Global growth was sustained in the first quarter of 2018, but showed signs of moderation amid mixed incoming data in major economies. Oil prices, which rose 1 percent in March, gained considerable ground in mid-April with Brent exceeding $72/bbl for the first time since 2014. Oil prices have been supported by robust global demand, concerns about supply outages due to potential conflicts in Syria and Saudi Arabia and further output reductions in Venezuela. A stronger trade balance, which gained from higher value of commodity exports, anchored Russia's current account in the first quarter of 2018. In February 2018, industrial production growth slowed down on the back of lower growth in manufacturing. In March 2018, consumer inflation slightly accelerated. Labor market indicators improved in February. In the first two months of 2018, aided by higher oil revenues and lower expenditures, the overall federal budget stance and general government budget surplus improved significantly—by 1.1 and 2.1 percent of GDP respectively—compared to the same period in 2017. In February, the banking sector remained largely stable. On April 6th, the U.S. imposed new sanctions on seven Russian oligarchs, their 12 companies, 17 senior Russian government officials, and a state-owned Russian weapons trading company and its subsidiary. The fiscal impact of the April 6th sanctions remains to be seen as it will depend on the nature and magnitude of public support to affected firms. Possible public intervention could increase the state footprint in the economy, further affecting competition and productivity.

The Global Context
Global growth was sustained in 2018Q1, but it showed signs of moderation amid mixed incoming data in major economies. In March, business and consumer confidence were still elevated but dropped from their post-crisis highs of January-February. Global PMI surveys fell significantly, reaching a 16-month low in March as activity decelerated in both manufacturing and services. In China, growth continues to moderate but industrial production has been robust so far this year. The recent tariff increases announced by the United States and China, if implemented, would affect about one-tenth of China’s exports to the U.S., and more than one third of U.S. exports to China. The impact of these measures will largely depend on their ultimate scope, but a rise in trade policy uncertainty could itself weigh on global confidence, financial market sentiment, and eventually on activity.

Oil prices, which rose 1 percent in March, gained considerable ground in mid-April with Brent exceeding $72/bbl for the first time since 2014 (Figure 1). Oil prices averaged $65/bbl during 2018Q1, almost $12/bbl above 2017Q1. On the supply side, U.S. oil production rose to a record 10.3 mb/d in March after bottoming in mid-2016 at 8.7 mb/d. The rig count in the U.S., a rough measure of future supply response, followed suit. However, prices have been aided by robust global demand, concerns about supply outages due to potential conflicts in Syria and Saudi Arabia and further output reductions in Venezuela. On the policy front, OPEC producers have exceeded the December 2016 agreed cuts by 47 percent while non-OPEC producers are 15 percent below their targeted cuts. Moreover, Saudi Arabia has publicly favored a longer-term arrangement on supply management between OPEC and key non-OPEC producers, with more information expected to be revealed after the June 22nd OPEC meeting.

Figure 1: Oil prices, which rose 1 percent in March 2018, gained considerable ground in mid-April

Russia’s Recent Developments
In March 2018, the ruble slightly depreciated with respect to the U.S. dollar (Figure 2). Despite oil prices increasing by 1.6 percent in March compared to the previous month, the ruble exchange rate with respect to the U.S. dollar depreciated by
0.5 percent as the Federal Reserve increased the policy rate by 25 basis points on March 21st and the Central Bank of Russia (CBR) continued its easing cycle. In the beginning of April, new sanctions led to a sell-off of Russian financial assets and the ruble’s depreciation. By April 18th, the ruble lost 7.5 percent with respect to the U.S. dollar as compared to the end of March. Yet the ruble was supported by growing oil prices.

A stronger trade balance supported the current account in the first quarter of 2018. In the first three months of 2018, the current account increased to US$28.8 billion from US$22.3 billion in the same period last year. An increase in the trade surplus, due to higher exports supported by the increase in oil prices, was the key factor behind the strengthening of the current account surplus. Net private capital outflows in the January-March 2018 period reached US$13.4 billion compared to US$16.4 billion from January-March 2017, and this was largely due to an increase in the foreign assets of the non-banking sector. The international reserves gained US$19.3 billion in the January-February 2018 period compared to an increase of US$11.3 billion in the January-February 2017 period on the back of foreign currency purchases by the Ministry of Finance and the repayment of previously provided liquidity in foreign currencies by credit institutions to the Bank of Russia.

