Bank of Russia

TALKING TRENDS
Economy and markets

Research and Forecasting Department Bulletin

APRIL 2024

CONTENTS

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Executive summary

Monthly summary

- The Russian economy demonstrated a steady upward trend in January–February and will likely continue to expand in March, as evidenced by high-frequency indicators and survey results. The industrial sector, wholesale and retail trade, and public catering showed the most significant growth rates. Increasing economic activity is pushing up the demand for labour resources, intensifying companies' competition for personnel and supporting the fast rise in wages. People have sufficient incomes to both save and expand consumption. Consequently, the easing of inflationary pressure in the economy and the consumer sector is slow, although monetary conditions are tight. To bring inflation back to the target, it is necessary to maintain tight monetary conditions for an extended period.
    - Consumer demand is still high. Alongside rising incomes, high demand is also driven by rapidly expanding car and unsecured consumer lending. The growth rates in these segments remain elevated, despite higher credit rates and the toughening of the macroprudential regulation. This might become a reason for a further surge in prices at a pace above 4% in annualised terms.
    - In March, the monthly growth of consumer prices decelerated notably. However, the slowdown was largely associated with one-off disinflationary factors in certain goods and services markets. The measures of underlying inflation are declining slowly, staying elevated. The accumulated deviation upwards from the price growth path that would return inflation to 4% as of the end of the year equalled 0.5 percentage points in 2024 Q1.
    - The recent data on the balance of payments show that exports significantly expanded in March, whereas imports remained unchanged overall. Accordingly, the current account surplus reached the highest level since the end of 2022.
    - Sentiment in the Russian financial markets was mostly positive in March. Nevertheless, bond yields still price in a high inflation risk premium. The equity market was expanding. The exchange rate remained stable. However, due to the time lags related to transportation and payment processing, earnings from exports that increased in March will be influencing the foreign exchange market only in the next few months.

In focus. Proinflationary risks in labour market: cross-country comparisons

- Nominal wage growth in a number of emerging market economies is close to its multi-year highs, which is far above the pre-COVID levels. An important cause behind the increased growth rate is the structural transformation of economies at large and labour markets in particular in the COVID and post–COVID periods.

- In some countries, above all, those in Central and Eastern Europe (CEECs), unfavourable labour supply trends led to a significant wage growth acceleration starting in late 2020 and a subsequent rise in inflation. Moreover, the pace of wage growth remained elevated in 2023, generating substantial proinflationary risks. Countries with a favourable demographic situation and low dependence on migrant labour saw a more moderate and temporary wage and inflation rise.
- Structural changes which the Russian economy has undergone in recent years have given rise to, among other things, increasingly tighter labour market. An imbalance between demand and supply in the labour market creates prerequisites for sustainable wage increases outstripping labour productivity growth. This factor can lengthen the lags of tight monetary policy transmission to changes in demand and price movements.
- The Bank of Russia's monetary policy decisions will help to gradually bring the pace of aggregated demand growth further in line with the potential of supply expansion in the economy, ensuring the return of inflation to the target in 2024 and its subsequent stabilisation at around 4%. As part of this process, it is important to continue implementing a set of macroeconomic policy measures seeking to reallocate labour to more efficient companies and enhance overall labour productivity.

1. Inflation

Consumer price growth slowed in March after its stabilisation in January–February, but chiefly due to one-off factors.[1] These factors somewhat diminished monthly price rises compared with growth in the prices of the most stable consumer basket's components, which remains elevated. While the overall disinflationary trend continues, it is so far not as pronounced as March's consumer price index shows.

Why was the significant easing of inflationary pressure in late 2023 not followed by a similar continuation in early 2024? Our analysis suggests that Q3 2023, when the fastest rate of current price rises was registered, saw a concurrence of strong proinflationary factors on the side of demand and supply alike. In particular, it was this period which saw the most rapid rises in costs, as reported by respondents in various polls. The cost growth significantly slowed towards the year end, substantially easing the proinflationary impact of demand-side factors. The proinflationary effect of demand-side factors also abated, although not as significantly, given the continued strong expansion in demand. Therefore, for the ongoing seasonally adjusted consumer price growth to sustainably slow to 4% in annualised terms, demand needs to slow more significantly.

The rate of and factors behind consumer price rises indirectly suggest a *moderately* tight monetary stance, despite the high nominal interest rates. This degree of tightness is sufficient for a gradual price rise slowdown but does not ensure its rapid deceleration. That said, the ongoing consumers and produces' adaptation to the rising interest rates amid the continuing fiscal stimulus may give new impetus to demand growth, which will likely outstrip supply expansion potential in the short term. In this environment, we may see a pronounced inertia of the ongoing elevated rate of price growth.

1.1. Sustainable price growth of around 4% is yet to take shape

- Seasonally adjusted price growth slowed in March relative to January–February, coming closer to the target (in annualised terms). The analytical indicators of price movements were mixed but overall they suggest that inflationary pressure remains elevated. It is, therefore, too early to claim that prices have reached a sustainable path corresponding to an annual inflation rate of 4%.
- Household and business inflation expectations continue to slide overall but remain elevated. The decline of inflationary pressure is gradual and requires a tight monetary stance to be maintained for a long time.

Consumer price growth tangibly slowed in March, coming close to a level corresponding to an inflation rate of 4%, standing at 4.5% MoM SAAR, down from 6.3% MoM SAAR in January–February (Figure 1). The price growth slowdown is largely driven by one-off factors:

[1] One example of this is a faster than seasonably normal significant decline in some fruit and vegetable items.

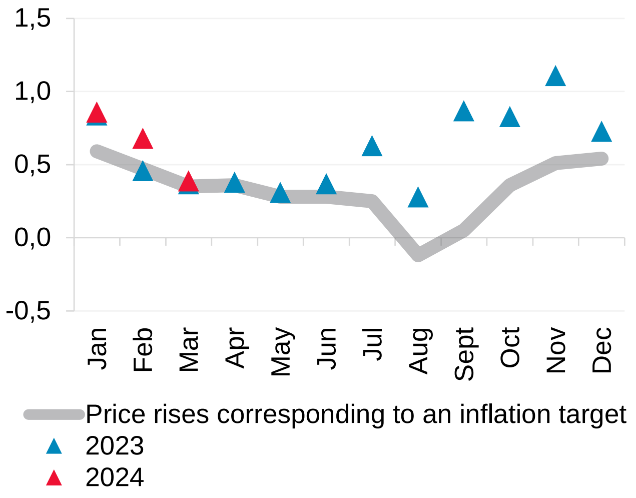
a significant downward deviation of fruit and vegetable prices from the normal seasonal pattern and a slowdown in the rise of services' volatile component after its spike in February. Rises in the prices of the consumer basket's most stable components slowed but not so much as the overall price growth, staying above 4%. Annual inflation remained at February's level at 7.7% (Table 1).

Table 1. Inflation and its components

	Mar. 2022	Mar. 2023	Jan. 2024	Feb. 2024	Mar. 2024
% YoY					
All goods and services	**16.7**	**3.5**	**7.4**	**7.7**	**7.7**
Core inflation	**18.7**	**3.7**	**7.2**	**7.6**	**7.8**
Food	18.0	2.6	8.1	8.1	8.1
Non-food goods	20.3	0.1	6.2	6.6	6.7
Services	9.9	9.7	8.1	8.5	8.3
% MoM SAAR					
All goods and services	**140.1**	**4.2**	**6.3**	**6.3**	**4.5**
Core inflation	**179.0**	**2.8**	**6.7**	**6.8**	**6.1**
Food	115.4	0.6	5.4	2.8	1.3
– net of fruit and vegetables	**89.7**	**0.8**	**5.3**	**5.4**	**5.2**
Non-food goods	258.8	1.5	6.1	3.2	3.1
– net of refined petroleum products	**331.5**	**1.6**	**6.1**	**3.8**	**3.2**
Services	61.1	13.0	7.6	15.2	10.9
– net of housing and communal services	**104.5**	**17.5**	**10.2**	**20.3**	**13.0**

Sources: Rosstat, R&F Department estimates.

