

Russian key rate: a tactical hold

Bank of Russia held on to 4.25% today, in line with expectations. The door for further cuts remains open, though uncertainties with budget and foreign policy may extend the pause till December. With Russian real rates becoming elevated among peers, our call for the nominal 3.5-4.0% rate floor is still valid, though risks are tilted to the upper bound



The Central Bank of Russia headquarters in Moscow

4.25%

Russian key rate

unchanged

As expected

Bank of Russia kept the key rate unchanged at 4.25%, in line with market and [our](#) expectations. The overall tone of the [commentary](#) also didn't surprise, as the moderately dovish mid-term signal remained in place.

CBR rhetoric confirms our take that the reasons for the tactical hold include more a more active recovery in local [economic activity](#), higher foreign policy risks and [market volatility](#), slightly higher-

than-expected [CPI](#) trajectory for reasons beyond the base effect, and elevated CPI expectations among households and businesses.

The mid-term signal remains moderately dovish, as CBR pointed that

- the economy is growing below potential, and Governor Nabiullina stressed the need to maintain loose monetary policy (real rate below 1%) in 2021
- market expectations for CPI for 2021 are below 4%
- the upcoming [budget consolidation](#) may slow down the recovery in demand

This suggests that the scope for further cuts is not exhausted.

Meanwhile, we note that the CBR commentary also contains signs of lower certainty in its dovish base case

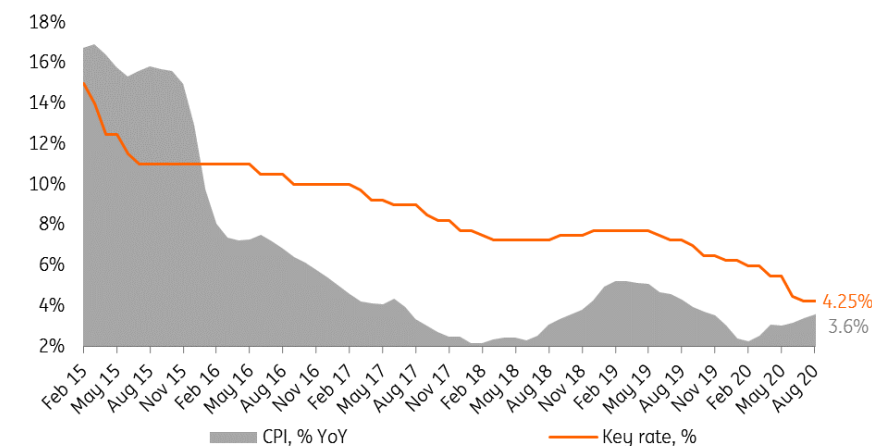
- There is higher attention to foreign politics: according to CBR, the global foreign policy tensions (including on trade) can lower the potential growth, which could lead to higher risk of overheating; it also can lead to higher volatility of the financial markets, also being potentially pro-inflationary in Russia's case
- CBR highlighted that its base case in no small part relies on the Finance Ministry's ability to defend its tight fiscal policy approach. The 2021-23 budget draft is current under discussion, and is likely to be finalised in December

Based on the tone of the communique and press-conference by the governor, we believe that another 25bp key rate cut this year is possible, though not necessarily in October. The finalisation of the Russian budget drafting process is expected only in December, and the US political cycle renews in November. We would not exclude that CBR would like to clear those uncertainties before proceeding with further cuts.

In a longer run, we continue to believe in further scope for the key rate cut, as the Russian real key rate (1.0% based on expected CPI in 12 months) has reached CBR's threshold between loose and neutral monetary policy, and is now leaning again towards the upper border of the peer spectrum (which spans from -2.6% to +2.8%), however we share CBR's pro-inflationary concerns (we see upward risks to our CPI forecast of 3.3% for 2021) and see that the key rate floor should be in the middle or at the upper border of our 3.5-4.0% forecast range.

