Weekly Review
8 • 23.2.2018
BOFIT

Russia

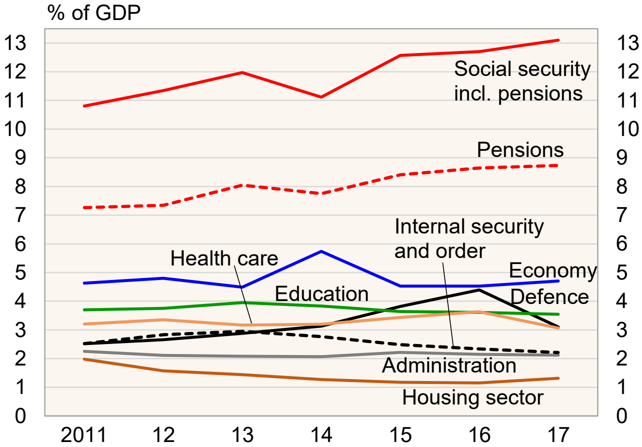
Russia's fiscal sector strengthened in 2017. Consolidated budget revenues (federal, regional and municipal, plus social funds) increased by over 13 % y-o-y. However, 2016 was a low base year whether the funds received from the sale of a stake in the Rosneft oil company are included or not (here not included). Higher oil prices helped increase revenues via oil & gas tax income (up 23 %) whose share rose to close to a fifth of total budget revenues.

Other budget revenues rose by over 10 %, which is rapid even if the data was adjusted for inflation. Revenues from corporate profit taxes and goods excise taxes rose especially fast. Value-added tax revenues provided 17 % of total budget revenues and were up by well over 10 %, reflecting both economic recovery and improved tax collection. Mandatory social taxes on worker wages, which represent 22–23 % of budget revenues, still showed notably strong growth.

Growth in consolidated budget spending accelerated last year to over 6 % (here 2016 spending does not include the large sum granted to defence industry to pay off their bank loans). The growth in social security spending rose to over 10 % and the share increased to over 36 % of total budget spending. Spending on various sectors of the economy increased by over 10 % as spending on transport rose fast. Spending on space activity appears to have tripled and the sub-category of other spending on the economy grew quickly (these two lack further itemisations). After a long decline, spending on the housing sector jumped, mainly on big spending on housing by the City of Moscow.

Spending on education turned to growth, while health care expenditures defied expectations by showing a fall. Spending on public administration rose slightly faster than inflation, excluding a hefty increase in spending on international cooperation. Spending on internal security and order remained flat, while the defence spending category declined.

Largest expenditure items in Russia's consolidated budget, 2011–17



Source: Russian Ministry of Finance.

The revenue bump helped reduce the consolidated budget deficit to around 1.5 % of GDP.

Russian retailer Magnit sold to state-owned bank VTB. Last week businessman Sergei Galitski announced he was selling nearly all his holdings in the company he founded, the retail and supermarket chain Magnit to VTB. Magnit, one of Russia's largest retail chains, has suffered in recent years from the notable contraction in household purchasing power. With its purchase of a 29.1 % stake, VTB will become the company's largest shareholder by far, as majority of the shares are on free float. The reported price of the share package, 138 billion rubles (2 billion euros), implied a small discount. The news surprised the markets, and Magnit's share price fell after the announcement, but have recovered lately.

VTB's purchase decision has caused some head-scratching. Some observers think that VTB may be considering exploiting Magnit's extensive outlet network for its banking services. By some estimates, the purchase of Magnit, which targets lower-income customers, could even be an effort to support government social policy. VTB has also earlier acquired companies outside its core business and it still has a significant stake e.g. in St. Petersburg's Pulkovo International Airport and teleoperator Tele2.

The acquisition has also raised concerns that the government's extensive role in the economy is only getting larger. Unlike in many other branches, the share of state ownership has been small in the Russian retail sector.

Russia loses more educated people than receives. The Gaidar Institute recently published a review on migration of educated people in Russia. Researchers relied on e.g. foreign statistics and survey data as they do not believe Rosstat figures provide a comprehensive picture of the situation. The review does not cover illegal guest workers in the country.

Researchers estimate that roughly 100,000 Russians a year have emigrated to the West in recent years. Some 40 % of them have higher education. Most have left Russia in the face of decaying economic and labour market conditions. The main motive for about a quarter of emigrants, however, is the country's political situation: in particular the geopolitical events of 2014, but also disappointment with the 2012 presidential election. A third of emigrants say they will not return to Russia, while roughly a half are open to the option of returning and the rest are actively planning to move back.

Researchers found that the educational level of people moving to Russia has declined in past decades, and on average immigrants are now less educated than the Russian population. According to survey results only 13–17 % of immigrants had higher or incomplete higher education. Even these people had trouble finding work corresponding to their education in Russia. Russia has tried to attract high-skilled workers through preferences, but after six years of implementation Russia has received only 150,000 high-skilled immigrants.

