Bank of Russia

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ECONOMY

Information and analytical commentary

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Economy: facts, assessments and comments (February 2019)

In February 2019, economic activity continued to expand. The economy is close to its potential. Annual growth of industrial production stepped up on the back of the calendar effect, among other things. Output increased across a wide range of production sectors. As predicted by the Bank of Russia's forecast, growth in annual retail sales declined in January-February as a result of the VAT increase and a slowdown in wage growth. Current consumer demand movements and labour market conditions create no excessive inflationary pressure. Investment activity indicators demonstrated unstable and mixed dynamics in early 2019. Given the high base effect, estimated fixed capital investment in January-February 2019 held below the level seen in the same period last year. Estimates suggest that annual GDP growth will come in at 1-1.5% in 2019 Q1 and 1.2-1.7% as of the year-end.

CORE ECONOMIC INDICATORS *Table 1*
(growth, % YoY, unless indicated otherwise)

	December 2018	2018 Q4	2018	January 2019	February 2019
Output of goods and services by key industry	1.9	2.5	2.9	0.2	...
Industrial output	2.0	2.7	2.9	1.1	4.1
Agricultural output	-0.1	4.1	-0.6	0.7	1.0
Construction	2.6	4.1	5.3	0.1	0.3
Freight turnover	3.2	2.3	2.8	2.4	1.7
Retail sales	2.3	2.7	2.6	1.6	2.0
Unemployment rate / seasonally adjusted* (% of labour force)	4.8/4.7	4.8/4.8	4.8	4.9/4.7	4.9/4.7
Nominal wage	7.3	8.1	9.9	6.1	6.0
Real wage	2.9	4.1	6.8	0.2	0.7
Household real disposable money income	0.1	-1.1	-0.2	-1.3	–

** Bank of Russia estimate.*
Source: Rosstat.

Production activity

In February 2019, production activity expanded. Annual industrial production growth accelerated in February to 4.1% from 1.1% seen in January (Charts 1 and 2). This was in part caused by the calendar effect[1] which, according to estimates, contributed 0.6 pp to annual output growth. Industrial production also expanded month on month, adjusted for seasonality and calendar effects (SA) (according to Bank of Russia estimates, growth stood at 1%). Output increased across a wide range of production sectors.

Raw material production. Mining and quarrying increased in February 2019 month on month (SA), largely on the back of an expanded gas production amid faster growth in external demand and the launch of Yamal SPG natural gas liquefaction facilities. That said, oil production, as expected, continued its downward trend as oil exporters delivered on updated agreements.

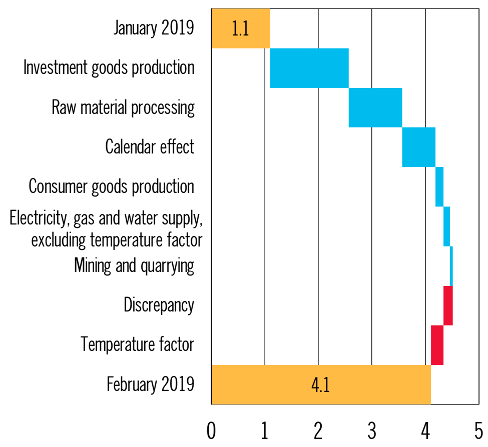
Intermediate goods production. In February, the production of raw material processing products grew further month on month (SA) largely on the back of stable growth in metal and oil product output. Estimates suggest that the output of oil products (petrol and fuel oil) increased mainly to meet domestic demand.

Investment goods production. Recovery growth (month on month, SA) was registered in February 2019 in the output of investment goods (Chart 3). This offset, in part, the contraction of production in this segment in the

[1] *Substitute holidays in May instead of February 2019.*

DECOMPOSITION OF CHANGES IN INDUSTRIAL PRODUCTION *Chart 1*

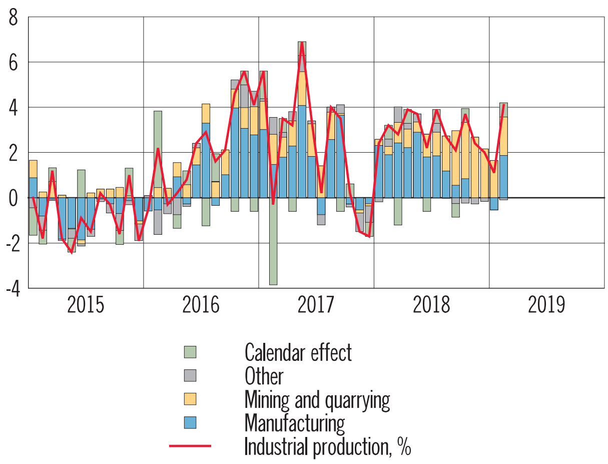
Contribution to annual growth, pp



Sources: Rosstat, Bank of Russia calculations.

