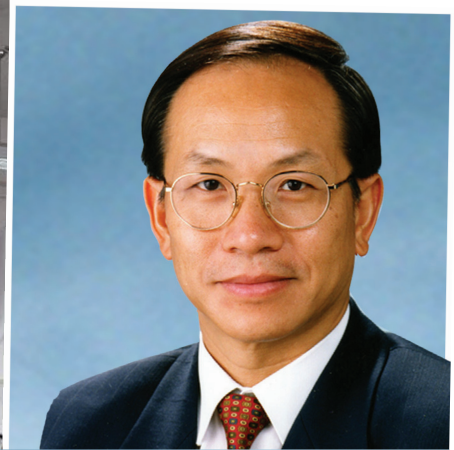

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China's Common Prosperity Goal

End of Capitalism?

Beijing has launched a sweeping overhaul of its education sector that includes banning private companies from teaching the school syllabus during weekends and vacations, and from making a profit, among a host of other restrictions.

As Beijing turns its focus on edtech, after a sudden and shocking crackdown on the nation's Big Tech, it is important to recollect how it all began. The readers may recollect from my article "Behind Beijing's Big Tech Crackdown", which appeared in this magazine's September 2021 issue, that it all started with the perception amongst the authorities that the Big Technology firms might have grown their boots!

That may not be totally uncalled for though. A look at the China tech sector will show that some of the Mainland's giant tech conglomerates have indeed morphed into national oligarchs. They are cannibalizing smaller competitors, spreading socially-destabilizing financial risks, and defying regulatory capacity to catch up with them. Concentration of businesses in fewer hands magnifies the nation's already serious economic inequality, threatening to destabilize the country.

Bolstered by their success at reining in Big Tech, the authorities now turn their attention to edtech as they feel that their rise has not done any good to the education sector, and instead set it back by several years. In the first ever crackdown on the technology firms operating in the segment, the regulators have introduced a set of guidelines to ease the burden of excessive homework and off-campus tutoring for students undergoing compulsory education. It does not take much to understand that commercial private tuition increases the financial and study burden on China's hard-pressed students, who are trapped in the fiercely-competitive National Higher Education Entrance Exam (*高考 Gao Kao*) that determines entry to better universities, and by ex-

New Regulations for China's Education Sector

The sector had attracted billions of dollars because it had been expected to generate 491 billion yuan ($76 bn) in revenue by 2024. Those lofty expectations groomed a generation of promising startups like Yuanfudao and Zuoyebang. It's a stunning reversal of fortune for an industry that had emerged as one of the hottest investment plays in China in recent years. Alibaba, Tencent and ByteDance Ltd. were among the big name backers, along with the overseas players like Tiger Global Management, Temasek Holdings Pte and SoftBank Group Corp. The new regulations are in a nutshell:

- Companies and institutions that teach the school curriculum must go non-profit
- Such institutions cannot pursue IPOs, or take foreign capital
- Listed companies will be prohibited from issuing stock or raising money in capital markets to invest in school-subject tutoring institutions, or acquiring their assets via stock or cash
- Foreign firms are banned from acquiring or holding shares in school curriculum tutoring institutions, or using Variable Interest Entities (VIEs) to do so. Those already in violation need to rectify the situation
- All vacation and holiday curriculum tutoring is off-limits
- Online tutoring and school-curriculum teaching for kids below six years of age is forbidden
- Agencies cannot teach foreign curriculums or hire foreigners outside of China to teach

Courtesy: Bloomberg

tension, chances for a better life. The dice is loaded in favor of kids of richer families able to afford high private tuition fees.

An added, yet important, side effect is aggravating the prevalent disincentive to raise a family or to have more than one child. This exacerbates the country's worsening demographics, making it more likely that China will get old before becoming rich.

The private tuition sector has been highly corporatized, with the bigger behemoths offering sky-high salaries to attract the best teachers from government and other private schools. The outcome is that corporatized commercial schools tend to monopolize the best teachers, which in turn enables them to charge higher fees. Some schools may be colluding with these enterprises by reserving certain competitive topics to be taught through private tuition.

