

MONITORING OF RUSSIA'S ECONOMIC OUTLOOK:

TRENDS AND CHALLENGES OF SOCIO-ECONOMIC DEVELOPMENT

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Monitoring of Russia's Economic Outlook

Monitoring has been written by experts of Gaidar Institute for Economic Policy (Gaidar Institute), Russian Presidential Academy of National Economy and Public Administration (RANEPA).

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1. THE FEDERAL BUDGET EXECUTION IN 2020

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According to the preliminary data released by the Finance Ministry of Russia, the federal budget revenues constituted Rb18.7 trillion against the projected Rb20.6 trillion for 2020,¹ and expenditures – Rb22.8 trillion against planned Rb19.7 trillion. Such difference in the state budget execution was due to the outbreak of pandemic and the need to put in place the relief programs for business and the population. The total amount of funds for that purpose stood at Rb5 trillion.

Over 12 months of 2020, the federal budget revenues in real terms decreased by 11.7% compared to 2019 (Table 1) and constituted 90.8% of the approved projected amount. In real terms the highest reduction by Rb3.5 trillion is recorded in oil and gas revenues including by Rb2.3 trillion in MET, and by Rb1.2 trillion in export customs duties. At 2020 year-end, proceeds from the oil and gas revenues to the budget came to Rb4.9 trillion up by Rb0.3 trillion of their base value² which allowed to keep practically untouched the National Welfare Funds (the NWF funds directed to financing the federal budget deficit in 2020 amounted to Rb289.8 bn) for balancing the budget. As a result, as of January 1, 2021, the value of NWF in ruble equivalent increased to Rb13,545.7 bn (\$183.3 bn) against Rb7,773.1 bn (\$125.6 bn) a year earlier which was due to additional oil and gas revenues charged to NWF obtained at 2019 year-end and to exchange rate revaluation.

The non-oil and gas revenues of the federal budget over 12 months of 2020 moved up by Rb1.2 trillion or by 9.8% in real terms against January-December of the previous year. This growth was due to transfer of central bank's profit obtained from the sale of PAO Sberbank (reflected in the budget line other revenues). With respect to other tax revenues there was a decline in proceeds:

- on profit tax – down by Rb145.1 bn or by 12.2% in real terms against 2019;
- on domestic VAT and excises – down by 4.6% or 1.1%, or by Rb196.1 and Rb10.7 bn, respectively;
- on import VAT – down by Rb43.7 bn or by 1.5%;
- on export customs duties – down by Rb38.3 bn or by 5.3%.

The federal budget expenditures as January-December-end of 2020 to the same period of 2019 went up by Rb3.5 trillion or by 19.4% in real terms at rapid disbursement in 2020 (Table 2).

1 According to Explanatory Note to FZ No. 380 (dated March 18, 2020).

2 With regard to adjustments on excise reimbursement.

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Table 1

The main parameters of the federal budget over 12 months of 2019–2020

	January-December 2019		January-December 2020		Deviation, 2020 to 2019		
	Rb bn	% GDP	Rb bn	% GDP	Rb bn (in 2019 prices)	In constant prices, ¹ %	p.p. GDP
–oil and gas, including	20 188.8	18.3	18 699.3	17.5	-2 363.0	-11.7	-0.8
–MET	8 247.7	7.5	4 950.2	4.6	-3 528.7	-42.8	-2.9
– export duties	5 971.7	5.4	3 819.4	3.6	-2 330.7	-39.0	-1.8
–oil and gas, including	2 276.0	2.1	1 130.8	1.0	-1 198.0	-52.6	-1.1
–non-oil and gas, including:	11 941.1	10.8	13 749.1	12.9	1 165.8	9.8	2.1
–corporate income tax	1 185.0	1.1	1 090.9	1.0	-145.1	-12.2	-0.1
–VAT on goods sold in RF	4 257.8	3.9	4 260.7	4.0	-196.1	-4.6	0.1
– VAT on goods imported to RF	2 837.4	2.5	2 930.6	2.7	-43.7	-1.5	0.2
–excises on goods sold in RF	997.5	0.9	1 035.2	1.0	-10.7	-1.1	0.1
–import customs duties	716.9	0.6	711.8	0.7	-38.3	-5.3	0.1
– other revenues	1 946.5	1.8	3 719.9	3.5	1 599.6	82.2	1.7
Expenditure, including:	18 214.2	16.5	22 812.7	21.4	3 532.9	19.4	4.9
– interest	730.8	0.7	784.2	0.7	16.8	2.3	0.0
– non-interest	17 483.4	15.8	22 028.5	20.7	3 516.1	20.1	4.9
Surplus (deficit) of budget	1 974.6	1.8	-4 113.4	-3.9	-5 895.9	–	-5.7

Sources: Ministry of Finance, Federal treasury, GDP for 2020 – Rosstat estimates, own calculations.

Table 2

The federal budget expenditures over 12 months of 2019-2020

	January-December 2019		January-December 2020		Deviations, 2020 to 2019		
	Rb bn	% GDP	Rb bn	% GDP	Rb bn (in 2019 prices)	In constant prices ² , %	p.p. GDP
Expenditures, total, including	18 214.2	16.5	22 812.7	21.4	3 532.9	19.4	4.9
Nationwide Issues	1 363.5	1.2	1 502.4	1.4	68.7	5.0	0.2
National Defense	2 997.4	2.7	3 167.8	3.0	22.4	0.7	0.3
National Security and Law Enforcement	2 083.2	1.9	2 225.5	2.1	38.3	1.8	0.2
National Economy	2 827.1	2.6	3 483.8	3.3	494.0	17.5	0.7
Housing and Utilities	282.2	0.3	370.0	0.3	70.5	25.0	0.0
Environmental Protection	197.5	0.2	260.6	0.2	50.9	25.8	0.0
Education	826.5	0.7	956.7	0.9	85.5	10.3	0.2
Culture and Cinematography	122.4	0.1	143.9	0.1	14.8	12.1	0.0
Healthcare	713.0	0.6	1 334.5	1.3	559.2	78.4	0.7
Social Policy	4 882.8	4.4	6 991.0	6.6	1 781.6	36.5	2.2
Physical Culture and Sports	81.4	0.1	75.2	0.1	-9.7	-11.9	0.0
Mass Media	103.5	0.1	121.1	0.1	11.9	11.5	0.0
Public Debt Servicing	730.8	0.7	784.2	0.7	16.8	2.3	0.0
Intergovernmental fiscal transfers	1 003.1	0.9	1 395.9	1.3	327.6	32.7	0.4

Sources: Finance Ministry of Russia (operational data), Federal Treasury, own calculations.

