China News in Brief
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Compiled by Yimin Zhang, University of Shanghai for Science and Technology and distributed free of charge.
May CPI eases to 3.0%

China's consumer price index (CPI), a main gauge of inflation, slowed to 3.0 percent year-on-year in May, the National Bureau of Statistics (NBS) said Saturday. It marked a 17-month-low, easing from April's 3.4 percent and 3.6 percent in March. Compared with the previous month, it edged down 0.3 percent in May, the NBS said. The CPI climbed 3.5 percent in the first five months compared with the same period of last year. Food prices, which account for nearly one-third of the weighting in the calculation of China's CPI, increased 6.4 percent last month from one year earlier, down from 7 percent in April. On a monthly basis, food prices dropped 0.9 percent from April, the NBS said.

Meanwhile, China's Producer Price Index (PPI), a main gauge of inflation at the wholesale level, fell 1.4 percent in May from a year earlier in response to falling global commodity prices. It fell deeper than April's 0.7 percent, and marked another month of decline year on year after China's PPI saw a drop in March for the first time since December 2009, NBS data showed. China's economy cooled to a three-year low of 8.1 percent in the first quarter as a result of sluggish exports, the domestic property market and its self-gearred slowdown of fixed-asset investment. Since the government’s policy shift to shore up growth has become all the more necessary and the NDRC has ruled out the possibility of launching a massive stimulus package featuring large-scale investment projects, analysts expected that more monetary easing will be implemented to put growth on track.

Source: Xinhua: May CPI eases to 3.0%, 2012-06-09

Second Month of Slow Economic Growth in China: [Foreign Desk]

Growth in industrial production, retail sales and investment in fixed assets like factories and office buildings was little changed from April, according to data released on Saturday afternoon in Beijing by China's National Bureau of Statistics. Some economists had considered the April figures to be a fluke and had predicted a rebound in May, when the Chinese government began measures to rekindle growth. April had been the weakest month in China since 2001 for growth in fixed-asset investment, and May was slightly weaker still. Before adjustment for inflation, retail sales grew even more slowly in May than in April.

One of the most reliable proxies for growth has been electricity generation, because a handful of big companies dominate the industry and report data directly to Beijing. Electricity generation grew only 3.2 percent in May compared with a year earlier, the National Bureau of Statistics said on Saturday, far short of its usual double-digit pace. That was up from year-over-year growth of 1.5 percent in April. Excluding the effects of the Chinese New Year, April and May were the two slowest months for growth in electricity generation since the spring of 2009, when many export factories temporarily closed during the global financial crisis. Since China relies on coal to generate four-fifths of its electricity, very slow growth may have a small environmental benefit, by slowing emissions of toxic gases and global-warming gases.


China to 'maintain 8% growth for over 20 years'

China still enjoys huge development potential and will maintain the eight-percent growth rate for at least another
20 years, Justin Yifu Lin, former chief economist of the World Bank, said Monday. Lin made the remarks at a seminar at Peking University, his first public appearance in the country after he finished a four-year tenure as World Bank chief economist and senior vice president. Lin said that developing countries should promote the growth of industries where they have comparative advantages, while governments will play a key role in selecting and developing those industries. "At each given stage of development, the market is the fundamental mechanism for effective resource allocation, but the state needs to play a proactive, facilitating role in the move from a lower stage to a higher stage,” Lin said.

Source: Xinhua: China to maintain 8% growth for over 20 years', 2012-06-19

**China PMI Falls, Points To Need for Stimulus**

The HSBC China Manufacturing Purchasing Managers' Index fell to 48.1 in June compared with a final reading of 48.4 in May. It was the eighth straight month of a reading below 50, which indicates contraction, though Qu Hongbin, HSBC chief economist for China, noted that the pace of slowdown had eased slightly. The drop was mainly driven by a further deterioration in new export orders, which fell by 2.6 points to 45.9 in June--the lowest reading since March 2009. Total new orders also slid to a seven-month low of 46.8 in June compared with 47.9 in May. China's economy slowed to 8.1% in the first quarter of 2012 compared with a year earlier, the slowest pace since the spring of 2009, and a number of analysts are expecting a further decline in the second quarter to roughly 7.5% year-over-year.

HSBC said China faces continued weakness in its key export markets, noting that the European debt crisis is still far from over while the U.S. is hampered by slower employment data and consumer spending growth.


**Prudent' monetary policy to go on**

China's central bank governor says the country will continue with its "prudent" monetary policy and fine-tune it to cope with economic conditions, even as drops in industrial profit levels accelerated in May. Speaking on Friday to the annual Lujiazui Forum in Shanghai, a three-day gathering of the country's top financial officials and executives, Zhou Xiaochuan, governor of the People's Bank of China, also said China would step up efforts to reform its financial markets as well as its interest rates and the yuan's exchange rate. "The country will continue adopting prudent monetary policies, though timely and measurable fine-tuning will be made," he told delegates at the forum at which officials and executives are meeting to discuss financial reforms. The Lujiazui Forum started as the National Bureau of Statistics said on Friday that combined profits at the country's major industrial enterprises were 390.9 billion yuan ($61.5 billion) in May, down by 5.3 percent year-on-year, and accelerating from a decline of 2.2 percent in April. In the first five months of the year, industrial profit also dropped 2.4 percent year-on-year to 1.843 trillion yuan. This week, the People's Bank of China is expected to inject a total of 197 billion yuan into the banking system through reserve repurchases.

Also at the forum, Hu Xiaolian, the central bank's vice-governor, cautioned delegates of systemic risks involved with the yuan's use in international trade and investment. She said that the central bank will set up a system to identify and monitor such risks and use market-based tools to manage them.

Source: Gao Changxin in Shanghai: 'Prudent' monetary policy to go on, China Daily, 2012-06-30

**Changing times require changing strategies**

China's transition is posing a challenge to all companies, including those with overseas investment. Factories owned by overseas investors have long been a more competitive part of China, using its abundant labor
to generate increasing export incomes. But now, as the economy is changing from export-led growth to growth driven primarily by domestic consumption, they will have to rethink their China strategies. There is a question they all face: What are they here for? Using the country's cheap labor to produce things for their home market or third countries? Or to make and sell things primarily in China?

They did not have to think about this when they first came, amid the boom of the so-called processing trade. The processing trade first came to the mainland in 1978 in Humen, now part of Dongguan, an industrial city in the Pearl River Delta that has one of the largest clusters of foreign-invested manufacturing operations in China. While still contributing about 35 percent of China's foreign trade last year, the glory days of the processing trade are over. Land and labor are no longer in abundant supply, and North America and Western Europe are no longer generating big orders. So for companies wanting primarily cheap labor, probably they will find it is time to go someplace cheaper.

For companies turning to the Chinese market, they also have to make some changes. Amid a rise in all costs, labor in particular, they must learn to innovate and find more creative ways to do business. Some, among the companies that have chosen to stay, said they had cut labor's share in their total costs to below 10 percent. Rising wages, said an executive of Advanced Micro Devices Inc, a US semiconductor company, is a problem that the company has been trying to address for a long time. "We stay here not for the low wages, but for the size of the market," he said.

Lite Array Co Ltd, a Dongguan-based company with Hong Kong investment. Starting as a typical original equipment manufacturer, Lite Array realized its business model was no longer sustainable and began to seek a transition in 2005. It moved away from its traditional line of household electrical appliances and into opto-electrical products. "We had to do so because we felt competition was already too fierce in the market for household electrical appliances. As a Hong Kong company, we don't enjoy any advantage in cost. So we had to make a move," said Shu Weiping, general manager. It decided to go for technology-intensive production and, after quite some market research and much thought, chose to make camera modules that enable mobile phones to take pictures. To implement the plan, Shu and his team went on a nationwide search for talent at many universities, making generous offers to PhDs in optics and micro-electronics. Lite Array made a smart bet. In the years that followed, these moves slashed operating costs. Its electric bill fell 1 million yuan ($157,584) per month and the workforce shrank by more than 2,000. These developments also helped the company move from a net loss before the change to about 20 million yuan in annual profits. The company is still eyeing the future. The increasing use of mobile phones has no apparent limits, which means more potential markets. The company formerly exported all of its products, but now it ships 85 percent of its output domestically. As the case of Lite Array seems to suggest, in a broad sense, the processing trade is but one kind of trade, and all trade is based on comparative advantage.

In the old days, China's unique resources were thought to be its cheap land and labor. Today, they may be its under-utilized universities and university graduates, and even its increasingly more valuable currency.

Source: Zheng Yangpeng: Changing times require changing strategies, China Daily:, 2012-06-12

Economist recommends widening of economic reforms
A leading economic expert has recommended that China deepen and widen its economic overhaul to create a stable platform for the reform of its financial centers in the coming 10 years. Paola Subacchi, the research director of international economics at the Chatham House think-tank in London, is to deliver her advice on financial reforms at the Lujiazui Forum which started in Shanghai on Thursday. Among attendees at the Forum are representatives from the People's Bank of China and China's Regulatory Commissions for banking, securities, and insurance. Before her departure for Shanghai, Subacchi told Xinhua that China has a very strong banking
sector, but less developed capital and bond markets and therefore, reforms to strengthen these areas would benefit China. Without a mature financial sector with enough liquidity, the capital account can never be fully opened up, which makes financial reform a necessity for China, she said. "You can allow inflows and outflows only when you feel that your domestic stability cannot be jeopardized by sudden events and a sudden shock, so you need a mature financial sector." Reforms of currency, exchange rate and interest rate should all go hand in hand, she said, advising a broad set of reforms and a progressive approach to avoid presenting a risk to China.

She said that the goal of building Shanghai a major financial hub by 2020 provided a viable timeframe for the reform. “Ten years is a reasonable timetable for completing this reform. It is a step-by-step reform, it has started and it will continue. In the last year there have been significant steps for more liberalization,” she said. An opening up of the financial sector would see four major financial centers - Shanghai, Hong Kong, Taipei, and Shenzhen - as its pillars. Subacchi advised that China also look for more connections with fellow BRICS nations -- Brazil, Russia, India and South Africa. Shenzhen, a regional and domestic center, has a strong advantage in small and medium enterprises and should continue developing its market for SMEs, Subacchi said.

Source: Xinhua: Economist recommends widening of economic reforms, 2012-06-29

**Lenders raise deposit interest rates**

Chinese lenders are in fierce competition to attract savers after the central bank raised the deposit rate ceiling. Smaller lenders such as Shenzhen Development Bank and Huaxia Bank raised their one-year deposit rates to 3.575 percent, a day after the Big Five lenders raised the interest rate they pay to savers to 3.5 percent. The Big Five lenders are: Bank of China, Agricultural Bank of China, Industrial and Commercial Bank of China, China Construction Bank and Bank of Communications.

