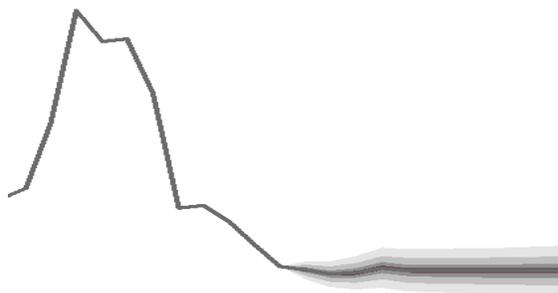


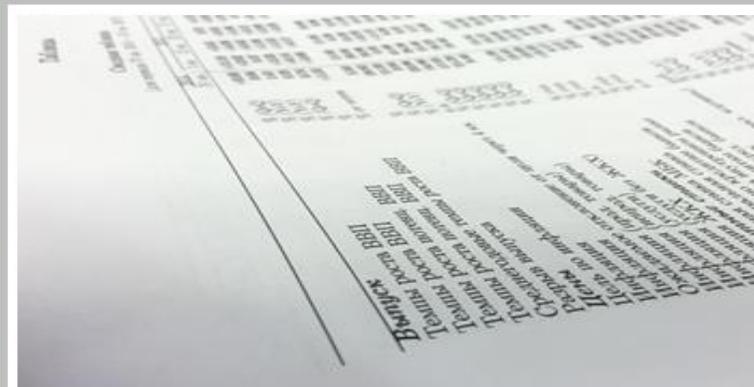


Bank of Russia

The Central Bank of the Russian Federation



4%



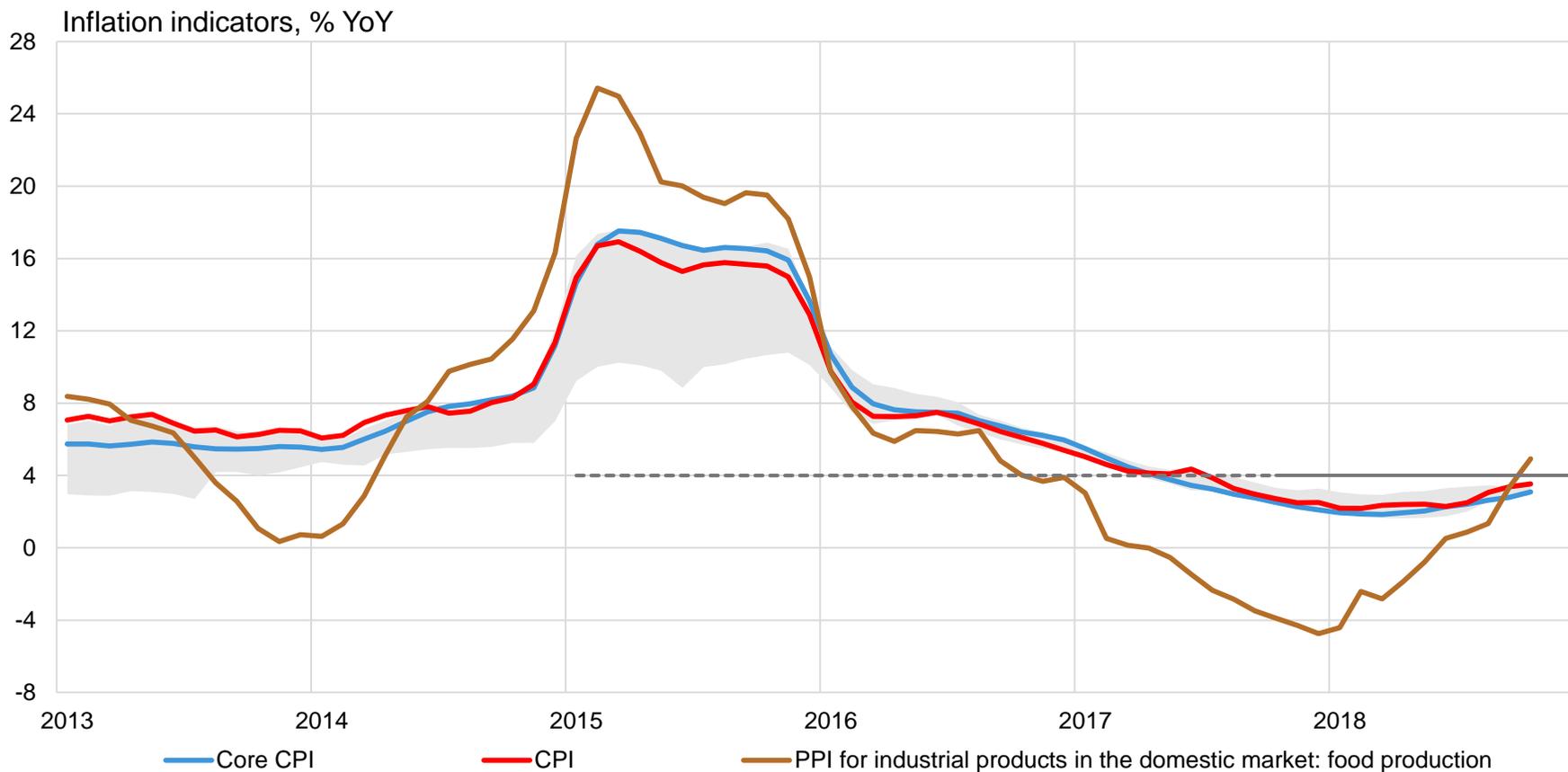
# RUSSIA'S ECONOMIC OUTLOOK AND MONETARY POLICY

December 2018



## Consumer prices (1)

At the end of 2018, inflation is expected to be close to 4%, which corresponds to the Bank of Russia's target

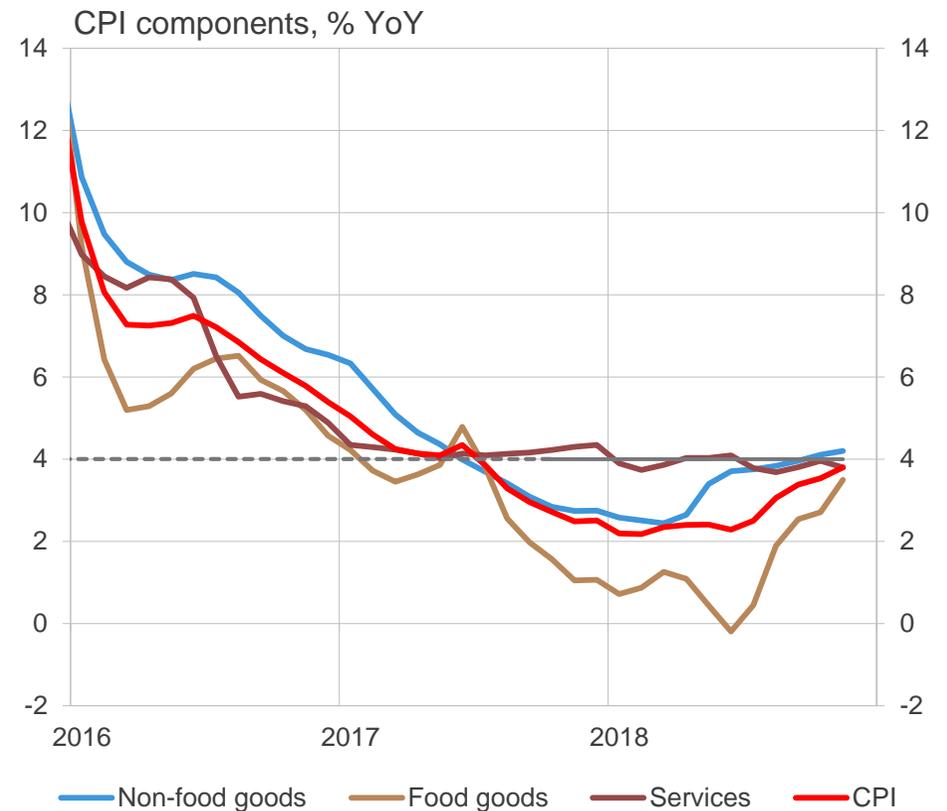
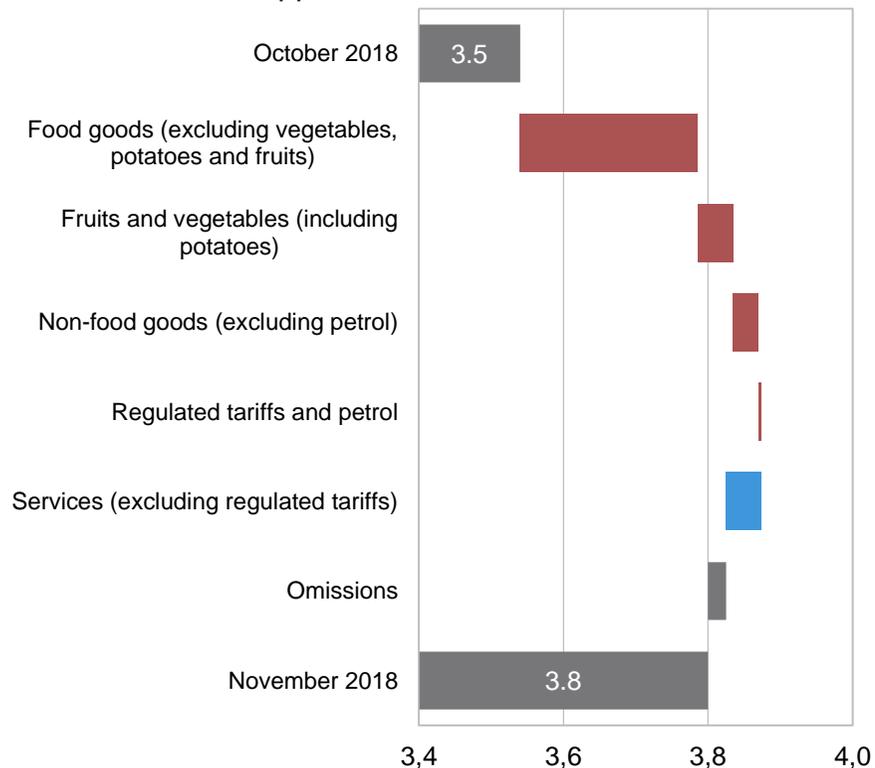




