Bank of Russia

JUNE 2019

MONETARY POLICY REPORT

24 June 2019

The report has been prepared based on statistics as of 14 June 2019.
The data cut-off date for forecast calculations is 7 June 2019 (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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Please send your suggestions and comments to monetarypolicyreport@mail.cbr.ru.

This publication has been prepared by the Monetary Policy Department.

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Statement by Bank of Russia Governor Elvira Nabiullina

in the follow-up to Board of Directors meeting 14 June 2019

Today, the Bank of Russia has decided to cut its key rate to 7.50 % per annum.

We also revised our end-2019 inflation forecast downwards by 0.5 pp, to 4.2-4.7%.

Should our baseline forecast materialise, we hold open the possibility of a further rate cut at one of the upcoming Board meetings. We assume that we may shift to neutral monetary policy by mid-2020.

I will now highlight the factors we considered while making today's decision.

First. There is a stable trend towards inflation slowdown. It is attributed to the Bank of Russia's key rate decisions including the preemptive hike in the second half of last year. We passed the inflation peak of 5.3%, slightly lower than we expected, in March. Inflation slowing down from this lower peak is overall in line with our forecast. In the February-May period, prices rose by approximately 0.3-0.4% a month, seasonally adjusted. That means that the monthly growth pace has returned to the lowest readings since last August and stands near 4% in annual terms. Annual inflation fell to 5.1% in May, and came in at 5% precisely as at the beginning of this week. This dynamics is attributed to the following factors.

The effect of the VAT increase on inflation has run its course.

The ruble's strengthening since the beginning of the year made an additional contribution to inflation slowdown. Higher oil prices and overall favourable external conditions helped. International investors' interest in Russian assets recovered, which was the most distinctive in the OFZ market.

The agreements on retail fuel prices between the Russian Government and oil majors are continuing to play a significant role. Consumer petrol prices rose in May by 2.8% year-on-year, and their growth is likely to be moderate in the near future. That said, the new regulation in this market, in particular, the offsetting mechanisms (including reverse excise duties), is rather complicated. Currently, it is hard to accurately estimate its medium-term economic effectiveness, especially for scenarios providing for tangible oil price fluctuations.

Modest domestic demand is also curbing inflation.

This calls for a deeper insight into the economy. This is the second most important factor that we took into account. Economic growth in the first half of the year has been lower than expected.

We predicted that business activity might slow down somewhat at the beginning of the year on the back of the following factors: the VAT hike, a likely slowdown in growth of the global economy and demand for Russian goods and services, and the implementation period of the major national projects scheduled for the second half of the year. Some of these factors had a stronger effect than expected. In particular, budget expenditure dynamics.

We will be able to take a deeper insight into the economic growth slowdown after detailed GDP statistics are released. However, the 2018 data released in April and preliminary Q1 2019 estimates allow us to update our GDP forecast for this year. In particular, the revision is associated with lower export growth rates and a tempered outlook for growth in the global economy and external demand. We have left the forecast for consumer and investment demand unchanged in view of the expected rise in public expenses in the second half of the year. As a result, we have updated the 2019 economic growth forecast from 1.2-1.7% to 1-1.5%.

Third. Proinflationary risks have declined over a one-year horizon. First, we no longer expect any deferred effects of the VAT hike. Second, the US Fed consistently eased it rhetoric since the year start amid the expected slowdown of global economic growth. All else being equal, this constrains the risks of considerable capital outflow from emerging markets.

In March-April, we noticed that the risks of accelerated growth in prices of certain food products diminished. Overall, they remain moderate, though current food inflation was somewhat higher in May than in the previous three months, seasonally adjusted.

Moving forward, we expect that record crop areas, early spring, and overall favourable weather will bring a good harvest of vegetables, grains and other crops. Domestic and global grain prices have been down since the beginning of the year. This contains proinflationary risks for food products.

As regards monthly growth in prices of non-food goods and services, it held close to or below 4% in annual terms in March-May.

Fourth. We factored in that inflation expectations of households and businesses remain elevated against both the inflation target and the minimum levels reached in the opening months of 2018. Inflation expectations show mixed dynamics. Business price expectations continued to decline in April-May. Inflation expectations of households came in at 9.3-9.4% during this period. However, we expect that inflation decline to 4% will bring down inflation expectations of households and businesses.

Analysts' expectations remain anchored at the inflation target of close to 4%.

Fifth. Monetary conditions are softening. This is driven by changing expectations of domestic and external financial market players. First, this is enabled by revised expectations as to the path of the Bank of Russia key rate; second, by an adjustment in expectations and yields in the external financial market against the background of changes in major central banks' rhetoric – which I have mentioned. OFZ yields are declining in this environment, enabling a potential reduction in deposit and lending rates. Between April and May, a number of major banks revised downwards their interest rates on several deposit products; interest rates on mortgage loans were also beginning to trend down. Today's decision to cut the key rate alongside the signal we have sent out will work to solidify these trends.

Medium-term outlook. The outcome of OPEC+ negotiations remains uncertain. We look to further concerted actions by deal parties to warrant smooth oil price dynamics over the forecast horizon. Based on their actual movements since the year start, we have upgraded the average annual Urals crude price in our baseline scenario from $60 to $65 per barrel in 2019 and from $55 to $60 per barrel in 2020. We retain our conservative assumptions for 2021 whereby the oil price is expected to reach $55 per barrel.

Key balance of payments figures in the baseline scenario have also been adjusted to oil price movements and the expected dynamics of the global economy. This year's current account balance is estimated to total $98 billion (approx. 6% of GDP) and drop subsequently to $50 billion (approx. 3% of GDP) in 2021. This is attributed to downward oil price trends and expanding imports as economic growth accelerates.

The private sector's financial account balance in 2019 is set to amount to approx. $50 billion (3% of GDP). Financial transactions of private sector balance already reached $35 billion in the first five months of the year. We expect it to drop substantially in the second half of the year compared to both the past year's last six months and the first six months of this year. The main reasons behind this outlook are as follows. First, it comes as a reflection of the seasonality which is typical of balance of payments figures. Second, we look to normalisation in the accumulation of foreign assets, which has quickened considerably since the middle of the past year in the context of strengthened external, including geopolitical risks.

Our medium-term economic growth outlook is essentially the same. 1-1.5% GDP growth in the current year is expected to accelerate gradually to 2-3% in 2021. Having said that, our forecast will largely depend on the timeframes and successful implementation of the national projects along with other fiscal policy decisions.

Discussions are currently underway about possible options of spending the liquid part of the National Wealth Fund in excess of the 7% of GDP cap. As we look into such options, it is imperative that we remember the key objective of the fiscal rule, which is to reduce the reliance of the economy, of the real exchange rate and of public finances on a volatile energy price environment so that they all become stabilised in a state equivalent to the oil price cut-off. We have largely delivered on this objective, with the impact of oil price fluctuations on the Russian economy having considerably weakened. Current suggestions are essentially focused on changes to the rule. They could result in either direct or indirect change in the cut-off price, entailing a strengthening of the real ruble exchange rate and undermining competitiveness of our products. Alternatively, the stabilising mechanism of the fiscal rule could be undermined, yet again adding to the vulnerability of the Russian economy to fluctuations in external environment.

More so, the 7% of GDP cap was set a long time ago; yet another review is needed to establish whether this volume of liquid assets is adequate to resist to sharp and lengthy change in external conditions.

As we review these and similar suggestions, we urge to fully consider the benefit and loss balance driven by change in macroeconomic conditions which may be tangible enough.

Approaches to fiscal and structural policies will have a significant impact on both our forecast and estimates of the balance of risks for inflation. This will in turn determine the monetary policy path.

Governor of the Bank of Russia ***Elvira S. Nabiullina***

BANK OF RUSSIA'S MEDIUM-TERM FORECAST

IN THE FOLLOW-UP TO BOARD OF DIRECTORS MEETING 14 JUNE 2019

KEY PARAMETERS OF THE BANK OF RUSSIA'S FORECAST SCENARIOS
(GROWTH AS % OF PREVIOUS YEAR, UNLESS INDICATED OTHERWISE)

Table 1

	2018 (actual)	Baseline			High oil prices		
		2019	2020	2021	2019	2020	2021
Urals price, average for the year, US dollars per barrel	69.8	65	60	55	70	75	75
Inflation, as %, in December year-on-year	4.3	4.2–4.7	4.0	4.0	4.2–4.7	4.0	4.0
Inflation, average for the year, as % year-on-year	2.9	4.7–4.9	4.0	4.0	4.7–4.9	4.0	4.0
Gross domestic product	2.3	1.0–1.5	1.8–2.3	2.0–3.0	1.0–1.5	2.0–2.5	2.0–3.0
Final consumption expenditure	1.8	1.0–1.5	1.8–2.3	2.0–2.5	1.0–1.5	2.0–2.5	2.0–2.5
– *households*	*2.3*	*1.0–1.5*	*1.8–2.3*	*2.5–3.0*	*1.0–1.5*	*2.3–2.8*	*2.5–3.0*
Gross capital formation	0.8	0.5–1.5	3.5–4.5	3.5–4.5	0.5–1.5	3.5–4.5	3.5–4.5
– *gross fixed capital formation*	*2.9*	*1.0–2.0*	*3.5–4.5*	*3.5–4.5*	*1.0–2.0*	*3.5–4.5*	*3.5–4.5*
Exports	5.5	0.8–1.3	2.7–3.2	2.7–3.2	0.8–1.3	2.7–3.2	2.7–3.2
Imports	2.7	1.0–1.5	3.8–4.2	4.5–5.0	1.0–1.5	4.0–4.5	4.5–5.0
Money supply in national definition	11.0	8–12	7–12	7–12	9–13	8–13	8–13
Banking system claims on the economy in rubles and foreign currency*	11.5	8–12	7–12	7–12	9–13	7–12	7–12
– *claims on organisations in rubles and foreign currency; growth as % over year*	*8.4*	*7–10*	*6–10*	*6–10*	*8–11*	*6–10*	*6–10*
– *claims on households in rubles and foreign currency; growth as % over year*	*22.0*	*15–20*	*11–16*	*10–15*	*16–21*	*12–17*	*10–15*

** Banking sector claims on the economy mean all claims of the banking system on non-financial organisations and financial institutions and households in the currency of the Russian Federation, foreign currency, and precious metals, including loans extended (including overdue loans), overdue interest on loans, investments of credit institutions in debt and equity securities and promissory notes, other forms of stakeholding in the capital of non-financial organisations and financial institutions, and other receivables under settlement operations with non-financial organisations and financial institutions and households.*

Source: Bank of Russia.

RUSSIA'S BALANCE OF PAYMENTS INDICATORS*
(BILLIONS OF US DOLLARS)

Table 2

	2018 (actual)	Baseline			High oil prices		
		2019	2020	2021	2019	2020	2021
Current account	**114**	**98**	**72**	**50**	**106**	**112**	**103**
Balance of trade	194	184	160	139	190	203	199
Exports	*443*	*434*	*424*	*415*	*443*	*475*	*493*
Imports	*249*	*250*	*264*	*276*	*253*	*272*	*294*
Balance of services	-30	-33	-37	-37	-31	-35	-40
Exports	*65*	*62*	*63*	*66*	*66*	*70*	*73*
Imports	*95*	*95*	*100*	*103*	*97*	*105*	*113*
Balance of primary and secondary income	-51	-53	-51	-52	-53	-56	-56
Current and capital account balance	**113**	**98**	**72**	**50**	**106**	**112**	**103**
Financial account (excluding reserve assets)	**77**	**32**	**16**	**7**	**32**	**29**	**24**
General government and the central bank	9	-18	-6	-6	-18	-6	-6
Private sector	68	50	22	13	50	35	30
Net errors and omissions	**3**	**0**	**0**	**0**	**0**	**0**	**0**
Change in reserve assets ('+' is increase, '-' is decrease)	**38**	**66**	**56**	**43**	**74**	**83**	**79**

** Signs according to BPM6. In financial account, '+' denotes net lending and '-' denotes net borrowing.*
Note: Due to rounding total results may differ from the sum of respective values.

Source: Bank of Russia.

1. ECONOMIC OUTLOOK

In the context of the current global and Russian economy and domestic consumer price dynamics, the Bank of Russia has lowered its end-of-year annual inflation forecast for 2019 in the baseline scenario as compared to its March issue of the Monetary Policy Report published on 1 April 2019. Under the baseline scenario, annual inflation is expected to be 4.2–4.7% as of the end of 2019. The revised forecast takes into account the completion of the VAT increase pass-through to prices (including the influence of secondary effects) and the preservation of relatively favourable external conditions and moderate dynamics of domestic demand. Moving on, according to the Bank of Russia's forecast, annual inflation will stay close to 4%.

The Bank of Russia has also lowered the GDP growth rate forecast in 2019 to 1.0–1.5% in the light of the statistics on GDP dynamics in 2018 – 2019 Q1 published by Rosstat. As previously expected, the VAT hike in the beginning of the year, a certain slowdown in global economic growth, and the gradual decrease in global oil prices will have a restraining effect on the economic activity in 2019. At the same time, according to the Bank of Russia's estimates, the effect of some of these factors on the dynamics of domestic demand in 2019 H1, together with the shift of the implementation periods of major national projects to the second half of the year, could be more pronounced than previously expected, which was the reason for the forecast adjustment. After a slight slowdown in 2019, economic growth in the baseline scenario will gradually accelerate in 2020 and 2021 as the positive effects from fiscal policy measures planned by the government and national projects accumulate, subject to their successful implementation.

One of the key uncertainty factors for the Russian economy in 2019–2021 is further global economic developments. In this respect, in addition to the baseline scenario, the Bank of Russia continues to consider a high oil price scenario and a risk scenario.

In the scenario with high oil prices at $75 per barrel in 2020–2021, economic dynamics in 2020 will be better than in the baseline scenario thanks to additional support for business sentiment and consumer and investment activities in the context of improved trade conditions. Inflation will remain at the baseline scenario level throughout the entire forecast horizon, as the slightly greater upward pressure resulting from changes in demand or the effect of oil and gas tax manoeuvres will be partially compensated by the downward influence of the pass-through of a stronger exchange rate than in the baseline scenario, and the Bank of Russia will take this into account when implementing its monetary policy.

The risk scenario parameters have been slightly tightened as compared to the March issue of the report. A significant deterioration of external conditions may cause temporary inflation acceleration of over 4% and a downturn in the economy. However, this effect will be short-lived considering the increased resilience of the Russian economy to external developments, the smoothing effect of the fiscal rule and a timely monetary policy reaction. In the second half of the forecast horizon, the key forecast parameters under the risk scenario will draw closer to the baseline scenario.

In addition to further external developments, including geopolitical factors and global economy slowdown risks due to further tightening of international trade restrictions, future dynamics of inflation expectations and fiscal policy parameters, such as decisions to use the liquid part of the National Wealth Fund in excess of the 7% GDP cap, remain among additional uncertainty factors for the baseline scenario.

According to the Bank of Russia's estimates, short-term inflation risks have abated as compared to March. With regard to internal conditions, the effects from the VAT hike have fully materialised. As for external conditions, the revision of interest rate paths by the US Fed and other central banks in advanced economies in 2019 H1 reduces the risks of significant capital outflows from emerging markets.

The Bank of Russia leaves mostly unchanged its estimates of risks associated with wage movements, prices of individual food products, and possible changes in consumer behaviour. These risks remain moderate.

1.1. BASELINE SCENARIO AND FORECAST UNCERTAINTY FACTORS

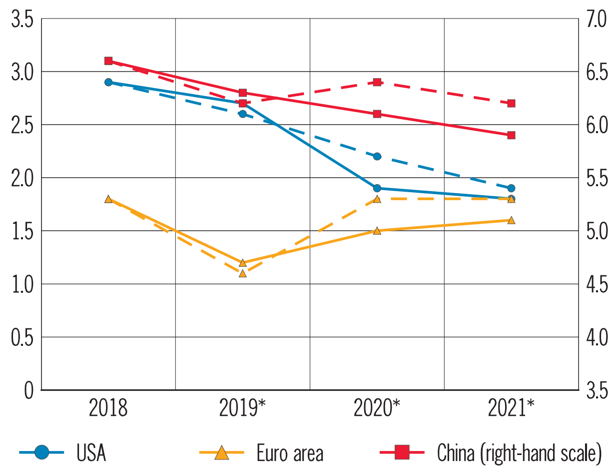
FORECAST ASSUMPTIONS

Global economic growth. As in the Monetary Policy Report published on 1 April 2019 (hereinafter, Monetary Policy Report 1/19), in its baseline scenario the Bank of Russia expects the gradual slowdown of global economic growth rates over the 2019–2021 horizon (Chart 1.1.1). The expected slowdown in the global economy is largely driven by continued moderate economic activity in the euro area, the gradual exhaustion of the fiscal impulse effect, the transition to the late phase of the economic cycle in the US, the smooth deceleration of the Chinese economy, as assumed in the baseline scenario, and by remaining concerns about the future tightening of international trade restrictions. At the same time, based on comments by officials and clarified estimates by international organisations, in its baseline scenario the Bank of Russia has slightly downgraded the forecast of the potential economic growth rate for the euro area and China (Chart 1.1.1). According to the Bank of Russia's estimates, in the baseline scenario, as it was assumed before, the growth rates of the US economy will gradually slow down remaining however slightly above the potential until 2021. Overall, this forecast by the Bank of Russia is consistent with the expectations of market participants and international organisations.

Oil prices. In the baseline scenario, the Bank of Russia proceeds from a gradual price drop in Urals crude to $55 per barrel and maintaining it near this level (Chart 1.1.2). This trajectory is based on the gradual slowdown of the global economy and the continued high probability of the excess of supply over demand in the oil market over the forecast horizon, including due to a significant growth in production outside OPEC+ countries.

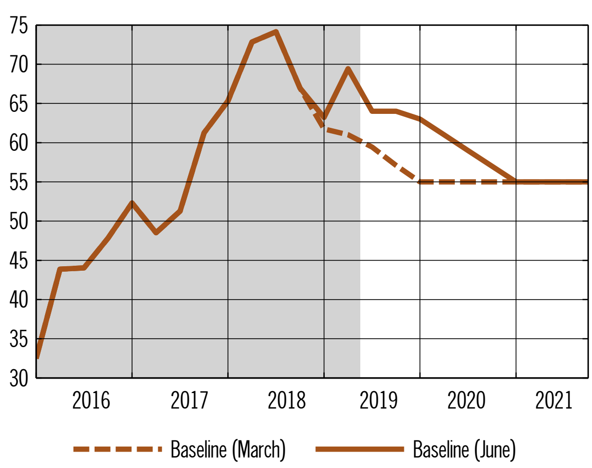
At the same time, it is assumed now that $55 per barrel will be achieved in early 2021, unlike it was stated in Monetary Policy Report 1/19, where the price of oil decreased to $55 per barrel by the end of 2019. Thus, the average oil price in the baseline scenario has been increased from

GROWTH INDICATORS OF LARGEST GLOBAL ECONOMIES IN BASELINE SCENARIO *Chart 1.1.1*
(PER CENT CHANGE ON PREVIOUS YEAR)



** Forecast. Note: dotted line shows the previous forecast (MPR 1/19).*
Source: Bank of Russia calculations.

OIL PRICE TRAJECTORY IN BASELINE SCENARIO *Chart 1.1.2*
(US DOLLARS/BARREL)



Note: nominal Urals crude prices.
Source: Bank of Russia calculations.

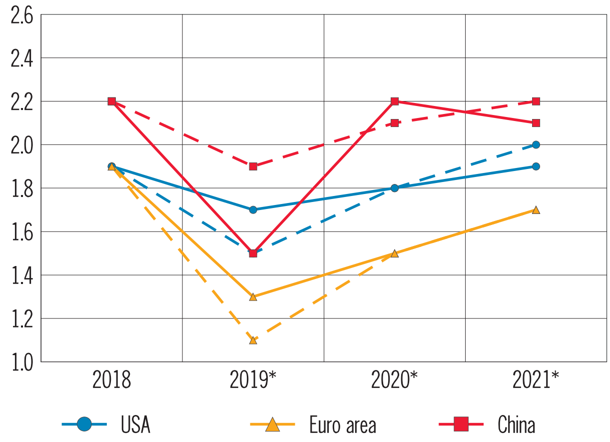
$60 to $65 per barrel in 2019 and from $55 to $60 per barrel in 2020. This is due to the actual dynamics of oil prices that have taken shape since the beginning of 2019 and persisting expectations of a decrease in oil extraction and exports from Iran and Venezuela. The Bank of Russia has also clarified its expectations regarding the actions of OPEC+. The baseline scenario assumes continued coordination of actions between OPEC+ members.

Inflation abroad. As in March, the Bank of Russia's baseline scenario provides for weaker inflationary pressure in Russia's key trading partners in 2019–2021. This will be largely due to a gradual downturn in oil prices and a global economic slowdown. The Bank of Russia has updated the forecast of consumer price growth in the US, the euro area and China as compared to Monetary Policy Report 1/19 in the light of the revision of the oil price trajectory in the baseline scenario in 2019–2020 (Chart 1.1.3).

Monetary policies of foreign central banks. In 2019–2021, the Bank of Russia expects a pause in further tightening of the monetary policy in the US. The Bank of Russia has revised its assumption regarding interest rate growth in the US (Chart 1.1.4) given the latest communication of the US Fed (see Subsection 3.1.2) and the downward shift of expectations of market participants in this regard. Now, the Bank of Russia's baseline scenario assumes that the US Federal Reserve base rate will remain at the current level over the entire forecast horizon. At the same time, the Bank of Russia maintains its mid-term view of the dynamics of interest rates in the euro area. As stated in Monetary Policy Report 1/19, the baseline scenario expects that they will start growing in 2020 H2 (Chart 1.1.5).

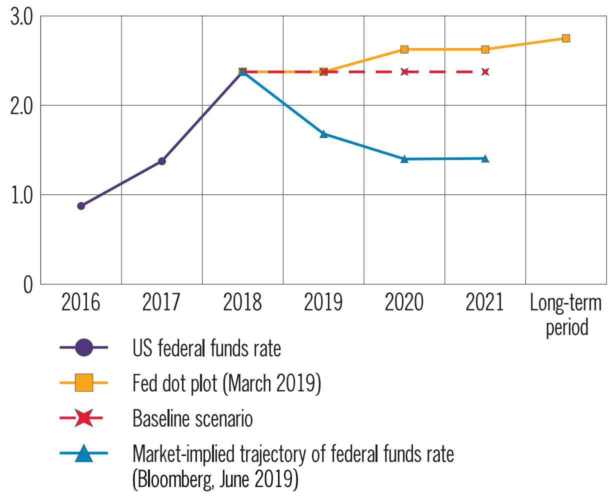
Global financial markets. Compared to Monetary Policy Report 1/19, in its current baseline scenario, the Bank of Russia proceeds from a weaker US dollar against the euro in 2020–2021. The weaker dollar dynamics are primarily caused by the revision of interest rate growth prospects in the US. In turn, such rate dynamics will contribute to the formation of softer-than-expected monetary conditions in advanced economies over the forecast horizon, which will help mitigate the risks of a steady capital outflow from emerging market economies (hereinafter, EMEs). Having in mind the

INFLATION INDICATORS OF LARGEST GLOBAL ECONOMIES IN BASELINE SCENARIO *Chart 1.1.3*
(PER CENT CHANGE YOY AS OF THE PERIOD-END)



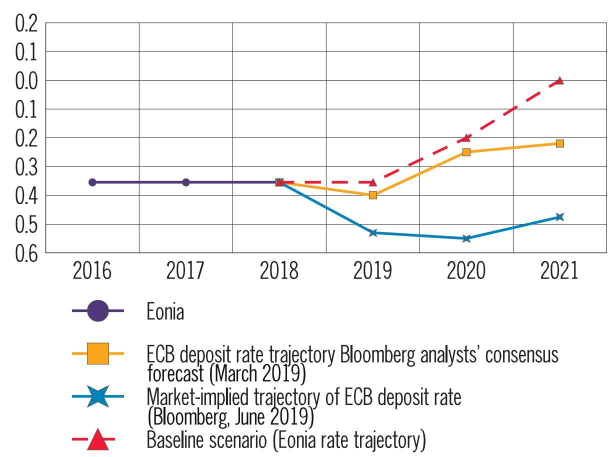
** Forecast. Dotted line shows the previous forecast (March 2019).*
Note: PCE Price Index is forecast for the US, HICP – for the Euro area, and CPI – for China.
Sources: Bank of Russia calculations, Bloomberg.

EXPECTED TRAJECTORIES OF FEDERAL FUNDS RATE *Chart 1.1.4*
(% P.A.)



Note: values are given as of the end of each period.
Sources: Bank of Russia calculations, the US Fed, Bloomberg.

EXPECTED TRAJECTORIES OF EURO AREA INTEREST RATES *Chart 1.1.5*
(% P.A.)



Note: values are given as of the end of each period (Bloomberg analysts' consensus forecast for 2021 is given as of the end of 2021 Q3).
Sources: Bank of Russia calculations, Bloomberg.

actual dynamics of EME risk premiums since the beginning of this year and the clarification of the mid-term dynamics of US interest rates, the Bank of Russia has slightly decreased the equilibrium country risk premium for EMEs in general and for Russia in particular in the baseline scenario.

Geopolitical factors. As before, in its baseline scenario the Bank of Russia proceeds from the retention of international sanctions imposed on Russia in 2014–2018 over the entire forecast horizon. This involves instituting a country risk premium for Russia at a slightly higher level than if there were no sanction restrictions. Relying on conservative risk premium assumptions, in the baseline scenario, the Bank of Russia takes into account the potential volatility in financial markets in the case of emergence of short-term episodes of increased geopolitical tension.

Russia's state policy measures. In terms of key internal assumptions, in its monetary policy for 2019–2021, the Bank of Russia factors in past and expected changes in taxation, the Government's measures for overcoming the structural constraints of the Russian economy, including national projects, and the effect of the fiscal rule.

Among the key changes in the tax policy, the Bank of Russia's baseline scenario reflects primarily the VAT increase from 18 to 20% effective from 1 January 2019. The Bank of Russia also takes into account the changes in excise taxes on individual products included in the consumer basket and an oil and gas tax manoeuvre, whose estimated contribution to annual inflation in 2019–2021 has not changed substantially as compared to the March forecast. Thus, in 2019–2021, the contribution of the tax manoeuvre to the annual inflation in the baseline scenario will be close to zero.

The Bank of Russia also maintains its assessments of the effect that the government's measures aimed at mitigating the existing structural constraints in the Russian economy and increasing its potential growth rates at the level of those published in October 2018 (in the Monetary Policy Guidelines for 2019 and for 2020 and 2021) may have on the Russian economy. Such measures include a phased increase in the pension age, as well as additional investment expenditures and expenses for the development of human capital in 2019–2024.

MEDIUM-TERM FORECAST

Inflation. In line with the pursued monetary policy, the Bank of Russia has lowered its end-of-year annual inflation forecast for 2019 from 4.7–5.2% in Monetary Policy Report 1/19 to 4.2–4.7%. The revised forecast takes into account the completion of the VAT increase pass-through to prices (including the influence of secondary effects) and the preservation of relatively favourable external conditions and moderate dynamics of domestic demand. Moving on, according to the Bank of Russia's forecast, annual inflation will stay close to 4%.

Inertia inflation factors, including the moving average annual inflation, will remain higher during the whole 2019 than in 2018, but in 2020–2021, they will stay close to 4%.

The Bank of Russia estimates the total contribution of the VAT hike to annual inflation in 2019, including secondary effects, at approximately 0.6–0.7 pp, which corresponds to the lower bound of the Bank of Russia's expectations range.

Economy. The Bank of Russia has updated its view of the Russian economy in 2019 as compared to Monetary Policy Report 1/19. As previously expected, the VAT hike in the beginning of the year, a certain slowdown in global economic growth, and the gradual decrease in global oil prices will have a restraining effect on the economic activity in 2019. At the same time, according to the Bank of Russia's estimates, the effect of some of these factors on the dynamics of domestic demand in 2019 H1, together with the shift of the implementation periods of major national projects to the second half of the year, could be more pronounced than previously expected (see Sections 3.3 and 3.4). Taking into account GDP growth statistics for 2018 – 2019 Q1 published by Rosstat, the Bank of Russia has lowered its GDP growth forecast for 2019 from 1.2 – 1.7% to 1.0 – 1.5%.

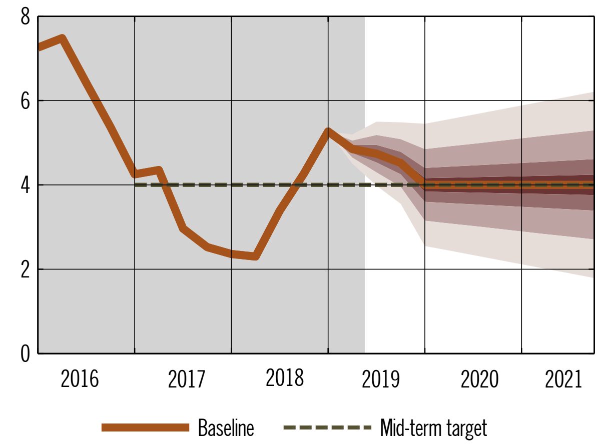
The Bank of Russia has also slightly updated the view of the GDP growth structure in 2019. For example, as compared to Monetary Policy Report 1/19, the forecast growth of export quantities in 2019 has been lowered from 2.5 – 3.0% to 0.8 – 1.3%, which is mainly explained by weaker-than-expected actual dynamics of exports in late 2018 – early 2019. The Bank of Russia has also adjusted the forecast growth rate of gross formation in 2019 downwards from 1.0 – 2.0% to 0.5 – 1.5%, taking into account the possible material adjustment of inventories in Q1 (see Section 3.3). At the same time, given the time frames for the launch of implementation of some major national projects (see Section 3.4), the Bank of Russia maintained its forecast of the annual growth rates of gross fixed capital formation in 2019 in the range of 1.0–2.0%. Investment growth will be supported by an increase in investment expenditures planned by the Government in 2019 H2.

As before, the Bank of Russia continues to forecast that accelerated growth of the Russian economy in 2020 and 2021 will reach 1.8–2.3% and 2.0–3.0%, respectively (Chart 1.1.7). This will be driven by a gradual accumulation of the positive effect of the planned fiscal policy measures and national projects once they are successfully implemented. In its baseline scenario, the Bank of Russia assumes that higher growth rates in the Russian economy will not create demand-side inflationary pressure, as it will result in the expanded production capacity of the economy.

Monetary indicators. The forecast monetary indicators have been updated slightly as compared to Monetary Policy Report 1/19 in terms of claims of the banking system on households. Their growth rate in 2019 has been increased in view of faster-than-expected growth early in the year (see Section 3.2). At the same time, the Bank of Russia still expects a gradual slowdown of their growth rates versus 2018 (22.0% at year-end), which is in part due to measures intended to restrict an increase in the debt burden of the population in general and of individual borrowers in particular, and to a saturation of the retail lending market. The gradual easing of price lending conditions due to a decrease in the key rate (see Section 4.1) will support stable lending growth, including, primarily, corporate and mortgage lending. Non-price lending conditions will soften gradually, reflecting banks' conservative approach to assessing borrowers and taking risks.

INFLATION
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)

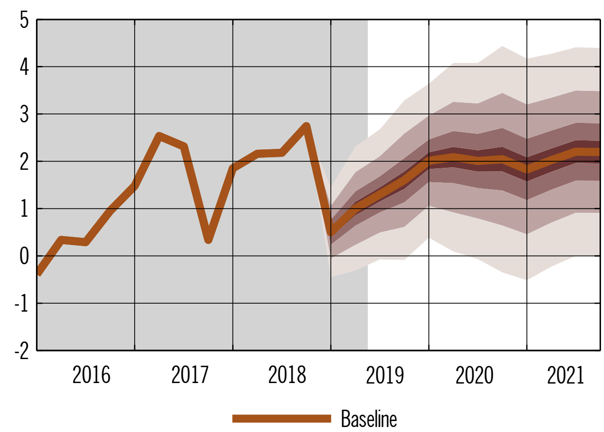
Chart 1.1.6



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 uncertainty of inflation.
Source: Bank of Russia calculations.

GDP GROWTH RATE
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)

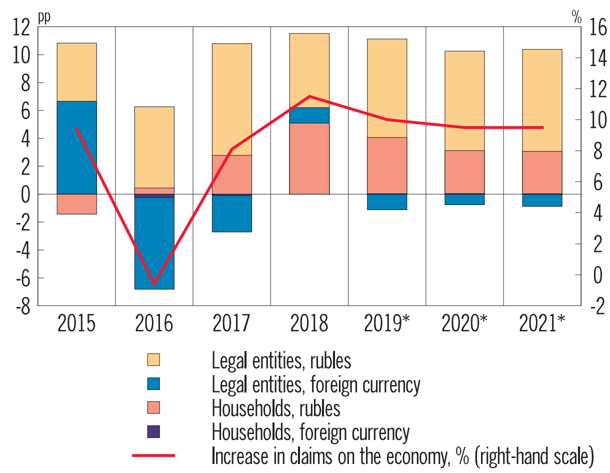
Chart 1.1.7



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 uncertainty of GDP growth rate.
Source: Bank of Russia calculations.

DECOMPOSITION OF INCREASE IN CLAIMS ON ECONOMY
(CONTRIBUTION TO ANNUAL GROWTH, PP)

Chart 1.1.8



** Forecast. Decomposition is shown for the increase in claims on the economy corresponding to the middle of the forecast range in the baseline scenario.*
Source: Bank of Russia calculations.

Given the effect of all of the above factors, lending activities will continue to grow overall in 2019–2021 at a stable pace that corresponds to the increasing effective demand and does not pose any risks to price stability (Chart 1.1.8). The debt burden of the economy will remain at levels that do not create any threats to the financial stability of the economy while increasing smoothly (Charts 1.1.9, 1.1.10). Credit will remain the key driver of changes in the money supply, and the monetary supply growth rates in such conditions will be close to the growth rates of claims on the economy (Chart 1.1.11).

Balance of payments. The balance of payments indicators forecast has been adjusted compared to Monetary Policy Report 1/19 in view of the revised assumptions regarding oil prices in 2019–2020 and the updated GDP growth forecast for 2019, as well as actual data on the main components of the balance of payments since the beginning of the year. Thus, the forecast current account balance has been increased from $88 to $98 billion. The private sector financial account balance has also been raised from $35 to $50 billion. At the same time, taking into account the actual inflow of foreign investor funds to the OFZ market in the first half of the year and the successful placement of Russian eurobonds, the public sector financial account deficit (in BPM6 signs, i.e. net capital inflow) has been revised from $6 to $18 billion.

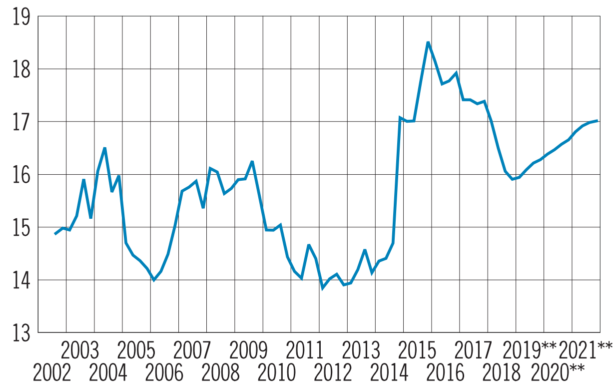
Over the mid-term horizon, despite the gradual downturn in oil prices, the current account balance will remain consistently positive: 6% of GDP in 2019, 4% of GDP in 2020, and 3% of GDP in 2021 (vs 7% of GDP in 2018). The Government's measures aimed at stimulating non-commodity exports will support the growth of export quantities, which will soften the effect from the expected oil price downturn and the slowdown of global economic growth (Chart 1.1.12).

The private sector financial account balance will shrink in 2019–2021: from 3% of GDP in 2019 to 1% of GDP in 2020–2021 (vs 4% of GDP in 2018) against the backdrop of reduced external debt payments and somewhat limited possibilities for Russian companies to accumulate foreign assets in the context of lower prices for core Russian exports (Chart 1.1.13).

In 2019–2021, the Bank of Russia will also continue to replenish international reserves under

CORPORATE DEBT BURDEN
(DEBT SERVICE RATIO*, AS % OF GDP)

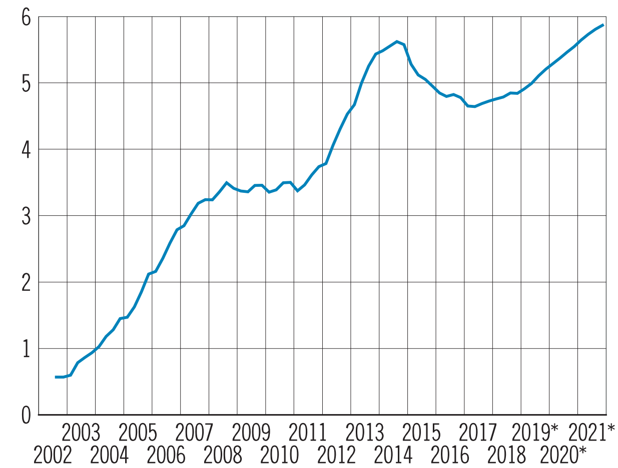
Chart 1.1.9



** Debt service ratio is calculated based on the methodology described in Donets S.A., Ponomarenko A.A., Measuring Debt Burden. Money and Credit. No. 4, 2017. 2019 Q1 value – Bank of Russia estimate.*
*** Forecast. Debt burden is calculated for the credit corresponding to the middle of the forecast range in the baseline scenario.*
Source: Bank of Russia calculations.