Parents keep the pressure up by overloading students with extra tuitions and paid extra-curricular lessons such as in violin, ballet, and sports, for fear that they may be outcompeted by the Joneses. This creates social mores of "educational snobbishness", worsening the sense of inequality in a country governed with socialist principles.

What is more, it leads to an unhealthy phenomenon of 'force-fed' students, pejoratively referred to as 'chicken babies' (*鸡娃 Jī wá*), spawning a generation of tired and frustrated youth. Added to a school system obsessed with examination results, students' healthy, all-round development is called into question.

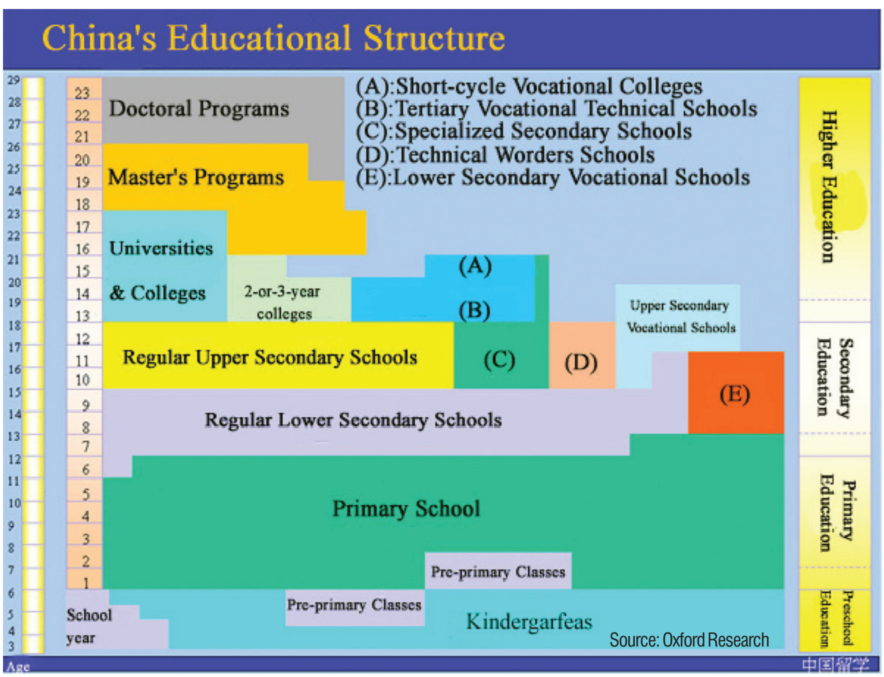
Published in my previous article is a Timeline showing the wider sectors affected by the Big Tech crackdown: "FinTech, e-Commerce, Education, Ride-hailing, Social Media and User-generated Video, Music, Literature and other IPR; Gaming, e-Cigarettes, and Insurance". Virtually, all of these categories are widely accessible to students. When misused in frustration, they could potentially divert their occupation or even 'corrupt' their morals.

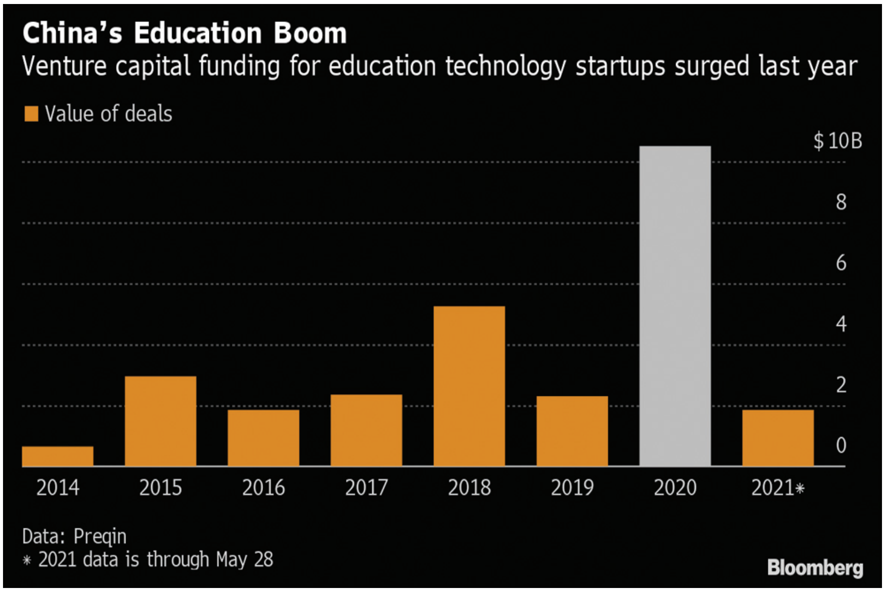
A case in point is the authorities' recent censorship of adoration of popularized pop models and 'sissy males', as reported in the *South China Morning Post* of September 10. Tencent, China's iconic multinational tech giant, is now on cue, restricting how much time and money youngsters can spend on its online gaming platform.