INDUSTRIAL PRODUCTION *Chart 2*

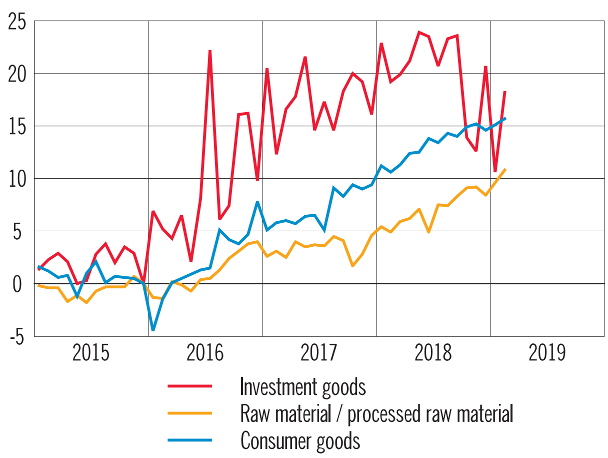
Contribution to annual growth, pp



Sources: Rosstat, Bank of Russia calculations.

INDUSTRIAL PRODUCTION BY PRODUCT GROUP *Chart 3*

Growth on December 2015, % SA



Sources: Rosstat, Bank of Russia calculations.

previous month. The output of these products has remained volatile and exposed to specific factors.

Consumer goods production. In February 2019, monthly growth of food production accelerated (SA). This was, in part, driven by the development of competitive factories. Thus, since August 2018, the output of processed potato-based products rose after the launch of a Lipetsk Region-based French fries factory and import substitution in this product category.

The production of non-food consumer goods shrank in February (month on month, SA) mainly because of textile output figures. The production of other non-food goods, including durables, in contrast, turned to growth after a January drop (SA) that reflected slowdown in consumer demand.[2]

Business survey. In February 2019, both industrial producer surveys and statistics pointed to output growth. Respondents to the IHS Markit (PMI) survey noted that production volumes had accelerated growth. The Bank of Russia-conducted company monitoring suggests that the economic situation improved in manufacturing, energy and trade companies. Business sentiment improved in all federal districts.

That said, PMI data suggest that growth of new orders, including exports, slowed down. Under these circumstances, speculations about stable acceleration of industrial production growth would be premature. The production dynamics of a wide range of products remain unstable and exposed to short-term fluctuations associated, among other things, with specific factors. Given the above, the annual industrial production growth rate will hold in 2019 Q1 at the previous quarter's level (2.5-3.0%), according to estimates.

Investment activity

Such investment activity indicators as the output of investment goods and machine building imports continued to show mixed and rather unstable dynamics in February 2019

[2] *See the previous issue of Economy, information and analytical commentary (No. 1, January 2019).*

(Chart 4). On the one hand, machine building output rose against the January readings (SA). On the other hand, its output shrank considerably. Construction works held at the previous month's level (SA). Given the high base of the beginning of last year and the unstable dynamics of indirect indicators, fixed capital investment in January-February 2019 held below the level seen in the same period last year.

Consumer activity

In early 2019, consumer activity remained moderate. Retail sales held in February at the previous month's level (SA, Chart 5). The indicator's low annual growth rates in January-February 2019 developed amid slowing nominal wage growth (see the *Labour market* section) and temporary inflation acceleration. A considerable contraction was registered in the sales of light vehicles (Chart 6) where annual price growth accelerated by 1.1 pp in January-February 2019 compared with late 2018.[3]

Household surveys also point to moderate consumer activity. According to inFOM data, in February-March 2019, the consumer sentiment index and the estimation of the favourableness of this time period for large purchases lagged considerably behind the average readings registered at the beginning of last year.

The Bank of Russia's estimates suggest that in this environment annual growth of retail sales will come in at 1.5-2.0% in 2019 Q1.

