Weekly Review
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Russia

Russia's public sector finances recover this year; tightening expected next year. The finance ministry predicts revenues to this year's consolidated budget (federal, regional and municipal budgets plus state social funds) to increase by over 10 % in nominal rubles (when the income received from the sale of a stake in state oil giant Rosneft is not included in 2016 revenues). Most revenue improvement comes from an over 20 % increase in oil & gas related taxes, duties and fees. The finance ministry expects Urals-grade crude oil to average slightly less than 50 dollars a barrel this year, which is well above the 2016 average price. Revenues have also been boosted by changes in oil & gas taxation. Other budget revenue streams are expected to increase by 9 % this year. Spending should increase by over 6 % (omits costs of large 2016 financing package to help defence contractors pay off bank loans). Thus, the consolidated budget deficit would be 2.3 % of GDP.

In its newest version of the 2018–20 budget framework, the finance ministry expects consolidated budget revenues to increase by about 6 % next year, over 2 % higher than inflation, and in the following years at about the pace of inflation. As in previous years, revenues are estimated to reach 32–33 % of GDP. Oil & gas tax revenues will shrink next year if the average price of Urals oil falls as expected to below 44 dollars a barrel. Other revenue streams should keep growing next year at 9 % and at a robust pace also in the following years. Estimates of other revenue growth assume the economy ministry's forecasted annual GDP growth above 2 % materialises and tax collection is improved. Besides scheduled tax increases, a few new minor tax hikes have been proposed.

The consolidated budget deficit should contract to 1.5 % of GDP next year and less than 1 % of GDP in 2019–20. Based on the revenue estimate, the deficit target and the new federal budget spending rule, the finance ministry expects spending in nominal rubles to rise by less than 4 % next year and by just 2 % in 2019. Inflation is assumed to run at around 4%. The spending is set to decline towards 33 % of GDP.

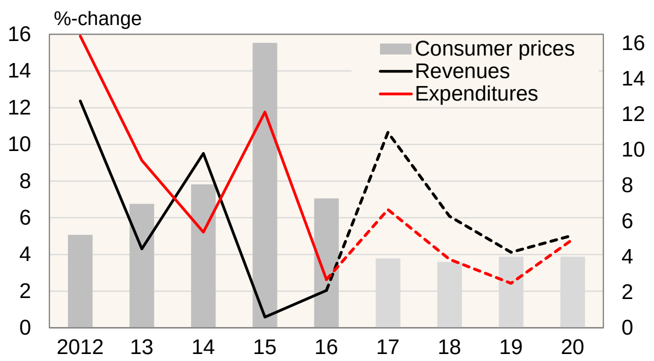
Much of Russia's GDP growth spurt last spring came from inventories. Russian GDP grew in April-June by 2.5 % y-o-y. According to fresh GDP figures, however, much of the growth came from a build-up in inventories, suggesting that growth is still on a rather fragile base. Other domestic demand also recovered as household consumption grew by 3 % y-o-y and fixed investment rose by 6 %. The growth in demand was, however, largely directed to imports rather than domestic production, as the volume of imports grew by over 20 %. Growth in exports, which supports domestic production, slowed considerably from the first quarter. Both the Central Bank of Russia and the economy ministry estimate that GDP growth slowed to around 2 % y-o-y in 3Q17.

CIS countries have had to relax foreign exchange policies in recent years. The currencies of countries in the Commonwealth of Independent States have had to endure severe devaluation pressures, due e.g. to the conflict in Ukraine, sliding oil prices and Russian economic problems that feed through to other CIS economies. This has forced many CIS countries to loosen their currency-steering approaches.

Under the IMF classification, CIS countries with de facto floating exchange rate regimes include Armenia, Georgia, Kazakhstan, Moldova, Russia and Ukraine. Russia is the only one classed as having a free-floating exchange rate (the CBR has refrained from any forex market interventions since summer 2015). The central banks of the other countries occasionally intervene to e.g. mitigate high exchange rate volatility, but do not target a specific exchange rate and they publish information about their interventions. In early September, Uzbekistan also allowed its currency, the som, to float.

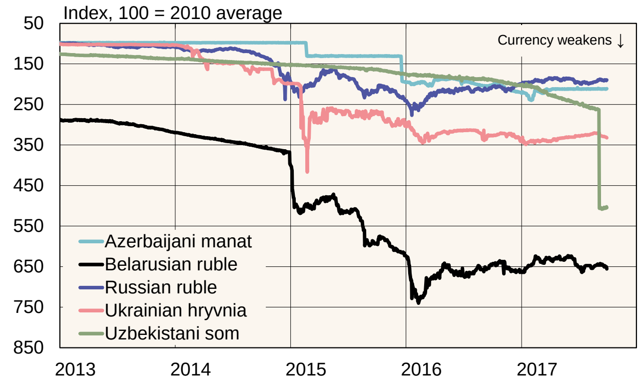
The currencies of Azerbaijan, Belarus, Kyrgyzstan and Tajikistan are not linked to any specific level, but the central banks of these countries seek to smooth fluctuations through interventions. So their regimes are not considered fully floating nor pegs and IMF groups such foreign exchange arrangements under the "other managed arrangement" category. Only Turkmenistan still pursues a pegged exchange rate policy. The Turkmenistani manat is pegged to the US dollar and has held its value stable since devaluation at the end of 2014.

