



Bank of Russia



BANKING SECTOR LIQUIDITY AND FINANCIAL MARKETS

No. 8 (54) • August 2020

Information and analytical commentary

10 September 2020

BANKING SECTOR LIQUIDITY AND FINANCIAL MARKETS: FACTS, ASSESSMENTS AND COMMENTS (AUGUST 2020)

- The structural liquidity surplus averaged 1.9 trillion rubles in the August required reserve averaging period, remaining the same compared to the July averaging period. The decrease in the liquidity surplus as of the beginning of September was the result of the redistribution of funds between credit institutions' correspondent and deposit accounts with the Bank of Russia and the outflow of liquidity caused by a rise in the amount of cash in circulation.
- The spread between interbank lending rates and the Bank of Russia key rate contracted to -12 bp (vs -25 bp in the July averaging period). The reason for this was that market participants' expectations regarding a key rate change had no impact on interest rate movements.
- The interest rate spread in the FX swap and interbank lending segments remained negative (-25 bp on average) amid a reduction in the banking sector's foreign currency liquidity in June – August.
- In August, financial markets in the majority of countries continued to recover. Furthermore, markets in advanced economies showed more solid growth compared to developing countries. Specifically, elevated volatility, predominantly caused by local factors, was observed in August in the foreign exchange markets of Turkey, Brazil, Chile and Russia.
- In July, most banks reviewed their deposit conditions, following which the decline in retail deposit rates sped up. Moreover, short-term ruble deposits were the main drag on the growth of the retail deposit portfolio.
- Interest rates on corporate loans continued to trend down in June. Preferential lending support programmes contributed to the decrease in the interest rate on long-term SME loans which dropped below the market average. In July, the average mortgage interest rate hit its new record low once again.
- Record-high disbursements of mortgage loans, coupled with the continuing recovery in unsecured consumer lending, accelerated the growth of the retail loan portfolio.

Banking sector liquidity and money market

Ruble liquidity. The structural liquidity surplus averaged 1.9 trillion rubles in the August required reserve averaging period, remaining the same compared to the July averaging period. As of the end of August, the structural liquidity surplus totalled 1.6 trillion rubles, shrinking by 0.5 trillion rubles against the end of the previous month (Table 2).

The decrease in the liquidity surplus as of the beginning of September was primarily the result of the redistribution of funds between credit institutions' correspondent and deposit accounts with the Bank of Russia. Although the averaging of required reserves was sufficiently uniform in July and August, balances in

correspondent accounts increased by 0.3 trillion rubles as of the beginning of September.

The impact of budget operations on liquidity was almost neutral (Chart 1). Budget revenues from the payment of the main taxes continued to recover in August. In addition, a number of major companies transferred dividends to the budget. At the same time, there was a seasonal decrease in budget spending. General government expenditure exceeded general government revenues, and as before, this difference was financed through OFZ offerings and fiscal rule-based operations to sell foreign currency. Banks' debt on Federal Treasury (FT) operations also slightly contracted (Chart 7).

The outflow of liquidity provoked by an increased amount of cash in circulation continued to decrease, approaching its August 2019 level.

Among other things, this was associated with the progressive revival of economic activity and an increase in cash collected as retailers' earnings. Yet, the reduction in cash settlements is still insignificant.

A slight outflow of funds from banks was also associated with their payments of insurance premia and the partial loan repayment to the Deposit Insurance Agency.

Money market. The spread between short-term interbank lending rates¹ and the Bank of Russia key rate contracted to -12 bp (vs -25 bp in the July averaging period) (Chart 2). The spread volatility decreased to 7 bp (vs 15 bp in the July averaging period). The month before, as market participants expected a further reduction in the key rate, this put downward pressure on interest rates. However, there was no key rate revision in August, and therefore, this factor did not impact the behaviour of market participants. As a result, the average spread got close to the levels of those averaging periods when the key rate was not expected to go down either.

Foreign currency liquidity. The interest rate spread in the FX swap and interbank lending (basis) segments changed only slightly, averaging -25 bp (vs -20 bp in the July averaging period) (Chart 3). The basis remained negative due to the reduction in the banking sector's foreign currency liquidity in June – August resulting from a low foreign currency inflow in the current account of the balance of payments. The latter was associated with low oil prices, coupled with oil production cuts under the OPEC+ deal, as well as dividend payouts and a slight rise in foreign currency lending.

The forecast of the structural liquidity surplus for the end of 2020 remains at the level of 1.4–2.0 trillion rubles.

Key rate expectations. Market participants' expectations regarding the key rate remained almost unchanged in August, while expectations based on market indicators slightly increased. However, this rise was due to the growth of the risk premium driven by higher volatility in the foreign exchange and bond markets (Table 1).

¹ The interbank lending rate is the interest rate charged on unsecured loans in the money market.

KEY RATE EXPECTATIONS REMAINED UNCHANGED

Table 1

1. Expectations based on market indicators,* interest rate (instrument)	September 2020	December 2020
– MosPrime 3M (FRA)	3.99 (4.35)	4.19 (4.45)
– RUONIA (ROISfix)	4.29 (4.12)	4.29 (4.01)
– RUONIA (futures)	– (4.12)	4.04 (4.01)
2. Analysts' key rate expectations*	As of 30.09.2020	As of 31.12.2020
– Bloomberg survey	4.00 (4.00)	4.00 (4.00)
– Reuters survey	4.00 (4.00)	4.00 (4.00)

* The values are given as of the end of the current and previous (in brackets) months.
Source: Bank of Russia calculations.

IN AUGUST 2020, THE BANKING SECTOR'S STRUCTURAL LIQUIDITY SURPLUS DECREASED
(START OF BUSINESS, BILLIONS OF RUBLES)

Table 2

	01.01.2017	01.01.2018	01.01.2019	01.01.2020	01.08.2020	01.09.2020
Structural liquidity deficit (+) / surplus (-)	736	-2,639	-3,016	-2,761	-2,076	-1,596
Bank of Russia's claims on credit institutions	1,258	10	21	18	10	13
Auction-based facilities	216	-	-	-	5	5
– repos and FX swaps	-	-	-	-	5	5
– secured loans	216	-	-	-	-	0
Fixed interest rate facilities	1,042	10	21	18	5	8
– repos and FX swaps	632	4	8	13	0	3
– secured loans	411	5	13	5	5	5
Credit institutions' claims on the Bank of Russia	785	2,729	3,293	2,983	2,647	2,185
Deposits	785	2,372	1,902	1,026	1,939	1,355
– auction-based	397	2,125	1,478	697	1,750	1,210
– fixed interest rate	388	247	424	330	189	145
BoR coupon bonds	0	357	1,391	1,956	708	830
Standing reverse facilities, other than standard monetary policy instruments of the Bank of Russia*	263	81	256	204	561	576

* These transactions include the Bank of Russia's specialised refinancing instruments, loans granted by the Bank of Russia within irrevocable credit lines, and USD/RUB and EUR/RUB sell/buy FX swaps.
Source: Bank of Russia calculations.

THE FORECAST OF THE STRUCTURAL LIQUIDITY SURPLUS FOR THE END OF 2020 REMAINS
AT THE LEVEL OF 1.4–2.0 TRILLION RUBLES
(TRILLIONS OF RUBLES)

Table 3

	2019 (actual)	January – August 2020	August 2020	2020 (forecast)
1. Liquidity factors	0.5	-0.9	-0.2	[-1.4; -0.9]
– change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	0.2	1.0	0.0	[0.2; 0.5]
– change in the amount of cash in circulation	-0.1	-2.0	-0.1	[-1.6; -1.4]
– Bank of Russia interventions in the domestic FX market and monetary gold purchases**	0.4	0.1	0.0	0.1
– regulation of banks' required reserves with the Bank of Russia	0.0	0.0	0.0	-0.1
2. Change in free bank reserves (correspondent accounts)*** (demand)	0.7	0.3	0.3	[-0.1; 0.0]
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	-0.3	-0.8	-0.5	[-1.1; -0.5]
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	-0.1	0.4	0.0	0.3
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	-2.8	-1.6		[-2.0; -1.4]

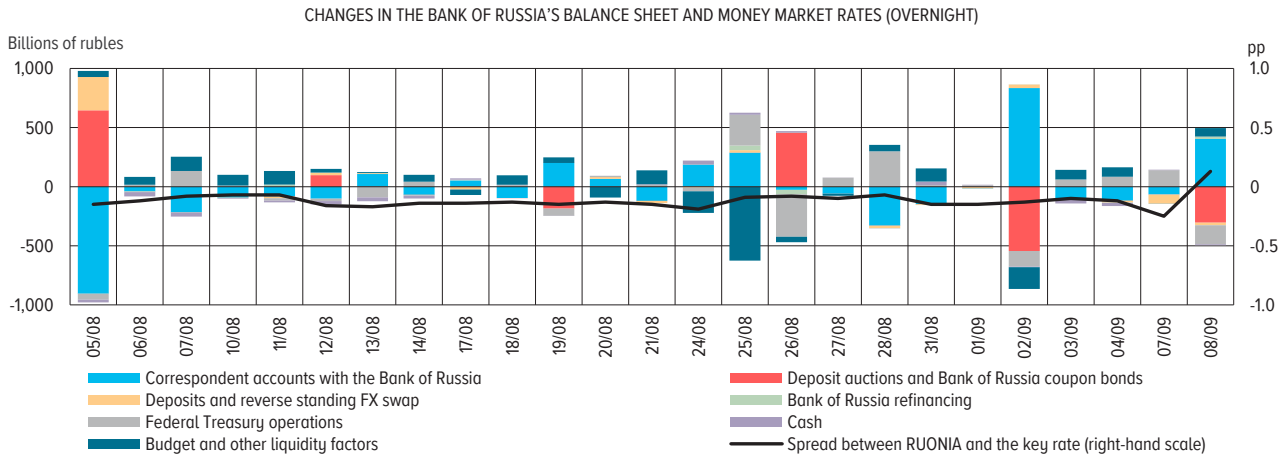
* Including fiscal rule-based operations to buy (sell) foreign currency in the domestic FX market, settlements on Bank of Russia USD/RUB FX swaps, and other operations.

