Bank of Russia

FEBRUARY 2021

MONETARY POLICY REPORT

20 February 2021

The report has been prepared based on statistics as of 11 February 2021.

The data cut-off date for forecast calculations is 11 February 2021 (if statistics or other information relevant for decision-making come in after the data cut-off date, they are included in the text of the Report and may be used to adjust the mid-term forecast).

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This publication has been prepared by the Monetary Policy Department.

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STATEMENT BY BANK OF RUSSIA GOVERNOR ELVIRA NABIULLINA

IN FOLLOW-UP TO BOARD OF DIRECTORS MEETING 12 FEBRUARY 2021

Today, we have decided to keep the key rate at 4.25% per annum.

The economy is bouncing back rather steadily. I would like to remind you that at our previous meeting we expected economic revival to pause at the end of 2020. However, GDP statistics and high-frequency indicators evidence that this did not happen. Moreover, inflation also exceeds our expectations.

I will further on dwell on the factors, which we were taking into account when making our decision today.

***I will start out with the situation in the economy**. It has turned out to be better than we expected, and there is a range of reasons for this. First, the restrictions in autumn and winter were not as tough as in spring. Second, both households and businesses were better prepared for the resurgence of coronavirus cases and adjusted faster. Credit activity did not decline, and consumer demand remained unchanged, including owing to a rise in online purchases. Third, external demand for Russian exports also turned out to be higher than our expectations.*

We assume that demand in the economy will be recovering steadily further on, promoted by lending expansion amid accommodative monetary policy, mass vaccination, and an improvement in household and business sentiment.

Over the acute phase of the crisis, budget spending considerably supported the real sector. The effect of stimulus measures is expected to continue in the first half of the year as well. Further on, the scheduled fiscal policy normalisation will reduce the extent of this influence. Nonetheless, the budget will remain expansionary as compared to the long-term parameters provided for by the fiscal rule.

In these conditions, economic growth will continue owing to a further revival of both domestic and external demand. The recovery of domestic demand will be driven by the cancellation of restrictions as the epidemic situation improves, especially in the service sector. External demand will be boosted by a rebound in the global economy. Disinflationary demand-side pressure will thus be decreasing overall.

Given the current positive trends, we keep unchanged our forecast of GDP growth at 3–4% for 2021. Furthermore, the economy may reach its pre-pandemic levels already by late 2021, and not by mid-2022, as we assumed earlier. This will become possible primarily as a result of a less significant decline in 2020.

The second factor is inflation*. Annual inflation sped up to 5.2% in January, exceeding the Bank of Russia's target. This elevated inflation rate largely resulted from the pass-through of the ruble weakening and price growth in global commodity markets. According to our estimates, the contribution of the pass-through of the exchange rate movements to annual inflation approximated one percentage point. The contribution of high prices in food markets was slightly lower yet substantial. Given increased inflation expectations and supply-side restrictions, these factors may have a longer-lasting effect on prices.*

The pass-through of last year's ruble depreciation to prices still continues, although it is waning. Recently, prices could be affected not only by ruble exchange rate fluctuations in 2020 H2, but also its weakening in spring, when enterprises were unable to revise their prices immediately due to a slump in demand. Eventually, the combination of the two episodes of the ruble depreciation may be a reason why inflation expectations will stay elevated for a longer period.

Upward pressure on domestic prices persists due to the situation in global commodity markets, first and foremost in food markets. Food prices have risen because of reduced inventories and unfavourable weather conditions. Moreover, the growth of prices for cereals increases costs in meat product manufacturing and is not only a proinflationary factor in itself, but it may also entail secondary effects. It is worth noting that the new mechanism of export duties in grain markets will smooth out the influence of global price fluctuations on domestic prices.

Finally, inflation is still affected by a group of factors associated with the epidemic situation. It includes staff shortages in a number of industries, increased costs incurred by companies to comply with sanitary and epidemiological rules, and persistent temporary delays in supplies due to disruptions in logistics chains. These are supply-side factors putting upward pressure on inflation.

Given the nature of these processes, we estimate that annual inflation will pass its peak in February—March, after which it will be going down incrementally. This will become possible as the impact of the above proinflationary factors is gradually exhausted. Beginning from March, the statistical base effect will also play a significant role in the decrease in annual inflation. Taking into account the monetary policy pursued, we forecast that prices will grow by 3.7%—4.2% over the year.

The third factor we were taking into account when making our today's decision is that monetary conditions remain accommodative. *While nominal interest rates on loans and deposits changed only slightly, real price conditions were eased. Banks also continued to ease non-price lending conditions in a range of segments. Yields on federal government bonds increased somewhat amid the growth of long-term interest rates in global financial markets.*

Owing to the monetary policy pursued and the Government's anti-crisis support measures, the increase in the banking system's claims on companies accelerated to 10.2% last year, which is more than in 2019. The growth rate of claims on households equalled 12.9%. The economy and borrowers obtained the funds they needed to more smoothly overcome the acute phase of the crisis and resume development.

In 2021, monetary conditions will remain accommodative, further promoting lending expansion, despite the expected gradual termination of preferential programmes. The banking system's claims on companies are forecast to increase by 7–11% this year, *and those on households — by 14–18%, largely as a result of the accelerated expansion of mortgage lending.*

As regards fluctuations in banking sector liquidity observed in recent months, they had no impact on monetary conditions. As before, the Bank of Russia preserved money market rates close to the key rate. This became possible owing to the streamlined operational procedure which is efficient amid both a deficit and a surplus of liquidity.

Today, we have published the Bank of Russia's updated baseline forecast. *It relies on the following assumptions:*

First of all, external conditions have become more promising. The global economy is expected to grow faster owing to mass vaccination and additional fiscal stimuli in advanced economies. This will strengthen external demand for Russian exports. Therefore, we have increased our forecast of oil prices from 45 to 50 US dollars per barrel for 2021 and 2022. Nonetheless, our forecast remains conservative given the high uncertainty about a potential further spread of the pandemic. According to our estimates, a faster recovery of the demand for oil may translate to a greater extent into a rise in oil output rather than oil prices.

As regards the 2022–2023 horizon, our forecast remains unchanged. *The economy will expand by 2.5–3.5% in 2022 and by 2–3% in 2023. Given the monetary policy pursued, inflation will return to the target at the end of 2021 and stay close to 4% further on.*

I will now speak on possible risks to the forecast. Disinflationary risks do not prevail any longer in 2021. Moreover, this is generally a balance between proinflationary and disinflationary risks over the forecast horizon.

Proinflationary risks *include, first and foremost, a possible rise in prices in global commodity markets. Second, the epidemic situation remains one of the least predictable factors. Its potential worsening will be the reason why companies' costs will stay high, with goods transportation problems and production chain disruptions persisting. Third, inflation expectations may remain elevated for a long period of time. Fourth, it is worth emphasising that economic rebound may be uneven and involve local price spikes in individual segments. For instance, as restrictions are lifted in the service sector hardest hit by the pandemic, an increase in demand amid an insufficient rise in supply may become a temporary proinflationary factor. The scale and duration of its impact will depend on a new balance between demand and supply, households' behaviour, changes in consumer preferences, and the pace of the cancellation of restrictions on foreign travels. Fifth, we still take into account persistent geopolitical risks as they may affect yield trends and inflation and exchange rate expectations.*

The second group of risks include disinflationary factors. *First of all, the fiscal policy normalisation may have a more significant influence on final demand and, accordingly, price movements. Second, the uncertainty regarding future consumer behaviour remains. During the quarantine and long self-isolation period, a lot of people abandoned some services, formed new consumption preferences, and changed their mode of life. We do not know whether they will become steady and how they will be influencing price trends. Third, after the boundaries are reopened, it is natural to expect that the demand will shift towards outbound tourism services. As labour migrant flows and logistics chains restore, this will become a disinflationary factor. Finally, as the restrictions are eased, companies will be able to reduce their costs for the sanitation of their premises and the anti-pandemic protection of their staff and customers, which will ease pressures on businesses' costs.*

In conclusion, I would like to comment on monetary policy prospects. *The accommodative monetary policy and the Government's package of anti-crisis measures have been promoting economic revival after the acute phase of the crisis. According to our estimates, we consider that the potential for monetary policy easing has been exhausted. Its further easing could additionally increase proinflationary risks. Nonetheless, monetary policy will remain accommodative on average throughout 2021, supporting the recovery of the Russian economy. The baseline scenario provides for a gradual return to neutral monetary policy. We will assess the timeline and pace for this return taking into account our goal to maintain inflation at our target.*

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

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

As the epidemic situation worsened in 2020 Q3–Q4, a large number of countries tightened their anti-pandemic restrictions, economic activity recovery slowed down, and global stock indices adjusted downwards. However, trends in global financial and commodity markets started to improve already in November, inspired by the news about highly efficient anti-coronavirus vaccines and a stabilising political situation in the USA.

Economic activity in Q4 exceeded the forecast given by the Bank of Russia in October: in contrast to the expectations, the recovery growth that had started in Q3 did not pause, but only decelerated. These dynamics mostly resulted from steadier domestic and external demand. Manufacturing was the major contributor to the growth of output in the key industries in 2020 Q4. Moreover, as compared to Q3, output expanded in all large goods categories, and most considerably in investment and consumer goods. As of the end of the year, GDP contracted by 3.1% (MPR 4/20: a 4.0–5.0% decline).

A gradual termination of restrictions worldwide as epidemic risks go down will promote the further growth of Russia's economy. According to the Bank of Russia's forecast, the more active rebound in 2020 H2 will help close the output gap faster over the medium-term horizon. Eventually, it is expected to have a significantly weaker disinflationary impact. The estimates of GDP growth in 2021–2023 remained the same as in the October forecast.

Price movements in late 2020–early 2021 were driven by proinflationary factors, including supply-side shocks in a range of domestic food markets, a rise in global prices for exchange-traded commodities, higher producer costs, and the continuing pass-through of the ruble weakening to prices. As of the end of 2020, the growth rate of consumer prices reached 4.9%, exceeding the Bank of Russia's forecast (MPR 4/20: 3.9–4.2%). In February–March 2021, inflation is expected to peak as compared to the same period last year, after which it will start to trend downwards. As of the end of 2021, inflation will equal 3.7–4.2% and will stay close to the target further on. The Bank of Russia will determine the timeframe and pace for returning to neutral monetary policy, taking into account actual and expected inflation movements relative to the target and trends in the Russian economy and external markets.

In addition, it should be noted that despite a pause in the market rates reduction in 2020 H2, monetary conditions actually eased even more, as increased inflation expectations amid the acceleration of observed inflation and the unchanged key rate caused a notable decline in real interest rates.

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

FOLLOWING THE BANK OF RUSSIA BOARD OF DIRECTORS' KEY RATE MEETING ON 12 FEBRUARY 2021

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

	2020 (actual / estimate)	Baseline		
		2021	2022	2023
Inflation, % in December YoY	4.9	3.7–4.2	4.0	4.0
Inflation, yearly average, % YoY	3.4	4.4–4.8	4.0	4.0
Gross domestic product	-3.1	3.0–4.0	2.5–3.5	2.0–3.0
Final consumption expenditures	-5.2	4.7–5.7	2.0–3.0	1.8–2.8
– households	*-8.6*	*5.0–6.0*	*2.5–3.5*	*2.0–3.0*
Gross capital formation	-4.2	3.9–5.9	3.0–5.0	2.5–4.5
– gross fixed capital formation	*-6.2*	*3.2–5.2*	*2.4–4.4*	*2.5–4.5*
Exports	-5.1	1.1–3.1	3.6–5.6	2.2–4.2
Imports	-13.7	8.9–10.9	3.4–5.4	2.9–4.9
Money supply in the national definition	13.5	10–14	7–11	7–11
Banking system claims on the economy in rubles and foreign currency*	10.9	9–13	7–11	7–11
– on businesses	*10.2*	*7–11*	*6–10*	*6–10*
– on households	*12.9*	*14–18*	*10–14*	*10–14*
housing mortgage loans	*21.2*	*16–20*	*14–18*	*14–18*

** Banking sector claims on the economy mean all claims of the banking system on non-financial and financial institutions and households in Russian rubles, foreign currency, and precious metals, which include loans issued (including overdue loans), overdue interest on loans, credit institutions' investment in debt and equity securities and promissory notes, as well as other forms of equity interest in non-financial and financial institutions, and other receivables under settlement operations with non-financial and financial institutions and households.*
The growth rate of claims is adjusted for foreign currency revaluation. For the purpose of the adjustment for foreign currency revaluation, the growth in claims in foreign currencies and precious metals is recalculated into rubles at the period average RUB/USD exchange rate. Housing mortgage loans, net of claims on such loans acquired by banks.
Source: Bank of Russia.

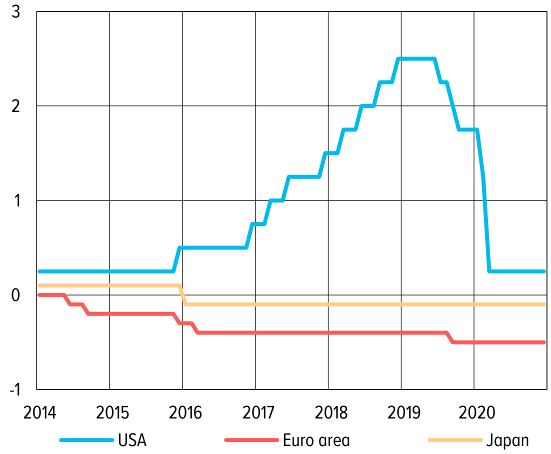
RUSSIA'S BALANCE OF PAYMANETS INDICATORS IN THE BASELINE SCENARIO* *Table 2*
(billions of US dollars, if not indicated otherwise)

	2020 (estimate)	Baseline		
		2021	2022	2023
Current account	**33**	**39**	**29**	**25**
Balance of trade	89	119	116	119
Exports	*330*	*375*	*389*	*406*
Imports	*240*	*256*	*273*	*287*
Balance of services	-18	-35	-41	-48
Exports	*45*	*49*	*53*	*58*
Imports	*63*	*84*	*94*	*106*
Balance of primary and secondary income	-39	-45	-46	-47
Current and capital account balance	**32**	**39**	**29**	**25**
Financial account (excluding reserve assets)	**50**	**26**	**12**	**6**
General government and the central bank	-2	-9	-8	-9
Private sector	52	35	20	15
Net errors and omissions	**4**	**0**	**0**	**0**
Change in foreign currency reserves ('+' is increase, '-' is decrease)	**-14**	**13**	**17**	**19**
Urals crude price, yearly average, US dollars per barrel	**42**	**50**	**50**	**50**

** On the basis of the methodology set out in the 6th edition of the Balance of Payments and International Investment Position Manual (BPM6). In the financial account, '+' denotes net lending and '–' denotes net borrowing.*
Note: final values may differ from the total of the respective values due to rounding.
Source: Bank of Russia.

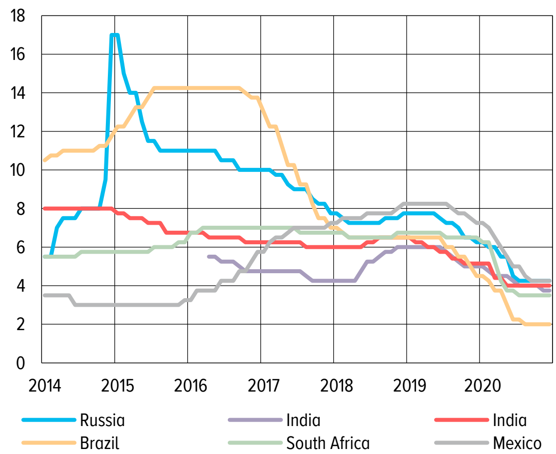
[1] *The alternative scenarios of the Bank of Russia's forecast (proinflationary, disinflationary, and risk scenarios) are provided in Monetary Policy Guidelines for 2021–2023.*

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



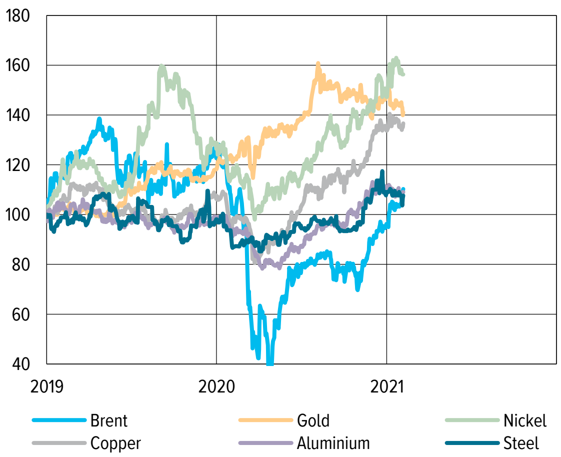
Source: Bloomberg.

POLICY RATES: EMES *Chart 1.1.2*
(%)



Source: Bloomberg.

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



Source: Bloomberg.

1.1. CURRENT SITUATION

At the end of 2020, the recovery in the global economy slowed down. This was caused by the worsening epidemic situation and tougher restrictions in both advanced and emerging market economies. Moreover, the economic rebound remained uneven, which was largely associated with the extent of the tightening of anti-pandemic restrictions.

The slowdown of the economic recovery put downward pressure on inflation. The acceleration of inflation which occurred in November–December in a range of EMEs (Brazil and Mexico) was partially driven by temporary factors, namely a rise in global food prices. As a result, the majority of central banks, including in EMEs, kept their policy rates unchanged in 2020 Q4, emphasising the importance of maintaining accommodative monetary conditions. The Central Bank of the Republic of Turkey was the only exception: it tightened the monetary policy increasing its policy rate in November–December from 10.25% to 17.00% p.a. amid a significant acceleration of actual inflation and increased risks for its forecast.[1]

A range of central banks in EMEs where policy rates remain close to zero (Poland, Hungary, and Chile) continued to acquire assets in order to maintain accommodative monetary conditions. As regards other EMEs, Bank Indonesia continued to purchase government bonds in the primary market to finance the budget deficit, and the Reserve Bank of India kept buying government bonds in the secondary market to support liquidity, stability in the debt market, and the government's borrowing target.

Beginning from October, central banks in advanced economies predominantly expanded their asset purchase programmes so as to promote economic recovery and stabilise inflation close to the targets (the ECB, the Bank of England, the Riksbank, and the Reserve

[1] *In its communication, the Central Bank of the Republic of Turkey explained that the considerable tightening of the monetary policy was needed to limit the impact of proinflationary risks over the forecast horizon, stabilise inflation expectations, and ensure steady disinflation in the economy. It also stressed that it might tighten the monetary policy further if needed.*

Bank of Australia).[2] The U.S. Federal Reserve System and the Bank of Japan kept their programmes unchanged, while updating their communications regarding their next moves. The US Fed promised not to reduce the pace of buying Treasuries and mortgage-backed bonds until the moment when a considerable further progress was made towards the achievement of the employment and inflation targets. The Bank of Japan announced possible further stimulus measures in March within its policy framework of quantitative and qualitative monetary easing with yield curve control.

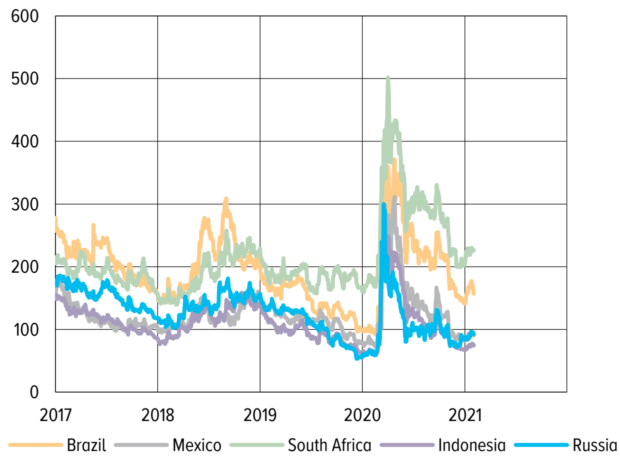
As the epidemic situation worsened worldwide, global stock indices temporarily adjusted downwards at the end of October. Nonetheless, their trend reversed already in November, driven by the news about highly efficient anti-coronavirus vaccines and preparations for their usage in the near future, as well as a stabilising political situation in the USA.

Upward trends also prevailed in commodity markets. Besides favourable news, prices for core Russian exports were supported owing to the OPEC+ deal on crude oil production cuts observed by the parties and an additional agreement concluded on 3 December 2020 on a slower-than-earlier assumed output expansion in January 2021 (by 0.5 mbd instead of 2 mbd). The Urals crude price averaged 44.3 US dollars per barrel in 2020 Q4, which is 2.4% higher quarter-on-quarter. In 2020, the average Urals crude price equalled 41.6 US dollars per barrel, decreasing by one-third against 2019.

