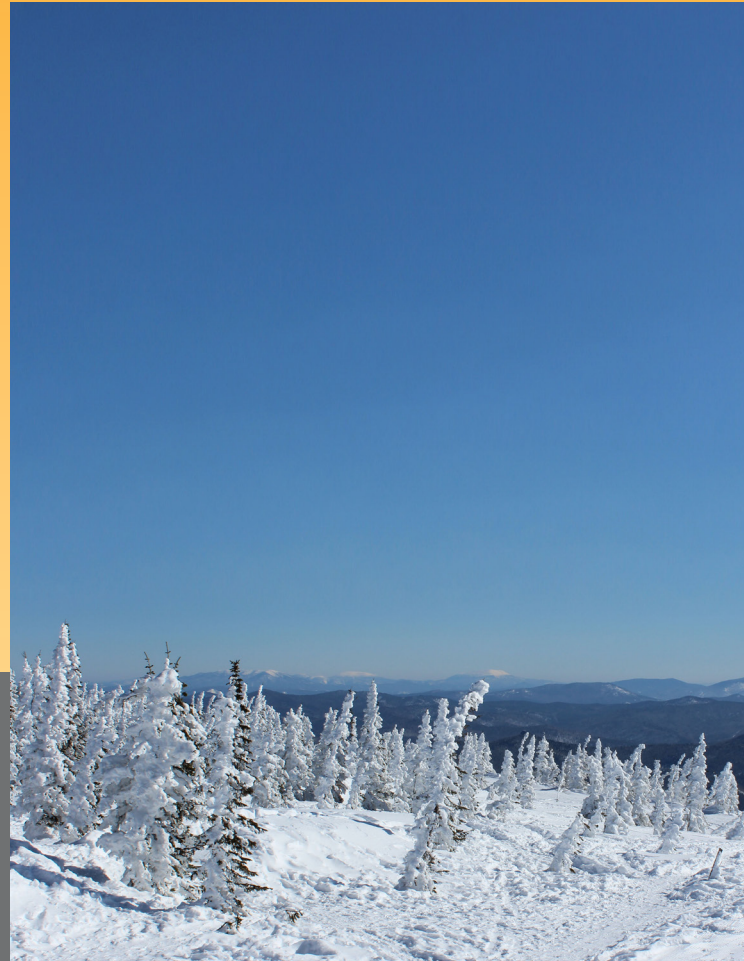




Bank of Russia



BANKING SECTOR LIQUIDITY AND FINANCIAL MARKETS

No. 1 (59) • January 2021

Information and analytical commentary

16 February 2021

BANKING SECTOR LIQUIDITY AND FINANCIAL MARKETS: FACTS, ASSESSMENTS AND COMMENTS (JANUARY 2021)

- In January, the structural liquidity deficit temporarily increased due to an outflow of budgetary funds and banks' delays in required reserves averaging. The inflow of funds into banks resumed at the beginning of February. As a result, the banking sector returned to a steady liquidity surplus by the middle of the month.
- In the first half of January, the average spread between interbank lending (IBL) rates and the Bank of Russia key rate turned positive as a result of the liquidity outflow under Federal Treasury (FT) operations. However, the increase in funds placements under FT operations resumed at the beginning of February and the spread returned to negative territory.
- The situation with foreign currency liquidity in the banking sector remained stable, including as a result of the considerable inflow of clients' funds in November.
- At the beginning of January, global financial markets continued to grow amid the news about the expansion of the stimulus plan to support the US economy. However, markets adjusted in the second half of the month on the back of the US Fed's announcement about a slowdown in the US economic recovery and the news about a potential delay in the approval of the stimulus plan.
- In December, interest rates on retail ruble deposits rose only slightly, driven by seasonal offerings in the short-term segment and higher federal government bond (OFZ) yields in the long-term segment. As before, households transferred their funds from time deposits to current accounts, while the growth of deposits for over three years continued. An inflow of funds into the foreign currency segment also promoted the increase in households' saving activity in December.
- In the last months of 2020, interest rates on corporate ruble loans were close to their record lows. The annual growth of loans granted to non-financial organisations slowed down a little, yet remained considerable.
- Low mortgage rates and extended mortgage loan maturities contributed to a further rise in mortgage lending, which was still the major driver of the increase in the retail loan portfolio.
- In December, a faster rise in claims on businesses supported the steady growth of money supply. The M2 and M2X aggregates demonstrated diverse trends in annualised terms, which was associated with the inflow of foreign currency deposits.

Banking sector liquidity and money market

Ruble liquidity. On average, the structural liquidity deficit in the January required reserve averaging period increased from zero to **0.1 trillion rubles** against the December averaging period. The liquidity deficit amounted to **0.8 trillion rubles** as of the beginning of February, after the liquidity surplus of 0.2 trillion rubles as of early January (Table 2). By the middle of February, the banking sector returned to a steady liquidity surplus which is expected to remain throughout the year.

The increase in the liquidity deficit was caused by banks' delays in required reserves

averaging, among other things. In the first half of the averaging period, the significant outflow of funds from banks was associated with the repayment of debt under FT operations. Expecting the resumption of these operations and the related liquidity inflow, some credit institutions delayed their required reserves averaging for the second half of the averaging period. As a result, they had to increase their balances in their correspondent accounts with the Bank of Russia by the beginning of February to comply with the established ratio, simultaneously reducing the amount of deposits as compared to the same period of the previous month.

Operations in the budget system's accounts were the key factor of the liquidity outflow in January. Budget revenues increased owing to a rise in the payments of main non-oil and gas taxes (quarterly VAT and profit tax, while personal income tax slightly declined) and social contributions. Budget spending rose year-on-year, yet remained seasonally low. A small inflow of funds was formed as a result of fiscal rule-based foreign currency purchases by Russia's Ministry of Finance, an increase in funds placed with banks by local governments, and coupon payments on OFZ bonds which exceeded the amount of government securities placements. However, in contrast to the expectations, there was no offsetting rise in the FT's placements of temporarily available budgetary funds over this period. This was the reason why the banking sector shifted to the structural liquidity deficit. The inflow of funds under FT operations resumed at the beginning of February. As a result, the banking sector returned to a steady liquidity surplus by the middle of the month. The situation is expected to remain unchanged in the next few months, with the surplus continuously growing.

After the New Year holidays, the amount of cash in circulation decreased, which is typical of this season. Nonetheless, the inflow of funds due to this factor was slightly smaller than in previous years, namely 0.2 trillion rubles against 0.4 trillion rubles in January 2020.

In 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 locally uneven liquidity distribution, as before. Banks' demand for these operations totalled 1.1 trillion rubles in January. Banks' investment in Bank of Russia coupon bonds (coupon OBRs) remained at the level of 0.6 trillion rubles in January.

The pandemic and related restrictions intensified the volatility of liquidity factors. This mostly affected the amount of cash in circulation, pushing it upwards. At the beginning of the year, changes in the structural liquidity surplus primarily depended on budget operations. Still, the Bank of Russia has all necessary instruments helping it mitigate the impact of these factors

on money market overnight rates and maintain them, as before, close to the key rate.

Money market. The spread between short-term IBL¹ rates and the Bank of Russia key rate equalled -8 bp (in the December averaging period: -3 bp; since the beginning of 2020: -8 bp) (Chart 3). The spread volatility rose to 26 bp (vs 7 bp in the December averaging period; since the beginning of 2020: 25 bp). In January, IBL rates formed primarily above the Bank of Russia key rate due to a rise in the demand for rubles in the IBL segment driven by the significant liquidity outflows under FT operations and the uncertainty about the time and amount of the resumption of these operations. Specifically, a range of market participants were forced to raise Bank of Russia loans at a fixed interest rate and increase borrowings in the IBL and FX swap segments. At the beginning of February, the FT offered 1.3 trillion rubles for placement on a net basis, following which the demand for liquidity in the market declined and the spread between IBL rates and the Bank of Russia key rate returned to negative territory.

Foreign currency liquidity. The interest rate spread in the FX swap and IBL (basis) segments contracted to +2 bp on average (vs -12 bp in the December averaging period; -17 bp over 2020) (Chart 4). The situation with foreign currency liquidity remained favourable, including owing to a significant inflow of foreign currency into the banking sector in November. Non-residents maintain a large amount of long ruble positions, offering rubles in the FX swap segment to receive foreign currency.

Structural liquidity surplus will remain throughout 2021. The quantitative parameters of the forecast of the structural liquidity balance will be adjusted with account of the updated macroeconomic forecast in February's issue of the Monetary Policy Report.

Key rate expectations. In January, amid faster inflation and increased volatility in financial markets, even more market participants expected the Bank of Russia to keep the key rate at 4.25% (at least for 2021 H1) (Table 1).