The People’s Bank of China last week cut interest rates for the first time since 2008, in a bid to tackle slowing growth. The benchmark one-year saving rate was cut to 3.25 percent from 3.5 percent. Commercial banks were also allowed for the first time to set deposit rates higher than the benchmark. They got permission to set their deposit rates up to 1.1 times the benchmark.

Source: Gao Changxin in SHANGHAI: Lenders raise deposit interest rates, China Daily, 2012-06-11

**Chinese banks ramp up fight for customers**

When China cut interest rates last week, the move was seen as an effort to stimulate the slowing economy. But in the long term, the greater significance may lie in a less-noticed change to the way that Chinese banks set deposit rates. The new measure permitted banks to set deposit rates 10 per cent above the benchmark level. This seemingly minor adjustment was an important first step towards dismantling a ceiling on deposit rates that the government had previously used to limit competition between banks. The move has unleashed competitive forces that analysts say will reduce banks’ profits. The government hopes the move will also change China’s growth model away from its current emphasis on investment.

Over the past week, China’s 15 biggest banks have set deposit rates an average of 8 per cent higher than the benchmark. The next 15 have set deposit rates 9 per cent higher on average, and 10 of those have been offering the maximum permissible rate, which is 3.575 per cent for a one-year deposit. While the gap between banks is slim – only 7.5 basis points separate the highest rates from the lowest – the fact that there is a difference at all is new for China. For years, Beijing set a ceiling on deposit rates and a floor on lending rates, creating a spread of about 3 percentage points. This produced a steady stream of income, which has driven about 80 per cent of Chinese banks’ profits. This spread is now being squeezed. For banks, weaker interest earnings are a clear threat to their profitability. The willingness of smaller banks to take a bigger hit on interest margins could shake up the pecking order in the sector. The five biggest banks control nearly half of all deposits. Beijing hopes smaller
lenders will be able to boost market share. The government also views interest rate deregulation as a crucial step towards shifting China’s growth model away from over-reliance on investment. Higher deposit rates will allow people to earn more on bank savings, providing a much-needed spur for consumption, while banks will seek higher returns on loans and so will allocate capital more carefully.


**Joint venture bank to open in July in Shanghai**

Shanghai Pudong Development Bank and Silicon Valley Bank will start operating their joint venture bank in China in July at the earliest, the China Bank Regulatory Commission said. The Shanghai office of the agency did not provide detailed information about the opening date. "The branch will open in next few months. In an optimistic situation, it will open in July," said a spokesman at the CBRC.

The joint venture bank, in which both companies have a 50 percent stake, was established to provide financial support to small-and-medium sized technology companies in China. It's the first bank focusing on technology companies in China. The investment capital is 1 billion yuan ($158 million). The CBRC approved the establishment of the bank in Oct 2011. The bank will not launch retail businesses in the first three years after the formal launch and is projected to be a regional bank, according to the Shanghai-based Oriental Morning Post.


**China vows to speed up tax reform in 2012**

China will accelerate tax cuts and reforms for selected industries this year to boost domestic consumption, Finance Minister Xie Xuren said in remarks published on Thursday. The pledge is the latest made by China's policymakers to cushion a slowdown in growth set to extend for a sixth straight quarter and leave the world's second biggest economy on course for its weakest full year of expansion since 1999.

"In 2012 we will push forward tax reforms and try to make significant progress in some key sectors," Xie said, according to a statement published on the ministry's website, summarizing a speech made in late April. "We will further improve the policy of cutting taxes for some sectors to spur domestic demand," he added. So far, Beijing has taken several steps overhaul its tax regime, such as launching a pilot program to replace business tax with value-added tax, cutting import duties on some consumer goods and providing tax breaks for smaller firms. Local media have reported that China may unveil a plan to expand its value-added tax beyond Shanghai as soon as in early June, with 10 cities and provinces on a waiting list.

Xie also pledged to make fiscal policy play a bigger role in adjusting China's economic structure, citing energy price reform and setting up a nationwide social security network. He also called for the establishment of a risk-alert and prevention system to enhance supervision of local government debt, without further elaboration.

China has increased efforts to support the economy in the face of a deepening European debt crisis and slowing demand at home, fast-tracking infrastructure investment, providing consumption subsidies in some household sectors and pushing ahead with financial reforms to help safeguard growth. It has eased banks' required reserves in three steps since the autumn of 2011, cutting 150 basis points in total to 20 percent and freeing up an estimated 1.2 trillion yuan for fresh lending. It has also cut taxes and slashed red tape.

Source: Xinhua: China vows to speed up tax reform in 2012, 2012-06-8

**Investors oppose 'int'l board' on Web**

News about possible foreign companies listing on the A-shares market has met with fierce responses from Chinese investors and capital market watchers. On June 1, eight State Council departments, including the
National Development and Reform Commission and the Ministry of Commerce, jointly issued a set of guidelines on promoting new advantages in international cooperation and competition, which included allowing foreign companies to list in the A-shares market as an important part of financial internationalization. The document urged the A-shares market to make technical preparations to embrace foreign companies and formulate relevant rules.

The news immediately became a subject of debate on major microblogging sites like Sina Weibo and QQ.com. While a few netizens defended the introduction of foreign companies, the majority cried out against the thought of opening an "international board". "What do you want to do with the international board? Rescue the whole world? Save ourselves first, please!" wrote "Guan Hangjun" on Sina Weibo. Guan is identified as chairman of the board of Yindu Media Co Ltd in Wuhan, Hubei province. Most economists and financial experts have also come out in opposition to foreign companies listing in the domestic market, largely because they feel that neither the market environment nor the A-shares operating system are ready for introducing foreign companies.

In the past few years, news about the international board has frequently stressed the A-shares market and has met with a market slump almost every time, prompting some netizens to dub it "the sword of Damocles" for Chinese investors. After carefully studying the guidelines issued this month by the State Council, some netizens took comfort in the fact that the Securities Regulatory Commission was not among the eight departments to sign the document, which shows that the guidelines may not represent the ideas of the market watchdog. The Shanghai Stock Exchange on Monday said there are no near-future plans for overseas companies to list in A-shares market. Nevertheless, the A-shares markets in Shanghai and Shenzhen both dropped dramatically at the close of Monday trading, with the Shanghai Composite Index losing 2.73 percent, or 64.89 points, to 2308.55 points, and the Shenzhen Component Index shedding 2.67 percent, or 271.29 points, to 9874.52 points.

Source: Xinhua: Investors oppose 'int'l board' on Web, 2012-06-5

Global Finance: China Is Opening Its Market Gates

China's securities regulator has proposed rules that will ease restrictions and broaden market access for foreign institutional investors, marking the latest effort to liberalize its financial sector. In draft rules issued Wednesday, the China Securities Regulatory Commission said it would lower entry requirements and simplify the approval process for applicants under the Qualified Foreign Institutional Investors program, the primary program for foreign investors to enter China's capital markets. It also will allow qualified foreign investors to hold more shares in domestically listed companies and enter the country's interbank bond market. In a statement, the commission said the move is aimed at "further attracting long-term offshore funds, strengthening confidence in the domestic market and promoting the steady development and opening up of our country's capital markets." The proposal follows a string of changes aimed at easing conditions and broadening the investment scope for foreign investors. Comments on the proposal will be accepted until July 5.

The draft rules for foreign investors said China will lower minimum qualifications for applicants. For foreign fund managers, insurers and pension funds applying for licenses, the minimum requirement for assets under management will be lowered to $500 million from $5 billion, the commission said. For securities companies and commercial banks, the requirement will be lowered to $5 billion from $10 billion. The securities regulator also proposed to raise the ceiling on combined stakeholdings by qualified foreign investors in any listed company in China's domestic A-share market to 30% from 20%. The draft rules also proposed allowing qualified investors to invest in the country's interbank bond market, in which only a small number of them, including foreign central banks, have been granted access.

Rate cut fails to boost Chinese shares
The People's Bank of China (PBOC), the country's central bank, announced Thursday night it would lower the benchmark interest rates by 25 basis points and at the same time give banks more freedom in setting the deposits and interest rates, a significant step towards the liberalization of the interest rates. Banks are allowed to adjust the upper limit of the floating band of deposit rates to 1.1 times the benchmark while offer a lending rate discount as much as 20 percent.

Boosted by the central bank's rate cut, the Shanghai Composite Index opened 0.57 percent higher but wavered at one point into the negative territory over concerns that the country's economy may slow further in the second quarter. It picked slightly by 0.14 percent to close at 2,296.24 for the morning break. Pessimism over the economic data to be released this weekend dominated the market in the afternoon session before losing 11.68 points, or 0.51 percent, to close at 2,281.45. The Shenzhen Component Index rose 0.86 percent at opening but gave up its gains afterwards in a similar course before closing at 9,707.18, down 48.46 points, or 0.5 percent.

Source: Xinhua: Rate cut fails to boost Chinese shares, 2012-06-08

Junk bonds entering the market
Investors offered potentially higher returns but with far greater risks. China has for the first time added junk bonds - high-risk but potentially high-yield securities with low credit ratings - into the market in a move that has been met with a mixed response from investors. Advocates say it diversifies China's financing channels and helps small and medium-sized enterprises break free from usurious loans made by both official and underground banks. Opponents, however, fear that lax regulations and law enforcement combined with under-educated investors could cause turmoil in a fledgling bond market. Regulators said the country will launch its first high-yield bond market on the Shanghai and Shenzhen stock exchanges by mid-June as a way to expand funding access for SMEs.

Small domestic companies which are not listed on the stock exchange are eligible to participate. Issuance will be conducted through private placement. Regulators say they didn't opt for public offerings because only selected investors are able to take on the high levels of risk involved with the bonds. Investors deemed qualified are required to have a paid-in capital of no less than 10 million yuan ($1.59 million). Property and finance companies are excluded from the scheme. Maturities must be longer than one year and the coupon rate should not exceed three times the central bank's benchmark interest rate. That means rates must be lower than 19 percent, based on the benchmark interest rate on June 8. Regulators did not set any requirements on issuers' net assets or revenues, making the threshold low for issuers and the risk high for investors.

