Weekly Review
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BOFIT

Russia

Russian economic growth accelerated. Rosstat's preliminary estimate puts third-quarter GDP growth at 1.7 % y-o-y, well above the 0.7 % rate for the first six months of this year. The acceleration in GDP growth apparently reflects higher export volumes and inventories, as there have been few signs of any revival in domestic demand. Retail sales growth in the third quarter slowed to just 0.8 % y-o-y, a decline from the 1.8 % pace set in the first half of this year. Construction has remained practically flat for the entire year. Our latest *BOFIT Forecast for Russia* expects GDP growth of around 1 % this year.

Russian stock exchange on the upswing. In recent weeks, the RTS (Russian Trading System) index, Russia's core dollar-denominated stock index, has climbed to levels not seen since 2013. The rise in share prices has been driven by oil & gas companies, which account for about half of the RTS index weighting. The sub-index for companies in the oil & gas sector has risen to its highest levels in over a decade. The trends in other sectors have been more modest. Weak private consumer demand in recent years has hurt the performance of companies in the consumer sector. The financial sector sub-index has been depressed by such factors as Western sanctions and problems at certain banks.

The Russian media conglomerate RBK recently compiled a list of Russia's fastest growing companies. Oil & gas companies are the most numerous in the list. The top ten also include companies involved in building infrastructure for the energy sector, metal ore mining, as well as firms involved in agriculture and the gaming industry. A similar list produced by the *Financial Times* for fast-growing firms in Europe is dominated by technology and e-commerce firms.

Russia's RTS stock index and some sectoral sub-indices

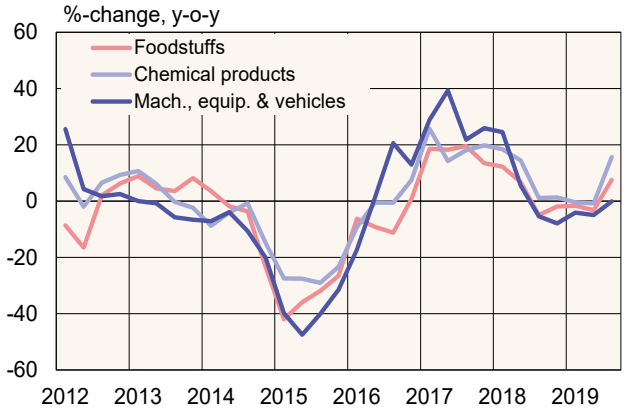
Source: Macrobond.

Russian foreign trade development remains muted. The value of Russian goods exports contracted by 5 % y-o-y in the first nine months of this year to a level of 390 billion dollars. The contraction mainly reflected lower oil prices. Combined export volume of crude oil and oil products grew by 1 % y-o-y. While the volume of natural gas exports through pipelines declined slightly, exports of liquefied natural gas (LNG) soared with the ramping up of production on the Yamal peninsula this year. Oil & gas still accounted for nearly two-thirds of Russia's exports. Other important export products include metals (9% share) and chemical products (6 %). While metal exports have contracted this year, exports of chemical products have grown slightly.

The value of Russian goods imports in January-September was essentially unchanged from a year earlier, holding at around 175 billion dollars. While growth in imports of chemical products and metals was modest, imports of machinery, equipment & transport vehicles contracted slightly. Machinery, equipment & transport vehicles accounted for nearly half of imports. Other major import categories included chemical products (19 %) and foodstuffs (12 %).

The EU accounted for 45 % Russian goods exports and 36 % of goods imports. China was Russia's largest individual trading partner, accounting for 13 % of exports and 22 % of imports. Countries in the Eurasian Economic Union accounted for just under 10 % of both exports and imports.

Change in value of Russian imports in select product categories



Sources: CEIC and BOFIT.

Russia prepares new measures to support firms subject to Western sanctions. In order to systematise subsidies, Russia's finance ministry has proposed a legal distinction for firms subject to Western sanctions. While the relevant subsidies have yet to be defined, suggestions include looser forex rules and the possibility of not disclosing certain economic information. The finance ministry is even contemplating the establishment of a separate stock exchange for sanctioned firms to help them raise financing. Russia's ministry of industry and trade has proposed favouring firms subject to Western sanctions in public procurements.

The proposed measures are feared to further reduce competition, weaken transparency in the economy and increase opportunities for various abuses.

