Journal of the European Union Chamber of Commerce in China

EURObiz

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November/December 2016

SMEs

WHAT GOT YOU HERE WON'T GET YOU THERE
Corporate entrepreneurship in China

THE TOOLS TO THRIVE
Providing effective support to SME globetrotters

STARTING SMALL, THINKING BIG
Building a better platform for SME growth

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SMES IN CHINA:
NEW OPPORTUNITIES AND OLD CHALLENGES

Jörg Wuttke
President of The European Union Chamber of Commerce in China

The European Chamber has long advocated for the interests of European SMEs in China. In the EU they are important sources of employment – over the past five years, SMEs have created around 85 per cent of new jobs and provided two-thirds of total private sector employment.[1] Improving the business environment for SMEs in China should therefore be prioritised accordingly.

To its credit the Chinese Government *has* begun to pay more attention to SMEs in recent years, as it works to foster new drivers of economic growth and employment. For example, in September 2015, Prime Minister Li Keqiang announced the establishment of a National SME Development Fund with euro (EUR) eight billion of capital,[2] with the first sub-fund dispersing EUR 36 million to 14 projects by the end of August 2016.[3] Unfortunately, it is still unclear whether or not European companies will be able to participate in this fund; by contrast, Chinese investors that take stakes in European SMEs are very much eligible for EU funding for R&D.

The revised draft of the *SME Promotion Act*, which was released on 31st October, 2016, addresses some of the issues faced by EU SMEs. These include problems related to late payments; access to finance and non-banking finance; alleviation of administrative burdens; improving coordination of different government departments; protection of intellectual property rights at the local level; and their exclusion from public procurement processes. Ensuring that these issues remain in the final text of the *SME Promotion Act* would go some way towards establishing a business ecosystem in which SMEs can thrive.

These issues do not just pose challenges for European SMEs in China, though. They also seriously impact the ability of domestic Chinese SMEs to succeed, especially in industries where the dominant position of state-owned enterprises prevents them from gaining market access. As we see with Germany's 'hidden champions', SMEs are often technological leaders in their field. Denying them the opportunity to fully participate in the market therefore has direct implications on China's ability to drive innovation. At a Chamber event in May 2016, an Assistant Director General from the Ministry of Industry and Information Technology (MIIT) implicitly recognised this when he noted that SMEs are major research and development (R&D) and manufacturing contributors, accounting for 25 per cent of all new products in the market.[4]

Eradicating this opportunity gap is extremely important for the future of China's economy. The Chamber's *Business Confidence Survey 2016* found that nimble SMEs are more optimistic than their larger counterparts regarding their operations in China, with fewer of them planning to cut costs here and more of them willing to make increased contributions. Therefore the faster that China's business ecosystem is improved, the sooner European SMEs will expand their local operations and R&D investments, take on additional hires and make larger tax contributions. The Chamber will continue to advocate on behalf of EU SMEs, to ensure that the National SME Development Fund and final text of the *SME Promotion Act* be used to turn the Chinese Government's admirable goals into reality.

To end on a personal note, as we ease towards the end of the year, the winter weather begins to bite, and, at least for me, the waistline is challenged by Christmas temptations, I would like to extend my warmest greetings of the season to all. I wish you a relaxing time with your family and friends and a happy and prosperous Year of the Rooster. According to the Chinese zodiac, roosters are loyal, honest, bright communicative and ambitious, characteristics that I hope will define the Chamber in 2017. In some cultures roosters are even thought to ward off evil spirits – something we could perhaps all do with as protectionist forces continue to gather… I look forward to seeing you all in good spirits in 2017.

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1 Entrepreneurship and Small and Medium-sized Enterprises (SMEs), European Commission, viewed 8th November, 2016,<http://ec.europa.eu/growth/smes>

2 *Li Keqiang chaired a State Council executive meeting*, State Council, 1st September, 2015, viewed 8th November, 2016, <http://www.gov.cn/guowuyuan/2015-09/01/content_2923201.htm>

3 The Scale of the First Sub-Fund of the National SME Development Fund has Reached a Scale of CNY 60 Billion, Xinhua, 29th August, 2016, viewed 8th November, 2016, <http://news.xinhuanet.com/fortune/2016-08/29/c_129261274.htm>

4 Taken from a speech delivered by Mr Zhou Pingjun, Assistant Director General, China Centre for the Promotion of SME Development (MIIT), during the *EU SME Annual Conference: How to Tackle a Changing China*, which took place in Beijing on 31st May, 2016.

TOEING THE PARTY LINE

China's 6th Plenum: discipline, anti-corruption and policy implementation

The Central Committee of the Chinese Communist Party (CCP) concluded its sixth plenary session (6th Plenum) in late October. The plenum has been described predominately as an effort by the Party to elevate the status of President Xi Jinping and enshrine his administration's anti-corruption efforts. **Nicholas Consonery**, **Kevin Ma**, and **Peter Folland**, political risk and strategic communications professionals at **FTI Consulting**, provide detailed analysis of the plenum and conclude by laying out the likely implications for foreign business in China.

In discussing the session, an editorial in the CCP journal *Qiushi* stated that the 6th Plenum was about making anti-corruption work a "permanent course of action" and that while "some call the current anti-corruption efforts 'a storm', the storm will never pass."

At the plenum the leadership promulgated new regulations on how the Party supervises and governs itself. These regulations subject officials throughout the bureaucracy to greater and more regular disciplinary inspections and checks. They also empower the Central Commission for Discipline Inspection (CCDI), which oversees internal supervision within the Party, at the local levels by solidifying a shift wherein local CCDI staff report to their superiors in the CCDI instead of reporting to local-level political officials (who would have obvious incentive to shape their findings).

The plenum also amended long-standing guiding principles on Inner-Party Political Life, a crucial governing document that was put in place in 1980, which commits to collective, consensus-based decision-making. The newly amended principles strongly recommit to the collective leadership model. But they also say that decisions need to be carried out once made: they call on Party officials to "unswervingly implement the Party's basic line", for example, and to "uphold the Party Central Committee's centralised and unified leadership".

Significantly, the CCP also gave Xi the official designation of 'core' leader at the plenum – an honorific given, perhaps in a more qualified sense, to previous presidents Deng Xiaoping and Jiang Zemin, as well as retrospectively to Chairman Mao, with previous president Hu Jintao the notable exclusion.

The plenum's focus on anti-corruption and Party governance is not surprising. It is widely understood that Xi's first term has been about cleaning up corruption in the CCP and refocusing the Party on its ideological roots. Internal politics were also always going to be on the agenda for this particular event. As Chris Johnson and Scott Kennedy at the Center for Strategic and International Studies in Washington DC pointed out in a piece discussing the plenum, "the Sixth Plenum of each party administration typically focuses on some issue related to culture or ideological matters."

So while it is important to try to understand the Party's signalling, it is also important to try and differentiate between routine matters of governance and genuinely new or interesting political developments.

And on that front we think there is a bit more to the story of the 6th Plenum. In our reading of the event, the plenum was not just about anti-corruption itself. The Xi administration is also working to use all instruments at its disposal to force implementation of intended policy changes at the local level. This includes compliance with anti-corruption work, but also with the broader set of policies the Party is pursuing. To the extent that President Xi and his team are successful in strengthening their hand, this could actually be positive for economic reform.

The new documents issued at the plenum lay the groundwork for this. The supervision regulations argue, for example, that Party officials must "ensure the Party's organisation adequately fulfils its functions". They also call for "strict compliance with direction throughout the whole Party" and state that "individual Party members must obey the organisation and lower authorities must obey higher authorities".

In discussing the plenum, the overseas version of the Party's newspaper, the *People's Daily*, drew these conclusions: "While vigorously advancing the anti-corruption campaign, the top authorities have also paid great attention to some officials' inaction. Since some officials have chosen to be 'lazy' to avoid committing 'mistakes' and being caught in the act, the authorities should strengthen the anti-corruption measures to identify the guilty and bring them to book."

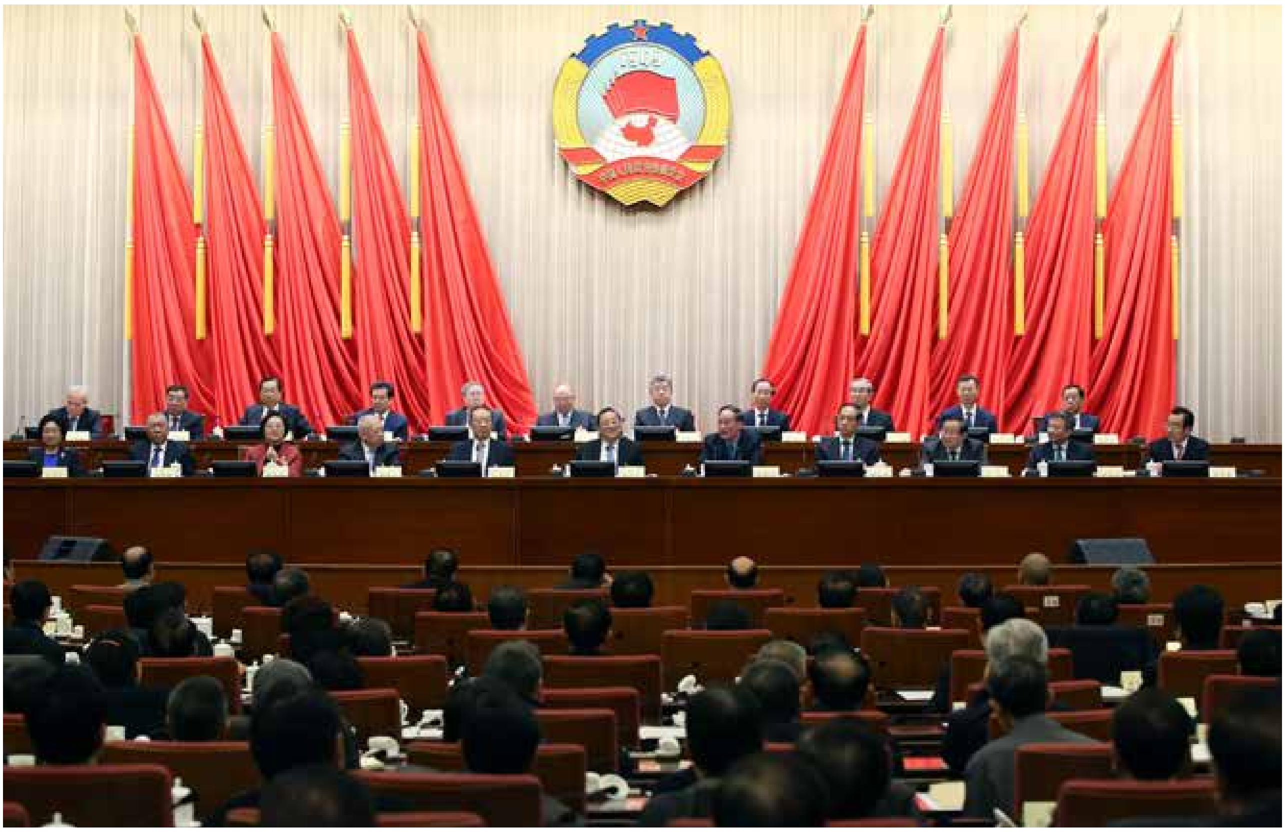
In other words, the leadership is solidifying its ability to hold officials accountable when they do not comply with intended reforms.

In arguing that "Party organisations at higher levels should be more responsible for organisations at lower levels" the new supervision regulations also issue a not-so-subtle hint that the leadership will be looking to hold higher-level officials and organs responsible for continuing anti-corruption problems or lacking policy implementation by individuals or bodies underneath their purview.

In short, we see a leadership team that is working on improving its own ability to govern as it heads into its second term.

For foreign companies doing business in or with China, the question this raises is…to what ends?

It was at an earlier plenum, the third of the 18th Central Committee in November 2013, where Xi's team laid out a bold set of commitments to economic reform – the *Decision*. This widely-discussed third plenum agenda raised hopes in the business community that the Chinese Government would take meaningful steps toward more consumer-driven, sustainable, market-based growth. An ideal outcome would have seen Xi's government moving quickly towards addressing key concerns of the foreign business community, such as opening new sectors to



foreign investment, reducing policy support for state-owned enterprises (SOEs), meaningfully cutting excess production capacity in a number of sectors and better protecting intellectual property.

To be fair, some progress has been made on each of these areas over the past three years. The government rolled out a set of new free trade zones, for example, and is experimenting with intellectual property rights courts. It has also been pressing local governments and industry for production capacity cuts, even if implementation has disappointed.