The bond market is underdeveloped in China, although it became the world's second biggest economy after the US last year. Data from regulators show 80 percent of bonds issued are based on State credit and most of the rest are from AAA or AA-rated large enterprises, which are also effectively risk-free. China's total bond balance, at 22.1 trillion yuan at the end of 2011, is only one-tenth of the $36 trillion in the United States. In 2011, new issuance of enterprise bonds - issued by State-owned enterprises and government agencies - was 247.3 billion yuan, according to the People's Bank of China, the country's central bank. The volume of corporate bonds, issued by listed companies and State-owned companies, was 124.1 billion yuan. Bonds issued by SMEs account for a mere 5.2 billion yuan. China's corporate and enterprises bond market has risen 20 times since 2005, mainly in a risk-free way. Analysts say the introduction of junk bonds will diversify China's fledgling bond market.

In the city of Wenzhou, the birthplace of China's private economy, in East China's Zhejiang province, debt-laden entrepreneurs, unable or unwilling to repay their debts, fled in droves, threatening to damage the real
and virtual economies. Premier Wen Jiabao cited the boosting of direct financing as one of the important goals of the country's financial reform in his annual government work report in March. On the buy side, junk bonds afford investors, especially those with a higher risk appetite, with one more tool to choose from when arranging their portfolios. In a country that has one of the world's highest saving rates, more lucrative investment products could help put more of those unproductive savings to work. The launch of high-yield bonds is especially good news for the country's hedge funds, a nascent industry that emerged after China introduced short-selling to its stock market in 2010. With a lack of investment tools, hedge funds, known for their sometimes high investment returns, are having problems beating the stock index in China. The Howbuy China Hedge Fund Index, which tracks 174 hedge funds nationwide, was only slightly above the CSI 300 stock index last year, realizing returns of just 4.65 percent.

Chinese public companies are known for their reluctance to pay out dividends. Wang said they will have to pay out more or lose investors once the high-yield bond market has risen in scale. For a junk bond market to flourish, analysts say, related derivatives including credit default swaps should be introduced to provide investors with tools to hedge risks. Hedging is a relatively new concept in China, where the capital markets could not be shorted until short-selling was introduced. For now, the size of the country's interest rate swaps and credit default swaps markets is largely irrelevant, since defaults are rare in the State-dominated bond market. An incomplete regulatory framework could also wreak havoc in the high-yield bond market.

Source: Gao Changxin in Shanghai: Junk bonds entering the market, China Daily, 2012-06-11

Global Finance: China Weighs Easing of Bond Curbs
China is considering relaxing restrictions on short-term bond issuance by some firms, people familiar with the matter said, in the latest move to increase access to credit amid slowing economic growth. The authorities have boosted efforts in recent weeks to prop up the economy, including lowering benchmark interest rates, accelerating approvals for infrastructure projects, offering subsidies for home-appliance purchases and reducing taxes. They also issued rules in late May to allow unlisted small enterprises to sell bonds on China's two stock exchanges, opening a fundraising avenue for a group consistently denied bank loans.

The National Association of Financial Market Institutional Investors, a central-bank-backed association overseeing corporate bonds in the interbank market, is considering permitting all companies with at least double-A ratings to enjoy the same exception, the people said. The proposal is pending central bank approval, they said. For high-rated companies, the cost of borrowing via short-term bonds is much lower than the cost of bank loans. The yield on one-year bills issued by a double-A-rated company was 3.57% on Thursday afternoon, compared with the benchmark one-year lending rate of 6.31%.


Weak China Data Hit Asian Shares
In China, Hong Kong's Hang Seng Index fell 1.3% to 19265.07, while the China Shanghai Composite dropped 1.4% to 2260.88. Australia's S&P ASX 200 slid 1.1% to 4087.60 and South Korea's Kospi was down 0.8% to
The preliminary HSBC China Manufacturing Purchasing Managers Index fell to 48.1 in June compared with a final reading of 48.4 in May, strengthening the case for further policy steps aimed at boosting China's growth.

Markets started the day mostly lower on disappointment that the U.S. Federal Reserve held off from aggressive action to boost the U.S. economy. The Fed instead extended its Operation Twist program aimed at keeping long-term borrowing costs low by selling short-term Treasurys and putting the money into long-term bonds.


Shanghai needs time to be financial hub: AmCham

Shanghai can indeed become a global financial center, although it will take longer than expected, said the American Chamber of Commerce in Shanghai on Tuesday. The chamber made the comment after Shanghai's ambition of becoming a global financial hub by 2020 got a new boost from the central bank's move to liberalize the country's interest rate formation system, allowing lenders to set deposit rates up to 10 percent higher than the benchmark. A market-based interest rate regime and a fully convertible currency are widely seen by economists as two prerequisites for Shanghai to achieve its ambition. The 55-page research report, jointly published by AmCham and the Brookings Institution, looked in detail at the pros and cons of Shanghai's financial industry and came to the conclusion that Shanghai has the potential to become a global center for finance, but probably not as early as 2020. 2020 may be "unrealistically soon" for Shanghai to become a true global financial center rather than a regional hub.

Shanghai has made rapid progress in developing its financial industry since a central government decision in 2009 called on the eastern city to speed up its process of becoming a large international financial center. The transaction volumes of the city's stock, bond and commodities exchanges are already among some of the world's biggest. In 2010, the Shanghai Stock Exchange's market capitalization ranked sixth globally, just behind London. The city has also established shipping and insurance exchanges as part of a move to develop the city's derivatives market.

The AmCham report gave a list of Shanghai's seven key disadvantages, including regulatory opacity and a limited use of sophisticated financial products. Walker Wallace, a partner at the law firm O'Melveny & Myers LLP, said that the lack of regulatory transparency in China is the main reason many Chinese companies seek listings overseas. In the report, AmCham recommends that China's stock market transit from an approval-based listing system to a disclosure-based system. Talent is another issue Shanghai needs to deal with to achieve its goal. And lowering the tax rate is essential to attract financial talents who typically get big paychecks. The personal tax rate is substantially higher in the mainland than in other financial centers. High-income individuals could be taxed by a rate of 40 percent in the mainland, while the rate ceiling is 15 percent in Hong Kong and 20 percent in Singapore.

Source: Gao Changxin in Shanghai: Shanghai needs time to be financial hub: AmCham, China Daily , 2012-06-26

A third of SME capital is from private loans

An audit report has found one third of the capital needed for small and medium-sized companies came from private lending in 2011, China’s top auditor said on Wednesday. The investigation, which analyzed 746 companies nationwide, revealed a serious lack of capital for small and medium-sized enterprises to borrow. The companies were in debt to the tune of 13.5 billion yuan ($2.1 billion) owed to private lenders. This amounted to
half of the loans they received from banks. Of the audited loans, nearly one quarter of private lending was borrowed at an interest rate four times higher than the one-year benchmark interest rate.

The investigation was undertaken following a high-profile lawsuit that resulted in businesswoman Wu Ying being sentenced to death with a two-year reprieve last month. Wu was charged with illegally raising up to 770 million yuan ($122 million) from 11 lenders with the promise of high returns from 2005 to 2007. Some believe she was innocent because the money was borrowed from friends.

Source: Zhao Yinan: A third of SME capital is from private loans, China Daily, 2012-06-27

**IPOs drop in first six months**

The number of IPOs of Chinese companies at home and abroad dropped in the first half of 2012, a Zero2IPO report said on June 29. In the first half of 2012, 128 Chinese companies launched initial public offerings at home and abroad and raised $14.6 billion, the report said. Due to the weak global economic conditions, only 24 Chinese companies went public overseas, down almost 50 percent year-on-year. Their financing amount was $2.98 billion, a 65.1 percent decline compared with the same period in 2011.

As China’s economy slowed and the Chinese Securities Regulatory Commission launched a series of regulations on new stock issuance, domestic IPOs were also lackluster. Only 104 companies launched IPOs in Chinese mainland stock exchanges in the first half of this year, while the number in the same period last year was 167. Financing amounts decreased 56.2 percent year-on-year to $11.6 billion. According to the report, 229 companies globally got listed in the first six months of the year, down 32.4 percent year-on-year, and their whole financing amount was $44.1 billion, down 51 percent compared with the same period last year.

Source: Cai Xiao: IPOs drop in first six months, China Daily, 2012-06-29

**Qianhai poised to be hub of cooperation**

The central government has unveiled bold plans for the development of a new financial and commercial hub in the Qianhai Bay economic zone near Shenzhen, which will offer low corporate taxes, tax-free working, and a strong legal regime with nearby Hong Kong playing a key role in its success. The new zone will officially be known as the Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone, and has been given "national strategic importance" by the State Council. Qianhai will focus on financial, logistics and IT services and is set for completion in 2020, said officials. It will become a modern service industry cooperation zone and a pilot district for future cooperation between Hong Kong and the Chinese mainland, said Zhang Xiaohui, vice-minister of the National Development and Reform Commission, in Hong Kong on Friday.

He stressed the pilot measures to be launched in Qianhai had been carefully designed to reflect Hong Kong's unique position in the area's development and had also taken into consideration the city's opinions and demand during the policy making process. The series of pilot measures cover finance, taxation, legal, human resources, education, medicine as well as telecommunications, he said. Eligible companies allowed to operate in the new zone will enjoy a 15 percent preferential corporate profit tax rate, while workers will also be exempted from personal income tax. "Since the mainland is targeting the gradual achievement of full yuan convertibility, Qianhai should be a pioneer for the progress," said Zhang. He added foreign equity investment funds will be encouraged to develop in Qianhai and the threshold for Hong Kong financial institutions to enter the district will also be lowered under the Closer Economic Partnership Agreement. The pilot measures reflected Hong Kong's important role in mainland's reform, while carrying out the "win-win" financial cooperation between Hong Kong and Shenzhen, said HKMA.

