EUROJÄRJESTELMÄ
EUROSYSTEMET

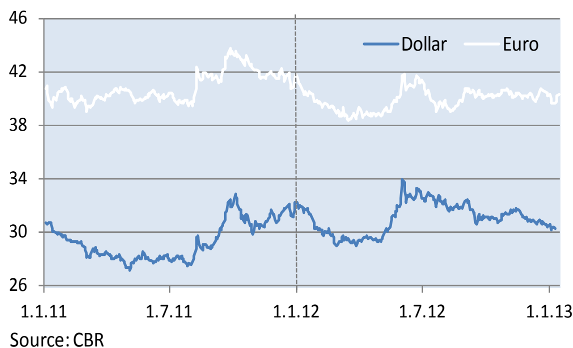
# BOFIT Weekly

3 • 18.1.2013

# Russia

**Ruble strengthened slightly in 2012.** The ruble appreciated 2–3 % last year against the euro and US dollar. One euro bought 40.23 rubles at year's end, while one dollar fetched 30.37 rubles. The real exchange rate, which takes into account differences in the inflation rates of Russia and the US and EU countries, saw the ruble strengthen 7–8 % against the euro and dollar. The real appreciation of the ruble was greater than its appreciation in nominal terms, as the inflation rate in Russia was higher than in the EU and the US. Russian inflation was 6.6 % at the end of 2012.

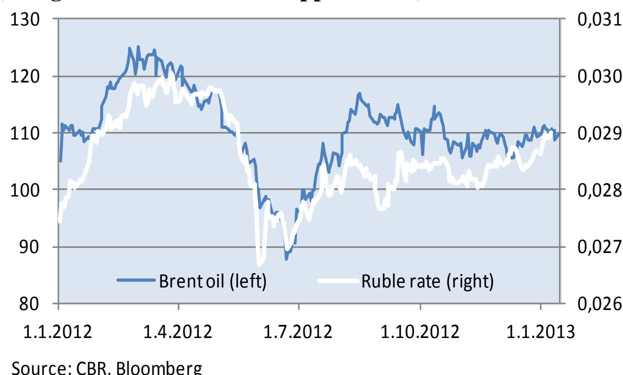
**Euro/ruble and dollar/ruble rates, 2011–2012 (rising trend indicates ruble depreciation)**



Source: CBR

The ruble's exchange rate continued to closely track world crude oil prices. The ruble strengthened as the oil price spiked in Q1/2012, then declined with the oil price in late spring and early summer. Since autumn, the oil price and ruble exchange rate have been less volatile.

**Brent-oil price (US$/bbl) and ruble/dollar-euro basket, 2012 (rising trend indicates ruble appreciation)**



Source: CBR, Bloomberg

The Central Bank of Russia manages the ruble float with market interventions designed to keep the ruble within a preset fluctuation band based of its value relative to a dollar-euro currency basket. The band has been widened in recent years and the CBR has reduced its interventions so that the ruble's exchange rate is now more freely determined by the markets. The CBR last year only intervened to support the ruble with forex selling in June and July, and for a brief period in September. When the crude oil price shot up at the start of the year, the CBR smoothed the rise of the ruble by selling rubles.

**Russia returns to stricter fiscal policies.** In December, the Duma approved a law to check growth in federal budget spending and over-dependence on energy prices by setting limits on spending and creating a mechanism that automatically transfers excess budget revenues to reserve funds. Russia's heavy reliance on world energy prices is obvious from the fact that half of federal budget revenues and nearly 30 % of all public sector revenues are derived from production fees for oil and natural gas and export duties on oil, petroleum products and gas.

Similar, but stricter, budget restraints were in force from 2004 to 2008, before they were abandoned to deal with the recession. The reserves amassed during that period allowed Russia to power through the recession without having to cut federal spending or take on new government debt.

Under the new law, annual federal budget spending is based on revenue that would accrue if the price of oil would equal the average price over previous years. Spending can exceed that revenue by up to 1 % of the budget year's forecast GDP. Under the government budget guidelines for the 2013–2015 period, the rule was somewhat eased for the 2013 budget. Starting in 2014, however, the rules are applied in full. The price of oil at which the federal budget balances would be around $105/bbl.

Excess revenues from oil and gas fees will be transferred to the Reserve Fund until it reaches a size equivalent to 7 % of GDP. Surplus revenues thereafter will go to the National Welfare Fund. Up to half of excess revenues can, however, be diverted to infrastructure projects. The Reserve Fund is currently worth about 3.5 % of GDP.

The government's debt policies for 2013–2015 call for the federal government to continue to ramp up its borrowing well beyond its needs to make up the possible budget deficit. The aim is to help in rebuilding reserves. The Reserve Fund would be rebuilt mostly through borrowing and privatisation sales so that by 2015 the Reserve Fund would reach about 5.5 % of GDP. The assets of the National Welfare Fund would not grow and would correspond to about 3.5 % of GDP in 2015. They amount currently to about 5 % of GDP.

