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METRIX

131
billion dollar

That's the combined market value in US dollars of all private start-ups in China at the end of 2016. The Chinese Ministry of Science and Technology said **the so-called "unicorns"**, mostly young and innovative tech firms, almost doubled their combined market value compared to 2015.

TOPIC OF THE WEEK: Hong Kong after the elections



Carrie Lam, center, declares her victory in the Hong Kong chief executive election, Hong Kong, March 26, 2017.
Source: Imagine China

New chief executive faces tough challenges

Carrie Lam, Hong Kong's newly elected chief executive faces an uphill struggle after her comfortable election victory last Sunday. On March 26th the Beijing-backed candidate was selected by a 1200-person election committee stacked with Beijing loyalists. She received 777 votes. Lam, the former Number 2 in the Special Administrative Region, now has to manage **the balancing act** of fulfilling Beijing's expectations while preventing a further polarization of Hong Kong's society.

Lam defeated the former finance secretary John Tsang, who received only 365 votes. During the election campaign Tsang, like Lam, took a Beijing-friendly stance but also expressed sympathy for demands

for greater autonomy. According to polls, Tsang enjoyed considerable more support from the general public than Lam. When her selection was announced last Sunday, protestors took to the streets of Hong Kong and hurled toilet paper at the liaison office of the Chinese Communist Party.

Many people in Hong Kong consider as undemocratic the way Lam got elected. Debates in 2015 on how to reform and democratize the election process **came to nothing**. Meanwhile Beijing has increased pressure on the semi-autonomous city: The disappearance of booksellers critical of the Beijing government and the exclusion of opposition politicians from the city's legislative council have fueled resentment especially among younger Hong Kong residents.

Lam must now try to **ease social and political tensions** that have simmered since the so-called umbrella protests of 2014. But many people in Hong Kong regard her as an extension of the Beijing government. They don't believe she can tackle many of the city's everyday problems and social issues – such as the growing gap between rich and poor. Many see in her a clone of her predecessor, unpopular Chun-ying Leung. In a reference to his initials, Lam is often called “CY 2.0”.

Mareike Ohlberg, research associate at MERICS: “In times of growing social and economic discontent, it's going to be really difficult for Carrie Lam to reconcile the different political camps.”

THE EUROPEAN VIEW

Britain and Europe are too busy with their own divorce to care about Hong Kong's future

Reactions in Europe to the elections in Hong Kong range from despondent **media coverage** to outright disinterest. The British government, which used to stand out in Europe and openly criticized Beijing's infringements of the city's autonomy, appears far too busy struggling with homemade political challenges to care about the political future of Hong Kong. Britain's coming divorce from the EU, made official with the triggering of Article 50 this Wednesday, is thus already showing paralyzing effects on British and European policy towards Hong Kong. Read more in our **latest blog post by Bertram Lang**.

CHINA AND THE WORLD

Australia shelves planned extradition treaty with China

The Australian government canceled a vote on Tuesday this week to finally ratify an extradition treaty with China, 10 years after the deal was signed. The parliamentary vote was taken off the agenda following concerns raised by lawmakers over human rights violations and the rule of law in China. The shelving of the vote is a set-back for the Australian government, which had warned that failing to ratify the treaty could damage **Sino-Australian relations**.

But Australian opposition politicians who control the upper house Senate had made it clear they would not support the treaty. Canceling the vote thus saved the government from an embarrassing defeat. The parliamentary vote had been scheduled two days after China's premier Li Keqiang left the country. His visit was dominated by economic and security issues.

The developments in Australia are a setback for China's overseas hunt for officials accused of corruption. If Australia had ratified the pact, it would have become one of a handful of Western countries that have entered into extradition treaties with China. Both France and Spain have signed and ratified such treaties while Canada and New Zealand are considering requests from Beijing to do the same.

Concerns in Australia over the rule of law in China have grown recently. During premier Li's visit, the Chinese authorities prevented a Sydney academic, [Feng Chongyi](#), from leaving China following a work trip. Mr. Feng, who was born in China but is a permanent resident in Australia, has published research critical of Beijing's growing influence in Australia.

Read more about China's extradition treaties and its international law enforcement drive in the [MERICS China Monitor](#).