## Consumer prices (2)

This November's upward movement of inflation was largely driven by annual food price growth accelerating from 2.7% to 3.5%. Prices are further adjusting to the ruble exchange rate that has weakened since the beginning of the year and to the VAT increase scheduled to take effect from 1 January 2019

Contribution of **components** to the change in annual inflation in November 2018, ppts





## Inflation expectations – summary

Horizon		2017						2018											
		I	II	III	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
<b>Inflation expectations (absolute numbers), %</b>																			
<b>Households</b>																			
FOM	Next 12 months	11.2	10.3	9.6	9.9	8.7	8.7	8.9	8.4	8.5	7.8	8.6	9.8	9.7	9.9	10.1	9.3	9.8	
FOM (observed inflation)	Prev. 12 months	14.0	12.4	11.2	11.2	10.4	10.0	9.9	9.4	9.2	8.3	9.2	10.6	10.3	10.4	10.2	10.1	10.1	
FOM (Bank of Russia calculations)	Next 12 months	4.0	4.0	2.8	2.5	2.3	2.4	2.1	2.1	2.2	2.2	2.2	2.6	2.8	3.5	3.8	3.8	4.4	
<b>Professional analysts</b>																			
Bloomberg	2018		4.0	4.0	4.0	4.0	4.0	4.0	3.8	3.6	3.6	3.7	3.8	3.8	3.7	3.9	3.9	4.0	
Interfax	2018	4.2	4.1	4.1	3.9	3.9	3.9	3.8	3.8	3.7	4.0	3.8	3.8	4.0	4.0	3.9	3.9	4.0	
Reuters	2018		4.1	4.0	4.0	4.0	4.1	3.8	3.8	3.6	3.8	3.7	3.8	3.8	3.8	3.8	3.9	3.8	
Bloomberg	2019											4.0	4.0	4.2	4.4	4.7	4.5	4.6	
Interfax	2019							3.6	3.7	3.8	4.1	4.0	4.1	4.3	4.4	4.3	4.2	4.4	
Reuters	2019										3.9	3.9	4.0	4.3	4.5	4.5	4.5	4.7	
<b>Financial markets</b>																			
OFZ IN (option not subtracted)	Next 5 years	4.9	4.6	4.2	4.0	4.1	5.1	4.0	3.9	3.8	4.1	4.2	4.5	4.6	5.2	5.3	5.5	5.4	
OFZ IN (option not subtracted)	Next 10 years											4.3	4.6	4.6	5.0	5.4	5.2	5.2	
<b>Inflation expectations (balanced index*)</b>																			
<b>Households</b>																			
FOM	Next 12 months	-1.0	-1.4	-5.3	-3.0	-5.7	-4.4	-4.5	-0.7	-1.4	0.9	3.6	9.8	7.6	10.0	6.5	9.1	11.8	
FOM	Next month	-12.3	-13.3	-16.0	-16.7	-17.7	-15.7	-16.5	-17.4	-15.4	-15.8	-12.8	-7.7	-10.3	-6.8	-6.9	-5.1	-5.3	
<b>Businesses</b>																			
Bank of Russia monitoring	Next 3 months	7.4	9.3	7.3	7.2	7.3	7.1	6.5	6.9	8.5	9.8	10.2	11.0	11.2	12.4	12.9	13.6		
PMI input prices	Next month	7.8	9.0	12.2	12.4	14.6	10.6	9.2	11.4	12.2	27.4	27.2	28.4	21.6	22.8	24.2	23.4	22.6	
PMI output prices	Next month	1.0	3.4	6.8	3.6	3.0	3.0	2.8	2.8	4.0	13.6	6.4	6.6	8.2	6.6	5.8	7.6	7.6	
Retail prices (Rosstat)	Next quarter	27	24	24			22				20		20			20			
Tariffs (Rosstat)	Next quarter	4	3	0			0			5			5			0			

**Change:**

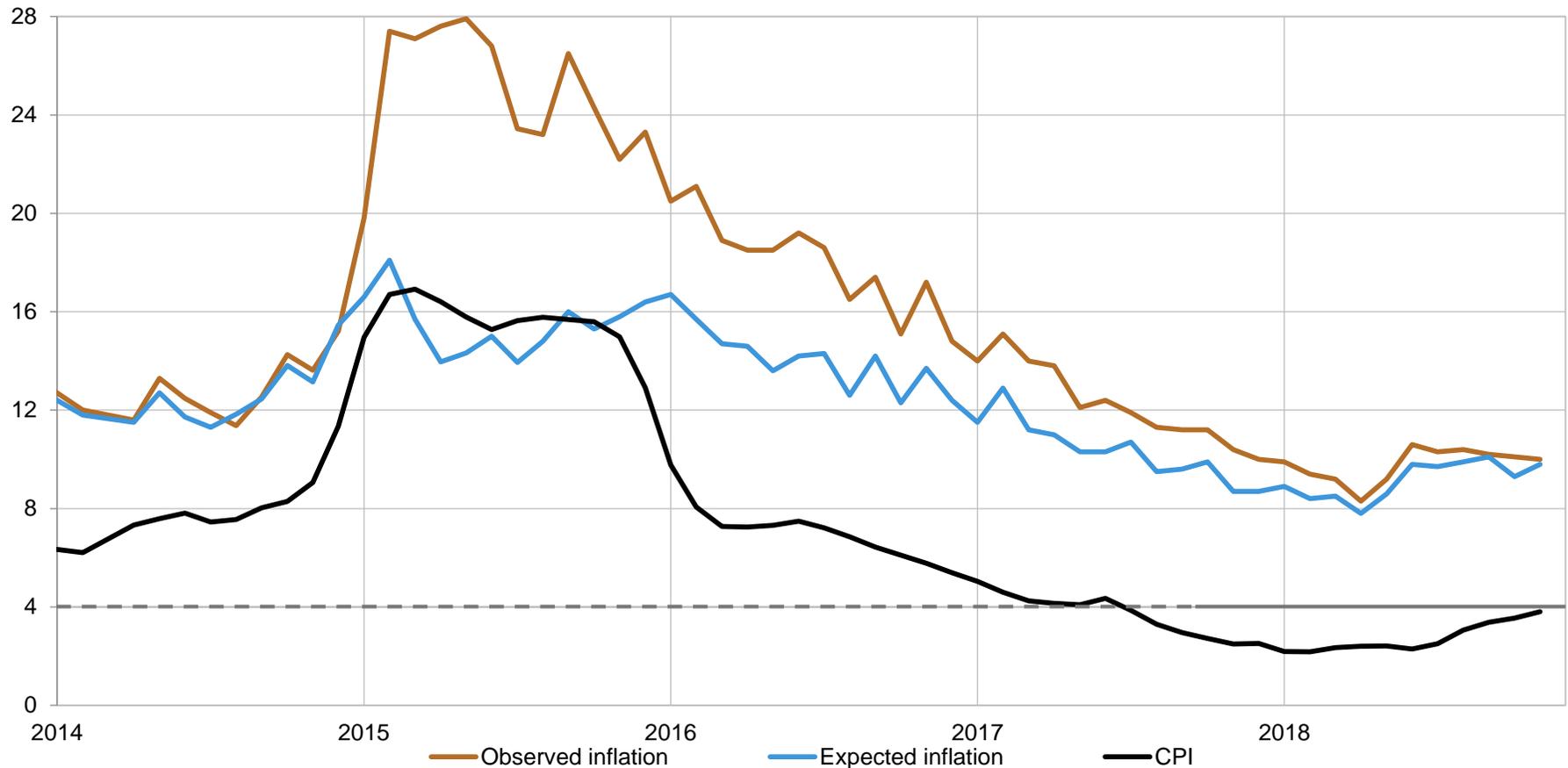
- Inflation expectations become better (more than 1 standard deviation)
- Inflation expectations become better (less than 1 standard deviation)
- Inflation expectations unchanged ( $\pm 0,2$  standard deviations)
- Inflation expectations become worse (less than 1 standard deviation)
- Inflation expectations become worse (more than 1 standard deviation)

