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Expert Commentary

UBS economists on Russian economy and Ruble

” ***Russia is not in a fiscal crisis, but the fiscal balance is nonetheless expected to continue deterioration.***

The current drop in oil prices suggests that the country's economy is currently facing a deep recession. Do you agree with this view? What reforms should be introduced to prevent the economy going deeper into crisis?



Russia's well-known external challenges are likely to continue in the near term. As such, we think any 2016 recovery will be subdued at best, and medium-term prospects are weak.

Russia is not in a fiscal crisis, but the fiscal balance is nonetheless expected to continue deterioration. The mildly expansionary fiscal stance of the 2015 budget was justified in light of the recession, according to the IMF. In the medium term however, we think more fiscal consolidation is required. Changes to the fiscal rule, which change the oil price benchmark from the current backward-looking mechanism, would be a positive development.

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The type of fiscal spend also matters; we estimate 44% of Russia's fiscal outlays are related to defence and social services. According to Rosstat data, about a quarter of employment is in what one can broadly define as "public sector" – government administration, defence, education and healthcare. This year's wage freeze for federal employees provided some limited fiscal relief and also lowered the inflation outlook through lower public sector wages in real terms.

Capital flight may slow now that the Ruble has stabilized, but "de-offshorisation" would nonetheless help net FDI inflows. For these inflows to occur, we think further structural reforms, including support for SMEs and tax reform, would be necessary. Though still in surplus, Russia's declining current account balance also poses challenges at a time when low domestic savings pressure the balance of payments.

According to the IMF, Russian officials agree that increasing labour participation, strengthening property rights, revamping transport infrastructure and enhancing competition in goods and services markets are needed.

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” ***In spite of low inflation, the CBR continues to show to take a cautious approach to policy normalization, gradually easing following the 650 bps rate hike in December 2014.***

Due to the already mentioned oil prices decline, more experts all over the world expect further depreciation of the Russian Ruble against the Greenback. What is your opinion on the matter?

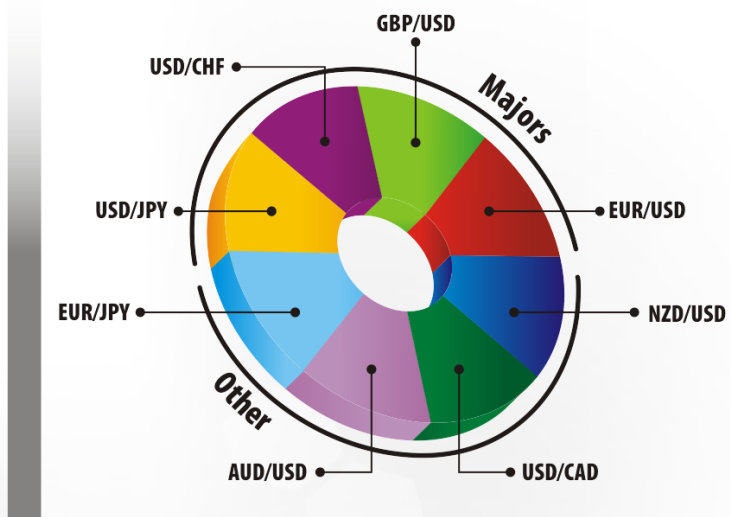


We are definitely not optimistic on further performance of the Russian Ruble; however, on the positive side, the Central Bank has managed to stabilize the currency. Similarly, the financial sector has been stabilized following the implementation of a capital support program in December 2014. In spite of low inflation, the CBR continues to show to take a cautious approach to policy normalization, gradually easing following the 650 bps rate hike in December 2014.

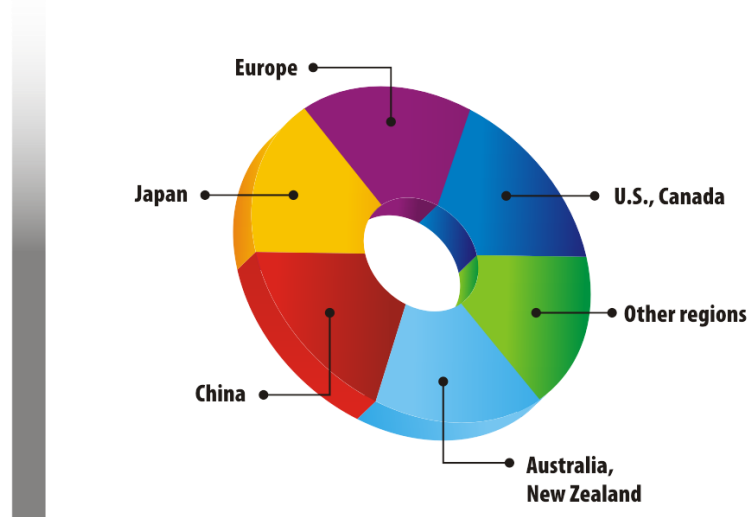
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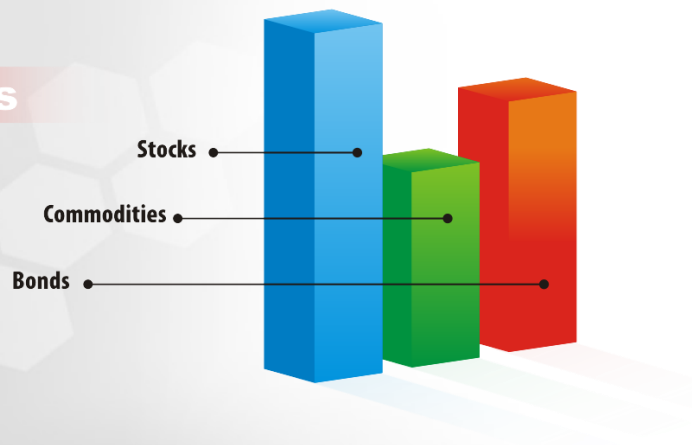
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