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KSE Institute Russia Chartbook

Russia's Overheating Economy Increasingly Hard to Manage

August 2024

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Executive Summary

1. **Economy shows signs of weakness, becomes harder to manage.** Activity across several key sectors slowed in June as a much tighter monetary policy is finally having an impact. But despite the central bank's policy rate reaching 18%—an increase of more than 10 percentage points vs. early-2023 and approaching double digits in real terms—inflation continues to rise. This shows that the war and sanctions economy is becoming much more difficult to manage for authorities, despite robust headline numbers like GDP.
2. **Supportive external environment provides macroeconomic stability.** Despite the current account slipping into deficit in July on the back of weaker exports, stronger imports, and larger services and income deficits, the Jan.-Jul. surplus ($39.7 billion) is almost 70% larger than over Jan.-Jul. 2023. Key driver is a $13.5 increase in the trade surplus. Interestingly, this shift was driven entirely by smaller imports, while exports remained stable as stronger oil earnings were offset by weaker exports of other products.
3. **Weak energy sanctions enforcement remains reason for concern.** The discount on Russian oil export prices—a good proxy for the strength of enforcement of the price cap—reached its lowest level since the start of the full-scale invasion in July at $10.6/barrel. On average, Russia earned almost $15/barrel extra for every barrel of crude oil it sold—or roughly $2.2 billion. One reason for the narrowing discount is that the vessel designation campaign's limited nature has allowed Russia to rebuild shadow fleet capacity.
4. **No major fiscal constraints, but risks to the outlook are increasing.** Over 7M 2024, Russia's federal budget deficit reached 1.4 trillion rubles—64% of the full-year target and 47% less than in 7M 2023. Sharply higher revenues (+36%) more than offset higher spending (+23%). While the country remains on track to reach its 2024 deficit target, significant risks are emerging: a slowing economy, attacks on oil infrastructure, higher spending due to the Kursk situation, and rising borrowing costs.
5. **Reduced buffers to become a problem if the economy slows further.** Russia has already lost access to roughly $300 billion in CBR reserves, which limits the central bank's policy space. Once weakening economic activity impacts budget revenues, the fact that liquid NWF assets have been significantly reduced will turn into a major challenge. The Ministry of Finance will have to rely more heavily on borrowing in the domestic market, where only Russian banks remain as buyers and debt service costs will rise.

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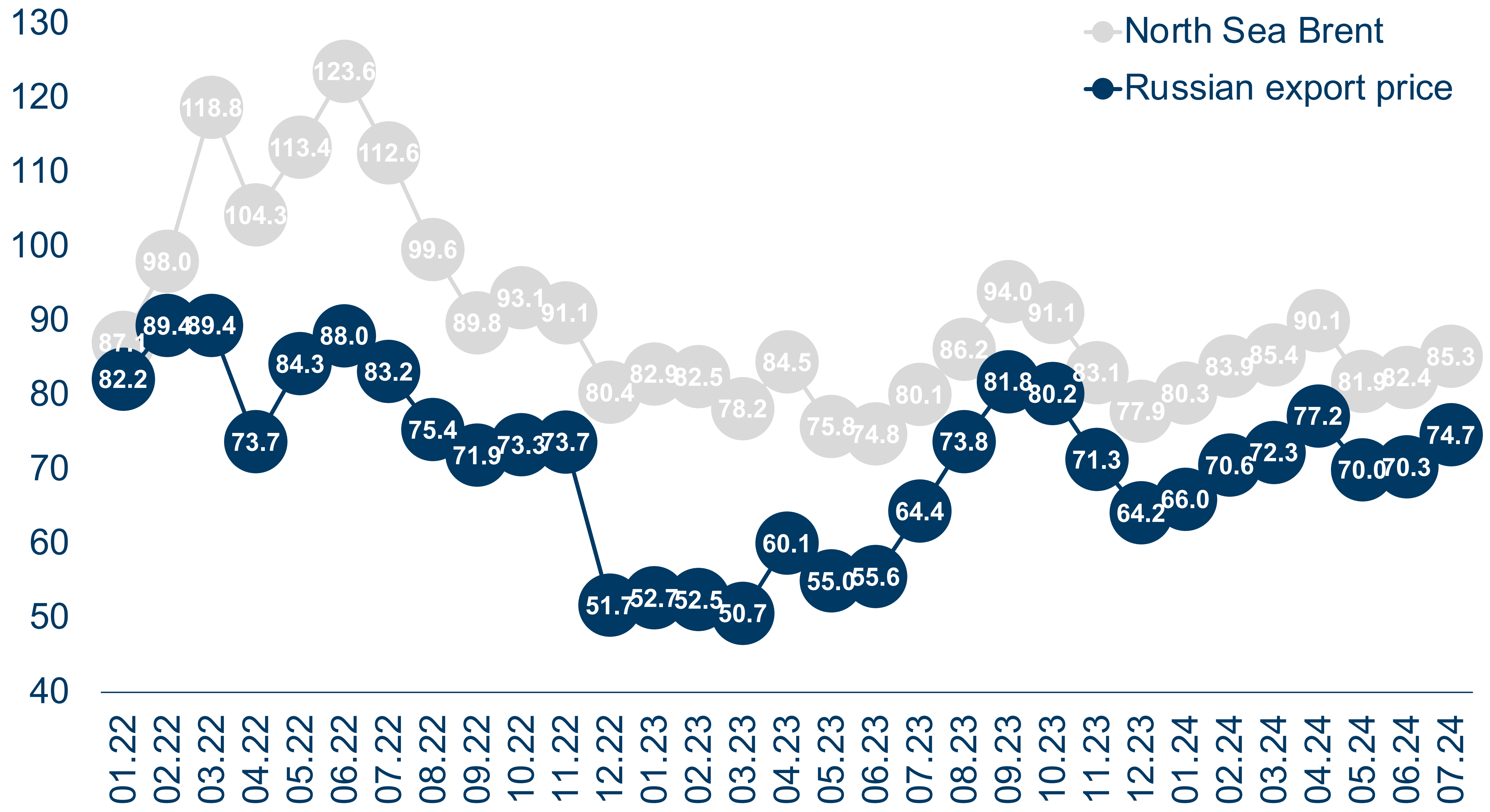
Prices for Russian oil are rising; further action is urgently needed to maintain the price cap’s effectiveness and credibility.

Discount on Russian oil at lowest level since full-scale invasion.

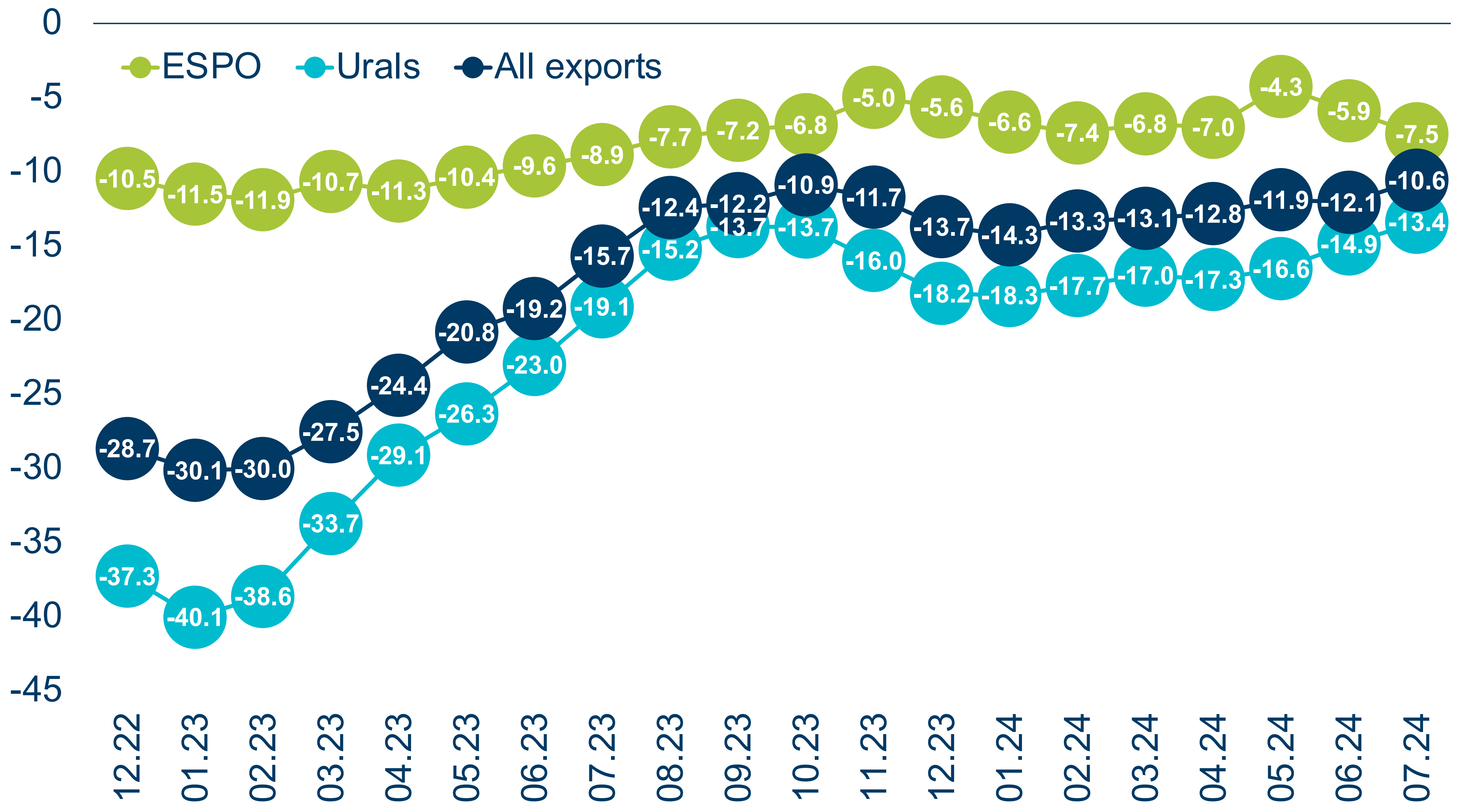
- The widening of the price discount that occurred in the last quarter of 2023 has now been fully reversed.
- The vessel designation campaign’s limited nature has allowed Russia to replace lost transport capacities.
- Together with rising global oil prices, this has led to an average export price of close to $75/barrel in July.

Crude oil prices, in U.S. dollar/barrel*



Source: Federal Customs Service, International Energy Agency, KSE Institute
*export price until November 2022 from Russian customs, all other numbers from IEA

Discount of Russian export prices vs. Brent, in U.S. dollar/barrel

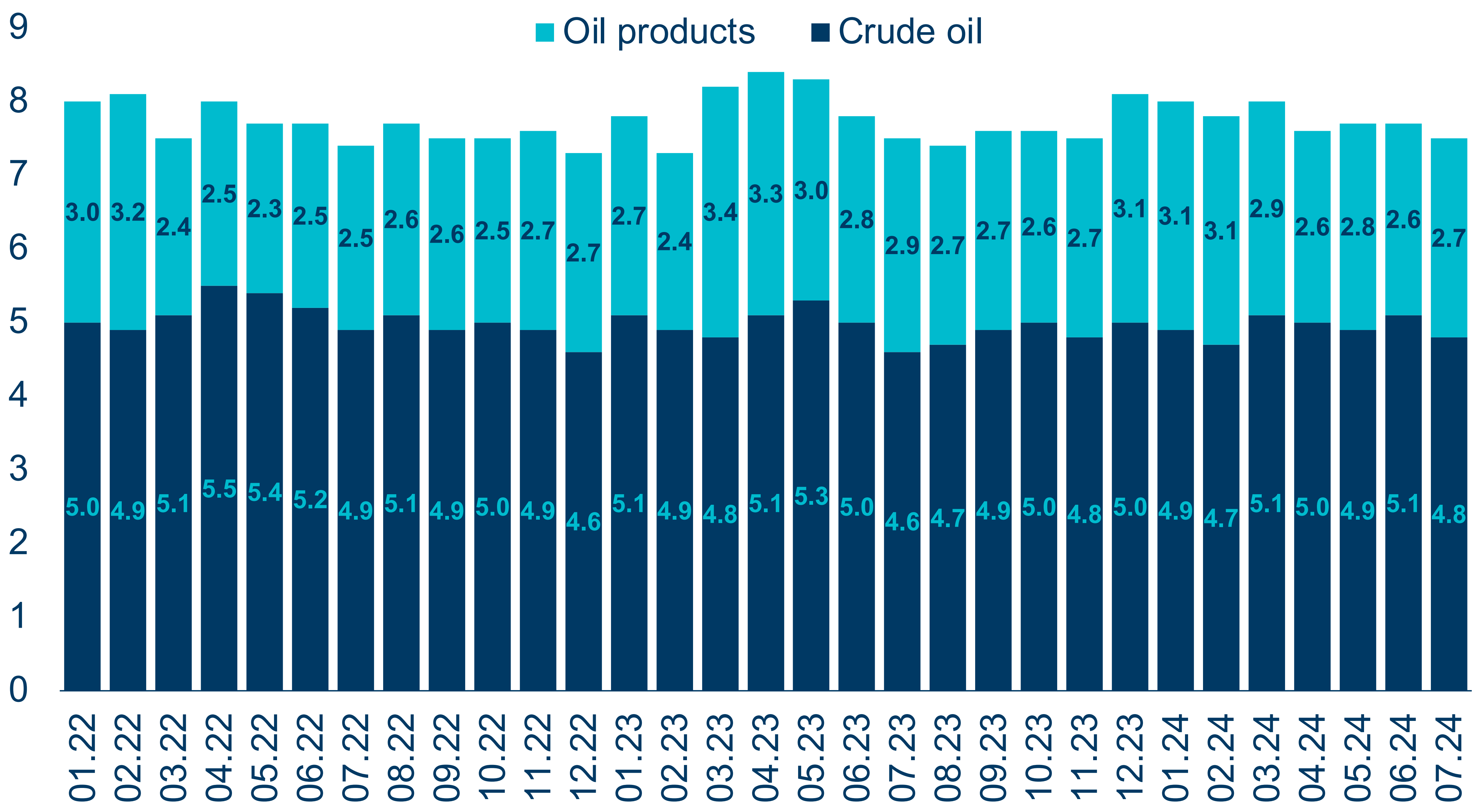


Source: International Energy Agency, KSE Institute

Supply of Russian oil to the global market remains stable.

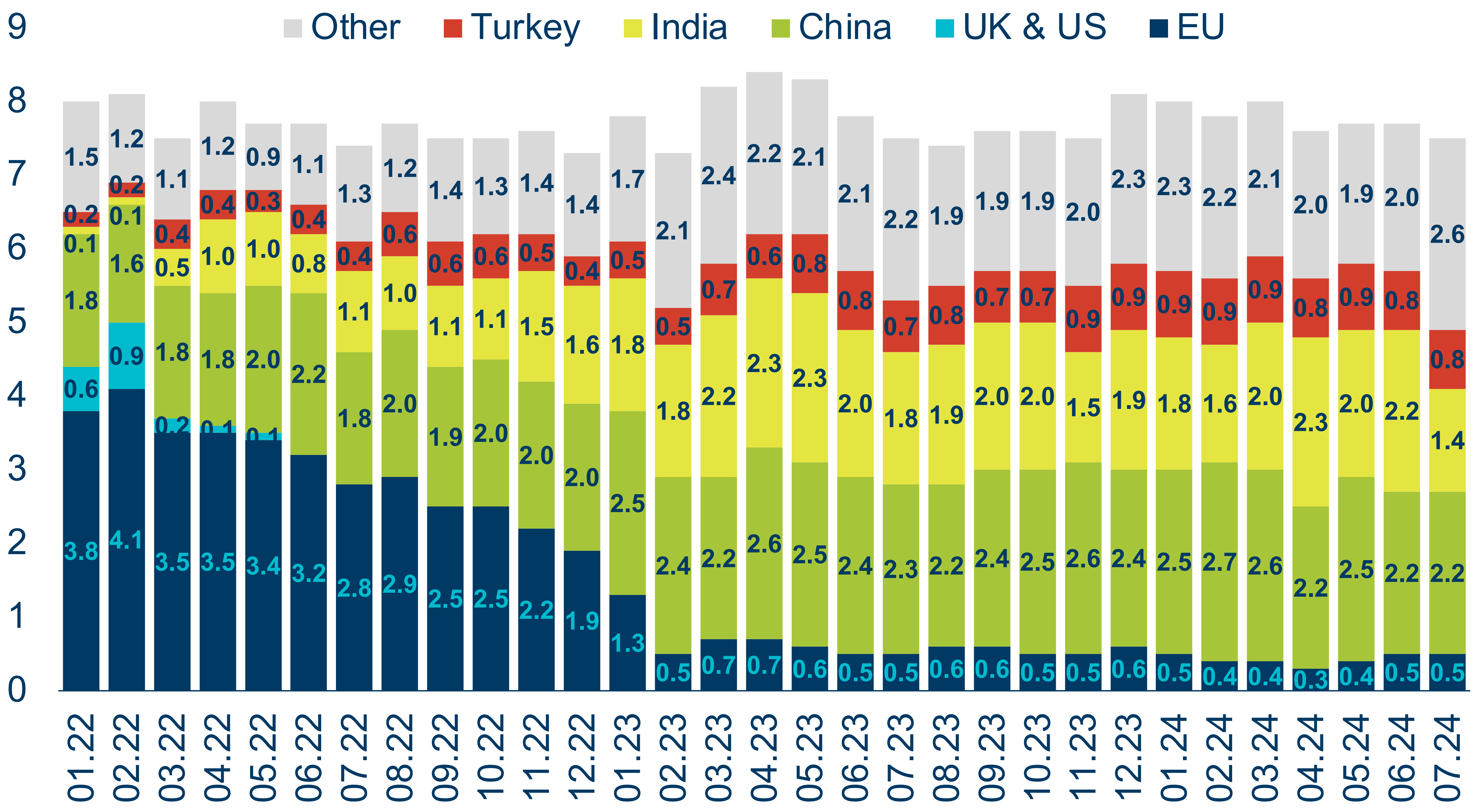
- Russian oil export volumes have been remarkably steady over the last 2.5 years despite sanctions.
- Thus, the price cap has succeeded at keeping Russian oil on the market and prevent supply issues.
- China, India, and Turkey are the most important buyers, together accounting for 60-70% of exports.

Russian oil export volume by type, in million barrels/day*



Source: International Energy Agency, KSE Institute *March 2024 = KSE Institute estimate

Russian oil export volume by destination, in million barrels/day*



Source: International Energy Agency, KSE Institute *no March data from IEA

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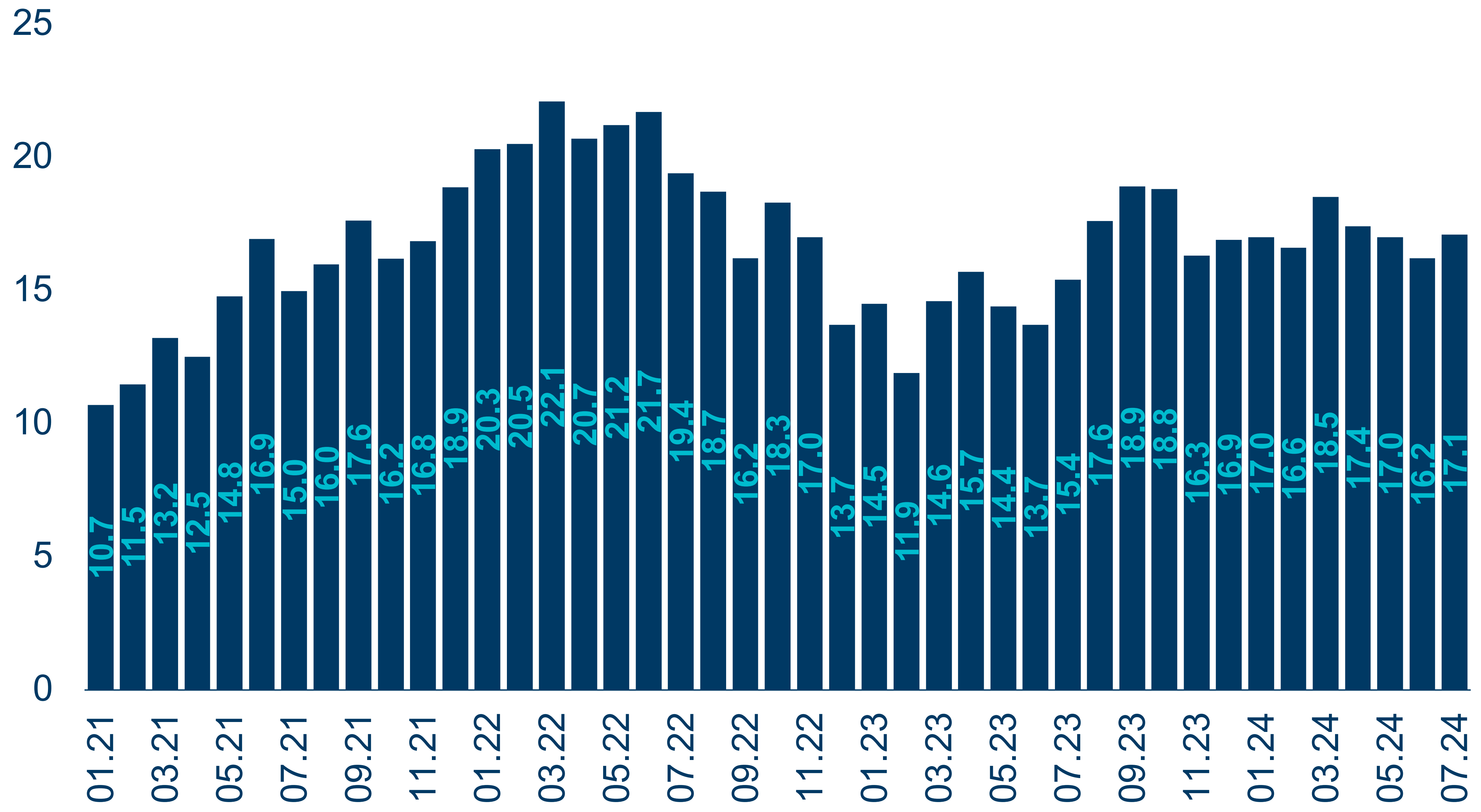
Ineffective price cap helps Russia with exports and budget revenues.

- In Jan.-Jul., oil export earnings averaged $17.1 billion vs. $17.3 billion in H2 2023 and $14.1 billion in H1 2023.
- Budget revenues from oil were also roughly unchanged compared to H2 2023 but 75% higher than in H1 2023.
- Russia's ability to fund its government and, thus, its war in Ukraine appears largely unconstrained by oil sanctions.

Oil export earnings, in U.S. dollar billion



Source: Federal Customs Service, International Energy Agency, KSE Institute
*2021 data from Russian customs service, 2022-23 data from IEA

Federal budget oil revenues, in ruble billion*

Source: Ministry of Finance, KSE Institute *includes extraction tax and export duty

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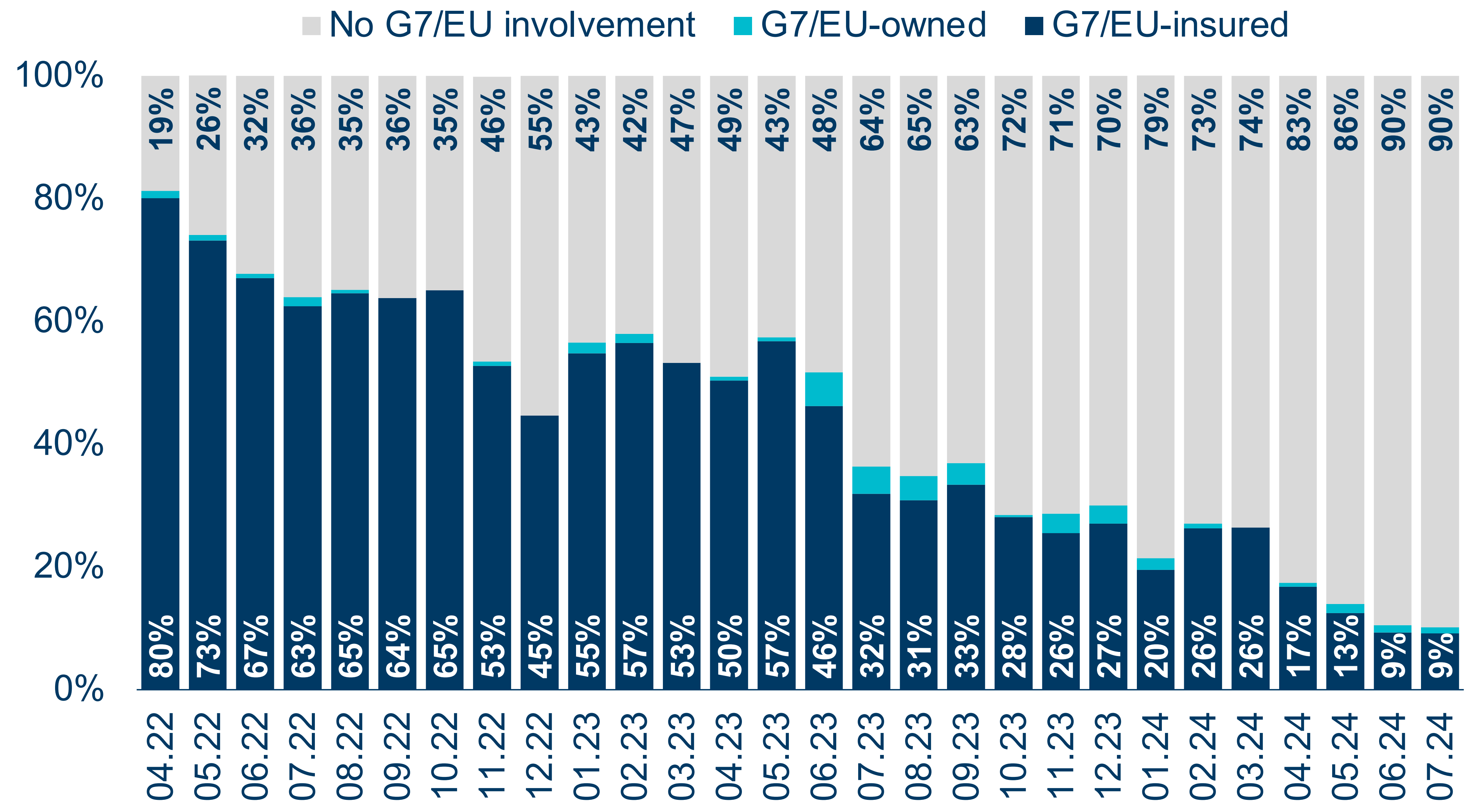
Shadow fleet has fundamentally eroded the price cap’s leverage.