** Forecast values of the indicator are in line with the actual amount of operations conducted.

*** The forecast for the end of the year implies uniform averaging of required reserves by banks and correspondent account balances close to the required ratio.
Source: Bank of Russia calculations.

IN AUGUST 2020, THE OUTFLOW OF LIQUIDITY FROM BANKS CAUSED BY AN INCREASED AMOUNT OF CASH IN CIRCULATION CONTINUED TO DECREASE, WITH THE IMPACT OF BUDGET OPERATIONS ON LIQUIDITY BEING ALMOST NEUTRAL

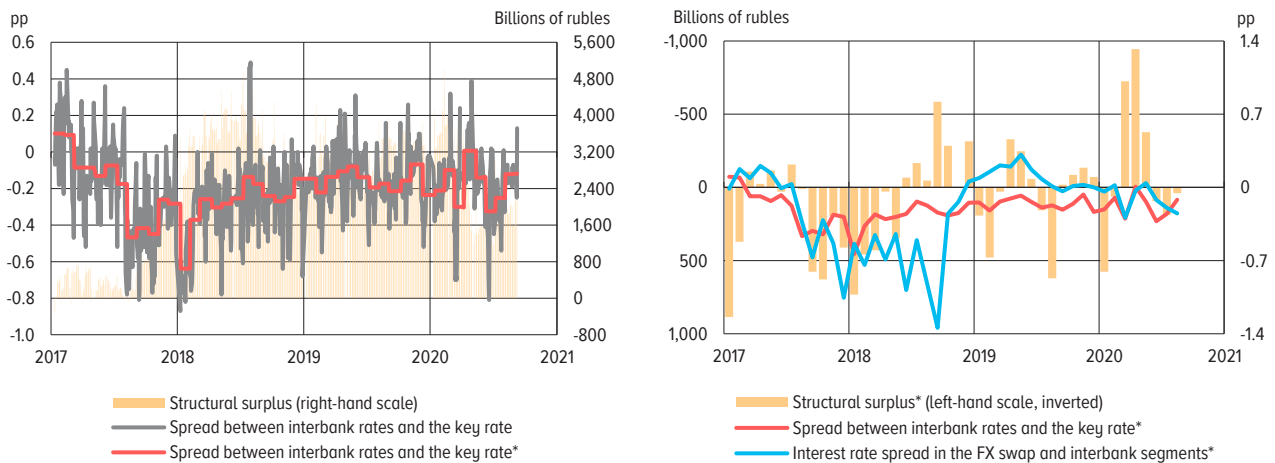
Chart 1



Source: Bank of Russia calculations.

THE SPREAD BETWEEN INTERBANK LENDING RATES AND THE BANK OF RUSSIA KEY RATE CONTRACTED

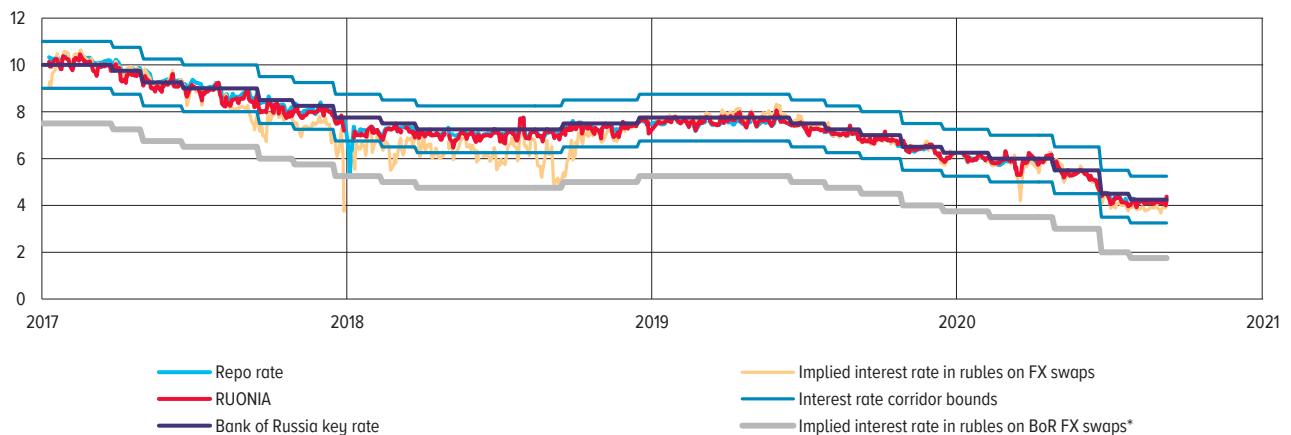
Chart 2



* Average for averaging periods.
Source: Bank of Russia calculations.

THE SPREAD IN THE FX SWAP AND INTERBANK LENDING SEGMENTS CHANGED ONLY SLIGHTLY (% P.A.)

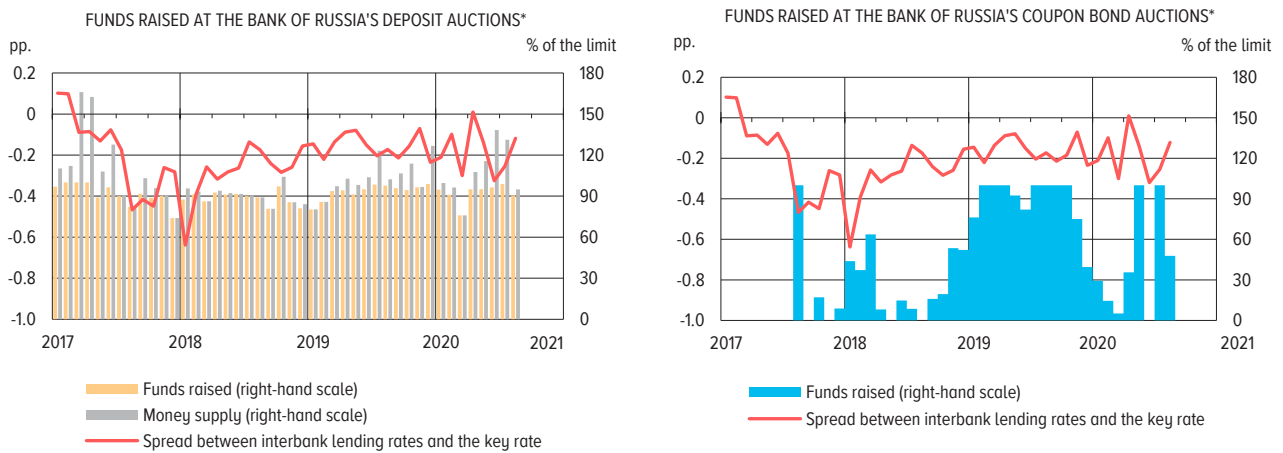
Chart 3



* Implied rate on BoR reverse FX swap = ruble lending rate – foreign currency borrowing rate + LIBOR (from 19.12.2016: key rate – 1 pp – (LIBOR + 1.5 pp) + LIBOR = key rate – 2.5 pp).
Source: Bank of Russia calculations.

