

MONITORING OF RUSSIA'S ECONOMIC OUTLOOK

trends and challenges
of socio-economic development

Gaidar Institute



25(198) NOVEMBER 2025

FEATURES AND RISKS OF THE FEDERAL BUDGET DRAFT FOR THE NEXT THREE YEARS

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The draft federal law “On the Federal Budget for 2026 and the Planning Period of 2027 and 2028” (hereinafter referred to as the Bill) was adopted in its second reading on November 18th. This issue of the monitoring attempts to assess the risks of meeting the revenue and expenditure targets envisaged in the budget, their impact on the Russian economy, and their significance for medium-term budgetary sustainability.

In 2026, federal budget revenues are expected to exceed 2025 levels by Rb 3.2 trillion in nominal terms, while remaining at the same level as a share of GDP (17.1% of GDP). According to forecasts by the Russian Ministry of Finance, budget revenues will decline to 16.6% of GDP by 2028. This decline is due to the downward trend in oil and gas revenues from 4% of GDP in 2025 to 3.5% of GDP in 2028, while non-oil and gas revenues in 2026–2028 are projected to be in the range of 13.3–13.1% of GDP, respectively. Thus, the draft law provides for a further reduction in the budget's dependence on raw materials (the non-oil and gas deficit will decrease to 4.8% of GDP in 2028 instead of the expected 6.6% in 2025).

The volume of oil and gas revenues in 2026–2028 will be impacted primarily by energy price dynamics and, to a lesser extent, by the introduction of a tax deduction on excess profit tax (EPT) for highly developed subsoil plots commencing in 2027 and the extension of price differentials and fuel damping mechanism parameters. The estimates presented in the Bill for oil and gas revenues amounting to 3.8% of GDP in 2026, with a subsequent reduction to 3.5% of GDP by the end of 2028, appear to be overly conservative. According to our estimates, oil and gas revenues in 2026–2028 are more likely to amount to Rb9.2–9.3–9.9 trillion, respectively.

According to the Bill, the total level of non-oil and gas revenues to the federal budget as a share of GDP is expected to increase by 0.2 p.p. to 13.3% of GDP in 2026, stabilize at this level in 2027, and then decrease by 0.2 p.p. to 13.1% of GDP in 2028. A key change in non-oil and gas revenues is an increase in

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Table 1

Key parameters of the federal budget, Rb bn

Indicator	2024 (report)	2025 (estimate)	2026 (Bill)	2027 (Bill)	2028 (Bill)
Revenues including:	36 709	37 085	40 283	42 910	45 869
<i>in % of GDP</i>	<i>18.2</i>	<i>17.1</i>	<i>17.1</i>	<i>16.8</i>	<i>16.6</i>
Oil and gas	11 131	8 654	8 918	9 050	9 705
<i>in % of GDP</i>	<i>5.5</i>	<i>4.0</i>	<i>3.8</i>	<i>3.5</i>	<i>3.5</i>
Non-oil and gas	25 578	28 431	31 365	33 860	36 164
<i>in % of GDP</i>	<i>12.7</i>	<i>13.1</i>	<i>13.3</i>	<i>13.3</i>	<i>13.1</i>
Expenditure	40 181	42 821	44 070	46 096	49 383
<i>in % of GDP</i>	<i>20.0</i>	<i>19.7</i>	<i>18.7</i>	<i>18.0</i>	<i>17.9</i>
Deficit (-) / Surplus (+)	-3 472	-5 736	-3 787	-3 186	-3 514
<i>in % of GDP</i>	<i>1.8</i>	<i>2.6</i>	<i>1.6</i>	<i>1.2</i>	<i>1.3</i>
Non-oil and gas deficit	-14 603	-14 390	-12 705	-12 236	-13 219
<i>in % of GDP</i>	<i>7.3</i>	<i>6.6</i>	<i>5.4</i>	<i>4.7</i>	<i>4.8</i>

Source: Bill.