But foreign firms would like to see more – the European Chamber of Commerce's *Business Confidence Survey 2016* reported a "deepening disillusionment in China's reform agenda" among its members, for example. Instead, as Chinese investment has continued to flood into western countries this year, there has been increased anxiety at the lack of opening up of vast sectors of the Chinese economy to foreign investors.

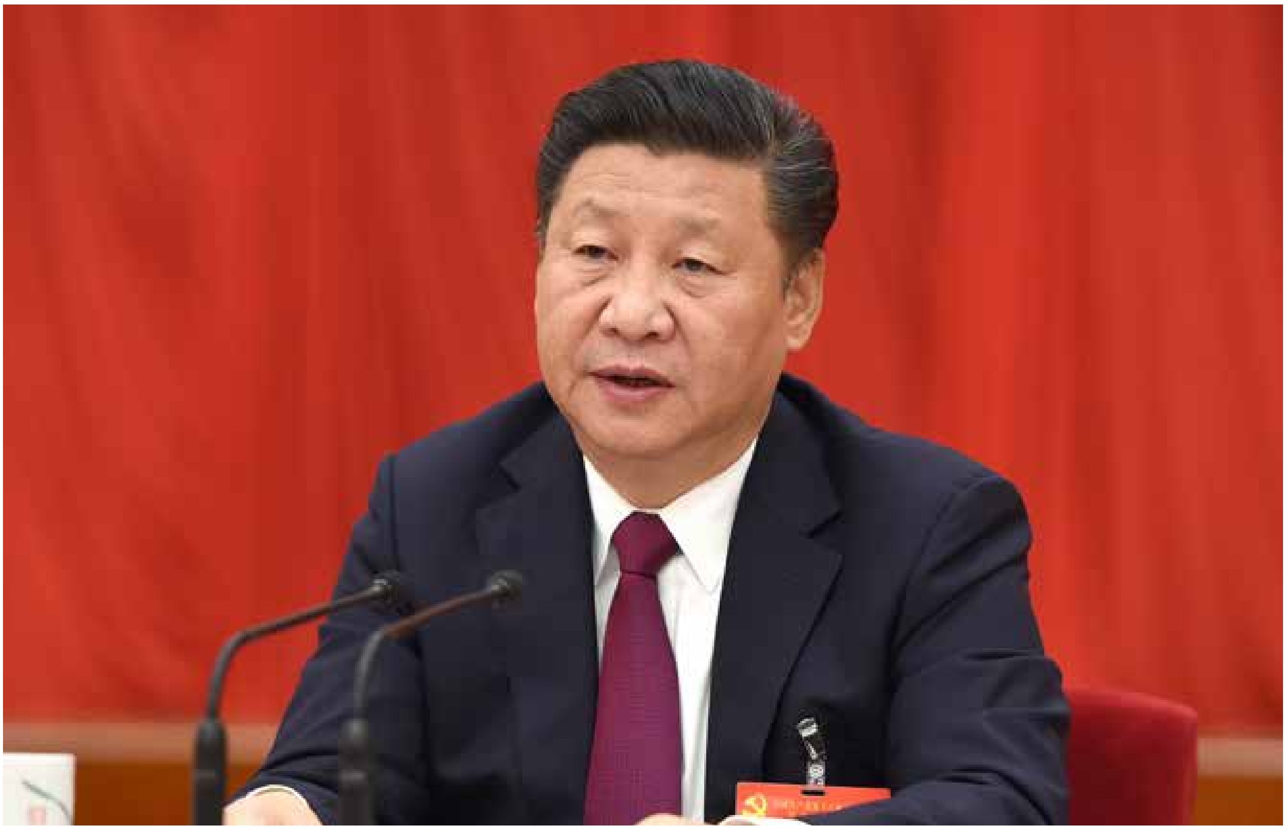
Unless new sectors are opened in China and progress is made on improving the foreign investment environment, it is quite likely that pushback to Chinese multinational companies' (MNCs') takeovers in the West will continue: the German Government, for example, reopened its review last month of a EUR 670 million Chinese acquisition of German chip-equipment manufacturer Aixtron; and ChemChina's USD 44 billion offer for Syngenta is still under review, with European and US regulators delaying the deal following concerns raised by rival mergers in the global agricultural products sector.

That Xi's government is using one of its two major political conclaves for the year (the other being the annual meetings of China's top legislative and consultative bodies – the National People's Congress and the Chinese People's Political Consultative Conference) to try to streamline decision-making and improve the outlook for governance is no accident and should be viewed positively. These are the latest in a series of moves to do so, following a widely-discussed article in the *People's Daily* earlier this year where an anonymous advisor—obviously close to Xi—sharply derided local governments and officials for their inability or refusal to push forward needed economic reform efforts.

Taken together, the 6th Plenum put Xi in a stronger position, entrenched anti-corruption work and gave Beijing a bit more muscle to push for local compliance of intended policy changes. Below we highlight the implications of these developments for MNCs in the China market:

Implications for Business

- The leadership is hoping to sustain anti-corruption



work beyond next year's leadership transition and into Xi's second term as Party chairman (which starts at the kickoff of the 19th Party Congress next autumn and will showcase the anointment of a new leadership team). For MNCs, the plenum's focus on entrenching anti-corruption work means that the ongoing scrutiny of them from central and local regulators will not let up.

- Expect policymakers to continue to be wary of meetings with MNCs in this climate. Following the 6th Plenum there will be an even greater emphasis than before on making sure that Party members uphold the Party's constitution and internal regulations. The CCDI will be further empowered to examine behaviour and oversee policy compliance. Policymakers subsequently will be extra keen to toe the party line, and will be cautious and risk averse in dealing with the private sector.

- Anti-corruption work will also mean continued risk aversion by SOEs and regulators in approving new investments or business ventures. This is likely to continue to impact Chinese business partners of foreign companies operating in China, who are not going to want to make decisions without an immense level of due diligence and oversight.

- This will be strongly exhibited by SOEs, where the Party is elevating its role and its oversight functions. Expect greater caution from SOEs when negotiating with foreign companies on a widespread number of business deals and collaboration.

- President Xi's elevation as 'core' leader is backed by his commitments to restore national greatness – which has included a set of more assertive defence and foreign policies. Particularly with the uncertainty around the surprise election of Donald Trump, geopolitical risks to bilateral relationships will remain elevated – including to the crucial relationship with the US.

- Keep an eye out for the leadership's economic reform agenda as Xi's second term approaches. The leadership has made many good commitments but so far underachieved in the way of follow through. Xi's second term, where he will be in a stronger position to implement change, may be a brighter period on the economic reform front. Eb

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DEALING WITH CHANGE

Business opportunities and challenges for EU SMEs in China's shifting landscape

The Chinese market has seen many changes in 2016, opening up new opportunities for European small businesses while demanding even more advanced local knowledge and experience. In this article, China experts at the **EU SME Centre** review the key changes that affected European SMEs in 2016, and share advice on how to better prepare for the future.

Meet the experts

Chris Cheung, Director

What are the key market trends that you think European small businesses should be aware of?

Despite the many changes taking place in the global socio-economic environment European companies remained, confident of the long-term prospects in China. The GDP growth rate is slowing, of course, from the double-digits of the past to the recent 6.7 per cent, and in the near future this looks set to decrease further to around five per cent. The change emphasises China's aspirations to restructure its economy – moving from investment- and export-orientated growth, to an environment where domestic consumption, increased productivity and innovation are the key drivers. This transition will bring with it the potential for greater opportunities for European businesses contemplating the market. The three top trends for 2017 that I would highlight are:

Moving up the value chain

China is striving to move its industrial processes up the value chain; looking to automatise and informatise its supply chains so that its goods can be produced more efficiently. Hand-in-hand with this move will be China's hunger for technology required to make the change – from industry robotics, transportation equipment, to agri-equipment and their related services, there will be opportunities for EU SMEs.

Growing domestic consumption

China's 'new normal' recognises that domestic consumption will play a larger role in the economy. Meanwhile, Chinese consumers, driven by the fast growing middle class, crave more goods from the EU. Small EU businesses should be particularly aware of the rapid growth of e-commerce platforms in China which has diversified the entry modes to the country, providing them with more channels to sell to the market.

Chinese outbound investment

The trend of increasing Chinese outbound investments is another key change. Spurred on by policies such as 'One Belt One Road', Chinese companies will increasingly be encouraged to venture outside the mainland to export and invest abroad. European businesses should grab the opportunities to service these new Chinese investors and, more importantly, to build the relationships with them on which long-term, successful business can be sustained.

Ludmila Hyklova, Legal Advisor

What was the one key legal update for European SMEs in 2016 in terms of doing business with or in China?

China's foreign investment administration reform. Starting from October 2016, foreign companies setting up a company in China in the industry sector—provided its activities are not in the category of restricted or prohibited according to the *Foreign Investment Guidance Catalogue* or other regulations—no longer need to apply for prior approval from the Ministry of Commerce (MOFCOM). The reform applies to both traditional wholly foreign-owned enterprises (WFOEs), Sino-foreign equity joint ventures (EJVs) and cooperative joint ventures (CJVs), and those invested in by foreign-funded investment enterprises in China. The filing process also applies to changes within current foreign-invested enterprises (FIEs).

This new regulation is another step in the foreign investment reform that started in several free trade zones some time ago, which aims to simplify procedures by replacing former approval requirements with filing. However, the pool of industries and activities in the category still requiring MOFCOM prior-approval is not small.

What would be your top advice for FIEs in China this year?

Understand how this reform affects your business when it comes to set up and company reporting. It is crucial that companies keep themselves aware of these significant steps. The Chinese Government continues to take measures aimed at attracting foreign investors while still maintaining high market access standards in certain sectors.

Rafael Jimenez, Business Development Advisor

What was the most important update for European SMEs in 2016 in terms of doing business with or in China?

Cross border e-commerce (CBEC). In April, the Chinese Government made a number of significant amendments to the regulation of CBEC in the country, including a new tax policy and a list of products authorised to be imported via CBEC. Both amendments can affect all participants in the supply chain of imported products through CBEC into China, from suppliers and traders in the EU, to online platforms registered to trade with imported products via CBEC.

What do you think the biggest market challenge is for European SMEs?

The major challenge for SMEs now is to understand that success in China requires much more granularity. From now on SMEs need to manage a scale or level of detail much deeper in identifying the opportunities.

What would be your top advice this year for European SMEs interested in the Chinese market?

They need to segment their targeted market more carefully. Product category no longer defines an opportunity. It has to be mapped out beforehand in terms of cities, sales channels, target consumers, pricing, distribution, types of retailer, types of partner, and sub segments for each of these criteria. There are a growing number of opportunities—that's the bright side for SMEs—and we remain positive.

Martina Gerst, Market Access Advisor

What changed the most for European SMEs in 2016 in terms of market access?

The implementation of China's new Food Safety Law (NFSL). China has been implementing this new law for over a year, which is recognised as the country's strictest food safety law by far. It is important for European companies in the food and beverage (F&B) sector to keep a close eye on its implementation and understand how to comply with it to avoid unnecessary problems.

What would be your top advice this year for European SMEs in the F&B sector?

Compliance is essential. You must immediately face all legal aspects required in China, not grope in the dark with the hope that everything will be alright. To ensure compliance you may want to establish a special China food safety team, ideally consisting of members from the legal, food technology, product management and quality assurance departments before exporting.

Establishing a specific internal Chinese food safety working procedure as a reference for employees involved in various stages of handling a food safety issue is also useful, as is keeping organised written records for all activities. Investigation dossiers should include written records such as correspondence, meeting minutes, testing reports, findings of investigations, conclusions reached by the investigation team and corrective measures, if any, that have been taken.

Close attention should also be paid to legal updates. Different authorities, or even individual officers, often have different interpretations of the regulations. Being accurately informed of legal and regulatory updates in China is crucial for your business success here.

Finally, you should monitor different enforcement levels and local regulations across the country. While the central government has published, or is drafting, regulations to enforce the NFSL, local governments are also actively developing new implementing rules. You can expect tighter control and inspection in some cities (e.g. Beijing) while others could still delay the application of the new rules or enforce them in a more relaxed way.

Success Stories in the Chinese Market

Getting the first crate of beer from the UK to China

Lancaster Brewery is a British company producing and selling a variety of beer products. It entered the Chinese market in July 2016, successfully reaching the country and clearing customs in less than a month. It is targeting Guangdong Province to start with but plans to expand business in other first-tier cities in the near future.

Lancaster Brewery is currently exporting to China with the assistance of a local Chinese business partner who handles the process of customs clearance and relabelling in bonded warehouses. The company also plans to send an employee to Guangzhou for a period of six months to represent the brand in the market, provide support to the partner and develop a network of distribution channels.

