

The costs of war are driving the economy: Russia's economic situation in 2024

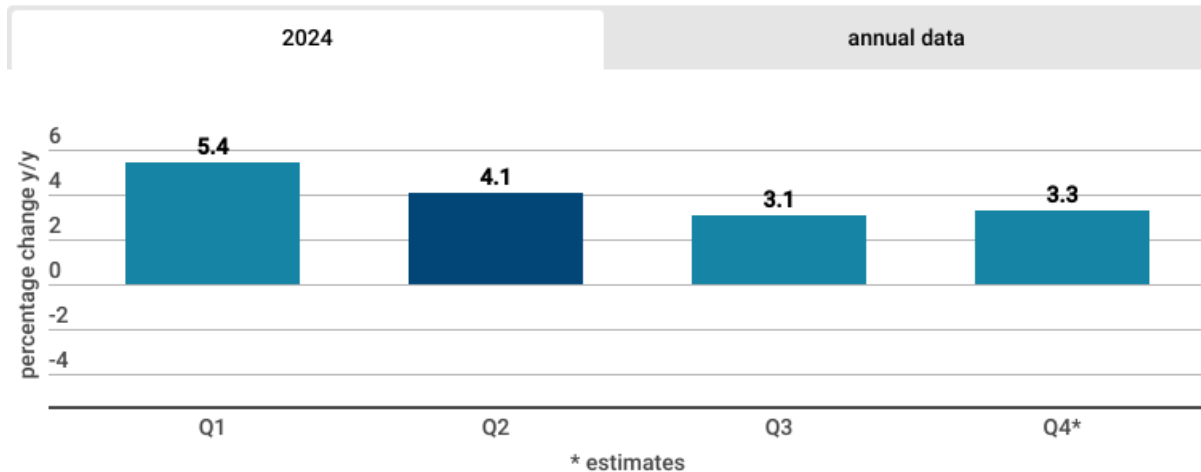
Iwona Wiśniewska

The sharp increase in wartime budget spending in 2024 has helped to sustain Russia's high economic growth rates, particularly double-digit growth in manufacturing industries serving the military. However, the number of economic challenges facing the government is rising. A shortage of labour has led to wage increases outpacing productivity growth. Domestic industry is unable to meet surging demand, while sanctions prevent shortages from being covered by imports. The central bank has so far failed to curb rising inflation. Consequently, increasing loan interest rates are negatively impacting investment activity. According to forecasts, these mounting problems are expected to slow economic growth in 2025 to 2.5% of GDP (according to the government) or 1–2% of GDP (according to the central bank).

In 2024, Russia's **GDP grew** by 4.1%, matching the rate of the previous year,^[1] and significantly exceeding initial projections. In December 2023, the government forecast growth of 2.3%, later revising its estimate to 3.9% in September 2024. Although strong growth momentum in the first half of the year slowed considerably in the third quarter, a further increase in budget spending towards the end of the year revitalised growth. Overall, the government estimated that additional budgetary and quasi-budgetary funds in the Russian economy, including investments from the National Welfare Fund (NWF), accounted for over 3% of GDP in 2024. Between 2022 and 2024, the so-called 'budgetary impulse' was estimated at over 10% of GDP.

These funds were used to sustain demand (through measures such as pension indexation and payments to active soldiers) while also supporting supply. Businesses benefited from subsidies, tax breaks for selected sectors, such as IT, and reduced import duties on certain goods. Preferential loans constituted another important channel of support, including mortgage lending and financing for the defence sector.

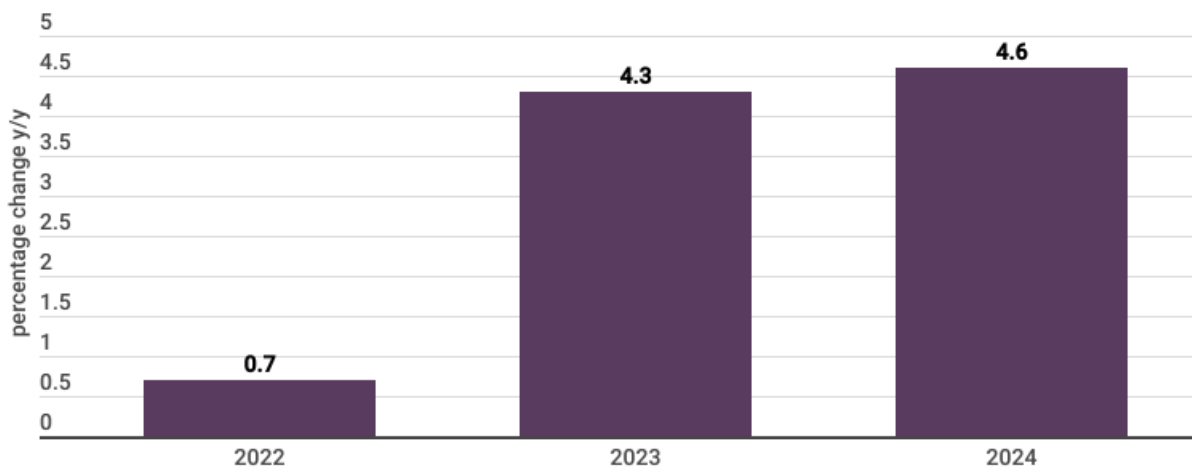
Chart 1. Russia's GDP



Source: Rosstat.

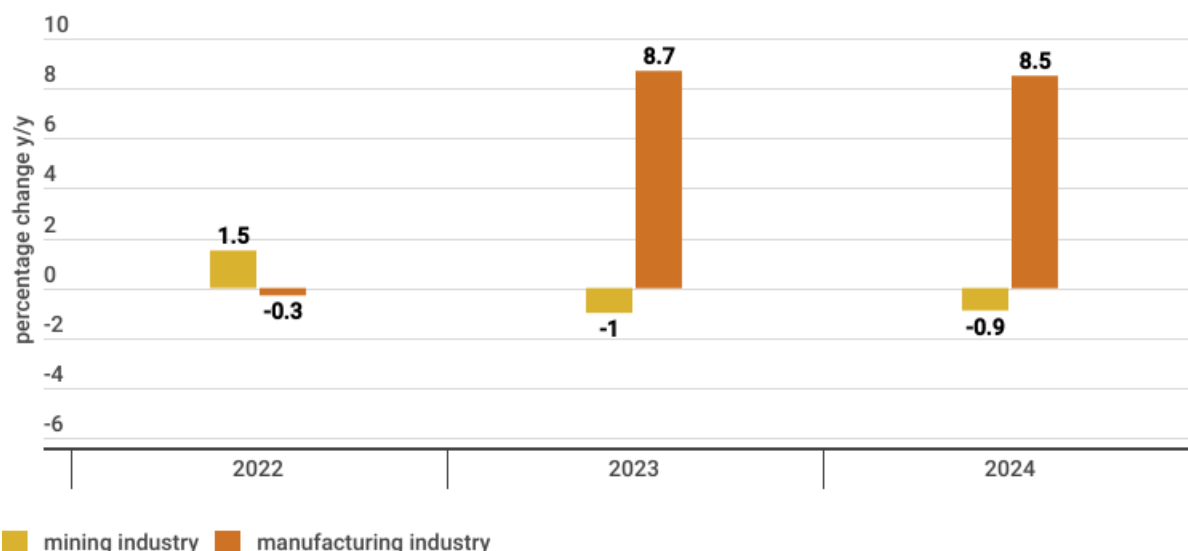
Industrial production in 2024 continued to grow at a dynamic pace, driven by strong performance in the manufacturing sector. However, the mining industry recorded another year of declining output, primarily due to the oil sector, which is estimated to have reduced production by approximately 1.5% (the government has not published official statistics since 2022). The coal sector also experienced a decline, with output falling by 0.6%. After two years of sharp declines in natural gas production, Russia managed to increase output, with Gazprom reporting a 16% rise.^[2] Consequently, the economic performance of companies operating in the mining industry has deteriorated. The coal industry is in the most challenging position; at the end of 2024, it recorded financial losses, with over 50% of companies reporting negative results.

