

Snap | 6 August 2021

RUSSIA

Russian CPI: stabilisation in July is fragile, but gives way for cautious optimism

Seasonal deflation in fruits and vegetables prevented further acceleration in inflation from the June level of 6.5% YoY, but upward price pressure in less volatile segments leaves room for negative surprises in the next few months. Still, the case for our below-consensus expectations for the year-end is still intact



A man making a choice in a Russian supermarket

6.46

Russian inflation for July, % YoY

down from 6.50% YoY in June

Lower than expected

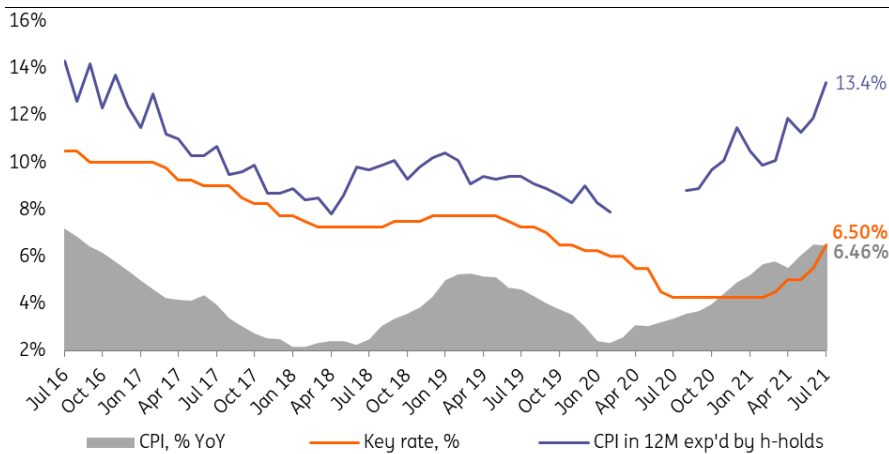
July inflation better than expected on volatile items

Russian consumer inflation was reported at 6.46% year-on-year in July, which is marginally lower than the 6.50% YoY reported for June and 0.1 percentage point lower than we and the market [expected](#). We are reluctant to take this development as a cause for optimism in the near term, as this seeming stabilisation was assured by highly volatile items and aided by statistical base effects.

- Given the higher base effect from July 2020, a true stabilisation in the consumer prices would require a slowdown in the annual rate by around 0.2 percentage points YoY in July.
- Core CPI, reflecting the performance in the less volatile items of the consumer basket, picked up from 6.55% YoY to 6.78% YoY, a five-year high.
- Food CPI was the primary source of positive news, decelerating from 7.90% YoY to 7.43% YoY thanks to deeper-than-expected monthly deflation in the fruit and vegetable segment, but the less volatile items did not show deceleration en masse, and prices for fish and dairy continued to climb.
- Non-food CPI remains a cause concern, accelerating from 7.04% YoY to 7.55% YoY and its contribution to the overall CPI basket climbed from 2.3 to 2.5 percentage points, according to our estimates. The primary cause is construction materials, where price growth spiked from 24% to 30% YoY, reflecting the construction and renovation boom aided by the subsidised mortgage programme. Upward price pressure also remains in pharmaceuticals (with persistent pandemic risks we do not expect the situation to change materially anytime soon), consumer electronics and household appliances (though somewhat restrained by the ruble stability). The true positive was some moderation in the gasoline price growth for the second month in a row, possibly showing the result of stabilisation measures by the government.
- Price growth in services moderated from 3.95% to 3.83% YoY, mainly on some easing in the tourism-related items after the reopening of the popular foreign destinations. At the same time, upward pressure was seen in domestic utilities services and healthcare.

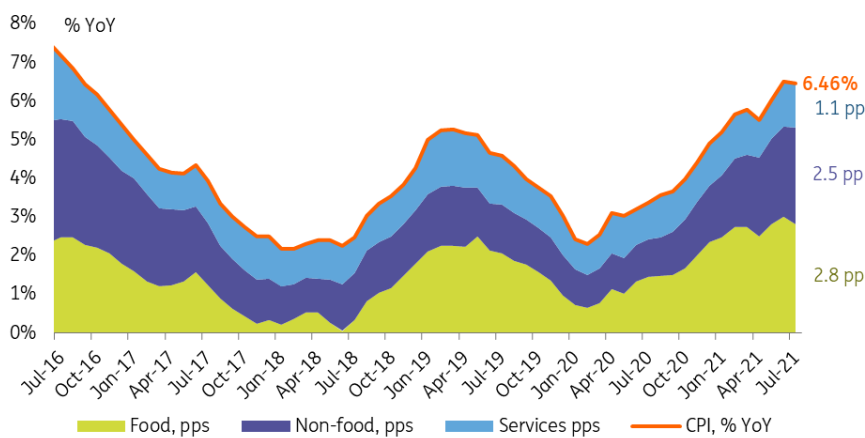
Based on the CPI structure, elevated inflationary expectations by the households, and increased reliance of consumption on borrowing and withdrawal of deposits, we believe the near-term CPI risks will remain elevated. As a result, we do not see material easing in Bank of Russia's monetary policy stance in the near term.

