SUOMEN PANKKI FINLANDS BANK EUROSYSTEM 18 11

Weekly Review
50 • 13.12.2019

BOFIT

Russia

OPEC and Russia agree on further cuts in oil production. Over the past three years, Russia has worked closely with OPEC members in a number of voluntary agreements to restrain crude oil production and stabilise prices. Partly as a result of the increased cooperation between Russia and Saudi Arabia, oil-producing countries in recent years have managed, at least to some extent, to hold to the agreed production ceilings in order to support oil prices. The combined crude oil production of Russia and OPEC represents roughly half of global oil output.

At the beginning of 2017, OPEC members, Russia and several other non-OPEC producer countries (a group sometimes referred to as "OPEC+") agreed to voluntarily reduce their combined output by about 1.7 million barrels a day. Under the deal, Russia was obliged to cut its daily production by 0.3 million barrels. The agreement was later extended several times through June 2018. Russian oil production rose to a record-high level in autumn 2018, but the countries met again and agreed to reinstate roughly 1.2 million barrels in cuts from the start of 2019.

At last week's (Dec. 6) OPEC and Non-OPEC Ministerial Meeting, the parties agreed to new production cuts until the end of March 2020. Overall, the parties agreed to cut production by roughly 1.7 million barrels in 1Q2020. In addition, Saudi Arabia committed unilaterally to reduce its own production by about 0.4 million barrels a day. As in its previous agreements, Russia committed to cuts of about 0.3 million barrels a day. The required cuts are, however, smaller than earlier, as gas condensate production will no longer be included in Russia's production quota. Energy minister Alexander Novak noted that under the new calculation method, which excludes gas condensates, Russia would have more than exceeded its reduction targets in November 2019, even if it only achieved 85 % of its agreed cuts under the old system.

While Russian officials wish for public spending to spur economic growth, experts remain sceptical. Many Russian officials hope that the elixir to cure Russia's malaise of low economic growth would be found from the national projects and spending money from the National Welfare Fund. Most economic experts, however, point out that the impacts of these public-sector measures are likely to be limited and transitory. Economic growth driven by public spending could even come at a fairly high cost as one ruble of public spending does not even come close to producing corresponding increase in GDP.

The national projects announced by president Vladimir Putin last year call for a total of roughly 18 trillion rubles (260 billion euros) in budget funding during 2019–2024. This year's budget allocates 1.8 trillion rubles for national projects. Government officials have been criticised for moving too slowly in applying allocated funds. At the start of November, only 70 % of this year's funds had been disbursed. Deputy prime minister Konstantin Chuychenko said slow spending was preferred to avoid misuse of funds.

Use of assets from the National Welfare Fund to support the economy has also been discussed, because the Fund has grown substantially in recent years. Under the fiscal rule, the government can access the Fund to support the economy when its liquid part exceeds 7 % of GDP. A pending bill allows spending up to 1 trillion rubles during 2020–2022 on investments in domestic infrastructure and provision of export credit. Funding requests have already been submitted by e.g. Russia's postal service and state railways RZD, as well as fertilizer giant Uralkali for construction of a plant in Angola.

International and Russian domestic research institutions estimate that national projects could accelerate Russian economic growth by 0.1–0.3 percentage points a year in 2020 and 2021. Even with the national projects, total expenditures of Russia's public sector will grow slowly in real terms in the coming years. Spending from the National Welfare Fund would increase public spending. Moscow's Higher School of Economics (HSE) estimates that spending of 300 billion rubles from the Fund next year could speed up economic growth by 0.2–0.3 percentage points depending on the use.

Russia and China rise in World Bank rankings; unchanged in WEF rankings. Both annual comparisons were released in October. The World Bank's survey of 190 economies in *Doing Business 2020* shows Russia rising from 31st place last year to 28th this year, while China climbs from 46th to 31st in the rankings. Among the 141 economies covered in the World Economic Forum's (WEF) *Global Competitiveness 2019*, no changes in the rankings are reported for Russia, which remains at the 43rd spot, while China holds at 28th.

The World Bank's business-friendliness assessment looks at factors such as official practices, regulation and judicial system. Indicators are illustrated through case examples. For instance, "trading across borders" is evaluated in terms of the ease of importing auto parts, while "dealing with construction permits" considers the time, cost and ease of building a warehouse. The assessments concern each country's largest or two largest cities. The World Bank claims that this practice makes its comparison studies feasible. On the other hand, the cases do not provide a comprehensive assessment of the business environment. The comparison also ignores e.g. corruption. Countries can improve their score by making small, targeted reforms. The report notes Russia's reform of its tax-payment system. China wins praise for easing registration and permitting burdens, as well as simplifying tax payments.

The WEF competitiveness study considers such factors as institutions, infrastructure and market functionality. Larger economies benefit from the fact that size of the economy is weighted in the index. Russia failed to make it into the top 90 economies in such categories as security, independence of the judiciary, corruption, press freedom, property rights, openness to foreign trade and financial market stability. China performed poorly in such sub-categories as social capital, press freedom, adult internet use and financial system stability.

