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BOFIT Weekly

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Russia

Economic stimulus policy gaining ground in Russia. The stimulus measures planned so far do not appear to have increased the federal budget deficit, which is limited to 0.5 % of GDP this year. However, part of the savings in the National Welfare Fund garnered from fees and taxes on oil and gas production and exports have been designated for investing in domestic projects, which is a clear deviation from earlier policy.

Economy minister Alexei Ulyukayev, known as a proponent of strict monetary policy when he acted as Central Bank of Russia deputy chairman until late June, argued for stimulus at the cabinet meeting on July 25. He noted that the long-term growth outlook for the Russian economy has been eroded by weakness in the global economy and changes in international trade patterns. He added that the episode of record growth of the Russian economy a few years ago was largely driven by a huge increase in export earnings that is unlikely to be repeated. The government this year forecasts GDP growth of 2.4 %.

Ulyukayev justified stimulus measures by noting that Russian economic growth has recently fallen below its potential level. Unemployment has begun to rise, even if, at 5.4 % in June, it is still low by international standards. Moreover, the utilisation of industrial production capacity has begun to decline (again, from relatively high levels). Ulyukayev said that application of fiscal and monetary stimulus measures to boost output would not accelerate inflation under current conditions.

The need to improve business conditions in Russia has been brought up as one of the measures to boost economic growth. At its July 25 meeting, the government approved Ulyukayev's proposal for a programme addressing these issues.

The first goal of the programme is to simplify operations for small and medium-sized enterprises (SMEs), particularly access to finance. For this purpose, the government will create e.g. an organisation to guarantee loans to SMEs. The organisation would be in part funded out of the National Welfare Fund.

To revive capital investment, money from e.g. the National Welfare Fund and the State Pension Fund would be made available for large public projects that are being prepared as part of the stimulus. The programme calls for repayment of the investment and requires that clear criteria will be formed for project selection and effective oversight systems are in place during project implementation.

The CBR would extend credit to banks and thus businesses by allowing loans to SMEs to be used as collateral.

Public procurement by the federal government and municipal governments would in certain cases be limited to contractors within the Russia-Belarus-Kazakhstan economic area.

Russia strives to increase waste recycling. Sergei Donskoi, minister of natural resources and environment, wants to see Russia raise the utilisation and neutralisation level of waste from 11 % to 80 % by 2020. Municipal waste handling and recycling in particular are to be improved, which practically means a need to create a whole new industrial branch. The IFC, a World Bank agency, estimates that Russia presently exploits or recycles only a few per cent of its municipal waste. The EU average is about 60 %.

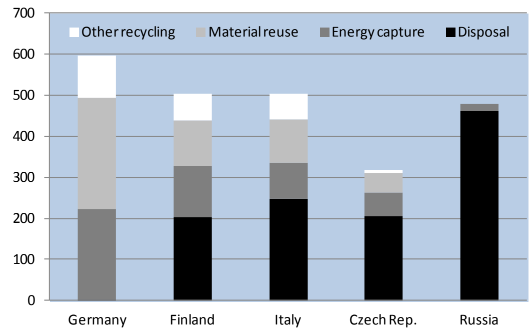
Massive investment is required to make significant improvements waste handling and recycling in Russia. The IFC estimates that reaching a municipal waste recovery rate of 40–45 % by 2025, calls for investing €40 billion.

Despite tremendous potential, it may be hard for Russia to attract investment to the waste management business, due, according to operators in the field, to inadequate regulation and legislation. For example, a law on recycling fees has been under preparation for three years. With the current schedule, the law should be finalised by next spring. The bill requires manufacturers of products made of e.g. glass, plastic and certain metals to assume recycling responsibility for their products. Manufacturers would have the option of recycling their products themselves or paying a recycling fee to the state to cover recycling costs. The recycling fees are estimated to come into force in 2016 at the earliest.

State-owned conglomerate Rostech has already shown interest in getting into the waste management business. CEO Sergei Chemezov says his company wants to be one of Europe's biggest waste handling and recycling companies. Rostech puts the current value of Russia's waste market at 50 billion rubles (€12 billion) a year and has already begun to acquire domestic waste handling facilities.

Russian consumers show a gradual increase in their interest in recycling. Research company VTsIOM reports that the majority of Russians see sorting of their trash and use of recyclable materials in consumer products as important or very important. On the other hand, only a third of respondents said they were ready to spend their own money on environmental protection or to pay environmental taxes.