Figure 1. Price rises corresponding to an inflation rate of 4%, % MoM



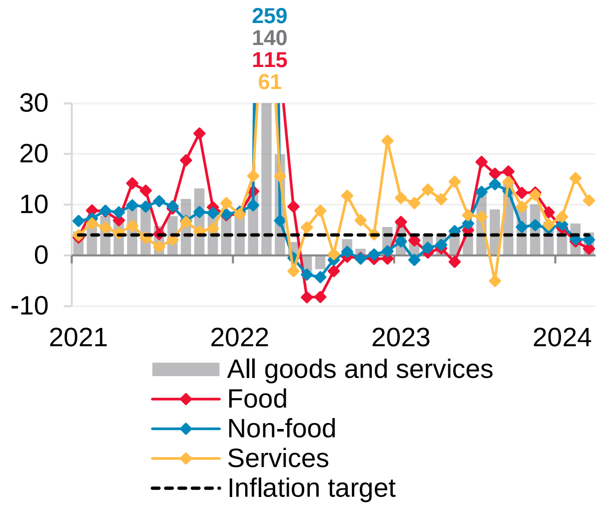
Sources: Rosstat, R&F Department estimates.

Food prices went up just 1.3% MoM SAAR in March, helped by a fruit and vegetable price decline at a faster rate than seasonally normal, thanks to, among other things, a rise in the output of greenhouse vegetables and banana imports. Net of this category, food price rises slowed just marginally to 5.2% MoM SAAR from 5.4% MoM SAAR.

Food price growth remains the most volatile of all large components. After a sharp price rise acceleration in Q3, driven by a concurrent increase in demand and constraints on supply, the disinflationary trends in food price movements became the most visible as supply-side problems were dealt with and demand growth slowed (Figure 4). The disinflationary impact of animal husbandry product prices is, however, gradually abating. March saw a resumed acceleration in the meat product price rises: the elevated rate of price growth may be underpinned by robust domestic demand and export expansion, with world prices rising. Growth in milk and dairy product prices also gained momentum, due to, among other things, hikes in minimum export prices of dairy products from Belarus.

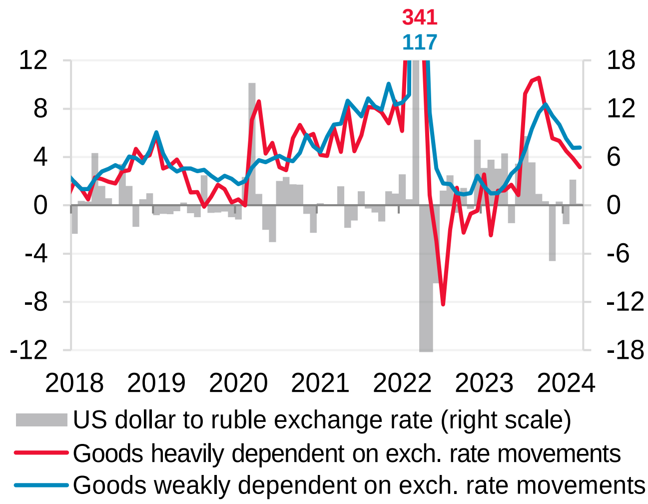
Price rises remain moderate in the non-food segment at 3.1% MoM SAAR after 3.2% MoM SAAR a month earlier. The strongest restraining impact came from a temporary price cut for a car brand whose manufacturer introduced sizeable discounts for cars produced in 2023. The discounts and a rise in the car disposal fee as of 1 April 2024 helped car dealers to dispose of surplus stocks built up last year. Car dealers are expecting price to moderately rise in the short term due to the forecasted cooling of demand.

Figure 2. Seasonally adjusted price growth, % MoM SAAR



Sources: Rosstat, R&F Department estimates.

Figure 3. Median CPI (% MoM SAAR) and US dollar to ruble exchange rate (%)



Sources: Bank of Russia, Rosstat, R&F Department estimates.

Rises in the prices of other non-food goods on average accelerated. Fuel prices started to climb modestly. Despite the petrol production contraction, deliveries to the domestic market are being maintained by inventories, with the damaged facilities being gradually restored and caps on exports imposed. Exchange (wholesale) fuel prices substantially rose, but the damper mechanism will be restraining further price hikes.

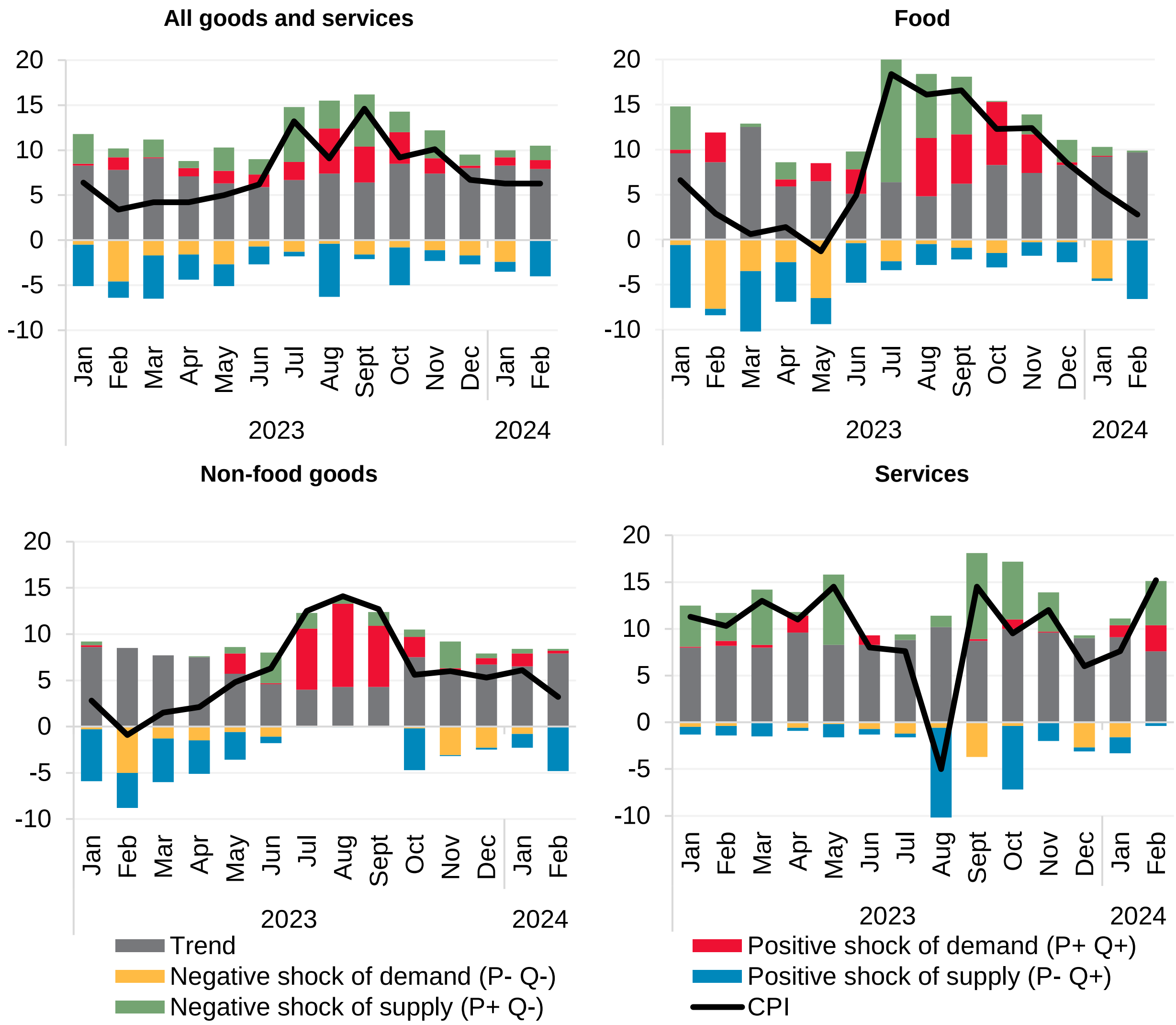
The pace of price increases in services slowed to 10.9% MoM SAAR down from 15.2% MoM SAAR in February. This was due to dynamics in air and rail transport services, as well as in foreign tourism, which accounted for February's price surge. Meanwhile, domestic tourism prices notably rose, driven chiefly by travel to Russia's Black Sea coast. Net of the above components, the pace of services price hikes remains elevated at 6.1% MoM SAAR after 7.5% MoM SAAR a month earlier. The fastest price growth was posted in the services of arts, entertainment and recreation organisations, personal and health care services, with the regulated segment playing a restraining role.

