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AEB North-Western Regional Committee

ECONOMIC-FINANCIAL OUTLOOK: CHALLENGES AND PERSPECTIVES FOR 2015

Briefing by EBRD and Danske Bank

27th January, 2015

St. Petersburg
Consulate General of Finland

Sponsor:

Danske Bank



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Timo Mikkonen

AEB North-Western Regional Committee Chair

Welcome address



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AEB NWRC PLANS FOR 2015

- 1. AEB NWRC General Meeting – March 25, 2015**
- 2. 6th Forum "Northern Dimension" – March 26, 2015**
- 3. Open event on "E-Trade in Russia: Current situation, challenges and opportunities" – February, 2015 (tbc)**
- 4. World Bank briefings – April, October, 2015**
- 5. Sustainable principles of Green Building – February-March, 2015**
- 6. Briefing of Migration authorities representatives – March, 2015**
- 7. Open event: "Market overview and legal update" – September, 2015**
- 8. 20th Anniversary of AEB – September-October, 2015**



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Peter Tabak

**European Bank for
Reconstruction and
Development (EBRD)**



European Bank
for Reconstruction and Development

Russia: Economic outlook and scenarios for 2015

Peter Tabak
EBRD

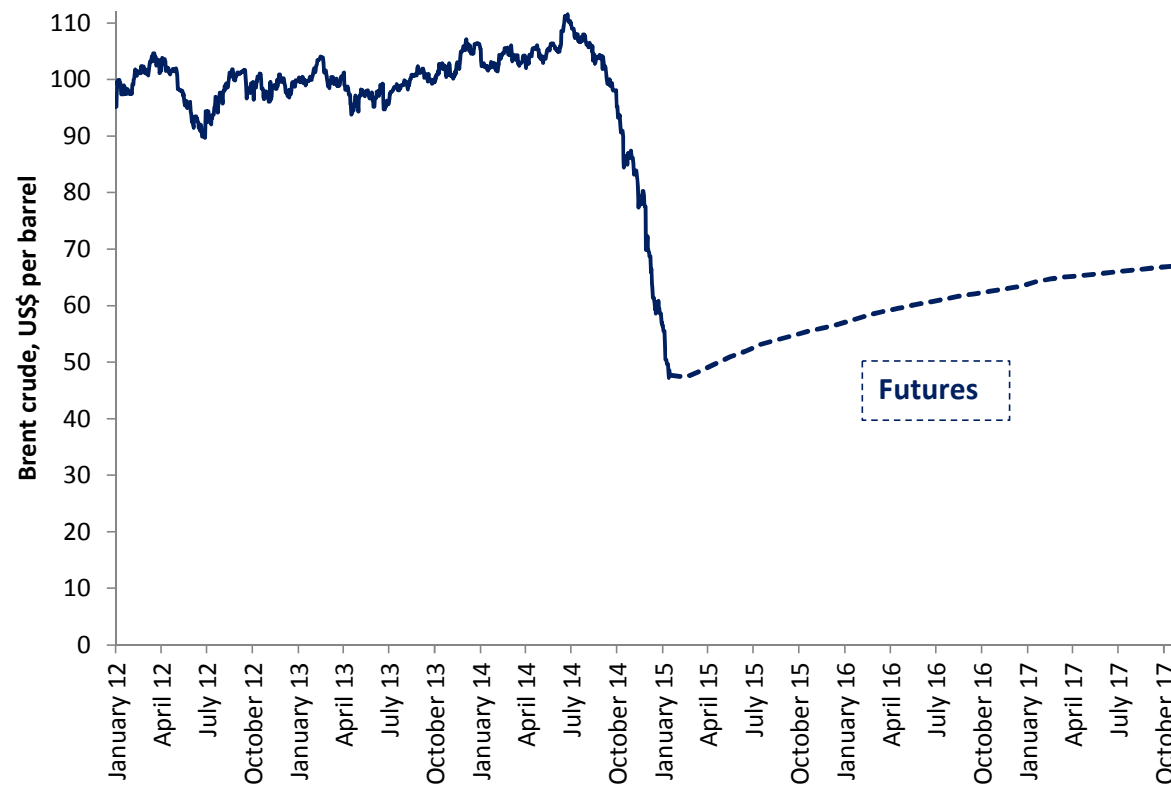
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27 January 2015

Oil prices have dropped sharply...



European Bank
for Reconstruction and Development

- Futures prices show gradual recovery...
- ...but prices are expected to be lower in 2015 (around US\$ 60) than in 2014 (around US\$ 100)



Source: Bloomberg

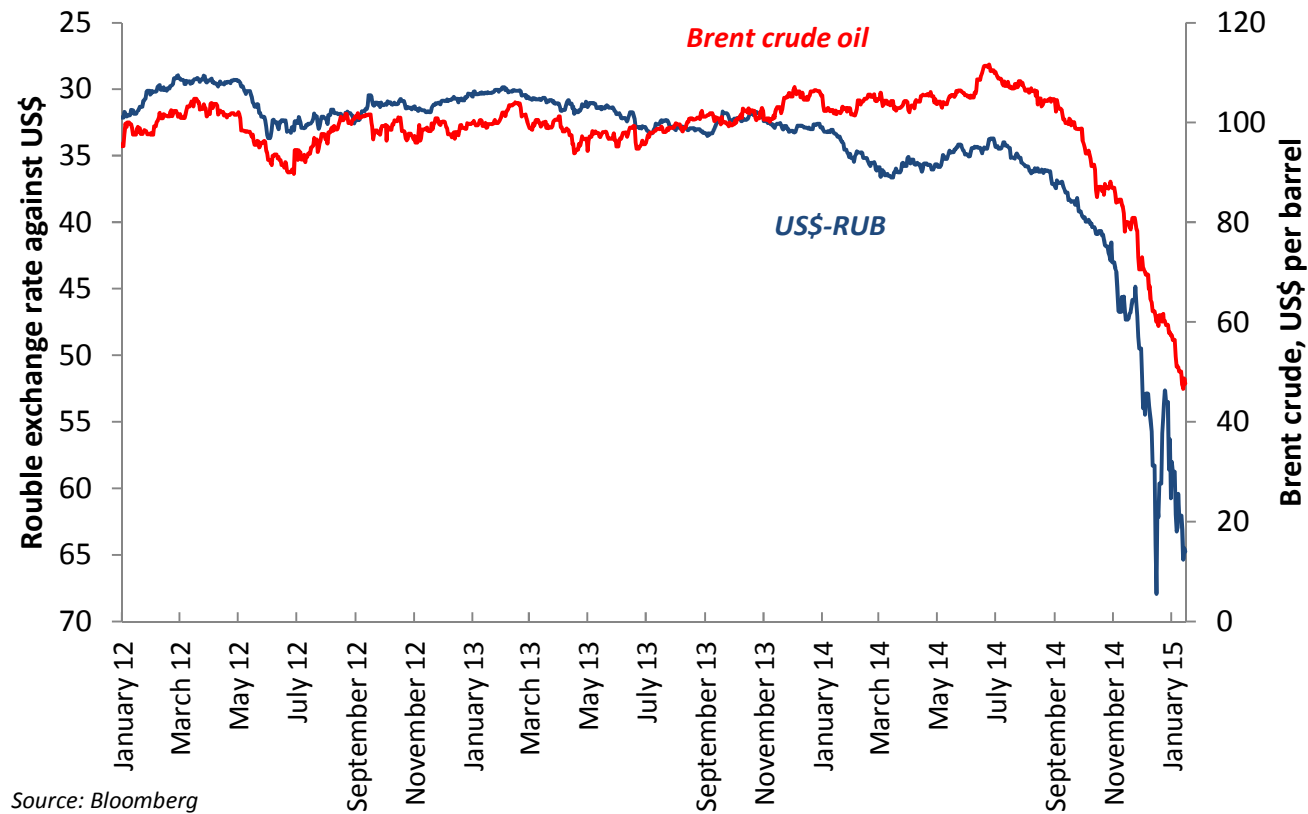
...reshaping the regional outlook



- Russia: oil price drop compounds the impact of long-run structural problems, weak investor confidence and increasingly biting sanctions
- Other major commodity producers also see slowdown
- Significant negative spill-overs to countries with close ties to Russia, outweighing terms of trade impact
- Commodity importers with weaker ties to Russia will be net gainers (CESEE, Turkey)
- However, considerable headwinds from eurozone and eventual normalisation of US monetary policy
- Overall: average growth in the EBRD region turns negative in 2015, but with significant country variations

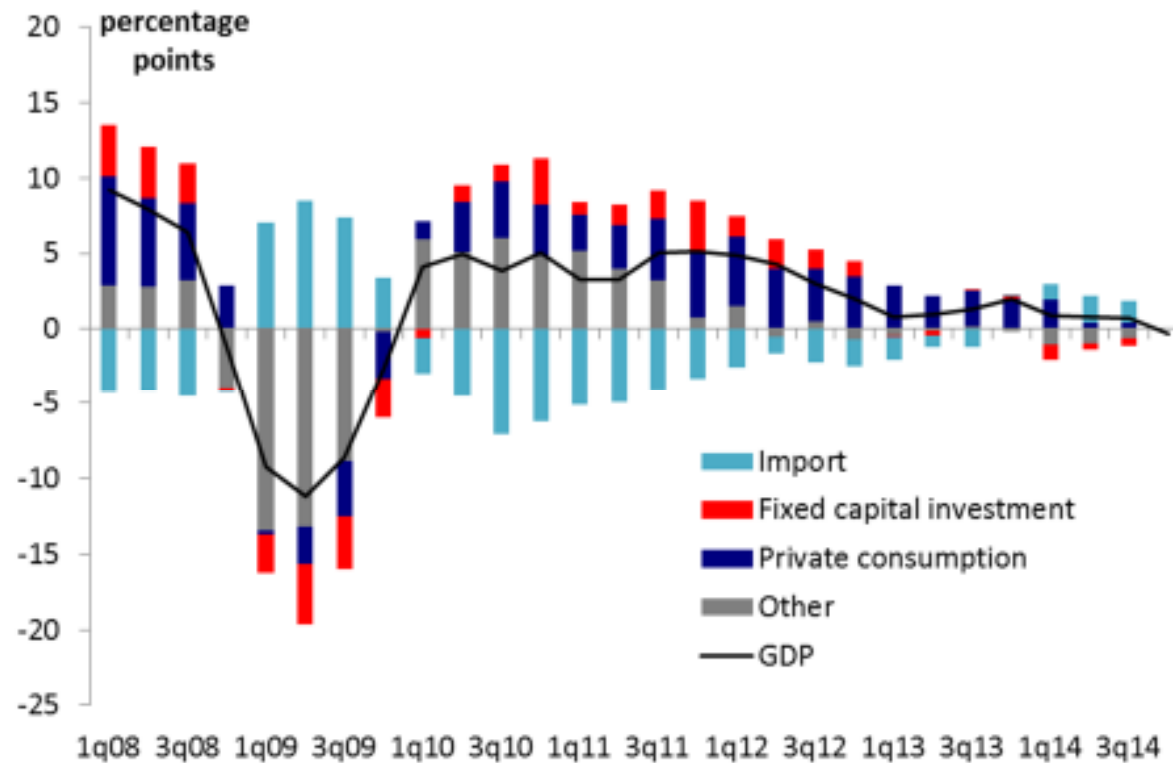
Economic outlook has deteriorated in Russia