- Russia’s shadow fleet of 430+ tankers allows it to evade the price cap for a large share of its oil exports.
- In July 2024, close to 90% of seaborne crude oil was transported without involvement of G7/EU services.
- For this portion, Russia is currently able to realize an average price that lies $15/barrel above the cap.

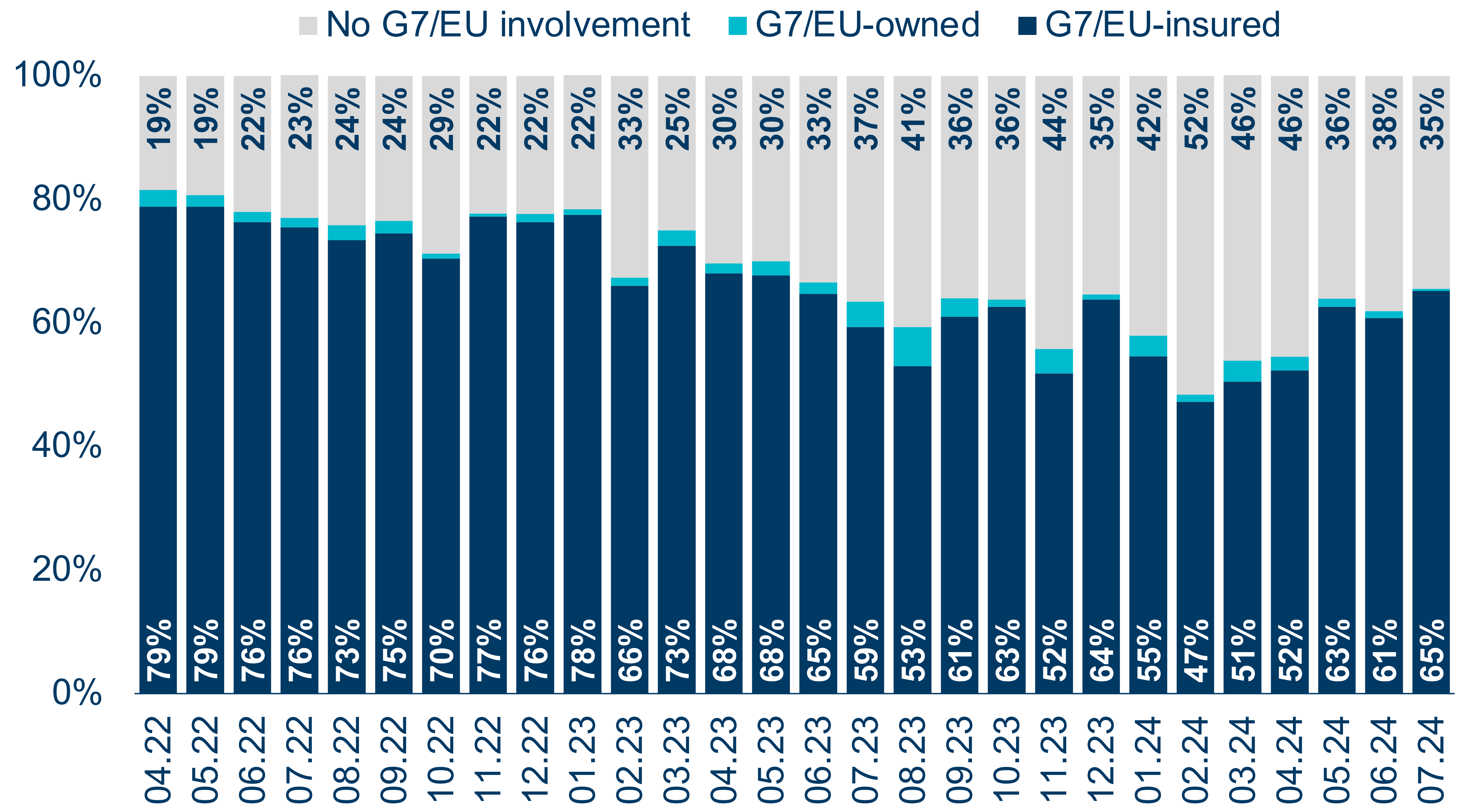
Read KSE Institute’s in-depth assessments of the shadow fleet here and here.

Composition of seaborne crude oil exports, in %



Source: Equasis, Kpler, P&I Clubs, KSE Institute

Composition of seaborne oil product exports, in %



Source: Equasis, Kpler, P&I Clubs, KSE Institute

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Designations have largely removed shadow tankers from operations.

- A total 64 shadow fleet tankers have been sanctioned by the United States, European Union, and United Kingdom.
- Most have effectively been removed from commercial operations as entities in third countries fear any involvement.
- Designations remain a powerful tool to rein in the shadow fleet, which should be scaled up gradually going forward.

Current status of designated vessels

Name	Designated by	Status	Name	Designated by	Status	Name	Designated by	Status
Adygeya	UK	Underway*	Hs Legend	US	Ballast/drifting	Ns Spirit	EU	Loaded/drifting
Anatoly Kolodkin	US	Ballast/drifting	Hs Star	US	Underway	Ns Stream	EU	Loaded/drifting
Andromeda Star	EU	Loaded/drifting	Kaliningrad	US EU	Ballast/drifting	Ocean AMZ	UK EU	Ballast/drifting
Antarktika	US	Ballast/drifting	Kareliya	US	Ballast/drifting	Pictor	US	Ballast/drifting
Apus	US	Part. loaded/drifting	Kazan	US	Ballast/drifting	Primorsky Prospect	UK	Ballast/drifting
Aristo	US	Part. loaded/drifting	Kemerovo	US EU	Ballast/drifting	Robon	UK EU	Ballast/drifting
Avril	US	Ballast/drifting	Korolev Prospect	UK	Underway	Rocky Runner	UK	Ballast/drifting
Beks Aqua	EU	Ballast/drifting	Kotlas	US	Ballast/drifting	Sakhalin Island	US	Ballast/drifting
Belgorod	US	Underway	Krasnoyarsk	US EU	Ballast/drifting	Sanar 15	US	Loaded/drifting
Bettle	US	Ballast/drifting	Kruger	US	Ballast/drifting	Sara Ii	US	Ballast/drifting
Bratsk	US	Planned voyage	Krymsk	US EU	Ballast/drifting	Scf Amur	EU UK	Ballast/drifting
Canis Power	UK EU	Ballast/drifting	La Pride	US	Ballast/drifting	Scf Pechora	UK	Planned voyage
Dynamik Trader	UK	Planned voyage	Ligovsky Prospect	US	Ballast/drifting	Scf Primorye	US	Ballast/drifting
Fighter Two	UK	Loaded, floating storage	Liteyny Prospect	US	Ballast/drifting	Sensus	US	STS transfer
Galian 2	EU	Ballast/drifting	Mona	US	Ballast/drifting	Vasily Lanovoy	US	Underway
Georgy Maslov	US	Ballast/drifting	Nellis	US	Ballast/drifting	Vela Rain	EU	Ballast/drifting
Hai Ii	US	Ballast/drifting	Nevskiy Prospect	US	Ballast/drifting	Viktor Bakaev	US	Underway
Hana	EU	Ballast/drifting	Ns Commander	UK	Ballast/drifting	Zaliv Amurskiy	UK	Ballast/drifting
Hebe	US EU	Planned voyage	Ns Consul	US	Ballast/drifting			
Hs Buraq	US	Ballast/drifting	Ns Laguna	UK	Ballast/drifting			
Hs Esberg	US	Ballast/drifting	Ns Leader	US	Ballast/drifting			
Hs Everett	US	Ballast/drifting	Ns Lion	US	Ballast/drifting			
Hs Glory	US	Ballast/drifting	Ns Lotus	EU UK	Ballast/drifting			

Green – out of commercial operations
Yellow – in operation, monitoring required
Red – completed voyage, investigation needed
– completed voyage after designation
*loaded before designation

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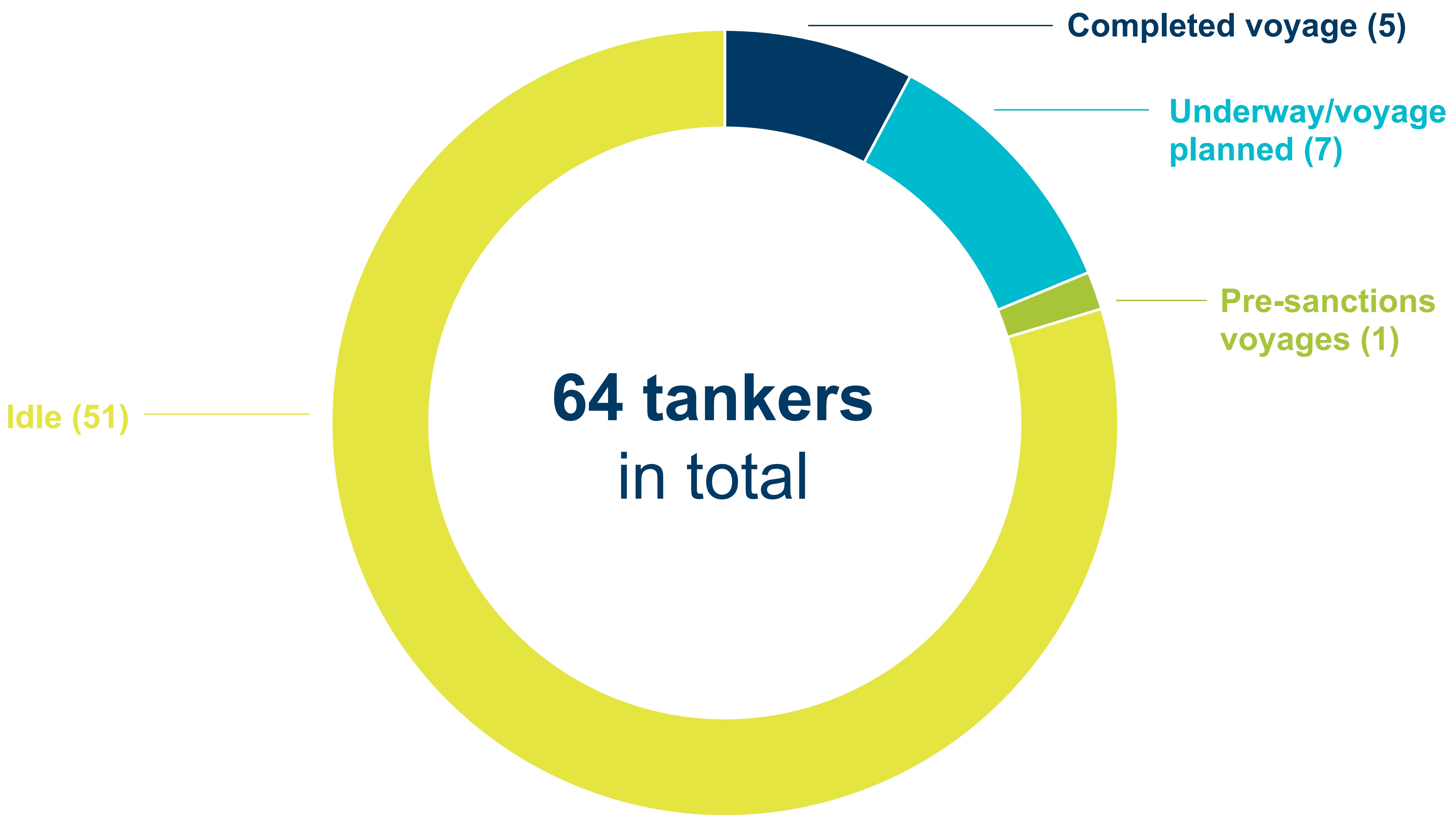
Individual cases deserve attention and should result in enforcement action.

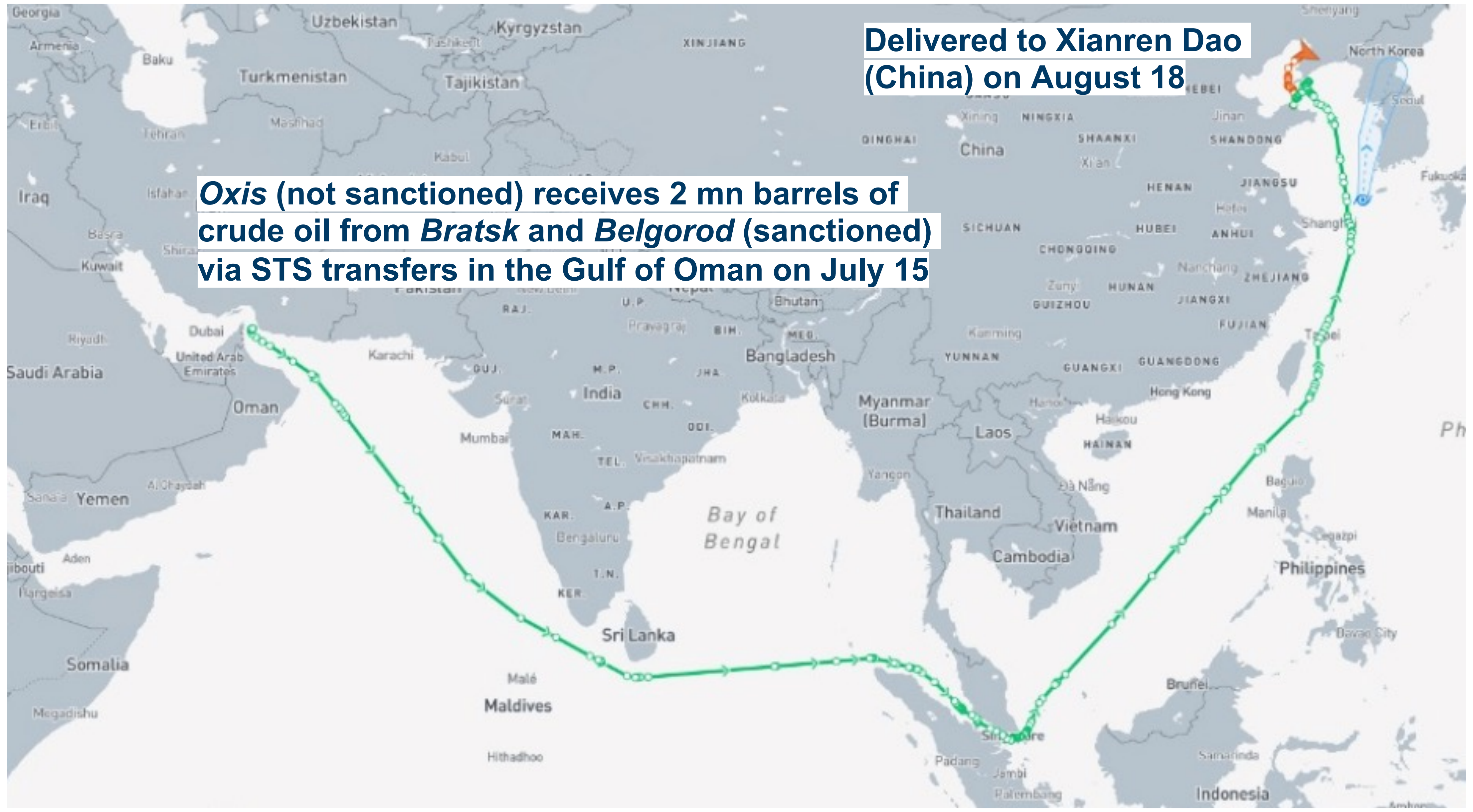
- Of the 64 sanctioned shadow tankers, five are suspected to have completed voyages since the designation.
- To preserve the credibility of vessel designations, enforcement action against involved entities is critical.
- Several additional tankers are underway or have voyages scheduled; this requires additional monitoring.

Status of designated vessels



Source: Kpler, KSE Institute *vessel was underway at time of designation

Designated vessel with completed voyage: Bratsk



Source: Kpler, KSE Institute

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External conditions remain supportive; weak sanctions enforcement helps Russia; hard currency inflows have fallen sharply.

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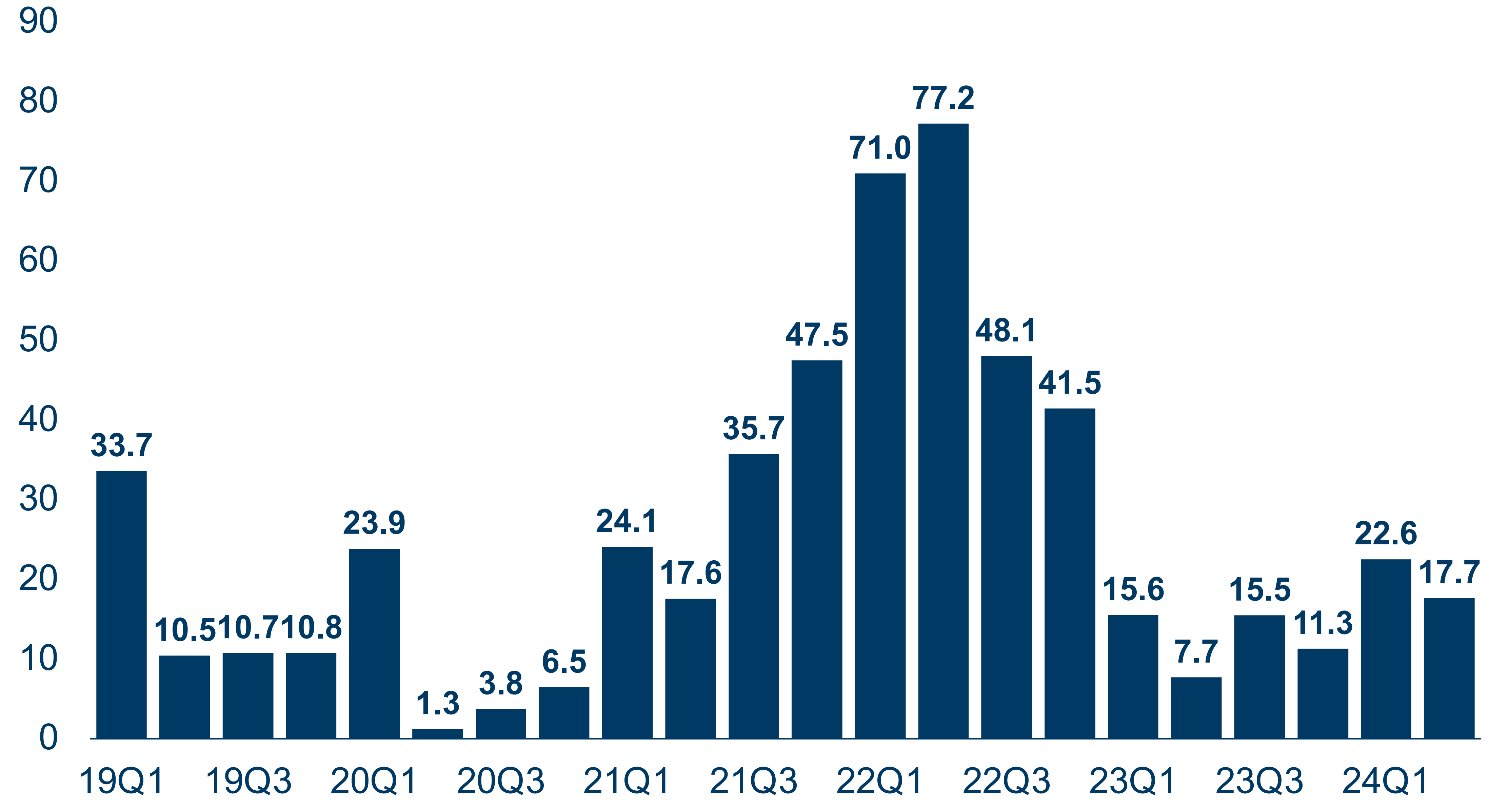
External environment has become more supportive in 2024.

- The current account slipped into deficit in July (-$0.5 billion) after recording a surplus of $5.1 billion in June.
- This was driven by weaker exports, higher imports, and larger deficits for services, and income & transfers.
- Nevertheless, the Jan.-Jul. 2024 surplus of $39.7 billion is almost 70% bigger than the one in Jan.-Jul. 2023.

Quarterly current account balance, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

Composition of the current account, in U.S. dollar billion

	C/A	Goods			Services			Income & transfers		
Time period	Bal.	Bal.	Exp.	Imp	Bal.	Cred.	Deb.	Bal.	Cred.	Deb.
Q1 2024	22.6	33.8	100.9	67.1	-7.3	10.2	17.4	-3.9	8.6	12.5
Q2 2024	17.7	34.8	105.7	70.9	-9.6	9.6	19.1	-7.5	10.1	17.7
Apr. 2024	7.1	11.2	33.6	22.4	-2.6	3.1	5.7	-1.5	3.5	5.0
May 2024	5.5	12.2	36.8	24.7	-3.3	3.2	6.5	-3.3	3.5	6.8
June 2024	5.1	11.5	35.3	23.8	-3.7	3.2	6.9	-2.7	3.2	5.9
July 2024	-0.5	8.1	32.6	24.5	-4.2	3.2	7.4	-4.4	3.4	7.8
Jan.-Jul. 2024	39.7	76.6	239.2	162.6	-21.0	23.0	44.0	-15.9	22.1	38.0
Memorandum: 2021	125.0	193.1	494.2	301.0	-20.3	55.6	75.9	-47.8	96.3	144.1
2022	237.7	315.6	592.1	276.5	-22.1	48.8	70.9	-55.8	51.0	106.8
2023	50.1	121.6	424.5	302.9	-35.3	41.2	76.4	-36.2	44.8	81.0
Q1 2023	15.6	30.5	105.1	74.6	-7.6	9.9	17.5	-7.3	11.4	18.7
Q2 2023	7.7	26.3	103.4	77.1	-8.9	10.4	19.3	-9.6	12.7	22.3
Apr 2023	0.3	6.8	31.6	24.8	-2.4	3.3	5.8	-4.0	4.1	8.1
May 2023	5.5	10.4	37.4	26.9	-3.1	3.4	6.4	-1.9	3.7	5.6
June 2023	2.0	9.0	34.5	25.4	-3.4	3.6	7.0	-3.7	4.9	8.5
July 2023	0.2	6.2	31.7	25.5	-3.7	3.2	6.9	-2.2	3.4	5.6
Jan.-Jul. 2023	23.5	63.0	240.2	177.2	-20.2	23.4	43.6	-19.2	27.4	46.7

Source: Bank of Russia, KSE Institute

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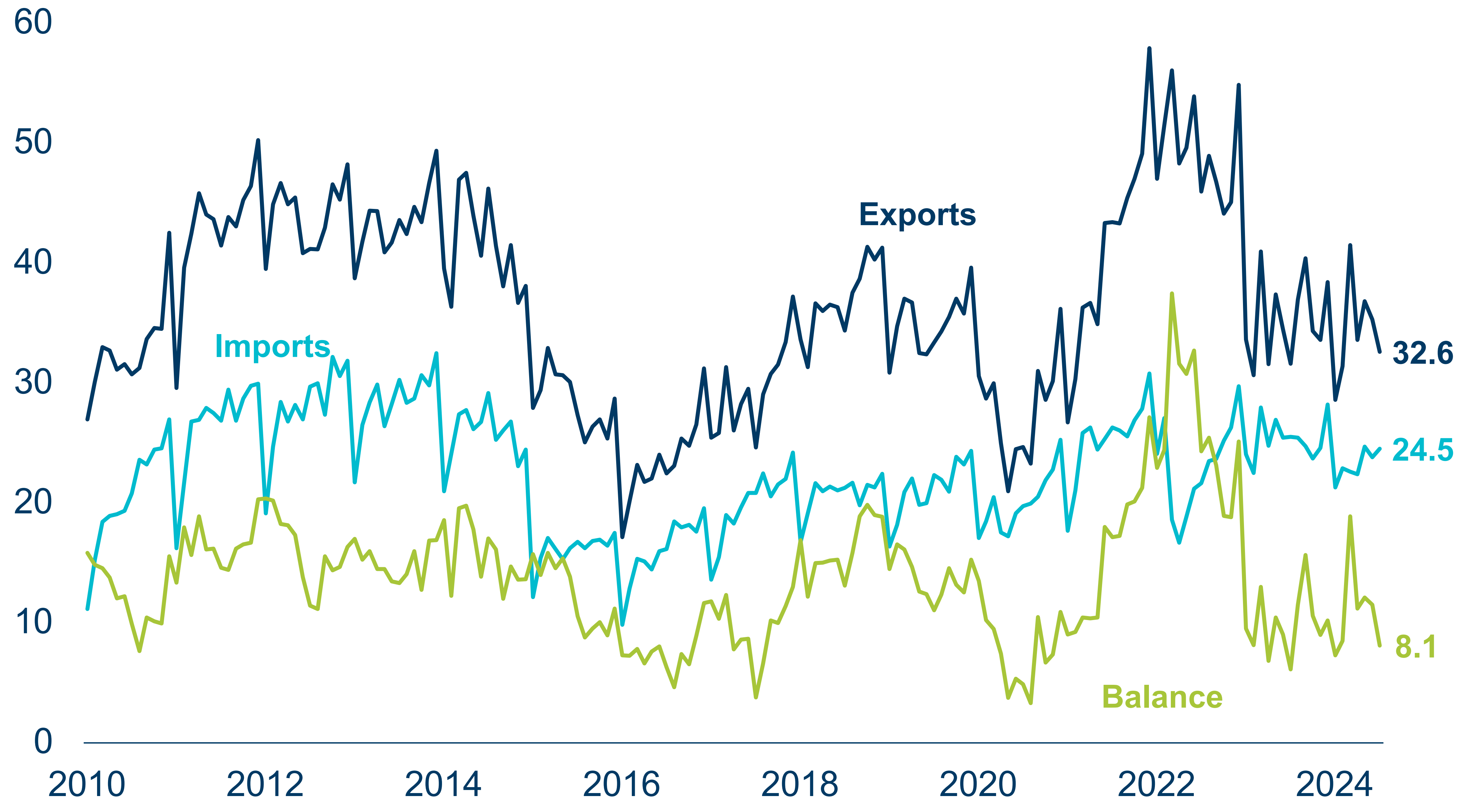
Foreign trade has settled in at a new post-full scale invasion baseline.

