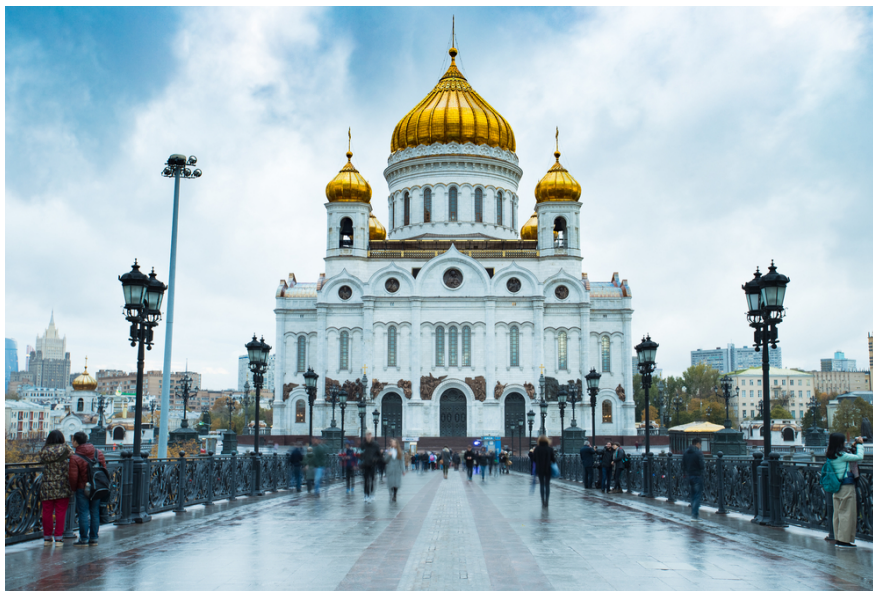


Russia: Capital outflow may reflect lower investment demand

Capital outflow totalled US\$18.6 billion in 2M19, sterilizing 83% of the current account. It means a build-up of international assets, which is partially seasonal and does not reflect higher nervousness about sanctions. Rather, it reflects low investment demand locally, highlighting the structural weakness of Russia's balance of payments



Source: Shutterstock

\$18.6 bn

2M19 net private capital outflow

83% of current account surplus

Worse than expected

Preliminary balance of payments statistics did not surprise on the current account side - the surplus remained high at US\$10.5 billion in February after US\$11.8 billion in January - thanks to the strong oil price environment and restrained imports. At the same time, the scale of net private

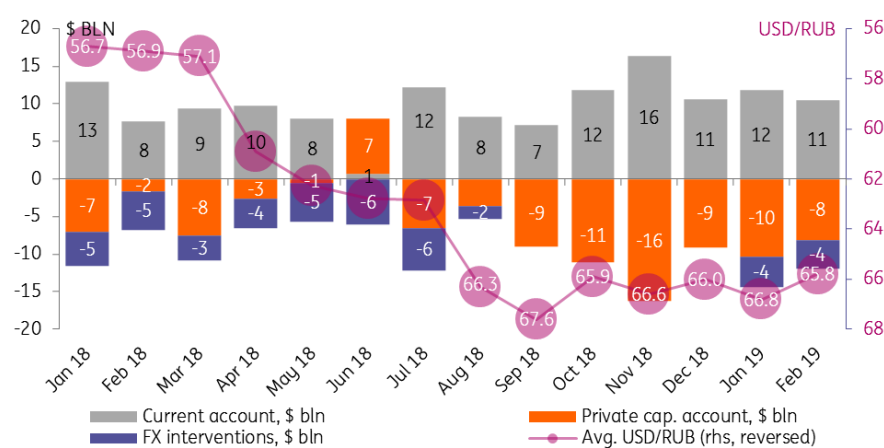
capital outflow - US\$8.2 billion in February after US\$10.4 billion in January - was larger than expected and reflected an accumulation of corporate international assets. This outflow can be partially attributed to seasonality, as the corporate sector is known to accumulate international assets in 1Q for technical reasons, however, we note that relative to the size of the current account surplus the net private capital outflow increased from 31% in 2M17 and 42% in 2M18 to 83% in 2M19.

The balance of payments numbers do not point to a higher nervousness regarding sanctions, as

- the latter would have translated into more active foreign debt redemption, which does not seem to be the case, based on the commentary by the Bank of Russia
- the risk of sanctions tends to be channelled via portfolio flows related to the state bonds (OFZ), which is not included into the private flow number. According to the Central Bank of Russia (CBR) data, OFZ saw US\$0.8 billion portfolio inflows in January, and anecdotal evidence from the market suggest that the positive inflow continued in February

High net private capital outflow and almost US\$8 billion of FX purchases in 2M19 did not prevent RUB's appreciation to USD by 6% since the beginning of the year amid 2% appreciation of RUB's EM peers, reflecting a recovery in oil prices and some moderation of Russia-specific risk perception.

Key parameters of monthly balance of payments



Source: Bank of Russia, Bloomberg, ING

At the same time, the corporate sector's low preference to repatriate the current account surplus beyond mandatory tax payments may reflect low local investment demand and possibly low confidence in RUB as a savings currency. Strong corporate capital outflow seems to contradict the CBR's call that the increase in the mandatory FX purchases should automatically lower the amount of FX channelled into the net private capital outflow, and makes our full-year expectations of US\$20 billion capital outflow too optimistic. We now see it at least at US\$30 billion for 2019, which also forces us to downgrade our year-end 2019 USDRUB target from 65.0 to 66.0. Strong capital outflow also highlights RUB's vulnerability in 2-3Q19, when the current account surplus is seasonally weak, which means that even in the benign external environment RUB trading range may shift to RUB66-68 in the next couple of quarters. This view may be subject to further deterioration in the case of global risk-off on negative foreign policy developments around Russia.

Author

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user’s investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.