

Central Bank Leaves Interest Rates, Unworried by Drought

By [The Moscow Times](#)

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The Central Bank left interest rates on hold Tuesday as forecast and signaled no hikes in coming months as it did not expect drought-related price rises to threaten midterm inflation targets.

The benchmark refinancing rate was left on hold at a record low of 7.75 percent for a third month in a row, the Central Bank having halted a 13-month easing cycle in May after 14 rate cuts aimed at reviving sluggish domestic lending.

The ruble extended losses to session lows of 34.56 against its currency basket after the news, which confirmed no immediate prospects of support from higher rates.

The Central Bank said it expected rates to stay put over coming months, "which should encourage further growth in lending activity and provide support for the economy on the path to stable growth."

Inflation rose in August, "due to diverging estimates of the impact of abnormal weather conditions on agriculture production and to the rise of grain prices on the global market," the bank said.

It said there were currently no grounds for concluding that the price spike would have a negative impact on mid- or long-term inflation, though some analysts said risks existed.

The Central Bank also noted "signs of instability in the recovery of economic growth" in Russia and abroad, a further potential reason not to tighten policy.

The Economic Development Ministry reckons that the summer drought and heat wave, which saw many factories halt production, could cut this year's growth by up to 0.8 percentage point.

"The situation with inflation and economic dynamics is seriously distorted by the summer drought, and they clearly want to wait until September data to decide what is really going on," said Maxim Oreshkin, senior strategist at Credit Agricole, who expects that rate hikes will start in early 2011.

Citibank's Elina Rybakova said the Central Bank's cautious tone on inflation risks could be explained by its desire not to further fuel inflation expectations. "Risks clearly exist; an acceleration of inflation is possible," she said.

With drought killing off about a third of this year's crop, consumer prices rose 0.6 percent in Aug. 1 to 23, as Russians stockpiled buckwheat, flour and dry pasta.

But year-on-year inflation is still modest, at 5.9 percent in the month to Aug. 23, according to the Central Bank — meaning that real interest rates are still well in positive territory.

"Inflation is not accelerating because of monetary factors — they cannot make food appear [in stores] by changing rates," said Pyotr Milovanov, a dealer at Metallinvestbank.

The prospect for an extended period of unchanged rates added to an already negative backdrop for the ruble, which had been hurt earlier in the session by a retreat in oil prices and stock markets.

"Rates remain at a very low level and that stimulates capital outflow rather than its inflow," Oreshkin said.

Most analysts polled by Reuters last week predicted that the Central Bank would start to hike rates in early 2011, although a sizable minority reckon that the tightening could begin as soon as the fourth quarter of 2010.

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