

Shanghai Flash

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The Yangtze River Delta (YRD): New Economic Situation and Opportunities for Swiss Investments

(with the latest figures of Swiss presence in the region)

- *Despite of government target to slow down the economy, the economic growth rate of the Shanghai led YRD recorded the fastest growth in the past three years, expanding over 13% for the first three quarters of 2007. The growth was mainly fuelled by strong exports and the picking-up of consumer spending.*
- *The YRD region remains an economic powerhouse and solid foreign investment destination. Regional integration has been brought to strategic level of the YRD development, which will lead to integrated transportation infrastructure, unified market access regulations and administrative services. New policies are expected to be released soon.*
- *The development pattern of Shanghai is changing towards service-orientation, resulting in tertiary industry accounting for over half of the city's GDP.*
- *Imports from Switzerland to the YRD region have significantly grown by 35.74% for the first half of 2007, while exports from the region increased 18.51%, which brought a 54.2% growth of trade surplus in favour of Switzerland during the period.*

1. Current Economic situation of the YRD

(1) General situation: remains economic powerhouse

As the locomotive of China's economy, the Shanghai led Yangtze River Delta¹ maintains its leadership position, with growth rates still above national level. For the first three quarters of this year, the region reported a **GDP of RMB 3'333.45 billion** with an increase of **15.2%**, **3.7% higher than the national growth rate**. The growth was mainly fuelled by strong exports and climbing private consumption. With less than 2% of the country's land area and 6.3% population, the aggregate **GDP of the region contributed to 20.1% of China's total**. The GDP contribution ratio of the three industries in this region was **2.8%: 55.1%: 42.1%**, among which the ratio of secondary industry was 4.8% higher than the national average and tertiary industry was 3.3% higher.

The region remains also a **solid foreign investment destination** and still takes the lead in China's foreign trade. For the same period, the region reported **USD 565.5 billion of foreign trade²** in value, accounting for **36% of China's total**, with **29.8% increase**. The **trade surplus** continued to expand with a 47.9% increase, amounting to **USD 87.50 billion**, and accounting for **47.1% of China's total trade surplus**. In terms of foreign direct investment (FDI), **37.4%** of the foreign

¹ The Yangtze River Delta region here refers to Shanghai and 15 surrounding cities in Zhejiang and Jiangsu Provinces. These are 8 more developed cities in Jiangsu Province and 7 in Zhejiang Province.

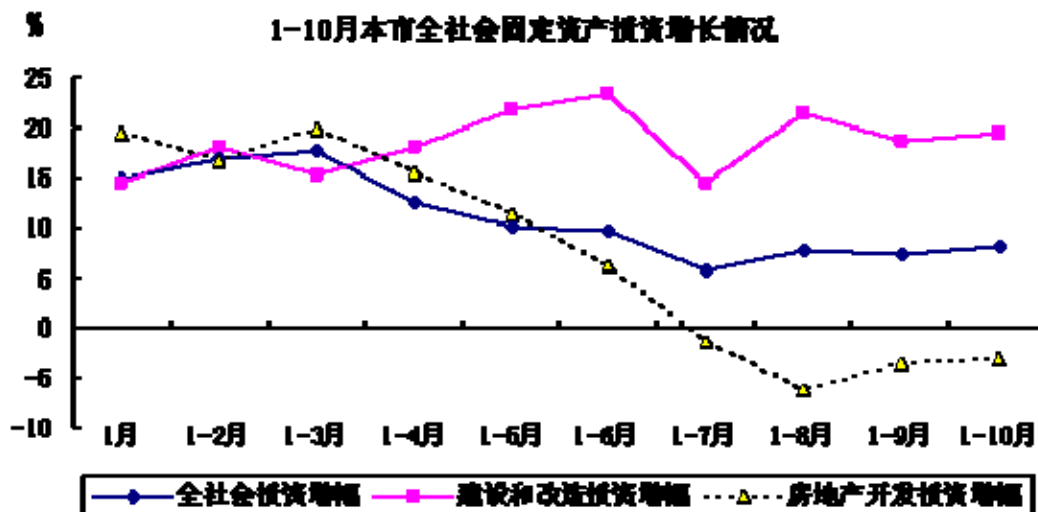
² USD326.5 billion exports and USD239.0 billion imports.

invested projects were located here, actually utilising USD 23.1 billion capital, accounting for **72.4%** of the country's total utilised foreign investment.