the VAT tax burden (due to an increase in the rate to 22% and a reduction in the threshold for the simplified taxation system (STS) and patent from January 1, 2026). As a result, the share of VAT revenues in the structure of non-oil and gas revenues of the federal budget is projected to grow from 52% in 2025 to almost 58% in 2028. At the same time, the forecast of a Rb1.4 trillion increase in VAT revenues as a result of the proposed changes seems overly optimistic in our view, as it assumes not only the best possible dynamics of key macroeconomic variables, but also continuous growth in VAT collection. In addition, when forecasting the net fiscal effect of these tax innovations on the budget, it is necessary to take into account the possible consequences of a decline in the purchasing power of business and household income, including a potential reduction in income tax revenues to the federal and regional budgets, insurance contributions, and personal income tax revenues due to a reduction in the wage fund. One of the long-term effects may be the risk of a slowdown in the pace of reduction of the Central Bank of Russia's key rate, which will increase the cost of new borrowings for the Russian Ministry of Finance.¹

Another important source of revenue in 2026–2028 is corporate income tax. The only significant change worth noting is the continuation of restrictions on loss carry-forwards until 2030 (the tax base for the current period cannot be reduced by more than 50% by the amount of losses incurred in previous tax periods). It should be noted that the trend towards a reduction in the corporate income tax base commenced in 2024: the balanced financial result (profit minus loss) of organizations (excluding SMEs, credit and non-credit financial organizations, state (municipal) institutions) in current prices decreased by almost 7% relative to the 2023 level, which in real terms means a drop of more than 16%. Given the processes observed in the Russian economy, this trend is not only continuing but also has all the prerequisites for acceleration in 2025. In particular, according to the results of January-June 2025, based on available

¹ For more details on the possible budgetary effect of legislative innovations in VAT, see: No. 24(206) October 2025 "Monitoring the economic situation in Russia: trends and challenges of socio-economic development."

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operational data from Rosstat,¹ the balanced financial result in current prices amounted to 91.6% compared to the same period last year. Therefore, the shortfall in the initially planned income tax revenues in 2025 is already quite obvious. Moreover, scientific literature notes that the increase in income tax worsens the long-term profitability estimates of Russian companies using the general taxation regime, which in conditions of recession or near-zero economic growth in the country may lead to a gradual reduction in the tax base in real terms at a rate greater than the increase in the tax rate can compensate for.

It is worth noting that the cost of bank lending, which will remain at “unsuitable for investment” levels in 2026 against the backdrop of a general economic slowdown, a contraction in demand and a shift towards “cheaper” products, increased corporate debt servicing costs, and the possibility of partial loss carry-forward (the amount of which will increase significantly by the end of 2025) will put pressure on the profits of profitable organizations and lead to a decline in investment in the Russian economy, even compared to 2025. Taking these factors into account, our forecast for income tax revenues in 2026 is Rb90 bn less than the estimates of the Russian Ministry of Finance included in the federal budget. Naturally, it should be borne in mind that a reduction in income tax revenues to the federal budget automatically means similar problems with collection at the regional level.

Federal budget expenditures in 2026 are expected to increase slightly by Rb1.3 trillion, or 2.9% in nominal terms, compared to the current year. At the same time, as a share of GDP, expenditures in 2026 will decrease by 1 p.p. to 18.7% of GDP compared to 2025. In 2027–2028, expenditures will grow at rates of 4.6% and 7.1%, respectively, in nominal terms, while as a share of GDP, expenditures are expected to decline to 17.9% of GDP in 2028.

It should be noted that for the upcoming three-year period, the requirement to maintain the primary structural balance of the federal budget will be implemented, which is a continuation of the positive practice of the previous budget cycle. Meanwhile, it should be noted that revising federal budget expenditures upward during the budget execution process without an equivalent increase in revenue sources could ultimately lead to a violation of budget rules, rendering their application practically useless.

The emerging trends in the change in the structure of federal budget expenditures are noteworthy (*Fig. 1*).

