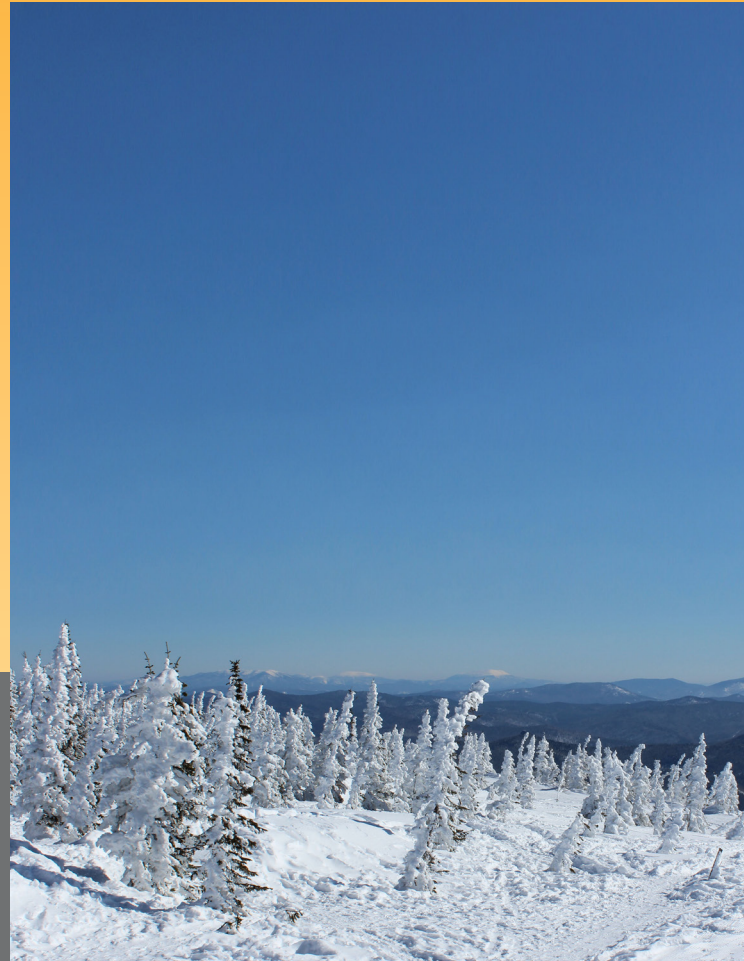




Bank of Russia



BANKING SECTOR LIQUIDITY AND FINANCIAL MARKETS

No. 11 (57) • November 2020

Information and analytical commentary

10 December 2020

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

- In November, the surplus of structural liquidity shrank due to the outflow of funds resulting from OFZ offerings and tax payments. The forecast of the structural liquidity surplus for the end of 2020 remains at the level of 1.0–1.4 trillion rubles, with account of a rise in budget expenditures in December.
- The spread between interbank lending (IBL) rates and the Bank of Russia key rate expanded as a result of lower demand for rubles amid a reduction in the liquidity outflow.
- The interest rate spread in the FX swap and IBL segments contracted as the supply of foreign currency expanded and major banks providing services to exporters lowered the demand for it in the money market.
- November became a positive month for financial markets. Markets expanded in the majority of advanced and emerging market economies, including Russia. This upward trend was driven by the end of the US election and news about highly efficient anti-coronavirus vaccines and their possible usage in the near future.
- In October, households' saving activity decreased, including due to reduced real returns on deposits, as well as the rising demand for real estate resulting in larger balances in escrow accounts.
- Average interest rates on long-term corporate and retail loans hit new record lows in September. Interest rates on household loans with over one-year maturities continued to lower in October.
- Credit activity in October was steadily growing in both the corporate and retail segments of the credit market.

Banking sector liquidity and money market

Ruble liquidity. On average, the structural liquidity surplus in the November required reserve averaging period shrank by **0.5 trillion rubles** against the October averaging period, to equal **0.5 trillion rubles**. Its amount as of early November decreased by **0.4 trillion rubles** compared to the beginning of the previous month, to total **0.3 trillion rubles** (Table 2).

Operations in the budget system's accounts were the key factor of the liquidity outflow in November, just as the month before. Russia's Ministry of Finance continued to expand its offerings of federal government bonds (OFZ) in the domestic market. However, after the Ministry reached its annual borrowing target, it significantly decreased its borrowing activity. Companies' tax payments also contributed to the outflow of liquidity. Budget revenues

contracted in November after their rise in October, while remaining at the 2019 level. The growth of personal income tax payments and earnings from social contributions and profit tax slowed down (Chart 2).

The inflow of funds as budget expenditures and Federal Treasury (FT) operations with temporarily available budgetary funds did not fully offset the outflow of liquidity from the banking sector through the fiscal channel. Budget expenditures continued to increase in November, compared to the previous year. However, the FT increased its lending to the banking sector only slightly, specifically by less than 0.2 trillion rubles. As a result, balances in the federal budget accounts with the Bank of Russia rose (Chart 7).

For the first time since January, the outflow of liquidity caused by the increased amount of cash in circulation reversed to a slight inflow as cash returned to banks. Owing to the accumulated

cash holdings, households and businesses more calmly respond to the autumn rise in coronavirus cases. Furthermore, the demand for cash is expected to gradually decrease to its pre-pandemic levels as economic activity continues to return to normal, yet this process may take a long time.

In November, the Bank of Russia increased the maximum amount of funding provided at its one-month repo auction from 1.0 to 1.5 trillion rubles, in order to help credit institutions offset the currently uneven distribution of liquidity. As a result, banks raised 1.2 trillion rubles through these operations. In December, the Bank of Russia did not change the maximum amount of funding provided for one month. However, banks' demand for these operations lowered to 0.8 trillion rubles. Banks' demand for refinancing from the Bank of Russia is expected to go down as they receive funds to finance budget expenditures.

Amid the contracting surplus of the banking sector liquidity in November, banks reduced their investment in Bank of Russia coupon bonds (coupon OBRs) by 0.1 trillion rubles, to 0.6 trillion rubles. In December, the Bank of Russia decided not to hold an auction for the placement of the 40th coupon OBR issue, in order to ensure greater flexibility in absorbing liquidity through its one-week deposit auctions. The Bank of Russia will determine the further schedule and amount for the placement of the 40th coupon OBR issue in January 2021, depending on the situation with liquidity.

Money market. The spread between short-term IBL¹ rates and the Bank of Russia key rate equalled -21 bp (vs -7 bp in the October averaging period; since the beginning of 2020: -16 bp) (Chart 3). The spread volatility rose to 16 bp (vs 13 bp in the October averaging period; since the beginning of 2020: 18 bp). As the Russian Ministry of Finance reduced the amount of funds raised at OFZ auctions, this slowed down the outflow of liquidity from the banking sector. As a result, the demand for rubles in the overnight IBL segment decreased, including on the part of individual market participants who had earlier

demonstrated the demand for OFZ bonds. This put downward pressure on money market rates. As banks adjusted to the changed environment, the spread between short-term IBL rates and the Bank of Russia key rate in the first half of the averaging period moved closer to the levels corresponding to the annual averages.

Foreign currency liquidity. The interest rate spread in the FX swap and IBL segments contracted, averaging -18 bp (vs -49 bp in the October averaging period; since the beginning of 2020: -18 bp) (Chart 4). The spread narrowed as the supply of foreign currency expanded and major banks providing services to exporters lowered the demand for it in the money market. Concurrently, these banks recorded an increase in clients' liabilities. In addition, non-residents maintain their long ruble positions offering rubles in the FX swap segment and borrowing foreign currency, which may put upward pressure on the cost of foreign currency liquidity.

The **forecast of the structural liquidity surplus for the end of 2020** remains at the level of 1.0–1.4 trillion rubles. As before, this forecast implies that Russia's Ministry of Finance will fully comply with its schedule of budget expenditures. If the budget expenditures planned for 2020 are partially carried over to 2021, the Federal Treasury may increase the amount of funds offered for depositing with banks. This implies that banks' debt under FT operations will grow compared to the previous year. In terms of seasonal distribution, budget expenditures are shifted to the last days of the year; therefore, the FT usually reduces the maturities of its operations at the beginning of December. Nonetheless, the financing of expenditures and the reduction in FT funds deposited with banks are expected to take place simultaneously, which will largely smooth out the effect of budget operations on liquidity.

The Bank of Russia carries out daily analysis of budget expenditures and takes this information into account forecasting the banking sector liquidity. Therefore, if any temporary gaps occur due to an earlier decrease in funds placed by the FT, the Bank of Russia will promptly adjust the limits on its liquidity management operations. This will enable the Bank of Russia to balance the situation with liquidity at any point of time

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

and achieve its operational objective, that is, keep overnight money market rates close to the key rate.

The liquidity forecast for 2020 also maintains the assumption that a rise in the demand for cash in December may turn out to be lower than in previous years. Generally, an increase in the issue amount during this period is primarily associated with the fact that banks build up their cash balances to replenish their cash offices and ATMs during the New Year holidays. This year, the cash holdings formed by households over the year may lower their needs in withdrawing additional cash during this period. If banks replenish their cash offices and ATMs in the same amounts as previously, the outflow of liquidity may be above and the surplus may accordingly decrease below the

forecast. However, this factor will be temporary, and these funds will return to banks as early as the first days of January.

