Weekly Review
9 • 4.3.2016

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Russia

Russia approves 2016 anti-crisis economic programme. Over its several weeks of planning, the anti-crisis programme has seen its price tag repeatedly reduced as Russia's fiscal outlook faltered. Funding decisions were made for only some measures of the approved plan, though the sources are still partly unclear. The fate of other measures (including support for the troubled VEB state development bank) will depend on economic trends in the first half of this year.

The total value of the package amounts to just under 700 billion rubles (€8 billion). However, most of the measures inked in the programme are already included in this year's federal budget. The additional funding needs are put at 160 billion rubles. This corresponds to 0.2 % of GDP, so the impact on the economy is likely to be limited. It is also still unclear where the additional funding will come from.

Some 60 % of the total 700-billion-ruble package will go to regions and social spending, a bit more than a third will go to supporting industry and rest to help small and medium-sized enterprises (about half in the form of government guarantees). Over 70 % of the 160-billion-ruble additional funding is marked for industry, with the remainder going to regions and social spending. Carmakers are the big winners; they are set to receive support worth 140 billion rubles.

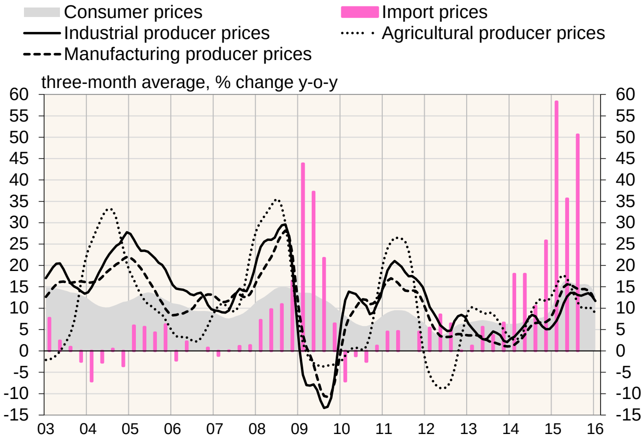
The programme also includes a long list of structural reforms. These cover a broad spectrum of various measures like regulatory reforms and improved oversight of state firms.

Inflation in Russia moderates. Consumer and producer price inflation have slowed recently. Industrial producer prices were in fact down clearly on-month in December-January. In on-year terms industrial producer prices and consumer prices were still up 8–10 % in January. A similar 12-month rise in industrial producer prices was last seen in 2012 (not counting the 2015 spike).

Inflation picked up when the ruble's slide steepened in spring 2014 with the Ukraine conflict and the following summer on foreign sanctions and Russia's retaliatory import bans on food and agricultural products. Inflation picked up sharply last winter as the ruble crashed and import prices soared in ruble terms (up 75 % in just six months), more than even in the 2008–2009 ruble crisis. Imports have had a large share in the economy, e.g. spending on imported consumer goods and spending by Russian travellers on goods and services abroad equalled about 15 % of private consumption, while imported investment goods represented a fifth of total investment.

This winter, the ruble's slide has been much milder compared to last winter. Central Bank of Russia governor Elvira Nabiullina noted that the effect of the ruble's slide on prices has also been weaker than a year ago. The CBR reports this is due to weak demand and the fact that there has been no rush to buy goods, unlike last winter. The CBR expects consumer price inflation to slow to 7–8 % y-o-y by the end of this year.

Changes in consumer, producer and import prices, 2003–2016



Source: Rosstat.

Finland's trade with Russia declined sharply last year. The contraction reflects mainly lower oil prices, weak Russian demand and the ruble's devaluation. EU-imposed sanctions on trade with Russia have apparently had only modest impact on trade. The food import bans imposed by Russia reduced Finnish food exports. The value of goods exports was €3.2 billion and goods imports €6 billion. Exports and imports shrank by nearly a third to levels well below the troughs of the 2009 recession. Russia accounted for 6 % of Finnish goods exports and 11 % of imports.

The structure of exports has scarcely changed in recent years. Some 34 % of exports last year consisted of machinery and equipment, 26 % of chemical products and 14 % of wood and paper products. Foodstuffs fell slightly to 4 %. In 2009, the share of machinery, equipment and transport vehicles contracted sharply, largely on the collapse of re-exports of mobile phones and passenger cars, which have not recovered much since. Finnish customs says re-exports (i.e. exports of goods manufactured in a third country) accounted for 22 % of Finland's exports to Russia in 2014. Re-exports currently include e.g. some machinery and pharmaceuticals.

The structure of imports has also showed little change. Last year mineral fuels (mainly crude oil) still accounted for over 70 % of imports, so the fall in imports was largely due to lower oil prices. Chemical products were 13 % of imports, wood products 6 % and metal products 3 %.

Russian tourism in Finland also declined sharply last year. Slightly over 9 million people crossed Finland's eastern border, a decline of about 20 % from 2014. Tax-free sales fell roughly the same measured by the number of purchases. Overnight stays of Russian travellers declined by over 40 %. Nevertheless, Russians were still the single largest foreign tourist group visiting Finland last year.

