

Russia: Frozen spring

The extension of the lockdown from 1 week in March to all of April is in line with our expectations, and for now we maintain our 2.5% GDP drop forecast for 2020. Meanwhile, expansion of so far modest fiscal support is now key and seems more likely. We maintain our constructive expectations of USDRUB 70-75 by year-end but see near-term risks



Update based on recent events

In this Covid-19 update we summarize our key views on Russia based on the events that have happened so far.

GDP: We continue to expect a 2.5% GDP drop in 2020, as the president's recent [decision](#) to extend the de-facto quarantine (when most of the population is allowed a paid leave and is given a strong recommendation to stay at home) from the last week of March to entire April is more or less with our initial [expectations](#). Given the cross-country experience and the dynamics of the Covid-19 outbreak in Russia, it had been clear from the start that one week of quarantine was not enough, and the end of April seems to be the consensus deadline for major countries at this point. We do not expect a total economic meltdown in April as most of the businesses and employees will opt to continue operating remotely. Still a 20-30% YoY GDP contraction in April, mostly in the services sector, is not out of the question, which would mean a 5-10% YoY drop in 2Q20 after around 2% YoY increase in 1Q20. Assuming prompt removal of the lockdown and a global recovery, which is [ING's base case scenario](#), Russia's overall 2.5% drop in 2020 appears feasible. Obviously, a

prolonged Covid-19 outbreak globally and longer-than-expected lockdowns would result in further downgrades, however a repeat of the 2009 experience of almost a 10% GDP drop appears as a very remote possibility.

Fiscal stimulus to expand from the current very modest 1-2% of GDP. The new presidential address suggests a likelihood of a state of emergency being declared in the most heavily affected regions, including Moscow, however it will be up to governors and mayors to decide. The federal government, which has a stronger focus on economic policy (the prime minister is the former head of tax service, first deputy prime minister is a former economic aide to the president) will be in charge of containing the economic fallout. So far the fiscal support measures have been limited at around 1-2% GDP, which is modest compared to 5-15% GDP seen in major economies hit by Covid-19. Meanwhile, according to [Bloomberg](#), the government is discussing an increase of the borrowing programme by 1.0-1.5% of GDP, which could be a sign of an upcoming increase in the fiscal support to the economy in the form of additional spending or tax breaks. The resulting budget deficit which under Urals of US\$36/bbl may now be a bit wider than the 3-4% GDP we originally expected, will be covered by a mix of National wealth fund (the fund size is around 10% of GDP) spending and net local borrowing of 2.5-3.0% of GDP. Most of that new debt supply will most likely will have to be absorbed by the local players, however non-residents may join in in 2H20 if the global markets stabilise. The market participants should expect commentary from the government and Finance Ministry very soon.

Central Bank of Russia to expand support to banks and borrowers. Given the disruptive nature of the quarantine measures for businesses, and the still limited room for fiscal support we believe the banking sector, which is dominated by the large state entities, will co-finance the recovery both on the corporate and retail side. As a result, we expect the first weekly briefing by the CBR governor, which is to take place this Friday, to focus on the list of support measures the CBR already extended and will extend in the future to banks and borrowers. The interest rate policy is currently not a priority, and we expect the governor to downplay the current acceleration of CPI (from 2.3% to 2.8-3.0% year on year over March) on pre-quarantine stocking up, which would mean a low likelihood of a key rate hike from the current 6.0% level. A further spike in CPI above the CBR target of 4% is possible in 2Q20, however we see a slowdown back to 4.0-4.5% by the year-end on demand pressure. A focus on the FX market during the governor's briefing is also not very likely, as CBR operations are regulated by the fiscal rule, and so far RUB has not deviated materially from its commodity and EM peers.

USDRUB to face near-term volatility but still can recover to 70-75 by year-end. [Verbal interventions](#) by the US president on the oil market has improved the near-term mood regarding commodity currencies, including the ruble. At the same time we see high risk of volatility in the near-term, as both expectations on oil supply and demand are subject to a great deal of uncertainty related to foreign policy tensions and the Covid-19 outbreak. According to [ING's house view](#), Brent may still drop to US\$20/bbl in 2Q20 before seeing some recovery in 2H20. Based on this, we still see high risk of USDRUB entering the 80-85 range in 2Q20. However, for 2H20 we are more optimistic for several reasons. In addition to expected stabilisation of the oil prices, RUB could benefit from the likely drop of imports of goods and services (the latter will be due to both a weaker ruble and travel restrictions), lower dividend outflow, as well as FX sales under the fiscal rule and no extra pressure from local capital flows. As a result, for now as a base case we keep our expectations of USDRUB 70-75 by the year end. We will elaborate more on our RUB expectations after the 1Q20 balance of payments statistics is released.

Author

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

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