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# China News Alert Issue 326

## Capital Markets

### China overtakes Germany as world's top exporter

Germany's multi-year reign as the world's number 1 exporter is officially over, with the crown passing to rising China after new figures show that German exports slid by nearly a fifth in 2009, their biggest decline in 60 years.

The German government figures only confirmed an open secret: China's runaway growth and resilience amid the financial crisis put its exports ahead of Germany, which suffered a severe recession before returning to growth in last year's second quarter.

Last month, China's customs reported that total 2009 exports were more than US$1.2 trillion, well ahead of the €803.2 billion (US$1.1 trillion) that Germany reported.

For Germany, the figure was a drop of 18.4 percent from 2008, although exports returned to year-on-year growth in December.

"The crisis has accelerated the shift in power in world trade toward the emerging countries," said Anton Boerner, the head of Germany's BGA exporters' association. However, "the fact that we are passing on the title of world export champion to China doesn't cause us any worries," he added. "The growth of the Chinese economy will also secure our growth and jobs in Germany for many years."

Boerner noted that in December demand for German products from all parts of the world was up year on year. Declining imports indicate that "large parts of the economy are still in neutral," Boerner said. "Everything must be done to encourage and stabilise the upturn in exports."

Germany took over the top spot in terms of exports in 2003, surpassing the US.

China's newfound status is mostly symbolic but highlights its growing presence as an industrial power, major buyer of oil, iron ore and other commodities and, increasingly, as an investor and key voice in managing the global economy. Its ability to unseat longtime export leader Germany reflected the ability of agile, low-cost Chinese manufacturers to keep selling abroad even as other exporters have been hammered by a slump in global demand.

The change is the second time in three years Germany has been overtaken by China. In 2007, China surpassed Germany to become the world's third-largest economy, just behind number 2 Japan and the United States, which held the top spot.

China's growth also benefits other companies and countries, but particularly those in Germany, because of its voracious demand for raw materials, consumer goods and more. Germany's leading luxury car makers, Mercedes-Benz, BMW AG and Audi AG, all have reported that their sales in China more than doubled year on year last month, helping them to improve their global performance. Germany and Europe are also noted for quality and craftsmanship.

Nick Reilly, the new chief executive of General Motors Company's German-based European unit, Opel, said he believes that "manufacturing must have and will have a bright future in Europe." "Yes, wage rates are higher here than in other countries, but productivity, production excellence, logistics costs, quality and the work force's outstanding skill base largely offset that cost disadvantage," said Reilly, who was previously the US automaker's Shanghai-based executive vice president of international operations. He pointed to "Opel's German engineering" as an asset to GM.

[Source: China Daily](http://www.chinadaily.com.cn/2010-02/10/content_9453359.htm) ([archived copy](China_overtakes_Germany_as_world_top_exporter.pdf))

### China's rate of inflation is 'still low'

Central bank signal comes amid division over interest rate hikes. Central bank governor Zhou Xiaochuan has said China's inflation rate remains "relatively low", amid ongoing debate among officials and economists on when policymakers should raise interest rates to rein in rising inflation and asset prices.

The inflation rate still needs to be "closely watched", Zhou told reporters in Sydney after a meeting with other central bankers.

China's consumer price index (CPI), a major measure of inflation, rose by 1.9 percent in December from 0.6 percent in November, due to the country's ample liquidity. The country initiated its economic stimulus plan to keep economic growth stable in late 2008. Chinese banks extended 9.6 trillion yuan (US$1.4 trillion) in new yuan loans in 2009, almost double that of 2008, while the lending in January is forecast to reach 1.3 trillion yuan.

The rapidly rising inflation, together with surging house prices, has led to expectations of imminent interest rate hikes. The stock market has also been declining in recent trading days as investors expected more tightening policies following the country's move to raise the reserve requirement ratio of commercial banks and tighten real estate deals.

But Dai Xianglong, chairman of the influential National Social Security Fund, said in a speech in India that China was unlikely to raise interest rates in the first half of 2010 as the economic recovery was still not on solid ground.

