Bank of Russia

RUSSIA'S ECONOMIC OUTLOOK AND MONETARY POLICY

MARCH 2020

Coronavirus (COVID-19) and oil prices

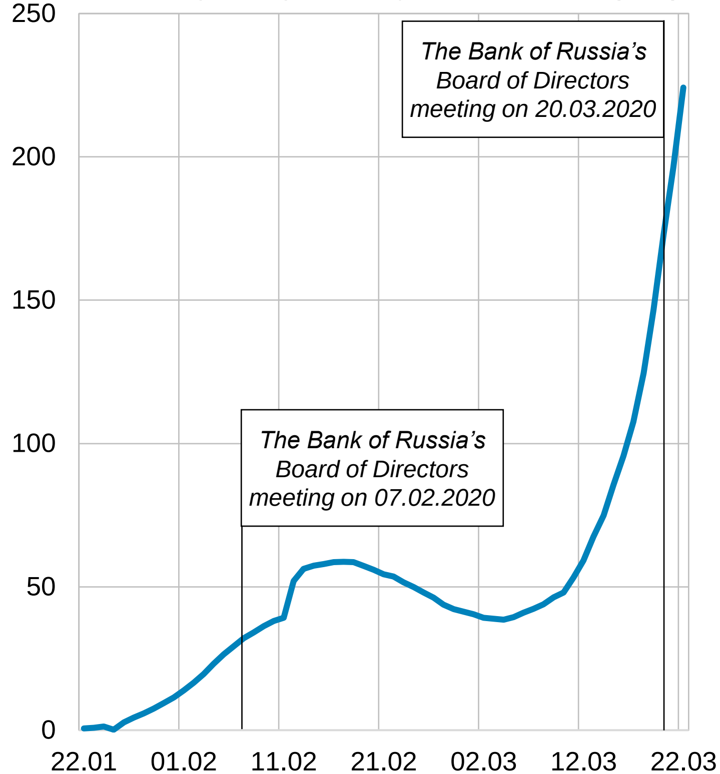
In February — March, the situation has been developing with a significant deviation from the Bank of Russia's forecast under the baseline scenario.

This is related to changes in external conditions:

1) the spread of the coronavirus epidemic;

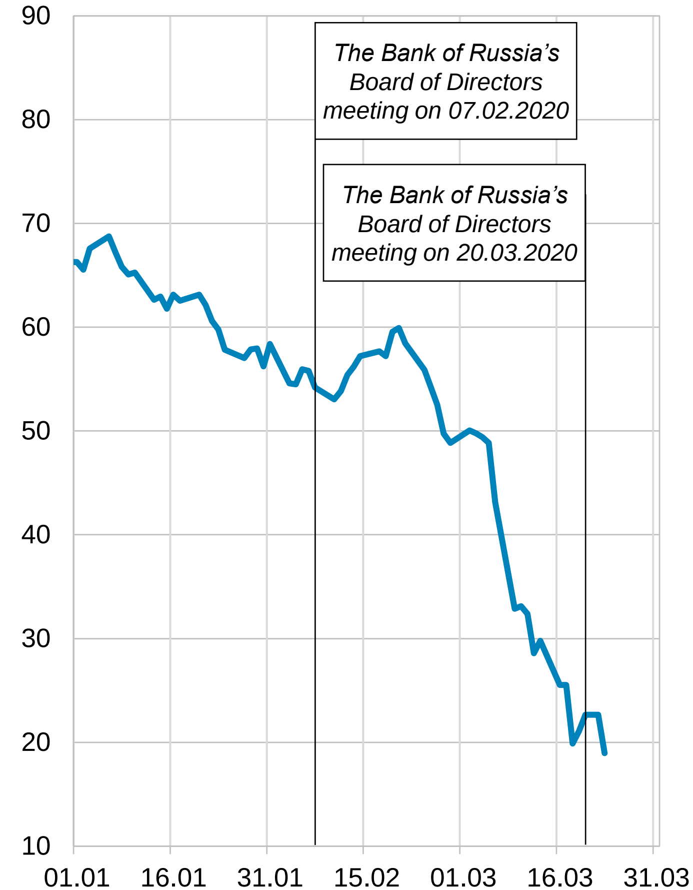
2) a sharp drop in oil prices.

Number of active* COVID-19 cases in the world since the beginning of this year, thousand people



* Total number of active COVID-19 cases = Total number of cases – Total number of recovered and deceased patients

Urals oil price dynamics, USD/bbl



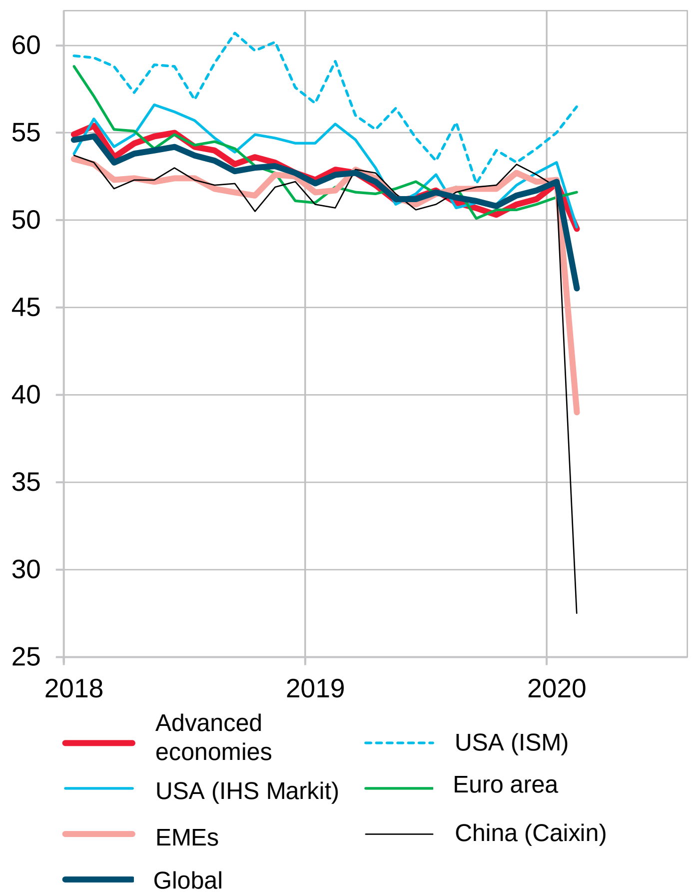
Sources: www.worldometers.info, Thomson Reuters

Global PMI Composite и Manufacturing

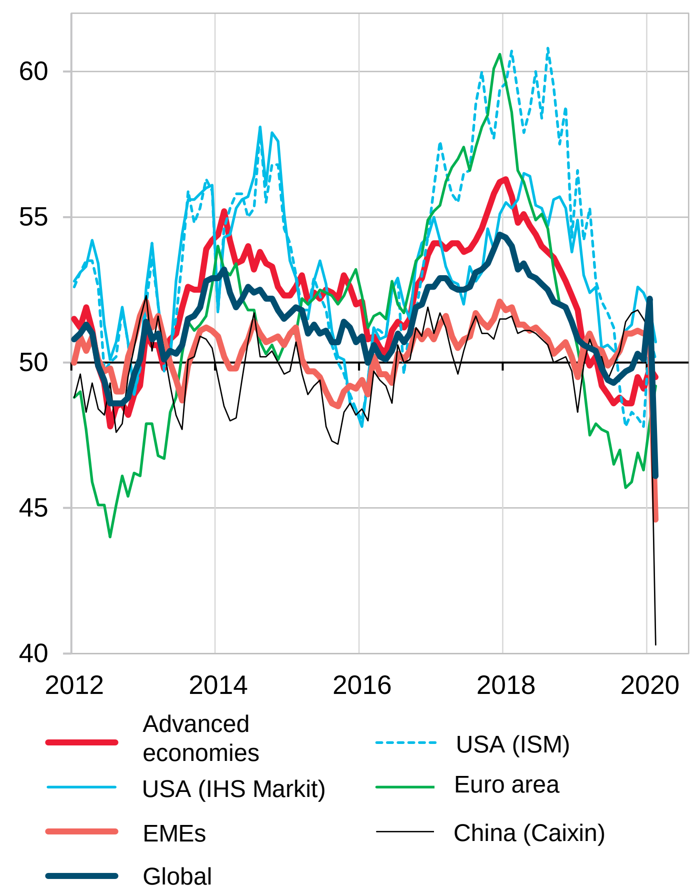
	Feb	Jan
Composite	46.1↓	52.2↑
Manufacturing	47.2↓	50.4↑
Services	49.5↓	52.1↑
Mfg, USA	50.7↓	51.9↓
Mfg, EA	49.2↑	47.9↑

The coronavirus pandemic and measures taken to contain it exert pressure on the global economy, which simultaneously reduces both output and demand, and influences the behaviour of businesses and households.