Municipal waste handling in five countries in 2011, kg/person



Sources: Eurostat, OECD, IFC

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China

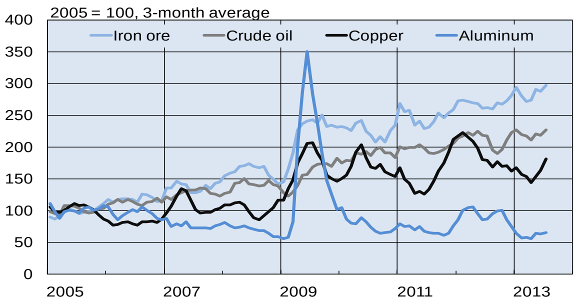
Chinese exports and imports picked up in July. After a lacklustre May and June, China's goods exports measured by value grew 5 % y-o-y in July. After showing weakness during spring and early summer, exports to Europe and the United States showed signs of strengthening in July, suggesting balancing within the global economy. Thanks to a strong first half, the value of China's total imports in the first seven months of the year was up about 10 % from the same period a year earlier.

After showing virtually no growth in May and June, China's imports in value terms were up 11 % y-o-y in July. US imports experienced robust growth for the second month in a row and imports from the EU showed signs of improvement. China's increased commodity imports may also signal improving conditions in the Chinese economy following fairly tepid growth in the first half of this year. The value of China's total imports increased 7 % y-o-y in the January-July period.

Japan-China trade continued to dwindle, both in terms of China's exports to Japan and imports from Japan. The deterioration of bilateral political relations is taking a long-term toll on both economies.

Growth of China's trade surplus slowed in July to $18 billion for the month. The trade surplus for January-July amounted to $127 billion, over $30 billion more than in the same period in 2012. Price trends partly accounted for the increase in the trade surplus. Chinese statistics show import prices fell over 2 % in the first half, while export prices were unchanged from the first half of 2012.

Volumes of select Chinese commodity imports, 2005–2013



Sources: Macrobond, BOFIT

China's health care sector dogged by problems even as state spending on public health care continues to rise. The Ministry of Finance's budget estimate shows China spent 380 billion yuan on public health care in the first half of the year, an increase of 22 % from 1H2012. Health care services now account for over 6 % of public sector spending, but the figure is still quite low by international standards.

OECD figures (OECD Health Data) released this summer show total health care spending (public and private) in China amounted to about 5 % of GDP in 2011. In comparison, health care spending as a share of GDP is about one percentage point higher in both Russia and Mexico. The average share of health spending to GPD in the OECD's 34 member states, most of which have long-established market economies, is around 9 %. Per capita spending in absolute terms varies much more widely, however. Per capita health care spending in 2011 was around €300 in China, €1,000 in Russia and €2,500 in Finland. The ratio of doctors and nurses to the general population in China is also far below the OECD average.

The prices for health care services in China have long been rising faster than wages. The *South China Morning Post* reports China's leadership is attempting to respond to the situation this year by cutting the cost of medical bills. At the moment, many Chinese have to turn to private providers for health care services, which means that about 44 % of health care spending in China is shouldered by private individuals (OECD average 28 %). Publicly funded health care has been on the rise in recent years as services covered under national health insurance have been expanded. Moreover, planned reforms to China's *hukou* household registration system would extend health care access to migrant populations currently outside the system (see [BOFIT Weekly 27/2013]).

China's extensive use of coal and its long-term impacts on health constitute a huge burden on the Chinese health care system. A study released in June found that the policy of providing free coal for home heating from the 1950s to the 1980s in Northern China decreased the average lifespan of residents by about 5.5 years relative to their neighbours in surrounding regions where free coal was not distributed. The OECD says the average Chinese lifespan has been rising steadily since the 1960s and currently stands at about 73 years (OECD average 80 years). A number of studies suggest that air pollution is a big factor restraining further lifespan gains. The *China Daily* reports that China plans to spend nearly €380 billion in coming years to prevent further contamination of air and water, as well as take measures to correct environmental damage that has already occurred.

China's health care system is plagued by corruption. One of the biggest reasons contributing to this problem is that most hospitals lack an adequate financial base. Hospitals also engage in side businesses such as pharmacies, which, in turn, may motivate doctors to over-prescribe medicines. Media reports also indicate it is common practice for patients to offer money to doctors to assure they get adequate quality treatment. The pervasive corruption in the pharmaceutical industry was highlighted in late June when China started investigating UK-based GlaxoSmithKline for bribing hospital administrators and doctors to raise retail prices on certain medicines and boost sales.

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