During their market research process, Lancaster Brewery came across the EU SME Centre's content online. The information helped the company better understand the technicalities of exporting products to China and to clarify the requirements for labelling, customs procedures and intellectual property protection in China. "The *Alcoholic Drinks Market in China* webinar, held on May 10th, provided me with crucial data to pitch the China opportunity to our company board and win their approval," says Giulia Ravasi, International Export Manager.

As advice for other European businesses interested in the Chinese market, Ravasi emphasises the importance of establishing trusted relationships with Chinese business partners, doing market research and the willingness to seek help.

Accessing China's Fashion Market

Just Campagne is a family-run business based in France, designing and making 100% hand-made leather bags and accessories. With three boutiques already in France, the company is now looking to develop in the Asian market, particularly China.

In their early days in China, they carried out a market study in Beijing by organising private events for potential clients to show them their products. The feedback they received afterwards was very positive and encouraging.

Célia Berkouk, Head of Marketing and Sales at Just Campagne, first heard about the EU SME Centre during an event organised by a Beijing-based women's professional network. After discussing the Chinese fashion industry with Rafael Jimenez, the Centre's Business Development Expert, Berkouk very quickly got the advice she needed to get started.

China is a high potential market for Just Campagne, because customers are in search for niche and exclusive products with great quality and service. "They fully understood that our product category is not aimed at the mass-market," says Berkouk.

Understanding payment methods of Chinese travellers and *daigou* was also very useful for Berkouk. Just Campagne adopted Chinese payment methods for developing brand awareness for Chinese people travelling abroad and visiting one of their stores in France. All the boutiques accept UnionPay and the ones in Paris accept AliPay as well.

No less important was the insistence on registering the company's trademark in China. Early on, the Centre referred Berkouk to the China IPR SME Helpdesk to seek advice on trademarks.

The EU SME Centre in Beijing provides a comprehensive range of hands-on support services to European small and medium-sized enterprises (SMEs), getting them ready to do business in China.

Our team of experts provides advice and support in four areas – business development, law, standards and conformity and human resources. Collaborating with external experts worldwide, the Centre converts valuable knowledge and experience into practical business tools and services easily accessible online. From first-line advice to in-depth technical solutions, we offer services through Knowledge Centre, Advice Centre, Training Centre, SME Advocacy Platform and Hot-Desks.

The Centre is funded by the European Union and implemented by a consortium of six partners - the China-Britain Business Council, the Benelux Chamber of Commerce, the China-Italy Chamber of Commerce, the French Chamber of Commerce in China, the EUROCHAMBRES, and the European Union Chamber of Commerce in China.

To learn more about the Centre, visit website www.eusmecentre.org.cn

EUSME Centre

WHAT GOT YOU HERE WON'T GET YOU THERE

Corporate entrepreneurship in China

Having changed profoundly in just 10 years, it is perfectly conceivable that the pace of change to China's business landscape will increase further over the next decade. What will this mean for European companies with subsidiaries in China? While many of them are currently market leaders maintaining this position won't get easier, on the contrary, competition is set to become fiercer. The key to sustainable success, says **Dr Laurenz Awater**, Managing Partner at the **INNOVA Management Institute** (**Shanghai**), is encouraging and developing corporate entrepreneurs, and creating a framework that allows them to flourish.

Past patterns of success are by no means a guarantee for future growth and prosperity. The key to survival is the anticipation of coming changes and swift adjustment, agility. This requires closeness to customers and markets as well as sound and fast decision-making, conditions that call for greater empowerment of China CEO's and leaders at regional headquarters who take the designated role of corporate entrepreneurs.

Nurturing corporate entrepreneurs

Small and medium-sized enterprises (SMEs) are typically built around entrepreneurial personalities and need corporate entrepreneurs to flourish. We dare to make a prediction: SMEs that do not nurture corporate entrepreneurs will struggle, fail or even vanish altogether.

Corporate entrepreneurs are the engines of organisational growth, providing much of the initiative, energy and motivation that is required. They identify and create opportunities, drive change and innovation, start new ventures and provide leadership for strategic renewal to create economic value. They excel due to their ability to bring others along.

What sets corporate entrepreneurs apart from more traditional managers? The two most important qualities of corporate entrepreneurs are open-mindedness and cognitive ability. They tend to be independent thinkers who make sense of the world based on their own observations and experiences. They deal proactively with ambiguity and uncertainty, and act as trail blazers, pioneers, business builders and change agents. They are not necessarily the idea generators but their strong execution orientation allows them turn ideas into profitable businesses.

Typically, corporate entrepreneurs are driven and motivated by the excitement of a challenge, willing to take on risks and actively look for opportunities to stretch and grow. What makes them effective leaders is that they are adept at setting the right direction and know how to exploit core businesses while exploring new ones.

Entrepreneurial leaders don't grow on trees, they need to be developed over time.

Fostering entrepreneurial behaviour

Identifying, hiring and developing entrepreneurial talent is essential for nurturing corporate entrepreneurship. But to effectively foster entrepreneurial behaviour more profound changes are necessary, changes which provide individuals and teams with opportunities to learn and grow. These include:

- Recognising the unique qualities that corporate entrepreneurs bring to the organisation;
- Giving corporate entrepreneurs the freedom to experiment, and recognising that frequent trial and error is an inherent part of discovery;
- Assigning corporate entrepreneurs to your organisation's biggest and most challenging problems;
- Encouraging innovative and entrepreneurial behaviour by financially supporting projects, knowing that some of the projects will fail;
- Providing decision-making latitude and freedom from excessive oversight by delegating authority and responsibility to corporate entrepreneurs; and
- Providing training and professional development opportunities in key areas of entrepreneurship, such as navigating amidst uncertainty and creative thinking.

Models of corporate entrepreneurship

To establish corporate entrepreneurship as a core competency of your organisation, you have to decide which approach to corporate entrepreneurship best suits your corporation's culture, strategy and business model, and refine the processes used by individuals and teams to develop new businesses, products, or services. Researchers at MIT Sloan have identified two dimensions that consistently differentiate how companies approach corporate entrepreneurship:

- *Organisational ownership*: who, if anyone, within the organisation has primary ownership for the creation of new businesses? and
- *Resource authority*: whether there is a dedicated pot of money allocated to corporate entrepreneurship, or whether new business concepts are funded in an ad hoc manner through divisional or corporate budgets or 'slush funds'.

Together the two dimensions generate a matrix with four dominant models: the opportunist (diffused ownership and ad hoc resource allocation); the enabler (diffused ownership and dedicated resources); the advocate (focused ownership and ad hoc resource allocation); and the producer (focused ownership and dedicated resources).

Each of the models requires different forms of leadership, processes and skill sets, the researchers found. An enabler model depends on establishing and communicating simple, clear processes for selecting projects, allocating funds and tracking progress, all with well-defined executive involvement. Advocate models require individuals with the instincts, access and talent to navigate the corporate culture and facilitate change. The producer model requires considerable capital and staffing and a direct line to top management.

Evolving from the opportunist model to any of the more deliberate forms of corporate entrepreneurship typically begins with a broad, clearly communicated vision. Whatever model is selected, your organisation should experience a significant increase in the number of proposals, which leads to the challenge of scaling field-proven, new businesses and finding organisational homes within the company. And the more distant a new concept is from the 'comfort zone' of the core business, the greater the challenge.

In a slowing economy with considerable overcapacities in many industries advocating corporate entrepreneurship is no easy game as budgets get trimmed and risk aversion prevails. It is corporate entrepreneurs, however, who hold the keys to the company's long-term success. Eb

Dr Laurenz Awater *is managing partner at the* ***INNOVA Management Institute (Shanghai)****, a consulting firm focusing on change, innovation, leadership and organizational development. Laurenz is co-facilitator of the management programme Corporate Entrepreneurship in China.*

THE TOOLS TO THRIVE

Providing effective support to SME globetrotters

Providing support to SMEs has been a long-standing policy of the European Union, particularly helping them to establish businesses and succeed overseas. **Jean-Marie Avezou**, DG Internal Market, Industry, Entrepreneurship and SMEs, **European Commission**, says that the majority of EU SMEs tend to stick to their own backyard due to a number of difficulties, such as high export costs and challenging regulatory environments often encountered in third countries. However, there are, he explains, various tools at the disposal of EU SMEs to help them internationalise and thrive.

In a globalised world, SMEs need to be able to face up to increasing competition from developed and emerging economies and to plug into the new market opportunities these countries are providing. International activities reinforce growth, enhance competitiveness and support the long-term sustainability of companies. Moreover, a direct link has been established between internationalisation and increased SME performance.

As demonstrated by the result of an EU study released in 2015,[1] few small businesses in Europe export beyond the EU: 69 per cent of EU SMEs have not engaged in any business activities outside the European Internal Market in the last three years. The main barriers identified by exporting EU SMEs are: burdensome administrative procedures when exporting, high delivery costs, the difficulty of identifying business partners abroad and the high volume of financial investment needed.

Increasing the internationalisation of SMEs and helping them access third markets remains crucial for Europe's competitiveness, economic growth and innovation. The EU priority is therefore to ensure that enterprises can rely on a business-friendly environment and make the most out of growth markets outside the EU. How is this translated into practice?

The fact is that over the years EU SME policy has paid a great deal of attention to the internationalisation of the more than 21 million small businesses representing the backbone of the European economy and a key source of jobs and growth. Support provided by the EU in this area consists of different actions and programmes: the EU has developed a wide range of support measures to foster SMEs' internationalisation. Its main aim is certainly not to duplicate what is done at national level by each Member State of the European Union. It is rather to provide clear added value through a European dimension where it makes sense.

For example, almost 22 per cent of the total budget (EUR 2.3 billion) allocated for 2014–2020 to the COSME programme (Competitiveness of Enterprise and SMEs) is going to the priority area of 'Supporting internationalisation and access to markets'. The COSME programme funds the Enterprise Europe Network, which is the world's largest support network for SMEs. Present in more than 60 countries, the network helps European businesses to expand internationally by providing them with advice, information on markets and rules or regulations to be complied with and matchmaking opportunities. A total of 4,500 experts in internationalisation and technology transfers are available to accompany SMEs' various development projects in markets beyond the EU, as well as in the European Internal Market. In countries like China, the network is represented by Business Cooperation Centres (in Chengdu, Changsha and Shanghai) run by local organisations. The aim is to connect Chinese SMEs with European SMEs through matchmaking events or business missions to develop partnerships, business cooperation and trade.

The COSME programme is also financing several targeted actions helping SMEs to internationalise through clusters, international fairs (Business beyond Borders project) or the definition of a new methodology to support and trigger SMEs' readiness to develop international business in third-country markets.

Another example of practical support for SMEs' internationalisation is the EU Gateway|Business Avenues mission developed in Asia through the Partnership Instrument. This is an EU initiative helping European companies to establish long-lasting business collaborations in Asia. Selected European companies, including SMEs, get the opportunity to participate in a one-week business mission in any of the three target markets—Korea, South East Asia and China—focused on a specific sector. Companies benefit from a range of business support services, which include coaching, logistical and financial support.

To accompany SMEs in developing their presence abroad, a network of intellectual property rights (IPR) helpdesks is on hand to provide free advice on IPR, which is often mentioned as one of the key concerns of EU SMEs when considering internationalisation. Initially set up in Mainland China, IPR SME helpdesks are now covering broader China (Taiwan, Hong Kong and Macao) as well as Southeast Asian and Latin American countries. They provide jargon-free, first-line and confidential advice on IPR issues, using innovative communication techniques to more effectively reach out to SMEs.

More general assistance is also given to intermediary organisations that have developed EU business centres to help European SMEs to enter non-EU markets. These centres have been established in different Asian countries, including China. They provide first line support services including market access assistance, guidance on local business practices and regulatory issues. In the case of the successful EU SME Centre in China, its website is allowing SMEs in Europe to make informed decisions through the use of diagnostic business tools before they enter the Chinese market.

The business environment in third countries is an important factor that can determine if SMEs develop their activities and thrive. Small businesses are

[1] *Eurobarometer* study on Internationalisation of Small and Medium-sized Enterprises

indeed more vulnerable to red tape and to difficult or unpredictable regulatory frameworks. The various government-to-government industrial policy or regulatory dialogues set up by the EU, notably with China, contribute directly to the improvement of the business environment. They help to address the issues that SMEs face when they go international. Specific SME policy dialogues exist with relevant administrations of China and the US: they constitute regular fora where best practices in the field of SME policy are exchanged.

