

Financial Considerations To Help You Succeed In Doing Business With China

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Considering China?

- ▶ Things to consider in order to succeed
 - ▶ Visibility of your supply chain
 - ▶ Do you know your Chinese counterparties?
 - ▶ Look for ways to unlock your cash
 - ▶ Consider the RMB
 - ▶ Making the jump into China

Visibility Of Your Supply Chain And Your Counterparties

Exporting & Sourcing

China is less and less about cheap labour and more about selling to China's domestic market

China will still lead in many industrial verticals

But

- ▶ Are you still competitive selling or buying? – move west, move out
- ▶ Is your existing supplier really your supplier? - have you done an audit? In person?
 - ▶ **CSR considerations – pollution, safety, security, labour**

Agents and Suppliers

- ▶ Where to find them?
 - ▶ Internet? – verified only means the company exists
 - ▶ Trade Shows – better - a limited pool found outside China
 - ▶ Industry referrals, DFATD assistance
- ▶ Due diligence needed before selecting your agent and supplier
 - ▶ One Agent for all China? Who is he/she representing? The Guanxi oversell
 - ▶ Sourcing Agents – commission based
 - ▶ DFATD, Industry colleagues, CCBC, Chinese Business Research Agencies, Administration of Industry and Commerce
 - ▶ Get on the Ground!
- ▶ Multiple samples before you buy, negotiate quality standards and penalties for slippage in delivery and quality, change & rush orders

Payment – Protect Yourself

Exporting:

- ▶ Receivable Insurance is used in more than 90% of EDC supported export contracts
- ▶ Terms typically up to 90 days but can be longer
 - ▶ **Issues:**
 - Good buyer relationships are critical. Some buyers have refused or frustrated payment (even on L/C terms against confirmed docs) when commodity or input prices fluctuated during shipment or during a long manufacturing period
 - Appetite for margining of receivables varies across banks in Canada

Buying: Avoid unsecured methods/ Expect LC requests - Sinasure

Unlock Your Cash

Don't forget that insured receivables may be marginable

Talk to your bank!

More capacity for your operating lines in Canada

Bid, Advanced Payment and Performance bonds all part of a typical Chinese contract when exporting – you will need to post SBLC's

- ▶ Performance bonding on holdback amounts can be at risk since Chinese buyer may wish to reopen the contract to negotiate additional product/spare parts/ training etc.
- ▶ Wrongful call – 100% coverage
- ▶ Rightful call – 95% cover if outside the exporter's control

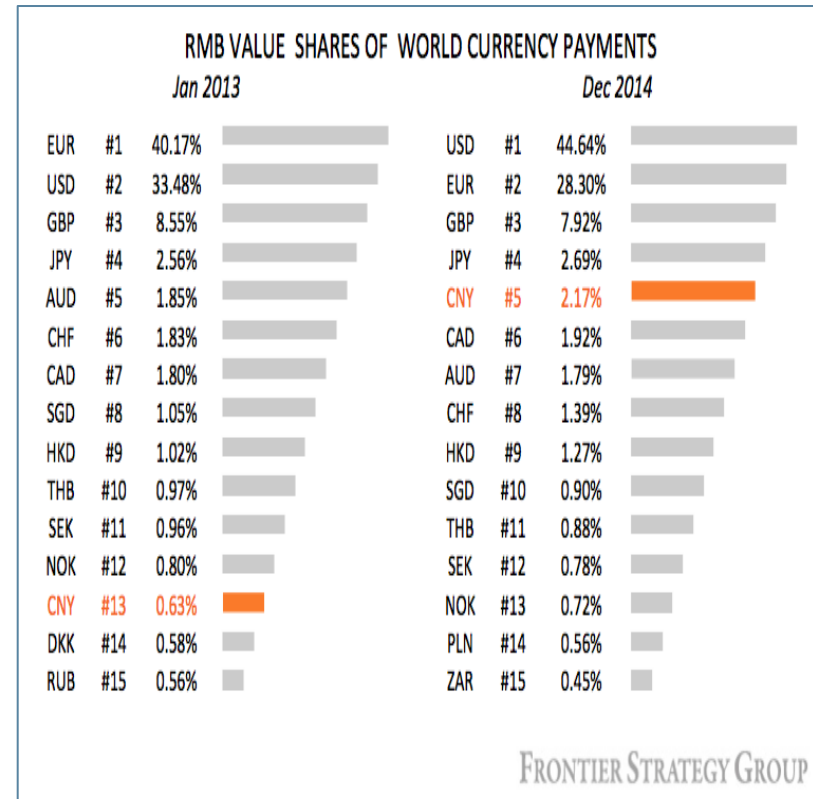
RMB Internationalization

Launch in March of the Canadian RMB Clearing Hub for Americas

Facilitates easier access and settlement of trade payments in RMB

Coming Soon.....
China International Payment System (CIPS)

Capital Account Relaxation



RMB As Payment - Considerations

- ▶ Direct conversion advantage: the Canadian clearing bank makes the trade faster and more transparent. Once direct CAD-CNY trades are permitted, there will be an additional savings.
- ▶ FX transaction fees: when the Chinese buyer pays in RMB they no longer have to take on the FX transaction costs,
 - ▶ between 0.5-2.5% depending on a variety of factors: transaction size, amount of recurring business, banking relationships, etc.
- ▶ Convenience: many Chinese buyers do not have USD liquidity and need to work through FX agents within China. Added cost.
- ▶ FX risk: when the Chinese buyer pays in RMB they no longer have to take on the FX risk, which can vary between depending on the term and market volatility.
- ▶ Natural Hedging

Buyer Financing

Be aware that China's FX regulator (SAFE) prohibits most Chinese companies from obtaining a hard currency loan from outside China

This includes RMB located offshore

Some exceptions:

Strategically important SOEs and national priority projects may have approval

Buyers in the Shanghai FTZ

If buyer asks – a potential sign of credit distress of the buyer or simply a request for longer payment terms under LC or open account

Moving into China

FX regs affect foreign JVs and wholly owned foreign enterprises as well

Borrowing Gap Headaches

- ▶ Cdn investors need to work closely with an experienced LOCAL lawyer and tax consultant and bank to ensure proper affiliate licensing and debt strategy
- ▶ BIG issue affecting companies in China that didn't structure their investment well and expected to use external debt to fund and grow their China based operations

This is a fundamental transition period in China's FX regime so anyone thinking to business with or invest in China consult your bank, local lawyers and the Canadian and Quebec Trade Commissioners Service

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