In January, energy commodity prices continued to trend upwards, driven, among other things, by Saudi Arabia's decision on additional output cuts in February–March. **Economic activity will gradually revive worldwide as more people are vaccinated against the coronavirus in 2021, which will promote a further rise in the demand for energy commodities and commodity prices. According to the Bank of Russia's estimate, the average annual price**

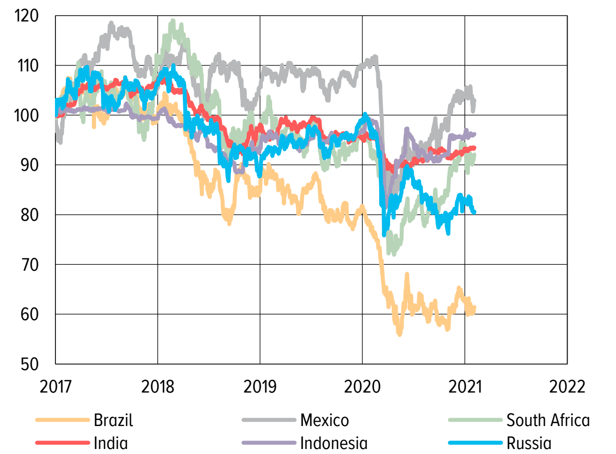
[2] *The Reserve Bank of Australia lowered its target for the yield on 3-year government bonds to 0.10% p.a. in November and introduced for the first time the target amount of 100 billion Australian dollars for government bond purchases. In February, this target amount was increased twofold by another 100 billion Australian dollars.*

CDS OF EMES *Chart 1.1.4*
(bp)



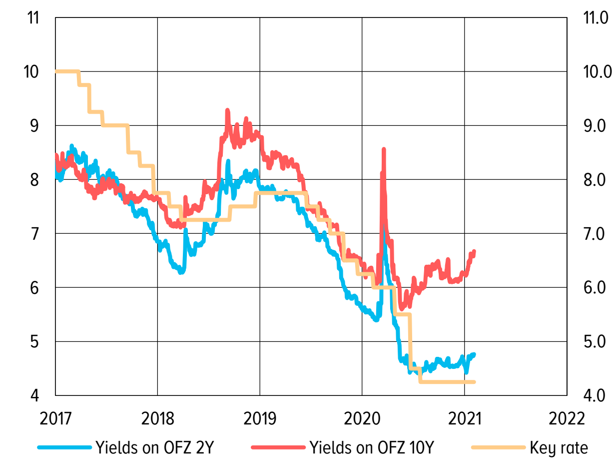
Source: Reuters.

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



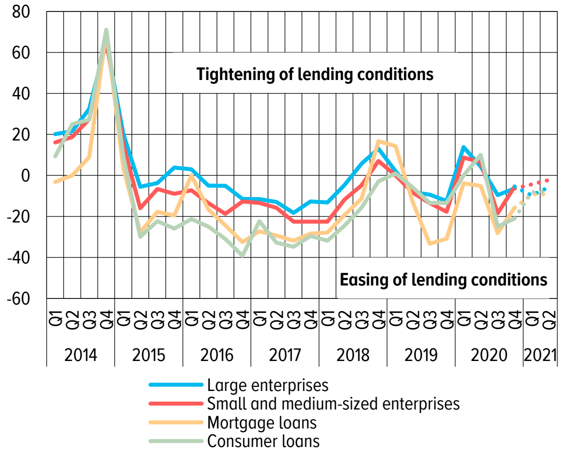
Source: Reuters.

OFZ YIELDS AND BANK OF RUSSIA KEY RATE *Chart 1.1.6*
(% p.a.)



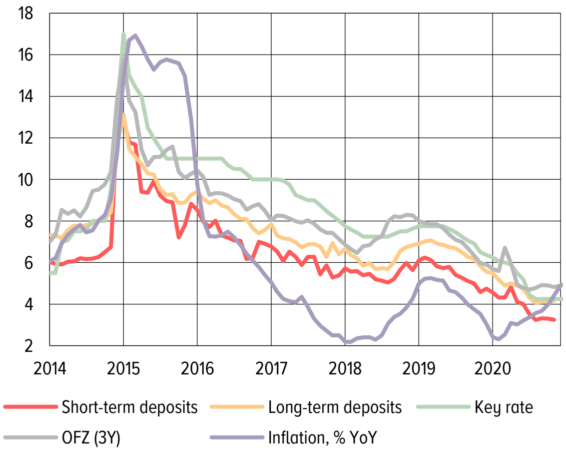
Sources: Moscow Exchange, Bank of Russia.

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



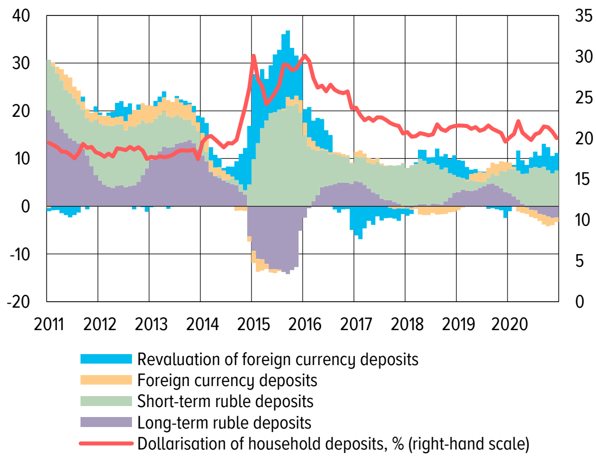
** The dotted lines show the expectations of respondent banks in 2020 Q4.*
Source: Bank of Russia.

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



Source: Bank of Russia.

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



Source: Bank of Russia.

for Urals crude oil will exceed in 2021 the level assumed before, reaching 50 US dollars per barrel (MPR 4/20: 45 US dollars per barrel).

Country risk premia for the majority of EMEs decreased in 2020 Q4, while their currencies strengthened against the US dollar. Russia's CDS spread ranged from 75 to 80 basis points beginning from mid-November. As it soared temporarily in December (due to elevated geopolitical risks), it equalled 89 bp as of the end of the year. Russia's CDS spread widened by 34 bp over the year, which is comparable to other EMEs.

The ruble exchange rate reached 74.4 RUB/USD as of the end of the year, losing 20% against early 2020. The extent of the ruble depreciation in 2020 is comparable with other EMEs (Brazil and Turkey).

In January 2021, EMEs' risk premia slightly rose, and the ruble weakened amid increased volatility and risk-off sentiment in stock markets. However, in the first half of January 2021, the ruble was mostly strengthening against the background of rising demand for high-risk assets in global markets, with this trend reversing only in the second half of the month.

In Q4, activity in the OFZ market was high, including owing to SICIs. Russia's Ministry of Finance reached its 2020 OFZ borrowing target as early as in November. Overall, in 2020 the Ministry of Finance placed OFZ bonds at the auctions in the amount of 5.3 trillion rubles and Eurobonds totalling 0.2 trillion rubles at face value over the year, which is a record high. The entire OFZ yield curve moved lower from the start of the year, with short-term OFZ yields declining most significantly. This was associated with a considerable reduction in the key rate and the Bank of Russia's shift towards accommodative monetary policy in 2020.

Monetary conditions in Russia's economy remained almost the same in Q4. This was because the Bank of Russia Board of Directors decided not to change the key rate in September–December. Furthermore, banks continued to pursue conservative policies in relation to borrowers amid the uncertainty about future economic developments caused by the coronavirus pandemic.

The reduction in average market loan rates discontinued in 2020 Q4. A number of market segments recorded their moderate rise, which was largely associated with a decreased portion of preferential credit products in lending amounts. Nonetheless, market interest rates stayed close to their record lows, while credit activity was high in both retail and corporate lending. Non-price lending conditions in the main segments of the credit market remained nearly the same in 2020 Q4.

In September–November, deposit rates stayed close to their 2020 Q3 level: 4.1–4.2% on long-term and 3.2–3.3% on short-term ruble deposits. In December, interest rates on ruble deposits adjusted upwards in certain market segments. This was driven by a moderate rise in yields on financial market instruments, banks' competition for depositors, and attractive seasonal offerings on the eve of the New Year holidays. Interest rates on foreign currency deposits stayed close to their record lows.

As of the end of 2020, the annual growth[3] of household deposits[4] slowed down to 4.3% (from 9.3% in 2019). **Activity in the deposit market weakened amid lower real returns on deposits and rising demand for savings alternatives, including real estate.** Specifically, the annual growth of balances in escrow accounts exceeded 1 trillion rubles as of the end of 2020 (against less than 150 billion rubles in 2019).

In 2020 Q4, the structure of the retail deposit portfolio was dominated by two key trends. First, as the economic situation remained uncertain and the spread between interest rates on time and demand deposits contracted, households continued to transfer their funds from time deposits to current accounts. The only segment of the time deposit market with the inflow of households' funds remaining positive was longer-term deposits (for over three years). This could be associated with higher interest rates in this market segment, as compared to deposits with shorter maturities.

Second, the inflow of funds into household foreign currency deposits in the last months of the year slowed down the annual decrease in foreign currency deposits (from 8.8% as of the end of October to 4.6% as of the end of December). Nonetheless, the share of foreign currency deposits in the retail portfolio contracted in Q4 owing to a stronger ruble and the revaluation of foreign currency deposits.

Generally in 2020, reducing balances in foreign currency deposits, households simultaneously expanded their investments in alternative foreign currency instruments, primarily foreign currency-denominated securities.

According to Rosstat's first estimate, GDP contracted by 3.1% in 2020 (against +2.0% in 2019).[5] This is significantly better than the Bank of Russia's forecast given in its MPR 4/20 (a 4.0–5.0% decline).

This was primarily because of an 8.6% reduction in households' consumption (vs +3.2% in 2019) amid a decrease in their real disposable incomes and the impact of restrictions on the operation of the services sector. Two other significant and comparable drags on GDP were gross fixed capital formation (GFCF) and exports, although their influence was lower than that of consumption. A surge in uncertainty and the introduction of temporary restrictions on companies' operation caused a 6.2% decrease in GFCF (vs +1.5% in 2019). Exports shrank by 5.1% (vs +0.9% in 2019), pulled down by weak external demand and oil production cuts.

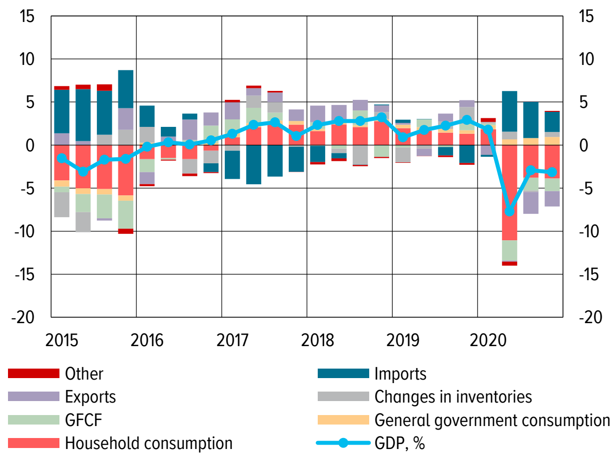
Temporary restrictions on foreign travel and decreased demand in the economy resulted in a 13.7% contraction of imports (vs +3.5% in 2019), which became the major driver of GDP dynamics. Aggregate output was also supported by a 4% rise in general government consumption (vs +2.4% in 2019) amid large-scale fiscal stimulus

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

[4] *Hereinafter, deposits do not include escrow accounts under equity construction contracts.*

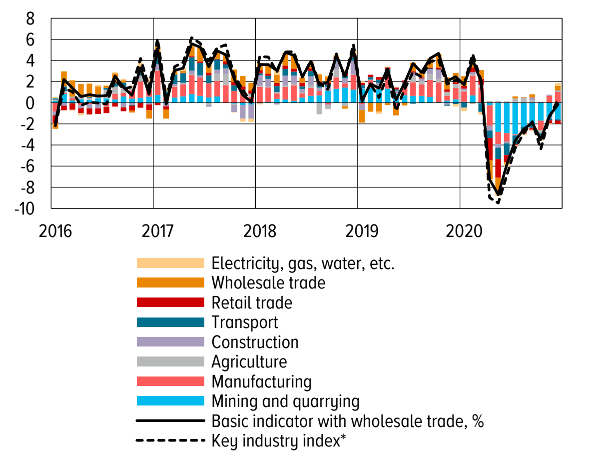
[5] *Rosstat revised the 2018–2019 statistics on GDP, but released only annual results. The breakdown of GDP movements by quarter is based on the Bank of Russia's assessment (for details, see the Box 'Adjusting quarterly GDP data series according to revised annual assessments').*

GDP BY EXPENDITURE* Chart 1.1.10
(contribution to annual growth, pp)



* *Bank of Russia estimate, by quarter in 2018–2020.*
Sources: Rosstat, Bank of Russia calculations.

BASIC OUTPUT INDICATOR* Chart 1.1.11
(contribution to annual growth, pp)



* *Bank of Russia estimate. Reflects annual dynamics of production activity by key industry (manufacturing, agriculture, wholesale and retail trade, construction, and transport).*
Sources: Rosstat, Bank of Russia calculations.

measures. Over 2020, the non-oil and gas deficit of the fiscal system and the federal budget expanded by 3.7 trillion rubles and 3.4 trillion rubles, respectively. Nonetheless, the fiscal impulse in 2020 turned out to be slightly lower than assumed by the Bank of Russia in its MPR 4/20, which implies that fiscal consolidation will be less considerable in 2021 than expected earlier.

As regards the breakdown of aggregate output by industry, the main drag on GDP in 2020 was value-added decreases in mining and quarrying (-1.2 pp), transportation (-0.6 pp), trade (-0.3 pp), and in the hotel and restaurant business[6] (-0.2 pp). The most significant contributor supporting aggregate output was a value-added rise in finance (+0.3 pp).

In the second half of the year, economic activity in Russia was bouncing back. In Q3, the revival was mostly driven by industries focused on domestic consumption (retail and services), while in Q4 this upward trend was largely supported by manufacturing.[7]

Although restrictions were tightened due to the worsening epidemic situation in 2020 Q4, economic activity continued to bounce back. According to the Bank of Russia's assessment, output in the key industries expanded in 2020 Q4 by 1.7% quarter-on-quarter (SA)[8] (vs +5.9% in 2020 Q3). The annual decrease in output slowed down to 1.8% (vs -3.0% in Q3).

Manufacturing was the major contributor to the growth of output in the key industries in 2020 Q4. Moreover, as compared to Q3 (SA), output expanded in all large goods categories, and most considerably in investment and consumer goods. In November–December, this was driven to a great extent by a surge in the output of pharmaceuticals, namely medicines (for details, see the Box 'Pharmaceutical output in late 2020–early 2021').

Manufacturing output in 2020 remained at the level of 2019 on average. Moreover,

[6] *According to the OKVED 2 system (the Russian Classification of Economic Activities): hotels and public catering.*

[7] *Hereinafter, the estimates provided do not take into account the data released on 15 February 2021, including the revised statistics for December 2020.*

[8] *Hereinafter, seasonally adjusted.*

consumer goods output increased to its five-year high (+4.2 vs 2019), and investment goods output remained close to its 2019 level. Industries manufacturing intermediate goods intended for exports were considerably affected by the pandemic. This negative effect was explained by a high volatility of global prices and restrictions on production activity and transportation remaining in a range of Russia's trading partners.

A rather serious decline in mining and quarrying output in 2020 was induced by decreased global demand for energy commodities in the first half of the year and the OPEC+ oil production cuts in the second half of the year. Overall, mining and quarrying output contracted by 7% in 2020. Nonetheless, output in mining and quarrying was rebounding in 2020 Q4. Its future dynamics will largely depend on the extent to which the OPEC+ countries will ease their oil production cuts and on the recovery pace of economic activity in Russia's trading partners.

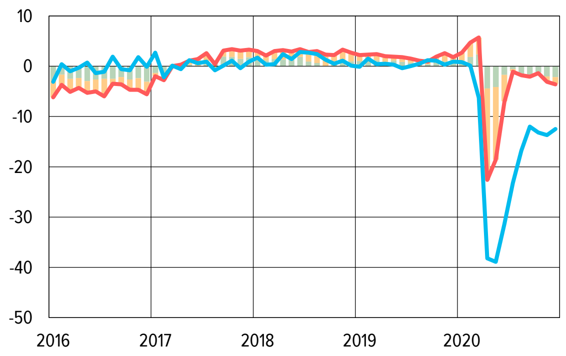
As investment goods output continued to expand, this was evidence that investment activity was reviving further. It was supported by the anti-crisis measures implemented by the Russian Government and accommodative monetary conditions. According to the Bank of Russia's assessment, fixed capital investment in 2020 Q4 increased quarter-on-quarter (SA). As assessed by the Bank of Russia, fixed capital investment contracted by 3.3–3.8% over the year in general, which was largely because companies significantly revised their investment plans amid decreased demand in 2020.

Overall, industrial output (SA) expanded by 2.4% in 2020 Q4 against Q3, as assessed by the Bank of Russia. Its annual reduction slowed down to 2.5% (vs -4.8% in Q3). On average, it was 2.9% lower in 2020 than in 2019.

In 2020 Q4, the situation in the labour market improved, with the unemployment rate going down to 6.1% (SA). However, this recovery was uneven, with the demand rising predominantly for low-skilled and construction workers, which was associated with a shortage of migrants. The demand for staff combating the coronavirus also increased.

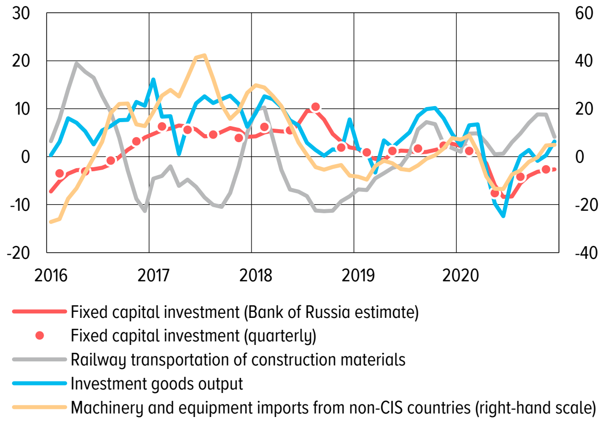
In October–November 2020, the annual rise in nominal wages slowed down to 4.5–4.6%,

RETAIL TRADE AND SERVICES *Chart 1.1.12*
(% change on the same month of the previous year)



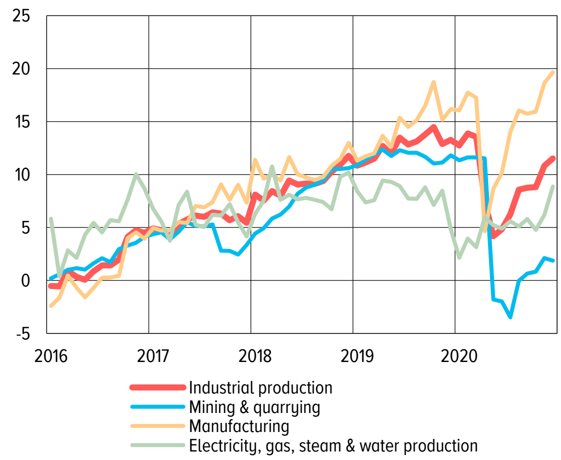
Sources: Rosstat, Bank of Russia calculations.

FIXED CAPITAL INVESTMENT *Chart 1.1.13*
(% 3MMA**)*



** 2020 Q4 – Bank of Russia estimate.*
***3MMA per cent change on the same period of the previous year.*
Sources: Rosstat, FCS, Russian Railways, Bank of Russia calculations.

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



Sources: Rosstat, Bank of Russia calculations.

with the public sector remaining the driver of this growth. The increase in real wages decelerated to 0.2–0.5% due to faster inflation.

As the epidemic situation remained challenging and households' incomes were growing slowly in 2020 Q4, this continued to hinder consumer activity. According to the Bank of Russia's assessment, consumption[9] generally remained at the previous quarter's level (SA). Moreover, the recovery trend continued only in commercial services, which was probably associated with their deeper decline in Q2, while retail turnover stayed at its Q3 level (SA). Over this period, consumer activity was supported by shifts in the structure of household spending as people tended to purchase more goods and services inside Russia amid the remaining restrictions on outbound tourism.

As coronavirus cases decrease, Russia's economy will continue to bounce back. This recovery will be gradual and largely driven by a rise in domestic demand.

The growth of consumer prices sped up significantly beginning from October 2020. As of the end of 2020, inflation reached 4.9%, which is considerably higher than the Bank of Russia's forecast given in its MPR 4/20 (3.9–4.2%). In January 2021, inflation continued to rise (to 5.2%), including because of the low base effect. Supply-side factors were the major contributor accelerating the growth of consumer prices in October 2020–January 2021 (for details, see Section 2).

Food inflation surged due to an increase in costs, driven by a weaker ruble, among other factors, and higher global prices for agricultural raw materials and food products, as well as the decreased supply of certain food products in the domestic market. A drastic acceleration of sugar and sunflower oil price growth was contained owing to the administrative measures imposed by the Russian Government in the middle of December 2020 (see the Box 'Situation in the sugar and sunflower oil markets in October 2020–January 2021').