Most of the planned government borrowing would come from domestic investors. Of about 1.45 trillion rubles of gross borrowing this year, over 1.2 trillion rubles is expected to be raised domestically. Borrowing from abroad is expected to reach around €6 billion a year during 2013–2015. Despite the borrowing, the gross federal debt will only rise to about 13.5 % of GDP in 2015. The gross federal debt at the moment is equal to just over 10 % of GDP.

Bank of Finland • Institute for Economies in Transition, BOFIT
P.O. Box 160, FI-00101 Helsinki
Phone: +358 10 831 2268 • Web: www.bof.fi/bofit

Editor-in-Chief Seija Lainela • Email: Seija.Lainela@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.*

EUROJÄRJESTELMÄ
EUROSYSTEMET

# BOFIT Weekly
**3 • 18.1.2013**

# China

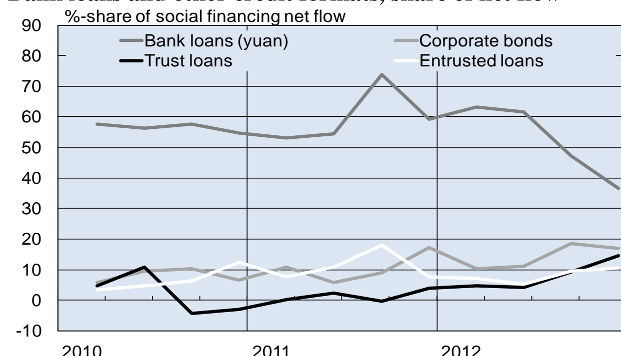
**Share of traditional bank loans in finance continues to decline.** Assessing macroeconomic conditions in China has become increasingly difficult in recent years with the dramatic change in structure of financial market. As officials have tried to rein in bank lending since the stimulus measures in 2009–2010, less-regulated modes of financing have become popular. For the last two years, officials have used the term "social financing" to describe this broader measure of financing. In addition to traditional bank loans, social financing includes forms of financing that do not show up on bank balance sheets such as bank accepted bills, corporate debt paper, equity financing, and entrusted loans and trust loans, where banks or specialised trust companies mediate money from private entities.

Although traditional bank loans still dominate the total financing stock, yuan bank loans now represent less than 40 % of new financing issues to firms and households. In contrast, financing based on corporate bonds, entrusted loans and trust loans has soared. The second half of 2012 also saw a distinct jump in forex bank loans, probably a response to yuan appreciation. Share emissions and short-term bank accepted bills, in contrast, saw hardly any uptick last year.

Out-of-pocket financing covers 70 % of corporate investment, compared to just over 20 % for bank loans (although firms are in highly disparate positions with respect to access to financing). New channels of finance have opened as private individuals and firms have sought better yields than for bank deposits. In addition to the above mentioned forms of financing, China has a vast informal and unregulated lending market that does not appear on official radar.

Altogether, China's financing markets are quite opaque, which impedes supervision, complicates monetary policy and generates systemic risks. Regulators are also concerned about mounting default risk as the share of short-term borrowing has skyrocketed.

**Bank loans and other credit formats, share of net flow**




*Source: Macrobond*

**Forecast revisions and financial market reforms rock stock prices.** China's stock markets were down overall in 2012, and in early December A-share prices on the Shanghai stock exchange reached their lowest level since the start of 2009. Shares then jumped 16 % in the final weeks of 2012 on an improved outlook for Chinese growth. 2012 ended with the Shanghai A-share index up 3 % from 12 months earlier. In comparison, share prices were up 11 % on-year in Russia, and the Morgan Stanley emerging market index was up 15 %. Chinese stocks have continued on an upward trend in January.

Since China's stock markets began to attract serious interest in the mid-2000s, it has experienced violent swings. Before the global financial crisis hit in autumn 2007, share prices reached a level more than 2.5 times their current valuations. The average price-to-earnings (P/E) ratio at times exceeded 70. At present, the average P/E for traded shares is about 12, a bit lower than the global average.

Chinese share prices have also been rocked by changes in China's financing system and stock market reforms. At the start of January, prices of B-shares, which are directed to foreign investors, were hit by speculation that Chinese firms are phasing them out and replacing them with Hong-Hong-listed H-shares. The China Securities Regulatory Commission (CSRC) plans to further open up China's markets through substantial increases in foreign quotas on China's securities markets.

The nature of Chinese securities markets was evident last week when the Shanghai stock exchange assumed that it was its task to instruct members to pay out dividends equal to at least 30 % of profits to stimulate stock trading. Even if the instruction might have been well-justified in the case of many of China's state-owned firms, a bedrock rule of corporations law is that the board, not a securities exchange, recommends the paying and size of a dividend to shareholders.

**Shanghai, Moscow and Morgan Stanley Capital International Emerging Market indexes**

*Source: Bloomberg*

Editor-in-Chief Seija Lainela • Email: Seija.Lainela@bof.fi
Bank of Finland • Institute for Economies in Transition, BOFIT
P.O. Box 160, FI-00101 Helsinki
Phone: +358 10 831 2268 • Web: www.bof.fi/bofit

*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.*