CBR MEETING REVIEW: LONG MEANS LONGER

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At today's meeting the CBR kept the key rate unchanged at 16%, in line with our and market expectations. The decision was based on persistently strong inflation risks.

The signal was toughened slightly, indicating that the period of tight monetary conditions may last longer than initially expected. While we expect a reduction of the key rate in 2H24, its scale will depend on the dynamic of demand.

The CBR kept the key rate unchanged at 16% for a third straight meeting, in line with the consensus and our expectation[1]. While the great majority of board members favored keeping the rate unchanged, the number of votes in favor of an increase rose slightly, while the number of those advocating for a cut decreased.

The decision to keep the key rate at a high level stemmed from the predominance of inflationary risks, namely instability of oil export prices, persistently high inflation expectations, overheating of the labor market and uncertainty regarding the parameters of the upcoming budget policy update.

In response to the ongoing "skew" in risks, the CBR has actually been gradually tightening monetary policy: maintenance of the nominal key rate at unchanged levels since December amid waning household inflation expectations (-3.2 pps to 11.0%) over the period has led to growth of the real key rate.

Monetary conditions have not changed much since the March meeting. Rising real rates are supporting the propensity to save, although growing household income is facilitating further growth in consumption. While lending activity is unevenly spread across sectors, overall growth in corporate lending has decelerated relative to 4Q23.

The signal on the future trajectory of monetary policy remained tough: "The return of inflation to the target and its further stabilization near 4% suggests a longer period of maintaining tight monetary policy in the economy than previously predicted." This signal can be interpreted as a refusal to cut the rate at the June meeting and a smaller likelihood of a reduction in July.

A direct consequence of the increasing deviation of the demand trajectory from the CBR's February forecast was an upward revision of year-end economic growth estimates:

- GDP growth is expected to total 2.5-3.5% (vs. 1-2% in the February forecast).
- The annual average key rate will equal 15-16% (vs. 13.5-15.5% previously). According to our estimates, this means that at year end the rate might range from 12-16% (vs. 10-15% previously).
- Inflation will slow by December to 4.3-4.8% from 4.0-4.5% previously, while the achievement of the CBR's target (4.0%) is expected already at the beginning of 2025.

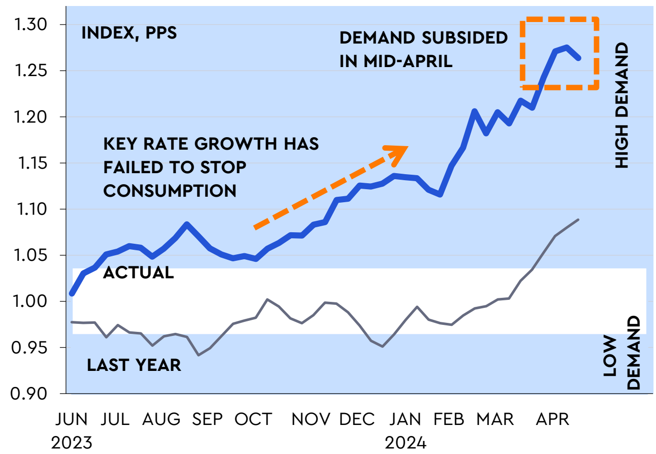
Overheating of domestic demand is becoming a key factor for the CBR. Rapid growth of household income and confident consumer sentiment are shaping the observed intransigence of consumer activity[2] toward a tightening of monetary policy. However, according to our estimates[3], current data over the past few weeks indicate some stabilization of demand, which could create favorable conditions for the Central Bank to switch to rate cuts in 2H24.

If the downtrend in demand continues, the key rate may be lowered to 12% by year end. Otherwise, a year-end rate of 14% would become more likely.

The CBR further clarified its forecast for foreign trade parameters. Expectations for the current account surplus in 2024 were improved to $50 bln from $42 bln in the February forecast. This revision assumes higher oil prices[4] despite risks of their instability as noted by the Central Bank. This improvement will provide additional support to the local currency and **heightens the likelihood that the ruble will consolidate near USD/RUB 95/dollar by year end.**

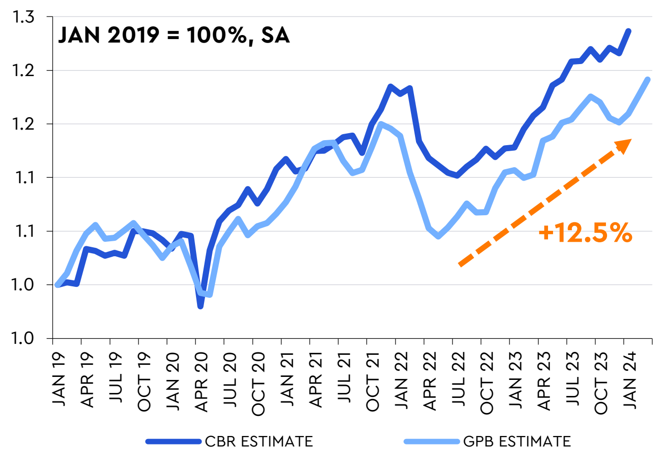
[1] *For details, see our April 22 "CBR meeting preview: Pas de deux for supply and demand".*
[2] *For details, see our April 18 "CPI Monitor: Higher Demand, Lower Prices".*
[3] *For details, see our April 25 "CPI Monitor: First Signs of Cooling Demand?".*
[4] *The CBR's oil price forecast only reflects the dynamics for Brent – an increase to $85/bbl from $80/bbl in the February forecast.*

