

CHINA: RECENT TRENDS AND OUTLOOK - PART V

Business structures in China

Investors or exporters interested in China must consult with their government's representatives in China to find out the requirements of the Chinese Ministry of Commerce, as well as the conditions imposed by the *Catalogue Guiding Foreign Investment in Industry* for its specific sector before launching into any costly operation in China.

A variety of options are available to companies interested in setting up operations in China. The following are the most common:

- Open a representative office
- Enter into a joint venture
- Set up a foreign-owned company.

Regardless of the form of representation selected, prior approval must be obtained from a competent authority, usually the Ministry of Commerce. The choice of business structure is usually dictated by the *Catalogue Guiding Foreign Investment in Industry*.

The rep office has limited privileges. It can canvass for customers, promote and coordinate the company's activities in China. However, it is not allowed to conduct business operations in its own name. The rep office needs a guarantor, a Chinese company certified by the Ministry of Commerce. This guarantor is responsible for handling bureaucratic formalities.

A joint venture is the most frequently encountered form. It consists of two partners, one of which must be Chinese. Although the size of the foreign stake is theoretically unlimited, in certain specific segments it may be restricted to a minority stake. The amount must be greater than 25% for the joint venture to benefit from tax benefits.

The foreign-owned company has been the fastest growing business structure in recent years. Such companies—Chinese corporations created by foreign investors—are subject to specific sector-based regulations and are not allowed in certain strategically sensitive sectors.

CONSTRAINTS AND DIFFICULTIES ENCOUNTERED ON THE CHINESE MARKET

China is an emerging country looking to acquire technology from abroad and to equip itself in order to produce and export.

Although import tariff barriers are being phased out, it bears mentioning that customs duties are not the same for all product categories, since the Chinese are out to encourage local industry rather than imports.

With regards to hygiene, phytosanitary and technical aspects, China often applies import restrictions that sometimes have no technical justification, for example, labelling approval that is particularly long to obtain for food products and equally time-consuming certifications for vehicles.

Other import restrictions are simply a form of retaliation in response to justified restrictions imposed by China's trade partners for hygiene and anti-dumping reasons.

Copying and pirating apply not only to consumer goods but also to capital goods such as automobile parts. Although the process can take up to two years and redress is difficult to obtain in case of infringement, trademark registration and patent filing is a must. Justice outside big cities is sometimes hard to come by, since the perpetrators are often state-owned enterprises protected by the authorities.

Bureaucracy and corruption

Bureaucracy exists at all levels and, in cases of major contract or contracts involving strategic sectors, is simply unavoidable.

The Transparency Index, which measures the risks related to a lack of openness in economic decision-making, places China in the trio of the three worst countries. Corruption is rampant and costs on average 8% of the contract amount. Official statistics are disingenuous, as are the many political decisions that affect business.

Finally, as stated in an earlier bulletin, financing remains a major handicap. Chinese banks still do not offer attractive conditions, and many Western banks are not receptive to this market.

WHY NOT HONG KONG?

Hong Kong is a good gateway to China for exporters and investors. Well developed, this island operates in a free market economy and has an extremely low tax rate.

Most Canadian SMEs that set up on the island have been able to rapidly expand their activities to China and even other neighbouring countries. Hong Kong companies have the financial means, know-how and contacts required to do business in Mainland China, and the cost of using a partner is generally offset by the greatly decreased risk involved in trying to go it alone in China.

Moreover, like its neighbour, Hong Kong offers many projects in the spheres of infrastructures and technologies related to transportation and environmental improvement.

Conclusion

Asia, and particularly China, will be the site of the greatest economic growth in the next 15 years.

For Canadian enterprises, a market study beforehand will be especially useful, and can be used both to capitalize on opportunities in China and to better confront the stiff competition this country delivers on the global stage.

The Chinese economy and market are highly complex and constantly changing. Investors and importers seeking to do business in the Middle Kingdom can turn to a number of government agencies and private companies to help them identify the risks and opportunities in this country.