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BOFIT Weekly

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Russia

The government prepares to extend car recycling fee to Russian-made cars. Economy minister Andrei Belousov reports that a decision on the matter has been reached, and that the cabinet is currently reviewing the necessary legislative changes for extending the recycling fee to all cars in Russia. The change was initially given impetus by president Vladimir Putin, who gave the government one month to come up with a solution to level the playing field for domestic and foreign carmakers after last December's EU-Russia summit. The recycling fee should enter into force in about six months.

The recycling fee was introduced together with reductions in auto import duties after Russia's WTO accession last year. The amount of recycling fees was matched to the reductions in import duties hence providing protection to domestic production from increased foreign competition. Russia's domestic carmakers have largely been protected by high tariffs since 2009, when import duties, especially on used cars, were raised substantially. Before the hikes, used foreign car imports had become the biggest competitors to mid-range cars built in Russia.

The recycling fee has been a point of contention for Russia's trade partners – so much so that the EU, the United States and Japan have brought the matter up in WTO. The recycling fee violates WTO rules because it is not applied to domestic manufacturers who have committed to handle the recycling of their vehicles themselves.

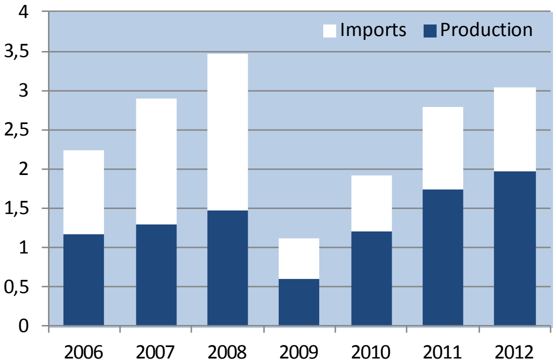
The extension of recycling fees to cars built in Russia has not pleased domestic carmakers or foreign manufacturers operating assembly plants in Russia. Belousov noted that the cabinet is currently considering measures that would offset the costs to Russian carmakers from the recycling fee. The law on foreign investment protects investors from measures that weaken their terms of contract, like recycling fees.

Car imports and car production in Russia hit record highs in 2012. Last year a total of nearly 3 million passenger cars were sold in Russia, narrowly beating out the 2008 record. Car sales last year were up over 10 % from 2011, even if sales growth slowed sharply in the final months of 2012. Russia was Europe's second largest car market last year after Germany. There are over 500 cars per 1,000 inhabitants on Germany, while the figure for Russia is only 240 per 1,000 inhabitants.

Russia would like to raise visibly the profile of its car industry. The output of the auto sector has amounted to only about 0.5 % of GDP past years. Vehicle manufacturing employs about a million people in Russia. The heartland for Russia's car industry is the city of Tolyatti in the Samara region, where an entire city has built up around the Avtovaz plant. Other carmaking complexes are found outside St. Petersburg and in the Kaluga region near Moscow, where most of the assembly plants of foreign carmakers are located.

Russia wants to increase domestic car production and reduce its reliance on foreign car imports. Over two-thirds of cars sold in Russia last year were already built domestically. In the pre-crisis period, domestic production only accounted for about half of sales. Russian car production is focused on economy models, while most expensive cars are imported from abroad. Most domestic production, however, actually consists of assembly of foreign makes. The localization ratio of foreign assembly production is still quite low, largely due to the lack of parts suppliers in the manufacturing chain. A few percentages of Russian car production are exported, mainly to CIS countries.

Russian production and imports of passenger cars (million)



Sources: Rosstat, Russian customs.

OECD takes up Russia's membership application again. Russia first applied for OECD membership in 1996. Processing of the membership application began in earnest in 2007, but discussions were sidetracked during Russia's final push in WTO talks. Now the process is continuing.

The OECD requires its members to commit to market-economy principles. The OECD's 22 special committees examine various aspects of the applicant's compatibility and embrace of the OECD approved principles and give recommendations and input on measures for the applicant to implement. Areas of focus include the applicant country's financial, social and competition policies, as well as its financial markets and consumer protection.

Russian officials claim their country already meets many of the OECD's most important membership criteria such as WTO membership and signing the UN Convention Against Corruption. They expect Russia's membership to take place within the next couple of years.

