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The 13th Five-Year Plan highlights the opportunities and challenges in China for Foreign Invested Enterprises

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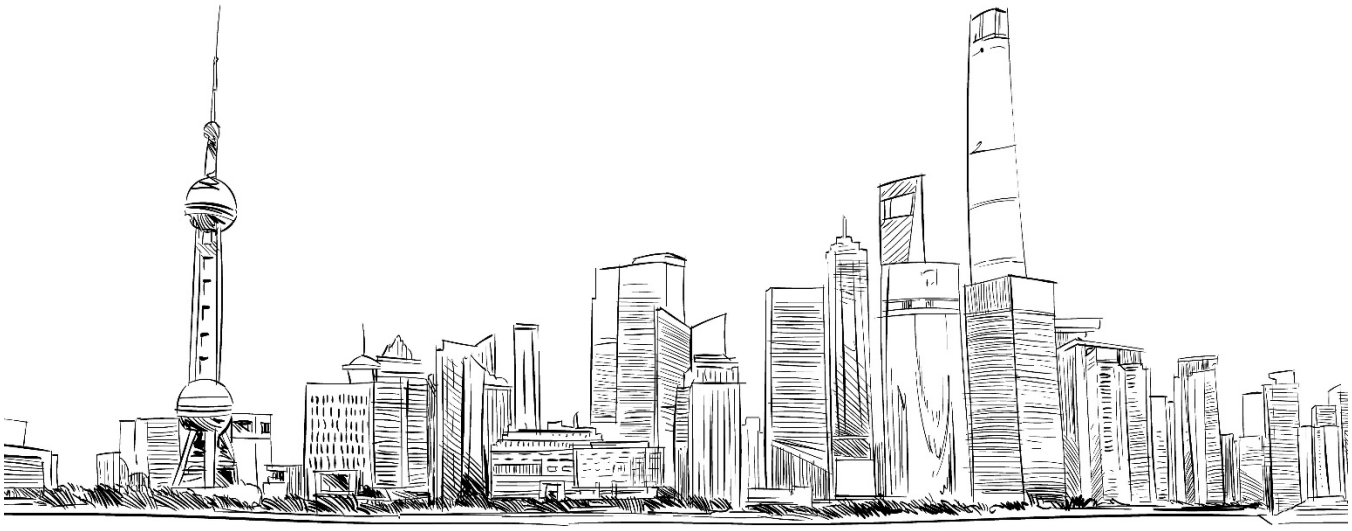

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The perception in China is that that there are constant limitations and obstacles when doing business. The 13th Five Year Plan (FYP) highlights these challenges that will be occurring for foreign investors. However, as indicated in the previous article, the "Negative List" is looking to reduce the threshold for foreign investment and foreign startups to enter the Chinese market – a positive aspect for foreign investors. In addition, there are opportunities for foreign investors in specific key sectors and industries as outlined in the 13th five-year plan (FYP).

The 13th FYP - ratified by the National People's Congress (NPC) in March 2016 - established Chinese President and General Secretary of the Chinese Communist Party (CCP) Xi Jinping's vision for China's development over the next five years.

The 13th FYP creates an outline for China's future development based around five key themes:

1. Innovation:

Innovation is a cornerstone of China's development strategy in the 13th FYP and will be an important component of moving Chinese manufacturing up the "value-added" manufacturing chain and enhancing its future global competitiveness and technological edge. The plan establishes broad goals for China's economy to become:

- an innovative nation by 2020,
- an international innovation leader by 2030 and
- a world powerhouse of scientific and technological innovation by 2050.

The 13th FYP supports the "Made in China 2025" and "Internet Plus" initiatives as key policies to move up the value-added chain. These initiatives seek to accelerate China's transition to higher-value-added, intelligent manufacturing by focusing on innovation and upgrading emerging industries, such as

- high-end equipment,
- integrated circuits,
- biomedicines,
- cloud computing,
- mobile Internet,
- and e-commerce.

In support of these sectors, the Chinese government cultivates local and national champions, negotiates for technology transfers as the price of market access, regulates foreign investment and technology imports through government catalogues, promotes Chinese technology standards domestically and internationally, and supports greater Chinese exports through its "Going Out" strategy.
The "Made in China 2025" Action Plan lays out 12 targets with 2020 and 2025 deadlines that focus on

enhancing China's innovation, productivity, quality, digitalization, and efficiency. For example, automation and efficiency targets aim to improve Chinese firms' productivity and move their products up the value-added chain by increasing intelligent manufacturing capabilities. In addition, this initiative seeks to build domestic firms that are globally competitive with a goal of gradually substituting foreign technology and products with local technology and production first at home then abroad. Although this top-down initiative reiterates the Chinese government's long-held objectives toward indigenous innovation and import substitution, Made in China 2025 is larger in scope and resources with greater government coordination than previous plans. Made in China 2025 targets ten key sectors for additional government support. These sectors are:

1. new energy vehicles,
2. next-generation information technology (IT),
3. biotechnology,
4. new materials,
5. aerospace,
6. ocean engineering and high-tech ships,
7. railway,
8. robotics,
9. power equipment, and
10. agricultural machinery.