As another assumption, the forecast also implies a uniform averaging of required reserves by banks. This means that the balance of funds in banks' correspondent accounts with the Bank of Russia is expected to be close to 2.6 trillion rubles as of the end of the year. Further on, the liquidity surplus may go down. Specifically, the surplus may contract to 0.6–1.3 trillion rubles by the end of 2021.

Key rate expectations. As in October, analysts' and market participants' expectations remained unchanged in November. They presume that the key rate will be kept at 4.25% until the end of the year (Table 1).

MARKET PARTICIPANTS DO NOT EXPECT THE KEY RATE TO BE CUT THIS YEAR

Table 1

1. Expectations based on market indicators,* interest rate (instrument)	December 2020
– MosPrime 3M (FRA)	4.25 (4.25)
– RUONIA (ROISfix)	4.30 (4.27)
– RUONIA (futures)	4.37 (4.46)
2. Analysts' key rate expectations*	As of 31.12.2020
– Bloomberg survey	4.25 (4.25)
– Reuters survey	4.25 (4.25)

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

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

Table 2

	01.01.2017	01.01.2018	01.01.2019	01.01.2020	01.11.2020	01.12.2020
Structural liquidity deficit (+) / surplus (-)	736	-2,639	-3,016	-2,761	-680	-296
Bank of Russia's claims on credit institutions	1,258	10	21	18	633	1,287
Auction-based facilities	216	-	-	-	628	1,230
– repos and FX swaps	-	-	-	-	628	1,230
– secured loans	216	-	-	-	0	0
Fixed interest rate facilities	1,042	10	21	18	5	57
– repos and FX swaps	632	4	8	13	0	0
– secured loans	411	5	13	5	5	57
Credit institutions' claims on the Bank of Russia	785	2,729	3,293	2,983	1,931	2,199
Deposits	785	2,372	1,902	1,026	1,233	1,593
– auction-based	397	2,125	1,478	697	1,083	1,457
– fixed interest rate	388	247	424	330	150	136
BoR coupon bonds	0	357	1,391	1,956	699	606
Standing reverse facilities, other than standard monetary policy instruments of the Bank of Russia*	263	81	256	204	618	616

* 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 STRUCTURAL LIQUIDITY SURPLUS FORECAST FOR THE END OF 2020 REMAINS
AT THE LEVEL OF 1.0–1.4 TRILLION RUBLES
(TRILLIONS OF RUBLES)

Table 3

	2019 (actual)	January– November 2020	November 2020	2020 (forecast)	2021 (forecast)
1. Liquidity factors	0.5	-2.3	-0.2	[-1.8; -1.5]	[-0.2; 0.4]
– change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	0.2	-0.2	-0.2	[0.3; 0.4]	[0.0; 0.3]
– change in the amount of cash in circulation	-0.1	-2.1	0	[-2.1; -1.9]	[-0.1; 0.2]
– Bank of Russia interventions in the domestic FX market and monetary gold purchases**	0.4	0.1	0	0.1	0
– regulation of banks' required reserves with the Bank of Russia	0	-0.1	0	-0.1	-0.1
2. Change in free bank reserves (correspondent accounts)*** (demand)	0.7	0.2	0.2	[-0.1; 0.0]	[0.2; 0.3]
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	-0.3	-0.8	0.3	[-0.5; -0.1]	[-1.8; -1.1]
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	-0.1	1.7	0.7	1.3	-1.3
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	-2.8		-0.3	[-1.4; -1.0]	[-1.3; -0.6]

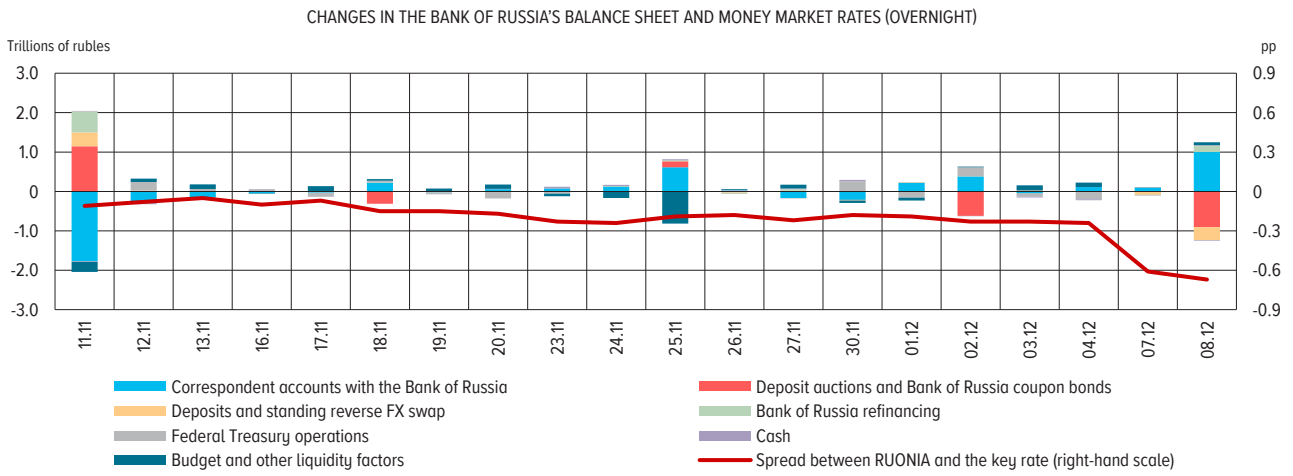
* Including fiscal rule-based operations to buy (sell) foreign currency in the domestic FX market, settlements on Bank of Russia USD/RUB FX swaps, and other operations.

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

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

BUDGET OPERATIONS CAUSED AN OUTFLOW OF LIQUIDITY FROM THE BANKING SECTOR IN NOVEMBER 2020

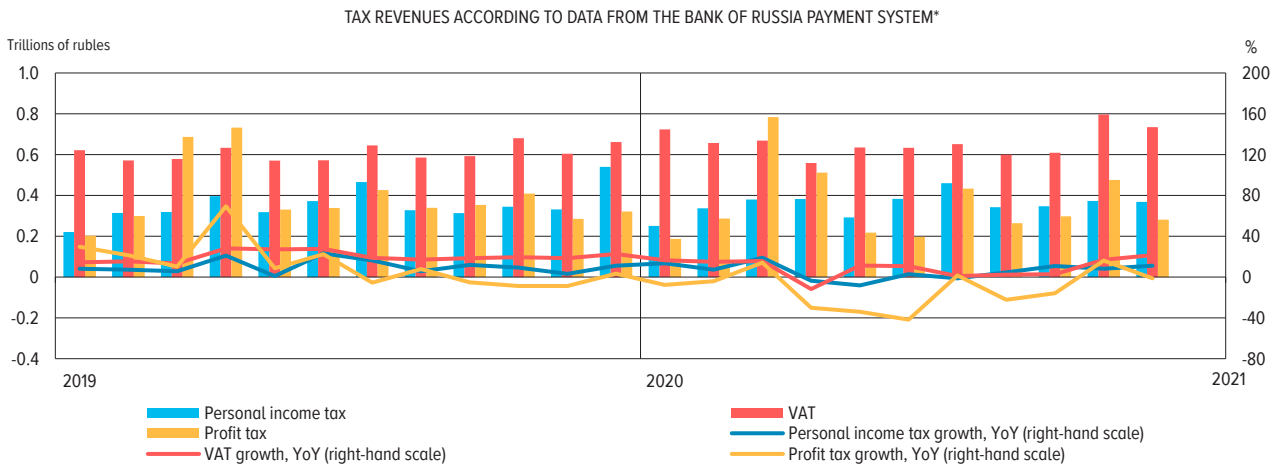
Chart 1



Source: Bank of Russia calculations.

THE GROWTH OF PERSONAL INCOME TAX PAYMENTS AND EARNINGS FROM SOCIAL CONTRIBUTIONS AND PROFIT TAX SLOWED DOWN IN NOVEMBER 2020

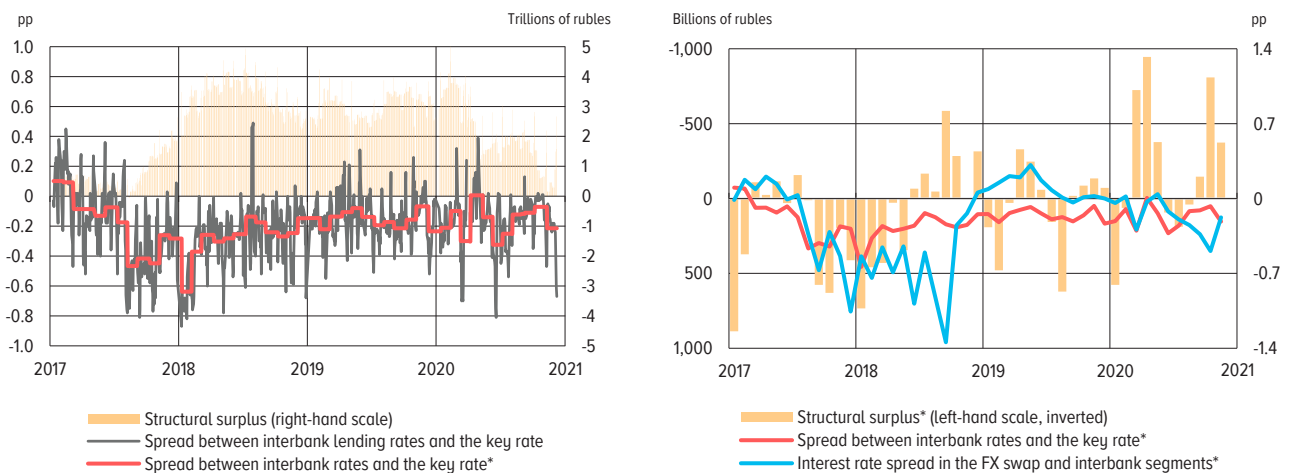
Chart 2



* Funds transfers from credit institutions' accounts to the budget system's accounts with budget classification codes corresponding to the above taxes.
Source: Bank of Russia calculations.

