



Bank of Russia



INFLATION EXPECTATIONS AND CONSUMER SENTIMENT

No.7 (31) • July 2019

Information and analytical commentary

30 July 2019

Inflation expectations and consumer sentiment (July 2019)

July 2019 saw a continued decrease in inflation observed by the public. Businesses' price expectations for the months to come also declined, due to weak demand and appreciation of the ruble. The downward trend in long-term inflation expectations of financial market participants, which had reached 3.7-3.8%, persisted. However, the median estimate of inflation expected by households in the next 12 months remained unchanged and stayed elevated, while the estimate of their expectations calculated by the Bank of Russia increased. Analysts' predictions remain virtually unchanged and suggest that annual inflation will continue declining, to reach 4.3-4.5% as of year-end and stabilise near 4% in 2020 Q1. According to the Bank of Russia's forecast, taking into account the pursued monetary policy, annual inflation will return to 4% in early 2020.

INFLATION EXPECTATION INDICATORS

Table 1

	Expectation horizon	July 2017	July 2018	May 2019	June 2019	July 2019
Inflation, %		3.9	2.5	5.1	4.7	
Households' inflation expectations, %						
Public Opinion Foundation (median, expected inflation)	next 12 months	10.7	9.7	9.3	9.4	9.4
Public Opinion Foundation (median, observed inflation)	past 12 months	11.9	10.3	10.4	10.2	9.9
Public Opinion Foundation (subgroup with savings)	next 12 months	9.8	8.5	8.6	8.3	8.6
Public Opinion Foundation (subgroup without savings)	next 12 months	11.4	10.2	9.9	10.0	9.7
Public Opinion Foundation (Bank of Russia calculations)	next 12 months	4.1	2.8	5.5	4.9	5.3
Professional analysts, %						
Bloomberg	2019 Q4		4.2	4.5	4.5	4.3
Interfax	December 2019		4.3	4.5	4.3	
Reuters	December 2019		4.3	4.6	4.3	
Implied inflation for OFZ-IN, %						
OFZ-IN 52001, August 2023	next 4-year average	4.8	4.6	4.2	3.9	3.7
OFZ-IN 52002, February 2028	next 9-year average		4.6	4.3	3.9	3.8
Qualitative estimates of inflation expectations						
Businesses, balance of responses	next 3 months	9.1	10.9	9.6	10.2	9.0
PMI input prices, diffusion index	current month	56.4	60.8	57.1	55.9	
PMI output prices, diffusion index	current month	52.1	54.1	52.8	52.2	

Household inflation expectations

According to a Bank of Russia-commissioned inFOM survey, the median estimate of annual inflation observed by households in July 2019 with respect to the past 12 months continued to decrease to 9.9% from 10.2% a month earlier (Table 1, Chart 1), reflecting the actual inflation dynamics registered by Rosstat. Nevertheless, the median estimate of inflation expected in the next 12 months remained unchanged compared to the previous month at 9.4% (Chart 1). It remains virtually unchanged for the fourth

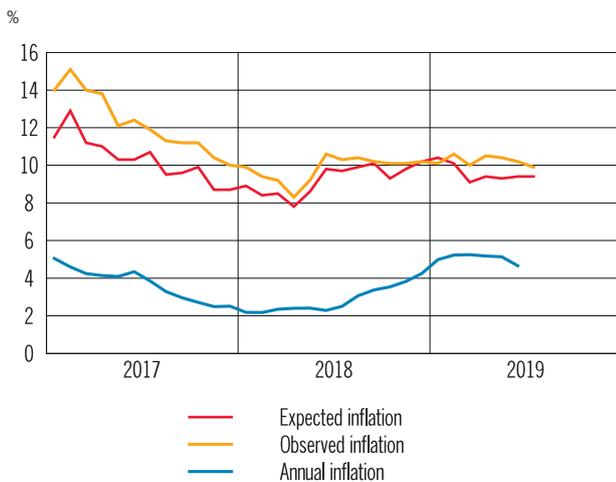
month in a row following a decline in March 2019 (its level is higher than in 2018 H1). Meanwhile, the inflation expectations of respondents who have savings went up by 0.3 pp, returning to the middle of the range where they have been located since last May (Chart 2).¹ However, the inflation expectations of respondents who have no savings went down by 0.3 pp and stay close to the minimum values observed since last May.

