KIEP Opinions

Russian Economy and the COVID-19 Pandemic: The Past, Current and Afterwards

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The impact of COVID-19 on the Russian economy was undoubtedly enormous, clearly, negatively. The GDP of the Russian economy shrank 3% in 2020, the sharpest contraction after the previous economic disaster in 2008. The two economic downturns resemble each other. They show that resource-dependent economies are susceptible to sudden declines in raw material prices, where they resort to too much. It is not anew that fossil fuel exports, including oil and natural gas, serve as a linchpin for the Russian economic system. Exports of the energy resources constitute a whopping 60% of all goods exports while accounting for more than a major bulk of government revenues. Excessive economic dependence on the resource sector has been a perennial concern, and the ominous premonition was correct again. The Russian economy contracted 8.5% in the second quarter of 2020 when the Ural oil price plummeted to $18 per barrel, reminiscent of the 2008 economic recession sparked by the sudden collapse of the oil price by more than 70% of its peak value.

Surprisingly, the 8.5% drop of the total production in the second quarter of 2020 turned out relatively modest compared to wealthier nations. For instance, the US and Germany suffered nearly 10% loss of their GDP, and the

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UK almost 20% loss over the same period. The Russian government's actions nullifying the economic impact of the unexpected pandemic were undoubtedly swift, clearly, positively. Despite the five cuts in the key interest rate in the previous year, the central bank of Russia again cut the key rate to 6.0% in February 2020, followed by a further cut to 5.5% in April. The fiscal authority was also quick to loosen the purse strings of the economy. The Russian government announced $28 billion worth of economic stimulus measures twice in March and April to counterbalance the hollowing domestic demand caused by the pandemic. In particular, intensive support for SMEs was compelling. The government prepared various debt relief measures and loan programs for SMEs to relax their debt stresses while pouring direct funds for them to ease payroll spending when faced with a mass furlough.

A series of hard-headed, perhaps a bit draconian, containment measures were also accompanied to mollify the vehement spread of the infectious disease. On March 25th 2020, President Putin announced the postponement of the Russian constitutional referendum due to the epidemic and did so. In the same month, international flights were grounded after the government ordered the civil aviation authority to suspend all regular and charter flights to and from the country. On March 29th, the Mayor of Moscow issued a stay-at-home order starting the next day. On March 30th, similar orders or recommendations were announced in numerous other federal jurisdictions, with many more announcing such restrictions over the next few days. The same day, the border was shut, with all border crossings closed. In April, the non-working period was prolonged twice, lasting until May 11th.

It might be safe to contend that the Russian economy's recovery outpaced expectations. The economy grew 10.3% in the second quarter of 2021 compared to the same period of 2020, recording its first positive growth in the last four quarters. Maxim Reshetnikov, the head of the Ministry of Economic Development, expressed appealing confidence in the speedy economic recovery, saying on average, in the first quarter of 2021, it was plus 0.3% to the pre-pandemic level. The recovery of the labor market is particularly encouraging. Russia's unemployment rate has continued to fall, and in July, finally returned to the level of 2019, before the epidemic. In July, the unemployment rate fell from 4.8% in the previous month to 4.5% in September 2019. The good news is not limited to the increase in the number of jobs. Real wages surged 4.9% year-on-year a month ago. The vitality of the labor market made private consumption sanguine. Retail sales, the yardstick for consumer demand, rose 4.7% year-on-year in July.

It seems not crystal-clear at this moment how much the national efforts responding to the pandemic have offset economic harms—conceivably, at least in part, due to the resurgence of the oil price. A more dubious question is whether or not the vigorous economic resurrection will persevere. Worries about inflation significantly weigh on the growth prospects of the Russian economy. The rapid recovery of private consumption, together with inflated government spending, has contributed to intensifying inflationary pressure. The inflation rate has stayed higher than the inflation target of 4.5%, demanding the Central Bank of Russia to raise the key rate despite the recent hike in July from 5.5% to 6.5%. High interest rates will result in a more sluggish recovery of private investment, not just dampening the rapid recovery of private consumption as well. The re-proliferation of COVID-19 due to the low vaccination rate can also be a problem. The vaccination rate is well below the government target of 60%. Also, about 90% of the recently confirmed coronavirus cases in Moscow appear to have been infected with the Delta variant of the virus. This is why the possibility of large-scale spread cannot be ruled out. The full recovery of the Russian economy is not yet done.