THE SPREAD BETWEEN IBL RATES AND THE BANK OF RUSSIA KEY RATE EXPANDED

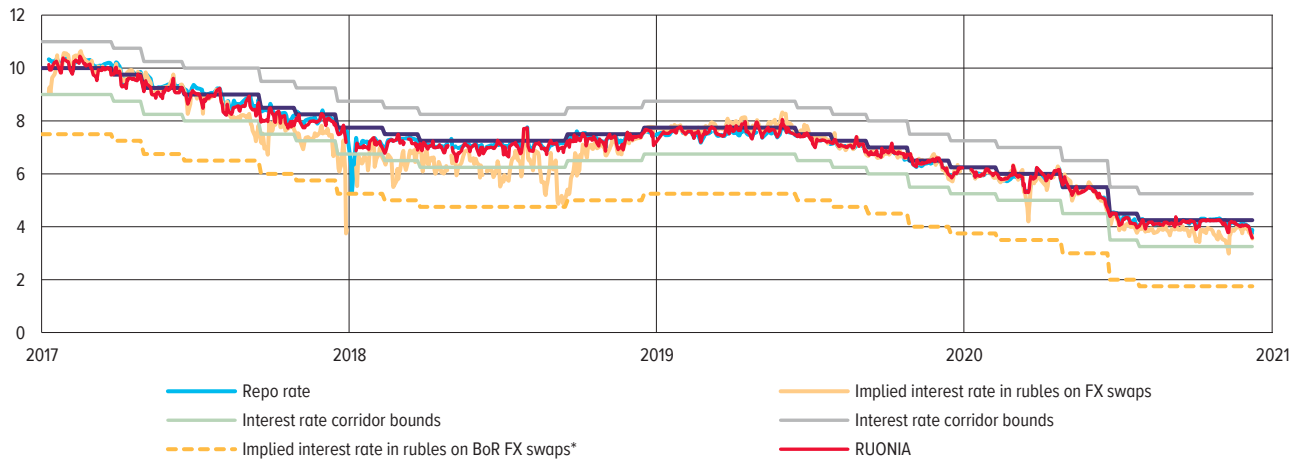
Chart 3



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

THE SPREAD IN THE FX SWAP AND IBL SEGMENTS SHRANK (% P.A.)

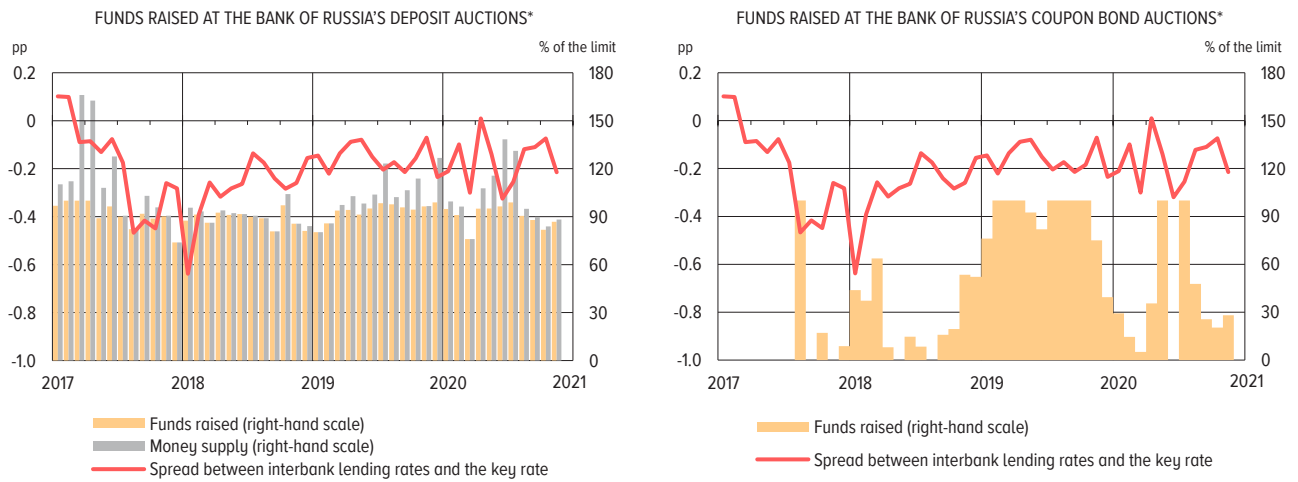
Chart 4



* 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 ONE-WEEK DEPOSIT AUCTIONS WAS SLIGHTLY BELOW THE ESTABLISHED LIMITS

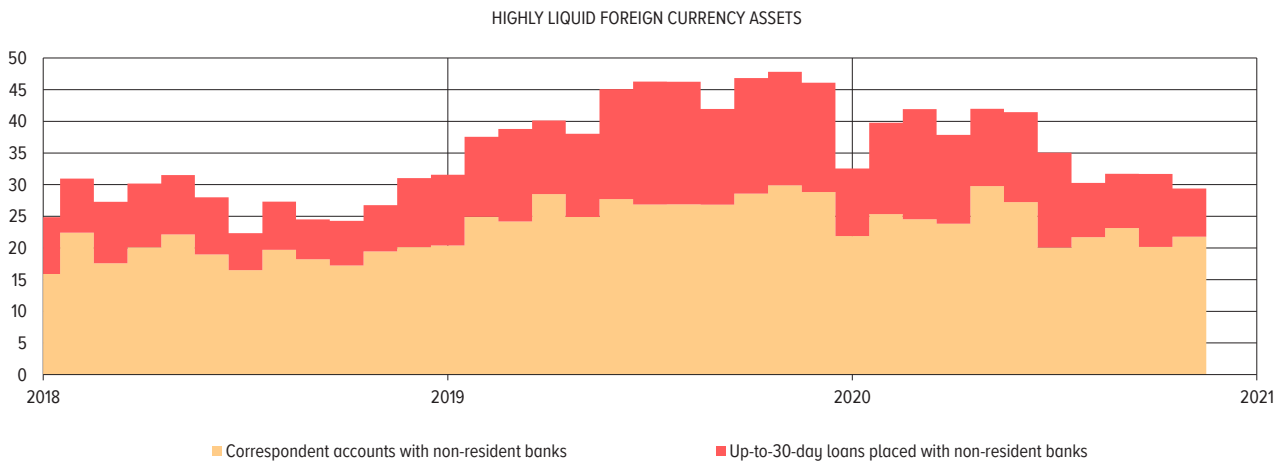
Chart 5



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

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

Chart 6

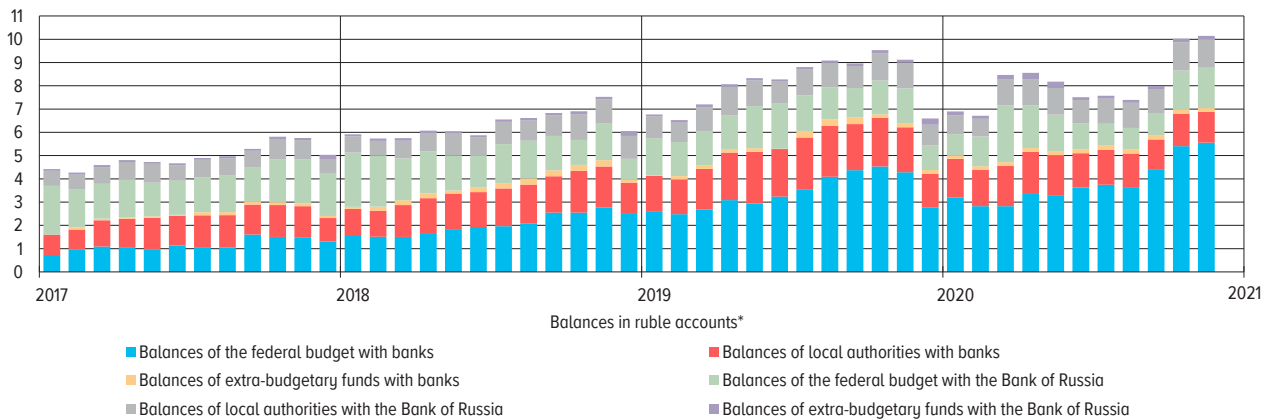


Source: Bank of Russia calculations.

