

SCI China Market Update – December 2014

Dear friends,

The Holiday Season is now upon us in the U.S. - “The most wonderful time of the year!” Some 30 years ago, when I was helping my hometown, Tianjin, establish a Sister City relationship with Philadelphia, I learned that the “old” City of Brotherly Love dates back to 1682, some 300-plus years ago. China’s history is, of course, about ten times longer than that, stretching back some 3,000 years. And its Holiday Season for all that time has been the Chinese New Year “Spring Festival” – also the most wonderful time of the year.

The Chinese New Year celebration begins on eve of the New Year and ends with the Lantern Festival – the 15th day of the Chinese New Year. But, in fact, no one in China calls this 15-day period a “Holiday Season”. Nor are there any special holiday season songs as in the U.S., and there are certainly no live trees cut down for home celebrations. Typically, the Chinese decorate rooms with colorful lights and lanterns and decorate windows and doors with red paper cutouts. And they light tons of fireworks on New Year’s Eve to welcome spring and celebrate the coming crops. That is the Chinese New Year tradition.

In fact, cutting and selling pine trees in China to be used as house decoration would very likely be considered a criminal activity. This is because its 1.3 billion population needs trees desperately. Dating back to the so-called “Great Leap Forward” in the 1950’s, the land has been severely depleted for so many years, leaving yellow, contaminated soil and no trees. Of course, there are rich forests in the far South and in the West, but in the highly developed and populous East the land is nearly barren. The Chinese people remember that millions died of starvation as a result of the agricultural devastation of the Great Leap. In their minds any piece of land must be used not only for trees but to grow food to prevent such mass calamity from ever happening again. Symbolic of this need, beginning in Deng Xiaoping’s time, China designated March 12th each year as “National Tree-Planting Day”. No, there can surely be no Christmas tree industry in China; it is a luxury the country cannot afford. And even though China is likely the world’s largest producer of plastic Christmas trees, in fact it does not even use these for home celebrations. The Christmas tree really reflects a lot of the differences in culture and tradition between the U.S. and China, and a different way of thinking.

Below is some very recent China market news taken from a variety of public sources for your information:

China's manufacturing growth at eight-month low

China's manufacturing growth skidded to an eight-month low in November, an official survey showed, fuelling speculation authorities will take further steps to stimulate the world's second-largest economy.

China's official Purchasing Managers' Index (PMI) released by the National Bureau of Statistics came in at 50.3 last month, is lower than the 50.8 recorded in October and the weakest since a similar 50.3 reading in March. The index, which tracks activity in factories and workshops, is considered a key indicator of the health of China's economy. A figure above 50 signals expansion, while anything below indicates contraction.

Interest rates cut to bolster growth

China has cut benchmark interest rates for the first time since July 2012 in an effort to prop up growth as the economy continues to slow. The one-year benchmark-lending rate will be lowered by 40 basis points to 5.6 percent and the one-year benchmark deposit rate by 25 basis points to 2.75 percent. Some economists and market insiders have been looking for interest rate cuts for some time. But others were surprised by the change because the People's Bank of China, the central bank, is reluctant to use rates to boost the economy for fear of fueling a credit bubble.

The central bank also freed up deposit rates, allowing banks to pay depositors 1.2 times the benchmark level, up from 1.1 times.

ABB to support China's first large-scale shale gas project

ABB, a leading power and automation technology group, will work to support production in the Sinopec Fueling Shale Gas Project. ABB announced a deal with China Petroleum and Chemical Corporation (Sinopec) to provide automation and engineering services for Phase I of Sinopec's Shale Gas Project in Jiaoshiba Block in Fuling, Chongqing, over the next three years.

This is expected to alleviate natural gas supply shortage in the country, as well as optimize China's energy structure, promote energy conservation and cut emissions. The Fuling field, discovered in 2012, has reserves of 2.1 trillion cubic meters of shale gas, according to Sinopec.

China's energy plan reduces reliance on coal

Chinese officials announced limits on growth in energy consumption aimed at making the country less dependent on coal.

Under a development plan issued by China's Cabinet, energy consumption by 2020 must be no more than 28 percent higher than the 2013 level. For coal specifically, the increase would be limited to 16 percent.

The State Council released the plan a week after the country announced it would stop the growth of its carbon dioxide emissions by 2030 at the latest. China is the world's biggest energy user and emits more greenhouse gases than any other country. Coal, in particular, is a top contributor to greenhouse gases and meets 65 percent of the country's total energy consumption.

The country has said its carbon dioxide emissions will peak in 2030 but has yet to announce at what level. The council also announced non-fossil fuels would make up 15 percent of the country's total energy needs by 2020. The country is aiming to boost that to 20 percent a decade later.

