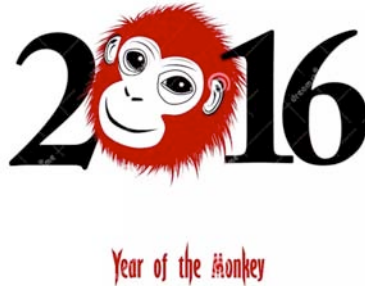


**2015 is behind us but what about 2016?**  
Gilbert Van Kerckhove, Beijing January 2016



**How does China look in 2016?**

"China will continue to experience an economic slowdown and major challenges still have to be met." China Daily 20 January 2016

It is difficult to be an optimist, in Europe and in many other countries. China is not an exception. Get used to the "new mediocre" (Christine Lagarde). Or, as François Hollande says "We are in a state of economic emergency". In August 2014 I wrote a paper on the many challenges China was facing and the difficult task for the government to deal with it. Find it here:

<http://blog.strategy4china.com/wp-content/uploads/2014/08/140815-China2014.pdf>

Things have not changed for the better, on the contrary.

Chinese experts agree that the economy is facing serious problems. I only name a few:

- Further **slowing down of the economy** where government intervention might not help anymore or even make matters worse;
- Weak world markets and the end of the massive investment party in China have **decreased manufacturing activity**, also impacting the countries selling to China the many commodities, now they also have less money to buy from China.
- How to revive **tourism** in China?
- How to tackle the **housing inventory** in real estate and carry out "destocking"?
- "**Supply-side reform** with Chinese characteristics": what will really become of it?
- The need to close down the many **zombie SOE** and tackle **overcapacity**, with a dark cloud of unemployment and social instability.
- Total **debt** to increase; further weakening of the RMB; **capital flight** (China capital outflows rise to estimated US\$1 trillion in 2015 - Bloomberg Business); serious increase of **non-performing loans**.
- Increasing **costs and taxes** and cumbersome bureaucracy are making the industry less competitive while quality levels tend to rather worsen than improve.
- "Open-door policy" has become an oxymoron in China; the paranoia for instability and threat to the Party is further **closing the doors to the outside world** as well as for foreigners and foreign business, all despite the nice words of the government; in many areas "success" for foreign investment is doubtful. Not surprisingly, Amcham survey says most companies feel "less welcome" and 25% intend to leave China. At the same time China Daily claims foreign companies are happy in China.

- Expect more **foreigners to leave** as work permits and visas are getting worse (not to even mention pollution); foreigners are just a "nuisance" when there are so many critical issues to deal with internally; maybe when the dust has settled and there are no more stability risks we might be really welcome again; many foreigners are naïve and do not see the trend; Shanghai and some second-tier cities might still be "more welcoming".
- Total of Chinese **Green Cards** said to total "over 7300 for the 600,000 foreigners living in China". The card is the most difficult to get in the world, is often a problem to use and fails miserably in "granting the same rights as to Chinese citizens". As for the amount of foreigners in China: the country probably beats most countries as having the least foreigners per inhabitants. And some Chinese still think we are too many.
- **Self-censorship** is recommended, even if well intended advice seems to be in line with a socialist society.
  - The risk remains that **nationalism** and some level of arrogance will grow as a diversion tactic and for other reasons, increasing the risk for international friction and conflicts. The territorial disputes in the South China Sea are probably the biggest worry.
  - The **draft NGO** law is still out there without any clear view what will happen next. If the draft becomes law as it is now, the effects will be ominous, while many underestimate its reach: "We will be OK". You will NOT.
  - Chinese will continue their "conquest" of **foreign markets and companies**, but they will need to adapt and learn to avoid a backlash.
  - Education, health care, income inequality, food security, social security, the need for creativity and innovation will all remain on the table as hard-to-solve-issues.
  - The battle against pollution, corruption and injustice is still being fought but how will it end?

## **Conclusion**

We should remain modest and admit the challenges China is facing are not easy and nobody can claim to have "the" solution. China has been going through many difficult periods in its history and somehow it always managed to come out better.

Our challenge is first to seek a solution for the myriad of problems we have in our Western countries (including Belgium) where politicians seem pretty clueless to find long-term solutions. Let's not even mention the USA and the circus around presidential elections.

A hard-landing in the Chinese economy is "unavoidable"  
 Billionaire investor George Soros, January 2016 in Davos

Are we heading to a meltdown, a hard landing, a deep recession – whatever you want to call it? Personally I don't think so. But we all need to think careful what to do, how to proceed, and proceed wisely and carefully.