The impact of the ruble exchange rate on consumer price movements remains neutral overall. The price growth median in the group of goods highly sensitive to the ruble exchange rate is still staying somewhat below that of the groups of goods showing low sensitivity to the exchange rate (Figure 3).

Analytical indicators of price movements showed mixed changes in March. The mean of the modified core inflation estimates was all but unchanged in March at 4.5% in annualised terms (Figure 5). The median of price growth distribution slightly declined to 5.12% MoM SAAR from 5.41% MoM SAAR in February, but stays above 4% in annualised terms for all enlarged components. That said, the weight of items rising in price at an accelerated pace (above 4% in annualised terms) ceased to decline, which also suggests a significant input of some items to the ongoing price growth slowdown (Figure 6).The trend inflation estimate went up to 7.18% from 7.09% in February. Thus, despite a notable slowdown in the ongoing price growth, inflationary pressure remains elevated in the stable components.

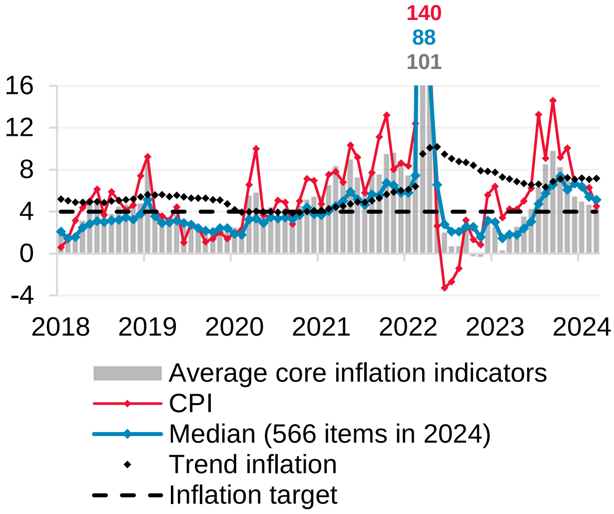
Inflationary pressure began to ease much more slowly in Q1 2024 than in late 2023, staying generally elevated relative to the Bank of Russia target. The input of supply factors to price growth sharply fell in late 2023 (Figure 4) (a temporary disinflationary supply-side effect seems to have also emerged in the goods segment at the start of 2024). The proinflationary effect of demand factors also diminished but less significantly, given the continuing sizeable demand expansion. This stalled the disinflation process. Therefore, for the ongoing seasonally adjusted consumer price growth to sustainably decelerate to 4% in annualised terms, demand expansion needs to slow further.

Figure 4. Price growth decomposition, % MoM SAAR



Sources: Rosstat, Sapova, Kharlamova (2023), R&F Department estimates.

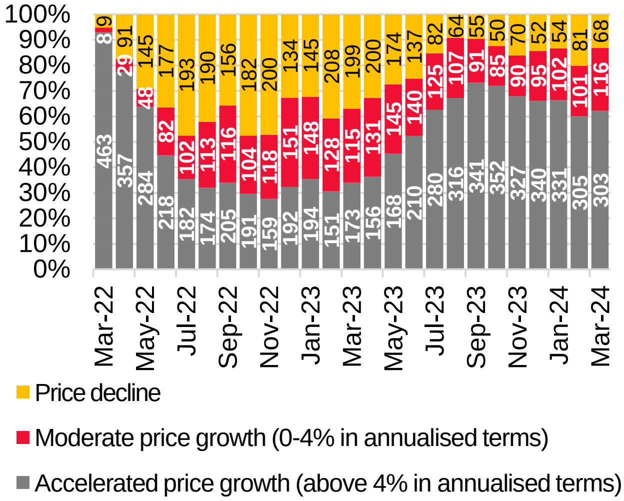
Figure 5. Modified core inflation indicators* (% in annualised terms) and trend inflation estimate (%YoY)



** Indicators are computed using the method of excluding the most volatile components and the truncation method.*

Sources: Rosstat, R&F Department estimates.

Figure 6. Aggregate weight of goods and services* distributed based on seasonally adjusted price growth



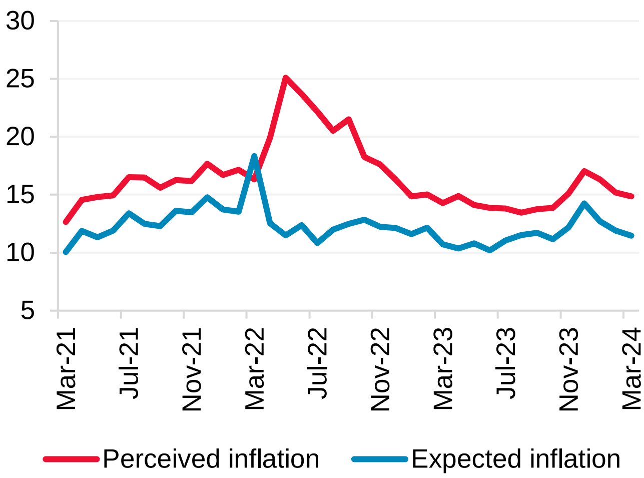
**Net of fruit and vegetables and regulated services.*

Note. The figures represent the number of items.

Sources: Rosstat, R&F Department estimates.

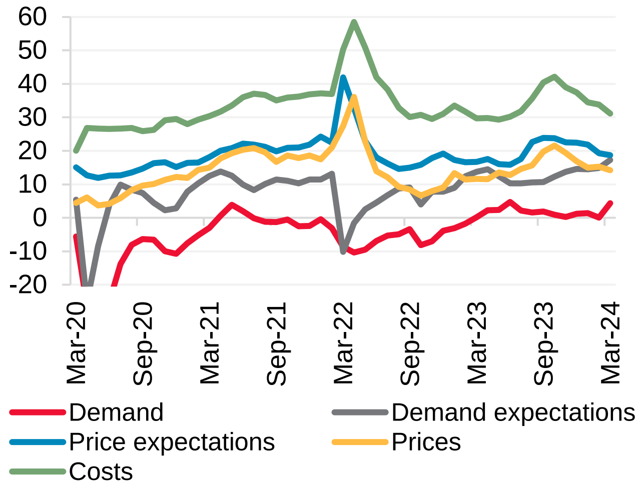
Despite the easing of inflationary pressure, a sustainable disinflationary trend propelling price growth to a trajectory close to 4%, is yet to take shape. Household inflation expectations continued to decline in March but remained close to the high levels of the autumn of 2023 (Figure 7). Firms' price expectations corrected down for the economy at large amid a cost growth slowdown (Figure 8). Meanwhile, pressure from producer prices on retail prices rose.

Figure 7. Household inflation perceptions: median readings, annual percentage change



Source: InFom.

Figure 8. Business survey data for the economy at large, pp, SA



Source: Bank of Russia.

2. Economic performance

Q1 2024 saw the Russian economy continue to grow, probably at an even faster rate than in Q4 2023. One exception was the fuel industry, which scaled down production for various reasons unrelated to domestic demand. The sources of growth are consumer and government demand, as well as some recovery of non-oil and gas exports. As a result, the labour market became even tighter, with nominal wage growth accelerating, based on January's data (although it seems to have been in part due to bonuses for the year).

Russia's overall positive economic performance for the 2022–2024 period was driven by the impact of several factors.

First, a rise in budget expenditure as fiscal rule parameters changed. The oil price level in the calculation of base oil and gas revenue was dramatically raised from 46 USD/bbl in the initially approved 2022 budget to 60 USD/bbl in 2024.

Second, as in the acute COVID period, part of household demand turned out to be "locked" inside Russia due to a dramatic complication of foreign travel logistics and a sizeable rise in its prices. This stimulated household demand for domestic tourism, public food services, durable goods, and housing.

Third, import substitution generates additional demand for intermediate and investment goods and services. Demand for domestic production factors rises, the share of gross capital formation in GDP increases.

