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# China News Alert Issue 349

## Capital Markets

### 'Softened' IMF tone eases yuan pressure

The International Monetary Fund's (IMF) softened tone towards China's exchange rate regime will ease pressure on the appreciation of the yuan, when the world's third-largest economy faces increasing risks of a slowdown, Chinese economists have said.

In a summary of comments by the IMF's 24-member executive board on Chinese policy released on 27th July, the Washington-based lender welcomed China's recent decision to return to a managed floating exchange rate system but contended that the yuan was still "undervalued".

The tone was slightly different from the IMF's long-held position, which claimed that the Chinese currency is "substantially undervalued". IMF Managing Director Dominique Strauss-Kahn reiterated the stance in June.

China scrapped the yuan's 23-month-old peg to the US dollar and pledged to seek greater flexibility in the value of its currency on 19th June. The yuan has edged up about 0.7 percent since.

"Given the current downside risk that the Chinese economy is facing and the complicated external environment, it is not realistic to expect the yuan to appreciate significantly," said Zhang Xiaojing, a senior economist at the Chinese Academy of Social Sciences. Zhang said he expects the yuan to rise about 3 percent this year.

" The view showed that the IMF has recognized China's effort in pursuing greater currency flexibility and generally agreed with the country's approach to let the yuan appreciate in a gradual manner," Zhang said.

The country's economic growth slowed to 10.3 percent in the second quarter, from the 11.9 percent three months earlier, due to tightening measures on the property sector and control on credit growth. These added to uncertainty in the country's economic outlook for the rest of the year, analysts said.

However, the IMF report indicated that it remained optimistic about China's growth outlook, forecasting that the Chinese economy will expand at 10.5 percent this year.

Hu Xiaolian, vice-governor of the People's Bank of China, the central bank, said in an article published on the bank's website last week that the exchange rate will maintain overall stability at a reasonable and balanced level. But the currency might show "two-way movements" against a single currency depending on market conditions, Hu said.

The IMF report said some of its board members agreed that the exchange rate is undervalued, but other members disagreed with the assessment of the exchange rate, noting that it is based on uncertain forecasts of the current account surplus.

The IMF's conciliatory tone came after the release of the much-awaited US Treasury report earlier this month, when it admitted that China's economic rebalancing policies have led to "a significant decline" in its current account surplus and "China has made progress" in rebalancing its growth. The Treasury report did not label China as a currency manipulator.

Chinese economists forecast that the country's exports will face tougher conditions in the second half due to lackluster external demand, which will lead to a further drop in the country's trade surplus.

"Since the outbreak of the financial crisis, it was the international capital flow, rather than current account surplus, that has contributed much to an imbalance in China's international payments," said Dong Xiaojun, professor at the economic research center with the Chinese Academy of Governance.

Current account surplus accounted for 69 percent of China's international payment surplus in 2009, compared with an average of 76.2 percent in the past decade, Dong said. The figure has dropped to 43 percent in the first quarter of this year, she said.

"Therefore, it is not reasonable to blame China's exports as the cause of the country's surplus in international payments. Countries implementing loose monetary policy during the crisis should also take the blame," she said.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2010-07/29/content_11065101.htm) ([see archive](Softened_IMF_tone_eases_yuan_pressure.pdf))

### China gets top ranking in survey of world's emerging economies

China ranks Number 1 among 27 emerging economies due to its huge consumer market and rapid economic growth, according to the Emerging Markets Opportunity Index released by US accounting firm Grant Thornton.

The index takes account of key factors such as the size of the economy, wealth, involvement in world trade, growth potential and levels of human development.

China scores 454 points, double the India's score (222 points) in second place and almost triple that of Russia (163 points) in third place.

"China leads the way thanks to the country's huge consumer market, an increasingly open economy and extremely rapid trade growth, which offer a myriad of business opportunities for potential investors," said Xia Zhidong, partner and vice-chairman of Grant Thornton China.

According to figures from the United Nations Conference on Trade and Development, China attracts the most foreign investment among the BRIC (Brazil, Russia, India and China) countries.

Last year, the inward foreign direct investment (FDI) flow to China was US$95 billion, followed by Russia at US$39 billion and with India and Brazil posting US$35 billion and US$26 billion respectively.

