

Russia

Direct investment outflows from Russia remain significantly larger than FDI inflows. Flows of direct investment to and from Russia's non-bank corporate sector have been smaller over the past five years than earlier. This concerns inbound FDI to Russia especially, even though they rose temporarily due to two individual relatively massive investment operations in the period (the ownership restructuring of the TNK-BP joint venture between the Russian state oil giant Rosneft and BP in 2013, and the sale of a large stake in Rosneft to foreign investors in 2016). FDI flows into Russia's corporate sector over the past decade have almost continuously been smaller than FDI outflows from the Russian corporate sector.

As in previous years, most 2018 FDI inflows to Russia's corporate sector were reinvested profits. Intragroup credit between parent and subsidiary companies became a popular practice a decade ago to bring capital into Russia but that has shifted in recent years to a slight drain of capital out of the country. Owning more equity in Russia has not been quite appealing: net inflows of inward share capital (excluding Rosneft arrangements) have been small over the past ten years. Last year even saw the situation where that net flow was an exceptionally large negative. This could also be seen in the fact that, for the past couple of years, foreign companies launched fewer new firms in Russia than earlier and the number of closures of established foreign firms in Russia rose.

The types of finance in Russia's corporate sector FDI outflows, in contrast, remained quite diverse. Reinvestment of profits has stayed popular, while investment in share capital and lending by Russian parent companies to their foreign subsidiaries also retained their roles.

The direction of the small FDI flows involving the banking sector have almost constantly been into Russia rather than out. FDI inflows to the Russian banking sector for many years have almost entirely consisted of reinvested profits. Most FDI outflows from the Russian banking sector have been made in the form of share capital.

Inward and outward direct investment flows, 2007–2018



Source: Rosstat.

Revenue boom of Russian federal budget begins to normalise. After climbing by nearly 30 % last year in nominal terms, budget revenues rose another 13 % y-o-y in the first quarter of this year. Revenues from oil & gas taxes increased by 7 % after rising by about 50 % last year. Other budget revenues increased at about the earlier rate of over 15 %. A similar pace of growth was seen in VAT revenues. The impact on budget revenues from the VAT increases of January 1, 2019 is still ahead as VAT is paid with a quarter's delay.

Growth in federal budget spending accelerated from last year to over 8 %, which is the pace budgeted for this year. Defence spending increased by 13 % y-o-y in the first quarter. The budget surplus for the last twelve months still corresponded to 2.8 % of GDP.

Russian spending on private insurance increases.

The Central Bank of Russia reports that in 2018 Russians paid a total of 1.48 trillion rubles (20 billion euros) for various types insurance (excluding mandatory insurance policies for healthcare and pensions), which works out to about 10,000 rubles (140 euros) per capita. The insurance market saw nominal overall growth of 16 % between 2017 and 2018. Growth has been rapid even if we take into account inflation of about 5 % a year. Even so, Russia's insurance market is still rather small relative to most advanced economies.

About 30 % of insurance payments go to life insurance. Health, accident and prescription drug insurance account for another 20 % combined, while car insurance is about 30 %. The rise of life insurance in recent years has made up for the downturn in premia paid on other types of policies (though other insurance categories also grew last year). Russia's pension system and healthcare system are funded through mandatory contributions, so the role of private insurance is supplemental. Private life insurance policies represent a small share of pension insurance, and only a small slice of the Russian population purchases supplemental health insurance.

Life insurance has been the strongest growth category in the insurance sector. During 2016 and 2017, the total amount of life insurance premia collected increased at a pace of over 50 % a year, and last year grew by yet another 30 %. The central bank, which is responsible for supervision of Russia's financial markets, also intervened this year to regulate the life insurance business. New guidance that entered into force this month requires insurance companies to better inform their clients of the terms of life insurance policies and ensure that the policies fit the needs of their clients. The Central Bank pays special attention to the clarity of payout conditions and amounts.

At the end of 2018, there were 275 companies operating in Russia's insurance markets. About 200 were companies, 12 mutual insurance groups and the rest insurance brokers. The number of operating licences declined, but the drop was due more to voluntary relinquishing of operating licences than official action. In contrast, the Central Bank has had few qualms about revoking banking licences lately. It has been responsible for oversight of insurance companies since 2014.