BANKS' SUPPLY AT THE BANK OF RUSSIA'S WEEKLY DEPOSIT AUCTIONS WAS CLOSE TO THE ESTABLISHED LIMITS

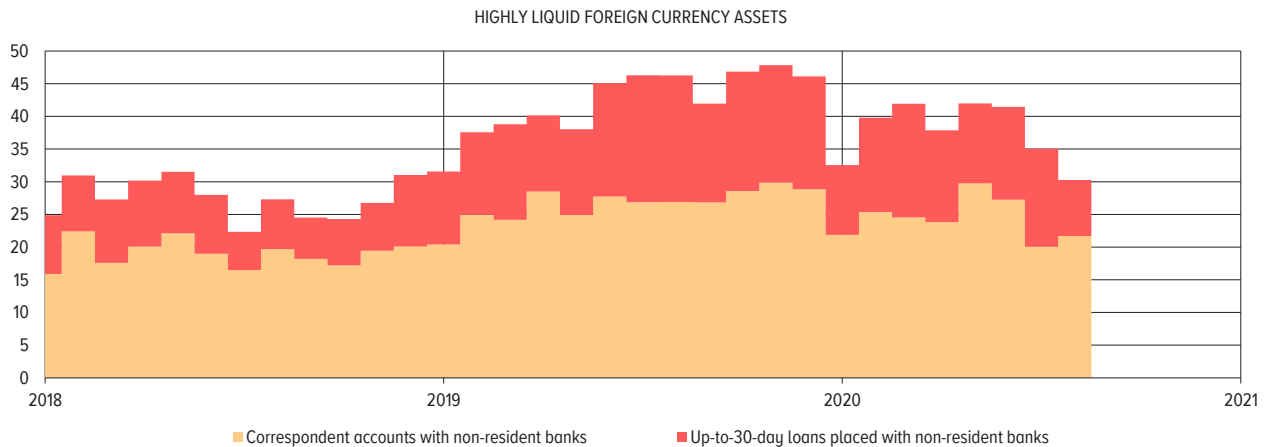
Chart 4



* Average for averaging periods.
 Source: Rosstat.

THE AMOUNT OF HIGHLY LIQUID FOREIGN CURRENCY ASSETS DECREASED IN JULY (AS OF 1 AUGUST)
(BILLIONS OF US DOLLARS)

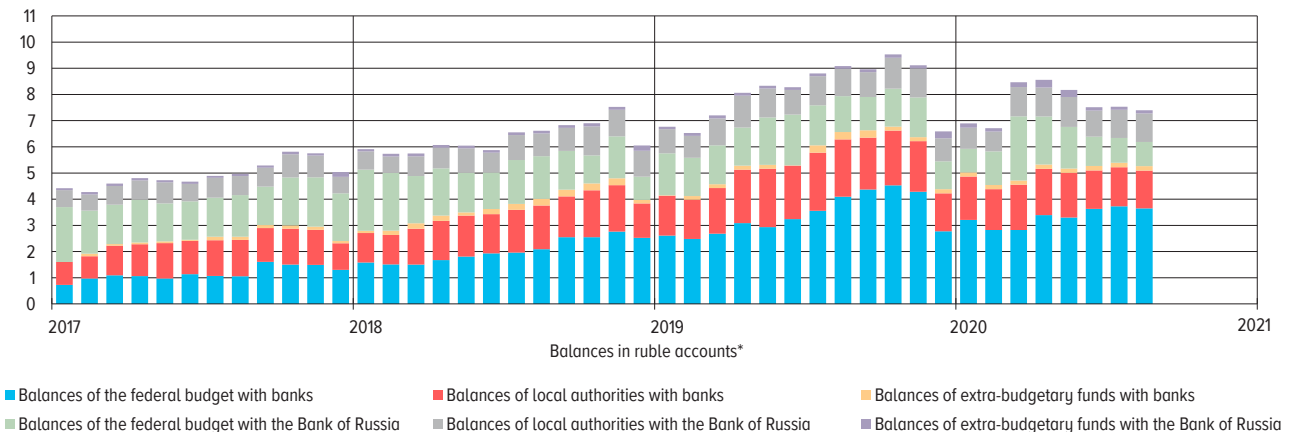
Chart 5



Source: Bank of Russia calculations

IN AUGUST 2020, BALANCES IN THE FEDERAL BUDGET ACCOUNTS WITH THE BANK OF RUSSIA REMAINED ALMOST UNCHANGED AS GENERAL GOVERNMENT REVENUES GRADUALLY RECOVERED AMID THE SEASONAL DECREASE IN BUDGET SPENDING
(TRILLIONS OF RUBLES, AS OF THE PERIOD-END)

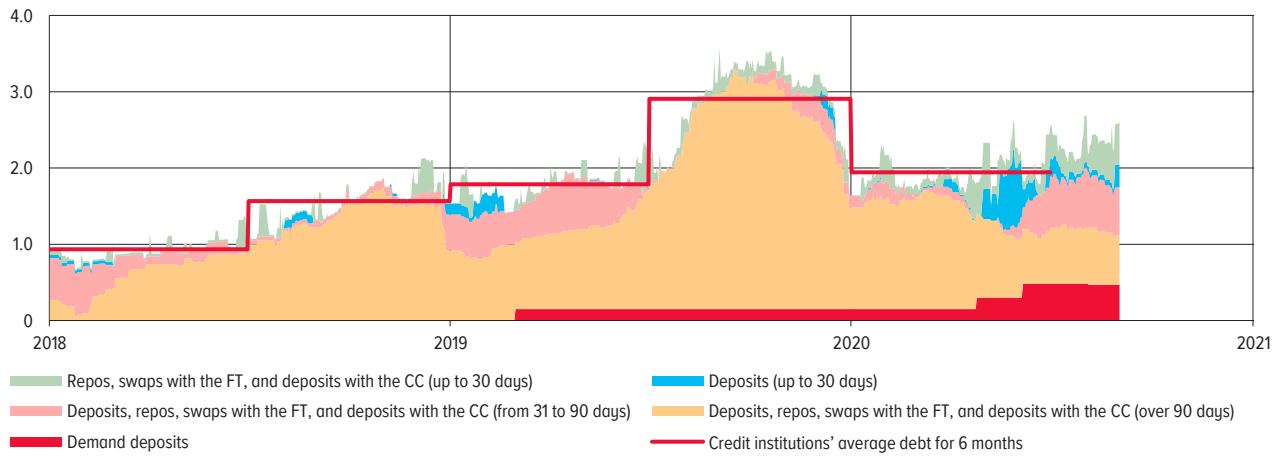
Chart 6



* According to banking reporting form 0409301 'Performance indicators of a credit institution'.
 Source: Bank of Russia calculations.

CREDIT INSTITUTIONS' DEBT TO THE FEDERAL TREASURY SHRANK BY 0.1 TRILLION RUBLES IN AUGUST 2020
(TRILLIONS OF RUBLES)

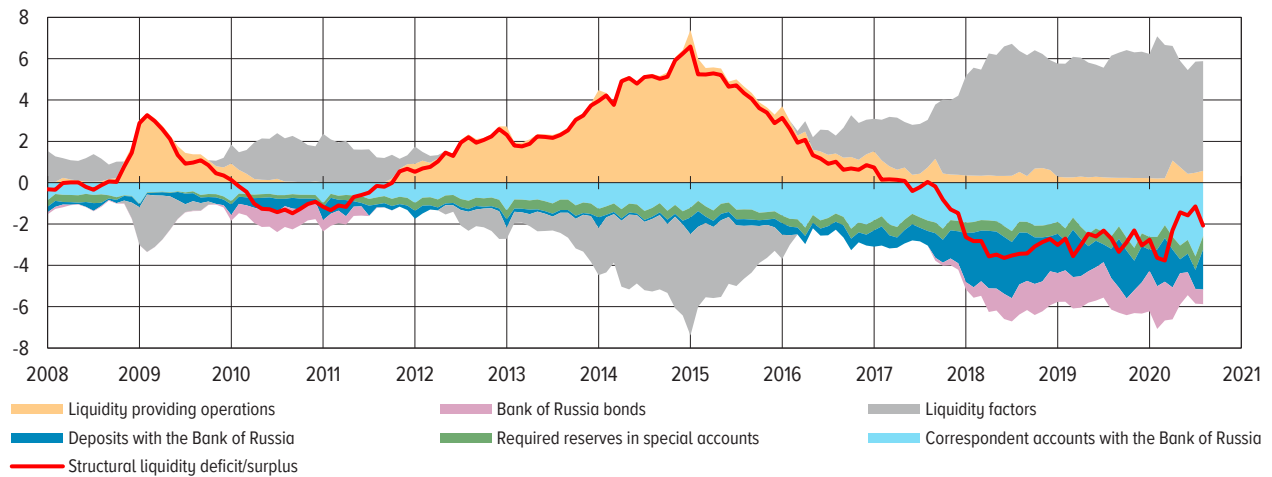
Chart 7



Sources: Federal Treasury, Bank of Russia calculations.

BANK OF RUSSIA'S BALANCE SHEET
(TRILLIONS OF RUBLES)

Chart 8



Source: Bank of Russia calculations.

Foreign exchange and stock markets

In August, financial markets in the majority of countries continued to recover. Furthermore, markets in advanced economies showed more solid growth compared to developing countries. Specifically, elevated volatility, predominantly caused by local factors, was observed in August in the foreign exchange markets of Turkey, Brazil, Chile and Russia.

