Rating-Agentur Expert RA GmbH assigned 'BB+' ratings to Russia

Rating-Agentur Expert RA GmbH assigned 'BB+' sovereign government credit rating (SGC) to Russia in national currency (Sufficient level of creditworthiness of the government), and 'BB+' in foreign currency (Sufficient level of creditworthiness of the government).

Rating-Agentur Expert RA GmbH assigned 'BB+' country credit environment rating (CCE) to Russia in national currency (Sufficient quality of credit environment of the country), and 'BB+' in foreign currency (Sufficient quality of credit environment of the country).

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

Positive factors:

- Low projected government debt load stood well below other major peers at 18,8% of GDP and 53,7% of budget revenues in 2015 (according to IMF estimations);
- Marginal levels of short-term debt at 1% of GDP and 2,8% of budget revenues in December 2015;
- FX reserves (USD 370 bn including gold reserves) are high enough to cover around 10 months of imports, laying above major peers. The amount of FX reserves has been increasing since the CBR introduced the free flotation of the exchange rate in late 2014;
- Budget deficit remains at a tolerable level (projected at 3% of GDP in 2015);
- Adequate management of the fiscal and monetary policy. Measures were put in place to stabilize the budget following the oil price decline. Additionally, the change of the FX policy to a free-floating regime combined with an increase of the key interest rate, refurbished FX reserves and cushioned the pass-through effect of devaluation on inflation rate;
- Banking sector still shows a profitable and solvent position with banks' assets/GDP at 105,5% and ROA at 0,25% as of 3Q 2015 as well as sufficient level of capital adequacy (average capital adequacy ratio was 9,3% by the end of 2015). However, the forecast is negative;
- As a result of western sanctions and lower consumption of imported goods in Russia, the trade balance reported a positive and higher figure in 2015 compared to 2014. Balance of goods and services/GDP amounted to 13,7% and 18,1% in 2014 and 2015 respectively.

Restricting factors:

- Following the economic contraction in Russia, the share of distressed loans in total loans increased to 7,4% in 2015 from 6,7% in 2014. However, this figure could be higher due to the large amount of rolled-over debt held by banks;
- High concentration of share trades in the 10 largest issuers (78,4% during 1H 2015). Additionally, market capitalization was low at 20% of GDP;
- Inflation has been steadily and constantly increasing from 6,1% in 2011 to 12,9% in 2015;
- Moderate economic competitiveness as evidenced by Russia's position in the Index of economic competitiveness from the World Economic Forum. In 2015 Russia was at 49th place out of 159 countries.

Negative factors:

- Decline of real GDP over the last three years (real GDP declined from 50,5 trillions of RUB in 2012 to 44,9 trillions of RUB in 2015);
- As a result of Western sanctions and a sharp RUB devaluation, inflation rate soared in 2014 and 2015 (CPI increased by 11,4% in 2014 and 12,9% in 2015);
- Relatively high yield on the 10-year government bonds (10,38% as of January 2016);
- High share of state-owned banks in the banking sector (TOP-6 Russian banks are directly or indirectly owned by the Government and represent around 60% of total banks' assets).

Stress factors:

- Concentration of tax revenues on one single industry. Almost half of fiscal revenues proceed from oil and gas taxation (weak stress-factor);
- Western sanctions on Russia, which had a negative impact on prices of imported goods and on international financing possibilities, remain in place (weak stress-factor).

ADDITIONAL FACTORS THAT INFLUENCED CCE RATINGS:

Negative factors:

- Significant fluctuation of real interest rate over the last six years.

Restricting factors:

- Average performance of the country's stock exchange index (MICEX) over the last six years;
- Moderately high private sector debt at 96% of GDP in 2015.

Positive factors:

- Moderately high quality of investors' protection in the country (Russia occupied the 66th place in the ranking of Protecting Investors (part of Doing Business) out of 180 countries in 2015);
- Low level of real interest rate, which was 3,8% in 2015.

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Withdrawal of western sanctions on Russia;
- Increase of oil prices on the face of better than expected world economic conditions.

The following developments could lead to a downgrade:

- Deterioration of the banking sector's solvency and profitability indicators;
- Sharp deterioration of government debt and fiscal metrics.

"The ratings of Russia reflect the country's underperforming macroeconomic indicators which resulted from deteriorating external conditions. Low oil prices since mid-2014 have fueled a sharp devaluation of the RUB and contributed to the constant deterioration of the country's fiscal position. While the government debt load remains low, the constantly increasing private sector debt presents one of the major long-term risks for the Russian economy.

The external position of the country remains sound as consumption of imported goods declined faster than overall exports during 2014-2015. Since the Central Bank of Russia moved to a free-floating regime in late-2014, FX reserves resumed growth providing the country with additional external buffers. Future developments of oil prices and a decision on the prolongation of sanctions will play a key role in the rating dynamic of Russia." – Clarified Gustavo Angel, Expert of Rating-Agentur Expert RA GmbH.

Responsible expert: Gustavo Angel, Expert of Rating-Agentur Expert RA GmbH.

Reviewer: Hector Alvarez, Expert of Rating-Agentur Expert RA GmbH.

Research report on Russia is available at:

http://www.raexpert.eu/reports/Research_report_Russia_29.01.2016.pdf

Next scheduled rating publication: 22 July 2016. The full sovereign rating calendar can be found at http://raexpert.eu/sovereign.php#conf-tab-5.

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Minute's summary

The rating committee for Russia was held on 27 January 2016. The quorum for the rating committee was present. After the responsible expert presented the factors, which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Sovereign methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the voting.

The following methodology was used for the rating assessment: Methodology for Assigning Sovereign Government Credit Ratings and Country Credit Environment Ratings. Short Public Version (from April 2015) can be found under the following link: (http://raexpert.eu/files/methodology/MethodologyShort_Credit_Ratings_Sovereign_2015.pdf). Descriptions and definitions of all rating categories can be found within the aforementioned methodology. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

These ratings are unsolicited. The rated entity did not participate in the rating process.

Main sources of information: Central Bank of Russia, Ministry of Finance of the Russian Federation, World Federation of Exchanges, Russian Federal State Statistic Service, International Monetary Fund, World Bank, Trading Economics, World Economic Forum, Doing Business, United Nations, Moscow Stock Exchange (MOEX).

Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information that was considered to be reliable, complete and non-biased. The responsible expert performed the rating assessment of the country with information considered as the most reliable and up to date in accordance to the overall position of the country and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

Despite similar methodologies, credit ratings of Russia from RAEX (Moscow) (both SGC and CCE) may be different from those assigned by Rating-Agentur Expert RA GmbH due to:

- Possible differences in expert assessments of individual factors;
- Some differences in methodologies (methodologies are similar but not identical);
- Differences in the date/period of assessment for individual factors.

Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. All employees involved in the rating assessment and revision of the rated entity have reported absence of conflicts of interests before initiation of the rating process.

Rating-Agentur Expert RA GmbH is completely independent from the activities of other agencies of the RAEX group.

Risk warning

The Agency disclaims all liability in connection with any consequences, interpretations, conclusions, recommendations and other actions directly or indirectly related to the conclusions and opinions contained in the Agency's Research Reports.

This Report represents the opinion of Rating-Agentur Expert RA GmbH and is not a recommendation to buy, hold or sell any securities or assets, or to make investment decisions.

Office responsible for preparing the rating

The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

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The European Securities and Markets Authority (ESMA), the EU's direct supervisor of credit rating agencies (CRAs), has registered Rating-Agentur Expert RA GmbH as a CRA under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, with effect from 1 December 2015.

Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.