Russian regions: emerging opportunities and existing challenges for growth

Analytical Credit Rating Agency (ACRA)

Natalia Porokhova
Head of Sovereign Ratings and Forecasting Group, PhD
natalia.porokhova@acra-ratings.ru
Deglobalization – one of Key Drivers of Changes in Russian Economy

Key trends in Russian economy that can contribute to future economic growth and development:

1. **Population ageing** – constrains economic growth but gives additional stimuli for some industries.

2. **Switching to low inflation mode** – higher predictability for business and cheaper loans, but government and businesses should seek new forms of flexibility.

3. **New major economic policy measures** – retirement age growth, VAT +2%, rebalancing expenditures (May decrees).

4. **Turn to East** – increase in share of Asian countries in exports, imports, FDI and external debt.

5. **Less globalized trade and finance** – sanctions are in the general trend of deglobalization.

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<tbody>
<tr>
<td>Real GDP (%; y-o-y)</td>
<td>2.5</td>
<td>0.2</td>
<td>1.5</td>
<td>1.6</td>
<td>1.4</td>
<td>1.5</td>
<td>1.4</td>
<td>1.4</td>
</tr>
<tr>
<td>Inflation (%; Dec/Dec)</td>
<td>13.2</td>
<td>5.4</td>
<td>2.5</td>
<td>4.2</td>
<td>4.6</td>
<td>4.0</td>
<td>3.9</td>
<td>3.8</td>
</tr>
<tr>
<td>Urals oil price, USD/bbl</td>
<td>51.3</td>
<td>42.3</td>
<td>53.5</td>
<td>72</td>
<td>63</td>
<td>59</td>
<td>61.6</td>
<td>62.8</td>
</tr>
<tr>
<td>USD/RUB (12-month average)</td>
<td>61.3</td>
<td>67.2</td>
<td>58.3</td>
<td>63.1</td>
<td>64.1</td>
<td>60.1</td>
<td>61.2</td>
<td>62.6</td>
</tr>
<tr>
<td>Unemployment, %</td>
<td>5.6</td>
<td>5.5</td>
<td>5.2</td>
<td>5.2</td>
<td>5.3</td>
<td>5.3</td>
<td>5.3</td>
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Now it is potential. Probability of something negative happening here has increased.

10 Years Ago Income Level in Russia Was Closer to Latin America Countries...

GRP per capita (according to PPP) compared to GDP per capita (according to PPP) in group of countries

<table>
<thead>
<tr>
<th>Region</th>
<th>PPP (2006)</th>
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<tbody>
<tr>
<td>Russia</td>
<td>$14916</td>
</tr>
<tr>
<td>South Asia</td>
<td>$3071</td>
</tr>
<tr>
<td>East Asia (excl. Japan)</td>
<td>$5917</td>
</tr>
<tr>
<td>Latin America</td>
<td>$11295</td>
</tr>
<tr>
<td>East Europe</td>
<td>$15889</td>
</tr>
<tr>
<td>Eurozone</td>
<td>$32539</td>
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</table>

- **Purchasing power parity (PPP)** states that the purchasing power of a sum of money in one country should be able to purchase the same basket of goods no matter from where the consumption basket was bought.
- The estimation of PPP for Russian regions is based on the basis of Rosstat statistics depending on different prices on the same consumer basket.

Source: ACRA, World Bank, Rosstat
Now It is Closer to Eastern European Countries

GRP per capita (according to PPP) compared to GDP per capita (according to PPP) in group of countries

- **2016**
  - Russia = $24789
  - East Asia (excl. Japan) = $13840
  - Latin America = $15211
  - East Europe = $26851
  - Eurozone = $42064

**Purchasing power parity (PPP)** states that the purchasing power of a sum of money in one country should be able to purchase the same basket of goods no matter from where the consumption basket was bought.

The estimation of PPP for Russian regions is based on the basis of Rosstat statistics depending on different prices on the same consumer basket.

Source: ACRA, World Bank, Rosstat
Differentiation across Regions Decreased between Crises

Russian GDP growth and regions contribution to it, %

Source: ACRA
Political Factor Can Influence Regions Credit Quality in the Future

- Share of regions and municipalities bonds with ACRA rating is 77% (34 out of 84, as at November 9, 2018).
- In 31 Russian regions governor was changed in 2018.

Source: ACRA
Budgets of 10 out of 85 Subjects of the Russian Federation Depend on Sanctioned Companies by more than 20%
Number of Long-Term Oil Field Development Projects Were Cancelled after Sanctions

- Majority of cancelled projects are Rosneft and ExxonMobil joint ventures
- Estimate of ExxonMobil losses – $200 mln

Estimate of resources at the projects (as at 01.01.2018):

- Oil and gas condensate – 12.3 bln tons
- Gas – 15.2 trln m³

Source: Rosneft's website

http://www.acra-ratings.com/
Sanctions' Effects on the Financial Performance of Companies and Banks Are Weak...