The highest growth (12 months of 2020 to 12 months of 2019) in real terms is reported with respect to expenditures on relief of economy and social sphere in the wake of the pandemic: increased spending on social policy amounted to Rb1,781.6 bn (36.5%), national economy – Rb494.0 bn (17.5%), healthcare – Rb559.5 bn (78.4%), intergovernmental fiscal transfers – Rb327.6 bn (32.7%). On

1 According to consumer price index.


2 According to consumer price index.

1. The Federal budget execution in 2020

the whole, the real volume of the federal budget expenditures over 12 months of 2020 exceeded the planned annual volume by more than Rb3.0 trillion which was mainly due to financing three relief packages and the implementation of the National plan of economic recovery.¹ As of 2020 year-end, the aggregate volume of relief measures aimed at support of the population, banking sector, the real sector of the economy, and the regional budgets hit around Rb5.0 trillion or 4.5% of GDP.²

The federal budget deficit as of January-December-end of 2020 constituted Rb4,113.4 bn against a surplus of Rb1,974.6 bn for the same period of 2019. Consequently, the non-oil and gas deficit moved up from Rb6,273.1 bn to Rb9,063.6 bn. Over 12 months of 2020, the government borrowed Rb5.2 trillion on the domestic market in order to cover the budget deficit. Under a planned placement of Rb2.3 trillion, the volume of borrowing on the external market in the ruble equivalent constituted Rb180.6 bn and the volume of redemption – Rb381.2 bn (planned volumes – Rb207.2 bn and Rb343.1 bn, respectively).

Domestic borrowing at such unprecedented amounts can be considered as rather fruitful because, firstly, OFZ yield in October-December 2020 stood practically at the pre-crisis level seen in January 2020, secondly, the borrowing terms averaged around 7 years which, in its turn, should allow Russian economy and budget revenues to recover at the debt maturity period, thirdly, the ruble denominated debt does not pose any currency risk for the federal budget.

At the same time, the ramping up of public debt during a single budget cycle makes a wake-up call especially with due regard for a possibility of a protracted economic crisis and slow easing of COVID-19 restrictions. This makes it necessary to go for additional borrowings in 2021. Moreover, at the current oil price (above base price of \$43.3 per bbl) the effective fiscal rule does not permit to direct NWF funds to cover budget expenditures. 

1 Approved by the Government of the Russian Federation on September 23, 2020. Total financing of this plan is valued at over Rb3.8 trillion, including Rb2.6 trillion in 2021.

2 Source: G20 Summit. Presentation of the President of the Russian Federation V.V. Putin. URL: <http://kremlin.ru/events/president/news/64460>.

2. THE CONSUMPTION OF GOODS AND SERVICES IN 2020: THE PANDEMIC MODEL

Alexandra Burdyak, Senior Researcher, Standard of Living and Social Protection Studies Laboratory, INSAP, RANEPA

The real cash incomes of the population in 2020 decreased by 3.0% compared to 2019, the real disposable cash incomes contracted by 3.5%. Consumption model of Russian people has changed in the wake of the pandemic: the share of expenses on services has decreased to near 2016 level, meanwhile the share of expenses on food has notably increased. Against the backdrop of the overall reduction in food products sales turnover, their sales have gone up in large and medium-size retail chains. People will return to the common consumption model solely after total lifting of pandemic restrictions.

Monthly statistical data of retail sales¹ recorded maximum decline (down by 23% to the same month of the previous year) in April 2020 including by 35% in non-food goods sales and by 9% in food products sales. The retail sales in services² plunged by 38–39% in April-May 2020 year-on-year. Retail sales of non-food goods recovered rapidly by July-October 2020 year-on-year due to pent-up demand. However, the foodstuffs consumption by early autumn stood below last year indexes by 3–4% (August-September). In September, the volume of paid services hit 88% year-on-year, however, with new restrictions in place in November-December, the consumption of goods and services declined again year-on-year.

On the whole, the retail sales over January-December 2020 declined in comparable prices by 4.1% year-on-year including by 2.6% on food products and by 5.2% on non-food goods. The volume of paid services plunged by 17.3% in comparable prices. And if similar in scale recession in consumption of food products and non-food goods we observed in 2016 (*Fig. 1*) then such significant contraction of services reported in 2020 was unprecedented.

By more than half year-on-year contracted the values of paid services rendered to the population by tourist agencies (48% of the 2019 level) and by cultural institutions (47%). By over a third plunged the value of services rendered by institutions of physical culture and sports (67.4%), by hospitality business (64.9%), sanatorium-and-health-resort facilities (59.8%), and by transportation firms (60.9%). To a lesser extent the pandemic hit personal services (85.4%), paid education services (87.4%), medical (90.5%), legal (91.2%), telecommunication (95.2%), and utility services (96%). That said, the consumption of courier and post services have gone up in annual terms (103.6%). The minimum decline in

1 A Report "Socio-economic Situation in Russia" / Rosstat. URL: <https://rosstat.gov.ru/compendium/document/50801>.

2 Maleva T.M., Grishina E.E., Burdyak A.Ya., Chumakova Yu.B. The Epidemiological Crisis in H1 2020.: Socio-economic Situation of the Population // Russian Economic Developments. 2020. Vol. 27. No. 10. P. 60–72.

2. The consumption of goods and services in 2020: the pandemic model

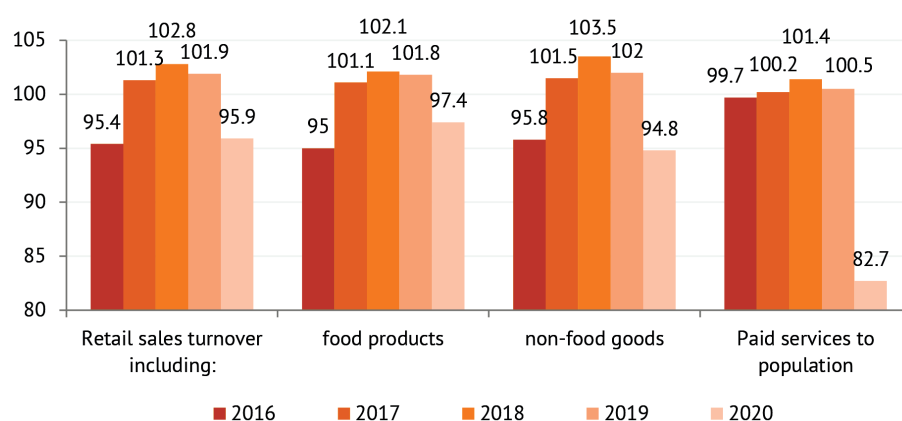


Fig. 1. Annual retail sales turnover in comparable prices and index of physical volume of paid services for the population, % year-on-year

Source: Rosstat.

personal services in 2020 was reported in maintenance and repair of transport vehicles, machinery and equipment (91.5%); leasing firms including car sharing (94.3%). Increase in funeral services was the sad result of the pandemic (103% against 2019).

