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Russia

Russia became a WTO member on Wednesday. WTO accession brings down Russia import duties 3 % on average, a small drop as Russian import duties have traditionally been fairly low by international standards. The weighted average import duty will eventually be about 7 %. Some tariff cuts go immediately into effect and some are subject to transition periods. Most transition periods are 2–5 years, and the longest, for car imports, is 7 years.

Russia's WTO commitments apply to both goods and services. In the insurance sector, Russia will raise the ceiling on foreign capital participation from 25 % to 50 % of the sector's total capital. After a transition period, foreign insurance companies will also be allowed to establish branch offices. Russia, however, will still not allow foreign banks to set up branch offices, and the banking sector will continue to maintain a 50 % limit on foreign ownership.

Russia's WTO membership commitments with respect to the US are still in limbo as the US Congress failed to pass legislation establishing permanent trade relations with Russia before going on its summer recess. As a result, the US still has the Cold War legacy of the 1975 Jackson-Vanik amendment, which bans granting the Soviet Union permanent most-favoured-nation status in foreign trade. The Soviet Union ceased to exist over 20 years ago, but trade between Russia and the US still is governed by the amendment, so a most-favoured-nation exemption for Russia must be granted each year. Such bans violate WTO rules, which has left the US temporarily outside the scope of Russia's WTO agreement. (In fact, under its WTO commitments, Russia's lower tariffs also apply to the US, but they must be implemented under the annual exemption from by the US.)

Russia's WTO membership brings some tariff relief important for Finland. With Russia's WTO membership becoming official on Wednesday (August 22), lower import tariffs on certain paper products took immediate effect. However, the bulk of import tariff reductions for Finland's main export goods only go into effect after several years of transition. Although Russia's import duties on average only decline a few percentage points, some tariffs will be cut as much as to a third from their current level (e.g. certain paper and chemical industry products).

One of the most important impacts for Finland are cuts in export duties on raw timber. To date, Russia's export duty on the bulk of wood types has been 25 % of the export value with a minimum of €15 per cubic metre. With WTO membership, the export duty on raw birch falls to 7 %. Pine and spruce are subject to export quotas, and within those quotas the export duty on spruce will fall to 13 % and pine to 15 %. The EU quotas on pine and spruce amount to double or even triple last year's actual import volumes. Hence quotas and lower import duties are expected to cover all the import requirements of European buyers.

WTO membership means Russia is committed to more predictable and transparent customs procedures. This should improve trade flows as customs procedures have traditionally been mentioned by Finnish firms as one the most problematic aspects of trade with Russia.

Strong protection of Russia's car industry will continue even with WTO membership. Russia's WTO commitments include lowering automobile import tariffs gradually through 2018. At that time, the import duty on passenger cars that are new or new-ish (less than three years old) cannot exceed 15 % of the customs value. The import duty on older cars (over three years old) will be 20 %. The prevailing import duty since 2008 had been 30 % for new cars and 35 % for old cars.

The first reduction in tariffs went into effect immediately upon WTO membership, whereby Russia lowered the import duty on new cars by five percentage points to 25 % and old cars to 30 %.

Lower import duties, however, will not translate into cheaper cars. Under a new law passed in July, the discount will be absorbed by a recycling fee. The law enters into force on September 1, and applies to cars imported into Russia and cars manufactured in Russia. Car importers will have to pay the fee for every imported car, while companies that manufacture cars in Russia will instead commit to making arrangements for the recycling of the cars they produce. For the time being, Russia has no comprehensive recycling system for vehicles nor a law governing the issue, so setting up a functional recycling system will take time. It is also unclear how the system will be funded.

The size of the fee will be decided by the government. According to the proposal submitted by the industry and trade ministry, the size of the fee will be based on the age of the vehicle and volume of engine displacement. The older the car and the larger the engine, the higher the recycling fee. The recycling fee for an old car will be as much as six times higher than that of a new car. Cars manufactured in Russia faced severe competition from imported used cars before the 2008 hike in the import duty on passenger cars. Imports came to a near halt after the tariff hike. The high recycling fee for used cars is meant to keep them out of the Russian market also in the future.

Russia's car industry in the last decade has grown rapidly. Most growth has been generated by assembly plants established by foreign carmakers on Russian soil. Russia has boosted the development of the industry by significant support measures, e.g. imposing high import duties on foreign cars.