Chart 2. Industrial production, 2022–2024



Source: Rosstat.

Chart 3. Production in selected industries



Source: Rosstat.

Growth in **manufacturing industry** output was primarily driven by sectors serving wartime needs. The government generated demand for their output, for example, by placing orders for ammunition and military equipment, often paying in advance for contracts. In 2024, planned budgetary spending on national defence (including military procurement) was expected to total approximately \$108 billion (around 27% of total budgetary spending); however, the actual figure was even higher. The defence sector also benefited from preferential loans, government subsidies for research and development, and extra-budgetary funds. For example, in January 2025, the government invested 111 billion roubles from the National Welfare Fund (NWF) into the state-owned company Rostec.

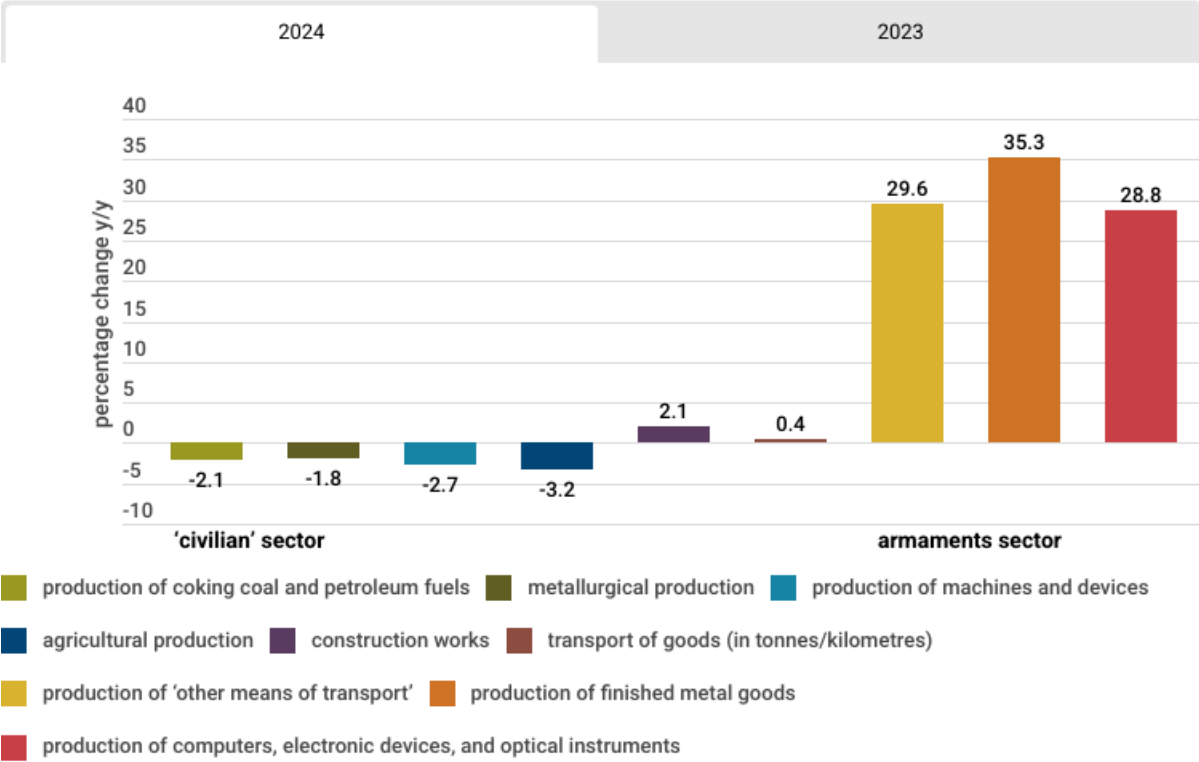
In Russian statistics, the **armaments sector** is not categorised separately. However, industries reporting results for enterprises within this sector have shown anomalous growth. For example, 'production of other means of transport' includes shipbuilding, aerospace manufacturing, and tank production, while 'production of finished metal products' includes ammunition manufacturing. It is important to note that defence industry enterprises operate outside the market economy, and prices for their products are set arbitrarily. Given the military's substantial current demand, the armed forces procure everything the sector can produce, regardless of the quality of the equipment.

The accumulation of financial, material, and human resources in the armaments sector is causing significant difficulties for industries **serving civilian needs**, which are unable to compete effectively. This is particularly evident in the context of rising production costs, driven primarily by increasing labour expenses and sanctions that restrict access to technology and components.

Growth in the **construction sector** has also slowed significantly, despite it having been one of the key drivers of Russia's economic development in recent years. This decline is largely due to the government's decision in July 2024 to discontinue the mass preferential mortgage loan programme (currently, subsidies are only available to families with children

and military personnel).

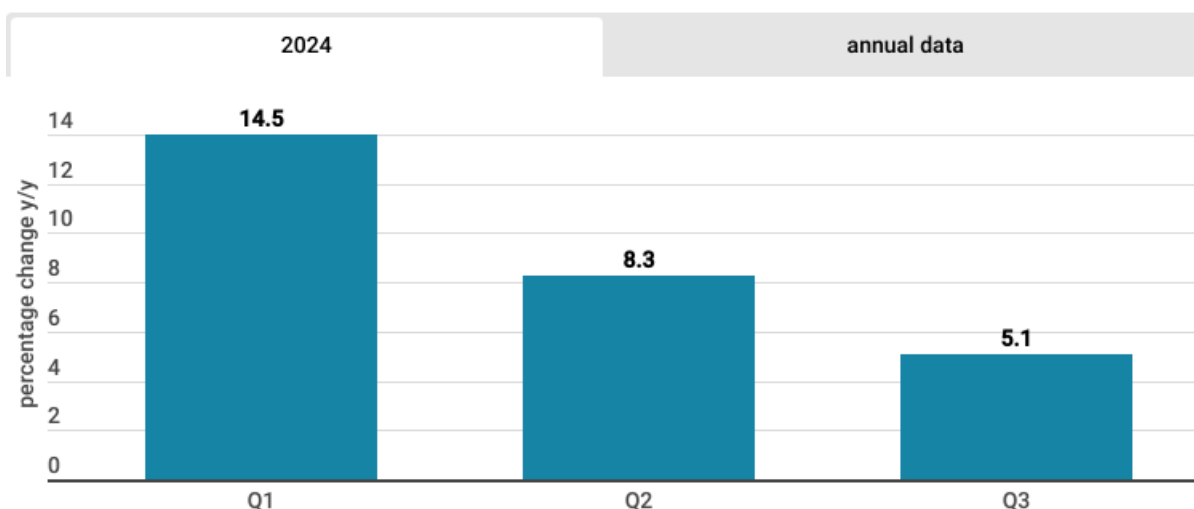
Chart 4. Production in the ‘civilian’ sector and the armaments sector in 2024



Source: Rosstat.

In 2024, the pace of **investment** in the Russian economy remained high, although a slowdown was recorded in subsequent quarters. According to government estimates, around 70% of investment spending was allocated to adapting to new economic conditions, particularly in response to sanctions. This included replacing Western machinery and reorganising trade relations, while only 30% was directed towards expanding production. Since the outbreak of the full-scale war, a significant portion of investments has been undertaken by the Russian defence sector and large state-owned enterprises such as Gazprom, Russian Railways, and Sovcomflot. These companies have focused on infrastructure projects aimed at reducing dependence on the West, benefiting from access to preferential loans.

