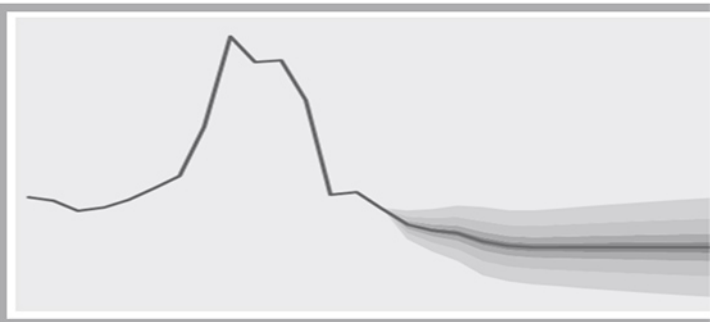
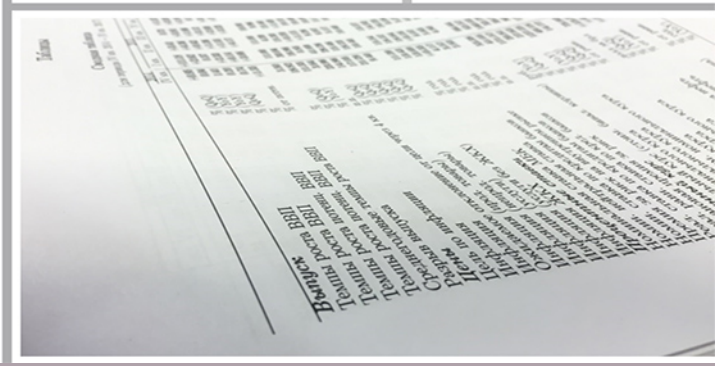
Bank of Russia

The Central Bank of the Russian Federation



4%



No. 3
SEPTEMBER 2016

MONETARY POLICY REPORT

Moscow

DEAR READERS,

In order to improve the effectiveness of the Bank of Russia's information policy with regard to its monetary policy and to assess the relevance of and demand for the materials published, we would be grateful if you could answer the following questions.

1. Do you consider there to be an optimal level of detail in the material presented?

2. Which subjects, in your opinion, should be illustrated in this report?

3. Do you have any other comments or suggestions regarding the report?

4. What is your professional field of interest?

Many thanks in advance for your assistance.

The report has been prepared based on statistics as of 9 September 2016.
Data cut-off date for forecast calculations is 9 September 2016.

An electronic version of the information and analytical review can be found on the Bank of Russia website at http://www.cbr.ru/publ/.

Please send your suggestions and comments to monetarypolicyreport@mail.cbr.ru.

CONTENTS

SUMMARY

In September 2016, the Bank of Russia decided to reduce the key rate from 10.50% to 10.00% p.a. In June-August, the Russian economy developed in line with earlier trends and Bank of Russia forecasts presented in the previous issue of the Monetary Policy Report. Inflation continued to slow down and inflation expectations resumed receding. At the same time, disinflationary pressure from the demand side shows signs of weakening. According to the Bank of Russia's estimates, for the trend towards sustainable decline in inflation to strengthen the current value of the key rate needs to be maintained till end-2016 with its further possible cuts in 2017 Q1-Q2. In line with the decision taken, monetary conditions in real terms will remain moderately tight, shaping the ground for well-balanced lending and consuming strategies of economic agents, thus encouraging further inflation slowdown.

Quarterly year-on-year consumer price growth is expected to settle close to the level of 4% as early as in the first half of 2017. At the same time, annual inflation will gradually decline from the current level of 6.6% to 5.5–6.0% in December 2016 to reach the target of 4% in late 2017. The main factors behind the inflation slowdown will include weak consumer demand, decreasing inflation expectations and relatively stable exchange rate dynamics on the back of moderately tight monetary policy. The reduction of consumer price growth will also be influenced by expected abundant grain crop in Russia in 2016. Moreover, the dynamics of producer costs along with relatively low energy prices will be favourable to the decline of consumer price growth.

Given the relative stable external environment and internal financial conditions, the slowdown of the annual GDP reduction will continue. However, the development and strengthening of positive trends in the economic activity will take some time. The situation in industry is marked by instability and uneven trends among sectors and regions. Later on the output growth will also be restrained by slacking world economy growth along with internal structural factors, including those related to the demographic situation, infrastructure and institutional environment. Considering plans on government spending and budget deficit, the Bank of Russia also expects a certain short-term restraining influence on the economy, triggered by fiscal policy.

Taking into account the aforementioned factors, the baseline scenario suggests that the GDP growth rate in 2017 will be modest and will not exceed 1%. In future, as a result of demand recovery together with monetary policy easing, given achievement of inflation target, the GDP growth rate will pick up, but its potential will be limited by structural factors. In light of this, according to the Bank of Russia estimates, it will amount to 1.5–2% on a year-on-year basis in 2018-2019. The investment rebound will happen on the back of improving consumer demand, decreasing debt burden on the real sector of economy and gradual softening of price and non-price lending conditions.

Given the slowdown of world economy growth and gradual recovery of internal demand the current account balance within the forecast period will remain low. Together with this net private capital outflow on the forecast horizon is also expected to remain low. These trends will be encouraged by a gradual decrease in external debt repayments and broader options for its refinancing, as well as by ensuring the incentives to invest in ruble financial assets, taking into account fairly high real interest rates in the economy.

Future developments in the world economy, as well as in financial and commodity markets still remain uncertain. In this context, aside from the baseline scenario, the Bank of Russia also continues to consider optimistic and risk scenarios. Under the risk scenario, assuming that oil price decrease and then settle at lower level, the economic recession will be deeper and more protracted, whereas inflation will overshoot

5% in 2017 and reach the 4% target only in 2018. The Bank of Russia will pursue a tighter monetary policy to avoid higher price and financial stability risks and might consider the use of other instruments.

In case of optimistic scenario, which suggests a gradual increase in oil prices, the Bank of Russia expects more solid recovery, as compared to the baseline scenario. However, since the relative improvement of the external situation by itself cannot have a significant influence on the mid-term growth potential of the Russian economy, the growth in 2018-2019 after the recovery period will not exceed the figures of the baseline scenario.

At the same time, the main inflation risks are associated with internal factors, primarily with high persistence of inflation expectations and possible consumer behavior adjustment due to lower propensity to save accompanied with weakening precautionary motive, accelerated growth of nominal wages or higher than planned budget spending. As a result, escalated recovery of the consumer demand outstripping the supply may generate additional inflationary pressure and contribute to the faster expansion of imports and the weaker ruble, giving rise to the growth of risks for price, financial and economic stability.

Within the next months, the Bank of Russia will assess inflation risks and economy and inflation dynamics' consistence with the baseline forecast. According to Bank of Russia estimates, to strengthen the trend to a steady decline in inflation the current key rate needs to be maintained till end-2016 with a possibility to cut it in 2017 Q1-Q2.

1. MACROECONOMIC CONDITIONS

In June-August 2016, the external economic conditions in Russia were on the whole in line with the forecasts published in the previous Monetary Policy Report[1] (hereinafter, the Report).

During this period, the situation in the Russian economy fluctuated within previously recorded trends. The slowdown in year-on-year GDP growth continued, however, economic activity dynamics, including across economic sectors and regions, were still varied. Inflation slowed, as expected. Inflation risks persisted, as indicated in part by a slight weakening of demand's moderating influence on prices. Against this backdrop, the continuation of a moderate-to-tight monetary policy established the necessary conditions for economic agents to adopt a balanced approach to borrowing and consumption, thereby contributing to a further inflation slowdown, the achievement of the 4% target in 2017 and, at the same time, financial stability.

Despite the short-term surge in volatility in the global financial markets in connection with the 23 June referendum on the United Kingdom's decision to leave the EU[2], in June-August 2016 the global economy remained generally stable and developed in line with previous trends. The situation in developed and emerging markets was still varied: economic growth rates in the largest developed countries showed greater stability, while business activity dynamics in EME[3] were less favourable (Chart 1.1). According to the Bank of Russia's estimates, aggregate growth in Russia's trading partners remained close to 2015 levels, at roughly 2% per year. This forecast is based on the assumptions that the Chinese economy will gradually slow, on the one hand, and the US economy will recover slightly, on the other.

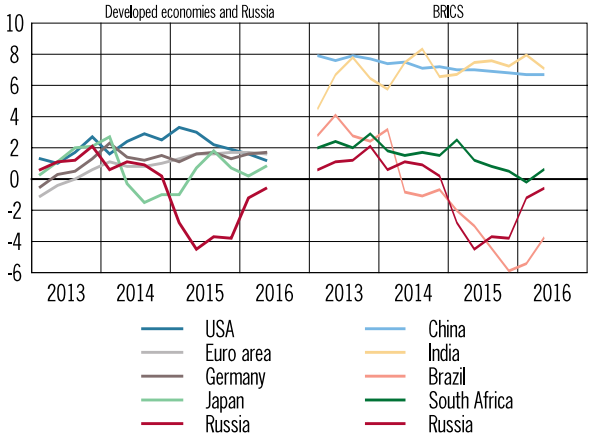
In view of the restrained growth in global demand and relatively high level of supply and inventories, global commodity prices for the most part remained low (Chart 1.2).

However, the situation in the energy market over the summer months was still relatively volatile, due to the varying influences of supply-side factors. On the one hand, among the factors forcing an adjustment in prices were the gradual recovery in crude oil supplies from Canada and the more optimistic estimates for oil production from alternative sources in the US. On the other hand,

Chart 1.1

GDP growth rates of key developed and emerging economies

(percent change on corresponding period of previous year)

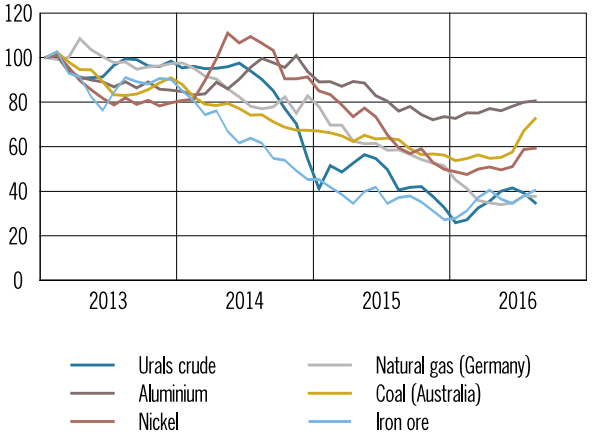


Sources: national statistics agencies, Bloomberg.

Chart 1.2

World prices of Russian principal export commodities

(1.01.2013 = 100%)



Sources: World Bank, Reuters data (Urals crude price).

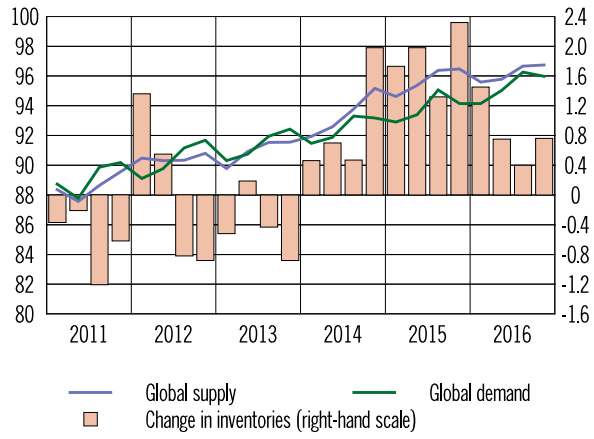
[1] *Monetary Policy Report No. 2 (14), June 2016.*

[2] *See Abbreviations.*

[3] *See Abbreviations.*

Chart 1.3

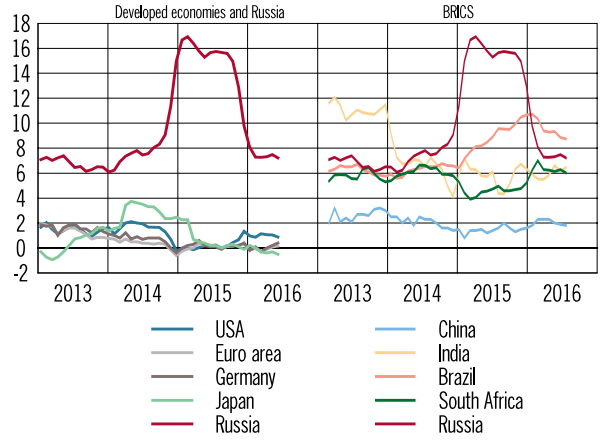
Balance of global supply and demand for oil and other liquid fuel
(million barrels/day)



Source: US Department of Energy.

Chart 1.4

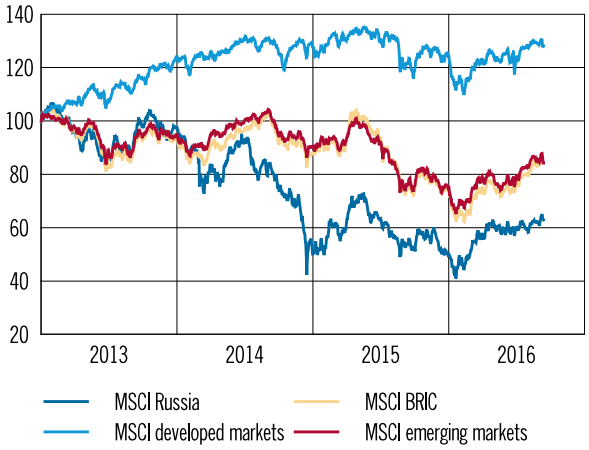
Inflation in key developed and emerging economies
(percent change on corresponding period of previous year)



Sources: national statistics agencies, Bloomberg.

Chart 1.5

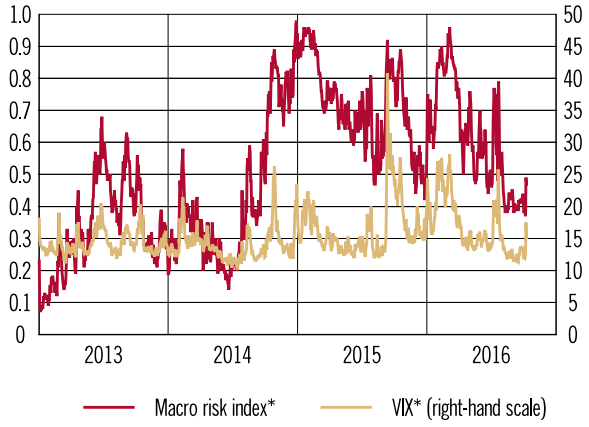
Global stock indices
(January 2013 = 100%)



Source: Bloomberg.

Chart 1.6

Indices of volatility and global financial market risk perception by investors
(points)



** See the Glossary.*
Source: Bloomberg.

the on-going interruptions to oil supplies from Libya and Nigeria and the expectations of a potential freeze in production due to agreements between oil-producing countries (OPEC and others) exerted temporary upward pressure on global oil prices. Meanwhile, estimates of the supply and demand trade-off in the global oil market remained virtually unchanged: the excess oil supply is expected to persist until 2017 (Chart 1.3). Taking this into account, the Bank of Russia kept its baseline Urals crude price forecast at $40 per barrel until the end of 2016.

Global food market prices continued to show signs of recovery relative to the lows at the start of the year. However, the knock-on effect on domestic food prices was restricted by the ruble appreciation. In July-August, the price increases in the global markets slowed considerably, in part due to the favourable changes in the situation in the grain market. However, the risks of price growth for key types of agricultural raw materials will remain in future, partly as a result of the increased likelihood of the natural phenomenon La Niña[4] in October 2016 – January 2017.

Amid the restrained business activity dynamics in the global economy, in June-August inflation in

[4] *A natural phenomenon associated with decreases in water surface temperatures in the equatorial area of the Pacific Ocean. It can intensify after El Niño, affects the same regions and can bring about both intense rainfall (which can lead to flooding) and, conversely, the start of a drought (for example, in the south of Brazil and central Argentina).*

Russia's trading partners changed rather slowly, remaining at relatively low levels (Chart 1.4). Taking into account the pricing situation in the global markets up to the end of this year, external inflationary pressure is not expected to increase.

The situation in the global financial markets in June-August was mostly characterised by the upward dynamics of global stock indices. Volatility and investor risk appetite indicators returned to normal levels after a short-term leap in June (Charts 1.5, 1.6).

In June, the result of the referendum on the United Kingdom's exit from the EU had an impact on market participants' sentiments (see box 'Brexit'). The referendum's outcome in favour of the United Kingdom leaving the EU was an unpleasant surprise to investors and led to sharp growth in financial market volatility due to the fears of potentially marked growth in macroeconomic uncertainty both in the United Kingdom and EU and in the global economy as a whole. However, statements made by central bank representatives of a number of developed countries and the measures implemented by the Bank of England to ease monetary policy in the wake of the referendum more than offset the potential economic and financial risks associated with this event, according to investors.

With the relatively low inflationary pressure persisting amid restrained demand dynamics in the global economy and taking into account the consequences of the UK's decision to leave the EU, the monetary policy of some of the largest global central banks remained relatively eased (See Annex, table 'Monetary policy rates in various countries'). Market participants' expectations regarding the speed with which the US Fed's

Brexit

The United Kingdom's exit from the EU (Brexit) was announced on 24 June 2016. This news caused a surge in volatility in global markets. The pound sterling plummeted against the US dollar to its 30-year low at the start of trading. The stock market of the United Kingdom and other major global stock exchanges also collapsed. In a wave of panic, investors sold off all British assets and increased their investment in government debt securities, which led to a significant reduction in their yields.

Assessments of Brexit's consequences for the UK economy are predominantly negative, meaning that analysts have revised the UK's GDP growth forecasts for 2016 downwards by up to 1 pp. Experts' long-term forecasts (up to 2020–2030) anticipate that the combined inhibitory contribution of Brexit's effects on the country's GDP could range from 3 to 7 pp[1]. A great deal, however, will depend on the conditions of the UK's exit from the EU, in particular on its bilateral trade regulations with the EU. The most pessimistic estimates are based on the fact that the UK will not be given any trading preferences and will have to trade on the WTO terms equal for all member states. Theresa May, the UK's Prime Minister, claimed not to launch Brexit proceedings before the end of 2016. More time is therefore needed for analysts to refine their medium-term forecasts.

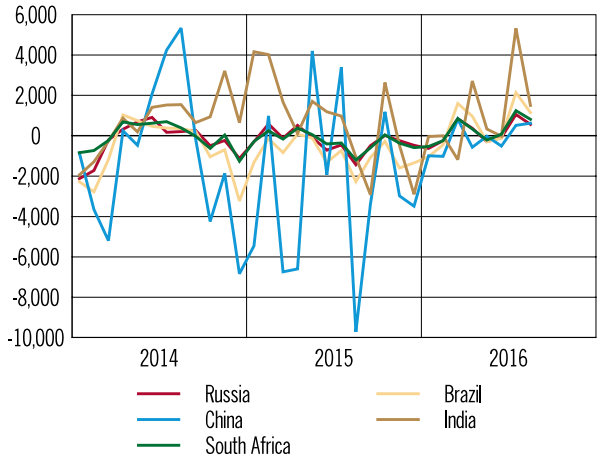
The impact of Brexit will be negative not only for the UK. The European Central Bank forecasts that this event could reduce economic growth in the euro area by a total of 0.5 pp over the next three years. The impact of Brexit on global economic growth will be less marked, according to estimates. Analysts at the International Monetary Fund anticipate that the global economy will slow by 0.2 pp as a result of the UK's exit from the EU. However, this impact could, to a large extent, be offset by the effect of response measures to ease monetary policy, primarily by the Bank of England and ECB.

