



Russia, Covid-19 & Oil

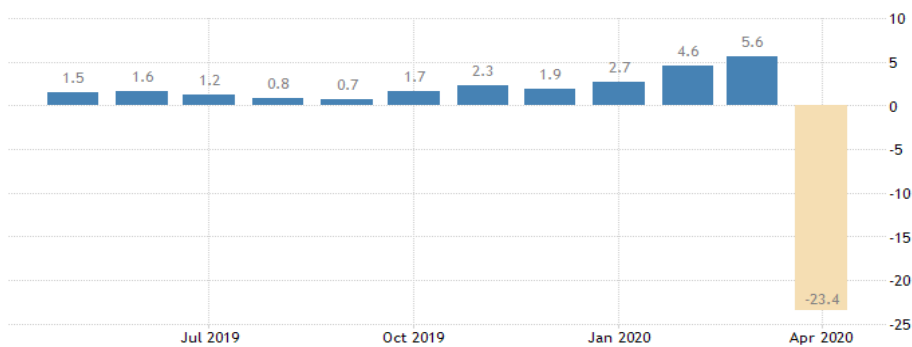
How will the crisis affect business and opportunities

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- ❑ Russia's economy started the year with good growth but that abruptly stopped with the lockdown
- ❑ The data emerging for May suggests that recovery has already started across most sectors, although not in retail or services
- ❑ The government has deliberately adopted a “problem fixing” stance while waiting for the virus, and the oil price, to settle. We should start to see a more robust response from early June
- ❑ That will mean some budget changes and altered project timelines, especially for National Projects
- ❑ Localisation will again be a key theme for the government and for foreign owned businesses operating in Russia. This will be the subject of a major debate in the summer months
- ❑ The country is much better prepared for this “crisis” than at any time in the past. That will help prevent a steep economic decline and a quicker recovery time
- ❑ There are no concerns about political or social stability and none are expected

- ❑ **Strong start to 2020.** GDP expanded by 1.8% in Q1. The main drivers were the strong retail and consumer sector activity and also a pick up in National Projects spending
- ❑ **Big hit in April.** The lockdown from end March hit the economy badly in April – with the retail/consumer sectors leading the way down
- ❑ **Q2 will see a steep decline.** GDP is expected to contract by 8-10% in Q2 but to recover steadily as the lockdown restrictions ease and government introduces support and recovery measures

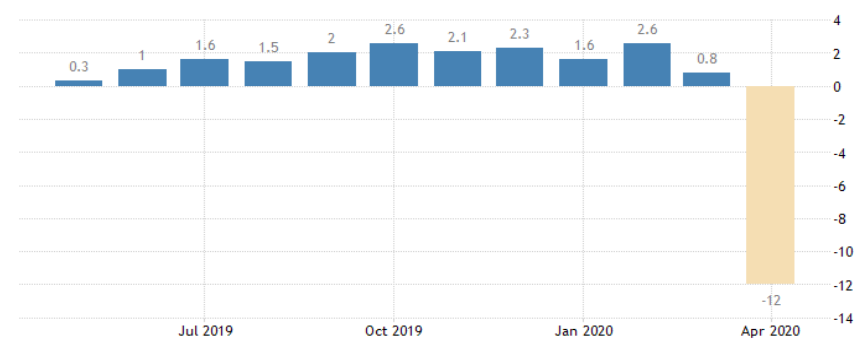
Retail Sales: April Collapse



SOURCE: TRADINGECONOMICS.COM | FEDERAL STATE STATISTICS SERVICE

Source: Tradingeconomics.com

Leading Economic Indicator Dropped Steeply in April



SOURCE: TRADINGECONOMICS.COM | MINISTRY OF ECONOMIC DEVELOPMENT

Source: Ministry of Economic Development

- ❑ **Heat-Map of activity.** In the week beginning May 18th, total spending by Sberbank customers was up 1.7% w-o-w and down 14% YoY. It does now look as though we saw the worst in the first week of April and spending has recovered since then – but on basic items/services