Dai, a former central bank governor, said that despite possible policy adjustments to combat inflation and asset bubbles, money and lending supply will remain relatively loose over the course of the year. "Interest rate hikes are not the most appropriate tool if policymakers want to control inflation," said Zuo Xiaolei, chief economist of China Galaxy Securities. China's recent inflation rise, in essence, stems from increasing liquidity in the financial system. The best way to curb inflation is to raise banks' reserve requirement rate or conduct open market operations, she said.

China announced the raising of banks' reserve requirement ratio, or the proportion of money commercial banks must keep in reserve, on 12th January. It has also resorted to a number of open market operations to mop up liquidity as banks rushed to lend to pre-empt a possible tightening of policy.

China may continue to raise the requirement ratio this year, possibly increasing it three or four times to 18 percent from the current 16 percent, said Qu Hongbin, chief China economist of HSBC. Qu said an interest rate hike could come in April because inflation could be very serious if interest rates are not raised. China is scheduled to release its first-quarter economic data in mid-April.

Economists also forecast that China's CPI could be mild in January, because of the relatively high base of last January. China's traditional Spring Festival fell in January last year. But it can rise up to 3 percent in February as consumption can still pick up during the Chinese New Year period, which starts on 14th February, analysts said. Inflation could stabilise later, Nomura Securities reported. "If that happens, the possibility of interest rate hikes would decrease," said Zhang Lan, head of research at Shanghai-based Changjiang Securities.

[Source: People's Daily](http://english.people.com.cn/90001/90778/90859/6892076.html) ([archived copy](Rate_of_inflation_still_low.pdf))

## Corporate & Commercial

### Luxury carmakers trade up to China market

China has become the target market for the world's luxury auto manufacturers as demand for upscale vehicles surged last year despite a global slump.

"China has been the most important market for luxury vehicles, so with consumption power increasing, the structure of the global automobile market is also changing and shifting its focus to China," said Liu Siyang, chief researcher with Samsung Economic Research Institute. "In the years to come, China's automobile market will not only improve sales numbers, but also enhance itself through sector restructuring."

Analysts believe that with the economy growing again wealthy individuals will increasingly drive demand for luxury vehicles in China.

Statistics from Boston Consulting Group show that by the end of 2009, China had 450,000 millionaires (calculated in US dollars), and over the next four years that number will rise to 800,000.

In 2008, 33.4 out of 100 Chinese families owned a vehicle, compared with 16.2 out of 100 in 2005.

According to the German luxury carmaker Audi, last year, 392,000 premium cars were sold in China, a surge of 38 percent over 2008.

"In the European and American markets, as well as Japan, one out of every five car owners drives a luxury sedan. However, the figure in China is one in 10," Klaus Maier, president and CEO of Mercedes-Benz China told China Daily, indicating the growth potential for the luxury car market is strong.

The German automaker concluded 2009 with its highest sales figures in its 23-year history in China, with 68,500 units moved off lots last year; that positioned the company as a market leader with the highest growth rate in the luxury sector, an annual increase of 77 percent year-on-year.

The Mercedes' S-Class luxury car had sales of nearly 15,000 units in 2009, reinforcing the fact China is one of the company's largest markets in the world. "China was our group's fourth-largest market last year we are confident that the country will be Mercedes' number 3 global market this year," said Maier. He predicts China's luxury car sector will expand slightly faster than the industry as a whole, which is up 10 to 15 percent so far this year.

Mercedes' German rival BMW reported record sales of 90,536 units in 2009, a 38 percent year-on-year increase.

BMW and its Chinese partner, Brilliance Auto Group, announced last November that they would invest at least 5 billion yuan in China to construct a new plant designed to boost the joint-venture'sBMW Brilliance Automotiveannual output from 30,000 to 75,000 units by the end of 2010.

For Audi, 2009 China sales surged 33 percent to 157,188 vehicles over the previous year, allowing it to easily maintain its dominance of the nation's luxury car segment.

Johannes Thammer, general manager of Audi sales division at Sino-German joint venture FAW Volkswagen Automobile Company, said he expects China's overall luxury car sector to rise by 25 to 30 percent this year.

Porsche SE, which counts China as its third biggest market, said it aims to sell over 10,000 cars in the country this year as rising wealth makes luxury vehicles more affordable. Porsche increased sales by about 9 percent to 9,090 vehicles in China last year.

