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Russia

CBR reorganises banking supervision to improve effectiveness. The Central Bank of Russia's Banking Regulation and Supervision Department, which is responsible for drafting bank regulations and bank inspections, is divided into two separate departments; one for regulation and the other for inspection and supervision. Russian banking regulation is planned to be brought closer to international practice which should lead to relaxation of regulations in some cases. For example, the risk ratings for certain types of bank loans are currently stricter than in other countries, weakening the competitiveness of Russian banks.

Banking supervision will be strengthened and it will focus especially on Russia's larger banks in response to banking abuses that came to light over the past two years. Supervision of big banks will be centralized to CBR headquarters in Moscow. Previously, banks have been supervised by the CBR's regional offices. Some observers note the concentration of supervisory functions could reduce the impact of often close relations of regional offices and banks on supervision.

In the wake of the federal government's nearly 300 billion ruble (€7.5 billion) bailout of Bank Moskvy last year, the CBR has increased supervision of banks partly owned by local governments, placing particular scrutiny on bank lending to owners. The problems of Bank Moskvy, which was partly owned by the City of Moscow, came to light after a shakeup in Moscow city leadership in late 2010.

The CBR has also decided to ease rules for foreign-owned banks seeking to establish Russian branch offices. Foreign banks currently need CBR permission to establish a branch. After the change, it will be sufficient for a foreign bank to declare its plans to the CBR. The change conforms to Russia's WTO commitments on giving equal treatment to foreign entities and domestic enterprises (with certain exceptions). Foreign-owned banks have opened only a few branches in Russia in recent years.

Financial sector's tight liquidity situation persists. In the first half of 2011, Russia's financial sector enjoyed a good liquidity situation. Since autumn, however, liquidity has tightened and according to CBR renewed loosening is not in sight.

Part of the reason for the situation has been a gradual shift in Russian foreign exchange policy that has been underway since the 2009 financial crisis. The CBR is today more willing to let supply and demand establish the ruble's exchange rate, and no longer intervenes as extensively to curb ruble appreciation. Hence the excess ruble liquidity in domestic market has diminished. A second factor is the underdevelopment of Russia's financial sector which leads to Russian banks being relatively more dependent on foreign borrowing in their funding. Tighter credit on international financial markets has reduced the supply of funding flowing to emerging markets like Russia, which in turn has made access to borrowing on international markets harder for Russian banks.

Banks have recently sharply boosted their deposit rates in order to compete for deposit funding. The big state banks VTB and Sberbank started to offer higher interest rates last autumn and they were followed by mid-sized banks offering even better deals. The CBR is concerned about rate increases and considers deposit interests exceeding 10 % p.a. too high.

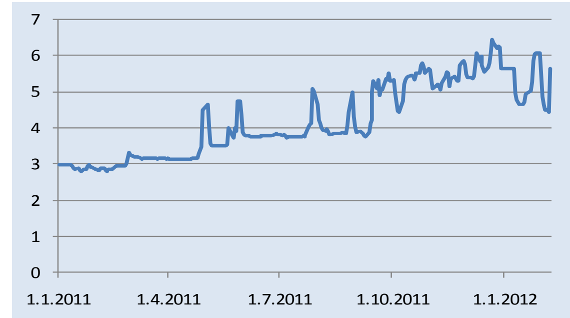
The CBR is also worried about last year's exceptionally rapid growth in borrowing by households. The CBR has warned banks against excessive lending and the current aggressive marketing approaches used by some banks to push credit. The CBR emphasised that banks have social responsibilities and are obliged to determine the real ability of borrowers to repay loans.

Last week's CBR board meeting finds no reasons to adjust rates. The February 3 decision is based on risk assessment of inflation pressures and slowing economic growth, as well as the development of international economic conditions.

Consumer prices were up just 4.1 % y-o-y in January. The CBR expects price growth to accelerate during this year, bringing the inflation rate up to the range of 5–6 % by year's end. At the end of 2011, inflation was 6.1 %. Inflation was exceptionally low for January as this year's scheduled hikes in regulated rates of municipal services were postponed until summer. Typically, rates for municipal services are raised at the start of the year and have a substantial impact on the inflation rate.

The CBR's one-day repo credit rate remains at 6.25 % and the one-day deposit rate at 4 %. The CBR said that the liquidity situation of the financial sector is not alarmingly tight, and gave assurances that it would continue to conduct market operations and provide commercial banks with adequate access to funds. While interbank rates fluctuated sharply in January, they remain relatively high.