All support actions for SMEs' internationalisation should be seen in the broader framework of the new concept of EU economic diplomacy currently developed within European institutions. Economic diplomacy is about using all available levers to promote EU economic interests abroad. It is not about developing new instruments but rather reinforcing the articulation between all existing ones so that they form together a coordinated, coherent and user-friendly 'package' that businesses will be able to fully exploit. This means removing barriers and creating incentives to trade and investment by opening global markets, fostering cooperation on economic governance and regulatory convergence. Improving the coherence and effectiveness of the external action of the EU in the economic field will reinforce the support to EU businesses and SMEs' internationalisation. Eb

Giving a boost to start-ups in Europe, too

The European Commission recently adopted a Start-up and Scale-up Initiative, which aims to give Europe's many innovative entrepreneurs every opportunity to become world leading companies. It pulls together all the possibilities that the EU already offers and adds a new focus on venture capital investment, insolvency law and taxation. There is no lack of innovative ideas and entrepreneurial spirit in Europe. But many new firms do not make it beyond the critical first few years, or they try their luck in a third country instead of tapping into the EU's potential 500 million customer base. The European Commission is determined to change that and help start-ups deliver their full innovation and job creation potential. The Initiative addresses the main obstacles for companies to starting up and scaling up in Europe, which were identified in a recent public consultation.

The Start-up and Scale-up Initiative brings together a range of existing and new actions to create a more coherent framework to allow start-ups to grow and do business across Europe, in particular: improved access to finance, a second chance for entrepreneurs, simpler tax filings and fostering ecosystems where start-ups can connect with potential partners such as investors, business partners, universities and research centres. A set of measures will also be adopted to support the use of IPR by SMEs and take action to support access by start-ups to the European public procurement market.

BREAKING DOWN BORDERS

How SMEs can accelerate e-commerce business through free trade zones

China's cross-border e-commerce (CBEC) market continues to both evolve and boom. The digital economy has become a crucial driver for China's economic development, and its market is now a global leader, opening new opportunities for foreign business. Many European SMEs, aware that China's middle-class is increasingly demanding food safety and higher product quality, feel that they could hold a competitive advantage by expanding their business in China via the Internet. **Andrew Zhang**, Partner, and **Mireia Paulo**, Business Development Manager, **A&Z Law Firm**, analyse China's model of Cross-Border E-commerce Comprehensive Pilot Areas (CBECPAs) outlining the policies that can benefit European SMEs looking to step into the ring.

Fast-growing e-commerce market forces to look at

The Chinese online community continues to expand and has now become the largest in the world: data provided by the China Internet Network Information Centre showed that by December 2015, there were about 688 million Internet users in China. In addition, the number of online shoppers in China increased by 125 per cent in 2014, to 361.4 million, compared with 2010. The Internet and the ongoing digitalisation of people's habits have affected a dramatic shift in Chinese consumers' behaviour.

Internet users now need just spend a few minutes to look for all kind of products, select what they want, press a few buttons to pay online and then receive the goods at home within a short time—often the same day—and all without having to leave the comfort of their own sofas. Companies such as Alibaba, Jingdong and Suning are cashing in on this trend by innovating, expanding and riding the wave as China develops and improves its own digital systems. According to a report about CBEC published by the Ali Research Institute in 2016, [1] CBEC business size had reached CNY 4.8 trillion in 2015, up 28 per cent from the previous year. While still in its infancy, the total size of this market for import and exports represented 19.5 per cent of China's total in 2015. The report forecasts that China's CBEC business will reach CNY 12 trillion by 2020, accounting for 37.6 per cent of China's total import and export trading volume. Based on the Ministry of Commerce's data released in September 2015, the number of CBEC business platforms in China had already exceeded 5,000.

Two common CBEC business models

The proliferation and enhanced integration of the Internet of Things, social media and e-commerce in daily life have impelled European SMEs to look at this new sales channel. However, despite the promising future of CBEC in China, a lack of understanding of the local context and certain policies pose some constraints to European companies. The difference of tax and inspection standards between conventional trade and CBEC, for example, generates a great deal of confusion as to whether or not policies applied to China's CBEC market are actually favourable.

Based on prevailing Chinese regulations and policies, companies working in CBEC commonly apply one of the following two business models:

- **Direct Purchase Import (B2C) via international express courier**

  Under this model, companies establish an overseas CEBC platform, such as AMAZON.COM, and sell products directly to consumers in China. The online platform will submit particulars of the order, including payment and logistics details, to customs in real time, while at the same time products will be delivered from an overseas warehouse via an international express courier, such as UPS or DHL, to the consumer in China. The international express courier will undertake the responsibility for China customs declaration. Upon completing customs clearance, inspection and quarantine procedures, the product will be delivered to the Mainland consumer.

- **Bonded Import mode (B2B2C) via a free trade zone**

  This mode requires the establishment of a company in China for importing goods in batches into a free trade zone (FTZ) to be stored in bonded warehouses. When a consumer places an order with such a CBEC platform, the platform makes a real-time customs declaration, transferring the goods from the bonded warehouse to China's customs. At that time, order, payment and logistics details are checked and confirmed, before the goods are cleared through customs at the bonded zone and express couriered to the consumer.

When comparing both models, the second one offers some advantages in terms of speed of delivery and a reduction in transportation risk. Also, there is a greater number of products authorised for sale via this method, as long as the products are included in the *List of Products Authorised for Retail Import via China's Cross Border E-commerce*.[2] For instance, if you want to import liquid milk you will only be allowed to do so via a FTZ. Consequently, this business model is becoming more popular.

On the regulatory level, both models have favourable policies governing cross-border B2C e-commerce. Products are sold at a lower price, as most imported products brought into the FTZ are subject to a blended tariff rate—the so-called Cross-Border E-commerce Retail Import Tax—rather than normal import tariffs imposed on goods that are conventionally imported. For example, if an order transaction amount is lower than CNY 2,000 (roughly EUR 267) and an individual purchases products up to the value of CNY 20,000 (roughly EUR 2,671) annually, import duties will be levied for the imported goods. There is another favourable tax rate in this case: import VAT and consumption tax will be reduced by 70 per cent. These policies do not apply if the cost of products exceed the amount previously indicated.

Attention should be paid by SMEs to the most suitable business model according to their specific needs by selecting an FTZ that has a special preferential policy focus most applicable to its own CBEC business. For instance,

[1] Originally translated from阿里研究院：《2016中国跨境电商发展报告》全文, http://www.orangebank.com.cn/index_e/hy/hyzx_kjds_e/85087.html

[2] "List of the Cross-border E-commerce Retail Imports" First Batch, 6 April 2016,http://gss.mof.gov.cn/zhengwuxinxi/zhengcefabu/201604/t20160401_1934275.html Second Batch, 15 April 2016. Accessed November 3, 2016. http://gss.mof.gov.cn/zhengwuxinxi/zhengcefabu/201604/t20160415_1952574.html

areas known as Cross-Border E-commerce Comprehensive Pilot Areas (CBECPAs) and Pilot Free Trade Zones would be most recommendable for European SMEs. However, it should be kept in mind that FTZs differ in function, policies and names, which can initially cause confusion.

CBEC Pilot Areas

The State Council has approved the establishment of 13 CBECPAs in Hangzhou, Tianjin, Shanghai, Chongqing, Hefei, Zhengzhou, Guangzhou, Chengdu, Dalian, Ningbo, Qingdao, Shenzhen and Suzhou. The plans for these areas are implemented at the provincial level, with the pilot programmes varying between each area in terms of technical standards and regulatory models. These areas are considered more suitable for CBEC business because local governments actively implement programmes that aim to solve existing problems with customs clearance, settlement of exchange and tax rebates.

Some of the preferential policies associated with CBECPAs include, but are not limited to, the following:

- Special customs clearance models:

    - CBEC enterprises can make batch declarations to customs, and do not need to make a declaration for each individual order.

    - CBEC enterprises can pay duty, import VAT and consumption tax once per month, and do not need to pay such duty and tax for each declaration.

    - CBEC enterprises can withhold and remit duty and tax, which is paid by the consumer, helping the CBEC enterprise to improve the consumer experience.

- Establishment of 'one-stop window' systems, allowing CBEC businesses to make only one customs declaration – customs then deal with the entry-exit inspection and quarantine bureau (CIQ) to examine all documentation and products. This system improves the average customs clearance time and efficiency, and reduces costs.

- Permission for CBEC enterprises to open a personal foreign exchange bank settlement account without the USD 50,000 per year limit.

- Providing improved conditions for logistics companies in order to attract them to provide suitable services for CBEC business.

- Strengthened IPR protection and an established credit system for CBEC enterprises, providing more fair competition in China for foreign CBEC business.

Taking into consideration that European SMEs do not have the same pool of resources that the Chinese e-commerce giants do, it is highly recommendable that they spend time identifying the most suitable business model and the location for their specific company. China's FTZs, including CBECPAs and its pilot FTZs, could provide the most convenient platforms that will enable them to compete and prosper. Eb

A&Z *is a leading Chinese law firm, which employs over 55 experts consisting of attorneys, legal practitioners and business analysts across 11 jurisdictions. The Shanghai, Beijing, Dalian, Wuhan and Tokyo offices provide a full range of services covering Foreign Investment, Overseas Investment, Competition and Antitrust, Intellectual Property, M&A and Corporate Restructuring, Labour and Social Security, Dispute Resolution, Compliance and Corporate Social Responsibility, Finance and Capital Markets, Customs Logistics and Maritime Commerce, and Environment, Health and Safety (EHS).*

NEWBORN AND REBORN

The Benefits of Embracing Digital Globalisation

The process of digital globalisation is allowing enterprises to expand their reach beyond what they may have previously thought possible, in an efficient and cost effective way. **Diane Wang** of **DHgate.com** says that this revolution is helping to level the playing field between large enterprises and SMEs, while also pushing more female entrepreneurs to the fore.

Slowly but surely, large-scale enterprises are becoming increasingly prepared for digital globalisation and are embracing new types of digital businesses, like cross-border e-commerce platforms. Traditional manufacturing enterprises and traditional foreign trade enterprises, as well as marketing, payments, logistics, distribution warehouses, financial services and other business processes, are all undergoing significant changes as a result. The deep integration between traditional business and the Internet, including the adoption of both an online and an offline presence by businesses of all kinds, is already highly visible.

According to conservative estimates, only half of traditional enterprises are likely to be experience this 'rebirth' in the future, though; the remaining fifty per cent will have to contend with them. The result will be that, by 2030, approximately two billion jobs will have vanished, accounting for roughly half of existing job opportunities worldwide. However, after 15 years, many new types of global companies are predicted to emerge.

Closer ties between traditional industry and the Internet

We are already in the midst of this evolution. For example, in China, street vendors must now support mobile phone payment methods, or risk being abandoned by customers. This is also true for big chain stores like WalMart, as well as 'mom-and-pop' shops selling baked goods. These may be examples of the shallow integration of traditional industries and the Internet, but this is just the beginning. In the future, businesses' more prominent use of the Internet will create inestimable opportunities.

Traditional enterprises will only have access to these opportunities if they leverage the Internet to enhance their *core* abilities. We are still in the early stages of companies with an online presence alone gaining an offline presence, and traditional enterprises gaining an online presence. Deep integration like this will allow new companies to rise in every industry; in addition, such integration will remould industries' ecosystems. In time, offline-only enterprises and online-only enterprises will become fewer and fewer.

Not long ago, I was chatting with the owner of the biggest foreign trade group in China. They offer services to thousands of local SMEs that engage in foreign trade, helping them with customs clearance and tax return settlements. However, they were surpassed by a small company that leverages the Internet and foreign trade services more effectively than they do. This is an example of how digital globalisation helps level the playing field; it also helps worthy enterprises achieve the success they deserve.

With the merging of traditional industries and the Internet, the strategies that enabled past successes, like possessing multiple warehouses, are no longer relevant today. Thus, all resources must be re-examined with digital globalisation in mind. That being said, the nature and goals of the business have not changed, providing quality products and services to customers is still essential.

Taking the aforementioned foreign trade group as an example, the thirty years of experience in foreign trade that the owner has accumulated remains the organisation's most valuable asset. But while historically he was rightly focused on customer service, there was also a need to build a comprehensive foreign trade service platform capable of attracting more customers from other provinces, while developing innovative services. It was the Internet that provided the opportunities for this kind of deep integration.

First, the Internet provided the opportunity to scale up his business. Many companies like his are scattered across various heavily-populated places, such as Zhuhai, Qingdao and Hangzhou, but only serve customers within their respective regions. After he achieved deeper integration with the Internet, he broke free of such regional confines. Now, he not only serves local customers, but also those across the country.

Second, through online service platforms, the cost of services that they provide has been reduced, while efficiency has actually improved.

Third, digital integration has provided the opportunity for them to develop more innovative services, such as supply chain finance and assisting customers to handle their tax returns. Before, it took six months for customers to receive their returns, now the time is much shorter. The tax return can be given immediately to the customer, because banks can utilise online data to determine the customer's credit before offering a direct return.