THE GROWTH OF BALANCES IN THE FEDERAL BUDGET ACCOUNTS WITH THE BANK OF RUSSIA SLOWED DOWN IN NOVEMBER 2020 DUE TO A REDUCTION IN TAX REVENUES AND OFZ PLACEMENTS

Chart 7

(TRILLIONS OF RUBLES, AS OF THE PERIOD-END)

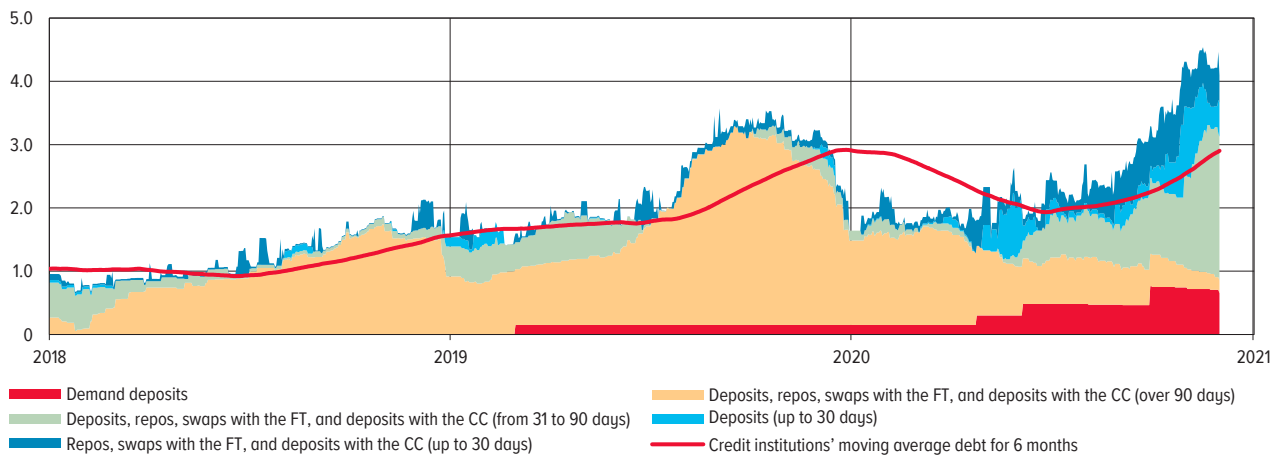


* According to banking reporting form 0409301 'Performance indicators of a credit institution'.
Source: Bank of Russia calculations.

CREDIT INSTITUTIONS' DEBT TO THE FT INCREASED BY 0.2 TRILLION RUBLES IN NOVEMBER 2020

Chart 8

(TRILLIONS OF RUBLES)

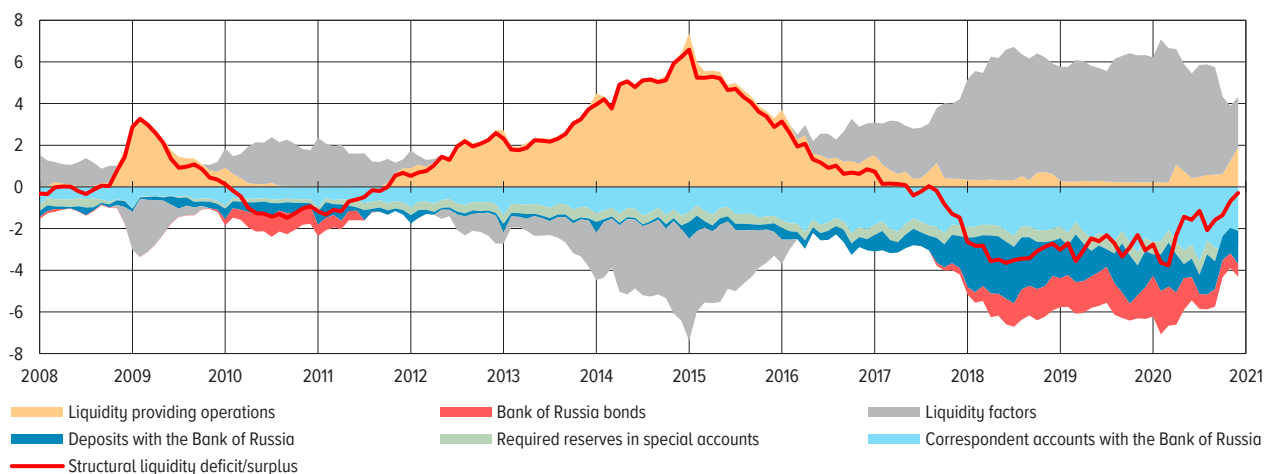


Sources: Federal Treasury, Bank of Russia calculations.

BANK OF RUSSIA'S BALANCE SHEET

Chart 9

(TRILLIONS OF RUBLES)



Source: Bank of Russia calculations.

Foreign exchange and stock markets

November became a positive month for financial markets. Markets expanded in the majority of advanced and emerging market economies (EMEs). This rise was driven by the end of the US election and news about highly efficient anti-coronavirus vaccines and their possible usage in the near future. The Russian market also recorded an upward trend, although investors believe that the rhetoric about sanctions against Russia is likely to become tougher due to Joe Biden's election as the next US president.

Exchange rate. As of the end of the month, the exchange rate of the ruble gained 3.9%, rising to 76.39 rubles per US dollar (Chart 10). In November, the ruble was strengthening at the highest pace recorded since May 2020, when the exchange rate was rising amid the overall risk-on sentiment inspired by the slower spread of the pandemic and a partial lifting of quarantine restrictions. Market sentiment was positive, which was also a major driver of this growth. Over this period, the JP Morgan EM Currency Index edged up by 3.8%, the oil price rose by 27%, and Russia's CDS spread narrowed by 25 basis points. The ruble exchange rate in November was almost completely driven by these three factors.

Country risk premium. As of the end of the month, Russia's 5Y CDS spread shrank by 25 bp, to 81 bp (Chart 11). This is its lowest level since the end of May 2020 and is 20 bp higher than in early 2020 when the emerging pandemic was not yet affecting markets. Other EMEs also recorded a decrease in CDS spreads. Moreover, in many countries, this reduction was even more significant than in Russia, partially because their

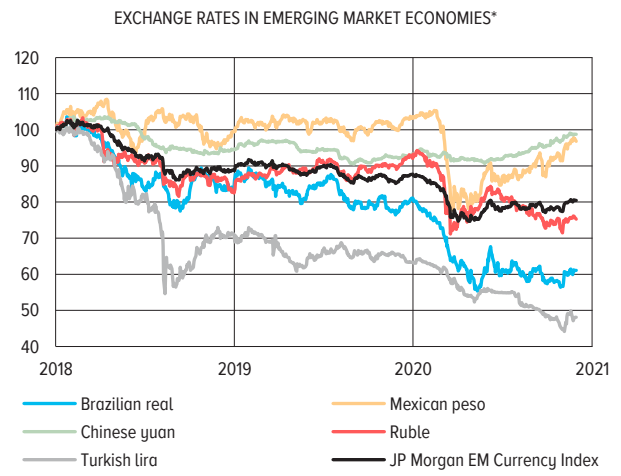
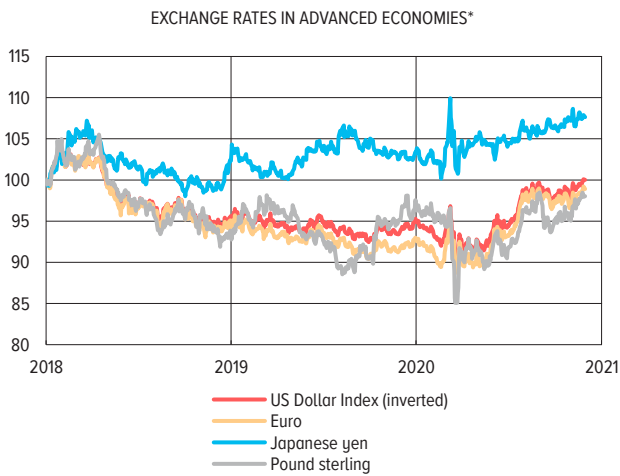
levels had been originally higher. As regards investment- and speculative-grade US corporate bonds being among the most popular indicators of risk appetite, their CDS spreads returned to February's pre-crisis levels in November, reaching 50 and 300 bp, respectively (-15 and -120 bp over the month).

Federal government bonds. Yields of OFZ bonds declined by 9–26 bp (Chart 12): OFZ 2Y – 4.56% (-9 bp), OFZ 5Y – 5.34 bp (-21 bp), and OFZ 10Y – 6.15 bp (-26 bp). The decrease in yields of long-term OFZ issues was more pronounced owing to a considerable inflow of non-residents' funds. Over the month, they increased their investment by 102.2 billion rubles (Chart 14). Before this, non-residents were as active in February 2020. Amid favourable external conditions, Russia's Ministry of Finance successfully placed two issues of Eurobonds amounting to 0.75 and 1.25 billion euros, with the maturities of 7 and 12 years, respectively. Additionally, the Ministry of Finance reached its 2020 OFZ borrowing target, placing OFZ bonds in the amount of 814.6 billion rubles at face value in November. As in October, floating-rate coupon government bonds (OFZ-PK) accounted for the largest portion of the offerings (88.6%), with systemically important credit institutions being the major buyers.

