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# BOFIT Weekly

**47 • 21.11.2014**

# Russia

**Federal budget so far in surplus; next year's budget likely to dip slightly into the red.** Preliminary finance ministry figures show a January-October federal budget surplus of 1.9 % of GDP. Although the decline in world crude oil prices in recent months has reduced Russia's dollar-denominated export earnings, the collapse of the ruble has largely offset the drop. Measured in rubles, budget revenues from taxes on oil production, as well as export duties on oil, have largely matched their budget targets. Other budget revenue categories have felt a modest boost from the pick-up in inflation.

The end-year surplus is likely to be largely wiped out as government agencies try to spend their full budget allotments before the end of the year. As a result, this year's budget should be nearly in balance by the end of December. The federal budget this year was earlier expected to show a deficit of around 0.5 % of GDP.

On November 14, the Duma approved the critical second reading of next year's budget act. The proposed budget would have a deficit of 0.6 % of GDP. Fees and duties from oil set aside in the Reserve Fund would be used to cover the deficit. The budget calculations assume an average Urals oil price in 2015 of $100 a barrel and an average exchange rate of 34 rubles to the dollar. Both assumptions are already outdated. According to the finance ministry, the situation will, however, be improved by ruble weakness, which will increase oil income in ruble terms compared with earlier calculations.

**Russia puts ceilings on consumer credit rates.** Last year the Duma passed an amendment giving the central bank the authority to set ceilings on consumer credit charges (combined total of interest and other fees converted to a per annum interest rate). The move sought to rein in the often sky-high costs of consumer credit in Russia.

The Central Bank of Russia has for the first time released figures on the average costs of consumer loans. The data cover the third quarter of 2014. Based on the information, the CBR has issued guidance that the total cost of a consumer loan granted in the first quarter of 2015 may not exceed by more than 33 % the average total cost of consumer loans granted in 3Q14. The allowed quarterly maximum costs are categorised according to lender and credit type.

Hence, credit institutions can in 1Q15 collect costs and interest on e.g. unsecured loans of less than 30,000 rubles (€510) at up to 46.8 % p.a. Organisations making unsecured loans of less than 30,000 rubles for periods of one month or less may not charge a rate equivalent higher than 914.8 % p.a.

Growth in bank lending to households has slowed steadily since 2013. One reason is that banks have tightened their lending rules to comply with CBR guidelines. CBR guidelines, in turn, have been shaped to reduce the exposure of banks to credit risk from consumer loans. Credit risk related to unsecured loans, in particular, has increased sharply.

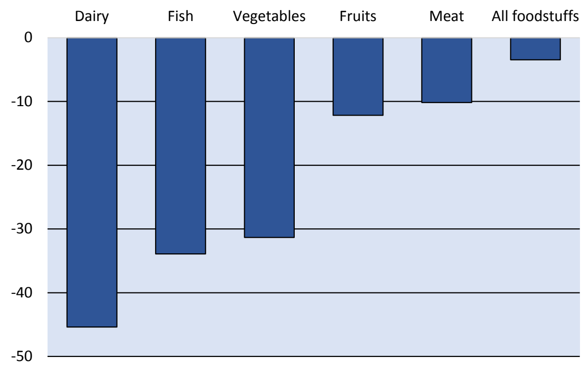
**Russian foreign trade continues to contract.** The value of Russian goods exports in the first nine months of the year was just over $380 billion and the value of goods imports was just under $220 billion. The value of exports shrank 1 % y-o-y, while the value of imports fell 6 % y-o-y.

The value of third-quarter goods exports fell 4 % from a year earlier, due in large part to lower oil prices and contractions in volumes of both crude oil and natural gas exports. Crude oil exports to non-CIS countries fell by 5 % y-o-y, while gas exports to non-CIS countries decreased by more than 25 %. In contrast, exports of refined petroleum products grew briskly. Gas exports to CIS countries plunged over 50 %, mainly on a sharp decline in gas exports to Ukraine. EU countries account for over half of Russia's total exports.

Driven largely by the fall in the ruble exchange rate, the value of goods imports contracted in the third quarter by nearly 7 % y-o-y. While imports contracted in nearly all product categories, the biggest drop (12 %) among the most important ones was seen in machinery, equipment and transport vehicles, which account for about half of Russian goods imports.

Impact of the import ban on select food items that Russia imposed in August was visible in imports. Food represents 13–14 % of Russia's total goods imports; the ban targets about three percentage points of that slice of imports. Imports of products in categories affected by the ban fell by nearly 25 % y-o-y (in both value and volume terms) in the August-September period. Imports of dairy products and fish have been hardest for Russians to replace as their imports have contracted most.

**Change in value of main categories of food imports affected by Russia's ban and total food imports, Aug.-Sept. 2014, % y-o-y**




*Sources: BOFIT, Russian customs*

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# China

**"Through Train" link of Shanghai and Hong Kong stock exchanges expands access to Chinese equities.** The opening of China's capital markets took a great leap forward on Monday (Nov. 17) with the launch of linked trading on mainland China and Hong Kong stock exchanges. The arrangement allows foreign investors to trade shares on the Shanghai Stock Exchange (SSE) via the Hong Kong Stock Exchange (SEHK), and Chinese on the SEHK via the SSE.

