

CHINA FOCUS

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Is China's Door Closing?

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This year marks the 40th anniversary since Deng Xiaoping's "Open Door Policy" kickstarted China's opening up to the world. President Xi Jinping has promised that the country's doors will continue to open "wider and wider" to foreign trade and investment. But against the backdrop of rising trade tensions on the global stage, and grand industrial ambitions at home, will China keep its word?

Many of our clients are optimistic. They welcome recent tax reductions and the lifting of foreign-ownership caps in the automotive and financial sectors (see p. 2). They appreciate China's anti-pollution drive

– despite its short-term costliness – for its effective and fair enforcement across foreign-invested and domestic entities. And they see fields of opportunity in the country's wealthy and experimental consumer market (see p. 4).

But new roadblocks have also emerged. In sectors where China is pursuing dominance, such as high-tech manufacturing and materials, some feel that government funding, unfair licensing processes, and "buy local" policies are skewing competition in favour of domestic players.

Across industries, international firms are also burdened by China's ever more impenetrable "Great Firewall". And when it comes to the US-China trade dispute, it's either already causing cost hikes (see p. 3) or threatening to seriously disrupt supply chains if it keeps escalating – a scenario which, unfortunately, looks increasingly likely.

So which way is China's door swinging? For executives who are drawing business plans and making investment decisions, it might seem necessary to side either with the optimists or pessimists. But our recommendation is not to. The future of

China's business environment is too complex and industry-specific to make simplistic projections. Some doors will close but others will open. Accepting this is the starting point to ensuring that your business is ready to avert risks as well as seize opportunities.

For four decades, China's gradual reforms and export-led growth model have benefited the Chinese economy and foreign companies simultaneously. Now that China has established itself as an economic power, it is pursuing a second wave of tech-driven development with larger global ambitions. This time around, it's harder to say whether the results will be "win-win".

In a climate of geopolitical uncertainty, it's more important than ever to have open, informed discussions about China's business environment. This issue of China Focus is our attempt to spark a nuanced conversation. We invite you to join our upcoming events, where we will keep exploring the open doors and firewalls that matter for your China business. ☘



German-speaking event
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China's grand mission to shift gears towards high-tech and consumption-led growth has coincided with a rise in global tensions. The result is an eventful year full of frequent and sometimes confusing regulatory moves. In an attempt to make sense of it all, we have put together a table highlighting some of the reforms and barriers that have impacted our clients the most over the past year.

OPEN DOORS FIREWALLS

	OPEN DOORS	FIREWALLS
TRADE	 <p>Chinese Tariff Cuts</p> <ul style="list-style-type: none"> ▶ Dec 2017 - Jul 2018: Tariff cuts on 1,700 types of consumer goods including food, garments, and sport gear took effect. ▶ Jul 2018: Tariffs on cars and car parts were reduced. Only 4% of cars sold in China are imported, so the impact has been small. 	 <p>US-China Trade Dispute</p> <ul style="list-style-type: none"> ▶ Jul 2018: US imposed 25% tariffs on \$34b worth of Chinese goods, e.g. medical equipment, machinery, and cars. China raised equal tariffs on US food and e-vehicles. ▶ Aug 2018: US threatened China with further tariffs on \$200b worth of goods. China vowed to retaliate.
MARKET ACCESS	 <p>Liberalisation in Key Sectors</p> <ul style="list-style-type: none"> ▶ China vowed to phase out the rule forcing foreign carmakers to form local joint ventures. Tesla signed an agreement to open a wholly-owned plant in Shanghai. ▶ Foreign ownership caps for financial services and life insurance firms will be raised from 49% to 51%. 	 <p>“Made in China 2025”</p> <ul style="list-style-type: none"> ▶ 43% of EU firms surveyed by the EUCCC in 2018 reported “increased discrimination” under MIC2025 (China’s plan to dominate high-tech industries). ▶ MIC2025 barriers include “buy local” policies. E.g. Since 2017, Sichuan hospitals can only buy China-made PET/CT scanners.
	 <p>“Negative List” Updates</p> <ul style="list-style-type: none"> ▶ China’s “Negative List” outlines all sectors where FDI is prohibited/restricted. In 2018, the list was cut for the 7th consecutive year. ▶ However, many reformed sectors are still blocked by strict licensing requirements, SOE dominance or unofficial barriers. 	 <p>Stricter Merger Reviews</p> <ul style="list-style-type: none"> ▶ Jul 2018: China warned it will broaden its merger review process – following similar moves by the US and Germany. ▶ Trade war weapon? Chinese regulators failed to approve Qualcomm’s takeover of NXP (the biggest semiconductor deal ever) shortly after the US went ahead with tariffs.
EASE OF DOING BUSINESS	 <p>Simplified Business Setups</p> <ul style="list-style-type: none"> ▶ “One Window, One Form”: A reform to simplify foreign business registrations was rolled out nationwide on June 30. The real extent of the reform is yet to be seen. ▶ “Internet Plus”: >70% of government services for foreign investors are planned to be accessible online by the end of 2019. 	 <p>The “Great Firewall”</p> <ul style="list-style-type: none"> ▶ US and EU chamber surveys rank China’s web restrictions as a top operational burden. Banned websites/apps hamper communication and data exchange. ▶ The 2017 Cybersecurity Law requires foreign entities to store data locally, which implies costly and complex IT solutions.
	 <p>Tax Cuts</p> <ul style="list-style-type: none"> ▶ May 2018: First round of VAT cuts (part of a US\$64b tax cut plan for 2018) take effect: <ul style="list-style-type: none"> • Manufacturing: 17% → 16% • Transportation, construction, agricultural, and telecom enterprises: 11% → 10% 	 <p>Anti-Pollution Crackdown</p> <ul style="list-style-type: none"> ▶ Since early 2017, China has ramped up factory inspections and introduced an Environmental Protection Tax. The result: higher compliance and production costs, factory closures, and tougher approvals for construction sites.