Weekly Review
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BOFIT

Russia

Russian government releases new guidelines for national projects. As part of his inaugural decrees in May 2018, president Putin set forth twelve national priority areas and a handful of infrastructure modernisation programmes to be implemented during 2019–2024. The twelve national priority areas comprise 69 federal-level projects. The costs of implementing the projects is currently put at 26 trillion rubles or about 4.3 trillion rubles (65 billion dollars) annually, an amount that corresponds to approximately 4.5 % of 2018 GDP. While 70 % of funding is supposed to come from budget, it is still unclear how much of an increase in budget spending, if any, will be required to cover the costs.

The biggest ruble spending will go to implementation of infrastructure, road and demography programs. Each federal-level project in the programme has its own detailed set of goals. Often there are hundreds of benchmarks for hitting these goals. Some project targets are quite simplistic (e.g. the average housing loan interest rate will be 7.9 % in 2024), while some are expansive and general (e.g. the share of persons younger than 40 among academic researchers will grow). The mass of specific performance criteria for the wide-ranging projects creates a benchmark jungle that is difficult to oversee and possibly counterproductive to project implementation.

Russia last year produced and exported more gas and oil than before. Russia extracted 556 million metric tons of crude oil and associated gas in 2018. Average daily crude production exceeded 11 million barrels a day last year. This is 2 % more than in the previous year. Thanks to a reinterpretation of the agreement on voluntary production restrictions among a group of oil-producing countries in June, Russia's daily output increased by 4 % during the second half of 2018. However, new restrictions will likely reduce production in coming months. Also natural gas production grew last year. Production reached 725 billion cubic metres. This is 5 % more than in the previous year.

Most of Russia's oil and gas production still takes place near the Urals mountain range in the Perm, Komi, Nenets and Khanty-Mansi regions. Other fields are found in the Far East, lower Volga and Caucasus regions. About two-thirds of Russian oil production and one-third of gas production goes to exports, mostly to Europe. The combination of increased oil and gas export volumes from higher production and higher oil and gas prices lifted export earnings of the energy sector by a third.

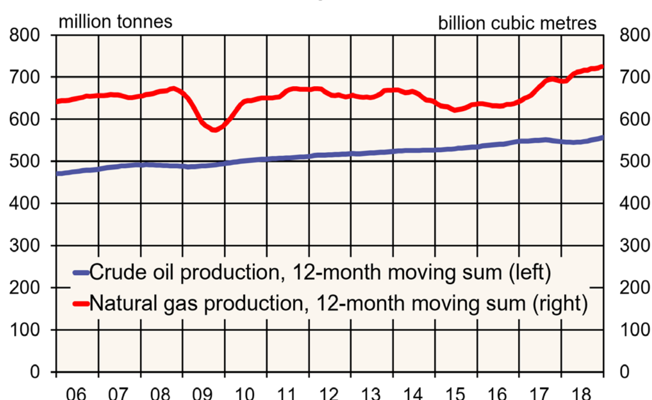
Natural gas has traditionally been transmitted via large pipeline grids, but liquefaction makes cargo shipments possible, too. The recent phased start-up for the liquefied natural gas (LNG) facility on the Yamal peninsula has facilitated gas exports. At the end of last year, about 10 % of Russia's natural gas exports were already being shipped in liquid form. In addition to new gas export pipelines to China and Germany under construction, new LNG facilities are planned.

Russian retail sales up overall, but growth has slowed in recent months. The volume of retail sales last year grew by 2.6 % y-o-y. The pace of growth varied during the year, however, slowing to 2.3 % y-o-y in December. After several years of contraction, Rosstat reports that the volume of retail sales increased by roughly 5 % in the time period of 2017–2018.

The volume of food sales rose by 1.7 % last year. The volume of retail sales increased despite lower household disposable incomes (BOFIT Weekly 2019/06). This may be partly explained by the rise in sales of inexpensive goods as well as a distinct increase in household borrowing. The stock of household borrowing increased by 22 % last year. However, most of the increased borrowing came from housing loans (BOFIT Weekly 2019/07).

In January 2019, retail sales volume growth was dragged down by a general increase in the value-added tax (VAT) rate from 18 % to 20 %. January retail sales volumes rose by 1.6 % y-o-y, while growth in sales of non-food goods slowed sharply to just 1.2 %. The VAT rate on food was unchanged, however, and growth in food sales picked up slightly last month.

Russian crude oil and natural gas output



Source: CDU TEK.

Annual growth in Russian retail sales

Source: Rosstat.