Tighter restrictions to curb capital outflows through Hong Kong

China has introduced further restrictions to curb capital outflows through Hong Kong. State-backed UnionPay, the biggest bank card provider on the [Chinese mainland](#), has banned customers from using its cards for down payments on Hong Kong properties.

Many companies and Chinese citizens use the property market in Hong Kong to move their money out of mainland China. Chinese funds had been flooding into the former British colony last year amid concerns about slower economic growth on the mainland and the depreciation of the yuan.

Overall capital outflows from China surged last year causing a sharp decline in Chinese foreign exchange reserves and prompting authorities to strengthen capital controls.

The new restrictions on UnionPay card holders in Hong Kong underline that policy makers in Beijing continue to worry that existing measures are not stringent enough. The concerns persist despite foreign exchange reserves recovering slightly [in February](#).

The impact of the new restrictions is likely to be limited though. Mainland clients could still pay with other credit cards or cash, [a real estate agent](#) was quoted as saying. However, authorities are trying to close loopholes.

Since last October, UnionPay has tried several times to restrict the transfers of funds from the mainland to Hong Kong. The state-backed company imposed a ban on using its service to buy investment-related insurance products in Hong Kong, another potential gateway for capital flight. That was followed by new regulations halving the amount of cash customers can withdraw from the company's ATMs in Macau.

In a related development, China apparently plans to introduce new regulations on outbound direct investments (ODI). **Media reports** say the Ministry of Commerce and the National Development and Reform Commission (NDRC) plan to define the range of overseas investment and list prohibited areas. Both the ministry and the NDRC have not confirmed these reports.

News in brief

- **New partnership:** China and Saudi Arabia plan first drone factory in the Middle East
- **Membership boost:** 13 countries, including Canada, Belgium and Hungary, join China-led AIIB
- **Conciliatory tone:** Rex Tillerson and Xi Jinping emphasize cooperation
- **Joint exercise:** Chinese troops march with Pakistani soldiers for the first time

POLITICS, SOCIETY AND MEDIA

Propaganda chief urges media to rally around CCP ahead of key party meeting

Months before a key party congress this fall, a senior communist party leader this week called on media organizations to “create an atmosphere of favorable public opinion” (营造良好舆论氛围). Liu Yunshan, head of the Central Leading Group on Propaganda and Ideology, said media organizations had to be aware of their political responsibility, publicize the view of the CCP and “reflect the voice of the people”. He made his remarks **during a visit** on March 23rd to the office of the party newspaper the People’s Daily.

Liu also stressed **the role of social media**. He called for the integration of traditional and new media channels to create what he called “a new type of main stream media” (新型主流媒体).

Liu’s remarks echoed those by Chinese president and party leader Xi Jinping last year. Xi had told Chinese media organizations to toe the party’s line, stressing that all media carried the surname “party”.

Liu is a member of the Standing Committee of the Political Bureau. His renewed emphasis on conformity with party policy indicates that the CCP wants to ensure media loyalty ahead of the 19th Party Congress later this year. This in turn seems to suggest that positions on central party policy differ within the ranks of the CCP and that the leadership is worried that those controversies could become public. During the party congress, several key positions in the party leadership are going to be decided.

MERICS analysis:

Boosting the party’s voice: **China’s quest for global ideological dominance**

Governance through information control: **China’s leadership struggles with credibility in social media**

Top prosecutor to review murder charge in controversial loan shark killing case

China’s top prosecutor this week agreed to review a controversial criminal case in which a man was sentenced to life in prison after killing a loan shark who had sexually assaulted his mother. The case ignited **widespread public anger** over alleged police negligence.

Yu Huan (22) from Shandong province was sentenced to life in prison in February after attacking four of his mother's creditors who had exposed themselves in front of the woman and demanded the **repayment of a debt**. One of the debt collectors died. Yu's mother had borrowed more than 1m yuan from the four men and had agreed to 10 per cent monthly interest, state-media said. The police were called to the scene of the dispute but did not intervene. The fatal stabbing happened after the officers left.

Yu's life sentence for murder was widely criticized: Many internet commentators questioned the inaction of the police. Twenty law professors argued that Yu had acted in self-defense. China's top prosecutor now said he would review the case and the charge and investigate possible dereliction of duty by the police.

