China News in Brief
July, 2012

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<table>
<thead>
<tr>
<th>In China, spending is a hard sell</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chinese inflation continues to weaken</td>
</tr>
<tr>
<td>In China, Price Drops Spur Talk of Deflation</td>
</tr>
<tr>
<td>China Q2 growth slows to 3-year low of 7.6%</td>
</tr>
<tr>
<td>Chinese economic growth slows to 7.6%</td>
</tr>
<tr>
<td>China: Slowing Growth, Spreading Consumer</td>
</tr>
<tr>
<td>Data Hint Chinese Economy Is Better Off</td>
</tr>
<tr>
<td>Stabilizing growth remains top priority</td>
</tr>
<tr>
<td>More funding urged to fight floods, droughts</td>
</tr>
<tr>
<td>VAT pilot program to expand</td>
</tr>
<tr>
<td>China to cut retail prices of gasoline and diesel</td>
</tr>
<tr>
<td>Shenzhong Represents New Frontier for Global Banks</td>
</tr>
<tr>
<td>Interest rates cut to spur growth</td>
</tr>
<tr>
<td>Interest rate cuts set to hit profits</td>
</tr>
<tr>
<td>Zhejiang private lending dispute on the rise</td>
</tr>
<tr>
<td>PBOC: Time ripe for deposit insurance system</td>
</tr>
<tr>
<td>China's financial slowboat speeding up</td>
</tr>
<tr>
<td>China must cut dependence on bank debt: regulator</td>
</tr>
<tr>
<td>China is outgrowing its financial system</td>
</tr>
<tr>
<td>A boom driven by distortions</td>
</tr>
<tr>
<td>US 'golden opportunity' for Chinese banks</td>
</tr>
<tr>
<td>China's household assets hit $69t</td>
</tr>
<tr>
<td>China will not relax property control policies</td>
</tr>
<tr>
<td>More Chinese firms seek delisting from US market</td>
</tr>
<tr>
<td>China commodity prices to have global impact</td>
</tr>
<tr>
<td>China's corporate bond market booms</td>
</tr>
<tr>
<td>Netizens cry for IPO suspension</td>
</tr>
<tr>
<td>China's stocks slump to record low in 3 years</td>
</tr>
<tr>
<td>Chinese mainland ranks 34th in innovation</td>
</tr>
<tr>
<td>China calls for sci-tech innovation</td>
</tr>
<tr>
<td>Smart city initiatives to boost economy</td>
</tr>
<tr>
<td>Eastern promise fades as western growth soars</td>
</tr>
<tr>
<td>Private firms eager to tap more sectors</td>
</tr>
<tr>
<td>China OKs private investment in defense sector</td>
</tr>
<tr>
<td>Private investment encouraged</td>
</tr>
<tr>
<td>China economy: China's steel worries</td>
</tr>
<tr>
<td>Chinese earnings</td>
</tr>
<tr>
<td>McKinsey: Chinese firms still lack global status</td>
</tr>
<tr>
<td>Flash PMI at 5-month peak HSBC</td>
</tr>
<tr>
<td>Zhejiang enterprises scale down output</td>
</tr>
<tr>
<td>79 Chinese companies listed on Fortune 500</td>
</tr>
<tr>
<td>Clinton warns Beijing on sea dispute</td>
</tr>
<tr>
<td>The China-bashing syndrome</td>
</tr>
<tr>
<td>Rebalancing the Global Economy</td>
</tr>
<tr>
<td>Iran/China economy: Sanctions show importance of China for Iran's economy</td>
</tr>
<tr>
<td>Shenzhen OK'd to test first use of yuan</td>
</tr>
<tr>
<td>Yuan included in Trade Finance Program</td>
</tr>
<tr>
<td>Sovereign wealth fund suffers losses in 2011</td>
</tr>
<tr>
<td>SAFE 'to invest $500m' in Blackstone property fund</td>
</tr>
<tr>
<td>Trade grows 3% in first half</td>
</tr>
<tr>
<td>China's Rx: Foreign-Owned Hospitals</td>
</tr>
<tr>
<td>The Invest in China Guidebook Series (3) (Second Edition)</td>
</tr>
<tr>
<td>Companies have home thoughts from abroad</td>
</tr>
<tr>
<td>China's FDI falls 6.9% year-on-year</td>
</tr>
<tr>
<td>Extra effort needed on China-US investment</td>
</tr>
<tr>
<td>Govt stressing quality for FDI, ODI</td>
</tr>
<tr>
<td>More channels open for foreign investors</td>
</tr>
<tr>
<td>M&amp;A cool in China, heats overseas</td>
</tr>
<tr>
<td>China's H1 outbound direct investment surges 48%</td>
</tr>
<tr>
<td>CHINA: Inexperience complicates overseas investment</td>
</tr>
<tr>
<td>China Push in Canada Is Biggest Foreign Buy</td>
</tr>
<tr>
<td>Chinese investment up US 'set for record year'</td>
</tr>
<tr>
<td>CHINESE FIRMS MORE THAN TRIPLED INVESTMENT IN EUROPE IN 2011</td>
</tr>
</tbody>
</table>
In China, spending is a hard sell

Chinese remain among the world’s stingiest consumers. Household consumption in China accounted for a paltry 35 percent of the overall economy in 2010, compared with 71 percent for Americans and 57 percent for Europeans. Chinese also save far more than others, with an average household savings rate of 38 percent in 2010, compared with just 3.9 percent for Americans and 2.8 percent for Japanese, according to figures compiled by Bloomberg Businessweek magazine, using statistics from the World Bank and the Organization for Economic Cooperation and Development, along with other data. And while younger Chinese have begun to buy more, save less and take advantage of credit more often than their parents, the old habits appear to be eroding slowly and may change only with a new generation. The high rate of savings contrasts with the increasingly visible consumerism in cities such as Beijing and Shanghai, which are filled with Ferraris, shopping malls and luxury boutiques. But there are other very practical reasons that people in China save. Buying a home typically requires a down payment of at least 25 percent and more often 30 percent, an astronomical sum of money for many. Also, many here have their first, and often only, child in their 30s, which is when they begin saving for future education expenses.

Getting people to spend more has become the government’s latest mantra. "Expanding domestic demand, particularly consumer demand . . . is essential to ensuring China's long-term, steady and robust economic development," Premier Wen Jiabao told the legislature in his annual work report in March. "We will improve policies that encourage consumption." But changing the policies that discourage private consumption could prove difficult, requiring China's Communist Party rulers to adopt a host of reform measures they have long resisted, such as freeing interest rates to rise and letting the Chinese currency float freely. The policies introduced so far have been largely symbolic, according to experts. The policies include subsidies to allow people to purchase more energy-efficient home appliances such as air conditioners and flat-screen televisions. There also have been proposals for cutting import taxes on some consumer goods. A pilot program in Shanghai replaced a business tax with a value-added tax. Chinese consumers who were interviewed agreed that the government could take several more decisive steps that would have a dramatic and direct impact on spending and savings habits. For example, credit could be made more available, and interest rates could be allowed to rise to reflect market rates. So while domestic consumption is growing, it accounts for only a small share of the overall economy because the state sector still looms so large.


Chinese inflation continues to weaken

China’s consumer prices rose at the slowest pace in 29 months in June, along with the lowest industrial inflation in 31 months, strengthening expectations that the world’s second largest economy may suffer the most serious impact after the 2008 financial crisis. June consumer prices increased by 2.2 percent from a year earlier, the slowest growth since February 2010. The figure was 0.8 percentage points lower than in May, the National Bureau of Statistics said on July 9. During the first six months of the year, the country's CPI increased 3.3 percent compared with the same period last year, lower than the full-year target of 4 percent set by the central government in March.

As market demand is shrinking because of the deepening eurozone crisis and the weakening global economy, China's GDP growth may decrease to 7.5 percent - the slowest pace since the second quarter of 2009, after the 8.1 percent year-on-year increase in the first three months, according
to economists. Sharply easing inflation pressure was one of the reasons for the central bank to consecutively cut benchmark interest rates twice since June. The People's Bank of China lowered interest rates last week by 25 basis points to boost growth, the second time in a month. It has also cut commercial banks' required reserve ratios by 150 basis points since November 2011, setting free about 1.2 trillion yuan ($190 billion) for credit. Also, the producer price index fell deeper less than zero for the fourth straight month to minus 2.1 percent, indicating industrial deflation, which indicated that the demand for companies' output both overseas and domestically is weakening amid the gloomy global economy.

Source: Chen Jia: China calls for sci-tech innovation, China Daily, 2012-07-09

In China, Price Drops Spur Talk of Deflation: [Business/Financial Desk]

Prices are tumbling across the Chinese economy, according to government data released on Monday, as a flood of goods pouring out of the country's factories and farms exceeds anemic demand from Chinese households and businesses. The news of falling prices, together with a pledge by Prime Minister Wen Jiabao on Saturday to maintain stringent bans on real estate speculation, produced a slide in mainland Chinese stock markets. The main index of the Shanghai stock market dropped 2.4 percent, while the Shenzhen stock market's benchmark fell 2.2 percent.

Consumer prices dropped 0.6 percent in June from May, the largest month-to-month drop in two years. Producer prices, measured at the factory gate, were down 2.1 percent in June from a year earlier, and down 0.7 percent in June from May. Chinese economic policy makers did little to respond to the country's slowing economy from mid-March to mid-May. The country's leadership now seems to be reacting with policies aimed at offsetting the economic slowdown. Mr. Wen took an inspection tour of east central China over the weekend and called for more aggressive fiscal and monetary policies. The Chinese central bank cut interest rates twice over the last month. But Mr. Wen also reaffirmed over the weekend the central government's commitment to improving the affordability of housing, through policies designed to discourage real estate speculation. Banks have been discouraged from issuing mortgages for second and third homes, for example.

A few economists are starting to ask whether China could face deflation, a sometimes intractable condition of falling prices that can become self-reinforcing, as Japan has found over the last two decades. But most economists are still skeptical that China faces a significant risk of sustained deflation. Regulated bank lending rates are at 6 percent, leaving a long way for them to be cut.


China Q2 growth slows to 3-year low of 7.6%

China's economy reported 7.6 percent of growth in the second quarter, the lowest since the first quarter of 2009 when the global financial crisis was rampant, amid concerns about the slow-down of the second-largest in the world and the strongest one in the major economies. The National Bureau of Statistics said on Friday that in the first half, the country's economy grew by 7.8 percent to 22.71 trillion yuan ($3.56 trillion). The growth in the first quarter was 8.1 percent. It is the lowest growth in the past 13 quarters.

China's manufacturing, foreign trade and investment have been slowing down this year, triggering worries about a hard landing of its economy, whose role is more important as the eurozone is still struggling with the debt crisis, the US is still on the way to recover and emerging
economies such as India and Brazil are also slowing down. China's central bank has cut the interest rates twice this year to stabilize the growth. Premier Wen Jiabao also vowed to maintain a stable economy in recent visits in the nation and major conferences.

"China has to get to the point where the consumers in China need to start consuming more. It has to start re-balancing the economy. China is not a wealthy country but it is a middle-class country right now, too," said Abruzzese. "The Chinese government needs to start creating more social safety programs, more social insurance programs, where people then won't feel they need to save quite as much as they do." Abruzzese said "a little less saving and a little more spending" would be better for China's and the world's economy. "China's economy is strong but it's a little bit distorted. When China starts to buy more, everybody else will be a little happier, too," he said. Abruzzese believed the Chinese government's recent moves of cutting the interest rates shows the country is being more integrated and more involved in the global economy.

Source: Zhang Yuwei in New York and Chen Jia in Beijing: China Q2 growth slows to 3-year low of 7.6%, China Daily, 2012-07-13

**Chinese economic growth slows to 7.6%**

China’s growth fell to 7.6 per cent in the second quarter, its slowest since early 2009, as a property market downturn and weak exports weighed on the world’s second-biggest economy. Over the past two months, as evidence of the slowdown has mounted, the government has shifted its policy to a pro-growth stance, which analysts say is likely to bring about a recovery in the second half of the year.

The year-to-date investment figure jumped from 20.1 per cent in May to 20.4 per cent last month, an indication that the increase in investment in June alone must have been considerably stronger, following on the heels of the government’s moves to stimulate the economy. The Chinese central bank cut interest rates last week, the second time in less than a month. Premier Wen Jiabao has also said that the government will look to increase public investment to stabilise the economy. A steep drop in inflation – from last year’s high near 7 per cent to just over 2 per cent – has cleared the way for more aggressive policy easing. The latest bank lending figures, published on Thursday, confirmed that the government is clearly trying to support growth. New loans reached Rmb920bn ($114bn) in June, up from Rmb793bn in May and more than expected.

Yet officials have also repeatedly vowed that they will not unleash a massive stimulus programme as they did in late 2008 when the global financial crisis erupted. That boom in spending and bank lending fuelled debt worries that China is still trying to contain as well as a property bubble that it has been trying to deflate. The peak-to-trough drop in growth would be 4.5 percentage points from 2010 to now. That contrasts with a plunge of 8 percentage points in the previous downturn, from 2007 to the start of 2009.