\*Balanced index is the difference between the shares of those who expect prices to rise and to fall



## Inflation expectations – households

In November, household inflation expectations increased to 9.8% (+0.5 pts) and once again got close to the observed inflation

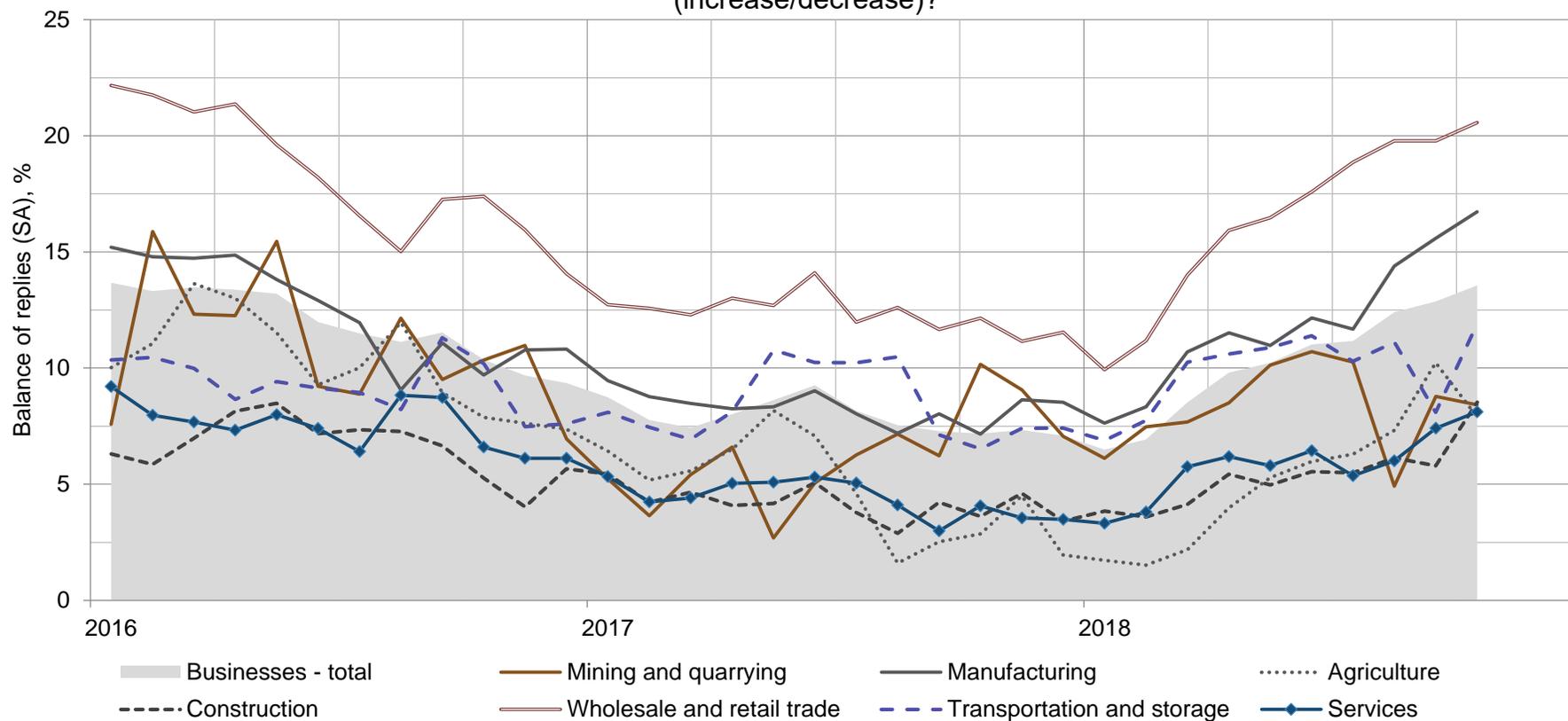




## Inflation expectations - firms

Short-term inflation expectations of firms are rising ahead of the VAT increase

Replies of firms to the question: “How will the prices of final goods change in the upcoming 3 months (increase/decrease)?”

