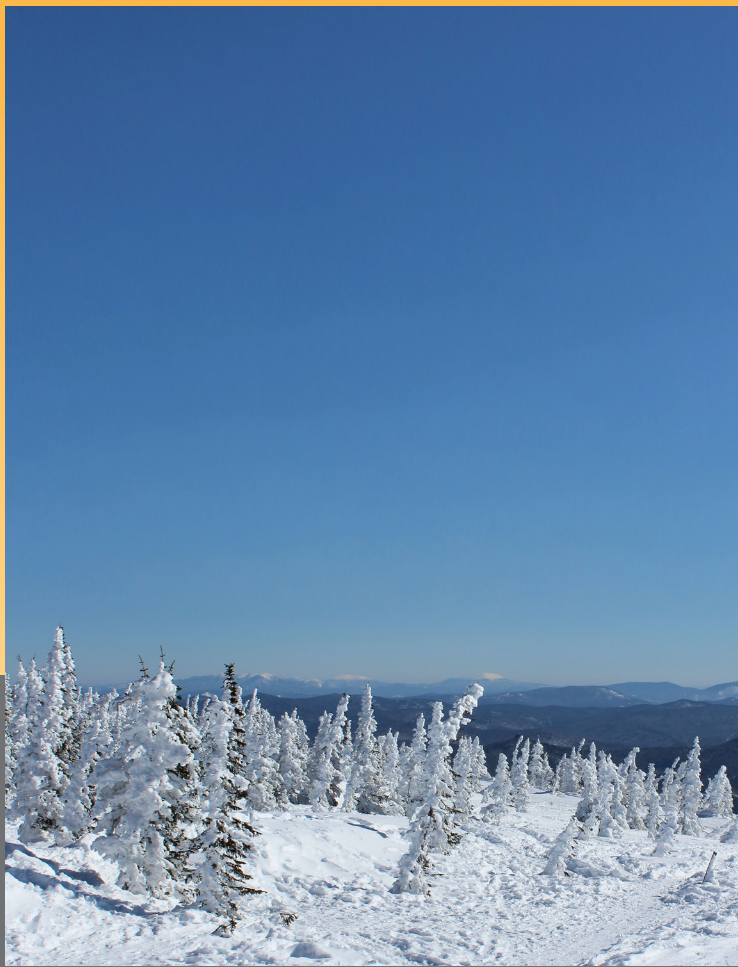
Bank of Russia



BANKING SECTOR LIQUIDITY AND FINANCIAL MARKETS

No. 12 (58) • December 2020

Information and analytical commentary

19 January 2021

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

- Structural liquidity surplus contracted in December. The inflow of funds through the fiscal channel was beneath the expected level, while the amount of cash in circulation increased above forecasts.
- The forecast of the liquidity surplus for the end of 2021 remains at the level of RUB 0.7–1.3 trillion rubles. This forecast factors in adjusted assumptions regarding the time when cash will partially return to banks after the elevated demand for it during the pandemic period, and a rise in temporarily available budgetary funds to be placed with banks.
- The spread between interbank lending (IBL) rates and the Bank of Russia key rate shrank due to the increased demand for rubles in the overnight IBL segment demonstrated by a number of market participants amid a smaller-than-expected liquidity inflow through the fiscal channel in December.
- The situation with foreign currency liquidity in the banking sector remained stable, including as a result of a considerable inflow of clients' funds in November.
- Global financial markets continued an upward trend in December, although a whole range of countries reintroduced lockdowns. Investor sentiment improved amid inspiring news about coronavirus vaccine rollouts and ambitious plans to vaccinate a significant number of people in major economies in 2021 H1.
- In October–November, interest rates on retail demand deposits changed only slightly. As nominal interest rates were low, the annual growth of banks' deposit portfolio continued to slow down and time deposits were still being replaced with current accounts.
- Due to transactions with large borrowers, short- and long-term interest rates on ruble loans to non-financial organisations showed diverse trends in October. Interest rates on loans to small and medium-sized enterprises (SMEs) were up because the anti-crisis concessional lending programmes launched in spring were terminated. The average mortgage rate went upwards in November, including because the share of the secondary segment in the market turnover continued to expand.
- Corporate lending demonstrated sustainable growth in November. A slight slowdown in the retail segment was caused by mortgage asset securitisation transactions and lower consumer activity. Banks' liabilities not included in money supply (escrow accounts, bonds) increased significantly, slightly slowing the annual growth of money supply.

Banking sector liquidity and money market

Ruble liquidity. On average, the structural liquidity surplus in the December required reserve averaging period shrank by **RUB 0.5 trillion** against the November averaging period, to equal **nearly zero**. Its amount as of early January decreased by **0.1 trillion rubles** compared to the beginning of the previous month, to total **0.2 trillion rubles** (Table 3).

The outflow of liquidity in December was mainly caused by the increased amount of cash in circulation. Its changes were close to last year's readings, with credit institutions replenishing their cash offices and ATMs in amounts equivalent to those in the same periods of previous years. Moreover, the December forecast factored in the assumption that a rise in the demand for cash will be lower owing to the already existing holdings. However, the outflow of liquidity due to cash as of the end of the year turned out to be larger than expected.

The inflow of liquidity at the end of the year was driven by a seasonally large amount of budget account operations. However, this inflow was considerably below expectations. This was associated with an increase in tax revenues (specifically, due to the payments of personal income tax and insurance and social contributions) (Chart 2), as well as reduced budget spending. Russia's Ministry of Finance continued to place federal government bonds (OFZ) in small amounts, accumulating funds for financing, including future expenses. According to the Bank of Russia's forecast, a potential impact of higher budget revenues or reduced spending on liquidity was to be fully offset by a corresponding increase in operations carried out by the Federal Treasury (FT) and other budget process participants to place temporarily available funds with banks. However, this did not happen, and the balances of funds of the budget system with the Bank of Russia increased by 1.2 trillion rubles as of the end of 2020 (Chart 7).

In December and January, the Bank of Russia kept the maximum amount of funding provided at its one-month repo auction at 1.5 trillion rubles, in order to enable individual credit institutions to offset temporarily uneven liquidity distribution, as before. In the first half of December, banks' demand for these operations trended downwards to 0.8 trillion rubles; yet, following the auction in January, their liabilities increased anew, to total 1.1 trillion rubles. A range of banks expected the inflow of funds through the fiscal channel to be more significant (as expenditures and/or FT placements) as of the end of December. Eventually, since the inflow of funds turned out to be below their forecasts, they offset this by increasing their repo operations with the Bank of Russia.

Banks' investment in Bank of Russia coupon bonds (coupon OBRs) remained at the level of 0.6 trillion rubles in December. As the banking sector's structural liquidity surplus contracted and in order to ensure greater flexibility in absorbing liquidity through its one-week deposit auctions, the Bank of Russia decided not to place the 40th coupon OBR issue, just as in the previous month.

In the coming months, changes in the structural liquidity surplus will primarily depend on budget operations. Due to seasonal factors, budget revenues exceed expenditures at the beginning of the year, which causes an outflow of liquidity from banks. If the FT does not increase proportionately the amount of its placements with credit institutions, the banking sector may again temporarily face a structural liquidity deficit. Nonetheless, the inflow of budgetary funds is expected to resume in the coming months, with the banking sector returning to a sustainable liquidity surplus.

Money market. The spread between short-term IBL[1] rates and the Bank of Russia key rate equalled -3 bp (in the November averaging period: -21 bp; since the beginning of 2020: -15 bp) (Chart 3). The spread volatility went down to 7 bp (vs 16 bp in the November averaging period; since the beginning of 2020: 18 bp). Expecting a substantial inflow of budgetary funds at the end of the year, a number of credit institutions opted to avoid a significant increase in their correspondent account balances in mid-December, slightly delaying their required reserves averaging. However, since the inflow of budgetary funds and FT placements with banks were beneath the expected levels, a range of credit institutions raised the demand for rubles in the overnight IBL segment, which triggered a rise in IBL rates at the end of December and in the demand for the Bank of Russia's refinancing operations at a fixed interest rate. The above factors also pushed upwards IBL rates in the first business days of January 2021.

Foreign currency liquidity. The interest rate spread in the FX swap and IBL (basis) segments changed only slightly, shrinking to -12 bp on average (vs -18 bp in the November averaging period; -17 bp over 2020) (Chart 4). The situation with foreign currency liquidity remained favourable as a result of a significant inflow of foreign currency to the banking sector in November.[2] In December, non-residents also continued to build up their long positions in the FX swap segment, offering rubles and borrowing foreign currency. As of the end of the year, the amount of these positions reached the level recorded at the end of January 2020.

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

[2] *Refer to Banking Sector Liquidity and Financial Markets: Facts, Assessments and Comments, No. 11 (57), November 2020.*

The forecast of the structural liquidity surplus for the end of 2021 remains at the level of 0.7–1.3 trillion rubles (with the forecast range reduced slightly given the actual data for December 2020). This forecast factors in the assumption that cash will gradually return to banks, after the rise in the demand for it during the pandemic period. However, this process may take several years. Additionally, as the FT will switch to using the treasury single account (TSA) in 2021, this will expand its opportunities to manage budgetary funds. As a result, a larger amount of temporarily available balances of budgetary funds may be deposited with banks. After the Bank of Russia updates its macroeconomic forecast in February 2021, it will adjust its liquidity forecast.

Key rate expectations. As inflation accelerated, the Bank of Russia's decision to maintain the key rate at 4.25% was in line with market expectations. Moreover, actual inflation movements were one of the reasons why analysts and market participants now expect the key rate to remain unchanged at least until mid-2021 (Table 2).

Banking sector liquidity in 2020

In 2020, banking sector liquidity was largely affected by how households and businesses responded to the restrictions introduced due to the outbreak of the pandemic, as well as the measures launched by the Russian Government to support the economy and households. Overall, the outflow of liquidity from banks in 2020 was predominantly because households raised the demand for cash.

