Bank of Russia

No. 4

OCTOBER 2020

MONETARY POLICY REPORT

2 November 2020

The report has been prepared based on statistics as of 22 October 2020.
The data cut-off date for forecast calculations is 15 October 2020 (if statistics or other information relevant for decision-making come in after the data cut-off date, they are included in the text of the Report and may be used to adjust the mid-term forecast).

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This publication has been prepared by the Monetary Policy Department.

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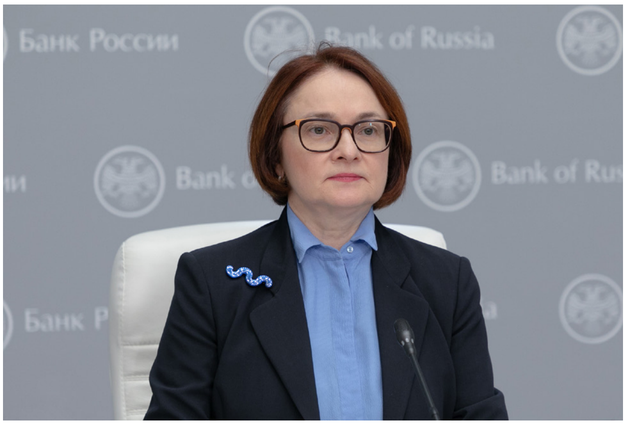
STATEMENT BY BANK OF RUSSIA GOVERNOR ELVIRA NABIULLINA

IN FOLLOW-UP TO BOARD OF DIRECTORS MEETING ON 23 OCTOBER 2020



Today, we have made the decision to keep the key rate at 4.25%.

The economy continues to recover, albeit at a slower pace than in summer. Financial markets are still characterised by elevated volatility, and geopolitical risks persist. Moreover, the epidemiological situation is deteriorating, which may increase demand-side disinflationary pressure.

I would like to dwell on the factors we considered today.

Firstly, inflation processes are generally evolving in line with our baseline scenario. *We forecast that inflation will come in at 3.9–4.2% by the end of the year.*

Stable inflation indicators are close to 4%. However, demand- and supply-side factors are changing unevenly, having different impacts on prices in individual goods and service groups. The effect of pent-up demand on inflation has been mostly exhausted. The weakening of the ruble continues to affect the price growth rate. This is evident in non-food categories in the first place.

There is also a range of one-off factors temporarily slowing down the rise in service prices. Specifically, given the current epidemiological situation, the authorities have recommended to limit the increase in prices for educational services. A number of regions have made decisions on only partial indexation of housing and utility rates. Further on, these prices may adjust over time, and we take this into account in our inflation forecast.

Secondly, inflation expectations have increased. *To a certain extent, they are responding to exchange rate fluctuations. Businesses are also reporting a rise in costs.*

Thirdly, the economic recovery has slowed down, predominantly due to domestic demand trends. *This is evident from investment and consumption trends, as well as the leading indicators of consumer and business activity. As noted above, the positive effect of pent-up demand has been mostly exhausted by now. This demand was driving the fast revival* *of economic activity immediately after the cancellation of the restrictions imposed in spring and summer. This recovery was primarily recorded in sectors focused on consumer goods production. The revival in intermediate goods industries was less pronounced. However, the deteriorating epidemiological situation is hampering the growth of consumption expenditures, affecting companies' investment plans.*

It is still highly uncertain how fast the global economy will be recovering, especially with account of repeated restrictions being imposed in a number of countries. The economic environment is also being affected by geopolitical factors, including trade tensions, the Brexit situation, and the upcoming elections in the USA. The decline in sentiment is increasing volatility in global markets. In such conditions, external demand may hardly be expected to support the economy.

The fourth factor is monetary conditions. *We can see that the earlier decisions on the key rate continue to translate into the easing of monetary conditions and banks' pricing policies. Along with the decrease in interest rates, non-price lending conditions are also easing.*

In addition, we also factor in that the preferential corporate and retail lending programmes are becoming increasingly important. In August, the portion of subsidised mortgage loans exceeded 35% in the overall amount of loans disbursed. The total monthly amount of issued mortgage loans hit its record high. As regards lending to small and medium-sized enterprises, the percentage of short-term loans issued at interest rates that are close to 2% per annum rose in August from one-fourth to one-third of their overall amount. These programmes are also indirectly influencing the general pricing environment in the credit market. In the future, we will be estimating how monetary conditions are adjusting as these programmes terminate.

Now, I will proceed to the forecast. Today, as always after the core meeting, we have published our updated baseline scenario. *When revising our forecast, we considered a range of factors. The ruble has weakened. The period of the recovery growth, that is, the initial rebound after the lifting of the spring restrictions, has almost ended. The epidemiological situation is deteriorating, which is already affecting economic activity. Nonetheless, export dynamics have turned out to be better than expected, for both oil and gas exports and the exports of other goods, especially gold.*

Taking into account the overall impact of competing factors, the GDP forecast has been revised upwards. According to estimates, GDP will go down by 4–5% as of the end of 2020, which is better than it was expected in July.

As to domestic demand indicators, their overall dynamics as of the end of 2020 ar e expected to be worse than forecast in July. This is associated with the released data on GDP components for the second quarter. The restrictions that were in place over this period had a stronger negative impact on both investment and consumption than it had been assumed. However, the recovery in the third quarter was also faster than forecast. Furthermore, as you know, GDP results for the second quarter were generally better that our preliminary estimates. This was associated with higher exports indicators over this period, compared to our expectations.

Amid the deterioration of the pandemic situation in the fourth quarter and possibly at the beginning of 2021, economic revival will be somewhat slower than we forecast earlier. Therefore, GDP growth in 2021 has been revised downwards by one-half of a percentage point, to 3–4%. Making this adjustment, we took into account the effect of the higher base of 2020, given that the 2020 GDP forecast has been improved.

Now a few words about the 2022–2023 horizon. At the moment, our forecast assumptions and parameters have remained unchanged. The economy will expand by 2.5–3.5% in 2022 and by 2–3% in 2023. We still expect that we will return to the pre-crisis level in the first half of 2022.

Given the current monetary policy stance, inflation is forecast to stand at 3.5–4.0% in 2021 and further remain close to 4%.

Regarding the balance of payments forecast, it has been significantly updated, primarily due to the upward adjustment of export estimates. The current account is expected to be notably higher over the entire forecast horizon. This is related to both the adjusted volume and the expected price environment for Russian export products. We have updated the 2021 average oil price assumption from $40 to $45 per barrel taking into account the current price movements and assuming that the situation in the oil market will remain stable.

Regarding the fiscal policy, we build our baseline forecast on the figures specified in the draft Fiscal Policy Guidelines for 2021–2023. However, when making our key rate decisions, we will consider potential adjustments in the measures implemented by the Government.

Another factor that we take into account is the specifics of the operation of the transmission mechanism in the current conditions. *Increased financial market volatility requires that we consider financial stability aspects in our key rate decisions. In a normal situation, cutting the key rate should prompt a decline in interest rates on all financial instruments and a certain weakening of the ruble, which altogether would lead to an easing of monetary conditions. However, in an unstable situation in financial markets with elevated risks, a key rate cut could lead to an increase in interest rates on long-term financial instruments and a more pronounced reaction of the exchange rate than in steady conditions. As a result, monetary conditions could even tighten. Therefore, we should carefully use our room for monetary policy easing given potential financial stability risks.*

In conclusion, I would like to speak about our further steps. *As I have already said, the worsening of the pandemic situation will have mainly disinflationary effects. A potential slowdown in the global economy will have similar consequences. At the same time, short-term proinflationary risks stemming from the situation in financial markets have strengthened recently. The upward pressure on prices can also be exerted if the epidemiological situation causes a notable influence on both demand for and supply of goods and services. Although the ratio of proinflationary and disinflationary factors may change over the short-term horizon, we believe that disinflationary risks prevail in the medium term. Therefore, we still see room for a key rate decrease.*

A more significant influence of disinflationary factors may require more prolonged and, potentially, more pronounced accommodative monetary policy than it is currently stipulated in our baseline scenario.

However, we also take into account that it is important to ensure that our monetary policy is stable under any scenarios in order to maintain inflation close to 4%. This is especially important today when so many diverse factors are influencing the current situation.

Bank of Russia Governor ***Elvira Nabiullina***

1. CURRENT SITUATION AND THE BANK OF RUSSIA'S FORECAST

The Bank of Russia updated its baseline forecast regarding GDP changes in 2020–2021, as compared to its MPR 3/20, with account of two key factors.

Firstly, according to the revised assessment by Rossat, the annual decline in GDP in 2020 Q2 was slower, and the recovery pace of both Russia's economy and the global economy turned out to be higher in July–August than expected earlier. Rising global demand and the conservative approach to expanding oil production, despite the easing of the OPEC+ restrictions, contributed to the increase in prices for commodities, including oil, compared to the levels assumed in the Bank of Russia's forecast presented in MPR 3/20. Russia's economy was recovering predominantly owing to industries focused on domestic consumption. This economic revival was supported by the easing of monetary conditions and fiscal policy measures. As a result, the estimate of GDP growth in 2020 Q3 was revised upwards.

Secondly, due to the worsening epidemiological situation, the recovery of the Russian economy discontinued in September. Beginning from August, the stimulating effect of the fiscal measures started to diminish. Accordingly, the estimate of GDP growth in 2020 Q4 was adjusted downwards.

According to the updated baseline scenario, GDP is expected to decrease by 4.0–5.0% by the end of 2020, which is slightly better than assumed in MPR 3/20 (4.5–5.5%). Nonetheless, the 2021 forecast was revised downwards to 3.0–4.0% (against 3.5–4.5% in MPR 3/20), which is because the recovery slowed down after the higher levels of 2020 compared to those expected earlier. The GDP growth forecast for 2022 remained unchanged versus MPR 3/20.

Until the end of 2020, weak consumer demand will remain the main drag on price growth. Amid the currently pursued monetary policy, inflation will reach 3.9–4.2% in 2020, which is in line with the baseline range specified in MPR 3/20 (3.7–4.2%). Inflation forecast for the next years was not changed: 3.5–4.0% in 2021 and close to 4.0% thereafter.

BANK OF RUSSIA'S MEDIUM-TERM FORECAST[1]

IN THE FOLLOW-UP TO THE BOARD OF DIRECTORS KEY RATE MEETING ON 23 OCTOBER 2020

KEY FORECAST PARAMETERS OF THE BANK OF RUSSIA'S BASELINE SCENARIO *Table 1*
(growth as % of previous year, if not indicated otherwise)

	2019 (actual)	Baseline			
		2020	2021	2022	2023
Inflation, as % in December year-on-year	3.0	3.9–4.2	3.5–4.0	4.0	4.0
Inflation, average for the year, as % year-on-year	4.5	3.2–3.3	3.3–4.0	4.0	4.0
Gross domestic product	1.3	-(4.0–5.0)	3.0–4.0	2.5–3.5	2.0–3.0
Final consumption expenditure	2.4	-(6.2–7.2)	4.2–5.2	3.0–4.0	2.1–3.1
– *households*	*2.5*	*-(9.5–10.5)*	*5.3–6.3*	*3.7–4.7*	*2.5–3.5*
Gross capital formation	3.8	-(7.8–10.8)	3.1–5.1	4.2–6.2	3.0–5.0
– *gross fixed capital formation*	*1.5*	*-(7.8–9.8)*	*3.3–5.3*	*4.5–6.5*	*3.2–5.2*
Exports	-2.3	-(5.1–7.1)	(-0.8) – 1.2	3.6–5.6	2.0–4.0
Imports	3.4	-(18.0–21.0)	3.9–5.9	8.4–10.4	4.9–6.9
Money supply in national definition	9.7	14–17	8–12	7–11	7–11
Claims on organisations and households in rubles and foreign currency*	10.1	9–12	7–11	7–11	7–11
– *on organizations*	*7.1*	*8–11*	*6–10*	*6–10*	*6–10*
– *on households*	*19*	*13–16*	*12–16*	*10–14*	*10–14*

** Banking sector claims on organisations and households means all of the banking sector's claims on non-financial and financial institutions and households in rubles, foreign currency and precious metals, including loans issued (including overdue loans), overdue interest on loans, credit institutions' investment in debt and equity securities and promissory notes, as well as other forms of equity interest in non-financial and financial institutions, and other accounts receivable from settlement operations involving non-financial and financial institutions and households.*
Claims' growth rates are given with the exclusion of foreign currency revaluation. In order to exclude the effect of foreign currency revaluation the growth of claims in foreign currency and precious metals is converted to rubles using the period average USDRUB exchange rate.
Source: Bank of Russia.

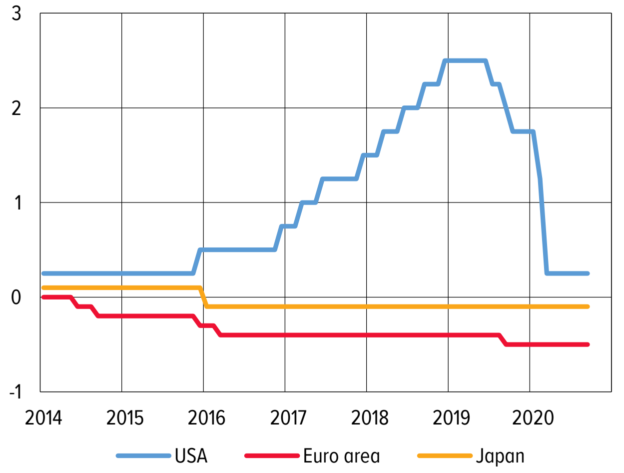
RUSSIA'S BALANCE OF PAYMENTS INDICATORS IN THE BASELINE SCENARIO* *Table 2*
(billions of US dollars)

	2019 (actual)	Baseline			
		2020	2021	2022	2023
Current account	**65**	**33**	**32**	**18**	**30**
Balance of trade	165	88	99	100	126
Exports	*420*	*316*	*331*	*353*	*400*
Imports	*255*	*228*	*232*	*253*	*274*
Balance of services	-36	-14	-24	-38	-51
Exports	*63*	*44*	*48*	*52*	*57*
Imports	*99*	*59*	*71*	*90*	*109*
Balance of primary and secondary income	-64	-41	-43	-44	-45
Current and capital account balance	**65**	**33**	**32**	**18**	**30**
Financial account (excluding reserve assets)	**-4**	**49**	**30**	**17**	**11**
Government and the central bank	-23	-4	-5	-4	-4
Private sector	19	53	35	20	15
Net errors and omissions	**-2**	**0**	**0**	**0**	**0**
Change in reserve assets ('+' is increase, '-' is decrease)	**66**	**-16**	**2**	**1**	**19**
Urals price, average for the year, US dollars per barrel	**64**	**41**	**45**	**45**	**50**

** Using the methodology of the 6th edition of "Balance of Payments and International Investment Position Manual" (BPM6). In the Financial account "+" stands for net lending, "-" – for net borrowing. Due to rounding total results may differ from the sum of respective values.*
Source: Bank of Russia.

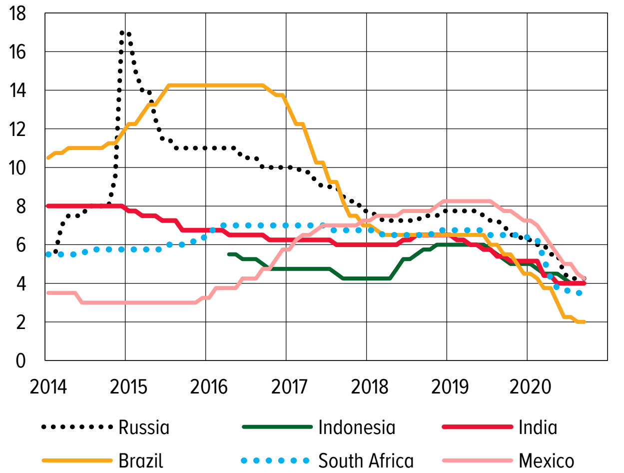
[1] *The Bank of Russia's forecast under the supplementary scenarios (high oil prices and risk) were published in the Monetary Policy Guidelines for 2020-2022 on 25.10.2019.*

POLICY RATES: ADVANCED ECONOMIES (%) *Chart 1.1.1*



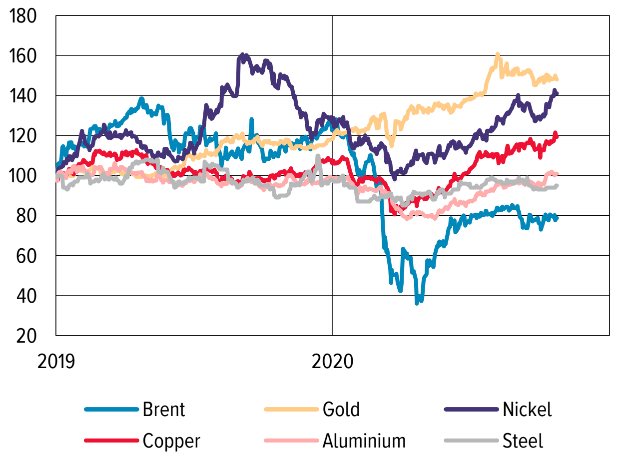
Source: Bloomberg.

POLICY RATES: EMES (%) *Chart 1.1.2*



Source: Bloomberg.

GLOBAL PRICES FOR KEY RUSSIAN EXPORT COMMODITIES (01.01.2019 = 100%) *Chart 1.1.3*



Source: Bloomberg.

1.1. CURRENT SITUATION

In July–August, the global economy continued to bounce back. Although uneven, this recovery inspired most major economies **to revise upwards their GDP growth estimates for 2020 Q3 and 2020 in general**.

Since demand increased, including in the services sector, inflation slightly rose in both advanced and emerging market economies. In these conditions, major central banks predominantly kept their policy rates unchanged, presuming that real rates might temporarily shift to negative territory.

As the economic activity restrictions were eased gradually in summer, investors' sentiment improved and financial markets recorded growth. Upward trends also prevailed in commodity markets. The revival of global demand supported prices for core Russian exports. As a result of the easing of the OPEC+ cuts in August, oil output expanded less than expected,[1] which supported oil prices and, coupled with reviving global demand, also contributed to their moderate growth.

Country risk premia for the majority of EMEs decreased in July–August, and their currencies strengthened against the US dollar. In September, the epidemiological situation worsened in a significant number of countries, including Europe. Rising concerns about the reintroduction of quarantine measures reversed trends in both commodity and financial markets.

Amid concerns over global demand weakening, the Urals crude price dropped by 8% on average in September–October against its average level in July–August.[2] Restoring production in Libya also put downward pressure on oil prices. Nonetheless, as a result of the actual growth in July–August, **the oil price exceeded the overall Q3 level assumed in the Bank of Russia's July forecast, following which the average annual estimate for 2020 was revised upwards from USD38 to USD41 per barrel**.

[1] *According to the agreement, the OPEC+ production cuts eased in August by 2 million bpd from the basic level, to 7.7 million bpd, including by 1.2 million bpd for OPEC countries. The actual production by OPEC expanded in August by 0.9 million bpd.*

[2] *Estimate as of 22 October 2020.*

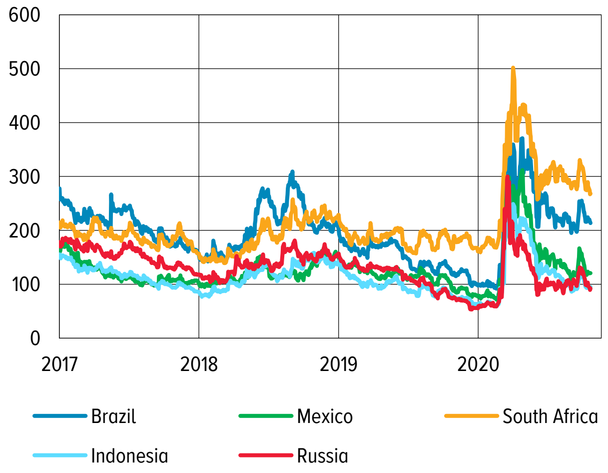
In late August–September, global financial markets experienced risk-off reactions and surging volatility. Stock indices adjusted downwards. The decline in demand for high-risk assets induced a spike in EMEs' and Russia's CDS. The yield curve of federal government bonds (OFZ) rose over its entire length. In October, volatility in global financial markets slightly decreased as the negotiations on support measures for the US economy progressed. Over the period of elevated volatility, non-residents considerably reduced their investment in OFZs, with this decline mostly offset already in October.