"In the future, more opportunities will lie in improved infrastructure, enhanced human capital, investments in R&D and the increasing middle-class base," Xia said.

However, a lack of skilled labour, increasing labour costs and the low per capita gross domestic product (GDP) pose major challenges to foreign investment in China.

According to Grant Thornton China, 23 percent of Chinese enterprises said they faced a shortage of skilled labour, higher than the global average of 21 percent.

In the top five places of the index, BRIC countries take four positions.

India, although a long way behind, boasts a huge consumer market and a booming services industry, which accounts for around 55 percent of GDP, compared to 40 percent in the Chinese mainland.

Russia, in third place, has a much smaller consumer base than either China or India, but it boasts a per capita GDP which is more than double that of China, and more than five times as high as India. In addition, its high-level per capita consumption is close to the levels of the major cities of Europe's advanced economies.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2010-07/28/content_11059443.htm) ([see archive](China_gets_top_ranking_in_survey_of_worlds_emerging_economies.pdf))

### Everbright Bank to list in Shanghai on 18th August

China Everbright Bank will list on the Shanghai stock exchange on 18th August, and will soon release its prospectus for an IPO slated to raise up to US$2.9 billion, the Shanghai Securities News reported on 29th July.

Everbright Bank, China's 11th biggest bank by assets, would sell up to 6.1 billion shares in the initial public offering. The paper said the bank will soon start its road shows in Beijing, Shanghai, Shenzhen and Guangzhou.

The China Securities Regulatory Commission said it had approved the IPO.

Everbright Bank's IPO follows Agricultural Bank of China's mammoth US$19 billion dual-listing earlier in July which had prompted a tight liquidity squeeze in Shanghai A shares.

Analysts say that upcoming IPOs including Everbright Bank's are unlikely to have a great impact on the stock market, which has rallied strongly in recent sessions as liquidity has sizably improved and investors eye reasonable valuations.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2010-07/29/content_11065900.htm) ([see archive](Everbright_Bank_to_list_in_Shanghai_on_Aug_18.pdf))

### China to strengthen punishment for illegal forex activities to curb hot money inflow

China's foreign exchange regulator has said that it will increase punishments for illegal foreign exchange activities.

The move aims to help curb the hot money inflows and promote sound development of the foreign exchange management, the State Administration of Foreign Exchange (SAFE), the regulator, said in a statement.

During the inspections in the past two years, SAFE found that some banks had relaxed approval regulations in a bid to quickly expand its foreign exchange business, though its statement does not list the names of the erring banks.

The regulator said it will intensify the scope and frequency of investigations into banks' foreign exchange activities.

Starting from February this year, investigations into speculative hot money, which have entered the country, betting on an appreciation of the Chinese currency, and a hike in asset prices, have found 190 cases, or US$7.35 billion, of hot money inflow, the SAFE said earlier this month.

Capital flow into and out of China for purposes other than import - export payments are strictly controlled by the SAFE, which manages China'sUS$2.45 in foreign exchange reserves.

[Source: English People](http://english.people.com.cn/90001/90778/90859/7086304.html) ([see archive](China_to_strengthen_punishment_for_illegal_forex_activities_to_curb_hot_money_inflows.pdf))

### CIC reaps gains from rosy overseas investments

China Investment Corporation (CIC), the nation's sovereign wealth fund, said it posted a solid return of 11.7 percent on its global investment portfolio in 2009, thanks to major global moves made last year.

The fund said it reaped a net profit of US$41.66 billion in 2009 after making a total investment of US$58 billion over the period.

If the domestic portfolio of State-owned financial institutions is also taken into consideration, the fund has made a return on registered capital of 12.9 percent, it said.

"We deployed significant capital into markets around the world last year and earned a satisfactory return for our shareholders," CIC Chairman Lou Jiwei said in its 2009 annual report, the second of its kind since the fund was established in late 2007.

Lou said the fund "accelerated its investment activities" since May 2009 as the global economy began to show signs of recovery. That compares to its strategy in 2008, when the fund kept the bulk of its assets in cash to limit losses amid the worsening global financial crisis.

The fund posted a negative 2.1 percent return from its global investment in 2008 with only US$4.8 billion being invested in overseas market.