- Structural slowdown exacerbated by sanctions and fall in oil prices



Russian GDP may have declined in Q4

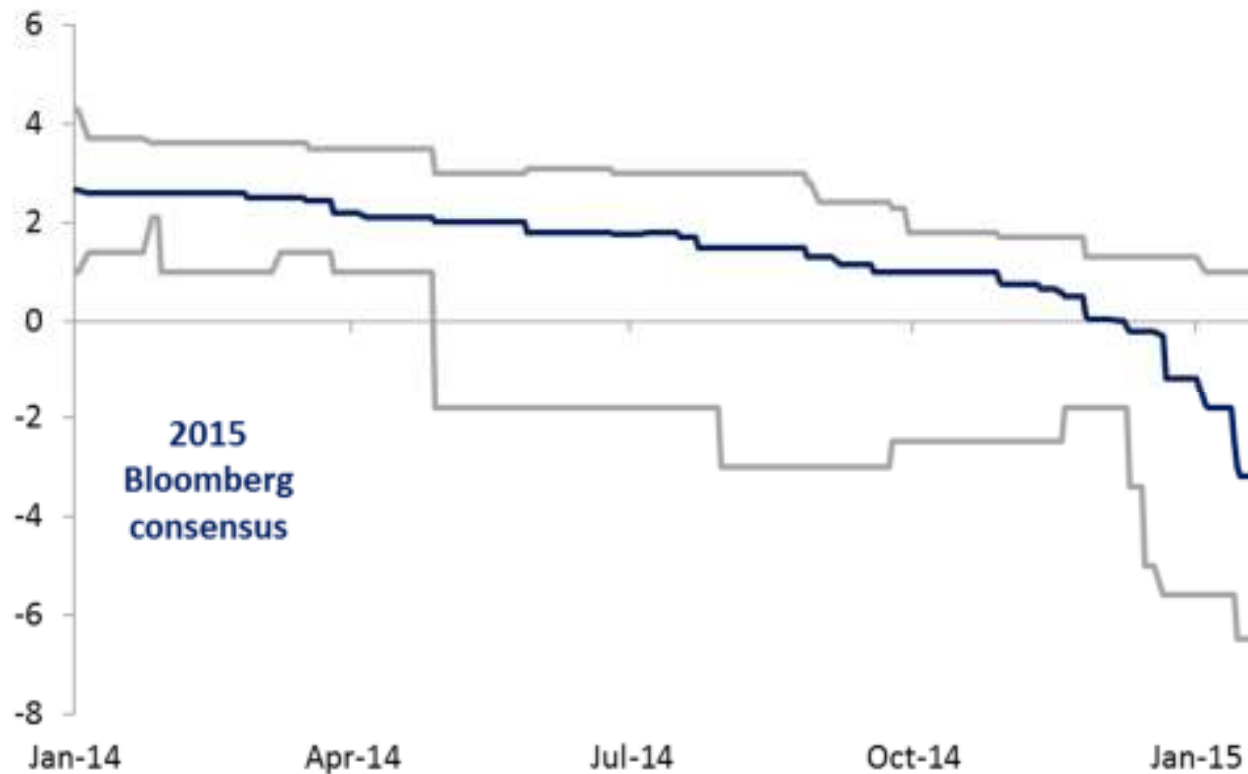
- Slowdown in all domestic demand components with some offsetting effect from import contraction
- No investment growth in the last two years



Source: Rosstat

Most analysts expect recession in 2015

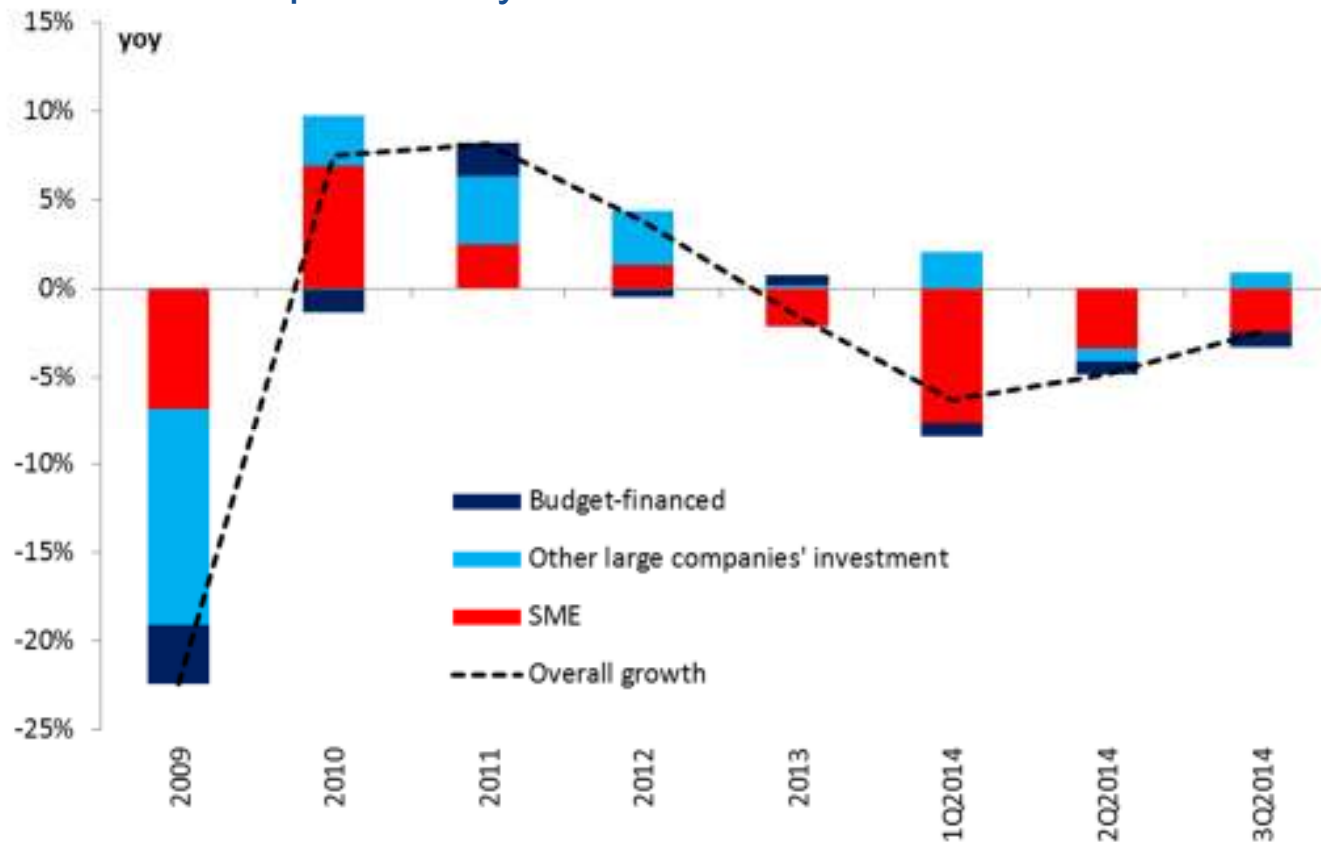
- Weak investor confidence, tight financing conditions, slowing real wage growth and retail lending contributes to the slowdown



Source: Bloomberg

Low investments...

