Weekly Review
28 • 15.7.2016

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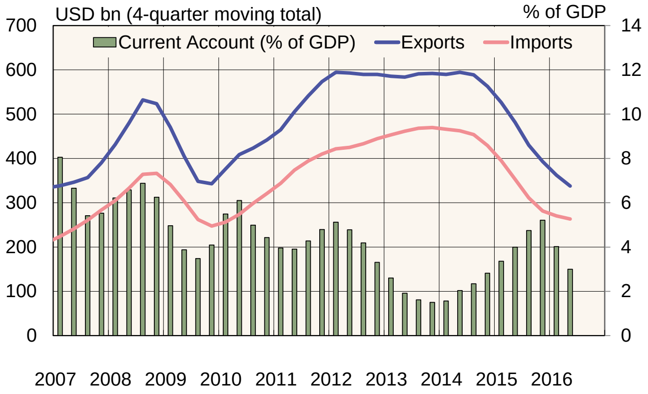
Russia

Contraction in Russian foreign trade and capital outflow slowed down. Preliminary balance-of-payments figures show the value of Russian imports shrank 10 % y-o-y in dollar terms during April-June. Goods imports were down 5 % y-o-y, while services imports plunged by over 20 %. Among the hardest hit were travel services, which were still down by more than a third in 2Q16. Largely due to low oil prices, the dollar value of Russian exports contracted on-year by a quarter in April-June. Oil & gas exports declined by about a third on-year, while other exports were off by about 15 %. With a more substantial decline in exports than imports, Russia's current account surplus contracted in the first six months of the year to $16 billion, a level on par with 2009.

Mainly as a result of Russia's falling foreign debt, the net outflow of private sector capital continued to slow in April-May. Banks continued to pay down their foreign currency debts and repatriate assets from abroad. For other firms, both direct investment inflows and outflows were up slightly, but the levels were quite modest – just over $6 billion. Total private sector net capital outflow in 1H16 was just over $10 billion compared to over $50 billion a year ago. The Central Bank of Russia expects the private sector net capital outflow to reach $25 billion by the end of the year.

Trends in Russian foreign trade and current account balance



Sources: Macrobond, CBR, BOFIT.

Russian state reduces stake in diamond giant Alrosa. In a secondary public offering (SPO), the government sold off mostly to Russian and European investors a 10.9 % stake in the diamond company. After the sale, the Russian state owns a third of Alrosa, the regional and local administration of Sakha Republic a third, with the remainder now freely traded. The divestment sale raised 52 billion rubles (€700 million) for the state coffers.

Alrosa has been on the privatisation list for years, i.e. a state-owned company in which the government plans to reduce its participation. Implementation of privatisation sales has been repeatedly postponed in recent years due to unfavourable market conditions. This year's tight budget, however, seems to have speeded up the sales. Russia's government estimates that selling off its stakes in various enterprises this year could provide as much as 1 trillion rubles to cover the budget deficit. In 2014 and 2015, income from privatisation sales amounted to a modest 7–8 billion rubles, as the government was reluctant to sell stakes in any large firms.

Deputy prime minister Shuvalov noted that this year's planned sale of a 10.9 % stake in VTB Bank, at least, would still be postponed to next year. The decision to hold off on the sale may reflect the fact that VTB remains subject to EU and US financial sanctions. Shuvalov stated that the state plans this year sell off stakes in shipping company Sovkomflot and oil company Bashneft. The sale of a stake in Rosneft is also under discussion. The government is interested in finding strategic investors and Shuvalov does not rule out the possibility of selling Bashneft shares to Rosneft. The privatisation programme approved for 2014–2016 also seeks reductions in state participation in such firms as state airline Aeroflot, rail company RZD and pipeline operator Transneft, but they have not appeared much in sales discussions this year.

The role of state-owned enterprises in the Russian economy is significant and has even increased in recent years. SOEs provide about 30 % of all jobs and account for 40 % of the net sales of the country's 600 largest firms.

Russia seeks ways to reduce grey pay. Facing budgetary shortfalls, the government is trying to increase revenues also by improving tax collection. Finance minister Siluanov has noted that grey wages cause a huge loss of tax revenue, perhaps as much as 1.5-2 trillion rubles (2 % of GDP) a year. The finance ministry and tax administration are now considering ways to get a handle on undeclared income, including reviews of financial sources of large household purchases such as real estate. Earlier a limit to cash transactions was also proposed, but that seems to be dropped. Russia's 13 % flat income tax applies to wages and most other forms of household income.

Some 15 to 30 million Russians (20–40 % of employed persons) are estimated to work in the grey economy. Rosstat estimates that 13–14 million people work solely and another 1-2 million partly in the unofficial sector. Corresponding estimates of Russia's Presidential Academy of National Economy are 9 and 20 million. Surveys of the Academy of National Economy and VTSIOM found that in recent years about 10–15 % of workers received all of their wages under the table, while about 15–20 % has a portion of their wages paid under the table. Half of Russians said they had paid for services or work under the table.

Rosstat GDP figures include an estimate of the grey economy i.e. legal, but unrecorded, economic activity. The estimate does not include criminal activity such as trafficking in illegal drugs. In the first part of 2000s, Rosstat estimated that Russia's grey economy accounted for 20–25 % of GDP and that in recent years that share has declined to around 15 % of GDP. Statistics Finland's estimate for Finland is 1–2 %.