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

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

Table 1

1. Expectations based on market indicators,* interest rate (instrument)	March 2021	June 2021
– MosPrime 3M (FRA)	4.34 (4.15)	4.52 (4.39)
– RUONIA (ROISfix)	4.39 (4.36)	4.43 (4.47)
– RUONIA (futures)	4.57 (4.36)	4.50 (4.39)
2. Analysts' key rate expectations*	As of 31.03.2021	As of 30.06.2021
– Bloomberg survey	4.25 (4.25)	4.25 (4.00)
– Reuters survey	4.25 (4.25)	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 DEFICIT INCREASED IN JANUARY 2021
(START OF BUSINESS, BILLIONS OF RUBLES)

Table 2

	01.01.2017	01.01.2018	01.01.2019	01.01.2020	01.01.2021	01.02.2021
Structural liquidity deficit (+) / surplus (-)	736	-2,639	-3,016	-2,761	-204	756
Bank of Russia's claims on credit institutions	1,258	10	21	18	976	1,361
Auction-based facilities	216	-	-	-	847	1,154
– repos and FX swaps	-	-	-	-	847	1,154
– secured loans	216	-	-	-	-	-
Fixed interest rate facilities	1,042	10	21	18	129	207
– repos and FX swaps	632	4	8	13	118	0
– secured loans	411	5	13	5	10	207
Credit institutions' claims on the Bank of Russia	785	2,729	3,293	2,983	1,796	1,217
Deposits	785	2,372	1,902	1,026	1,221	662
– auction-based	397	2,125	1,478	697	844	554
– fixed interest rate	388	247	424	330	377	108
BoR coupon bonds	0	357	1,391	1,956	575	555
Standing reverse facilities, other than standard monetary policy instruments of the Bank of Russia*	263	81	256	204	616	611

* 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 STRUCTURAL LIQUIDITY SURPLUS FOR THE END OF 2021
(AS OF EARLY JANUARY 2021)
(TRILLIONS OF RUBLES)

Table 3

	2019 (actual)	2020 (actual)	January 2021	2021 (forecast)
1. Liquidity factors	0.5	-2.6	-0.3	[0.9; 1.4]
– change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	0.2	0.0	-0.5	[0.6; 0.9]
– change in the amount of cash in circulation	-0.1	-2.6	0.2	[0.4; 0.6]
– Bank of Russia interventions in the domestic FX market and monetary gold purchases**	0.4	0.1	-	-
– regulation of banks' required reserves with the Bank of Russia	0.0	-0.1	0.0	-0.1
2. Change in free bank reserves (correspondent accounts)*** (demand)	0.7	-0.1	0.7	[0.3; 0.4]
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	-0.3	-1.2	-0.6	[-0.9; -0.3]
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	-0.1	1.4	0.4	-1.4
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	-2.8	-0.2	0.8	[-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.

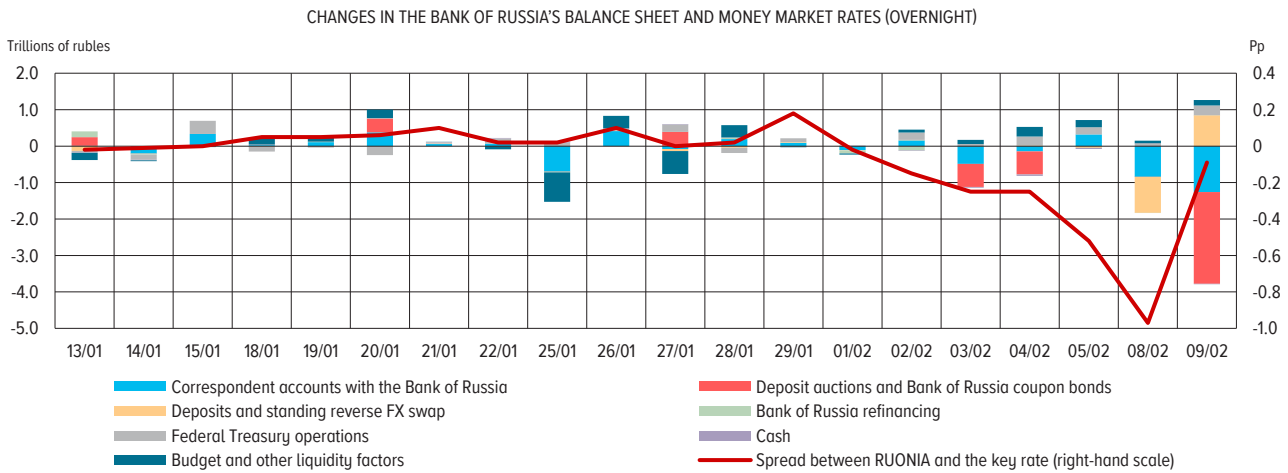
** Forecast values of the indicator are in line with the actual amount of operations conducted.

*** 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 AN OUTFLOW OF LIQUIDITY FROM THE BANKING SECTOR IN JANUARY 2021

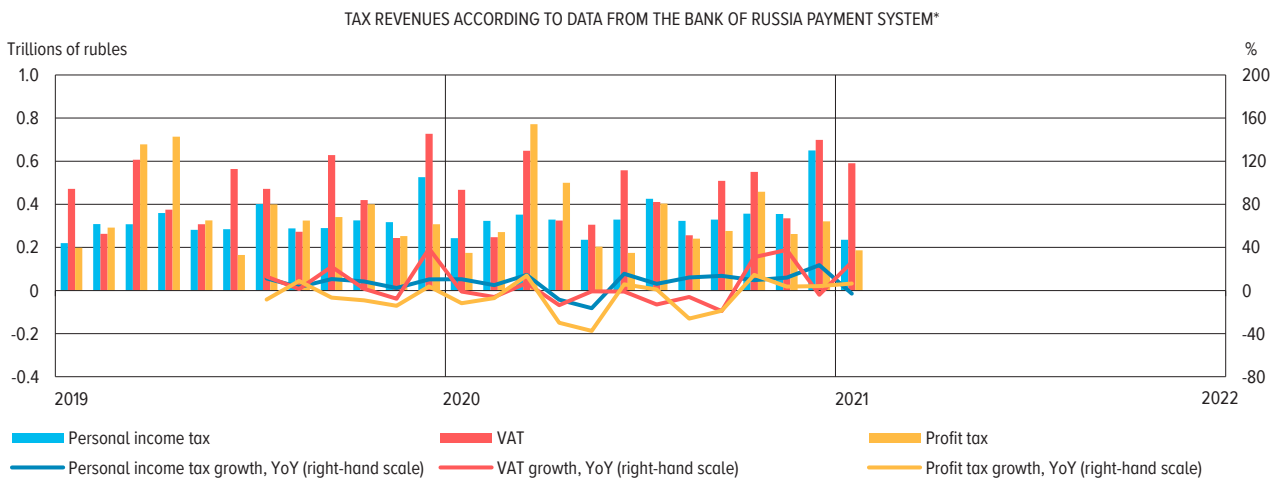
Chart 1



Source: Bank of Russia calculations.

