

Eva PEREA

ACCESSING THE CHINESE MARKET

*A critical look at the challenges and
best practices of Spanish firms*

Tesis Doctoral
dirigida por
Dr. Ferran PORTA JACQUES

Universitat Abat Oliba CEU
FACULTAD DE CIENCIAS SOCIALES
International PhD

Departamento de Ciencias Económicas y Empresariales
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*Standing by the deep valley makes you think deep,
and scaling the heights makes you aim high.*

Read at the Humble Administrator's Garden in Suzhou,
July 2011.

*Success depends upon previous preparation,
and without such preparation, there is sure to be failure*

CONFUCIUS
(Chinese philosopher, 551-479 BC)

Abstract

China represents today the world's most-attractive emerging market. Most economic indicators agree on this. China embodies a country with a thriving GDP, a growing urban population, a burgeoning middle class and an increase in both private and public spending. In spite of all this, Spanish exports to China are still very low and underscore an unfavourable and chronic trade deficit. Efforts are being made to redress this trade imbalance. The evolution from 2009 onwards shows an increase in Spanish exports to China, a small reduction in the deficit and an increase in the Direct Foreign Investment. However, put together this still represents a very modest change.

The present paper is based on three hypotheses: in the first place, accessing the Chinese market dictates that foreign firms in general, and Spanish ones in particular, adapt their products or services to this specific market. In the second place, China offers an attractive market made up of many consumers and a significant emerging middle class. Spain is not taking advantage fully of this opportunity. Finally, accessing the Chinese market is full of obstacles: it requires a significant investment, skilled staff, a long payback period, much patience and endurance. Therefore, it is a market only accessible for large firms.

While the first two are confirmed, the third one is not. Some large and highly recognised Spanish brands are being very successful in China. But there are also hundreds of smaller ones that operate fruitfully in this country, in all sectors. The survey has confirmed that there are significant chances for success independent of the company size. The crucial question is to have a very clear strategy for implementation. Therefore we can conclude that it is not mainly about size (even if that can help at times) but about having a clear strategy and fulfilling certain requirements that will be analysed in detail.

A thorough research has been carried out using quantitative and qualitative data. A questionnaire was sent to Spanish firms in China to categorise who they are and identify the opportunities found; study their difficulties and future plans in the country; to find out the best practices: a practical framework for corporate performance that will support practical strategic action for our businesses. All these variables are found fully developed in the chapters ahead.

Finally, we may conclude that the world is moving at a turbulent pace and businesses try to adapt quickly to those changes. If in the recent past, western firms moved to China to access their cheap labour cost, nowadays they try to access the growing domestic market. Opportunities are opening thanks to a rapidly-increasing middle class that is eager for consumption. Access is difficult and full of obstacles. At the same time, short term profits are not easily available. But opportunities are there for Spanish firms of all sizes and sectors (one in particular being quality tourism from China to Spain). The document proposes to unify efforts of the different Autonomous Communities to promote Spain and its brand. China is here to stay and Spanish firms are in China to stay.

Resumen

China representa hoy el mercado emergente más atractivo del mundo. Muchos indicadores económicos lo confirman: China encarna un país con un PIB próspero, una creciente población urbana, una floreciente clase media y un aumento en el gasto privado y público. A pesar de todo esto, las exportaciones españolas a China son aún bajas y subrayan un déficit comercial desfavorable y crónico. Por supuesto, se hacen esfuerzos para corregir este desequilibrio de comercio. La evolución a partir de 2009 muestra un aumento de las exportaciones españolas a China, una pequeña reducción en el déficit y un aumento en la inversión directa. Sin embargo, todo esto todavía representa un cambio muy modesto.

El presente documento se basa en tres hipótesis: en primer lugar, el acceso al mercado chino dicta que las empresas extranjeras en general, y españoles en particular, adapten sus bienes o servicios a esta demanda específica. En segundo lugar, China ofrece un atractivo mercado conformado por muchos consumidores y una significativa emergente clase media. España no aprovecha plenamente estas oportunidades. Finalmente, el acceso al mercado chino está lleno de obstáculos: se requiere una inversión importante, personal especializado, un período de recuperación largo, mucha paciencia y perseverancia. Por lo tanto, es accesible sólo para las grandes empresas.

Mientras se confirman las dos primeras hipótesis, no ocurre lo mismo con la tercera. Algunas grandes y muy reconocidas marcas españolas están teniendo gran éxito en China. Pero también hay cientos de pequeñas empresas que operan de manera fructífera en este país, en todos los sectores. La encuesta realizada confirma que hay importantes posibilidades de éxito, independientemente del tamaño de la empresa. La cuestión crucial es tener una estrategia muy clara para la implementación del proyecto en China. Por lo tanto, podemos concluir que lo fundamental no es principalmente el tamaño (aunque pueda ayudar) sino tener una estrategia clara y cumplir con ciertos requisitos que se analizarán en detalle.

Se ha realizado una exhaustiva investigación utilizando datos cuantitativos y cualitativos. Se envió un cuestionario a las empresas españolas en China para categorizar quiénes son e identificar las oportunidades; estudiar sus dificultades y planes para el futuro en el país; descubrir las mejores prácticas que respalden la acción estratégica de nuestras empresas. Todas estas variables se encuentran desarrolladas en los capítulos siguientes.

Finalmente, podemos concluir que el mundo se halla en un entorno turbulento y las empresas tratan de adaptarse rápidamente a los cambios. Si en el pasado reciente las empresas occidentales se trasladaron a China para acceder a su mano de obra de bajo costo, hoy en día intentan acceder al creciente mercado interno. Se abren oportunidades gracias a una clase media ansiosa por consumir que aumenta rápidamente. El acceso es difícil y lleno de obstáculos y las ganancias no se consiguen a corto plazo. Pero existen oportunidades para las empresas españolas de todos los tamaños y sectores (en particular, el turismo de calidad de China hacia a España). El documento propone unificar esfuerzos promover la marca España ya que China está aquí para quedarse, y las empresas españolas están en China para quedarse.

Resum

Xina representa avui el mercat emergent més atractiu del món. Molts indicadors econòmics ho confirmen: Xina encarna un país amb un PIB pròsper, una creixent població urbana, una ascendent classe mitjana i un augment en la despesa privada i públic. Malgrat tot això, les exportacions espanyoles a Xina són encara baixes i subratllen un dèficit comercial desfavorable i crònic. Per descomptat, es fan esforços per corregir aquest desequilibri de comerç. L'evolució a partir de 2009 mostra un augment de les exportacions espanyoles a Xina, una petita reducció en el dèficit i un augment en la inversió directa. No obstant això, tot això encara representa un canvi modest.

El present document es basa en tres hipòtesis: en primer lloc, l'accés al mercat xinès dicta que les empreses estrangeres en general, i espanyoles en particular, adaptin els seus productes o serveis a aquesta demanda específica. En segon lloc, Xina ofereix un atractiu mercat conformat per molts consumidors i una significativa emergent classe mitjana. Espanya no aprofita plenament aquestes oportunitats. Finalment, l'accés al mercat xinès està ple d'obstacles: es requereix una inversió important, personal especialitzat, un període de recuperació llarg, molta paciència i perseverança. Per tant, és accessible només per a les grans empreses.

Mentre es confirmen les dues primeres hipòtesis, no ocorre el mateix amb la tercera. Algunes grans i molt reconegudes marques espanyoles estan tenint gran èxit a Xina. Però també hi ha centenars de petites empreses que operen de manera fructífera en aquest país, en tots els sectors. L'enquesta realitzada confirma que hi ha importants possibilitats d'èxit, independentment de la grandària de l'empresa. La qüestió crucial és tenir una estratègia molt clara per a la implementació del projecte a Xina. Per tant, podem concloure que el fonamental no és principalment la mida (encara que pugui ajudar) sinó tenir una estratègia clara i complir amb certs requisits que s'analitzaran detalladament.

S'ha realitzat una exhaustiva investigació utilitzant dades quantitatives i qualitatives. Es va enviar un qüestionari a les empreses espanyoles a Xina per categoritzar qui són i identificar les oportunitats; estudiar les seves dificultats i plans per al futur al país; descobrir les millors pràctiques: un marc que recolzi l'acció estratègica de les nostres empreses. Totes aquestes variables es troben desenvolupades en els propers capítols.

Finalment, podem concloure que el món avança a un ritme turbulent i les empreses tracten d'adaptar-se ràpidament als canvis. Si en el passat recent les empreses occidentals es van traslladar a Xina per accedir al seu baix cost laboral, avui dia intenten accedir el mercat intern creixent. S'obren oportunitats gràcies a una classe mitjana ansiosa per consumir que augmenta ràpidament. L'accés és difícil i ple d'obstacles. Al mateix temps, els guanys no s'esperen fàcilment a curt termini. Però existeixen oportunitats per a les empreses espanyoles de totes les grandàries i sectors (un en particular és el turisme de qualitat de Xina cap a Espanya). El document proposa unificar esforços per promoure la marca Espanya, ja que Xina està aquí per quedar-se i les empreses espanyoles estan a Xina per quedar-se.

Keywords

China – Chinese market - access to market – emerging markets – foreign trade –
Spain - Spanish companies- internationalisation - country analysis – opportunities –
challenges - key success factors – best practices

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I. INTRODUCTION

The main objective of this paper is to shed light on the key success factors in accessing the Chinese market for Spanish companies. To create a framework for companies wishing to sell their products in China and what they need to do to succeed.

For several years, many Western companies off-shored their production to countries with low cost labour, like China. Today, these same companies, regardless where they manufacture, are seriously considering accessing the emerging markets. If we focus on China, we are talking about a market of over 1,300 million people, with a purchasing power, albeit limited, on the increase. How can we try to start marketing our products there? It is an arduous, slow task and it can be very expensive with many potential pitfalls. The company that wants to try should consider well its strategy to succeed.

1. Objectives of the research

The world is changing at a pace we struggle to adapt to. There are new forces that are reshaping the environment of business and as a result we are living in a new era of rapid and unpredictable change. It seems highly likely that the levels of volatility and unpredictability that we have experienced in recent years will continue into the future. These changes are classified by Robert M. Grant¹ into (1) economic changes, with the world stuck in the worst economic downturn since the 1930s, which picture an image of volatility and low growth, at least for the western world, (2) technology changes with a “New Economy” that has moved from an industrial economy to a knowledge economy, driven by the digital revolution, and (3) societal pressures: “for organisations to survive and prosper it is required that they adapt to the values and expectations of society – something which organisational sociologists refer to as *legitimacy*. Loss of social legitimacy may be as great a threat to the survival of commercial and investment banks as are their weak balance sheets”.

In this situation of economic recession and lower demand for our products, western companies find it more and more difficult to find customers in the domestic marketplace. In the search for more attractive markets, these businesses look around and observe how some emerging markets are growing at an unprecedented speed. They obviously wonder if accessing these markets would be something they could do, will it be hard, will it be possible, has anyone similar to me done it before, how a company can be successful. In short, businesses often feel at a loss when trying to enter a new market that is so unknown for them in terms of culture, language, geographical distance, distribution channels, and so on.

There are two main approaches when we consider the access to global markets. On the one hand, Friedman states that the world is flat, in his book of the same name.²

¹ GRANT, R. M. *Contemporary Strategy Analysis*. John Wiley & Sons. Barcelona, 2010.

² FRIEDMAN, T. L. *The world is flat. A brief history of the twenty-first century*. FSG Books. New York, 2005.

He explains how, during a trip to India, he discovered a large number of European and American companies operating in India, and how globalisation has shifted the world. One can get an American designed product built in different Asian countries, with outsourced technology from a third country, supported by call centres placed in India, for European customers, and so on. According to Friedman, ten forces have flattened the world, amongst others the fall of the Berlin Wall, the connectivity achieved by the internet, digital technologies or the improvement of communications and infrastructures.

This flattening of the world opens up many opportunities and makes the world smaller and perfectly accessible to everyone. National differences do not account for much, as such, it is easy to access foreign markets, even if they are far away and different to us as the Chinese market is.

On the other hand, Ghemawat portrays a somewhat different picture³. According to this author, the world is circular, countries are still not completely integrated, and borders still matter. These borders are developed in his well-known CAGE model: there are still strong differences that can be cultural, administrative, geographic and economic distance. He concludes showing a kind of caution sign for businesses that want to operate globally: “failing to keep it in view can be a recipe for poor performance” Therefore he warns that country and regional differences still matter and do surpass easily the similarities of a flat world.

Therefore, following his theory, if a firm tries to compete in the same way in all the markets, it is in for an unpleasant surprise.

This paper will try to analyse who is right: can we access the Chinese market using the same products, services, strategy as we do in our domestic market? Or do we have to adapt strategically to fit into a new market? How easy is it to access the Chinese market? Can small and medium-sized companies achieve the goal successfully or are we facing a impossible task? What are the obstacles and the opportunities? Summarising the question: is the world flat or is it round?

We shall try to answer to these questions in the following pages.

But first, we need to focus on the country of China. We are going to study its enormous growth, compared to Spain. We will try to prove that:

1. There are increasing opportunities due to the growth of the population (in particular urban population and middle classes), growth of the Gross Domestic Product and Gross Domestic Product per capita, consumption growth and increase of the imports.

³ GHEMAWAT, P. *Redefining global strategy. Crossing borders in a world where differences still matter*. Harvard Business School Press. Boston, 2007.

2. Indicators of economic confidence are also positive. The recession suffered in Spain is not affecting China as greatly. Perhaps the economic growth will slow down but it will be a soft landing.
3. In spite of these opportunities, the access to the market is proving difficult due to legal, cultural and language barriers, amongst others. But some large Spanish firms have successfully entered the market.
4. There are several hundred medium and small-sized Spanish businesses regularly doing business in China. A survey has been carried out to help draw a profile of these firms: why they set up business in China, what were their main obstacles, their priorities for the next years and the best practices learned after the process. We will deduce how to take fully advantage of the opportunities that open in front of us.

2. Hypotheses

H1- Accessing the Chinese market requires that foreign firms in general, and Spanish ones in particular, adapt their products or services to that specific market. Moreover, the adaptation should not be restricted to those products but also be applied to the management style and the strategic approach of the foreign companies towards China.

Explanation: in a world that is global, where tastes and habits are becoming increasingly homogeneous among countries, there is still a strong specific underlying culture, negotiation peculiarities and specific market needs in China that have to be addressed. Otherwise, the foreign company will not be successful.

H2- China offers an attractive market made up of many consumers and a significant emerging middle class. Spain is not taking advantage fully of this opportunity.

Explanation: while the opportunities China presents are colossal (in terms of GDP growth, urban population with increasing disposable income, high consumer confidence levels, blooming middle class, rising demand for all products, etc), Spanish firms are not taken as much advantage of these opportunities as expected: the trade balance is negative, exports are still very low and so is Direct Investment in the country.

H3- Accessing the Chinese market is full of obstacles: it requires a significant investment, skilled staff, a long payback period, much patience and endurance. Therefore, it is a market only accessible for large firms.

Explanation: the path into China is twisty and long. Cases of large firms setting up successfully in China are very well-known and continuously portrayed in the media. But what about the smaller or medium-sized ones? We need to give an answer to the following related issues:

- Detect which Spanish companies are operating in the Chinese market and identify the opportunities in accessing it;
- Sorting out the challenges for our companies: what are their difficulties and future plans in the country;
- Find out the best practices: a practical framework for corporate performance that will support practical strategic action for our businesses.

We shall try to deduce the keys to success, or best practices, so that companies in the future can use this knowledge to increase their chances when accessing the Chinese market.

3. Methodology

The present research is the result of several years of work, study and travels within Europe and China. Several different methods have been used in order to grasp the complexity of the subject:

Firstly, an extensive literature review on China (history, culture, economy, trade, etc.), and also on Spanish businesses, has been carried out,

Secondly, substantive research has been done on quantitative data. The main sources that have been used are all official data bases from: International Monetary Fund, World Bank, Asian Development Bank (ADB), the US-China Business Council, Chinese Customs, the Spanish Statistical Office (INE), the Spanish Institute for Foreign Trade (ICEX), Casa Asia and Eurostat, amongst others.

Thirdly, a research framework leading to a comprehensively-designed set of interview questions was created. Qualitative information has been collected mainly from interviews done in China, Spain and different parts of Europe to experts in the following fields:

- Chinese economy and International Relations,
- Foreign Trade between Spain and China,
- Businesses with Chinese marketplace experience,
- Export promotion agencies.

As a start point, institutions and trade organisations (Chambers of Commerce, Casa Asia, Catalanian Government Agency ACC10, consulting companies, etc.) with a track record in the promotion of exports to China were identified. A selection of firms that actively export to China were interviewed as well. Other experts in economics and foreign trade from the finance sector and from academic institutions were consulted. These interviews took place between January 2011 and June 2012. Questions were open-ended to gain a maximum of insight. We would like to thank herewith the availability of these persons, and the generosity they showed when

sharing their knowledge. Annex 1 shows in detail the list of persons interviewed while Annex 2 details the contents of such interviews.

Figure 1. Collection of qualitative data through interviews with experts



Source: own elaboration

Last but not least, a survey has been carried out to help draw a profile of Spanish firms operating in China: why they set up business in China, what were their main obstacles, their priorities for the next years and the best practices learned after the process. The survey was conducted between January and May 2012 among the 360 Spanish firms that are based in China.

Table 1. Summary of methodology for the survey

Concept	Dates
Date of the survey launching	January 2012
Dates of the reminders	15 th February 1 st March 2012 15 th March Some preliminary results were sent to all to encourage further answers in May. Telephone follow up was carried out throughout the period.
Population	360 firms from two databases: Spanish firms that belong to the Spanish Chamber of Commerce in China plus the ICEX Database of Spanish firms in China.
Sectors	All sectors are represented, from industrial products, construction and civil engineering to all kinds of services.
Location in China	All firms in China are considered, regardless of the geographic area, although three areas are more represented: Pearl River Delta (Beijing Area), Yangtze River Delta (Shanghai Area), Bay of Bohai

Concept	Dates
	(South of China).
Alliances	Different institutions have helped to encourage answers, namely Casa Asia and different Chambers of Commerce.
Number of Questionnaires sent	360
Number of answers received	78 (i.e. 21.6% of the total) It can be affirmed that the survey represents the total population of firms, in terms of sector, size and geographical destination.

Source: own elaboration

The diagram below shows the different steps in the process:

Figure 2. Chronological summary of the different steps in the research



Source: own elaboration

Shortcomings of our methodology:

There are firms that are actually exporting to China but, however, are not represented in our study. We considered that the main variables to take into account were: firms that are trading in China on a regular basis, not just as a one off. Therefore, it was considered that having some direct investment in the country was a must: from the simplest form like a Representation Office, to a production plant or other facilities.

What is not the objective of our research?

One of the problems encountered in our path has been the wideness of the subject, along with the huge volume of data and speed of change. For that reason, we find relevant at this point to establish what has **not** been the specific object of our research:

- To analyse the history of China or the philosophy that underlies the Chinese culture;
- To study in depth the political or even the economic panorama of China. In that sense, we have only evaluated the indicators that could serve our purpose: the variables that explain China as an emergent market with plenty of opportunities;
- To explore the legal or fiscal framework of foreign firms in China;
- To compare the case of Spanish businesses with other Western countries.

4. Acknowledgements

We would like to thank all the people who have helped us write this document. In fact, the research is the result of the cooperation of many individuals and organizations. First, we wish to thank the more than 40 talented experts who so generously shared with us their experiences and accumulated years of knowledge about China and doing business in this fascinating country.

We also wish to thank the 78 firms that were so collaborative and helpful so as to fill in our questionnaire. In a turbulent world where everybody is always in such a hurry, such generosity is doubly valued and appreciated.

Concerning the Abat Oliba CEU University, our special thanks go to Dr. Ferran Porta, for his guidance in the difficult paths of research, whose insightful comments on the key issues facing this work helped us clear the way ahead. Dr. Joan Ripoll was extremely helpful with data sources, data analysis and its comprehension. He spent many hours revising the document and he always had very valuable and wise advice. The discussions we had helped me greatly to develop the ideas put forward in this work. Alejandro Gisbert gave me a very useful hand with access to data, in particular with the Bloomberg database. He has also offered much advice and insight in the last phases of our work, and one could not hope for a friendlier advisor. Josep Maria Muntaner helped with the development of the questionnaire from the IT perspective while Dra. Ana Beriain was ever so clever with her comments to develop a sound survey. Chema Salmons never failed to give is a hand when IT support was required, like our students Alejandro Rey and Adrià Birlanga, with some data extraction. In addition, we would like to thank the University Abat Oliba in general for the support and the constant backing we have received from the whole organization during these years.

This International PhD has been successfully completed thanks to the active cooperation of the Corvinus University of Budapest, where I spent time talking to experts and revising bibliography. We chose this University for several reasons: first, because of the presence there of Prof. Simai, expert in China, United Nations Economic Commissioner for Europe, former General Director of United Nations University, former Vice-Chairman of the UNICEF Executive Board and has taught in many universities world-wide. Second, because of the specialization of this University in Chinese affairs; they have a Chinese centre to promote economic and cultural relations. Last, but not least, because of the opportunity that was presented

to us to spend some time in Budapest, invited by the Corvinus University. All these reasons together made us choose this city and university to complete our research.

This document has been reported by Dr. Bernadett Lehoczki, Professor at the Corvinus University, expert in China and its international relations. We would like to thank her for her advice and support. Our warm recognition goes too to Professor Dr. Nagy Sándor Gyula, Vice-dean of the Faculty of Economics, who has enabled the stay in Budapest and the contacts with all the authorities in the subject. His assistance to define the hypothesis and his continuous optimism proved to be invaluable.

Finally, I would wish to add special thanks to my family for their support, resilience and endurance during all this period.

I. INTRODUCCIÓN

El objetivo principal de este trabajo es arrojar luz sobre los factores clave de éxito en el acceso al mercado chino para las empresas españolas. Crear un marco de referencia para las empresas que deseen vender sus productos en China, que ilustre todo aquello que es necesario tener en cuenta para tener éxito.

Durante unos años, muchas empresas occidentales deslocalizaron su producción a países con mano de obra barata, como China. Actualmente, estas mismas empresas, independientemente de dónde fabriquen, están considerando seriamente acceder a los mercados emergentes. Si nos centramos en China, estamos hablando de un mercado de más de 1.300 millones de personas con un poder adquisitivo, aunque limitado, en aumento. ¿Cómo podemos comenzar a comercializar nuestros productos allí? Es una tarea ardua, lenta y puede ser costosa, con muchos peligros potenciales. La empresa que quiera intentarlo deberá planificar muy bien su estrategia para llegar a tener éxito.

1. Objetivos de la investigación

El mundo está cambiando a un ritmo que exige luchar para lograr adaptarse. Existen nuevas fuerzas que están remodelando el entorno de los negocios y, como resultado, estamos viviendo en una era de cambios rápidos e impredecibles. Parece muy probable que los niveles de volatilidad e imprevisibilidad que hemos experimentado en los últimos años continúen en el futuro. Robert M. Grant⁴ clasifica estos cambios en (1) cambios económicos, con el mundo atrapado en la peor crisis económica desde la década de 1930, que nos muestra una imagen de inestabilidad y bajo crecimiento, al menos en el mundo occidental, (2) cambios tecnológicos, con una *Nueva Economía* que ha pasado de una economía industrial a una economía del conocimiento, impulsada por la revolución digital, y (3) presiones sociales: "para que las organizaciones puedan sobrevivir y prosperar es necesario que se adapten a los valores y expectativas de la sociedad - algo que los sociólogos organizacionales denominan *legitimidad*. La pérdida de legitimidad social puede ser una amenaza tan grande para la supervivencia de los bancos comerciales y de inversión, como un balance débil".

En esta situación de recesión económica y de menor demanda de nuestros productos, a las empresas occidentales les resulta cada vez más difícil encontrar clientes en su mercado interno. En la búsqueda de mercados más atractivos, estas compañías miran a su alrededor y observan cómo algunos mercados emergentes están creciendo a una velocidad sin precedentes. Se preguntan si el acceso a estos mercados es algo viable: si será duro, si será posible, si otras empresas similares lo han conseguido antes. En resumen, las empresas se sienten a menudo desorientadas a la hora de entrar en un nuevo mercado que les es desconocido en términos de cultura, idioma, canales de distribución, etc. y además, situados a gran distancia geográfica.

⁴ GRANT, R. M. *Contemporary Strategy Analysis*. John Wiley & Sons. Barcelona, 2010.

Existen dos enfoques principales cuando consideramos el acceso a mercados globales. Por un lado, en su obra con el mismo título, Friedman afirma que la tierra es plana.⁵ Explica cómo, durante un viaje a la India, descubrió un gran número de empresas europeas y estadounidenses que operan en este país, y cómo la globalización ha transformado el mundo. Uno puede conseguir un producto de diseño americano construido en diferentes países de Asia, con la tecnología externalizada de un tercer país, con el apoyo de los *call-centres* indios, para los clientes europeos, y así sucesivamente. Según Friedman, diez fuerzas han aplanado el mundo, entre otros la caída del Muro de Berlín, la conectividad alcanzada por internet, las tecnologías digitales o la mejora de las comunicaciones y las infraestructuras.

Este aplanamiento del mundo abre muchas oportunidades y hace que nuestro planeta sea más pequeño y perfectamente accesible para todos. Las diferencias nacionales no cuentan mucho y, por tanto, es fácil acceder a los mercados extranjeros, aunque estén lejos y sean muy diferentes al nuestro, como puede ser el mercado chino.

Por otro lado, Ghemawat muestra una imagen muy distinta⁶. Según este autor, el mundo es redondo, los países todavía no están completamente integrados y las fronteras aún importan. Agrupa las diferentes barreras en su conocido modelo CAGE: existen fuertes diferencias culturales, administrativas, geográficas y económicas entre los países. Concluye mostrando una señal de aviso para las empresas que quieren operar a nivel mundial: "no tener en cuenta estas diferencias puede ser una receta para el fracaso". Advierte, pues, que las diferencias nacionales y regionales siguen importando y pesan más que las similitudes de un supuesto mundo plano.

Por lo tanto, a raíz de su teoría, si una empresa intenta competir de la misma manera en todos los mercados, le deparan sorpresas desagradables.

En este trabajo trataremos de analizar quién tiene la razón: ¿se puede tener acceso al mercado chino con los mismos bienes, servicios y estrategias que en nuestro mercado interno? ¿O tenemos que adaptarnos estratégicamente al nuevo mercado? ¿Cómo de fácil es acceder al mercado chino? ¿Pueden las empresas pequeñas y medianas alcanzar la meta con éxito o estamos frente a una tarea imposible? ¿Cuáles son los obstáculos y las oportunidades? Resumiendo la pregunta: ¿Es el mundo plano o es redondo? En las páginas siguientes trataremos de dar respuesta a estas cuestiones.

⁵ FRIEDMAN, T. L. *The world is flat. A brief history of the twenty-first century*. FSG Books. New York, 2005.

⁶ GHEMAWAT, P. *Redefining global strategy. Crossing borders in a world where differences still matter*. Harvard Business School Press. Boston, 2007.

Pero primero, tenemos que centrarnos en China como país. Estudiaremos su crecimiento y trataremos de demostrar que:

1. Hay oportunidades cada vez mayores debido a una serie de indicadores favorables: el crecimiento de la población (en particular de la población urbana y la clase media), el crecimiento del Producto Interior Bruto y el Producto Interior Bruto per cápita, la progresión del consumo y el aumento de las importaciones.
2. Los indicadores de confianza económica también son positivos. La recesión sufrida en España no está afectando a China con tanta fuerza. Tal vez el crecimiento económico se desacelere, pero se espera un aterrizaje suave.
3. A pesar de estas oportunidades, el acceso al mercado chino está resultando difícil debido a las barreras legales, culturales y del lenguaje, entre otros. Sin embargo, algunas grandes empresas españolas han entrado con éxito en el mercado.
4. Hay varios cientos de empresas españolas medianas y pequeñas que operan regularmente en China. Hemos llevado a cabo un estudio para ayudar a trazar un perfil de estas empresas: por qué establecieron su negocio en China, cuáles fueron sus principales obstáculos, sus prioridades para los próximos años y las mejores prácticas aprendidas después del proceso. A partir de aquí, deduciremos cómo aprovechar al máximo las oportunidades que se abren ante nosotros.

2. Hipótesis

H1- El acceso al mercado chino requiere que las empresas extranjeras en general, y las españolas en particular, adapten sus bienes o servicios a este mercado específico. Por otra parte, la adaptación a China de las empresas no puede limitarse solo a los productos, sino también aplicarse al estilo de gestión y a su enfoque estratégico.

Explicación: en un mundo global, donde los gustos y hábitos son cada vez más homogéneos entre los países, existe aún una fuerte cultura específica subyacente, peculiaridades en la negociación y necesidades específicas del mercado. Estos temas tienen que ser abordados: en caso contrario, la empresa extranjera no tendrá éxito.

H2- China ofrece un mercado atractivo compuesto por un gran número de consumidores gracias a una gran clase media emergente. España no está aprovechando plenamente esta oportunidad.

Explicación: mientras que las oportunidades presentes en China son colosales (en términos de crecimiento del PIB, una población urbana con ingresos disponibles cada vez mayores, altos niveles de confianza de los consumidores, floreciente clase media, la creciente demanda de todos los productos, etc.), las empresas españolas

no aprovechan estas oportunidades como se podría esperar: la balanza comercial es negativa, las exportaciones siguen siendo bajas y la inversión directa en el país es insuficiente.

H3- El acceso al mercado chino está lleno de obstáculos: se requiere una alta inversión, personal capacitado, un periodo largo de recuperación, mucha paciencia y perseverancia. Por lo tanto, se trata de un mercado accesible únicamente para las grandes empresas.

Explicación: el camino hacia China es sinuoso y los resultados solo son visibles a largo plazo. Los casos de las grandes empresas establecen con éxito en China son muy conocidas y continuamente retratados en los medios de comunicación. Pero ¿qué pasa con las pequeñas y medianas empresas? Hemos de dar respuesta las siguientes cuestiones:

- Detectar qué empresas españolas están operando en el mercado chino e identificar las oportunidades para acceder a él;
- Definir los desafíos para nuestras empresas: cuáles son sus dificultades y sus planes futuros en el país;
- Descubrir las mejores prácticas: un marco para el desempeño corporativo que dibuje la acción estratégica de nuestros negocios.

Vamos a tratar de deducir las claves del éxito, y las mejores prácticas, a fin de que las empresas puedan utilizar este conocimiento en el futuro, y así aumentar sus oportunidades en el acceso al mercado chino.

3. Metodología

La presente investigación es el resultado de varios años de trabajo, estudio y viajes a China y Budapest. La metodología empleada para captar la complejidad del tema se ha basado en varios pilares:

En primer lugar, una extensa revisión bibliográfica sobre China (historia, cultura, economía, comercio, etc.), y también sobre las empresas españolas;

En segundo lugar, un análisis a fondo de los datos cuantitativos. Las principales fuentes que se han utilizado son las bases de datos de organismos oficiales como: Fondo Monetario Internacional, Banco Mundial, Banco Asiático de Desarrollo (BAD), el Consejo Empresarial EEUU-China, la Aduana China, la CEPAL, la Oficina Española de Estadística (INE), el Instituto Español de Comercio Exterior (ICEX), Casa Asia y Eurostat, entre otros.

En tercer lugar, se ha desarrollado un marco de investigación basado en entrevistas a expertos en China, España y Hungría, sobre los campos siguientes:

- Economía china y relaciones internacionales,
- Relaciones comerciales entre España y China,
- El mercado chino y sus peculiaridades
- La promoción de las exportaciones a China.

En concreto, se han entrevistado instituciones y organizaciones profesionales que promocionan las exportaciones a China (por ejemplo Cámaras de Comercio, Casa Asia, ACCIO10 -Agencia de la Generalitat de Catalunya-, empresas consultoras especialistas en China, etc.). Se entrevistó también a una selección de empresas que exportan activamente a China. Se consultó a diversos expertos en economía y comercio exterior del sector financiero y de instituciones académicas. Estas entrevistas se llevaron a cabo entre enero de 2011 y junio de 2012. Las preguntas eran abiertas para ganar un máximo de penetración en el tema. Nos gustaría dar las gracias a las personas que se mostraron dispuestas a entrevistarse con nosotros, por su disponibilidad y la generosidad que mostraron al compartir sus conocimientos. El anexo 1 muestra la lista de las personas entrevistadas mientras que el anexo 2 detalla los contenidos de las mismas.

Figure 3. Recogida de datos cualitativos mediante entrevistas a expertos



Fuente: elaboración propia

Por último, aunque no menos importante, se ha realizado una encuesta a empresas españolas que operan en China: por qué establecer un negocio en China, cuáles fueron sus principales obstáculos, sus prioridades para los próximos años y las mejores prácticas aprendidas después de la proceso. La encuesta se realizó entre enero y mayo de 2012 entre las 360 empresas españolas que tienen su sede en China.