[9] *The growth rate of consumption was calculated as the weighted average of the rises in retail turnover and commercial services, accounting for 3/4 and 1/4 in this calculation, respectively.*

Anti-pandemic requirements continued to affect primarily the dynamics of service prices, with their annual growth rates remaining decreased. At the same time, the gradual revival of demand limited proinflationary pressure to a lower extent than in previous months.

The increase in costs and product prices was driven by the exchange rate pass-through, including its deferred effects.

Higher costs and prices pushed up households' and businesses' inflation expectations. Analysts' long-term inflation forecasts remained anchored at the Bank of Russia's target.

1.2. THE BANK OF RUSSIA'S FORECAST

The global economy is recovering from coronavirus shocks faster than expected earlier. The external output gap will remain negative until the end of the forecast horizon, yet it will be close to zero already beginning from 2021 Q4.

Many large economies (e.g. the UK, Germany, Italy, the USA, Japan) implemented large-scale budget-funded support measures, which enabled them to prevent a drastic decline forecast in mid-2020. Furthermore, the recovery processes emerging in the global economy have strengthened as households and businesses gradually adjusted to the pandemic situation, the restrictions reintroduced by countries in 2020 Q3–Q4 due to the resurgence of coronavirus cases were targeted, and various countries started mass vaccination.

Nonetheless, this recovery is uneven across economies, while the emergence of new coronavirus variants and delays in vaccine rollouts are forcing a range of countries to extend their anti-pandemic measures hindering certain economic activities. Additional measures implemented by governments to aid households and businesses help to slightly cushion the adverse consequences of the persistent pandemic.

Taking into account the above trends, the Bank of Russia has revised its estimate[10] of the recovery path of external output over the forecast horizon. As compared to the previous estimates given in MPR 3/20 and MPR 4/20, the rebound is much faster. The growth rates of new coronavirus cases and related restrictions are assumed to peak in 2020 Q4–2021 Q1, the availability of various vaccines for general public will be increasing, and active recovery processes in external economies are forecast to complete already by late 2021, while previously the significant negative output gap was expected to remain until the end of the forecast horizon. Moreover, according to the updated path, the external output gap will stay negative until the end of the forecast horizon, yet it will be close to zero already beginning from 2021 Q4. The key factor for the external output gap to remain negative is the situation in the euro area affected by the resurgence of coronavirus cases at the end of the year more drastically than other macro-regions (e.g. the USA, China), facing challenges in rolling out the vaccine, and allocating a considerably smaller aggregate amount of fiscal stimulus to the economy as compared to the USA.

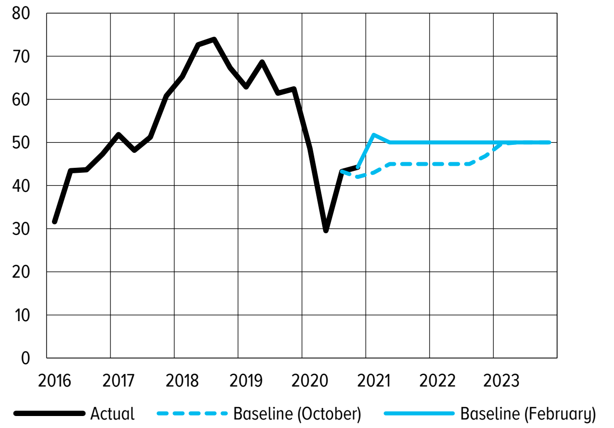
Given a more active economic rebound abroad and the revision of historical time series (for details, see the Box 'Adjusting quarterly GDP data series according to revised annual assessments'), the Bank of Russia has reviewed its estimates of exports growth in 2021 from the previously forecast (-0.8)–1.2% up to 1.1–3.1%. Further on, exports growth is expected to stay close to the levels assumed in MPR 4/20.

Investor sentiment was optimistic at the end of the year, contributing to a steady decrease in volatility in financial markets and risk premia for EMEs.

Compared to mid-2020, market sentiment became much more positive in late 2020–early 2021. As the third stage of the clinical trials of several vaccines completed and countries launched mass vaccination, markets started to focus more on the expected recovery path,

[10] *For more details on the Bank of Russia's model for estimating development trends in the external sector, see Olga Korotkikh (2020). A Multi-Country BVAR Model for the External Sector, 79 (4), pp. 98–112.*

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



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

rather than on the pandemic situation. As the major economies of the world (the USA and China) announced additional support measures in November–December 2020, this intensified investors' enthusiasm, which influenced, among other things, volatility index movements and investors' estimates of EMEs' risks. As a result, EMEs' risk premia edged down as of the end of the year, to the levels considerably lower than expected in October. Moreover, market participants also estimated risks for Russia as lower (see Section 1.1 'Current situation').

Taking into account the actual developments in markets, the Bank of Russia has revised its estimate of risks for EMEs and Russia. As compared to MPR 4/20, risk premia over the medium-term horizon will be lower for both EMEs and Russia. Risk premia are assumed to incrementally grow until the end of the forecast horizon, rising to the levels corresponding to the long-term balance of risks for these countries.

Oil prices increased amid global economic revival, yet they are not expected to rise further over the medium-term horizon.

As economic activity was bouncing back in multiple countries worldwide, this contributed to the increase in the demand and prices for exchange-traded commodities, including oil (see Section 1.1 'Current situation'). Furthermore, oil prices are still supported owing to the OPEC+ deal, under which its parties reached new agreements in December–January on a slower production expansion in early 2021 and Saudi Arabia undertook additional obligations to cut oil production by 1 mbd in February–March.

Given the actual developments in the oil market, the Bank of Russia has raised the oil price path in 2021–2022 from 45 to 50 US dollars per barrel. Nonetheless, given the high uncertainty of the situation, the Bank of Russia's medium-term forecast of oil prices remains conservative. A surge in prices would increase oil production by the USA and other non-OPEC+ countries and the probability that the parties to the deal would be raising oil production quotas faster. Taking into account these factors, oil prices are expected to stabilise close to 50 US dollars per barrel until the end of the forecast horizon (see the Box 'Global oil demand and supply amid the pandemic').

Russia's economy has weathered the shocks of the coronavirus better than expected, and will be recovering increasingly more steadily as epidemic risks decrease. The economy may return to its late 2019–early 2020 level already by the end of 2021.

According to the released statistics and economic activity indicators, the 2020 decline in Russia's economy was not so deep as expected earlier (see Section 1.1 'Current situation'). Despite the reintroduction of a range of anti-pandemic restrictions in 2020 Q4, the recovery growth only slowed down, but not paused, as was assumed in MPR 4/20. In 2020, output was largely supported owing to the Russian Government's anti-crisis package and accommodative monetary policy (see Section 1.1 'Current situation').

As compared to the October forecast, the Bank of Russia has updated its estimate of the situation in the domestic economy as a result of both the newly published data on actual developments and the revision of historical time series (see the Box 'Adjusting quarterly GDP data series according to revised annual assessments'). The growth rate and level of potential GDP are estimated slightly better than in October. The negative output gap as of the end of 2020 is forecast to be almost twice smaller than assumed in MPR 4/20.

As evidenced by actual results, Russia's economy has already passed a part of its recovery path, although a steady shift towards the revival was previously forecast in 2021. The recovery peak is now expected in 2021, rather than 2022. As a result, the output level corresponding to late 2019–early 2020 (pre-pandemic) readings may be reached as soon as by the end of 2021, the negative output gap will move close to zero, and the disinflationary pressure of the negative output gap will be significantly weaker than expected earlier. As of the end of 2021, GDP growth will equal 3.0–4.0%.

Stable domestic demand, more favourable conditions in trade, and rising external demand will promote a further rise in Russia's economy. Output growth will exceed the potential rate in 2020 H2 and is forecast to reach 2.5–3.5% as of the end of the year, partially due to the expiry of the OPEC+ deal, which will push upwards oil and gas output. In 2023, output growth will return to the potential rate.

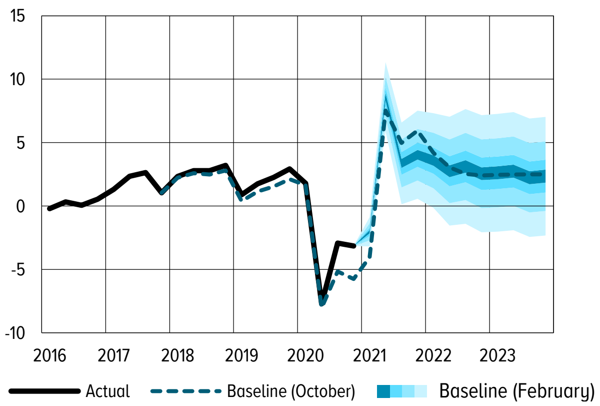
Gross fixed capital formation exceeded expectations in 2020. The recovery will continue in 2021, with GFCF rising close to the rate expected in MPR 4/20, i.e. the range of 3.2–5.2%. In 2020–2023, as fiscal consolidation progresses and the effect of pent-up investment demand is exhausted, the growth rate of GFCF will stabilise at 2.5–4.5%.

The recovery growth of household demand started already in 2020, as a result of which the decline in household final consumption expenditure turned out to be lower than expected. In 2021, households will continue to satisfy pent-up demand, yet it will translate to a greater extent into purchases of imported products and services, while consumption growth inside the country will be moderate. As households partially satisfied pent-up demand in 2020, the rise in household final consumption expenditure in 2021 will be slightly below the previously forecast level, specifically in the range of 5.0–6.0% (MPR 4/20: 5.3–6.3%), in 2022 – in the range of 2.5–3.5% (MPR 4/20: 3.7–4.7%), slowing down to 2.0–3.0% in 2023 (MPR 4/20: 2.5–3.5%). Simultaneously, imports growth promoted by the improving epidemic situation abroad and the reopening of borders earlier than was assumed in October will reach its highest rate in 2021 (8.9–10.9%), rather than 2022.After households and businesses satisfy pent-up demand for imports in 2021, the rise in imports will slow down to 3.4–5.4% in 2022 and to 2.9–4.9% in 2023.

Compared to the same period last year, inflation will exceed the target in 2021 Q1–Q3, yet will go down to 3.7–4.2% as of the end of 2021. Given the monetary policy pursued, inflation will stay close to 4.0% over the medium-term horizon.

As compared to MPR 4/20, the Bank of Russia has adjusted its estimate of the balance of proinflationary and disinflationary risks. In October, disinflationary factors were expected to have the dominant influence on inflation trends. However, shocks in a number of food markets, as well as the effects of supply-side shocks that occurred only partially (specifically, their influence is evident from the results of

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



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

the *monitoring of enterprises* carried out by the Bank of Russia), and the continuing pass-through of the ruble weakening accelerated price growth at the end of 2020. Along with one-off factors, inflation was also boosted by the domestic demand revival that was more active and steadier than expected.

As compared to the assumptions in October, fiscal policy in 2020 put more significant proinflationary pressure on prices. As of the end of 2020, Russia had a federal budget deficit of 3.9% of GDP, which was less than forecast in MPR 4/20, largely owing to a more solid rise in non-oil and gas revenues (personal income tax: +6.9% YoY and VAT: +1.4% YoY), with their growth driven by the economic recovery. A smaller deficit implies that the scale of required fiscal consolidation will be lower in 2021 and, accordingly, fiscal policy will have weaker disinflationary impact. In 2022–2023, the influence of fiscal policy will remain as forecast.

According to the Bank of Russia's estimate, the proinflationary pressure of the above factors will persist throughout 2021 H1, gradually weakening further on. The accumulated effects of demand- and supply-side shocks induced by anti-pandemic restrictions will contain price growth in 2021–2022. Nonetheless, disinflationary risks have generally become less intense over the medium-term horizon due to both higher domestic demand and expected improvements in external markets that will boost Russian exports growth and enhance trade conditions. Although households' inflation expectations lowered in January 2021 for the first time since August 2020, they still remain elevated as compared to the pre-pandemic levels.[11] Inflation expectations surged to four-year highs at the end of 2020, predominantly driven by increased prices for certain food products.

Inflation is expected to peak in 2021 Q1, as compared to the same period last year. Further on, price growth will slow down as a result of the weakening of proinflationary factors. Inflation will return to the 4% target as of the end of the year and will stay close to this rate in the

[11] *For details, see the information and analytical commentary Inflation Expectations and Consumer Sentiment, No. 1 (49), January 2021.*

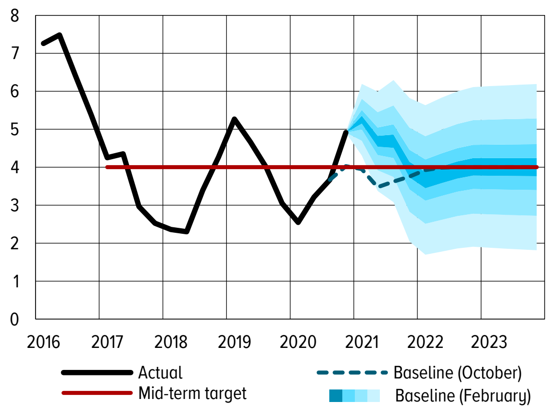
future. The Bank of Russia will determine the timeframe and pace for returning to neutral monetary policy, taking into account actual and expected inflation movements relative to the target and trends in the Russian economy and external markets.

Furthermore, monetary conditions will remain accommodative in 2021, promoting a rise in corporate and retail lending by 7–11% and 14–18%, respectively. In addition to the key rate reduction in 2020 H1, monetary conditions eased even more in late 2020–early 2021 as a result of increased inflation expectations amid faster observed inflation and the unchanged key rate, which caused a significant decline in real interest rates. Lower real rates also influenced OFZ-IN price movements. According to the Bank of Russia's assessment, the easing of monetary conditions in 2020 provided additional support to the recovery of domestic demand. Beginning from 2022, owing to the stabilising economic situation, lending growth rates will move towards their long-term equilibrium values of 6–10% for businesses and 10–14% for households.

The current account surplus relative to GDP will contract as restrictions are eased and demand for imports rises. A decrease in the risk premium will contribute to a capital inflow into the general government sector.

According to the Bank of Russia's preliminary estimates, the current account balance in 2020 was close to the forecast in MPR 4/20.[12] Nonetheless, given a faster recovery of the global economy coupled with the increase in actual oil prices, the estimates of the current account surplus have been adjusted accordingly over the forecast horizon. The current account surplus is estimated at higher nominal levels in 2021–2022, as compared to MPR 4/20. However, in contrast to the October forecast, it is expected to steadily decrease to 1.3% in 2023 as a percentage of GDP. This estimate primarily relies on the assumption that the epidemic situation will normalise faster both in Russia and abroad and, accordingly, service imports will expand more significantly. To a certain extent, the current account surplus will shrink

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



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

[12] *For details, see the information and analytical commentary Russia's Balance of Payments, No. 4 (6), 2020 Q4.*

due to an increase in the negative contribution of non-tradable components – the primary and secondary income account – driven by a rise in Russian companies' dividend payouts to foreign shareholders as the economic situation returns to normal, as well as by the rebound of foreigners' economic activity in Russia.

Higher oil prices over the forecast horizon are also a reason for revising the forecast for reserve assets which are expected to grow beginning from 2021 owing to the effect of the fiscal rule.

The estimate of net lending by the Russian private sector to the rest of the world remained the same: it is expected to contract to 35 billion US dollars in 2021, 20 billion US dollars in 2022, and 15 billion US dollars in 2023. Simultaneously, the inflow of foreign capital into the general government sector will expand as a result of the decreased risk premium for Russia.

Risks to the baseline scenario remain elevated, yet the impact of the epidemic situation on the economy is gradually diminishing.

The coronavirus and related anti-pandemic restrictions still have a considerable influence on both the current economic environment and the forecast of economic development in Russia over the medium-term horizon.

The epidemic situation may still worsen, and this probability cannot be totally excluded until coronavirus cases continue to increase and new variants are identified, with vaccination being delayed in a number of countries. Moreover, if the coronavirus mutates significantly, the existing vaccines may turn out to be inefficient against new variants and restrictions will remain in place worldwide over a longer-term horizon.

There is also a possibility for a structural shift in consumer preferences that may have altered during the period of the pandemic. First, consumers now visit conventional stores less frequently and prefer online orders or more rare visits with larger purchase amounts. If this trend continues, this may reduce overall demand (e.g. when stores are visited less frequently, the value of unplanned purchases is also lower). Second, as a result of anti-pandemic restrictions, households are seeking to create financial cushions in order to have support if their incomes decrease. The pattern to maintain larger savings and unwillingness to spend available funds may be a reason why the recovery path of domestic demand will be below the expected level.

Companies' investment demand may also turn out to be lower than expected if anti-pandemic risks rise. In a range of industries, companies seeing no recovery prospects after the pandemic, may review their long-term development programmes and decrease their investment spending below their pre-pandemic targets.

Finally, central banks worldwide, responding to a faster economic recovery in respective countries, may terminate their stimulus programmes too early, which will increase volatility in markets and raise estimated risks for EMEs. If market volatility surges, this may aggravate debt problems in EMEs that are forced to allocate substantial budget funds to support households and businesses during the pandemic, already having large public debt. This may also exacerbate geopolitical tensions, including those associated with protectionist policy. However, the probability that this set of risks may materialise is shifted towards the end of the forecast horizon.

Overall, households and businesses have largely adjusted to the conditions of the pandemic, and the start of mass vaccination, even though there are some difficulties with vaccine rollouts in individual countries and regions, makes it possible to give relatively optimistic estimates of development prospects in the next few years.

2. INFLATION AND INFLATION EXPECTATIONS

CONSUMER PRICES FOR MAIN GROUPS OF GOODS AND SERVICES
(% change on previous month, SA)

Table 2.1

	August 2020	September 2020	October 2020	November 2020	December 2020	January 2021
Inflation	0.39	0.26	0.46	0.58	0.55	0.45
Food products (excluding fruit and vegetables)	0.30	0.22	0.58	0.66	0.58	0.51
Non-food goods (excluding petroleum products)	0.43	0.53	0.64	0.59	0.48	0.49
Services (excluding utilities)	0.25	-0.12	0.34	0.28	0.26	0.27

Sources: Rosstat, Bank of Russia calculations.

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

Table 2.2

	August 2020	September 2020	October 2020	November 2020	December 2020	January 2021
Inflation	3.58	3.67	3.99	4.42	4.91	5.19
Food products (excluding fruit and vegetables)	3.72	3.80	4.41	5.03	5.44	5.87
Non-food goods (excluding petroleum products)	3.52	3.94	4.38	4.82	5.12	5.37
Services (excluding utilities)	2.41	2.07	2.10	1.97	2.21	2.54

Sources: Rosstat, Bank of Russia calculations.

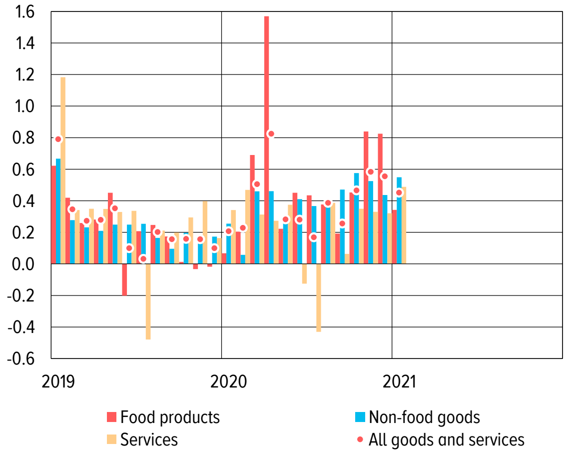
CONSUMER PRICES FOR MAIN GROUPS OF GOODS AND SERVICES
(% change on previous month, SAAR)

Table 2.3

	August 2020	September 2020	October 2020	November 2020	December 2020	January 2021
Inflation	4.78	3.17	5.66	7.19	6.80	5.54
Food products (excluding fruit and vegetables)	3.65	2.71	7.19	8.20	7.14	6.25
Non-food goods (excluding petroleum products)	5.25	6.50	7.95	7.26	5.97	5.99
Services (excluding utilities)	3.04	-1.40	4.15	3.41	3.12	3.29

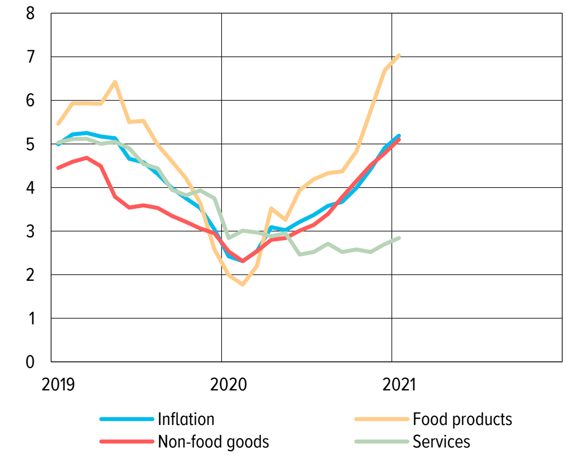
Sources: Rosstat, Bank of Russia calculations.

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



Sources: Rosstat, Bank of Russia calculations.

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



Source: Rosstat.

