Bank of Russia

TALKING TRENDS
Economy and markets

Research and Forecasting Department Bulletin

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The views and recommendations expressed in the bulletin do not necessarily reflect the official position of the Bank of Russia.
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Executive summary

Monthly summary

- Current growth of prices was persistently high between July and August, including in the underlying components of inflation. A further rise was seen in household and business inflation expectations. At the same time, there were tentative signs of an emerging disinflationary trend, with demand posting a more moderate pace. This came on the back of a slowdown in retail lending and less dynamism in household consumption. This is expected to encourage a switch to more moderate production plans and, combined with gradually increasing productivity, help soften a tight labour market.
    - In July, the seasonally adjusted growth of consumer prices – even excluding utility rates – was highest since the start of the year. It was driven by fruit and vegetable and petrol prices. However, considerably less growth was seen in the underlying components of inflation. While seasonally adjusted price growth declined in August, it is premature to speak of a steady reduction in inflationary pressures. To return inflation to 4% in 2025, tighter monetary conditions are needed than in 2024 H1. Whether this will require an additional increase in the key rate will depend on incoming data.
    - The July–August data and surveys mostly signal slower growth in economic activity, including in household consumption. Retail lending progressed at a slower pace, excluding car loans. Overall, this enables a gradual reduction in overheating in the economy and a transition to more moderate but sustainable growth, providing that price stability is achieved.
    - Between late July and August, developments in domestic financial markets were driven by a hostile geopolitical environment as well as an investor rethink on the timeframe of tight monetary policy. The foreign currency market grew more fragmented, with further complications in yuan-ruble pricing. Negative trends prevailed in the equity and fixed–income bond markets, while variable yield bonds and money market funds retained investor appeal.

1. Inflation

The inflationary background remained tough in July–August, despite some seasonally adjusted easing of price rises in August. Business and household inflation expectations, which so far continue to climb, remain an important proinflationary factor.

At the same time, annual inflation seems to have reached its peak in July. An increasing number of signs suggest that demand growth is softening in Q3. Should this trend continue, inflationary pressure will again subside.

There is, however, reason to believe that this process will be slow, given the prevalence of both demand- and supply-side proinflationary factors, highly inertial to boot (inflation expectations).

In an environment of high inflation expectations, an increase in propensity to save is only possible under significantly positive interest rates, surpassing the level of economic agents' inflation expectations, in particular, those of households. The elevated savings ratio allows households to boost income from investments (interest rates on deposits, bond coupons, dividends, and capital gains). Part of such income just offsets inflation, keeping up the value of savings in real terms. The portion of investment income exceeding inflation, in effect, transfers consumption from the present to the future. This helps restrain consumer activity today by building up financial resources for stepping up consumption tomorrow in the event of income growth slowdown.

We note that household bank holdings (in current accounts and time deposits) are part of broad money supply (M2 and M2X). At the same time, they are not the source of money supply growth, being a derivative quantity of credit and budget deficit. If these funds were used for consumption, then, as a first approximation, money supply would remain the same. These funds would simply be redistributed within the banking system to firms and other households' accounts. The creation thereby of extra demand in the economy and acceleration of money circulation velocity would generate an additional inflationary impulse. It therefore now remains important to keep up and enhance households' savings incentives.

Under these circumstances, for the disinflationary trend to form and annual inflation to return to 4% in 2025, tight monetary stance should be maintained for a long time.

1.1. Price growth remain fast even adjusted for one-off factors

- July saw price growth accelerate in all enlarged categories. The key contribution came from an increased indexation of communal services prices. But even exclusive of this indexation, price increases price notably accelerated. Persistent inflationary pressure remains elevated.
- Household inflation expectations rose further. Increased demand amid strong consumer activity and lending enables firms to pass rising costs through to prices.

- Medium-term proinflationary risks remain high. For sustainable disinflationary trends to form and inflation to return to target, tight monetary stance needs to be maintained for a long time.

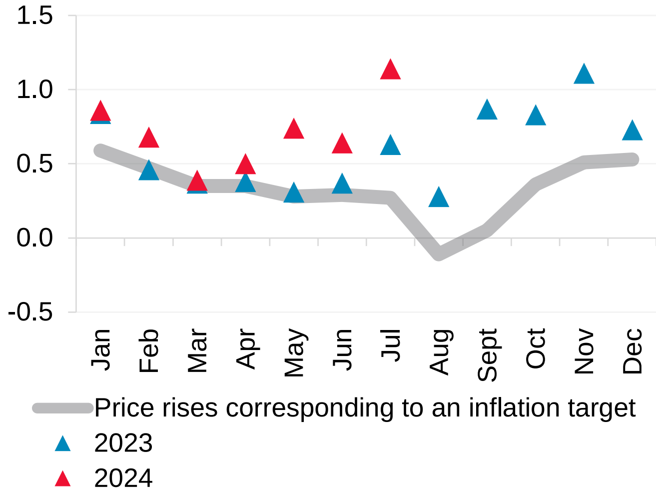
Consumer price growth accelerated to 16.1% MoM SAAR[1] in July from 9.3% MoM SAAR in June. Annual inflation went up to 9.1%, likely reaching a peak, from which it will be gradually descending (Table 1). Price growth acceleration this fast came on the back of communal services price indexation by almost 10%. Net of communal services, the pace of price rises in July still accelerated, but less sharply at 12.1% MoM SAAR compared with 9.7% MoM SAAR a month earlier. A notable input to the elevated price growth pace continued to be provided by volatile components, such as fruit and vegetables, while price increases in stable components also remained far above 4% in annualised terms.