Table 2. Resumen de la metodología de la encuesta

Concepto	Fechas
Lanzamiento del cuestionario	Enero 2012
Recordatorios múltiples	15 Febrero 1 Marzo 15 Marzo 2012 En mayo se enviaron unos resultados preliminares a todos los encuestados para propiciar más respuestas. También se hizo un seguimiento telefónico durante todo el período.
Población del estudio	360 empresas de dos bases de datos: empresas españolas socias de la Cámara de Comercio Española en China, y la base de datos del ICEX.
Sectores	Todos los sectores están representados, desde la industria, la ingeniería y todos los servicios.
Localización geográfica en China	Todas las empresas, independientemente de su lugar de destino en China. Tres son las zonas más frecuentes: Delta del Río Perla (zona Beijing), el delta del Río Yangtze (zona Shanghai), y la Bahía del Bohai (Sur de China).
Alianzas	Diferentes instituciones han ayudado a animar las respuestas a los cuestionarios, en especial Casa Asia y las Cámaras de Comercio.
Número de cuestionarios enviados	360
Número de respuestas recibidas	78 (es decir, 21.6% del total). Puede afirmarse que la encuesta representa a la población total de empresas estudiadas en cuanto al tamaño, los sectores de actividad y el lugar geográfico de implantación en China.

Fuente: elaboración propia

Limitaciones de nuestra metodología:

Hay empresas que exportan a China, pero, sin embargo, no están representadas en nuestro estudio, ya que no cuentan con presencia física alguna en este país. Hemos considerado que las principales variables a tener en cuenta son: las empresas que comercian con China de forma regular, no sólo de forma puntual. Por lo tanto, se partió de la base que tener algún tipo de inversión directa en el país era un requisito para ser entrevistado: ya fuera la forma más simple, como una Oficina de Representación, o inversiones más potentes, como una planta de producción u otras instalaciones.

El diagrama que se presenta a continuación muestra las diferentes etapas del proceso:

Figure 4. Resumen cronológico de las diferentes etapas seguidas en la investigación



Fuente: elaboración propia

Qué **NO** ha sido objeto de nuestra investigación:

Uno de los problemas encontrados en nuestro camino ha sido la amplitud de la materia, junto con el enorme volumen de datos existentes, en constante cambio. Por esa razón, encontramos pertinente en este punto establecer lo que no ha sido objeto específico de nuestra investigación:

- Analizar la historia de China o la filosofía que subyace en la cultura china;
- Profundizar en la política o incluso en el panorama económico de China. En ese sentido, nos hemos limitado a evaluar aquellos indicadores que podrían servir para nuestro objetivo: las variables que describen el mercado emergente de China, lleno de oportunidades;
- Explorar el marco legal y fiscal de las empresas extranjeras en China;
- Comparar el caso de las empresas españolas con las de otros países occidentales.

4. Agradecimientos

Nos gustaría dar las gracias a todas las personas que nos han ayudado a elaborar este documento. De hecho, la investigación es el resultado de la cooperación de muchas personas y organizaciones. En primer lugar, queremos agradecer a los más de 40 expertos que tan generosamente compartieron con nosotros sus años acumulados de experiencias y conocimientos sobre China y cómo hacer negocios en este fascinante país.

También queremos dar las gracias a las 78 empresas que estuvieron dispuestas a colaborar rellenando nuestro cuestionario. En un mundo turbulento donde todos vamos con tanta prisa, esta ayuda es doblemente valorada y apreciada.

En cuanto a la Universidad Abat Oliba CEU, nuestro agradecimiento especial se dirige al Dr. Ferran Porta, por su guía en los caminos difíciles de la investigación, cuyas observaciones sobre las cuestiones clave que afronta este trabajo nos ayudaron a despejar el camino a seguir. El Dr. Joan Ripoll ha sido extremadamente valioso en su ayuda con las fuentes de datos, análisis de datos y su comprensión. Pasó muchas horas revisando el documento y siempre tenía consejos valiosos y sabios. Las discusiones con él me han ayudado en gran medida al desarrollo de las ideas expuestas en este trabajo. El Profesor Alejandro Gisbert nos asesoró en el acceso a las fuentes de datos, y en particular, nos ayudó enormemente a extraer datos de Bloomberg. También nos ofreció muchos consejos y conocimiento en las últimas fases de nuestro trabajo, siempre aconsejando de la manera más cordial. Josep Maria Muntaner me ayudó con el desarrollo del cuestionario desde la perspectiva informática, mientras que la Dra. Ana Beriain resultó crucial con sus comentarios a la hora de desarrollar un cuestionario sólido. Chema Salmons nunca ha dejado de echarnos una mano cuando hemos necesitado su valiosa ayuda con los programas informáticos, así como los estudiantes Alejandro Rey y Adrià Birlanga con la extracción de datos. Además, nos gustaría dar las gracias a la Universidad Abat Oliba, en su conjunto, por el apoyo y el respaldo constante que hemos recibido de toda la organización durante estos años.

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Esta tesis ha sido informada por la Dra. Bernadett Lehoczki de la Universidad Corvinus, experta en China y sus relaciones internacionales. Agradecemos vivamente su consejo y apoyo. Nuestro especial agradecimiento se dirige también al Profesor Dr. Sándor Nagy Gyula, Vicedecano de la Facultad de Economía, quien ha favorecido la estancia en Budapest y los contactos con las autoridades en la materia. Su ayuda a definir la hipótesis y su continuo optimismo han demostrado ser insustituibles.

Por último, desearía añadir un agradecimiento especial a mi familia por su apoyo, ánimo y resistencia durante todo este período.

II. THE POPULAR REPUBLIC OF CHINA: AN INCREASINGLY ATTRACTIVE MARKET

1. Introduction to the Popular Republic of China. Key indicators

The Chinese economy grew by 9.2% in 2011, a robust pace of growth that, even if it is the lowest in the last decade, shows that China's economy is not going to stop growing, as some reports pointed out. Instead, China is going towards a slow landing. The reasons of its downturn can be found in a slow recovery of the exports, due to a lower demand of the global economy, plus a decrease of the investment.

The risks of a recession are very limited, according to most of the surveys consulted, for instance, the ones of La Caixa.⁷ In the first place, China still has a high potential to increase its internal demand. Even if it is true that certain consumer goods are approaching saturation (mobile phones, televisions or home appliances), namely in urban areas, other sectors, such as cars, still have a very long way to go. Regarding investment, the factors that suggest a decreasing trend are very limited, centred in infrastructures and in building. The first one was seriously affected by the high-speed-train accident that took place in Wenzhou last summer. The second one is distressed due to credit restrictions being applied in order to stop the growth of inflation. However, bearing in mind that more than 300 million people in rural areas are willing to move into cities, the demand for housing is ensured. The activity indicators such as industrial production and electric production are still growing strongly (by 14% and 11% respectively in the third quarter of 2011). Finally, foreign trade, both exports and imports are on the increase, even if not as strongly as in the past decade. Therefore, it can be concluded that the Chinese economy is not going to drop, but to slowly cool down slightly.

Perhaps the main risk is the high inflation rates, still high at 6.1% in September 2011. Inflation rate for food is at a worryingly high 13.4%, factor of considerable social relevance that is a matter of concern for Chinese authorities.

Associated with price increases are swelling labour costs: this erodes the competitiveness of Chinese traditionally cheap labour. As a result, it obliges the country to reorient the economy towards more domestic consumption and to produce more sophisticated goods.

Therefore, we can conclude that growth is to continue, even if perhaps at a slower rate. We would like to stress the idea at this point that independently of whatever happens now at short time, the interest for China in the long run remains unaffected. This is not a fashion, this does not depend on short term indicators: China is here to stay and its influence as a second world power is unquestionable.

⁷ LA CAIXA. *Monthly and Annual Report*. November 2011 (p. 12-14).

Table 3. The Popular Republic of China: A selection of key indicators

	2006	2007	2008	2009	2010
POPULATION					
Total population <i>million; as of 31 December</i>	1,314.5	1,321.3	1,328.0	1,334.7	1,339.7
Population density <i>persons per square km.</i>	136.9	137.6	138.3	139.0	140.0
Population <i>annual change, percent</i>	0.5	0.5	0.5	0.5	0.4
Urban population <i>percent of total population</i>	43.9	44.9	45.7	46.6	49.7
LABOR FORCE <i>million; calendar year</i>	782.4	786.5	792.4	798.1	...
Employed					
Agriculture	764.0	769.9	774.8	780.0	...
Manufacturing	325.6	314.4	306.5	297.1	...
Others	438.4	455.5	468.3	482.9	...
Unemployed	8.5	8.3	8.9	9.2	...
Unemployment rate <i>percent</i>	4.1	4.0	4.2	4.3	4.1
Labor force <i>annual change, percent</i>	0.5	0.5	0.8	0.7	...
NATIONAL ACCOUNTS <i>billion Yuan; calendar year</i>					
At Current Prices					
GDP, total at current market prices	21,631.4	26,581.0	31,404.5	34,050.7	39,798.3
At Current Market Prices <i>Yuan</i>					
Per capita GDP	16,500.0	20,169.0	23,708.0	25,605.0	29,762.0
Price Indexes <i>annual change, percent</i>					
Consumer price index	1.5	4.8	5.9	-0.7	3.3
Producer price index	3.0	3.1	6.9	-5.4	5.5
EXTERNAL TRADE <i>billion US Dollars; calendar year</i>					
Exports, fob	969.0	1,217.8	1,430.7	1,201.7	1,577.9
Imports, cif	791.5	956.0	1,132.6	1,005.6	1,394.8
Trade balance	177.5	261.8	298.1	196.1	183.1
External Trade <i>annual change, percent</i>					
Exports	27.2	25.7	17.5	-16.0	31.3
Imports	19.9	20.8	18.5	-11.2	38.7
Balance of Payments <i>percent of GDP at current market prices</i>					
Exports	35.7	34.9	31.7	24.2	26.9
Imports	-27.7	-25.9	-23.8	-19.1	-22.6
Balance on goods	8.0	9.0	8.0	5.0	4.3
Current account balance	9.3	10.6	9.6	6.0	5.2
EXCHANGE RATES <i>Yuan per US Dollar</i>					
End of period	7.81	7.30	6.83	6.83	6.62
Average of period	7.97	7.61	6.95	6.83	6.77

Source: Asian Development Bank (ADB). www.adb.org. July 2012.

There are, however, certain facts that show that the economic growth model needs to be revised, in order to counterbalance certain challenges affecting the Chinese economy. These are the increasing inequality, the social contradictions, the environmental hazards, the weak technological innovation, the irrational industrial structure or the fragile agricultural structure, to name a few. This is the summary for China of the ADB Outlook 2012⁸. It reflects precisely the situation in a few lines:

Domestic demand rather than exports was the driving force behind 2011's strong performance, with high investment and consumption. The outlook for 2012 and 2013, despite uncertain global prospects, is for only moderately slower growth. The economy is gradually diversifying, with imports rising rapidly and the trade surplus now much less as a percentage of economic output. Currency appreciation, rising wage rates, increasing income disparities, and environmental concerns underscore the need for modifying the country's growth model. With a strong fiscal position and declining inflation, the government is well positioned to implement the 12th Five-Year Plan, designed to further transform the economy.

The Chinese Government is aware of the need for a change of economic model and, to that purpose it has developed a tool to implement such change: the 12th Five-Year Plan 2011-2015. Premier Wen Jiabao said in a speech at the Fifth Plenary Session in Beijing 6th March 2012⁹:

2012 is an important year for the 12th Five-Year Plan period and the last year of the current administration. We should accelerate the transformation of economic development model and adjustment of economic structure, strengthen self-innovation and energy saving and emission reduction, and facilitate socialist economic, political, cultural, social and ecological development in an all-round way.

Premier Wen Jiabao noted that the expected annual growth of GDP this year will be 7.5%, slightly lower than that of last year mainly because in consistency with the targets of the 12th Five-Year Plan. It will guide each region and department to focus on accelerating the transformation of economic development model and raising economic development quality and benefits to achieve long, high-level and better development.

We will make new progress in areas such as industrial restructuring, self-innovation, energy saving and emission reduction (...) We will keep on the implementation of a steady monetary policy, and keep on strict control of the loans to the industries with high energy consumption, heavy pollution or excessive productivity. We will achieve better combination of keeping

⁸ ASIAN DEVELOPMENT BANK (ADB). *ADB Outlook 2012. Confronting rising inequality in Asia*. www.adb.org. (p. 131 onwards). July 2012.

⁹ Wen Jiabao stresses that China will not seek economic growth at the cost of the environment and public health at the Fifth Plenary Session of the 11th National People's Congress (NPC). Ministry of Environmental Protection. www.english.mep.gov.cn. August 2012.

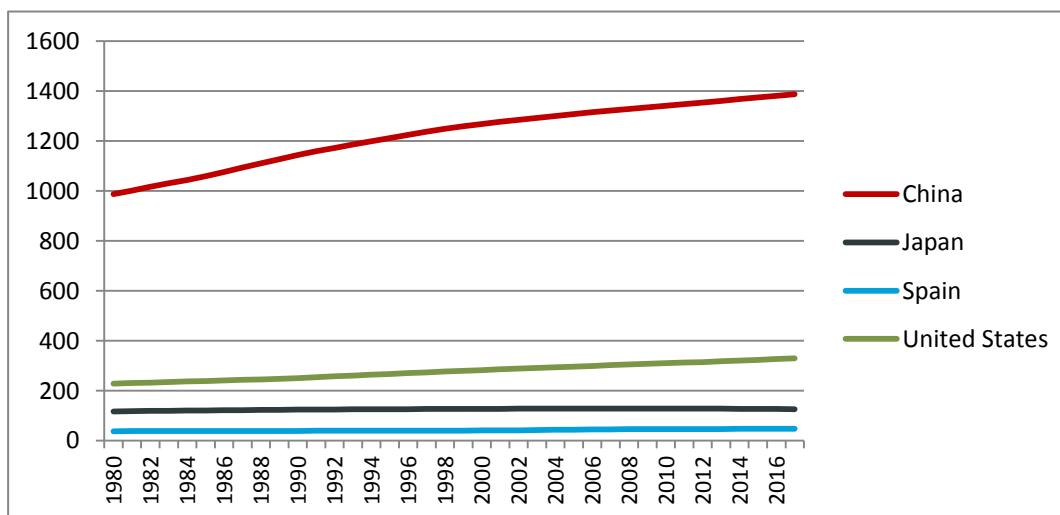
steady growth with controlling price, adjusting economic structure, benefiting public welfare, promoting reform and facilitating harmony.

To summarise, the Popular Republic of China is expected to continue growing, although at a slower pace compared to the last 25 years. With a population of over 1.3 billion people, it is surely going to surpass the US GDP in some years, a fact that is perfectly natural due to its much larger population volume. In addition, several factors are challenging China's economy and they will have to be dealt with in the next years. The following sections analyse in depth the accession of China to the World Trade Organization, the economic variables that influence the attractiveness of the Chinese marketplace (income, employment, middle class expansion...), and the challenges China is facing towards the future.

2. China, the most populated country in the world

The population of China was approximately 1,347 million people in 2011, around 30 times the population of Spain. As such China is therefore the most populous country in the world, accounting for more than 20% of the world's population. By 2016 the population is expected to be 1,380 million people, compared to 47 million of Spain (estimates carried out by the IMF¹⁰). In the graph we can appreciate both the evolution and the volume difference between the two countries.

Figure 5. Evolution of Population: China, Japan, USA and Spain 1980-2017. In millions

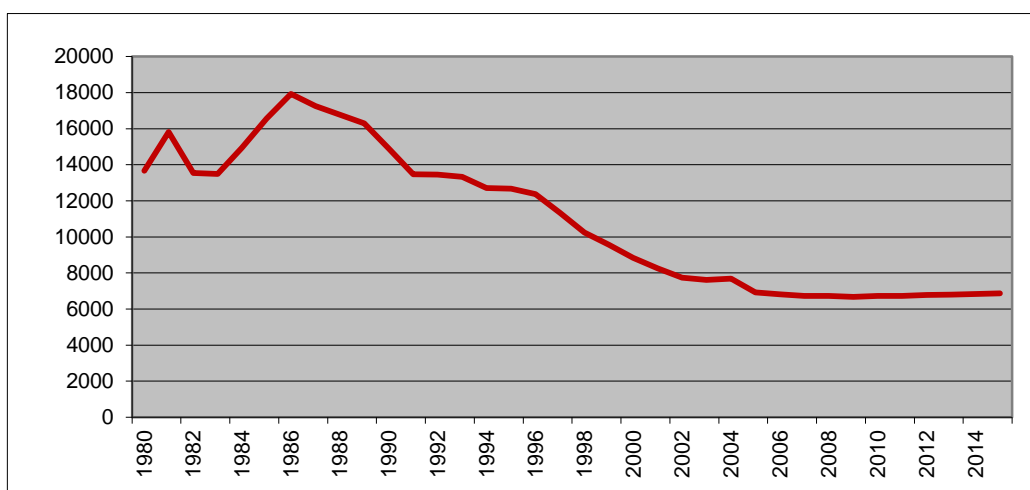


Source: IMF, World Economic Outlook Database (WEO), 2012. Estimates start after 2011.

¹⁰ INTERNATIONAL MONETARY FUND (IMF). According to the official IMF web site (www.imf.org), the International Monetary Fund (IMF) is an organization of 187 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world. The IMF publishes a range of time series data on IMF external trade, exchange rates and other economic and financial indicators. Some IFM data have been used for the present research, mostly the World Economic Outlook Database (WEO), the International Financial Statistics (IFS) and the Direction of Trade Statistics (DOTS) Database. September 2012.

While the population of Spain grew at a rate of 18% in the last twenty years (1996-2016), in the same period the population of China grew at a slower pace, 12% in the same years. However, if we consider the absolute figures, the growth in China means that every year, in the period 2000-2016, the total population increases by 6 to 8 million people.

Figure 6. Evolution of the annual population growth in China 1980-2014 (in thousands)



Source: IMF, World Economic Outlook Database (WEO), 2012. Estimates start after 2011

It is of special relevance in the case of China to establish a clear difference between the rural and the urban population. While a majority of 55.1% of the population is still rural compared to 44.9% urban population, the intense migratory movements make us believe that by 2035, 70% of the population will be living in the five largest urban areas: Shanghai (18.9 million), Beijing (16.7), Canton (7.8), Tianjin (11.8) and Chongqing (28.4)¹¹.

That means that the urban population - with access to products and services, with needs to be fulfilled and with some considerable purchasing power - from being around 600 million people, will become 1 000 million in the next 14 years.

To summarise, we can conclude that population growth accounts for an increase of 6-8 million people annually (80-100 million people in the next 14 years), but more importantly, some 400 million people will move from rural to urban areas in the same period of time.

At the end of 2012, the total employed population in China was over 800 million people, of whom around 128 were employed in urban areas. According to the National Bureau of Statistics, unemployment rate was 4,1%. This figure is questioned by some surveys that believe that the figure does not really reflect the real situation. Active population accounts for 59% of the total population (quite a low figure if we compare it with developed countries where it stands around 65%). The primary

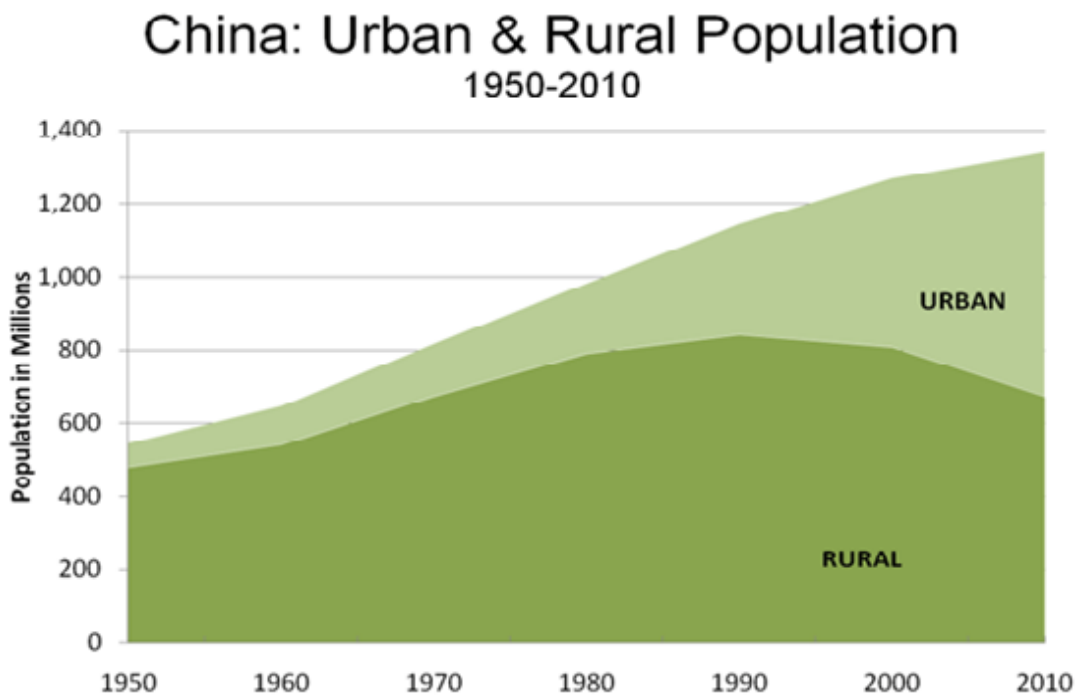
¹¹ INSTITUTO ESPAÑOL DE COMERCIO EXTERIOR (ICEX), *Country Guide, China*, 2010.

sector, which accounts for 11% of the GDP, employs 40% of the workers: this shows that the productivity is very low in this sector. Secondary sector accounts for 27% of the employment while services employ the remaining 33%. To a certain extent, the growth of employment and productivity in China comes from the migratory movements from low productivity rural areas to urban areas, where activities are more productive.

As we can see, migratory movements towards urban areas, combined with the increase in wealth in these areas, represent a new world of opportunities in terms of market growth that are currently taking place and that can be expected to continue in the future.

In 2011, the proportion of urban population was more than 50% for the first time ever. Statistics show that from 18% of urban population in 1978, it has reached 51.3% in 2011. The graph below shows clearly the growing importance of the urban population over the whole, mostly from the 80s.

Figure 7. Evolution of rural and urban population in China, 1950s-2010



Source: National Bureau of Statistics, Popular Republic of China.

Migration policy in China since the revolution has evolved significantly. According to Webber, Wang and Ying¹², the period 1958-84 was one of restricted migration, since industrialisation was unable to absorb all the peasants who had migrated to the cities. People could only move to cities if they had an employment certificate, were

¹² WEBBER, M.; WANG, M. *China's transition to a global economy*. Palgrave MacMillan. New York, 2002. (p. 12).

enrolled at a university or had a specific permission of the immigrating city. Since 1984, migration has been partially restricted. Peasants could migrate to market towns if they had savings, could provide their own accommodation or had managerial skills (they had to prove they had worked at a firm for several years). Such people could become legal town residents. More recently, however, mostly since year 2000, several provinces have begun to remove controls over migration. For instance, Guangdong province, according to the above mentioned authors, has completely removed all controls. Other provinces, such as Zhejiang, Beijing, Shanghai or Anhui have relaxed the restrictions over people mobility.

The main migration stream is, as one could expect, from the rural world to the cities. "Now, in rural areas of the centre and the east of the country, it is hard to find a household from which at least one male has not worked in a city, at least temporarily".¹¹

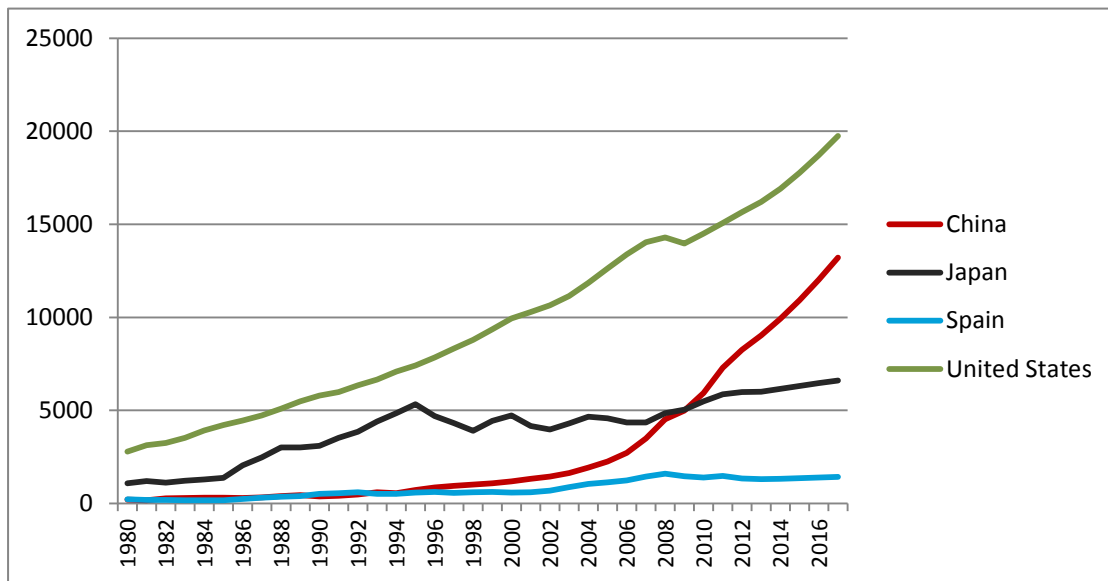
As peasants move to the cities, they shift residence, at least temporarily. But, even if they live in the city most part of the year, they mostly keep their registration in the village where they come from, because they prefer to remain tied to the land. In fact, they continue to do part-time farm work, helping the family that has stayed in the country. As a consequence, there is a mismatch between the location where they are employed (the city) and the registration location (the village). Therefore, information about the rate of migration is scarce. It is not easy to know exactly how many people live in rural areas versus urban citizens. It is very likely that urban figures are under-estimated.

3. China is still the fastest-growing country of the major economies

In 1980, the GDP of Spain was higher than that of China. As we can appreciate in the graph below, the situation changed in the 80s when the Chinese GDP overtook that of Spain, and since then the gap has become more pronounced, year after year. Deng Xiaoping, leader considered to have led China towards a market economy, is responsible for the economic reforms. In fact, his reputation involves being "the architect" of a new brand of socialist thinking: he developed socialism with Chinese characteristics and led his country's economic transformation through a series of reforms that became known as the "socialist market economy". Deng's initiatives included the opening of China to foreign investment, to the global market and private competition.

The goals of his reforms were summed up by the "Four Modernizations", those of agriculture, industry, science and technology and the military. Deng emphasized that socialism does not mean shared poverty and therefore he allowed the entrance of competition of market forces. His is the famous quote "It doesn't matter if a cat is black or white, as long as it catches mice", referring to the dilemma of communism versus capitalism. History has given him the credit for developing China into one of the fastest growing economies in the world for over 30 years and raising the standard of living of hundreds of millions of Chinese.

Figure 8. Evolution of GDP in China, Japan, USA and Spain, 1980-2017 (billions of US\$)

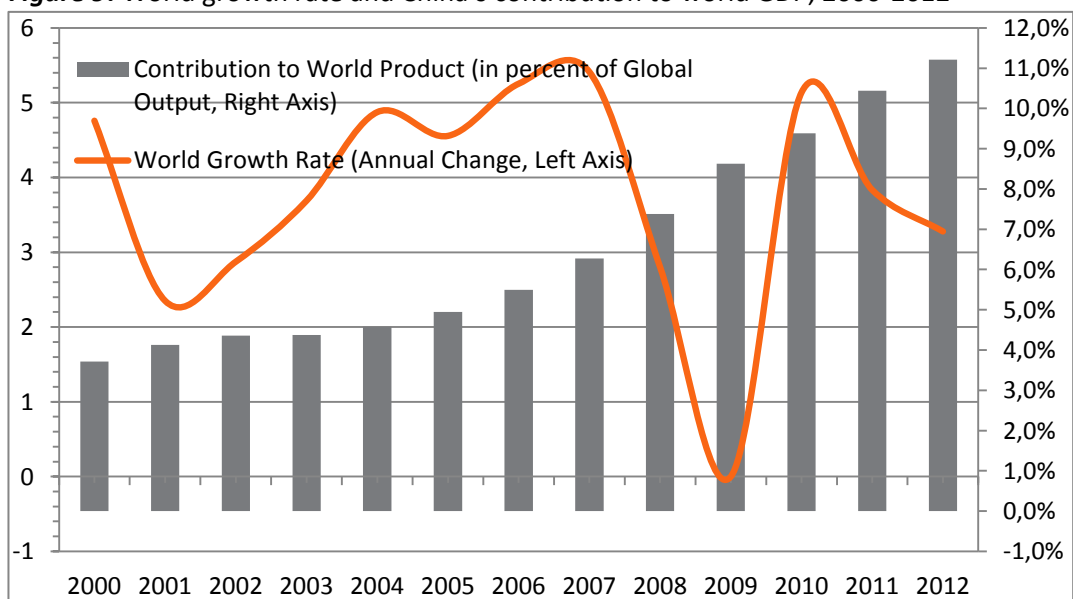


Estimates start after 2011. Billion US\$.

Source: IMF, World Economic Outlook Database (WEO), 2012.

China's GDP in 2010 was 5,800 billion US\$, second in the world after USA (14,600 billion US\$). It has only been in the past few years that China's GDP overtook Japan, Germany or France. China is still the most dynamic driver of growth in the world economy, with a growth rate of 9.2% in 2011. The growth target set by the Chinese authorities for 2011-2015 is 7% a year, which is below the recent trend. The estimates for the next years are all around 8-8.6%, which means that the country continues to be the fastest-growing of the world's major economies. The graph below shows China's contribution to world GDP, is over 8% since 2010. As parts of the world go into a recession, China's contribution to global GDP consolidates itself.

Figure 9. World growth rate and China's contribution to world GDP, 2000-2012



Source: IMF, WEO Database. 2012.

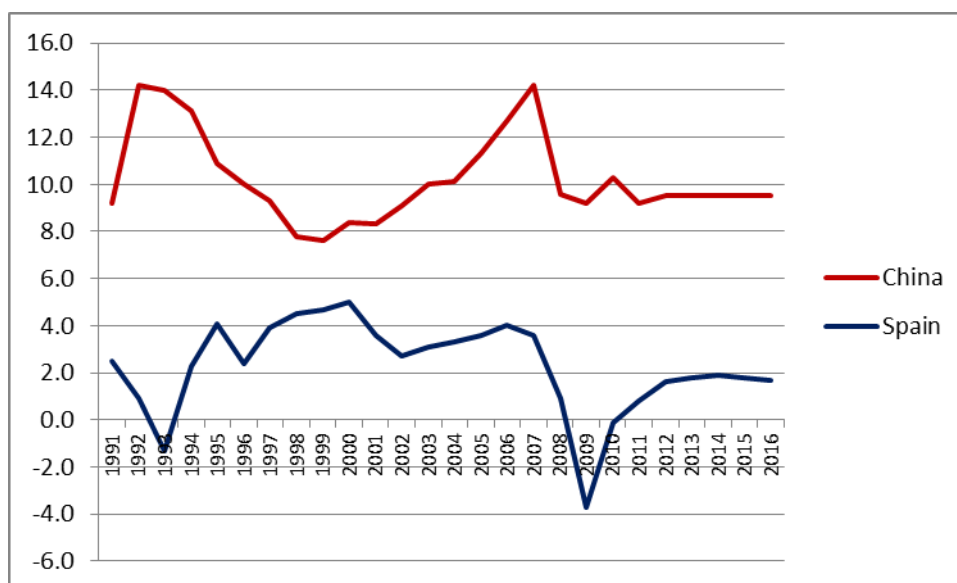
To continue with the comparison between China and Spain, if we stated that in 1980 Spanish GDP was higher than the Chinese, by 2010 Chinese GDP was four times that of Spain. Estimates assess that by 2016 Chinese GDP will amount to 6.5 times that of Spain. This is due to the astounding growth of the Chinese GDP: the average annual increase since 1990 has been 10%, compared to 2.3% in Spain. China has therefore grown at a speed five times as fast as Spain. We can see the annual growth details in the table below:

Table 4. Evolution of real GDP annual growth (in %)

GDP Annual growth (in %) Estimates start after 2011.		
Year	China	Spain
1991	9.2	2.5
1995	10.9	4.1
2000	8.4	5
2005	11.3	3.6
2010	10.4	-0.1
2011	9.2	0.8
2012	9.5	1.6
2015	9.5	1.8
2016	9.5	1.7
Total growth	266.0	59.6
Average annual growth	10.2	2.3

Source: IMF, World Economic Outlook Database (WEO), 2012, and own calculations.

Figure 10. Evolution of GDP annual growth, 1980-2016, China and Spain (%)



Source: IMF, World Economic Outlook Database (WEO), 2012, and own calculations.

