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REGIONS | RUSSIA

ACCOUNT BALANCES SHOULD BE MANAGED PROPERLY

Analysis of intra-annual liquidity of the budgets of regions and municipalities

2021 was characterized by significant budget surpluses for Russian regions. Having analyzed preliminary data, ACRA assumes that the total surplus of unconsolidated budgets in 2021 may exceed RUB 430 bln. According to the latest available official reporting, in the first 10 months of 2021, the total surplus of the non-consolidated budgets of the regions of the Russian Federation amounted to a record RUB 1.2 tln.

Municipal entities also finished the first 10 months of last year with an overall surplus (RUB 137 bln, or around 9% of total tax and non-tax revenues), however, municipalities in 15 regions recorded a total intermediate deficit of just over RUB 6 bln. The Perm Krai and the Republic of Chuvashia accounted for more than half of this deficit (RUB 2.0 bln and RUB 1.5 bln, respectively).

Significant intermediate budget surpluses and the lack of need for regions to reduce debt¹ contributed to a cumulative increase in their account balances over the 10 months of 2021 by RUB 1.6 tln. Although Moscow provided for around 27% of growth, or around RUB 0.5 tln, according to preliminary data, as of the end of the year, the capital's budget was executed with a deficit. This means that account balances had declined as of the end of 2021.

Regions placed part of their accumulated funds in bank deposits, which increased the total volume of funds placed since the start of 2021 by approximately RUB 1 tln. The volume of deposits declined by RUB 0.1 tln over the same period in 2020, while in

¹ Commercial debt was partially refinanced using budget loans.

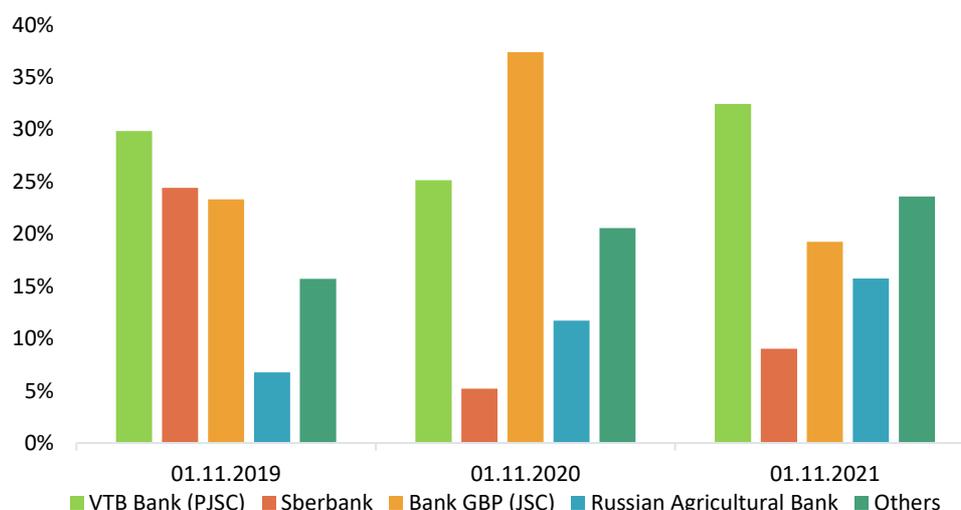
For further details, see ACRA's analytical commentary "Interest on account balance" from June 28, 2021.

2019 it increased by RUB 0.7 tln. Based on an analysis of various data², the volume of deposits of Russia's regions could be estimated at RUB 1.6–1.9 tln as of November 1, 2021. As expected, the regions that recorded the most growth of deposited financial assets include those with the highest increase of intermediate surpluses — Moscow, Saint Petersburg, the Moscow Region, and the Krasnoyarsk Krai.

It is noteworthy that regions started receiving interest income from transactions for managing funds in the single treasury account in 2021. This may have affected the quantity of deposits placed by regions, and, as a result, impacted the total volume of deposits (the size of deposits may have been more significant if this new type of income for regions had not been introduced).

As of November 1, 2021, most of the funds of regional authorities (RAs) had been deposited at the following banks: VTB Bank (PJSC)³ — 32%, Bank GBP (JSC)⁴ — 19%, and Russian Agricultural Bank⁵ — 16% (Fig. 1). As of November 1, 2021, Sberbank⁶ accounted for 9% of deposits placed by RAs, while in 2019 this indicator stood at 24%, placing the bank in second place among the three leaders — VTB Bank (PJSC), Sberbank, and Bank GBP (JSC) — which accounted for 78% of the portfolio of bank deposits of RAs. Sberbank's share over the past two years has fallen in favor of Russian Agricultural Bank, the share of which increased from 7% as of November 1, 2019 to 16% as of November 1, 2021, and a number of other banks who have increased their total share from 16% to 24% (including PJSC Sovcombank, the share of which increased from 2% to 6%⁷).

Figure 1. Leading banks in terms of volume of funds deposited by RAs



Sources: Bank of Russia, ACRA

Regions' budget surpluses for 10M 2021 and the federal center's policy aimed at substitution of the commercial debt of the regions with budget loans led to a decrease in the volume of bank loans issued to regional and municipal authorities (RMAs) by almost half compared to the beginning of 2021.

However, based on the preliminary data, almost a third of regions showed budget deficits in 2021, so, for some of these regions, the volume of bank lending could

² Comparison was carried out using the form of reporting of credit institutions aggregated by the Bank of Russia and the form of reporting on the execution of the consolidated budget of the regions of the Russian Federation formed by the Federal Treasury.

