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# China News Alert Issue 289

## Capital Markets

### SAFE move will hike capital inflow

China's efforts to streamline approval procedures for foreign exchange business applications under the capital account category are expected to boost foreign investment into the country, experts said.

The State Administration of Foreign Exchange (SAFE) recently issued a circular giving more power to its local bureaus in approving as many as 10 foreign exchange categories under the capital account.

"The move is to simplify procedures and facilitate foreign investment and trade," SAFE said on its website. The new rules will take effect from June 1, according to the foreign exchange administrative body.

"SAFE's measure will provide a more convenient environment for foreign investment in China on both foreign direct investment (FDI) side and for those investing in China's capital markets," Li Xiaogang, director of the Foreign Investment Research Center under the Shanghai Academy of Social Sciences, told .

"Compared to FDI, which takes rather long for investment decisions, the measure will have a more immediate effect in triggering foreign investment in the capital markets.".

According to the new SAFE rule, qualified foreign institutional investors (QFIIs) only need to get approval from local SAFE bureaus if the amount they want to buy or sell from their mutual funds on the mainland capital market exceeds $50 million.

But experts warned that the move did not mean that China would loosen controls on foreign exchange management.

"It just means SAFE will be more efficient in approving foreign investment applications," Li said.

"In the long run, SAFE will give more power to local bureaus," said Chen Bingcai, senior researcher from China National School of Administration and a former SAFE official.

The Ministry of Commerce (MOC) took a similar move in March when it decided to give its local branches more power in approving foreign-funded projects. Local officials are allowed to approve the establishment of foreign-funded companies with a registered capital of $100 million or less.

The move is part of the government's efforts to boost FDI inflow, which has been affected by the global financial crisis.

Foreign investment, both to China's financial and non-financial sectors, was significantly down last year.

The combined foreign direct investment inflow to China was $160.9 billion in 2008, up 8 percent from a year ago, but was 65 percentage points slower, SAFE said in a report on China's balance of payments in 2008, which was released last month.

The financial sector attracted $14.7 billion while the non-financial area drew $146.2 billion.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-05/15/content_7780206.htm) ([see archive](SAFE_move_will_hike_capital_inflow.pdf))

### CBRC unveils norms for consumer finance firms

Consumer finance firms are likely to boost consumer spending in China and provide competition to the consumer lending services offered by banks, analysts said.

The China Banking Regulatory Commission (CBRC) issued draft rules recently that would allow domestic and foreign financial institutions to establish consumer finance firms to provide personal loans to finance purchases of durables. The CBRC said it is seeking feedback on the rules from the public till June 12.

"Personal loans account for only a small portion of the loan portfolio in most Chinese banks. This is mainly because loans to consumers have a relatively high cost compared to corporate loans," said Zhang Jing, analyst, Minzu Securities.

Zhang said he expects the competition from the soon-to-be established consumer finance firms to prompt Chinese banks to put more efforts into consumer lending.

Despite a record-setting 4.58 trillion yuan of new loans issued in the first quarter, consumer-lending growth in Chinese banks remained relatively weak.

Industrial and Commercial Bank of China (ICBC), the world's largest bank by market value, extended 52.5 billion yuan worth of new loans to consumers in the first quarter, accounting for just 8.2 percent of ICBC's 636.4 billion yuan of new loans in the first quarter.

The proportion of personal loans in China Construction Bank and Bank of China, the other two of the country's top three State-controlled banks, was 8.6 percent and 8 percent in the first quarter, respectively.

According to the draft rules issued by the CBRC, the consumer finance firms will not be allowed to take deposits or to offer automobile loans or housing mortgage loans. But they are expected to provide loans to consumers faster than banks and can issue loans of up to five times the applicant's monthly salary.

Compared with credit cards with similar credit lines, which usually require cardholders to repay the credit within 50 days, personal loans offered by the consumer finance firms give customers a longer time for repayment.

Applicants, willing to set up such a consumer finance company, are required to have at least five years experience in consumer lending and possess assets of no less than 800 million yuan.

The CBRC also set a 10 percent capital adequacy ratio and 100 percent loan-loss coverage ratio requirement for the proposed consumer finance companies.

The Chinese government has recently unveiled a series of measures aimed to spur domestic consumption.

The central government began to dole out 5 billion yuan of subsidies to help rural residents buy vehicles in March. It also introduced a program to help consumers in rural areas buy appliances at a discount.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-05/14/content_7775708.htm) ([see archive](CBRC_unveils_norms_for_consumer_finance_firms.pdf))

### GEM draft listing rules mark major step in China's capital market innovation

The draft listing rules for China's upcoming Growth Enterprise Market (GEM) had displayed the spirit of prudence, innovation, efficiency and market orientation, analysts said.