Rising sanction risks and geopolitical tensions, including those associated with the US elections, an increase in the capital outflow resulting from the repayment of external debt, and declining risk appetite in global financial markets aggravated volatility in the Russian financial market and, in particular, weakened the ruble which lost 8% over the period from late July through late October. Risk appetite recovered somewhat in October, contributing to the ruble's strengthening as compared with the late September lows.

Monetary conditions in the Russian economy continued to ease in June–September. In the first place, the easing of price conditions was facilitated owing to the decisions made by the Bank of Russia Board of Directors in April–July to cut the key rate by a total of 1.75 bp, coupled with the signals about a possible further easing of monetary policy. Banks also reported that the loosening of bank lending conditions in 2020 Q3 was also driven by the regulatory easing and stronger competition among market participants.

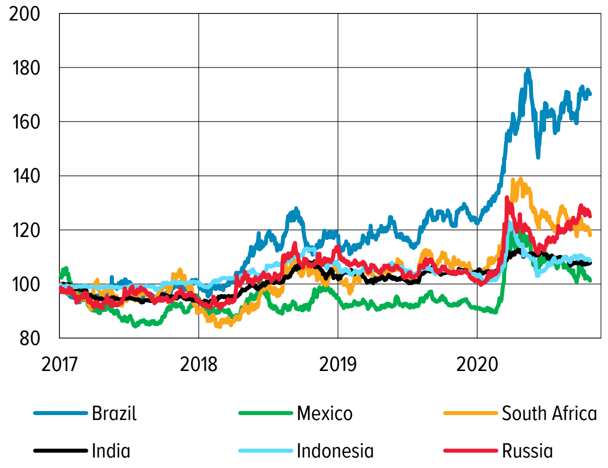
Preferential lending programmes had a large-scale, yet a temporary effect on loan rate movements. By mid-2020, over one-third of all new mortgage loans had been issued within preferential programmes, predominantly the 6.5% Programme. This significantly pushed up monthly turnover in the mortgage market hitting its record high in August (390 billion rubles), and largely supported demand for housing in Q2 (see the Box 'On the impact of demand- and supply-side shocks on the housing market in 2020'). According to preliminary data, the majority

CDS OF EMES *Chart 1.1.4*
(bp)



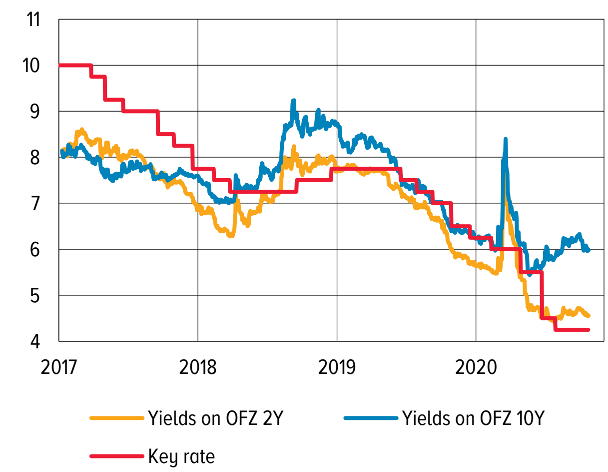
Source: Bloomberg.

USD EXCHANGE RATE AGAINST RUBLE AND EME CURRENCIES *Chart 1.1.5*
(Index, 01.01.2017=100)



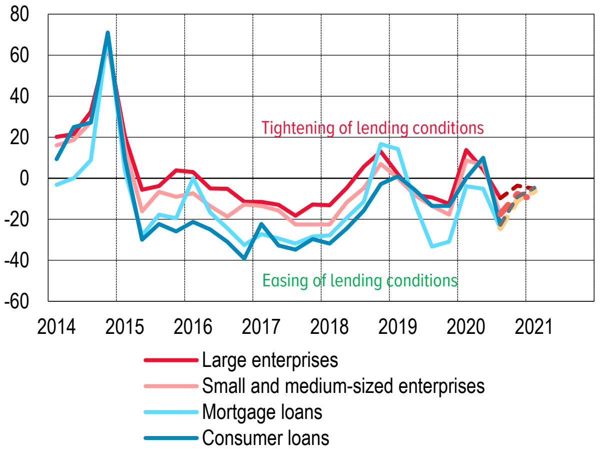
Source: Bloomberg.

OFZ YIELDS AND BANK OF RUSSIA KEY RATE *Chart 1.1.6*
(Index, 01.01.2017=100)



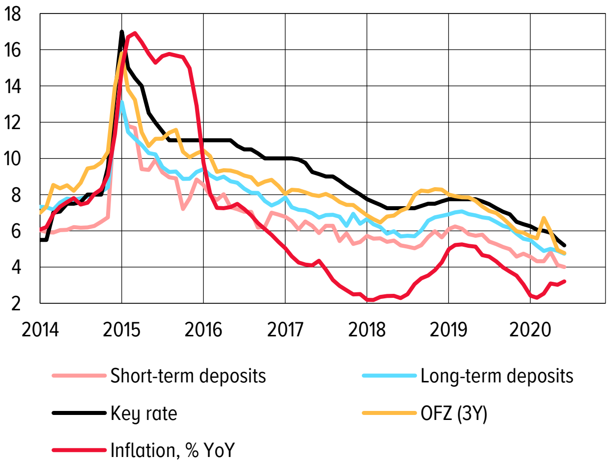
Sources: Cbonds.ru, Bank of Russia.

INDICES OF CHANGES OF BANK LENDING CONDITIONS* *Chart 1.1.7*
(pp)



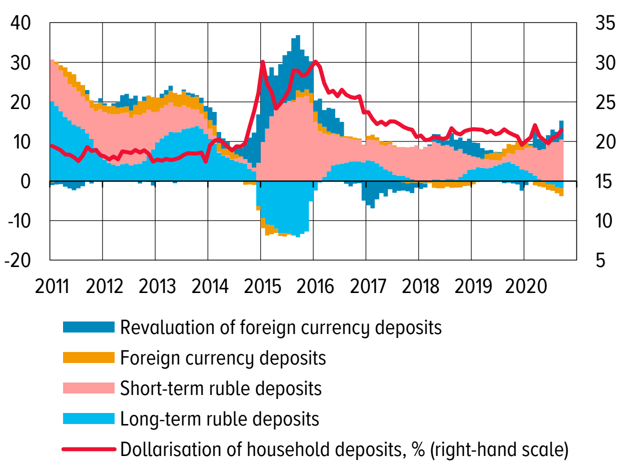
** The dotted lines show the expectations of respondent banks in 2020 Q3.*
Source: Bank of Russia.

INTEREST RATES ON HOUSEHOLD RUBLE DEPOSITS *Chart 1.1.8*
(% p.a.)



Source: Bank of Russia.

HOUSEHOLD DEPOSITS *Chart 1.1.9*
(contribution to annual growth, pp)



Source: Bank of Russia.

of banks were also easing non-price lending conditions in 2020 Q3, and most notably in the retail segment.

Deposit rates trended down in June–August. In August, this decrease slowed down as returns on financial market instruments rose and a number of large market players offered seasonal deposits in their range of deposit products. The potential for a further reduction in deposit rates is limited. As of the end of August, the annual growth[3] of household deposits slowed down only slightly, to 6.8% (from 7.2% in June), which is evidence that deposits remain an attractive savings instrument. Moreover, the rise in deposits was driven by the ruble segment, predominantly short-term products (deposits for up to 30 days, including demand deposits). This was explained by an increase in both households' demand for highly liquid assets and the attractiveness of demand deposit accounts resulting from the gradual convergence of interest rates on deposits with various maturities. The annualised amount of foreign currency deposits continued to shrink in August.

According to Rosstat's data, GDP declined by 8.0% in 2020 Q2, which is slightly better than the Bank of Russia's estimate given in MPR 3/20 (a decline of 9–10%). This deviation from the forecast was associated with more significant export volumes than expected, primarily oil and gas exports, as well as inventory accumulation stemming from the slump in domestic demand which declined more notably than assumed in the July forecast.

In 2020 Q3, economic activity in Russia started to revive, predominantly owing to industries focused on domestic consumption. According to the Bank of Russia's assessments, output in key industries expanded in Q3 (SA),[4] adding 2.6% against Q2.

[3] Hereinafter, increases in banks' balance sheet indicators are calculated based on the reporting data of operating credit institutions recorded in the State Register as of the relevant reporting date. Increases in foreign currency claims and liabilities are calculated in US dollar terms. To analyse the flows of funds between banks and their customers, the growth of the foreign currency component is converted into rubles using the period average exchange rate where increases in balance sheet indicators comprising foreign currency and ruble components are calculated herein.

[4] Hereinafter, seasonally adjusted.

The easing of the restrictions affecting the operation of the services sector and pent-up household demand supported consumer activity. As a result, non-food retail turnover largely bounced back, returning to its 2019 Q3 readings. Contrastingly, the value of commercial services to households remained close to its record lows due to the remaining restrictions affecting the operation of the services sector in a number of Russian regions, as well as the impact of social distancing required by the Federal Service for Surveillance on Consumer Rights Protection and Human Wellbeing (Rospotrebnadzor). Shifts in consumer preferences also hindered the recovery of demand. Amid the substantial decline in household incomes and increased unemployment in Q2–Q3, consumer activity was largely supported by government measures implemented at both the federal and regional levels.

The 2020 Q3 dynamics of budget indicators were in line with the Bank of Russia's July baseline forecast. Budget expenditures allocated to prop up the Russian economy during the pandemic reached their peak at the end of Q2 – the beginning of Q3. In August, the stimulating effect of the fiscal measures started to gradually diminish.

The restoration of production and logistics chains and the increase in households' demand for housing (see the Box 'On the impact of demand- and supply-side shocks on the housing market in 2020') revived investment activity. The anti-crisis measures being implemented by the Russian Government and the monetary easing continued to support fixed capital investment. Nonetheless, according to the Bank of Russia's assessment, fixed capital investment in Q3 remained by far below the Q2 level, which was largely because companies significantly revised their 2020 investment plans downwards.

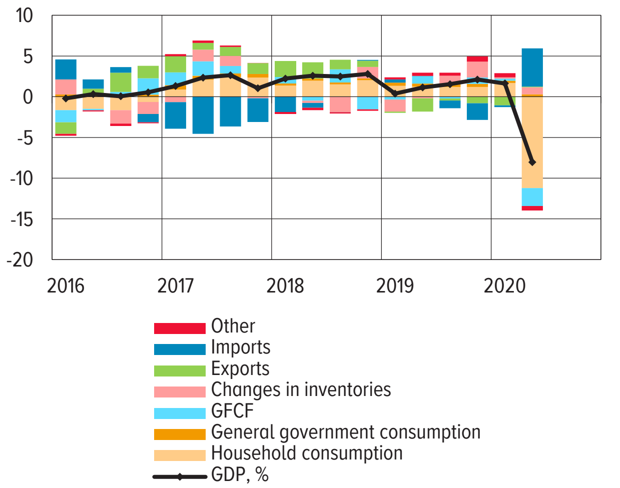
Production activity was bouncing back[5] in July–August.[6] By August, output in

[5] *In October, Rosstat revised upwards the entire path of production growth for 2019–2020. As assessed by the Bank of Russia, considering new data (SA), the recovery of industrial production after its decline in 2020 was faster than expected earlier.*

[6] *For details on economic activity in July–August, see Economy No. 7 (55) and Economy No. 8 (56), information and analytical commentaries.*

GDP BY EXPENDITURE
(contribution to annual growth, pp)

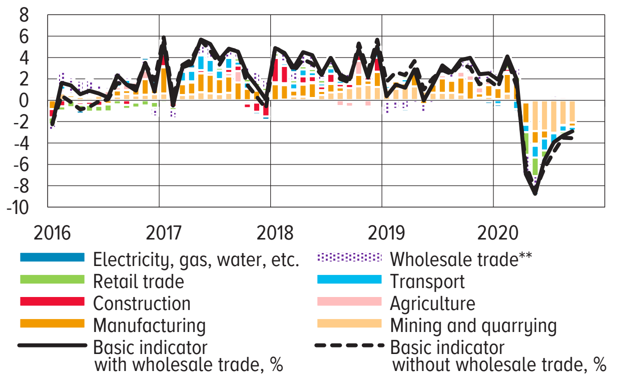
Chart 1.1.10



Sources: Rosstat, Bank of Russia calculations.

BASIC OUTPUT INDICATOR*
(contribution to annual growth, pp)

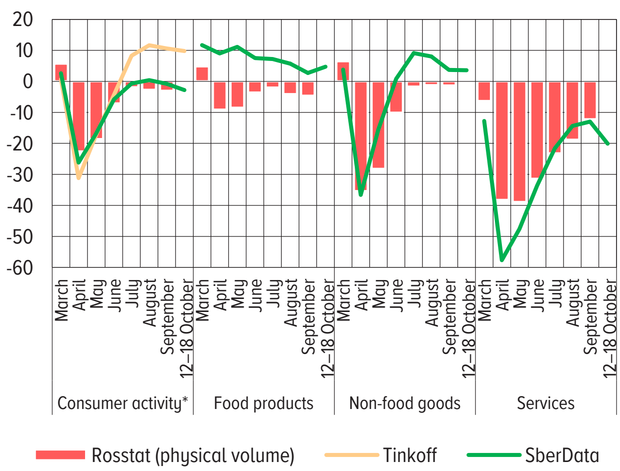
Chart 1.1.11



** Bank of Russia estimate. Reflects annual dynamics of production activity by key industry (manufacturing, agriculture, wholesale and retail trade, construction, and transport). Due to the publication of wholesale trade data with a certain lag, the indicator is calculated in two variants: with and without data on wholesale trade.*
*** Estimate based on updated wholesale trade data for September.*
Sources: Rosstat, Bank of Russia calculations.

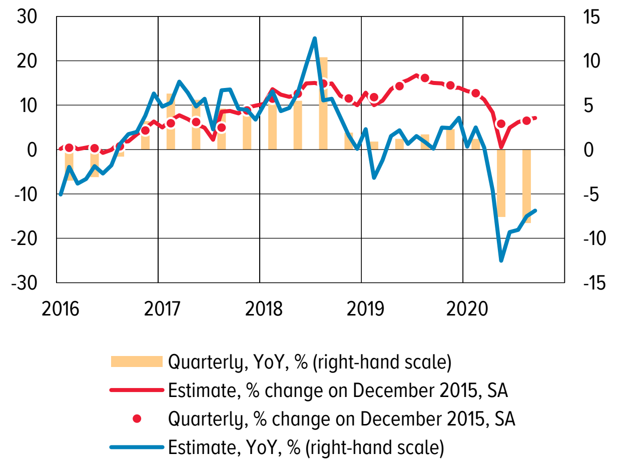
CONSUMER DEMAND INDICATORS
(% change on the same period of the previous year)

Chart 1.1.12



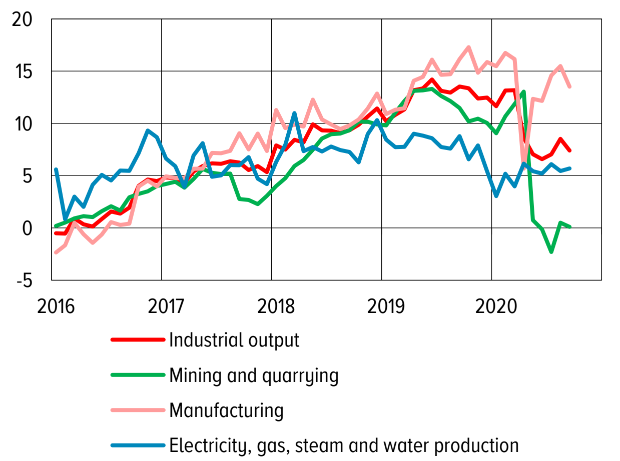
** Retail turnover for Rosstat.*
Sources: Rosstat, SberData Laboratory, Tinkoff.

FIXED CAPITAL INVESTMENT* *Chart 1.1.13*



** 2020 Q3 – the Bank of Russia's estimate.*
Sources: Rosstat, Bank of Russia calculations.

INDUSTRIAL OUTPUT *Chart 1.1.14*
(% change on December 2015, SA)



Sources: Rosstat, Bank of Russia calculations.

manufacturing recovered completely, with the output of investment and consumer goods even exceeding the averages[7] recorded in 2019 H2 – early 2020. Conversely, the output of intermediate goods showed relatively weak dynamics due to subdued external demand and persistent local disruptions in production and logistics chains. Output in primary industries remained low, which was mostly explained by the effect of the oil production cuts.

Overall, data on GDP and its components in 2020 Q2, as well as on economic activity in July–August resulted in an upward revision of the Q3 GDP growth outlook.

However, the revival discontinued already in September.[8] As of the end of September, industrial production contracted (SA), predominantly due to the decreased output of investment goods (both construction materials and engineering products). The annualised decline in industrial output, adjusted for calendar effects, sped up to 5.5% (vs 3.7% in August). The revival of consumer activity slowed down, with retail sales decreasing mostly due to food products.

The significant reduction in the output of investment goods in September may suggest that investment activity might shrink in the next months. The leading indicators of consumer activity also point to its further decline in early October. As the epidemiological situation deteriorates and the fiscal stimulus programmes contract, consumer activity may go down by the end of the year.

With account of the above, the GDP estimate for Q4 was revised downwards. By the end of 2020, GDP is expected to decrease by 4.0–5.0%, which is slightly better compared to the MPR 3/20 forecast.

Consumer prices showed unsteady dynamics in 2020 Q3, primarily due to volatile services prices (see Section 2 'Inflation and inflation expectations'). Their volatility intensified since the scale of the anti-pandemic restrictions was uneven across both market segments and

[7] *According to the Bank of Russia's assessment, seasonally adjusted (SA).*

[8] *For details on economic activity in September, see Economy No. 9 (57) (September 2020), information and analytical commentary.*

Russian regions, and authorities made local decisions regarding administered prices.

Annual inflation rose to 3.67% in September, primarily driven by the faster growth of non-food prices. Proinflationary pressure on non-food prices was caused by the weaker ruble and the revival of consumer activity in July–August. Demand remained moderate overall, which limited the growth rate of prices.

Food prices were mostly impacted by disinflationary factors, specifically steady growth in agriculture, including both livestock and crop production. The rise in annual food inflation was associated with the effect of last year's low base. The monthly growth rate of food prices decreased in Q3.

Prices in various goods and services groups may continue to change very unevenly throughout 2020. A short-term impact on current price movements may be caused by the weaker ruble and the tightening of the anti-pandemic measures, including those aimed at stricter control over compliance with Rospotrebnadzor's requirements. **Conservative consumer demand will remain the key factor hindering price growth. As forecast by the Bank of Russia, amid the currently pursued monetary policy, annual inflation will equal 3.9–4.2% in 2020.**

1.2. BANK OF RUSSIA'S FORECAST

The global economy will bounce back slowly, and the external output gap will remain negative until the end of the forecast horizon.

The decline in the global economy in 2020 Q2 turned out to be less significant than forecast earlier by the Bank of Russia. Moreover, Q3 leading indicators evidence an active recovery (see the section 'Current situation').

However, the resurgence of infection cases and the reintroduction of restrictions in a range of countries (namely, in Europe) at the end of Q3 – the beginning of Q4 became the reason why the estimate of the recovery path until the end of 2020 and in 2021 was revised. On the one hand, the Bank of Russia slightly improved its estimate of annual growth in the global economy. On the other hand, the Q4 estimate of the sequential quarterly growth of GDP was adjusted downwards since the considerable rise in coronavirus infection cases adversely affected consumer and investor sentiment. Consequently, recovery processes will be less active in 2021 than it was expected earlier.

It may take a long time to return to normal life, while differences in the possibilities to adjust to the new situation across countries and industries will make it hard to accelerate recovery growth. Another factor that will hinder a fast revival will be the search for new business models meeting changes in the environment and consumer preferences (social distancing, new consumer patterns, and an increased level of savings).

Therefore, the Bank of Russia assumes that the external output gap will remain negative even by the end of the forecast horizon.

Elevated uncertainty in the global economy inducing a higher volatility of capital flows in emerging market economies may persist until the end of 2020, gradually decreasing by the end of 2021.

The accelerated spread of the coronavirus worldwide at the end of Q3 – the beginning of Q4 spurred the growth of volatility in financial markets (see the section 'Current situation').