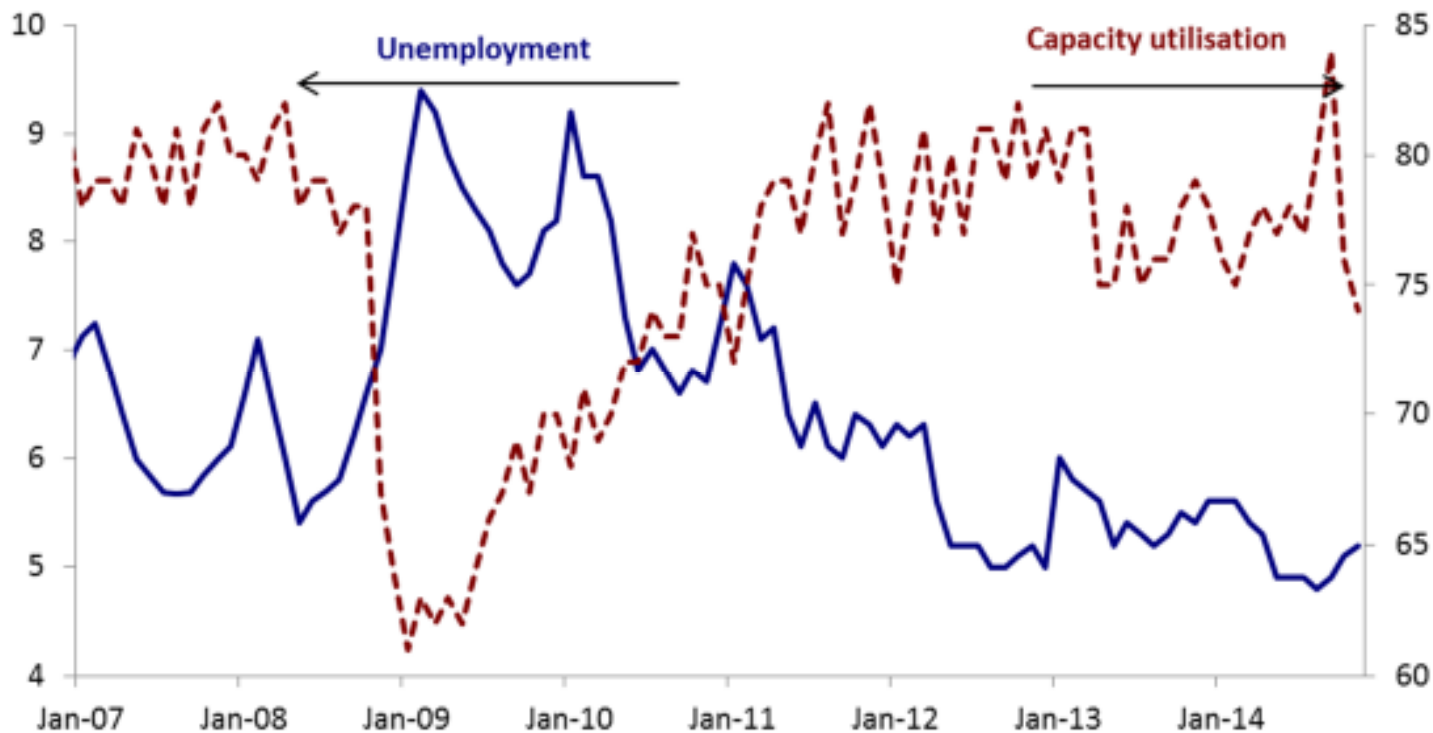
- As Sochi preparation drew to a close, state and related investments slumped
- SME investment is particularly weak



Source: Rosstat

...may have strong implications for long-term growth

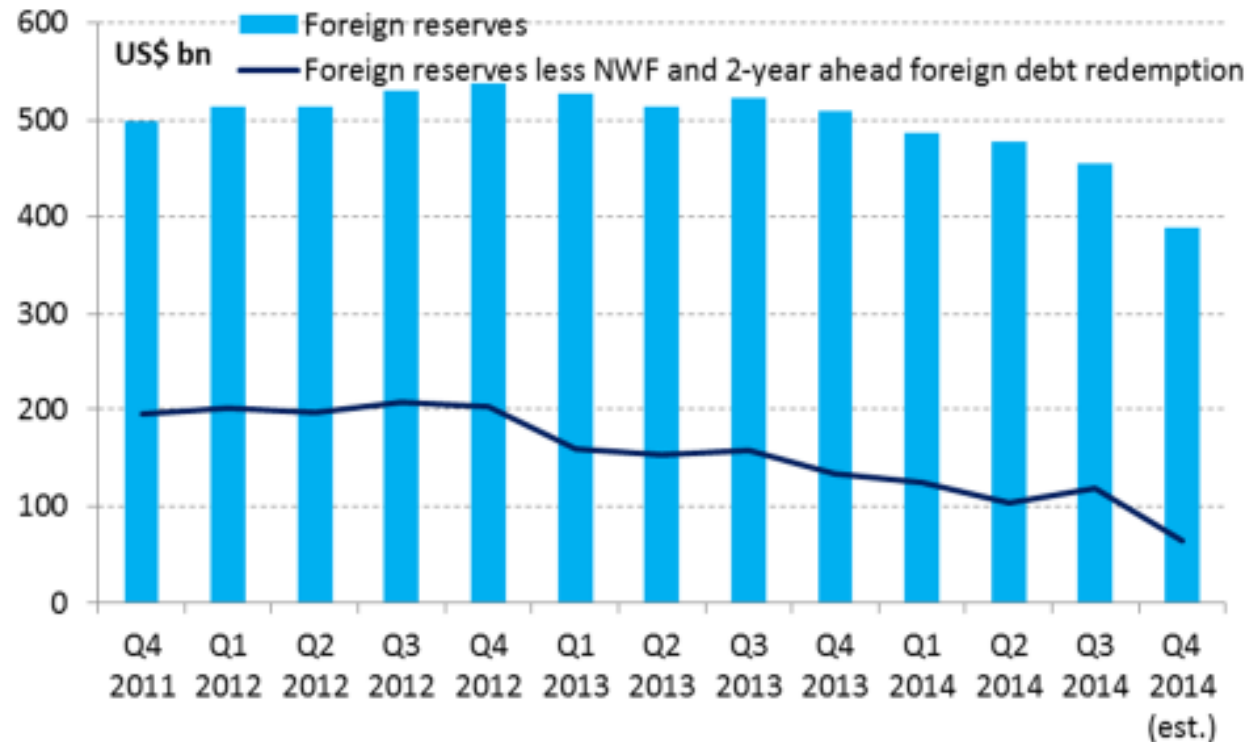
- Rebound will be much more protracted than in 2009 due to...
- ...adverse demographic trends, outdated/insufficient production capacities, constrained financing



Source: Rosstat, REB

Headline reserves are still relatively high but with large commitments...

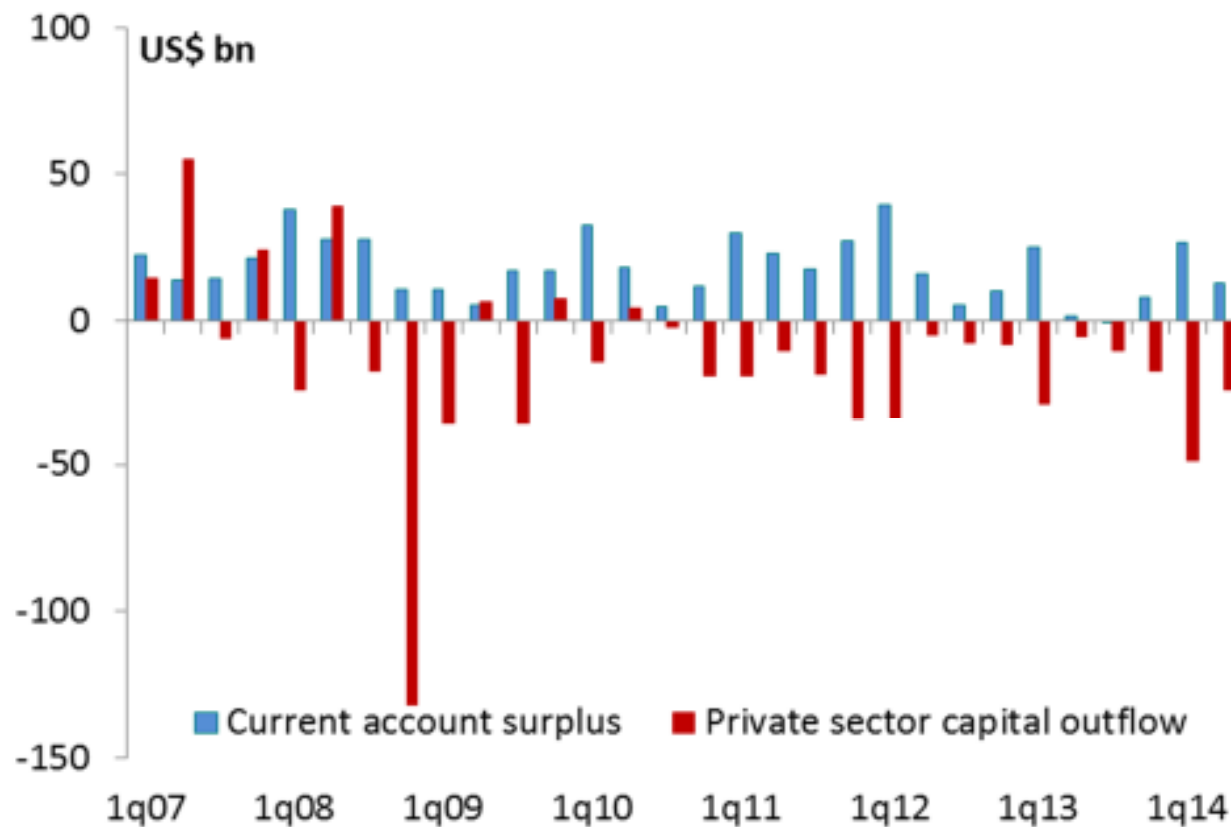
- Reserves declined by 25% or US\$ 125 bn in 2014
- Present balance of to US\$ 385 bn covers 2.5 years of foreign debt redemptions (around US\$ 300 bn) and consists of less liquid NWF assets (about US\$ 80 bn)