After the seasonal inflow of funds to banks in January–February caused by the return of cash after the New Year holidays and the increase in budgetary funds placed with banks by the FT, the liquidity surplus expanded considerably. However, in mid-March the inflow of funds to the banking sector reversed to an outflow. Shortly before the non-work days were announced, households increased the demand for cash. Moreover, there was a reduction in cash inflows to banks as a result of the collection of retailers' earnings. This entailed an outflow of liquidity from the banking sector. The situation in Russia is not unique: changes in the amount of cash in 2020 both in advanced and emerging market economies were comparable, with this upward trend being even more pronounced in a number of countries. Beginning from July, the amount of cash in circulation was rising more slowly, coming closer to the readings recorded in previous years. The forecast amount of cash in 2020 factored in the assumption that the demand for cash in December would be lower than in previous years owing to the already existing holdings. However, banks were replenishing their cash offices and ATMs in amounts equivalent to those during the same periods of previous years. As a result, the outflow of liquidity due to cash as of the end of the year turned out to be larger than expected. The Bank of Russia expects a gradual return to banks of the cash withdrawn by households and businesses from their accounts after the outbreak of the pandemic. Accordingly, the amount of cash in circulation will be gradually decreasing. This will take time, largely depending on how quickly the epidemic situation normalises. In addition, a wider use of cashless payments will continue to restrain the demand for cash.

Fiscal flows also altered notably beginning from 2020 Q2. There was a reduction in both oil and gas revenues of the budget system (due to which Russia's Ministry of Finance shifted from foreign currency purchases to sales) and non-oil and gas revenues. In addition to the decreased tax base, the latter were also pulled down by tax payment deferral. Contrastingly, budget expenditures expanded since measures implemented to support households and provide medical care were financed from the budget. Eventually, the budget system's spending exceeded its revenues in Q2. This local gap was covered primarily through a decrease in balances in the general government accounts with the Bank of Russia and a rise in the internal borrowings of Russia's Ministry of Finance. Having received the Bank of Russia's profit from the sale of the equity stake in Sberbank, the FT, on the contrary, managed to increase the amount of deposits placed with banks, while reducing the maturities of its operations so as to preserve the capacity to promptly finance growing expenditures. As a result, 2020 H1 recorded an inflow of liquidity to the banking sector through the fiscal channel.

Since economic activity bounced back in summer, the payments of non-oil and gas taxes to the budget started to return to normal. In autumn, Russia's Ministry of Finance considerably expanded its OFZ placements to finance the budget deficit, with the FT depositing the raised funds with banks with a certain time lag. This increased the volatility of fiscal flows and their impact on the banking sector liquidity. As expected, budget expenditures were large in December, while the overall inflow of liquidity through the fiscal channel was below the expected level. In its forecast for the end of the year, the Bank of Russia took into account an additional inflow of funds to banks resulting from the transactions to sell Sberbank shares to the Russian Government reduced by the net sales of foreign currency in addition to fiscal rule-based operations. The impact of all other budget operations, including fiscal rule-based ones, was assumed to be close to zero. Nonetheless, budget revenues were above the planned level, while budget expenditures were slightly below it. Moreover, not all excess liquidity was placed by the FT and the budget system's financial institutions in the banking sector. As a result, the overall liquidity inflow through the fiscal channel was below the forecast as of the end of the year.

The banking sector's increased demand for liquidity in 2020 was also driven by the growth of required reserves to 2.8 trillion rubles (+0.4 trillion rubles) to be maintained by banks in their correspondent accounts with the Bank of Russia, which primarily resulted from the foreign currency revaluation of credit institutions' liabilities. Banks transferred another 0.1 trillion rubles into specialised required reserve accounts. However, as banks somewhat delayed their required reserve averaging, banks' balances in their correspondent accounts totalled 2.5 trillion rubles as of the end of the year, which is close to the forecast.

THE OUTFLOW OF LIQUIDITY FROM BANKS IN 2020 WAS PREDOMINANTLY BECAUSE HOUSEHOLDS RAISED THE DEMAND FOR CASH. THE IMPACT OF BUDGET OPERATIONS (INCLUDING FOREIGN EXCHANGE TRANSACTIONS, OFZ PLACEMENTS, AND FT OPERATIONS) ON LIQUIDITY WAS CLOSE TO ZERO

Table 1

(TRILLIONS OF RUBLES)

	2020 (actual)	2020 (forecast)	Deviation
1. Liquidity factors (supply)	**-2.6**	**[-1.8; -1.5]**	**-1.0**
– change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	0.0	[0.3; 0.4]	-0.4
– change in the amount of cash in circulation	-2.6	[-2.1; -1.9]	-0.6
– Bank of Russia's interventions in the domestic FX market and monetary gold purchases**	0.1	0.1	0.0
– regulation of banks' required reserves with the Bank of Russia	-0.1	-0.1	0.0
2. Change in free bank reserves (correspondent accounts)* (demand)**	**-0.1**	**[-0.1; 0.0]**	**0.0**
3. Change in banks' claims on deposits with the Bank of Russia and BoR coupon bonds	**-1.2**	**[-0.5; -0.1]**	**-0.9**
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	**1.4**	**1.3**	**0.1**
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	**-0.2**	**[-1.4; -1.0]**	**1.0**

** 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.*
*** The 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.

MARKET PARTICIPANTS DO NOT EXPECT THE KEY RATE TO BE CUT IN 2021 H1 *Table 2*

1. Expectations based on market indicators,* interest rate (instrument)	**March 2021**	**June 2021**
– MosPrime 3M (FRA)	4.86 (4.75)	4.94 (4.73)
– RUONIA (ROISfix)	4.21 (4.15)	4.22 (4.14)
– RUONIA (futures)	4.21 (4.21)	4.24 (4.21)
2. Analysts' key rate expectations*	**As of 31.12.2020**	**As of 31.12.2021**
– Bloomberg survey	4.25 (4.125)	4.00 (4.00)
– Reuters survey	4.25 (4.125)	4.25 (4.00)

** 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 DECEMBER 2020 *Table 3*
(START OF BUSINESS, BILLIONS OF RUBLES)

	01.01.2017	**01.01.2018**	**01.01.2019**	**01.01.2020**	**01.12.2020**	**01.01.2021**
Structural liquidity deficit (+) / surplus (-)	**736**	**-2,639**	**-3,016**	**-2,761**	**-296**	**-204**
Bank of Russia's claims on credit institutions	**1,258**	**10**	**21**	**18**	**1,287**	**975**
Auction-based facilities	216	-	-	-	1,230	847
– repos and FX swaps	-	-	-	-	1,230	847
– secured loans	216	-	-	-	0	0
Fixed interest rate facilities	1,042	10	21	18	57	129
– repos and FX swaps	632	4	8	13	0	118
– secured loans	411	5	13	5	57	10
Credit institutions' claims on the Bank of Russia	**785**	**2,729**	**3,293**	**2,983**	**2,199**	**1,795**
Deposits	785	2,372	1,902	1,026	1,593	1,221
– auction-based	397	2,125	1,478	697	1,457	844
– fixed interest rate	388	247	424	330	136	377
BoR coupon bonds	0	357	1,391	1,956	606	575
Standing reverse facilities, other than standard monetary policy instruments of the Bank of Russia*	**263**	**81**	**256**	**204**	**616**	**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 FORECAST OF THE STRUCTURAL LIQUIDITY SURPLUS FOR THE END OF 2021 REMAINS AT THE LEVEL OF 0.7–1.3 TRILLION RUBLES AND FACTORS IN THE ASSUMPTIONS THAT A PART OF CASH WILL GRADUALLY RETURN TO BANKS, AFTER THE ELEVATED DEMAND FOR IT DURING THE PANDEMIC PERIOD, AND THAT BALANCES OF BUDGETARY FUNDS WITH THE BANK OF RUSSIA WILL DECREASE *Table 4*

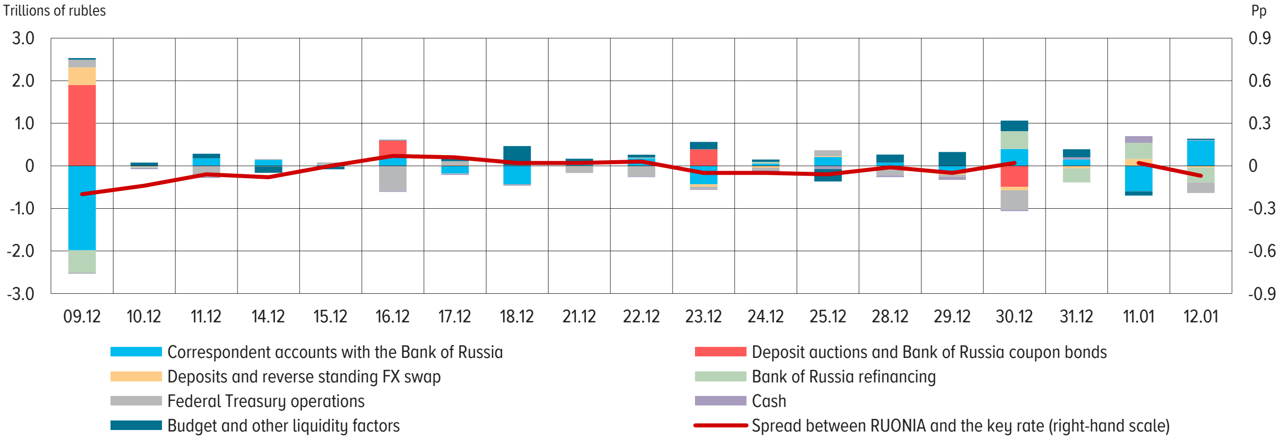
(TRILLIONS OF RUBLES)