PMI Composite since 2018



PMI Manufacturing since 2012



Sources: Bloomberg, Thomson Reuters

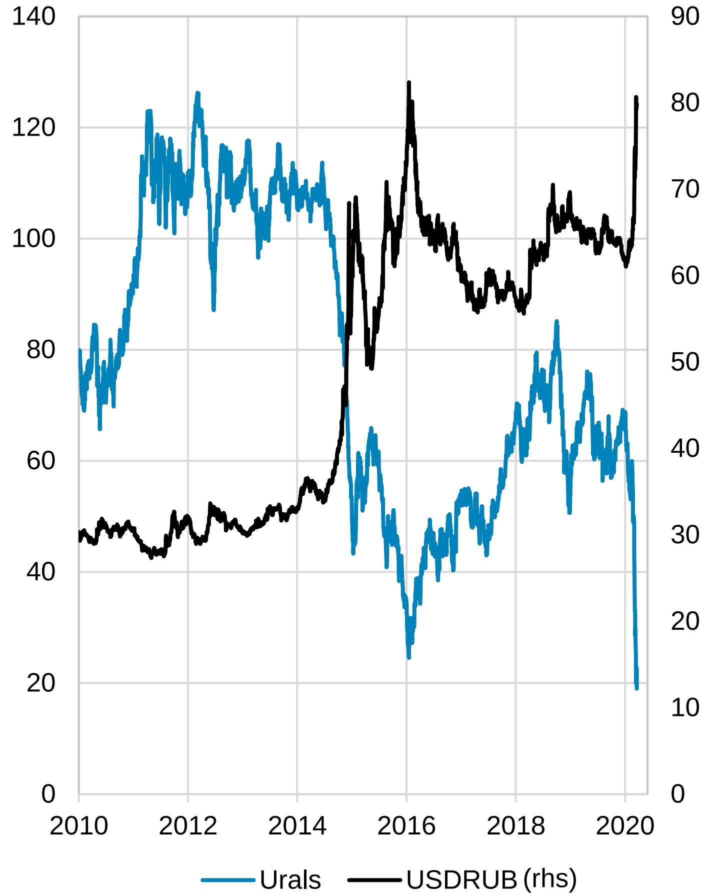
Global financial markets (1)

Volatility in financial markets has surged. The pandemic developments were accompanied by a profound drop in oil prices caused both by a considerable increase in oil production and a considerable decline in its consumption.

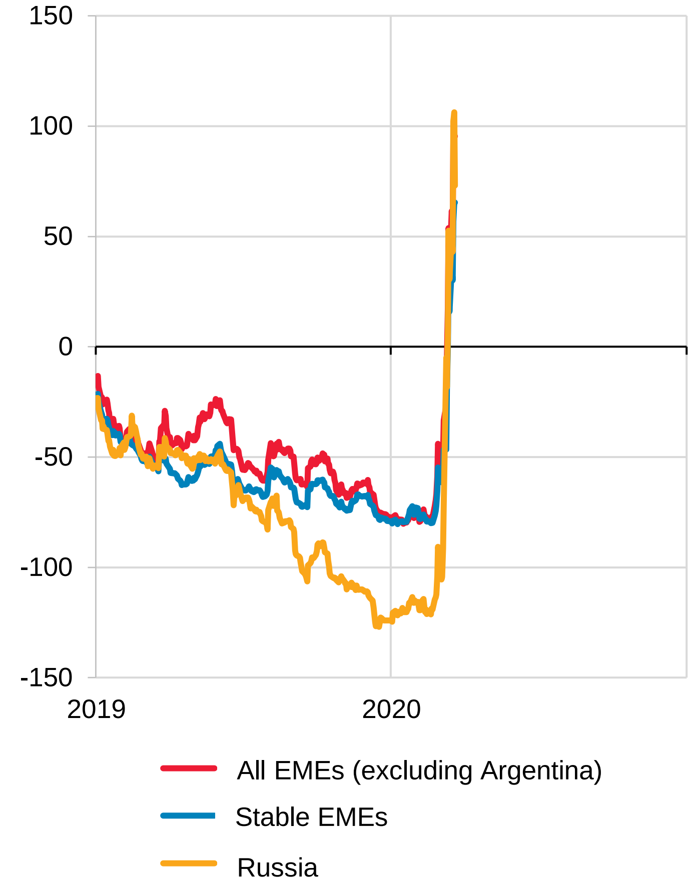
In turn, the slowing of the global economy made investors abandon risky assets. This exacerbated the volatility of capital flows and fluctuations in global financial markets and raised country risk premiums.

Against this backdrop, the ruble weakened in February-March.

Ruble and Urals oil price dynamics



CDS of EMEs (change on 02.01.2017, bp)

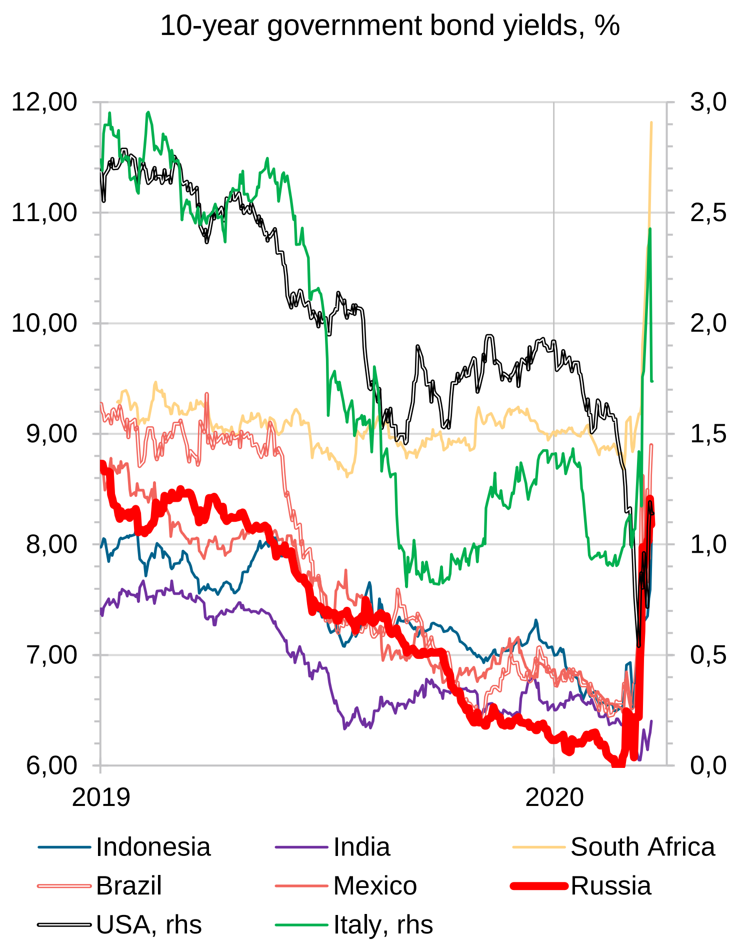


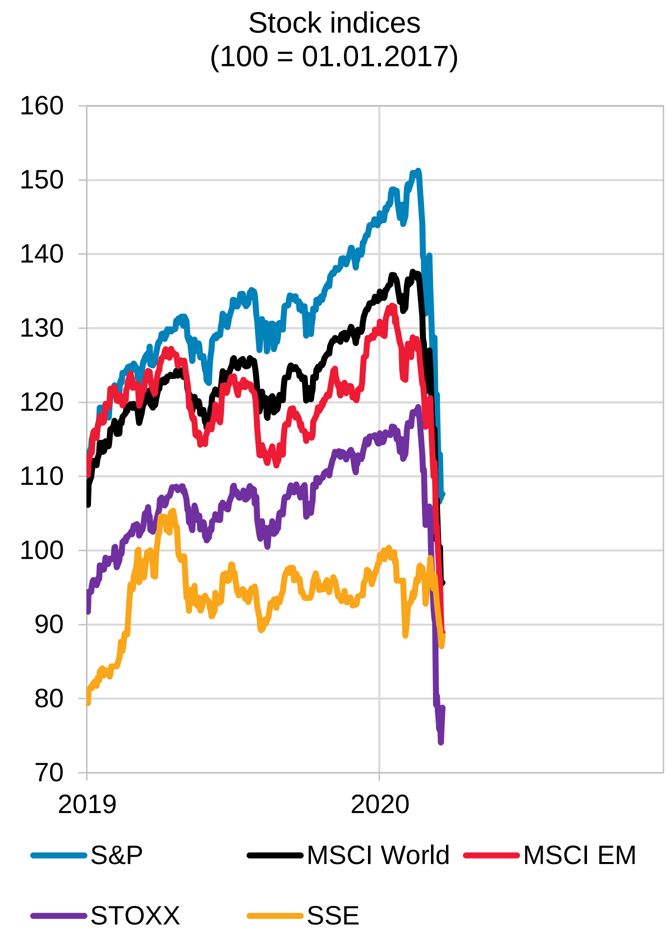
Sources: Reuters, Bloomberg, Bank of Russia calculations

Global financial markets (2)

Against the background of a deteriorating situation in the global economy and an increase in country risk premiums, government bond yields in emerging markets increased, including OFZ yields.