Given the above assessments, the negative impact of the UK's decision to leave the EU on global financial markets has been short-term. The higher expectations that advanced economies will stick to an easy monetary policy longer than expected have dragged down yields in developed countries. As a result, investors have stepped up their search for more attractive options to place their funds. Assets from emerging markets enjoyed higher demand, which boosted the inflow of portfolio investments in developing markets in July-August, according to data from the Institute of International Finance and EPFR Global, among others (Chart 1.7).

[1] *Estimates by analysts at the OECD, London School of Economics, UK Ministry of Finance and PricewaterhouseCoopers.*

Chart 1.7

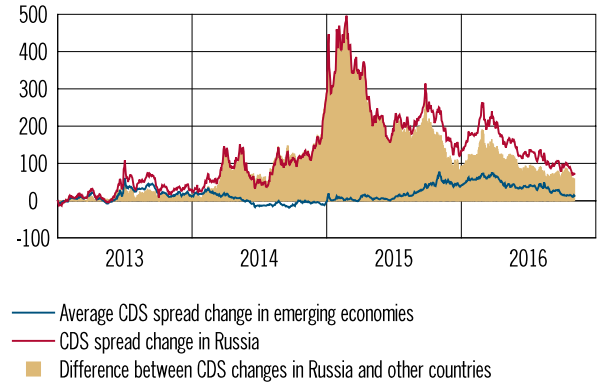
Capital inflow into BRICS countries
(millions of US dollars)



Source: EPFR Global.

Chart 1.8

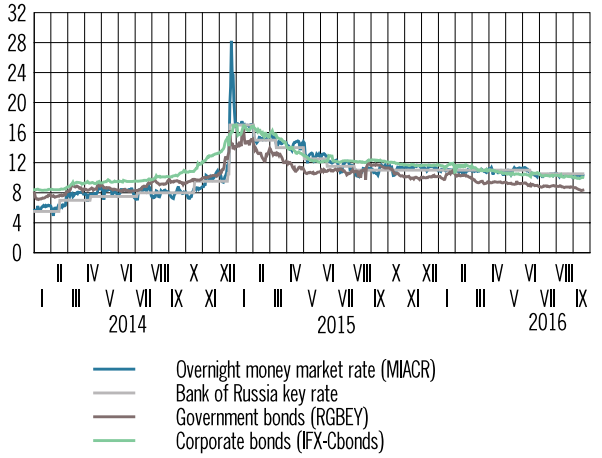
Change of risk premium in Russia and emerging economies*
(basis points)



** Average CDS spread for emerging economies is based on the data for Brazil, China, Turkey, Mexico, Malaysia, Poland, Hungary, etc.*
Sources: Bloomberg, Bank of Russia calculations.

Chart 1.9

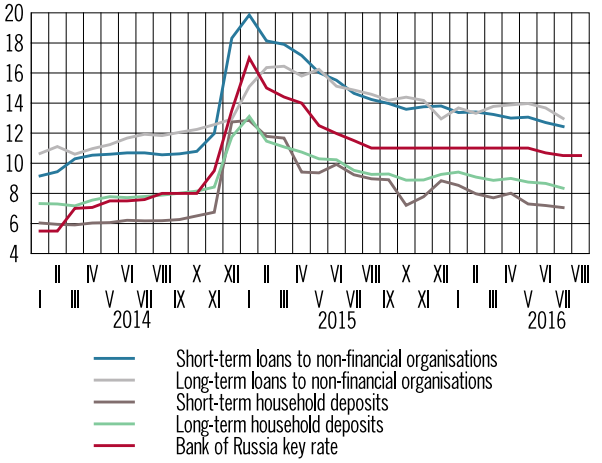
Bond market yields, Bank of Russia key rate and MIACR
(% p.a.)



Sources: MICEX SE, Bank of Russia.

Chart 1.10

Interest rates on bank ruble operations and Bank of Russia key rate
(% p.a.)



Source: Bank of Russia.

monetary policy would return to normal continued to exhibit downward trends: at present, the majority of experts believe that rates will increase no more than once before the end of this year (based on preliminary estimates, in December). However, considering the official statements of members of the US Fed's Open Market Committee, the possibility of a faster normalisation of monetary policy cannot be entirely ruled out.

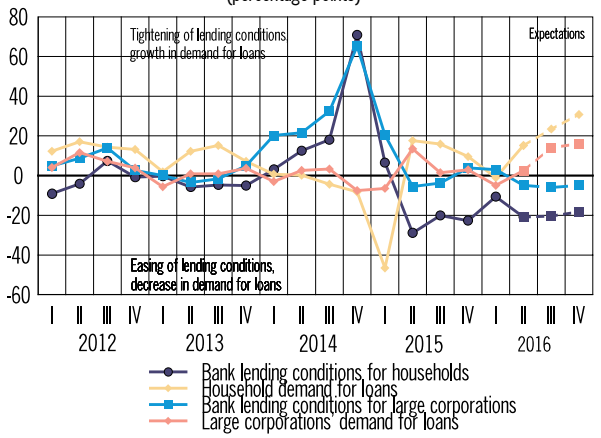
Amid the moderate volatility in the global financial markets and the continued easy monetary policy of the central banks of some of the largest developed countries, the yields on their financial assets remained relatively low over the summer months of 2016. This was conducive to global investors' persisting demand for risky assets and helped maintain the capital inflow into EME, including Russia, in July-August (Chart 1.7). However, the ruble exchange rate against other key currencies gradually strengthened slightly faster than the Bank of Russia forecast. Russia's risk premium was relatively low (Chart 1.8). The Russian corporate sector's opportunities for external borrowing were still restricted by international financial sanctions. In view of this, investment activity and secondary trading in the corresponding segments continued to be low, with major companies accounting for the overwhelming majority of loans.

Internal financial conditions in the Russian economy, which have been shaped by the

Chart 1.11

Lending conditions and demand for loans indices

(percentage points)

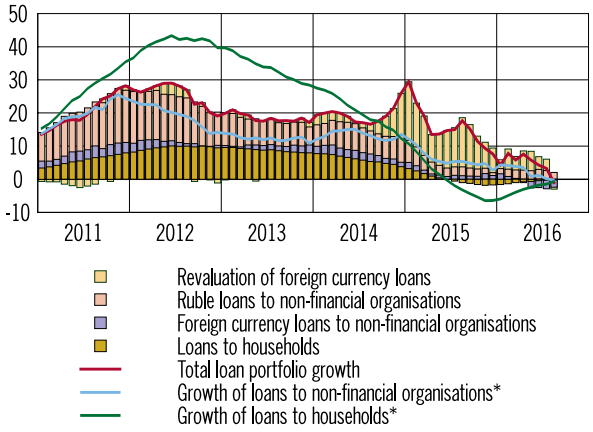


Source: Bank of Russia.

Chart 1.12

Contribution of various components to annual growth rate of banks' loan portfolio

(%)

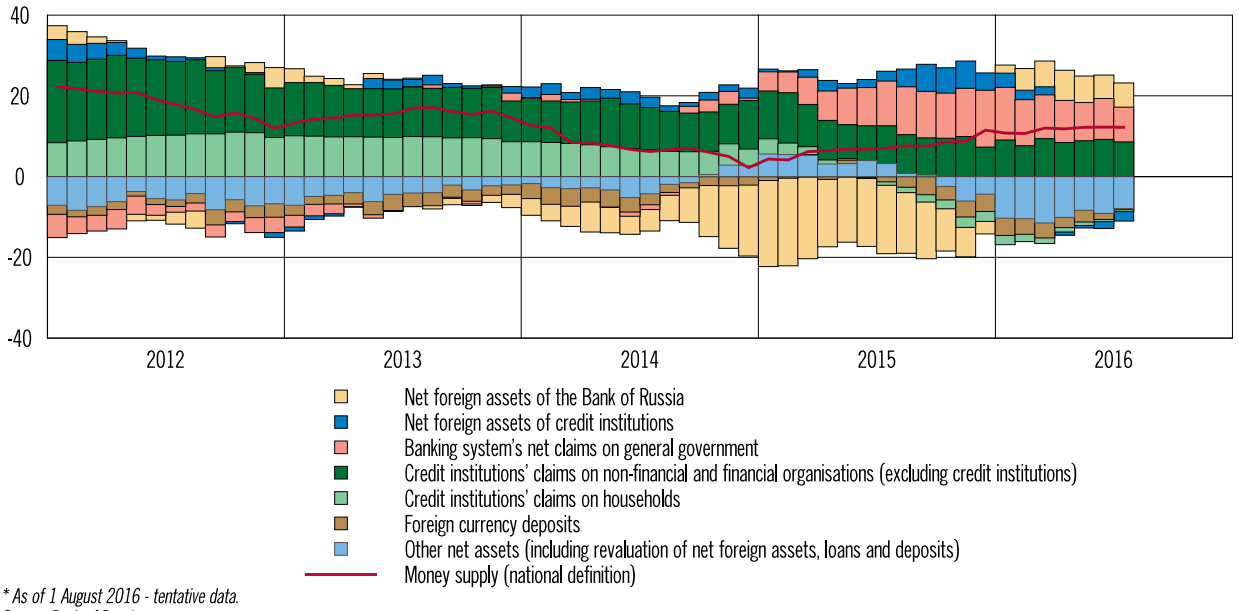


** Adjusted for foreign currency revaluation.*
Source: Bank of Russia.

Chart 1.13

Sources of money supply (national definition)*

(annual growth, %)



** As of 1 August 2016 - tentative data.*
Source: Bank of Russia.

continuation of a moderate-to-tight monetary policy aimed at reducing inflation and maintaining the financial system stability, also remained virtually unchanged compared with previous months.

Nominal market interest rates continued to fall in June-July (Charts 1.9, 1.10). Their dynamics reflected the key rate reduction in June 2016 (from 11% to 10.5%) and the prospective cuts expected as inflation slows. However, in view of inflation and inflation expectation dynamics, real interest rates can be assumed to remain relatively high, maintaining economic agents' balanced approach to savings and lending.

In turn, non-price BLC[5], appraised by the Bank of Russia through the survey among credit institutions, eased in 2016 Q2 (Chart 1.11), pointing to a minor improvement in banks' assessments of credit risks in the economy. At the same time,

[5] *See Abbreviations. Non-price bank lending conditions include loan maturity, loan amount, requirements for borrower's financial position, collateral requirements, additional fees, and the range of lending types.*

the changes in non-price BLC still varied across different types of lending being more favourable for households than for the corporate sector. The relaxation of lending conditions and borrowing opportunities for companies in the real sector were still restricted by the overall debt burden which, despite the slight decrease, was still relatively high. Amid these conditions, lending activity was restrained: the annual growth in banks' loan portfolios slowed slightly to 3–4% in June-July (Chart 1.12). The growth in the banking sector's lending to the economy is expected to be 4–6% by the end of 2016.

In June-August 2016, the moderate growth in monetary aggregates persisted (Chart 1.13). Sources of money supply showed no considerable changes as compared with previous months: the increase in the banking system's net lending to the general government amid the persistently high budget deficit (see box 'Fiscal policy') made a further positive contribution to money supply growth along with higher lending to the economy. Given the slightly reduced expected growth in private sector lending, the Bank of Russia revised its forecast for money supply growth (in the national definition) for

Fiscal policy

According to data from the Russian Ministry of Finance, the Russian Federation's budget deficit in January-July 2016 remained virtually unchanged at ₽0.9 trillion (1.9% of GDP) compared with the same period in 2015. The federal budget deficit was ₽1.5 trillion (3.3% of GDP), an increase of ₽0.5 trillion compared with the same period in 2015.

Budget revenue for January-July 2016 reduced by 2.0% year-on-year to ₽14.9 trillion (32.9% of GDP) and federal budget revenue fell by 10.6% to ₽7.0 trillion (15.3% of GDP). The main factor behind this reduction in revenue was the fall in oil and gas receipts (by 27.1%). At the same time, the level of non-oil and gas receipts remained stable, mainly due to the growth in receipts from direct taxes (VAT and excise duties) on domestically-produced and imported goods (by 9.3%).

Budget expenditure reduced by 1.7% year-on-year to ₽15.8 trillion (34.7% of GDP) and federal budget expenditure decreased by 4.0% to ₽8.5 trillion (18.7% of GDP). Amid the reduced spending on national defence and security, social spending (on social policy, health care and education) increased.

In August 2016, the Government of the Russian Federation decided to make a one-time ₽5,000 payment to pensioners in January 2017 in place of a previously discussed additional indexation of their pensions (pensions have already been indexed by 4% since the start of the year). This decision in part makes up for the reduction in pensions in real terms, but carries less inflation risks in the medium term than an additional indexation as the one-time payment does not increase the baseline for pension incomes for the next year.

A further ₽0.4 billion were transferred from the Reserve Fund in August to finance the federal budget deficit, making a total of ₽1.2 trillion since the start of 2016. In addition, the Russian Ministry of Finance continued to successfully implement its government debt placement programme, with the net placement of OFZ portfolio reaching ₽312.0 billion overall in January-July. In June-July, the Russian Ministry of Finance also used other sources to fund the deficit.

With the stepping up of domestic borrowing programmes, the amount of domestic federal debt rose in June-August 2016 by ₽0.1 trillion to ₽7.3 trillion. At the same time, external debt continued to fall in June-July to ₽3.4 trillion, due to foreign exchange revaluation.

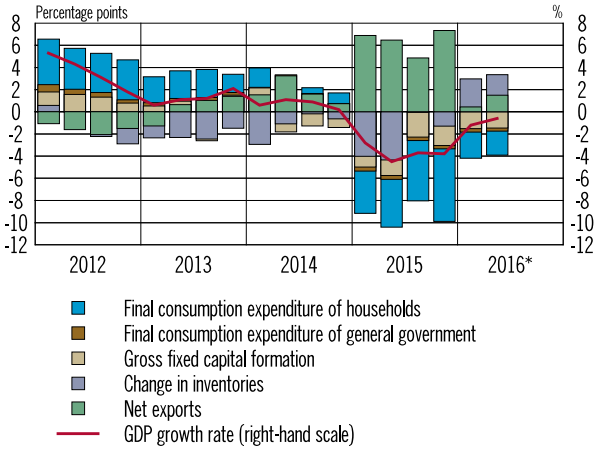
The Russian Ministry of Finance forecast the federal budget deficit to be 3.3% of GDP by the end of 2016 (the Bank of Russia's forecast is 3.6% of GDP). In future, there are plans for fiscal consolidation, reducing the deficit to 3.2% of GDP in 2017, 2.2% of GDP in 2018 and 1.2% of GDP in 2019. Based on conservative oil price assumptions of $40 per barrel, expenditure needs to remain at a constant level in nominal terms to reduce the federal budget deficit. According to the Russian Ministry of Finance's estimates, the Reserve Fund resources used to finance the federal budget deficit in 2016 could reach ₽2.3–3.0 trillion depending on the outcome of privatisation programme and raising funds through other sources to finance the deficit. At the same time, in 2017, the Russian Ministry of Finance plans to increase the amount of funding for the budget deficit using net domestic borrowing, which could grow 4 times to more than ₽1 trillion, according to the preliminary estimates by the Russian Ministry of Finance.

According to Bank of Russia estimates, in 2016 the fiscal policy contribution to domestic economic activity dynamics will more than likely be near zero. In 2017–2019, taking the planned fiscal consolidation into account, the contribution will be slightly negative. However, the continuation of the conservative policy for indexing public-sector wages and social benefits should have a further moderating impact on inflation through inflation expectations.

Chart 1.14

GDP growth structure by expenditure

(on corresponding period of previous year)



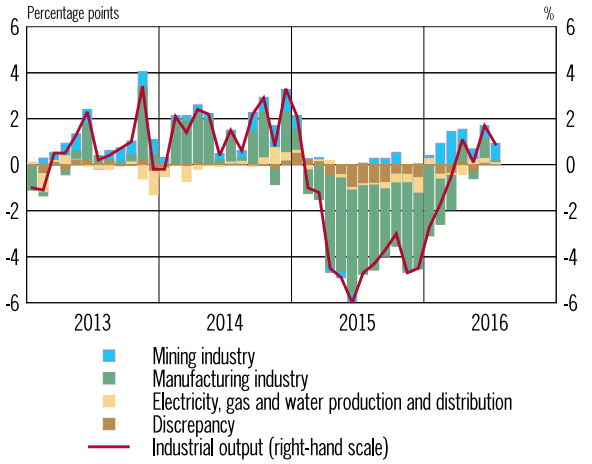
** 2016 Q2 - Bank of Russia estimate.*

Sources: Rosstat, Bank of Russia calculations.

Chart 1.15

Contributions of industrial output components (adjusted for calendar factor)

(on corresponding period of previous year)



Sources: Rosstat, Bank of Russia calculations.

the end of 2016 to 9–12% (10–13% in the previous Report).

As the external situation and internal financial conditions remained relatively stable, economic downturn continued to slow. According to Rosstat data, in 2016 Q2, GDP fell by 0.6% as compared with the corresponding quarter of the previous year (by 1.2% the previous quarter, Chart 1.14), which slightly exceeded the Bank of Russia's forecast published in the previous Report. This discrepancy resulted largely from more restrained export dynamics, including for non-commodities, than previously expected.

However, industrial production dynamics for the most part remained positive (Chart 1.15). Annual growth in industrial production adjusted for calendar differences fluctuated around 1% in May-July 2016. Meanwhile, monthly growth in industrial production (seasonally adjusted) slowed slightly compared with the first few months of 2016.

Amid the relatively stable external situation, the mining industry showed growth compared with the same period of the previous year, in part due to external demand. The mining industry's contribution to industrial production growth (adjusted for calendar differences) was 0.5-0.7 pp.

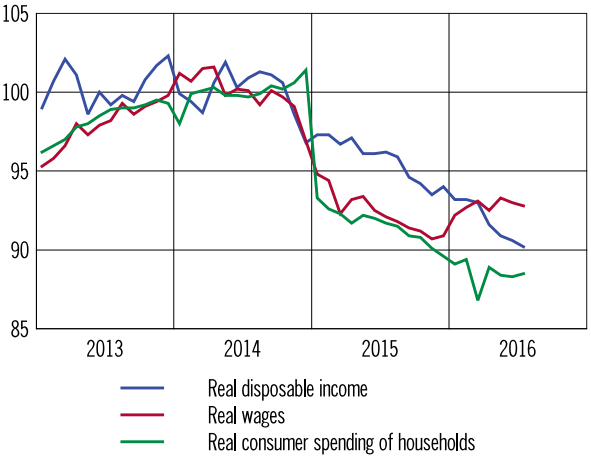
At the same time, the situation in the manufacturing industry was unstable and varied by activity type in May-July. In particular, amid the slightly slower growth in the former leaders (the chemical and food industries), certain high-tech industries (household appliances, machinery, and medical equipment) underwent a revival; however, the positive contribution of these industries to industrial production dynamics was generally modest.

Labour market did not exhibit any significant changes: unemployment and part-time employment figures remained at the same levels as previous months (Table 1.1). Annual nominal wage growth was still high at roughly 8%. However, monthly wage dynamics over the summer months were extremely moderate: in June-July nominal wages grew by 0.3–0.4% month-on-month (seasonally adjusted). During this period, wage growth varied across sectors: the highest growth was seen in activity types where the level of income was above the economy's average, including mining, financial sector, real estate and services.

Chart 1.16

Real wages, disposable income and consumer spending of households

(seasonally adjusted, 2014 = 100%)



Sources: Rosstat, Bank of Russia calculations.