Stocks. Stock markets rose by more than 10% in the majority of economies (Chart 13). S&P 500 was up by 10.8%, and MSCI EM added 9.2%. The Russian market was among the leaders, with the MOEX Index and the RTS Index growing by 15.5% and 20.2%, respectively. The Russian indices rose more significantly, compared to other EMEs, on the back of the oil market rally and weaker dynamics in previous months.

THE RUBLE WAS STRENGTHENING AT THE HIGHEST PACE SINCE MAY 2020
(02.01.2018 = 100)

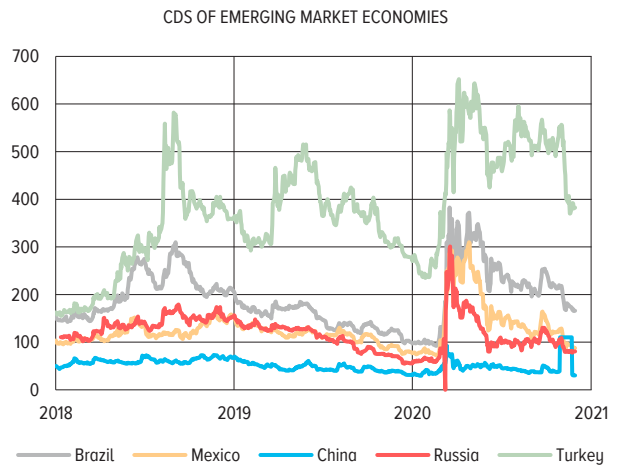
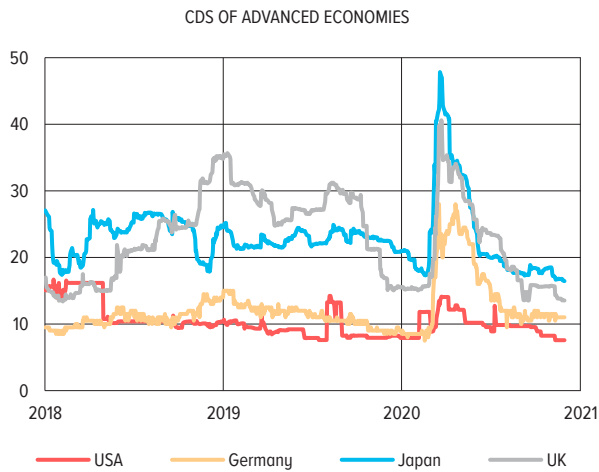
Chart 10



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

RUSSIA'S 5Y CDS SPREAD NARROWED TO ITS MAY 2020 LEVEL
(BP)

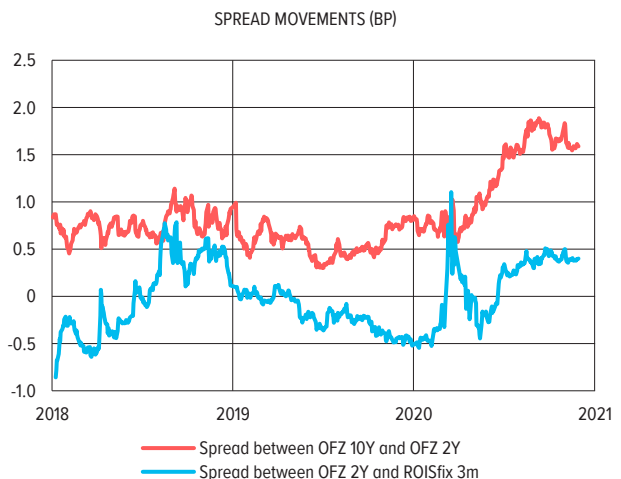
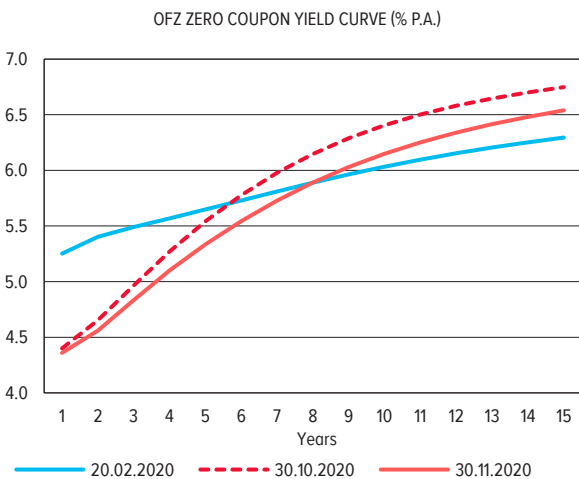
Chart 11



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

MEDIUM- AND LONG-TERM OFZ YIELDS DECREASED OWING TO NON-RESIDENTS' DEMAND

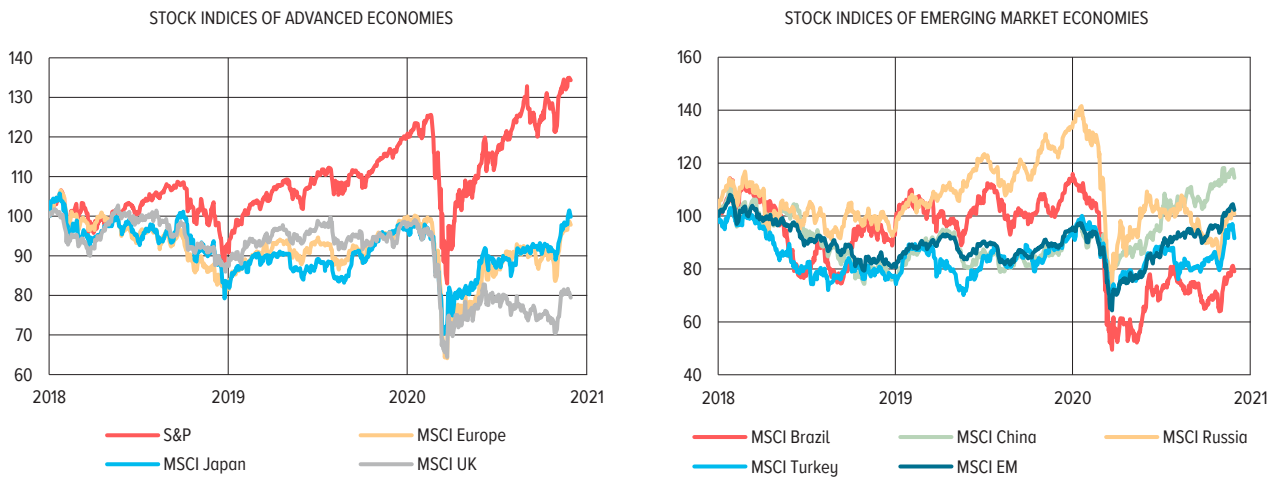
Chart 12



Source: PJSC Moscow Exchange.

THE RUSSIAN MARKET WAS AMONG LEADERS IN TERMS OF GROWTH IN EMES
(02.01.2018 = 100)

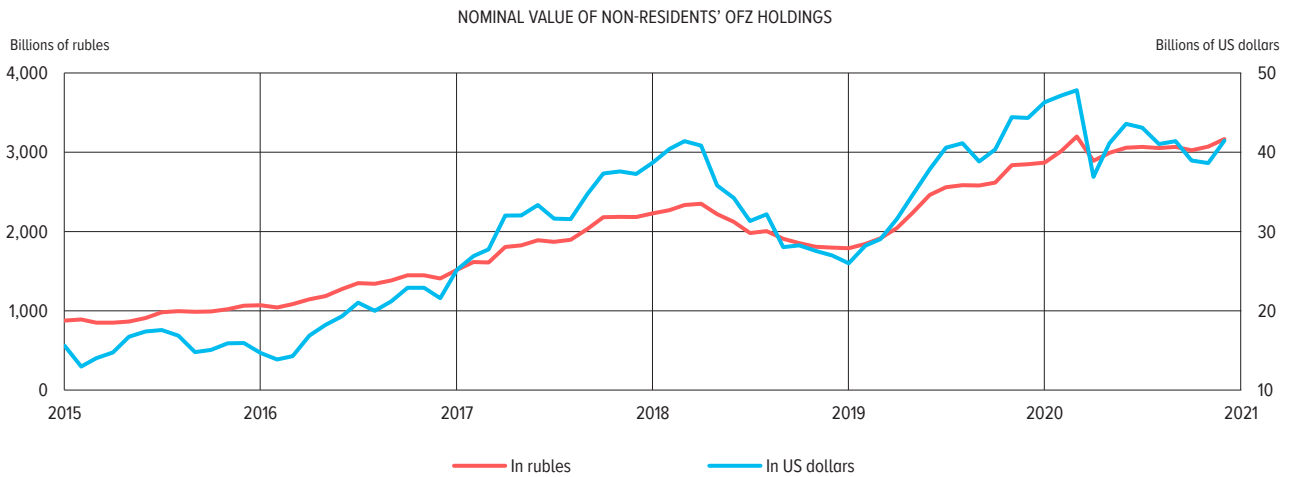
Chart 13



Sources: Bloomberg, Bank of Russia calculations.

