21 April 2016

Flash Comment

Russian output and demand: cautious stabilisation

- **Russia's output buoyed around zero.**
- **Private consumption still weak but stabilising.**
- **We see upside risks to our 2016 GDP forecast.**

Assessment and outlook

Russia's economy continues to hover in a deep frost, while the base effect signals that the bottom is already behind us. The oil price rebound, RUB strengthening and decreased volatility are bringing some relief for Russia's macro indicators. The Brent price has recovered 55.6% y/y since its low point in January 2016, while the Russian currency is up 25.4% against the USD providing private consumption with a reprieve.

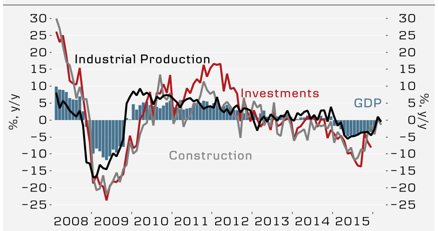
March 2016 output and demand data show clear signs of stabilisation, while the development of macro indicators continues to be L-shaped and we expect a recovery in late H2 16. The fall in industrial production was -0.5% y/y in March, after a 1.0% expansion in February, as the leap year effect was positive. Yet, seasonally adjusted monthly data show positive growth in industrial production in early 2016. The demand side remains weak because of the negative real wage growth and low consumer confidence despite slowing inflation (7.3% y/y in March 2016 versus 16.9% y/y in March 2015). Real wages shrank by 3.0% y/y, which is still weighing on retail sales and is stabilising on the base effect. It confirms our view that the bottom on the demand side was reached in Q4 15. Yet, given the current environment of a relatively low oil price, inflation risks and shrinking real income, we do not expect consumer demand to expand before Q3 16 at the earliest.

On the output side, good news continues to flow from the agricultural sector, which grew by 2.8% y/y in Q1 16, expanding 3% y/y in 2015, as Russia's countermeasures regarding food imports boosted local supply. Food production was up 3.2% y/y in Q1 16. While manufacturing continued to shrink (-3.1% y/y in Q1 16), chemical production grew 3.0% y/y and machinery and equipment production grew 5.1% y/y (+13.1% y/y in March), as the weak RUB continues to support local producers.

The labour market surprised slightly on the negative side, as unemployment ticked up to 6.0% in March from 5.8% a month earlier, hitting its three-year high as the country is entering the second consecutive year of recession for the first time in more than 20 years. The weaker RUB and flexible labour market are protecting the majority of jobs, while real wages collapsed and benefits have been slashed widely.

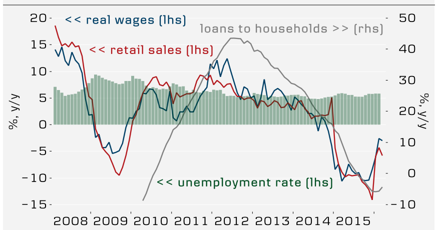
According to our base-case scenario, we expect Russia's economy to shrink by 2.1% y/y in 2016 on the assumption the Brent average price stays at USD31/bl as crude futures were pricing in mid-January 2016 (USD36.4/bl YTD). As the crude average continues to improve, we see upside risk to our base-case scenario forecasts, while we estimate growth will remain in negative territory this year.

Russia's macro indicators remain negative



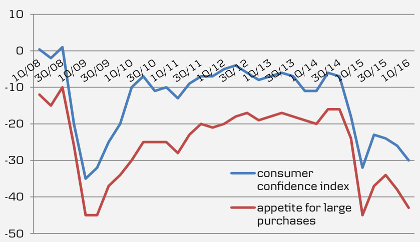
Source: Macrobond Financial, Danske Bank Markets

Consumer demand is frozen deeply...



Source: Macrobond Financial, Danske Bank Markets

...as private consumers remain pessimistic



Source: Rosstat,, Danske Bank Markets

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This research report has been prepared by Danske Bank Markets, a division of Danske Bank A/S ('Danske Bank'). The author of the research report is Vladimir Miklashevsky, Analyst.

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