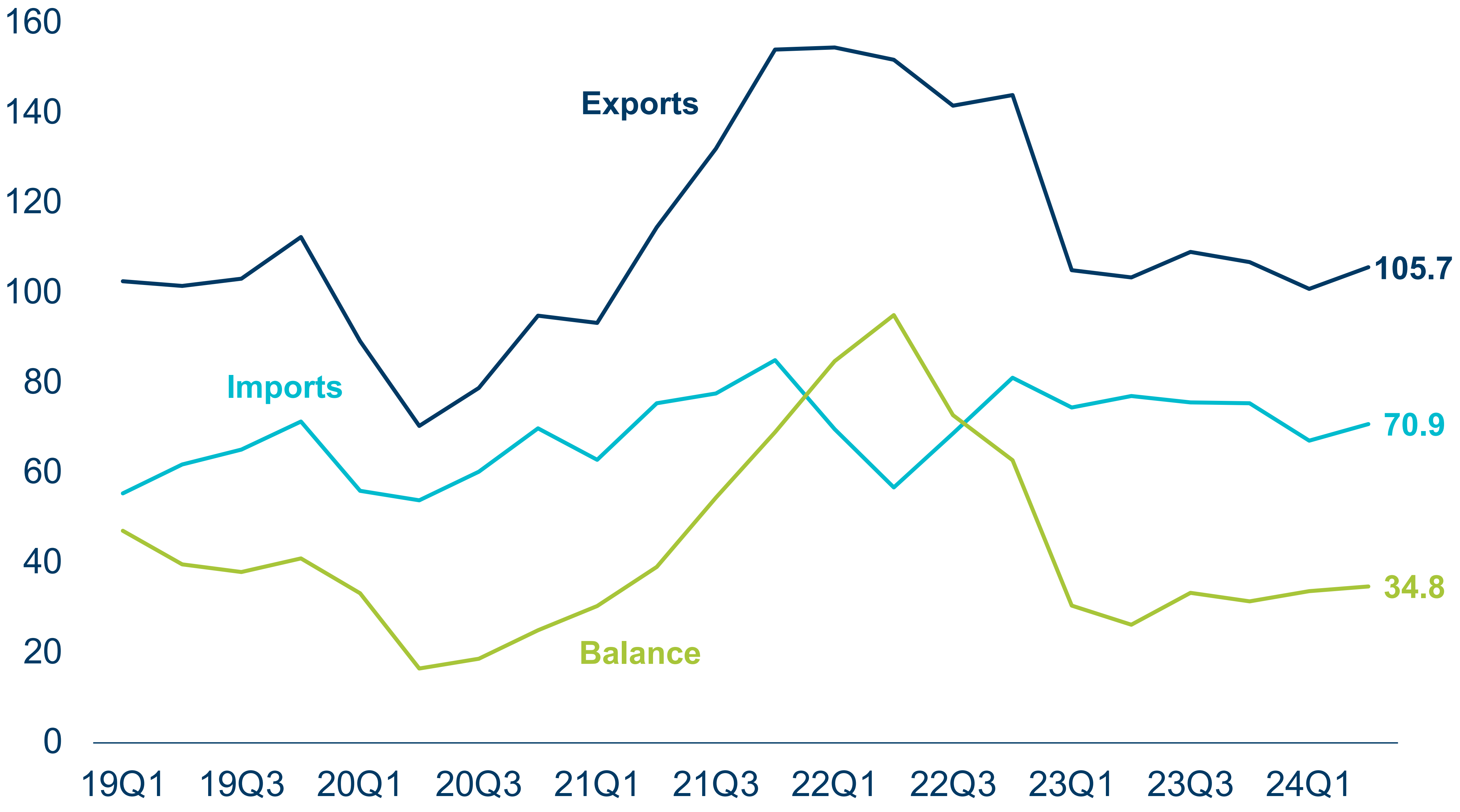
- Russia's foreign trade has stabilized at a new baseline of ~$100 billion in exports and ~$75 billion in imports per quarter.
- This represents a significant change to 2022 when soaring commodity prices drove up exports while imports weakened.
- However, any further erosion of Russia's external accounts will require more decisive measures on the sanctions front.

Monthly trade statistics, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

Quarterly balance of payments statistics, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

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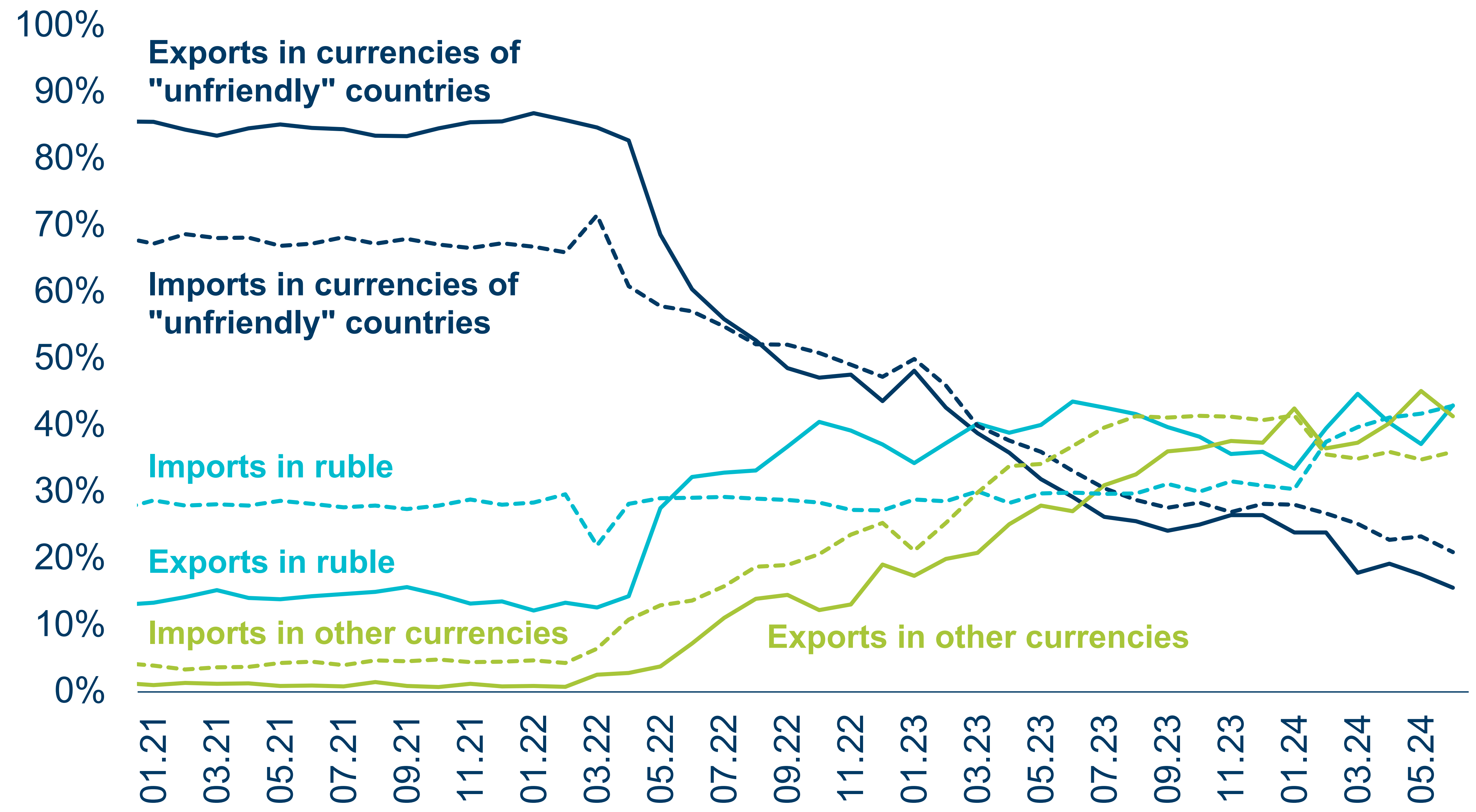
Change to currency composition of trade creates hard currency shortage.

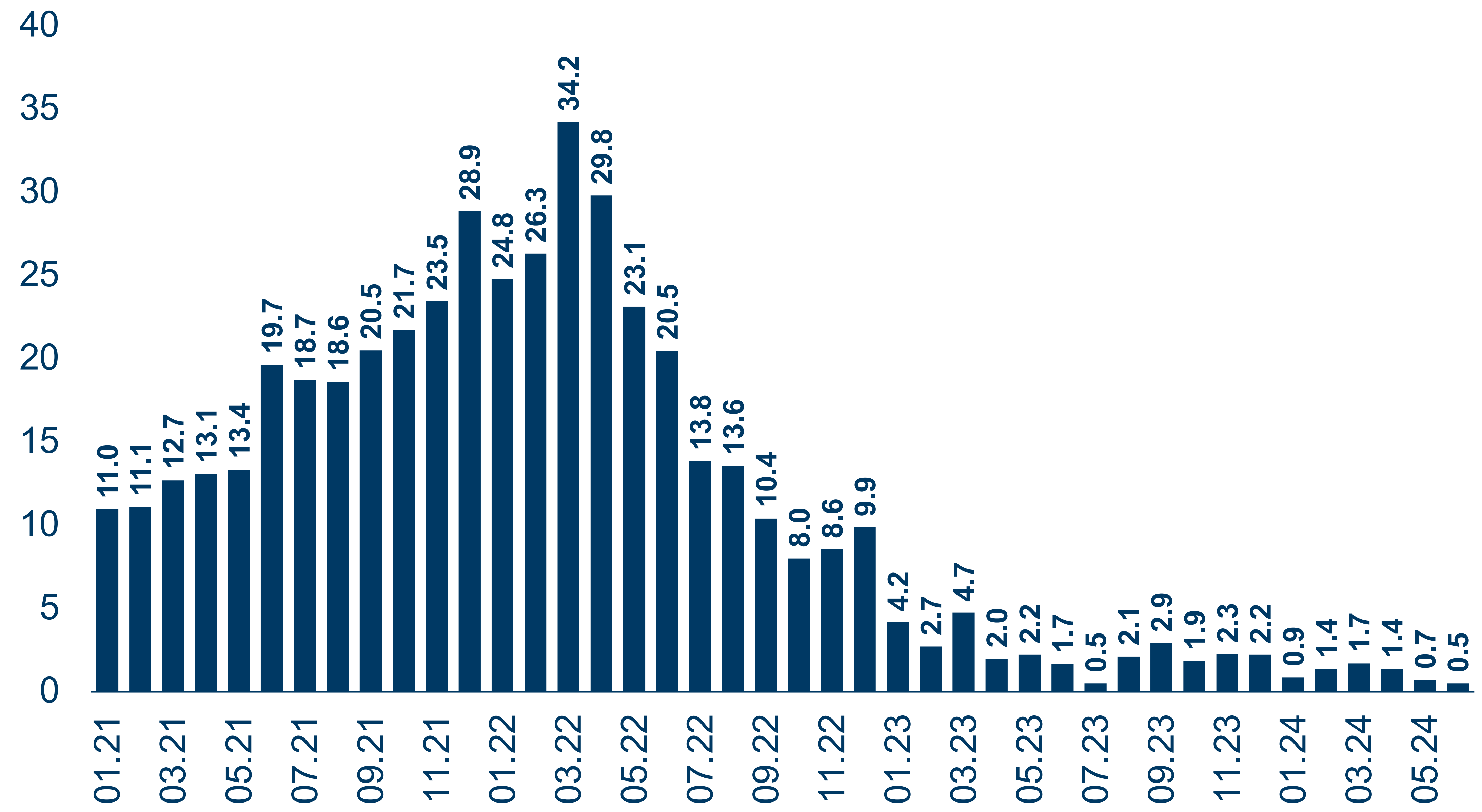
- The share of “unfriendly” countries’ currencies (e.g., USD, EUR, GBP, JPY, CHF) in Russian trade has fallen sharply.
- Other currencies have risen for both exports and imports, while the ruble has gained importance mostly for exports.
- These shifts have created a shortage of hard currency as net inflows from goods trade have essentially disappeared.

Currency composition of Russia’s foreign trade, in %



Source: Bank of Russia

Net inflows of hard currency from goods trade, in $ billion*



Source: Bank of Russia, KSE Institute *includes currencies of “unfriendly” countries

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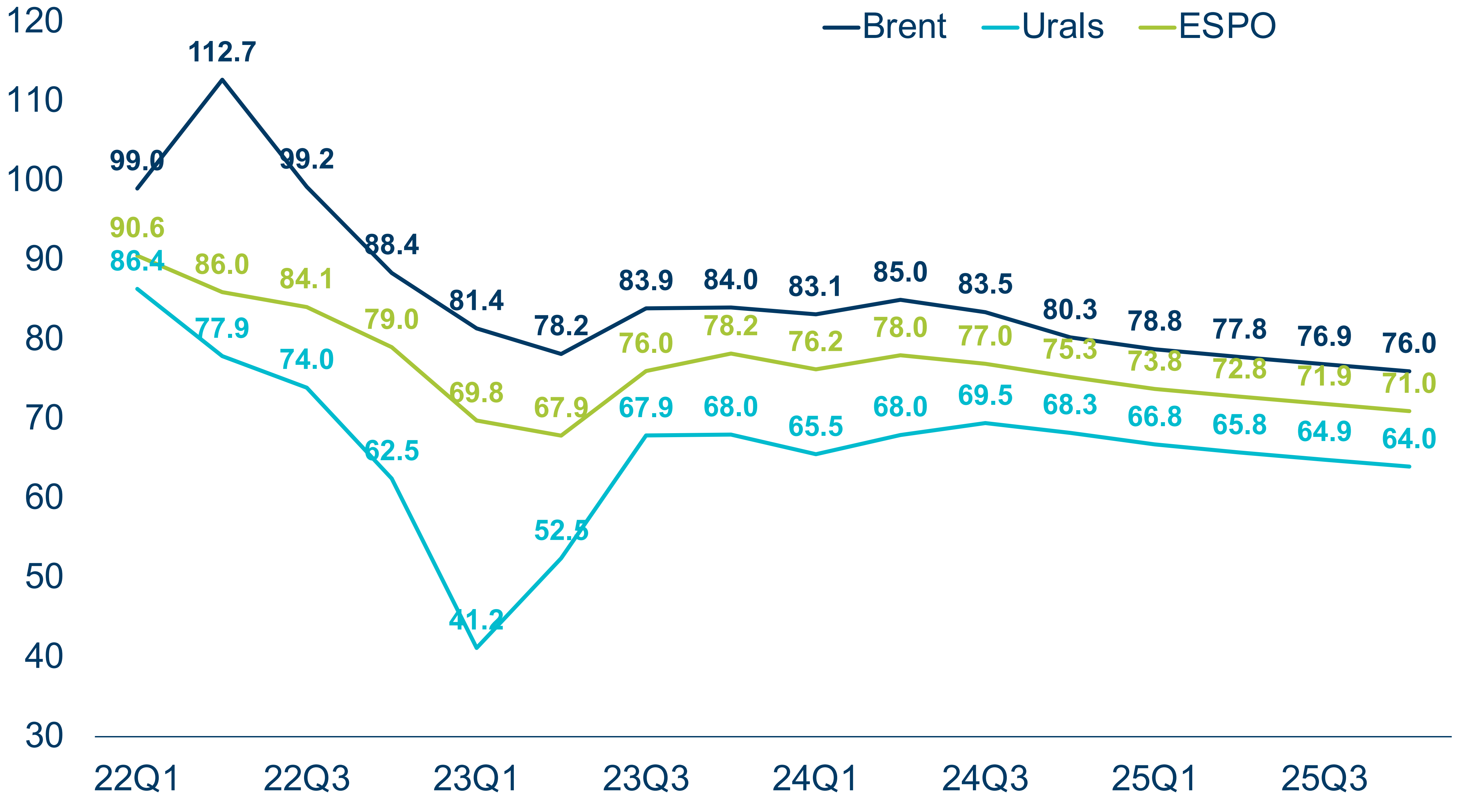
Weak sanctions enforcement scenario is increasingly likely.

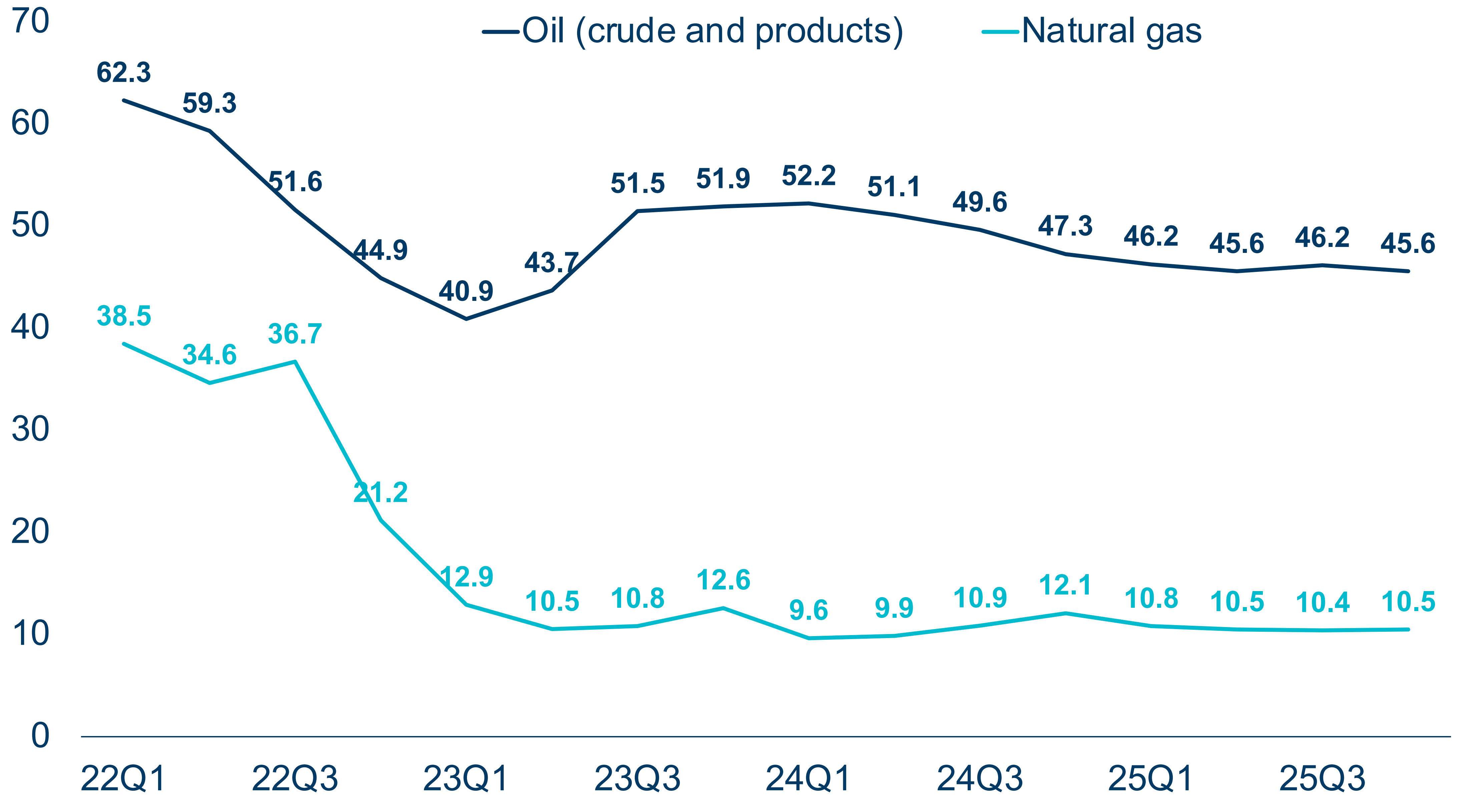
- It looks increasingly likely that our bearish scenario of weak energy sanctions enforcement is materializing.
- This scenario assumes an Urals discount of $12/barrel and an ESPO discount of $5/barrel going forward.
- In this situation, Russia would be able to generate significantly higher oil export earnings vs. the base case.

Oil prices, in U.S. dollar/barrel



Source: KSE Institute

Oil and gas export earnings, in U.S. dollar billion



Source: KSE Institute

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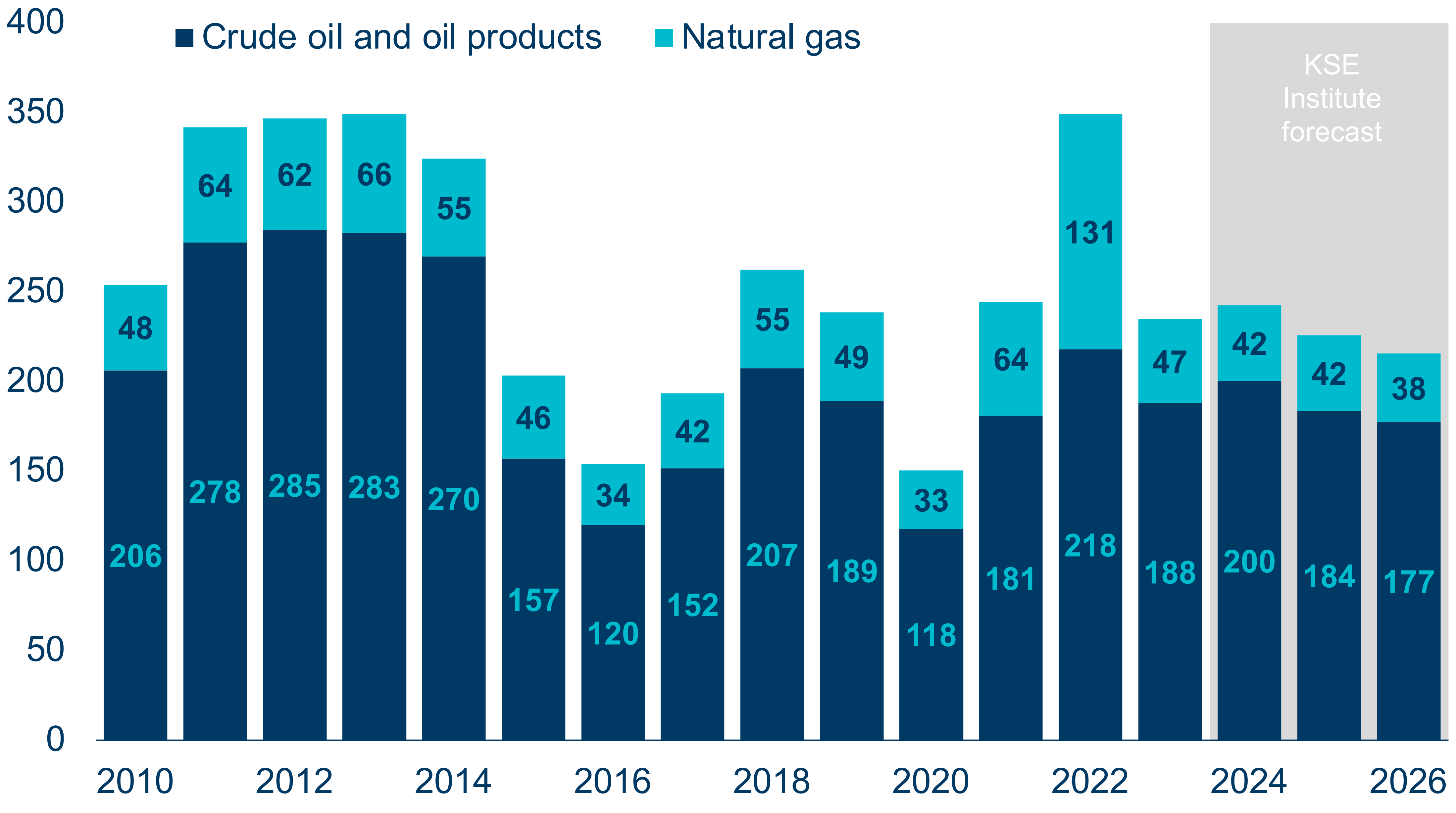
Current account surplus to improve markedly this year.

