Generous spending in Russia's budget amid higher oil prices

The Russian budget saw a higher than expected RUB645bn deficit in 2M21 on strong spending growth which supports our expectations of an upward revision in the annual expenditure plan. The higher than expected oil price means that the full-year deficit is likely to narrow to 1.2% of GDP; we were previously forecasting 2%

A man walks in Moscow's Red Square

The Russian federal budget was fulfilled with a large RUB645bn deficit in January-February, significantly exceeding both the market expectations of around RUB200bn and our RUB400 bn forecast. We have the following observations and takeaways:

- The key reason for the larger deficit is continued acceleration in spending from a downwardly revised -4% YoY in January to 14% YoY in 2M21 (which will be somewhat downgraded later). That corresponds to a 35% YoY spike in February. The spending volume for 2M21 corresponds to 15.8% of the official annual plan, exceeding the 13-14% range seen for January-February in the previous 3 years.
- Looking at the structure of expenditure growth, the key outperformers include non-pension social benefits (up 85% YoY in 2M21), urban and housing infrastructure (up 1.2 times), education (up 15%), and industrial support (up 12%). **We continue to expect, that this**

year's annual spending plan will be increased by 0.5-1.0% GDP, to accommodate stronger support to household income and, to a lesser extent, the industrial sector, to avoid a sharp tightening in the fiscal policy ahead of parliamentary elections scheduled for September.

- The pick up in spending in 2M21 suggests a potential positive surprise for economic activity for February relative to our conservative expectations, and could also be partly contributing to a higher than expected CPI trajectory in recent months.
- The revenue side of the budget is strong, with non-fuel revenues up 8% YoY in 2M21, mainly on aggressive growth in consumption-related taxes amid tightening in collection measures. Fuel revenue is down 15% YoY in 2M21, with the trend is improving along with oil prices. Based on the upgrade in ING's house view on oil, **we have improved our fiscal deficit outlook for 2021 from 2.0% to 1.2% of GDP, now expecting US$25bn of fuel revenues to be accumulated in the sovereign fund** (NWF) instead of previous US$10bn expectations.
- The recent statement by the Finance Ministry on the possibility of a cut in the borrowing plan for this year suggests that the cut will take place thanks to the extra non-oil revenues received in 2020 (RUB762 bln higher than expected by them in autumn), and would allow keeping public debt within 20% GDP instead of 20.3% GDP initially planned. This means that the expected cut should be within RUB350-760bn, or close to the RUB0.5tr we initially expected for this year. We welcome the fact that there is no mentioning of using oil revenues to finance the deficit. However, the question remains as to the sources of financing the increase in the spending plan for this year, a scenario we continue to consider our base case.

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