China's nuclear power bid saluted

The Energy Development Strategy Action Plan (2014-2020), published by China's State Council recently, set the goal to reach a nuclear power generating capacity of 58 GW by 2020, from the current 19.1 GW level. It would make China the number three country in terms of nuclear power generating capacity, following the US and France. The plan also says that an additional 30 GW or more of new nuclear power generating capacity will be under construction in 2020. Fatih Birol, chief economist at the IEA, said on Monday that half of the 80 GW of nuclear power capacity now under construction in the world is located in China.

China, Russia ink energy agreements

Gas import from Russia via the western route will hit 30 billion cubic meters per year and last for three decades, according to China National Petroleum Corp (CNPC). CNPC signed a framework agreement with Gazprom on Nov 9 detailing the natural gas import arrangement.

The deal is another step forward in gas cooperation, preceded by the two oil giants inking a purchase and sales contract on gas import via the eastern route in May 2014. Meanwhile, CNPC said that gas imports from Myanmar had totaled 3 billion cubic meters by Nov. 11 via the China-Myanmar natural gas pipeline.

Bayer acquires OTC drug firm Dihon for \$586 million

Germany-based drugmaker Bayer AG said it has completed the acquisition of privately held Dihon Pharmaceutical Group Co Ltd in Kunming, capital of Yunnan province, for 3.6 billion Yuan (\$586 million), which will help it become the world's largest non-prescription medicine group. Bayer will hold

100 percent of Dihon, which specializes in over-the-counter skin products and herbal traditional Chinese medicine products for women.

China's healthcare expenditures are forecast to nearly triple to \$1 trillion by 2020, consultancy McKinsey & Co Inc. has forecast.

More Chinese consumers are turning to health supplements and OTC health treatments, which will support the health and wellness market in the country. The Boston Consulting Group has forecast that China's consumer health and wellness market will approach \$70 billion by 2020

China to Pay for India's High-Speed Rail Study

China will pay for and conduct a feasibility study in India for a high-speed rail line to connect Delhi with the southeastern city of Chennai, a spokesman for India's Ministry of Railways has said. Chinese and Indian officials, meeting in China, will this week sign an agreement for the feasibility study, the spokesman said.

Cost estimates for the proposed 1,750-kilometer line were not shared. But a separate study for a high-speed 500-kilometre line connecting Mumbai with Ahmedabad, being conducted by the Japan International Cooperation Agency, estimated that project to cost 600bn rupees (\$9.7bn, £6.2bn, €7.8bn).

China, which has built over 12,000km of high-speed track at home in less than a decade, has bagged contracts to build railway lines in Saudi Arabia and Turkey.

Yili to invest \$327 million in NZ dairy industry

Inner Mongolia Yili Industrial Group Co Ltd, one of China's largest dairy producers, said it will invest 2 billion Yuan (\$327 million) in four dairy projects in New Zealand. Yili unveiled its Oceania production base in Waimate, South Island, New Zealand, which has involved investment of 1.2 billion Yuan. The base, covering packaging, production, processing and research and development, is the largest integrated dairy production base in the world, according to Yili.

The move came as increasingly more Chinese customers prefer overseas dairy products as the reputation of local brands was damaged in the melamine-tainted baby formula scandal in 2008. The second-phase investment will be four projects, a raw milk processing plant, a UHT milk plant, a milk powder plant and a packaging plant. Also, Yili signed an agreement with Lincoln University of New Zealand to focus research on how to improve nutrition and to ensure quality of dairy products.

China Orders Microsoft to Pay \$137m in Back Taxes for Tax Evasion

Tech giant Microsoft will have to pay a big amount in fines after the company was found evading taxes in China, in the first case in the country concerning cross border tax evasion. China's Xinhua official news agency reported that China has levied about 840m Yuan (\$137m, €110m, £87m) on a US multinational in back taxes and interest, and more than 100m Yuan in additional taxes per year in the future.

In response to the news agency, Microsoft neither confirmed nor denied the report. "In 2012 the tax authorities of China and the United States agreed to a bilateral advanced pricing agreement with regards to Microsoft's operations in China," said a Microsoft spokesman in an emailed statement.

Global automakers target luxury segment in China

China is the new El Dorado for US automakers looking to develop sales of their luxury brands, which globally are lagging behind German and Japanese competitors. GM already sells more cars in China each month than it does in its home market and expects that to continue. GM launched a Chinese-produced luxury sedan, the XTS, last year and is steadily adding more vehicles to its Cadillac range.

For more information about today's China market and opportunities please visit our website at www.s-c-i.com or call me at the number below, or Dr. Tim Weckesser at 610-828-8060.

Best regards

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