The OPEC+ decision to delay an easing of production cuts in February and March supported oil prices, with crude oil prices rising 15 percent in December and continuing to strengthen in January. The start of COVID-19 vaccinations in major economies and news of a stimulus package in the U.S. supported investors’ sentiment towards a global recovery and appetite for riskier assets, which strengthened emerging market currencies, including the ruble. Economic performance improved in November on the back of stronger performance in manufacturing and agriculture. In December, industrial production output grew by 1.5 m-o-m, sa (-0.2 percent, y/y) due to a stronger performance in manufacturing. Due to higher food inflation, the annual headline consumer price index (CPI) inflation accelerated to 4.9 percent in December (versus 4.4 percent in November). Labor market dynamics slightly improved in November. In 2020, higher public spending, driven by the response to the spread of the pandemic, and the need to support the economy amidst lower oil/gas revenues, worsened the fiscal stance: the federal budget registered a deficit of Rub4.1 trillion1 (3.8 percent of GDP), compared to a surplus of Rub1.9 billion last year (1.8 percent of GDP). Overall, in 2020, Russia’s current account (CA) surplus halved (US$32.5 billion) as the country faced a sizable negative terms of trade shock with lower global demand for most exported products and services. Lower oil prices, elevated uncertainty, higher geopolitical risks, and significant financial markets volatility resulted in the increase of net capital outflows (US$49 billion compared to US$22.2 billion in the previous year).

The Global Context

The sharp resurgence of the COVID-19 pandemic continued to accelerate, and the total number of global COVID-19 cases exceeded 100 million, with over 2 million deaths. The rapid rise in new cases has forced many governments to tighten stringency measures, which has weighed on global activity, particularly the services sectors. Global PMI lost momentum in December but remained above the expansionary threshold at 52.7. After a modest improvement in mid-2020, international tourist arrivals and retail and recreation mobility indicators deteriorated in 2020Q4. The Sentix global economic sentiment index, however, has continued to improve on the back of vaccine rollouts, reaching 14.9 points in January 2021. Global financing conditions remain supportive, with the emerging markets bond index spread at 330 basis points in mid-January—roughly half the 2020 high that was observed in March.

Crude oil prices rose 15 percent in December and continued to strengthen in January. The price of Brent crude oil reached US$55/bbl in mid-January, its highest level since February 2020, but still more than 10 percent below its pre-COVID level. A key factor supporting prices in January was the decision by OPEC+ to delay an easing of production cuts in February and March. While the delay applied to the majority of members, Russia and Kazakhstan were allowed a modest increase in production of 65 thousand barrels per day (kb/d) and 10kb/d respectively. However, this was more than offset by a voluntary cut of 1mb/d by Saudi Arabia, which will result in a net decrease in production among OPEC+ relative to its level in 2020H2. Outside of OPEC+, the rise in prices has stimulated a recovery in activity, with the U.S. rig count increasing to 287 in mid-January, nearly 70 percent higher than its low in August 2020, although still well below its pre-COVID level. On the demand side, a reintroduction of COVID-19 preventative measures amid surging infection rates caused the recovery in oil demand to falter, particularly in the U.S. and Europe. In its January report, the International Energy Agency revised down its expectation for global oil demand in 2021 by 0.3mb/d, although a sizeable pickup in 2021H2 is still expected as the rollout of vaccines gathers speed.

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1 Cash basis.
Figure 1: Crude oil prices rose 15 percent in December and continued to strengthen in January

![Graph showing oil prices from January 2020 to January 2021.](source: Bloomberg)

Recent economic developments in Russia

As of January 28, 2021, the total number of COVID-19 cases in Russia exceeded 3.7 million, the 4th highest count after the U.S., India, and Brazil. As of now, the new strains of coronavirus infection with the increased ability to be transmitted, which appeared in the UK, Brazil, South Africa and the United States have not been detected in community transmission in Russia. The number of new cases in Russia has started to decline since the end of December, but remains at a high level: On January 28th, Russia registered 19,138 new cases. Since the beginning of the pandemic, Russia has registered 71,651 deaths (575 deaths on January 27). The total number of tests conducted: greater than 100.7mln. New cases are mostly concentrated in Moscow, St. Petersburg, and Moscow oblast (38 percent of the total number of cases). Different regions have introduced their own restrictions depending on the epidemiological situation, but there are no strict lockdowns. In Moscow, the coronavirus infection rate has improved: Average daily new cases decreased by 35 percent compared to the end of December, standing at 2,897 on January 28th. The Moscow government consequently announced a significant loosening of the existing restrictions starting on January 22nd.