PRICES FOR CERTAIN GOODS AND SERVICES *Table 2.4*
(% change on the same month of the previous year)

	September 2020	October 2020	November 2020	December 2020	January 2021
Computers	2.9	3.6	3.9	4.8	5.0
Smartphones	-2.5	-1.7	-0.9	0.8	1.2
Fruit & citrus fruit	12.3	10.3	12.4	12.9	13.5
New imported cars	7.0	8.4	9.4	10.3	10.8
New domestic cars	6.3	8.0	9.2	9.4	9.1
Construction materials	3.0	3.7	4.4	5.3	6.3
Furniture	2.6	3.4	4.3	5.2	5.9
Domestic tourism	0.5	0.5	0.7	1.1	1.6
Outbound tourism	-1.0	-0.2	-1.4	-0.5	0.4
Air transportation	-10.7	-12.8	-12.6	-9.3	-8.4

Source: Rosstat.

In October 2020–January 2021, the current and annual growth rates of consumer prices were up. Over this period, their average monthly rise sped up to 0.5% (vs 0.3% in Q3) (Chart 2.1). Annual inflation rose to 5.19% (up by 1.52 pp against September). Price growth accelerated most significantly in Q4. In December, inflation equalled 4.91%, exceeding the Bank of Russia's forecast given in October (MPR 4/20: 3.9–4.2%). In January 2021, annual inflation continued to increase, reaching 5.19%.

A weaker ruble, higher global prices, reduced supply in individual food groups, and increased input costs were the reasons why food inflation sped up to 7.03% in January 2021 from 4.37% in September 2020. Exchange rate movements and a rise in input costs amid a certain revival accelerated the annual growth of non-food prices to 5.10% (up by 1.32 pp against September). Changes in services prices were largely influenced by anti-pandemic requirements. The growth rate of services prices rose by 0.32 pp to 2.84% (Chart 2.2).

A faster increase in costs and prices also affected inflation expectations. In October–January, both households and businesses generally raised their short-term (up to one year) inflation expectations. In January, analysts' inflation forecasts for the next two years stabilised close to 4%.

INFLUENCE OF THE RUBLE EXCHANGE RATE

In October 2020–January 2021, a rise in inflation was associated with the ruble weakening caused by external factors. Its direct impact was especially notable in the consumer market segments with a high import content, namely electronics and imported food products (Table 2.4).

Exchange rate movements also affected prices indirectly, specifically through input costs for imported intermediates (raw materials, components, and equipment). Their rise amplified pressure on prices for goods with a significant import component in prices (cars and home improvement goods).

Exchange rate movements also indirectly influenced inflation through changes in export parity prices for Russian exports affecting supply and prices in the domestic market. In July–

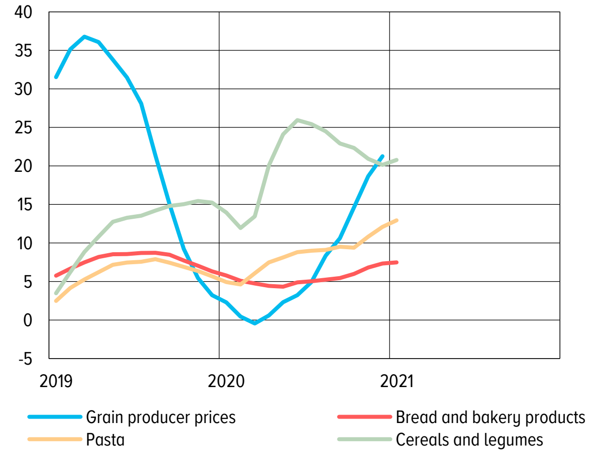
October, the ruble depreciated simultaneously with a rise in world prices for grains. All these factors accelerated the growth of producer prices for wheat and other (food and feed) grains. Eventually, this amplified pressure on prices and sped up the rise in prices for bread, baked goods, pasta, and semolina (Chart 2.3). As regards other grains, prices moved diversely depending on harvests. Overall, the growth of prices for grains and legumes trended downwards.

As export parity prices surged and exports expanded considerably, this accelerated the growth of prices for sunflower seeds and related products (oil and mayonnaise). The decline in the sunflower harvest also amplified pressure on prices. It should be noted that the rise in prices was largely recovery-type, after their decrease in previous years. Over the last five years, sunflower oil prices were growing more slowly than consumer prices in general (Chart 2.4). Nonetheless, they surged extremely fast in Q4, with their growth rate reaching 25.91% against 6.61% in September (on the same month of the previous year). In the middle of December, the Russian Government set maximum prices for sunflower oil and implemented other measures to stabilise the situation in the market. In January 2021, the rise in the annual growth rate of sunflower oil prices discontinued (see the Box 'Situation in the sugar and sunflower oil markets in October 2020–January 2021).

INFLUENCE OF FOOD SUPPLY

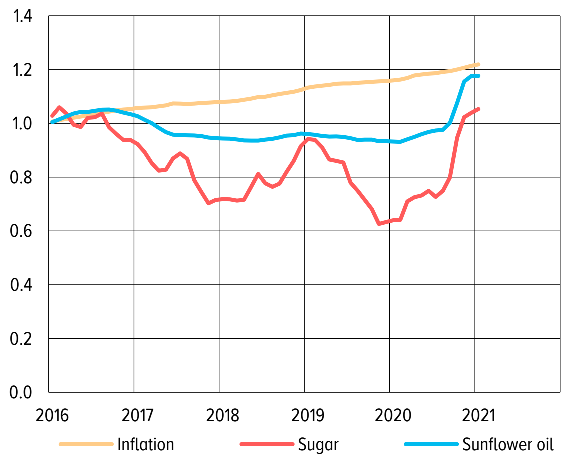
As supply contracted, this significantly accelerated the growth of prices for a range of food products. In 2020 Q4, sugar prices rose even more than sunflower oil prices, with the annual growth of sugar prices surging to 64.54% in December from 12.12% in September. This upward trend in the growth rate was observed throughout the year and was associated with the decrease in sugar beet cultivation areas – this measure was implemented by producers in order to offset the excess supply formed over previous years and restore profitability. As sunflower oil prices, sugar prices had been rising more slowly than consumer prices in general over the last five years (Chart 2.4). Nonetheless, the reduction in sugar supply and the surge in

PRICES FOR GRAIN, LEGUMES AND PRODUCTS OF THEIR PROCESSING
(% change on the same month of the previous year)
Chart 2.3



Source: Rosstat.

PRICES FOR SUNFLOWER OIL AND SUGAR
(December 2015 = 1)
Chart 2.4



Sources: Rosstat, Bank of Russia calculations.

PRICES FOR CERTAIN SERVICES *Table 2.5*
(% change on the same month of the previous year)

	September 2020	October 2020	November 2020	December 2020	January 2021
Sanatorium and health services	2.9	3.6	3.3	3.8	4.5
Passenger transport services	0.5	0.0	0.3	1.1	2.0
Public catering	1.8	2.0	2.1	2.3	2.6
Air transportation services	-10.7	-12.8	-12.6	-9.3	-8.4

Source: Rosstat.

sugar prices in Q4 were more significant than could be expected based on the scale of the decrease in the cultivation areas. As the sugar beet harvest declined and global prices and exports increased, this also affected sugar prices. The contribution of these factors to inflation is estimated at 0.1 pp.

As sugar prices surged drastically, the Russian Government decided to implement administrative measures regulating the market (see the Box 'Situation in the sugar and sunflower oil markets in October 2020–January 2021). In January 2021, the rise in the annual sugar price growth rate discontinued.

Potato prices also surged in Q4, and the acceleration of price growth was driven predominantly by a reduction in supply. As the gross harvest declined and the quality of the harvest was not high, this sped up the annual growth of potato prices from 8.71% in September 2020 to 37.6% in January 2021. It should be noted that fruit and vegetable prices are generally characterised by high volatility.

The surge in sunflower oil, sugar and potato prices significantly **worsened households' one-year ahead inflation expectations**.

It should be noted that annual price fluctuations are naturally regulating agricultural products supply: rising prices boost output, and vice versa. However, administrative measures regulating the sugar and sunflower markets have considerably increased the uncertainty about agricultural companies' plans.

INFLUENCE OF ANTI-PANDEMIC RESTRICTIONS

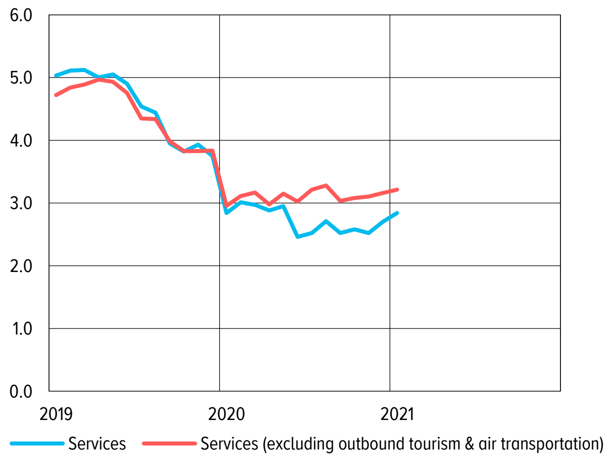
Anti-pandemic requirements continued to affect price trends in late 2020–early 2021. From the middle of autumn, a large number of Russian regions recorded a resurgence of coronavirus cases, due to which they had to toughen their anti-pandemic restrictions, primarily in the services sector. These restrictions were generally not as tight as in spring–summer and thus did not significantly change prices for the majority of service types, as compared to Q3. Overall, their annual growth rate remained subdued (2.84% in January).

Outbound tourism was prohibited almost completely. On the eve of the New Year holidays, this factor (coupled with the government programmes supporting the demand for holidays inside Russia) boosted the demand for sanatorium and health services and accompanying transport and public catering services (see the report *Regional Economy: Commentaries by Bank of Russia Main Branches*). This sped up the annual growth of prices for these services (Table 2.5). Nonetheless, their contribution to the rise in inflation was minor.

As foreign tours and air flights were restricted, this continued to affect the informativeness of statistics since their prices were nominally shown as unchanged. From June 2020, the annual increase in prices for services, excluding transport and foreign travel, steadily exceeded the aggregate reporting indicator by approximately 0.6 pp (Chart 2.5). As the epidemic situation improves (with demand and supply restoring in this services segment), this gap will decrease, with price growth accelerating.

SERVICES PRICES
(% change on the same month of the previous year)

Chart 2.5



Sources: Rosstat, Bank of Russia calculations.

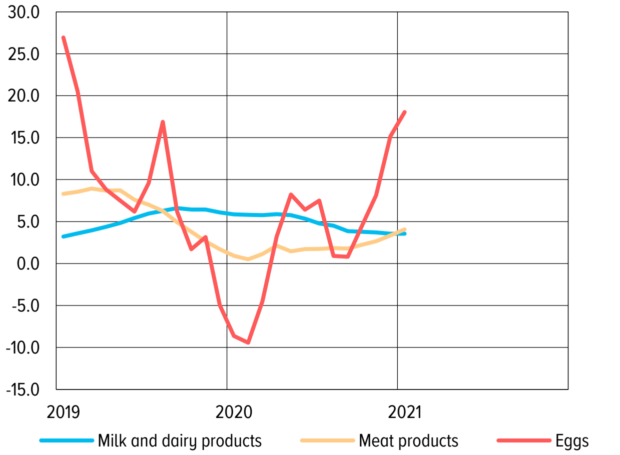
INFLUENCE OF DEMAND

In October 2020–January 2021, input costs continued to go up. In addition to a weaker ruble, this upward trend was also driven by the growth of prices in global commodity markets, including due to the pandemic, and expenses for anti-pandemic measures. Higher input costs as the main factor pushing up prices were mentioned by companies in multiple industries, including those focusing on consumer demand (see the report *Regional Economy: Commentaries by Bank of Russia Main Branches*).

Decreased demand was the key factor that contained an increase in consumer prices in 2020. Nevertheless, as anti-pandemic restrictions were eased in 2020 H2, economic activity, incomes and consumption started to recover slightly. **This expanded the possibilities for producers to pass through their input costs to prices.**

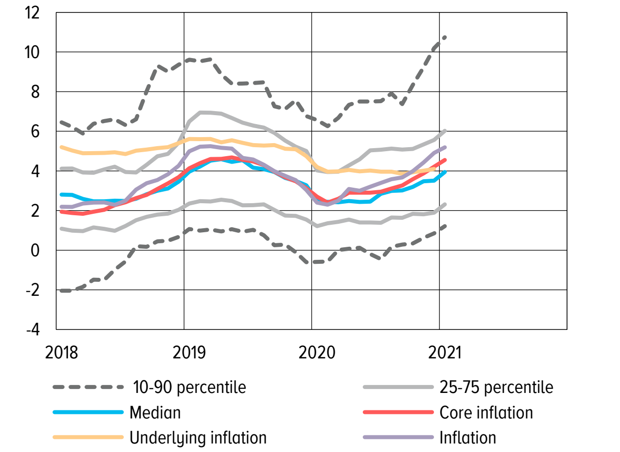
For instance, the growth rate of car prices sped up in Q4, thus becoming the major driver of a faster annual rise in non-food prices. In addition to the above general factors, the revival in the car market was also supported by government programmes. An additional factor of higher demand in late 2020 could be the disposal fee as it is expected to be raised in spring 2021. Furthermore, the pass-through

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



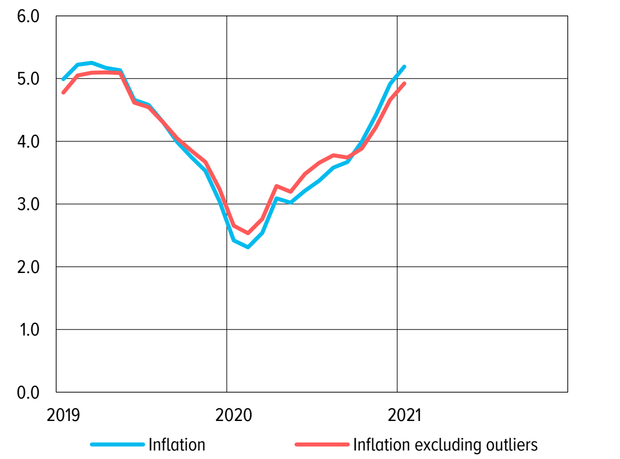
Sources: Rosstat, Bank of Russia calculations.

DISTRIBUTION OF GOODS AND SERVICES PRICE GROWTH, INFLATION, CORE INFLATION, AND UNDERLYING INFLATION
(% change on the same month of the previous year)
Chart 2.7



Sources: Rosstat, Bank of Russia calculations.

INFLATION EXCLUDING OUTLIERS
(% change on the same month of the previous year)
Chart 2.8



Sources: Rosstat, Bank of Russia calculations.

of input costs to prices intensified in Q4 as the situation in trade returned to normal: in March–July, car sales predominantly carried out offline discontinued amid tight anti-pandemic requirements. In January, the rise in car prices slowed down slightly, which was probably because the effects of the pass-through of accumulated costs was gradually diminishing.

In October–January, the annual growth rates of prices for construction materials and furniture also surged. The demand for this category of goods increased as a result of higher activity in the housing market, boosted in part by government support measures.

Contrastingly, the growth of prices for meat products was limited as households' preferences shifted towards cheaper goods. Meanwhile, pressure on prices strengthened due to input costs: the rise in domestic prices for feed grains accelerated and livestock producers' costs for imports (veterinary medicines, consumables, and equipment) increased. Eventually, prices for animal products changed diversely: the annual growth rate of prices for meat products edged up moderately, for eggs (generally characterised by high volatility) – accelerated, and for diary products – slowed down (Chart 2.6).

An overall rise in inflation is also evident from the movements of stable inflation indicators (net of volatile and administered components) (Chart 2.7). Inflation sped up as well without taking into account specific spikes in prices (for sugar, sunflower oil, and cars) and the categories where price statistics were distorted (transport and outbound tourism) (Chart 2.8).

Overall, the contribution of exchange rate movements in 2020 Q4 (including indirect effects in the sunflower oil, mayonnaise, and car markets) to the rise in inflation above the Bank of Russia's forecast is estimated at 0.5–0.6 pp. The additional contribution of the faster sugar price growth is estimated at 0.1 pp.

INFLATION EXPECTATIONS

In October 2020–January 2021, households and businesses raised their short-term (within one year) inflation expectations amid the accelerated growth of input costs and prices. Analysts' forecasts in early 2021 remained anchored close to 4%.

Households' inflation expectations. According to InFOM's surveys of households (commissioned by the Bank of Russia), the estimates of inflation observed by households were rising in October 2020–January 2021 amid the faster growth of prices for frequently purchased food products. Respondents were especially concerned about increased egg and sunflower oil prices. In January, the median estimate of inflation observed by households over the past 12 months reached 12.8% (the highest level since mid-2017; Chart 2.9).

The median estimate of inflation expected in the next 12 months also rose in Q4. In January, it edged down, probably owing to the stabilising situation in the sunflower oil, sugar, and egg markets. Nonetheless, its level still remained elevated (10.5%). The percentage of respondents believing that inflation will considerably exceed 4% in the next three years also decreased in January (by 5 pp to 47%).

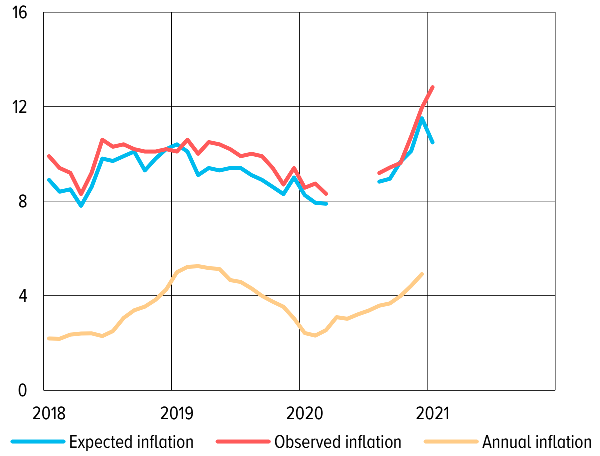
Companies' price expectations. According to the Bank of Russia's surveys, companies' three-month ahead price expectations were higher in October–January than in the previous two quarters (Chart 2.10). Respondents mentioned higher prices for raw materials, components, and supplies as the main reason for the expected increase in prices. The percentage of enterprises referring to the ruble weakening as a reason for the expected price rise lowered in December–January.

Price expectations changed diversely across industries. Price expectations rose in the mining and quarrying sector and in manufacturing, driven by higher input costs and prospects for demand recovery, including in external markets. Retailers' price expectations trended downwards beginning from November, while staying the highest compared to all other industries.

Analysts' inflation expectations. In October–November, analysts[1] reviewed their inflation forecast for 2021 (Chart 2.10). In December 2020–January 2021, their forecasts for 2021 and 2022 remained almost unchanged, staying close to 4%.

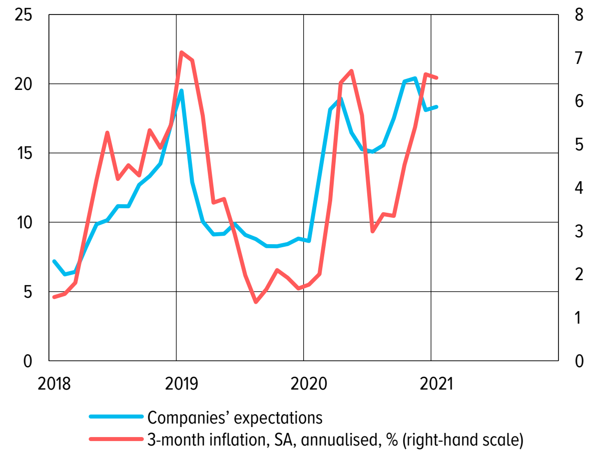
[1] *Surveys by Interfax, Bloomberg, and Thomson Reuters.*

INFLATION OBSERVED AND EXPECTED BY HOUSEHOLDS (MEDIAN ESTIMATE) *Chart 2.9*
(%)



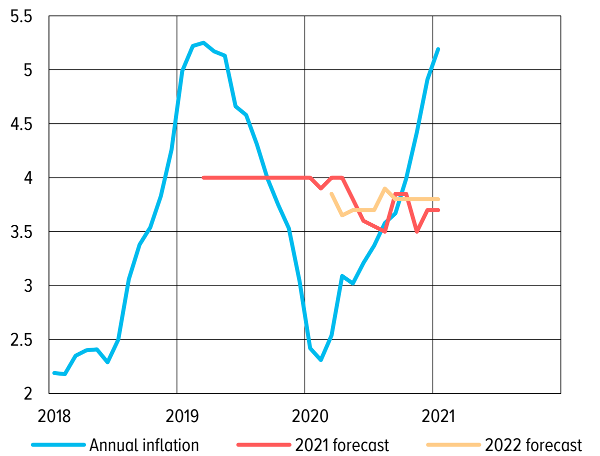
Sources: InFOM, Rosstat.

COMPANIES' PRICE EXPECTATIONS *Chart 2.10*
(balance of responses, %)



Sources: Bank of Russia, Rosstat.

BLOOMBERG ANALYSTS' CONSENSUS FORECAST *Chart 2.11*
(%)



Sources: Bloomberg, Rosstat.