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China

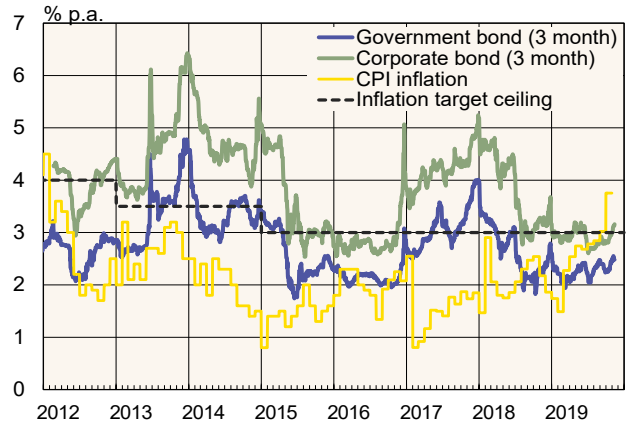
Rising inflation limits monetary easing in China. Consumer prices rose 3.8 % y-o-y in October, outpacing the government's target ceiling of 3 %. Inflation target in China is, however, not as critical a component of monetary policy as in many other countries. The setting of the inflation target occurs at the National People's Congress in March along with setting of many other key figures used to provide economic guidance.

The National Bureau of Statistics reports that higher prices of pork boosted consumer price inflation by 2.4 percentage points in October, when wholesale and retail pork prices were up more than 100 % y-o-y. Core inflation, which excludes food and energy prices, has held at 1.5 % since August. Producer prices fell by 1.6 % y-o-y in October.

Given the difficult economic situation, China's decision-makers must reconcile many contradictory pressures when setting monetary policy. The People's Bank of China this month slightly lowered the rate on its one-year medium-term lending facility (MLF) for commercial banks from 3.3 % (the rate set in April 2018) to 3.25 %. In August, the PBoC introduced a new reference rate for the pricing of bank loans based on the MLF rate (BOFIT Weekly 34/2019). Money market rates have remained fairly stable this year.

The stock of bank loans continued to grow at a rate of 12 % y-o-y in October. Growth has remained at around 12–13 % for over three years. The use of financial instruments in China's shadow banking sector, however, has been on the decline for more than a year.

CPI, 3-month treasury bond and AAA corporate bond rates

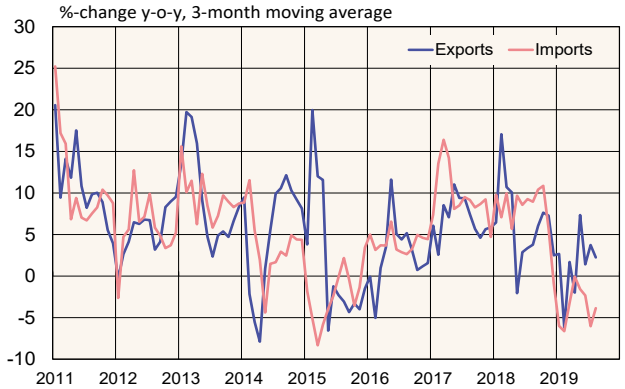


Source: Macrobond.

Chinese imports continued to contract in October. China Customs reports that the value of goods imports measured in dollars contracted by 6 % y-o-y in October. Exports were down by 1 %. In the first ten months of the year, imports were down 5 % y-o-y. Exports remained unchanged, however, so China's foreign trade surplus increased. For the January-October period, the trade surplus amounted to 340 billion dollars, close to the value of the entire 2018 surplus.

While price and exchange-rate shifts explain some import trends, the decline in imports largely reflects lower import volumes. During the first eight months of this year, monthly goods import volumes were off about 3 % y-o-y on average. For example, the import volume of machinery & equipment was down 5 % on average, while vehicles were off by over 10 %. In contrast, the volume of exports increased by a couple per cent. The net impact from foreign trade has been to support real economic growth.

Volume of Chinese goods trade (2011–present)



Sources: China Customs, CEIC and BOFIT.

China and 14 other Asia-Pacific nations prepare to sign RCEP trade pact next year. At a summit in Bangkok, Thailand early this month, the representatives of ten ASEAN countries, plus South Korea, Japan, China, Australia and New Zealand, announced they had reached agreement on the terms of the Regional Comprehensive Economic Partnership (RCEP). The trade agreement will be signed next year if no problems emerge in the review phase.

While details of the agreement have yet to be revealed, it is clear that the agreement is less ambitious than the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) free-trade agreement that partly entered into force at the end of last year. Seven CPTPP countries are also part of the RCEP agreement. Media reports note that the RCEP agreement focuses on goods trade and mainly unifies bilateral tariff arrangements of its members. Customs tariffs will decline in many fields. Some observers note that the agreed unification of rules of origin may be even more important than lower tariffs as it promotes production chains within the region.

Countries acceding to the RCEP trade pact represent almost 30 % of the world's population and global GDP (in nominal dollar terms). The agreement's economic impacts are expected to be relatively modest, however, and further diminished by the long transition periods.

China, which accounts for 62 % of the population in the RCEP area and 54 % of its nominal GDP, strongly supports the trade agreement. India withdrew from the agreement after it failed to gain concessions for its agricultural sector. India also feared that its participation in RCEP would lead to a flood of Chinese products onto its market.

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