All of these strictures reflect the country's imperative to realize the China Dream of becoming a "strong, democratic, civilized, harmonious, and modern socialist country" by 2049, the hundredth anniversary of the founding of the People's Republic of China. A key theme of this centenary goal is "Common Prosperity".

In the "Opening Up and Reform" drive in 1978, Chinese Leader Deng Xiaoping sounded a clarion call "to let a small proportion of people get *rich* first". Since then, China has never turned back.

According to *Forbes*, mainland China has now 626 dollar-billionaires, the second highest number in the world. There are also 5.28 million dollar-millionaire households. 50% of all families have a household income from $22,400 to $48,000. In 2020, the wealthiest 1%





of Chinese people held 30.6% of the country's wealth, up from 20.9% two decades ago, according to a Credit Suisse report. For comparison, in the US, in the first quarter of 2021, the share of the top 1% increased from 23.5% of total net wealth to 32.1%.

On the other hand, according to Premier Li Keqiang, China still have 600 million people with average monthly income of about $160. China's Gini coefficient (a measure of inequality that ranges from 0 to 1) has reached 0.47. By comparison, that of the US is around 0.41.

Except a minority of self-made millionaires, the good life seems to elude a whole generation of fresh university graduates, now numbering some nine million a year. Big bosses, including Jack Ma of Alibaba, embrace the so-called "9-9-6" work culture—everyday work from nine in the morning to nine in the evening, six days a week. Limited promotion opportunities, relentless competition in the private sector dominated by big enterprises, and increasing costs of housing in big cities where the better-paid jobs are, all add to youth frustrations, let alone financial hurdles to raise a family. Many are debating whether to press on (euphemistically referred to as 内卷 – curling inwards) or to give up (躺平 – lying flat).

Chinese leaders have insisted a number of times that inequality above 0.40 is potentially destabilizing, as reported by Branko Milanovic in *Foreign Affairs* of 11 February, 2021. He also predicted in his article that the oligopolies resulting from decades of mixed capitalism could only be tackled by the government as their creator in the first place.

Beijing is now rising to the challenge

The above 'crackdown' or course-correction signifies that 'Common Prosperity' is being achieved through a three-pronged economic redistribution.

The first is poverty eradication. After lifting 800 million Chinese people out of poverty, representing 60% of the global total, China now claims to have lifted all of its people out of extreme poverty, using the poverty line of $2.30 a day, slightly above the World Bank's lowest threshold of $1.90. Nearly everyone completes compulsory schooling, matching the average level in high-income countries. There is almost universal access to electricity and safe drinking water. The child mortality rate has plummeted, according to the UN.

The second prong is rejigging the economic model from excessive dependence on exports and capital investments, which tend to favor large enterprises, to a more balanced and higher-quality model towards services, domestic consumption, and the ecology, which shares the cake more evenly.