Table 1. Inflation and its components

	Jul.	Jul.	May	Jun.	Jul.
	2022	2023	2024		
% YoY					
All goods and services	**15.1**	**4.3**	**8.3**	**8.6**	**9.1**
Core inflation	**18.4**	**3.2**	**8.6**	**8.7**	**8.6**
Food	16.8	2.2	9.1	9.8	9.7
Non-food goods	16.5	2.4	7.1	7.0	6.7
Services	10.8	10.0	8.6	8.8	11.4
% MoM SAAR					
All goods and services	**-3.2**	**12.5**	**10.7**	**9.3**	**16.1**
Core inflation	**-0.9**	**7.7**	**11.6**	**6.9**	**6.0**
Food	-9.2	16.7	8.4	12.4	14.6
– net of fruit and vegetables	**-0.2**	**5.4**	**10.2**	**7.8**	**7.0**
Non-food goods	-4.3	12.5	6.3	4.7	8.2
– net of refined petroleum products	**-4.7**	**10.1**	**6.3**	**3.2**	**4.4**
Services	8.4	7.3	19.7	10.7	28.4
– net of housing and communal services	**8.9**	**7.9**	**27.8**	**12.5**	**9.8**

Sources: Rosstat, R&F Department estimates.

Figure 1. Price rises corresponding to an inflation rate of 4%, % MoM



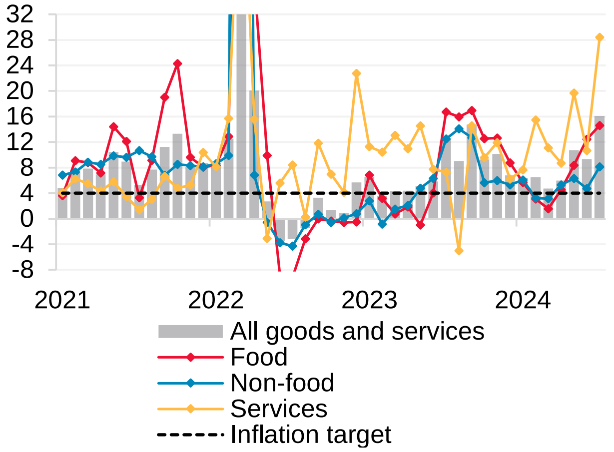
Sources: Rosstat, R&F Department estimates.

Food price growth accelerated to 14.6% MoM SAAR in July from 12.4% MoM SAAR in June, with the main contribution continuing to come from fruit and vegetables, whose price decline was substantially lagging the usual seasonal pattern. Agricultural producers note that [field vegetables are being harvested under a normal schedule](), while strong demand allows rising costs to be put through to prices.

In other food products, the rate of price growth somewhat slowed but remained elevated at 7.0% MoM SAAR after 7.8% MoM SAAR a month earlier. Meat product price rises continued to lose momentum. That said, the fast pace of price increases is still seen in a number of items with a significant weight in the consumer basket: dairy products, oils, bakery and confectionary products. Producers [expect the upward price movements to continue in August–September]() as costs (raw materials, packaging, logistics) climb.

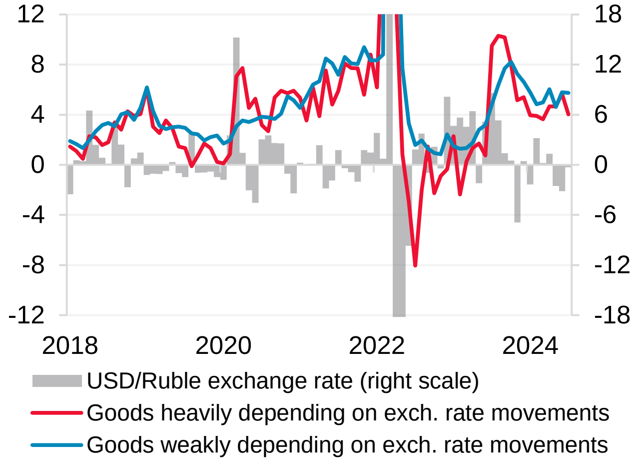
[1] The seasonal adjustment of communal services is traditionally made in the following way: 4% is distributed throughout a year as a seasonal component and the rest is attributed to price growth in a corresponding month.

Figure 2. Seasonally adjusted price growth, % MoM SAAR



Sources: Rosstat, R&F Department estimates.

Figure 3. Median CPI (% MoM SAAR) and US dollar to ruble exchange rate (%)



Sources: Bank of Russia, Rosstat, R&F Department estimates.

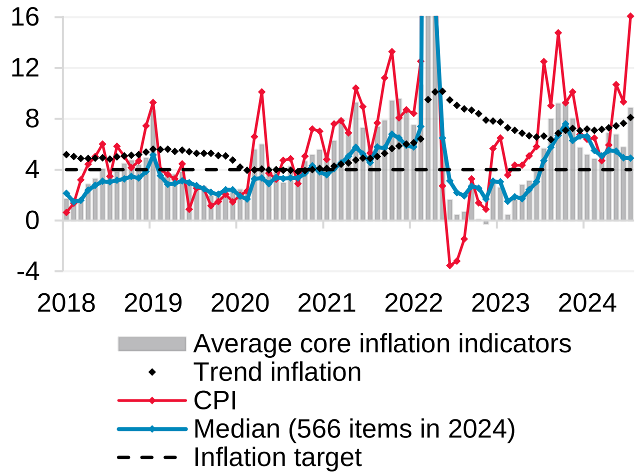
The non-food segment saw price growth accelerate to 8.2% MoM SAAR in July from 4.7% MoM SAAR in June, driven chiefly by fuel price increases. Retail fuel prices are rising at an elevated rate, following in the footsteps of wholesale prices as the world prices go up. Further domestic price rises will be contained by the reimposition of the petrol export ban effective from 1 August to the end of the year. The Russian government is also preparing additional measures to stabilise the market, in particular, maintaining the priority of refined petroleum products in rail shipments.

In the services sector, price growth temporarily accelerated to 28.4% MoM SAAR, owing mainly to housing and communal services[2] price indexation (housing services – by 3.0%, communal services – by 9.9%). Net of housing and communal services, the rate of price rises in services slowed to 9.8% MoM SAAR from 12.5% MoM SAAR in June but remained high. There was a slowdown in domestic tourism price increases. Transport services prices, meanwhile, continued to climb at a fast pace.

Services price rises are highly likely to slow dramatically in August. This is owed to changes in recent years in the categories included in the Rosstat consumer basket, as well as in household preferences. Seasonality in these components' prices is not captured by statistical methods so far and introduces additional volatility to price movements. May saw the opposite picture, where changes in people's preferences towards domestic tourist destinations increased the estimates of seasonally adjusted price growth.

