BOFIT Weekly
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Russia

Russia's current account surplus persists, capital outflow diminishes. Preliminary balance-of-payments figures show that Russia's current account surplus amounted to nearly $20 billion in the second quarter of this year. Over the past four quarters, the surplus corresponded to about 4 % of GDP.

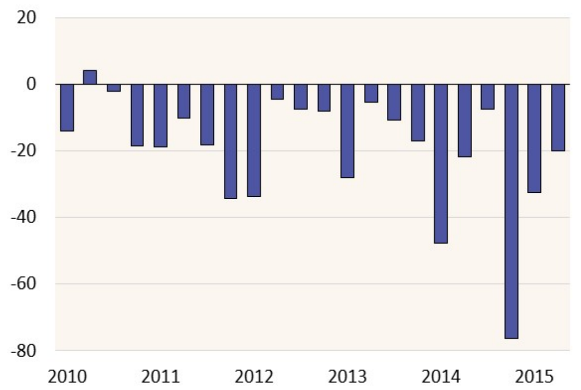
In the second quarter, the value of goods and services exports shrank nearly 30 % y-o-y in dollar terms, while imports were down 40 % in dollar terms (20 % in euros). Foreign trade also contracted nearly as much in the first half as a whole. For the January-June period, the value of exports was $210 billion and the value of imports $140 billion.

Capital outflows from Russia continued in the second quarter, but were slower than earlier. The private sector's net capital outflows amounted to about $20 billion.

Banks continued to pay down their foreign debt faster than they acquired new foreign debt, but not quite as fast as in the first months of 2015. Moreover, banks invested more of their assets abroad than they repatriated.

In contrast, the foreign debt held by other firms increased in the second quarter for the first time in nearly a year. Most of the new debt is from direct investors. Non-banks, however, still invested more abroad than repatriated their assets.

Quarterly net capital flow of Russia's private sector (USD billion)



Source: Central Bank of Russia

Russia's foreign debt remains unchanged. The Central Bank of Russia estimates that Russia's foreign debt stood at nearly $560 billion (30 % of GDP) as of end-June. Russia's second-quarter foreign debt remained practically unchanged from the first quarter as banks paid down their foreign debt while other firms acquired more of it.

However, the value of foreign debt has contracted sharply compared to a year ago. As of end-June 2014, Russia's foreign debt was still $730 billion. While a substantial amount of debt has actually been repaid, part of the decline reflects exchange rate fluctuations. About a fifth of Russian foreign debt is denominated in rubles.

Russia's public-sector foreign debt amounted to $35 billion at the end of June. Banks' foreign debt stood at $150 billion and that of other firms at $360 billion. State-controlled firms accounted for more than 60 % of banks' foreign debt and for about 40 % of other firms' foreign debt.

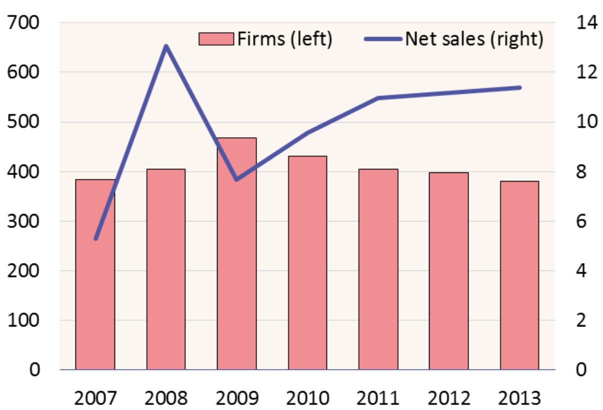
The CBR estimates debt servicing obligations coming due in the second half of this year will total nearly $80 billion.

Several hundred firms in Finnish ownership in Russia. The latest figures from Statistics Finland show 380 subsidiaries of Finnish firms operating in Russia in 2013. The net sales of Finnish subsidiaries operating in Russia at that time amounted to €11.3 billion and provided employment for over 46,000 people. Finland's exports of goods and services to Russia amounted to €7.5 billion in 2013.

Rosstat reports there were 460 Finnish-owned firms in Russia in 2013. Rosstat figures also include firms, where Finns hold a minority stake. Some 60 % of Finnish-owned firms are sited in Northwest Russia, mostly in St. Petersburg, in the Leningrad region or in the Karelian Republic. About a quarter are based in and around Moscow.

Finnish-owned firms accounted for about 2 % of foreign firms operating in Russia. A substantial portion of foreign firms in Russia are, however, Cypriot-owned, and it is estimated that the ultimate owners in most of such cases are in fact Russian. The region where Finns accounted for the largest share of foreign-owned firms is the Karelian Republic. Well over a third of foreign firms there have Finnish owners.

