

Russian budget: 2020 deficit on track to widen

Russia's budget deficit remains at RUB1.8tr in 10M10 thanks to a temporary improvement in local activity in 3Q and SBER's dividends in October. The full-year figure should widen to RUB4.5-5.0tr, for which Minfin already borrowed RUB4.6tr through OFZ and Eurobonds. Next year's plan is to consolidate; parliamentary elections could soften the path



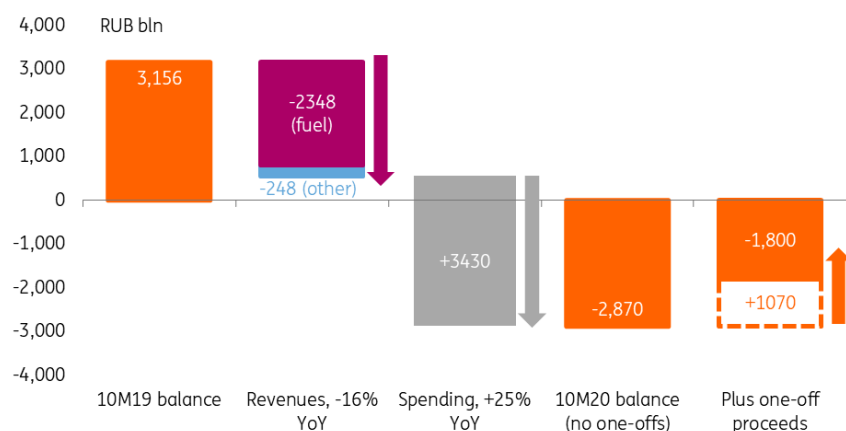
Russian budget fulfilment turned out tighter than expected, with RUB1.8 tr deficit on the federal level for 10M10, which only a minor widening compared to RUB1.7tr reported for 9M20 (the initial [9M20 estimate](#) has been slightly improved due to a downward revision in expenditures). Remember, the headline balance is distorted by a RUB1.1 trillion one-off proceeds from the Bank of Russia (as per the handover of a 50% equity stake in SBER, Russia's largest lender). Net of this transaction, the 1020 federal budget deficit would have been RUB2.9 trillion, a material deterioration from the RUB3.2 trillion surplus seen in 10M19 (Figure 1). We have the following observations:

- The reasons for restrained fulfilment in October lie purely on the non-fuel revenue side (Figure 2). The latter showed a 50% YoY uptick in October after just 4% YoY increase in

9M20. Around two-thirds of that increase is attributable to the better performance of local consumption-related taxation, such VAT and excise, and we take it positively and supportive of our above-consensus October retail trade expectations. The rest seems to be related to the RUB211 bn dividend payment from SBER to government, its 50%+1 shareholder. Given the signs of moderation in the activity recovery starting in October and no further support from dividends, we expect budget revenue trend to stabilize by the year-end.

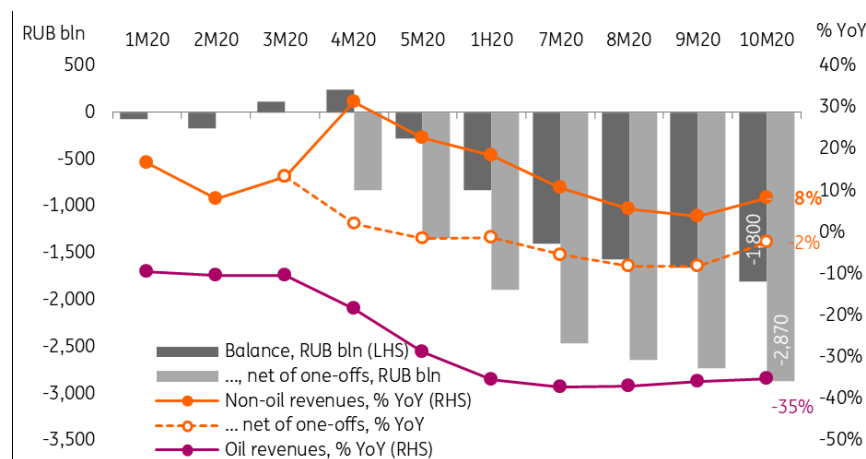
- On the expenditure side, there were no surprises, with federal spending growth stable at 25% YoY in 10M20, and around 2/3 of that increase (Figure 3) targeted at healthcare, direct social benefits and transfers to the regional budgets (which are also responsible for healthcare and social spending). This is part of the 4% GDP fiscal stimulus (including 2.5% GDP, or RUB3.0 trillion of extra spending) announced earlier.
- Assuming a continuation of 10M20 revenue and expenditure trends until the year-end, the federal deficit is set to widen materially to RUB4.5-5.0 trillion, or 4.0-4.5% of GDP for the full year. The main bulk of the expected deficit will be covered by borrowing, which has already taken place. First, year-to-date, the Finance Ministry borrowed gross RUB 5.1 tr and net RUB4.4 tr through placing local currency bonds (OFZ, Figure 4) among local banks and other investors.
- This is different from the previous years when non-residents made up to two-thirds of the OFZ market growth. Second, today Minfin placed Eurobonds with volumes likely to reach EUR2 bln, or slightly under RUB0.2 tr. In addition, in January-November Minfin used RUB0.2tr from the National Wealth Fund, in line with the fiscal rule. This means that Minfin already has the necessary funds to cover the deficit this year, and the widening in the deficit in November-December should be net-positive for ruble liquidity in the banking system.
- For next year, the guidance is for [consolidation](#) at the federal level, which in our view is inevitable given the need to address the unsustainably high \$80/bbl breakeven level, yet given the signs of stalling in the post-Covid recovery in 4Q20 and the upcoming parliamentary elections scheduled for September 2021, the intensity of this consolidation could be challenged. The room for looser than expected fiscal policy is technically confirmed by the suspension of the fiscal rule, the presence of RUB1.1 tr spending backlog and extra cash on the interim Treasury accounts, as well as proposal to ease the regulatory requirements for market borrowing at the regional level. The latter would mean potential decoupling between the balances of the federal and regional budget, which are currently linked through the practice of nearly 100% of the regional deficits to be covered by the transfers from the federal budget (Figure 5).

