

# Profit Slumps Herald More Trouble Ahead for Russia's Corporate Giants

Russian companies' first quarter financial results are already showing the impact of the coronavirus. The worst is yet to come.

By [Jake Cordell](#)

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Rosneft CEO Igor Sechin has overseen the oil giant's first quarterly loss in eight years. **Kremlin.ru**

Russia's blue chip companies have posted some of the bleakest financial results for years in the first few months of 2020, with analysts saying the hit to earnings will only grow sharper.

Energy giants, banks and airlines all saw their earnings slump over the first three months of the year, and the damage could last well beyond the coronavirus as economists don't expect economic activity in Russia to rebound anytime soon.

Just over half of Russia's largest corporates have already published financial results for the first quarter — covering the period of peak financial volatility in mid-March but only the first

few weeks of the coronavirus economic slowdown in Europe and Russia.

The figures represent what could be the tip of the iceberg in terms of plunging earnings.

### **Banks: Loan losses and macro headaches**

State-owned lender Sberbank — Russia's largest bank — has already seen profits atrophy, down 47% in the first three months of the year in official results.

Another trading update gave a sign of how bad the earnings picture could get for Russian companies once the period of Russia's "non-working" weeks, introduced at the end of March, is included — profits were down 85% in April compared to last year.

With most companies only posting results for the first three months of the year, the biggest immediate hit from the coronavirus has not yet been reflected in results. Regardless, Russian banks are bracing for a much longer hit to earnings than just one or two quarters, Dmitry Puchkaryev, an analyst at BCS, told The Moscow Times.

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"It's not possible to talk about improving results in the banking sector anytime in the near future, as the problems in the domestic economy due to the pandemic may have long-lasting consequences for lenders," he said.

Sberbank has increased its provisions for losses on its loan book eightfold in response to rising unemployment and falling earnings.

Rival VTB — also state-owned — saw profits down 14% in the first quarter as it also increased loss provisions and marked down the value of its investments.

Analysts at VTB Capital, the investment arm of VTB, said financial earnings in the sector will likely not bounce back for at least 18 months.

"The size of [government] aid to the banking sector and borrowers is more modest than during the crises of 2008 and 2014. We therefore believe that the effect of the Covid-19 outbreak is likely to be absorbed by banks with delay ... with earnings fully recovering only in 2022," Mikhail Shlemov, an equities analyst at VTB Capital wrote in a research note.

### **Energy: Low prices and low production**

Russia's energy giants are also bracing for a longer-term hit, fuelled by the double whammy of lower oil prices and forced output production due to the renewed OPEC+ agreement between Russia and Saudi Arabia.

Oil goliath Rosneft posted its first quarterly loss in eight years, hemorrhaging \$2.2 billion during the first three months of the year. That was more than twice as bad as analysts had expected, and came even before the [chaos](#) on the oil markets in April.

Rosneft's numbers were the "first harbinger of real trouble," VTB's head of oil and gas research, Dmitry Loukashov said.

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"As the quarantine measures are curtailed, oil demand may gradually recover, and the OPEC+ agreement will provide additional support to the market. However, this can be expected only in the third or fourth quarters if the epidemiological situation stabilizes," BCS's Puchkaryev said.

Russian oil companies also face longer-term challenges from the OPEC+ agreement. The nature of Russian oil extraction means that stopping production at some wells, in the Arctic for instance, could cause them to freeze over, making it both more expensive to restart production and potentially creating a permanent hit to output.

### **Technology: Diversified income and deep pockets**

The picture at Russia's two flagship technology firms — Yandex and Mail.Ru — was more mixed, with their diversified holdings, earnings streams and cash buffers providing a degree of protection.

Revenues at both grew during the first quarter, up 25% at Yandex and 14% at Mail.Ru, while [profits](#) fell back — nothing like at Sberbank or Rosneft — in a sign of the firm's sprawling expansion and growing cost bases. Yandex's profits were down 5%, while Mail.Ru's fell 22%.

A drop in advertising revenue is expected to hit both harder in the second quarter, while the quarantine in big cities has seriously affected Yandex's transport units. Customers at market leader Yandex Taxi dropped 70% between the beginning and end of March, while a ban on car sharing in Moscow has seen Yandex Drive's fleet of around 20,000 cars sit idle since early April.

Meanwhile, a 75% jump in the use of online food delivery services, such as express grocery service Yandex Lavka and restaurant delivery app Yandex Eats, has cushioned the fall. The company also highlights its almost 200 billion ruble (\$2.75 billion) cash pile as enough to weather the storm.

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Mail.Ru's management withdrew its earnings guidance for 2020 — a measure taken by many firms — stating volatility was too high to give an idea of how much cash it will bring in. Nevertheless, the company struck an upbeat tone in a conference call with investors, pointing to revenues more than doubling at its own food delivery venture, Delivery Club over the last year and highlighting the sector as "the largest net beneficiary from Covid-19."

"We believe this crisis will lead to a permanent shift in consumer and business behavior with increasing digitalization across a broader set of industries and a wider share of the population," said Matthew Hammond, Mail.Ru's chief financial officer.

## Bright spots

The first stream of earnings results since the coronavirus pandemic started has also revealed some Russian winners from the crisis.

“Among those companies whose results were not adversely affected by the coronavirus are the Moscow Exchange, Magnit and X5 Retail,” said Puchkaryev.

“Panic on the world markets in the first quarter led to a strong increase in volatility and an increase in trading on the Moscow Exchange. In March, the trading platform reported record trading volumes,” he added, pointing to profits jumping 91% to 5.9 billion rubles (\$81 million).

Revenues at retailers Magnit and X5 Retail were up by more than 10% each in the first three months, boosted by [panic-buying](#) and [orders](#) for people to stay at home.

## A slow recovery?

For most of Russia’s largest companies, the true hit of the coronavirus has not yet been reflected in the results reported so far. The second quarter started with a six-week nationwide “non-working period” that shut down 30% of the Russian economy, and the official lockdowns in Moscow and St. Petersburg are ongoing.

There are concerns that muted levels of government support for households and businesses could mean a slow recovery. Surveys show that up to 60% of Russian businesses say government support is either completely useless or just postponing their problems.

Consumer spending is also likely to suffer — the outlook for salaries and employment is at its worst for five years, a Deloitte [survey](#) of Russia’s leading chief financial officers (CFOs) recently found.

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“Corporate expectations about the future have plummeted to levels last seen in 2008–2009,” [said](#) Heli Simola, a senior economist focusing on Russia at the Bank of Finland.

Such weak confidence in the boardroom highlights the potential long-term nature of the corporate crisis Russia could be facing. Seven in ten CFOs expect income to fall over the next six months, and more than half believe revenues will still be down by the end of 2021, Deloitte found.

In the earnings reports already released, a number of companies have announced postponements to dividend payments, while others — including retailers who have seen a shift to online buying — are cutting back on investment programs or putting planned strategy updates and expansion plans on hold.

Gunter Deuber, head of economics at Raiffeisen Bank wrote in a recent report: “Russian elites have little interest in taking on more risks.”

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