In February 2018, industrial production growth slowed down to 1.5 percent, y/y, compared to 2.9 percent, y/y, in January 2018 (Figure 3). It decreased by 1.3 percent, m/m, sa. In February 2018, manufacturing expanded by 1.9 percent, y/y, compared to a growth of 4.7 percent, y/y, in January 2018. Growth was supported by chemicals and production of other transportation equipment. In February 2018, mineral resource extraction grew by 0.3 percent, y/y, supported by growth in natural gas extraction and mining services, but it was dragged down by the continued contraction in the production of crude oil. In February 2018, Russia’s production of crude oil shrank by 1.3 percent, y/y, as Russia’s compliance to the December 2016 OPEC+ agreement improved, compared to the same period last year.

In March 2018, consumer inflation slightly accelerated (Figure 4). The 12-month Consumer Price Index (CPI) rose to the level of 2.4 percent, y/y, from 2.2 percent, y/y, in February 2018. An increase in food inflation contributed to the CPI growth. In March, core inflation remained at about the same level as in February (1.8 percent, y/y, vs. 1.9 percent, y/y), indicating low inflation pressures. Inflation expectations remain on the high side, and marginally increased from 8.4 percent in February to 8.5 percent in March.

Labor market indicators improved in February 2018. The unemployment rate decreased in February by 0.2 percentage points to the level of 5 percent. The seasonally adjusted rate declined by the same amount and reached 4.7 percent (Figure 5). Real wages continued to grow and increased in February.
2018 by 9.7 percent compared to the same period in the previous year and by 1.5 percent compared to January 2018 after seasonal adjustment. Real disposable incomes increased in February by 4.4 percent compared to the same period in 2017. They also rose by 4.7 percent compared to January 2017 after seasonal adjustment. However, this indicator is volatile and it is driven, to a large extent, by sources of income that are not registered by statistics. Pensions were indexed in the beginning of the year and their real growth was 1.1 percent compared to February 2017.

**Figure 5: Labor market indicators improved in February 2018**

![Labor market indicators](image_url)

Source: Rosstat, Haver Analytics, World Bank team.

In the first two months of 2018, aided by higher oil revenues and lower expenditures, the federal budget primary surplus strengthened to 2.7 percent of GDP from 0.4 percent of GDP in the same period last year. While higher oil prices prompted an increase in federal budget oil revenues from 8.1 percent of GDP in January - February 2017 to 9.5 percent of GDP in January - February 2018, non-oil revenues decreased from 10.2 percent of GDP to 9.2 percent of GDP. Such a drop in non-oil revenues is largely attributed to lower receipts of excise tax, compared to a high base last year due to uneven tax collection last year. Federal budget primary expenditures decreased from 19 percent of GDP in January-February 2017 to 17 percent of GDP in January-February 2018 mainly due to lower spending on social policy due to the one-off pension payments in January 2017. The overall federal budget stance improved from 0.6 percent of GDP deficit in January - February 2017 to 1.7 percent of GDP surplus in January - February 2018. General government budget surplus improved from 0.2 percent of GDP in January - February 2017 to 2.3 percent of GDP in January - February 2018.

**Figure 6: In February 2018, the banking sector remained largely stable**

![Banking sector stability](image_url)

Source: CBR.

The CBR announced that it will create a “bad bank” to transfer distressed assets in the amount of RUB 1.1 trillion (US$17 billion) from the three large private banks that were bailed out in 2017 via the CBR Banking Sector Consolidation Fund. The “bad bank” will be based on a branch of Otkritie (Bank Trust), which was rescued by the CBR in August 2017, and it will function as a fund. It will receive a loan of RUB1.1 trillion from the CBR at the preferential rate of 0.5 percent.

On April 6, 2018, the U.S. imposed new sanctions on seven Russian oligarchs, their 12 companies, 17 senior Russian
government officials, and a state-owned Russian weapons trading company and its subsidiary. All assets of the designated individuals and entities subject to U.S. jurisdiction were frozen, and U.S. persons are generally prohibited from any dealings with them. The imposition of sanctions, coupled with increased geopolitical tension, caused a massive sell-off of Russia’s financial assets and the ruble’s depreciation. The Ministry of Finance postponed its domestic debt auction on the back of the interest rate increase (resumed auctions on April 18) and refrained from currency purchases in the budget rule framework to stabilize the FX market. The Government of Russia is working on measures to support sanctioned companies. However, by April 18th, the markets calmed down to some extent and the ruble gained back about 50 percent of its losses. The fiscal impact of sanctions is not clear and it will depend on the nature and magnitude of public support of affected firms. However, any public intervention could increase the state footprint, further affecting competition and productivity. Russia’s largest bank – Sberbank –, which is state-owned, may become vulnerable to sanctions due to lending to certain Russian companies. However, according to Sberbank management, loans to companies on the new sanctions list — which are now barred from making payments in dollars or accessing western markets — total “no more than 2.5 percent” of Sberbank’s total assets.