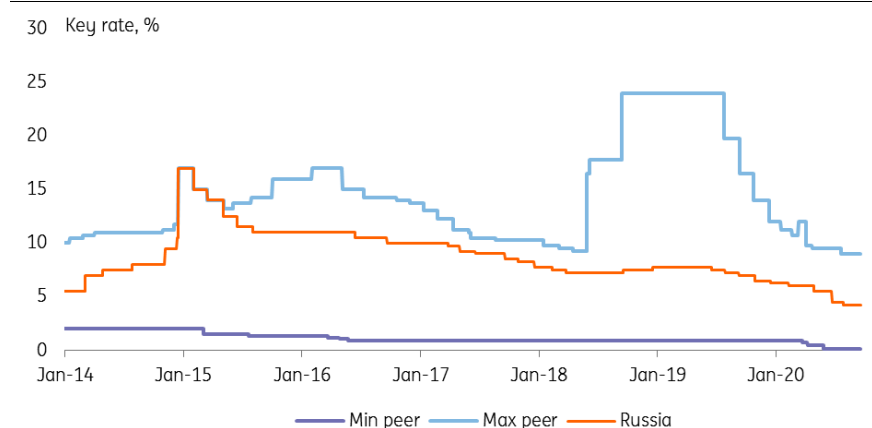
A return to the neutral monetary policy, which in CBR's definition is 1-2% in real terms and 5-6% in nominal terms, at this point appears as a prospect for periods beyond 2021.

Figure 1: CBR keeps the key rate unchanged amid accelerating CPI



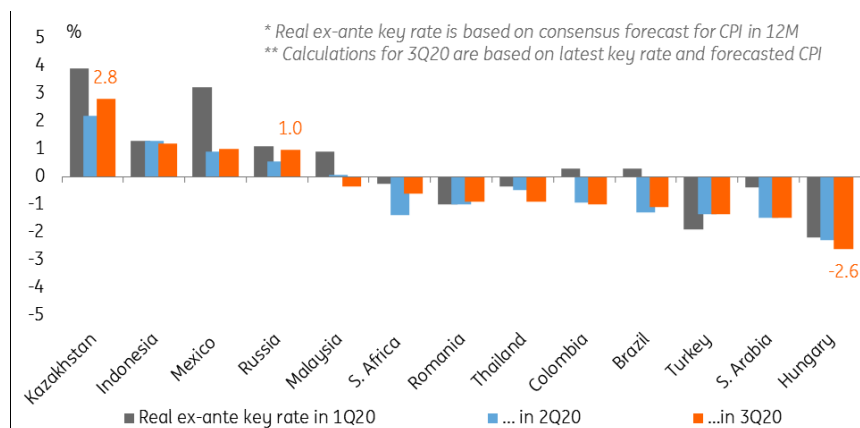
Source: Bank of Russia, Rosstat, ING

Figure 2: Russia's EM/commodity peers have also slowed down the easing cycle



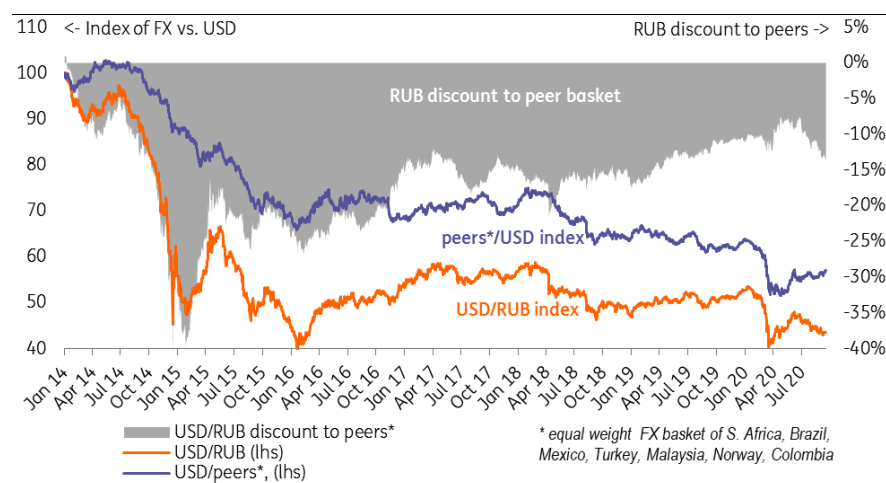
Source: Bloomberg, ING

Figure 3: Russian real rates are becoming elevated again



Source: Bloomberg, ING

Figure 4: Elevated real rates may be justified by increased country-specific risk perception



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 www.ing.com.