Source: Sophie He in Hong Kong: Qianhai poised to be hub of cooperation, China Daily, 2012-06-30
Premier calls for academic freedom
Premier Wen Jiabao said in a Monday report delivered at a scientific conference that academic freedom and independent thinking should be promoted to spur innovation. The key to a nation's prosperity is whether the nation can make good use of the enormous creative potential and independent thinking spirit of its people, Wen said in the report. The government should foster a free academic environment that is free from restraint and encourages invention and innovation, he said. Wen asked top scientists and engineers attending the conference to find and train more promising young researchers and provide a favorable academic environment to put their talents to good use. Wen said he expects scientists and engineers to contribute more by using their expertise to advise the government on scientific and technological issues. The world is undergoing a new round of scientific and technological revolution, Wen said. He asked the scientists and engineers to take the opportunity to make major achievements and bridge the gap between China and developed countries in terms of economic and sci-tech development. More than 1,200 scientists and engineers attended the biennial conference of the Chinese Academy of Sciences and the Chinese Academy of Engineering.
Source: Xinhua: Premier calls for academic freedom, 2012-06-13

Space economy to boom in China
The successful launch of the Shenzhou IX spacecraft indicates China's economic infrastructure and technology have made great progress and the country is ready to explore aerospace economy, reported Economic Information Daily on Monday. The aerospace economy boasts unusually wide industry range, containing almost every industry from energy, steel, new materials, electronics, machinery, and communications to space clothing and space food, which involve the textiles, garment processing, agricultural products and food processing industries. The achievements resulting from space technology development can be widely applied to other sectors of the economy, and thereby trigger innovation in these sectors, the report said. According to a report by China Aerospace Science and Technology Corporation, 80 percent of the more than 1,000 types of new material developed in China in recent years benefited from space technology, and nearly 2,000 kinds of space technology have been adopted in various sectors of the national economy.
Source: Xinhua: Space economy to boom in China, 2012-06-18

China's first female astronaut excels in performance
Liu Yang, the first Chinese woman entering the space, had an excellent performance in past eight days, a spokeswoman of China's manned space program said Sunday. The 33-year-old veteran pilot adapted to the weightlessness in space in a short time, said Wu Ping, spokeswoman for China's manned space program. "She is in good mental and physical state," said Wu, adding that all her physiological indices were normal. The spokeswoman said Liu had good teamwork with the other two male astronauts Jing Haipeng and Liu Wang, and obtained a lot of treasurable experimental data. Liu is in charge of medical experiments during the 13-day mission, which features China's first attempt at a manual space docking procedure. "We have made special arrangements for her life in space including personal hygiene and cleaning supplies. She will tell you whether she is satisfied with the arrangements when she comes back," said Wu.

Joining the People's Liberation Army (PLA) Air Force in 1997, Liu became a veteran pilot after flying safely for 1,680 hours. She was promoted to deputy head of a PLA flight unit before being recruited as a prospective astronaut in May 2010. She is now an Air Force major. After two years of training, which shored up her astronautic skills and adaptability to space environment, Liu excelled in testing and was selected in March this year to crew Shenzhou IX. Since joining the military service, she has received accolades for her public speaking, winning the first place in a military speech contest in 2010. She also impressed others as a quick
After becoming an astronaut candidate in 2010, she devoted the first year to basic academic and physical training, only starting to study aerospace and astronautics one year ago. Before the start of the Shenzhou IX mission, she finished all scheduled training courses.

Source: Xinhua: China's first female astronaut excels in performance, 2012-06-24

China’s first woman in space arrives home

China’s Shenzhou 9 spacecraft thudded to earth in Inner Mongolia on Friday, capping a two-week space mission that has transfixed the world’s most populous nation and put the first Chinese female astronaut into space. Chinese leaders applauded the mission, which tested space docking procedures that are crucial steps toward China’s goal of creating a manned station by 2020. “This is another outstanding contribution by the Chinese people to humanity’s efforts to explore and use space,” said Wen Jiabao, the Chinese premier.

China’s space programme is several decades behind that of the US and Russia – which launched manned space stations in 1973 and 1971, respectively – but Beijing’s determination to boost its programme comes as the US is cutting back its investments in space. The US retired its space shuttle fleet last year. China, by contrast, has invested about $6bn in space programmes since 1992 to catch up with its counterparts, raising eyebrows in military circles in Washington.

During the latest space mission, the Shenzhou 9, or “divine vessel”, successfully docked with China’s orbiting module Tiangong 1, which means “heavenly palace”, a manoeuvre that is of key importance for China’s planned manned space station. Millions of television viewers across China watched the black capsule as it fell to earth just after 10am, rolling a few times before it came to a stop in a meadow. The mission put China’s first female astronaut in space, the 33-year-old air force pilot Lieutenant Liu Yang. Hundreds of students gathered at her former middle school in the city of Zhengzhou, holding up her picture and singing the national anthem, according to media reports.

Source: Leslie Hook in Beijing: China’s first woman in space arrives home, Financial Times, June 29, 2012

China to bolster co-op in manned space program

China will boost cooperation with other nations and regions in its manned space program in order to promote the development of global space technology, the program's director said Friday. Wang Zhaoyao, director of China's manned space program office, said the country will continue to bolster international cooperation "with a positive and open stance." Wang said future cooperation will focus on technological exchanges, collaborative science experiments, responding to the United Nations’ call to share technology with other countries and allowing Chinese professionals to work with their international peers in training and research. "The purpose of China's manned space program is the peaceful use of the space and common development of humankind," said Wang. Joint experiments overseen by Chinese and German scientists were part of last November's Shenzhou VIII space mission, marking the first time for China to allow foreign scientists to conduct experiments in one of its space vessels. "The experiments went smoothly. Scientists from both countries are analyzing their data and have obtained results," Wang said, adding that the results of the experiments will be released in a timely manner.

Source: Xinhua: China to bolster co-op in manned space program, 2012-06-29

Jiaolong starts last dive in Mariana Trench

China's manned submersible, Jiaolong, began its 6th and last dive in the Mariana Trench Saturday morning, targeting a depth between 6,900 to 7,100 meters below the surface of the Pacific Ocean. The Jiaolong set a national dive record on Wednesday after reaching 7,062 meters below sea level during its fifth dive into the Mariana Trench, the deepest part of the world's oceans. After arriving at the area earlier this month, the Jiaolong
had succeeded in reaching depths of 6,671, 6,965, 6,963 and 7,020 meters in its first four dives from June 15 to 24, easily surpassing the previous national record of 5,188 meters it set last July. The Jiaolong enabled China to join the ranks of deep-sea faring countries. The United States, Japan, France and Russia currently lead the world in the development of deep-sea exploration technology, each possessing their own submersibles and support bases.

Source: Xinhua: Jiaolong starts last dive in Mariana Trench, 2012-06-30

China calls on US to end pollution checks

The air monitoring station at the US embassy – which broadcasts hourly pollution readings to more than half a million Chinese followers on micro blog Sina Weibo – has not sat well with China’s leaders. On Tuesday a senior Chinese official called for the US to stop publishing its embassy’s pollution readings and said that doing so was a violation of the Vienna conventions that govern diplomatic conduct. Deputy environment minister Wu Xiaoling said at a press conference that it was illegal for foreign consulates to publish air pollution data and called on diplomats not to “interfere in the internal affairs” of China. The comments, the first of their kind, underscore the political sensitivities of China’s battle with pollution, as the world’s second-largest economy wrestles with the environmental costs of its rapid growth. 750,000 Chinese die prematurely each year from pollution-related causes, according to a World Bank report.

The air pollution data gathered by the US embassy in Beijing – as well as by US consulates in Shanghai and Guangzhou – measures small particulate matter that is not routinely reported in Chinese pollution statistics. Chinese cities are only required to release data for larger particulate matter, which is not as harmful to human health as the smaller particles, and they typically publish aggregate pollution data once a day as opposed to every hour. As a result of reporting differences between the US and Chinese data, the widely followed US numbers sometimes paint a more dire picture of the air quality than the official pollution index. The data discrepancy sparked a public outcry last year, when a toxic smog engulfed Beijing for days. Official data indicated only moderate pollution, in contrast to the US data, which showed hazardous levels. After a widespread outcry from Chinese media, the Beijing city government began publishing hourly data for small particles in January, albeit only from a single pilot location in western Beijing. China’s environment ministry is slowly raising standards for pollution reporting, and more than 70 cities will be required to disclose data for small particulate matter, known as PM 2.5, by the end of this year.

Source: Leslie Hook in Beijing: China calls on US to end pollution checks, Financial Times, June 5, 2012

Slowing China, Hidden Job Strength

While the U.S. struggles with a relatively jobless recovery, China seems to have the opposite challenge. Despite a sharp slowdown in China's economy, data suggest that labor markets are tight. In the first quarter, a survey of local employment bureaus found a record dearth of workers. In the same period, government data suggest that wages for migrant workers rose 16.6% year over year. But the general picture contrasts sharply with the U.S., where 8.2% unemployment and weak wage growth are the depressing reality. It also is different from the situation in China in 2009. Back then, the collapse in foreign demand for Chinese exports put about 20 million migrant workers out of a job and knocked wages for the group down 10%, according to estimates by researchers at Stanford University and the Chinese Academy of Sciences.

Structural changes in China help explain why this year isn't seeing a repeat and demand for workers is outstripping supply. The working-age population already has peaked. And after 30 years, the flood of rural workers willing to make the trek from the farm to the factory has turned to a trickle. Stable employment also may help explain why dismal economic data of late haven't sparked a big response from Beijing. Growth in April
was as bad as it has been since the financial crisis. But growth is largely a means to support social stability. If employment is holding up, lower growth is less cause for alarm. Tight labor markets reduce the scope for stimulus, too. For years, excess supply in China’s labor markets helped keep wages down; the government could kick-start the economy without a pass-through to inflation. Excess demand for labor puts an end to that luxury, though. Manufacturing-sector wages rose 20% in 2011, according to data from the statistics bureau. More stimuli could reignite the inflation that China’s policy makers spent much of 2010 and 2011 trying to tame.


Walmart faces new food safety claims in China

Walmart is facing fresh accusations of selling substandard food products in China just months after a scandal over the mislabelling of products cost its country head his job and damaged the chain’s reputation in a market where food safety is a major concern. The animal husbandry and foodstuff bureau of Dazhou city, a city of nearly 7m people just outside Chongqing, said it had asked Walmart’s local branch in January to stop selling pork ribs sourced from diseased pigs. A separate report published by state media on the same day said that a branch of Walmart in Beijing was found to be selling sesame oil with carcinogenic ingredients, and fresh squid with too much heavy metal. Local state media reports said Walmart had withdrawn all the products from its shelves.

The latest incidents could prove a blow to Walmart’s efforts to improve its performance in China, where it has 370 stores. In the last quarter, China was the only country where Walmart’s sales lagged behind the overall market. Comparable store sales only grew 1.2 per cent from a year ago. The company has been sanctioned 21 times by the Chongqing government since 2006. The worst scandal was the discovery last October that ordinary pork was being sold as more expensive organic pork. That led to the arrests of two store managers in Chongqing and the overhaul of Walmart’s China management team.

