Weekly Review
4 • 26.1.2018

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Russia

Relatively slow growth outlooks for Russian economy. Updated forecasts from the IMF and World Bank expect Russian GDP growth to reach 1.7 % this year. The Central Bank of Russia sees similar growth. The January Consensus Economics forecast is a bit higher. In general, major institutions have raised their outlooks from last summer by several tenths of a percent on higher oil price assumptions. The oil price climbed by about 25 % last year from 2016, averaging about 53 dollars in 2017. While the IMF and World Bank expect a clearly higher average oil price this year, the CBR forecast oil price assumption is a bit more cautious. The Russian economy ministry says GDP grew by 1.4–1.8 % last year.

Global economic growth is generally expected to accelerate. The forecasts see the Russian economy growing slower than nearly all other CIS countries, Europe's advanced economies, the US, and among relatively large economies, e.g. Poland, Turkey, Brazil and Mexico.

Russian GDP growth forecasts, 2018–2019

	GDP		Oil price, USD	
	2018	2019	2018	2019
Bank of Russia (12/17)	1.5–2.0	1.0–1.5	55 (Urals)	45
IMF (1/18)	1.7	1.5	60	56
World Bank (1/18)	1.7	1.8	58	59
Consensus Economics (1/18)	1.9	1.8	61	

Sources: IMF, World Bank, CBR and Consensus Economics.

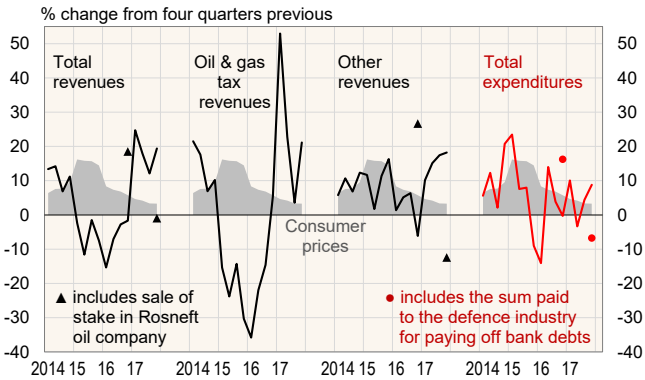
Improved Russian federal budget performance; deficit shrinks. 2017 fourth-quarter budget revenues were again up significantly from 4Q16 (not including funds received in 4Q16 from the sale of a 19 % stake in state oil giant Rosneft). Oil & gas tax revenues were boosted by higher oil prices, and other budget revenue streams continued to see significant gains.

For the entire year 2017, federal budget revenues increased by 18 % (again, excluding the money from the 2016 sale of the Rosneft stake). Tax revenues from oil & gas were up by nearly 25 %, significantly outperforming original budget projections. The additional oil revenues to be transferred to the Reserve Fund were abundant as the average price of Urals-grade crude last year climbed to 53 dollars a barrel (the initial 2017 budget assumption was 40 dollars). Other budget revenues increased by 15 %, e.g. on higher VAT revenues that account for over 55 % of the federal budget's non-oil revenue streams and about a third of total federal budget revenues. Tax collection improved.

On-year growth in federal budget spending picked up in the fourth quarter (excluding the massive government repayment of bank loans taken on earlier by defence contractors, a.k.a. the OPK complex, at the end of 2016. Rather tight budget discipline was maintained last year, with spending increasing by 5 % (excluding the OPK bank loan repayment), or about 1 % in real terms. Defence spending fell by about 4 % (or about 25 % if the 2016 OPK bank debt operation is included). Spending on domestic security and law enforcement increased about 1 % in nominal terms, while a lot of the spending in this category was allocated from other subcategories to Russia's National Guard, which currently accounts for a substantial part of Russia's domestic security forces.

Thanks to improved revenue performance, the 2017 federal budget deficit was just 1.4 % of GDP, less than originally planned. In 2016, the budget deficit was nearly 3.5 % of GDP. Without money from oil & gas tax revenues, the deficit contracted in 2017 to less than 8 % of GDP.

Federal budget revenues, expenditures and inflation 2014–17



Sources: Russian Ministry of Finance and BOFIT.

Russian foreign debt turned to slight growth last year. At the end of 2017, Russia's foreign debt was about 530 billion dollars, an increase of 3 % y-o-y. Russian banks continued to pay down foreign debt, while debt of non-bank companies and government increased. At the end of 2017, the foreign debt of banks amounted to 105 billion dollars, non-bank firms 354 billion dollars and government 56 billion dollars. About 85 billion dollars in debt comes due this year.

From the peak of end-2013, the value of foreign debt has fallen by 200 billion dollars. Nearly half of the reduction, however, came from shifts in foreign exchange rates, particularly ruble depreciation (about a quarter of Russia's foreign debt is denominated in rubles). Russian banks have reduced their foreign debt by about half since the end of 2013, while other corporates have seen their indebtedness fall only slightly. Although firms have paid down their dollar-denominated debt, their ruble- and euro-denominated debt has risen since the end of 2013.