Chart 1. Demand began to decline in mid-April



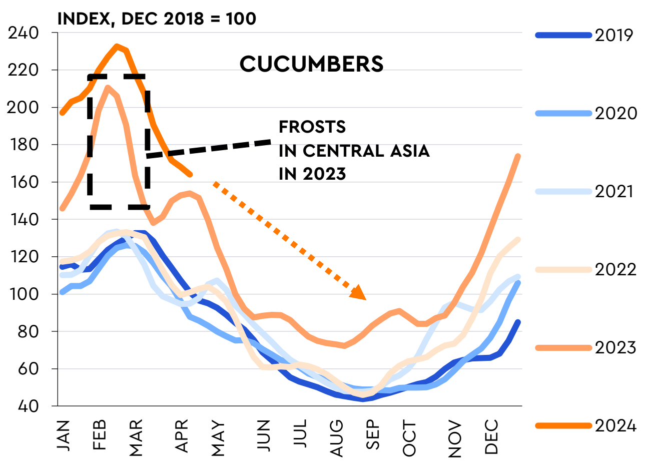
Source: Romir data adjusted for seasonality and inflation, Gazprombank estimates

Chart 2. Production of consumer goods is surging



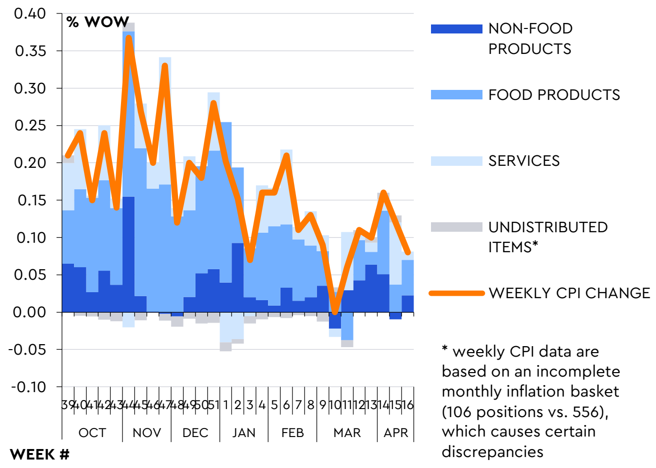
Source: CBR, State Statistics Service, Gazprombank estimates

Chart 3. Vegetable prices as a temporary disinflation factor



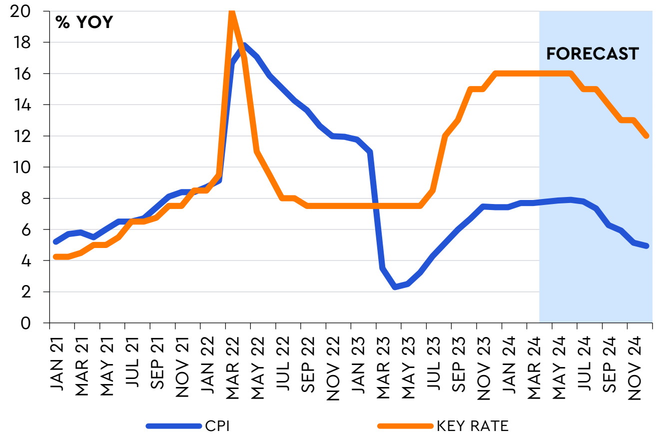
Source: State Statistics Service, Gazprombank estimates

Chart 4. Price pressure is declining



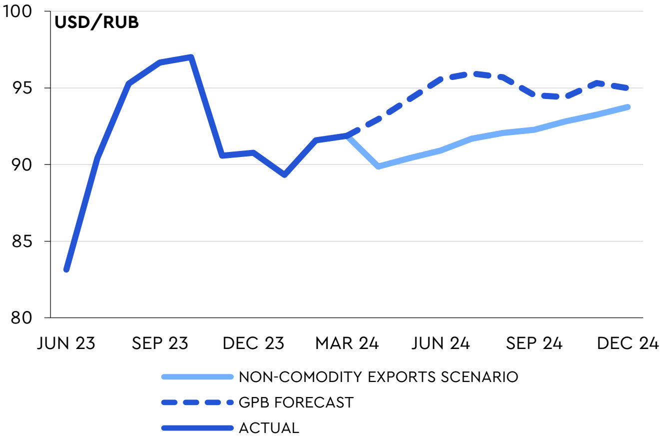
Source: CBR, Gazprombank estimates

Chart 5. Key rate and inflation forecasts



Source: CBR, State Statistics Service, Gazprombank estimates

Chart 6. Forecast trajectory of ruble exchange rate



Source: Minfin, State Statistics Service, CBR, open sources, Gazprombank estimates

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