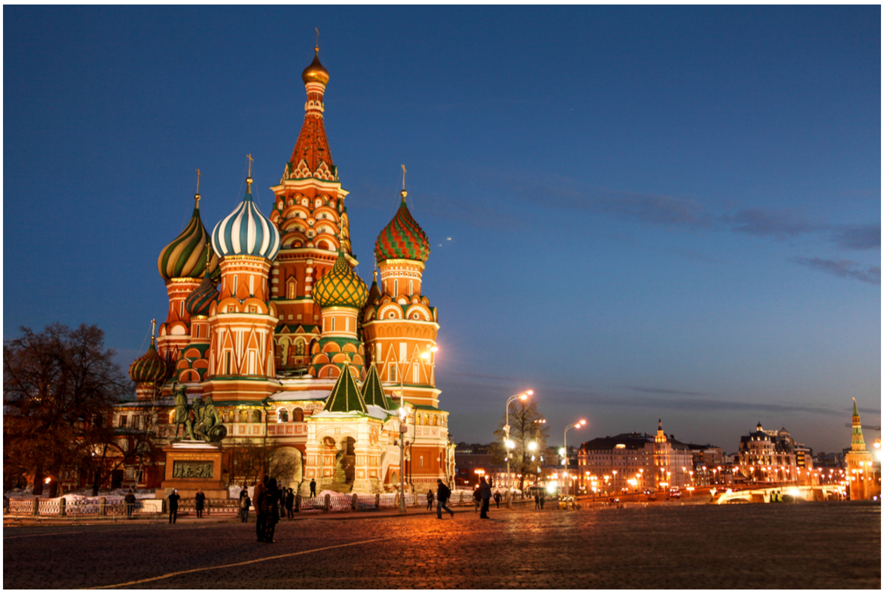
Drop in Russian foreign debt confirms improvement in the capital outflow structure

Russian banks and other corporates reduced foreign debt by US$11bn in 3Q20 after a similar spike in 2Q20. The swings here could be technical, but the 3Q20 drop confirms that the private capital outflow unrelated to foreign debt seems to have stabilised. This is a promising future sign for the balance of payments



Corporate foreign debt reversed its previous gains, suggesting technical nature of recent flows

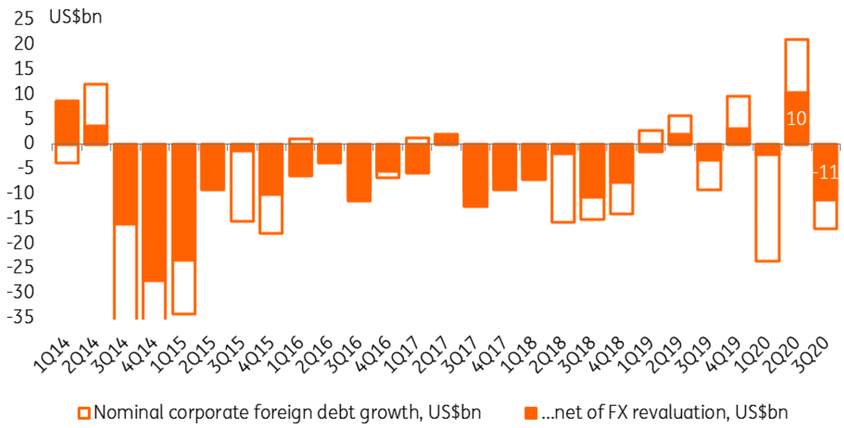
The recently released foreign debt statistics for 3Q20 provide additional colour to the broader balance of payments we covered earlier. You can download the foreign debt details here. And you can get the balance of payments numbers here.

