RUSSIA

Highlights

- **The Covid-19 pandemic has dealt a serious blow to the economy.** The collapse of the price of oil, which accounts for a major share of Russia's exports, has exacerbated the situation.
- **Russia's strong macroeconomic situation entering the crisis has helped to limit the damage.** Several years of conservative macroeconomic policies to protect the economy in the face of international sanctions mean it is well placed to weather external shocks.
- **A comprehensive recovery plan is being implemented.** The plan includes a range of measures to strengthen the health system, support households, small and medium-sized enterprises (SMEs) and large-scale investments. However, the timetable for broader, medium-term national development goals and projects has been extended.

Key priorities for 2021

- **Efforts to diversify away from commodity exports should be intensified.** A renewed focus is needed on investing in technology and digitisation of the economy in order to improve the competitiveness of non-military sectors, such as manufacturing, agriculture and services.
- **Further reforms to improve the business environment are needed.** Priorities include reducing the state's role in the economy, addressing physical infrastructure gaps and implementing business-friendly measures to enhance private-sector competitiveness.
- **Planned public investments need to be well targeted to contribute to growth.** The delayed timetable for the National Projects partly reflects challenges in implementation. In this regard, key priorities include coordination among public institutions and inclusion of stakeholders in the planning and implementation phases of public investments.

Main macroeconomic indicators %

	2016	2017	2018	2019	2020 proj.
GDP growth	0.2	1.8	2.5	1.3	-4.5
Inflation (average)	7.1	3.7	2.9	4.5	3.2
Government balance/GDP	-3.7	-1.5	2.9	1.9	-3.5
Current account balance/GDP	1.9	2.0	6.9	3.8	1.2
Net FDI/GDP [neg. sign = inflows]	-0.8	0.5	1.4	-0.6	0.0
External debt/GDP	40.1	32.9	27.3	28.9	n.a.
Gross reserves/GDP	29.5	27.5	28.1	32.7	n.a.
Credit to private sector/GDP	53.1	52.1	50.9	52.4	n.a.

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Covid-19: macroeconomic implications

Before the Covid-19 pandemic, the Russian economy was in a relatively strong position. At the end of the first quarter of 2020 the trade, current and fiscal accounts were all in surplus, and inflation was at an historical (post-Soviet) low. This was largely thanks to several years of conservative macroeconomic policies, including an overhaul of the budget, which gave rise to a much lower breakeven oil price of US$ 42.45 per barrel, the introduction of a fiscal rule that helped lower the rouble's sensitivity to oil price fluctuations, and the adoption of a flexible exchange rate. In early 2020 the government announced a RUB 2.1 trillion (US$ 27 billion) social spending package to support real incomes. It also pledged to push the 12 National Projects, a US$ 400 billion investment aimed at modernising and revitalising Russian society, the implementation of which had been behind schedule.

The Covid-19 pandemic hit both the supply and demand side of the economy. The global nature of the crisis led to a plunge in the prices of oil and gas, key exports for Russia. The main effects of these shocks were a drop in consumption, driven by a two-month lockdown of the entire economy, a significant fall in external demand for commodity exports, and supply chain bottlenecks. The economy contracted by 8.0 per cent year-on-year in the second quarter of 2020, but activity started to pick up again in the third quarter, as did oil and gas prices.

Foreign reserves have increased despite the economic downturn. By September 2020 the level of reserves exceeded US$ 600 billion. This contrasts sharply with previous crises, and can largely be explained by the flexibility of the exchange rate. Although the cost of the recovery plan has turned the budget surplus into a deficit, this has been funded by profit received by the central bank of Russia (CBR) from the sale of Sberbank shares and the placement of domestic rouble debt. The government has not so far needed to tap the National Wealth Fund (NWF), which stood at US$ 176 billion as of September 2020.

A recovery is expected in 2021. Overall, the economy is expected to shrink by 4.5 per cent in 2020, followed by a rebound of 3.0 per cent in 2021. This forecast is subject to significant upside and downside risks, depending on the path of oil prices, the possibility of a second wave of the pandemic, and the outcome of several geopolitical issues.

Policy response to Covid-19

A comprehensive recovery plan is in place. The National Plan for Economic Recovery, adopted in June 2020, is the government's programme to help the economy recover after the Covid-19 shock subsides and oil prices increase. It runs for 18 months, costs RUB 6.4 trillion (US$ 83 billion) and consists of 500 programmes. Some of these programmes overlap with the National Projects. Combined with measures introduced to address the immediate impact of Covid-19, this makes a total of RUB 7.2 trillion (US$ 93 billion) of support, or 7 per cent of GDP. Of this, RUB 5 trillion (US$ 65 billion) is budgetary funds (spending and missing revenues) and RUB 2.2 trillion (US$ 28 billion) is reserved for infrastructure investment. The funds foresee social support, of which the prime goal is to stabilise income trends, increase employment and liberalise and deregulate labour relations. A special section targets SMEs via offers of tax relief, grants and subsidies. There is also a section covering investment, the digital economy and import substitution, largely repeating what was in the National Projects goals.

Large investment projects remain a key part of the recovery and development plan. Once the impact of Covid-19 subsides, the heart of the government's structural reform programme remains the US$ 400 billion National Projects scheme, comprising key development targets for the period 2019-24 in the social, economic and environmental sectors.

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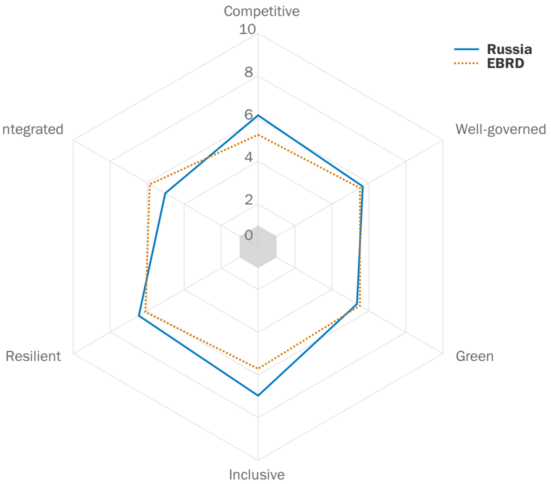
Assessment of transition qualities (1-10)



Structural reform developments

Following the constitutional amendments of July 2020, the President signed a decree that outlines a new set of national development goals for Russia. Instead of a National Projects-style roadmap of state-driven investment across 12 major areas, the new goals are less specific, and the timeline for completion has been extended from 2024 to 2030. Five development goals are outlined: maintain population, health and wellbeing; create possibilities for self-fulfilment and development of talents; a comfortable and safe living environment; effective labour and successful entrepreneurship; and digital transformation.

Local content provisions have expanded. One element of the government's import substitution strategy in recent years has involved the use of domestic content rules, notably in the electronics and information technology sectors, the segments of the economy in which Russia has one of the most broad-ranging and ambitious import substitution goals. In September 2020 the Russian Ministry of Industry and Trade proposed further changes to Decree 719 which regulates local content requirements for various industries and which applies to procurement by the public sector and state-owned enterprises.

Tax collection has improved drastically in recent years thanks to a digital overhaul of the Federal Tax Service. In recent months several further changes have been introduced which will help boost revenues. A progressive tax to apply above the 13 per cent flat tax has been proposed which will impact Russia's wealthier taxpayers. The mineral extraction tax has been increased, applicable to companies that mine metals, ores and rock used to make fertilisers, and all double taxation agreements are currently being reviewed, which would result in withholding tax being payable on dividend and interest payments by residents of the countries concerned.