[2] The effect of communal services price indexation will depart in August, allowing services price growth to slow dramatically.

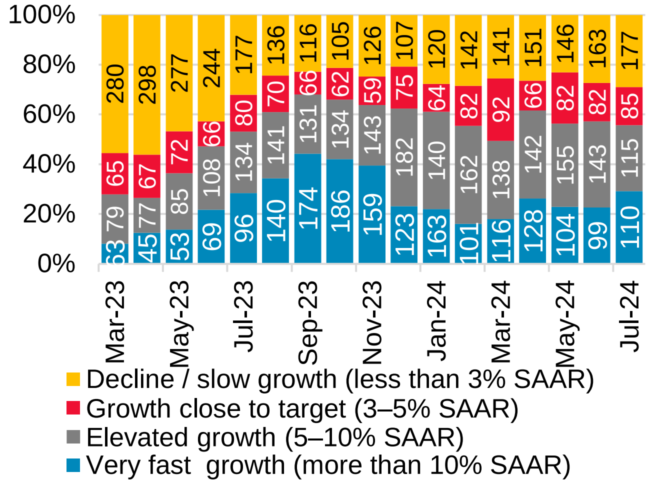
Figure 4. Modified core inflation indicators* (% in annualised terms) and trend inflation estimate (%YoY)



** Indicators are computed using the method of excluding the most volatile components and the truncation method.*

Sources: Rosstat, R&F Department estimates.

Figure 5. Aggregate weight of goods and services* distributed based on seasonally adjusted price growth



**Net of fruit and vegetables and regulated services.*

Note. The figures represent the number of items.

Sources: Rosstat, R&F Department estimates.

The impact of the exchange rate on price rises remains neutral. The median of price growth in goods and services highly sensitive to the ruble exchange rate has somewhat declined amid ruble strengthening in recent months (Figure 3). Meanwhile, the overall pass-through effect of the ongoing ruble appreciation episode will be insignificant due to the rising logistics and payment costs of imports.

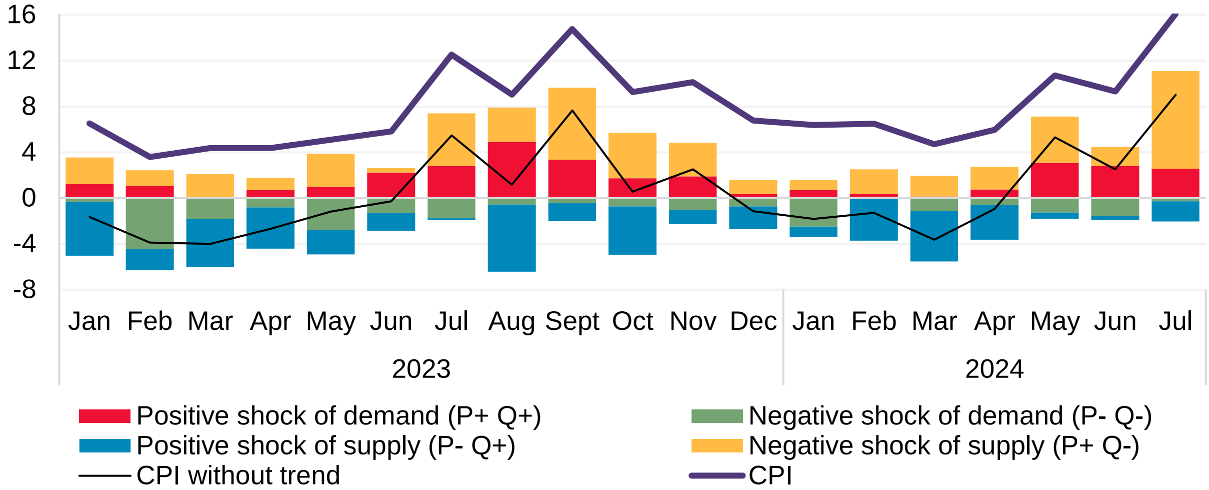
The persistent inflationary pressure is still notably above 4%. July saw mixed moves in the estimates of modified core inflation indicators: the estimate obtained by the truncation method slightly declined, while the indicator excluding volatile components rose sharply[3] (Figure 4). The median of price growth distribution remained on the previous month's level together with the total weight of components rising in price at an accelerated pace (Figure 5). The trend inflation estimate continued to increase, climbing to 8.11% from 7.65% in June.

The price growth decomposition (Figure 6) bears out the high level of persistent inflationary pressure: the contribution of demand-side factors to price increases remains substantial. Indeed, the input of the positive effect of the demand-side shock inherent in heated demand (a simultaneous increase in the volume of demand and prices) remains on a relatively high level. That said, a considerable price growth acceleration in July was largely driven by supply-side factors, which are transient in nature. In particular, the greater part of the negative supply-side shock was owed to the communal services price indexation.[4]

[3] Communal services are formally not included in the list of the most volatile components.

[4] The nominal volume of communal services provided in July was smaller than the size of the price indexation.

Figure 6. Price growth decomposition, % MoM SAAR

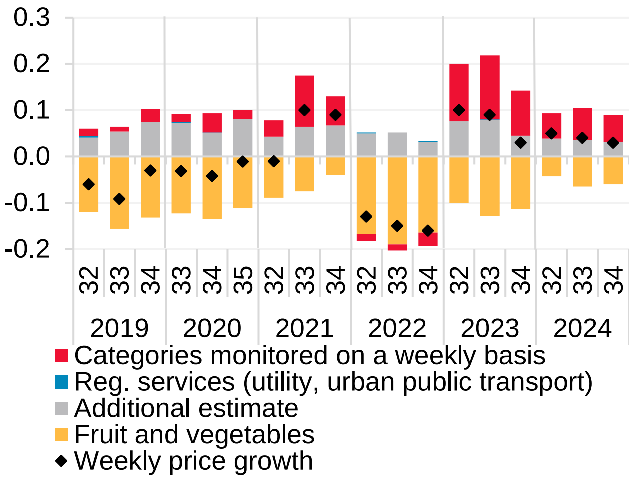


** The diagram uses Rosstat data on CPI and retail sales (in physical terms) for 45 categories of goods and services with a total weight of more than 80% of the consumer basket. The idea of the method is based on the baseline model of aggregate demand and supply: if changes in price (P) and volume of consumption (Q) are oppositely directed, then the cause of these changes is deemed to be a shift of the supply curve, if changes are codirectional, then the cause is assumed to be the shift of the demand curve.*

Sources: Rosstat, Sapova, Kharlamova (2023), R&F Department estimates.

