

Central Bank Holds Rates to Boost Fragile Economy

By [The Moscow Times](#)

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The Central Bank said Tuesday that it might hold interest rates at record lows for a few more months as it tried to boost a fragile economic recovery while insisting inflationary pressures remain in check.

The bank kept the benchmark refinancing rate unchanged at 7.75 percent, in line with expectations, saying that despite a drought-related spike in food prices, "inflationary risks, defined by monetary conditions, remain at an acceptable level."

"The current parameters of monetary policy are thought by the Bank of Russia to ensure an acceptable balance between main macroeconomic risks in coming months," the Central Bank said.

The measured tone caught some analysts by surprise after Central Bank Chairman Sergei Ignatyev said last week that the drought's impact could last until next fall and 2010 inflation

could reach 8 percent — a full percentage point more than had been forecast at the start of September.

"I had expected them to start to turn around their language toward admitting that the pickup in inflation is moving out of the boundaries of just the food sector," said Alexander Morozov, chief economist at HSBC in Moscow.

"I had also expected that the language about [rates being on hold] in coming months would be excluded from the text."

Most analysts polled by Reuters before the Central Bank's decision said they expected it to keep money rates on hold until the end of the year.

Consumer prices rose 0.6 percent in the first 22 days of the month — compared with zero inflation in September 2009 — as the worst drought in decades reduced the grain harvest by a third.

M2 money supply, meanwhile, rose 32.8 percent year on year in August, Central Bank data showed Tuesday.

The Central Bank made no reference to the ruble exchange rate or the potential inflationary impact of the currency's steep drop to multi-month lows in recent weeks.

"The weakness of the ruble may have an extra stimulating impact on prices through pushing up import costs," Morozov said.

A key reason for keeping rates on hold is the still fragile health of the domestic economy, which is recovering from its worst recession in 15 years.

"An increase in uncertainty in the development of the external economic situation creates additional risks for the stable growth of the Russian economy, which means it is necessary to retain a stimulating monetary policy in order to support internal growth factors," the Central Bank said.

Russia's dependence on exports of oil, gas and metals make it especially vulnerable to swings in the global cycle.

"There is a feeling that the Central Bank still sees the need to keep the current monetary policy to support lending growth," said Maria Pomelnikova, economist at Trust.

The drought — and the record heat wave that caused it — took their toll on domestic activity, although the Economic Development Ministry expects growth to return in the fall after gross domestic product shrank a seasonally adjusted 0.4 percent in August, month on month.

Many analysts now expect the Central Bank to start raising rates in the final months of this year or in early 2011.

"It will be interesting to hear the Central Bank's rhetoric after September inflation, when it will be clear how its pace has been affected not just by the food component but by the part that depends on monetary factors," said Vladimir Kolychev, an analyst at Rosbank. "That could

demand some kind of action."

One possible option open to the Central Bank would be to start raising banks' reserve requirements rather than rates, he added.

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88