THE RISE IN THE PAYMENTS OF VAT AND PROFIT TAX SPED UP IN JANUARY, 2021, WHILE PERSONAL INCOME TAX PAYMENTS DECREASED

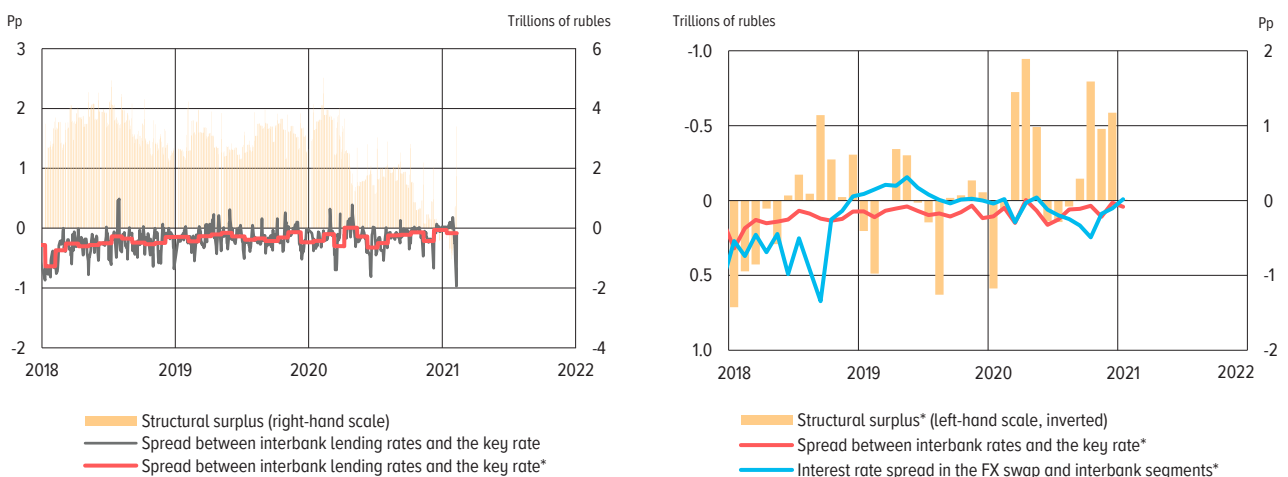
Chart 2



* 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

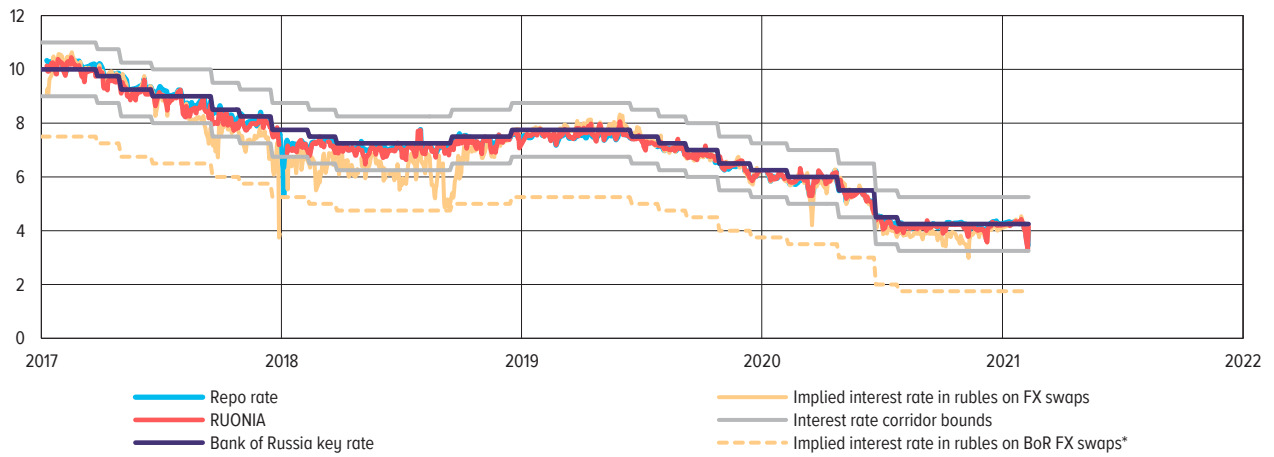
Chart 3



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

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

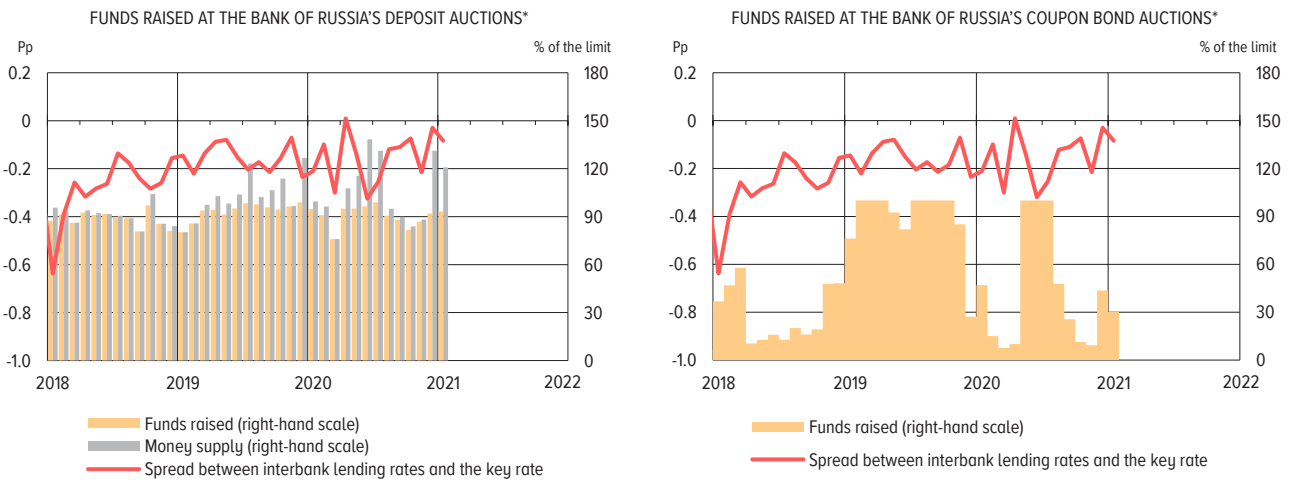
Chart 4



* 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 SLIGHTLY EXCEEDED THE ESTABLISHED LIMITS

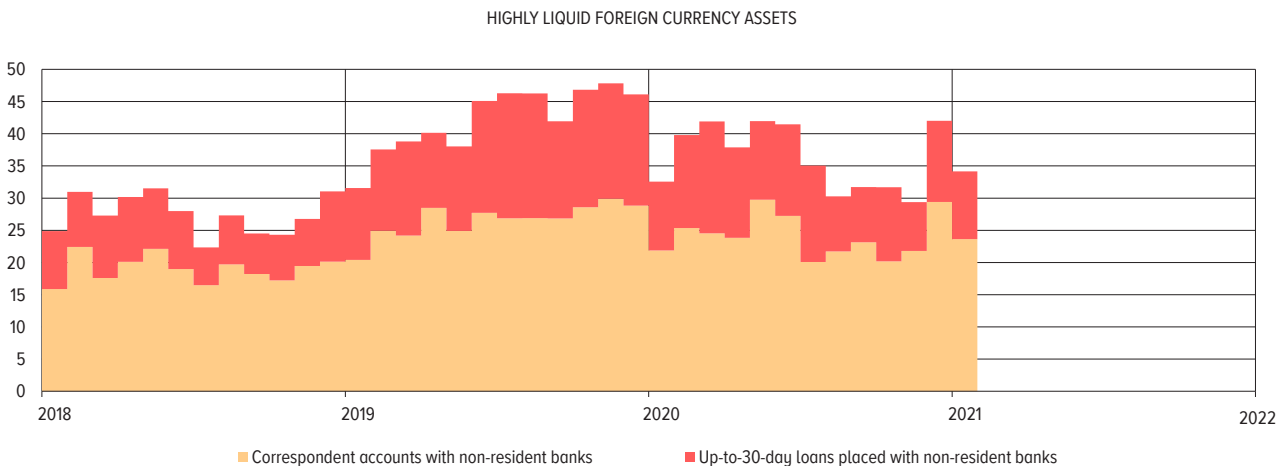
Chart 5



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

HIGHLY LIQUID FOREIGN CURRENCY ASSETS DECREASED IN DECEMBER (AS OF 1 JANUARY) (BILLIONS OF US DOLLARS)

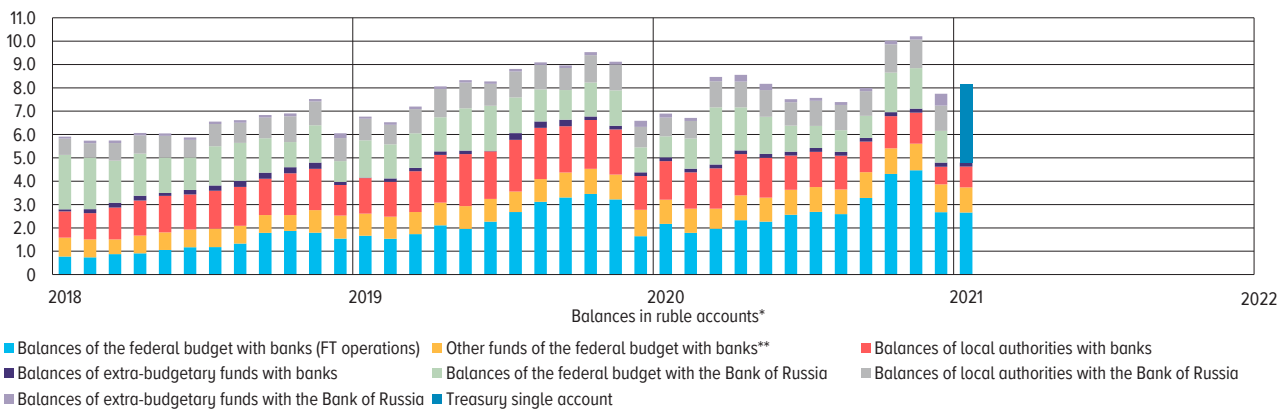
Chart 6



Source: Bank of Russia calculations.