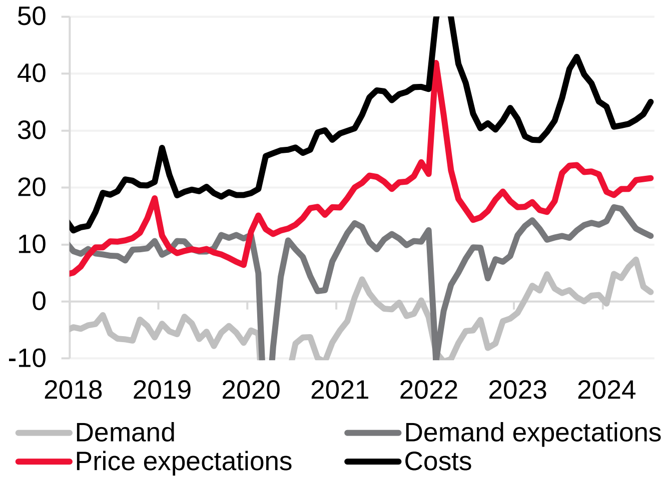
According to preliminary estimates, persistent inflationary pressure remained elevated in August, with weekly price growth rates high by historical standards (Figure 7). Consumer activity stayed on a high level, household inflation expectations continued to rise. Under these circumstances, businesses are able to pass the rising costs through to prices: manufacturing producer price growth accelerated in July[5], companies' inflation expectations continued to climb in August (Figure 8). Proinflationary risks remain high, for sustainable disinflationary trends to form, a tight monetary stance needs to be maintained for a long time.

Figure 7. Weekly price growth decomposition, pp.



Sources: Rosstat, R&F Department estimates.

Figure 8. Business monitoring data for the economy at large, pp, SA



Source: Bank of Russia.

[5] Net of metallurgy and oil refining it remained close to the high level of June (0.6% MoM).

2. Economic performance

Incoming statistics for July, as well as a wide range of real-time indicators and survey data suggest a more moderate economic activity expansion at the start of Q3 compared with Q2.

It is important to note that this moderate performance is at least partially owed to a lesser rise in demand than companies expected. As a result, industry saw signs of some increase in the stocks of finished products. Although investment and hiring plans remain ambitious by historical standards, there has emerged a trend towards their contraction.

Retail lending has shown signs of a slowdown since July, largely owed to the cancellation or reformatting of subsidised mortgage lending programmes. The lending growth slowdown was also helped by the tightening of macroprudential regulation for unsecured consumer lending. There emerged signs of a growth slowdown in the consumption of goods and services by households in July–August. At the same time, corporate lending continues to expand at a fast pace.

Overall, one can conclude that there emerge indications of the starting movement towards balanced growth rates accompanied by inflation deceleration. Accordingly, this has lowered the risks of stagflation, where an economy hits a limit of its production capabilities amid strong demand leading to inflation.

2.1. Economic activity cools in early Q3

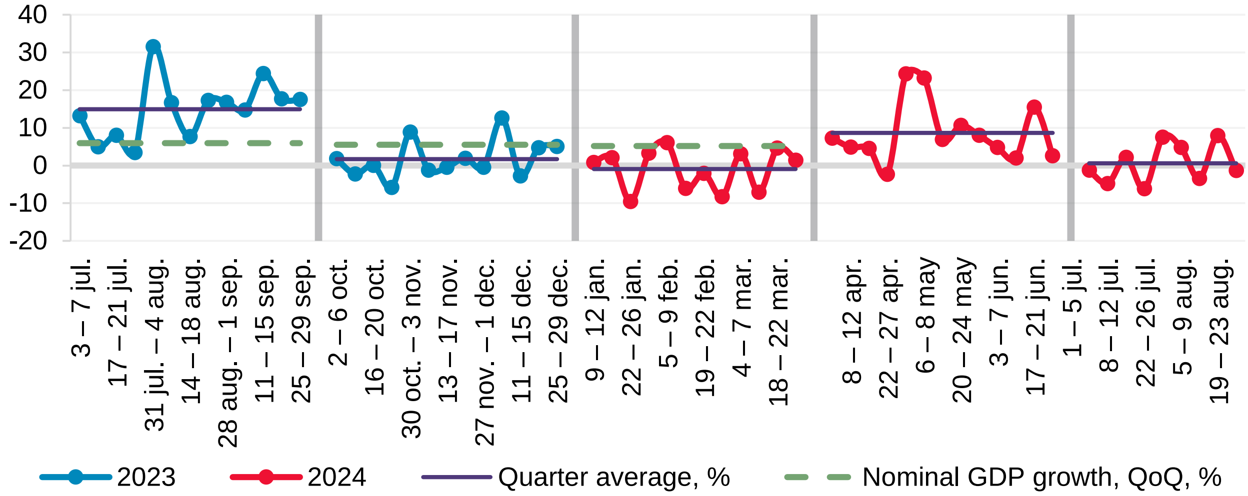
- Based on the preliminary estimate of GDP growth released by Rosstat, the economy's expansion may have slowed dramatically in Q2, dragged down by both external demand weakening and mounting supply-side constraints.[6] That said, growth in core industries' output[7] in Q2 continued at a pace similar to that in Q1 (Figure 10), i.e., the slowdown may have occurred in industries outside of this group.
- Business activity expansion slowed at the start of Q3, as indicated by changes in financial flows (Figure 9) along with business surveys (Figure 11). August's Manufacturing PMI showed the lowest reading since July 2023 (52.1). The Bank of Russia Business Climate Index declined to 7.0 from an H1 average of 9.4 (6.8 in 2023). A survey of industrial enterprises by the Institute for Economic Forecasting of Russia's Academy of Sciences showed a drop in the balance of demand perceptions to a 20-month low and a rise in the balance of estimates of changes in the stocks of finished products.
- An industrial output growth slowdown in Q2 was chiefly driven by oil extraction cuts as part of commitments under the OPEC+ agreement. The contraction continued into Q3. June saw a moderate output contraction in manufacturing for the first time since the start of the year (Figure 12). Negative trends were only registered in a number of the most volatile industries of the investment goods group and in the sector of goods meeting

[6] Primarily concerned with the labour market and bad weather conditions reducing agricultural output, as well as downtime at some refineries.
[7] Index of core economic activities.

intermediate demand. These were driven mainly by temporary factors (repairs at refineries and metal manufacturing facilities, specifics of the production cycle in the heaviest industries[8]). Manufacturing output contraction continued in July, affecting also a considerable part of industries producing consumer goods and services (Figure 13).

