

Russia Macro View

We cut 2014E GDP growth to 1.0% from 2.6% previously

- **We downgrade GDP growth on heightened uncertainty.** The rising tensions in Ukraine ([Uncertainty in Ukraine: Tensions Persist Amidst Progress on Interim Government and a Rising Separatist Threat](#)) make for a very challenging backdrop to the Russian economy, creating substantial downside risks to economic performance. The combination of more subdued investment and consumption spending related to heightened uncertainty, and tighter monetary policy, lead us to downgrade our 2014 GDP forecast from 2.6% to 1.0% (1.3% in 2013).
- **Investment spending will be the key avenue via which market volatility will affect growth performance.** The sectoral breakdown of last year's investment suggested that private-sector consumption-related investment has been growing, while it was oil and gas investment that was holding back overall investment activity. Our more positive view on 2014 GDP was critically dependent on the assumption that government-led oil and gas investment would come out of its 2013 doldrums, with new projects coming on stream. However, given the uncertain backdrop, we now have much less confidence about this scenario playing out, even if, in principle, the government may feel more pressure to 'take control' of SOE investment plans. We, therefore, cut our real investment growth forecast to zero from 3.8% previously.
- **Consumer spending will also feel the pain.** While consumption is the only bright spot in Russian macro, it has been on a downtrend recently as fears of a consumer boom turning into a bubble have led to more restrictive regulatory behavior ([Is there more room to consume?](#)). Now broader uncertainty will further weigh on real private consumption spending, which we cut to 3.2% from 4.2% previously.
- **CBR's rate hike will further constrain growth.** The CBR was right, in our view, to [hike rates by 150bps to 7.00%](#) to ward off contagion, but this will also come at the cost of stronger headwinds to growth even if the CBR fully unwinds the hike by year-end.
- **More generally, Russia faces a tight fiscal-monetary policy mix.** As discussed in more detail in our recent [Russian trip notes](#), in addition to the CBR being unwilling to jeopardize its credibility on inflation, Russia is pursuing a tight fiscal policy, which limits the borrowing requirement to no more than 1% of GDP. The MinFin argues that the small output gap and sensitivity of public finances to lower prices is a strong argument for pursuing a prudent fiscal policy at this juncture.
- **The current account will benefit from a weaker currency and more subdued growth.** Concerns about the [fast-declining current account surplus](#) have recently focused market attention. The significant currency depreciation of the last couple of months and more subdued growth-driven imports should lead to somewhat larger surplus this year. We upgrade our annual surplus forecast from US\$24bn to US\$33bn.

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Figure 1. Russia Economic Indicators

