Asia Perspective Economic Update Report

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Strengthened corporate prospects amidst global concerns

The World Bank recently revised its global economic forecast down to 2.4 % for 2016. The modification is due to slower growth in advanced economies, increasing doubts regarding global free trade, low commodity prices and diminishing capital flows.

In China, however, the economy continued to show stable growth figures at 6,8 % in Q4, thus reaching the Chinese government's economic growth target of at least 6,5 % GDP in 2016.

In addition, Chinese companies displayed a rise in revenue, higher capital investments and increased hiring during Q4 compared to the previous quarter, according to a survey by China Beige Book. This resulted in increased corporate profit margins as prices rose and input costs fell. The industrial profits rose to 14,5 % in November, up from October's figure of 9,8 %.

Even though the GDP growth is in line with the "new normal" policy, it has been largely fuelled by stimulus funds by the Chinese government. This is illustrated by an 20,5 % increase in government investments in the first 10 months of 2016. In addition, increasing capital outflows by 1,7 % in November due to a weakened Yuan against the American Dollar, pose yet another concern.

Nevertheless, consumption on the Chinese market continued to display bright figures as retail sales grew to 10,3 % in November compared to 10 % in October.

The consumer-price index, oftentimes used as a measurement of inflation, reached 2,2 % year on year in November. The producer-price index doubled to 2,4 % year on year, between October and November.

However, a deteriorating cash flow posed a potential concern during Q4. In addition, the Chinese government's policy to restrain the country's fast-growing housing prices, might cause a larger slowdown than intended.

The Purchasing Managers Index (PMI) compiled by the Chinese National Bureau of Statistics, focusing on large state-owned factories, closed at 51,4 % in December, down from 51,7 % in November. The PMI figure at 51,7 % in November is the highest number recorded since April, 2012, illustrating a strong recovery in the manufacturing sector. The Caixin China Manufacturing PMI, focusing on mid-size companies, climbed to 51,9 % in December.

Together this illustrates a continuous growth in China's manufacturing sector and a continued recovery of China's economy, largely supported by the government's stimulus plan.

Looking ahead, 2017 will be an important period in China as the Communist Party is expected to appoint president Xi Jinping for a second five-year term. This is believed to be followed by extensive reallocations of the top leadership posts in the party.

Trump and China

Donald Trump's election for the next US president on November 8th 2016, has spurred an increased anxiety about growing protectionism and rising trade barriers influencing global trade.

The president elect Donald Trump's previous statements regarding China during the election campaign, have caused concerns about the future relationship between the world's two economical superpowers as well as the validity of trade agreements worldwide.

For instance, Donald Trump has re-confirmed his intention to withdraw from the Trans-Pacific Partnership (TPP) when taking office in January, 2017. The TPP was thought of as a new deal for promoting free trade and potentially as a new free trade market similar to the European Union.

The member states of the TPP include the US, Japan, Malaysia, Singapore, Brunei, Vietnam, Australia, New Zealand, Canada, Mexico, Chile and Peru. Notably, the TPP would not include China and was originally initiated to counter-balance China's growing influence in the Asia-Pacific region.

A US withdrawal from the TPP, is potentially good news for Beijing as this opens up an opportunity for China to take on a greater role and trade leadership in the Asia-Pacific region.

In addition, combined with recent Chinese initiatives such as the development, trade and infrastructure framework "One Belt, One Road" along with newly founded institutions such as the Asian Infrastructure Investment Bank headquartered in Beijing. This development has great potential to further expand China's investment, trade and influence in the region.

Indeed, the recent developments and statements by Donald Trump have already harmed the US reputation in the Asia-Pacific region. This opens up for China to build its image as a more reliable and long-term partner in the region compared to the US' apparent short-term commitments.

China-US FDI Underestimated

According to a recently published study by the Rhodium-Group, the actual amount of Foreign Direct Investment (FDI) flows between China and the United States are two to four times higher than official statistics suggest. The benefits of FDI might thus have been largely ignored and underestimated due to the inaccurate numbers presented, not least by the reborn protectionism in the US. This conclusions comes from the Rhodium Group that has studied every business investment of over 1 million US dollars or more between the two countries during the past quarter century.

US businesses initially invested in China due to lower cost considerations. At present, however, investments by US companies tend to focus more on the Chinese consumer market. Chinese companies, on the other hand, have during the past five years accelerated investments in the US, mostly by the means of acquiring American businesses.

The chart below illustrates the investments by China in the US, and vice versa. As shown by the chart, Chinese investments in the US has increased rapidly during recent years while the US investments in China have remained at a steady pace.

Source: The Wall Street Journal

Combating Pollution

China is currently the world's largest renewable energy investor and already a green energy superpower. The Chinese government has set out a number of ambitious climate goals to deal with the country's pollution caused mainly from its various coal power plants.