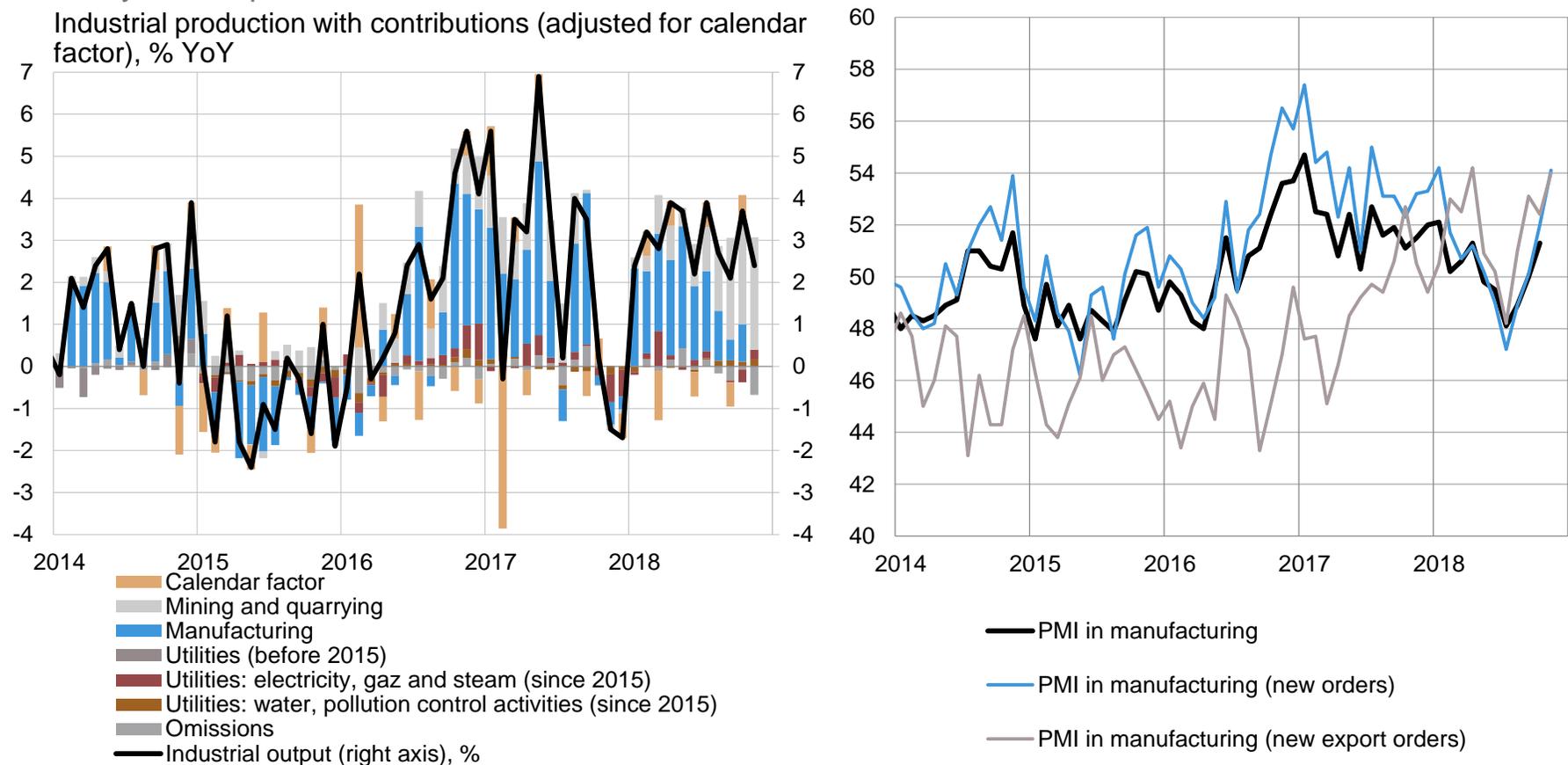


Sources: Bank of Russia's monitoring of enterprises survey



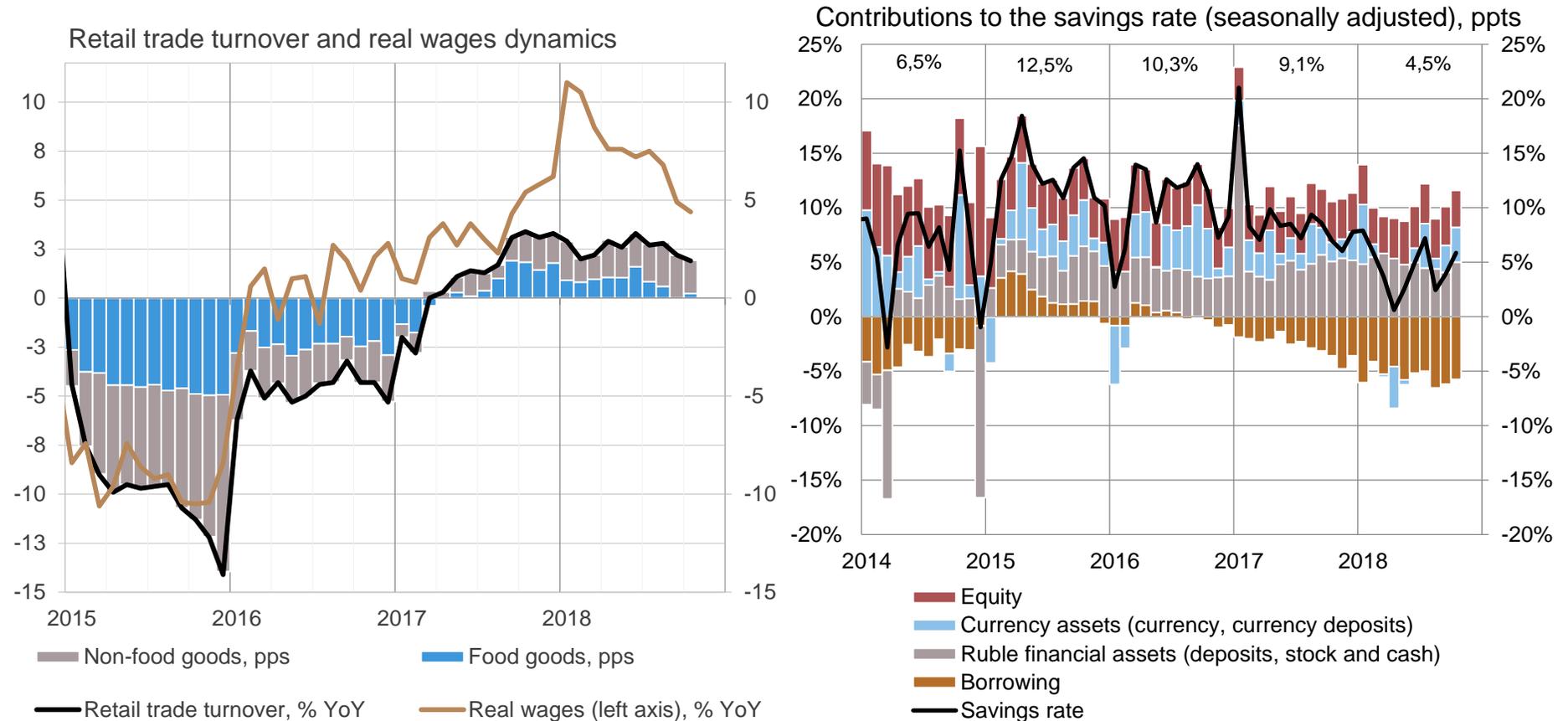
## Economic activity

Industrial production keeps expanding at around 3% p.a., but the mix of growth entirely shifted from manufacturing to upstream resource industries. Manufacturing PMI reverted to expansion territory, driven by new export orders



## Retail sales and savings rate

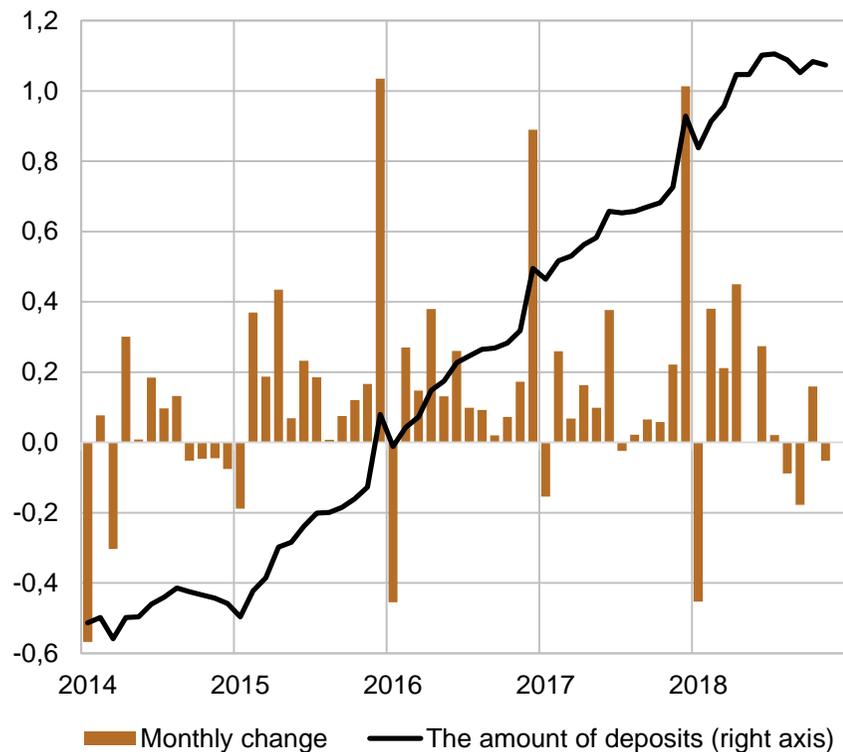
Consumer demand growth is moderating with retail sales at +1.9% in October, still mostly driven by non-food sales. Savings rate bounced back to 6%, which is still well below 2015-17 averages.



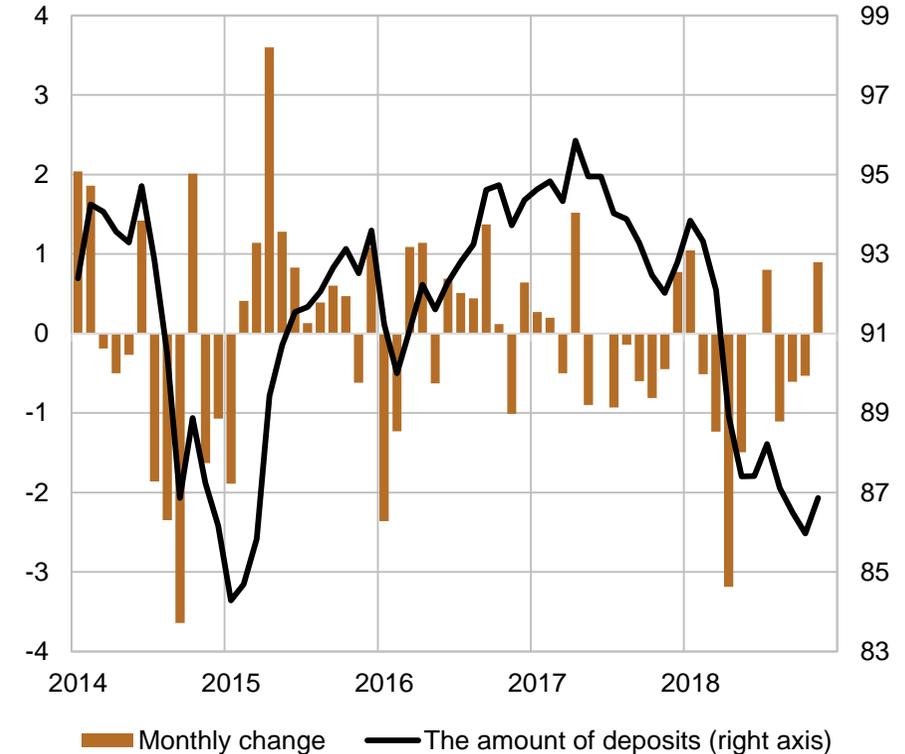
## Deposits – households

In November rouble deposits were marginally down, but FX deposits gained after three months of outflows

Ruble deposits of households in Russian banks,  
trln rub



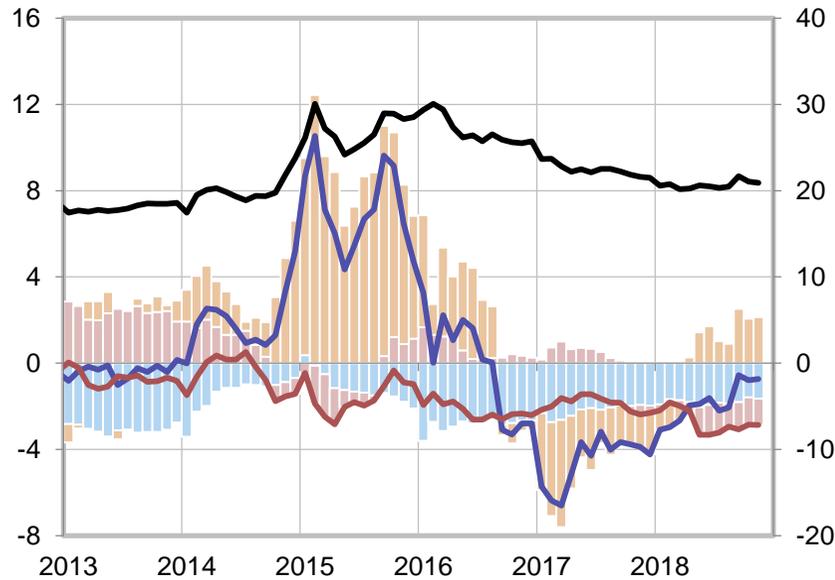
FX deposits of households in Russian banks, bln  
USD



