

## Russia

**Russian economic recovery slow last year.** Preliminary figures from Rosstat show that Russian GDP grew by 1.5 % in 2017, slightly less than nearly all forecasters had expected. Recovery was relatively slow given that the oil price rose by over 25 % from 2016. On-year GDP growth fell below 1.5 % in the fourth quarter.

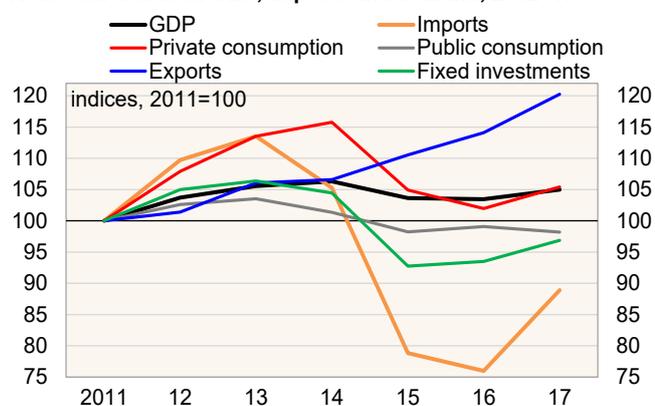
The rise in GDP was partly stymied by imports, which soared 17 %. The growth of imports relative to GDP growth was exceptionally fast. The rise in imports reflected the extremely low level of imports in 2016, a 25 % rise in Russian export earnings and real ruble appreciation of 16 % from 2016. Import growth cooled a bit in the fourth quarter, but was still 15 % y-o-y.

Most of the economy's demand categories rose in a good tempo last year. Growth in the volume of Russia's exports accelerated, reaching 5.4 %. Domestic demand increased by over 3.5 %. That was the pace of growth also in private consumption, which was reflected in rising domestic retail sales and sales of services as well as the spending of Russians when travelling abroad. Public consumption further declined slightly.

Fixed investments rose over 3.5 %. The Central Bank of Russia estimates that most of the growth in investments came from one-off government investments and construction of the Power of Siberia natural gas pipeline. Growth in inventories made an unusually large contribution to growth in domestic demand. The figures for GDP components in 2017 may see even substantial revisions later on as suggested by the large entry for "statistical discrepancy" in the preliminary figures.

GDP last year returned to its 2013 level. Consumption and fixed investments were still below the levels where they were half a decade ago, however. Imports were about 10 % below their 2011 level.

**Real-term trends in GDP, imports and demand, 2012–17**



Source: Rosstat.

**Role of the Russian state in banking sector continues to expand.** Three systemically important banks were placed under central bank administration last year. Additionally, a total of 63 credit institutions had their licences revoked. Most of the banks losing their licences were relatively small players, so their departure from the market had little impact. The Deposit Insurance Agency reimbursed private individuals with accounts at these banks as planned.

[Otkritie Bank](#) and [B&N Bank](#) (Binbank), two of Russia's top 10 banks in terms of total assets, failed late last summer. Both were placed under central bank administration. After a rash of rumours about impending collapse of a third large bank, [Promsvyaz Bank](#), the CBR stepped in and took over in mid-December. Market reaction has been muted as the central bank interventions were largely anticipated. After the take-overs, seven of Russia's ten largest banks are state-owned. Collectively, they represent 60 % of the banking sector's total assets.

The CBR now plans to merge the operations of Otkritie and Binbank. The goal is to create a competitive universal bank that could eventually be privatised. Finding interested private buyers in the near future looks challenging, however. The restructuring of Promsvyaz will likely focus on creating a bank specialised in serving military-industrial complex and state procurement.

While the departure of small boutique banks is likely to improve banking sector efficiency and financial intermediation, the total collapse of three major banks has raised eyebrows. Despite strict banking supervision, even large banks have managed to conceal their risk exposures. During 2017, total assets of the banking sector rose by 6.4 %, slightly outpacing inflation. If banks that lost their licences are not included, the growth in bank balance sheets was around 8 %. At the start of 2018, 561 banks operated in Russia and the total assets of the banking sector equalled 92 % of 2017 GDP.

**Fast growth in household lending in 2017.** The CBR reports that the bank credit stock rose by 3.5 % when exchange rate shifts are included. The stock of corporate loans was largely unchanged, while household lending soared. The stock of household lending grew by 13 % last year, and stood at 12 trillion rubles (\$200 billion) at year's end. According to various credit bureaus, the total amount of new lending last year reached 5.7 trillion rubles, an increase of about 40 % from 2016. Highest growth was registered for unsecured credit card debt and housing loans. The microcredit industry also expanded rapidly. Such speedy growth has raised concerns about over-indebtedness. Even with rising wages, the real incomes of Russians fell by 1.7 % last year.

Small banks only account for a tiny share of household lending. Russia's 50 largest banks hold about 90 % of all household loans. While only about half of Russian banks are registered in Moscow, over 90 % of household credit is granted by Moscow-based banks. About a third of borrowers live in Moscow or the surrounding Central Federal District.

