

## Russia: State of the Nation - more about the state

The budget will remain socially focused, local business climate still needs to find ways to overcome administrative challenges and prospects of an easing foreign policy remain unclear - these are our three main key takeaways from President Putin's presidential 'State of the Nation' address yesterday



Source: shutterstock

The primary focus of this year's presidential address was social policy. According to media reports, almost 48% of the President's speech was about issues related to social benefits, combating poverty, indexation of pensions, healthcare, education and budget sector salaries, which is four times more than last year. We think this change of focus is an attempt to partially compensate for the impact of the unpopular decisions to hike the retirement age and VAT rate, as well as to address the negative demographic trends.

The list of announced measures is long and includes targeted benefits for families with several children, higher disability benefits, subsidies to mortgages, higher payments for regional doctors and teachers, higher pension indexations. The additional cost of these initiatives to the budget appears modest, as the first deputy prime minister and finance minister, Anton Siluanov estimated

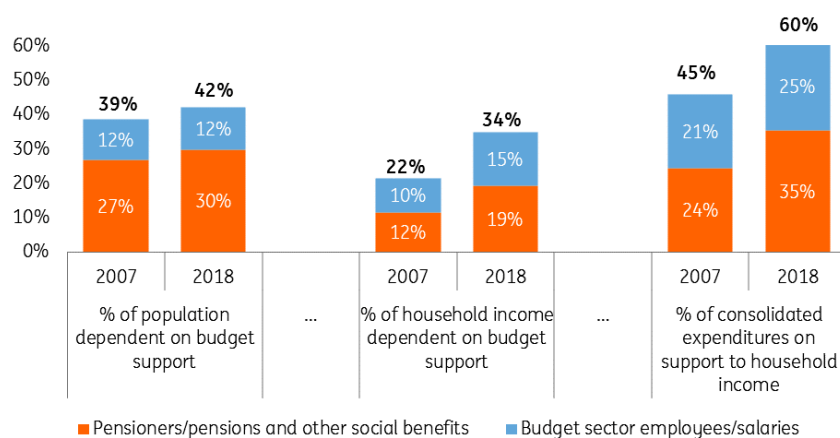
the presidential package at RUB 100-120 billion per year, which is 0.5% of the annual federal expenditures and 0.3% of the annual consolidated budget spending, which suggests, budget stability remains a priority. Given that the budget execution keeps bringing positive surprises on the non-oil revenue side in 2018 and early 2019, the announced extra social spending is unlikely to become a burden.

*The current rhetoric suggests households high dependence on state injections is here to stay and might even increase if they require additional support*

At the same time, the presidential address confirmed, that the direct support of the household income remains the primary reaction to the deteriorating consumption trend. According to our estimates, thanks to the indexation of state salaries in healthcare, education, military and state administration, as well as growth in pensions and other social benefits, the share of household income directly dependent on budget expenditures increased from 22% to 34% over the last 11 years.

Conversely, the share of consolidated budget expenditures channelled to support household income went up from 45% to 60%. The current rhetoric suggests households high dependence on state injections is here to stay and might even increase if they require additional support.

## Social focus of the Russian budget policy



Source: State statistics service, Finance Ministry, ING

The challenges to business climate the investment community has been focused on in recent days due to the prosecution of top managers of an investment fund, accounted for only 7% of the President's speech, and included proposals to create a digital platform that would allow businesses to publicly report cases of administrative pressure or unfair prosecution. President Putin also reiterated his long-lasting push towards de-criminalisation of the legal framework for economic activities.

---

*Two key questions are if the government manages to stay within the spending guidelines and if state investments result in broader-based investment growth*

---

Another topic related to the business environment was 'state investments' into infrastructure, which accounted for the remainder of the 10% of the speech, confirming the priority of large state-sponsored projects. According to our estimates based on previously announced parameters of the national projects, the government will spend RUB 14 trillion in the next six years (1.0-1.5% of GDP per year) on infrastructural projects in transportation, IT and urban development. The projects have already been budgeted into the spending program and don't represent a threat to budget stability.

However, the two key questions are if the government manages to stay within the spending guidelines and if state investments result in broader-based investment growth, as the infrastructure related to football championship, Crimea, and oil & gas sector failed to do so in 2018.

Lastly, according to media reports, foreign policy and military were given far less attention - down from 36% to 14% this year. This change of tone seems to correlate with the normalisation of Russia's military spending from the post-Soviet high of 4.4% GDP in 2016 to 2.7% GDP in 2018, which is below the 12-year average. At the same time, it remains unclear if the tone and content of the President's address provide any grounds for easing foreign policy tensions anytime soon.

Given the upcoming conclusion of the Robert Mueller investigation next week and the re-introduction of DASKA act, envisioning sanctions against the new state debt and banks, foreign policy uncertainties surrounding Russian assets are likely to persist at least in the near future.

## Author

### Dmitry Dolgin

Chief Economist, CIS

[dmitry.dolgin@ing.de](mailto: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>.