## Deposits – share of FX deposits

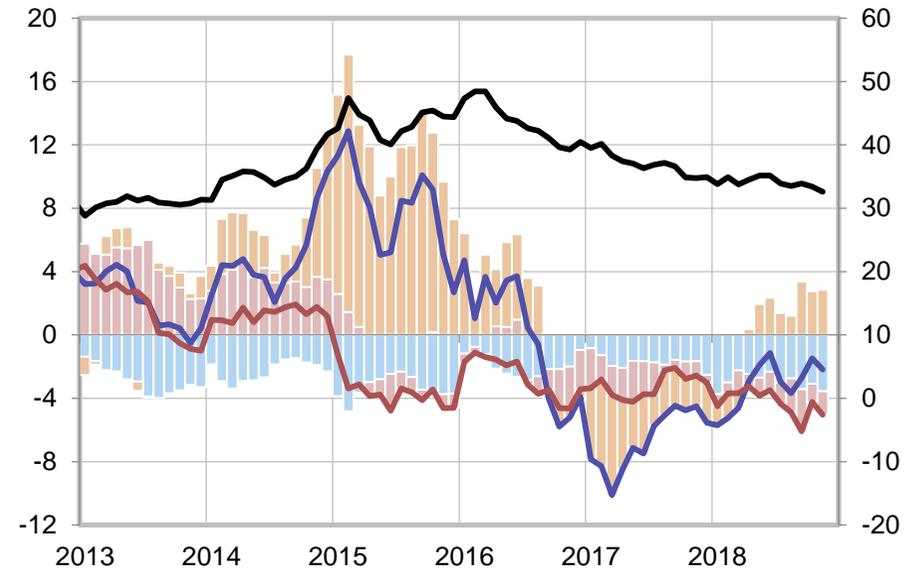
Fairly stable since the start of the year for households and is trending down for corporates

Contribution of factors to the annual change of household's deposit dollarisation, ppts



- Ruble exchange rate
- FX accounts balance
- Ruble accounts balance
- Overall change
- Change without foreign currency revaluation
- Level (right axis), %

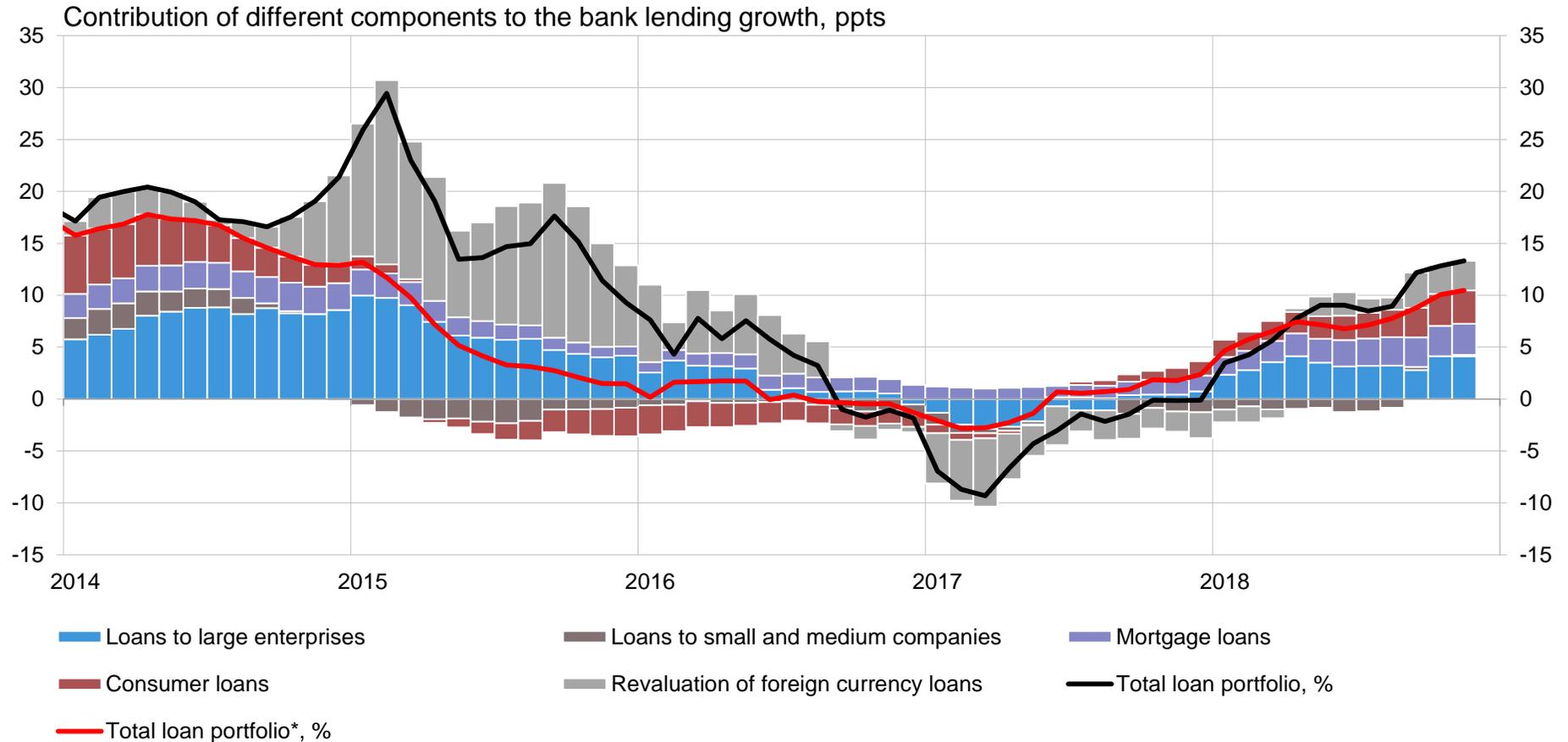
Contribution of factors to the annual change of NFO's dollarisation of accounts and deposits, ppts



- Ruble exchange rate
- FX accounts balance
- Ruble accounts balance
- Overall change
- Change without foreign currency revaluation
- Level (right axis), %



## Loans – growth rate still on the rise, both for retail and corporate lending



\* Excluding foreign currency revaluation



## Monetary policy and inflation around the globe

In 2019 the rise in interest rates is expected to continue in developed and most of the developing economies

	Current situation				Analysts' expectations				
	13.12.2018	Δ 6M (bps)	Nov.2018	Δ 6M (ppts)	Q4 2019	Δ to the current rate (bps)	Q4 2019	Δ to current inflation (ppts)	Rise is expected (↑) / Reduction is expected (↓)
	Interest rate		Inflation (YoY)		Interest rate		Inflation (YoY)		
<b>Developed economies</b>									
USA (upper bound)	2.25%	(+50)	2.2%	(-60)	3.25%	(+100)	2.3%	(+10)	↑
Canada	1.75%	(+50)	2.4%	(+20)	2.50%	(+75)	2.2%	(-20)	↑
United Kingdom	0.75%	(+25)	2.4%	(-)	1.00%	(+25)	2.0%	(-40)	↑
Norway (Deposit Rate)	0.75%	(+25)	3.5%	(+120)	1.25%	(+50)	2.2%	(-130)	↑
Eurozone (Main refinancing rate)	0.00%	(-)	2.0%	(+10)	0.05%	(+05)	1.5%	(-50)	↑
Japan (Target rate)	-0.10%	(-)	1.4%	(+80)	-0.04%	(+06)	1.9%	(+50)	↑
Australia	1.50%	(-)	1.9%	(-)	1.75%	(+25)	2.3%	(+40)	↑
Switzerland	-0.75%	(-)	0.9%	(+10)	-0.50%	(+25)	0.9%	(-)	↑
<b>Developing economies</b>									
Argentina (LELIQ 7-D Notes Rate)	59.13%	(+1913)	45.9%	(+2000)	32.00%	(-2713)	27.0%	(-1890)	↓
Turkey	24.00%	(+750)	21.6%	(+950)	24.00%	(-)	14.7%	(-690)	-
Indonesia	6.00%	(+150)	3.2%	(-)	6.50%	(+50)	4.1%	(+90)	↑
India (Repo Rate)	6.50%	(+50)	2.3%	(-260)	7.00%	(+50)	5.1%	(+280)	↑
Mexico	8.00%	(+50)	4.7%	(+20)	8.00%	(-)	3.7%	(-100)	-
South Africa	6.75%	(+25)	5.2%	(+80)	7.00%	(+25)	5.2%	(-)	↑
Chile	2.75%	(+25)	2.8%	(+80)	3.63%	(+88)	3.0%	(+20)	↑
South Korea	1.75%	(+25)	2.0%	(+50)	2.00%	(+25)	1.8%	(-20)	↑
China (Lending Rate)	4.35%	(-)	2.2%	(+40)	4.35%	(-)	2.3%	(+10)	-
Brazil	6.50%	(-)	4.1%	(+120)	8.00%	(+150)	4.3%	(+20)	↑
Poland	1.50%	(-)	1.2%	(-50)	1.50%	(-)	2.4%	(+120)	-
Taiwan	1.38%	(-)	0.3%	(-144)	1.50%	(+12)	1.4%	(+110)	↑

