

## Economics Group

Jay H. Bryson, Global Economist  
[jay.bryson@wellsfargo.com](mailto:jay.bryson@wellsfargo.com) • (704) 410-3274

### Russian GDP Growth Downshifts in Q3-2017

**Real GDP growth slowed to 1.8 percent in Q3 from 2.5 percent in Q2, which was weaker than most analysts had expected. Growth in consumer spending likely remained solid in Q3.**

#### Growth in Consumer Spending Likely Remained Solid

Preliminary data released today showed that real GDP in Russia grew 1.8 percent on a year-ago basis in Q3-2017 (top chart). The outturn represents a slowdown from the 2.5 percent rate registered during the previous quarter and came up a bit short of the 2.0 percent rate that the market consensus had anticipated.

A breakdown of the GDP data into its underlying demand-side components or into industry sectors is not yet readily available. However, previously-released monthly data provide some insights into the underlying drivers of the Russian economy at present. On a positive note, growth in real retail spending continued to strengthen in the third quarter (middle chart). The strength in retail spending likely means that growth in real personal consumption expenditures, which includes spending on goods (i.e., retail sales) as well as services, likely remained solid in Q3.

The combination of the Ukrainian crisis and the collapse in oil prices caused the Russian ruble to nosedive between 2014 and 2016. This sharp depreciation in the value of the ruble caused inflation to skyrocket. The associated downturn in real disposable income from the moonshot in inflation led to weakness in consumer spending. However, now that the ruble has rebounded, inflation has receded markedly (bottom chart). The acceleration in real wages has helped to support renewed growth in real retail spending.

So if growth in real consumer spending likely remained solid in Q3, from where did the slowdown in overall GDP growth emanate? We know that growth in Russian industrial production slowed to about 1 percent in Q3 from nearly 4 percent year-over-year in Q2. So there appears to be two likely candidates. We do not have data on Russian export volumes, but growth in the value of Russian exports downshifted a bit in Q3, so some of the quarter's slowdown may have emanated from exports. That said, global economic growth has been rather buoyant in the past few quarters, so it's doubtful that growth in real exports would have slowed too much.

The other candidate would appear to be investment spending, which weakened significantly during the 2014-2016 recession but has staged a bit of a comeback in recent quarters. That said, the investment environment in Russia is not exactly stellar at present with international sanctions still in place and with oil prices remaining depressed. Although we look for investment spending to continue to grow in the next few years, a return to the run-rate of the early years of the past decade, when double digit growth rates were the norm, does not look likely. Indeed, our forecast looks for the Russian economy to eke out real GDP growth rates of roughly 2 percent per annum in 2018 and 2019.



## Wells Fargo Securities Economics Group

Diane Schumaker-Krieg	Global Head of Research, Economics & Strategy	(704) 410-1801 (212) 214-5070	diane.schumaker@wellsfargo.com
John E. Silvia, Ph.D.	Chief Economist	(704) 410-3275	john.silvia@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Jay H. Bryson, Ph.D.	Global Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	Currency Strategist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Eugenio J. Alemán, Ph.D.	Senior Economist	(704) 410-3273	eugenio.j.aleman@wellsfargo.com
Azhar Iqbal	Econometrician	(704) 410-3270	azhar.iqbal@wellsfargo.com
Tim Quinlan	Senior Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Eric Viloría, CFA	Currency Strategist	(212) 214-5637	eric.viloria@wellsfargo.com
Sarah House	Economist	(704) 410-3282	sarah.house@wellsfargo.com
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Jamie Feik	Economist	(704) 410-3291	jamie.feik@wellsfargo.com
Erik Nelson	Currency Strategist	(212) 214-5652	erik.f.nelson@wellsfargo.com
Michael Pugliese	Economic Analyst	(704) 410-3156	michael.d.pugliese@wellsfargo.com
E. Harry Pershing	Economic Analyst	(704) 410-3034	edward.h.pershing@wellsfargo.com
Hank Carmichael	Economic Analyst	(704) 410-3059	john.h.carmichael@wellsfargo.com
Ariana Vaisey	Economic Analyst	(704) 410-1309	ariana.b.vaisey@wellsfargo.com
Abigail Kinnaman	Economic Analyst	(704) 410-1570	abigail.kinnaman@wellsfargo.com
Shannon Seery	Economic Analyst	(704) 410-1681	shannon.seery@wellsfargo.com
Donna LaFleur	Executive Assistant	(704) 410-3279	donna.lafleur@wellsfargo.com
Dawne Howes	Administrative Assistant	(704) 410-3272	dawne.howes@wellsfargo.com

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