Chart 5. Investments in the economy

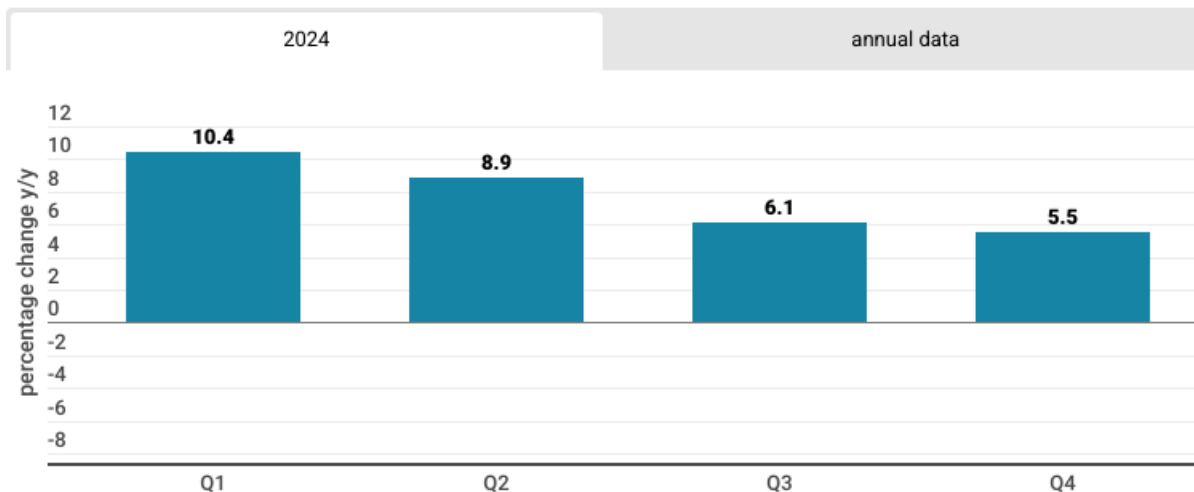


* estimates prepared by the Ministry of Economic Development of the Russian Federation

Source: Rosstat.

Due to the increase in citizens' real incomes (adjusted for official inflation data), **consumer demand** grew at a dynamic pace. For example, in 2024, retail trade expanded at a similar rate to the previous year; however, a noticeable slowdown was recorded in subsequent quarters.

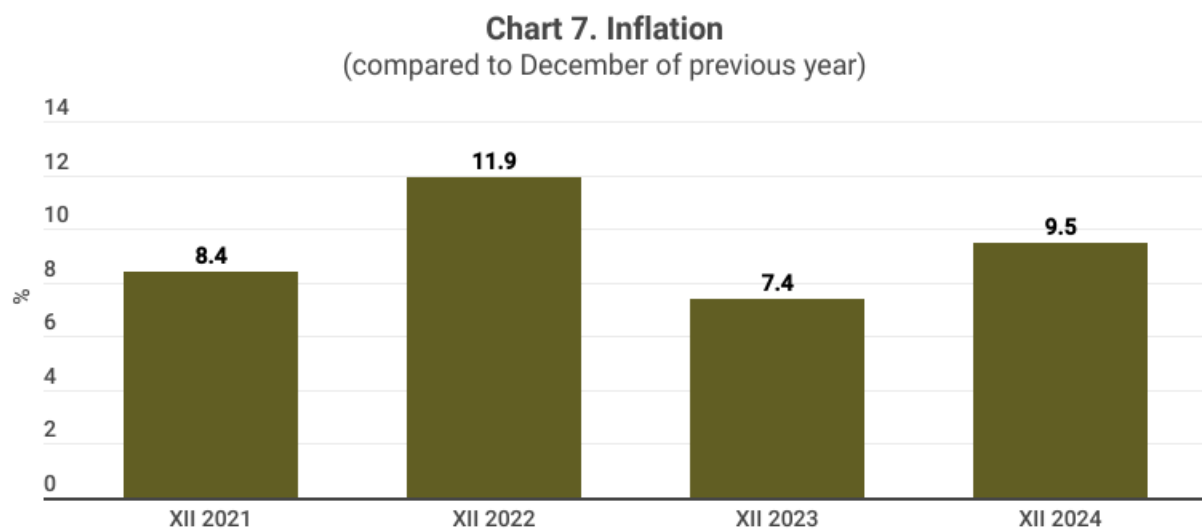
Chart 6. Retail trade



Source: Rosstat.

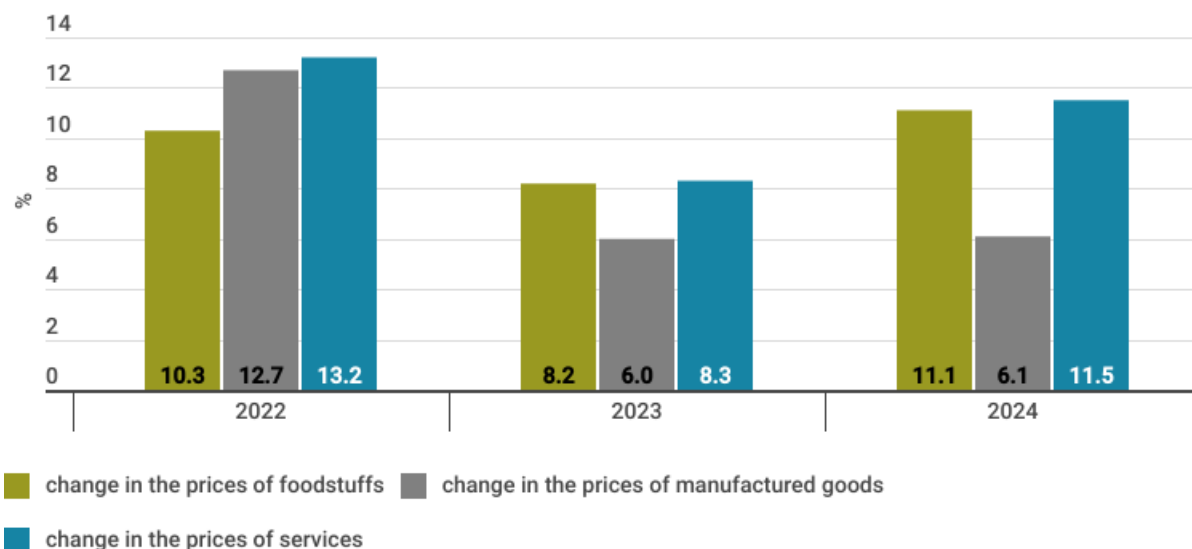
The inability of supply to keep pace with demand is driving price increases in Russia. According to official statistics, in 2024, **inflation** reached 9.5% and continues to accelerate, surpassing double digits by early February 2025. In 2024, particularly pronounced price hikes were recorded in categories such as foodstuffs, medicines, and services (including housing and utilities), disproportionately affecting the poorest groups, such as pensioners and families with children, for whom these expenses account for the bulk of their

subsistence costs. The inflation rate is a key factor in determining state indexation of social welfare benefits and pensions, making it crucial for the state budget. However, the pace of price growth remains a contentious issue. Many institutions, experts, and ordinary citizens have accused Rosstat of underreporting inflation. The official methodology does not account for the declining quality of some goods. For example, the average price of passenger cars has risen by 50% over the three years of the full-scale war, yet consumers are now mostly limited to Chinese-made vehicles or Russian cars assembled with Chinese-made parts. A similar trend has been observed for household appliances and electronic devices. A study by the Romir Institute, which monitors the prices of essential goods based on receipts from 40,000 Russian consumers, found that prices increased by nearly 18% in 2024—twice the official rate. Additionally, the significant gap between the central bank’s base interest rate and the officially reported inflation level suggests that actual price increases may be occurring at a considerably faster pace.



Source: Rosstat.

