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Russia

Russia and Belarus stay on daylight saving time. While the rest of Europe shifted back to standard time on October 28, Russia, in keeping with an initiative of president Dmitri Medvedev last year, decided to stay on daylight saving time. Moscow is now three hours ahead of most of Western Europe. Belarus followed suit and also stayed on daylight saving time.

Government decides on next year's big share sales of state enterprises. Last week's cabinet decision was based on the privatisation programme approved last summer that included a list of state-owned enterprises (SOEs) eligible for partial or total divestment in coming years. In the case of most SOEs, proposed share offerings involve partial stakes, and complete privatisation is not envisioned.

The cabinet's decision concerns the sale of stakes in at least eight major SOEs. If the business cycle permits, sales might be extended to include stakes in other state companies as well.

One of the biggest deals is likely the offering of a 6 % stake in the Rosneft oil company. Press reports note that the total stake the state will divest next year is actually around 12 % as last week Rosneft agreed with the multinational BP to give BP 6 % of Rosneft shares in exchange for BP's stake in the TNK-BP joint venture.

Another big share sale next year involves a 10–25.5 % stake in VTB Bank, Russia's second largest bank. The offering next year was moved up after Sberbank's successful share offering in September. The state's ownership stake in VTB is presently 75.5 %.

Other planned 2013 sales include a 7–14 % stake in the diamond mining company Alrosa, a 25.5 % stake in Sibir Airlines and the state's 25.1 % stake in regional electricity producer TGK-5. TGK-5 remained partly in state ownership after the sweeping 2010 reform of the electricity sector.

The share sales have touched off a discussion in the cabinet over whether SOEs are eligible to acquire the shares of other SOEs as they come up for offer. Prime minister Medvedev's position is that SOEs should not be able to participate in these sales; buyers should be private entities as one point of the sales is to reduce the state's presence in the corporate sector. The cabinet is preparing a decree limiting the participation of SOEs in share purchases of other SOEs, but its exact content is still open.

Russian oil and gas production in 2012–2015: slow growth ahead. Crude oil production rose about 1 % y-o-y in January-September, a slightly brisker pace than in 2011. As in 2011, however, the volume of crude oil exports has continued to shrink as an increasing share of oil production is diverted to domestic refineries. In January-September, the amount of oil going to domestic refining rose more than 4 % y-o-y as Russia secured sufficient supplies to meet its growing domestic demand for refined oil products and refineries increased the share of higher value-added petroleum products in their business. Production of petroleum products has been on the rise for years and grew 2–3 % y-o-y. Exports of refined petroleum products recovered notably after a small dip last year.

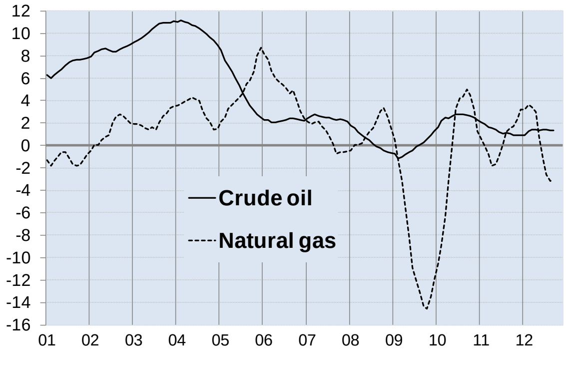
After rising in 2010 and 2011, natural gas production fell 3 % in January-September as gas exports contracted. Exports of gas this year have been at about the 2010 level. Notably, gas exports to Ukraine have dropped due to an ongoing dispute over gas prices and Ukraine's efforts to cut dependence on Russian gas through alternative sources.

This autumn's forecast from the economy ministry slightly lowers the earlier outlook for gas production and export. Gas production is forecast to increase at about 1.5 % a year during 2013–2015, while gas exports are expected to increase at over 2.5 % a year.

The oil sector is expected to develop more slowly than currently. Crude oil production should plateau as should the volume of crude oil exports. The volume of oil going to domestic refining should also stay about the same but refining operations are expected to evolve especially towards growing production of motor fuels. Export of petroleum products, however, will decline at about 2 % a year as Russia's demand for petroleum products increases as the domestic economy grows.

Sustaining production and transport of oil and gas will require vast investment. In the economy ministry's forecast, the volume of investment in natural gas production is expected to more than double from the 2011 level by 2015, and gas pipeline investment should rise about 40 %. Growth in investment in production of crude oil is estimated to increase nearly 20 %. Investment in oil refining capacity will be boosted e.g. by agreements made between oil companies and public agencies.