Bank of Finland • Institute for Economies in Transition, BOFIT
P.O. Box 160, FI-00101 Helsinki
Phone: +358 9 183 2268 • Web: www.bofit.fi/en

Editor-in-Chief Jouko Rautava• Email: Jouko.Rautava@bof.fi
The information is compiled and edited from a variety of sources. The Bank of Finland assumes no responsibility for the completeness or accuracy of the information, and opinions expressed do not necessarily reflect the views of the Bank of Finland.

Weekly Review
50 • 13.12.2019
BOFIT

China

China's foreign trade remains weak. The dollar value of China's goods exports in the first eleven months of this year was unchanged from the same period last year (but down 1 % y-o-y for November). The value of imports fell in January-November by 5 % y-o-y, but there was no change in November from a year earlier. The trade surplus for the first eleven months of this year rose to nearly 380 billion dollars, up by over 80 billion dollars from a year earlier.

Demand in China's main export markets have weakened over the past year. Exports to the EU and South Korea were still growing in the first half of this year, but in the past three months they have gone flat and the decline in exports to the US and Japan has become steeper. In contrast, exports to the ten-country ASEAN market have grown rapidly. In November, the value of Chinese exports to the ASEAN region were as large as exports to the EU or the US. Strong export growth to countries such as Vietnam are believed to be partly related to the trade war and companies' efforts to circumvent US punitive tariffs. Export weakness affects a broad swath of China's main export products.

While growth in China's imports from the EU in the past three months remained slightly in negative territory, the decline in imports from Japan and the United States slowed. Chinese goods imports from South Korea in September-November were down 18 % y-o-y. Imports from ASEAN countries, which have reached a level on par with China's imports from the EU, were up 5 %. The import volumes for many commodities have increased since summer, which might indicate stimulus-driven revival in Chinese domestic construction.

Trends in Chinese goods exports and imports

Sources: China Customs and Macrobond.

Companies in China find it increasingly difficult to service their debts. This year over 50 Chinese firms have defaulted on their bonds, while last year just over 40 firms defaulted. The amount defaulted has also increased from last year, reaching 120 billion yuan (15 billion euros) as of end-November. Given the size of the Chinese market, the amounts are still relatively small. Most defaults on the bond market concern private firms, but some state-owned enterprises have also defaulted.

Companies involved in public administration are generally seen as safe investments in China as investors believe the government will step in as payer of last resort to cover their debts. It is therefore notable that this month public administration related firms have had difficulties to service their bonds. Specifically, Inner Mongolia's Hohhot Economic & Technological Development Zone Investment Development Group, a local government financial vehicle (LGFV), defaulted on a 1-billion-yuan (140-million-euro) 5-year privately placed note. While the LGFV managed to pay off part of its debts a few days later and declared that the balance would be paid early next year, the default was only the second ever in recent history. In the other instance, a company largely owned by Peking University went into default this month when it failed to make payment on its 2-billion-yuan (250-million-euro) bond.

While a rise in payment defaults can indicate weakening economic conditions, such defaults are also a natural part of financial system development as they force lenders to consider carefully their actual risk exposure.

Chinese teens romp in 2018 PISA scores. Participating students in Shanghai, Beijing, Jiangsu and Zhejiang snagged top scores in all three of PISA's major categories (reading, mathematics and natural sciences). The Chinese students posted particularly high scores in mathematics and natural sciences. Only 2 % of the students scored poorly in math, the smallest percentage of any PISA participant country.

Notably, China does not PISA-test at the national level. Instead, the OECD uses an abbreviation for the major cities involved in the study with the moniker S-P-J-Z (China). While the population covered in the S-P-J-Z cities totals 180 million, it is unclear how well the performance in these relatively wealthy areas are applicable to the country as a whole. The quality of teaching varies considerably within China. In assessing the effectiveness of school systems, PISA researchers also determine time spent on school work. Chinese students spent about 57 hours a week studying, which was the second highest number of hours for any country. Finnish students, in contrast, spent about 37 hours a week studying, the lowest amount of time for any of the countries surveyed.

Students in Hong Kong and Macao also posted strong scores. Student scores have traditionally been excellent in developed Asian countries such as Singapore, Japan and South Korea. Estonia and Finland were Europe's top-scoring countries. Russian students posted scores slightly below the OECD average in all three categories.

Every three years, the OECD conducts its internationally coordinated PISA testing of 15–16-year-olds. Not all of the 80 survey participant countries are OECD members, and not all students in the age cohort are tested. Instead a sample of schools is chosen. Schools can opt out of the sample and not all students in participating schools necessarily take part in the test.

Bank of Finland • Institute for Economies in Transition, BOFIT
P.O. Box 160, FI-00101 Helsinki
Phone: +358 9 183 2268 • Web: www.bofit.fi/en

Editor-in-Chief Jouko Rautava• Email: Jouko.Rautava@bof.fi
The information is compiled and edited from a variety of sources. The Bank of Finland assumes no responsibility for the completeness or accuracy of the information, and opinions expressed do not necessarily reflect the views of the Bank of Finland.