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Russia

Medvedev reiterates reform goals at the St. Petersburg International Economic Forum. At last week's annual economic forum, which has become an important international PR event for the Russian economy, president Dmitri Medvedev again stressed the necessity of modernising Russia's economy.

Medvedev suggested a number of concrete measures to improve the investment climate and business environment. One proposal was to expand divestment of state assets and increase the number of state firms listed last autumn in the government's sales programme. Under last year's plan, in large companies only minority stakes would be sold; now Medvedev suggested majority stakes should also be available. Implementation of the programme approved last year has been slow, due e.g. to the fact that it takes time to get many of these firms in shape for sale. The Federal Agency for State Property Management, which handles sales of state assets, has also been accused of dragging its feet.

Medvedev said more power needs to be transferred from the federal level to regional and local administrations particularly in economic matters. Russia is simply too big to be administered from one place. His proposal reverses policies of the 2000s, when decision-making power was taken from the hands of regional and local administrators.

A lawyer himself, the president noted the court system remains in dire need of reform, so e.g. specialisation of judges must be encouraged, the process for picking judges needs to change and more effective disciplinary measures must be developed. The fight against corruption must be strengthened e.g. by making it easier to sack corrupt officials and fully disgorge their illegal gains.

He said efforts to transform Moscow into an international financial hub should continue, pointing out that major legislation on the financial sector was being drafted. While many experts consider the notion of Moscow as an international financial centre far-fetched, the plan seems to serve as an impetus to bring about important legislative initiatives. The legislation under preparation includes improvements in the status of minority shareholders through better access to financial information and better reporting requirements for substantial changes in a company's ownership structure. Preparations for merger of Moscow's RTS and the MICEX securities exchanges are currently underway. In conjunction with that a single national securities depository and clearing centre is being created; a move most welcome to foreign investors.

The president promised that visa rules for foreign investors and businesspersons involved in large-scale business in Russia would be eased – a move that would indicate a significant shift in Russian visa policies.

The president proposed that the area of the City of Moscow be expanded and that federal administration offices downtown be transferred to new areas on the outskirts of the city to open up the centre to other activities and reduce traffic congestion.

Medvedev has over the past few years repeatedly pushed for action to improve the operating environment for firms, but often with little impact. However, progress on certain concrete questions seems to be happening. For example, he ordered in March that state representatives be replaced by experts on the boards of state-owned firms. This has meant that many ministers and high-level officials have had to give up their seats on boards of major state firms. The shake-up should be complete by the end of September.

Decision taken on reducing social security contributions. At the St. Petersburg economic forum, president Medvedev announced that he had reached agreement with the government on reducing the mandatory social security contributions of firms from the start of 2012.

After an intricate process (see BOFIT Weekly 23/2011), a compromise was agreed whereby the basic social security contribution rate would fall from the current 34 % to 30 %. For small businesses not involved in retailing, the social security contribution would fall to 20 %. The current rates for employer social security contributions entered into force at the start of this year.

How will Russians vacation this summer? According to the annual poll conducted by the Levada-Center research institute, 46 % of respondents said they expect to spend their summer holidays at home this year. Of those, 40 % will stay home because they lack the resources to travel anywhere. The share of Russians taking "staycations" has declined steadily throughout the 2000s; in 2000, 68 % of respondents planned to spend summer at home.

Approximately one in four Russians spends their summer vacations at their summer house or farm plot. The *dacha* is not merely a holiday destination, but crucial to the household economy as Russians actively cultivate vegetables and fruits, as well as harvest forest treats like mushrooms and berries in conjunction with summer-house living. For part of the Russian population, produce from tiny farm plots makes an important contribution to the household food supply.

6 % of respondents said they would be vacationing in states of the former Soviet Union (including the Baltics), and 3 % would be visiting non-FSU countries.

Rosstat reports that for all of 2010, Russians made a total of nearly 13 million vacation trips to non-FSU countries. The number of travellers has nearly doubled since 2004, when statistical records of tourist travel began to be kept. The favourite destinations of Russian tourists are Turkey and Egypt.

