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Central Bank of the Russian Federation



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Information
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commentary

Economy

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Economy: facts, assessments and comments

(July 2018)

In the second quarter of 2018, annual GDP growth stood at 1.8%, which is consistent with the lower bound of the Bank of Russia's estimate (1.8-2.2%). In July, economic performance proved weaker than expected. This is associated with industrial production and investment dynamics. Industrial output showed mixed data across sectors. On the one hand, the output of engineering products contracted, which may be attributed to the effect of short-term factors, among other things. On the other hand, metallurgical output recovered; production and sales of consumer goods continued to increase at a moderate pace as real wages and consumer lending showed positive dynamics. Given the above, there is no substantial reason to revise the GDP forecast. The Bank of Russia will assess the balance of short- and long-term factors' effect on economic performance as new data are released.

Economy in July 2018 (year-on-year growth, %, unless indicated otherwise)

	2017	2018 Q1	June 2018	2018 Q2	July 2018
Output of goods and services by key industries	2.4	2.3	1.5	3.0	2.8
Industrial output	2.1	2.8	2.2	3.2	3.9
Agricultural output	2.4	2.6	0.9	1.9	0.9
Freight turnover	5.5	2.4	2.1	3.4	4.0
Construction	-1.4	-4.0	-1.3	0.9	-0.7
Retail trade turnover	1.3	2.4	3.0	2.7	2.5
Unemployment rate* / seasonally adjusted**	5.2	5.1/4.8	4.7/4.8	4.8/4.8	4.7/4.8
Nominal wage	6.7	12.7	9.7	10.1	10.7
Real wage	2.9	10.2	7.2	7.6	8.0

* As % of labour force.

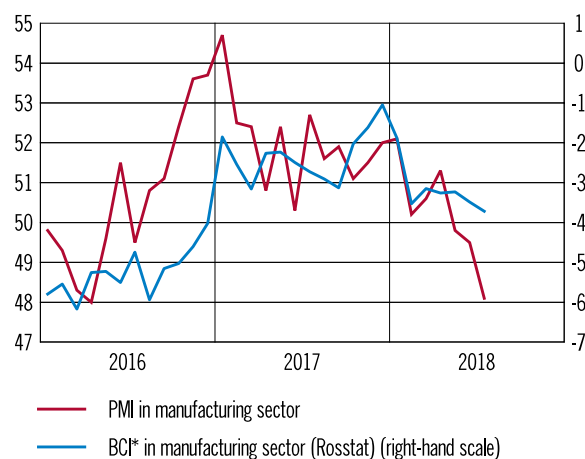
** Bank of Russia estimate.

Source: Rosstat.

According to Rosstat's preliminary estimate, **2018 Q2 GDP growth totalled 1.8% YoY**. This is consistent with the Bank of Russia's estimate (1.8-2.2%) released in the June commentary on the economy.¹ **Output growth was largely triggered by expanding external demand both for domestic intermediate and investment goods and services.** In particular, catering and certain types of transport and hotel services registered faster turnover growth due to the FIFA World Cup. As a result, the Bank of Russia's estimates² suggest that export quantities increased by 6.8%. Domestic demand, partially covered by imports, expanded moderately. The Bank of Russia's growth estimates for final consumption expenditure of households and

Chart 1

Surveys suggest that companies' expectations deteriorate



* Business Confidence Index.
Sources: Rosstat, IHS Markit.

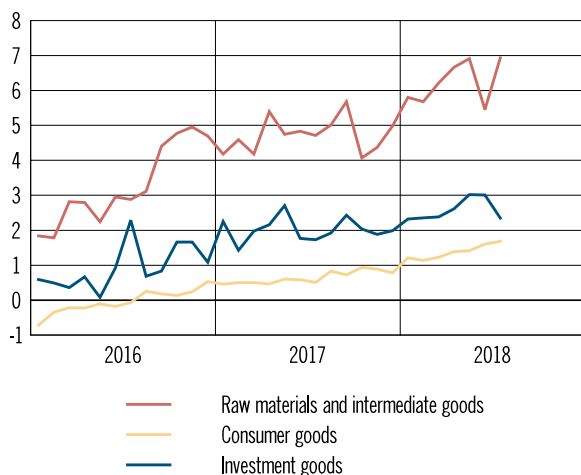
¹ Economy, No. 6 (30), June 2018.

² Data by the FCS and the Bank of Russia.

Chart 2

Investment output declined unexpectedly

Growth as % on 2013, seasonally adjusted



Sources: Rosstat, Bank of Russia calculations.

gross fixed capital formation remained unchanged at 3.0-3.5% and 2.5-3.5% respectively.

Economic activity indicators undershot the Bank of Russia's expectations in July. However, this gives no grounds for forecast revision. Industrial output remained unchanged compared to the previous month's readings (adjusted for seasonality and calendar effects) as growth was expected to be weak.