## China

### China's new initiatives to protect the environment.

Official rhetoric on improving the environment in China has been backed up with deeds in recent months. In addition to a new environmental protection tax, the government has banned the import of problematic waste and announced the implementation of an emissions trading scheme. Defying expectations, tighter environmental regulation resulted in an improvement in Beijing's air quality last year. Greenpeace reports that air pollution values were down by over 30 % in the last quarter of 2017, which offset the poor air quality trend of the first three quarters. Progress nationwide, however, was not as impressive, with the least progress in improving air quality in years. Part of the problem was that industrial production growth appears to have accelerated from the low growth of previous years, even if it is difficult to discern any fluctuations in growth from official GDP figures.

The new environment protection tax, which entered into force at the beginning of January, replaces an arrangement in place since 1979, whereby polluters paid an emissions fee to the environmental regulators. The shifting of collection responsibilities to tax officials should make it more difficult to evade payment, a fairly common activity in the past. The tax rate varies according to pollutant and province. Local governments have been granted the authority to impose taxes as long as they are within the range set forth by the central government. Implementation of the environmental protection tax has been criticised for giving local governments too much freedom in setting rates. Many local governments have decided to set the rates close to the lower limits, even if they retain the taxes collected. For example, under the upper and lower limits set by the central government, an air pollutant tax could be set anywhere in the range of 1.2 to 12 yuan per 0.95 kilograms of nitrogen or sulphur dioxide emissions. China's biggest coal-producing region, Shanxi province, has imposed an air pollution tax of just 1.8 yuan. A similar move was taken by Guangdong province, a hub of high-tech production. Critics point out that it is not at all certain that officials are capable of gathering reliable data on the amount and nature of pollution generated by firms. There are also worries that companies will try to circumvent emission taxes.

An import ban on problematic waste was imposed in conjunction with the environmental protection tax. The ban applies to 24 types of problematic waste such as household plastics and unsorted paper. The ban has global implications. Many countries, particularly developed Western nations, send their waste abroad for processing. China has been the world's leading waste importer for decades. In 2017, for example, China imported about 40 million metric tons of plastic, paper and metal waste worth roughly \$22 billion.

The government also announced at the end of December that a pilot emissions trading scheme was being rolled out nationwide. While only power plants are initially required to

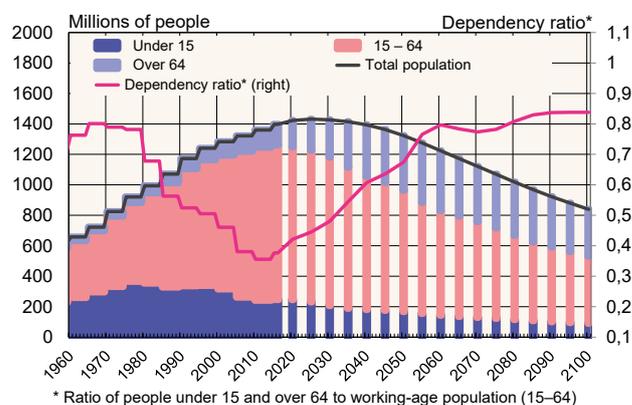
participate in the trading scheme, the goal is to eventually expand the programme to include other polluters.

**Beijing's population growth stopped last year.** Last year, for the first time this millennium, the population of Beijing showed no increase. The population of Beijing was 12.6 million people in 1999, and 21.7 million in 2016. The city's official population last year declined by 22,000 people. Part of this reflected local government efforts to limit pollution, traffic congestion and internal migration. The shantytowns of migrant workers have been torn down and the operation of small business restricted. Factories, logistics centres, schools and hospitals have been forced outside the city limits. A cap on Beijing's permanent resident population has been set at 23 million until 2020. In Shanghai, China's largest city, the goal is to cap the population at 25 million by 2035 (the population was about 24.2 million in recent years).

The UN projects that China's population will peak at 1.43 billion about ten years from now, and thereafter begin to decline. While the one-child policy was replaced two years ago with a two-child policy, it appears that the change has done little to increase childbirths to the extent hoped for by policymakers. The new policy targeted annual births of 20 million. The actual number of children born in China in 2016 was 17.9 million. Last year's number was 17.3 million.

With lower birth rates and people living longer, China's dependency ratio is deteriorating rapidly. According to a UN forecast, by 2050 there will be nearly 70 dependents (children under 15 or adults over 64) per 100 working-age persons. In 2015, the number of dependents per 100 workers was just 37. Finland's dependency ratio in the same timeframe is expected to rise from 58 to 71. The measurement technique, however, underestimates China's true dependency ratio, because the retirement age in China is well below 64 years. Women typically retire between 50 and 55, while men retire at 60. The predicted shift in China's demographic structure increases the pressure on the central government to institute reforms, particularly in the areas of pensions and family policy.

### Trends in China's population and dependency ratio



Sources: UN and Macrobond.