	2019 (actual)	December 2020	2020 (actual)	2021 (forecast)
1. Liquidity factors	**0.5**	**-0.4**	**-2.6**	**[0.9; 1.4]**
– change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	0.2	0.1	0	[0.6; 0.9]
– change in the amount of cash in circulation	-0.1	-0.5	-2.6	[0.4; 0.6]
– Bank of Russia interventions in the domestic FX market and monetary gold purchases**	0.4	0	0.1	0
– regulation of banks' required reserves with the Bank of Russia	0	0	-0.1	-0.1
2. Change in free bank reserves (correspondent accounts)* (demand)**	**0.7**	**-0.3**	**-0.1**	**[0.3; 0.4]**
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	**-0.3**	**-0.4**	**-1.2**	**[-0.9; -0.3]**
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	**-0.1**	**-0.3**	**1.4**	**-1.4**
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	**-2.8**	**-0.2**		**[-1.3; -0.7]**

** 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 A SLIGHT INFLOW OF LIQUIDITY TO THE BANKING SECTOR IN DECEMBER 2020 *Chart 1*

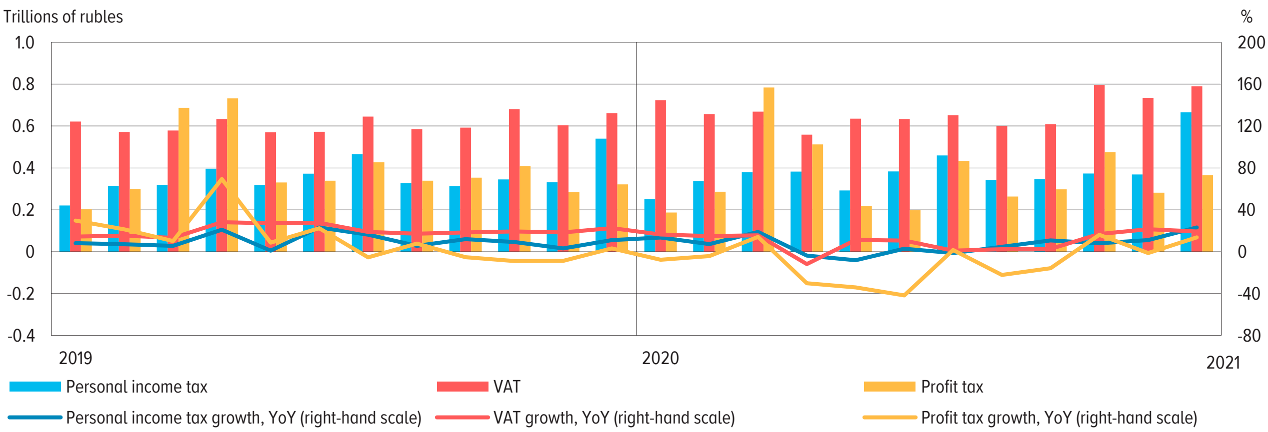
CHANGES IN THE BANK OF RUSSIA'S BALANCE SHEET AND MONEY MARKET RATES (OVERNIGHT)



Source: Bank of Russia calculations.

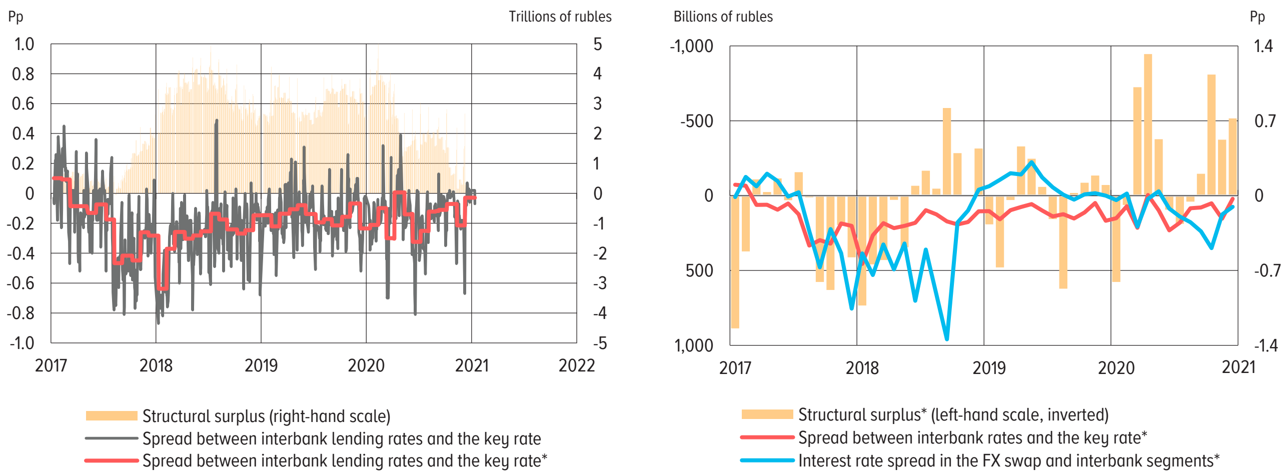
THE GROWTH OF PERSONAL INCOME TAX AND PROFIT TAX PAYMENTS SPED UP IN DECEMBER 2020 *Chart 2*

TAX REVENUES ACCORDING TO DATA FROM THE BANK OF RUSSIA PAYMENT SYSTEM*



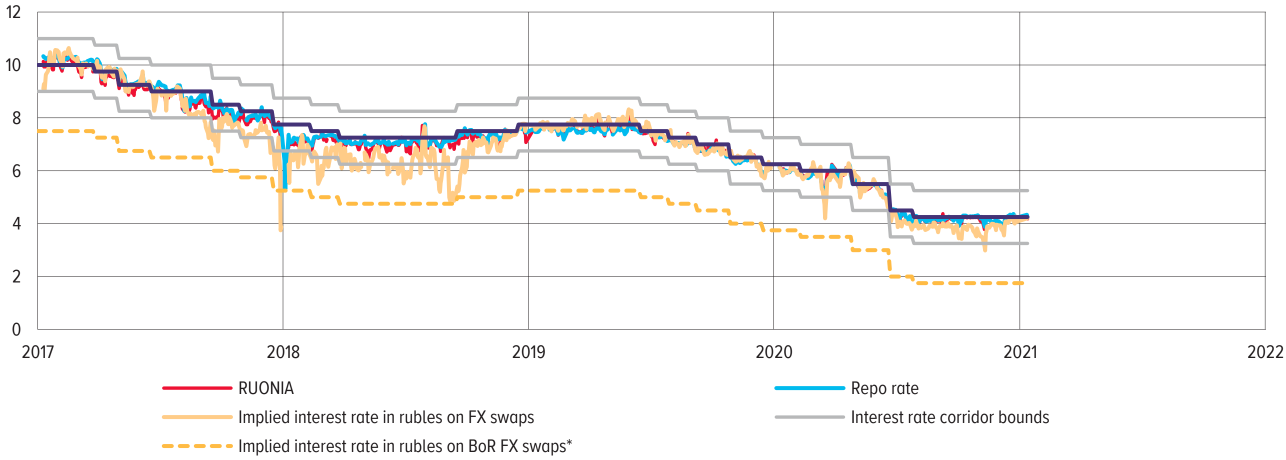
* *Funds transfers from credit institutions' accounts to the budget system's accounts with budget classification codes corresponding to the above taxes.*
Source: Bank of Russia calculations.

THE SPREAD BETWEEN INTERBANK LENDING RATES AND THE BANK OF RUSSIA KEY RATE CONTRACTED *Chart 3*



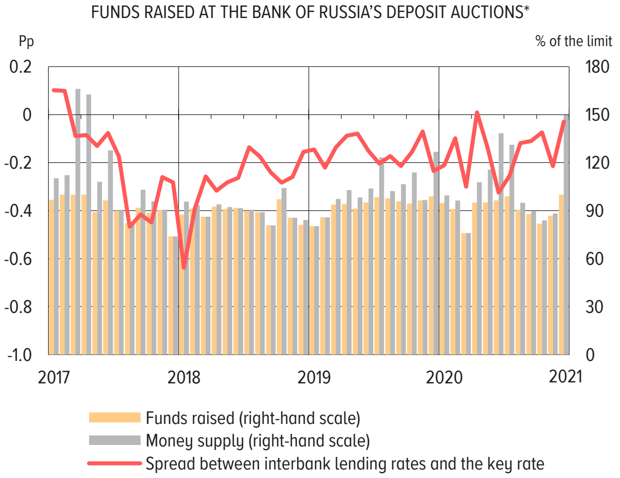
* *Average for averaging periods.*
Source: Bank of Russia calculations.

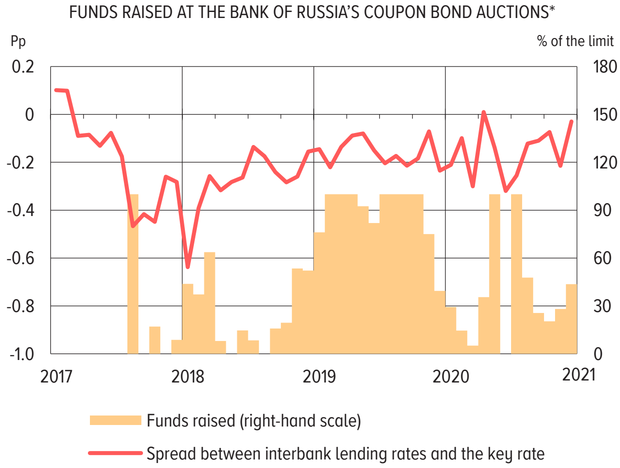
THE SPREAD IN THE FX SWAP AND IBL (BASIS) SEGMENTS SHRANK *Chart 4*
(% P.A.)