Amid the persistent uncertainty over the recovery pace of the global economy and the further spread of the coronavirus, EMEs' risk premia will remain increased at the end of 2020, starting to trend down gradually in early 2021. Russia's risk premium will remain elevated in 2021 due to the additional effects of idiosyncratic geopolitical factors. Increased uncertainty and higher risk premia may cause more significant capital flow fluctuations in EMEs and Russia both until the end of 2020 and throughout 2021.

Beginning from the end of 2021, the balance of risks for EMEs, including for Russia, will return to the levels common to these markets. As risk premia go down gradually, capital inflows to EMEs will stabilise.

Oil prices will stabilise close to USD45–50 per barrel in 2022–2023.

The fulfilment of the OPEC+ deal and the recovery of global demand for oil will gradually drive the average annualised oil price upwards to USD45 per barrel in 2021–2022 and USD50 per barrel in 2023. Nonetheless, the recovery of oil prices will be moderate due to the expected gradual expansion of non-OPEC+ oil supply and the easing of the OPEC+ oil production limits.

Russia's economy will shift to a sustainable recovery in early 2021 and will reach its potential output level in 2022 H1, maintaining this level until the end of the forecast horizon.

In late 2019 – early 2020, the growth rate of the Russian economy was close to its potential, with the output gap approximating zero. The pandemic provoked a slump in Russia's actual output to the level below the potential. As in many other countries, the 2020 Q2 data show that Russia's GDP declined slightly less than expected earlier by the Bank of Russia. However, the reduction in final consumption and gross fixed capital formation turned out to be more significant. Contrastingly, exports demonstrated unexpected growth, while it was forecast to contract notably (see the section 'Current situation').

As a result, the Bank of Russia revised upwards its estimate of the annual growth of Russia's GDP, while considerably adjusting sequential quarterly changes in 2020 Q3–Q4. According to up-to-date indicators, economic activity recovered markedly in 2020 Q3. However, the worsening of the epidemiological situation at the end of Q3 – the beginning of Q4 is the reason why this trend may hardly be expected to continue. Consequently, in contrast to the progressive recovery of the GDP growth rate in Q3–Q4 forecast earlier by the Bank of Russia, the current baseline scenario relies on the assumption of the substantial acceleration in Q3 of the sequential quarterly GDP growth and its near-zero rate in 2020 Q4. In 2021, Russia's economy will continue to bounce back.

The recovery growth of consumer and investment demand will be promoted by accommodative monetary policy and the measures taken in 2020 by the Russian Government to support households and businesses. At the same time, the support from fiscal policy will steadily diminish, with gradual budget consolidation starting already in 2021 Q2 and the level of spending brought in line with the fiscal rule parameters in 2022–2023.

Loose monetary conditions and the recovery of confidence among households and businesses about their future incomes will boost demand for credit. After 9–12% in 2020, the growth of the banking system's claims on the economy will go down to 7–11% in 2021 and remain at this level further on. Contrastingly, the banking system's claims on households will continue to expand slightly faster (to 10–14% by 2023) than claims on companies (to 6–10%).

The contribution of budget operations to money supply will decrease, and by 2023 the growth of money supply will be driven by the expansion of banks' claims on the economy, equalling 7–11%.

As a result, the increase in households' final consumption expenditure will total 5.3–6.3% in 2021 and 3.7–4.7% in 2022, getting closer to its long-term rates of 2.5–3.5% in 2023. Gross fixed capital formation will be recovering more smoothly, with its growth reaching 3.3–5.3% in 2021 and 4.5–6.5% in 2022 and subsequently slowing down to 3.2–5.2% in 2023.

Output will return to its 2020 Q1 level at the beginning of 2022. The negative output gap due to expenditure consolidation in the budget system, the effect of the OPEC+ restrictions, and only a partial recovery of external demand will remain throughout 2021. In early 2022, this gap will be close to zero, staying at this level until the end of the forecast horizon. Accordingly, the recovery pace of Russia's economy will exceed its potential growth rate in 2021 and is expected to be close to it beginning from mid-2022. Potential growth may accelerate in 2023, provided the Government of the Russian Federation successfully implements the measures aimed at overcoming structural constraints, including as part of the approved national projects.

Inflation will stabilise close to 4% amid the currently pursued accommodative monetary policy.

In 2020, price trends were influenced by both disinflationary (weak domestic and external demand) and proinflationary factors (a weaker ruble and extra costs incurred by businesses, including to comply with the anti-pandemic requirements) (see the section 'Current situation'). According to the baseline scenario, inflation will be in the range of 3.9–4.2% as of the end of 2020.

The disinflationary impact of subdued demand will prevail throughout 2021 until early 2022, with sequential quarterly price growth slowing down noticeably. As aggregate demand progressively recovers owing to decreasing epidemiological risks, the negative output gap will gradually close. Coupled with accommodative monetary policy, this will gradually speed up price growth to 4%.

As the Russian economy revives and inflation stabilises close to 4% over the forecast horizon, the Bank of Russia will assess a possible time and pace for shifting from accommodative to neutral monetary policy, including with account of the downward revision of the real neutral key rate from 2–3% to 1–2% per annum (for details regarding the estimate of the neutral rate, see Box 2 'Neutral interest rate' in the draft Monetary Policy Guidelines for 2021–2023).

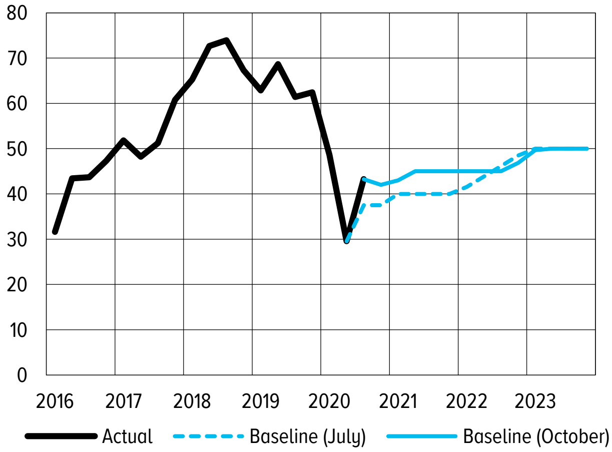
The current account surplus will shrink against 2019; net lending by the Russian private sector to the rest of the world will decrease by the end of the forecast horizon.

A considerable decline in external demand and the slump in oil prices will reduce the current account surplus in 2020 compared to 2019. Russian exports were supported to a certain extent by global demand for gold which soared amid the uncertainty in the global economy (see the section 'Current situation').

The adverse effect of the external demand shock on Russia's economy will persist throughout 2020 and during the most part of 2021. In 2022–2023, in addition to the normalisation of the situation in the global economy, exports will also be promoted by the lifting of the OPEC+ restrictions.

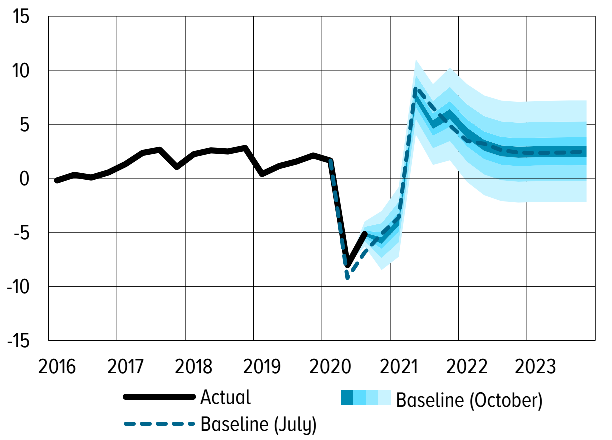
In 2020–2021, the current account surplus will approximate 2%, but will go down to 1% in 2022 owing to the recovery of tourist activity (imports in the 'Travels' item), provided that the average annualised oil price remains stable (USD45 per barrel in 2021 and 2022). In 2023, as

OIL PRICE TRAJECTORY* IN THE BASELINE SCENARIO *Chart 1.2.1*
(US dollars per barrel)



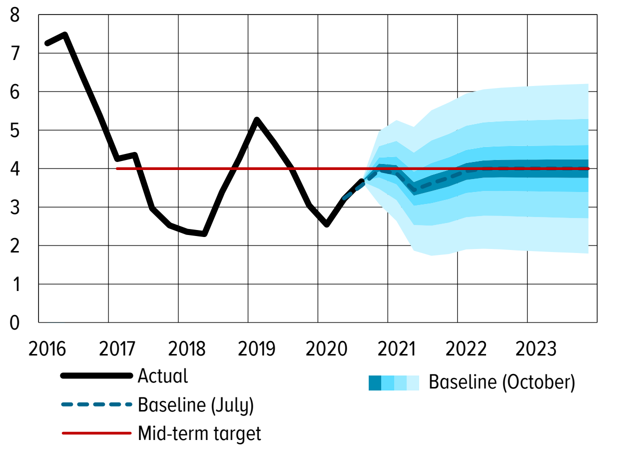
** Nominal Urals crude prices (the arithmetic mean of Urals crude price delivered to the Mediterranean and north-western Europe).*
Source: Bank of Russia calculations.

GDP GROWTH TRAJECTORY IN THE BASELINE SCENARIO *Chart 1.2.2*
(% change on the same period of the previous year)



Note: shaded areas on the forecast horizon show the probability of different GDP growth values. Colour gradation reflects probability intervals. Confidence intervals are symmetrical and based on historical estimates of GDP growth uncertainty.
Source: Bank of Russia calculations.

INFLATION TRAJECTORY IN THE BASELINE SCENARIO *Chart 1.2.3*
(% change on the same period of the previous year)



Note: shaded areas on the forecast horizon show the probability of different inflation values. Colour gradation reflects probability intervals. Confidence intervals are symmetrical and based on historical estimates of inflation uncertainty.
Source: Bank of Russia calculations.

the situation in the global economy normalises, the current account surplus will expand again to 2%, including owing to the rise in oil prices to the average annualised level of USD50 per barrel.

As risks in the global economy go down and the impact of idiosyncratic geopolitical factors weaken, the balance of the private sector's financial transactions will gradually contract, which will improve Russia's investment attractiveness amid accelerating economic growth.

Risks to the implementation of the baseline scenario remain significant.

Despite the gradual adaptation of the entire world to living in the pandemic, any economic forecasts still involve a high degree of uncertainty compared to previous years' forecasts. The occurred shock will most likely have a negative impact on economic processes throughout the next few years. The scale and uniqueness of the combination of the pandemic-related shocks could also affect the transmission mechanism, and these changes are still to be assessed.

If the epidemiological situation remains acute, this will cause a steady decline in consumer and investor sentiment.

A further spread of the coronavirus will entail extra costs for businesses if the budget system provides no support. Specifically, companies will need to ensure safe communication with customers, adjust their logistics chains, which includes changes in transport types, and redistribute their assets across different activities.

A contraction of economic activity following the reintroduction of tight restrictions in a range of countries may push the oil price below the path presumed in the baseline scenario, even despite the OPEC+ efforts to contain excess supply, which will induce a decline in oil and gas revenues in the Russian budget.

Affected by steadily weak consumer and investor demand and shrinking oil and gas revenues in the economy, inflation in Russia may drop considerably below the level forecast under the baseline scenario. Declining household incomes will also be a factor contributing to disinflationary trends.

2. INFLATION AND INFLATION EXPECTATIONS

In 2020 Q3, consumer price dynamics remained unsteady. Fluctuations in current price growth rates were predominantly associated with services price movements caused by changes in anti-pandemic requirements and decisions on administered prices. The growth of food prices (seasonally adjusted) slowed down as supply continued to expand. The weaker ruble sped up the rise in non-food prices. Overall, average monthly growth was below 4% in annualised terms.

Households' and businesses' short-term inflation expectations increased amid intensifying proinflationary pressures. Analysts also adjusted their forecasts upwards, close to the inflation target.

Inflation is currently in line with the Bank of Russia's forecast and is expected to be in the range of 3.9–4.2% as of the end of 2020.

CONSUMER PRICES FOR MAIN GROUPS OF GOODS AND SERVICES IN 2020 *Table 2.1*
(% change on previous month, SA)

	April	May	June	July	August	September
Inflation	0.84	0.28	0.28	0.19	0.40	0.23
Food products (excluding fruit and vegetables)	0.89	0.47	0.45	0.38	0.30	0.22
Non-food goods (excluding petroleum products)	0.57	0.33	0.33	0.29	0.43	0.53
Services (excluding utilities)	0.26	0.42	-0.37	0.12	0.23	-0.17

Sources: Rosstat, Bank of Russia calculations.

CONSUMER PRICES FOR MAIN GROUPS OF GOODS AND SERVICES IN 2020 *Table 2.2*
(% change on the same month of the previous year)

	April	May	June	July	August	September
Inflation	3.09	3.02	3.21	3.37	3.58	3.67
Food products (excluding fruit and vegetables)	3.40	3.44	3.61	3.71	3.72	3.80
Non-food goods (excluding petroleum products)	2.99	3.08	3.22	3.25	3.52	3.94
Services (excluding utilities)	2.97	3.12	2.37	2.26	2.41	2.07

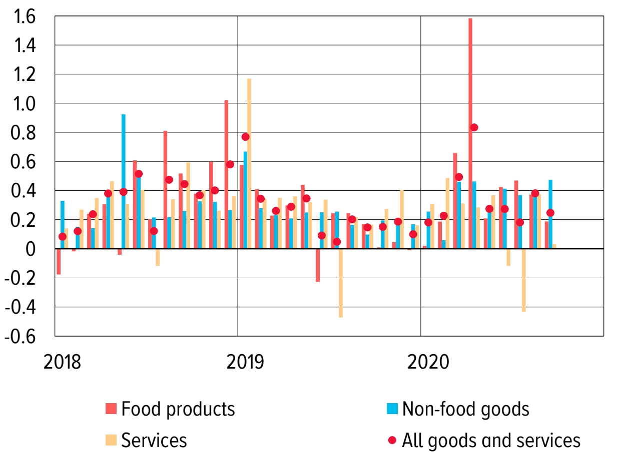
Sources: Rosstat, Bank of Russia calculations.

CONSUMER PRICES FOR MAIN GROUPS OF GOODS AND SERVICES IN 2020 *Table 2.3*
(% change on previous month, SAAR)

	April	May	June	July	August	September
Inflation	10.56	3.41	3.41	2.30	4.91	2.80
Food products (excluding fruit and vegetables)	11.28	5.82	5.51	4.62	3.63	2.71
Non-food goods (excluding petroleum products)	7.01	4.05	4.05	3.51	5.25	6.54
Services (excluding utilities)	3.19	5.10	-4.35	1.44	2.81	-2.03

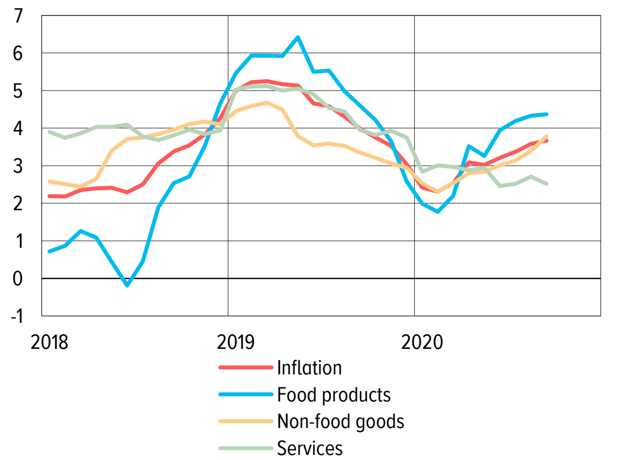
Sources: Rosstat, Bank of Russia calculations.

GOODS AND SERVICES PRICES *Chart 2.1*
(% change on previous month, SA)



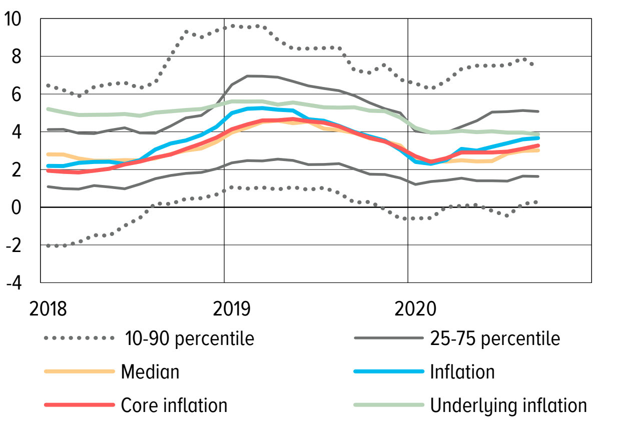
Sources: Rosstat, Bank of Russia calculations.

INFLATION AND ITS COMPONENTS *Chart 2.2*
(% change on the same month of the previous year)



Sources: Rosstat, Bank of Russia calculations.

DISTRIBUTION OF GOODS AND SERVICE PRICE GROWTH, INFLATION, CORE INFLATION, AND UNDERLYING INFLATION *Chart 2.3*
(% change on the same month of the previous year)



Sources: Rosstat, Bank of Russia calculations.

INFLATION

In 2020 Q3, inflation movements were driven by competing factors of various nature: the loosening of social distancing restrictions and the related revival in economic activity and demand which, nonetheless, was still sluggish overall, the weakening of the ruble, including time-lag effects, and expanding food supply.

The easing of anti-pandemic requirements was phased, varying across both Russian regions[1] and individual market segments of consumer goods and services. This was the reason why **prices continued to move diversely, which was most evident in the services market**. The fluctuations of services prices caused unsteadiness in the monthly growth rates of consumer prices in general (according to the seasonally adjusted assessment; hereinafter, SA; Table 2.1; Chart 2.1). They ranged from 0.19% to 0.41% (SA).

The pass-through of the ruble's weakening to prices was most pronounced in non-food price movements. The monthly growth of non-food prices (SA) increased over the quarter. Nonetheless, the effect of this pass-through generally remained relatively small. **Food inflation remained low because of the steadily expanding supply** of meat products and the good harvest of main crops.

In September, inflation reached 3.67% (from 3.21% in June; Chart 2.2), primarily driven by the faster annual growth of non-food prices. There was also an increase in the steadier indicators of price dynamics, including annual core inflation, median, and price growth rates excluding the most volatile or administered components (Table 2.2; Chart 2.3). Underlying inflation[2] trended down to 3.86% in September (vs 4.02% in June).

Inflation is currently in line with the Bank of Russia's forecast and is expected to be in the range of 3.9–4.2% as of the end of 2020.

[1] *For more information on inflation in Russian regions, see the Annex 'Economic situation in Russian regions'.*

[2] *For more information on underlying inflation, see Macroeconomic Bulletins in the Research section on the Bank of Russia website.*

The impact of short-term factors associated with anti-pandemic measures

Since anti-pandemic restrictions were lifted unevenly across various services sectors, this amplified the volatility of services prices and, consequently, consumer prices in general.

Prices fluctuated most significantly for recreation and transportation services, which remained under the effect of anti-pandemic restrictions (Table 2.4). Specifically, the reopening of the main Russian resorts in August sped up the rise in prices for domestic tourism services highly requested because the main overseas tourism destinations remained closed for Russians. In statistics, prices for them[3] were recorded as unchanged beginning from April, and their annual growth was negative. However, since the portion of expenses for overseas tourism services is small (1.9%), the contribution of changes in their prices to inflation did not exceed 0.1 percentage points. Air fares remained highly volatile in Q3, which was associated with the impact of restrictions and the uneven resumption of regular flights.

Measures aimed at providing social support to households caused deviations in the growth of administered prices for individual types of services from the conventional pattern, which also affected price volatility. Specifically, a number of regions postponed the indexation of some utility rates in July. Accordingly, their annual growth was below the originally planned level (Table 2.5). Utility rates were gradually raised in subsequent months. Beginning from July, the annual growth of prices for housing services in the administered segment[4] was lower than in Q2. In September, the annual growth of prices for higher education services decreased (to 1.14% from 7.42% in August): as a measure of social support to students, Russia's Ministry of Education and Science jointly with the Russian Union of Rectors recommended that universities kept the cost of education in 2020 at its 2019 level.

PRICES FOR RECREATIONAL AND TRANSPORTATION SERVICES IN 2020 *Table 2.4*
(% change on the same month of the previous year)

	April	May	June	July	August	September
Domestic tourism	2.4	2.6	2.7	0.6	1.2	0.5
Outbound tourism	1.2	1.3	-0.6	-2.5	-2.8	-1.0
Air transportation	0.0	3.7	6.2	-7.6	-6.0	-10.7

Source: Rosstat.