Anger at miscarriages of justice and police incompetence has grown in China in recent years. In 2009, murder charges against a young women were dropped following a public outcry. **Deng Yujiao** had fatally stabbed an official who had tried to rape her. Last year, a man from Hebei province, who killed a village official after the demolition of his home, was executed despite widespread online criticism of his sentence.

Xinjiang boosts investment in education and infrastructure



Schoolkids in Xinjiang. Source: Peter Morgan via flickr

The autonomous region of Xinjiang in China's West plans to send more ethnic minority students to eastern provinces to improve access to higher education. The regional authorities also want to boost investment into infrastructure in the region, which is less developed than many other parts of China and has suffered from ethnic strife for many years. Xinjiang is also an integral part of China's ambitious Belt and Road Initiative (BRI).

Over 20,000 students from ethnic minorities in Xinjiang will be accepted into schools and universities in other provinces **this year**. According to numbers released by the Xinjiang education department, about 9,800 will study at high schools outside Xinjiang, 3,300 will attend vocational schools and 8,600 will study at universities. Ethnic minority students have been awarded places at schools and universities outside Xinjiang since 1989.

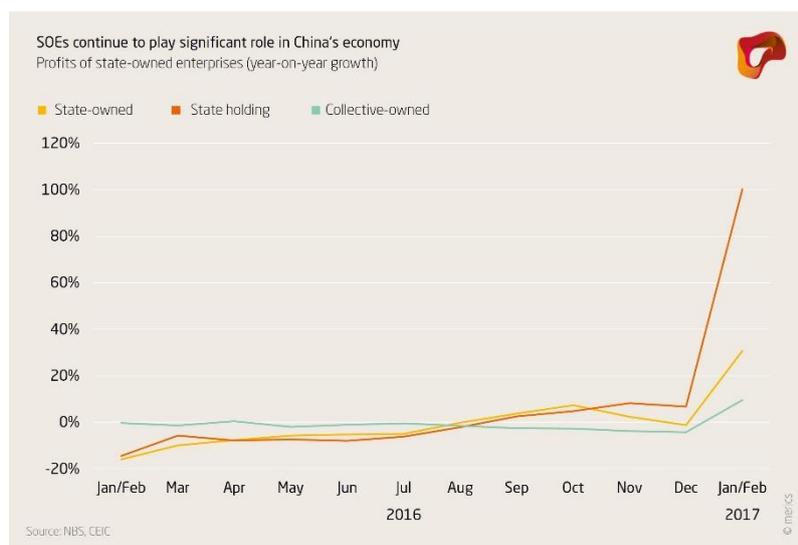
Xinjiang also plans to increase investment in BRI related infrastructure projects. The **regional government** has set a target of 1.5tr CNY this year for fixed asset investments. Banks play an important role in financing BRI projects. Both the state-owned Beijing Bank and the Habib bank, one of Pakistan's biggest private banks, have recently set up branches in the regional capital Urumqi. Both banks expressed an interest in getting involved in BRI projects. Xinjiang is an important part of the BRI initiative and the starting point of the Sino-Pakistani Economic Corridor linking China with the Pakistani port of Gwadar on the Arabian Sea.

News in brief

- Upgrade: **Microsoft has wrapped up work on a customized version of Windows 10 for the Chinese government**
- Bogus break-ups: Central banks urges tighter mortgage checks to curb fake divorces
- Surprise win: **China beats South Korea in World Cup qualifier amid political tensions between Beijing and Seoul**
- Expansion: **Founder of US security firm Blackwater plans bases in China**

ECONOMY, FINANCE AND TECHNOLOGY

China pushes mergers of state-owned enterprises



The Chinese government has given a new push to the consolidation of its economy by pursuing mergers of state-owned enterprises in the nuclear industry. The latest **candidates for a merger** later this year are the National Nuclear Corporation (CNNC) and China Nuclear Engineering & Construction (CNEC). In addition, talks are under way for the trade and real estate conglomerate China Poly Group to absorb Sinolight Corporation, a firm that produces textiles, paper, alcoholic beverages, cigarettes, and other products. The mergers are aimed at making the SOEs **more competitive** – at home but also internationally.