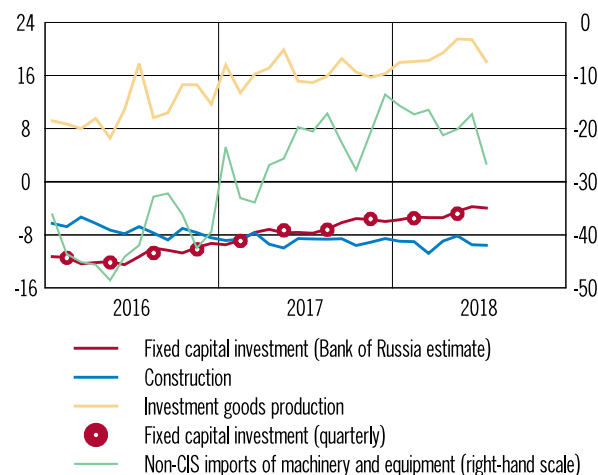
Having said that, certain components of industrial production demonstrated unstable dynamics. In particular, after a considerable drop in non-ferrous metallurgy output in previous months, production saw an almost complete recovery in July. At the same time, engineering output contracted pronouncedly. The output of mechanical equipment (engines and bearings), motor vehicles (lorries and buses) and other vehicles were the main contributors to production decline in this product category. This may be attributed to, among other things, a temporary suspension in some companies' operations because of the FIFA World Cup and modernisation of some production lines. Given the short-term nature of these factors, the engineering output may be expected to recover in the future.

The output of construction materials is affected by mixed factors. On the one hand, growth in the output is largely supported by external demand. The period between May 2017 and May 2018 saw a sizeable hike in exports of various construction materials (including glass, cement and artificial

Chart 3

Investment activity dropped in July

Growth as % on January 2014, seasonally adjusted



Sources: Rosstat, FCS, Bank of Russia calculations.

stone products) to CIS countries. On the other hand, stagnating construction has contained output dynamics in this product category.

The ongoing decline in construction works and the contraction of investment goods imports due to, among other things, the ruble depreciation point to **weaker than expected investment activity** in July 2018.

The dynamics of industrial production and investment activity may also have been affected by companies' deteriorating sentiment, as suggested by PMI and Rosstat surveys. In particular, the PMI index in manufacturing has been falling for the third straight month. Respondents note a shrinking volume of new orders and slack demand from both domestic and foreign customers.

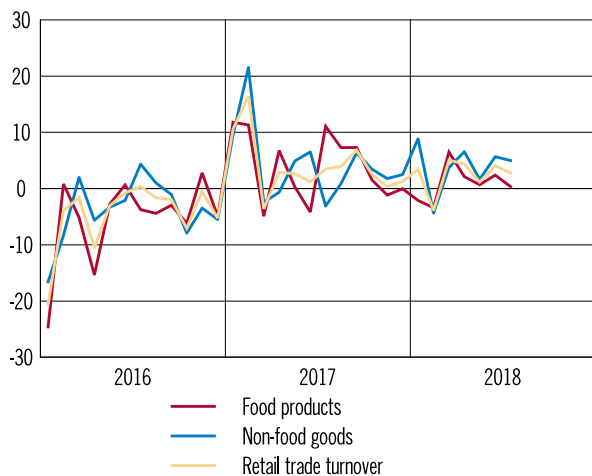
As statistics are released, the Bank of Russia will be able to determine with greater precision whether these factors have a significant effect on economic activity. Also, the Bank of Russia will consider the need to update its forecasts.

Consumer demand continued to grow at a moderate pace in July without posing excessive proinflationary pressure. Retail trade turnover was up in July both on a month-on-month (seasonally adjusted) and year-on-year basis. Consumer demand was boosted in July 2018 by positive movements in real wages and a steady increase in consumer lending.

On the backdrop of July's rising demand, **companies intensified the output of consumer goods.** Having said that, both production and sales

Sales of non-food goods showed the most pronounced growth

Annualised monthly growth, %, seasonally adjusted



Sources: Rosstat, Bank of Russia calculations.

Chart 4

of non-food goods showed faster growth than food products. This may have been partially associated with football fans' elevated demand for souvenirs, clothes and sportware.

The Q3 annual GDP growth forecast was revised downwards from 1.5-2.0% to 1.3-1.7% taking into account the actual Q2 dynamics. That said, the Q3 GDP forecast remained unchanged compared to the previous quarter, adjusted for seasonality and calendar effects. The forecast 2018 GDP growth rate remains at 1.5-2.0%.

Cut-off date – 30 August 2018.

A soft copy of the information and analytical material is published on the Bank of Russia website (<http://www.cbr.ru/DKP/>).

Please send your comments and suggestions to svc_analysis@cbr.ru.