Source: Simon Rabinovitch Beijing: Chinese economic growth slows to 7.6%, Financial Times, July 13, 2012

**China: Slowing Growth, Speeding Consumer**

Growth in China's economy decelerated to 7.6% year-on-year in the second quarter of 2012, the lowest since the start of 2009. The old mainstays--exports and investment--both disappointed. The share of investment in growth fell relative to 2011, and slowing exports were a drag. This time it's different. The 2009 stimulus did the job, but it also ballooned total credit levels from around 134% of gross domestic product in 2008 to 173% in 2011, unleashed a wave of inflation, and tilted the economy further toward reliance on investment to drive growth. A repeat performance isn't in prospect. The 2012 stimulus is markedly smaller and pays more attention to solving, or at least not exacerbating, structural problems. Rate cuts have been executed so they protect returns to household savers even as they cut the cost of credit for business borrowers. Income tax for low earners has been reduced.
With the government in no rush to flood the markets with liquidity, and business reluctant to start another round of investment, the chance of the 2012 mini-stimulus putting a rocket under equity and hard commodity markets is remote. Instead, the slowdown could be a chance for China's consumer to step forward--shopping bag in hand--to pick up the slack from fading investment and exports. Firms like Yum Brands, whose KFC and Pizza Hut restaurants saw 50% of 2011 operating profit come from China compared with 32% from the U.S., are well placed to benefit. In the boom years for China's economy, a bet on the commodities that fueled investment and the ships that transported exports was the best way to benefit. Now growth is slowing but incomes are rising, and it's time to go shopping with the Chinese consumer.


World News: Data Hint Chinese Economy Is Better Off
The preliminary HSBC China Manufacturing Purchasing Managers Index, a gauge of nationwide manufacturing activity, rose to 49.5 in July compared with a final reading of 48.2 in June, HSBC Holdings PLC said Tuesday. The reading was the highest in five months and could ease market concerns over a sharp slowdown in the world's second-largest economy. In the second quarter China's economic growth slowed to 7.6%, the slowest rate since the global financial crisis. Beijing has stepped up its efforts to rekindle growth, including two cuts in lending rates since the beginning of June. The data indicate that "earlier easing measures are starting to work," HSBC Chief Economist for China Qu Hongbin said in a statement. Markets had a mildly positive initial reaction to the data. The Australian dollar, which is highly sensitive to Chinese demand for raw materials, rose slightly against the U.S. dollar. Chinese stocks also posted gains immediately after the data were released, but they were later flat.


Stabilizing growth remains top priority
Chinese authorities on Tuesday reaffirmed their stance of maintaining stable economic growth as the top priority, pledging the adherence to proactive fiscal policy and prudent monetary policy to weather the current hardships. The ongoing pace of economic growth is within expectations, but the external environment remains grim and poses difficulties and challenges to growth, according to a newsletter released after a meeting of the Political Bureau of the Communist Party of China Central Committee, which was presided over by President Hu Jintao. "We should observe the problems and risks, strengthen risk-awareness and make good preparations, while noting that economic growth is sound," read the newsletter. "We should remain firmly confident in our economic work to promote steady and relatively fast growth," it said.

Dwindling orders from Europe and other trade partners have sapped China's exports and, combined with a cooling property sector, slowed the country's economic growth rate to 7.6 percent in the second quarter, the lowest level since the first quarter of 2009. The government has vowed to expand domestic demand, develop the real economy, accelerate reforms and improve people's living standards over the rest of the year. The possibility of a housing price rebound has been looming in some cities. The committee said it will implement cooling policies to curb speculative demand and increase supplies of smaller apartments and subsidized housing.

The committee also pledged to cut taxes, maintain moderate credit growth and optimize investment structures to enhance efficiency. The government will beef up support for key projects and implement policies that allow private capital to play a bigger role, the committee said, adding that foreign trade policies will stay consistent. On July 26, Hu called for more efforts to ensure agriculture production and stabilize jobs, adding that
authorities must remain alert against economic risks and closely watch changes in the global economy. "Favorable policies should be implemented in order to boost crop output, farmers' incomes and the agricultural modernization drive," Hu said. Premier Wen Jiabao said the country's economic and social development has been "in a good situation in general," and the economy, despite slowing growth, has remained within expectations. However, Wen said that "concerning the domestic economy, the most obvious problem is that economic downward pressure is still relatively big." Wen said difficulties and risks should not be underestimated, as the world economy is expected to continue its slow growth for a very long time, posing hardships for expanding external demand. "Various monetary policies should be adopted to ensure the steady and moderate increase of currency loans," said Wen. Wen urged the deepening of reforms in key fields and the strengthening of policies to boost the non-public sector. In addition, Wen promised to "resolutely" carry out policies to adjust and control the real estate market in order to prevent housing prices from rebounding.

Source: Xinhua: Stabilizing growth remains top priority, July 31, 2012

More funding urged to fight floods, droughts
China's Ministry of Finance Tuesday called on local authorities to increase financial support for flood control and drought relief. The MOF said in a statement that it comes at a crucial moment for the country to fight against floods, pledging a special fund from central budgets to fight serious floods and droughts. It also urged governments at all levels to ensure that the fund is not misappropriated.

On Sunday, the MOF allocated 120 million yuan ($19 million) to help the municipalities of Beijing and Tianjin and neighboring province of Hebei to fight floods. Rainstorms since the weekend have ravaged many parts of China, including the capital city where the heaviest rain in 60 years caused 37 deaths. Torrential rain has swept through 17 provincial areas since July 20, leaving 95 dead and another 45 missing, the Ministry of Civil Affairs said on Monday.

Source: Xinhua: More funding urged to fight floods, droughts, July 25, 2012

VAT pilot program to expand
The State Council on Wednesday approved a plan to extend a value-added tax pilot program in Shanghai to eight provincial-level regions. The program to replace the business tax with a VAT will extended to Beijing, Tianjin, Jiangsu, Zhejiang, Anhui, Fujian, Hubei and Guangdong, and the cities of Xiamen and Shenzhen, according to a statement of a State Council meeting presided over by Premier Wen Jiabao. The plan will start on Aug 1 and be finished by the end of this year, the statement said. To avoid double taxation, the State Council on Oct 26 approved the pilot program to replace the business tax with a VAT on selected service sectors, such as the transportation sector, in Shanghai from Jan 1.

A business tax is a tax on the gross revenue of a business, while a VAT is a tax levied on the difference between a commodity's price before taxes and its cost of production. The replacement of the business tax could lift GDP growth by 0.5 percentage points and export growth by 0.7 percentage points, while helping create about 700,000 jobs, said Xiao Jie, director of the State Administration of Taxation, Xinhua News Agency reported in March. The pilot program will be expanded to more areas and sectors nationwide next year, the State Council said on Wednesday.

Alan Wu, PricewaterhouseCoopers China national indirect tax leader, said in a report on Wednesday that the current business-tax system is not a business-friendly tax. The costs of business tax are squeezing businesses' profit margins and increasing the cost of goods and services for consumers, he said. "The transition to VAT is certainly a welcome change, given the current pressures in terms of affordability and the levels of taxation that are affecting the public," Wu said.
China to cut retail prices of gasoline and diesel
The government will cut retail prices of gasoline and diesel beginning on Wednesday, China Central Television quoted Zhou Wangjun, deputy director of the National Development and Reform Commission's department of pricing, as saying. The government is looking for the right time to promote the reform of refined oil prices, he said. According to China's current pricing mechanism, if the price of a basket of international crude oil changes by more than 4 percent within 22 working days, China may adjust the domestic refined oil price.
Source: Xinhua: Private firms eager to tap more sectors, 2012-07-10

Shenzhen Represents New Frontier for Global Banks
While global bank's previous dealings in China via joint ventures have focused on large offerings and privatizations of state-owned companies, experts say in the future, small and medium sized businesses will be the driving force for capital markets. One of the greatest untapped markets for global banks right now is Shenzhen, a city in southern China near Hong Kong, according to Reuters. Last year, it hosted an average of one IPO per business day--more than London, New York and Hong Kong combined. So far, the banks, brokers and retail investors participating in Shenzhen's mostly smaller public offerings have been mainly local, but China plans to create a mini-Hong Kong financial hub in the city and ultimately aims to put Shenzhen on the level of London or New York. A handful of global banks like Morgan Stanley and Citibank won approval to do business in China last year. While global bank's previous dealings in China via joint ventures have focused on large offerings and privatizations of state-owned companies, experts say in the future, small and medium sized businesses will be the driving force for capital markets.

Interest rates cut to spur growth
The central bank cut interest rates for a second time in a month, fueling concerns that the slowdown in the world's second-largest economy is worse than predicted. The People's Bank of China lowered benchmark deposit rates on Thursday by 25 basis points and cut lending rates by 31 basis points, effective from Friday. The central bank cut interest rates on June 8 for the first time since 2008 to bolster economic growth. "The limits for rates charged on individual property loans will not change and financial institutions must strictly implement differentiated policies on property loans to continue constraints on speculative purchases," the central bank said. A leading economist said that cutting rates twice in a month suggests weak growth.
Apart from shoring up the economy, the surprising move is in line with other central banks of major economies, said Zhang Monan, an economist at the State Information Center. The Bank of England announced on Thursday it will increase its quantitative easing stimulus policy by 50 billion pounds ($78 billion) while keeping the main interest rate at a record low of 0.5 percent. The European Central Bank also announced on Thursday it will reduce the interest rate on the main refinancing operations of the euro system by 25 basis points to 0.75 percent. "It is a replica of last year, when the world's six major central banks joined hands to save the market. It seems that the world's major banks have a tacit agreement," Zhang said.
The central bank also allowed commercial banks to set the interest rates charged on their loans at or above 70 percent of the government's benchmark rate, down from the previous 80 percent. With external demand hit by the European debt crisis, growth in fixed-asset investment would be hard to shore up, as local governments are tangled in debt issues, he said.
Interest rate cuts set to hit profits
Recent cuts in interest rates by China's central bank could strain the Chinese banking sector's profitability in 2013, but any extra pressure on profitability this year is unlikely, Standard & Poor's Ratings Services said in a report on Wednesday. "These moves will enable banks to price their loans at levels that should allow them to compete more effectively with the bond markets. We estimate that the central bank's actions will weaken the banking sector's return on assets in 2013 by 10 basis points more than our previous forecast of a 20- to 25-point reduction," said Ryan Tsang, primary credit analyst of S&P.
Source: Xinhua: Interest rate cuts set to hit profits, 2012-07-12

Zhejiang private lending disputes on the rise
The number of private lending disputes in East China's Zhejiang province has been on the rise since the global financial crisis in 2008, according to new research by the province's higher court. Both the number of disputes in Zhejiang, where private businesses serve as a pillar of the prosperous local economy, and the amount of money involved rose very fast over the past few years, according to a report released on Tuesday by the court. Courts in Zhejiang handled 58,037 private lending disputes involving 28.4 billion yuan ($4.5 billion) in the first half of 2012, up 27 percent and 129.6 percent, respectively, from the same period last year, according to the report. Over the past few years, private financing disputes accounted for almost half of all commercial lawsuits in Zhejiang, it added.

More than half of 2,835 companies surveyed in Zhejiang last year have sought financial help from private creditors, as banks are typically unwilling to lend to smaller companies. During last year's credit crunch, about 100 managers or heads of private companies in Wenzhou, a Zhejiang city known as the cradle of China's private businesses, were reported to have disappeared, committed suicide or declared bankruptcy - invalidating debts worth about 10 billion yuan. In late March, the State Council, or the central government, announced plans to set up a pilot zone in Wenzhou, and later a private lending registration service center was inaugurated to serve as an intermediary between borrowers and lenders in an attempt to standardize private lending in the city.
Source: Xinhua: Zhejiang private lending disputes on the rise, 2012-07-12

PBOC: Time ripe for deposit insurance system
The People's Bank of China, the country's central bank, said now is the time for the country to establish a deposit insurance system. That announcement came as part of an official report that was released over the weekend and is a strong indicator that the long-awaited system will be introduced soon. Deposit insurance protects depositors from losses they would incur if a bank they had put their money in found itself unable to pay its debts. It is thus seen by many as an important means of promoting financial stability. Experts said introducing the system will accord with the country's plans to liberalize its interest rates. In the past month, the central bank allowed the interest rates banks pay on deposits to fluctuate more widely, setting in motion a liberalization of interest rates.
Source: Zheng Yangpeng: PBOC: Time ripe for deposit insurance system, China Daily, 2012-07-16

China's financial slow boat speeding up
China's financial regulators are beginning to look like tugboat captains on a speedboat. They have the right instincts for steering their vessel – the country's markets – in the desired direction, but the engine is proving more powerful than they at first thought. Their objective is a smaller banking sector, one that is less dominant in
China’s financial system. At present, banks account for 80 per cent of corporate financing in China, according to official data, well above the norm of 50 per cent or less in other countries – be they developed or developing. These regulators have a carefully charted plan to reach that destination. But powerful market forces are now propelling China along this course far more quickly than intended and creating new, dangerous risks in their wake.

Beijing wants to bring change to the financial sector in a careful, step-by-step way and it has nudged this agenda forward in recent months. Most notably, with its two interest rate cuts since the start of June, the government has given banks more freedom to set deposit and lending rates. It still guarantees them a tidy interest margin, but the margin is smaller than before – forcing bankers to get used to a world where funding costs actually matter. The government has also made progress in the corporate bond market, which was long hobbled by an onerous approval process for issuers. Regulators have recently lightened their touch, fast-tracking approvals and encouraging more bond issuance.

But Beijing’s progress looks slow when set against the rapid pace of change in Chinese financial markets, which is occurring beyond the confines of the official reform agenda. The wealth management products that banks are selling are an example of real interest-rate liberalisation. These products, which are typically loans repackaged as short-term investment products, barely existed a few years ago. By the end of the first quarter of this year, they were worth about Rmb10.4tn – equal to 12 per cent of total bank deposits. Banks use these wealth products to fight for customers, luring them with higher yields than they can offer on capped deposit rates. To measure the boom in fixed income products, forget the formal bond market and look to the trust sector. Chinese trusts are companies that extend loans or make equity investments, then combine them into fixed-income products for customers. Barely a blip on the radar a decade ago, these trust companies manage more than Rmb5.3tn today – putting them on track to eclipse the insurance sector in asset size this year. The comparison with bonds is even more striking. Trust products are worth about 20 times more than the total amount of corporate debt traded on China’s exchanges.