[Source: People's Daily](http://english.people.com.cn/90001/90778/90860/6891305.html) ([see archive](Luxury_carmakers_trade_up_to_China_market.pdf))

### SMIC to upgrade facilities in profit hunt

Semiconductor Manufacturing International Corporation (SMIC) said that it plans to significantly boost its capital spending this year to upgrade its current facilities in an effort to improve competitiveness and return to profit.

David Wang, the newly appointed chief executive of China's largest contract chip maker, said the company plans capital spending of US$335 million this year, up 76 percent from US$189.9 million last year. He said SMIC aims to maintain its gross margin at double digits throughout 2010 and outpace the chip foundry market's average 20 percent growth this year.

Founded in 2000, SMIC is the largest foundry in the mainland and gets significant support from the Chinese government, which has long been trying to build up its high-value-added technology industries.

However, after getting off to a relatively strong start, SMIC has posted net losses for the past 14 quarters, as it struggles to gain the scale necessary to compete with Taiwan Semiconductor Manufacturing Company (TSMC) and United Microelectronics Corporation (UMC), the world's top two contract chipmakers.

At the end of last year, SMIC announced that Richard Chang, the company's founder and chief executive, would leave the firm and would be replaced by David Wang, a 63-year-old director at Solar Fun Power Holdings.

"One specific goal is sustained profitability," said Wang in his first quarterly results call since becoming CEO. "To achieve this goal we need to make the company more solid in all aspects of the operation."

SMIC said its fourth-quarter revenue totaled US$333.1 million, up 3 percent from the previous quarter and up 22.2 percent from a year earlier. It said it expected revenue to rise 2 percent in the first quarter.

SMIC also announced an overhaul of its top management, including the naming of new chief financial and operating officers.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2010-02/11/content_9461621.htm) ([see archive](SMIC_to_upgrade_facilities_in_profit_hunt.pdf))

### CNPC clinches deal to develop Iranian gas field

China National Petroleum Corporation (CNPC), the country's largest oil and gas producer, has clinched a deal to develop phase 11 of Iran's South Pars gas project, and beef up its oil and gas operations in the country that holds one of the world's top oil and gas reserves, an industry official told media.

CNPC will start drillings in the gas field as early as March to evaluate the reserves, after its initial overall development plan won Tehran's approval near the end of last year, pushing ahead the mega-project worth US$4.7 billion after a preliminary pact was sealed last June. "The real work will start as soon as after the Chinese New Year holiday," said the official familiar with CNPC's international operations.

CNPC, parent of listed PetroChina, had in December beefed up staff to about 60, based in Beijing and Tehran, dedicated to operations in Iran that also include two oil projects: North Azadegan and the smaller Masjed-i-Suleiman.

CNPC's spokesperson was not immediately available for comment.

Company officials told reporters that CNPC had internally acclaimed 2009 as the year which marked one of the firm's biggest feats in its decades-long overseas drive, led by company Chairman Jiang Jiemin.

Apart from the South Pars deal, CNPC won two service contracts in Iraq to develop the giant Rumaila and Halfaya oilfields, allowing the firm access to total estimated reserves of about 21 billion barrels. "CNPC has made it a distinctive strategy to gain a foothold in countries with top reserve bases. Iraq and Iran are among the top in the list," the official said.

But production from the giant South Pars field remains in question partly because the United States and US sanctions prohibit access to key liquefying gas technologies that are mostly in the hands of US firms, analysts have said.

It was not clear if Petronas, Malaysia's state oil and gas firm, would still tie up with CNPC for the South Pars project. Petronas said last June that it would partner with CNPC when the Chinese firm takes over as the main foreign investor.

CNPC said earlier it increased its overseas production to a record last year after gaining access to more fields in Kazakhstan and Canada. The company boosted crude oil output by 12 percent to 69.62 million metric tons from fields outside China in 2009. Natural gas production gained 22 percent to 8.2 billion cu m, while overseas refineries boosted the volume of oil processed to 10.08 million tons.