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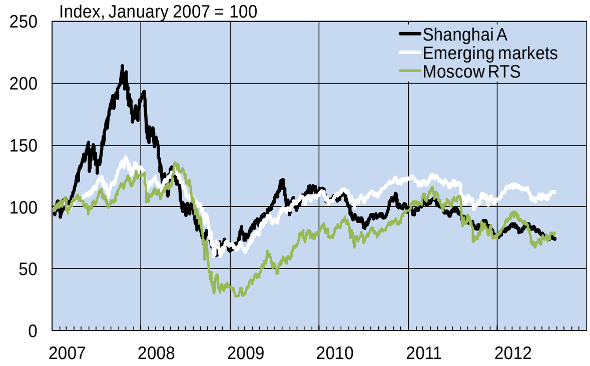
China

Prices on Shanghai stock exchange tumble. This week, the Shanghai stock exchange's A-share index hit its lowest point since autumn 2008. The Shanghai A-share index has dropped about 4 % this year, while stock exchanges in other emerging markets are on average up by about 6 %. The downturn in Chinese share prices has been fuelled by worries over the slowdown in economic growth. Moreover, listed firms have started to release their second quarter results, which have been weaker than in previous years.

Share prices trends for the Shanghai A, Moscow RTS and MSCI Emerging Markets indices



Source: Bloomberg

China to continue active development of North Korean special economic zones. China's Ministry of Commerce reports that China and North Korea are satisfied with the bilateral cooperation taking place in two special economic zones located along the China-North Korea border. Rason, North Korea's first special economic zone was established in 1991, while the second, Hwanggumphyong and Wihwa Islands economic zone, was established in July 2011. The infrastructure and relevant regulations governing the zones will now be developed in order to attract more foreign investment. The immediate goal of developing the zones is accelerating North Korea's economic growth.

China is by far the biggest trade partner of internationally isolated North Korea. Trade between the two nations has grown briskly in recent years. In the first seven months of 2012, for example, Chinese exports to North Korea rose 14 % y-o-y and the value of exports was $2 billion. North Korea imports many of its critical commodities, energy and manufactured products from China. China's imports from North Korea climbed 15 % y-o-y in January-July to $1.5 billion. The bulk of imports consisted of coal and iron ore.

China's role in trade has gained even more significance for North Korea after South Korea tightened trade sanctions on North Korea in 2010. Even so, the Koreas continue to maintain economic ties in North Korea's 65-square-kilometre Kaesong industrial complex just north of the demilitarised zone. Media reports indicate the value of industrial output has increased sharply from last year and an increasing number of North Koreans work for the area's joint ventures.

Famine is a most serious problem in North Korea. In a June UN assessment, about two-thirds of North Koreans were found to suffer from chronic food insecurity. The situation worsened recently after flooding from severe July rains damaged grain crops and critical infrastructure in North Korea.

Active development of the special economic zones may indicate broader economic reforms are being contemplated by North Korea. If the current experiments succeed, observers speculate that they might begin to be applied more widely.

Closer cooperation with China could also contribute to stabilising the situation on the Korean peninsula, a further motive for China to actively develop North Korea's special economic zones beyond straightforward economic purposes.

Japan is one of the most important trade partners for China. Relations between the world's second and third largest economies, China and Japan, have grown tense in recent days after a group of Japanese activists landed on the tiny Senkaku/Diaoyu islands claimed by both Japan and China. The islands lie in a part of the East China Sea with hydrocarbon potential, and the two countries have not been able to resolve their territorial claims or shared utilisation of hydrocarbon reserves.

In recent years, disputes over boundaries have caused a series of spats. For example, in 2010, China banned exports of rare earth metals to Japan after Japan arrested the captain of a Chinese fishing vessel in the disputed area. On top of the demarcation disputes, there is a difficult history between the two countries. In 2005, widespread demonstrations broke out in China against Japan after the Japanese revised school history textbooks on events in the wars between the two countries.

Even so, the countries are inextricably linked economically. Although Chinese imports from Japan fell slight on-year in the first seven months of the year, China still imports more goods from Japan than from any other country. Japan is also China's third largest export market after the US and the EU. The top goods category, both for imports and exports, is machinery and equipment.

China is by far Japan's top trade partner; China accounts for about 20 % of Japan's exports and imports. Japanese firms have also made major investments in China.

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