However, the rise of trusts and wealth products also presents serious risks. The government has encouraged a belief that debt defaults are almost impossible by ordering banks to bail out companies on the brink of trouble, such as rayon maker Shandong Helon earlier this year. Many wealth and trust products have been sold with implicit guarantees that debtors won’t default. Investors could be in for a nasty surprise. For years, China’s regulators have been supremely cautious about steering the country’s financial system into the stormy waters of competition. The regulators are finally heading toward that destination, but the financial system is in a much bigger hurry to get there.

Source: Simon Rabinovitch : China’s financial slow boat speeding up, Financial Times, July 17, 2012

**China must cut dependence on bank debt: regulator**

China must cut its dependence on bank credit alone to drive economic growth and be wary of the risk of a rebound in bad debt, a banking regulator said in remarks published on Tuesday. Yan Qingmin, assistant chairman of the China Banking Regulatory Commission, said weak demand in the current economic slowdown exposed banks to rising bad loans, particularly from industries with overcapacity, smaller enterprises and export-related businesses. "Currently, we face pressures from a rebound in bad bank loans in some areas, especially when small firms are affected by the economic slowdown and local government financing vehicles have entered a peak period in loan repayments," Yan said in an article he wrote in Financial News, an official newspaper operated by the People's Bank of China, the central bank. "Given the high base of total bank loans, a rebound in bad loans could affect financial stability," he added. He said that China's credit to GDP ratio had climbed in recent years, hitting 123.4 percent by the end of 2011 - an unsustainable level that overly concentrates risks on the banking
sector.

China's recent efforts to liberalize its interest rate system would squeeze bank profits and should force a shift in their business orientation from lending to fee-based income in the future, Yan said. Fee-based services around underwriting securities issues, dealmaking and advisory work are key sources of income for international banks in developed markets. China launched its high-yield "junk bond" market in June, kicking off a new funding channel that by some estimates will see as much as $50 billion in capital flow to cash-starved private Chinese companies within a few years.

Source: Xinhua: China must cut dependence on bank debt: regulator, July 18, 2012

China is outgrowing its financial system

At the beginning of July, a mix of the most thoughtful Chinese and foreign policy makers, academics and market practitioners gathered in Shanghai for the annual Lujiazui financial forum. The economic backdrop wasn’t great. Europe continues at the edge of the precipice while the US has lost momentum and emerging markets are also slowing. The world still hasn’t recovered from the global financial crisis made in the US and swiftly exported to much of the world. Meanwhile, hopes that China will save the planet look increasingly forlorn. Exports, a lagging indicator, came in at a relatively strong 11.4 per cent while far weaker imports, a leading indicator, at just over 6 per cent, suggest as much.

One of the lessons that China learned from the global financial crisis is that the West doesn’t have much to teach it when it comes to building a financial system. Yet China is outgrowing the system that served it well up to now. So change is inevitably coming and the Communist Party, obsessed with control, may not be able to control the process. Meanwhile, much of the discussion in Shanghai was dedicated to the hottest topics on the reform agenda; the liberalisation of interest rates, the gradual dismantling of capital controls and the expanding international use of the renminbi.

For example, in recently adjusting interest rates in the hope of sparking more demand for loans in China’s slowing economy, the changes have been asymmetrical. For the first time, Beijing cut the interest rates on loans more than on deposits while leaving the banks with some discretion to raise the return on deposits. Still, Beijing was being far more reactive than proactive in introducing this departure. Many people and companies are putting their money in trust company products with far better returns than those on offer at the banks. And even at the banks, as much as half of all new deposits are going into wealth management products, according to Fitch Ratings, while there have been no new net corporate deposits at all in five years. If the authorities hadn’t acted, they would merely have accelerated the flight out of deposits and out of the banks. But such liberalisation is a double-edged sword. The banks have thrived on the huge gap between the rates at which they lend and what they pay out on deposits but now that is gap is narrowing. That is extremely inconvenient. Banks will need more capital to help them deal with bad debts from the last round of fiscal stimulus, which is always done through the banks.

China continues to move toward capital account liberalisation as well. In the past, much of the demand for renminbi from the rest of the world was rooted in the expectation that the currency would appreciate. Now such expectations have vanished but demand remains in part because of a dollar shortage, especially in Asia. In trade-weighted terms, the renminbi has already appreciated a lot and many hedge fund managers think today the currency is about where it ’should’ be. Now, in a reversal of fears of undue appreciation, there are whispers in the capital as well as on the sidelines of the forum in Shanghai about a potential flight of capital, whether just out of the banks or, more alarmingly, out of the country altogether. The trigger could be benign, such as a rally in the stock market, which has been in the doldrums for years, attracting funds away from the banks. Or it could be something darker, such as riots in the streets. Fears of capital flight are one factor that keeps Beijing from lifting
capital controls. But those who set the policy agenda have their own agendas as well. Self interest also influences outcomes.

Source: Henny Sender: China is outgrowing its financial system, Financial Times, July 19, 2012

A boom driven by distortions
Severe distortions in China’s financial system are seen by many analysts as the biggest single factor behind the country’s runaway investment boom. Large corporations and state-backed entities are able to borrow money from banks at artificially cheap levels, fuelling reckless spending decisions. Meanwhile smaller businesses – the lifeblood of the economy, generating about 80 per cent of jobs – are seen as risky borrowers since they lack government backing and so have little access to the state-run financial system. “Money flows to the state-owned enterprises in the end and they can use this to get into real estate or to provide financing for others, so asset bubbles get more and more serious,” says Zhang Jun of Shanghai’s Fudan University. The government has ordered state-owned companies to stop investing in real estate if it is not one of their core businesses in a bid to halt a development that officials feared was driving up property prices and increasing balance sheet risks. But many companies ignored this edict. For example, COFCO, the country’s top grain trader, is also one of its biggest shopping mall developers. “Our major concern is making a profit, not quitting the housing market,” an unnamed official at a state-owned firm was quoted as saying by China Business News, a local paper. Ordinary people subsidise such largesse by stuffing their savings into bank accounts with exceptionally low interest rates. Deposit rates in real terms have averaged 1.5 per cent since 2004, despite the economy growing 10 per cent a year. Chinese people have few other choices for their money. The country’s stock market is riddled with insider trading and rotten corporate governance; it is extremely difficult for individuals to invest abroad; and the mutual fund and insurance industries remain under-developed. Outside of banks, savers have one other viable investment option: property. A study by China’s Southwest University of Finance and Economics recently found that city dwellers owned on average 1.2 homes.

Source: Simon Rabinovitch: A boom driven by distortions, Financial Times Chinese, July 20, 2012

US 'golden opportunity' for Chinese banks
Big Four banks still able to extend credit as Western counterparts recapitalize. Three years ago, Chinese banks provided support to various big US companies that were finding it difficult to obtain loans from lenders in their own country. While helpful to businesses that were in need of capital, the extension of credit also dovetailed with the banks’ desire to expand overseas. The most prominent example of such lending came in December 2009, when General Electric Co’s financing unit, GE Capital, obtained a three-year, $400 million loan from Industrial and Commercial Bank of China Ltd. ICBC, the world's biggest bank measured by market capitalization, made the loan a year after GE Capital had entered, and then quickly exited, a bailout program offered by the US government. The loan had come at a fortuitous time. ICBC had set up its first US branch in New York in 2008, intending to concentrate on commercial lending. That same year, at the peak of the US recession, many of these companies responded warmly to Asian banks' willingness to lend. Among US companies, the bank has also provided loans to the computer technology company Dell Inc, the delivery company United Parcel Service Inc and Southwest Airlines Co.

With many Western banks still keeping a tight rein on capital, Chinese banks have a "golden opportunity" to play a greater role in the US, said Chew Ping, managing director of China operations for Standard & Poor’s. "However, they must be aware that they are operating in a market that is very different from China's market," he said. "This is a learning process for them."
Just five years ago, Chinese banks were unlikely to lend to US corporations, said Brian Caplen, editor of the UK financial magazine The Banker. "Chinese banks still are able to extend credit, while US and European banks incurred so many bad loans during the crisis that they need to recapitalize," Caplen said. "Their capacity to lend is less now." Chinese institutions, as measured by The Banker, gained a bigger slice of global bank profits after the economic downturn. They now generate nearly 30 percent of those profits, compared with just 4 percent in 2007, according to a worldwide survey of 1,000 banks the magazine released in early July. China's Big Four banks - ICBC, China Construction Bank Corp, Bank of China Ltd and Agricultural Bank of China Ltd - were among the banks with the five largest annual profits on the Top 1,000 World Banks 2012, a list compiled by The Banker. ICBC led the pack.

Among world banks, ICBC was ranked third by The Banker in a list of banks with the largest amounts of Tier 1 capital. That was the highest spot ever accorded to a Chinese bank. Tier 1 capital is a measure of a bank's financial soundness and ability to withstand unexpected losses. It consists of capital held in common stock - equity that can't be redeemed at the option of shareholders - as well as retained earnings, or reserves. "One big factor of their huge profits is the domestic situation in China," Caplen said. "The economy was growing at 8 to 9 percent a year. Property prices were rising, and companies were expanding.” But the banks' business outside China is still quite small compared with what they do inside the country. Some experts said it remains to be seen how greatly Chinese banks will become "internationalized". "It's inevitable for Chinese banks to go overseas,” said Chew. "But it will take quite some time for them to be truly internationalized.”

While Chinese banks are seeking opportunities to lend to Western companies, their main objective is to help Chinese enterprises operate overseas, Caplen said. "As Chinese corporations go abroad to diversify their sources of supply, Chinese banks will naturally follow them,” he said. ICBC's completion in July of its acquisition of an 80 percent stake in BEA USA, the California-based subsidiary of the Bank of East Asia Ltd, paves the way for the Chinese bank to expand its US business. The deal marked the first time the Federal Reserve had approved a Chinese bank's attempt to purchase a US bank. To Caplen, the deal showed there is "declining US resistance" to Chinese investment. H. Rodgin Cohen, a partner at Sullivan & Cromwell LLP, the law firm that represented the Bank of East Asia in the transaction, said the purchase of the stake suggests the Fed is more receptive to such investment. But, he added, "nobody knows for sure how receptive it would be" toward future deals. The Fed recognized that Chinese banks have made progress in a relatively short time, Cohen said. "The Chinese banking regulatory system is clearly more modernized and Chinese banks now have better performance, in terms of being more consistently profitable and having better asset quality,” he said.

One cause of ICBC’s success with regulators was the fact that its New York branch turned a profit within its first year. Also, its loans to some Western companies during the crisis helped the Fed in its decision. But those were not the chief reasons the deal was approved. In October 2010, ICBC bought the US broker-dealer operations of Fortis Securities from the France-based BNP Paribas SA. ICBC paid a token $1 for Fortis, which BNP acquired as part of its crisis-fueled 2009 purchase of Fortis Bank of Belgium. The unit, though small, overlapped with the French bank's existing US broker operations. "When ICBC submitted its application to the Fed, it already had a good track record in the US," Zou said. "For other Chinese banks that aim to expand in the US, a careful expansion plan will be helpful." The Fed has also decided to allow the Agricultural Bank of China to build a New York office. And Bank of China, which has branches in New York and Los Angeles, was allowed to build a third branch in Chicago. In Maryland, the state's Department of Business and Economic Development is expecting the arrival this fall of the Export-Import Bank of China, whose first US office will be established in the World Trade Center building along Baltimore's Inner Harbor. In San Francisco, the home builder Lennar Corp and its partners are in talks with China Development Bank about obtaining $1.7 billion in capital to accelerate the development of the long-delayed Treasure Island and Hunters Point Shipyards-Candlestick Point
housing complexes.

**China's household assets hit $69t**
The total assets of Chinese households were 21 percent higher than the assets of households in the United States in 2010, Beijing Morning Post reported, citing Gan Li, professor of Southwest University of Finance and Economics. Federal Reserve data shows that US household assets reached $57.1 trillion in 2010, said Gan, director of the university's Chinese Household Finance Survey Center. Chinese household assets reached $69.1 trillion in the same year, Gan added. David Wise considered the data to be reasonable as China's population is four times that of the US and China's home prices were surging while US' property prices were declining at the time, Beijing Morning Post reported.
Source: Anonymous: China's household assets hit $69t, China Daily, 2012-07-09

**China will not relax property control policies**
China will continue to maintain a firm grip of its real estate market and consolidate previous achievements in bringing down home prices so as to prevent them from rebounding, according to an urgent government notice released Thursday. "Local authorities must strictly implement the nation's property control policies. They should not relax the control and relevant requirements unauthorized," according to the notice. "Those that have loosened up controls must set straight the policies," said the notice, which was jointly released by the Ministry of Land Resources and the Ministry of Housing and Urban-Rural Development. It also ordered local authorities to step up efforts in monitoring land pieces left idle even though they were sold.