It marked a major step in the development of the country's first Nasdaq-style stock market, a vital part of China's capital market innovation.

The draft was issued by China's Shenzhen Stock Exchange recently to solicit public opinion. With a major concern over risk control, the document had set out a stricter delisting mechanism, information disclosing rules, and more rigid stock sale restrictions for controlling shareholders on GEM, compared with stocks trading on the main boards in Shanghai and Shenzhen.

"We had designed the regulation in a way that better protects investors, improves market efficiency, and promotes long-term and healthy development of the market," an official of the Shenzhen Stock Exchange said.

The design of the GEM system has distributed greater responsibilities to market players such as accounting and law firms, and aimed at laying a sound platform for the capital market, said analysts, adding that much experience could be drawn from the GEM operations.

China Securities Regulatory Commission (CSRC) published measures for initial public offerings and listing on GEM on March 31, which have been in effect since the beginning of May.

It later issued draft measures governing the approval committee and the sponsors of securities issuance for public feedback, which nearly concluded April 24.

With the release of the listing rules draft, the launch of the GEM is drawing nearer. Under the current financial crisis, it would effectively expand the financing channels of smaller and middle-sized companies, which were anxious to make use of the opportunity, said Hong Liang, analyst from the China Galaxy Securities.

[Source: Xinhua](http://news.xinhuanet.com/english/2009-05/09/content_11343686.htm) ([see archive](GEM_draft_listing_rules_mark_major_step_in_Chinas_capital_market_innovation.pdf))

### Plans progressing for foreign firms to list in Shanghai

China is advancing its study of plans to allow foreign companies to list on the Shanghai Stock Exchange and may work out preliminary arrangements as early as this year, industry sources said recently.

The country is expected to step up communications with other nations in the coming months on the development of an international board in the city after concluding a deal with Britain for further stock-market reform, the sources said.

"China agrees to allow qualified foreign companies, including United Kingdom companies, to list on its stock exchange through issuing shares or depository receipts in accordance with relevant prudential regulations," the two countries said in a joint statement issued on recently.

The agreement, reached by Chinese Vice Premier Wang Qishan and British Finance Minister Alistair Darling following a meeting in London, is set to pave the way for large British companies like HSBC to sell shares in Shanghai.

HSBC said in a statement that it "would like to be the first foreign bank to list in Shanghai if the authorities allow," and is working toward that goal. It did not give a specific timetable for a stock sale in the city.

Peter Wong, executive director of HSBC subsidiary Hongkong & Shanghai Banking Corp, said earlier this month that a Shanghai listing would consolidate HSBC's brand influence and raise funds for expansion in the Chinese mainland market.

Two years ago, China started to consider permitting foreign companies to issue yuan shares to help boost the status of its fledgling stock market on the mainland. But the program has proceeded slowly as regulators worked to ease investor jitters over a stock glut.

#### Program revived

The project entered the spotlight again after China's State Council issued a guideline in late March allowing Shanghai to prepare for allowing overseas companies to sell yuan-denominated shares and bonds on the city's bourse.

Other companies including Hong Kong-based Hang Seng Bank and the Bank of East Asia have also publicly expressed an interest in listing shares in Shanghai.

"Apparently, the program was revived," said a Beijing-based brokerage executive close to the China Securities Regulatory Commission. "Preparatory work will be paced up, with the initial arrangement likely to be settled by year end."

Industry insiders said any public stock sale by an overseas company would not be likely to occur until at least late next year as there's a great deal of work to be done.

One key obstacle for foreign companies is that they will have difficulty switching the proceeds of their mainland listings into other currencies and repatriating the money as the yuan is not fully convertible.

Hu Xiaolian, head of China's foreign exchange regulator, indicated in London that the country won't likely move quickly to free up the yuan under the capital account.

[Source: China.org](http://www.china.org.cn/business/news/2009-05/13/content_17768243.htm) ([see archive](Plans_progressing_for_foreign_firms_to_list_in_Shanghai.pdf))

### Avoid risky derivatives, SOEs told

State-owned enterprises (SOEs) should proceed cautiously in overseas derivatives trading in order to minimize the potential risks, and the government should make efforts to develop the domestic futures market to accommodate these companies' risk hedge needs, regulators and experts said.

The government has become increasingly concerned about the financial derivatives trading by large State-owned enterprises after some of them incurred huge losses.

The State-owned Assets Supervision and Administration Commission (SASAC), which supervises 138 of the country's largest State-owned companies, had earlier ordered companies under its watch to review their derivative products such as futures, options, forwards and swap contracts in overseas markets and stop the ones with high risks.