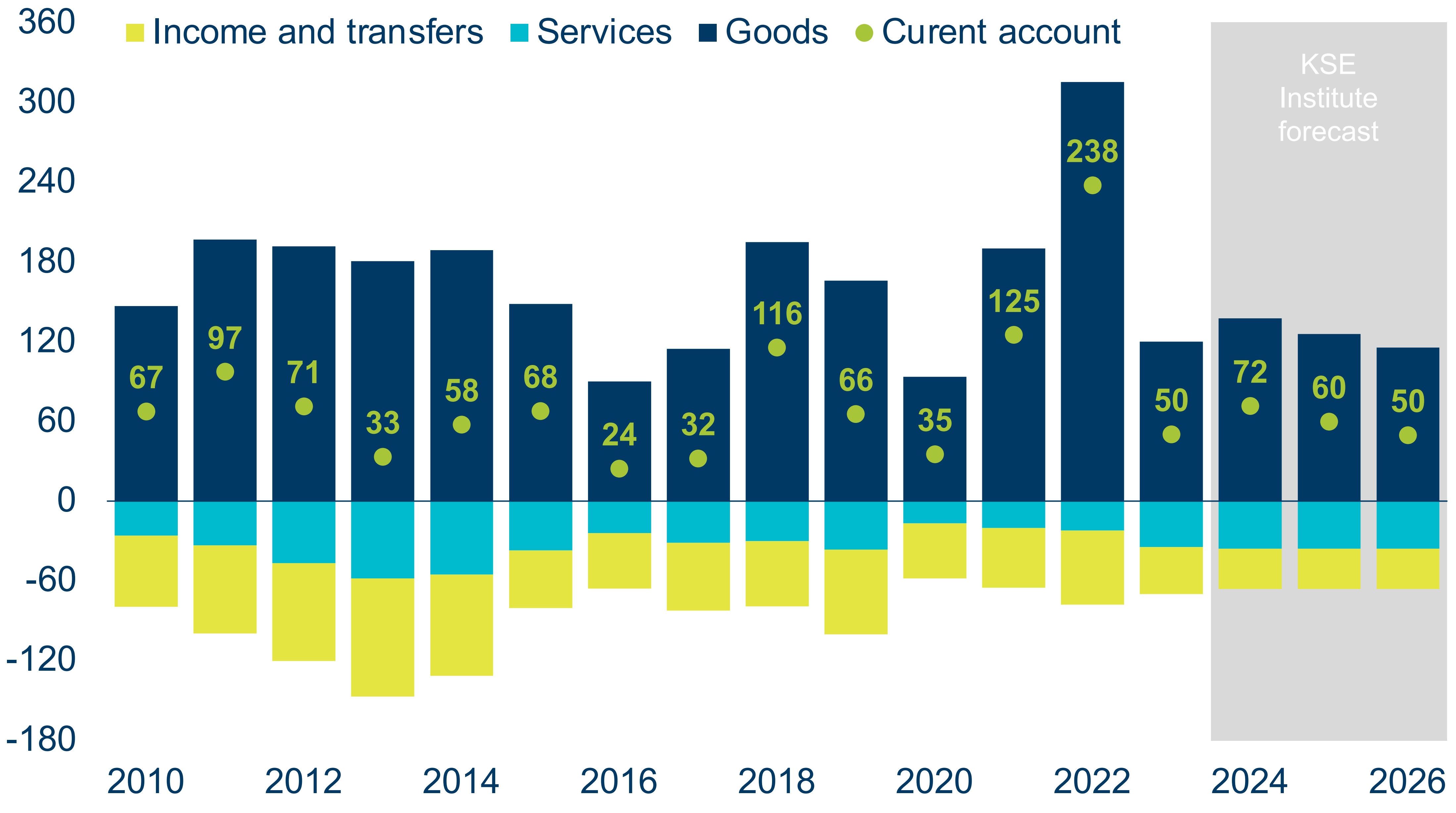
- O&G exports are projected to rise to $243 billion in 2024 (vs. $235 billion in 2023) before declining to $226 billion in 2025.
- As a result, the current account surplus is set to rise to $72 billion this year and $60 billion next (vs. $51 billion in 2023).
- In terms of its external accounts, this leaves Russia in a quite comfortable position and will limit any depreciation pressure.

Oil and gas earnings, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

Current account and components, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

Robust revenues keep deficit contained despite significantly higher spending; budget vulnerable in case of economic slowdown.

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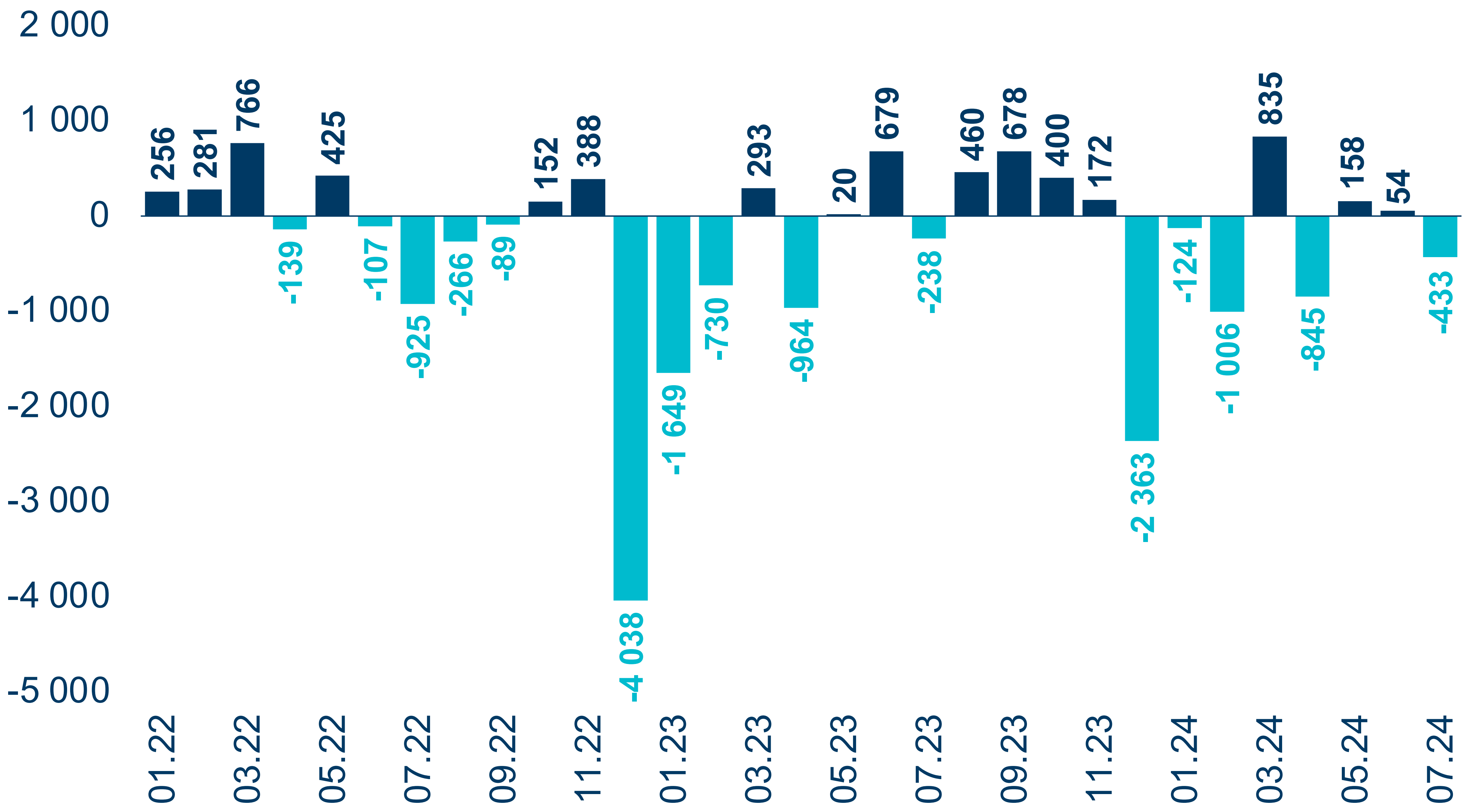
Sharp rise in revenues significantly improved fiscal situation.

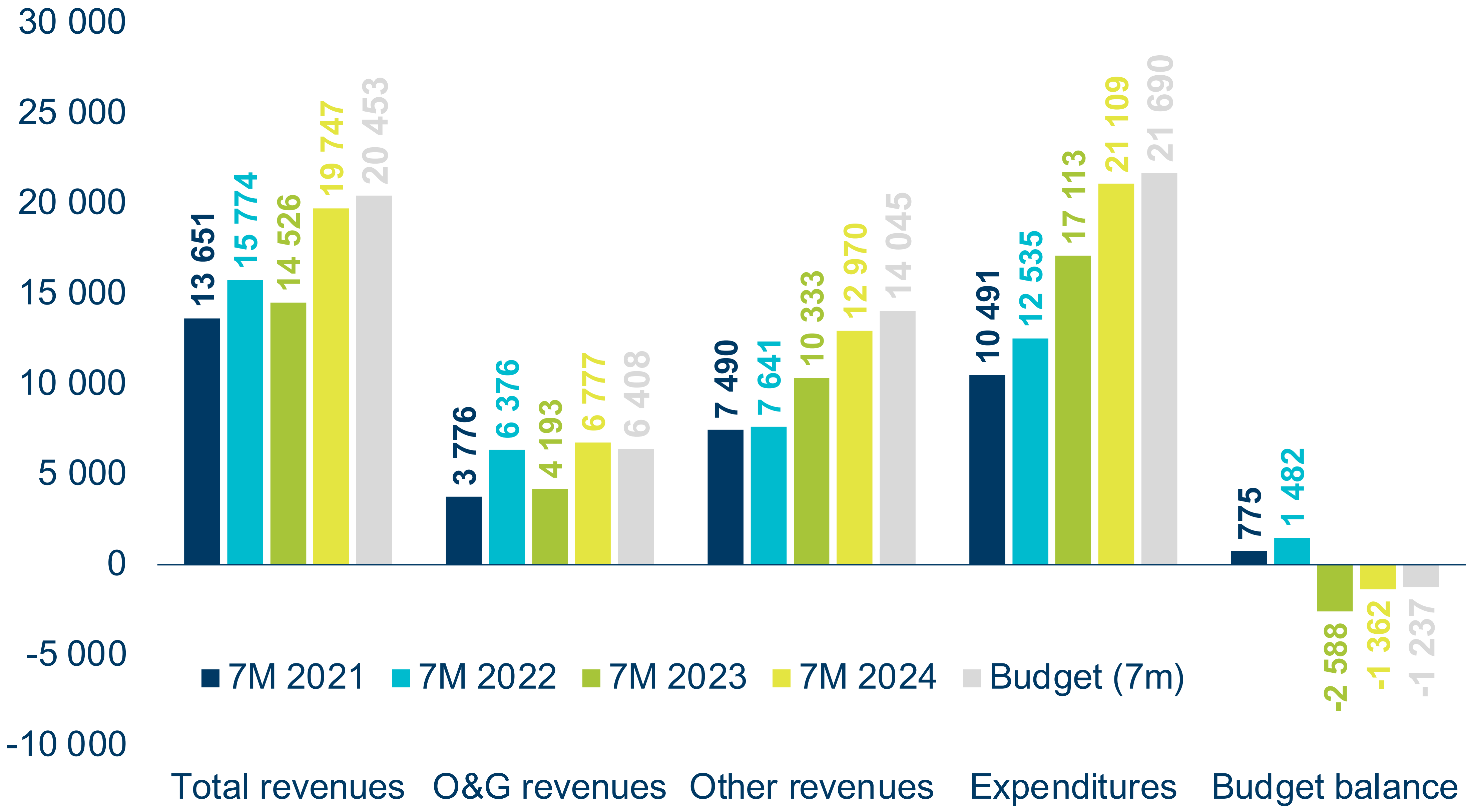
- In January-July 2024, Russia's federal budget deficit reached 1.4 trillion rubles, 64% of the full-year plan.
- O&G revenues were 62%, non-O&G revenues 26%, and expenditures 23% higher vs. January-July 2023.
- It is unlikely that Russia will face any serious fiscal constraints that would affect planned military spending.

Federal government balance, in ruble billion



Source: Ministry of Finance, KSE Institute

Revenues and expenditures, in ruble billion

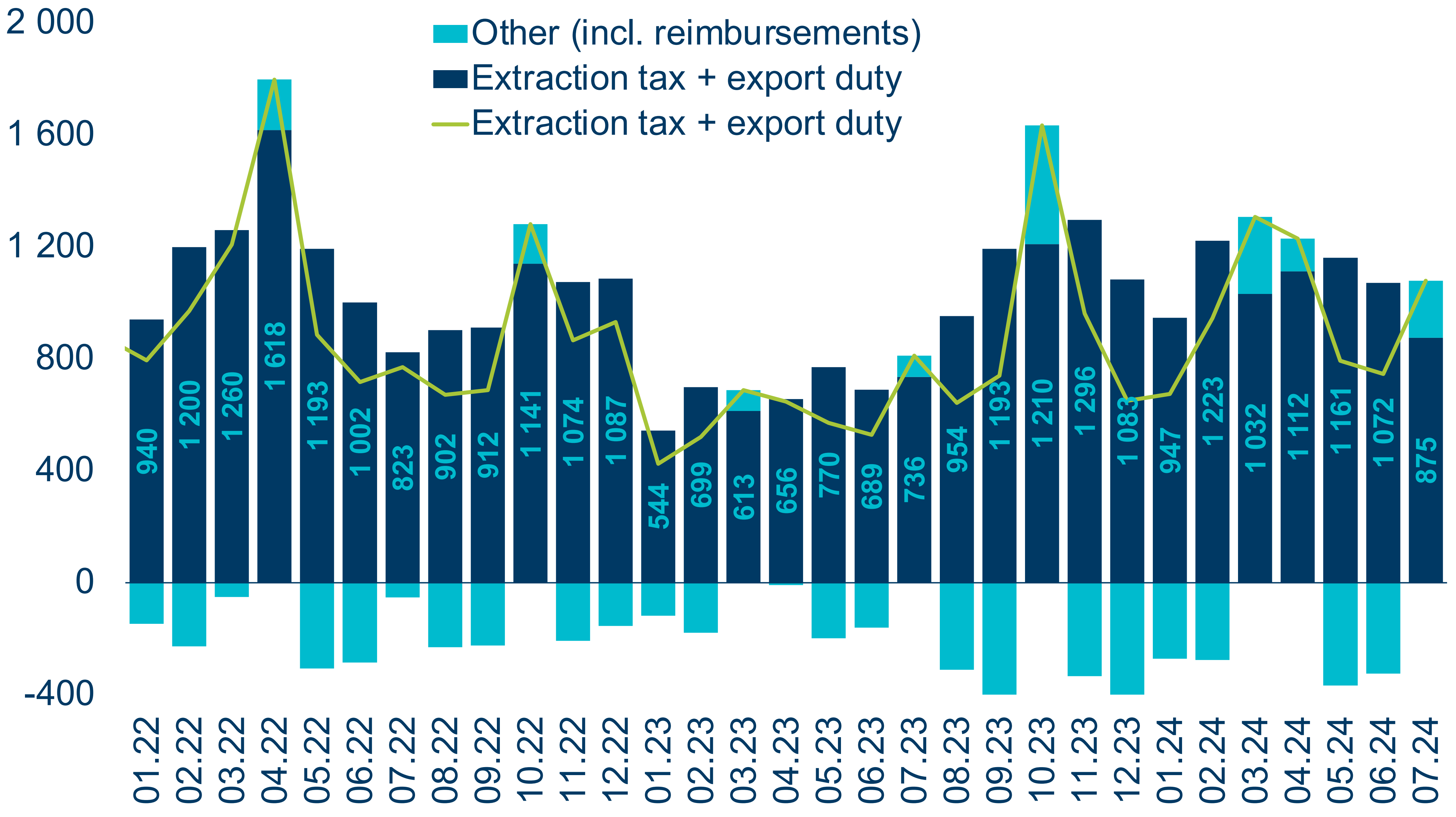


Source: Ministry of Finance, KSE Institute

Strong oil and gas revenues provide support to the budget.

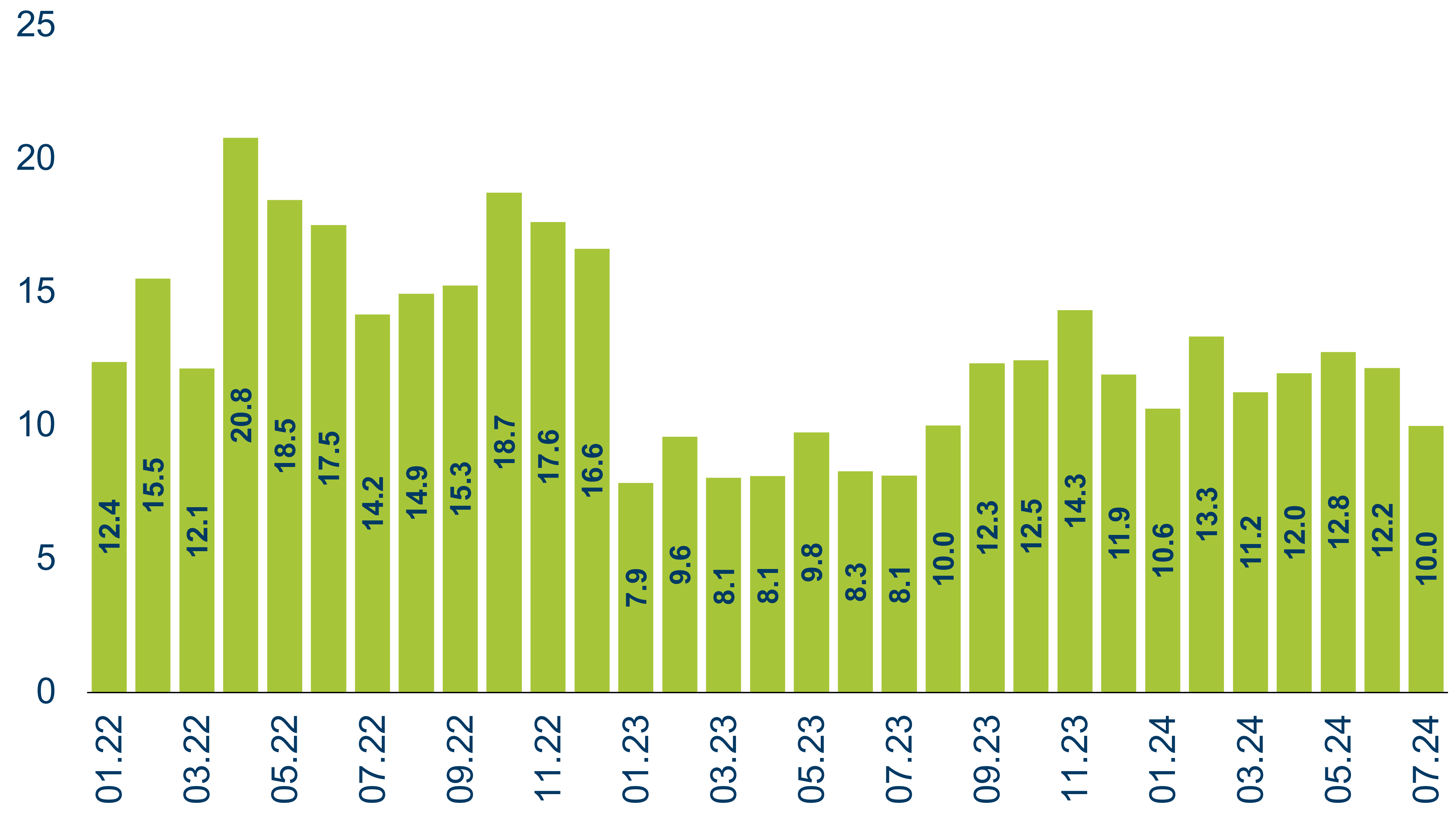
- O&G revenues from extraction taxes and export duties have averaged more than 1 trillion rubles this year.
- Total receipts over January-July 2024 (6.8 trillion) represent a 62% increase over the same period in 2023.
- With export prices at current levels, it is very unlikely that the Russian budget will come under pressure.

Federal oil and gas revenues, in ruble billion



Source: Ministry of Finance, KSE Institute

Federal oil and gas revenues, in U.S. dollar billion*



Source: International Monetary Fund, Ministry of Finance, KSE Institute
*includes extraction tax and export duty; calculated with monthly average exchange rate

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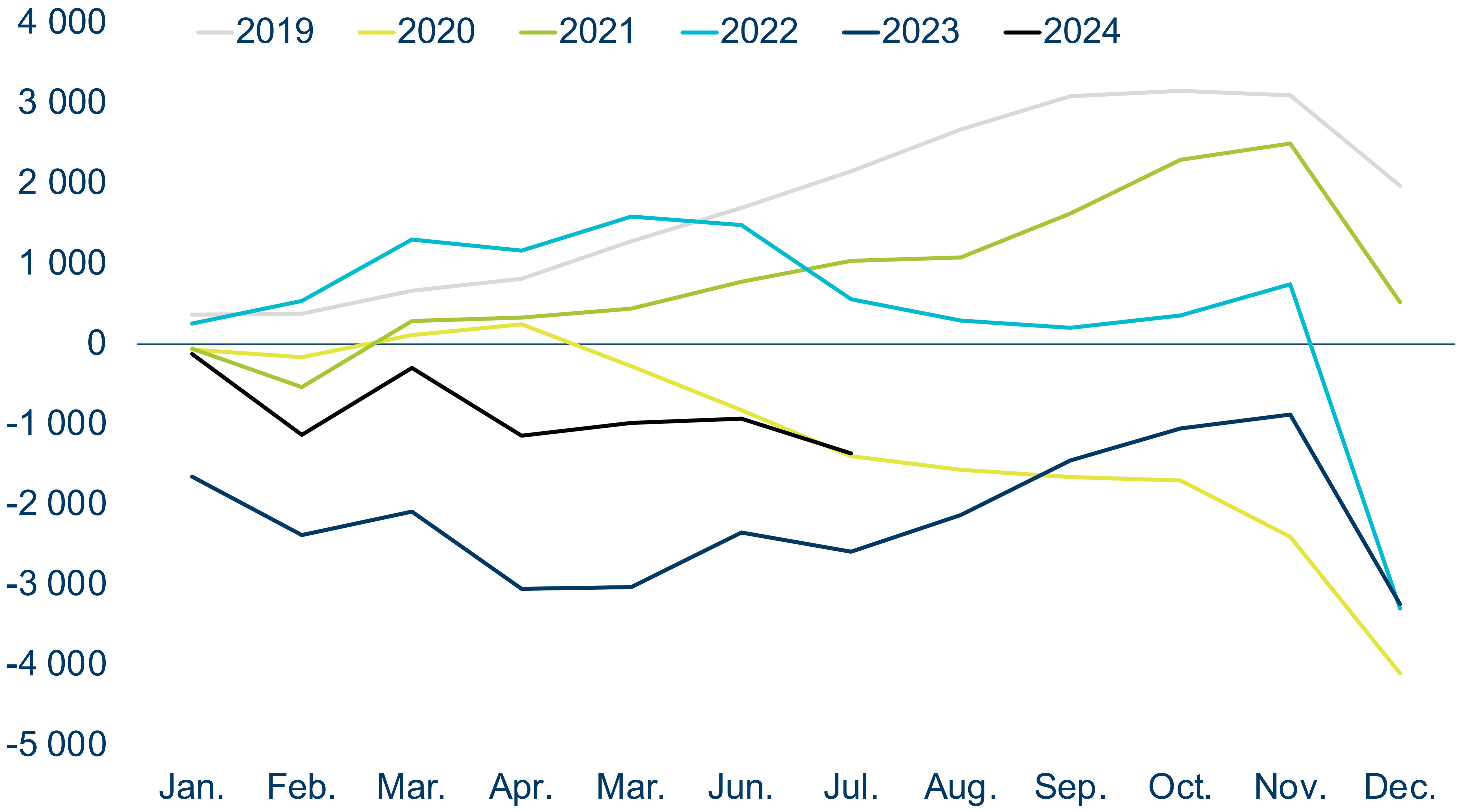
Contained budget deficit means financing is not a challenge.

