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Russia

CBR hikes key rates as inflation accelerates. The CBR board raised all rates 25 basis points as of 14 September. After the hike, the rate of the CBR's key policy instrument, the one-day minimum repo auction rate, stood at 5.5 %. The minimum repo auction deposit rate is now 5 %.

The CBR said accelerating inflation motivated its decision to raise rates. On-year inflation accelerated to 5.9 % at the end of August and reached 6.3 % in the first weeks of September after hikes in regulated rates for municipal services were implemented at the start of the month. The inflation rate now exceeds the central bank's 6 % target for this year. The CBR noted that higher food prices and poor harvests have added to inflation pressures in the near term.

The CBR said its decision also reflects its view that the economy is growing at a rate near its potential level. According to the bank's assessment, domestic demand will remain stable due to the good employment situation and the rapid expansion of credit.

Preliminary Rosstat figures show GDP growth in the second quarter of 2012 was up 4 % y-o-y. GDP grew 4.9 % in the first quarter, and 4.5 % in the first half.

CBR sells some of its shares in Sberbank. Russia's central bank announced on Monday (Sept. 17) that it was selling 1.71 billion shares, or a 7.6 % stake, in the Russian savings bank Sberbank. After the sale, the CBR retains its majority (50 % + one share) stake in Sberbank.

The shares were sold on the Moscow and the London stock exchanges. On Wednesday, the CBR reported that the final price for Sberbank shares was 93 rubles (€2.30) a share, exceeding the minimum offer price of 91 rubles a share announced on Monday. The final price was about 1 % below the closing price of trading on the Moscow stock exchange on Wednesday. The CBR raised 159 billion rubles (just under €4 billion) from the offering.

Reduction of the CBR's Sberbank holdings has been discussed for years and considered critical by international financial institutions and others for Russia's integration with the global financial system. Sale of a tranche of Sberbank shares was included in the government's 2011–2013 privatisation plans. The divestment, initially scheduled a year ago, was postponed due to the weak market conditions. The sale of shares was carried out now as share prices on stock exchanges around the world have recovered, in part due to wide use of stimulus policies.

Measured by market capitalisation, Sberbank is Russia's largest bank and Europe's third largest bank. Sberbank controls a 46 % share of Russia's deposit market and has Russia's largest nationwide network of branch offices (19,000). In recent years, Sberbank has modernised its operations and actively expanded operations internationally. Sberbank acquired the Austrian Volksbank International in February and the Turkish Denizbank in June.

President Putin signs decree to protect Gazprom. On September 11, president Vladimir Putin signed a decree to defend the Russian Federation's interests in Russian "strategic" firms operating abroad. Under the decree, strategic firms may only comply with rules imposed by foreign national or multinational organisations (including regulators) after getting permission from the Russian government.

The decree applies when a foreign organisation 1) seeks disclosure of information other than information required by Russian legislation (excluding information required of companies planning to issue shares abroad), 2) demands changes in the trade practices or pricing that has been agreed under contract between the Russian firm and its foreign partner, or 3) requires the Russian firm to surrender its license to engage in business operations abroad, divest its holding in a foreign firm or sell property. The government may deny permission if compliance with the requirements could harm Russia's economic interests.

The decree is intended to protect Gazprom after the European Commission launched an investigation at the start of September into possible antitrust violations in the EU by Gazprom. The European Commission wants to determine whether Gazprom has interfered with the function of Europe's natural gas market by preventing gas buyers from selling excess gas in third countries and limiting competition e.g. by forcing buyers into long-term supply contracts and requiring minimum annual purchases. The contract terms have led to wide disparities in prices paid for Gazprom gas in EU member countries. The Commission will also look into Gazprom's pricing scheme that ties the gas price to the oil price. This practice has kept supply contract prices well above prices on spot markets. The problems are worst in the EU's newest member states in Eastern and Central Europe. The new EU members have less bargaining power with Gazprom than the largest EU members.

The presidential decree directly affects investigations launched by the Commission regarding the disclosure of information to investigators looking into Gazprom operations, as well as any demands for corrective measures.

The presidential decree covers Gazprom and all other state-owned enterprises designated as strategic. Putin approved a list of strategic companies in 2004. The list includes, among others, two internationally active oil companies (Rosneft and Zarubeshneft), as well as national pipeline grid operator Transneft and Russian Railways.

Some observers say the presidential decree conflicts with Russia's civil code and numerous international treaties and agreements signed by Russia.

