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THE FEDERAL BUDGET STILL HAS A SAFETY MARGIN, HOWEVER BALANCING IT IS BECOMING MORE DIFFICULT

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The short-term sustainability of the federal budget is not in question, even despite a fairly significant current deficit and the suspension of debt financing in July 2026. Meanwhile, the risks of falling short on non-oil and gas revenues are increasing, volatility in commodity revenue flows is rising, and geopolitical uncertainty persists. All of these factors could significantly complicate both the execution of this year's budget and the process of drafting the federal budget for the coming year.

Despite the rather substantial deficit (*Table 1*), the results of federal budget execution for H1 2026, while not appearing critical, have revealed a number of emerging trends that could significantly complicate the process of balancing the federal budget as early as next year.

In the first half of the year, federal budget revenue amounted to just over 46% of the annual target. Oil and gas revenues totaled Rb3.7 trillion, which is more than 22% below the level for the corresponding period last year and about 41% of the annual target. In addition, oil and gas revenue did not exceed its baseline level calculated in accordance with the budget rule, which necessitated the use of Rb370 bn in liquid reserves from the National Wealth Fund.

Table 1

Federal budget execution: current status and trends

	2026 (the law in its original version)		Execution for January-June 2026		Execution for January-June 2025		Deviation, y/y	
	Rb bn	% GDP	Rb bn	% of annual targets, plan	Rb bn	% of annual targets, plan	Rb bn	%
Revenues, including:	40 283	17.1	18 622	46.2	17 594	47.2	1 028	5.8
- oil and gas	*8 918*	*3.8*	*3 661*	*41.1*	*4 735*	*55.9*	*-1 074*	*-22.7*
Note: base level of oil and gas revenues	*8 957*	*3.8*	*3 825*	*42.7*	*4 487*	*53.5*	*-662*	*-14.8*
- non-oil and gas	*31 365*	*13.3*	*14 961*	*47.7*	*12 860*	*44.6*	*2 101*	*16.3*
Expenditures	44 069	18.7	24 353	55.3	20 981	48.9	3 372	16.1
Deficit	-3 786	-1.6	-5 731	151.4	-3 387	60.2	-2 344	69.2

Sources: Ministry of Finance of Russia, Rosstat, own calculations.

The factors behind the shortfall in oil and gas revenues that were characteristic of 2025, namely lower oil prices and a stronger ruble than anticipated when the draft budget was prepared only partially continued to have an impact in 2026. It should be recalled that the federal budget for 2026 was formulated based on estimates of an average annual price of Urals crude at $59 per barrel and a ruble exchange rate of Rb92.2 per dollar. By the end of the first half of the year, the average price of Russian crude had risen to $68 per barrel. This was due both to the U.S. – Iran military conflict that began in late February and the blockade of the Strait of Hormuz – through which up to 20% of global oil supplies and 30% of liquefied natural gas (LNG) volumes were transported – and to damage to hydrocarbon production and refining infrastructure in several Middle Eastern countries. These factors led to a spike in energy prices and significantly complicated the logistics of transporting resources already extracted in the region.

However, the budgetary impact of higher-than-expected prices for Russian oil proved insufficient to offset the impact of the strong ruble on the federal budget (the average exchange rate for the half-year was Rb76.4 per dollar). Given the dynamics of the national currency's exchange rate observed in recent years, it can be argued that the previously effective role of the devaluation mechanism in smoothing out external price shocks on hydrocarbon revenue dynamics has not only weakened but, in some months, has actually amplified the impact of price volatility (price and exchange rate changes have moved in the same direction: for example, the decline in Russian oil prices in May-June against the backdrop of a strengthening ruble).

Non-oil and gas revenues to the federal budget for H1 2026 reached nearly Rb15 trillion, which is 16% higher than the same period last year and equivalent to 48% of the annual target. However, the steady growth in non-oil and gas revenues in recent years has been made possible not so much by sustained economic growth as by consistent increases in key tax rates (personal income tax, corporate income tax, and VAT) and by inflation exceeding the targets set in the federal budget law (for example, the law sets an annual inflation rate of 4.0% for 2026, whereas in June 2026 it stood at 6.0%).

The key driver of growth in non-oil and gas revenues this year is VAT; the most significant changes to its regulation include an increase in the rate from 20% to 22% and a reduction in the threshold for inclusion in the VAT base for most types of microbusiness activities from Rb60 mn to Rb20 mn in annual revenue. In the first half of the year, VAT collections totaled Rb8.6 trillion, representing 49% of the annual target (Rb17.5 trillion). However, given the likelihood that the Russian economy will enter a recession in the second half of the year and the ongoing decline in overall business profit margins, reaching the planned level of VAT revenue will only be possible due to inflation; otherwise, according to our estimates, the shortfall in VAT revenue will amount to between Rb0.6 trillion and Rb0.8 trillion by the end of the year.