- Real wage growth continued in Q2,[9] and, given the still intact positive financial sentiment and rising inflation expectations, additional income was used primarily for expanding consumption (Figure 14). That said, real-time indicators suggest that August saw a growth slowdown in consumer demand, which was, meanwhile, still strong. (Figure 18, Figure 19).
- The disinflationary effect of cooling in demand growth will materialise gradually, because the capabilities of output expansion are still encountering significant constraints on the part of the labour market. The unemployment level was at an all-time low for the second consecutive month (Figure 16), and so was the difference between labour demand and supply (Figure 17), despite further growth in household economic activity (Figure 15). Given the limited demographic and migration potential for labour supply expansion, the departure from the well-established consumer behaviour model may materialise slowly. This exacerbates the risks of inflation deviation from target in 2025, calling for maintaining a tight monetary stance for a long time to come.

Figure 9. Incoming payments growth[10] relative to the previous quarter average weighted by industries' shares in gross value added, seasonally adjusted, %



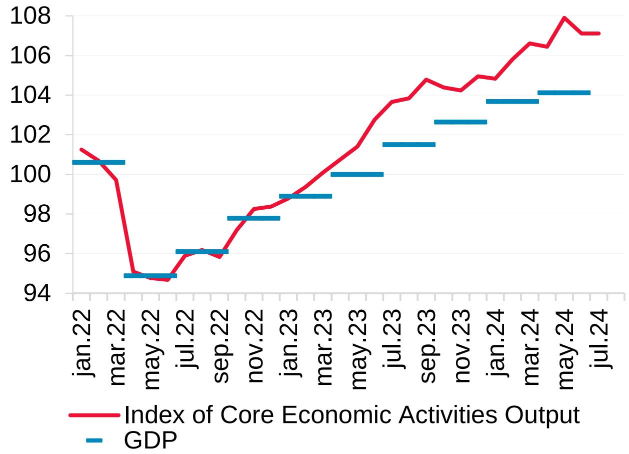
Sources: Bank of Russia, Monitoring of individual industries' financial flows.

[8] Two industries (manufacture of fabricated metal products, excluding machinery and equipment, and manufacture of other transport equipment), which have the heaviest weight in the structure of gross value added of the investment goods group (around 40% in total) and may show a significant output decline as the cycle of fulfilling major orders is completed.

[9] Adjusted for a temporary surge in March due to the payment of bonuses in some industries.

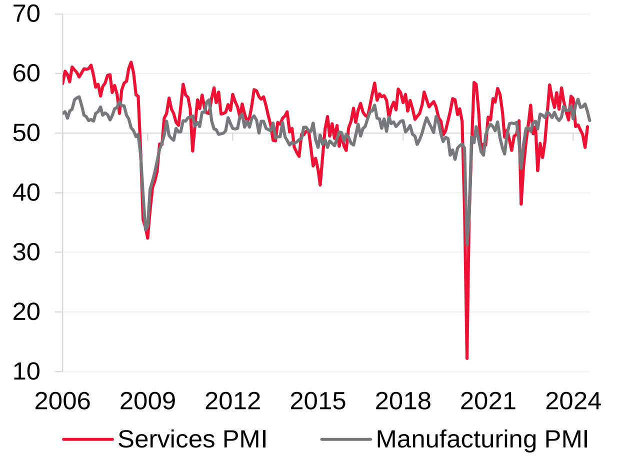
[10] Growth means a percentage change in the value: $g = \frac{(x_1 - x_0)}{x_0} * 100$.

Figure 10. Core economic activities output and GDP, Q4 2021 = 100, SA



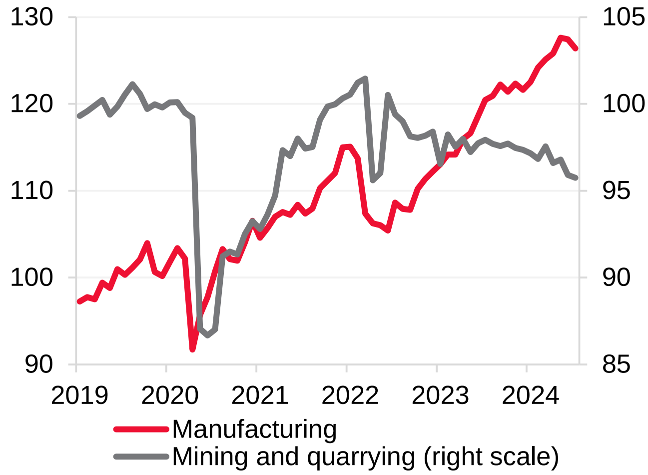
Sources: Rosstat, R&F Department estimates.

Figure 11. Russia's Manufacturing and Services PMI, points



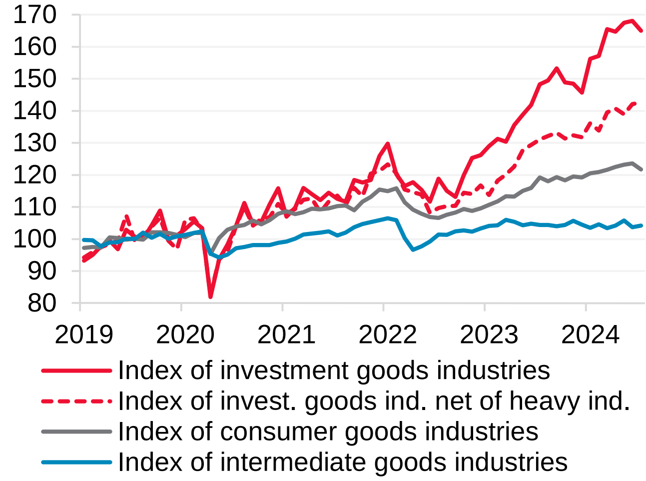
Source: S&P Global.

