Asia Perspective Economic Update Report

Issue 3, October 2016

In This Report:

- Recovering Manufacturing and Strong Retail Sales
- Increasing Prices are Saving Manufacturers
- New Free Trade Zones
- An Educational Goldmine

Recovering Manufacturing and Strong Retail Sales

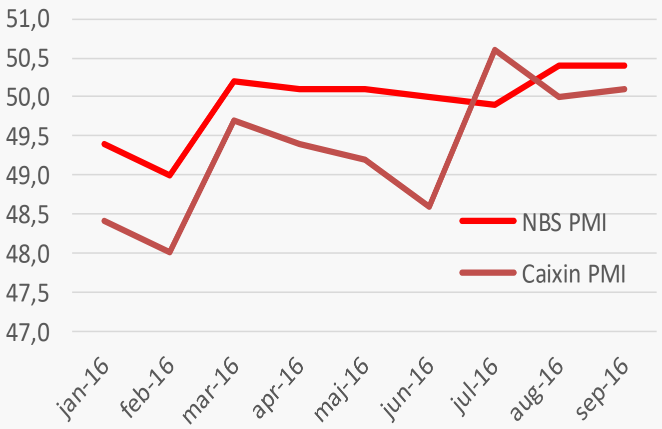
During the last quarter, the global economy has continued on a path of moderate expansion, sporting a GDP growth of around 3% - an important sign of economic recovery. Data from China has offered similar ground for optimism. According to estimates, the GDP growth in Q3 stayed at 6.7%, just as in the previous quarters. The government is doing its best to fuel economic growth as real estate, infrastructure and manufacturing keep slowing down the growth. In September alone, the government announced its intent to spend over one trillion Yuan ($149.25 billion) on public investments and projects, according to Xinhua news agency.

Consumption growth, China´s recently strongest indicator, continues to impress. Retail sales accelerated to a 10,6% growth year-on-year in August, thus beating the 10,2% in July.

The Purchasing Managers Index (PMI) by the National Bureau of Statistics (NBS), surveying mostly large and state-owned enterprises, has recovered since its marginal contraction at 49.9 in July. Both August and September sported PMI levels of 50.4, thus indicating expansions in the manufacturing sector. The Caixin PMI, surveying smaller-scale private firms, accelerated to 50.6 in July but moderated to 50.0 in August, and closed at 50.1 in September. This indicates a more or less stagnant market in this segment.

Together this illustrates that the economic growth is led by large enterprises and to a large degree by state stimulus. Some experts are also warning that optimistic economic indicators might be inflated by the overheated property market. As authorities are trying to cool the property market down with new policies and tighter control, the rebound might be short-lived.

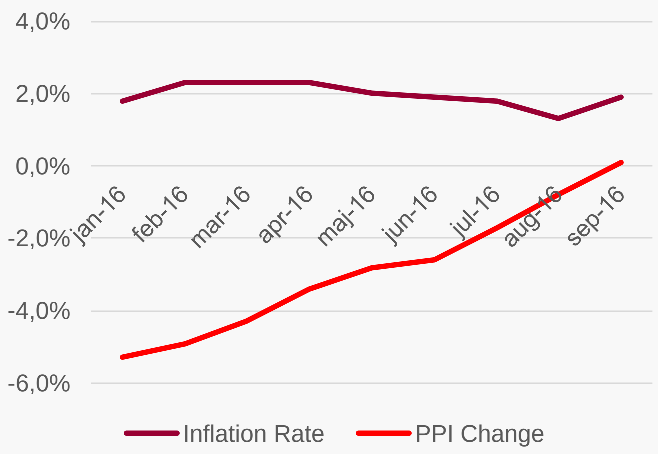
The main concern for all economists now is, however, a continuously low level of private investments. Fixed Assets Investment growth remained at 8.1% year-on-year in August, while private investment growth have not recovered from July´s historically low level of 2.1%. Especially smaller private companies, remain reluctant to borrow and increase their investments.



Increasing Prices are Saving Manufacturers

China has finally overcome its long streak of industrial deflation. The Producer Price Index (PPI), focusing on prices of the manufacturing output, saw its first increase since 2012 as September data reported 0,1% growth. The monthly price decrease has been steadily declining during the entire year until finally ending the multi-year negative run. This puts an end to the Industrial deflation that has been plaguing the Chinese manufacturing sector for years, and offers manufacturers a well needed relief.

The improvement is an effect of various positive trends and efforts. Among these is government´s effort to cut excess industrial capacity, rising global commodity prices, a recovering property market and large infrastructural investments.



The rising prices will increase revenue and profits of many Chinese companies. On average, large companies in the industrial sector increased their profits by 19,5% year-on-year in August, thus marking the largest improvement in two years.