Source: Enid Tsui in Hong Kong and Barney Jopson in New York: Walmart faces new food safety claims in China, Financial Times, June 13, 2012

China introduces measures to enhance food safety

The State Council, China’s Cabinet, on Wednesday laid out measures to improve food safety, including tighter supervision and harsh punishments for violators. "It is an onerous task for the government to ensure food safety," as China’s food industry is still suffering from unstandardized management and many hidden safety risks, according to a statement released Wednesday after a State Council executive meeting presided over by Premier Wen Jiabao. The government should enhance supervision by setting up an efficient mechanism that covers all links in the food industry and a rigid food recall and destroy system for defective products, the statement said. The State Council has vowed a "harsh crackdown" on those endangering food safeties, saying violators should be ensured penalties in accordance with laws and regulations. Meanwhile, relevant policies, laws and regulations should be revised to increase costs for violators, according to the statement. The State Council urged Chinese enterprise owners to accept primary responsibility in ensuring quality and safety, while government departments should enhance quality and safety monitoring. More efforts should be taken to accelerate the establishment of a complete food safety standard and quality assessment mechanism to improve agencies’ capabilities to conduct tests and issue emergency response in case of food scandals, it said.

Source: Xinhua: China introduces measures to enhance food safety, 2012-06-14

Fakes and status in China
China is known for "malinvestment". Its consumption habits are also pretty dodgy. Economists and policymakers around the world want China to consume more. They are eager for it to reduce its dependence on investment, which amounted to almost half of GDP last year. No economy that invests so heavily can possibly invest it all wisely. Economists therefore worry about a widespread misallocation of capital, or "malinvestment". But some of China's consumption is also a bit questionable. Fake goods are rife. Researchers once stopped every fifth person in a Shanghai mall and asked them about their buying habits. Of the 202 who completed the survey, almost three-quarters admitted to buying knock-off luxury goods. The resulting paper by Ian Phau and Min Teah of Curtin University of Technology in Australia was titled "Devil wears (counterfeit) Prada". Some people buy luxury brands as an act of self-expression. Others buy them as an act of social emulation. They want to wear the same brands as the people they aspire to be. The Chinese are more likely to be this second type of buyer, according to Lingjing Zhan of Hong Kong Polytechnic University and Yanqun He of Fudan University. And, other studies suggest, such status-seeking consumers are more likely to buy counterfeits.


**China to regulate residential power use**

The National Development and Reform Commission announced Thursday that China will initiate a trial to charge residents more for electricity if their usage exceeds a certain level. The trial, known as tier-based electricity pricing mechanism, will take effect July 1, said a statement on the NDRC's website, China's top economic planning body. The statement said 80 percent of the population will not be affected because their monthly usage was too low. However, the electricity price for the rest who use more power will be raised by as much as 0.3 yuan (5 cents) per kilowatt-hour. According to the statement, local authorities are also authorized to adjust the pricing threshold either on a monthly or annual basis in different seasons and depending on the size of a family. The NDRC first started to seek public views on the tier-based electricity pricing mechanism in October 2010. The NDRC said the new measure will help save energy and protect the environment without causing a marked increase in the cost of power usage for the majority.

Source: Xinhua: China to regulate residential power use, 2012-06-14

**China’s public sector in need of business education**

In a significant reform move, China is set to reshape its government-funded public institutions to improve the effectiveness and cost-efficiency of public services. The Chinese government recently issued blueprints for the reform that will affect more than 40m public sector staff currently working in approximately 1.26m government-run public institutions across the country such as schools, hospitals, publishing houses and the agriculture and forestry sectors. Any reorganisation across China’s public sector will not automatically yield a more market-oriented, customer-friendly and cost-effective service. The root cause of the problems can be found in the lack of education and training in modern business and management methods.

Furthermore, to deliver training that is really tailored to the needs of Chinese consumers, a blend of Chinese and western methods is needed. Chinese consumers have become more demanding and will only be satisfied with higher quality standards and more efficient service delivery, aspects that western methods are used to supplying. China’s public sector reform will only succeed if it is supported by an education and training culture that transcends the entire public sector. Education and training often viewed by Chinese managers as an unnecessary cost or at best a necessary evil, needs to be seen as the key to long-term progress and success. China’s economic miracle is at a crossroads right now and public sector reform is one of the key challenges facing further progress. Long-lasting education and training-led reform is the way forward with no time to lose.

China telecoms: ZTE's handset headaches

Although successful in selling low-cost smartphones, ZTE is trying to boost profits by launching higher-end models. Its experience so far is mixed. China's ZTE is the world's fourth-largest handset maker and fifth-largest telecoms equipment provider. Despite its higher ranking in handsets, this product segment is a mixed blessing for the company. Last year, ZTE shipped 80m handsets, an increase of 54% over 2010. Smartphone shipments reached 12m, a five-fold increase on the previous year. The company's smartphone success was fuelled by the Blade, a low-cost model popular in both China and abroad. Surging handset sales, however, are not fully reflected in profits. The gross margin for ZTE's handset unit is falling, standing at around 15% at the end of 2011, a far cry from the 30% margin recorded for software and services and 40% on network equipment. Handsets account for one-third of ZTE's revenue but only a quarter of profits.

ZTE is struggling to find a middle ground between popular low-cost smartphones and pricier models that include more features but are a tougher sell. Customer surveys suggest that Rmb1,000 (US$158) is a key point at which enthusiasm for smartphones wanes, with interest falling sharply for handsets that cost Rmb2,000 or more. Regardless of price, buyers demand as many features and the best performance as possible, putting pressure on costs for manufacturers. China Telecom recently launched five smartphones priced at RMB999, representing a 23% price cut in just six months. In the first quarter of this year, China became the largest market for smartphone shipments, overtaking the US, according to research firm Canalys. This growth is driven by low-cost models from the likes of ZTE and others. At the same time, a large share of profits from smartphones sold in China goes to Apple, Samsung and others that focus on the higher end of the market.

This strategy has boosted ZTE's market share of shipments at home and abroad. Following the success of the Blade, ZTE rolled out the Skate in late 2011. This new model, targeting the elusive mid-range smartphone market, is made for China Unicom's WCDMA network. In addition to the features found in the Blade, the Skate is dual-SIM and dual-mode (compatible with GSM), and is priced just under RMB2,000.

To keep ahead of this profit-eroding trend, this month ZTE launched the Grand, a high-end smartphone that uses the CDMA EV-DO for China Telecom. According to ZTE, the Grand features a 1.5GHz dual-core CPU, 4.3-inch display, and 8GB storage and twin video cameras. The model runs in dual-mode (CDMA and GSM) and is priced at around RMB2,000. ZTE also plans to make a quad-core Grand later this year for sale in Europe and the US. ZTE plans for its high-end models to account for 20-30% of its smartphone sales this year. In addition to the Grand, another handset expected to contribute to this segment, the Orbit, runs on the Windows platform. A ZTE official says that the company is committed to Windows-based smartphones because they have "greater room for profit" than Android phones. These phones are pitched at the high-end almost by default; the licensing fee charged by Microsoft in order to use its platform is around US$27 per handset, compared with US$5 for Android models.

ZTE's recent success in the telecoms equipment market is thanks largely to its price advantage over western rivals. Even so, the company's networks division enjoys higher margins than its handsets division; the profitability of ZTE's equipment is also growing while margins on its handsets shrink. Despite efforts to capture a greater share of the middle and high-end smartphone market, ZTE is yet to demonstrate that it can climb the value chain as successfully in phones as it has for the network equipment that services them.

Source: EIU viewswire: Industry Briefing: China telecoms: ZTE's handset headaches, June 18th 2012

Overcapacity for Negative View on China

China bears say that massive industrial overcapacity is about to swamp China in a wave of bankruptcies. The numbers tell a different story. The argument goes like this: a combination of cheap capital and poor policy has
resulted in colossal overinvestment in China's industrial sector. Sooner or later, China's factories will reap what they sowed. A wave of oversupply will crush profit margins and wipe out swathes of businesses. Certainly some sectors are looking a little swamped. Steel producers have seen profit margins hammered by over supply. At Angang Steel--one of China's largest by output--the net margin in 2011 was -2.4%, down from a high of 13% in 2006. Return on assets fell to -2% from 19% over the same period. But evidence of overcapacity at the economy-wide level is harder to find. Indeed, the numbers suggest that China's businesses have become more, not less, efficient. Asset turnover for China's industrial sector as a whole has been on a steady rising trend for the last decade. Sales as a percentage of assets rose to 128% in 2011, up from 69% in 2001. Return on assets is also stable at 8% in 2011, after a long rise from 1% at the end of the 1990s.

One reason for that is investment in industrial capacity has not been as huge as some might imagine. In 2009, China's investment stimulus was focused on public infrastructure. In 2010 and 2011 it was real estate that stole the show. The manufacturing sector accounts for just a third of China's total investment--most of the remainder is not adding to production capacity. In a period of weak demand--like right now--China's industrial sector will suffer from cyclical oversupply. But a structural problem might be a figment of China bears' overcapacity for negative thinking.


Industry: In search of inspiration

China overtook the US as the world’s biggest goods producer by output last year, reclaiming the global supremacy it lost in the 19th century. But it still has to dispel the image of being a low-cost workshop where quality is inferior and the best ideas are copied – or stolen – from the west. In Gao Jifan’s headquarters, abutting Trina’s huge factory of 14,000 employees, Mr Gao is relentlessly upbeat about China’s industrial creativity. He points to Trina’s new generation of “Honey” solar cells, which have produced record-breaking efficiency levels, as being examples of homegrown Chinese innovation. “We’ve progressed by spending a lot on research and development, but also thanks to a commitment to service and quality,” says Mr Gao, who set up the company in 1997 after a background in chemical engineering.

China’s industrial rise has also commanded increasing attention because its companies are acquiring western rivals. Recently, Chinese companies have even bought companies in Germany, the bastion of European manufacturing. Targets have included Putzmeister, a construction equipment group, and Kiekert, an auto parts maker. Chinese government planners want more “industrial champions” like Trina to create sustainable wealth generation at a time when rising wage costs mean the country can no longer rely on a reservoir of cheap labour as its engine of growth. Perhaps paradoxically, the efforts of Chinese companies such as Trina to move up the value chain by developing new technologies are also in the interests of major western and Japanese manufacturers that spend billions of dollars on Chinese factories and research units.

The more China becomes a “normal industrial country” – with standards of manufacturing close to or on a par with, say, Germany or the US – the more likely it is that these companies will be able to turn China into a vital part of their operations. Take Voith, a German engineering group that is a world leader in hydroelectric equipment and paper-making machines. Hubert Lienhard, chief executive, is typical in saying that his company’s global priority is “establishing a China industrial footprint”. Voith’s business also clearly reveals the shifting priorities of companies setting up in China. Ten to 15 years ago, most were there to set up factories where they could churn out goods for export. Now, like many other executives, Mr Lienhard espouses the mantra of “in China, for China”. His focus is to use China’s manufacturing prowess to sell locally. Of its €1bn of sales to customers based in China last year, half came from the company’s China plants, with the rest imported into the
country, mainly from Germany. “By 2015, my plan is to increase annual sales in China to €1.5bn, of which two-thirds would come from our China operations,” Mr Lienhard says. Over the period, he intends to triple the size of Voith’s China workforce to 10,000. Mr Lienhard dismisses the idea that by transferring more of its knowhow to China, his company risks surrendering some of its technical edge to Chinese competitors.