Table 1.1

Labour market

Indicators	2014				2015				2016	
	I	II	III	IV	I	II	III	IV	I	II
Employment and unemployment (seasonally adjusted)										
Unemployment rate, %	5.0	5.2	5.2	5.2	5.3	5.7	5.6	5.7	5.4	5.8
Employed to unemployed ratio	18.6	18.3	18.3	18.3	17.9	16.5	16.9	16.6	17.4	16.2
PMI Composite Employment Index, points	48.2	47.4	48.2	46.6	44.8	46.0	47.4	45.9	46.5	48.6
Wages (as % year-on-year)										
Nominal wages	11.1	10.2	8.3	7.7	5.7	5.9	4.7	3.3	7.7	7.9
Real wages	4.4	2.4	0.6	-1.7	-9.0	-8.5	-9.5	-9.8	-0.6	0.5
Wage arrears	6.2	5.7	-11.9	-10.2	7.9	22.6	38.6	55.9	45.4	24.5
Part-time employment										
Number of part-time employees, as % of previous period (seasonally adjusted)										
Total	-1.2	-0.1	2.2	0.1	1.1	2.6	0.1	1.2	0.6	0.2
Part-time employment	7.8	-4.2	-3.4	4.6	11.9	2.7	-3.5	3.8	9.8	1.1
Part-time employment on employer's initiative	14.6	-1.7	-8.0	11.9	18.0	22.7	-3.4	-6.9	-0.7	15.4
Part-time employment upon mutual agreement	-0.7	1.7	1.7	1.8	2.5	3.7	2.6	3.6	2.7	3.3
Idle employees	0.0	-1.3	12.7	-11.1	10.4	-2.8	-4.3	2.4	-7.5	0.6
Unpaid leave	1.5	-0.1	0.8	0.3	0.2	1.4	-0.1	0.6	0.9	0.5
Part-time employees, as % of headcount										
Total	9.0	9.5	10.4	10.3	9.4	10.4	11.0	11.0	10.0	10.7
Part-time employment	2.2	2.1	2.0	2.2	2.4	2.5	2.4	2.5	2.8	2.8
Part-time employment on employer's initiative	0.3	0.3	0.2	0.3	0.4	0.4	0.4	0.4	0.4	0.4
Part-time employment upon mutual agreement	1.9	1.8	1.8	1.9	2.0	2.1	2.0	2.1	2.4	2.4
Idle employees	0.7	0.6	0.6	0.8	0.8	0.7	0.5	0.9	0.7	0.6
Unpaid leave	6.1	6.8	7.8	7.3	6.2	7.2	8.1	7.6	6.5	7.3
Alternative indicators of part-time employment										
Average working hours per employee (year-on-year)	0.3	0.4	0.2	-0.1	-0.3	-0.4	-0.5	-0.1	-0.3	0.1
Labour force utilisation in industrial production (normal level = 100)	87.7	86.7	89.0	85.7	81.7	86.7	87.7	88.0	83.7	88.3

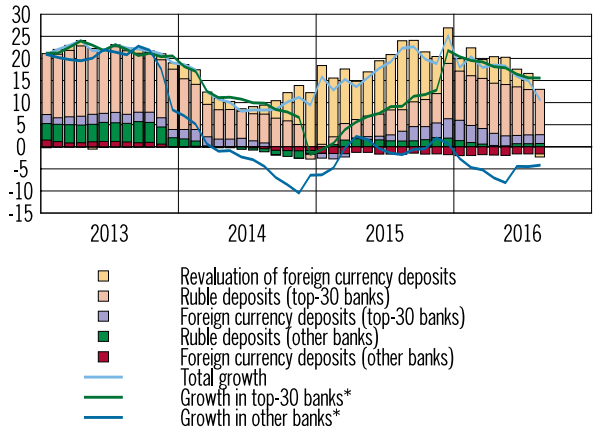
Change compared with previous 12 months:
– situation improved (more than 1 standard deviation)
– situation improved (less than 1 standard deviation)
– situation remains unchanged (± 0.15 standard deviations)
– situation deteriorated (less than 1 standard deviation)
– situation deteriorated (more than 1 standard deviation)

Sources: Rosstat, Bank of Russia calculations, Russian Economic Barometer, Markit Economics.

Chart 1.17

Contribution of individual bank groups to annual growth of household deposit portfolio

(%)

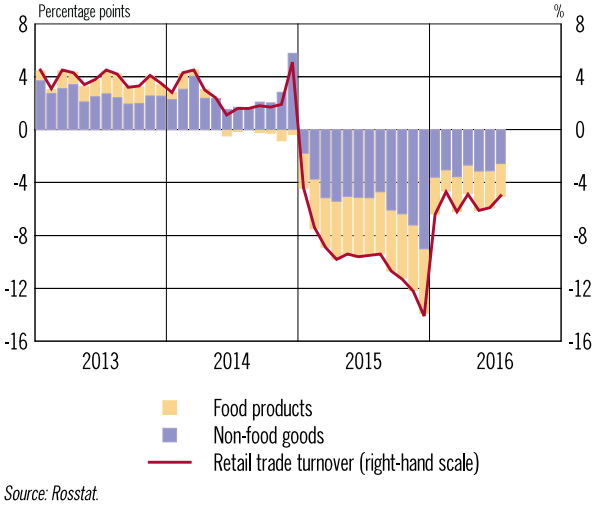


** Adjusted for foreign currency revaluation.*
Source: Bank of Russia.

Chart 1.18

Growth in retail trade turnover

(contribution to growth rate, on corresponding period of previous year)



Source: Rosstat.

Divergence in consumption and wage dynamics

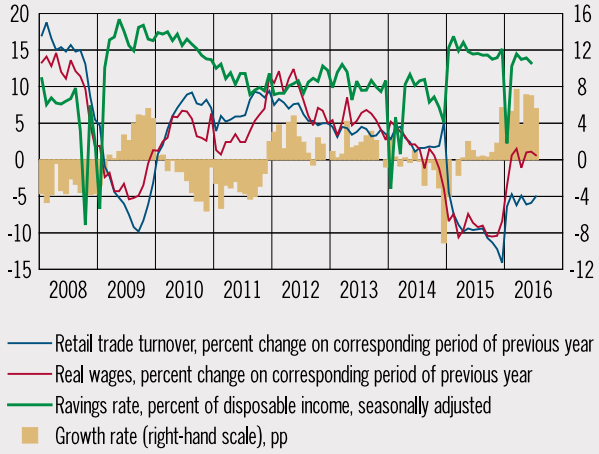
Since the start of 2016, the imbalance in consumer activity and wage dynamics has increased: amid a recovery in real wages, retail trade turnover has continued to fall. Previously, the divergence in the dynamics of these indicators increased during times of economic booms and slumps, while during periods of relatively stable growth, real wages were a key factor behind retail trade turnover dynamics (Chart 1.19).

To identify the factors influencing this divergence, econometric methods were used to assess the dependence of retail trade turnover on wages and a number of additional factors such as savings rates, pensions, wage arrears, household lending and interest rates on deposits over one year[1].

The results of these assessments show that the growth in real wages in 2016 Q2 made a positive contribution (roughly 0.4 percentage points) to retail trade turnover dynamics. The overall decrease in retail sales was a result of the combined influence of other factors, with the largest negative contribution coming from the persistently high savings rates (2.9 percentage points). Real interest rates on deposits over one year (0.2 percentage points), pensions, wage arrears and household lending (0.1 percentage points each) made a significant, but less negative contribution to retail trade turnover dynamics. Furthermore, the dynamics of indicators such as real income from entrepreneurial activity, foreign currency sales and other income had a restraining effect on consumer demand during this period, according to estimates (Chart 1.20).

Chart 1.19

Retail trade turnover, wages and savings rate

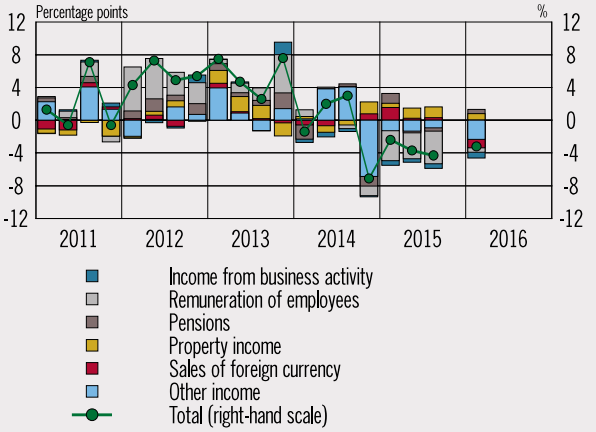


Sources: Rosstat, Bank of Russia calculations.

Chart 1.20

Growth in real household income*

(on corresponding period of previous year)



** Data for 2015 Q4 are unavailable. Positive contribution of pensions in real household income in 2016 Q1 results from growing number of pensioners amid lower real pensions.*

Sources: Rosstat, Bank of Russia calculations.

[1] The regression was assessed based on quarterly data. All of the variables, except savings rates, are in real terms. The majority of the variables (except savings rates and deposit interest rates) are given as seasonally adjusted growth rates relative to the previous quarter. Since households' expectations regarding the future inflow of income influence savings rates, retail trade turnover dynamics and savings rates will be determined simultaneously. Given that savings rates are endogenous, the instrumental variables method was used. Lags in Rosstat's consumer confidence index, real rates on household deposits over 1 year, and the lag in the savings rates themselves were used as instruments for savings rates. These instruments were tested for validity and relevance according to standard econometric criteria.

While wage dynamics show a sustainable growth, real disposable incomes continued to fall in May-July due to shrinkages in pensions, business and other incomes in real terms (Chart 1.16). The overall downward trend in real disposable household income continued to constrain internal demand. The persistently weak consumer activity was also largely linked to the continued high savings rates and inertia in savings dynamics (see box 'Divergence in consumption and wage dynamics').

Relatively high real interest rates remain the main reason behind the elevated propensity to save, therefore fund depositing appeals to households. Another important factor behind the high household savings rates is caution surrounding the ongoing uncertainty over income and employment

prospects. The impact of this factor is corroborated by the stronger households' inclination to deposit funds with major banks (Chart 1.17) since they are generally perceived as more reliable, despite having lower return on deposits compared with smaller banks. Ultimately, the wage growth pass-through to consumption was hampered by the aforementioned uneven wage growth across industries.

Retail trade turnover continued to fall in May-July under the influence of all of these factors – the reduction in real household disposable income along with persistently high savings rates, on the one hand, and the continuing growth in wages in real terms, on the other hand, – though the year-on-year decline slowed (Chart 1.18).

Both investment and consumer demand remained weak. The reduction in fixed capital investment continued in 2016 Q2, but its annual reduction slowed slightly to 3.9% from 4.8% the previous quarter (the previous Report forecast 3–4%), mostly down to the low base effect. Assessments based on indirect indicators (construction works and investment goods production index) point to persistently weak investment dynamics in July, too (Chart 1.21).

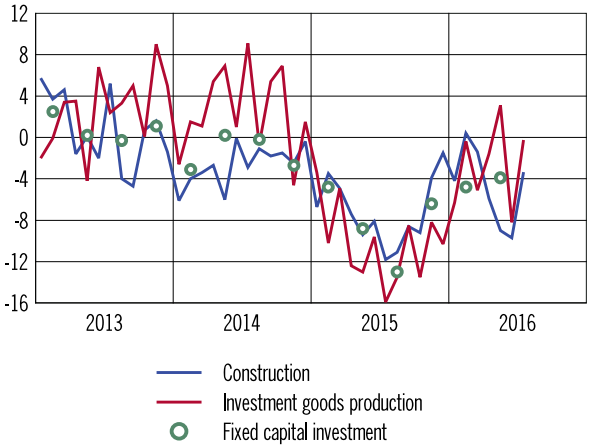
The ongoing demand-side restrictions, moderately tight lending conditions, relatively high debt burden of certain companies, and slight deterioration in profits in some industries (see box 'Financial position of real sector organisations in 2016 H1') continued to exert a negative influence on companies' investment plans[6]. One factor which did provide some support for investment activity was the slight recovery in machinery and equipment imports. Given these factors, the Bank of Russia estimates that fixed capital investment will contract by 2.5–3.5% year-on-year in 2016 Q3.

Amid the persistently weak consumer and investment demand, positive dynamics of inventories made a significant contribution to GDP performance over the last two quarters, according to estimates. The accumulation of inventories after the anticipated good harvest, among other things, will support output in 2016 Q3 as well. However, given the lack of prospects of a dynamic recovery

Chart 1.21

Investment, construction and investment goods production

(growth, percent change on corresponding period of previous year)



Sources: Rosstat, Bank of Russia calculations.

in demand[7], the positive effect of changes in inventories on GDP dynamics is estimated to gradually weaken in future.

Growth in net exports also continued to make a positive contribution to GDP. Relatively stable external demand amid quite high commodity inventories and excess capacity in some industries created the preconditions for growing competition among suppliers in global commodity markets accounting for a sizeable share of Russian exports. As a result, export dynamics improved somewhat in 2016 Q2. According to estimates, in 2016 Q2, annual growth in exports in real terms was close to zero. However, this result, as noted above, was significantly worse than expectations. Given the current trends, the Bank of Russia's export growth forecasts for the second half of the year have also been revised downwards.

At the same time, amid the slowing decline in demand and strengthening of the ruble, the import contraction slowed in real terms (to 7.5% year-on-year, according to estimates). Along with the unfavourable climate for Russian export prices, this meant that Russia's current account balance of payments in 2016 Q2 remained far lower than in the corresponding period of the previous year. However, capital outflow reduced proportionally, in part due to lower external debt repayments. In these conditions the stability in the foreign exchange market was maintained and banks continued repaying debts

[6] *According to the surveys carried out by the Institute for Economic Policy's survey division, business investment confidence was described as 'moderately pessimistic' in May-July.*

[7] *According to the Institute for Economic Policy's survey division, business expectations regarding the prospects of recovery in demand for their products were pessimistic.*

Financial position of real sector organisations in 2016 H1

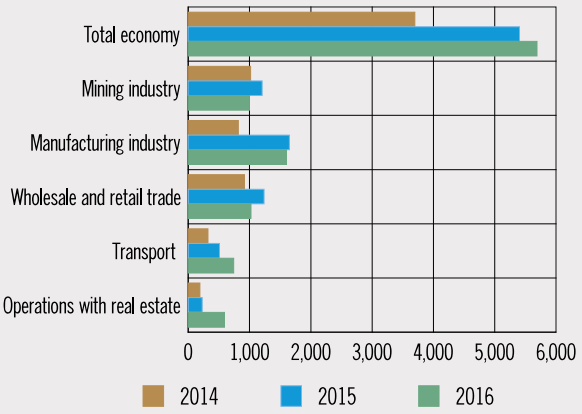
In the first half of 2016, corporate net profits were 5.3% higher in nominal terms than the figure for the same period in the previous year. Some growth in profits (by 7.4%) was seen amid a substantial increase in losses (by 21.4%).

The breakdown by industry reveals certain heterogeneity (Chart 1.22). The improved corporate financial performance was down to the infrastructure sector of the economy, which saw profits grow and losses shrink (in particular in real estate, leasing and services, construction, electricity, gas and water production and distribution, transport and communications). However, a fall in net profits and losses was seen in manufacturing, retail and wholesale trades, and mining and quarrying. The deterioration of the financial position of the companies in the sectors, which generate almost half of the financial performance and are generally the leading investors, is posing additional risks to investment activity. However, the improvement in the financial performance of the infrastructure sectors sets preconditions for improved efficiency in their operations, which could have a beneficial impact on economic growth potential in the long term.

Chart 1.22

Net profits of large and medium Russian companies in 2014-2016 H1

(billions of rubles)

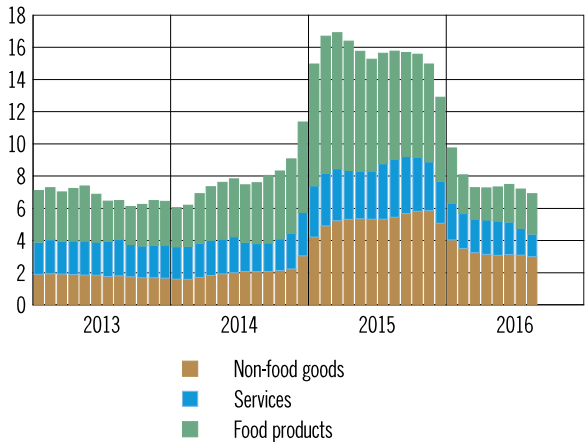


Source: Rosstat.

Chart 1.23

Contribution to inflation

(on corresponding period of previous year, percentage points)



Sources: Rosstat, Bank of Russia calculations.

on Bank of Russia reverse operations to provide foreign currency (see Annex 'Dynamics of major items in the Russian balance of payments in 2016 Q2).

Given the above trends, the Bank of Russia estimates that GDP will drop by 0.4–0.7% year-on-year in the third quarter. However, the quarterly GDP growth is expected to hit positive territory until the end of 2016. By the end of 2016, the decrease in GDP will be 0.3–0.7%, which is in line with the forecast published in the previous issue of the Report.

These financial and economic conditions paved the way for a further slowdown in inflation in 2016 Q3. Inflation dynamics in June-August 2016 were shaped by a set of factors. On the one hand, the growth in prices of consumer goods and services was curbed by the slack demand, stronger ruble, persistently moderate growth in producer prices, and the lower indexation of natural monopolies' prices and tariffs compared with the previous year. On the other hand, the slowdown in inflation was constrained by the worsening situation in certain food markets (buckwheat, sugar, fish products, vegetable oil) due to temporary factors and the weakening of demand-side restrictions.

As forecast by the Bank of Russia, in June annual inflation rose to 7.5% from 7.3% in March-May due to the base effect (Chart 1.23). In July, this decline resumed, and by the end of August annual inflation stood at 6.9%. Core inflation also fell to 7%. However, monthly price growth (seasonally adjusted) in June-August increased slightly compared with March-May. Annual price growth for non-food goods excluding petrol, one of the most

Table 1.2

Inflation expectations of economic agents

Survey	Expectation horizon	2014				2015				2016							
		I	II	III	IV	I	II	III	IV	January	February	March	April	May	June	July	August
Inflation expectations (absolute), %																	
Households																	
Public Opinion Foundation	next 12 months	11.8	11.7	12.5	15.5	15.7	15.0	16.0	16.4	16.7	15.7	14.7	14.6	13.6	14.2	14.3	12.6
Public Opinion Foundation (Bank of Russia calculations)	next 12 months	8.1	9.0	9.6	14.4	13.8	12.2	14.5	12.8	10.8	7.8	7.4	7.2	6.5	6.7	6.9	6.4
Professional analysts																	
Bloomberg	2016						6.7	7.0	7.2	8.0	8.3	7.9	7.4	7.2	6.5	6.4	6.4
Interfax	2016					7.0	6.7	7.4	7.6	8.5	8.3	7.6	7.4	7.3	6.7	6.6	6.2
Thomson Reuters	2016								7.5	8.1	7.9	7.4	7.1	7.0	6.5	6.3	6.0
Financial markets																	
OFZ-IN	next 8 years							6.4	5.8	6.2	6.1	5.4	5.2	5.0	4.6	4.6	4.5
OFZ-IN (without option adjustment)	next 8 years							8.1	7.3	7.7	7.6	6.9	6.7	6.5	6.0	5.8	5.6
Bond market	next quarter	7.1	7.2	7.9	8.4	10.7	15.1	14.2	14.1	-	-	12.5	-	-	7.4		
Interbank market	next quarter	7.2	8.1	8.9	9.7	13.0	18.4	15.2	12.4	-	-	10.9	-	-	7.1		
Inflation expectations (balance of replies*)																	
Households																	
Public Opinion Foundation	next 12 months	84	85	84	83	76	72	80	83	85	82	84	83	81	78	82	77
Public Opinion Foundation	next month	79	82	76	77	68	60	71	78	80	76	72	74	70	68	72	69
Enterprises																	
Russian Economic Barometer	next 3 months	26	26	32	70	32	20	28	48	46	22	14	16	30	38		
Bank of Russia (Banking Supervision Department)	next 3 months	14.3	12.4	13.9	30.3	14.8	12.7	12.1	17.3	15.6	13.6	12.4	11.5	11.5	12.1	10.1	
Retail prices (Rosstat)	next quarter	42	41	41	43	31	28	30	29	-	-	32	-	-	29		
Tariffs (Rosstat)	next quarter	6	5	2	5	7	6	2	2	-	-	5	-	-	5		

Change compared with previous 3 months:

– inflation expectations improved (more than 1 standard deviation)

– inflation expectations improved (less than 1 standard deviation)

– inflation expectations remain unchanged (± 0.2 standard deviations)

– inflation expectations deteriorated (less than 1 standard deviation)

– inflation expectations deteriorated (more than 1 standard deviation)

** Balance of replies is a difference in the share of replies of the respondents, who expect that prices will increase and that prices will decrease.*

Sources: Public Opinion Foundation survey results, Rosstat, Interfax, Bloomberg, Thomson Reuters, Bank of Russia calculations, Russian Economic Barometer.

stable components of inflation, remained relatively high (Chart 1.24).