2020 Russian Consumer Spending By Category, % change on same week in 2019

	3/23/2020	3/30/2020	4/6/2020	4/13/2020	4/20/2020	4/27/2020	5/4/2020	5/11/2020	5/18/2020
Telecoms equipment	67.2%	-3.9%	36.7%	44.2%	15.4%	14.8%	10.1%	23.3%	23.8%
Alcohol retail	31.8%	31.0%	32.1%	34.2%	15.7%	22.8%	12.3%	23.2%	23.8%
General retail		-32.5%	-20.2%	12.5%	48.8%	86.6%	70.9%	90.8%	109.8%
Food retail	16.3%	9.2%	10.1%	14.8%	-1.0%	12.4%	3.8%	8.6%	8.1%
Digital goods	-0.3%	17.4%	1.5%	5.5%	20.9%	39.4%	8.9%	10.0%	9.8%
Medicines	37.8%	15.5%	1.5%	-5.2%	-3.4%	5.5%	-0.1%	-3.3%	0.1%
Home improvement	28.0%	-33.6%	-5.2%	-2.8%	-15.3%	-15.4%	-13.0%	-10.3%	-8.3%
White goods, electronics	16.3%	-58.2%	-48.1%	-34.6%	21.9%	13.8%	5.0%	9.2%	11.6%
Cafés and restaurants	-42.9%	-75.6%	71.5%	-71.0%	-64.6%	-64.9%	-66.7%	-60.1%	-60.9%
Furniture and interiors	-6.1%	-81.0%	-69.2%	-59.4%	-15.9%	-36.0%	-35.7%	-19.4%	-19.0%
Entertainment	-78.2%	-85.2%	-72.7%	-73.5%	-68.8%	-78.1%	-68.0%	-68.4%	-73.1%
Sport	-52.6%	-90.7%	-91.7%	-88.2%	-75.0%	-70.2%	-65.8%	-60.1%	-56.6%
Air travel	-83.0%	-92.6%	-93.7%	-89.2%	-93.5%	-87.9%	-88.8%	-83.7%	-85.0%
Clothing	-51.0%	-94.2%	-83.1%	-89.5%	-76.6%	-75.1%	-74.3%	-59.7%	-59.2%
Hotels	-47.5%	-85.3%	-87.5%	-87.7%	-87.2%	-87.4%	-95.5%	-90.8%	-92.0%
Beauty salons	-34.1%	-94.8%	-92.4%	-83.0%	-79.6%	-82.1%	-82.3%	-71.6%	-70.4%
Tour agencies	-90.4%	-96.9%	-97.4%	-95.6%	-89.0%	-95.0%	-97.6%	-94.0%	-94.4%
Jewellery	-38.3%	-97.0%	-94.7%	-88.4%	-86.9%	-83.9%	-83.9%	-71.2%	-68.1%

Source: Sberbank

- **Changes will come in phases.** These are the expected phases of government response to managing the crisis and preparing for the recovery:
 - **Phase 1** Emergency measures to deal with the crisis – coming to an end
 - **Phase 2** Interim budget adjustment to reflect the changed reality - expected in early June
 - **Phase 3** An assessment of immediate policy and spending priorities - during the summer months
 - **Phase 4** A comprehensive budget review, probably in the autumn and possibly with tax changes. Much will depend on where oil receipts are and expectations for oil and recovery in 2021.
 - **Phase 5** After the crisis eases the government is expected to accelerate efforts to attract investment and to improve the business climate. This will create opportunities for companies and investors. But, also expect changes to localization efforts and to procurement practice

- ❑ **Fourth crisis in 22 years.** This is the fourth oil based economic decline to hit the Russian economy since 1998
- ❑ **Better financial position today.** This time Russia is in a better financial position than previously, largely because of the changes the government was forced to make because of the sanctions + oil crisis of 2014-16:
 - Financial reserves are at \$570 bln. That is \$135 bln higher than in early 2015
 - The National Fund has \$160 bln of mostly liquid assets
 - National debt is under 15% of GDP and external state debt is less than 3% of GDP
 - The flexible ruble policy means that the budget is better protected against a weaker oil price:
 - In 2013 the budget needed \$115 p/bbl to balance
 - Last year it would have balanced at \$50 p/bbl
 - This year will depend on a range of factors

❑ The National Projects programme is being reviewed. Some projects will have funding cut and others will be delayed.

