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Russia

Forecasters expect Russian economic growth to pick up this year and next. The latest Rosstat figures show GDP grew 1.3 % last year. Most 2014 GDP growth forecasts fall into the 2–2.5 % range, although they vary from 1 % to 3 %. Growth is expected to accelerate slightly in 2015 and 2016.

Economic growth would still be based to a large extent on private consumption. The growth in consumption is expected to slow from 4.7 % last year but most forecasters see consumption rising still 3.5–4 % this year.

Uncertainty about developments internationally and in Russia has meant that fixed capital investment forecasts are quite varied. After last year's zero growth, fixed investment this year is generally expected to grow a couple of per cent. Some forecasting institutions, however, expect investment will stagnate also this year. Investment growth would improve in 2015.

Selection of Russian GDP growth forecasts, % change

	2014	2015	2016	Released
IMF	2.0	2.5		1/14
World Bank	2.2	2.7		1/14
OECD	2.3	2.9		1/14
UN/DESA	2.9	3.6		1/14
EBRD	2.5			1/14
Citibank	2.6	2.7	2.9	1/14
Consensus Economics	2.2	2.6		1/14
Interfax Consensus	1.3	2.3		1/14
J.P.Morgan	1.8	2.5		1/14
Alfa Bank	1.0	1.4		1/14
Sberbank Investment Research	2.3			1/14
Danske Bank	2.6			1/14
Russian economy ministry	2.5	2.8		12/13
VTB Capital	1.3			12/13
Central Bank of Russia	2.0	2.5	3.0	11/13

Growth in Russian bank lending moderated last year, but households continued to pile on debt. Corporate borrowing rose 13 % last year, matching the 2012 pace. Growth in the stock of household credit slowed from nearly 40 % in 2012 to 29 %.

Corporate borrowing last year was reined in by the economic slowdown and stagnating investment.

The Central Bank of Russia has become quite concerned about the rapid build-up in household debt, particularly the increase in unsecured loans. Unsecured credit now accounts for over 60 % of household borrowing. Unsecured loans carry larger risk than secured loans.

With households taking on heavier debt burdens and slowing income growth, the stock of non-performing loans in bank portfolios has begun to rise. Households with loans devoted on average nearly 25 % of their income to debt servicing last year.

To calm the credit boom, the Central Bank of Russia last year increased the reserve requirements concerning household loans with further hikes planned this year. The requirements target unsecured loans.

The CBR is also investigating high interest rates charged on some loans. At the end of 2013, the average rate charged on a household consumer loan for over a year was around 18 %, while inflation was 6.5 %. Interest rates on unsecured loans are particularly high. The new consumer credit law, which will come into force at the beginning of July, grants the CBR authority to restrict rates charged on consumer loans.

Clean-up of Russia's banking sector proceeds smoothly. Last autumn, the CBR launched a clean-up of the banking sector to shut down banks with shaky finances and those involved in shady activities. Last year licenses were withdrawn from 29 banks and reorganization required on another two banks. As of end-December, 923 banks operated in Russia.

Most of the banks that have lost their licences are small or mid-sized, and their shutdown has not significantly affected the banking sector. However, depositors have become wary, with some smaller banks facing difficulties as depositors tried to empty their accounts. Some of the panic has come from unsubstantiated online warnings about impending bank licence withdrawals. As has happened in similar situations earlier, competing banks are often responsible for spreading the false information, but this time around the CBR took a proactive stance by publicly dismissing the rumours.

Russia's deposit insurance agency last year paid out a record 110 billion rubles (€2.4 billion) in compensation, depleting the deposit insurance fund by half. The deposit insurance agency, nevertheless, estimates that it will have sufficient funding this year to cover its obligations without having to hike fund contributions of banks. From the start of this year, also sole proprietorships are eligible to compensation from the deposit insurance fund in addition to households.

Although Russia's deposit insurance scheme covers deposits in nearly all banks, the uncertain situation in the banking sector has benefited state-owned banks and other large banks as people move their deposits to them. Russia's five largest banks are state-owned. Their combined share in the total assets of the banking sector increased last year by over two percentage points to nearly 53 %.

At the beginning of 2014, the CBR adopted capital adequacy requirements in accordance with Basel III banking supervision standards. The CBR next year will stage a gradual rollout of Basel III liquidity requirements that significantly tighten liquidity demands on Russian banks.