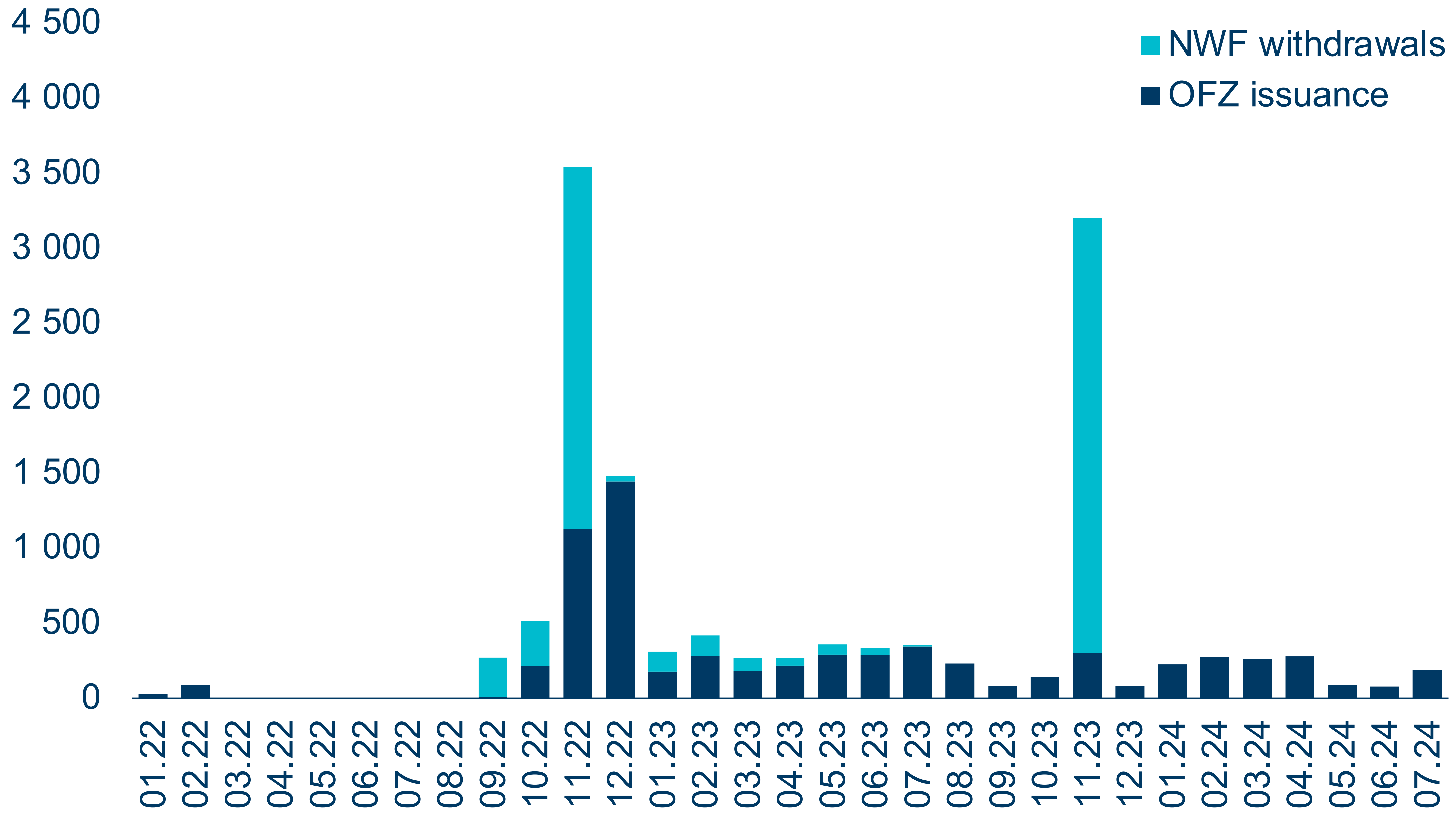
- The January-July 2024 deficit is 47% smaller compared to 2023, albeit expenditures are up sharply due to the war.
- Due to the improved fiscal situation, Russia has been able to finance the budget via moderate domestic debt issuance.
- Risks: higher spending due to Kursk situation & attacks on oil infrastructure, a slowing economy, and high debt costs.

Cumulative federal budget balance, in ruble billion



Source: Ministry of Finance, KSE Institute

Key fiscal financing channels, in ruble billion

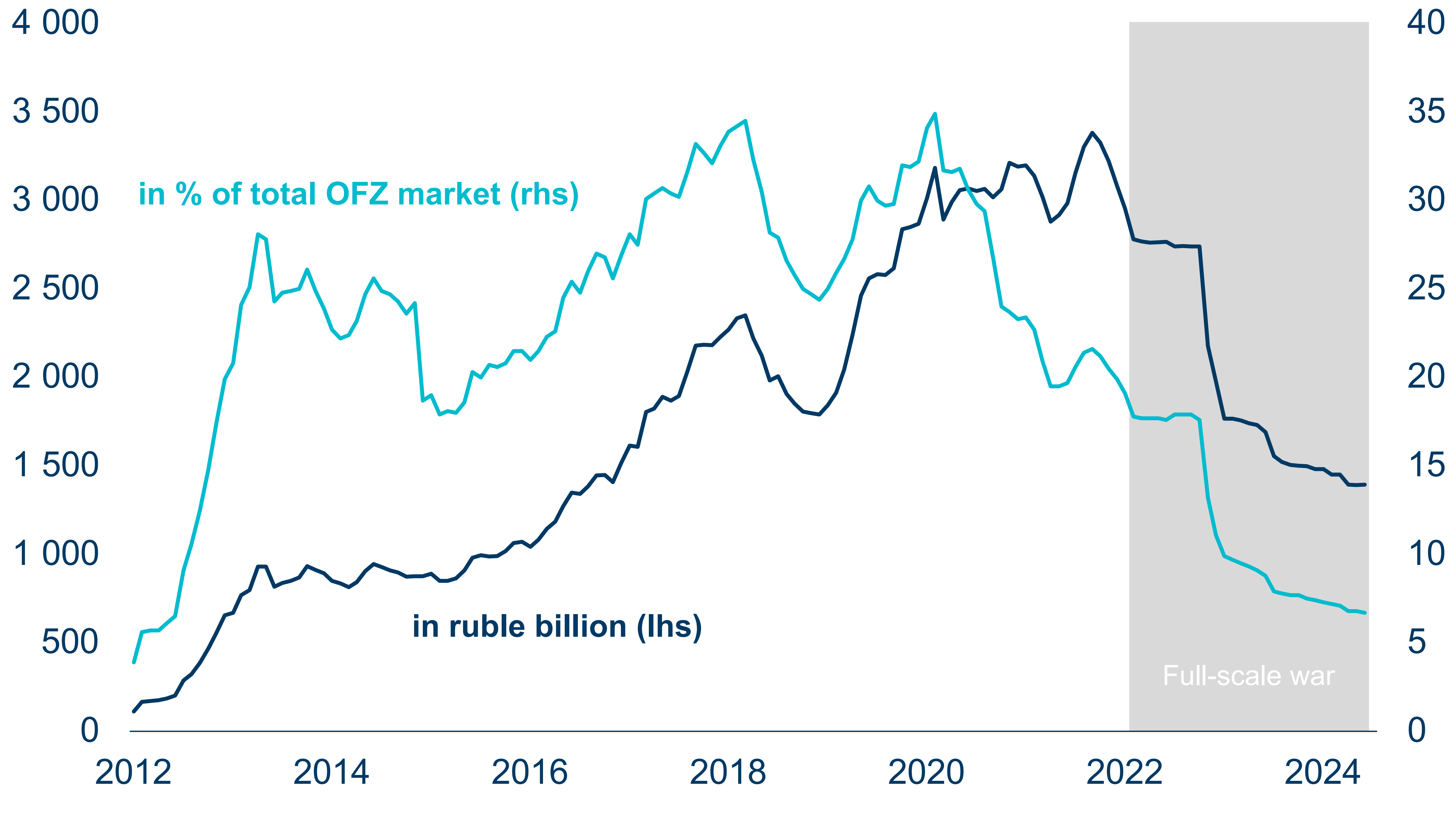


Source: Ministry of Finance, KSE Institute

Domestic banks are the only remaining buyers for OFZs.

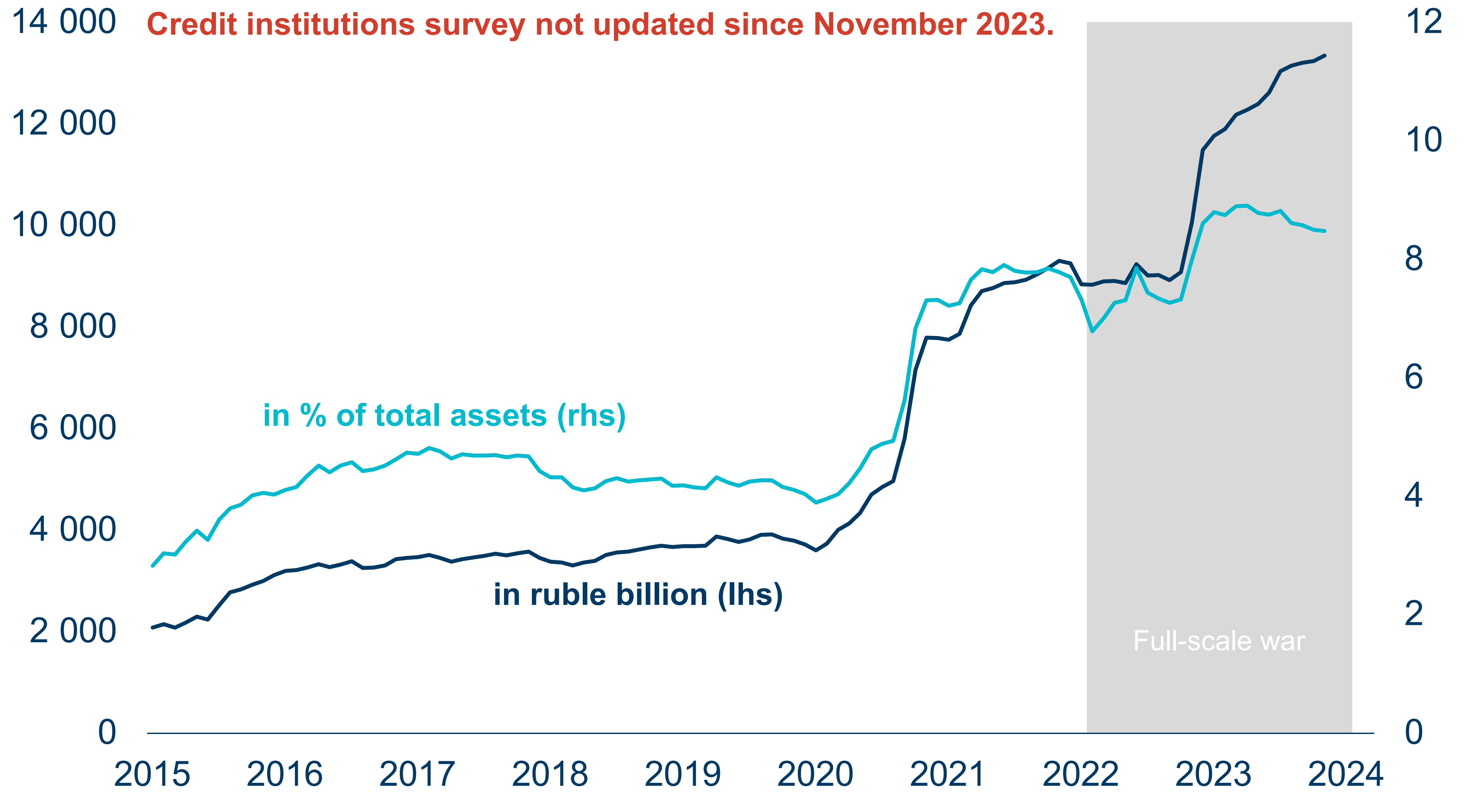
- Foreigners have largely disengaged from the Russian sovereign debt market since the start of the war.
- Non-resident holdings have dropped 1.35 trillion rubles (or 49%) since October 2022 as bonds matured.
- Credit institutions' holdings of OFZs, on the other hand, have risen significantly over the same period.

Non-resident OFZ holdings



Source: Bank of Russia, KSE Institute

Credit institutions OFZ holdings

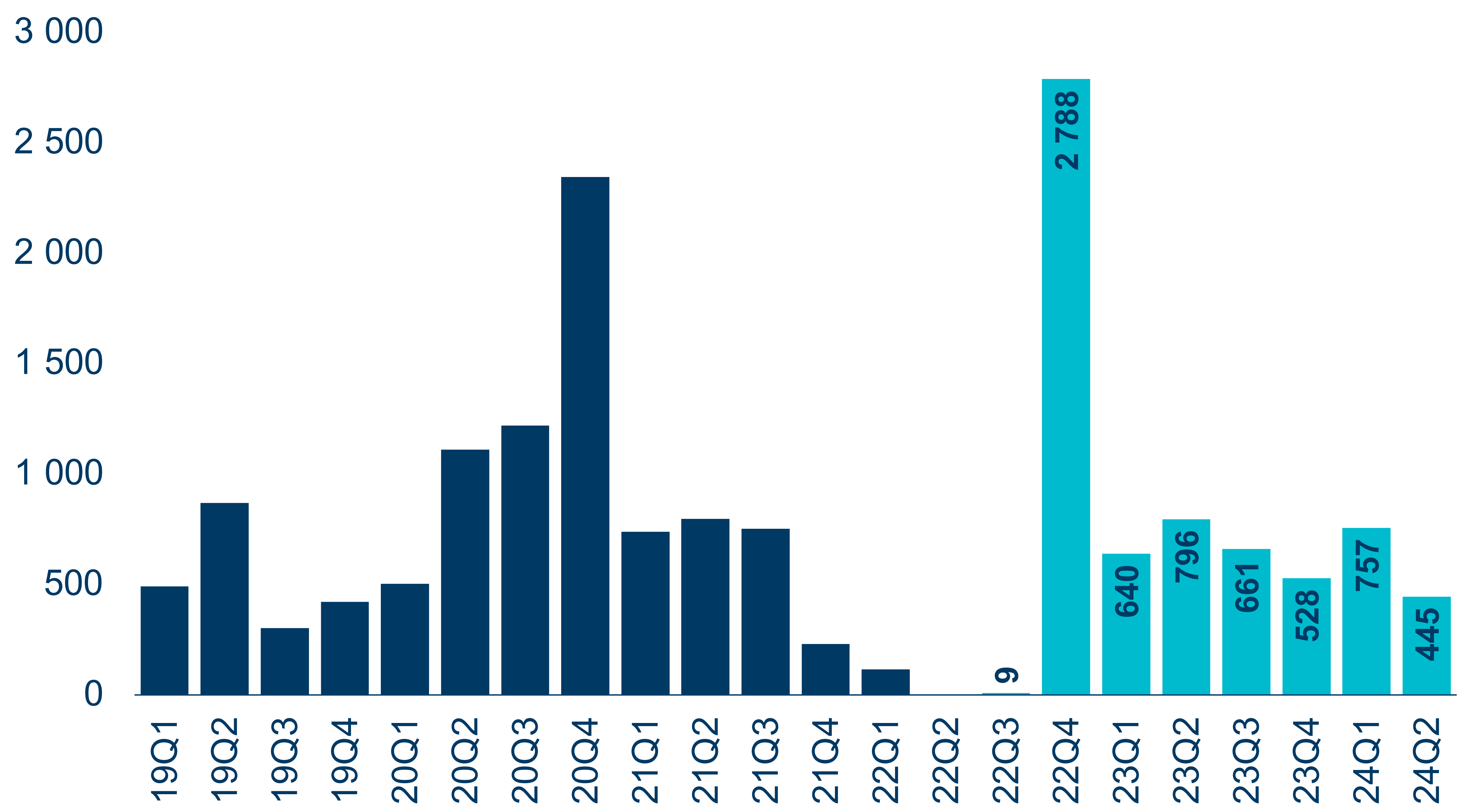


Source: Bank of Russia, KSE Institute

Domestic borrowing stable due to limited fiscal pressure.

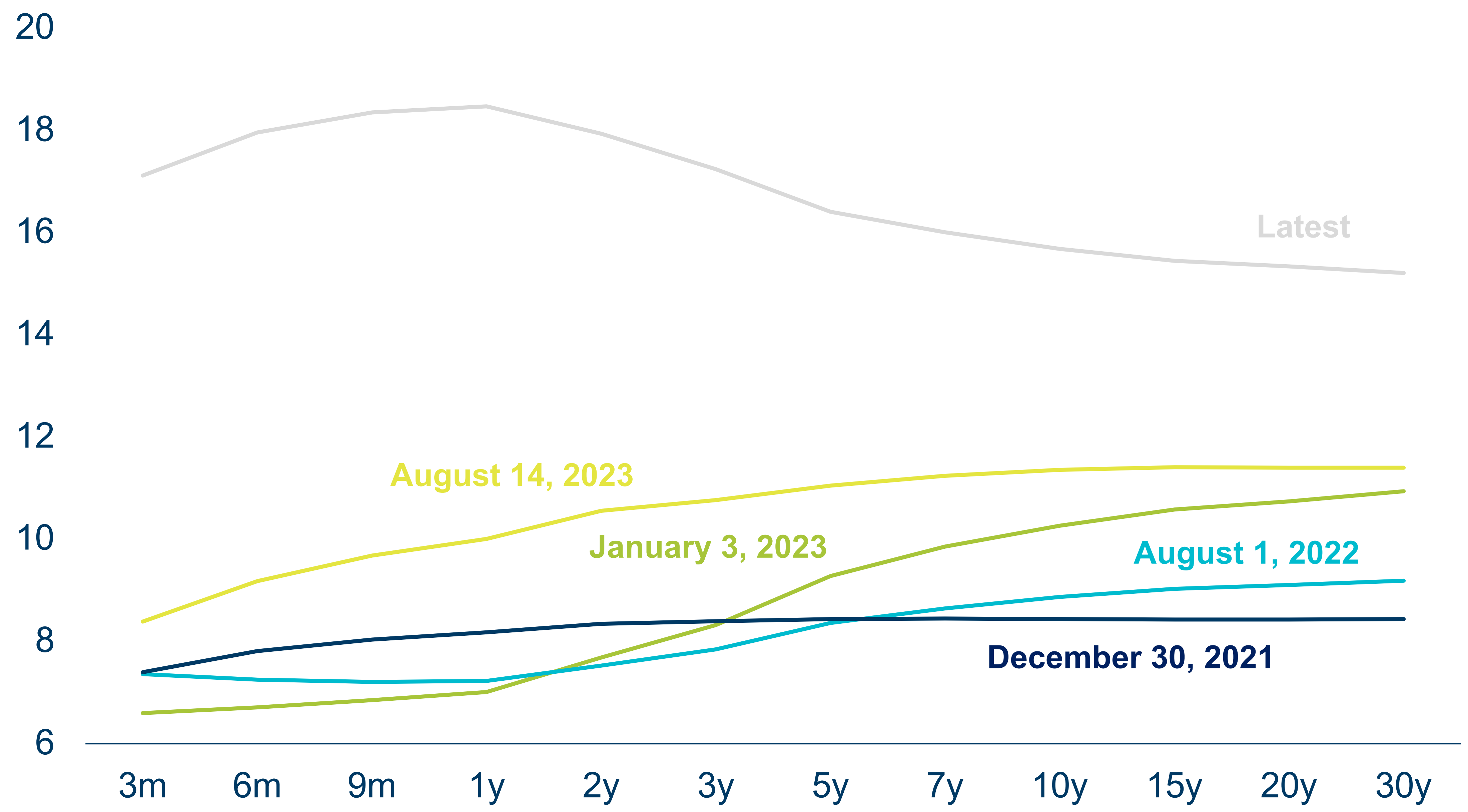
- Borrowing in the domestic market has been broadly stable in the last 1.5 years.
- The OFZ yield curve reflects the recent CBR rate hikes (of cumulative 1,050bps).
- Funding costs are higher but limited in their impact due to the small budget deficit.

New domestic debt (OFZ) issuance, in ruble billion



Source: Ministry of Finance, KSE Institute

OFZ yield curves, in %



Source: Bank of Russia, KSE Institute

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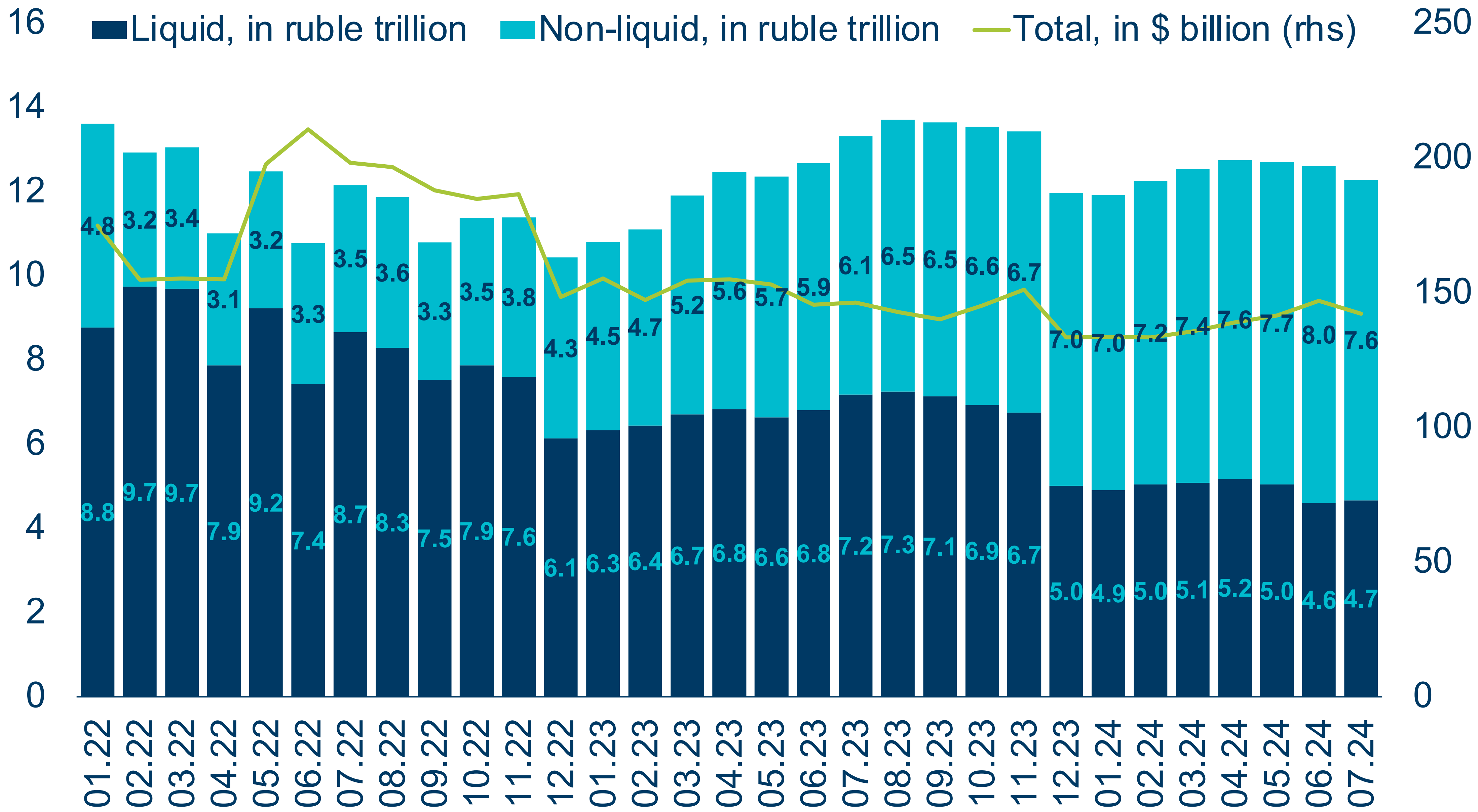
Macro buffers seriously depleted by war and sanctions; limited policy options in the case of further erosion of macroeconomic stability.

Half of the NWF’s liquid assets have been used up since February 2022.

