

Russia

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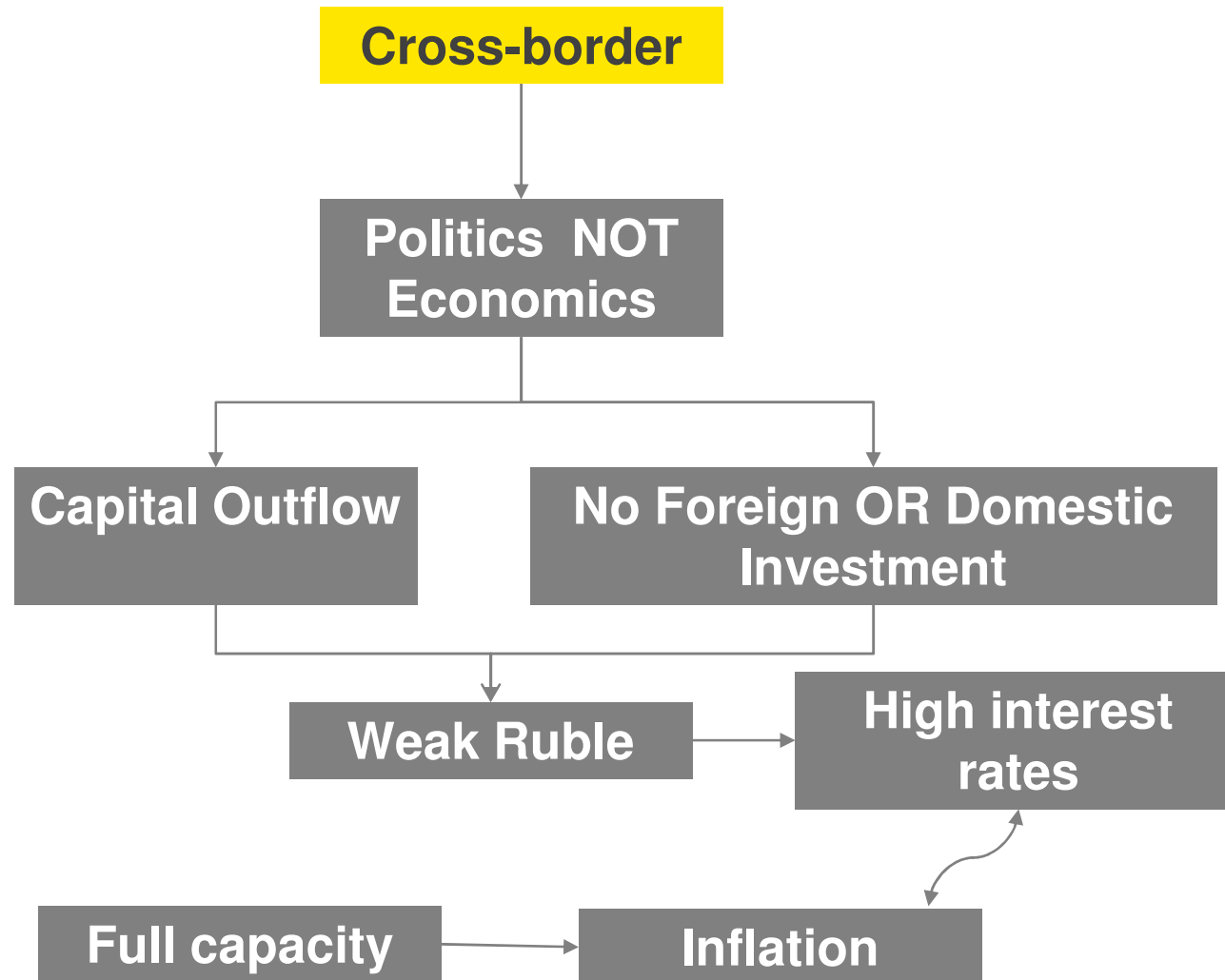
November 2014



