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Russian Government Draws Up Rescue Plan for VEB Development Bank

By Peter Hobson

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Russian officials are discussing sweeping measures to save the government's development bank after its bailout needs rose to about $20 billion.

Vneshekonombank, also known as VEB, ran into difficulty after Western sanctions cut its access to international lending in 2014. The bank had borrowed heavily to fund Russia's Sochi Winter Olympics and other politically driven projects, and the sanctions left it struggling to repay the debts.

Despite an economic slump that is squeezing the government's finances, Prime Minister Dmitry Medvedev at a board meeting on Tuesday announced the government would give VEB 150 billion rubles ($2.2 billion) to boost its capital this year.

But the meeting also discussed a much broader rescue plan, according to the Vedomosti business newspaper, which on Wednesday obtained a document listing the proposed measures.

The plan, which would boost capital, increase liquidity and potentially shrink VEB's balance sheet and stock of bad loans, includes the following options:

• The Central Bank converts hundreds of billions of rubles in loans previously given to VEB into capital.

• A number of state organizations deposit a large amount of cash at VEB. These include 55 billion rubles ($815 million) by the Finance Ministry, a further 50 billion rubles from the National Welfare Fund, one of Russia's reserve funds, at least 100 billion rubles from Russia's Pension Fund, and deposits by unidentified state-owned companies.

• VEB sells assets including a 2.7 stake in Gazprom, the natural gas producer, worth around $1.3 billion at current stock prices, along with its shares in Russian banks Sviaz-Bank and Globex Bank, and Ukraine's Prominvestbank. VEB also sells its leasing operation, and the trains and planes belonging to it.

• Auditors are invited in to probe part of VEB Capital, one of VEB's subsidiaries.

• Spending on charitable causes is trimmed to 1 billion rubles ($15 million). It is unclear how much VEB previously spent on charity.

• Assets that are part of special projects, likely meaning Olympic and other loss-making loans, could be spun off into separate entities, potentially removing them from VEB's balance sheet.

It is unclear how much of the plan will be implemented, but "it solves the short term problems and allows VEB to repay $3 billion in overseas loans this year," said Karen Vartapetov, an analyst at ratings agency S&P.

However, it is unlikely to remove the bank's fundamental structural problems, he said. These include a bloated corporate structure, massive non-performing loans and an investment strategy that is driven by politics.

Since its creation in 2007, VEB has been closely overseen by President Vladimir Putin. Despite its stated aim of financing export and industrial modernization, it has repeatedly been used to achieve the government's aims.

It rescued banks and industry during the economic crisis of 2008-9, funneled billions of dollars into Olympic construction for the 2014 Sochi Games and and, in a series of secretive deals over 2009-10, lent more than $8 billion to Russian investors to buy up industrial plants in eastern Ukraine.

Much of the lending has proved unprofitable. Essentially, VEB was used as an off-budget funding vehicle for the state's special projects, Vartapetov says.

According to the TASS news agency, Medvedev on Tuesday said: "Despite the current situation, we are not talking about changing the general goals for which VEB was created. The bank will continue be a leading development institute and fund major projects in multiple sectors of the economy."

That means the rescue package may be used to paper over cracks, rather than fundamentally

reform VEB. “The bank will always be a both a commercial and political structure, and it will be difficult to separate those functions,” Vartapetov said.

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