❑ Safe Projects are:

- Health
- Housing
- Ecology
- Digital Economy
- Export Support
- Some infrastructure projects are safe, especially those linked to trade infrastructure

National Projects Spending Sources (RUB, US\$ billion and Eur billion)

Source	Ruble Spending	US\$ Bln spending*	Euro Bln**	%
<u>Human Capital</u>				
Health	1,726	23.80	21.98	6.7%
Education	785	10.82	9.99	3.1%
Demographics	3,105	42.83	39.56	12.1%
Culture	114	1.57	1.45	0.4%
<u>Quality of Life</u>				
Safe and better roads	4,780	65.93	60.89	18.6%
Housing	1,066	14.71	13.58	4.1%
Ecology	4,041	55.74	51.48	15.7%
<u>Economic Growth</u>				
Science	636	8.77	8.10	2.5%
Small Business	482	6.64	6.13	1.9%
Digital Economy	1,635	22.55	20.83	6.4%
Labor Productivity	52	0.72	0.66	0.2%
Export Support	957	13.20	12.19	3.7%
Transport Infrastructure	6,348	87.56	80.87	24.7%
Total	25,725	354.83	327.71	100%

Source: Government of the Russian Federation

* using R/\$ 72.5 rate

** using Rub-Eur 78.5 rate

- ❑ **Freely-floating ruble is a big help.** This was forced on the government in early 2015 and it has both helped budget management and increased economic competitiveness
- ❑ **No major financial interventions.** The Central Bank is not spending much money in an effort to support the ruble. FX Reserves dropped \$7 bln in March but recovered that in April
- ❑ **Targeting a R/\$65 rate.** The government confirms it prefers a ruble-dollar exchange rate near 65 over the medium term. The CBR will try to “manage” the rate towards this level – timing will depend on the oil price.

Ruble-Dollar Exchange Rate (LHS) and Brent US\$ p/bbl (LHS) - 3 Months

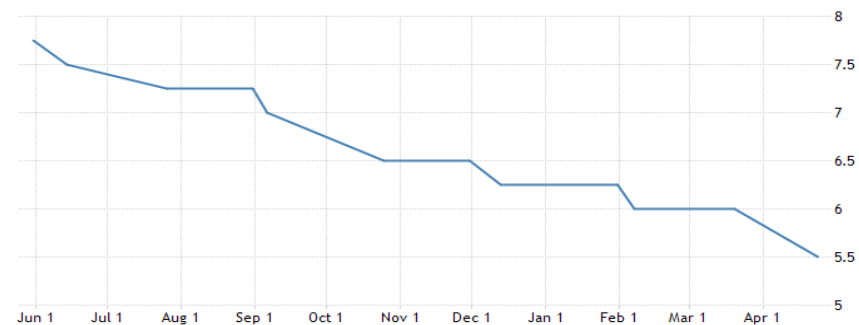


Source: TradingEconomics

- ❑ **OPEC+ deal saved the oil price.** The purpose of the OPEC+ & G20 deal was to provide temporary support for Brent. Despite the dip in late April, it is doing that
- ❑ **Recovery is based on optimism.** The Brent price should hold close to \$30 p/bbl while traders wait for evidence about:
 - Covid-19 impact
 - Oil demand trend
 - US production volumes
 - OPEC+ compliance
 - Oil inventory drawdown
- ❑ **Hard data comes in June.** The June meeting of OPEC+ will be important but the more important decisions about future cooperation may come only in the autumn
- ❑ **Saudi relationship is important for Russia.** It combines good business with good politics. Putin was very keen to repair the damage from the March 6th fallout as quickly as possible.

- ❑ **More cuts.** The CBR Governor said that she expects a cut of between 50 and 100 bps at the next policy meeting - June 19th
- ❑ **Pressing for greater debt cost relief.** The CBR is now leaning on the banks to cut the interest rate they charge to SMEs and to personal borrowers
- ❑ **No spike in inflation.** The CBR retains its year-end inflation target at 4% and sees a summer range of 5-6% range
- ❑ **Different to 2015.** There is much less of an inflation impact from the weak ruble than used be the case – the May inflation indicator will be published June 5