By the end of 2009, over 32 percent of CIC's assets were in cash or cash equivalent products, 36 percent in global equities, 26 percent in fixed income securities and 6 percent in alternative investments.

"If the projects we pledged to invest in are taken into account, till now we have deployed some 90 percent of our available funds," a top fund official said.

Lou said this year will continue to present a challenging investment environment and the condition of the world economy is "by no means certain and markets remain volatile". CIC, established in 2007 with the mission to diversify China's financial holdings, embarked on its latest large-scale recruitment drive on Wednesday with 64 positions being advertised.

The fund is looking for financial professionals including asset allocation researchers, financial analysts, credit risk analysts and hedge fund analysts.

By the end of 2009, CIC had grown to nearly 250 team members, with over 80 percent having advanced degrees and over 50 percent having overseas work or education experience.

[Source: People's Daily](http://english.people.com.cn/90001/90778/90859/7086438.html) ([see archive](CIC_reaps_gains_from_rosy_overseas_investments.pdf))

### Agricultural Bank of China announces full exercise of over-allotment option

China's Agricultural Bank (ABC) has announced the over-allotment option for its global offering has been exercised in full by the joint bookrunners on behalf of the international underwriters on the day.

The move will bring about HK$11.96 billion (about US$1.54 billion) for the company, according to a statement released by ABC via the Hong Kong Stock Exchange.

The statement says the bank will issue a total of 3,811,764,000 H shares, represents approximately 15 percent of the Offer Shares initially available under its global offering, at HK$3.2 per share.

Meanwhile, the state-owned shareholders of the company are required to transfer to the Social Security Fund (SSF), in proportion to their respective shareholdings in the company, in aggregate equivalent to 10 percent of the number of the H shares issued under the over-allotment option, or pay the equivalent cash at the offer price to the SSF.

The A shares transferred to the SSF from the state-owned shareholders will be converted into H shares on a one-to-one basis.

The bank has already got approval from the Hong Kong Stock Exchange to list and trade the over-allotment shares on 5th August 2010.

[Source: People's Daily](http://english.people.com.cn/90001/90778/90859/7085816.html) ([see archive](Agricultural_Bank_of_China_announces_full_exercise_of_over-allotment_option.pdf))

## Corporate & Commercial

### China and Russia sign power-grid agreement

The State Grid Corp of China has signed a framework agreement with the Russian national grid operator to extend their collaboration on grid technology, cooperation and management, the company announced.

The cooperation will cover "technology and experience exchange, power grid construction and management, equipment supply, and technology consulting", State Grid said on its website.

According to Rusnews.cn, a Russian news portal, both companies will build a 500 kV, cross-border power line in the Amur region of Russia.

The project is scheduled to start in 2011. The investment value of the project was not disclosed.

The cooperation is in line with growing power cooperation between China and Russia, said analysts. In order to meet rising demand, China may increase power imports from Russia in the next few years.

The move is also in line with State Grid's strategy of going abroad, they said. The company has accelerated its overseas development in recent years.

Imported electricity from Russia surged in 2009, up more than 316 times over 2008 figures to reach 738 million kilowatt-hours (kWh), according to statistics from northeastern China's Harbin Customs. The power link cost China around US$29 million, according to the provincial capital's customs.

Around 1 billion kWh of electricity will be imported by the end of 2010, with a total value of over US$40 million, according to Heilongjiang Electric Power Company.

As the worlds two major energy consumers and producers, China and Russia are planning to build several power transmission lines across their borders. This would involve "multi billion yuan" investments, said an official familiar with the project who asked not to be named.

Currently, there is no technology barrier in building such projects, and domestic companies are cooperating with foreign power giants such as Areva SA in feasibility studies on some electricity lines, said Hu Xuehao, an expert with the China Electric Power Research Institute. Buying more electricity from Russia now is a reasonable way for China to meet its surging power demand, he said.

China may face temporary power shortages in some regions this summer due to the rapid increase in consumption, the State Grid said earlier.

Power shortages will occur in central, eastern and northern parts of the country during peak summer hours, as uncertainties still exist over demand and supply, the company said. The operator is responsible for supplying power to 26 provinces, municipalities and autonomous regions.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2010-07/29/content_11064800.htm) ([see archive](China_and_Russia_sign_power-grid_agreement.pdf))

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