The latest announcement came as the nation's housing prices and sales both showed signs of warming. Official data released Wednesday showed that 25 cities, out of a statistical pool of 70 major cities, saw new home prices rise in June from the previous month. The figure was drastically up from six cities that saw month-on-month price gains in May. "Fluctuations have appeared recently in the property market and land market. Although they have not changed the overall picture, the complexities and instabilities have increased in the market," said the notice. The notice also said that the Ministry of Land Resources will enhance monitoring of the nation's land market in order to prevent the occurrence of high-priced land pieces for both commercial and residential property. Premier Wen Jiabao said earlier this month the government must make unswerving efforts to ensure house prices return to reasonable levels and block a price rebound that would undermine the effects of previous efforts.
Source: Xinhua: China will not relax property control policies, July 20, 2012

**More Chinese firms seek delisting from US market**
The listing of Chinese companies in the United States remains stagnant, with only one IPO in the first half of this year but 19 companies delisted, a report by Ernst & Young showed on Tuesday. That's a very different story from 2010, when 42 Chinese companies were successfully listed in the US market and three were delisted. As a result, the total funds raised so far this year, at $72 million, are only 5 percent of those in the first half of 2011. Ivan Tong, assurance partner with Ernst & Young, said more Chinese companies are seeking delisting partly because the stock prices are lower than expected, thus "they would rather wait for better chances and better markets". He added that "stock exchanges in Europe have been active in attracting Chinese companies".

However, Tao Jingzhou, managing partner of Dechert LLP Asia Practice, said no markets would be available for Chinese companies unless they adopt stricter self-discipline. "Investor confidence has been heavily
affected because of a series of financial defects among US-listed Chinese companies revealed by (the recent) Muddy Waters Research (into Chinese due diligent levels)." Tao said. "The supervision standard in Europe and on other global boards is as strict as in the US, thus Chinese companies seeking listing anywhere else in the world are very much likely to face the same results as in the US," he said.

As for the US Public Company Accounting Oversight Board's requirement to examine the audit working papers of US-listed Chinese companies, Tong said that there are "procedural difficulties", as some State-owned enterprises are reluctant to allow the board to do so due to concerns over the leaking of sensitive information. But he said he hopes that regulators from the US and China could find a solution, such as allowing the Chinese authorities to conduct the inspection instead. But Tao said Chinese regulators should be more open in receiving foreign supervision. Tao said Chinese companies' financial reports need to be more transparent in order to win investors' and regulators' confidence. "The freeze for Chinese companies in overseas market may last at least two more years," he added.

Source: Wei Tian : More chinese firms seek delisting from US market, China Daily, 2012-07-4

**China commodity prices to have global impact**

Commodity markets in China, the largest user of copper and iron ore, will increasingly set global benchmarks as financial markets are opened to overseas investors, Australia & New Zealand Banking Group Ltd said. "Greater access will make domestically generated prices more influential," the bank said in a report as it introduced a commodity index based on consumption patterns in China. Having markets that are more open "will accelerate the shift from a follower of international prices toward setting global benchmarks", ANZ said.

Source: Xinhua: China commodity prices to have global impact, 2012-07-12

**China’s corporate bond market booms**

China’s economy is slowing, profits are falling and its stock market is drifting down, but its corporate bond market is moving in the exact opposite direction: it is booming. Bond issuance was up about 60 per cent by volume in the first half from a year earlier. By comparison, virtually all other forms of financing were sluggish. Equity issuance fell, new bank loans were barely up and off balance-sheet lending contracted. The fact that corporate bonds have bucked this trend is an important and positive development. It indicates that China is gradually making the transition to a direct financing model, reducing an over-reliance on bank credit that officials and analysts see as one of the major dangers for the economy. Banks have long been the primary source of capital in China. Total outstanding bank loans were 123 per cent of gross domestic product at the end of 2011, while corporate bonds were just 11 per cent of GDP, according to Credit Suisse.

A series of China’s biggest state-owned companies, from oil giant Sinopec to China National Nuclear, have taken advantage of the appetite for bonds to issue debt with coupon rates below bank lending rates. Private companies such as Goldwind and Chang’an Automobile, which traditionally have had a slightly harder time getting bank credit, have also met strong demand in the bond market. Total debt issuance by Chinese non-financial corporations was Rmb853bn ($134bn) in the first half of 2012, the most on record and up from Rmb530bn during the same period last year, according to Wind, a Chinese data provider. Moreover, the funds that companies have raised through bonds this year equate to about a third of the total that they have borrowed from banks, versus a quarter last year. This indicates that while bank financing is still dominant, its grip on Chinese corporate balance sheets is diminishing.

The major reason for this has been regulatory reform, with officials clearing away some of the obstacles that have stood in the way of the development of the bond market. China’s corporate bond market has long been divided into three separate fiefdoms. The National Development and Reform Commission, a central planning
agency, controls enterprise bonds, which are issued by state-owned companies. The China Securities Regulatory Commission manages bonds that are issued by listed companies and traded on a public exchange. And finally, the central bank oversees commercial paper and medium-term notes, which are traded only in the interbank market.

But the situation began to improve in 2008 when the central bank injected vigour into China’s sclerotic bond market with its promotion of medium-term notes. It greatly simplified the issuance process, opting for a registration system rather than an approval system – a move that forced investors, not regulators, to assess credit risks. The relative ease of issuing made a huge difference: the volume of medium-term note issuance was nearly twice as large as that of exchange-listed bonds over the past two years. The central bank’s success has, in turn, prodded the other regulators to follow its example. The securities regulator has made especially big strides this year. It has started to fast track issuance approval, cutting waiting times to just over one month. And in June it launched a new high-yield ‘junk’ bond market, adopting a registration, not an approval, system, just like the central bank. These initiatives have had an immediate impact. Exchange-listed bonds have clawed their way to be about level in issuance volume with medium-term notes this year, according to data from Thomson Reuters.

Just as vital for the development of the Chinese bond market, secondary trading has increased dramatically. Many bonds used to be held by banks to maturity, making them little different to loans. But with the increase in exchange-traded bonds, a wider variety of institutions plus retail investors have been clamouring to add fixed-income securities to their portfolios. But despite its speedy growth, this year has also served up a reminder that China’s bond market still has a lot of maturing to do. Shandong Helon, a rayon maker, was on the verge of defaulting on Rmb400m in commercial paper in April. It would have been the first major default in China’s corporate bond market, teaching investors a lesson about risk. But instead, the local government intervened and ensured that state-owned banks would bail out the company. “There have been no defaults, so everyone thinks that bonds cannot default,” Mr Shi said. “Investors are far too relaxed about credit risk.”

Source: Simon Rabinovitch Beijing: China’s corporate bond market booms, Financial Times, July 12, 2012

Netizens cry for IPO suspension
The badly performing stock market is driving Chinese investors to vent their frustration and anger online, calling for a suspension in the initial public offerings, which they believed is behind the lacklustre performance. A widely-circulated article, first posted on the popular Chinese website www.tianya.cn, called for netizens to sign an e-petition for the suspension of IPOs. Urging the security watchdog to stop companies using IPOs to maliciously seize money from the market, the author "Chanluxiaozhang" wrote, "Endless IPOs have severely hurt the interests of Chinese investors, and the country's stock market is on the brink of a collapse." As of 3 pm Thursday, the post had attracted nearly 200,000 readers and more than 10,000 of them had signed the petition. "Why should investors suffer the losses, which should have been suffered by listed companies because of their regulation violation, poor management or even fraud?" posted "zg201212" on the forum. "Cherish your lives, away from Chinese stocks," another user "Ahuatian205" joked. The topic was also simmering on China's twitter-like microblog website weibo.com. "IPO suspension will be the best solution to boost the stock market", "Gaoshandahai" wrote, saying the Chinese stock market was like a bull drained of its blood.

China's stock market has been shaken this year over concerns of a deepening slowdown in the national economy amid the global downturn. The key Shanghai index has declined more than 10 percent from its peak in February. The country's GDP expanded 7.6 percent in the second quarter of the year, down sharply from 9.5 percent a year earlier and half a point below the 8.1 percent rise for the first three months of this year. An online survey by news portal Sina.com showed 96.9 percent out of the 133,341 respondents believed that the poor performance of the stock market was partly due to continuous IPOs, while 91.8 percent think an IPO pause will
help shore up the market. However, some other commentators expressed different opinions, saying that suspending IPOs is irrational and harmful to investors’ benefits in the long term.

China Securities Regulatory Commission also hinted an IPO suspension was unlikely. "Suspending IPO launches is an administrative action, which should be avoided as the country continues to reform new share issuance regulations," the CSRC’s investor protection bureau said in a statement. The bureau noted the stock market decline was due to a lack of investor confidence during global and domestic economic difficulties, but not a result of liquidity strains. "Previous experience has proved that an IPO suspension will have no substantive bearing on boosting the market," it said. Despite the CSRC remarks, however, the commission has quietly slowed the pace of IPO reviews this month. In the first two weeks of July, CSRC reviewed IPO applications of four companies, compared to a monthly average of 32 companies in the first half of this year. To regulate the stock market, CSRC has issued a string of policies since late 2011 after Guo Shuqing took office as CSRC chairman. These included improving the delisting system for companies listed on the second board, requiring listed companies to pay dividends and working to eliminate illegal activities in stock markets.

Source: Xinhua: Netizens cry for IPO suspension, July 20, 2012

China's stocks slump to record low in 3 years
China’s stocks on Thursday slumped to record low in more than three years as fears of further economic slowdown still weighed on the market. The benchmark Shanghai Composite Index moved down 0.48 percent, or 10.15 points, to close at 2,126, while the Shenzhen Component Index lost 0.8 percent, or 73.45 points, to close at 9,081.9.

Source: Xinhua: China's stocks slump to record low in 3 years, July 26, 2012

Chinese mainland ranks 34th in innovation
The Chinese mainland has gained the 34th place in the Global Innovation Index among 141 economies worldwide, while Hong Kong ranks eighth, CRI reported. Among the top ten economies, seven are European countries; two are Asian economies, Hong Kong and Singapore; and the United States is placed 10th. This year's Global Innovation Index was released on July 3 by the European Institute of Business Administration and the World Intellectual Property Organization. The Chinese mainland ranked 30th last year. However, in the Innovation Efficiency Index, which examines how economies leverage their enabling environments to stimulate innovative results, the Chinese mainland ranked first, followed by India.

Source: Anonymous: Chinese mainland ranks 34th in innovation, China Daily, 2012-07-04

China calls for sci-tech innovation
China's top leaders have called for the country to become more innovative in science and technology, and for these systems to be reformed in a bid to build scientific power. While attending the national conference on science and technology innovation held Friday and Saturday, President Hu Jintao stressed a strategy of invigorating the country with science and technology, as well as human resources. Hu also urged China to enhance its capacity for innovation in these fields, and to integrate science and technology with social and economic development. "We must focus on promoting innovation in science and technology if we want to push forward reform and opening-up policy, the modernization of socialism, and achieve the overall target for building a moderately prosperous society in an all-round way, improve the people's living standard, as well as achieve the great rejuvenation of the Chinese nation," said Hu at the conference.

According to Hu, the targets for the development of science and technology in 2020 include building a national innovation system that conforms with the socialist market economy, significantly enhanced capacity in
original innovation, improved environment for innovation. The president proposed six suggestions for accelerating the construction of a country of innovation, including promoting innovation-driven development, improving self-innovation capacity and system for the cultivation of talented people, deepening reform of scientific and technologic system, optimizing environment for innovation, and expand international cooperation. Hu also urged authorities at all levels to expand investment in science and technology so that spending in research and development of the whole society will account for more than 2.5 percent of GDP in 2020.

Premier Wen Jiabao said at the conference that the most important work of the reform of science and technology system is to address the integration of science and technology with economy, as well as strengthen enterprises' capacity in innovation, which are of strategic importance to the long-term development of the country. For this purpose, Wen urged the government to support enterprises to build high-level research and development centers, integrate manufacturing with studies and research, build a sharing system for scientific and technologic resources, and create a fair and open market environment for enterprises. Wen also called for coordination of related policies and regulations to promote innovation.

Source: Xinhua: China calls for sci-tech innovation, 2012-07-09

'Smart city' initiatives to boost economy

"Smart city" initiatives in China are expected to attract huge money and create jobs, thus contributing to the country's economic growth, analysts said Tuesday. Investment in smart city projects might exceed 1 trillion yuan ($159 billion) by 2015, smart city specialist Jiang Defeng said. He said smart city construction takes advantage of advanced information technologies, especially the "Internet of Things", to provide fast and effective information services in areas such as traffic management, health care and environmental protection, among others. Jiang said over 300 cities nationwide have already begun to cooperate with China's telecommunication service providers to "get smart", with hundreds more likely to do so in the near future.

At a time when China is experiencing slower economic growth, building smart cities will be a huge driving force for not only the information industry but also related industries, said business owner Yang Bingzhi, who is also an adjunct professor at Zhejiang University. "The huge investment will in the long run pay off," Yang said. However, he said, China's smart city projects still lag behind developed economies, due to a lack of key technologies, high-end products and mature management.

Source: Xinhua: 'Smart city' initiatives to boost economy, July 24, 2012

Eastern promise fades as western growth soars

Traditional powerhouses splutter as inland regions go full throttle. Growth in central and western regions was stronger than the traditional coastal powerhouses in the first six months of the year. The shift was due mainly to the transfer of technology and manufacturing, a focus on infrastructure and declining exports, analysts said.

A total of 22 provinces, autonomous regions and municipalities published their first-half growth figures, after the National Bureau of Statistics reported 7.8 percent national growth earlier this month. Guizhou province, in Southwest China, registered the highest first-half growth of 14.5 percent, while Beijing and Shanghai were neck and neck with 7.2 percent expansion, the lowest score, in the first six months. While these figures would be remarkable in almost any other country they do represent a relative slowdown. "This is due to global conditions and measures initiated by local authorities to transform the economy, which, have made progress," Yan Jun, chief economist at Shanghai's municipal bureau of statistics, said. Shipped exports from Shanghai dropped 5.1 percent year-on-year, but non-store retail sales jumped 52.3 percent. "The service sector has contributed 6 percentage points to the 7.2 percent growth," Yan said, adding that the proportion of the real estate sector in the city's economy fell by 0.9 percentage points.
Most regions in East China, apart from Tianjin and Fujian, reported growth lower than 10 percent, while inland provinces were growing above that level. Guangdong province remained the largest in terms of economic clout but even here growth fell by 2.7 percentage points to 7.4 percent for the year. "Shrinking exports are having a bigger impact on costal provinces, such as Guangdong and Zhejiang," said Zhang Qizi, assistant director of the Institute of Industrial Economics at the Chinese Academy of Social Sciences.