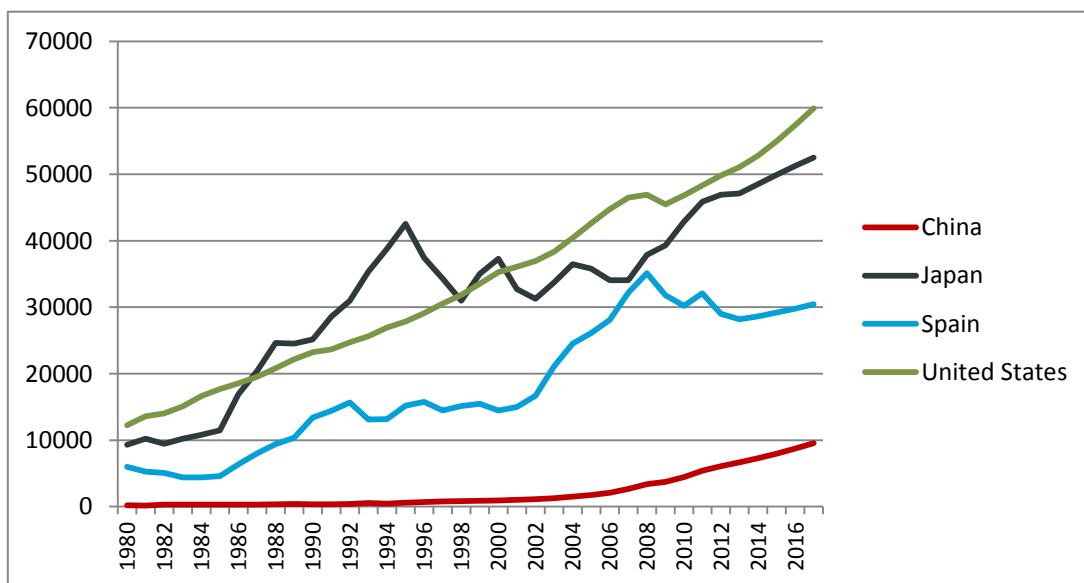
The picture somehow is transformed when we talk about GDP per capita, the unresolved (or one of the unresolved) matter for China. It is estimated that by 2013 the GDP per capita of China will more or less represent the same as in Spain in 1980. It will only get to 5000 US\$ per capita by 2012, but it is undoubtedly growing at a very stable and unmistakable pace. In fact, if in 1980 the GDP of a Spanish person was 30 times that of a Chinese, by 2016, it is estimated it will be only four times as big. Still a remarkable difference, no doubt, but significantly lower anyway.

Table 5. GDP per capita, current prices. US\$

GDP per capita, current prices. US\$		
	China	Spain
1980	205	6,005
1985	290	4,600
1990	341	13,408
1995	601	15,164
2000	946	14,464
2005	1,726	26,305
2006	2,064	28,244
2007	2,645	32,468
2008	3,404	35,364
2009	3,739	32,030
2010	4,382	30,639
2011	4,833	32,176
2012	5,321	32,947
2013	5,917	33,730
2014	6,589	34,601
2015	7,316	35,539

Source: IMF, World Economic Outlook Database (WEO), 2012. Estimates start after 2011.

Figure 11. Evolution of GDP per capita, China, Japan, USA and Spain, current prices, US\$. 1980-2017



Source: IMF, World Economic Outlook Database (WEO), 2012. Estimates start after 2011.

Considering how diverse China is and, more in particular, the great difference between rural and urban areas, we can probably say that the 8,000 US\$ per capita estimated for 2016 will not be very equally distributed: the one thousand million inhabitants concentrated in the main cities will probably account for most of the wealth, while it is estimated that the remaining 600 million living in the rural areas would hardly benefit from the per capita increase.

The growth of the GDP per capita in China is projected to grow by 10%, and even quite possibly to 20% or 30% year on year and it is foreseen that it will continue to do so following the IMF estimates until 2016. Perhaps at a slower pace (around 9-10%), which is in anyway a marked increase (compared with Spanish growth projections of 2 or 3% annually).

In order to continue with the analysis of GDP evolution, we can compare the growth in both countries, China and Spain, using the GDP Deflator¹³. The Index equals 100 for year 2005 (see table below). While the final index increases in both cases, the pace is remarkably different. The evolution of the Spanish index corresponds to a developed country with an economic slow down starting in year 2008. China's index, on the contrary, experiences an enormous pace of growth: more than 13 points from 2005 to 2011.

Table 6. GDP Deflator Index. Year 2005=100

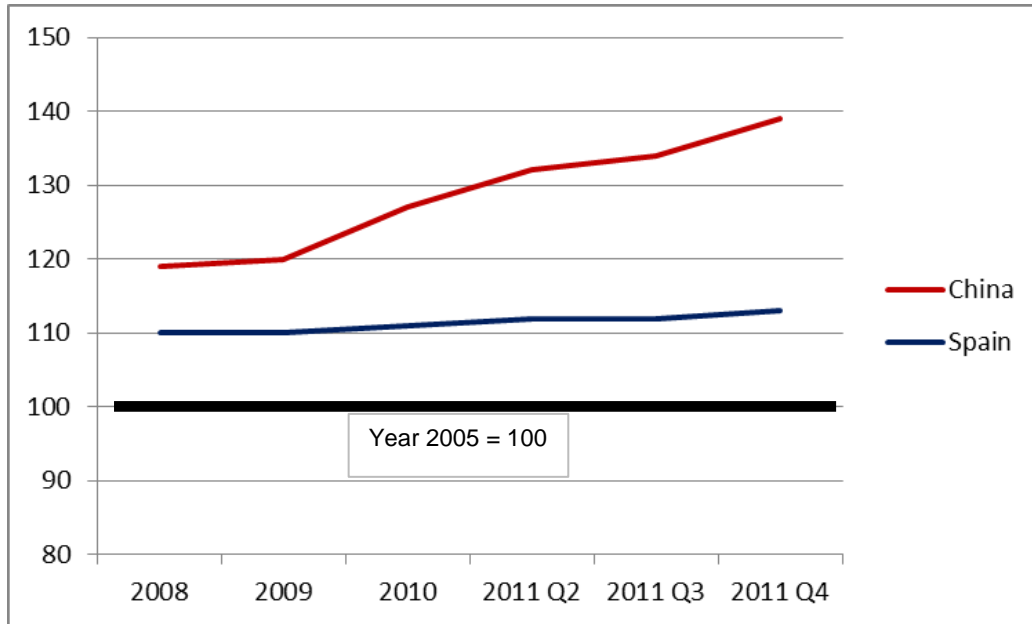
GDP, Deflator Index	2008	2009	2010	2011 Q2	2011 Q3	2011 Q4
China	119	120	127	132	134	139
Spain	110	110	111	112	112	113

Source: IMF. IFS Database. April 2012

The following graph shows the evolution of this deflator by means of a graph, comparing both countries. The line in black represents year 2005 and is equal to 100. As we can clearly observe, while the evolution is positive in both cases, the pace of the growth is much higher for China, especially after 2009.

¹³ The Gross Domestic Deflator (GDP Deflator) is an economic measure that tracks the cost of goods produced in an economy relative to the purchasing power of the US dollar.

Figure 12. GDP Deflator Index – China and Spain. Year 2005=100



Source: IMF. IFS Database, April 2012.

Increasing GDP with a rising inflation

According to IMF estimates, the GDP growth for China is still very high but slowing down slightly (8.3% forecast for 2012). At the same time, inflation is on the increase (3.7% estimates for 2012). To summarise, while GDP growth is still strong, inflation starts to pose a risk. However, the increase in consumer prices has been kept under control. Published figures by the Asian Development Bank (ADB) show an inflation rate of 5.4% in 2011¹⁴. One year later, the figure has been kept to a minimum of 3.7%.

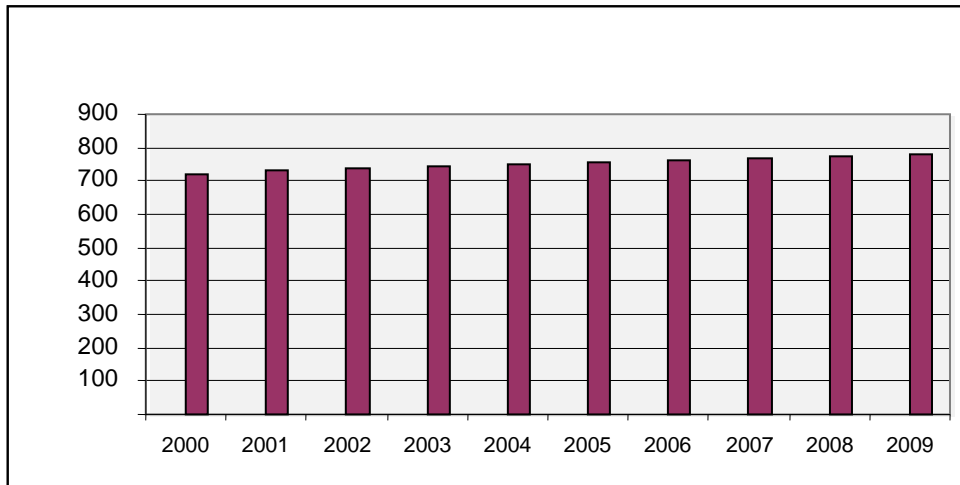
Industrial production in China grew by 9.3% in 2011, following the same sources as above. Apart from China, very few other countries managed to grow their industrial production by more than 8%: Egypt, Taiwan and Japan. In the same period, Spain's industrial production fell by 10.4%.

4. Low unemployment figure

The number of persons employed in China is increasing, going from 720 million in 2000 to 780 million by 2009, according to IMF figures. This means that 60 more million people hold a job in the short period of 9 years, what represents an increase of 8% (see graph below). In the same period, in Spain the numbers of persons employed moved from 15 to 18 million.

¹⁴ ASIAN DEVELOPMENT BANK (ADB). Development Indicators and Policy Research Division. Basic Statistics 2012. www.adb.org. July 2012.

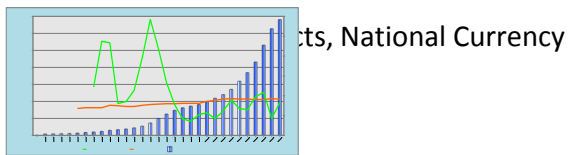
Figure 13. Evolution of the persons employed in China, in millions.



Source: IMF. IFS Database, April 2011.

Below we can see the main three indicators in clearly differing evolution: constantly growing Gross Domestic Product, unemployment rate and variable consumer prices.

Figure 14. Evolution of China's key indicators: GDP, unemployment rate and consumer prices, 1980-2009



Source: IMF. IFS Database, June 2012.

4.1. Urban workforce

New employment positions filled in China's urban areas hit 8.51 million in the first nine months of 2009, according to the the Ministry of Human Resources and Social

Security (MHRSS)¹⁵. The figure accounted for 94 percent of the government's annual target of 9 million, ministry spokesman Yin Chengji told a press conference.

The number of newly employed people in China's urban areas had reached 900,000 a month in 2010. Moreover, in the first nine months of 2009, 4.02 million laid-off workers found new jobs, accounting for 80 percent of the government's target of 5 million for the whole year.

By the end of the third quarter, 9.15 million people had registered as unemployed in urban areas, a rate of about 4.3 percent, unchanged from the number reported at the end of the second quarter. 74% of the 6.11 million new graduates from the country's universities and colleges had been employed as of Sept. 1, which was moderately higher than the ratio from a year earlier. The government has resorted to a series of measures to help college graduates find jobs, such as giving them preference in military recruitment and encouraging them to take grass-roots posts in the countryside and relatively poor western regions.

4.2. Unemployment

Regarding unemployment, it is remarkably low in China, 4.1% in 2010¹⁶, and estimated around 4% for the coming years until at least 2016, according to IMF estimates. Although an effort is being made by the Chinese Government to improve the quality of statistics, there are still doubts about their accuracy. Therefore, data should be analysed with caution. Nevertheless, it can be stated that unemployment rate is low: this means that the demand for goods and services is going to continue to grow, as more and more workers join the workforce. Clearly, if we compare these figures with 24.1% of unemployment in Spain in March 2012¹⁷, we can see how the Spanish market is very mature - and not expected to grow significantly in the coming five years.

Such low unemployment rates as the one found in China could only be found in very few countries in the western world such as Switzerland (3.1%), Norway (3.2%), or Austria (4.0%), or in Asian countries like Malaysia (2.9%), South Korea (3.5%), or Taiwan (4.2%). In the other extreme of the spectrum we can find countries with soaring rates such as South Africa (25.2%), Spain (24.1%) or Greece (21.7%).

5. China is optimistic about the future

When analysing Chinese confidence levels, we can quickly appreciate how, compared to the general pessimism found in Europe, the Chinese are confident about the future. It is a well-known factor that, in economics, confidence means a great deal.

¹⁵ XINHUANET NEWS AGENCY. www.news.xinhuanet.com/english/. October 2011.

¹⁶ NATIONAL BUREAU OF STATISTICS OF CHINA. www.stats.gov.cn. June 2012.

¹⁷ INSTITUTO NACIONAL DE ESTADÍSTICA (INE). www.ine.es. June 2012.

Table 7. Chinese climate business, entrepreneur confidence and consumer confidence indexes. Evolution 1999- 2011

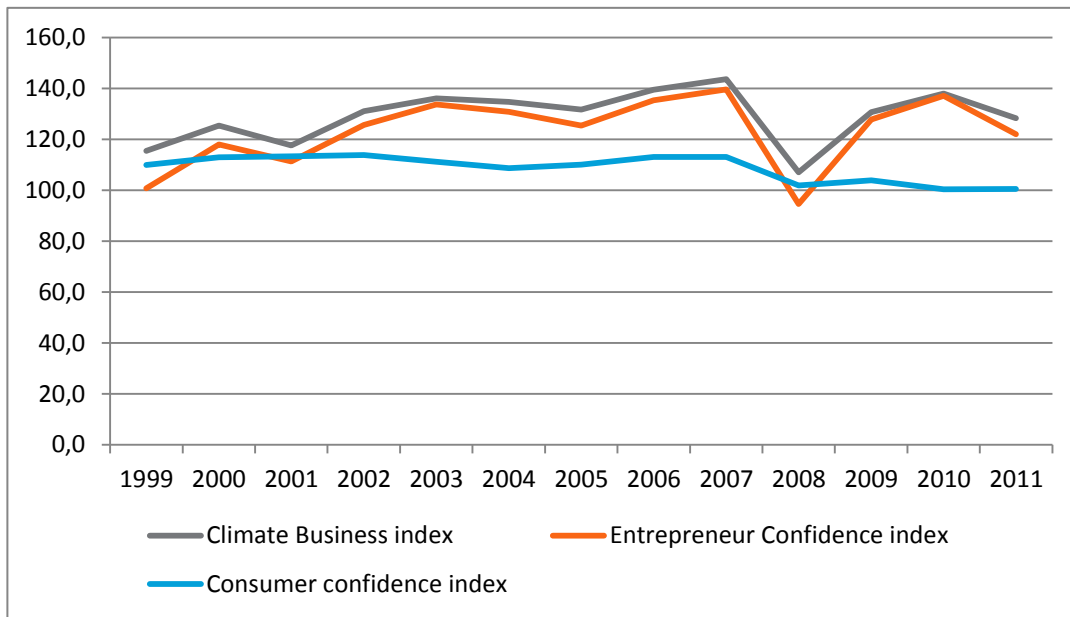
	Climate Business index (a)	Entrepreneur Confidence index (b)	Consumer confidence index (c)
1999	115.4	100.7	109.9
2000	125.4	117.9	112.9
2001	117.6	111.3	113.3
2002	131.0	125.6	113.8
2003	136.0	133.7	111.2
2004	134.7	130.8	108.7
2005	131.7	125.4	110.0
2006	139.4	135.3	113.1
2007	143.6	139.6	113.1
2008	107.0	94.6	101.8
2009	130.6	127.7	103.9
2010	138.0	137.0	100.4
2011	128.2	122.0	100.5

Source: Bloomberg

- (a) **The Business climate index** is the quantitative description of the business climate survey, which can directly reflect the real situation of the economy. The business climate index is ranging from 0 to 200%. 100 is the critical value, when the climate index is larger than 100, it indicates that the economic performance is picking up or improving. When it is lower than 100, it shows that the economic performance is declining or worsening.
- (b) **The Entrepreneur confidence index** reflects the confidence of entrepreneurs on China's macroeconomic environment and takes the same ranges as (a).
- (c) **The Consumer confidence index** is an average of responses to the following questions: 1. Respondents appraisal of current business conditions. 2. Respondents expectations regarding business conditions six months hence. 3. Respondents appraisal of the current employment conditions. 4. Respondents expectations regarding employment conditions six months hence. 5. Respondents expectations regarding their total family income six months hence.

Apart from the 2008 sudden drop in the confidence levels for both the general climate and the entrepreneurs – that recovered quickly afterwards- the indexes remain well over 100. The consumer confidence index is somehow shy and far from the levels of 2007 and before, well over 110. It can be stated that consumers are no doubt affected by the general world economic recession. However, overall, the climate is of moderate optimism, with confidence on the performance of the economy.

Figure 15. Evolution of different Confidence Indexes in China 1999-2011

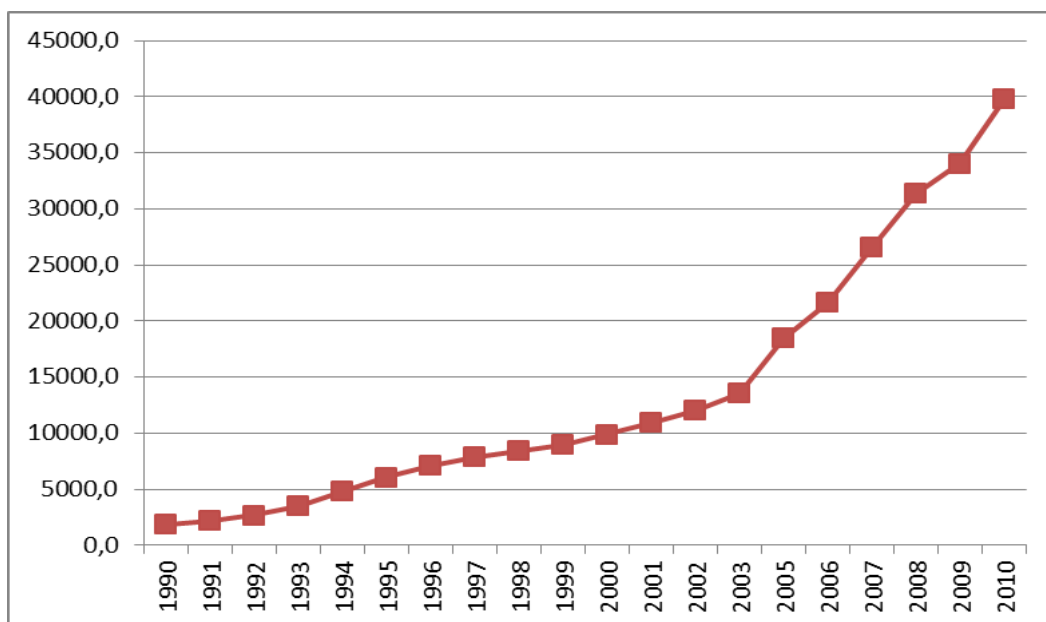


Source: Bloomberg

6. Household and government consumption on the rise

Expenditure on GDP at current market prices in China is on the rise. During the period between 1990 and 2010 expenditure multiplied itself by more than twenty times, reaching almost forty thousand billion yuans. In other words, in twenty years it has multiplied by twenty times, showing the increasingly great need to provide itself with absolutely everything, see graph below.

Figure 16. Evolution of expenditure on GDP at current market prices. China 1990-2010. Billions of RMB, calendar year



Source: Asian Development Bank. Key Indicators for Asia and the Pacific.

This soaring consumption growing at such a fast pace is related to both domestic and public spending. If we look at the figure below, we can appreciate that both indicators increase by 14 and 20 times in the relatively brief period of 20 years. We can therefore conclude that, in principle, there are opportunities for both the private and the public sector.

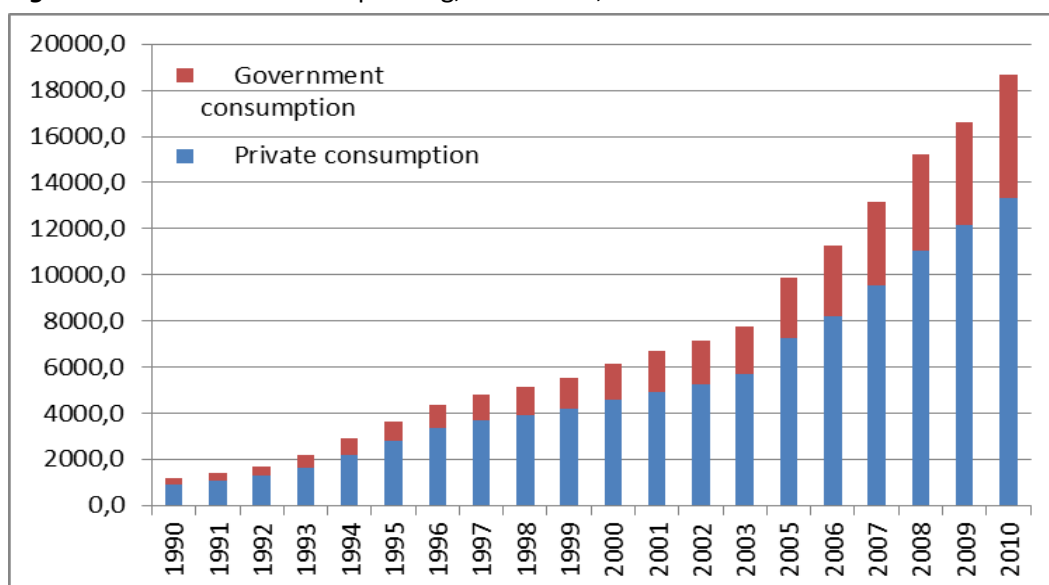
Table 8. Consumer spending in China, billions of RMB

Year	Expenditure on GDP at current market prices	Private consumption	Government consumption
1990	1866,8	945,1	264,0
1995	6079,4	2837,0	837,9
2000	9921,5	4585,5	1566,1
2005	18493,7	7265,3	2639,9
2006	21631,4	8210,4	3052,8
2007	26581,0	9561,0	3590,0
2008	31404,5	11059,5	4175,2
2009	34050,7	12171,3	4441,3
2010	39798,3	13329,1	5361,4

Source: Asian Development Bank, 2012

The graph belows shows the evolution of both the private and government consumption.

Figure 17. China: Consumer spending, 1990-2010, Billions of RMB

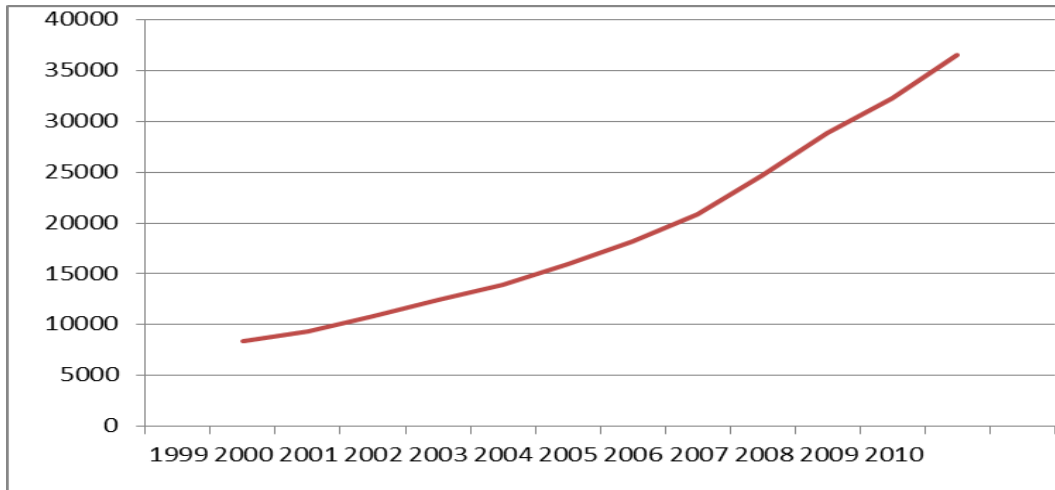


Source: ADB, 2012.

Average salaries are also increasing rapidly, at least in the cities. In the last decades these wages have increased every year by more than 10%: sometimes by 12% but

other years up to 18%. One of the consequences of this fact – the one that interests us at this point- is that workers in urban areas have an increasing disposable income to spend in consumption goods¹⁸.

Figure 18. Average earnings by urban workers. RMB



Source: Bloomberg

As wage levels in China have recently been critically analysed (for instance, Foxconn, a key supplier for Apple, amongst others, raised salaries at their China factories by 25 percent recently following international disapproval after suicides scandal), the country’s minimum wage levels have been rapidly rising. The Chinese government has been increasing minimum wage levels by 15 percent to 25 percent annually for the past three years. Rates vary by region and are set by each respective local government, calculated together with a number of other indicators, including the local housing market. They are also expected to grow over the coming years as China looks to shift its economy towards a more consumer-oriented society. To achieve that goal, Chinese citizens need to have increasing levels of disposable income so demand for products and services can increase.

A contradiction between two models is appearing. On the one hand, China must keep salaries being low and long working hours, to remain competitive. On the other hand, there is a strategy to rise salaries and promote the consolidation of a large middle class. In the next few years, China will have to decide which path is finally going to take.

The map below helps understand how the wage levels are distributed along the country: the east coastal provinces boast relatively higher minimum wage levels than the more slow-to-develop western areas. It is however important to note that, to retain workers, employers must normally pay more than the minimum salaries fixed by law: “Minimum wages are of course the legal minimum, and increasingly in

¹⁸ Such increases in salaries have other immediate consequences such as the loss of competitiveness of the Chinese economy. However, this factor is properly analysed in a different section of this paper.

China are not applicable in any sensible business model – assuming one wishes to retain workers”. It is also important to add that “on top of wages, employers must also contribute mandatory social welfare benefits for each of its employees. This again varies by region, but can add an additional 40 percent to 50 percent on top of each Chinese employee’s base salary”¹⁹.

Figure 19. Geographical distribution of minimum wages



Source: China Briefing.

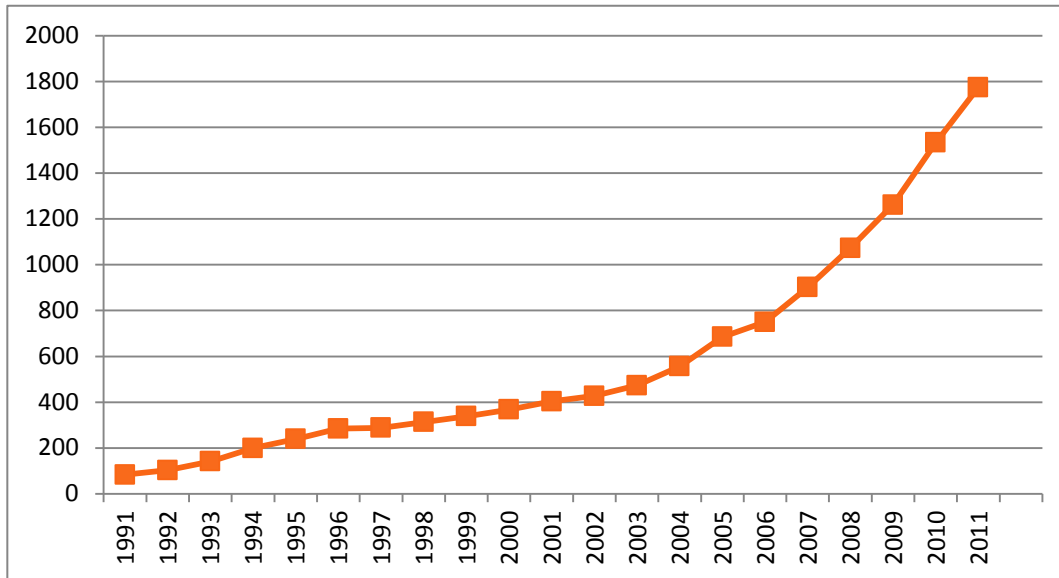
Following with our analysis, we move forward to analyse what has been the evolution of retail sales. According to Bloomberg’s CNRSCONS Index²⁰, Chinese retail

¹⁹ CHINA BRIEFING. www.china-briefing.com. March 2012.

²⁰ Retail Sales of consumer goods include: 1) Sales of wholesale and retail enterprises: consumer goods sold to urban and rural households: commodities sold to foreigners, overseas Chinese and Chinese compatriots from Hong Kong, Macao and Taiwan visiting in China, commodities sold to government agencies, institutions, social organizations, military and armed police units, and commodities sold to enterprises in the form of retail sales. 2). Sales of staple food, cooked dishes, beverage, tobacco and other articles by catering units 3). Sales of books, newspapers, magazines, audio-visual products and post products by publishing and post departments to urban and rural households and to enterprises, institutions, military and armed police units. 4). sales of food, beverage, tobacco, garments, footwear, headgear, articles for daily use, medicines, medical and health articles, work of art, handicrafts, toys, funeral articles and other articles by other service trades.

sales have increased on average by 11% in the last 22 years. Moreover, in some years in particular 2005, 2007 and 2010, the growth has surpassed 20%.

Figure 20. Evolution of retail sales in China. Billions of RMB



Source: Bloomberg

7. High income inequality but a powerful emerging middle class

Moving on with our research, we should now consider a very different kind of variable that takes into account, not the evolution of absolute numbers, but how the wealth that is undoubtedly being created in China is distributed.

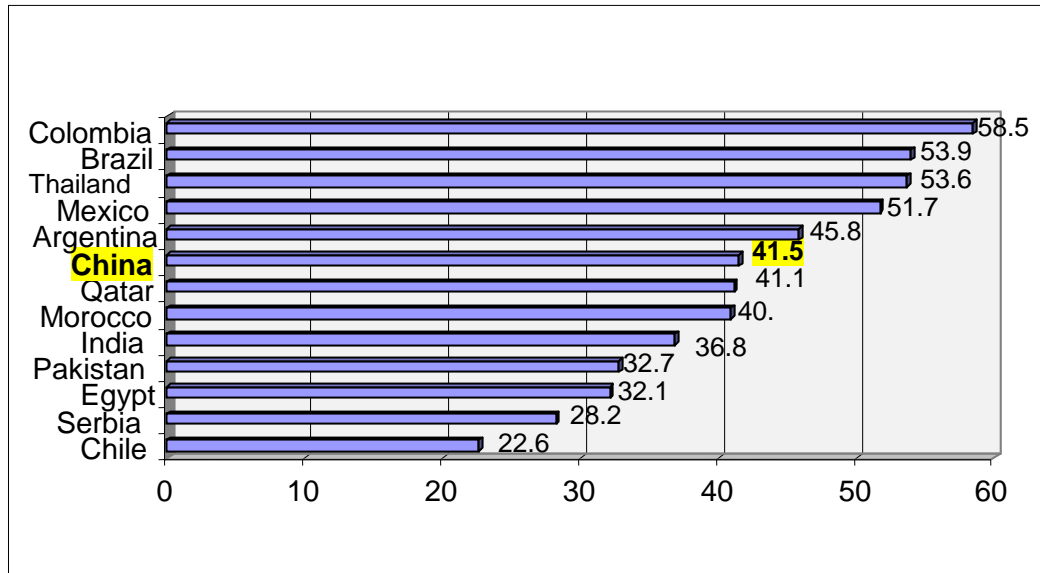
For this, we will analyse the “income equality”: that is the ratio of the share of national income going to the richest 20% of households in a country, to the share of the poorest 20%. This indicator, calculated by the World Bank²¹, gives an idea of the existing inequality in a country: the highest world figures are mostly found in Latin American countries (in Colombia, the most extreme case, the income of the top fifth is almost 25 times that of the bottom fifth). Most emerging Asian countries are less unequal: in China, the income of the richest 20% persons is 8 times the income of the 20% poorest.

If we take a similar index, the Gini index, where 100 points would mean perfect inequality, China scores 41.5 points. This shows that inequality in this country is higher than in countries such as India, Pakistan or Egypt. To complete the

²¹ WORLD BANK. www.worldbank.org. Gini index measures the extent to which the distribution of income (or, in some cases, consumption expenditure) among individuals or households within an economy deviates from a perfectly equal distribution. A Lorenz curve plots the cumulative percentages of total income received against the cumulative number of recipients, starting with the poorest individual or household. The Gini index measures the area between the Lorenz curve and a hypothetical line of absolute equality, expressed as a percentage of the maximum area under the line. Thus a Gini index of 0 represents perfect equality, while an index of 100 implies perfect inequality. August 2012.

international comparison, the average for the EU is 30 points while the one for Spain is 34.

Figure 21. Income inequality comparison amongst different countries, measured by the Gini Index (100= perfect inequality), 2010



Source: World Bank. April 2011.

According to some authors such as Wei, overall inequality not only is high in China, but “over the last two decades, overall inequality in China has risen”.²² This is going to be one of the problems that the Chinese Government has not yet been able to tackle successfully and it is bound to become one of the weaknesses of the Chinese society in the future.

As a matter of fact, the problem lies mostly in the evolution of the inequality: in 1970 China represented one of the most equalitarian distributions of income and wealth in the world. However, the formidable growth experimented from the beginning of the opening to the outside world in 1978 brought along a growing inequality. According to an Economic Report by the OECD in February 2010, this trend is no longer so, and the increasing differences between the poorest and the richest are no longer growing. The change in the trend has been favoured mostly by two factors: first, the increase in social expenditure in rural areas and, second, by the migratory movements from the rural areas towards urban areas. This shows that the poverty pockets are mostly concentrated in China’s rural world.

According to the latest ICEX China Country Report²³, Gini’s Index of 16 (relative equality) moved to 48 in 2011. Moreover, some experts establish its value as high as 53: this implies inequality of the income in China is larger than in United States,

²² WEI, S. J. *China as a window to the world : trade openness, living standards and income inequality*. Reserve Bank of Australia, 2002. www.rba.gov.au/publications. June 2011.

²³ ICEX, *Country Guide: China*. www.icex.es. May 2012.

Korea, or most of Europe, but smaller than in South Africa, Russia, Indonesia or Turkey.