3. THE BANK OF RUSSIA'S MONETARY POLICY

In December and February, the Bank of Russia Board of Directors decided to keep the key rate at 4.25% p.a. Over the period from October, inflation was above the Bank of Russia's forecast. This trend was largely driven by proinflationary factors in individual markets and the continuing pass-through of the ruble depreciation observed in 2020 to prices. According to the Bank of Russia's estimate, the impact of these factors may be longer-lasting and more significant amid a faster recovery of demand, persistent supply-side constraints, as well as the earlier rise in inflation expectations and related secondary effects. Given the above, disinflationary risks do not prevail any more over the horizon of 2021.

The Bank of Russia forecasts that annual inflation will peak in February–March and go down further on. The path of this downward trend will depend on the time when the influence of proinflationary factors tapers off and on the 2020 base effects. The Bank of Russia assumes in its baseline scenario that given the monetary policy pursued, annual inflation will equal 3.7–4.2% in 2021 and will stay close to 4% further on.

If the situation develops in line with the baseline forecast, the Bank of Russia will determine the timeframe and pace for returning to neutral monetary policy. The Bank of Russia will make its key rate decisions, taking into account actual and expected inflation movements relative to the target and economic developments over the forecast horizon, as well as risks created by internal and external conditions and how financial markets respond to them. The Bank of Russia will also factor in highly uncertain current trends in the economy and price movements.

Over the period from October 2020 to the first half of February 2021, the liquidity surplus in the banking sector slightly contracted. As of the end of 2020, it amounted to 0.2 trillion rubles, which was below the Bank of Russia's forecast. The main reasons behind this deviation were a smaller-than-expected liquidity inflow via the budget channel and a larger liquidity outflow in December. In January 2021, the outflow of liquidity through budget accounts resumed, yet it was not offset by a rise in temporary available budgetary funds placed with banks by the Federal Treasury. This was the reason why the banking sector temporarily shifted to the structural liquidity deficit. Beginning from early February, the Federal Treasury increased the amount of its operations. As a result, by the middle of the month the banking sector returned to a steady liquidity surplus which is expected to remain throughout the year. The forecast of the liquidity balance for the end of 2021 equals 0.8–1.4 trillion rubles. This estimate factors in the assumptions that cash will partially return to banks after the elevated demand for it during the pandemic period and that there will be a rise in budgetary funds to be placed with banks.

3.1. KEY RATE DECISIONS

Earlier key rate decisions. In December and February, the Bank of Russia Board of Directors decided to keep the key rate unchanged at 4.25% per annum, maintaining accommodative monetary policy.

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

First, **inflation** was exceeding the Bank of Russia's forecast during the period from October. This trend was largely driven by proinflationary factors in individual markets and the continuing pass-through of the ruble depreciation observed in 2020 to prices. In these conditions, annual inflation rose to 5.2% in January 2021, from 4.0% in October 2020. As assessed by the Bank of Russia, over the period under review, the indicators of the current consumer price growth rates reflecting the steadiest price movements also increased, while staying close to 4% in annualised terms.

The Bank of Russia noted that the impact of these proinflationary factors might be longer-lasting due the growth of households' and businesses' inflation expectations that had occurred in 2020 and the persistent supply-side constraints. Specifically, although households' inflation expectations lowered in January, they still remained elevated as compared to the pre-pandemic period, pushed up by a rise in prices for a range of basic goods and exchange rate volatility. Nonetheless, the Russian Government's measures implemented in December limited the growth of prices for certain food products.

Over the period from October, the containing effect of domestic demand on price dynamics was weakening gradually. According to the Bank of Russia's estimates, it was offset by proinflationary factors over the short-term horizon which arose due to companies' higher input costs, among other things. The strongest influence was exerted by such proinflationary supply-side factors as staff shortages in a number of professions and higher expenses incurred by companies to comply with anti-pandemic requirements.

The Bank of Russia forecasts that annual inflation will peak in February–March and go down further on. The path of this downward trend will depend on the time when the influence of proinflationary factors tapers off and on the 2020 base effects. The Bank of Russia assumes in its baseline scenario that given the monetary policy pursued, annual inflation will equal 3.7–4.2% in 2021 and will stay close to 4% further on.

Second, **monetary conditions** remained accommodative and almost unchanged over the period from October. OFZ yields increased somewhat amid the rise in inflation expectations, the growth of long-term interest rates in global financial markets, and persistent geopolitical tensions. The accelerating pace of vaccination and expected additional fiscal stimulus in individual countries contributed to price growth in financial and commodity markets.

Over the period under review, credit and deposit rates mostly stayed unchanged. However, as price growth rates remained elevated and inflation expectations rose over the recent months, real price lending conditions were eased slightly. Banks also continued to ease non-price lending conditions in a range of market segments. In this environment, lending trended upwards further.

Along with accommodative monetary conditions, lending expansion was still driven by the Russian Government's preferential programmes and regulatory easing. As before, making its key rate decisions, the Bank of Russia will estimate how the termination of these anti-crisis measures will impact monetary conditions.

Third, **economic activity trends** in 2020 in general and over the period from October in particular were better than expected by the Bank of Russia. Specifically, GDP shrank by 3.1% in 2020, which was less than forecast by the Bank of Russia in December (-4.0%). In December, the Bank of Russia expected a possible pause in the economic rebound as the epidemic situation worsened both in Russia and worldwide. However, according to the Bank of Russia's current estimates, the Russian economy continued to recover in 2020 Q4. This was largely owing to the fact that the effective restrictions were targeted (as compared to Q2) and that both households and companies had largely adjusted to the new conditions. In this environment, households' real incomes were recovering and unemployment started to edge down.

In early 2021, the up-to-date indicators of economic activity showed that the economy continued to bounce back. Moreover, the Bank of Russia estimated that the further recovery pace would be supported by an improvement of consumer and business sentiment amid the termination of some restrictions and people's coronavirus vaccination.

The Bank of Russia forecasts that the recovery growth of the Russian economy will reach 3.0–4.0% in 2021. Nonetheless, the extent of the rebound may still significantly vary across industries. According to the baseline scenario, Russia's economy may reach its pre-pandemic level as early as by the end of 2021, and not by mid-2022 as was assumed earlier.

The Bank of Russia forecasts that GDP will expand by 2.5–3.5% in 2022 and 2.0–3.0% in 2023. The medium-term path of economic growth will largely depend on coronavirus pandemic trends in Russia and abroad, the specifics of the rebound in private demand amid potential shifts in households' and businesses' behaviour, and the process of budget consolidation.

Fourth, when making its key rate decisions in December–February, the Bank of Russia factored in that **disinflationary risks lowered over the horizon of 2021, while the impact of short-term proinflationary factors strengthened**. Specifically, the Bank of Russia estimated in February that disinflationary risks no longer prevailed over the horizon of 2021. According to the Bank of Russia's estimate, the influence of proinflationary factors may be longer-lasting and more significant amid a faster recovery of demand, as well as the earlier rise in inflation expectations and related secondary effects.

As was noted by the Bank of Russia, proinflationary pressure may also arise due to currently remaining disruptions in production and logistics chains, as well as extra costs incurred by businesses to protect employees and consumers against the threat of the coronavirus spread. Proinflationary risks stem from changes in domestic prices for individual food products driven by supply-side factors and the situation in respective global markets.

Short-term proinflationary risks are also associated with intensified volatility in global markets caused by, among other factors, a range of geopolitical events, which may affect exchange rate and inflation expectations. In addition, as the global economy is bouncing back faster than expected and, therefore, advanced economies' need in unprecedented fiscal stimuli diminishes, monetary policy normalisation may start earlier in advanced economies. The Bank of Russia assumes that this may become an additional source of higher volatility in global financial markets.

Disinflationary risks for the baseline scenario are mostly associated with a weaker recovery of demand both in Russia and abroad. The economic rebound may slow down due to such factors as the spread on new coronavirus variants, slower vaccine rollouts, and restrictions tightening, etc. Inflation may be contained by steady shifts in households' preferences and behaviour, including a potential consistent increase in their propensity to save, and a slower recovery of households' incomes. Furthermore, the reopening of borders as restrictions are lifted may drive a recovery in the consumption of foreign services and weaken supply-side constraints in the labour market owing to an inflow of labour migrants.

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

Since fiscal policy also significantly impacts medium-term inflation, the Bank of Russia's baseline scenario takes into account the parameters of the federal budget and budgets of the constituent entities of the Russian Federation presented in the Guidelines for Fiscal, Tax and Customs and Tariff Policy for 2021 and the 2022–2023 Planning Period, as well as the announced schedule of the termination of the

Russian Government's and the Bank of Russia's anti-crisis measures.

According to the Bank of Russia's estimate, there is generally a balance between proinflationary and disinflationary risks over the forecast horizon.

Medium-term monetary policy. The Bank of Russia considers that the potential for further monetary policy easing has been exhausted since this may provoke an additional rise in proinflationary risks. If the situation develops in line with the baseline forecast, the Bank of Russia will determine the timeframe and pace for returning to neutral monetary policy. The Bank of Russia will make its key rate decisions, taking into account actual and expected inflation movements relative to the target and economic developments over the forecast horizon, as well as risks created by internal and external conditions and how financial markets respond to them. The Bank of Russia will also factor in highly uncertain current trends in the economy and price movements.

The baseline scenario provides for a gradual return to neutral monetary policy. Nonetheless, Russia's monetary policy will remain accommodative on average throughout 2021, supporting the recovery of the Russian economy. Throughout the forecast horizon, the Bank of Russia will pursue monetary policy in such a way as to ensure inflation stabilisation close to 4%.

Effect of the decisions made on key rate expectations. Since the release of MPR 4/20, market participants have partially adjusted upwards their expectations regarding the key rate. In particular, the number of analysts expecting the key rate to be cut at the end of 2020 or over the horizon of 2021 has been decreasing gradually.

Following the Board of Directors' meeting in October when the key rate was kept at 4.25% p.a., the Bank of Russia preserved its message that it will explore the need for further key rate reduction if the situation develops in line with the baseline forecast. In these conditions, analysts predominantly continued to expect the key rate to remain unchanged at 4.25% p.a. until the end of 2020, although some assumed that it might be cut by 25 bp in December. As regards the level of the key rate in 2021, the majority expected it to stay in the range of 4.00–4.25% p.a.

As the time of the December meeting of the Bank of Russia Board of Directors approached, market participants strengthened the consensus that the key rate would not be changed at the upcoming meeting. This was largely the result of the intensified impact of proinflationary factors compared to October, which were associated with the situation in individual product markets and exchange rate volatility. Another factor was the persistent uncertainty caused by the worsening epidemic situation both in Russia and abroad.

At its December meeting, the Bank of Russia Board of Directors also kept the key rate at 4.25% p.a. In its communication following the meeting, the Bank of Russia noted that the impact of proinflationary factors had become stronger, while disinflationary risks were losing their prevalence over the horizon of 2021. The Bank of Russia also stressed that, given highly uncertain current trends in the economy and price movements, it will analyse future developments and the potential for further key rate reduction.

In this environment, analysts slightly adjusted their expectations upwards, predominantly assuming that the key rate would remain at 4.25% p.a. throughout 2021. Conversely, according to key rate expectations based on money market indicators, it was still assumed that the key rate might be raised slightly in 2021.

Given the Bank of Russia's communication in December and inflation trends in late 2020–early 2021, as the time of the February meeting of the Bank of Russia Board of Directors approached, analysts and financial market participants strengthened the consensus that the key rate would not be changed at the upcoming meeting.

At its meeting in February, the Board of Directors kept the key rate at its current level. The Bank of Russia communicated that if the situation develops in line with the baseline forecast, it will determine the timeframe and pace for returning to neutral monetary policy. In these conditions, analysts predominantly continued to expect that the key rate would not be changed in 2021. However, a part of them started to assume that the key rate might be increased by 25 bp in 2021 H2.

According to the majority of analysts, the time when the Bank of Russia starts to shift towards neutral monetary policy will largely depend on the duration of proinflationary factors, the scale of fiscal consolidation, the pace of the further economic rebound, global reflation prospects, and the overall situation in financial and commodity markets affected by geopolitical factors, among other things.

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

Banking sector liquidity. The structural liquidity surplus contracted on average across required reserve averaging periods from 1.8 trillion rubles in September–October 2020 to 0.3 trillion rubles in October 2020–February 2021. As of the end of 2020, it amounted to 0.2 trillion rubles, which was below the Bank of Russia's forecast of 1.0–1.4 trillion rubles. The main reasons behind this deviation were a smaller-than-expected liquidity inflow via the budget channel and a larger liquidity outflow in December.

Cash in circulation. In October 2020, the outflow of liquidity caused by the increased amount of cash in circulation slowed down and was close to its seasonal levels, while in November, for the first time since January, it reversed to a slight inflow as cash partially returned to banks. Owing to the accumulated cash holdings, households and businesses more calmly responded to the autumn rise in the sickness rate. In December, the outflow of liquidity was mainly driven by the seasonal increase in the amount of cash in circulation. Its changes were close to last year's readings as economic agents did not return the earlier withdrawn cash to banks, while credit institutions were replenishing their cash offices and ATMs in amounts equivalent to those in December 2019. However, the Bank of Russia's forecast included the assumption that a rise in the demand for cash would be lower owing to the already existing holdings. Eventually, the outflow of liquidity due to cash as of the end of the year turned out to be larger than expected.

In January, after the New Year holidays, the amount of cash in circulation decreased, which is typical of this season. Nonetheless, the inflow of funds due to this factor was slightly smaller than in previous years, namely 0.2 trillion rubles against 0.4 trillion rubles in January 2020.

Budget account operations. In October–November 2020, operations in the budget system's accounts were the key factor of the liquidity outflow. As economic activity was bouncing back in the previous months, payments of the main non-oil and gas taxes (VAT, profit tax, personal income tax) to the budget increased to pre-pandemic levels. Another reason for the liquidity reduction in the banking sector was public companies' dividend payments rescheduled from summer to October. Furthermore, Russia's Ministry of Finance continued to expand its OFZ offerings.

The outflow of liquidity caused by the above factors was offset only partially by the inflow of funds to the banking sector as budgetary expenditures and operations to place temporarily available budgetary funds. The Federal Treasury did not place the entire amount of received revenues and borrowings with the banking sector.

In contrast, a seasonally large amount of budget account operations became a factor of the liquidity inflow in December 2020. However, this inflow was considerably below expectations. This was associated with an increase in tax revenues and reduced budget spending. According to the Bank of Russia's forecast, a potential impact of higher budget revenues or reduced spending on liquidity was to be fully offset by a corresponding increase in operations carried out by the Federal Treasury and other budget process participants to place temporarily available funds with banks. However, this did not happen, and the balances of funds of the budget system with the Bank of Russia increased by 1.2 trillion rubles as of the end of 2020.

In January 2021, the outflow of liquidity through budget accounts resumed. Due to seasonal factors, budget revenues exceed expenditures at the beginning of the year. However, this year, there was no offsetting rise in the Federal Treasury's placements of temporarily available budgetary funds. This was the reason why the banking sector temporarily shifted to the structural liquidity deficit. At the beginning of February, the inflow of liquidity through the budget channel resumed.

The **forecast of the structural liquidity surplus for the end of 2021** equals 0.8–1.4 trillion rubles. This forecast factors in the assumption that cash will gradually return to banks, after the rise in the demand for it during the pandemic period. However, this process may take several years. According to estimates, the amount of cash in circulation will decrease by 0.2–0.4 trillion rubles in 2021. In addition, the Federal Treasury is expected to reduce the balances of budgetary funds in its accounts with the Bank of Russia. As a result, temporarily available funds to be placed by the budget system with banks will exceed previous years' amounts. It is estimated that an additional amount of 0.7–1.0 trillion rubles may be placed with banks as of the end of the year. Furthermore, an inflow of liquidity in the amount of 0.2 trillion rubles will be ensured by budget expenditures to be financed using the remaining profit received by the Bank of Russia from the sale of the equity stake in Sberbank in 2020.

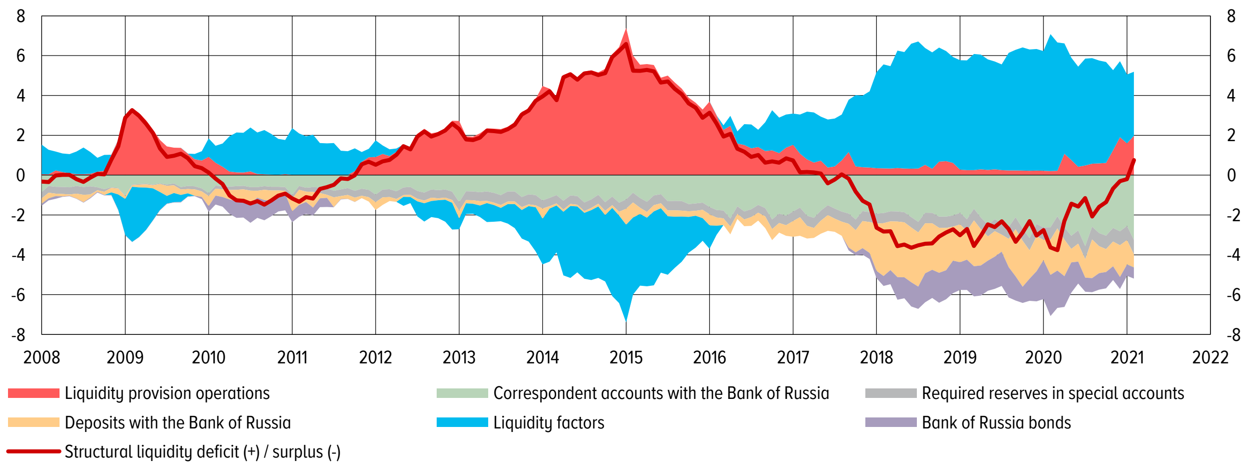
Monetary policy instruments. The Bank of Russia continued to hold one-month fixed-rate repo auctions and one-year floating-rate repo auctions. In October–November, amid the outflow of liquidity through the budget channel, the Bank of Russia raised the threshold amount of liquidity provided at its one-month repo auctions from 0.4 trillion rubles to 1.0 trillion rubles and then to 1.5 trillion rubles. As a result, banks raised over 1.2 trillion rubles through these operations. In December and January, the Bank of Russia kept the maximum amount of funding provided at its one-month repo auction at 1.5 trillion rubles. In the first half of December, banks' demand for these operations trended downwards to 0.8 trillion rubles; yet, following the auction in January, their liabilities increased anew, to total 1.1 trillion rubles. A range of banks expected the inflow of funds through the budget channel (as expenditures and/or placements of the Federal Treasury) to be more significant in December. Eventually, since the inflow of funds turned out to be below the forecast, they offset this by increasing their repo operations with the Bank of Russia.

Amid the contracted surplus of the banking sector's liquidity in October–November, banks reduced their investment in Bank of Russia coupon bonds (coupon OBRs) by 0.2 trillion rubles, to 0.6 trillion rubles. In December, the Bank of Russia made the decision not to hold the auction for the placement of the 40th coupon OBR issue, in order to ensure greater flexibility in absorbing liquidity through its one-week deposit auctions.

In the coming months, further changes in the structural liquidity surplus will primarily depend on budget operations. From early February, the Federal Treasury resumed funds placements with banks, increasing their amounts. If current

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

Chart 3.2.1



Source: Bank of Russia calculations.

trends continue, the banking sector will return to a steady liquidity surplus.

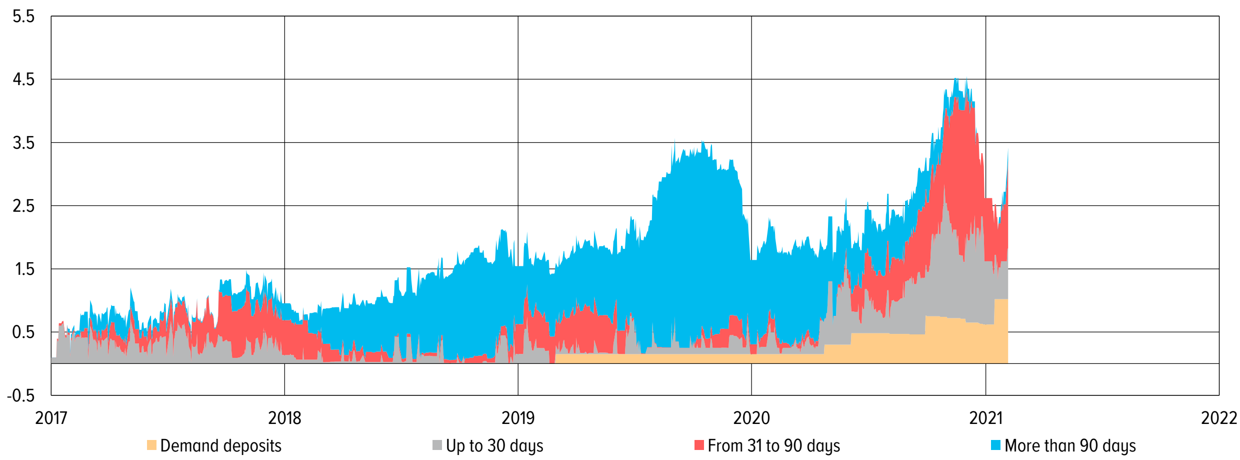
The Bank of Russia carries out daily analysis of fiscal flows and factors in their dynamics in its banking sector liquidity forecast. The Bank of Russia's operations make it possible to promptly balance the situation with liquidity at any point of time and ensure the efficient management of money market rates.