Transit transport from Finland to Russia contracted about 40 % last year. It was the fourth consecutive year of contraction and the value of transit freight was just €8 billion (down from €30 billion in peak years).

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China

China relaxes monetary policy. China this week lowered by a half percentage point the reserve requirement on bank deposits. Since March 1, large banks must place 17 % of their deposits with the People's Bank of China, while small and mid-sized banks must give 15 %. The cut should free up about $100 billion in yuan deposits for lending. Reserve requirement ratio was last lowered in October.

Besides lowering reserve requirement to boost lending, the PBoC injects short-term liquidity into the system through open market operations by buying securities from banks with a promise to sell them back (reverse repo). The central bank also has other monetary tools to help banks meet their liquidity needs and target lending, including the standing lending facility (SLF), medium-term lending facility (MLF) and pledged supplementary lending (PSL).

Strong credit and money supply growth in January point to relaxed monetary policy stance. Short-term money-market rates (7-day), however, have remained at around 2.5 % since last summer and lowered reserve requirement appears to have had no immediate effect on interest rates. China's monetary policy framework remains complex, which complicates the assessment of the monetary policy stance.

Environment for monetary policy is challenging. On the other hand, monetary policy is expected to support the government's growth target, yet labour markets, price trends and the economy's structural shift argue for embracing a lower growth path. Furthermore, China's mounting debt problems, capital outflows and the depreciation pressure of yuan are not making it easier for the policymakers.

China's service sector increasingly shouldering growth burden. China's service sector grew by over 8 % in real terms last year, while industrial and construction output was up 6 % and primary production (mainly agriculture) just 4 %. Fuelled by high growth, the service sector last year contributed its highest share of economic activity ever, accounting for 50 % of GDP. Even so, China's service sector is relatively small. While smaller shares can be found from African countries and petrostates, the service sector in advanced economies typically generates 70–80 % of GDP.

Structure of China's service sector and real growth in 2015

	Growth, %	Share, %
Accommodation and catering	6	4
Transport and storage	5	9
Real estate	4	12
Finance and insurance	16	17
Wholesale and retail trade	6	19
"Other"	9	39
Total service sector	8	100

Source: China National Bureau of Statistics.

Finance and insurance have been the fastest growing branches within the service sector in recent years. In contrast, growth slowed last year in trade, transport, and accommodation and catering services. The "other" services category, which encompasses about 40 % of China's service sector, has enjoyed robust growth and suggests a rapid expansion of public services. The most recent available figures from 2012 show about 60 % of "other" services are generated by public administration, education, health care and research activity.

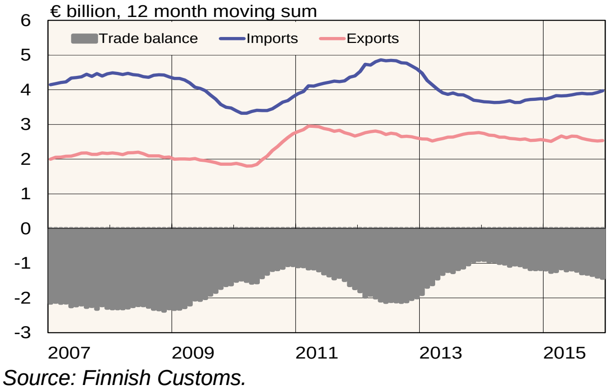
China increased its share of Finnish foreign trade last year. Although the value of Finnish goods exports to China fell 1 % last year to €2.5 billion, the value of imports rose 6 % y-o-y to €4.0 billion. The total value of Finnish goods exports last year fell by 4 %, while the value of imports declined some 6 %. China is Finland's fifth-largest trading partner with a 6 % trade share.

The value of Finnish raw-material exports to China exceeded the value of exports in the machinery and equipment category. Raw materials last year accounted for 40 % of all Finnish exports to China. The largest groups were pulp (19 % of total exports) and furs (11 % of exports). The machinery and equipment category, in contrast, shrank to 38 % of exports to China. Chemical products had a 7 % share.

Finland's imports from China consisted largely of machinery and equipment (52 % of imports) and variety of other finished goods (45 % of imports). Imports of machinery and equipment mainly consisted of consumer electronics. Phones last year accounted for 13 % of Finland's imports from China and computer equipment 10 %. Finland imports a wide range of Chinese consumer goods. The share of clothing and footwear declined last year slightly to 15 %.

Chinese travellers last year had 182,000 overnight stays in Finnish hotels and inns, an increase of 53,000 overnight stays from 2014. Overnight stays of all foreign travellers in Finland declined slightly. The number of visitors from China last year exceeded the number of Japanese visitors for the first time. However, the Japanese tended to stay longer and thus had more overnight stays than the Chinese. The number of Chinese travellers in Finland doubled in just three years. Today, 5 % of all visitors to Finland are Chinese.

Trends in Finland-China trade



Source: Finnish Customs.

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