World stock market indices have been falling.





Sources: Reuters, Bloomberg, Bank of Russia calculations

Monetary policy of central banks around the world

In the last few weeks a number of central banks in the countries dominated by disinflationary factors have made decisions to lower interest rates.

Central banks in some advanced economies have relaunched quantitative easing.

	Country	The number of recent consecutive unidirectional changes of the policy rate	Policy rate level	Δ	Consensus on the year-ahead level of the policy rate (at the moment of the decision)	An increase (↑) / decrease (↓) in the rate is expected	Inflation rate (at the moment of the decision)	Consensus on the year-ahead inflation rate (at the moment of the decision)	An increase (↑) / decrease (↓) in inflation is expected	Real interest rate based on inflation over the past 12 months	Real interest rate based on the year-ahead inflation
19.03.2020	Great Britain	(2)	**0,10**	-0,15	0,20	↑	**1,80**	1,50	↓	-1,70	-1,40
19.03.2020	South Africa	(3)	**5,25**	-1	6,15	↑	**4,60**	4,52	↓	0,65	0,73
19.03.2020	Indonesia	(6)	**4,50**	-0,25	4,60	↑	**2,98**	3,20	↑	1,52	1,30
19.03.2020	Australia	(17)	**0,25**	-0,25	0,35	↑	**1,80**	2,00	↑	-1,55	-1,75
18.03.2020	Brazil	(18)	**3,75**	-0,5	4,60	↑	**4,01**	3,58	↓	-0,26	0,17
17.03.2020	Poland	(11)	**1,00**	-0,5	1,50	↑	**4,70**	2,70	↓	-3,70	-1,70
17.03.2020	Turkey	(6)	**9,75**	-1	9,75	→	**12,37**	9,15	↓	-2,62	0,60
16.03.2020	Chile	(4)	**1,00**	-0,75	1,55	↑	**3,89**	3,40	↓	-2,89	-2,40
16.03.2020	New Zealand	(10)	**0,25**	-0,75	0,60	↑	**1,90**	1,85	↓	-1,65	-1,60
15.03.2020	USA	(5)	**0,25**	-1	0,70	↑	**2,30**	2,00	↓	-2,05	-1,75
12.03.2020	Norway	(1)	**1,00**	-0,5	1,55	↑	**0,90**	2,10	↑	0,10	-1,10
11.03.2020	Great Britain	(1)	**0,25**	-0,5	0,65	↑	**1,80**	1,70	↓	-1,55	-1,45
04.03.2020	Canada	(1)	**1,25**	-0,5	1,60	↑	**2,40**	1,90	↓	-1,15	-0,65
03.03.2020	Australia	(16)	**0,50**	-0,25	0,35	↓	**1,80**	2,00	↑	-1,30	-1,50
03.03.2020	USA	(4)	**1,25**	-0,5	1,65	↑	**2,50**	2,00	↓	-1,25	-0,75
20.02.2020	Indonesia	(5)	**4,75**	-0,25	4,70	↓	**2,68**	3,20	↑	2,07	1,55
19.02.2020	Turkey	(5)	**10,75**	-0,5	9,90	↓	**12,15**	9,70	↓	-1,40	1,05
14.02.2020	Mexico	(5)	**7,00**	-0,25	6,25	↓	**3,24**	3,60	↑	3,76	3,40
10.02.2020	Russia	(5)	**6,00**	-0,25	5,90	↓	**2,40**	3,75	↑	3,60	2,25
05.02.2020	Thailand	(3)	**1,00**	-0,25	1,20	↑	**1,10**	1,40	↑	-0,10	-0,40
05.02.2020	Brazil	(17)	**4,25**	-0,25	5,05	↑	**4,31**	3,60	↓	-0,06	0,65
22.01.2020	Malaysia	(2)	**2,75**	-0,25	2,80	↑	**1,00**	1,30	↑	1,75	1,45
16.01.2020	Turkey	(4)	**11,25**	-0,75	10,25	↓	**11,84**	9,70	↓	-0,59	1,55
16.01.2020	South Africa	(2)	**6,50**	-0,25	6,35	↑	**3,60**	4,81	↑	2,90	1,69

Sources: Bloomberg, Bank of Russia calculations

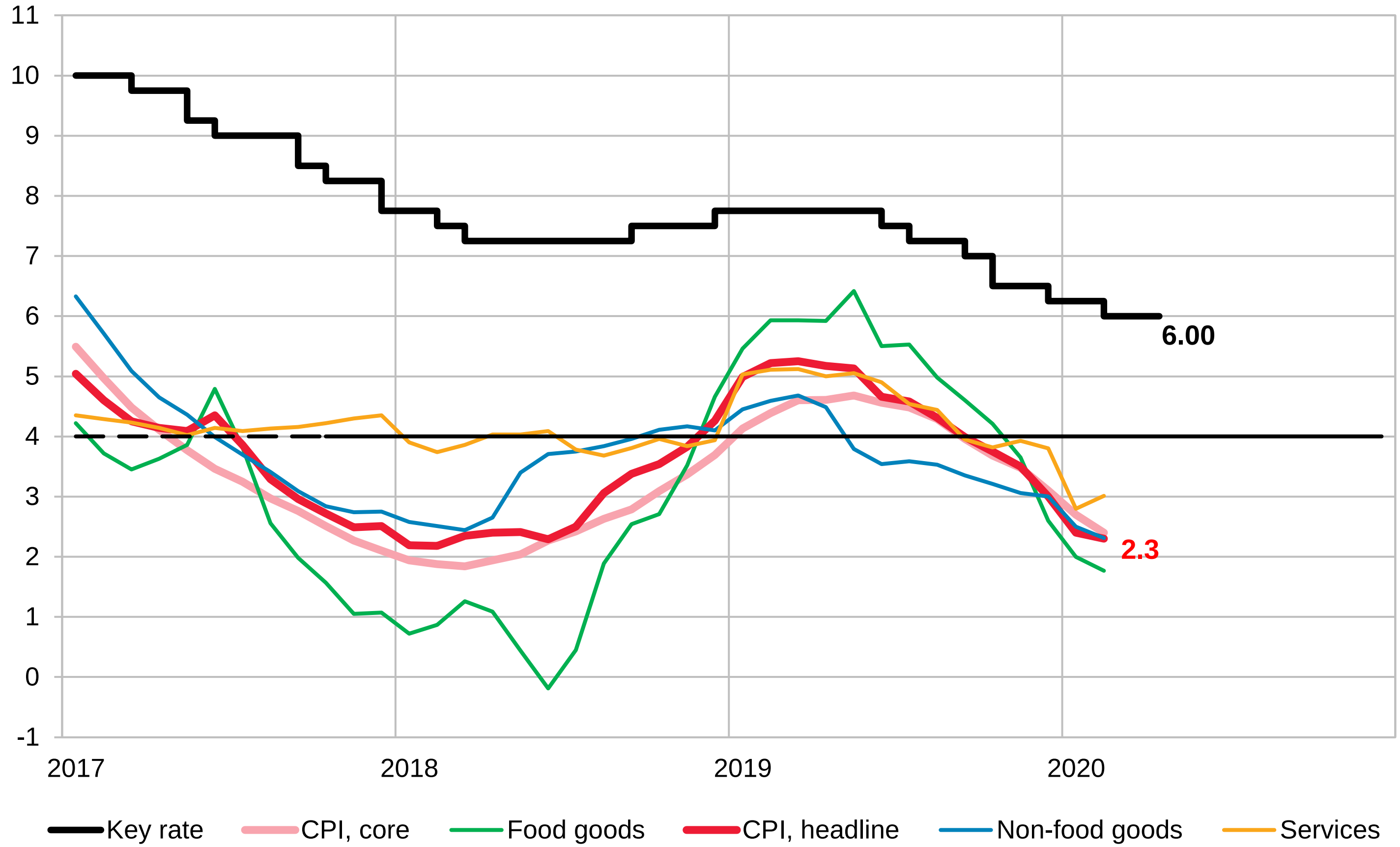
Consumer prices

	Jan	Feb	Δ,pp
CPI, headline	**2.4**	**2.3**	**-0.1**
CPI, core	**2.7**	**2.4**	**-0.3**
Median	**2.5**	**2.4**	**-0.1**

The ruble’s depreciation is a temporary pro-inflationary factor. It might prompt annual inflation to exceed the target level this year. However, the dynamics of domestic and external demand will exert a meaningful constraining influence on inflation on the back of a pronounced slowdown of global economic growth and increased uncertainty.

Given the current monetary policy stance, annual inflation will return to 4% in 2021.

Inflation by main groups, core inflation (% YoY) and the Bank of Russia key rate (% p.a.)