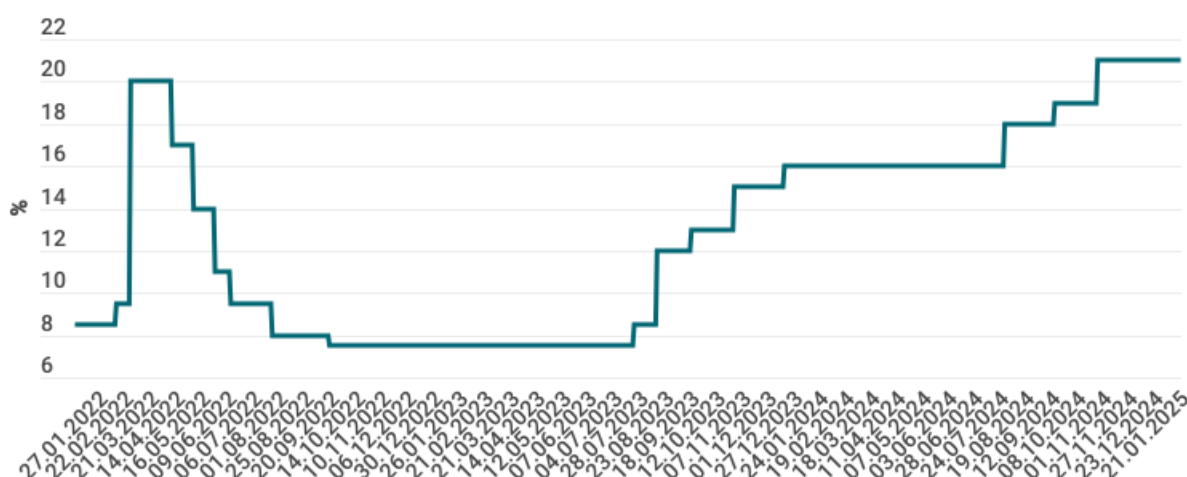
Chart 8. Increase in prices of goods and services
(compared to December of previous year)



Source: Rosstat.

The central bank has repeatedly attempted to curb rising inflation. In 2024, the regulator raised its base rate three times, bringing it to 21%. Despite a noticeable slowdown in lending activity towards the end of the year—both among individuals and businesses—increased government spending in the fourth quarter of 2024 and the early months of 2025 sustained high demand, which, in turn, continued to drive up prices.

Chart 9. CBR's base rate

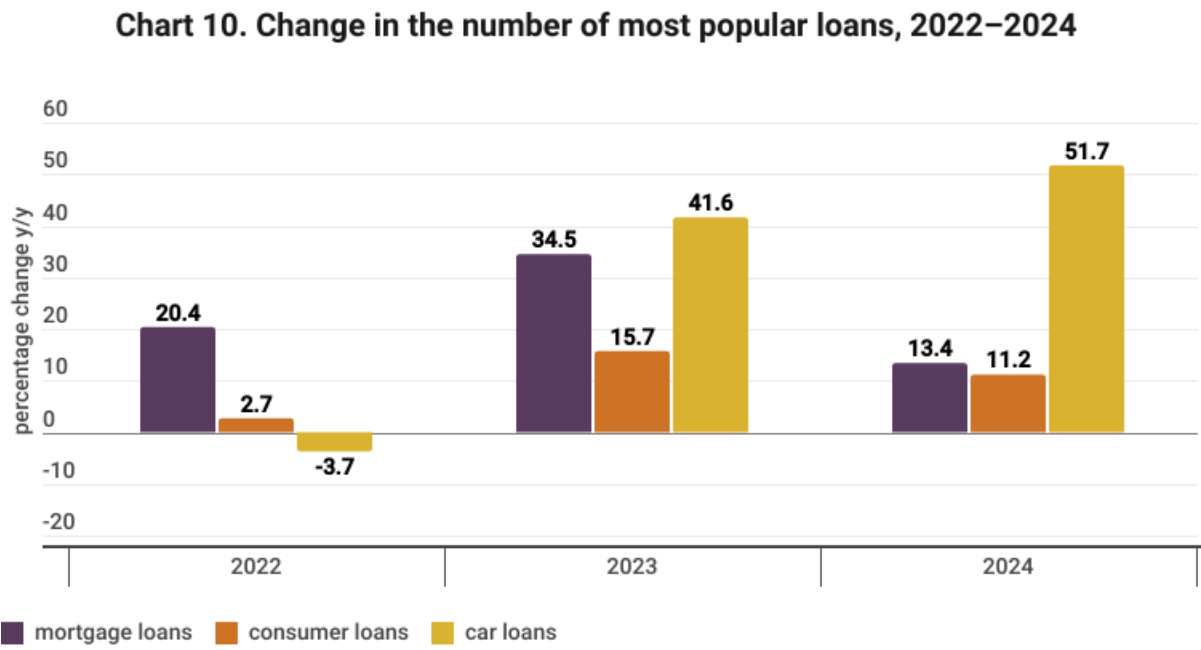


Source: Central Bank of Russia.

Over the past three years, Russia's growing demand has largely been financed through **loans**. In 2024, corporate debt increased at a faster rate than in 2023. However, the government's decision to discontinue the mass preferential mortgage loan programme helped slow the growth of household debt. A sharp rise in car loans was driven by government policy, particularly the substantial (70–85%) increase in environmental disposal

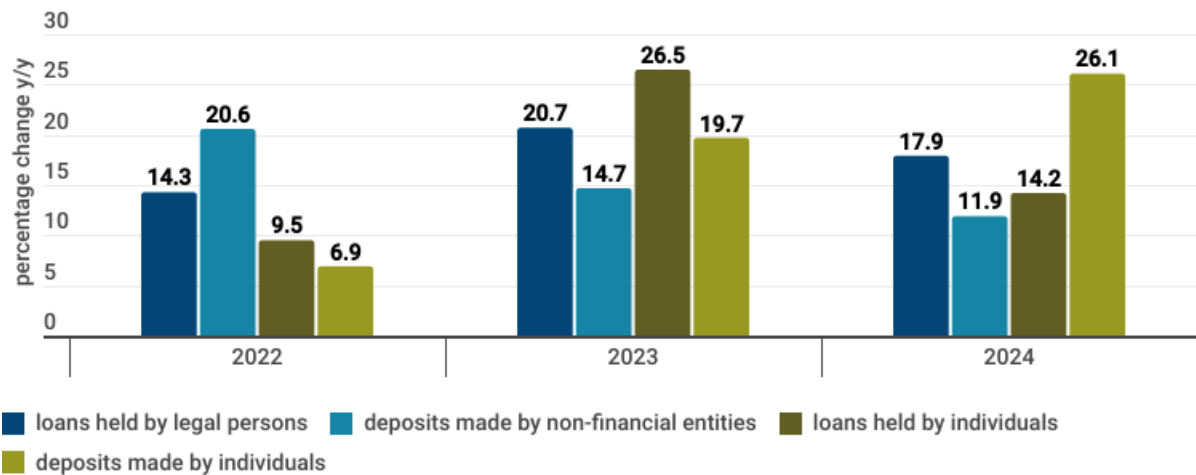
fees on imported vehicles (recycling fee), introduced on 1 October 2024. This resulted in a surge in car purchases ahead of the new regulations, which, in turn, contributed to further price increases.

High interest rates and regulations imposed by the Central Bank of Russia (CBR) are restricting access to loans. For the time being, the share of overdue loans remains low, at around 4%. However, the CBR fears that if GDP growth slows and consumer demand weakens, both individuals and businesses will find it increasingly difficult to repay their debts. At the end of 2024, the CBR reported that 25% of borrowers had three or more loans, marking a twofold increase over the first two years of the full-scale war.



Source: Central Bank of Russia.

Chart 11. Increase in the number of loans and deposits in the Russian banking sector, 2022–2024



Foreign trade was heavily impacted by tightened financial sanctions imposed by the United States, which restricted Russian entities' ability to conduct cross-border transactions. In 2024, Russian exports declined for a second consecutive year (this time by 2% y/y), and imports also recorded a slight decrease. As a result of these restrictions, foreign banks either halted or significantly limited their cooperation with Russia, leading to longer transaction processing times and higher costs. Consequently, the prices of imported goods increased, adding further inflationary pressure. Exporters faced significant difficulties repatriating capital to Russia. In addition, US sanctions on Russia's oil sector, introduced in January 2025,^[3] led to Russian oil export prices falling below 60 US dollars per barrel by early February 2025.

