

Russia Economic Report 32: Policy Uncertainty Clouds Medium-Term Prospects

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The Russian economy is near stagnation, with continued lowered domestic demand leading to growth of 0.8 percent in the first half of 2014, similar to 0.9 percent in 2013, the World Bank said today in its latest Russia Economic Report launched in Moscow. Economic activity was already hamstrung by lingering structural problems and a wait-and-see attitude on the part of both businesses and consumers in 2013. An additional negative impact on the economy - besides slow structural reforms - came from increased geopolitical tensions and an uncertain policy environment. It is policy uncertainty about the economic course the country will take that is casting the longest shadow on Russias medium-term prospects.
In the first half of 2014, macroeconomic stability continued and Russia remains in possession of large buffers to uphold stability in the near future, said Birgit Hansl, World Bank Lead Economist for the Russian Federation and the main author of the Report. "However, there is little movement on the structural reform agenda, which could boost Russias growth potential in the medium-term. Both of these observations together are captured in the World Banks most likely scenario - the baseline scenario - with positive but low growth near stagnation in 2015 and 2016.
The World Banks report says there are substantial risks to the medium-term outlook for Russias 2014-2016 growth. As the Russian economy needed to internalize several rounds of sanctions, countersanctions and measures to stabilize the economy, this environment of higher risk lowered domestic demand. The baseline scenario is one of stagnation with projected 0.5 percent growth for 2014, 0.3 percent in 2015 and 0.4 percent and 2016. This baseline is paired with two alternative scenarios: an optimistic scenario foresees a small growth recovery to 0.9 percent in 2015 and 1.3 percent in 2016. A pessimistic scenario sees the economy slipping into a low-level recession, contracting by 0.9 percent in 2015 and 0.4 percent in 2016.
Several policy recommendations emerge from the report to unlock Russias growth. A return to higher growth in Russia will depend on solid private investment growth and a lift in consumer sentiment, which will require creating a predictable policy environment and addressing the unresolved structural reform agenda.
"This important policy effort should go hand in hand with renewed focus on improving the economys structural fundamentals to allow for more efficient markets, said Michal Rutkowski, World Bank Country Director for the Russian Federation. "The special focus part of our report suggests structural reform priorities to unlock Russias growth potential within the framework of finding a more diversified development path for the country.
A more balanced and diversified portfolio of national assets, including natural resources, capital, and economic institutions, will help overcome structural constraints to growth. Institutional weaknesses are now the main stumbling block on the road to greater economic efficiency and a higher growth potential. Structural reforms would need to focus on improving economic institutions to ensure stable public finances and well-managed volatility; improved education and infrastructure to make workers more productive; and stronger competition regimes to encourage private enterprises and entrepreneurship. Stabilization, education, and competition should be the reform priorities for the next decade.
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