** 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.

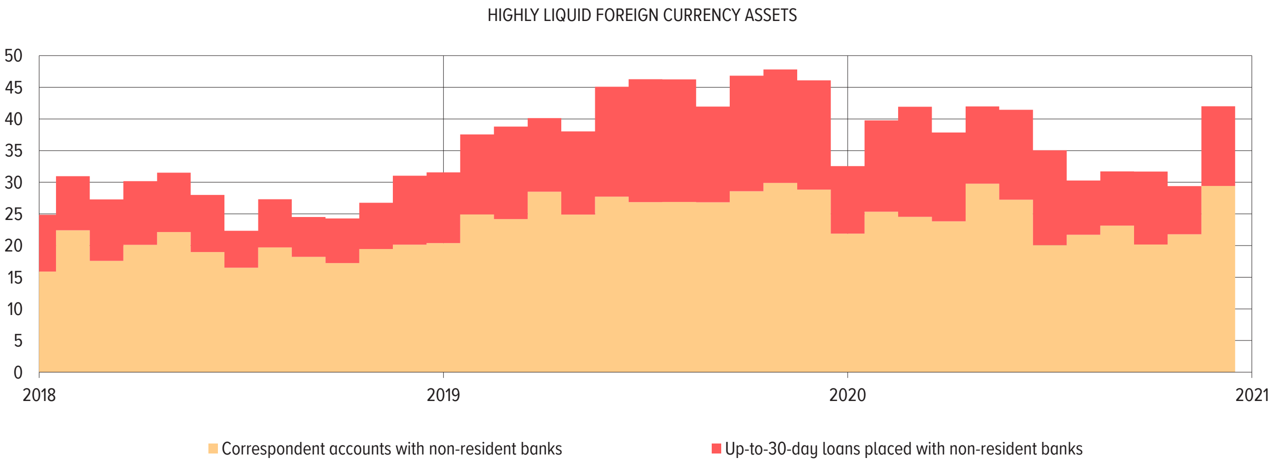
BANKS' SUPPLY AT THE BANK OF RUSSIA'S ONE-WEEK DEPOSIT AUCTIONS SLIGHTLY EXCEEDED THE ESTABLISHED LIMITS *Chart 5*





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

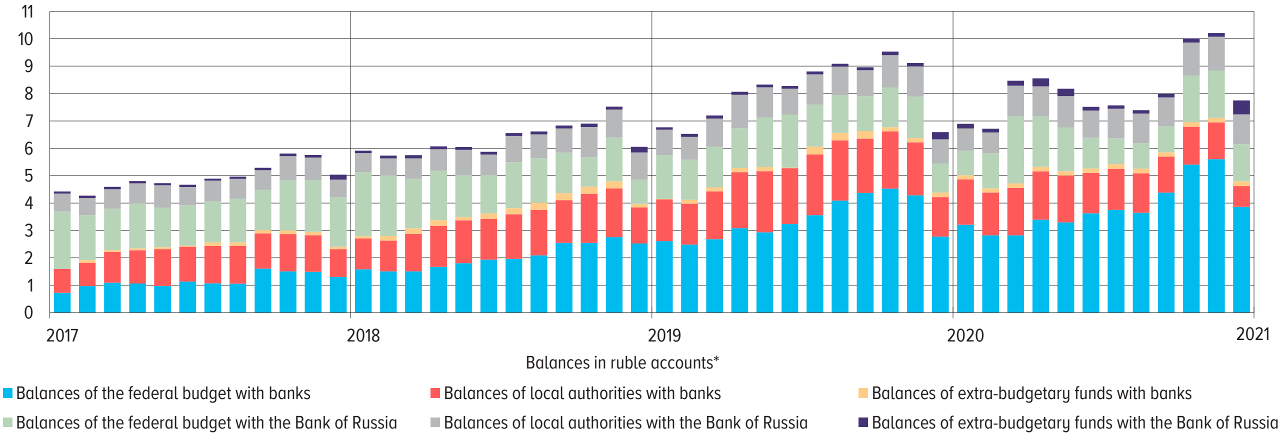
THE AMOUNT OF HIGHLY LIQUID FOREIGN CURRENCY ASSETS INCREASED IN NOVEMBER (AS OF 1 DECEMBER) *Chart 6*
(BILLIONS OF US DOLLARS)



Source: Bank of Russia calculations.

THE FT AND THE CONSTITUENT TERRITORIES OF RUSSIA REDUCED THE AMOUNT OF FUNDS DEPOSITED WITH BANKS IN DECEMBER 2020, BUT BALANCES IN BUDGET ACCOUNTS EXPANDED AS OF THE END OF THE YEAR *Chart 7*

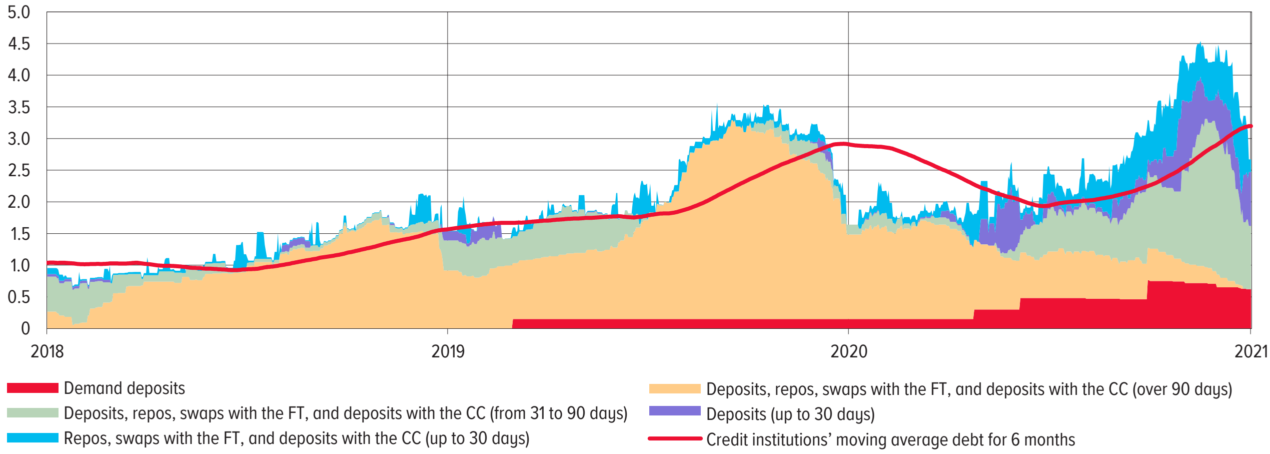
(TRILLIONS OF RUBLES, AS OF THE PERIOD-END)



** According to banking reporting form 0409301 'Performance indicators of a credit institution', the Bank of Russia's daily balance sheet.*
Source: Bank of Russia calculations.

CREDIT INSTITUTIONS' DEBT TO THE FT SHRANK BY 1.8 TRILLION RUBLES IN DECEMBER 2020 *Chart 8*

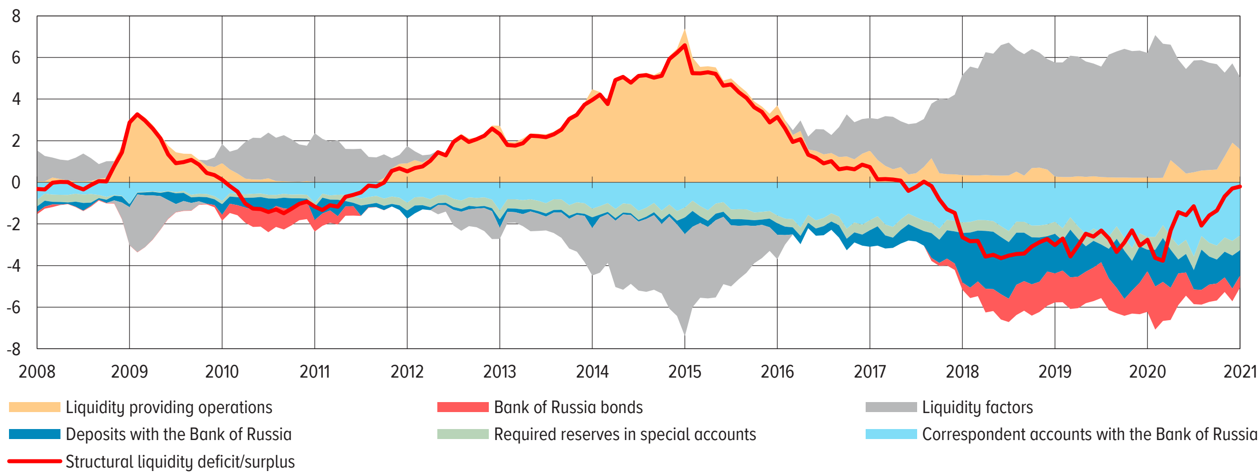
(TRILLIONS OF RUBLES)



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

Global financial markets continued an upward trend in December, although a range of countries reintroduced lockdowns. Investor sentiment improved amid inspiring news about coronavirus vaccine rollouts and ambitious plans to vaccinate a significant number of people in major economies in 2021 H1. In addition, political risks in the USA associated with a potential challenge of the election result lowered. Following global markets, the Russian financial market also revived, except the government bond segment with prices there going down amid faster inflation.

Exchange rate. The ruble significantly strengthened (from 76.4 to 73 against the US dollar) in the first half of the month on the back of the general growth of emerging market economies' (EMEs) currencies (Chart 10) and oil prices. Further on, the news about cyber attacks in the USA induced a drastic weakening of the ruble, with its exchange rate returning to the readings recorded at the beginning of the month. However, as there was no official response from the US authorities, this calmed down investors, and the ruble started to strengthen again, reaching 74.4 against the US dollar as of the end of the year. Thus, the ruble lost 20% over 2020, which is comparable with 2018, when the ruble had weakened by 21% amid escalating rhetoric about sanctions. Nonetheless, this is significantly less than over the worst period of the 2008 crisis (in March 2007 – February 2008, the ruble lost 50%) or the 2014 crisis (the ruble weakened almost twice). The EM currency index declined only by 5.7% over the year, which is partially explained by a high percentage in the index of the Chinese yuan which gained 6.7% over the year. The national currencies of Brazil and Turkey also lost approximately 20%.

