17 March 2017

Flash Comment

CBR rate decision preview: on hold preparing for cuts

- **We expect the CBR to hold the key rate unchanged on 24 March, though during the past few days the market has started pricing a cut of up to 50bp.**
- **We would expect the CBR's tone to soften, if it is preparing the public for a very gradual easing.**
- **We expect the CBR to start cutting rates during its meeting on 28 April, probably switching to a 25bp step, but we do not completely exclude a 25bp cut on 24 March. However, an action in March would weaken CBR's consistency in communication.**

Assessment and outlook

Next week Friday (24 March 2017) at 11:30 CET, Russia's central bank (the CBR) is due to announce its monetary policy decision. We expect the CBR to keep the key rate unchanged, as does consensus, though within the past few days the market has started pricing a rate cut of up to 50bp.

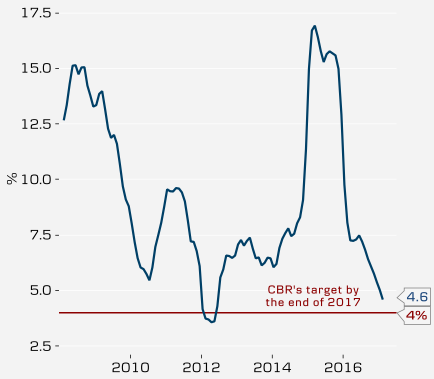
The change in pricing towards a cut in March and the shift in some economists' expectations came after the head of the monetary policy department, Igor Dmitriev, stated that due to a significant decline in inflation 'a rate increase is now out of the question, while a cut of 25 basis points to 50 basis points is possible, as well as holding it unchanged'. However, his disclaimer to this dovishness was that 'risks persist, including from the oil market, the harvest's performance, the global food market. Inflation expectations remain high.' In February 2017, inflation expectations were up and they have been a very important indicator for the CBR's decision making, despite continuing disinflation (CPI fell to 4.6% y/y in February 2017).

During previous press-conferences the CBR governor Elvira Nabiullina has mentioned Q2 17 as a time slot for resuming monetary easing. In addition to the latter argument for no cut in March, the Ministry of Finance's (Minfin) new FX operations mechanism (see our note *Russia unveils FX purchases plan putting a 'speed limit' on the RUB*, 27 January 2017) is maintaining the CBR's hawkishness and cooling down the central bank's monetary easing path in 2017. In February 2017, Minfin was buying approximately USD105m of FX daily, while plans for March purchases are around USD50m per day.

We continue to expect the first cut in Q2 17, with the CBR introducing a 25bp cut on 28 April, while expecting a slowdown in the monetary easing path during 2017. We expect the real rate to stay over 3.0%, subduing possible increases in inflation expectations (also creating downside risks for our 2017 GDP growth forecast of 1.2% y/y), but we see the key rate being cut to 8.50% by end-2017 (our previous expectation was 8.00%).

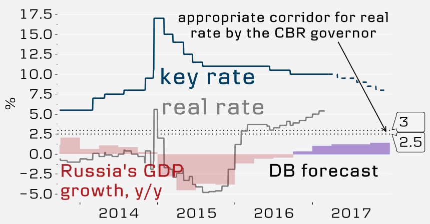
We do not expect a strong reaction in RUB after the meeting if no surprise is delivered and CBR's consistency holds. Yet, given the dovishness of recent comments, a 25bp cut should not be excluded, which would contain RUB's rally, if it were implemented.

The CBR firmly moves closer to the target



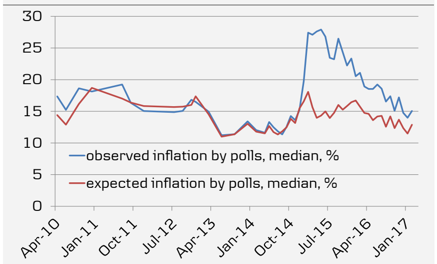
Source: Macrobond Financial, Danske Bank Markets

...while real rate escape from the appropriate corridor is set to curb inflation risks further



Source: Macrobond Financial, Danske Bank Markets

Inflation expectations increased in February 2017



Source: CBR, Danske Bank Markets

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This research report has been prepared by Danske Bank Markets, a division of Danske Bank A/S (‘Danske Bank’). The author of the research report is Vladimir Miklashevsky, Senior Analyst.

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Expected updates

None.

Date of first publication

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