

Russia

BOFIT 25th Anniversary Conference examines evolutionary paths of Russia and other post-communist systems.

The first keynote address, delivered by Professor Gerárd Roland (University of California, Berkeley) discussed the evolution of post-communist economies towards democratic market economies. The transition in Central and Eastern Europe began when their increasingly complex economies had become impossible to centrally operate. This translated to a gradual shift in power, especially to corporate bosses. As the old system lost its grip, the process accelerated. The change of system resulted in an increase in corruption and strengthening of unholy alliances of political and economic forces in many of these countries. For some, this problem continues to this day and partly explains their poor economic performances during the 1990s and thereafter. In some of the countries, however, strong civil society helped push back against these forces. In addition, institutional development was much stronger in those countries of Central and Eastern Europe that joined the EU in the 2000s. The perspective of EU membership encouraged many countries to make substantial reforms, especially prior to accession.

The conference programme and links to presentations are available [here](#).

Russia's economic recovery still uncertain. October figures for seasonally and workday-adjusted industrial output showed slight improvement from September, even if they were roughly unchanged from the final months of 2015 and last spring. Russia has experienced spurts and lulls in industrial output growth since February 2015, but the level has remained nearly unchanged. In the case of extractive industries, output declined slightly in October, while manufacturing output rose slightly. The on-year trends for both output categories have displayed some weakening in recent months.

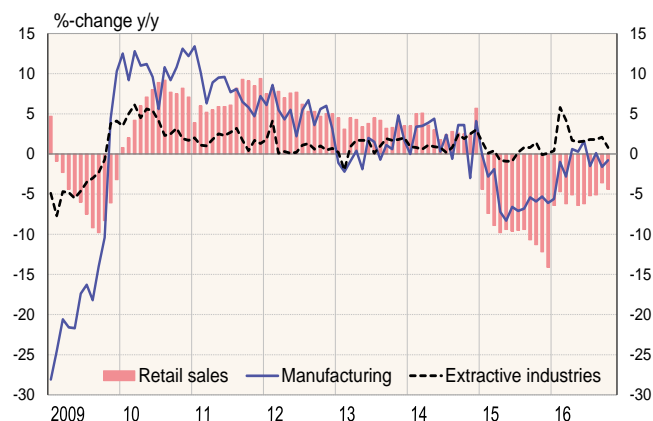
Russia's domestic demand has shown a two-track trend in recent months. The volume of retail sales (seasonally adjusted) continued to fall slightly in October, continuing a slide of 22 consecutive months. The volume of trade was down 4.4 % y-o-y, and 15 % below the October 2014 level. Real household disposable incomes contracted, falling nearly 5 % y-o-y in October. The trends in household borrowing and bank deposits have provided little support for consumption.

The on-quarter slide in fixed investment eased in the third quarter, and was even slightly up from a year earlier, when investment plummeted. For the first nine months of the year, fixed investment was down 2.3 % y-o-y.

The first official Rosstat figures for Russian 3Q GDP suggest a contraction of 0.4 % y-o-y. For the first nine months of the year, the contraction was 0.7 % y-o-y. The Central Bank of Russia and the economy ministry estimate that seasonally adjusted GDP in 3Q was roughly at the same level as in the

previous quarter. The 3Q GDP was boosted by Russia's bumper harvests.

Development of Russian retail sales and industrial output



Source: Rosstat.

Russia on track for record grain harvest. Preliminary figures suggest the grain harvest this year will exceed 123 million metric tons, and increase of about 15 % over last year. Thanks to good weather, the wheat harvest will be nearly 20 % larger than in 2015. Last year's wheat harvest was about 65 million metric tons, of which about 26 million tons went to export. Wheat exports this year are expected to rise to over 30 million tons, which would make Russia the world's largest wheat exporter. Good harvests for most of the world's wheat producers have lowered the wheat price to its lowest level in a decade. The decline in export prices and ruble appreciation threaten the profitability of many farm operations. To ease the strain on farmers, the government decided in September to temporarily eliminate wheat export tariffs.

Russia's agricultural land amounts to about 385 million hectares (ha), of which about half is arable land. Last year about 140 million ha of arable land was in agricultural use, of which about 80 million ha were under cultivation. Rosstat reports that about 47 million ha was devoted to grain crops, and about half of that was wheat. Some 17 million ha was allocated for fodder crops (e.g. hay, alfalfa) and about 12 million ha to vegetable oil crops (e.g. rapeseed, sunflower).