Figure 12. Mining and quarrying and manufacturing indices (2019 = 100), SA



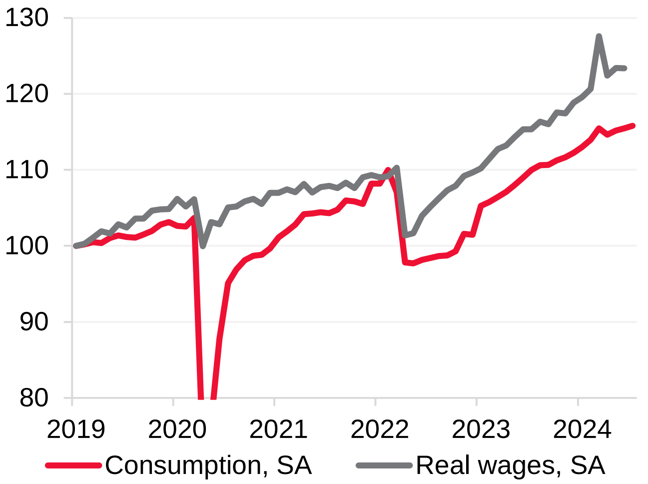
Sources: Rosstat, R&F Department estimates.

Figure 13. Output in groups of manufacturing industries, SA, 2019 = 100%



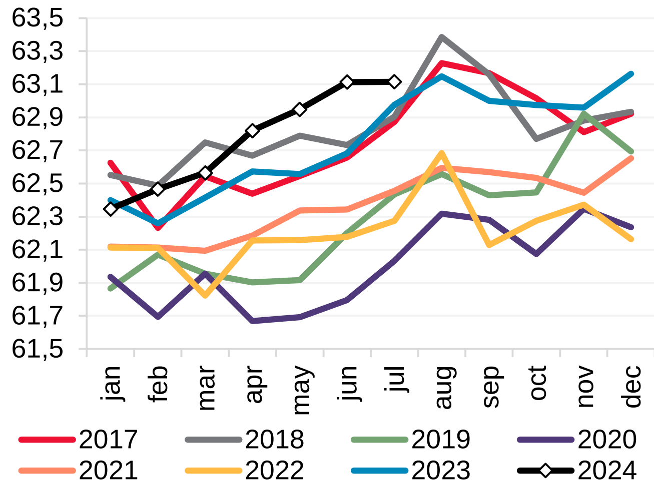
Sources: Rosstat, R&F Department estimates.

Figure 14. Proxy indicator for consumption (sum of retail, services and public food services sales) and real wages, 01.2019=100, SA, %



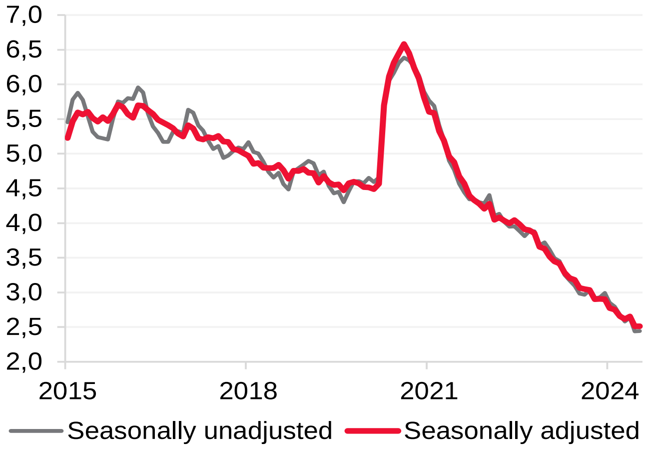
Sources: Rosstat, R&F Department estimates.

Figure 15. Labor force participation rate, %



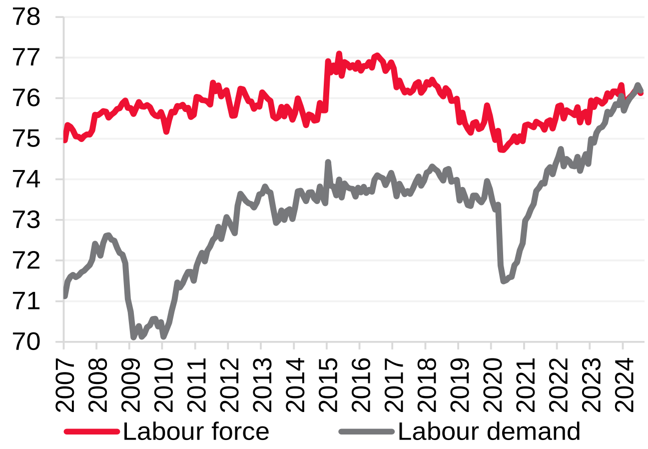
Sources: Rosstat, R&F Department estimates.

Figure 16. Unemployment rate, %



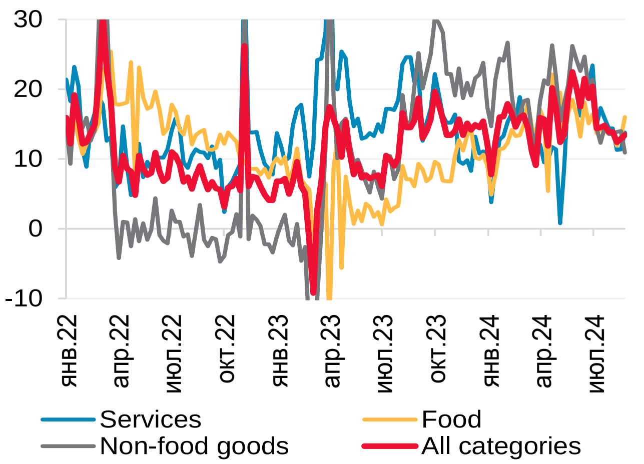
Sources: Rosstat, R&F Department estimates.