Chart 12. Russia's imports and exports, 2021–2024

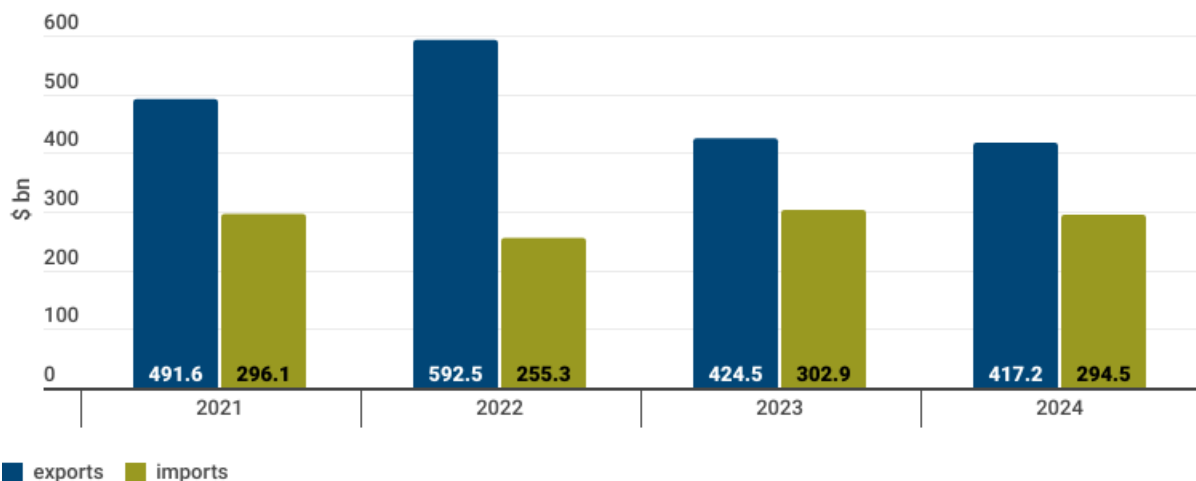
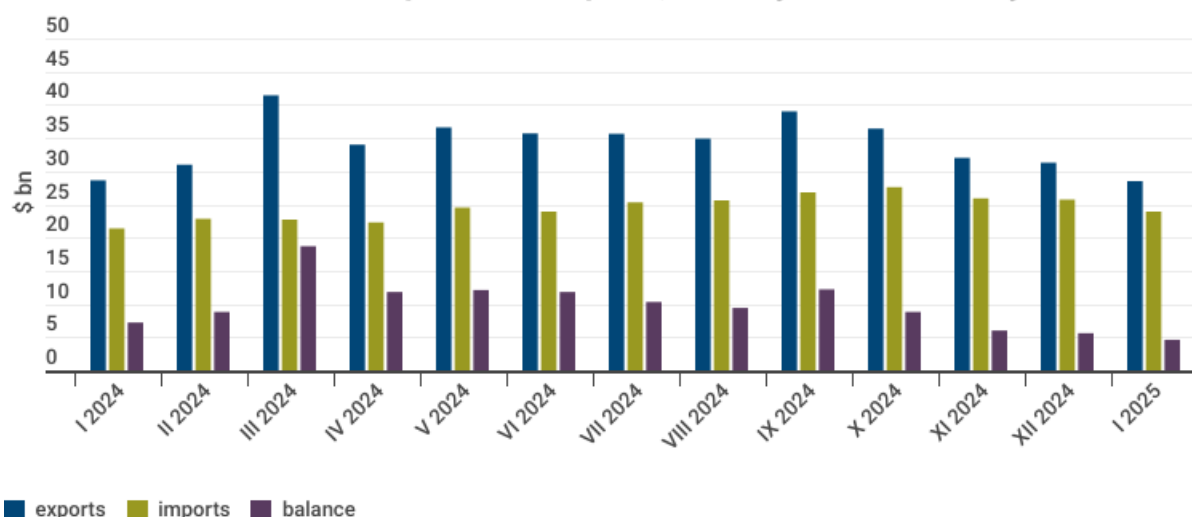


Chart 13. Russia's exports and imports, January 2024 – January 2025



Source: Central Bank of Russia.

To support cross-border transactions, the authorities eased the requirements imposed on exporters regarding the mandatory repatriation of foreign currency earnings from raw material sales. In June 2024, the 80% limit introduced in 2022 was reduced to 60%, and in October it was further lowered to 40%. While the funds retained abroad have facilitated the funding of import operations, they have had a negative impact on the domestic foreign exchange market. Consequently, the reduced inflow of foreign currency contributed to the **devaluation of the rouble**. In January 2025, the exchange rate reached approximately 100 roubles to the US dollar, compared with just under 90 roubles at the beginning of the year. It is important to note that, since June 2024, when the Moscow Exchange was placed under US sanctions, **the official exchange rate of the Russian currency has no longer been determined by market mechanisms** but is instead set by the Central Bank of Russia, based on foreign exchange transactions carried out by selected commercial banks. This has been detrimental to both importers and exporters, as banks impose high margins on currency operations and offer unfavourable exchange rates (due to the wide spread between buying and selling prices).

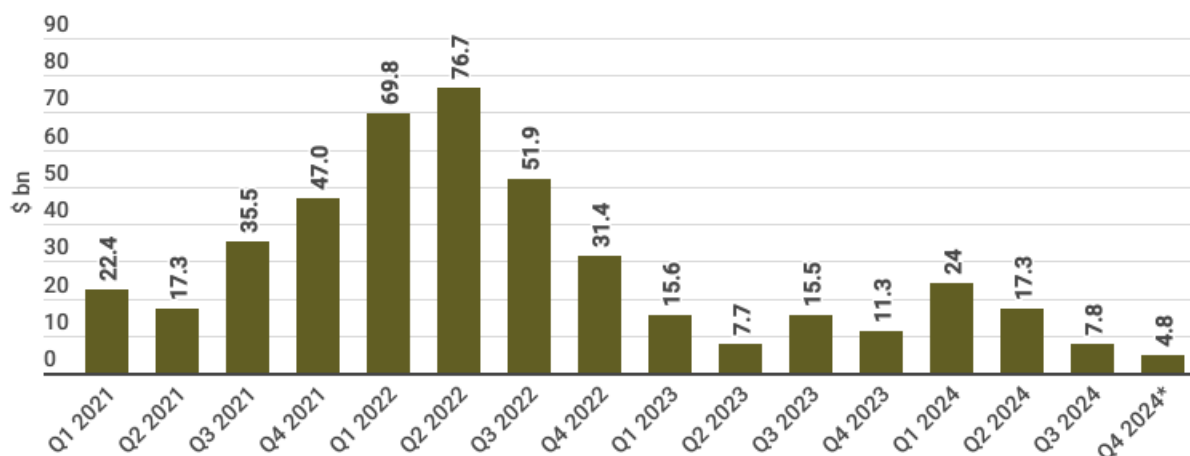
Chart 14. Dollar to rouble exchange rate



Source: Central Bank of Russia.

With Russia cut off from foreign capital markets, the exchange rate of the rouble has become almost entirely dependent on the performance of foreign trade. The **positive balance of commodity trade** now effectively serves as the sole significant source of foreign currency inflows into the country. This helps to offset the negative balance of trade in services, (particularly related to international tourism), and to meet the demand for foreign currency from businesses and citizens.