Speaking about the basic food products consumption at the early stage of the pandemic, there was a panic buying of pasta, cereals, flour, sugar, and vegetable oil in March 2020 reported by large and medium-size retail sales chains¹ (Fig. 2). Sales of pasta returned to the previous year level in April-June and sales of cereals and especially sugar from April through the end of 2020 were below the 2019 level. Drinking milk sales changed insignificantly.

The aggregate sales of sugar and cereals by large and medium-size retail chains came to 89.4% and 96.9% in January-December 2020 year-on-year. The sales growth was reports in 2020 against 2019 regarding other groups of food products: eggs up by 28%, fresh potatoes – by 25%, animal fats, butter, poultry meat, flour, and fresh fruit – by 22%, cheese – by 20%, meat – by 16%, vegetable oil – by 15%, and fresh fruit – by 11%.

Accordingly, in the wake of the overall decline in retail sales of food products by 2.6%, the retail sales of food products went up in large and medium-size retail chains. On the one hand, this was due to a reduction in catering turnover by over 50% during the

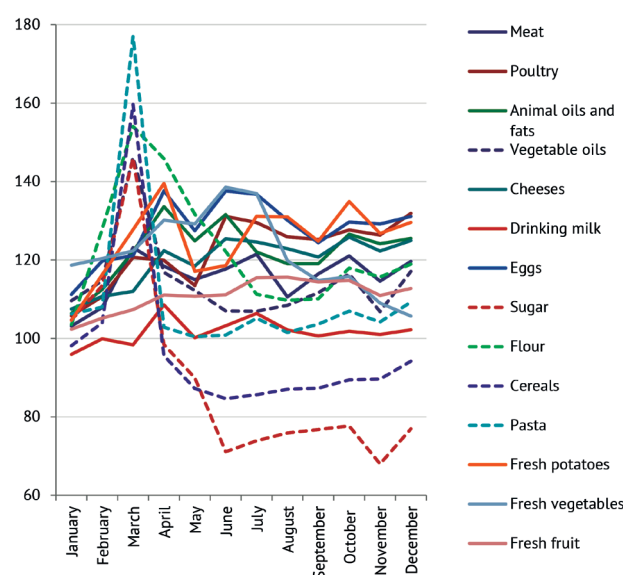


Fig. 2. Retail sales of staple food products by large and medium-size retail chains, in % to the same months of the previous year in comparable prices

Source: Rosstat.

1 Retail sales of staple food products by large and medium-size retail chains (operational data) / Rosstat. URL: <https://rosstat.gov.ru/folder/11188>.

stringent first lockdown put in place in April-May, on the other hand, increased sales of prepacked products and boxed lunches, spread of free delivery service from large chains during the pandemic. To a certain extent, customers tried to minimize their visits to shops by shopping in trade centers, the value of an average sales check year-on-year¹ confirms this.

Taking the example of the current year consumption model, Rosstat calculates weight matrix², designed for calculation of the consumer price index (CPI) for the next year. The consumer spending pattern dynamic for recent 10 years is presented in Fig. 3, three stages can roughly be separated. In 2010–2013, the share of spending on food products was falling (from 38.5 to 36.5%) while on-food goods consumption was growing (from 35.6% to 37.7%) against the backdrop of constant share of expenses on services (25.8–25.9%). In 2014–2015, on the contrary, expenses on food products were going up (up to 38%) while the share of expenses on non-food goods was contracting (down to 36.5%). In 2015–2019, the share of expenses on services went up (from 25.5 to 27.8%) meanwhile expenses of food products and non-food goods were falling. In 2020, the consumption model underwent changes: the share of expenses on services decreased by nearly 2016 level, meanwhile the share of spending on food products moved up notably.

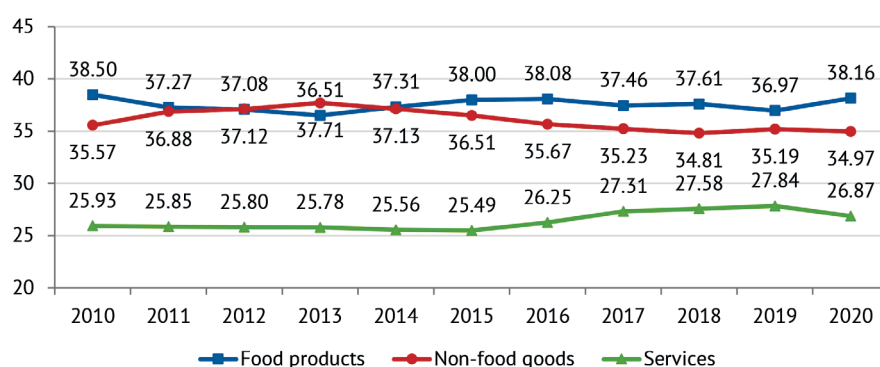


Fig. 3. Consumer spending pattern for calculation of consumer price index next year, %

Source: Rosstat.

In “quiet” non-pandemic time, the households’ expenses growth on food products could have signified poverty growth because the low-income households’ budgets focus on foodstuffs spending. However, the latest available to date official statistical information report about an insignificant growth of the share of poor in January-September 2020 when in it recorded an up-tick by 0.2 p.p. year-on-year³.

On the whole, there was an erosion of the financial situation of the Russian people during the pandemic. On the one hand, according to FOM⁴, in April-May 2020, up to 45% of the population went on saving more than prior to the


1 Average sales check has demonstrated the record value in December. / Romir. January 19, 2021. URL: <https://romir.ru/studies/sredniy-chek-pokazal-rekordnoe-znachenie-v-dekatre>

2 Prices. Pattern of consumer spending for calculation of CPI / Rosstat. URL: <https://rosstat.gov.ru/price>.

3 On correlation between cash incomes and living standard, and the number of poor people across the Russian Federation as a whole in Q3 2020 / Rosstat. URL: https://www.gks.ru/bgd/free/B04_03/IssWWW.exe/Stg/d02/12.htm.

4 Indicators of pandemic-induced economic fallout: dynamic in 2020 / FOM URL: <https://covid19.fom.ru/post/indikatoriy-ekonomicheskikh-posledstviy-pandemii-dinamika-v-2020-godu>.

2. The consumption of goods and services in 2020: the pandemic model

outbreak of pandemic. In August-September, the share of those who saved more fell to 36% and in October-December, it against exceeded 40%. On the other hand, the erosion has affected not all the people: in the wake of the pandemic the share of Russian households who had to save during last year or have abandoned the idea of previously planned purchases was consistently high between February and December 2020 and stood at 75% plus-minus 2 p.p. That said, nearly quarter of households did not save. 

