ROSBANK
SOCIETE GENERALE GROUP

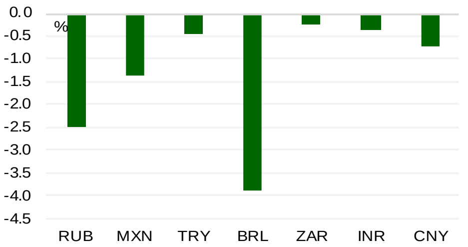
Café et Croissant

Monday, December 07, 2020

Main Indicators

	Last	1wk	ytd
USD/RUB	74.2	-2.9%	19.8%
EUR/RUB	89.8	-1.2%	29.2%
EUR/USD	1.21	1.7%	8.2%
DXY	90.7	-1.2%	-5.9%
Brent, $/bbl	49.3	2.2%	-25.4%
Gold, $/t oz	1,839	2.9%	21.2%

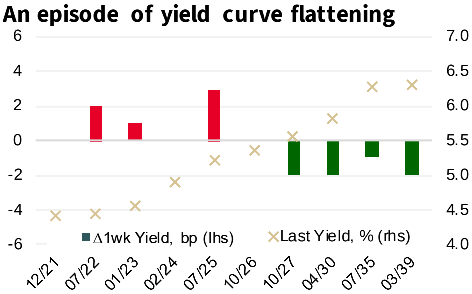
EM currencies over the week *



** '+' = depreciation, '-' = appreciation*

	Last	1wk	ytd
$ UST'10, %	0.97	0.13	-0.95
€ BUND'10, %	-0.55	0.04	-0.36
$ Russia'29, %	2.26	0.02	-0.68
OFZ 5y (26229), %	5.23	0.01	-0.94
OFZ 10y (26228), %	5.81	-0.02	-0.55
OFZ 15y (26225), %	6.22	-0.01	-0.31

An episode of yield curve flattening



Russian Weekly

Foreign Currency Market

Commodity currencies led the charge last week as the Russian ruble gained extra 2.5% on the US dollar but only posted 4th best performance across EM FX, losing out to COP, BRL and CLP. The weekly low for USD/RUB registered 73.76, i.e. the strongest level for the Russian currency since early September.

We view oil market rally as the key driver of the move: Brent price almost touched $50/bbl in the aftermath of the OPEC+ decision to smooth production hikes from the start of 2021. Global risk sentiment also stayed robust, thanks to expectations of vaccination against covid-19 coming soon in a number of countries.

Domestically, announcement on the MinFin FX market interventions for December was a rare highlight. At RUB 2.2bn daily, the volume doesn't look massive by itself. However, coupled with RUB 4bn of daily operations from the CBR, this should provide support to the ruble, given thin liquidity overall.

This week, we expect attempts to stabilize from the USD/RUB, as market participants start pondering whether the recent rally has stretched too far (lest we forget, there were trades at 80.95 in early November). Oil prices look destined to adjust lower as well, with headlines on likely production boosts from Norway and Iran denting the sentiment. In addition, price-wise, the USD/RUB is nicely balanced around the 200-day moving average (74.21) and needs clear drivers to break this level.

On the contrary, the EUR/USD should meet extra volatility this week as the EU and the UK are stuck in race against time to strike the long-awaited trade agreement. Even a last-minute deal might be challenging for business on both sides of the la Manche tunnel, given so little time to prepare legislation. The euro is already above 1.21, time to prove this level is sticky.

Fixed Income

Transition into festive season goes on. Last week, performance of local sovereign bonds varied across the curve, ranging from +3/+5bp on the front end to -1/-3bp for longer-dated benchmarks. As the Russian yield curve remains very steep by recent historical standards – e.g. 2s10s spread at 135bp vs. 36bp average over 1H'20 – the long-end bonds are a more enticing play at times when the global sentiment improves. Generally, however, activity level remains subdued as the year come to its close.

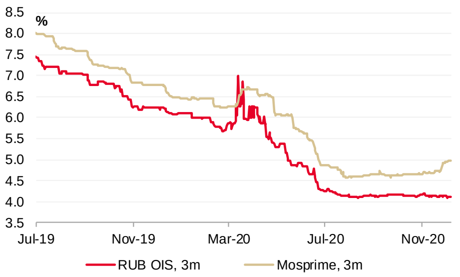
On the primary market, the Finance Ministry kept experimenting by offering fixed-rate securities – even knowing in advance demand would be weak, unless there was a whopping yield pick-up to grab. Last Wednesday, total demand amounted to unimpressive RUB 34.7bn and placement volume landed at RUB 18.5bn, as the authorities consented to a ca. 5bp yield premium. Again here, there was no excitement around primary auctions, with annual domestic borrowing plan 99% accomplished.

At this stage, the biggest question to us is how long the OFZ market can ignore global demand for risk assets, reflected, inter alia, via strong rally in the ruble. Yes, domestic banks are already full of RUONIA-floaters, following the 2-month-long binge over October and November. Yes, international accounts are staying on the sidelines before J.Biden assumes the Oval Office in Jan'21. Yes, inflation in Russia is on the up (November reading 4.4% yoy), likewise the ruble interest rates (MosPrime 3m 4.97%). But for anyone who can look beyond that and focus on long-term drivers, such as persistent weakness of domestic demand (i.e. inflation containment) and gradually diminishing primary debt supply from the MinFin, nominal OFZ yields as high as 5.81% for 10 years and 6.29% for 15 years should look appealing.

