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Opportunities in China's (Shanghai) Pilot Free Trade Zone: A Polish Perspective

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The establishment of the China (Shanghai) Pilot Free Trade Zone in September 2013 has been widely perceived as a focal point of the new Chinese leadership's market-oriented economic reforms. Its aim is to test new instruments for further opening the Chinese economy to the world, thus to support its pivot from an export-based to a more innovative, consumption-based economic model. The zone could create attractive business opportunities for Central and Eastern European countries. Polish companies, especially those offering agricultural and luxury goods, and the Polish government should attentively monitor the development of the zone for such opportunities and publicize when conditions change for doing business in China.

The China (Shanghai) Pilot Free Trade Zone (CSP FTZ) is one of the most ambitious Chinese economic projects in recent years and marks a new phase in market reforms in the country. The zone's creation is based on the country's rich and positive experience with Special Economic Zones (SEZ), which have been established in China since 1980, such as in Shenzhen, Zhuhai or Xiamen. Given the success of the SEZs in terms of introducing elements of the market economy to China, enhancing the administration's efficiency, and accelerating the pace of economic growth, the most beneficial reforms implemented in the zones, e.g., tax preferences for investors, have subsequently been adopted in other parts of the country, including in the coastal "open" cities.

CSP FTZ could play a similar role to the SEZs, contributing to a more open and less bureaucratic Chinese economy as well as becoming a template for reforms in the Chinese economy in the coming years. This is indicated by the use of the word "China" in its formal name. President Xi Jinping's visit to the zone in May 2014, during which he called the project an "important step in China's reform," would seem to support this theory. The zone can also be perceived as part of a strategy aimed at shoring up strength in trade vis-à-vis international trade agreements that do not include China but which are now in negotiations, such as the Trans-Pacific Partnership (TPP).¹

A New Generation SEZ. At nearly 29 sq. km, CSP FTZ combines four previously existing economic areas in Shanghai: the Waigaoqiao Free Trade Zone, Waigaoqiao Bonded Logistics Park, Yangshan Free Trade Port Area, and the Pudong Airport Free Trade Zone. The establishment of a new special zone in Shanghai was based on the city's potential to become the main financial centre in East Asia, as well as its coastal location, advanced infrastructure and rich history of contacts with the rest of the world.

CSP FTZ differs from the SEZs as it concentrates mainly on facilitating the services sector rather than manufacturing. Moreover, the scope is relatively narrower than in the past and does not include such benefits as significant tax reductions. Nevertheless, there are several areas in which considerable changes have been adopted.

Among them, the first is far-reaching financial reforms that have been announced will be implemented, especially enhanced cross-border usage and convertibility of the renminbi (RMB). That should attract foreign investors by facilitating international financial transactions and should encourage companies to relocate their regional headquarters to Shanghai. Furthermore, the zone will be a testing ground for the adoption of market-oriented interest rates on

¹ D. Wnukowski, "Trans-Pacific Partnership Negotiations; Lessons for the TTIP talks?" *PISM Bulletin*, 2 October 2013, www.pism.pl/publications/bulletin/no-104-557.

foreign-currency deposits. These moves could attract major international financial institutions and contribute to the enhancement of China's links with the world financial system. Second, customs regulations will be loosened. The changes in this area are reflected by replacement of the "first-border system," which required prior approval for goods to be exported to China before they entered the country, by a "second-border system," which assumes there will be controls after products arrive to the zone. This should generate lower costs for exporters and streamline trade. These efforts are aimed at creating in Shanghai a key distribution and logistic hub in East Asia in the coming years.