Country risk premium. Russia's CDS spread stayed in the range of 75–80 bp beginning from mid-November, soaring to 93 bp amid elevated geopolitical risks and going down to 89 bp by the end of the year. As a result, Russia was the only major EME with its CDS spread expanding as of the end of the month (+8 bp). It increased by 34 bp over the year, which is comparable with other EMEs.

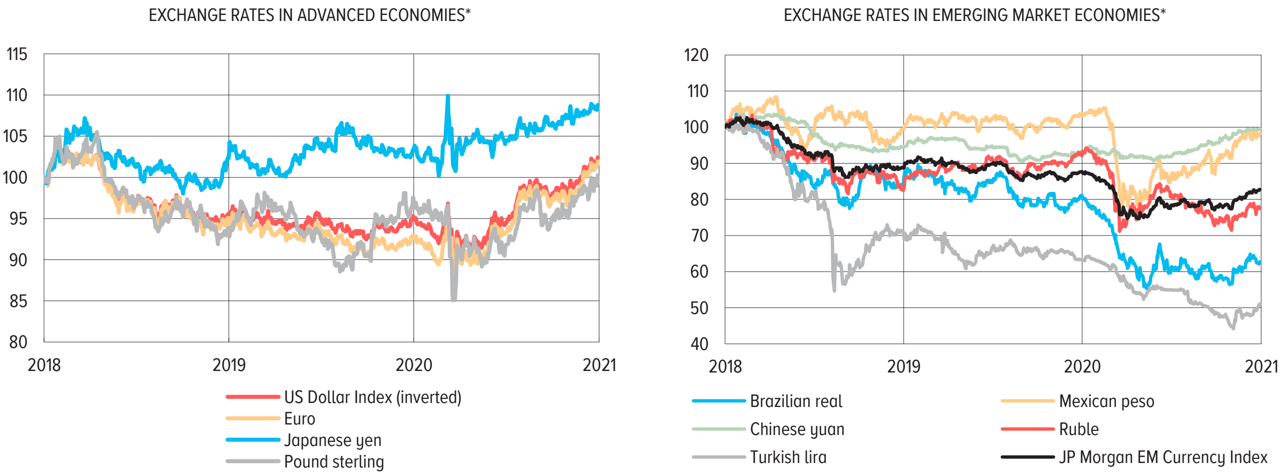
Federal government bonds. Medium- and long-term OFZ yields rose (Chart 12): OFZ 2Y – 4.57% (+1 bp), OFZ 5Y – 5.47 bp (+14 bp), and OFZ 10Y – 6.27 bp (+12 bp). As the Bank of Russia considerably reduced the key rate and shifted to accommodative monetary policy in 2020, this caused an overall decrease in the OFZ yield curve, with short-term OFZ yields declining the most. From the beginning of the year, the yields of OFZ 2Y and OFZ 10Y declined by 104 and 14 bp, respectively.

Russia's Ministry of Finance reduced its issues, since the target for OFZ placements was achieved as early as in November. In the course of the seven recent auctions, the Ministry of Finance placed bonds worth 118.4 billion rubles (vs 814.6 billion rubles in November). Overall, OFZ bonds placed by the Ministry of Finance over the year totalled 5.3 trillion rubles at face value, which is a record high. Russian banks purchased 77% of this amount, while foreign investors accounted for 13%. In December, non-residents continued to build up their OFZ holdings, increasing them by 25.8 billion rubles over the month (Chart 14).

Stocks. Stock indices in the majority of economies continued to rise, exceeding pre-pandemic levels in a number of countries (Chart 13). The Russian market demonstrated a similar trend. The MOEX Index gained 5.8% in December, adding 8.0% over 2020, which is its new record high. The RTS index edged up by 8.2% in December, while declining by 10.4% as of the end of the year due to the ruble's weakening.

MOST CURRENCIES STRENGTHENED AGAINST THE US DOLLAR
(02.01.2018 = 100)

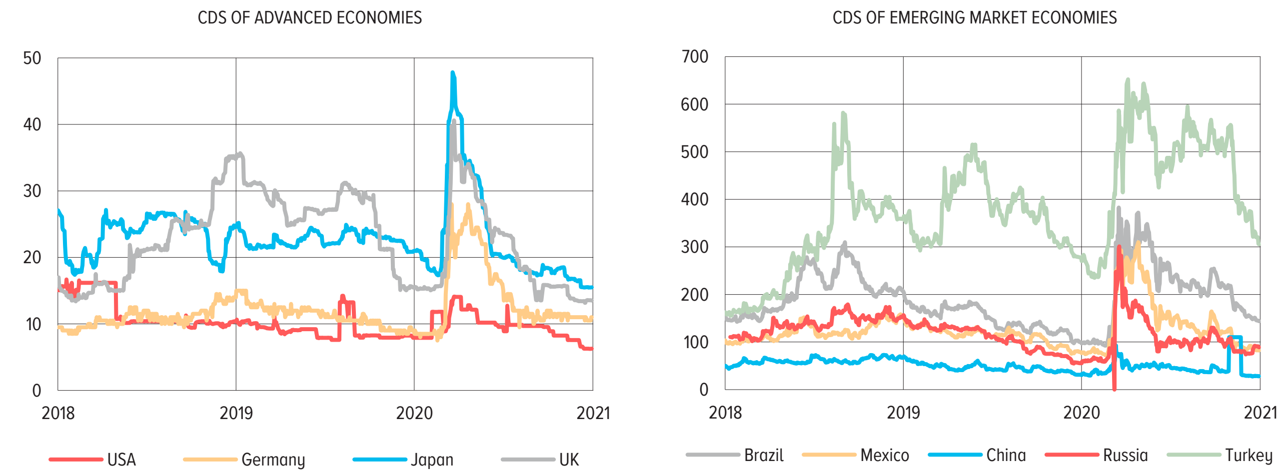
Chart 10



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

RUSSIA'S CDS SPREAD EXPANDED IN CONTRAST TO THE MAJORITY OF ECONOMIES
(BP)

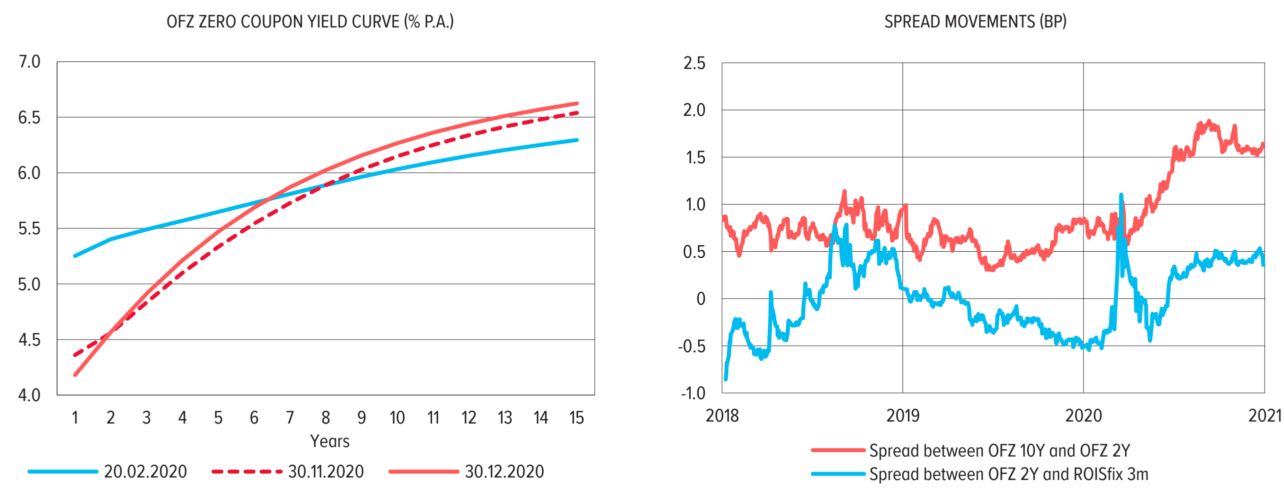
Chart 11



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

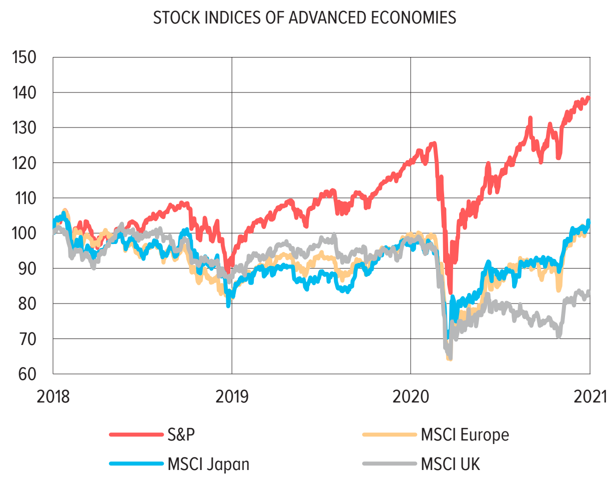
MEDIUM- AND LONG-TERM OFZ YIELDS INCREASED AMID ELEVATED INFLATION EXPECTATIONS

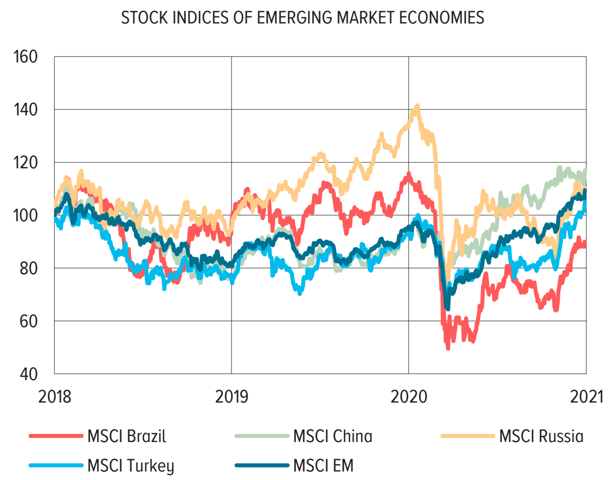
Chart 12



Source: PJSC Moscow Exchange.