In December, the start of the COVID-19 vaccinations in major economies and news of a stimulus package in the U.S. supported investors’ sentiment towards a global recovery and appetite for riskier assets, which strengthened emerging market currencies, including the ruble. Higher oil prices provided additional support to the ruble. In December, the ruble continued to appreciate with respect to the U.S. dollar, gaining 3.9 percent, m/m (Figure 3). The BOP data reveal modest net inflows of capital from non-residents to the OFZ market in 2020Q4 (US$1.5 billion) compared to net outflows of US$0.5 billion in the third quarter. The ruble strengthening rolled over to the first half of January despite the resumption of FX currency purchases in the fiscal rule framework by the Ministry of Finance. According to the Ministry’s estimate, during December 2020 – January 2021, fiscal oil and gas revenues would exceed base oil and gas revenues by 106.3 billion rubles (US$1.4 billion), which would result in daily purchases of FX currency of about US$96.5 million from January 15 – February 4, 2021.
According to the CBR’s preliminary estimates, in 2020, the current account (CA) registered a surplus of US$32.5 billion, about half of the surplus in 2019 (US$64.8 billion). In 2020, Russia faced a sizable negative terms of trade shock due to oil prices dropping by about 32 percent, lower global demand for most exported products and services, elevated uncertainty, and significant financial markets volatility. While imports of goods and services dropped (by 14.5 and 35.9 US$ billion, respectively) on the back of the REER depreciation, GDP contraction, and restrictions on travel, this could not compensate for the drop in the value of energy exports (-US$90 billion) and services export (-US$17.4 billion). The non-energy goods export value remained resistant to the crisis induced by the pandemic, largely due to higher exports of gold (with the CBR halting its purchases of gold for international reserves in April 2020, and thus releasing higher volumes of gold for exports) (Figure 4). Higher export values of wheat, vegetable oil, rolled iron, and copper supported non-energy exports as well. Export and import of travel services dropped the most in percentage terms. An improved investment income balance also supported the current account (investment income payments decreased with the REER depreciation and lower profits). Net private capital outflows grew to US$49 billion, compared to US$22.2 billion in the previous year. A fall in the external liabilities of the banking and non-banking sectors drove net capital outflows. Elevated uncertainty and lower reinvestment of profits wiped out incoming FDI, which decreased to US$6.3 billion, down from US$22.6 billion last year. International reserves dropped by US$14.9 billion in 2020, largely due to FX sales in the fiscal rule framework and public debt payments. With the downward pressure on export receipts, financial markets volatility, elevated uncertainty, and elevated geopolitical risks (especially in 2020Q3), the REER depreciated by 7.5 percent, y/y; however, the REER adjustment to lower oil prices in 2020 could have been much more severe without the fiscal rule.

Household consumption drove a resumption of economic activity in the third quarter, with all the other components of domestic demand registering a contraction on q-o-q basis. While GDP contracted in 2020Q3 by 3.4 percent, y/y, compared to the second quarter, in quarter on quarter terms, economic activity somewhat resumed (+2.8 percent, saar, q/q) as COVID-19 cases declined, restrictions eased, and government support measures (fiscal, monetary, and regulatory) positively affected incomes and firms’ solvency. Household consumption dropped by 8.4 percent, y/y, (vs -22.2 percent, y/y, in 2020Q2) and expanded by 38 percent, q-o-q, saar. With elevated uncertainty persisting and companies’ balance sheets suffering, gross fixed capital formation continued contracting in Q3. The OPEC+ agreement and weak global demand weighed on export dynamics. In Q2, Russia outperformed the EU, which experienced a double-digit contraction with a slump in gross fixed capital formation.
and exports contracting more severely than in Russia. In the third quarter, the EU performance was similar to Russia’s: -4.3 percent, y/y, vs -3.4 percent, y/y, suggesting a stronger pick-up in the EU on quarterly basis.

