

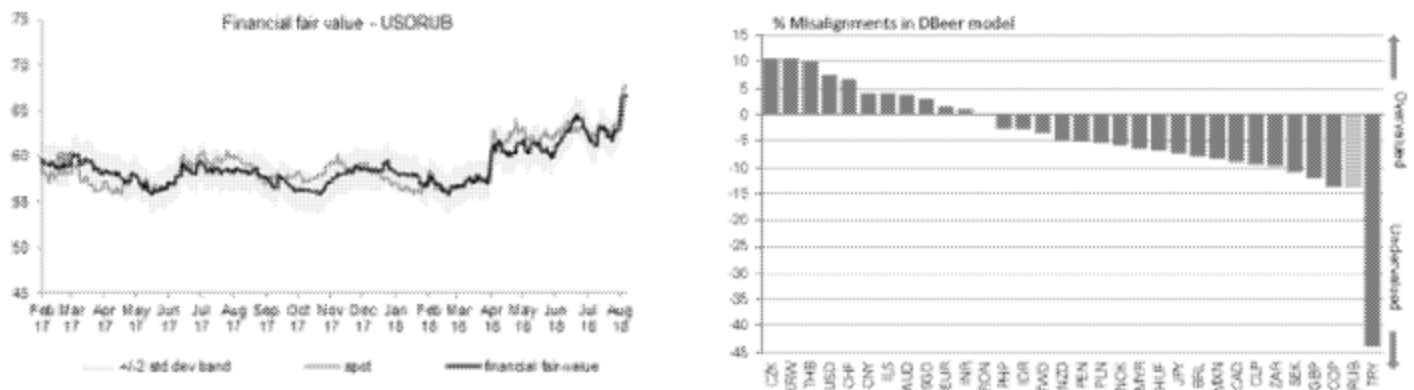
economy and an escalation of the situation is also not yet our base case scenario (see Econ section), near-term uncertainty has increased. The situation is noticeably more severe for FX than local bonds.

RUB: Our recently published EM FX Scorecard shows RUB as the fourth attractive EM currency. RUB benefits particularly from attractive long-term valuation (DBer fair value for USDRUB at 54.6), but also robust growth momentum, now lighter positioning and high real rates. Further, the hawkish stance of the CBR provides additional protection. Last but not least, even our short-term valuation model implies the fair-value somewhat lower (66.65). Although the residuals are not yet at extreme levels, all our models point towards an overshooting in price action during the recent selloff.

Local bonds: The local curve aggressively bear-flattened in recent weeks with 3Y-5Y bonds trading back above 8.0%. Overall, valuation looks attractive. Despite the upcoming increase in price pressure further fuelled by the FX weakness, we see limit risk of any interest rate hike anytime soon. This said, the market is now pricing rate hikes back into the curve. While the local curve (IRS vs Mosprime) is pricing 60bp of hikes until end-year, the XCCY swap curve is back to unchanged interest rates by year-end, the most hawkish pricing since early April. Further, foreign holdings are back to the lowest level since Q2-17 and upcoming supply dynamics are reasonably favourable.

Our long-term fair-value model for 10Y local bonds based on a) inflation, b) oil, c) short-end rates implies 10Y local bonds closer to 7.25% vs the current level of 8.30 (see chart). This said, term-premium on the curve remains low with a spread of only 10bp between Feb-24 and May-34. While we preferred long-end bonds so far, we now see more value in the belly of the curve.

Figure 5: Our short-term financial valuation model implies that FX overshoot during the recent selloff..., however, the actual dislocation is relative to the long-term fair value



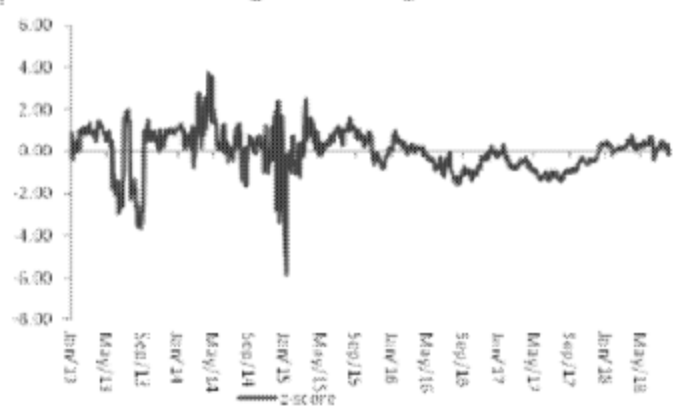
Source: Deutsche Bank

Figure 7: Foreign holdings are back to the lowest level since Q2-17



Source: CBR, Deutsche Bank

Figure 8: Term-premium in local bonds (shown as z-score) has once again declined in recent weeks and is now back to the long-term average.



Source: Deutsche Bank