Figure 1: Russian CPI stabilised in July thanks to higher base effect and volatile items, but the household expectations are elevated



Source: Bank of Russia, Rosstat, ING

Figure 2: Stabilisation in the headline CPI masks the deterioration in the non-food segment



Source: Bank of Russia, Rosstat, ING

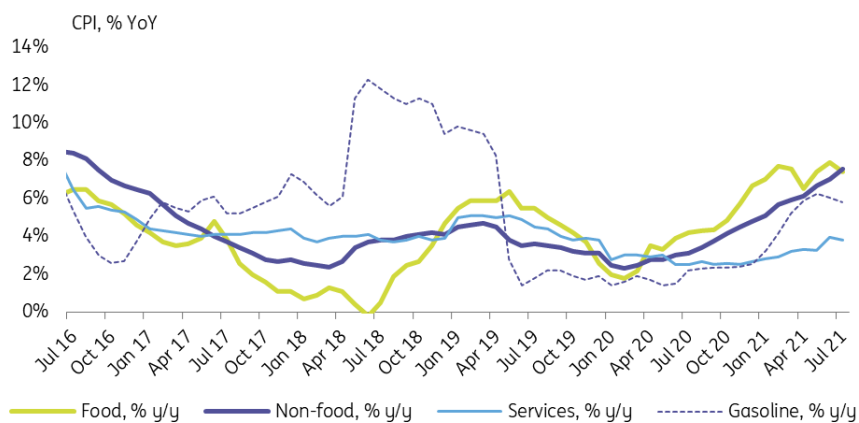
We are still optimistic for the medium term, but uncertainty is high

The period of seasonal deflation in fruits and vegetables should restrain the CPI performance in August and September, but the growing demand-driven inflation in the non-food segments should keep the overall CPI growth close to the current 6.5% YoY level in the next couple of months. The high level of inflationary risks should maintain

upward pressure on the key rate, and we expect a further 25 basis point hike at the September meeting.

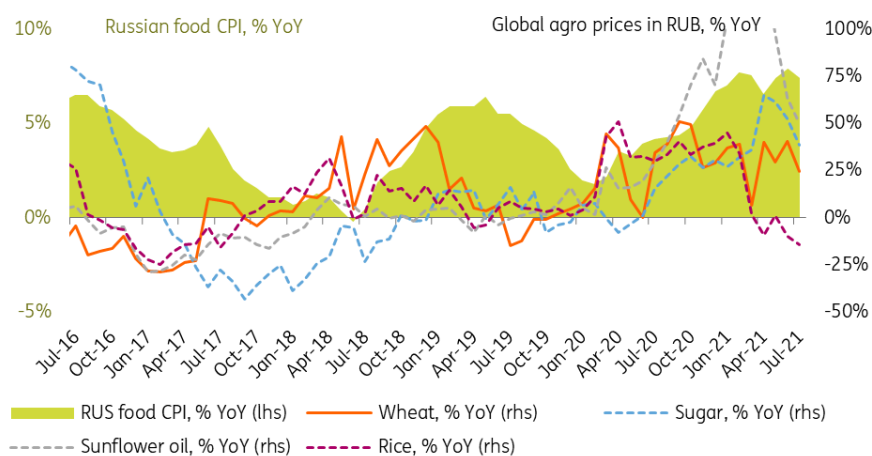
At the same time, for the medium term we are more optimistic on the stabilisation in gasoline prices, global agricultural commodities, ruble, and local monetary supply (since September last year). Also, the recent indication from the government that the local investments out of the sovereign fund (NWF) into the local infrastructural projects, which we initially saw at up to US\$10bn per year starting 2021, are now likely to be postponed till 2022, meaning lower inflationary risks from the budget policy. As a result we see CPI decelerating in 4Q21 to the lower bound of Bank of Russia's 5.7-6.2% forecast range, which is slightly better than consensus. This should limit the medium-term ceiling of the key rate in the 6.5-7.0% range. Meanwhile, the new wave of Covid globally and EMs in particular, combined with unclear prospects of global liquidity suggests that the uncertainty around CPI and key rate forecasts should remain elevated for the time being.

Figure 3: Moderation in the gasoline price growth is a cause for cautious optimism



Source: Bank of Russia, Rosstat, ING

Figure 4: Global food prices are also stabilising



Source: Rosstat, Refinitiv, ING

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