Consolidated budget revenues and expenditures, inflation rate 2012–20 (2017–20 finance ministry estimate)



Source: Finance ministry.

Exchange rates for certain CIS currencies w.r.t. USD



Source: Macrobond.

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China

European Union Chamber of Commerce in China wants to see promised reforms implemented. The European Union Chamber of Commerce in China released its annual position paper last month. The European Chamber expressed satisfaction with the comments of China's leaders with respect to increased openness and the government's calls last January for policies that make it easier for foreign firms to invest in China, offering new incentives for foreign investment, as well as taking steps to create a competitive environment that is fair to both domestic and foreign firms. Despite speeches and policy goals, however, little has been done to translate words into action. The European Chamber's *Business Confidence Survey 2017*, released this summer, found that only 15 % of its member companies expected regulatory barriers to operation in China to decrease over the next five years. The recent OECD survey of openness to foreign investment also ranked China 59th out of 62 countries surveyed.

The European Chamber found that China has reversed direction from opening up its economy in some areas, and expressed concern that the foreign firms are being closed out of certain branches. Among other things, China has introduced rules that favour domestic firms or domestic production, as well as increased trade barriers (e.g. the October tightening of permit requirements for agricultural products and food imports). The government has also purposefully enlarged state-owned firms, which has reduced room for private actors to participate in certain markets. Moreover, China introduced a cybersecurity law in June that has complicated the ability of foreign firms to do business.

While China has offered temporary advantages in selected special economic zones to attract foreign direct investment, the most important changes sought by European firms involve concrete implementation of reforms that improve basic conditions such as predictability of the regulatory environment, transparency and rule of law.

China has the most industrial robots. Data published by the International Federation of Robotics (IFR) at the end of September show that China has surpassed Japan for the top global spot in terms of numbers of industrial robots in service. At the end of 2016, China had 340,000 robots, or nearly a fifth of the world's industrial robots in use.

China has been the world's largest market for new industrial robots since 2013. Last year saw the sale of 87,000 robots, or 30 % of global industrial robot sales. Robot sales increased in China by 27 % y-o-y last year, while robot sales rose by 16 % globally. China's industrial robot market is roughly the same size as that of Europe and North America combined. As a result of extremely rapid automatisation, the electronics industry now rivals the automobile industry in terms of robot purchase, both globally and in China.

China's position for the industrial robot market will only increase in coming years, since China still lags well behind the leading countries (South Korea, Singapore, Germany and Japan) in terms using robots to augment labour. The IFR reports that China's manufacturers are experiencing a rapid shift in terms of the number of robots used per 10,000 workers. For China, that number is only 68 at the moment, compared 631 in Korea and over 300 in Germany and Japan. Use of robots in the car industry everywhere is significantly more extensive than in any other major industrial branch.

Notably, China's significance also is increasing as it develops its own robot production capability. About a third of the robots purchased last year by China's electronics industry came from Chinese robot-makers. China's car industry, in contrast, only bought 13 % of its robots from domestic producers. Chinese firms have ambitions to increase their technical sophistication and market share, which is reflected in acquisitions of foreign robot manufacturers.

China, South Korea, Japan, the US and Germany account for 74 % of the global market for industrial robots. The IFR estimates that global sales of industrial robots will grow at least 18 % this year and by about 15 % a year in 2018–2020.

Chinese tourism continues to grow rapidly; emphasis shifting to domestic tourism. Chinese made 2.5 billion domestic vacation journeys and 60 million holiday trips abroad in the first half of the year. Domestic holiday travel grew by 13 % y-o-y. After years of soaring growth, foreign holiday travel grew by just 5 %, because, even as traveller numbers soar, it is natural that growth in percentage terms slows. Moreover, lower wage growth favours cheaper in-country holidays, but there are also other factors such as fear of terrorism, which have reduced the growth in foreign travel.

The economic impacts of Chinese foreign travel are substantial. Chinese tourists have been the biggest holiday spenders abroad since 2012 compared to tourist groups of other nationalities. The World Tourism Organization reports that Chinese tourists spent 260 billion dollars abroad in 2016, well ahead of the second-place Americans, who spend 120 billion dollars on their travels abroad. A big influence on Chinese spending patterns is that 60 % of foreign travellers fall into the 18–34 age group, and China's younger generations carry fewer stigmas about consuming than their elders. China's tourism spending abroad accounts for nearly 60 % of the annual current account's spending on services. This spending has significantly reduced the country's current account surplus.

This week Chinese spend their annual Golden Week holidays. Some 710 million Chinese (up 10 % from last year) are expected to take holiday trips somewhere inside China. Another 6 million will journey abroad. The record number of travellers has huge economic impacts. Domestic spending on tourism this week is expected to reach 89 billion dollars.

The growth of Chinese visitors to Finland has been staggering. Statistics Finland reports that overnight stays of Chinese tourists in Finnish inns and hotels reached nearly 180,000 in the first seven months of this year, a 46 % increase from the same period in 2016.

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