Achieving the operational objective of monetary policy. Short-term interbank lending rates in the money market predominantly stayed in the lower half of the interest rate corridor close to the Bank of Russia key rate. The average spread equalled -8 bp in October 2020–February 2021 (vs -16 bp in Q3), fluctuating from -67 to +18 bp (vs from -54 to +13 bp in Q3).

The outflow of liquidity from the banking sector through the budget channel in October 2020 caused short-term imbalances in liquidity distribution among credit institutions, which put upward pressure on IBL rates. A number of banks built up their net borrowings to process large transactions. In addition, as foreign currency liquidity slightly contracted, this pushed up the demand for rubles in the IBL segment on the part of some market participants. In November 2020, the outflow of liquidity from banks slowed down, and they adjusted to the changed conditions. As a result, the demand for rubles in the overnight IBL segment decreased, including from those

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

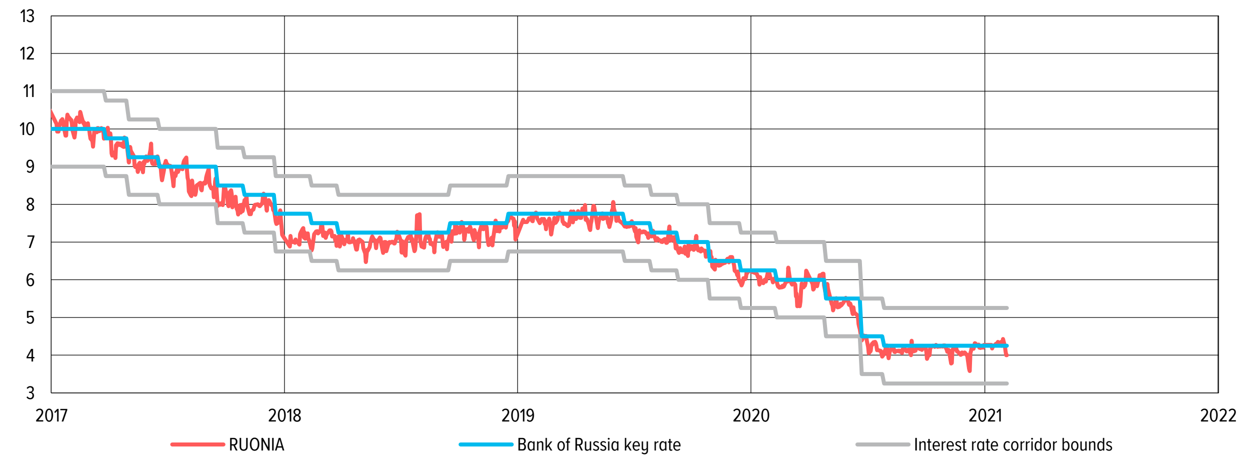
Chart 3.2.2



Sources: Federal Treasury, Bank of Russia calculations.

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

Chart 3.2.3



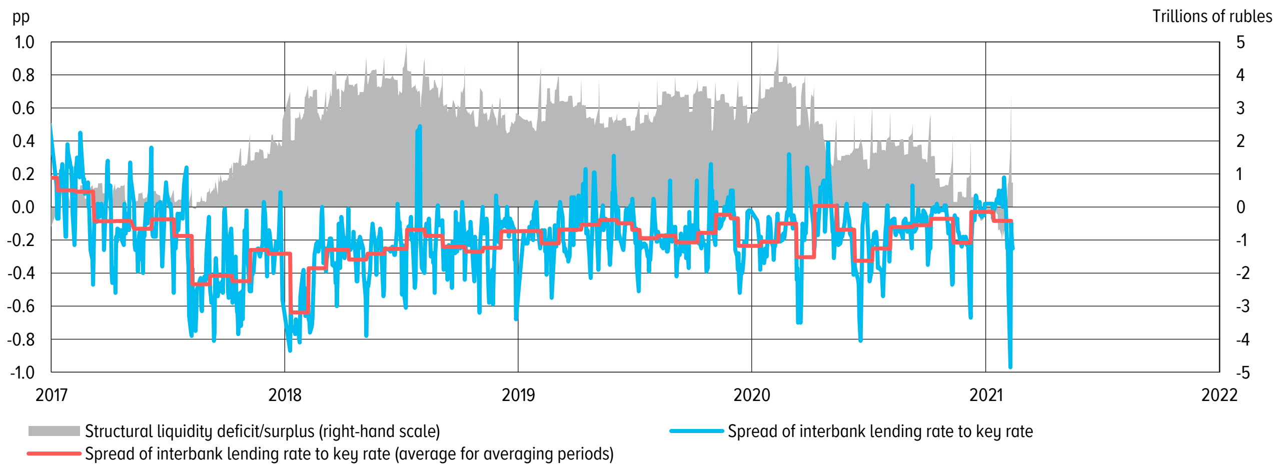
Source: Bank of Russia.

market participants who had earlier demonstrated significant demand for OFZ bonds. This in turn put downward pressure on money market rates.

In December, expecting a substantial inflow of budgetary funds at the end of the year, a number of credit institutions opted to avoid a considerable increase in their correspondent account balances in the middle of the month, slightly delaying their required reserves averaging. However, since the inflow of budgetary funds and the Federal Treasury's placements with banks were below expected levels, a range of credit institutions raised the demand for rubles in the IBL segment at the end of the year, which triggered an increase in interest rates and the demand for the Bank of Russia's fixed-rate refinancing operations. In January 2021, IBL rates formed primarily above the Bank of Russia key rate due to a rise in the demand for liquidity following large outflows through the budget channel and under Federal Treasury operations. The uncertainty about the time and amount of the resumption of these operations was a reason why Bank of Russia loans at a fixed interest rate remained requested and borrowings in the IBL and FX swap segments increased. At the beginning of February, the Federal Treasury resumed its operations, following which the demand for liquidity in the market declined and the spread between IBL rates and the Bank of Russia key rate returned to negative territory.

STRUCTURAL LIQUIDITY SURPLUS AND MONEY MARKET RATES

Chart 3.2.4



Source: Bank of Russia calculations.

STRUCTURAL LIQUIDITY SURPLUS AND LIQUIDITY FACTORS
(trillions of rubles)

Table 3.2.1

	October 2020	November 2020	December 2020	January 2021	2021 (forecast)
1. Liquidity factors	**-1.1**	**-0.2**	**-0.4**	**-0.3**	**[1.0; 1.5]**
- change in the balances of funds in general government accounts with the Bank of Russia, and other operations*	-1	-0.2	0.1	-0.5	[0.9; 1.2]
- change in cash in circulation	-0.1	0.0	-0.5	0.2	[0.2; 0.4]
- regulation of banks' required reserves with the Bank of Russia	0.0	0.0	0.0	0.0	-0.1
2. Change in free bank reserves (correspondent accounts)	**-0.4**	**0.2**	**-0.3**	**0.7**	**[0.3; 0.4]**
3. Change in banks' claims on deposits with the Bank of Russia and coupon OBRs	**0**	**0.3**	**-0.4**	**-0.6**	**[-0.8; -0.2]**
4. Change in outstanding amounts on Bank of Russia refinancing operations (4 = 2 + 3 - 1)	**0.6**	**0.7**	**-0.3**	**0.4**	**-1.4**
Structural liquidity deficit (+) / surplus (-) (as of the period-end)	**-0.7**	**-0.3**	**-0.2**	**0.8**	**[-1.4; -0.8]**

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

BOXES

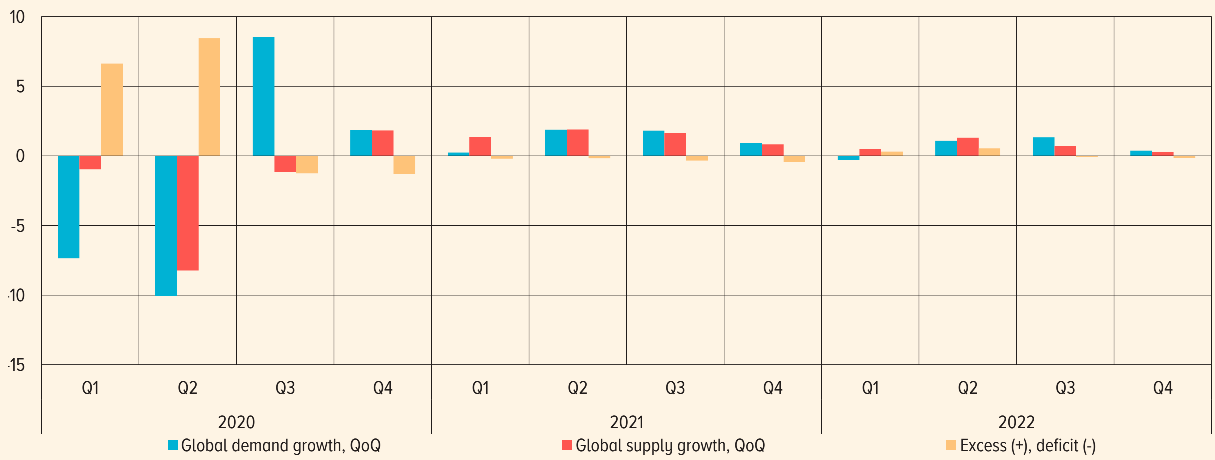
GLOBAL OIL DEMAND AND SUPPLY AMID THE PANDEMIC

In 2020 H1, the coronavirus pandemic provoked an unprecedented oil demand shock, which became the largest in recent years. The demand for fuel plummeted due to quarantine restrictions imposed in the majority of countries and the decline in transportation. The suspension of enterprises' operation induced a slump in oil consumption. Accordiwng to different assessments (Table 1), the demand for oil in 2020 declined by 9–10 mbd compared to the previous year, with the most significant decrease (by approximately 20 mbd against December 2019) recorded in April. In order to stabilise the situation in the oil market, oil countries at the G20 and OPEC+ meetings in April made the decision to reduce oil production by 9.7 mbd in May–June. Pursuant to the original arrangements, the decrease in OPEC+ oil production was to be lowered from the base level to 7.7 mbd in 2020 H2 and to equal 5.8 mbd in January 2021–April 2022.

Beginning from May, the demand for oil started to bounce back gradually. Coupled with limited supply (according to the OPEC+ decision, the May–June quotas were extended to July, while oil production in the USA was contained by low prices and oil producers' financial discipline), this ensured a rise in oil prices and their subsequent stabilisation in the range of 45–50 US dollars per barrel amid the persistent risks of a resurgence of coronavirus cases. In November 2020, price growth resumed, driven by the news about a high efficiency of vaccines being developed and the start of vaccination expected in the near future. In January 2021, prices were also supported owing to the OPEC+ decision implying that oil production should be expanded more slowly at the beginning of the year (by 0.5 mbd in January and by 0.075 mbd in February and March) and that Saudi Arabia should cut oil production by 1 mbd in February–March (in addition, it was also agreed to extend compensation plans for underproduction by individual countries until the end of March 2021).

In the next few years, the demand for oil will continue to rise as economies recover from the aftermath of the coronavirus. However, the risks of new pandemic waves and the extension of the existing restrictions remain. Nonetheless, a surge in US oil production with oil prices staying below 60 US dollars per barrel is unlikely due to the increased financial discipline of shale oil producers and the new administration's environment protection policy. In these conditions, the OPEC+ policy will remain the key in balancing the oil market and prices as the recovery of global demand will most probably exceed the increase in production by other countries. As forecast by market participants (Chart 1), the reduction in oil stocks that began in June 2020 will continue in 2021. In 2022, demand and supply in the oil market will be more balanced.

AVERAGED FORECAST OF BALANCE IN THE OIL MARKET (IHS, EIA, WOOD MACKENZIE) *Chart 1*
(mpd)



Sources: IHS, EIA, Wood Mackenzie.

FORECAST CHANGE IN DEMAND/SUPPLY IN THE OIL MARKET
(mbd, YoY)

Table 1

	US Department of Energy (EIA, 12.01.2021)			OPEC (14.01.2021)		Wood Mackenzie (05.02.2021)			IHS (15.01.2021)		
	2020	**2021**	**2022**	**2020**	**2021**	**2020**	**2021**	**2022**	**2020**	**2021**	**2022**
Brent price, USD per barrel	42	53	53	-	-	42	59	58	42	57	60
Global demand	**-9.0**	**5.6**	**3.3**	**-9.8**	**5.9**	**-9.8**	**6.4**	**3.0**	**-10.3**	**5.9**	**3.8**
China	-0.5	0.9	0.4	-0.4	1.1	-0.4	1.3	0.7	-0.6	1.4	0.7
OECD	-5.6	2.5	1.7	-5.5	2.6	-5.8	2.5	1.3	-5.8	2.1	1.8
Non-OECD (excluding China)	-2.9	2.2	1.2	-3.8	2.2	-3.6	2.6	1.0	-3.9	2.4	1.3
Global supply	**-6.4**	**2.9**	**3.5**	**-6.3**	**-**	**-5.7**	**1.8**	**3.4**	**-6.7**	**3.0**	**4.6**
OPEC	-4.1	1.6	1.2	-3.8	-	-3.4	0.7	1.7	-3.9	1.5	2.3
USA	-0.9	0.1	0.9	-0.8	0.4	-0.6	0.1	0.5	-0.9	0.1	0.4
Russia	-1.0	0.1	0.9	-1.0	-0.2	-1.0	0.3	0.7	-1.0	0.0	0.8
Other non-OPEC countries	-0.4	1.0	0.5	-0.7	0.7	-0.5	0.5	0.4	-0.3	0.9	0.8
Changes in stocks	**2.0**	**-0.7**	**-0.5**	**3.5**	**-**	**4.4**	**-0.3**	**0.2**	**2.9**	**0.1**	**0.8**

Sources: OPEC, IHS, Wood Mackenzie, EIA.

Given the above factors (including the risks of a resurgence of coronavirus cases and a faster rise in OPEC+ quotas following the recent growth of oil prices), the Bank of Russia maintains a rather conservative view of the medium-term oil price path, increasing the oil price in its baseline scenario by 5 US dollars per barrel in 2021–2022 to 50 US dollars per barrel, as compared to MPR 4/20. It should be noted that despite February’s oil price rise to 60 US dollars per barrel, largely associated with optimism about the demand recovery and OPEC+ production cuts, as well as the US production decline due to the unprecedented cold weather, international organisations have not revised their statistics and forecasts, which implies that there is a risk of a downward adjustment of prices in the short run. Moreover, marginal oil production costs that are essential for pricing in the medium term have changed only slightly, which is confirmed by the long end of the futures curve.

ADJUSTING QUARTERLY GDP DATA SERIES ACCORDING TO REVISED ANNUAL ASSESSMENTS

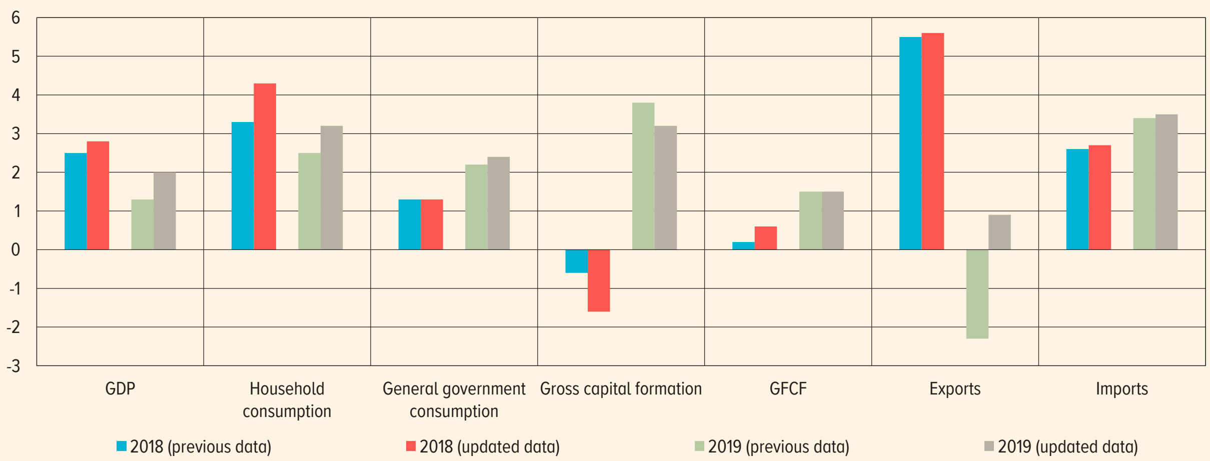
On 30 December 2020, Rosstat released the third assessment of GDP for 2019 and the fifth assessment of GDP for 2018 (Chart 1).

The annual GDP growth rate for 2018 was raised by 0.3 pp to 2.8% (the largest revision was for household final consumption expenditure and GFCF). The annual GDP growth rate for 2019 was adjusted upwards by 0.7 pp to 2.0% (the largest revision was for household final consumption expenditure and exports). However, the updated quarterly series used to prepare materials supporting monetary policy decisions will be released by Rosstat in April 2021. This creates the problem of the lack of comparability of the available quarterly data and new annual results. Generally, the adjustment of GDP assessments over a year is based on the revisions of the assessments for all quarters, while dynamics over a quarter may significantly change. The forecast of new quarter-on-quarter rates over a year is a rather labour-intensive task in terms of both the search for indicators identifying the true rates and the evolving seasonality in GDP components, as well as a high probability of an error in seasonally adjusted data series. In order to employ all available information for delivering a more precise assessment of the output gap, the Bank of Russia has adjusted the data series based on the following assumptions:

- The growth rate was changing evenly over the year, as a result of which the quarterly growth rates were changing by the same constant value.
- Seasonal factors were unchanged, with the existing quarter-on-quarter dynamics remaining the same.
- Adjusted GDP as of the end of the year is in line with Rosstat's updated assessment for the year.

The same approach was applied to adjust the quarterly data series after the release of the first assessment of GDP for 2020 (-3.1%) on 1 February 2021. One of the standard approaches to take into account the annual assessment, with information available for the first three quarters, is to make an additional calculation for the fourth quarter (the imputed growth rate delivering the assessment for a year). However, if applied to the 2020 performance, this method may produce unsatisfactory results. Specifically, if final consumption remains unchanged in Q1–Q3, to find the actual value for the year, final consumption growth in Q4 shall approximate 4.5% QoQ (SA) and general government final consumption expenditure shall equal about 10% QoQ (SA). Given the available statistics on trade and commercial services for October–December 2020, such a significant change in the last quarter of the year seems hardly probable. Therefore, using the same set of assumptions similarly to the adjustment of the data series for 2018–2019, the Bank of Russia uniformly adjusted the quarterly data series for 2020. They were used to prepare the Bank of Russia's medium-term forecast in the baseline scenario. The resulting path is technically a more reliable approximation of current statistics compared to using completely unadjusted data series or data

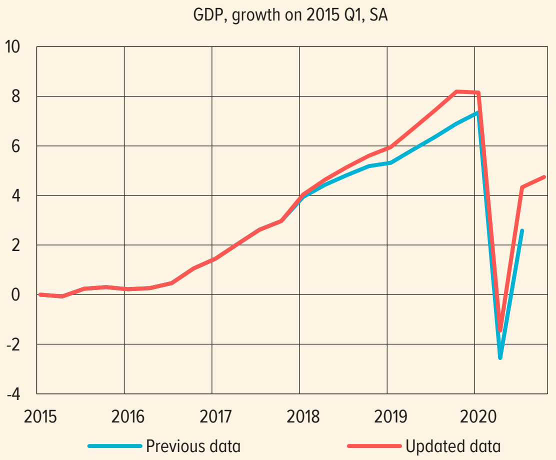
UPDATED GDP ASSESSMENTS IN 2018–2019 *Chart 1*

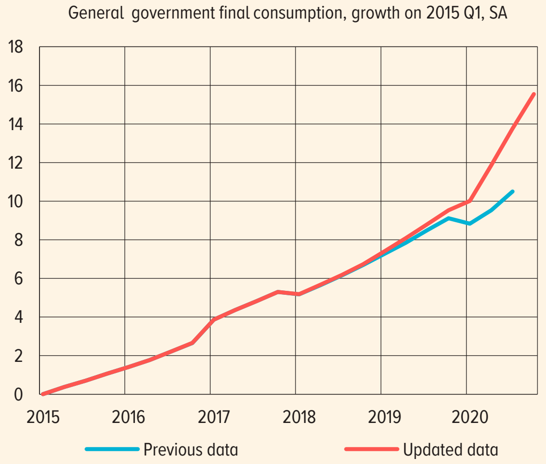


Sources: Rosstat, Bank of Russia calculations.

