Weekly Review
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BOFIT

Russia

Putin wins Russian presidential election as expected. Russia's sitting president garnered 77 % of the national vote last Sunday (Mar. 18), while his regional performances ranged from 65 % in Russia's Far East regions to over 90 % in the republics of Southern Russia. Putin took 71 % of the vote in Moscow and 75 % in St. Petersburg. Voter turnout was nearly 68 %, slightly higher than in the 2012 presidential election.

No major changes are expected for the main lines of economic policy as a result of the election. In principle, the results give the president a strong mandate that could enable realization of difficult, but badly needed, structural reforms of the Russian economy. In reality, most observers expect the administration to interpret the election results as an endorsement of current policies and thus allowing to ignore the reform agenda. The composition of the new government should be announced in early May after Putin's inauguration ceremony.

After the election results became clear, Putin proclaimed that the central issues of his next term would be economic growth and securing the country's defence capabilities. The comments were in line with his platform speech earlier this month. Putin called already last week on the presidential administration to prepare new executive decrees on national goals for the upcoming six years. These included e.g. reducing poverty by half and making Russia the world's fifth-largest economy. Putin issued similar decrees in the beginning of his current term, but most of those goals (e.g. substantial productivity gains and increased job-creation in high-technology sectors) have failed to materialise.

Russian government places two Eurobond issues. Last week the finance ministry placed 11-year and 30-year Eurobond issues worth a total of 4 billion dollars. The 11-year bond carries an initial yield of 4.63 % p.a. while the 30-year bond pays 5.25 %. Most of the money raised from the issue will go to buying back 3.2 billion dollars of state sovereign bonds set to come due in 2030 and carrying a hefty coupon of 7.5 %.

Demand for the new bonds was about double the supply. Finance minister Anton Siluanov said that foreign investors bought most of the debt. The heavy demand for Russian bonds reflects, among other things, their high real yields relative to most sovereign bonds at the moment and the fact that large international institutional investors can again invest in Russian sovereigns with the recent upgrades in Russia's creditworthiness (BOFIT Weekly 9/2018).

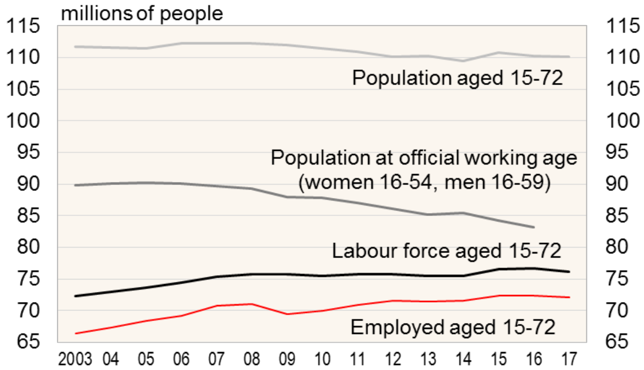
According to CBR estimates, the Russian government owed roughly 55 billion dollars (slightly over 4 % of GDP) in foreign debt at the end of 2017. Of this amount, approximately 15 billion dollars is foreign currency debt, denominated almost entirely in US dollars. The remaining 40 billion dollars consisted of ruble-denominated debt. The 2018 federal budget law reserves the authority for the government to issue about 7 billion dollars in foreign debt.

Number of people employed in Russia declined last year; labour force also shrank. Even as the Russian economy began to revive from recession last year, Rosstat reports that its labour force survey of people aged 15 to 72 years found the number of employed people declined slightly. Their number last year averaged around 72.1 million. A mild drop in employment is fairly unusual during periods of economic growth, even if the same thing happened also during two years in the past. Moreover, the number of unemployed persons fell slightly last year to just under 4 million people, a record low. The unemployment rate was 5.2 % in the labour force formed by 15–72-year-olds (according to Russia's regularly conducted labour survey based on the International Labour Organization's methodology).

Rosstat's monitoring suggests that the decline in the number of employed people may in part stem from the fact that large and mid-sized firms employed more effectively their part-time and temporarily laid-off workers. In a couple of years earlier, the number of part-time workers and those temporarily laid-off increased. Last year their number contracted considerably, while the number of hours worked per worker increased in an exceptional pace. In addition, a slightly larger number than usual of Russia's well over 10 million working pensioners may have ceased working. Since 2016, working pensioners have no longer been eligible for a general inflation adjustment to their pensions if they continue to work.

The reductions in the numbers of both employed and unemployed persons meant a sizeable drop in the labour force last year. While pensioners ending their work naturally exit the labour force, the biggest factor is demography, whereby the working-age population has shrunk continually since around 2005. The employment rate for the working-age population is increasingly harder to raise. Despite the contraction in employment last year, their employment rate was still above 76 %.