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China

Yuan now ranks among top ten most-used currencies in international payment transactions. According to the Society for World Interbank Financial Communication (SWIFT), the Chinese currency in December accounted for 1.12 % of international payments, making it the world's eighth most-used payment currency. Although the share of yuan use will likely decline temporarily in January and February due to the Chinese New Year holidays, it is clear that the yuan has established itself as a major payment currency. The two top payment currencies by far are the US dollar and the euro, followed by the British pound and the Japanese yen. The Canadian dollar (1.90 %), Australian dollar (1.89 %) and Swiss franc (1.29 %) still had larger payments market shares than the yuan in December.

Three-quarters of yuan payments occurred in Hong Kong, but use of the yuan soared also at other offshore yuan trading centres in London, Singapore and Taiwan. The growing international role of the yuan is also apparent in the on-going rise in yuan-denominated deposits in Hong Kong. Yuan deposits in the Hong Kong special administrative region were up 43 % y-o-y in December.

Chinese statistical data show yuan use in Chinese foreign trade continued to increase in the second half of 2013 after a short pause. As of December, 15 % of Chinese foreign trade was conducted in yuan, up from 10 % in August.

Official figures underestimate Chinese investment in OECD countries. The expansion of Chinese businesses in the international arena has further secured China's increasing role in the global economy. The phenomenon has attracted considerable attention in the media and has struck a note of concern among policymakers. Part of the nervousness reflects the fact that many large Chinese enterprises are state-controlled and not always subject to market forces. This feature of Chinese corporate ownership has been at the heart of recent disputes in Europe and the US in e.g. the telecommunications sector.

While the magnitude of FDI flowing into developed economies appears relatively modest, China's official figures likely underestimate outbound investment. The official statistical data only reflect investments that are approved by China's commerce ministry. According to these numbers, FDI outflows from China (excluding financial sector investments) exceeded $90 billion last year, up 16 % from 2012. Total financial sector FDI outflows amounted to $10 billion in 2012.

Although the commerce ministry has recently improved its practices and formally committed to complying with international standards, many still believe that the official figures underestimate the true numbers. International standards call for the use of surveys to get investment figures. In China's case, official figures are still compiled from data collected in the course of the investment approval process. Particularly small and private enterprises tend to underreport investments.

A second cause of the statistical distortion is the practice of "round-tripping" investments through tax havens. Investments pass through the tax haven to be reinvested in China or third countries. Such transactions go undetected as the Chinese practice only registers the first leg of the investment outflow from China, not the country where the money eventually ends up. Official figures show about 70 % of Chinese foreign investment goes to Hong Kong, the Cayman Islands or the Virgin Islands. The final destination of this investment usually goes undisclosed.

A new China Global Investment Tracker database from the Heritage Foundation registers investments of Chinese firms exceeding $100 million. The database confirms that OECD countries receive considerably more Chinese FDI than official Chinese figures indicate. OECD countries, especially Australia, the US, Canada and the UK attracted a much larger share of Chinese investment than official figures show. The database also reveals that nearly half of all Chinese investment outflows go to the energy sector and about a fifth to the mining sector. The database mentions numerous investment projects that have been abandoned or failed for some reason or another. Most of these projects are related to the energy or mining sectors.

January was a busy month for Chinese firms investing abroad. Many firms seek to increase their international reach and acquire technological capabilities through corporate acquisitions. For example, technology giant Lenovo agreed to buy the business operations of mobile phone maker Motorola from Google for $2.9 billion. Lenovo, which saw its international growth take off in 2005 with its acquisition of IBM's personal computer business, bought IBM's server business last month for $2.3 billion. In addition, banking giant ICBC agreed to acquire a controlling stake in Standard Bank's London-based markets unit for nearly $800 million.

Rhodium Consulting reports that Chinese investment in the US doubled in 2013, mostly on large corporate acquisitions. UNCTAD further confirms that the value of corporate acquisitions by emerging market enterprises in North America (NAFTA countries only) grew 63 % y-o-y in 2013 to $37 billion. UNCTAD's assessment expects more FDI outflows from China also to emerging markets, particularly Southeast Asia. They are often geared to infrastructure development or financial and production sectors. China has recently been active in negotiations to protect and increase foreign investment. The EU and China agreed in December to enter into talks on a bilateral investment treaty.

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