The appreciation of the ruble amid the generally stable foreign economic climate made a significant contribution to the slowdown in inflation, exerting a marked constraining influence over price growth for non-food goods and services. According to estimates, the contribution of the ruble exchange rate to annual inflation was roughly 1 pp in August, after 2 pp in May.

Producer price dynamics, affected in part by the moderate price growth in global commodity markets, generally continued to be a factor curbing growth in consumer prices. In addition, the favourable situation in the Russian agricultural market helped reduce inflationary pressure from producer prices.

However, inflation expectation dynamics restricted the speed of inflation reduction (Table 1.2). In June-July inflation expectations stabilised at April-May levels, and resumed their downward trend in August[8]. At the same time, the overall level of household and corporate inflation expectations remains elevated, meaning that it is as yet premature to characterise the observed downward trend as stable.

In addition, the slowing decline in consumption, including non-food goods, could signal that deflationary effect of demand is weakening as households and companies gradually adapt to the current economic conditions following, among other things, the slight improvement in consumer confidence due to the stable growth in wages.

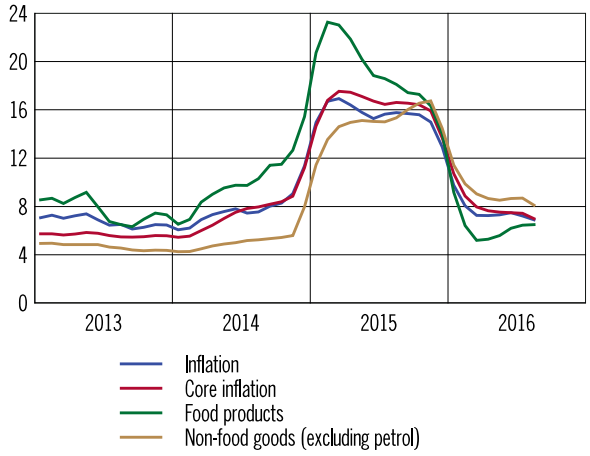
One sign of the lower contribution of demand-side restrictions to the slowing inflation may be the fact that inflation was in line with the Bank of Russia's forecast despite the disinflationary effect of the faster than expected recovery of the ruble amid the relatively favourable foreign economic climate in 2016 Q3.

The Bank of Russia's moderately tight monetary policy will help further reduce inflation in 2016.

Chart 1.24

Prices of consumer goods and services

(percent change on corresponding period of previous year)



Sources: Rosstat, Bank of Russia calculations.

According to the baseline forecast, inflation will be 5.5–6.0% by the end of 2016.

The main inflation risks are associated with changing external factors, lower savings incentives and persistently elevated inflation expectations. Given the inflation slowdown in line with the forecast and the slight reduction in inflation expectations despite the persistently unstable economic activity, on 16 September 2016, the Bank of Russia Board of Directors decided to cut its key rate to 10.00% p.a. Having said that, the Bank of Russia estimates that the achieved key rate needs to remain unchanged until the end of 2016 to consolidate stable downward inflation trends. The moderately tight monetary policy will ensure that positive real interest rates in the economy remain at a level which will encourage the propensity to save and boost demand for lending which will not increase inflationary pressure. This will contribute to a further reduction in inflation to the 4% target in 2017. When deciding on the key rate in the coming months, the Bank of Russia will assess inflation risks and how well economic and inflation dynamics correspond to the baseline scenario.

[8] *According to estimates based on the path of median forecast inflation for the year, calculated by inFOM, and the probabilistic methods applied by the Bank of Russia.*

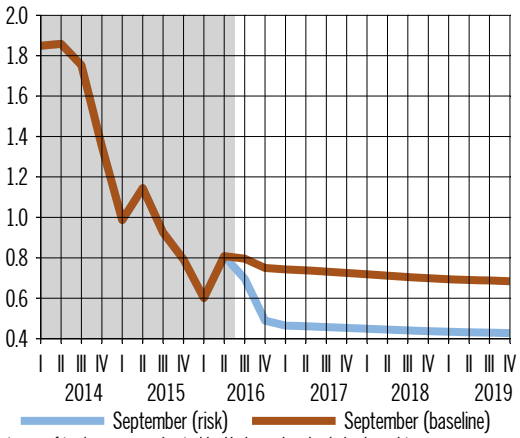
2. ECONOMIC OUTLOOK AND KEY RATE DECISION

In the previous Monetary Policy Report, the Bank of Russia considered three scenarios of Russia's economic development. The key differences in these scenarios were the assumptions made about oil price dynamics. The trends shaping the global financial and commodity market climate and the Russian economic environment in June-August 2016 were largely in line with the baseline scenario presented in the previous Report.

The baseline scenario assumed a slow adjustment in Urals crude oil prices from roughly $48 per barrel in June 2016 to $40 per barrel in 2016 Q3. Its actual average level in July-August 2016 was roughly $43 per barrel, which is slightly higher than the previous forecast. Oil production and supply outages of some exporters, which boosted oil prices in spring-summer 2016, are abating (supplies from Canada have almost been restored, but there are still problems with supplies from Nigeria, Libya and Venezuela). Talks between OPEC member-states and major non-OPEC exporters to limit oil production are unlikely to have a lasting effect on the market situation. This would only occur if the parties were to agree to directly reduce production relative to current levels, an outcome which is extremely unlikely. The more likely decision to fix production and exports at levels close to those at present will not have a significant impact on the balance of supply and demand in the global oil market.

Chart 2.1

Terms of trade



Note: terms of trade are approximated by Urals crude price index in real terms (oil prices adjusted for foreign inflation).
Source: Bank of Russia calculations.

Given these trends, the Bank of Russia has not changed the assumption regarding the path of oil prices in the baseline scenario: Urals crude oil prices are expected to continue their adjustment from current levels (roughly $43 per barrel) to roughly $40 in 2016 Q4 and to remain close to this level in 2017–2019.

The Bank of Russia also has not changed its assumptions regarding general external economic conditions over the three year forecast period. In June-July 2016, international organisations adjusted their global economic growth forecasts slightly downwards[1]. At the same time, taking into account Russia's external trade relations, the Bank of Russia left unchanged its previous GDP growth forecasts for Russia's trading partners, which were based on relatively conservative assumptions: in 2017–2019, they are expected to remain close to 2% p.a.

The monetary policy of most global central banks will be predominantly accommodative, which will help keep interest rates low in global financial markets. Central banks of developed countries (primarily the US Fed) will raise interest rates gradually in view of the pace of economic recovery in these countries and the existing risks of a change in the situation in global markets, including the situation in emerging markets.

The baseline scenario assumes that Russia's country risk premium will stabilise over the forecast period at a relatively low level close to the 2016 average, provided that oil prices do not show considerable fluctuations and international investors are relatively calm in their risk perception.

The international financial sanctions against Russia are expected to remain in effect over the entire forecast period, but their impact on the

[1] *The IMF adjusted its global economic growth forecast downwards from 3.2% to 3.1% in 2016 and from 3.5% to 3.4% in 2017; the World Bank revised its forecasts down from 2.9% to 2.4% in 2016 and from 3.1% to 2.8% in 2017.*

economy will decline. As the results of 2016 Q1 and Q2 showed, the EU and US restrictions are having a diminishing impact on the corporate sector: Russian companies and banks have successfully refinanced most of their external debt and have reduced their foreign liabilities to a lower level than assumed in the external debt repayment schedule.

In terms of domestic financial conditions, in the medium term, as inflation reduces to the 4% target and settles at this level, the Bank of Russia is expected to be able to gradually ease its monetary policy. This will pave the way for lower nominal market interest rates in the economy. Non-price lending conditions are also expected to gradually relax as the overall economic environment improves, which will allow banks to ease their requirements for borrowers and loan collateral, and to gradually expand the range of lending offers. However, interest rates in the economy in real terms will be positive, remaining at a sufficient level to maintain economic agents' balanced approach to distributing income between consumption and savings, and to create the necessary conditions to preserve price and financial stability.

The recovery in lending activity will be gradual. Over the coming year, the growth in lending to the real sector of the economy will continue to be held back by the high overall debt burden, in addition to the relatively tough price and non-price lending conditions. By the end of 2017, the banking sector's loan portfolio is forecast to grow by the total of 4–6% and accelerate to 7–11% in 2018–2019.

In 2017, money supply growth will still outstrip the increase in lending to the economy due to the contribution made by the banking system's net lending to the government. According to estimates, money supply (in national definition) will grow by 7–9% in 2017. In 2018–2019, money supply growth will stabilise in the range of 8–11%, close to the lending growth rate. However, net lending to the government will contribute less to money supply dynamics as the budget deficit decreases as expected.

The uncertainty surrounding the fiscal policy in 2017–2019 remains in the absence of official regulatory decisions. However, in the recent months, the Government of the Russian Federation has announced preliminary agreements regarding the three-year budgeting framework. They assume that the balanced approach to budget expenditures will remain over the forecast period. On the one hand, the amounts of spending will be planned with consideration given to conservative assumptions regarding changes in external conditions, which are having a negative impact on income. On the other hand, restrictions on growth in budget expenditures will be determined based on the objective of further reducing the budget deficit to ultimately balance the budget by 2020. This approach will ensure a safe (from a financial stability perspective) level of government debt and stable government finances, and therefore the financial system as a whole in the medium and long term. In addition, the conservative approach to the indexation of public sector wages and other payments, if maintained, could help maintain stability in inflation expectations and inflation. However, during the consolidation period, fiscal policy will continue to have a moderately constraining influence on economic growth. Given the objective restrictions on increasing budget expenditures, the role of measures aimed at optimising their distribution and structural improvements in the business climate in the economy will increase.

In the medium term, structural restrictions, including those linked to the demographic situation, infrastructural and institutional characteristics of the economy, the persistence of a commodity-oriented economy and insufficient diversification, will continue to constrain economic growth. Past experience in Russia and abroad has shown that overcoming these restrictions can take a long time, which increases the uncertainty surrounding economic growth prospects. Developments in the current situation indicate that the scale and duration of this constraining factor may prove more significant than previously anticipated.

Taking into account the expected changes in external and internal conditions up to the end of 2016 and later in 2017, inflation rates will continue to fall. Quarterly consumer price growth is forecast to stabilise at roughly 4% year-on-year as early as 2017 H1. Annual inflation will gradually fall from 5.5–6.0% in December 2016 to the target level at the end of 2017. The main factors contributing to the slowdown in inflation will be the restrained consumer demand and relatively weak exchange rate dynamics amid the moderately tight monetary policy. Producer price dynamics will contribute to the slowdown in consumer price growth. This will

Table 2.1

Key parameters of the Bank of Russia's baseline forecast

(growth as % of previous year, unless indicated otherwise)

	2016	2017	2018	2019
Urals price, average for the year, US dollars per barrel	40	40	40	40
Inflation, % in December year-on-year	5.5-6.0	4.0	4.0	4.0
Gross domestic product	-(0.7-0.3)	0.5-1.0	1.5-2.0	1.5-2.0
Final consumption expenditure	-(3.5-3.0)	0.2-0.6	1.7-2.2	2.0-2.5
– households	*-(4.0-3.5)*	*0.3-0.7*	*2.4-2.8*	*3.0-3.5*
Gross formation	2.0-3.0	1.8-2.5	3.0-3.7	0.8-1.3
– gross fixed capital formation	*-(6.5-6.0)*	*1.2-1.7*	*2.7-3.2*	*3.2-3.7*
Net exports	12.5-15.6	-1.9-2.2	-3.6-0.5	-3.6-1.0
– exports	*-(1.5-1.0)*	*1.2-1.6*	*1.1-1.6*	*1.3-1.8*
– imports	*-(7.5-7.0)*	*1.6-2.0*	*1.9-2.4*	*2.0-2.5*
Money supply in national definition	9-12	7-9	8-10	9-11
Monetary base in narrow definition	3-5	3-5	4-6	4-6
Loans to non-financial organisations and households in rubles and foreign currency	4-6	4-6	7-9	9-11

chiefly be the result of persistently low energy prices in the absence of significant exchange rate fluctuations and the planned continuation of moderate indexation rates for administered prices and tariffs for the services of natural monopolies. In addition, the expected good grain harvest in Russia in 2016 will have a short-term downward effect on consumer price growth. In the medium term, the anticipated gradual downturn in inflation expectations will be an important factor in stabilising inflation.

At the same time, the realisation of a number of risks primarily linked to the possible retention of high inflation expectations in the long term and changes in household savings behaviour may have an impact on how the situation develops.

The main area of uncertainty at present is the future dynamics of households' propensity to save amid renewed economic growth. A faster increase in household spending on final consumption in this case will create additional inflationary pressure. In addition, the possibility of budget spending rising above the planned levels cannot be entirely ruled out, which will also create preconditions for growth in consumer activity. It should be noted that an increase in economic activity as a result of this factor is unlikely to be sustainable in the long term, for a number of reasons. First, it creates the conditions for inflation to remain high and volatile, which will reduce incentives for investment. Second, given the limited opportunities for rapid import substitution, growth in consumer demand will lead to an expansion of imports and depreciation of the ruble, as well as growing risks to price stability. If signs of these risks present themselves, the Bank of Russia will pursue a tighter monetary policy than envisaged in the baseline scenario.

The fact that inflation expectations are still elevated amid the slowing inflation in 2016 H1 points to a high degree of inertia in these indicators. Existing data on inflation expectation dynamics for August point to some positive shifts, but it is still premature to speak of any stable downward trends emerging. High inertia in expectations in future may be a source of additional pressure. Overcoming this inertia in inflation expectation dynamics is an important objective and may require a tighter monetary policy.

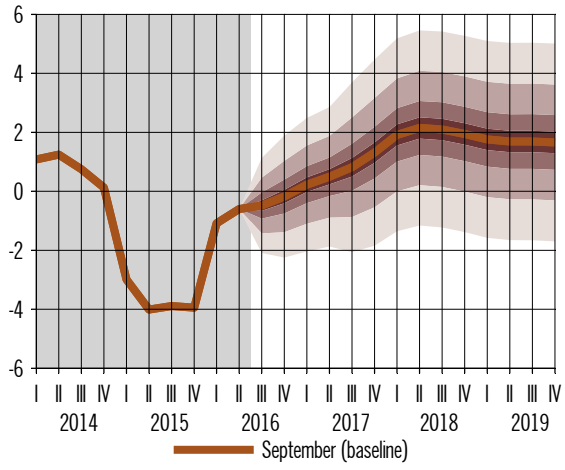
To prevent these risks, in 2017 the Bank of Russia may reduce its key rate at a slower rate than previously anticipated while maintaining a moderately tight monetary policy, meaning that the contribution of monetary policy to restoring demand will be less significant.

Given the above factors, the GDP growth forecast has been revised downwards: in 2017 GDP is expected to grow by 0.5–1.0% compared with growth of 1.1–1.4%, which was previously forecast (Table 2.1). In 2018–2019, in part due to the gradual monetary policy easing and achievement of inflation targets, economic growth will accelerate to 1.5–2% p.a. After a period of renewed economic activity,

Chart 2.2

GDP growth rate

(percent change on corresponding period of previous year)

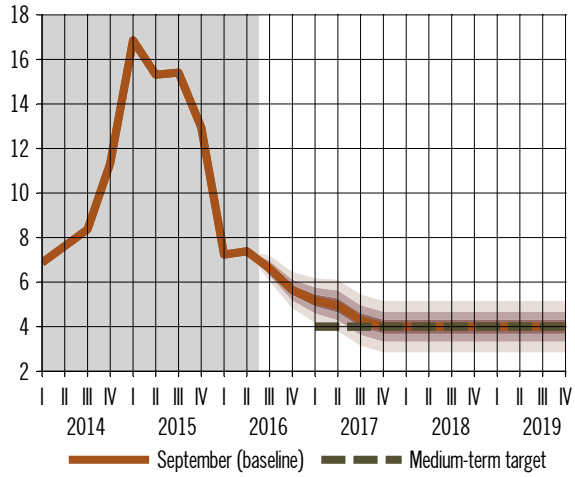


Source: Bank of Russia calculations.

Chart 2.3

Inflation

(percent change on corresponding period of previous year)



Source: Bank of Russia calculations.

GDP growth may again slow to 1–1.5%, which is in line with the medium-term estimates of Russia's economic growth potential taking into account the current structural limitations.

The economic recovery is forecast to be relatively even across all components of aggregate demand. Persistently high savings rates amid positive real rates on deposits will constrain growth in consumer demand. Household spending on final consumption is expected to grow by 0.3–0.7% in 2017, reaching growth of 2.4–3.5% in 2018–2019.

After a long period of decline, investment activity will revive gradually as a result of improved demand dynamics, the reduced corporate debt burden and the gradual easing of lending conditions. Annual gross fixed capital formation growth is expected to be 1.2–1.7% in 2017, accelerating to 2.7–3.7% in 2018–2019. Dynamics of inventories, caused by the anticipated gradual recovery in consumer demand, will make a further contribution to gross capital formation growth in 2017–2018.

External demand for Russian goods amid the restrained global growth, high inventories and relative excess capacity in a number of industries will not provide any significant support for exports. Annual growth in physical exports in 2017–2019 is expected to be 1.1–1.8%. However, the recovery in internal demand which has already begun will cause an increase in physical imports in 2017 by 1.6–2.0% and 1.9–2.5% in 2018–2019. As a result, the contribution of net exports (exports less imports) to GDP in 2017 will fall significantly and, from 2018 onwards, is likely to be negative.

With these dynamics in physical exports and imports of goods and services, and taking into account the stabilisation of energy prices, the current account surplus over the forecast period will gradually shrink (Table 2.2, Annex 'Balance of payments forecast for 2016-2019'). The net outflow of private capital over the forecast period is also expected to remain low (roughly 2% of GDP). The low capital outflow will result from both the gradual reduction in external debt repayments in line with the repayment schedule, and the expanded opportunities to refinance external debt. The positive real interest rates in the economy, promoting investment in ruble-denominated financial assets, will also help maintain low rates of capital outflow. As economic activity recovers, the capital outflow will largely start to be shaped by the increase in foreign assets in the real sector, which, however, will still be significantly lower compared with the level observed in the period 2010–2014.