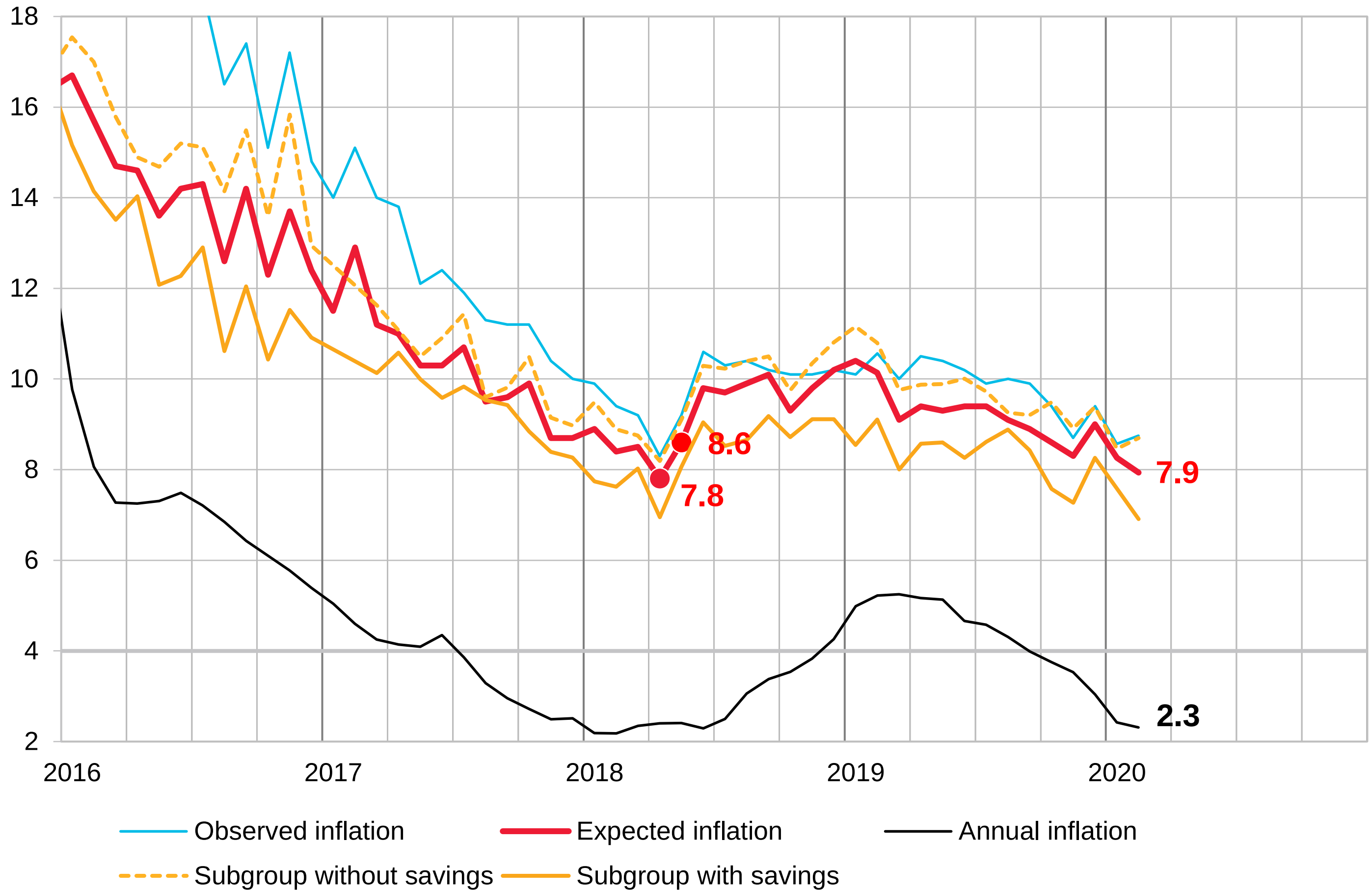
Sources: LLC “inFOM”, Rosstat

Inflation expectations – households

	Mar 20,%	MoM, pp
Observed	**8.3**	**-0.4**
Expected	**7.9**	**0.0**
- with savings	**6.9**	**0.0**
- w/out savings	**8.5**	**-0.2**

The observed weakening of the ruble and the consecutive acceleration of consumer price growth rates may cause a temporary rise in inflation expectations of households and businesses.

Inflation observed and expected by households, median estimate, %



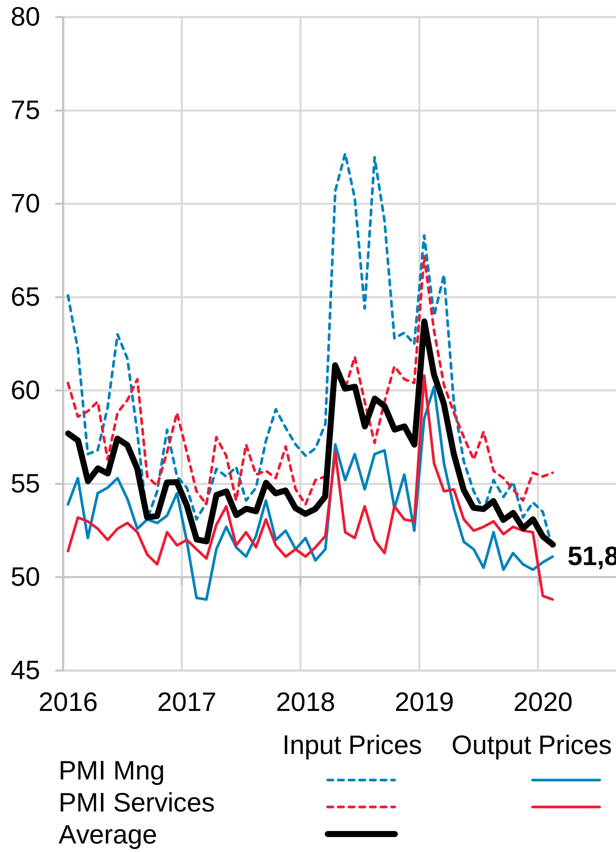
Sources: LLC “inFOM”, Rosstat

Price expectations – businesses

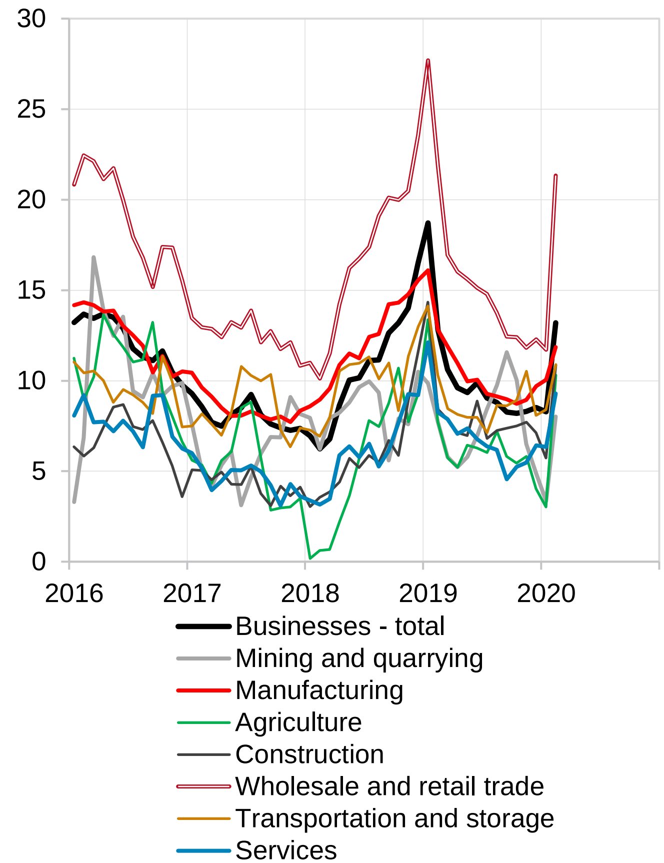
	Feb	Jan	Δ, p.
Mfg Input	**51.5**	**53.5**	**-2.0**
Mfg Output	**51.1**	**50.8**	**0.3**
Serv. Input	**55.6**	**55.4**	**0.2**
Serv. Output	**48.8**	**49.0**	**-0.2**

According to the Bank of Russia's survey, a significant increase in the price expectations of businesses in February is in part caused by the increased uncertainty of external conditions.