Figure 17. Labour force and labour demand, mln people, SA



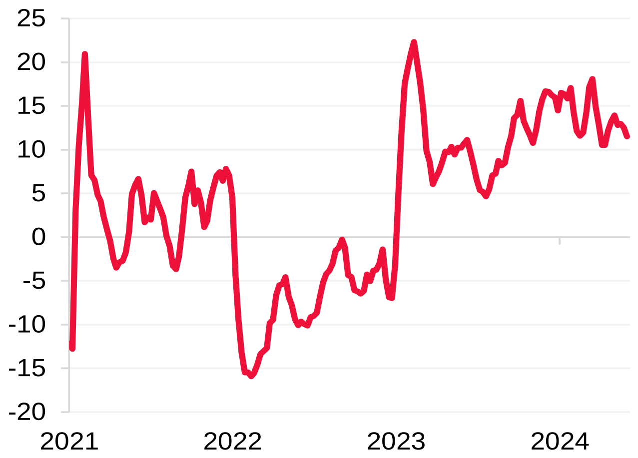
Sources: Rosstat, R&F Department estimates.

Figure 18. Nominal consumer expenditure growth by category, % YoY



Source: SberIndex.

Figure 19. Real daily consumer expenditure growth (4-weeks average), % YoY



Sources: Romir, R&F Department estimates.

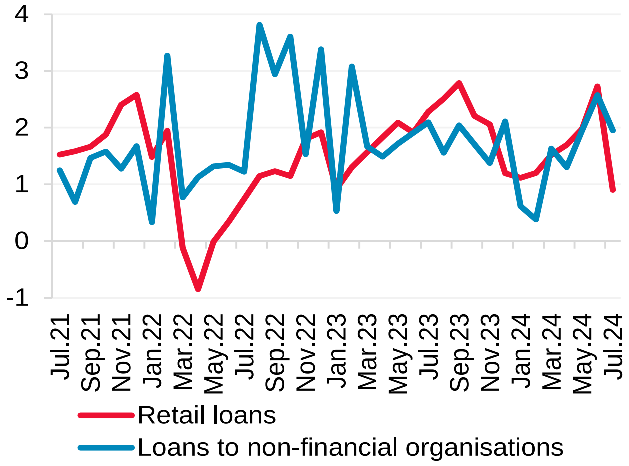
2.2. Retail lending growth slows

- Lending growth slowed at the start of Q3. In addition to an expected deceleration in the mortgage lending segment after the choice and conditions of subsidised programmes had been changed, expansion in unsecured consumer loans and loans to nonfinancial organisations stalled. Lending growth continues to provide a significant input to demand expansion, but its scale is gradually diminishing. The credit impulse (Figure 22) slid from its peaks of late 2023. Monetary stance tightening will provide for further cooling in lending and stabilisation of its growth rate on sustainable levels.
- Retail lending growth slowed to 0.9% MoM SA in July from 2.7% MoM SA (Figure 20). The growth slowdown was expectedly driven by, above all, the termination of the umbrella Subsidised Mortgage Lending programme and tightening the terms and conditions of other mortgage lending programmes. On top of that, a restraining impact on demand in

the unsubsidised segment may have arisen from hikes in market interest rates on mortgage loans. The number of mortgage loan transactions shrank to 54%, which is comparable with the seasonally low level of the start of the year, while mortgage loan growth slowed to 0.8 MoM SA in July after a 2.3% MoM SA spike in June (Figure 23). Figure 24). But July's mortgage loan slowdown is so far not indicative enough, because part of loans were provided under agreements signed prior to 1 July, while terms and conditions of the programmes were changed in the middle of the month. It will be reasonable to estimate the full effect of changes to the programmes for the full month of September and subsequent months.

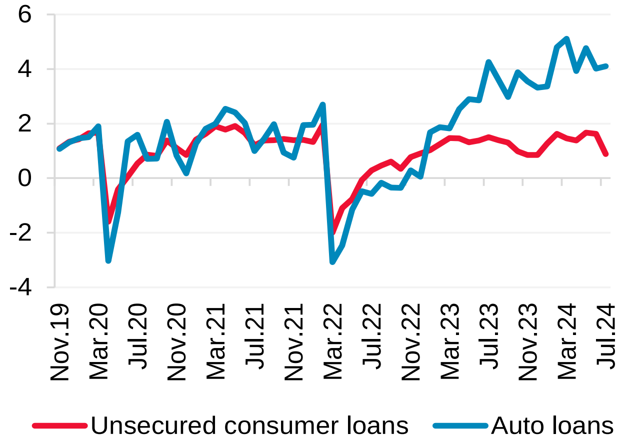
- Growth in unsecured consumer lending slowed to 0.9% % MoM SA in July from 1.6% MoM SA a month earlier (Figure 21), the slowest month-on-month rise from mid-2002. This change in the pace of growth may be owed to gradual tightening of non-price conditions of loan provision following the adoption of macroprudential measures. July saw the number of new credit cards decline and the limits for new cards contract.
- The pace of auto loan portfolio expansion stayed on the high level of June at 4.1% MoM SA after 4.0% MoM SA. Growth in the number of loans extended was posted in the new and used car segments alike. Demand for new cars and loans may have been strongly supported by price hikes pre-announced by a major Russian car maker. Growth in demand for auto loans may stay robust in August–September due to expectations for a disposal charge rise as of October. That said, auto loan provision may be restrained by add-ons to risk weights imposed for borrowers with a debt-to-income ratio of more than 50%.
- Growth in loans to non-financial organisations slowed to 2.0% MoM SA in July from 2.6% MoM SA in June. This growth rate is still high, hardly compatible with an inflation slowdown to 4%. The tight monetary stance will help gradual deceleration of corporate portfolio expansion.
- The pace of growth in household funds at banks was unchanged at 1.6% MoM SA in July. (Figure 25). This growth rate was buttressed by a rise in interest rates on deposit products amid continuing fast pace of disposable income expansion. At the same time, the pace of deposit growth came in below its rate in late 2023 – early 2024, which agrees with the estimates of a household savings ratio decline at the end of Q2 – start of Q3.

