

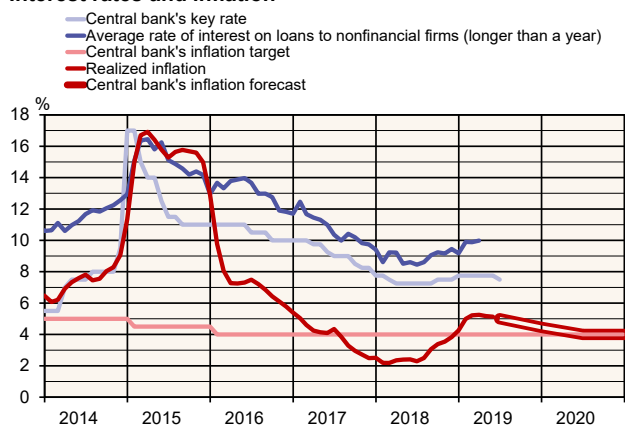
Russia

Central Bank of Russia lowers key rate. On June 14, the Central Bank of Russia, as markets anticipated, lowered the key rate by 25 basis points. The key rate is now 7.5 %. The CBR said their decision reflected slowing annual inflation and tepid economic growth in the first half of the year.

Annual inflation peaked in March at a rate of 5.3 %, and annual consumer price growth reached an estimated 5 % at the beginning of June. Ruble appreciation (up 8 % against the dollar since the start of the year) and slowing growth in retail sales contributed to slowing inflation. The CBR also noted that the pass-through of the VAT hike at the start of the year has been transferred to consumer prices. The central bank now forecasts 12-month inflation slowing further to a range of 4.2–4.7 % (reduced from the earlier forecast of 4.7–5.2 %) at the end of 2019. In 2020 and 2021, annual inflation is expected to remain close to 4 %.

The weaker-than-expected economic data early in the year ([BOFIT Weekly 21/2019](#)) also have caused the CBR to slightly cut its GDP growth forecast for this year. The updated forecast reduces the growth outlook from a range of 1.2–1.7 % to 1–1.5 %. Government investment projects, however, might return growth to a level of 2–3 % in 2021. The CBR did not rule out the possibility of a further rate cut at one of the upcoming board of directors' meetings.

Interest rates and inflation



Source: Macrobond.

Rapid expansion of Russian consumer borrowing raises concerns. Preliminary data released by the CBR show that on-year growth in the stock of credit granted to households accelerated in the first four months of this year. The credit stock, which grew at less than 20 % y-o-y in spring 2018, increased by 24 % y-o-y this April.

The acceleration in growth of unsecured consumer credit to its current pace of over 25 % y-o-y is seen as a particular cause for concern. Nominal wages in Russia are only rising at about 7 % y-o-y and real incomes continue to shrink. Consumer loans represent about half of household borrowing.

The CBR has sought to moderate credit growth by e.g. though several hikes in the risk ratio buffers for unsecured credit and by announcing its willingness to increase requirements further if needed. From the beginning of October, banks granting new loans will have to determine the debt burden ratio on each loan applicant (ratio of total credit-servicing costs to the previous year's average monthly earnings).

The growth in housing loans is seen as less of a cause for worry than that of consumer loans, but the increasing loan-to-value ratios (ratio of mortgage amount to appraised value of property) have raised some questions. At the beginning of January, the CBR increased risk ratio buffers for highest-risk housing loans (loan-to-value ratios above 80 %), thereby slightly increasing interest rate on these loans. The loan-to-value ratio for about 40 % of housing loans granted during the first months of this year exceeded 80 %. At the same time, the average size of a housing loan has risen. Approximately 400,000 new housing loans were granted in January-April, which was slightly fewer than in the same period in 2018. The average interest rate on new housing loans is currently just under 10 %.

Less than 1 % of household loans are denominated in foreign currency. About 20 % of household deposits are in foreign currency.

Household borrowing and deposits

	3/2019	3/2018	3/2019
	RUB billion	12-month change, %	
Loan stock	15846	17 %	24 %
Housing loans	6909	3 %	21 %
Consumer loans	7702	15 %	24 %
Deposits	28810	10 %	8 %

Source: Central Bank of Russia.

Russia's labour force shrinks along with unemployment. Rosstat's latest labour market survey, which is based on the methodology of the International Labour Organization (ILO), finds that the employed population (aged 15–72 years) fell by about 1 % y-o-y in the first quarter of this year. The contraction in the number of unemployed is now in its third year.

In the four-quarter period from April 2018 to March 2019, the employed population averaged just over 72 million, while number of unemployed averaged 3.6 million. After several years of increase, the employment rate fell slightly this year to 65.4 %. The unemployment rate fell to 4.7 %.

The size of Russia's total labour force, which includes both employed and unemployed workers, witnessed an unusually large decline this year. At the same time, the number of persons outside the labour force increased. The increase is due almost entirely to the over 1 million persons in potential labour force, i.e. not actively seeking work, but who would like to have a job.