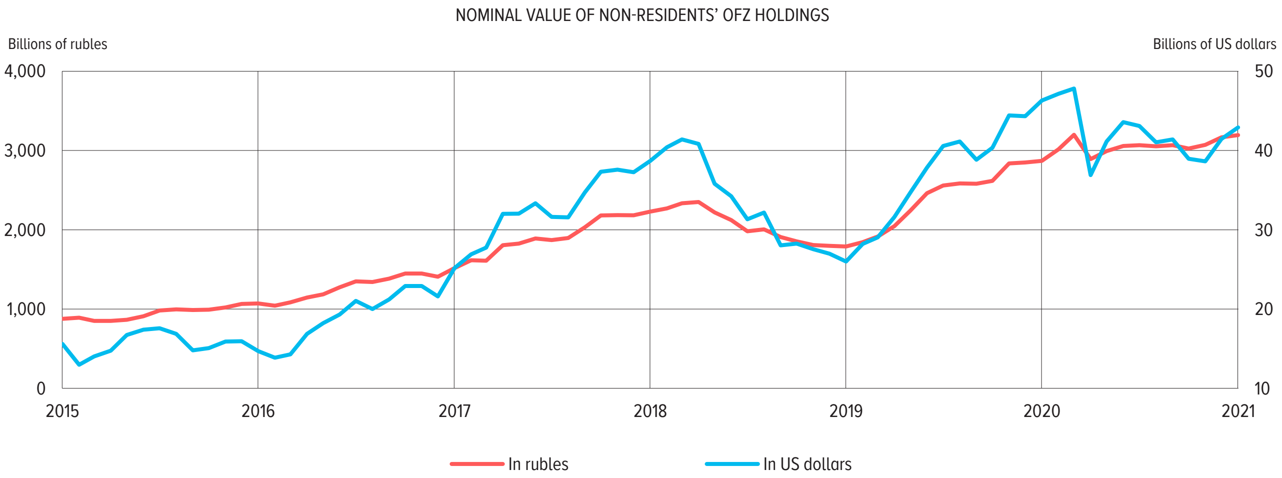
STOCK MARKETS CONTINUED TO BOUNCE BACK AMID THE NEWS ABOUT CORONAVIRUS VACCINE ROLLOUTS *Chart 13*
(02.01.2018 = 100)





Sources: Bloomberg, Bank of Russia calculations.

FOREIGN INVESTORS CONTINUED OFZ PURCHASES *Chart 14*



Source: Bank of Russia calculations.

GLOBAL MARKET PRICES CONTINUED TO GROW IN DECEMBER *Table 5*

Indicator		30.12.2020	1M	3M	6M	YTD	1Y
Russian financial market							
RUB/USD exchange rate		74.41	2.6	4.1	-4.5	-20.0	-20.0
MOEX Index		3,289	5.8	13.2	19.9	8.0	8.0
RTS Index		1,387	8.2	17.7	14.4	-10.4	-10.4
Government bond yield		5.76	11	-13	20	-45	-45
Corporate bond yield		6.11	-9	-19	15	-62	-62
Regional bond yield		5.68	-12	-8	0	-59	-59
CDS spread		89	8	-35	-18	34	34
RVI		33	2	-5	-2	10	10
Exchange rates (per US dollar, % change, '+' – appreciation, '-' – depreciation)							
AEs*	US Dollar Index	89.68	-2.4	-4.5	-7.7	-7.0	-7.3
	Euro	1.23	3.1	4.9	9.3	9.7	9.8
	Japanese yen	103.19	1.1	2.2	4.1	5.3	5.5
	Pound sterling	1.36	2.3	5.5	9.2	2.8	3.9
EMEs	JP Morgan EM Currency Index	57.99	2.9	6.4	5.9	-5.6	-5.5
	Ruble	74.41	2.6	4.1	-4.5	-20.0	-20.0
	Brazilian real	5.19	2.7	8.0	2.4	-22.6	-22.6
	Mexican peso	19.90	1.4	11.1	14.0	-4.9	-4.9
	Chinese yuan	6.52	0.9	4.1	8.4	6.7	7.1
	Turkish lira	7.38	6.0	4.5	-7.3	-19.4	-19.4
	South African rand	14.61	5.8	14.5	16.6	-4.3	-3.5
10-year bond yield (% p.a., change in bp, '+' – increase, '-' – decrease)							
AEs	USA	0.93	8	24	25	-99	-96
	Germany	-0.57	0	-5	-18	-38	-38
	Japan	0.02	-1	1	-2	4	4
	UK	0.21	-9	-2	0	-61	-65
EMEs	Russia	5.92	8	-33	1	-45	-46
	Brazil	6.59	-103	-78	-1	-9	-9
	Mexico	5.54	-25	-58	-19	-135	-133
	China	3.12	-15	-1	28	-1	-1
	Turkey	12.93	136	7	141	98	101
	South Africa	8.75	-22	-67	-45	-27	-25
5Y CDS spreads (bp, change in bp, '+' – increase, '-' – decrease)							
AEs	USA	6	-1	-3	-3	-2	-2
	Germany	11	0	-1	-5	2	2
	Japan	16	-1	-3	-4	-5	-5
	UK	14	0	-2	-10	-2	-2
EMEs	Russia	89	8	-35	-18	34	34
	Brazil	144	-22	-106	-101	45	44
	Mexico	82	-6	-69	-67	3	3
	China	28	-3	-21	-20	-3	-3
	Turkey	306	-77	-222	-172	28	28
	South Africa	203	-24	-109	-90	41	39
Stock indices (points, % change, '+' – increase, '-' – decrease)							
AEs	S&P	3,732	3.0	11.0	19.8	15.5	15.9
	MSCI Europe	1,856	5.5	16.3	20.4	4.0	4.1
	MSCI Japan	1,106	2.99	12.6	18.3	6.6	6.6
	MSCI UK	1,837	4.3	11.5	5.4	-14.8	-15.3
EMEs	MSCI EM	1,289	7.0	19.1	28.8	15.6	15.3
	MSCI Russia	668	9.5	19.2	9.8	-17.2	-17.5
	MSCI Brazil	1,882	13.6	36.9	26.4	-20.7	-20.7
	MSCI Mexico	4,644	8.1	31.9	35.6	-2.4	-2.8
	MSCI China	108	2.2	10.6	23.3	26.0	25.6
	MSCI Turkey	1,698,877	14.9	25.9	21.2	13.1	12.6
	MCSI South Africa	1,356	4.0	7.3	7.0	-1.0	-2.4

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

Credit and deposit market

Deposit rates. In the last months of 2020, interest rates on ruble deposits remained almost unchanged against the levels recorded as of the end of Q3, with long- and short-term deposit rates staying at 4.1–4.2% p.a.[1] and 3.2–3.3% p.a., respectively (Chart 15). Interest rates on long-term deposits edged up slightly (by 2–3 bp per month), supported by a moderate increase in returns on financial market instruments and banks' competition for depositors. Market average interest rates on short-term deposits alternately rose and lowered.

As the inflow of households' funds into demand deposits and current accounts (see the section 'Deposit operations') increased, this toughened price competition among banks in this market segment. In November, the average market interest rate on demand deposits equalled 2.9% p.a., almost reaching short-term deposit rates.

Interest rates on foreign currency deposits stayed close to their record lows (0.4–0.6% on US dollar-denominated deposits and 0.0–0.3% on euro deposits) as interest rates in the global market remained low and banks demonstrated low interest in expanding their foreign currency assets and liabilities.

Deposit operations. The inflow of households' funds into deposits[2] continued to slow down in November (Chart 16). As of early December, the annual growth of the retail deposit portfolio[3] totalled 3.0% (vs 3.4% in the previous month). As in previous months, the increase in deposits slowed down due to the rising demand for savings alternatives, including real estate (balances in escrow accounts rose by more than 170 billion rubles in November) and securities (the number of active retail customers at the Moscow Exchange hit another record high in November, exceeding 1.3 million people).

The slowdown of the growth of deposits came along with changes in their structure. As the epidemic situation remained uncertain and the spread between interest rates on time and demand deposits contracted, households continued to transfer their funds from time deposits to current accounts. As of early December, balances in demand deposits were 1.5 times higher than a year before. Balances in time deposits shrank by nearly 11% over the same period. The only segment of time deposits with an inflow of households' funds was deposits for over three years (+7%). Banks seeking to form sustainable liabilities offered more attractive interest rates on deposits with longer maturities.

The reduction in the portion of foreign currency deposits slowed down in November, although this trend had been prevailing in the market in recent years. The annual growth of ruble deposits (5.7% vs 6.9% in the previous month) and the annual decrease in foreign currency deposits (-6.6% vs -8.8%) both decelerated as of the end of the month. Nonetheless, the strengthening of the nominal exchange rate of the ruble contributed to a notable reduction in retail foreign currency deposits (from 21.9% at the beginning to 21.4% at the end of the month), owing to the decline in the ruble value of foreign currency deposits.

Credit rates. Interest rates on ruble loans in the corporate segment[4] of the market moved diversely, primarily influenced by transactions with large borrowers. Specifically, the weighted average interest rate on short-term loans edged down by 0.13 pp to 6.02% p.a., while rising in long-term lending by 0.23 pp, to reach 7.04% (Chart 15). Moreover, the average interest rate on loans to SMEs was growing for the second consecutive month, due to the gradual termination of the concessional lending programmes launched in spring and the increased uncertainty over a resurgence of

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[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, deposits do not include escrow accounts under equity construction contracts.