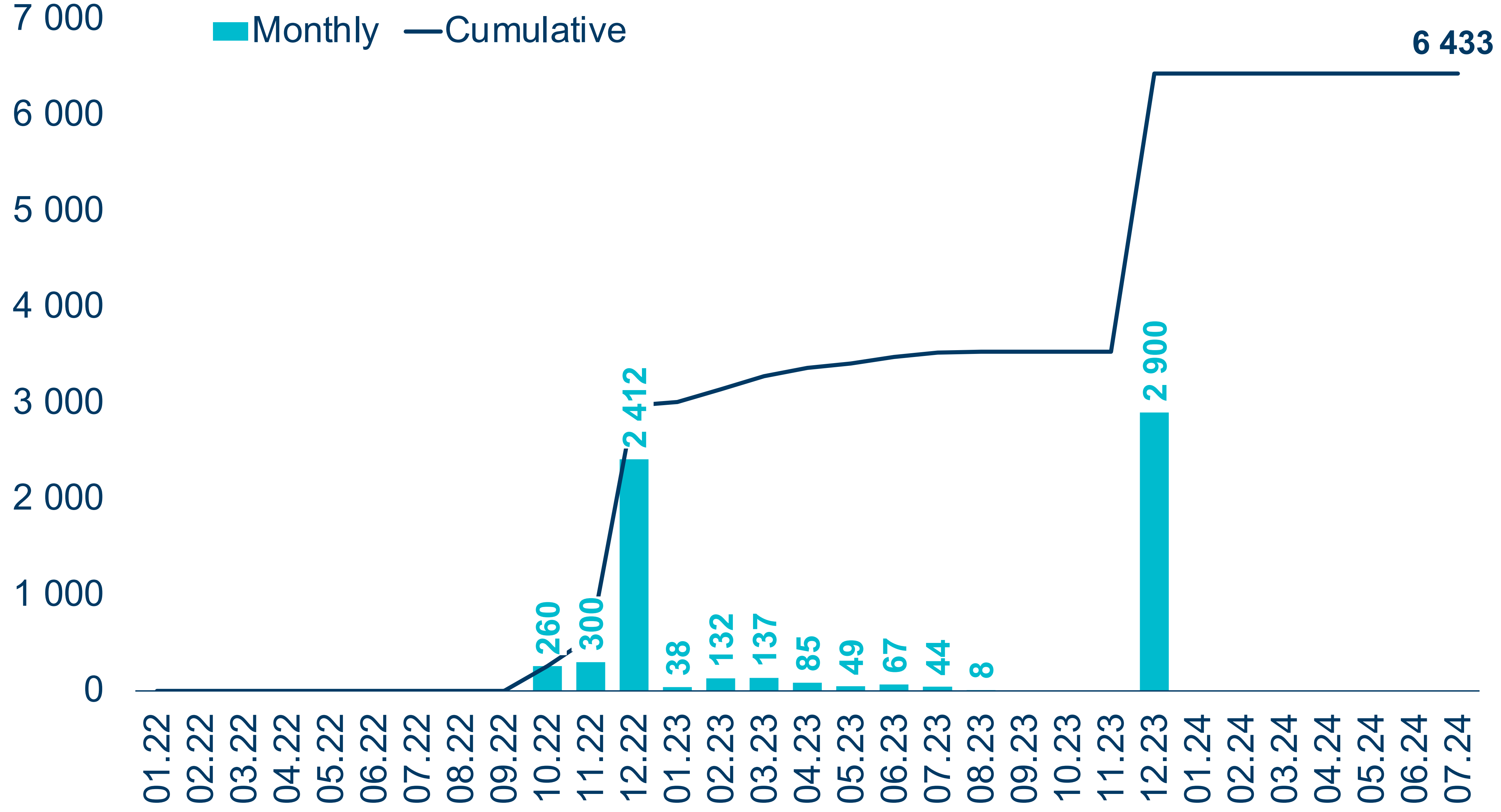
- Total assets of the National Welfare Fund stood at 12.3 trillion rubles ($142 billion, 6.4% of GDP) in July 2024.
- The liquid portion now only accounts for 38% of the total as a stronger ruble weighs on the local currency value.
- Since the start of the full-scale invasion, Russia has used more than half (~5.1 trillion) of the NWF’s liquid assets.

Assets of the NWF, in ruble billion and U.S. dollar billion



Source: Ministry of Finance, KSE Institute

NWF contributions to the budget, in ruble billion



Source: Ministry of Finance, KSE Institute

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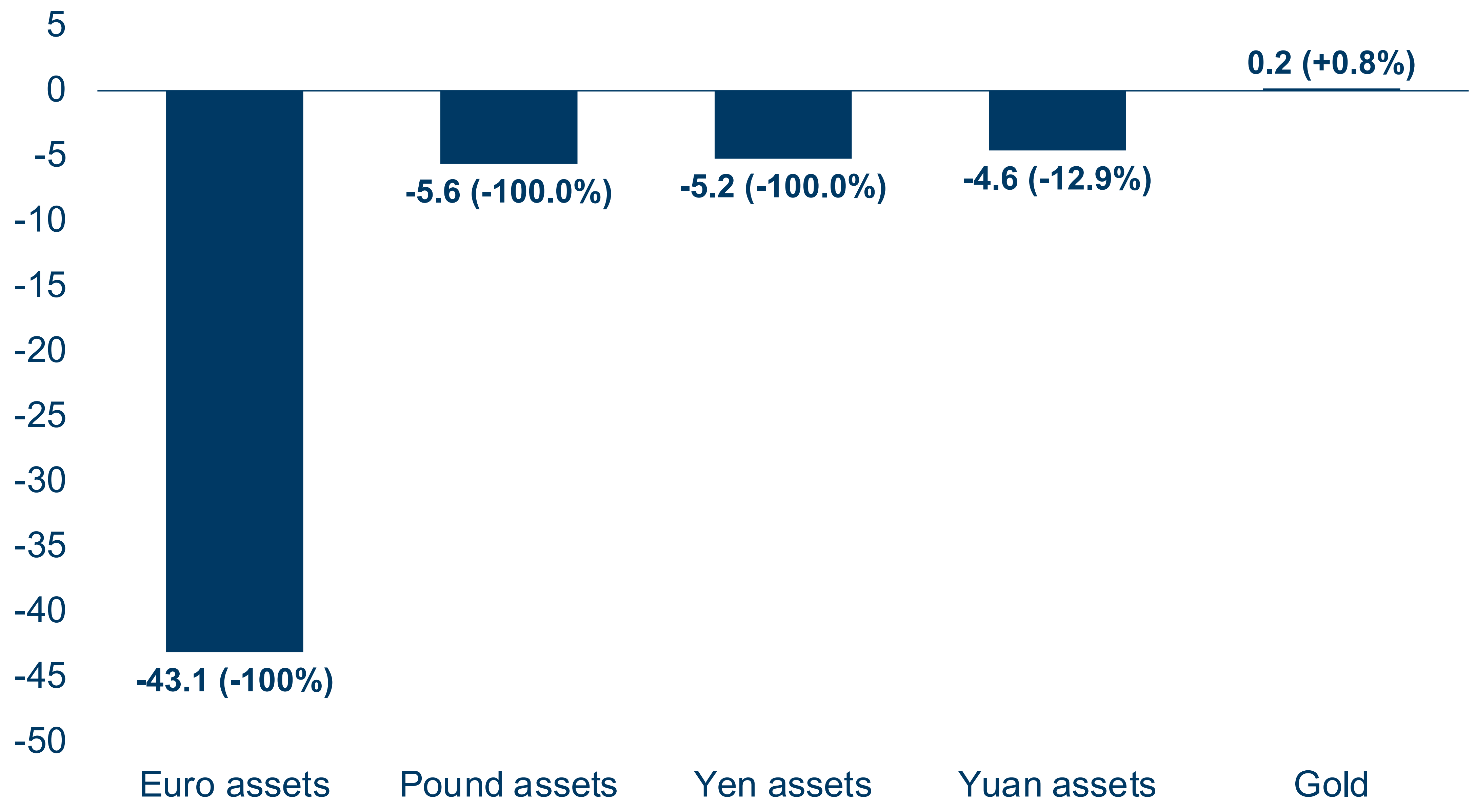
Headline NWF numbers conceal that hard currency assets are gone.

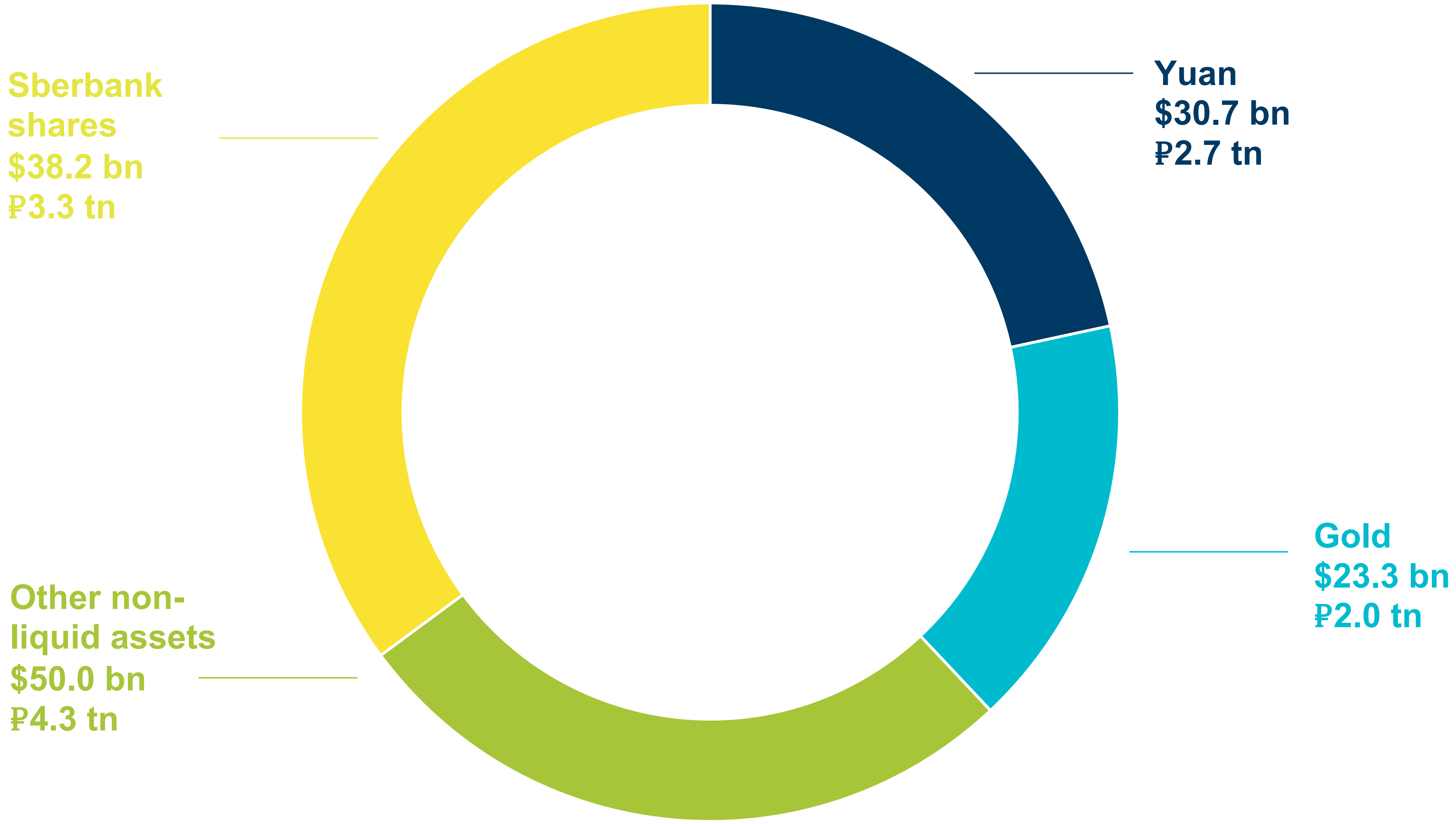
- Russia has depleted all hard-currency holdings of the NWF, with euro assets falling to zero in December 2023.
- Only yuan-denominated assets and gold remain in the liquid portion, totaling 4.7 trillion rubles (or $54 billion).
- As these are more difficult to use, at least at scale, budgetary funding via the NWF will become more challenging.

Change in liquid assets (Aug. 2024 vs. Jan. 2022), in U.S. dollar billion



Source: Ministry of Finance, KSE Institute

Composition of NWF assets as of August 1, 2024*

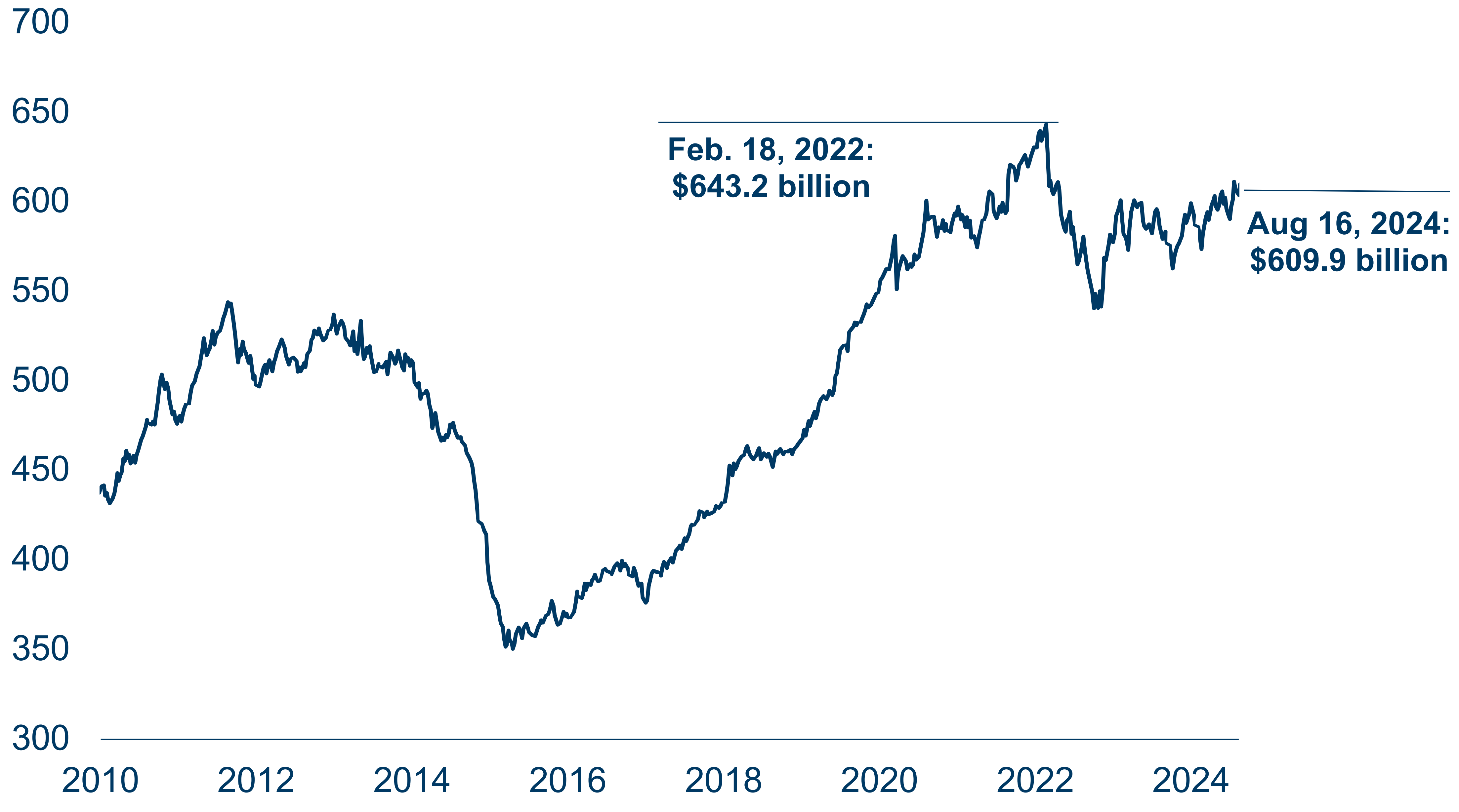


Source: Ministry of Finance, KSE Institute *based on market exchange rates/prices

A substantial share of international reserves remain immobilized.

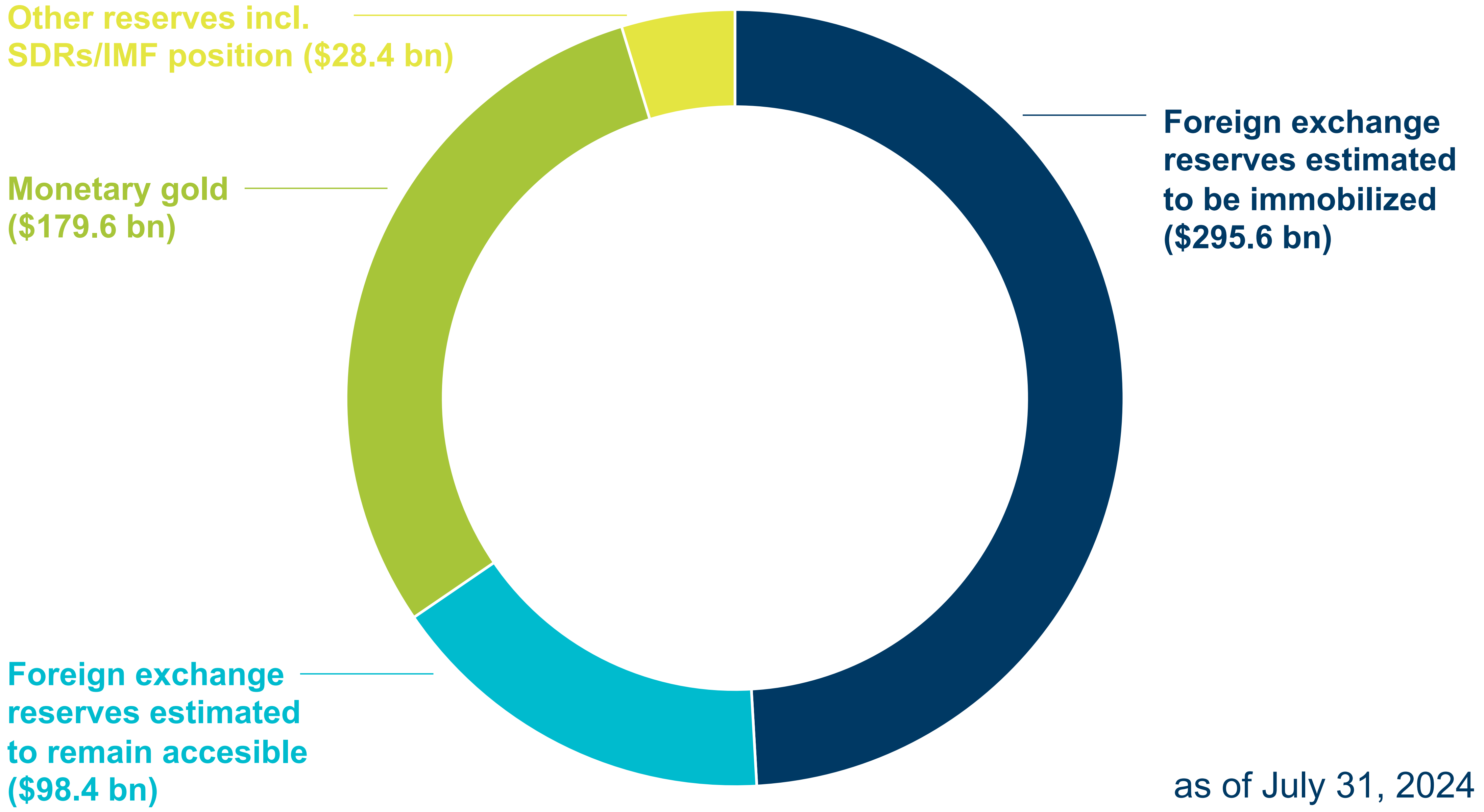
- Before the invasion, Russia held $643 billion in international reserves, part of what is described as *"Fortress Russia".*
- We estimate that around $296 billion are currently immobilized due to international sanctions on CBR and NWF.
- This leaves Russia with access to $180 billion in monetary gold and roughly $98 billion in FX assets (largely yuan).

Total reserves, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

Estimated composition of reserves, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

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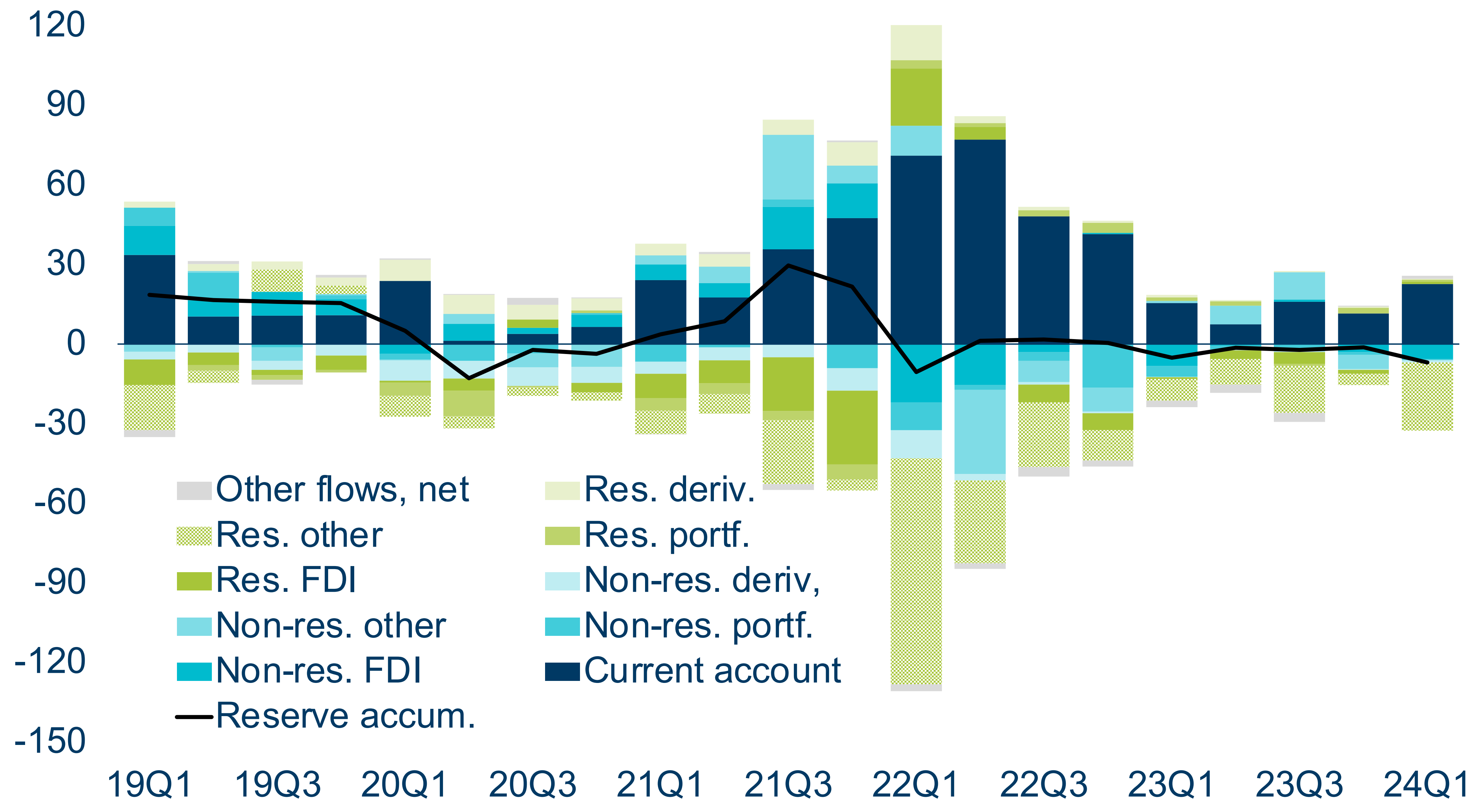
Significant accumulation of new foreign assets since 2022.

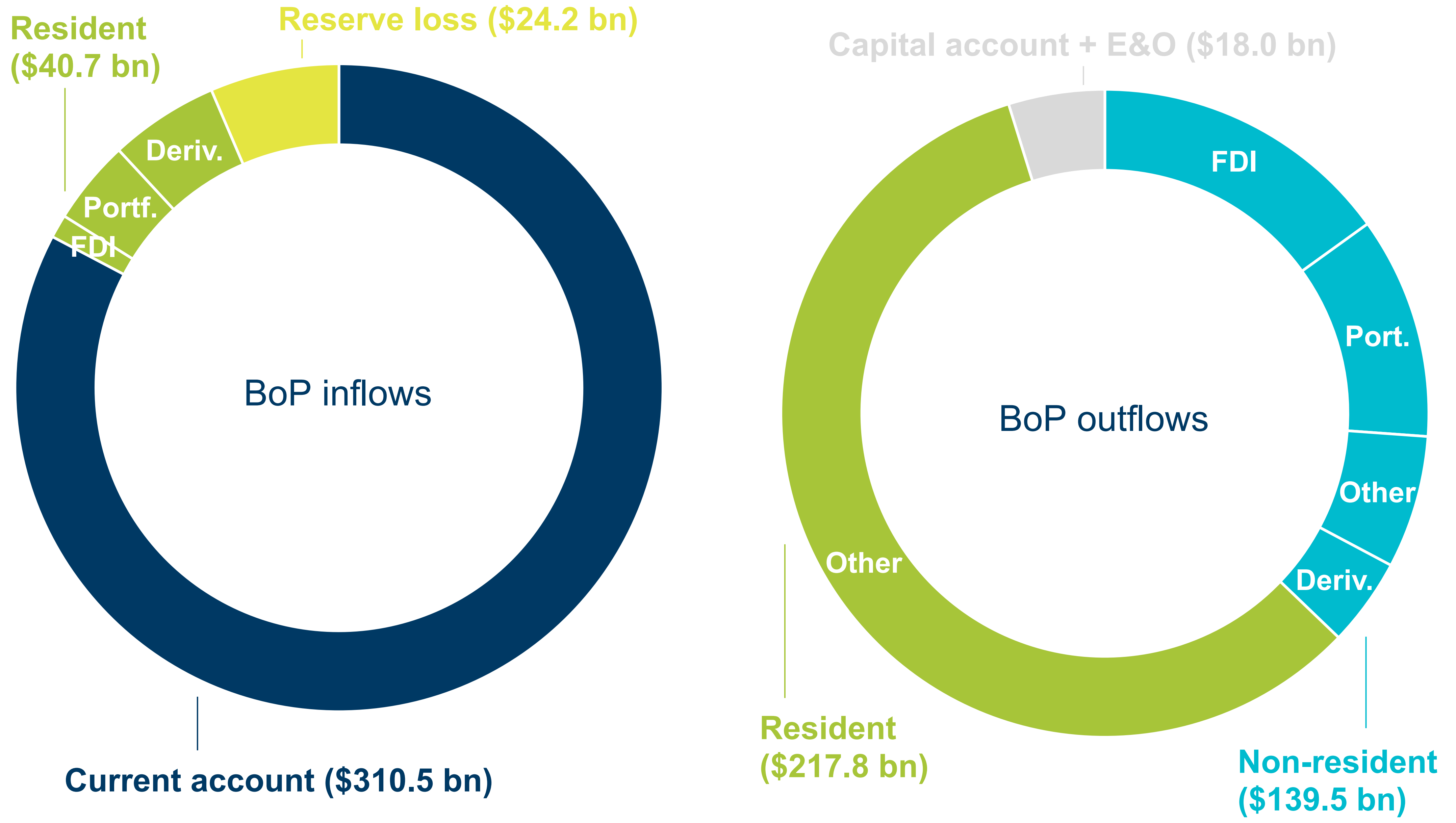
- It is time to focus attention on foreign assets that Russia has been able to accumulate due to favorable BoP dynamics.
- Non-resident capital outflows partially ate up the large current account surplus and resident inflows in Q1 2022-Q1 2024.
- But Russian banks and corporates were able to acquire $218 billion in assets abroad, which need to be kept out of reach.