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China

Chinese stock markets continue their slide; interest rates are in rise. After small gains in the first three months of 2011, Chinese share prices have declined since April. Share prices on the Shanghai exchange this week were off 13–14 % from their April highs. The price-to-earnings ratio (P/E) on the Shanghai exchange for A-shares (aimed at domestic investors) is currently about 16. On the Shenzhen stock exchange, which is geared to shares of smaller firms, the average P/E is about 29.

Prices on China's stock exchanges reflect a set of global shocks, including the ongoing fiscal problems in Europe, a slowdown in the US economic recovery and Japan's post-earthquake challenges. Share prices in China have also been depressed by monetary measures to restrain inflation and expectations of an impending economic slowdown. Share prices have been pushed down further by worries over the real estate sector that could have profound impact on the banking sector.

In recent days, money market rates have risen sharply as banks prepare to meet their mandatory end-quarter reserve requirements. At the beginning of the week, the reserve requirement for banks was increased by 0.5 percentage points. The reserve requirement for China's large banks now stands at 21.5 % of deposits.

Key share indexes for China, Russia and emerging markets, January 2007=100

Sources: Bloomberg, BOFIT

Rules further relaxed on travel from mainland China to Taiwan. Progress was made in normalising relations at the third Straits Forum in Xiamen. On June 28, mainland China and Taiwan will launch a pilot travel program allowing mainland tourists to visit Taiwan individually. Travel to Taiwan was earlier only possible for mainland Chinese in group package tours arranged by travel agencies. Direct flights between the mainland and Taiwan will be increased and air traffic expanded to include several new cities.

Relations between Taiwan and the mainland have improved gradually since 2008, when Taiwan's president Ma Ying-jeou took office. Direct flights between Taiwan and the mainland were introduced in 2008, and travel from the mainland to Taiwan has boomed ever since. News of eased travel rules was welcomed by Taiwan's service sector; measured by tourist arrivals, mainland Chinese last year surpassed the Japanese as Taiwan's top tourist group. Taiwan statistics suggest that about 1.6 million mainland Chinese travelled to Taiwan last year, a third of total tourist traffic. In 2009, about a fifth of tourists visiting Taiwan came from mainland China.

China imposes tighter rules on exports of rare earth metals, prices soar. At the end of May, China's commerce ministry and the government announced to tighten their control over the rare earth element (REE) metals by expanding the export quota system and applying higher taxes on crucial minerals needed in many high-tech products. The government has prepared guidelines aimed at concentrating over the next two years some 80 % of heavy rare earth production in southern China under three largest Chinese companies. In addition, mining permits will be limited, especially in areas designated by the state as national strategic reserves. Officials justified the move on environmental grounds, but the aim is also to rein in overproduction and illegal sales.

Since the Chinese government's announcement, prices of several REEs have more than doubled on the Shanghai commodity exchange. The rise in REE prices is expected to continue if China further reduces export quotas.

China's demand for REEs is expected to soar, due to e.g. the massive rollout of electrified transport systems and investment in wind power. China has sought to meet demand by limiting its rare earth exports. China produced 119,900 tons of rare earth metals in 2010, with some 40,000 tons going to export. This year's REE production has been limited to 93,800 tons and export quotas in the first half of the year have been limited to 14,500, a 35 % reduction from last year. At the moment, no nation has filed complaints with the World Trade Organization (WTO) on China's decision to limit exports.

In January-May, exports of rare earth metals climbed 26 % y-o-y to 23,740 tons, indicating that China, once again, cannot hold its own export quota this year. While China only has about a third of the world's known REE reserves, it presently accounts for 97 % of production. With global demand well exceeding China's export quotas, smuggling has become a serious issue for China. Annual smuggling levels are estimated to have reached 10,000 tons, which is a great amount compared to the total export. The shortfall in supply is expected to last through 2013 while mines in the West come on stream. At that point, China's production share is estimated to fall to around 60 % of world production.

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