All of these factors will likely have a long-term effect. Therefore, increased domestic demand will continue. At the same time, it becomes increasingly difficult for these factors to drive further economic growth due, in particular, to budget constraints. Therefore, growth will likely slow to more sustainable levels going forward, regardless of monetary policy to be pursued.

2.1. No signs of economic growth slowdown at the start of the year

- A quarterly estimate of 2023 GDP growth released by Rosstat has borne out a slight economic growth slowdown at the end of the year. We estimate that in Q1 2024 economic activity expansion continued at a comparable rate or even accelerated, with the economy continuing to deviate upwards from the balanced growth trajectory. This is, in particular, evidenced by core industries' output (Figure 9), survey-based business activity indicators,[2] and an array of other real-time metrics.
- Most industries meeting domestic demand are showing sustainable growth. Manufacturing output is gaining pace, while the mining and quarrying sector is stagnating (Figure 11). At the same time, manufacturing's growth is still highly volatile and varies across the sector's individual industries (Figure 12).

[2] The Bank of Russia's Business Climate Indicator hit an all-time high, industrial optimism reached the highest level since 2022 (Sergey Tsukhlo's surveys), while the PMI Manufacturing hit a 18-year high.

- This is, in particular, true of output in a broad spectrum of industries in the *investment goods* group. Growth in the output of fabricated metal products, machinery and equipment,[3] and non-metallic mineral products was in part offset by an output drop in the manufacture of computer, electronic and optical products, and other transport equipment (except for passenger cars). The *intermediate goods* industries saw an output fall in the manufacture of refined petroleum products offset by strong results in the manufacture of basic metals. The pace of output expansion in the group of *consumer goods* industries remains stable, with the manufacture of food products and motor vehicles restraining growth.
- Consumer demand continues to rise at a fast pace. Month-on-month retail sales growth accelerated to a twelve-month high of 1.4% MoM SA in February from an average of around 1% MoM SA over the previous months (Figure 13). The complication of logistics along with rising prices of foreign travel prompted a reorientation of a large part of consumer demand to domestic tourism,[4] services and Russian durable goods, thus providing additional stimulus for domestic demand as household income grows.
- It appears from real-time indicators that consumer expenditure still shows no signs of sustainable growth slowdown. The cooling of consumer activity is contained by the rising labour market tightness[5] (Figure 15, Figure 16), accompanied by growth in current real wages (Figure 14) and households' confidence regarding their future labour income[6] (Figure 17). Consumer sentiment indices are hitting new highs (Figure 19). The savings ratio growth (Figure 20) to its highest levels (exclusive of its surges on the back of restrictions imposed during the COVID pandemic) is accompanied by an increase in the propensity to make major purchases.
- As appears from across-the-board optimism of respondents in surveys varying in the composition of samples (SMEs, PMI, Bank of Russia's Business Climate Indicator, Sergey Tsukhlo), entrepreneurs positively assess orders prospects. That said, the capabilities of supply expansion still lag demand. Potential for further unemployment reduction is minor (Figure 18) and may fail to meet a record rise in jobs.[7]

[3] Those not included in other groups.

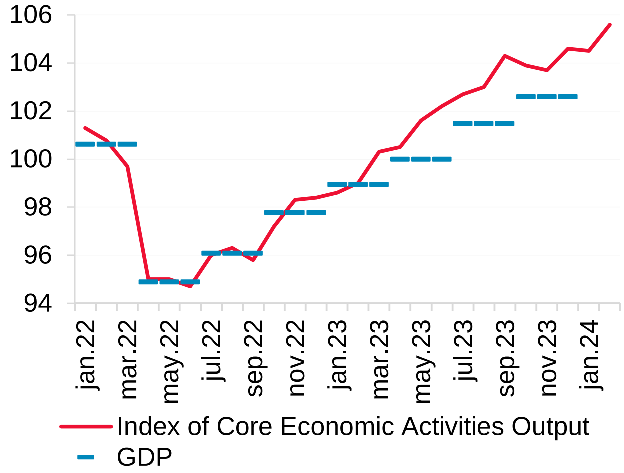
[4] Incoming payments in the provision of short-term accommodation services (hotels) in Q1 were 36% above the Q1 2023 level.

[5] The rate of unemployment and a gap between labour demand and supply are at all-time lows (2.8% SA and 50 thousand people SA in February, respectively). The HeadHunter Index declined in March by 0.16 pp in seasonally adjusted terms to 3.2 pp SA, which is also an all-time low.

[6] Growth in optimism is further fuelled by the announced expansion in social support measures, supplemental pay increases and a raise of health care workers' base salaries, set forth in the RF President's address to the Federal Assembly.

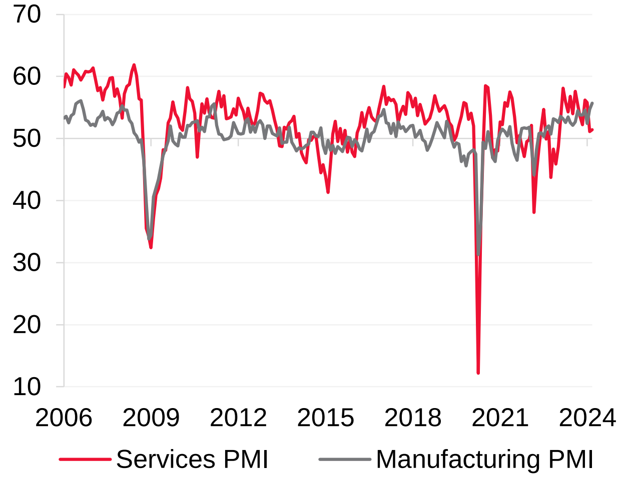
[7] According to a PMI poll, the rate of job creation was the fastest in 24 years in March.

Figure 9. Core economic activities output and GDP, Q4 2021 = 100[8]



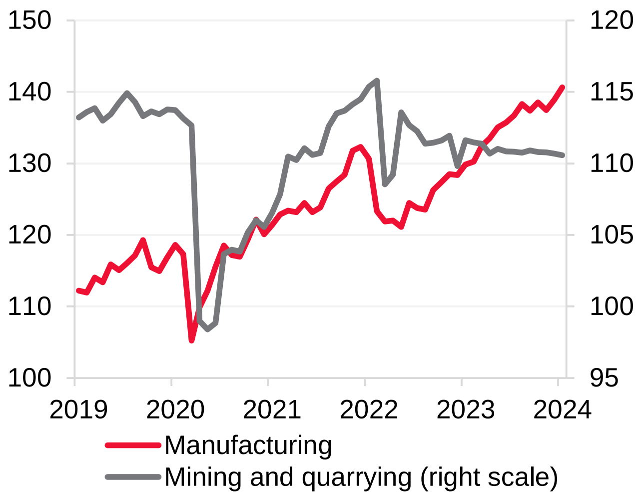
Sources: Rosstat, R&F Department estimates.

Figure 10. Russia's Manufacturing and Services PMI, points



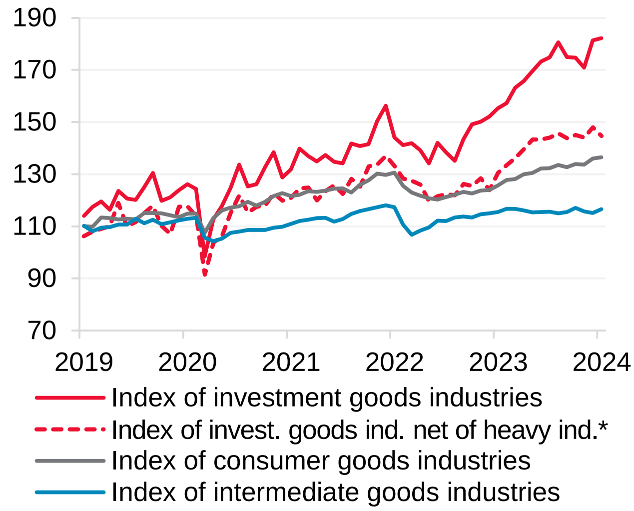
Source: S&P Global.

Figure 11. Mining and quarrying and manufacturing indices (2014 = 100), SA



Sources: Rosstat, R&F Department estimates.