Considering the moderate demand for foreign assets, current account receipts are expected to be sufficient to repay external debts. As a result, if the baseline scenario is realised, the Bank of Russia will continue to gradually reduce the amount of funds supplied to banks through foreign currency refinancing instruments. Credit institutions' debts on these operations are expected to reduce to zero before the end of 2017.

With the ongoing uncertainty surrounding global economic developments and global financial and commodity markets, the Bank of Russia also

Table 2.2

Russia's balance of payments indicators – baseline scenario
(billions of US dollars)

	2016	2017	2018	2019
Current account	**27**	**27**	**25**	**25**
Balance of trade	91	94	96	101
Exports	*276*	*289*	*301*	*315*
Imports	*-186*	*-194*	*-204*	*-214*
Balance of services	-23	-24	-26	-28
Exports	*50*	*53*	*55*	*57*
Imports	*-73*	*-77*	*-81*	*-85*
Primary and secondary income balance	-41	-44	-46	-48
Capital account	0	0	0	0
Current and capital account balance	**27**	**27**	**25**	**25**
Financial account (net of reserve assets)	**-11**	**-18**	**-25**	**-25**
General government and the central bank	3	0	0	0
Net private capital outflow	-14	-18	-25	-25
Net errors and omission	**-3**	**0**	**0**	**0**
Change in FX reserves («+» – decrease, «-» – increase)	**-13**	**-9**	**0**	**0**

considers optimistic and risk scenarios, alongside the baseline scenario.

The risk scenario assumes that oil prices will fall to $25 per barrel at the end of 2016 and remain close to this level on average until the end of 2019. Such a fall in oil prices could occur either if there are signs of a drastic slowdown in the Chinese economy or if the US Fed accelerates its normalisation of monetary policy, or if supplies from Nigeria or Libya recover quickly, and other oil exporting countries (primarily Iran and Iraq) expand their supply considerably.

Under the risk scenario, deterioration in the terms of trade will cause a stronger economic decline in 2016–2017 compared with the baseline scenario. The adverse impact of the foreign economic situation on the Russian economy will take the form of a drop in income from exports, a decrease in the solvency of borrowers who have outstanding debt in a foreign currency, a deterioration in expectations regarding the Russian economy's growth prospects, and a significant decline in the attractiveness of investments in the Russian economy for domestic and external investors. However, opportunities to support economic activity with fiscal policy in this situation will be extremely limited, given the further reduction in oil and gas tax proceeds and the planned restriction of the budget deficit to ensure the necessary degree of stability for government finances.

At the same time, the increased economic stability in the face of external shocks supported by the corresponding monetary policy responses and fluctuations in the exchange rate needs to be taken into account. This will curb the decline in aggregate output. According to forecasts, GDP could decline by 1.0–1.5% in 2017, reducing to near zero in 2018 and achieving positive growth in 2019.

At the same time, the possible increased volatility in the global and Russian financial markets assumed in this scenario could lead to a sharp deterioration in exchange rate and inflation expectations, which will significantly increase inflation risks and risks to financial stability. Under these conditions, inflation is estimated to remain slightly above 5% in 2017, reaching its target value of 4% in 2018. In order to prevent these risks from snowballing, the Bank of Russia will use both interest rate policy measures and other instruments.

If this scenario materialises, the Bank of Russia will implement a tighter monetary policy than envisaged in the baseline scenario for a longer period of time. In addition, if a negative scenario develops, the Bank of Russia will look into foreign exchange interventions in the event of a threat to financial stability, and increase foreign currency provision to credit institutions on a repayable basis should companies and banks encounter problems in servicing their external debts.

The optimistic scenario assumes a gradual increase in Urals crude oil prices to $55 per barrel in 2019 before stabilising at this level. Such terms of trade could occur if the global economy experiences a faster recovery not accompanied with faster increases (compared with the baseline scenario) in interest rates by central banks around the world (primarily the US Fed).

The impact of improvements in the terms of trade on inflation will vary. On the one hand, the strengthening of the ruble amid the expected rise in oil prices in 2017 H1 will have a moderating effect on inflation. On the other hand, economic agents' increased incomes and decreased uncertainty will support growth in consumer spending, which will have a pro-inflationary effect. Overall, the Bank of Russia estimates that it would be possible to deliver on the inflation target under these conditions with a less tight monetary policy. At the same time, in its key rate decision-making, the Bank of Russia will analyse the relationship between these effects and take action if the balance changes and threatens to cause inflation to deviate from the forecast.

If the preconditions are in place for the optimistic scenario, economic activity is expected to recover more confidently than in the baseline scenario. Apart from improvements in the terms of trade, economic growth will also be buoyed by both external and internal economic agents' revised expectations of the Russian economy's growth prospects.

Since a slight improvement in the external situation alone is not capable of having a significant impact on the medium-term growth potential of the Russian economy, after a period of recovery in 2018–2019, economic growth rates will not exceed the figures set out in the baseline scenario if inflation dynamics and monetary conditions are similar. This period sees a higher risk of excessive optimism among economic agents, which reduces the willingness to undertake structural reforms. The Bank of Russia will assess the situation for signs of overheating in the commodity and credit markets to avert any risks of accelerating inflation, excessive debt growth and destabilisation of financial markets.

This scenario, similar to the baseline one, assumes that credit institutions repay their debts on Bank of Russia refinancing instruments in foreign currency by the end of 2017. Further down the line, the Bank of Russia does not rule out purchasing foreign currency with a view to increasing its international reserves, provided this is not at odds with ensuring price and financial stability. The current account balance relative to GDP and capital outflow relative to GDP will be higher than in the baseline scenario. The higher current account balance over 2017–2019 can be explained primarily by the higher oil prices. The sizeable capital outflow will result from stronger demand for foreign assets in the private sector with the ruble stronger than in the baseline scenario.

Under any of the considered scenarios, the Bank of Russia does not rule out the possibility of additional risks materialising, which could have an impact on inflation performance. Along with changes in external commodity market environment, significant risks to the inflation forecast over the next three years include inflation expectation dynamics and changes in household consumption pattern, surges in internal and external food prices (due to supply-side factors), changes in fiscal policy, including a possible acceleration in the indexation of expenditures or increased taxes, and faster growth in administered prices and tariffs, none of which are incorporated into these scenarios. The required monetary policy response to these risks will be determined taking into account the scale and duration of their effect on inflation processes.

The Bank of Russia will continue to implement a moderately tight monetary policy aimed at reducing inflation and its subsequent stabilisation at the target rate of 4%. To consolidate this stable slowing trend in inflation, according to the Bank of Russia's estimates, the key rate will need to stay at the achieved 10.0% level until 2017 Q1-Q2. In its decision-making, the Bank of Russia will use assessments of medium-term economic growth forecasts, inflation and inflation risks.

ANNEX

Dynamics of major items in the Russian balance of payments in 2016 Q2

In 2016 Q2, the reduction[1] in the current account surplus accelerated compared with Q1. The current account balance shrank by more than 80% compared with 2015 Q2, to a little over $3 billion. However, this reduction was primarily due to differences in the seasonal dynamics of certain current account components: given a trade balance that has fallen year-on-year but has been stable in Q1-Q2, the usual seasonal worsening of the balance of investment income and balance of services had a comparatively stronger impact on the combined current account balance (Chart 1).

The reduction in goods exports slowed slightly in Q2 to 26% compared with 33% in 2016 Q1, as oil prices adjusted. Amid the irregular supplies in a number of exporting countries, Urals crude prices rose compared with Q1 by more than 35%, while the year-on-year fall in prices slowed significantly. However, actual oil exports continued to grow (according to the Russian Federal Customs Service (FCS), by 7.6%), while the reduction in actual exports of petroleum products slowed to 10.7% compared with 16% the previous quarter. As the low base effect disappeared, the amount of exported gas supplies shrank by 3%, following growth of 18% in 2016 Q1.

In turn, as the situation in the economy stabilised, the annual rate of decline in imports decreased rapidly: the value of imports reduced by less than 5% in Q2, compared with 15% in Q1. The smaller decrease in imports was down to the ruble appreciation and the slight improvement in the economic situation. According to FCS data, in 2016 Q2, for the first time in three years, annual growth was registered in imports of machinery, equipment and vehicles, causing their share in total imports to rise from 43% in Q1 to 46% in 2016 Q2. Overall, these export and import dynamics caused a reduction of nearly 50% in the trade balance.

In future, as oil prices stabilise and the recovery in imports slows, trade balance dynamics will also even out.

The balance of services deficit continued to fall quickly year-on-year in Q2, however, it rose slightly compared with Q1 due to the usual seasonal increase in imports of tourism services (this increase was slightly more pronounced than in the previous year). These dynamics – the year-on-year reduction and significant growth compared with the previous quarter – were also exhibited by the deficit from the balance of non-tradable components. This was also due to the specific seasonal dynamics of one of the parts making up the balance of non-tradable components – the balance of investment income. Russian companies traditionally make their dividend payments in June, including to non-resident shareholders, which is reflected in the balance of payments as a sharp one-time increase in investment incomes payable. As a result, amid the relatively stable trade balance in Q1-Q2, the seasonal downturn in the balance of services and non-tradable components led to a short-term drastic reduction in the current account surplus.

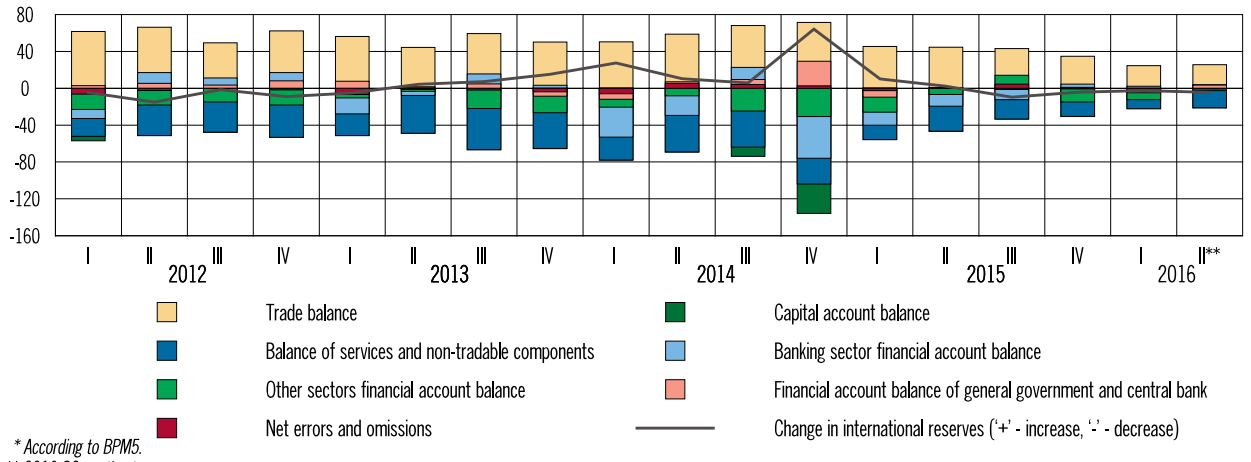
The reduction in the current account surplus did not cause any additional pressure on the foreign exchange market, given that the capital outflow in the form of financing external liability payments or purchasing foreign assets also decreased considerably. Net private capital outflow reduced by more than twofold in 2016 Q2 compared with 2015 Q2, to $5.3 billion[2]. However, despite the limited access to Western capital markets in 2016 Q2 due to sanctions, the outflow developed mainly as a result

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

[2] *Adjusted by the amount of foreign currency liquidity provided by the Bank of Russia to credit institutions on a reverse basis, by the amount of operations in resident banks' correspondent accounts with the Bank of Russia, and also by the amount of funds in foreign currency received by the Bank of Russia as part of FX swaps.*

Chart 1

Major balance of payments components*
(billions of US dollars)



Trade balance
Balance of services and non-tradable components
Other sectors financial account balance
Net errors and omissions
Capital account balance
Banking sector financial account balance
Financial account balance of general government and central bank
Change in international reserves ('+' - increase, '-' - decrease)

** According to BPM5.*
*** 2016 Q2 - estimate.*
Source: Bank of Russia.

of growth in private sector external assets, funded by current account revenues, and the non-financial sector obtaining new loans (banks continued to reduce their liabilities to non-residents). Banks repaid their external debt amid reduced amounts of foreign currency liquidity provided by the Bank of Russia to credit institutions on a reverse basis.

Balance of payments forecast for 2016-2019

Compared with the forecasts in the previous Monetary Policy Report[1], the forecasts of a number of macroeconomic indicators[2] have been revised downwards in the baseline scenario (including economic growth rates) over the three-year period under review. These changes, as well as adjustments to estimates after the release of actual balance of payments data for 2016 Q2, had an impact on the forecast dynamics of the balance of payments items (Charts 1, 2).

Amid the gradual elimination of the irregular supplies from a number of oil exporting countries, and the persistently high commodity reserves, the baseline scenario assumes that oil prices will stabilise at $40 per barrel in 2016 Q4 and remain close to this level on average right up to 2019. As a result, the value of exports in the baseline scenario will reduce in 2016 by almost 20% (the forecast has been revised slightly downwards compared with the previous Report), and in 2017–2019 amid stable oil prices, a gradual increase in exports is expected, primarily due to the moderate growth in external demand and, consequently, actual supply volumes.

In turn, the goods imports forecast has been slightly raised compared with the previous Report, partly due to the marked strengthening of the ruble since the start of 2016. The value of imports will fall in 2016 by less than 5% (after a fall in Q1-Q2, marginally positive growth in imports is expected in the second half of the year) and in subsequent years will grow as demand recovers in line with growth in the Russian economy.

The negative balance of non-tradable components in 2016 will remain low as a result of the fall in external liabilities and the consequent decline in investment income payable. However, amid the assumed improvement in the situation with foreign lending to other sectors (non-financial companies are returning to a net increase in foreign liabilities faster than expected, which means higher external debt), it is expected to grow faster compared with the previous forecast for 2017–2019.

As a result of the steady growth in exports, recovery in imports and slight deterioration of the balance of non-tradable components, the baseline scenario current account balance in 2016 will decrease markedly in nominal terms compared with the previous year and will then remain virtually unchanged at roughly $25 billion, reducing slightly in relative terms from 2.2% of GDP in 2016 to 1.9% of GDP in 2019.

The main component of capital outflow in 2016 will be the continued (amid ongoing international sanctions) settlement of external liabilities by Russian companies and banks. According to the external debt repayment schedule, the total payments by banks and other sectors in 2016 could be roughly $90 billion. However, the actual reduction in private sector liabilities is estimated to be significantly lower: roughly $15 billion. Due to the expected continued growth in liabilities in the form of direct investments[3], intragroup loans, and partial refinancing of debts, the forecast was revised slightly downwards compared with the June Report ($15-20 billion). In future (under the baseline scenario), as the economic situation improves and, consequently, Russia's appeal increases in the eyes of foreign investors, companies' opportunities to use sources not affected by the sanctions will increase. Thus, the amount of capital outflow associated with the net reduction in liabilities will continue to decrease in 2017, and 2018–2019 will see a transition to a net increase in liabilities to the external sector.

In turn, the inflow of capital associated with the reduction in foreign assets (primarily by banks) will virtually halt in 2016 under the baseline scenario. In 2017–2019, it will be replaced with a capital outflow as a result of the gradual growth in demand for foreign assets from the private sector due to the growing incomes of economic agents. However, the financial position of economic agents will not improve to the extent that they can significantly increase the amount of their funds used to acquire foreign assets. Moreover, some liquid foreign assets will be used to fund payments on liabilities, including repayments of banks' outstanding amounts on Bank of Russia FX repos.

---

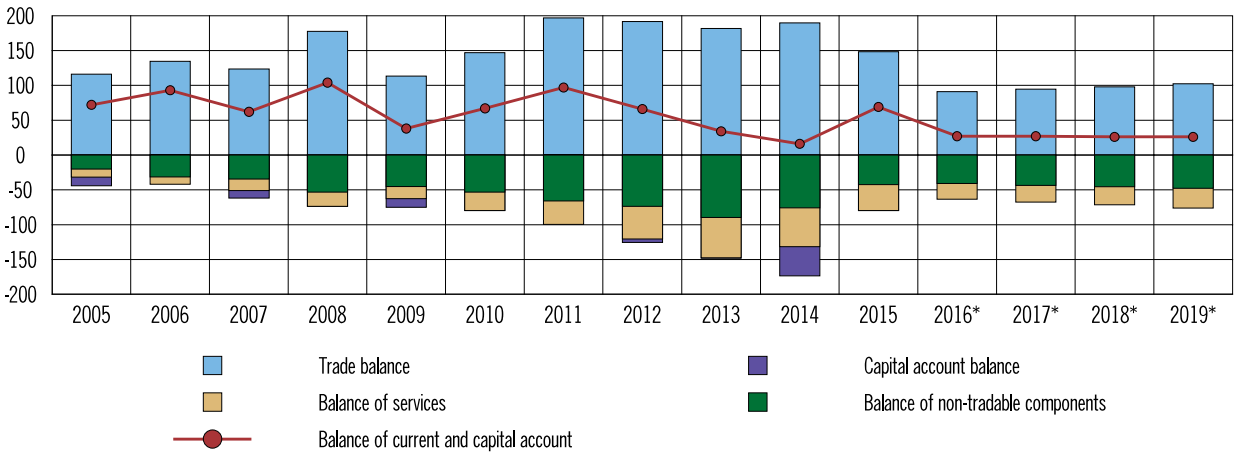
[1] *Monetary Policy Report No. 2 (14), June 2016*

[2] *See Section 2 'Economic outlook and key rate decision'.*

[3] *Including liabilities not associated with debt accumulation (for example, equity holdings in affiliated and subsidiary companies).*

Chart 1

Major current account components
(billions of US dollars)



** Baseline scenario forecast.*
Source: Bank of Russia.

Taking into account the low forecast economic growth and the persistently high appeal of ruble-denominated investments compared with foreign currency investments due to the dynamics of internal interest rates, the growth in demand for foreign assets will be relatively moderate and the capital outflow through this channel will remain comparatively low by historical standards. The capital outflow associated with net demand for foreign assets will, according to Bank of Russia estimates, increase under the baseline scenario from less than $20 billion in 2017 to $40–45 billion in 2019, and from 2017 onwards will again become the main component in the total private capital outflow.

Current account and financial account balance dynamics, as forecast in the baseline scenario, will create the preconditions for an increase in international reserves through the Bank of Russia's removal of foreign currency refinancing operations in 2016–2017.

In the event that the Bank of Russia's risk scenario materialises, in which global oil prices are expected to fall[4], export revenues will be significantly lower than in the baseline scenario. At the same time, lower economic growth rates will also cause lower demand for imported goods compared with the baseline scenario. The fall in export earnings will be greater than the reduction in imports, meaning that a marked decrease in the current account balance is forecast in 2017, before falling more gradually in the years that follow.

The capital outflow under the risk scenario will be significantly higher than in the baseline scenario. The net reduction in liabilities will grow – projects in Russia are becoming less appealing to foreign investors and refinancing existing borrowing and obtaining new loans will be more difficult compared with the baseline scenario. Moreover, amid this new fall in oil prices, volatility in the foreign exchange market may increase and demand for foreign assets among residents may rise. If companies and banks experience difficulties in funding their external debt payments, in 2017–2019, the Bank of Russia might increase its operations to provide foreign currency on a reverse basis in order to avoid risks to financial stability or, if necessary, resort to direct interventions in the foreign exchange market.