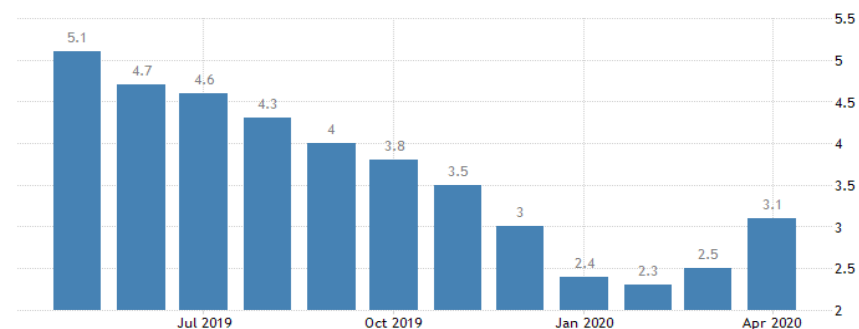
Russia Key Rate, %



SOURCE: TRADINGECONOMICS.COM | CENTRAL BANK OF RUSSIA

Source: Central Bank of Russia

Headline Inflation Rate: Trending up from April



SOURCE: TRADINGECONOMICS.COM | FEDERAL STATE STATISTICS SERVICE

Source: Tradingeconomics.com, Federal State Statistics Service

	2020(F)	2021(F)	2022(F)
❑ GDP	-3.5%	2.5%	2.5%
❑ Inflation, year end	4.5%	3.7%	3.5%
❑ CBR, Key Rate	4.5%	4.5%	4.0%
❑ Retail sales, % YoY	-6.0%	4.0%	2.5%
❑ Budget Balance, % GDP	-3.5%	-0.2%	0.2%
❑ Average Oil price, \$ p/bbl	\$36	\$48	\$55
❑ RUB/US\$, year end	70.0	68.0	65.0

Slide 26 for more Base Case macro forecast details

Provisional Pessimistic Case

	2020(F)	2021(F)	2022(F)
❑ GDP	-5.5%	-1.0%	1.0%
❑ Inflation, year end	6.5%	5.5%	5.0%
❑ CBR, Key Rate	5.0%	5.0%	5.0%
❑ Retail sales, % YoY	-8.0%	0.0%	1.0%
❑ Budget Balance, % GDP	-4.5%	- 1.0%	-0.1%
❑ Average Oil price, \$ p/bbl	\$28	\$33	\$45
❑ RUB/US\$, year end	78.0	74.0	70.0

Slide 27 for more Scenarios macro forecast details

CBR Remains Cautious

- ❑ **CBR expects a bounce in 2021** The Central Bank expects GDP to contract by between 4% and 6% this year based on a cautious and slow recovery from the current lockdown and a slower recovery in the oil price.

- ❑ **Pessimistic Audit Chamber.** The head of the Audit Chamber, former Finance Minister Alexei Kudrin, is notoriously more cautious than most others. He expects the decline in this year's GDP to mirror that seen in 2009 when the contraction was at 7.8%

Central Bank of Russia Revised Macro Forecasts

	2020F	2021F	2022F
GDP, % Change YoY	-4.0% to -6.0%	+2.8% to +4.8%	+1.5% to +3.5%
Inflation, year end, %	4.0%		
Budget Deficit, % of GDP	-4.0% to -6.0%		
Urals, \$ p/bbl average	\$27.0	\$35.0	\$45.0

Source: Central Bank of Russia

GDP, % Change - Others

	2020F
Finance Ministry	-5.0%
Audit Chamber	-7.0% to -8.0%
Fitch Rating Agency	-3.3%
Median Russian Economists	-3.7%

Source: Published comments

- ❑ **Sanctions threat level has eased, but not gone away.** There is optimism that the momentum in the US to pursue new sanctions against Russia has slowed, there have been reminders that the threat has not gone away
- ❑ **FBI & DHS report.** It reported that the US Department of Homeland Security and the FBI warned that Russia has new tactics for interfering in the 2020 US elections that **may include** "covertly advising candidates and campaigns." The report said Russia **may also** hack and release sensitive information about candidates, use "state-controlled media arms" or social media to "propagate election-themed narratives,"
- ❑ **Engaging with the EU.** Dmitry Kozak, discussed further steps in resolving the conflict in Ukraine's east (Donbas) in bilateral talks with German officials in Berlin recently. Unlike the US, the EU has specifically linked sanctions relief to progress in Donbass and Moscow appears intent on compromises with Ukraine to force the EU into some relief actions
- ❑ **Middle East.** Moscow appears to be avoiding major controversies while also trying to rebuild relations with Saudi Arabia