Source: Bloomberg, ACRA
Sanctions have accelerated the development and implementation of measures aimed at higher sustainability of the Russian economy:

- **Trade barriers.** Russian countersanctions have limited the imports of certain categories of food products, which led to an increase in their prices. The effect on real incomes of the population is estimated at -2–3 p.p. for 2018.

- **Financial market infrastructure.** The threat of disruption of the continuous monetary turnover accelerated the development of regulations that stimulate the use of internal alternatives of global financial services in the following areas: payment systems, credit ratings, etc.

- **Data storage and software localization.** The need to meet the localization regulations increased the costs of technology-intensive and telecommunications companies.

- **Fiscal policy.** The budget planning process is now based on assumptions that are more conservative. External borrowings are no more considered a reliable source of funding.

- **International reserves.** The need to preserve liquidity has led to a change in the structure of investments: the share of sovereign securities issued by sanctions initiators has declined (probably, for a long period).
US Residents Hold 8% of Russian Sovereign Debt

Geography of holders of Russian sovereign debt (Federal Loan Bonds (OFZ) + Eurobonds), as at January 1, 2018

Sources: IMF, national central banks, Bloomberg, ACRA
ACRA sees its mission in developing best practices that provide the Russian financial market with basis for sustainable performance.

ACRA's expertise is unique in terms of its competences and profound understanding of credit risk.

ACRA trainings are aimed at enhancing qualifications of financial market participants and building up efficiency of managerial and investment decision making.

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- Fundamentals of credit analysis of regional and municipal authorities (December 3-4, 2018)
- Fundamentals of structured finance deals analysis (December 10-11, 2018)
- Fundamentals of credit analysis of banks and non-banking credit institutions (January 24-25, 2019)
- The art of presentation in credit analysis hosted and presented by Ekaterina Trofimova, ACRA CEO (February 27-28, 2019)
- Change management hosted and presented by Ekaterina Trofimova, ACRA CEO (March 22, 2019)
- Fundamentals of credit analysis of insurance companies (April 4-5, 2019)
- Fundamentals of asset management companies reliability analysis and credit analysis of non-state pension funds (April 18-19, 2019)
- Fundamentals of sovereign risk credit analysis (April 23-24, 2019)
- Forecasting in credit analysis. Course 1: macroeconomic and industry forecasting fundamentals (May 14-15, 2019)
- Advanced analysis of structured finance deals (May 21-22, 2019)
- Forecasting in credit analysis. Course 2: practical aspects of economic modeling (September 9-10, 2019)

For more information and enrollment, please contact
Artem Mayorov, Manager
artem.mayorov@acra-ratings.ru
+7 495 139 04 80, ext. 147
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[https://www.acra-ratings.com/research](https://www.acra-ratings.com/research)

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<th>Sector</th>
<th>Document Type</th>
<th>Date</th>
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<tbody>
<tr>
<td>Stressful scenarios are becoming more likely for the Russian economy</td>
<td>Sovereigns</td>
<td>Forecast</td>
<td>25.10.2018</td>
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<td>Russia 2022 Economic Outlook Update</td>
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<tr>
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<td>Telecommunications</td>
<td>Forecast</td>
<td>12.10.2018</td>
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<td>Russian telecom market: 2022 outlook</td>
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<td>Sovereigns</td>
<td>Analytical comment</td>
<td>21.08.2018</td>
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<td>Structural Financial Stress Index for Kazakhstan</td>
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<tr>
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<td>Sovereigns</td>
<td>Analytical comment</td>
<td>17.08.2018</td>
</tr>
<tr>
<td>Geography of holders of Russian sovereign debt</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Growth of dividends paid by Russian major companies is curbed by negative cash flow</td>
<td>Corporates</td>
<td>Research</td>
<td>31.07.2018</td>
</tr>
<tr>
<td>Analysis of dividend payouts by Russian non-financial companies</td>
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<tr>
<td>Oil dependence recovers along with Azerbaijan economy coming out of stagnation</td>
<td>Sovereigns</td>
<td>Forecast</td>
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Contact Details

Russian website: www.acra-ratings.ru
English website: www.acra-ratings.com

ACRA Rating Agency

General Contacts:
info@acra-ratings.ru
+7 495 139 04 80
75, Sadovnicheskaya emb.,
Moscow, 115035, Russia

On Cooperation Issues:
Client Manager
Marina Leeva
marina.leeva@acra-ratings.ru
+7 495 139 04 80, ext. 123

Regulatory Affairs & Compliance:
Head of Compliance and Internal Control
Alexandra Prokudina
alexandra.prokudina@acra-ratings.ru
+7 495 139 04 80, ext. 155

Credit Ratings Methodology:
Director – Head of Methodology
Artem Iskandarov
artem.iskandarov@acra-ratings.ru
+7 (495) 139 0494
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