HOUSEHOLD DEBT BURDEN
(DEBT SERVICE RATIO, AS % OF GDP)

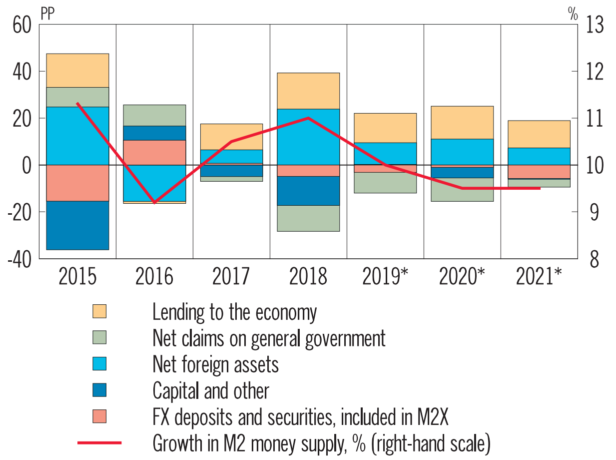
Chart 1.1.10



** Forecast. Debt burden is calculated for the credit corresponding to the middle of the forecast range in the baseline scenario.*
Source: Bank of Russia calculations.

DECOMPOSITION OF GROWTH IN MONEY SUPPLY IN NATIONAL DEFINITION IN BASELINE SCENARIO
(CONTRIBUTION TO ANNUAL GROWTH, PP)

Chart 1.1.11



** Forecast. Decomposition is shown for the increase in money supply in the national definition corresponding to the middle of the forecast range in the baseline scenario.*
Source: Bank of Russia calculations.

the fiscal rule. Its forecast takes into account, among other things, the purchase of foreign currency in the domestic market postponed in 2018.

FORECAST UNCERTAINTY FACTORS

External conditions. Since March 2019, proinflationary risks associated with specific external factors have continued to decrease. The revision of expectations in 2019 H1 with respect to the mid-term dynamics of US interest rates (see Section 3.1) reduces the risks of steady capital outflow from EMEs.

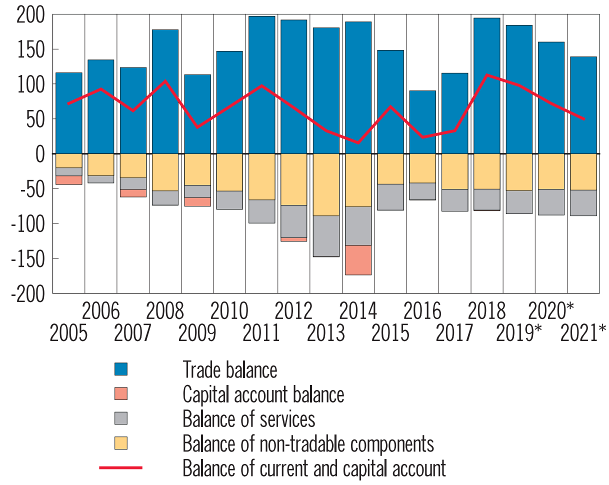
At the same time, other external risks remain material. There are still risks that the global economy will slow down amid the actual slowdown of the economic growth observed in the majority of key global economies (see Section 3.1). The continuing uncertainty regarding the UK's exit from the European Union (EU) and concerns about the results of US negotiations with key trade partners (primarily, China) related to foreign trade restrictions are additional factors in the deterioration of expectations with respect to the growth of major economies (see Section 3.1).

New foreign trade tariffs may have a negative impact on EMEs, including Russia, due to the decreasing external demand caused by the global economy slowdown, higher global financial market volatility, lower demand for risky assets, and increasing risk premiums. Deteriorating conditions in the EME financial markets in the short-term may create proinflationary risks through the dynamics of national currencies and exchange rate expectations. However, in the mid-term, a slowdown of the global economy in the case of the extension of foreign trade restrictions by the US could be of a disinflationary nature for most economies, including EMEs.

Geopolitical risks remain high. Their materialisation may lead to increased volatility in global commodity and financial markets and affect exchange rate and inflation expectations.

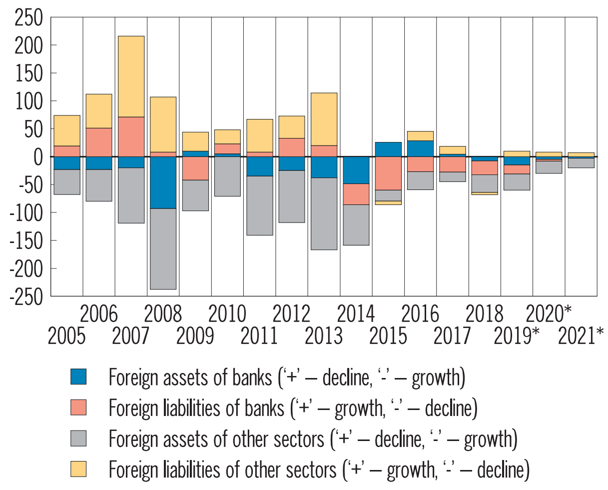
Further oil price dynamics remain a source of uncertainty, despite the fact that prices remain relatively high at present (see Section 3.1). The increased volatility of oil prices may be preserved influenced mainly by supply-side factors. Oil prices

MAJOR CURRENT ACCOUNT COMPONENTS IN BASELINE SCENARIO *Chart 1.1.12*
(BILLIONS OF US DOLLARS)



** Forecast in signs according to BPM6.*
Source: Bank of Russia.

MAJOR PRIVATE SECTOR FINANCIAL ACCOUNT COMPONENTS IN BASELINE SCENARIO *Chart 1.1.13*
(BILLIONS OF US DOLLARS)



** Forecast.*
Source: Bank of Russia.

may be lower or higher than the baseline scenario over the forecast horizon.

In such conditions, the Bank of Russia maintains a conservative approach to forming assumptions in the baseline scenario in terms of external factors, while not excluding the high oil price scenario and the risk scenario, which assumes a combination of adverse external events.

Inflation expectations. The inertia of inflation expectations, their sensitivity to price increases for individual goods and services, as well as their unanchored character remain a significant risk for inflation's upward deviation from the baseline forecast.

Effects of other economic policy measures. The scope and the nature of the influence of scheduled public policy measures are an uncertainty factor for the economic growth outlook over the forecast horizon, primarily starting from 2020. It will depend on the speed and the efficiency of the implementation of the planned measures. An additional uncertainty factor is the structure of investment of the liquid portion of NWF funds in excess of the 7% GDP threshold level set in the Budget Code. According to the baseline scenario of the Bank of Russia, this level will be reached in 2020. Should developments in 2020 – 2021 differ from these Bank of Russia assumptions and should the upward influence of increasing government spending on consumer demand significantly outpace the impact on production capacity, the acceleration of economic growth may be accompanied by upward pressure on inflation.

The gradual overcoming of structural constraints in the Russian economy may simultaneously decrease the sensitivity of domestic prices to specific external and domestic factors and have a downward effect on inflation in the case of a faster-than-expected increase in the potential growth rates of the Russian economy. This may occur as a result of reduced dependence of the Russian economy on exports of energy resources, increased competition, and the development of transport and logistics infrastructure.

The Bank of Russia will continue to pay great attention to assessing the short-term and long-term effects of planned fiscal measures by clarifying the scope and nature of their impact on the economy and inflation as they are worked out in detail and implemented.

Other factors. The Bank of Russia leaves mostly unchanged its estimates of risks associated with wage movements, prices of individual food products, and possible changes in consumer behaviour. These risks remain moderate.

1.2. HIGH OIL PRICE SCENARIO

FORECAST ASSUMPTIONS

Oil prices. The key difference between the high oil price scenario and baseline scenario is the oil price path of $75 per barrel over the forecast horizon. The primary reason for such path may be factors behind the supply of energy commodities. These include tougher restrictions on production under OPEC+ agreements as compared to the basic scenario, a greater decline in production in Iran because of sanctions, as well as a more substantial and prolonged drop in oil production in Venezuela in the context of the ongoing economic and political crisis in that country. Given the actual dynamics since the beginning of the current year, the Bank of Russia has slightly updated the oil price trajectory in the high oil price scenario for 2019 preserving the average annual oil price in 2019 at $70 per barrel (Chart 1.2.1).

Other assumptions. Other external and internal assumptions in the high oil price scenario mostly coincide with the baseline scenario. However, higher oil prices bring about stronger inflationary pressure caused by expenditures in the real economy sector of oil exporters, which may lead to faster tightening of the monetary policy in developed economies than in the baseline scenario. Although, the scope of this tightening will be less pronounced than the one assumed in Monetary Policy Report 1/19 due to the revision of the Bank of Russia's outlook of the mid-term dynamics of US interest rates. Thus, in the revised high oil price scenario, as in the baseline scenario, the Bank of Russia expects that the US Fed base rate will be preserved at the current level in 2019–2021. At the same time, as in the previous high oil price scenario and the current baseline scenario, interest rates in the euro area are expected to start growing in 2020. However, this increase will take place a quarter earlier than in the baseline scenario.

In the high oil price scenario, the contribution of the oil and gas tax manoeuvre to the annual inflation dynamics in 2019–2021 will also be slightly positive as compared to the baseline scenario.

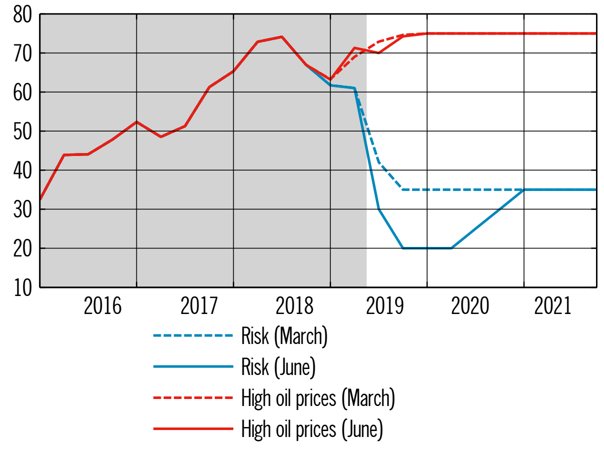
MEDIUM-TERM FORECAST

Inflation. Inflation forecast under the high oil price scenario remained close to the baseline forecast; therefore, it was similarly revised downward for 2019 as compared to the Monetary Policy Report 1/19. A faster expansion of domestic demand, than in the baseline scenario, along with the oil and gas tax manoeuvre, will have a slight upward pressure on inflation in 2019. However, the effect of these factors on inflation will be in part offset by the downward influence of the exchange-rate pass-through because the ruble will prove somewhat stronger than in the baseline scenario, according to Bank of Russia estimates. In such conditions, in 2019, the annual inflation will remain within the same range as in the baseline scenario, while in 2020–2021 it will be close to 4% (Chart 1.2.2).

At the same time, an additional factor of the forecast uncertainty in the high oil price scenario as compared to the baseline scenario is potential inflationary pressure from petroleum products price trends in the context of preservation of high global oil prices. The scope of this pressure will depend, in addition to the pricing policy of oil companies, on the efficiency of the effective excise duty redemption framework and other possible measures of state regulation aimed at smoothing price dynamics in the oil products market.

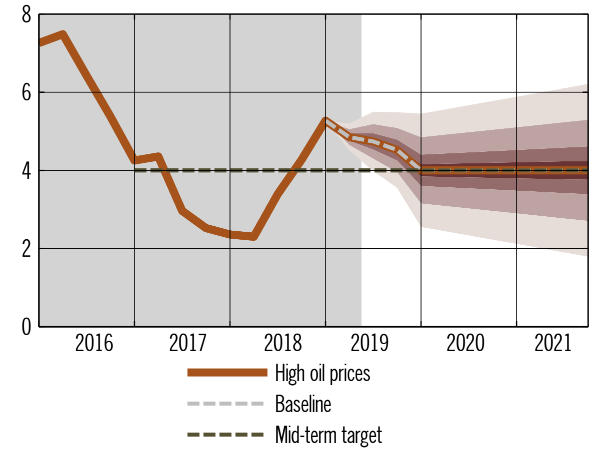
Economy. The estimated economic growth in the high oil price scenario was also close to the baseline scenario due to the effect of the fiscal rule, which smooths over the influence of oil price fluctuations on the domestic economic environment. Alongside with that, as it was expected in the March forecast, the dynamics of specific components of the domestic demand and the GDP growth rate in the high oil price scenario may be overall higher in 2020 than in the baseline scenario. That will be caused by higher oil prices

OIL PRICE
(US DOLLARS PER BARREL)
Chart 1.2.1



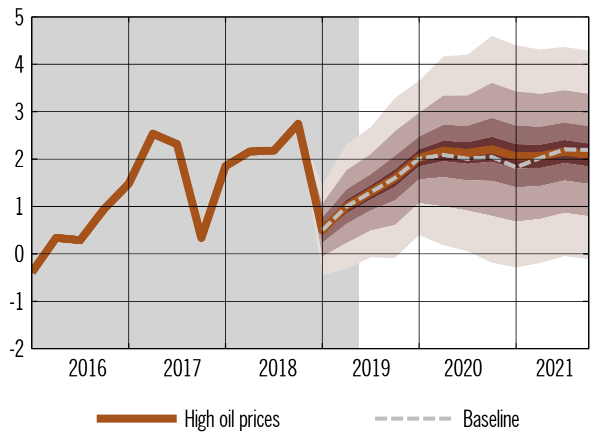
Note: nominal Urals crude prices.
Source: Bank of Russia calculations.

INFLATION
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 1.2.2



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 uncertainty of inflation.
Source: Bank of Russia calculations.

GDP GROWTH RATE
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 1.2.3



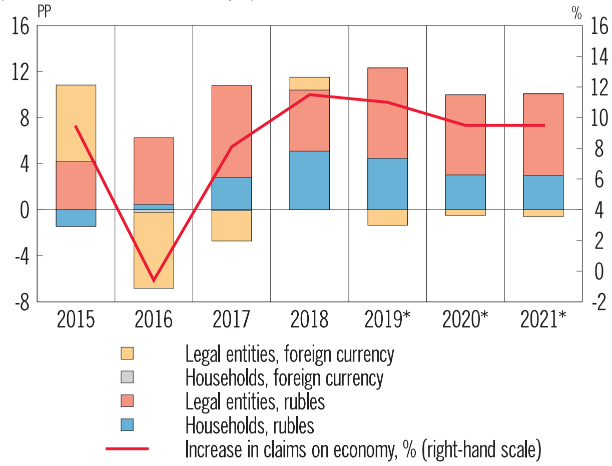
Note: shaded areas on the forecast horizon show the probability of different GDP growth values. Colour gradation reflects probability intervals. Confidence intervals are symmetrical and based on historical estimates of uncertainty of GDP growth rate.
Source: Bank of Russia calculations.

that will provide additional support to business sentiment, consumer and investment activity (Chart 1.2.3). As the oil price in both scenarios will remain relatively stable, its further dynamics will not have any significant additional effect on GDP growth.

Monetary indicators. The dynamics of credit and monetary aggregates will stay generally close to baseline scenario levels and will not pose any risks for price and financial stability (Chart 1.2.4). There will be a slight difference in the growth rate of the banking system's claims on the economy in 2019. They will be a bit higher than in the baseline scenario following income dynamics that will grow somewhat faster in the context of higher oil prices. Retail lending will demonstrate a smoother slowdown in 2019–2020. Additionally, on the back of a faster expansion of the banking system's net foreign assets under the high oil price scenario, the growth in money supply over the forecast horizon may slightly exceed the growth in claims on the economy, therefore being higher than in the baseline scenario.

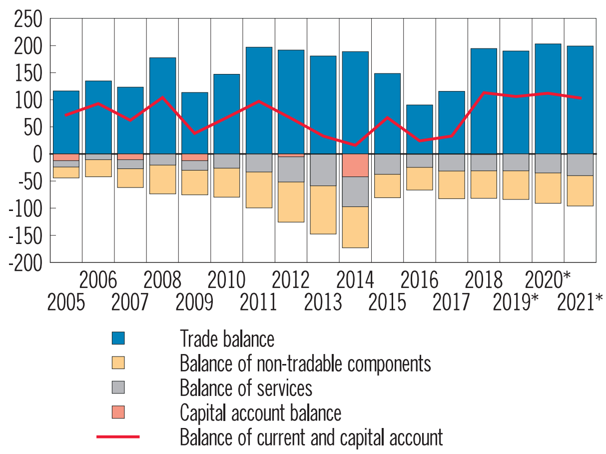
Balance of payments. As in March, the difference between the balance of payment indicators of the high oil price scenario and the ones of the baseline scenario is due to the marked positive effect of higher global oil prices on export volumes in 2019 – 2021. The deviation from the baseline scenario is higher in the second half of the forecast horizon, where the difference in assumptions with respect to global oil prices between the scenarios is growing. The current account balance (Chart 1.2.5) over the entire forecast horizon will exceed the baseline scenario and amount to approximately 5–6% of GDP in 2019–2021. The private sector financial account balance (Chart 1.2.6) will also be higher than in the baseline scenario: it will amount to 3% of GDP in 2019, 2% of GDP in 2020, and slightly above 1% of GDP in 2021. This will be facilitated by a slightly greater expansion of foreign assets held by Russian companies and banks amid a more significant increase in export revenues. The high oil price scenario also assumes that international reserves will show a more sizeable increase compared to baseline scenario projections due to more significant fiscal rule-based foreign currency purchases in the context of higher oil prices.

DECOMPOSITION OF INCREASE IN CLAIMS ON ECONOMY IN HIGH-OIL-PRICE SCENARIO *Chart 1.2.4*
(CONTRIBUTION TO ANNUAL GROWTH, PP)



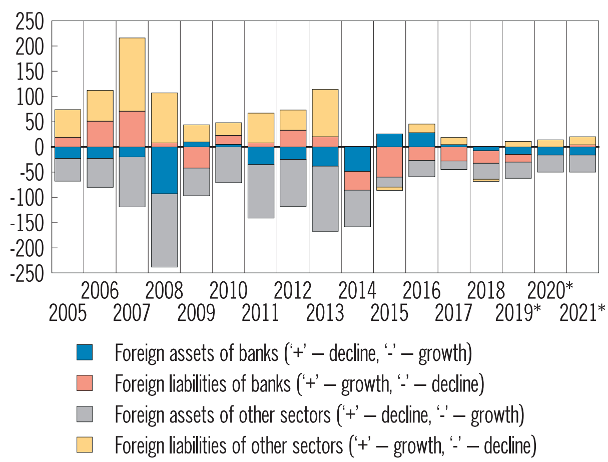
** Forecast. Decomposition is shown for the increase in claims on the economy corresponding to the middle of the forecast range in high-oil-price scenario.*
Source: Bank of Russia calculations.

MAJOR CURRENT ACCOUNT COMPONENTS IN HIGH-OIL-PRICE SCENARIO *Chart 1.2.5*
(BILLIONS OF US DOLLARS)



** Forecast in signs according to BPM6.*
Source: Bank of Russia.

MAJOR PRIVATE SECTOR FINANCIAL ACCOUNT COMPONENTS IN HIGH-OIL-PRICE SCENARIO *Chart 1.2.6*
(BILLIONS OF US DOLLARS)



** Forecast.*
Source: Bank of Russia.

1.3. RISK SCENARIO

FORECAST ASSUMPTIONS

External conditions. The assumptions of the risk scenario have been slightly tightened as compared to Monetary Policy Report 1/19. In particular, they provide for a deeper oil price downturn in the acute crisis phase that was moved to 2019 H2 – 2020 H1. They still suggest a significant deterioration in external conditions over the entire forecast horizon.

The risk scenario implies a significant global economic slowdown, which is both long and cyclical. This may be accompanied by increased volatility in global financial markets, a significant decline in global risk appetite, and a drop in global oil prices to $20 per barrel (in the most acute crisis phase) due to lower global demand for energy commodities. The further consolidation of global oil prices at $35 per barrel in this scenario will be also conditioned on supply-side factors and related to the deteriorating coordination of oil production within OPEC+ and a significant non-OPEC production growth. Such serious changes in external conditions will have an especially adverse effect on emerging markets, including Russia. Similar to other developing economies, the Russian economy will face worse economic growth prospects in the risk scenario, a significant increase in its country risk premium, and higher capital outflows. An additional factor increasing the scale of capital outflow is the further escalation of geopolitical tension as expected in the risk scenario. The fiscal rule will also smooth the impact of deteriorating trade terms on public finance, the economy and the exchange rate.

MEDIUM-TERM FORECAST

Inflation. Similar to the risk scenario in Monetary Policy Report 1/19, the inflation forecast provides for its short-term material acceleration with a subsequent return to 4% over the horizon of about 1–1.5 years. The accelerated capital outflow in the assumption of the deterioration of external conditions in the end of 2019 will exert a downward pressure on the current account and, correspondingly, may result in a short-term weakening of the ruble and the growth of exchange rate and inflation expectations. As a result, in 2019, if the risk scenario materialises, inflation may increase to levels materially exceeding the baseline scenario. However, taking into account the decreased sensitivity of domestic prices to changes in external factors, including in the context of consistent implementation of inflation targeting, the price growth rates in 2019 – early 2020 will be materially lower than during the turbulent period of 2014–2015. Nevertheless, a tightening of the monetary policy will be necessary in order to limit the deviation of inflation from the target. In the case of a timely response of the monetary policy, annual inflation will return to the Bank of Russia's target of near 4% by the beginning of 2021.

Economy. Deterioration of external conditions in the end of 2019 within the risk scenario framework, including a substantial decrease in external demand, will become the reason for a short-term economic slowdown. For that reason, the GDP growth rate in the risk scenario will become materially negative in 2020. The GDP response to the realisation of external risks will be somewhat longer than the inflation response. In 2021, as the economy adjusts to the new external conditions, it will start recovering.

2. INFLATION AND INFLATION EXPECTATIONS

In March 2019, annual inflation reached a local high (5.3%), and in April it started decreasing reaching 5.1% in May. The median of distribution of annual consumer price growth in May decreased for the first time since last August. The exhaustion of the effect of the VAT hike, the strengthening of the ruble, and motor fuel price regulation contributed to the slowdown of annual inflation. The proinflationary effect of individual one-off factors was also limited by proactive decisions of the Bank of Russia to increase the key rate in September and December 2018. Annual growth in non-food goods prices slowed down, while the growth rate of service prices remained practically unchanged. At the same time, food inflation grew slightly in May due, among other reasons, to base effects. Core inflation continued to grow, primarily due to food inflation components.

The monthly growth rate of consumer prices in March – April (adjusted for seasonality) was lower than in late 2018 – early 2019. It increased in May, to a great extent due to the growth rate of food prices.

In April – May 2019, business price expectations continued to decrease. Household inflation expectations remained stable at 9.3–9.4%. The Bank of Russia continues to assess inflation expectations as elevated and not anchored around 4%. Professional analysts expect that inflation will return to levels corresponding to the Bank of Russia's target in 2020 Q1. Estimates of long-term inflation expectations of financial market participants were decreasing, gradually approaching 4%.

According to the Bank of Russia's forecast, inflation will continue to slow down in 2019. At 2019 year-end, it will be 4.2–4.7% and hold near 4% thereafter.

Annual inflation reached a local peak of 5.3% in March 2019 and started decreasing in April (Chart 2.1), which corresponds to the Bank of Russia's forecast.[1] It amounted to 5.1% in May. The exhaustion of the effect of the VAT hike, the strengthening of the ruble, and the regulation of retail prices of petroleum products were the primary factors in inflation slowdown. The effect of one-off proinflationary factors was also limited by the Bank of Russia's decisions about proactive key rate increase in September and December 2018.

Annual growth of non-food goods prices slowed down, while service prices remained generally stable. Annual food inflation in February – April remained unchanged (5.9%) and increased in May to 6.4%, mainly due to base effects. Prices for the main groups of food products showed mixed dynamics, forming under the influence of specific factors.

This affected annual core inflation. In March – May, it grew by 0.1 pp and amounted to 4.7%, primarily owing to food inflation components. At the same time, the median value of annual price growth decreased (to 4.5%) for the first time since last August (Chart 2.2). The share of goods and services that rise in price much faster than the CPI continued to decrease. The convergence of price growth rates is indicative of the cessation of the effect of one-off factors, which, in turn, forms prerequisites for the subsequent slowdown of inflation.

According to estimates, the monthly growth of consumer prices, adjusted for seasonality, in February – March was close to 0.3%, which is the lowest value since last August (Chart 2.3). It accelerated to 0.4% in May, mainly due to the acceleration of price growth of certain food types.

Monthly core inflation and other price dynamics indicators, net of volatility components (e.g., growth in prices for non-food goods excluding oil products, core inflation excluding food products) and seasonally adjusted, in March – May were close to 4% YoY.

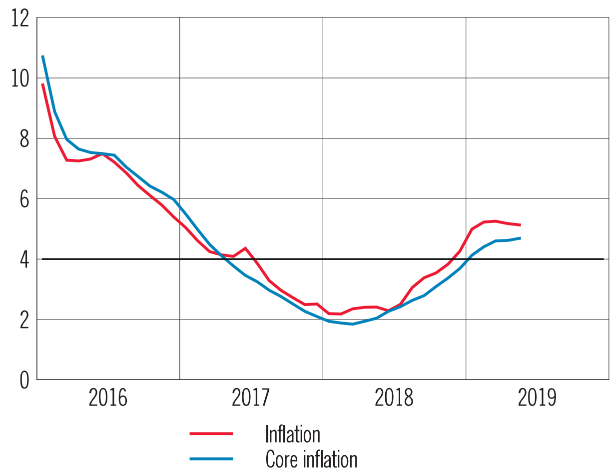
According to estimates made based on Rosstat's latest update, annual inflation as of 10 June is estimated at 5.0%.[2]

[1] Monetary Policy Report 1/19.

[2] As of 17 June, 4.9–5.0%.

INFLATION AND CORE INFLATION
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)

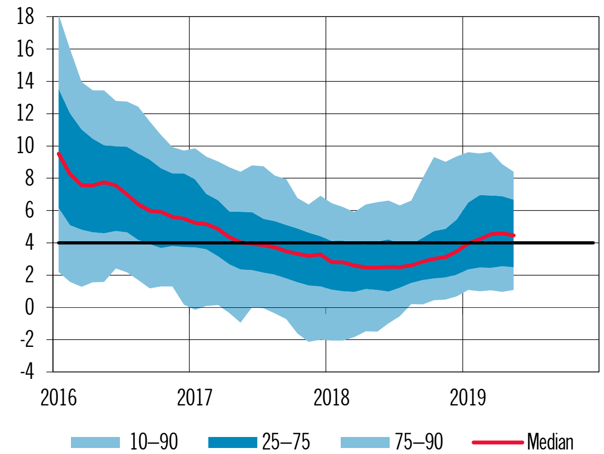
Chart 2.1



Source: Rosstat.

DISTRIBUTION OF GOODS AND SERVICES PRICE GROWTH
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)

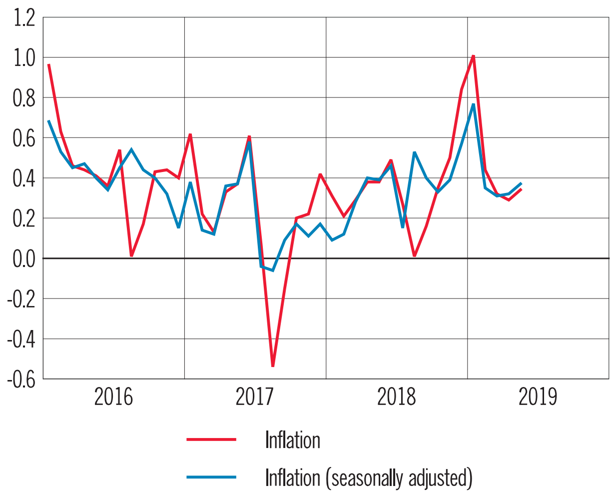
Chart 2.2



Sources: Rosstat, Bank of Russia calculations.

INFLATION
(PER CENT CHANGE ON PREVIOUS MONTH)

Chart 2.3



Sources: Rosstat, Bank of Russia calculations.

Pursuant to the Bank of Russia's baseline forecast, annual inflation will continue to decrease in 2019. At year-end, it will be 4.2–4.7% and hold near 4% thereafter.

FOOD PRODUCTS

In February – April 2019, the monthly growth of prices for food products (seasonally adjusted) was in the range of 0.3–0.4% after an increase in December 2018 – January 2019 (Chart 2.4). In that period, annual food inflation was 5.9% (Chart 2.5).

In May, monthly growth rate of food prices increased to 0.5%, while the annual growth rate increased to 6.4% (due, among other things, to base effects in the fruit and vegetables market).

In March – April, the monthly growth of prices for food products excluding fruit and vegetables (seasonally adjusted) remained the same as in February (according to estimates, 0.3%). In May, it accelerated to 0.5%.

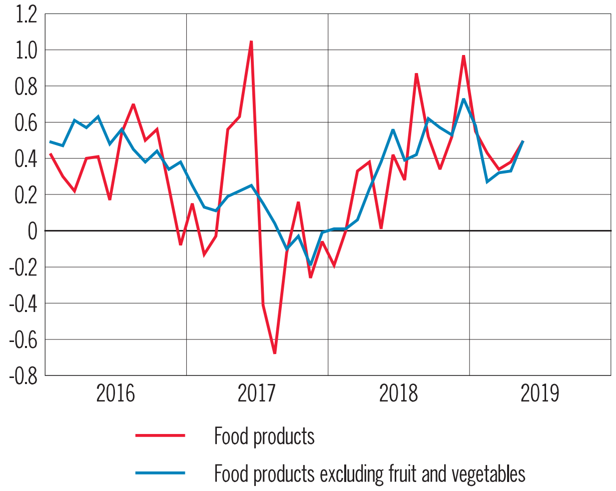
The growth of food prices is expected to slow down in the next few months. The adjustment of supply of some food products to demand, which caused an increase in price growth rates in 2018 H2 – early 2019, has nearly completed. Favourable weather conditions also point to a good harvest. Earlier ripening of fruit and vegetables may result in a shift of summer seasonality of the food inflation to earlier dates.

Fruit and vegetables (weight in the CPI: 4.0%). In March – April of the current year, the annual growth rate of prices for fruit and vegetables was quite stable (Chart 2.6), while the monthly rate (seasonally adjusted) was moderate (0.4–0.6%).

In May, the monthly growth rate of prices for fruit and vegetables (seasonally adjusted) decreased to 0.2%. Under the influence of the base effect, the annual rate accelerated to 9.7% (by 3.6 pp). Last May saw prices for fruit and vegetables go down under the influence of one-off supply-side factors (such as receiving cheap new-harvest potatoes from Egypt with residue domestic products still in stock and the drop in global prices of bananas).

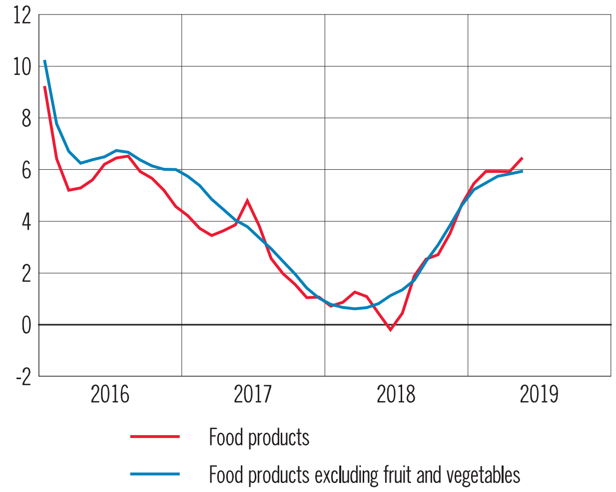
The prices for vegetables in the 'borsch basket' were significantly higher in the first months of 2019 than in the comparable period of 2018. This was caused by diminished ground vegetables harvest in Russia and Europe and increased import

GROWTH OF FOOD PRICES
(PER CENT CHANGE ON PREVIOUS MONTH, SEASONALLY ADJUSTED)
Chart 2.4



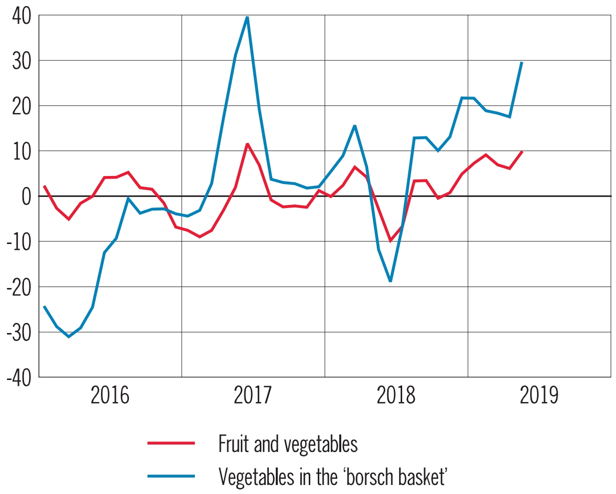
Sources: Rosstat, Bank of Russia calculations.

FOOD PRICES
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)
Chart 2.5



Source: Rosstat.

GROWTH OF FRUIT AND VEGETABLE PRICES
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)
Chart 2.6



Sources: Rosstat, Bank of Russia calculations.

prices. In May, the gap increased due to the low base effect.[3] This year, the Russian Ministry of Agriculture forecasts that the harvest of ground vegetables will equal that of the last year while the harvest of greenhouse vegetables will increase. In these circumstances, no further steady growth of vegetable and fruit prices is expected.

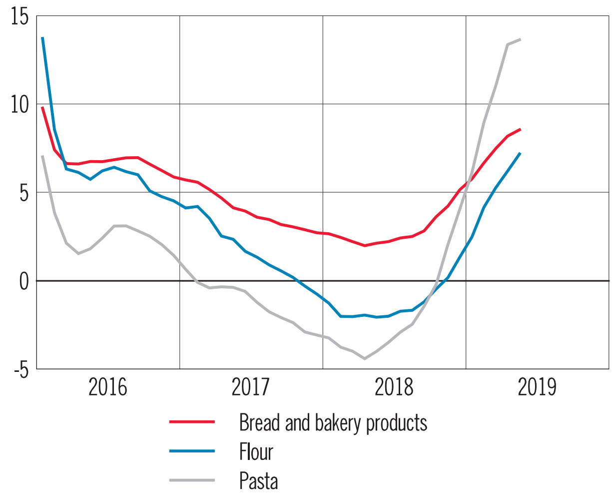
Food products excluding fruit and vegetables (weight in the CPI: 33.6%). Annual growth rates of prices for food products (excluding fruit and vegetables) continued to increase (to 5.9% in May after 5.5% in February), which was caused, among other things, by base effect.

The most noticeable increase in March – May was observed in the annual growth of prices for grain products (cereals and beans, bread, bakery products and pasta; Chart 2.7–2.8). This was caused by an increase in grain prices in the second half of last year after their fall over the course of two years amid record harvests and decreasing business profitability.[4] The price of millet went up most of all (twofold) due to shrinking crop areas. However, the year-to-date decline in domestic and global grain prices, and the forecast of good harvest in Russia[5] and main exporters pave the way to an overall slowdown in growth of grain product prices.

In March – May, the monthly (seasonally adjusted) and annual growth of prices for dairy products (including milk) and cheeses observed since the second half of 2018 continued (Chart 2.9). That resulted partly from measures designed to improve the sector's profitability, including import restrictions. Moreover, global prices for dairy products imported by Russia (milk powder, butter) have been rising since the beginning of the year amid expectations of a decrease in supply from major producers (New Zealand and Australia) due to droughts. In May, FAO Dairy Price Index approached a five-year high. Market adjustment to the inclusion of dairy products in Mercury, an electronic veterinary certification system, starting 1 July may be an additional factor in the growth of prices for dairy products.

BREAD, FLOUR, AND PASTA PRICES
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)

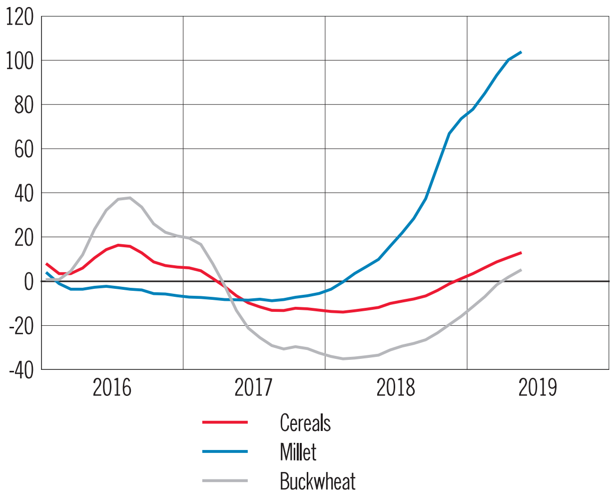
Chart 2.7



Source: Rosstat.

CEREALS
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)

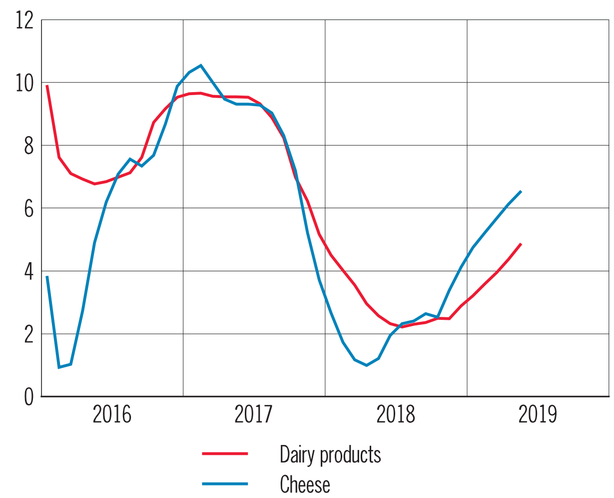
Chart 2.8



Source: Rosstat.

