Банк России

12 Neglinnaya Street, Moscow, 107016 Russia
8 800 300-30-00
www.cbr.ru

Statement by Bank of Russia Governor Elvira Nabiullina in follow-up to Board of Directors meeting on 29 April 2022

29 April 2022 Speech

Today, we have made the decision to decrease the key rate by 3 percentage points to 14% per annum.

I would like to remind you that our decision to raise the key rate to 20% was an anti-crisis measure and was made to limit financial stability risks in the first place. Since early April, they stopped to increase. The situation is stabilising, and this means that we may remove the increment from the key rate that was needed to mitigate these risks. Inflation trends have enabled us to ease monetary policy. The reduction in the key rate will promote the structural transformation of the economy without creating proinflationary risks.

I would now dwell on the reasons behind our decision.

Firstly, inflationary pressure and inflation expectations are declining. The evidence for this is that households' soaring demand has diminished and the ruble has strengthened. Over the last two weeks of March, inflationary pressure stabilised after its surge in early March. However, it still remains high.

In April, households' inflation expectations returned to the levels of mid-2021. According to the surveys of households, expected inflation is below the observed price growth, that is, people believe that prices will no longer rise as fast. Companies' short-term price expectations edged down as well, but they are still higher than last year. The stabilisation of inflation expectations and an increase in households' propensity to save mean a decrease in the risk that the inflationary spiral might get out of control.

Secondly, economic activity is declining. In the current situation, supply is contracting more significantly than demand. This is what provokes inflationary pressure at the moment.

Disruptions in technological, production and logistics chains and the termination by some foreign companies of their operation in Russia cause a reduction in the range and availability of many consumer goods. The most illustrative example is the automobile industry. Companies that used foreign raw materials or components are facing problems as they are gradually running out of stocks. The question is how long these difficulties will persist and how quickly businesses will be able to find new suppliers and replace the missing links of the production chain.

The decline in demand is still more moderate compared to the shrinkage of supply, but might become more considerable. In particular, investment demand is going down because the economic situation is highly uncertain. In such conditions, companies opt to invest available unallocated funds in risk-free assets or return them to shareholders rather than make investment in development projects. Moreover, some investment projects are no longer relevant and thus cannot be completed, whereas companies will need time to prepare new projects. As regards consumer demand, after its surge in late February—early March, people now prefer to save rather than consume. This is evident from both the expansion of ruble deposits and the contraction of consumer lending. In terms of inflation, it is important to consider how demand trends will be changing relative to supply dynamics in the future.

During this period, monetary policy should take into account the processes of adaptation and structural transformation in the economy. They inevitably involve a temporarily higher level of inflation. This is why we have no intention to quickly bring inflation back to the target. Squeezed demand would hamper the structural transformation of the economy. This would lead to a situation in the economy where prices would grow slowly, whereas the range of goods and services would become increasingly more limited and some essential products would be simply unavailable.

Speaking of monetary conditions, they remain tight.

On the one hand, both the ruble exchange rate and yields on federal government bonds returned to the level of mid-February. Financial stability risks lowered. On the other hand, the risk premium included in credit rates edged up amid uncertainty. Additionally, banks' requirements for borrowers and collaterals are stricter today, which makes price and non-price lending conditions tighter. The decrease in the key rate will help alleviate this situation to a certain extent.

I would now speak on our macroeconomic forecast.

The termination of long-term economic relations will have a negative impact on GDP this year. GDP will decline by 8–10%, dropping to the lowest point in the fourth quarter. A gradual decrease in demand and supply shocks, monetary policy, fiscal policy, as well as structural measures implemented by the Government will promote the recovery of economic growth since the beginning of next year. Due to the high base of the first quarter of 2022, the overall change in GDP next year as compared to the entire 2022 will range from zero to minus three percent. The fluctuations are very sharp. Hence, to illustrate future dynamics, it would be more representative to compare the fourth quarter of 2023 against the lowest point of the decline, that is, the fourth quarter of 2022. This is exactly why we included a special line in the table of our forecast. We expect GDP to expand by 4–5.5% by the end of 2023, as compared to the end of this year. The same is true for household consumption. Although consumption will decline in 2023 against the overall figures of 2022 (again, because of the high base of the first quarter 2022), it will be 4.5–6% higher in the end of next year than in the fourth quarter this year.

I would briefly talk of the labour market. The situation here is currently quite stable. By March 2022, the employment rate dropped to its record low. Today, the labour market is adjusting to the new conditions primarily through forced leaves, part-time employment schemes, and reduced bonuses. However, due to the current transformation of the economy, the labour market has to address new challenges. The structure of employment will be definitely changing, which might require a redistribution of labour resources both between industries and professions and across regions. We will assess how these processes will influence the pace of the structural transformation of the economy and, accordingly, inflation processes.

The situation with the balance of payments has altered significantly. This year, we might see a record high current account surplus reaching 145 billion US dollars. However, this is not a favourable situation. It only evidences that the contraction of imports is much more considerable as compared to exports, in terms of both their quantities and value. During the next two years, trade flows will be partially rerouted. Imports will start to bounce back gradually. Exports will continue to edge down, including due to declining global prices for core exports. This will cause a notable decrease in the current account surplus.

Speaking of inflation this year, the main driver will be the factors limiting product and service supply. These are rising costs incurred by companies, including for logistics and rearrangement of their production processes, and changes in business models. Supply is contracting more significantly than demand, which is intensifying inflationary pressure. According to our forecast, consumer prices will go up by 18–23% over the year, but this figure comprises the earlier surge in prices beginning from late February, which was most significant in March. Future inflation, that is, annual inflation for the next 12 months, will be much lower as of April 2023. Our baseline forecast assumes that it will range from 10% to 12%.

Prices will mostly adjust to the changed conditions this year, and to a lesser extent — next year. As a result, annual inflation will slow down to 5–7% next year and return to the target in 2024. Inflation will decrease and return to 4% owing to the pursued monetary policy.

Our forecast takes into account all fiscal policy decisions approved and announced by the Government. Updating our forecast in the future, we will factor in all additional decisions as they may have a significant effect on our forecast.

Winding up, I would like to talk of possible risks to our forecast and monetary policy prospects.

The current situation is extremely uncertain. Simultaneously, supply trends and the factors driving aggregate demand are also changing dramatically.

Today, supply is declining faster than demand, but this trend might change in the future. This means that proinflationary and disinflationary effects are both possible. Therefore, it is crucial for the Bank of Russia to make prudent decisions factoring in the changing balance of risks.

At the moment, we consider that the scenario where proinflationary factors and risks prevail is the most probable one. Nonetheless, the pendulum might swing the other way, and in this case demand will decline more quickly than supply. This might occur in a situation where consumers still prefer to save as much as possible, while supply already starts to recover.

There are also other circumstances that might impact our future decisions. For instance, they might be associated with exchange rate movements and a credit contraction, as well as new external trade and financial restrictions that might occur. Indeed, a lot will depend on the development of the situation that is changing very fast. Hence, high-frequency indicators, both at the macrolevel and at the industry and regional levels, are becoming increasingly more important. Today, we see room for a key rate reduction until the end of the year. Currently, the forecast range of the average key rate is 12.5–14.7% for this year, 9–11% — for next year, and 6–8% — for 2024. However, our actual decisions and time when this decrease might become possible will depend on incoming information, future developments, and further changes in the balance of risks.

We will make our further decisions on monetary policy considering that the economy needs to adjust to the dramatically changing conditions. Price stability is always the top priority for us as it is critical for steady economic growth.

Thank you all for your attention.