Source: CBR, MinFin

...and steady private sector capital outflows may reduce them further

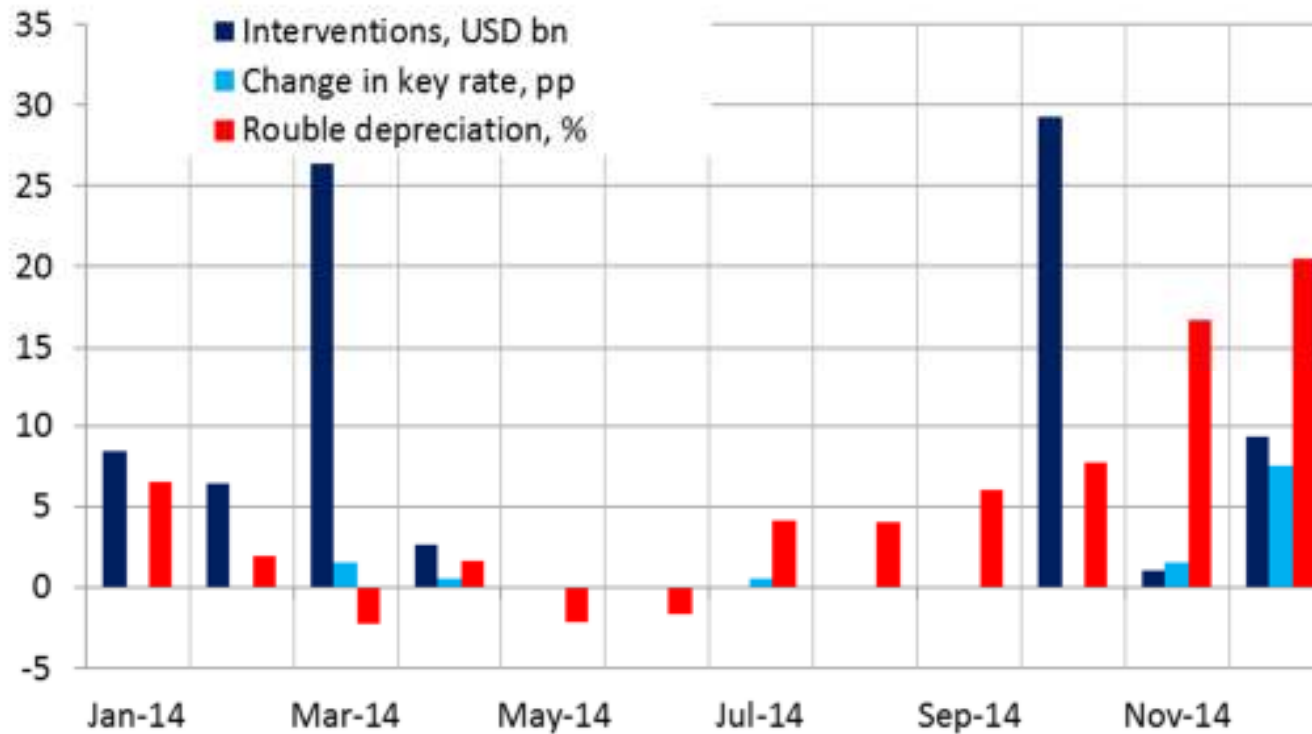
- 4Q 2014 capital outflow was close to record 2008...
- ...including US\$ 18 billion by households as rouble volatility increased



Source: CBR

CBR policy change tries to save reserves...

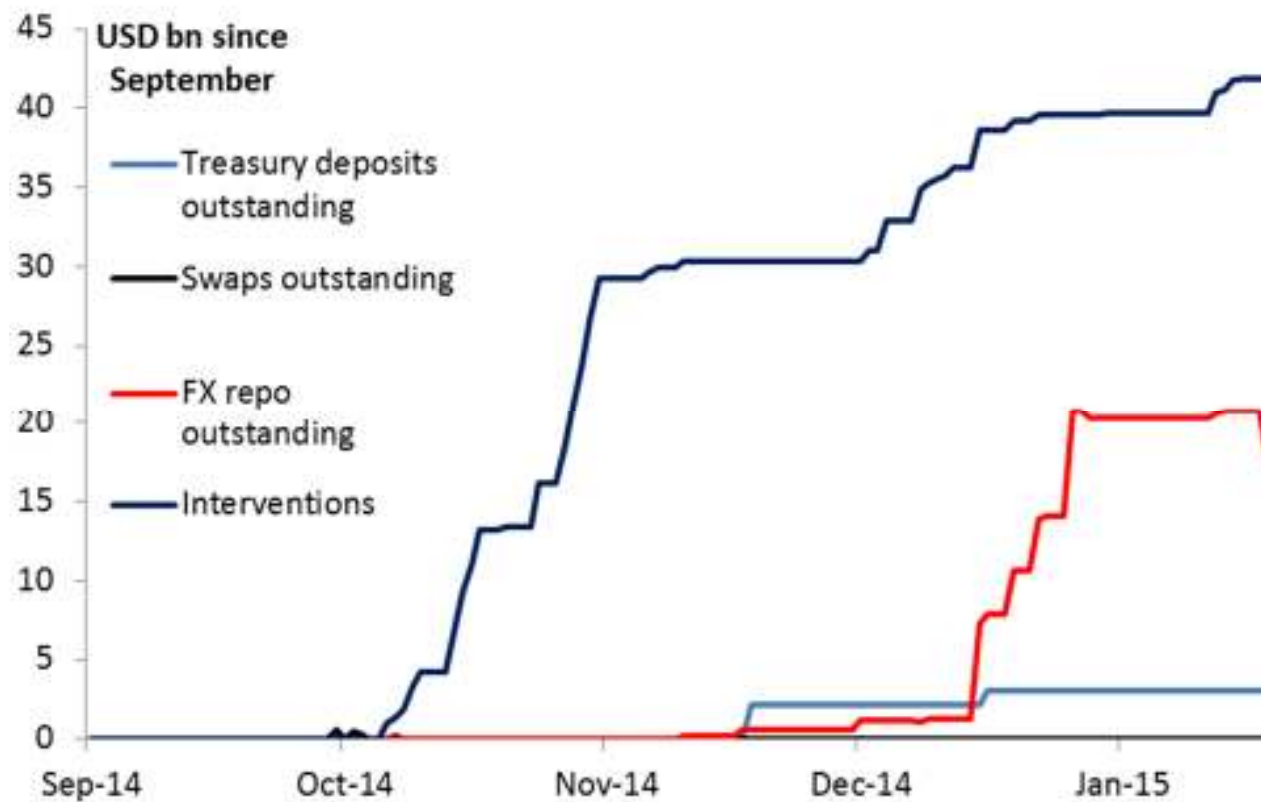
- Floating exchange rate regime operates with less intervention...
- ...but more interest rate volatility



Source: CBR

...while providing FX liquidity

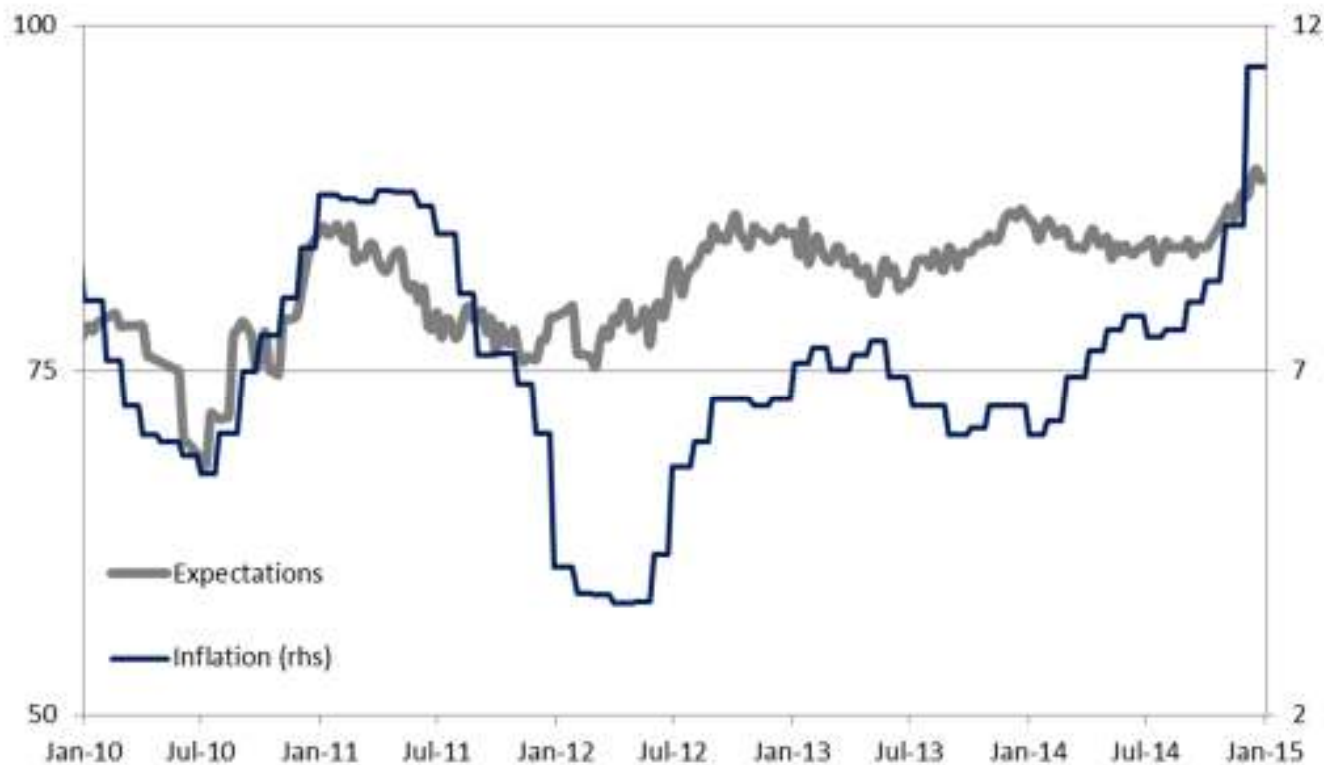
- FX liquidity provision through repos and swaps allows more flexible operations