In July, the rise in the prices of fruit and vegetables was less frequently perceived as

¹ *Monetary Policy Report No. 2 (26), June 2019, box 'Survey microdata-based assessment of the relationship between inflation expectations and household saving behaviour'.*

INFLATION OBSERVED AND EXPECTED BY HOUSEHOLDS (MEDIAN ESTIMATE)

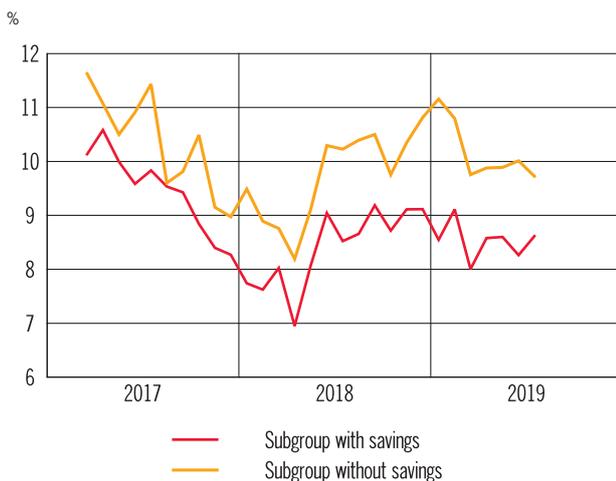
Chart 1



Sources: InFOM, Rosstat.

INFLATION EXPECTATIONS BY SUBGROUP OF RESPONDENTS (MEDIAN ESTIMATE)

Chart 2



Sources: inFOM, Bank of Russia calculations.

FACTORS BEHIND HOUSEHOLD INFLATION EXPECTATIONS (% OF RESPONDENTS)

Table 2

	April 2019	May 2019	June 2019	July 2019
Current change in petrol prices	48	47	52	50
Ruble exchange rate fluctuations	39	41	40	38
Current change in food prices	36	35	35	37
Wage and pension indexation	31	32	32	31

Source: InFOM.

considerable (Chart 3 of the inFOM Analytical Report on the Seventh Survey in 2019, further referred to as the 'Report'), which is probably caused by seasonal price dynamics. Utility services were mentioned somewhat more frequently due to the planned indexation of utility rates in July. The frequency of mentions of other goods and services changed insignificantly.

Household estimates for current and expected inflation depend to a large extent on changes in petrol prices (Table 2). Their significant growth was registered by 27% of respondents, practically the same percentage as in June (28%). This is explained by moderate actual price dynamics and indicates that petrol price movements did not affect inflation expectations, as was noted in the June commentary.²

Estimates of household inflation expectations for the next 12 months, calculated by the Bank of Russia with the use of inFOM survey data, increased in July, against a backdrop of the growing frequency of answers about inflation acceleration in the next 12 months (Chart 5 of the Report). In July, the shares of respondents who expect 2019 and 3-year inflation to be near 4% remained virtually unchanged (30% and 23% respectively, Charts 8 and 9 of the Report). The low shares of such respondents indicate that inflation expectations are not anchored to the Bank of Russia's targets.

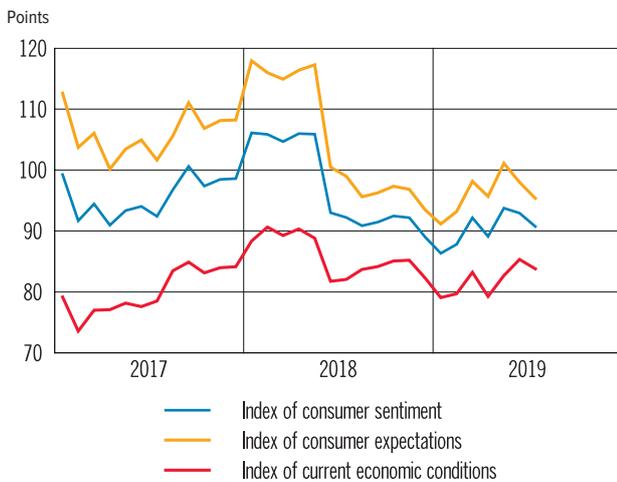
Household consumer sentiment

In July, the consumer sentiment index continued to go down for the second month in a row (by 2 pp to 91 points, Chart 3). The decline was observed in both the index of consumer expectations and the index of current economic conditions (Chart 11 of the Report). Among the components of the index, respondents' assessments of the prospects for this country's development deteriorated the most (Chart 12 of the Report).