Momentum is Gaining

Agriculture & Food Processing

Telecoms & Online Commerce

Technology

Logistics & Packaging

Fintech

Medical Services & Equipment

Renewable Energy

Environment

Value-Added Processing

ESG

Momentum is or, may Slow

Retail – High Street & Malls

Real-Estate ... Offices

Aviation & Services

Banks – Traditional Services

Autos – combustion engines

Oil – longer Term

Construction – some areas

Hospitality

Chemicals – Plastics

Russia Macro Update – May:	Planning, and hoping, for a U Shaped Recovery
Russia Covid-19 Check-up:	Not out of the woods yet
Eurasia Covid-10 Check-Up:	Emerging Eurasia confidence
Russia-Eurasia Macro Update:	How has Covid019 and Oil affected the Region?
Future Growth Strategies:	The drive for export growth in Russia
Oil, Russia and OPEC+:	Survival of the Fittest
Beltway 360 series:	Covid-19 and Russia in US Politics
Kazakhstan:	Macro & Politics Update
Uzbekistan:	Health Sector Introduction

Please contact Sarah Ludwig on sel@macro-advisory.com if you would like a copy of any of these recent reports

Using Base Case Scenario Assumptions

	2013	2014	2015	2016	2017	2018	2019	2020E	2021E	2022E
GDP, RUB bln, nominal	70,499	77,200	84,320	90,222	95,004	99,944	105,741	112,866	121,702	129,410
GDP, US\$ bln	2,210	2,000	1,360	1,347	1,635	1,592	1,633	1,568	1,739	1,931
Growth, real % YoY	1.3%	0.7%	-2.8%	-0.2%	1.5%	2.3%	1.3%	-3.5%	2.5%	2.5%
CPI - year-end, % YoY	6.5%	11.4%	12.9%	5.4%	2.5%	4.3%	3.0%	4.5%	3.7%	3.5%
CPI- average, % YoY	6.8%	7.8%	15.6%	7.2%	3.8%	2.9%	4.5%	4.5%	4.0%	3.8%
Gross fixed investment, real % YoY	0.9%	-1.0%	-11.0%	0.8%	3.5%	4.3%	2.4%	-6.0%	4.0%	3.0%
Industrial production, real % YoY	0.4%	1.7%	-0.8%	2.2%	2.1%	2.9%	2.4%	-4.0%	3.5%	3.0%
Agricultural output, % change YoY	3.1%	1.2%	3.5%	4.8%	2.4%	-0.8%	4.1%	4.0%	4.2%	4.5%
Central bank key rate, %		17.0%	11.0%	10.0%	7.8%	7.75%	6.25%	4.50%	4.50%	4.00%
Bank average lending rate, %	9.5%	11.3%	16.0%	13.0%	10.5%	10.0%	8.5%	8.0%	7.5%	7.0%
Retail sales, % YoY	3.9%	2.5%	-10.0%	-5.2%	1.2%	2.6%	1.7%	-6.0%	4.0%	2.5%
Real disposable income, % YoY	4.8%	-1.0%	-6.5%	-5.9%	-1.7%	0.1%	0.8%	-3.5%	2.0%	1.5%
Unemployment, % EOP	5.6%	5.3%	5.6%	5.4%	5.0%	4.7%	4.6%	6.0%	5.2%	4.8%
Budget, balance % of GDP	-0.5%	-0.5%	-2.4%	-3.4%	-1.4%	2.7%	1.8%	-3.5%	-0.2%	0.2%
Current account, % GDP	1.6%	3.0%	5.3%	1.9%	2.1%	7.1%	4.3%	0.5%	1.0%	2.0%
RUB/US\$, year-end	32.9	61.4	73.5	61.3	57.7	69.4	62.0	70.0	68.0	65.0
RUB/US\$, average	31.9	38.6	62.0	67.0	58.1	62.8	64.8	72.0	70.0	67.0
RUB/EUR, year-end	45.3	72.0	79.7	64.5	69.7	79.5	69.5	78.0	76.0	72.0
RUB/EUR, average	42.3	51.5	67.0	74.0	68.0	73.9	71.5	80.0	79.0	75.0
Brent, US\$ p/bbl, average	\$108	\$100	\$54	\$45	\$55	\$72	\$63	\$36	\$48	\$56

Source: State Statistics Agency, Central Bank, Macro-Advisory estimates

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