3. THE CURRENT OUTCOME OF FOOD PRICES REGULATION

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The direct regulation of prices for vegetable oil, sugar, and bread has helped to stop their growth, however it has not resulted in halting food inflation as a whole. Restrictive measures on wheat exports have led to world prices growth but when put into effect they can reduce prices for the consumers on the domestic market. The proposed mechanism for revenue shortfall compensation for agricultural producers will reimburse direct losses from the imposition of export duties but not losses incurred from price reduction on the domestic market.

Measures aimed at foodstuffs price regulation put in place in mid-December 2020 were immediately followed by a stabilization and even decline in prices on food products subject to regulation: sugar, sunflower oil, and bakery products. According to Rosstat, over 6 weeks (from December 2020 through February 1, 2021) the average consumer prices of sugar and sunflower oil declined by 4.7%, sunflower oil down by 0.9% and went up by 0.5% on bread and bakery products made of wheat flour (Fig. 1).

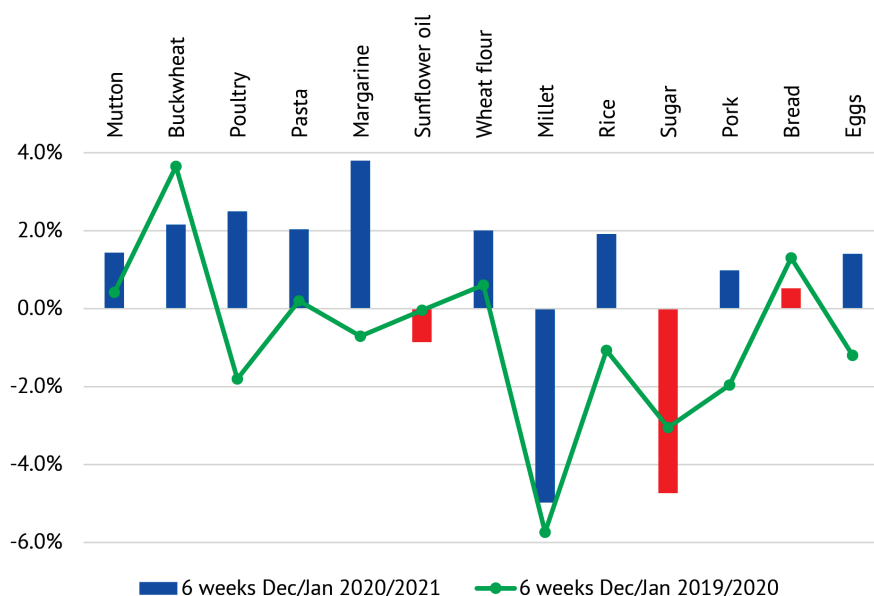


Fig. 1. Growth rates of retail prices on certain foodstuffs, December/January 2019/2020 and 2020/2021, %

Source: Rosstat.

3. The current outcome of food prices regulation

Meanwhile prices on certain foodstuffs that were not subject for regulation but which production involves wheat and vegetable oils have significantly increased in price. For example, pork, mutton, poultry, and egg prices have gone up by 1.0, 1.4, 2.5 and 1.4%, respectively (at average change for the comparable period 2017–2020 of -1.0, +0.4, -0.6, and +1.2%). Prices of pasta, vermicelli, flour, rice, and buckwheat up by 2.0, 2.2, 2.0, 1.9 and 2.2%, respectively (+0.7, +0.9, +1.1, +0.4, +0.6% on average for the comparable period 2017–2020, respectively). Prices of margarine up by 2.8% (-0.1% in 2017–2019). Solely millet prices plunged by 5% as they returned to the early 2019 price level.

Given that the period under analysis is dominated by the impact of seasonal price growth on vegetables and fruit, the overall estimate of foodstuffs price dynamic is in doubt if we apply the corresponding index. However, a spike in prices for basic foodstuffs demonstrates that the market price restriction fell short of the target.

The retail chains' information regarding the issues regarding the procurement of butter and sugar at regulated prices that popped up in mid-January 2021¹ did not come again, however, a host of experts point to the risks of food products shortage. That said, the shortage threat decreases in consumers' expectations: according to Yandex search requests, the first wave of the pandemic and stringent lockdown measures imposed in the second half of April 2020 demonstrated maximum concern (100%) with the shortages issue. Following the summer-autumn 2020 recession, shortages concern staying at to 27% went up to 87% at the launch of price regulation in December, however, it decreased by 66% by late January 2021.

Measures of domestic price regulation of food products put in place in late 2020 have affected the foreign trade of basic agricultural products – wheat and oil crop. The shifts in foreign trade regulation exert a considerable impact on producers because exports accounted for around a half of wheat and sunflower oil production over last 5 years. Consequently, restrictions in exports in large measure determine long-term trends of sector's development.

The Russian Government Resolution No. 2096 dated December 14, 2020 imposed a quota on wheat exports with an export duty at €25/mt within the quota, and if the export volumes exceed the quarter, the duty for wheat would rise to 50% of the customs price but no less than 100 €/mt. The restrictions were to be in effect from January 15 through July 30, 2021.

Given that a grain export quota limiting shipments to 17.5 mn tons on the whole corresponds to resources and needs of the market, the effect from the export customs duty within the quota, according to our calculations, projected a decline in price for wheat-exporting regions down to 13% on condition that exporters pay the duty while the price remains unchanged. However, by being the largest wheat exporter and accounting to 20% of the world market, Russia significantly influences the wheat price dynamic. Information regarding the introduction of projected export duty was transferred to prices on the date it's been enforced (December 10, 2020²) which led to a spike in wheat world prices by 5.1% by January 11, 2021 (*Fig. 2*). The price hike amounted to \$13 in export prices on Russian wheat (Russian wheat 12.5% FOB Black Sea), in other words, nearly 50% of the export duty went into prices. Consequently, possible effect of price reduction contracted to 7%.