(2) Shanghai: Dragonhead of the Yangtze River Delta

Shanghai is defined as the nucleus of the regional development. Its economy has expanded **13.4%** during the first three quarters of 2007, recording the fastest growth in three years. Different from other cities in the region, Shanghai's growth has changed from an export-and-investment-driven pattern to a more service-oriented one, reporting a relatively balanced trade. Hit by the tightening policy and the scandal of the former Party Secretary Chen Liangyu³, the **growth in fixed assets investment continued to slow down** and increased only at a one-digit rate of **7.4%** for the first time since 1990s. The contribution of fixed assets investment to GDP has shrunken to 38%, while the nationwide fixed assets investment still accounted for over half of China's total GDP.

The graph below shows the growth of Shanghai's fixed assets investment during the first 10 months of this year. The blue line presents the growth of completed investment in fixed assets, while red line stands for that of construction and reconstruction of infrastructure and the dotted line exhibits the growth of the real estate investment. As a result of the government efforts to curb the overheated real estate sector, its growth experienced a sharp decline this year. Influenced by stricter regulations, **foreign investment in real estate also decreased 19.5% for the first three quarters.**



Graph 1: Growth of fixed assets investment in Shanghai Jan.-Oct. 2007

Source: Shanghai Statistics Bureau

On the other hand, **foreign investors still show strong confidence** on the prospects of the city. There were **3'042 new FDI projects** approved during the period from January to September, with an increase of 3.6%, which brought in contractual capital of **USD 10.56 billion**. Among these FDI projects, 636 were from the secondary industry, while 2'402 were investments in the tertiary sector.

Asian countries still remain the **most important FDI nations**, accounting for 47.6% of the total contractual capital in the first three quarters of 2007. It is noticeable that overseas Chinese were the main source of investment. **Hong Kong** topped the list with a 30.7% share. Investment from the **Virgin Islands** and the **Cayman Islands** ranked number 2 and 4 with shares of 18.1% and 8.1% respectively, while **Japan and the U.S.** have taken 8.1% and 6.8% share, ranking number 3 and 5 respectively. Contractual FDI from Europe decreased by 26% during the same period, but that from France increased 1.3 times, reaching USD 190 million.

³ Chen was dismissed as Shanghai Party secretary in September, 2006, in an anti-corruption campaign that found the city's 10-billion-yuan (US\$1.27 billion) corporate annuities had been managed via irregular loans without proper collateral and placed in risky investments

2. Swiss Trade and Investment in the YRD

The Shanghai led Yangtze River Delta plays an important role in the Sino-Swiss bilateral economic relation: for the first half of 2007, nearly **40%** of the Sino-Swiss bilateral trade, in terms of both imports and exports, is conducted through the YRD. **Swiss exports** to the region continued to grow with a **total volume of USD 1'106.57 million and a 35.7% increase** for the first half of 2007. Shanghai and Zhejiang, which are richer in the region measured by per capita GDP, saw a sharp increase in imports from Switzerland with 28.5% and 32.1% growths. In the meantime, the YRD exported to Switzerland a total volume of USD 500.78 million which represents an increase of 18.5%, resulting a **trade surplus of USD 605.79 million** in favour of Switzerland. The surplus was 54.2% higher than the same period of last year and contributed to a significant **two third of the total Sino-Swiss trade plus**.

The major imports of goods from the region were watches and components, machinery, chemicals and pharmaceuticals, as well as apparatus and electronics. **Exports to Switzerland** were dominated by machinery, garments and accessories, as well as textiles and shoes.

At present, there are **278** Swiss invested companies (among which 240 are wholly owned) and **138** chief representative offices present in **Shanghai and nearly 500** Swiss companies in the region, with a total amount of direct investment of **USD 2'538.91 million**. Switzerland is presented in this region not only by well-known multinational companies such as ABB, Roche, Nestlé, and Novartis, but also by small and medium sized enterprises, many of which are operating quite well and expanding quickly. These companies are mainly operating in the fields of chemicals, pharmaceuticals, machinery and machine tools, food and processing, precision instruments, watches and jewellery.

For the first 6 months of 2007, **32** new Swiss invested projects have chosen to locate in the region, accounting for **64%** of the total Swiss invested projects in China.

3. New outlook: Shanghai and YRD

In Shanghai's 11th Five Year Plan, the overall goal for the city is to lay a foundation for the city to become an international economic, financial, trade, and shipping center by 2020.

