Weekly Review
4 • 25.1.2019

BOFIT

Russia

Russian export earnings up significantly in 2018. Preliminary balance-of-payments figures for the fourth quarter of 2018 show Russian revenues from exports of goods & services were up nearly 20 % y-o-y even if the growth was no longer as fast as in the previous quarter. For the entire year, export earnings were up by over 20 % as revenues from energy exports ballooned by over 30 % on strong export prices.

Russia's spending on imports of goods & services in the second half of last year was unchanged from 2H17. For all of 2018, spending on imports was up by a few per cent. The spending of Russian travellers abroad was up by about 10 % for the year although the growth stopped in the fourth quarter. The overwhelming underlying factor was ruble depreciation. Total spending on imports of goods & services in the second half of last year roughly matched 2008 and 2010 levels.

The gap between export earnings and spending on imports widened in 2018 to produce a whopping current account surplus of about 7 % of GDP – Russia's largest current account surplus since 2006.

The net capital outflow from the private sector increased substantially in 2018. The flow of direct investments from abroad into the Russian corporate sector (excl. banks) dried up almost entirely, while FDI outflows from Russia remained rather notable. Similar to 2017, banks' capital outflow abroad mostly arose from decreases in their foreign liabilities.

Russian balance-of-payments key items, 2016–2018

	USD billion			% of GDP		
	2016	2017	2018 (preliminary)	2016	2017	2018 (preliminary)
Current account	**25**	**33**	**115**	**1.9**	**2.1**	**7.0**
- Exports (goods & services)	332	411	509	25.6	26.1	31.0
- Imports (goods & services)	266	327	345	20.5	20.7	21.0
Trade balance (goods)	90	115	194	7.0	7.3	11.8
- Exports	282	354	443	21.7	22.4	27.0
- Imports	191	238	249	14.8	15.1	15.2
Services trade balance	-24	-31	-30	-1.8	-2.0	-1.8
- Exports	51	58	65	3.9	3.7	4.0
- Imports	75	89	96	5.8	5.6	5.8
Other current account items	-42	-51	-49	-3.2	-3.2	-3.0
Financial account & net errors	**-16**	**-10**	**-76**	**-1.2**	**-0.7**	**-4.6**
Government (excl. central bank)	4	12	-5	0.3	0.8	-0.3
Private sector total (A+B)	-19	-25	-68	-1.4	-1.6	-4.1
A. Banks	1	-23	-31	0.1	-1.5	-1.9
B. Other private, incl. net errors	-20	-2	-37	-1.5	-0.1	-2.2
- Direct investment	11	-9	-24	0.8	-0.6	-1.5
- to Russia	31	27	2	2.4	1.7	0.1
- from Russia	20	36	26	1.6	2.3	1.6
- Portfolio investment	-4	-10	-2	-0.3	-0.6	-0.1
- to Russia	0	-4	-1	0.0	-0.3	-0.0
- from Russia	4	5	1	0.3	0.3	0.1
- Foreign currencies in cash *	5	6	7	0.4	0.4	0.4
- Fictitious transactions	1	0	0	0.0	0.0	0.0
- BoP net errors and omissions	-5	2	1	-0.4	0.1	0.0
- Other items under B	-27	8	-19	-2.1	0.5	-1.2

* Positive value = decrease in the stock of foreign currencies in cash

Source: Central Bank of Russia.

Russian foreign debt declined last year. Russians owed roughly 450 billion dollars to foreign (non-resident) entities at the start of this year. Russia's foreign debt, measured in dollars, fell by 12 % in 2018.

While half of Russia's foreign debt is denominated in dollars and a quarter in rubles, nearly two-thirds of government foreign debt is denominated in rubles. Measured in dollars, the debt has decreased due to debt repayment and depreciation of the ruble. Foreigners have reduced their investment positions, especially in ruble-denominated government debt.

The government accounts for 10 % of the country's foreign debt, banks another 19 % and non-bank corporates nearly 70 %. Especially banks' foreign liabilities are counterbalanced by their assets held abroad and receivables from abroad.