One-day MosPrime rate, %



Source: CBR

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China

Productivity gains key to Chinese economic growth. The American research institution, The Conference Board, in January published its annual brief on productivity trends across countries. This year's report finds that growth in labour productivity slowed globally last year, with the global average in output per worker employed up just 2.5 %. Employment growth was up a mere 1.4 % in 2011, so productivity growth accounted for nearly two-thirds of the global GDP growth of 3.9 % in 2011. Regional differences, however, were huge. Employment growth was the main driver of productivity gains in Africa, the Middle East and Latin America, while the lion's share of GDP growth elsewhere mainly came from productivity gains.

China, which posted the highest productivity growth of any major country, 8.8 % last year, nevertheless saw a slowdown of over one percentage point from 2010. The Conference Board this year expects China's productivity growth to slow to 7.6 %. Even if China's employment growth is a mere 0.3 %, the Conference Board expects China's GDP growth to reach about 8 % this year. In India, where the growth in the size of the labour force increased over 2 % last year, most of last year's approximately 7.5 % GDP growth came from productivity gains.

The breakdown in the main sources of Chinese growth show that the growth driven by labour productivity has been founded on massive investment in traditional production. According to Conference Board estimates, about six percentage points of China's 10 % GDP growth in 2010 came from increased capital investment, under one percentage point from IT investment, and about two percentage points from the increase labour force growth and improvements in quality. The remaining three percentage points came from increased total factor productivity, which measures how effectively inputs such as labour and machinery are utilised. Good overall productivity is seen as the result of economic structural reforms and an ability to innovate. The Conference Board offered sobering evidence that total factor productivity in the Euro Area has been close to zero for most of the past decade.

Although productivity growth is soaring in Asia, several countries still lag far behind the global productivity leaders. If productivity is measured in terms of a purchasing power parity adjusted GDP per worker, and the United States is assigned a value of 100, China's productivity level is just 16 at the moment. A decade ago, the productivity of a Chinese worker was only 7 % of an American worker's productivity. Labour productivity in India is still below 9 % of the US level. On the other hand, labour productivity is 79 % of US productivity in Taiwan and 89 % in Hong Kong. Both countries currently match productivity of the best performers in Western Europe.

The low overall productivity of China stems from its labour-intense, low-tech agricultural sector. Farming employs a huge share of the labour force, yet agriculture on makes a small contribution to GDP. China also is plagued with problems in collecting and reporting output and labour statistics. Any productivity comparisons should only be taken as rough indicators. In advanced countries, estimates of labour productivity are generally based on hours worked per unit of output. In other countries, statisticians have to use a rougher output-per-worker measure.

China grants licence to first foreign credit card issuer. Citibank announced this week that Chinese officials have given the green light to its credit card project. Progress in rolling out credit cards has been closely followed internationally as the WTO is currently considering a complaint filed by the US on China's restrictions on foreign credit cards. The US complaint concerns a demand by Chinese officials whereby credit card issuers have to execute payments through the China UnionPay Co. (UniPay). According to media reports, transactions on Citibank credit cards would also have to go through UniPay.

Over two billion bank cards had been issued in China as of last September. Most of those cards are debit cards; just over 200 million were credit cards. The number of issued credit cards grew about 20 % last year.

Taiwan's China-friendly president keeps his job. Taiwan's presidential elections held in mid-January were won by incumbent Ma Ying-jeou, who leads the pro-normalisation Kuomintang Party. The president's margin of victory was clearly smaller than in the previous election, suggesting the pro-China approach is losing favour in the island nation. Despite lower support, Ma announced that he remained committed to promoting economic cooperation with the mainland. Both China and the United States said they were satisfied with the election outcome. Since Ma took office in early 2008, relations between mainland China and Taiwan have warmed substantially. Changes in recent years include an easing of direct flights and ferry trips to and from the mainland, the reduction or elimination of certain duties and increased investment opportunities.

Taiwan's economy grew 4 % last year. The country's strongly export-driven growth, however, began to slow towards the end of the year as the global economic conditions deteriorated. The value of Taiwan's exports fell three months in a row after October. However, Mainland China's strong growth gives Taiwan a cushion against weakness in the rest of the global economy, and Taiwan's growth is expected to remain this year slightly lower than last year. Nearly 30 % of Taiwan's exports go to mainland China.

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