Conversely, under the optimistic scenario[5], export earnings will be significantly higher than in the baseline scenario in 2017–2019. However, a faster economic recovery and higher ruble exchange rate compared with the baseline scenario will, at the same time, contribute to accelerated growth in imports. As a result, the current account balance in 2017–2019 will grow and generally be slightly higher than in the baseline scenario.

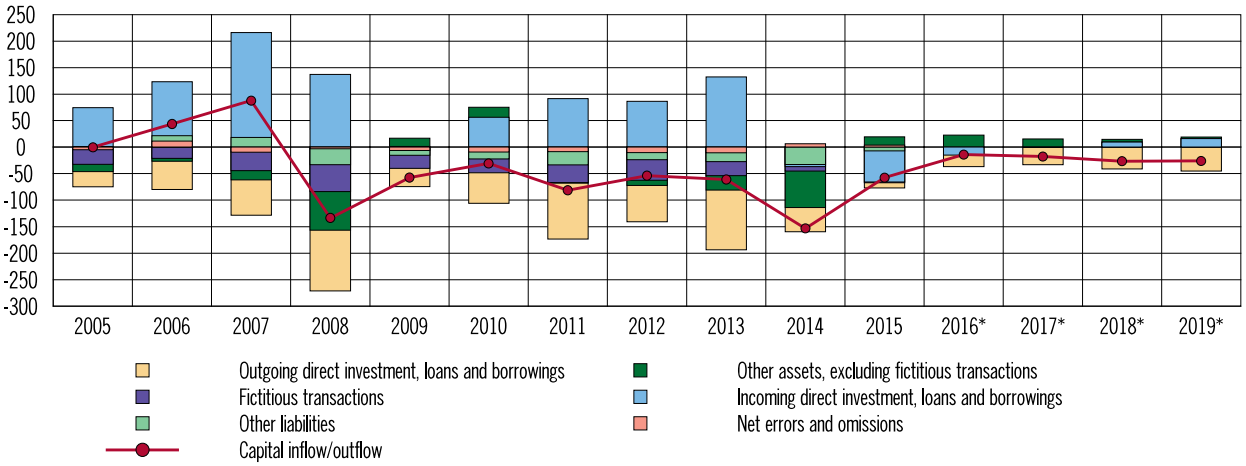
The capital outflow under the optimistic scenario will also increase compared with the baseline scenario. With the higher demand for risky assets in the international financial markets and improved

[4] *See Section 2 'Economic outlook and key rate decision'.*

[5] *See Section 2 'Economic outlook and key rate decision'.*

Chart 2

Capital outflow*
(billions of US dollars)



** Baseline scenario forecast.*
Source: Bank of Russia.

assessments of Russian economic prospects by foreign investors, Russian companies will find it slightly easier to attract foreign liabilities. However, this is expected to be more than offset by growth in economic agents' demand for foreign assets amid their increased incomes. As in the baseline scenario, in 2016–2017, the Bank of Russia will remove its foreign currency refinancing operations, which will lead to an increase in international reserves.

Statistical analysis of differences in economic development of Russian regions

The trend towards decreasing heterogeneity in regions' development, observed in 2016 Q1, remained in Q2. Based on mid-year results, annual growth in the majority of economic indicators in the constituent territories of the Russian Federation moved closer to the Russian average.

The overall recovery in production activity in Russia in the first half of 2016 was reflected by a slight increase in the average annual growth in industrial production in regions amid a reduction in the heterogeneity of the distribution of indicators (Chart 1)[1]. The increase in the number of regions exhibiting positive growth in industrial output was a positive trend. However, the number of regions experiencing a continued slump was still large. The variation in the situations across the regions is to a large degree explained by the differences in their industrial specialisation (Chart 2). In regions with the most competitive mechanical engineering, growth in industrial production accelerated significantly. Output in regions with a diversified production structure and regions specialising in production of raw materials and intermediate goods remained close to the previous year's levels. However, in those regions which are moderately or poorly developed in terms of production potential, the slump in industrial production accelerated.

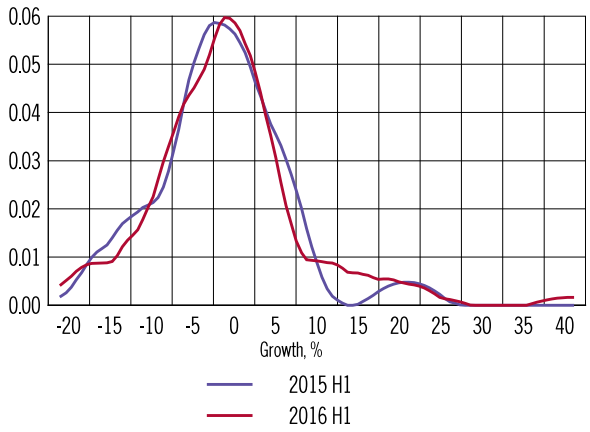
In the first half of 2016, the inequality in nominal wage dynamics across Russian regions was still high (Chart 3). The difference in this indicator's dynamics between regions with the fastest growing incomes and regions with lagging income growth was still significant[2].

Despite the fact that the reduction in the retail trade turnover continued in the first half of 2016,

Chart 1

Distribution of regions by industrial production growth rate

(percent change on corresponding period of previous year)

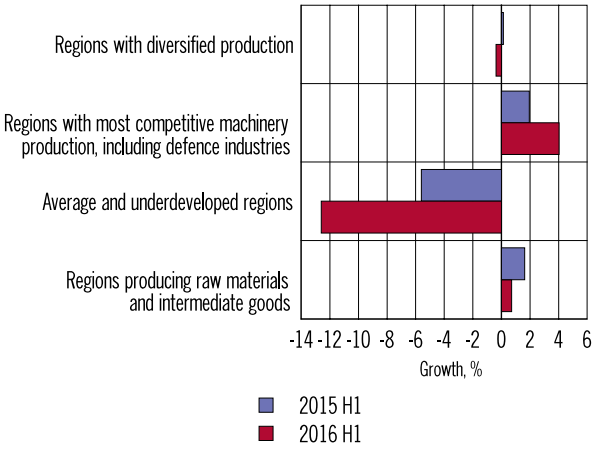


Sources: Rosstat, Bank of Russia calculations.

Chart 2

Industrial production growth by region (grouped by specialisation)

(percent change on corresponding period of previous year)

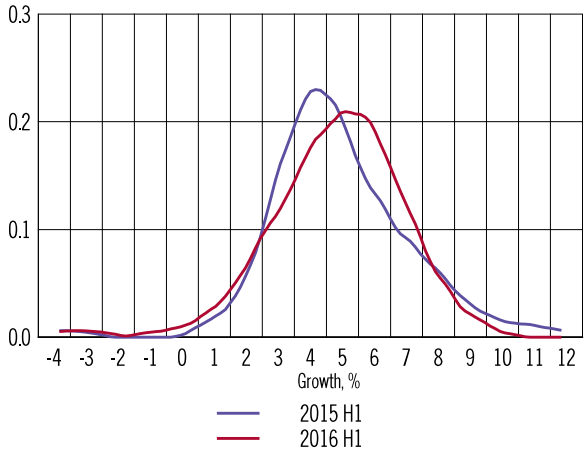


Sources: Rosstat, Bank of Russia calculations.

Chart 3

Distribution of regions by nominal wage growth rate

(percent change on corresponding period of previous year)



Sources: Rosstat, Bank of Russia calculations.

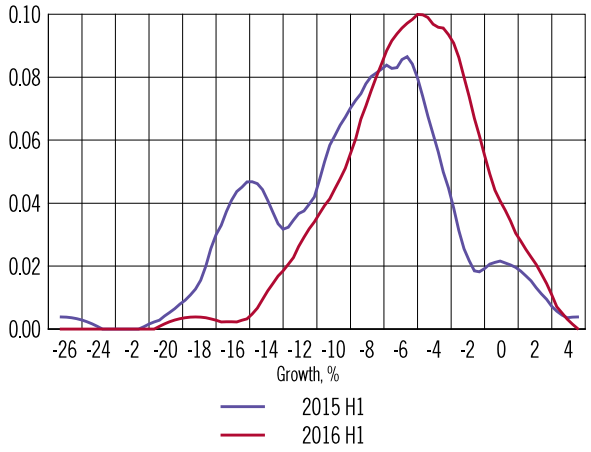
[1] *The Republic of Crimea and the city of Sevastopol have not been included in the totals for the regions due to the lack of data for some indicators for the first half of 2015.*

[2] *The standard statistical features indicate that the shape of the indicator's regional distribution remains: the 'tails' are still long.*

Chart 4

Distribution of regions by retail trade turnover growth rate

(percent change on corresponding period of previous year)

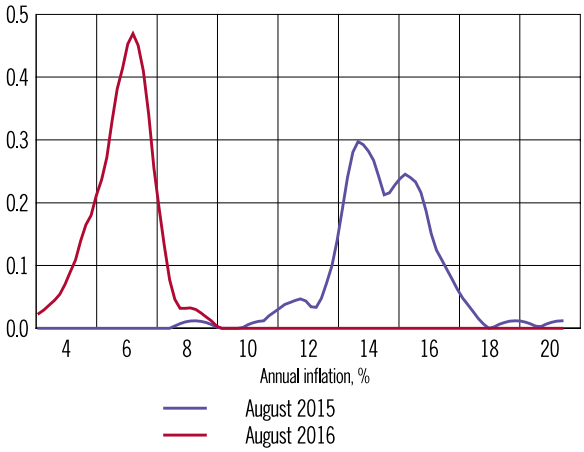


Sources: Rosstat, Bank of Russia calculations.

Chart 5

Distribution of regions by annual inflation

(percent change on corresponding period of previous year)



Sources: Rosstat, Bank of Russia calculations.

the marked decrease in interregional differences compared with the corresponding period of the previous year is a positive trend (Chart 4). The number of regions in which the retail trade turnover shrank by more than 12%[3] decreased by a factor of nine. The number of regions in which the retail trade turnover growth was seen increased, but in most cases this growth was still due to the base effect (given the significant reduction in consumption the year before).

A marked change took place in regional inflation dynamics. With the ongoing slowdown in annual inflation (to 6.9% for Russia as a whole in August 2016), the regional heterogeneity decreased significantly (Chart 5). Disinflationary trends continue to persist in most constituent territories of the Russian Federation, and this could point to the fact that the inflation risks for the country as a whole are not intensifying.

[3] *This is reflected by the disappearance of the distribution's left mode.*

Changes in the system of monetary policy instruments and other Bank of Russia measures

Table 1

Changes in the system of monetary policy instruments and other Bank of Russia measures

Increase in required reserve ratios	From 1 July 2016, the Bank of Russia increased required reserve ratios on credit institutions' foreign currency liabilities by 1 percentage point. This decision was taken as part of measures to discourage growth in foreign currency liabilities in the structure of credit institutions' liabilities. From 1 August 2016, the Bank of Russia increased required reserve ratios on credit institutions' liabilities in rubles and foreign currency by 0.75 percentage points. This measure will allow the Bank of Russia to partially mop up liquidity inflow caused by financing federal budget deficit through the Reserve Fund, as well as be conducive to discouraging growth in foreign currency liabilities in the structure of credit institutions' liabilities.
Changes to the requirements for a minimum rating of the issuer (issue) of securities included in the Bank of Russia Lombard List	Pursuant to the decision of the Bank of Russia Board of Directors of 5 July 2016, requirements for a minimum rating of the issuer (issue) of some categories of securities reincluded in the Bank of Russia Lombard List have been changed. From 8 July 2016, minimum long-term international credit ratings of the issuer (issue) of bonds of legal entities – residents of the Russian Federation, as well as debt issue-grade securities issued by legal entities – non-residents of the Russian Federation outside of the Russian Federation and included in the Bank of Russia Lombard List were increased from B-/B3 to B+/B1 by classification of S&P Global Ratings, Fitch Ratings/Moody's Investors Service. This decision was taken to improve the quality of securities included in the Bank of Russia Lombard List. A decreased structural banking sector liquidity deficit, a reduced demand for refinancing operations from credit institutions and their substantial free market collateral were also taken into consideration.
Changes to certain adjustment ratios used to adjust the value of non-marketable assets	From 1 September 2016, the Bank of Russia changed the adjustment ratios used to adjust the value of non-marketable assets eligible as collateral for Bank of Russia loans pursuant to Bank of Russia Regulation No. 312-P, dated 12 November 2007, 'On the Procedure for Extending Bank of Russia Loans Secured by Assets or Guarantees to Credit Institutions'.
Expansion of the Bank of Russia Lombard List	According to the decisions of the Bank of Russia Board of Directors of 8 July and 26 August 2016, 42 securities issues were added to the Bank of Russia Lombard List.

Table 2

Interest rates on Bank of Russia operations to provide and absorb ruble liquidity

(% p.a.)

Purpose	Type of instrument	Instrument	Term	Frequency	As of 1.01.15	From 2.02.15	From 16.03.15	From 5.05.15	From 16.06.15	From 3.08.15	From 14.06.16	From 16.09.16
Liquidity provision	Standing facilities	Overnight loans; lombard loans; loans secured by gold, non-marketable assets or guarantees; FX swaps (ruble leg); repos	1 day	daily	18.00	16.00	15.00	13.50	12.50	12.00	11.50	11.00
		Loans secured by gold	from 2 to 549 days[1]		18.50	16.50	15.50	14.00	13.00	12.50	12.00	11.50
		Loans secured by non-marketable assets or guarantees			18.75	16.75	15.75	14.25	13.25	12.75	12.25	11.75
	Open market operations (minimum interest rates)	Auctions to provide loans secured by non-marketable assets	3 months[1]	monthly	17.25	15.25	14.25	12.75	11.75	11.25	10.75	10.25
			from 1 to 3 weeks[2]	occasionally								
			18 months[1,2]									
		Lombard loan auctions	36 months[1,2]									
		Repo auctions	1 week	weekly[4]	17.00 (key rate)	15.00 (key rate)	14.00 (key rate)	12.50 (key rate)	11.50 (key rate)	11.00 (key rate)	10.50 (key rate)	10.00 (key rate)
			from 1 to 6 days[3]	occasionally								
		FX swap auctions	from 1 to 2 days[3]									
Liquidity absorption	Open market operations (maximum interest rates)	Deposit auctions	from 1 to 6 days[3]									
			1 week	weekly[4]								
	Standing facilities	Deposit operations	1 day, call	daily	16.00	14.00	13.00	11.50	10.50	10.00	9.50	9.00

[1] Loans provided at a floating interest rate linked to the Bank of Russia key rate.

[2] Operations have been suspended since 1 July 2016.

[3] Fine-tuning operations.

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

Memo item: in 2015, the Bank of Russia refinancing rate was 8.25% p.a. From 1 January 2016, the value of the Bank of Russia refinancing rate equals its key rate as of the respective date. From 1 January 2016, no individual values are set for the refinancing rate.

Source: Bank of Russia.

Statistical tables

Table 1

Bank of Russia operations to provide and absorb ruble liquidity

Purpose	Type of instrument	Instrument	Term	Frequency	Bank of Russia claims on liquidity provision instruments and obligations on liquidity absorption instruments, billions of rubles						
					As of 1.01.15	As of 1.07.15	As of 1.01.16	As of 1.04.16	As of 1.07.16	As of 1.08.16	As of 1.09.16
Liquidity provision	Standing facilities	Overnight loans	1 day	daily	0.0	4.0	0.0	0.0	1.5	0.0	3.7
		Lombard loans			3.7	4.0	2.9	3.2	1.2	1.2	1.3
		FX swaps			121.6	49.9	14.9	0.0	0.0	0.0	0.0
		Repos			96.2	275.9	264.9	192.6	273.7	225.7	362.5
		Loans secured by gold	from 1 to 549 days		1.2	0.5	0.5	0.6	0.0	0.0	0.0
		Loans secured by non-marketable assets or guarantees	from 1 to 549 days		2055.9	335.1	234.8	637.3	242.1	205.3	339.1
	Open market operations	Auctions to provide loans secured by non-marketable assets	3 months	monthly	2370.9	2685.0	1553.8	744.9	219.6	219.6	216.2
			from 1 to 3 weeks[1], 18 months[1]	occasionally							
		Repo auctions	1 week	weekly[2]	2727.6	1572.3	1448.5	650.3	370.7	480.8	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
Liquidity absorption	Open market operations	Deposit auctions	from 1 to 6 days		0.0	0.0	0.0	0.0	0.0	0.0	220.8
			1 week	weekly[2]							
	Standing facilities	Deposit operations	1 day, call	daily	804.5	293.1	557.8	400.9	436.8	392.7	366.4

[1] Operations have been suspended since 1 July 2016.
[2] Either a repo or a deposit auction is held depending on the situation with liquidity.
[3] Fine-tuning operations.

Source: Bank of Russia.

Table 2

Required reserve ratios in 2015-2016

(%)

Liability type	Periods			
	From 1.01.15 to 31.03.16	From 1.04.16	From 1.07.16	From 1.08.16
To households in rubles	4.25	4.25	4.25	5.00
To non-resident legal entities in rubles			4.25	5.00
Other liabilities in rubles			4.25	5.00
To households in foreign currency			5.25	6.00
To non-resident legal entities in foreign currency		5.25	6.25	7.00
Other liabilities in foreign currency				

Source: Bank of Russia.

Table 3

Required reserve averaging ratio

Types of credit institutions	As of 1.01.15	From 10.09.15
Banks	0.7	0.8
Settlement non-bank credit institutions, settlements centres of the organised securities market, and non-bank credit institutions entitled to transfer funds without opening bank accounts and to conduct other related bank operations	1.0	1.0
Non-bank credit institutions performing deposit and lending operations	0.7	1.0

Source: Bank of Russia.

Table 4

Bank of Russia operations to provide foreign currency

Instrument	Term	Frequency	Minimum auction rate as spread to LIBOR[1], pp; fixed interest rate for FX swaps[2],% p.a.					Bank of Russia claims, millions of US dollars						
			As of 1.01.15	From 30.03.15	From 13.04.15	From 21.04.15	From 14.12.15	As of 1.01.15	As of 1.07.15	As of 1.01.16	As of 1.04.16	As of 1.07.16	As of 1.08.16	As of 1.09.16
Repo auctions[3]	1 week	weekly	0.50	1.00	1.50	2.00	2.00	209.8	18.3	100.1	100.0	0.0	0.0	0.0
	28 days							14,900.8	6,623.6	5,016.7	12,109.5	12,955.2	12,189.2	10,919.0
	12 months[4]		0.50	1.00	1.75	2.50	3.00	4,737.3	23,479.2	15,550.0	4,346.6	168.5	164.0	159.6
Loan auctions	28 days	monthly	0.75	1.25	1.75	2.25	2.25	—	440.0	—	0.0	0.0	0.0	0.0
	365 days		0.75	1.25	2.00	2.75	3.25	—	2,526.8	1,494.7	0.0	0.0	0.0	0.0
USD/RUB sell/ buy FX swaps	1 day	daily	1.50	1.50	1.50	1.50	1.50	1,600.0	0.0	0.0	0.0	420.5	0.0	0.0

[1] In respective currencies and for respective terms.
[2] For dollar leg; the rate for ruble leg is equal to the Bank of Russia key rate less 1 pp.
[3] Claims on credit institutions under the second leg of repos.
[4] From 1 June through 14 December 2015 and from 1 April 2016, 12-month FX repo auctions were suspended.