Russian oil and gas production 2001–2012, production volume over previous 12 months, % change y-o-y



Source: Rosstat

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China

Problems lurk as China's financial markets evolve. The latest IMF Global Financial Stability Report risks to the global economy have increased since the April assessment. The top driver of increased risk is the European debt crisis. The report notes that the emerging Asian economies are generally in a stronger position than advanced economies and the emerging economies in Central and Eastern Europe tied to the Euro Area, but still offers a warning to brace for further deterioration in the global economy.

As in many emerging economies, China's central bank cut interest rates last summer to stave off a sudden slowdown in economic growth. However, the People's Bank of China's room to relax monetary policy has been limited by explosive growth in bank lending in recent years and a sharp rise in housing prices, although Chinese officials have focused on reining in rising credit risk and prevent a housing bubble through such measures as limits on lending to local administrations and stricter rules on apartment purchases and financing.

The most intriguing issue facing China's financial system is how to manage growth and development of the financial system. The country's banking system remains dominated by the four large state-owned banks, which hold nearly half of all the banking sector assets. While banks are still quite healthy, their profitability will be negatively affected by liberalisation of interest rate policy and intensified competition.

At the end of 2011, the total market for debt securities was about 56 % of GDP. The debt securities market is currently dominated by public bonds, but the emergence of robust corporate debt securities markets is expected to vastly increase competition in financial markets by providing companies with alternative access to funding. As of end-2011, the value of China's stock markets was about 46 % of GDP.

A second big issue for financial policymakers is the explosion in financial intermediation outside the formal banking system. This market can be divided into informal lending, the far more transparent trust company sector, and commercial banks' asset management services. The latest GFSR estimates that these financing activities now equal about 35 % of GDP, compared to official corporate and household lending, which is about 140 % of GDP. The risks posed by nonbank actors is reflected in the fact that interest rates on informal loans often exceed 20 %, while the reference rate for official one-year bank loans is currently around 6 %. Some fear that serious problems in servicing trust loans and loans behind wealth management products could spread to the formal banking sector. The report notes signs of debt-servicing difficulties in small enterprises are already evident.

China's bank and financial markets are undergoing a major upheaval. The GFSR says successful risk management calls for active upgrading of prudential oversight and effective use of market discipline.

China invests in natural gas. Over the past five years, the share of natural gas in China's overall energy consumption nearly doubled, accounting for 5 % of all energy consumption last year. The shift to gas reflects increased domestic production, a rapid expansion in domestic gas transmission and distribution, as well as a sharp increase in gas imports.

China has the world's 14th largest proven gas reserves. Most of that gas is located in western parts of China. To get the gas to the metropolises on the east coast, China is building gas pipelines spanning the country. The first pipeline was commissioned in early 2005, and a second completed in August this year. A third transnational pipeline should be completed in 2015.

China's transnational pipelines also extend beyond the western borders to Kazakhstan, Uzbekistan and Turkmenistan. China has agreed on substantial deliveries with Turkmenistan through 2039, and reached a major supply deal with Uzbekistan last summer (the gas began to flow in August). Another pipeline running from Myanmar to southern China is currently under construction and should be ready sometime next year. China is still in negotiations on a gas pipeline from Russia. Russian gas giant Gazprom announced this week its go-ahead on the Vladivostok gas pipeline geared to meet at least Japan's energy needs. The pipeline should be completed in 2017.

Pipeline transmission of gas is nothing new to China, but even last year some 75 % of imported gas still arrived in the form of liquefied natural gas (LNG). Australia has been China's most important foreign gas supplier, but will probably be overtaken by Turkmenistan this year, as gas pipeline transmission has been increasing sharply.

To satisfy its thirst for energy, China is substantially ramping up the use renewable energy sources such as hydro, wind and solar power. Growth of China's nuclear industry, in contrast, has been cautious, with nuclear power only providing about 1 % of the country's energy supply at the moment. Plans to build new nuclear power plants were shelved in spring 2011 after the Fukushima disaster. Last month, China announced it was again green-lighting new nuclear projects, but plans are more cautious than pre-Fukushima and long-term production targets for nuclear plants have been lowered.

Coal is still China's top energy source (68 %), with crude oil in second place (19 %) and hydropower in third (7 %).

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