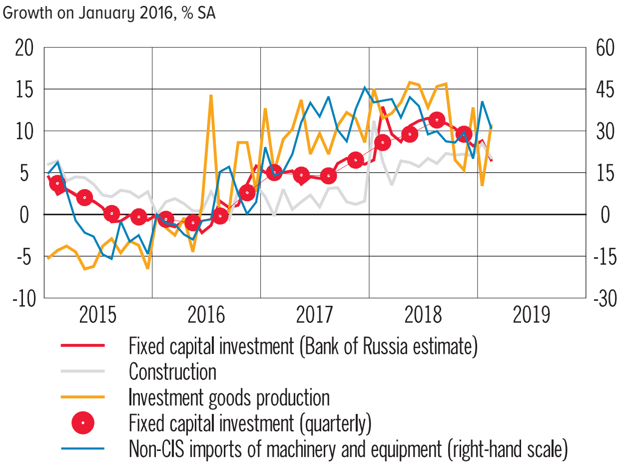
Labour market

According to the Bank of Russia's estimates, the labour market held close to the equilibrium in February 2019. Unemployment held at 4.7% SA (Chart 7), which is close to an inflation neutral level. Demographic factors[4] coupled with positive employer sentiment held unemployment at a low rate. According to a

[3] *The acceleration of car price growth resulted, among other things, from the VAT rate hike and the upward revision of excise taxes. For details of the effect of the excise tax revision on inflation in 2019, see the December issue of the Monetary Policy Report.*

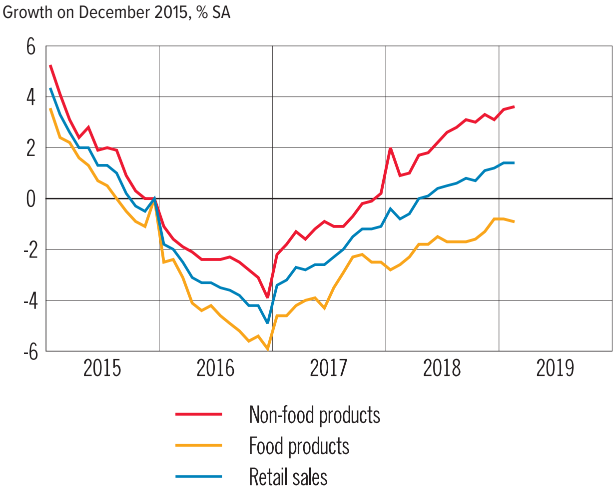
[4] *The bulk of the labour force includes population groups where unemployment rates are the lowest.*

INVESTMENT ACTIVITY INDICATORS *Chart 4*



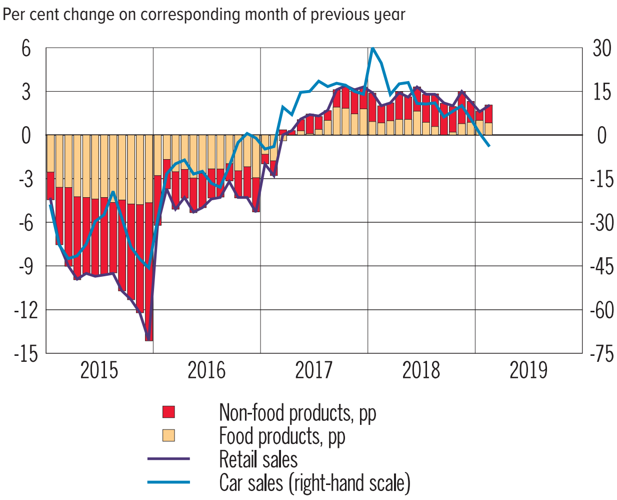
Sources: Rosstat, FCS, Bank of Russia calculations.

RETAIL SALES *Chart 5*



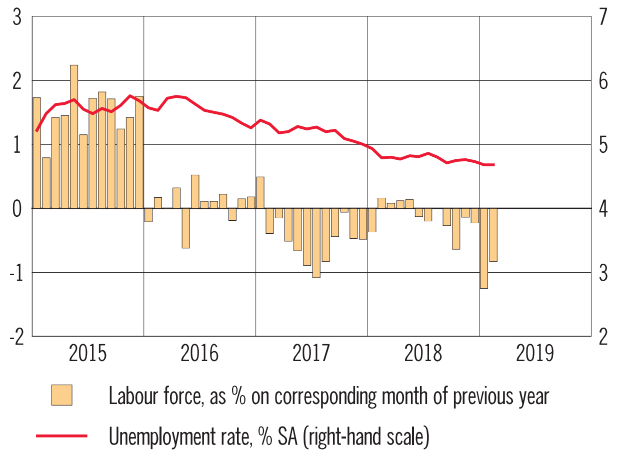
Sources: Rosstat, Bank of Russia calculations.

