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Russia's Central Bank to Build Up Forex Reserves for Years to Come

By The Moscow Times

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ST. PETERSBURG — Russia's Central Bank intends to keep accumulating reserves for years to come, until they reach a "comfortable" level up to $500 billion, bank Governor Elvira Nabiullina said on Thursday, as an economic crisis facing the country is far from over.

Her comments signal the bank will continue regular purchases of foreign exchange, a policy likely to weigh on the ruble as the bank would need to buy some $140 billion to restore reserves — now worth $360.5 billion — to the indicated pre-crisis level.

The policy of rebuilding reserves toward this level also underscores concerns that the economy is highly vulnerable to new financial shocks despite recent signs of stabilization.

"In the optimal situation reserves must be enough to cover significant outflows of capital lasting two to three years. Therefore we now consider as very comfortable a level of reserves, covering long stress situations, of up to $500 billion. This is the level that we were used to," she told a banking conference in St. Petersburg.

Last month the Central Bank announced it would buy between $100 million and $200 million each day in foreign exchange to replenish reserves — a pace that would need to be maintained for some three to six years to restore reserves to $500 billion.

Commenting on broader economic trends, Nabiullina said that although economic indicators were better than expected there were no grounds for complacency.

"It is too soon to speak about all the crisis phenomena passing," she said. "Risks have diminished but in essence they remain just the same and we have to be perfectly aware of that."

Western sanctions, introduced against Russia in response to its actions in Ukraine last year, have made it difficult for Russian companies to borrow abroad, requiring the Central Bank to step in heavily to address shortages of foreign currency.

The bank has recently been winding down its repo facilities for lending foreign currency to banks, which Nabiullina said reflected limited need for these facilities now that a peak of foreign debt repayments this year has passed.

However, she said the specific problems facing Russia meant that it still needed forex reserves that far exceed levels implied by international norms.

She said that according to these norms, Russia already has enough reserves, as they are big enough to cover three months of imports, short-term international debt and 20 percent of the money supply.

Based on a composite index of these common standards, the adequate level of reserves for Russia would be $188 billion, she said, with existing reserves almost twice that level.

"The situation is such that we must consider also covering demand for reserves connected with limited access to the markets, [and] with the outflow of capital, for a longer period than is proposed by standard approaches to reserve sufficiency," Nabiullina said.

"Therefore one of the tasks over the period ahead is to grow the reserves over the course of years."

Nabiullina also said the pace of reserve accumulation could be varied depending on market conditions.

She said the policy would not be allowed to interfere with the bank's central monetary policy goal of lowering inflation to 4 percent in the medium term.

Commenting on the bank's interest rate policy, Nabiullina said the bank had cut rates "smoothly" this year as it judged the risk of a cooling economy to be greater than inflationary risks, but she added that a faster pace of cuts would be risky.

"Inflation expectations are still high and a too rapid reduction (of rates) in these conditions could lead to a new wave of destabilization on the currency market and a jump in inflation," she said.

The bank next meets to discuss its key lending rate on June 15, with a Reuters poll of analysts predicting a one percentage point cut.

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