	2007	2008	2009	2010	2011	2012	2013F	2014F	2015F
Summary Data									
Nominal GDP, US\$ bn	1,304	1,665	1,229	1,524	1,897	2,012	2,127	1,939	2,070
Nominal GDP, local currency bn	33,247	41,277	38,807	46,309	55,800	62,599	67,710	72,498	78,759
GDP per capita, US\$	9,081	11,585	8,554	10,611	13,227	14,055	14,890	13,612	14,566
Population, mn	143.7	143.7	143.7	143.6	143.4	143.2	142.8	142.5	142.1
Unemployment, % of labour force	6.1	6.4	8.4	7.5	6.6	5.5	5.5	5.7	5.8
Economic Activity									
Real GDP, % yoy	8.5	5.2	-7.8	4.5	4.3	3.4	1.3	1.0	2.3
Real investment growth % yoy	21.0	10.6	-14.4	5.9	10.2	6.0	-0.3	0.0	3.5
Real consumption growth % yoy	10.7	8.4	-3.9	3.5	4.8	5.0	3.3	2.5	2.4
private consumption growth % yoy	14.2	10.4	-5.1	5.5	6.3	6.7	4.3	3.2	3.1
Real export growth, % yoy	6.3	0.6	-4.7	7.0	0.3	1.4	1.5	2.0	2.1
Real import growth, % yoy	26.2	14.8	-30.4	25.8	20.3	9.5	5.5	4.5	5.0
Prices, Money & Credit									
CPI, % yoy	11.9	13.3	8.8	8.8	6.1	6.6	6.5	5.5	5.0
CPI, % avg	9.0	14.1	11.6	6.8	8.4	5.1	6.8	6.0	5.2
Nominal wages, % yoy	26.0	27.4	9.1	12.8	11.7	13.3	12.3	13.5	12.7
Credit extension to private sector, % change	49.3	37.2	2.6	12.9	28.1	19.4	17.2	15.0	15.0
Policy interest rate, %, eop	6.50	9.50	6.00	5.00	5.25	5.50	5.50	5.50	5.25
1 month inter-bank rate, %, eop	6.09	20.20	6.32	3.78	6.37	6.90	6.81	6.43	6.23
Long-term yield, %, eop	6.58	10.90	9.45	8.23	8.77	7.04	7.88	7.93	7.73
RUB/US\$, eop	24.6	29.4	30.2	30.5	32.2	30.4	32.7	38.1	38.0
RUB/US\$, avg	25.6	24.9	31.8	30.4	29.4	31.1	31.8	37.4	38.1
RUB/EUR, eop	35.7	41.4	43.4	40.3	41.7	40.2	45.0	53.4	53.5
RUB/EUR, avg	35.0	36.4	44.2	40.3	40.9	40.0	42.3	51.9	53.5
Balance of Payments, US\$ bn									
Current account	72.2	103.9	50.4	67.5	97.3	72.0	34.0	33.3	24.3
% of GDP	5.5	6.2	4.1	4.4	5.1	3.6	1.6	1.7	1.2
Trade balance	123.4	177.6	113.2	147.0	196.9	192	169	169	160
Exports	346.5	466.3	297.2	392.7	515.4	528.0	523.6	536.7	552.8
Imports	223.1	288.7	183.9	245.7	318.6	335.7	355.0	367.4	393.1
Service balance	-16.7	-20.4	-17.6	-26.1	-33.5	-46.5	-63.0	-63.0	-59.9
Income balance	-28.8	-46.5	-39.7	-47.1	-60.4	-67.7	-67.6	-69.0	-70.5
FDI, net	11.1	19.1	-6.7	-9.4	-11.8	-18.1	12.4	22.3	10.0
International reserves	466.4	410.7	405.8	432.9	441.2	473.1	468.3	446.6	445.9
Total Amortisations	28.5	47.2	49.9	40.8	52.0	90.5	139.0	103.1	105.3
Public Finances, % of GDP									
General government balance	5.4	4.1	-5.9	-3.9	0.8	0.0	-0.2	0.0	-1.0
General government primary balance	5.8	4.4	-5.4	-3.4	1.2	0.6	1.6	1.8	0.8
Public debt	7.1	5.2	9.5	9.3	9.4	11.4	11.2	12.0	12.7
Domestic	4.0	3.3	5.8	6.3	7.1	7.9	7.5	8.5	9.5
Foreign Assets & Liabilities, US\$ bn									
External debt	471.2	480.6	467.3	488.9	538.9	636.4	697.4	684.3	699.0
Public	37.4	29.5	31.3	34.5	34.7	38.1	43.1	44.9	51.0
External debt / GDP, %	36.1	28.9	38.0	32.1	28.4	31.6	32.8	35.3	33.8
External debt / XGS, %	120.7	91.8	136.3	110.7	94.0	107.8	120.3	115.9	116.2
Short-term debt	99.7	73.6	52.7	60.2	68.2	81.5	76.8	81.0	84.7
Short-term debt/International Reserves, %	21.4	17.9	13.0	13.9	15.5	17.2	16.4	18.1	19.0

Quarterly Economic Indicators

	2013 Q2	2013 Q3	2013 Q4	2014 Q1	2014 Q2	2014 Q3	2014 Q4	2015 Q1	2015 Q2
GDP, % yoy	1.2%	1.2%	1.4%	1.0%	1.2%	0.8%	1.0%	2.5%	2.8%
CPI, % yoy	6.9%	6.1%	6.5%	6.4%	6.0%	6.2%	5.5%	5.4%	5.4%
Policy interest rate, %, eop	5.50%	5.50%	5.50%	7.00%	6.50%	6.00%	5.50%	5.25%	5.00%
1 month inter-bank rate, %, eop	6.71%	6.53%	6.83%	6.63%	6.63%	6.48%	6.43%	6.31%	6.31%
Long-term yield, %, eop	7.93%	7.62%	7.88%	8.13%	8.13%	7.98%	7.93%	7.92%	7.81%
RUB vs USD	32.71	32.35	32.73	36.50	37.14	37.77	38.12	38.09	38.07
RUB vs EUR	42.72	43.65	44.97	50.05	51.33	52.64	53.41	53.44	53.48

Source: National sources, Citi Research estimates

Appendix A-1

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