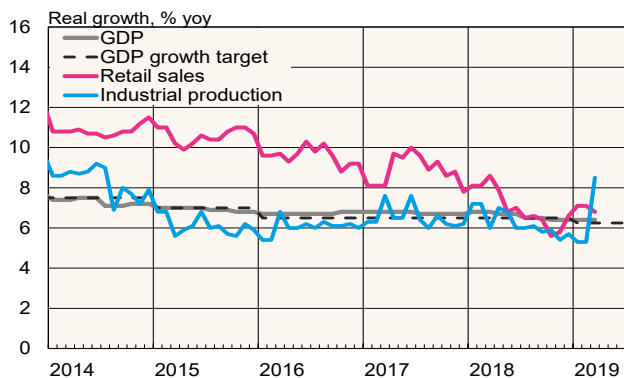
China

Despite monthly fluctuations, China's official GDP growth numbers remain remarkably steady. China's National Bureau of Statistics reports that economic output increased by 6.4 % y-o-y in the first quarter of 2019, matching the growth pace of the previous quarter. The official GDP growth figure was higher than expected in light of weak indicator readings in January and February, and despite the anticipated growth gains of March. The extreme consistency of official GDP growth is less a reflection of actual economic trends than a showing that official growth targets are met.

The NBS also reports that March industrial output grew by 8.5 % y-o-y, well outpacing growth just over 5 % in January and February. While the revival in industrial output was broad-based, stand-out growth performances were seen in export branches such as equipment manufacture, electronics and textiles. The revival was not reflected in domestic consumption. Retail sales in real terms in March grew by less than 7 % y-o-y.

Consumer price inflation accelerated from 1.5 % in February to 2.3 % in March, mainly on higher food prices. The rise in producer prices also picked up from 0.1 % in January and February to 0.4 % in March.

GDP, retail sales and industrial output



Sources: Macrobond, CEIC and BOFIT.

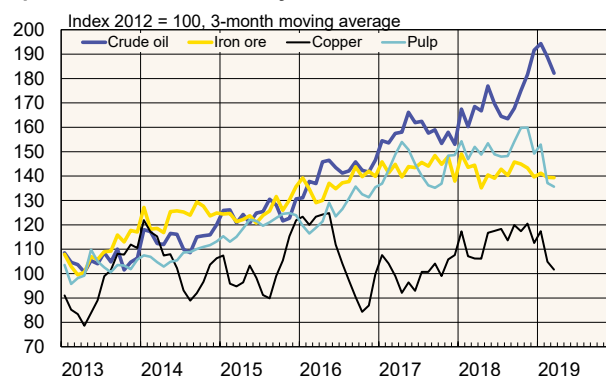
China's exports revived in March, while imports continued to contract. The value of Chinese exports in the first three months of this year (USD 552 bn) represented an increase of just over 1 % from a year earlier, even if on-year growth in March accelerated to 14 %. The value of imports (USD 475 bn) declined in 1Q19 by 5 % y-o-y. March imports were down by nearly 8 %. The first-quarter goods trade surplus was 76 billion dollars, up from 45 billion dollars in 1Q2018.

The revival of on-year growth in exports in March was driven by demand in EU markets (up 24 %), but strong growth was also registered elsewhere. Exports to the US in March were up 4 % y-o-y.

China's slack demand for imports reflects persisting weakness in domestic demand. In March, imports from the EU fell by 5 % y-o-y while imports from the US were down by more

than 25 %. Also imports from Japan, South Korea and Taiwan plunged. In addition to imports of finished goods from above mentioned countries, the volume of many key commodity imports have recently been in decline.

Import volumes of select key commodities to China



Source: CEIC.

China's capital flows were nearly in balance last year.

Balance-of-payments figures for 2018 show a small current account surplus and a surplus in the financial account. FDI inflows to China amounted to 204 billion dollars, while outflows from China were 97 billion dollars. Foreign portfolio investment in China was up sharply from 2016 and 2017, while Chinese portfolio investment abroad declined significantly.

Market reforms in recent years have largely sought to attract financing to China. Regulation of direct investment of Chinese firms abroad has been tightened and possibilities for portfolio investment outside China has been restricted. For example, only the investment channel to mainland China has been opened for bond investment under the Bond Connect programme launched in 2017. The channel for Chinese investors to invest in the Hong Kong bond market remains closed.

However, the negative number in the "net errors and omissions" item suggests larger capital outflows than the recorded flows indicate. The net errors item, which has been negative for the past decade, mainly reflects unspecified capital flows. When the net errors item is included, China's balance of payments was roughly in balance last year and its foreign currency reserves increased only by 19 billion dollars.

China's balance-of-payments highlights, USD billion

	2015	2016	2017	2018
Current account	304	202	195	49
Goods trade	576	489	476	395
Services trade	-218	-233	-259	-292
Other items	-54	-54	-22	-54
Capital and financial account	-434	-416	109	130
Direct investment	68	-42	28	107
Portfolio investment	-66	-52	29	107
Other items	-436	-322	52	-84
Net errors & omissions	-213	-229	-213	-160
Change in reserves	-343	-444	92	19

Source: SAFE.