6.7. Exchange Rate Implications (RC)

Introduction

As a foreign owned entity, you will be influenced by the exchange rates for your imports, exports, dividends and also services. In the past the US Dollar has been pretty stable compared to the Chinese Renminbi, but lately the tendency towards more volatility is increasing.
In the year 2017 the exchange rates for

- USD to RMB changed around 5% and
- EUR to RMB changed around 8%.

If you have therefore a choice regarding the currency you should consider which one might be the less volatile in the near future.

Planned Exchange Rate vs. Real Exchange rate

To provide a stable calculation basis, international companies often define planned exchange rates and base their operations on them. Due to the volatility of the exchange rate markets, they do often not match with reality though and sudden unplanned events can heavily influence the tendency:

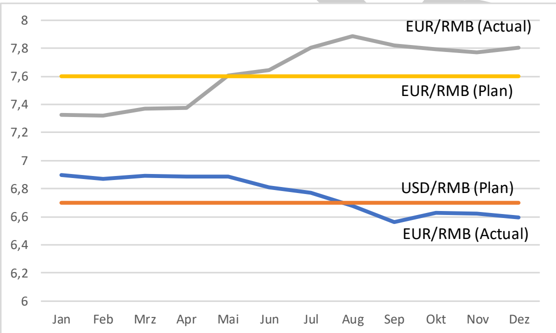

Figure 9: Exchange Rates deviation from plan rate

Pricing systems often are maintained with one base currency, e.g. Euro, and depending on the sales currency they calculate the sales price based on the plan exchange rate.

Relevancy for Intercompany business

For intercompany pricing from a group perspective there is no big influence if we neglect possible influences on taxes and fees. For deviations between the plan exchange rate and the actual exchange rate, it just moves around money within the group as exchange rate losses or earnings. Example:

- Plan Exchange Rate is 1 EUR = 10 RMB
- Actual Exchange Rate is 1 EUR = 7 RMB.
- One good that is priced with 10 EUR will be sold to the Chinese company with the plan exchange rate:
  10 EUR * 10 RMB/EUR = 100 RMB.
- As a comparison, if the actual exchange rate would be used, this would equal
  10 EUR * 7 RMB/EUR = 70 RMB.
- The price difference between both types of calculation is 30 RMB.
- When using the plan exchange rate to calculate the sales price, the Chinese company has to pay 30 RMB more than with the actual rate and therefore has an exchange rate loss.
  When using the actual exchange rate, the influence on the local company is zero while the selling entity is receiving less than defined, leading to an exchange rate loss on their side.

As a summary, while the changing exchange rate is having an influence on the total performance of the group, it does not matter if the planned exchange rate or the actual exchange is used since with this the exchange rate earnings or losses just get moved around within the group.

Relevancy for external business

This changes though as soon as you start selling goods to external customers since this will lead to money inflow or outflow of the group. When you are doing business in foreign exchange with third parties, you should ensure that a reasonable exchange rate is being used during calculation since this will directly influence your operations result.

Common pitfalls and tips

- If a company offers you two different currencies to pay for their services or products, ask for both prices.
  Depending on their internal pricing system you might be able to get a serious

discount when their plan exchange rate deviates from the real exchange rate a lot.

- SAP usually uses one or several price tables for pricing and all prices are maintained in one currency. Be aware of the risks that you bring to yourself regarding low-margin products if you choose that the conversion should be based on standard exchange rate.

7. Company Taxation

The taxation of companies in China is in a constant development: Most recently the change from business tax to VAT is one of the driving topics, but also other tax changes e.g. regarding the change of the general VAT rate from 17% to 16% in 2018 that was suddenly announced and implemented within just a few weeks can have an ongoing influence on your company.

This chapter will focus on the most common taxes, e.g.:

- Corporate Income Taxes
- VAT and VAT Surcharges

Additionally, it will give you an outlook on different ways for profit repatriation to the shareholder of your company by using commonly used approaches.