Exchange rate. The exchange rate of the ruble gained 0.4%, reaching 74.07 rubles per US dollar, as a result of its strengthening over the last week of the month. However, the ruble was weakening over the most part of the month, falling at its lowest to 76 rubles per US dollar. The depreciation of the ruble was associated with increased geopolitical risks, the conversion of dividend payouts into foreign currency, and low sales of foreign currency revenues. As of the end of August, the MSCI EM Currency Index lost 0.3%, which resulted from declines in the exchange rates of the Brazilian real by 4.9%, the Turkish lira by 5.1%, and the Chilean peso by 2.6%. Other major EMEs' currencies were up. This rise did not exceed 2% (Chart 9).

Country risk premium. Russia's CDS spread changed only slightly, shrinking by 2 bp, to 102 bp (Chart 10). Risk premia also trended down in the majority of other EMEs, including Brazil, Turkey and Chile facing a rise in volatility in the foreign exchange market. In the second half of September, 5-year CDS spreads may grow by 10–20 bp due to technical reasons. Specifically, the basic contract will be changed because by this time the maturity of the basic contract will be 4.5 years.

Federal government bonds. The slope of the OFZ yield curve continued to increase: OFZ 2Y – to 4.46% (-3 bp), OFZ 5Y – to 5.37% (+11 bp), and OFZ 10Y – to 6.28% (+21 bp). August recorded a rise in yields on long-term bonds in the majority of countries. In particular, yields on 10-year government bonds gained 18 bp in the USA, 15 bp in Germany, 21 bp in the UK, 35 bp in Mexico, and 61 bp in Brazil (Table 4). There

are several factors that might have driven the growth of yields in these economies, which include an increase in inflation expectations due to large-scale economy support measures, the expansion of public borrowing by the majority of the above states, and the US Fed's new strategy to adopt an average inflation target.

Russia's Ministry of Finance reduced borrowings in August because of a rise in OFZ yields and higher volatility in the foreign exchange market, opting for variable coupon-income federal government bonds (OFZ-PK). Market participants demonstrated high demand at OFZ-PK auctions. However, the majority of the bids involved a significant yield premium, due to which the actual amount of the offerings by Russia's Ministry of Finance was not high. Over the month, the Ministry managed to raise 179 billion rubles, which is 20.7% less than in July. For the Ministry of Finance to achieve its Q3 target for borrowings in September, it should place bonds amounting to nearly 600 billion rubles at five auctions. Given the record-high placements in May, when the Ministry was able to raise each time 130–180 billion rubles over one auction, this target is technically achievable. However, since the potential for further reduction in the key rate has been largely utilised by now, in contrast to May (which was one of the key drivers of demand in April – June), the Ministry of Finance will likely have to offer premia. Furthermore, provided geopolitical risks go down, a rise in foreign investors' demand for OFZ may also contribute to the achievement of this target. In August, their OFZ holdings remained almost unchanged, despite increased risks (Chart 13). Concurrently, the recent auctions recorded non-residents' demand for OFZ-PK that had been previously purchased only by residents. This was probably associated with unsatisfied demand for fixed-coupon federal government bonds (OFZ-PD) since their supply contracted this month.

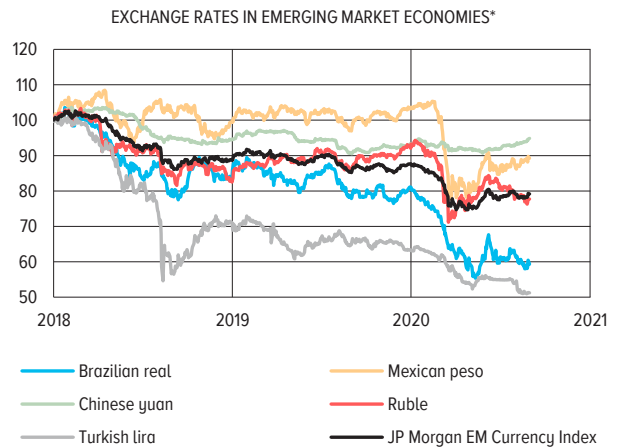
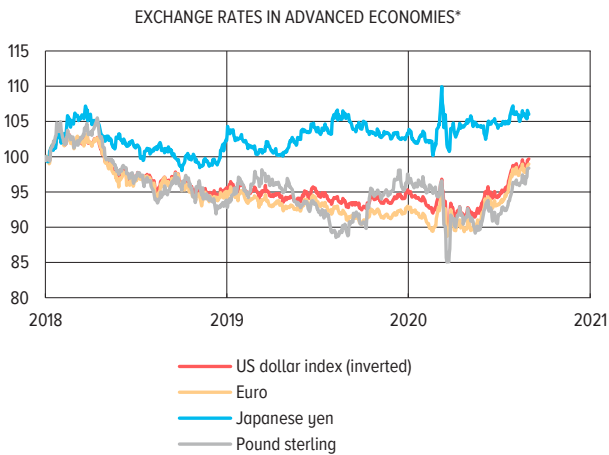
Stocks. Stock indices in most advanced economies increased by about 7–8%. The S&P index erased its March losses, hitting a new record high. EMEs showed a less uniform rise in

their indices. The US dollar-denominated MSCI EM index edged higher by 2.1%, while the MSCI Brazil, MSCI Chile and MSCI Turkey declined by 9.0%, 9.8% and 8.4%, respectively (Chart 12).

The MOEX Index gained 1.9% in August, while remaining below its early 2020 high of 8%. The RTS Index rose by 2.0%.

EXCHANGE RATES IN EMES CHANGED IN A DIVERSE MANNER
(02.01.2018 = 100)

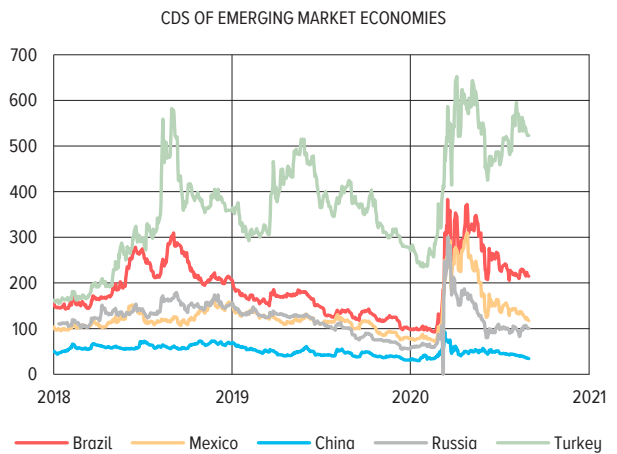
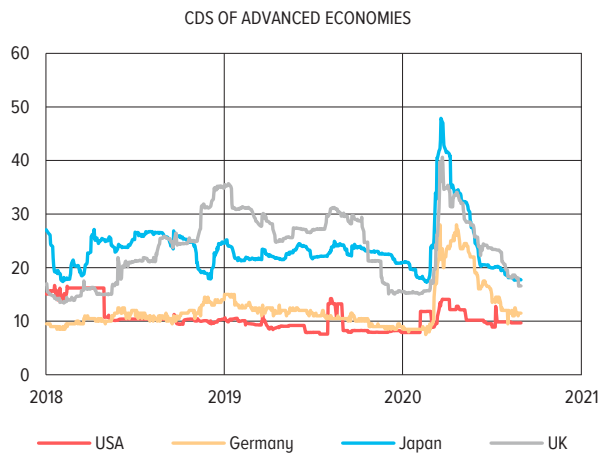
Chart 9



* Against the US dollar. Reverse exchange rates.
Sources: Bloomberg, Bank of Russia calculations.

IN THE MAJORITY OF ECONOMIES, CDS SPREADS CONTRACTED DESPITE INCREASED VOLATILITY
IN THE FX MARKET OF A NUMBER OF EMES
(BP)

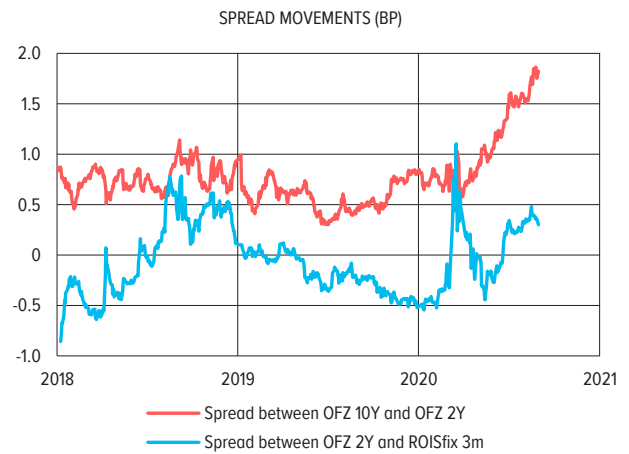
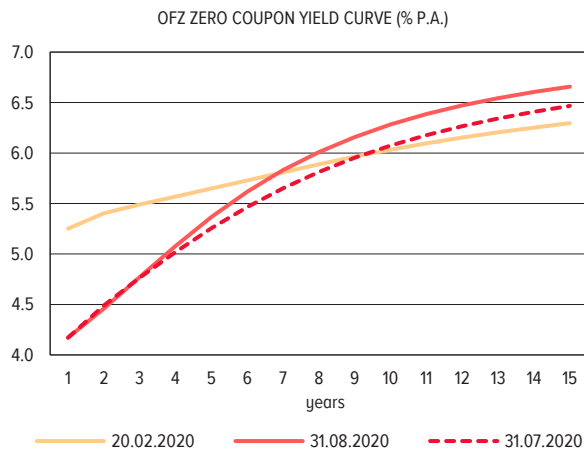
Chart 10



Sources: Bloomberg, Thomson Reuters, Bank of Russia calculations.