PMI survey data on producer input and output prices, diffusion index, pp



Replies of businesses to the question: "How will the prices of final goods change in the upcoming 3 months (increase/decrease)?", balance of replies, % SA



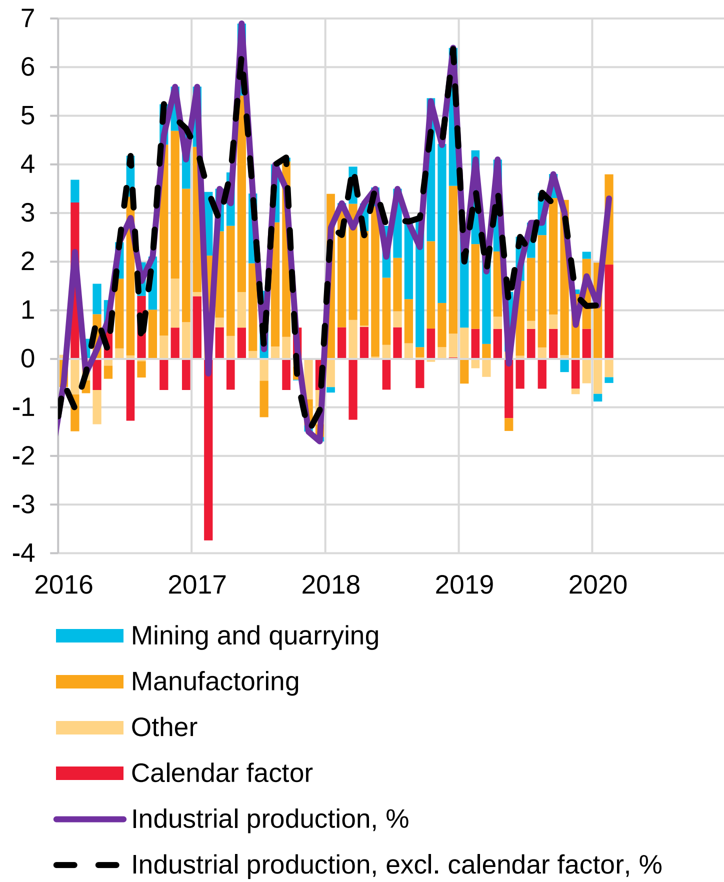
Sources: Bank of Russia's business survey, IHS Markit

Industrial production and investment activity

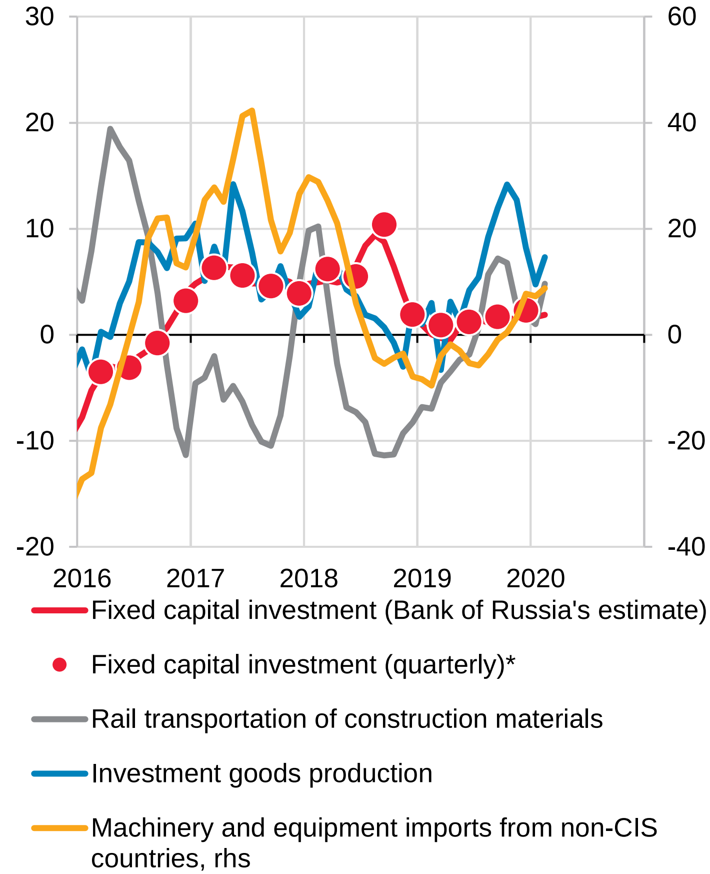
Under the influence of negative external factors, the moderate growth of the Russian economy at the beginning of the year might change to a downturn of the economic activity in the coming quarters.

The Russian economy's growth path will in many ways depend on the scale of the fallout from the further spread of the coronavirus and the action to counter it, alongside with the impact of this action on production, demand and business and consumer sentiment.

Industrial output, contribution to annual growth, pp



Investment activity indicators, % YoY 3MMA



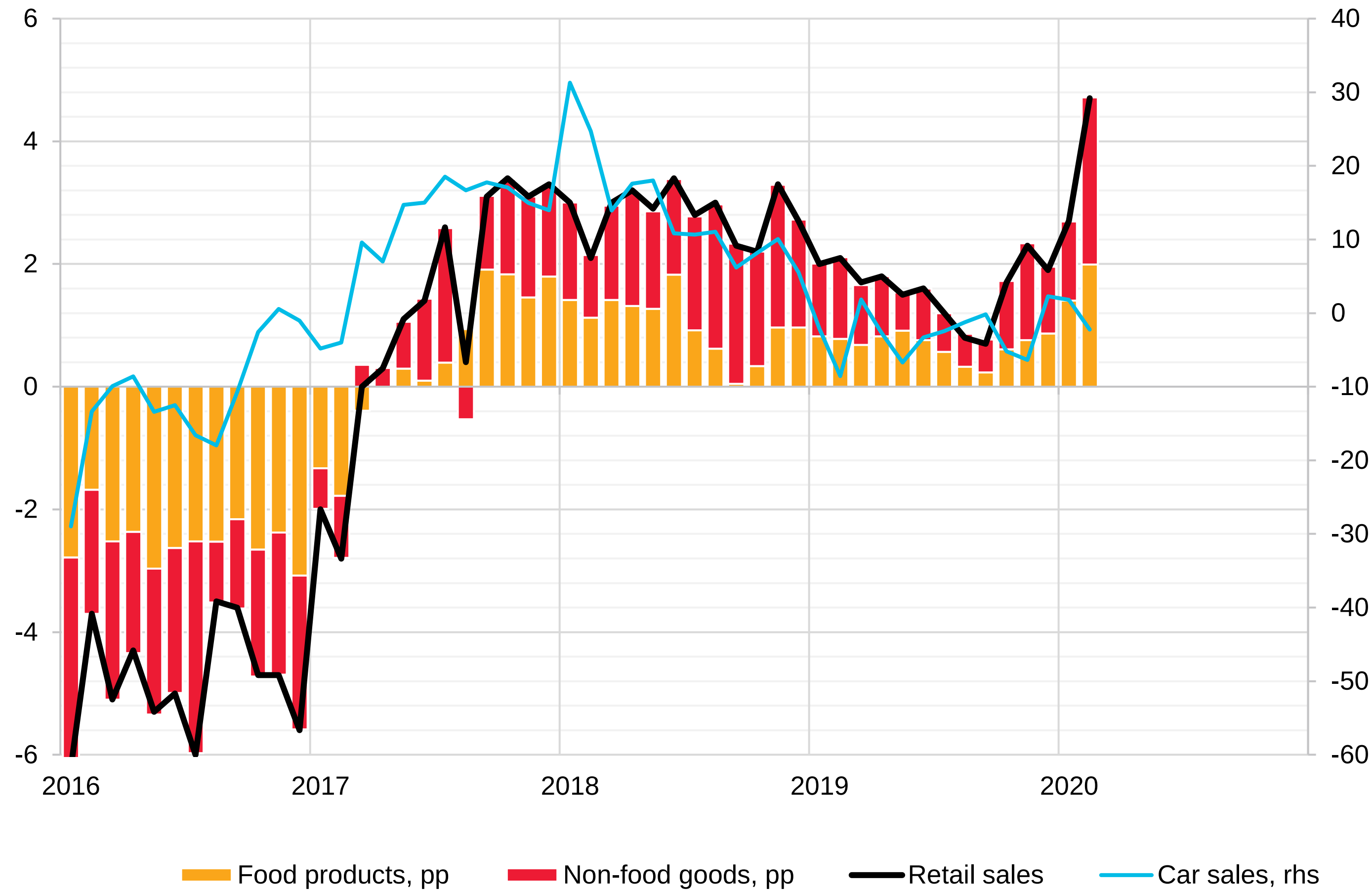
** In % to the corresponding period of the previous year*

Sources: Rosstat, Bank of Russia's estimates

Retail sales

A temporary increase in current demand for a number of products and services, triggered by consumers' drive to accumulate stocks, may have a short-term pro-inflationary effect.

