ROSBANK

SOCIETE GENERALE GROUP

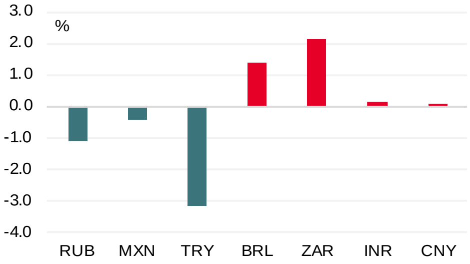
# Café et Croissant

Thursday, June 17, 2021

## Main Indicators

| | Last | 1wk | ytd |
|---|---|---|---|
| USD/RUB | 72.1 | -1.0% | -2.8% |
| EUR/RUB | 87.4 | -1.6% | -3.6% |
| EUR/USD | 1.212 | -0.6% | -0.8% |
| DXY | 90.5 | 0.6% | 0.7% |
| Brent, $/bbl | 72.9 | 1.9% | 40.7% |
| Gold, $/t oz | 1 864 | -1.6% | -1.6% |

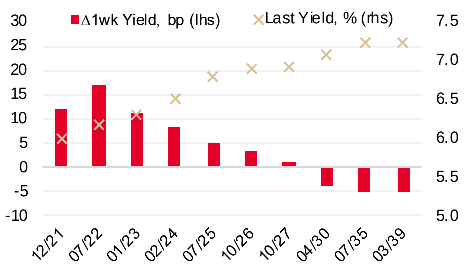
**EM currencies last week ***




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

| | Last | 1wk | ytd |
|---|---|---|---|
| $ UST'10, % | 1.49 | -0.07 | 0.58 |
| € BUND'10, % | -0.25 | -0.05 | 0.32 |
| $ Russia'29, % | 2.46 | -0.11 | 0.34 |
| OFZ 5y (26229), % | 6.89 | 0.04 | 1.37 |
| OFZ 10y (26228), % | 7.17 | -0.06 | 1.12 |
| OFZ 15y (26225), % | 7.23 | -0.05 | 0.79 |

**Russian local sovereign bonds last week**




## Russian Weekly

### Foreign Currency Market

**The ruble preserved appreciation bias over the last week** with the USD/RUB targeting 71.50 and the EUR/RUB 87.0. The move was backed by a number of external and internal factors, which may have temporary effect and high versatility.

- First, the oil market backdrop preserved bright colors with the Brent breaking above $73.0/bbl. The outperformance of the spot price still runs amidst of solid backwardation (12m discount is 7.8%) and bright views on potential recovery of demand during holiday season. Meanwhile, SG strategists downgraded their outlook for medium-term price Brent performance to $60/bbl for 2022 (-$5/bbl) by stating that backwardation is excessive compared with potential inventories depletion.
- Second, anticipation of further tightening of the monetary policy in Russia gained some arguments last Friday following the 50bp hike. Despite the move, hawkish views on the CBR stance prevailed that might render bullish views on the RUB excited. The net long CFTC positon on the RUB remained fairly positive, while the risk-reversal estimate (difference between call and put options) declined to minimum levels seen post the pandemic, implying more attractive carry opportunities.
- Third, the geopolitics is the hottest topic for this week due upcoming Putin-Biden meeting on 16 June. The agenda will be manifold and will likely touch the most sensitive topics, which have been mentioned recently in the context of potential sanction restrictions against Russia. Provided minimal signals on potential concessions, any kind of concern or misunderstanding between parties might be perceived as a signal for volatility.
- At last, the dollar-bears kept rebuilding positions ahead of the FOMC meetings. The DXY struggled to correct amidst of short covering in the UST segment. Nonetheless, dollar liquidity inflows from the Fed will likely remain open end and render initiative to the non-dollar world, especially, commodity currencies.

### Fixed Income

**All eyes on the primary market.** Last week, preparation for the hawkish outcome of the CBR MPC meeting was still driving sentiment in the local bond space. The OFZ curve continued to flatten - on the week, yields changed by +9bp/+17bp on the front end and by -4bp/-6bp on the long end. This week, attention jumps to the primary market as the MinFin is about to place the inaugural local bond after restrictions for US persons entered into force on 14 June.