1 URL: <https://www.kommersant.ru/doc/4641602>.

2 URL: <https://tass.ru/ekonomika/10226357>.

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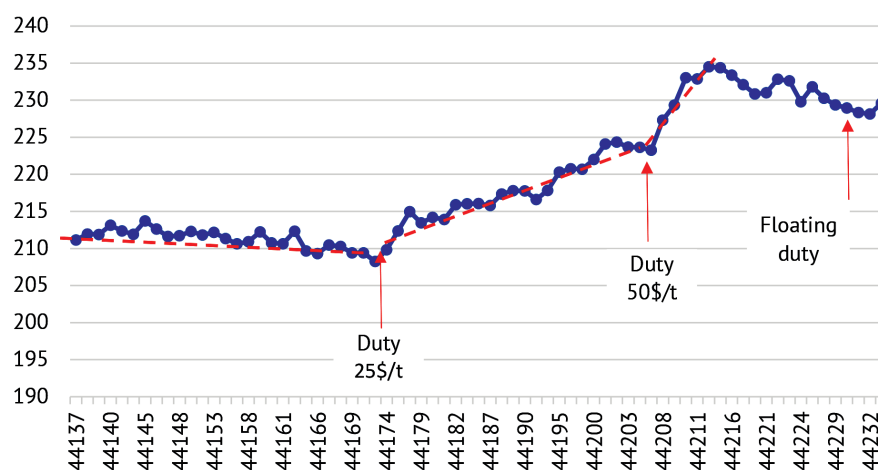


Fig. 2. The wheat world price dynamic IGC-GOI Wheat sub-index in November-February 2020 and 2021

Source: IGC.

In the wake of still growing wheat prices on the world market with partial leveling of the impact of previously imposed export duty on domestic market prices, the Ministry of Agriculture proposed to raise the export duty on wheat and introduce it on other grains.¹ Just like in case of export duty effective in December, the world market reacted swiftly with price hike along with the first news outbreaks as of January 11.²

The RF Government Resolution No. 33 dated January 23, 2021 enforced an export duty of €50/mt on wheat from March 1 through July 30, 2021, an export duty on barley of €10/mt, and on corn €25m/mt effective from March 15 through July 30, 2021.

From January 11, 2021 (first information about the export duty increase) world prices for wheat came to 3.8% by January 29, 2021. By the same date, the world prices of wheat went up by 9.2% compared to December 10, 2020 (first information on the imposition of duties).

The potential effect of the duty growth on prices came to 14% by January 11, 2021 and with due regard for world market reaction – 9%. According to our calculations, the overall effect of two-phase regulation of wheat exports in December 2020 and January 2021 with due regard for world prices adjustment will constitute 15% of price reduction at the ports of export.

Export price growth of Russian wheat was outstripping the average world price growth and by January 22, 2021 amounted to \$45 or 17.5% against the December 11, 2020 level thus compensating $\frac{3}{4}$ of the coming duty value. However, the price of around \$300/t was the utmost for importers who reduced their purchases.³ As a result, by the end of January the export price of Russian wheat fell to \$295/mt.

At the briefing held on February 4, the Minister of Economic Development, Maxim Reshetnikov, confirmed the introduction of a floating export duty on grains and setting up of a mechanism for grains damper allowing to reimburse duties for the agricultural sector by spreading it according to production volume

1 URL: <https://www.agroinvestor.ru/analytiks/news/35097-poshlina-na-pshenitsu-mozhet-vyrasti-do-45-evro-za-tonnu/>.

2 URL: <https://tass.ru/ekonomika/10437407>.

3 URL: <http://agropravda.com/news/agrorynok/15576-importery-pshenicy-otkazyvajutsja-pokupat-zerno-po-vozroshhim-cenam>.

3. The current outcome of food prices regulation

of export products. Respective resolutions No. 117 and 118 were signed by the RF Government on February 6, 2021. According to those resolutions, if the price exceeds the threshold, the value difference between the market and the base export price at Novorossiysk FOB will attract a duty of 70% (\$200 for wheat, and \$185 for barley and corn).

That said, the world wheat prices apparently staying at the maximum level for importers did little to react to the actual abolition of an export duty on Russian grain in the long term: The International Grain Council index as of February 8, 2021 exceeded by 0.3% the level seen in February 3, 2021 and stood below the maximum level of the current season by 2.1% (January 18, 2021).

The RF Government Resolution No. 2065 dated December 10, 2020 "On Amendments to Export Customs Duties on Goods Exported from the Russian Federation beyond the bounds of the member states of Customs Union Agreement" raises export customs duties on seeds of sunflower and rape from 6.5 to 30% for the period from January 9 through June 30, 2021. By contrast with measures aimed at the wheat market regulation which by-products are consumed on the domestic market and are exported in insignificant volumes, restrictions of sunflower exports without export restriction imposed sunflower oil does not provide an independent effective instrument for regulating domestic prices on the final product. We view this decision as an informal incentive for producers to come to an agreement on fixing top release and retail prices on sunflower oil. Imposition of a tax on sunflower oil exports will be an enforcement tool for adhering to the agreement.¹

As an additional measure to stabilize domestic food market, the government introduced an export duty on soya at 30% but no less than €165/mt from February 1 through June 30, 2021. This measure should stabilize domestic prices on soya-by products which will impact the retail prices in the following way: reduction in production cost of food products using soya oil; reduction in production cost in the animal husbandry sector where soya and its by-products are used as fodder. Moreover, soya export restrictions will absorb idle capacities in fat-and-oil industry which are estimated by the experts behind the measure to stay at 30%.

Under the current soya export restrictions, the government took into account the negative experience of previous restrictive measures associated with geographic unevenness of production and processing distribution: the Far-Eastern Federal Okrug accounts on average for 1/3 of soya production and solely 1/8 of its processing, the remaining volume is exported to China. According to the RF Government Resolution No. 54 dated January 27, 2021, the soya beans produced in Far East can be shipped to Central, Siberian, and Volga Federal Districts at zero railway tariff. Inefficiency of such shipments must be solved while soya processing capacities are built in the Far East.

The wheat world price growth in H2 2020 on the whole is not due to the shift in the resource base. The FAS USDA estimates world wheat production to stay at 5-year high and in January was adjusted upward by 0.3% to 772.6 mn tons compared to September estimates. Despite a growing consumption the stocks estimate at the season-end also stays at 5-year high and constitutes 313.5 mn tons down by 1.9% against the September estimate. Stocks estimate adjustment is primarily due to growing wheat consumption in China (+3.8%, or up by 5 mn t). ■

1 URL: <https://www.interfax.ru/russia/741200>.

4. MORTGAGE CREDIT IN 2020

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The final transition to escrow accounts model in financing residential construction was the highlight of the mortgage market in 2020. The model provided state guarantee for the citizens investing in housing at the construction stage.

The reduction of credit rates and implementation of the state program on interest rate subsidization for newly constructed building mortgage loans have resulted in upward demand on the real estate market. Over 2020, the Russian banks have built up the value of mortgage loans exceeding record indexes previously recorded in 2018.