RETAIL SALES AND CAR SALES *Chart 6*



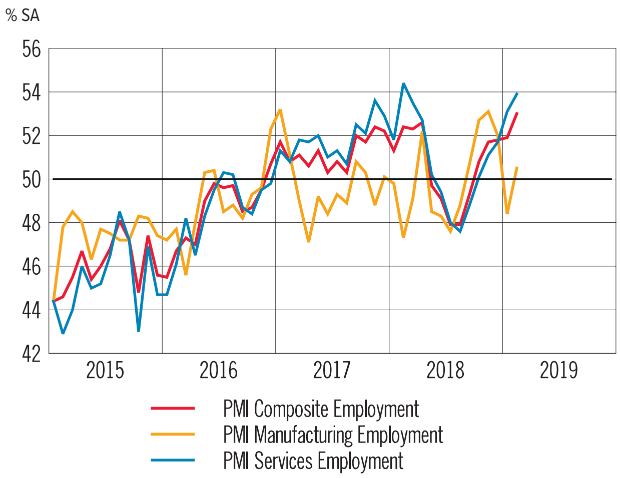
Sources: Rosstat, Association of European Businesses, Bank of Russia calculations.

UNEMPLOYMENT AND LABOUR FORCE *Chart 7*



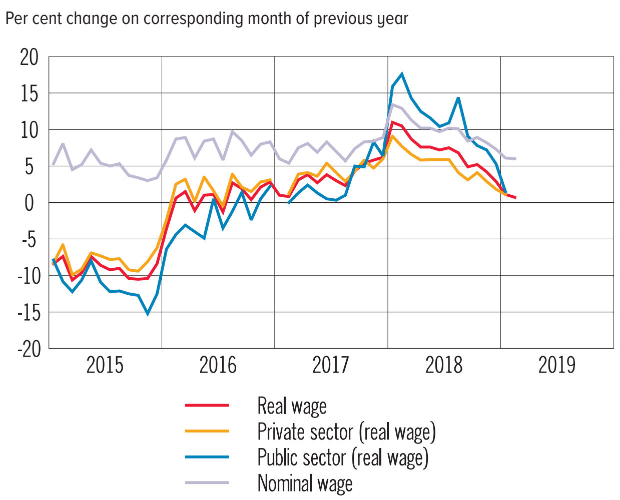
Sources: Rosstat, Bank of Russia calculations.

PMI IN EMPLOYMENT *Chart 8*



Source: IHS Markit.

WAGES *Chart 9*



Sources: Rosstat, Bank of Russia calculations.

manufacturing and service company survey, the composite PMI index in employment reached 53% SA in February 2019, which is close to the high reading of early 2018 (Chart 8).

Nominal wage growth continued to slow down. According to Rosstat estimates, in February 2019, it rose by 6.0% YoY (Chart 9). The decline in the annual wage growth rates from 7.3% seen in December was explained by the base effect: labour remuneration of public sector employees and culture workers was raised most dramatically in 2018 Q1. This coupled with inflation acceleration to influence real wages where annual growth slowed to 0.7%, the 18-month low.

Forecast

Economic activity in February 2019 was overall in line with the Bank of Russia's expectations. The economy is close to its potential. Projections for the annual final consumption expenditure of households and gross fixed capital formation in 2019 Q1 come in at 1.0-1.5% as before. Annual GDP growth estimate for 2019 Q1 remained overall unchanged at 1.0-1.5%. In 2019, GDP growth is still forecast at 1.2-1.7%.[5]

[5] *The medium-term Bank of Russia forecast released in the follow-up to the Board of Directors policy meeting of 22 March 2019.*

Cut-off date – 22 March 2019.
A soft copy of the information and analytical commentary is available on the Bank of Russia website (http://www.cbr.ru/DKP/).
Please send your comments and suggestions to svc_analysis@cbr.ru.
This commentary is prepared by the Monetary Policy Department.
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