As can be seen in *Fig. 1*, there has been a steady increase in the share of conditionally unproductive expenditures. This primarily concerns defense expenditures, whose share increased from 23.9% in 2021 to 40.3% in 2025 and, according to the Bill, will remain at an elevated level thereafter (38.2% in 2026). This indicates a systemic reorientation of budget resources towards ensuring the country's security and defense capabilities. Meanwhile, spending on the national economy is set to decline from 17.6% in 2021 to 10.9% in 2025–2026, reflecting a weakening of the budget's investment-stimulating function. There is also a decrease in the share of social spending, from 38.1% in 2021 to 25.1% in 2026. Despite the preservation of their nominal priority, the share of fixed obligations in the structure of federal budget expenditures is increasing, which reduces the flexibility of budget policy. In addition, the doubling of the share of interest payments over a relatively short period of time, from 4.4% in 2021

1 On the financial results of organizations in January-June 2025 // Federal State Statistics Service (Rosstat). URL: https://rosstat.gov.ru/storage/mediabank/130_27-08-2025.html.

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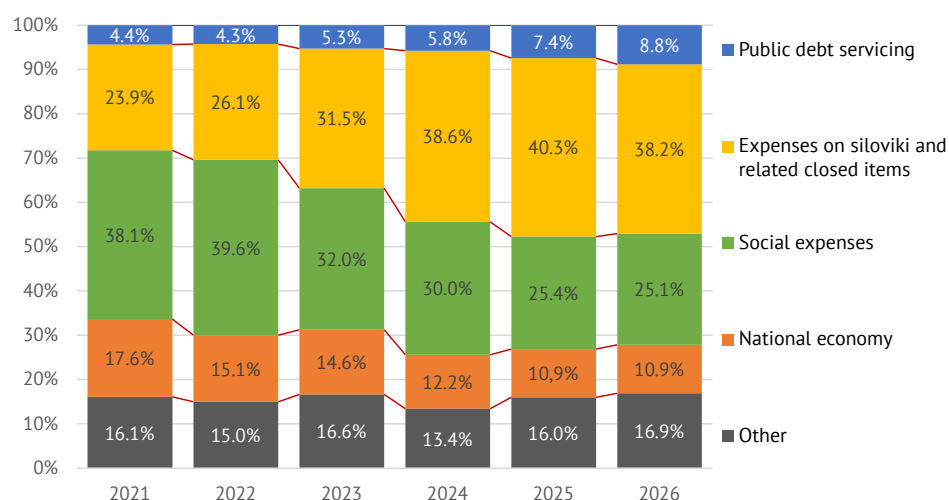


Fig. 1. Changes in the structure of federal budget expenditures in 2021–2026, %

Source: own calculations.

to 8.8% in 2026, is a cause for concern. As is well known, increased spending on servicing the national debt reduces the scope for budgetary maneuvering within non-interest expenditures, limiting the state's ability to finance strategic priorities in the economy.

The federal budget will remain in deficit throughout the three-year period, but the annual budget deficit will decline from 1.6% of GDP in 2026 to 1.2% of GDP in 2027, followed by an increase to 1.3% of GDP in 2028. This deficit is quite comfortable for maintaining long-term fiscal sustainability, but it depends primarily on the implementation of the revenue plan.

Domestic government borrowing will be virtually the only source of financing for the federal budget deficit in 2026–2028. The Russian Ministry of Finance plans to raise net borrowings (excluding repayments) from the market in the amount of Rb4.0–4.7 trillion annually over the next three years. The structure of public debt by source of borrowing will not change significantly: the share of domestic debt will be 88% in 2028. The planned volume of borrowing is not particularly significant in terms of increasing the debt burden given the projected economic growth rates. At the same time, the expansion of the practice of, in essence, indirect issuance financing of public debt by the Central Bank of the Russian Federation (increasing the volume of OFZs in the bank's assets as a result of repo transactions with credit organizations) reinforces the pro-inflationary effect and, consequently, creates the conditions for additional indexation of public regulatory and other expenditure obligations.▲