In Case You Missed It: CSOP's Weekly China Wrap Up

Annual "Two Sessions" begin, leaders discuss national policy priorities

More than 5,000 political, economic and social leaders trekked to Beijing last Friday for the official start of China's "Two Sessions," the annual parallel meetings of China's National People's Congress (NPC) and the Chinese People's Political Consultative Conference (CPPCC). The gatherings offer a forum for leaders to discuss priorities, propose policy ideas, and pass legislation on critical issues. This year's session will be particularly scrutinized, as global onlookers seek clarity about China's response to slowing economic growth, looming November leadership reshuffle, and potential threats from a Trump administration.

Of the two sessions, the NPC is the more important. The Congress is China's top legislative body; its standing committee is responsible for national lawmaking. Unlike their NPC counterparts, members of CPPCC do not have voting rights. However, membership does afford a rare opportunity to put forth divergent voices and is heavily pursued as a status symbol. Moreover, the "Two Sessions" offer one of the only chances for provincial and lower-level officials to meet and impress their more senior counterparts in the hope of being promoted in the future.

Upset at missile defense system, China launches multi-pronged assault on South Korea economy

In response to ongoing concern over a new anti-missile defense system, China has reportedly ordered domestic groups to halt travel to South Korea as well as boycott a controversial Korean conglomerate's China operations. At issue is South Korea's decision to cooperate with the United States, who want South Korea to install the Lockheed-Martin built system to help intercept North Korean missiles. Beijing objects to the installation, claiming that the system's radar can penetrate its territory and thus impede its sovereignty.

To express the country's displeasure, China's State Tourism Bureau allegedly cautioned Chinese travelers, travel agents, and cruise ships against visiting South Korea. The move is a blow to the South Korean economy, which is heavily reliant on China's tourists. Analysts predict mainland visitors could fall by 70%. Already feeling the pressure, impacted companies are urging Seoul to normalize relations with Beijing.

Lotte, the Korean conglomerate supplying land for the missile defense system, is especially vulnerable. The retailer saw a pronounced drop in visitors and products removed from shelves as Chinese consumers and suppliers boycotted the brand.

Anti-corruption efforts target insurance firms and underground banks

In preparation for a major leadership reshuffle, Communist Party officials are expanding efforts to tackle financial crimes, focusing particularly on insurance companies and underground banks.

China's securities watchdog levied a ten-year industry ban on Foresea Life's chairman after accusing the company of falsifying documents and improperly using insurance policies proceeds to purchase listed companies. Foresea had been on a buying spree the past year, gobbling up big names such as property developer Vanke (000002), glass manufacturer CSG (000012), and home appliance manufacturer Midea

(000333). Evergrande Life was also barred from investing in equities for one year due to improper short-term, speculative trades.

Onlookers generally support the punishments. They fear the consequences of speculating with insurance premiums and other unregulated funding sources, wary that buyers lack relevant experience in the targeted industries and will destroy corporations for short-term profit. However, critics charge that authorities are cherry-picking scapegoats, as some companies guilty of similar practices have not been reprimanded.

In a separate example of regulatory tightening, China's Ministry of Public Security announced the breakup of 380 underground banks involving over RMB 900 billion (USD 130 billion) in assets.[1] Cloaked as internet finance and online payment platforms, the illegal banking operations helped investors transfer money outside of China. As payment for their services, the platforms profit from the spread between the official exchange rate and their own exchange rate-- usually several hundred basis points.

Due to the attractive margins, some legitimate businessmen have been unable to resist the temptation to enter this business, especially in the background of slower economic growth. Authorities arrested 800 money laundering suspects in 2016 alone in attempt to discourage copycat practices. The central government indicates it will continue the crackdown, asserting that the mass of cross-border transactions threatens China's financial system and must be monitored more closely.

Xi promotes creation of financial super-regulator

China's President Xi told the country's top financial regulators to establish a more effective system for financial policymaking coordination. The message was sent ahead of the annual "Two Sessions" meetings and mirrored warnings delivered during last December's Central Economic Work Conference.

Xi's admonitions indicate the urgency with which top leaders hope to tackle economic and financial headwinds potentially endangering the country's social stability. Onlookers expect regulations to change in accordance with international standards, with many predicting creation of a super-regulatory agency by combining the CBRC, CIRC and CSRC. [2]

China launches new tax breaks to develop interior provinces

China is employing tax breaks to promote economic development in the country's poorest interior provinces-- Tibet and Xijiang. The provinces have been increasingly plagued by ethnic upheaval in recent years as the quality of life has diminished for the largely agrarian populations.

To remedy the problem, authorities have introduced preferential tax treatment to encourage more investment into the regions. Under the new policies, companies that register in Tibet will enjoy a corporate tax rate of 15 percent, far below the standard national rate of 25 percent. The rate can drop as low as 9 percent for companies who take advantage of all available inducements.

Similarly, a "National Special Economic Development Zone" has been established in Khorgos, Xinjiang Province to provide companies income tax waivers for five years. Although optimistic onlookers expect Tibet and Xinjiang to benefit from the special taxation regimes, critics counter that registered firms are not required to hire local residents, potentially providing wealthy business owners a loophole for tax evasion rather than an effective vehicle for poverty eradication.

Notes:

1. RMB: Renminbi, the national currency of China
   USD: US Dollar, the national currency of the United States
2. CBRC: China Banking Regulatory Commission
   CIRC: China Insurance Regulatory Commission
   CSRC: China Securities Regulatory Commission