**Economic performance improved in November.**

**Industrial production strengthened in December (Figure 5).** In November, output in five basic economic activities contracted by 2.3 percent, y/y, compared to 4.1 percent, y/y, in October. This was due to the stronger performance of industrial production (namely manufacturing) and agriculture. In November, output in manufacturing expanded by 1.1 percent, y/y, after contracting by 3.7 percent, y/y, in the previous month. Growth in chemicals, wood products, and textiles supported this expansion. Output in agriculture contracted by 2.1 percent, y/y, but it was better than in October (-6.6 percent, y/y). Lower harvests of some vegetables continued to weigh on the sector’s performance. In December, industrial production output grew by 1.5 m-o-m, sa (-0.2 percent, y/y). This was due to stronger performance in manufacturing (+4.4 percent, y/y), especially in transportation equipment and medical products. Higher public spending was one of the factors which supported manufacturing performance. OPEC+ agreement continued to weigh on mineral resource extraction, which dropped by 8.5 percent, y/y. In December, PMI in services (48) pointed to contraction at the same rate as in October.

**Figure 5. The slump in domestic demand weighed down on GDP growth in the second quarter of 2020**

**Inflation continued to be influenced by an increase in food prices (Figure 6).** In December, the annual headline consumer price index (CPI) inflation reached 4.9 percent compared to 4.4 percent in November. The acceleration of food inflation contributed the most to the growth of headline CPI, increasing to 6.7 percent, y/y, (compared to 5.8 percent, y/y, a month before). The growth of food inflation resulted from the ruble’s depreciation, higher global food prices, and a lower harvest for some agriculture items and contributed the most to the growth of the headline CPI. The government has responded to the surge in food prices by introducing price caps and export quotas. While these measures are politically attractive, they are also distortive. A better approach would be to use targeted social assistance to deliver relief to the most vulnerable segments of the population. Non-food inflation increased to 4.8 percent, y/y, up from 4.5 percent, y/y, in the prior month. Meanwhile, low inflation in services on the back of subdued demand amidst COVID-19 restrictions contain the growth of the headline CPI inflation. Inflation in services slightly increased to 2.7 percent, y/y, up from 2.5 percent in November. In December, the core CPI stood at 4.2 percent, y/y, (compared to 3.9 percent in November). In 2020, the average CPI inflation posted 3.4 percent, y/y, in line with our expectations.

In December, developments around inflation expectations were mixed. Household inflation expectations were on an upward trend (increasing to 11.5 percent compared to 10.1 percent in November)—mainly due to the increase in food prices. Price expectations of corporates decelerated to 19 percent (down from 20.4 percent in the previous month) — due to the ruble strengthening and weak demand.
Inflation continued to be influenced by an increase in food prices.

Figure 6: Inflation continued to be influenced by an increase in food prices

Labor market dynamics slightly improved in November. The unemployment rate showed improvement, decreasing to 6.1 percent (sa), compared to 6.2 percent in October. The number of unemployed people fell to 4.6 million from 4.7 million a month earlier, and those officially registered declined to 3.1 million versus 3.5 million in October. The real wage growth decelerated, increasing by 0.5 percent, y/y, in October (2.2 percent, y/y, in September). Overall, the cumulative growth for the ten months was 2.4 percent, y/y.

Figure 7: In November, the unemployment rate showed improvement

In 2020, the federal budget registered a deficit of Rub4.1 trillion (3.8 percent of GDP), compared to a surplus of Rub1.9 (1.8 percent of GDP) billion in 2019.

This was on the back of higher spending driven by the response to the spread of the pandemic and the need to support the economy amidst lower oil/gas revenues. In 2020, oil/gas revenues dropped by 33.9 percent, y/y, as energy prices plummeted and energy production decreased. Non-oil tax receipts, helped by the ruble’s depreciation, stayed at about the same level as in 2019, dropping in real terms by 2 percent. Total fiscal revenues decreased by 9.1 percent, y/y, (12.5 percent, y/y, not accounting for the one-off channeling of the receipts from the Sberbank purchase). Government measures aimed at fighting the COVID-19 pandemic and mitigating its economic impact led to a primary expenditures increase of 26 percent, y/y, (+4.6 trillion RUB), driven mainly by growth in spending on social policy (+2.4 trillion RUB, y/y), national economy (+1 trillion RUB, y/y), and health (+0.8 trillion RUB, y/y). Compared to the pre-pandemic plans, primary expenditures grew by about 3.4 trillion rubles (3.3 percent of GDP). With the COVID-19 pandemic being the main challenge in 2020, spending on National Projects reached 55 percent of the planned amount by end-September, yet it accelerated in the last months of 2020 and totaled 97.4 percent by year end. The federal budget deficit was largely financed by borrowing in the domestic market. In 2020, the federal government ruble denominated debt grew by Rub4.6 trillion, amounting to Rub14.8 trillion (14.3 percent of GDP). This debt was purchased largely by domestic investors, as the share of non-residents in government bonds dropped to 23.7 percent at the end of November, compared to 31.9 percent in the same period in 2019.