THE SLOPE OF THE OFZ YIELD CURVE CONTINUED TO INCREASE

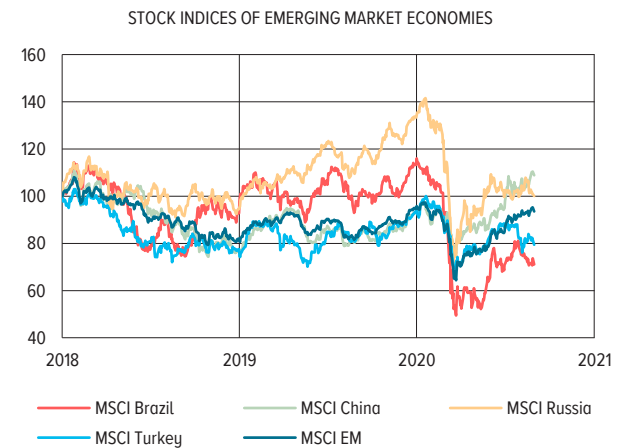
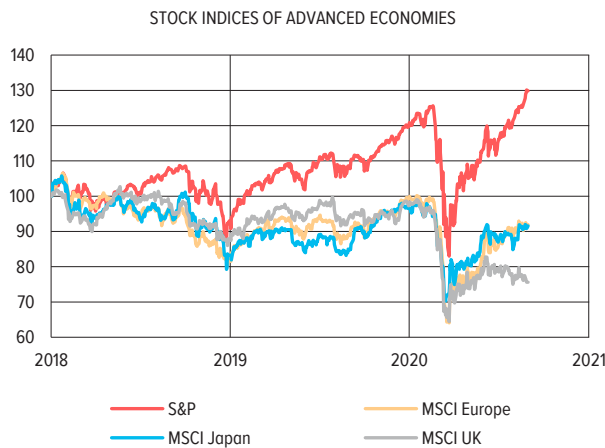
Chart 11



Source: PJSC Moscow Exchange.

S&P 500 ERASED EARLY 2020 LOSSES, HITTING A NEW RECORD HIGH (02.01.2018 = 100)

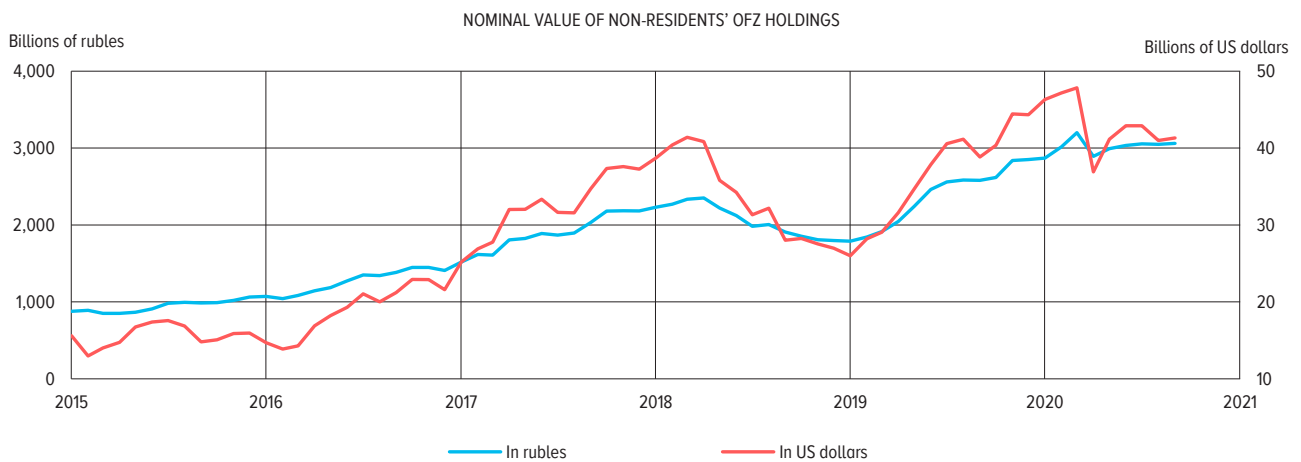
Chart 12



Источники: Bloomberg, расчеты Банка России.

FOREIGN INVESTORS' OFZ HOLDINGS REMAINED ALMOST THE SAME

Chart 13



Source: Bank of Russia calculations.

THE DOMESTIC AND EXTERNAL MARKETS DEMONSTRATED A RISE IN YIELDS
ON LONG-TERM GOVERNMENT BONDS

Table 4

Indicator		31.08.2020	1M	3M	6M	YTD	1Y
Russian financial market							
RUB/USD exchange rate		74.01	0.2	-7.2	-11.6	-19.5	-11.2
MOEX Index		2,966	1.9	7.9	7.2	-2.6	9.3
RTS Index		1,259	2.0	0.9	-3.4	-18.7	-2.0
Government bond yield		5.72	14	39	-56	-49	-139
Corporate bond yield		6.01	5	2	-67	-72	-181
Regional bond yield		5.68	-8	-16	-88	-59	-215
CDS spread		100	-4	-14	19	45	0
RVI		33	1	-2	-5	11	12
Exchange rates (per US dollar, % change, '+' – appreciation, '-' – depreciation)							
AEs*	US Dollar Index	92.14	-1.3	-5.8	-5.4	-4.4	-6.5
	Euro	1.19	1.3	7.2	7.2	6.4	7.9
	Japanese yen	105.91	-0.1	1.6	2.3	2.6	0.6
	Pound sterling	1.34	2.2	7.0	4.8	0.9	9.8
EMEs	JP Morgan EM Currency Index	55.45	-0.3	0.9	-5.3	-9.7	-7.3
	Ruble	74.01	0.2	-7.2	-11.6	-19.5	-11.2
	Brazilian real	5.49	-5.0	-2.4	-18.6	-26.8	-24.1
	Mexican peso	21.89	1.8	0.7	-11.4	-13.5	-8.0
	Chinese yuan	6.85	1.8	4.1	1.6	1.7	4.3
	Turkish lira	7.34	-5.1	-7.3	-16.1	-19.1	-20.6
	South African rand	16.94	0.8	2.5	-9.1	-17.4	-9.6
10-year bond yield (% p.a., change in bp, '+' – increase, '-' – decrease)							
AEs	USA	0.71	18	5	-46	-121	-79
	Germany	-0.40	13	1	23	-21	30
	Japan	0.05	3	4	17	7	34
	UK	0.31	21	8	-9	-51	-12
EMEs	Russia	6.08	15	59	-34	-28	-109
	Brazil	6.92	64	-6	61	23	-44
	Mexico	6.07	35	-8	-50	-82	-94
	China	3.02	5	29	28	-12	-1
	Turkey	13.50	100	205	121	155	-210
	South Africa	9.27	3	50	11	25	37
CDS spreads (% p.a., change in bp, '+' – increase, '-' – decrease)							
AEs	USA	10	0	-1	1	2	-4
	Germany	12	-1	-8	2	3	1
	Japan	18	-1	-7	-6	-3	-6
	UK	17	-3	-9	-1	1	-13
EMEs	Russia	100	-4	-14	19	45	0
	Brazil	215	-3	-62	89	115	77
	Mexico	117	-26	-55	16	39	2
	China	34	-9	-19	-14	3	-12
	Turkey	523	-31	-13	165	246	98
	South Africa	287	-20	-43	88	124	98
Stock indices (points, % change, '+' – increase, '-' – decrease)							
AEs	S&P	3,500	7.0	14.5	13.3	8.3	19.7
	MSCI Europe	1,652	3.9	10.6	3.5	-7.4	3.3
	MSCI Japan	984	7.91	3.7	5.9	-5.2	9.1
	MSCI UK	1,676	0.8	-4.0	-11.8	-22.3	-18.7
EMEs	MSCI EM	1,102	2.1	15.8	8.3	-1.2	13.5
	MSCI Russia	605	0.2	-4.2	-9.1	-25.0	-10.5
	MSCI Brazil	1,490	-9.0	8.6	-23.7	-37.2	-26.2
	MSCI Mexico	3,484	0.3	-0.7	-21.6	-26.8	-19.1
	MSCI China	101	5.6	21.7	19.6	17.3	34.3
	MSCI Turkey	1,282,408	-3.4	-4.6	-6.7	-14.7	-2.7
	MSCI South Africa	1,299	-1.8	10.1	4.3	-5.2	-1.6

* Advanced economies.