Consumer Inflation increased for the first time in five months as September sported a consumer inflation of 1,9%. This was a significant increase compared to the year-on-year rate of just 1.3% in August. The price increase has been driven by high energy prices and food, especially vegetables and fruits.

New Free Trade Zones

At the end of August, the central government approved the opening of seven new free trade zones (FTZs) in China, bringing the total number to 11. The new FTZs are set to open in Chongqing, Zhejiang, Henan, Hubei, Sichuan, Shaanxi, and Liaoning. The opening of FTZs is part of an effort to combat the slowing economic growth, and the program was started with a pilot zone opening in Shanghai in 2013. Additional free trade zones have since then be established in Tianjin, Fujian and Guangdong.

Whereas the first zones were established on the coast, five out of the seven new ones are located inland. This reflects the “go west” strategy, improving the competitiveness of inland regions. As the Middle Kingdom is attempting to diversify its economy, the FTZs are seen as a way to open up the market to new industries and to attract foreign investments.

Unlike the first zone in Shanghai, the goal is not to experiment and test concepts for nationwide reform, but rather to support certain industries and the development in certain regions.

According to the Chinese Minister of Commerce Gao Hucheng, the Liaoning Province in North-eastern China will focus on market-oriented reforms to transform its old industrial base. Coastal Zhejiang is dedicated to further develop as a centre of trade with commodities, while central China's Henan will focus on transportation and logistics. Hubei on the other hand, is set to develop high-technology industries to facilitate the development of the Yangtze River Delta.

The FTZs in Chongqing, Sichuan and Shaanxi, are less focused of specific industries, and are set to promote international economic cooperation and drive the overall development in the region.

There is not yet any time plan for the establishment for the new zones, but they are expected to be opened during the next year.

An Educational Goldmine

Despite setting new records in the number graduates every year, China is continuously facing shortages in skilled labour. This is one of the main problems facing the country as it is trying to move its production up the value chain. The problem is however not in the sheer number of graduates. While employers find it increasingly hard to find suitable white- and blue-collar workers, unemployment remains fairly high among new graduates. This indicates that the Chinese institutions of higher education are not as aligned to the market as they should be. In order to fight these challenges, China is slowly opening the educational sector to foreign investments. This, however, remains a highly controversial due to the close association between education and the fostering of the Chinese ideology.

While primary and middle schools, as well as special training institutions such as the military and police, remain closed to foreign investments, pre-school, high schools, and tertiary educational institutions, have now opened up. Foreign majority ownership is allowed in these sectors, but there are still requirements that leading positions are to be held by Chinese nationals.

The Chinese educational sector is booming, perhaps more than any other industry in China. In 2015, the market totalled 1.6 trillion RMB, and it is expected to almost double to 3 trillion by 2020. Pre-school education, online schooling and vocational training are the major growth areas. In 2015, almost 20% of all investments in the education industry went to vocational education, including business oriented language training, finance & accounting as well as IT. In order to align the education with market demand, the Ministry of Education encouraged successful domestic companies to establish vocational schools. These schools will not only make the education more specialized to enterprises' demands but also hopefully guarantee employment upon graduation.

To make the educational industry more compelling for both domestic and foreign investments, the Chinese government changed the Education law and Higher Education Law in 2016, thus allowing private educational institutions to be either for-profit or non-profit. The latter are to be receiving government funding. In 2020, over 80% of all vocational schools are estimated to be non-government operated and the number of students enrolled in these is expected to increase from the 16.5 million today to over 38.5 million students in 2020.

The Chinese government is intensifying its support for vocational education and will continue to promote policies that encourage vocational schools to work with overseas educational institutions. Among these efforts is the development plan *Innovation and Development of Higher Vocational Education (2015-2018)*. Altogether, the development is creating new investment opportunities for foreign investors.

The development that is driving increased foreign investments into the Chinese education industry is occurring on three fronts: economical, political, and cultural. Firstly, the rapid economic development has increased Chinese parents' willingness and ability pay for private, foreign education. Secondly, the public focus on transforming China into an innovation superpower by the centenary of the establishment of the Peoples Republic in 2049, brings reforms into the previously government controlled education. This has so far meant that foreign ownership and teaching methods have been being allowed into schools in China. Thirdly, The Chinese society is transforming as the middle class grows dominant and bring with it a pre-love for all things western, especially education.

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What differentiates us from our competitors is the knowledge and expertise we have gained after several years in the Asian market. We have experience from a variety of industries and clients including leading international companies from Europe, the US and Asia.

With a highly collaborative team of problem solvers and a passion for excellence we will add value to your business. We work closely with our clients to create and deliver insight, advantage and real impact.

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