Balance of payments, in U.S. dollar billion



Source: Bank of Russia, KSE Institute

2022Q1-2024Q1 balance of payments flows, in U.S. dollar billion

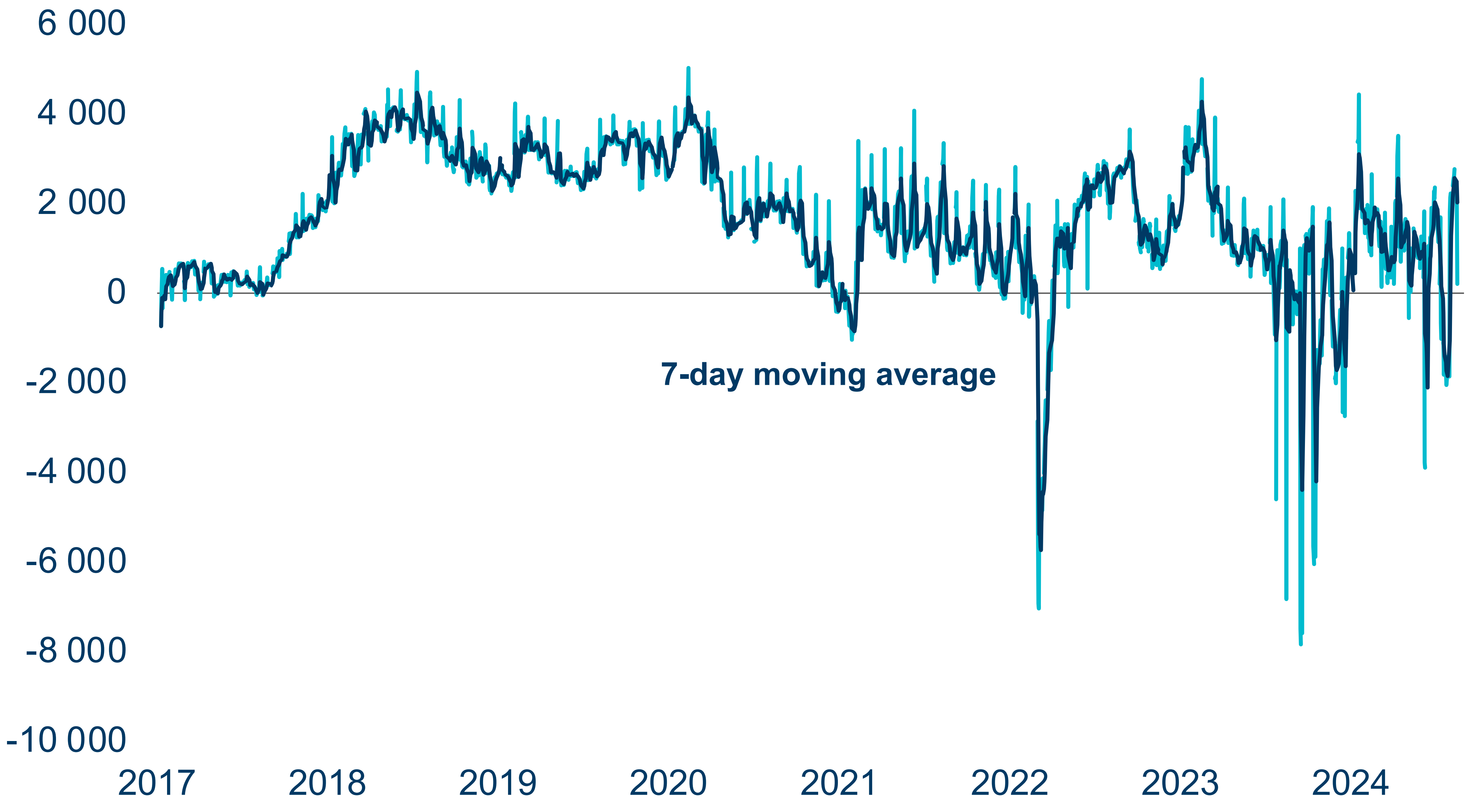


Source: Bank of Russia, KSE Institute

CBR rate hikes have impacted banking system liquidity in recent months.

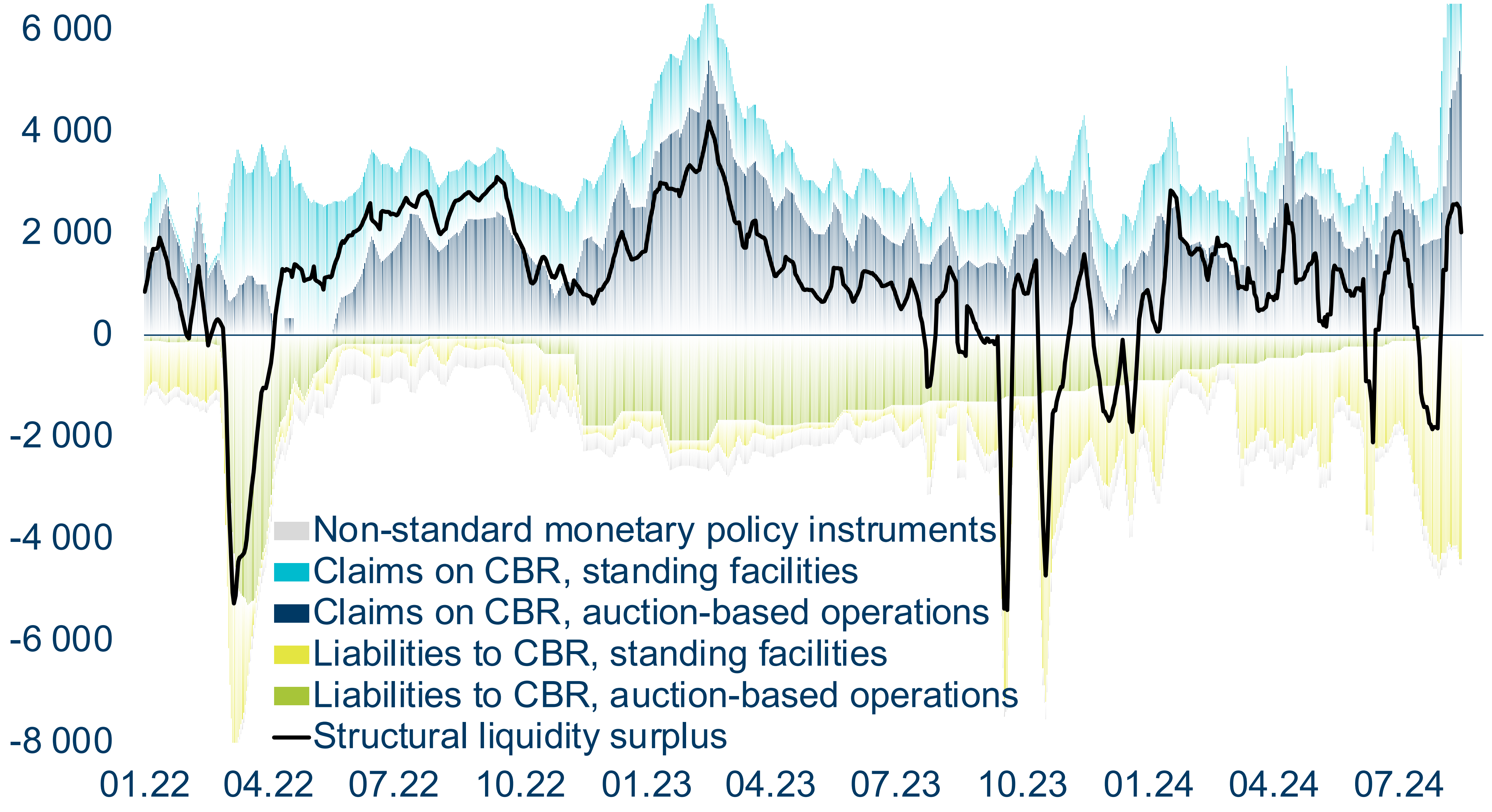
- Liquidity conditions recovered quickly after the initial shock from the full-scale war and imposition of sanctions.
- A closer look at the composition of the structural liquidity surplus points to some stress in the interbank market.
- The data clearly shows the effects of the CBR's monetary tightening since mid-2023 (cumulative +1,050 bps).

Banking system structural liquidity surplus, in ruble billion



Source: Bank of Russia, KSE Institute

Composition of structural liquidity surplus, in ruble billion*



Source: Bank of Russia, KSE Institute *7-day moving average

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Signs of weakening economy as capacity constraints hit; overheating pushes up inflation despite large interest rate hikes.

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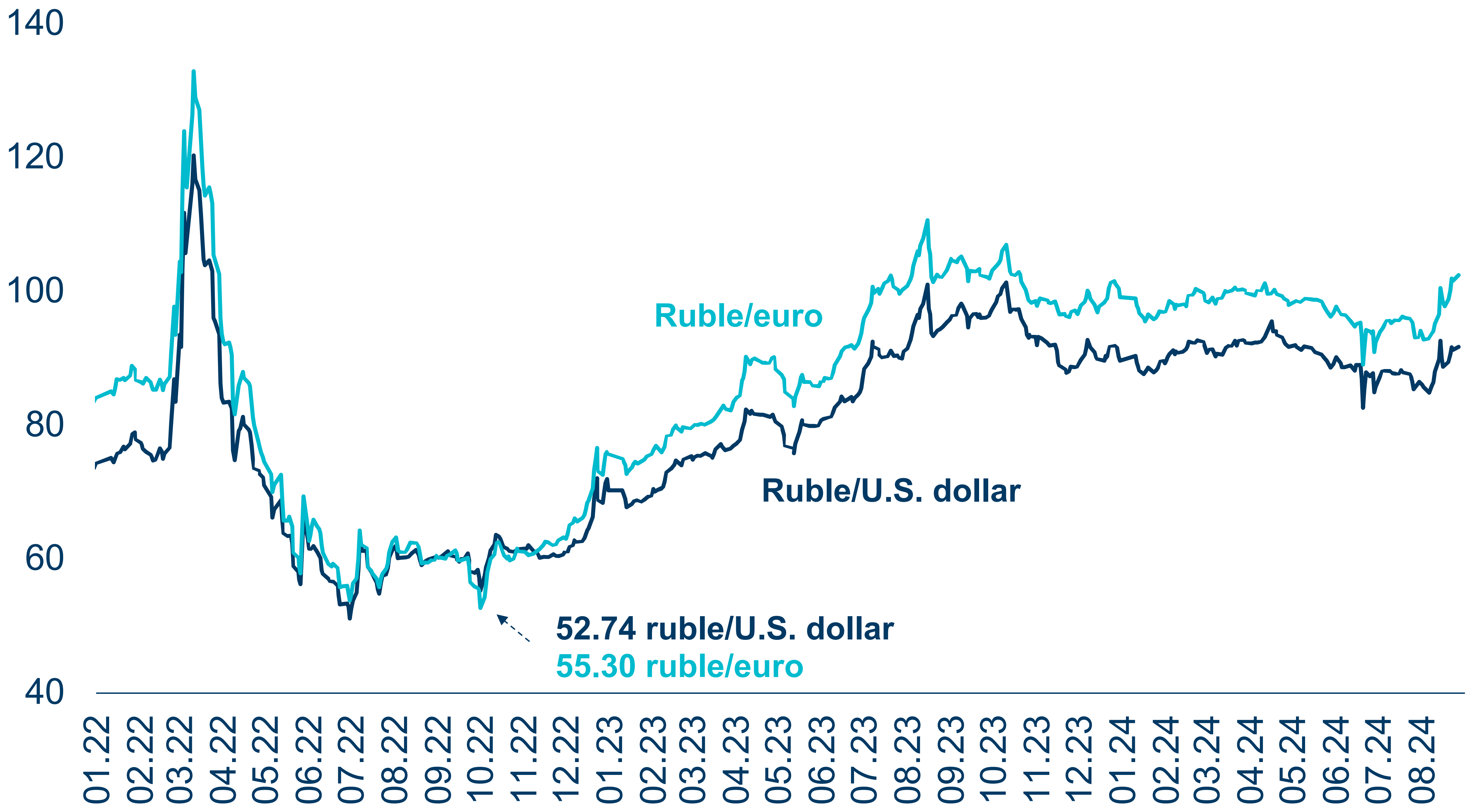
Ruble has stabilized but inflation continues to rise.

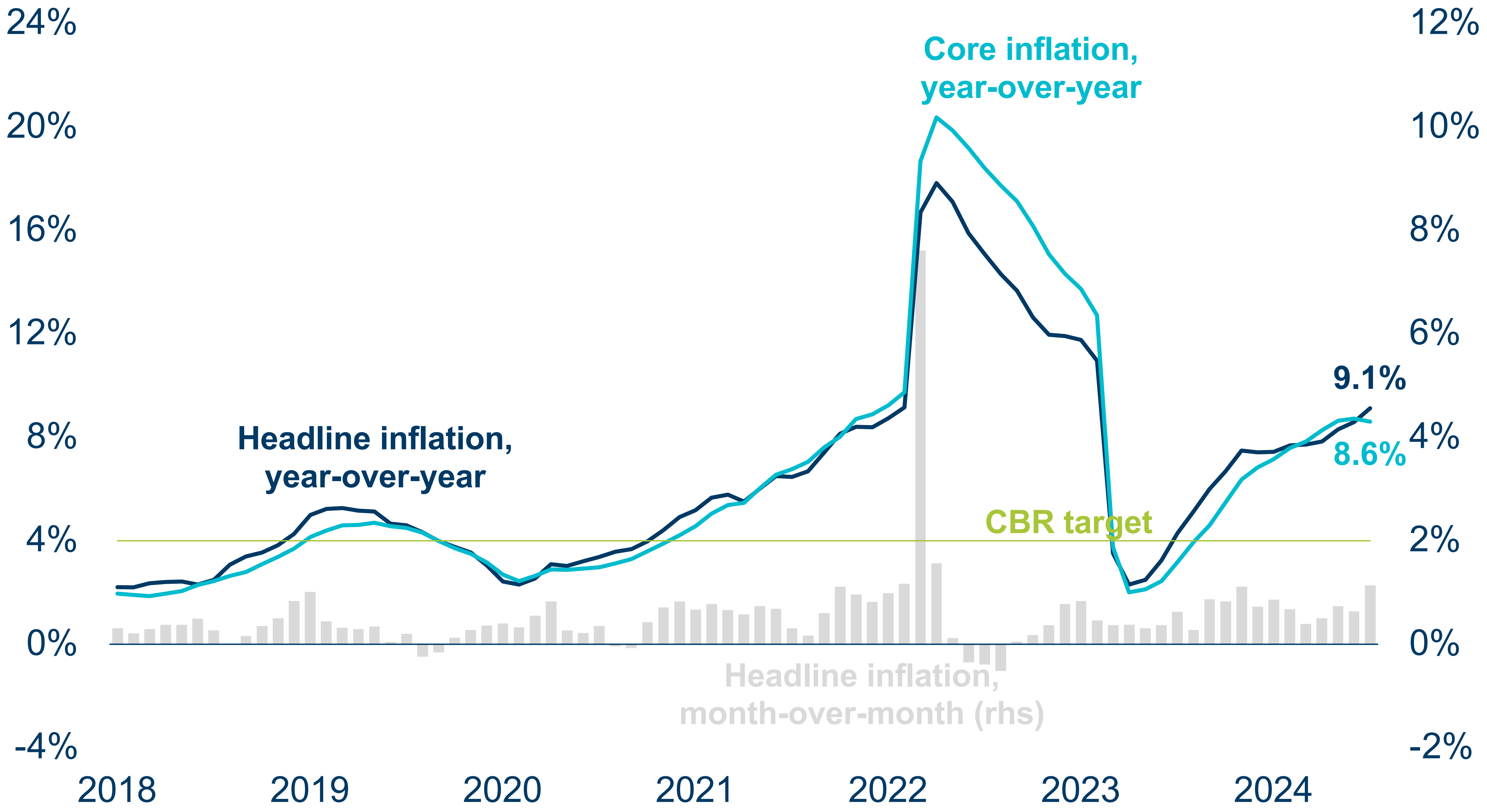
- Russia’s currency has been relatively stable but is down 40% vs. dollar and 49% vs. euro since the fall of 2022.
- Depreciation picked up in recent days, likely due of Ukraine’s successful counter-offensive in the Kursk region.
- Despite the ruble’s stabilization, inflation continues to rise, reaching 9.1% for headline and 8.6% for core in July.

Ruble exchange rate vs. U.S. dollar and euro



Source: Bank of Russia, KSE Institute

Inflation, in %



Source: Bank of Russia, KSE Institute

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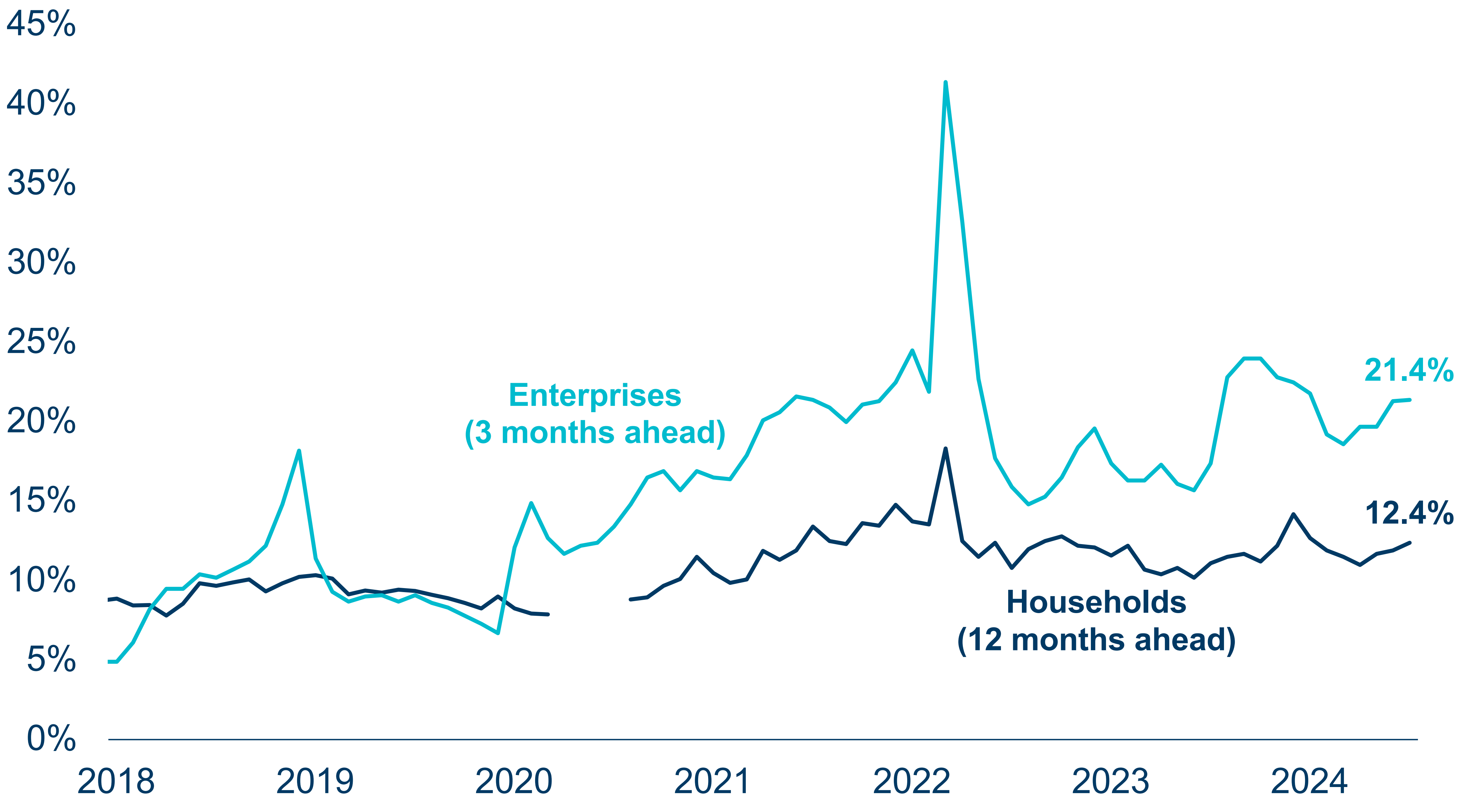
CBR has been forced to undertake dramatic monetary tightening.

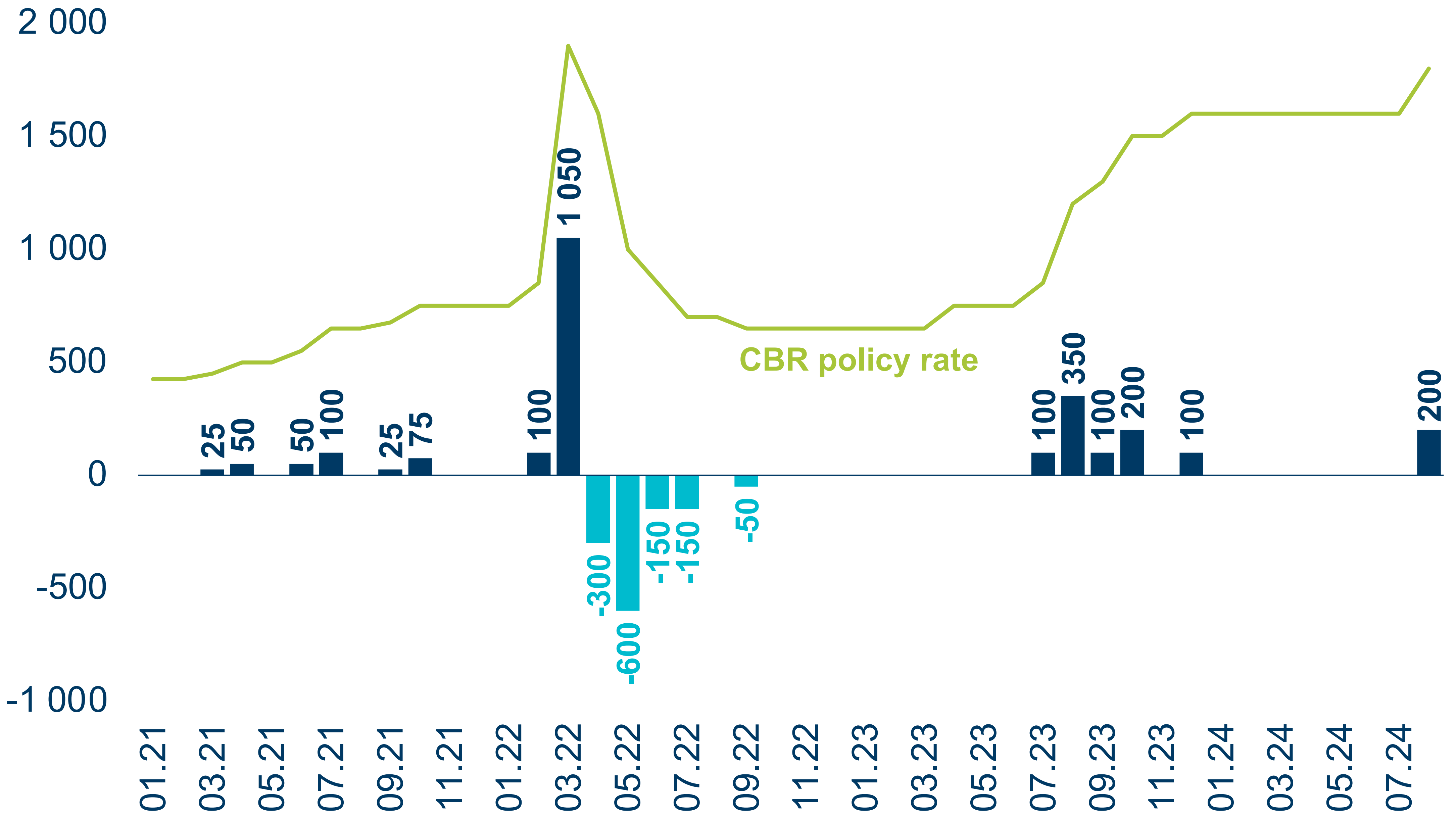
- These inflation dynamics have forced the CBR to hike interest rates once again—by 200 bps.
- Cumulative hikes of 1,150 bps have brought the key rate within 100 bps of its March 2023 value.
- So far, significant tightening of monetary policy has failed to bring rising inflation under control.