Number and combined net sales (EUR billion) of Finnish-owned subsidiaries in Russia



Source: Statistics Finland

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China

China's Q2 economic growth remained at 7 %. China's National Bureau of Statistics reports second-quarter GDP growth of 7.0 % p.a. First quarter GDP growth was also 7.0 %. On-quarter growth in the second quarter was 1.7 %.

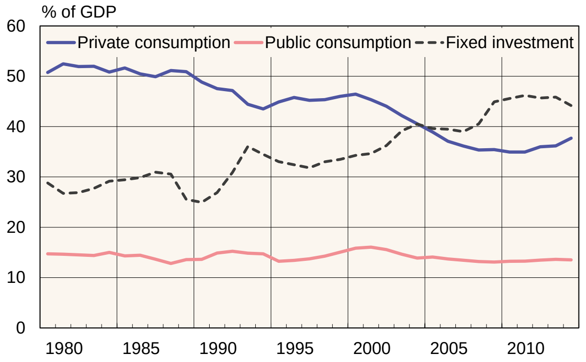
Industrial output growth in the first half lagged GDP growth. In June, however, industrial output perked up to 7 % y-o-y. On-year growth in fixed asset investment slowed in the first half to 11 %. Growth in housing investment, in particular, slowed in the first half to 5 %, down from 14 % in 1H14. Real estate sales, however, rebounded in the first half after falling for nearly one-and-a-half years.

Private consumption increasingly is the main engine of growth in China. Real disposable incomes rose about 8 % in the first half, while retail sales growth in June remained above 10 %. Consumer price inflation accelerated slightly in June to 1.4 % y-o-y. Producer prices fell 4.8 % y-o-y.

Structure of Chinese economy keeps evolving. Demand-side factors in the just-released 2014 GDP figures show that private and public consumption corresponded to over half of China's GDP for the first time since 2006. Private consumption's share of GDP has again begun to rise after several years of stagnation, while the relative importance of fixed capital investment continues to decline. Even so, Chinese fixed capital investment equalled over 40 % of GDP, which is remarkably high by global standards.

As economic emphases change, China is moving gradually from an export- and investment-driven growth model to growth based on the service sector and domestic consumption. In 2013, the service sector generated for the first time a larger share of GDP than manufacturing. In the first half of 2015, the service sector accounted for half of GDP.

Structure of Chinese GDP



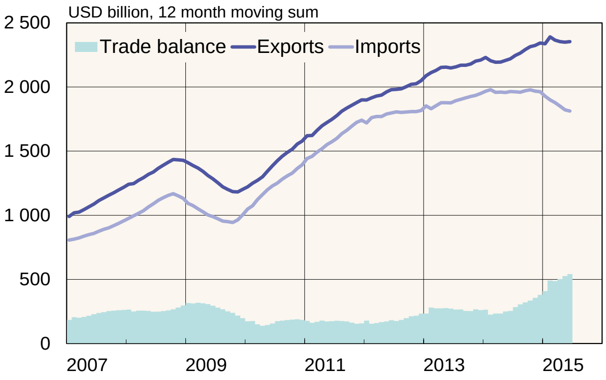
Sources: CEIC, Macrobond

The World Bank latest China Economic Update finds China has made progress in its attempts at economic reform. As growth slows in China, the assessment noted that reforms of the financial sector will require special focus, so that financing will be channelled to sectors that are capable of sustaining growth over the longer term. The World Bank continues to hold the view of continued modest slowing of Chinese economic growth.

Slow export growth in China in the first half; value of imports declines. In the first six months of 2015, the value of exports increased about 1 % from 1H14. The value of imports declined 16 %. Exports to the US rose 9 %, while exports to EU countries declined 3 % and to Japan 11 %. China's 1H trade surplus was $263 billion, up over 150 % y-o-y. The trade surplus boost reflects lower import prices.

Foreign trade picked up in June. Exports were up 3 % y-o-y, while the slide in imports was only 6 %. June crude oil imports reached nearly 30 million metric tons, up 27 % y-o-y. Stocking of the country's strategic reserves partly explains the surge in oil imports. Imported oil volumes were up 8 % y-o-y in the first half. The import price of oil in the first half of the year averaged about 30 % less than in 2014.

Value of China's foreign trade



Source: Bloomberg

China introduces draft legislation on foreign investment and cyber-security. The proposed laws e.g. would give officials the possibility to shut down online connections in some situations and require foreign firms to store their data collected in China on servers physically located in China. In addition, foreign investments would need official approval in cases where such investment could be seen as a threat to national security. The draft laws presented last week are now out for comment. The drafts are part of a larger, recently approved, legislative package on national security.

Problems arising from the tighter regulation worry foreign firms operating in China. Already tight Internet surveillance affects e.g. corporate research efforts. Many firms see the new laws as an effort to bolster the competitiveness of Chinese firms. The EU, for example, has voiced strong concerns over the impacts of the new legislation on the operations and investment climate for foreign firms, and offered comments and amendments to Chinese officials.

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