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China

Big differences in regional economic growth rates. Regional 2017 GDP growth figures for China's provinces range from a decline of 14 % in Inner Mongolia to a rise of nearly 16 % in Shanxi province. In addition to Inner Mongolia (which was revealed to fake its statistics), weakest growth provinces included north-eastern province of Heilongjiang, which is characterized by the agrarian economic structure and low annual household incomes, as well as China's second-least-populous province Qinghai, which is dependent on heavy industry and oil & gas production. Most provinces, however, saw GDP growth above the national average (6.9 %). Highest growth was posted in central provinces. Resource rich Shanxi and Guizhou, industrial Anhui and Shaanxi all saw annual GDP growth above 14 %.

Nominal GDP of Tibet, China's smallest provincial economy, reached 130 billion yuan ($20 billion), roughly the GDP equivalent of Iceland or Cyprus. Some of China's coastal provinces posted huge GDP figures: nearly 9 trillion yuan ($1.4 trillion) for Guangdong and 8.5 trillion yuan ($1.3 trillion) for Jiangsu, putting them on par with economies like South Korea or Russia.

Chinese provincial data should be viewed with some scepticism. Statistical malfeasance has continued to come to light in recent months (BOFIT Weekly 3/2018), indicating that regional administrations are still fudging numbers to meet their hard growth targets. Reported regional GDP in aggregate has typically exceeded the National Bureau of Statistics national GDP figure. However, some regional governments recently lowered their growth targets for 2018. Even if most GDP adjustments are marginal, some are considerable. The port city of Tianjin east of Beijing, for example, conceded it manipulated its data and then lowered its growth target from last year's 8 % to 5 % in 2018.

Northeast China: home to low-growth provinces.

Sources: NBS, Macrobond, Power BI and BOFIT.

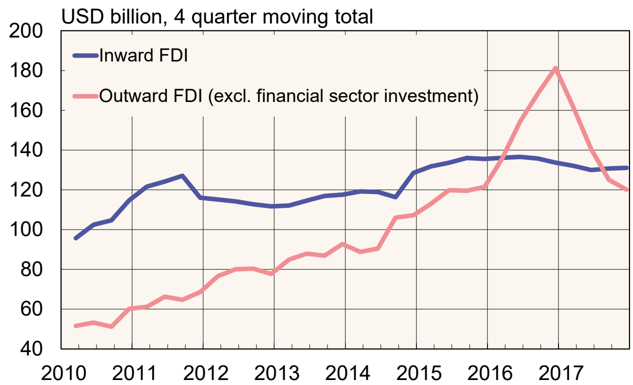
Restrictions diminished outward FDI flows from China last year. China's commerce ministry reports that outbound foreign direct investment from China (excluding the financial sector) fell by a third from 2016 to $120 billion. The commerce ministry figures also showed that inward FDI to China (excl. financial sector) amounted to $131 billion, a slight increase from 2016. Official balance-of-payments figures, which are based on different reporting, however, show outward FDI last year fell by over 50 %.

The drop in FDI outflows from China stems from the crackdown on capital exports that began in late 2016. Guidance published last August (BOFIT Weekly 35/2017) limits investment in branches such as real estate, hotels and entertainment. Another factor is the harsher scrutiny in approval processes for Chinese investment in target countries. As approvals drag on, some Chinese investors give up and go home.

China's official figures fail to give a comprehensive picture of the breakdown of foreign investment by country or by branch. For this reason, several organisations compile their own figures on Chinese investment. These figures, too, note a drop in investment of Chinese firms abroad, especially when ChemChina's massive $43 billion acquisition of the Swiss Syngenta late last year is not included. The investment decline is evident from the Heritage Foundation's China Global Investment Tracker (CGIT) dataset. It suggests that nearly all of last year's drop can be attributed to a decline in Chinese investment in the US. The value of Chinese FDI in the US fell by over 50 % last year compared to 2016. Setting aside the Syngenta deal, Chinese investment in Europe fell by over 10 %. With the Syngenta deal, FDI in Europe rose by 60 %.

The new guidelines give preference to investments under the umbrella of the Silk Road Project, aka the Belt & Road Initiative (BRI). The trade ministry notes that BRI-related investments in all 65 countries aboard in the Silk Road Project, remained at previous year's level in 2017. This is also evident from the CGIT dataset, where BRI investments remain at the $30 billion level of 2016. CGIT data show the largest BRI investments last year went to Singapore and India and that Chinese SOEs are largely responsible for investment. According to the Economist Intelligence Unit, some 50 state enterprises invested in over 1,700 BRI projects in 2014–17.

China's inward and outward FDI flows



Sources: China's Ministry of Commerce and CEIC.

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