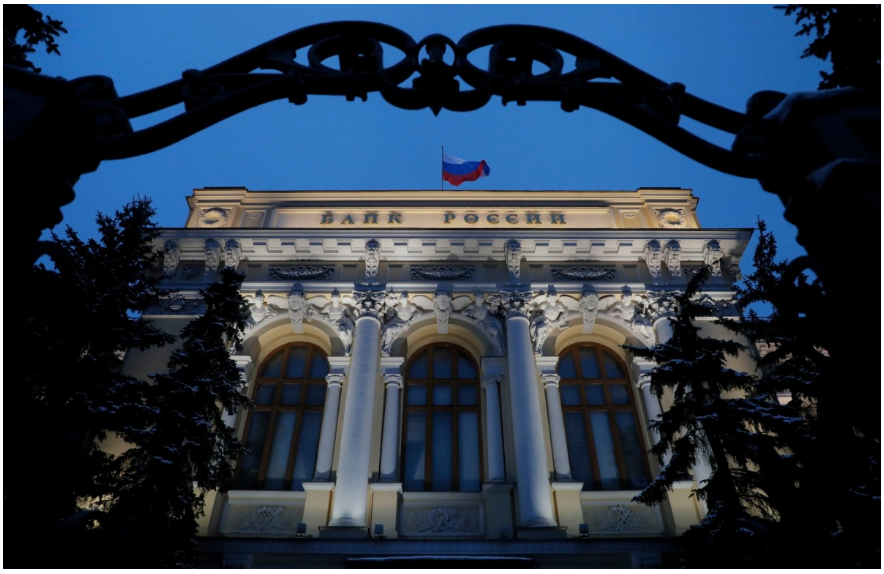
Russia: CBR involvement on FX market shrinks to a minimum

Russia will cut FX sales in August by half to $0.9bn, in line with expectations. In addition, the FX selling and purchase backlogs have been largely netted out, also in line with our expectations. The CBR's minimal presence in the FX market in 3Q20 is positive for transparency and capital flows, but leaves RUB open to volatility in the near-term



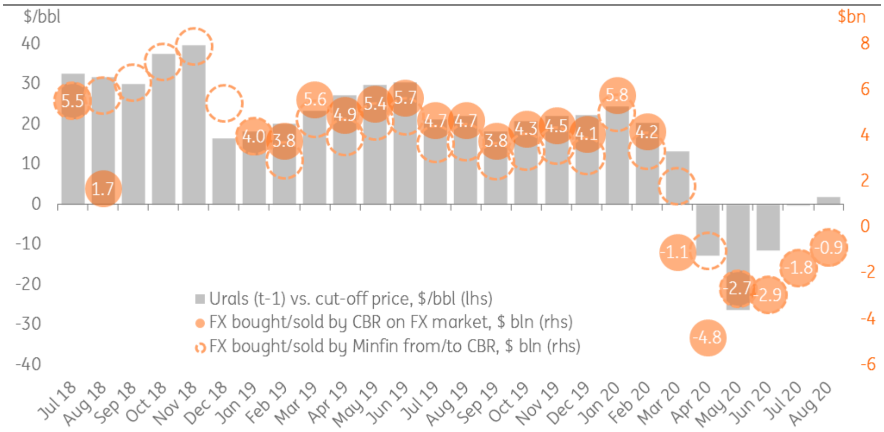
The Central Bank of Russia headquarters in Moscow

The Russian finance ministry announced that it will cut the volume of FX sold to the Central Bank of Russia (off-market transactions) from RUB 126bn ($1.8bn) in July to RUB 65bn ($0.9bn) in August. This is close to consensus expectations of RUB 80bn and our forecast of RUB 75bn. The cut in the FX sales is explained by higher expected fuel revenues thanks to the increase in the monthly Urals from $42/bbl in June to $44/bbl in July, and the easing in the OPEC+ mandated constraints to oil output since August.

- FX sales will persist despite the Urals price exceeding the $42.4/bbl official cut-off (the level of zero-intervention), as even with the recent easing in the OPEC+ restrictions on oil output, Russia is expected to supply around 8.9-9.0 MMb/d in August, significantly below the pre-cut level of around 11.0 MMB/d. This suggests that the actual cut off in the Urals price for FX interventions should be closer to $50/bbl, in line with our earlier expectations.

- The Minfin guidance will be fully executed by the CBR on the local FX market, as the CBR confirmed our expectations that FX sales' obligations related to the SBER handover (around $26 bln) will be netted with the FX purchase backlog from 2018 ($23-24 bln), leaving a residual US$2.5bn of FX sales to be evenly spread through 4Q20. This suggests that in case of Urals stays around 45/bbl (our base case), the CBR presence on the local market until the year-end will be minimal ($0.5-1.0 bn sales in September and $1.0-1.5bn monthly sales in 4Q20).
- While generally positive in terms of transparency and capital flows, the reduction in FX sales is increasing the dependency of RUB on capital flows. Based on the CBR's recent macro forecast update, the current account is expected to see $20 bn deficit in 2H20 (after the $22 bn surplus in 1H20), while the net private capital inflow is to total only $3.9 bn in 2H20 (after the $28.9 bn outflow in 1H20). The portfolio inflow to state bonds should total $5 bln (so far, the daily data for July-August suggests a small outflow of around $265 mln). The preliminary balance of payments data for July, due for release on 11 August, should shed more light on how realistic those expectations are.
- It remains to be seen whether the amendments to cross-border taxation agreements for dividends and interest payments proposed by Russia in March and the denunciation of the double taxation treaty between Russia and Cyprus initiated in August is an additional factor of corporate capital flow volatility. As of the beginning of 2020, Russia's outward FDI to Cyprus totalled $217 bn out of $500bn, inward FDI from Cyprus to Russia was $180bn out of a total of $586 bn.

MinFin's FX sales in August to drop below $1bn on higher oil price, increased oil output



Source: Finance Ministry, Bank of Russia, ING

RUB view unchanged so far

The FX interventions announcement for August does little to change our RUB view, with heightened volatility seen in 3Q20 in the USDRUB 70-75 range, with subsequent stabilisation in 4Q20 on the seasonality of balance of payments and residual FX sales. Meanwhile, global EM risk appetite, oil prices, US foreign policy, as well as Russia's renegotiation of tax agreements with FDI partners are the obvious factors of uncertainty for this view.

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