Most economic growth in Guizhou province in the first half was driven by fixed asset investment. Guizhou's investment picked up 60 percent, year-on-years, to 346 billion yuan ($54 billion), while another 400 billion yuan is scheduled for the second half. Ministry of Commerce data showed that foreign capital flowing into central and western regions increased by 14 and 28 percent, while nationally the figure grew by 10 percent. "Investment-driven growth is still the most effective way to boost growth for the western regions, as it has a higher marginal effect than in the east," Zhang said. "The western provinces are following the same development pattern as the eastern regions did a few decades ago, receiving relocated manufacturing. "But in the long run, the western regions will eventually face the same problem the eastern provinces are facing today," he said.


Private firms eager to tap more sectors

Following the unveiling of a string of policies by the central government to encourage the opening of monopolized sectors to private investment, some private enterprises have decided to test the waters. Guanghui Energy Co Ltd, a privately held natural gas pipeline operator based in the Xinjiang Uygur autonomous region, said that it had applied for a crude oil import license, an area which is currently strictly controlled by several State-owned enterprises. "We sent the application to the top authorities quite a while ago, but have yet to receive any feedback," said Wang Yuqin, board secretary of Shanghai-listed Guanghui Energy. The Xinjiang government has set up a coordination team to communicate with the National Energy Administration and China National United Oil Corp on licensing issues, China Securities Journal reported last week. If successful, Guanghui Energy will become the first private company to have such a qualification, another breakthrough for the company after it got the green light to build a cross-border natural gas pipeline connecting Kazakhstan and Xinjiang in June last year, the first private investment in such a project.

Since May, ministries including the Ministry of Land and Resources, the Ministry of Transport, and the Ministry of Railways have announced a slew of detailed policies to materialize the "New 36 Rules" released in 2010 on private investment in State-monopolized sectors including natural resources, energy, railway construction, banking and public utilities. The government has decided to open these monopolized sectors to private capital, but it still remains to be seen whether these measures can take effect, said Shang Jiqiang, chairman of Guanghui Energy.

The company purchased a 49 percent stake in Kazakhstan-based Tarbagatay Munay LLP in 2009 to develop an 8,300-square-kilometer oil and gas block in eastern Kazakhstan. Guanghui also gained 50 percent of TMB's management rights. But the company has to import the oil and gas produced in the Central Asian country to China via China National United Oil, which is responsible for the crude oil import and export operations of China National Petroleum Corp, the country's biggest energy conglomerate, as Guanghui lacks an oil import license. "Without the crude oil import license, we have to set our production volume based on China National United Oil's import quota. It's intolerable for us," Shang said. Although the central government has encouraged private companies to import petroleum, no private company has so far managed to fully tap into the oil and gas sector, he added. Guanghui Energy remains the only privately owned oil and gas producer in the mainland. "It's an experimental move for the industry, we'll keep a close watch on how the government responds to the
application. It's a complex process that will involve financial and energy regulation," Lu said, adding that the quota, which may be much smaller than State companies', will have little effect on oil prices in the domestic market.

Source: Zhou Yan in Beijing and Shao Wei in Urumqi: Private firms eager to tap more sectors, China Daily, 2012-07-17

**China OKs private investment in defense sector**

China has pledged to further open its defense-related industries to private capital in a "fair and safe manner", according to an investment guideline unveiled Thursday. Private investors and State-owned military enterprises will receive equal treatment in multiple areas, including licensing and taxation, said a guideline jointly created by the central government's defense industry supervisor and the General Armament Department of the People's Liberation Army. The guideline also highlighted security protocols for private players involved in related industries and pledged to boost supervision in order to safeguard national security. The guidelines will only be applied to private investors on the Chinese mainland.

Source: Xinhua: China OKs private investment in defense sector, July 19, 2012

**Private investment encouraged**

China's government said on Monday that it would introduce a number of projects to allow private investment in areas dominated by State-owned enterprises. The announcement, made after an executive meeting of the State Council, said the country must "introduce some projects as soon as possible to allow private investment in the railways, public utilities, energy, telecommunications, financial, health and education industries". The move comes a week after the National Development and Reform Commission, China's top economic planning agency, and other central ministries, issued 42 new rules to attract private investment and remove barriers. The NDRC admitted on Friday that there are differences between the new rules and public expectations, and vowed to take concrete measures to boost investor confidence.

"The cabinet meeting urged several regions and government departments to take candid and effective measures to implement policies to create an environment that is fair, transparent and predictable to all market players, including private ones," the statement said. The government will study and solve the questions raised by private investors, such as lack of clarity in entry rules, and standards and conditions for private capital. It also promised further overhauls of the administrative examination and approval system.


**China economy: China's steel worries**

China's investment-led economic model has led to an unprecedented boom in steel production, but the short-term outlook for the sector is now uncertain. China was the world's largest steel producer in 2011: output reached 684m tonnes, nearly one-half of global output that year. No other nation comes close to this level of production, with Japan and the US in second and third place at 108m tonnes and 86m tonnes respectively. However, the China Iron and Steel Association (CISA), a consortium of domestic steel enterprises and related groups, estimated that China's production capacity totalled 850m tonnes at the end of 2011, underlining the problematic run-up in capacity at a time when official policy has been to eliminate outdated production capacity.

Faltering steel demand

By April the Chinese government was warning banks of the credit risks associated with lending to steel companies, not least because loans to steel companies had been used to finance investments in property and stocks. The result is that amid falling prices and faltering demand for steel, the profits of large and medium-sized
steel producers were down by 97% year on year in January-April, according to CISA. Steel output was up by just 2.2% year on year in January-May to 296.3m tonnes, with daily output in May dropping to 1.98m tonnes from 2.02m tonnes in April, leading to a flurry of news reports of growing iron ore stockpiles in ports. The Chinese authorities are suggesting that steel output will rise to around 700m tonnes this year, making it unlikely that all of the existing steel capacity will be brought into play for some years to come.

The outlook for China's steel industry is important not just for Chinese manufacturers, but also for countries such as Australia that depend on selling raw materials to China. Global iron ore producers will be particularly affected. Provinces that are particularly steel-intensive, such as Hebei, are likely to avoid ramping up new steel production capacity. Although China has more than 10,000 steel mills, only around a dozen are thought to make high-end steel, leading to the import of more than 1m tonnes a year of high-end stainless steel products. High-end steel investment is likely to be a growth area, even as the rest of the steel industry is forced to consolidate. Advancement in this area will require foreign involvement, however, as local steelmakers still rely on foreign partners, such as Japan's Nippon Steel or South Korea's POSCO, for know-how and technology to make higher-value added products such as steel sheet for cars. The government involvement that has led to the problems in China's steel sector is holding it back from becoming a more advanced, healthier industry.

Source: EIU ViewsWire: China economy: China's steel worries, Jul 2, 2012

**Chinese earnings**

Navigating hard times is a test of good or bad leadership, as the Chinese people know well. With the economic slowdown in China, corporate earnings are suffering. So is confidence. Over the past 30 days, three quarters of revisions to earnings of Chinese listed companies have been downwards. As labour costs rise and competition increases, profitability has shrivelled to the lowest level in more than a decade. Net margins at Chinese non-financial companies could fall to 4 per cent this year, down from 5 per cent last year, Bank of America notes. Poor stock control means that slowing demand has pushed inventory days up by five over the past year to 67 days.

Is the sour mood overdone? Both the Hang Seng and Shanghai Composite indices trade at about 10 times forward earnings – near the historical lows of the 2008 crisis. With margins depressed too, that often suggests stocks are poised for a rebound. But far from looking like cyclical lows, margins have been declining steadily. That makes it much harder to pick a bottom. There are also question marks over whether management teams used to only the good times can tackle rising costs and competition.


**McKinsey: Chinese firms still lack global status**

Chinese companies still have relatively low profitability and lack global status despite a record presence in the latest Fortune 500 list, McKinsey & Company said on Thursday. As economic structural reform advances and cost advantages fade away, investment-driven growth must give way to higher productivity, said the US-based consultancy firm. The average profit margin of China's 42 central State-owned enterprises on Fortune Magazine's latest annual ranking of the world's 500 largest companies by revenue was only 2.2 percent, compared with an average of 4.8 percent for non-financial companies outside the Chinese mainland.

Sinopec Group, the largest company in China by revenue, which ranked fifth globally, reported a profit margin of 2.8 percent in 2011. In comparison, Exxon Mobil, which came third on the list, had a profit margin of 8.6 percent. The mainland had a total of 70 companies on the list, overtaking Japan for the first time as the second-largest base for the world's top 500 companies. However, Xu Haoxun, a director with McKinsey China, said that less than 10 of these companies can really be regarded as "world-class enterprises". "The growth of
China's SOEs is mostly a result of their competitive edge in the domestic market, but these Chinese 'giants' face a lot more challenges when they enter the global market," Xu said. Apart from its monopolized sectors, the Chinese market has the most severe competition in the world, which has resulted in the lowest profit margins, Xu said, adding that the investment-driven growth of previous years is no longer sustainable.

Meanwhile, rising costs in the domestic market mean that managers need to pay more attention toward both human and capital costs. "The best form of defense is offence, thus taking a slice of the global market is key to the survival of Chinese enterprises," he added. To build world-class enterprises, Chinese companies need to make more efforts to improve their profitability and sustainability, and improve the efficiency of their management systems and their ability to allocate resources globally, he said. "In the next five to 10 years, China will need at least 100 CEOs with the ability to run Fortune 500 companies, 100,000 talented and experienced managers, and millions of skilled workers who can operate advanced equipments," Xu said.

The State-owned Assets Supervision and Administration Commission recently launched a program to improve internal controls in SOEs, and Xu said that McKinsey is working with the national assets watchdog to help build these companies into "world-class enterprises". Xu said that as this process continues, more SOEs will pull out from non-core businesses, offering more opportunities to private business.

"Sometimes it's not that the SOEs don't want to reform, they do face a lot of resistance," said Xu Baoli, a researcher with the research center affiliated to SASAC. The researcher said despite the SOE reform in 1998, there are still some non-performing assets, and the problem has been hidden by the rapid growth since 2003. "Coping with contraction will be a tougher mission than expansion for the management of SOEs," SASAC's Xu said. "World-class enterprises in the West evolved in an environment of complete competition, but China's SOEs have to deal with more social responsibilities, thus there isn't a universal standard," he added.


Flash PMI at 5-month peak: HSBC
A China purchasing managers' index rose in July to its highest level since February, boosted by a pick up in the pace of manufacturing output, preliminary results of a survey showed on Tuesday. HSBC's Flash China manufacturing purchasing managers index rose to 49.5 in July from 48.2 in June, rising close to the 50 level that divides expansion from contraction. The increase was driven by a jump in the output sub-index to 51.2 - the best showing since October 2011. The new orders sub-index recovered to a three-month high while new export orders gave their best showing since May, although both remained below 50. An employment sub-index fell to its lowest level since March 2009.

The flash PMI is the first significant Chinese data point in the third quarter of the year and signals that a sequential improvement in the economy in the second quarter may be broadening as pro-growth government policies gain traction. Still, the HSBC PMI has been below 50 for nine straight months, showing a need for those policies to remain in place. The PMI, compiled by UK data provider Markit, showed broad improvement across the manufacturing sector with five sub-indexes showing their rate of decline slowing and five showing a change of direction. The output price sub-index broke above 50 for the first time in five months, a sign that final demand may be lifting factory gate prices, which have been in deflation for four months. The flash PMI is based on 85-90 percent of total PMI survey responses, set to be published in full around a week later.

Source: Xinhua: Flash PMI at 5-month peak: HSBC, July 24, 2012

Zhejiang enterprises scale down output
Weak demand, rising labor costs and strained liquidity are ravaging enterprises in East China's Zhejiang province, a traditional stronghold of China's entrepreneurship, and forcing them to scale down or even halt production, a
Zhejiang government report said. The report, based on a month-long investigation and interviews with local government officials and businessmen, said the falling earnings, rising production costs and dwindling orders are now plaguing most of Zhejiang companies. In Wenzhou alone, 60.43 percent of the industrial enterprises have scaled down or halted production. In the first five months of the year, the net profit of large companies dropped 23.8 percent, for medium companies decreased 18.3 percent and for small and micro enterprises declined 14.3 percent. The report warned that the bleak situation for Zhejiang's enterprises could snap their capital chains and threatens to cripple the credit system.

Source: Xinhua: Zhejiang enterprises scale down output, July 27, 2012

**79 Chinese companies listed on Fortune 500**

A total of 79 companies in China, including Hong Kong and Taiwan, made the list of the Fortune Global 500 for the year 2012. China has exceeded Japan to be the country with the second largest number of Fortune Global 500 companies, next to the United States.

Sinopec Group, with revenue of $ 375,214 million, ranked No 5 on Fortune magazine's annual ranking of the world's largest corporations. Sinopec Group, China's biggest oil producer and refiner, is known as China Petroleum and Chemical Corp. China National Petroleum Corporation and State Grid made No 6 and No 7. Greenland Group, the only real estate developer in China making its way onto the Fortune Global 500, is ranked 483rd. Zhejiang Geely Holding Group is also a new comer to the Fortune Global 500 this year, ranking 475th. More Chinese companies will join the Fortune Global 500 group next year as long as China's economy can grow 7.5 percent year-on-year as planned by the Chinese government, the Beijing News reported, citing Fortune magazine.