COMPARISON OF ADJUSTED TIME SERIES AND PREVISOUSLY RELEASED ONES

Chart 2

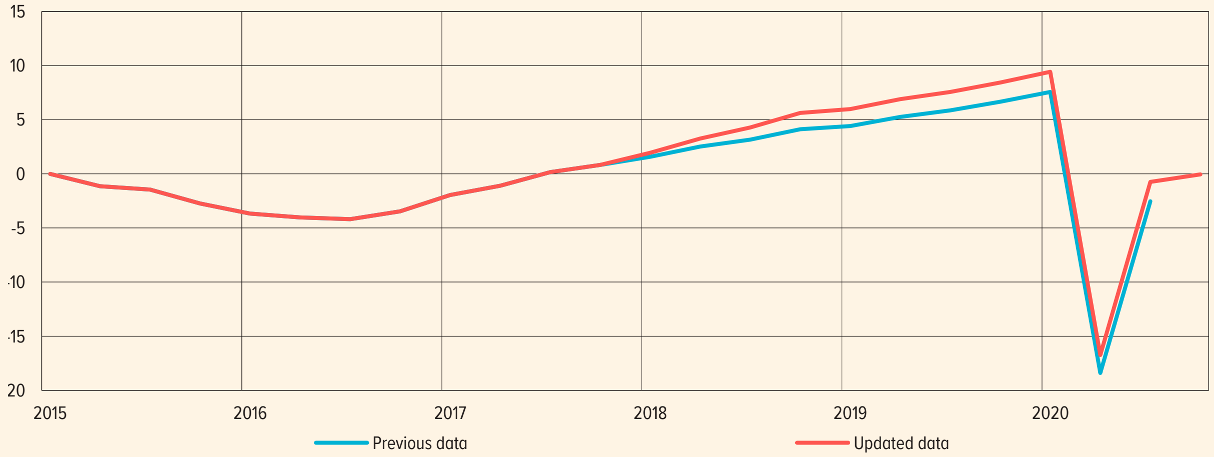




Sources: Rosstat, Bank of Russia calculations.

HOUSEHOLD FINAL CONSUMPTION, GROWTH ON 2015 Q1, SA
(%)

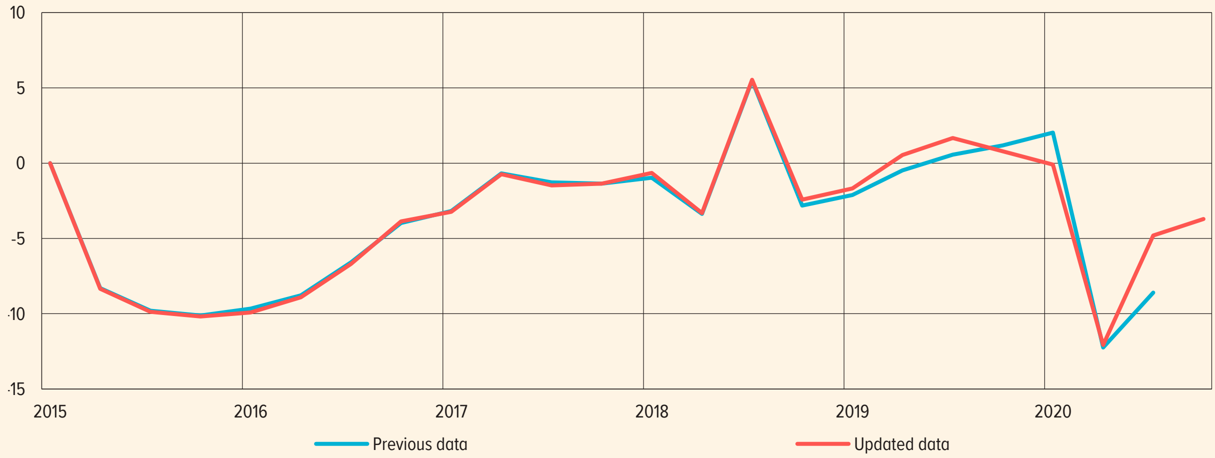
Chart 3



Sources: Rosstat, Bank of Russia calculations.

GFCF, GROWTH ON 2015 Q1, SA

Chart 4



Sources: Rosstat, Bank of Russia calculations.

series adjusted as of the last quarter of 2020 (Chart 2). Moreover, it should be noted that there is no single true method for adjusting quarterly data series; therefore, adjustment results obtained using any method available will most probably differ from final assessments.

In its next Monetary Policy Report (to be published on 4 May 2021), the Bank of Russia will apply Rosstat's actually revised quarterly GDP data series to be released on 1 April.

PHARMACEUTICAL OUTPUT IN LATE 2020–EARLY 2021[1]

In November–December 2020, Russia recorded a surge in the output of pharmaceuticals and medical instruments. Its overall increase in Q4 was 13.7% quarter-on-quarter (SA; vs +2.2% in Q3). **Moreover, December's growth of output in this category was the major contributor to the monthly rise in manufacturing output (SA; 0.6 of 0.9 pp) and became a significant factor of its annual growth (1.3 of 4.4 pp).**

This accelerated growth was almost fully driven by a considerable expansion of **the output of medicines and medical goods**. Its average monthly rise (SA) sped up to 36% in November–December, and output reached its record high. This upward trend was driven by several factors.

First, the rise in coronavirus cases in Russia resumed from mid-September and continued until the end of December. According to the *information* from the anti-coronavirus task force, the daily growth rate of coronavirus cases was up 4.8 times from 15 September through 31 December, and the overall number of newly identified coronavirus cases in Russia exceeded 2 million people. In this situation, people substantially increased the demand for medicines, first and foremost those included in *the coronavirus treatment regimen approved by Russia's Ministry of Health*, specifically antibiotics (azithromycin, levofloxacin), anticoagulants (enoxaparin sodium, rivaroxaban), immunomodulators (recombinant interferon, umifenovir), and immunosuppresants (hydroxychloroquine, tocilizumab), etc. Furthermore, as the epidemic situation worsened, people preferred to purchase these medicines, including in advance. This entailed temporary shortages in the pharmaceutical market that became most acute at the end of the autumn. In order to eliminate this gap, enterprises significantly expanded their output in November–December. Moreover, the Government increased its purchases of medicines, especially those with supply problems. In addition, in order to improve the process of pharmaceuticals supply to the market, beginning from 6 November the authorities simplified the procedure for the mandatory marking of pharmaceuticals.[2] As reported by *TASS* with reference to Russia's Ministry of Industry and Trade, the average weekly output of anti-coronavirus medicines in November 2020 expanded by 65% month-on-month.

Second, the market recorded shortages not only of anti-coronavirus medicines, but also of oncology medicines in 2020. In view of this, the Government established an interagency task force at the beginning of December 2020 which approved the decision to expand the output of 26 oncology medicines until the end of 2020 and in 2021. According to Rosstat, the output of anti-tumour medicines and immunosuppresants increased 2.3 times in December 2020, in annualised terms.

Third, the list of the groups of people who became eligible in Russia for coronavirus vaccination with Russia's Sputnik V expanded considerably in December. By the end of the month, the vaccine was approved for people aged 60+ as well. According to *Russia's Ministry of Industry and Trade*, as of 9 February Russia produced 8.6 million two-component doses of the Sputnik V vaccine at six facilities, with target output until the end of Q1 totalling more than 30 million doses, which will enable the vaccination of approximately 30% of Russians. Moreover, 5.4 million doses of EpiVacCorona, another Russian coronavirus vaccine, are planned to be produced by the middle of the year.

In addition to medicines, the output of pharmaceutical substances was also steadily growing in 2020. Just as medicines, it reached its record high in December 2020. The output of pharmaceutical substances intended to manufacture medicines, including vaccines, expanded due to the surge in the demand for medicines. The increase in the output of pharmaceutical substances resulted from the rise in the output of medicines, including vaccines and antibiotics. It was also driven by a reduction in imported substances from China caused by temporary disruptions in production and logistics chains in 2020.

The majority of factors influencing the development of the pharmaceutical industry at the end of 2020 will also remain in 2021. Given the target output of coronavirus vaccines, its contribution to a rise in the output of medicines is expected to increase. In this regard, the contribution of the pharmaceutical industry to growth in manufacturing will most likely remain quite significant in 2021.

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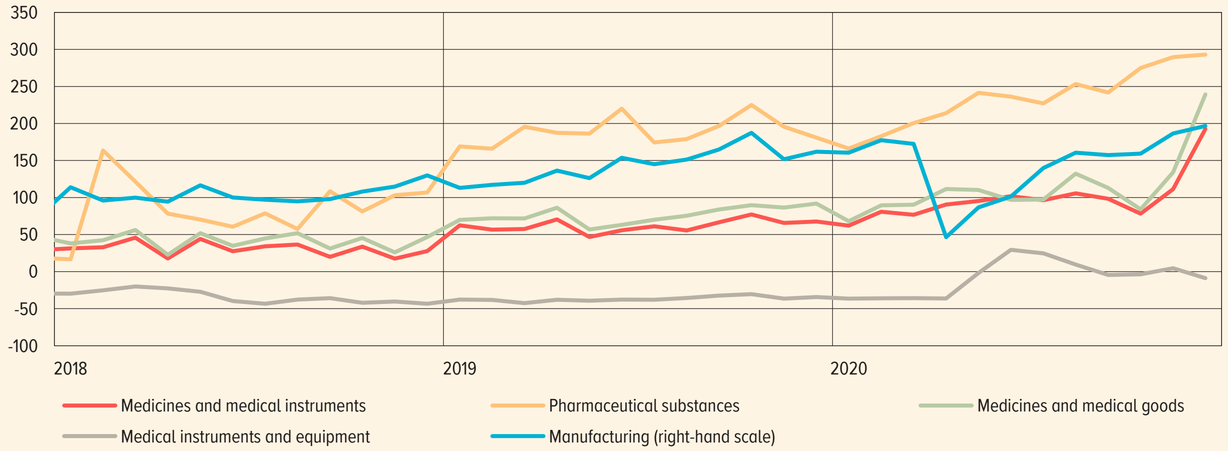
[1] *Hereinafter, the estimates provided do not take into account the data released on 15 February 2021, including the revised statistics for December 2020.*

[2] *Russian Federation Government Resolution No. 779, dated 2 November 2020, 'On Amending the Regulation on the System for Monitoring the Turnover of Human Medicines'.*

OUTPUT OF MEDICINES AND MEDICAL INSTRUMENTS
(% change on December 2015, SA)

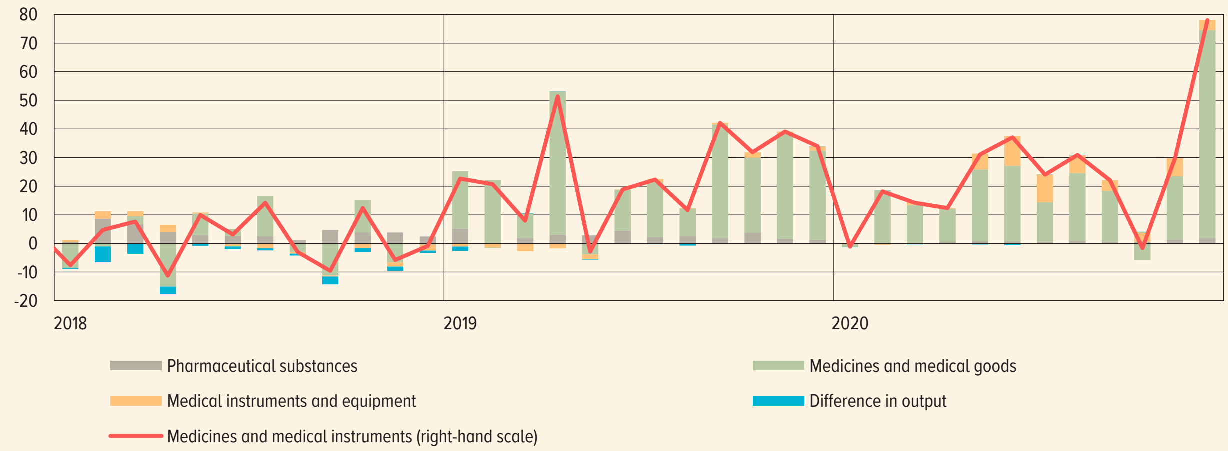
Chart 1



Sources: Rosstat, Bank of Russia calculations.

MEDICINES AND MEDICAL INSTRUMENTS
(contribution to annual growth, pp)

Chart 2



Sources: Rosstat, Bank of Russia calculations.

SITUATION IN THE SUGAR AND SUNFLOWER OIL MARKETS IN OCTOBER 2020–JANUARY 2021

In October–December 2020, the accelerated growth of sugar and sunflower oil prices accounted for over two-thirds of the rise in food inflation.

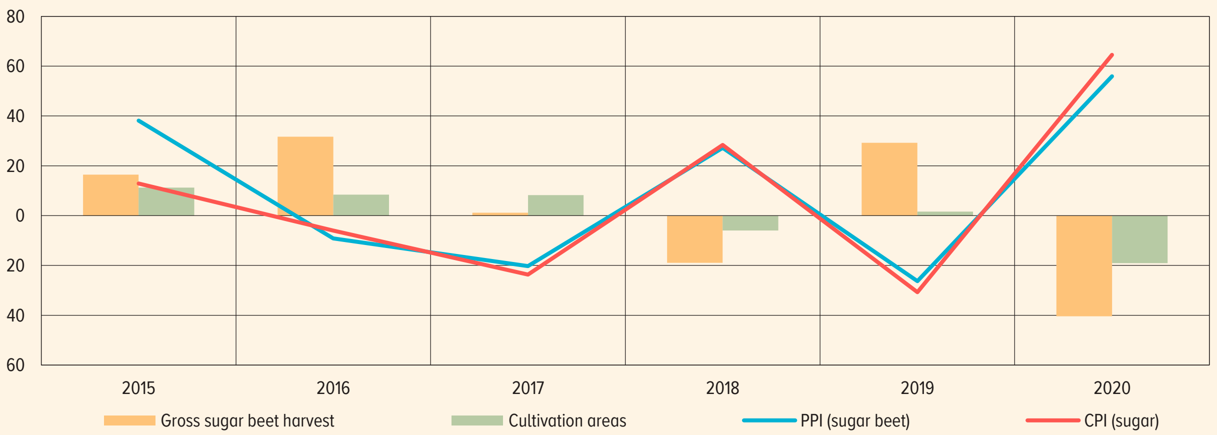
The surge in sugar prices was largely provoked by a reduction in the total yield of sugar beet, which is estimated at 40.4% according to preliminary data (Chart 1). The decline in the harvest was expected since agricultural producers had decreased their cultivation areas significantly (by 19.1%) in order to reduce the excess supply formed over previous years and restore their profitability. In order to address this task, they also expanded sugar supplies to CIS countries. However, due to unfavourable weather conditions decreasing the harvest, the decline in the total yield turned out to be two times larger than the reduction in cultivation areas. Higher prices for agricultural raw materials sped up the growth of consumer prices for sugar. Overall, this was catch-up growth, and the total rise in sugar prices over the past five years did not exceed inflation over the same period. Nonetheless, the surge in prices was extremely fast, with the annual growth in November reaching 65.17% (vs 12.12% in September). According to InFOM's survey commissioned by the Bank of Russia, beginning from November sugar was mentioned by respondents as the product demonstrating the most significant price growth rate (in September, it took the 16th position on the list of products most frequently referred to by households due to considerable price rises).

The increase in sunflower oil prices was less significant, yet also rather fast. Among other factors, it was driven by a decline in the total yield of sunflower seeds, which is estimated at 13.7% according to preliminary data. As in the sugar beet market, this decline resulted from producers' efforts to ensure a balance in the market by reducing cultivation areas. The decrease in the harvest in Russia being the major sunflower exporter, as well as in other countries supplying this crop provoked a rise in its global prices. Coupled with the ruble weakening, this entailed an increase in export prices (Chart 2). Another factor driving the expansion of sunflower exports was that in November Turkey, accounting for the largest share of sunflower exports from Russia, introduced a zero import duty on sunflower seeds. Eventually, sunflower producers raised domestic prices, including for sunflower products. The annual growth of consumer prices for sunflower oil surged from 6.61% in September to 23.84% in November. It moved from the 23rd position in September to the 10th position in November on the list of products most frequently mentioned by households for significant price rises.

In the middle of December, the Russian Government responded to the surge in sugar and sunflower oil prices by signing the agreement with major retailers and producers setting maximum retail prices to remain effective from 20 December 2020 until 1 April 2021. In addition, the Government raised export duties on sunflower seeds from 9 January through 30 June. The Government also plans state support measures for domestic sugar producers.

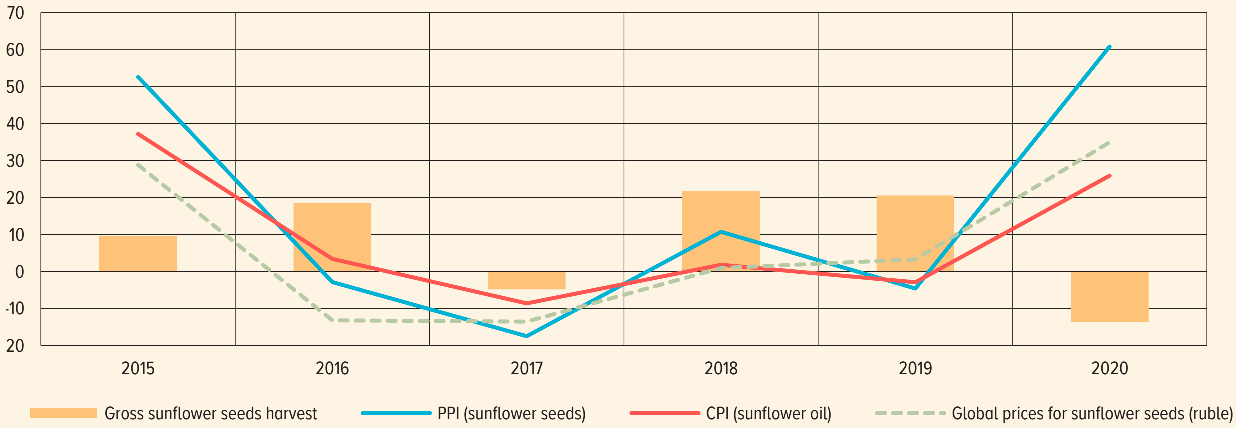
SUGAR BEET HARVEST, PRODUCER PRICES AND CONSUMER PRICES FOR SUGAR
(% change on the same period of the previous year)*

Chart 1



** Price indices are given as the ratio of values for December this year to previous December.*
Sources: Rosstat, IMF, Bank of Russia calculations.

HARVEST, GLOBAL AND DOMESTIC PRICES FOR SUNFLOWER SEEDS, AND CONSUMERS PRICES FOR SUNFLOWER OIL *Chart 2*
(% change on the same period of the previous year)*



** Price indices are given as the ratio of values for December this year to previous December.*
Sources: Rosstat, IMF, Bank of Russia calculations.

The above administrative measures helped normalise the situation. In December–January, the annual growth of sugar prices stabilised. Its high rate (64.01%) is associated with the low base effect of early 2020. The rise in the annual growth rate of sunflower oil prices discontinued (it equalled 26.17% in January).

Nonetheless, it should be noted that non-market regulation in such highly competitive segments as the sugar and sunflower oil markets distorts the signals of supply and demand manifested through prices. This brings about the risk of local shortages and the use of shady schemes of work. Moreover, this reduces the effective range of monetary policy aimed at maintaining price stability through market mechanisms.

LIST OF PUBLICATIONS

Bank of Russia information and analytical commentaries released after the publication of MPR 4/20 on 2 November 2020[1]:

1. *Consumer Price Dynamics, No. 10 (58), October 2020 (12 November 2020)*
2. *Banking Sector Liquidity and Financial Markets, No. 10 (56), October 2020 (12 November 2020)*
3. *Inflation Expectations and Consumer Sentiment, No. 11 (47), November 2020 (25 November 2020)*
4. *Economy, No. 10 (58), October 2020 (30 November 2020)*
5. *Consumer Price Dynamics, No. 11 (59), November 2020 (10 December 2020)*
6. *Banking Sector Liquidity and Financial Markets, No. 11 (57), November 2020 (10 December 2020)*
7. *Inflation Expectations and Consumer Sentiment, No. 12 (48), December 2020 (24 December 2020)*
8. *Economy, No. 11 (59), November 2020 (28 December 2020)*
9. *Banking Sector Liquidity and Financial Markets, No. 12 (58), December 2020 (19 January 2021)*
10. *Consumer Price Dynamics, No. 12 (60), December 2020 (20 January 2021)*
11. *Russia's Balance of Payments, No. 4 (6), 2020 Q4 (28 January 2021)*
12. *Inflation Expectations and Consumer Sentiment, No. 1 (49), January 2021 (3 February 2021)*
13. *Consumer Price Dynamics, No. 1 (61), January 2021 (15 February 2021)*

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

STATISTICAL TABLES

INTEREST RATES ON MONETARY POLICY INSTRUMENTS[1]
(% p.a.)