Figure 12. Output in groups of manufacturing industries, SA, 01.2016 = 100%[9]

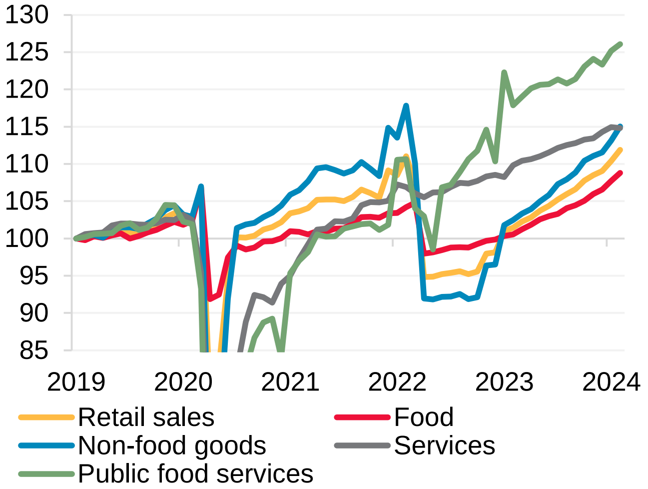


Sources: Rosstat, R&F Department estimates.

[8] The estimate from the Indicator of Core Economic Activities Output (ICEAO), net of agriculture's input in September–November is calculated based on an aggregated indicator reproducing the ICEAO in the composition and performance and including seasonally adjusted output growth in other industries relative to the preceding month.

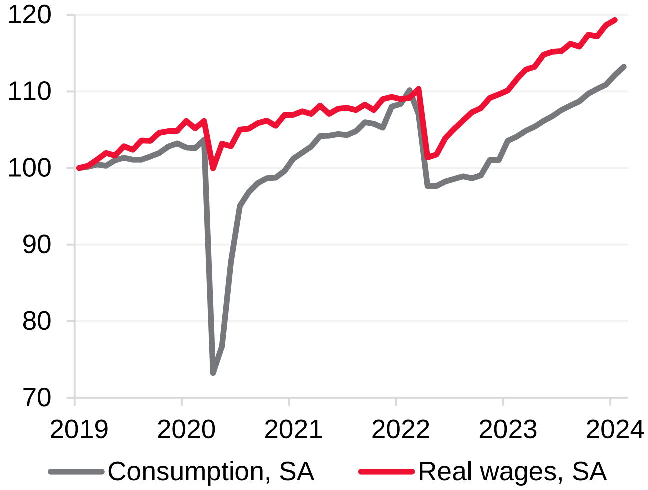
[9] The "heaviest" industries mean the manufacture of prefabricated metal products, except machinery and equipment and other transport and equipment, which account for the heaviest weight in the structure of the investment goods group.

Figure 13. Retail sales, sales of the paid services segment and public food services, 01.2019 = 100, SA, %



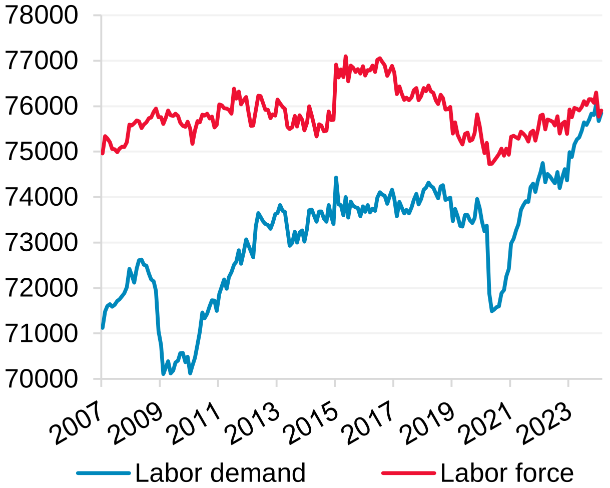
Sources: Bank of Russia, Rosstat, R&F Department estimates.

Figure 14. Proxy indicator of consumption (sum of retail, services and public food service' sales) and real wages, 01.2019 = 100, SA, %



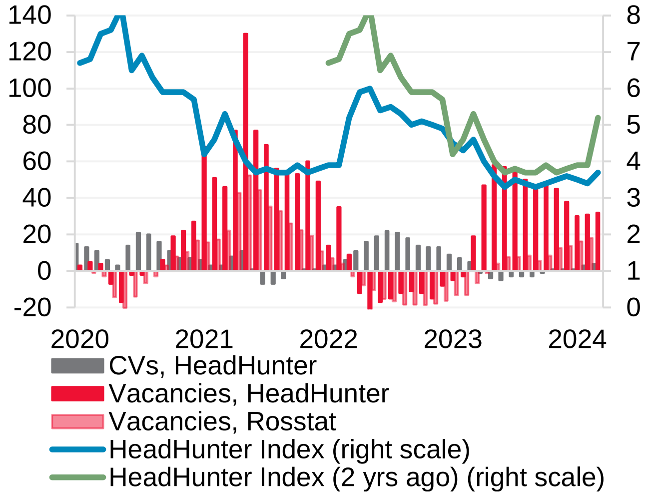
Sources: Rosstat, R&F Department estimates.

Figure 15. Labor force and demand for labor, thsd people, SA



Sources: Rosstat, R&F Department estimates.

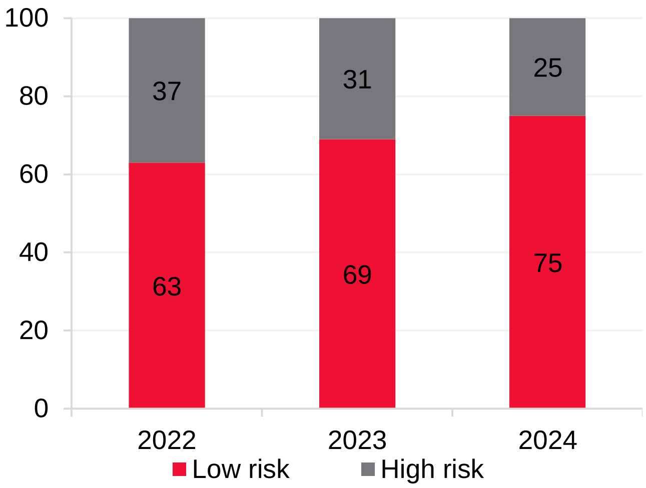
Figure 16. CVs, vacancies (% YoY) and HeadHunter index* (points)



** Ratio of active CVs to vacancies.*

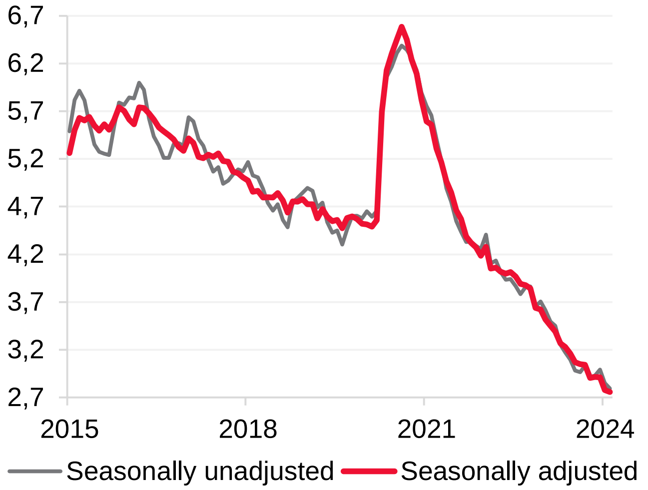
Sources: Rosstat, HeadHunter.

Figure 17. Risk of job loss, %



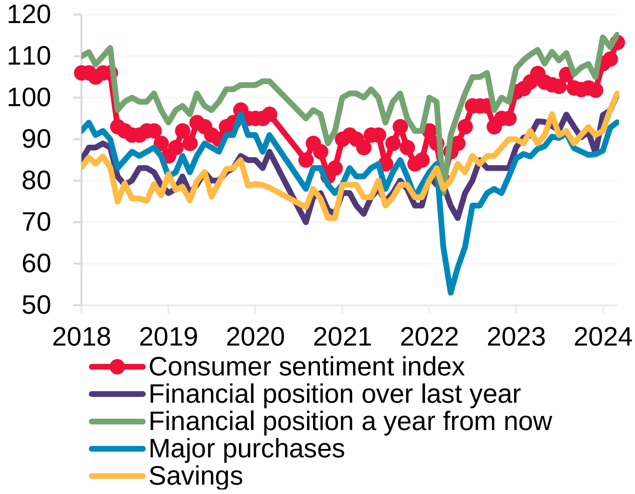
Sources: Romir, ANCOR.