Besides foreign debt, the stock of direct investments that have flowed from abroad into Russian firms (incl. banks) was about 520 billion dollars at the beginning of October.

Topics at Moscow Gaidar Forum feature future economic growth and national projects. At the annual mega-get-together for economic discussions last week, economy minister Maxim Oreshkin noted that Russian economic growth will not be driven by global growth but will rather depend on domestic measures and fixed investments. The ministry's forecast expects GDP growth to accelerate from its current pace of around 1.5 % to over 3 % in 2021, if investment growth picks up to over 7 %. The economist panel at the forum saw that the fixed investments would have to come especially from private firms. They were assessed to account for about 70 % of investments. The panel included outlooks anticipating GDP growth of some 1.5–2 % for the next few years.

Alexei Kudrin, Russia's finance minister throughout the 2000s and currently chairman of the Accounts Chamber, said that it would be extremely difficult to achieve growth above 3 %. He noted that the outlook for domestic demand was insufficient for that and stressed the need to improve the export capabilities of Russian industries. He further emphasised the need to improve business market confidence through systemic reforms such as reforming public administration, reducing the role of the government in the economy and the burden on firms caused by officials' actions as well as devolving own authority to regional administrations.

Kudrin said that such reforms are not included in the national projects launched, thus denoting that the projects will not be enough to reach the country's growth and investment goals (the 13 national projects cover areas such as infrastructure, productivity, education and health care). Kudrin pointed out the high complexity of administrative structures for national projects, programmes and target plans. In addition, finance minister Anton Siluanov noted the need to coordinate state projects at the federal and regional levels, pointing out that over half of the tasks included in the national projects is in the competence given to regional and local authorities. An amount equivalent to nearly 4 % of GDP will be channelled to national projects during 2019–2024. Of that amount, over one quarter is additional funding for projects set forth in president Putin's May inauguration Decree.

Bank of Finland • Institute for Economies in Transition, BOFIT
P.O. Box 160, FI-00101 Helsinki
Phone: +358 9 183 2268 • Web: www.bofit.fi/en

Editor-in-Chief Jouko Rautava• Email: Jouko.Rautava@bof.fi

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China

China's economy continues to slow. Official figures show Chinese GDP growth slowed further last year to 6.6 % p.a. from the revised 2017 growth of 6.8 %. In the fourth quarter of 2018, the pace of on-year growth officially slowed to 6.4 %. China last experienced such weak growth figures in the first quarter of 2009, when the impacts from the global financial crisis hit the Chinese economy hardest. In nominal terms, GDP grew last year by 9.7 % to around 90 trillion yuan (13.6 trillion dollars, 11.5 trillion euros).

Several indicators suggest a sharper slowing in growth than the official figures imply. The weakness in fixed investment is particularly difficult to square with official GDP figures, even with the obvious litany of problems with investment figures themselves. Fixed investment officially correspond to about 40 % of Chinese GDP, while real growth in urban-area fixed asset investment (FAI, which does not correspond to fixed investment in the national accounts) last year was only about 1 %. Because the net impact of foreign trade on economic growth was even negative, it is hard to see domestic consumption alone propping up the official GDP growth figures. Retail sales, a key measure of consumer demand, increased by about 7 % last year in real terms, down from 9 % in 2017. Thus, the reported mere 0.2 percentage point slowdown in GDP growth from 2017 seems suspect.

While GDP demand figures have yet to be released, the NBS reports three-quarters of 2018 growth came from domestic consumption. Output-side figures show services slightly increased their relative share of GDP to just over 52 %, while the combined share of manufacturing and construction was 41 % and primary production 7 %.