Many of these listed sectors are not new and merely redouble government support for long-held strategic industries.

To capitalize on China's huge online consumer market and optimize manufacturing, finance, healthcare, and government, the "Internet Plus" plan is aimed at building up the country's domestic mobile Internet, cloud computing, big data, and the "Internet of Things" sector firms and creating global competitors by assisting domestic firms' expansion abroad. Under the 13th FYP the Chinese government wants to improve Internet access in rural China—thus increasing China's consumer base.

2. Urban-rural, interregional, and global integration

The Chinese government is deepening urban-rural, interregional, and global integration to reduce economic and regional disparity, enhance urban planning and infrastructure development, redistribute industry drivers, and improve energy efficiency and environmental conservation. The 13th FYP outlines:

- urbanization,
- the Beijing-Tianjin-Hebei megaregion,
- the Yangtze Economic Belt initiative, and

- the Silk Road Economic Belt and 21st Century Maritime Silk Road initiatives (or One Belt, One Road);

as key to its coordinated development policy agenda. In April 2016, the State Council approved a "Chengdu-Chongqing city cluster" that will boost interregional development and pursue greater integration with the One Belt, One Road and Yangtze Economic Belt initiatives.

3. The "Green" development

The FYP reinforces the Chinese government's desire to address China's severe environmental degradation and build its clean energy, green manufacturing, and environmental service sectors. Environment-related targets account for 10 out of the 25 targets laid out in the 13th FYP, and all 10 are binding targets that must be met by 2020. Targets establish caps for energy use and ambitious goals for city air quality, carbon dioxide intensity, and reduction of soil and water contamination.

The Chinese government will support the growth of its energy-saving and environmental protection industries into globally competitive firms. Industries singled out for support include:

- new energy vehicles,
- soil remediation, and
- advanced energy-saving technologies and equipment.

The 13th Five-year plan is also attempting to retool China's heavy industry by pushing for green construction and green mining and mobilizing domestic and international investment toward green industries, pollution and climate change mitigation efforts, and environmentally friendly projects through green financing.

4. China's Globalization and Outbound Investment

The 13th FYP sets goals to benefit China's domestic industries' expansion abroad by increasing exports and outbound investment, supporting the international use of the RMB, and strengthening China's role in driving the international economic agenda and setting international standards. Encouragement of imports and inbound foreign investment is limited to designated sectors, where China is seeking to meet existing demand and build domestic capacity.

This imbalance signals that foreign firms will continue to face significant barriers to access China's market. In addition, the Chinese government is seeking to expand its interregional and international

trade through the creation of the Beijing-Tianjin-Hebei megaregion, the Yangtze Economic Belt, and the One Belt, One Road initiative. Priorities of China's openness theme include:

- Increasing exports: The 13th FYP attempts to boost exports with faster processing of export tax rebates, expansion of cross-border e-commerce, expansion of free trade zones, and support of trade in services.

- Encouraging select imports: Expansion of advanced technology and equipment and high-quality consumer product imports is strongly encouraged under the 13th FYP, potentially creating opportunities for Western high-value-added exports. In addition, the 13th FYP plans a greater opening of the finance, education, health, culture, Internet, and logistics sectors to foreign firms.

- Guiding investment to industrial and economic objectives: To meet growing domestic demand and remedy the lack of domestic capacity, the 13th FYP pledges to loosen foreign investment restrictions on preschools and childcare centers, elder care, architecture, accounting, auditing, banking, insurance, and securities. Reflecting both its industrial and economic objectives, the 13th FYP also encourages greater foreign investment in advanced manufacturing, high-tech, energy-saving and environmental protection, and modern services, particularly in central and western provinces. However, China maintains a pattern of first welcoming foreign investment into strategic sectors to gain foreign technology, intellectual property, and know-how then restricting investment in those sectors as domestic firms become competitive. This policy creates market space for China's new firms by pushing out foreign competitors. Thus, the sectors outlined in 13th FYP will likely enjoy only a temporary respite from a loosening of China's market access barriers. Foreign companies operating in industries championed by the 13th FYP are likely to see market barriers temporarily loosened in ways that benefit domestic competitors.

