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IMF Cuts 2014 Russian Economic Forecast to 1.3%

By The Moscow Times

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The International Monetary Fund cut its 2014 economic growth forecast for Russia by two-thirds on Tuesday and warned that downside risks remain on geopolitical uncertainties after Moscow's takeover of Crimea.

The Fund cut its gross domestic product growth forecast to 1.3 percent from an earlier 2 percent, revising down its estimates for the third time in a row, from an initial 3 percent.

"The balance of risks [for Russia and neighbors] remains to the downside, considering rising geopolitical uncertainties following the takeover of Crimea by Russia, tightening financial conditions, and volatile capital flows," the Fund said in a report.

"Intensification of sanctions and counter-sanctions could affect trade flows and financial assets."

The IMF forecast follows gloomier estimates from the World Bank of the likely economic damage from the Kremlin's standoff with the West over Ukraine. The bank warned the Russian economy may contract by 1.8 percent if the conflict escalates and grow by 1.1 percent at best.

The IMF is also more optimistic in its GDP growth estimates than the Russian Economic Development Ministry, which said earlier this month that economic expansion may come "significantly" below 1 percent if current trends continue.

The U.S. and the European Union have imposed asset freezes and visa bans on a group of Russians and threatened economic sanctions if Moscow escalates the crisis further. The standoff is estimated to result in up to $70 billion in capital flight from Russia in the first quarter.

The World Bank says capital outflow may come to $150 billion if the crisis deepens. The IMF has not provided estimates of how much money could flee Russia this year.

The Fund said Russia's slowdown would have a spillover effect on former Soviet republics such as Kazakhstan, Armenia or Tajikistan.

"A slowdown in Russia owing to unsettled conditions would affect the Caucasus and Central Asia through both real sector and financial channels, particularly if energy supply is disrupted and oil and gas prices rise," the Fund said.

Consumer price inflation is likely to average 5.8 percent during the year, the IMF said, and is likely to remain above 5 percent, the midpoint of Russia's target range, by year-end.

The Central Bank said last month that inflation is likely to come at between 5 and 6 percent by year-end, within its 3.5 to 6.5 percent target range but above the midpoint.

The ruble's weakening was the main reason for the rise in annual inflation last month to 6.9 percent from 6.2 percent a month earlier.

"Russia should continue to rely on exchange rate flexibility to facilitate adjustments while avoiding excessive volatility, keep monetary policy focused on anchoring inflation, and maintain a broadly neutral structural fiscal policy," the Fund said.

The Central Bank was forced in March to raise its key lending rate by 150 basis points to 7 percent to stem off capital flight after Russia asserted its right to intervene militarily in Ukraine.

The bank also introduced temporary changes to its rules that enable larger forex market interventions. It expended some $25 billion to support the ruble in March, putting on hold plans to make the ruble more flexible.

Last week, Central Bank Governor Elvira Nabiullina said the bank did not plan to cut its key lending rate until its June meeting at the earliest, as inflation concerns remain.

The ruble is down 7 percent against the dollar this year, after falling 11 percent in March at the peak of the crisis.

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