BALANCES IN BUDGET ACCOUNTS WITH THE BANK OF RUSSIA (SINCE 2021 – TSA) WERE UP IN JANUARY 2021, DRIVEN BY AN INCREASE IN TAX REVENUES AMID SEASONALLY LOW BUDGET SPENDING
(TRILLIONS OF RUBLES, AS OF THE PERIOD-END)

Chart 7

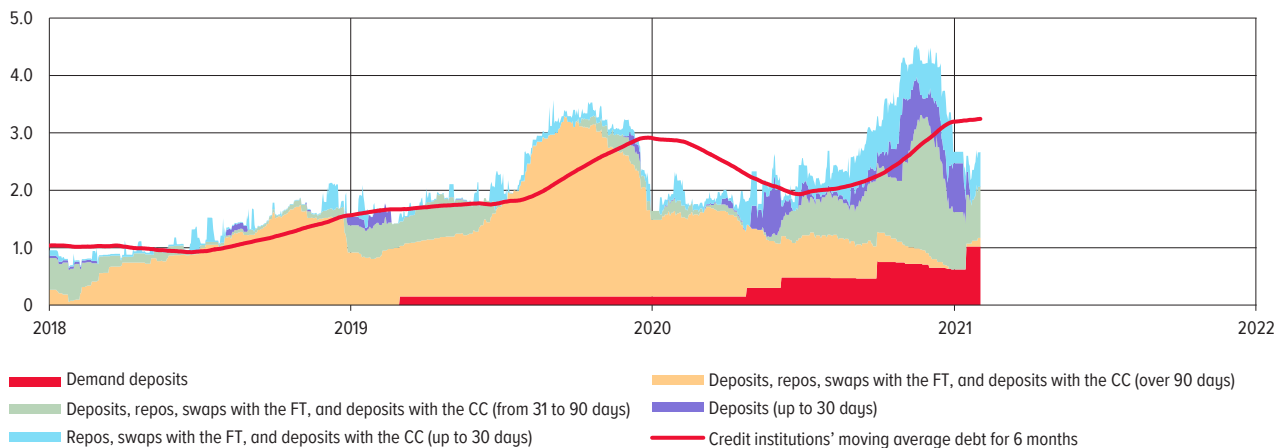


* According to banking reporting form 0409301 'Performance indicators of a credit institution' of the Bank of Russia's daily balance sheet.

** Other funds comprise VEB.RF budgetary funds, election commissions' funds, funds received for temporary use, funds for the cash transactions of Russia's Ministry of Finance, and others.
Source: Bank of Russia calculations.

CREDIT INSTITUTIONS' DEBT ON FT OPERATIONS IN JANUARY 2020 REMAINED THE SAME AS IN DECEMBER
(TRILLIONS OF RUBLES)

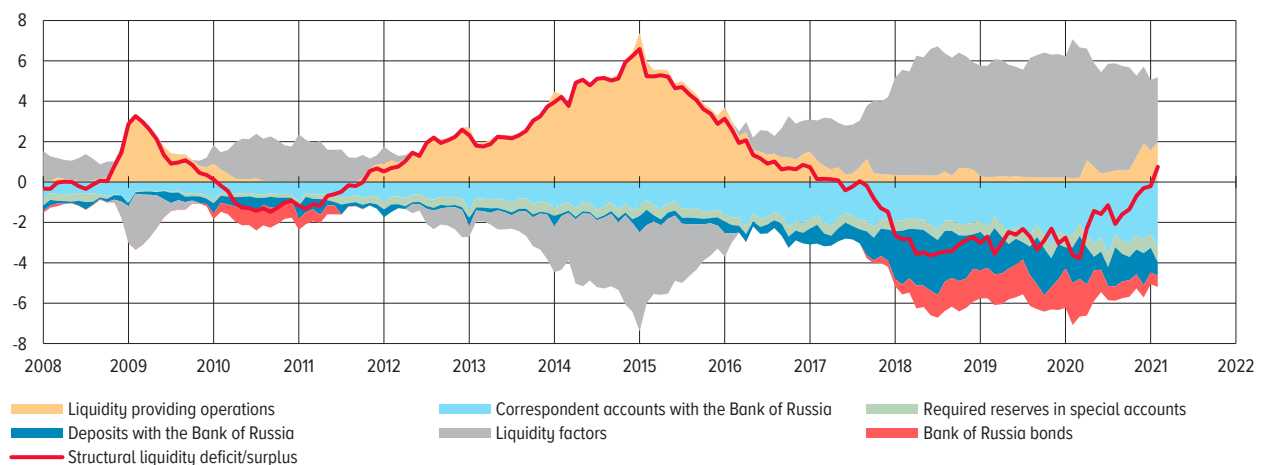
Chart 8



Sources: Federal Treasury, Bank of Russia calculations.

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

Chart 9



Source: Bank of Russia calculations.

Foreign exchange and stock markets

At the beginning of January, global financial markets continued to grow amid the news about the expansion of the stimulus plan to support the US economy to 1.9 trillion US dollars. However, markets adjusted in the second half of the month on the back of the US Fed's announcement about a slowdown in the US economic recovery and the news about a potential delay in the approval of the stimulus plan. Increased geopolitical risks put additional pressure on the Russian market.

Exchange rate. The ruble exchange rate fluctuated between 73 and 75 RUB/USD in the first half of January, but then started to weaken, just as other EMEs' currencies, amid growing geopolitical risks (Chart 10). At its lowest, the ruble declined to 76.50 RUB/USD – the exchange rate recorded at the end of November 2020. Overall, the ruble lost 1.8% over the month, and the EM Currency Index edged down by 1.5%. The Brazilian real (-4.9%), the Mexican peso (-3.4%), and the South African rand (-3.1%) depreciated most significantly.

Country risk premium. As of the end of the month, Russia's 5Y CDS spread increased by 7 bp to 97 bp, which is its highest since early November 2020 when markets were experiencing elevated volatility due to the US election (Chart 11). Just as in relation to the exchange rates, an even greater expansion of their spreads was recorded by Brazil (+31 bp), South Africa (+24 bp), and Mexico (+14 bp).

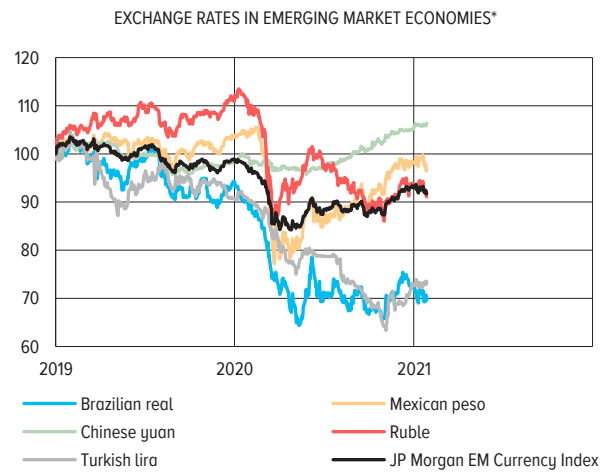
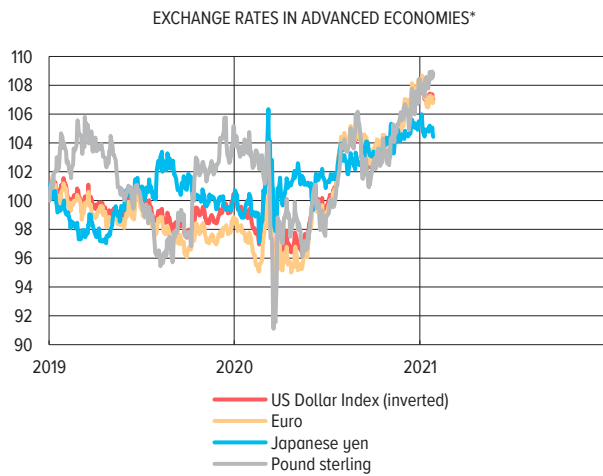
Federal government bonds. The OFZ yield curves on bonds continued to grow, reaching April–June 2020 levels as of the end of the month (Chart 12): OFZ 2Y – 4.35% (+17 bp), OFZ 5Y – 5.78% (+31 bp), and OFZ 10Y – 6.59% (+32 bp).

Long-term OFZ yields increased predominantly due to a rise in US treasury yields (+15 bp) resulting from elevated inflation expectations amid the news about the new stimulus plan to support the US economy. Besides, the end of the month recorded an outflow of foreign investors due to risk-off sentiment in global markets and increased geopolitical risks. Foreign investments in OFZ bonds totalled 28 billion rubles before 25 January, while after 25 January they decreased by 12 billion rubles. Short-term OFZ yields rose primarily owing to local factors, such as faster inflation and expectations that the Bank of Russia would not continue monetary policy easing in the near future. In this environment, Russia's Ministry of Finance reduced its issues, offering two OFZ-IN issues and two OFZ-PD issues over the month. No OFZ-PK issues (which were extensively placed in 2020 Q3 and Q4) were offered to investors. Eventually, total OFZ placements amounted to 61.1 billion rubles over the month, which is the lowest level since December 2018.

Stocks. During the last week of January, the risk-off situation was most notable in stock markets (Chart 13). In the majority of countries, the indices in national currencies declined by 3–7%. The VIX (volatility index) reached 37 points for the first time since early November 2020. As of the end of the month, the decrease in the indices was not so significant. Moreover, a range of economies even recorded a rise driven by risk-on sentiment at the beginning of the year. Having hit a new record high in early January, the MOEX index then receded, dropping by 0.4% as of the end of the month, and the RTS index lost 1.4%. The MSCI EM index was up by 3.0%, driven almost completely by the growth of the Chinese market (7.4%).