Source: CBR

Rouble weakening translates into surging inflation

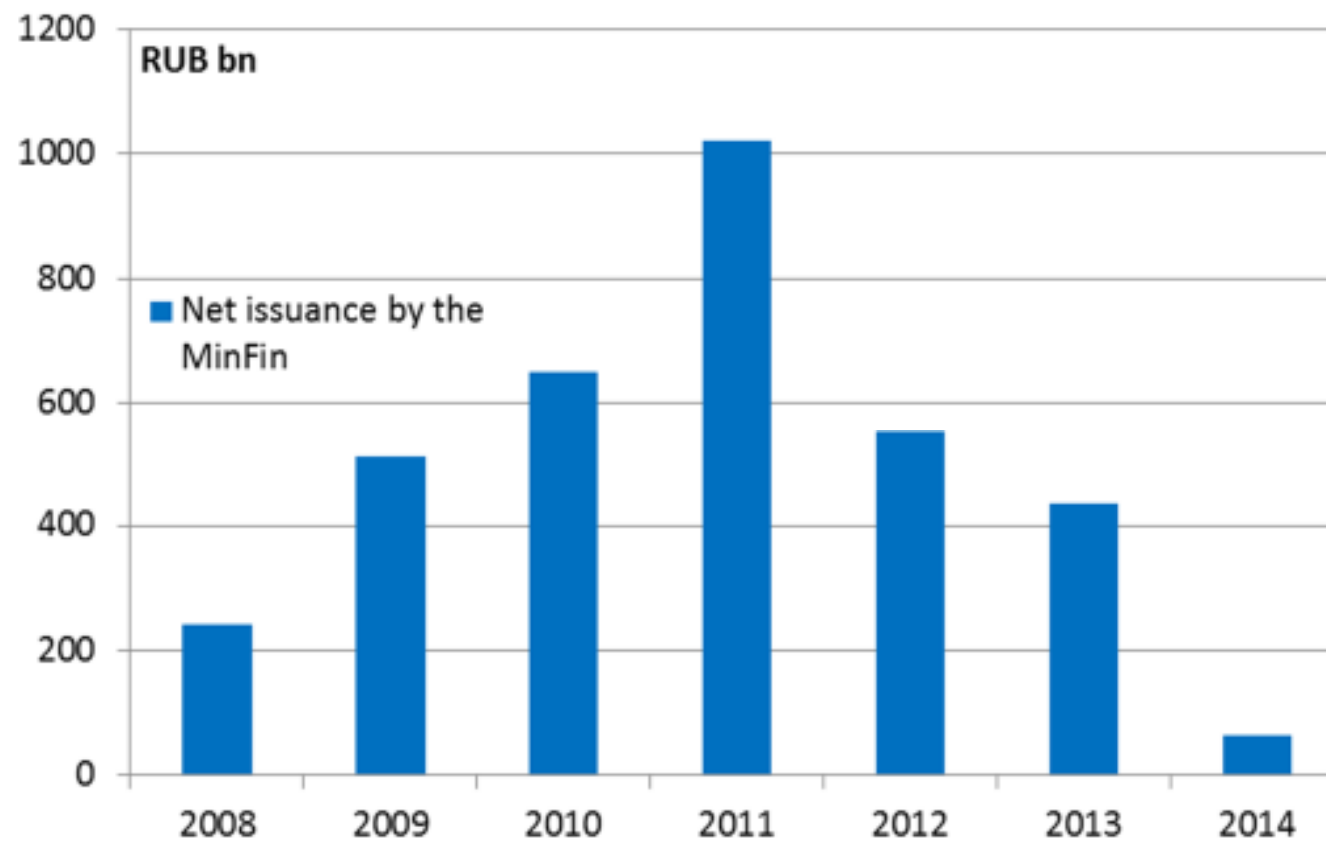
- Inflation may reach over 14 per cent in 2015
- Stabilisation of expectations will be key for disinflationary policy



Source: FOM, Rosstat

Sovereign financing is difficult...

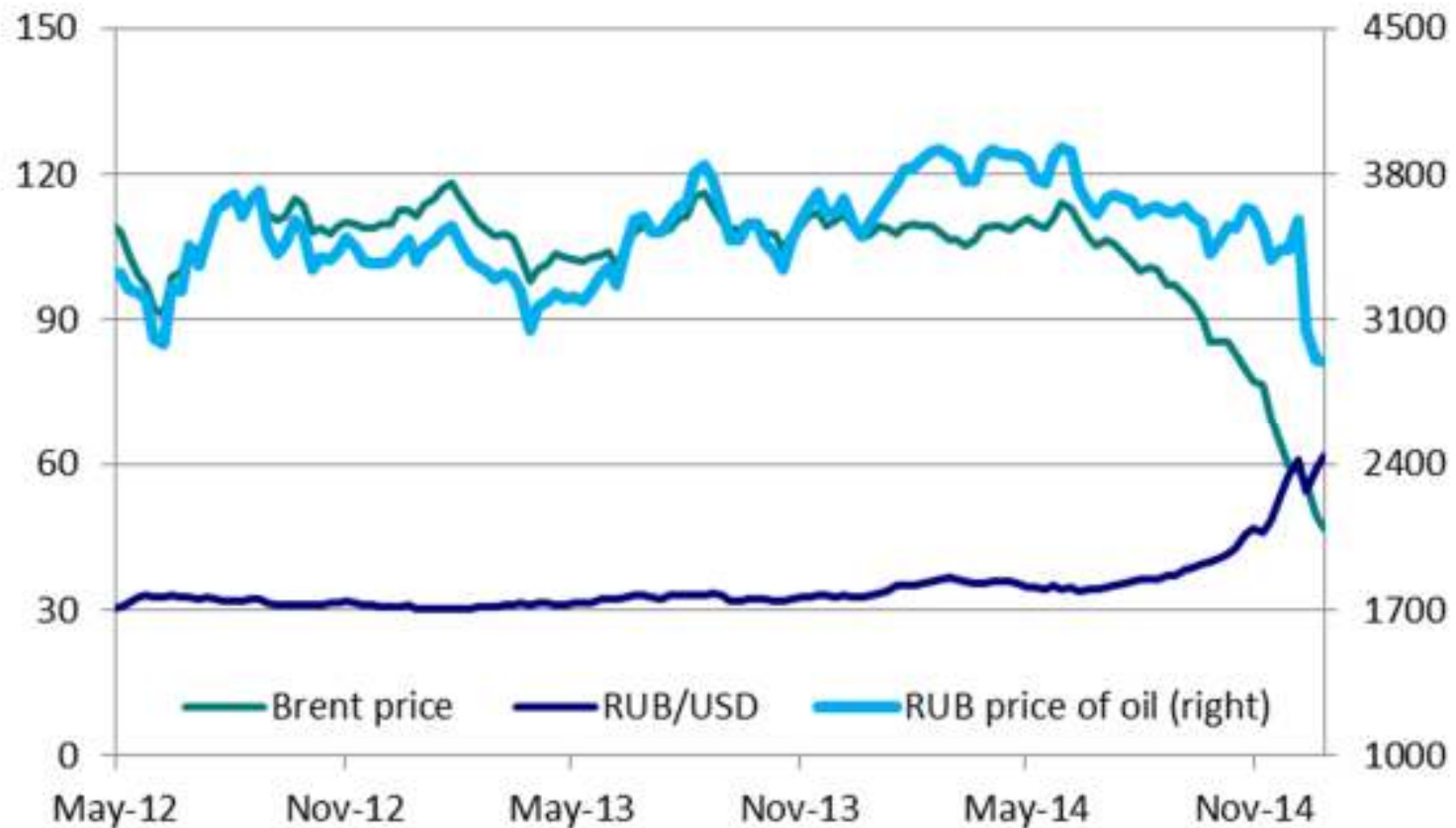
- Auctions were cut back on weak demand and high interest rates



Source: Treasury

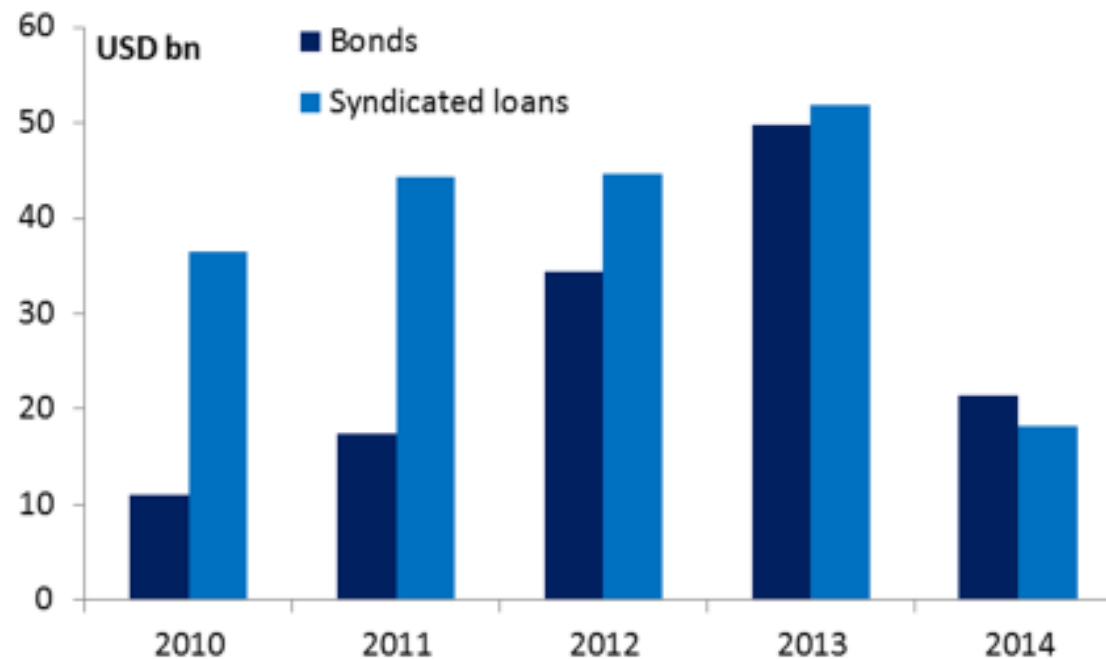
...but weak rouble has some counterbalancing effect

- Rouble depreciation may offset about 2/3 of the oil price fall



Corporates, especially private sector and SMEs are hurt most

- Deleveraging and investment cuts due to tight foreign and expensive domestic funding
- State support is more restricted than in 2009 and targets strategic companies



