

AB-ICI: Retail lending in focus

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Investment Summary

- AB-ICI rose 0.2% in June reacting to the increased appetite for risk on the financial markets
- Retail lending started to cool in the last two months, market concerns about credit crunch risks
- The CBR is likely to use faster budget spending of 2H19 to intensify lending control at the cost of GDP growth

AB-ICI up 0.2% in June

AB-ICI up 0.2% under mixed trends

The AB-ICI was up 0.2% in June, however the index components delivered a mixed trend in June:

Economic confidence was mixed as the share of forex deposits declined to 20.9% but ruble-denominated deposit growth is below 7% y/y

- **Economic confidence** delivered a mixed performance. On the one hand the share of foreign currency deposits declined slightly to 20.9% of total deposits pointing to better confidence for ruble stability. At the same time, the nominal value of forex deposits kept increasing in June and reached \$96bn from \$88bn seen on the local accounts in December 2018. Also, the scale of the ruble-denominated retail deposit growth remains below 7% y/y, pointing to weakness in the local saving trend.

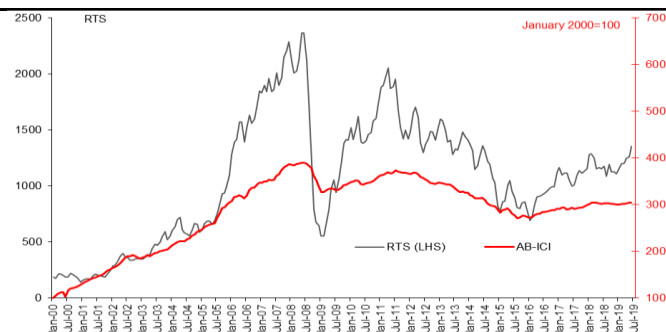
CDS were down and RTS up

- **Market confidence** remained positive with a continuing decline in CDS and continuing increase of the Russian RTS. At the same time to the large extent this growth seems to be not related to the Russia's specific reason but rather reflects the general increase in global appetite for risks.

Foreign confidence down as the presence of foreign banks in the banking sector was down to 8.0%

- **Foreign confidence** disappointed in June with the foreign banks market share from 8.3% to 8.0% level in one months. The decline in their presence is however not surprising – the intensified talks over the possible constraints of the foreign payments system operations in Russia are mainly hitting foreign banks operating in Russia and we generally consider local market being more friendly for the local rather than for foreign players

Fig. 1: AB-ICI and RTS Index: AB-ICI up 0.2% in June



Source: RTS, Alfa Bank

AB-ICI:

AB-ICI: Dedollarization a confidence measure

AB-ICI: Retail lending in focus

AB-ICI performance deviated from the poor GDP growth of 1H19 – in 1Q19 GDP grew only 0.5% and 2Q19 also risks bringing disappointment

The strong performance of the AB-ICI since the beginning of this year could be explained by the increase in global appetite for risk, however it clearly lacked support from growth. The 1Q19 GDP growth came 0.5%, below the official 0.8% y/y forecast and substantially below the 1.0-1.5% y/y projected by the CBR. The 2Q19 trend does not look to be much stronger: the Economy Ministry has estimated 1H19 growth at 0.7% y/y, implying some acceleration in 2Q19, but the CBR expects investment to have dropped 1.3-1.8% y/y last quarter after the 0.5% y/y increase reported by Rosstat for 1Q19. A number of indicators – the decline in Russian Railway's loading indicators by 3.5% y/y in 2Q19, decline in car sales in May-June – also points for the weakness in the economic trend.

Growing concerns in the coming months are related to retail lending – the market is convinced that this segment is in trouble and its growth should slow from 22% y/y currently to a more appropriate level of 15-20% y/y

A growing concern in the coming months is related to the dynamic of the retail lending and the possible implications of its deceleration on the economic performance. Local observers are convinced that retail lending in Russia is in bad shape. This perception is based on a number of very simple observations. First, the rapid retail loan growth was the subject of debate between the Economy Minister Maxim Oreshkin and the CBR Governor Elvira Nabiullina, with the CBR indirectly accused of not controlling lending risk. Second, during the past year, the CBR itself announced two rounds of measures to curb retail loan growth – the first was implemented from September 2018 and the other in March 2019 – however both failed to produce a cooling effect on the market, despite being reinforced by two rate hikes in September and December 2018. Finally, retail lending seems to have peaked in recent months, a development which in the past would have led to a path of contraction. Another reason for concern is that using the 2014 lending metrics as a benchmark for risk assessment, one could draw rather negative conclusions. The size of both the non-mortgage and mortgage loan book now exceeds the 2014 level and the non-mortgage loan-per-capita to average salaries is going to reach 145% by end-2019, which is approaching the 160-170% level seen in 2013-14. The cost of debt, which in 2014 was 4.1% of total household income, is likely to grow to 4.0% by end-2019, which also signals an accumulation of risk. All in all, it looks like before this year ends, lending growth is set to decelerate.

Funding for national projects which will intensify in 2H19 will provide the CBR with an opportunity to tighten retail lending control; reducing lending risks will, however, limit GDP recovery and thus the AB-ICI

Cooling the retail lending growth does not seem to be an easy task - as we stressed in our previous publications and as confirmed by the CBR release, the continuing retail loan growth is currently the main supportive factor for growth: in 1Q19, private consumption was the only contributor to GDP growth and without the acceleration of the retail loan growth seen in 1H19, economic growth rather would rather be zero. As a result, tightening lending conditions could immediately damage growth and the CBR ought to wait for an opportunity. One is expected to come relatively soon: funding for the national projects is projected to intensify before this year end and is the main reason behind positive growth expectations for 2020: according to polls conducted by Development Center, the consensus foresees Russian GDP growth to accelerate to 1.7% y/y in 2020 from 1.1% in 2019. A better growth pattern would provide an ideal opportunity for the CBR to slow retail lending growth; however, in this case, the positive effect of government spending would at least partially be neutralized by a weaker consumption pattern. As a result, assuming the CBR uses the coming quarters to follow Minister Oreshkin's advise to tighten retail lending regulation, it would be reasonable to expect only a modest GDP growth acceleration as opposed to the strong consensus growth forecast. All in all, while we see little chance Russia could experience a banking crisis because of the strong retail lending growth, the need to cool this segment will keep local growth capped and, thus, ruin the fundamentals for AB-ICI growth.

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