Main Indicators

	Last	1wk	ytd
Ruonia o/n % (1-day lag)	4.02	-0.05	-2.21
USD/RUB swap o/n, %	3.72	-0.21	-2.27
₽ Mosprime'3m, %	4.97	0.04	-1.48
$ Libor'3m,%	0.23	0.00	-1.68
USD/RUB Xccy 1y, %	4.06	-0.02	-2.04
USD/RUB basis 1y, bp	-79	1	-35

Mosprime-OIS basis to top out



Russian Weekly

Money Market

Structural liquidity surplus started to improve. The structural RUB liquidity surplus improved to RUB 0.88tn last week, and should continue rising higher through the end of December. A plunge in the roll of the 1m REPO from the CBR into January 2021 by c. RUB 0.4tn to 0.8tn should push the structural balance to RUB 1.2-1.3tn already on Tuesday. More to come over the next few weeks, with the budget system opting to switch between saving and spending modes. Namely, the MinFin should distribute roughly RUB 2.0tn to meet the deficit target of RUB 4.7tn, certainly if no bureaucratic delays emerge similar to those seen last year (up to RUB 1.0tn of spending on National Projects was postponed).

This improvement in the liquidity landscape raised hopes for better supply of medium-term deposits, which are highly important for banks to replace deposits from the MinFin and the DepFin of Moscow. Limited supply of medium-term cash from financial authorities has already pushed the 3m Mosprime higher to 4.97%, though speed of adjustment geared down (+2bp on the week). Residual pressure may pass onto 3m Mosprime in forthcoming weeks, especially given an intrigue with a guidance from the CBR on December 18. However, with the key rate seen flattish in the range 4.25-4.50% during 2021 (and even 2022) we consider the turning point in the Mosprime-OIS (85bp) basis has been reached and may open opportunities for receiving Mosprime and IRS implieds.

Indicator *	Last		Prior	
Markit PMI Mfg	Nov	46.3	Oct	46.9
Markit PMI Services	Nov	48.2	Oct	46.9
Car Sales, % yoy	Nov	5.9	Oct	7.0
CPI, % yoy	Nov	4.4	Oct	4.0
CBR Reserves, $bn	Oct	583	Oct	583
Trade Balance, $bn	Sep	10.1	Aug	3.2
Budget Balance, ytd ₽tn	Oct	-1.8	Sep	-1.8
Ind. production, % yoy	Oct	-5.9	Sep	-3.6
Retail Sales, % yoy	Oct	-2.4	Sep	-3.0
Unemployment Rate, %	Oct	6.3	Sep	6.3
Real Wages, % yoy	Sep	2.2	Aug	0.1
GDP, % yoy	3Q20	-3.6	2Q20	-8.0
CA Balance, $bn	3Q20	2.5	2Q20	-0.5

Outlook

Indicator	1Q21	2Q21	3Q21
Brent, $/bbl	45.0	50.0	52.5
USD/RUB	72.0	69.5	68.5
EUR/RUB	86.4	85.5	85.6
GDP, % yoy	-1.1	5.4	2.7
CPI, % yoy	4.3	4.1	4.0
Key rate, %	4.25	4.25	4.25
OFZ 10y, %	5.20	5.00	5.20

** recent updates highlighted with red*

Macroeconomics

Inflation seasoned with depressive PMIs. Last week, the IHS Markit reported further decrease in manufacturing PMI in Russia (46.3p vs. 47.7p in October) and solid increase in services PMI (48.2p vs. 46.0pp in October). This combined change should hardly leverage the recovery of the domestic economy through the end of the year as both remained in 'depressive' area and did not express much hope for recovery of demand in the near term. The picture has a striking difference with the US and China, where comparable indicators continue to evolve in expansionary mode.

The only conclusion we may infer from PMI readings is that the authorities should prefer expansionary policies. While the fiscal stance is not an intrigue with the budget finally approved, the CBR remained a closed book. The point of concern is that the CPI rate in November spiked to 4.42% yoy driven by food prices (5.97% yoy). This may have direct impact on 1Q21 inflation as a starting point for index calculation (i.e. base effect versus 1Q20) and indirect implication for inflation expectations later during the year, especially for those demand-sensitive segments, which were unable to implement upfront indexation in 4Q20. One of such segments is the services sector (c. 28% of the consumption basket, of which c. 14% are not regulated by the Government) – it has demonstrated stalling prices at 2.33% yoy excluding tariffs (2.57% yoy tariff-based inflation) till now, but hardly will ignore the post-pandemic recovery.

Against such backdrop, the CBR will have a brain-teaser on December 18 of balancing out front-load inflation acceleration (above the expected range 3.9-4.2% on the turn of the year) and potential disinflation induced by the stalling recovery of the labor market. We do not see a better solution than tightening guidance for at least 1-2 upcoming meetings and thinking about the bottom of the key rate further on.

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Appendices

Date	Event	Forecast	Expected impact
December 10	ECB meeting	Extension of PEPP into December 2021, TLTRO IV launched	Further support for the European assets, spotlight on the US authorities to follow-up with the stimulus package

Café et Croissant

Weekly – November 30 (eng)

Weekly – November 23 (eng)

Weekly – November 16 (eng)

Weekly – November 9 (eng)

Markets and economics

Russian macro update – 3Q'20 (eng)

OFZ Auction Alert – November 25 (eng)

Russian forecasts update – Nov'20 (eng)

CBR meeting preview – Oct'20 (eng)

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