- Strengthening China's leadership in the international system: The 13th FYP outlines a greater role for China in reforming the international economic system and driving the international economic agenda through promotion of more equitable participation of developing countries; the pursuit of bilateral and multilateral free trade agreements; participation in the development of global Internet governance and international standards; and the formulation of international standards for the Internet, deep sea, the Arctic and Antarctica, and space.

- Promote the One Belt, One Road Initiative (OBOR): President Xi's OBOR initiative, first announced in 2013, is a cornerstone of the 13th FYP openness objective, accounting for an entire chapter in the plan. This initiative is composed of a land-based economic corridor through Central Asia and a maritime counterpart that will run through Southeast Asia and the Indian Ocean to Africa and the Mediterranean Sea. The goal of the OBOR initiative is to facilitate access to natural resources

and encourage economic development in China's poorer western provinces. The priorities of the OBOR is strengthening transportation infrastructure, easing investment and trade, enhancing financial cooperation, and deepening cultural exchanges. OBOR could provide significant economic benefits for the region through greater connectivity and development. However, because it prioritizes China's economic interests by focusing on exporting it's local competitiveness, OBOR could create regional dependence, especially among less developed countries, allow China to delay reining in its excess capacity, and limit access for non-Chinese firms to projects.

5. Boosting China's internal development:

The 13th FYP expands upon the 12th FYP to push to create a harmonious society toward pursuing "inclusive growth" for all Chinese citizens by alleviating poverty, raising Chinese citizens' standard of living, improving accessibility and affordability of healthcare services, and promoting education. These targets seek to increase household disposable income, expand basic retirement insurance coverage,

reduce the number of residents living below the poverty line, redevelop urban shantytowns, and expand average education levels. Broader urbanization efforts, higher-value-added manufacturing, and environmental reforms will also bolster the 13th FYP goals to alleviate poverty, boost domestic consumption, and create new drivers of economic growth.

Conclusion

The Chinese government's continued interference in the domestic economy and legal system reinforces its objective to open the world to China, not China to the world.

The Chinese government continues to use preferential support for domestic firms, localization targets, and high market access barriers to build domestic capacity and eventually replace foreign technology and products with domestic technology and production first at home then abroad. These policies are slowly closing market opportunities for foreign firms in China and creating new Chinese competitors that will be able to challenge foreign companies, with potential negative impacts on overseas employment, productivity, and innovation.

High market access barriers for foreign firms remain and are only loosened in sectors where China is

seeking to meet demand and build domestic capacity. For example, the Chinese government has permitted foreign investment in the automobile and aviation sectors—industries the Chinese government has long sought to develop—but this access has come at a cost. Foreign automotive and aviation firms must form joint ventures with Chinese SOEs and integrate Chinese firms into their production and supply chains as the price of entry.

In line with its objectives to move up the value-added chain and meet its growing domestic consumption needs, the Chinese government uses the 13th FYP to encourage advanced technology and high-quality consumer product imports and inbound foreign investment in select industries. This lowering of market barriers on previously restricted sectors creates new markets for foreign firms. However, this expanded access is unlikely to last. The Chinese government has a history of gradually pushing out foreign firms by reinstituting investment restrictions once domestic firms become competitive.

Finally, the 13th FYP agenda will require significant private capital to adequately fund its mandates. Urban infrastructure projects, healthcare and pension spending, and environmental remediation efforts alone will cost trillions of dollars. The Chinese government has already acknowledged it will only be able to fund a portion of these needed efforts and is seeking foreign and domestic private investment to make up the difference. But to attract this investment, the Chinese government will need to further loosen capital controls, limit intervention in the market, and lower existing market access barriers for foreign financial service firms. The Chinese government has thus far not implemented such reforms because they weaken the role of the state and increase market volatility.

A risky and complex market

The overall conclusion of this article is YES – through the 13th FYP there are plenty of opportunities for foreign invested enterprises to enter the Chinese market. It is a matter of how quickly you approach the market and take advantage of all the benefits being offered by the Chinese government. It is critical to be aware that as domestic companies flourish and become more “equal” counterparts, restrictions may come into effect for the foreign investors. At that point, it will not be a fair playing field any longer, but rather a question of “who has the right product/service for the right price and quality and more importantly who holds the relationship”. The longer you are in the market, the more time you have available to create and maintain relationships for the development of your business. Develop this “guanxi” and your business will be a success.

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