FOREIGN INVESTORS CONTINUED OFZ PURCHASES

Chart 14



Source: Bank of Russia calculations.

MOST SEGMENTS OF THE FINANCIAL MARKET RECORDED A RISE IN PRICES

Table 4

Indicator		30.11.2020	1M	3M	6M	YTD	1Y
Russian financial market							
RUB/USD exchange rate		76.39	3.9	-3.1	-10.5	-23.2	-19.2
MOEX Index		3,108	15.5	4.8	13.0	2.0	6.1
RTS Index		1,282	20.2	1.9	2.8	-17.2	-10.9
Government bond yield		5.65	-19	-7	32	-56	-70
Corporate bond yield		6.20	-12	19	21	-53	-75
Regional bond yield		5.80	0	12	-4	-47	-106
CDS spread		81	-25	-20	-34	25	10
RVI		30	-11	-3	-5	8	11
Exchange rates (per US dollar, % change, '+' – appreciation, '-' – depreciation)							
AEs*	US Dollar Index	91.87	-2.3	-0.3	-6.1	-4.7	-6.6
	Euro	1.19	2.4	-0.1	7.1	6.4	8.3
	Japanese yen	104.31	0.3	1.5	3.1	4.1	5.0
	Pound sterling	1.33	2.9	-0.4	6.7	0.5	3.2
EMEs	JP Morgan EM Currency Index	56.36	3.8	1.6	2.6	-8.2	-5.5
	Ruble	76.39	3.9	-3.1	-10.5	-23.2	-19.2
	Brazilian real	5.36	7.7	3.0	0.6	-24.6	-21.4
	Mexican peso	20.18	5.0	8.4	9.2	-6.2	-3.5
	Chinese yuan	6.58	1.7	4.1	8.3	5.8	6.9
	Turkish lira	7.82	6.6	-6.1	-13.0	-24.0	-26.5
	South African rand	15.47	5.0	9.5	12.2	-9.5	-4.9
10-year bond yield (% p.a., change in bp, '+' – increase, '-' – decrease)							
AEs	USA	0.84	-3	14	18	-108	-93
	Germany	-0.57	6	-17	-17	-38	-21
	Japan	0.03	-1	-2	2	5	12
	UK	0.30	4	-1	7	-51	-37
EMEs	Russia	5.84	-32	-25	34	-53	-61
	Brazil	7.62	-2	71	65	94	88
	Mexico	5.78	-50	-28	-36	-111	-131
	China	3.27	9	25	54	13	9
	Turkey	11.57	-244	-193	12	-38	-59
	South Africa	8.97	-33	-29	21	-4	-24
5Y CDS spreads (% p.a., change in bp, '+' – increase, '-' – decrease)							
AEs	USA	8	-1	-2	-3	0	0
	Germany	11	1	-1	-8	2	2
	Japan	16	-2	-1	-8	-5	-6
	UK	14	-2	-3	-12	-2	-3
EMEs	Russia	81	-25	-20	-34	25	10
	Brazil	166	-52	-49	-110	66	41
	Mexico	88	-40	-30	-85	9	-4
	China	30	-80	-9	-23	-5	-9
	Turkey	382	-170	-141	-153	105	64
	South Africa	227	-50	-60	-103	64	40
Stock indices (points, % change, '+' – increase, '-' – decrease)							
AEs	S&P	3,622	10.8	3.5	18.5	12.1	14.8
	MSCI Europe	1,759	16.9	6.5	17.7	-1.4	2.1
	MSCI Japan	1,073	12.19	9.1	13.1	3.5	4.1
	MSCI UK	1,761	12.7	5.0	0.8	-18.4	-17.1
EMEs	MSCI EM	1,205	9.2	9.4	26.7	8.1	14.7
	MSCI Russia	610	20.8	0.7	-3.5	-24.4	-19.0
	MSCI Brazil	1,657	23.7	11.2	20.8	-30.2	-21.7
	MSCI Mexico	4,298	19.4	23.4	22.5	-9.7	-5.4
	MSCI China	106	2.7	5.1	27.9	23.3	30.8
	MSCI Turkey	1,479,165	15.3	15.3	10.1	-1.6	3.4
	MSCI South Africa	1,304	5.3	0.4	10.5	-4.9	-0.7

* Advanced economies.

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

Credit and deposit market

Deposit rates. In October, average market deposit rates stayed close to the previous month's level. Expectedly, this was mainly driven by a pause in monetary policy easing and banks' competition for stable retail funding amid households' rising interest in savings alternatives. The average interest rate on short-term deposits was 3.3% p.a. and that on long-term deposits – 4.1% p.a.¹ (Chart 15).

In November, banks adjusted their interest rates on existing deposit products upwards and launched attractive seasonal deposits on the eve of the New Year holidays. Therefore, the average interest rate on retail deposits may be expected to stay close to its current level until the end of the year.

The average market rates on short- and long-term foreign currency deposits edged up slightly in October, to exceed September's record lows by 6 and 5 bp, respectively.

Deposit operations. In October, households decreased their saving activity: the annual growth of retail deposits, excluding escrow accounts, lowered by 1.1 pp, to 3.4%² (Chart 16). The inflow of households' funds into deposits slowed down because retail investors increased the demand for alternative financial instruments amid lower real returns on deposits and partially used their savings to maintain consumption. Another drag on savings was the rising demand for real estate, which sped up the growth of balances in escrow accounts, among other things.

As regards the structure of the portfolio, ruble deposits continued to replace foreign currency-denominated ones. In October, the annual decrease in foreign currency deposits sped up

from 8.6% to 8.8%. As the uncertainty about the further spread of the coronavirus persisted and deposit rates were low, households continued to transfer their funds from short-term (up to three years) ruble deposits to current accounts. Activity in the segment of deposits for over three years stabilised, with the annual growth of such deposits equalling 9.7% by the end of October, as in the previous month.

As a result of this trend in the deposit market, the portion of foreign currency-denominated deposits (excluding escrow accounts) remained unchanged in October, totalling 21.9% (Chart 16).

Credit rates. The cost of borrowing in the corporate segment³ of the credit market changed diversely in September. The average interest rate on loans for up to one year edged up by 0.13 pp, to 6.15% p.a., driven by an increase in the portion of loans granted on market terms. Among other things, this growth was associated with the gradual termination of the preferential lending programmes launched in spring to support pandemic-hit industries. Conversely, the average interest rate on loans for more than one year decreased by 0.16 pp over the month, to hit its new record low of 6.81% p.a. (Chart 15). The cost of long-term lending declined because of lower interest rates on loans to large corporates, while the average interest rate in the higher-risk SME lending segment, to the contrary, adjusted upwards.

As regards the retail segment of the credit market, interest rates changed unevenly in October. The average rate on household loans for up to one year rose by 0.1 pp, and that on loans for over one year declined by 0.3 pp. The cost of long-term lending decreased due to both lower interest rates on car loans and unsecured consumer loans and the expanded portion of less expensive housing mortgage loans in market turnovers driven by record-high activity in this segment. Nonetheless, as the loan disbursements for purchasing finished housing continued to increase, the average mortgage rate stayed close to the level recorded in September.

¹ 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.

² 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.

³ Hereinafter, the corporate segment of the credit market implies lending to non-financial organisations.

Given that in October the Bank of Russia decided not to revise the key rate, changes in credit rates in the near future will largely depend on fluctuations of preferential lending amounts in market turnovers, as well as banks' risk appetite and borrowers' willingness to increase their debt burden amid the partial reintroduction of restrictions due to the worsening of the epidemiological situation since early autumn.

Corporate lending. Corporate lending expanded in October: the annual growth of the portfolio of loans to non-financial organisations accelerated from 6.3% to 6.6%, fully offsetting the slowdown observed since mid-2019. The credit quality of the portfolio generally remained stable, although differing across banks and borrower categories (Chart 17).

The major driver of the corporate lending growth in October was ruble-denominated loans, predominantly those for more than three years, including both individual transactions with large borrowers and preferential loans to systemically important companies. Owing to these transactions, the annual growth of ruble loans with maturities of over one year totalled 7.6% against 6.4% in the previous month. Long-term ruble borrowings thus remained the major contributor to the dynamics of non-financial organisations' overall loan portfolio.

Contrastingly, the rise in lending for up to one year slowed down to 9.1% against 9.6% in September, which may be partially explained by companies' lower need in borrowing than in Q2 to support business continuity as incoming financial flows⁴ predominantly returned to normal. In addition, the market of non-financial corporate bonds considerably expanded, which continued to complement the activity in corporate lending: by the beginning of November, the portfolio of such bonds almost reached 9 trillion rubles, increasing by 1.2 trillion rubles year-on-year, compared to 0.7 trillion rubles the year before.

