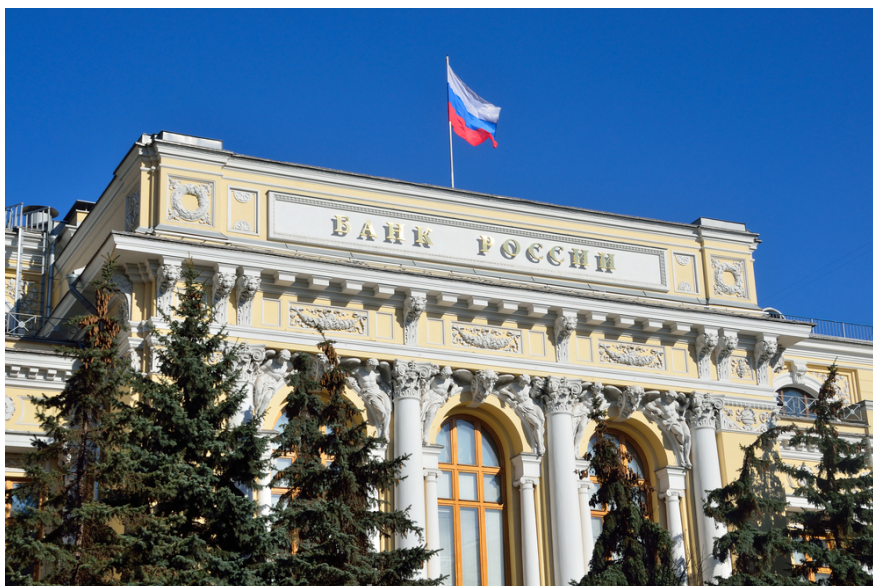


Russia key rate to be cut, dovish guidance may be reinforced

The central bank has an opportunity to make the first rate cut - to 7.50% - on 14 June, as a number of risks have failed to materialise. The central bank is also likely to confirm room for further rate cuts in the future. However, we still see a number of risks of cuts being too fast on the way to the terminal 6.5% rate



Central Bank of Russia, Moscow

CBR to make the first cut as early as 14 June

While following the Central Bank of Russia's (CBR's) April announcement that the first key rate cut may take place in 2-3Q19, we were unsure about the CBR's ability to make the first move before September 2019, a number of global and local developments has pushed the likely timing to June.

- global markets are now confident in a more dovish Fed stance, with the implied probability of a September Fed cut increasing from 30-50% to nearly 100%.
- risks to RUB exchange rate have so far failed to materialise, as the local currency remained stable in May, supported by continuous foreign portfolio inflows into the local state debt market (OFZ) of around US\$3 billion.
- local CPI rate continued to undershoot expectations, decelerating from 5.2% YoY in April to 5.1% YoY in May, and preliminary data for the first week of June suggests a possibility of CPI

going below 5.0% YoY soon. Households' inflationary expectations seem to have moderated.

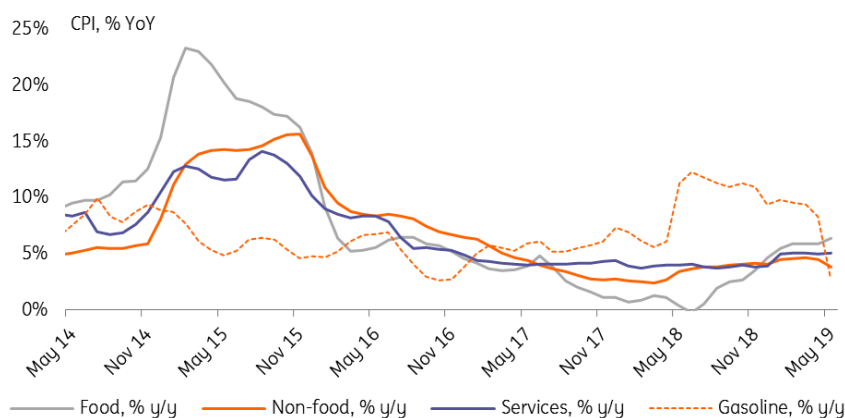
Mid-term guidance the key focus

Now, as only a very strong negative external surprise could stop the cut next week, the key question is the forward-looking guidance. We expect some downward revision in the CBR's CPI outlook for year-end 2019, which is currently 4.7-5.2%, higher than our 4.6% forecast. This would confirm the downward mid-term trend in CPI and the key rate, however, a number of risks could still prevent the CBR from being too aggressive in the way to the terminal rate, which we see at 6.5% and to be reached in 2020:

- the recent US\$15/bbl drop in the oil price, re-ignition of US-China tensions, combined with the local dividend season (up to US\$9 billion to be converted into FX) and stable US\$5-6 billion monthly FX interventions suggest persisting risks to RUB.
- we are concerned that the May CPI slowdown was driven largely by the base effect-related slowdown in gasoline price growth (from 8.3% YoY in April to 2.8% YoY in May), which may have started to pick up again, based on the most recent weekly CPI data. Other components of the CPI basket, including food and services, have shown an acceleration in the annual price growth, and the core CPI posted an acceleration from 4.6% to 4.7% YoY.
- the slowdown in RUB retail and corporate deposits evident from the recently released April banking data suggest that too fast cuts may increase risks of re-dollarization.

<https://think.ing.com/reports/russia-dividend-payments-ahead-favouring-cautions-rub-view/>

CPI growth by segments



Source: State Statistics Service, ING

For now, we expect two 25 basis point cuts to take place this year – in June and September, with risks to this view skewed towards more cuts in 2019 depending on the tone of the CBR guidance on 14 June and if the risks to RUB for 3Q19 we have indicated earlier keep failing to materialise.

Author

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.