DAIRY PRODUCTS
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)

Chart 2.9



Source: Rosstat.

[3] On the dynamics of prices for fruit and vegetables in May 2018 (see Monetary Policy Report 2/18).

[4] See Monetary Policy Report 2/18.

[5] The current cereal crop forecast of the Ministry of Agriculture stands at 118 million tonnes, which exceeds the 2018 figure by 5%. Market experts and analysts also expect larger crops.

However, the increase in prices was moderate. In May 2019, dairy products (including milk) were 4.8% more expensive, and cheese was 6.5% more expensive than in May 2018.

Simultaneously in different markets, there are signs that the adjustment of demand to supply is complete. For example, annual price growth rates for main types of meat (pork and poultry), eggs and sugar decreased as compared to February; these rates accelerated significantly in the second half of last year (Chart 2.10). Price growth rates for beef are still increasing.

NON-FOOD PRODUCTS

In March – May 2019, the monthly growth rate of prices for non-food goods (seasonally adjusted) stabilised at the lowest level since last August (slightly above 0.2%; Chart 2.11). This was caused partly by the regulation of prices of key types of motor fuel. The exhaustion of the effect of the VAT hike and the strengthening of the ruble contributed to the slowdown of the growth of prices for other commodity groups.

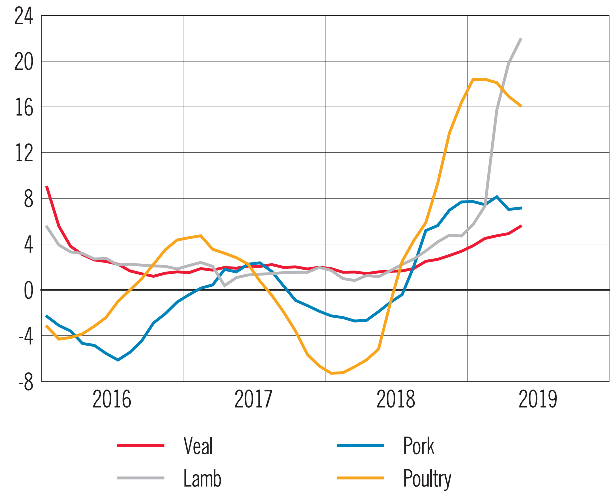
Annual inflation in the non-food goods market has been slowing down since April and reached 3.8% in May (0.9 pp lower than in March; Chart 2.12). Base effects in the retail oil product market made a significant contribution to its decrease.

Motor fuel (weight in the CPI: 4.4%). Since the beginning of the year, prices for key types of motor fuel have been under the influence of agreements between the Government of the Russian Federation and major oil companies. In March – May, prices for petrol rose by 0.1%, while diesel fuel prices decreased by 1.7% (due, among other reasons, to the switch to summer fuel; Chart 2.13).

The annual growth rates of petrol and diesel fuel prices slowed down most noticeably in May (by 5.5 and 5.9 pp respectively, as compared to April), which was driven by base effects (in April – May 2018, prices for motor fuel increased noticeably).

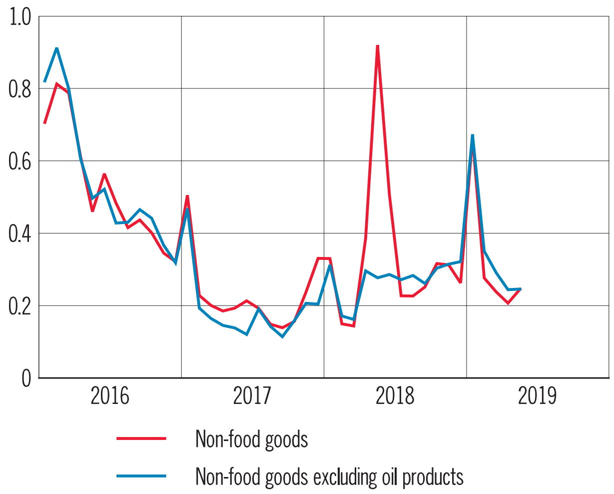
Prices for gas motor fuel that were not subject to regulation increased by 2.9% in March – May after a downturn in the previous six months. Nevertheless, base effects also contributed to a slowdown of its annual price growth rates.

MEAT PRODUCT PRICES *Chart 2.10*
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)



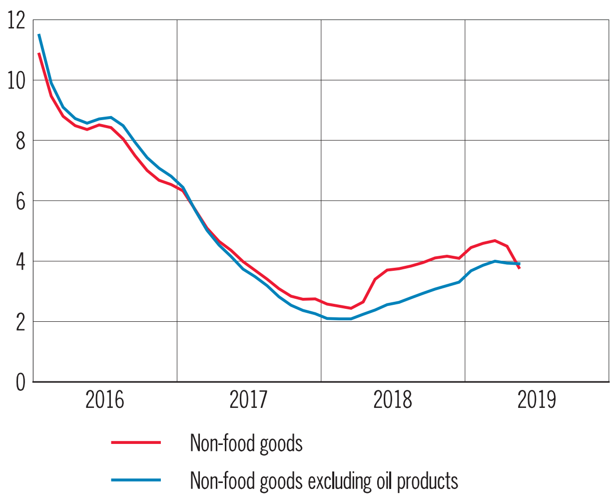
Source: Rosstat.

NON-FOOD PRICES *Chart 2.11*
(PER CENT CHANGE ON PREVIOUS MONTH, SEASONALLY ADJUSTED)



Sources: Rosstat, Bank of Russia calculations.

NON-FOOD PRICES *Chart 2.12*
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)



Sources: Rosstat, Bank of Russia calculations.

Overall, the price movement corresponds to a long-term upward trend in petrol and diesel fuel prices marked by increased volatility.

It is worth noting certain proinflationary risks associated with the growing rates of return of oil product exports since the beginning of the year, which resulted in a rise in wholesale prices (Chart 2.14). They may become apparent in July, upon the expiry of the effect of price restrictions. The dynamics of motor fuel prices will depend on the effectiveness of compensating tools such as the reverse excise tax and the dynamics of global crude and oil product prices.

Other non-food goods (weight in the CPI: 30.5%). The monthly growth rate of prices for non-food goods excluding oil products (seasonally adjusted) has been decreasing since February having reached 0.2% in April – May after an upsurge in January. It slowed down in the context of the exhaustion of the VAT hike pass-through to prices, the strengthening of the ruble, and moderate demand.

Annual inflation in this market segment reached its local peak in March (4.0%) and decreased in April – May for the first time since last April (to 3.9%).

The decrease in price indices for household appliances and electronics, caused, among other things, by the strengthening of the ruble since the beginning of the year, was the most noticeable. At the same time, annual growth rates of prices for household chemicals, perfume and beauty products continued to increase (Chart 2.15).

Mixed price dynamics for individual groups of commodities suggest a dominant role of factors specific for certain markets given the overall exhaustion of the VAT hike pass-through.

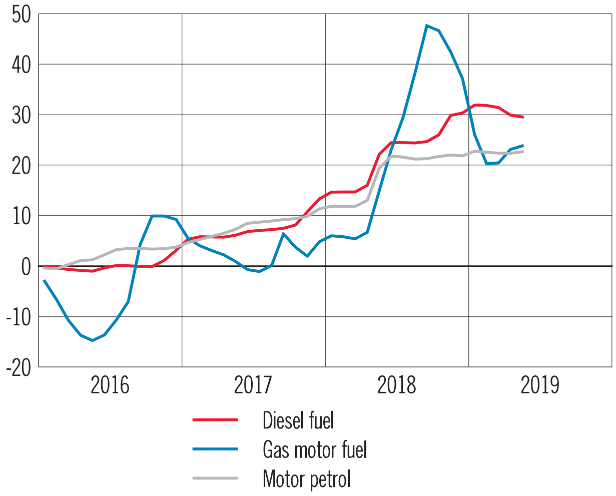
SERVICES

According to estimates, in March – May 2019, the monthly growth of prices for services (seasonally adjusted) was 0.3–0.4% (Chart 2.16). That rate was typical for August – December of the last year. Annual inflation was also stable holding in the range of 5.0–5.1%, same as in January – February (Chart 2.17).

Utility services (weight in the CPI: 10.0%). In March – May, prices for utility services remained practically unchanged, which corresponds to the

GROWTH OF OIL PRODUCT PRICES
(PER CENT CHANGE ON DECEMBER 2015)

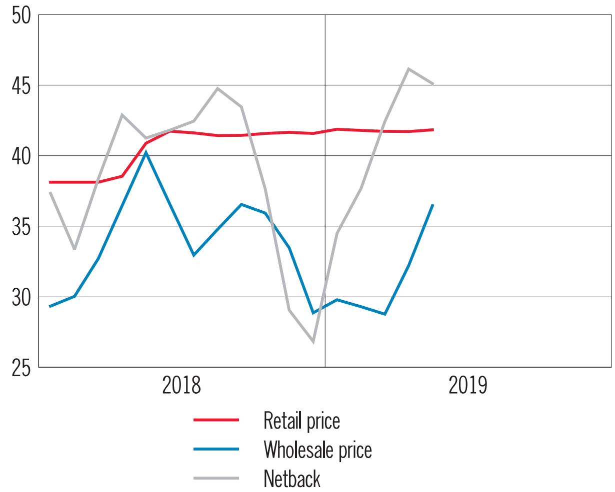
Chart 2.13



Sources: Rosstat, Bank of Russia calculations.

AI-92 PETROL PRICES
(RUBLES PER LITRE)

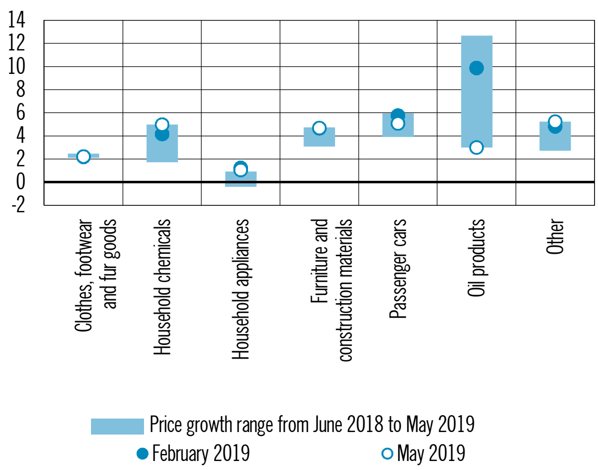
Chart 2.14



Sources: Rosstat, SPIMEX, Bank of Russia calculations.

PRICE GROWTH FOR KEY NON-FOOD PRODUCT GROUPS
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)

Chart 2.15



Sources: Rosstat, Bank of Russia calculations.

schedule for their indexation. Annual inflation, which increased in January due to the VAT hike and increased tariffs for the disposal of municipal solid waste, also remained stable (5.9–6.0%).

It should be noted that annual growth rates of tariffs for utility services will decrease in July: their indexation from 1 July will be lower than a year before and will amount to 2.4%. Subject to the increase in January, the aggregate indexation this year corresponds to last year's value.

Services excluding utility services (weight in the CPI: 17.6%). In March – May, the monthly growth rate of tariffs for services excluding utility services was 0.3–0.4% (seasonally adjusted). Annual inflation reached a local peak in March (4.7%) and then decreased to 4.5–4.6% in April – May.

The dynamics of prices for foreign tourism services, which formed under the influence of the strengthening of the ruble, contributed the most to the slowdown of annual price growth for services. The increase in their price (seasonally adjusted) was significantly less than a year before (when the ruble exchange rate was going down).

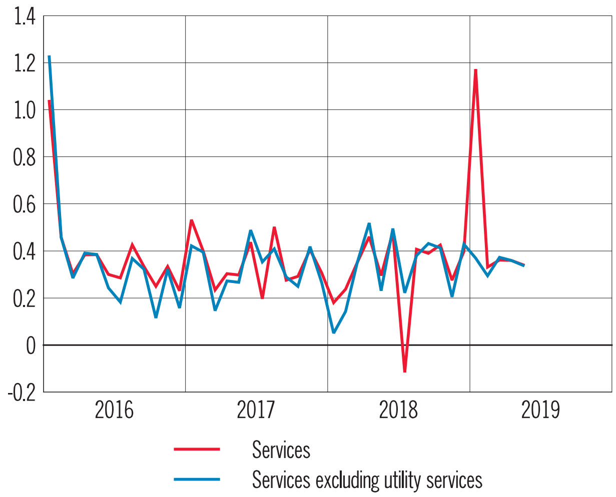
The change in prices for other key services groups was minor in March – May (Chart 2.18). As compared to March, the increase in the annual growth rates of railway fares was the most significant, as a result of differences in fare revisions in the current and past year. Annual growth rates will continue to fluctuate in 2019.

INFLATION EXPECTATIONS

Inflation expectations of economic agents in March – May 2019 remained unchanged or continued to decrease after growth in 2018 H2 – early 2019. Going forward, economic agents expect inflation slowdown.

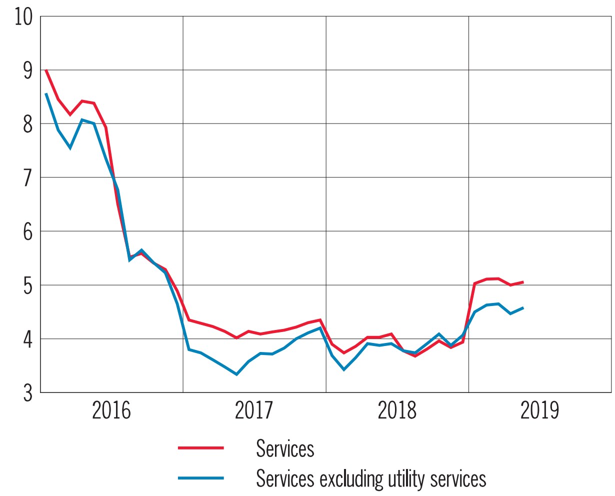
Inflation expectations of households. According to the inFOM surveys commissioned by the Bank of Russia, the median estimate of inflation observed by households remained at the level established in the second half of 2018 (10.0–10.5%; Chart 2.19). At the same time, the frequency of mentioning goods and services whose price increase was perceived as significant went down. This is indicative of prerequisites for a lowering of expectations.

GROWTH OF SERVICES PRICES
(PER CENT CHANGE ON PREVIOUS MONTH, SEASONALLY ADJUSTED)
Chart 2.16



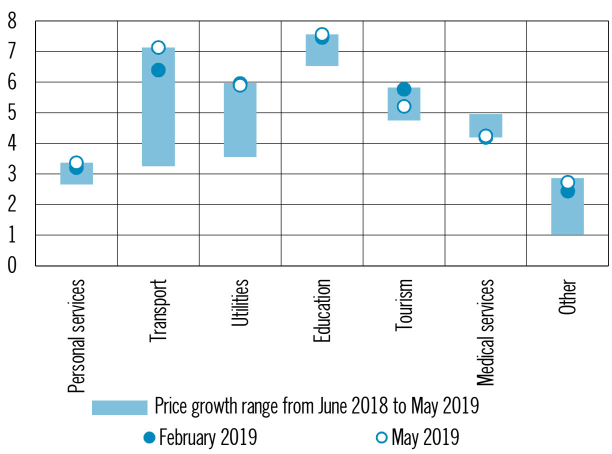
Sources: Rosstat, Bank of Russia calculations.

GROWTH OF SERVICES PRICES
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)
Chart 2.17



Sources: Rosstat, Bank of Russia calculations.

PRICE GROWTH FOR KEY SERVICES GROUPS
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)
Chart 2.18



Sources: Rosstat, Bank of Russia calculations.

Household inflation expectations for the next 12 months in March – May 2019 were lower than in December 2018 – February 2019 (9.1–9.4% vs 10.1–10.4%). According to the responses, increased inflation expectations in that period were caused by a temporary factor, the change in the VAT rate. Despite the decrease, inflation expectations remain higher than in the first half of last year.

In March – May, the gap between actual and expected inflation widened. This indicates that a growing number of respondents perceive the current acceleration of price growth as temporary and expect that it will slow down.

Business inflation expectations. According to business surveys conducted by the Bank of Russia,[6] in March – May 2019, companies' price expectations for three months ahead decreased to the level observed in the middle of the last year (Chart 2.20). The rate of this decline was slowing down as compared to February. This is indicative of the exhaustion of the effect of the VAT hike and the weakening of the ruble in late 2018, which caused a temporary upsurge of inflation expectations in January.

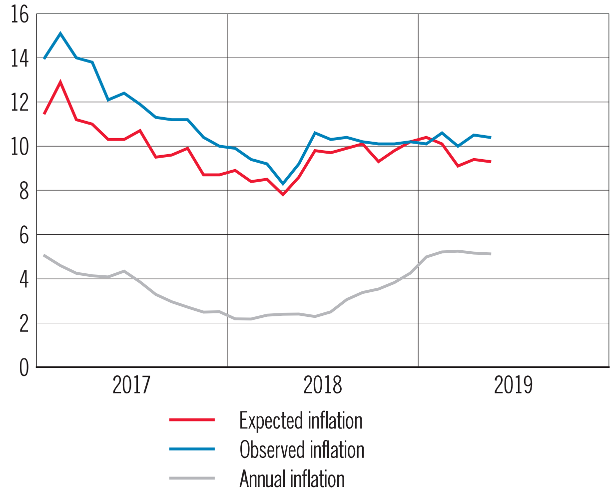
Expectations declined relatively homogeneously in different sectors most noticeably in the wholesale, pharmaceuticals and food industries. The strengthening of the ruble and the slowdown of cost increases were named most often as the primary factors for lowering of expectations.

At the same time, inflation expectations in the agriculture increased. Representatives of companies associated it with higher global prices for meat and dairy products.

Inflation expectations of professional analysts. In March – May 2019, inflation expectations of experts with respect to inflation in the end of 2019 changed insignificantly. That said, both analysts and the Bank of Russia believe that the acceleration of inflation is temporary in nature. Their forecasts suggest that annual inflation is set to begin to decline from 2019 Q2 to return to the near 4% level in 2020 Q1 (Chart 2.21).

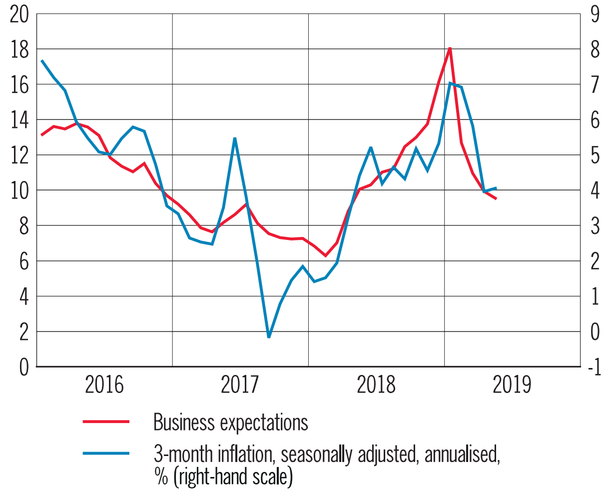
[6] *For survey details, see http://www.cbr.ru/Content/Document/File/62 829/analysis_18–12.pdf. The aggregate index is a balanced representation of responses, i.e. the difference in the share of respondents who expect prices will increase and those expecting prices to decrease.*

INFLATION OBSERVED AND EXPECTED BY HOUSEHOLDS *Chart 2.19*
(MEDIAN ESTIMATE, %)



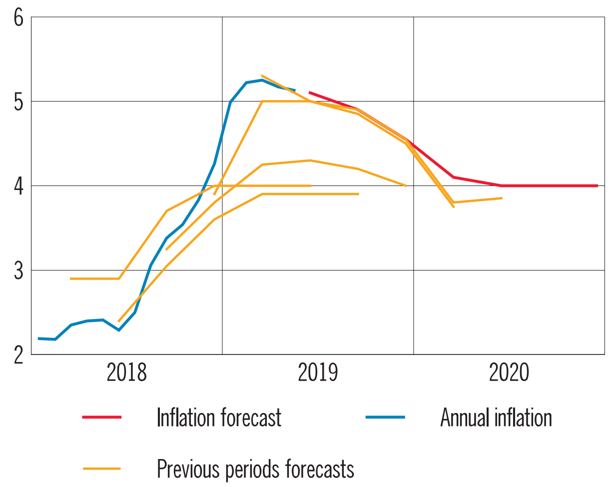
Sources: Rosstat, inFOM.

BUSINESS PRICE EXPECTATIONS *Chart 2.20*
(BALANCE OF RESPONSES, PP)



Sources: Bank of Russia, Rosstat.

INFLATION FORECAST DYNAMICS *Chart 2.21*
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)



Sources: Bloomberg, Rosstat.

3. MACROECONOMIC CONDITIONS

The external conditions for the development of the Russian economy in Q1 and the first two months of 2019 Q2 were generally favourable. The global economy was stable, and external price pressure was low. The Urals crude price exceeded the baseline scenario values in Monetary Policy Report 1/19. Monetary authorities in many countries took a break from tightening their policy. Country risk premiums remained stable.

Russian FX and stock markets looked better than those of other EMEs. The ruble exchange rate was slightly stronger than the Bank of Russia had expected. Despite the fact that deposit interest rates stopped rising in March – April, ruble deposits continued to increase, with long-term deposits growing at a faster pace. Interest rates continued growing in the loan market. However, interest rate growth slowed down in March in most market segments, and a number of large banks reduced mortgage rates in April – May. During the first months of this year, corporate lending growth remained low.

In 2019 Q1, GDP growth slowed down and reached a level below the Bank of Russia's expectations. The slowdown was primarily caused by certain temporary factors, such as the reaction of demand to the VAT hike and the adjustment of inventories. Moreover, according to estimates, fiscal policy made a negative contribution to the aggregate demand in early 2019. Data for 2018 Q4 – 2019 Q1 are also indicative of a more-than-expected slowdown in the export growth due to lower global economic growth.

In March – April 2019, annual industrial output growth rates were close to late 2018 – early 2019 level. Investment activity remained low, while consumer demand was moderate. Its expansion was prevented by a decline in real disposable income that was only partially compensated by the continued high growth of retail lending.

According to Bank of Russia's forecast, in Q2–Q3, Russian economy's growth will accelerate due to the expansion of consumer activity as the effect of temporary factors is exhausted, the implementation of national projects intensifies, and public investment grows.

The improvement of companies' financial standing will encourage the expansion of investment activity: the profit and loss balance in Q1 reached a multi-year high, while the debt burden remained practically unchanged.

3.1. EXTERNAL CONDITIONS AND BALANCE OF PAYMENTS

GLOBAL ECONOMY

Economic growth worldwide. In the first half of this year, the global economic environment stabilised in the context of a pause in normalisation or a certain softening of the monetary policy in a number of major economies (such as the US and China) amid preservation of moderate inflation.

In 2019 Q1, the slowdown of growth stopped, both in advanced (AEs) and emerging market economies (EMEs). Annual GDP growth rates in a number of Russia's important trade partners, such as China (6.4%) and the euro area (1.2%), were above the forecast and remained at the previous quarter's level. Germany, the leading economy of the euro area, transitioned from stagnation to growth (0.4% QoQ) on the back of the recovery of the motor vehicle industry and exports and in response to the implementation of fiscal incentives (budget expenditures on infrastructure, education, housing construction and digital technologies in 2019, according to Bundesbank estimates, will amount to 0.25–0.5% of GDP).[1]

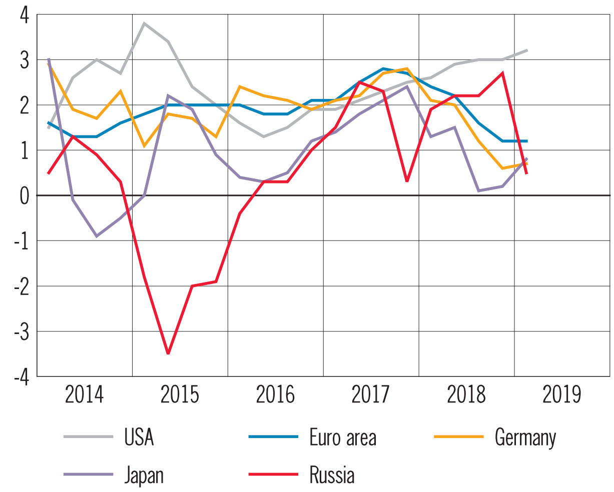
In the US, annual GDP growth rates remain high (3.2% YoY in Q1 vs 3% in the previous quarter). The government shutdown earlier this year did not have a material effect on the economy.

At the same time, Q1 saw a slowdown of annual growth rates in other major economies, such as India (from 6.6 to 5.8%), Brazil (from 1.1 to 0.9%), Mexico (from 1.7 to 1.3%), South Korea (from 3.1 to 1.8%), and South Africa (from 1.1 to 0%).

There are still risks of a global economic slowdown, primarily associated with trade controversies. On 10 May, the US decided to raise tariffs from 10 to 25% on Chinese exports amounting to 200 billion of US dollars. In response, China intends to introduce higher duties on US exports that amount to 60 billion of US dollars. PMIs and other statistical data indicate that the situation in the main global economies in April – May remained ambiguous. In China, the composite PMI decreased from 52.7 to 51.5 points in May.

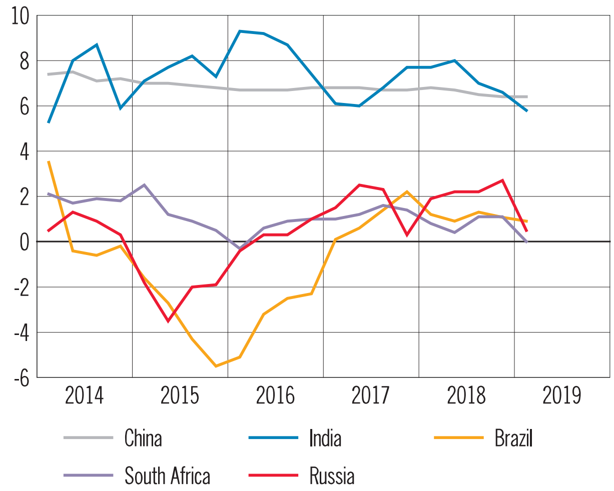
[1] In 2018–2022, the cumulative fiscal impulse in Germany will amount to 2.8% of GDP.

GDP GROWTH RATE: ADVANCED ECONOMIES AND RUSSIA
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 3.1.1



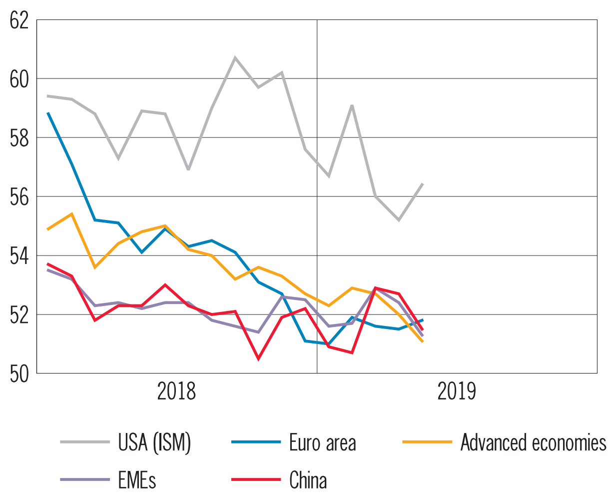
Source: Bloomberg.

GDP GROWTH RATE: EMES AND RUSSIA
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 3.1.2



Source: Bloomberg.

DYNAMICS OF PMI COMPOSITE
(POINTS)
Chart 3.1.3



Source: Bloomberg.

The data are indicative of a slowdown in industrial output (to 5% YoY from 8.5% in March and from 5.4% in April respectively). At the same time, retail sales recovered to 8.6% YoY (vs 7.2% in April). In the euro area, economic activity is supported by the services sector: the composite PMI remained in the range of 51.5–51.8 points in March – May, while the manufacturing PMI has remained below 48 points for three months in a row. In the US, where the economic activity dropped in February – March from high to normal levels and the effect of the fiscal stimulus is being gradually exhausted, a cooling of the economic activity was noted in May. The composite indicator calculated by IHS Markit decreased from 53 to 50.9 points, and PMI ISM stabilised at 56.4 vs 55.2 points in April; new job rates slowed down in May.

Inflation worldwide. Although external inflationary pressure increased slightly in March – April, it still remained quite low, both in AEs and in most EMEs (Charts 3.1.4, 3.1.5). A rise in oil prices is not resulting in acceleration of inflation YoY, as prices are nominally close to last year's levels. Combined with the stabilisation of the growth rates of major economies, this leads to the preservation of moderate inflationary pressure. For countries where the statistics have already been published, a slowdown of price growth in May is observed.

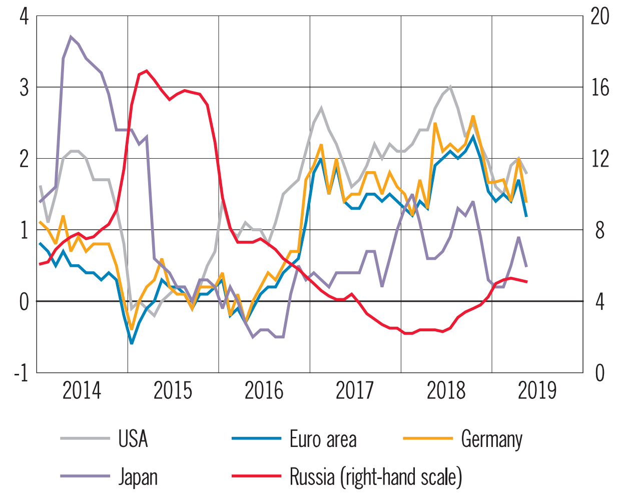
In the US, inflation in May amounted to 1.8% YoY as compared to 2.0% in April and 1.9% in March. In the euro area, inflation accelerated from 1.4 to 1.7% in April but slowed down to 1.2% in May. In Japan, inflation in May amounted to 0.5% vs 0.9% in April. In major EMEs, inflation in China grew to 2.5% in April from 2.3%, while price growth rates in India remained at 2.9%.

MONETARY POLICIES OF FOREIGN CENTRAL BANKS

In the first half of this year, in response to a slowdown in growth rates and a decrease in growth forecasts for 2019 – 2020 in most countries, monetary authorities ceased the tightening of the monetary policy.

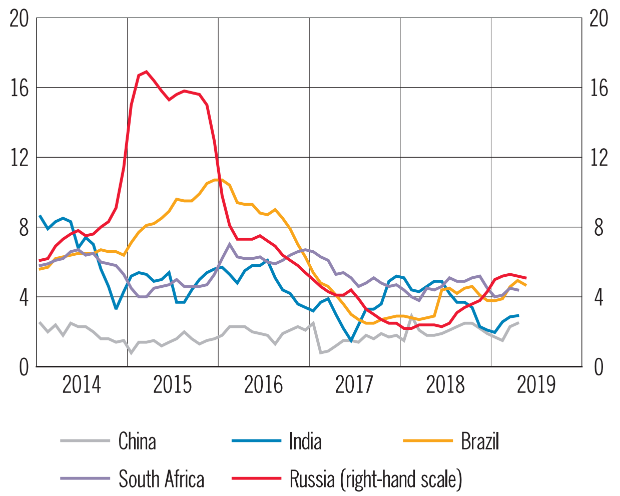
The monetary policy of the US and the euro area. According to the minutes of the US Fed's meeting of 30 April – 1 May, the regulator's representatives remain committed to a pause with respect to changing the key rate until the end

INFLATION: ADVANCED ECONOMIES AND RUSSIA
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 3.1.4



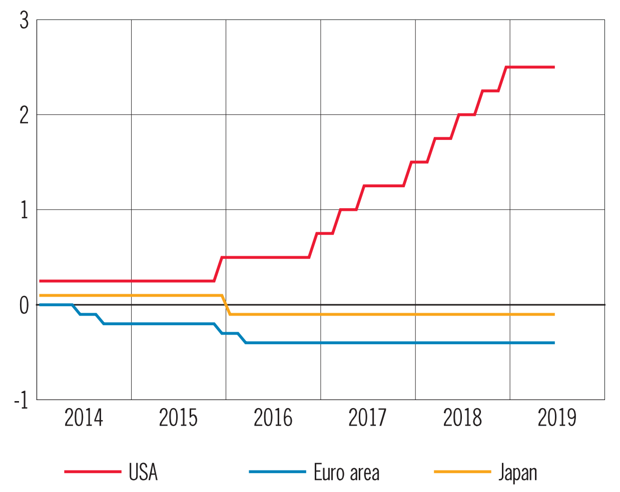
Source: Bloomberg.

INFLATION: EMES AND RUSSIA
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 3.1.5



Source: Bloomberg.

POLICY RATES, ADVANCED ECONOMIES
(%)
Chart 3.1.6



Source: Bloomberg.

of this year. The document does not contain any signals by the US Fed about a potential softening of the policy in 2019, which is already expected by many market participants. At the same time, some US Fed representatives believe that the rate may be decreased due to trade controversies, inflation risks, and the yield curve inversion.

The cutting of the Fed's balance has slowed down. Starting in May, the limit of net repayment of treasury obligations was decreased from \$30 billion to \$15 billion, and reinvestment in these securities will cease in September of this year. Parameters of reinvestment of funds received from repayment of mortgage securities remain unchanged for the time being (\$20 billion per month).

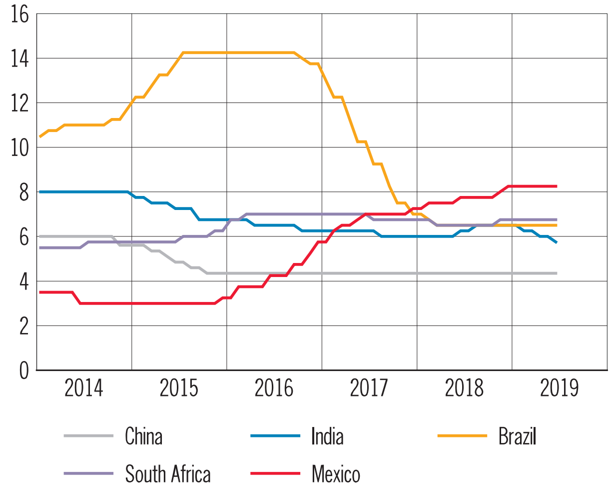
Following the results of the meeting held on 10 April, the ECB did not change its monetary policy parameters and confirmed that the rate would not be increased in the euro area this year. Auctions for the provision of long-term liquidity to the banking sector of the euro area within the framework of the targeted longer-term refinancing operations programme (TLTRO III) will be held in the second half of the year.

Monetary policies in other countries. Other regions conducted mixed monetary policy, and its developments were caused by specific aspects of each country's economic situation. In particular, key rates were increased in March – May in the Czech Republic and Norway (by 0.25 pp to 2% and 1%, accordingly). Rates were decreased (also by 25 bp) in India (twice, to 5.75%), Australia (to 1.25%), Malaysia (to 3%), New Zealand (to 1.5%), and the Philippines (to 4.5%). In Chile, the rate was decreased by 0.5 pp to 2.5%.

GLOBAL FINANCIAL MARKETS

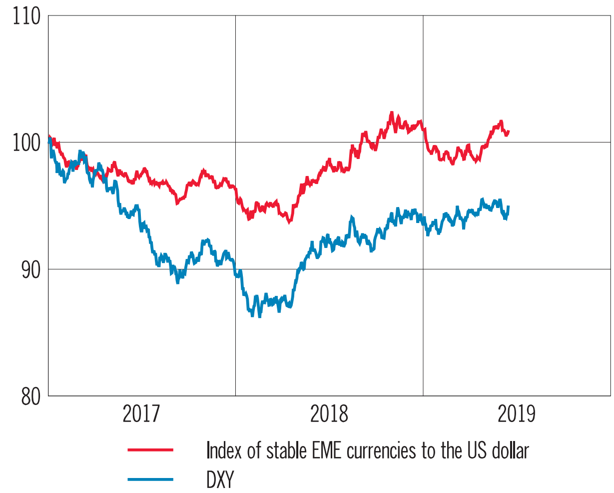
Currencies. Most currencies of both advanced and developing economies were weakening against the US dollar in April – June. Until mid-April, the demand for risky assets prevailed in markets amid the absence of tightening of the monetary policy and more positive than expected economic and companies' reporting data for 2019 Q1. However, while domestic risks were growing in some countries, and after a temporary abandonment of a trade deal between the US and China, there formed a trend toward

POLICY RATES, EMES *Chart 3.1.7*
(%)



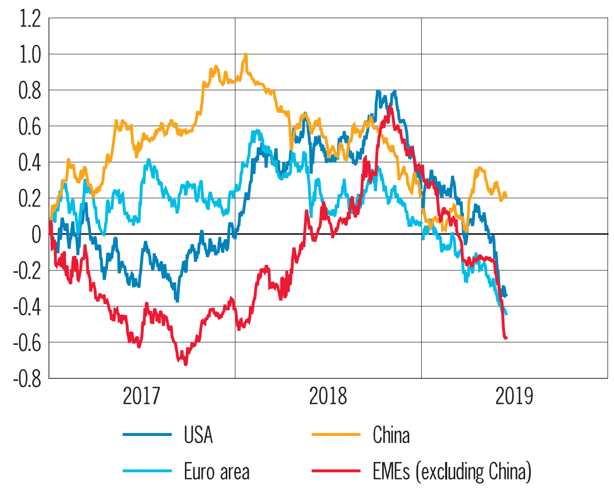
Source: Bloomberg.

US DOLLAR EXCHANGE RATE AGAINST ADVANCED ECONOMIES' AND EMES' CURRENCIES *Chart 3.1.8*
(100 = 02.01.2017)



Sources: Reuters, Bank of Russia calculations.