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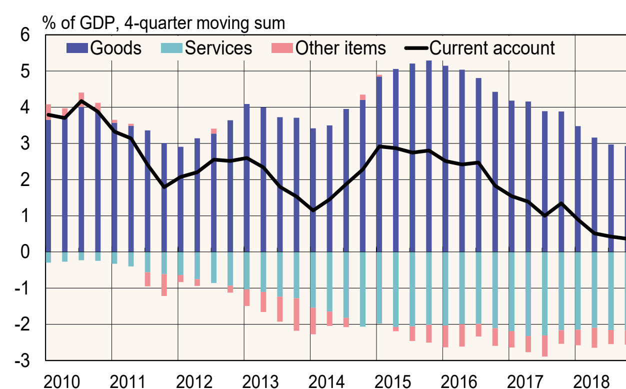
China

China's current account surplus nearly evaporated last year. China's current account surplus last year fell to just 0.4 % of GDP, down from 1.3 % in 2017. In monetary terms, the 2018 current account surplus amounted to a mere 50 billion dollars. The goods trade surplus of roughly 400 billion dollars was largely offset by a services trade deficit of about 300 billion dollars and a deficit in net income and transfer payments totalling another 50 billion dollars.

Besides the reduction in the goods trade surplus, the current account surplus has been curtailed by increased purchases of foreign services. Tourism, in particular, has caused large outflows of money from China. Chinese tourists abroad last year spent 240 billion dollars more than foreign tourists spent on visits to China.

China's current account, % of GDP



Sources: SAFE, Macrobond and BOFIT.

Chinese bank lending breaks records in January. The People's Bank of China reports that the stock of yuan bank loans increased to 3.23 trillion yuan (480 billion dollars) in January, an increase of 13.4 % y-o-y. January bank lending activity is typically brisker than in the final months of the year. The PBoC this year has been actively encouraging commercial banks to increase their lending.

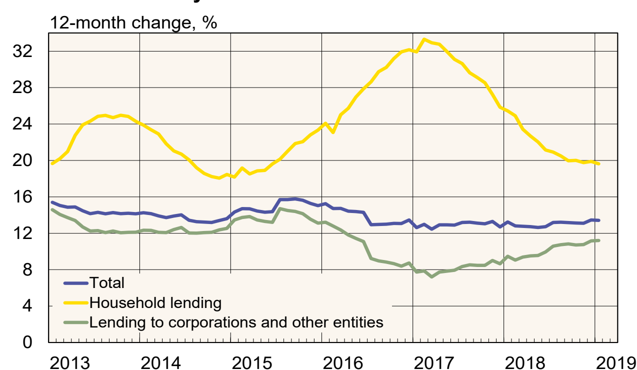
The stock of lending to households increased by 990 billion yuan in January. About a third of that was short-term lending. Lending to non-financial companies and state organisations increased by 2.58 trillion yuan. Nearly half was in the form of short-term loans (e.g. bill financing), suggesting that demand for financing of real investment is relatively weak.

The PBoC reports that the average 12-month interest rate on bank loans was 5.9 % at the end of September. At the end of January, the stock of yuan-denominated bank loans was 139.53 trillion yuan (155 % of GDP). Thus, if the average interest rate is applied to the entire credit stock, the interest costs alone would be about 690 billion yuan (100 billion dollars) a month. A big part of new corporate sector borrowing likely goes to paying down debt and interest.

Besides bank loans, firms sought financing in January through the net issue of 500 billion yuan in corporate bonds and another 340 billion yuan's worth of shadow banking sector instruments. While the stock of shadow banking instruments was up again in January, it is still 10 % smaller than a year ago.

The stock of yuan bank deposits increased by 7.6 % y-o-y. Growth has slowed over the past two years, and new deposits were down on-year in January. At the end of January, the stock of yuan deposits was 180.79 trillion yuan (201 % of GDP).

Growth in stock of yuan-denominated bank loans



Sources: PBoC, CEIC and BOFIT.

US-China trade talks continue. On February 14–15 in Beijing, China's vice premier Liu He and US trade representative Robert Lighthizer prepared a memorandum of understanding to serve as a basis for an eventual trade agreement to be signed by the presidents of both countries. Both parties acknowledged progress in the talks, but no concrete results were mentioned. Talks resumed this week in Washington, DC.

EU intensifies monitoring of Chinese investment. On February 14, the EU parliament approved by a large majority new rules on screening investments and acquisitions of third-country companies seeking to make inroads into strategic EU sectors. The new rules enter into force in October 2020.

The new system gives the European Commission opportunities to investigate and comment on third-country investments in EU strategic branches. The purpose of the legislation is to assure that foreign state-owned enterprises are unable to threaten fundamental EU interests such as security and public order. While China was not specifically named, the investment activities of Chinese state enterprises appear to have provided impetus for the legislation.

Even with the European Commission's new authority, the power to permit or prevent foreign investment remains with EU member states. The new system calls for better exchanges of investment information among member states, but does not require every state to have its own monitoring regime. About half of EU states have third-country investment monitoring schemes in place.

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