Inevitably, China’s increasing wage costs are at the heart of the discussion on cost-effectiveness. Between 2008 and 2010, according to a study by Germany’s Ifo economics institute, the average year-on-year rise in labour costs in China’s engineering sector was 11.6 per cent, against a comparable rise of 1.9 per cent in the EU and a decline over the same period of 8.5 per cent a year in the US and 3 per cent in Japan. The higher wages have triggered speculation that some foreign manufacturers will increasingly shift away from China to seek cheaper bases in south-east Asia. But China still has pronounced advantages in terms of labour costs, to say nothing of infrastructure, technology and consumers. China’s factory labour is still often 80-90 per cent cheaper than in many western nations. As plants use more technology – especially in industries such as electronics that China wants to encourage – labour is becoming a smaller part of operating costs, in many industries representing only 10-15 per cent of the total. Yoshitaka Morinaga, head of a Chinese plant run by Nichicon, a leading Japanese maker of capacitors, says that – in his industry at least – the impact of higher wages has been minimal. Much more important has been China’s growing sophistication in manufacturing, with better suppliers, fewer quality problems and improved logistics networks. Mr Morinaga says: “We have 50 to 60 suppliers in China and because they are better [in terms of quality and reliability] than previously, we can now make capacitors in China at 70-75 per cent of the equivalent cost in Japan, as opposed to 80-85 per cent five years ago.”

A good demonstration of the differences between industries is that most “national champions” in China – with perhaps the exception of Huawei and ZTE – have excelled in building on the technology platforms already mapped out for them by large western businesses and where most advances have been incremental. Chinese companies have yet to display their prowess in industries that are much more inherently complex, such as laser-cutting machines, heavy-duty automotive presses, top-quality steel for applications such as nuclear pressure vessels and most areas of advanced medical equipment. Overall, in the 20 years in which it has been climbing up the ranks of manufacturing nations, China has made startling progress when it comes to getting the basics right. But when it comes to technology breakthroughs – exactly in line with what would be expected for a country whose reinvention as an industrial nation has only just begun – it is still setting out.

Source: Peter Marsh: Industry: In search of inspiration, Financial Times, June 11, 2012

Real estate speculative demand restrained
Two years after the real estate regulation had been implemented, the speculative demands are basically out of the market now, reported Shanghai Securities News on Monday, citing an official. According to the report, Qin Hong, director of the Policy Research Center of Housing and Urban-Rural Development Ministry, said at the 2012 Strait Real Estate Forum in Fuzhou, Fujian province that real estate speculative demand has been effectively restrained. She said the aims of the current round of real estate regulation are very clear. The first goal is to
restrain the speculative demand in real estate market, contain rising housing prices and the other goal is to construct affordable housing to meet the demands of the market. Qin also noted that the development space of China's real estate market will remain big in the future, especially for individual purchasing needs and improving housing condition. However, the growth rate of the property market will decrease, Qin added.

Related Stories
Source: Anonymous: Real estate speculative demand restrained, China Daily, 2012-06-25

WTO starts 4th trade policy review of China
The fourth trade policy review of China, where members of the World Trade Organization examine the trade policies and practices of China over the past two years, began on Tuesday. Yu Jianhua, head of the Chinese delegation and assistant minister of commerce, told members about the macro-environment for China's economy, trade and investment development. He said since the last WTO review in 2010, China has been confronted with a complicated economic and trade environment. The ongoing financial crisis and the non-conventional monetary policies adopted by some members caused many negative impacts on China.

External demand has been sluggish, and the influence of the eurozone debt crisis has been deepening. Inside China, the government has been under much pressure to stabilize prices, the cost of labor has shot up while an aging population brings more challenges. However, to promote robust, sustainable, and balanced growth, the Chinese government has deepened reform and opening up, expanded domestic demand, and accelerated economic restructuring and the transformation of the economic growth model. The development of China's economy and trade has maintained a good momentum, and China's economic and trade links with other countries and regions have been further strengthened on the multilateral, regional, and bilateral fronts, Yu said.

China's import growth has outpaced export in the past two years, indicating that trade is on the way to becoming more balanced. In 2010 and 2011, China's total export of goods was $1.58 trillion and $1.9 trillion, up by 31 percent and 20 percent respectively over the previous year. Meanwhile, total imports were $1.4 trillion and $1.74 trillion, up by 38.8 percent and 25 percent respectively, according to Yu. He said China has fully capitalized on its comparative advantages, adhered to reform and opening up, endeavored to create a sound investment climate and facilitated trade and investment. It has become an indispensable manufacturing link in the global value chain, and has been one of the most attractive investment destinations for many years. "We hope that with our joint efforts, the mutually beneficial and win-win trade and economic relations between China and all other WTO members could continue to develop soundly and steadily," he said.

Eduardo Munoz Gomez, chairman of the Trade Policy Review Body and Colombian ambassador to the WTO, said China had received a record number of more than 1,700 written questions from nearly 30 members, including the United States, the European Union, Brazil and India. He said the questions were mainly about China's export policies, Sanitary and Phytosanitary measures, intellectual property rights protection, agriculture, government procurement, services, and anti-dumping measures. Members will make comments and raise questions with China during Tuesday's session. The Chinese delegation will deliver replies when the review continues on Thursday. All WTO members are subject to review, with the frequency of review depending on the country's size. The US, China, EU and Japan are reviewed every two years.

China 'plays constructive role' in G20
President Hu Jintao, addressing the G20 Summit on Monday in the Mexican resort of Los Cabos, said that China supports increasing the resources of the IMF and enhancing its ability to tackle the crisis and provide emergency assistance. Hu also called on the group to continue supporting Europe "in a constructive and cooperative way".

The financial contribution is "a positive thing", and EU countries will welcome the decision, the EU ambassador to China, Markus Ederer, said on Tuesday at a speech at the University of International Business and Economics in Beijing. China has been playing "a constructive role" in supporting the EU to tackle the crisis, Ederer said. "If China expresses confidence in the eurozone, it is a very important signal to the market." But Ederer emphasized the support from the IMF is "the second line of defense", as he stressed the EU's own responsibilities.

G20 finance chiefs agreed in April to increase the financial firepower of the IMF by more than $430 billion. The IMF said that it will tap the new resources to shield the global economy from the European debt crisis only if it uses up its existing resources. The approach by the US and other developed countries in not boosting IMF resources does not match their economic strength, according to Jia Xiuguo, an expert on international affairs with the China Institute of International Studies. "It is inconsistent with Washington's responsibility to the IMF," Jia said. China's decision to boost IMF resources, rather than give direct loans to European countries, is a good way to use its large foreign exchange reserves, said Wang Yizhou, an expert on the global economy and politics at the Chinese Academy of Social Sciences.

During a meeting with German Chancellor Angela Merkel ahead of the G20 Summit on Monday, Hu said that China will continue to support Europe's efforts in promoting integration and maintaining the stability of the euro. A united, stable and prosperous Europe serves the interests of the world, including China, Hu said. The EU is China's largest export destination. Merkel said Europe appreciates China's confidence in the continent and its support for European integration. She also noted that a steady, robust Chinese economy is an important factor in any global economic recovery.

Source: Wu Jiao in Los Cabos and Zhou Wa in Beijing: China 'plays constructive role' in G20, China Daily, 2012-06-20

**China's external debt highest since 1985**

China's outstanding external debt in 2011 totaled more than $751 billion by the end of March, the highest since 1985, according to data released by the State Administration of Foreign Exchange on Tuesday. The proportion of short-term debt also rose to a record high. The total debt went up by 8.1 percent from the $695 billion three months earlier. Outstanding medium and long-term debt stood at $193.6 billion, accounting for 26 percent of the total debt, while the short-term debt of $557.7 billion took up 74 percent, up by 2 percentage points compared with the end of 2011. "Among the short-term debt, trade credit between enterprises and trade finance from banks together accounted for 75.11 percent, indicating that the surge in short-term debt is closely related to the rapid development of China's foreign trade in recent years," SAFE said in a statement.

In the first three months, China borrowed $9.3 billion in medium- and long-term external debt, down by 34.3 percent year-on-year. "Dollar-denominated debt took up 77 percent of China's registered external debt, followed by euro debt, which made up 8.23 percent, less than 1 percentage point higher than three months earlier. Yen debt accounted for 7 percent," SAFE said. Experts warned that regulators must watch fast-growing short-term liabilities. The proportion of short-term external debt to the total also climbed to a record high of 72 percent as of Dec 31, in contrast to 68 percent in 2010 and 60 percent in 2009. "Regulators should be alert to China's rapidly rising short-term external debt, as the proportion of 72 percent is well above the international alert level of 25 percent," said Li Chao, deputy head of SAFE, in December. However, "the ratio of short-term debt to foreign exchange reserves stood at 15.75 percent, far below the globally recognized warning line of 100 percent," SAFE said earlier in March. As of 2011, China's other external debt indicators all fell into the “safety” range, according to international standards, it said.

Source: Wang Xiaotian: China's external debt highest since 1985, China Daily, 2012-06-26
China: Currency forecast

China’s current-account and trade surpluses are both forecast to fall to modest levels as a proportion of GDP in the forecast period, and the country will therefore be in a strong position to resist external pressure to allow a faster rate of currency appreciation.

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Source: EIU viewswire: China economy: Reform push, April 18th 2012

China's unfair tactics

China has arrived at the stage where it has no option but to liberalise its currency market and export capital a little more easily in one way or another. It is choosing to do so through administrative measures, such as bilateral CNY swaps. Until this month, China had focused these swaps in local currencies of major emerging market trading partners, and not with developed market partners such as the US and the EU. But, a couple of weeks ago, China announced that it would do CNY:JPY swaps with Japan, a developed and large trading partner.

What are the implications of the latest Chinese measure to introduce CNY:JPY swaps? They are not likely to be significant immediately as few internationally traded contracts are denominated in either CNY or JPY. The same arrangement for CNY:USD or CNY:EUR would have been more globally significant and would have led to CNY internationalisation more quickly. However, the question raises some interesting possibilities where China-Japan, China-Asan and Japan-Asan trade is concerned. Triangulation on trade and trade-related long-term investment among these three large trading blocs/players (more if one includes Korea and Taiwan) holds out interesting possibilities for the growth of Asian markets in regional currency trades and derivative hedges. Also, Japanese multinationals are major investors in Chinese export production, which is linked to their own export production for global markets, in innumerable and intricate ways. If the CNY:JPY arrangements stabilise the influence of currency fluctuations on such bilateral and pass-through trade then the CNY/RMB will benefit and internationalise faster.


