CHINA Insights

Corporate FX & Structured Products
Tel: 6349-1888 / 1881

Fixed Income & Structured Products
Tel: 6349-1810

Investments & Structured Product
Tel: 6349-1886

Interest Rate Derivatives
Tel: 6349-1899

Treasury Research & Strategy
Tel: 6530-4887

Tommy Xie Dongming

+(65) 6530 7256

xied@ocbc.com

Sailing against the current

Thursday, January 19, 2017

Highlights:

- **The State Council approved detailed plans to relax restrictions on foreign investment.**
- **The new rules will ease the investment barrier for three sectors including service industry, manufacturing and mining industry. Meanwhile, foreign investors will also be allowed to participate in infrastructure investment.**
- **China will continue to improve fair treatment for foreign investors.**
- **China will create a supportive environment to improve the efficiency of capital usage and broadening funding channels for foreign investors.**
- **China will also give foreign investors tax discount to invest in less developed areas.**
- **The latest announcement shows China's attitude to fill the US gap in promoting globalization. This is helpful to offset the capital outflow risk.**

China reacted to the emerging risk of protectionism with an open mind. The State Council approved detailed plans to relax restrictions on foreign investment. This echoed President Xi Jinping's remarks in Davos this week that "pursuing protectionism is just like locking oneself in a dark room: wind and rain might be kept outside but so are light and air."

China's foreign direct investment inflow has slowed down after peaking in 2013 as a result of slower growth outlook and rising costs. The net FDI inflows under the Balance of Payment decelerated to US$32.23 billion as of 3Q 2016, lowest since 2Q 2009. In contrast, China's overseas direct investment expanded rapidly. As such, China has recorded the deficit in direct investment for the first time in 2016, which has become one of the key drivers to RMB depreciation.

The new rules will ease the investment barrier for three sectors including service industry, manufacturing and mining industry. For service sector, foreign investment curbs on banking, security company, asset management, futures, insurance and insurance brokers will be eased. In addition, restrictions on accounting, audit, architect design and rating agency will also be eased while China will gradually ease restrictions on telecom, internet, culture, education and transportation sectors.

Chart 1: China's foreign direct investment has been falling

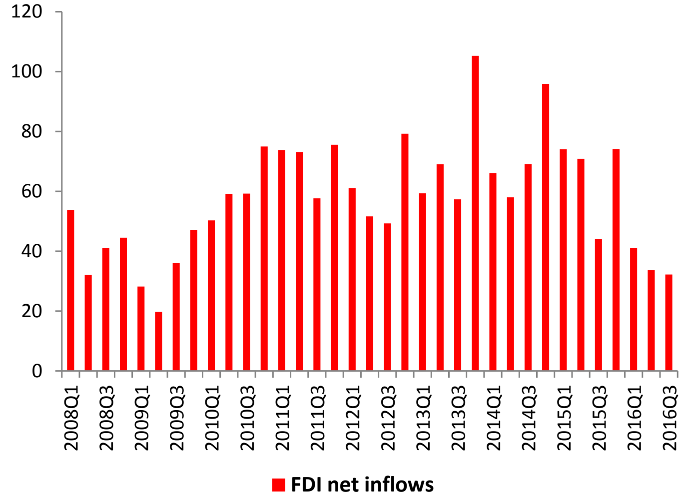
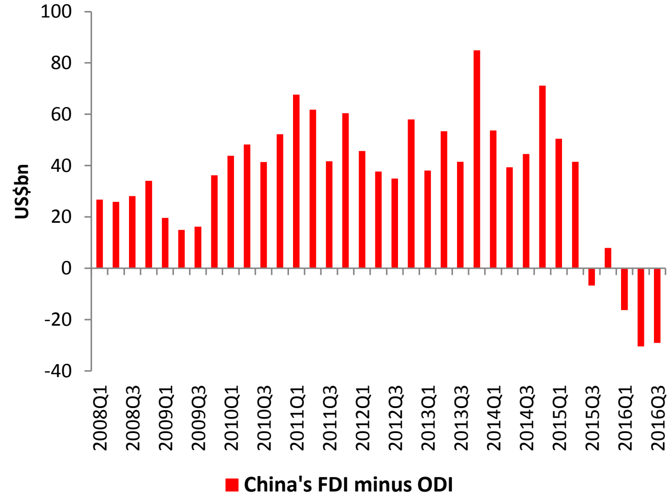


Chart 2: First deficit in direct investment recorded in 2016



Source: Bloomberg, OCBC

Meanwhile, foreign investors will also be allowed to participate in infrastructure investment in form of franchise investment.

Fair treatment

China will continue to improve fair treatment for foreign investors. For example, the minimum registered capital for foreign investment will be eliminated. The same land policy will be applied to domestic and foreign investors. Incentives will be given to foreign investors on use of industrial land for as low as of 70% price. In addition, foreigners holding China permanent residence permit will be treated same as Chinese citizen when setting up the technology company in China.

More funding support

On funding, China will create a supportive environment to improve the efficiency of capital usage and ease funding for foreign investors. China will promote two-way flows to attract MNCs to set up their regional headquarters, purchasing centre and settlement centre in China. In addition, foreign investors will be able to access to the same channels as the local company to raise money via equity financing, bond financing as well as foreign debt.

Last but not least, China will also give foreign investors tax discount to invest in less developed areas such as Central China, West China and North East part of China.

Implications:

The latest announcement from the State Council shows China's attitude the fill US gap in promoting globalization. China's political stability and large domestic market are likely to attract more foreign investors should China lower the barrier and treat foreign investors fairly. As such, this may be helpful to offset the capital outflow risk, which may help alleviate pressure for RMB depreciation.

Co.Reg.no.:193200032W