So, fasten seat belts, watch your back and be happy. Beijing is not that a bad place to be, despite all our complaints! Where would we go anyway?

## Looking back

2015 has been a difficult year but also with some happy and exciting moments, like seeing our daughter move to Brussels for her new job and me participating in the 3D HD movie "The New Three Gorges". And my first ever real holiday in fifteen years.

My main website was hacked. Then I was the victim of a dishonest and unprofessional "local" IT company (foreigners!) who ran away with my money and viciously trashed my website. Fortunately I found a great savior and I started working on my new and renovated websites. See down below. We had some unpleasant problems with a Chinese government department that shook my confidence in the system. We solved it but it left a bitter taste.

Then, when I was close to finalizing my websites and other work, my main Apple laptop had a devastating (software) crash in December. Worse, it turned out my "Time Machine backup" did not work due to a software bug from Apple. I bought a big iMac and managed to recover myself all data and some critical settings.

2016 is here, the websites look great and the new iMac and iPhone are slowly obeying my orders. The whole experience showed how dependent we have become on technology and how much time it consumes. So one of my goals for the year is to see how to simplify IT stuff and increase efficiency. And relax more!

My plans for 2016 are to further step away from "business" except for the essentials that include my China seminars and occasional stints with government entities for fun stuff like tourism, aging issues, qipao fashion, and who knows what more. We continue to assist Chinese companies abroad, now mainly in Africa.

Rotary will keep me busy too.

A major goal is to restart writing book(s), and not only do blogging – ideas have been spinning in my head since long.

### *Note*

I talk extensively in private and in my seminars about the challenges mentioned.  
*Additional written comments are available on request.*

### *About my websites*

<http://blog.strategy4china.com> had become too vast. We have now more focused websites. Some are in the final stages of implementation, other will gradually grow. Some of the old posts are migrating to the new sites. See here:

Beijing Global Strategy Consulting Co., Ltd. - the company's website:  
[www.strategy4china.com](http://www.strategy4china.com) (needs more work)

Business & Economy: <http://blog.strategy4china.com>

Beijing life: [www.beijing1980.com](http://www.beijing1980.com) (includes Rotary, events, views on China, and more)

My books - Toxic Capitalism: [www.damulu.com](http://www.damulu.com) (updates on future books + publishing)

Environment & Society: [www.unirizon.com](http://www.unirizon.com)

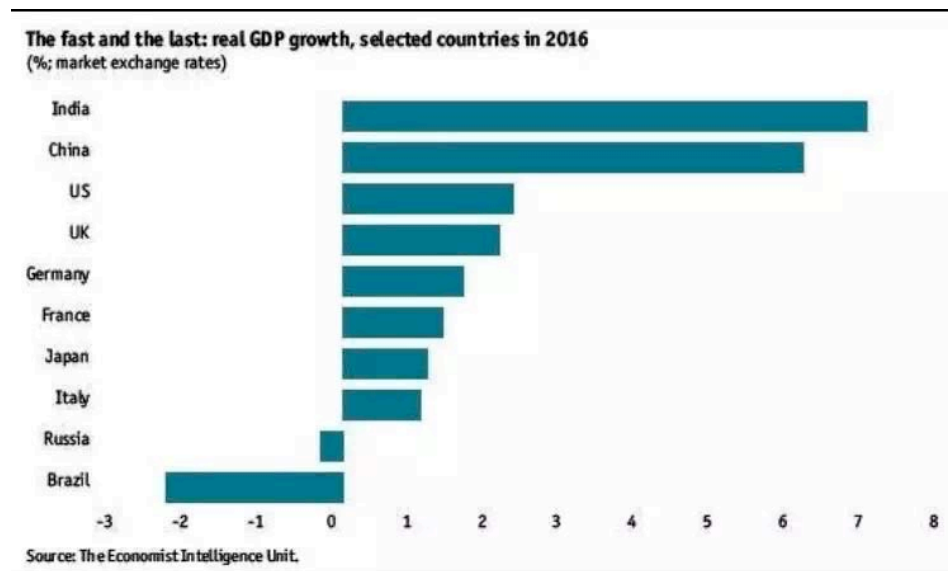
Pictures of China: [www.prc.pics](http://www.prc.pics) (under development)

## Additional notes and thoughts

### *A challenging world*

In my book "Toxic Capitalism" I mention a series of ills in our society and economies that are continuing to negatively affect our present and future. In this respect some of the recent statements from well-known economists such as Joseph E. Stiglitz sound all too familiar to me.