Yuan experiment to start in 'mini-Hong Kong': Beijing to test convertibility in 15 sq km zone in Shenzhen

Three decades ago, Shenzhen pioneered economic reforms that eventually led to the opening up of the entire
China said the southern city will once again lead the way, this time in experimenting with currency convertibility. The test-bed is a 15 sq km zone in western Shenzhen, called Qianhai Financial Zone. Hong Kong banks can lend yuan directly to Chinese companies there. Currently, this is not allowed by China.

Said Mr Zhang Xiaogiang, vice-chairman of China's top economic planning agency National Development and Reform Commission: 'China will eventually make the renminbi (yuan) convertible. Qianhai will walk in front of the rest of the country in testing that out. It will be a venue for financial innovation.'

Mr Will Sage, managing director of the Asia Securities Industry and Financial Markets Association, said it is part of China's process to ensure the domestic market has the right infrastructure, and domestic players have sufficient expertise, before full liberalisation. 'If Qianhai goes well, they will expand to other cities. If it doesn't, they can make adjustments or not extend the pilot,' he said. Qianhai, which sits on reclaimed land, is now barren land, with just a showpiece boulder carved with its name. But US$45 billion ($56 billion) will be poured into it to turn it into a 'mini Hong Kong' providing financial, logistics and IT services. The goal is to achieve a gross domestic product of 150 billion yuan ($30 billion) by 2020. To entice Hong Kong companies to make the journey - 1.5 hours by bus - across the border, those eligible will get a 15 per cent corporate tax rate, lower than the 16.5 per cent levied in the city. Personal income tax concessions will be dangled to get talents from Hong Kong and overseas, and Hong Kong companies can build international schools and hospitals without the need for a local partner. Meanwhile, a comprehensive transport network is in the works, linking three subway lines, highways and sea passage to the zone. Already, there are 21 companies registered and 170 projects ready to start, said Mr Xu.

Source: Li, Xueying: Yuan experiment to start in 'mini-Hong Kong': Beijing to test convertibility in 15 sq km zone in Shenzhen, The Straits Times [Singapore], 30 June 2012.

China extends trade goods forex reform

China will extend a nationwide trial of simplified procedures for passing foreign currencies between banks and companies in goods trades, the country's foreign exchange regulator announced on Friday. The move is aimed at "making foreign trade more convenient, increasing trading firms' global competitiveness and promoting stable growth of foreign trade," according to a statement issued by the State Administration of Foreign Exchange (SAFE). The trial program, started in eight provinces and cities on December 1, 2011, canceled the previous procedure of verifying each foreign exchange payment and receival for goods trading firms. The program also allowed easier export declaration and export tax rebate procedures, while enabling the SAFE to share information with tax and customs authorities to crack down on illegal cross-border capital flows, tax fraud and smuggling. The trials, carried out in the provinces of Jiangsu, Shandong, Hubei, Zhejiang (excluding Ningbo), and Fujian (excluding Xiamen), as well as in the cities of Dalian and Qingdao, produced good results, the SAFE said. The nationwide extension of the program from August 1 comes as China tries to maintain foreign trade growth amid weakening external demand due to economic difficulties in key Western markets as well as rising costs of labor and raw materials. In the first five months of 2012, China's foreign trade rose 7.7 percent year on year to $1.51 trillion, much slower than the 27.4-percent increase registered during the same period last year.

Source: Xinhua: China extends trade goods forex reform, 2012-06-30

Yuan has worst quarter in 7 yrs

The yuan had its biggest quarterly decline since a dollar peg ended in 2005 as Europe's crisis hurt demand for Chinese exports. The People's Bank of China lowered the currency's daily reference rate by 0.48 percent this quarter, while the Dollar Index strengthened 4 percent as investors favored safer assets. The yuan weakened 0.88 percent this quarter to 6.3541 per US dollar in Shanghai, according to the China Foreign Exchange Trade
Exports rise but outlook still cloudy
Exports jumped by more than 15 percent in May, from the previous year, as shipments to the United States rose significantly and trade with the European Union rebounded. However, exports did beat market expectations to surge by 15.3 percent to $181.1 billion in May, against 4.9 percent growth in April, according to figures released on Sunday by the General Administration of Customs. And imports rose 12.7 percent year-on-year, to $162.4 billion last month, much stronger than the 0.3 percent rise in April. Both exports and imports hit record highs in terms of value. The trade surplus in May hit $18.7 billion after reaching $18.4 billion in April.

China faces the risk of further slowdown in the economy amid European woes. The People's Bank of China, the central bank, lowered interest rates by 25 basis points last week, taking one-year borrowing costs down to 6.31 percent and the one-year savings rate to 3.25 percent. Exports surged by 8.7 percent, year-on-year, to $774.4 billion from January to May, and imports increased by 6.7 percent to $736.5 billion during the same period, according to the figures. Trade with the US jumped 12 percent to $190 billion during the first five months, and trade with the EU picked up by 1.3 percent. China's shipments to the US jumped by 23 percent in May, from a year earlier, the biggest increase this year.

Both experts and officials have recently downplayed export prospects. Pressure has been increasing on the government to roll out more stimulus measures, experts said. "Time is pressing for the exporters to change their growth model," Zhang said.

World News: Chinese Data Show Economic Strength
China's exports and imports both rose sharply in May, while inflation slowed substantially, hopeful signs for the world's second-largest economy. Rafts of data released over the week end by the Chinese government present a mixed picture, but overall suggest an economy stronger than many market players feared at the end of last week. A surprise-interest rate cut by the central bank Thursday prompted speculation that the monthly data for May would be especially weak. Instead they showed that growth in industrial production ticked up slightly, albeit from an April pace that was the slowest in nearly three years, and that auto sales and property investment were stronger -- signs of life for the Chinese economy, despite the sovereign debt crisis in Europe and a sluggish recovery in the U.S.

The data indicate that measures taken by the Chinese government to support growth are already having an effect, said HSBC economist Ma Xiaoping. "It is almost certain that China's economy will bottom out in the second quarter and rebound in the third quarter," she added. Government initiatives rolled out in recent weeks include purchase incentives for energy-efficient household appliances, targeted tax cuts and accelerated approval for investment projects by companies and local governments. On Friday, officials called for additional spending on railway construction. May exports were up 15.3% from a year earlier, China's General Administration of Customs said Sunday, beating April's feeble 4.9% rise and well above the 6.9% rise forecast by a poll of economists. Similarly, May imports were up 12.7%, compared with April's 0.3% increase and expectations for a 3% rise. On Saturday, the National Bureau of Statistics said that China's consumer-price index for May showed the slowest rise since June 2010. It was up 3% from a year earlier, easing from April's 3.4% pace and below expectations for a 3.2% rise.

World News: U.S. Clears China From Iran Oil Sanctions
The U.S. exempted China from penalties for doing business with Tehran as the latest set of U.S. sanctions targeting Iran's oil exports took effect on Thursday. The State Department, which had determined that China had significantly reduced its purchases of Iranian crude, had previously exempted 19 other countries, all traditional purchasers of Iranian crude. That left China, the biggest buyer of Iranian oil, potentially shut out of doing business with the U.S. The Obama administration determined that China met the requirements because its purchases of Iranian crude fell about 25% in the first five months of the year. The exemption lasts for six months.

Beijing has opposed the latest round of U.S. sanctions, which ban companies that deal with Iran's central bank from doing business in the U.S. Chinese officials said this month that purchases of Iranian oil are "legitimate." A decision not to grant an exemption to China would have risked a diplomatic and economic showdown with an important trading partner, a country Washington is trying to persuade to play a more constructive role in other areas, such as the Syrian conflict and North Korea's nuclear program.


Searching for FDI Stability
China made a splash yesterday with a cut in interest rates, as well as a slight relaxation of the regulations that govern these rates. More broadly, it's dawning within Chinese policy circles that fundamental reform may be needed to transform the country's development model. Some are realizing that much of the stimulus-produced investment of 2009 and 2010 has been wasted. The announcement out of last month's Strategic and Economic Dialogue that foreign investment banks can hold up to 49% of joint venture securities firms, up from 33%, is another recent example. Opening China's securities markets to more foreign participation has long been a key plank of U.S.-China dialogue. Unfortunately, this and other steps are at best small and technical. Judging from similar minor openings over the past 15 years, such moves rarely lead to real breakthroughs.

In another weak pass at reform in April, the new change-minded chairman of the securities regulator approved dozens of new foreign investors in China's stock markets under the Qualified Foreign Institutional Investor (QFII) program. He also increased the amount of foreign capital that can be brought into these markets. These moves, together with the central bank's doubling of the yuan's daily trading band, have been touted as steps toward the freeing up of the exchange rate and the opening of the capital account. These recent steps are welcome, but hardly qualify as reform. The rush of QFII approvals hides the fact that the existing facility, in operation for nearly nine years, remains the most restrictive such facility in all of Asia. The hurdles to attain QFII status remain extremely high and many dedicated Asian or China fund managers, unable to meet Chinese requirements, are limited to trading via Hong Kong or other overseas listings.

The closest Beijing has come to jump-starting reform was Premier Wen Jiabao's startling call earlier this year to break up the oligopoly of the big four state-owned banks. Against the backdrop of the trial program being rolled out in Wenzhou, in the eastern Zhejiang province--where banks begin to serve medium and small businesses instead of state-owned enterprises--the premier's words might be taken to mean the government seriously intends to focus on channeling credit to the private sector. If successful and expanded to the broader economy, Wenzhou-style commercial banking would entail a major transformation of the state banks from simple suppliers of capital directed and priced by the government, to institutions able to measure and value risk.

It certainly sounds great and fits right into the reform playbook, but is the premier just trying to burnish his own
legacy rather than set a course for the coming years? It's hard to forget that opportunities for greater reform were missed in the past decade, under this premier's watch, as the banking system became a victim of political infighting.

Reform is desperately needed, in completely liberalizing interest rates, ensuring that lending is based on economics not politics, opening access to capital for all investors, making the exchange rate flexible and enabling capital to cross borders. But strong leadership will be required to make tough decisions, and the recent announcements show such leadership still lacking. Not embracing deep reforms in the next few years means that China will continue to misprice capital and only repeat the same mistakes it and other countries made in the past. The price of bad or postponed decisions will be more ghost cities, bubbles and oversupply in steel and heavy industry, ultimately becoming an ever greater burden on the rest of the economy.