The move came after several high-profile State-owned companies such as the country's flagship carrier Air China and shipping giant China Cosco Holdings reported massive losses on derivatives.

At present, 28 State-owned companies under SASAC supervision are involved in financial derivative trading, and a majority of them suffered losses, Li Wei, SASAC's deputy director, said in a statement without disclosing other details.

"This has posed serious threat to companies' sustainable operations and also endangered state assets," Li said.

He added that his agency would conduct a thorough review of State-owned companies' investment in financial sectors this year and work out the relevant policies based on the investigation.

SASAC has also urged local State asset watchdogs to take similar moves to better supervise local State-owned companies.

Li said companies should use derivative instruments as a tool to hedge risks "but not as a means to gain profit", and should never be engaged in speculative trading.

"If companies do not use derivatives as a tool for hedging risks and use its price-discovery functions, they will be in a disadvantaged position amid cut-throat international competition," Li said.

State-owned companies, Li said, must meet strict requirements like getting prior approval along with tight risk-control mechanisms, before being qualified for derivatives trading.

Many of the companies were conducting derivatives trading without prior approval, Li said.

The government should accommodate the rising demand for derivatives trading by these companies if it needs to reduce the huge risks involved in overseas derivative instruments, experts said.

Many Chinese firms were trading in derivatives abroad in the past two years, often without government approval, partly due to lack of tools for hedging risks in the domestic market, Li Fuan, director of innovation supervision at the China Banking Regulatory Commission, told a financial conference recently.

Financial institutions, Li said, should develop more derivative products to meet the demand but they should be more transparent in risk disclosure.

"Efforts should also be made to develop the domestic futures market to allow companies the chance to hedge their business risks," said Hu Yuyue, futures professor, Beijing Technology and Business University.

"Otherwise companies will be forced to take chances in overseas derivative markets," he said.

Air China lost 7.47 billion yuan in aviation fuel hedging contracts. China Eastern Airlines lost 6.2 billion yuan in aviation fuel hedging contracts. China Cosco Holdings Co, the world's largest operator of dry-bulk ships, lost 3.95 billion yuan from wrong-way bets on freight rates as of Dec 12, 2008.

[Source: Sina](http://english.sina.com/business/2009/0507/239714.html) ([see archive](Avoid_risky_derivatives_SOEs_told.pdf))

## Corporate & Commercial

### Chinese mainland market opened wider to HK businesses

The Chinese central government and the government of the Hong Kong Special Administrative Region (HKSAR) recently signed the sixth supplement to a key trade agreement to give Hong Kong firms greater and easier access to the mainland market for tourism, securities and banking services, among others.

Under the supplement agreement, authorization requirements will be further eased for Hong Kong commercial banks to expand their existing networks in the neighboring mainland province of Guangdong to cover different cities province-wide.

Joint venture securities investment advisory firms between Hong Kong businesses and their mainland counterparts shall also be allowed starting Oct. 1, although the percentage of shareholding by the Hong Kong side was restricted to no more than one-third.

Mainland travel agents can also organize group tours for mainland residents bounding for the province of Taiwan to enter and remain in Hong Kong in transit. The aim was to help the trade develop multi-destination package offers, said Donald Tsang, Chief Executive of HKSAR.

The Supplement VI to the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) was signed by John Tsang, who is financial secretary of the HKSAR government, and Jiang Zengwei, the central government's Vice Minister of Commerce at a ceremony in Hong Kong.

Speaking at the ceremony, Donald Tsang said the supplement agreement introduces 29 measures that are built on the liberalization of 20 services sectors and open two more sectors to Hong Kong businesses, namely, research and development and rail transport.

"With the new supplement, the total number of services sectors covered by the CEPA and its supplements will thereby be expanded from 40 to 42," Jiang said.

The liberalization measures cover, among others, audio and visual services, telecommunications, legal services, convention and exhibition, transport, printing and publishing. Some of the measures will be first implemented in Guangdong on a pilot basis.

Mutual recognition of professional qualifications will be explored and encouraged in sectors such as accounting, architecture, real property and printing services. Hong Kong pharmacists shall be allowed to sit for exams and register in the mainland.

In addition to joint venture law firms, Hong Kong lawyers, upon meeting certain qualification requirements, can apply to practice as lawyers in the mainland.

The new measures will take effect on Oct. 1, three months earlier than usual, to "allow the trade to enjoy the benefits earlier," Jiang said at the ceremony.

Donald Tsang welcomed the agreement, saying that the new measures will be mutually beneficial and help Hong Kong overcome the impacts of the ongoing economic downturn.

