29 April 2016

Flash Comment

CBR rate decision: unchanged on inflation fears

- **Russia's central bank keeps its key rate unchanged at 11.0%.**
- **The CBR tone softens as inflation fears prevail.**
- **We continue to be bullish on the RUB and expect the first cut on USD/RUB under 60.**

Assessment and outlook

Russia's central bank kept its key rate unchanged today (29 April) at 11.0%, in line with our and consensus expectation. The main reasons were 'elevated inflation risks' stemming from 'uncertainty in parameters of the national budget' and declining money market rates on abundant liquidity in the banking sector. The latter is viewed by the CBR as a small easing step, we believe, as despite a positive real rate interbank rates dove under the key rate.

However, in the statement the CBR sounded cautiously softer than previously. The central bank introduced conditionality of resuming monetary easing: 'should inflation risks fall as much as to ensure with greater certainty that the Bank of Russia achieves its inflation target', which remains at 4% y/y by end-2017. Inflation posted 7.3% y/y as of 25 April. Yet, we expect inflation to accelerate to 8.1% y/y on low base effect by end-2016.

This time the CBR omitted its list of 'scapegoats' (oil, the slowdown in the Chinese economy and moves by the Fed) as global conditions have improved. Given the present inflation fears as the CBR's cautious stance continues, we believe a 50bp key rate cut at the next meeting on 10 June is possible if the current upward trend in the oil price and the RUB continues, with USD/RUB sliding under 60 and the crude price jumping over USD50/bl. Otherwise, we believe any oil price weakening and deterioration of global risk sentiment would shift the cut into H2 16. We still expect the key rate to fall to 9.5% by the end of 2016.

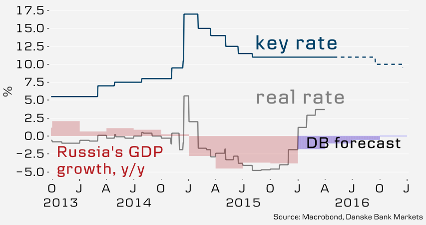
RUB rallies after the decision

Before the CBR's rate decision, the RUB continued to strengthen as the crude price climbed. After the decision the RUB rallied further returning to its pre-decision levels within an hour as the CBR showed improved consistency. The RUB keeps its position as the best performer in YTD spot returns in the emerging market universe. RUB-denominated sovereign bonds OFZs entered the rally on CBR's softer tone.

We continue to be bullish on the RUB. The RUB's free float continues to protect Russia's current account surplus and economy despite probably another year of slump. The rising oil price prospects, an upward oil futures curve and marginal FX redemptions by the corporate sector, combined with low FX demand by individuals, should also be RUB supportive.

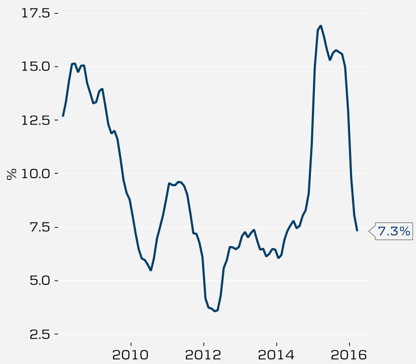
We keep our USD/RUB profile unchanged and see the cross at 63.30 in 3M, 61.10 in 6M and 58.0 in 12M. Our EUR/RUB forecasts are 70.90 (3M), 69.70 (6M) and 68.40 (12M).

CBR holds on inflation fears...



Source: Macrobond Financial, Danske Bank Markets

...while disinflation continues



Source: Macrobond Financial, Danske Bank Markets

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