Source: Anonymous: 79 Chinese companies listed on Fortune 500, China Daily, 2012-07-10

**Clinton warns Beijing on sea dispute**

Hillary Clinton has warned China that its approach to solving territorial disputes in the South China Sea, one of the world’s most important shipping routes, is a recipe for “confrontation”. The US secretary of state insisted on Thursday that territorial disputes had to be settled in a region-wide agreement that included all the claimants, rather than the approach favoured by China of conducting talks with each country. “Issues such as freedom of navigation and lawful exploitation of maritime resources often involve a wide region, and approaching them strictly bilaterally could be a recipe for confusion and even confrontation,” she told a regional summit in Cambodia. Mrs Clinton was speaking at a meeting of the Asean Regional Forum, which brings together the 10-nation south-east Asian organisation with the US, China and other Asian powers, held in Phnom Penh, Cambodia’s capital.

Since Mrs Clinton began attending the summit two years ago, it has become a forum for discussing the groups of disputed islands in the South China Sea, which Beijing claims as part of its sovereign territory but which are also claimed in entirety or in part by Vietnam, Taiwan, the Philippines, Brunei and Malaysia. Tensions have been high in recent months after incidents involving China and the Philippines, as well as Vietnam. The disputes have become a focus of international interest, given that as much as half of global ship-borne trade by volume passes through the sea, which also has potentially rich oil deposits. “No nation can fail to be concerned by the increase in tensions, the uptick in confrontational rhetoric, and disagreements over resource exploitation,” Mrs Clinton said.

At the same time as they clashed over how to resolve issues in the South China Sea, the US and China said they would work together to address sensitive issues. Yang Jiechi, China’s foreign minister, said Beijing was ready to “expand our common ground, respect each other, properly handle differences on sensitive issues” with
Washington. The US has been quietly encouraging Asean in its effort to negotiate a code of conduct for the South China Sea, which would provide a mechanism for solving disputes. US officials said the Asean nations had reached a consensus on the principles of a code of conduct and that China had now agreed to join a “dialogue” with Asean on the subject. The US views Asean’s approach to the dispute as test of its ability to function as a coherent institution. A senior US official said there were signs of Asean “maturing”. “They are neither avoiding the so-called elephant in the room, nor are they pounding their slippers on the table,” the senior official said.

Source: Geoff Dyer in New York: Clinton warns Beijing on sea dispute, Financial Times, July 12, 2012

The China-bashing syndrome; Lexington

It is a truth universally acknowledged that a man in possession of a major American political party's presidential nomination must be in want of a more assertive policy on China. Bill Clinton upbraided George Bush senior for "coddling dictators"; Mr Bush's son went on to accuse Mr Clinton, when president, of much the same thing. Barack Obama, during his first presidential campaign, called the younger Mr Bush "a patsy" in his dealings with China. Now it is Mitt Romney's turn: in February he described Mr Obama as a "near supplicant to Beijing". Mr Romney, as befits the author of a book called "No Apology: The Case for American Greatness", says that if elected he would not hesitate to put China in its place. On his first day in office, no less, he has pledged to declare it a currency manipulator, a step that could lead to across-the-board tariff increases on Chinese imports. More broadly, he says he will force China to play by the rules of international trade and investment: no more theft of intellectual property, no more unfair subsidies for state-owned firms, no more predatory pricing. And economics is not his only concern: he promises to chastise China more loudly for its human-rights abuses and to bolster America's armed forces to counteract China's growing military clout.


Rebalancing the Global Economy: [Op-Ed]

A credit surplus in wealthy countries resulted in a production surplus in emerging, export-oriented countries like China and Brazil. These imbalances have had negative effects for both sides. In the West, manufacturing has been hollowing out for decades as industrialists migrate to developing countries, where labor, equipment and materials are cheaper. Moreover, the middle class has shrunk, as the returns of a finance-driven economy have flowed to "fat cats" who control the levers of credit. In emerging economies, urbanization and industrialization have lifted hundreds of millions of people out of poverty but have also exacted a heavy toll on the environment.

The world's largest economies -- the United States, China, and the European Union -- must improve coordination on macroeconomic policies, as well as regulation and trade, and resist the temptation of protectionism. Balance must be restored: between the financial sector and the real economy; between domestic and overseas demand; between developed and developing countries. China has moved to encourage domestic consumption instead of relying solely on exports.

While it is crucial for the United States and China to bolster their own development, they also need to strengthen cooperation in trade, investment, finance, infrastructure, technology and other fields. The two economies have become highly interdependent; last year, bilateral trade topped $450 billion. Frictions are hardly avoidable, but what's important is for the two sides to handle their differences through coordination based on equality and mutual understanding. Only by acknowledging our extreme interdependence will we make the fishbowl effect work for humanity, rather than against it.

Iran/China economy: Sanctions show importance of China for Iran's economy

According to a report from Petro-Logistics, an oil consultancy, China will take up to 54% of Iran's oil exports—or roughly 590,000 barrels/day (b/d)—in July. China has become an increasingly important trade partner for Iran since 2007 when it overtook Japan as the single largest destination for Iranian exports. In 2011 China received US$30.3bn worth of Iranian exports over 75% of which was oil and related products, according to China Customs. Iran’s exports to China jumped by nearly 66% year on year in 2011, probably because oil prices rose by 39% year on year last year. China is also becoming a larger exporter to Iran. Imports of Chinese goods rose by 33% to reach US$14.8bn in 2011, mainly in the form of machinery, metals and vehicles. Imports from China may be considerably higher, though, as much of the trade between the two countries is thought to pass through the UAE, which has a valuable re-export trade, worth US$57.2bn in 2011, of which Iran received 22.5% according to data from the UAE's National Bureau of Statistics.

Trade between China and Iran appears to be somewhat disconnected from the political pressure that the US is trying to put on importers of Iranian fuel. From February to April, Chinese imports of Iranian oil and related products dropped precipitously, by an average of 31% compared with the same period of 2011. They appear to have since recovered, growing by 4.5% year on year in May and then in June surpassing the average of crude imported in 2011 (557,000 b/d) with China buying 635,000 b/d according to Bloomberg. China has managed a nuanced approach since the US announced sanctions on firms dealing with Iran's central bank at the beginning of the year, reflecting its geopolitical and business interests both in Iran and in the US. The slip in imports from February to March was thought to be more to do with Chinese buyers seeking to drive a hard bargain over the price of Iranian oil rather than yielding to US pressure.

Hydrocarbons investments’ struggling to make progress Chinese interest in Iran has not been limited only to trade partnerships. As Western firms have drawn down their investment in Iran’s oil and gas sector because of pre-existing sanctions and a challenging operating environment, Chinese companies have filled in the gap. China National Petroleum Corporation (CNPC) took over the upstream development of Phase 11 of the South Pars gasfield in 2009. CNPC also agreed in 2009 to develop the North Azadegan oilfield, with expected production of around 75,000 b/d over the next 25 years. The same year CNPC signed a Memorandum of Understanding to develop the South Azadegan oilfield, which has an expected production of 260,000 b/d. However, according to a report from Platts, an energy industry publication, none of the CNPC investments has moved beyond the Memorandum of Agreement stage owing to the difficult operating and investment climate in the country. In April 2012 Iran’s oil minister, Rostam Qasemi, threatened to kick CNPC off of the South Pars projects if it did not begin development within one month. China National Offshore Oil Corporation (CNOOC) signed an agreement in 2008 to exploit the North Pars gasfield after Royal Dutch Shell and Spain’s Repsol withdrew, but there have been reports that Iran has cancelled the contract. Work is also overdue at the Yadavaran oilfield in Khuzestan, with reserves reported at 15bn barrels, where Sinopec has agreed exploitation rights.

Facing strong domestic political pressure, particularly from right-wing groups, the US administration has gradually overcome its wariness about putting pressure on China over Iran. Last year the US blacklisted 20 Hong Kong-based shipping companies it said were fronts for the Islamic Republic of Iran Shipping Lines (IRISL), which was earlier censured by the UN for aiding Iran’s nuclear and military programmes. (IRISL has apparently continued to operate in mainland China through front companies and subsidiaries.) In January this year the US announced sanctions against Zhuhai Zhenrong, reportedly Iran’s largest supplier of refined petroleum products. This was a signal to China to fall in line with sanctions, rather than a decisive blow against Chinese trade with Iran, as Zhuhai Zhenrong has little or no business in the US. However, there are many other Chinese companies with extensive US business: Sinopec is listed in New York, as is PetroChina, a CNPC subsidiary. CNOOC and
Sinopec are also active in the US shale gas sector and will be aware that an expansion of their activities in Iran may damage their prospects in the US market.

With China being the single largest consumer of Iranian oil, stability in its appetite for Iranian crude will be crucial for Iran. Iran's fiscal position is closely linked to its oil exports, which provide roughly 60% of government revenue. At a popular level, many Iranians buy but are also resentful of the cheap Chinese goods that have flooded the market, bankrupting domestic textile and shoe manufacturers, and there are rumbles too over the quality of Chinese technology in building the Tehran metro.


Shenzhen OK'd to test freer use of yuan

Qianhai Bay zone to carry out series of innovations in financial reforms. Beijing has formally approved a $45 billion test project in the southern city of Shenzhen to allow a freer use of the yuan, underscoring its determination to make the yuan more convertible and used more often internationally. The 15-square-kilometer Qianhai Bay zone near Hong Kong deals in six categories of activity, including finance, taxation and telecommunication, and has regulations meant to emulate Hong Kong's administrative regulations.

Beijing has also announced new policies for Hong Kong. Among other things, they will allow the stock exchanges in Shanghai, Shenzhen and Hong Kong to form joint ventures among themselves and allow Hong Kong financial firms to conduct retail business in neighboring Guangdong province, which contains Shenzhen. Of the rules related to finance, one of the most important will encourage companies in the zone to experiment with making cross-border loans using the yuan. Financial institutions in the zone will be encouraged to make yuan-denominated loans to overseas companies, and lenders in Hong Kong are being allowed to extend yuan loans to companies in the zone. The rule further opens the country's capital account to international payments. At the same time, though, capital to be used in a few types of transactions in China will not be allowed to flow across borders, a policy meant to protect the country's fledgling financial market from instability. The additional means of having yuan come back onshore could bring new momentum to Hong Kong's development as an offshore yuan center. The pace of yuan transactions slowed this year in Hong Kong as expectations of the currency's appreciation weakened.

Offshore one-year non-deliverable forwards, a main gauge of expectations for the yuan's valuation, stood at 6.3980/6.4050 on Wednesday, when the People's Bank of China set the yuan at 6.3121. The figures show the yuan will appreciate against the US dollar by 1 percent in the next 12 months.

Cross-border loans will come as bargains to companies in the Qianhai zone, as offshore lending rates are lower than onshore rates. The one-year rate for lending in yuan now stands at about 4.5 percent in Hong Kong. That is substantially lower than the central bank's current one-year benchmark of 6.31 percent, despite a 0.25 percentage point reduction being approved on June 8. But money market experts said the rate difference will lead to little arbitrage and few speculative opportunities. Qianhai's economy is too small, they explained, and financial firewalls will be put in place between the zone and the rest of the country.

The central government's consent for Shenzhen means the southern boomtown is once again exploring the road of reform for the rest of the country. Three decades ago, Shenzhen, which was then a remote fishing village, set a remarkable example in China's reform and opening-up, a policy that has led to China's fast economic growth in the past 30 years. Many policies have been tried out in Shenzhen and later introduced to other inland cities, such as Shanghai and Beijing.

Many believe Qianhai will be a competitor to Shanghai, which has said it wants to become a global financial hub by 2020. Lu Zhengwei, chief economist with Industrial Bank Co Ltd, disagreed. He said Shanghai
will be a partner of Qianhai and that many new measures will be tested in Shenzhen before being introduced in Shanghai. In fact, the central government has already consented to Shanghai's plan to become a global center for yuan trade by 2015.

Source: Gao Changxin in Shanghai: Shenzhen OK'd to test freer use of yuan, China Daily, 2012-07-05

**Yuan included in Trade Finance Program**

The likelihood that yuan will be used more widely in settling intra-regional transactions has prompted the Asian Development Bank to include the currency in its Trade Finance Program. ADB's Board of Directors on Tuesday approved the inclusion of the renminbi and Indian rupee in the program, which "fills market gaps for trade finance by providing guarantees and loans to banks to support trade", it said.


**Sovereign wealth fund suffers losses in 2011**

The China Investment Corporation, the nation's sovereign wealth fund, said Wednesday its overseas portfolio yield for 2011 stood at negative 4.3 percent due to slow recovery of global economy and the European debt crisis. The accumulated annualized return since its founding in 2007 stayed at 3.8 percent, according to its 2011 annual report. The fund confirmed it received $30 billion of cash injection from the State Administration of Foreign Exchange, which meant the latter had become the shareholder of the fund. But the company said the move would not affect company's independence in investment decisions.


**SAFE 'to invest $500m' in Blackstone property fund**

China is strengthening its efforts to diversify the world's largest foreign exchange reserves and increase returns on its portfolio by investing in a private-equity fund. The State Administration of Foreign Exchange has decided to invest $500 million in a real-estate private-equity fund managed by Blackstone Group LP, the Wall Street Journal reported on Friday, citing anonymous sources. The fund that SAFE has agreed to invest in is the biggest of its kind, as it has attracted more than $12 billion. Blackstone expects the fund to reach $13.3 billion at the final close in the next few months. Both SAFE and Blackstone declined to comment on the issue.