Amongst the goals set out by the Chinese government are; peaking carbon emissions by 2030 or sooner, lowering total carbon intensity of the country's GDP, as well as increasing low-carbon energy sources to around 20 % of total energy production.

The main reasons behind China's investments in clean energy are addressing the country's pollution problems as well as promoting technology innovation. In addition, the investments in renewable energy have been claimed to be a means of tackling poverty in the country's remote areas with limited access to electricity. With more than 70 million people in China still living below the poverty line, president Xi Jinping has made installation of solar energy in lesser developed areas a priority in a recent energy initiative.

The project involves installation of rooftop and micro solar energy systems in poor villages. The idea is to allow people in poor villages to generate electricity for their own use and subsequently sell the potential surplus to the power grid. Around 200 million households are expected to gain help from the project with a generated 3000 Yuan extra income each year.

However, questions remain regarding both the implementation and financing of the project.

Furthermore, whether the targeted households will benefit from the project or not, depends on the quality of the rooftop- and micro-grid systems as well as the potential to sell the surplus electricity.

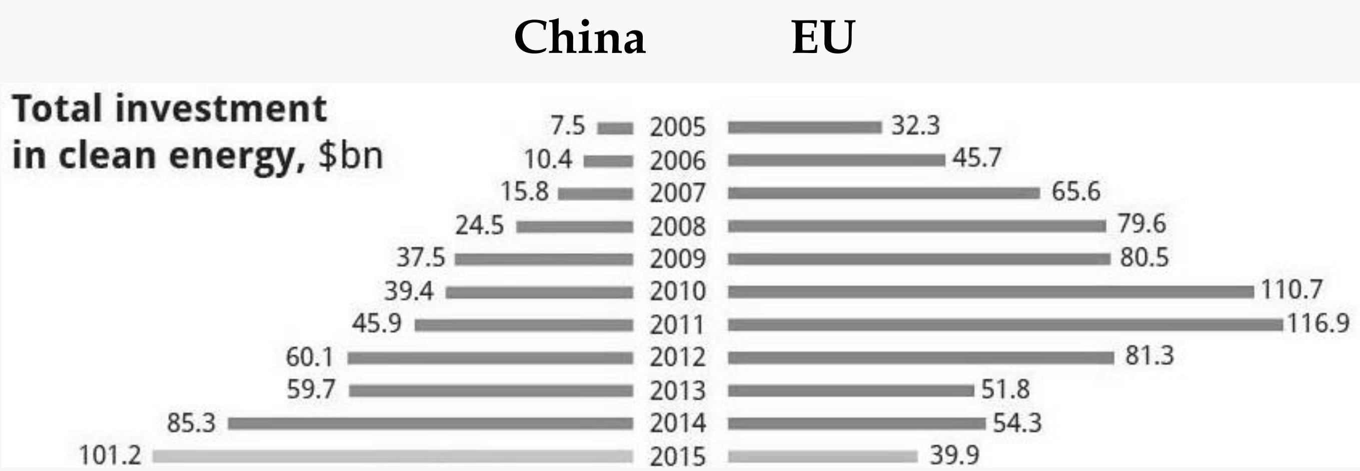
Similar challenges have already faced the existing renewable energy sources in China where the integration and delivery of the clean energy to the final consumer has not been efficient, resulting in renewable power being wasted. As a consequence of the inefficiency, the initial targets for solar and wind power set by 2020 by the Chinese government, was recently lowered.

China's energy transition from fossil fuels to renewable energy, seems to have spotted some dark clouds on the horizon. Nevertheless, enormous opportunities still persist regarding renewable energy investments in China, and the clean energy sector is expected to continue expanding.

Solar energy capacity is due to double from 2015 to 2020 and wind power will similarly see an increase in capacity by 50 % during the same period.

The proclaimed "war against pollution" will continue to receive large resources, with total investments expected to reach 2,5 trillion Yuan per year by 2020. The investments in clean energy will thus make up 2,7 % of China's total GDP compared to less than 1 % in 2000, illustrating the fast development in this sector.

In summary, if China can overcome the current obstacles regarding efficiency and distribution of its clean energy to the final consumers, it has a vast potential of becoming the global leader in the transition to a new, low-carbon energy future.



Source: BNEF, Xinhuanet

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About Asia Perspective

Asia Perspective is an Independent Management Consultancy with global presence and local knowledge. We assist our clients with business advisory regarding Analysis, Strategy and Implementation. Our mission is to turn our clients' Asia business vision into reality and add significant value to your business.

We offer specialist services covering Supply Chain Management, Purchasing, Market Entry, and Financial Advisory. This includes market entry research and strategy sourcing and pricing strategy, M&A advisory, risk management, operational improvements etc.

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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