The intention of the MinFin to target the long-end of the curve in new bond issuance stays intact. On Friday, 11 June the authorities announced that the first 3 series eligible for auctions have maturities in March 2029 (issue 26237), July 2031 (26239) and May 2041 (26238). That does make sense from the issuer's perspective, but investors aren't necessarily as excited about the flat shape of the OFZ curve (e.g. the 10y yield is only 28 bp above the 5y) as the MinFin itself.

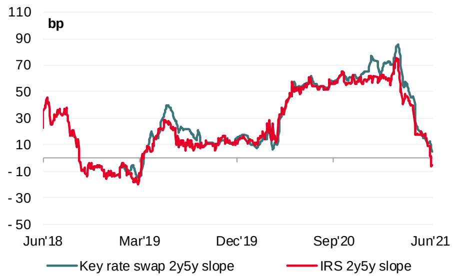
The big question for auctions tomorrow is whether the MinFin targets a larger volume of debt (thus, is ready to pay up) or targets a cheap yield (thus, is ready to cut aggressive orders). The only somewhat similar experience from the past came in November 2020, when the Ministry carried out the inaugural EUR-denominated transaction after the US restrictions for non-ruble primary borrowings entered into force in August 2019. Back then, EUR 750mn of the 7-year bond were priced at a 148bp spread over mid-swaps and EUR 1.25bn of the 12-year bond, at 197bp, vs. the EUR 1.75tn of the outstanding 5-year bond trading at a 119bp spread. This implies the spread pick-up for maturity extension was some 10-20bp juicier than for the curve of EUR-denominated bonds issued by Mexico at the time. So, in a nutshell, nothing is alarming.

Knowing that tomorrow the MinFin will target a moderate issuance volume (RUB 30bn), we believe the authorities will try to avoid serious yield pick-up over the now-off-the-run bond series. The Ministry has already executed 56% of the annual RUB 2.8tn plan, hence, proper signaling to market participants with regards to yield would look comparatively more important at this stage.

## Main Indicators

| | Last | 1wk | ytd |
|---|---|---|---|
| Ruonia o/n % (1-day lag) | 5.04 | 0.30 | 0.77 |
| USD/RUB swap o/n, % | 5.50 | 1.09 | 0.76 |
| ₽ Mosprime'3m, % | 6.18 | 0.24 | 1.26 |
| $ Libor'3m,% | 0.12 | -0.01 | -0.12 |
| USD/RUB Xccy 1y, % | 6.25 | 0.24 | 2.02 |
| USD/RUB basis 1y, bp | -80 | 11 | 2 |

### Swap curves on the brink of inversion




| Indicator * | Last | | Prior | |
|---|---|---|---|---|
| Markit PMI Mfg | May | 51.9 | Apr | 50.4 |
| Markit PMI Services | May | 57.5 | Apr | 55.2 |
| Car Sales, % yoy | May | 133 | Apr | 290 |
| CPI, % yoy | May | 6.0 | Apr | 5.5 |
| CBR Reserves, $bn | May | 605 | Apr | 590 |
| Trade Balance, $bn | Apr | 10.6 | Mar | 10.0 |
| Budget Balance, ytd ₽tn | May | 0.3 | Apr | 0.2 |
| Ind. production, % yoy | Apr | 7.2 | Mar | 2.3 |
| Retail Sales, % yoy | Apr | 34.7 | Mar | -3.4 |
| Unemployment Rate, % | Apr | 5.2 | Mar | 5.4 |
| Real Wages, % yoy | Mar | 1.8 | Feb | 2.0 |
| GDP, % yoy | 1Q21 | -1.0 | 4Q20 | -1.8 |
| CA Balance, $bn | 1Q21 | 16.8 | 4Q20 | 6.1 |

### Outlook

| Indicator | 3Q21 | 4Q21 | 1Q22 |
|---|---|---|---|
| Brent, $/bbl | 65.0 | 62.5 | 60.0 |
| USD/RUB | 73.0 | 72.0 | 72.0 |
| EUR/RUB | 91.3 | 91.4 | 90.0 |
| GDP, % yoy | 2.7 | 2.2 | 4.0 |
| CPI, % yoy | 6.2 | 5.0 | 4.1 |
| Key rate, % | 5.75 | 5.75 | 5.75 |
| OFZ 10y, % | 7.30 | 7.10 | 7.00 |

** recent updates highlighted with red*

## Russian Weekly

### Money Market

**The ruble liquidity market returned to normal, medium-term deposits were priced with a larger premium.** The new averaging period brought all the aspects of cash market into common stance. Banks withdrew a dramatic portion from short-term deposits held with the CBR (-RUB 3.1tn to RUB 1.0tn) back to nostro accounts (RUB 3.7tn today in the morning), while the MinFin continued to rebalance term deposits (-RUB 416bn) and direct spending (+RUB 224bn).