Sources: Bloomberg, PJSC Moscow Exchange, Cbonds.ru, Bank of Russia calculations.

Credit and deposit market

Deposit rates. In July, most banks expectedly reduced their interest rates on standard deposit products, which pushed average market interest rates on retail deposits downwards.¹ Moreover, since the market participants who revised their deposit conditions included a range of major banks, the decrease in interest rates exceeded June's cuts, although the potential for a reduction in returns in the related segments of the financial market resulting from the actual and expected decisions on monetary policy easing was largely exhausted by early August (Chart 14). Interest rates on short- and long-term deposits declined by 0.5 and 0.4 pp, respectively (vs 0.1 and 0.2 pp in June).²

In August, banks were reviewing the parameters of their deposit products much less extensively, and a number of market participants even announced their new seasonal deposits, which is expected to contain the decline in average market deposit rates in the short run.

The decrease in deposit rates was also the predominant trend in the foreign currency segment of the market. Average market interest rates on short- and long-term US dollar-denominated deposits again hit their new record lows in July, which was largely explained by the fact that the cost of dollar-denominated assets remains low in the global market, expectedly discouraging Russian banks to increase their foreign currency assets and liabilities.

Deposit operations. Although the decline in deposit rates persisted and households continued to demonstrate elevated demand for cash, saving activity in the retail segment remained stable in July. As of the end of the month, the annual growth of the retail deposit

portfolio totalled 7.3%³ against 7.2% in June (Chart 15).

Moreover, retail customers continued to give preference to ruble-denominated deposits, with their annual rise speeding up to 11.3% as of the end of July, compared to 10.9% in the previous month. As before, short-term transactions and demand deposits remained the major drivers of the faster growth of ruble-denominated deposits.

Activity in the segment of current accounts has noticeably increased after the launch of the anti-coronavirus restrictions. This might be explained not only by the fact that households have been using their savings to cover their everyday needs, but also by the existing trend for the convergence of interest rates on deposits with various maturities. This trend enhances the attractiveness of highly liquid savings and, particularly, popular savings accounts and their analogues ensuring higher returns for borrowers compared to conventional demand deposits, while making their funds readily available on a continuous basis. Furthermore, the rise in demand deposits was partially driven by the consistent growth of balances in escrow accounts, as the mechanism of escrow accounts for financing housing construction is becoming increasingly widespread.

In contrast to ruble-denominated deposits, households demonstrated lower demand for foreign currency deposits as a saving instrument, with their decline accelerating in July from 6.7% to 7.2% in annualised terms. In addition, amid the reduction in interest rates and the persistent uncertainty over exchange rate expectations, short-term deposits (excluding current accounts) decreased most notably. Nonetheless, the portion of foreign currency deposits in the retail portfolio expanded by 0.7 pp over the month, to reach 20.5%, due to the weakening of the ruble.

¹ Refer to *Banking Sector Liquidity and Financial Markets*, No. 7 (53), July 2020.

² Short-term deposits are deposits with any maturities of up to one year, excluding demand deposits; long-term deposits are deposits with any maturities of over one year.

³ Hereinafter, increases in banks' balance sheet indicators are calculated based on the reporting data of operating credit institutions recorded in the State Register as of the relevant reporting date. Increases in foreign currency claims and liabilities are calculated in US dollar terms. Where increases in the indicators comprising foreign currency and ruble components are calculated herein, the growth of the foreign currency component is converted into rubles using the period average exchange rate.

Credit rates. The trend for a decrease in interest rates in the corporate segment of the credit market that had emerged in May also remained in June. This was associated with the continuing expansion of the lending support programmes and the easing of monetary policy. Specifically, the interest rate on short-term loans declined by 0.4 pp, to 6.9%, and on long-term loans – by 1.1 pp, to 7.1% (Chart 14). As compared to May, the corporate segment demonstrated a faster and more marked decrease in interest rates on loans with maturities of over 1 year, which was driven not only by the reduction in interest rates for lower-risk large borrowers, but also by the decrease in interest rates on loans for small and medium-sized enterprises (SMEs). In particular, the interest rate on SME loans dropped by 2.4 pp in June, to 7.0%, thus reaching the level not exceeding the average market interest rate on long-term corporate loans, for the first time over the entire history of the credit market. This trend in interest rates for SMEs was driven by the implementation of the preferential 2.0% lending programme launched to support businesses amid the coronavirus pandemic.

Interest rates in the retail segment of the credit market continued to go down in July. According to preliminary data, the average interest rate on loans with maturities of up to 1 year decreased by 0.3 pp, and on loans with maturities of over 1 year – by 0.5 pp. The faster reduction in interest rates in the long-term segment was explained by the decline in the mortgage rate which hit its new record low. Specifically, the average market interest rate on ruble-denominated mortgage loans dropped by 0.22 pp, to 7.28%, as a result of the implementation of the 6.5% programme for subsidising interest rates on mortgage loans.

In the short run, the preferential programmes to support both corporate and retail lending will continue to push interest rates downwards, thus contributing to the easing of lending conditions expected by banks in 2020 Q3–Q4 (Chart 18). Concurrently, credit risks that have risen due to the coronavirus pandemic will continue to significantly affect volatility of loan rates.

Corporate lending. As before, July's trends in corporate lending were driven by the progress

of the government's support programmes and decreasing interest rates amid the easing of monetary policy. As of the end of the month, the annual growth of the portfolio of loans to non-financial organisations sped up by 1.5 pp, to reach 6.0% (Chart 16). Among other things, this was coupled with a rise in overdue debt, with its percentage in the portfolio increasing by 0.5 pp, to 8.2%. However, the latter was explained by the fact that an individual bank identified non-performing loans as a result of its debt collection efforts and, therefore, does not imply any system-level deterioration of the loan portfolio quality (Chart 16). Furthermore, the effective loan restructuring programmes continue to contain an increase in overdue debt. In these conditions, the annual growth of the performing part of the corporate loan portfolio accelerated by 1.1 pp as of the end of July.

The sustainable rise in lending to non-financial organisations in July was mostly supported by long-term transactions. Specifically, the annual growth of ruble-denominated loans with maturities of over 1 year reached 7.1% against 5.1% the month earlier. The expansion of the corporate loan portfolio was also driven by transactions in foreign currency. The annual growth of foreign currency lending was positive for the first time since early 2016.

In the short run, corporate lending may be expected to demonstrate sustainable growth, as economic activity revives and demand for borrowing goes up, which is expected by banks according to the study of bank lending conditions in 2020 Q2 (Chart 18).

Retail lending. Activity in retail lending trended up in July: the loan portfolio expanded by 1.7% over the month against 1.0% in June (Chart 16). The mortgage segment remained the key driver of this rise, including owing to the effective preferential mortgage lending programmes launched by the government (Chart 17). The amount of ruble-denominated mortgage loans disbursed in July reached its record high of 362 billion rubles. Thus, as of the end of the month, the annual growth of the portfolio of mortgage loans⁴ sped up by 2 pp, to

⁴ *Housing mortgage loans, net of claims on such loans acquired by banks.*

reach 15.7%. Moreover, the mortgage segment of the credit market still has a potential for further growth, owing to the implementation of the measures aimed at increasing the availability of 6.5% preferential mortgage loans and involving a reduction in the minimum down payment and an increase in the limit under this programme.

Higher-risk retail lending segments were recovering for the second consecutive month, supported by the decrease in loan rates. In particular, outstanding unsecured consumer loans expanded by more than 90 billion rubles, and outstanding car loans – by over 20 billion rubles.

Banks prefer to grant loans primarily to reliable borrowers, which is evidenced by higher activity in the retail lending market and a gradual reduction in interest rates amid the tightening of non-price lending conditions (the requirements for borrowers' financial standing) as of the end of 2020 Q2. Coupled with the practice of loan repayment holidays, this limits the decline in the quality of the retail loan portfolio. Thus, as of the end of July, overdue debt in the retail loan portfolio rose by 0.1 pp, to 4.8% (Chart 16).

In the coming months, as the situation in the non-financial sector returns to normal, consumer lending may be expected to continue its recovery. Among other factors, this will be supported by the Bank of Russia's measures reducing risk-based buffers for unsecured consumer loans granted beginning on 1 September 2020 and cancelling buffers for loans issued through 31 August 2019, which will enable banks to release capital needed to build up lending.