² See 'Inflation Expectations and Consumer Sentiment', No. 6 (30), June 2019.

INDEX OF CONSUMER SENTIMENT

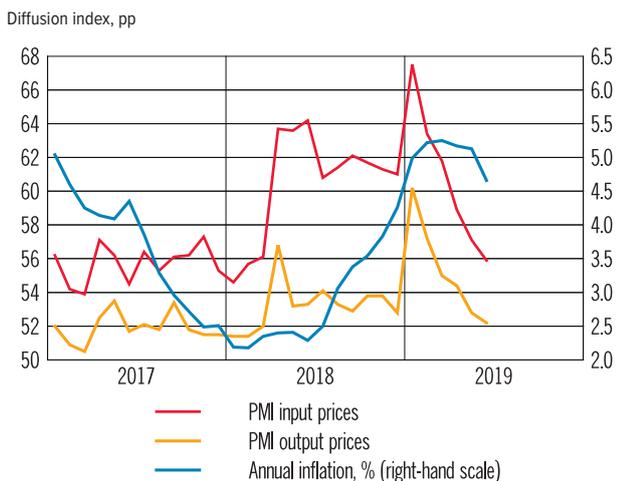
Chart 3



Source: InFOM.

CHANGES IN COMPANIES' PRICES (MARKIT PMI)

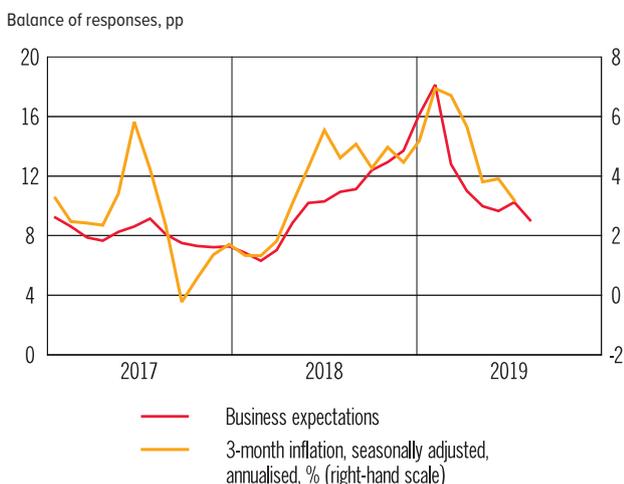
Chart 4



Sources: IHS Markit PMI, Rosstat.

BUSINESS PRICE EXPECTATIONS (BANK OF RUSSIA)

Chart 5



Sources: Bank of Russia, Rosstat.

In July, respondents were asked about their behaviour in situations when they are short of money (Chart 27 of the Report). Over the past year, 58% of the respondents faced such situations. Over half of those (32%) borrowed funds, and 9% borrowed from banks or microfinance organisations. Considering respondents' answers about the number of consumer loans taken out over the past year, nearly half of instances of borrowing were caused by financial troubles.

Business price expectations

According to Markit PMI surveys,³ the diffusion index of input and output prices of businesses continued to decline in June 2019 (Chart 4). Both indices came within touching distance of the values of early 2018. According to businesses, the main factor behind the ongoing slowing of growth in output prices was weak demand restricting their abilities to raise prices. Meanwhile, the situation in the food and fuel markets was called proinflationary.

