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Russia

Russian Duma approves law extending recycling fee to domestic-built vehicles; new forms of subsidy for domestic car industry proposed. EU-Russia trade relations have been strained ever since Russia joined the WTO in August 2012 due to Russia's imposition of a recycling fee on all imported cars. The fee equals the duty reduction for cars mandated in Russia's WTO membership negotiations. The recycling fee violates WTO principles as it exempts domestically produced vehicles from the fee.

Russia promised last January to correct the situation within six months. After nothing happened, the EU and Japan filed in July an official request for consultations with the WTO. The EU further asked the WTO last month to form a working group on the matter. The legislation requiring domestic carmakers to pay the recycling fee was rapidly processed by the Duma and passed on October 16. The law goes into effect at the beginning of next year. As a result, the WTO is holding off on its investigation, which would be a first for Russia under the WTO's dispute resolution process.

Russia's industry and trade ministry has drafted a bill that extends subsidies to the car industry from the start of next year. Subsidies would be paid to all car manufacturers engaged in assembly operations, and thus would cover practically all major carmakers. The subsidies would be paid for production of low-emission vehicles, as well as for covering costs related to product development and maintaining employment, among others. Russian experts say that the proposed subsidies conform to WTO rules.

Customs union summit exposes Kazakh and Belarusian unhappiness. The summit was held last Friday (Oct. 25) in Minsk. Kazakhstan's president Nursultan Nazarbayev offered the strongest criticism of the custom union. In his opinion, trade imbalances have increased since the customs union was created in 2010. Producers in Kazakhstan and Belarus find it difficult to get their products onto the Russian market due to technical barriers to imports. Part of the problem is that the customs union has yet to adopt common product standards. Russia's certification system differs substantially from the Kazakh system, making export of meat products from Kazakhstan to Russia essentially impossible. Kazakhstan's economy has also suffered from the fact that the country has yet to be allowed to export electricity to Belarus via Russia. Nazarbayev also wants to see relaxation of inspection measures for goods at the outside borders of the custom union.

Nazarbayev complained that the Russian members of the Eurasian Economic Commission, the customs union's highest regulatory body, take their orders from Moscow, even if the commission is supposed to be independent. For this reason, Kazakhstan sees no point in supporting proposals to increase commission powers.

Belarus president Alexander Lukashenko complained that exceptions and restrictions on free trade for specifically agreed products during the formation phase of the customs union have actually increased for the time being, even if the ultimate goal is to gradually eliminate such exceptions altogether. The thorniest issues relate to exceptions for crude oil and petroleum products. Russia and Belarus disagree e.g. on duties of petroleum products refined from Russian crude in Belarus for export to third countries.

Customs union members are currently drafting a basic agreement on the Eurasian Economic Community that will replace the customs union in 2015. President Vladimir Putin said the agreement must clearly specify obligations of members in various spheres of economic regulation. The agreement should guarantee free movement of goods, labour and capital. Putin lamented that all customs union goals have yet to be implemented.

World Bank finds Ukraine, Ruanda and Russia make biggest strides in becoming more business friendly. The latest World Bank Doing Business 2014 survey notes that over the past year Russia has risen from 112th to 92nd place among the 189 countries surveyed. Russia's current business environment is on par with e.g. Albania and Serbia.

The World Bank survey measures the impact of state regulation on business activity in the largest city of each country in the survey. The survey ranks each country in ten categories, each of which is evaluated by three or four indicators. Assessments of experts and regulatory officials provide the basis for each country's scoring.

President Putin decreed in May 2012 that Russia would become one of the top 20 most business-friendly countries in the world by 2018. The move has made Russian officials look into what should be done to make such gains in each of the World Bank categories.

Russia saw its largest gain this year in the category for how long it takes for a company to get hooked up to the electricity grid, with the average number of days for a connection falling from 280 to 195 days. The average number of days to process a building permit fell from 344 to 297 days, while the number of days to register property dropped from 44 to 22 days.

A noteworthy limitation to the World Bank survey is that it only covers one of the areas affecting business environment, namely state regulation. Hence, it omits such important factors as ease of access to markets, free and fair competition, judicial independence and existence and extent of corruption. The survey also overlooks the qualitative aspects of official activity.

Russia's generally weak business environment is a big reason that domestic firms invest relatively little in their home country, preferring to hold significant amounts of their assets offshore.