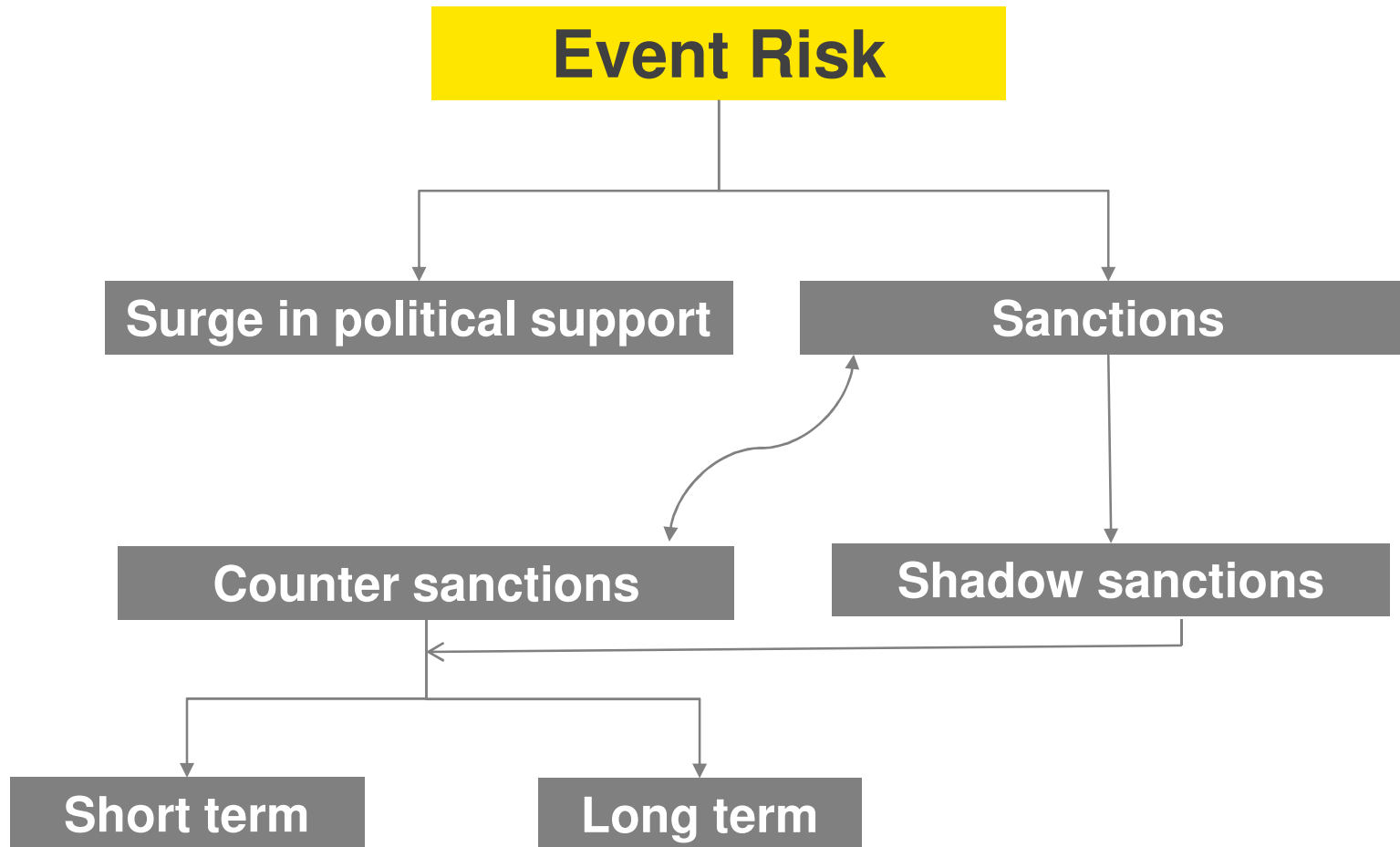
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Совершенствуя бизнес,
улучшаем мир