MOST CURRENCIES WEAKENED AGAINST THE US DOLLAR AT THE END OF THE MONTH
(02.01.2018 = 100)

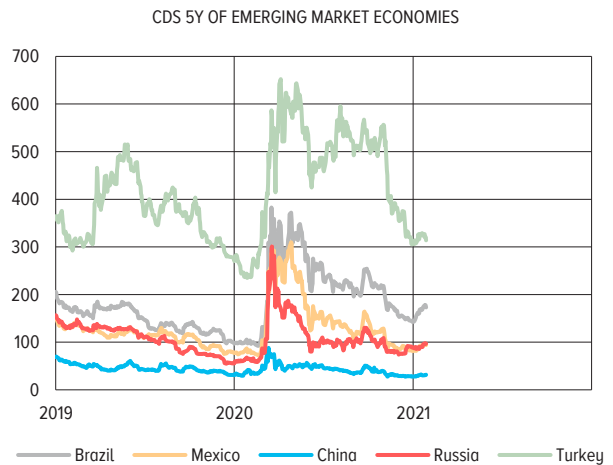
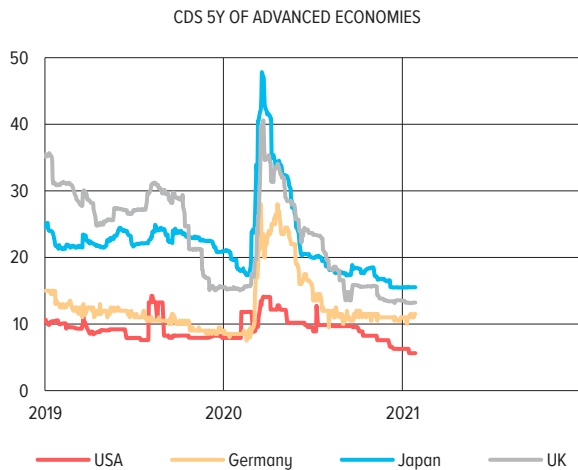
Chart 10



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

RUSSIA'S CDS SPREAD REACHED ITS NOVEMBER 2020 HIGH
(BP)

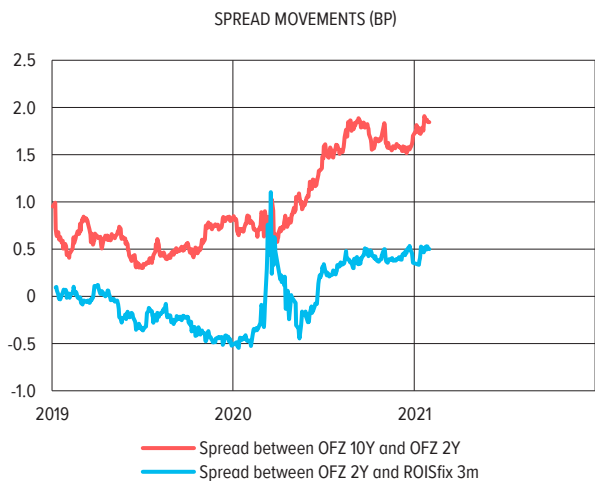
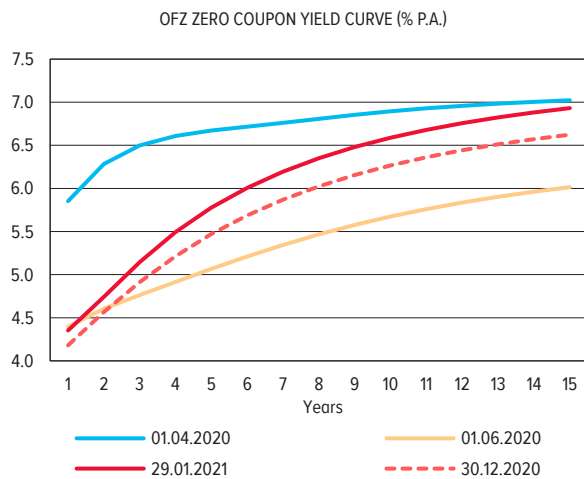
Chart 11



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

THE OFZ YIELD CURVE INCREASED TO APRIL–JUNE 2020 LEVELS

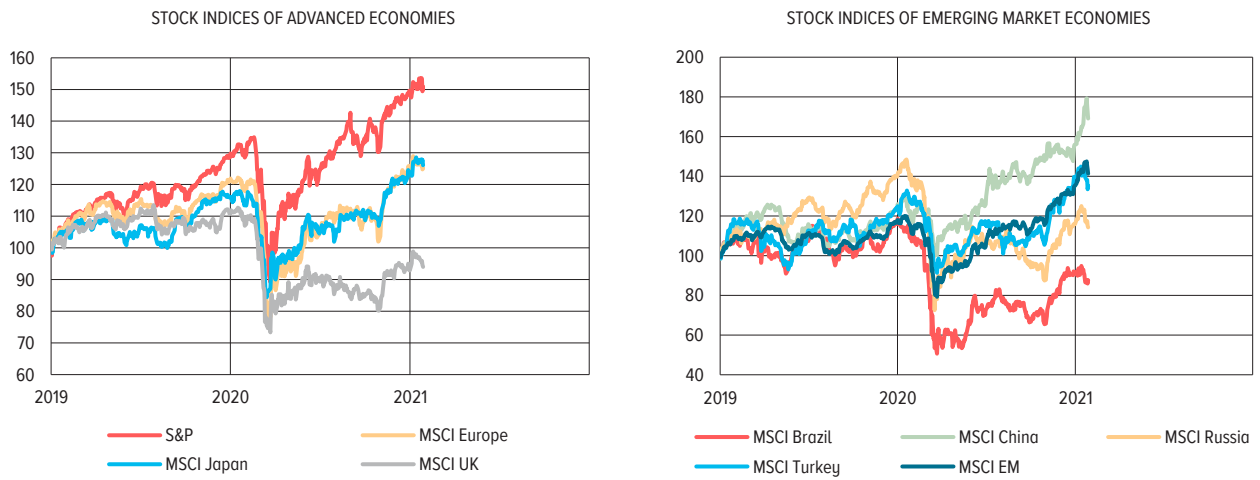
Chart 12



Source: PJSC Moscow Exchange.

STOCK MARKET SIGNIFICANTLY ADJUSTED AT THE END OF THE MONTH
(02.01.2018 = 100)

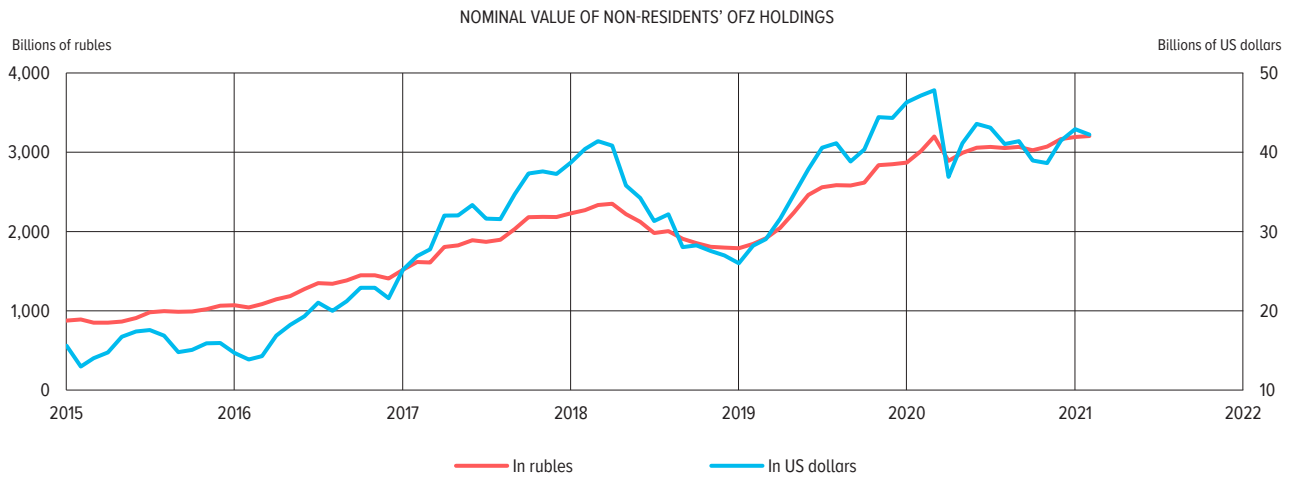
Chart 13



Sources: Bloomberg, Bank of Russia calculations.

FOREIGN INVESTORS' OFZ HOLDINGS REMAINED ALMOST THE SAME

Chart 14



Source: Bank of Russia calculations.

