Russia Takes Double Punch as Vanishing Workers Fan Prices

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Photographer: Andrey Rudakov/Bloomberg. An employee works on the assembly of a truck cabin on the production line at the OAO KamAZ plant in Naberezhnye Chelny, Russ

The aging workforce is packing a double punch for the Russian economy

The unborn generation of the 1990s, a period of hyperinflation and instability after the Soviet breakup, left the nation depleted of younger workers. Unemployment is at a record low, putting pressure on wages (RUMEREAL) and helping keep inflation near the fastest since 2011. The poor demographics are shaving 0.5 percentage point off economic growth a year, according to the Higher School of Economics in Moscow, which estimates the working-age population will shrink by as many as 15 million people, or more than the size of the Russian capital, by 2030.
Aging populations are unsettling central bankers from Tokyo to Frankfurt in their struggle to prevent deflation as older workers tend to defer consumption in favor of savings. Russia faces the opposite threat: entrenched inflation that risks shackling monetary policy already lurching from one crisis to another since Crimea was annexed in March.

“Taking into account low unemployment and tight supply on the labor market, wages will remain at a high level, affecting inflation,” said Natalia Orlova, chief economist at Alfa Bank in Moscow. With the central bank increasingly drawing attention to poor demographics, it’s “in effect saying it can do nothing for the economy, whose problems are structural in character.”

**Demographic Factor**

Russia is caught in a vise of elevated inflation and stalling economic growth. The central bank, which has increased borrowing costs three times this year, has pointed to demographics as a long-term drag on the economy in every statement since April after meetings to review interest rates.

Following last week’s decision to hold the benchmark rate at 8 percent, the central bank used some of the strongest language yet, attributing “anemic” economic growth mostly to “structural reasons” and saying that “the long-term demographic trends” are squeezing labor supply.

“We have actually started to monitor more attentively what happens on the labor market in order to react to factors affecting the pace of economic growth,” central bank Chairman Elvira Nabiullina said at a Sept. 12 news conference following the policy meeting. “Under the influence of demographic trends, there is a deficit of labor supply, reflected in the decline of the working-age and economically active population.”

**Economy Halts**

That doesn’t bode well for a country already besieged by U.S. and European sanctions over Ukraine and facing the slowest economic growth since a 2009 slump. The government predicts the $2 trillion economy will expand 0.5 percent this year after a 1.3 percent gain in 2013, a far cry from average growth of about 7 percent a year during President Vladimir Putin’s first two terms in the Kremlin from 2000 to 2008.
The probability of a recession in the next 12 months rose to 65 percent from 50 percent, the highest since the first such Bloomberg survey in June 2012, according to the median estimate of 26 economists in a poll last month.

Demographic trends are often a bellwether for an economic future. A report by UBS AG last year traced Asia’s economic expansion during the past five decades to rapid labor-force growth fed by younger and growing populations. In 2012, the Bank of Japan governor attributed the country’s weak growth during the previous 10 years particularly to “rapid aging.”

For Russian policy makers, the demographic challenges underscore the limits of their ability to chart an economic path.

**Inflation Focus**

The central bank has looked past the slowdown and focused increasingly on curbing price growth amid plans to shift to inflation targeting next year. Its main lending rate was last cut in December 2011 and inflation has held above target for 24 months. Last week, the central bank said inflation is on course to miss policy makers’ goal in 2015 for a fourth straight year.

Nabiullina said the central bank’s medium-term target of 4 percent will anchor inflation expectations and create the conditions for long-term savings and investment. Prices rose 7.6 percent, almost twice that goal, from a year earlier last month, when inflation expectations registered a “noticeable” jump for the coming year.

The tight labor market is fanning price pressures. Wages adjusted for inflation climbed an average of 3 percent in the first eight months even as productivity gains are growing at the weakest clip since 2009. In Germany, real wages are set to grow 1.9 percent this year, the most since 1992, following wage increases negotiated by labor unions.

**Unemployment Record**

Russia’s joblessness hit a record-low of 4.8 percent in August, decreasing from 4.9 percent a month earlier, the Federal Statistics Service said today in Moscow. That’s more than 5 percentage points below the average unemployment rate in the European Union.

After contracting by 500,000 people a year since 2006, the working population is set to shrink at double that pace during the next five or six years, the Higher School of Economics estimates. People aged 41 to 50 make up the most numerous group at
Russian companies and the shortage of qualified employees is leading to “overstated” salary demands, according to a 2012 report by OAO Sberbank, Russia's biggest lender.

Russia has made inroads in stemming the demographic crisis after its population fell to 142.7 million in 2009 from 148.3 million in 1991, the year the Soviet Union collapsed, as the government introduced measures such as payments to mothers with multiple children. For the first time in its post-Soviet history, births exceeded deaths by about 20,000 people in 2013, according to the Federal Statistics Service.

Demographic ‘Hole’

Yet it will take years for demographic improvements to filter through. The country is falling into a longtime demographic “hole” and won’t be able to offset its labor shortage with younger workers, later retirement or greater participation by women, Rostislav Kapeliushnikov and Alexei Oschepkov, analysts at the Labor Research Center of the Higher School of Economics, said in a July article published in the magazine Voprosy Ekonomiki, or Problems of Economics.

Migration may act to offset the role of demographics as a major restraining factor on the economy, according to Evgeny Gavrilenkov, chief economist at Sberbank CIB.

Migrants, Mobility

“On one hand, migrant inflows will partially compensate for the decline in the working-age population and on the other, there’s a huge potential to increase labor mobility inside the country,” Gavrilenkov said. “All problems can be solved.”

While the graying of the world is putting a brake on economic growth, in Russia it also represents a further risk to the inflation outlook. That’s because consumption patterns of Russian pensioners differ from retirees in developed economies.

Rather than pinching pennies, older Russians spend the bulk of their pensions on food and medicine, according to Julia Tsepliaeva, head of macroeconomic research at Sberbank. The two categories account for more than one-third of the consumer basket used for calculating inflation.

The share of Russian pensioners may jump to 29 percent of the population by 2030 from 23 percent last year, the statistics service estimates.

Larisa Garkusha, a 71-year-old Muscovite, is typical in that regard.
“My husband and I spend our pensions on day-to-day costs, housing -- we don’t set anything aside from our pensions because that’s impossible,” said Garkusha, who retired 10 years ago after working in a private company. “But we use money we saved when we were working to travel abroad once a year.”

How policy makers navigate the economic crosscurrents may well determine Russia’s ability to weather its slowdown. With demographics, they can do little more than watch.

The demographic “decline has the character of a long-term trend and will have a huge impact on all aspects of economic life in the country’s economic life,” Kapeliushnikov and Oschepekov said.

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