Figure 18. Unemployment rate, %



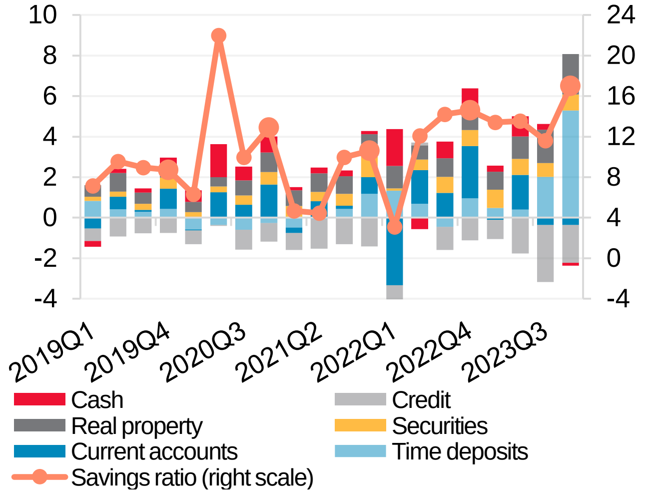
Sources: Rosstat, R&F Department estimates.

Figure 19. Consumer sentiment index and its subindices, points



Source: inFom.

Figure 20. Savings components (trillion rubles) and savings ratio (% SA, right scale)



Sources: Bank of Russia, Rosstat, R&F Department estimates.

2.2. Role of credit channel of monetary policy transmission increases

- The tight monetary stance is increasingly manifested via the credit channel of the transmission mechanism. Lending expansion has generally slowed in recent months but its rate is still elevated. That said, the segment-specific structure of growth has substantially changed.
- The pace of retail lending growth was all but unchanged in February, remaining at 1.1% MoM SA[10] for the third consecutive month (Figure 21). The cooling of the mortgage

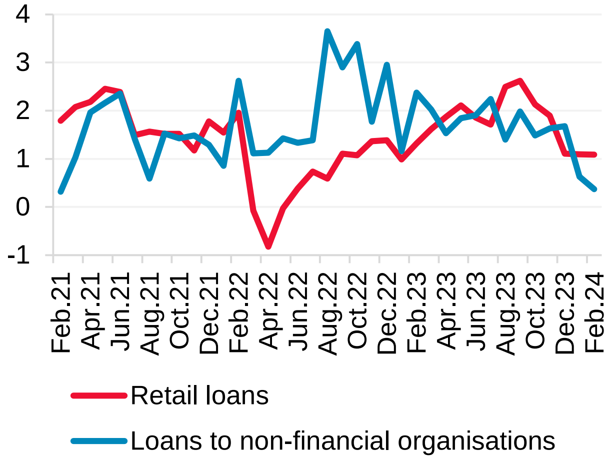
[10] Here and further on in this section, seasonally adjusted data are R&F Department estimates.

lending segment after the terms and conditions of subsidised mortgage loan provision were tightened is compensated by growth acceleration in other segments. Expansion in unsecured consumer lending accelerated to 1.6% MoM SA in February from 1.3% MoM SA in January. Despite the high interest rates, loan demand remains significant amid continued wage growth.

- The auto lending segment enjoyed significant growth acceleration to 4.8% MoM SA in February. According to preliminary data, this growth may have further accelerated in March amid expansion in the sales of cars, new and used ones alike. A large proportion of auto loans are taken to finance the purchase of used cars.
- Among the causes behind such strong demand for auto loans, the most salient are the resumption of government support programmes, people's desire to purchase a car before the new rules for charging the disposal fee take effect as of 1 April, as well as a variety of promotional campaigns and discounts offered by distributors seeking to scale down surplus stocks. Another possible factor behind the elevated rate of auto lending growth is an outflow of demand from the unsecured consumer loan segment, where macroprudential limits are applied. Prior to the impositions of the limits, some bank customers may have preferred to take auto loans in order to cut down on red tape involved in the car purchase transaction.
- Growth in ruble loans to non-financial organisations continues to gradually slow – to 0.4% MoM SA from 0.6% MoM SA in January.[11] The key portfolio growth driver was project financing. The slowdown arises from the monetary stance tightening, a drop in loan demand from companies which have received budget funds after performing government contracts, as well as from the scaling down of credit activity by systemic banks after the easing of the quick liquidity ratio was cancelled as of March 2024.
- Growth in household deposits is still strong at 2.2% MoM SA in February compared with 2.6% MoM SA in January (Figure 26). This trend continues due to the attractiveness of high deposit rates (Figure 25), especially as household income continues to expand. Corporate funds growth stayed at 1.3% MoM SA, as in January, which is in line with the rate of growth in domestic demand and is also owed to the receipt of budget funds.
- Broad money supply expansion has slightly slowed in recent months but remains at an elevated level (Figure 27). Meanwhile, the budget's contribution is still minor relative to that in 2022–2023, with lending remaining the key source of money supply growth.

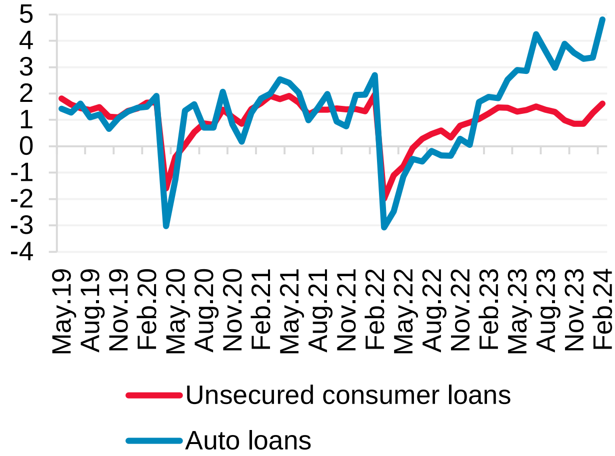
[11] Sole proprietor loan growth slowed to 1.5% MoM SA from 2.2% MoM SA.

Figure 21. Ruble loans portfolio growth, % MoM SA



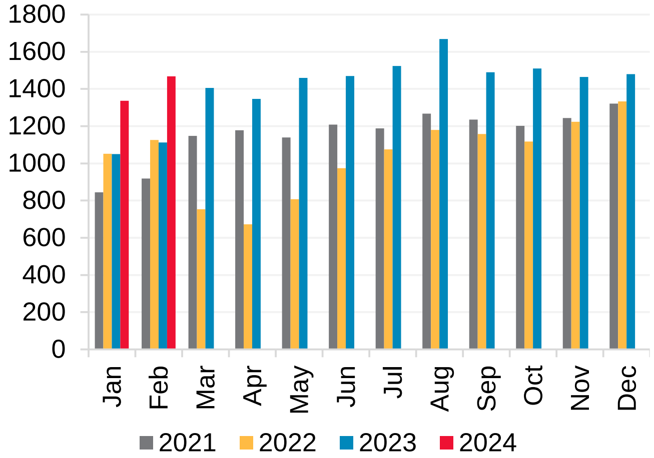
Sources: Bank of Russia, R&F Department estimates.

Figure 22. Ruble retail loans portfolio growth, % MoM SA



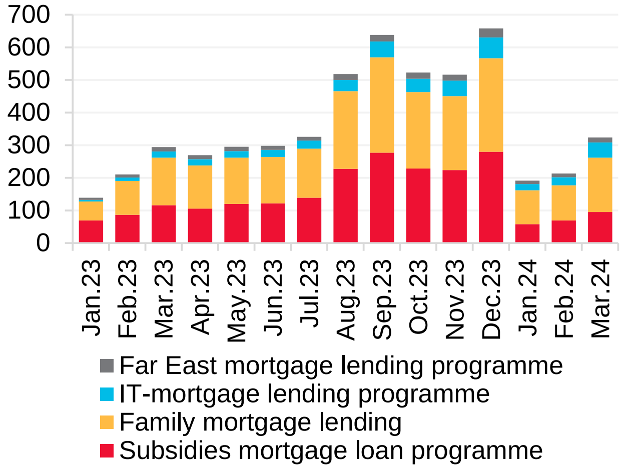
Sources: Bank of Russia, R&F Department estimates.

