

CIS region faces economic downturn and uncertain prospects in 2016-17, says UN report *Region to feel negative influence of Russian economy slowdown*

Moscow, 26 January – Economic activity in the Commonwealth of Independent States (CIS) area contracted sharply in 2015, as the region suffered from a deterioration in the terms of trade, precarious access to external finance and high levels of uncertainty, according to the United Nations World Economic Situation and Prospects 2016 report, launched today.

Contracting output in the Russian Federation had a depressing influence throughout the region. Declines were also observed in other large economies, including Belarus and Ukraine. The aggregate Gross Domestic Product (GDP) of the CIS and Georgia is estimated to have contracted by about 3.0 per cent in 2015. A return to growth is expected in 2016, but the recovery will be limited, with GDP increasing by about 0.7 per cent in 2016 and 1.8 per cent in 2017.

Domestic demand plummets

The region has suffered from a combination of an adverse external environment and domestic contractionary forces. Falling real wages, eroded by inflation, and worsened access to credit depressed household consumption. Investment was deterred by poor economic prospects and high financing costs, as well as the diversion of retained earnings to more profitable financial assets. A decline in remittances, predominantly from the Russian Federation, which almost fell by half in dollar terms, and other spillover effects, including reduced exports and investment, largely offset the impact of lower energy prices for the region's small energy-importing countries.

Inflation accelerates in many economies, while labour markets deteriorate

Inflation rose throughout the region, driven by the sharp depreciation of national currencies. Weak domestic demand partly offset the inflationary pressures that resulted from the depreciation, while price controls remained in place in some countries. As exchange rates are expected to stabilize somewhat in 2016, inflationary pressures should moderate. In some countries, however, inflation will remain in double digits, while in other countries, currency interventions to reduce exchange-rate pressures have depleted foreign-exchange reserves.

The sharp deterioration in economic performance took its toll on the region's labour markets, including in the Russian Federation and Ukraine. As a lagging indicator of economic activity, unemployment is expected to further increase in the CIS in 2016, before declining in 2017.

Russian economy expected to stagnate in 2016

According to the report, the Russian economy will stagnate in 2016, before returning to a modest growth of 1.2 per cent in 2017. Investment in 2015 contracted sharply, despite growing profits, which were mainly used to reduce corporate debt. The unemployment rate has marginally increased, despite the preference of cutting wages, rather than labour. Inflation remains high, driven by the sharp currency depreciation. Although net private capital outflows from the economy moderated in 2015, they may still surpass US\$60 billion. These capital outflows have been associated with a substantial reduction in external debt as the corporate sector repays loans instead of rolling them over.

Sharp economic contraction in Ukraine to be followed by zero growth in 2016

In Ukraine, the destruction of productive capacity due to the conflict in the East of the country and the precarious access to the Russian market led to a sharp fall of exports. However, with imports plummeting, net external demand partly offset the contraction of domestic demand—consumption, in particular.

Unemployment, which increased sharply throughout 2014, continued to climb higher. Higher gas prices added to headline inflation, which was expected to average about 50 per cent in 2015. The economy is expected to shrink by 10.5 per cent in 2015, post a zero growth in 2016 and to expand by a mere 2.1 per cent in 2017.

Better picture in Central Asia and Caucasus

In Azerbaijan, Turkmenistan and Uzbekistan, public investment programmes boosted growth in 2015. For the region's small energy-importing countries, the decline in remittances and other spillover effects, including reduced exports and investment from the Russian Federation, largely offset the impact of lower energy prices. Still, a number of these countries still managed to register decent growth rates in 2015. This may be explained by one-off factors, such as base-year effects or ample agricultural output, but also increased linkages with China.

Risks and uncertainties ahead but also new possibilities

The economies of the CIS face a difficult external environment, which will heighten internal vulnerabilities. A persistent period of low commodity prices makes fiscal consolidation unavoidable. Low investment will constrain future growth and prevent progress towards much-needed economic diversification. In many countries, the persistent fragilities in the banking systems have been exacerbated by the weakening of exchange rates in highly dollarized financial systems. Geopolitical tensions continue to weigh on business sentiment. On the positive side, the Russian Federation is less exposed than other emerging markets to growing financial uncertainty, given the lack of access to international capital markets due to the sanctions. The establishment of the Eurasian Economic Union of Armenia, Belarus, Kazakhstan, Kyrgyzstan and the Russian Federation on the basis of the former Customs Union in January 2015 opens new possibilities for increased trade and investment in the region, although many aspects of the regional integration still have to be negotiated.

About the report: *The World Economic Situation and Prospects report is produced annually by the UN Department of Economic and Social Affairs (UN/DESA), the UN Conference on Trade and Development (UNCTAD), the five UN regional commissions and the World Tourism Organisation (UNWTO). The report is available from <http://bit.ly/WESP>.*

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