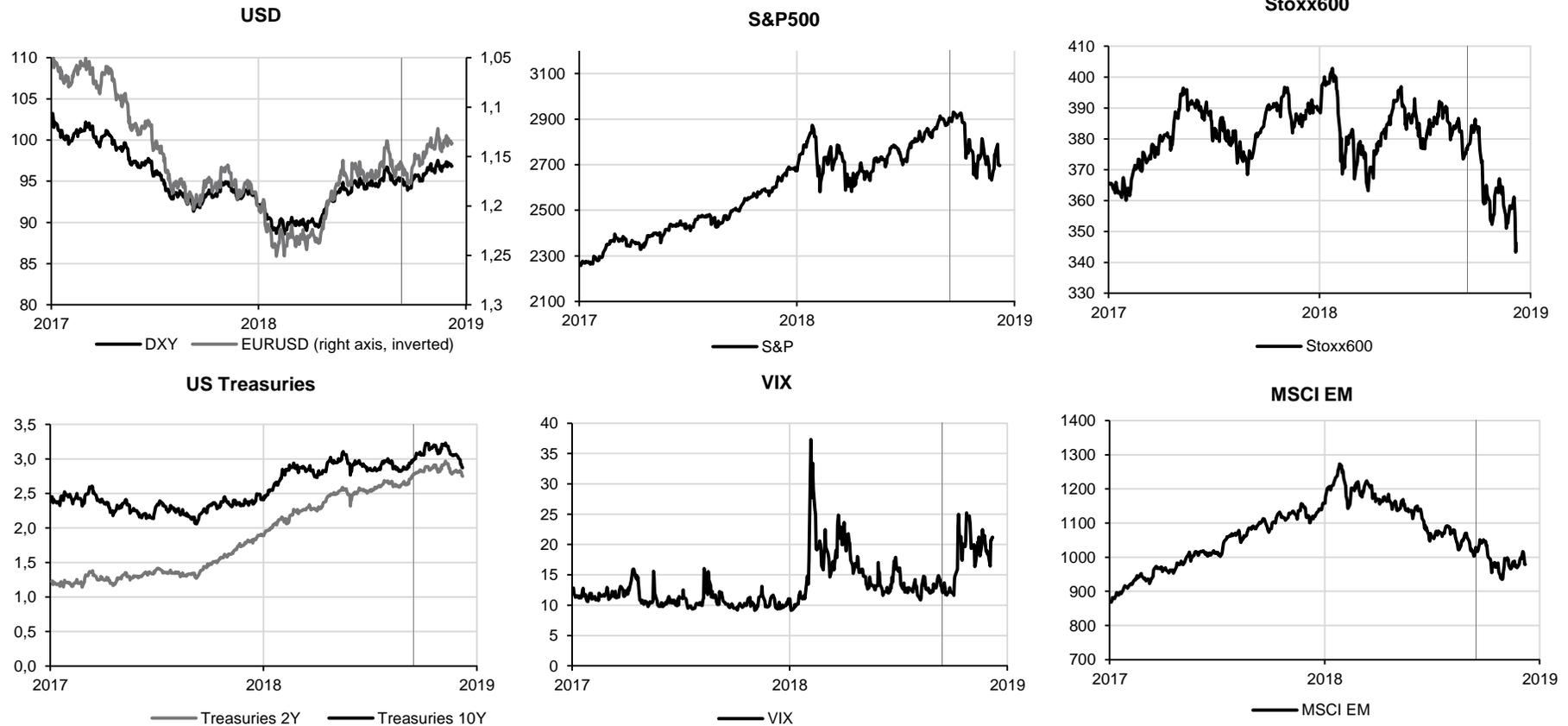
Inflation data for Canada, UK, Argentina is as of October 2018. For Australia – as of Q3 2018. For other countries – as of November 2018.

Source: Bloomberg



# Financial markets – global

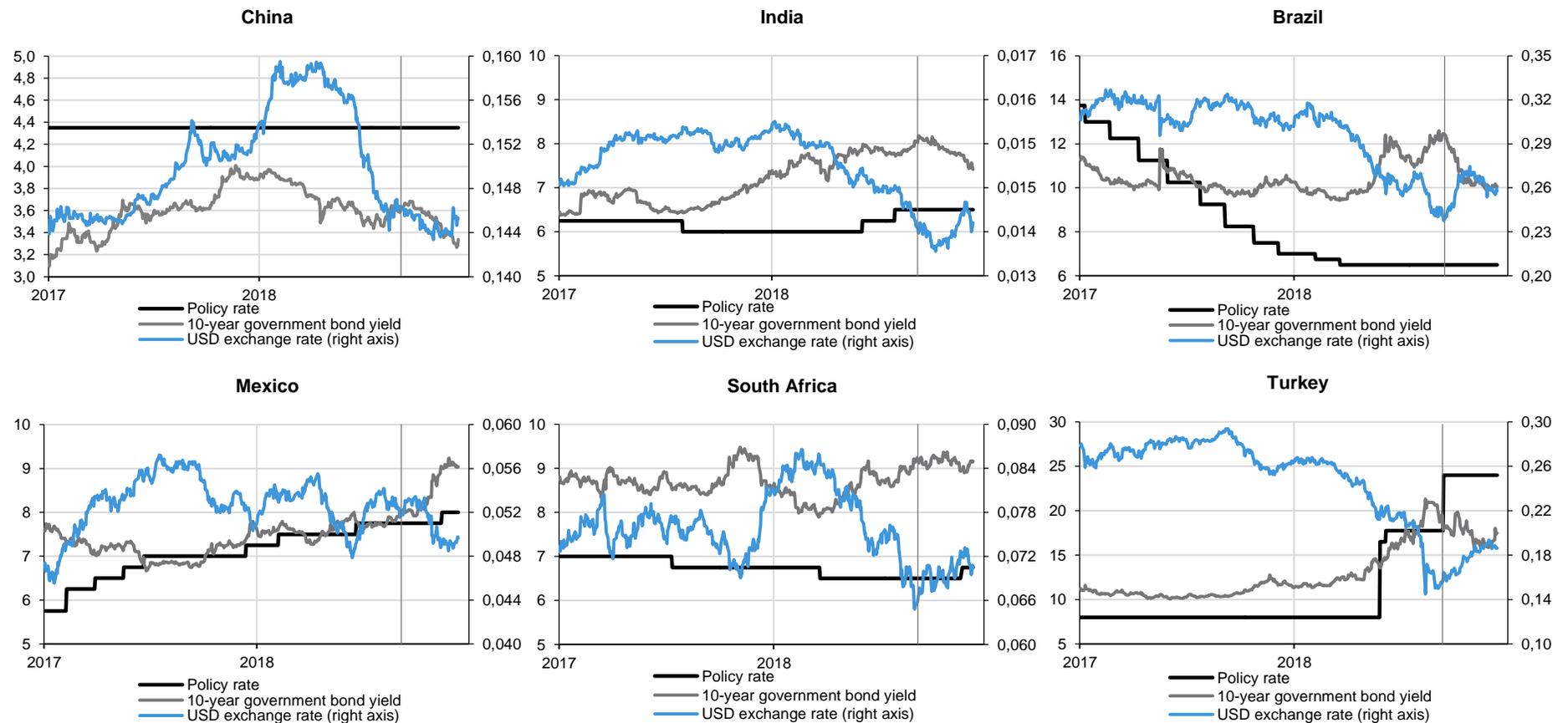
Moderation in US Treasuries yields, downtrend in stocks, firmer US dollar