The Russian housing mortgage lending (HML) market reported record levels in 2020 despite the recession induced by the coronavirus pandemic. Credit organizations have extended 1.71 mn mortgage loans in the course of the past year. Accordingly, the growth went up by 34.9% against 2019 (1.27 originated loans) and by 16.4% against record high 2018 (1.47 originated loans). The value of extended credits totaled Rb 4.30 trillion over last year (up by 50.8% against 2019 and up by 42.6% against 2018).

At last year-end, the overall hypothecary debt exceeded Rb9 trillion. Annual loan debt growth hit 21.4% against 17.1% in 2019, and 23.9% in 2018. The total number of originated mortgage loans constituted 45.2% of the total bank retail loan portfolio against 42.3% as of early 2020.

Refinancing of credit remains an important factor behind the mortgage market growth. At 2020 year-end, it totaled 13.7% of the overall value of mortgage lending (in 2019, refinancing amounted to 6.8%).

Mortgage lending is the best retail credit segment, outstanding mortgage debt stays at consistently low level – at the year-end, its value constituted merely 0.8% (at 2019 year-end overdue debt stood at 0.9%, and 1.0% at 2018 year-end). To compare, outstanding debt comes to 7.8% in other segments of retail lending. The value of non-performing loans (NPL 90+) was at 1.4%¹ staying unchanged over the year.

Mortgage loans denominated in foreign currency are in little demand. The value of debt denominated in foreign currency stood at Rb16.1 bn at the year-end or around 0.2% of total number of housing mortgage loans extended dropping by 24.6% over the year. The quality of foreign currency credit portfolio is way below the ruble denominated loans: the share of outstanding debt came to 39.9% at the 2020 year-end.

¹ As contrasted with outstanding debt, this indicator takes into account the total loans amount which were unpaid over 90+ days.

4. Mortgage credit in 2020

The average loan maturity upward trend remains unchanged. In December 2020, the weighted average loan maturity constituted 225.1 months, up by 6.7 months or by 3.0% over the year.

The launch of the soft mortgage loan program “6.5%” and reduction in the market interest rates are behind the peak indicators of the mortgage market in 2020. The average interest rate on the ruble loans dropped to 7.36% against 9.68% year earlier. In October-November last year, mortgage deals in the foreign currency segment were at 5% interest rate.

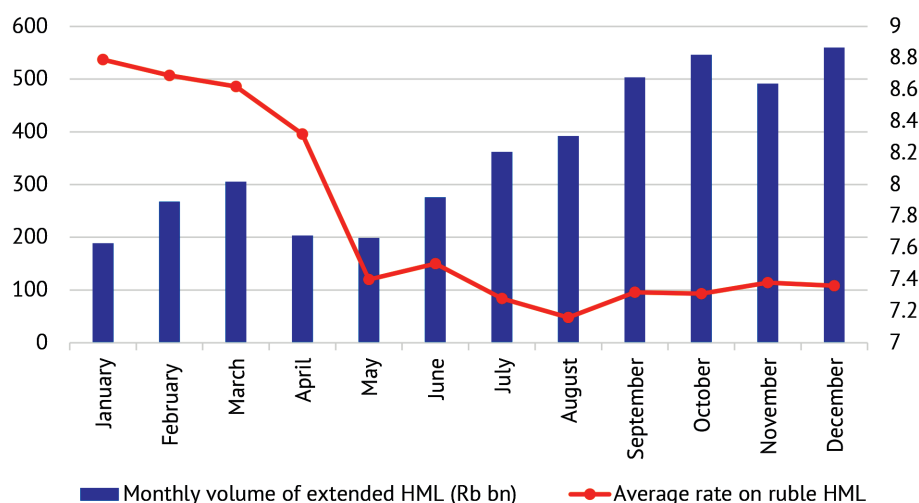


Fig. 1. Monthly lending numbers and interest rates dynamic of the housing mortgage lending market in 2020.

Source: Information on housing mortgage lending market in Russia. Information Bulletin No. 8. Statistical Indexes January 01.2018 – January 01.2021.

Credit rates on the primary market (new-built housing) remain around 2 p.p. below those seen on the secondary market (secondary housing) owing to the implementation of a number of soft mortgage loan programs (soft mortgage loan program “6.5%, household mortgage, Far-Eastern mortgage). Nevertheless, the high housing demand unfolding on the secondary residential market is primarily behind the mortgage lending growth. Out of the total number of issued housing mortgage loans, 71.7% account for the purchase of new-built housing.

Originally, the state soft mortgage loan program was to be effective through November 2020, however it was extended in late October 2020 through July 1, 2021.

Mortgage lending was least affected by the pandemic shock (3.1% of past due debt was restructured) including thanks to timely kick start of the state program of interest rates subsidization of 6.5%.

The reduction in mortgage rates due to the Bank of Russia monetary easing coupled with the launch of soft mortgage loan programs have boosted demand for housing and mortgage. This being said, the unprecedented growth in mortgage lending has not created a housing bubble, the mortgage lending remains the best segment of the retail lending market. However, amid peak growth of real estate market (over 2020, the average value of sq. m on the secondary market went up by 16.2%) and reduction in real disposable cash income of the population (down by 3.5% during 2020), there is no risk of a potential housing bubble. Small down payment (15–20%) on soft mortgage

loans poses risks both for banks and clients. In case of unfavorable economic situation (influenced by the pandemic, political factors, etc.), the real estate market will decrease by more than the down payment amount, and in case of borrower's non-payment the foreclosure sale will not cover debt before bank. There was similar situation in Russia following the 2008 financial crisis on the foreign currency mortgage market, however its volumes were small.

Despite the implementation of stimulus measures, the introduction of the new model of residential construction financing that ensure total state guarantee for the citizens who invest in housing construction has succeeded. In December 2020, the volume of housing under construction with the help of escrow accounts exceeded the volume of housing delivered under the old rules. Transition of housing construction to project financing has allowed avoiding the issue of hoodwinked investors even during the hardest months of self-isolation when construction and housing sales practically halted in many Russian regions. As a result, there was not a single escrow account induced case reported since the launch of the reform. Transition from the previous cost sharing construction model to escrow account project financing resided in the fact that the buyer deposits his/her funds on escrow account that arrive in developer's account after the escrow agreement terms and conditions have been met (completion of construction) and are cheap funding of developers' projects at the construction stage. Banks play the role of intermediaries (escrow agents) by opening accounts for the buyers and extending developers project financing from the funds held on escrow accounts. In the event the developer has problems with completion of construction, the buyer always can count on the return of deposit from the escrow account. The new system of housing purchase excludes a situation when an investor having paid to developer the total amount for an apartment in case of construction shutdown remains without money and apartment.

