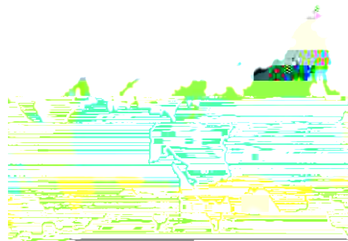
Russia Monthly Economic Developments

January 2015

THE WORLD BANK

- The retreat in crude oil prices continued in December and the first half of January with oil prices falling below US$50 per barrel for the first time since 2009.
- The continued downward adjustment in oil prices amplified the Russian currency crisis and the increasing risk to the financial sector, to which the authorities reacted with coordinated stabilization measures.
- Inflation soared into the double digits at the end of 2014 despite the CBR's tightening.
- The 2014 federal budget is expected to be in deficit due to measures to recapitalize Russia's banking sector.
- The World Bank further lowered its 2015 growth projection for Russia to -2.9 percent from -1.5 percent.

The retreat in crude oil prices continued in December and in the first half of January with oil prices falling below US$50 per barrel for the first time since 2009. The oil market is searching for a new equilibrium price in the ongoing competition for market share between OPEC and non-OPEC producers, more so since OPEC's decision not to cut oil output at its November 27 meeting. Brent (the international marker) was trading at around US$46 per barrel (bbl) on January 12, having dropped by as much as US$69/bbl (60 percent) over the last six months from above US$115/bbl. Non-OPEC supply, particularly US output, continues to grow and oil production in Iraq and Russia surged to the highest level in decades. Russian oil production rose in December to a post-Soviet record of 10.67 million barrels per day (bpd), while Iraq exported the highest volume since the 1980s at 2.94 million bpd. On the demand side, only the US market has shown some signs of improvement and the global oil market is expected to return to a new balance only later in 2015.



The continued downward adjustment in oil prices amplified the Russian currency crisis. In 2014, the Ruble lost about 46 percent of its value versus the US$ and 38 percent versus the dual currency basket while the Central Bank of Russia (CBR) spent about US$87.8 billion of its foreign currency reserves to support the Ruble. As a result, the reserves fell to US$388 billion at the end of 2014, which include the balances of the two sovereign wealth funds managed by the CBR (the Reserve Fund with a balance of US$88 billion and the National Welfare Fund with a balance of US$78 billion). In December, pressure on the Ruble had continued, forcing the CBR to resume interventions in support of the free-floating currency with US$10.3 billion during the first half of the month. On December 16, the CBR hiked its key policy rates for the sixth time in 2014, by 650 basis points to 17 percent. This resulted in a cumulative increase of 1,150 basis points in 2014. However, the Ruble continued to devalue, adversely impacted by falling oil prices and financial sector sanctions which contributed to a foreign exchange liquidity crunch. Constrained access to external financing led to the hoarding of foreign currency by Russian banks and corporations in order to be able to service large external debt payments of about US$35 billion due in December. The loss of CBR's reserves, the limited debt rollover capacity of the Russi $

The Ministry of Finance

started the sale of foreign currency in the second half of December and the CBR introduced new 28 and 365 days foreign currency loans to banks with a capital over RUB 100 billion (for which 11 largest banks qualify). The government also ordered five major state-owned exporters to reduce their net foreign assets by March 1, 2015 back to the level of October 1, 2014 with the schedule for sales of foreign currency by these companies to be agreed with the CBR. New measures were also introduced to enhance the stability in the banking sector: (i) the government approved a RUB1 trillion recapitalization plan for banks financed with domestic sovereign bonds (OFZ); (ii) the State Duma approved a bill allowing the government to place up to 10 percent of the National Wealth Fund on subordinate deposits and subordinate bonds of Russian banks.

The 2014 federal budget is expected to be in deficit due to According to the latest estimates by the Ministry of Finance, the federal budget balance in 2014 will be at a 0.7 percent of GDP deficit as opposed to the previously estimated 0.4 percent of GDP surplus. This deterioration in the fiscal position is due to issuance of OFZ bonds in the amount of RUB1 trillion (1.4 percent of GDP) to recap5 487.75 Tm(s)5(t 0 1 151.7 4n0102 TJETBT.s)5(t3)-4(an)-7(ks)]TJETBT1 0 0 1 182.73 501.59 Tm(.0101 Tc(.)]TJET

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