³ ACRA rating AAA(RU), outlook Stable.

⁴ ACRA rating AA+(RU), outlook Stable.

⁵ ACRA rating AA(RU), outlook Stable.

⁶ ACRA rating AAA(RU), outlook Stable.

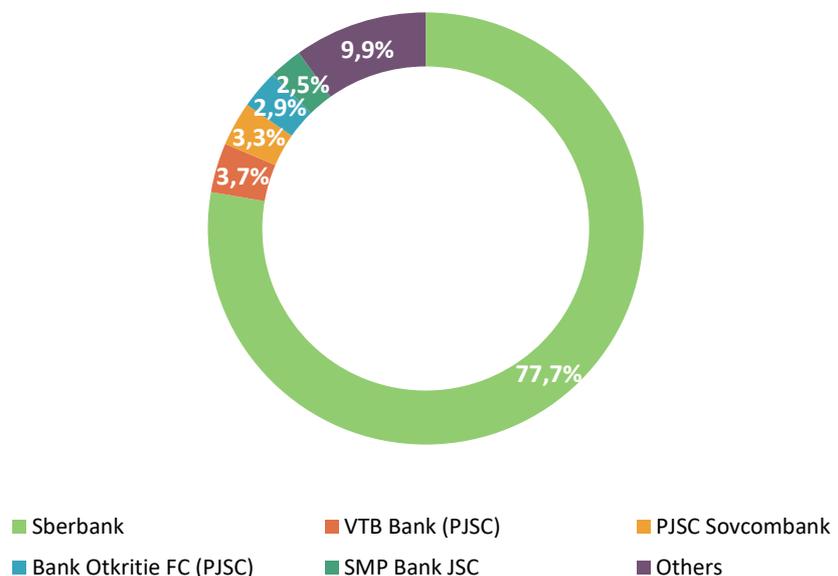
⁷ ACRA rating AA-(RU), outlook Stable.

partially recover. Nevertheless, the current situation is as follows: as of December 1, 2021, the total volume of bank loans issued to RMAs was just below RUB 0.4 tln, which is the lowest figure for at least the last six years. Moreover, as of the latest available date (November 1, 2021), the volume of bank deposits held by Russian regions exceeded their total debt to banks by more than four times for the first time in several years.

The share of short-term loans continued to increase in anticipation of an increase in the interest rate: as of November 1, 2021 (latest available data), loans due in up to six months accounted for 22% of the total debt of RMAs compared to 20% as of November 1, 2020 and 11% as of November 1, 2019. The share of medium-term bank loans issued for one to three years has decreased from 77% as of November 1, 2019 to 70% as of November 1, 2020 and 2021. The share of long-term loans issued for more than three years has also significantly decreased: from 11% (November 1, 2019) to 6% (November 1, 2021). All of these factors allow one to say that refinancing the commercial debt of RMAs with budget loans is a proactive measure on the part of the federal center.

Sberbank has long been the leader in lending to RMAs. As of November 1, 2021, its share in the total portfolio of these loans was 78%; VTB Bank (PJSC) accounted for about 4%, and PJSC Sovcombank, Bank Otkritie⁸ Financial Corporation PJSC and SMP Bank JSC took 3% each (Fig. 2). Despite the continued leadership of Sberbank, its share significantly decreased over 10M 2021 compared to the same periods in 2019 and 2020, when Sberbank issued about 86% of loans to RMAs.

Figure 2. Sberbank is the all-time leader in the share of loans issued to RMAs



Sources: Bank of Russia, ACRA

Against the backdrop of economic trends — growing revenues and liquidity, decreasing commercial debt — that are positive for regions and municipalities, there are signs that the financial position of a number of administrative entities could not be impacted by either the general favorable market conditions or the federal government's measures. In addition to intermediate deficits at regional or municipal level, this is evidenced by the persistence of overdue principal debt to banks. In absolute terms, this debt is insignificant (RUB 289 mln as of November 1, 2021) and is distributed among three banks, of which the largest share is due to Sberbank

⁸ ACRA rating AA(RU), outlook Stable.

(RUB 147 mln). Judging by the small volumes of the debt, it can be assumed that the debt falls on municipalities. Over the past two years, the maximum amount of overdue debt of RMAs to banks was recorded on November 1, 2020, when its total amount increased to RUB 344 mln from RUB 180 mln as of the beginning of the year. The Russian Ministry of Finance obliged the regions participating in the commercial debt restructuring program to report on the ratio of the total debt obligations on market borrowings of a region and its municipalities to the region's consolidated budget revenues (excluding transfers)⁹. Regions may decide on the volume of budget loans to be transferred to municipalities on the same terms. According to ACRA's estimates, as low as around RUB 20 bln (or 6% of the total debt/10% of commercial debt of municipalities as of December 1, 2021) was transferred to municipalities from higher budgets.

Given the low volume of substitution, the level of market borrowing by municipalities in some cases may become an obstacle to the fulfillment of the ratio prescribed by the Russian Ministry of Finance as the volume of commercial debt of municipalities is approaching a quarter of the commercial debt of the regions (excluding federal cities). Municipalities are not as transparent in their reporting disclosures as regions, so it is often impossible for an outside observer to draw reliable conclusions based on available data. As a result, public monitoring of the credit quality of municipalities may become more relevant in the near future and may require greater data transparency and openness.

⁹ Clause 7 (a) of Resolution of the Government of the Russian Federation No. 1206 dated July 15, 2021.

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