The Federal law dated November 9, 2020 No. 368-FZ "On Amendments into the First and Second Parts of the Tax Code" came into force in early November 2020. This law has settled the paramount taxation issue for the developers of cost sharing construction – the escrow funds being targeted financing. This will allow the majority of developers to exclude from the tax base escrow funds by solely paying tax on the amount exceeding investor's deposit over construction costs of cost sharing construction site transferred to the investor on the acceptance act.

According to Russia's central bank¹, according to January 1, 2021:

- over 303,000 escrow accounts have been opened for cost sharing housing construction;
- the value of escrow funds deposited has exceeded Rb 1.19 trillion, which is 8.5-fold than at 2019 year-end;
- Rb 126.7 bn have been released from the escrow accounts on construction completion in 64 subjects of the Russian Federation, i.e. have been transferred to the developers or directed to repayment of credits obtained for projects construction;
- there are 2,242 active mortgage credit agreements worth Rb 2.72 trillion signed by between banks and developers which is 200% more than a year earlier.

Subsequently, the new scheme of project financing which the sector adopted from July 1, 2019 has been spreading fast. Despite the positive market dynamic

1 URL: <https://cbr.ru/analytics/finansirovanie-dolevogo-stroitelstva/2021-01-01/>.


4. Mortgage credit in 2020

and relative high quality of the aggregate credit portfolio, in late 2020 a number of negative effects emerged, in particular, rise in housing prices (up by 10.5% over 9 months of 2020) that is significantly over the inflation rate. The situation is getting worse on the back of contraction of household incomes. Consequently, borrowers' gain from lower rates is significantly wiped out.

In H2 2020, loan refinancing deals according to top up¹ scheme became frequent when the principal debt goes up amid interest rate reduction. In 2007, such practice was one of the reasons for the mortgage crisis in the US. In Q1 2020, the difference between the new and old loan (top up) came to 3.8%, and by Q3 it went up to 5.6%.

Furthermore, banks oftener issued loans with low (below 20%) down payment: 35% of the mortgage loans extended in Q3 2020 compared to Q2 2020. Moreover, this share went up still more from 24 to 40% in the housing mortgage lending on the primary market.

The intention to preserve their savings amidst the ruble's depreciation, low bank interest rates and uncertainty regarding the unfolding crisis have led to erosion of marketable supply from the market.

The ballooning growth in housing mortgage lending in the wake of economic and socio-political turbulence raises risks of the housing market crisis as well as raises credit risks. The experience of many countries demonstrates that the initial effect from the easing of mortgage financing affordability on the back of rates reduction finally results in reverse effect: decrease in housing affordability. In this respect, high and sustainable growth of real cash incomes comparable with the housing price growth should be the main macroeconomic task fueling housing affordability growth. 

¹ Loan top up – loan for redemption of available loan. By contrast with classic refinancing, such loan is extended for already existing borrowers and without signing a new loan agreement.

5. FAMILY RESOURCES AND YOUTH EDUCATIONAL TRAJECTORY CHOICES

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As shown by the study conducted in 2020 by the RANEPA Center for Lifelong Learning Economics (CLLE),¹ the main reasons behind the respondents' choice in favor of secondary vocational education (SVE) can be divided into four groups: lack of proper knowledge and/or motivation to learn; shortage of family resources; a strategy of maximizing the advantages in the labor market; a strategy of choosing training in the SVE system as a step towards higher education.

The education level of a young person strongly depends on the education level of his or her parents and the parental family resource potential. Therefore, the study by the CLLE targeted the resources of those households that had reared the young graduates of secondary vocational schools (SVS).

The results of the study revealed that most of the graduates of SVSs (66%) lived in families with a low resource availability level, for a third of them (31%) that level was average, and only 2.9% lived in households with high resource availability (Fig. 1).

The sociological survey showed that the parents of the majority of respondents also had secondary vocational education. In the parental families of 60% of the respondents, the mother has a secondary vocational education; in 56% of the respondents, the bearer of such an education it is the father. Less than 20% of secondary vocational school graduates have at least one parent with a higher education, and 11% of the respondents grew up without a father (Fig. 2). Parents' education can influence the level of education received by their children in several ways. First, children may "follow in the footsteps of their parents"; secondly, the low education level of the parents quite often narrows their awareness of the available methods of getting an education and underestimates the merits of higher education in accordance with their limited worldviews; in the final analysis, this can translate into the distorted educational trajectories of their children. Moreover, parents quite often bring down the starting potential

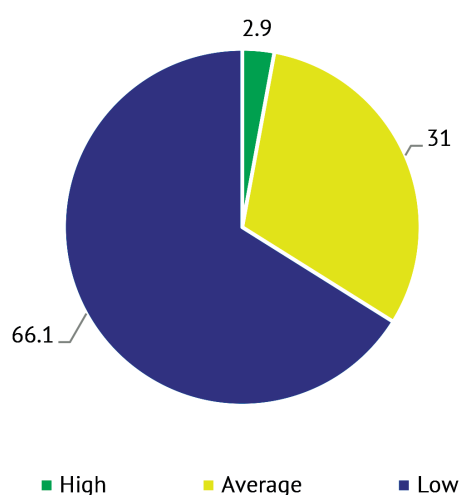


Fig. 1. The distribution of SVS graduates into groups relative to their parental family resource availability, %

Source: RANEPA CLLE study.

¹ The study analyzed, by type, the resources influencing the educational trajectory choices of young people. The typology of parental families was based on four indicators: parental education; family financial situation; parents' ability to help with studies; their ability to help with finding employment. The survey involved 903 respondents with secondary vocational education and a permanent job in the Sverdlovsk, Samara, and Volgograd regions.

5. FAMILY RESOURCES AND YOUTH EDUCATIONAL TRAJECTORY CHOICES

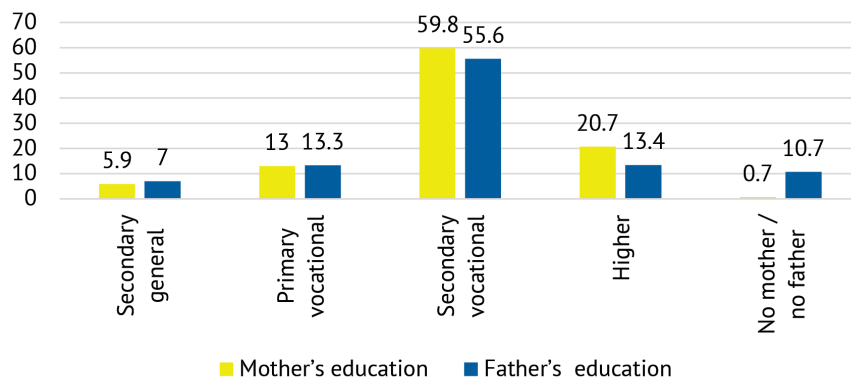


Fig. 2. The distribution of respondents relative to their parents' education level, %

Source: RANEPa CLLE study.

of young people by failing to support them in their choice of an educational trajectory.