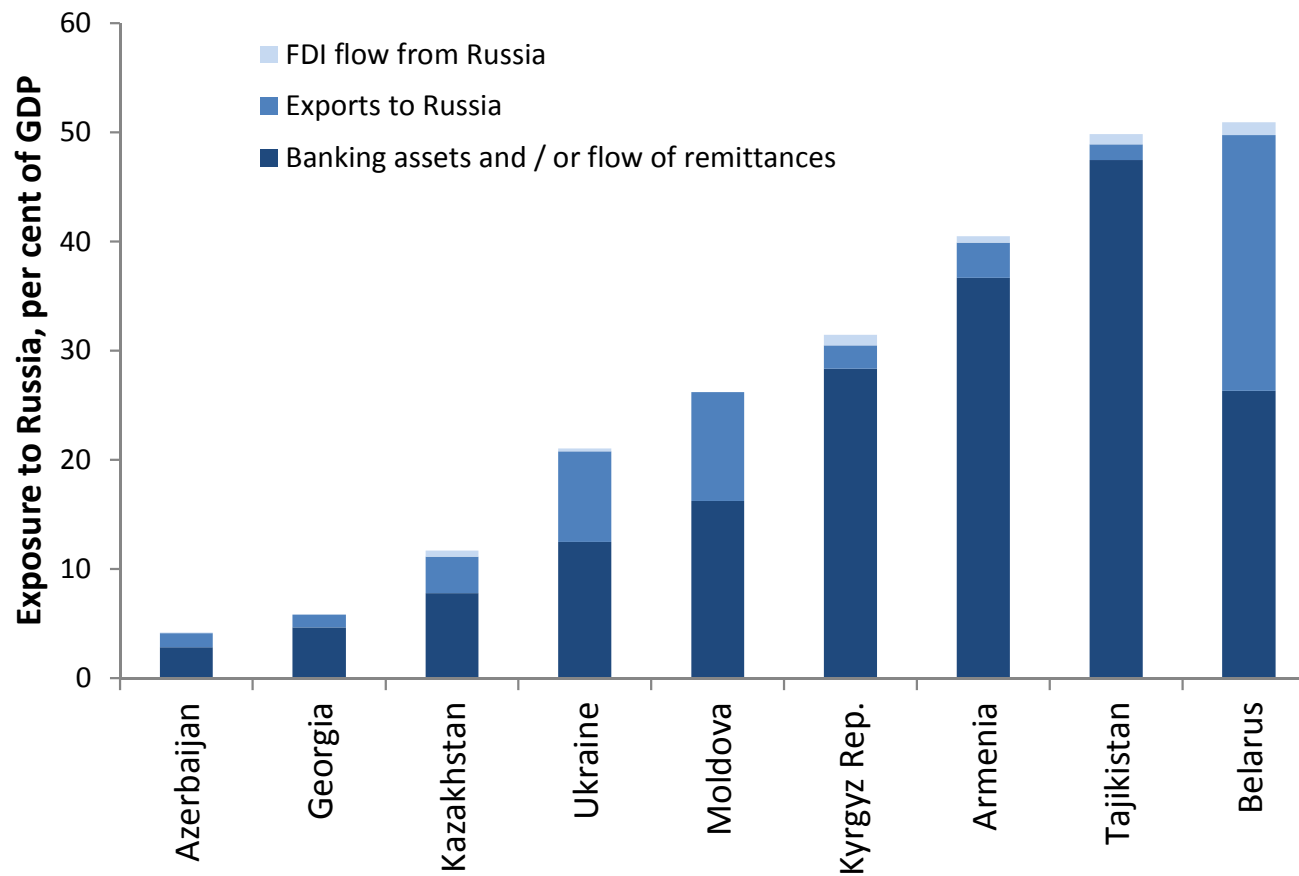
Source: Bloomberg

In EEC and CA, spill-overs from Russia may more than offset cheaper oil



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- Lower remittances, export demand and lower investment
- Reduced availability of credit from Russian banks

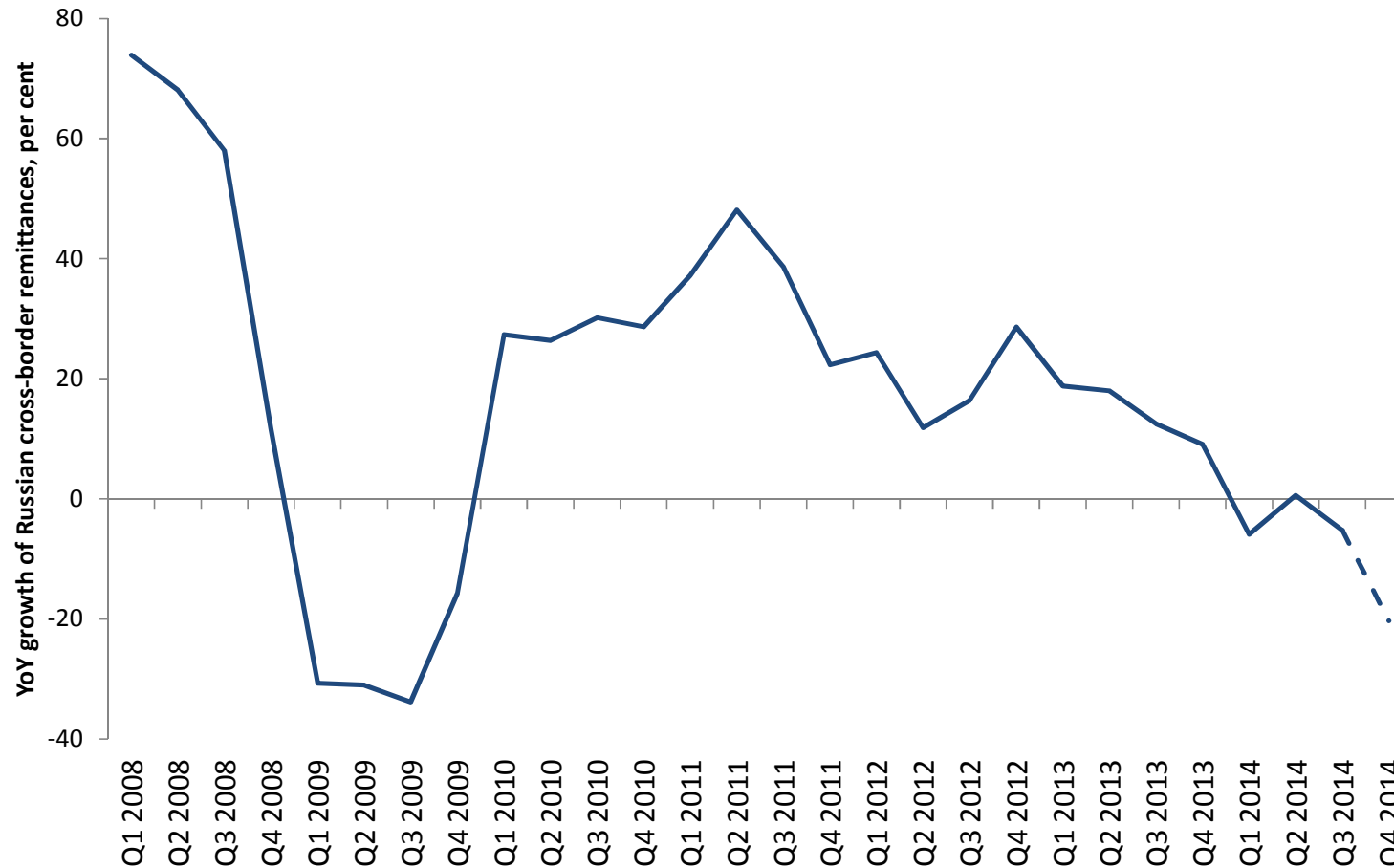


Sources: National sources via CEIC

Remittances to EEC and Central Asia are declining at an accelerating pace



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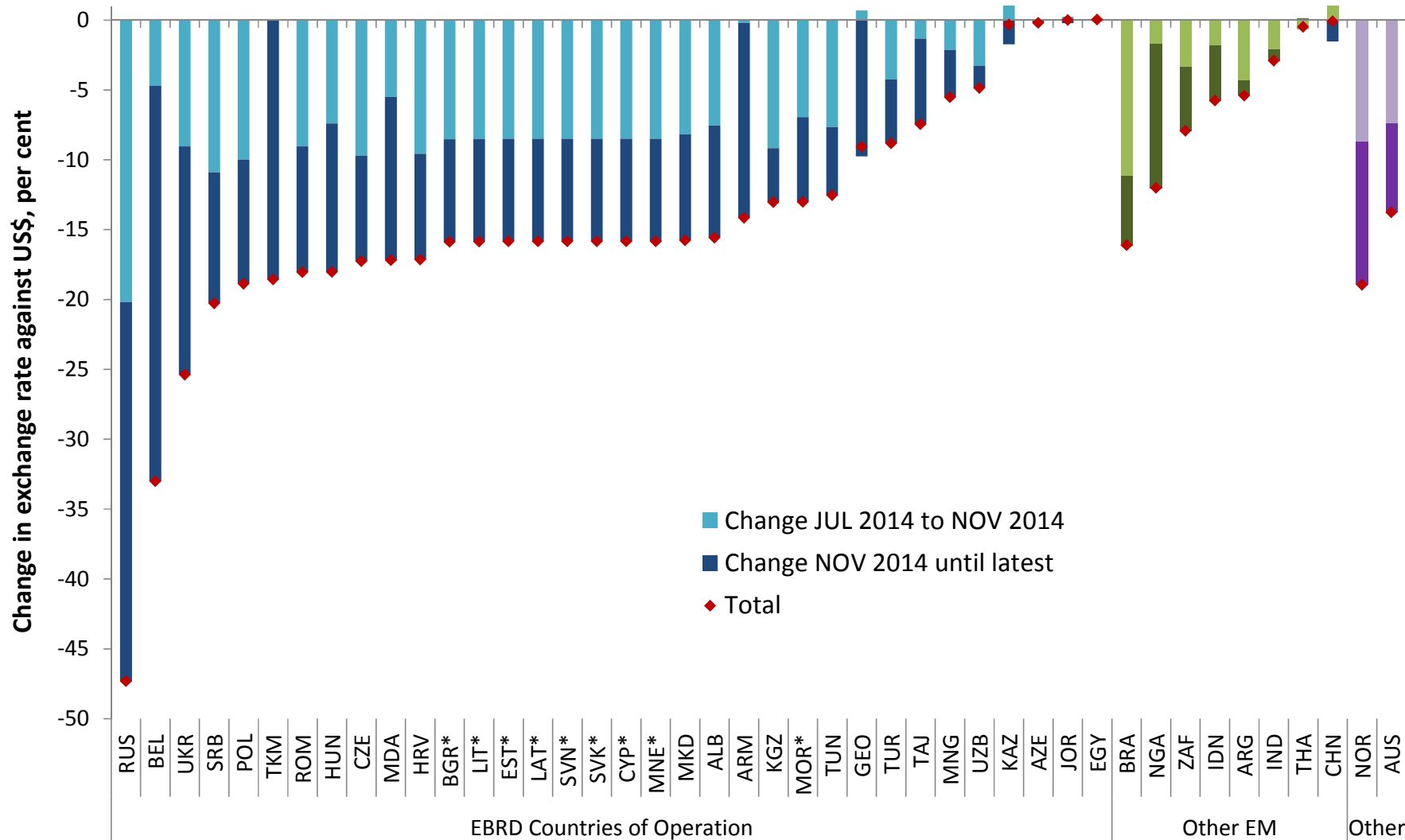


Source: Central Bank of Russia; National sources; EBRD calculations

Many currencies have come under pressure with rouble depreciation



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Source: Bloomberg



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Vladimir Miklashevsky

Danske Bank

The background of the lower half of the slide is an abstract graphic of overlapping, wavy blue lines and bands, creating a sense of motion and depth. The colors range from light sky blue to a deeper, more saturated blue.