YIELDS ON 10-YEAR GOVERNMENT BONDS *Chart 3.1.9*
(CHANGE ON 02.01.2017, PP)



Sources: Reuters, Bank of Russia calculations.

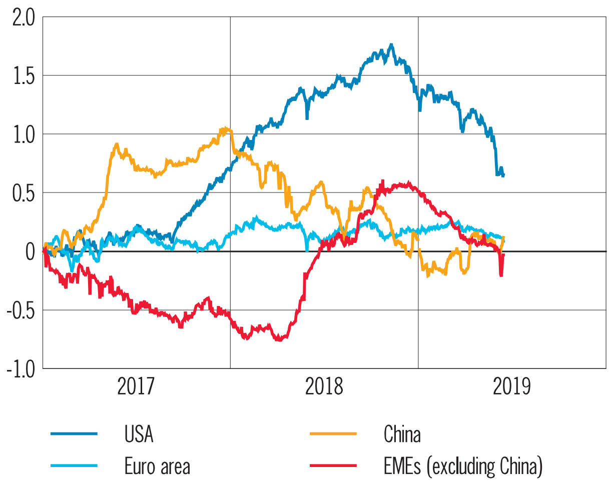
the strengthening of protective currencies. The Argentinian peso and the Turkish lira dropped the most against the US dollar due to remaining internal economic problems. FX rates of Latin American and certain Asian countries that have a material current account deficit, face economic difficulties or risks of deterioration of foreign trade terms also depreciated significantly.

Currencies of advanced economies were also generally weakening against the US dollar in April – May. The exception was the Japanese yen, which strengthened against most world currencies as demand for protective assets grew.

Interest rates. Despite higher-than-expected estimates of economic growth in 2019 Q1 and the improvement of leading indicators in March – April, inflationary pressure remained low in most advanced economies. On the back of the expected stable growth of rates in advanced economies until at least the end of 2019 and the growth of expectations of market participants about further softening of monetary conditions, interest rates were decreasing in most advanced economies. In April – June, yields in the US decreased by 20–50 points along the entire yield curve of public debt in the national currency. In Germany, yields on securities with a maturity of over one year decreased by 7–30 points. In the UK, yields on securities with a maturity of over two years fell by 6–22 points. In France, this decline was 3 to 40 points. Among the advanced economies, a significant yield growth was recorded only in Italy due to remaining fiscal risks. The uncertainty with respect to global risks (Brexit, trade negotiations) and the expectations of a global economic slowdown resulted in a flattening of the yield curve in countries whose debt obligations are traditionally considered protective. In the US, since the end of March, the spread between 10-year and 3-month government bonds did not exceed 20 points, settling below 0 in mid-May. Inversion at this section of the yield curve was recorded for the first time since 2007. In Germany, the similar spread went down 45 points, for the first time since 2008.

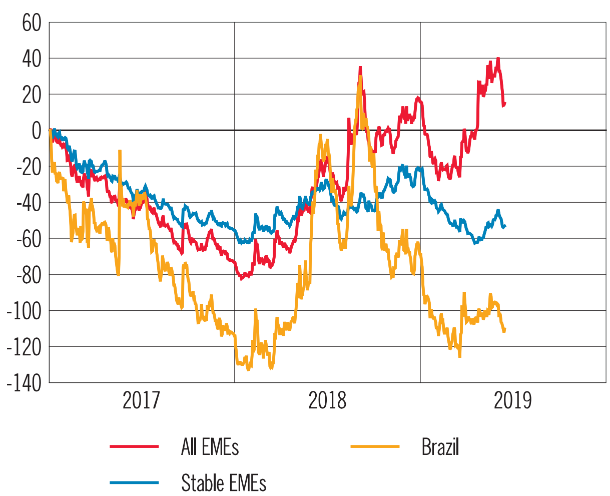
The yield reduction in most advanced economies contributed to a decrease in rates for public debt in stable EMEs. The yield growth in the national currency was only recorded in some

YIELDS ON 2-YEAR GOVERNMENT BONDS
(CHANGE ON 02.01.2017, PP)
Chart 3.1.10



Sources: Reuters, Bank of Russia calculations.

CDS OF EMES
(CHANGE ON 02.01.2017, BP)
Chart 3.1.11



Sources: Reuters, Bank of Russia calculations.

countries, with the most significant increase in Turkey.

Country risk premiums. In advanced economies, the market for credit default swaps remained stable in March – May. The cost of 5-year contracts increased only in Italy due to the remaining uncertainty with respect to the fiscal policy. However, it did not exceed 220 points, which is below local maximums of 2019 Q1.

At the same time, the cost of credit default swaps increased in many EMEs, primarily in countries with significant foreign trade imbalances, low reserves, or economic problems or in countries that may face challenges should new import duties be introduced. Despite the increased cost of contracts, in most countries the cost of insurance against default remained significantly below the levels of 2018 Q3 – Q4.

Stocks. In March and the first half of April, stock markets in both AEs and EMEs continued to grow actively amid favourable global economy data. However, starting in the second half of April, an escalation of trade controversies between the US and China provoked a correction of EME indices. The size of the drop in stock indices of developing countries varied depending on investors' assessment of country risks. Most indices remained above the levels of the beginning of 2019.

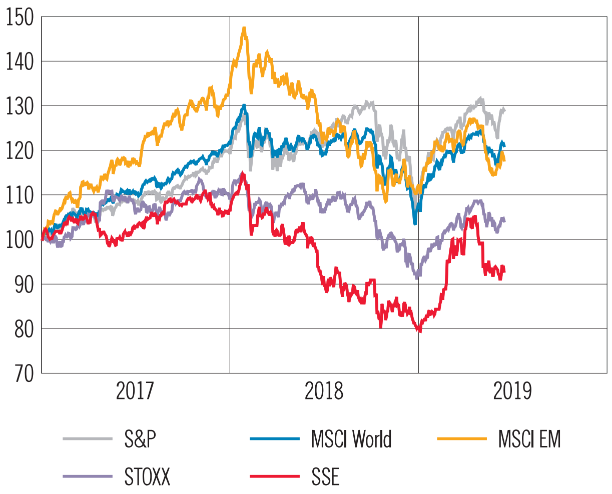
AEs' markets adjusted less than EMEs due to lesser sensitivity to international trade risks. Most AE stock markets transitioned to consolidation in May at levels exceeding those of the beginning of the year by 10% or more.

GLOBAL COMMODITY MARKETS

Oil. Global prices of oil, the primary Russian export commodity, continued growing in April – May 2019. On 25 April, the price for Urals crude oil reached a high of $76 per barrel, and its average price for April – May exceeded $70 per barrel. The main drivers for price support were overfulfilment of obligations for production cuts under the OPEC+ agreement, continued reduction of output in Iran, and reduced export of oil from Venezuela. Moreover, a disruption in supplies of Russian oil through the Druzhba pipeline contributed to a deficit of sulphur-bearing oil. However in the second half of May – the first half of June, the

STOCK INDICES
(100 = 02.01.2017)

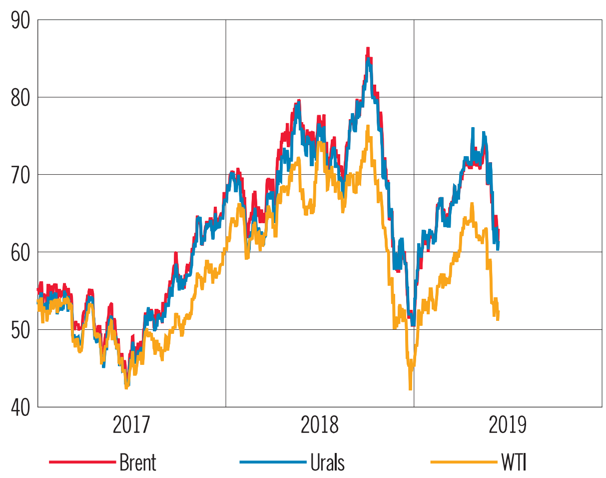
Chart 3.1.12



Source: Reuters.

OIL PRICES
(US DOLLARS PER BARREL)

Chart 3.1.13



Sources: Thomson Reuters, Bloomberg.

price of oil decreased sharply amid increased risks for global demand.

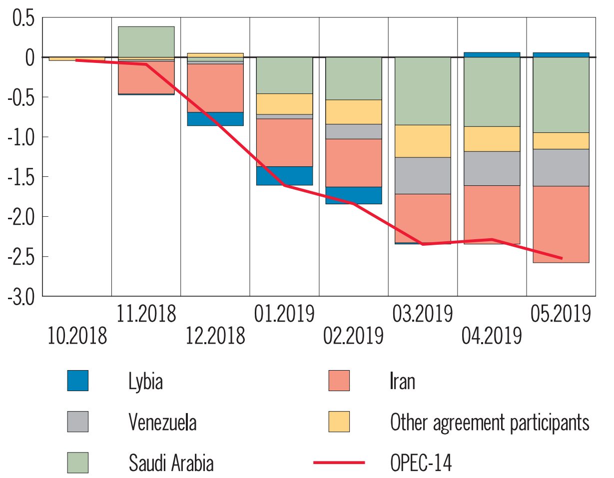
Oil – global demand. In June, the IEA lowered the forecast for the increase in the global demand for oil in 2019 for the second successive month to 1.2 million barrels per day. The US Department of Energy and OPEC in June also worsened the forecasts of global oil consumption. In the context of increased tension in trade relations between the US and China, risks for the economic growth of major oil consumers escalated.

Oil – OPEC+. According to estimates by the Joint Ministerial Monitoring Committee, the arrangement fulfilment level reached 168% in April, and 120% on average in January – April 2019. In May, OPEC's production continued to decline. According to the data provided by OPEC's secondary sources, in May, Saudi Arabia decreased production in excess of obligations under the agreement by 0.6 million barrels per day, i.e. since October 2018, its production has decreased by more than 0.9 million barrels per day. Angola, Kuwait, UAE and some other countries also overfulfilled their obligations. Production cuts by non-OPEC parties to the agreement (Kazakhstan, Russia and other countries) also supported the oil price. According to the data provided by the Russian Ministry of Energy, Russia decreased production in May vs October by about 300,000 barrels per day, i.e. more than it was stipulated by the latest arrangements. Oil supply from Russia was also affected by a temporary suspension of pumping of contaminated oil through the Druzhba pipeline. In addition, measures for purifying the oil and cleaning the pipeline were taken. Supplies are gradually recovering.

Oil – supply from Iran and Venezuela. Oil production decline accelerated in Iran in May 2019 due to the end of easing of requirements provided by the US for importers of Iranian oil. According to OPEC's secondary sources, the production has dropped by 1 million barrels per day since October and by 1.5 million barrels per day since May 2018. Oil supply from Venezuela also decreased amid the termination of its export to the US due to the imposition of US sanctions.

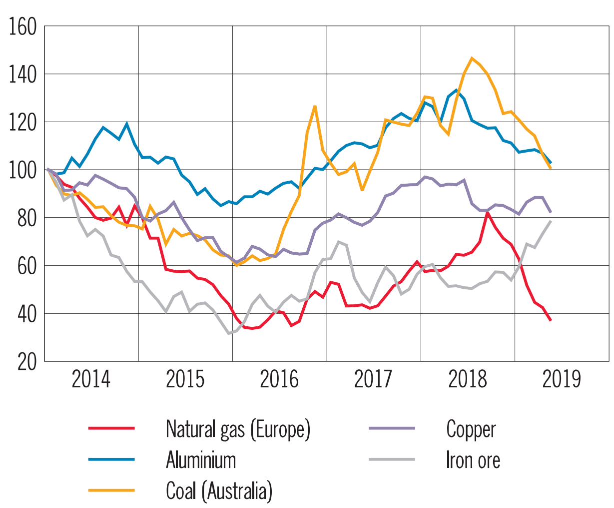
Oil – production outside of OPEC+. Expansion of production in countries outside of OPEC that are not parties to the arrangements partially compensates for the falling output of Iran,

CHANGE IN OPEC CRUDE OIL PRODUCTION SINCE OCTOBER 2018* *Chart 3.1.14*
(MILLION BARRELS PER DAY)



** For Kuwait – since September 2018.*
Source: calculations based on OPEC secondary source data.

WORLD PRICES OF RUSSIAN PRINCIPAL EXPORT COMMODITIES *Chart 3.1.15*
(JANUARY 2014 = 100%)



Source: World Bank.

Venezuela and OPEC+. According to the data provided by the US Department of Energy, the US supply of oil and other liquid fuel has increased by 0.9 million barrels per day since October and by 2.3 million barrels per day since May 2018. Resumed productivity growth at shale deposits on the back of the quick recovery of oil prices during the first five months of 2019 supports US production.

Situation in other commodity markets. The dynamics of world prices for other key Russian export goods were mixed (Chart 3.1.15). In Europe, natural gas continued to cheapen in spring amid growing reserves in the context of a mild winter and significant imports of LNG encouraged by an attractive price differential. World prices for coal also fell to the minimum since mid-2017 on the back of the limited coal consumption in China. At the same time, global prices for iron ore continued to grow due to a disruption of supplies from Australia and Brazil due to breakdowns.

Food products. World prices for food in March – May 2019 remained below the level of March – May of last year. Grain cheapened amid expectations of a larger harvest in 2019. At the same time, many food groups have become more expensive since the beginning of 2019. In May 2019, FAO Composite Food Price Index rose to an 11-month high. World prices for dairy products grew the most on the back of expectations of a seasonal decrease in supplies from Oceania due to drought. The growth of world prices for meat was caused by a sharp increase in China's import amid a decline in domestic production due to the rapid spread of African swine fever. Further increase in global food prices may act as a proinflationary factor.

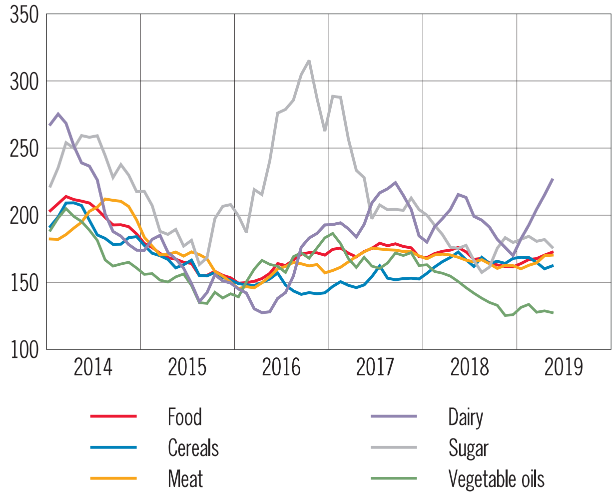
BALANCE OF PAYMENTS

Current account. According to a preliminary estimate, the current account surplus in 2019 Q1 increased by $3 billion to $33 billion.[2] This was caused by an expansion of surplus mainly due to declining imports. In January – May 2019, the current account surplus amounted to $49 billion.

Exports. In 2019 Q1, exports did not change significantly. Expansion of energy commodity

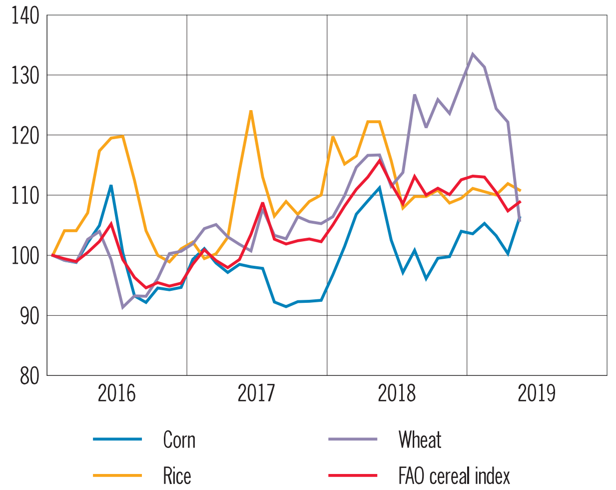
[2] *Here and below, changes are relative to the corresponding period of the previous year, unless otherwise indicated.*

WORLD FOOD PRICES
(2002–2004 =100%)
Chart 3.1.16



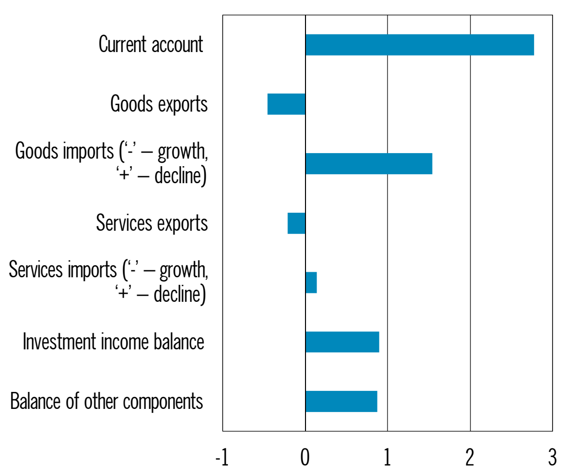
Source: UN Food and Agriculture Organization (FAO).

WORLD CEREALS PRICES
(JANUARY 2016 = 100%)
Chart 3.1.17



Sources: World Bank, Bloomberg, UN Food and Agriculture Organization (FAO).

GROWTH STRUCTURE OF CURRENT ACCOUNT BALANCE IN 2019 Q1*
(BILLIONS OF US DOLLARS ON CORRESPONDING QUARTER OF PREVIOUS YEAR)
Chart 3.1.18



** 2019 Q1 estimate.*
Source: Bank of Russia.

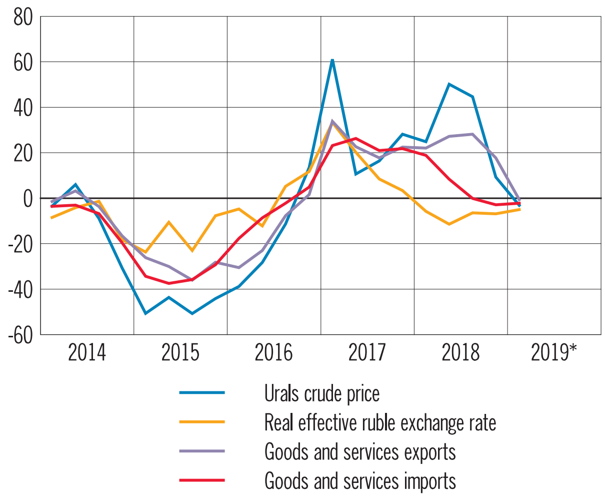
production supported exports. Oil production remained above the 2018 Q1 level, although it has decreased since last October due to the OPEC+ agreement. Russia's oil and petroleum product export quantities increased by 1.4%, mainly thanks to Korea, China and the Netherlands that diversified imports amid US sanctions against Iran. Both production and exports of coal were growing, mainly to Germany, which has closed its mines. Aluminium exports were also steadily growing: Russian companies have successfully re-oriented their supplies to Europe from the US, where additional duties were imposed in 2018. At the same time, global prices for many commodities remained below the 2018 Q1 level. In April – May, the total value of exports decreased: their quantities were negatively affected by problems with the Druzhba pipeline.

Imports. In 2019 Q1, imports of goods dropped by 3%. The effect of the ruble's weakening outweighed the support from demand. The real effective ruble exchange rate fell by 5% vs 2018 Q1. Imports of some goods, including machinery and industrial equipment, tractors, and computers, decreased by physical volume. For other goods (telephones), import prices fell. In April – May 2019, imports of goods and services did not significantly change as compared to the corresponding period of last year.

Non-trade components. Among non-trade components, the decreased deficit of the balance of investment returns due to lower costs for servicing of the reduced external debt contributed most to the increase in the current account in 2019 Q1. At the same time, the deficit of the balance of investment returns increased significantly amid material growth of dividends of Russian companies.

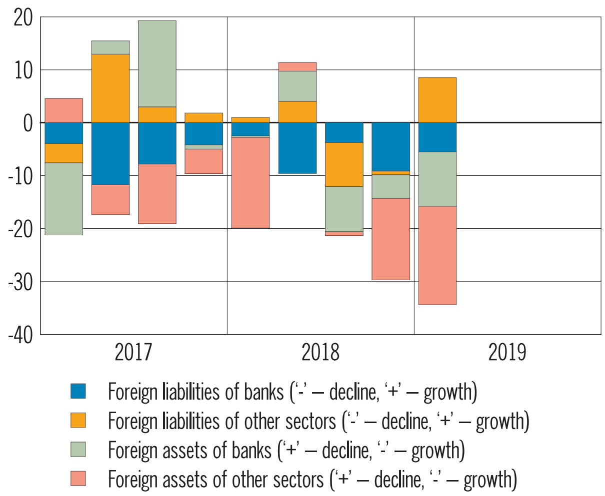
Financial account – private sector. The balance of private sector financial transactions in 2019 Q1 increased to $25 billion from $16 billion in 2018 Q1, mainly due to the growth of foreign assets. The banking sector accumulated a more significant volume of foreign currency amid remaining high inflows from foreign economic activity. The continuing decline in foreign obligations of banks amid limited access to the Western capital market also contributed to the expansion of the financial account balance. At the same time, companies

FOREIGN TRADE
(PER CENT CHANGE ON CORRESPONDING QUARTER OF PREVIOUS YEAR)
Chart 3.1.19



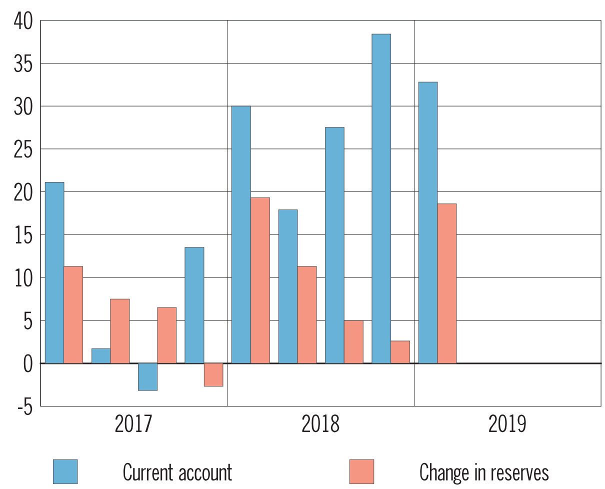
** 2019 Q1 import and export estimate.*
Sources: Bank of Russia, Thomson Reuters.

MAJOR PRIVATE SECTOR FINANCIAL ACCOUNT COMPONENTS
(BILLIONS OF US DOLLARS)
Chart 3.1.20



** 2019 Q1 estimate.*
Source: Bank of Russia.

RESERVE ASSETS AND CURRENT ACCOUNT
(BILLIONS OF US DOLLARS)
Chart 3.1.21



** Current account 2019 Q1 estimate.*
Source: Bank of Russia.

have increased their foreign obligations, mainly in the form of foreign direct investments.

Financial account – public sector. In 2019 Q1, there was a foreign capital inflow to the public sector amid new offerings of government bonds and secondary market purchases by non-residents.

Foreign currency reserves. An increase in reserves in 2019 Q1 by $19 billion resulted mainly from foreign currency purchases under the fiscal rule and the inflow of funds from sovereign Eurobond placements.

FOREIGN CURRENCY MARKET

Ruble exchange rate. The ruble exchange rate remained relatively stable in April – June, although EMEs' currencies decreased by 1.5% on average (pursuant to JP Morgan EM currency index). The high demand of foreign investors for Russian sovereign bonds, the continuing growth of the ruble's attractiveness for carry-trade transactions and the absence of news about potential tightening of sanctions supported the ruble. On average, the ruble was slightly stronger in Q2 than the Bank of Russia expected in March due to foreign investors' demand for OFZ and higher oil prices.

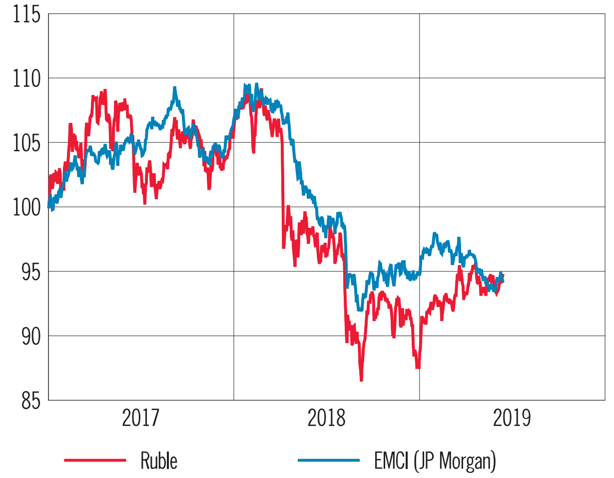
3.2. MONETARY CONDITIONS

MONEY MARKET

Overnight rates. Short-term interest rates in the IBL segment of the money market primarily formed slightly below the Bank of Russia's key rate. The average spread from the beginning of April until 17 June was -9 bp (in Q1, -18 bp) and fluctuated in the range of -43 to 31 bp (in Q4, from -55 to 6 bp) (for details about IBL rates formation and the liquidity position see Section 4.2).

FX liquidity. The interest rate spread in the IBL and FX swap segments remained positive on the back of continuing favourable FX liquidity situation in the banking sector. The average spread of short-term interest rates in the FX swap and IBL segments in April – June was 24 bp (in Q1, 9 bp). The situation with foreign currency liquidity was supported by a high foreign currency inflow in the current account of the balance of payments amid

DYNAMICS OF RUBLE AND EME CURRENCIES INDICES (100=02.01.2017, BP) — *Chart 3.1.22*

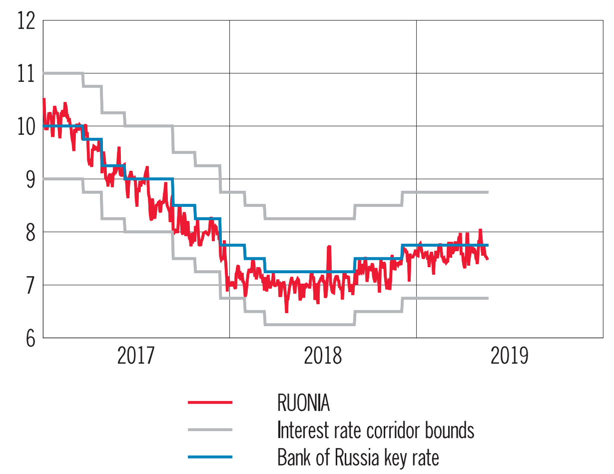


Source: Thomson Reuters.

CARRY-TO-RISK RATIO DYNAMICS — *Chart 3.1.23*

Sources: Thomson Reuters, Bank of Russia calculations.

RUONIA AND BANK OF RUSSIA INTEREST RATE CORRIDOR (% P.A.) — *Chart 3.2.1*



Source: Bank of Russia.

high oil prices, and an increase in non-residents' investments in OFZs. In the short run, the cost of FX borrowings in the Russian money market may increase to a certain extent due to a seasonal decrease of foreign currency inflow in the current account of the balance of payments and also due to the reverse conversion of dividend payments by non-residents into foreign currency. However, no significant change in the situation is expected, as banks accumulated a significant FX liquidity cushion in 2018 H2 – early 2019.

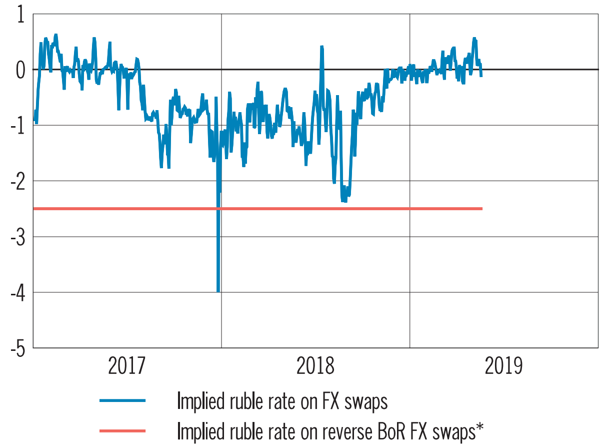
Money market yield curve. Money market rates for the period exceeding one day decreased slightly (the average 6M Mosprime was 8.38% in April – June vs 8.64% in Q1). The decrease in rates was primarily caused by the revision of the expected short-term interest rates' path by market participants. The comment made by the Bank of Russia in its April press release about a possible key rate cut as early as in Q2–Q3 and the comments made by the members of its Board of Directors in May shifted the expectations of market participants on the 6 to 12 months' horizon downwards by 26–38 bp. The contraction of major banks' demand for liquidity in this money market segment in favour of overnight FX swap borrowings amid increased foreign currency liquidity reserves (see the previous paragraph) also contributed to the decrease in interest rates.

STOCK MARKET

Similar to the FX market, the situation in the Russian stock market in April – June was better than in other EMEs. In April, the Russian market was mostly growing along with other EME markets on the back of overall increasing risk appetite. However, in late April – early May, that trend was exhausted due to a temporary failure of US/China trade negotiations, and EME indices started to fall. At the same time, most segments of the Russian market continued growing or remained at the level reached until the end of May, thanks to a number of positive local factors.

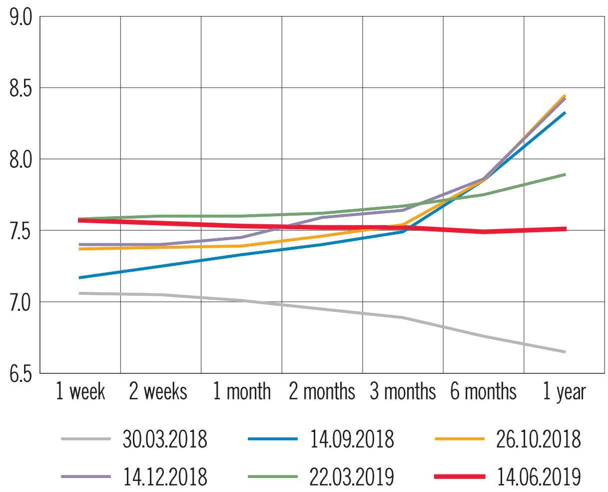
Government bond market. In the government bond segment, the situation was more positive. Due to an absence of limits at auctions, the Russian Ministry of Finance continued to place OFZs extensively, having overfulfilled the borrowing plan for Q1 and Q2. Despite the uncertainty with

SPREAD OF INTEREST RATE IN FX SWAP SEGMENT TO KEY RATE *Chart 3.2.2*
(PP)



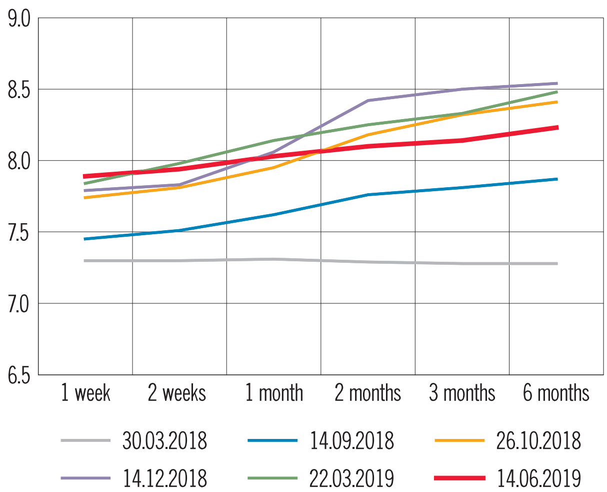
** Implied rate = ruble lending rate – FX borrowing rate + LIBOR (from 19.12.2016: key rate – 1 pp – (LIBOR + 1.5 pp) + LIBOR = key rate – 2.5 pp).*
Source: Bank of Russia calculations.

ROISFIX CURVE *Chart 3.2.3*
(% P.A.)



Source: SRO NFA.

MOSPRIME CURVE *Chart 3.2.4*
(% P.A.)



Source: SRO NFA.

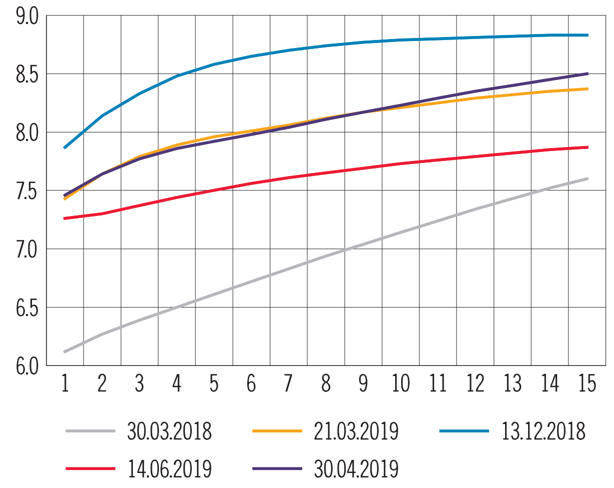
respect to tightening of sanctions on OFZs, foreign investors were making extensive purchases. In the primary market, they acquired 40% of all placed securities, which is more than SICIs (34%) and banks (14%). Moreover, foreign investors acquired securities in the secondary exchange and OTC markets. As a result, their investments in OFZs in absolute terms reached a historic high (₽2.5 trillion) and exceeded the level recorded before sanctions were imposed in April 2018. Despite the high interest of foreign investors in April, the short and mid sections of the OFZ yield curve remained at the same level while the long end even slightly rose, which could be partially caused by a significant offer of securities. In May, the yield curve started to decrease, although it was mainly caused by increased expectations of easing of the Bank of Russia's monetary policy. Despite that fact and although non-residents had already bought back the entire volume of OFZ sold in 2018, yields of government bonds were still exceeding the levels recorded in March 2018 (by 30–115 bp depending on maturity).

Higher yields in the short end of the curve resulted from expectations of a higher key rate (vs expectations in March 2018), and in the long end, from a risk premium due to the threat of sanctions tightening.

Corporate bond market. The yield reduction in the corporate bond market that started early in the year continued in April and May. It was generally commensurate with the decrease in OFZ yields, and as a result the spread between them stabilised at 60 bp. Amid the yield reduction, a moderate recovery of issuance activity was observed. In April – May, securities for $523 billion were placed, which is comparable to the corresponding period of 2017, when securities for $566 billion were placed (the comparison with 2018 would be incorrect, as the placement volume was significantly lower due to sanctions). Despite the increased issuance activity, the growth rate of the corporate bond portfolio remains near multi-year lows and lags significantly behind the growth rates of the OFZ portfolio.

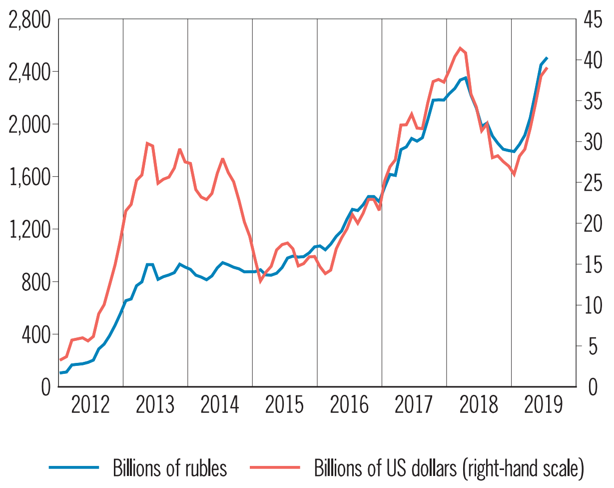
Equity market. Russian stock indices were growing in April along with the indices of other EMEs, but started adjusting downwards in May amid a global decrease in risk appetite.

OFZ ZERO COUPON YIELD CURVE
(% P.A.)
Chart 3.2.5



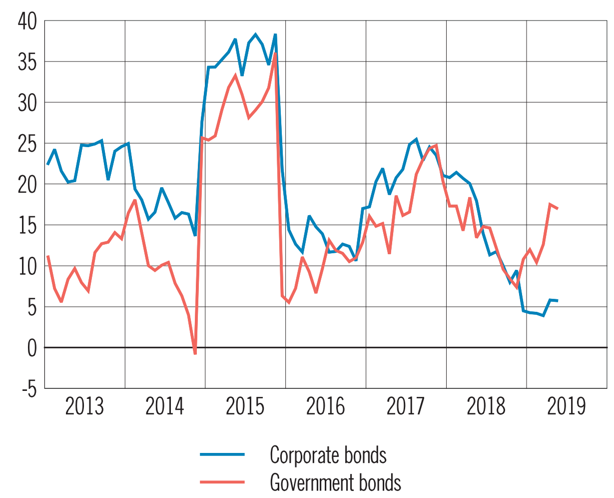
Source: Moscow Exchange.

NOMINAL VALUE OF OFZ HELD BY NON-RESIDENTS
(ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 3.2.6



Source: National Settlement Depository.

CORPORATE AND GOVERNMENT SECURITIES PORTFOLIO
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)
Chart 3.2.7



Source: Cbonds.ru.

However, the correction was not deep due to the beginning of the dividend period, when a number of companies announced significantly increased dividend payments. According to the Bank of Russia's estimates as of 30 May 2019, Russian companies will pay $1.9 trillion in May – August 2019, which is 43% higher than last year. This news caused the MOEX index to renew its historical high in June while the RTS and MSCI Russia indices returned to the July 2014 level.