The material well-being level of families likewise influences the educational choice of students. Among the respondents, 72.4% assessed the financial situation of their parental family as being average; 6.3%, as being above average; 14.5% thought that it was below average; 4.1% lived in low-income families; and only 7% of the respondents stated that the financial situation of their parental families was good. A low family well-being level can reduce the ability of parents to help their children in learning, and so the children leave school rather early in order to enter the secondary vocational education (SVE) system. The shortage of family resources also forces children to combine studies with work, and to enter the labor market earlier.

This is not to say that for the young people included in our survey their transition to the SVE system was invariably a better choice, consciously made. The data obtained in the course of our study have confirmed that for many, the choice of training in a vocational educational establishment (VEE) is a "necessity of life", and they have made it because they lacked the resources needed for entering a higher educational establishment (HEE). The main reason for enrolling at a VEE, as indicated by the respondents, was their desire to start working earlier (32.8%), and also the lack of funds for entering a HEE (24.6%). Only 9% of the respondents noted that they entered a VEE in order to avoid taking the Unified State Exam (USE).

At the same time, the young people from families with high and low resource availability for the most part make quite different choices. Thus, for example, young people from low-income families are more likely to enter a VEE, either free of charge or with a low tuition fee, which is frequently situated close to their home, because they prefer to live with their parents during their studies. Our survey demonstrates that about 80% of the respondents have received their education in the SVE system free of charge. Meanwhile, the share of those who have studied on a paid basis is higher among those who enrolled at a vocational educational establishment after completing 11 grades at a secondary school. This category primarily includes those young people who come from higher-income families, because this was the factor that enabled them to study in grades 10–11. However, as a rule, these young people did not pass the USE very successfully, with flying colors, and they chose to study in a VEE on a contractual

basis in those specialties that they believed to be the most promising ones. Also, their choice of the SVE system after completing the 11th grade may have had to do with their choice of a specialty that requires a certificate of upper secondary education (grade 11, and not grade 9; e.g., the field of information and communications technologies). Among the respondents, 68.3% went on to a VEE after completing the 9th grade; 1.6%, after completing the 10th grade; and 30.1%, after completing the 11th grade. At the same time, the share of those who moved either to another region or to another city inside their home region to continue their studies in the SVE system is higher among those who graduated from grade 11. It should also be noted that young women turn out to be more mobile than young men, as they more frequently moved to another city or region to continue their studies (Fig. 3).

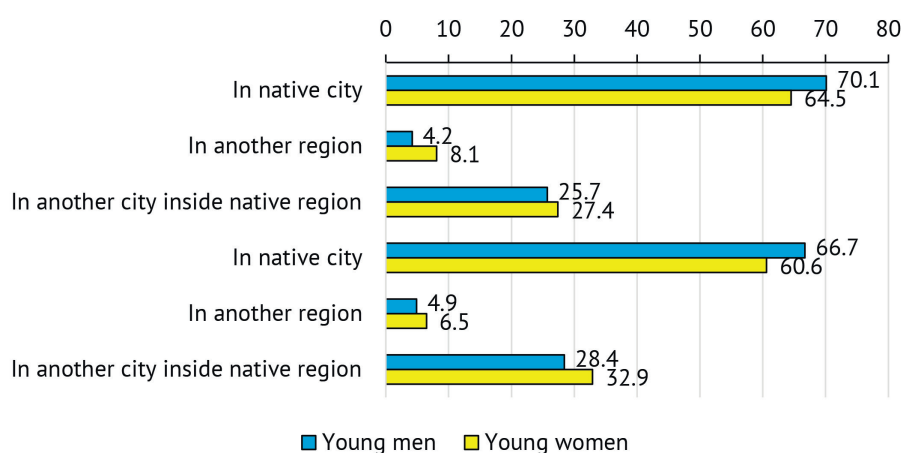


Fig. 3. Educational mobility, by gender and secondary graduation time, %

Source: RANEPa CLLE study.

When evaluating the role of their parents in helping them with their education choice, 34.6% of the respondents stated that their parents had limited opportunities to help them with their studies, and more than half of the respondents (55.5%) admitted that their parents could not help them with getting an education. Only 5.1% of young people noted that their parents had helped them in choosing an educational trajectory, and 4.9% of the respondents found it difficult to answer this question.

The most common way to prepare for entering a VEE, as shown by our survey, is pro-active self teaching (60.2%). Overall, 21.6% of the respondents attended preparatory courses; but this was done by only 4% of young women, and by 19% of young men. About 16.7% of the respondents studied individually with tutors, and 8.8% of the respondents attended group classes. The share of young women among those who invested special effort in preparing for the admission exams (i.e., those who during the survey noted at least one exam preparation method) was higher than that of young men: 36.1% of young men, and only 20.5% of young women, did not indicate any method employed in their preparation for final exams and for the admission exams to a VEE.

Their parents' advice was followed by 36% of young people when choosing a VEE; 20% made this choice based on their interest in their future profession/specialty; 19.6% were interested in one or another specialty because of the ease

5. FAMILY RESOURCES AND YOUTH EDUCATIONAL TRAJECTORY CHOICES

of admission and training; and 14.8% of the respondents pointed out the ease of finding a job after completing their studies as the motive behind their choice.

According to the respondents, they made their choice of a profession/specialty either in their last year of secondary general education school, or after graduation. The reasons varied depending on whether the respondent chose a particular profession deliberately or accidentally. For the respondents who purposefully chose their profession, the main factor was their interest in that profession; while those who chose a profession at random, were guided by the ease of admission and training, and this was pointed out by 27.3% of young men and 24.9% of young women.

The main reason for choosing a non-prestigious specialty was the lack of resources, and this was the answer to that question given by 41.2% of young people; another 20.6% of the respondents noted that they did not care which course to enter; 19.4% chose a non-prestigious specialty because it was more interesting for them; and 15.1% indicated their lack of abilities as a reason for choosing a non-prestigious profession/specialty.

For 24.5% of the respondents, their parents had certain opportunities to help them with finding employment after graduating from a VEE; almost two thirds (67%) of the graduates noted that their parents could not help them with getting a job. Half of the respondents planned to work in their chosen specialty after graduation, and a quarter of the respondents did not rule out such a possibility. The factor of a purposeful or accidental choice of their specialty by the young people also determined their plans for work in the specialty that they received in a VEE: those who chose it randomly were less inclined to stick to their choice. Among those who made a purposeful choice of a profession, the majority of respondents (64.7% of young women and 74.3% of young men) did plan to work in their specialty after graduation. 