Inflation expectations, in %



Source: Bank of Russia, KSE Institute

CBR policy rate and MPC decisions, in basis points

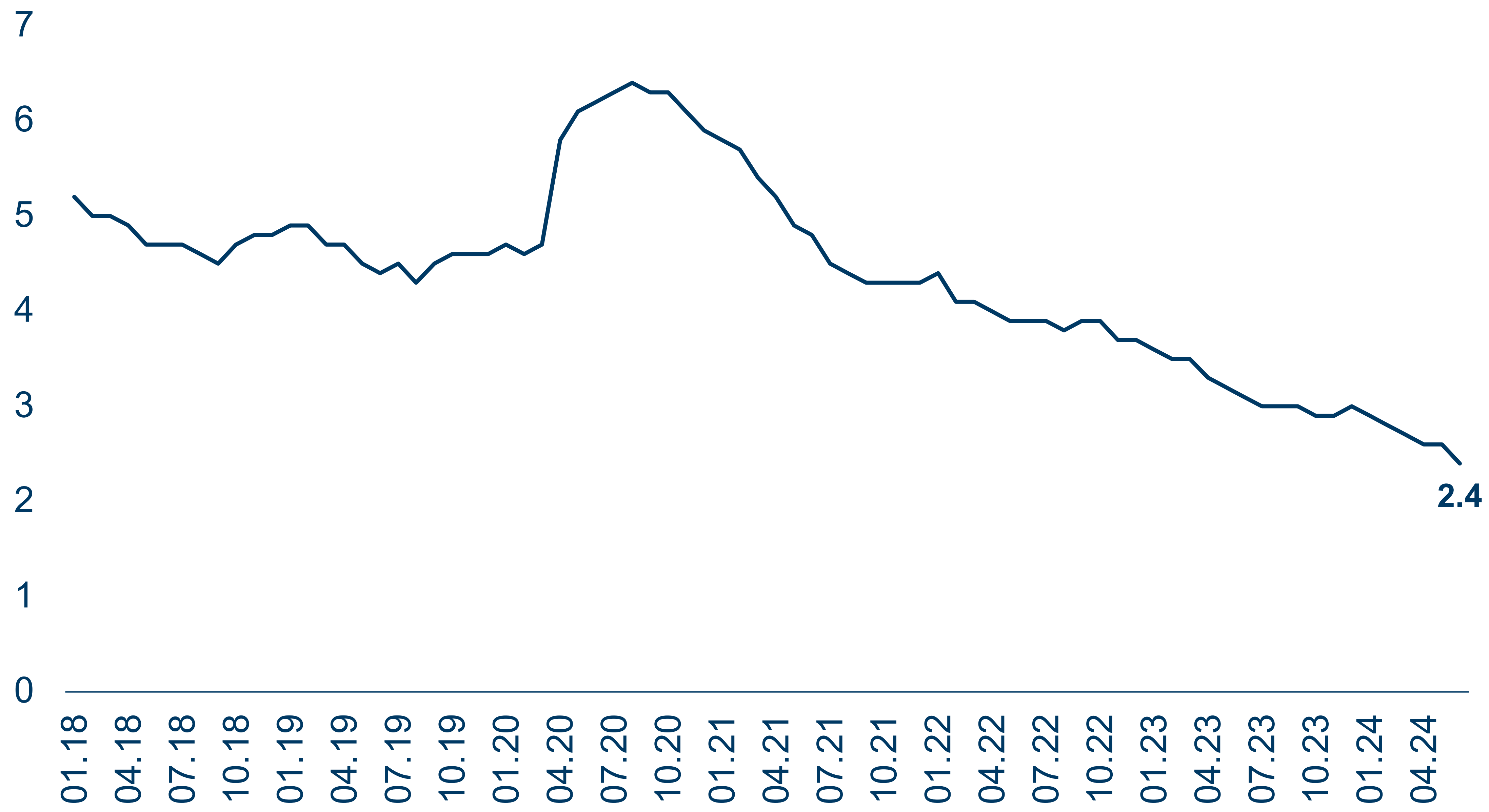


Source: Bank of Russia, KSE Institute

Tight labor market is driving up wages and creating inflation.

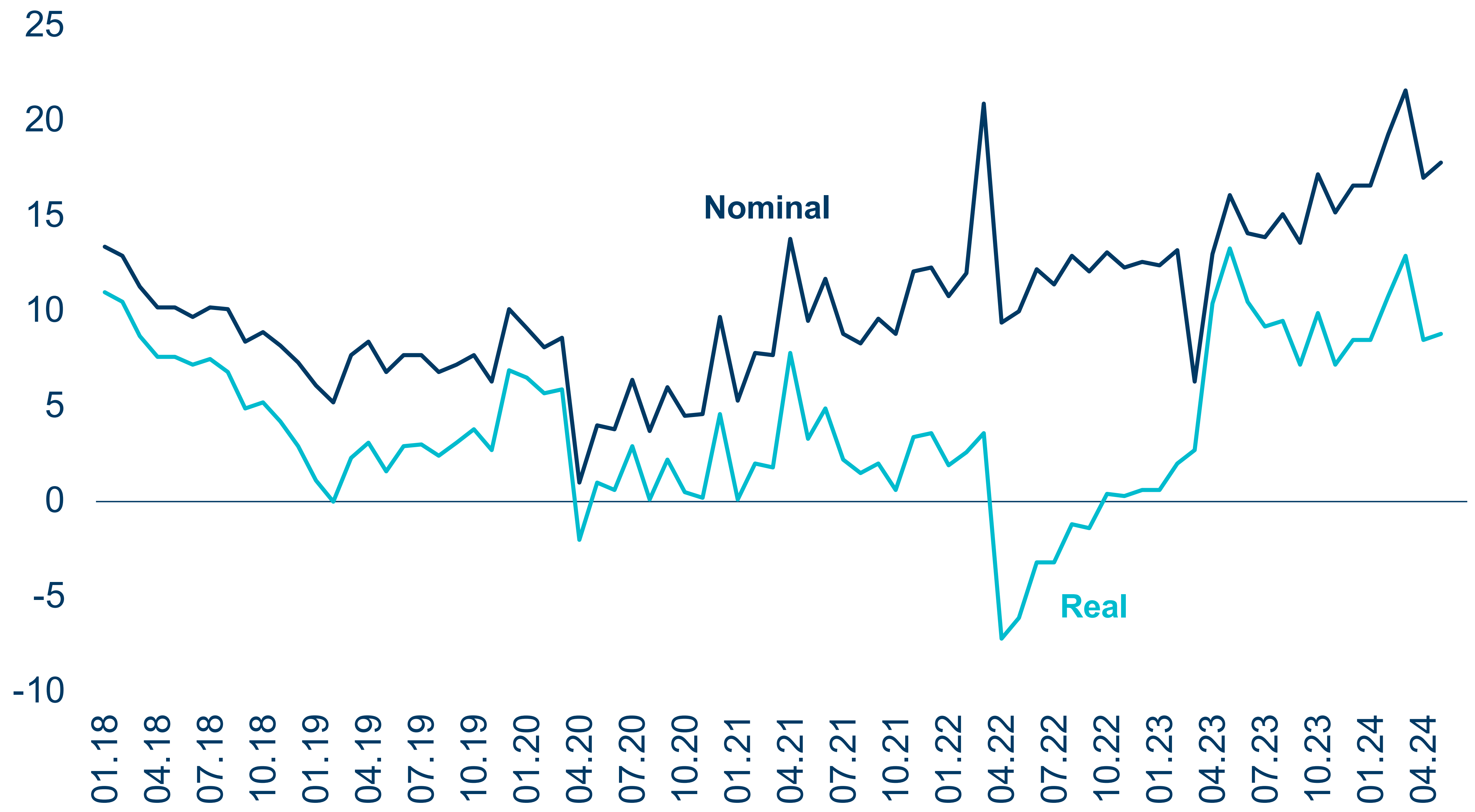
- The unemployment rate has fallen to a record-low 2.4% in June—which technically means full employment.
- Nominal wage growth has trended up since the start of the full-scale invasion and stood at 17.8% in May.
- In addition to creating inflationary pressures, the economy has effectively no spare capacity left to draw from.

Unemployment rate, in %



Source: Rosstat

Wage growth, in % year-over-year



Source: Rosstat

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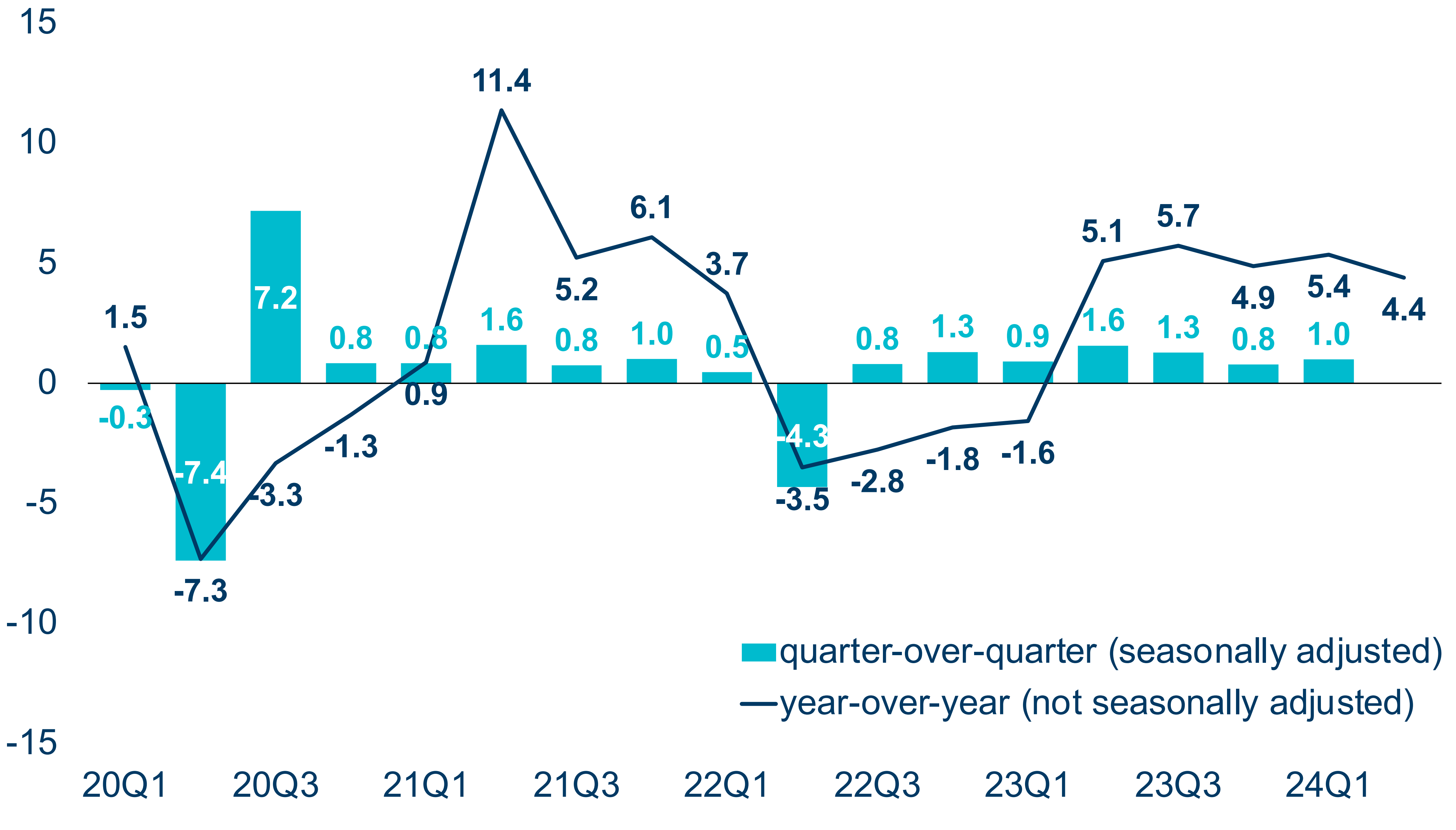
Early signs of an economic slowdown are emerging.

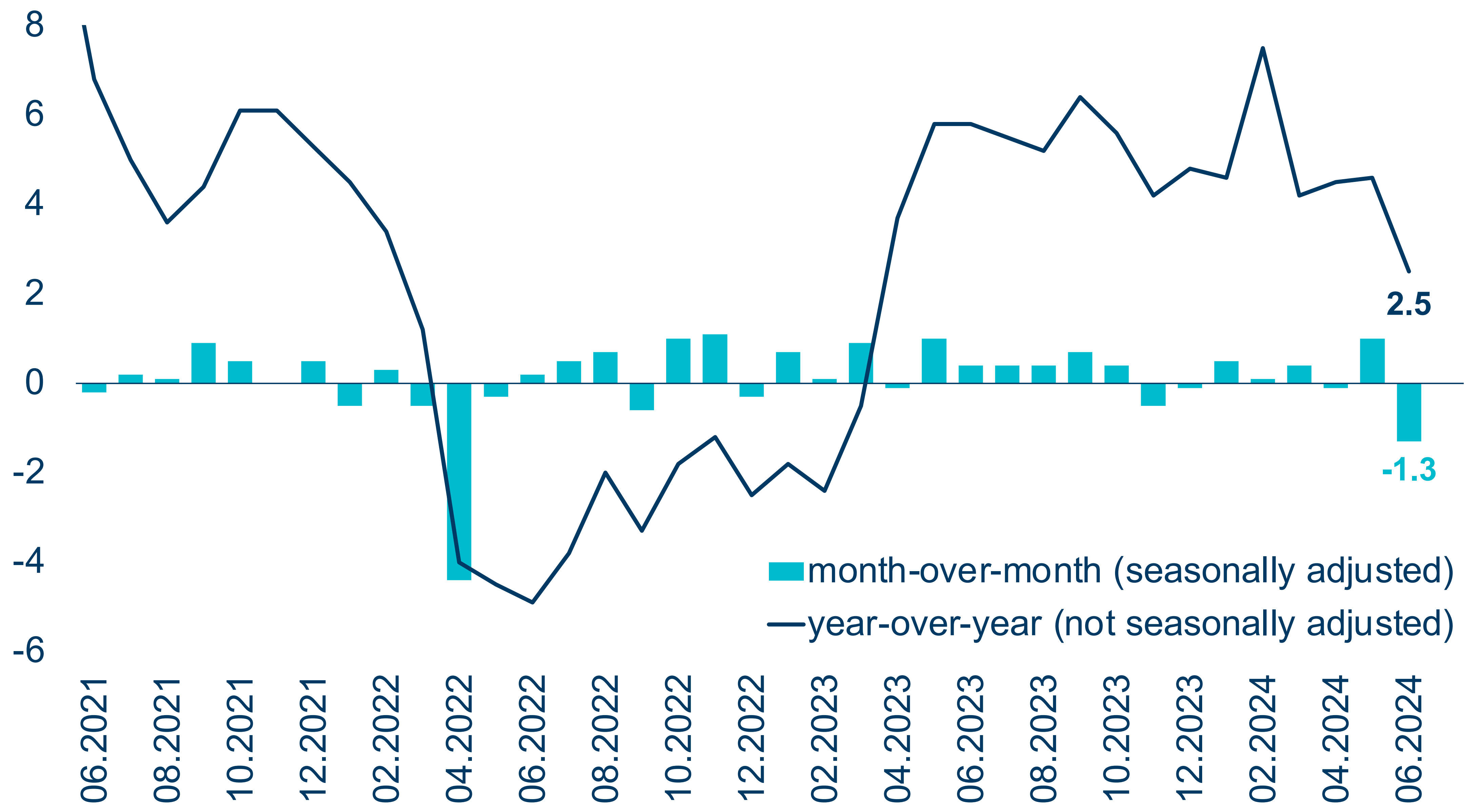
- Real GDP growth in Q2 2024 was reported at 4.4% year-over-year by Russia's statistics agency Rosstat.
- This is slightly lower than in the previous four quarters but still points to a robust economic performance.
- However, monthly data shows that the economy is finally being affected by much tighter monetary policy.

Quarterly real GDP dynamics, in %



Source: Rosstat, KSE Institute

Monthly real GDP dynamics, in %



Source: inveb.ru

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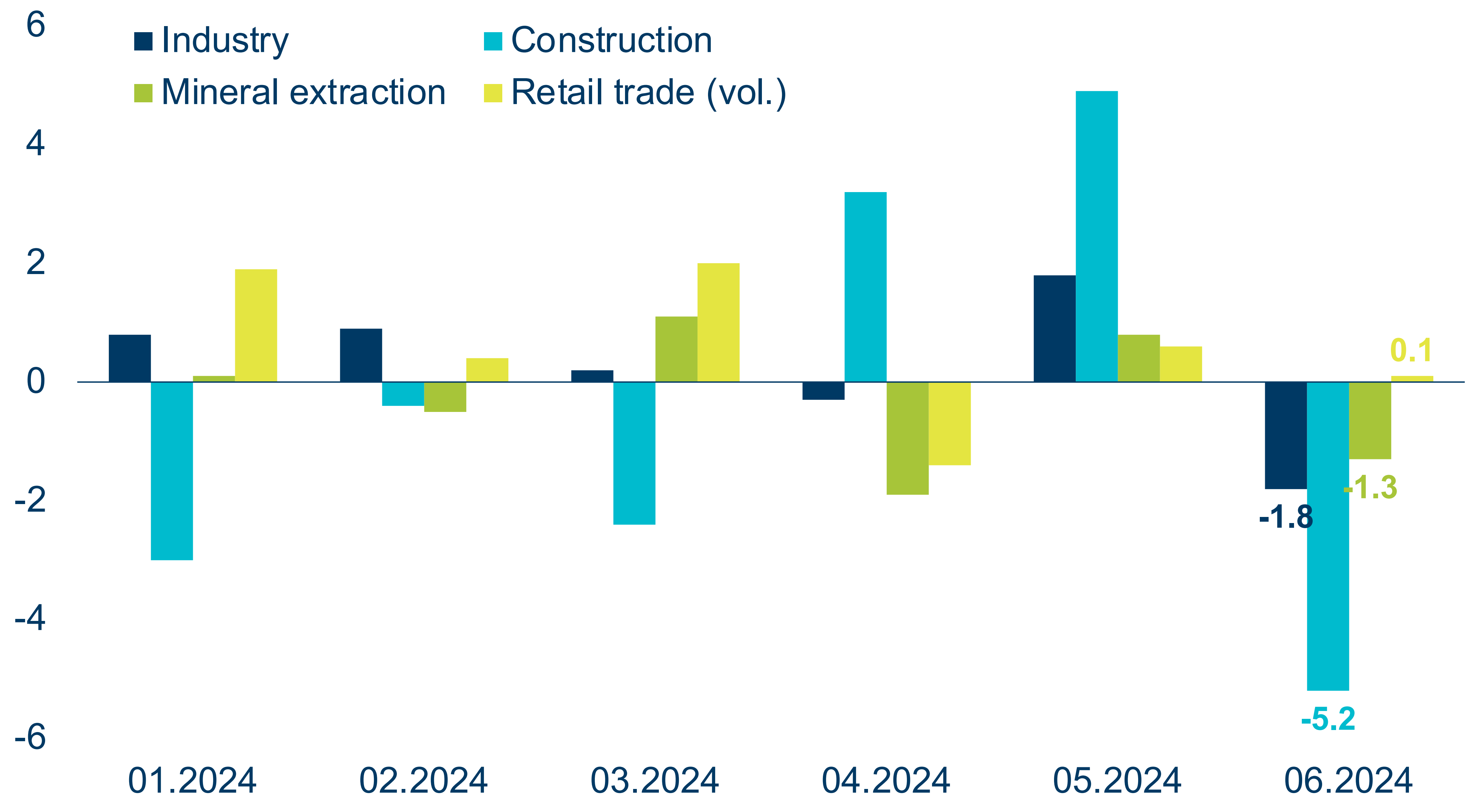
Broad-based slowdown could lead to downgrades of the outlook.

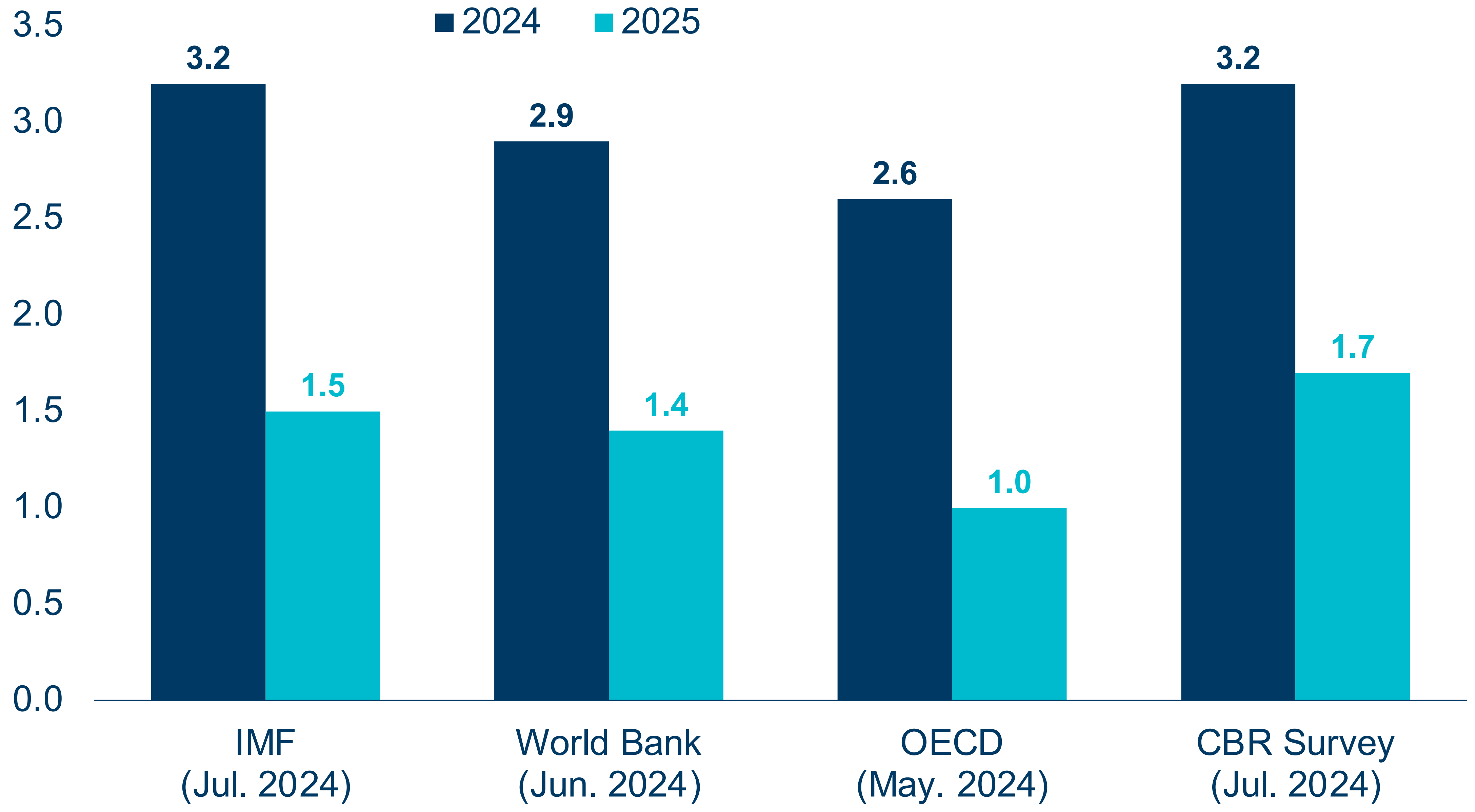
- Higher interest rates appear to be affecting several key industries, but construction is, unsurprisingly, hit hardest.
- GDP forecasts have not been revised yet to reflect concerns over an overheating and, potentially, slowing economy.
- Even so, the Russian economy is already expected to grow significantly slower next year and beyond.

Economic activity, in % month-over-month (seasonally adjusted)



Source: inveb.ru

2024-25 forecasts for Russian real GDP, in % year-over-year



Source: Bank of Russia, IMF, OECD, World Bank

Previous editions of KSE Institute's Russia Chartbook

- July 2024
- June 2024
- May 2024
- April 2024
- March 2024
- February 2024
- January 2024
- December 2023
- November 2023
- October 2023
- September 2023
- July 2023
- May 2023
- April 2023
- March 2023
- February 2023
- December 2022