Embracing global thinking and removing barriers between nations

In China, TaoBao, China's leading domestic e-commerce platform, has been revolutionary in multiple areas, particularly with gathering goods from across the country and redistributing them. However, digital globalisation has brought another change – cross-border e-commerce platforms have been breaking down the boundaries between countries. The future holds the promise of people being able to buy and sell globally much more easily.

Over the past 10 years, the Chinese Yiwu Commodity City, the Guangzhou wholesale market, the Russian

market and the Spanish wholesale clothing market, have all been receiving less and less attention. According to the the head of the Yiwu Commodity City, the flow of people is only a quarter of what it used to be; nowadays, everyone is sourcing their products online.

In actuality, digital globalisation has not abandoned these major markets. Through cross border e-commerce platforms they can transform their businesses, acquiring business from beyond the confines of their locality, accepting orders from across the globe. Therefore, businesses are not limited to selling their goods to Chinese customers alone; they can also sell to Chilean, Brazilian and Singaporean customers. Companies can function both online and offline. They can also choose to use a combination of the two, using online payment for in-store purchases.

Digital globalisation means more equality

When it comes to digital globalisation, there is no rich or poor, big or small, male or female. In other words, due to the nature of international business, people cannot and will not discriminate against sellers based on such criteria. More companies can thus enjoy the prospect of increased sales.

First, during the era of traditional trade, it took some developing countries several decades or even centuries to catch up to developed countries. But today, the forces of digital globalisation have allowed developing countries to develop far more quickly. China is by far the most successful case, but Brazil's progress is quite impressive as well: digital globalisation has resulted in its GDP being two to three times higher than some developed countries.

Second, even if a company does not have the same name recognition that companies like Lenovo or Huawei have, SMEs can still become multinational enterprises and compete with much larger companies in the global market. Even the smallest company can gain an international following.

Third, digital globalisation helps women have the same equal entrepreneurial opportunities as men. According to a 2015 survey conducted by Alibaba, only 3.6 per cent of female entrepreneurs work in traditional industries, however; I am proud to say that roughly half of the entrepreneurs on DHgate.com are women.

A woman named Jolie Shen is one such entrepreneur. In 2011, after she graduated with her associate's degree, she resigned from a foreign headhunting company based in Beijing and moved to Suzhou to be with her family. As a stay-at-home mother, she decided to start her own business on DHgate.com, selling wedding dresses to buyers in Europe and the United States. Her one-woman operation evolved into a company with over seventy people in four years. Just last month, the company attracted the attention of a new investor. She intends to use this funding to realise her dream of attaining international brand recognition, through cross border e-commerce.

Embracing both the Internet and globalisation clearly increases the number of opportunities available to female entrepreneurs, helping them to succeed in their chosen industries.

Conclusion

It is evident that digital globalisation is reaching every corner of the world, offering everyone the opportunity to realise their dreams. With the help of digital integration, we can achieve more equitable capital allocation across the globe, making the act of embracing digital globalisation a worthy pursuit. Eb

***DHgate.com** is the first to market and the biggest transactional cross-border B2B e-commerce marketplace in China, providing global buyers with quality products at competitive prices. Founded in 2004, DHgate.com has approximately 10 million global buyers from 230 countries and regions, with 1.4 million global sellers offering 40 million products. DHgate.com's business enables buyers to directly access global manufacturers of the world's top brands with rich product selections. DHgate.com is an all-in-one platform with integrated services for international logistics, cross-border payments, internet financing.*

FOREIGN SMES' NEXT BIG SHOT

China's consumer goods market

Although China is gradually shifting to a consumer-driven economy, with increasing rates of urbanisation and rising household incomes, opportunities for domestic consumer goods companies are becoming scarcer. Analysts point to the fact that they face persistent price deflation in a low-inflation environment, along with flat sales volumes in overcrowded markets. This is partly due to overcapacity, which is affecting several sectors, including food and beverage, retail and textiles. **Rosario Di Maggio**, Business Development Director at **Vistra China**, says that under these conditions, the high reputation enjoyed by many foreign brands could give them the edge in this expanding market.

Foreign brands win consumer favour

While in the current climate domestic brands are suffering in China, its marketplace is being increasingly filled by competing foreign brands. They are winning consumer preference due to the perception that they are better quality and more fashionable. In addition, e-commerce business models are making it easier for them to reach consumers, while lower logistics costs and reduced import tariffs are also playing an important role in their rise. But while it is not so surprising to hear that big brands are making their moves, the market is also attracting some heroic, small-sized businesses and a very determined bunch of entrepreneurs.

Saverio Paolillo is a 30-year-old Italian from Torre del Greco, a small city on the shores of the Gulf of Naples known for its production of coral jewellery since the seventeenth century. He is the fourth generation of a family of coral traders and, with his dad and three siblings, runs a business that sells coral in three continents. Four years ago, Paolillo moved to Guangzhou, the primary jewellery hub of China, to tackle a market that he defines as "astonishing for the numbers, crazy for the way people make purchasing decisions…and so difficult to understand that it became a permanent challenge". Business was very good for the first three years, however, in the last six months, with growth rates slowing, Paolillo has started to look for more opportunities in other major cities, such as Beijing and Shanghai.

"I think it would be nice to live in China for a few more years and build strong sales channels. It is difficult as there are a lot of competitors and a lot of fake products around here, but clients are getting sophisticated," says Paolillo.

China's emerging middle class fuels consumption

A recent McKinsey report shows that China's consumer spending data is not a reliable measure of prosperity and its economy is now too complex and distorted; what really counts is household income. China has an emerging middle class, with higher average household incomes and steadily rising consumption. Furthermore, the size of China's average household income is ahead of other emerging markets, which makes China an unprecedented, unique and exciting phenomenon. The report forecasts growth of six per cent and above until at least 2020, for semi-necessities such as clothing and household products, and discretionary categories of goods such as transport and recreation. Moreover, a lot of income in China is unreported, which means that actual numbers are probably even higher.

The spending attitude in China is far heathier than in developed countries, where consumption has stalled in recent years. Consumption is rising 14 per cent a year among the under 35s (twice that of older generations). Another recent McKinsey study found that 55 per cent of consumers in China are confident that their incomes will rise significantly over the next five years. Furthermore, Boston Consulting Group predicts that even if economic growth falls to 5.5 per cent, China's consumer economy will expand exponentially, creating an additional mass equal to the entire consumer economy of Britain or Germany.

Exporting to China: the next big trend?

While many big brands seem very confident about these trends—Pepsi has just opened its first Quaker Oats manufacturing plant in China, Ferrero has recently opened a plant in Hangzhou (its biggest investment outside of Italy), and McDonald's and Starbucks are already pushing to add 1,250 and 500 more outlets respectively—smaller players must be more cautious.

Anna and Artem are two young Russian entrepreneurs that, facing a troubled economy at home, decided to launch an e-commerce platform, importing Russian-manufactured goods to China. They sell products including canned food, beverages and cosmetics. After doing their homework and putting together a strong business plan, they approached several potential investors, until they found people interested in funding them. Their sales in China are made both offline and online, taking advantage of the new e-commerce wave. The decrease in the ruble and a strongly appreciating RMB has also given them an additional competitive advantage.

With a long history of excellence in producing consumer goods, exporting to China could well be the next trend for developed countries such as Australia, Italy, France or Spain. Developed countries that are able to produce more than they need and that have built brands over the decades tend to excel in exporting consumer and capital goods to China.

In a July 2016 special report on China, *The Economist* lays out all of China's paradoxes regarding politics, society and the distribution of wealth. However, the article still struggles to explain the resilience of the current Chinese economic model. The article also referenced McKinsey's data, which estimates the Chinese middle class to have reached 225 million households—with an additional 50 million households predicted by 2020—compared with only 5 million in 2000, and with an annual income between USD 11,500 and 43,000.

Tahsin Toraman is a businessman that relocated to

Shanghai three years ago. With a strong background in medical consumables, he intends to tap into one of the biggest opportunities of all time: China's ageing population.

"To come to China was a tough decision but the opportunities here are unbelievable…to build a business from scratch is probably more difficult here than anywhere else. It can also be very rewarding," says Toramin. "You are on your own and all the information is confusing…before choosing my service providers, I met 20 of about 40 that I found over the Internet. Believe me, it wasn't about the money, it was about trust. They had to show me that they knew what they were talking about, solve my problems and that I could trust them. This place is so difficult that you need to be able to rely on your advisers," he concludes.

Conclusion

There are several recurring issues that small (and large) foreign businesses face when doing business in China, and several constants that characterise those that are successful. An unpredictable legislative environment, administrative issues and discretionary law enforcement are three of the main recurring issues pointed out by longstanding, resident foreign businesses. The result is that many small businesses will have their best people working to solve these problems instead of focusing on generating business. The only solution, to at least mitigate risks here, is to find a trusted adviser that can navigate you through these challenges.

As China is becoming a second-home market for many SMEs, you will need to send your best people on the ground to stay on top of the changing market, while still understanding its fundamental Chinese characteristics. Local managers will need direct access to headquarters to keep abreast of changes and adapt to new challenges and opportunities.

As the war for talent goes on, companies will struggle to recruit and retain good employees. Identifying strong technical skills in prospective local employees, though not easy, may be more important in developing business than individuals with strong English-language skills.

Finally, newcomers will need to budget wisely as China is not cheap, especially when the aim is to sell consumer goods and services, which requires localisation downtown in big cities. Rent, human resources and administration costs might be very high and taxes are not as low as you would expect. However, as Toraman rightly puts it, "to come to China was a tough decision but the opportunities here are unbelievable." Eb

Rosario Di Maggio *has over 13 years' experience in assisting SMEs with their foreign direct investment projects in Asia. He specialises in business structuring, international taxation and regulatory compliance. Di Maggio is also Chair of the European Chamber's SME Forum.* ***Vistra*** *is a global independent provider of corporate services with 2,500 professionals and 63 offices in 40 jurisdictions. In China, Vistra is present with about 160 professionals in four major cities: Shanghai, Beijing, Guangzhou and Shenzhen. Our China team is dedicated to providing high-quality, tailored corporate services including company formation, accounting and tax compliance, HR advisory, payroll and company secretarial services.*

STARTING SMALL, THINKING BIG

Building a better platform for SME growth

One of the keys to SMEs' success is a focus on long-term economic growth and financial stability. They should start by adopting a business model that not only enhances performance, say **Joe Carr**, Global Leader of SME Advisory Services and **Fabrice Demarigny**, Global Leader of Capital Markets, **Mazars**, but also one that has a positive impact on society.

Small and medium-sized enterprises (SMEs) have been particularly hard hit by China's slowing economic growth. Yet, as they employ more than 65 per cent of the global, private sector workforce and account for 52 per cent of total gross value added,[1] SMEs should merit an increased level of support from government, trade bodies and trusted financial advisors on the particular challenges they face.

[1] The Association of Chartered Certified Accountants (ACCA)

One of the main challenges facing SMEs is their inability to fully participate in Chinese markets. Access to global value chains is a crucial component of growth, yet many SMEs find themselves excluded. In particular, lending restrictions, following the financial recession, has meant that SMEs have seen their access to finance curtailed, which has in turn acted as a barrier to market entry.

Challenging the barriers to inclusiveness

The challenge to improve market participation and access to finance is among a set of issues that are important to SMEs. Initiatives designed to remove the obstacles that SMEs are facing include improving the transparency and availability of data on SMEs to help reduce the risks associated with lending to them.

A realignment of the regulatory and capital market landscape, to allow SMEs greater freedom to participate in global markets, is another element of change required. The development of tailored financial instruments such as loan guarantees, as well as a review of transaction laws and the encouragement of equity finance, will help provide a firmer footing for SMEs to operate more effectively.

Perhaps the biggest challenge, though, is to provide support to SMEs embarking on expansion programmes. Access to local market information, protecting rights and compliance with international labour, social, environmental and quality standard laws can add considerably to the complexity and costs that SMEs face. Greater technical assistance and advice on how SMEs can deal with these issues is therefore an essential part of the policy recommendations now on the table.

Reforming the landscape in which SMEs operate is without doubt an ongoing process. New research, continued debate and participation in legislative and regulatory change, as well as the formulation and adoption of new financial tools that both harness and develop SME growth, should be welcomed. Making more practical information available on how the SME sector functions can only help to shed further light on the particular constraints SMEs experience, as well as how they can overcome such hurdles.

Achieving a sustainable balance

Some recent research that we carried out,[2] shows that the success of SMEs is not solely reliant on the removal of market barriers. It is also about how they react to changes in the operational environment. As a result of the so-called ‘new normal’, many SMEs find themselves in a very competitive space where organic growth is now difficult.