Chart 15. Current account

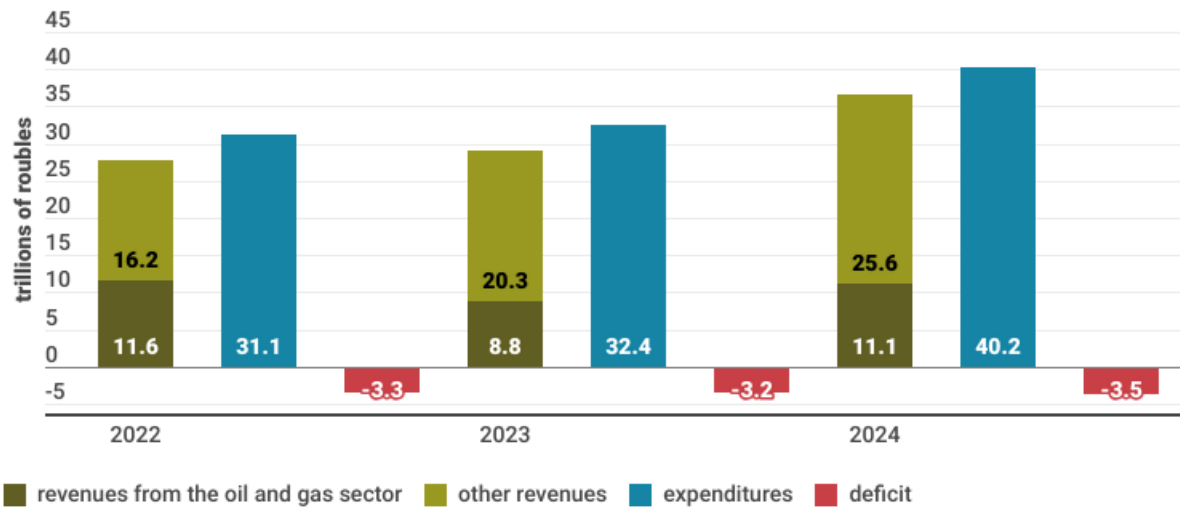


Source: Central Bank of Russia.

Despite mounting economic challenges, in 2024, **budget revenues** increased by 26% y/y, with both oil and gas revenues and other sources growing at a similar rate. Several factors contributed to this rise in budget revenues – besides overall GDP growth, these included higher tax burdens, elevated inflation, the devaluation of the rouble (as taxation of the oil and gas sector depends on export prices), and an increase in the average price per barrel of oil. Consequently, despite a 1.5% y/y decline in oil production, rouble-denominated revenues

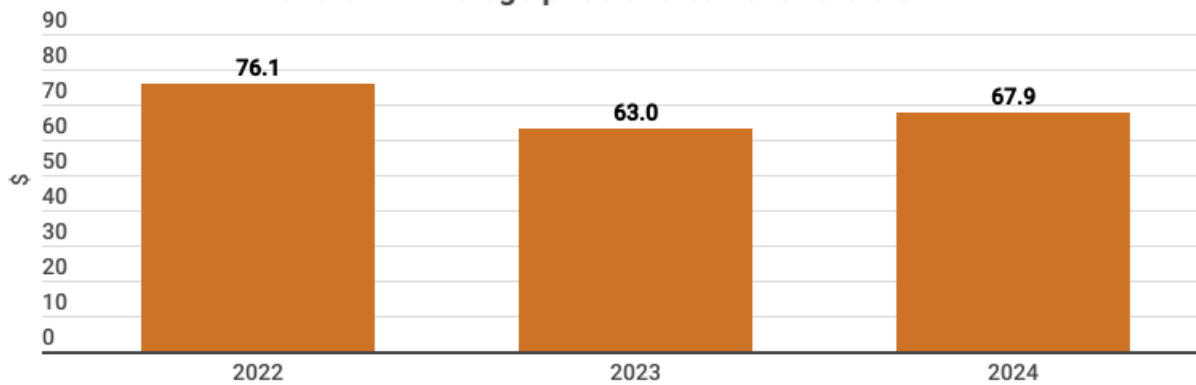
from the sector decreased by just 4% compared with the record-high year of 2022.

Chart 16. Budget revenues and expenditures



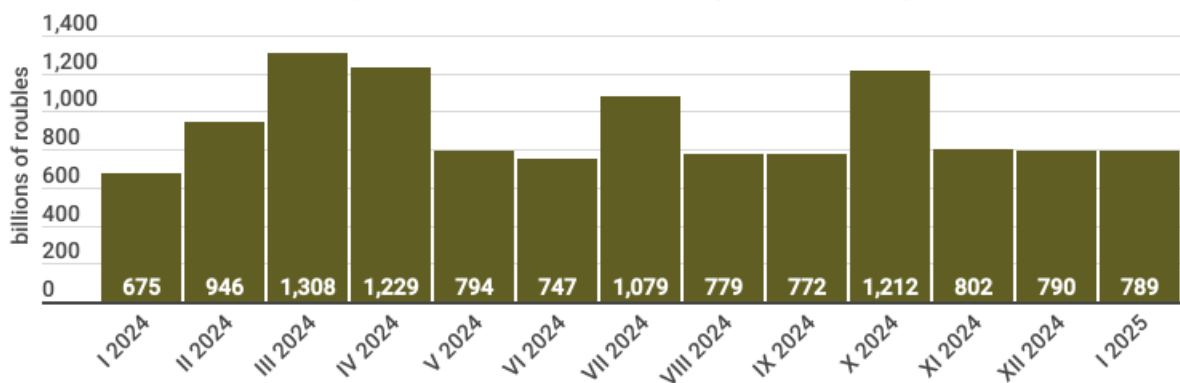
Source: Rosstat.

Chart 17. Average price of a barrel of Urals oil



Source: Rosstat.

Chart 18. Budget revenues generated by the oil and gas sector



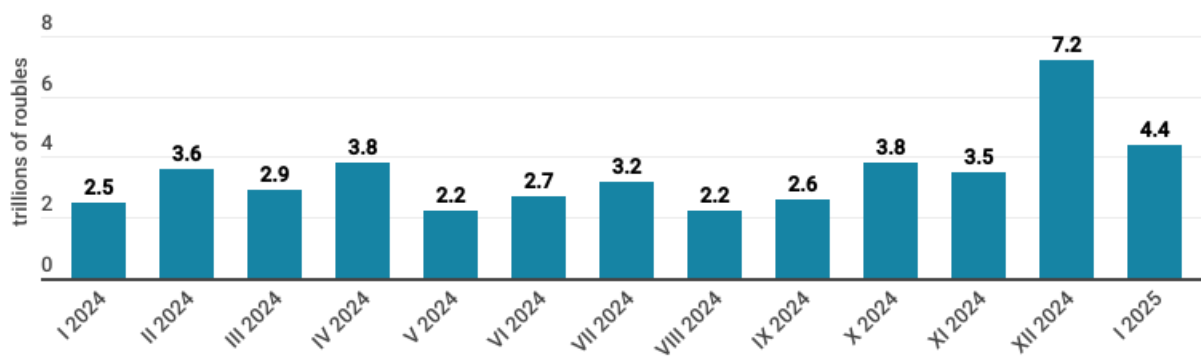
Source: Ministry of Finance of the Russian Federation.

In 2024, Russia’s total budget expenditures increased by more than 24% y/y. The largest budget item was spending on ‘national defence’, which for the first time officially surpassed expenditures on social welfare policy. Financing the war consumed at least 35% of the budget. Beyond direct ‘national defence’ spending, this figure also includes expenditures on internal security and a portion of funds allocated to the national economy.^[4]

Throughout 2024, the government continuously increased budget expenditures, with spending peaking in the fourth quarter, rising by nearly 30% y/y. Total expenditures for the year were ultimately 10% higher than initially planned in the 2024 budget law. Most of the additional funds were allocated to financing the war effort. However, since 2022, Russian authorities have not published detailed data on budget execution, disclosing only government spending plans. Consequently, the exact share of expenditures allocated to military operations remains unknown. **The rising costs associated with sustaining the war effort are forcing the Kremlin to cut other spending categories, including social welfare programmes and financial support for regions,** despite their increasing financial obligations.