GOVERNMENT BOND YIELDS ROSE IN GLOBAL MARKETS

Table 4

Indicator		29.01.2021	1M	3M	6M	YTD	1Y
Russian financial market							
RUB/USD exchange rate		75.75	-1.8	4.8	-1.8	-1.8	-21.1
MOEX Index		3 277	-0.4	21.8	12.6	-0.4	4.7
RTS Index		1,368	-1.4	28.2	10.8	-1.4	-12.9
Government bond yield		6.14	38	30	56	38	6
Corporate bond yield		6.21	10	-11	25	10	-33
Regional bond yield		6.00	32	20	24	32	-34
CDS spread		97	7	-9	-8	7	31
RVI		35	3	-6	4	3	15
Exchange rates (per US dollar, % change, '+' – appreciation, '-' – depreciation)							
AEs*	US Dollar Index	90.58	0.7	-3.7	-3.0	0.7	-7.6
	Euro	1.21	-0.7	4.2	3.0	-0.7	10.2
	Japanese yen	104.68	-1.3	-0.1	1.1	-1.3	4.1
	Pound sterling	1.37	0.3	5.9	4.8	0.3	5.3
EMEs	JP Morgan EM Currency Index	57.07	-1.5	5.1	2.6	-1.5	-5.3
	Ruble	75.75	-1.8	4.8	-1.8	-1.8	-21.1
	Brazilian real	5.47	-4.9	5.1	-4.4	-4.9	-22.6
	Mexican peso	20.57	-3.4	2.9	8.2	-3.4	-9.2
	Chinese yuan	6.43	1.5	4.1	8.5	1.5	7.5
	Turkish lira	7.31	1.6	14.1	-4.7	1.6	-18.5
	South African rand	15.16	-3.1	7.1	12.5	-3.1	-3.7
10-year bond yield (% p.a., change in bp, '+' – increase, '-' – decrease)							
AEs	USA	1.07	15	19	54	15	-52
	Germany	-0.52	5	11	1	5	-14
	Japan	0.05	3	1	4	3	9
	UK	0.33	13	7	22	13	-19
EMEs	Russia	6.27	35	11	33	35	3
	Brazil	7.27	68	-37	100	68	80
	Mexico	5.59	6	-69	-12	6	-105
	China	3.18	4	0	22	4	19
	Turkey	12.93	0	-108	43	0	309
	South Africa	8.72	-1	-58	-51	-1	-28
5Y CDS spreads (bp, change in bp, '+' – increase, '-' – decrease)							
AEs	USA	6	-1	-3	-4	-1	-2
	Germany	11	0	1	-1	0	3
	Japan	16	0	-3	-3	0	-3
	UK	13	0	-2	-6	0	-2
EMEs	Russia	97	7	-9	-8	7	31
	Brazil	174	31	-44	-44	31	76
	Mexico	95	14	-33	-48	14	17
	China	32	4	-8	-11	4	-7
	Turkey	307	2	-245	-246	2	72
	South Africa	227	24	-50	-80	24	48
Stock indices (points, % change, '+' – increase, '-' – decrease)							
AEs	S&P	3,714	-1.1	13.6	13.5	-1.1	13.5
	MSCI Europe	1,813	-1.5	20.5	14.0	-1.5	2.8
	MSCI Japan	1,110	0.39	16.0	21.7	0.4	7.8
	MSCI UK	1,797	-0.7	15.1	8.1	-0.7	-16.1
EMEs	MSCI EM	1,330	3.0	20.5	23.2	3.0	21.1
	MSCI Russia	650	-2.8	28.7	7.6	-2.8	-20.0
	MSCI Brazil	1,727	-7.9	28.9	5.5	-7.9	-23.4
	MSCI Mexico	4,376	-4.2	21.6	26.0	-4.2	-12.6
	MSCI China	117	7.4	13.3	22.5	7.4	39.0
	MSCI Turkey	1,603,528	-5.2	24.9	20.8	-5.2	3.6
	MSCI South Africa	1,428	5.2	15.3	7.9	5.2	5.7

* Advanced economies.

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

Credit and deposit market

Deposit rates. In December, amid a moderate rise in returns on financial market instruments and banks' competition for depositors, the average interest rate on long-term¹ retail ruble deposits slightly adjusted upwards by 2 bp, to equal 4.17% p.a. The average-weighted interest rate on short-term ruble deposits rose more significantly (by 17 bp to 3.42%) owing to attractive seasonal offerings (Chart 15). The majority of banks did not change their interest rates in January. As a result, the average interest rate on retail deposits may be expected to hover around its current levels in the next few months.

As before, most banks kept their interest rates on retail foreign currency deposits close to their record lows in December, demonstrating their reluctance to expand their foreign currency assets and liabilities.

Deposit operations. The inflow of funds into retail deposits² sped up in December. The annual growth of the retail deposit portfolio edged up by 1.2 pp to 4.3% (Chart 16). As in previous months, amid the persistent uncertainty about the epidemic situation and the convergence of interest rates on deposits with various maturities, households continued to transfer their funds from time deposits of up to three years to current accounts. This was accompanied by the growth of balances in households' accounts, which is typical of December.

Although retail investors demonstrated high demand for savings alternatives and real estate investment (in December, balances in escrow accounts used for settlements under equity construction contracts increased by more than 171 billion rubles), the segment of deposits for over three years continued to expand. As of the end of December, the annual growth in this segment of the retail deposit market totalled 14.9%, up from 6.9% the month before.

Saving activity was also supported by foreign currency deposits as the pace of their annual

decrease considerably slowed down over the month from 6.6% to 4.6%. Nonetheless, the portion of foreign currency deposits in the retail portfolio contracted from 21.4% to 20.7% in December, including as a result of the ruble strengthening.

Credit rates. Interest rates on corporate³ ruble loans predominantly lowered in November 2020. According to the top banks participating in the quarterly bank lending conditions (BLC) survey, large companies' demand for loans remained weak (Chart 19). Amid the economic uncertainty caused by the coronavirus pandemic, banks remained cautious in selecting their borrowers, which boosted competition for reliable counterparties. As the cost of bank funding remained low, this enabled banks to leverage price competition mechanisms. In November, average interest rates on both short- and long-term corporate ruble loans decreased (Chart 15), reaching their new record lows (5.9% and 6.6% p.a., respectively). The average interest rate rose only in the segment of short-term ruble loans to small businesses. This could be associated with the scheduled termination of a range of lending support programmes predominantly aiding small and medium-sized enterprises (SMEs).

Banks pursued cautious credit policies in retail lending as well, which manifested itself in interest rate trends. In the mortgage segment characterised by lowest risks, interest rates on main ruble-denominated credit products were close to their record lows in December (5.8% p.a. in the market of housing under construction and approximately 8.0% in the market of finished housing). Fluctuations in the average market mortgage rate at the end of the year were largely caused by changes in the market structure.

In November–December, interest rates on ruble loans in higher-risk market segments (car and consumer lending) predominantly declined, while demonstrating increased volatility. Interest rates even rose in certain categories of transactions (for instance, the interest rate

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

on short-term car loans edged up by 6 bp in December as compared to October).

Loan rates may be expected to stay close to their current levels in the short run. Interest rate movements will be largely influenced by market structure fluctuations.

Corporate lending. In December, amid significant government expenditures, Russian companies were repaying short-term loans and settling overdue payments on bank loans. Therefore, the corporate loan portfolio contracted as of the end of the month. Short-term loan repayments were more considerable in December 2020 year-on-year. As a result, while staying close to its local highs, the annual increase in the portfolio of loans to non-financial organisations slightly slowed down as of the end of December to 7.0% against 7.4% in the previous month (Chart 17).

This downward trend of the loan portfolio was accompanied by changes in its structure. Reducing short-term borrowings, Russian companies continued to raise more long-term loans. Eventually, the trend observed in 2020 when short-term lending was rapidly increasing weakened, with the annual growth rate of the short-term loan portfolio declining considerably (from 13.3% to 10.6%) and that of long-term loans slightly rising (from 5.6% to 5.7%).

The corporate loan portfolio was expanding more slowly in both the ruble and foreign currency segments of the credit market. However, this slowdown was more notable in the foreign currency segment (2.7% as of the end of December against 3.4% as of the beginning of the month) than in the ruble segment (8.3% against 8.6%), which contributed to a further reduction in the portion of foreign currency loans in banks' loan portfolio.

Lending to SMEs demonstrated a substantial rise at the end of 2020, promoted by both support programmes for this category of borrowers (including long-term ones not related to anti-pandemic measures) and an increase in large companies' borrowings in the market of corporate bonds being an alternative source of borrowed funds.

In 2021 H1, a rise in the demand for loans expected by banks (Chart 19) will contribute to

a further increase in lending activity. Moreover, the share of foreign currency claims in the loan portfolio may be expected to gradually go down, with lending in the long-term segment of the market reviving.

Retail lending. In 2020 Q4, the annual growth of the retail loan portfolio hovered around the rate recorded as of the end of September (Chart 17). As of the beginning of 2021, it equalled 13.5%, which is slightly higher than three months before. Mortgage lending remained the major contributor to the growth of the retail segment of the credit market (Chart 18). In Q4, mortgage lending accounted for over three-fourths of the increase in the retail loan portfolio, despite large mortgage securitisation transactions limiting the growth of banks' mortgage loan portfolio.