Source: Reuters



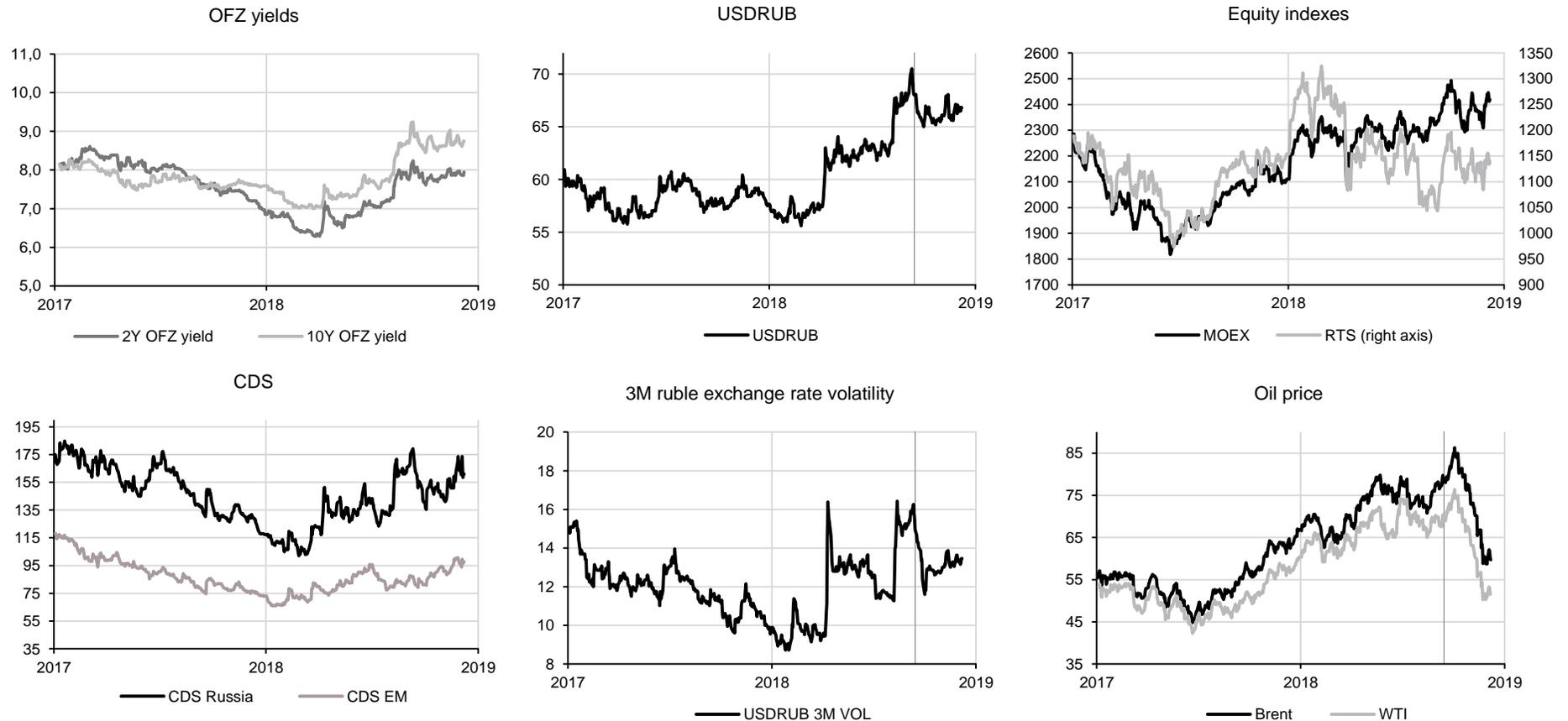
## Financial markets – selected EM countries



Sources: Bloomberg, Reuters



## Financial markets – Russia and Oil



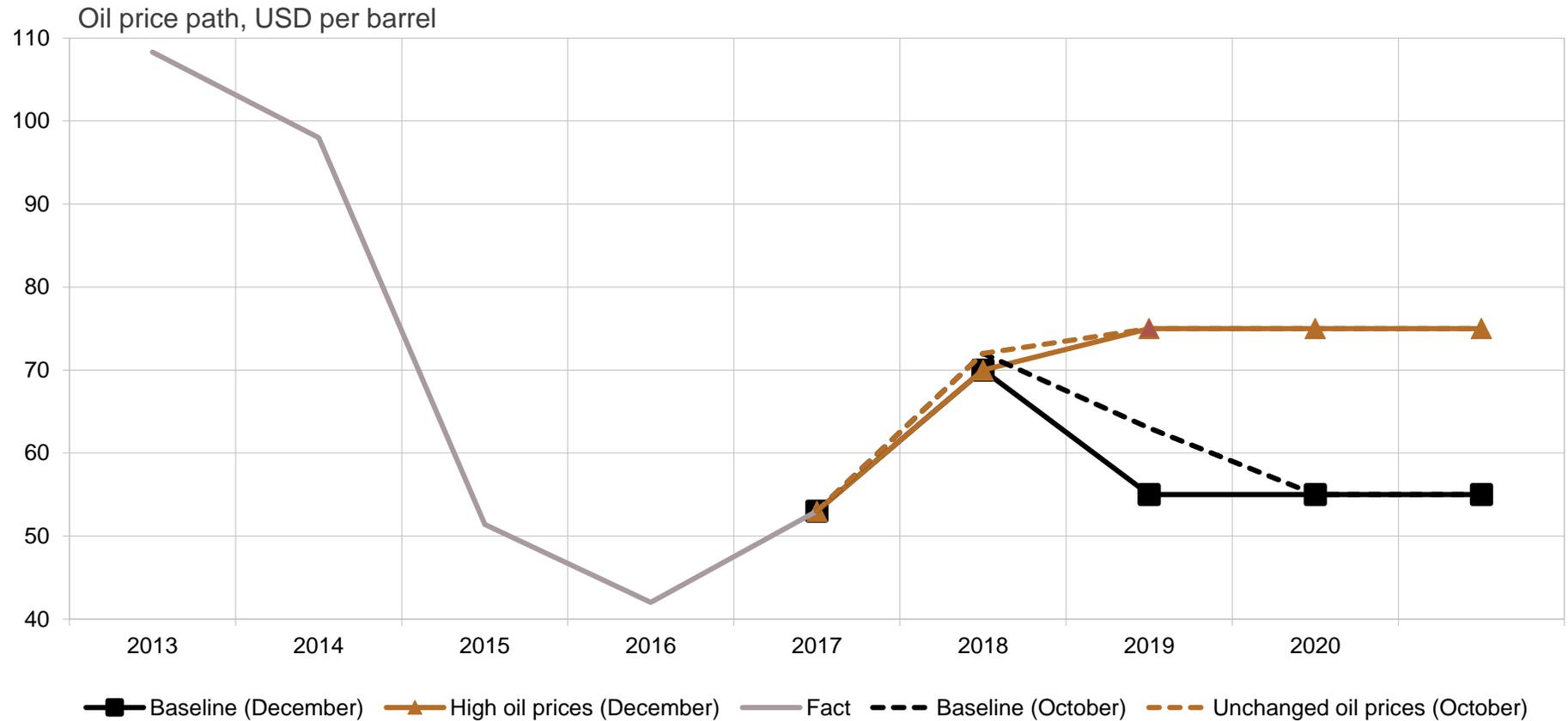
Sources: Reuters, Bloomberg, Bank of Russia

- 14.09.18 Bank of Russia's Board meeting



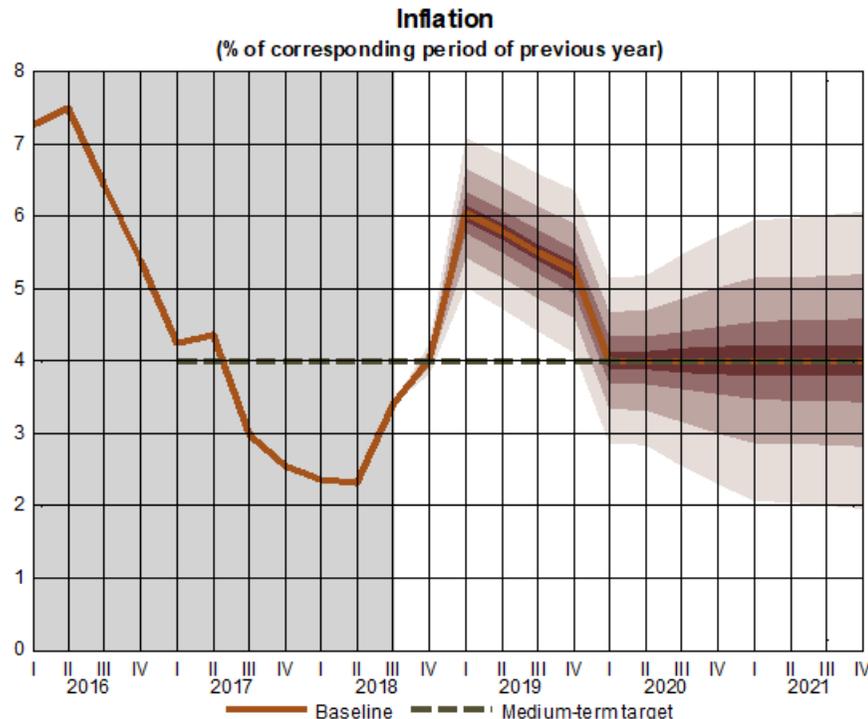
## Oil price assumptions

Baseline trajectory assumes faster convergence to the longer-term steadystate; now at \$55/bbl for Urals in 2019 and onwards (October forecast: 63-55-55)



