Weekly Review
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BOFIT

Russia

Dry summer reduces Russian harvest. Data from the beginning of November show Russia's grain harvest this year was about 15 % smaller than last year. Last year's harvest, however, was exceptionally large due to favourable summer grain-growing conditions. Compared to 2016, this year's harvest was only a few per cent smaller. The sugar beet crop was about 10 % smaller than last year, while potato and other vegetable crops matched 2017 levels.

The area of land under cultivation has expanded in recent years, but arable land is unevenly distributed across Russia. Wheat and sugar beet cultivation is concentrated in the steppe that stretches from the Black Sea to Siberia, while potato and rye cultivation succeeds at more northern latitudes. Also crop composition has changed since the breakup of the Soviet Union with the traditional rye and buckwheat crops replaced increasingly by maize and wheat. In terms of weight, two-thirds of Russia's grain crop is now wheat. Wheat is exported especially to countries in the Middle East.

The size of harvests impacts food prices and thus the general price level. Foodstuffs represent 37 % of Russia's consumer goods basket used for price indexing. Compared to many other countries, this is a large share. Thus, the large harvest last autumn slowed down slightly the rise in consumer prices during last winter and spring. Accordingly, this year's smaller autumn harvest can be expected to slightly accelerate inflation over coming months.

Robust increase in Russian government revenues, substantial budget surpluses. Revenues to the consolidated budget (federal, regional and local budgets, plus government social funds) in the first nine months of this year were up 20 % from the same period in 2017. Oil & gas tax revenues were up by nearly 50 %, and rose even faster in the third quarter on quite high oil prices.

Other revenue streams to the consolidated budget rose by 13 % y-o-y in January-September. While value-added taxes and corporate profit taxes boosted budget revenues remarkably, revenue streams from mandatory social taxes of employers and labour income taxes were up well over 10 %.

Budget expenditures, in contrast, have only risen modestly, up by just 6 % y-o-y in January-September. Healthcare spending topped the increase, rising by nearly 20 %, followed by education at more than 10 %. The increases mainly reflect substantial hikes in wages in these sectors. Spending on administration turned to hefty increase, while spending on domestic security was up by a few per cent. Growth in defence spending strengthened to over 7 %. Budget categories this year seeing increases of only about 1 % (i.e. real declines) include the economy's various sectors, and pensions and other forms of social support.

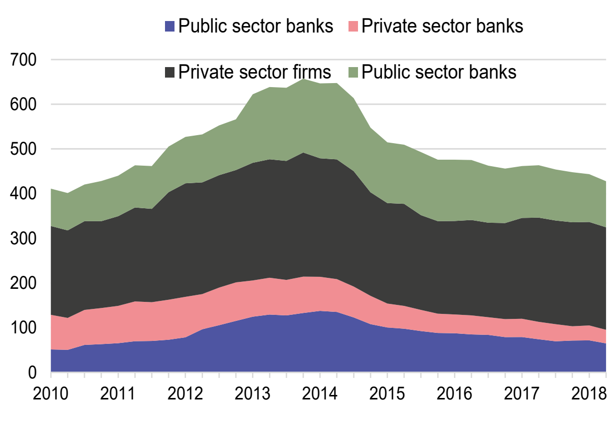
The rapid growth in revenues has turned Russia's government finances to surpluses. The 12-month surplus of the consolidated budget exceeded 1.5 % of GDP in September. The finance ministry expects the federal budget surplus to end up at about this level for the whole of this year even if the newly-approved supplemental budget spending (rather small) for this year will materialize and the large remaining amounts of last year's budget funds will all be used.

A fifth of foreign debt of Russian banks and other businesses denominated in rubles. The Central Bank of Russia reports that the total foreign debt of Russian banks and other Russian corporations stood at around 428 billion dollars as of end-June. Some 21 % of that debt was denominated in rubles, 57 % in dollars and about 20 % in euros.

The banking sector's foreign debt has contracted continuously since spring 2014. Bank foreign debt, which declined by 114 billion dollars over the past four years, stood at 95 billion dollars as of end-June. The foreign debt of state-owned banks, in particular, contracted dramatically. Some of the debt reduction reflects exchange rate fluctuations, but differences between banking groups are also substantial. About 30 % of the foreign debt of private banks is denominated in rubles. In contrast, only about 15 % of the foreign debt of large state-owned banks is in rubles. The foreign receivables of banks have also fallen, but still considerably exceed bank debt loads.

The foreign debt of non-financial corporations has contracted over the past four years. At the same time, the share of debt liabilities to direct investors in corporate sector's total foreign debt has constantly increased. In June the share was over 40 %. About a third of corporate credit stock (103 billion dollars) was large state-owned enterprise debt. When liabilities to direct investors are excluded, only 5 % of foreign borrowing of state-owned enterprises is denominated in rubles. In contrast, about 30 % of the foreign borrowing of private firms is in rubles. Not counting the debt and receivables associated with direct investment, the value of the foreign net assets of the non-banking corporate sector was close to zero.