Projections for annual revenue from corporate income tax and personal income tax to the federal budget – Rb3.9 and Rb1.1 trillion, respectively – may also prove to be somewhat exaggerated, as of July 1, 53% and 13% of the targets were met, respectively.

One must take into account the damage to the national fuel sector caused by the blows to oil refining enterprises, which, among other things, has become a significant inflationary factor. However, for federal budget revenues, a decline in oil refining – provided that export prices for Russian oil remain higher than domestic prices – could mean a reduction in the excise tax on crude oil intended for refining, which is projected to amount to -Rb2.7 trillion in 2026. In other words, due to the damping mechanism (reverse excise tax), the Russian Ministry of Finance may "save" a portion of the budgeted compensation for oil refiners as a result of the decline in the volume of petroleum products they produce.

Another "innovation" of 2026 was the initiative announced by a number of Russian businesspeople to donate a portion of their wealth to the state. As of early June, the federal budget had received approximately Rb232 bn in non-repayable payments to the treasury from non-governmental organizations. It should be noted that this initiative arose during a period of active discussion regarding the possibility of reintroducing a tax on excess profits earned in the previous period (either for 2025 or for a number of years, though no specific parameters were established).

Turning to the expenditure side of the federal budget, it is worth noting a more consistent pace of funding than in previous years: As of the end of the first half of 2026, federal budget expenditures totaled more than Rb24 trillion, or 55% of the approved annual amount, whereas cash execution for the corresponding period in 2024 stood at 49% (*Table 1*). According to the Russian Ministry of Finance, the accelerated pace of fund disbursement is primarily due to active advance payments under government contracts in the first months of the year; however, this budget financing strategy for 2023–2025 resulted in expenditures exceeding the amount planned in the original version of the budget law by between Rb1.5 trillion and Rb3.5 trillion in nominal terms by the end of the year.

Given the lack of transparency regarding the current execution of expenditures broken down by functional sections, earmarked items, and types of spending, it should be noted that as of July 25, 2026, the revised expenditure plan, according to the "Electronic Budget" service, had been increased to Rb45.14 trillion, i.e., by nearly Rb1.1 trillion compared to the original version of the federal budget law.

Furthermore, domestic debt has been designated as the source of funding for additional budget expenditures, and to ensure a more consistent pace of borrowing by the Russian Ministry of Finance, the State Duma adopted a temporary amendment (effective until the end of the year) to budget legislation (clause 24 of Article 5 of Federal Law No. 195-FZ dated June 26, 2026), allowing the Government of the Russian Federation to decide, without amending the budget law, to increase the volume of domestic financing sources for the federal budget deficit within the limits of the balances in the single treasury account. In other words, the Russian Ministry of Finance has been granted the right, without parliamentary approval, to borrow in excess of the domestic debt ceiling established by the budget law, with such additional borrowing limited to the amount of the balance in the unified treasury account, which as of early July was equivalent to Rb5–6 trillion. Although this measure is temporary and primarily technical in nature, it has the potential to double the volume of net borrowing (excluding redemptions) raised by the Russian Ministry of Finance from the market (the initial plan was to raise net borrowing in the amount of Rb4–4.5 trillion) and thereby further increase the burden on the budget due to ever-rising interest payments, not to mention the risk of further crowding out private investment (capital flows into government bonds, diverting it from the real sector) and the impact on inflation. Therefore, it is extremely important how – and to what extent – the Russian Ministry of Finance will ultimately exercise this right. Nevertheless, it is already clear that an additional source of uncertainty has emerged for the Central Bank of Russia.

It should also be noted that the requirement to maintain the primary structural balance – which forms the basis of the budget parameters – has once again not been met due to an upward revision of expenditures without a corresponding increase in revenue sources. In essence, this appears to be yet another deviation from the budget rule, which ultimately seriously undermines its practical usefulness.

As of the end of the first six months of 2026, the federal budget deficit stood at Rb5.7 trillion, compared with an approved annual target of 3.8 trillion rubles. In recent months, rising oil prices have helped halt the growth of the deficit, but the outpacing growth of budget expenditures, coupled with looser controls on borrowing, could lead to a new surge in the budget deficit as early as this fall. And although the budget still has a margin of safety, according to our estimates, the annual deficit may increase even further, and its final amount will depend heavily on the trend in oil and gas revenues in the second half of the year.