Figure 20. Ruble loans portfolio growth, % MoM SA



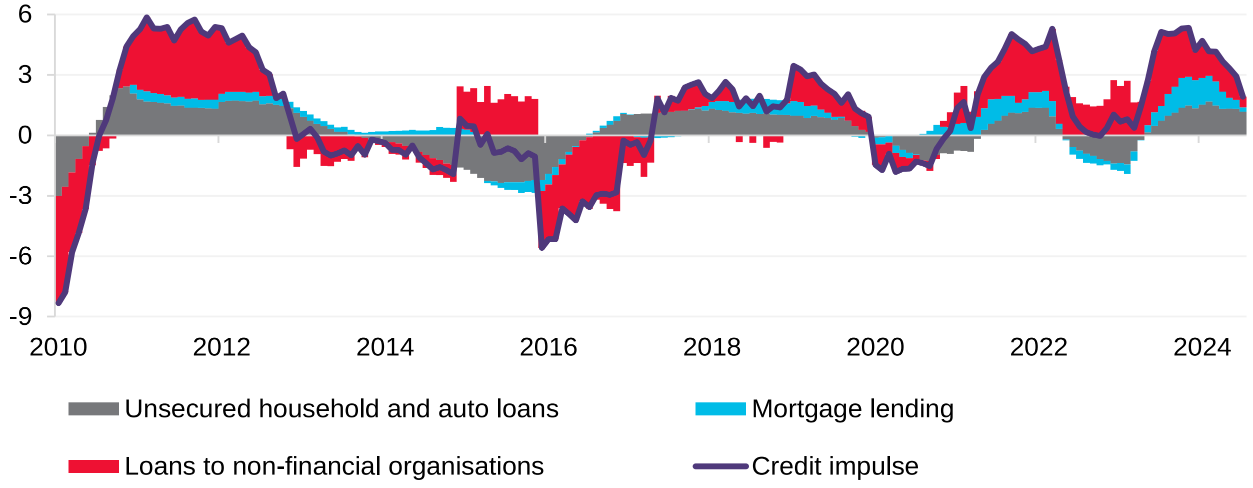
Sources: Bank of Russia, R&F Department estimates.

Figure 21. Retail loans portfolio growth, % MoM SA



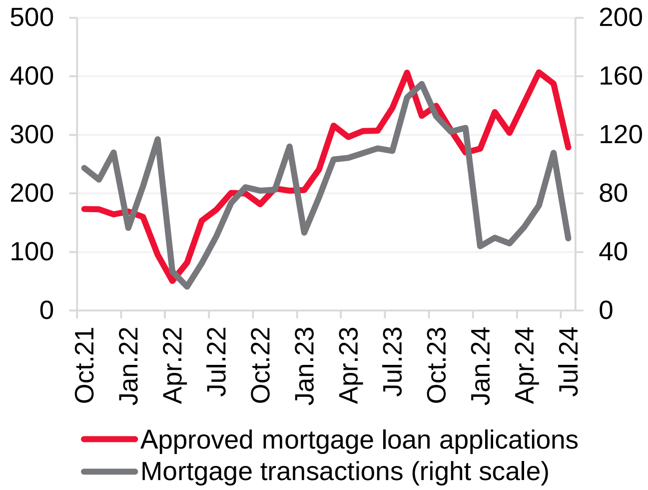
Sources: Bank of Russia, R&F Department estimates.

Figure 22. Credit impulse, % of GDP



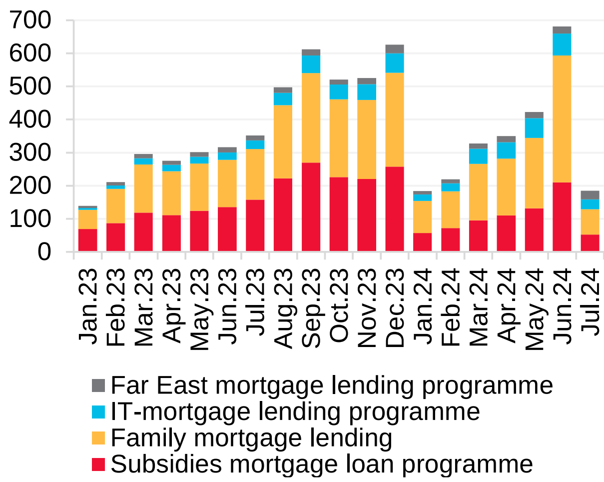
Sources: Bank of Russia, R&F Department estimates.

Figure 23. Approved mortgage loan applications and transactions, thousand



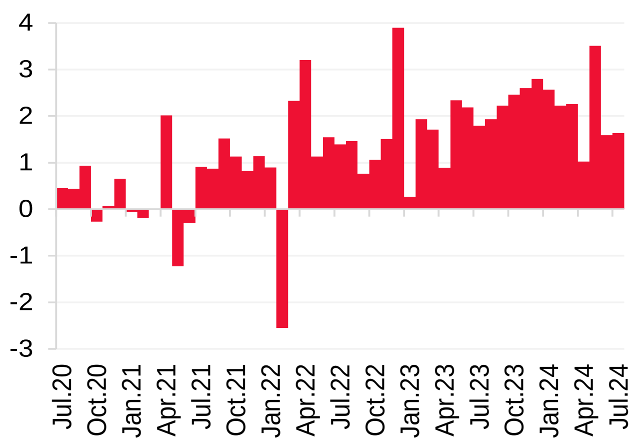
Sources: DomClick, R&F Department estimates.

Figure 24. Loan issuance under subsidies mortgage loan programmes, billion rubles [11],



Sources: DOM.RF, R&F Department estimates.

Figure 25. Household funds at banks, % MoM SA



Sources: Bank of Russia, R&F Department estimates.

[11] Loan provision as part of the Subsidised Mortgage Lending programme in July 2024 was carried out under agreements signed prior to 01.07.2024.