[Source: People's Daily](http://english.people.com.cn/90001/90778/90861/6893075.html) ([see archive](CNPC_clinches_deal_to_develop_Iranian_gas_field.pdf))

### Dairy consolidation gathers pace as New Hope acquires the remaining 41 percent stake in Anhui Purity

New Hope Dairy, a wholly owned subsidiary of New Hope Group, said it had acquired full ownership of Anhui Purity Dairy Company Limited after buying the remaining 41 percent stake in the company.

Sichuan-based New Hope Group said in a filing to the Shenzhen Stock Exchange that it paid 26.51 million yuan for the remaining stake in the State-owned dairy. "It highlights New Hope's ambition to compete in the high-growth dairy market," said Qin Jun, an industry analyst with Guotai Junan Securities.

According to Qin, New Hope Dairy has now 12 local dairy brands and is highly likely to consolidate them into its own.

In recent years, New Hope Dairy has acquired a total of 12 small- and medium-sized dairy companies in Hefei, Anhui province, Baoding, Hebei province, Changchun, Jilin province and Qingdao in Shandong province. "Although the dairy market is dominated by three big companiesYili, Mengniu and Bright Dairythere still remains growth potential for newcomers to tap," said Qin.

"Since the melamine scandal was made public in 2008, the domestic milk industry went into freefall in both reputation and sales. The industry-wide crisis forced the top three giants to slow the pace of their consolidation. This leaves some opportunities for players in the second-tier group, such as New Hope Dairy," added Qin.

China's per capita milk consumption among urban residents was only 27 kilograms in 2008, nearly one-tenth the amount in the US, and the figure will be even lower in rural areas, according to the analyst.

Wu Zhengwu, an analyst with Aijian Securities, said New Hope Dairy will encounter fierce competition in vying for a larger market share. "The overall market has already formed, and it's hard to disturb the status quo. In addition, an increasing number of foreign milk powder brands are entering. A newly launched brand such as New Hope will face a lot of difficulties," Wu said.

New Hope Group is the nation's largest animal feed producer, but its profits from animal feed and a meat processing sideline are declining. In recent years, 80 percent of its earnings came from profits in investments in China Minsheng Bank, said Wu.

Analysts said in the past decade, New Hope Group made a lot of money from equity investments and property development. "Neither of them are its core business but, as we all know, making money from the agricultural industry is time-consuming and the profit is lower than from other industries," said Qin.

In an interview with the Economic Daily, Liu Yonghao, chairman of New Hope Group, said he was determined to prioritise the agricultural industry in his blueprint for the group. "The first document issued by the central government will encourage us to make further developments in agriculture," Liu said.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2010-02/11/content_9462755.htm) ([see archive](Dairy_consolidation_moves_gather_pace.pdf))

### Chinese shoemaker coalition supports nation's WTO action against EU shoe levy

A business coalition made up of more than 100 Chinese shoemakers, material and machinery providers, issued a statement voicing support for China's decision to launch action in the WTO against EU duties on Chinese shoes.

China filed the complaint with the WTO (World Trade Organisation) on 4th February after the EU's decision to extend anti-dumping duties. In the statement, the coalition said it was an active participant throughout the EU's investigation and that it believes the EU measure ignores the economic situation of the global shoe industry and hurts the EU industry's longer-term interests.

The coalition said, "China's decision is an important step to ensure the country's legitimate trade interests are protected under the WTO legal framework." "The challenge through the WTO to the EU's imposition of the anti-dumping duties is justified. It is not a case of China throwing its weight around, but merely a WTO member taking its first step in protecting its trade interests," Wu Zhenchang, president of the coalition and chairman of the board of Guangdong-based shoemaker Chuangxin, said.

"The EU's anti-dumping duties on Chinese shoes don't make any sense and it harms the commercial interests of both the EU and China," he said.

Wu also said some leading European business, consumer and retail organisations have challenged the measures.

Under WTO dispute settlement procedures, the EU and China have 60 days after the complaint is filed to find a solution to their dispute through consultation. If consultation fails, China can ask for a WTO expert panel to investigate and rule on the dispute.

[Source: People's Daily](http://english.people.com.cn/90001/90778/90861/6893054.html) ([see archive](Chinese_shoemaker_coalition_supports_nations_WTO_action_against_EU_shoe_levy.pdf))

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