DEPOSIT AND LOAN MARKET

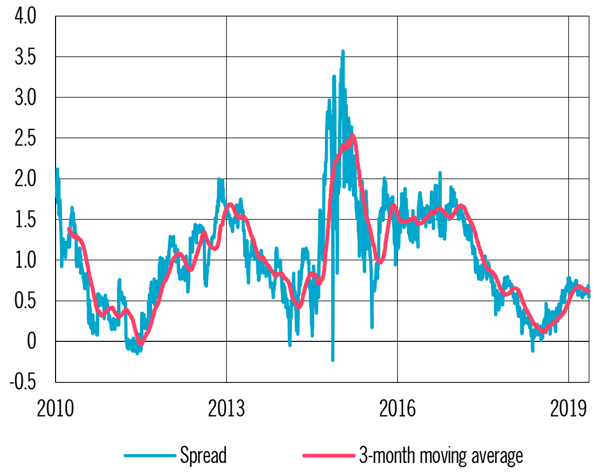
Deposit rates. By the beginning of 2019 Q2, the growth of deposit rates observed since September 2018 had ceased (Chart 3.2.11). In April 2019, the interest rates for short-term ruble deposits increased, as compared to February, by 0.4 pp, and for long-term ruble deposits, by 0.1 pp. A gradual decrease in average market deposit rates can be expected by the end of the year as inflation gradually returns to the target level and long-term money market rates and bond yields are adjusted accordingly.

Deposit operations. In March – April, the inflow of household funds to deposits increased. As of the beginning of May, the annual growth of household deposits[3] amounted to 6.8% vs 5.7% as of the beginning of March. The inflow of funds in FX deposits in March – April slowed down vs previous months but remained stable. As a result, FX deposits started to make a positive contribution to the annual growth of household deposits for the first time since mid-2017. By the beginning of May, FX deposits accounted for almost 20% of the annual growth of household deposits.

In the ruble segment, depositors continued to express an interest in long-term deposits (Chart 3.2.12), the annual growth of which as of early May exceeded 11% (for short-term ruble deposits, the corresponding indicator was less than 5%). In the short run, it can be expected that the current rate of inflow of household funds to deposits will remain, with ruble deposits dominating growth in the deposit portfolio of banks.

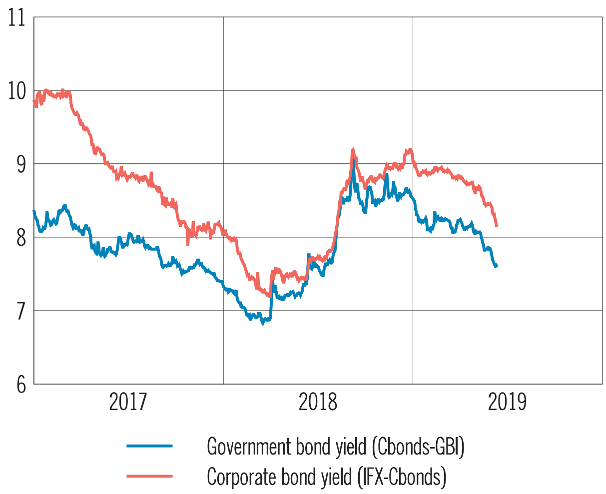
[3] *Here and below, the growth of bank foreign currency balance sheet indicators are shown in the dollar equivalent; balance sheet indicators that include foreign currency and ruble components are shown net of foreign currency revaluation.*

SPREAD BETWEEN YIELDS OF CORPORATE AND GOVERNMENT BONDS *Chart 3.2.8*
(PP)



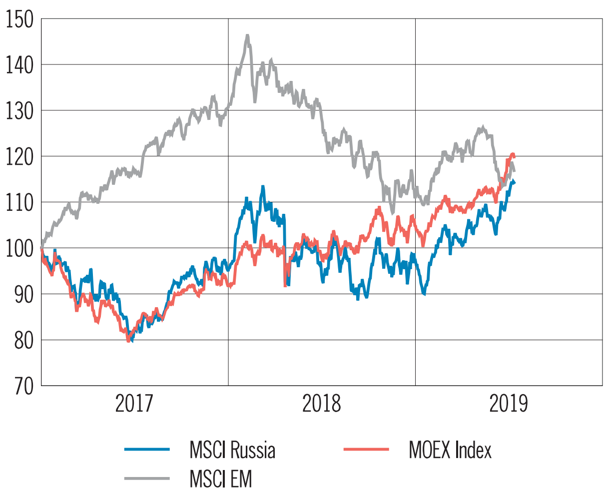
Source: Cbonds.ru.

CORPORATE AND GOVERNMENT BOND RETURN INDICES *Chart 3.2.9*
(% P.A.)



Source: Cbonds.ru.

STOCK INDICES *Chart 3.2.10*
(100 = 03.01.2017)



Source: Bloomberg.

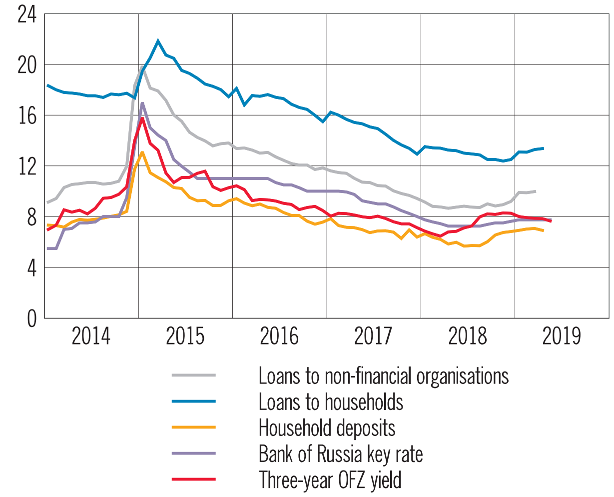
Credit rates. In March – April, the lending market also followed the trend towards the growth of credit rates that had formed in 2018 H2 (Chart 3.2.11). In the recent months, the largest growth of interest rates was recorded in the mortgage lending segment, where the March interest rate exceeded the local minimum of September 2018 by 1 pp. The interest rate for 1-year+ auto loans increased by less than 0.3 points during the same period while the rate on long-term corporate loans increased by 0.7 points. One of the factors behind the faster-than-expected growth of credit rates could be the extension of the average maturity of loans to 17.8 years in March 2019 (vs 16.3 years six months earlier).

By March, the growth of interest rates in most market segments slowed down. In April – May, a number of major banks reduced their mortgage rates, and the average auto loan rate decreased slightly. For that reason, fluctuations of interest rates around the current level can be expected in the next few months, with a transition to downward dynamics toward the year-end.

Corporate lending. In the first months of 2019, the growth of corporate lending remained low. As of early May, annual growth rates of loans to non-financial organisations remained almost the same as in early March and amounted to 5.4%. Russian corporate borrowers continued replacing foreign currency loans with ruble loans (Chart 3.2.13): the annual growth of ruble loans to non-financial organisations was 11.4% while foreign currency loans dropped 9.1%. In the short run, we expect a gradual growth of corporate lending with a continued dedollarisation in this market segment.

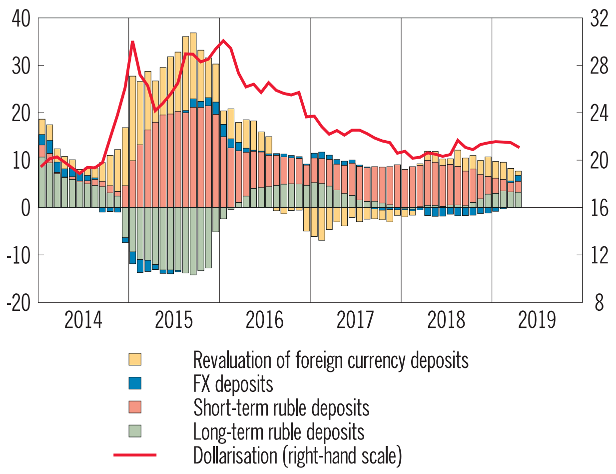
Retail lending. In the retail loan market, lending growth continued to accelerate in early 2019, although not as fast as in the previous year. As of the beginning of May, the annual growth of household loans amounted to 23.8% vs 23.4% two months earlier. The faster-than-expected increase in consumer lending growth rates led to the fact that the growth of consumer loan portfolio exceeded the mortgage loan portfolio growth by early May. The share of consumer loans in the retail loan portfolio also started to increase (Chart 3.2.14). Considering the gradual saturation of the retail loan market and measures taken by the Bank of Russia to contain the excessive

INTEREST RATES ON LONG-TERM RUBLE OPERATIONS IN RUSSIAN MARKET
(% P.A.)
Chart 3.2.11



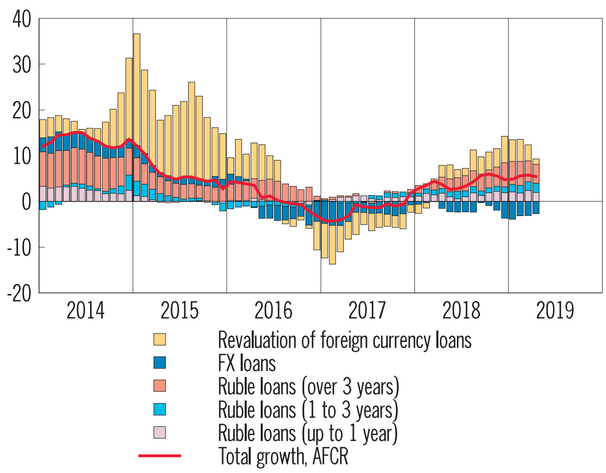
Source: Bank of Russia.

CONTRIBUTION OF VARIOUS COMPONENTS TO ANNUAL GROWTH OF HOUSEHOLD DEPOSITS
(PP)
Chart 3.2.12



Source: Bank of Russia.

CONTRIBUTION OF VARIOUS COMPONENTS TO ANNUAL GROWTH OF CORPORATE LOAN PORTFOLIO
(PP)
Chart 3.2.13



Source: Bank of Russia.

growth of some of its segments, in the short run we may expect that current household lending growth rates will remain at this level, with their subsequent slowdown by the year-end.

3.3. ECONOMIC ACTIVITY

GROSS DOMESTIC PRODUCT

According to Rosstat's preliminary estimates, the annual GDP growth rate slowed down in 2019 Q1 to 0.5% from 2.7% in the previous quarter and ended up below the Bank of Russia's forecast range of 1.0–1.5% (Chart 3.3.1).

The weakening of consumer and investment activity was caused by the VAT rate hike, effective from 1 January 2019, and related temporary acceleration in price growth rates. The tightening of monetary conditions in 2018 H2 caused by external factors also affected the domestic demand.

Economic activity was also contained by weak external demand for Russian products and services amid global economy's slowdown and restrictions imposed on oil production by the OPEC agreements.

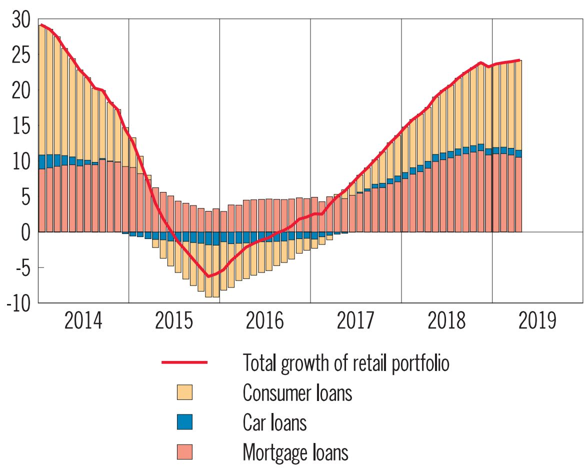
Furthermore, it is estimated that the adjustment of inventories could also significantly impact GDP growth in the first quarter of 2019. According to estimates, the level of inventories returned to the values of 2018 Q2–Q3 after an increase in Q4 (Chart 3.3.2). The accelerated year-end increase in inventories could be related to the forthcoming VAT hike. Notably, due to the specifics of statistical accounting, the official estimate of inventories can, potentially, be significantly reviewed.

The base effect also contributed to GDP growth slowdown: in the first quarter of 2018, annual GDP growth accelerated to 1.9% from 0.3% in the previous quarter.

According to estimates, the slowdown of GDP growth in 2019 Q1 was temporary to a great extent. The dynamics of economic activity indicators in April 2019 suggest that annual growth rate of the aggregate output of products and services may increase in the second quarter to reach 0.5–1.0%.

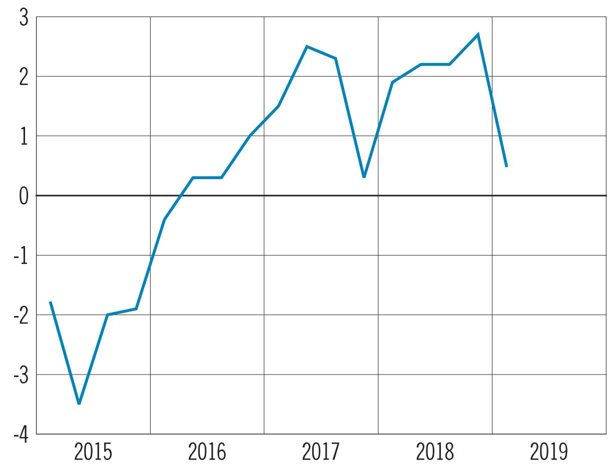
In Q3, as national projects are implemented and public investments are expanded, the GDP growth rate will accelerate to 0.8–1.3%.

CONTRIBUTION OF VARIOUS COMPONENTS TO ANNUAL GROWTH OF RETAIL LOAN PORTFOLIO
(PP)
Chart 3.2.14



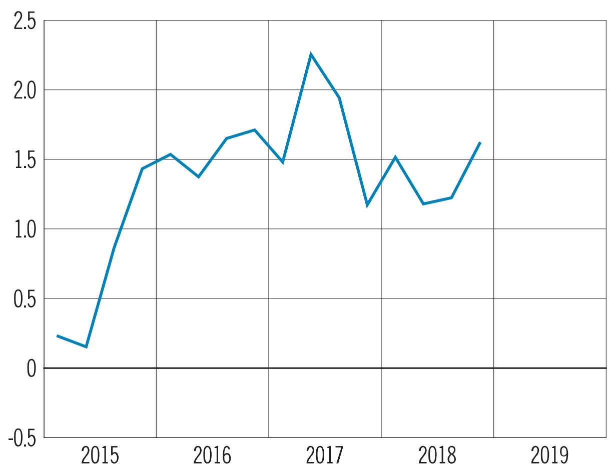
Source: Bank of Russia.

GDP GROWTH RATE
(PER CENT CHANGE ON CORRESPONDING QUARTER OF PREVIOUS YEAR)
Chart 3.3.1



Source: Rosstat.

CHANGE IN INVENTORIES
(AS % OF GDP IN 2016 PRICES, SA)
Chart 3.3.2



Sources: Rosstat, Bank of Russia calculations.

PRODUCTION ACTIVITY

In March – April 2019, industrial production continued to grow (Chart 3.3.3). The average annual growth of industrial output during that period was 2.9%, which is close to values of late 2018 – early 2019. As compared to February, the industrial production (SA) increased with output growing across a wide range of product groups.

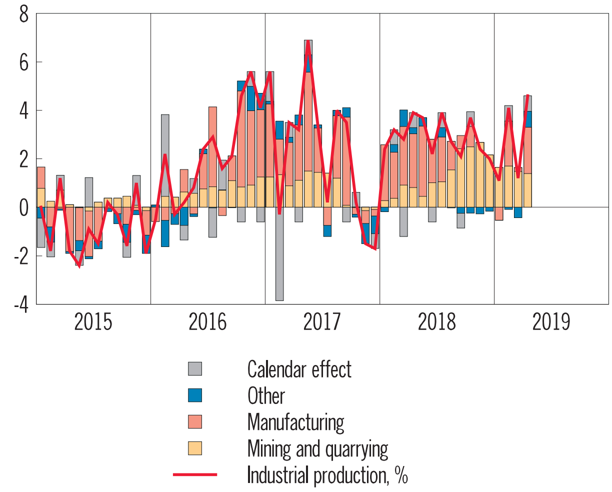
Raw material production. Mining and quarrying output increased in March – April 2019. However, this sector's growth rates, both annual and monthly (SA), slowed down. Production growth was contained by weak external demand for Russian gas due to warm weather in Europe and restrictions imposed on oil production under the OPEC+ agreement. On the contrary, the output of marble and other limestones increased, which could be associated with renovation works conducted in the country's major cities.

Intermediate goods production. In March – April 2019, the production of intermediary goods decreased vs February (SA). A decrease in metallurgical production caused by the dynamics of external demand for Russian metals made the largest contribution. The external demand for other Russian intermediary goods was, on the contrary, expanding, which led to an increase in output of rubber and plastic goods and products produced by the wood processing and chemical industries.

Investment goods production. Production of investment goods in March – April 2019 increased as compared to February (SA, Chart 3.3.4). Production of construction materials continued to grow, which may reflect expectations of a recovery in the construction industry. Nevertheless, construction work volumes in March – April remained at the level of previous months (SA, see Investment Activity subsection).

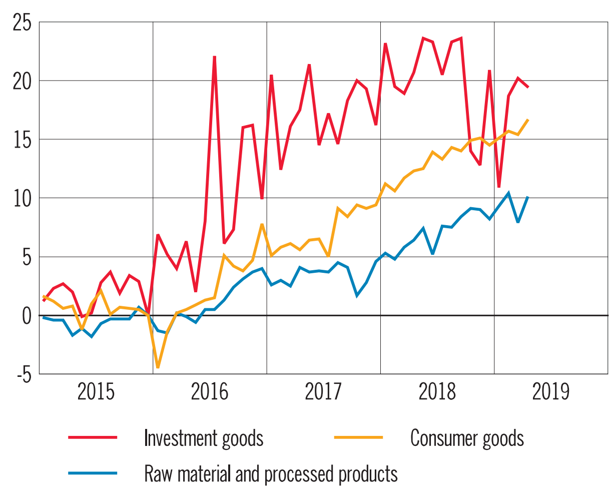
Output of engineering products remained volatile. After a significant growth in March 2019, it decreased again in April. Having said that, medium-term trends point to a stagnant or shrinking output in key product groups. For example, the growth of production of electrical equipment and other vehicles recorded in 2017 – early 2018 gave way to a decrease in output volumes in mid-2018 due to lower government orders for those products.

INDUSTRIAL PRODUCTION
(CONTRIBUTION TO ANNUAL GROWTH, PP)
Chart 3.3.3



Sources: Rosstat, Bank of Russia calculations.

INDUSTRIAL PRODUCTION BY PRODUCT GROUP
(PER CENT CHANGE ON DECEMBER 2015, SA)
Chart 3.3.4



Sources: Rosstat, Bank of Russia calculations.

Consumer goods production. Production of consumer goods increased in March – April 2019 (vs February, SA) mainly due to the growth of food production, including meat and dairy products. This took place due to imports substitution on the back of existing restrictions and accelerating growth of global prices related, among other things, to unfavourable epizootic developments in certain countries. Output of particular consumer durable goods, including passenger cars, continued to grow. This may indicate that producers expect recovery in consumer demand in the months to come.

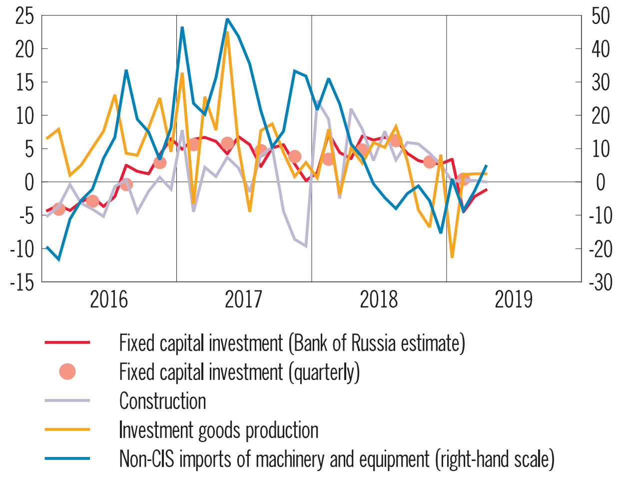
INVESTMENT ACTIVITY

Fixed capital investments in Q1. In the first quarter of 2019, annual growth rate of fixed capital investment slowed down to 0.5% from 2.9% in the previous quarter (Chart 3.3.5). Fixed capital investments (SA) remained near the seasonally adjusted 2018 Q4 level. As in the end of the previous year, investment activity was restrained by a temporary slowdown of government investments and the tightening of monetary conditions. Against this background, the growth rate of private sector fixed capital investments (exclusive of infrastructural investments) slowed down to 0.6% from 2.4% a quarter earlier. However, it was public sector investments, which dropped by 19.4% YoY (vs -3.5% in 2018 Q4, Chart 3.3.6), that had the most negative effect on the annual growth of fixed capital investments.

Investment activity in April. In April 2019, the annual growth of engineering imports amounted to 4.7%, a maximum value since June 2018. That was encouraged by the strengthening of the ruble observed since the beginning of the year (Chart 3.3.5). However, the volume of construction works remained at the prior month's level (seasonally adjusted) amid mixed dynamics of output of various groups of investment goods (see Production Activity subsection). For that reason, it will be premature to speak about the growth of investment activity.

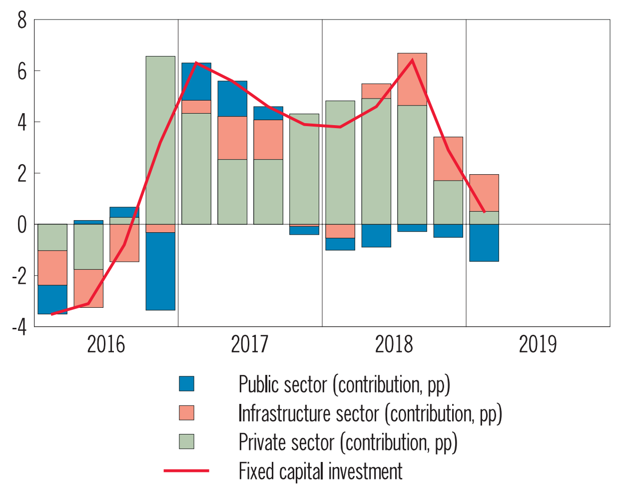
Pursuant to the Bank of Russia's estimates, gross fixed capital formation in 2019 Q2 will grow by 0.5 – 1.0% YoY. According to estimates, the change in inventories will remain near the Q1 level. In this context, the growth of gross fixed

INVESTMENT ACTIVITY INDICATORS *Chart 3.3.5*
(PER CENT CHANGE ON CORRESPONDING PERIOD OF PREVIOUS YEAR)



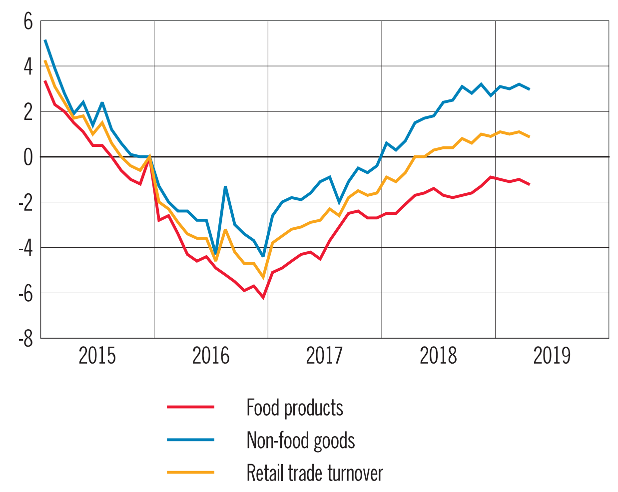
Sources: Rosstat, FCS, Bank of Russia calculations.

FIXED CAPITAL INVESTMENT *Chart 3.3.6*
(PER CENT CHANGE ON CORRESPONDING QUARTER OF PREVIOUS YEAR)



Sources: Rosstat, Bank of Russia calculations.

RETAIL TRADE TURNOVER *Chart 3.3.7*
(PER CENT CHANGE ON DECEMBER 2015, SA)



Sources: Rosstat, AEB, Bank of Russia calculations.

capital formation in 2019 Q2 will remain negative. In Q3, as national projects are implemented, the annual growth of gross fixed capital formation will accelerate to 2.8 – 3.3%.

CONSUMPTION

Retail trade turnover. In March – April 2019, consumer demand remained contained. Retail trade turnover (SA) was close to late 2018 – early 2019 levels (Chart 3.3.7). Its annual growth rate dropped to 1.2% in April 2019 (Chart 3.3.8), which is the lowest figure since September 2017, coming in below Bank of Russia's expectations.[4] Both food and non-food products sales growth slowed down.

Demand expansion was prevented by falling real disposable household income (see Labour Market and Incomes subsection). At the same time, according to the estimates, its negative impact on demand was not offset by growing consumer lending (see Section 3.2). Consumer demand stagnation also reflects the impact of temporary acceleration in price growth after the VAT hike. As the influence of this factor has largely faded away, it is expected that retail trade turnover will start growing in the second quarter of 2019 QoQ (SA). Pursuant to the Bank of Russia's estimates, retail trade turnover will grow in 2019 Q2 by 1.5 – 2% YoY.

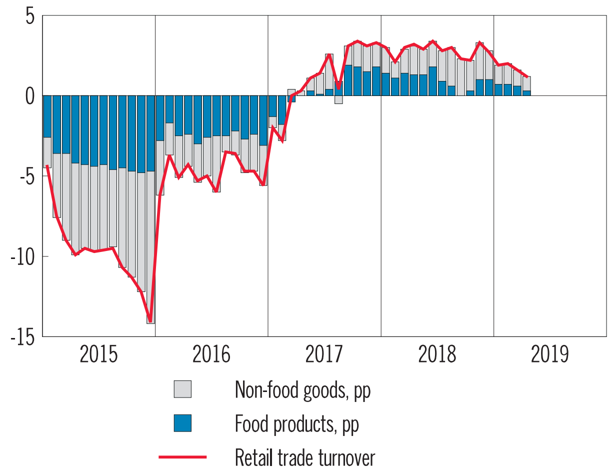
LABOUR MARKET AND INCOMES

Unemployment rate. In March – April 2019, unemployment fell to the all-time low level of 4.6% (SA, Chart 3.3.9). Unemployment was declining mainly under the effect of structural factors, primarily, further decrease in labour resources. The additional expansion of labour resources at the expense of individuals who were affected by the pension reform was insufficient to compensate for that.

Wages. The annual growth of real wages in March 2019 was 2.3% (about zero in February, Chart 3.3.10). Wages rose most noticeably in finances and insurance as well as in related sectors where one-off payments most likely took place due to a significant improvement of companies' financial results for the previous year. However,

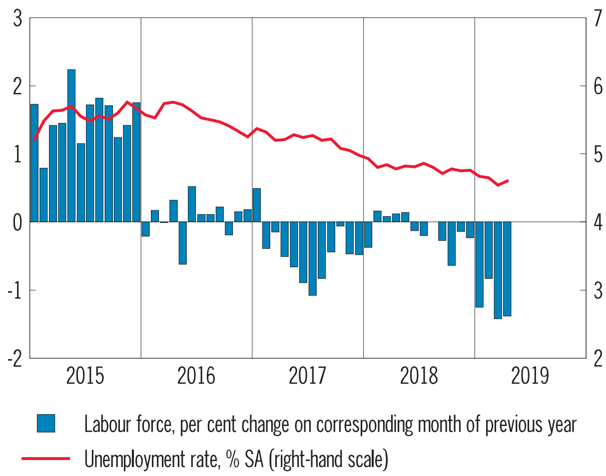
[4] *On 20 June 2019, Rosstat revised the annual growth rate of retail trade turnover in April 2019 to 1.6%.*

RETAIL TRADE TURNOVER
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)
Chart 3.3.8



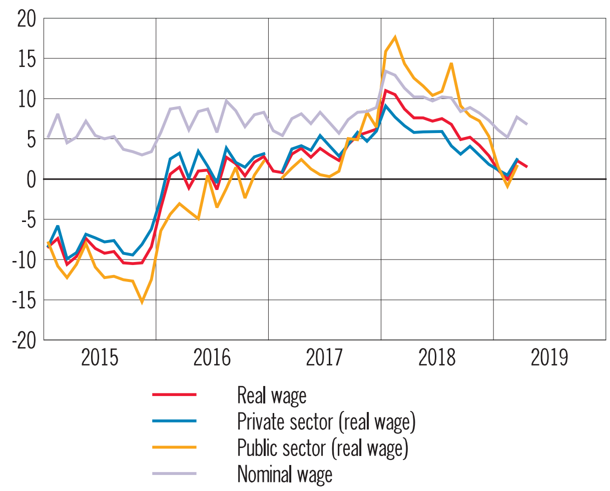
Sources: Rosstat, Bank of Russia calculations.

UNEMPLOYMENT AND LABOUR FORCE
Chart 3.3.9



Sources: Rosstat, Bank of Russia calculations.

WAGES
(PER CENT CHANGE ON CORRESPONDING MONTH OF PREVIOUS YEAR)
Chart 3.3.10



Sources: Rosstat, Bank of Russia calculations.

in other sectors, labour compensation dynamics remained contained and in line with the Bank of Russia's expectations. Preliminary estimates suggest that in April 2019 annual real wage growth stood at 1.6%.[5] Given the current dynamics and the expected acceleration of the GDP growth rates in Q2–Q3, the indicator's growth is expected to be near 2% YoY.

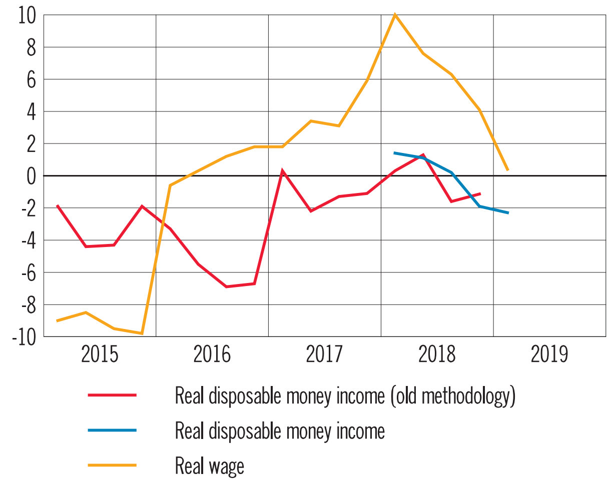
Household incomes. In March 2019, Rosstat announced a transition to a new methodology for calculating money income and household spending. Newly released data for 2018 – 2019 are largely in line with wage movements (Chart 3.3.11). The extensive growth of labour remuneration during 2018 provided the main positive contribution to the formation of incomes (Chart 3.3.12). The difference between income and wages since 2018 Q2 resulted from the shrinkage of other earnings, including primarily undisclosed ones. In 2019 Q1, other monetary earnings continued to decline. Together with the slowing wage growth and accelerating inflation, this led to a 2.3% contraction of real household disposable money income.

FINANCIAL STANDING OF ENTERPRISES

Financial result. According to Rosstat's latest updates, the balanced financial result of large and medium enterprises in 2019 Q1 reached a new 12-year high, amounting to ₽3.8 trillion, after ₽3.6 trillion in the previous quarter and ₽2.5 trillion in 2018 Q1 (Chart 3.3.13). The profit and loss balance in manufacturing industries increased significantly amid favourable dynamics of industrial production, and in trade (Chart 3.3.14). By contrast, the financial result in mining and quarrying decreased slightly vs the previous quarter, which was mainly caused by a decrease in oil production by OPEC countries during that period (see Section 3.1). In general for the economy, the profit of enterprises was 3.8% higher than in the previous quarter. According to the operational data of Rosstat, the total losses of businesses dropped by 6% vs the previous quarter. The scope of the segment of loss-making companies did not significantly change.

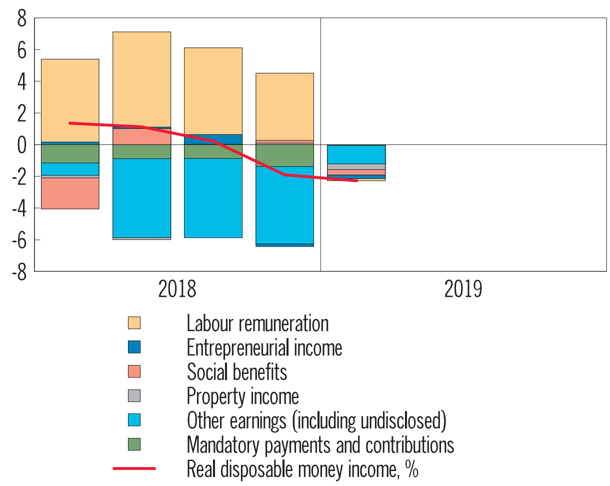
[5] *On 20 June 2019, Rosstat revised the annual growth rate of real wages in April 2019 to 3.1%.*

DISPOSABLE MONEY INCOME AND REAL WAGE *Chart 3.3.11*
(PER CENT CHANGE ON CORRESPONDING QUARTER OF PREVIOUS YEAR)



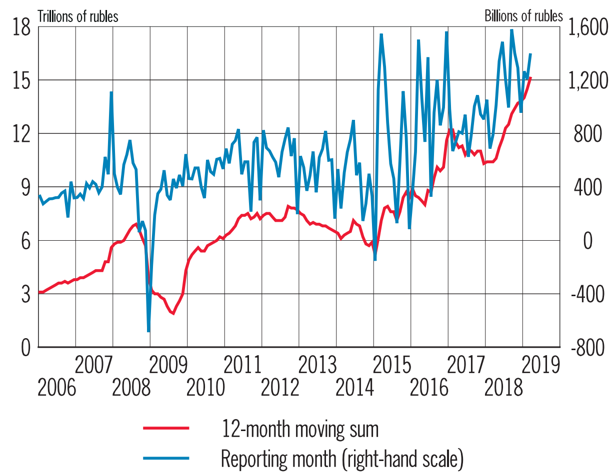
Sources: Rosstat, Bank of Russia calculations.

HOUSEHOLD REAL DISPOSABLE MONEY INCOME *Chart 3.3.12*
(CONTRIBUTION TO ANNUAL GROWTH, PP)



Sources: Rosstat, Bank of Russia calculations.

BALANCED FINANCIAL RESULT *Chart 3.3.13*



Sources: Rosstat, Bank of Russia calculations.

According to the Bank of Russia's estimates, the increase in the average sales profit margin from 9.4% in January – March 2018 to 11% in January – March 2019 made the greatest contribution to the growth of the financial result YoY.

Debt. According to the Bank of Russia's estimates, the volume of claims of the banking sector against legal entities, including financial institutions, in rubles and foreign currency grew in 2019 Q1 by 1.4% (after 3.2% growth in the previous quarter). The growth rates slowed down due to the dynamics of claims in foreign currency. Due to the ruble's strengthening in January – March, foreign debt of enterprises decreased by 2.4%, and their foreign currency-denominated internal debt dropped by 6.4% (Chart 3.3.15, 3.3.16). Claims in rubles during that period grew by 3.2%. The debt burden[6] remained practically unchanged amid comparable quarterly growth rates of claims and incomes (nominal GDP).

3.4. PUBLIC FINANCES

Based on the results of January – April 2019, the budget surplus of the general government[7] continued to grow (Table 3.4.1). Its formation was stipulated by the faster-than-expected growth of income by 16.3% as compared to a 6.7% increase in expenses YoY. Both oil and gas income (by 9.3%) and non-oil and gas income (by 18.3%) continued to grow due to the VAT base rate hike and high profits of enterprises in 2018. In April 2019, the 12-month rolling non-oil and gas deficit decreased to 4.8% of GDP (vs 5.8% in 2018).

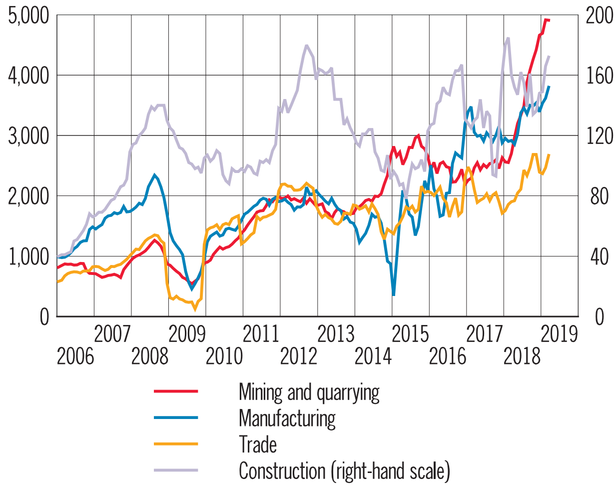
Macroeconomic effects of the fiscal policy. In early 2019, the fiscal policy made a restraining contribution to the aggregate demand. Investment expenditures[8] of the general government in January – April 2019 grew in nominal terms by only

[6] *Debt service ratio is calculated based on the methodology described in Donets S.A., Ponomarenko A.A., Measuring Debt Burden. Money and Credit. No. 4, 2017. Value for 2019 Q1 is the Bank of Russia's estimate.*

[7] *Here and below, the concept of general government includes the consolidated budget of the federal centre, the constituent entities of the Russian Federation, and state extra-budgetary funds.*

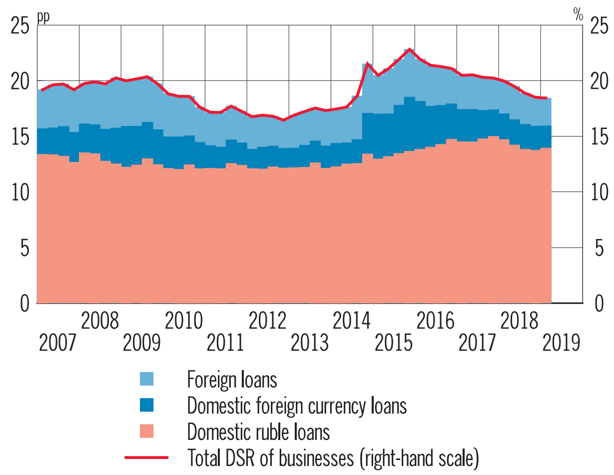
[8] *Capital investments in government (municipal) property. Data source: the Federal Treasury report on the 'Consolidated budget of the Russian Federation and the budgets of state extra-budgetary funds of the Russian Federation', dated 1 May 2019 (as per the classification of types of expenditures).*

BALANCED FINANCIAL RESULT BY ACTIVITY TYPE
(12-MONTH MOVING SUM, BILLIONS OF RUBLES)
Chart 3.3.14



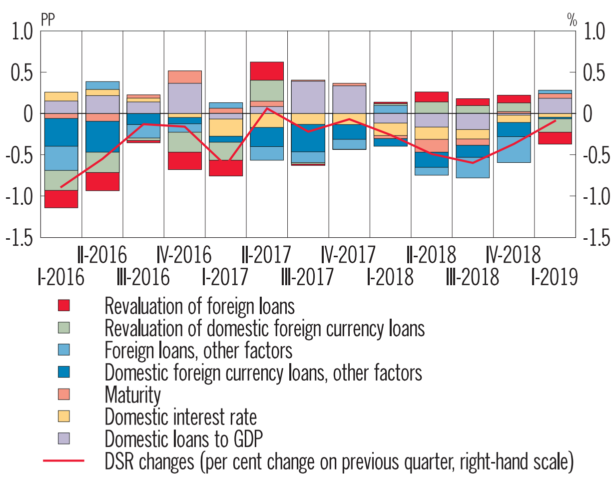
Sources: Rosstat, Bank of Russia calculations.