The statistics suggest the need for some tough choices. In addition to repositioning a product or service offering, consolidation with other SMEs to achieve economies of scale at regional or national level could also be a viable consideration, not least to improve access to credit, which tends to favour larger organisations. Having said this, it is important to recognise that there is often a trade-off between size and the inherent ability to react quicker to fast-changing market conditions and customer requirements that is the trademark of SMEs. In addition to this agility, which enables them to make decisions quicker than larger firms, SMEs have often developed stronger personal relationships with their clients which is an important ingredient for better business in society.

Better access to finance is a key agility factor for SMEs. In addition to access to credit, funding through capital markets should also play a major role. This can be achieved by encouraging angel investment, venture capital and private-equity investment with appropriate tax incentives and pooling of investment vehicles. It also requires making sure that disclosure and other regulatory requirements for smaller firms are more proportionate in order to facilitate greater issuance and trading of SMEs’ debt and equity.

Getting the balance right is therefore crucial. Rather than simply trusting that bigger is better, the more useful lesson to learn is that SMEs should ‘right-size’. So if a company is staying small it needs to ensure it maintains a niche focus and that it is deeply rooted in supply chains and the wider ecosystem to ensure the benefits of critical mass can be leveraged. This may involve outsourcing non-core activities and developing strong partnerships with others as an alternative to internal organic growth. Linking to important sectoral clusters and ecosystems to enhance value chains and remaining abreast of sectoral innovations and best practices is one way of staying ahead.

Lessons for SMEs

Certainly more in-depth analysis of the SME sector will help towards the formulation and adoption of high-level principles such as beneficial ownership transparency. Transparency around ownership and control of companies is a key issue in the battle against corruption, money laundering and tax evasion. Getting a consistent cross-border approach to beneficial ownership transparency, whereby there is agreement on benchmarking and compliance standards, will help simplify and reduce the burden experienced by all businesses, but particularly SMEs.

Governments, trade bodies and professional firms now have an important role to play in raising awareness of the strategic challenges facing SMEs. Central to this is the will and expertise to promote and participate in effective regulation, trust and transparency so that businesses gain the capacity to change for good. Eb

***Mazars** is an international, integrated and independent organisation, specialising in audit, accountancy, tax, legal and advisory services. As of 1st January, 2016, Mazars operates throughout the 77 countries that make up its integrated partnership. We draw on the expertise of 17,000 professionals to assist major international groups, SMEs, private investors and public bodies at every stage of their development.*

[2] *How to be a Stand Out SME: A Performance Study of the EU SME Sector for the Period 2008–2013*, Mazars, <http://www.mazars.co.uk/Home/Your-needs/Owner-managed-businesses/How-to-be-a-Stand-Out-SME>

A CASE IN POINT

Real-life IPR infringement cases

Even though China's IPR regime has improved over the years, counterfeiting and other IP infringements are still commonplace, making IP protection a priority when doing business in or with China. In order to demonstrate the importance of IP protection for European SMEs, the **China IPR SME Helpdesk** have provided two case studies involving European SMEs that were victims of IP infringement in China. The first case study demonstrates the importance of IP registration and IP regulation with contracts; the second shows how important it is to be informed of the details and nuances of China's IP protection regime.

Case study 1

SME background

Nationality: Dutch

Industry: Producer of additives

Status in China: WFOE

Case

A Dutch SME produces their additives in China under the name Roi Jaguar. Their general manager in China is tasked with making sure that the brand is protected in accordance with Chinese law. At one point the Chinese general manager leaves the company. Soon after he leaves, the Dutch SME discovers a very similar product on the Indian market called Roi Lynx. Both brands thus exist with the same word followed by the name of a species of big cat.

After some research, the Dutch SME finds out that after quitting the job its former general manager has started competing against it with very similar products. Also, after consulting the China IPR SME Helpdesk, the SME finds out the manager has registered the trademarks of the company in China in his own name instead of under the Dutch company in China.

The situation escalates due to some other related outstanding issues for which the former general manager still demands certain payments. The Dutch company refuses, so the former general manager goes to the local Authority of Industry and Commerce (AIC) and shows them the trademark certificate of Roi Jaguar, which results in the AIC confiscating the infringing products of the Dutch SME that carry the name Roi Jaguar. As the Chinese trademark registration is in the name of the former general manager, and the Dutch SME does not have the legal right to the name Roi Jaguar, the former general manager legally closes down the business of the Dutch SME with regard to the brand Roi Jaguar.

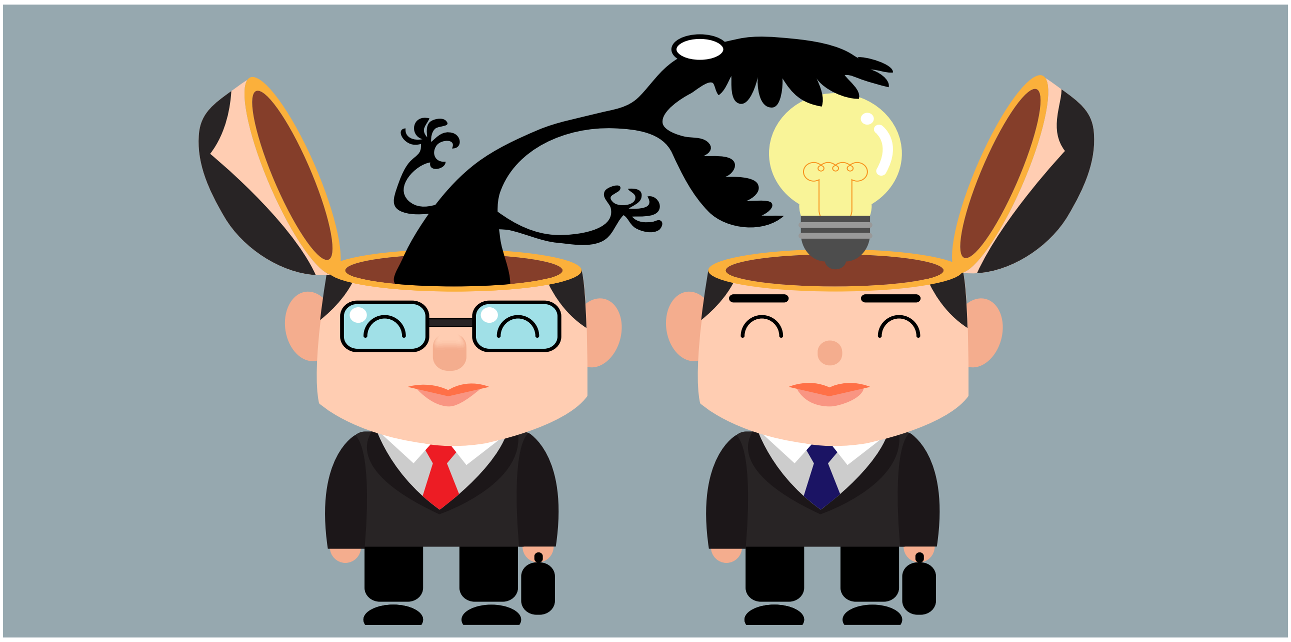
Action taken

The trademark registration carried out by the former general manager was done in bad-faith due to his existing relationship with the Dutch SME. The Dutch SME thus filed for a trademark cancellation as the trademark was registered in bad faith, and then subsequently applied for the trademark itself.

After first having filed the trademark cancellation, which temporarily stopped infringement of the Roi Jaguar trademark, the Dutch SME continued to produce the product, but under a different product name. Before the new product name was used, the company checked that there were no conflicting trademarks that had already been registered in China, with regard to additives for that new name. The Dutch SME then registered the wordmark, logo and the Chinese character name of the new product. Once the cancellation was concluded and the trademark was applied for in the Dutch SME's name, the Dutch SME was able to put its products under the Roi Jaguar name back on the market.

Lessons learned

- Be on top of trademark registrations in China, and make sure the registration of the trademark is conducted in your own company name.
- Draft your contracts with care and with the assistance of legal professionals and translators to make sure that all terms, conditions and obligations are clear for both parties.



Case study 2

SME background

Nationality: Spanish

Industry: Scientific research and development

Status in China: Market entry

Case

A Spanish SME in the scientific research and development industry has patents on certain cutting edge surgical instruments, all around the world, including China. At an international exposition of surgical instruments the Spanish Company discovers a Chinese company advertising their patented products under the name of the Chinese company. The Spanish company obtains flyers and photos of the products. However, the Spanish company is also concerned that the Chinese company might have defensive utility model patents in place. Since utility model patents are approved quickly (usually within one year) and do not require an official examination of novelty, inventiveness and industrial applicability, this could potentially bar the Spanish company from entering the Chinese market.

Action taken

The flyers and photos of the products obtained by the Spanish company were not recognised as evidence under Chinese law. In China, potential evidence must be notarised by a Chinese notary public before it is recognised as official evidence. Therefore, the Spanish company hired a law firm and a Chinese notary public to facilitate this process.

The company first employed a patent attorney to make correct assessments on whether infringement actually occurred and on the patent portfolio of the Chinese company. This was necessary because Chinese companies often use defensive patents against foreign companies to scare them away from the Chinese market and from going through the financial burden of a patent infringement case.

If it were to go to a defensive patent case, the Chinese company would claim the original patents of the Spanish SME to be invalid and that the SME is therefore infringing upon the patents of the Chinese company, which are often utility model patents.

After conducting a patent search, it was revealed that the Chinese company indeed owns many utility model patents.

The Spanish company's patent attorney will now need to carry out a patent assessment with regards to the infringement case after the notarised evidence is obtained. After obtaining the evidence, the Spanish company then has three options. The first would be to negotiate with the Chinese company to stop the infringement. The second would be to take administrative action through the local Intellectual Property Office where the infringer is located in order to raid the premises and confiscate and destroy the infringing goods and to penalise the company. The Spanish SME also has a third option of starting a court action against the Chinese company in order to obtain a long-term solution to the infringement.

Lessons learned

- Make sure evidence is notarised in China by a Chinese notary public.
- Assess a competitor's patent portfolio before taking action.
- Assess whether or not a Chinese patent is infringed before you start any enforcement against a Chinese infringer. Eb

*The China **IPR SME Helpdesk** supports small and medium sized enterprises (SMEs) from European Union (EU) member states to protect and enforce their Intellectual Property Rights (IPR) in or relating to China, Hong Kong, Macao and Taiwan, through the provision of free information and services. The Helpdesk provides jargon-free, first-line, confidential advice on intellectual property and related issues, along with training events, materials and online resources. Individual SMEs and SME intermediaries can submit their IPR queries via email (question@china-iprhelpdesk.eu) and gain access to a panel of experts, in order to receive free and confidential first-line advice within 3 working days.*

CHINA IPR SME HELPDESK

EUROPEAN CHAMBER LOBBYING HIGHLIGHTS

Catching up with the Belgian Prime Minister in Beijing

European Chamber President Joerg Wuttke met with Belgian Prime Minister Charles Michel at the Belgian Embassy in Beijing on 30th October. President Wuttke spoke to Prime Minister Michel about the Chamber's *European Business in China Position Paper 2016/2017*, before going on to discuss specifically how the Chamber lobbies the Chinese authorities on behalf of Belgian companies in the market.

President Wuttke Shares Views with Vice Premier Ma Kai and Vice President Katainen

As a sideline to the High-level Economic and Trade Dialogue held between the EU and China in Brussels on 19th October, European Chamber President Joerg Wuttke attended a breakfast with European Commission Vice President Katainen and Chinese Vice Premier Ma Kai. President Wuttke commented that he was encouraged by Vice Premier Ma's pledge that reform efforts will not slow down. He also called on the Chinese authorities to implement the Made in China 2025 initiative to upgrade China's industrial base in an inclusive manner and to refrain from using subsidies to support 'indigenous innovation', as doing so can be expected to distort market access.

Chamber Delegation Visits Shenzhen Vice Mayor

On 27th September, Chamber President Joerg Wuttke led a major Chamber delegation, including members of its Executive Committee and the board of the South China Chapter, to meet with Shenzhen Vice Mayor Mr Chen Biao. Also in attendance were representatives of Invest Shenzhen, the Shenzhen Municipal Foreign Affairs Office, the Shenzhen Municipal Economy, Trade and Information Commission, the Shenzhen Municipal Market Supervision Bureau MOFCOM Representative office, the Shenzhen SME Association and the Shenzhen International Exchange and Corporation Foundation. After the delegation had introduced the Chamber's work to the Shenzhen authorities, Vice Mayor Chen shared his views on the latest developments in the city's economy. He also introduced the heads of several government departments in order to ensure that working-level cooperation can continue to move forward. At the conclusion of the meeting, Vice Mayor Chen was presented with a copy of the Chamber's *European Business in China Position Paper 2016/2017*.