Money supply. In July, the growth of the banking system's claims on the economy⁵ remained almost unchanged, as compared to the previous month. Contrastingly, companies'

debt expanded by 7.7% in annualised terms, which is its highest level since early 2018. This rise was mostly driven by an increase in ruble-denominated transactions with both non-financial organisations and financial institutions. In addition, the retail lending segment also showed first positive shifts: after the three-month decline induced by the pandemic, the annual growth of claims on retail borrowers started to speed up again, reaching 12.4% as of the beginning of August.

Since the amount of budget spending remained significant in July,⁶ the positive contribution of the banking system's net claims on the general government to the growth of broad money continued to increase. Combined with the sustainable rise in claims on the economy and the increase in the value of the Bank of Russia's gold and foreign currency reserves resulting from the rise in world gold prices, this pushed the annual growth rates of the M2X and M2 monetary aggregates upwards to their multi-year highs of 11.1% and 15.5%, respectively (Chart 19).

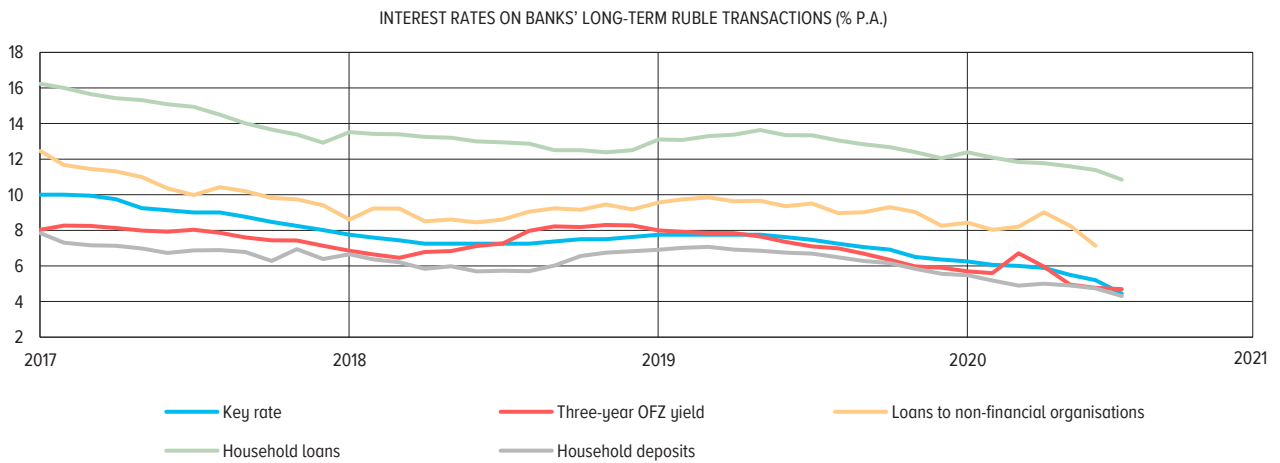
Moreover, ruble-denominated deposits of the non-financial sector remained the key component of broad money. However, taken separately, the contribution of households' and businesses' ruble deposits to the growth of the M2X monetary aggregate turned out to be lower than that of cash in circulation outside the banking system, for the first time in a long period of time. As of the end of July, the annual rise in the M0 aggregate reached almost 28%, which was primarily associated with lower cash inflows to banks as a result of the collection of retailers' earnings. As economic activity rebounds, the impact of cash on money supply will weaken, gradually returning to its pre-pandemic level.

⁵ *Banking sector claims on the economy mean all claims of the banking system on non-financial and financial organisations and households in Russian rubles, foreign currency, and precious metals, which include loans extended (including overdue loans), overdue interest on loans, credit institutions' investment in debt and equity securities and promissory notes, as well as other forms of participation in non-financial and financial organisations' equity, and other receivables under settlement operations with non-financial and financial organisations and households.*

⁶ *Refer to Banking Sector Liquidity and Financial Markets, No. 7 (53), July 2020.*

LOAN AND DEPOSIT RATES CONTINUE TO GO DOWN AS A RESULT OF THE ACTUAL EASING OF MONETARY POLICY

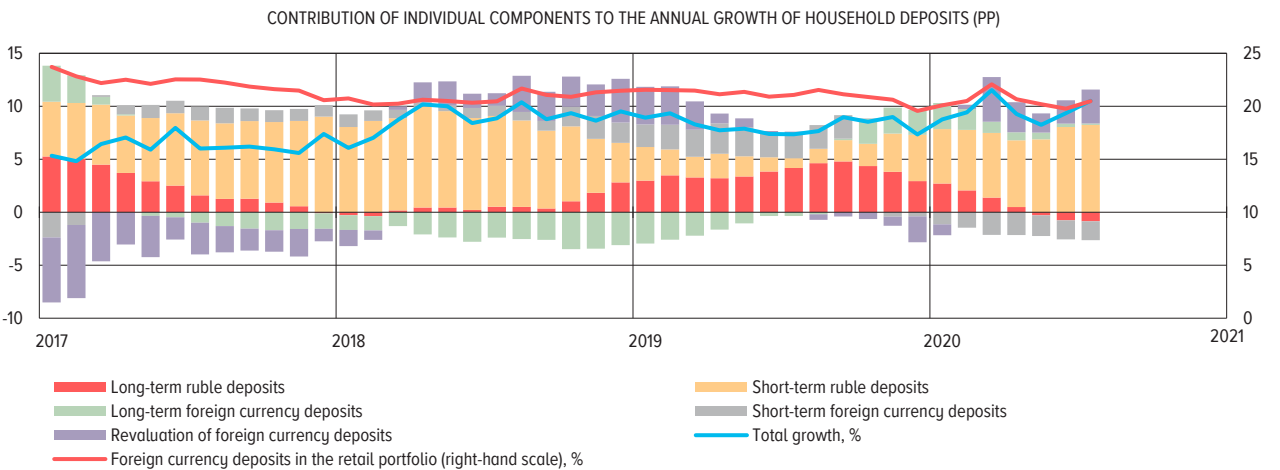
Chart 14



Source: Bank of Russia.

SHORT-TERM DEPOSITS REMAIN THE MAIN DRIVER OF THE RETAIL DEPOSIT MARKET

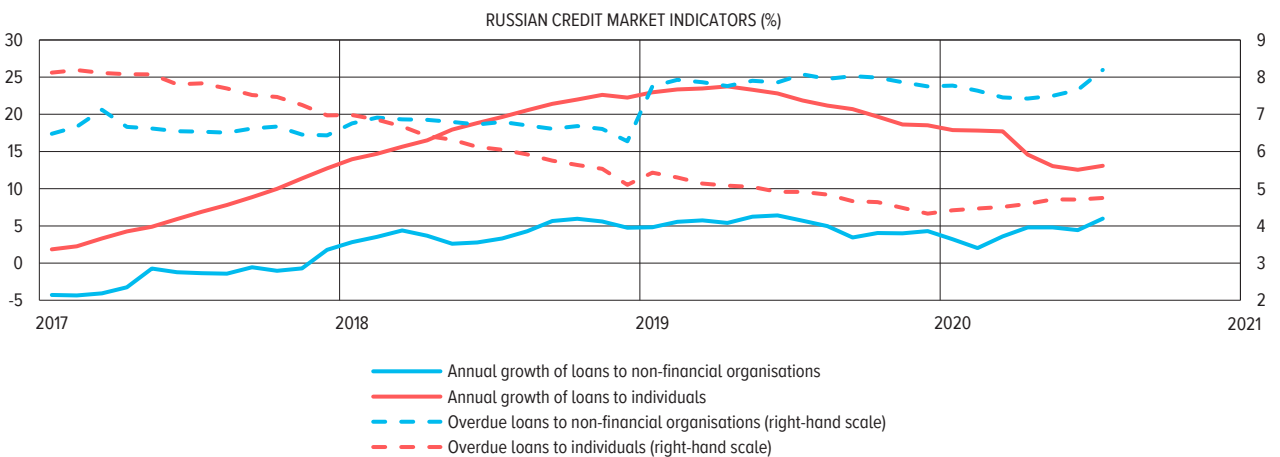
Chart 15



Source: Bank of Russia calculations.