The value of the Russian government's total foreign debt has also shrunk from the end of 2013 largely on ruble depreciation. The government has paid down its dollar-denominated debt while increasing its ruble-denominated debt. Russia's government debt is still quite low: at the end of 2017, foreign debt was 56 billion dollars and domestic debt 124 billion dollars, or 11 % of GDP in total.

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China

Forecasts of major international institutions see China sustaining strong growth in coming years. Following the World Bank's lead earlier this month, the International Monetary Fund released its own updated global economy forecast this week. Both forecasts revised their China 2018 growth outlooks up slightly on, among other things, recovery in external demand. The medium-term risks are trending upward with the financial sector's increasing vulnerability and rising trade barriers around the world. The IMF slightly raised its global economy forecast, and now expects growth of 3.9 % p.a. in 2018 and 2019.

Other forecasting institutions generally agree that Chinese growth will remain robust in coming years and that China will make its long-term policy goal of doubling real GDP between 2010 and 2020. At the moment, this would require average growth in the range of 6.2–6.3 % p.a. up to 2020. The EIU had earlier expected that China's leaders would have already shifted their policy emphasis to getting debt under control, with growth slowing significantly in 2018–20. The new EIU forecast sees lower growth shift coming after 2020. Investment banks that monitor China expect growth to average 6.5 % p.a. in 2018. Forecasts range from 5.8 % to 6.9 %.

Even if official figures show that China is on track to hit its GDP growth target, two international forecasting bodies, the Conference Board and Capital Economics, point out that China's methodology for calculating GDP growth is faulty and fails to reflect true economic trends. Both forecasters release alternative estimates for the Chinese economy that suggest significantly lower growth than official estimates. The alternative indicators, in particular, diverge from official GDP growth figures in the 2015–16 period, when also many other measures of China's growth indicated much lower readings.

GDP growth forecasts for China, %

	2017	2018	2019
IMF 1/2018	6,8	6.6	6.4
World Bank 1/2018	6.8	6.4	6.3
OECD 11/2017	6.8	6.6	6.4
Asian Development Bank 12/2017	6.8	6.4	-
Economist Intelligence Unit 1/2018	6.8	6.4	6.3
Conference Board (proxy)11/2017	4.2	3.9	3.8*
Capital Economics (proxy) 1/2018	5.8	4.5	4.5
BOFIT 9/2017	6.5	6	5

** Average of Conference Board growth forecast for 2018–2022.*

Lower growth in China's debt ratio. The People's Bank of China reports that its broad measure of credit, Total Social Financing (TSF), was up 12 % y-o-y in December. The TSF stock rose by a percentage point less than in December 2016. The stock of bank loans, which represents over two-thirds of TSF financing, continued to rise at the same pace as in 2016 (about 13 % y-o-y). The stock of TSF credit reported for the shadow banking sector grew faster than the traditional banking sector (up 15 %). Most growth came from trust and entrusted loans. Such loans are subject to new restrictions from the start of this year. Growth in corporate bond financing was lower than the TSF average.

About half of new bank lending went to households. The stock of household loans rose by about 25 % over the course of last year. Fastest growth was in short-term household lending, usually in the form of unsecured credit (at year's end the pace of growth exceeded 40 % y-o-y). Such credits are partly used as bridge loans (e.g. to help meet the downpayment on an apartment purchase). Household lending has increased in recent years and now accounts for about a quarter of bank lending. The stock of corporate loans rose 13 % y-o-y in December.

The stock of TSF credit stood at 211 % of GDP at the end of 2017. Nominal GDP growth accelerated slightly (up 11 %), and growth in the debt ratio slowed to a crawl. The debt ratio was only up by 2 percentage points from December 2016, even if it has averaged growth of over 10 percentage points a year over the past five years. The BIS cited its own evidence that growth in the debt-to-GDP ratio has slowed. The total indebtedness of Chinese firms, households and the public sector at the end of June 2017 was 256 % of GDP, four percentage points higher than in June 2016, when the debt ratio had grown by nearly 20 percentage points over 12 months.

Trends in TSF growth and China's debt ratio

Sources: BIS, PBoC and Macrobond.

Borrowing becomes more expensive in China. The PBoC's slight tightening of monetary policy during 2017 was reflected in interbank market as higher SHIBOR rates and demands for higher yields on new issues of government and corporate bonds. The interest rate on China's 10-year government bond rose by nearly 100 basis points last year to 3.9 %. The yield on corporate bonds rose even more last year. Higher financing costs were also reflected in the price of bank loans in the first three quarters of 2017. As of end-September, the nominal rate on the average bank loan was 5.8 %, while apartment loans were slightly cheaper (5 %). Both average rates were about 50 basis points higher than a year earlier. Respective real interest rates (4.2 % and 3.4 %) rose even more due to modest inflation. Even so, they were considerably lower than at the beginning of 2015.

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