CORPORATE DEBT BURDEN
(DEBT SERVICE RATIO AND ITS COMPONENTS, AS % OF GDP)
Chart 3.3.15



Source: Bank of Russia calculations.

DECOMPOSITION OF CHANGES IN CORPORATE DEBT BURDEN
(DEBT SERVICE RATIO AND CONTRIBUTION OF FACTORS TO ITS CHANGES, AS % OF GDP)
Chart 3.3.16



Source: Bank of Russia calculations.

3.1% as compared to the corresponding period of the previous year. In 2019 Q3–Q4, according to the Bank of Russia's estimates, the fiscal impulse will be gradually entering the positive area. Thus, by the end of 2019, the fiscal policy will start encouraging aggregate demand, partly owing to the accomplishment of national targets and the implementation of priority projects.

General government budget. According to the data provided by the Federal Treasury,[9] the 12-month rolling surplus of the general government budget increased in January – April 2019 (3.9% of GDP vs 2.9% of GDP as of 2018 year-end). The growth was caused by the slow realisation of expenses as compared to the plan of the Russian Ministry of Finance and increased non-oil and gas revenues. In particular, there was an increase in inflows from profit tax (by 47.5%) and personal income tax (by 10.1%) YoY. Despite a slight nominal growth, the 12-month rolling budgetary system spending decreased against the GDP (Table 3.4.1).

Federal budget. The data on the fulfilment of the federal budget in January – May 2019[10] confirm the preservation of the main trends of last year. Since the beginning of the year, the 12-month rolling surplus of the federal budget gradually increased and amounted to 3.1% of GDP as of the end of May 2019 (Table 3.4.1, Chart 3.4.2). The surplus was growing due to the slow realisation of expenses as compared to the plan of the Russian Ministry of Finance (5.2% growth) and due to income growth (by 13.8% YoY). Incomes were growing mainly from the non-oil and gas component (16.3% growth): inflows from VAT on goods imported and sold in the Russian Federation in January – May 2019 increased by 19.6 and 13.1% as compared to the corresponding period of last year. Oil and gas revenues also increased YoY (by 10.7%) but remained practically unchanged against the GDP.

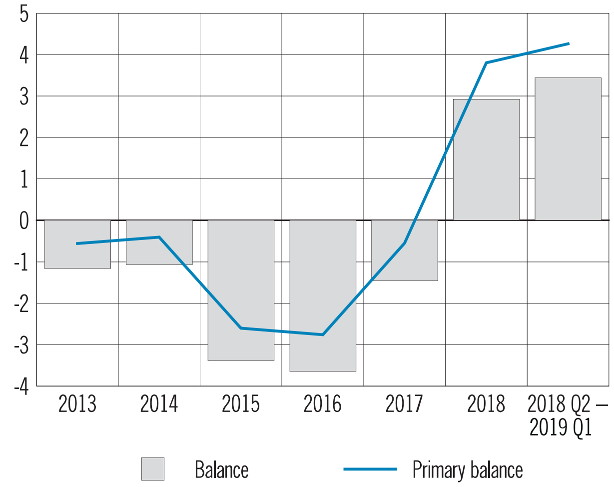
Balances of funds in budget accounts with the banking system. On the back of high tax returns and moderate budgetary expenses,

[9] Data source: the Federal Treasury monthly report on the 'Consolidated budget of the Russian Federation and the budgets of state extra-budgetary funds of the Russian Federation', as of 1 May 2019.

[10] Data source: progress report of the Federal Treasury 'On the fulfilment of the federal budget' as of 1 June 2019.

BUDGET SYSTEM BALANCE
(AS % OF GDP)

Chart 3.4.1



Sources: Federal Treasury, Bank of Russia calculations.

BUDGET SYSTEM PARAMETERS
(12-MONTH MOVING SUM, AS % OF GDP)

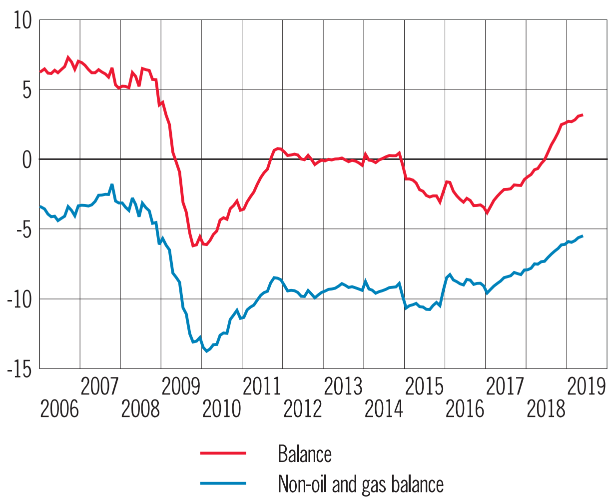
Table 3.4.1

	2017	2018	April 2019	May 2019
General government budget				
Revenue	33.7	35.9	36.8	–
Spending	35.2	33.0	32.9	–
Balance	-1.5	2.9	3.9	–
Federal budget				
Revenue	16.4	18.7	19.1	19.1
Oil and gas revenue	6.5	8.7	8.7	8.7
Additional oil and gas revenue (excess revenue)	0.9	4.1	4.0	4.0
Non-oil and gas revenue	9.9	10.0	10.4	10.4
Spending	17.8	16.1	16.0	16.0
Balance	-1.4	2.6	3.1	3.1

Sources: Federal Treasury, Bank of Russia calculations.

FEDERAL BUDGET BALANCE
(12-MONTH MOVING SUM, AS % OF GDP)

Chart 3.4.2



Sources: Federal Treasury, Bank of Russia calculations.

balances in budget accounts with the Bank of Russia and credit institutions continued to grow (Chart 3.4.3). At the same time, the demand of banks for funds placed by the Federal Treasury did not significantly increase, which resulted in the growth of balances in accounts of the federal budget with the Bank of Russia.

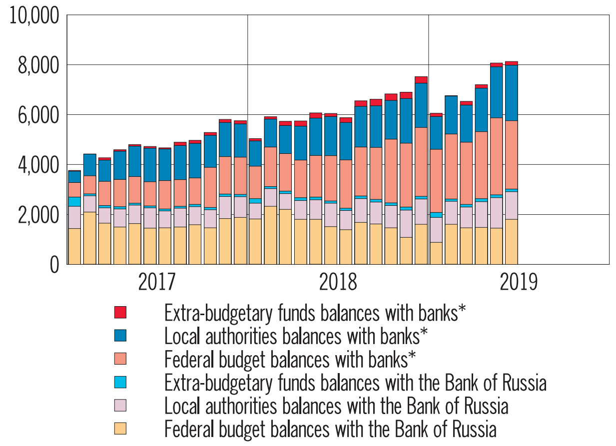
National Wealth Fund. The volume of the National Wealth Fund as of 1 June 2019 totalled $58.7 billion (3.6% of GDP). The volume of excess oil and gas revenues received in 2018 and awaiting transfer to the NWF in the current year amounted to roughly $66.6 billion. Taking into account the crediting of additional oil and gas revenues received in the previous year, the Bank of Russia estimates that in the baseline scenario, the liquid part of the NWF will not exceed 7% of GDP at the end of 2019. This level is expected to be exceeded in 2020, after the transfer of excess oil and gas revenues of 2019.

Public debt. According to the Ministry of Finance of Russia, the volume of the aggregate public and municipal debt of the Russian Federation totalled 14.6% of GDP as of 1 May 2019, which is 0.7 pp lower than the last year level (Chart 3.4.5).

The growth of the aggregate public and municipal debt in nominal terms occurred due to the domestic federal debt, which since the beginning of 2019 increased by 0.7% of GDP (according to the data of the Russian Ministry of Finance as of 1 May 2019). A favourable market environment and a new format of OFZ placement auctions (without a pre-announced placement volume) enabled the placement of federal government bonds at an accelerated pace. In January – May, the Russian Ministry of Finance placed over a half (53%) of the OFZ placement volume scheduled for 2019 and exceeded the placement volume scheduled for the first half of the year by 23%.

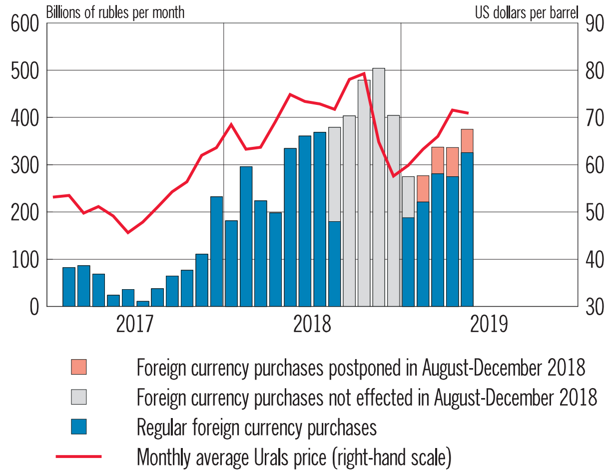
In 2019 Q1, the largest one-off placement of Russian Eurobonds for the last five years took place, which exceeded the limit stipulated by the budget for 2019 by 29%. However, taking into account a favourable market environment, the Russian Ministry of Finance again borrowed funds in the international capital market in June 2019, which is likely to lead to a respective decrease in borrowing in the domestic market.

BUDGET SYSTEM BALANCES OF FUNDS IN RUBLE ACCOUNTS WITH BANKS AND THE BANK OF RUSSIA
(BILLIONS OF RUBLES)
Chart 3.4.3



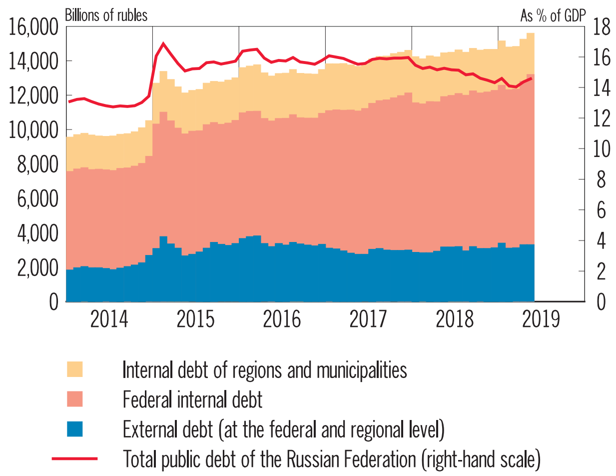
** According to data from banking reporting form 0409301 'Indicators characterising the performance of a credit institution'.*
Source: Bank of Russia calculations.

OPEN MARKET OPERATIONS TO REPLENISH THE NATIONAL WEALTH FUND
Chart 3.4.4



Sources: Russian Ministry of Finance, Bank of Russia.

PUBLIC DEBT OF THE RUSSIAN FEDERATION
Chart 3.4.5



Source: Russian Ministry of Finance.

4. BANK OF RUSSIA'S MONETARY POLICY

4.1. KEY RATE DECISIONS

Key rate decisions. On 26 April, the Bank of Russia Board of Directors decided to keep the key rate unchanged at 7.75% per annum, and on 14 June, to reduce it by 25 bp to 7.50% p.a. The Bank of Russia made these decisions taking into account inflation and economic dynamics against the forecast, as well as the risks posed by external conditions and the response of financial markets.

After the meeting of the Board of Directors on 22 March, it was necessary to evaluate the resulting effect of the VAT increase on inflation, including secondary effects. Further change in the external environment and the dynamics of inflation expectations also remained uncertainty factors.

As actual data were obtained in April – the first half of June, the Bank of Russia was clarifying its vision of the expected inflation dynamics, economic developments, and the assessment of inflation risks. In March 2019, annual inflation passed a local peak, somewhat below expectations, and started decreasing. In May – June, a trend toward a slowdown in inflation stabilised. The existing price dynamics made it possible to evaluate the remaining risks of secondary effects of the VAT increase as insignificant by the time of the meeting of the Board of Directors on 26 April, and to speak of the completion of the tax increase pass-through to prices in June. The external environment in April – the first half of June was relatively favourable (see Section 3.1). In this context, exchange rate dynamics made an additional contribution to the slowdown of inflation. The revision of interest rate paths by the US Fed and other central banks in advanced economies helped reduce the risks of significant capital outflows from emerging markets. Overall, short-term proinflationary risks decreased as compared to March.

Consumer demand trends continued to constrain inflation. The receipt of data on GDP dynamics in 2018 and 2019 Q1 and the refinement of insights on the prospects of global economic growth resulted in a reduction of the forecast of the GDP growth rate in 2019 (see Section 1.1).

These developments enabled the Board of Directors to ease the signal about the future monetary policy at the April meeting, indicating the possibility of a key rate cut in 2019 Q2 – Q3 if the situation evolves in accordance with the baseline forecast, and, following the results of the June meeting, to revise the inflation forecast for 2019 downwards and reduce the key rate.

Monetary policy over a medium-term horizon. If the situation develops in line with the baseline forecast, the Bank of Russia admits the possibility of further key rate reduction at one of the upcoming Board of Directors' meetings and a transition to neutral monetary policy until mid-2020. The Bank of Russia continues to estimate the long-term neutral interest rate in the range of 2 – 3% in real terms and, accordingly, 6 – 7% in nominal terms. In its key rate decision-making, 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 posed by internal and external conditions and the reaction of financial markets.

Given the downward revision of the inflation forecast and GDP growth in 2019 in the baseline scenario and reduced short-term inflation risks as compared to March 2019, the expected key rate path was shifted downwards somewhat as compared to the path in the forecast made in Monetary Policy Report 1/19.

In the high oil price scenario, monetary policy will be close to that of the baseline one, as additional proinflationary and disinflation factors in the high oil price scenario, according to the Bank of Russia's forecast, will balance each other and cause inflation dynamics to be close to the baseline scenario over the entire forecast horizon (see Section 1.2). In the risk scenario and in case additional proinflationary risks materialise (see subsection 'Forecast uncertainty factors', Section 1.1), the key rate path will be higher than assumed in the baseline scenario mostly over a short-term horizon. If this is the case, a prompt response from the monetary policy will make it possible to limit the duration and scale of inflation deviation from the target.

The effect of the key rate decisions on expectations. Since the publication of Monetary Policy Report 1/19, market expectations for the key rate have mainly adjusted downwards. In late March 2019, after the Board of Directors' meeting, analysts and financial market participants were expecting a slight reduction of the key rate (by 25 bp, pursuant to the consensus forecast of analysts) in 2019 Q4. After the Bank of Russia eased the signal about its future monetary policy following the results of its meeting on 26 April, expectations continued to gradually adjust downwards. In early May, most analysts expected that the key rate would start decreasing no sooner than in 2019 Q3. As data was obtained evidencing that current inflation dynamics were forming below the path assumed by the forecast in Monetary Policy Report 1/19, the share of experts and market participants expecting that the key rate would be cut as early as in Q2 grew significantly. The scale of the monetary policy easing expected to take place this year also rose.

That was reflected in the dynamics of long-term money and stock market interest rates, including OFZs and corporate bonds (for details see Section 3.2). The decision to cut the key rate made by the Bank of Russia on 14 June 2019 and the signal about the future monetary policy will help anchor the updated expectations of market participants with regard to the key rate path.

4.2. THE SYSTEM OF MONETARY POLICY INSTRUMENTS AND OTHER BANK OF RUSSIA MEASURES

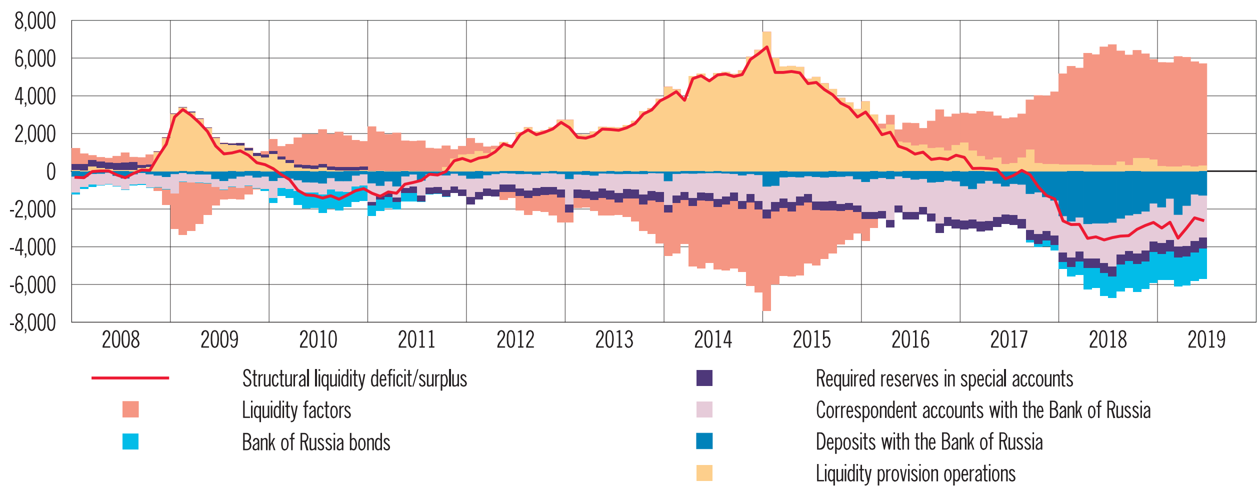
Banking sector liquidity. The structural liquidity surplus decreased in March – May 2019 from ₽3.6 trillion to ₽2.6 trillion. A significant outflow of funds formed as a result of banks making large tax payments on behalf of their customers and the placement of OFZs by the Russian Ministry of Finance. Amid seasonally low budgetary expenditures, this withdrawal of liquidity was not fully compensated by the growth of bank liabilities on deposits of the Federal Treasury and constituent entities of the Russian Federation.

The volume of cash in circulation did not significantly change during the period under review: the outflow of funds from banks before the May holidays and their inflow in March and May had a neutral effect on banking sector liquidity in aggregate.

Starting from 1 April 2019, the Bank of Russia's decision came into force that updates the composition of reservable liabilities of credit institutions. This decision was designed to increase transparency and standardise the procedure

BANK OF RUSSIA BALANCE SHEET
(START OF BUSINESS, BILLIONS OF RUBLES)

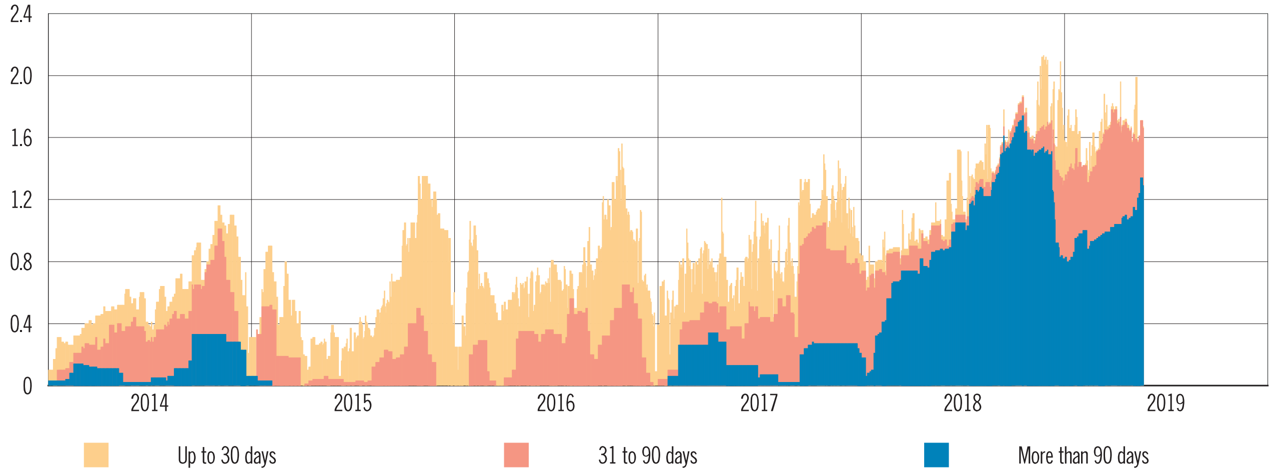
Chart 4.2.1



Source: Bank of Russia calculations.

BANKS' OUTSTANDING AMOUNTS ON FEDERAL TREASURY DEPOSITS, REPOS AND SWAPS
(TRILLIONS OF RUBLES)

Chart 4.2.2



Sources: Federal Treasury, Bank of Russia calculations.

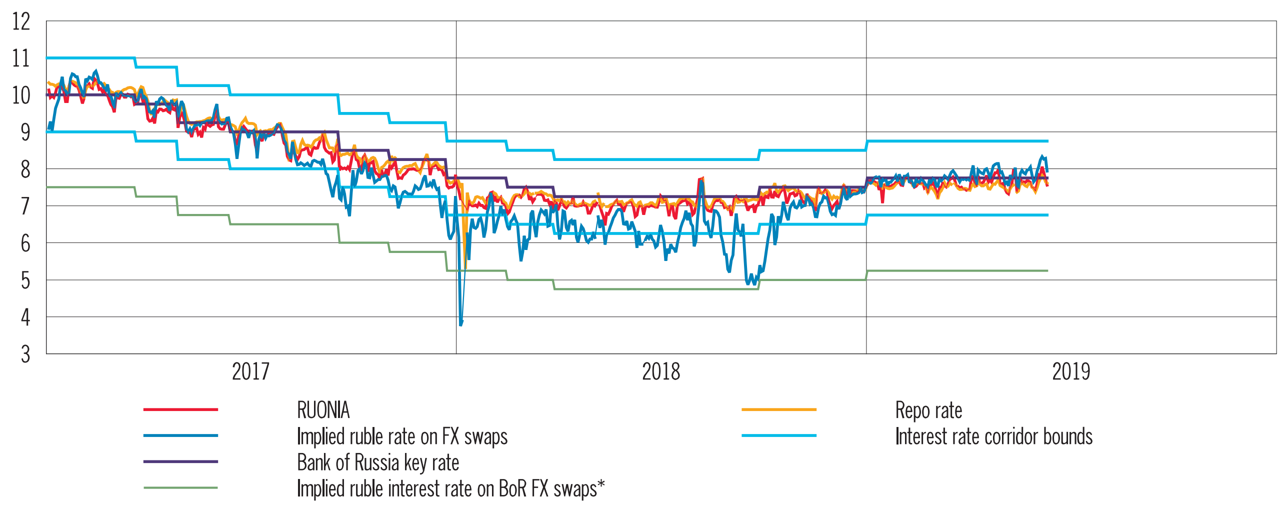
for the calculation of required reserves. To compensate for the increase in required reserves, the Bank of Russia simultaneously reduced the required reserve ratios for certain types of liabilities. Given the above, these decisions were generally neutral for the banking sector liquidity. The fact that banks increased their balances in correspondent accounts with the Bank of Russia as compared to early March due to a more even averaging of required reserves during the period under review facilitated the temporary decrease in surplus for March – May.

The structural liquidity surplus at the end of 2019 is expected to amount to ₽3.0 – 3.3 trillion. In 2020 – 2021, certain growth of the structural liquidity surplus related to further execution of foreign currency purchases in the domestic market under the fiscal rule postponed in 2018, is expected.

Federal Treasury operations for the administration of temporarily available budgetary funds. In April, in pursuance of measures for expanding the line of instruments, the Russian Ministry of Finance and the Federal Treasury prepared a procedure and rules for the administration of balances in the unified federal budget account to the extent of concluding bank deposit agreements with a central counterparty. Fund placement through deposits with a central counterparty will broaden the number of financial market participants that will be able to raise budgetary funds. The Bank of Russia will send suggestions

MONEY MARKET RATES
(%)

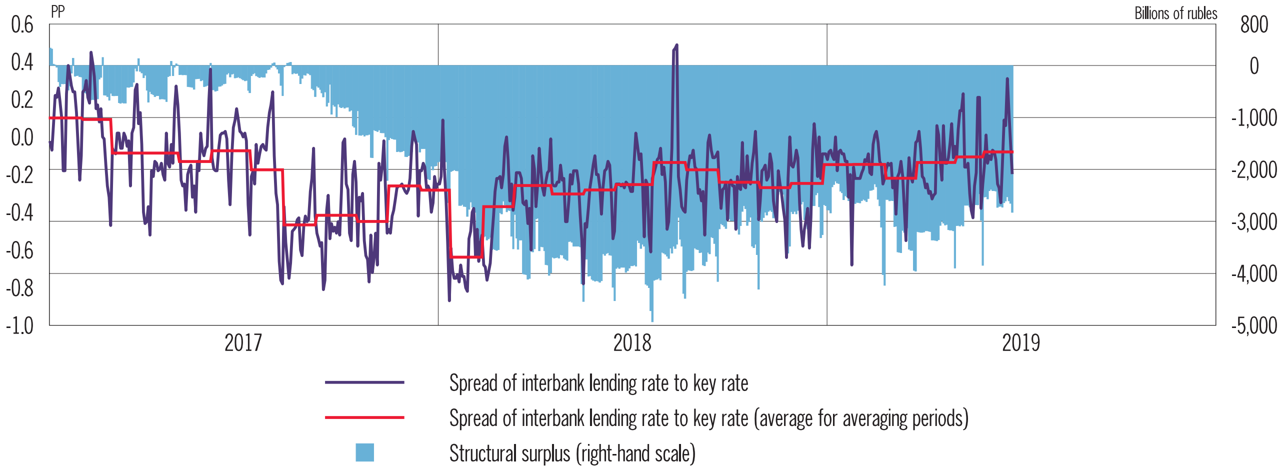
Chart 4.2.3



** Implied rate on reverse BoR FX swap = ruble lending rate - FX borrowing rate + LIBOR (from 19 December 2016: key rate – 1 pp - (LIBOR + 1.5 pp) + LIBOR = key rate - 2,5 pp).*
Source: Bank of Russia calculations.

STRUCTURAL LIQUIDITY SURPLUS AND MONEY MARKET RATES

Chart 4.2.4



Source: Bank of Russia calculations.

regarding the parameters of such operations to the Federal Treasury. Thus, recommendations on the minimum rate and the maximum amount of funds placement (if bank liabilities under these transactions exceed ₽100 billion) will be provided for operations for a period of 7 days or less, and recommendations on the maximum placement amount only, for operations for a period of 8 to 30 days. This will enable the Bank of Russia to restrict the potential effect of such operations on the volatility of short-term money market rates.

Achieving the operational goal of the monetary policy. Short-term rates in the interbank lending segment of the money market were formed in the lower half of the interest rate corridor close to the Bank of Russia key rate. The average spread from the beginning of April until 17 June was -9 bp (in Q1, -18 bp) and fluctuated in the range of -43 to 31 bp (in Q4, in the range of -55 to 6 bp). The decrease in the spread and its volatility was encouraged by even fulfilment of required reserve requirements by banks, without any significant front-running. Consequently, the supply at Bank of Russia deposit auctions was formed close to the established limits. The growth of banks' investments in Bank of Russia coupon bonds made it possible to additionally absorb a portion of the stable excess liquidity. This somewhat reduced banks' operations related to the need to manage large amounts of funds each week through weekly auctions. This also kept market rates near the Bank of Russia key rate.

STRUCTURAL LIQUIDITY SURPLUS AND LIQUIDITY FACTORS
(TRILLIONS OF RUBLES)

Table 4.2.1

	March 2019	April 2019	May 2019
1. Liquidity factors	**-0.1**	**-0.2**	**-0.1**
– change in the balances of general government accounts with the Bank of Russia, and other operations*	-0.2	0.0	-0.3
– change in cash in circulation	0.1	-0.2	0.1
– Bank of Russia interventions in the domestic FX market and monetary gold purchases	0.1	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)	**0.4**	**0.4**	**-0.3**
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	**-0.5**	**-0.6**	**0.2**
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	**0.0**	**0.0**	**0.0**
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	**-3.0**	**-2.5**	**-2.6**

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

Source: Bank of Russia calculations.

Deadline extension for submission of applications for Bank of Russia loans. Starting 15 April 2019, the Bank of Russia extended the deadline for submitting applications for Bank of Russia loans and requests for cancelling such applications in the electronic form until 8:25 p.m. Moscow time. The time extension allowed credit institutions to manage their own liquidity in the course of the settlement period of the Bank of Russia Payment System's regular session. During that time (8:00 p.m. – 9:00 p.m.), credit institutions do not execute new customer payments, which enables them to more precisely evaluate the balance of their accounts with the Bank of Russia and decide how much funds they need to raise or place in the interbank market or through Bank of Russia operations before the end of the business day without forming an excessive liquidity reserve. The availability of Bank of Russia operations during the settlement period allows preventing cases when, in the evening, credit institutions perform transactions in the interbank market at rates outside the Bank of Russia interest rate corridor.

BOXES

DYNAMICS OF HOUSEHOLD REAL DISPOSABLE MONEY INCOME

In 2018, real disposable household income grew slightly after a decrease in 2014–2017. The indicator's increase in 2018 H1 was to some extent caused by wage indexation in the budgetary sector pursuant to May decrees and a decrease in inflation to historical lows (Table 1[1]). In 2018 Q4 – 2019 Q1, real disposable household income went down again.

For example, in 2019 Q1, the decrease in real disposable household income was 2.3% as compared to 2018 Q1. This was caused by the accelerating inflation and slowing nominal income growth. In particular, in 2019 Q1, inflation accelerated by 3.0 pp vs 2018 Q1 (to 5.2%), while the contribution of nominal income growth decreased by 1.6 pp (to 3.5 pp).[2]

To some extent, the decrease in disposable income reflects an increase in interest payments for loans. In 2019 Q1, their negative contribution increased by 0.5 pp as compared to 2018 Q1 and amounted to -0.8 pp.[3] The growth of interest payments is caused by an increase in households' outstanding loans. With respect to consumer lending, the growth of debt is a sign of recovery: it slowed down in 2013–2014, and in 2015–2016 its volumes decreased (Chart 1). With respect to mortgage lending, the acceleration was caused by a reduction of long-term interest rates.

CHANGE IN HOUSEHOLD REAL DISPOSABLE INCOME
(CONTRIBUTION TO GROWTH, PP ON CORRESPONDING PERIOD OF PREVIOUS YEAR)

Table 1

Contribution to growth, pp on corresponding period of previous year	2018					2019
	Q1	Q2	Q3	Q4	Year	Q1
Money income	**5.1**	**4.7**	**4.5**	**3.8**	**4.5**	**3.5**
Including:						
Labour remuneration	6.8	7.7	7.5	6.7	7.2	3.4
Income from entrepreneurial and other production activity	0.3	0.3	0.9	0.1	0.4	0.1
Social benefits	-1.5	1.5	0.7	1.0	0.5	0.8
Property income	-0.1	0.0	0.2	0.3	0.1	-0.1
Other income	-0.5	-4.8	-4.6	-4.3	-3.7	-0.7
Mandatory payments and contributions*	**-1.5**	**-1.2**	**-1.3**	**-1.9**	**-1.5**	**-0.7**
Including:						
Interest on loans	-0.3	-0.3	-0.3	-0.6	-0.4	-0.8
Other mandatory payments	-1.1	-0.9	-0.9	-1.3	-1.1	0.1
Disposable income	**3.6**	**3.5**	**3.2**	**1.9**	**3.0**	**2.8**
Inflation (period average)	2.2	2.4	3.0	3.9	2.9	5.2
Household real disposable income	**1.3**	**1.1**	**0.2**	**-1.9**	**0.1**	**-2.3**

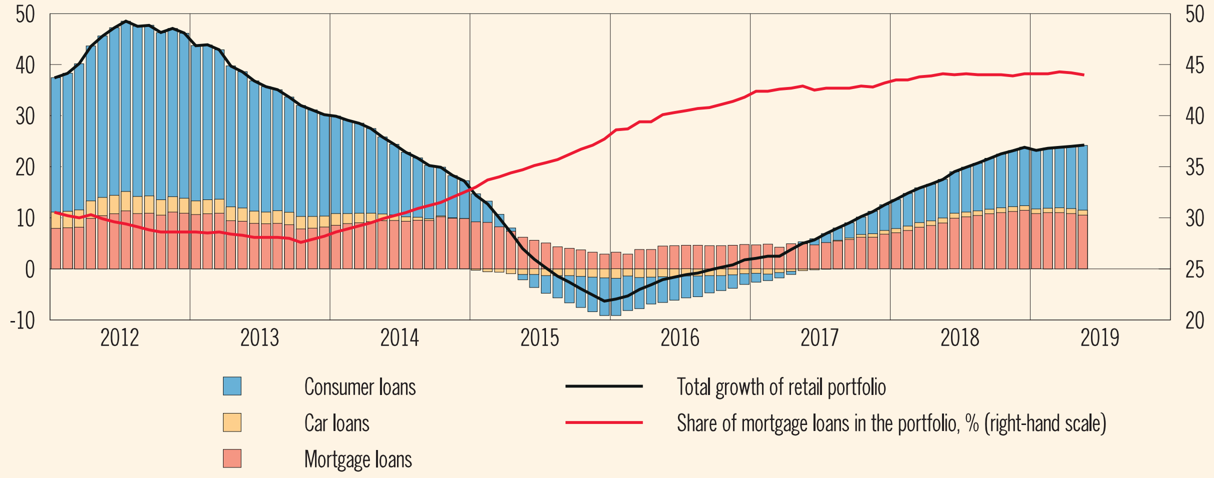
** Increasing mandatory payments has negative contribution*
Sources: Rosstat, Bank of Russia calculations.

[1] *Due to a change in methodology, comparable data about the dynamics of real disposable income components are available only from 2018.*

[2] *The effect of these factors was partially compensated by a decrease in other mandatory payments, including a significant drop in life insurance premiums. According to the data of the All-Russian Insurance Association, life insurance premiums decreased by 5.5% YoY at the end of 2019 Q1. Investment life insurance, which accounts for over 46% of insurance premiums, dropped the most (-26.1%). The negative dynamics in the investment life insurance market may be caused by the expansion of Bank of Russia requirements for the disclosure of information about insurance products by both insurers and their partner banks.*

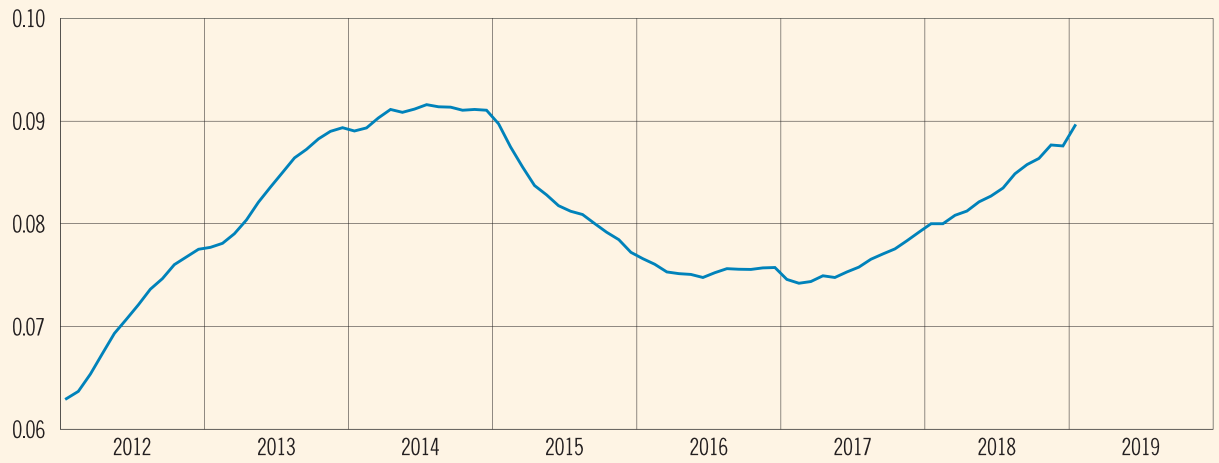
[3] *For reference: when using the old methodology of household income and spending statistics, the negative contribution of the growth of interest payments in 2012–2013 was 0.9–1.7 pp.*

CONTRIBUTION OF INDIVIDUAL COMPONENTS TO ANNUAL GROWTH OF RETAIL LOAN PORTFOLIO* *Chart 1*
(PP)



** Claims grouped into homogenous loan portfolios.*
Source: Bank of Russia.

HOUSEHOLD DEBT SERVICE RATIO *Chart 2*
(AS % OF MONEY INCOME)



Source: Bank of Russia calculations.

At the same time, the share of mortgages in banks' retail loan portfolio has been growing since 2013. Mortgage lending is characterised by significantly lower interest rates as compared to car and consumer lending, and the repayment of mortgage loans takes more time. In this context, the growing share of mortgage loans in household liabilities leads to a slower growth of the debt burden.

