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Chinese government hints at removing limit on foreign shareholdings of local vehicle production JVs

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Chinese officials have hinted that the authorities are considering relaxing the regulation that limits international automakers to owning no more than 50% of vehicle production joint ventures (JVs) in China. Speaking at an industry event in Tianjin, a senior official of the National Development and Reform Commission (NDRC), which imposes the policy, stated that the state body was considering lifting the current regulation. Xu Shaoshi, chairman of the NDRC, stated at the World Economic Forum in Tianjin that the government is looking at lifting the 50% cap that has limited foreign automakers' stakes in their JVs with local Chinese players since 1994, reports Bloomberg.

This is the second time in recent months that the government has hinted that the regulation may be lifted. In April, another senior official from a government body claimed that the law's restrictions were against bilateral trade agreements. In April, Miao Wei, the head of the Ministry of Industry and Information Technology (MIIT), said, "The restrictions are severely questioned by the US side." He gave a general timetable of when the lifting of the law was likely to take place. "What we can do is to resist the questioning for as long as possible. We will have to remove the restrictions in three to five years at the earliest, in eight years at the latest," he said.

Outlook and implications

The question is whether the Chinese government would actually relax this policy and, if it did, would Chinese automakers be able to stand their ground and maintain their market shares of their domestic market. The Chinese government is under international pressure to relax the policy, which safeguards the interests of local automakers in their JVs with international players by mandating that the Chinese automaker must have a majority stake or an equal 50% stake in the joint venture. This means that control of the JV, as well as majority financial revenues, rest with the local player.

Changing the policy to relax the 50% cap on foreign ownership implies that foreign automakers could then own a majority stake in a JV, or indeed create a wholly owned foreign enterprise (WOFE) in China if the law was completely relaxed. The China Association of Automobile Manufacturers (CAAM) has vociferously stated its concerns about the suggested relaxation of the policy, stating that Chinese brands would be "killed in the cradle" if the law was relaxed.

However, there is also growing optimism regarding Chinese automakers, as they currently have gained share in the domestic market with products offered at a cheaper price point, but with the attributes to entice local Chinese consumers. On a year-to-date basis, the volume of Chinese-brand passenger vehicle (PV) sales hit 4.02-million units in May, up 10.9% year on year (y/y) and accounting for 43.4% of the PV market. Of these sales, Chinese-brand sedan sales totalled 891,000 units, down 17.7% y/y and accounting for 19.2% of the segment's sales. Chinese-brand sport utility vehicle (SUV) sales hit 1.82-million units, up 50.5% y/y and accounting for 56.7% of segment's sales. Chinese-brand multipurpose vehicle (MPV) sales totalled 936,000 units, up 18.3% y/y and accounting for 90.9% of the segment. When compared with the preceding month's data, the share of Chinese brands edged down in most segments in May.

On the one hand, Chinese brand products operate at a lower price point on average compared with international models produced by JVs in China. As they do not compete directly against each other, some market analysts believe that relaxing the policy would not completely eliminate the local brands from the market. However, others voice concern that technologically Chinese brands are still behind their international counterparts. International automakers are already planning major product offensive strategies in China to gain back lost market share, and they are planning models to meet the lower price point as well.

There is also the question of subsidies, as there is currently a series of subsidies on offer to automakers in China. The new energy vehicle (NEV) segment is one area where the government offers substantial monetary subsidies to promote product development and sales. NEVs include pure battery electric vehicles (EVs) and plug-in hybrid electric vehicles (PHEVs), and funds are also available for fuel-cell vehicles (FCVs). In addition, there is the reduction in the vehicle purchase tax, which was introduced 1 October 2015 and which is expected to expire this year, under which cars with engines of 1.6 litres or smaller are given a 50% reduction in the new-car purchase tax, while for NEVs this tax of 10% is completely abolished.

Additionally, there are the special annual research-and-development (R&D) funds allocated on a case-by-case basis to Chinese automakers. Consequently, should the Chinese policy limit of 50% ownership for foreign OEMs in local production JVs be relaxed, these R&D funds will continue to work to strengthen the local players. Funds are given annually to local automakers depending on the products they are developing. The government gave Chery Automobile subsidies worth CNY633 million (USD95 million) in 2009, CNY1.12 billion in 2010, and CNY594 million in 2011 − and the annual subsidies are continuing and to a range of automakers.

Chinese players have also begun a major talent recruitment drive in recent years with the hiring of international talent, from engineers to car designers, thereby strengthening their in-house capabilities and subsequently their product line-ups. Optimists in the market believe that the now-stronger Chinese brands should be pushed to stand on their own now. Li Shufu, founder and chairman of Chinese automaker Geely and owner of Swedish automaker Volvo, is a major advocate for relaxing the policy. He insists that Chinese manufacturers have been given a "sugar-coated bomb". In an interview with the *Financial Times* in 2015, Li reportedly said that Chinese automakers have become complacent and that the policy is not constructive for their growth as it limits their aspirations for developing a competitive edge.

Meanwhile, in 2004 the Chinese government relaxed the policy that limited international supplier companies to owning a 50% stake in local JVs. Following a relaxation of the law, international suppliers have been able to form WOFE companies in China.

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