Third, administrative procedures and legal rules have been simplified. For the first time, business activities are accepted in every area except those specified by a "negative list," which includes elements for such industries as mining, agriculture or gas and water supply. Conducting business in the listed sectors in the CSP FTZ is still highly restricted, through such means as pre-approval procedures. However, this list could be shortened in the future and even happened at the end of June this year when it was reduced from 190 to 139 items. In less-restricted sectors, such as banking or professional services, the whole process has been loosened, that is, such requirements as permission may be granted after the start of some activity and the system of company inspections has been replaced by annual reports. Local authorities are also obliged to ensure equal treatment of Chinese and foreign entities, which has been a serious obstacle in doing business in China so far. Other changes concern the entity registration process, which has been shortened from about a month to a couple of days with the creation of a "one-stop shop" to deal with formalities. Furthermore, in selected sectors it is possible to establish fully foreign-owned companies instead of joint ventures with local partners. Moreover, CSP FTZ is a testing ground for the administration's capacity to implement future reforms.

All of these changes will be implemented gradually and at a relatively slow pace, which could hamper business activities. Some of the reforms, such as allowing foreign banks to transfer funds overseas, does not function well in practice. The reason for this could be in the internal political factors of the zone's creation and reflects Communist Party authorities' vision of CSP FTZ's future shape so it does not undermine the stability of the country's economy, and thus the regime. Businesses are also concerned about the effectiveness of the adopted regulatory measures and the ability of the local authorities to create a stable legal environment.

Opportunities for Polish Businesses. By the end of May 2014, more than 16,000 entities had been registered in CSP FTZ, but only about 1,200 were foreign firms. The zone is treated by local entrepreneurs as a tool to start acting globally and gain experience with a more open-market economy. Nevertheless, foreign companies, including some from the CEE, could also make use of the changes adopted in CSP FTZ to start or enhance the extent of their presence in China.

From a Polish perspective, the most important aspects of interest are related to the changes in customs regulations. These could encourage Polish companies to start or increase the export of goods to China, as cost and complexity would decrease. In particular, the export of agricultural goods, such as meat, honey or dairy products, seems to be attractive as all of the obligations concerning such things as customs duties or sanitary requirements can be easily fulfilled in the "one-stop shop." Moreover, sales of other consumer goods, such as cosmetics or furniture and luxury goods, including amber jewellery, may be easier not only because of the flexible registration procedures but also the existing promotional venues in Shanghai, such as its numerous exhibition centres. Polish entrepreneurs may also find attractive niches in the professional services sector, such as legal, consulting or training. Furthermore, the medical services sector could become very interesting for investors as institutions fully based on foreign capital may be established. Additionally, Polish firms may also be able to compete in logistics and maritime transport as many of them have significant experience on the international market. CSP FTZ could also be a favourable location to set up regional offices or trade representations of companies from Poland and other CEE countries active in East Asia.

Conclusions and Recommendations. As China is becoming a more and more important export partner for the CEE countries, including Poland (50% growth in the first quarter of 2014 in comparison to the same period in 2013), more attention should be paid to the changing business environment. In this context, by carefully monitoring developments in the CSP FTZ Poland could disseminate valuable information for those firms making long-term business decisions. Moreover, a quick entrance into the zone could entail better access to the whole Chinese market in the future. Nevertheless, intensive efforts aimed at promoting CEE business in CSP FTZ should be actively undertaken according to each country's promotional strategy.

For Poland, the efforts should concentrate on improving its image in China through its "POLSKA" brand campaign. Polish ministries, especially the ministries of Foreign Affairs and Economy as well as public agencies that support promotion worldwide should more actively inform entrepreneurs, for instance, through the special programme "GoChina" or via contacts with business organizations. Also, the Polish Trade and Investment Promotion Office (WPHI) in Shanghai and embassy in Beijing should continue to promote awareness of CSP FTZ among businesses and ensure practical support in such areas as legal interpretations or searching for reliable local business partners.. The export information system within the country, including the Network of Investors and Exporters Service Centres (COIE) should also be improved. Polish firms should press the administration more to monitor the reforms in China and seek out business opportunities. Moreover, high-level and medium-level visits by Polish officials accompanied by entrepreneurs could be beneficial to Polish business activity in CSP FTZ.