(1) A shift to service sector and headquarter economy

In an effort to change the investment-dependent growth pattern, Shanghai has been promoting the development of the service sector, which accounted for **51.9%** of the city's GDP for the first three quarters of 2007. For the first time since 2001, the tertiary industry grew faster than the secondary industry with a **14.1%** gain.

The promotion of foreign investment in the service sector is continuing in Shanghai. Aiming to build up China's "**headquarter capital**", Shanghai had attracted 178 regional headquarters of multinational corporations, 159 investment companies, 215 foreign R&D centres by the end of this September. During the first three quarters, there have been 24 newly registered foreign regional headquarters, 9 investment companies and 19 R&D centres in Shanghai,

It is also notable that due to the rising business cost, shrinking land availability and curbs on low-end manufacturing, foreign investment of production facilities is moving outside further to Jiangsu and Zhejiang provinces. However investment return ratio remained high in Shanghai. According to the statistics of Shanghai Foreign Economic Relations and Trade Commission, for the first three quarters of 2007, foreign invested companies in Shanghai reported **profits at over RMB 86.21 billion**, which is a **45% increase** compared with the same period of last year. Foreign investors remain positive and confident about the development of the city, and the supplementary investment accounted for 57.1% of the contractual FDI for the same period.

(2) International Shipping Centre: Yangshan Deepwater Port

As the key drive to the headway towards an international shipping centre, the first and second phase of Yangshan Deepwater Port have been completed and put in use. Currently the Port of Shanghai ranks No. 2 in the world, followed by Hong Kong and only passed by Singapore in terms of container through-put. In the first half of 2007, the general cargo output of Shanghai port arrived at 278 million ton, including 120 millions of foreign trade products. Container throughput reached 13.52 million TEU, up by 24.2%.

The Yangshan Port Development project is divided into four phases, which will be completed by 2012 and includes a 52-berth container terminal, located on a cluster of partially inhabited islands in Hangzhou Bay, south of Shanghai. In addition, the project includes a 32.5 km bridge that connects the islands to the closest on-shore point and a shore-based terminal to accommodate subsidiary facilities that cannot fit on the small islands.

An important characteristic feature of the Yangshan Deepwater Port is that it is China's first free trade port. The Yangshan Free Trade Port Area is a special functional zone under unified supervision by the China Customs, composed of a free trade zone, an export-oriented processing zone, and a bonded logistics zone. It is expected to offer unprecedented convenience to shipping and logistics businesses.

(3) Transportation Development

Shanghai has a combination-style international airport hub with Pudong international airport as the core and Hongqiao airport as the supplement. Pudong international airport is planned to have an annual capacity of 80 million passengers and 5 million tons of airfreight when the planned three terminals, two satellite halls and five runways are realised.

In order to transit the expected World Expo 2010 Shanghai 70 million visitors flow, Shanghai will transform Hongqiao Airport into a transport hub which integrates aviation and multiple modes of transport such as Maglev, high speed railway, regular railway, rail transit, bus and taxi.

Shanghai is also one of the four national railway hubs. The high-speed train between Shanghai and Beijing has been approved by the central government. The construction will start in January 2008 and complete in 2010. The speed of trains will reach 350 km/hour, cutting travel time between Beijing and Shanghai from the current 10 hours to less than five. The rail network, together with the expressway system will integrate the transportation within the YRD region and enhance ties with inland provinces.

(4) Changes in political personnel

China's Communist Party (CPC) concluded its 17th National Congress in October 2007. The Party Congress, held once every 5 years, is the nation's most significant political gathering and usually decides and strengthens economic development model and brings along important changes in personnel. The 17th Party Congress further stressed President Hu Jintao's "Scientific Development" and "Harmonious Society" concepts and announced the 9-member group of the Politburo Standing Committee (PSC), China's top decision-making body. Among the four new members of the PSC, Mr. Xi Jinping, former Party Secretary of Shanghai, is widely expected to inherit Mr. Hu's position as the fifth generation leader, although this is not officially announced.

As the successor to Mr. Xi, Mr. Yu Zhengsheng, the former Party Secretary of Hubei Province, has been appointed as the Party Secretary of Shanghai. Yu, 62 years old, is also elected as the member of the CPC Central Committee. Before Party chief of Hubei Province, Yu had been Minister of Construction and once Mayor of Qingdao, a coastal city in Shandong Province.

Mr. Xi Jinping's seven months in Shanghai has been mainly for the purpose of shaking off the influence of the corruption scandal of his predecessor Chen Liangyu and the overall strengthening of the Party. Mr. Yu, for his last term in his political career before retirement, is expected to be in line with the central government and continue to pursue the economic development goals of President Hu Jintao.