[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.

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

coronavirus cases. In October, this rise in interest rates was more significant in the short-term segment as the disbursements of preferential loans to agricultural companies were reduced.

The decrease in interest rates on long-term retail ruble loans discontinued in November. The interest rate on loans with over one-year maturities was up by 0.22 pp, to reach 10.29% p.a. This was driven by the growth of interest rates on ruble-denominated mortgage loans, including due to the increasing share of the secondary segment in the mortgage market turnover. Another reason was that the disbursements of mortgage loans had passed their peak in the previous month. The average interest rate on retail ruble loans granted for up to one year edged down slightly by 0.05 pp to 13.77% p.a.

As the Bank of Russia kept the key rate unchanged in December, interest rates may be expected to hover around the September–October levels in the short run. As before, the general trend of interest rates will depend on the percentage of concessional lending in the market turnover, banks' willingness to progressively expand lending to higher-risk borrowers, and borrowers' demand for loans amid the persisting uncertainty caused by the coronavirus pandemic.

Corporate lending. Corporate lending continued to expand faster in November: the annual growth of loans to non-financial organisations sped up from 6.6% to 7.4%, hitting its five-year high (Chart 17). Nonetheless, the portion of overdue loans in the portfolio was close to the previous month's level.

Corporate lending was predominantly driven by ruble transactions. Moreover, the short-term segment again started to grow at an increased pace in November, which was associated with the introduction of local restrictions amid the deteriorating epidemic situation. As of the end of the month, the annual growth of loans for up to one year sped up to 10.5% against 9.1% the month before, and that of loans for over one year – to 7.8% against 7.5% in the previous month.

Along with high activity in corporate lending, market participants also expanded borrowings in the bond market: as of early December, non-financial issuers' market bond portfolio approximated 9.8 trillion rubles, adding 1.9 trillion rubles over the year.

In the short run, the further growth of corporate lending may be hindered by the actual worsening of the epidemic situation and, consequently, the unsteady revival of domestic demand coupled with the significant expansion of the bond market.

Retail lending. In November, activity in retail lending slightly slowed down, with the annual growth of the household loan portfolio declining to 13.9% from 14.6% in the previous month (Chart 17). This trend predominantly resulted from a deceleration in mortgage lending caused by securitisation transactions: the annual growth of the mortgage loan portfolio[5] edged down by 1.2 pp, to equal 20.8% as of the end of November (Chart 18). Nevertheless, credit activity in this segment of retail lending remained high. As the preferential 6.5% mortgage lending programme was extended and interest rates on loans for purchasing finished housing dropped to their record lows, housing mortgage loans granted over the month totalled nearly 491 billion rubles, which was only 55 billion rubles beneath the peak achieved in October.

In November, the recovery growth in car and unsecured consumer lending slowed down from 2.3% to 0.9% and from 1.5% to 1.1%, respectively, dragged down by lower consumer activity amid the deteriorating epidemic situation.[6]

Retail lending may be expected to continue a steady upward trend in the short run, still driven mostly by mortgage loans, including owing to the extension of the preferential lending programme in the new housing segment until the middle of 2021. The growth in household lending will also be supported by the stable quality of loans: the portion of overdue loans in the portfolio remained unchanged over the month, equalling 4.7%.

[5] *Housing mortgage loans, net of claims on such loans acquired by banks.*

[6] *Refer to Economy: Facts, Assessments and Comments, No. 11 (59), November 2020.*

Money supply. In November, the rise in the banking system's claims on the economy[7] continued to speed up, driven by corporate lending (see the section 'Corporate lending'). By early December, the annual growth of claims on businesses totalled 9.0%, which is close to its three-year high. As in previous months, ruble loans to financial and non-financial organisations were the key contributor to the increase in claims, with loans to non-financial organisations accounting for a higher percentage in this growth in November. The rise in banks' claims on households slowed down as of the end of the month; yet, this deceleration was technical (see the section 'Retail lending').

Budget operations continued to drive the growth of money supply, but their contribution remained almost unchanged in November. Although lending in the non-bank sector expanded and budget spending stayed at the same level, the increase in money supply slightly slowed down as of the end of November, as compared to October's highs: as of the end of the month, the annual growth of broad money (the M2X aggregate) reached 11.6% and that of money supply in the national definition (the M2 aggregate) – 14.1%. This trend emerged because the Russian financial system continued to become more complicated, funds were transferred from current and time deposits included in money supply into other forms of banks' liabilities (escrow accounts, bonds), and the low base effect of summer and autumn 2019 was exhausted.

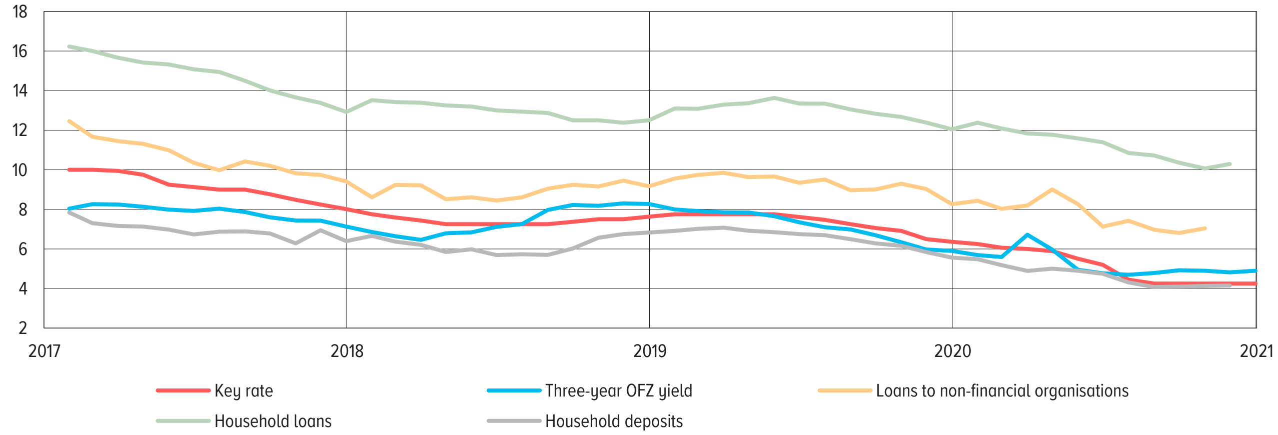
As in previous months, ruble-denominated instruments were the main contributor to the growth of money supply, as a result of which the M2 aggregate expanded more considerably than broad money. In addition, the importance of cashless transfers started to rise again. In November, the amount of ruble cash money in circulation decreased for the first time since early 2020, with its annual growth slowing, which may be a sign of a return to the economic behaviour prevailing before the pandemic.

[7] *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.*

INTEREST RATES IN THE MAIN SEGMENTS OF THE CREDIT AND DEPOSIT MARKETS SLIGHTLY FLUCTUATED SHOWING DIVERSE TRENDS

Chart 15

INTEREST RATES ON BANKS' LONG-TERM RUBLE TRANSACTIONS (% P.A.)

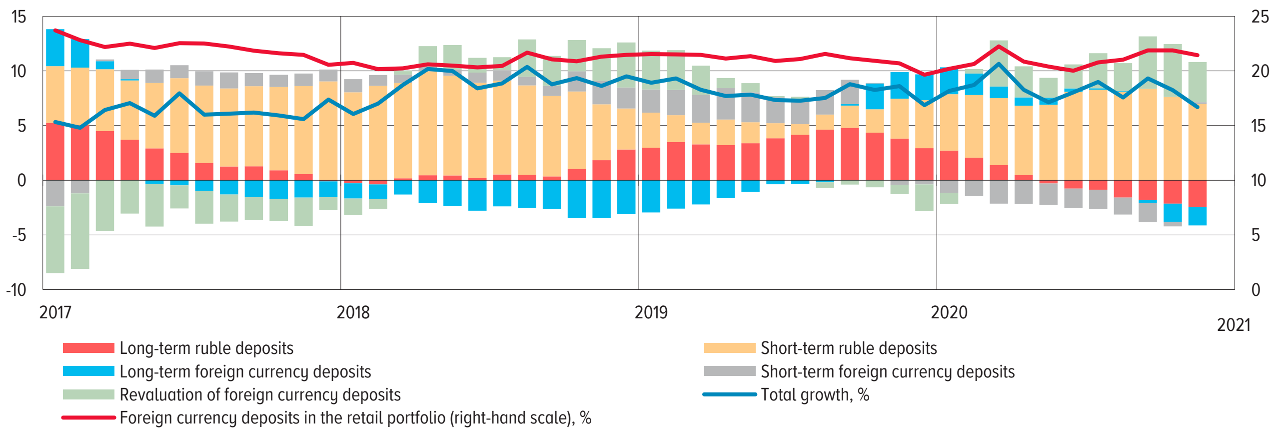


Source: Bank of Russia.