There has been a strong concentration of farmland holdings in recent years. Farms of private homesteaders average about 240 ha, while farmland held by an average large agricultural business is about 12,100 ha. A list compiled by the consulting firm BEFL shows that Russia has at least 43 firms with land holdings of more than 100,000 hectares (1,000 square kilometres). The six largest holders of farmland together control about 3.5 million ha of farmland. Family members of agriculture minister Alexander Tkachev own the dairy producer Agrokomplex, which controls about 456,000 ha. The average field area of a Finnish farm is about 44 ha.

China

BOFIT 25th Anniversary Conference raises insights into China's structural adjustments and growth outlook.

The first keynote address was delivered by professor Gérard Roland (University of California, Berkeley), who provided an overview of the transition in post-communist economies in Eastern Europe and China. Notably, the reasoning behind the transition in China and post-communist regimes in Europe was fundamentally different. In the European context, economic transition can be regarded as part of the dissolution of communist regimes, while in China market reforms were launched to preserve the power of the Communist Party of China. Reforms have strengthened the party apparatus, and it continues to be essential in implementing the reforms. Roland noted that the CPC is now probably the world's most powerful organisation. Under market economy conditions, old ideology and corrupt behaviours are an issue. In China's case, however, Roland said the sustainability of current system should not be underestimated. Roland saw only few hopes for any major political reforms.

The second keynote address was delivered by professor Justin Yifu Lin (Peking University), who analysed China's current economic situation and opportunities for growth over the medium and long term. Unlike most observers, Lin does not ascribe the slowdown in Chinese economic growth in recent years to China's structural issues, but rather that the slowdown largely reflects external business cycle factors related to the global financial crisis. Lin said the slowdown in growth was also evident in many other countries, so there was little reason to ascribe the slowdown to structural problems that would restrain China's future growth.

Lin said China still has a way to go before it reaches the technology frontier of advanced economies, so it can still enjoy the catch-up advantage as Japan and South Korea did decades ago. Chinese per capita income is currently about a quarter of the US per capita income. If China follows the path of its Asian neighbours, Lin believes China could still enjoy GDP growth potential as high as 8 % p.a. until 2028. China's current growth is supported by urbanisation, fixed investment, technological advances and economic reforms. Thus, China should have little trouble in achieving the government's current 6.5 % p.a. growth target over the next four years.

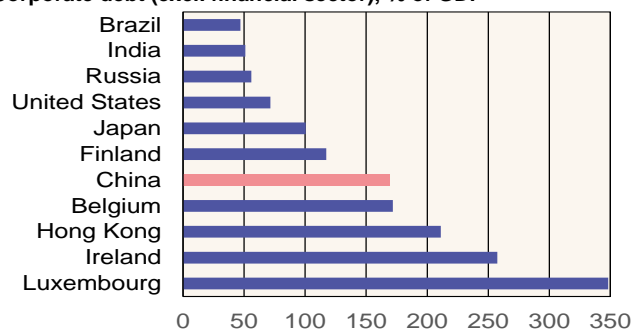
Unlike professor Lin, most forecasters expect China's growth to remain at its current level or slow in the final years of this decade.

Payment delays on the rise in China. It now takes exchange-listed firms over 90 days on average to receive payment from their customers. In 2011, the average payment time was under 60 days. Since then, the average payment delay has increased by about one week each year. The last time the belated payment situation was this bad was after the Asian financial crisis of the late 1990s. The industrial sector has the longest payment times.

The late payment problem has forced many Chinese firms to sell their invoices to third-party finance firms or banks. In exchange for quick cash, the firms surrender a portion of the invoice to the factoring firm. For example, construction equipment manufacturer Sany has reportedly sold payments receivable to factoring firms for 9 % below their face value.

Figures from the Bank for International Settlements (BIS) show that the debt burden on Chinese firms is among the highest on earth relative to the size of the economy. Drawn-out payment times, decelerating economic growth and the ongoing structural change make it more difficult for many firms to service their debts. Non-performing bank loans (NPLs) are on the rise, even if banks claim the problem is small. Many observers note that the actual NPL problem is much more serious than banks are willing to admit.

Corporate debt (excl. financial sector), % of GDP



Source: BIS.

Yuan loses ground on dollar appreciation. The yuan has lost about 2 % of its value against the dollar since the end of October. At the same time, the dollar index (DXY) has strengthened by over 3 %. The yuan has appreciated nearly 2 % against the euro, and its trade-weighted effective exchange rate has strengthened by 1 %. The People's Bank of China seems to tolerate a more volatile dollar exchange rate and put more weight on yuan's stability relative to a multi-currency basket. The markets appear to have no difficulties to live with the current situation as there have been no major reactions from the interbank or equity markets. The exchange-rate difference between mainland China and Hong Kong has also remained relatively small.

Yuan-dollar and yuan-euro exchange rates



Sources: Reuters, ECB.