(5) Regional Integration

Despite much discussion of regional integration, the economies of the cities in the region were not very well-integrated. Local protectionism remained and competition to attract R&D and high-valued FDI increased in recent years.

At a recent symposium attended by the top leaders of the region⁴, the integration and co-operation of the YRD was first time brought to the development strategy level and a long-anticipated regional-development outline is expected to be soon released.

The symposium ensured Shanghai's core position of the region and YRD region will remain confirmed the economic hub of China. The concept of YRD could be expanded from 16 major cities to include the entire region to bring about smooth integration among Shanghai and the neighbouring Jiangsu and Zhejiang provinces.

While sustained coordinative mechanisms and more policies are in the pipeline, more integrated transportation infrastructure as well as unified market administration and access regulations have been already announced. The Administration of Industry and Commerce⁵ (AIC) in Shanghai and its two neighbours signed a joint memorandum of understanding on unifying market access for businesses in the region. Foreign investors registered in one city of the region will be able to do business in other cities of the region without administrative barriers.

The region also declared to share the 2010 Shanghai World Expo opportunities and expanding the Expo's effects.

4. Opportunities and challenges for Swiss companies

(1) New foreign investment guidance

China's National Development and Reform Commission (NDRC) has issued new guidelines, which have taken effect on 1st December 2007, specifying the industries in which foreign investment is encouraged, restricted or forbidden.

In an effort to upgrade China's technology and service economies, foreign investment is encouraged to shift from traditional manufacturing and export-based industries to hi-tech and advanced equipment manufacturing, services and logistics, as well as recycling and renewable energy sector.

The announcement listed also sectors that are restricted for foreign investors, including banking, financial and financial leasing companies, trust and investment companies, and monetary brokerage companies. Specifically, the guidelines set a maximum limit on foreign investors' share holdings in local securities institutions: below 33% for securities companies and below 50% for mutual fund

⁴ On 1st December 2007, the Party Secretary of Shanghai, Jiangsu and Zhejiang Province, together with the Mayor of Shanghai and Governors of Jiangsu and Zhejiang Provinces have met at the International Symposium on Regional Development of the Yangtze River Delta in Shanghai to discuss the future development of the region.

⁵ AIC is a unique organisation which doesn't have similar counterparts in other countries. It can be compared as the police for enterprises. The sanctions adopted by AIC over companies that behave against the law can be suspension of production, confiscation of products, freezing of bank account, revoke of business licence.

management companies. Compared with the old version, the limits are loosened, while futures companies, which were forbidden before, are now listed as restricted sector.

(2) Rising consumerism and more quality-oriented in YRD

Decades of bristling economic growth in the region has fostered an emerging middle-class and more sophisticated consumers groups, whose life style and consumption behaviours are influenced by western countries. On the other hand, the first generation babies after China's single-child policy in 1978, who have been the "little emperors" in the family, have grown up and became the major employees in urban cities. Their solipsistic tendencies have been further encouraged by escalating spending power, resulting in rising consumerism among the young people.

This group of urban wealthier consumers has fuelled tendency to pursue "quality satisfaction". Their consumption behaviour is very much influenced by leading brands and luxury items, which generates great opportunities for Swiss brands and goods. As *Swissness* is perceived as of high quality and high price in China, it is easier to build up brand awareness for Swiss products in the market.

However, China is not a unified homogeneous market. Even in the YRD region, spending power and consumption behaviours are different between cities. Shanghai is China's largest market for a great range of goods and has high discretionary purchase. Jiangsu's consumer economy is relatively small compared to Zhejiang and Shanghai. Its development is now more focused on investment than consumption and looking towards domestic markets for its products. Due to its immigration tradition and strong private economy, more consumers from Zhejiang are luxury brands followers.

Most Swiss companies focus on top end and niche market, where Chinese competition is less. Forging and pirating are however the common challenges they have to face in the market. Although the situation of IPR protection has been improved in recent years, lack of implementation of relevant legislation, weak enforcement and local protectionism remain in many regions. While court is one of the places to seek solution for such cases, the Administration of Industry and Commerce could be another powerful administrative institution.