On December 22, 2020, the U.S. adopted new sanctions against 45 Russian companies deemed “military end users”. The sanctions restrict exports of certain goods and technology to these companies. The list of companies includes, but is not limited to the Ministry of Defence, Rosoboronexport, Russian Aircraft Corporation MiG, Sukhoi Civil Aircraft, Tupolev JSC, Public Joint Stock Company United Aircraft Corporation, and Russian Helicopters JSC.

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2 Cash basis

3 Not accounting for one-off channeling of the receipts from the Sberbank purchase.
Banks’ key credit risk and performance indicators remained largely stable, supported by the CBR’s regulatory forbearance measures (Figure 8). As of November 1, 2020, the aggregate capital adequacy ratio stood at 12.3 percent (against a regulatory minimum of 8 percent). Non-performing loans slightly declined to 9.3 percent of total loans from 9.5 percent a month remained largely unchanged at 9.3 percent before as banks benefited from the regulatory forbearance measures, which delay the accrual of loan loss reserves on restructured loans. The banking sector profitability has been affected by the pandemic: from January-November 2020, the banking sector’s net profit remained substantially lower than in 2019, standing at Rub1.4 trillion, (or US$19.5 billion) compared to Rub1.9 trillion (US$28.8 billion) in the same period in 2019 due to increasing loan loss provisioning. Consequently, the return on assets (ROA) and return on equity (ROE) were 1.7 percent and 15.8 percent, respectively, compared to 2.1 percent and 19.1 percent at the beginning of the year.

In November, both household and corporate sector lending growth slowed down somewhat but given the limited pandemic-related restrictions and the continuation of the government’s credit support programs, positive credit growth continued. Credit to households in rubles grew by 0.7 percent, m/m, and 13.9 percent, y/y, versus 1.9 percent, m/m, and 14.7 percent, y/y, in October. Some slowdown in retail lending could be attributed to the increased uncertainty due to the worsening pandemic situation. Mortgage lending, largely driven by the government’s subsidized mortgage lending program, remains the major contributor to household credit growth. Credit growth to the corporate sector in rubles continued to grow, although at a slower pace, increasing by 0.5 percent, m/m, in November versus 1 percent, m/m, in October. In annual terms, corporate lending has been growing at 10.1 percent, y/y, (after adjusting for FX changes).

In December, demand from borrowers, both households and corporates, for the restructing of their loans decreased. Although the application period for payment holidays for individuals and SMEs ended on September 30th— this was adopted as an extraordinary crisis support measure—, the CBR extended its recommendation to financial institutions to restructure loans of individuals and SMEs facing a deteriorating financial situation due to the pandemic until March 31, 2021. For the period March 20th to December 29th, 2020, banks restructured 1.8 million loan agreements of individuals, amounting to about Rub860 billion. The volume of corporate restructured loan debt exceeded Rub5.1 trillion for the period March 20th to December 1st (14.4 percent of the total portfolio of the systemically important credit organizations, excluding SMEs). The total amount of restructured SME loans reached Rub853.5 billion, or over 15 percent of the total portfolio of SME loans as of December 29th. In particular, 50.3 percent of the total number of the restructured SME loans accounted for wholesale and retail trade enterprises, 16.8 percent for transportation and storage and 10 percent for hotels and catering. Overall, the total volume of restructured loans amounted to more than Rub6.8 trillion -- about 10 percent of the loan portfolio.

Figure 8: Key credit risk and banking performance indicators remained stable
In its analytical work, the World Bank uses official statistics of the Russian Federation.

By relying on these data, the World Bank does not intend to make any judgment on the legal or other status of the territories concerned or to prejudice the final determination of the parties' claims.