It should be noted that the specifics of statistical accounting of interest payments in the case of mortgage servicing overvalue their effect on household disposable income/purchasing power. For example, for some households, the purchase of real estate using a mortgage loan is an alternative to renting it, i.e. mortgage servicing replaces rent payments. Interest paid is recorded as mandatory payments, while rent expenses are reflected in the statistics of consumer expenses. As a result, the reduction of disposable household income caused by increased interest payments under mortgage loans has a smaller effect on the purchasing power due to lower rent expenses.

Thus, the increase in loan interest payments is a secondary factor having a negative impact on the dynamics of real disposable household income. Furthermore, the significant share of mortgages in the loan portfolio overstates the negative impact of interest payments on household budgets, as it simultaneously reduces rent expenses.

In general, the debt burden of Russian households, as characterised by the debt service ratio (hereinafter, the DSR),[4] is at a moderate level compared to both advanced and developing economies. According to Bank of Russia estimates, DSR of Russian households in 2019 Q1 amounted to about 9% of money income (Chart 2). This is 2–2.5 times less than in advanced economies and 20–30% less than in EMEs. At present, the Bank of Russia does not expect the formation of bubbles in retail lending and is taking macroprudential measures to prevent them. However, this indicator takes into account the income of the Russian population in general, including those who do not have any loans. The irregular distribution of the credit burden may strengthen its influence on the aggregate demand.[5]

[4] *This indicator is calculated using the following formula:*

$$\mathrm{DSR} = \frac{D_t \times i_t}{Y_t \times (1-(1+i_t)^{-s_t})} = \frac{D_t}{Y_t} \times \frac{i_t}{(1-(1+i_t)^{-s_t})},$$

where D_t – is the aggregate debt;
i_t – s the average interest rate for loans and borrowings weighted by debt amount;
s_t – is the average maturity weighted by debt amount;
Y_t – s the current yield.

[5] *For more details see 'Financial Stability Review. 2018 Q4 – 2019 Q1'.*

SURVEY MICRODATA-BASED ASSESSMENT OF THE RELATIONSHIP BETWEEN INFLATION EXPECTATIONS AND HOUSEHOLD SAVING BEHAVIOUR

Inflation expectations play a key role in the inflation targeting regime aimed at maintaining consistently low inflation near the target value. When making its monetary policy decisions, the regulator considers the dynamics of inflation expectations, striving to influence them through its forecasts and statements.

Inflation expectations have a direct impact on the operation of the interest rate channel of the monetary policy transmission mechanism. If inflation expectations decrease with unchanged nominal rates, real interest rates must increase, making consumption today more expensive as compared to consumption tomorrow. Households with savings must make a decision about the amount of their savings. Growing real interest rates mean that households that smooth their consumption will increase savings and reduce their consumer demand today, which will affect economic activity and inflation dynamics.

Households with no savings allocate all their resources to current expenses and, consequently, are less guided by interest rates in their decisions about consumption volumes. Of course, a number of such households use loans to finance consumption. However, consumer loan rates are materially higher than deposit rates, and therefore are less sensitive to monetary policy tools. For this reason, as regards the population, the interest rate channel acts to a greater extent through the group of households with savings. In this context, the following question is appropriate: are there any significant differences in the inflation expectations of households with savings and households without them?

To answer that, the results of monthly surveys commissioned by the Bank of Russia and conducted by inFOM from April 2014 through April 2019 and containing both a question about inflation expectations and a question about the existence of savings were considered.[1] The share of the subsample with savings in all respondents is quite consistent and amounts to about 35%.

An important feature of the survey data on inflation expectations is interval responses. Interval data arise when only the lower and upper limits of the variable interval are observed, and its true value remains unknown. On the one hand, interval responses make it possible to increase the probability of receiving a response from a respondent as compared to concrete responses, which decreases gaps in data. On the other hand, when calculating statistical indicators and testing hypotheses, certain assumptions about the distribution of responses within intervals are required.

To evaluate statistical indicators based on interval data, a linear interpolation, i.e. an assumption about the uniform distribution of an indicator within each interval, is used. To plot the median value of inflation expectations by subgroups in each survey wave, a bootstrap of subsamples from interval data is made with weights reflecting the number of observations in each interval, and the median value and its confidence interval is plotted based on the obtained ‘artificial’ samples.

The obtained results demonstrate that the median value of inflation expectations for the subsample with savings is almost always lower than the median value of inflation expectations for the subsample without savings (Chart 1). Average values for each subsample for last five years and two years, the difference between them, and the maximums and minimums are given in Table 1.

It should be noted that, in inflation acceleration episodes, except for the end of 2014, inflation expectations of households without savings grow more than the inflation expectations of households with savings.

Table 1

	April 2014 – April 2019			April 2017 – April 2019		
	Average	Minimum	Maximum	Average	Minimum	Maximum
With savings, %	11.1	6.9	17.4	8.8	6.9	10.6
Without savings, %	12.8	8.2	18.3	10.0	8.2	11.4
Difference, pp	1.8	-0.3	4.9	1.2	0.1	2.6

[1] *‘In your opinion, how much will prices grow in the next 12 months?’ and ‘Do you (does your family) have any savings / money savings or not?’.*

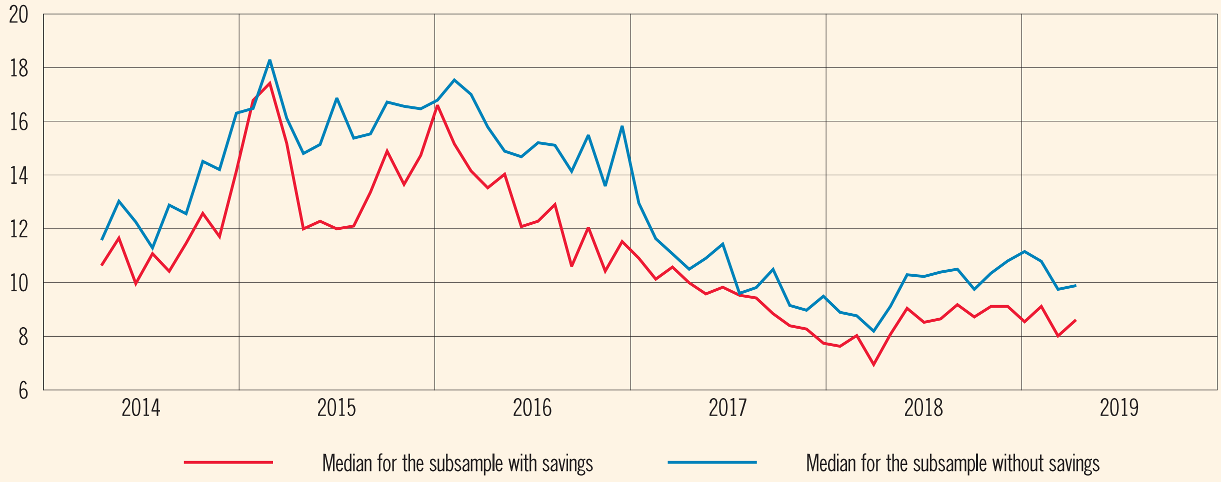
To test the hypothesis about the statistical value of the observed difference in the median values of inflation expectations in the subsamples with savings and without savings, the bootstrapped interval was plotted for the difference of the median values. A statistically significant (90% significance level) difference of median values is confirmed in practically all survey waves for the subsamples under review (Chart 2).

Thus, the survey data confirm the existence of a material interrelation between savings behaviour and the inflation expectations of households. This interrelation works both ways. On the one hand, households with lower inflation expectations, all else being equal, will be more inclined to accumulate savings, having a higher assessment of the expected real interest rate on their savings. On the other hand, households with savings form more rational inflation expectations, which is reflected in a narrower range of their variation and a smaller deviation from the Bank of Russia's target.

As noted above, the behaviour of 'saving' households has greater significance for the monetary policy transmission mechanism. With that in mind, monitoring of inflation expectations of this category of households is a useful addition to the analysis of inflation expectations in general.

INFLATION EXPECTATIONS DYNAMICS
(BY GROUP OF RESPONDENTS, % YOY)

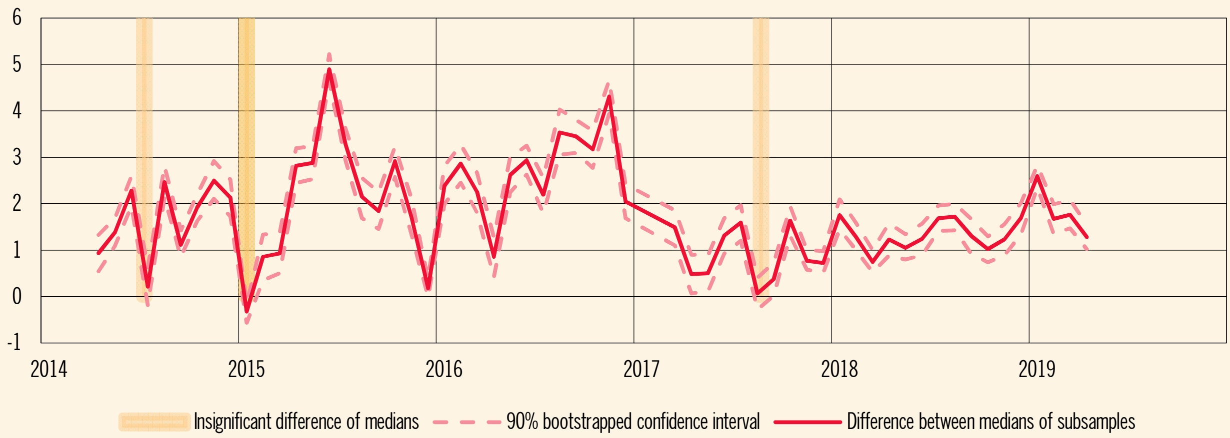
Chart 1



Source: Bank of Russia.

DIFFERENCE BETWEEN INFLATION EXPECTATIONS MEDIANS OF RESPONDENTS WITH AND WITHOUT SAVINGS IN THE CURRENT PERIOD

Chart 2



Source: Bank of Russia.

ANNEXES

ECONOMIC SITUATION IN RUSSIAN REGIONS

In March – May 2019, after several months of homogeneous acceleration, the dynamics of inflation in the regions diverged. The number of regions where inflation was slowing down in April – May exceeded half of the total number. However, the regional heterogeneity of price dynamics decreased, mainly due to a slowdown in inflation in regions where its values were highest. The dynamics of the economic activity in federal districts also became more homogeneous, with a decrease in the number of regions with positive growth rates. The slowdown of production activity contained the growth of household income and consumer demand in most federal districts..

PRINCIPAL ECONOMIC AND INFLATION INDICATORS BY FEDERAL DISTRICTS
(%)

Table 1

	Central FD	North-Western FD	Southern FD	North Caucasian FD	Volga FD	Urals FD	Siberian FD	Far Eastern FD
Inflation (May)	5.3	4.9	5.6	5.4	5.0	4.3	5.4	5.0
Economic activity indicator (YoY, April)	2.3	0.5	-1.9	-3.1	2.0	2.2	2.3	1.8
Industrial production (YoY, April)	9.4	4.8	2.6	1.1	4.1	6.3	1.9	12.2
Retail trade turnover (YoY, April)	1.4	1.6	2.8	0.8	1.6	2.1	0.4	0.9
Volume of paid services (YoY, April)	0.5	-0.2	1.7	0.7	1.8	3.2	3.9	-5.9
Volume of construction works (YoY, April)	-10.3	-20.6	-28.9	-23.7	-12.1	-18.5	1.1	-2.9
Growth in outstanding amounts on household loans (YoY, April)	25.4	25.1	24.5	22.9	22.6	20.8	21.0	21.5
Growth in outstanding amounts on corporate loans (YoY, March)	5.7	8.9	1.5	5.2	-4.8	1.0	4.8	15.7
Real wage (YoY, March)	4.1	1.5	2.4	1.0	1.2	-1.0	1.6	1.6
Unemployment rate (Q1)	3.0	3.7	5.5	11.6	4.4	4.5	6.5	6.1

Sources: Rosstat, Bank of Russia.

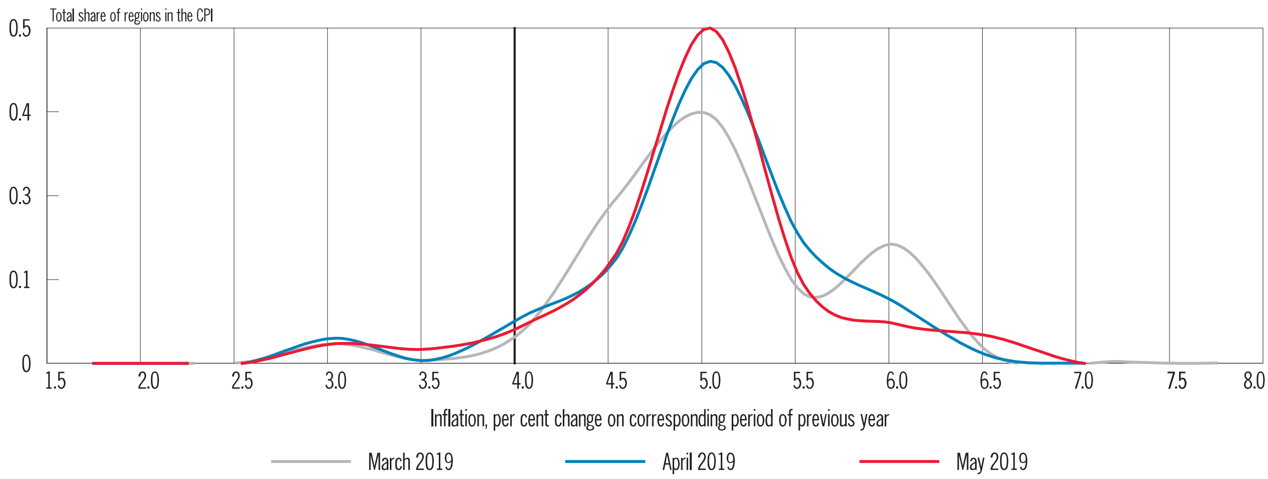
INFLATION AND PRICE EXPECTATIONS

DISTRIBUTION OF REGIONS BY INFLATION LEVEL

After homogeneous acceleration of price growth in the regions in December – February, the dynamics of regional inflation in March – May were mixed. In March, a slowdown in price dynamics was recorded in almost half of the regions (37 out of 85), while in April and May the number of such regions was over 40 (45 in April and 42 in May). Inflation slowed the most in April – May in the Central Russia, while price growth was accelerating in many southern regions and in constituent entities with the lowest inflation (the Nenets Autonomous Area, the Yamalo-Nenets Autonomous Area, and Yakutia). In general, against the background of a slowdown in the countrywide dynamics of prices, in April – May, the spread of regional inflation values decreased; that spread had been growing since November 2018, due, among other things, to a non-uniform manifestation of the effect of the VAT increase in the regions. Annual inflation values in the regions varied in May from 2.6 to 7%, with the countrywide average value of 5.1%. The regional distribution of inflation also changed: it retained a ‘three-headed’ form in late 2018 – early 2019 and became more homogeneous in April – May (Chart 1). In those months, inflation was slowing down in regions where its values were highest, as a result of which they moved to the main group. At the same time, in the group comprising certain regions

DISTRIBUTION OF REGIONS BY ANNUAL INFLATION

Chart 1



Sources: Rosstat, Bank of Russia calculations.

of Western Siberia (the Tyumen Region, the Khanty-Mansiysk Autonomous Area, the Yamal-Nenets Autonomous Area, and the Altai Republic), the Far East (Sakhalin, Yakutia), the Udmurt Republic, and Ingushetia, inflation was still significantly below the average Russian level. Higher inflation, despite a slowdown, remains in many regions of the Central Russia, in the South, and in Siberia (Chart 3).

FOOD INFLATION

Food inflation continues to make a major contribution to the preservation of the regional heterogeneity of price dynamics, although its range in April – May narrowed as compared to previous months (Chart 2). The values of inflation of food products in the regions in May varied from 2.1 (the Yamalo-Nenets Autonomous Area) to 9.2% (the Kabardino-Balkar Republic), whereas values for the main group of regions (66 out of 85 constituent entities) are in the range from 4.9 (the Kirov Region) to 7.9% (Sevastopol). In April – May, acceleration of food inflation continued. The most significant acceleration was recorded in a number of southern regions. The dynamics of prices for fruit and vegetables made a major contribution to the acceleration. The faster-than-expected growth of prices for those products was caused, among other factors, by a decrease in reserves of field vegetables due to a reduced harvest in 2018 in some regions that are major producers (including the Volgograd Region, the Rostov Region, the Kabardino-Balkar Republic, Dagestan, Crimea, and the Stavropol Territory). Moreover, the supply of greenhouse vegetables decreased in the North Caucasus due to the refocusing of some producers on flower growing (related, pursuant to surveys of enterprises, to the higher profitability of that activity type). In March – April, accelerated growth of prices of meat products was observed in a number of republics of the North Caucasus, caused by a decrease in the supply of lamb and poultry as a result of a strike of producers, a fire at a major enterprise, and the continuing growth of exports of certain meat products to Azerbaijan and Iran. Food inflation slowed down in April – May in many regions of the Central Russia and the North-West, where large reserves of potatoes contained the price increase. The dynamics of food prices also slowed down in some regions of the Far East, which may be caused by peculiarities of the delivery of certain products, including imported goods, amid the continuing strengthening of the ruble.

NON-FOOD INFLATION

Inflation of non-food goods in May remained relatively homogeneous by regions (as compared to inflation of food products and services): indicator values for the main group of regions (75 constituent entities with a total weight in the country CPI of over 94%) varied from 2.5 (Dagestan) to 5%

(Buryatia). The slowdown of non-food inflation recorded in most regions in April – May was mainly caused by a decrease in the annual growth rate of motor fuel prices. The most significant slowdown was recorded in a number of regions of the Central Russia, Siberia and the North Caucasus, where the high base effect in petroleum product prices was the strongest. In most regions in April – May, a slowdown of the growth of passenger car prices was observed due to the strengthening of the ruble. The dynamics of prices for other non-food goods in the regions was varied and was determined by local factors to a great extent. In general, the slowdown of inflation of non-food goods made a major contribution to the general inflation slowdown in most regions (83 out of 85).

INFLATION IN THE SERVICES SECTOR

The spread of services inflation in the regions in May remained significant: indicator values ranged from 1.5 (Ingushetia) to 10.4% (Sevastopol), while for the main group of regions (73 constituent entities with a total weight in the country CPI of over 94%) they ranged from 3.6 (North Ossetia) to 7% (the Mari El Republic). After a slowdown in service price dynamics in March – April, services inflation accelerated in May in most regions. Acceleration was the most significant in certain northern regions (the Nenets Autonomous Area and the Yamalo-Nenets Autonomous Area, and Yakutia), where it was caused by the strong growth of prices for passenger transportation services, which were catching up after an extended period during which tariffs remained unchanged.

PRICE EXPECTATIONS

The change in business price expectations for three months ahead in the federal districts in May was mixed. After a homogeneous decrease in February – April, in some federal districts (the North-Western Federal District, the Southern Federal District, and the Far Eastern Federal District) price expectations increased slightly in May (Chart 4), mainly due to the growth of expectations of agricultural enterprises caused by the effect of local factors in livestock production. Despite this, in general, price expectations in these districts remained close to the levels of the corresponding period of 2018. As in previous months, the highest business price expectations were recorded in the Urals. At the same time, annual inflation values in that district remained the lowest among all federal districts, which is indicative of the continued potential for the catch-up growth of price dynamics.

INFLATION BY INDIVIDUAL SUBCOMPONENT ACROSS FEDERAL DISTRICTS

Table 2

	Weight in CPI								Inflation (%, May)							
	Central FD	North-Western FD	Southern FD	North Caucasian FD	Volga FD	Urals FD	Siberian FD	Far Eastern FD	Central FD	North-Western FD	Southern FD	North Caucasian FD	Volga FD	Urals FD	Siberian FD	Far Eastern FD
All goods and services	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**5.3**	**4.9**	**5.6**	**5.4**	**5.0**	**4.3**	**5.4**	**5.0**
Food products	**36.2**	**37.2**	**40.4**	**45.2**	**37.4**	**36.5**	**37.8**	**37.4**	**6.7**	**6.0**	**7.4**	**7.2**	**6.0**	**5.1**	**6.7**	**6.0**
– excluding fruit and vegetables	**32.5**	**32.9**	**35.6**	**38.8**	**33.8**	**32.8**	**34.0**	**33.1**	**6.5**	**5.4**	**6.5**	**5.9**	**5.6**	**5.0**	**6.6**	**5.9**
Meat products	10.1	8.5	10.0	12.8	8.9	8.5	9.3	8.5	8.7	8.4	9.2	9.5	8.2	6.7	9.3	9.8
Milk and dairy products	2.9	3.5	3.2	3.2	3.2	3.3	3.4	3.1	5.1	4.6	5.0	4.5	3.3	5.7	5.7	5.0
Fruit and vegetables	3.6	4.3	4.7	6.5	3.5	3.8	3.8	4.3	8.4	10.1	14.7	15.0	10.2	5.8	7.6	6.9
Bread, pasta and cereals	2.2	2.4	2.9	3.4	2.7	2.4	2.6	2.3	11.4	6.6	10.8	5.4	11.4	8.5	11.2	9.1
Fish products	2.8	1.7	2.1	2.1	1.8	1.7	1.9	1.8	5.0	5.5	3.8	4.3	5.2	4.5	4.1	0.0
Oils and fats	1.0	1.1	1.4	2.2	1.2	1.0	1.2	1.0	5.1	3.5	5.3	7.5	4.5	3.2	4.8	3.9
Eggs	0.5	0.5	0.6	0.6	0.5	0.5	0.5	0.6	9.4	8.6	3.6	5.9	5.4	9.5	9.6	3.7
Sugar	0.3	0.3	0.5	1.3	0.5	0.4	0.6	0.4	15.1	13.5	12.8	11.3	11.4	10.9	12.6	11.9
Other	11.0	12.6	11.9	9.4	12.7	12.5	12.0	12.8	3.8	3.0	3.6	2.9	2.8	3.0	4.5	4.0
Non-food goods	**34.4**	**34.0**	**34.9**	**32.9**	**35.6**	**35.1**	**36.7**	**34.2**	**4.2**	**3.6**	**3.6**	**2.9**	**3.9**	**3.1**	**3.9**	**3.2**
– excluding petrol	**30.0**	**29.5**	**31.1**	**28.6**	**31.3**	**30.4**	**32.0**	**29.8**	**4.5**	**3.7**	**3.6**	**3.1**	**4.0**	**3.0**	**4.0**	**3.0**
Clothes, footwear and fur goods	7.4	6.7	7.3	8.1	7.5	6.3	6.9	7.3	2.6	2.3	1.6	1.4	2.2	1.0	2.0	1.9
Passenger cars	6.3	5.6	5.3	2.5	6.4	7.6	6.2	4.4	6.0	4.6	5.2	5.0	5.4	4.2	3.7	2.2
Oil products	4.4	4.5	3.7	4.3	4.3	4.7	4.7	4.4	2.5	3.3	3.4	2.0	3.4	3.3	3.1	4.5
Household appliances	2.7	2.4	3.3	2.7	2.8	2.5	2.6	2.6	1.5	-1.2	1.9	0.5	1.1	0.7	0.0	0.3
Furniture and construction materials	2.8	2.5	3.3	3.2	3.3	2.5	2.9	2.9	5.3	4.1	3.8	3.9	5.4	3.6	5.2	3.7
Household chemicals	0.7	0.8	0.9	1.1	0.9	0.7	0.9	0.9	6.4	5.6	3.8	5.3	5.3	2.9	4.5	7.4
Other	10.1	11.5	11.0	10.9	10.6	10.7	12.5	11.7	5.5	4.9	4.7	3.9	4.6	3.9	5.7	4.3
Services	**29.4**	**28.8**	**24.8**	**21.9**	**27.0**	**28.4**	**25.5**	**28.4**	**4.8**	**5.0**	**5.3**	**5.5**	**5.0**	**4.7**	**5.8**	**5.7**
– excluding utilities	**19.7**	**18.9**	**14.4**	**12.6**	**16.9**	**18.0**	**16.0**	**17.0**	**4.3**	**4.2**	**4.7**	**5.5**	**4.4**	**4.7**	**5.1**	**5.9**
Utilities	9.8	9.9	10.4	9.3	10.1	10.4	9.5	11.4	5.9	6.6	6.0	5.6	5.9	4.8	6.8	5.4
Personal services	3.5	3.8	3.3	2.8	3.1	3.1	2.7	3.2	2.8	3.6	4.3	3.2	3.8	2.5	4.2	4.1
Passenger transport	2.5	3.0	1.8	1.9	2.1	2.2	2.4	3.1	5.9	6.4	9.6	11.4	6.9	8.1	8.6	8.3
Tourism services	3.3	2.2	0.7	0.4	1.5	2.9	0.9	1.1	5.6	5.3	3.9	5.0	4.7	4.9	5.7	6.1
Education services	2.3	1.7	2.1	1.3	2.1	1.8	1.7	2.1	7.7	6.6	6.2	7.5	6.9	6.6	7.4	14.0
Medical services	1.7	1.5	1.4	1.2	1.6	1.4	1.2	1.4	3.2	4.5	3.6	3.7	5.3	5.1	5.7	5.4
Other	6.8	7.5	5.5	5.1	6.9	6.8	7.3	6.4	2.8	3.0	3.3	4.4	2.4	2.9	3.3	2.9

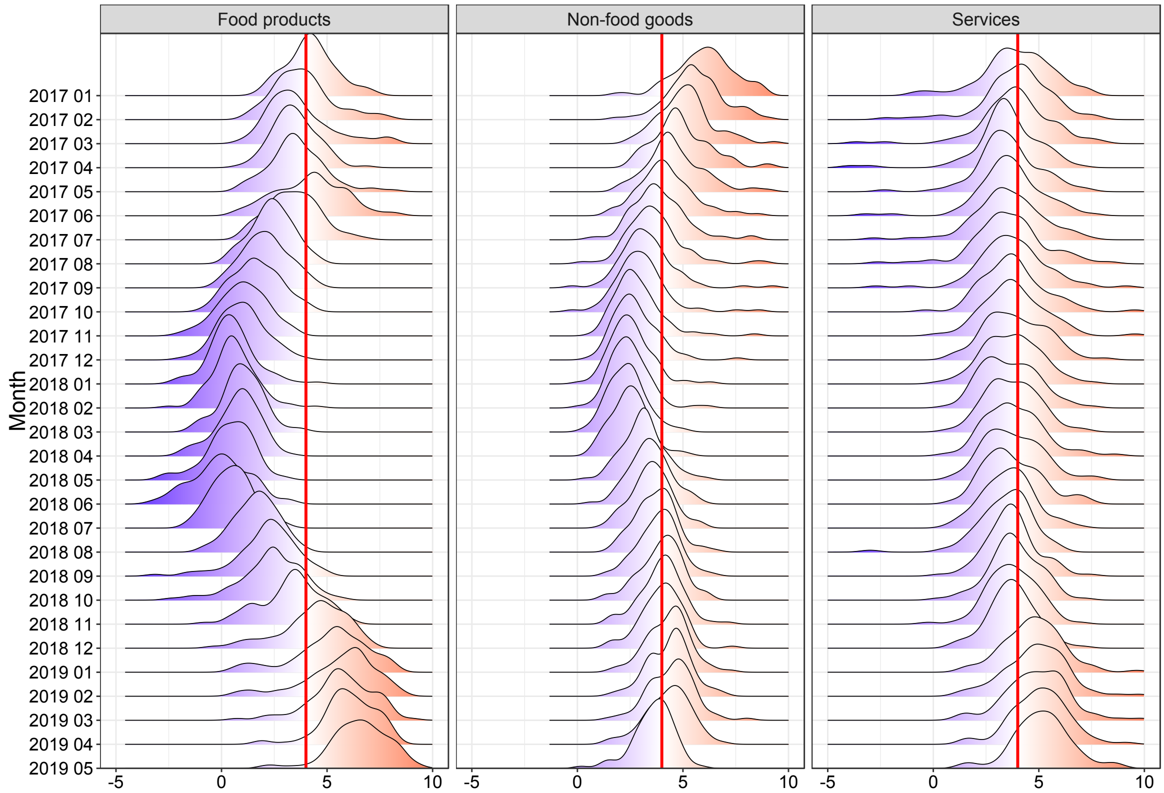
– *maximum values (weight and inflation) for all federal districts.*

– *minimum values for each subcomponent.*

Sources: Rosstat, Bank of Russia.

DISTRIBUTION OF REGIONS BY CONTRIBUTION TO ANNUAL INFLATION OF GOODS (FOOD AND NON-FOOD) AND SERVICES

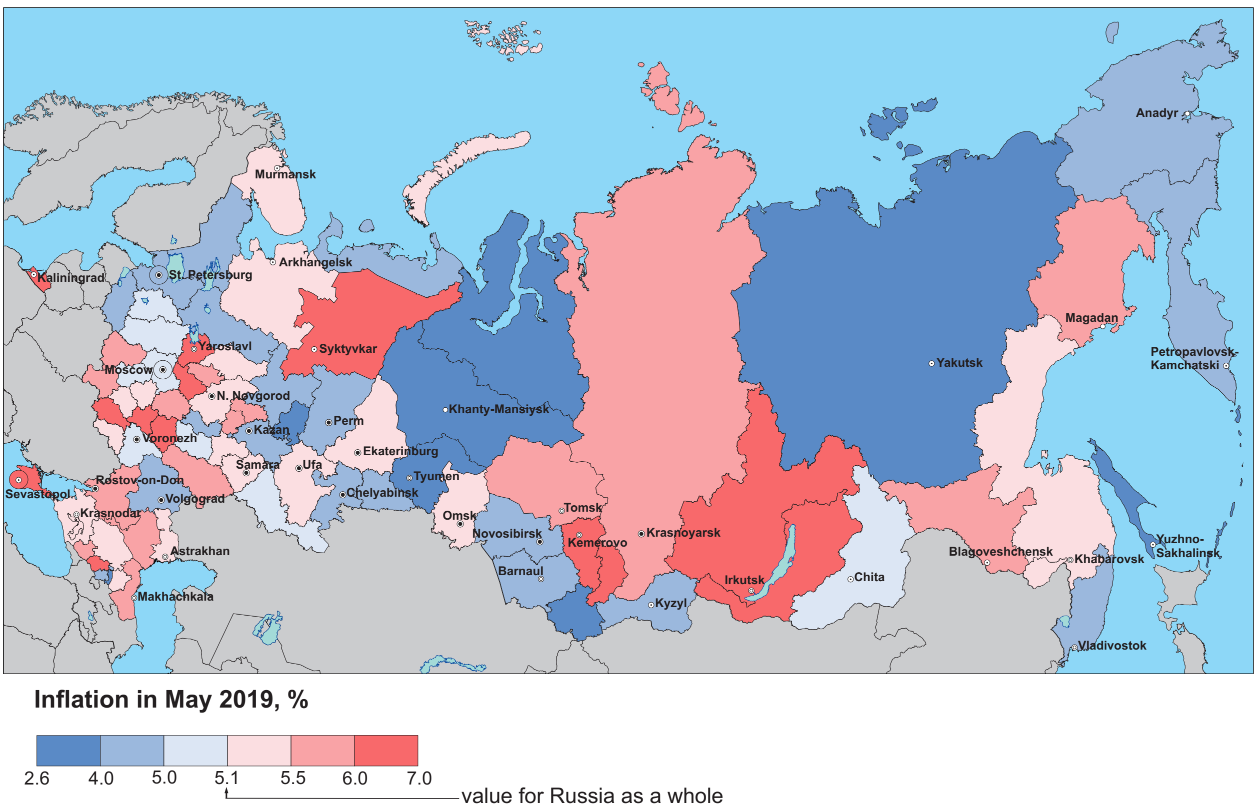
Chart 2



Note: the horizontal axis shows inflation (annualised, %); the vertical axis shows the total weight of regions.
Sources: Rosstat, Bank of Russia calculations.

INFLATION ACROSS REGIONS IN MAY 2019

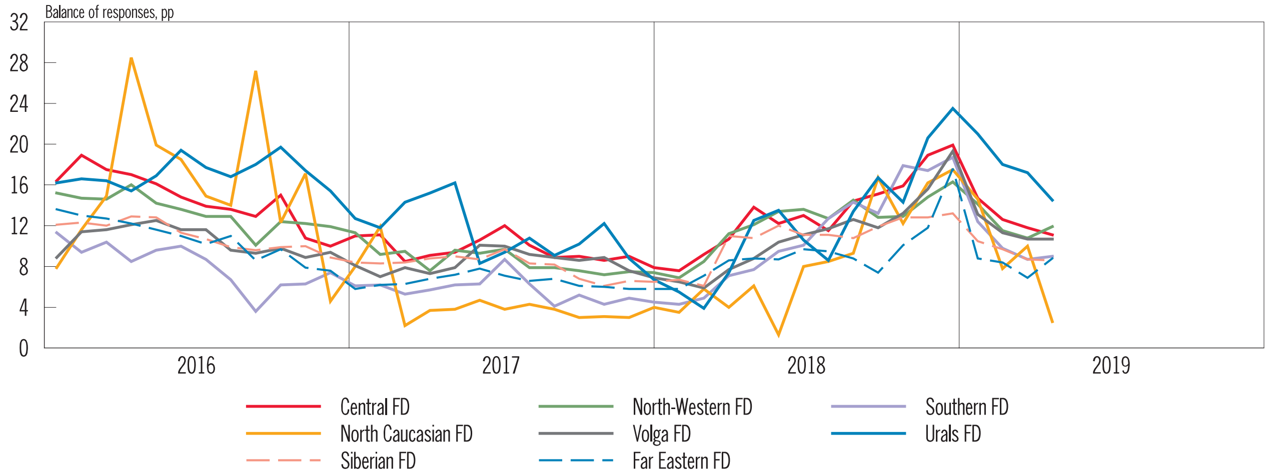
Chart 3



Sources: Rosstat, Bank of Russia.

BUSINESS PRICE EXPECTATIONS

Chart 4



Source: Bank of Russia.

MONETARY CONDITIONS

HOUSEHOLD LENDING

The dynamics of the assessment of price bank lending conditions (BLC) for households[1] in 2019 Q1 changed insignificantly (Chart 5). Their tightening, which occurred starting in 2018 H2 due to deteriorating external conditions, growing price expectations, accelerating inflation and increasing key rate, slowed down to some extent in the beginning of 2019 in many regions. The change of non-price lending conditions was also insignificant; their moderate easing continued in most regions. Certain tightening occurred only in the North Caucasus, where the highest loan risks remain, which is reflected by the overdue debt share indicator. In general, assessments of household lending conditions in all federal districts and most regions were within the neutral area (in 41 out of 68 where the survey was conducted): they were assessed as tight in 8 regions, and as soft in 19. Against the background of the stabilisation of BLC dynamics, the lending growth rates for individuals in March – April accelerated in all districts, having returned, after a slowdown in the beginning of the year, to the values of the last months of 2018. At the level of individual regions, growth of the household loan portfolio (YoY) in April in most constituent entities ranged from 17 (the Volgograd Region, Buryatia) to 32% (Ingushetia, the Chukotka Autonomous Area). In Crimea and Sevastopol, growth rates remain significantly higher (75 and 88%, accordingly), which is caused by the catch-up growth of consumer lending in those regions.