CCPIT Secretary General Receives Chamber Publications

On 14th October, Shanghai Chapter General Manager Dr Ioana Kraft met with Mr Zhao Jiandong, Secretary General of the Chinese Council for the Promotion of International Trade (CCPIT) Shanghai. After presenting Mr Zhao with copies of the *Business Confidence Survey 2016* and the *Position Paper 2016/2017*, Dr Kraft outlined the history and focus of the European Chamber and some of the key takeaways from the two publications. Secretary General Zhao spoke highly of the Chamber's work and proposed to further develop cooperation between the two organisations by jointly organising some seminars of interest to members of both organisations as well as by assisting companies in match-making.

Joint Meeting with MOFCOM

Chamber Vice President Sara Marchetta and Beijing Chapter General Manager and Head of Government Affairs Maggie Xie joined representatives of the American Chamber of Commerce and the Chinese Association of Enterprises with Foreign Investment on 21st September, to meet with the Foreign Investment Administration of the Ministry of Commerce (MOFCOM). Deputy Director General Fan Wenjie highlighted the key points of the *Interim Measures on the Filing System for Establishment and Change of Foreign-Investment Enterprises* (*Interim Measures*), on which the MOFCOM has been calling for public comments. Vice President Marchetta extended the Chamber's appreciation to the MOFCOM for making the effort to better facilitate foreign-invested enterprises' business in China and shared some suggestions on the *Interim Measures*. General Manager Xie made inquiries about the legislation plan for the *Foreign Investment Law*.

Discussing Cooperation Opportunities with Yiwu Vice Mayor

Shanghai Chapter Vice Chair Marcus Wassmuth and the Vice Mayor of Yiwu, Xiong Tao, met on 20th September to discuss opportunities to expand cooperation between Yiwu City and the European Chamber. During the meeting Vice Mayor Xiong outlined recent developments with the Yiwu-Europe Smart Industrial Park, new freight train routes and policies that are being adopted in order to improve Yiwu's business environment. Vice Chair Wassmuth expressed appreciation for the efforts that have been made to improve operating conditions for business in Yiwu and gave a positive view of Yiwu's future development prospects. Both sides agreed to work toward fostering cooperation between European business and Yiwu in the logistics, financial and manufacturing sectors.

DRIVING CHANGE IN CHINA

Introduction of new commercial vehicle standard represents Chamber lobbying success

From 1st January, 2017, China's roads are set to become a little bit safer. With the promulgation of GB1589-2016, which governs the legally-allowed weight and dimensions of commercial vehicles, the playing field for European and Chinese vehicle manufacturers will also become more level. **Mats Harborn**, former Chamber Vice President and Vice Chair of the **Automotive Working Group**, explains the new standard in the context of China's overall reform drive.

China is undergoing change on a scale perhaps unprecedented in the history of mankind: if it is to continue to prosper, it now needs to undergo deep and comprehensive reform. So frustrated is President Xi Jinping by the lack of understanding in China about what reform really means, that on 10th May he used the official Party newspaper, *People's Daily*, to outline his views on this topic. In the article he reiterates that market forces should play a decisive role in resource allocation, and for that to happen there needs to be a level playing field. That in turn requires all players to abide by the same rules, standards and laws, which cannot be achieved without strict and equal enforcement.

In the field of road transportation, these issues become very concrete, visual and easy to understand. Up until now, the standard regulating the weight and dimensions of commercial vehicles (GB1589-2004) has not been enforced, although a revised standard *was* published and enforced in 2004: instead, in the blind pursuit of economic growth and high GDP numbers at any cost, the regulatory agencies turned a blind eye to violations.

Transportation companies have basically been free to overload and to use both trucks and trailers that violate even the most basic safety standards. Nowhere is this more observable than in the area of car transportation. It is still common to see 30-metre-long semitrailers with cars loaded two levels high and in two rows – one single car carrier can carry over 40 cars. It goes without saying that these vehicles are dangerously long, far too wide and that pressure from their axles badly wears down China's newly-built road network.

Of course, in the short term, such enormous car carriers result in low unit costs per tonne per kilometre, which stimulates economic growth through low prices. However, what has become increasingly obvious in the past few years is that the consequences of this 'growth at any cost' strategy are serious. Again using the car carrier as an example, such externalities can be seen in the form of road accidents, air pollution, reckless competition, and wear and tear of roads and bridges. Who is to bear these costs?

It is exactly this principle that President Xi addresses in his article. China must change its development model from one that pursues blind, inefficient growth to one that is sustainable and resource-lean. Growth has to serve the people and create higher quality of life for all, and that also includes road safety.

What's in the standard?

The Ministry of Transportation, together with the Ministry of Public Security and the Ministry of Industry and Information Technology, took the lead in revising the weights and dimensions standard. This work was started back in 2010, and serves to create a level playing field for road transport companies: by making them all play by the same rules it is hoped that service levels and efficiency will be improved as a result of the innovations that open competition fosters. The new mass and dimension standard—GB1589-2016—was launched on 26th July, and has been in the process of being gradually enforced since 21st September.

GB1589-2016	
Gross trailer weight (GTW)	≤49 tons (6X4 tractor + three axle semitrailer)
Max length of semitrailer	13.75m and 13.95m for 45' container
Max length of tractor + semitrailer	17.1m (18.1m for bonneted cab)
Max length of rigid truck with centre-axle trailer	20m
Max width	2.55m + 5cm for cold chain bodies
Max height	4m (same as EU Directive 96/53/EC)

What impact will the standard have?

This measure should be viewed in the larger context of allowing market forces to play a more decisive role in resource allocation: it demands that the same rules apply for all market players and that they be strictly enforced. This is the basis for rule of law in China, a principle that has been advocated since its promulgation during the Fourth Plenum in 2014, and hence this time around there is great determination to enforce this standard.

The European Chamber and the ACEA (the European Automotive Manufacturers' Association) have for the past five years been deeply involved in the revision of this standard. Violations of both the previous and this new standard represent a great problem for society as a whole, and in particular impact European companies in China that are committed to safety and sustainability and thus comply with Chinese legislation as a matter of course. That so much road transport in China flouts existing standards and regulations is one contributing factor to the higher costs of transport and logistics in China compared with the rest of the world. In China the cost is around 17 per cent of GDP whereas in Europe it is around nine per cent.

Among other things, GB1589-2016 will also affect the design of car transporters – over a period of two years, all cars will need to be transported on compliant, 22-metre-long, 2.55-metre-wide carriers. This means that it will only be possible to transport a maximum of ten cars on one car carrier. At first glance this would imply that four times as many car carriers will be needed to match the same transport capacity. In real life, the change will not be that extreme. China will likely be able to manage with approximately the same number of car carriers, but with each car carrier being used far more efficiently and some other types of vehicle taking over some of the transport flows. Today, the average car carrier drives less than 80,000 km per year; but with

better equipment, higher running speeds and better transport planning, the utilisation rates can be improved and the annual mileage at least tripled. While this will not be easy, it is exactly such challenges that drive progress.

Next steps and implementation

As of 1st January, 2017, all newly-produced vehicles in China will have to adhere to the new masses and dimensions standard. Since non-compliance can result in heavy fines, as well as the cancellation of transport licences, there is a lot of fear in the market: a great deal of existing vehicles do not comply with the standard to a large extent. The good news is that everyone is now aware of GB1589-2016 and understands that the industry will have to adapt. The question that everyone is now asking is, *how long will the government allow the industry to make the necessary adjustments?*

The Chamber has been in close contact with the Ministry of Transport since the No.62 decree, which announced the introduction and enforcement of the standard, was issued. A clarification notice was sent out on 14th October, granting a grace period for the transport operators and equipment manufacturers to adapt. Although the length of the grace period is not clearly defined, it is expected that it will last around one year. However, overloading will no longer be tolerated with immediate effect.

Any company transporting goods in China will henceforth have to follow the new standard GB1589-2016. Any exemptions permitted during the transition period, which allows for higher loading capacity than intended, should not be used in the calculation of freight rates. Instead, better transport planning, higher utilisation rates of equipment, lighter and better-designed equipment will produce a more sustainable transport system in China with more competitive rates.

The intention of reform, as President Xi has stated many times, is that innovation will be the new driver of the Chinese economy. Innovation is not only about technology, it is also about business models and management. China has entered a period in its economic development where the old model for growth is void. Thus, the phrase 'new normal' was born, which is, in essence, about getting more value out of fewer resources and creating more sustainable business models.

Nowhere will this change be more visible than in the area of road transport. Put another way, if we do not see China's roads becoming safer, it may imply that the reform programme has failed… Eb

For more information on this standard, please contact the Automotive Working Group: Ink Zheng at izheng@europeanchamber.com.cn, 010 6462 2066 ext 23.

RISE OF THE MACHINES

Robot industry leads China Manufacturing 2025 strategy

With its vast manufacturing base and diminishing workforce, China's appetite for robots is increasing fast. One in four of the industrial robots sold in the world last year was in China, totalling 68,000 units, a 17 per cent increase over the previous year.[1] Being the manufacturing engine of China how are Guangdong's factories reacting to the new industrial revolution? And what is the local government doing to support it? **Nick Chen**, Senior Project Manager at the **Foshan National High Tech Industrial Development Zone** (**FHIDZ**), takes a look.

[1] The Association of Chartered Certified Accountants (ACCA)

The robotics industry and its market in China

China has been the largest industrial robot market in the world since 2013. Driven by market demand and government support, China's robot industry is having to develop at an unprecedented rate in order to tackle the challenges presented by a dwindling workforce. It is estimated that by 2018, China's robot market will account for over a third of the industrial robots installed worldwide.

Due to early market entry, the robot market in China is currently dominated by foreign industry giants: ABB from Switzerland, FANUC and YASKAWA from Japan, and KUKA from Germany are all major players. In total, foreign-invested robotics companies account for over 70 per cent of the domestic industrial robot market.[2]

Meanwhile, domestic Chinese players have been somewhat lagging behind their international counterparts. They have historically faced problems due to a lack of the technological know-how required to produce high-quality key robot components, such as motor drives, gearboxes and controllers. As a result, many tended to specialise in the niche market – at present, domestic industrial robotics are mainly in the field of handling, loading and unloading, welding and brazing, assembly and disassembly, coating and sealing, processing and cleaning. Encouraged by a series of supporting policies, however, Chinese domestic players are beginning to catch up. There are over 800 companies involved in robotics manufacturing, and over 40 industrial parks focused in the robotics industry all over China.[3] The service scope of industrial robots has reached 36 national economic segments and 87 industrial sectors.[4]

The deployment of industrial robots is visible in many manufacturing companies in China, led by manufacturing clusters in some of South China's cities, such as Foshan and Dongguan. As early as 2012, the FAW - Volkswagen Foshan factory, which is located in Foshan National High Tech Zone, has been recognised as the plant with the highest degree of automation in China. There are 884 robots in its welding workshop, which covers a total of 91,000 square metres, and the level of automation is up to 70 per cent.[5]

Entrepreneurs interested in robotics are naturally gathering in designated areas that have been selected and supported by the government for this purpose. For example, Foshan has built several clusters for the robotics industry under the policy of national and local government. In these robotics industry bases, Chinese entrepreneurs, scholars and researchers are being summoned to work on the R&D and application of robotics.

In the Guangdong Technology University CNC Equipment Cooperative Innovation Institute, around 50 enterprises have registered, 21 of which are related to the robotics industry.[6] The institute's president, Yang Haidong, says that although most of the robotics companies in Foshan are SMEs, they all have their own unique, competitive advantages. According to Yang, Foshan robotics enterprises have four chief characteristics: first, they are specialised in different industrial segments of their own; second, they have strong R&D capability – almost all of the enterprises possess high-end research talent and professors, giving them a remarkable innovation advantage; third, they are very adaptive to the market and have strong expansion capability; finally, they share the concept of mutual development – they tend to collaborate with each other when working on major projects.[7]

The motivation to replace manual labour with robotics

The Chinese Government realised that the economic slowdown occurred, in part, due to its economic growth model leveraged by cheap labour. Since labour costs have exceeded 10 per cent of annual growth, many low-end manufacturing companies have been leaving China in favour of other cheaper Southeast Asian countries. In order to prevent the hollowing-out effect and the problems associated with the inevitable ageing workforce, the government has been strongly motivated to aggressively promote the application of robots in its manufacturing industry. It is expected by some that an economic model driven by the application of robots will lead to a new wave of steady and robust growth.

The main advantages of applying industrial robots are: 1) improved productivity; 2) an alleviation of labour costs; 3) a solution to the problem of recruiting workers, since less people are willing to do repetitive work; 4) guaranteed precision and speed of the tasks, and durability; 5) improved workplace safety by reducing the occurrence of occupational accidents; and 6) improved competitiveness and quality of China's manufacturing sector.