490 out of world top 500 firms invest in China

A senior commerce official said Friday that so far, 490 out of the world top 500 companies have invested in China and established more than 1,600 R&D centers and regional headquarters. Transnational corporations have kept investing more in China since the country adopted the policy of opening up to the outside world in the late 1970s. The companies have been playing an increasingly important role in boosting the nation's economic development, Gao Hucheng, a vice commerce minister, said at a meeting. Foreign-invested firms have reaped great benefits from this huge market. Sales of these companies exceeded 33 trillion yuan ($5.24 trillion) in China in 2010 alone, Gao said, adding that the nation has become a safe haven and a main source of income for many foreign-invested firms during the international financial crisis.

Meanwhile, China has stepped up its investment in other parts of the world. By the end of 2011, China's outbound direct investment topped $380 billion. There were more than 18,000 Chinese-funded companies operating in 178 countries and regions at the end of last year, with total assets reaching approximately $1.6 trillion, Gao said.

Source: Xinhua: 490 out of world top 500 firms invest in China , 2012-06-23

China’s investment arms extend reach

China established its official sovereign wealth fund China Investment Corp almost five years ago with the specific mandate to earn high returns by more actively investing abroad the dollars China earns from its exports. Now CIC is just one of several of Beijing’s investment arms that have increasing clout in the world. Today there are at least six such arms although some are too small to be consequential. However, they are all putting ever more money outside China. That outflow will have significant implications for the prices of securities and assets worldwide, especially because China’s investment style is becoming less passive by the day. Yet the decision making of these investment arms is increasingly centralised and therefore less transparent than ever.

China’s State Administration for Foreign Exchange has become an increasingly aggressive investor overseas through its investment arm, Safe Capital. Safe Capital has at least $300bn, but access to far more money from its parent’s $3.2tn balance sheet. While it is highly secretive, those familiar with it say its new active role signals Beijing's determination to diversify its investments generally, but especially away from US government debt and the dollar. Historically, China’s reserves have been managed very conservatively with the bulk invested in US Treasury securities, a shrinking pool of US government sponsored enterprises such as Fannie Mae and Freddie Mac mortgage securities, German government bonds and other highly-rated debt. Now that is changing. The Chinese government “thinks there is no sense in putting money in Treasuries or European government bonds, and financing western deficits” says one former Hong Kong financial official. “This is more
sensible.” The ‘this’ in that sentence refers to China’s determination to use investment as well as trade to secure the technology and resources it needs to take its growth to the next level and expand its footprint abroad. For example, many of CIC’s recent initiatives have to do with forming funds to help Chinese companies invest in and acquire companies in the rest of the world to obtain leading-edge knowhow in areas such as energy and a local presence in resource intensive economies such as Russia.

Both CIC and Safe have now been joined by a third investor, China’s State-owned Assets Supervision and Administration Commission (Sasac), which has also become more active. Sasac has been given about $10bn for its China reform fund which was established to support Chinese outbound investment. Today, Sasac can make investments through the state-owned enterprises it supervises or directly itself. Sasac’s new initiative is meant to turn China’s state-owned enterprises into multinational powerhouses by making acquisitions offshore, an objective similar to that of CICs. Even as it sets up competing institutions, the Chinese government seems to be centralising control of the money whenever it can. The new Sasac fund, for example, is controversial since some observers think it is better for each state-owned enterprise to make its own investment decisions because they are closer to the markets and the real world. But that would mean less power for Beijing, and the government is still clearly eager to control both the amount of money leaving China and where it goes. Investment decisions are increasingly political as well as returns driven.

Moreover, policy banks such as China Development Bank, which also have access to the government balance sheet, lend money on such concessional terms that they too are augmenting China’s financial clout in the world.

It is difficult to know how wisely the money is being disbursed throughout the world because there is little transparency about the way the Chinese government makes its decisions in most cases. The Chinese mobilisation of funds is already leading others, notably the Japanese, to step up their overseas activity. That competition could be a good thing for other countries in need of capital. Whether it is good or bad for the people of China itself is less clear. They could point out all the projects that the government should be financing at home before it uses their money to buy up the rest of the world.

Source: Henny Sender: China’s investment arms extend reach, Financial Times, June 11, 2012

**Germany top European investment country for Chinese firms**

Chinese entrepreneurs labeled Germany as the most attractive investment destination in Europe, considering more acquisition and joint ventures with German companies, a latest study showed Wednesday. The report of consulting firm Ernst & Young, based a survey of 400 executives of medium-sized and large Chinese firms from different industries, indicated that one in four Chinese managers viewed Germany as one of the three most appealing locations for investment worldwide. The other two were China itself, with 61 percent of votes and the United States, with 29 percent. Within Europe, Germany wins 63 percent of responses, ahead of France with 13 percent, the report said. Among Chinese companies that are planning to invest in Germany, Europe’s strongest economy, 9 percent are expecting business acquisitions, while 56 percent preferred joint ventures. Ernst & Young said Chinese companies, with substantial funds in hands, are “full to bursting” for the expansion in Germany. As for the particular sectors, 57 percent said they are interested in mechanical engineering, with automobile industry in the second place.

In March, the Berlin-based foreign trade and investment promotion agency Germany Trade & Invest reported that China became the biggest foreign investor in Germany in 2011, with 158 greenfield investment projects, ahead of the United States and Switzerland, which had 110 and 91 projects respectively.

Source: Xinhua: Germany top European investment country for Chinese firms, 2012-06-14
Global Finance: China Buys Overseas Assets

China's overseas investment surged in the first quarter to $21.4 billion as state-owned companies snapped up resource-related assets around the globe, according to a report by a private investment firm that counts China's sovereign-wealth fund among its partners. China's total overseas investments more than doubled from the year-earlier quarter, according to estimates by A Capital, a private-equity firm based in China and Paris that takes stakes in European companies alongside Chinese investors. That figure includes mergers and acquisitions as well as so-called greenfield investments, or construction of new plants and facilities.

Last year, A Capital identified some emerging trends, such as growing investment by private-sector companies. But investment in the first quarter was dominated by a more traditional pattern of Chinese state-owned companies investing in energy and resources companies in places like South America and Africa. The report also showed sustained interest in Europe by Chinese companies, a trend that continued from last year, as continuing sovereign-debt woes on the Continent have presented opportunities for investments at depressed valuations. State-owned companies accounted for 98% of all deal value in the first quarter, a new high and up sharply from 53% in the first quarter of 2011, A Capital estimated in its quarterly Dragon Index on China's outbound investment. Resources and energy deals accounted for 92% of the total, up from just 24% a year earlier. South America was the top destination for investment during the first quarter, at 43% of total foreign merger-and-acquisition activity by Chinese companies. The biggest single investment during the period was the acquisition by China Petrochemical Corp., or Sinopec, of a 30% stake in Petrogal Brasil, the Brazilian subsidiary of Portuguese oil company Galp Energia SA, for $5.16 billion. The A Capital report counted the investment as one in Latin America rather than Europe. Europe was the second-largest destination for investment, accounting for 16% of outbound M&A. That is down from 37% in the year-earlier period, but the decline is largely due to the increased focus on investing in resources. Investment in the U.S. was just $8 million in the quarter, down from $975 million a year earlier.


China SME Global Development Forum held in Austria

The China SME Global Development Forum opened Monday in Vienna, focusing on topics including the difficulties of Chinese SMEs in global development. More than 100 small and medium-sized enterprises from China's Zhejiang province and about 30 enterprises from Austria and the other EU countries attended the forum. During his speech on the forum, Director General of the United Nations Industrial Development Organization Kandeh K. Yumkella said that China is not only a huge market for enterprises over the world, but also increasingly an important breeding ground for scientific and technological innovation. In this sense, during the future development of the global economy, the world needs China, and China needs the world, too, he said. The UNIDO is willing to provide the Chinese enterprises with necessary assistance in the process of globalization, especially in their investment in developing countries and regions including Africa, he said.

"SMEs play a very important role in our national economic and social development," said Gao Yingzhong, head of Zhejiang SME Bureau. Like the other types of enterprises, Zhejiang's SMEs were also impacted by the financial crisis and the European debt crisis further exacerbated the impact on their traditional exports, he said. "Therefore, this year we have organized the forum to provide a platform to promote the expansion of Zhejiang's SMEs in the European market, to seek cooperation with their counterparts in Europe, and to promote the development and prosperity of Zhejiang's SMEs," he said.

Source: Xinhua: China SME Global Development Forum held in Austria , 2012-06-26
**Firms to unite in Europe**

Companies will help each other set up and create leading brands. An alliance of private-sector companies will establish offices in Europe to aid and advise other Chinese companies investing in the continent. The Aigo Entrepreneurs Alliance will see its members move into London and Brussels in the coming months. Feng Jun, president of Aigo Digital Technology, who founded the alliance in June 2011, said private companies should help each other expand overseas. The alliance has about 100 members, with many more set to join, including companies that have already set up an overseas presence.

Chinese companies are increasingly investing overseas. More than 13,000 domestic enterprises had invested in 178 countries and regions by the end of 2010, according to the Ministry of Commerce. Outbound direct investment for 2011-15 is expected to register double-digit annual growth to $560 billion, matching the nation's foreign direct investment, the ministry said earlier this year. More than selling cost-competitive products, Feng has a brand vision for the alliance. "Creating brands is different from just doing business because it requires absolute honesty. Our alliance will supervise the members and ensure quality products," Feng said. He also feels that overseas subsidiaries of Chinese businesses must create value for local communities. Consequently, Feng encourages the alliance's members to expand through joint ventures with foreign companies, rather than acquisitions.

The office in Greenwich will be set up at Greenwich Peninsula, a 77-hectare office and residential development currently under development. In Brussels, a group of the alliance's members are now beginning to move into Tour & Taxis, a business complex with shop space in central Brussels. Another two groups are soon to move into the European Market City (EMC), a business hub along the highway between Brussels and Antwerp.

Many of the companies choosing the are manufacturers. Guido Bernaerts, CEO of Group Bernaerts, which developed the EMC, said that the project connects manufacturers from China and retailers from Europe.

Feng represents a new generation of Chinese entrepreneurs who champion high-tech innovation and brand-value creation. As a testament to the effort his company invests in protecting innovation, Aigo Digital Technology won a landmark intellectual property rights case against Toshiba in a Chinese court in October. Other examples of Chinese companies that have come to realize the value of branding include clothes maker Bosideng and air conditioner producer Gree Electric Appliances.

Source: Cecily Liu and Zhang Haizhou in London and Ding Qingfen: Firms to unite in Europe, China Daily , 2012-06-28