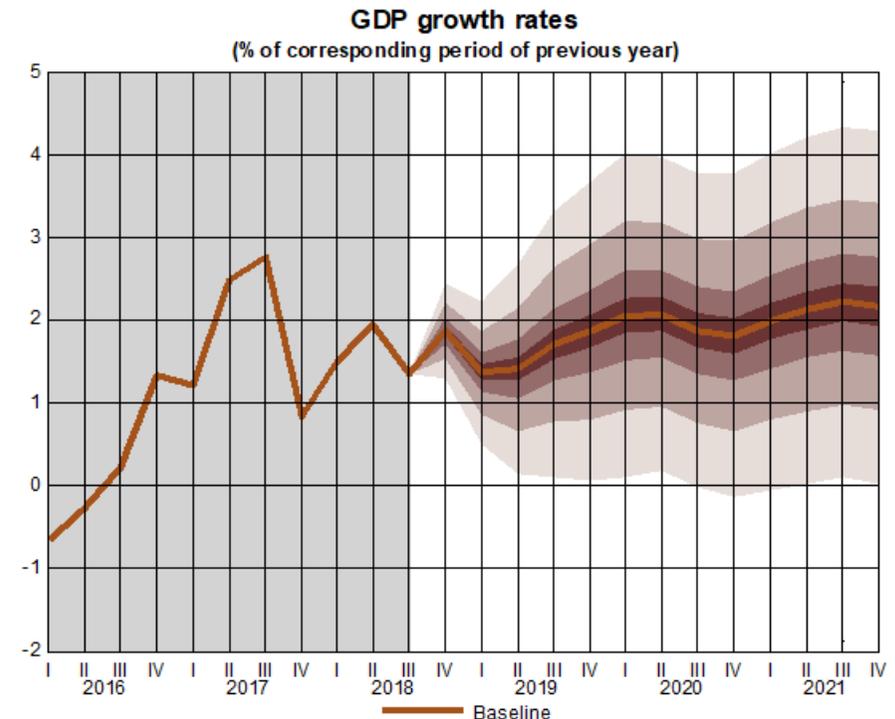
## Bank of Russia's baseline scenario (Dec 2018)

**Annual inflation will slow down to 4% in the first half of 2020 when the effects of the ruble's weakening and the VAT rise peter out**



Note: shaded areas on the forecast horizon show the probability of different inflation values.  
Colour gradation reflects probability  
Source: Bank of Russia calculations.

**Higher potential growth rates in 2020-2021 if the planned fiscal and structural measures are successfully implemented**



Note: shaded areas on the forecast horizon show the probability of different inflation values.  
Colour gradation reflects probability  
Source: Bank of Russia calculations.



## Bank of Russia's baseline scenario (Dec 2018) – details

<i>Increase compared to the previous period in % (unless noted otherwise)</i>	2017 (fact/ estimate)	2018	2019	2020	2021
		Baseline*			
Urals price (average for year), USD per barrel	53	70	55	55	55
Inflation in December compared to previous December, %	2.5	3.9-4.2	5.0-5.5	4.0	4.0
Inflation (average for year) compared to the previous year, %	3.5	2.8-2.9	5.0-5.5	4.0	4.0
GDP**	1.8	1.5-2.0	1.2-1.7	1.8-2.3	2.0-3.0
Final consumption expenditures	2.5	2.0-2.5	1.0-1.5	1.5-2.0	2.0-2.5
- of households	3.3	2.5-3.0	1.0-1.5	1.5-2.0	2.5-3.0
Gross capital formation	9.3	(-1.5-0.5)	1.5-2.5	2.5-3.5	3.5-4.5
- gross fixed capital formation	4.9	1.5-2.0	1.8-2.3	3.0-3.5	3.5-4.5
Exports	6.0	5.5-6.0	3.2-3.7	2.7-3.2	2.7-3.2
Imports	17.4	4.0-4.5	2.5-3.0	3.5-4.0	4.5-5.0
Money supply (using the national definition)	10.5	11-14	7-11	7-12	7-12
Lending to non-financial organisations and households, in roubles and foreign currencies***	8.2	12-14	7-11	7-12	7-12
- Lending to non-financial and financial organisations, in rubles and foreign currencies	7.1	9-11	7-10	6-10	6-10
- Lending to households, in rubles and foreign currencies	12	21-24	12-17	10-15	10-15

\* Published in Monetary policy report №4 (December 2018)

\*\* 2017 data – Bank of Russia estimate with Rosstat-revised industrial production data factored in

\*\*\* Banking sector's lending to the economy is defined as all the claims of the banking sector to financial and non-financial organisations as well as households in Russian or foreign currency and precious metals, including loans provided (with overdue debt counting as well), overdue interest on loans, credit institutions' investment in equity and debt securities and promissory notes, any forms of participating in the equity of financial and non-financial organisations, and any other receivables for settlements with financial and non-financial organisations and households



## Bank of Russia's baseline scenario (Dec 2018) – balance of payments

<i>USD billions</i>	2017 (estimate)	Baseline*			
		2018	2019	2020	2021
<b>Current account</b>	<b>33</b>	<b>112</b>	<b>71</b>	<b>55</b>	<b>48</b>
Trade balance	115	191	154	143	139
<i>Export</i>	354	441	400	405	416
<i>Import</i>	-238	-250	-246	-262	-277
Balance of services	-31	-31	-33	-34	-36
<i>Export</i>	58	65	61	62	64
<i>Import</i>	-89	-96	-94	-97	-100
Balance of primary and secondary income	-51	-49	-51	-53	-55
Capital account	0	0	0	0	0
<b>Financial transactions account (reserve assets excluded)</b>	<b>-14</b>	<b>-72</b>	<b>-19</b>	<b>-11</b>	<b>-8</b>
<i>Public administration and central banks</i>	13	-5	1	2	3
<i>Private sector</i>	-28	-67	-20	-13	-11
<b>Net errors and omissions</b>	<b>4</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Change in FX reserves (+ is for decrease, - is for growth)</b>	<b>-23</b>	<b>-39</b>	<b>-52</b>	<b>-44</b>	<b>-40</b>

\* Using BPM 5 methodology. Due to rounding total results may differ from the sum of respective values

Published in Monetary policy report №4 (December 2018)



## Bank of Russian FX operations related to the fiscal rule

The Bank of Russia decided to **resume regular foreign currency purchases** in the domestic market as part of the fiscal rule implementation **from 15 January 2019**

The decision was made given the **stabilisation** in the domestic financial market

The decision on the foreign currency purchases in the domestic market that were **postponed in 2018** will be taken **after regular purchases resume**

The postponed purchases may be carried out **gradually** in 2019 and in subsequent years



## Monetary policy decision, 14 December 2018

### Inflation and inflation expectations

- Prices continue to adjust to the ruble weakening since the beginning of the year
- Consumer price growth starts to react to the the VAT increase pending on 1 January 2019
- Uncertainty persists over the subsequent movements of inflation expectations
- At the end of 2018, inflation is expected to be close to 4%, which corresponds to the Bank of Russia's target. 2019 forecast – 5,0-5,5% (unchanged)
- The forecast takes into account the BoR's decision to resume regular foreign currency purchases
- Annual inflation will slow down to 4% in the first half of 2020 when the effects of the ruble's weakening and the VAT rise are out of the calculation window

**Monetary conditions:** some further tightening still ongoing

### Economic activity

- Russian economic growth slowed somewhat, but remains close to potential
- The Bank of Russia's outlook for the mid-term growth prospects remains unchanged
- In 2019, the forthcoming VAT increase might have a slight constraining effect on business activity (mostly in the beginning of the year)
- The following years might see higher growth rates as the planned structural measures are implemented

**Pro-inflationary risks remain elevated, especially over a short-term horizon**  
→ The decision taken is proactive in nature

- **The main risks:** (1) continuing uncertainty over future external conditions and their impact on financial asset prices, (2) increased risks of supply exceeding demand in the oil market in 2019, (3) secondary effects from the VAT-induced inflation spike in 1Q19
- **Moderate risks** – estimates are mostly unchanged: (4) wage movements, (5) possible changes in consumer behavior, (5) budget expenditures

### Decision

The Bank of Russia  
**raises the key rate**  
by 25 bps to 7.75% p.a.

### Signal

*“...The Bank of Russia will consider the necessity of further increases in the key rate, taking into account inflation and economic dynamics against the forecast, as well as risks posed by external conditions and the reaction of financial markets...”*

## Money market conditions

In the light of the persistent structural surplus RUONIA remains moderately below the key rate; in 4Q the spread so far averaged -21bp, same as in 3Q, and the least deviation from the key rate since 2Q17