While economic growth in China in the last three decades has taken out of poverty some hundred million people, the income of the richest has grown even faster. Most of the inequality comes from the differences between the rural versus the urban world. In 2010 the rent per capita in the cities was about 5,500 US\$. The one in the country was between a third and a fourth of it. If we add to this that propensity to save is larger for those who earn more, we conclude that the inequality tends to grow over time. In terms of market opportunities, if private consumption is to be increased, it is necessary that the rent distribution is improved considerably. This is perhaps not true for some sectors, namely the luxury goods, but it is certain for most of the others, and more importantly, for China's wellbeing, for justice and for the development of a fair and stable country.

7.1 Emerging middle class

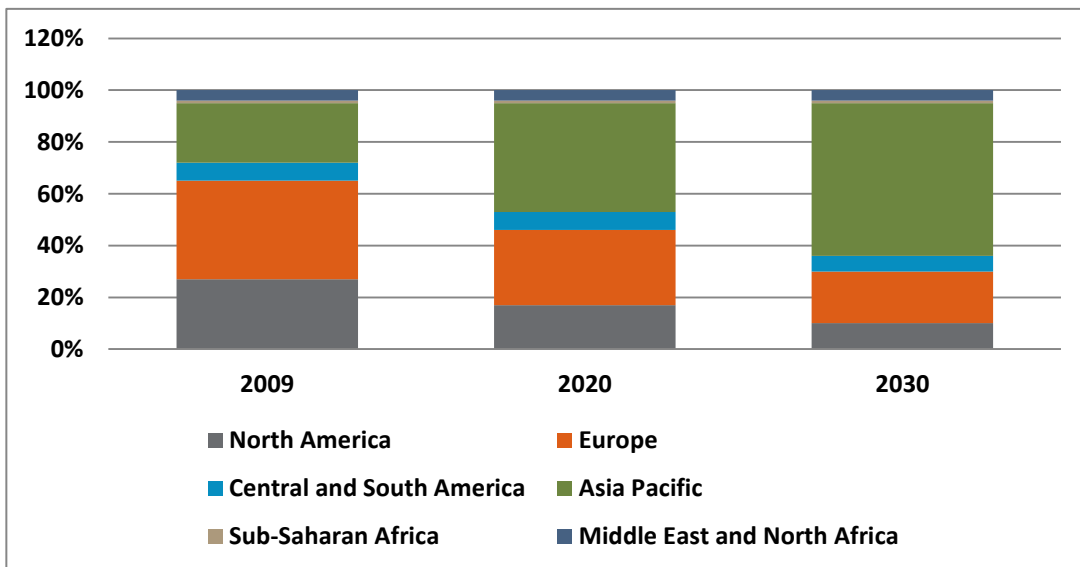
While there is a shift in wealth from the western world towards the so-called emerging countries or BRICS, the structure of social classes in these countries also alters, mainly with the emergence of a powerful middle class. All the authors, experts and publications consulted coincide that the middle class in China is, firstly, increasing at a very high pace, and, secondly, the engine of the economy and the consumption in this country. H. Kharas, a world expert on the subject, states in his wellknown paper on the emerging middle classes in developing countries that "over the coming decades, Asia's emerging middle class will be large enough to become one of the main drivers of the global economy".²⁴

Two thirds of the world's middle class population is expected to be in the Asia-Pacific region by 2030, as against 21% in Europe and North America. The dynamic growth that is forecast for the middle class in China and India could partly offset the stagnation expected in North America and Europe. It is also consistent with the greater emphasis the Chinese authorities wish to place on domestic demand (and, within this, consumption) in future growth, partly in response to the need to reduce imbalances between rural and urban areas and between the dynamic coastal zones and the less developed interior.

The graphs below show the distribution of the middle class population by world's main regions.

²⁴ HOMI K. *The emerging middle class in developing countries*. OECD Development Centre. Working Paper n. 285. January 2010. Homi Kharas is a senior fellow and deputy director for the Global Economy and Development program. Kharas also works with the Development Assistance and Governance Initiative. Formerly a chief economist in the East Asia and Pacific Region of the World Bank, Kharas currently leads a research project on aid agency effectiveness, and also has expertise on East Asia development and global economic trends.

Figure 22. Distribution of the middle class population by main world regions



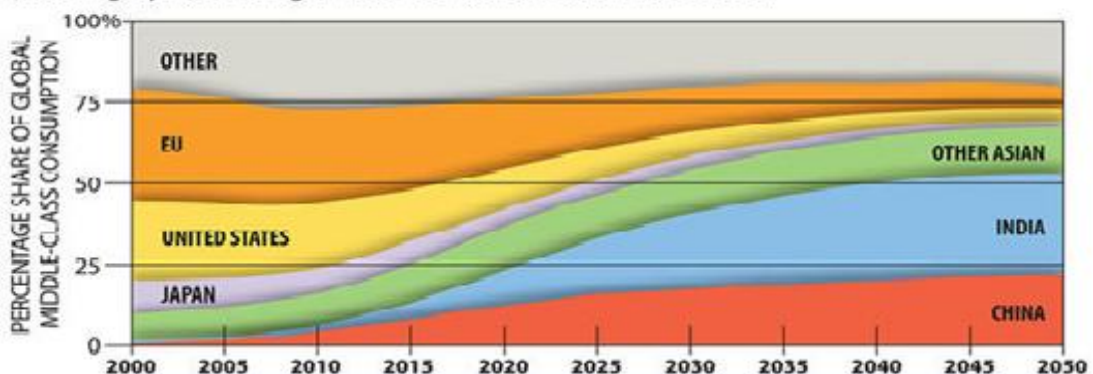
Source: Economic Commission for Latin America and the Caribbean (ECLAC)

There are of course many discussions on how to define middle class: it could be defined as the “ability to lead a comfortable life”²⁵ from a subjective point of view. Its importance lies mainly on the fact that middle class is the source of consumption, entrepreneurship and innovation. Since the definition of middle class is not the objective of the present research, we will assume Kharas’ definition in his above mentioned paper: “this paper defines a global middle class as all those living in households with daily per capita incomes of between USD10 and USD100 in PPP terms”, which offers the advantage of a more objective and operational definition.

Figure 23. Growing middle class consumption in China

The global middle-class wave

Global middle-class consumption will shift heavily toward China, India, and other Asian countries (excluding Japan) as the high-income countries see their share decrease.



Source: H. Kharas, OECD.

²⁵ GEOFFREY G.; HOMI K. *The new global middle class: a cross over from west to east*. Wolfensohn Center for Development. Brookings, 2010.

Kharas, by combining household survey data with growth projections for 145 countries, showed that Asia accounts nowadays for less than one quarter of today's middle class. But, and here lies the most important fact, by 2020, that share could double. As a result, more than half the world's middle class will be in Asia, and Asian consumers will soon account for over 40 per cent of global middle class consumption. How can this be explained? According to Kharas' findings, a large mass of Asian households have incomes today that position them just below the global middle class threshold. Therefore, increasingly large numbers of Asians are expected to become middle class in the next ten years.

How is that general trend for Asia translated into a reality for China? According to Kharas, China's middle class today is already very large in absolute terms – estimated at 157 million people. Only the United States has a larger middle class. This represents an enormous opportunity and explains why so many retailers and businesses are anxious to penetrate the Chinese market.

China accounts for over 20% of the world population and has a constantly growing middle class, making it a market of huge potential. The rise in per capita income expected over the coming decades should boost both the size and the purchasing power of the Chinese middle class, turning it into a key market for food, higher-quality wearing apparel, tourism, pharmaceuticals, medical services, retail services and luxury goods, among other goods and services.

Table 9. Population growth in the world

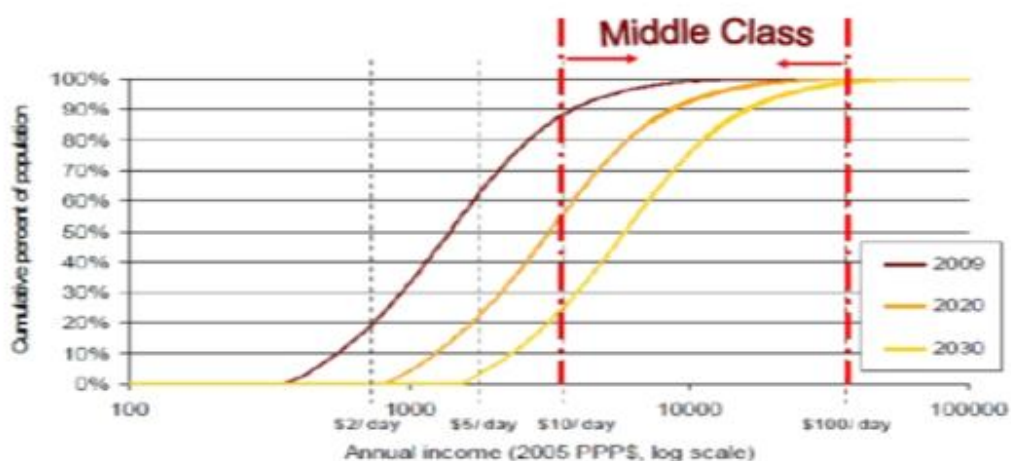
Selected regions and countries: population growth	(Millions of people annualized growth rates)					
	2010	2020	2030	2040	2050	Annualized growth rate, 2010-2050
Latin America and the Caribbean	585.0	647.1	696.5	696.5	746.0	0.6
Central America	42.5	50.5	58.3	58.3	71.6	1.3
South America	392.3	431.2	461.1	461.1	487.6	0.5
The Caribbean	36.3	39.2	41.2	41.2	42.3	0.4
Mexico	113.4	125.9	135.4	135.4	143.9	0.6
Asia	4164.3	4565.5	4867.7	4867.7	5142.2	0.5
China	1341.3	1387.8	1393.1	1393.1	1295.6	-0.1
South East Asia	593.4	655.9	706.0	706.0	759.2	0.6
India	1224.6	1386.9	1523.5	1523.5	1692.0	0.8
Other Asia	1004.9	1134.9	1245.2	1245.2	1395.4	0.8
United States	310.4	337.1	361.7	361.7	403.1	0.7
European Union	499.3	509.7	514.5	514.5	510.3	0.1
World	6895.9	7656.7	8321.4	8321.4	9306.1	0.8
Chinese share of the total	19.5	18.1	16.7	16.7	13.9	...

*Includes Brunei Darussalam, Cambodia, Philippines, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Singapore, Thailand, Timor-Leste and Vietnam.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations, *World Population Prospects*, 2010 revision.

The graph below illustrates this point: China’s middle class is still small compared to the size of the total population, but is quickly on the increase thanks to economic growth.

Figure 24. China’s middle class is small but quickly rises. Percentage of middle class population falling within the threshold of US\$10/day to US\$100/day



Source: H. Kharas, OECD

Over the last 25 years, America’s consumption has been perceived as a major driver of the world economy. However, China’s middle class is expected to surpass America’s by 2020.

According to the authors of the study *The \$10 trillion prize*²⁶, the real growth of the middle classes is going to take place in India and in China: “Consumers in India and China are the new kings and queens of the global economy. They have fast-changing tastes and appetites and they are transforming the world with their consumption”.

Table 10. Lifetime consumption patterns in China

Consumption patterns	Born in 1960	Born in 2009
Life expectancy (years)	47	73
Per capita consumption at birth (US\$)	102	1,429
Per capita consumption at death (US\$)	1,129	21,400
Lifetime consumption (US\$)	16,443	632,024
	➔ multiplied by 38 times	

Source: Silverstein and other authors. *The \$10 trillion Prize*.

²⁶ SILVERSTEIN, M.J. AND OTHER AUTHORS. *The \$10 Trillion Prize. Captivating the Newly Affluent in China and India*. Harvard Business Review Press. Boston, 2012. (p. IX)

The newly affluent consumers save enormous percentages of their income (over 50% of the GDP is saved for future use). They save, among others, because of the lack of social security net, the education for their children and the rising job insecurity. However, it is expected that the feeling of optimism for the long term will gradually move them from saving to spending.

As they become wealthier, Chinese consumers look for branded goods. They focus mostly on the brand because they see it as an indicator of quality and functionality. The first goods that are chosen by the new upper class are luxury items and prestige cars. After those two, they choose life-enhancing activities, such as dining out, going to the cinema, playing sports and going on overseas trips, especially to the USA and Europe.

Table 11. Consumers' reasons for trading up, by country

Reasons for trading up	Respondents (%)						
	China	India	Brazil	Russia	USA	Europe	Japan
Because of the brand name	70%	64%	60%	26%	30%	19%	24%

Source: Silverstein and other authors. *The \$10 trillion Prize*.

China's twelfth five-year plan (2011-2015) is designed to reorient the Chinese economic towards a model that is more reliant on domestic consumption, more sustainable, more socially cohesive and more innovative. Rebalancing towards greater domestic consumption is necessary not only to offset the expected weakness in demand from industrialized countries but also to improve distribution indicators, which show deterioration in earnings and a rise in income concentration:²⁷ "One very ambitious goal is to universalize medical insurance coverage by incorporating a further 200 million people into the scheme, this will be accompanied by greater public spending on social housing and social insurance in an attempt to narrow differences in incomes and quality of life between the urban and rural populations".

According to Evelyn Hollands²⁸, Director at HKTDC, by 2012 the middle class in China will be 18% of its population. This represents 243 million people, the world's largest.

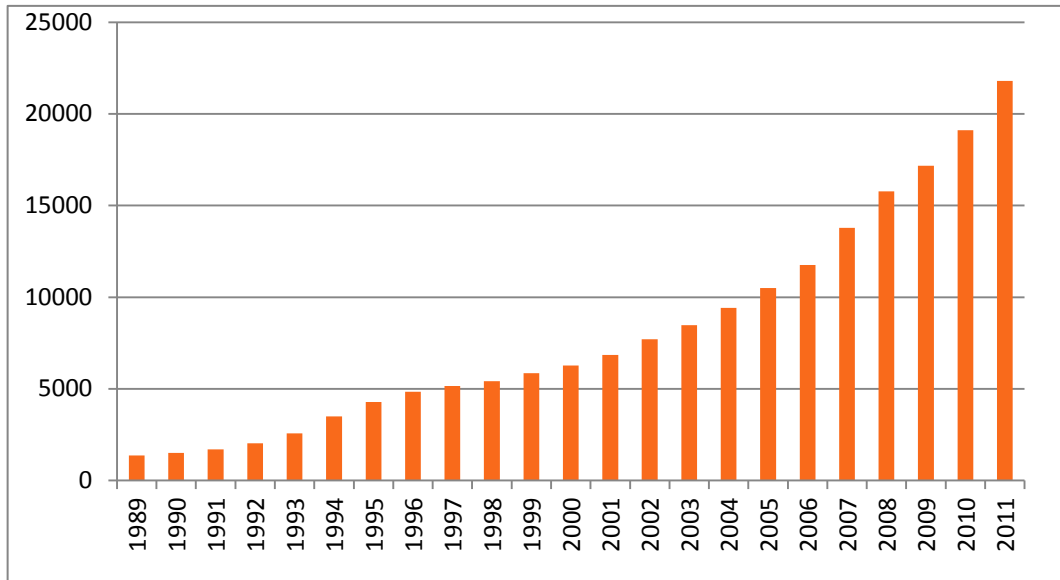
Another interesting variable can be added here, the per capita annual disposable income of urban households. The evolution in absolute figures has been from 1,374 in 1989 to 21,810, which represents sixteen times more in the 23 year period. This

²⁷ ECLAC. *The People's Republic of China and Latin America and the Caribbean*. United Nations. 2012 (p.18).

²⁸ HONG KONG TRADE CENTRE. www.hktdc.com. Evelyn Hollands, Director at Hong Kong Trade Centre. Service organisation whose mission is to create opportunities for Hong Kong companies, by promoting trade in goods and services, while connecting the world's small and medium-sized enterprises through Hong Kong's business platform. June 2012.

means that in urban areas, the disposable income of households has grown enormously, with the resulting increase in the demand for all sorts of consumer goods. This represents a great market opportunity for Chinese products and for foreign ones as well. As it will be explained in chapter 5, Chinese people spend a lot of time shopping and they value very highly all the western goods, in particular European and American brands.

Figure 25. Per capita annual disposable income of urban households. RMB



Source: Bloomberg

But the figures do not stop here. Going back to Gertz and Kharas, “by 2021 there could be more than 2 billion Asians in middle class households. In China alone, there could be over 670 million middle class consumers, compared with the 150 million today”²⁹.

7.2. Other variables to consider: an aging population and the real estate market

The situation of the labour market begins to be a source of concern for the authorities, since it is feared that the decline in the supply of labour, due to structural reasons, will cause a rapid increase in wages that limits the economy competitiveness. As a result, issues such as the retirement age or the flexibility of the "one-child" policy have recently been opened to public debate.

Currently, the retirement age is established between 50 and 55 years for women and 60 years for men. According to the latest ICEX country report³⁰, 170 million

²⁹ GEOFFREY G.; HOMI K. *The new global middle class: a cross over from west to east*. Wolfensohn Center for Development, Brookings, 2010.

³⁰ ICEX, *Country Guide: China*. www.icex.es. May 2012.

people exceed this age, which represents 12.8% of the population. Chinese people are aging and that is a fact to be taken into account for many aspects: in terms of labour, in terms of market needs, market size, consumption habits, future trends and a long etcetera.

On the other hand, some studies indicate that the "one-child" policy has prevented 400 million of births since its implementation 30 years ago. These discussions are developed in parallel with a changing economic model and the recognized need of the Government to increase wages. In the long term, the Government expects that the Chinese economy raises several steps in the value chain and becomes less intensive in labour, in order to rebalance the labour market. The big doubt is if this path can be taken progressively and maintaining social stability.

Regarding the real estate market, a year ago, in 2010, public measurements began to be implemented to limit speculation, cut the demand for housing and reduce the medium and long term risks to the financial sector. In the cities of Shanghai and Chongqing a new tax on the purchase of a second home has been implemented. The new tax levies between 0.4 and 1.2 on the price of the purchase of second homes whose value is higher than the average market price. Another measure to prevent speculation has been the increase in the down payment requirement for a mortgage: it used to be a minimum of 50% of the total cost of the housing and it has been increased to 60%.

Beijing has limited access to purchasing a second home by residents and a first home by non-residents, measures that are considered even more restrictive than those implemented in Shanghai and Chongqing. In general, this type of restrictive initiatives in the housing market is being implemented in the majority of first, second and third tier cities. At the same time, the Government has established an objective to build 10 million subsidized flats during 2011, an increase of 74% compared to 2010.

As a conclusion, the latest data confirm that the price of housing continues to rise, but it does so at a slower rate than before the adoption of the measures explained above.

8. Towards the future: China's some important challenges

China's weight in the global economy is so strong that the world's attention is constantly watching it. In fact, "no previous industrial revolution has been so widely watched"³¹. Its rapid development has caused some long-term problems that are a challenge for the Chinese Government, and that should be tackled before long.

These challenges could be the object of a study on its own. We will only outline very briefly the main ones that pose a bigger threat on the Chinese authorities:

³¹ THE ECONOMIST. *How strong is China's economy?* May 26th 2012 (p.13).

8.1. Social inequality

China's economic model is unfair on its people. For instance, the system denies equal access to public services for rural migrants, who work in the cities but are registered in the villages. Following the article we have just mentioned, "arbitrary land laws allow local governments to cheat farmers, by underpaying them for the agricultural plots they buy off them for development. And many of the proceeds end up in the pockets of officials".

Rural health care is another example of unfairness: one family doctor for every 22,000 people. If ordinary Chinese knew that their health would be looked after in their old age, they would save more and spend more. Household consumption accounts for little more than a third of the economy.

Unequal distribution of the income will result in increasing social tension and contradictions. Also migratory movements will accentuate the conflict: "The movement of some 200 million farmers (and their 200–300 million dependents) to cities over the next two decades will create tremendous social pressures unless the Chinese government provides them with greater rights and an effective social safety net."³²

8.2. Corruption

China suffers from widespread corruption. For 2010, China was ranked 78 of 179 countries in Transparency International's Corruption Perceptions Index, ranking slightly above fellow BRIC nations India and Russia, but below Brazil and most developed countries. It is nearly impossible to conduct significant business in China without participating in corruption.

In 2009, according to internal Party reports, there were 106,000 officials found guilty of corruption, an increase of 2.5 percent on the previous year. The number of officials caught embezzling more than one million Yuan (US\$146,000) went up by 19% over the year. With no independent oversight like NGOs or free media, corruption has flourished.

These efforts are punctuated by an occasional harsh prison term for major offenders, or even executions. But rules and values for business and bureaucratic conduct are in flux, sometimes contradictory, and "deeply politicized." In many countries systematic anti-corruption measures include independent trade and professional associations, which help limit corruption by promulgating codes of ethics and imposing quick penalties, watchdog groups like NGOs, and a free media. In China, these measures do not exist as a result of the CCP's means of rule.

³² PERKINS, D. *The Challenges of China's growth*. American Enterprise Institute for Public Policy Research (AEI). Feb. 2007.

“Money-worship, irresponsibility and corruption have spread to all strata of society. Scandals have implicated local Party leaders in numerous cases, such as the illegal sale of blood in Henan and the use of slave labour in Shaanxi brick kilns with protection from local authorities”³³.

8.3. Environmental problems

Although progress has been made in some areas, China is struggling to harmonize economic development and environmental protection. As a result of the fast economic growth, some fundamental dilemmas are arising. The gross domestic product is continuously increasing, but the natural resources on which the economic development relies have been heavily exploited or even overexploited. This leads to acute environmental problems and a tenuous relationship between humans and nature. One of the fields where problems are more severe and related to water: water shortage and pollution:

China is one of the 13 countries in the world with the most limited water resources. The available per capita volume of water is ~2200 m³, only 25% of the world average. In addition, water resources are distributed unevenly in China. About 44% of the population lives in the north but has access to only ~15% of the water resources. More than 60% of the 669 cities (of population >0.1 million) in China have problems with water shortages, and the situation in 110 of those cities is categorized as serious. In addition, more than 24 million rural people have insufficient drinking-water supplies.³⁴

The “bicycle kingdom” is being replaced by cars, with the resulting problems of traffic jams and pollution. There is a popular sentence that says “I’d rather cry in the back of your BMW than laugh on the back of your bicycle”, which shows that people in the cities want to leave behind poverty, underdevelopment and all that resembles the rural China. This is quite the opposite of the trend we see in developed countries, where the use of bicycle is on the increase and where local authorities are trying to promote its use.

Natural resources are being depleted. Growth is unsustainable: “Rapid urbanization has taken place in China ever since the economic development and socioeconomic changes of the 1980s. Approximately 40% of the population now lives in cities, compared with ~20% in 1980. The current annual urbanization rate is 1%, which means that 13 million people move into cities every year.”³⁵

³³ ALLÈS, E. *Class struggles in China today: towards a third Chinese Revolution?* Article from CHINA PERSPECTIVES. *Special Feature China’s WTO Decade*. (p. 3-4).

³⁴ FU B. J. AND OTHER AUTHORS. *Environmental problems and challenges in China*. Chinese Academy of Sciences. *Environmental Science & Technology*. November 2007.

³⁵ FU B. J. AND OTHER AUTHORS. *Op. cit.*

Rapid urbanization has created huge pressure on the maintenance of agriculture. To achieve a higher production rate from the remaining smaller arable lands, China has become the largest user of fertilizers and second of pesticides.

Domestic waste, air pollution, acid rain, ecological degradation are just a few of the subjects combined in a multi-faceted environmental problem. The impacts include damage to human health, social conflicts and economic losses. Strategically, China is trying to establish an integrative decision-making mechanism for harmonizing the environment and economic development. The country is changing its mode of economic development and is trying to promote a sustainable economy that includes resource recycling. This provides a favourable socio-political environment for making policies and laws that are oriented toward sustainable development.

8.4. Real Estate bubble

Examples of waste are abundant, such as the ghost city of Ordos, in China's northern part, to decadent resorts on its southern shores. Some reports suggest that middle-class bankruptcies will expand dramatically: "buyers have aggressively bought multiple properties with every penny of free cash flow. All that is needed for a wave of bankruptcies is further interest rate rises (targeting inflation) that result in a blip down in house prices just as mortgage payments rise". This has happened already in many major cities in Asia. It would seem that government leaders are totally out of touch with the true cost of urban housing.

Restrictions to buy second homes are going to stop speculation. Also increasing interest rates will contribute to lessen the demand for housing.

However, China's banks are highly liquid. Their deposits are higher than their loans and they keep a fifth of their deposits in reserve at the central bank. That gives the banks enough scope to handle potential troublesome loans. In fact, China's saving rate at 51% is one of the world's highest.

8.5. Financial system- Banking System

According to the Institute of Policy Studies of the World Bank, the Chinese financial system is underdeveloped and in urgent need of a structural reform: "the underdevelopment of the domestic financial system may help explain the high rates of both savings and investment in China³⁶". It adds that a better financial system could stimulate consumption (by providing more credit to families and businesses) and reduce the need for maintaining high savings levels (either for precautionary motives or to finance future consumption).

³⁶ WINTERS L. A.; YUSUF, S. *Dancing with giants*. Institute of Policy Studies, PPS. The World Bank. Washington DC, 2007 (p. 117).

Savers are starting to be tired of the miserable returns on their deposits and demand alternatives: according to *The Economist* (26th May 2012) “some are also finding ways to take their money out of the country, contributing to unusual downward pressure on the currency. China’s bank deposits grew at their slowest rate on record in the year to April (2012)”.

The reform of the Chinese banking system has progressed favourably since 2002, supported by capital injections, tax exemptions, introduction of foreign funds and other key government policy changes. The major Chinese commercial banks have improved their capital and asset structures remarkably: in fact, four of the five biggest commercial banks have changed their ownership structure and have successfully been listed on stock exchanges. Medium-sized nationwide commercial banks have also developed their business aggressively, although a few of them are still facing serious deterioration in their balance sheets. “However, these changes do not mean that the business foundation of Chinese banks has become completely stable. Compared to the world’s leading banks, major Chinese commercial banks are still very weak in terms of asset quality, business profitability, and the diversification of their services. More broadly, the Chinese banking system is not yet functioning as an efficient financial intermediary due to the banks’ own weaknesses and to environmental problems such as the loose credit culture and widespread disregard for the rule of law”³⁷.

There is a problem of credit risk management: risk in China has not been valued historically as in the western financial organizations. As the system tries to incorporate risk management, an obstacle is found: there is not enough historical data to perform an accurate assessment. In addition, banks find themselves in a transition period towards price formation of financial assets. It is the Central Bank who fixes the prices nowadays. In the future, as the market gets liberalized, commercial banks should have to learn how to price their products.

Although China’s somewhat repressed banking system is inefficient, it is also resilient because most of its vast pool of depositors have nowhere else to go. So far, there is not a serious fear that the Chinese banking system will fall into serious panic in the near future. According to Zhang Jiuquin³⁸, researcher at the International Trade Academy in the Commerce Ministry of China, Chinese institutions are still limited in their size, relatively weak in their capacity to foresee market risks and have mostly an obsolete mentality. Regarding their employees, he considers they do not have yet the required professional level, legal consciousness, skills, or experience compared to staff in more developed countries.

Therefore, in his opinion, the financial sector in China requires some deep reforms and more openness. “In the future, the Chinese Government will need to continue

³⁷ OKAZAKI, K. *Banking system reform in China. The challenges of moving toward a market-oriented economy*. Rand Corporation. www.rand.org/pubs. December 2011.

³⁸ ZHANG J. *La situación del sector financiero en China: balances y perspectivas*. Magazine CHINA HOY. *10 años de China en la OMC. Balance para el país y para el mundo*. Vol. LII num. 12 diciembre 2011. (p. 25-28).

adopting flexible and innovating systems to learn from how direct investment is being done abroad (...) The key to evaluate the reform and the financial development resides in the quality of the service that it supplies to the economy in general. To develop, the financial sector must not just think of itself, but must have a global vision. This is the main lesson to be learned after the financial crisis of 2008”.

8.6. Inefficiency

China’s fast growth has been possible thanks to shifts of workers from low productivity agriculture to industry. But maintaining economic growth will be difficult with the drag of inefficient state-owned enterprises (SOEs), which benefit from implicit subsidies, sheltered markets and politically encouraged loans. China is going to have to learn how to use its capital more wisely. While agriculture is organized in a fragile structure, industry presents an irrational one.

According to C.H. Dahlman³⁹, China will have to build solid foundations for a knowledge-based economy and it “must raise the technological level of the economy by:

- diffusing new technologies actively throughout the country;
- improving the research and development system;
- exploiting global knowledge”.

The country's sustainable agricultural development has encountered many obstacles. These include, as already mentioned above, agricultural water-use shortage; cultivated land loss; inappropriate usage of fertilizers and pesticides and environmental degradation.

Finally, the composition of the energy mix is highly inefficient in China. The amount of energy required to obtain their production is far too high, compared to developed countries. In the long run, if it is not optimized, this will cause a loss of competitiveness.

8.7. Labour Market

The decreasing labour market is becoming a source of worry for the authorities: with less people willing to work, salaries will continue to grow, diminishing competitiveness to the Chinese economy. There is a starting debate concerning retirement age to retard it (nowadays the retirement age is between 50 and 55 for women and 60 for men). Also there is an increasing debate to make the one-child-policy more flexible. All these measures would be trying to incorporate more workers into the labour market so as to stop salaries to increase so much.

³⁹ DAHLMAN, C. H.; AUBERT J.E. *China and the knowledge economy. Seizing the 21st century*. WBI Development Studies. World Bank Institute. Washington, 2002.

Only a few years ago, in 2003, the IMF had as a main concern to absorb the surplus labour:

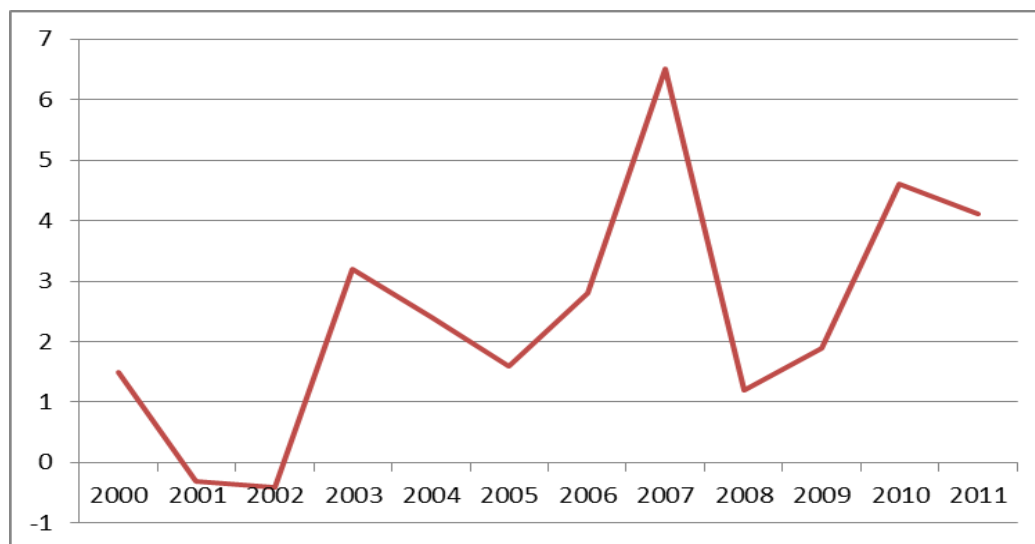
A more market-oriented labour market has emerged in China in the past twenty years with growing importance of the urban private sector, as state-owned enterprises have downsized. Despite the progress on reforms, a sizable surplus of labour still exists in the rural sector and state-owned enterprises. The main challenge facing China's labour market in coming years is to absorb the surplus labour into quality jobs while adjusting to World Trade Organization (WTO) accession⁴⁰.

Nowadays the worry is exactly the opposite: the labour market is decreasing alarmingly. Policy should focus on encouraging private sector development while reducing barriers to labour mobility, improving worker skills, upgrading job search services, and strengthening the social safety net.

8.8. Inflation

With a heated economy, inflation poses a major risk. In 2011 there was a deep concern about the inflation menace, but one year later there are symptoms of it being controlled by the government. Efforts have been made to control this inflation, with a considerable success. If we analyse the figures (see graph below) it is quite clear that after the 2007 sharp increase up to 6.5%, in the last two years, even if still above 4%, it is being kept under control.

Figure 26. Inflation rate in China, 2000-2011. In %



Source: Bloomberg. June 2012.

⁴⁰ BROOKS, R.; TAO, R. *China's labor market Performance and challenges*. IMF Working Paper. Nov. 2003.

However, one of the major problems is the inflation in food prices, lately over 13%. With the agriculture being so inefficient and infrastructure somewhat precarious, often agricultural products cannot get to market.

According to McKinsey Quarterly report:⁴¹ “the food supply chain, running at the limit, is close to breaking, and the pressures this problem creates will lead to further food quality crises (...). A major second – or third-tier Chinese city will see demonstrations over food price rises”. The concern is that these protests are copied and transferred elsewhere in the country.

