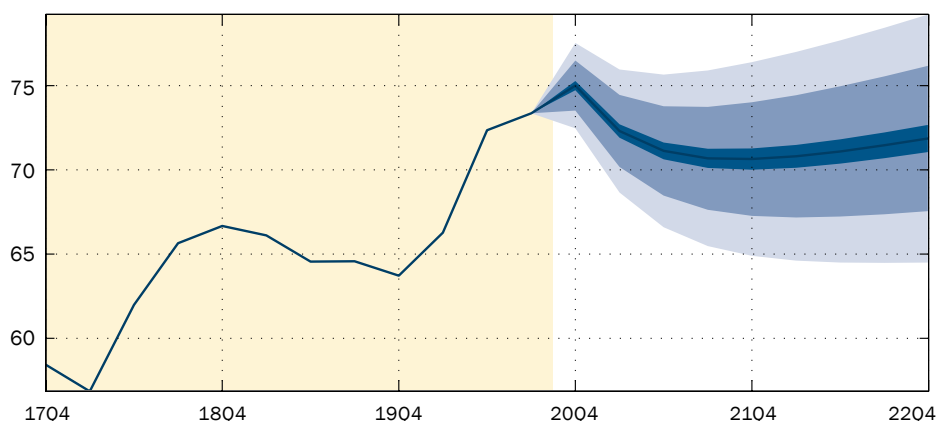
In the second half of August–early September 2020, pressure on the Russian ruble exchange rate grew due to the increasing geopolitical risks. This resulted in the ruble weakening to about 75 per U.S. dollar. This factor is likely to remain key during the rest of the year, which will hinder the full strengthening of the national currency. In 2020, the average annual exchange rate of the Russian ruble vs. the U.S. dollar is projected to be around 71.7 per USD.

**Correction of exchange rate to equilibrium level in 2021**

The exchange rate is expected to adjust to an equilibrium level during 2021 assuming a slowdown in the coronavirus spread and normalization of the geopolitical situation. In this scenario, investors might become more interested in emerging market assets, including those denominated in rubles with their relatively high yield level. This may result in the Russian currency strengthening against the U.S. dollar in 2021.

In 2022, the EDB projects the ruble rate against the U.S. dollar to stay within equilibrium trajectory, without putting additional pressure on inflation. The weakening of the exchange rate in nominal terms will be due to a higher growth rate of consumer prices in Russia compared to the U.S.

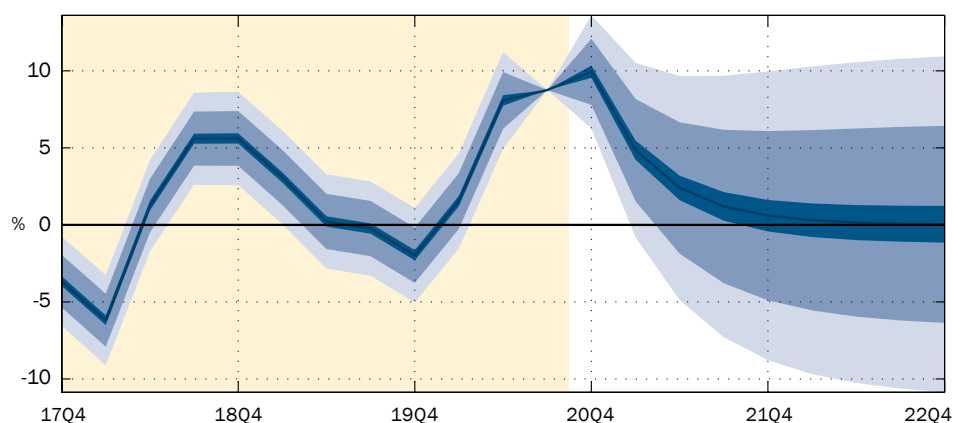
**Figure 30.**  
**Russian Ruble to**  
**U. S. Dollar Exchange**  
**Rate**  
(RUB per USD)



**Source:** calculations by the authors, EEC

The main risks to the exchange rate emanate from the external sector. Negative trends in the global economy might trigger a drop in key Russian export prices, provoking a reduction in investor demand for emerging market assets. Sanctions imposed by Western countries against Russia also remain a risk factor.

**Figure 31.**  
**Real RUB to**  
**USD Exchange Rate**  
**Gap**  
(+ = the ruble is undervalued)



**Source:** calculations by the authors, EEC

**Table 2. Key Macroeconomic Indicators of the Russian Federation**

Indicators	2017	2018	2019	2020F	2021F	2022F
<b>GDP</b> in constant prices (% growth YoY)	1.8	2.5	1.3	-4.2	3.2	2.7
<b>Consumer price index</b> (% growth in December to previous year's December)	2.5	4.3	3.0	3.9	3.5	3.7
<b>Nominal MIACR rate in national currency</b> (the year's average% per annum)	9.0	7.1	7.2	4.9	4.1	4.7
<b>Nominal Russian Ruble to U. S. Dollar Exchange Rate, RUB per USD</b> (the year's average)	58.3	62.5	64.7	71.7	71.2	71.3

**Source:** calculations by the authors, EEC



## **Eurasian Development Bank**

**RESEARCH DEPARTMENT,  
EURASIAN DEVELOPMENT BANK**

Your comments and suggestions concerning this review  
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