Figure 23. Volume of consumer loans issued, billion rubles



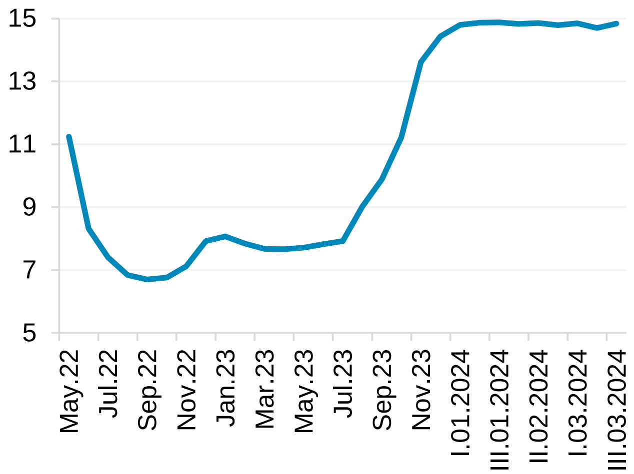
Sources: Bank of Russia, R&F Department estimates.

Figure 24. Loan issuance under subsidies mortgage loan programmes, billion rubles



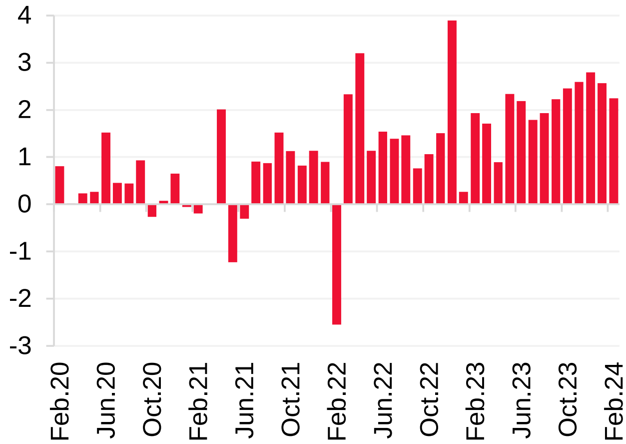
Sources: DOM RF, R&F Department estimates.

Figure 25. Maximum interest rate of 10 credit institutions taking the largest household deposits, %



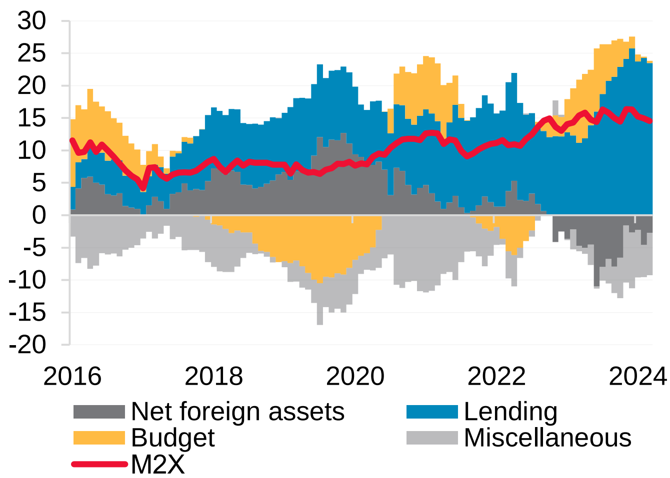
Note. Roman numerals stand for ten-day interval numbers.
Sources: Bank of Russia, R&F Department estimates.

Figure 26. Household funds with banks, % MoM SA



Sources: Bank of Russia, R&F Department estimates.

Figure 27. Key drivers of annual growth in broad money supply on the asset side, %



Sources: Bank of Russia, R&F Department estimates

In focus. Proinflationary risks in labour market: cross-country comparisons

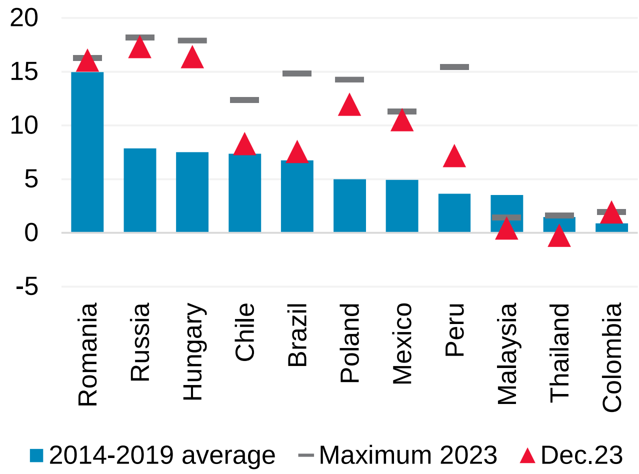
- Nominal wage growth in a number of emerging market economies is close to its multi-year highs, which is far above the pre-COVID levels. An important cause behind the increased growth rate is the structural transformation of economies at large and labour markets in particular in the COVID and post–COVID periods.
- In some countries, above all, those in Central and Eastern Europe (CEECs), unfavourable labour supply trends led to a significant wage growth acceleration starting in late 2020 and a subsequent rise in inflation. Moreover, the pace of wage growth remained elevated in 2023, generating substantial proinflationary risks. Countries with a favourable demographic situation and low dependence on migrant labour saw a more moderate and temporary wage and inflation rise.
- Structural changes which the Russian economy has undergone in recent years have given rise to, among other things, increasingly tighter labour market. An imbalance between demand and supply in the labour market creates prerequisites for sustainable wage increases outstripping labour productivity growth. This factor can lengthen the lags of tight monetary policy transmission to changes in demand and price movements.
- The Bank of Russia's monetary policy decisions will help to gradually bring the pace of aggregated demand growth further in line with the potential of supply expansion in the economy, ensuring the return of inflation to the target in 2024 and its subsequent stabilisation at around 4%. As part of this process, it is important to continue implementing a set of macroeconomic policy measures seeking to reallocate labour to more efficient companies and enhance overall labour productivity.

Recent years have seen rapid sustainable growth in nominal and real wages in Russia. A substantial change in the balance of labour demand and supply towards workforce shortages results in the unemployment rate regularly hitting new lows. Employers' intensified competition for labour results in rapid wage growth. The Russian case is not an exception, a similar situation is seen in a number of other countries.

In many emerging market economies (EME), nominal wage growth is close to its multi-year highs, standing far above the pre-COVID levels (Figure 28). The reason common to these countries is largely the structural consequences of the pandemic for the labour market. Stringent and protracted mobility restrictions during the pandemic, including those self-imposed by people, brought about a heavy fall in demand for services, and therefore a mass departure of workers from this sector.

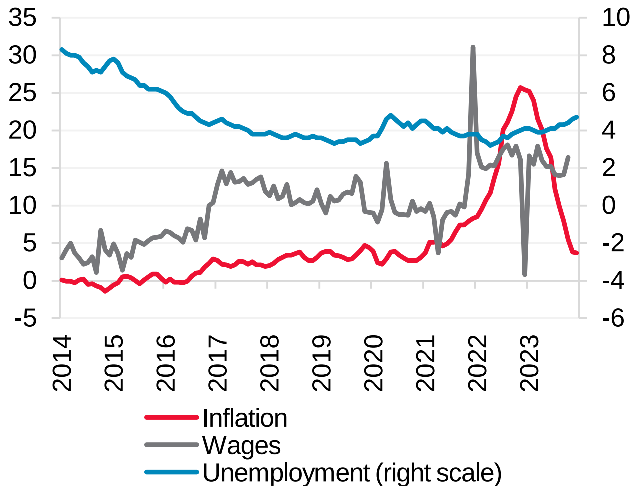
As the pandemic-related restrictions were eased, services, by contrast, became one of the fastest-growing sectors, thanks to massive government programmes supporting demand. After the restrictions were lifted, expenses for services, in particular, for leisure and entertainment and tourism, started to rise, delivery services were buoyantly expanding. Labour demand began to grow in these sectors, but by that time many workers had already got retrained, so not all industries enjoying rising consumer demand were able to find the sufficient number of workers. All this ramped up employers' competition for labour in the post-pandemic period, which produced wage growth outstripping an increase in labour productivity and, consequently, mounting proinflationary risks.