In the short run, the growth of corporate lending may be limited not only by a considerable expansion of the bond market, but also by the unsteady recovery of domestic demand amid

the aggravation of the epidemiological situation and the tightening of related restrictions beginning from the second half of October.⁵

Retail lending. In October, retail lending maintained a steady upward trend. As a result, the annual growth of the retail loan portfolio sped up to 14.6% against 13.4% in September, thus returning to the level recorded before the introduction of restrictions in spring 2020. The portion of overdue loans in the retail portfolio remained close to its pre-pandemic level, partially because of the significant expansion of the loan portfolio (Chart 17).

As in previous months, the mortgage segment was the major driver of retail lending (Chart 18). As of the end of October, housing mortgage lending hit another record high (nearly 550 billion rubles), and the annual growth of the mortgage loan portfolio⁶ exceeded 22.0% for the first time since mid-2019, adding as many as 3.4 pp over the month. Furthermore, record-high activity was observed not only in the segment of housing under construction supported by the preferential 6.5% mortgage programme, but also in the segment of finished housing owing to record-low interest rates on loans granted on market terms. As of the beginning of November, finished housing again accounted for almost two-thirds of the disbursements, which is comparable with the pre-pandemic levels.

Unsecured consumer loans and car loans also notably increased in October, specifically by 1.5% and 2.3%, respectively, compared to 1.1% and 0.9% the month before. Among other things, this trend could be driven by the reviving demand for durable goods (cars, household appliances, and furniture), the output of which expanded in October.⁷

As the preferential mortgage programme in the new housing segment was extended until mid-2021 and because interest rates in this market segment are record low, mortgage

⁴ Refer to *Monitoring of Sectoral Financial Flows*, No. 26–29, 2020.

⁵ Refer to *Economy: Facts, Assessments and Comments*, No. 10 (58), October 2020.

⁶ *Housing mortgage loans, net of claims on such loans acquired by banks.*

⁷ Refer to *Economy: Facts, Assessments and Comments*, No. 10 (58), October 2020.

lending will probably remain the key driver of retail lending in the near future. As regards unsecured consumer loans and car loans, trends in these segments will largely depend on how strongly anti-pandemic restrictions will be dragging down the recovery of domestic demand.

Money supply. In October, the annual growth of the banking system's claims on the economy⁸ sped up by 0.5 pp, to 9.8%, primarily driven by an increase in claims on households. Amid record-high activity in the mortgage segment, the rise in the banking system's claims on households totalled 14.0% as of the end of October, up from 12.9% the month before. The annual growth of claims on organisations also sped up by 0.2 pp, to reach 8.2% as of the end of October, predominantly boosted by ruble lending to non-financial companies, while the annual increase in claims on financial institutions slightly slowed down in October.

As budget expenditures increased against the previous year,⁹ the banking system's net claims on the general government remained a driver of money supply growth in October. Coupled with a lower impact of net foreign assets on the annual growth of money supply and the quicker rise in the banking system's claims on the economy, the increase in the monetary aggregates as of the end of October remained almost unchanged as compared to the previous month. Specifically, the M2 aggregate gained 16.2% and M2X – 11.8% (Chart 20).

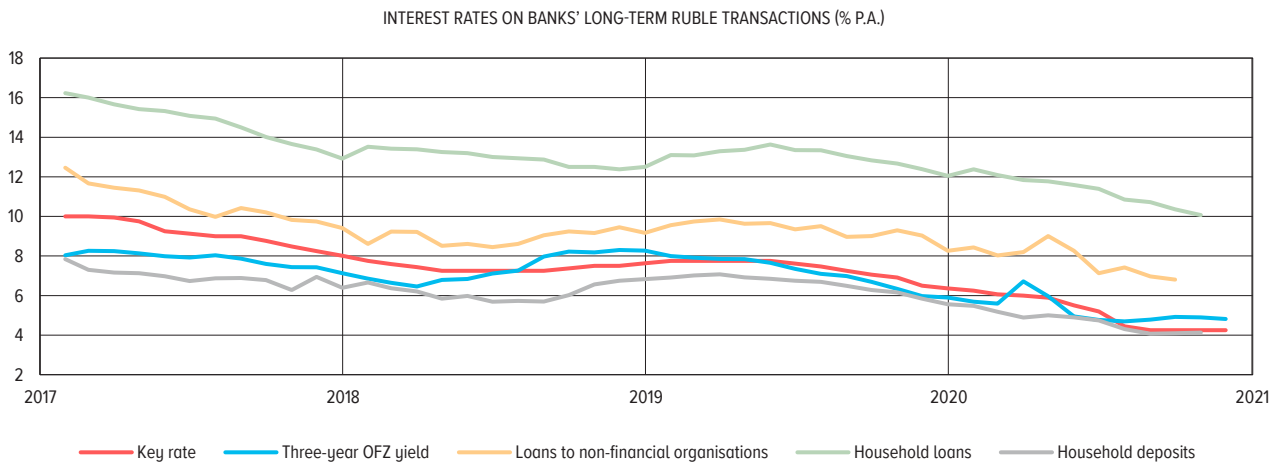
As before, non-financial companies' ruble-denominated deposits are the main component of money supply, with cash in circulation remaining a significant contributor to the growth of the M2 and M2X aggregates. In addition, the month-on-month increase in the M0 aggregate expectedly continues to gradually return to its pre-pandemic level.

⁸ *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.*

⁹ *Refer to Banking Sector Liquidity and Financial Markets: Facts, Assessments and Comments, No. 10 (56), October 2020.*

DEPOSIT RATES DO NOT DECLINE FURTHER FOR THE SECOND CONSECUTIVE MONTH

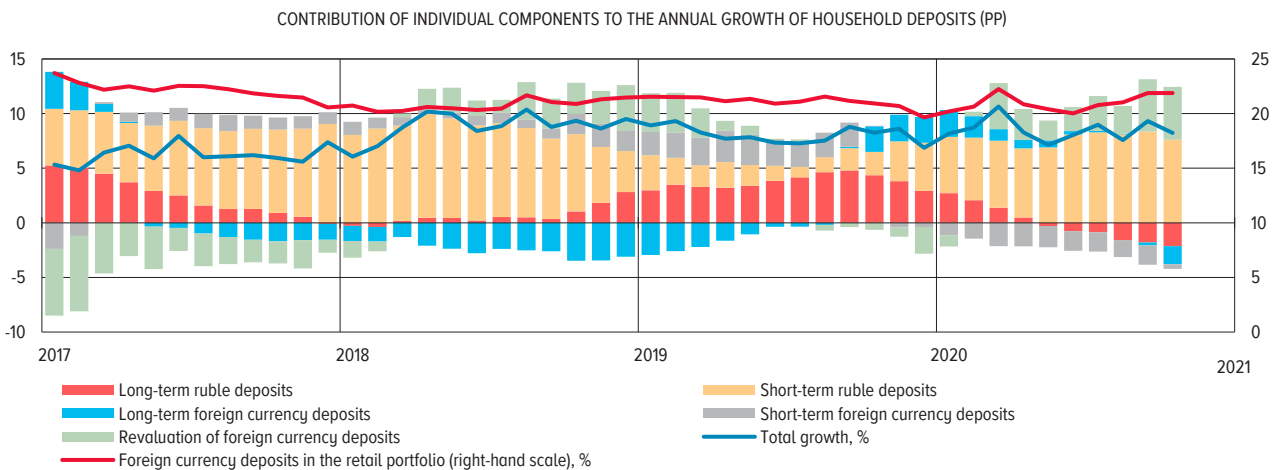
Chart 15



Source: Bank of Russia.

HOUSEHOLDS' SAVING ACTIVITY TRENDED DOWN IN OCTOBER

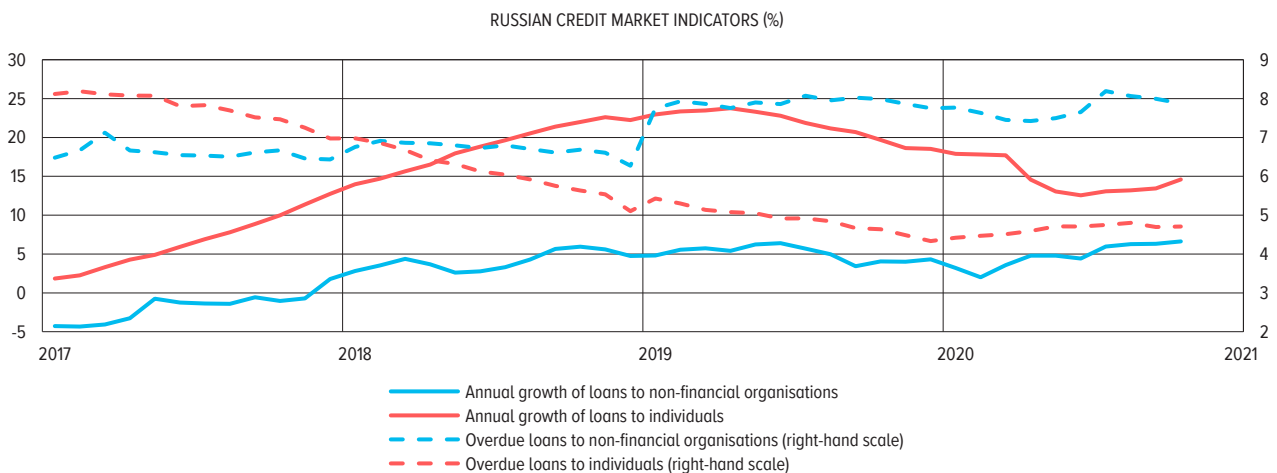
Chart 16



* Excluding escrow accounts.
Source: Bank of Russia calculations.