8.9. *Social unrest*

In the past few years, the People’s Republic of China has experienced rising social unrest, including protests, demonstrations, picketing, and group petitioning. Disturbances have grown by nearly 50% in the past years (figures refer to 58,000 incidents in 2003 to 87,000 in 2005). Although political observers have described social unrest among farmers and workers since the early 1990s, recent protest activities have been broader in scope, larger in average size, greater in frequency, and more impulsive than those of a decade ago. Fears of greater unrest have triggered debates with the Communist Party leadership about the pace of economic reforms and the proper way to respond to protesters. The report on China’s social unrest of the Cornell University states:

Growing disparities of income, official corruption, and the lack of democratic institutions are likely to continue to fuel social unrest. The potential for widespread social upheaval has captured the keen attention of the Communist Party leadership. However, in the medium term, the PRC government is likely to be able to contain protests through policies that mix accommodation and violence and that promote continued economic growth. Most analysts do not expect social unrest to evolve into a national political movement unless linkages among disaffected groups strengthen and other social groups, particularly the middle class, intellectuals, and students, join the protests as well.⁴²

According to this report, the most active protest groups are:

- In the first place, the farmers, due to increasing unemployment, rising taxes, stagnant income, land confiscation caused by local project development, declining social services and environmental degradation;
- In the second place, workers in SOEs, protesting against layoffs, unpaid wages, low pensions, government corruption and the arrest of labour

⁴¹ ORR, G. McKinsey Quarterly. *What might happen in China this year?* McKinsey & Company. January 2011.

⁴² LUM, T. Specialist in Asian Affairs. *Social unrest in China*. p. 4. Congressional Research Service (CRS) Report for China. Cornell University, ILR School. May 2006 (p.4).

activists. These protests are considered more “dangerous” since the protesters are more educated, they have access to social networks, other activists, intellectuals and the media so they can replicate the protests in an easier way;

- In the third place, workers in Special Economic Zones (SEZ). Until recent years, workers in China’s light or labour intensive industrial sector, located in the coastal Special Economic Zones, generally avoided labour activism. Mostly young, female migrants from poor rural areas, these workers possessed a strong desire to earn money to send home and little understanding of labour rights, and were reluctant to complain despite enduring appallingly abusive conditions. Many factories in the SEZs are owned and managed by investors from Hong Kong, Taiwan, and South Korea, who supply U.S. retailers and brands. However, lately, these workers feel stronger to protest for higher pay and unpaid wages;
- Finally, homeowners: a relatively recent social phenomenon in China is the rise of protests involving home owners and peasants opposing eviction or the loss of farmland due to urban renewal, industrialization, and other problems related to economic development: “Many aggrieved citizens have claimed that they were not sufficiently consulted or properly compensated and have engaged in public demonstrations when their complaints were ignored by local officials. Guangzhou police estimated that in 2003 and 2004, forcible evictions constituted nearly one-fourth of protest activities in the city — becoming the largest source of social unrest”.⁴³

8.10. Political issues

According to Prof. Simai⁴⁴, the main challenge for China is the political future, with two major worries:

1. How to cope with increasing inequalities and social tensions. Uprisings are possibly going to increase.
2. How to cope with the increasing power of regional centres. Two institutions keep the country together: the Communist Party and the army. However, these two are evolving and who knows how they will do so.

⁴³ LUM, T. Op. cit. p. 12.

⁴⁴ Economist. Professor at Corvinus University. Professor Simai is a member of the Hungarian Academy of Sciences. Currently he is working in the Institute for World Economics of the Hungarian Academy of Sciences as a Research Professor. He is also a Professor at Corvinus University in Budapest. He is the Honorary President of the World Federation of United Nations Associations.

He does not see likely a Chinese version of the Arab spring, because in these countries there was a large group of unemployed youth with no hope and no family support. In China there is employment for all so far, and the *social lift* works.

Who wants democracy in China? The middle class is pragmatic and therefore not interested. The rural class neither. Only the intellectuals are willing, and that is not enough to start a change process.

Researchers at UN detected certain conditions that need to be present for sustainable democracy:

- highly educated population who understand problems and cannot be easily manipulated;
- tolerant and enlightened political leaders;
- resilient and flexible institutions;
- a standard of living that creates an increasing *cake* that satisfies most people.

Out of these, Simai considers that China only fulfils the last one: the cake is big and growing enough. However, even that condition is doubtful since China gets affected by the world crisis: because of the demand crisis in the west plus an economy based mainly in exports, China has lost more than 14 million salaried employees, who have had to go back to their villages.

The direction in which the political power will go is still uncertain and will depend on two factors: first, if the economic development continues. Second, if it does, will the growth be integrative, will the economic development favor the majority of the population.

As long as the state can ensure economic growth, it retains the support of a large section of the middle class. Furthermore, to the extent that the leadership remains united and overcomes divergent interests, it will be able to control tensions in the country. However, revolutions cannot be always be foreseen. As Mao Zedong said, "a single spark can start a prairie fire".

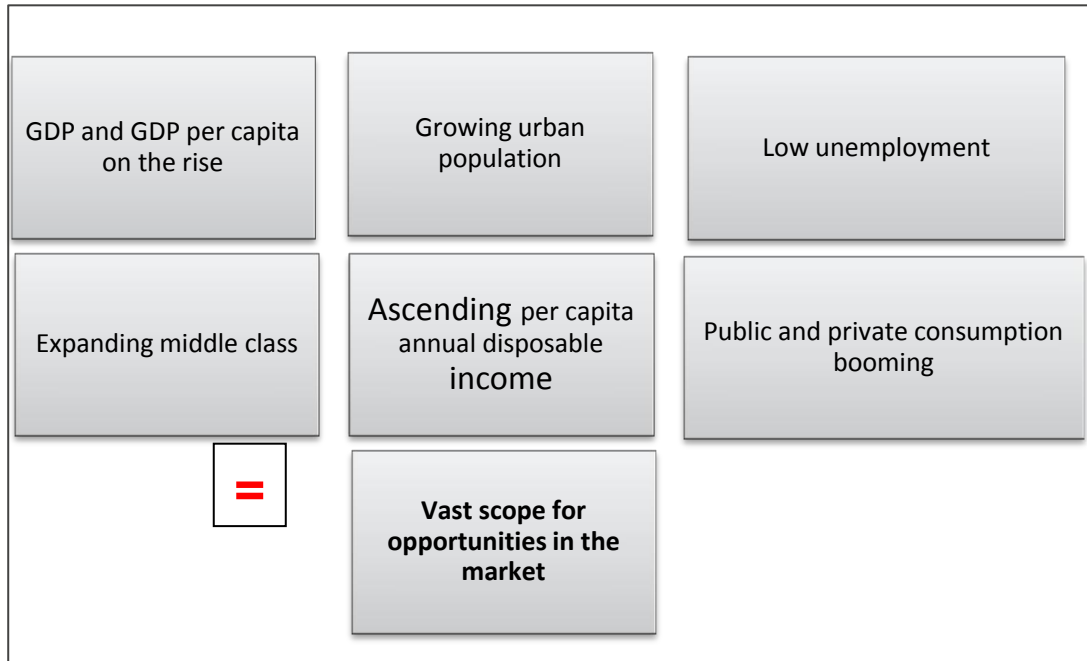
Municipal elections have taken place in China since 1978 and have been continued on a trial basis since then. Even if it is an incomplete system and it cannot be compared to western democracies, it may well be a start. The elections could be consolidating Communist rule, as CCP leaders may claim some legitimacy through these elections. At the same time, village elections are also preparing - perhaps - the way for a democratic transition. People are getting familiarized with democratic procedures and with representative institutions. All these developments suggest that the Chinese Communist Party is undergoing a significant transformation. We may be witnessing the beginning of a local-to-national model of democratization.

China's internal market as an attractive option

Following the various analyses carried out above, we can conclude that there are many factors combined that suggest a significant remarkable opportunity in terms of marketplace, as perhaps it has never been witnessed before. These factors include:

1. Chinese population is growing by 6-8 million people per year in absolute figures;
2. Moreover, the migration from rural to urban areas means that 400 more people will be living in cities by 2035 (therefore one billion in total): these are persons who will have access to the market, needs for products and services and this will represent, in turn, a vast potential growth;
3. GDP is growing an annual average of 10%, from 1991 till 2008. This growth is unprecedented and will mean the opening of many opportunities. Even if the growth has slowed down somehow, it is not expected to halt but to experiment a "soft landing";
4. GDP per capita is still low for western standards, but is also growing significantly, by more than 10% per year;
5. Population, especially urban population, is growing and people in the cities are working, unemployment remaining around 4%. Disposable income in urban areas has multiplied by sixteen times in the last 23 years. Retail sales are booming, and have experimented an annual growth of 11% on average in the last 22 years;
6. Although income inequality is still acute in China, there is a powerful emerging middle class. If today it is estimated to be just over 150 million people, their number is growing incessantly: while some experts estimate the number of persons considered middle class will be 243 million people by 2012, others sustain that it will reach 670 persons by 2021.

Figure 27. Summary of the attractiveness of the Chinese market



Source: own elaboration

III. CHINA'S FOREIGN TRADE

1. Accession to the World Trade Organisation

On 17th September 2001 China passed an important historical milestone, joining the World Trade Organization (WTO)⁴⁵, after more than 15 years of hard negotiations. The signature of such agreement confirmed the courageous decision taken by China's leaders to enter the country into a program of ambitious and systematic economic reforms. "The agreement signalled China's willingness to play by international trade rules and to bring its often opaque and cumbersome governmental apparatus into harmony with a world order that demands clarity and fairness".⁴⁶

As negotiations went on during the decade of 1990s, China accepted most points on tariffs and barriers, terms of market entry for corporations, inclusion of services in trade talks, trade laws and policies, etc. However it refused to give ground on agriculture: China wanted to have the freedom to subsidize farmers up to 10% of the value of production, right that should be given as a developing country. Without going into details that are not the subject of this work, this is one of the problems that caused the accession to take over 15 years of negotiations. The whole process of accession is explained in detail by Panitchpakdi and Clifford in the book mentioned below.

In theory, China's 15-year odyssey to join the world trade body shouldn't have taken so long. WTO accession is, in its simplest form, a two-step process. First, the applicant must negotiate bilateral concession agreements with each current WTO member that requests such agreement. These bilateral agreements are then used as the basis to write an overall accession agreement that is approved by the entire WTO membership, known as the General Council. In keeping with the fundamental free-trade principal that one country cannot be favoured over another, the most favourable offer made to one country must be offered to all as part of the accession agreement.

⁴⁵ WORLD TRADE ORGANIZATION (WTO). As defined by the organisation itself at www.wto.org, The World Trade Organization (WTO) provides a forum for negotiating agreements aimed at reducing obstacles to international trade and ensuring a level playing field for all, thus contributing to economic growth and development. The WTO also provides a legal and institutional framework for the implementation and monitoring of these agreements, as well as for settling disputes arising from their interpretation and application. Over the past 60 years, the WTO, which was established in 1995, and its predecessor agreement the GATT (General Agreement on Trade and Tariffs) have helped to create a strong and prosperous international trading system, thereby contributing to unprecedented global economic growth. The WTO currently has 153 members, of which 117 are developing countries. January 2012.

⁴⁶ PANITCHPAKDI, S.; CLIFFORD M. L. *China and the WTO. Changing China, changing world trade*. John Wiley & Sons. Singapore, 2002.

The agreement was reached less than a week after the 11th September 2001 terrorist outrage in New York, a coincidence that caused it to go largely unnoticed by most of the world, too busy following the attacks. However, entry into the WTO is the most significant event for China, helping this country reclaim a place in the world that it had lost in the last two centuries. Ten years later, from 2001 to 2011, we can notice how accession to the WTO has helped to accelerate an economic revolution: the economy has opened to domestic and foreign competitors, the GDP has multiplied by more than four and China has taken the second place among the world's largest economies.

The WTO set out the rules for a market-based economy. Basically, to name a few, the following have been the major challenges that China has had to face after the accession:

- thorough restructuring of the economy, by opening up protected sectors to domestic and foreign competition - from finance to agriculture. More specifically, the lowering of China's tariff barriers, which at the time were far exceeding those of existing former GATT members;
- eliminating unfair treatment that until 2001 favoured state-owned firms and discriminated against foreign companies and local entrepreneurs;
- reforming of the banking and financial system which had to adapt to a modern system after a legacy of years of poor decision-making;
- modifying the lack of convertibility of the China's currency, the yuan;
- important change in the culture affecting all economic actors, including of course the government, which has had to adapt to a more open and accountable system;
- last but not least, foreign trade and direct investment have developed, grown exponentially and changed the world situation in just ten years, as we will see in the next chapters.

In the last two decades of the 20th century, China longed for an important role of the international economics scene and tried to promote an image of modernization. Becoming a member of the WTO as we have seen above, or the celebration of the 2008 Olympic Games in Beijing, are clear examples. The domestic reforms continue to be the main challenge. Reforms have been very positive in macroeconomic terms and it is true that a significant proportion of the population has benefited from increasing prosperity. But there are still reforms pending and new pressures emerging.

When we refer to China's reforms, it is necessary to go back to their launching in 1978, as well as the changes introduced since then by Deng Xiaoping and his successor Jiang Zemin. Although reforms have been evolving for more than twenty years, the country is still undergoing a period

of transition. The three decades of Maoism have been such a heavy burden for China that the country still needs a few more years in order to overcome that legacy in the economic, social and political spheres. [...] From an economic perspective, China is currently undertaking a whole set of domestic reforms, while adapting its economy to international pressures.⁴⁷

A retreat-retain strategy

There is no doubt that in the last twenty years, the state has retreated at least partially from administering and owning the means of production. The government wants to improve the performance of the industrial sector, which will in turn generate employment and boost fiscal revenues. The Government of the People's Republic of China (PRC) is retreating from competitive sectors where private businesses are already active, barriers to market entry are low and the performance of state firms is poor. These sectors include: textiles, chemicals, building materials, machinery, transport or commerce, to name a few.

However, at the same time, in state monopolies or in strategic industries, where larger firms are common, the government is not allowing privatization. There was a principle introduced in the 1990s called "grasp the big; let go of the small" that is still guiding the state policy. Sectors where decision making is retained by the state are basically large firms operating in energy, telecommunications, infrastructures, financial services and defence.

As explained by Stephen Green and Guy S. Liu in their book "Exit the dragon?"⁴⁸, the Chinese government is enforcing a double strategy: free certain competitive sectors while retaining the strategic ones: "In short, even though privatization is undoubtedly occurring, so are attempts to strengthen the state's grip on large and strategic parts of industry. The PRC government appears to have developed a retreat/retain (2-R) strategy. On the one hand, it is retreating from competitive sectors. [...] At the same time, in natural monopolies and so-called strategic industries, control is not yet generally up for sale".

As a conclusion, we can state that China has engaged with the global economy in the last three decades, mostly since the 80s. There has been, and is still on-going, a progressive marketisation in a twofold manner: first, of the production systems and, second, of the distribution of products and services. "Increasingly, markets are being used to allocate labour and to reward that labour. The development of markets reflects a twin process – of the replacement of subsistence production by production for markets and of the replacement of state-directed production by market-directed production"⁴⁹. Although these changes have occurred in China over the past 50

⁴⁷ FISAC, T; FERNÁNDEZ-STEMBRIDGE, L. *China today. Economic reforms, social cohesion and collective identities*. Routledge Curzon, Taylor & Francis Group. London 2003.

⁴⁸ GREEN, S.; LIU, S. G. *Exit the dragon? Privatization and State Control in China*. Blackwell Publishing. The Royal Institute of International Affairs. London, 2005.

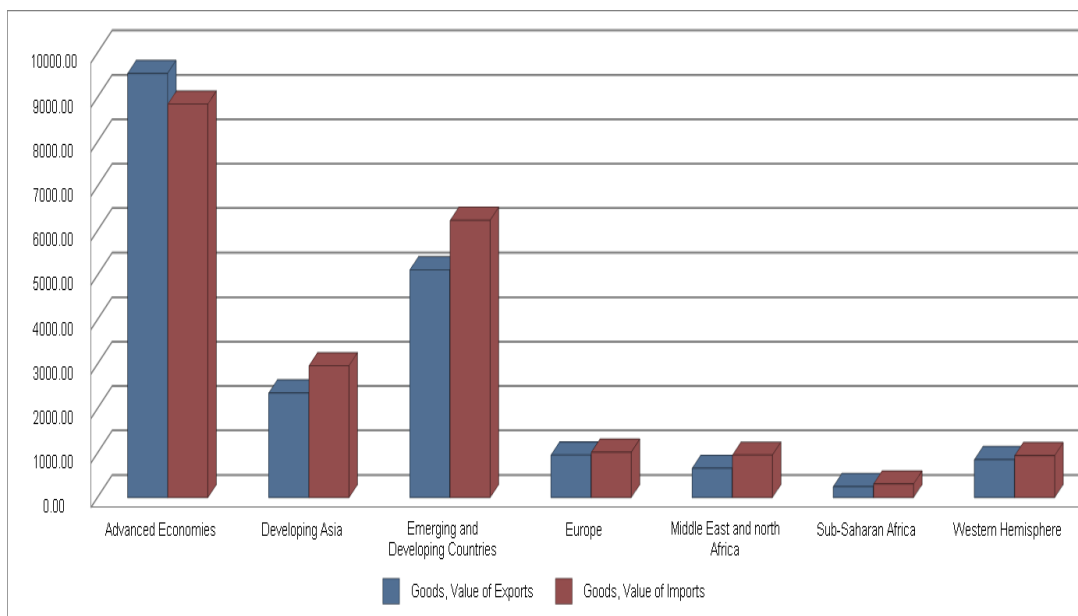
years, globalisation has increased the pace of the evolution in the 80s and 90s. With the access to the WTO in 2001, globalisation has totally restructured the market of production and distribution.

2. China, leader in world trade

After the analysis of variables such as population, GDP, employment or consumption expenditure, we are going to narrow down our look into another aspect that actually focuses more closely on the market opportunities: foreign trade. In the next pages we will take a close look at the Chinese imports and exports and their evolution. We will focus on the bilateral trade relations between China and the world, China and the EU and, finally, China and Spain. This analysis will help us to understand who are China's main partners and what kind of goods are being traded. However, as such, trade relations are not the chief objective of our document. What will be found here is a summarised review of Chinese commerce. It is not our intention to compile an exhaustive study thereof, which could be the object of another investigation⁵⁰.

China is the world's largest exporter, overtaking Germany from 2009 onwards, accounting for more than 13% of world's exports. Both its imports and exports as a percentage of the world total are ascending. In terms of absolute numbers, Chinese bilateral trade went from €4 billion in 1978 to over €300 billion in 2011.

Figure 28. Regional distribution of world exports and imports of goods, 2012. In Billions of US\$



Source: IMF. DOTS. June 2012.

⁴⁹ WEBBER, M; WANG, M; YING, Z. *China's transition to a global economy*. Palgrave MacMillan. New York, 2002.

⁵⁰ Many sources document the trade relations of China with the world. China's Customs Statistics, The OECD, The International Monetary Fund (IMF), The Asian Development Bank (ADB), Eurostat, or The US-China Business Council (USCBC), to name a few.

The table below shows the evolution of the share of trade of goods by main world traders, in particular, the share of national imports in world imports. The most remarkable trend is that developed countries such as the EU, the United States, Canada and Japan, all decreased their weight in the world imports. These four main partners accounted for 58.5% of total world imports in 1999. By 2010 that percentage had already fallen to 43%. In the meantime, China's weight in the world imports had multiplied by three: from accounting for just 4% of the world imports to 12% of them by 2010. This figure shows the importing growing power of an emerging market that eclipses the old established western world.

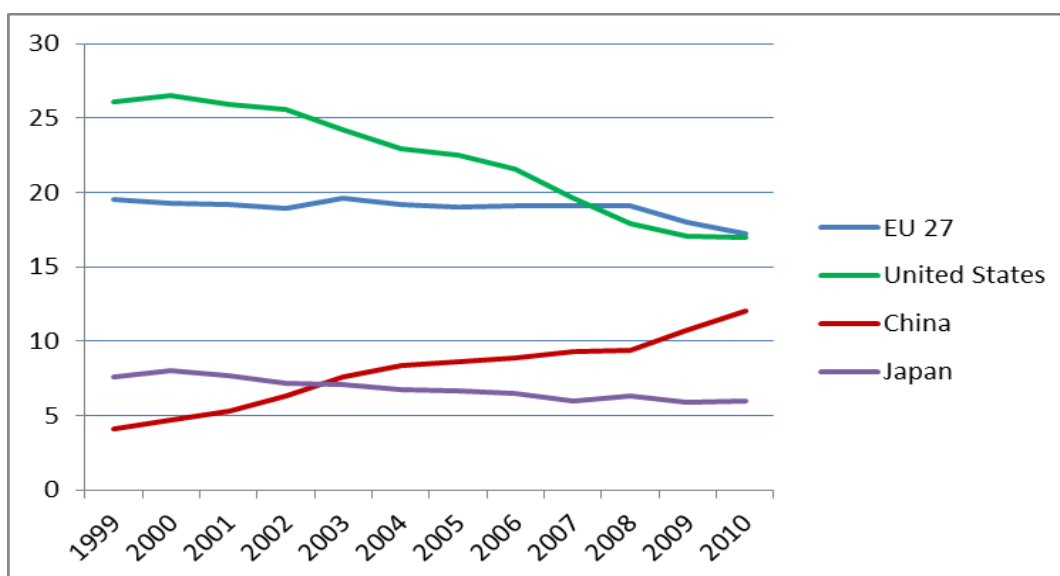
Table 12. Share of national imports in world imports (%). Evolution 1999-2010

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
EU 27	19.5	19.3	19.2	18.9	19.6	19.2	19	19.1	19.1	19.1	18	17.2
Canada	5.3	5.1	4.9	4.7	4.4	4.1	4.1	3.9	3.7	3.4	3.4	3.4
United States	26.1	26.5	25.9	25.6	24.2	22.9	22.5	21.6	19.6	17.9	17.1	17
China	4.1	4.7	5.3	6.3	7.6	8.4	8.6	8.9	9.3	9.4	10.8	12
Japan	7.6	8	7.7	7.2	7.1	6.8	6.7	6.5	6	6.3	5.9	6

Source: Eurostat.

The same conclusion can be reached from the figure below. The economic powerhouses of the 20th Century (namely the USA and Europe) are forced to give way to an ascending emerging market, China, who needs to buy from all over the world in order to feed its industries.

Figure 29. Evolution of the share of national imports in world imports. Main world traders. In %

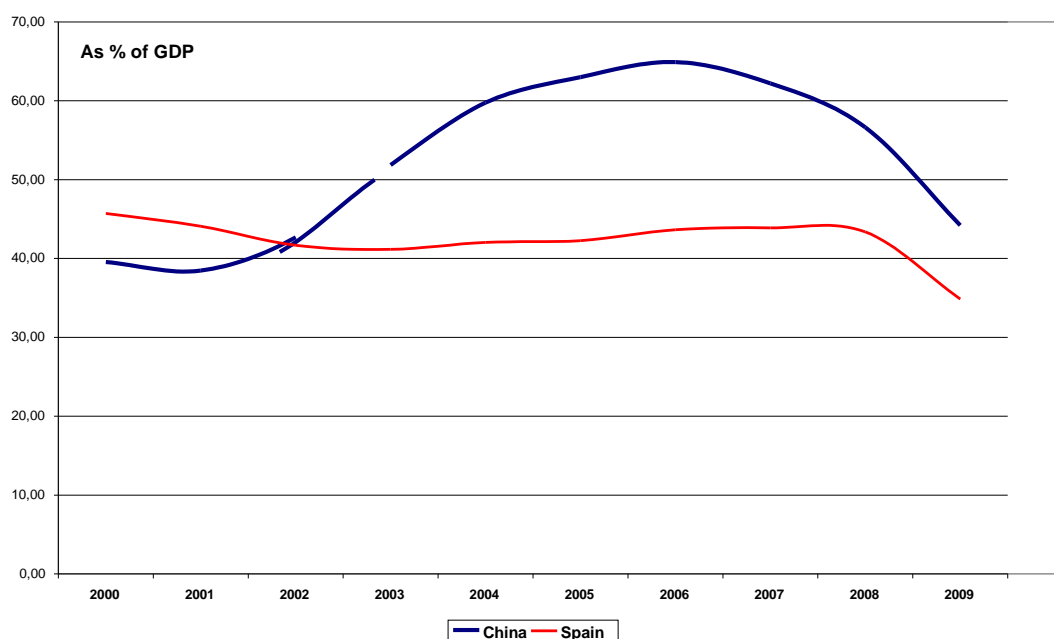


Source: Eurostat

China's imports represent 18.3% of the GDP, while exports represent a much higher 23.6%. The Chinese economy is based largely in the high weight of their exports, a truly engine of their GDP growth. On the whole, Chinese trade openness, ie. its trade as a percentage of its GDP (that shows to which extent the economies are integrated), is 42% (IMF data).

A percentage of 42% shows quiet an integrated economy⁵¹ but not as high as the new threshold of 45%, that would be considered a strictly high international economic integration. According to data from the External Trade Institute of Spain (ICEX) the Spanish trade openness rate is 43.9%⁵², almost two points above that of China. Although China's trade has been affected by the world recession, its impact has been considerably lower than for most countries in the WTO.

Figure 30. Evolution of trade openness for China and Spain, 2000-2009. In %



Source: IMF, DOTS & WEO Databases and own calculations. Trade openness as trade-to-GDP ratio (exports + imports) /GDP

⁵¹ APOTEKER, T.; CROZET, E. *Davos versus Porto Alegre. A survey on key issues behind international trade and financial integration and liberalisation*. To consider the issues of trade openness and financial liberalisation it can be useful to look at how analysts measure them. The ratio of world exports (or world trade, i.e. exports and imports) to world GDP is used to see to what extent the economies are integrated. Any increase in this ratio denotes a state of higher international economic integration. During the past thirty years (1970-2000), this measure has increased significantly, from slightly above 25% to above 45%.

⁵² ICEX. *China. Informe Económico y Comercial*. May 2010.

Wei sustains that over the last two decades, overall inequality in China has risen together with an increase in trade openness. Following this reason, someone would be tempted to conclude that the greater openness is somehow responsible for the greater inequality. “Yet, this conclusion is incorrect as the evolution of inequality is influenced by many factors in addition to openness. Within China, regions that have experienced a faster increase in openness have also experienced a faster reduction, rather than an increase, in inequality. So embracing trade openness has in fact created opportunities for poor people in rural areas not only to grow, but to grow at a faster pace than their relatively more fortunate urban neighbours.”⁵³.

The table below shows the volume and evolution of China’s trade with the world. Both the volume of exports and imports has increased by impressive amounts, as high as 37% in one year. In one recent occasion, however, in 2009, data showed the opposite trend, with a drop of 16% in the exports and 11% in the imports: this exception shows the adjustments that happened due to the economic recession affecting most of the world and definitely the western countries.

In any case, the trade balance has always been favourable to China in the period 2002-11, especially from 2005 onwards.

Table 13. China's Trade with the World, 2002-11 (Million US\$)

	Exports	% Variation Exports	Imports	% Variation Imports	Trade Balance
2002	325,783.11	-	295,440.00	-	30,343.12
2003	438,485.69	34.59	412,836.77	39.74	25,648.92
2004	593,769.76	35.41	560,811.29	35.84	32,958.47
2005	762,647.53	28.44	660,224.37	17.73	102,423.17
2006	969,698.50	27.15	791,794.57	19.93	177,903.93
2007	1,218,696.60	25.68	956,263.83	20.77	262,432.77
2008	1,429,337.98	17.28	1,131,917.50	18.37	297,420.49
2009	1,203,418.83	-15.81	1,003,908.85	-11.31	199,509.98
2010	1,580,397.43	31.33	1,393,918.99	38.85	186,478.44
2011	1,901,478.21	20.32	1,741,449.39	24.93	160,028.82

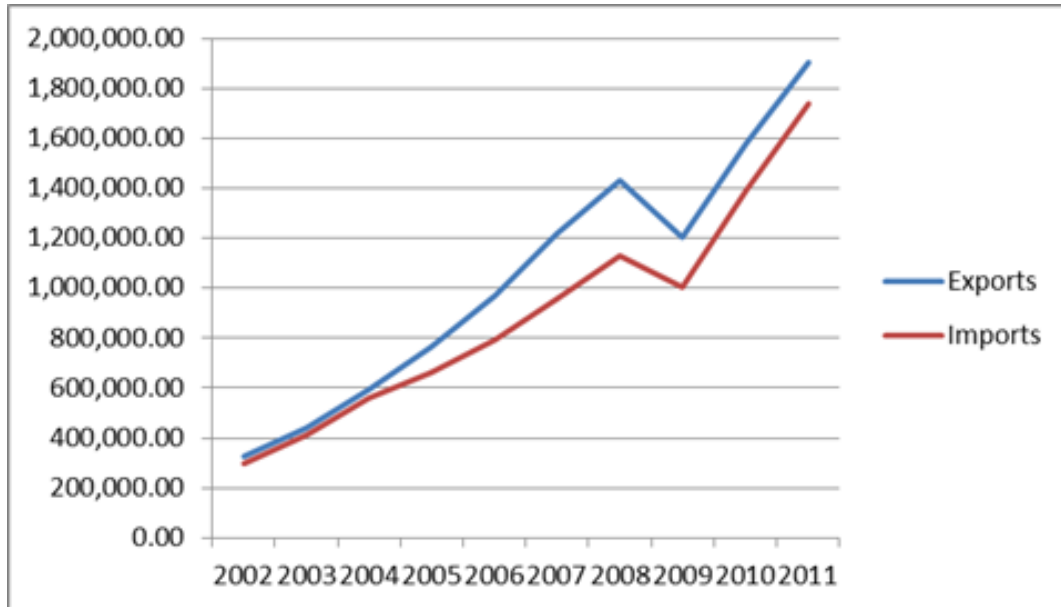
Source: IMF. DOTS Database. Extracted June 2012.

The graph below shows the same situation, by means of a graph: as we can see, Chinese foreign trade has grown formidably since its access to the WTO. Trade follows a cyclical pattern, along with the behaviour of the general economy. Annual growth of exports and imports has been around 20%. There has only been one exception, the year 2009, when exports dropped by 16% and imports dropped by 11%. But this fall only lasted one year, recovering immediately by 2010 with increases over 30%. This shows that the general recession suffered in the western

⁵³ WEI, S. J. *China as a window to the world : trade openness , living standards and income inequality*. Reserve Bank of Australia, 2002. www.rba.gov.au/publications. June 2011.

world in general and in Spain in particular, has not affected in the least the Asian giant's trade.

Figure 31. Foreign trade of goods: China with the world. Evolution 2002-2011. In millions of US\$



Source: IMF, DOTS Database. Extracted June 2012.

We can subsequently focus on China's top world trade partners. They can be divided into two main groups: firstly, western most developed countries, such as the United States or the European Union, that export but mostly import from China. Secondly, countries in the same region as China, such as Japan, South Korea or Malaysia, that import but mostly export to China. This is due to what it is often called a *fragmented value chain*.

The fragmentation of the production process is a major research theme in international economics, business, geography and sociology. Production fragmentation is related to the growth of international trade and intermediate product exchanges and it is directly connected to the increasing integration of global commerce. Trade benefits now arise because of the entry of new countries bearing low labour costs, and this allows for firms to decrease—often to a surprising degree—their total production costs.

Global firms view the world as a pool of resources, and from this perspective, they can take whatever they need from the most favourable location in each case: access raw materials from a country, access labour from another, find certain components from a third country, to finally sell in a market elsewhere. "The 'slicing up' of the whole (or aggregate) value chain represents a major change in the new post-Fordist paradigm of production, and is largely discussed by researchers specializing in international business studies. These trends, which are closely related to

outsourcing, have enriched the theoretical perspective on the study of the global firm".⁵⁴

The globalization of business is, on the one hand, a modality through which multinational corporations organize the location of their activity, but, on the second hand, it is also the result of a multilevel strategy of configuration of internal and external activities. These are coordinated in various localities and through diverse alliances, through outsourcing and off-shoring. In this sense, the Asian region comprising China, Taiwan, Hong Kong, South Korea and Malaysia is of special relevance.

Local production systems have emerged, following specific patterns of clustering which characterize the development of individual regions, countries and large economic areas. For example, in the experience of East Asian countries like Taiwan, Singapore and South Korea, the initial outsourcing of processes from large Western MNCs producing electronic products transferred technology and new capabilities to local firms. Thus, firms like the global Taiwanese computer manufacturer Acer emerged from this process as a success story.²³

China is at the heart of what is known as "Factory Asia", assembling parts and components imported from other economies in the region and exporting finished products. Asian production chains have developed rapidly over the last two decades. Production processes are highly fragmented and each country specializes in the phase of production for which it has a comparative advantage. The importance of regional chains is indicated by the high percentage accounted for by intermediate goods (parts and components) in the intraregional exports and imports of a number of the region's main economies:

The network of interconnected producers in Asia has grown quickly over time, even as its configuration has shifted. In 1985 there were just four participants, with Japan at the centre and Indonesia, Singapore and Malaysia around it. Around 1990, Japan extended its supply chain to other countries such as the Republic of Korea, Thailand and Taiwan Province of China. In the early 2000s, China became the second giant in the Asian production chain. This was contributed to by its entry into the World Trade Organization in 2001 and its strong production links with the Republic of Korea and Taiwan Province of China⁵⁵.

The report continues that from 2005, China is at the centre of the Asian production chain, pushing Japan into second place. China is now the main regional market for intermediate goods, which are used to produce the finished goods exported to the markets of the United States and European Union. According to a 2010 study, the

⁵⁴ BELUSSI, F.; SEDITA, S. *Managing the fragmented value chain of global business: exploitative and explorative offshoring towards emerging market economies*. University of Padova. Advances in International Management. Padova, 2010.

