China
Opportunities and barriers to inbound construction

G20 rankings & data

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Financial metrics

- Total fiscal stimulus announced: £427bn
- Announced spend on construction in the next 3 years including fiscal stimulus to construction: £109.2bn
- Construction industry value – 2009: £240bn
- Main corporate tax rate: 25%

Construction sector metrics

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<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
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<tr>
<td>Construction industry value, £bn</td>
<td>204</td>
<td>240</td>
<td>271</td>
<td>299</td>
<td>331</td>
<td>362</td>
<td>393</td>
</tr>
<tr>
<td>Construction industry, real growth, per cent y-o-y</td>
<td>10.3</td>
<td>9.9</td>
<td>7.9</td>
<td>7.2</td>
<td>7.0</td>
<td>5.9</td>
<td>5.0</td>
</tr>
<tr>
<td>Construction industry, per cent of GDP</td>
<td>7.7</td>
<td>7.5</td>
<td>7.6</td>
<td>7.8</td>
<td>7.8</td>
<td>8.0</td>
<td>8.1</td>
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BDO review of tax

- Amongst the lowest headline tax rates
- Relatively stringent thin capitalisation restrictions
- Tax depreciation available on buildings and other capital costs at competitive annual rates
- Withholding tax regime may add to overall tax burden of overseas companies providing services to the Chinese construction sector

Overall scoring: 7/10

3= out of the G20

BDO ease of doing business

There are many significant barriers and inbound construction activity will find it hard to do business

1 Very easy  2 Quite easy  3 Average  4 Quite difficult  5 Very difficult

Top construction firms

- China Railway Engineering Corporation
- Beijing Urban Construction Group
- China Railway Construction Corporation Ltd

The construction industry is dominated by some large state-owned construction companies and therefore relatively few opportunities are available for foreign construction companies. However, the contribution of these major state-owned enterprises to total construction output is being eroded by the recent influx of foreign contractors, encouraged by ongoing economic reforms.
“China offers a huge opportunity for inbound construction activity as its development continues. With extensive infrastructure and a multi-billion pound stimulus package demand is high for construction. However local construction firms are dominant and foreign players may find it difficult to move into some areas of China.”

Richard Kelly
Partner, Head of Construction

“With a relatively low headline corporate tax rate and potentially significant tax breaks in specific regional, technological and environmental arenas, the Chinese tax system for the construction sector has a number of attractive features.”

Stephen Herring
Tax Partner, Real Estate and Construction

Opportunities and barriers

Ranked 4th overall in our G20 heatmap, despite a challenging environment for inbound companies, the scale of opportunity in China is impressive.


In 2007, the Chinese construction sector witnessed significant large-scale development activity with a large number of foreign and local companies contributing to new project development. Growth was recorded in the areas of construction and expansion of airports, ports, rail and road networks, power projects, oil pipelines and allied infrastructure – key drivers having been the events of the 2008 Olympics in Beijing and the 2010 Shanghai World Expo. Growth in tourism leads to a rise in new hotels, resorts, public transport systems and commercial complexes. The government supports the construction and development of airports by granting permission to airport authorities to collect airport fees.

In November 2008 the Chinese government announced an economic stimulus package worth £427bn as a means of boosting the domestic economy. Infrastructure will receive a substantial portion of the package with rail being a key area of focus. While still offering enormous growth potential the infrastructure sector in China is maturing and this is expected to result in slower growth rates. The massive building programmes of the past years cannot be overlooked when forecasting future growth in the sector.

The Chinese government will employ substantial resources for the expansion and upgrading of the rural road network in the country. During the 11th five-year plan period (2006-2010) alone, more than 1.2m km of rural roads will be built or renovated.

Chinese investment in the development of railway infrastructure in the period 2006-2010 is likely to be to the tune of £95.4bn (£190.8bn, an average of £47bn) of investments annually. In that period, the country plans to add 17,000km of railroad, of which 7,000km will cater exclusively to passenger transport. Moreover, 15,000km of electric railroad will be constructed.

Some of the investments will be brought forward in 2009, as part of the government’s stimulus plan. In 2009 the government has earmarked £63.9bn for spending of railways, exactly double the amount invested in 2008. This will see the construction of a total of 5,150km of lines and bring five new passenger lines into operation, among other projects.

Barriers/challenges to construction activity

- Lack of trust in inbound construction companies and difficult tendering and project management requirements when dealing with government projects. (Majority of the top companies are state-owned).
- Local construction companies have great price advantages resulting in strong local construction industry with dominant control of the market.
- Poor labour conditions, high levels of corruption and a deficient legal system remain as China’s key structural problems plaguing its business environment. These concerns, combined with China’s immense bureaucracy, are significant challenges for inbound investment.

BDO viewpoint and advice

Pitfalls to avoid when doing business in China

- Due to the significant differences in respect to construction approach, inbound construction companies may find it difficult to accept and meet certain requirements applied in China.
- Government regulation can be complex, and some regional authorities may be unwilling to admit non-local players.

Practical advice for inbound construction activity

- Understanding the deep regional differences and complex government structure is essential for inbound construction activity. The key is to identify what is on the table and verify incentives with independent advisers.
- Forming strategic relationships with existing players is necessary in this market especially with government derived projects.
- Regarding the regulatory and competitive landscape, China’s construction industry remains quite protected. State-owned companies drive the construction sector in China.

- There are about 9,000 state-owned construction corporations, compared with just 400 foreign-owned firms doing business in the country. Foreign-owned construction companies are allowed to form joint ventures and are eligible to bid for works that are entirely foreign-funded or for projects that local companies are unable to undertake. However, the government does not allow foreign-owned enterprises to undertake design, construction or consulting alone.
- It is estimated that about £36.4bn worth of construction projects are open to foreign-owned companies every year, mainly in transport and water infrastructure. Key locations for construction spending are Beijing, Shanghai and the western provinces.

Useful tax and other incentives for inbound construction activity

Main depreciation rates:

- Tax depreciation must be claimed annually on a straight line basis based upon prescribed periods: Buildings – 20 years, Appliances, tools etc. – 5 years, Road vehicles – 4 years, Electronic equipment – 3 years.
- China offers a range of incentives to businesses. The regular corporate income tax rate is reduced in various economic, technology or special development zones. Incentives are offered based on industries and transactions, on business tax, value added tax, customs duty and other transactions tax. Local governments usually offer fiscal subsidies and tax refunds.

Sources