ADMINISTERED SERVICES PRICES IN 2020 *Table 2.5*
(% change on the same month of the previous year)

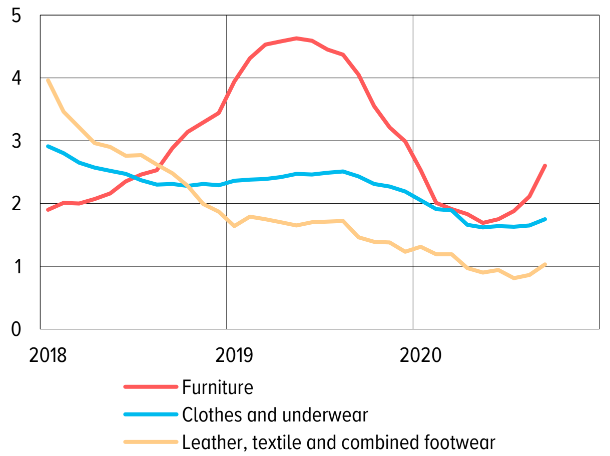
	April	May	June	July	August	September
Utility services	2.4	2.4	2.4	2.4	3.4	3.5
Housing services in the administered segment	4.3	4.2	4.2	3.9	3.8	3.8
Higher education	7.4	7.4	7.4	7.4	7.4	1.1

Source: Rosstat.

[3] *Included by Rosstat in the consumer basket to measure the CPI (namely, holidays in Turkey are not taken into account in the consumer basket).*

[4] *Residential payments in state-owned and municipal houses, housing maintenance and repair payments, etc.*

PRICES FOR CERTAIN NON-FOOD GOODS *Chart 2.4*
(% change on the same month of the previous year)



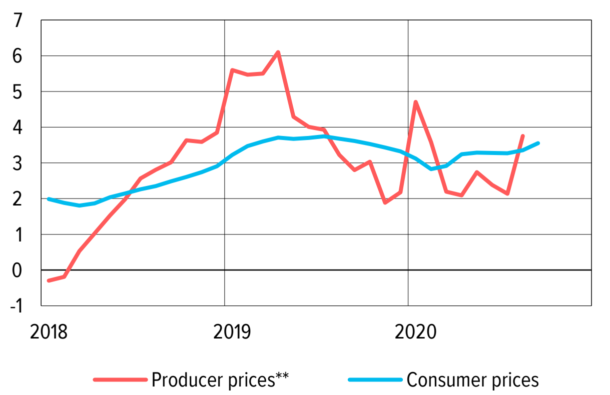
Source: Rosstat.

PRICES FOR CERTAIN NON-FOOD GOODS IN 2020 *Table 2.6*
(% change on the same month of the previous year)

	April	May	June	July	August	September
Household appliances	2.49	2.25	2.62	2.91	3.34	3.90
Instruments	2.47	3.12	3.35	3.23	3.82	4.36
Computers	1.13	1.48	1.88	1.68	2.09	2.91
New imported cars	4.28	4.59	5.47	5.3	5.87	6.98
Second-hand imported cars	0.02	0.15	-0.18	-0.45	0.2	1.59

Source: Rosstat.

PRODUCER PRICES OF NON-FOOD CONSUMER GOODS* AND CONSUMER PRICES *Chart 2.5*



**Clothing, underwear, knitted wear, furs, footwear, household chemicals, furniture, medical goods, domestic passenger cars, printed media, paper goods, and stationeries.*
*** Weighted according to their weighs in the consumer basket (total weight 15.63%).*
Sources: Rosstat, Bank of Russia calculations.

Influence of the ruble exchange rate

Trade restrictions were being eased in Q3 simultaneously with the pass-through of the ruble's weakening to price dynamics, including exchange rate movements occurred at the end of Q1 and in Q2. The pass-through was most evident in the growth of prices for non-food imports or non-food products with a significant import component in prices (Table 2.6). The annual growth rate in these groups was up. The average monthly growth (SA) of non-food prices in Q3 was generally higher than in Q2, exceeding 4% in annualised terms. Nonetheless, the extent of the pass-through was relatively low overall.

In the next months, the proinflationary pressure of the weaker ruble will most likely persist. However, this impact is a short-term factor and involves no risks to inflation in the medium term.

Influence of demand-side factors

Subdued consumer demand continues to limit inflation. After a certain revival at the beginning of the quarter promoted by the easing of anti-pandemic restrictions in retail trade, consumer activity weakened again already in September (see Section 1.1 'Current situation'). Overall, the increase in prices for clothing, footwear and furniture was slow during the quarter, not exceeding the rate recorded at the beginning of the year (Chart 2.4). Final demand also hindered the rise in producer prices for non-food consumer goods, even despite the weakening of the ruble (Chart 2.5).

Influence of food supply-side factors

The rich harvest of main crops[5] and the sustainable development of livestock production ensured stable food supply which even expanded in individual segments (in the first place, the supply of animal products; Chart 2.6). Over the course of Q3, the monthly growth of food prices (excluding fruit and vegetables characterised by high price volatility) was slowing down, reaching 0.21% in September (SA; vs 0.44% SA in June).

[5] *Specifically, in September, Russia's Ministry of Agriculture expected wheat harvest to be the second largest after the 2017 record.*

Annual food inflation was rising due to the base effect: last year, food prices were dragged down by a whole range of disinflationary factors, and their rise was uncommonly low. In September 2020, food prices were 4.37% higher than in the previous year (0.43 pp higher than in June), with the annual growth of prices for food products, excluding fruit and vegetables, equalling 3.80% (+0.19 pp vs June).

INFLATION EXPECTATIONS

In August–October 2020, economic agents raised their short-term (within one year) inflation expectations amid accelerated price growth and intensified proinflationary factors. Analysts also upgraded their forecasts, closer to the Bank of Russia's target.

Household inflation expectations

According to InFOM's surveys of households (commissioned by the Bank of Russia), inflation expectations were elevated in August–October. In September–October, the median estimate of inflation observed by households over the past 12 months was growing simultaneously with actual inflation, reaching 9.6% (Chart 2.7). The median estimate of inflation expected in the next 12 months also increased. In October, it hit its 2018 average and exceeded observed inflation, equalling 9.7%.

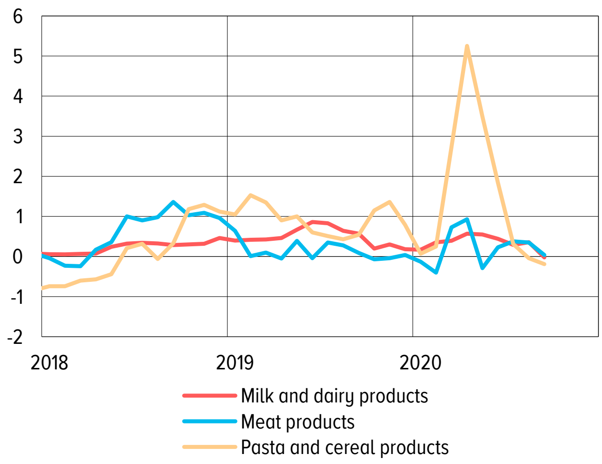
Households tend to notice rises in prices for the most frequently purchased goods and services. In August–October, households complained about higher prices for sugar, sunflower oil and cereals considerably more often than at the beginning of the year. Rosstat recorded the accelerated growth of prices for these products, which was caused by the decrease in the output of sugar beet, sunflower seeds, buckwheat and rice.

Business price expectations

According to business surveys carried out by the Bank of Russia,[6] price expectations trended up in August–October (Chart 2.8). The question about the reasons behind price growth showed that the increase in price expectations was

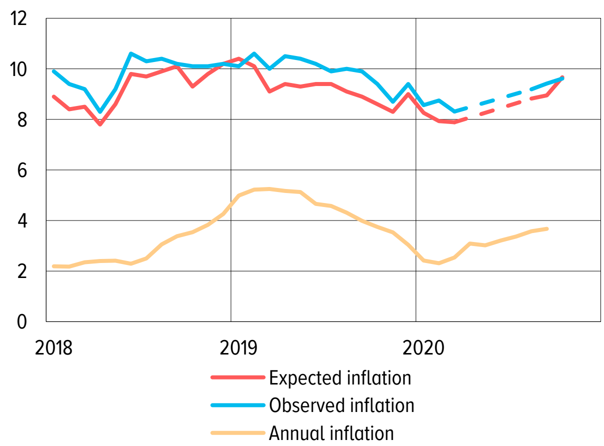
[6] *For details regarding the methodology of surveys, see the methodological commentary [Analysis of Companies' Price Expectations](), December 2018.*

PRICES FOR CERTAIN FOOD PRODUCTS *Chart 2.6*
(% change on previous month, SA)



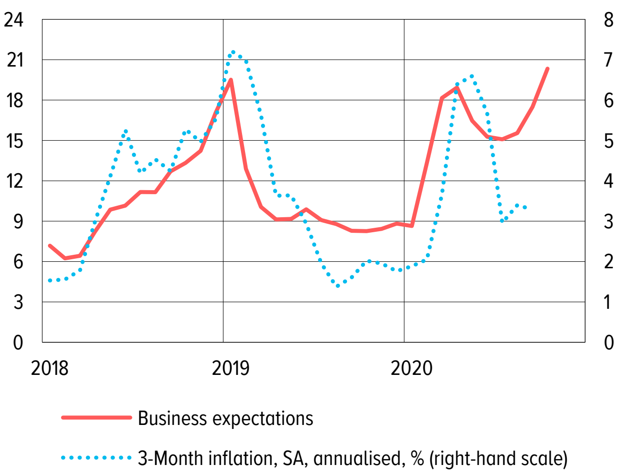
Sources: Rosstat, Bank of Russia calculations.

ANNUAL INFLATION, AND MEDIAN ESTIMATE OBSERVED AND EXPECTED BY HOUSEHOLDS *Chart 2.7*
(%)



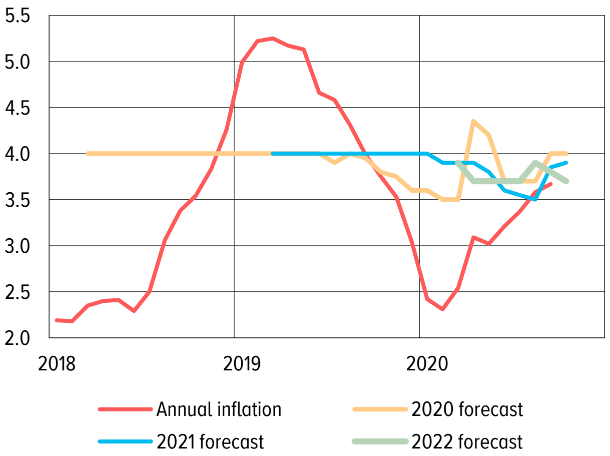
Sources: InFOM, Rosstat.

BUSINESS PRICE EXPECTATIONS *Chart 2.8*
(balance of responses, %)



Sources: Bank of Russia, Rosstat.

BLOOMBERG ANALYSTS' CONSENSUS FORECAST *Chart 2.9*
(%)



Sources: Bloomberg, Rosstat.

primarily caused by the depreciation of the ruble and the resulting rises in costs. Nonetheless, the scale of the expected price revision remained low beginning from 2020 Q2.

Price growth was expected to speed up across all industries and in the majority of Russian regions.[7] The highest increase in expectations was recorded in the wholesale and retail trade.

Analysts' inflation expectations

In July – early October, professional analysts were raising their inflation forecasts for 2020 and 2021, closer to 4% (Chart 2.9). Intensifying geopolitical tension and the weaker ruble were the key factors making analysts revise their forecasts.

Analysts' medium-term forecasts remained anchored at the Bank of Russia's target.

[7] *For details about regional differences in the dynamics of price expectations, see the Annex 'Economic situation in Russian regions'.*

3. BANK OF RUSSIA’S MONETARY POLICY

In September and October, the Bank of Russia Board of Directors decided to keep the key rate at 4.25% p.a. During the period from July, inflation was influenced by a number of important competing factors. On the one hand, this was the weakening of the ruble occurred in August–September due to generally increased volatility in global markets and intensified geopolitical risks. On the other hand, this was the slower revival of domestic demand in September–October as compared to summer. Households and businesses raised their inflation expectations, which was largely associated with the observed volatility of the exchange rate. Annual inflation is forecast to reach 3.9–4.2% by the end of 2020.

Disinflationary risks still prevail over the medium-term horizon, although the effect of short-term proinflationary factors slightly increased in autumn. Disinflationary pressure associated with the downward deviation of the economy from potential may increase amid the worsening epidemiological situation in Russia and abroad. Nonetheless, the earlier decisions to substantially reduce the key rate and the currently pursued accommodative monetary policy limit the risks of a significant downward deviation of inflation from its target in 2021. The Bank of Russia forecasts that, given the monetary policy pursued, annual inflation will equal 3.5–4.0% in 2021 and will stay close to 4% further on.

If the situation develops in line with the baseline forecast, the Bank of Russia will consider further key rate cuts at upcoming Board of Directors meetings. Making its key rate decisions, the Bank of Russia will take into account actual and expected inflation dynamics relative to the target and economic developments over the forecast horizon, as well as risks created by internal and external conditions and how financial markets respond to them.

Short-term interbank lending rates in the money market predominantly stayed in the lower half of the interest rate corridor and close to the Bank of Russia key rate. The key rate was not revised in August–October, and therefore, this factor did not impact the behaviour of market participants. As a result, the average spread got close to the levels of those averaging periods when the key rate was not expected to go down either.

Over the period from July through the first half of October, the surplus of the banking sector’s liquidity contracted. Although expanding considerably more slowly than in the previous months, the amount of cash in circulation still remained the major contributor to liquidity outflow. Demand for cash is still expected to gradually decrease to its pre-pandemic levels as economic activity returns to normal, yet this process will mostly shift to 2021. In view of the above and given the announced additional foreign currency sales in the domestic market, the forecast of the structural liquidity surplus for the end of 2020 was lowered from 1.4–2.0 to 1.0–1.4 trillion rubles.

3.1. KEY RATE DECISIONS

Key rate decisions. In September and October, the Bank of Russia Board of Directors decided to keep the key rate at 4.25% p.a., maintaining accommodative monetary policy.

Making its key rate decisions, the Bank of Russia took into account the following factors.

First, during the period from July, **inflation** was influenced by a number of important competing factors. On the one hand, this was the weakening of the ruble occurred in August–September due to generally increased volatility in global markets and intensified geopolitical risks. On the other hand, this was the slower revival of domestic demand in September–October as compared to summer. In these conditions, annual inflation rose to 3.7% in September, from 3.4% in July. As estimated by the Bank of Russia, over the period under review, the indicators of the current consumer price growth rates reflecting the most stable price movements were close to 4% in annualised terms. Annual inflation is forecast to reach 3.9–4.2% by the end of 2020.

In September–October, households and businesses raised their inflation expectations. This was largely how they responded to the intensified effect of short-term proinflationary factors, primarily those associated with the exchange rate volatility. Conversely, during the period from July, analysts' one-year-ahead inflation expectations remained slightly below 4%, which is evidence of dominating disinflationary factors. Over a longer-term horizon, their expectations are anchored close to 4%.

The persistent downward deviation of the economy from potential induces disinflationary pressure in the medium term which may increase amid the worsening epidemiological situation in Russia and abroad. Nonetheless, the currently pursued accommodative monetary policy limits the risks of a significant downward deviation of inflation from the target in 2021. The Bank of Russia forecasts that given the monetary policy pursued, annual inflation will equal 3.5–4.0% in 2021 and will stay close to 4% further on.

Second, over the period from July, **monetary conditions** generally continued to ease, in part owing to the considerable key rate reductions in April–July. Loan and deposit rates were predominantly declining; and lending continued to expand. In addition to the key rate decrease, interest rates and lending trends were significantly influenced by the preferential programmes launched by the Government and the Bank of Russia, as well as the regulatory easing. Making its key rate decisions, the Bank of Russia will take into account how the expected termination of the effect of these anti-crisis measures will impact monetary conditions.

Amid higher volatility in financial and commodity markets, yields on OFZs with longer maturities were moving diversely. Nonetheless, this did not have any significant influence on domestic monetary conditions. By the end of October, these yields stayed close to the levels recorded in mid-2020.

As a result of considerable decreases in interest rates, financial institutions, businesses and households are adjusting their behaviour, including saving models, to the new conditions in the financial market.

Overall, according to the Bank of Russia's opinion, it is essential to maintain accommodative monetary conditions in order to support the revival of domestic demand and ensure the stabilisation of inflation close to 4% over the forecast horizon.

Third, after the restrictions were eased in summer, **economic activity** started to bounce back faster than expected by the Bank of Russia. However, the up-to-date indicators of economic activity evidenced that the recovery growth of Russia's economy slowed down in September–October, which was largely due to domestic demand dynamics. The worsening of the epidemiological situation in Russia and abroad in September–October adversely affected household and business sentiment, which may entail both disinflationary and proinflationary effects. Nonetheless, the Bank of Russia estimates that disinflationary pressure induced by weaker demand will prevail.

According to the Bank of Russia's forecast, GDP will decline by a total of 4.0–5.0% in 2020, which is slightly less than assumed in July. This is primarily because export dynamics from the beginning of 2020 have turned out to be better than expected.

In 2021, Russia's economy is expected to recover, growing by 3.0–4.0%. In 2022 and 2023, GDP is forecast to gain 2.5–3.5% and 2.0–3.0% respectively. The path of economic growth will largely depend on the process of budget consolidation to take place further on, coronavirus pandemic trends in Russia and abroad, and the specifics of the rebound in private demand amid potential changes in households' and businesses' behaviour. The earlier key rate reduction will continue to support the economy both this year and in 2021.

Fourth, when making its key rate decisions in September–October, the Bank of Russia factored in that **disinflationary risks prevail over proinflationary ones** over the medium-term forecast horizon. Disinflationary risks to the baseline scenario are mostly associated with further coronavirus spread trends in Russia and abroad, the scale of possible anti-pandemic measures and their impact on economic activity, as well as the recovery pace of the Russian and global economies. Inflation may also be constrained by sustainable shifts in households' preferences and behaviour, including a potential consistent increase in their propensity to save.

However, according to Bank of Russia estimates, **short-term proinflationary risks slightly rose** compared to July. They are primarily associated with intensified volatility in global markets caused in part by a range of geopolitical events, which may affect exchange rate and inflation expectations. Proinflationary pressure may also arise due to temporarily remaining disruptions in production and logistics chains, as well as extra costs incurred by businesses to protect employees and consumers against the spread of the coronavirus.

The Bank of Russia also took into account that there is still uncertainty about long-term structural consequences of the coronavirus pandemic for the Russian and global economies, namely the scale of the decline in the Russian economy's potential. The global growth potential may also be materially affected by geopolitical factors, including rising trade tensions. In turn, the scale of the Russian economy's deviation from potential is the crucial factor influencing medium-term inflation trends.

Since fiscal policy also significantly impacts medium-term inflation, the Bank of Russia's baseline scenario relies on the fiscal policy trajectory presented in the draft Guidelines for Fiscal, Tax and Customs and Tariff Policy for 2021 and the 2022–2023 Planning Period.

Medium-term monetary policy. If the situation develops in line with the baseline forecast, the Bank of Russia will consider further key rate cuts at upcoming Board of Directors meetings. Making its key rate decisions, the Bank of Russia will take into account actual and expected inflation dynamics relative to the target and economic developments over the forecast horizon, as well as risks created by internal and external conditions and how financial markets respond to them.

Throughout the forecast horizon, the Bank of Russia will pursue monetary policy so as to ensure the stabilisation of inflation close to 4%.

Effect of the decisions made on key rate expectations. After the publication of MPR 3/20, market participants did not change significantly their expectations regarding the key rate, mostly assuming a potential further decrease in the key rate later on.

Following the Board of Directors' meeting in July when the key rate was cut by 25 bp to 4.25% p.a., the Bank of Russia announced in its signal that it will explore the need for further key rate reduction if the situation develops in line with the baseline forecast. In these conditions, analysts and financial market participants mostly continued to expect the key rate to be decreased further in September, to 4.00% p.a., and to be kept at this level through 2020 and in 2021 H1.

However, closer to the September meeting of the Bank of Russia Board of Directors, market participants changed their general opinion, expecting the key rate to be maintained at 4.25% p.a. in September. This opinion remained the same by the moment of the Board of Directors' meeting in October. This was largely the result of the intensified impact of short-term proinflationary factors compared to July, which was associated with the realisation of pent-up demand after the lockdown and the ruble's weakening in late August – September.

Moreover, the uncertainty over the coronavirus spread in Russia and abroad also increased.