In the book I mentioned the quest by China to look around the world to get the natural resources to feed their factories and people. Many countries that saw a boom in their exports to satisfy China failed to take advantage to invest wisely for the future. With commodity prices way down they now face difficulties to pay back for the over-investments they made and to balance their new budgets. China was a big player, e.g. consuming 60% of the world's iron ore, just to name one commodity. All that has changed while China still buys, but mostly less and at much lower price levels.



Demand in China has gone down a lot as the frantic wave of construction has abated and exports have weakened. Those exporting countries now also have less money to buy from China, another vicious circle.

### *Wrong strategies*

Many countries have taken the wrong decisions, opting for austerity and making things worse. The obstacles are anchored in narrow-minded politics and ideology. What we witnessed was paranoia for inflation and government spending. What we need instead are fiscal policies that are flexible and growth-friendly.

### *Investing for the future is lagging behind*

There is a lot to be done to improve infrastructure but most countries (including the U.S.A.) have failed miserably; in that sense China has been more forward-looking. Other areas where the governments should invest are education, the environment, industry transformation, technology and structural reform of social security and healthcare systems.

## *Tax evasion*

Of course government budgets should be as balanced as possible but that has proved difficult as big companies continue to evade taxes through loopholes defended by well-oiled lobbying, dictating the rules to politicians.

Recent complaints by the EU Commission about massive tax exemptions granted to MNCs by countries such as Belgium (among others) show the extent of the problem: the big companies enjoy huge tax breaks while smaller companies and normal tax payers struggle to survive under the tax burden. Companies mentioned as major evaders were already mentioned in part in my book: Anheuser-Busch InBev, Apple, BASF, Amazon, Fiat Finance and Trade, BP, Atlas Copco, Wabco and others.

## *Income inequality*

More needs to be done. One cannot hope for the increase of consumption as well as for higher quality and better recycling when wealth is shifting more from the lower and middle class to the rich minority that results in less spending overall.

The recent OXFAM report finds 62 people own as much wealth as half the rest of the world (being 3.5 billion people). Five years ago the number of billionaires needed to reach the same result was 388, showing how much the rich got richer.

The financial institutions may have recovered financially but still fail to perform the tasks they are supposed to do. The sector is shortsighted and dysfunctional.

## *Commodities*

*The world of commodities has been turned upside down, with weak demand, overcapacity and oversupply. We have seen a wave of bankruptcies and lay-offs.*

The drop in demand and prices for commodities has dramatically affected many countries, even the U.S.A. (crude oil, iron ore, agricultural crops, mining, ...). Other countries supplying copper, iron and aluminum ore, coal, crude oil, and gas are also suffering. Many made huge investments to increase supply and are now facing huge bills with drastically reduced income. Some abandon the new projects, others continue construction hoping for better days.

The list of affected countries is long: Chile, Peru, Australia, India, Brazil, Venezuela, Canada, USA, Nigeria, Angola, Ghana, Zambia, Mozambique, Indonesia, South Africa, Saudi Arabia, ...

As a result Chinese investments are on hold in several countries. It also shows Africa's vulnerability to economic changes in China.

Oil prices are not to return to former levels anytime soon, most agree. Shale oil and gas installations have been shut down massively in the U.S.A. impacting manufacturing and employment in the whole drilling industry, as prices are too low. That also means that whenever price levels increase for whatever reason (e.g. instability in the Middle East) those wells are ready to restart flowing, again levelling any serious increase in prices.

## ***Looking at China***

"Stability" remains the main concern

The power of the Party is closely linked to its ability to deliver economic progress. As long as the Party can prove it delivers jobs, good living standards and continued development of the economy the people will accept its far-reaching power and abstain from protests to claim workers' rights and other concessions. As the economy shows signs of trouble and a new wave of lay-offs is expected, especially in places like the Northeast rust belt it is a growing concern for the government. The top people realize the future of the Party is at stake.

What to expect of GDP growth? Most of the official figures do not survive scrutiny and I have never spent time trying to figure out GDP growth, past, present or future, at least not in exact numbers. A waste of time, I leave that to economists who end up usually off track.

It is clear the high growth figures are a thing of the past and will not come back anytime soon. As we had the pollution smog obscuring all in the past weeks, economic figures are also hard to see clearly. Most troubling is the lack of direction and a climate of uncertainty, in part reflected in the roller-coaster stock market.