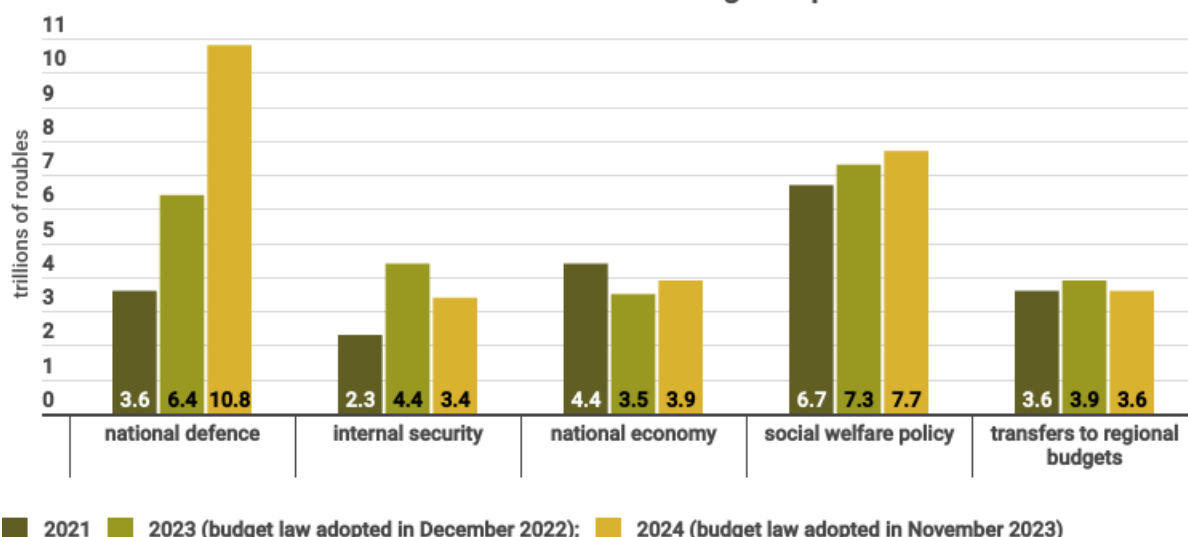
High levels of government spending continued into January 2025, with expenditures rising by a record 74% y/y. Over the past three years, the start of the year has typically been a period of increased funding, as the government traditionally makes advance payments for public procurement contracts, primarily in the defence sector. However, the exceptionally rapid growth in spending recorded in recent months was likely influenced by the change in the US administration and formed part of the government’s broader image-building strategy. The Kremlin sought to convince the West, particularly President Donald Trump, of its ability to sustain the war effort and the ineffectiveness of sanctions.

Chart 19. Monthly budgetary expenditures



Source: Ministry of Finance of the Russian Federation.

Chart 20. Structure of federal budget expenditures

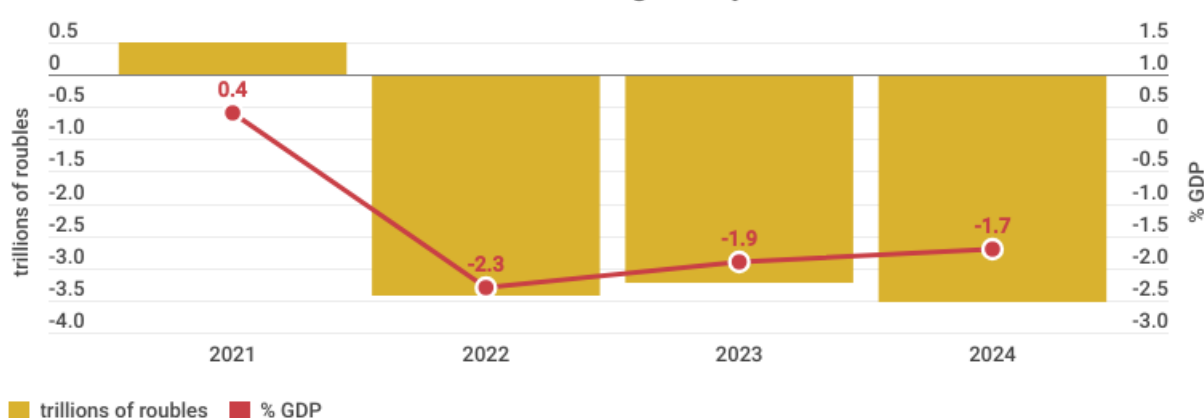


Data for 2022 is unavailable. The figures provided in the 2022 budget law are misleading, as they did not take into account the costs of the invasion. Throughout the year, the government increased spending to meet war-related needs.

Source: Ministry of Finance of the Russian Federation.

The sharp increase in government spending at the end of 2024 led to a **doubling of the budget deficit** compared to initial projections contained in the budget law, reaching approximately \$35 billion. This shortfall was partially financed through the issuance of sovereign bonds. By the end of the year, total domestic public debt had risen to 22 trillion roubles, or approximately 16% of GDP. Although the debt level remains relatively low, the rising cost of borrowing in Russia means debt servicing is consuming an increasing share of the budget, around 6% in 2024.

Chart 21. Federal budget surplus/deficit

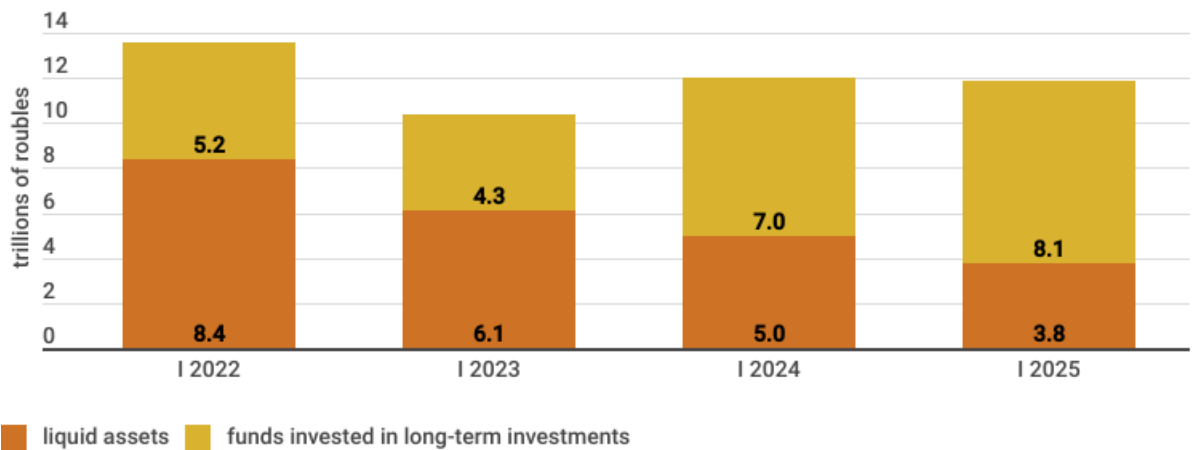


Source: the Government of the Russian Federation.

Reserves accumulated in the National Welfare Fund (NWF) were another major source of deficit financing. Consequently, the NWF's liquid assets **declined**; they are currently held in yuan and gold. By early 2025, the value of these assets had fallen to a level roughly

equivalent to the 2024 budget deficit. At the same time, the NWF’s total resources, measured in roubles, remained largely unchanged. This was due to exchange rate fluctuations, the rising valuation of companies in which the funds are invested, and additional government revenues from oil prices exceeding 65 dollars per barrel. The authorities also used NWF funds to support the economy—for example, by investing in infrastructure projects and the armaments sector.

Chart 22. Resources of the National Welfare Fund, including liquid financial assets
(as at the first day of the month)

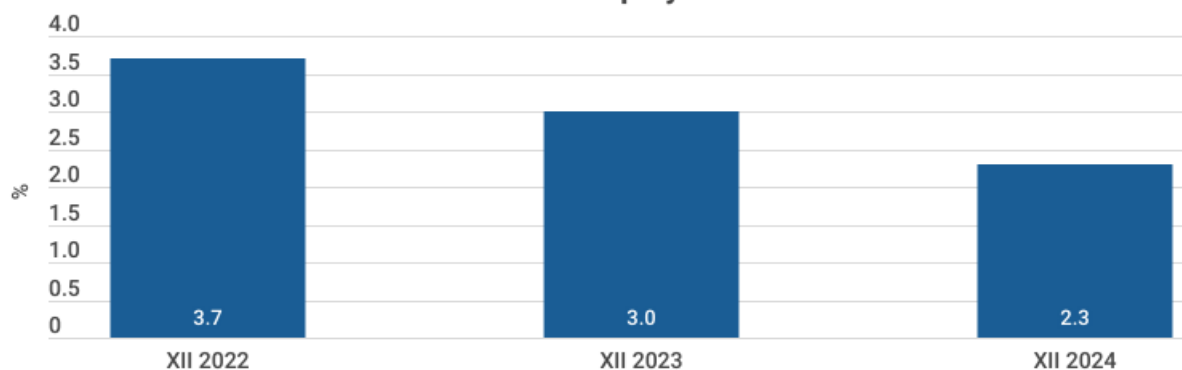


Source: Rosstat.