By the end of the year, interest rates on mortgage loans dropped to their record lows. Therefore, the potential for their further decrease is limited. For this reason, competing for borrowers, banks were actively easing non-price lending conditions. In particular, the average maturity of a mortgage loan in December was 18.8 years, which is 0.5 years more than in September. Owing to extended loan maturities and low interest rates, borrowers are able to service larger loans. Coupled with a rise in housing prices, this pushed up the average amount of a ruble-denominated mortgage loan.⁴ In December, it rose to 2.6 million rubles, which is 5% more than in September.

Extended maturities and increased loan amounts, combined with still low mortgage rates, contributed to an unprecedented surge in mortgage lending. In December, banks granted more than 210,000 mortgage loans totalling over 560 billion rubles (the highest amount over the entire history of the Russian credit market).

As the portion of mortgage loans in the retail portfolio was expanding, this contributed to the extension of the average maturity of household loans (loans with longest maturities accounted for the entire annual growth of retail lending, while the portfolio of household loans for up to three years contracted by 7% as of the end of 2020). The portion of overdue loans in the

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

retail portfolio which had increased in mid-2020 receded in Q4 (Chart 17).

Higher-risk retail lending segments continued to show weak growth, which was associated with both persistently strict criteria for selecting borrowers and potential borrowers' rather cautious behaviour. The annual increase in car and unsecured consumer loans⁵ equalled less than 10% as of the end of the year.

Banks expect households' demand for loans to decline moderately at the beginning of 2021 and bounce back in the longer run (Chart 19). If the situation develops in line with this scenario, the portion of mortgage loans in retail lending may be expected to expand further. Accordingly, the share of overdue debt in claims on households will shrink in this case.

Money supply. In December, the annual growth of the banking system's claims on the economy⁶ sped up by 0.8 pp to 10.9%. This was primarily driven by an increase in claims on businesses, with their annual growth accelerating by 1.2 pp, to reach its five-year high of 10.2% (predominantly owing to ruble lending to financial and non-financial companies). Contrastingly, the annual rise in claims on households slowed down slightly (from 13.3% to 12.9%), partially because of mortgage asset securitisation transactions.

As funds continued to be transferred from deposits included in money supply into escrow accounts, other liabilities remained a major negative contributor to money supply dynamics in December. Nonetheless, as budget operations boosted money supply and lending to the economy was up, the annual growth of the M2X aggregate sped up by 1 pp to 12.6% in December (Chart 20). Conversely, the annual growth of money supply in the national definition (the M2 aggregate) slowed down from 14.1% as of the end of November to 13.5% as of the end of December, which was associated with the inflow of households' and businesses' foreign currency deposits.

As in previous months, non-financial companies' ruble deposits remain the key component of the M2 and M2X aggregates, with cash in circulation still significantly contributing to the increase in these monetary aggregates. Despite the increased amount of cash in circulation formed since the outbreak of the pandemic and its reduction beginning to emerge in November, the M0 aggregate demonstrated a seasonal increase in December, comparable with previous years' seasonal growth.⁷ In annualised terms, the rise in M0 remained almost the same against the previous month, equalling 29.7%.

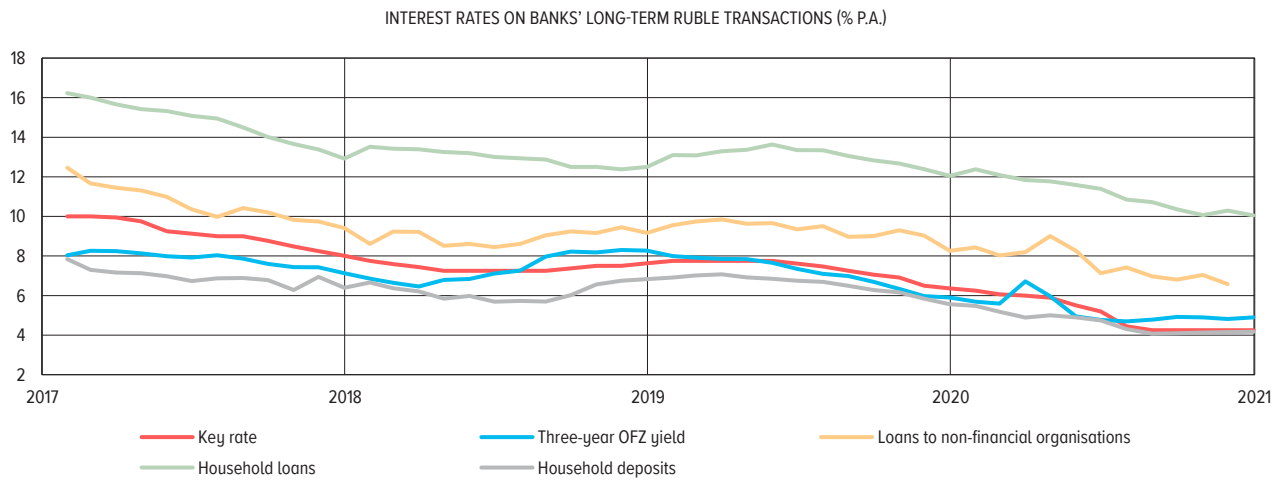
⁵ Standard loans grouped into homogeneous loan portfolios.

⁶ 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.

⁷ Refer to the information and analytical commentary *Banking Sector Liquidity and Financial Markets*, No. 12 (58), December 2020.

INTEREST RATES ON CORPORATE RUBLE LOANS ARE CLOSE TO THEIR RECORD LOWS

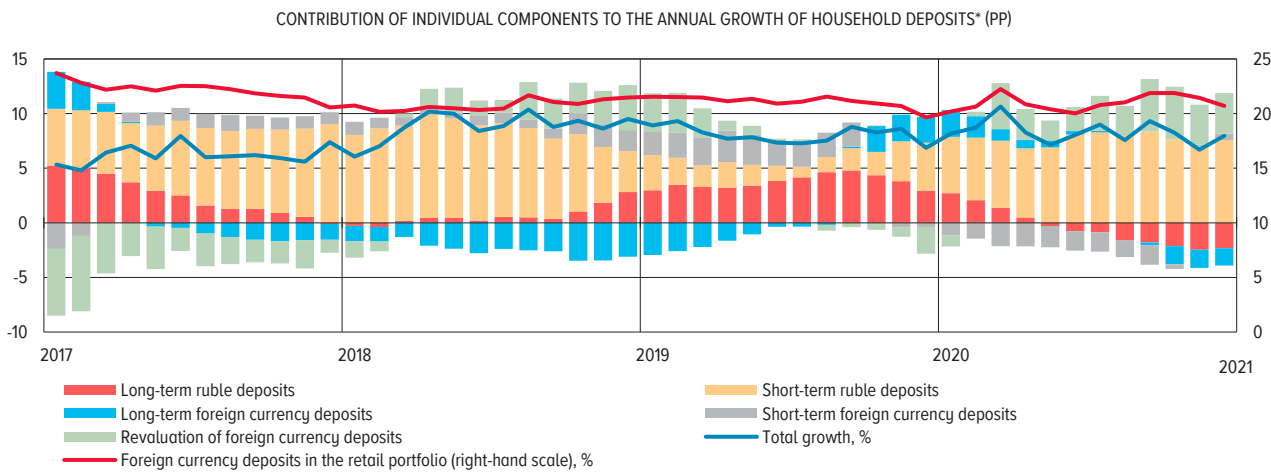
Chart 15



Source: Bank of Russia.

THE INFLOW OF HOUSEHOLDS' FUNDS INTO RUBLE ACCOUNTS AND FOREIGN CURRENCY DEPOSITS SPED UP IN DECEMBER

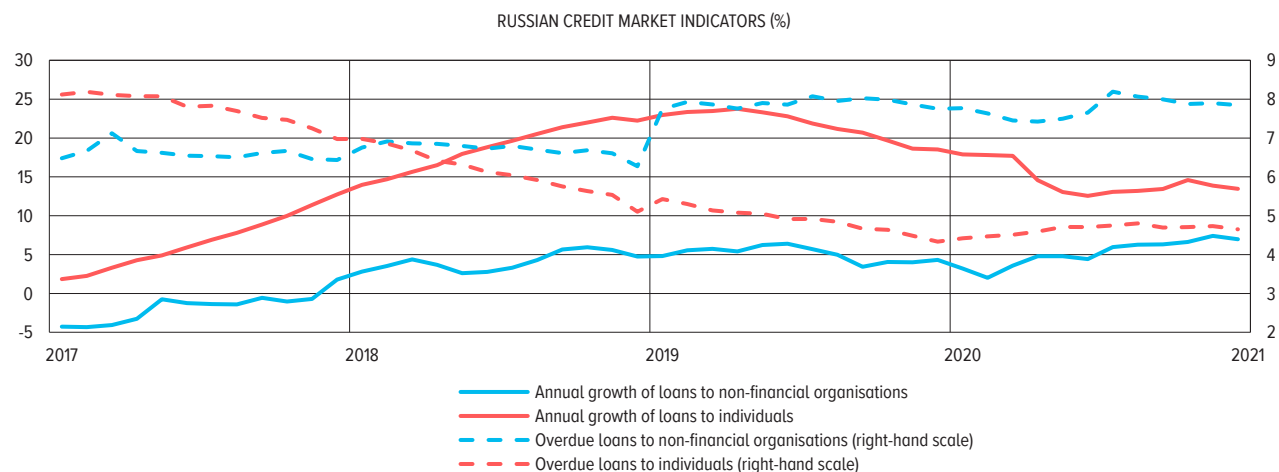
Chart 16



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

THE QUALITY OF LOAN PORTFOLIO IN BOTH RETAIL AND CORPORATE LENDING IMPROVED IN DECEMBER. THE ANNUAL GROWTH OF LENDING HOVERED AROUND THE RATE RECORDED IN RECENT MONTHS