This shift is reflected by the new 'Dual Circulation' economic strategy, setting greater store on the domestic economy, including grassroots consumption, self-reliant high-technologies, the green economy, including such items as new-energy vehicles, and interconnectivity with external trade

Understanding the Variable Interest Entities Structure

In a typical Variable Interest Entities (VIE) structure, a holding company is established in an overseas jurisdiction (e.g., the Cayman Islands) to issue shares to overseas investors. The offshore holding company, through one or more wholly-owned subsidiaries in China, enters into a set of control agreements with a China-based operating company which is typically set up as a 100% Chinese-domestically-owned company in order to retain requisite operating licenses or approvals in industrial sectors for which foreign investment or ownership is restricted. As such, a VIE structure essentially allows the overseas holding company to exercise control over management, financing and operation of the China-based operating company through contractual arrangements even though the overseas holding company does not hold any equity in the China-based operating entity.

Although the VIE structure sits in a grey area of Chinese law, as a practical matter, the Chinese government has been reluctant to take actual enforcement actions against such structure in the two decades since Sina Corporation completed its IPO in the US using a VIE structure for the first time. Although the opinions prohibit foreign investors from investing in 'subject-based' training institutions through mergers and acquisitions or VIE structures, it does not necessarily mean that the government has changed its position on the VIE structure itself. Rather, the opinions suggests that the Chinese government recognizes the VIE structure as one of the ways for foreign investors to invest in restricted sectors.

As for the VIE structure, it is reported that the Chinese government views VIEs as a necessary and vital part of how Chinese firms engage with global markets. We remain reasonably confident that the government will continue to maintain the status quo of the policies on the VIE structure, at least in the near term, although the suddenness of regulatory restrictions on particular industries has increased investor caution.

Courtesy: jdsupra.com

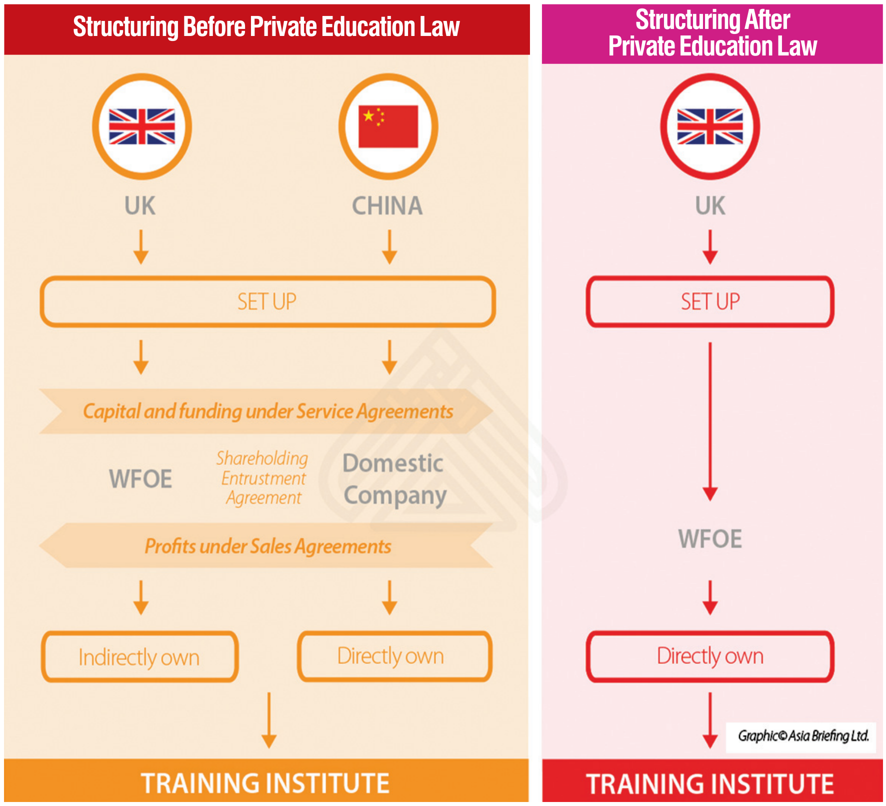
and exports.

Government spending will also shift more towards equality instruments like education, housing, and welfare, reducing the barrier to child-bearing, an important remedy for the nation's worsening demographics.

Additional measures to enhance productivity include gradual extension of the retirement age, promoting the use of robotics, a digitized economy, and expanded urbanization by doubling the world's most extensive high-speed rail system to 70,000 km over the next 15 years. This will connect all cities over half a million people, while an additional 200,000 km of modern railway will connect all towns, however remote, of 200,000 people and above.