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China

China-Japan island dispute a remainder of region's political risks. The dispute over Diaoyu (in Chinese) or Senkaku (in Japanese) Islands in the East China Sea, a subject to territorial claims of both Japan and China, once again sparked protests this week. The trouble started with Japan's decision to nationalise the islands by purchasing them from a private Japanese owner. The Japanese government says the reason for the purchase was to calm the controversy surrounding the islands.

The move backfired, however, touching off widespread protests throughout China against the Japanese action. Angry Chinese vandalised facilities of Japanese firms, leading many Japanese firms to shutter operations for security reasons. As in earlier incidents, the situation generally calmed down after a few days as Chinese officials called for an end to violent demonstrations.

Japan and China have repeatedly fought over various issues from the content of history school books in Japan to territorial boundaries and rights to hydrocarbon resources in the East China Sea. In 2010, boundary disputes spread to trade policy after China restricted exports of rare earth metals to Japan in response to Japan's arrest of a captain of a Chinese fishing vessel moving in the disputed waters.

Despite the problems, relations between the countries have generally been moving in a positive direction since the mid-2000s. In 2008, for example, president Hu Jintao travelled to Japan, the first official visit of a Chinese leader to Japan in a decade. During the visit, the two countries reached partial agreement on development of hydrocarbon resources in the East China Sea. In 2010, Japan relaxed visa requirements for Chinese tourists. In May 2012, China, Japan and South Korea signed a trilateral agreement to lower barriers to investment. As part of the deal, the countries agreed to begin talks this year on a trilateral free-trade agreement. The recent events have cast a shadow over the project, increasing the likelihood China and Korea will now move ahead on free-trade talks themselves as Korea tries to gain a competitive edge over Japan in the Chinese market.

Economically speaking, China and Japan are joined at the hip. Any severe damage to economic relations comes at a steep price for both countries. Although imports from Japan to China declined 6 % y-o-y in January-August, Japan still account for 10 % of Chinese imports, just after the EU, which accounts for 12 % of China's imports. China's exports to Japan also grew 5 % in the first eight months of this year with Japan accounting for 7 % of China's exports, making it China's third most important export destination after the EU (17 % share) and the United States (17 %). Tourism from China to Japan and from Japan to China has increased this year faster than travel from other destinations. All of Japan's biggest car and electronics companies have production facilities in China, and Japanese firms have been instrumental in raising Chinese technological sophistication. China accounts for about a fifth of Japan's trade.

More trade disputes filed with WTO. This week, the United States filed its third complaint against China this year, alleging China unfairly subsidises its car industry in violation of its WTO commitments. The disputed measures include granting concessions and cheap credit to exporters of cars and car parts. The US protested China's imposition of antidumping duties on US car in summer, and filed a WTO complaint on China's restriction of exports of rare earth metals in spring. China countered this week with its own complaint against the US for unjustified imposition of countervailing and antidumping duties on Chinese products. China has submitted similar complaints earlier, the most recently last May.

Rulings on most complaints brought before the WTO take a while. When a complaint is filed with the WTO, the parties will first try work out the problem with themselves. Only after consultation efforts have failed may the parties request that the WTO convene a panel to hear the dispute. Any decision reached by the board can then be appealed, and if the ruling requires changes in practices, the panel is usually expected to grant a reasonable transition period.

The use of antidumping duties is fairly common. Dumping is defined as selling a product for a lower price in an export market than in a country's own domestic market. Chinese products by far have been the biggest target of antidumping duties. Over the past five years, about 40 % of all such duties have been imposed on Chinese products. China itself has also been active in imposing its own antidumping duties. The EU's recent decision to look into whether China is dumping solar panels in Europe has inflamed trade tensions between China and the EU. The European manufacturers claim that China sells its solar panels in Europe at prices below actual production cost. China is by far the world's largest producer of solar panels.

Since the global financial crisis hit in autumn 2008, many observers feared that hard times could lead to an upswelling of protectionism in world trade. WTO figures at the moment do not bear this out, but the longer world economic growth remains tepid, the greater the temptation for policymakers to favour domestic producers.

Chinese now buy a quarter of the world's luxury goods. A new assessment from Hong Kong-based HSBC finds that Chinese now purchase 25 % of all luxury goods, up from 5 % just five years ago. China's domestic sales of luxury goods continue to rise sharply, but HSBC reports the Chinese still buy most of their luxury goods on travel. In Australia, for example, Chinese travellers spend an average of three times more than American or European tourists.

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