CORPORATE LENDING SPED UP IN JULY

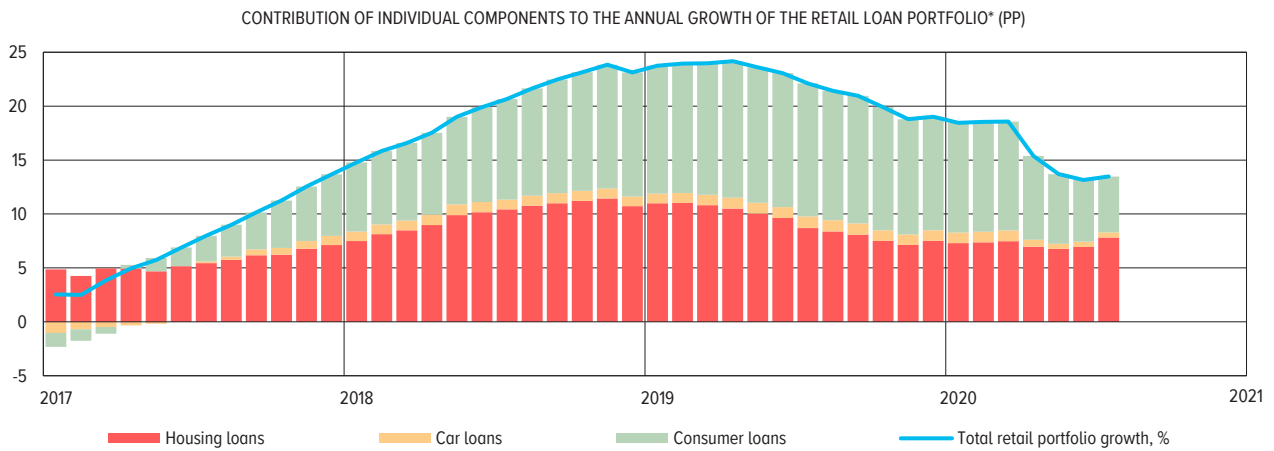
Chart 16



Source: Bank of Russia calculations.

CAR LENDING AND UNSECURED CONSUMER LENDING CONTINUED TO REBOUND IN JULY

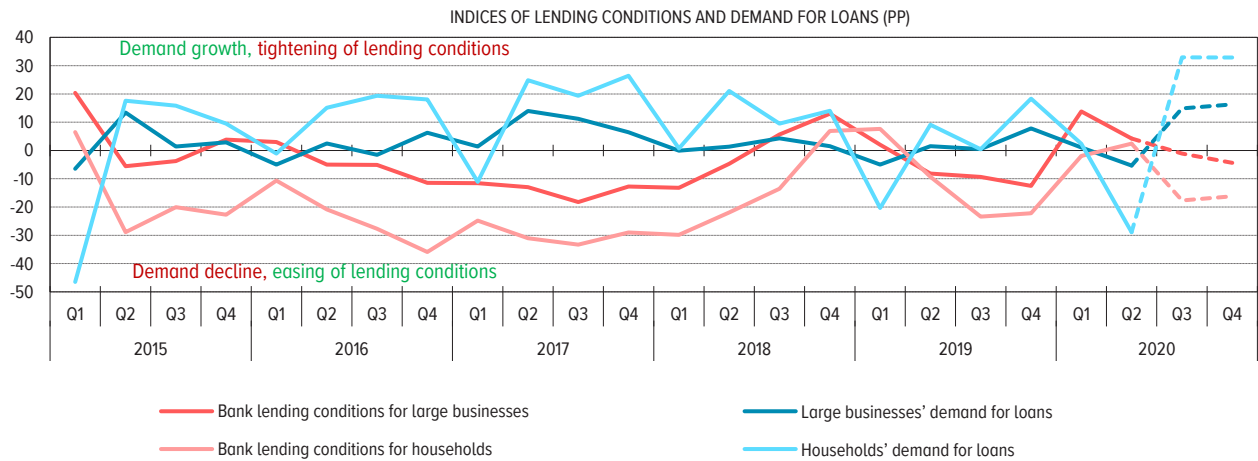
Chart 17



* For loans grouped into homogeneous loan portfolios.
Source: Bank of Russia calculations.

IN 2020 Q2 AMID DECLINING LOAN RATES, BANKS CONTINUED TO TOUGHEN NON-PRICE LENDING CONDITIONS FOR ALL MAIN GROUPS OF BORROWERS

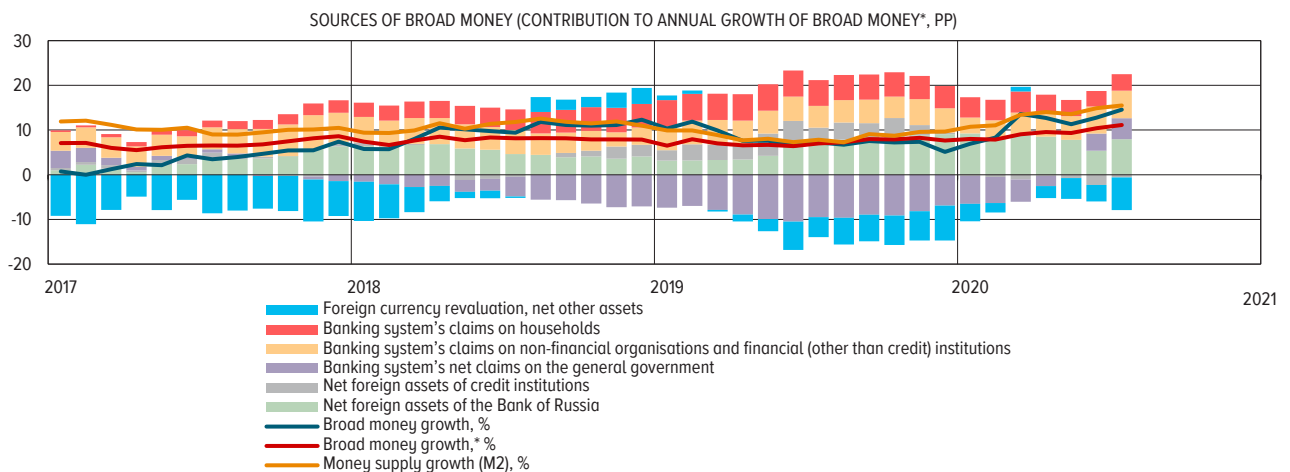
Chart 18



* The dotted lines signify respondent banks' expectations regarding changes in lending conditions and demand for loans in 2020 Q2.
Source: Bank of Russia.

BUDGET OPERATIONS REMAINED THE KEY DRIVER ACCELERATING THE GROWTH OF BROAD MONEY IN JULY

Chart 19



* Adjusted for foreign currency revaluation.
Source: Bank of Russia.

CREDIT AND DEPOSIT MARKET INDICATORS

Table 5

		April 2020	May 2020	June 2020	July 2020
Interest rates on banks' long-term ruble transactions					
– household deposits	% p.a.	5.0	4.9	4.7	4.3
– household loans	% p.a.	11.8	11.6	11.4	10.9
– corporate loans	% p.a.	9.0	8.3	7.1	-
Household deposits	% YoY, AFCR	6.4	6.4	7.2	7.3
– in rubles	% YoY	9.9	9.8	10.9	11.3
– in foreign currency	% YoY	-6.2	-5.9	-6.7	-7.2
– share of foreign currency	%	20.7	20.2	19.8	20.5
Loans to non-financial organisations	% YoY, AFCR	4.8	4.8	4.4	6.0
– short-term (up to 1 year)	% YoY, AFCR	12.4	13.9	15.0	11.3
– long-term (more than 1 year)	% YoY, AFCR	3.2	3.1	2.1	4.1
– overdue loans	%	7.4	7.5	7.7	8.2
Household loans	% YoY, AFCR	14.6	13.0	12.6	13.1
– housing mortgage loans	% YoY, AFCR	14.1	13.6	13.7	15.7
– unsecured consumer loans	% YoY	15.3	12.7	11.2	10.1
– overdue loans	%	4.6	4.7	4.7	4.8
Banking system's claims on the economy	% YoY, AFCR	8.6	8.2	8.8	9.0
– on businesses	% YoY, AFCR	6.7	6.7	7.6	7.7
– on households	% YoY, AFCR	14.0	12.6	12.0	12.4
Money supply (M2 monetary aggregate)	% YoY	14.0	13.6	14.9	15.5
Broad money	% YoY, AFCR	9.6	9.3	10.4	11.1

Note: YoY – year-over-year; AFCR – adjusted for foreign currency revaluation. The Marshall-Edgeworth decomposition is used to make the adjustment for foreign currency revaluation.
Source: Bank of Russia calculations.

Data cut-off dates:

- 'Banking sector liquidity and money market' section – 08.09.2019 (The reserve requirements are an important part of the Bank of Russia's instruments for managing banking sector liquidity and money market rates. Therefore, the operational procedure of the Bank of Russia's monetary policy should be analysed for efficiency with account of required reserves averaging periods. In August–September 2020, this period is from 05.08.2020 to 08.09.2020);
- 'Foreign exchange and stock markets' section – 31.08.2020;
- 'Credit and deposit market' section – 01.08.2020.

A soft copy of the [information and analytical commentary](#) is available on the Bank of Russia website.

Please send your comments and suggestions to svc_analysis@cbr.ru.

This commentary was prepared by the Monetary Policy Department.

Cover photo: A. Nikitin, Bank of Russia

12 Neglinnaya Street, 107016 Moscow

Bank of Russia website: www.cbr.ru