THE RISE IN LENDING SPED UP IN OCTOBER, WITH THE QUALITY OF BANK LOAN PORTFOLIOS REMAINING STABLE

Chart 17

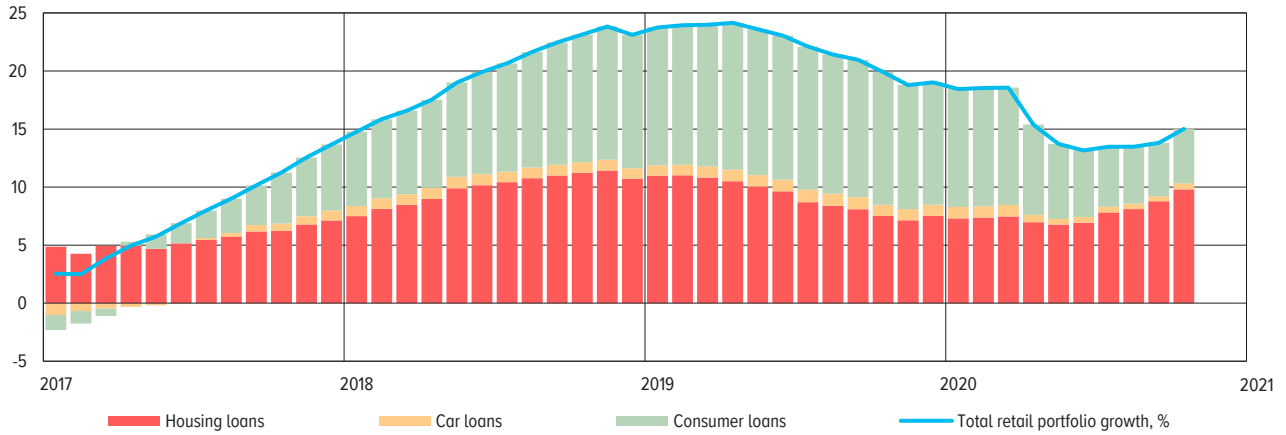


Source: Bank of Russia calculations.

AS A RESULT OF RECORD-HIGH ACTIVITY IN OCTOBER, THE MORTGAGE MARKET REMAINED THE KEY DRIVER OF RETAIL LENDING

Chart 18

CONTRIBUTION OF INDIVIDUAL COMPONENTS TO THE ANNUAL GROWTH OF THE RETAIL LOAN PORTFOLIO* (PP)

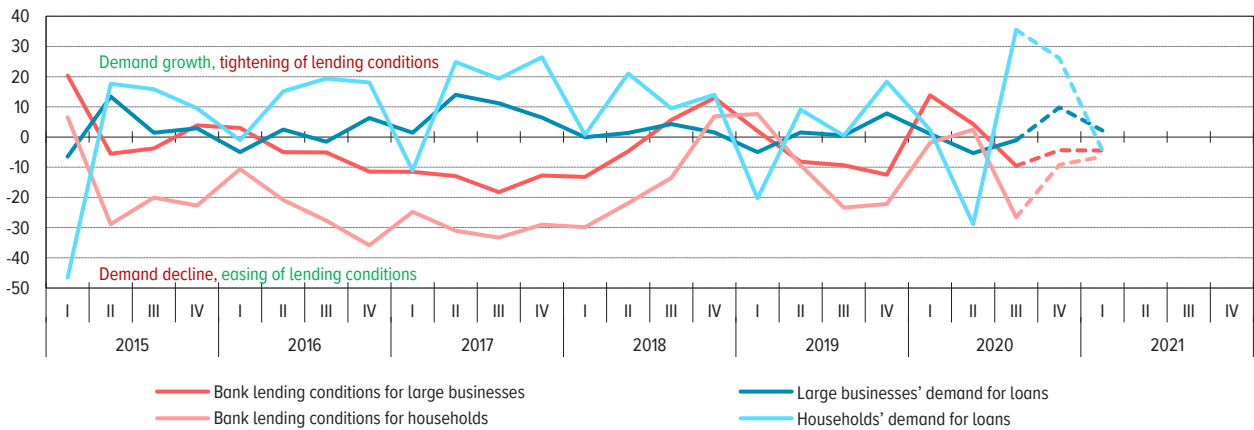


* For loans grouped into homogeneous loan portfolios.
Source: Bank of Russia calculations.

IN 2020 Q3, BANKS RESUMED THE EASING OF NON-PRICE LENDING CONDITIONS FOR ALL MAIN CATEGORIES OF BORROWERS

Chart 19

INDICES OF LENDING CONDITIONS AND DEMAND FOR LOANS (PP)

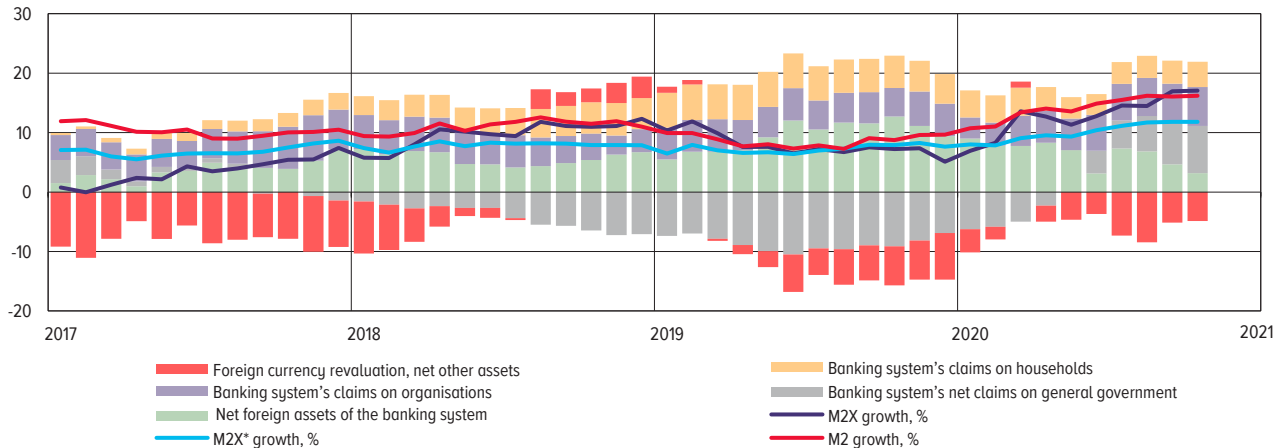


* The dotted lines signify respondent banks' expectations regarding changes in lending conditions and demand for loans in 2020 Q3.
Source: Bank of Russia.

BUDGET OPERATIONS CONTINUE TO BOOST MONEY SUPPLY

Chart 20

SOURCES OF BROAD MONEY (CONTRIBUTION TO THE ANNUAL GROWTH OF BROAD MONEY*, PP)



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

CREDIT AND DEPOSIT MARKET INDICATORS

Table 5

		July 2020	August 2020	September 2020	October 2020
Rates on banks' long-term ruble transactions					
– household deposits	% p.a.	4.3	4.1	4.1	4.1
– household loans	% p.a.	10.9	10.7	10.4	10.1
– corporate loans	% p.a.	7.4	7.0	6.8	-
Household deposits*	% YoY, AF CR	5.8	5.0	4.5	3.4
– in rubles*	% YoY	9.4	8.3	8.3	6.9
– in foreign currency	% YoY	-7.2	-6.5	-8.6	-8.8
– share of foreign currency*	%	20.8	21.0	21.9	21.9
Loans to non-financial organisations	% YoY, AF CR	6.0	6.3	6.3	6.6
– short-term (up to 1 year)	% YoY, AF CR	11.3	14.0	14.2	12.5
– long-term (more than 1 year)	% YoY, AF CR	4.1	4.1	4.1	5.0
– overdue loans	%	8.2	8.1	8.0	7.9
Household loans	% YoY, AF CR	13.1	13.2	13.4	14.6
– housing mortgage loans	% YoY, AF CR	15.7	16.6	18.6	22.0
– unsecured consumer loans	% YoY	10.1	9.5	8.9	9.1
– overdue loans	%	4.8	4.8	4.7	4.7
Banking system's claims on the economy	% YoY, AF CR	9.0	9.3	9.3	9.8
– on businesses	% YoY, AF CR	7.7	8.1	8.0	8.2
– on households	% YoY, AF CR	12.4	12.6	12.9	14.0
Money supply (M2 monetary aggregate)	% YoY	15.5	16.2	16.1	16.2
Broad money	% YoY, AF CR	11.1	11.7	11.8	11.8

* Excluding escrow accounts.

Note: YoY – year-on-year; AF CR – 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 – 08.12.2020 (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 November–December 2020, that period is from 11.11.2020 to 08.12.2020);
- 'Foreign exchange and stock markets' section – 30.11.2020;
- 'Credit and deposit market' section – 01.11.2020.

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.

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12 Neglinnaya Street, 107016 Moscow

Bank of Russia website: www.cbr.ru