HOUSEHOLDS CONTINUED TO TRANSFER THEIR FUNDS FROM TIME DEPOSITS TO CURRENT ACCOUNTS IN NOVEMBER AMID THE GENERALLY SLOWER INFLOW OF FUNDS INTO BANK DEPOSITS

Chart 16

CONTRIBUTION OF INDIVIDUAL COMPONENTS TO THE ANNUAL GROWTH OF HOUSEHOLD DEPOSITS (PP)

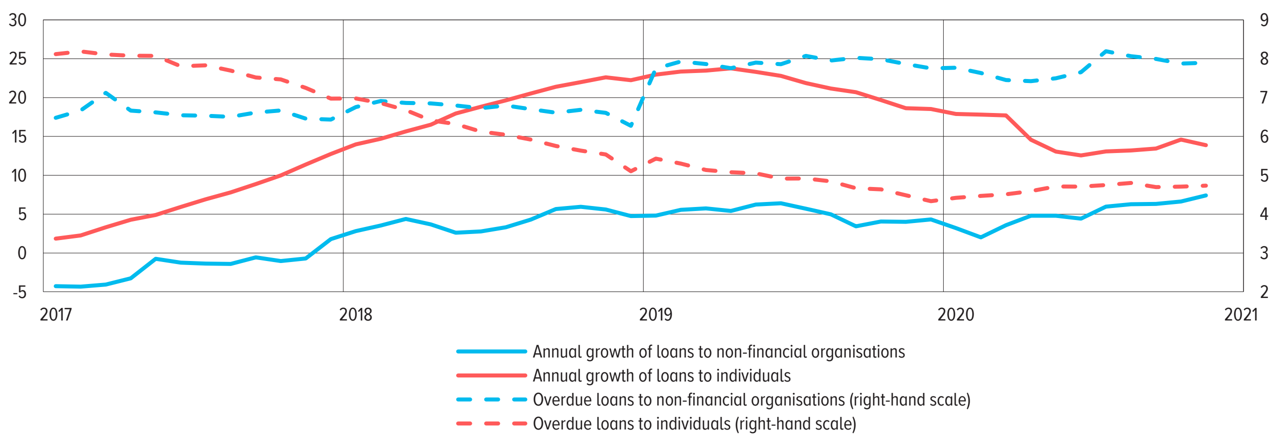


** Excluding escrow accounts.*
Source: Bank of Russia calculations.

CORPORATE LENDING CONTINUED A STABLE UPWARD TREND IN NOVEMBER

Chart 17

RUSSIAN CREDIT MARKET INDICATORS (%)

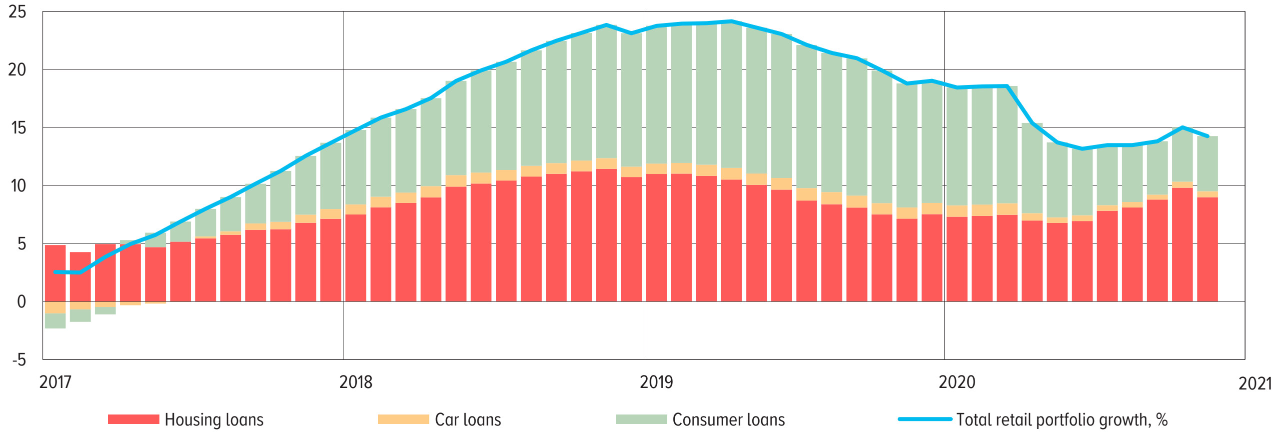


Source: Bank of Russia calculations.

RETAIL LENDING SLOWED DOWN IN NOVEMBER, PRIMARILY DUE TO MORTGAGE ASSET SECURITISATION TRANSACTIONS

Chart 18

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

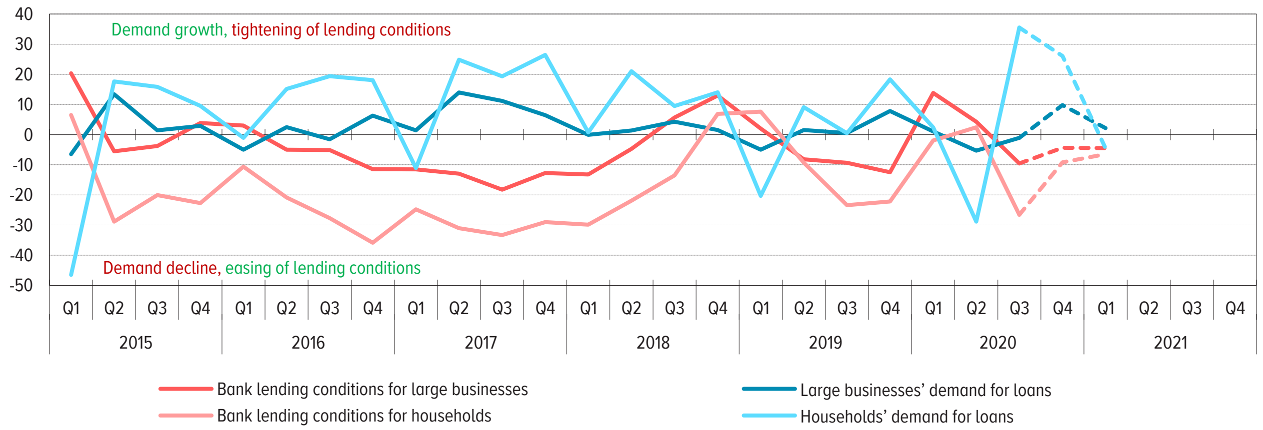


** For loans grouped into homogeneous loan portfolios.*
Source: Bank of Russia calculations.

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)

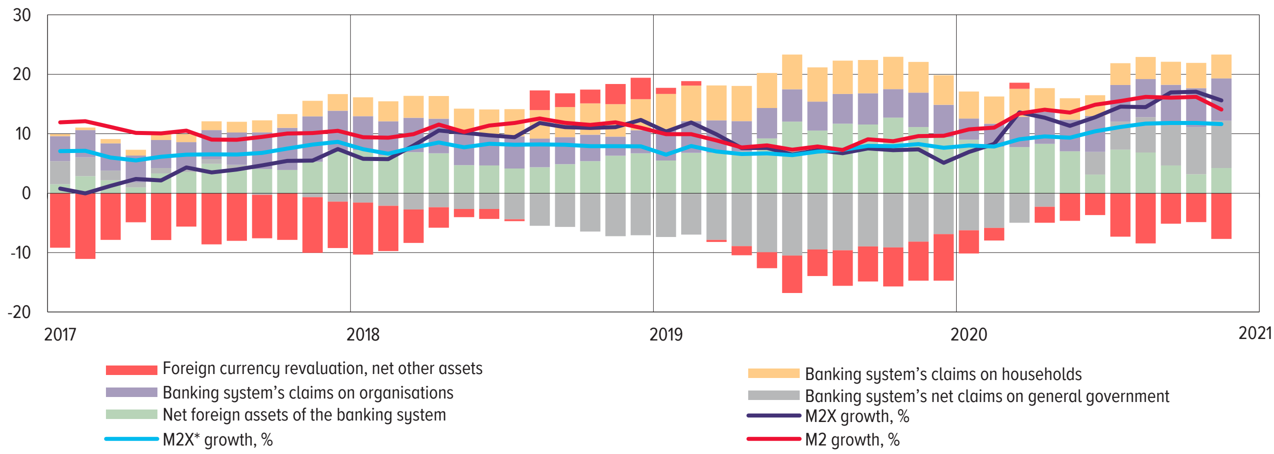


** The dotted lines signify respondent banks' expectations regarding changes in lending conditions and demand for loans in 2020 Q3.*
Source: Bank of Russia.

THE GROWTH OF MONEY SUPPLY SLIGHTLY DECLINED AS A RESULT OF FUNDS TRANSFERS TO BANKS' LIABILITIES NOT INCLUDED IN 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 6*

		August 2020	September 2020	October 2020	November 2020
Interest rates on banks' long-term ruble transactions					
– household deposits	% p.a.	4.1	4.1	4.1	4.2
– household loans	% p.a.	10.7	10.4	10.1	10.3
– corporate loans	% p.a.	7.0	6.8	7.0	-
Household deposits*	**% YoY, AFCR**	**5.0**	**4.5**	**3.4**	**3.0**
– in rubles*	% YoY	8.3	8.3	6.9	5.7
– in foreign currency	% YoY	-6.5	-8.6	-8.8	-6.6
– share of foreign currency*	%	21.0	21.9	21.9	21.4
Loans to non-financial organisations	**% YoY, AFCR**	**6.3**	**6.3**	**6.6**	**7.4**
– short-term (up to 1 year)	% YoY, AFCR	14.0	14.2	12.5	13.3
– long-term (more than 1 year)	% YoY, AFCR	4.1	4.1	5.0	5.6
– overdue loans	%	8.1	8.0	7.9	7.9
Household loans	**% YoY, AFCR**	**13.2**	**13.4**	**14.6**	**13.9**
– housing mortgage loans	% YoY, AFCR	16.6	18.6	22.0	20.8
– unsecured consumer loans	% YoY	9.5	8.9	9.1	9.2
– overdue loans	%	4.8	4.7	4.7	4.7
Banking system's claims on the economy	**% YoY, AFCR**	**9.3**	**9.3**	**9.8**	**10.2**
– on businesses	% YoY, AFCR	8.1	8.0	8.2	9.0
– on households	% YoY, AFCR	12.6	12.9	14.0	13.3
Money supply (M2 monetary aggregate)	**% YoY**	**16.2**	**16.1**	**16.2**	**14.1**
Broad money	**% YoY, AFCR**	**11.7**	**11.8**	**11.8**	**11.6**

** Excluding escrow accounts.*
Note: YoY – year-on-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 – 12.01.2021 (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 December 2020 – January 2021, this period is from 09.12.2020 to 12.01.2021);
- 'Foreign exchange and stock markets' section – 30.12.2020;
- 'Credit and deposit market' section – 01.12.2020.

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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