The situation in China is difficult. Since years there is talk to shift from investment-fueled economy and exports towards consumption and services. Again here many factors make that complicated. One is income inequality, in what is called a socialist economy. China Economic Review reported in January 2016:

Study finds top 1% of China's families own 1/3 of its wealth:

A study by Peking University's Institute of Social Science Survey has found that China's richest 1% own a third of its wealth – of which the poorest 25% own only 1%, The Financial Times reported. The study also found China's Gini coefficient for income, a measure of inequality, was 0.49 in 2012, well above the World Bank's standard for severe inequality of 0.40. That contrasts with official estimates that claimed the coefficient had tilted downward from 0.477 in 2011 to 0.469 in 2014. "To put it simply, the poor are getting poorer and the rich are getting richer," said Renmin University sociology professor Zhou Xiaozheng.

With all the talk to stimulate creativity, innovation and entrepreneurship, the environment is still not favorable. Issues: access to international information and the difficulty to work with modern Internet tools; increasing and silly censorship; the failure to attract dynamic and experienced people from abroad because of visa restrictions and sclerotic management structures, despite of all the hollow talk of officials – read the fine print of what type of "high-skilled" people are welcome; uneven efforts in IPR and quality assurance, the unsustainable tax burden for small companies, and much more.

If local companies struggle with the bureaucracy and tend to survive by evading taxes and rules, foreign companies' hope gets often trashed by colliding with the increasing costs, Chinese bureaucracy, over-complex laws, approval processes that take ages or never conclude, and debilitating taxes of all kinds. Add to the mix a corruption that still runs deeply, despite the efforts of President Xi Jinping. Foreign companies all seem to agree that state-owned companies have unfair advantages in financing, access to contracts, licensing and more. Many foreigners get burned in setting up businesses in China but their stories are kept very quiet. In China when one hears "Golden Opportunities" it is time to run away. Fast.

Does it mean "all is doomed and bad"? Not really, some niche players are still being successful but there is no room for the naïve.

### *Market access for foreign companies*

If one listens to foreign companies and foreign chambers of commerce, things are definitely not getting better. Obscure non-tariff obstacles, uncooperative customs procedures, imposition of restrictive standards, unfair court rulings, lack of legal protection, favoring local brands (even if of lower quality): the list is long – and strongly denied by the government.

Irony is welcome. China Daily mentioned in January 2016 the complaints of Chinese furniture companies: "It costs a lot of money to fulfill the ecological details adopted by the EU Commission in 2009". Indeed furniture imports must meet new criteria on environmental, ecological and formaldehyde emission standards. Chinese furniture makers believe these standards are complicated and costly to achieve. Oh! Really? Well maybe they should talk with foreign companies trying to import cheese, beer and other food products (as one example): they are facing ridiculous and unpredictable rules and testing procedures, costing lots of money and often resulting in goods being destroyed (without a good reason) by the customs. Who ever complains about that? The EU should enforce stringent rules for all Chinese foodstuff and TCM entering the EU. That would be interesting!

### *Real estate*

As I mentioned in my report dated June 2014, the situation is "difficult". See it here:  
<http://blog.strategy4china.com/wp-content/uploads/2014/06/140603-real-estate.pdf>

Some segments of the market are getting a bit better but recovery is still far away in many sectors, impacting many industries involved in construction. Calls to put three times more steel in buildings "to help the steel industry" are not exactly showing the way. Eliminating the existing inventory will take time. With a retail sector getting worse and more complex (online sales) the multitude of sub-standard shopping malls will face hard times.

Inventory of unsold new homes continued to increase in 2015, even as the government has pledged to help draw down excess stock across the country. Unsold inventory was up 11.2% for the year to 452.5 million sqm, increasing 11.6 million sqm in December 2015, according to the National Bureau of Statistics.  
Source: SCMP

In Beijing the situation is becoming unsustainable and devoid of logic. Many residential buildings are still empty but rents are sky-high, affecting mostly the lower-income people. Service people are either leaving or asking a big salary rise. Quality of service is getting worse by the day. The food and beverage sector is plagued by closures as landlords increase rentals to astronomic levels; many shopping centers count many empty units and many rentals are short-lived as the tenants bleed money. I have assembled a list of recently closed restaurants in Beijing, pretty scary, because often legal rights are a joke. Reason why I refuse to invest anything in such a business.

Office rents also going through the roof, with many empty units while showing "high occupancy rates" according to the real estate companies. Landowners such as SOHO are to be avoided due to their hostile attitudes towards tenants (and even clients). No improvement in view. One day it will implode in one way or the other.

Beijing is killing shopping for tourists (and even residents). The malls previously flooded with tourists looking for a bargain are now either banned or transformed into high-class shopping centers, devoid of customers. A typical example is Yashow in Sanlitun. Tourists will go home disappointed and the salespeople and manufacturers see their fortunes going up in smoke.