⁵⁵ ECLAC. *The People's Republic of China and Latin America and the Caribbean*. United Nations. 2012 (p. 20).

average import content of Chinese exports in 2008 was 37%, and it was as high as 56% in the case of products originating in export processing zones.

Table 14. China's Top Trade Partners, 2010 (US\$ billion)

Rank	Country/region	Volume	% change over 2009
1	United States	385.3	29.2
2	Japan	297.8	30.2
3	Hong Kong	230.6	31.8
4	South Korea	207.2	32.6
5	Taiwan	145.4	36.9
6	Germany	142.4	34.8
7	Australia	88.1	46.5
8	Malaysia	74.2	42.8
9	Brazil	62.5	47.5
10	India	61.8	-

Source: PRC General Administration of Customs, *China's Customs Statistics*

Chinese exports are concentrated towards the main developed countries in the western world, namely the United States and the largest EU Economies: Germany, The United Kingdom, Italy or The Netherlands. China does export to its neighbours in Asia, but these exports are focused namely to the most developed countries in the continent: Japan, South Korea and Singapore. These countries have similar purchasing patterns and the western world.

Table 15. China's Top Export Destinations, 2010 (US\$ billion)

Rank	Country/region	Volume	% change over 2009
1	United States	283.3	28.3
2	Hong Kong	218.3	31.3
3	Japan	121.1	23.7
4	South Korea	68.8	28.1
5	Germany	68.0	36.3
6	The Netherlands	49.7	35.5
7	India	40.9	38.0
8	United Kingdom	38.8	24.0
9	Singapore	32.3	7.6
10	Italy	31.1	53.8
21	SPAIN occupies position number 21 in the rank		

Source: PRC General Administration of Customs, *China's Customs Statistics*

However, it can be noted that concerning imports, China's top suppliers are not in the EU: only Germany is one of the main partners. China finds its main suppliers from the Asian region (following the explanation above about the fragmented value chain): Japan, South Korea, Taiwan, Malaysia etc.

Spain, country which should normally not be included on the list above, occupies ranking number 21, with 1.5% of the China's exports.

Table 16. China's Top Import Suppliers, 2010 (\$ billion)

Rank	Country/region	Volume	% change over 2009
1	Japan	176.7	35.0
2	South Korea	138.4	35.0
3	Taiwan	115.7	35.0
4	United States	102.0	31.7
5	Germany	74.3	33.4
6	Australia	60.9	54.1
7	Malaysia	50.4	55.9
8	Brazil	38.1	34.7
9	Thailand	33.2	33.3
10	Saudi Arabia	32.8	39.2
36	SPAIN occupies position number 36 in the rank		

Source: PRC General Administration of Customs, *China's Customs Statistics*

By product, China's top exports are, in the first place, a series of industrial goods such as equipment, electrical machinery, power generation, iron and steel and chemicals. These are followed by consumer goods where China has specialised and is a first world exporter: textiles, footwear, cars and other vehicles.

Table 17. China's Top Exports, 2010 (\$ billion)

Commodity description	Volume	% change over 2009
Electrical machinery and equipment	388.8	29.1
Power generation equipment	309.8	31.4
Apparel	121.1*	20.5*
Iron and steel	68.1*	44.1*
Optics and medical equipment	52.1	34.0
Furniture	50.6	30.0
Inorganic and organic chemicals	43.2*	34.9*
Ships and boats	40.3	42.1
Vehicles, excluding rail	38.4	37.5
Footwear	35.6	27.1

*Calculated by USCBC

Source: PRC General Administration of Customs, *China's Customs Statistics*

In terms of imports, the main variation compared to exports is the importance of raw materials. China is a top world consumer of unprocessed products, mostly since the enormous economic growth of the last decade. It needs to import enormous quantities of oil and fuels, ores, copper, iron and steel, etc. to supply the necessary raw materials to feed its industries and construction. Experts coincide in their

appreciation that there are two things China needs from the world: raw materials and technology. For the rest, they can manage by themselves. This represents a problem for most Spanish SMEs, not to be able to supply either of the Chinese two main needs. However, as we will see in the following chapters, Spanish firms can supply this technology in certain economic sectors, for instance, in renewable energies.

The table below lists the top imports, which, if analysed carefully, can be classified in one or the other.

Table 18. China's Top Imports, 2010 (\$ billion)

Commodity description	Volume	% change over 2009
Electrical machinery and equipment	314.4	29.0
Mineral fuel and oil	188.7	52.1
Power generation equipment	172.3	39.4
Ores, slag and ash	108.6	54.9
Optics and medical equipment	89.8	34.1
Plastics and articles thereof	63.7	31.3
Inorganic and organic chemicals	58.2*	37.2*
Vehicles, excluding rail	49.5	74.5
Copper and articles thereof	46.1	55.8
Iron and steel	34.5*	-6.1*

*Calculated by USCBC

Source: PRC General Administration of Customs, *China's Customs Statistics*

Summarising, China runs a trade surplus with the world's three major economic centres — the United States, the European Union, and Japan. The accession of China to the World Trade organization changed dramatically the world commerce, in many cases to provoke deep concern in countries like the US, where they saw this change as a threat to their world leading position:

As imports from the People's Republic of China (PRC) have surged in recent years, posing a threat to some U.S. industries and manufacturing employment, Congress has begun to focus on not only access to the Chinese market and intellectual property rights (IPO) protection, but also the mounting U.S. trade deficit with China as well as allegations that China is selling its products on the international market at below cost (dumping), engaging in "currency manipulation," and exploiting its workers for economic gain. Since 2000, the United States has incurred its largest bilateral trade deficit with China (\$201 billion in 2005, a 25% rise over 2004). In 2003, China replaced Mexico as the second largest source of imports for the United States. China's share of U.S. imports was 14.6% in 2005, although this proportion still falls short of Japan's 18% of the early 1990s. The United States is China's largest overseas market and second largest source of foreign direct investment on a cumulative basis. U.S. exports to China have been growing rapidly as well, although from a low base. In 2004, China

replaced Germany and the United Kingdom to become the fourth largest market for U.S. goods and remains the fastest growing major U.S. export market.⁵⁶

China has become a platform through which its Asian neighbours export to the developed countries. China has a trade deficit with some Asian countries (Republic of Korea or Japan), because these countries are China's main suppliers of capital goods and intermediate inputs for its manufacturing industry.

After manufacturing, China exports the finished goods to the EU and the USA, with which China has more favourable balances. This surplus is mainly in manufactures with low and high technology content. The table below shows China's composition of trade balances by technology intensity: low, medium and high technology, and natural resources. The deficit of China with the EU is mostly in medium technology and in natural resources.

Table 19. China's composition of trade balances with selected partners, by technology intensity, 2011. (Millions of US\$)

	Manufacturing balance					
	Overall Balance	Commodities Balance	Natural Resource based	Low-technology	Medium-technology	High-technology
Latin America and the Caribbean	-7,572	-221,282	-35,411	47,280	90,381	67,379
South America	-102,714	-212,178	-51,681	16,650	57,078	49,895
Mexico and Central America	83,026	-6,569	15,280	27,383	25,282	16,107
Caribbean	12,186	-2,535	991	3,247	8,022	1,376
Asia-Pacific	-569,482	-236,686	-124,749	144,469	-167,780	-2,249,098
ASEAN	-44,546	-79,471	-36,205	54,840	79,488	-113,960
Australia and New Zealand	-118,594	-195,980	-12,546	24,227	22,942	27,082
Republic of Korea	-237,112	15,725	-46,437	4,064	-82,525	-150,174
Japan	-169,230	23,042	-29,555	61,338	70,030	-71,045
United States	696,559	-61,872	2,637	257,263	41,130	299,953
European Union	556,872	6,496	-18,585	230,220	-77,832	301,298

Source: ECLAC. October 2012.

⁵⁶ LUM, T.; NANTO, D. *China's Trade with the United States and the World*. CRS Report to Congress. 2007 (p. 2-6).

As it was commented before referring to the fragmented value chain, China is importing heavily from its Asian trading partners — particularly precision machinery, electronic components, and raw materials for manufacturing. These are all materials that China uses to continue their production chain. As a result, China is running trade deficits with Taiwan and South Korea and has become a major buyer of goods from Japan and Southeast Asia.

What has represented a major change in terms of the meaning of what China is for the world is the evolution of the type of imports of China from the USA:

- If only ten years ago most of the US imports were in labour-intensive sectors;
- Nowadays they are in some of the most advanced technology sectors, such as office and data processing machines, telecommunications and sound equipment, electrical machinery and appliances.

China's exports to the United States are taking market share from other countries, particularly the East Asian newly industrialized countries (NICs), which have moved most of their low-end production facilities to China.

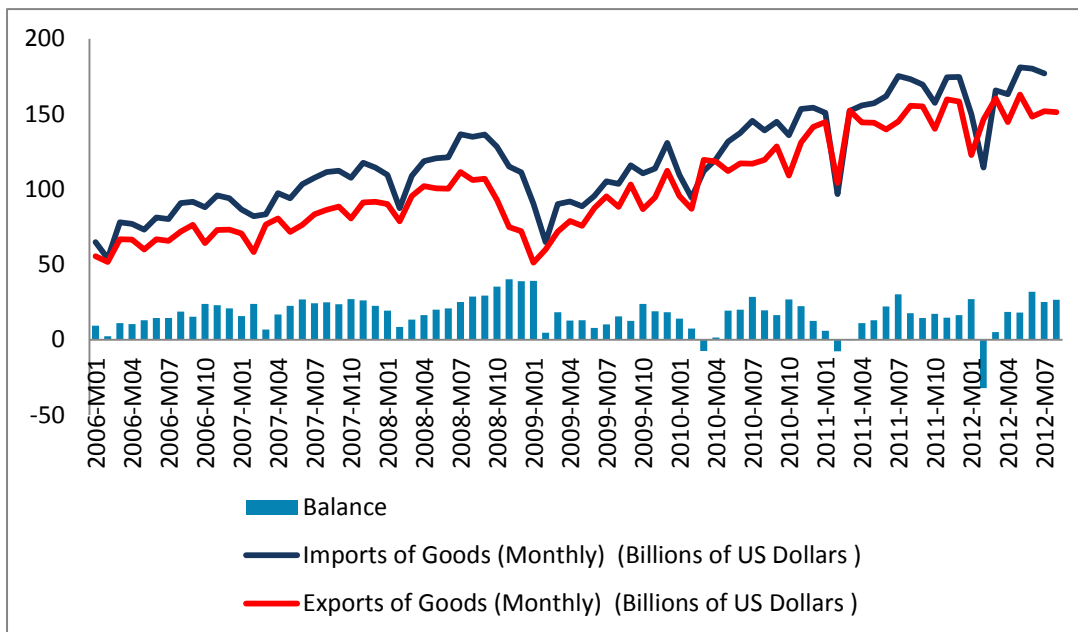
The most recent Chinese foreign trade data exceeded market expectations and suggest that the incipient slowdown since late 2011 could be coming to an end. The strong upward trend of Chinese exports and imports was cut short in early 2009 because of the global financial crisis. However, exports began to recover in March 2009 and imports in February that same year. Since then, both exports and imports have followed a generally upward trend:

There has been a gradual slowdown in China's external trade since the last four months of 2011, in an International context marked by low growth and high levels of uncertainty in the United States and, particularly, the European Union. However, China's foreign trade figures for May 2012 show a substantial rebound in both exports and imports, which grew by 15% and 13%, respectively, over the same month in 2011⁵⁷.

These figures compare favourably with earlier market projections, which put year-on-year export growth in May at about 7% and import growth at about 5%.

⁵⁷ ECLAC. *The People's Republic of China and Latin America and the Caribbean*. United Nations. 2012 (p. 23).

Figure 32. China exports, imports and trade balance with the world. January 2006 to May 2012.



Source: ECLAC. October 2012.

3. The EU continues to be China’s main market

The EU trade suffered from a drop in 2009 due to the economic recession in several countries of the EU, but it had already recovered by 2010. According to Eurostat data, “total EU-27 trade with the rest of the world (the sum of extra-EU exports and imports) was valued at EUR 2 850 539 million in 2010. As such, trade activity for the EU-27 returned almost to the record levels that had been recorded in 2008. In comparison with a year before, total trade in the EU-27 increased by EUR 546 922 million in 2010.”⁵⁸

After experiencing a sharp fall in both exports and imports in 2009, the EU-27 saw its exports rise to a record level of EUR 1 348 778 million in 2010, an increase of 23 % compared with the year before. This was largely driven by increases in the level of exports of machinery and transport equipment and other manufactured goods. Imports rose by 24 % to be valued at EUR 1 501 761 million, with the largest expansions recorded for imports of machinery and transport equipment, and energy products (all data from Eurostat).

If we turn our eyes to China, we can see that this country remained the most important supplier of goods imported into the EU-27 market in 2010, as imports from China grew by around 20% between 2009 and 2010. The large increase in these purchases from China was dominated by machinery and transport equipment, which made up over half of all the EU-27’s imports from China in 2010.

⁵⁸ EUROSTAT. www.eurostat.ec.europa.eu/statistics. July 2012.

For the European Union, exports to China represent only 8% of the total extra-EU exports. However, in terms of imports, China represents almost one fifth of the total imports. These figures, shown in the table below, confirm an important unbalance unfavourable to the EU.

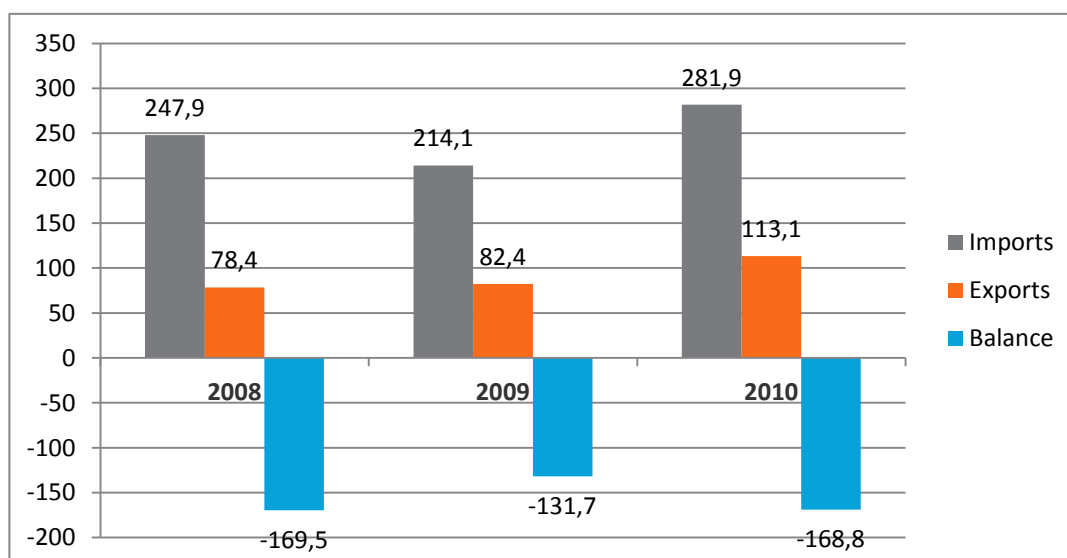
Table 20. Foreign trade of the EU27 with China

% OF TOTAL EXTRA-EU27	2008	2009	2010
Imports	15.8%	17.8%	18.9%
Exports	6.0%	7.5%	8.4%

Source: European Commission, Eurostat

This trade situation was explained as follows by the EU-China High Level Economic and Trade Dialogue⁵⁹. “The EU-China partnership builds on a solid and fast developing economic relation. The EU continues to be China’s main export market. In 2009 the EU imported €215 billion worth of goods from China”. At the same time, for Europe, China was the fastest growing export market. Exports towards China from the EU grew by 4% from 2008 to 2009.

Figure 33. Trade in Goods, EU-27 with China, billions of euros



Source: European Commission, Eurostat

The level of EU exports to China remains below the potential that this relationship would justify. “The EU runs a deficit with China on trade goods which was €133

⁵⁹ EUROPEAN COMMISSION. Factsheet: Results of the third meeting of the EU-China High Level Economic and Trade Dialogue: 20-21 December 2010. www.trade.ec.europa.eu/doclib/cfm/. The EU and China held their third High Level Economic and Trade Dialogue (HED) on 20 and 21 December 2010 in Beijing. The overarching theme of the meeting was how the EU and China can address challenges and create opportunities through open economies and cooperation. March 2010.

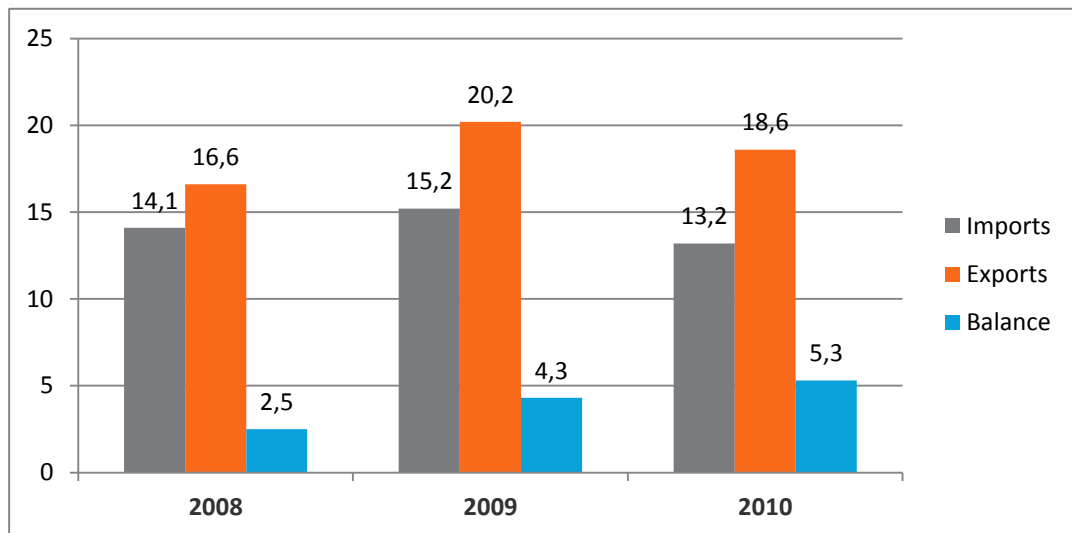
billion in 2009 (down from €169 billion in 2008). Through better market access, European exporters should be well placed to increasingly sell their quality products on the rapidly expanding Chinese consumer market.”

The discussions during this meeting held in December 2010 reaffirmed a powerful commitment to unlock trade and investment as essentials to recover from the recession. In particular, both parties stressed the need to make progress on the WTO agreements (Doha Development Round), to advance negotiations and try to achieve a trade situation that is more balanced between the EU and China: “move towards a more balanced trade relationship, including well-enforced intellectual property rights and strong patents systems”.

The EU stressed the importance to access the markets in an “undistorted” way because it is essential for international businesses to compete on a level playing field, that is, in a fair and equal way.

However, if we consider the trade in services, the situation is clearly different, and, this time, favourable to the EU: the EU27 obtained a surplus of 5.3 bn € in trade in services with China in 2010. Moreover, the positive balance gets more encouraging year after year. As we will have the chance to study in the next chapter, services is going to become one of the main opportunities for European and Spanish companies to enter China.

Figure 34. Trade in Services, EU-27 with China, billions of euros



Source: European Commission, Eurostat

Services is a very wide term. More specifically, services where the EU has a surplus can be found in other business services (+2.6 bn), royalties & license fees (+1.6 bn), computer and IT and other services. The ones where the net balance was favourable to China were transportation, insurance and personal, recreational and cultural services. Finally, China accounted for over 3% of total extra-EU27 trade in services.

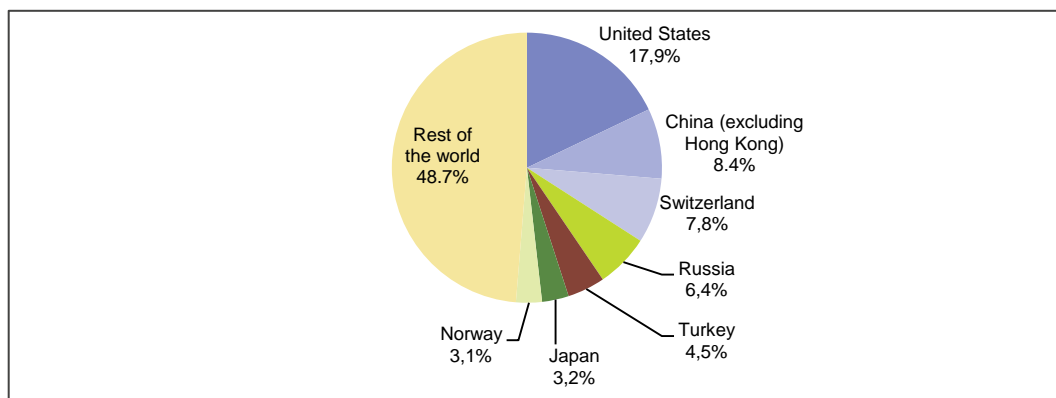
Table 21. EU27 trade in services with China, 2010 (millions of euros)

	Credit	Debit	Net
Total	18 515	13 223	5 292
Transportation	6 215	6 382	-167
Travel	2 076	1 861	214
Other services:	10 206	4 942	5 263
<i>Communications services</i>	267	155	112
<i>Construction services</i>	520	421	99
<i>Insurance services</i>	97	236	-139
<i>Financial services</i>	415	246	170
<i>Computer and information services</i>	953	174	778
<i>Royalties and license fees</i>	1 630	36	1 593
<i>Other business services⁴</i>	6 112	3 513	2 599
<i>Personal cultural and recreational services</i>	48	50	-1
<i>Government services other</i>	163	111	51
Total extra-EU27	478 987	415 012	63 974

Source: European Commission, Eurostat

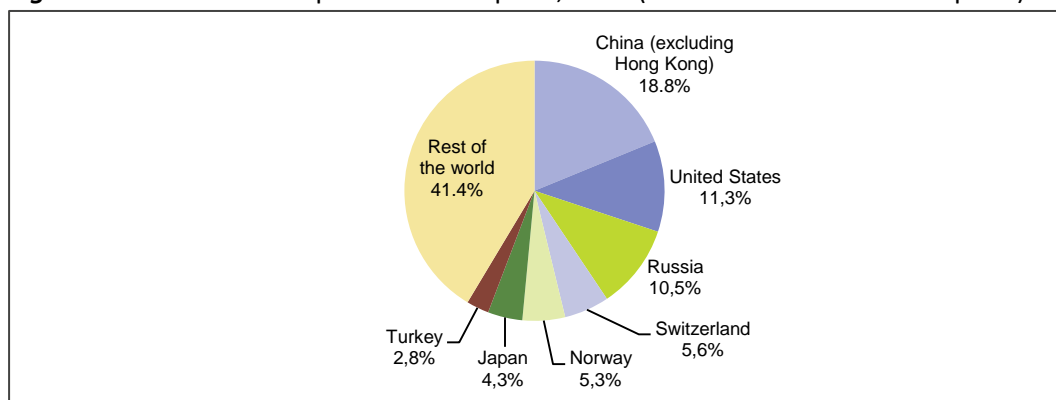
Who are the EU main trade partners? They are clearly the USA and China. The US is our chief destination of goods, followed by China, Switzerland, Russia and Turkey. China, on the other hand, is our chief origin of imports, with almost 20% of all our purchases. Other imports come from United States, Russia and Switzerland: that is, same set of partners both for imports and exports.

Figure 35. Main EU trade partners for exports, 2010 (% share of extra EU-27 exports)



Source: European Commission, Eurostat

Figure 36. Main EU trade partners for imports, 2010 (% share of extra EU-27 imports)



Source: European Commission, Eurostat

The EU exports 18% of the goods to the USA, and imports only 11% from this country. On the contrary, the EU imports 19% of the goods from China and exports only 8% to this country. Switzerland and Russia are the next most important partners, followed by Japan and Norway. The rest is very fragmented amongst many countries.

The table below shows the imports and exports of the EU with China and the USA. As expected, the trade balance with the USA is positive for the EU, while with China the trade is extremely favourable towards the Asian country. While the surplus with the US remains practically stable along the years, the deficit with China has multiplied by more than three in the last decade.

Table 22. Extra EU-27 trade by main trading partners (USA and China), EU-27, 2001-2010

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
EXPORTS										
Extra EU-27	884.7	891.9	869.2	953.0	1,052.7	1,160.1	1,240.6	1,309.9	1,097.1	1,348.8
United States	245.6	247.9	227.3	235.5	252.7	269.1	259.2	250.1	205.5	242.1
China (excl. Hong Kong)	30.7	35.1	41.5	48.4	51.8	63.8	71.8	78.4	82.4	113.1
IMPORTS										
Extra EU-27	979.1	937.0	935.3	1,027.5	1,179.6	1,352.8	1,435.0	1,566.3	1,206.5	1,501.8
United States	203.3	182.6	158.1	159.4	163.5	175.5	174.1	186.8	159.2	169.5
China (excl. Hong Kong)	82.0	90.1	106.2	128.7	160.3	194.9	232.6	247.9	214.1	282.0
TRADE BALANCE										
Extra EU-27	-94.4	-45.1	-66.0	-74.6	-126.8	-192.7	-194.5	-256.4	-109.3	-153.0
United States	42.3	65.3	69.2	76.1	89.2	93.6	85.1	63.3	46.3	72.6
China (excl. Hong Kong)	-51.3	-55.0	-64.7	-80.3	-108.5	-131.1	-160.8	-169.5	-131.7	-168.9

Source: European Commission, Eurostat and own elaboration.

It is interesting to note that while the EU exports to China mostly machinery and vehicles, other manufactured articles and chemicals, the largest imports are exactly the same: machinery and vehicles, other manufactures and chemicals (to a less extent). This can be explained because the level of technology of the manufactures varies: the EU exports machinery and goods with a higher technology level and imports manufactured goods from China more intense in labour cost.

Table 23. EU-27 trade in goods with China by product, Jan-Jun 2010. Millions of euros

Millions of euros	Exports	Imports	Balance
Total	53 462	124 944	-71 482
Primary products:	4 970	3 217	1 752
<i>Food & drink</i>	906	1 830	-923
<i>Crude materials</i>	3 757	1 288	2 469
<i>Energy</i>	306	100	206
Manufactured goods:	47 604	121 197	-73 594
<i>Chemicals</i>	6 117	5 105	1 012
<i>Machinery & vehicles</i>	32 727	64 576	-31 849
<i>Other manuf'd articles</i>	8 759	51 515	-42 756
Other	889	530	359

Source: European Commission, Eurostat and own elaboration.

To summarise, as it has been stated before, trade of goods presents a deficit for the EU. There are two exceptions to this: crude materials and chemicals. In both cases, the EU exports more than what it imports. The EU is especially weak in machinery and vehicles (including computers, electric and electronic parts), and in other manufactured articles (comprising textiles, rubber, shoes, accessories, scientific instruments, watches, cameras, etc.): in these two groups of goods the imports are a lot higher than the exports.

4. Foreign Direct Investment

We would like at this point to reinforce this idea, central to our research: there is an opportunity here that can be developed in the future. Direct investment in China is a source of future trade. Instead of only taking into account exports figures, attention should be also focused on investment figures, the pool position for a potential, solid and durable trade.

Table 24. Spanish Direct Investment in China. 2007-2011⁶⁰

Spanish Direct Investment in China	2007	2008	2009	2010	2011 (1st three months)
Thousands of euros	620,383.48	126,160.06	109,981.12	1,299,780.06	556,158.91

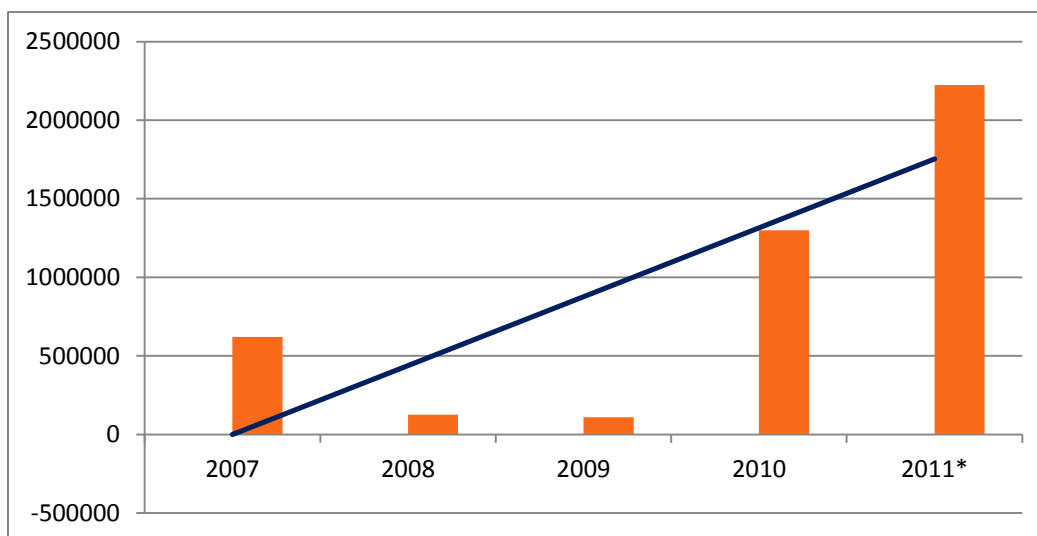
Source: Instituto Español de Comercio Exterior (ICEX)

In summary, we may conclude that even a modest industrial presence of Spain in China could have a significant impact in the access to the Chinese market. European industries established in China import most of its components and raw materials from Europe for processing and assembling in China. Therefore, the higher the industrial base of a foreign country in China, the greater its exports to China. As we can see the FDI of Spain in China is rising significantly. If we add this fact to the improvement of the trade balance, we can picture an optimistic picture for the future.

As we will see in the next chapters, there several hundred Spanish businesses of all sizes and all sectors set up in China. Most of them plan to remain in the country. They are in general satisfied with their business in the country and many are growing. It can be expected that their investment will grow too.

⁶⁰ ICEX. www.icex.es Datacomex Database. Gross investment flows in thousand euros. Data are available only from 2007 onwards. May 2012.

Figure 37. Spanish Direct Investment in China. Thousands of euros



Source: ICEX and own calculations. 2011* is an estimate, assuming the 2nd, 3rd and 4th quarters had the same positive behaviour as the first. Gross investment flows in thousand euros. (Data are available only from 2007 onwards).

We can draw now a final conclusion on the trade relations of Spain with China. In the world ranking, Spain occupies number 21 for China's exports, and Spain is provider number 36 (a very low position in the ranking, by the way). We may start with this negative first impression. In fact, imports of Spain are still five times larger than its exports.

However, if we look with more detail, the difference is changing favourably towards Spain year by year, slowly but surely. If Spanish exports grew by 32%, in 2011, imports grew by only 2%. This is due to the drop of the Spanish demand for consumer products caused by the economic recession. Therefore, even if the trade balance is still very negative towards Spain, the situation is shifting. Main sales of Spain to China focus on semi-manufactures of plastics, chemicals, steel products, automotive components electrical goods and construction materials. Along with this trade picture, we can appreciate an important growth of FDI of Spain in China in 2010 and 2011 (after dropping dramatically in 2008 and 2009). This will be source of future exports. So if the situation continues like this, there are sound reasons for optimism.

We can see the summary of the situation just described in the diagram below. It represents a very general and summarized overview of the circumstances, but it clarifies our reasons for a relative confidence in the future (especially when the general economic situation for Spain is so pessimistic). Now more than ever, Spain needs to look outside for market opportunities.

Figure 38. Summary of the trade balance situation Spain-China



Source: own elaboration

In the next chapters we shall analyse the main opportunities and challenges accessing the Chinese market and then, the structure of Spanish businesses: their size, the sectors in which they operate and their internationalization process.

IV. ACCESSING THE CHINESE MARKET. MAIN OPPORTUNITIES AND CHALLENGES

The present section of the research focuses on the actual opportunities and challenges which western companies in general, and Spanish ones in particular, face when entering the Chinese market. If until here the research done was mainly based on official data sources and established authors, this section is primarily based on the experience gained by consultants, business people and institutions that are trying to promote Spanish exports into China. From that point of view, we can say that the findings are practical and based on real life.

Spain established diplomatic relations with China in 1976. Eight years later, the first Spanish company set up business in the country: it was ALSA, a well-known business case of a firm that was successful in launching and consolidating a regular bus service between different Chinese cities. Before ALSA, buses in China ran when they were full, i.e. they did not have a regular schedule.

In the following years, Spain was not very active in the country and it was not until the 90s, and even after 2000, when a significant amount of Spanish businesses decided to establish a permanent basis on the country. Three veteran companies in this market - ALSA, Técnicas Reunidas and Bodegas Torres - and two companies that have arrived in relatively recently - Gamesa and Zara - constitute the core of gold of a business presence that is has been carving with effort and hard work for thirty years, and which has produced results of excellence embodied in an exemplary manner.

