

## Russia central bank takes a pause in policy easing

The adjusted forward guidance suggests the policy rate may end 2018 within the 6.50-7.00% range, a somewhat more cautious stance than before. But the uncertainty may change everything both ways



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**7.25%** Key rate

As expected

### Neutral policy in 2018, but with decreased downside risks

The Central Bank of Russia (CBR) decided to keep its key rate unchanged at 7.25% as we expected in line with consensus.

After the March meeting where it cut rates by 25bp, the Bank strengthened its easing bias pledging to normalise policy (i.e. get the key rate within 6-7%) in 2018. This time the CBR said it still

assumes policy neutrality will happen in 2018, but added that downside potential for the key rate somewhat decreased under rising global interest rates and higher risk premia on Russia. This is why it said the neutral policy might have shifted closer to the upper bound of its 6-7% corridor.

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*For now, we stick to our adjusted 6.50% year-end call expecting a cut by 25bp in June, September and December each with some upside risks*

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The Bank noted the rouble weakness might force a faster adjustment of inflation towards the 4% target, while it doesn't create risks of overshooting, so CPI growth is still seen within 3-4% in 2018 and near 4% in 2019. GDP growth is still expected at around 1.5-2% in 2018.

Major inflation risks stem from (1) geopolitical factors and rising interest rates in the global market, which may trigger higher markets volatility affecting inflation expectations; and (2) uncertainty about future fiscal parameters incorporating possible President Putin economic initiatives.

The CBR flagged it will take into account inflation risks, inflation performance and economic trends vs its forecast in taking future decisions about the key rate.

## **Expect 6.50-7.00% as a working range for 2018**

The CBR made a smart decision by both retaining its easing bias and flagging a lower downside potential for the key rate from geopolitical risks and higher core rates. We think it now keeps in mind a range of 6.50-7.00% as a working assumption about the policy rate in 2018. For now, we stick to our adjusted 6.50% year-end call expecting a cut by 25bp in June, September and December each with some upside risks appearing from the somewhat more cautious CBR stance.

We do acknowledge higher uncertainty including from geopolitical factors but think that there will be no material risks to inflation even if inflation expectations edges higher following the weaker rouble. The fiscal parameters, though, is a more significant story, but we need to have more clarity here after the formation of the new government to assess possible consequences.

We remain constructive on the rouble given the cautious CBR (i.e. high real policy rate), still credible OFZ story for foreigners from fundamental point of view, and likely current account adjustment in coming months to the weaker RUB (now) helping the Balance of Payment to stay balanced despite the continuing Ministry of Finance FX purchases and thus leaving a chance for some RUB recovery later in coming weeks or months.