During his speech at the annual National People's Congress in March, premier Li Keqiang stressed again that the government plans to further reduce the number of SOEs directly controlled by the government. By the end of the year their number is expected to drop to 99 – from 196 back in 2003.

Yet the overall restructuring of the SOEs, many of which are inefficient, is proceeding at snail's pace. That's partly due to their vital role in stabilizing economic growth. In addition, the SOEs' profits have risen considerably since the end of 2016 due to rising prices and growing demand. Those developments further hamper necessary SOE reforms.

Critics point out that merging big SOEs will only strengthen their oligopoly position on the Chinese domestic market. Increasing their size will not necessarily result in efficiency gains. One **Chinese think tank** voiced its criticism in a surprisingly frank way: Economic reforms were "to a certain degree" stuck, concludes a 200-page study by the Economic System and Management Institute that is closely associated with the National Development and Reform Commission (NDRC).

Max J. Zenglein, research associate at MERICS: *"By merging SOEs into even bigger industrial giants, China tries to create "national champions" without tackling the root causes of the country's economic problems. State owned companies are set to remain an integral part of the Chinese economic system."*

China's bike-sharing revolution

The former „kingdom of bicycles“ is getting back on two wheels: Bike sharing is **currently booming** in China. The two biggest providers of rental bikes, the start-ups Ofo and Mobike, now each have more than one million bikes on the streets of over 30 Chinese cities. Back in October their combined bike fleets amounted to just 100,000 bikes.

Both Ofo and Mobike don't have fixed docking stations. Cyclists can use smartphone apps to locate a bike close by and return it later to designated bike stands and curb side areas all over the cities. Municipal authorities already feel obliged to react to the boom: Shanghai, for instance, is working on new rules to **regulate the industry**.

The boom in bike sharing is just one aspect of the rapid development of e-commerce and the sharing economy in China. International companies have started to take note: Investors at Mobike include the Chinese internet giant Tencent, the American private equity company Warburg Pincus and Foxconn Technology Group. Ofo gets support from the Russian internet investor Yuri Milner, the ride sharing company Didi Chuxing and the smartphone manufacturer Xiaomi. Since January 1st 2017, the Chinese bike sharing market has attracted \$800m in investments. But the competition is also getting on its bikes:

Several start-ups like Shanghai-based Xiangqi put their money on e-bikes. All up there are now over 20 companies in China offering bike sharing services. The biggest firms have announced plans to expand abroad: Mobike recently started a bike sharing scheme in Singapore and says it plans to offer its services in 100 cities **worldwide**. Ofo wants to introduce its bikes to several US cities by the end of the year.

Mirjam Meissner, head of the research program Economy & Technology at MERICS: *“The Chinese bike sharing market is currently in the middle of a price war – similar to the price wars in the past between the taxi apps Didi Chuxing and Kuaidi Dache. Whoever wins in China is likely to o shake up the global bike sharing market in the future.”*

News in brief

- E-mobility: **Tencent acquires stake in Tesla**
- Balancing act: **Chinese central bank raises interest rates**
- Stimulus package: **Taiwan announces \$29bn to boost export-driven economy**

MAD MERIX

Chinese park goes high tech to stop toilet paper bandits

Progress in digital technology doesn't even stop at public toilets in China. The popular Temple of Heaven park in the south of Beijing **has installed facial recognition technology to stop toilet paper theft**. In the past, the bandits proved an elusive bunch. Hidden in back packs and shopping bags they smuggled sheet upon sheet of toilet paper past the security guards at the park's entrance. Now every visitor to the public toilets is screened.

Public restrooms in China have a unique feature: Visitors take toilet paper from a central dispenser before proceeding to the cubicles. In the Temple of Heaven park, they now first have to stare into a computer mounted on the wall for a few seconds. The machine then dispenses a sheet of toilet paper, exactly 60cm long. If visitors require more, they are out of luck. The machine will not dispense any paper to the same person for nine minutes.

For the park's visitors the new machines are a mixed blessing: A mother, whose child was too small to reach the camera, had to share her toilet paper with her offspring. The machine also does not hand out extra paper for drying hands. But park director Lei Zhenshan is happy about the new technology: He says toilet paper theft and extravagance has been reduced by 70 per cent.

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