Table 1

Purpose	Instrument type	Instrument	Term	Frequency	Interest rates as spreads to the key rate (pp)	As of 01.01.2020	From 10.02.2020	From 27.04.2020	From 22.06.2020	From 27.07.2020
Liquidity provision	Standing facilities	Overnight loans; lombard loans; loans secured by non-marketable assets; repos; FX swaps[2]	1 day	Daily	+1.00	7.25	7.00	6.50	5.50	5.25
		Loans secured by non-marketable assets	From 2 to 549 days[3]		+1.75	8.00	7.75	7.25	6.25	6.00
	Open market operations (minimum interest rates)	Auctions to provide loans secured by non-marketable assets	3 months[3]	Monthly[4]	+0.25	6.50	6.25	5.75	4.75	4.50
		Repo auctions	1 year[3]			-	-			
			1 month		+0.10	-	-	5.60	4.60	4.35
			1 week	Weekly[5]	0.00	6.25 (key rate)	6.00 (key rate)	5.50 (key rate)	4.50 (key rate)	4.25 (key rate)
			From 1 to 6 days	Occasionally[6]						
		FX swap auctions[2]	From 1 to 2 days							
Liquidity absorption	Open market operations (maximum interest rates)	Deposit auctions	From 1 to 6 days							
			1 week	Weekly[5]						
	Standing facilities	Deposit operations	1 day	Daily	-1.00	5.25	5.00	4.50	3.50	4.00

[1] The rates are set by the Bank of Russia Board of Directors.
[2] The interest rate is given for the ruble leg; the interest rate on the foreign currency leg equals LIBOR on overnight loans in US dollars or euros (depending on the currency of transactions).
[3] Loans and operations conducted at a floating interest rate linked to the Bank of Russia key rate.
[4] Loan auctions were discontinued in April 2016, and repo auctions were introduced in May 2020.
[5] Either a repo or a deposit auction is held depending on the situation with liquidity.
[6] Fine-tuning operations.
Memo item: From 1 January 2016, the value of the Bank of Russia refinancing rate equals its key rate as of the respective date.
Source: Bank of Russia.

MONETARY POLICY INSTRUMENTS
(billions of rubles)

Table 2

Purpose	Instrument type	Instrument	Term	Frequency	Bank of Russia claims under liquidity provision instruments and liabilities under liquidity absorption instruments					
					As of 01.01.2020	As of 01.04.2020	As of 01.07.2020	As of 01.10.2020	As of 01.01.2021	As of 01.02.2021
Liquidity provision	Standing facilities	Overnight loans	1 day	Daily	0,0	0,02	0,0	0,0	5,4	1,9
		Lombard loans			0,0	0,0	0,0	0,0	0,0	0,0
		Repos			0,0	12,3	0,0	0,3	0,1	0,0
		FX swaps			12,6	0,0	0,0	0,0	118,4	0,0
		Loans secured by non-marketable assets	From 1 to 549 days		5,1	5,1	5,1	5,1	5,1	205,1
	Open market operations	Auctions to provide loans secured by non-marketable assets	3 months	Monthly[1]	0,0	0,0	0,0	0,0	0,0	0,0
		Repo auctions	1 year		-	-	5,3	5,3	36,7	47,4
			1 month		-	-	0,0	0,0	810,2	1106,7
			1 week	Weekly[2]	0,0	868,9	0,0	0,0	0,0	0,0
			From 1 to 6 days	Occasionally[3]						
		FX swap auctions	From 1 to 2 days		0,0	0,0	0,0	0,0	0,0	0,0
Liquidity absorption	Open market operations	Deposit auctions	From 1 to 6 days		696,6	1673,5	773,4	999,2	843,9	554,0
			1 week	Weekly[2]						
		Auctions for the placement of coupon OBRs	Up to 3 months	Weekly[4]	1956,3	1544,2	708,2	818,5	574,9	555,1
	Standing facilities	Deposit operations	1 day	Daily	329,7	160,5	151,3	149,1	376,7	107,7

[1] Loan auctions were discontinued in April 2016, and repo auctions were introduced in May 2020.
[2] Either a repo or a deposit auction is held depending on the situation with liquidity.
[3] Fine-tuning operations.
[4] New issues of coupon OBRs are usually placed once a month, and after that they are placed on a weekly basis. If the reporting date falls on a weekend or holiday, the indicated amount of outstanding Bank of Russia coupon OBRs includes the accrued coupon interest as of the first working day following the reporting date.
Source: Bank of Russia.

REQUIRED RESERVE RATIOS

(%)

Table 3

Liability type	Validity dates			
	01.12.17–31.07.18	01.08.18-31.03.19	01.04.19–30.06.19	From 01.07.19[1]
Banks with a universal licence and non-bank credit institutions				
To households in the currency of the Russian Federation	5.00	5.00	4.75	4.75
Other liabilities in the currency of the Russian Federation				
To non-resident legal entities in the currency of the Russian Federation				
To households in foreign currency	6.00	7.00	7.00	8.00
To non-resident legal entities in foreign currency	7.00	8.00	8.00	8.00
Other liabilities in foreign currency				
Banks with a basic licence				
To households in the currency of the Russian Federation	1.00	1.00	1.00	1.00
Other liabilities in the currency of the Russian Federation				
To non-resident legal entities in the currency of the Russian Federation	5.00	5.00	4.75	4.75
To households in foreign currency	6.00	7.00	7.00	8.00
To non-resident legal entities in foreign currency	7.00	8.00	8.00	8.00
Other liabilities in foreign currency				

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

REQUIRED RESERVE AVERAGING RATIO

Table 4

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

Source: Bank of Russia.

Table 5

REQUIRED RESERVES AVERAGING SCHEDULE FOR 2020-2021 AND INFORMATION ON CREDIT INSTITUTIONS' COMPLIANCE WITH RESERVE REQUIREMENTS

Averaging period to calculate a required reserves amount for a respective reporting period	Averaging period duration (days)	Memo item:		Actual average daily balances in correspondent accounts (billions of rubles)	Required reserves to be averaged in correspondent accounts (billions of rubles)	Required reserves recorded to their respective accounts (billions of rubles)
		Reporting period	Required reserves regulation period			
11.12.2019–14.01.2020	35	November 2019	13.12.2019–17.12.2019	2,526	2,428	617
15.01.2020–11.02.2020	28	December 2019	22.01.2020–24.01.2020	2,479	2,418	618
12.02.2020–10.03.2020	28	January 2020	14.02.2020–18.02.2020	2,474	2,398	613
11.03.2020–07.04.2020	28	February 2020	16.03.2020–18.03.2020	2,536	2,431	622
08.04.2020–12.05.2020	35	March 2020	14.04.2020–16.04.2020	2,685	2,605	665
13.05.2020–09.06.2020	28	April 2020	20.05.2020–22.05.2020	2,700	2,635	671
10.06.2020–07.07.2020	28	May 2020	15.06.2020–17.06.2020	2,636	2,570	656
08.07.2020–04.08.2020	28	June 2020	14.07.2020–16.07.2020	2,590	2,529	647
05.08.2020–08.09.2020	35	July 2020	14.08.2020–18.08.2020	2,632	2,578	659
09.09.2020–06.10.2020	28	August 2020	14.09.2020–16.09.2020	2,699	2,634	673
07.10.2020–10.11.2020	35	September 2020	14.10.2020–16.10.2020	2,753	2,688	686
11.11.2020–08.12.2020	28	October 2020	16.11.2020–18.11.2020	2,806	2,737	699
09.12.2020–12.01.2021	35	November 2020	14.12.2020–16.12.2020	2,902	2,791	714
13.01.2021–09.02.2021	28	December 2020	22.01.2021–26.01.2021	2,879	2,818	721
10.02.2021–09.03.2021	28	January 2021	12.02.2021–16.02.2021	-	-	-
10.03.2021–06.04.2021	28	February 2021	15.03.2021–17.03.2021	-	-	-
07.04.2021–11.05.2021	35	March 2021	14.04.2021–16.04.2021	-	-	-
12.05.2021–08.06.2021	28	April 2021	18.05.2021–20.05.2021	-	-	-
09.06.2021–06.07.2021	28	May 2021	15.06.2021–17.06.2021	-	-	-
07.07.2021–10.08.2021	35	June 2021	14.07.2021–16.07.2021	-	-	-
11.08.2021–07.09.2021	28	July 2021	13.08.2021–17.08.2021	-	-	-
08.09.2021–12.10.2021	35	August 2021	14.09.2021–16.09.2021	-	-	-
13.10.2021–09.11.2021	28	September 2021	14.10.2021–18.10.2021	-	-	-
10.11.2021–07.12.2021	28	October 2021	16.11.2021–18.11.2021	-	-	-
08.12.2021–11.01.2022	35	November 2021	14.12.2021–16.12.2021	-	-	-

KEY ECONOMIC AND FINANCIAL INDICATORS

Table 6

		December 2019	January 2020	February 2020	March 2020	April 2020	May 2020	June 2020	July 2020	August 2020	September 2020	October 2020	November 2020	December 2020	January 2021
Real sector															
Inflation	% YoY	3.0	2.4	2.3	2.5	3.1	3.0	3.2	3.4	3.6	3.7	4.0	4.4	4.9	5.2
GDP*	% YoY	2.1			1.6			-8.0			-3.4				
GDP in current prices*	trillions of rubles	29.8			25.3			23.3			27.9				
Output by key activity types	% YoY	2.1	1.8	4.6	2.1	-9.0	-9.5	-6.9	-4.3	-2.9	-1.8	-4.4	-1.4	0.3	
Industrial production	% YoY	2.7													
Agricultural production	% YoY	5.6	2.9	3.1	3.0	3.1	3.2	3.0	4.2	4.2	2.3	-4.5	-1.7	0.5	
Construction	% YoY	0.4	2.8	3.5	2.4	-5.7	-4.2	-2.1	-0.4	0.3	3.1	0.7	0.6	0.9	
Fixed capital investment*	% YoY	2.3			1.2			-7.6			-4.2				
Freight turnover	% YoY	-2.7	-3.9	-0.5	-6.8	-6.0	-9.2	-9.5	-8.0	-4.6	-3.4	-3.6	-1.7	-1.3	
PMI Composite Index	% SA	51.8	52.6	50.9	39.5	13.9	35.0	48.9	56.8	57.3	53.7	47.1	47.8	48.3	52.3
Retail turnover	% YoY	1.8	2.7	4.7	5.7	-22.6	-18.6	-7.1	-1.1	-1.8	-2.1	-1.4	-3.1	-3.6	
Real disposable money income*	% YoY	1.8			1.0			-7.9			-5.3			-1.7	
Real wage	% YoY	6.9	6.5	5.7	5.9	-2.0	1.0	0.6	2.9	0.1	2.2	0.5	0.2		
Nominal wage	% YoY	10.1	9.1	8.1	8.6	1.0	4.0	3.8	6.4	3.7	6.0	4.5	4.6		
Unemployment rate	% SA	4.5	4.5	4.5	4.6	5.7	6.1	6.3	6.4	6.5	6.5	6.3	6.1	5.9	
Banking sector															
Broad money supply	% YoY, AFCR	7.6	8.0	7.9	9.1	9.6	9.3	10.4	11.1	11.7	11.8	11.8	11.6	12.6	
Money supply (M2)	% YoY	9.7	10.7	11.0	13.4	14.0	13.6	14.9	15.5	16.2	16.1	16.2	14.1	13.5	
Household deposits	% YoY, AFCR	9.8	9.2	8.3	6.4	5.4	5.3	5.8	5.8	5.0	4.5	3.4	3.0	4.3	
in rubles	% YoY	9.9	10.0	9.9	9.6	8.6	8.4	9.3	9.4	8.3	8.3	6.9	5.7	6.5	
in foreign currency	% YoY	9.8	6.3	2.3	-4.6	-6.2	-5.9	-6.7	-7.2	-6.5	-8.6	-8.8	-6.6	-4.6	
dollarisation	%	19.6	20.2	20.6	22.2	20.9	20.4	20.0	20.8	21.0	21.9	21.9	21.4	20.7	
Loans to non-financial organisations	% YoY, AFCR	4.3	3.2	2.0	3.6	4.8	4.8	4.4	6.0	6.3	6.3	6.6	7.4	7.0	
short-term (less than 1 year)	% YoY, AFCR	0.4	4.9	3.3	9.8	12.4	13.9	15.0	11.3	14.0	14.2	12.5	13.3	10.6	
long-term (more than 1 year)	% YoY, AFCR	3.2	2.8	1.9	2.3	3.2	3.1	2.1	4.1	4.1	4.1	5.0	5.6	5.7	
overdue loans	%	7.8	7.8	7.6	7.5	7.4	7.5	7.7	8.2	8.1	8.0	7.9	7.9	7.8	
Loans to households	% YoY, AFCR	18.5	17.9	17.8	17.7	14.6	13.0	12.6	13.1	13.2	13.4	14.6	13.9	13.5	
housing mortgage loans	% YoY, AFCR	16.9	15.6	15.4	15.2	14.1	13.6	13.7	15.7	16.6	18.6	22.0	20.8	21.2	
unsecured consumer loans	% YoY	20.8	20.1	20.2	20.0	15.3	12.7	11.2	10.1	9.5	8.9	9.1	9.2	8.8	
overdue loans	%	4.3	4.4	4.5	4.5	4.6	4.7	4.7	4.8	4.8	4.7	4.7	4.7	4.7	

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

KEY ECONOMIC AND FINANCIAL INDICATORS: BALANCE OF PAYMENTS

Table 7

		2018 Q1	2018 Q2	2018 Q3	2018 Q4	2019 Q1	2019 Q2	2019 Q3	2019 Q4	2020 Q1	2020 Q2	2020 Q3	2020 Q4[1]
Balance of payments[2]													
Urals crude price	% YoY	25.9	50.8	44.3	10.7	-3.7	-5.5	-16.9	-7.2	-22.6	-57.0	-29.6	-29.1
USD/RUB exchange rate ('+' – ruble's strengthening, '-' – ruble's weakening)	% YoY	3.4	-7.5	-9.9	-12.1	-14.0	-4.3	1.4	4.3	0.0	-10.7	-12.2	-16.4
Goods and services exports	% YoY	21.8	27.4	28.4	18.8	0.7	-6.7	-6.3	-7.9	-11.6	-31.3	-25.8	-20.8
Goods and services imports	% YoY	19.0	8.2	-0.1	-2.9	-3.4	-1.4	5.5	9.8	1.3	-23.7	-20.3	-12.1
Current account	**billions of US dollars**	**30.2**	**18.4**	**28.1**	**39.0**	**33.4**	**10.0**	**10.5**	**10.9**	**22.9**	**0.9**	**3.2**	**5.5**
Balance of trade	billions of US dollars	44.0	45.5	47.8	57.7	47.0	39.4	37.9	41.0	33.2	16.5	18.3	21.5
Exports	billions of US dollars	101.6	108.9	110.6	122.9	102.6	101.4	103.3	112.5	89.3	70.4	78.5	91.3
Imports	billions of US dollars	57.5	63.4	62.7	65.2	55.7	62.0	65.4	71.6	56.1	53.9	60.2	69.8
Balance of services	billions of US dollars	-6.6	-7.7	-8.8	-6.9	-6.1	-8.9	-11.7	-10.0	-6.8	-2.2	-3.9	-5.4
Exports	billions of US dollars	13.9	16.6	17.4	16.7	13.7	15.6	16.6	15.9	13.6	9.9	10.5	10.5
Imports	billions of US dollars	20.6	24.4	26.1	23.6	19.8	24.5	28.4	26.0	20.3	12.1	14.5	15.9
Balance of primary and secondary income	billions of US dollars	-7.2	-19.3	-11.0	-11.8	-7.5	-20.5	-15.7	-20.0	-3.5	-13.4	-11.2	-10.5
Current and capital account balance	billions of US dollars	30.0	18.2	28.1	38.3	33.4	9.8	10.4	10.5	22.9	0.7	3.1	5.2
Financial account excluding reserve assets (net lending (+) / net borrowing (-)	**billions of US dollars**	**12.7**	**9.8**	**24.9**	**31.0**	**12.3**	**-5.2**	**-7.2**	**-3.8**	**18.4**	**13.6**	**7.4**	**10.4**
Public sector	billions of US dollars	-6.6	11.1	2.9	1.3	-9.3	-6.2	-3.6	-3.8	0.4	1.3	-2.5	-1.4
Private sector	billions of US dollars	19.3	-1.3	22.0	29.8	21.6	1.0	-3.6	0.0	18.0	12.3	10.0	11.8
Net errors and omissions	billions of US dollars	2.1	2.9	1.8	-4.7	-2.5	1.6	-1.7	1.1	0.6	0.0	2.1	1.6
Change in reserve assets ('+' – increase, '-' – decrease)	**billions of US dollars**	**19.3**	**11.3**	**5.0**	**2.6**	**18.6**	**16.6**	**15.9**	**15.4**	**5.0**	**-12.9**	**-2.3**	**-3.6**

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

GLOSSARY

BALANCE OF PAYMENTS OF THE RUSSIAN FEDERATION

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

BANKING SECTOR LIQUIDITY

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

BANK OF RUSSIA KEY RATE

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

CONSUMER PRICE INDEX (CPI)

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

CORE INFLATION

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

CREDIT DEFAULT SWAP (CDS)

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

DOLLARISATION OF BANK DEPOSITS (LOANS)

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

FINANCIAL STABILITY

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

FLOATING EXCHANGE RATE REGIME

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

INFLATION

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

INFLATION EXPECTATIONS

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

INFLATION TARGETING

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

LIQUIDITY-ABSORBING OPERATIONS

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

MONETARY BASE

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

MONEY SUPPLY

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

MONEY SUPPLY IN THE NATIONAL DEFINITION (M2 MONETARY AGGREGATE)

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

MSCI INDICES

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

NEUTRAL RATE

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

REFINANCING OPERATIONS

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

REQUIRED RESERVE RATIOS

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

RUONIA (RUBLE OVERNIGHT INDEX AVERAGE)

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

STRUCTURAL LIQUIDITY DEFICIT/SURPLUS

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

TRANSMISSION MECHANISM

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

ABBREVIATIONS

AE – Advanced economies

AEB – Association of European Businesses

AFCR – adjusted for foreign currency revaluation

BLC – bank lending conditions

bp – basis point (0.01 percentage points)

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

BRICS – a group of five countries: Brazil, Russia, India, China and South Africa

Cbonds-Muni – municipal bond index calculated by Cbonds

CCPI – core consumer price index

CPI – consumer price index

DSR – debt service ratio (the ratio of the cash flow available to pay current debt obligations, including principal and interest, to current income value)

ECB – European Central Bank

EME – emerging market economies

EU – European Union

FAO – Food and Agriculture Organization of the United Nations

FCS – Federal Customs Service

Fed – US Federal Reserve System

FGUP – federal state unitary enterprise

FPG – fiscal policy guidelines

GDP – gross domestic product

GFCF – gross fixed capital formation

GRP – gross regional product

GVA – gross value added

IBL – interbank loans

IEA – International Energy Agency

IFX-Cbonds – corporate bond return index

Industrial PPI – industrial producer price index

inFOM – Institute of the Public Opinion Foundation

MC – management company

MIACR – Moscow Interbank Actual Credit Rate (weighted average rate on interbank loans provided)

MIACR-B – Moscow Interbank Actual Credit Rate-B-Grade (weighted average rate on interbank loans provided to banks with speculative credit rating)

MIACR-IG – Moscow Interbank Actual Credit Rate-Investment Grade (weighted average rate on interbank loans provided to banks with investment-grade rating)

MIC – military-industrial complex

MICEX SE – MICEX Stock Exchange

mbd – million barrels per day

MPD – Monetary Policy Department of the Bank of Russia

MPG 2021-2023 – Monetary Policy Guidelines for 2021-2023 (approved by the Bank of Russia Board of Directors on 5 November 2020)

MPR – Monetary Policy Report (mentioned in the text as 3/20 – No. 3 2020; 4/20 – No. 4 2020)

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

NFI – non-bank financial institution

NPF – non-governmental pension fund

NWF – National Wealth Fund

OBR – Bank of Russia bonds

OECD – Organisation for Economic Cooperation and Development

OFZ – federal government bonds

OFZ-IN – inflation-indexed federal government bonds

OFZ-PD – permanent coupon-income federal government bonds

OFZ-PK – variable coupon-income federal government bonds

OGR – oil and gas revenue

OJSC – open joint-stock company

OPEC – Organization of the Petroleum Exporting Countries

PJSC – public joint-stock company

PMI – Purchasing Managers’ Index

pp – percentage point

PPI – producer price index

QPM – quarterly projection model of the Bank of Russia

REB – Russian Economic Barometer, monthly bulletin

REER – real effective exchange rate

RGBEY – Russian Government Bonds Effective Yield until Redemption (calculated by the Moscow Exchange)

RUONIA – Ruble OverNight Index Average (reference weighted rate of overnight ruble deposits in the Russian interbank market)

SA – seasonally adjusted

SICI – systemically important credit institution

SME – small and medium-sized enterprises

SNA – system of national accounts

TCC – total cost of credit

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

VAT – value added tax

VCIOM – Russian Public Opinion Research Centre

VECM – Vector Error Correction Model

3MMA – three-month moving average