It is roughly estimated the service trade liberalization measures and the individual travel permit scheme under the CEPA agreements created 43,200 jobs from 2004 to 2008 in Hong Kong. The individual travel permit scheme alone contributed 58 billion HK dollars (7.4 billion U.S. dollars) of extra consumption in Hong Kong.

The CEPA measures, meanwhile, brought 46 billion HK dollars (5.9 billion U.S. dollars) of extra income to Hong Kong businesses providing services in the mainland and created 49,500 jobs in the mainland, Donald Tsang said at the ceremony.

[Source: Xinhua](http://news.xinhuanet.com/english/2009-05/09/content_11342443.htm) ([see archive](Chinese_mainland_market_opened_wider_to_HK_businesses.pdf))

### Stimulus fineprint for metals out

China will push forward consolidation in the non-ferrous metal industry to form three to five big firms in three years, a detailed stimulus plan released recently by the State Council showed.

The plan, whose draft was published in February, said: "The government seeks to make great progress in industrial consolidation. By 2011, the top 10 firms should control 90 percent of copper production, 70 percent of aluminum, 60 percent of lead and 60 percent of zinc."

The stimulus plan is one among a slew of packages to boost industries such as steel, shipbuilding, textile and automobile.

Some leading enterprises in the non-ferrous sectors, such as China Minmetals, Chinalco, and China Nonferrous Metal Mining Group, as well as some listed companies such as Zijin Mining, are expected to benefit from the plan, said Deng Xinrong, analyst with Founder Securities.

Under the plan, the industry should continue closing inefficient or polluting plants: 300,000 tons of capacity in copper smelting, 600,000 tons in lead, 400,000 tons in zinc, and 800,000 tons of capacity in aluminum smelting should be shut down this year. Kang Yi, the chairman of China Nonferrous Metals Industry Association, described the target as a "hard job".

The non-ferrous industry has been one of the worst hit by the financial turmoil as prices of metals have plunged by 30-40 percent.

The stimulus plan is intended to help enterprises not only survive the financial crisis but alsoenhance industry competitiveness, Kang said in an earlier interview.

In a move to help metal enterprises, the government will adjust tax rebate rates on non-ferrous metal exports, the plan indicated without elaborating. Kang's association had suggested Beijing raise rebates on exports of all aluminum products to 17 percent.

The plan also said the government will consider the need to expand reserves of metals and speed up the establishment of a national reserve system but it did not give any detailed figures of the stockpiling tonnages.

The State Reserves Bureau has bought 590,000 tons of aluminum and 159,000 tons of zinc since December. But it may not buy more aluminum and zinc in the first half as the prices have surpassed production cost of many smelters, experts said.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-05/12/content_7767437.htm) ([see archive](Stimulus_fineprint_for_metals_out.pdf))

### Action plan booster shot for equipment manufacturers

China will take a wide range of measures such as tax exemption, subsidy and industry consolidation to support its equipment manufacturing industry as part of its latest efforts to stimulate the economy, according to a detailed industry stimulus plan released recently by the State Council.

The government will exempt value-added tax (VAT) and import tax on key parts and raw materials needed in the manufacturing of major equipment products, the stimulus action plan said, without specifying the items falling into the category.

The plan said the government would set up a mechanism under which the customers who use the first batch of major equipment produced by domestic companies will get risk compensation, a policy designed to spur the homegrown industry.

The detailed action plan, which said the domestic industry should at least occupy 70 percent of the local market share, said the government would push forward industry consolidation and overseas expansion by extending financing support.

The government will extend support to companies involved in mergers and acquisitions (M&A) during their applications for issuing stocks, corporate bonds, bills and bank loans, the plan said.

It said the government would offer interest subsidies to domestic companies that acquire overseas peers and their R&D facilities.

Financial institutions, the plan said, would be encouraged to issue loans to companies that plan to make M&A moves, both in the local and overseas markets.

"The stimulus policy certainly will give the industry a boost, but its growth will ultimately rely on the performance of the economy," Fu Caixia, machinery industry analyst with China Minzu Securities, said.

"The leading industry players are expected to benefit from industry consolidation."

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-05/13/content_7770741.htm) ([see archive](Action_plan_booster_shot_for_equipment_manufacturers.pdf))

### Govt gives a boost to TCM use

Traditional Chinese Medicine (TCM) has a new prescription for health as medical institutions will now be required to bolster their TCM departments.

A circular released recently by the State Council ordered local governments to include hospitals for traditional medicine in their health service networks.

It also requires health institutions to improve TCM training, facilities and medicines.

"Every community health service station and village health clinic should be able to offer TCM services," the circular said.