Retail trade turnover, % YoY



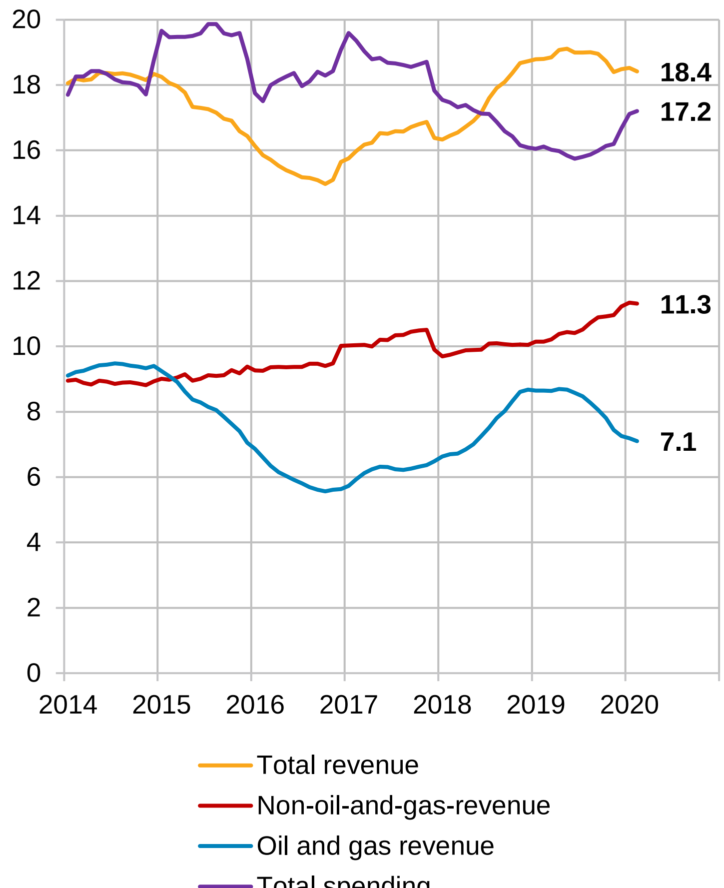
Sources: Rosstat, Bank of Russia's estimates

Fiscal policy

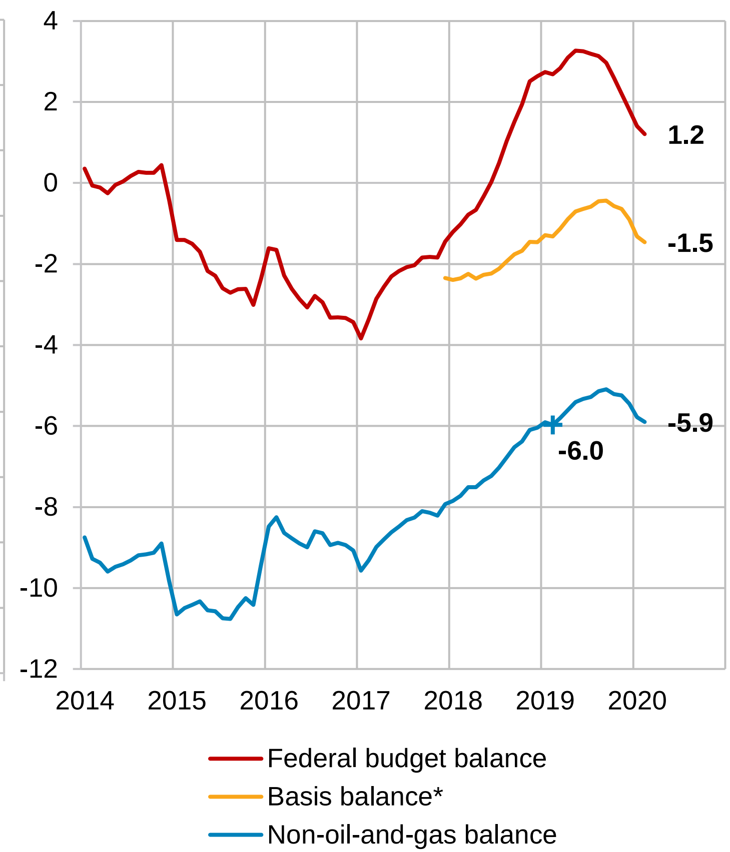
The Russian economy will gain support from the package of the Government and the Bank of Russia's economic measures to counter the consequences of the coronavirus pandemic and financial market volatility

Domestic demand is set to receive a boost this year from additional social policy measures announced in January, as well as the national projects being implemented as scheduled.

Federal budget revenue and spending,
12-month moving sum, as % of GDP



Federal budget balance,
12-month moving sum, as % of GDP



*Basis balance is an indicator of the budget policy calculated by the Ministry of Finance:
basis balance = basis oil and gas revenue + non-oil-and-gas revenue – total spending.

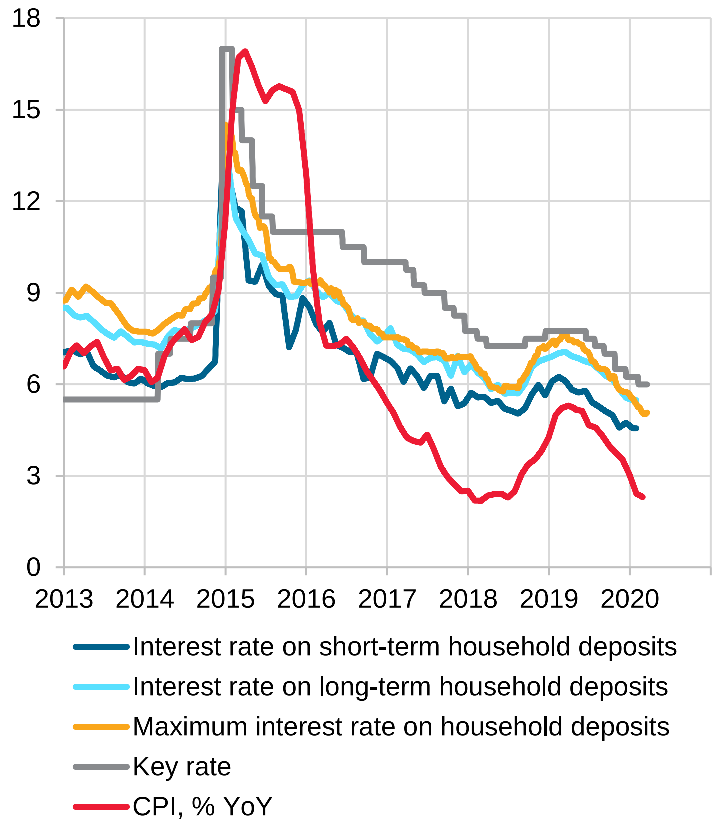
Source: Federal Treasury

Deposit and credit market – interest rates

Monetary conditions have tightened under the influence of negative external factors.

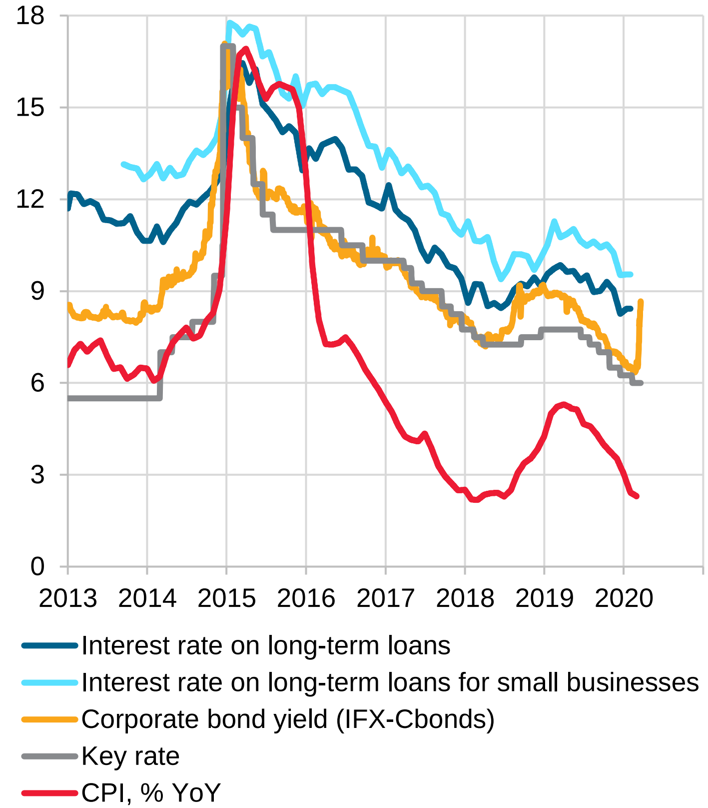
OFZ and corporate bond yields have increased. Certain banks have started to raise their loan and deposit interest rates.