Following its meetings in September and October, the Bank of Russia Board of Directors kept the key rate at 4.25% p.a., while giving the signal that it will explore the need for further key rate reduction at its upcoming meetings, provided that the situation unfolds in line with the baseline forecast.

In its communication regarding the decisions made by the Board of Directors in September and October, the Bank of Russia emphasised diverse trends in inflation dynamics and an increase in households' and businesses' inflation expectations, certain volatility in financial and commodity markets, including due to geopolitical factors and the worsening epidemiological situation, the decelerated recovery of the Russian economy, the prevalence of medium-term disinflationary risks, and a slight rise in short-term proinflationary risks.

In this context, financial market participants and analysts started to expect a further key rate reduction to be approved later on. Some analysts assumed that the key rate might be decreased slightly at the end of 2020, others – in early 2021. Conversely, given the unstable situation in financial markets, expectations derived from money market indicators did not rule out a slight increase in the key rate in 2021.

According to analysts, the possibility of a further key rate reduction will depend on a range of factors, including the effect of the worsening epidemiological situation on domestic demand recovery prospects, inflation dynamics in 2021, and the overall situation in financial and commodity markets which is also affected by geopolitical factors.

3.2. SYSTEM OF MONETARY POLICY INSTRUMENTS AND OTHER MONETARY POLICY MEASURES

Banking sector liquidity. The structural liquidity surplus contracted on average across required reserve averaging periods from 1.9 trillion rubles in July–August to 1.8 trillion rubles in September–October 2020. Although expanding considerably more slowly than in the previous months, the amount of cash in circulation still remained the major contributor to the outflow of liquidity. Another key factor was the increased amount of required reserves, including as a result of the revaluation of credit institutions' FX liabilities.

Cash in circulation. The rise in the amount of cash in circulation has slowed down, and common seasonal dynamics are starting to normalise gradually.

Demand for cash is still expected to gradually decrease to its pre-pandemic levels as economic activity returns to normal, yet this process will shift to 2021. Therefore, the forecast regarding the rise in the amount of cash in circulation in 2020 was upgraded from 1.4–1.6 to 1.9–2.1 trillion rubles.

Budget account operations. In July–September 2020, the impact of budget operations on the banking sector liquidity was close to neutral. Budget revenues from the payment of the main taxes continued to recover gradually. In addition, a number of major companies transferred dividends to the budget in August. Concurrently, there was a seasonal decrease in budget spending.

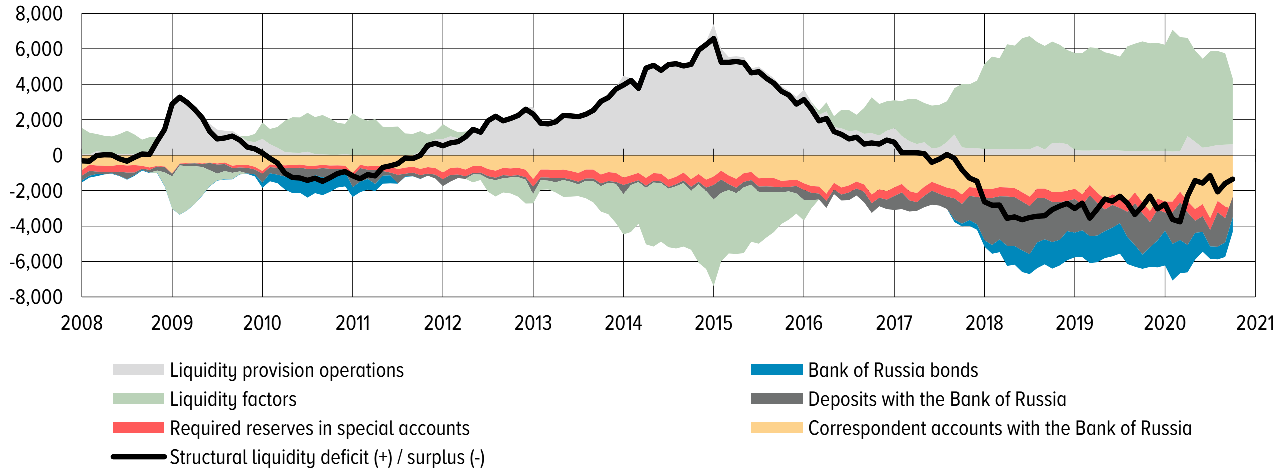
For the Ministry of Finance to achieve its 2020 target for borrowing and financing the excess of the general government's expenditure over its revenue, it significantly expanded its offerings of federal government bonds (OFZ). However, the impact of these operations on liquidity was almost fully offset by the rise in banks' outstanding amounts on Federal Treasury operations to place temporarily available budgetary funds.

The forecast of the structural liquidity surplus for the end of 2020 was downgraded from 1.4–2.0 trillion rubles to 1.0–1.4 trillion rubles. This was associated with the upward adjustment of the estimated outflow of cash from banks and the announced additional FX sales in the domestic market as part of the Aeroflot' stock transaction.

Monetary policy instruments. The Bank of Russia continued to hold one-month fixed-rate repo auctions and one-year floating-rate repo auctions. Banks demonstrated no demand for these refinancing operations in July–September,

BANK OF RUSSIA BALANCE SHEET
(start of business, billions of rubles)

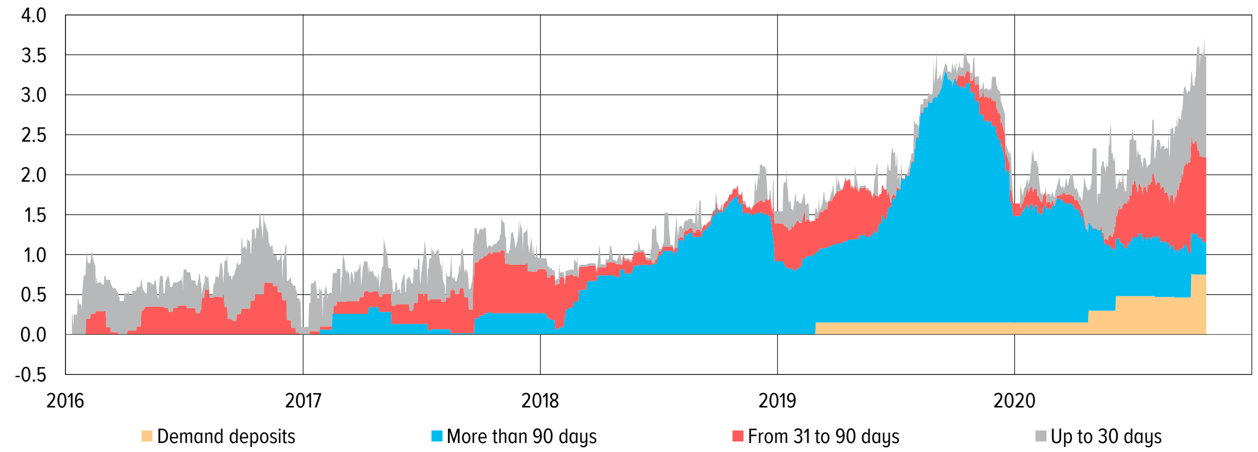
Chart 3.2.1



Source: Bank of Russia calculations.

BANKS' OUTSTANDING AMOUNTS ON FEDERAL TREASURY DEPOSITS, REPOS AND SWAPS
(trillions of rubles)

Chart 3.2.2



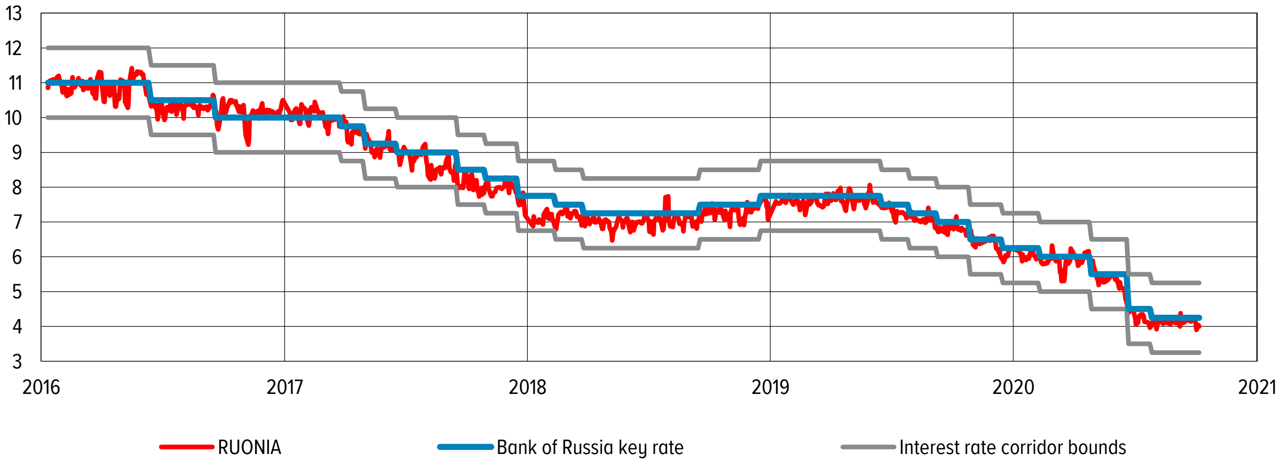
Sources: Federal Treasury, Bank of Russia calculations.

while attracting over 0.6 trillion rubles in October. The Bank of Russia increased the maximum amount of funding provided for one month from 0.4 to 1.0 trillion rubles, in order to enable credit institutions to offset the currently uneven distribution of liquidity. Although the extensive OFZ offerings by Russia's Ministry of Finance in the primary market for the financing of future budgetary spending were partially balanced by increased fund placements under Federal Treasury operations, these operations are not equivalent to banks to the full extent. In addition, the budget is expected to receive large transfers in October as a result of tax payments by banks' clients.

In terms of seasons, budgetary expenses are shifted to the last weeks of the year. Moreover, to be able to execute these operations, Russia's Ministry of Finance started to raise funds in advance. The subsequent financing of expenditure will result in an inflow of funds into bank accounts, which will enable credit institutions to repay their outstanding amounts under repos and neutralise their impact on liquidity.

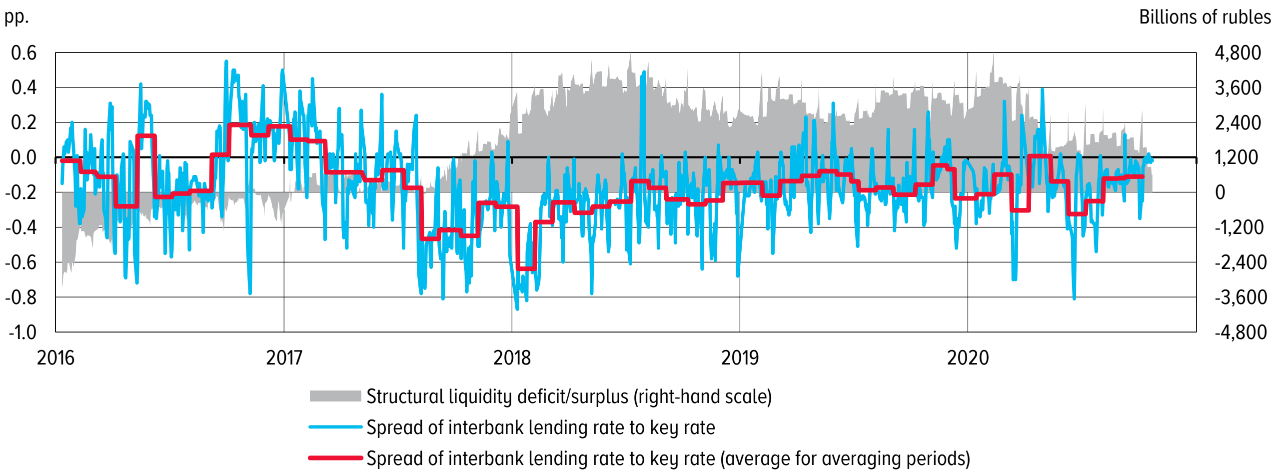
The Bank of Russia carries out daily analysis of budget expenses and factors in their dynamics in its banking sector liquidity forecast. Therefore, if credit institutions receive budgetary funds earlier or if they raise excess liquidity

RUONIA AND BANK OF RUSSIA INTEREST RATE CORRIDOR *Chart 3.2.3*
(% p.a.)



Source: Bank of Russia.

STRUCTURAL LIQUIDITY SURPLUS AND MONEY MARKET RATES *Chart 3.2.4*



Source: Bank of Russia calculations.

STRUCTURAL LIQUIDITY SURPLUS AND LIQUIDITY FACTORS *Table 3.2.1*
(trillions of rubles)

	July 2020	August 2020	September 2020
1. Liquidity factors	-0.1	-0.2	-0.1
– change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	0.1	0.0	0.0
– change in cash in circulation	-0.2	-0.1	-0.1
– Bank of Russia's interventions in the domestic FX market and monetary gold purchases	0.0	0.0	0.0
– regulation of banks' required reserves with the Bank of Russia	0.0	0.0	0.0
2. Change in free bank reserves (correspondent accounts)	-1.0	0.3	0.1
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	1.0	-0.5	-0.2
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	0.1	0.0	0.0
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	-2.1	-1.6	-1.4

** Including fiscal rule-based operations to buy (sell) foreign currency in the domestic FX market, settlements on Bank of Russia USD/RUB FX swaps, and other operations.*
Source: Bank of Russia calculations.

through repos, the Bank of Russia will absorb excess liquidity through deposit auctions. This will promptly balance the situation with liquidity at any point of time and ensure the efficient management of money market rates.

Achieving the operational objective of monetary policy. Short-term interbank lending rates in the money market stayed in the lower half of the interest rate corridor close to the Bank of Russia key rate. The average spread equalled -16 bp in Q3 (vs -13 bp in Q2), fluctuating from -54 to +13 bp (vs from -81 to +39 bp in Q2).

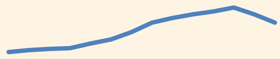
In July, as market participants expected a further reduction in the key rate, this put a downward pressure on interest rates. Nonetheless, this pressure decreased against June, since market participants expected a smaller step of key rate reduction. The key rate was not revised in August–September, and therefore, this factor did not impact the behaviour of market participants. As a result, the average spread shrank, getting close to the values of those averaging periods when the key rate was not expected to go down either. A certain upward pressure on interbank lending rates was exerted by the outflow of liquidity from banks resulting from increased OFZ placements by Russia's Ministry of Finance. This factor was offset by the inflow of liquidity under Federal Treasury operations, yet the distribution of funds among market participants occurred with a certain time lag. Consequently, interest rates were rising on certain days.

BOX

ON THE IMPACT OF DEMAND- AND SUPPLY-SIDE SHOCKS ON THE HOUSING MARKET IN 2020

The appreciable negative shock induced by the coronavirus pandemic also affected the dynamics of housing construction in Russia, entailing a temporary, yet a considerable annual decline in the commissioning of housing, specifically by 5.5% over the first eight months of 2020. Extensive government support measures at both the federal and regional levels, primarily the preferential 6.5% mortgage programme, limited the contraction of the housing market. Demand for mortgage lending was also supported by the substantial easing of lending conditions as the Bank of Russia transitioned to accommodative monetary policy. In the next 12 months, the situation in housing construction will largely depend on further decisions regarding government measures to support demand for housing, as well as the capability of the construction industry to proportionately increase the commissioning of residential real estate.

REGIONS WITH THE HIGHEST/LOWEST HOUSING AFFORDABILITY IN 2020 Q2* *Table 1*

Ranking**	Region	Equivalent of average monthly money income, sq.m***	Dynamics over 2017 Q1 – 2020 Q2
Regions with the highest housing affordability			
1 (1)	Yamalo-Nenets AA	1.24 (1.24)	
2 (2)	Khanty-Mansi AA	0.98 (0.99)	
3 (4)	Republic of Daghestan	0.82 (0.81)	
4 (3)	Kabardino-Balkarian Republic	0.80 (0.93)	
5 (6)	Kamchatka Territory	0.76 (0.78)	
Regions with the lowest housing affordability			
76 (75)	Zabaikalye Territory	0.41 (0.43)	
77 (77)	Saint Petersburg	0.40 (0.41)	
78 (78)	Primorye Territory	0.38 (0.41)	
79 (79)	Moscow	0.36 (0.38)	
80 (80)	Republic of Crimea	0.33 (0.35)	

* The indicator is calculated for the moving year.
** Values in brackets show the ranking as of 2019 Q4. Green colour is used for the regions which had improved their ranking by 2019 Q4, and red colour – for those with worsened ranking.
*** Values in brackets show the level of housing affordability as of 2019 Q4. In the regions shown in green the level of housing affordability had improved by 2019 Q4, and in the regions shown in red it had deteriorated.
Sources: Rosstat, Bank of Russia calculations.

The key demand-side factor hindering activity in the housing market was the slump in household real disposable income (by 8.4%[1]) in Q2 and the decreased affordability of housing (in more than 80% of Russian regions). On balance in 2019, average per capita income equalled the cost of 6.8 sq m of housing in the primary market; while over the 12 months[2] from 2019 Q3 through 2020 Q2, this indicator was 6.2 sq m of housing. Over the period from 2019 Q3 through 2020 Q2, housing was least affordable on average in the largest cities Moscow and Saint Petersburg, as well as in the Primorye Territory, the Republic of Crimea, and the Zabaikalye Territory. Moreover, all these regions also recorded a decrease in the affordability of housing over the past several quarters (Table 1).

Nonetheless, the real annual growth of households' expenses to purchase real estate (primarily, housing) remained in positive territory throughout 2020 H1. In 2020 Q1, demand for real estate was supported by a significant rise in real wage. In addition, households were considering alternative ways to make savings and investments, including in real estate, because of higher uncertainty and the ruble's weakening.

As a considerable part of households shifted to working from home and self-isolation in Q2, this spurred demand for real estate, including in the countryside and resort regions since overseas tourism options were limited. Moreover, according to the survey by the financial portal Bankiros.ru,[3] the majority of potential housing buyers, which is about 70% of respondents, opted for mortgage loans to purchase real estate. The new government programme to subsidise mortgage rates (6.5% p.a.), which is unprecedented in terms of the coverage of potential borrowers, was a key factor pushing up demand for mortgage loans in summer. It was largely owing to this programme that mortgage market participants' activity rose to its record highs by mid-2020, after a certain decline in April–May. In August, loans granted by banks exceeded 390 billion rubles (over the previous two years, the average monthly value of this indicator approximated 250 billion rubles). By the end of August, the annual growth of the loan portfolio[4] reached 16.6%, erasing the most part of its decline over previous months (Chart 2).

Overall, the coverage of households by preferential lending programmes considerably expanded in 2020. The preferential 6.5% mortgage lending programme was preceded by two new preferential mortgage lending programmes launched at the beginning of the year, specifically the Far Eastern Mortgage and Rural Mortgage programmes. As a result, by mid-2020, over one-third of all new mortgage loans were issued under the preferential programmes (Chart 3). The preferential mortgage lending programmes had a significant effect on the situation in the mortgage market in 2020. In the first place, they became an important contributor to the decrease in average market rates recorded in the middle of the year. As assessed by the Bank of Russia, the sharp increase in the portion of preferential loans in the turnover of the mortgage market accounted for nearly a half of the reduction in the average market rate in May–June. Furthermore, the preferential mortgage lending programmes enabled borrowers to receive larger loans, which also shifted the average market loan amount upwards. However, preferential loans only partially transformed into higher demand in the housing market, while the other part of them replaced loans granted on market conditions. According to some experts, mortgage borrowers decreased their activity in April–May, expecting the launch of the preferential 6.5% mortgage lending programme. Thus, during the period of declining incomes and increased uncertainty, the preferential mortgage lending programmes improved the affordability of new housing for certain groups of population.

Demand for mortgage loans was also supported by the substantial easing of lending conditions, including both price conditions (owing to the decrease in average market rates in the Russian economy after the Bank of Russia transitioned to accommodative monetary policy) and non-price conditions (as a result of the increase in loan maturities and maximum loan amounts). Moreover, a whole range of regions implemented additional measures to prop up demand for housing, such as regional subsidies to purchase housing, programmes to subsidise mortgage rates for individual groups of households, programmes supporting individual housing construction, low-rise construction development programmes, and others.