Government policies and financing

Since 2006, more than six Chinese state plans have set targets for China's industrial robotics sector. The recent Made in China 2025 initiative is the most ambitious, aiming to comprehensively upgrade China's manufacturing sector through the production and application of industrial robots. President Xi Jinping himself has said that the "robotics revolution" promised to become the "third Industrial Revolution," and that people regard industrial robots as the "jewel in the crown of manufacturing".[8] It is both high- and working-level support from China's leaders, and targeted government planning, that is sustaining the demand for, and driving China's own production of, robotics.

At the national level, in 2013, the Ministry of Industry and Information Technology released the *Guidance on Promotion of Development of the Robot Industry* to boost robot development. The guidance sets forth the objectives for the Chinese robot industry up to 2020. Featured policies include: attracting and assisting three to five world-leading

[2] http://mt.sohu.com/20160804/n462521232.shtml
[3] http://mt.sohu.com/20160804/n462521232.shtml
[4] http://mt.sohu.com/20160804/n462521232.shtml
[5] http://www.fs-hitech.gov.cn/news/201610/t20161021_6177191.html
[6] http://www.fsonline.com.cn/2016/1019/226463.shtml
[7] http://www.fsonline.com.cn/2016/1019/226463.shtml
[8] J. Ray et al (2016), China's Industrial and Military Robotics Development, Center for Intelligence Research and Analysis

robot companies to operate in China; developing eight to ten robot-related industrial fields; and promoting the application of robots to factories, outlining a robot population density of over 100 robots per 10,000 plant workers.[9]

At the local level, governments have set up investment funds and specialised capital to guide robotics innovation. In the coming the years, the Foshan Government plans to invest CNY 900 million in order to support the development of the robot industry.[10] It is also implementing a multi-layer supportive policy for machine-tool manufacturing enterprises. Furthermore, the Nanhai Park in Foshan founded the Robotics Industry Indigenous Innovation Supportive Sub-Fund in order to encourage enterprises to file for brand registration, formulate standards and to join exhibitions in groups. In 2015, an accumulated supportive fund of CNY 65 million was distributed to this sub-fund.[11]

China is also investing heavily in emerging technologies, such as artificial intelligence (AI) and nanotechnology, which can fundamentally change the capabilities of robot systems. Numerous finance and investment institutions are rightly keeping a close eye on the future of China's robotics industry. Listed companies are being actively encouraged to participate in capital contribution or technology acquisition, and this is already taking place. Chinese state-owned conglomerates, companies and venture capital firms are all actively acquiring and investing in AI and foreign robotics technologies companies, particularly in Europe. While national plans seem to guide these acquisitions by prescribing which advanced technologies Chinese firms should acquire, it is the involvement of the finance sector that is considered the indispensable force that can transform China's robotics industry from a follower to a frontrunner.

In order to provide funding assistance for the sustainable development of robotics companies, the Foshan Government has established a Robotics Mortgage Centre to attract funding. The Centre will gather qualified financing and leasing companies that can help companies to manage robotics installation projects through registering, financing and risk assessment. Additionally, subsidies will be available for companies using the mortgage service. This will allow factories to purchase robots through instalments while maintaining healthy liquidity. Eb

Foshan Hi-tech Industrial Development Zone (FHIDZ)*, a national-level, high-tech industrial development zone, was established with the approval of the State Council in December 1992. The FHIDZ is dedicated to building a "Golden Valley of Chinese Wisdom Manufacturing". It has become the major engine for technological innovation and the industrial upgrading of Foshan City. It is also an important component of the PRD National Indigenous Innovation Pilot Zone, and has attracted 61 Global Fortune 500 related enterprises, 44 listed companies and 380 enterprises with an output value of more than CNY 100 million.*

9 https://www.mizuhobank.com/service/global/cndb/economics/msif/pdf/R516-0002-XF-0105.pdf

10 http://www.fs-hitech.gov.cn/news/201610/t20161021_6177191.html

11 http://www.fs-hitech.gov.cn/news/201609/t20160919_6172631.html

Moroccan Foreign Minister and COP22 President Salaheddine Mezouar and French Environment Minister Segolene Royal at the COP22 opening ceremony in Marrakech

COP22

Insights from the action in Marrakech

For the second consecutive year, the European Chamber sent a delegation of observers to the Conference of Parties (COP22) of the United Nations Framework Convention on Climate Change (UNFCCC). Labelled by many as the 'African COP' or the 'COP of Action', it was held in Bab Ighli, Marrakech, Morocco from 7th to 18th November. According to **Renato Roldao**, Consulting Director – Climate Change at **ICF**, and Chair of the European Chamber's **Carbon Market Sub-working Group**, expectations this year were very high following the success of the COP21 in Paris in 2015. However, Roldao says that it was also clear from the beginning that COP22 would be much more a 'working-level' COP and the beginning of the process to transfer words into actions and prepare the means of implementing the Paris Agreement.

About a month has passed since the Paris Agreement entered into force on 4th November, 2016. As of 29th November, 2016, 114 of the 197 Parties to the Convention have ratified it and this number keeps growing. For those interested in more details of the progress that it is being made in terms of implementation of the Paris Agreement and how the world is taking it forward you can follow it using the United Nations' climate change progress tracker.[1]

The fact that the Paris Agreement is there at all, as a robust and long-lasting agreement, is in itself a guarantee that will allow for the necessary actions and increasing level of ambition to feed into the overall process off controlling climate change. Only through ambitious and collective action can the objective of keeping any increase in global temperatures between 1.5°C and 2°C, with global emissions to peak as soon as possible, be achieved.

While in Marrakech, I participated in two side events hosted at the International Emissions Association (IETA) business hub, dedicated to carbon markets. At these two events I had the opportunity to share my experience in supporting the design and implementation of the China national Emissions Trading Scheme (CETS) under the EU-China ETS Project (EuropeAid), the main design features of the CETS and the capacity building programme behind it to support the roll out of the world's biggest carbon market. I presented side by side with representatives from industry, academia and government from around Asia, such as Korea, Japan, Vietnam and Taiwan. In total, I counted at least four side events that took place during the two weeks of COP22 where the CETS was the central focus, but where the emerging cooperation on carbon markets across Asia also clearly stood out.

Article 6 of the Paris Agreement "establishes a mechanism to contribute to the mitigation of greenhouse gas emissions (GHG) and support sustainable development" and the possible use of markets. The article provides new impetus to the development of cooperative approaches between carbon markets and I believe that the discussions that took place in Marrakech will help to operationalise this article further down the road.

The *Marrakech Action Proclamation: for our Climate and Sustainable Development* was one of the documents released at the end of COP22. While there is not much novelty in its content, it will play an important role in the process ahead as it unites nations in the determination to implement the Paris Agreement and associated Sustainable Development Goals (SDGs). This is all very positive and shows that governments are willing to work together. It also sends a strong signal that we have unstoppable global momentum on climate change and sustainable development.

Another relevant document that was released in Marrakech was the *Marrakech Partnership for Global Climate Action*. Among other things it sets the outlook to 2020, stating: "Party and non-Party stakeholders have emphasized the need for a coherent process to support greater ambition in the period from 2017-2020 in accordance with the Paris decision. In the lead up to COP 24 a step wise approach will be facilitated with a focus on the delivery of results."

[9] http://unfccc.int/files/paris_agreement/application/pdf/pa_progress_tracker_281116.pdf

Key outcomes of COP22 and next steps

- I saw unparalleled political will to act on climate change.
- Marrakech featured close cooperation to advance critical issues, which can be seen in the conference outcomes. Governments took a crucial step towards writing the rules of the Paris Agreement. They outlined the finance, technology and capacity building support that enables the developing world to move to low-emission development and build resilience. Marrakech featured long-term de-carbonisation plans from major emitters and medium-income countries.
- Marrakech shined a light on movement in markets and in the private sector, and it highlighted climate actions by local governments.

Business and city/local government level initiatives launched or scaled up at COP22

- UN Global Compact
- Under2MOU
- NDC Partnership
- RE100 and EP100
- World Alliance on Clean Technologies
- The role of Agriculture in climate action

COP22 gave another boost to climate actions from companies that will be able to use science-based targets to reduce their emissions. Cities, sub-national government entities and individuals / civil society in general are already answering this call for action. Overall I noted that the main outcomes from Marrakech are in line with the European Chamber's *Carbon Market Sub-working Group Position Paper* in terms of the role that needs to be played by business and local governments.

Despite the 'Trump effect', which could have disrupted the work taking place at COP22 in many ways and negatively impacted the morale of delegates and observers, the opposite effect could be observed at all corners of COP22. It sent a very strong message that the journey towards a climate-resilient world with a low carbon economy is on an irreversible pathway, and that the momentum to make it happen bottom-up is there.

Indeed it was almost unanimously agreed among those on the ground that this UNFCCC gathering in Marrakech reinforced the message to the world that multilateralism under the UN is the best approach to combatting climate change. Next year's COP23 will be hosted by Fiji but will take place at the UNFCCC Secretariat Headquarters in Boon. It sets up 2018 as an important milestone to complete the work that was started in Marrakech.

***Renato Roldao**, Consulting Director – Climate Change at **ICF** and Chair of the European Chamber's **Carbon Market Sub-working Group**, led the Chamber's delegation of observers to the twenty-second Conference of Parties (COP22) of the United Nations Framework Convention on Climate Change (UNFCCC). Roldao is also the EU-China ETS Project (EuropeAid) Team Leader.*

EUROPEAN CHAMBER EVENTS GALLERY

BEIJING CHAPTER

1


2


3

Cybersecurity in the Era of Industry 4.0 and the Internet of Things (1)
On 26th October, the Chamber organised a conference on cybersecurity, focussing on how companies can enhance security in this bold new era. We would like to thank our sponsor SAP.

Human Capital Conference 2016: The Art of Attraction (2)
On 9th November, the Chamber held our annual Human Capital Conference. We would like to thank our sponsors Cornerstone, YCIS, National School of Development at Peking University, LinkedIn, Raffles Medical, ClubMed.

How to Identify and Prevent Supply Chain Risk in Emerging Markets with Advanced Analytics (3)
On 22nd November, the Chamber hosted a supply chain seminar. We would like to thank our sponsor Huaxia Dun & Bradstreet.

NANJING CHAPTER


1


2

BBQ Night (1&2)
The Chamber and Baden-Württemberg International jointly organised an evening of BBQ and networking on 20th October, 2016.

SHANGHAI CHAPTER

1

China Investment Conference: Innovation for China and for the World (1)

The Chamber's China Investment Conference took place on 26th September. The event provided a comprehensive overview of what's driving investment in China. We thank our sponsors Caohejing Hi-Tech Park, NJIPC, TEDA and 96357 International Investment Public Service Platform.

2

Compliance Conference 2016: Navigating Compliance Risks in China (2)

On 18th October the Chamber's Compliance Conference provided crucial insights on leading best practices and the role of technology in compliance in an ever-changing regulatory landscape. We thank our sponsors Ernst & Young Fraud Investigation and Dispute Services (EY FIDS) and ShangYanTong.

3

2nd CEO Talk: CSR Versus Profitability (3)

On 26th October, Mr Ming Cheng Chien, CEO of LANXESS Greater China, shared with attendees CSR models in the chemical sector and best practices. We thank Caring magazine for their support.

4

China Innovation and R&D Conference: Creating the environment for IP-Driven Innovation (4)

The Chamber's China Innovation and R&D Conference took place on 18th November. Attendees heard from IP and innovation experts on how to avoid IP pitfalls and utilise the benefits of innovation in China.

TIANJIN CHAPTER

1

The 11th European Business Gala Dinner (1)

The 11th European Business Gala Dinner took place on 21st October, 2016, with more than 200 attendees. A special thank you to our sponsors: Airbus, United Family Hospital, Siemens, International School of Tianjin, Wago and Wellington

2

Tianjin Chapter Inaugural Badminton Tournament(2)

The Tianjin Chapter's first-ever badminton tournament took place on 20th November. Eight teams comprising nearly 100 persons participated. Special thank you to our title sponsor National School of Development at Peking University.

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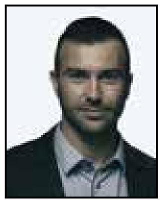
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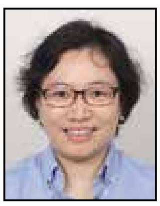
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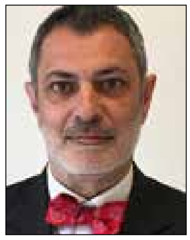
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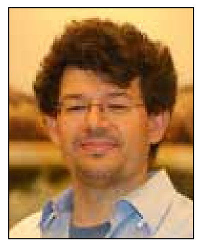
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