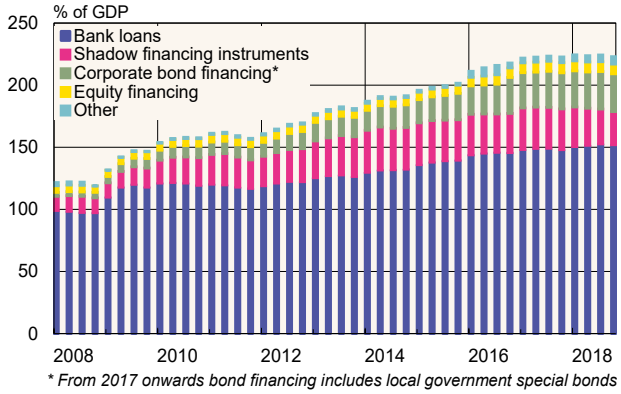
China's ratio of bank credit to GDP continues to rise. China's bank lending stock rose by 13 % y-o-y in December. However, monetary easing last year failed to significantly boost bank lending and economic growth as growth in the bank credit stock has averaged 12–13 % p.a. since 2016. Still, growth was considerably higher than nominal GDP growth (10 %). As of end-2018, the bank credit stock corresponded to 152 % of GDP (137 trillion yuan, 20 trillion dollars).

The stock of bank lending to households still grew by 20 % last year, despite deceleration due to a smaller rise in apartment prices. Household loans represented 39 % of all new bank loans issued last year and 28 % of the total bank credit stock. Excluding loans to households, the stock of bank lending rose by 11 % last year.

Central bank figures suggest that the stock of shadow-banking sector credit instruments (entrusted loans, trust loans and banker's acceptances) shrank by 11 % last year to 27 % of GDP (24 trillion yuan, 3.5 trillion dollars).

The ratio of corporate bonds to GDP was 30 %. That share does not include bonds issued by the government or banking sector, which are by far the largest bond issuers in China. Local governments have increasingly turned to issuance of so-called special-purpose bonds to finance infrastructure projects. The central government has raised special-purpose bond quotas for local governments to allow them to reduce their off-balance-sheet financing through local government financial vehicles. Last year, the PBoC added local government special-purpose bonds to be included in its aggregate financing statistics arguing that special-purpose bonds substitute for other financing formats such as bank loans and corporate bonds. The amount of special-purpose bonds on issue has more than doubled since early 2017. They now represent over a quarter of bonds on issue.

Non-bank corporate and household financing sources (stock)

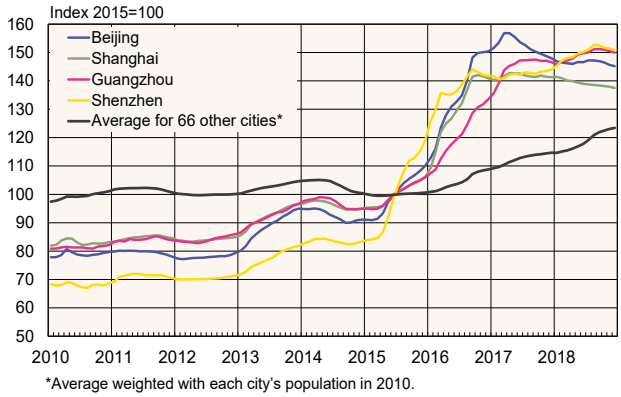


Sources: PBoC, CEIC and BOFIT.

Apartment prices in China's big cities in decline at the end of 2018. Figures from the National Bureau of Statistics and survey data produced by the Soufun housing real estate portal show that apartment prices in Beijing, Shenzhen and Guangzhou (prices per square metre of floorspace) went into decline in the latter of 2018. Shanghai apartment prices fell all last year. Even with the price drops, apartment prices in big cities are stratospheric relative to personal incomes.

Risks to the real estate sector persist. Many construction companies are deeply in debt. A significant adjustment in housing prices would spell trouble for builders and households, and ultimately the banks that finance them.

Average apartment prices in China's cities



Sources: NBS, CEIC and BOFIT.

Bank of Finland • Institute for Economies in Transition, BOFIT
P.O. Box 160, FI-00101 Helsinki
Phone: +358 9 183 2268 • Web: www.bofit.fi/en

Editor-in-Chief Jouko Rautava• Email: Jouko.Rautava@bof.fi