China

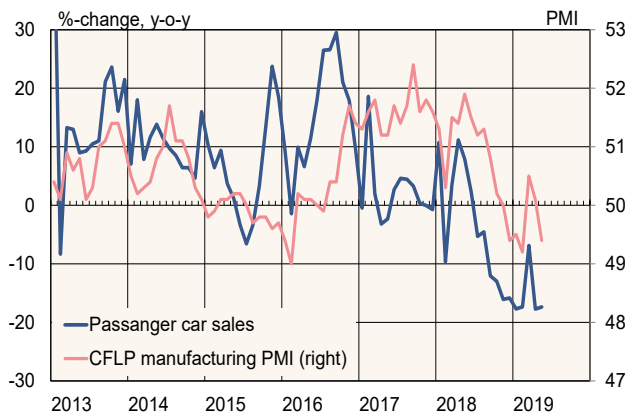
Chinese May industrial output growth low by historical standards. The China National Bureau of Statistics reports that the country's on-year growth in real industrial output slowed from 5.4 % y-o-y in April to 5 % in May. If the exceptional figures occasionally posted during the January-February Lunar New Year festivities are excluded, China has not officially announced such low growth since the early 1990s.

While China's official figures leave much to be desired, it is notable that industrial output growth in the first five months of this year averaged just 5.9 %, which was about 1 percentage point lower than a year ago. According to the main purchasing manager indices (PMI), industrial output in May was essentially unchanged from April.

China's car industry, once a major driver of economic growth, has seen its value-added trend decline in recent months (down by 5 % in May). The China Association of Automobile Manufacturers reports that over the past 12 months fewer than 22 million passenger cars have been built domestically, a decline of 13 % from last year. May output was down 24 % from May 2018. There is no quick fix for the car industry. The leading finance magazine *Caixin* reports that the central government does not intend to provide special subsidies to carmakers as earlier planned. Manufacturers also have to unload 3 million cars in inventory built to old emission standards before the new standards enter into force next summer.

Chinese growth continues to rely increasingly on growth in the service sector. Real growth in retail sales picked up from 5.1 % in April to 6.4 % in May. Real growth in retail sales in the first five months of this year was just 6.4 %, however, down from over 8 % in the same period a year earlier. The various purchasing manager indices showed that production of services continued to enjoy robust growth, but indicated no further acceleration in growth.

Monthly car sales and manufacturing PMI readings in China



Sources: CEIC, CAAM, CFLP.

China suspended its market economy status challenge at WTO. This month, the World Trade Organization (WTO) approved China's request submitted in May to suspend its complaint in a dispute raised with the EU over how import prices of Chinese products were determined in dumping cases. In practice, the complaint was intended to force the WTO to determine whether China meets the criteria for recognition as a market economy.

China asserts that its 2001 WTO accession agreement automatically conferred market-economy status after 15 years of WTO membership. Such status affects how and whether anti-dumping tariffs can be imposed on Chinese products. The dispute has been pending at the WTO since 2016.

The EU and the US dispute the Chinese interpretation. They say that the low pricing of many Chinese products continues to be based on large public subsidies, so the EU and US have used pricing in third countries with efficient markets to reveal evidence of price dumping in Chinese products. This evidence has been used by the EU and US to impose anti-dumping tariffs on Chinese products, and thereby supported the price competitiveness of their own companies.

A number of different sources report that China has requested that petition be withdrawn after it became apparent that the WTO was ready to issue a negative ruling. China's similar claim against the US is also expected to be dropped.

Hong Kong rocked economically and politically by mainland moves. The Hong Kong Census and Statistics Department reports that the special administrative region's GDP grew by just 0.6 % y-o-y in the first quarter of this year, the lowest growth pace since the 2009 financial crisis. Growth in private consumption was negligible, while investment in construction and machinery & equipment contracted. Foreign trade goods exports began to fall and growth in services exports slowed to around 1 % y-o-y. Imports of goods and services also contracted. Economic trends remained generally weak in April.

For Hong Kong, a small open economy, mainland China has huge economic importance. The movement of goods, services, people and money between the special administrative region and the mainland is quite lively. The slowdown in Hong Kong's economic growth also reflects weakness in the mainland China economy. Trade war, heightened protectionism and slowing growth in world trade also have diminished the region's economic growth.

When the UK surrendered control over Hong Kong to China in 1997, the parties agreed, among other things, that Hong Kong's economic system and constitution would remain in place until at least 2047. In recent years, however, China has tightened its grip on Hong Kong. The mass protests of recent weeks reflect dissatisfaction with this trend. The regional government postponed a change in the law that would make it easier to extradite a person accused of a crime to mainland China, but protestors continue to demand that the proposed law never be enacted and that Hong Kong's chief executive Carrie Lam step down.