RUB FX Edge

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27 January 2014

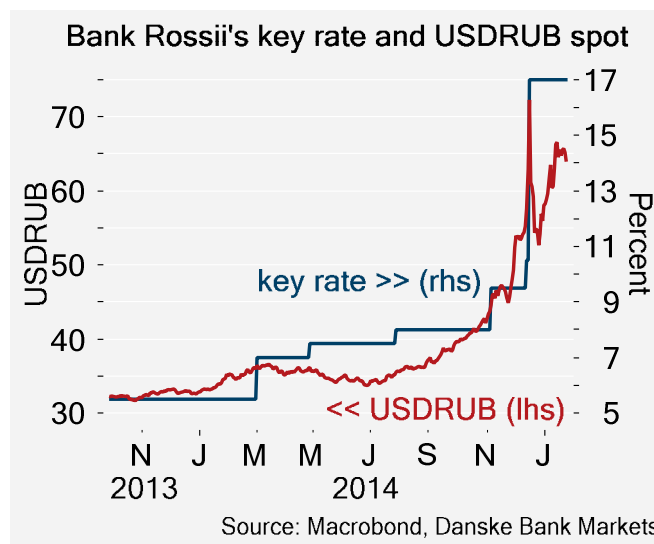
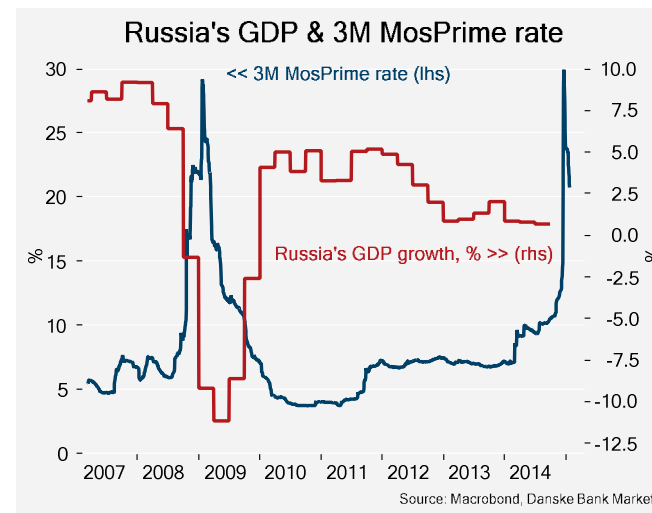


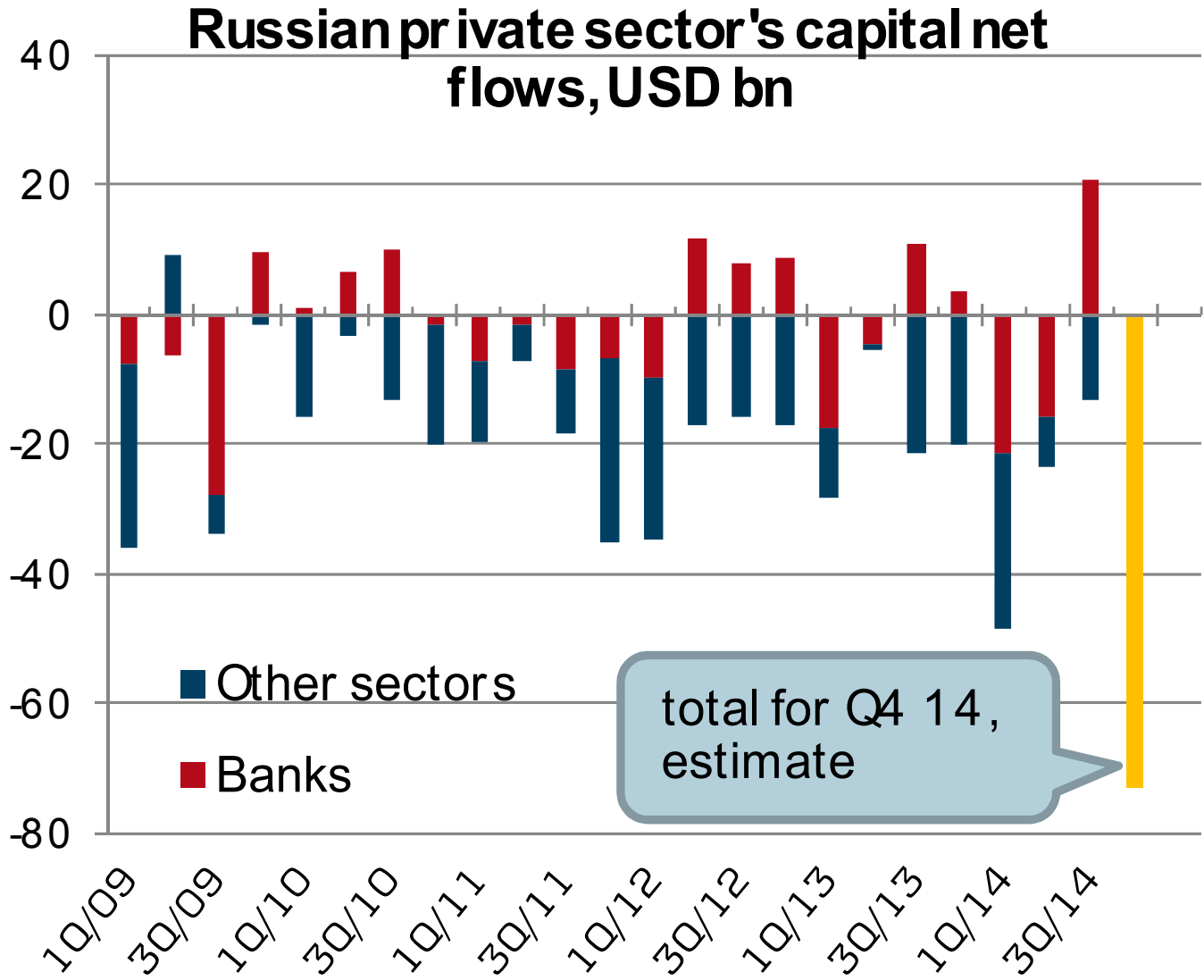
RUB FX forecast as of 13 November 2014

	Spot	Forecast			
		+1m	+3m	+6m	+12m
Exchange rates vs RUB					
USD/RUB	46.31	48.00	49.00	51.00	51.00
EUR/RUB	57.70	60.00	59.78	61.20	62.73
RUB/DKK	0.129	0.124	0.125	0.122	0.119
RUB/SEK	0.160	0.153	0.152	0.147	0.140
RUB/NOK	0.147	0.142	0.141	0.135	0.128