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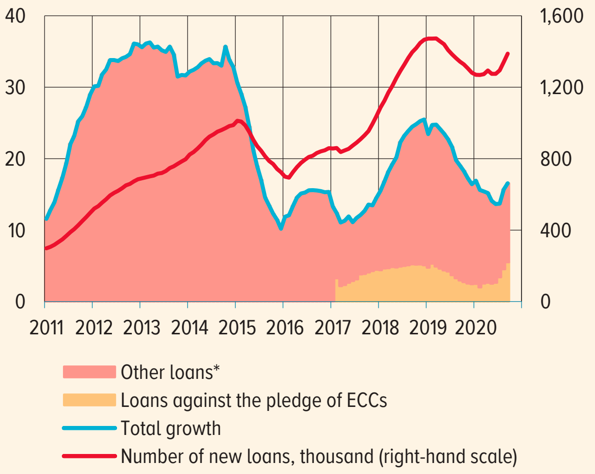
[1] *According to Rosstat's adjusted data.*

[2] *The 12-month measure is used due to a very uneven distribution of household income over the year.*

[3] *The survey was carried out online from 1 April to 15 June 2020 among 3,480 respondents from the majority of Russian regions, www. bankiros.ru.*

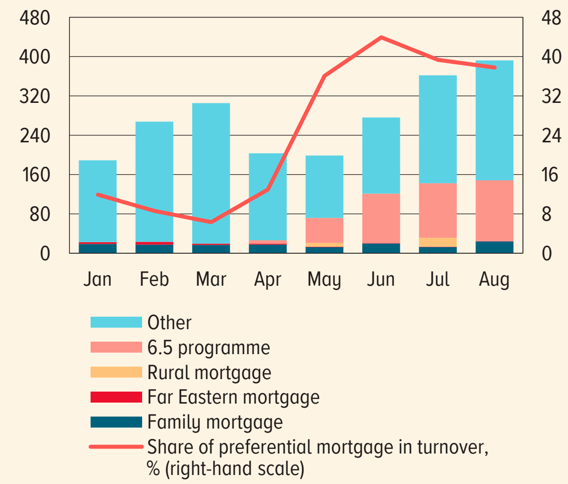
[4] *The portfolio of loans granted by banks; net of mortgage claims acquired.*

ANNUAL GROWTH OF MORTGAGE LOAN PORTFOLIO *Chart 1*
(% change on the same month of the previous year, AFCR)



** Data on loans issued against the pledge of ECCs are available only since 2016; therefore, the growth of loans issued against the pledge of ECCs is not excluded from 'Other loans' item before 2017.*
Source: Bank of Russia.

MORTGAGE LENDING MARKET TURNOVER IN 2020 *Chart 2*
(billions of rubles)



Sources: Bank of Russia, DOM.RF, Ministry of Finance, Bank of Russia estimates and calculations.

As a result, all these measures implemented to support demand, including both system-level and occasional ones, largely offset the adverse effect of declining incomes on housing sales. According to the Federal Service for State Registration, Cadastre and Cartography (Rosreestr), the annual growth rate of the number of registered equity construction contracts (ECCs) in the primary market shifted to positive territory already in August. However, the supply of new housing was limited over this period, which created possibilities for raising prices. The capacities to expand the commissioning of new housing were limited due to the imposed anti-pandemic measures. They suspended the registration of real estate in many Russian regions in late March – May and froze the construction of apartment buildings in Moscow and the Moscow Region from 13 April until 1 May, due to which the deadlines for the commissioning of a number of houses were postponed. In addition, measures affecting economic activity in Russia and its trading partners caused temporary interruptions in construction material deliveries due to disruptions in production and logistics chains, which also hindered activity in the construction industry.

If the accelerated growth of mortgage lending continues amid limited housing supply, this may contribute to the upward trend of housing prices, thus reducing the positive effect of the decrease in mortgage rates for improving the affordability of residential real estate. Moreover, it is essential to take into account that the preferential mortgage programme, although being a very reasonable and timely measure to support demand for housing in the extraordinary conditions of the pandemic, does not only increase the number of housing buyers, but also partially moves potential purchases from future periods to 2020.

In the next 12 months, the situation in housing construction will largely depend on further decisions regarding government measures to support demand for housing, as well as the capability of the construction industry to proportionately increase the commissioning of residential real estate.

The above and other issues are covered in detail in the analytical note *Housing Construction* (October 2020).

ANNEXES

ECONOMIC SITUATION IN RUSSIAN REGIONS

Amid the acceleration of country-wide inflation in July–September, its regional heterogeneity remained almost unchanged. The observed regional differences in price growth rates were associated with the uneven cancellation of the earlier imposed anti-pandemic restrictions, varying periods and amounts of the supply of new harvest to the market, the geography of the deliveries of imports, and the specifics of the structure of consumer spending. The economic revival continuing across all federal districts from June (according to surveys) slowed down in August–September and discontinued in October everywhere, except the North-Western region. According to the monitoring of enterprises, the economic recovery has been most active in recent months in the North Caucasus where the government support measures had the most significant effect on the economy. The increase in business expectations regarding output and demand slowed in August–September across all federal districts. In October, their expectations worsened in the majority of federal districts.

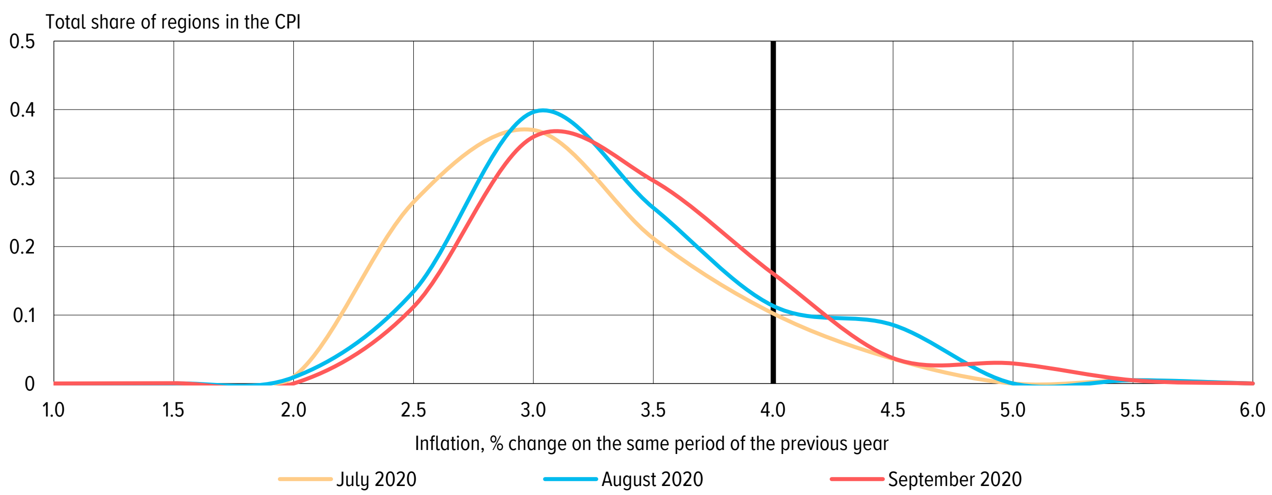
INFLATION AND PRICE EXPECTATIONS

Distribution of regions by inflation level

In July–September, the majority (76 out of 85) of the constituent territories of the Russian Federation recorded a pick-up in annual inflation. Over the three months, inflation sped up most notably in the Southern Federal District (FD), predominantly due to the stronger acceleration of food price growth. Inflation rose the least in July–September in the Far East where food price growth slowed down.

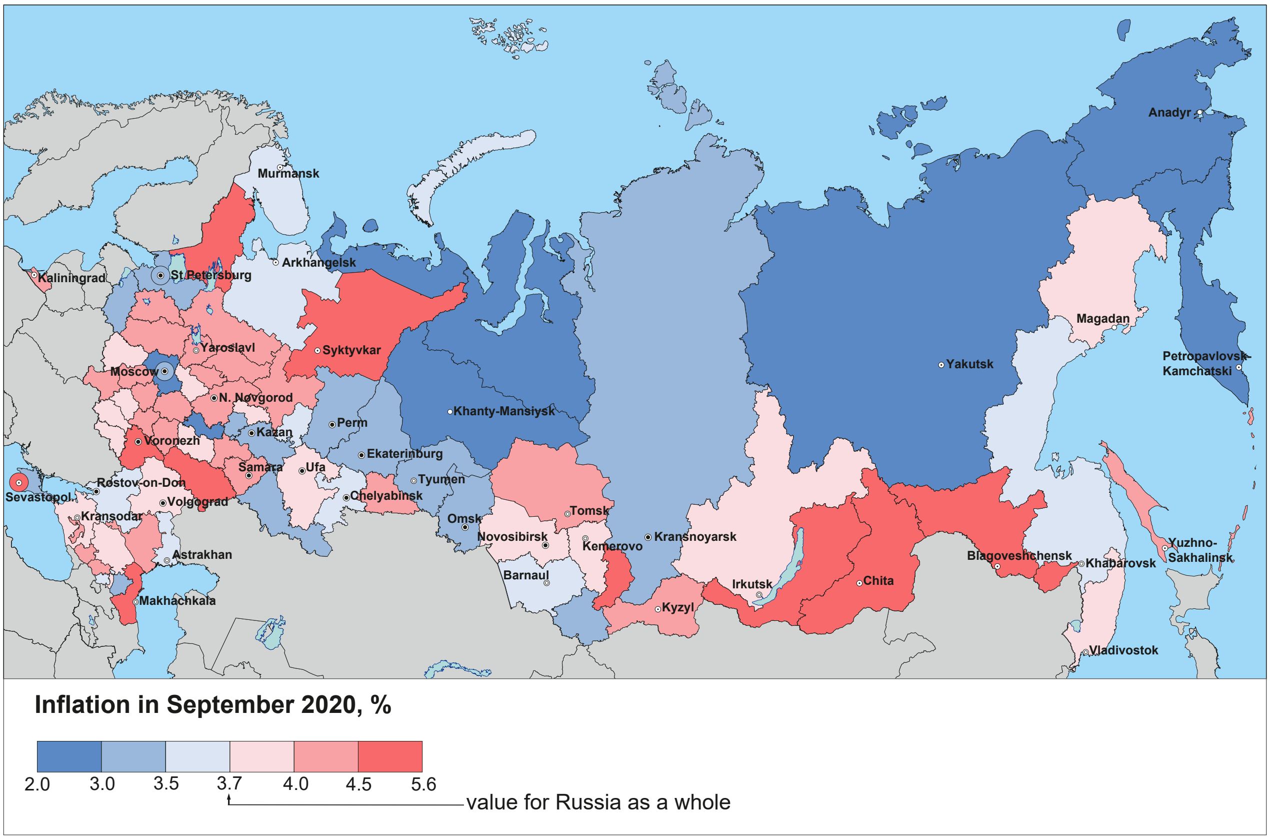
In September, annual inflation in Russian regions varied from 2.0% (the Chukotka Autonomous Area (AA) to 5.6% (the Amur Region) (Chart 2). The regional heterogeneity of inflation and the pattern of its distribution remained almost unchanged in July–September (Chart 1). The group of

DISTRIBUTION OF REGIONS BY ANNUAL INFLATION* *Chart 1*



** Data for the Tyumen and Arkhangelsk Regions incorporate data for autonomous areas.*
Source: Rosstat, Bank of Russia calculations.

INFLATION IN THE REGIONS IN SEPTEMBER 2020 *Chart 2*
(%)



Source: Rosstat.

constituent territories with the highest inflation rates was diverse in September, comprising the southern regions of the Far East and individual regions of the European part of Russia. Inflation rates were the lowest in many northern regions that may be characterised by a time-lag response of prices to the country-wide proinflationary factors observed in recent months, as well as in the Moscow agglomeration[1] where price growth is limited because of high competition in the consumer market.

Food inflation

In July–September, food inflation accelerated in 60 out of 85 constituent territories of Russia. The rise in inflation was most significant in many regions of the Southern FD, including in Sevastopol, the Republic of Crimea and the Republic of Adygeya where price growth sped up by over 1.5 pp. Faster food inflation in the south of Russia, just as across the country in general, was mostly driven by prices for fruit and vegetables. Price growth in this food category was more notable in many southern regions than on average across Russia because of the stronger effect of last year's low base.

Food inflation slowed down in July–September predominantly in the constituent territories of the Far East and in several Siberian regions. Fruit and vegetable inflation was the major contributor to this deceleration. In addition, some constituent territories also recorded a slower rise in prices for milk and meat products. The growth rates of fruit and vegetable prices in these regions also trended down owing the increased harvest of local agricultural producers, as well as the resumption of vegetable supplies from China – in the Far East. The slowdown of inflation for milk and meat products was also associated with the expanded supply from local producers.

[1] *Moscow and the Moscow Region*

Non-food inflation

Non-food inflation sped up in July–September in 81 out of 85 constituent territories of Russia. Regional differences in non-food inflation dynamics were mostly associated with the varying growth rates of car prices having a large weight in the CPI structure. Car prices rose most notably in Siberia. In the first place, this was caused by the realisation of pent-up demand since the easing of restrictions in the majority of the Siberian regions started later than across Russia in general. Moreover, the second stage of the cancellation of restrictions allowing the reopening of large retailers started in 11 out of the 12 regions of the Siberian FD exactly in July–September. Another contributor was the country-wide factor, specifically the weaker ruble.[2]

Non-food inflation slowed down in July–September in the Jewish AA, the Stavropol Territory, the Republic of Kalmykia and the Chukotka AA. In the Stavropol Territory and Kalmykia, this deceleration was associated with the slower growth of car prices due to sluggish demand. Another factor in Kalmykia was the effect of last year's high base. The Jewish AA recorded a slower rise in prices for tobacco products, knitwear and construction materials, and the Chokotka AA – in prices for perfume and beauty products, which could be associated with the impact of local factors on the regional markets of these goods.

Inflation in the services sector

Inflation in the services sector was changing diversely across regions in July–September. Over the three months, inflation sped up in 40 out of 85 constituent territories and slowed down in 44 of them. Inflation in the services sector accelerated the most in the regions of the North-Western FD. Utility services were the major contributor to this trend since the indexation of utility rates in a range of regions in the North-Western FD was above the Russian average. Furthermore, many tourist destinations of this federal district (the Kaliningrad and Leningrad Regions, and the Republic of Karelia) recorded a considerable rise in prices for sanatorium and health services associated with increased demand after the anti-pandemic restrictions were lifted.

In July–September, inflation in the services sector slowed down most notably (by over 1.5 pp) in the Nenets AA, the Sakha (Yakutia) Republic and the Krasnoyarsk Territory. These regions recorded a slower rise in air fares. Since air transportation services account for a considerable portion in the CPI due to the geographical remoteness of these regions, this slowdown also became a major contributor to the overall deceleration of inflation in the services sector. The Nenets AA and the Krasnoyarsk Territory also reported a significantly slower rise in prices for communication services, and Yakutia – in railway fares.

Price expectations

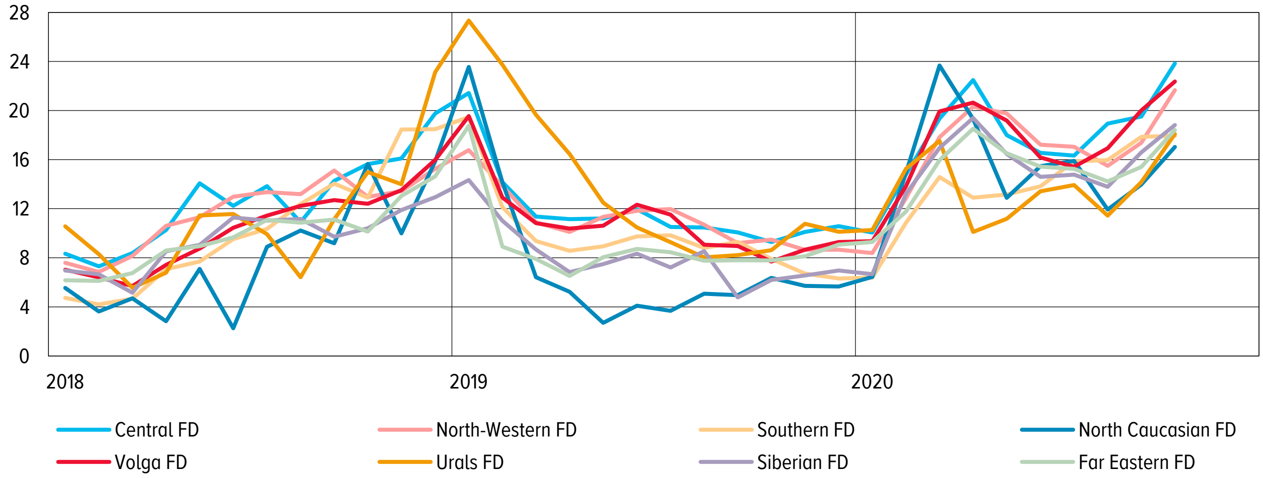
After a certain stabilisation in June–August, the price expectations of businesses participating in the Bank of Russia's monitoring trended up in September–October[3] across all industries and federal districts (Chart 3). Companies mentioned rises in input prices largely caused by the weaker ruble as the key factor of their increased price expectations. Over August–October, businesses' price expectations, broken down by region, rose in 57 out of 82 constituent territories (the Tyumen and Arkhangelsk Regions were taken into account together with the autonomous areas). Expectations increased the most in the central part of Russia, the North-West, and the Volga Region, where the weaker ruble affected businesses' expectations to a larger extent than across the country in general. This was because of companies' cost structure, since a lot of manufacturers, including in the automobile industry, operating in these regions have a large portion of imported components in their cost structure. The final consumption structure in the central part of Russia and in many regions of the North-West includes a larger portion of imports. This is the reason why the weakening

[2] *For more details regarding country-wide inflationary factors, see Section 2 'Inflation and inflation expectations'.*

[3] *Hereinafter, the month indicates when the questionnaires were collected; the reporting month is the previous one.*

BUSINESS PRICE EXPECTATIONS
(balance of responses, %)

Chart 3



Source: monitoring of enterprises conducted by the Banks of Russia.

of the ruble had a stronger effect on trade companies' expectations in these regions. Expectations in many southern regions of the European part of Russia either trended down, or rose less than on average across Russia. This was due to the improved estimates of this year's harvest (in summer, agricultural producers in many southern regions had negative expectations regarding the harvest because of unfavourable weather conditions).

CORPORATE LENDING

Corporate lending conditions

According to the Bank of Russia's quarterly survey of credit institutions, price lending conditions of banks continued to ease in 2020 Q3 across all federal districts and the country in general.[4] Moreover, for the first time since 2019 Q4, the majority of federal districts (the North-Western, Southern, North Caucasian, Urals and Siberian FDs) recorded an easing of non-price lending conditions as well. In three federal districts (the Central, Volga and Far Eastern FDs), non-price lending conditions remained unchanged. Despite the overall easing of lending conditions, they were still assessed as tight in the majority of regions (in 54 out of the 68 regions surveyed) and across all federal districts, except the Urals FD where lending conditions were assessed as neutral.