Labour shortages are the primary factor limiting Russia’s ability to sustain high rates of economic growth. By the end of 2024, unemployment had fallen to another record low. The already difficult labour market situation, resulting from demographic challenges that have persisted since the collapse of the USSR, was further exacerbated by the war. Most notably, at least 300,000 working-age men were sent to the front, while a further 500,000 citizens permanently emigrated. Additionally, owing to the Kremlin’s increasingly restrictive migration policies and difficulties in transferring earnings across borders, the **number of economic migrants declined by as much as 2 million.**[\[5\]](#)

According to official data, the Russian labour market is currently facing a shortage of approximately 1.5 million skilled workers. Despite high wages, vacancies remain unfilled, even in the armaments sector. Overall, Rosstat reports around 2 million unfilled positions across the economy, whereas other estimates, such as those from the Russian Academy of Sciences, suggest the actual shortfall could be as high as 5 million workers.

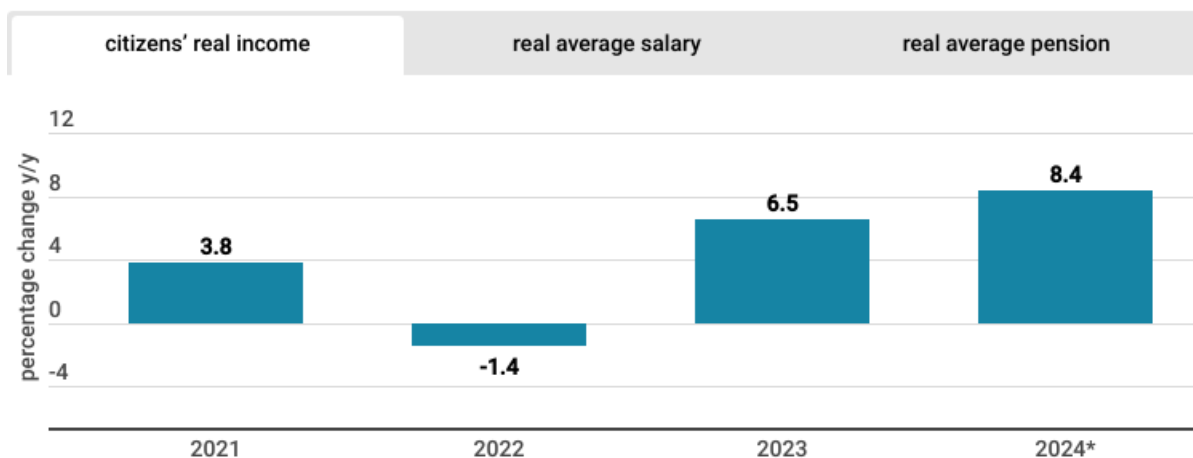
Chart 23. Unemployment rate



Source: Rosstat.

The imbalanced labour market is driving significant wage increases. Consequently, **although household incomes are rising, wealth distribution remains highly uneven** across different social groups and regions. For example, the average nominal salary in Moscow was around 150,000 roubles, while in Ingushetia it was just under 40,000 roubles. However, it is important to note that wage statistics in the North Caucasus republics tend to be underestimated owing to the high proportion of earnings generated in the informal economy, outside the tax system.

Chart 24. Citizens' real incomes



* data for January–November 2024

Source: Rosstat.

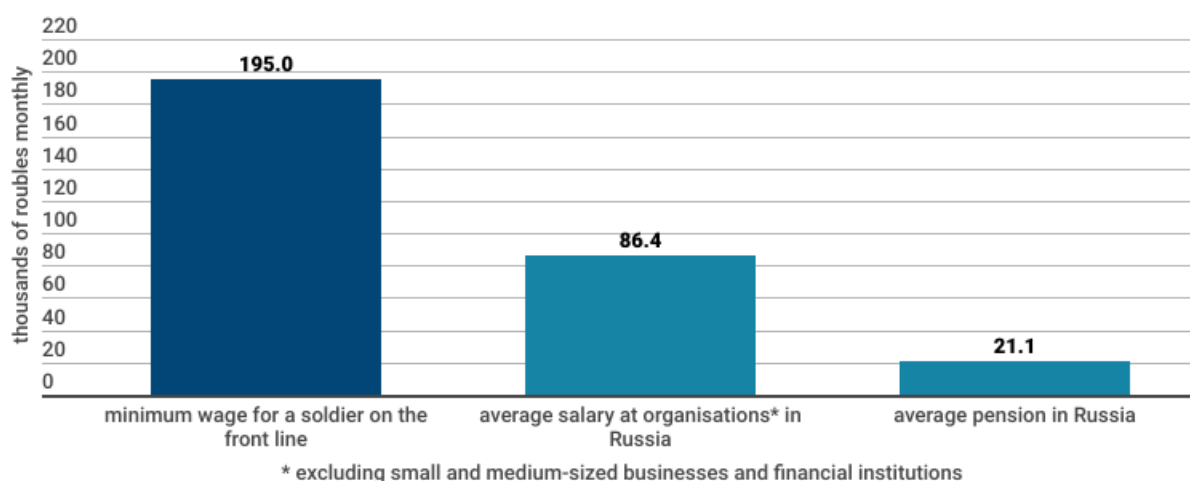
Wages increased across almost all sectors of the economy, with the largest pay rises recorded in the armaments industry. In many cases, the salaries of skilled workers—such as metalworkers and welders, were comparable to the pay of soldiers on the front line. Consequently, in Udmurtia, one of Russia's regions most dependent on the armaments sector, nominal wages rose by approximately 25%. Despite this, they remained below the national average. The primary beneficiaries of rising incomes were men willing to enlist in the military and their families. In addition to a soldier's monthly salary of at least approximately \$2,000, they received substantial one-off signing bonuses, largely funded by

regional authorities, which are responsible for recruiting soldiers and meeting Kremlin-imposed conscription quotas.

At the beginning of 2025, Samara Oblast offered the highest bonuses, amounting to 4 million roubles (approximately \$40,000), for signing a military contract. Additionally, the families of soldiers killed were entitled to over 13 million roubles (approximately \$130,000). According to Russian sources, more than 600,000 military personnel are currently deployed in combat zones; however, this figure cannot be independently verified. Independent estimates suggest that, over the three years of war, between 160,000 and 225,000 soldiers may have been killed. A significant proportion of those killed came from Russia's poorest social groups, particularly from the most economically disadvantaged regions, such as Buryatia, Tuva, and Dagestan. For many, income earned from military service was the only available means of achieving social mobility.

These figures stand in stark contrast to the situation of pensioners (more than 41 million individuals) and public sector employees, including teachers, social workers, nurses, and doctors. In 2024, their nominal wages increased at a rate below inflation, resulting in a decline in real incomes. Consequently, the average pension now amounts to just under 25% of the average salary, whereas prior to the invasion, it was approximately one-third.

Chart 25. Average salary and average pension in Russia, November 2024



Source: Rosstat.

[1] Preliminary estimates; all figures provided in the text come from Rosstat, unless stated otherwise.

[2] For more see F. Rudnik, *'Farewell to Europe: Gazprom after 2024'*, OSW Commentary, no. 644, 11 February 2025, osw.waw.pl.

[3] For more see F. Rudnik, *'Sanctions on Russia: the Biden administration's parting blow'*, OSW, 13 January 2025, osw.waw.pl.

[4] For more see I. Wiśniewska, *'Russia's budget for 2025: war above all'*, OSW, 22 November 2024, osw.waw.pl.

[5] For more see K. Chawryło, *'Short-term stability and long-term problems. The demographic situation in Russia'*, OSW Commentary, no. 610, 3 July 2024, osw.waw.pl.