Central bank trials financial reform

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Night view of the entrance to the China (Shanghai) Pilot Free Trade Zone Photo: IC

China's central bank issued a guideline Monday for financial support in the new China (Shanghai) Pilot Free Trade Zone (FTZ), with the aim of promoting the yuan's convertibility under the capital account and expanding cross-border usage of the currency.

Residents in the FTZ will be allowed to open free trade accounts, which will allow both local and foreign currency transactions, investment in overseas securities markets and transferal of income earned in the FTZ to offshore accounts, according to a statement released by the People's Bank of China (PBC) on its website.

Companies registered in the FTZ will be allowed to invest in the securities and futures markets in Shanghai, and their overseas parent companies will be allowed to issue yuan-denominated bonds in the mainland, the statement said.

The guideline included 30 detailed instructions, and aims to push forward liberalization of interest rates and deepen reforms of foreign exchange management, according to the central bank.

"Allowing free trade accounts is a highlight, which will promote cross-border capital flows, and the central bank is also strengthening supervision to curb speculative capital inflows," Xu Hongcai, director of the Department of Information under the China Center for International Economic Exchanges, told the Global Times on Monday.

The guideline reflects the PBC's long-held strategy of pushing for financial reforms whenever and wherever possible, and to force reforms in the domestic financial sector through opening-up, Barclays said in a research note released on Monday.

"The PBC's move is within our expectation that the liberalization process will occur in a controlled and gradual manner, but is lower than some market expectations, especially in terms of liberalization of interest rates," Chen Bo, an international economics professor at the Shanghai University of Finance and Economics, told the Global Times on Monday.

The central bank will remove the deposit rate ceiling for accounts with a small amount of foreign currency when the conditions are ripe, according to the statement.

The PBC removed controls on lending rates in July, and lifting controls on deposit rates is seen by analysts as the final step toward the full liberalization of interest rates.

"If the central bank liberalizes interest rates in the FTZ in a more aggressive way, it will lead to interest rate arbitrage," Chen said.

The PBC seems to be aware of potential risks from "opening too much" and remains cautious on aggressive capital account opening and interest rate liberalization, ANZ Research said in a research note sent to the Global Times on Monday. The PBC still wants to safeguard onshore financial stability, it noted.

The Shanghai FTZ, which was officially launched on October 1, is seen as a test ground for China's economic reforms. As of November 22, 1,434 companies had registered in the FTZ, but among them only 38 are overseas-funded, according to the latest data released by the administrative committee of the FTZ.

Tax extension offered

Companies registered in the Shanghai FTZ are to get an extension for paying their tax bill for non-currency asset outbound investment, an official statement said Monday, in a fresh sign of support for the FTZ.

The new policy allows companies in the FTZ to pay in regular annual installments when settling their enterprise income tax on gains from asset reorganization through non-currency asset outbound investment, said the joint statement by the Ministry of Finance and the State Administration of Taxation on Monday.

The payment extension is offered for a period of no more than five years. The extension will be canceled if companies transfer or withdraw their outbound investment within five years.

Also, companies who fold up their businesses within five years will cease to be eligible for the policy.