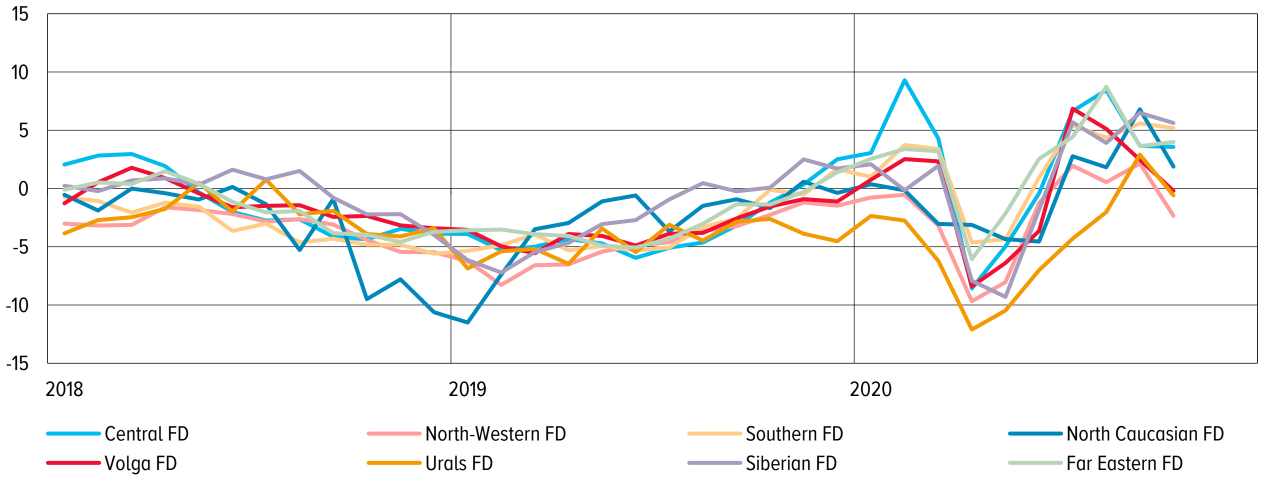
According to the monitoring of companies, lending conditions were improving more slowly in August–September in the majority of federal districts (Chart 4). In October, companies' opinions regarding bank lending conditions worsened across all industries, and most significantly in mining and quarrying. As compared with all other industries, trade and transportation enterprises assessed changes in lending conditions in August–October better, just as in the previous months. These sectors are on the list of the hardest hit by the coronavirus pandemic and, therefore, may qualify for government aid, including preferential lending. Overall, the balance of responses regarding changes in lending conditions in October remained positive in the majority of key industries. Negative assessments were only given in construction and in mining and quarrying. Construction companies' opinions regarding bank lending conditions remain worse than in all other industries beginning from late 2018, when the industry started to shift to the new rules for equity housing construction using project finance and escrow accounts.[5]

[4] *For more details regarding changes in monetary conditions across Russia in general, see Section 1.1 'Current situation'.*

[5] *For details about the situation in construction, see the analytical note Housing Construction (October 2020).*

ASSESSMENT OF CHANGES IN LENDING CONDITIONS BY BUSINESSES
(balance of responses, %)

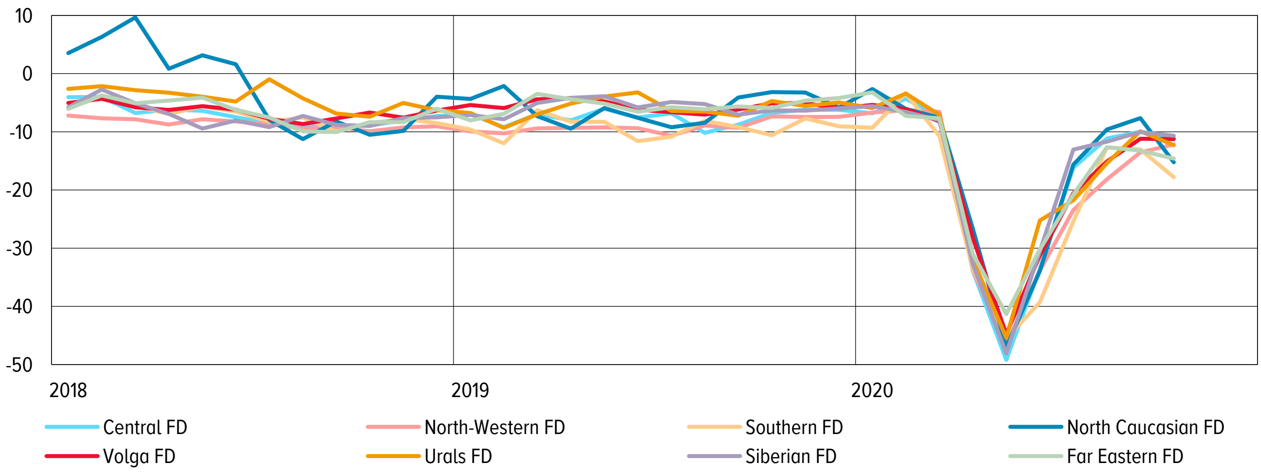
Chart 4



Source: monitoring of enterprises conducted by the Banks of Russia.

ASSESSMENT OF CHANGES IN ECONOMIC SITUATION BY BUSINESSES
(balance of responses, %)

Chart 5



Source: monitoring of enterprises conducted by the Banks of Russia.

ECONOMIC ACTIVITY

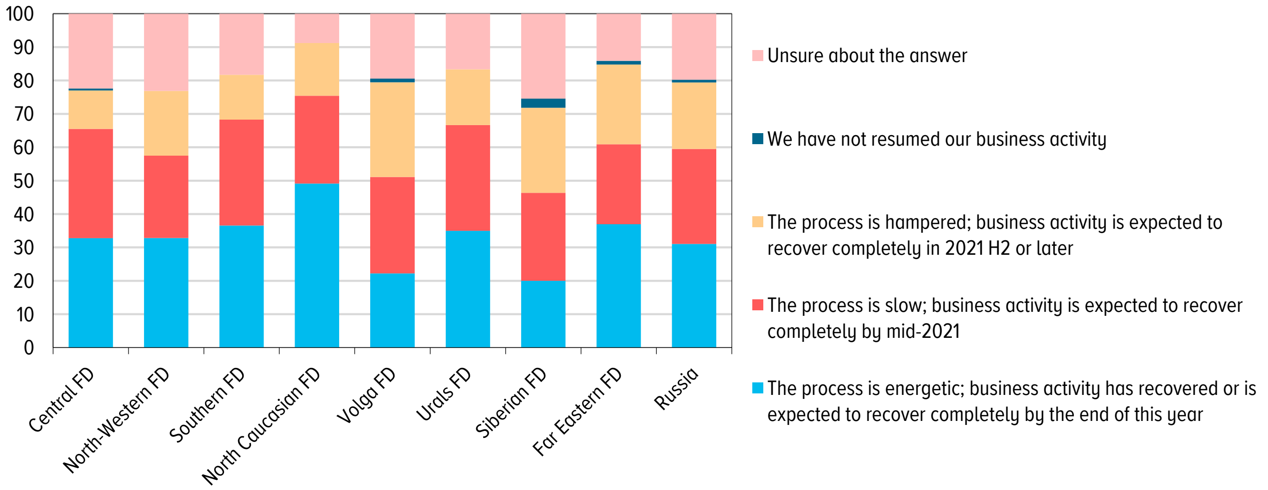
Production activity

In August–October, opinions about the economic situation were improving more slowly across all federal districts (Chart 5). Economic recovery slowed down everywhere due to country-wide factors, including the exhausted effects of pent-up demand and government support measures. This slowdown in economic activity was rather even across industries. In August–October, agricultural enterprises assessed changes in the economic environment slightly better than other industries. In agriculture, the improvement of companies' opinions might be associated with increased external demand for a range of products. Construction companies gave notably worse assessments of economic changes, compared with other industries.

According to surveys, business was bouncing back most actively in the North Caucasus. By October,[6] 49% of companies in the North Caucasian FD reported the complete recovery of their business or expected its recovery by the end of the year, with this portion exceeding 80% in certain

[6] *The survey was conducted on 7–13 October.*

DISTRIBUTION OF RESPONSES TO THE QUESTION 'IN WHAT WAY DOES YOUR BUSINESS RETURN BACK TO NORMAL?'* *Chart 6*
(%)



** Survey was held on 7-13 October 2020.*
Source: monitoring of enterprises conducted by the Banks of Russia.

regions (the Chechen Republic and the Republic of North Ossetia–Alania). Nonetheless, the total percentage of companies selecting this answer averaged 31% across Russia in general (Chart 6). The reason why the North Caucasus recorded the fastest economic revival could be the most extensive coverage by the government business support programmes launched in the regions of this federal district due to the spread of the coronavirus. Specifically, by the end of September,[7] government aid was provided to 31% of the surveyed companies in the North Caucasian FD, with this portion exceeding 60% in the Chechen Republic and the Stavropol Territory. On average, 21% of respondents across Russia were able to receive support, and 25% received preferential loans.

The recovery of companies' expectations[8] regarding output and demand changes slowed down in August–September across all federal districts, with the estimates of expectations unable to reach their early 2020 levels. In October, companies' expectations worsened in the majority of federal districts, except the Urals and the North West.

Consumer activity

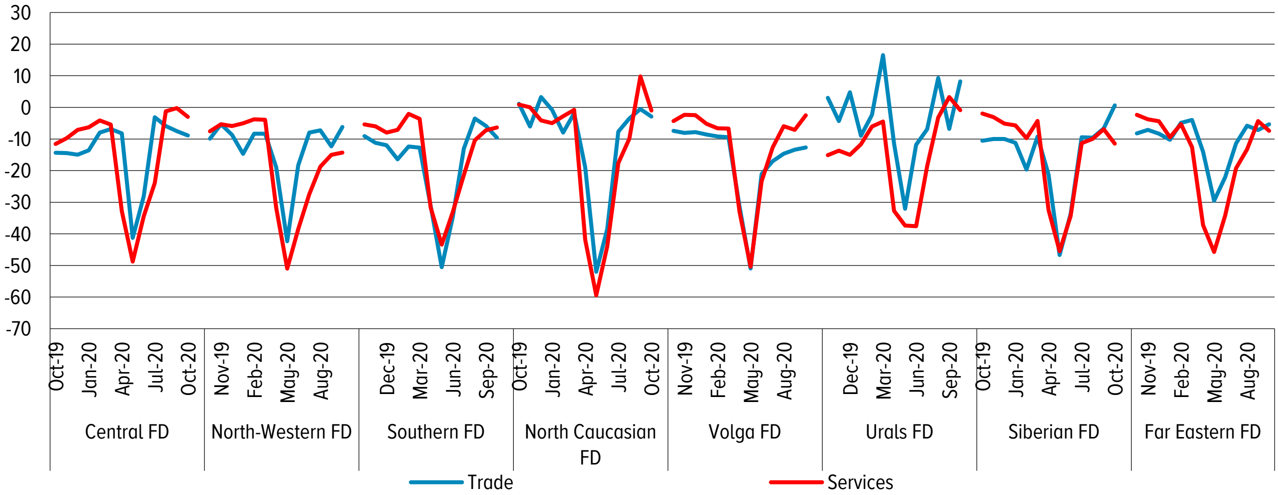
By August, consumer demand estimates reached the early 2020 readings across all federal districts. In September–October, demand estimates were changing diversely. Beginning from September, trade companies in a number of federal districts started to record a decline in demand (Chart 7). This could be because the effects of government payments to households and the realisation of pent-up demand were exhausted, and demand partially shifted to services, including in the tourism sector amid the holiday season and the resumption of flights to several foreign tourist destinations. In October, a number of federal districts also recorded a decrease in demand for services, which could be explained by the worsening epidemiological situation and the resulting changes in households' consumer behaviour. On average, trade and services companies' estimates of demand in August–October were the highest in the Urals and North Caucasus FDs. In the Urals, this could be associated with the later cancellation of restrictions, as a result of which the realisation of pent-up demand in the regions of this federal district happened in late summer – early autumn. As regards the North Caucasus, a more significant driver for consumer demand was government payments to households due to their lower incomes. Another reason could be the specifics of households' demographic structure: because of the larger average number of children in families in

[7] *The survey was conducted on 23–29 September.*

[8] *For the next three months.*

ASSESSMENTS OF DEMAND BY TRADE AND SERVICES COMPANIES
(balance of responses, %)

Chart 7



Source: monitoring of enterprises conducted by the Banks of Russia.

the North Caucasus, the per capita amount of payments for children there was higher than in the rest of Russian regions.

Investment activity

According to the Bank of Russia's quarterly business survey, investment activity was bouncing back in 2020 Q3 in the majority (7 out of 8) of the Russian federal districts, with estimates returning to the levels of 2020 Q1 almost everywhere. Investment activity estimates continued to decrease only in the Urals FD where investment contraction was recorded in agriculture, manufacturing, transportation, and trade. As regards Russia in general, the Q3 estimates of investment activity worsened only in agriculture. Nonetheless, their level still remains notably higher than in all other industries. Construction and transportation recorded the fastest revival of investment in Q3, following the most profound decline in these industries in Q2.

STATISTICAL TABLES

INTEREST RATES ON BANK OF RUSSIA OPERATIONS TO PROVIDE AND ABSORB RUBLE LIQUIDITY *Table 1*
(% p.a.)

Purpose	Instrument type	Instrument	Term	Frequency	As of 01.01.2019	From 17.06.2019	From 29.07.2019	From 09.09.2019	From 28.10.2019	From 16.12.2019	From 10.02.2020	From 27.04.2020	From 14.05.2020	From 22.06.2020	From 27.07.2020	General approach to rate-setting[1]
Liquidity provision	Standing facilities	Overnight loans; lombard loans; loans secured by non-marketable assets; FX swaps (ruble leg);[2] repos	1 day	Daily	8.75	8.50	8.25	8.00	7.50	7.25	7.00	6.50	6.50	5.50	5.25	Key rate + 1.00
		Loans secured by non-marketable assets[3]	From 2 to 549 days		9.50	9.25	9.00	8.75	8.25	8.00	7.75	7.25	7.25	6.25	6.00	Key rate + 1.75
	Open market operations (minimum interest rates)	Auctions to provide loans secured by non-marketable assets	3 months[3]	Monthly[4]	8.00	7.75	7.50	7.25	6.75	6.50	6.25	5.75	5.75	4.75	4.50	Key rate + 0.25
		Repo auctions	1 year[3]	Monthly	-	-	-	-	-	-	-	-				
			1 month		-	-	-	-	-	-	-	-	5.60	4.60	4.35	Key rate + 0.1
			1 week	Weekly[5]	7.75 (key rate)	7.50 (key rate)	7.25 (key rate)	7.00 (key rate)	6.50 (key rate)	6.25 (key rate)	6.00 (key rate)	5.50 (key rate)	5.50 (key rate)	4.50 (key rate)	4.25 (key rate)	Key rate
			From 1 to 6 days	Occasionally[6]												
		FX swap auctions (ruble leg)[2]	From 1 to 2 days													
Liquidity absorption	Open market operations (maximum interest rates)	Deposit auctions	From 1 to 6 days													
			1 week	Weekly[5]												
	Standing facilities	Deposit operations[7]	1 day	Daily	6.75	6.50	6.25	6.00	5.50	5.25	5.00	4.50	4.50	3.50	3.25	Key rate - 1.00

[1] From 4 June 2018, the interest rates on Bank of Russia operations with credit institutions are set as spreads to the key rate.
[2] From 23 December 2016, interest rates on the foreign currency leg equal LIBOR on overnight loans in US dollars or euros (depending on the currency of transactions).
[3] Operations conducted at a floating interest rate linked to the Bank of Russia key rate.
[4] Operations have been discontinued since April 2016.
[5] Either a repo or a deposit auction is held depending on the situation with liquidity.
[6] Fine-tuning operations.
[7] Until 16 May 2018, also demand deposits. From 17 May 2018, the Bank of Russia only conducts overnight deposit operations with credit institutions.
Source: Bank of Russia.

BANK OF RUSSIA OPERATIONS TO PROVIDE AND ABSORB RUBLE LIQUIDITY

(billions of rubles)

Table 2

Purpose	Instrument type	Instrument	Term	Frequency	Bank of Russia claims under liquidity provision instruments and liabilities under liquidity absorption instruments				
					As of 01.01.2019	As of 01.01.2020	As of 01.04.2020	As of 01.07.2020	As of 01.10.2020
Liquidity provision	Standing facilities	Overnight loans	1 day	Daily	8.1	0.0	0.0	0.0	0.0
		Lombard loans			0.0	0.0	0.0	0.0	0.0
		FX swaps			4.1	12.6	0.0	0.0	0.0
		Repos			3.6	0.0	16.7	0.0	0.3
		Loans secured by non-marketable assets	From 1 to 549 days		5.1	5.1	5.1	5.1	5.1
	Open market operations	Auctions to provide loans secured by non-marketable assets	3 months[1]	Monthly	0.0	0.0	0.0	0.0	0.0
		Repo auctions	1 year		-	-	-	5.3	5.3
			1 month		-	-	-	0.0	0.0
			1 week	Weekly[2]	0.0	0.0	0.0	0.0	0.0
			From 1 to 6 days	Occasionally[3]			854.4	0.0	0.0
		FX swap auctions	From 1 to 2 days		0.0	0.0	0.0	0.0	0.0
Liquidity absorption	Open market operations	Deposit auctions	From 1 to 6 days		1,478.2	696.6	1,673.5	773.4	999.2
			1 week	Weekly[2]					
		Auctions for the placement of coupon OBRs	Up to 3 months	Monthly[4]	1,391.3	1,956.3	1,544.2	708.2	818.5
	Standing facilities	Deposit operations	1 day[5]	Daily	423.8	329.7	160.5	151.3	149.1

[1] Operations have been discontinued since April 2016.

[2] Either a repo or a deposit auction is held depending on the situation with liquidity.

[3] Fine-tuning operations.

[4] New issues of coupon OBRs are usually placed once a month, and after that they are placed on a weekly basis. If the reporting date falls on a weekend or holiday, the indicated amount of outstanding Bank of Russia coupon OBRs includes the accrued coupon interest as of the first working day following the reporting date.

[5] Before 16 May 2018, also demand deposits. From 17 May 2018, the Bank of Russia only conducts overnight deposit operations with credit institutions.

Source: Bank of Russia.

REQUIRED RESERVE RATIOS

Table 3

(%)

Liability type	Validity dates			
	01.12.2017 – 31.07.2018	01.08.2018 – 31.03.2019	01.04.2019 – 30.06.2019	From 01.07.2019[1]
Banks with a universal licence and non-bank credit institutions				
To households in the currency of the Russian Federation	5.00	5.00	4.75	4.75
Other liabilities in the currency of the Russian Federation				
To non-resident legal entities in the currency of the Russian Federation				
To households in foreign currency	6.00	7.00	7.00	8.00
To non-resident legal entities in foreign currency	7.00	8.00	8.00	8.00
Other liabilities in foreign currency				
Banks with a basic licence				
To households in the currency of the Russian Federation	1.00	1.00	1.00	1.00
Other liabilities in the currency of the Russian Federation				
To non-resident legal entities in the currency of the Russian Federation	5.00	5.00	4.75	4.75
To households in foreign currency	6.00	7.00	7.00	8.00
To non-resident legal entities in foreign currency	7.00	8.00	8.00	8.00
Other liabilities in foreign currency				

[1] Bank of Russia Ordinance No. 5158-U, dated 31 May 2019. See the press release published on the Bank of Russia website on 31 May 2019.
Source: Bank of Russia.

REQUIRED RESERVE AVERAGING RATIO

Table 4

Types of credit institutions	
Banks with a universal licence, with a basic licence	0.8
Non-bank credit institutions	1.0

Source: Bank of Russia.