The OECD noted that Russia still has plenty of work ahead on harmonising its legislation, and in particular in the implementation of laws. During the processing of Russia's OECD application, special attention has been paid to e.g. the state's disproportionate role in the economy, treatment of foreign investors, corruption and environmental policy.

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China

Real estate prices rising again. After a massive stimulus in 2009–2010, officials moved to rein in rising real estate prices by for example raising the percentage of downpayment required to finance a mortgage. Real estate prices dropped until the latter half of 2012, when they began to rebound throughout China. Officials in Beijing seem concerned about the rebound; local officials last week were ordered to curb real estate speculators and impose further restrictions on real estate deals if needed. There is also a proposal to extent the current property tax experiment to more cities. At the moment, there is a pilot property tax programme in Shanghai, where the tax affects owners of more than one apartment. There is also a trial in Chongqing that imposes higher tax rates for luxury apartments.

Housing prices vary tremendously around the country. The average apartment price, measured in square metres of liveable floor space, average 16,500 yuan (€2,000) per m^2 in Beijing and 14,000 yuan (€1,700) per m^2 in Shanghai. In contrast, prices in cities in Western China and most cities in Central China, averaged 3,000–4,000 yuan (€400–500) per m^2. Prices also vary considerably within cities.

The uncertainty about the direction of apartment prices was evident last year with a drop of about 10 % in new housing starts. The housing stock was growing so fast that more apartments were being built than sold. The stock of unsold apartments, measured in floor space, increased about 40 % to 365 million m^2 last year. The bulk of unsold apartments is located in China's smaller cities. Although the National Bureau of Statistics in recent years has tried to improve the quality of its statistical data on the real estate sector, trying to get a handle on what is actually happening in the sector is still difficult.

Energy dominates China-Russia discussions on trade policy. Chinese figures show that China's 2012 exports to Russia increased to just over $44 billion and imports to just under $44 billion (i.e. trade was roughly in balance). Russia's share of China's exports and imports have long remained in the 2 % range.

From Russia's perspective, bilateral trade looks quite different. Russian statistical authorities report that China accounts for 17 % of Russia's imports. The data also show that Russia has been running a sizeable deficit with China in recent years despite the relatively high price of crude oil.

China's exports to Russia consist of a diverse range of manufactured goods. Competition from Chinese car imports is rapidly becoming a huge headache for Russia's car industry. China exported 67,000 cars to Russia last year, which is about 40 % more than in 2011. Russia has accounted for about 14 % of China's car exports in recent years. Passenger cars exports to Russia are still a tiny business for the Chinese; they only account for about 1 % of the value of China's total exports to Russia.

China's imports from Russia are mostly energy or raw materials. The inauguration of Russia-China oil pipeline at the beginning of 2011 meant that over 24 million tons of crude oil flowed to China last year. So, despite difficulties in early commissioning of the pipeline, Russian oil exports to China were up 60 % from 2010. Over the past two years, the share of China's imported oil that came from Russia rose from under 7 % to about 9 %.

Even after years of wrangling, China and Russia have yet to reach agreement on a gas pipeline that would run from Siberian gas fields via Altai to China. Most of the dispute is over pricing. The countries have recently moved on to trying to negotiate liquefied natural gas (LNG) deliveries.

China-India trade stumbled last year. The value of China's imports from India contracted by nearly a fifth to $19 billion last year, while the value of exports to India decreased by 6 % to $48 billion. The weak imports figures are in part due to a weak global market for iron ore, which has caused fall in ore price. Moreover, India's supreme court has imposed a ban on operations at iron ore mines in northern India due to environmental damage. The mining operations have polluted groundwater and have been linked to deforestation. Observers say that India has allowed its environmental problems to get out of hand due to the corruption of local political machines. It was the unwillingness of public officials to oversee mining operations at an earlier stage that allowed conditions to get so bad.

China is India's largest trade partner. India's main exports to China are various raw materials, while India imports from China a vast array of consumer and investment goods.

India, in contrast, represents only a couple of per cent of China's foreign trade. However, growth has been rapid. In the 2000s, growth in the value of trade averaged over 30 % a year. The fluctuations, however, have been large. Trade between the countries collapsed during the recession in 2009, when India imposed tariffs on Chinese goods in reaction to dumping charges.

China-India bilateral trade, % change of value

Source: China Customs

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