- Nominal corporate foreign debt (of banks and non-financial companies) dropped by US$17 billion in 3Q20 to US$388bn as of the end of 3Q20. However, as up to 45% of the corporate debt is denominated in EUR and RUB, a significant portion of the 3Q20 nominal growth reflects paper decline due to the quarterly depreciation of USDRUB from 70.4 to 78.8, partially mitigated by the appreciation of EURUSD from $1.12 to $1.17. Adjusted for this effect, the actual decline in corporate foreign debt was around US$11bn, in our estimates (Figure 1).

- This US$11bn decline mirrors the similar increase for 2Q20, which we now estimate at US$10bn (higher than our initial US$7bn assessment) following a CBR update on the foreign debt currency structure. The swings in foreign debt between 2Q and 3Q seem to be in line with seasonality, but the size of the quarterly moves appears quite large. Remember, corporate foreign debt has remained stable since 2019 after the sanction-driven net redemption we saw in 2014-18.

- As for the foreign debt structure, the fluctuations in the last two quarters are driven not by core items, such as debt to direct investors, loans and deposits, debt securities, trade finance, or leasing, but rather by the non-transparent 'other' item. Looking at the broader balance of payments, these flows are counterbalanced by swings in outward trade finance and advances. This suggests that the recent swings in foreign debt are more likely to reflect technical intra-group corporate transactions rather than market activity. On the macro level, the persistent sanction environment for the key publicly traded corporates, and lack of investment demand, are favouring stable foreign debt.

Figure 1: Swings in corporate foreign debt in 2Q-3Q20 are large but appear to be technical



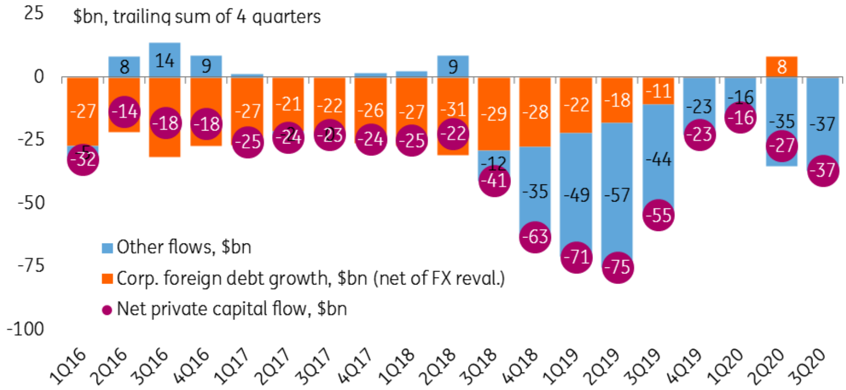
Source: Bank of Russia, ING

Stabilisation of corporate foreign debt confirms improvement in the capital flow structure

The corporate foreign debt dynamic for the last two quarters confirms the stabilisation of the foreign debt in the medium term, alleviating some of the concerns we had following the 2Q20 release. Moreover, it supports our more recent conclusion that the structure of the capital account improved in 3Q20. While the 2Q20 net private capital outflow was reported at US$10.5bn despite the US$10bn increase in the corporate foreign debt (meaning up to $20bn increase in foreign assets), in 3Q20 the capital outflow was reduced to $US7.9bn and is fully explained by the foreign debt redemption.

In other words, the foreign asset accumulation, which we attribute to low local trust, seems to have stabilised, which is a promising sign for the balance of payments. Assuming trends observed in 3Q20 continue until the end of the year, we expect to see net private capital inflow in 4Q20 of around $5bn after four consecutive quarters of outflows.

Figure 2: Capital outflow unrelated to foreign debt has stabilised



Source: Bank of Russia, ING

The drop in the corporate foreign debt fully explains the net private capital outflow in 3Q20 and suggests that other components of the capital account (mainly accumulation of foreign assets) have stabilised. This a positive sign for the balance of payments, suggesting fundamental support to the ruble from local players. Meanwhile, remember that RUB's vulnerability to foreign portfolio flows (driven by both EM risk appetite and Russia's country-specific risks) remains a factor of uncertainty for the FX market, especially in the next three to four weeks.

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