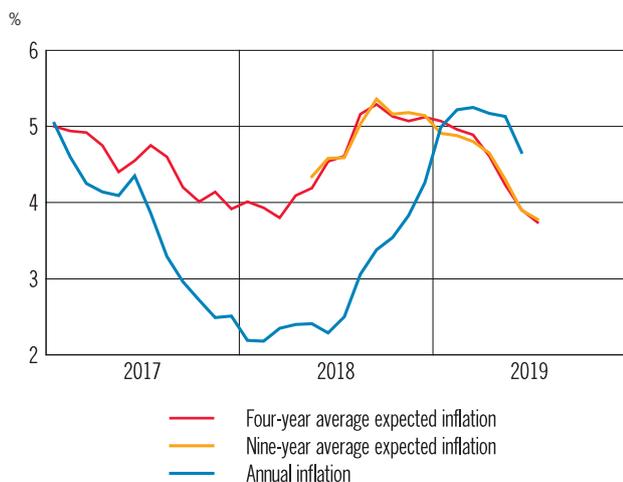
According to a Bank of Russia survey,⁴ businesses' price expectations for the three months ahead dropped in July 2019 following a rise in June caused primarily by one-off factors (Chart 5). The decrease in expectations affected all types of activity except for the mining and quarrying sector, where enterprises pointed out global expansion of metallic ore prices and the extension of the OPEC+ deal. The construction sector registered the maximum decline in expectations, which was related to an adjustment following the previous month's increase due to the introduction of escrow accounts. The ruble's appreciation was also a main factor in the decline of price expectations. The first half of 2019 saw an improved assessment of the foreign exchange rate's impact on business activity: considerable improvements were registered in wholesale and retail trade.

³ See <https://www.markiteconomics.com/public>.

⁴ For survey details, refer to https://www.cbr.ru/Content/Document/File/62829/analysis_18-12.pdf.

IMPLIED INFLATION
FOR OFZ-IN

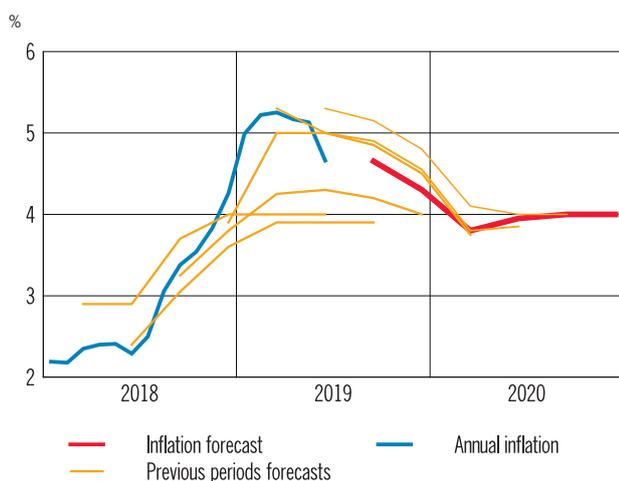
Chart 6



Sources: Bloomberg, Rosstat, Bank of Russia calculations.

BLOOMBERG ANALYSTS' CONSENSUS
FORECAST

Chart 7



Sources: Bloomberg, Rosstat.

Implied inflation for OFZ-IN

In July, four- and nine-year implied inflation priced in OFZ-IN, according to the Bank of Russia's estimates,⁵ stood at 3.7% and 3.8% respectively (compared to 4.9-5.1% in January and 3.9% in June, Chart 6). This is the minimum level over the entire history of observations. Such a decline is probably a response to the slowdown in monthly inflation. The current level of implied inflation is close to 4% and indicates stronger anchoring of the inflation expectations of financial market participants to the Bank of Russia's targets.

Analysts' inflation expectations

The range of analysts' inflation forecasts for December 2019⁶ has remained virtually unchanged since January, holding at 4.3-4.5% (Table 1). According to their forecasts, annual consumer price growth will continue decreasing to stabilise near 4% in 2020 Q1 (Chart 7).

Bank of Russia forecast

According to the Bank of Russia's forecast, taking into account the pursued monetary policy, annual inflation will return to 4% in early 2020.

⁵ The estimates are based on a comparison of the expected yields on inflation-indexed federal government bonds (OFZ-IN) and nominal OFZs.

⁶ Surveys by Interfax, Bloomberg, and Thomson Reuters.

Data cut-off date – 25 July 2019.

A soft copy of the information and analytical commentary is available on the Bank of Russia website (<http://www.cbr.ru/DKP/>).

Please send your comments and suggestions to svc_analysis@cbr.ru.

This commentary is prepared by the Monetary Policy Department.

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