Working-age populations, labour force and number of employed, 2003–2017



Source: Rosstat

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China

Yi Gang named PBoC governor. Yi's appointment was announced at the end of the People's National Congress this week. Outgoing People's Bank of China governor Zhou Xiaochuan (70), who was appointed to the central bank governor position in 2012, will now retire. His replacement, Yi (60), has worked at the PBoC since 1997 and served as deputy governor under Zhou for the past ten years. He also led the State Agency of Foreign Exchange (SAFE) in 2009–2016, during which time capital controls were relaxed and the yuan's role as an international currency was strongly promoted. Yi took his PhD in economics at the University of Illinois before moving on to an academic career in the US and elsewhere.

Yi is expected to continue Zhou's reform-minded approach. It should also keep the PBoC at the forefront in implementation of China's economic reforms. Yi has already promised a number new reforms in the near future.

Yi will face numerous challenges during his term as governor. He should use monetary policy to deal with increasing financial market risk and to lower China's indebtedness while he is also expected to provide cheap credit in order to sustain high economic growth. The situation is further complicated by the fact that interest rates should start rising in many countries. China's central bank is moving to an interest-rate-based monetary policy, but interest rates currently only augment the PBoC's otherwise diverse policy toolbox. These tools are applied on a case-by-case basis depending on the particular policy objective and make the whole system quite opaque.

While China says that it is committed to the eventual adoption of a free-floating currency regime and deregulation of capital movements, it still has a long way to go. While China's central bank functions as a part of government and lacks independence, the departing Zhou nevertheless succeeded in gradually opening the Chinese economy to the world and pursued reforms that led to the yuan's incorporation into the IMF's SDR currency basket in 2016. China's enthusiasm for market reform and opening its economy, however, shows signs of fading. Economic opening requires reforms in other parts of the economy, including the banking sector, state-owned enterprises and local government financing.

People's National Congress endorses numerous high-level appointments. Wang Qishan (69), who has spearheaded president Xi Jinping's anti-corruption campaign and has long experience in US-China relations, was elevated to vice president. Premier Li Keqiang (62) was appointed to a second term, while Han Zheng (63), the long-serving party secretary from Shanghai, becomes first vice premier. Other appointees to vice premier posts are Sun Chunlan (67), a former leader of an organisation that aims to increase the influence of the Communist Party in China and elsewhere; Hu Chunhua (54), earlier seen as Xi's possible successor (at least before the abolition of term limits on the Chinese presidency); and Liu He (66), China's "economic architect" and president Xi's chief advisor.

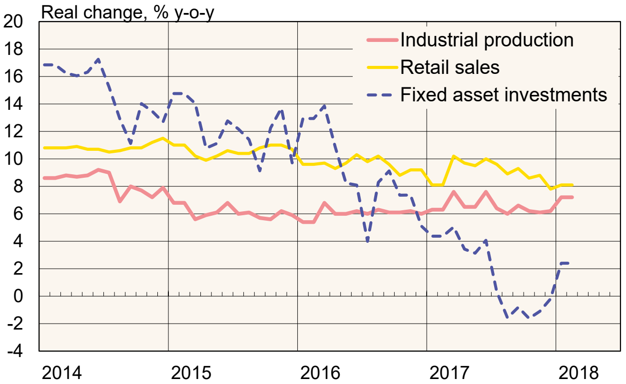
Liu Kun (61), former head of the commission for budget affairs, was named finance minister. Yang Xiadou (64) will head the newly created National Supervision Commission and becomes national anticorruption minister. Wang Yi (64) remains foreign affairs minister, while He Lifeng (63) reprises his role as head of the National Development and Reform Commission. Wei Fenghe (63), a general in the People's Liberation Army, becomes national defence minister. Han Changfu (63) continues as agricultural minister. Environment minister Li Ganjie (53) and natural resources minister Lu Hao (50) represent the young cadre.

Chinese economy powers ahead in first two months of 2018. Real industrial output rose by 7.2 % y-o-y in January-February – the highest January-February industrial output figure since 2014. Fixed asset investment (FAI) in urban areas rose about 8 % y-o-y in nominal terms in January-February, or one percentage point less than in the same period in 2017. On-year real FAI growth was around 2 %, assuming that inflation's impact on January-February investment was slightly lower than in the 4Q17.

Retail sales grew by nearly 10 % y-o-y in nominal terms in the first two months of this year. Online sales were up 37 % y-o-y, with online now accounting for about 15 % of all retail sales of consumer goods. While the nominal growth in retail sales was slightly higher than in the first two months of 2017, higher inflation held real growth to about 8 %.

The rise in consumer prices accelerated in February to 2.9 %, while the January figure was 1.5 %. The Chinese Lunar New Year fell this year in February, causing a rise in prices of certain consumer products. The February core inflation reading, which excludes food and energy prices, rose by 0.5 percentage points from January to 2.5 %. Producer price inflation continued to cool, falling from 4.3 % in January to 3.7 % in February. On-year growth in producer prices slightly exceeded 6 % on average for months in 2017.

Chinese industrial output, retail sales and fixed investment*



** January-February 2018 investment trend based on price estimate*
Sources: Macrobond, CEIC, BOFIT.

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