The newspaper said SAFE will allocate about 5 percent of the $3.2 trillion foreign reserves to alternative asset classes such as private equity, while investment in government bonds, cash and other liquid assets remains the main trend. The diversification of China's foreign exchange portfolio is vital for the country to maintain the value of its assets, said Zhang Anyuan, a senior analyst at the economic research institute under the National Development and Reform Commission. In 2008, the foreign reserve watchdog poured $2.5 billion into a fund managed by the US-based private-equity firm TPG and suffered losses after the fund's subsequent investment in Washington Mutual, the largest US savings-and-loan firm at the time, was wiped out after the lender's closure by the US government, the Wall Street Journal reported. SAFE has constantly reiterated that security is its top priority when making investments using foreign reserves, and it has already taken appropriate measures to offset potential major risks.

It has invested most of the reserves in low-yield assets such as government treasury bonds. China is the largest foreign holder of US Treasuries, having invested about a third of its foreign reserves in those bonds. About 20 percent has been invested in euro-denominated assets.

In February, the Blackstone's Real Estate Partners VII Fund will stop raising capital. Its Real Estate Partners VI invested the majority of its capital in business property in the United States, such as shopping mall-owner General Growth Properties Inc and hotel-owner Extended Stay. But some recent figures have raised doubts over
future returns. According to the results of a primary mortgage market survey released by Freddie Mac on Friday, fixed mortgage rates continue to reach record lows. The 30-year fixed rate mortgage averaged 3.49 percent, while the 15-year fixed-rate mortgage, a popular choice for those looking to refinance, hit a record low of 2.8 percent.

Trade grows 8% in first half
China's trade in the first half of the year grew 8 percent to hit $1,839.8 billion, the General Administration of Customs said on July 10 at a news conference. China's exports grew 9.2 percent, while imports grew 6.7 percent in the first half. Trade surplus increased 56.4 percent to reach $68.9 billion. The result, though short of the 10 percent annual growth target set by the Commerce Ministry, is better than previously expected, especially because trade growth dipped to 2.7 percent in April. However, the figure rebounded in May, when trade volume grew 14.1 percent. The rebound continued in June, with trade volume growing 9 percent. In June, China's exports grew 11.3 percent to $180.2 billion, while imports grew 6.3 percent to $148.5 billion. In the first half, the United States overtook the European Union as the largest export destination for China.
Source: Zheng Yangpeng: Trade grows 8% in first half, China Daily, 2012-07-10

China's Rx: Foreign-Owned Hospitals
The Chinese government announced in March that it wants 20% of the nation's hospital beds to be privately owned by 2015. With 260 million Chinese suffering from cancer, diabetes, and other chronic diseases, Beijing wants private investors to help upgrade medical services in a hurry. One draw for private operators is that 95% of Chinese had government-provided health insurance in 2011. Besides the big increase in the proportion of beds run by private operators -- it was 12% last year -- the government wants at least one or two hospitals in each of its 2,853 counties by late 2015. US- and European-owned companies have only been able to independently invest in hospitals since Jan 30, when the government took the industry off a restricted list that required non-Chinese investors to have a local partner and capped foreign ownership at 70%.

Invest in China: A Guidebook for Application and Approval of Foreign Investment Projects and Business Scope, the Invest in China Guidebook Series (3) (Second Edition)
Access China Management Consulting Ltd has worked hard to the second edition of the Guidebook Series for Investing in China in order to deal with the latest revised most key regulation, Catalogue for the Guidance of Foreign Investment Industries, which determines the license of industrial access for foreign companies and investors entry into the Chinese lucrative market and low cost manufacturing base.

Invest in China: A Guidebook for Application and Approval of Foreign Investment Projects and Business Scope is the third one of the Guidebook Series for Investing in China. It will focus on the application and approval of foreign investment projects and business scope, which is the most complex procedure in the process of setting up a foreign investment enterprise. It provides not only a comprehensive and thorough knowledge of the latest Chinese laws and administrative regulations, but also the guidance of practical operation for application and approval of foreign investment projects and business scope for foreign companies and investors.

Chapter 2 will address the Chinese government authorities for examination and approval of foreign investment projects and business scope for foreign investment enterprise, and sketch an organizational chart of the government authorities for examination and approval for investment projects and business scope from the
central government authorities, the government authorities of provinces, autonomous regions, municipalities directly under the Central Government to local government authorities. The aim of this chapter is to give direction of gateway for application and approval of investment projects and business scope for foreign investment enterprise.

Chapter 3 will elaborate the entire process of setting up a foreign investment enterprise in China, because the application and approval of foreign investment projects and business scope is the most significant procedure in the process of setting up a foreign investment enterprise.

Chapter 4 will introduce the applicable Chinese laws, administrative regulations, including the departmental regulations and rules, for application and approval of foreign investment projects and business scope for foreign investment enterprise. With the help of these various laws, administrative regulations, including the departmental rules and regulation, audience can clearly acquire a comprehensive and thorough knowledge of the latest Chinese laws and administrative regulations for application and approval of foreign investment projects and business scope, and lay the foundation for practical operation for application and approval of foreign investment projects and business scope for foreign investment enterprise.

Chapter 5 will introduce the practical operation for application and approval of foreign investment projects to guide investors step by step to go through the approval of the Chinese government authorities smoothly.

Chapter 6 will introduce the practical operation for application and approval of business scope for foreign investment enterprise in manner for case by case to guide foreign investors step by step to go through the approval of the Chinese government authorities smoothly.

The guidebook concludes in Chapter 7 by highlighting the significant suggestions for foreign companies and investors looking to achieve a successful application and approval for foreign investment projects and business scope for their companies and enterprises in China.

The another fascicle of the Guidebook Series for Investing in China--- Collection of Chinese Laws and Administrative Regulations for Application and Approval of Foreign Investment Projects and Business Scope will provide the full text in English of variously existing latest in effective Chinese laws, administrative regulations and rules, and departmental regulations and rules for application and approval of foreign investment projects and business scope for foreign investment enterprise, which is associated with this guidebook.


Companies have home thoughts from abroad
Companies, including General Electric, have defended their efforts in reshoring - moving work back to a company's country of origin - by citing a variety of factors. These include lower energy costs in the US, largely due to discoveries of natural gas, that are helping to drive down operating and transportation expenses and labor-cost advantages caused by the narrowing wage gap between Chinese and US workers. The steady appreciation of the yuan has also diminished the currency-exchange advantage that made China a hugely successful exporter.

With this latest twist in the global hunt for supply-chain efficiency, the expected increase in consumption among China's 1.37 billion people could provide a lucrative market for factories originally designed to produce goods for export to the US, an established practice known as offshoring, or offshore outsourcing. "Today we see an economic situation where a strong case can be made for many products - that they should be made closer to the customers," said William Scheller, a professor of industrial engineering at Kettering University in Michigan.

GE's Chairman and CEO Jeffrey Immelt has led the industrial conglomerate's reshoring initiative. One
notable example has been the addition of more than 1,000 jobs to GE's "lean manufacturing" site for large household appliances in Louisville, Kentucky. The company said offshoring has ceased to provide the cost savings that once justified overseas production of refrigerators and washing machines that were subsequently shipped to the US. GE also received tax breaks of $17 million from the state and local governments to entice it to add the jobs in Louisville.

The consistent expansion of the Chinese consumer market, despite slower-than-expected growth in the economy overall, has made it economically sound for GE and other US manufacturers to retool their factories in China to produce goods for the local market while also returning jobs to the US. "With China growing at 7 percent now, the US or European companies are not closing down plants in China, because of its rising (domestic) consumption," said Harold Sirkin, a senior partner at Boston Consulting Group in Chicago. "They are retooling their plants in China for Chinese consumption. In some cases, they are building more plants in China."

According to a recent survey by BCG, more than one-third of US-based manufacturers with yearly sales of more than $1 billion have plans to repatriate some production from China, or are at least considering such a move. A total of 106 companies across various industries took part in the survey, which cited "labor costs" as the prime reason for reshoring, while "product quality", "proximity to customers" and "ease of doing business" were other important factors. "In 2015, for a certain amount of goods imported, the cost of production in China will be 10 percent lower than the cost of production in the US. The difference is only 10 percent, and can be offset easily," Sirkin said.

Immelt, who heads President Barack Obama's Council on Jobs and Competitiveness, has since 2009 announced plans to create 11,000 manufacturing jobs in the US. GE officials, including the CEO himself, have insisted the company's reshoring moves have nothing to do with politics. "Part of what's going up in China we are able to bring down in the US," Freeman said, pointing to the "competitive wage agreement" the appliances division reached in 2011 with its unionized US workforce. For the first time, GE Appliances employees will work according to a two-tier wage structure under which those hired after 2005 earn $13 an hour while the hourly pay of longer-serving employees begins at $22. Equally important, Freeman said, is the "lean manufacturing" concept GE has followed in order to "eliminate waste in processes or materials, and to improve product quality in the same time". Redesigning its product line has helped lower production costs, according to Freeman. A water heater, production of which was moved to Louisville from China, is now more energy-efficient and less expensive, retailing in the US at $1,199 to $1,299 compared with $1,399 when it was imported.

GE officials said no Chinese factories were closed, nor were workers laid off. Appliances is a small part of the company's business, and any change in manufacturing locale has a limited effect on its Chinese operations, said Geoff Li, a spokesman for GE China. GE's revenue from operations in China in 2011 was $5.7 billion. That's a small fraction of its global revenue, but represents 20 percent growth in each of the 10 years since 2002 when the number was roughly $1 billion. In late May, the company opened its second research-and-development facility in the country, the China Innovation Center in the Southwestern boomtown of Chengdu. The new R&D center will enable GE to connect more directly with consumers across Asia, leading to products made specifically for them and based partly on their input. "The future in China will be innovation, not just low-cost manufacturing. The goal now in China is to localize, make the products simpler, and make the products more suited for Chinese development," said Immelt when he visited Chengdu for the center's opening.

Georgia-based NCR Corp, which makes ATMs and point-of-sale electronic devices, built a plant in the US state of Georgia to redirect production in 2009. The NCR plant in China, which used to produce ATMs for US customers, now serves its growing Chinese market and other countries in the Asia-Pacific region. The company wants to "meet the needs of the local market - whether in China, the US or Brazil", said Peter Dorsman, NCR's executive vice-president of global operations. "We are always concerned about rising costs in China, but these
are things you can't control. We try to focus on the ones that we can control," he said. NCR's Chinese market is "definitely growing a lot faster" than its US counterpart, Dorsman said. By 2015, the ATM installation base in the US is expected to have grown by 4 percent, while in China the rate will have soared by 160 percent, according to Retail Banking Research, which provides information about automation in the banking industry. Dorsman said NCR plans to add production capacity in China, either by increasing employee shifts or the number of production lines.

"We have noticed that some US companies have moved their manufacturing businesses back to their homeland from the Pearl River Delta. But these companies are traditionally concerned with lower-end manufacturing," said Feng Shengping, chief researcher with the Guangdong Situation Research Center. The reshoring trend has been well demonstrated by China's utilization of US investment in recent months, with the number of new companies approved by the Chinese authorities falling by 4.5 percent year-on-year to only 571 in the first five months of this year, according to sources with the Ministry of Commerce. Referring to US reshoring, Feng warned the authorities in Guangdong not to simply relocate traditional manufacturing businesses to other regions following a province-wide industrial upgrading policy adopted three years ago. "Only through developing a healthy industry chain including research, finance, processing and market distribution can you improve competitiveness amid the downturn," he said.

Source: Joseph Boris, Ariel Tung and Qiu Quanlin: Companies have home thoughts from abroad, China Daily, 2012-07-11

**China's FDI falls 6.9% year-on-year**

China's foreign direct investment in June reached $12 billion, a year-on-year drop of 6.9 percent, the Ministry of Commerce said on Monday. In the first half of this year, China utilized $59.1 billion of foreign direct investment, a decline of 3 percent over a year earlier.

Source: Xinhua: China's FDI falls 6.9% year-on-year, 2012-07-17

**Extra effort needed on China-US investment**

Restricted market access and an insufficiently transparent regulatory environment are impeding Chinese investment in the United States as well as US investment in China, and the investment issue will be a major item in future bilateral economic dialogue, a senior economist said at the conclusion of the third US-China Investment Cooperation Forum on Thursday. "Market access restrictions, a regulatory environment that is not transparent and stable enough, and unfair treatment during enforcement: these factors exist both in the US and Chinese markets," said Wei Jianguo, secretary-general of the China Center for International Economic Exchanges. The US-China Investment Cooperation Forum is co-hosted by the CCIEE, a think tank under the National Development and Reform Commission, and the US Chamber of Commerce. This year's meeting involved more than 300 government officials, entrepreneurs and scholars from both sides. Wei said both sides recognize the relatively slow growth and small size of mutual investment.

The US is the fourth-largest source of foreign direct investment in China. Total investment in China from US companies stood at $70 billion at the end of 2011. But China, though it is the second-largest trading partner of the US, remains a relatively small investor in the country. By the end of 2011, China's total investment in the US was less than $10 billion. At the forum, US political and business leaders' eagerness for Chinese investment was keenly felt. Myron Brilliant, senior vice-president for International Affairs at the US Chamber of Commerce, said one of its "major missions" at the forum was to show that the US is open to Chinese investment. Brilliant said the vast majority of Chinese investment in the US does not trigger national security or political concerns. There is some in the high-tech industry, but the "overwhelming" proportion of Chinese investment in the US
does not lead to national security concerns, he said. Wei said Chinese companies are aware of the huge potential of investing in the US. But the major concern they expressed during the forum was the lack of transparency during the review process for foreign mergers and acquisitions. "They are eager for clear information, for example, regarding which areas are restricted and which areas are not," Wei said. "We should learn about the US cultural and legal framework, which is different from ours. We should invest in the real economy which can bring job opportunities and tax revenue to them," said COSCO Group President Wei Jiafu. "Another issue is keeping in contact with labor unions."