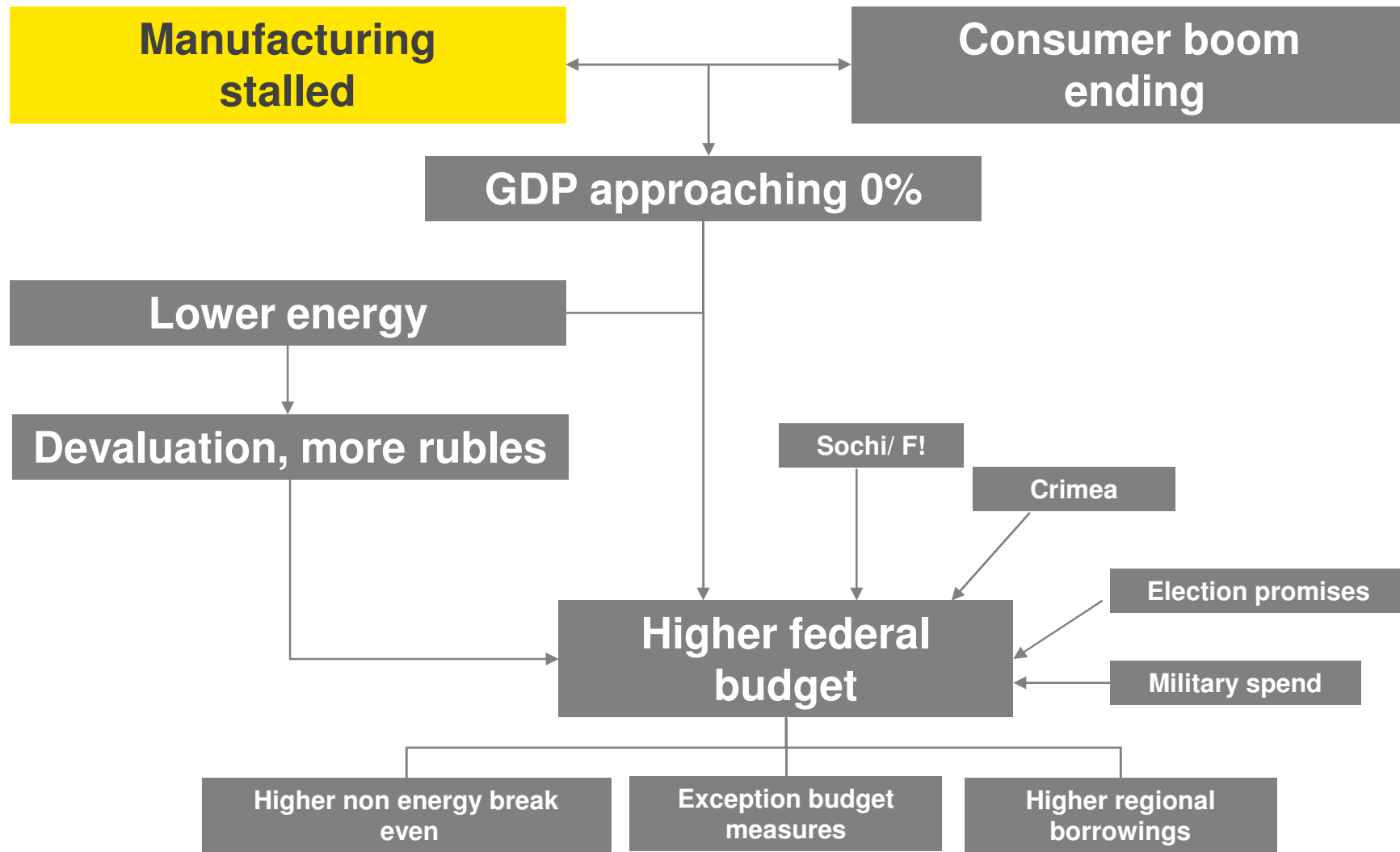
Developments



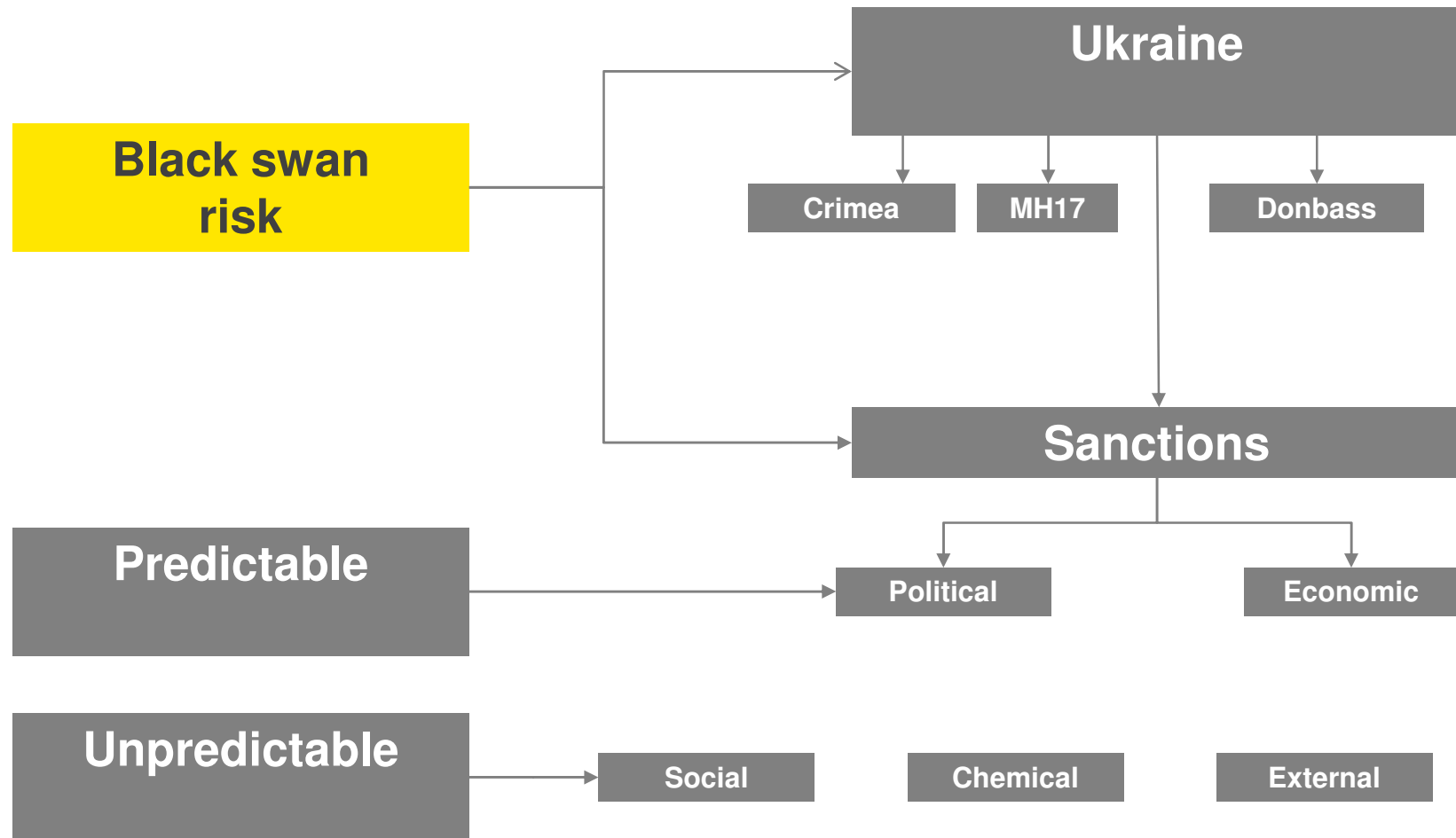
Event Risk Analysis



Domestic economy



Black swan risk



Big themes

- ▶ Political cross border risk, politics trumps economics.
- ▶ Capital flight and weak ruble reflect weakened confidence.
- ▶ Consumer boom has petered out (eg 26% drop yoy in car sales; retail sales only around 1% growth yoy by June).
- ▶ Brent crude in the low \$80's, for how long?
- ▶ State acquires Bashneft from Sistema, negative investment message.
- ▶ Sanctions and counter sanctions probably will not go away in the near term. Major impacts on the economy.
- ▶ GDP forecast for 2014 from 1.7% down to 0.2% maybe now; worse in 2015.
- ▶ The budget, federal borrowing pushed down to regions, medical insurance cap, issues of electoral pledges on salaries

Not a good place to start from

- ▶ Inflation over 8% with more to come from increased food prices (adding around 1.5% this year).
- ▶ CBR committed to inflation focus, increasing interest rate environment (5.5% to 9%), ruble remains weak.
- ▶ Absence of access to capital markets causes funding costs to increase.
- ▶ Ruble down 20% on year, helps local budget but reflects severe lack of confidence in the currency. Capital flight likely to top \$120bn.
- ▶ Retail lending due to slow (from 40% to 20% yoy) whilst corporate demand stays strong as bonds come back onshore.
- ▶ Manufacturing stays relatively strong but supported by military spend.
- ▶ Sanctions impact half the Russian debt directly and shadow.

Opportunities

- ▶ Import substitution across all sectors.
- ▶ Boost to local agribusiness from counter sanctions.
- ▶ PPP and other infrastructure spend will have heavy emphasis.
- ▶ Strong political support for the present.
- ▶ Development of own systemic supports eg National payment system.
- ▶ Ease of doing business has improved 30 places to #62 above China, Brazil and India, but negated by overall climate

Threats

- ▶ Politics trumps economics, reformers seem on the outside.
- ▶ Sistema appears to open Pandora's box for next steps.
- ▶ De offshorisation and dual nationality.
- ▶ Tightening internet rules.
- ▶ State employees increases only 5.5%, reduced disposable income.
- ▶ Wave of defaults on clean consumer will stress capital.
- ▶ When does consumer move out of rubles?
- ▶ S and P negative outlook one notch above junk for sovereign.
- ▶ Ukraine challenges economic and political destabilizes the region.

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