Source: Bank of Russia.

Table 5

Bank of Russia specialised refinancing facilities[1]

Purpose of indirect bank lending	Maturity	Collateral	Interest rate, % p.a.[2]	Bank of Russia claims on credit institutions, billions of rubles							Limit as of 1.09.16, billions of rubles
				As of 1.01.15	As of 1.07.15	As of 1.01.16	As of 1.04.16	As of 1.07.16	As of 1.08.16	As of 1.09.16	
Non-commodity exports	Up to 3 years[3]	Claims under loan agreements secured by contracts of insurance of JSC EXIAR	9.00	—	10.41	39.66	51.01	50.98	52.38	51.46	75.00
Large-scale investment projects[4]	Up to 3 years	Claims under bank loans for investment projects secured by the government guarantees of the Russian Federation	9.00	—	3.68	53.44	74.16	91.02	95.83	99.96	150.00
		Bonds placed to fund investment projects and included in the Bank of Russia Lombard List	9.00	2.85	2.85	2.85	2.85	0.86	0.83	0.83	
Small and medium-sized enterprises	Up to 3 years[3]	Claims under loan agreements of JSC SME Bank[5]	6.50	23.26	23.93	40.10	41.24	43.20	41.24	43.07	75.00
	Up to 3 years	Guarantees of JSC Russian Small and Medium Business Corporation issued under the Programme for Encouraging Lending to Small and Medium-sized Enterprises[6]		—	—	0.08	1.10	8.50	13.36	20.65	
Leasing	Up to 3 years	Claims on loans to leasing companies[7]	9.00	—	—	0.00	0.00	0.00	0.00	0.00	10.00
Military mortgage	Up to 3 years	Mortgages issued under the Military Mortgage programme	10.75	—	10.00	21.01	21.01	29.31	29.31	29.31	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 hamper the achievement of its key objective of ensuring price stability.

[2] For more information on the interest rates on the Bank of Russia's specialised instruments see the section Monetary Policy on the Bank of Russia website.

[3] Until 1 June 2015, the maturity of Bank of Russia loans was from one to 365 days. From 1 June 2015, the maturity of Bank of Russia loans was extended to three years.

[4] 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'.

[5] 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.

[6] The instrument was introduced in June 2015.

[7] The instrument was introduced in December 2015.

Source: Bank of Russia.

Table 6

Consumer prices by group of goods and services

(month on previous month, %)

	Inflation	Core inflation	Food	Food[1]	Vegetables and fruit	Non-food goods	Non-food goods excluding petrol[2]	Services
2014								
January	0.6	0.4	1.0	0.5	5.8	0.3	0.3	0.5
February	0.7	0.5	1.2	0.7	5.1	0.4	0.4	0.4
March	1.0	0.8	1.8	1.3	5.3	0.7	0.6	0.5
April	0.9	0.9	1.3	1.2	2.3	0.6	0.6	0.7
May	0.9	0.9	1.5	1.3	2.4	0.5	0.5	0.8
June	0.6	0.8	0.7	1.1	-2.8	0.4	0.4	0.9
July	0.5	0.6	-0.1	1.0	-8.1	0.4	0.3	1.4
August	0.2	0.6	-0.3	0.9	-10.7	0.5	0.4	0.7
September	0.7	0.9	1.0	1.2	-1.2	0.6	0.5	0.3
October	0.8	0.8	1.2	1.0	2.8	0.6	0.6	0.6
November	1.3	1.0	2.0	1.3	8.7	0.6	0.6	1.2
December	2.6	2.6	3.3	2.2	12.9	2.3	2.5	2.2
Total for the year (December on December)	11.4	11.2	15.4	14.7	22.0	8.1	8.0	10.5
2015								
January	3.9	3.5	5.7	3.7	22.1	3.2	3.5	2.2
February	2.2	2.4	3.3	2.7	7.2	2.1	2.3	0.8
March	1.2	1.5	1.6	1.6	1.2	1.4	1.6	0.3
April	0.5	0.8	0.3	0.9	-3.7	0.9	0.9	0.0
May	0.4	0.6	0.1	0.2	-1.0	0.5	0.6	0.5
June	0.2	0.4	-0.4	0.2	-5.0	0.3	0.3	1.0
July	0.8	0.4	-0.3	0.3	-4.2	0.5	0.3	3.0
August	0.4	0.8	-0.7	0.5	-9.8	0.8	0.7	1.3
September	0.6	0.8	0.4	0.7	-2.3	1.1	1.1	0.0
October	0.7	0.7	1.0	0.8	2.9	1.0	1.1	-0.1
November	0.8	0.6	1.2	0.7	5.6	0.7	0.8	0.2
December	0.8	0.6	1.2	0.6	6.6	0.4	0.5	0.7
Total for the year (December on December)	12.9	13.7	14.0	13.6	17.4	13.7	14.5	10.2
2016								
January	1.0	0.8	1.2	0.6	6.2	0.7	0.8	1.0
February	0.6	0.7	0.7	0.5	2.3	0.8	0.9	0.3
March	0.5	0.6	0.4	0.6	-1.3	0.8	0.8	0.1
April	0.4	0.5	0.4	0.5	-0.1	0.6	0.6	0.3
May	0.4	0.5	0.4	0.3	0.6	0.4	0.4	0.5
June	0.4	0.4	0.1	0.3	-1.1	0.5	0.4	0.6
July	0.5	0.3	0.0	0.5	-4.2	0.4	0.3	1.7
August	0.0	0.4	-0.6	0.4	-8.9	0.4	0.4	0.3

[1] Excluding vegetables and fruit.
[2] Bank of Russia estimate.

Sources: Rosstat, Bank of Russia calculations.

Table 7

Consumer prices by group of goods and services

(month on corresponding month of previous year, %)

	Inflation	Core inflation	Food	Food [1]	Vegetables and fruit	Non-food goods	Non-food goods excluding petrol [2]	Services
2014								
January	6.1	5.5	6.5	6.4	7.7	4.3	4.3	7.8
February	6.2	5.6	6.9	6.5	10.1	4.3	4.3	7.9
March	6.9	6.0	8.4	7.5	15.9	4.6	4.5	8.2
April	7.3	6.5	9.0	8.3	14.4	4.9	4.7	8.5
May	7.6	7.0	9.5	9.5	10.1	5.1	4.9	8.4
June	7.8	7.5	9.8	10.5	3.9	5.3	5.0	8.7
July	7.5	7.8	9.8	11.2	-1.5	5.6	5.2	7.0
August	7.6	8.0	10.3	11.5	-0.8	5.5	5.3	6.7
September	8.0	8.2	11.4	12.0	6.1	5.5	5.3	6.9
October	8.3	8.4	11.5	12.1	5.3	5.7	5.4	7.6
November	9.1	8.9	12.6	12.8	11.1	5.9	5.6	8.7
December	11.4	11.2	15.4	14.7	22.0	8.1	8.0	10.5
2015								
January	15.0	14.7	20.7	18.4	40.7	11.2	11.4	12.3
February	16.7	16.8	23.3	20.8	43.5	13.0	13.5	12.8
March	16.9	17.5	23.0	21.1	38.0	13.9	14.6	12.6
April	16.4	17.5	21.9	20.8	30.0	14.2	15.0	11.8
May	15.8	17.1	20.2	19.5	25.7	14.3	15.1	11.6
June	15.3	16.7	18.8	18.4	22.8	14.2	15.0	11.7
July	15.6	16.5	18.6	17.5	27.9	14.3	15.0	13.4
August	15.8	16.6	18.1	17.0	29.1	14.6	15.3	14.1
September	15.7	16.6	17.4	16.4	27.7	15.2	16.0	13.8
October	15.6	16.4	17.3	16.2	27.9	15.6	16.6	13.1
November	15.0	15.9	16.3	15.5	24.3	15.7	16.7	11.9
December	12.9	13.7	14.0	13.6	17.4	13.7	14.5	10.2
2016								
January	9.8	10.7	9.2	10.2	2.0	10.9	11.4	9.0
February	8.1	8.9	6.4	7.8	-2.7	9.5	9.9	8.5
March	7.3	8.0	5.2	6.7	-5.1	8.8	9.1	8.2
April	7.3	7.6	5.3	6.3	-1.6	8.5	8.7	8.4
May	7.3	7.5	5.6	6.4	0.0	8.4	8.5	8.4
June	7.5	7.5	6.2	6.5	4.1	8.5	8.7	7.9
July	7.2	7.4	6.5	6.7	4.2	8.4	8.7	6.5
August	6.9	7.0	6.5	6.7	5.3	8.1	8.4	5.5

[1] Excluding vegetables and fruit.
[2] Bank of Russia estimate.

Sources: Rosstat, Bank of Russia calculations.

Table 8

Macroeconomic indicators

(seasonally adjusted, growth as % of previous period)

	Industrial production[1]	Agriculture	Construction	Freight turnover	Retail trade turnover	Consumer expenditure	Output index of goods and services by key industries	GDP[2]
2014								
January	0.4	1.0	0.1	0.5	0.0	-1.3	0.8	
February	1.1	0.2	-0.5	-1.8	1.1	1.9	1.4	
March	-0.2	0.1	0.2	-0.9	0.7	0.3	-0.6	-0.1
April	1.5	0.6	0.2	0.3	-0.1	0.2	1.1	
May	0.2	0.2	-0.8	1.7	-0.1	-0.5	0.0	
June	-0.8	0.1	0.5	0.0	-0.1	0.0	-0.3	0.5
July	0.3	2.2	-0.3	-2.6	0.2	-0.1	-0.1	
August	-0.7	-1.7	0.0	0.4	0.1	0.1	-0.4	
September	0.8	0.8	-1.4	0.6	0.3	0.5	-0.3	-0.1
October	0.0	-9.5	0.0	-0.7	0.1	-0.2	-0.3	
November	-1.1	9.9	-1.5	0.2	0.2	0.4	-0.3	
December	1.7	0.6	-0.6	-0.7	1.2	0.8	-0.2	-0.1
2015								
January	-2.4	0.1	-1.1	0.1	-8.8	-7.9	-0.8	
February	-1.6	0.1	-0.7	0.5	-1.3	-0.8	-1.0	
March	0.7	0.5	-0.5	1.0	0.0	-0.3	0.2	-3.2
April	-1.5	0.0	-0.4	-1.2	-0.9	-0.6	-1.2	
May	-0.5	0.1	0.1	-0.6	0.3	0.5	0.2	
June	-0.3	0.3	-0.1	0.2	-0.4	-0.2	-0.5	-0.6
July	0.6	-1.2	-2.8	2.0	-0.4	-0.3	0.0	
August	-0.4	1.4	0.4	-0.7	-0.2	-0.3	-0.2	
September	0.9	0.5	0.1	1.0	-0.7	-0.6	0.4	0.0
October	-0.1	-1.1	-0.7	2.1	-0.4	-0.1	-0.4	
November	-0.6	1.2	0.4	-0.8	-0.6	-0.7	-4.1	
December	0.0	0.5	0.1	-0.2	-0.8	-0.6	0.8	-0.2
2016								
January	0.4	0.0	-1.0	-2.1	-0.5	-0.5	0.6	
February	1.3	0.4	0.6	0.4	0.1	0.3	0.5	
March	-0.5	0.2	-0.8	-0.2	-1.0	-2.9	0.4	-0.3
April	-0.3	0.3	-0.8	-0.1	0.1	2.5	0.1	
May	-0.1	0.3	-1.2	-0.7	-0.8	-0.6	-0.3	
June	0.4	0.1	-0.5	1.3	-0.3	-0.1	0.0	-0.1
July	-0.9	0.9	1.2	1.4	0.0	0.2	0.0	

[1] Rosstat estimate.
[2] Quarterly data.

Sources: Rosstat, Bank of Russia calculations.

Table 9

Macroeconomic indicators

(as % of corresponding period of previous year)

	2015	2016								Memo item: 2015
	Total	January	February	March	April	May	June	July	January-July	January-July
Output of goods and services by key industries	-4.1	-3.5	0.6	-0.5	-0.4	-0.3	-0.4	-1.0	-0.8	-4.2
Industrial output	-3.4	-2.7	1.0	-0.5	0.5	0.7	1.7	-0.3	0.3	-3.0
Agricultural output	3.0	2.5	3.1	2.7	2.7	2.6	2.1	4.9	3.2	0.3
Construction	-7.0	-4.2	0.4	-1.4	-5.9	-9.0	-9.7	-3.5	-5.2	-7.8
Retail trade turnover	-10.0	-6.4	-4.7	-6.2	-4.9	-6.1	-5.9	-5.0	-5.6	-8.5
Household real disposable money income	-4.3	-5.8	-4.3	-1.3	-7.0	-6.2	-4.6	-7.0	-5.3	-3.7
Real wage	-9.0	-3.6	0.6	1.5	-1.1	1.0	1.1	0.6	0.0	-8.9
Number of unemployed	7.4	6.2	0.4	1.4	2.3	0.3	2.1	1.4	2.0	6.5
Unemployment (as % of economically active population)	5.6	5.8	5.8	6.0	5.9	5.6	5.4	5.3	5.7	5.6

Sources: Rosstat, Bank of Russia calculations.

Table 10

Change in Bank of Russia forecasts of GDP[1] growth of Russia's trading partners

(%)

		Forecast of GDP growth in 2016, %		Memo item: country's share in aggregate GDP of trading partners
		May 2016	August 2016	
Total		2.00	1.91	100.0
1	Germany	1.28	1.35	13.67
2	Italy	0.84	0.81	8.95
3	China	6.33	6.41	8.93
4	The Netherlands	1.48	1.37	6.72
5	Turkey	3.16	3.40	6.62
6	Poland	3.65	3.40	4.92
7	Belarus	-1.50	-2.80	4.84
8	Belgium	1.08	1.05	4.50
9	Japan	0.55	0.49	4.42
10	United States	2.16	1.81	4.08
11	France	1.09	1.19	3.89
12	Korea, Republic of	2.47	2.51	3.79
13	United Kingdom	1.94	1.81	3.65
14	Kazakhstan	0.52	0.32	3.58
15	Finland	0.46	0.53	3.33
16	Switzerland	0.92	0.79	2.48
17	Latvia	2.36	2.07	2.44
18	Hungary	2.15	1.76	1.68
19	India	7.33	7.49	1.67
20	Slovakia	3.11	3.03	1.54
21	Czech Republic	2.04	2.13	1.44
22	Lithuania	2.34	2.39	1.44
23	Spain	2.48	2.53	1.42
24	Ukraine	1.30	1.27	0.00

[1] The aggregate GDP growth rate is calculated based on 24 Russia's trading partners which account for more than 1% of Russian exports on average for 5 years (from 2010 to 2014). Previously, the calculation for 2008-2012 was based on 23 countries. The share of each country was determined based on the exports to major trading partners. In this report, the aggregate GDP forecast excludes the economy of Ukraine and includes the re-exports of Russian energy commodities from the Netherlands.

Source: Bank of Russia.

Table 11

Monetary policy rates in various countries

Country	Policy rate	Current level	Date of latest change	Previous level	Change	Number of rate changes over the past 12 months	Inflation	Current level, %	12-month change, pp
Poland	target rate	1.50	04.03.2015	2.00	-0.50	0		-0.8	-0.20
Hungary	base rate	0.90	24.05.2016	1.05	-0.15	3		-0.3	-0.70
Czech Republic	repo rate (14 days)	0.05	01.11.2012	0.25	-0.20	0		0.5	0.00
Romania	base rate	1.75	06.05.2015	2.00	-0.25	0		-0.8	0.89
Bulgaria	base rate	0.00	01.02.2016	0.01	-0.01	1		-0.2	0.00
Serbia	key policy rate	4.00	07.07.2016	4.25	-0.25	4		1.2	0.20
Israel	target overnight rate	0.10	23.02.2015	0.25	-0.15	0		-0.6	-0.31
Brazil	target rate	14.25	29.07.2015	13.75	0.50	0		8.7	-0.82
Chile	monetary policy rate	3.50	17.12.2015	3.25	0.25	2		4.0	-0.60
China	lending rate (12 months)	4.35	26.10.2015	4.60	-0.25	1		1.8	0.20
	deposit rate (12 months)	1.50	26.10.2015	1.75	-0.25	1			
	required reserve rate	17.00	01.03.2016	17.50	-0.50	3			
India	reverse repo rate	6.50	05.04.2016	6.75	-0.25	2		6.1	2.38
	repo rate	6.00	05.04.2016	5.75	0.25	4			
Indonesia	target rate	6.50	16.06.2016	6.75	-0.25	4		2.8	-4.39
Korea, Republic of	base rate	1.25	09.06.2016	1.50	-0.25	1		0.4	-0.30
Malaysia	target overnight rate	3.00	13.07.2016	3.25	-0.25	1		1.1	-2.20
Mexico	target rate	4.25	30.06.2016	3.75	0.50	3		2.7	-0.09
Philippines	monetary policy rate	3.00	03.06.2016	4.00	-1.00	1		1.9	1.10
Russia	repo auction rate (7 days)	10.50	14.06.2016	11.00	-0.50	1		7.2	-8.40
South Africa	repo rate	7.00	17.03.2016	6.75	0.25	3		6.0	1.00
Thailand	repo rate	1.50	29.04.2015	1.75	-0.25	0		0.3	1.48
Turkey	repo rate (7 days)	7.50	24.02.2015	7.75	-0.25	0		8.8	1.98
United States	federal funds rate (upper bound)	0.50	16.12.2015	0.25	0.25	1		0.8	0.60
Euro area	refinancing rate	0.00	10.03.2016	0.05	-0.05	1		0.2	0.10
United Kingdom	base rate	0.25	04.08.2016	0.50	-0.25	1		0.6	0.50
Canada	target overnight rate	0.50	15.07.2015	0.75	-0.25	0		1.3	0.00
Australia	overnight rate	1.50	02.08.2016	1.75	-0.25	2		1.0	-0.50
New Zealand	overnight rate	2.00	11.08.2016	2.25	-0.25	4		0.4	0.00
Denmark	lending rate	0.05	20.01.2015	0.20	-0.15	0		0.1	-0.40
	certificate of deposit rate	-0.65	08.01.2016	-0.75	0.10	1			
Switzerland	3m LIBOR - min	-1.25	15.01.2015	-0.75	-0.50	0		-0.2	1.10
	3m LIBOR - max	-0.25	15.01.2015	0.25	-0.50	0			
Sweden	repo rate	-0.50	11.02.2016	-0.35	-0.15	1		1.1	0.31
Norway	key deposit rate	0.50	17.03.2016	0.75	-0.25	2		4.4	2.60

Note: As of 1 September 2016, changes occurred from the compilation time of the previous Monetary Policy Report issue (8 June 2016) are put in colour.

Source: Bloomberg.

LIST OF BOXES

GLOSSARY

Asset-backed securities (ABS)

Bonds or other securities backed by pooled assets which usually generate predicable cash flows and which are formed by banks or other credit institutions.

Averaging of required reserves

The right of a credit institution to meet reserve requirements set by the Bank of Russia by maintaining a share of required reserves not exceeding the averaging ratio in a correspondent account with the Bank of Russia during a specified period.

Banking sector liquidity

Credit institutions' funds held in correspondent accounts with the Bank of Russia to carry out payment transactions and to comply with the Bank of Russia's reserve requirements.