Total foreign debt of banks and other firms, USD billion



Source: Central Bank of Russia.

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China

EU steps up oversight of investment inflows from China. The EU Parliament, the Council and the Commission last week (Nov. 20) reached agreement on monitoring mechanisms for foreign direct investment flows into the EU. The EU wants to assure that FDI in critical infrastructure and technology do not imperil the EU's internal or external security.

The EU has sought tighter supervision of direct investment for years. While the new EU policy does not mention China specifically, the accord has been driven by fears that Chinese state-owned enterprises could target European firms involved in infrastructure and technology. Concerns over possible media ownership and influence over domestic policies have been also expressed.

The new regulations, which still require formal approval by EU bodies, are expected to enter into force in 2020. Half of the EU's 28 member states currently have some sort of FDI monitoring arrangements to assess possible security threats. The new arrangement does not move decision-making on FDI away from the national level, but rather seeks to increase oversight of FDI through coordination and information-sharing among member states. It also gives the European Commission the possibility voicing its position on major investment projects that are important for the Union.

While the views of the member states on Chinese investments differ, the general attitude also in Europe has become more critical. The German government, for example, last summer in practice torpedoed an effort by the Chinese Yantai to purchase German machine tool maker Leifeld.

US scepticism towards FDI, particularly deals involving the Chinese, has garnered far more attention than in the EU. The Committee on Foreign Investment in the United States (CFIUS) recently expanded its mandate to protect 27 strategic industries. Many other large countries have also increased scrutiny of foreign investments.

Labour strife on the rise in China. The Hong Kong-based China Labour Bulletin (CLB), an NGO that tracks the worker's movement in China, reports a sharp increase in labour disputes this year. Most protests have involved wage arrears.

According to the register maintained by CLB, about 1,150 protests over wage arrears were staged in the first ten months of this year. There were 813 protests in the same period last year. The record year was 2016, when 1,700 workplace disputes were registered over wage arrears.

As in previous years, the bulk of protests have been in the construction sector, which typically uses internal migrant workers from rural areas. Teachers, however, have staged the largest demonstration this year. Over 10,000 teachers took to the streets in Harbin in northeastern China to demand better pension payments.

Labour action has also been supported by Chinese universities, which students have helped to organise labour protests on behalf of workers. Media reports claim that the police have this year arrested dozens of student activists from China's top-tier universities. Officials monitor student movements extremely closely, well aware of the lessons from the 1989 Tiananmen protests.

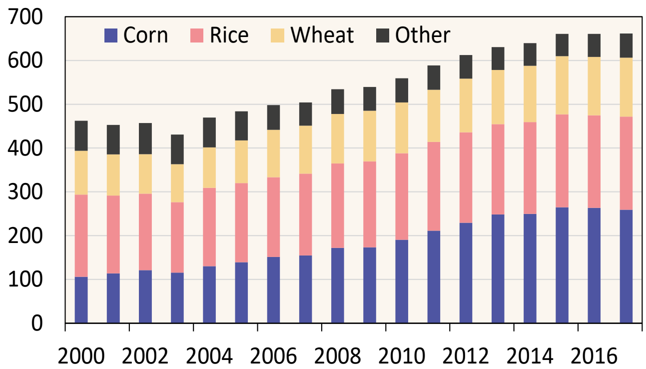
China enjoys another year of bountiful harvests. China's National Bureau of Statistics reports that this year's summer harvests (139 million metric tons) roughly match the scale of last year's bumper harvests. The summer harvests represent about a fifth of China's total harvests for the year. Although the autumn harvest figures have yet to be published, they are expected to be similar to last year's harvest numbers.

China's annual grain harvest in recent years has hovered around 660 million tons. After the 2003 crop failure, harvests grew quickly to current levels. Much of the improvement reflects higher productivity, but the area of land under cultivation has also increased. Production efficiency has been boosted through improvements in irrigation and fertiliser use, as well as a shift to higher-yield cultivars. The use of modern farm equipment has also increased.

Like other statistical data in China, agricultural figures should be viewed critically. A good example is the NBS' large upwards revisions this autumn of its figures for grain harvests and land under cultivation for the period 2007–2017. New figures show maize production last year exceeded previous estimates by whopping 43 million tons. The revision is huge; it boosts Chinese maize production by 20 % and global production by 4 %. The sizes of the wheat and rice harvests were also understated previously by several million tons.

China strives for self-sufficiency in certain major crops. It supports producers of critical crops through such measures as price guarantees. In the case of maize, a very costly price-guarantee subsidy was dropped in 2016. In 2017–18, the sell-off of state maize reserves purchased at the guaranteed price is estimated to have cost the government nearly 30 billion dollars. Rice and wheat still enjoy price guarantees.

Chinese grain harvests (millions of tons)



Sources: China National Bureau of Statistics, CEIC and BOFIT.

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