The dynamics of interest rates on household ruble deposits, % per annum



** Average of maximum declared one-year deposit interest rates (for deposits in top 10 banks amounting to 100 000 RUB, Monetary policy department estimate)*

The dynamics of interest rates on corporate loans in rubles, % per annum

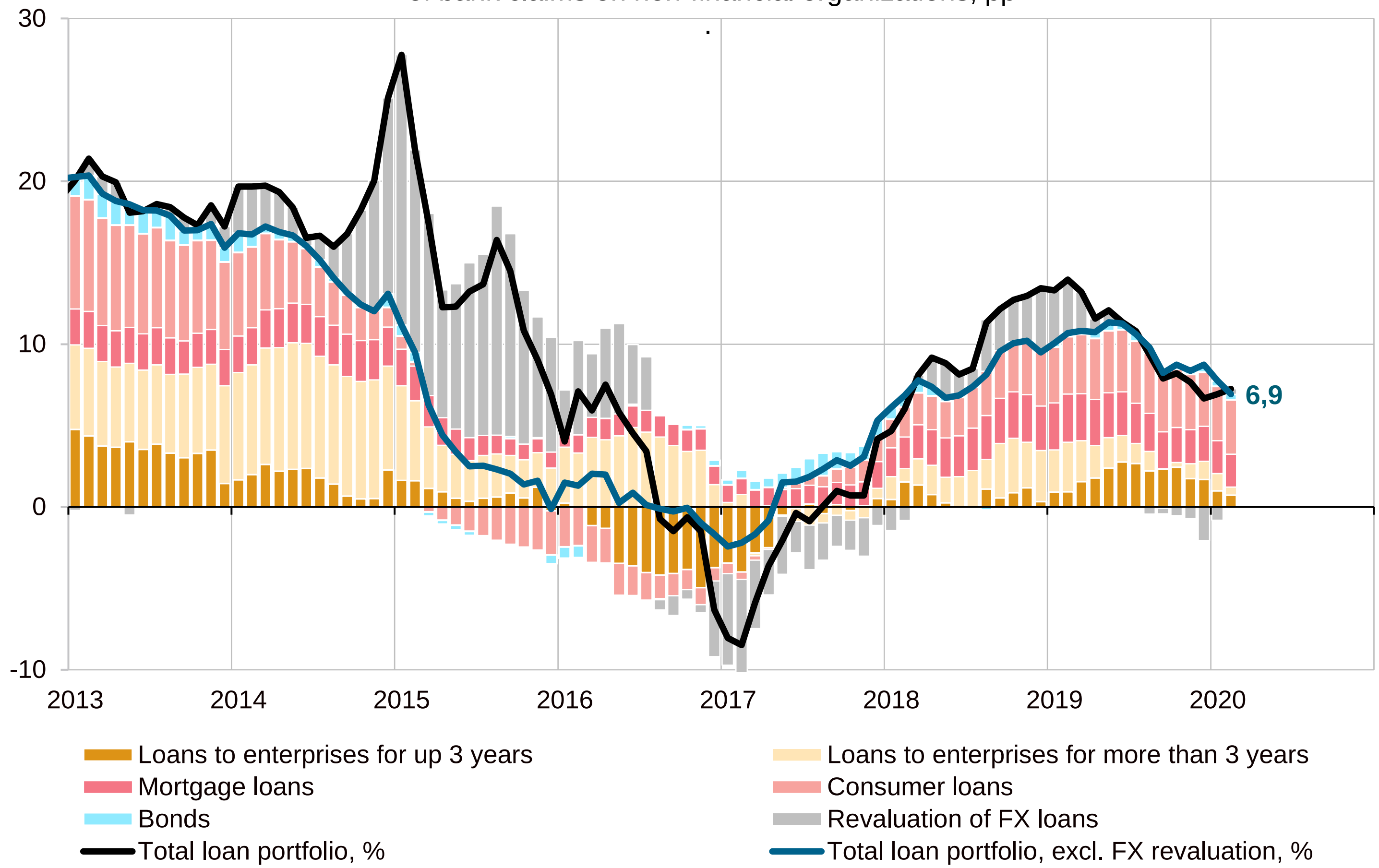


Source: Bank of Russia

Deposit and credit market – lending

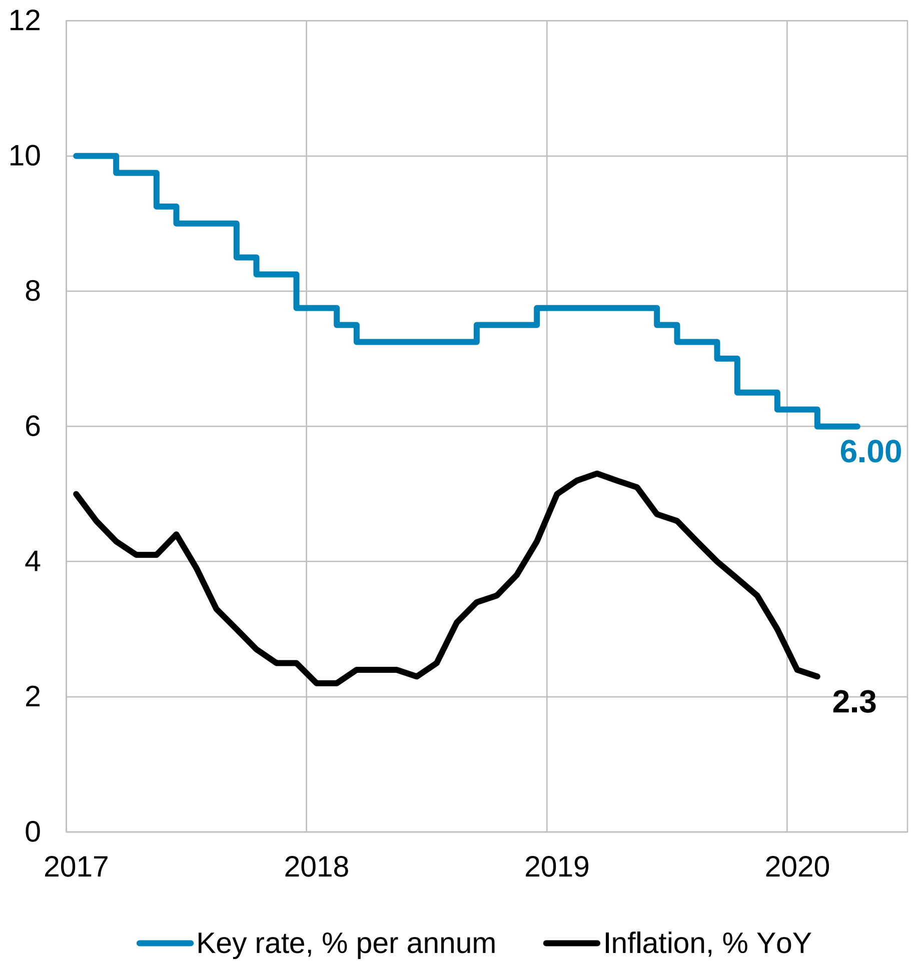
The Bank of Russia’s measures taken to curb financial stability risks and regulatory relaxations adopted will support credit expansion, including in the most vulnerable sectors, and will help limit the scale of tightening of monetary conditions.

Contribution of various components to annual growth of bank claims on non-financial organizations, pp



Source: Bank of Russia

Monetary policy decision on 20 March 2020



On 20 March 2020, the Bank of Russia Board of Directors decided **to keep the key rate at 6.00% per annum.** In February — March, the situation has been developing with a significant deviation from the Bank of Russia's forecast under the baseline scenario. This is related to changes in external conditions: the spread of the coronavirus epidemic and a sharp drop in oil prices. **The ruble's depreciation is a temporary proinflationary factor.** It might prompt annual inflation to exceed the target level this year. **However, the dynamics of domestic and external demand will exert a meaningful constraining influence on inflation** on the back of a pronounced slowdown of global economic growth and increased uncertainty. The package of measures adopted by the Government and the Bank of Russia ensures financial stability and will support the economy. All these factors were taken into account when making the key rate decision. **Given the current monetary policy stance, annual inflation will return to 4% in 2021.**

Moving forward, in its key rate decision-making the Bank of Russia will take into account actual and expected inflation dynamics relative to the target and economic developments over the forecast horizon, as well as risks posed by domestic and external conditions and the reaction of financial markets.

Source: Press release following the Bank of Russia's Board of Directors meeting as of 20.03.2020

The package of economic measures of the Government and the Bank of Russia

Bank of Russia

Measures aimed at:

1. Protecting those who have suffered from the pandemic and ensuring the availability of payment services for the people.
2. Supporting lending to small and medium-sized enterprises.
3. Supporting mortgage lending.
4. Supporting the financial sector's ability to provide resources to the economy.
5. Easing regulatory and supervisory burden for financial institutions.
6. Easing the burden on Russian joint-stock companies.
7. Maintaining the liquidity of the banking sector.

Government

Measures aimed at:

1. Fully implementing the scheduled 2020 budget expenditures, if necessary – providing additional support for regional budgets.
2. Granting tax holidays to companies in certain industries, including air transport and tourism, and exempting them from payments to funds.
3. Ensuring the stable operation of the trading industry.
4. Providing state guarantees for the purpose of restructuring and prolonging loans in certain sectors.
5. Expanding the list of systemic enterprises and, if necessary, providing additional support for them.
6. Expanding the concessional lending programme for small and medium enterprises.
7. Changing the Government's approach to government contracts with regard to suppliers affected by the current situation, in order to avoid penalties.

Sources: press release of the Government and the Bank of Russia on measures to ensure sustainable economic development as of 17.03.2020; the Bank of Russia's press release on measures to support people, economy and financial sector during coronavirus as of 20.03.2020.