The joint programme permits trading in shares included in the SSE 180 and SSE 380 indices, shares in the SEHK's Hang Seng Composite LargeCap and MidCap indices, as well as shares of companies listed on both the SSE and SEHK. Currently the programme covers 568 SSE-listed shares and 268 SEHK-listed shares.

The cap on foreign investor net purchases is 300 billion yuan (€39 billion) for the Shanghai exchange, less than 2 % of the SSE's market capitalisation. Net purchases of Chinese investors trading on the SEHK are capped at 250 billion yuan, less than 1 % of the SEHK's market capitalisation. Trade flows are also subject to daily limits: the SSE maximum daily net buys are 13 billion yuan (€1.7 billion), while the maximum net buys for the SEHK are 10.5 billion yuan. Investment in China is further limited by restrictions on foreign ownership. A single foreign investor may not hold more than 10 % of a Chinese firm and no more than a total of 30 % of a Chinese firm's shares may be in foreign hands.

Access to Chinese stock markets was earlier limited to investors with Qualified Foreign Institutional Investor (QFII) or Renminbi Qualified Foreign Institutional Investor (RQFII) status. Now any Hong Kong resident or foreign investor can trade on the Shanghai exchange. Mainland institutional investors and private investors with assets of at least 500,000 yuan (€65,000) can trade on the Hong Kong exchange. The arrangement lets mainland Chinese invest in some of China's largest SEHK-listed firms, including Tencent, Lenovo and China Mobile.

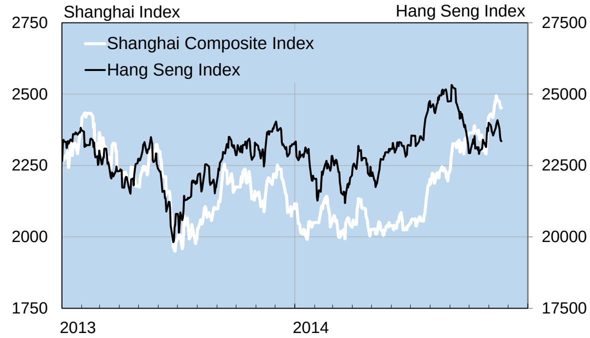
As all trading is in yuan, the "Stock Connect" experiment is hoped to increase international yuan demand and reinforce Hong Kong's position as a yuan-trading centre. As a symbolic gesture, the Chinese have also lifted the 20,000-yuan daily conversion limit on Hong Kong residents.

**Trading via Shanghai and Hong Kong stock exchange link off to weaker-than-expected start.** Although the start of linked trading on Monday (Nov. 17) appeared to reach the 13-billion-yuan daily buy quota for the Shanghai stock exchange, some trades were later cancelled. The total value of buy orders on the SSE via the link was 12.1 billion yuan. Link trading cooled sharply on Tuesday and Wednesday, bringing the total value of share purchases in the first three days of trading to 19.7 billion yuan (€2.6 billion). Foreign owners sold 400 million yuan (€52 million) in shares purchased on previous days. Intraday trading on the Shanghai stock exchange is prohibited.

Over the first three trading days, mainland Chinese purchased shares valued at 2.9 billion yuan (€382 million) on the SEHK. The value of sold shares was about 300 million yuan (€39 million). Chinese share buyers were put off by the relative priciness of Hong Kong shares, even if Hong Kong share prices have fallen in recent months. Prices on the Shanghai exchange are up 16 % from the start of the year, while Hong Kong share prices on average are about where they were at the start of the year. In the first three days of linked trading, share prices fell on both exchanges.

Thus far the Through Train arrangement has had little impact on daily trading volumes on either the SEHK or SSE. Trading under the programme during the first three days represented less than 4 % of the daily trading volume on the SSE and less than 2 % on the SEHK.

**Hong Kong and Shanghai stock indices, 1.1.2013–19.11.2014**




*Source: Macrobond*

**China's economic figures reveal long-expected slowing.** China's October inflation and other headline economic figures were somewhat lower than expected and reinforced the view that economic growth has settled into a long-term slowing trend. The 12-month change in consumer prices in October of 1.6 % was unchanged from September, and inflation remained at its lowest level since 2010. Producer prices continued to drop, down 2.2 % y-o-y in October. On-year growth in October in the loan stock, money supply and fixed capital investment slowed from September. Growth in lending by the shadow-banking sector showed an even more pronounced slowing than growth in the formal banking sector. Industrial output rose 7.7 % in October, a slight drop from 8 % in September. Growth in the value of exports and imports also slowed.

The slowdown in economic growth matches expectations, and GDP growth is expected to remain around the 7 % level. In recent months, the People's Bank of China has provided banks with short-term financing to increase market liquidity. Broader easing measures by the central bank might put at risk efforts to manage rising indebtedness in China.

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