Added to this is a new "Third Child Policy" to encourage fertility. Meanwhile, a reformed household registration system (*hukou*) is beginning to turn millions of village migrants into full citizens, hopefully ushering in an even larger middle-class in the coming decades.

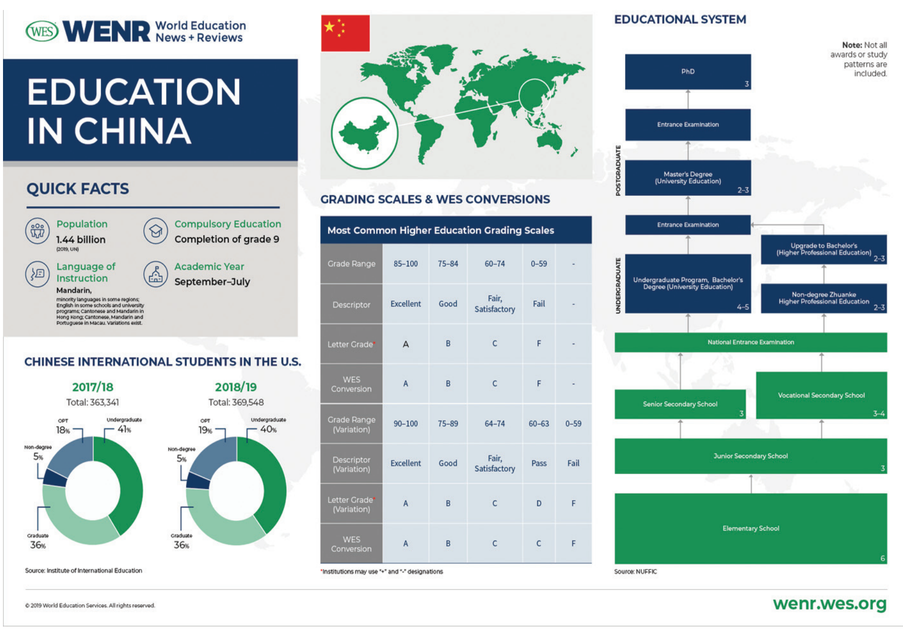
China has about 400 million people living on income between $15,000 and $77,000 for a family of three. This number of middle-class consumers is to double to 800 million people in about a decade, according to the Development Research Center, a think-tank attached to China's State Council. The ultimate aim is to create an "olive-shaped" economic profile with fewer richer people at the top and far fewer poor people at the bottom with a huge majority in the middle.



The third prong is to expand philanthropy, not merely to dole out cash but to help more people to become economically self-reliant and to spread wealth-creating capacities. On cue, the giant Alibaba Group proposes to launch a $15.5 bn 'common prosperity fund' by 2025 in Zhejiang, the Group's home province, with ten initiatives, including investments in technology, supporting small businesses and fostering development in rural areas.

There were initial alarms in some quarters that 'Common Prosperity' may signal return to a 'communist' model of planned economy and coercive redistribution. President Xi and his team were quick to dispel such irrational fears with open elucidations. After all, why should China reverse course to a much less successful past?

Indeed, such initial fears are typical of misreading China from a fixated Western perspective, that the Chinese Communist Party (CCP) leopard cannot change its spots. This fails to realize that the CCP has become highly adaptive in tune with the times, serving the Chinese people much better than the performance of many Western democracies, according to a Harvard Kennedy School Ash Center report of July 2020. ■



Grade Range	85–100	75–84	60–74	0–59	-
Descriptor	Excellent	Good	Fair, Satisfactory	Fail	-
Letter Grade*	A	B	C	F	-
WES Conversion	A	B	C	F	-
Grade Range (Variation)	90–100	75–89	64–74	60–63	0–59
Descriptor (Variation)	Excellent	Good	Fair, Satisfactory	Pass	Fail
Letter Grade* (Variation)	A	B	C	D	F
WES Conversion	A	B	C	C	F

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