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Russia's Economy Gives Putin Reasons Not to Extend OPEC+ Deal

The Russian leader is having to weigh up his desire for faster growth against the benefits of his alliance with Saudi Arabia.

By Bloomberg

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Oil production cuts are weighing on economic growth. **Alex Watson / Flickr (CC BY-NC 2.0)**

The OPEC+ pact is hurting the Russian economy, potentially giving President Vladimir Putin a reason not to agree on an extension of the deal.

While higher crude prices can bring the Kremlin additional revenue, production cuts are weighing on one of the country's biggest industries. As the Russian leader decides whether to prolong the curbs into the second half, he may have to weigh his desire for faster economic growth against the benefits of his alliance with Saudi Arabia.

"The OPEC+ deal was one of the factors behind slower economic growth in Russia in the first

quarter," said Kirill Tremasov, a former economy ministry official who's now an analyst at Loko-Invest in Moscow. "Given the oil price is now comfortable for the state budget and that crude producers are willing to pump up more, Russia may not want to extend the deal."

Russia's GDP unexpectedly grew just 0.5 percent in the first quarter, below all 14 estimates in a Bloomberg survey. That compares with a 2.7 percent increase in the last three months of 2018, which was the highest in more than six years as crude output reached a record 11.45 million barrels a day in December, according to ministry data as OPEC+ curbs eased.

In its deal with the Organization of the Petroleum Exporting Countries, Moscow pledged to reduce the country's oil output by 228,000 barrels a day. While many of its OPEC allies, including the group's de-facto leader Saudi Arabia, say they prefer extending the agreement, which expires next month, Russia has talked about relaxing the cuts.

The economy ministry reiterated that the current deal is "a restraining" factor for the nation's hydrocarbon production and mining. Data due Wednesday or Thursday is forecast to show that annual growth in industrial output was 2 percent in April, with estimates ranging from 0.8 percent to 3.9 percent, according to a Bloomberg survey of 15 economists.

Putin, who previously stated Russia will continue cooperation with OPEC+, is keeping all options on the table. "There are plans of our companies to develop new deposits, and we have a very attentive approach to that. We understand that the production shouldn't stop, investment should come to the sector, otherwise that may create problems both for us and for global energy," Putin said last month. "That's why there will be balanced decisions."

Related article: OPEC+ Affirms Commitment to Oil Cuts, Defers Decision to Extend

Fixed-capital investment in oil and natural gas output fell 2.3 percent last year, leading to an "extremely low" growth of investment in hydrocarbon production and mining, compared with a 2.2 percent total increase of fixed-capital investment, according to calculations from the Centre of Development Institute at the Higher School of Economics.

Rosneft PJSC, which pumps almost half of Russia's daily production, warned there will be a postponement of some projects for a few months "as a minimum" amid uncertainty over the OPEC+ deal.

Price boost

While the decline in output under the OPEC+ agreement is a negative for the economy, any slowdown is "easily offset by significant additional revenues that appear from higher oil prices" resulting from the deal, said Stanislav Murashov, an economist at Raiffeisenbank in Moscow. "With such global uncertainty and trade wars, Russian government is likely to prefer additional revenues that will increase its safety cushion," he said.

The OPEC+ agreement has boosted the federal budget amid higher prices for energy commodities, which account for almost half of state finances. Additional revenue for the budget was about 6 trillion rubles ($93 billion) in the past two years, based on an energy

ministry estimate that the output-cut deal resulted in a $10 increase per barrel in prices.

Under the so-called budget rule, all extra revenue from oil prices above $40 per barrel is transferred to a rainy-day fund which is now worth $59 billion, or 3.6 percent of GDP.

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