Source: Danske Bank Markets

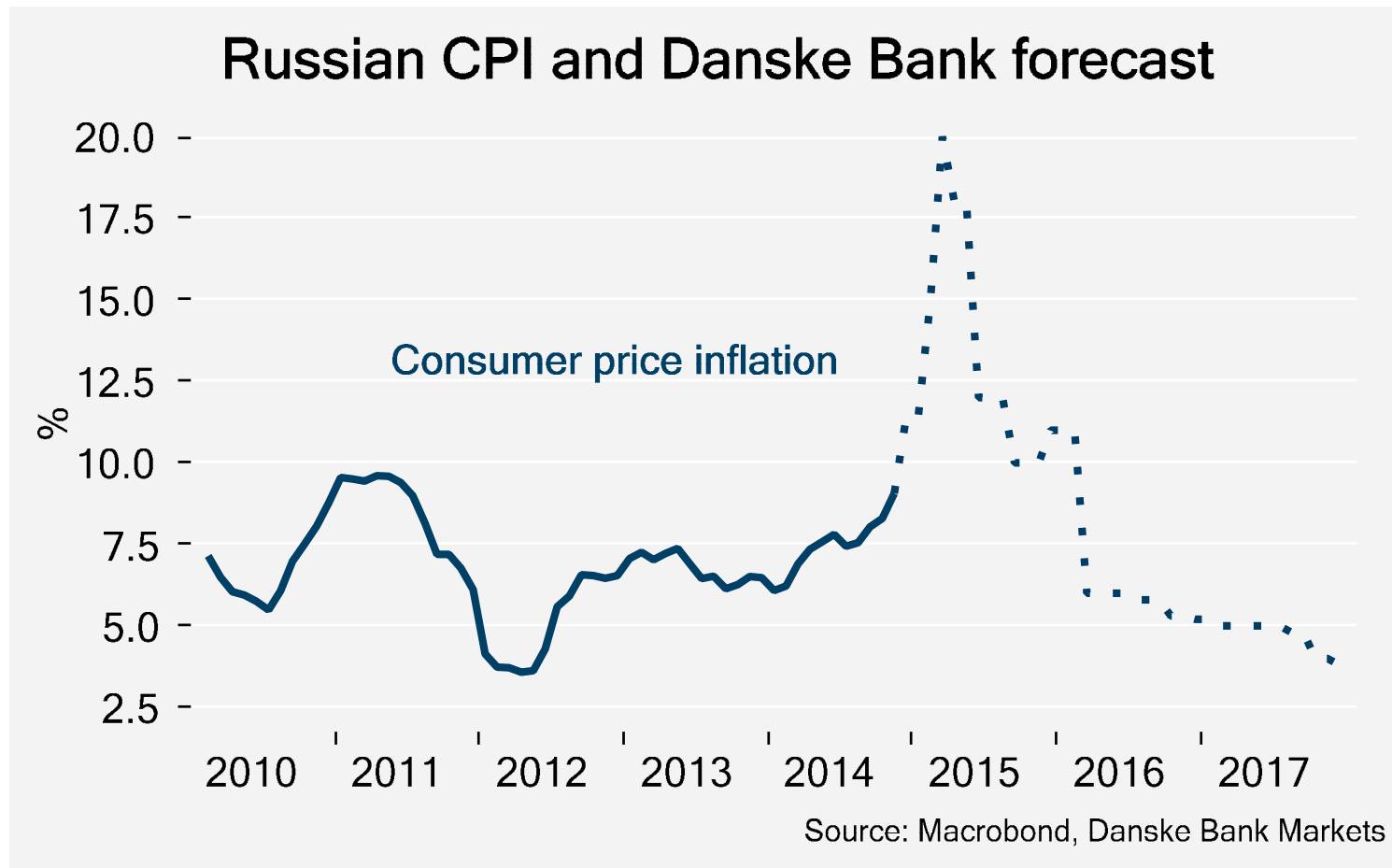
Deep recession ahead



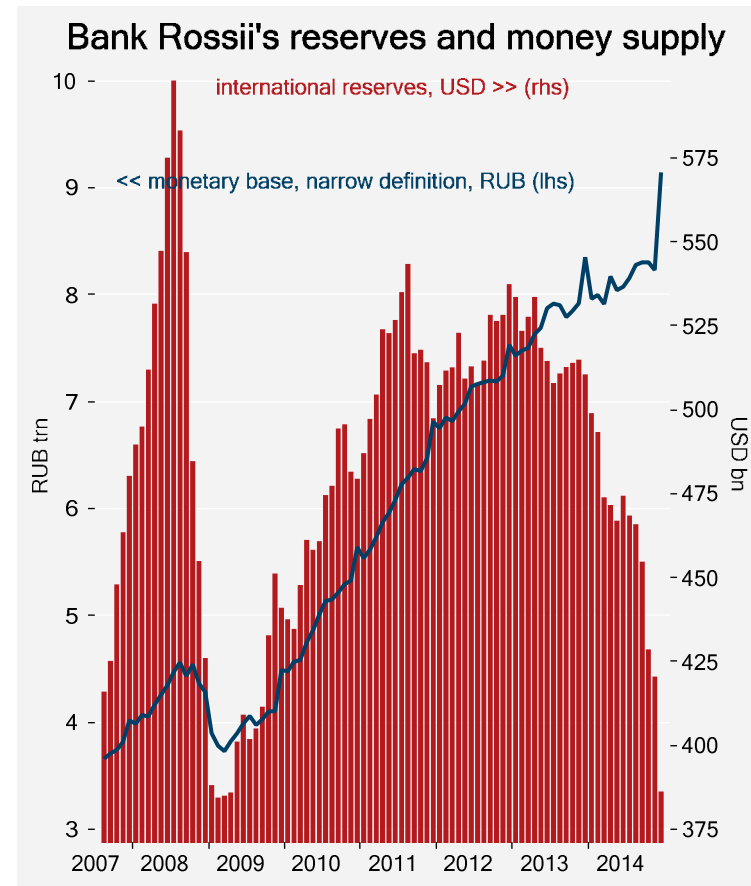
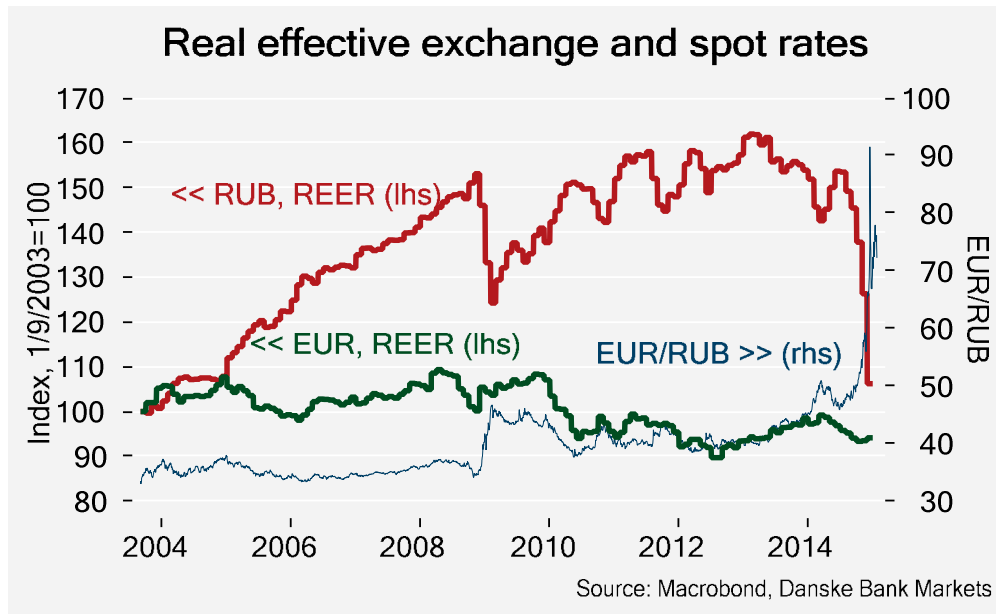


Source: Bank Rossii, Danske Bank Markets

Inflation climbs up on weak rouble and geopolitics

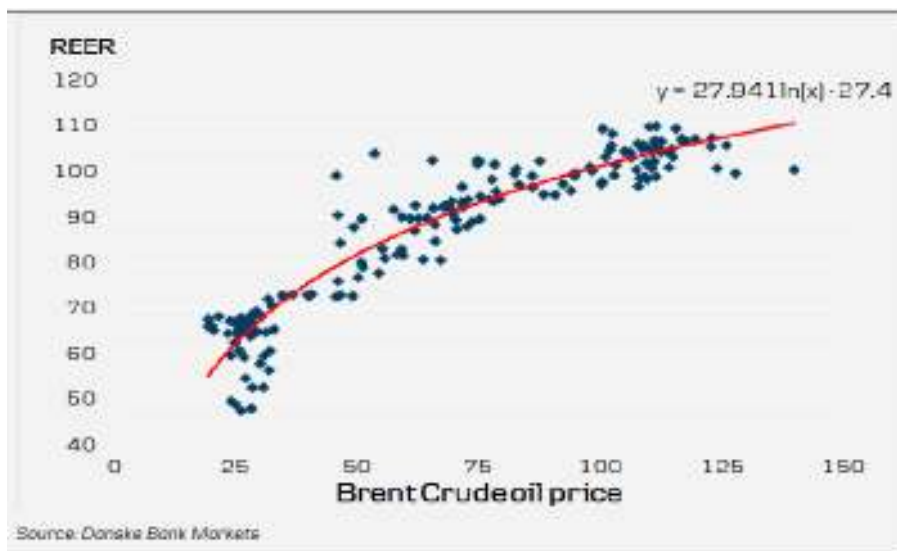


RUB: free float or free fall?



Source: Macrobond, Reuters EcoWin, Danske Bank Markets
(both charts)

Rouble risk: more about the oil price than geopolitics



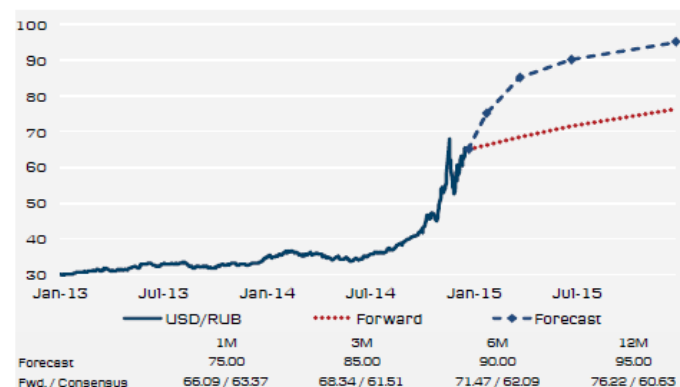
Macroeconomic and FX forecasts for Russia

Russian macro indicators and forecasts				
	2013	2014	2015	2016
GDP (% y/y)	1.3	-0.3	-7.9	-0.8
CPI (% Dec/Dec)	6.8	9.9	11	7.9
Private consump. (% y/y)	4.0	1.2	-5.5	-0.2
Fixed investments (% y/y)	-2.0	-3.7	-12	-1.2
Unemployment (%)	5.6	5.5	8.1	7.4
Current a/c (% of GDP)	2.0	1.0	-1.5	0.0

Source: Rosstat, Danske Bank Markets

USD/RUB

Forecast: 75(1M), 85(3M), 90(6M) and 95(12M)



Source: Danske Bank Markets

		EUR		USD		DKK		SEK		NOK	
		Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward	Danske	Forward
RUB	19-Jan-15	75.2		64.9		9.9		12.5		11.7	
	+1M	85.5	76.5	75.0	66.0	8.7	9.7	10.9	12.3	10.2	11.5
	+3M	95.2	79.2	85.0	68.2	7.8	9.4	9.8	11.9	9.5	11.1
	+6M	99.0	82.9	90.0	71.3	7.5	9.0	9.3	11.4	8.8	10.6
	+12M	106.4	88.7	95.0	76.1	7.0	8.4	8.5	10.6	7.8	10.0

Source: Macrobond, 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 this research report is Vladimir Miklashevsky, Economist, Trading Desk Strategist.

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