Governments at various levels will increase investment in public hospitals for traditional medicine to improve facilities, support research and train doctors.

"The guideline plays an important part in playing up the use of TCM in the recent medical reform," Wang Guoqiang, director of the State Administration of Traditional Chinese Medicine said recently.

"It will boost TCM development with concrete support from governments at all levels."

One of the highlights is that "the circular positions TCM equally with western medicines in legal status, academic development and in practice," said Wang, who is also vice-minister of health.

"Traditional medicines have outstanding advantages. They cost much less than western medicines," Professor Ha Xiaoxian from Tianjin University of Traditional Chinese Medicine was quoted by Xinhua as saying.

"They will fit in with the health service in rural areas and communities."

In the circular, the State Council said traditional medicines will be included with the State's basic medicines and traditional medicine hospitals will be in the list of designated hospitals under the country's basic health insurance programs for both rural and urban residents.

The government will welcome private investors to invest in hospitals or pharmacies for traditional medicine.

It also encourages veteran doctors to open their own clinics and allows doctors to work at dispensing shops that sell traditional medicines.

According to the circular, the government plans to register ancient medical books, develop a catalog and set up a digital database for them.

The government also encourages apprenticeships for training doctors as an alternative to medical schools, especially in rural areas.

Traditional Chinese medicine has unique theories and practices such as herbal medicines, acupuncture, massage and dietary therapy, independent from western medicine.

For some time, it was pushed to the side as many of its theories could not be explained by modern medicine, but it has recently become popular among Chinese as an alternative way to keep fit.

"Traditional medicine performs well in treating chronic diseases and its theories help people develop healthy life styles," Ha said.

[Source: People's Daily](http://english.peopledaily.com.cn/90001/6653344.html) ([see archive](Govt_gives_a_boost_to_TCM_use.pdf))

## Other

### SAT Regulated Preferential EIT Policies on Venture Capital Enterprises

Qualified venture capital enterprises are eligible to deduct 70% of their investment in small and medium-sized high-tech enterprises from the taxable incomes in the year when they have possessed the equities for 2 years.

Under the Circular on Issues Concerning Implementing Preferential Enterprise Income Tax Policies on Venture Capital Enterprises (Circular) released by China's State Administration of Taxation (SAT) on April 30, 2009, the aforementioned qualifications shall include: enterprises must have invested in the un-listed small and medium-sized high-tech enterprises via equity investment for more than 24 months; the invested small and medium-sized high-tech enterprises must be qualified with the high-tech enterprise authorization. In addition, number of the staff must not exceed 500, and their annual sales (business) volume and total assets must not exceed 200 million.

The Circular shall take effect as of January 1, 2008.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=5745) ([see archive](SAT_Regulated_Preferential_EIT_Policies_on_Venture_Capital_Enterprises.pdf))

### Auto sales may top 10m units this year

China's booming automobile market is expected to break the 10-million-unit in sales barrier this year, as the government's positive measures drive demand and revive consumer confidence, an industry body said recently.

China Association of Automobile Manufacturers (CAAM) has upgraded its forecast for this year's automobile sales to 10.2 million units, with year-on-year growth rate of 8.7 percent, up from the 5 percent projection earlier this year, said Dong Yang, its deputy director.

The passenger car segment is expected to grow by 10.2 percent while commercial vehicle sales are likely to increase by 5 percent this year, Dong said.

The association modified its forecast after vehicle sales hit a monthly record in April, the second consecutive month since March, with a year-on-year growth of 25 percent.

"It seems 2009 will be an optimistic year for China's automobile market, but we all should be cautious amid the gloomy global environment," said Dong.

According to CAAM, 1.153 million vehicles were sold in China last month, up 3.91 percent from March.

"The back-to-back pick-up in sales showed that China's auto industry has recovered and the government's stimulus package is taking effect," said Dong.

"Those vehicles that are eligible for government subsidies, which account for around 52 percent of the total industry, were the major driving force behind the rapid sales growth," said Zhu Yiping, associate secretary-general of CAAM.

The sales of passenger cars with engine capacity of or less than 1.6 liters increased by 56.5 percent over April 2008, to 419,000 units.

However, commercial vehicles continued to show a downtrend with 1 million units sold in April, a drop of 3.86 percent year-on-year.

In the first quarter, the total revenues of 19 major automakers dropped 14.2 percent, with their combined profits diving 48.36 percent year-on-year, according to CAAM.

In April, the US automobile market showed a 34.4 percent fall in unit sales over the past year, the lowest year-on-year growth rate in 30 years.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-05/12/content_7766591.htm) ([see archive](Auto_sales_may_top_10m_units_this_year.pdf))

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