Chart 17

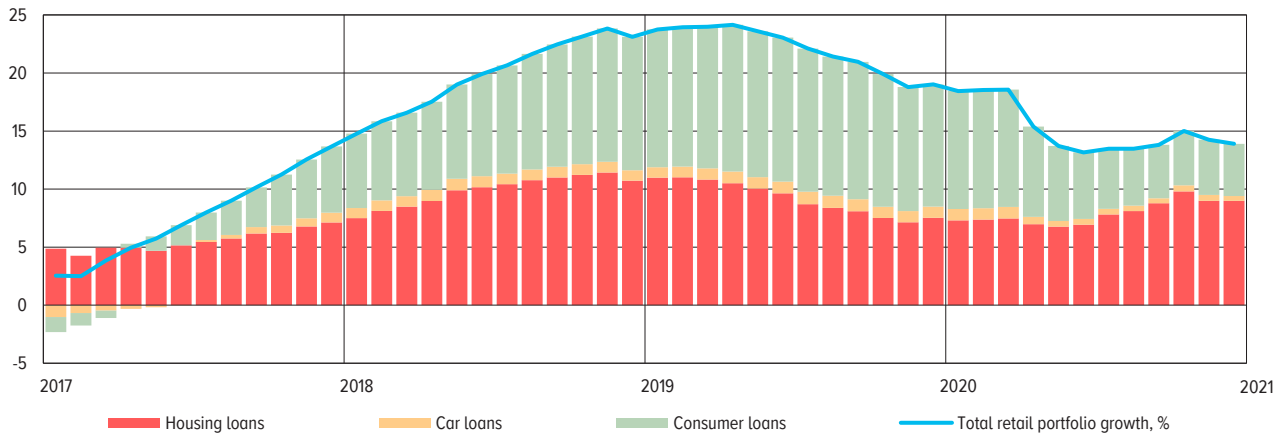


Source: Bank of Russia calculations.

MORTGAGE LOANS REMAINED THE MAJOR SOURCE OF RETAIL LENDING GROWTH AT THE END OF 2020

Chart 18

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

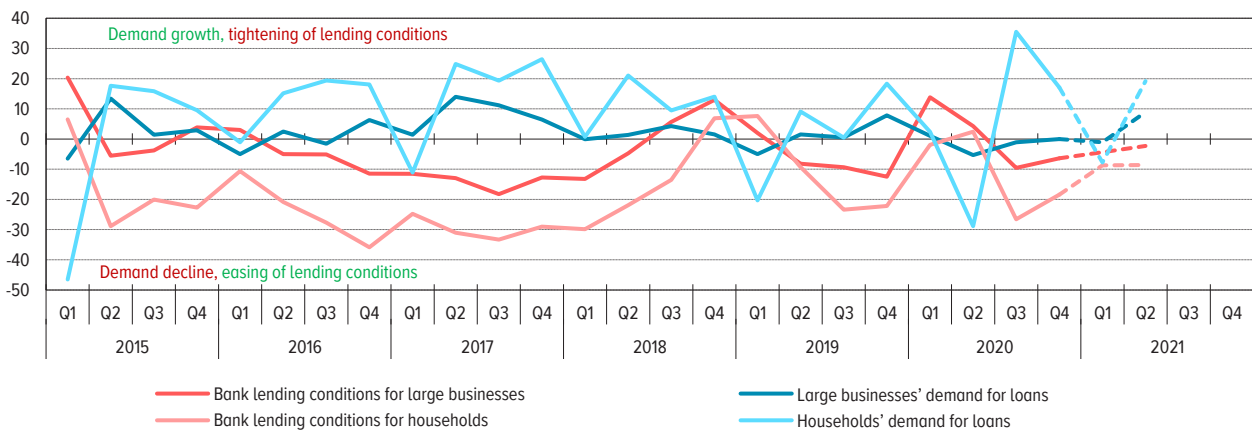


* For loans grouped into homogeneous loan portfolios.
Source: Bank of Russia calculations.

BANKS EXPECT MAIN BORROWER CATEGORIES TO RAISE THEIR DEMAND FOR LOANS BY MID-2021

Chart 19

INDICES OF LENDING CONDITIONS AND DEMAND FOR LOANS* (PP)

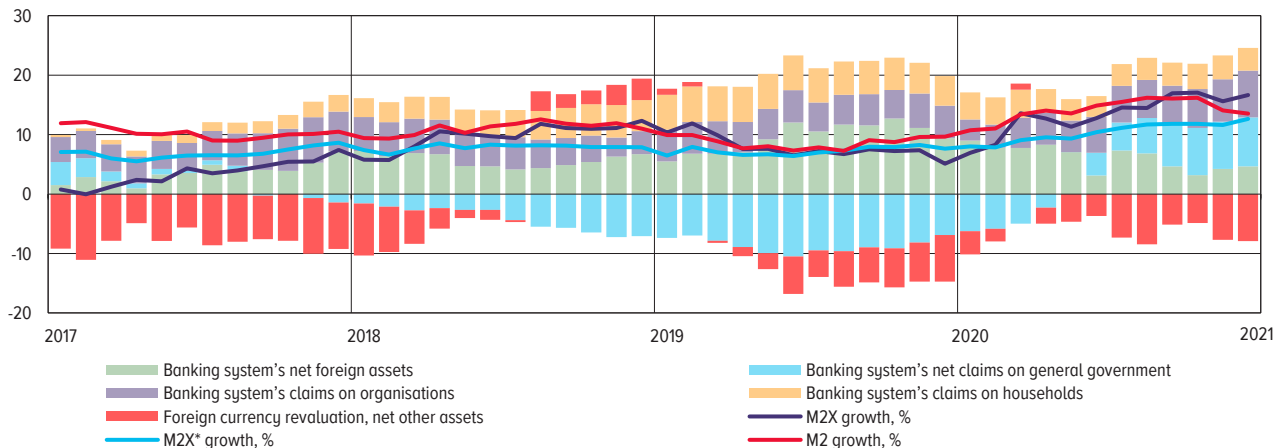


* The dotted lines signify respondent banks' expectations regarding changes in lending conditions and demand for loans in 2020 Q3.
Source: Bank of Russia.

MONEY SUPPLY GROWTH WAS SUPPORTED BY A FASTER RISE IN CLAIMS ON BUSINESSES

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

		September 2020	October 2020	November 2020	December 2020
Interest rates on banks' long-term ruble transactions					
– household deposits	% p.a.	4.1	4.1	4.2	4.2
– household loans	% p.a.	10.4	10.1	10.3	10.1
– corporate loans	% p.a.	6.8	7.0	6.6	-
Household deposits*	% YoY, AFCR	4.5	3.4	3.0	4.3
– in rubles*	% YoY	8.3	6.9	5.7	6.5
– in foreign currency	% YoY	-8.6	-8.8	-6.6	-4.6
– share of foreign currency*	%	21.9	21.9	21.4	20.7
Loans to non-financial organisations	% YoY, AFCR	6.3	6.6	7.4	7.0
– short-term (up to 1 year)	% YoY, AFCR	14.2	12.5	13.3	10.6
– long-term (more than 1 year)	% YoY, AFCR	4.1	5.0	5.6	5.7
– overdue loans	%	8.0	7.9	7.9	7.8
Household loans	% YoY, AFCR	13.4	14.6	13.9	13.5
– housing mortgage loans	% YoY, AFCR	18.6	22.0	20.8	21.2
– unsecured consumer loans	% YoY	8.9	9.1	9.2	8.8
– overdue loans	%	4.7	4.7	4.7	4.7
Banking system's claims on the economy	% YoY, AFCR	9.3	9.8	10.2	10.9
– on businesses	% YoY, AFCR	8.0	8.2	9.0	10.2
– on households	% YoY, AFCR	12.9	14.0	13.3	12.9
Money supply (M2 monetary aggregate)	% YoY	16.1	16.2	14.1	13.5
Broad money	% YoY, AFCR	11.8	11.8	11.6	12.6

* 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 – 09.02.2021 ((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 January–February 2021, this period is from 13.01.2021 to 09.02.2021);
- 'Foreign exchange and stock markets' section – 29.01.2021;
- 'Credit and deposit market' section – 01.01.2021.

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