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Table. 1

Current Economic Indicators* of the Swiss Consular Area

Year		2006		2007.1-6	
		Volume	Growth Rate (%)	Volume	Growth Rate (%)
GDP (billion RMB)	China	20'940.70	10.7	10'676.8	11.5
	Shanghai	1'029.70	12.0	556.19	13.0
	Jiangsu	2'154.84	14.9	1'175.2	15.0
	Zhejiang	1'564.90	13.6	834.44	14.7
	Anhui	614.19	12.9	340.46	13.2
	Consular Area	5'363.63		2'906.29	
Total Retail Sales of Consumer Goods (billion RMB)	China	7'641.0	13.7	4'204.4	15.4
	Shanghai	336.04	13.0	188.75	14.2
	Jiangsu	662.32	16.2	380.88	16.9
	Zhejiang	532.53	15.0	297.6	15.7
	Anhui	202.94	15.0	110.94	16.1
	Consular Area	1'733.83		978.17	
Completed Investment in Fixed Assets (billion RMB)	China	10'987.0	24.0	5'416.8	25.9
	Shanghai	392.51	10.8	192.84	9.6
	Jiangsu	1'006.37	20.3	386.59	22.4
	Zhejiang	759.30	13.8	331.1	11.4
	Anhui	354.47	40.6	205.46	47.9
	Consular Area	2'512.65		1'115.99	
Exports (billion USD)	China	969.10	27.2	546.7	27.5
	Shanghai	113.57	25.2	64.34	20.9
	Jiangsu	160.42	30.5	90.83	28.4
	Zhejiang	100.90	31.4	57.99	28.5
	Anhui	6.84	31.7	3.85	32.6
	Consular Area	381.73		217.01	
Imports (billion USD)	China	791.60	20.0	434.2	18.2
	Shanghai	113.91	19.1	63.64	21.3
	Jiangsu	123.58	17.7	67.22	17.6
	Zhejiang	38.25	25.1	22.59	31.8
	Anhui	5.41	37.7	3.42	33.7
	Consular Area	281.151		156.87	
Foreign Direct Investment (during the period)					
Projects	China	41'485	-5.76	18'683	-5.4
	Shanghai	4'061	-0.7	1'953	5.1
	Jiangsu	6'541	-8.2	3'317	16.5
	Zhejiang	3'583	5.5	1'453	-10.9
	Anhui	592	40.6	258	5.7
	Consular Area	14'777		6'981	
Contracted (billion USD)	China				
	Shanghai	14.57	5.4	6.79	-6.0
	Jiangsu	38.78		21.73	25.5
	Zhejiang	19.1	18.5	8.47	9.1
	Anhui	2.50	60.9	1.55	55.9
	Consular Area				
Actually Utilised (billion USD)	China	63.0	4.5	31.89	12.2
	Shanghai	7.11	3.8	4.30	7.3
	Jiangsu	17.43	32.2	12.60	48.2
	Zhejiang	8.89	15.1	4.92	26.5
	Anhui	1.39	102.4	1.28	160
	Consular Area	34.82		23.1	

Source: Chinese Authorities

* All statistics not including Taiwan, Hong Kong and Macao

Table. 2

Swiss - Yangtze-Delta Region Trade Relations*

	Import from Switzerland				Export to Switzerland			
	2006		2007.1-6		2006		2007.1-6	
	Million USD	Growth rate %	Million USD	Growth rate %	Million USD	Growth rate %	Million USD	Growth rate %
Shanghai	1,121.59	14.51	678.43	28.51	264.14	17.3	148.31	5.51
Jiangsu	427.00	24.2	225.38	7.53	345.00	63.93	175.11	13.27
Zhejiang	151.42	4.75	100.0	32.1	272.45	33.71	170.0	37
Anhui	28.95	45	6.38	- 61.91	12.59	34.75	7.36	41.28
Delta Region	1'728.96	17.86	1'106.57	35.74	894.18	39.95	500.78	18.51
China	4'583.14	18.1	2'496.51	29.0	2'260.14	16.1	1'587.77	34.0

Source: Chinese authorities

Table. 3

Swiss Investment in Delta Region

In the Region	Swiss Investment						Accumulated by end of June 2007		
	Project		Contracted million USD		Actually million USD		Project	Contracted	Actually
	2006	2007.1-6	2006	2007.1-6	2006	2007.1-6			
Shanghai	23	17	62.25	28.38			283	1'604.68	
Jiangsu	15	15	44.97	83.05	83.61	168.42	131	674.37	605.39
Zhejiang	10	0	101.16	1.18	45.45	17.34	54	220.0	120.0
Anhui	1	0	3.07	0	0	1.02	6	39.86	
Delta Region	49	32	211.45	112.61			474	2'538.91	
China	123	50			196.60	203			