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China

China expected to announce new economic policy framework and renew commitment to reform. The third plenary session of the 18th Central Committee of Communist Party convenes next week (9–12 November). The Central Committee is made up of 204 members, who serve a five-year term. The committee assembles annually, but traditionally the third plenum is reserved for hammering out major economic policy themes. Expectations were raised even further that something was in the works late last week, when Yu Zhengsheng, a member of politburo standing committee, described the reforms in consideration as "unprecedented."

Ministries, research institutes and other central players have prepared reports and policy recommendations for the Central Committee. While there have been no official announcements of the proposed reforms, some draft documents have been circulating in public.

The Development Research Centre (DRC), which serves as a think tank for the State Council, has reportedly proposed moving towards a more market-based economy, improving transparency in public administration and increasing legal protections. To achieve these goals, the DRC is calling for reforms in such areas as public administration, fiscal system, state monopolies, land ownership, financial sector, state ownership and treatment of foreign firms.

Other reforms that have been suggested include changes in the *hukou* household registration system and relaxation of the one-child policy so that couples could have a second child if only one of the parents is a single child. Currently, both parents have to be only children to be eligible for a second child.

No matter what the nature of the reform plans announced, what matters most is that China's leaders show a strong commitment to future reforms. The lesson from China and other countries suggests that structural reforms only succeed with decision-makers genuinely behind them.

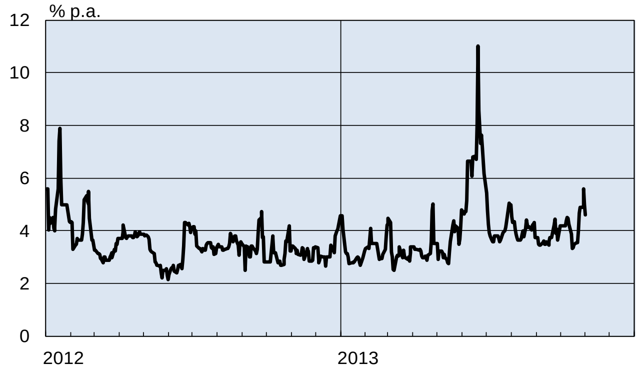
China takes further steps in deregulating interest rates. Late last month, the People's Bank of China introduced its new loan prime rate, which is calculated daily based on the weighted average rate that the nine largest banks charge their best corporate customers. The PBoC hopes the loan prime rate will provide more information about the level of market rates and help banks adjust, as the central bank is gradually giving them more freedom to set their rates.

The situation will, however, remain complicated for interest-rate policy in general. As the large state banks dominate how the loan prime rate is determined, the new rate will likely reflect the government's view of the appropriate interest rate. The loan prime rate now coexists with the PBoC's reference lending rates, even if lending was freed from interest rate regulations last July. The first loan prime rate (one-year) quote last week was 5.7 %, while the one-year reference rate stood at 6.0 % for the second year in a row.

Deposit rates, in contrast, are still subject to strict regulation, although the central bank has said it will soon allow market-based interbank trade on certificates of deposit. In addition to helping liquidity management of banks, freeing up the trade for wholesale savings is seen as a step towards deregulation of deposit rates. Among the obstacles to extensive deregulation of deposit rates is the lack of legislation on depositor protection. The government is considering new initiatives in this area.

At the end of October, bank liquidity again tightened and short-term interest rates spiked as corporate tax payments came due. Although no rate shock similar to that of late June is looming, rates are up since last spring.

Shanghai interbank offered rate (7-day Shibor)



Source: Macrobond

China's grain harvest increases again this year. The National Bureau of Statistics reports that this summer's grain harvest reached 132 million metric tons, up two million metric tons from last summer's harvest. The summer harvest constitutes about a fifth of the overall harvest. The main harvest season is autumn. Preliminary reports suggest the autumn harvest will also be bigger than last year. Meat production has tracked the increases in grain production, with both up just over 1 %.

China seeks to be 95 % self-sufficient in its main grain crops. Although farm output has risen in recent years, consumption has risen faster, forcing China to rely more on food imports from abroad. As imports have risen, China's self-sufficiency has fallen by some estimates to below 90 %.

Farm output has been boosted by switching to higher-yield varieties, increased irrigation and better training of farmers in fertiliser use. However, there is still plenty of room for improvement in Chinese farming methods. For example, the size of the average farm is still tiny (0.5 hectare), which prevents, among other things, efficient use of modern farming equipment.

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