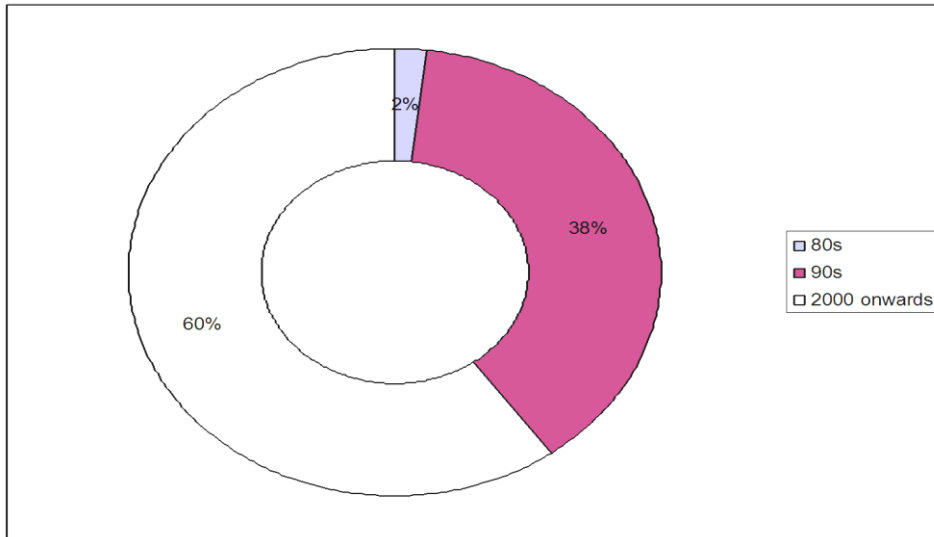
The presence of Spanish companies in China has grown by 70% in the last three years despite the legal insecurity, the problem of counterfeiting in China, the geographical distance and other difficulties. Currently, it is estimated that more than 500 companies, mostly SMEs, have presence in China. These include, on top of the five mentioned above, other very recognised ones such as Mango, Adolfo Domínguez, Roca, Cosentino, Santander, Telefonica, Mapfre, Acciona, Indra, Irizar, Fagor, Nutrexpa, Simon or Freixenet, to name a few. However, apart from these very recognised brands, there are hundreds of smaller firms that operate in China and are not so visible for the public opinion. The main sectors where they operate are related to fashion, design, habitat, food and wine, tourism and leisure, renewable energies, equipment and machinery, banking and finance or education.

As we can see in the graph below, the 80s represented a shy beginning of the establishments of firms Spanish in China. There was a strong reinforcement in the 90s and a decided consolidation in the 2000. The data shown below covers only up to 2006. In the survey we have carried out (see chapter 6) we will analyse in detail the chronological evolution until 2010, which show already the ascending trend until the 2008 crisis, from where numbers dropped significantly.

In general, it can be stated that Spanish firms have been relatively late to access this market, if we compare them to other EU countries such as Germany, France, United Kingdom or Italy, physically present in the country many years before. Spain has

generally been more connected to other world areas such as the EU, for geographical reasons, or Latin-American, for cultural reasons. Asia has been historically ignored, unknown, feared and neglected.

Figure 39. Chronology of establishment of Spanish firms in China



Source: Casa Asia. Data until 2006.

1. Main opportunities when accessing the Chinese market

In chapters 2 and 3 we looked at figures and indicators that show that China has become an interesting and growing market that offers plenty of opportunities from the point of view of objective data. Now, we will look at the market and its opportunities from a more qualitative point of view.

1.1. China does not want to be the world's factory

Or at least China wants to be many more things on top of being one of the world's factories. According to Lluís Lluich (Director of International Promotion at Barcelona Chamber of Commerce), the cost of labour in China is increasing non-stop. That fact, combined with the rise in oil prices, results in very expensive transport costs, which forces western firms to change their strategy. As a matter of fact, while only five years ago it was worth producing in China and then bringing the manufactured products back to Europe's market, this is no longer desirable.

The increase in labour and raw materials costs means that products made in China are no longer so cheap, even for the Chinese market. China offers now a wide range of products, and certain of them are quality-based and have medium-high prices.

Following Lluich, in a summarised comment, the evolution has been very fast: first, Spain was importing from China as the main feature. Then Spanish factories moved their production to China to sell in Europe. Now we try to sell that production, or part of it, in China, as an attractive market. And finally, as the new trend, China is investing in Spain. Europe may be moving towards a "re-industrialisation". Chinese

investment is apparently serious about setting up a factory in Barcelona to produce Chinese cars. China is becoming the main world investor in Latin America, Africa, or Europe. They are investing in strategic sectors, in raw materials and in infrastructures. According to Emilio Mulet, Director at China Consultants, China is operating as a strategic investor: they choose strategic regions of the world and in each one of them, the Chinese Government invests heavily in the most strategic sector. For instance, the Chinese firm Hutchison was awarded the concession to construct and operate the largest container terminal in the Port of Barcelona, and one of the largest in Spain. We could continue with a long list regarding investing in natural resources in Brazil, the chemical sector in Israel, car makers such as Volvo, etc., all part of this very well-planned strategy. According to this point of view, the Ministry of Commerce CCPIT, China Council for the Promotion of international Trade, employs the best talented people in China: they write reports that recommend top investments all over the world. Since the banks are public, decisions are easy and quickly made.

This perspective shows a complete mentality adjustment. All these changes have occurred in only one decade. A survey carried out by Casa Asia⁶¹ shows that foreign businesses are “changing their traditional concept of China as the world factory towards the notion of a vast marketplace with huge consumption potential”. So we need to change our perspective of China as a world factory to move towards the picture of China as the world’s largest middle class market, and China as the top-world investor. This mentality change requires that we reconsider the perspective we have had for centuries. Experts coincide that China’s leading position in the world is not something new. Chinese people think of themselves as the “country in the middle”. They must occupy a leading world position, because it is only natural.

The following table shows the historic evolution of the world GDP since 1700, mixing a variety of sources and estimations, and reflects the power China had in the past and is regaining back nowadays:

Table 25. Historic evolution of the world GDP (as % of world total)

year	1700	1820	1890	1978	2007	2015
EU	23.3	26.6	40.3	27.9	22.7	18.3
USA	-	1.8	13.8	21.8	21.4	18.3
Japan	4.5	3.0	2.5	7.7	6.6	5.1
China	23.1	32.4	13.2	5.0	10.8	16.9
India	22.6	15.7	11.0	3.4	4.6	6.3

Sources: Angus Maddison⁶² and IMF/WB

⁶¹ CASA ASIA. *Estudio sobre la presencia empresarial española en Asia*. Círculo de Negocios de Casa Asia. This report is based upon interviews carried out to 101 Spanish business executives of different sectors established in Asia (three quarters thereof in China). The findings being highly interesting are used also for other sections in this thesis.

⁶² Angus Maddison was a world scholar on quantitative macroeconomic history, including the measurement and analysis of economic growth and development. He was a Professor at the

Two hundred years ago, in 1820, China accounted for one third of the world total GDP. After that, for reasons we are not going to analyse here, its relative weight went down so much that by 1978 its influence on the world GDP was only 5%. In the last three decades, however, its contribution to the world wealth has not stopped to increase, and by 2015 it will reach almost 17%. For many experts, and for many Chinese people, this increase is only natural and it will not stop here: they see China's future as a path towards the world power.

Etymologically, China means "the Kingdom in the middle", or the "middle country", from the belief that they lay at the centre of the earth. See below the world's map according to China in 1763.

Figure 40. World map from the perspective of the "Middle Kingdom"



Source: Frank Jacobs⁶³ in www.bigthink.com

The name of the country China is normally translated as "middle kingdom". But a more accurate translation would be a country central to the world, wealthy in resources and capabilities, and well protected. They view themselves as central players on the world, in control of their own destiny, with a sense of prosperity, strength and hope for a better future. This contrasts with the sense of pessimism that is common now in Europe and more acutely, in Spain.

University of Groningen (The Netherlands). He passed away in 2010 but his work is being continued. This table was given to me by Prof. J. Tugores, to whom I thank.

⁶³ The map is similar to many present-day Chinese world maps in that it positions at the centre of the map China (which used self-confidently to refer to itself as the "Middle Kingdom"). It states that it is a 1763 copy of a fifteenth-century original. www.bigthink.com. April 2010.

Table 26. A unique Chinese self-identity: central, protected and wealthy

What does China mean in the Chinese language? 中国	Common translation 中国 Middle Kingdom
More accurate translation 中国 Central wealth protected by a wall	Chinese self-identity 中国 A place of great wealth, protected by walls, at the centre of world affairs

Source: Silverstein and other authors. *The \$10 trillion Prize*.

1.2. China has significantly reduced its tariffs

China has significantly reduced its tariffs. Its average tariff rate fell from almost 60% in the early 80's to 15.6% in 2001 and 9.5% in 2009⁶⁴. Interestingly, this reduction has been achieved in just 20 years, half the time it took the EU to an equivalent course. It should also be noted that the Chinese tariff cut was made mostly before WTO entry.

Table 27. China's average tariffs by sector (in percentages)

Product groups	Consolidated	Most-favoured nation
Animal products	14.9	14.80
Dairy products	12.2	12.00
Fruit, vegetables, plants	14.9	14.80
Coffee, tea	14.9	14.70
Cereals & preparations	23.7	24.30
Oilseeds, fats & oils	11.1	10.80
Sugars and confectionery	27.4	27.40
Beverages & tobacco	23.3	22.30
Cotton	22	15.00
Other agricultural products	12.1	11.30
Fish & fish products	11	10.80
Minerals & metals	8	7.40
Petroleum	5	4.40
Chemicals	6.9	6.50
Wood, paper, etc.	5	4.40
Textiles	9.8	9.50
Clothing	16.1	16.00
Leather, footwear, etc.	13.7	13.20
Non-electrical machinery	8.5	8.00
Electrical machinery	9	8.30
Transport equipment	11.4	11.50
Manufactures, n.e.s.	12.2	11.90

Source: World Trade Organization (WTO). World Tariff profiles 2011.

⁶⁴ CASA ASIA. *Estudio sobre la presencia empresarial española en Asia*. Círculo de Negocios de Casa Asia. Barcelona, 2006.

Moreover, import quotas were lifted in 2005 and export regime has been simplified, although complex measures to manage certain exports are still in use. The sum of exports and imports relative to GDP (trade openness rate) amounted to 44% in 2009 compared to less than 10% in 1978.

In short, the opening of a large number of key sectors of China's economy is growing, although there are still significant restrictions for foreign companies in certain sectors, such as the energy (for both conventional and renewable energy), telecommunications, banking, government procurement, insurance, engineering, construction, legal services and many others.

Despite liberalization measures, operational restrictions that prevent foreign firms to compete in equal terms with domestic ones still remain - in these sectors and many others. Norms, standards, regulations and interpretations of the above proliferate in a way that hinders the activity trade and investment by foreign companies.

1.3. Chinese consumers love shopping

According to the findings in section 3, the China market is growing exponentially thanks to: an increase in population, in urban population and in middle classes. Imports are growing and we can say that China needs everything.

Friedman, in his book "The world is flat"⁶⁵, explains that according to his findings "middle class is another way of describing people who believe that they have a pathway out of poverty or lower-income status toward a higher standard of living and a better future for their kids". It does not matter whether you make \$2 or \$200, if you believe in social mobility and that hard working and playing by the rules of your society will get you where you want to go. "Where people have hope, you have a middle class" a Chinese government official said. Friedman concludes that "the good news in China is that, with all its flaws and internal contradictions, it is a country now home to hundreds of millions of people who are hopeful enough to be middle class".

Retail sales are still growing at a fast pace: although they have slowed down from the 20+ per cent growth achieved in mid-2008, they continue to rise by a robust 15 per cent. In certain key industries that reflect directly middle class consumption, China is already rising to overtake the United States as the most important market. As recently as 2000, for example, "the US accounted for 37 per cent of global car sales, while China accounted for barely 1 per cent. This year (2010) China is expected to account for 13 per cent of global car sales. Including trucks and buses, vehicle sales in China may surpass 13 million in 2009, which would make China the world's largest vehicle market". Kharas then adds: "Five years ago General Motors sold 10 cars in the US for every one car sold in China; the ratio is now quickly approaching one to

⁶⁵ FRIEDMAN, T. L. *The world is flat. A brief history of the twenty-first century*. Farrar, Straus and Giroux, FSG Books. New York, 2005.

one, and soon China will be a bigger market than the US for America's largest automaker"⁶⁶.

Another product that reflects well the middle class consumption is the mobile phone market. In that respect, Kharas confirms that similarly to the car market, China has recently emerged as the world's biggest cell phone market, "home to an estimated 700 million subscribers. Last year Nokia, the largest cell phone maker in the world, had net sales of USD8.2 billion in China, more than three times its US revenues (Nokia 2008)".

Survey evidence also suggests China's new middle class is eager to become the world's leading consumers. Chinese consumers love consuming and spend an average of almost ten hours a week shopping, according to Kharas:

A 2007 survey of 6000 Chinese shoppers found that Chinese consumers spend 9.8 hours per week shopping, as compared to only 3.6 hours for the typical American. Additionally more than 40 per cent of Chinese survey respondents said shopping was a favourite leisure activity. It is such attitudes that have led global retailers to bet on the future of China's domestic market: in the 13 years since opening its first store in China, Wal-Mart has gone on to open an additional 257 retail units (Wal-Mart, 2009). The issue in China is that its middle class is still very small (less than 12 per cent) as a percentage of the total population.⁶⁷

Amadeo Jensana, Director of Economic Programmes and Cooperation of Casa Asia, invites to do the following comparison: consumption in the USA represents 70% of the GDP, while its equivalent for China is only 38%. Of course these data will take a long time to converge –if they ever do- but the expectation is that these indicators come closer together as time goes by. In other words, consumption in China is going to grow significantly. There is yet another powerful reason behind: the increase in Chinese salaries (some years this growth can be as high as 20%). This is allowing Chinese workers to dedicate each month more income to spending. The Chinese Government is encouraging western multinationals to increase the salaries of the Chinese workers.

Why do Chinese people save so much instead of consuming? Two reasons could explain the fact.

- In the first place, the credit market is underdeveloped, so Chinese people do not ask for credit as freely and lightly as Westerners do.
- In the second place, the welfare state is not as developed in China as we are used to: Chinese people feel they need to save to cover needs such as

⁶⁶ HOMI K. *The emerging middle class in developing countries*. OECD Development Centre. Working Paper n. 285. January 2010.

⁶⁷ HOMI K. *The emerging middle class in developing countries*. OECD Development Centre. Working Paper n. 285. January 2010.

education or health care (needs that in the European Union for instance are mostly covered by the public sectors). As we can see, there is a mix of economic and cultural reasons that explain the high level of savings. It is well-known that changes are slow and changes in culture are especially sluggish.

Finally, it will be worth introducing the concept of the “little emperor”: this is a name that refers to only children in the People's Republic of China after the one-child policy was implemented. “In the 1950s, Chinese women had an average of 6 children; by 1979, when policies were being established to minimize reproduction, the average fell to 3. By 1990, the total fertility rate dropped to 2.4. Increasingly more families are agreeing to sign a certificate promising not to have more than one child”⁶⁸

The concept “little emperor” is attributed most frequently to increased spending power within the family unit and the parents' desire for their child to experience the benefits they were denied. The children count with the sole command of the attention of their parents and grandparents. On the one hand, this may be considered as a problem that is changing how society functions. On the other, this segment of the population has great needs (from toys, to clothes, to education, jewellery or electronics goods – and pretty much whatever they want) and great resources to cover those needs. As China income per capita has raised, the parents and grandparents focus on a single child, resulting in “social and economic implications such as the perilous 4-2-1 indulgence: four grandparents and two parents indulging one child”.

The Little Emperor effect is primarily an urban phenomenon. The one-child policy is not as rigorously enforced in the countryside as in the urban communities. Little Emperors also bear the burden of heavy expectations. “Parents who feel they lost their chance in the Cultural Revolution (compensation syndrome) put immense pressure on these children to succeed and compete academically (Shao & Herbig)

According to Clay Chandler in his article about what he calls the *Me Generation*, “China’s only children – more than 100 million- make up the largest Me Generation ever. And their appetites are big”.⁶⁹

Geoff Dyer draws a very vivid picture of this generation in his article in the Financial Times⁷⁰: “China’s youth can get a bad press. In most accounts, they are the *Little Emperors* or the *Me Generation*, the spoilt and apolitical offspring of one-child families who are interested in fast cars, video games and designer goods but little else. At the main Shanghai store of Louis Vuitton there is a queue to get in at

⁶⁸ SHAO, A. T.; HERBIG P. *Marketing implications of China's little emperors*. Review of Business Vol. 16. 1994.

⁶⁹ CHANDLER, C. *Little Emperors*. CNN Money. October 4th, 2004. www.moneycnn.com. April 2012.

⁷⁰ DYER, GEOFF. *China's little emperors demand their due*. 7th July 2010. Financial Times. www.financialtimes.com. May 2012.

weekends – young women wait patiently in the rope line, as if they were trying to get into the hottest new LA club”.

This is a generation of well-educated people. But in spite of having all their desires fulfilled, they live under a lot of pressure. For the tens of millions of young Chinese graduates, buying a flat is a central part of their plan to live a modern, middle-class life. Apparently, “young Chinese men feel the social pressure the most”.

1.4. Chinese consumers love western trends and brands

The experts interviewed for this research coincide that Chinese customers are very open to western habits. For instance, even if it is still a marginal habit that applies to only a small percentage of households, Chinese people are starting to drink wine or use olive oil. Not in large quantities, or at least not only because of the products themselves, but for what they represent in terms of status, fashion or “coolness”.

Judith Padros, Area Manager for Asia at Barcelona Chamber of Commerce, states that since we cannot compete with China in terms of numbers (they are superior in terms of quantities, costs, prices), we can compete in image, reputation, quality or *western-orientation*. In the Chinese mentality, western products are more advanced; they have something appealing that makes them desirable, something to look forward to. This is where we can play a better game.

Therefore, even if we often need to adapt Spanish products to the Chinese tastes, it is recommended to leave a certain air of *Europeanism*, which will be appreciated by consumers.

According to Amadeo Jensana, fashion, luxury goods and food are sectors that offer an opportunity for Spanish firms in China. Moreover, Judith Padros, who had just come back from China when I interviewed her, has detected another opportunity that is worth a look into: many Chinese firms would like to access the European market. However, this is an unknown for them, at least for the medium and small businesses.

When Chinese firms try accessing the European market, they consider the EU as a whole (certainly like we Europeans do with China: we see it as a whole when it is not). Soon Chinese firms realise that they do not know the European marketplace well enough to introduce their products. This is where according to Judith Padros Spanish firms can be of help: offering a long list of services that go from packaging, advertising, marketing, or publicity and other services.

We shall analyse the opportunity sectors in the next pages.

1.5. Accessing the Chinese market through e-commerce

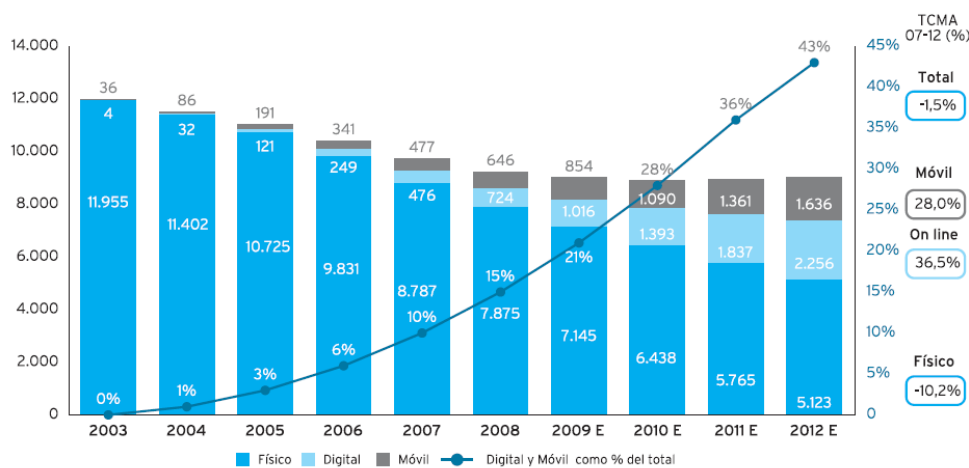
Digital commerce is causing a revolution in many sectors of the economy. In 2003 all the world commerce was physical. Since then, the amount of commerce carried out by digital and mobile means has increased yearly by considerable amounts. While

total retail sales slowed down in most of the markets, e-commerce continued increasing rapidly. For instance, in the US⁷¹, the estimate of U.S. retail e-commerce sales for the first quarter of 2012 was \$53.2 billion, an increase of 3.1% from the fourth quarter of 2011. Total retail sales for the first quarter of 2012 were estimated at \$1,082.6 billion, an increase of 1.7% from the fourth quarter of 2011. The first quarter 2012 e-commerce estimate increased 15.4% from the first quarter of 2011 while total retail sales increased 6.5% ($\pm 0.7\%$) in the same period. E-commerce sales in the first quarter of 2012 accounted for 4.9% of total sales.

The figures above refer to the US, country where these kinds of data are available, which is not the case everywhere. They serve as an example to give us an idea of the magnitude of the changes introduced by electronic sales. The graph below serves to the same purpose, to show the positive evolution of the digital commerce worldwide, compared to the traditional commerce.

Our purpose in this section is not to comprehend the whole world of e-commerce in China, but mainly to point to the potential that is offered to international actors. A Spanish firm who is interested in accessing the Chinese market should not discharge the possibility to exploit an e-commerce alternative without an intensive research first. The volume of trade is too large to be neglected.

Figure 41. Evolution of the digital commerce 2003-2012



Fuente: "Global and Entertainment and Media Outlook: 2008-2012" PricewaterhouseCoopers (2008)

Source: PriceWaterhouseCoopers

As we hope for a better economic climate for 2013, Forrester, a global research and advisory company, is predicting that online sales will average a 10% growth over the next 5 years. While we saw an economic downturn in 2008, e-commerce has remained one of the few positive trends in the market.

⁷¹ CENSUS BUREAU OF THE DEPARTMENT OF COMMERCE, USA. www.census.gov/retail. May 2012.

An increase in e-commerce is due to its growing global expansion and because many internet retailers are expanding their business abroad. Shipping will continue to play a bigger role with e-commerce businesses as the global landscape of shopping is changing and shifting more and more online.

Spain is number four in Europe in terms of e-commerce value, after the United Kingdom, Germany and France, and is stronger than Italy, Holland or Sweden.

1.5.1 Accessing the Chinese market through another door: main advantages to sell online

In the first place, selling online allows a firm to gain access to a larger base of potential customers, thanks to a larger geographical coverage, which is important when we are talking about a vast country like China. Customers all over the country are able to buy a firm's products without leaving their houses, independently of where they live. Selling abroad is no longer a barrier. The difficulty to find distributors in China becomes less of a barrier.

Secondly, e-commerce allows a firm to know better its customers and grow the business intelligence. The web tools allow a firm to know exactly the customers' profile in order to optimise communication strategies. We have already seen how important this is for the Chinese market.

Thirdly, directly related with the reason above, the firm will be able to optimise its marketing results by designing segmented promotional actions directed to a precise target. Therefore, these promotional activities' results can be measured accurately.

Fourthly, the firm that sells online will see how its brand is strengthened compared to that of its competitors. This will result in an increase in sales.

Last but not least, the business will be able to take advantage of the ROPO effect. ROPO is a term that refers to the process of researching online – purchasing offline. Virtually every consumer is within reach with a search engine. According to Paul Burani in his blog Search Engine Watch⁷², "roughly two-thirds of the consumers are using search engines to qualify purchase behaviour, and yet online sales represent at most 7 per cent of the total. So we're not exactly going out on a limb here, saying that a lot of commercially-motivated search behaviour is ending up in a black hole instead of the shopping cart".

One explanation for this is the ROPO effect (research online, purchase offline). In 2011, the overwhelming majority of offline purchases still include some online research component. But ROPO is not a trend that will die off as digital consumer culture continues to evolve; Google estimates that offline sales influenced by online research will grow 12% this year in the US, while online sales begin to flatten out.

⁷² SEARCH ENGINE WATCH. www.searchenginewatch.com Nov. 2011.

1.5.2 Strategic definition of the online business in China

If a business is to launch an online business or an online business department within an existing firm, one of the keys that all the researchers stress is the need to establish first a strategic definition of such a business. This is the guideline that unifies this research: every aspect related to internationalization in general and access to Chinese market (by traditional or e-commerce), has to be approached from a strategic perspective, involving always the whole organization and, in particular, the highest level management.

According to Amvos Consulting⁷³, the strategic definition needs to study the following aspects:

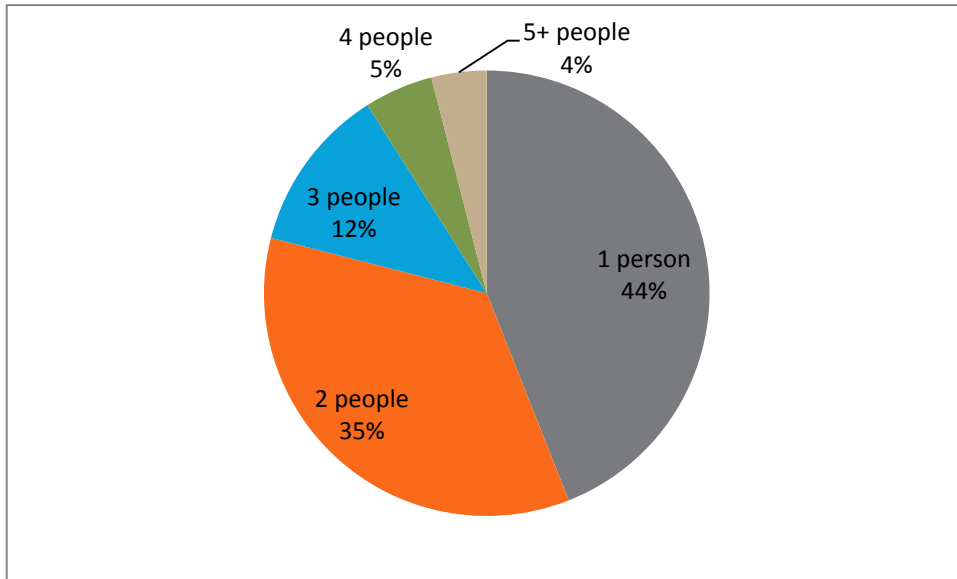
- Key figures about the sector and the competition;
- SWOT Analysis of the product or service;
- Selection and prioritization of the online markets that are going to be tackled;
- Design a solution for the channel conflict (channel conflict occurs when manufacturers get rid of their channel partners, such as distributors, retailers, dealers, or sales representatives, by selling their products directly to consumers for instance over the internet through e-commerce);
- Study the different providers and choose the best options;
- Select and design an online catalogue;
- Election of additional or alternative distribution channels, such as eBay, Amazon, Tmall, Taobao, Alibaba.com, etc.
- Define the commercial policy;
- Develop an online Marketing Plan;
- Define the business KPIs (Key Performance Indicators);
- Write the organization of resources, in particular Human Resources.

E-commerce departments are small. Most of them occupy just one person, and about 80% of them occupy one or two people. Since Spanish firms are mostly small ones, distributing by internet offers an array of new possibilities within their reach. The image of a firm and the power of the brand do not depend so much on the size of the firm anymore. A small firm can project a very strong brand in internet, and customers do not need to know that behind there is a small e-commerce department made up of only one or two people.

The figure below shows the number of persons employed in a typical e-commerce department, calculated according to the world average.

⁷³ AMVOS CONSULTING, during conference at Casa Asia, Barcelona Feb. 2012. www.amvos.com

Figure 42. Average size of the e-commerce departments. World figures

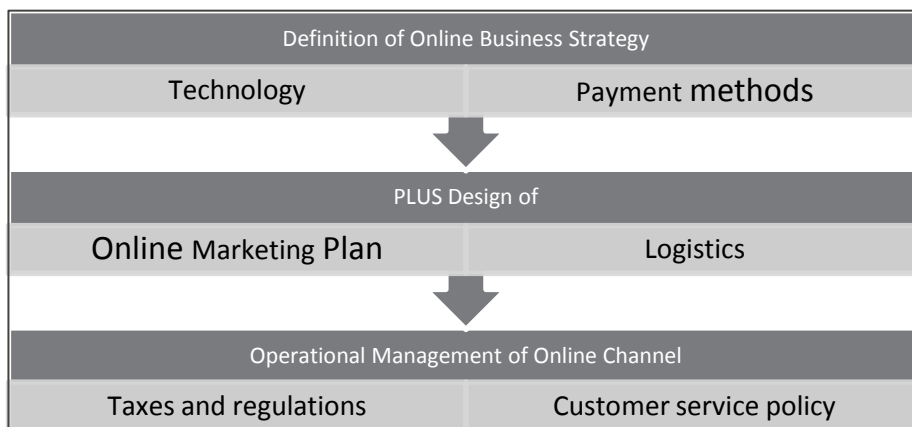


Source: Ecommerce Benchmark Report, UK, SagePay

For a traditional firm, to develop an online distribution channel is like building a business inside a business. The management of this new firm needs to contemplate the technology that is going to be used, the payment terms and methods and ad hoc online marketing plan. But also there are other subjects to be tackled, namely the design of the logistics and an after sales plan: customer relations and all the legal and tax matters that have to be fulfilled. These are all specific and of particular relevance factors for China.

This diagram shows the structure that the firm may want to follow adapted from Amvos consulting:

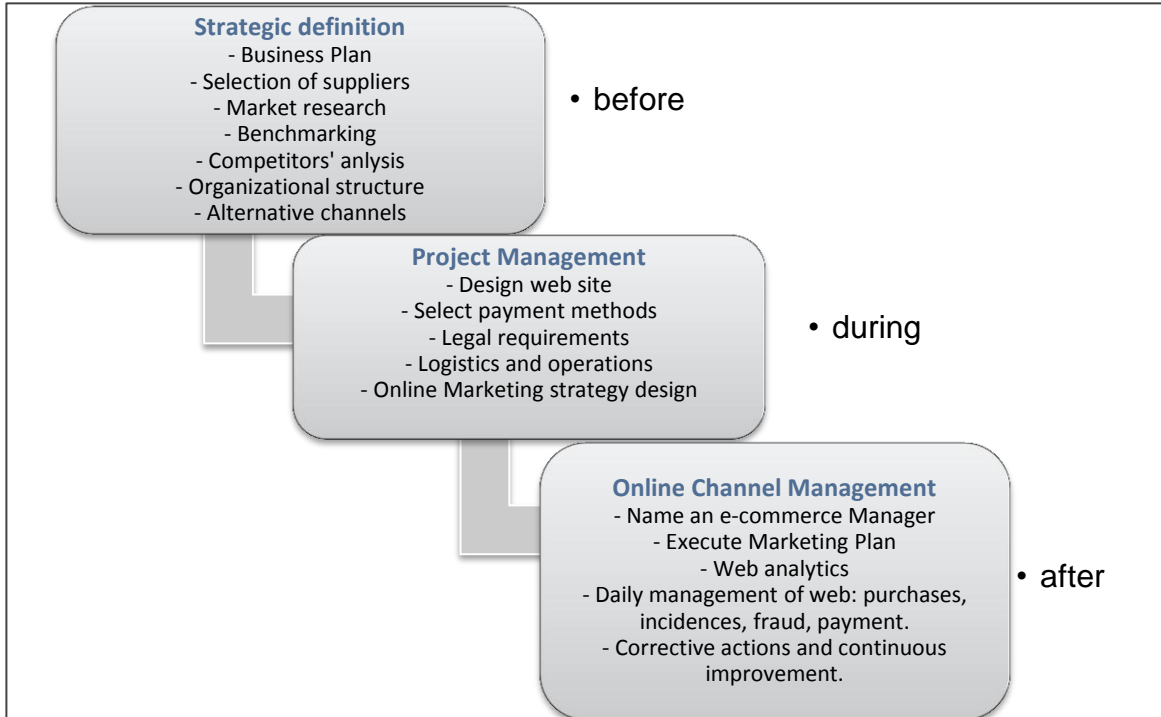
Table 28. Structure of a firm operating in the e-commerce sector



Source: adapted from Amvos & DaD Asia Consulting, 2012.

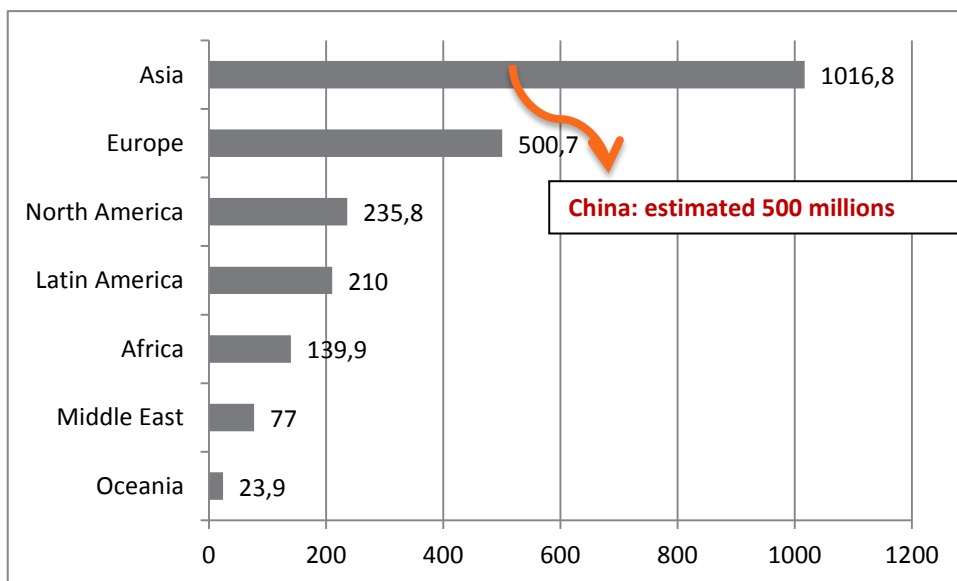
To complete the whole project, there are three phases that need to be completed: before, during and after. They can be summarised in the diagram below:

Figure 43. Phases for the completion of an e-commerce policy



Source: adapted from Amvos & DaD Asia Consulting, 2012.

