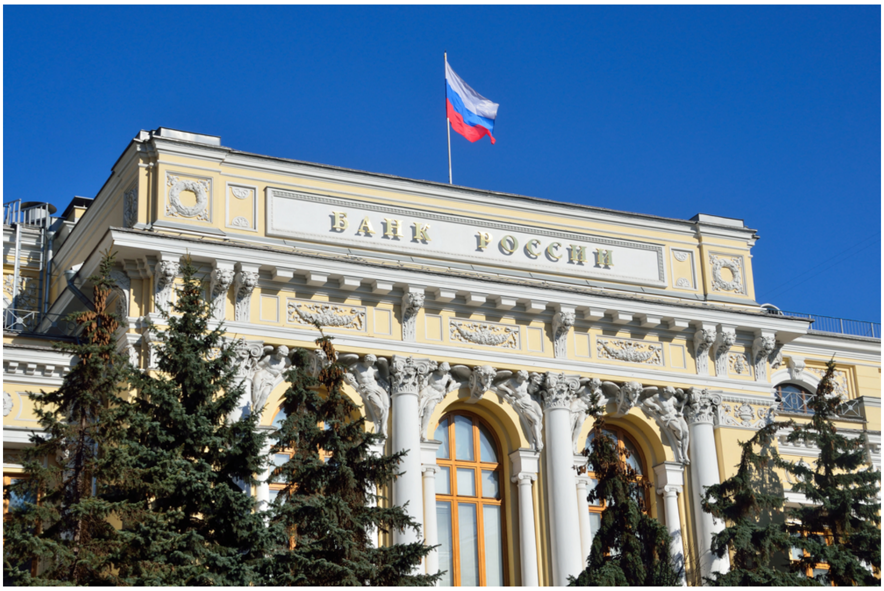
Russian key rate on hold, but is still looking down

Bank of Russia kept the 4.25% key rate on higher near-term CPI and market risks. It also maintained its medium-term dovish signal, in line with our expectations. CBR may resume cutting towards 3.5-4.0% if it becomes more evident that GDP and CPI will underperform in 2021, which we find increasingly likely. Yet stabilisation of markets is a prerequisite



Central Bank of Russia, Moscow

4.25%

Russian key rate

unchanged

As expected

Bank of Russia's rate decision to hold the key rate at 4.25% was not a surprise.

- The decision to extend the tactical hold reflects increased near-term pro-inflationary

pressure amid market volatility. The CBR's year-end 2020 CPI target is slightly raised from 3.7-4.2% to 3.9-4.2%. The CBR quotes recent RUB depreciation and foreign policy uncertainty as the primary cause. We agree that given the recent RUB depreciation by 8% to USD and by 12% year-on-year to EUR in 3Q20, the year-end CPI is more likely to approach 4.0% rather than our initial 3.7% forecast.
- In addition, the CBR mentioned several factors of near-term uncertainties including global market volatility amid the global trade tensions and pandemic, as well as local fiscal policy discussion we mentioned earlier. The Bank of Russia did not explicitly mention the halt in the easing cycle among peers, but we believe it was a contributing factor to the decision.

The decision to maintain dovish medium-term signal is in line with our expectations, but may bring relief to some market participants who feared tightening in the CBR message.

- CBR reiterated the wording from the last decision that it will consider the necessity of further key rate reduction at its upcoming meetings. This means a possibility of a cut at the next meeting if economic amd market developments go in line with CBR's base case scenario
- CBR's macro forecast remained unchanged for year-end 2021 CPI, with the 3.5-4.0% range reiterated. At the same time, the wording of the commentary and the downgrade of 2021 expectations for GDP (by 0.5 percentage point to 3.0-4.0%), exports (from 4.5-6.5% to -0.8% - +1.2%), suggests that the CBR is having increased concerns about the pace of the economic recovery next year, which could be a source of CPI underpeformance relative to the target. We do not exclude that the actual CPI range could be even lower - at 3.0-3.5% next year provided the ruble stabilises.
- The general improvement in the CBR's macro and balance of payments forecasts for 2020 seems to be reflecting an adjustment to the actual results of 9M20 rather than an improvement in the near-term expectations. Meanwhile we note, that the private consumption outlook for 2020 has been downgraded from -6.2-7.2% to -9.5-10.5% despite the upgrade in retail lending growth expectations from 6-9% to 13-16%.
- CBR's implied ruble expectations seem to be stable, as the drastic improvement in the current account forecast from US$2bn to US$33bn for 2020 reflects higher oil price, the effect oof which is sterilized by the fiscal rule and higher expected net private capital outflow (2020 outflow forecast raised from US$25bn to US$53bn, 2021 outflow increased from US$25bn to US$35bn).

Ahead of Governor Nabiullina's press-conference, which is about to take place, we take the CBR's decision and wording as confirmation of our take, that the scope for further cuts in the key rate – to the floor of 3.5-4.0% – remains. A December cut is not out of the question if the market volatility related to global concerns and Russia-specific challenges stabilises.

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