Figure 1: Net of one-off proceeds, the actual fiscal deficit is RUB2.9tr



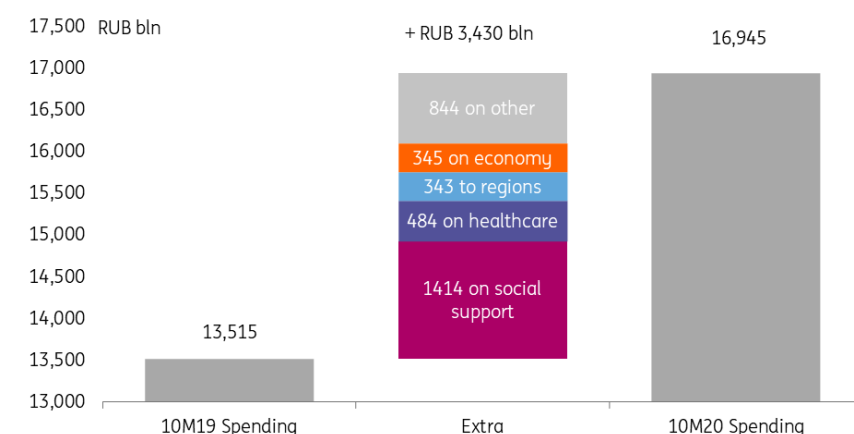
Source: Finance Ministry, media, ING

Figure 2: Non-fuel revenue dynamic improved in October reflecting temporary improvement in activity in 3Q20 and large dividend payout in October



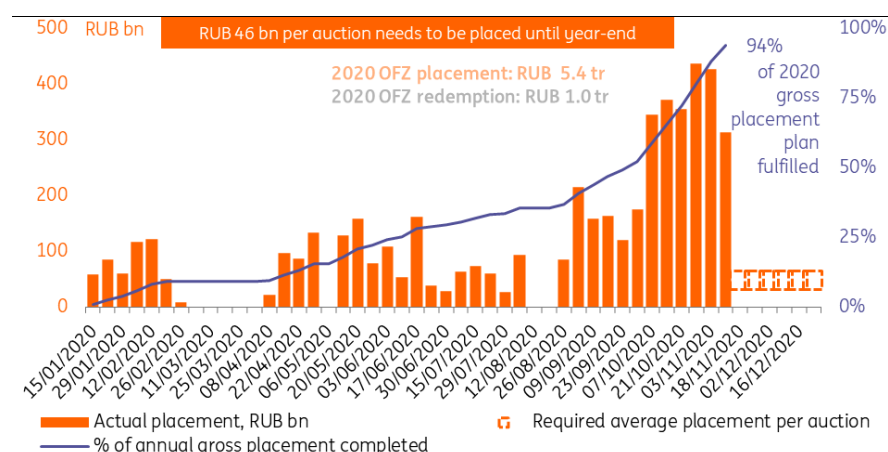
Source: Finance Ministry, media, ING

Figure 3: Spending growth stable at 25% YoY, almost two-thirds of the increase is directed to healthcare, social support and other regional spending



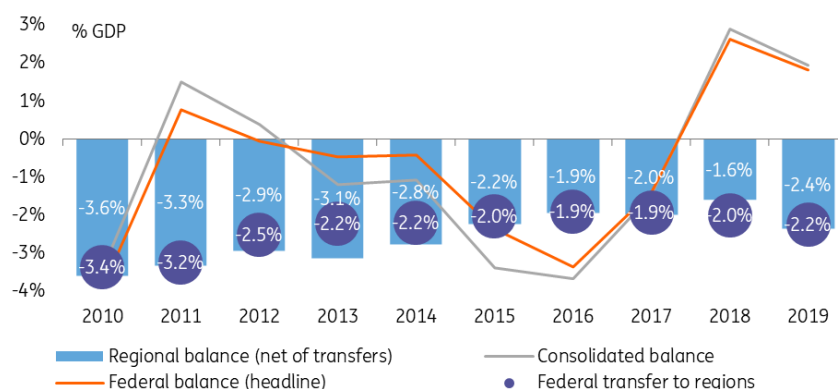
Source: Finance Ministry, ING

Figure 4: Minfin pre-emptively placed enough OFZs to cover the expected RUB4.5-5.0 tr deficit for 2020



Source: Finance Ministry, media, ING

Figure 5: Allowing regions to borrow could result in decoupling of regional deficits from the federal balance



Source: Finance Ministry, ING

Despite a stronger than expected revenue collection in October, this year's budget is on track to widen from RUB1.8tr in 10M20 to RUB4.5-5.0tr in 2020, which is already covered by pre-emptive borrowing year-to-date. Next year's plan is to consolidate on the federal level, which seems doable especially if the regional budget becomes less dependent on federal support. Fulfilment on the consolidated level could be looser given the softening in economic recovery and upcoming parliamentary elections in 2021. This will not be a threat to Russia's macro stability but may challenge expectations of disinflation in Russia for 2021.

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 www.ing.com.