Bank lending conditions index

A generalised indicator of changes to bank lending conditions, as calculated by the Bank of Russia based on the results of a quarterly survey among leading Russian banks operating in the lending market as follows: (share of banks reporting a significant tightening of lending conditions, as a percentage) + 0.5 x (share of banks reporting a moderate tightening of lending conditions, as a percentage) – 0.5 x (share of banks reporting a moderate easing of lending conditions, as a percentage) – (share of banks reporting a significant easing of lending conditions, as a percentage). Measured in percentage points (pp).

Bank of Russia interest rate corridor (interest rate corridor)

The basis of Bank of Russia interest rate system. The centre of the corridor is set by the Bank of Russia key rate; the upper and lower bounds are rates on overnight standing facilities (deposit facilities and refinancing facilities) symmetric to the key rate.

Bank of Russia key rate

The minimum interest rate at the Bank of Russia 1-week repo auctions and the maximum interest rate at the Bank of Russia 1-week deposit auctions. It is set by the Bank of Russia Board of Directors.

Bank of Russia Lombard List

A list of securities eligible as collateral for Bank of Russia refinancing operations.

Basis point

One hundredth of a percentage point.

Broad money (monetary aggregate M2X)

Total amount of cash in circulation and funds of the Russian Federation residents (non-financial and financial (excluding credit) organisations and households) in settlement, current and other on-demand accounts (including accounts for bank card settlements), time deposits and other types of deposits in the banking system denominated in the currency of the Russian Federation or foreign currency, and interest accrued on them.

Butterfly

An option position including options with the same maturity, whose quotation is calculated according to the formula: BF=(CALL+PUT-2*ATM)/2, where CALL and PUT are implied volatility values for call and put options with the respective deltas, and ATM is an implied volatility value for at-the-money option. This quotation means that the implied distribution of expectations of future exchange rate fluctuations has fatter tails relative to the risk neutral measure.

Carry trade

A strategy in which money is borrowed at a low interest rate in order to invest in higher-yielding assets. This strategy is employed by FX and stock market players to benefit from the positive differentials between active and passive interest rates in different currencies or for different maturities.

CBOE crude oil volatility index

The Chicago Board Options Exchange (CBOE) index calculated by applying the VIX methodology and reflecting the market's expectations of 30-day volatility of crude oil prices.

CDS spread

Premium paid by the CDS buyer to the seller, usually expressed in basis points of the nominal value of the debt and paid with a certain periodicity.

Consumer price index (CPI)

The CPI measures changes over time in the overall price level of goods and services purchased by households for private consumption. This index is calculated by the Federal State Statistics Service as the 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 prices of a previous (reference) period. The CPI is calculated on the basis of data on the actual structure of consumer spending being therefore one of the key indicators of household living costs.

Core inflation

Inflation being measured as a core consumer price index (CCPI). The difference between the CCPI and the consumer price index (CPI) lies in the CCPI calculation method, which excludes a change in prices for individual goods and services subject to the influence of administrative and seasonal factors (fruit and vegetables, fuel, passenger transportation services, telecommunications services, and the majority of housing and public utility services).

Countercyclical currency

A currency which normally faces appreciation in periods of instability in global markets and/or recession in the global economy. Specifically, this type of currencies includes the US dollar, the Japanese yen, and the Swiss franc.

Covered bonds

Bonds secured by payments on mortgage loans or government debt obligations. The difference between covered bonds and asset-backed securities lies in the fact that covered bonds remain on the issuer's balance sheet after the issue, therefore making the issuer liable for the credit risk on the assets which back the bonds.

Credit default swap (CDS)

An insurance contract protecting from default on reference obligations (sovereign or corporate securities with fixed yields). It is a credit derivative allowing the buyer of the contract to get insured against a certain credit event of the reference obligation issuer by paying an annuity premium (CDS spread) to the insurance seller.

Cross-currency basis swap

Currency interest rate swap which implies an exchange of nominal values and interest payments in different currencies. The price of this swap reflects the premium to one of the floating rates.

Current liquidity deficit/surplus

An excess of banking sector demand for liquidity over the liquidity supply on a given day. A reverse situation, an excess of the liquidity supply over demand on a given day, is current liquidity surplus.

Dollarisation of deposits

A share of deposits denominated in foreign currency in total banking sector deposits.

Factors of banking sector liquidity

Changes in the central bank balance-sheet items affecting banking sector liquidity, but which do not result from central bank liquidity management operations. These factors include changes in cash in circulation,

changes in balances of general government accounts with the Bank of Russia, Bank of Russia operations in the domestic foreign exchange market (excluding operations regulating banking sector liquidity), as well as changes in required reserves deposited by credit institutions in required reserve accounts with the Bank of Russia.

Fiscal stress index

Conceptual approach developed by IMF experts proposes an aggregate index which provides early warning signals of risks. The index is calculated on the basis of the study of the signals produced by three complementary sets of variables: basic fiscal variables, long-term fiscal trends, and asset and liability management (the total of 12 variables). Thresholds are calculated for all variables. By exceeding its threshold, the variable signals an upcoming crisis in the following year. Besides, each variable is assigned signaling power which shows its weight in the fiscal stress index. For more information on the approach see Baldacci E., McHugh J., Petrova I. Measuring Fiscal Vulnerability and Fiscal Stress: A Proposed Set of Indicators. IMF Working Paper, No. 94, 2011 and Baldacci E., Petrova I., Belhocine N., Dobrescu G., Mazraani S. Assessing Fiscal Stress. IMF Working Paper, No. 100, 2011.

Floating exchange rate regime

According to the IMF classification, under the floating exchange rate regime the central bank does not set targets, including operational ones, for the level of, or changes to, the exchange rate, allowing it to be shaped under the impact of market factors. However, the central bank reserves the right to purchase foreign currency to replenish international reserves or to influence the domestic FX market occasionally to smooth out the ruble's exchange rate volatility and prevent its excessive deviations.

Floating interest rate on Bank of Russia operations

An interest rate tied to the Bank of Russia key rate. If the Bank of Russia Board of Directors decides to change the key rate, the interest rate applied to the loans previously provided at a floating interest rate will be adjusted by the change in the key rate with effect from the corresponding date.

Foreign exchange swap

A deal which consists of two legs: one party of the deal initially exchanges a certain amount in domestic or foreign currency for an equivalent amount in another currency provided by the second party of the deal. Then, once the deal term has expired, the parties make a reverse transaction (in the corresponding volumes) at a predetermined rate. Foreign exchange swaps are used by the Bank of Russia to provide credit institutions with refinancing in rubles and foreign currency (US dollars).

Forward rate agreement (FRA)

A forward interest rate agreement on a certain future obligation, according to which the parties are bound, as of the effective date, to compensate for the differences in the amount of interest payments calculated on the basis of the agreed and actual rates and the agreed nominal value.

Funds in general government's accounts

Funds in accounts with the Bank of Russia representing funds of the federal budget, the budgets of constituent territories of the Russian Federation, local budgets, government extra-budgetary funds and extra-budgetary funds of constituent territories of the Russian Federation and local authorities.

Generalised (composite) consumer confidence index

Calculated by the Federal State Statistics Service on the basis of quarterly surveys, as an arithmetical mean value of five indices: occurred and expected changes in personal wealth; occurred and expected changes in the economic situation in Russia; and the favourability of conditions for high-value purchases. Partial indices are calculated by drawing up the balance of respondents' estimates (as a percentage). The balance of estimates is the difference between the sum of shares (as a percentage) of decisively positive and 1/2 of the rather positive answers and the sum of shares (as a percentage) of negative and 1/2 of the rather negative answers. Neutral answers are not taken into account.

Gross credit of the Bank of Russia

Includes loans extended by the Bank of Russia to credit institutions (including banks with revoked licences), overdue loans and overdue interest on loans, funds provided by the Bank of Russia to credit institutions through repos and FX swaps (USD/RUB and EUR/RUB swaps).

Implied volatility

A measure of exchange rate volatility that reflects current market prices of FX options under Black-Scholes model (as a rule, at-the-money).

Inflation-neutral output

Total output in economy which may be produced and allocated without setting grounds for changing the price growth rate. Besides, the volume of inflation-neutral output is not linked to any specific level of inflation, it only signals the existence/absence of conditions for its acceleration/deceleration.

Inflation targeting regime

A monetary policy framework setting that the final target of the central bank is to ensure price stability, i.e. achieving and maintaining sustainably low inflation. Under this regime a quantitative inflation target is set and announced. The central bank is responsible for achieving this target. Typically, under an inflation targeting regime, the monetary policy affects the economy through interest rates. Decisions are made primarily on the basis of economic forecasts and inflation dynamics. An important feature of this regime is regular explanations to the public of decisions adopted by the central bank, which guarantees its accountability and transparency.

Interest rate corridor

See Bank of Russia interest rate corridor.

Macro risk index

An index calculated by Citibank and demonstrating the perception of risk level in the global financial markets by investors. The index is bound between 0 (low risk level) to 1 (high risk level). The index is based on the historical dynamics of emerging market sovereign Eurobond yield spreads to the yield spreads of US treasuries, credit spreads on US corporate bonds, US swap spreads, and implied exchange rate, stock index and interest rate volatility.

Managed floating exchange rate regime

Under the managed floating exchange rate regime the central bank does not interfere in the trends of ruble dynamics which are shaped by fundamental macroeconomic factors. No fixed limits or targets are set for the ruble rate, with the central bank seeking to smooth out exchange rate fluctuations in order to support economic agents' gradual adaptation to changes in external economic environment.

MICEX index

Composite index of the Russian stock market calculated by CJSC MICEX Stock Exchange (hereinafter, the Exchange) based on the ruble prices of trades executed in most highly capitalised liquid securities admitted to trading on the Exchange.

MSCI indices

Group of indices calculated by Morgan Stanley Capital International. These are calculated as indices for individual countries (including Russia) and as global indices for various regions, for developed/emerging markets and 'world' index.

Monetary aggregate M1

Total amount of cash in circulation and funds of the Russian Federation residents (non-financial and financial organisations (excluding credit ones) and households) in settlement, current and other on-demand accounts (including accounts for bank card settlements) opened in the banking system in the currency of the Russian Federation and interest accrued on them.

Monetary policy transmission mechanism

The process of transferring the impulse of monetary policy decisions (i.e. decisions made by a central bank in relation to changes to interest rates on its operations) to the economy as a whole and to price dynamics, in particular. The most important channel of monetary policy transmission is the interest rate channel. The impact of the latter is based on the influence of a central bank policy on changes to the interest rates at which economic agents may deposit and raise funds, and, as a result, on decisions regarding consumption, saving and investment and, thereby, on the aggregate demand, economic activity and inflation.

Money supply

Total amount of funds of the Russian Federation residents (excluding general government and credit institutions). For the purposes of economic analysis various monetary aggregates are calculated (see Monetary aggregate M1, Money supply in the national definition (monetary aggregate M2), and Broad money).

Money supply in the national definition (monetary aggregate M2)

Total amount of cash in circulation and funds of the Russian Federation residents (non-financial and financial (excluding credit) organisations and households) in settlement, current and other on-demand accounts (including accounts for bank card settlements), time deposits and other types of deposits in the banking system denominated in the currency of the Russian Federation and interest accrued on them.

Net credit of the Bank of Russia to credit institutions

Gross credit of the Bank of Russia to credit institutions net of correspondent account balances in the currency of the Russian Federation (including the averaged amount of required reserves) and deposit account balances of credit institutions with the Bank of Russia, investments by credit institutions in Bank of Russia bonds (at prices fixed as of the start of the current year), and credit institutions' claims on the Bank of Russia under the ruble leg of FX swaps (USD/RUB swaps).

Net private capital inflow/outflow

The total balance of private sector operations involving foreign assets and liabilities recorded on the financial account of the balance of payments.

Non-marketable assets eligible as collateral for Bank of Russia loans

Promissory notes and credit claims eligible as collateral for Bank of Russia loans in accordance with Bank of Russia Regulation No. 312-P, dated 12 November 2007, 'On the Procedure for Extending Bank of Russia Loans Secured by Assets or Guarantees to Credit Institutions'.

Non-price bank lending conditions

Bank lending conditions aside from the cost of a loan to the borrower, such as maximum loan amount and lending term, requirements for collateral and the financial standing of the borrower.

Non-tradable sector of the economy

Sector of the economy engaged in electricity, gas and water supply, construction, wholesale and retail trade, motor vehicle and motorcycle maintenance, household goods and personal appliance repairs, hotels and restaurants, transport and communications, financial activity, real estate, leasing and services, including other communal, social and personal services.

Open market operations

Operations carried out on the initiative of a central bank. They include auction-based refinancing and liquidity-absorbing operations (repo auctions, deposit auctions, etc.), as well as purchases and sales of financial assets (government securities, foreign currency, and gold).

Output gap

Deviation of GDP from inflation-neutral output, expressed as a percentage. Characterises the balance between demand and supply and may be regarded as an aggregate indicator of the effect which the demand factors have on inflation. If the actual output is larger than the inflation-neutral output (positive output gap), all else equal, inflation is expected to accelerate. A negative output gap is an indicator of an expected slowdown in price growth.

Outstanding amount on Bank of Russia refinancing operations

Outstanding amount on loans extended by the Bank of Russia to credit institutions against the collateral of securities, non-marketable assets, guarantees, gold, repo operations, and FX swaps (USD/RUB and EUR/RUB swaps).

Overnight index swap (OIS)

An interest rate swap where fixed-rate payments are swapped for floating-rate payments set on the basis of overnight money market rates over a respective period of time.

PMI indices

Indicators of business activity based on company surveys in manufacturing and services industries. The PMI index series describe dynamics for the following aspects of business climate: output (or business activity for the services industry), new orders, new export orders, backlogs of work, stocks of finished goods, stocks of purchases, quantity of purchases, suppliers' delivery times, employment, output prices (prices charged for the services industry), input prices, and expectations for activity one year ahead (for the services industry). PMI readings over 50 indicate an expansion of business activity, while readings below 50 suggest a decline.

Procyclical currency

A currency which normally appreciates in periods of global economic growth. Specifically, this category of currencies includes the euro, the Canadian dollar, and the Australian dollar.

Realised volatility

Exchange rate volatility measure calculated on the basis of historical data taken for a given period of time. As a rule, a mean-square deviation of daily logarithmic returns of the exchange rate is assumed to be its realised volatility.

Relative prices

A ratio between CPI subindex and CPI.

Repo operation

A deal which consists of two legs: one party to the deal sells securities to the other party in return for cash, and then, once the deal term has expired, buys them back at a predetermined price. Repos are used by the Bank of Russia to provide credit institutions with liquidity in rubles and foreign currency in exchange for collateral in the form of securities.

Required reserves

Funds maintained by credit institutions in correspondent accounts with the Bank of Russia and accounts to record required reserves in order to fulfill reserve requirements. The latter comprises required reserve ratios and a required reserve averaging ratio.

RGBEY index

RGBEY (Russian Government Bond Effective Yield to Redemption) index reflects an effective yield to redemption of Russian government bonds calculated as an average gross yield to redemption without accounting for bond issue duration.

Risk-neutral measure

A theoretical measure of probability derived from the assumption that the current value of an option is equal to the mathematical expectation of its future payoff discounted at the risk-free rate.

Risk premium on market securities portfolio

Calculated in accordance with the capital asset pricing model as the difference between the yield of a market securities portfolio and the yield of a risk-free asset. The yield of a risk-free asset is, as a rule, taken to be the yield of government securities (for example, OFZ – federal government bonds). Measured in percentage points (pp).

Risk reversal

An option position, whose quotation is calculated as a difference between implied volatility values for call and put options with the respective deltas and same maturities (an option delta is roughly equal to the market participants' estimate of at-the-money option probability). This quotation reflects an asymmetric distribution of expectations of future exchange rate fluctuations relative to the risk-neutral measure.

RTS index

Composite index of the Russian stock market calculated by the Exchange based on the US dollar prices of trades executed in most highly capitalised liquid securities admitted to trading on the Exchange.

Ruble nominal effective exchange rate index

The ruble nominal effective exchange rate index reflects changes in the exchange rate of the ruble against the currencies of Russia's main trading partners. It is calculated as the weighted average change in the nominal exchange rates of the ruble to the currencies of Russia's main trading partners. The weights are determined according to the foreign trade turnover share of Russia with each of these countries in the total foreign trade turnover of Russia with its main trading partners.

Ruble real effective exchange rate index

Calculated as the weighted average change in real exchange rates of the ruble to the currencies of Russia's main trading partners. The real exchange rate of the ruble to a foreign currency is calculated using the nominal exchange rate of the ruble to the same currency and the ratio of price levels in Russia to those in the corresponding country. When calculating the real effective exchange rate, weights are determined according to the foreign trade turnover share of Russia with each of these countries in the total foreign trade turnover of Russia with its main trading partners. The ruble real effective exchange rate index reflects changes in the competitiveness of Russian goods in comparison to those of Russia's main trading partners.

Shadow banking sector

Financial intermediaries providing credit intermediary services whose activity is not regulated by the banking legislation.

Standing facilities

Operations to provide and absorb liquidity carried out by the Bank of Russia on the initiative of credit institutions.

Structural liquidity deficit/surplus

The state of the banking sector characterised by a stable demand by credit institutions for Bank of Russia liquidity provision operations. The reverse situation, characterised by a stable demand by credit institutions to deposit funds with the Bank of Russia, is a structural liquidity surplus. A calculated level of structural liquidity deficit/surplus is a difference between amounts outstanding on Bank of Russia refinancing and liquidity-absorbing operations.

Structural non-oil and gas primary budget deficit

Budget items that are not dependent on the phase of the business cycle and are determined by general government decisions. It is the overall budget deficit, excluding oil and gas revenues, net interest payments, one-off budget revenues, and other items directly dependent on changes in economic activity.

Terms of foreign trade

Ratio between a country's export price index and import price index.

Tradable sector of economy

Economy sector made up of agriculture, hunting, forestry, fishery, fish farming, mining and quarrying, and manufacturing industries.

Underlying inflation

Inflation indicator cleared of all shocks which are irrelevant for the monetary policy. The underlying inflation indicator used by the Bank of Russia is calculated on the basis of dynamic factor models.

US dollar index (DXY)

The DXY is a weighted geometric mean of the US dollar's value relative to a basket of six foreign currencies (EUR, JPY, GBP, CAD, SEK, CHF).

VIX

Calculated by Chicago Board Options Exchange index of expected volatility of S&P 500 stock index over the next 30-day period. VIX is constructed as a weighted average of premiums of a wide range of prices of put and call options on the S&P 500 index.

ABBREVIATIONS

AHML — Agency for Housing Mortgage Lending

BLC — bank lending conditions

bp — basis points (0.01 pp)

BPM6 — the 6th edition of the IMF's Balance of Payments and International Investment Position Manual

Cbonds-Muni — municipal bond index calculated by Cbonds

CCPI — core consumer price index

CIS — Commonwealth of Independent States

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

FPG — fiscal policy guidelines

GDP — gross domestic product

GFCF — gross fixed capital formation

IBL — interbank loans

IEA — International Energy Agency

IFX-Cbonds — corporate bond yield 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)

MICEX SE — MICEX Stock Exchange

MPD — Monetary Policy Department of the Bank of Russia

MTVECM, TVECM — Momentum Threshold Vector Error Correction Model, Threshold Vector Error Correction Model

NPF — non-governmental pension fund

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 — Organisation of the Petroleum Exporting Countries

PJSC — public joint-stock company

PMI — Purchasing Managers' Index

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

TVP FAVAR — Time-Varying Parameter Factor-Augmented Vector Auto-Regression

USA — United States of America

VCIOM — Russian Public Opinion Research Centre

VEB — Vnesheconombank

VECM — Vector Error Correction Model