Figure 28. Nominal wages in largest emerging markets, % YoY



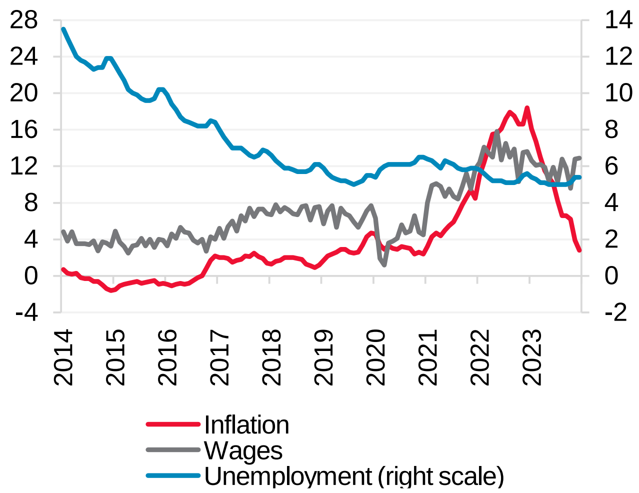
Sources: Rosstat, Cbonds, R&F Department estimates.

Figure 29. Inflation, wages (% YoY) and unemployment rate (%) in Hungary



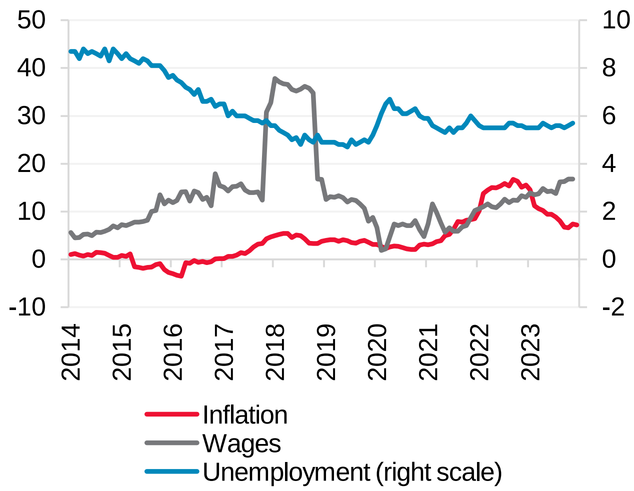
Sources: Rosstat, Cbonds, R&F Department estimates.

Figure 30. Inflation, wages (% YoY) and unemployment rate (%) in Poland



Sources: Cbonds, R&F Department estimates.

Figure 31. Inflation, wages (% YoY) and unemployment rate (%) in Romania



Sources: Cbonds, R&F Department estimates.

Therefore, the key influence on the labour market situation was exerted by changes in supply. EMEs suffering long-term population contraction and ageing saw an additional loss of workers. In the pre-pandemic period, this factor was largely offset by an inflow of labour from other countries. But in the pandemic period, many migrants had to return to their countries and were unable to come back quickly amid intercountry mobility restrictions. Workforce shortages in many EMEs were further aggravated by an outflow of skilled labour to neighbouring advanced countries.

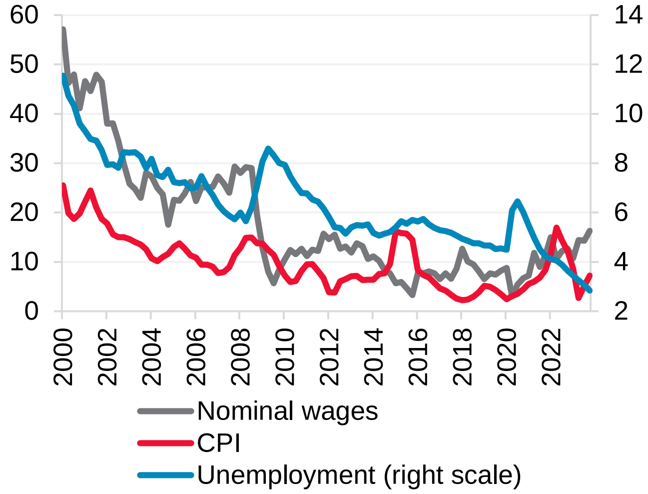
Indicative examples of EMEs where all of the above factors were present to a greater or lesser degree are Central and Eastern European Countries (CEECs). Indeed, before the start of 2022, Hungary, Poland, and Romania saw steady population contraction and ageing. After a sharp rise in 2020, the unemployment rate returned to local pre-pandemic lows. In this environment, the years 2020–2021 saw a dynamic wage growth acceleration, which, with a several quarters' lag, translated into a price rise acceleration.

Inflation in the overwhelming majority of EMEs exceeds the pre-pandemic average and often the central banks' targets. We, however, believe that the cases of Latin American countries and especially those of the Asian–Pacific region are much less indicative in this respect. Changes in wages and prices were generally co-directional, but wages grew in a catch-up mode, following inflation acceleration (i.e., the real wage level was being restored). Thus, there was no "sticking" of wages at an elevated level and, accordingly, no sustainable proinflationary risks arising from the labour market. Overall, cross-country differences in the nature of proinflationary risks arising from the labour market are owed to a broad spectrum of factors which need to be examined more thoroughly. These factors include, in particular, industry-specific structure of economies' growth, demographic trends, the labour market's sensitivity to migration flows, the maturity of trade unions, the share of the informal sector in the economy, and so on.

We believe that the Russian labour market' current conditions are to a great extent similar to the above case of selected CEECs. Moreover, an additional increase in the labour market tightness in the post–COVID period was in 2022 driven by a substantial change in external conditions, which led to the economy's structural transformation. This provokes intensive competition for labour and, given the historically low unemployment rate, brings about an increased pace of wage growth. This combination gives rise to proinflationary risks, which monetary policy decisions take into account.

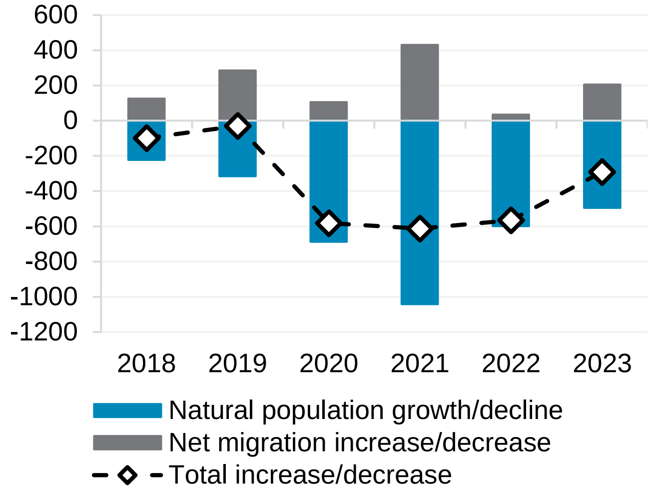
At the same time, Russia's current demographic situation is such that potential for substantial labour supply expansion in the years to come looks limited (Figure 33). The labour market tightness can be eased through bridging the imbalance between labour demand and supply. Therefore, as proinflationary risks arising from the aggregate demand situation continue, the Bank of Russia's monetary policy decisions seek to bring the rate of demand growth in line with supply expansion potential. This will be key to returning inflation to the target in 2024 and its subsequent stabilisation at around 4%. An additional important prerequisite to containing proinflationary pressure from the labour market, including on a longer horizon, is the continuation of the set of measures aiming to reallocate labour from relatively inefficient to efficient companies and labour productivity enhancement.

Figure 32. Nominal wages, CPI (increase, % YoY), and the unemployment rate (% SA)



Sources: Rosstat, R&F Department estimates.

Figure 33. Factors of population change, thousand people



** The new regions are not so far accounted for in Russia's population numbers. Net migration gain in 2023 includes people who have arrived from the new regions.*

Source: Rosstat.