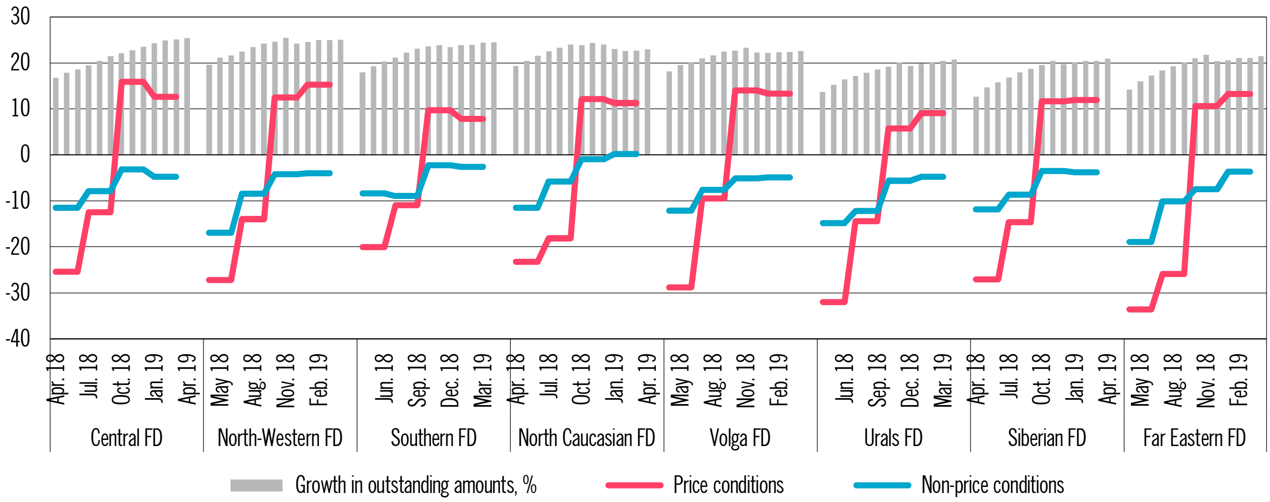
CORPORATE LENDING

Tightening of price bank lending conditions for corporate borrowers in 2019 Q1 slowed down significantly in all federal districts (Chart 6). Non-price conditions in most districts continued to ease, while an insignificant tightening, mainly related to higher collateral requirements, took place in the Central Federal District, the Volga Federal District, and the Far East. However, price bank lending conditions for legal entities in almost all federal districts are still mainly assessed as tight. The exception is the Urals Federal District, where BLC assessments are neutral. The dynamics of bank lending for enterprises in most regions in the beginning of 2019 were in the positive area. In Siberia, the Far East and the North Caucasus, where annual loan portfolio growth rates accelerated,

[1] *Pursuant to the data of a quarterly survey of major banks. BLCs are assessed on the basis of the diffusion index, which reflects the balance of the responses of credit institutions assessing the change in conditions as tightening or easing.*

CHANGE IN BANK LENDING CONDITIONS (NEGATIVE ZONE – EASING , POSITIVE ZONE – TIGHTENING) AND GROWTH IN OUTSTANDING AMOUNTS ON HOUSEHOLD LOANS (YOY)

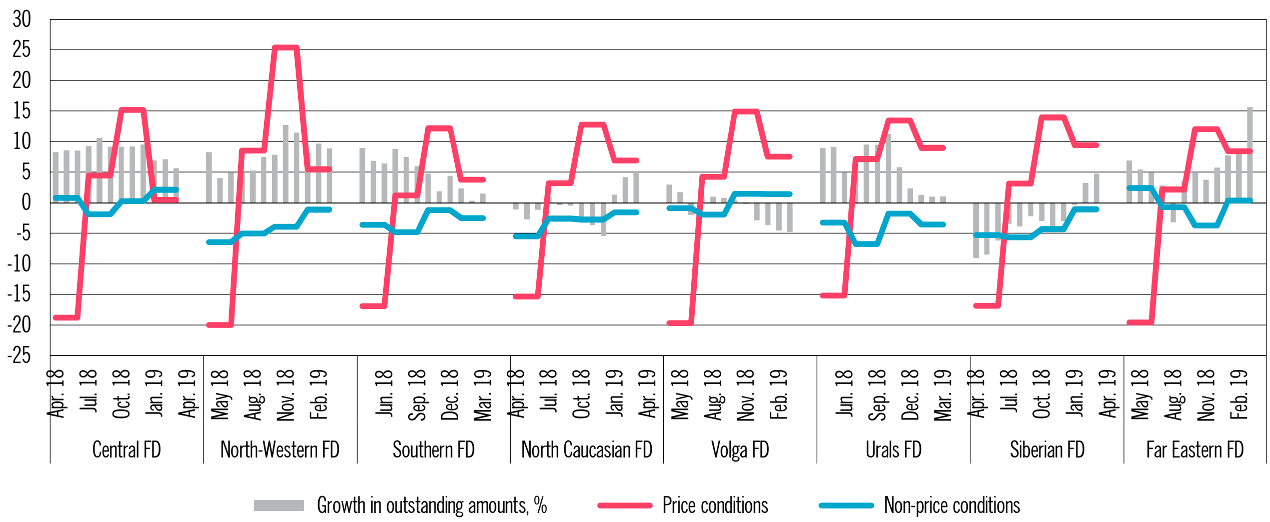
Chart 5



Source: Bank of Russia.

CHANGE IN BANK LENDING CONDITIONS (NEGATIVE ZONE – EASING , POSITIVE ZONE – TIGHTENING) AND GROWTH IN OUTSTANDING AMOUNTS ON CORPORATE LOANS (YOY)

Chart 6



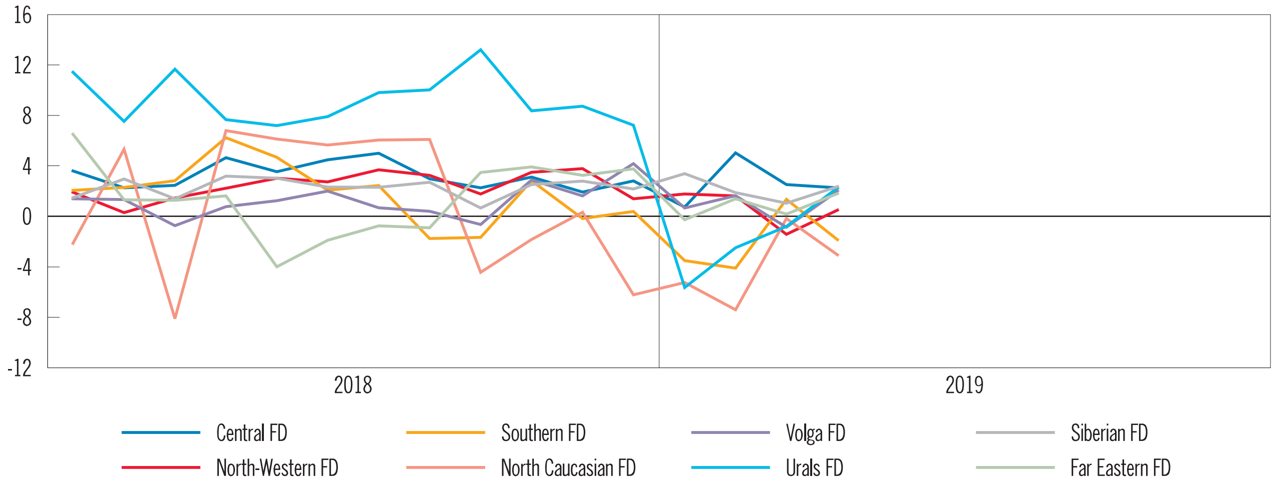
Source: Bank of Russia.

the extension of loans to a number of major systemically important companies in certain regions supported growth. Reduction of the corporate loan portfolio (YoY) was observed in the Volga Federal District, where the debt of industrial and construction companies was decreasing. The debt burden[2] of enterprises in the beginning of 2019 was decreasing in most regions. It grew slightly only in the North Caucasus, where the debt burden remains significantly below the average Russian level (22% vs 29% for Russia as a whole). At the same time, in half of the federal districts (Central, Southern, Volga, and Siberian), the share of overdue debt of corporate borrowers grew slightly.

[2] *The debt burden of corporate borrowers by region (federal district) was calculated as the ratio of outstanding corporate loans to the volume of goods shipped and works and services performed (12-month rolling sum).*

ECONOMIC ACTIVITY INDICATOR (JANUARY 2018 – APRIL 2019)
(YOY, %)

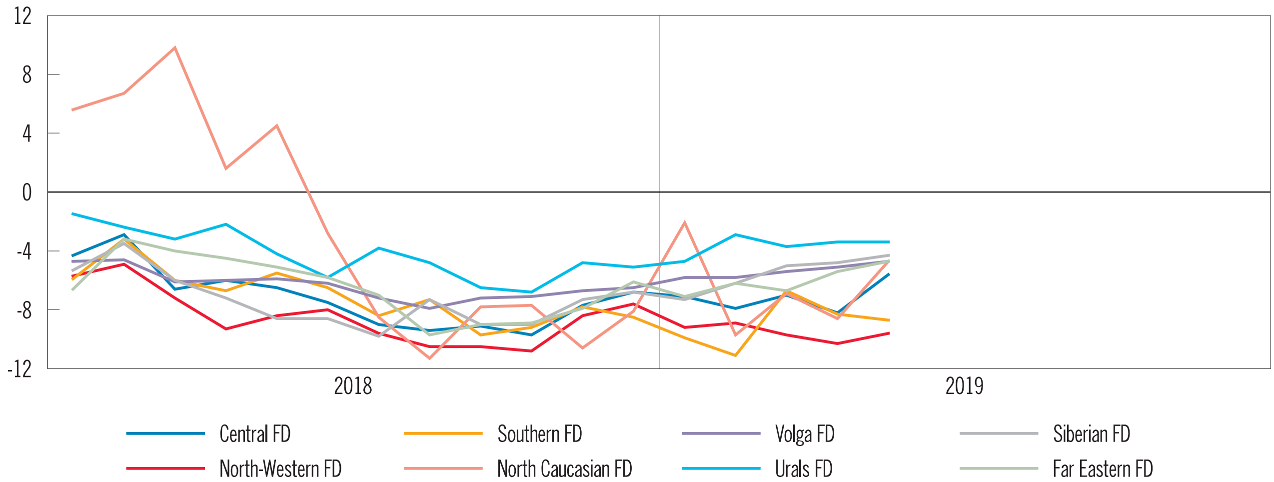
Chart 7



Sources: Rosstat, Bank of Russia calculations.

ASSESSMENT OF CHANGES IN ECONOMIC SITUATION BY BUSINESSES
(BALANCE OF RESPONSES, PP)

Chart 8



Source: Bank of Russia.

PRODUCTION AND INVESTMENT ACTIVITY

ECONOMIC ACTIVITY INDICATOR

In March – April 2019, there was a convergence of the dynamics of economic activity in various federal districts: the values of the economic activity indicator (EAI)[3] stayed in a narrow range near zero (Chart 7). Since the beginning of the year, the number of regions with positive dynamics of EAI has been decreasing: in December 2018, there were 61; in March 2019, there were 49; and in April, there were 50 such constituent entities. After a slowdown in March, the dynamics of economic activity in April accelerated slightly in most federal districts. Everywhere the main contribution to acceleration was made by industry, and in Siberia and the Urals, by services as well. In all districts, except for the Siberian Federal District, negative dynamics of construction continue (due, among

[3] *The economic activity indicator is calculated as the weighted average rate of the main economic activities: mining and quarrying, manufacturing, electricity, gas and steam supply, water supply, sewerage, waste collection and disposal, agriculture, construction, paid services provided to households, and trade. The weights of the respective economic activities in the structure of the gross regional product (GRP) are used as weights for calculating the average figure.*

other factors, to the high base effect); the greatest decrease was registered in the South and in the North Caucasus, where the reduction of construction works also causes an overall decrease in the EAI. The slowdown of economic activity in most regions in March was caused by the effect of both countrywide and industry- or region-specific factors. The first category included the effect of the VAT increase on manufacturers' costs and consumer demand and a slight tightening of monetary conditions. The second category included the adjustment of developers to changes in the regulation of equity housing construction and the completion of a number of major investment projects during previous periods in certain regions. In April, despite some acceleration of production activity dynamics, the economic growth rates in most regions remained below the values of 2018 H2.

BUSINESS SENTIMENT

Assessments of the economic environment by enterprises that participate in Bank of Russia monitoring improved slightly in April – May in most federal districts, remaining, in general, near the average values of previous months (Chart 8). The moderate improvement of assessments of the environment in the regions, according to survey data, was promoted by a continuing weakening of the negative effect of FX rate changes and the slight improvement of the assessment of the demand for the products of enterprises. Nevertheless, demand assessments remain mostly in the negative area. For almost half (47%) of the enterprises surveyed, low demand remains a factor restricting production growth, and enterprises do not expect a significant improvement in demand in the next three months: the balance of responses remains at the level of the first months of 2019.

INVESTMENT

Investment activity dynamics in 2019 Q1 moved into negative territory in most federal districts, except for the Central Federal District and the Siberian Federal District. In many regions, a slump or the deceleration of investment dynamics (YoY) was caused by the completion of a number of major investment projects in 2018. In the Central Russia and Siberia, investment growth in some major regions encouraged the preservation of positive dynamics at the district level: in Moscow, where major projects are being implemented in housing construction and transport; in the Irkutsk Region, the Kemerovo Region and the Krasnoyarsk Territory, where mining and quarrying and metallurgy industry facilities prevail among major investment projects. In 2019 Q1, the assessments of investment activity by enterprises that participate in Bank of Russia monitoring deteriorated slightly in most federal districts, except for the Central Federal District and the North-Western Federal District. In all districts except for the North Caucasian Federal District, the balance of responses remains in positive territory, near the average values of the previous year.

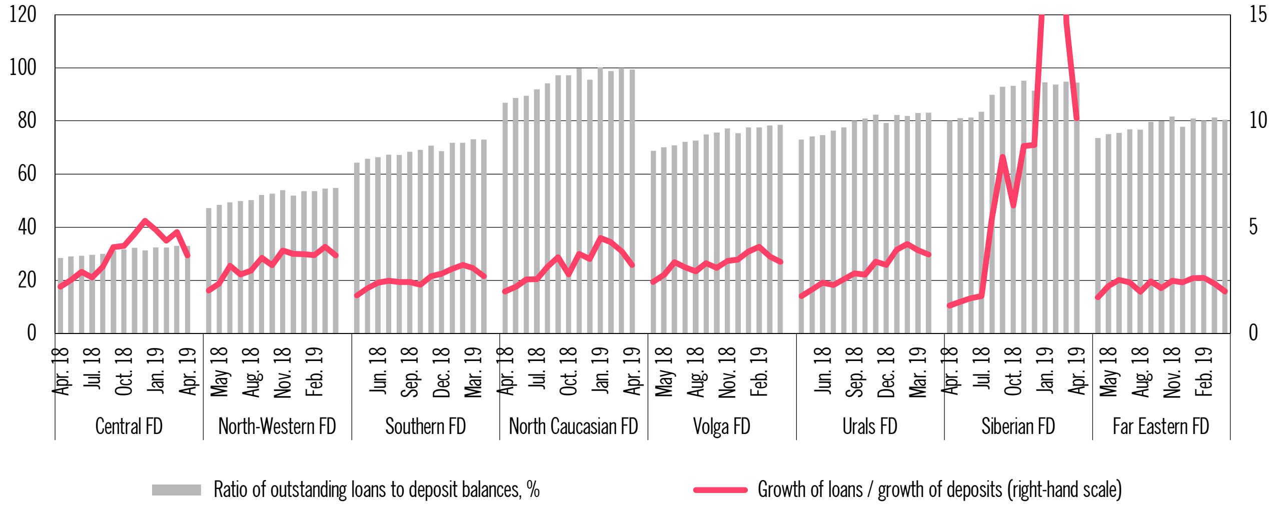
CONSUMER DEMAND AND SAVINGS

REGIONAL CONSUMPTION PECULIARITIES

The dynamics of the retail trade turnover and the value of paid services (YoY) in the first months of 2019 remained positive in most federal districts, having slowed down almost in all federal districts as compared to the levels of 2018 H2 (Chart 9). Negative dynamics of paid services in March – April were recorded in the North-Western Federal District and the Far Eastern Federal District. In the North Caucasus, the retail trade turnover has been heavily volatile and has stayed largely in the negative territory since mid-2018 amid a strong slowdown of annual household income growth rates. Continued growth of real wages in most Russian constituent entities and consumer lending growth, the rates of which recovered in all federal districts after a slowdown in the beginning of the year, contributed to the overall preservation of positive demand dynamics in the regions (Chart 10). In many federal districts, household deposit growth rates accelerated. However, they remain significantly below household lending growth rates.

HOUSEHOLD LOANS AND DEPOSITS IN FEDERAL DISTRICTS*

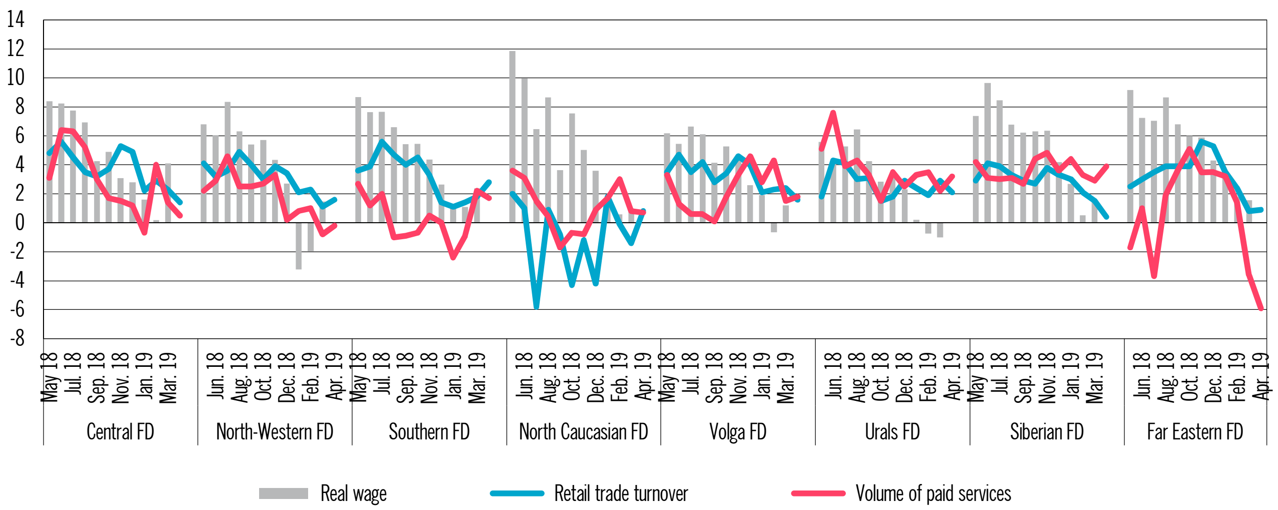
Chart 9



** The outlier in the dynamics of deposit growth in the Siberian Federal District is related to changes in statistic accounting by branches in one of the Novosibirsk region banks.*
Source: Bank of Russia.

REAL WAGE, RETAIL TRADE TURNOVER, AND VOLUME OF PAID SERVICES
(YOY, %)

Chart 10



Source: Rosstat.

LABOUR MARKET AND INCOMES

REGIONAL LABOUR MARKETS

The employment rate[4] in 2019 Q1 decreased slightly as compared to the values of the corresponding period of the previous year in most regions and in all federal districts. Its values in the regions varied widely: from 49 (the Karachay-Cherkess Republic) to 78% (the Chukotka Autonomous Area), with a countrywide average value of 64.5%. The growth of real wages (YoY) in March accelerated in most federal districts after a slowdown or slump in January – February; this indicator decreased only in the Urals (Chart 9). Here wage dynamics have been in the negative territory since February: real wages were decreasing in the Khanty-Mansiysk Autonomous Area, the Yamal-Nenets Autonomous Area, and the Kurgan and Chelyabinsk Regions. The inflation slowdown that started in most regions in April will support the growth of real wages in the months to come. The unemployment rate in 2019 Q1 (seasonally adjusted) continued to decrease in most regions. The exceptions were some regions

[4] *For the population aged 15 to 72.*

of the North Caucasus (Kabardino-Balkaria, Dagestan, Ingushetia, and Karachay-Cherkessia) and the South of Siberia (the Tyva Republic, the Altai Territory), where the unemployment rate, which traditionally exceeds average Russian values, increased slightly. In general, the values of this indicator by regions in January – March 2019 varied from 1.2 (Moscow) to 26.8% (the Republic of Ingushetia).

STATISTICAL TABLES

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

Purpose	Type of instrument	Instrument	Term	Frequency	As of 01.01.18	From 12.02.18	From 26.03.18	From 17.09.18	From 17.12.18	From 17.06.19	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	8.50	8.75	8.50	Key rate + 1.00
		Loans secured by non-marketable assets[3]	From 2 to 549 days		9.50	9.25	9.00	9.25	9.50	9.25	Key rate + 1.75
	Open market operations (minimum interest rates)	Auctions to provide loans secured by non-marketable assets[3]	3 months	Monthly[4]	8.00	7.75	7.50	7.75	8.00	7.75	Key rate + 0.25
		Repo auctions	1 week	Weekly[5]	7.75 (key rate)	7.50 (key rate)	7.25 (key rate)	7.50 (key rate)	7.75 (key rate)	7.50 (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	1 day[7]	Daily	6.75	6.50	6.25	6.50	6.75	6.5	Key rate - 1.00

[1] *From 4 June 2018, interest rates on Bank of Russia operations with credit institutions are set as key rate spreads. See the press release published on the Bank of Russia's website on 1 June 2018.*
[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 the transaction).*
[3] *Operations conducted at a floating interest rate linked to the Bank of Russia key rate.*
[4] *Operations have been suspended since April 2016.*
[5] *Either a repo or a deposit auction is held depending on the situation with liquidity. See press release http://www.cbr.ru/press/PR.aspx?file=19012015_154523 if2015-01-19T15_41_11.htm.*
[6] *Fine-tuning operations.*
[7] *Before 16 May 2018, also call operations. From 17 May 2018, the Bank of Russia only conducts overnight deposit operations with credit institutions.*
For reference: from 1 January 2016, the value of the Bank of Russia refinancing rate equals its key rate as of the respective date.
Source: Bank of Russia.

INTEREST RATES ON BANK OF RUSSIA SPECIALISED REFINANCING INSTRUMENTS[1] *Table 2*
(% P.A.)

Purpose of indirect bank lending	Maturity	Collateral	As of 01.01.18	From 12.02.18	From 26.03.18	From 17.09.18	From 17.12.18	From 17.06.19	General approach to rate-setting[2]
Large-scale investment projects[3]	Up to 3 years	Claims under bank loans for investment projects, whose performance is secured by the government guarantees of the Russian Federation	6.75	6.50	6.25	6.50	6.75	6.50	The lower of the two values: 9.00% p.a. or the key rate less 1.00 pp.
		Bonds placed to fund investment projects and included in the Bank of Russia Lombard List							
Non-commodity exports	Up to 3 years	Claims under loan agreements secured by the insurance contracts of JSC EXIAR	6.50	6.50	6.50	6.50	6.50	6.50	The lower of the two values: 6.50% p.a. or the key rate
Small- and medium-sized enterprises	Up to 3 years	Claims under loan agreements of JSC SME Bank[4]	6.50	6.50	6.50	6.50	6.50	6.50	
		Up to 3 years							
Leasing	Up to 3 years	Claims on loans to leasing companies	6.75	6.50	6.50	6.50	6.50	6.50	
Military mortgage	Up to 3 years	Mortgages issued under the Military Mortgage programme	7.75	7.50	7.25	7.50	7.75	7.50	Key rate

[1] Specialised refinancing facilities are Bank of Russia instruments aimed at encouraging bank lending to certain segments of the economy whose development is hampered by structural factors. Under these facilities, the Bank of Russia provides funds to credit institutions at lower rates and for longer maturities compared with standard Bank of Russia operations. Specialised refinancing facilities are temporary Bank of Russia instruments, which will be valid until conditions for their replacement with market instruments are created in the financial market. The provision of funds under the specialised facilities is restricted, because their application should not distort the stance of the monetary policy and prevent the achievement of its key objective of ensuring price stability.
[2] From 4 June 2018, the interest rates on Bank of Russia operations with credit institutions are set as spreads to the key rate. See the press release published on the Bank of Russia's website on 1 June 2018.
[3] Projects are selected in compliance with the rules established by Regulation of the Government of the Russian Federation No. 1016, dated 14 December 2010, 'On Approving the Rules to Select Investment Projects and Principals for the Provision of the Russian Federation State Guarantees on Loans or Bonded Loans Attracted to Carry out Investment Projects' or Regulation of the Government of the Russian Federation No. 1044, dated 11 October 2014, 'On Approving the Programme to Support Investment Projects Implemented in the Russian Federation Based on Project Financing'.
[4] Claims under loans issued to banks and microfinance organisations partnering with JSC SME Bank under the Programme for Financial Support of Small and Medium-sized Enterprises Development for lending to SMEs and claims under loans issued to leasing companies partnering with JSC SME Bank for leasing property to SMEs.
Source: Bank of Russia.

CLAIMS AND LIABILITIES ON BANK OF RUSSIA OPERATIONS TO PROVIDE AND ABSORB RUBLE LIQUIDITY
(BILLIONS OF RUBLES)

Table 3

Purpose	Type of instrument	Instrument	Term	Frequency	Bank of Russia claims and liabilities						
					As of 01.01.18	As of 01.04.18	As of 01.07.18	As of 01.10.18	As of 01.01.19	As of 01.04.19	As of 01.06.19
Liquidity provision	Standing facilities	Overnight loans	1 day	Daily	0.0	0.8	14.6	0.4	8.1	0.0	0.4
		Lombard loans			0.0	0.0	0.0	0.0	0.0	0.0	0.0
		FX swaps			0.0	0.0	0.0	0.0	4.1	32.8	37.8
		Repos			3.6	6.5	2.4	10.0	3.6	2.6	1.5
		Loans secured by non-marketable assets	From 1 to 549 days		5.5	30.1	5.4	377.8	5.1	8.1	6.1
	Open market operations	Auctions to provide loans secured by non-marketable assets	3 months	Monthly[1]	0.0	0.0	0.0	0.0	0.0	0.0	0.0
		Repo auctions	1 week	Weekly[2]	0.0	0.0	0.0	0.0	0.0	0.0	0.0
			From 1 to 6 days	Occasionally[3]							
		FX swap auctions	From 1 to 2 days		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liquidity absorption	Open market operations	Deposit auctions	From 1 to 6 days		2,124.9	2,520.6	2,389.1	1,761.8	1,478.2	1,680.0	1,120.0
			1 week	Weekly[2]							
		Auctions for the placement and additional placement of coupon OBRs[4]	Up to 3 months	Occasionally	357.4	1,139.1	1,123.0	1,502.1	1,391.3	1,515.3	1,616.5
	Standing facilities	Deposit operations	1 day[5]	Daily	246.8	264.6	329.1	499.0	423.8	136.4	160.9

[1] Operations have been suspended since April 2016.
[2] Either a repo or a deposit auction is held depending on the situation with liquidity.
[3] Fine-tuning operations.
[4] If the reporting date falls on a weekend or holiday, the indicated amount of outstanding coupon OBRs includes the accrued coupon interest as of the first working day following the reporting date.
[5] Before 16 May 2018, also call operations. From 17 May 2018, the Bank of Russia only conducts overnight deposit operations with credit institutions.
Source: Bank of Russia.

REQUIRED RESERVE RATIOS
(%)

Table 4

Liability type	Validity dates			
	01.12.17- 31.07.18	01.08.18-31.03.19	01.04.19-30.06.19	From 01.07.19[1]
For 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				
For 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's website on 31 May 2019.*
Source: Bank of Russia.

REQUIRED RESERVE AVERAGING RATIO

Table 5

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.

OUTSTANDING AMOUNTS ON BANK OF RUSSIA SPECIALISED REFINANCING FACILITIES[1]
(BILLIONS OF RUBLES)

Table 6

Purpose of indirect bank lending	Maturity	Collateral	Bank of Russia claims on credit institutions			Limit
			As of 01.01.19	As of 01.04.19	As of 01.06.19	As of 01.06.19
Non-commodity exports	Up to 3 years	Claims under loan agreements secured by the insurance contracts of JSC EXIAR	39.1	42.8	43.2	75.00
Large-scale investment projects[2]	Up to 3 years	Claims under bank loans for investment projects, whose performance is secured by the government guarantees of the Russian Federation	94.6	98.3	97.0	150.00
		Bonds placed to finance investment projects and included in the Bank of Russia Lombard List	0.0	0.0	0.0	
Small and medium-sized enterprises	Up to 3 years	Claims under loan agreements of JSC SME Bank[3]	7.9	6.6	5.8	175.00
		Guarantees of JSC Russian Small and Medium Business Corporation issued under the Programme for Encouraging Lending to Small and Medium-sized Enterprises	85.0	77.6	75.1	
Leasing	Up to 3 years	Claims on loans to leasing companies	0.2	0.2	0.2	10.00
Military mortgage	Up to 3 years	Mortgages issued under the Military Mortgage programme	8.3	8.3	8.3	30.00

[1] Specialised refinancing facilities are Bank of Russia instruments aimed at encouraging bank lending to certain segments of the economy whose development is hampered by structural factors. Under these facilities, the Bank of Russia provides funds to credit institutions at lower rates and for longer maturities compared with standard Bank of Russia operations. Specialised refinancing facilities are temporary Bank of Russia instruments, which will be valid until conditions for their replacement with market instruments are created in the financial market. The provision of funds under the specialised facilities is restricted, because their application should not distort the stance of the monetary policy and prevent the achievement of its key objective of ensuring price stability.

[2] Projects are selected in compliance with the rules established by Regulation of the Government of the Russian Federation No. 1016, dated 14 December 2010, 'On Approving the Rules to Select Investment Projects and Principals for the Provision of the Russian Federation State Guarantees on Loans or Bonded Loans Attracted to Carry out Investment Projects' or Regulation of the Government of the Russian Federation No. 1044, dated 11 October 2014, 'On Approving the Programme to Support Investment Projects Implemented in the Russian Federation Based on Project Financing'.

[3] Claims under loans issued to banks and microfinance organisations partnering with JSC SME Bank under the Programme for Financial Support of Small and Medium-sized Enterprises Development for lending to SMEs and claims under loans issued to leasing companies partnering with JSC SME Bank for leasing property to SMEs.

Source: Bank of Russia.

REQUIRED RESERVES AVERAGING SCHEDULE FOR 2019 AND INFORMATION ON CREDIT INSTITUTIONS' COMPLIANCE WITH RESERVE REQUIREMENTS

Table 7

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			
09.01.2019 – 05.02.2019	28	December 2018	22.01.2019 – 24.01.2019	2,329	2,258	586
06.02.2019 – 05.03.2019	28	January 2019	14.02.2019 – 18.02.2019	2,368	2,273	588
06.03.2019 – 09.04.2019	35	February 2019	15.03.2019 – 19.03.2019	2,346	2,279	587
10.04.2019 – 07.05.2019	28	March 2019	12.04.2019 – 16.04.2019	2,376	2,294	589
08.05.2019 – 04.06.2019	28	April 2019	21.05.2019 – 23.05.2019	2,389	2,324	593
05.06.2019 – 09.07.2019	35	May 2019	17.06.2019 – 19.06.2019	–	–	–
10.07.2019 – 06.08.2019	28	June 2019	12.07.2019 – 16.07.2019	–	–	–
07.08.2019 – 03.09.2019	28	July 2019	14.08.2019 – 16.08.2019	–	–	–
04.09.2019 – 08.10.2019	35	August 2019	13.09.2019 – 17.09.2019	–	–	–
09.10.2019 – 05.11.2019	28	September 2019	14.10.2019 – 16.10.2019	–	–	–
06.11.2019 – 03.12.2019	28	October 2019	15.11.2019 – 19.11.2019	–	–	–
04.12.2019 – 07.01.2020	35	November 2019	13.12.2019 – 17.12.2019	–	–	–

KEY ECONOMIC AND FINANCIAL INDICATORS *Table 8*

		05.18	06.18	07.18	08.18	09.18	10.18	11.18	12.18	01.19	02.19	03.19	04.19	05.19
Real sector														
Inflation	% YoY	2.4	2.3	2.5	3.1	3.4	3.5	3.8	4.3	5.0	5.2	5.3	5.2	5.1
GDP[1]	% YoY		2.2			2.2			2.7			0.5		
GDP in current prices[1]	trillions of rubles		24.8			27.1			29.5					
Output by key economic activities	% YoY	4.5	2.6	4.1	2.0	1.6	3.8	1.8	2.1	0.2	2.2	0.2	2.7	
Industrial production	% YoY	3.7	2.2	3.9	2.7	2.1	3.7	2.4	2.0	1.1	4.1	1.2	4.6	
Agricultural production	% YoY	2.2	0.8	1.7	-10.6	-4.7	12.1	-5.9	0.1	0.7	1.0	1.5	1.4	
Construction	% YoY	7.9	3.2	7.6	3.3	5.9	5.7	4.3	2.6	0.1	0.3	0.2	0.0	
Fixed capital investment[1]	% YoY		4.6			6.4			2.9			0.5		
Freight turnover	% YoY	2.8	2.4	4.2	2.6	2.0	1.5	2.2	3.2	2.4	1.9	2.6	2.3	
PMI Composite Index	% SA	53.4	52.0	51.7	52.1	53.5	55.8	55.0	53.9	53.6	54.1	54.6	53.0	51.5
Retail trade turnover	% YoY	2.9	3.4	2.8	3.0	2.3	2.2	3.3	2.7	1.9	2.0	1.6	1.2	
Real disposable money income[1]	% YoY		1.1			0.2			-1.9			-2.3		
Real wage	% YoY	7.6	7.2	7.5	6.8	4.9	5.2	4.2	2.9	1.1	0.0	2.3	1.6	
Nominal wage	% YoY	10.2	9.7	10.2	10.1	8.4	8.9	8.2	7.3	6.1	5.2	7.7	6.9	
Unemployment rate	% SA	4.8	4.8	4.9	4.8	4.7	4.8	4.8	4.8	4.7	4.6	4.5	4.6	
Banking sector														
Money supply (M2X)	% YoY, AFCR	7.7	8.3	8.1	8.2	8.2	7.9	7.9	7.9	6.5	7.9	7.0	6.6	
Money supply (M2)	% YoY	10.3	11.4	11.8	12.6	11.8	11.5	11.9	11.0	9.9	9.9	8.9	7.7	
Household deposits	% YoY, AFCR	7.7	7.1	7.7	7.0	6.0	6.5	5.7	5.4	5.4	5.7	5.6	6.8	
in rubles	% YoY	12.3	11.5	11.8	11.2	9.9	10.4	8.9	8.3	7.8	7.5	6.6	7.0	
in foreign currency	% YoY	-7.9	-7.9	-6.2	-7.2	-7.3	-7.0	-5.6	-5.2	-3.6	-1.2	1.6	5.8	
dollarisation	%	20.5	20.3	20.5	21.7	21.1	20.9	21.3	21.5	21.5	21.5	21.5	21.1	
Loans to non-financial organisations	% YoY, AFCR	2.6	2.8	3.3	4.3	5.7	6.0	5.6	4.7	4.8	5.6	5.7	5.4	
short-term (less than 1 year)	% YoY, AFCR	-5.6	-9.3	-7.1	-0.5	-1.3	2.2	3.7	3.8	-0.6	-2.0	2.7	-1.0	
long-term (more than 1 year)	% YoY, AFCR	4.3	5.4	5.3	4.9	7.2	6.9	6.0	5.4	4.9	6.1	5.2	5.8	
overdue loans	%	6.8	6.7	6.8	6.7	6.6	6.7	6.6	6.3	7.8	7.9	7.9	7.8	
Loans to households	% YoY, AFCR	18.0	18.8	19.6	20.5	21.4	22.0	22.6	22.2	23.0	23.4	23.5	23.8	
housing mortgage loans	% YoY, AFCR	22.3	23.2	23.9	24.5	24.8	25.3	25.5	23.4	24.7	24.8	24.2	23.5	
unsecured consumer loans	% YoY	15.6	17.0	18.1	19.3	20.5	21.4	22.5	22.7	23.4	23.7	24.2	25.2	
overdue loans	%	6.3	6.1	6.0	5.9	5.8	5.6	5.5	5.1	5.4	5.3	5.1	5.1	

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 9*

		2018 Q1	2018 Q2	2018 Q3	2018 Q4	2019 Q1[1]
Balance of payments[2]						
Urals crude oil price	% YoY	24.8	50.1	44.6	9.3	-3.2
USD/RUB exchange rate ('+' – ruble's strengthening, '-' – ruble's weakening)	% YoY	3.4	-7.5	-9.9	-12.1	-14.0
Goods and services exports	% YoY	22.0	27.2	28.1	17.7	-0.6
Goods and services imports	% YoY	18.8	8.3	-0.1	-2.9	-2.2
Current account	**billions of US dollars**	**30.0**	**17.9**	**27.5**	**38.4**	**32.8**
Balance of trade	billions of US dollars	44.2	45.4	47.8	57.1	45.3
Exports	billions of US dollars	101.7	108.7	110.5	122.2	101.2
Imports	billions of US dollars	57.4	63.4	62.7	65.1	55.9
Balance of services	billions of US dollars	-6.5	-7.6	-8.8	-7.0	-6.6
Exports	billions of US dollars	14.0	16.7	17.4	16.6	13.8
Imports	billions of US dollars	20.5	24.4	26.2	23.6	20.4
Balance of primary and secondary income	billions of US dollars	-7.7	-19.8	-11.5	-11.7	-5.9
Current and capital account balance	billions of US dollars	29.8	17.7	27.5	37.7	32.9
Financial account excluding reserve assets (net lending (+) / net borrowing (-))	**billions of US dollars**	**12.4**	**9.3**	**24.2**	**31.1**	**15.0**
Public sector	billions of US dollars	-6.5	11.1	2.9	1.5	-10.8
Private sector	billions of US dollars	18.9	-1.8	21.3	29.7	25.9
Net errors and omissions	billions of US dollars	1.9	2.9	1.7	-4.0	0.7
Change in reserve assets ('+' – increase, '-' – decrease)	**billions of US dollars**	**19.3**	**11.3**	**5.0**	**2.6**	**18.6**

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

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.

BANK OF RUSSIA KEY RATE

A main 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. It corresponds to the minimum interest rate at Bank of Russia one-week repo rate auctions and the maximum interest rate at Bank of Russia one-week deposit auctions.

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.

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, and is 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 which allows a CDS buyer to insure against a certain credit event (e.g., default) under financial obligations of a third party in exchange for regular payment of a premium (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 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.

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').

MONETARY BASE

The 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 amount of funds of Russian Federation residents (excluding general government and credit institutions). 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 on-demand accounts (including bank card accounts), time deposits and other types of deposits in the banking system, denominated in the currency of the Russian Federation, and 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.

OPERATIONS TO ABSORB LIQUIDITY

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

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)

Reference weighted rate of overnight ruble 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 OF THE BANKING SECTOR

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 the 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 in the key rate are translated into the economy through different channels (interest rate, credit, foreign exchange, balance sheet, inflation expectations and other channels).

LIST OF ABBREVIATIONS

- 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
- 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

- MPD – Monetary Policy Department of the Bank of Russia
- MPR 4/18 – Monetary Policy Report published on 14 December 2018
- MTVECM, TVECM – Momentum Threshold Vector Error Correction Model, Threshold Vector Error Correction Model
- NPF – non-governmental pension fund
- NPISH – non-profit institutions serving households
- 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
- 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 bond market, calculated by Cbonds)
- 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