**Govt stresses quality for FDI, ODI**

China will shift its direct-investment focus, both foreign and outbound, to quality instead of quantity, an economic planning guideline said on Tuesday. The National Development and Reform Commission, the country's top economic planning agency, outlined the nation's FDI and ODI development plan for the 12th Five-Year Plan (2011-15). The commission vowed to bring home advanced foreign technology, talent and management when attracting foreign capital. A government policy document called for quality FDI, and encouraged multinationals to set up R&D, procurement and financial management centers in China. To that end, China will encourage multinationals to set up regional centers, R&D centers, procurement centers and financial management centers. China will also encourage foreign companies to invest in advanced service sectors, such as modern logistics, software development, engineering design, consultancy and intellectual property service industries, the document said. The country will strictly limit foreign investment in industries that consume a lot of energy and resources, and high-pollution industries.

The guideline acknowledged several hurdles to meeting this goal. One major problem is the inability to transform the large amount of FDI to China's own technological strength. "In past years, the surging FDI preferred single ownership in China, which made the technology spillover effect hard to occur," Huo said. "Other joint ventures, targeting China's labor advantages or the consumer market, provided few chances for technology spillover." The document said the government will guide foreign capital into healthcare, culture and tourism sectors, but will be more cautious in finance, securities and telecommunications.

While stressing attracting quality foreign investment, the document also urged improving the quality of outbound investment. It said China will encourage investment in overseas high-tech and advanced manufacturing. The country will also seek to acquire foreign intellectual property rights through acquisitions, equity participation, joint ventures, and establishment of its own overseas R&D centers. Energy, mining and agriculture are identified as the key sectors that Chinese investors are encouraged to invest in abroad. Meanwhile, the document also noted difficulties facing China's outbound investment. "As China's might increases, there is growing skepticism toward China's overseas investment and subsequent restrictive practices," the document said. Political instability in some countries also raised the potential risks of China's investment, it added. Zhang Jianping, a researcher with the Academy of Macroeconomic Research under the NDRC, said encouraging more private and small and medium-sized enterprises to engage in foreign investment is a way to counter the skepticism and restrictions, which China's State-owned enterprises often encounter. "The government should offer more consulting for private firms and SMEs which aspire to invest abroad, and match up SOEs and private firms to jointly explore the foreign market," Zhang said.


**More channels open for foreign investors**

More financial channels in the Chinese mainland are being opened for foreign investors, in a move to better
support stable economic growth. The China Securities Regulatory Commission agreed at the weekend to further lower the requirements for market access for qualified foreign institutional investors. The move is based on the stance of "deregulation with strengthened supervision". The regulator encouraged long-term investment capital, including foreign pension funds, to be injected into the domestic market by choosing multiple trade brokers. Investors with QFII quotas can also invest in the inter-bank bond market, as well as in privately raised corporate bonds for small and medium-sized enterprises, the CSRC said. Overseas fund providers can hold 30 percent of the stocks of one company, compared with 20 percent before, which is a signal of an advanced opening-up reform to roll up the domestic capital market in the future, said a statement from the commission. On July 20, the State Administration of Foreign Exchange approved a QFII quota of $1.2 billion for six new foreign institutional investors. At the end of last week, 149 foreign institutions had received QFII approval in the mainland with a total quota of $28.53 billion, data from SAFE showed.

Source: Chen Jia: More channels open for foreign investors, China Daily, July 31, 2012

M&A cools in China, heats overseas

In the first half of this year, a total of 422 mergers and acquisitions deals were completed in China, down 21.3 percent year-on-year, according to Zero2IPO Research Center. Among them, 366 deals disclosed prices, hitting $28.65 billion, down by 22.03 percent from the same period of the previous year. Outbound M&As numbered 60 in the first half at a total price of $19.42 billion, up by 23.8 percent.

Source: Anonymous: M&A cools in China, heats overseas, China Daily, 2012-07-05

China's H1 outbound direct investment surges 48%

China's outbound direct investment in the non-financial sector hit $35.42 billion in the first half of 2012, up 48.2 percent year-on-year, the Ministry of Commerce said Tuesday.

Source: Xinhua: China's H1 outbound direct investment surges 48%, 2012-07-17

CHINA: Inexperience complicates overseas investment

Chinese investors in mature economies have run into vociferous criticism by community groups and unions. In the Australian mining sector, one of the most attractive targets for Chinese foreign direct investment (FDI) given the Chinese construction boom, investors have been criticised for failing to address the concerns of minority shareholders, employees and local communities when establishing new operations. This lack of attention to stakeholder engagement results from the fact that the Chinese investors are mainly state-owned firms who have the full support of government in their home market and have had a limited history of involving lower-level stakeholder groups when making business decisions.

Chinese firms may prefer direct investment in developing countries, where slow and costly stakeholder engagement is less necessary. Chinese investors will prefer to enter into joint ventures with local firms to ease their entry into mature foreign markets. During the last seven years, China's outbound FDI has increased 30-fold. Although Chinese FDI stocks now amount to 230 billion dollars, this only accounts for 1.2% of the total worldwide stock. It is likely to increase sharply if China follows the pattern of a typical emerging economy: the global stock of Chinese FDI is forecast to reach 1-2 trillion dollars by 2020.

Over the last five years Chinese companies have invested over 15 billion dollars in Australia, most of which has been concentrated in the resources and mining sector (see CHINA/ AUSTRALIA: Business trumps security divide - June 26, 2012). They have faced criticism for ignoring the voices of unions and aboriginal communities when establishing new operations, and have faced significant difficulties operating in the country. In response to growing anger from local stakeholder groups, Chinese investors have begun to acknowledge that they must
engage effectively with stakeholders when developing new mining projects. For example, Citic Pacific Mining, now in the process of developing the world’s largest magnetite iron-ore mine at Cape Preston in Western Australia, has promised to develop partnerships with local communities including indigenous aboriginal communities and deliver long-term economic, social and environmental benefits. They have also indicated their intention to source locally and use local employees. A recent survey highlights growing opposition to Chinese FDI among Australian citizens. Although the majority recognised the contribution of Chinese investment to the Australian economy, some 57% believed that Australia had become too reliant on it. In part as a response to such misgivings, the Australian government has made it harder for Chinese firms, especially state-owned enterprises, to undertake investment in the mining and resource sector. The approval process for investment from state-owned enterprises is more onerous than that for private investors given Australian government fears that the Chinese government is driving foreign investment in the resources sector for strategic reasons.

Foreign governments will scrutinise Chinese investors more carefully when deciding whether or not to grant them regulatory approval to undertake FDI. They will increasingly require firms to explain how they will work constructively with stakeholder groups to minimise the negative impact of their business activities on the local community, and comply in full with labour laws and regulations. This will increase the time it takes for Chinese firms to seek regulatory approval for foreign investment projects and may discourage them from acquiring assets overseas.


**China Push In Canada Is Biggest Foreign Buy**

Cnooc Ltd. swept into Canada with China's biggest overseas acquisition yet, a $15.1 billion deal to buy one of that country's largest energy producers that reignites a debate over the role of Chinese state players in North America's energy industry. If completed, the deal for Canada's Nexen Inc., would mark China's most ambitious push into the continent's oil and natural-gas fields. It would give Cnooc a key role in technologies reshaping the energy landscape and open the door for it to operate in North American fields alongside such oil-and-gas giants as Exxon Mobil Corp. and Statoil ASA. The deal, approved by Nexen's board, faces government and regulatory reviews in Ottawa and Washington, D.C. Nexen has considerable operations in the U.S. Gulf of Mexico, and U.S. officials are likely to scrutinize any change of ownership there.

Even in Canada, a country more accustomed to big Chinese investment in its oil patch, the deal could face heightened scrutiny. The offer is several times larger than any previous Chinese investment in Canada and nearly equivalent to total China investment in the province of Alberta, excluding real estate, according to Gordon Houlden, head of the University of Alberta's China Institute in Edmonton. "It is another order of magnitude" from previous deals, he said.


**Chinese investment in US ’set for record year**

Chinese investment in the United States is expected to hit a record high this year, thanks largely to big-ticket items, according to a report from the Rhodium Group, a New York-based organization that analyzes global trends. Chinese foreign direct investment, or outbound FDI, in the US reached $3.6 billion in the first half of this year, and covered 33 projects, the report said. Of these, 12 were acquisitions and 21 involved green-field investments (the construction of new facilities). The first six months of 2012 saw a record investment for any half year from China.

Major projects targeted by Chinese FDI this year include the $2.5 billion purchase by China Petroleum and
Chemical Corp, or Sinopec, of a one-third stake in five shale oil and gas fields across the US from Ohio-based Devon Energy. Copper-tube producer Golden Dragon also broke ground on a $100 million manufacturing facility in Wilcox County, Alabama. The banking sector also saw movement with the acquisition by Industrial & Commercial Bank of China of 80 percent of Bank of East Asia's US operations for $140 million.

Two headline-making investments were not included in the report: Dalian Wanda Group’s $2.6 billion acquisition of US movie-theater operator AMC Entertainment Holdings and Superior Aviation Beijing Co’s $1.8 billion bid for aerospace company Hawker Beechcraft in early July. While Super Aviation is still awaiting approval from US authorities (Hawker remains in federal bankruptcy proceedings in New York), Wanda and AMC announced Wednesday that they received approval from the Committee on Foreign Investment in the US. That, along with clearances from Chinese and other US authorities, mean the deal should close as planned by the end of August, according to Wanda. If the Super Aviation deal is also approved, these investments would push total Chinese FDI in the US beyond $8 billion this year and that does not include projects in the pipeline. While Chinese investors continue to pour money into a range of industries, a few sectors specified in the Rhodium report, including oil and gas, which, led by the Sinopec-Devon deal, accounted for the bulk of Chinese FDI in the US. "The US has rich natural and technological resources. If it’s fully open to foreign investors, Chinese investment will see significant growth in these two fields, especially in acquiring technology," Ge said.

Besides big-ticket projects, Rhodium Group pointed to recent positive developments in investment policy, both in the US and China. It cited US President Barack Obama’s order to increase visa-issuing capacity in China by up to 40 percent in 2012 and official statements welcoming Chinese participation in US infrastructure development during the May US-China Strategic and Economic Dialogue.

Rhodium’s Hanemann said there is deep concern in the US over Chinese FDI in the telecom sector, and recent incidents involving ZTE mean such sentiment won’t fade anytime soon. The company was recently accused of selling equipment to Iran from US companies Hewlett-Packard Co, Dell Inc, Cisco Systems Inc and Juniper Networks Inc, in violation of US export controls.


World News: Deeper Slowdown Suspected in China
Coming hard on the heels of a weak jobs report in the U.S in June, and fading business sentiment in European economic powerhouse Germany, fresh evidence of slowing growth in the world’s second-largest economy would be a further blow to an already fragile global recovery. If, as some economists suspect, growth is even slower than the official data suggest, that would compound fears that China is poorly placed to help lift the world economy out of its slump.

Economists have responded to long-standing doubts about the reliability of official data by constructing their own indexes of China's growth. London-based research firm Capital Economics created its own index during the last major downturn during the 2008-09 crisis. Capital Economics's proxy indicator suggests that China's economy grew by around 7.6% in the first quarter of this year, half a percentage point lower than the official GDP figure.

Under the new approach, in place since February, China’s biggest 700,000 enterprises report data directly to the NBS over the Internet. That replaces a system where many reported to local statistics offices, and information was then transmitted from town, to city, to province and to national levels. The latest approach is intended to overcome one of the main flaws in China's data system -- exaggeration of the growth rate by ambitious local officials. A notice on the National Bureau of Statistics website in February announcing the change called on businesses to "submit data independently, resisting any attempts at interference." That warning
to avoid interference may have been prescient. A report in the Chinese press in April, reproduced on the NBS website, cited many instances of abuse of the new system, with some local officials requiring businesses to coordinate with local statistical offices before reporting their data, effectively reintroducing the possibility of political interference. Recently, doubts have been raised that electricity-production data -- widely viewed as a reliable proxy for growth, also may be subject to political interference.


CHINESE FIRMS MORE THAN TRIPLED INVESTMENT IN EUROPE IN 2011

In 2011, Chinese firms invested $10 billion in Europe, more than triple the $3 billion they invested in 2010, according to a recent report by economic research firm Rhodium Group. Chinese firms have now invested in more than 30 sectors across Europe. Communication equipment and services, industrial machinery, and renewable energy are among the industries with the most Chinese investment. Geographically, Chinese investments are concentrated in Western Europe's largest economies like France, the United Kingdom, and Germany. Firms investing in the European Union seek European businesses' brand equity and technological edge, Europe's more advanced and business-friendly regulatory system, and price advantage from a weak Euro to compete in China, according to the study. The study says that Chinese firms' direct investments today are driven mostly by commercial, not political, motives. The authors conclude that Chinese businesses are less affected by government and politics than many observers believe.

While total Chinese overseas foreign direct investment (OFDI) is still small compared to US or European OFDI- Chinese OFDI is $300 billion compared to the United States' $4.8 trillion - the study projects that China will invest $1-2 trillion internationally from 2010 to 2020. (For more on Chinese OFDI in the United States, see p. 18.) Through new investment projects in particular, Chinese OFDI is predicted to create significantly more jobs for workers in the European Union. Chinese companies in Europe currently employ 45,000 EU workers. By comparison, US firms in Europe count 4.3 million EU citizens on their payrolls.