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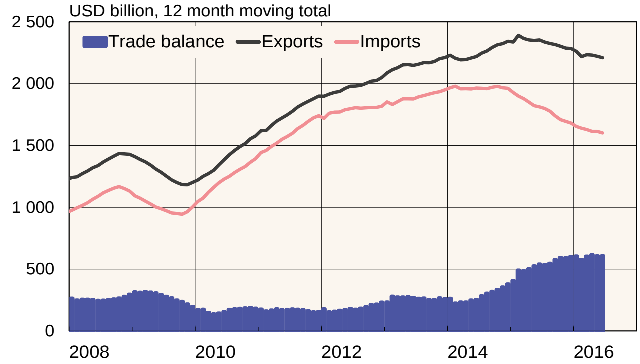
China

China's foreign trade continued to falter in first half. China's general administration of customs reports the dollar-value of goods exports fell 8 % y-o-y in the first half of 2016 and that the value of goods imports was down 10 % y-o-y. The value of foreign trade in June remained at the May level, but exports were still down 5 % y-o-y and imports 8 %.

Contradiction in trade value stemmed largely from low commodity prices and a decline in the yuan's exchange rate. The value of exports in yuan terms fell 1 % and the value of imports 4 % in the first half of the year. The volume of goods trade did not contract, however. Chinese official January-May figures show the volumes of exports and imports on-year were up by a few per cent. Import volumes of many major commodities were up in the first half, including crude oil (rising 19 % y-o-y), copper (26 %), coal (11 %) and iron ore (10 %).

With expectations of yuan depreciation, foreign trade pricing schemes, whereby companies exaggerate import invoices to ship capital out of the country, have again come to the fore as a means of circumventing capital controls in the first half. Chinese official statistics report a value for imports from Hong Kong during January-May that is 2.5 times higher than a year ago. In the same period, Hong Kong figures show the value of exports to China fell. Imports from Hong Kong account for about 1 % of the total value of China's imports.

Trends in Chinese goods trade



Source: Bloomberg

International court finds no historical basis for Chinese territorial claims over the South China Sea. In 2013, the Philippines took China to international arbitration court in the Hague over violations of the United Nations Convention on the Law of the Sea (UNCLOS). On Tuesday (July 12), the 5-member UN arbitration panel ruled in favour of the Philippines. China asserts that its "nine-dash line" demarcation of an area covering most of the South China Sea is based on historical rights. The tribunal, however, said it could find no legal basis for the claim. The panel further noted that none of the features claimed by China in the Spratly Islands met the definition of an island under UNCLOS, giving no right to claim an exclusive economic zone that gives rights to extract natural resources from the surrounding sea and seabed. The ruling is binding, but the tribunal has no power to enforce it.

It was the first time a court took a position on a territorial dispute in the South China Sea. China did not participate in the proceedings, claiming the arbitration panel lacked jurisdiction over the matter. China announced already before the ruling that it would not give credence to any ruling of the panel. It would rather like to seek to resolve differences on a bilateral basis. Besides the Philippines, Brunei, Malaysia, Taiwan and Vietnam also have territorial claims in the region that partly overlap China's. The South China Sea has some of the world's busiest shipping routes, as well as significant fishing waters and large oil & gas potential.

China strengthens its position as the world's largest market for industrial robots. The International Federation of Robotics (IFR) reports that about 248,000 industrial robots were sold globally last year, an increase of 12 % from 2014. China has led the global robot market since 2013. New robot sales climbed to 67,000 last year (an increase of 17 % y-o-y) and China's share of the global industrial robot market rose to 27 %. Asian technological status is reflected in the fact that after China the next biggest markets for robot sales are South Korea (15 % globally) and Japan (14 %). The US accounts for 11 % of the industrial robot sales and Germany 8 %. In 2015, industrial robot sales to China exceeded the sales to all of Europe, even if European sales rose 10 % to about 50,000 units.

Car manufacturers have led the push for industrial automation globally. They accounted last year for 38 % of robot sales, but the volume of growth in robot sales today is slow. While the number of robots working in China's car industry has risen rapidly, vast growth potential remains. The IFR reports that in 2014 there were just over 300 robots per 10,000 workers at Chinese carmakers, while carmakers in Japan had over 1,400 robots per 10,000 workers.

China has also risen rapidly among global robot manufacturers. Nearly a third of all industrial robots sold last year in China were manufactured locally. Although Chinese robot makers still mainly produce systems for fairly simple application, they aspire to advanced robotic capabilities. China's home appliance giant Midea this week announced it was acquiring a 50 % stake in the German Kuka, the world's largest manufacturer of industrial robots. The deal will increase its stake in Kuka to 64 %. Reuters reported last month that China's largest industrial robot maker Siasun is looking to acquire firms in Europe. In June, a Chinese-European investment fund purchased an Italian robot manufacturer.

China's rapid and continuous technological advancement was also evident last month when Chinese supercomputer Sunway TaihuLight took first place in the TOP500 supercomputer speed rankings. The Chinese already held the top position, but the latest breakthrough involved switching out traditional Intel processors with locally developed ShenWei processors. The new processors, however, slightly restrict the range of TaihuLight application areas compared to competing models.

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