REQUIRED RESERVES AVERAGING SCHEDULE FOR 2020 AND INFORMATION ON CREDIT INSTITUTIONS' COMPLIANCE WITH RESERVE REQUIREMENTS

Table 5

Averaging period to calculate a required reserves amount for a respective reporting period	Averaging period duration (days)	Memo item:		Actual average daily balances in correspondent accounts	Required reserves to be averaged in correspondent accounts	Required reserves recorded to their respective accounts
		Reporting period	Required reserves regulation period			
11.12.2019 – 14.01.2020	35	November 2019	13.12.2019 – 17.12.2019	2,526	2,428	617
15.01.2020 – 11.02.2020	28	December 2019	22.01.2020 – 24.01.2020	2,479	2,418	618
12.02.2020 – 10.03.2020	28	January 2020	14.02.2020 – 18.02.2020	2,474	2,398	613
11.03.2020 – 07.04.2020	28	February 2020	16.03.2020 – 18.03.2020	2,536	2,431	622
08.04.2020 – 12.05.2020	35	March 2020	14.04.2020 – 16.04.2020	2,685	2,605	665
13.05.2020 – 09.06.2020	28	April 2020	20.05.2020 – 22.05.2020	2,700	2,635	671
10.06.2020 – 07.07.2020	28	May 2020	15.06.2020 – 17.06.2020	2,636	2,570	656
08.07.2020 – 04.08.2020	28	June 2020	14.07.2020 – 16.07.2020	2,590	2,529	647
05.08.2020 – 08.09.2020	35	July 2020	14.08.2020 – 18.08.2020	2,632	2,578	659
09.09.2020 – 06.10.2020	28	August 2020	14.09.2020 – 16.09.2020	2,699	2,634	673
07.10.2020 – 10.11.2020	35	September 2020	14.10.2020 – 16.10.2020			
11.11.2020 – 08.12.2020	28	October 2020	16.11.2020 – 18.11.2020			
09.12.2020 – 12.01.2021	35	November 2020	14.12.2020 – 16.12.2020			

KEY ECONOMIC AND FINANCIAL INDICATORS *Table 6*

		September 2019	October 2019	November 2019	December 2019	January 2020	February 2020	March 2020	April 2020	May 2020	June 2020	July 2020	August 2020	September 2020
Real sector														
Inflation	% YoY	4.0	3.8	3.5	3.0	2.4	2.3	2.5	3.1	3.0	3.2	3.4	3.6	3.7
GDP[1]	% YoY	1.5			2.1			1.6			-8.0			
GDP in current prices[1]	trillions of rubles	28.9			29.8			25.3			23.3			
Output by key activity types	% YoY	3.9	4.0	1.8	2.1	1.7	3.5	0.6	-10.0	-10.6	-8.1	-5.7	-5.2	
Industrial production	% YoY	4.9	4.3	1.4	2.7	1.5	4.8	2.4	-4.5	-7.9	-7.1	-5.9	-4.2	-5.0
Agricultural production	% YoY	5.4	5.0	5.7	5.6	2.9	3.1	3.0	3.1	3.2	3.0	4.2	4.1	1.4
Construction	% YoY	1.0	1.1	0.3	0.4	1.0	2.3	0.1	-2.3	-3.1	-0.1	-0.2	-0.6	-0.1
Fixed capital investment[1]	% YoY	1.7			2.3			1.2			-7.6			
Freight turnover	% YoY	1.4	0.1	-3.2	-2.7	-5.1	-1.0	-7.1	-6.9	-6.5	-4.0	-1.6	1.3	-0.4
PMI Composite Index	% SA	51.4	53.3	52.9	51.8	52.6	50.9	39.5	13.9	35.0	48.9	56.8	57.3	53.7
Retail turnover	% YoY	0.9	1.9	2.6	1.8	2.7	4.7	5.7	-22.6	-18.6	-7.1	-1.9	-2.7	-3.0
Real disposable income[1]	% YoY	2.9			1.8			0.7			-8.4			-4.8
Real wage	% YoY	3.1	3.8	2.7	6.9	6.5	5.7	5.9	-2.0	1.0	0.6	2.9	0.1	
Nominal wage	% YoY	7.2	7.7	6.3	10.1	9.1	8.1	8.6	1.0	4.0	3.8	6.4	3.7	
Unemployment rate	% SA	4.6	4.6	4.6	4.5	4.5	4.5	4.6	5.7	6.1	6.3	6.4	6.6	6.5
Banking Sector														
Broad money supply	% YoY, AFCR	8.0	7.9	8.3	7.6	8.0	7.9	9.1	9.6	9.3	10.4	11.1	11.7	
Money supply (M2)	% YoY	9.1	8.7	9.6	9.7	10.7	11.0	13.4	14.0	13.6	14.9	15.5	16.2	
Household deposits	% YoY, AFCR	9.4	9.2	9.8	9.8	9.8	9.0	7.3	6.4	6.4	7.2	7.3	6.8	6.6
in rubles	% YoY	8.9	8.6	10.0	9.9	10.8	10.8	10.7	9.9	9.8	10.9	11.3	10.6	11.0
in foreign currency	% YoY	11.3	11.7	9.6	9.8	6.3	2.3	-4.6	-6.2	-5.9	-6.7	-7.2	-6.5	-8.6
dollarisation	%	21.1	20.9	20.6	19.6	20.1	20.5	22.1	20.7	20.2	19.8	20.5	20.7	21.4
Loans to non-financial organisations	% YoY, AFCR	3.4	4.1	4.0	4.3	3.2	2.0	3.6	4.8	4.8	4.4	6.0	6.3	6.3
short-term (less than 1 year)	% YoY, AFCR	1.2	1.3	0.6	0.4	4.9	3.3	9.8	12.4	13.9	15.0	11.3	14.0	14.2
long-term (more than 1 year)	% YoY, AFCR	2.1	3.0	3.1	3.2	2.8	1.9	2.3	3.2	3.1	2.1	4.1	4.1	4.1
overdue loans	%	8.0	8.0	7.9	7.8	7.8	7.6	7.5	7.4	7.5	7.7	8.2	8.1	8.0
Household loans	% YoY, AFCR	20.7	19.7	18.6	18.5	17.9	17.8	17.7	14.6	13.0	12.6	13.1	13.2	13.4
housing mortgage loans	% YoY, AFCR	18.3	17.3	16.4	16.9	15.6	15.4	15.2	14.1	13.6	13.7	15.7	16.6	
unsecured consumer loans	% YoY	23.4	22.6	21.1	20.8	20.1	20.2	20.0	15.3	12.7	11.2	10.1	9.5	
overdue loans	%	4.7	4.6	4.5	4.3	4.4	4.5	4.5	4.6	4.7	4.7	4.8	4.8	4.7

Legend:
YoY – on corresponding period of previous year;
SA – seasonally adjusted;
AFCR – adjusted for foreign currency revaluation.
[1] Quarterly data.
Sources: Rosstat, IHS Markit, Bank of Russia calculations.

KEY ECONOMIC AND FINANCIAL INDICATORS:
BALANCE OF PAYMENTS *Table 7*

		2018 Q1	2018 Q2	2018 Q3	2018 Q4	2019 Q1	2019 Q2	2019 Q3	2019 Q4	2020 Q1	2020 Q2	2020 Q3[1]
Balance of payments[2]												
Urals crude price	% YoY	25.9	50.8	44.3	10.7	-3.7	-5.5	-16.9	-7.2	-22.6	-57.0	-29.6
USD/RUB exchange rate ('+' – ruble's strengthening. '-' – ruble's weakening)	% YoY	3.4	-7.5	-9.9	-12.1	-14.0	-4.3	1.4	4.3	0.0	-10.7	-12.2
Goods and services exports	% YoY	21.8	27.4	28.4	18.8	0.8	-6.7	-6.0	-7.7	-12.3	-32.5	-27.2
Goods and services imports	% YoY	19.0	8.2	-0.1	-2.9	-3.4	-1.2	5.7	9.8	1.4	-23.8	-21.6
Current account	**billions of US dollars**	**30.2**	**18.4**	**28.1**	**39.0**	**33.5**	**9.9**	**10.7**	**11.2**	**22.1**	**-0.5**	**2.5**
Balance of trade	billions of US dollars	44.0	45.5	47.8	57.7	47.0	39.4	37.9	41.0	32.4	15.3	17.0
Exports	billions of US dollars	101.6	108.9	110.6	122.9	102.6	101.4	103.3	112.5	88.6	69.3	76.9
Imports	billions of US dollars	57.5	63.4	62.7	65.2	55.7	62.0	65.4	71.6	56.2	54.0	59.9
Balance of services	billions of US dollars	-6.6	-7.7	-8.8	-6.9	-6.0	-9.0	-11.5	-9.7	-6.8	-2.3	-3.1
Exports	billions of US dollars	13.9	16.6	17.4	16.7	13.8	15.8	17.0	16.2	13.5	9.8	10.7
Imports	billions of US dollars	20.6	24.4	26.1	23.6	19.8	24.7	28.5	26.0	20.3	12.1	13.8
Balance of primary and secondary income	billions of US dollars	-7.2	-19.3	-11.0	-11.8	-7.5	-20.5	-15.7	-20.0	-3.5	-13.5	-11.4
Current and capital account balance	billions of US dollars	30.0	18.2	28.1	38.3	33.5	9.7	10.6	10.8	22.1	-0.7	2.4
Financial account excluding reserve assets (net lending (+) / net borrowing (-)	**billions of US dollars**	**12.7**	**9.8**	**24.9**	**31.0**	**12.3**	**-5.2**	**-7.2**	**-3.8**	**17.3**	**13.8**	**3.2**
Public sector	billions of US dollars	-6.6	11.1	2.9	1.3	-9.3	-6.2	-3.6	-3.8	0.4	1.4	-3.2
Private sector	billions of US dollars	19.3	-1.3	22.0	29.8	21.6	1.0	-3.6	0.0	16.8	12.4	6.3
Net errors and omissions	billions of US dollars	2.1	2.9	1.8	-4.7	-2.6	1.7	-1.9	0.8	0.2	1.6	-1.5
Change in reserve assets ('+' – increase. '–' – decrease)	**billions of US dollars**	**19.3**	**11.3**	**5.0**	**2.6**	**18.6**	**16.6**	**15.9**	**15.4**	**5.0**	**-12.9**	**-2.3**

[1] *Estimate.*
[2] *Signs according to BPM6.*

LIST OF PUBLICATIONS

Bank of Russia information and analytical commentaries released after the publication of MPR 2/20 on 3 August 2020[1]:

1. *Consumer price dynamics, No. 7 (55), July 2020 (12 August 2020)*
2. *Consumer price dynamics, No. 8 (56), August 2020 (10 September 2020)*
3. *Consumer price dynamics, No. 9 (57), September 2020 (12 October 2020)*
4. *Inflation expectations and consumer sentiment, No. 8 (44), August 2020 (26 August 2020)*
5. *Inflation expectations and consumer sentiment, No. 9 (45), September 2020 (24 September 2020)*
6. *Inflation expectations and consumer sentiment, No. 10 (46), October 2020 (26 October 2020)*
7. *Economy, No. 7, July 2020 (28 August 2020)*
8. *Economy, No. 8, August 2020 (23 September 2020)*
9. *Banking sector liquidity and financial markets, No. 7 (53), July 2020 (11 August 2020)*
10. *Banking sector liquidity and financial markets, No. 8 (54), August 2020 (10 September 2020)*
11. *Banking sector liquidity and financial markets, No. 9 (55), September 2020 (9 October 2020)*
12. *Russia's balance of payments, No. 3 (5), 2020 Q3 (15 October 2020)*
13. *Housing Construction. Analytical Note, No. 2 (3) (7 October 2020)*

[1] *The date in the brackets is the publication date on the Bank of Russia website.*

GLOSSARY

BALANCE OF PAYMENTS OF THE RUSSIAN FEDERATION

A statistical system reflecting all economic transactions between residents and non-residents of the Russian Federation, which occurred during the reporting period.

BANKING SECTOR LIQUIDITY

Credit institutions' funds held in correspondent accounts with the Bank of Russia in the currency of the Russian Federation, mainly to carry out payments through the Bank of Russia payment system and to comply with obligatory reserve requirements.

BANK OF RUSSIA KEY RATE

The principal instrument of the Bank of Russia's monetary policy. The Bank of Russia Board of Directors sets the rate eight times a year. Key rate changes influence lending and economic activities and make it possible to achieve the primary objective of the monetary policy. The rate corresponds to the minimum interest rate at the Bank of Russia's one-week repo auctions and to the maximum interest rate at the Bank of Russia's one-week deposit auctions.

CONSUMER PRICE INDEX (CPI)

Ratio of the value of a fixed set of goods and services in current prices to the value of the same set of goods and services in the previous (reference) period's prices. This index is calculated by the Federal State Statistics Service. The CPI shows changes over time in the overall price level of goods and services purchased by households for private consumption. The CPI is calculated using data on the actual structure of consumer spending, being therefore one of the key indicators of living costs. Additionally, the CPI possesses a number of properties facilitating its wide-spread application: simple and clear construction methods, calculation on a monthly basis and publication in a timely manner.

CORE INFLATION

An inflation indicator characterising its most stable part. Core inflation is measured using the core consumer price index (CCPI). The difference between the CCPI and the consumer price index (CPI) lies in the CCPI calculation method, which excludes the change in prices for individual goods and services subject to the influence of administrative and seasonal factors (certain types of fruit and vegetables, passenger transportation services, telecommunication services, housing and public utility services, motor fuel, etc.).

CREDIT DEFAULT SWAP (CDS)

A financial instrument enabling buyer to insure against a certain credit event (e.g., default) concerning a third party's financial obligations in exchange for regular payments of premia (CDS spread) to the CDS seller. The higher the paid premium, the more risky the obligations which served as the subject matter of the credit default swap.

DOLLARISATION OF BANK DEPOSITS (LOANS)

The share of deposits (loans) denominated in foreign currency in total banking sector deposits (loans).

FINANCIAL STABILITY

A financial system characterised by the absence of systemic risks which, once they have evolved, may impact negatively on the process of transforming savings into investment and the real economy. In the event of financial stability, the economy demonstrates better resilience to external shocks.

FLOATING EXCHANGE RATE REGIME

An exchange rate regime, under which the central bank does not set targets, including operational ones, for the level of or changes to the exchange rate, allowing it to be influenced by market factors. However, the central bank reserves the right to purchase foreign currency to replenish international reserves or to sell it should threats to financial stability arise.

INFLATION

A sustained increase in the overall price level of goods and services in the economy. Inflation is generally associated with changes over time in the cost of a consumer basket, i.e. a set of food products, non-food goods, and services consumed by an average household (see also 'Consumer price index').

INFLATION EXPECTATIONS

Economic agents' expectations about future price growth. Inflation expectations can be given by businesses, households, financial markets, and professional analysts. Driven by expectations, economic agents make their economic decisions and future plans, which include consumption, savings, borrowings, investment, and loan/deposit rates. Capable of producing a certain effect on inflation, inflation expectations constitute an important indicator for the monetary policy decision-making process.

INFLATION TARGETING

A monetary policy strategy governed by the following principles: the main objective of monetary policy is price stability; the inflation target is specified and declared; monetary policy influences the economy largely through interest rates under a floating exchange rate regime; monetary policy decisions are taken based on the analysis of a wide range of macroeconomic indicators and their forecast. The Bank of Russia seeks to set clear benchmarks for households and businesses, including through enhanced information transparency.

LIQUIDITY-ABSORBING OPERATIONS

Bank of Russia reverse operations to absorb liquidity from credit institutions. These are operations either to attract deposits or place Bank of Russia bonds.

MONETARY BASE

Total amount of certain cash components and credit institutions' funds in Bank of Russia accounts and bonds denominated in the currency of the Russian Federation. The monetary base in a narrow definition includes cash in circulation (outside of the Bank of Russia) and credit institutions' funds in accounts recording required reserves on funds attracted by credit institutions in the currency of the Russian Federation. The broad monetary base includes cash in circulation (outside of the Bank of Russia) and the total funds of credit institutions in Bank of Russia accounts and bonds.

MONEY SUPPLY

Total Russian Federation residents' funds (excluding general government's and credit institutions' funds). For the purposes of economic analysis, various monetary aggregates are calculated (M0, M1, M2, M2X).

MONEY SUPPLY IN THE NATIONAL DEFINITION (M2 MONETARY AGGREGATE)

The total amount of cash in circulation outside the banking system and funds of Russian Federation residents (non-financial and financial organisations (excluding banks) and households) in settlement, current and other demand accounts (including in bank card accounts), time deposits and other types of deposits in the banking system, denominated in Russian rubles, as well as interest accrued on them.

MSCI INDICES

A group of indices calculated by Morgan Stanley Capital International. Calculations are made for indices for individual countries (including Russia), global indices (for various regions, for advanced/emerging economies) and the 'world' index.

NEUTRAL RATE

The level of the key rate when monetary policy neither slows down nor spurs inflation.

REFINANCING OPERATIONS

Bank of Russia reverse operations to provide credit institutions with liquidity. They may be in the form of loans, repos or FX swaps.

REQUIRED RESERVE RATIOS

Ratios ranging from 0% to 20% are applied to reservable liabilities of credit institutions to calculate the standard value of required reserves. They are set by the Bank of Russia Board of Directors.

RUONIA (RUBLE OVERNIGHT INDEX AVERAGE)

A reference weighted interest rate on overnight ruble-denominated deposits in the Russian interbank market. It reflects the cost of unsecured loans of banks with minimum credit risk. To calculate RUONIA, the Bank of Russia applies the method elaborated by the National Finance Association in cooperation with the Bank of Russia based on the information on deposit transactions made between member-banks. The list of RUONIA member-banks is compiled by the National Finance Association and concurred with the Bank of Russia.

STRUCTURAL LIQUIDITY DEFICIT/SURPLUS

A structural deficit is the state of the banking sector characterised by stable demand of credit institutions for Bank of Russia liquidity. A structural surplus is characterised by a stable surplus in credit institutions' liquidity and the need for the Bank of Russia to conduct liquidity-absorbing operations. The level of a structural liquidity deficit/surplus is a difference between the outstanding amount on refinancing operations and Bank of Russia liabilities on operations to absorb excess liquidity.

TRANSMISSION MECHANISM

The process of transferring the impulse of monetary policy decisions to the economy as a whole and to price dynamics, in particular. The process of transmitting the central bank's signal about a/no change in the key rate and its future path, from financial market segments to the real sector and, as a result, to inflation. Changes to the key rate are translated into the economy through different channels (interest rate, credit, foreign exchange, balance sheet, inflation expectations, and other channels).

ABBREVIATIONS

- **AE** – Advanced economies
- **АЕБ** – Association of European Businesses
- **AFCR** – adjusted for foreign currency revaluation
- **AHML** – Agency for Housing Mortgage Lending
- **BLC** – bank lending conditions
- **bp** – basis point (0.01 percentage points)
- **BPM6** – the 6th edition of the IMF's Balance of Payments and International Investment Position Manual
- **BRICS** – a group of five countries: Brazil, Russia, India, China and South Africa
- **Cbonds-Muni** – municipal bond index calculated by Cbonds
- **CCPI** – core consumer price index
- **CPI** – consumer price index
- **DSR** – debt service ratio (the ratio of the cash flow available to pay current debt obligations, including principal and interest, to current income value)
- **ECB** – European Central Bank
- **EME** – emerging market economies
- **EU** – European Union
- **FAO** – Food and Agriculture Organization of the United Nations
- **FCS** – Federal Customs Service
- **Fed** – US Federal Reserve System
- **FGUP** – federal state unitary enterprise
- **FPG** – fiscal policy guidelines
- **GDP** – gross domestic product
- **GFCF** – gross fixed capital formation
- **GRP** – gross regional product
- **GVA** – gross value added
- **IBL** – interbank loans
- **IEA** – International Energy Agency
- **IFX-Cbonds** – corporate bond return index
- **Industrial PPI** – industrial producer price index
- **inFOM** – Institute of the Public Opinion Foundation
- **MC** – management company

- **MIACR** – Moscow Interbank Actual Credit Rate (weighted average rate on interbank loans provided)
- **MIACR-B** – Moscow Interbank Actual Credit Rate-B-Grade (weighted average rate on interbank loans provided to banks with speculative credit rating)
- **MIACR-IG** – Moscow Interbank Actual Credit Rate-Investment Grade (weighted average rate on interbank loans provided to banks with investment-grade rating)
- **MIC** – military-industrial complex
- **MICEX SE** – MICEX Stock Exchange
- **million bpd** – million barrels per day
- **MPD** – Monetary Policy Department of the Bank of Russia
- **MPG 2020-2022** – Monetary Policy Guidelines for 2020-2020 (approved by the Bank of Russia Board of Directors on 25 October 2019)
- **MPR** – Monetary Policy Report (mentioned in the text as 2/19 – No. 2 2019; 3/19 – No. 3 2019; 4/19 – No. 4 2019, 1/20 – No. 1 2020; 2/20 – No. 2 2020)
- **MTVECM, TVECM** – Momentum Threshold Vector Error Correction Model, Threshold Vector Error Correction Model
- **NFI** – non-bank financial institution
- **NPF** – non-governmental pension fund
- **NPISH** – non-profit institutions serving households
- **NWF** – National Wealth Fund
- **OBR** – Bank of Russia bonds
- **OECD** – Organisation for Economic Cooperation and Development
- **OFZ** – federal government bonds
- **OFZ-IN** – inflation-indexed federal government bonds
- **OFZ-PD** – permanent coupon-income federal government bonds
- **OFZ-PK** – variable coupon-income federal government bonds
- **OJSC** – open joint-stock company
- **OPEC** – Organization of the Petroleum Exporting Countries
- **PJSC** – public joint-stock company
- **PMI** – Purchasing Managers' Index
- **pp** – percentage point
- **PPI** – producer price index
- **QPM** – quarterly projection model of the Bank of Russia
- **REB** – Russian Economic Barometer, monthly bulletin
- **REER** – real effective exchange rate
- **RGBEY** – Russian Government Bonds Effective Yield until Redemption (calculated by the Moscow Exchange)

- **RUONIA** – Ruble OverNight Index Average (reference weighted rate of overnight ruble deposits in the Russian interbank market)
- **SA** – seasonally adjusted
- **SME** – small and medium-sized enterprises
- **SNA** – system of national accounts
- **TCC** – total cost of credit
- **TVP FAVAR** – Time-Varying Parameter Factor-Augmented Vector Auto-Regression
- **VAT** – value added tax
- **VCIOM** – Russian Public Opinion Research Centre
- **VEB** – Vnesheconombank
- **VECM** – Vector Error Correction Model
- **3MMA** – three-month moving average