China’s 2019 Negative Lists

JULY 10, 2019

China’s National Development and Reform Commission (NDRC) and Ministry of Commerce (MOFCOM) as expected published three lists on foreign investment on June 30: a revised negative list applicable to the country as a whole (the 2019 Negative List); a revised and less restrictive negative list applicable to China’s pilot free trade zones (the 2019 FTZ Negative List); and a list of sectors in which foreign investment is encouraged, i.e., eligible for investment preferences as a general rule (the 2019 Encouraged List). The three new lists replace earlier editions, i.e., the 2018 negative lists and the 2017 encouraged list, respectively, and all take effect on July 30, 2019. The 2019 Encouraged List is divided into two parts: the first applicable throughout the country, and the second applicable on a province-by-province basis to the less-developed central and western regions of the country, which now applies to the northeast region as well.

The new lists on the whole mark relatively modest additional actions to open China’s economy wider to foreign direct investment.

The 2019 Negative List reduces from 48 to 40 the number of sectors in which foreign investment is subject to restrictions:

- The requirement for control by the Chinese party, i.e., majority Chinese ownership, is removed for domestic shipping agencies, the construction of urban gas and steam pipelines in cities with a population of half a million or more, the construction and operation of movie theaters, and performance brokers;
- The 50% foreign equity cap on three categories of value-added telecommunications services (VATS), i.e., domestic multiparty telecommunications, e-storage and forwarding, and call centers, which had previously been lifted in some pilot free trade zones and Beijing, is now lifted entirely, allowing up to 100% foreign ownership throughout the country (in addition to the lifting of the foreign equity cap on e-commerce in 2018);
- The joint venture requirement in oil and natural gas exploration and development is lifted;
- The prohibition on foreign investment in the mining of molybdenum, tin, antimony and fluoride is lifted;
- The prohibition on foreign investment in the production of Shuen paper and calligraphy brushes is lifted;
- The prohibitions on the development of wildlife and plants and resources protected in the

country of origin are lifted.

While the foreign equity cap (50%) remains for automobile production, the 2019 Negative List and 2019 FTZ Negative List continue to set out a timetable to lift such a cap (allowing 100% foreign ownership in commercial vehicle production by 2021 and 100% foreign ownership in passenger vehicle production by 2022).

The 2019 FTZ Negative List reduces from 45 to 37 the number of sectors in which foreign investment is subject to restrictions. These include restrictions on investment in fisheries (including aquaculture) within China and in China's territorial waters.

In a press conference held on the same day, NDRC officials stated that the promulgation of the new lists echoes President Xi's promise at the Osaka G20 Summit that China will continue to reform and open up. The negative lists in the future will continue to remove, rather than add, sectors where foreign investments are restricted. For sectors not included in the negative lists, foreign and domestic companies will receive equal treatment with respect to market access. The negative lists are expected to be updated annually and, once promulgated, will constitute an integral part of China's new Foreign Investment Law.

While some of the relaxations of restrictions on foreign investment will be welcomed, such as in some VATS sectors and oil and natural gas exploration and development, on the whole the narrowing of the two lists is relatively modest. Contrary to Premier Li Keqiang's remarks at the Boao Forum in March on further opening up of healthcare institutions to foreign investment, the biggest disappointments may be the failure to lift the 70% cap on foreign investment in healthcare institutions (a reform in a rapidly growing industry that had been publicly contemplated). In other words, healthcare institutions will still need to be structured like Sino-foreign joint ventures even after the joint venture laws no longer exist after the Foreign Investment Law takes effect next year. Other disappointments include the failure to open more VATS sectors to majority and ultimately 100% foreign ownership. Moreover, while 100% foreign ownership is newly allowed in some VATS sectors under the 2019 Negative List and the 2019 FTZ Negative List (domestic multiparty telecommunications, e-storage and forwarding, and call centers), many free trade zone administrations and local governments have yet to receive detailed guidelines on implementation. With respect to oil and natural gas exploration and development, there are existing rules mandating foreign investments through equity or cooperative joint ventures or programs with Chinese partners. How these rules are to be reconciled with the 2019 Negative List remains to be seen. Finally, some of the relaxations apply to sectors, such as calligraphy brushes, in which there is limited if any growth and limited foreign appetite.

However, at Summer Davos on July 2, just two days later, Premier Li Keqiang went beyond the negative lists by announcing that the foreign equity cap in the securities, futures and life insurance sectors, previously raised from 50% to 51% and scheduled to be lifted entirely in 2021, will now be lifted entirely in 2020, a year earlier. Premier Li also stated that there will be further but unspecified reforms in the value-added telecommunications services and logistic sectors that were not included in the 2019 Negative List.

The additions to the 2019 Encouraged List focus on China's economic priorities and may be divided into two categories: manufacturing and services. The manufacturing additions correspond closely to several of the priorities previously listed in the Made in China 2025 program, which is no longer publicized because it has become a 'red flag' to foreign governments and businesses. The encouraged categories include information technology (5G core components, IC etching machines, chip packaging equipment and cloud computing devices), manufacture of equipment (industrial robots, new-energy vehicles and key components of smart cars), modern pharmaceuticals (key raw materials for cellular therapy drugs and large-scale cell culture products) and new materials (aerospace new materials, monocrystalline silicon and large silicon wafers).

The service sector items are business services (engineering consulting, accounting, tax, inspection and testing certification), trade and circulation services (cold chain logistics, e-commerce and special railways) and technical services (artificial intelligence, clean production, carbon capture and the circular economy).

Encouraged sectors in less-developed regions vary across agriculture, industry and services.

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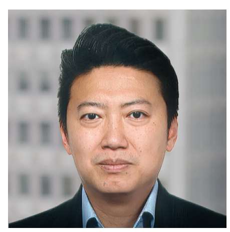

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