At the same time, the MinFin's span of instruments got a clearer shape: while the dominant portion of funds is built of 7, 14 and 35 day deposits, some regular opportunities for 63 and 182 days emerged. The longest deposit, if placed in early July will provide some transitory deposits into 2022, which usually has highest demand. Those options were well bid over the last couple months besides some residual speculation about the CBR stance – a solid premium in 63 (26bp on 10 June) and 182 days (66bp on 7 June) deposits hinted at some challenges with meeting LCR requirements by the end of 2Q21 (i.e. by 30 June). Other than that, dependence on Treasury funds remained decent (RUB 2.5tn).

Swap curves suffered from bear flattening. The 2s5s IRS swap slope ditched the inversion area at -6bp, while the 2s5s key rate swap curve slipped to 5bp amidst of further monetary tightening left on table last Friday by the CBR. Actually, the wording was a bit tougher than one could expect and paved the way for bearish trades in the rates space. In the macro section below we discuss why we do not consider the tightness of the CBR 'unconditional', so far we see further flattening of both curves as overstretched and conditions worth to be picked up (in favor of steeper curves). The moment to accumulate these trades will be contingent to the post-sanction regime in OFZ segment and some clearer picture on the US-Russia relations.

### Macroeconomics

**The CBR raised the key rate by 50bp (to 5.5%) and updated a number of assumptions made in April**, so that tightening of policy and guidance became the only possible option. According to the CBR, the current economic performance is dominated by a strong rebound in internal demand, which prompts sustainability of price deviations. The economy may restore its pre-crisis shape by the middle of 2021, while subsequent growth may bear reflationary risks owing to limited production capacity. Consequently, the regulator highlighted between the lines that the inflation pressure may have more features of 'permanent' process rather than globally presumed 'transitory' spike.

Nonetheless, we are not inclined to consider tightening of the guidance as 'unconditional' signal for further aggressive action. At least one comment of E.Nabiullina from her press-conference pointed to continual discussion of monetary tactics on the backstage of the MPC meeting. The regulator discussed a hike by 100bp at once, but declined to do so (or even a 75bp hike) because of a number of reasons. First, the recent key rate hike cannot be considered out of the context of tightening cycle started in March (the key rate was raised by +75bp before 11 June) that given the transmission channel might bring early fruits through the end of 2021. Second, atypical seasonality in price dynamics is blurring the side of manageable 'inflation shock', whilst even extreme front-load tightening is helpless to resist short-term inflation spikes. Because of this, the most suitable tactics is critical assessment of incoming data with a short note in mind that upcoming harvest season may cause strong impact on annual inflation dynamics and inflation expectations.

Given all this, we have mixed feelings about the outcome of the CBR meeting – we still see a wide range of options for the regulator on the upcoming meeting that keeps valid our baseline assumption of a 25bp hike in July. Nonetheless, we cannot exclude alternative moves (more or less hawking) in case of new extraordinary data prints.

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## Appendices

| Date | Event | Forecast | Expected impact |
|---|---|---|---|
| **16 June** | US and Russia presidents to hold a summit | | Geopolitical risks have been discounted by markets recently, so any signal of escalation could trigger volatility |
| **16 June** | Fed to hold regular meeting | SGe: unchanged, 0.0%<br>CNS: unchanged, 0.0% | Consensus drifted towards a non-event with respect to QE program. Nonetheless, some critical assessment of inflation or rates trajectory may cause correction in UST yields. |

### Café et Croissant

**Weekly – Jun 7** ( eng )

**Weekly – May 31** ( eng )

**Weekly – May 24** ( eng )

**Weekly – May 17** ( eng )

### Markets and economics

**Russian macro update – 4Q'20** ( eng )

**OFZ Auction Alert – June 9** ( eng )

**Russian forecasts update – May'21** ( eng )


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