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APPENDIX

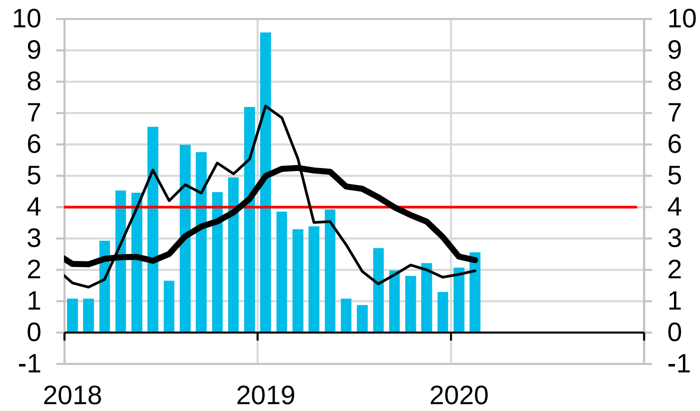
Inflation rates for main groups, seasonally adjusted (1)

Feb 2020, %	YoY, %	MoM SAAR
All	**2.3**	**2.6**
- ex. F&V, oil prod. and util.	**2.5**	**1.8**
Food	**1.8**	**1.8**
- ex. F&V	**2.3**	**-0.3**

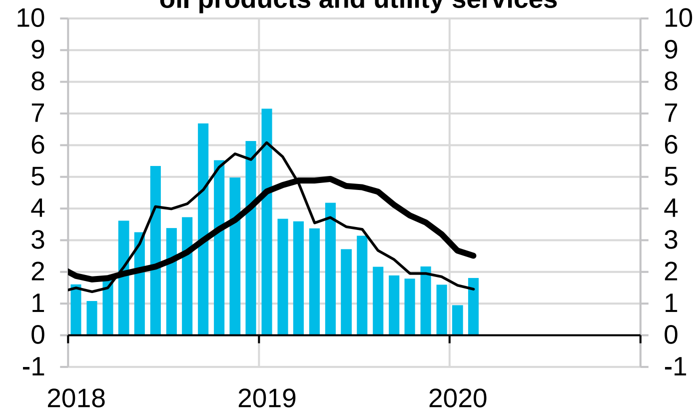
The price growth slowdown in February was caused by the overall high saturation of the food market, subdued demand, and time-lag effects of the ruble appreciation in the previous months.

The annual growth rates of food and non-food prices continued to decline.

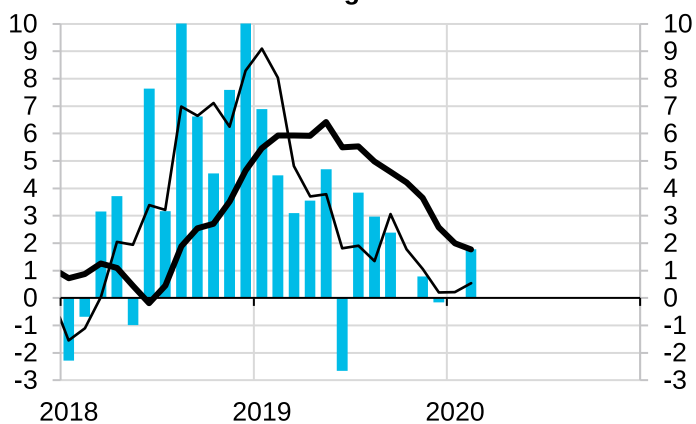
All goods and services



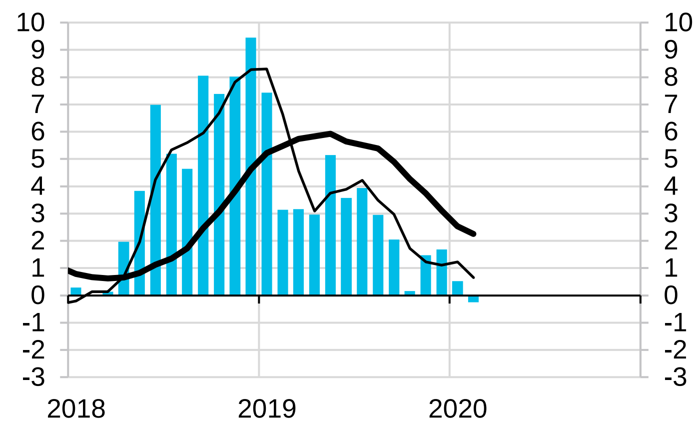
CPI, excluding fruit and vegetables, oil products and utility services



Food goods



Food goods, excluding fruit and vegetables



Columns – monthly price growth rate, seasonally adjusted, %
Line – annual inflation, % (rhs); thin line – 3MMA SAAR
Red line – 4% SAAR

Sources: Rosstat, Bank of Russia's estimates

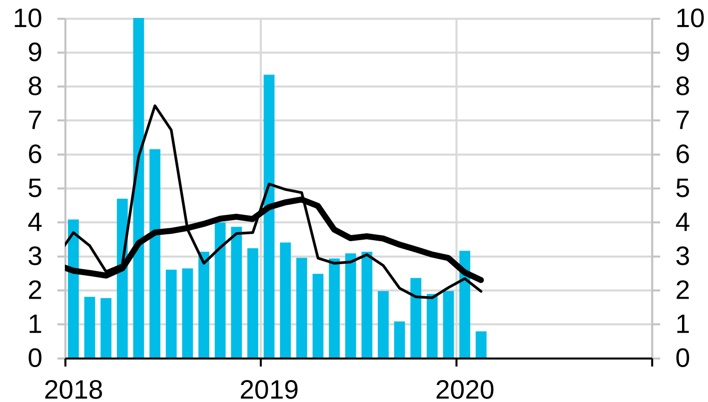
Inflation rates for main groups, seasonally adjusted (2)

Feb 2020, %	YoY, %	MoM SAAR
Non-food	**2.3**	**0.8**
- ex. petrol	**2.4**	**0.8**
Services	**3.0**	**5.8**
- ex. utilities	**3.2**	**6.6**

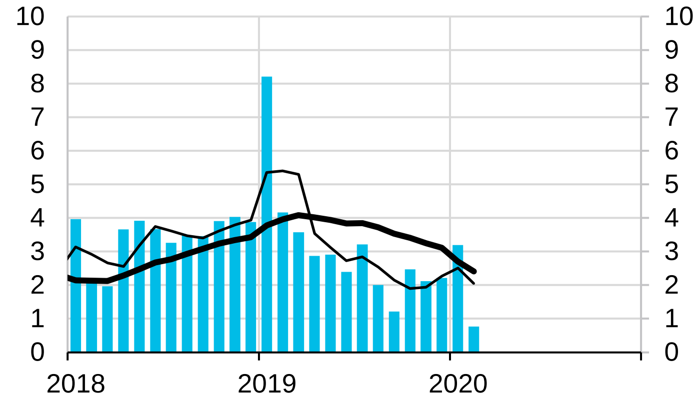
In February, the annual growth of service prices sped up slightly after a slowdown to its record-low in the previous month.

This increase against January was primarily driven by changes in prices for telecommunication and transportation services.

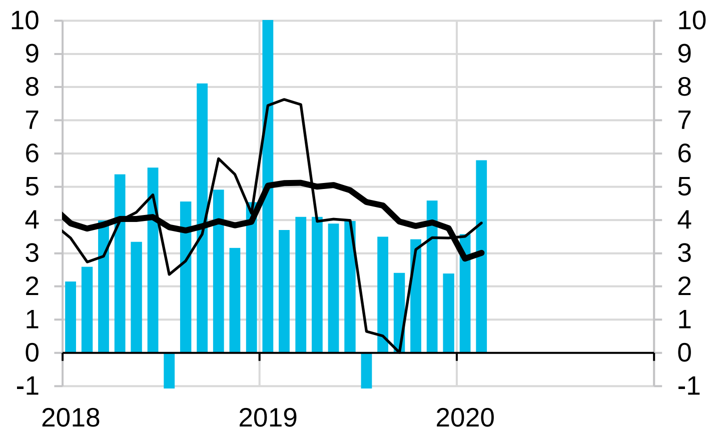
Non-food goods



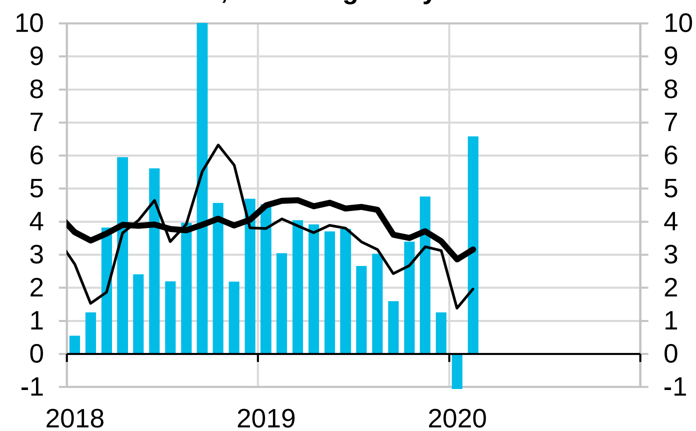
Non-food goods, excluding oil products



Services



Services, excluding utility services



Columns – monthly price growth rate, seasonally adjusted, %
Line – annual inflation, % (rhs); thin line – 3MMA SAAR

Sources: Rosstat, Bank of Russia's estimates