Figure 44. The internet market is already Asian. Number of internet users by continent. In millions



Source: InternetWorldStats.com

Out of the one billion internet users in the world, it is estimated that half of them are Chinese. In one of the reports, McKinsey Quarterly declared: “as the country is integrated into the world economy, best practices in China will be best practices globally, products developed in China will be global products, and industrial processes developed in China will be the global processes”. China has jumped many of the traditional western development steps to land directly into internet and the most advanced technology.

But who are these internet consumers? The BCG carried out a Digital Generations Consumer Research in 2009 that made a very good picture of those users. China has become a major Internet market with increasingly sophisticated consumers, who are online 3.6 hours a day. In a few years, it will likely become the largest online retail market in the world. Companies that want to win in China must understand the rapidly evolving digital lifestyles of these consumers.

Table 29. The six Chinese internet user segments. Motivations and behaviours

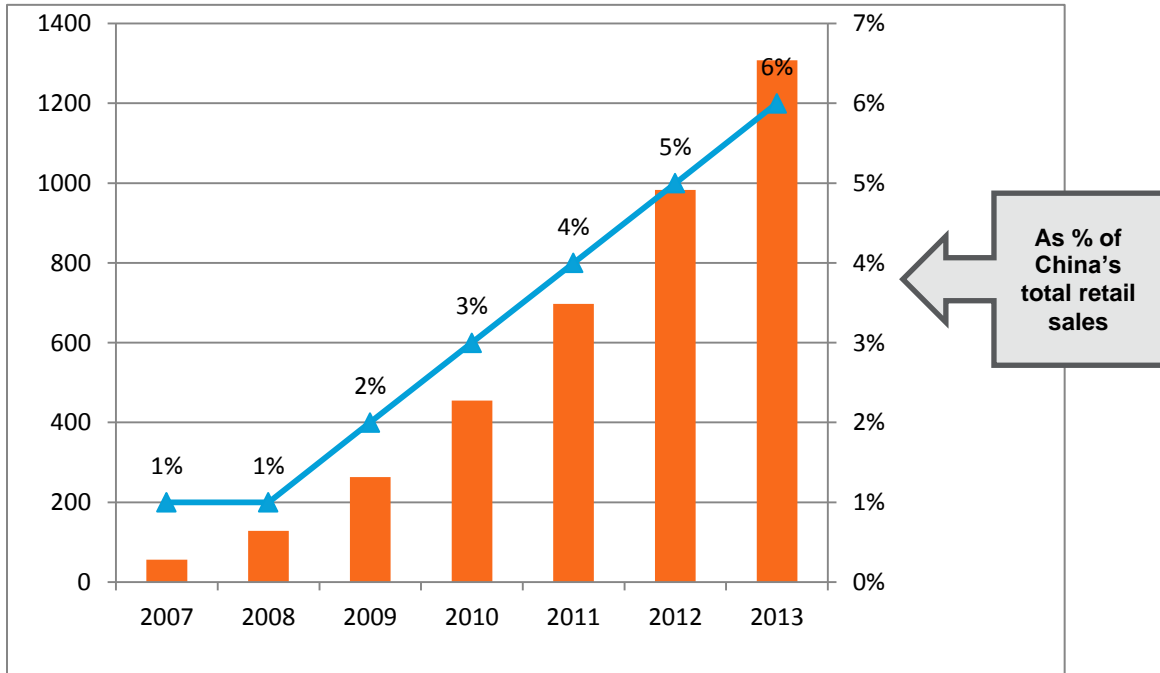
Internet user segments						
SEGMENT	Teenagers	University Students	Young Professionals	Young gamers	Active Middle Agers	Passive Middle Agers
Profile	14-18 y. Grown up with digital services	19-25 y. Grown up with digital services	26-35 y. Educated middle class. First internet experience at University	19-35 y. Lower education and income. First internet experience at internet cafés	36-55 y. Middle class. First internet experience at work	36-55 y. Lower education and income levels.
Penetration	85%	99%	99%	89%	67%	38%
Motivations	Fun & support in studies	Seeking friends	Work and career	Excitement and sense of achievement	Support for daily activities	Relax and kill time
Usage	Heavy users 2.7h day	Heavy users 3.6h day	Heavy users 4.0h day	Indulge heavily 3.2h a day	Occasional and pragmatic user 2.5h day	Infrequent user 1.8h day
		Most active		Most influential		

Source: Adapted from The Boston Consulting Group (BCG). Digital Generations Consumer Research, 2009.

Retail sales are losing ground to e-commerce. Below, China’s online shopping market in billion RMB, and on the right hand axis e-commerce as % of China’s total sales.

While e-commerce represented only 1% of the total in 2007, six years later it will reach a significant 6%, so it is gaining a whole point every year. This shows the opportunities that are opening in this field.

Figure 45. China's online shopping market. Total volume (in billions of RMB) and as a percentage of total retail sales (in %), 2010

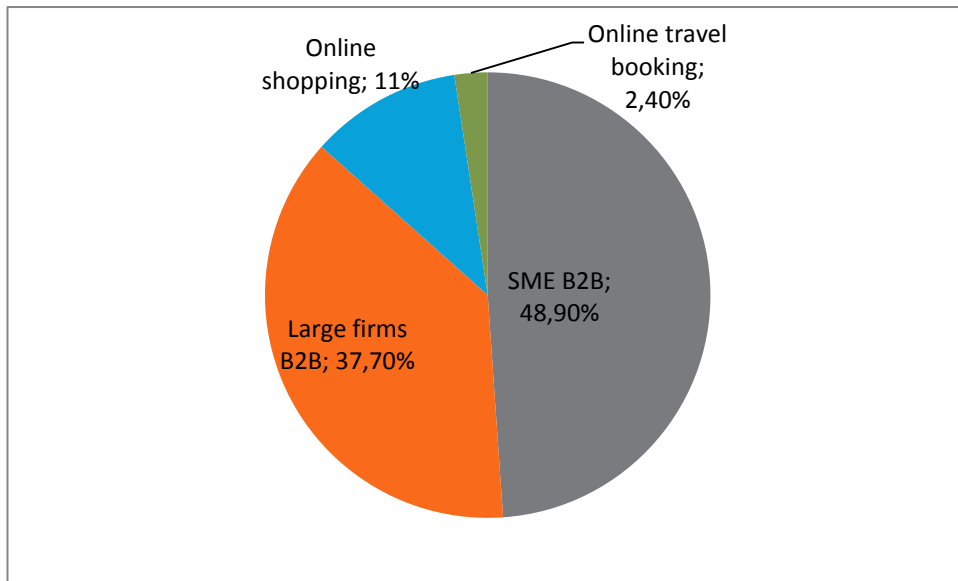


Estimates start after 2010.

Source: Morgan Stanley Research, iResearch.

How is the e-commerce distributed? According to the same research by Morgan Stanley, the total volume of internet sales amount to 840,000 million euros, of which B2B (Business to Business) accounts for most of the sales (86%). The sales to direct consumers represent a very small part of the pie, 13.4%, and are divided into online shopping (11%) and online travel booking (2.4%). B2B sales are mostly done by small and medium sized firms, and it is in this field where we find enormous potential for Spanish services companies.

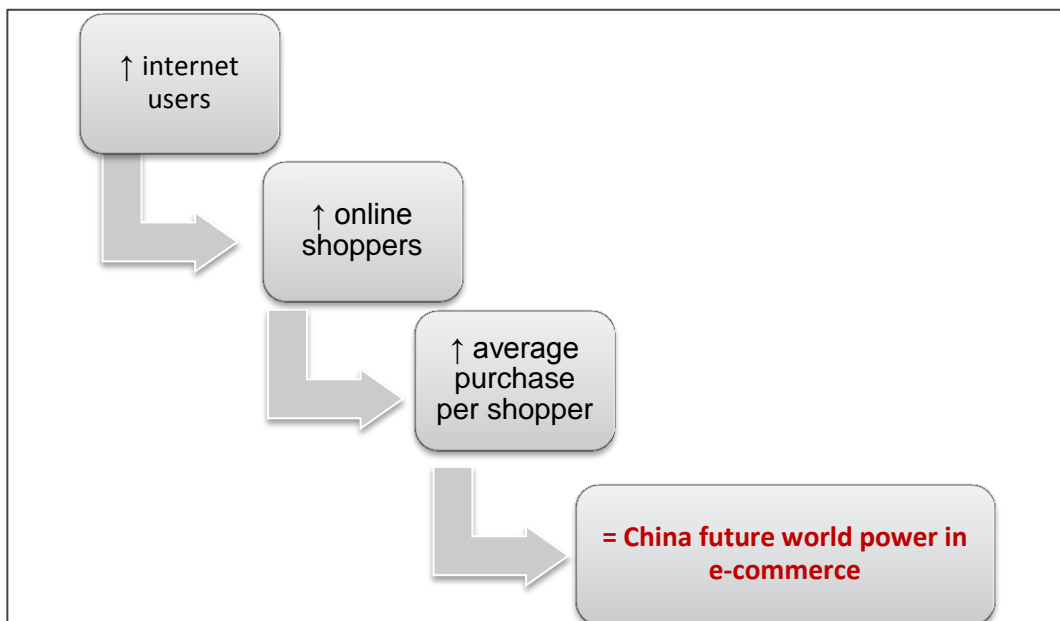
Figure 46. Chinese e-commerce market by type, 2010



Source: Morgan Stanley Research, iResearch.

If the figures are large by now, estimates⁷⁴ forecast a growth by 30% in the next three years. There is a long way ahead, and the basis are already there, to be exploited by whoever is able and willing.

Figure 47. Evolution of the growth expected in internet



Source: Morgan Stanley Research, iResearch.

⁷⁴ THE BOSTON CONSULTING GROUP. *The world's next e-commerce superpower. Navigating China's unique on-line shopping ecosystem.* BCG. 2010.

Most of the growth of course is expected in urban areas in Guangdong, Zhejiang, Jiangsu, Hunan and others.

Although it is not within the objective of this paper, we will add that Business to Consumers (B2C) platforms are very fragmented. The most active ones are 360 Jingdong Mall with 13% of the share followed by Dangdang and Joyo Amazon, these two with around 5% of the share. In B2B, on the contrary, the suppliers are concentrated 45% in Alibaba, a major supplier who is now also operating in most of the world included Spain. Finally, C2C (Consumer to Consumer) is almost a monopoly with the kingdom of Taobao.

Transactional channels are concentrated in Alibaba.com and Tmall.com, while for payment Alipay is compulsory.

Table 30. E-commerce platforms: B2C and B2B main actors

	B2C			B2B	
Ranking	Company name	Revenue (mill. RMB)	B2C market share	Company	B2B market share
1	360 Jingdong Mall	3.6	13.09%	Alibaba	45%
2	Dangdang	1.6	5.82%	Globalsources	7%
3	Joyo Amazon	1.5	5.45%	315 (commodities)	6.8%
4	Newegg	1	3.64%	Made in China	5%
5	Redbaby	0.4	1.45%	Hc360	5%

C2C	Company	C2C retail market share
Ranking		
1	Taobao	82.5%
2	Paipai	9.9%
3	Eachnet	3.3%

Source: Own elaboration from Amvos & DAD Asia Consulting

As we established before, it is not our objective to analyse the vast e-commerce Chinese market. There are plenty of data available and the subject is worth a whole new research on its own. Our intention was solely to first, point towards a potential solution for Spanish firms to access the Chinese market, with an enormous growth opportunity. Second, the process to follow would be similar to the launching of any new conventional business in China: planning and intensive market research before any investment is realised, adapt to the market, give autonomy to the Chinese subsidiary and continuous follow up of the market trends. We will analyse the best practices in chapter 6.

2. Main challenges when accessing the Chinese market

2.1. *“China is for the Chinese”*

When we were told the sentence “China is for the Chinese” for the first time during our interview with Amadeo Jensana - this was in fact his verdict- , we felt some concern. What if China is for the Chinese and Spanish firms cannot access the market at all?

He explained that, in general, as a matter of fact, Chinese firms have a strong negotiation power over their own consumers: they have the production of the products they need, they have good prices, they know their habits and tastes, they have the powerful “made in China” and they count with the knowledge of the distribution channels. They also enjoy the protectionist government policy: “first, the government protects the market. Afterwards, when they feel ready, they let western firms in, but only in alliance with Chinese firms. They fiercely want to be technologically independent from the western world, and they do not want to pay royalties. So everything is in place strategically so that China remains for themselves”.

Having said that, even if the sentence is generally correct, it does not mean that China is *only* for the Chinese and there is nothing we can do about it to gain access to that market.

Moreover, when facing my next interviewees with the same sentence, there was a general feeling that, yes, it is certain in a way but nevertheless there are possibilities for other players as well. China is a huge country and there is enough room for everybody, as long as one knows how to play the game.

2.2 *Difficult legal environment and Intellectual property issues*

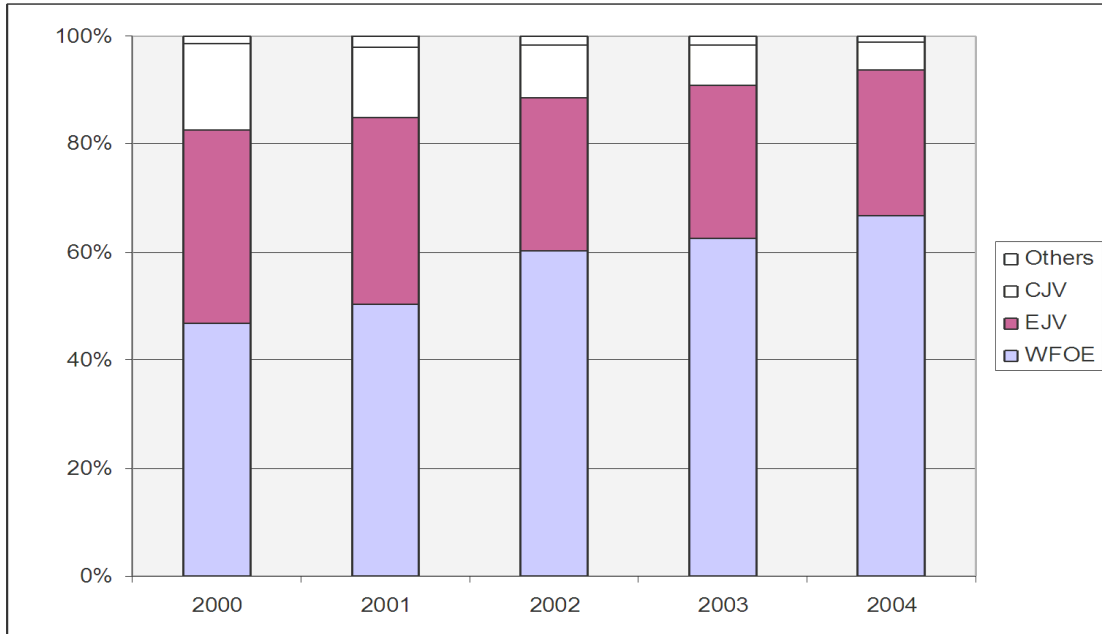
All the experts that were interviewed coincide that there is a duality in the legal system. Rules do not apply in the same way for Chinese firms as they do for foreign ones. Years ago, the joint venture was one of the legal forms that was most widely spread for foreign businesses: find a local partner and create a new firm for the purpose of the JV. This was a legal imperative for many sectors: the only way to establish a firm in China was to create such a legal form. Nowadays, this is no longer the case for most sectors.

Gao Wei, Director of the Centre for Business Promotion of ACCIO⁷⁵ in fact advises to avoid the JV: “I have had to help many Spanish firms out of the JV agreement. It is a

⁷⁵ ACCIÓ10 (that belongs to the Catalan Government) is based in Barcelona and has a network of 34 Business Promotion Centres across the globe, operating in markets spanning 70 states. “Our Business Promotion Centres provide Catalan business interested in expanding overseas qualified support, insight and advice. Many centres also offer guidance to international firms on opportunities and inward investment to Catalonia”. They have two business centres in China: Beijing and Shanghai.

very hard task, since the Chinese law normally gives all the rights to Chinese firms and nothing for the foreign ones. I advise –whenever possible- to make use of the WFOE⁷⁶,

Figure 48. Evolution of the legal form chosen by foreign firms investing in China, 2000-2004. In %



Source: China National Statistics Bureau

WFOE: Wholly Foreign Owned Enterprise. EJV: Equity Joint Venture. CJV: Cooperative Joint Venture.

Expert and consultant Emilio Mulet explains: “there is a duality in Chinese law. Their legal system is not based in the same ethics as our system. They have created laws just to satisfy the requirements of the western world (namely the WTO) but in reality they do not allow western companies to play in the same conditions as the Chinese. I have lived situations where a Spanish customer of mine was based in certain municipality, when the local government created a law just to make our life difficult”. According to him, legal obstacles remain still the main issue.

Apart from the legal difficulties explained above, there is an additional problem that all experts (and even more so business people) mention: difficulties coming from the lack of Intellectual Property Protection. Foreign companies get copied, and there is little one can do to counteract the attack. According to some of the experts

⁷⁶ The Wholly Foreign Owned Enterprise (WFOE or WFOFE) is a Limited liability company wholly owned by the foreign investor(s). In China, WFOEs were originally conceived for encouraged manufacturing activities that were either export orientated or introduced advanced technology. However, after China's entry into the WTO, these conditions were gradually abolished and the WFOE is increasingly being used for service providers such as a variety of consulting and management services, software development and trading as well. www.wfoe.org. November 2012.

consulted, the reasons why Chinese copy can be partially found in the educative system and historical reasons. On the one hand, Chinese children learn by copying, by repeating characters continuously, it is the way they were taught to learn. Follow the teacher, recite books, do not challenge. This mentality grows and sticks with people as they mature. On the other, intellectual property is seen as something free that does not belong to someone but as an achievement for all the people to enjoy. As a result, copying is considered as natural and rational, not at all negative but convenient and enriching.

Copying is nothing new in China, but it comes up as an interesting topic, compared to Westerners, especially Americans who loathe cloning. It hurts their pride and is an insult to their creativity and hard work. For Chinese, it comes as second nature and presents grand opportunity to seize a massive market potential.

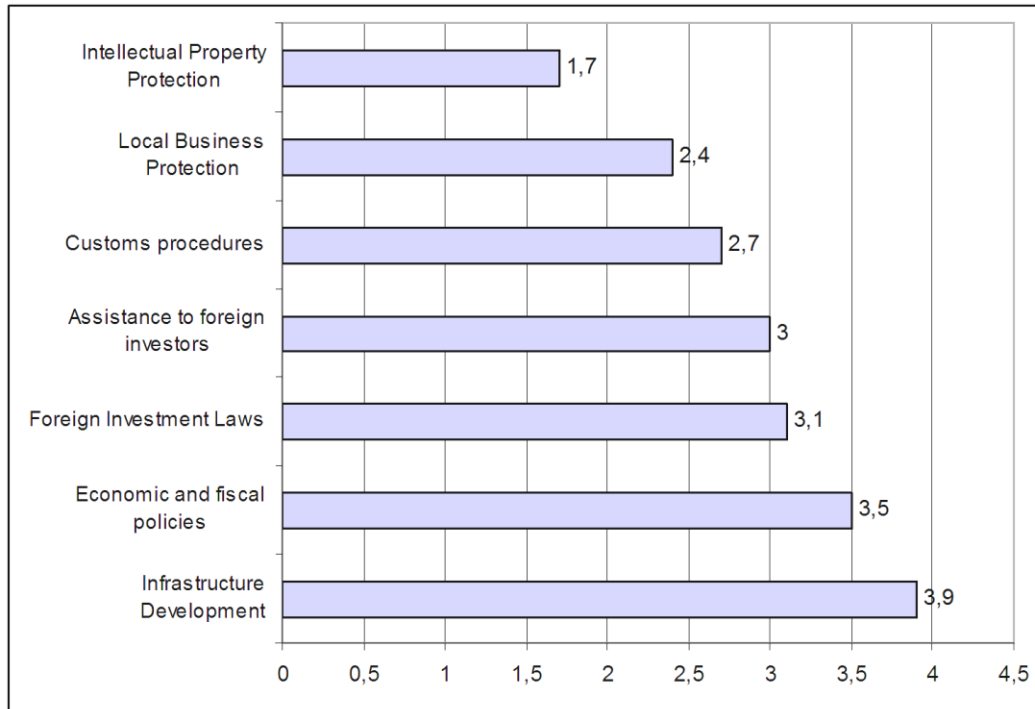
Moreover, many start-ups think, “Why shouldn’t I copy?” If the business model has been proven overseas and they know how to adapt it to China, then by not copying, it almost represents a missed opportunity. According to Peng Ong (now a Partner at GSR Ventures) co-founder of Match.com, “copying is a form of innovation. The best companies do never just copy, they copy and then localize. It’s like jazz, you have a basic rhythm and structure and you move around that. Is jazz copying? I don’t think there is any original idea. Google is a copy.”⁷⁷

We can state that the term ‘Innovation’ can be interpreted in many ways. In China, it means ‘to adapt and improve’, which is still a valid interpretation. To some degree everyone learns by copying, babies do it, adults do it. But where it becomes a sensitive subject, is when Chinese clones do not just copy the business model, they copy everything except the logo, from Nike shoes to Italian made furniture to tech start-ups, anything can be included. While in China copying is acceptable, in our Western mind-frame it is something incorrect.

How do Spanish firms rate the actions of the Chinese authorities? As we can perceive from the graph below, while economic and fiscal policies or even more so, the development of infrastructures, are welcome and highly rated, the main problems arise concerning protection. Spanish companies are unhappy about how the Chinese authorities protect their businesses and, even more, with the intellectual property protection. Even if it is true that efforts are being made to improve in this sense, there are still grounds for major improvement.

⁷⁷ TECH NODE. www.technode.com. September 2011.

Figure 49. How Spanish companies rate the actions of the Chinese authorities (values from 0 to 5)



Source: Casa Asia, 2006

According to Judith Padrós, Chinese authorities are trying develop a sounder IP protection, in order to improve the image and reputation of China. Nevertheless, she advises to register one's brand or product as soon as one gets there. She adds, "it is very cheap to do it, and it will save you from problems later on". However, in spite of her advice (which actually coincides with the advice given by all the other governmental bodies and lawyers' firms), it is well-known that many Spanish firms fail to register their intellectual property and by the time they want to do something about it, it is too late.

Joan Armenter, former Roca executive, explains their experience: "Chinese copy a lot. They are fast as well, so they copy and quickly afterwards you can find almost identical pieces in the EU marketplace". He adds: "copies are shameless. In the past, Japanese used to copy western products too, but they did it always improving and adding something. Chinese copies are shameless. Not only do they copy, but they try to confuse users by putting labels with EU made on them". However, there is very little one can do about it: "you can denounce bad practices; you can put pressure over your distributors so they do not handle copies, etc. But at the end of the day, your resources to limit damage are somehow restricted".

Experts agree that, in the first place, if one is copied, that is good news in a way: it means one's product is interesting for the Chinese market. In the second place, since protection is hampered, the best practice is being better and faster than the Chinese.

Therefore, as we can see, China is not an easy country to do business in. The World Bank publishes a very interesting index, the *Ease of doing business index*⁷⁸ that shows exactly the ranking by which countries can be considered easy / difficult.

Table 31. Ease of doing business index. World ranking (1 is the best / 183 is the worst).

Country	2009	2010
Singapore	1	1
Hong Kong (China)	2	2
New Zealand	3	3
United Kingdom	4	4
United States	5	5
Denmark	6	6
Canada	9	7
Norway	7	8
Ireland	8	9
...		
Spain	48	49
China	78	79

Source: World Bank, Doing Business Project. www.doingbusiness.org

2.3 Cultural differences

When we start a business, we are in a way playing a game. Normally, when we take part in a new sport, we need to get to know the rules to be able to play well. When establishing business relations with China, we must know certain peculiarities of its culture and negotiation that will enable us to play better. Failing to know this, can result in a great loss of time, money, energies and opportunities⁷⁹.

First, we need to know that while our culture is based on the Greeks, the Romans, the Jewish-Christian philosophy, Chinese people are ruled by a whole new set of values. Perhaps the strongest basis is Confucius. From this perspective, the individual is not important, but the group, the family, the connections. What is important is to maintain the harmony and avoid conflicts. While westerners follow natural law and fairness and justice, for the Chinese is more important to keep harmony. Relations are not egalitarian but based on power: the father over the child, the teacher over the pupil, the authority over the people. The most important aspect for the politician is not how he is going to rule, what decisions are to be taken, but to keep the order and the harmony. It is important to respect the hierarchy, the age and the status of the person we are dealing with.

⁷⁸ Ease of doing business index ranks economies from 1 to 183, with first place being the best. A high ranking means that the regulatory environment is conducive to business operation. The index ranks the simple average of the country's percentile rankings on 10 topics covered in the World Bank's Doing Business. The ranking on each topic is the simple average of the percentile rankings on its component indicators.

⁷⁹ When we talk about cultural differences, we are forced to make generalizations. Even if we try to be as objective as possible, we will probably make mistakes by generalizing.

Second, while westerners are characterised by a sequential or linear thinking, Chinese thinking is global or circular. In the west, we plan our work, even our life, by objectives in a sequential order. We negotiate following rules, objectives and we make progress as we go along. We work towards a final objective, the signature of a contract, for instance. Chinese people establish their business on trust and personal relations. The objective is not the end result but the process in itself. Therefore, points that had been decided and agreed upon come back to the negotiation table time after time. This makes negotiation processes very long. However, once we have established the relations and the mutual trust, businesses will probably be long lasting. While in the west we tend to think short-time, in the east the view is long term.

Family-directed operations

Western executives looking for the location of control of a Chinese family business should look to the head of the family. “Chances are that he or she is making all the important decisions for the business. This is especially important when the head of the family is not the same person as the business leader”⁸⁰. This family centred decision-making is frequently efficient, but according to Chen, it can lead to difficulties. Business responsibilities are often vaguely defined, and conscientious managers can feel frustrated and left out. Moreover, the lack of transparency can be discouraging to western business people who do not understand the principles by which the business family system works.

Table 32. Traditional Chinese versus western business practices

Chinese	Western
<ul style="list-style-type: none"> • Dominant purpose of company: serving family interests • Protection of financial data about company and family • Financing of company by family and other friendly families • Not for sale due to obligations to extended family • Unadvertised sale of company products, often based on family network 	<ul style="list-style-type: none"> • Dominant purpose of company: maximizing stockholder wealth • Required audits of financial reports • Financing by public sale of stocks and bonds • Mergers: unfriendly acquisitions • Brand promotion via advertising and customer service; stress on competitive market position

⁸⁰ CHEN, M. J. *Inside Chinese business. A guide for managers worldwide.* Harvard Business School Press. Boston, 2001.

Chinese	Western
<ul style="list-style-type: none"> • Senior managers recruited from within family, often by family patriarch • Stress on very long-term view of family prestige 	<ul style="list-style-type: none"> • Professional managers based on merit and attracted by money • Stress on short-run, bottom-line profits and changes in market value of stocks.

Source: CHEN, M. J. *Inside Chinese business. A guide for managers worldwide.*

Guanxi

In contrast with our western business culture, based mostly on transactions, Chinese business culture is based on relationships. A successful Chinese person is defined as a well-connected person. In this respect, the most fundamental word, studied by experts, is the concept of *guanxi*. This concept has received great media attention in the west, partially because it is a concept that has no direct translation into English, and partially because while essential to Chinese culture, it is a vague and difficult concept to understand.

It can be defined as *connections*: not just any connections but according to Chen, those “that are defined by reciprocity and mutual obligation. Ideally, these connections are also supported by a sense of goodwill and personal affection”. Sometimes *guanxi* has been viewed as a form of corruption and bribery due to misunderstanding of the Chinese culture. However, this is a wrong view of the concept.

Following Chen, “*guanxi* is grounded in trust, mutual obligations and shared experiences. The concept itself traces its roots back to ancient Chinese social customs wherein reciprocity and other modes of social exchange were used to build and maintain interpersonal relationships through society”.

Face

Face is a concept hard to understand although, even as Westerners, everyone has face. When equated to Western values, face is very similar to the notion of reputation. Face is a dynamic which applies to both personal and business relationships in China. This concept refers to always keeping the reputation of the person one is dealing with intact, especially in front of other people. The Chinese are very sensitive about this. When negotiating, one has to be extremely careful not to hurt the other person’s sensitivity, avoiding to cause others lose their face.

According to MacKinnon and Powell⁸¹, in the 70s there were four Cs that used to describe Chinese aspirations: Car – Cooler – Cooker – Console (referring to the television). Nowadays, the vital ingredients for the recipe for success in business dealing with Chinese can be framed in another set of 4 Cs, “the new four”: Cash, Clout, Connections and Culture. All of them are equally important. “We need to understand why certain ways of doing things are important to the Chinese, particularly reciprocity and the giving of face”.

Face is an accountable or bankable commodity that can be lost, can be saved and can even be lost. In situations where someone of reputation has made a mistake or done wrong, and the error is made attributable to that person in public, then that person has “lost face”: his reputation in the eyes of the others has been reduced. Losing face is an experience no-one wishes to have, therefore it is avoided at all cost.

Saving face implies a situation where someone's reputation is under question, or has already been lost, and is undergoing restoration. Saving face is an action through which one is able to prove that he was not wrong, or not as wrong as the others thought. This restoration is usually done with the help of someone else with good face: that could be called “lending face”. A person of recognised reputation is willing to support someone, endorse someone, to lend this person some of the trust he holds.

As a sociological construct, the Chinese concept of face is difficult to define. The famous writer and translator Lin Yutang (1895 –1976) even went so far as to say that “face cannot be translated or defined.” He implied that it is the delicate set of non-written norms by which Chinese social intercourse is regulated. The closest translations, on top of reputation that was stated above, are along the lines of “pride”, “dignity” or “prestige”. According to expert in Chinese culture,⁸² “the Chinese concept goes beyond the narrow Western concept of face (and is perhaps closer to the Arab concept of honor).” It is certainly interesting to know about this concept for the culture sake. But, moreover, for business, it is not just a question of mere culture, but of survival:

From the Western perspective, the Chinese are generally more sensitive to any perceived slights having to do with losing face since it's so ingrained in their culture. This cultural thin-skin is largely a product of culture that has valued social harmony as the prime rule (and generally avoided criticism). In the West, many of these slights are seen as minor and quickly forgotten. But in China, failing to appreciate face can cause serious problems. While an American business person might be respected back home for his frankness and being a “straight-shooter,” he would likely be viewed in China as uncultured, overbearing, and rude. For instance, an American subordinate attending a meeting where his boss is presenting would generally think nothing of raising a question, making an alternate suggestion, or even

⁸¹ MACKINNON, A.; POWELL, B. *China Calling. A foot in the global door*. Palgrave MacMillan. New York, 2008. (p. 94-95).

⁸² CHINA MIKE. Website on Chinese culture www.china-mike.com. May 2012.

disagreeing in front of others. In China, this would be a serious face-losing situation for the subordinate, boss, and even the company.

Negotiation differences

Negotiating with Chinese follows different rules to our western system. For instance, the choice of words is important when communicating with a Chinese person, as misinterpretation will lead to misunderstanding. It is also recommended to read between the lines, for double or hidden meanings. Although Chinese people do not deliberately hide the truth, they frequently do not say it openly in the same way as westerners do. Another difference is that Chinese often bring in new people during negotiations, or reopen subjects that seemed to be closed. This makes negotiations longer than one would have expected. The Chinese are process-oriented and seem to enjoy very long discussions. The main differences are listed on the table below:

Table 33. Differences in the negotiation process western versus Chinese

Chinese	Western
<p>The group is most important Hierarchical Decisions based on relations and trust</p> <p>Process-oriented</p> <p>The way is the goal Meetings are long combined with leisure activities Good things take time Negotiation process is continuous Relationship-oriented Never lose face</p> <p>Formality and protocol in relations</p> <p>Mutual consensus</p> <p>Use of mediators</p>	<p>Individualist Egalitarian Decisions based on cold facts</p> <p>Result-oriented</p> <p>Final goal is important Meetings are short and to the point.</p> <p>Time is money Negotiation process is limited Fact-oriented Get quickly to the goals</p> <p>Informal relations</p> <p>Efficiency</p> <p>Cold phone calls</p>

Source: Own research plus INTERNATIONAL JOURNAL OF CHINESE CULTURE AND MANAGEMENT. The importance of the cultural dimension when doing business in China. 2008.

Risk avoidance

Chinese avoid risk, which is a natural result if our foremost intention is to keep harmony. Chinese children at school spend most of the time copying: education is to certain extent based on the repetition of the characters. Talking in public, or being creative are activities which are not especially encouraged. Therefore people tend to

be very conservative, avoid risk and expect orders or very detailed instructions on how to perform tasks.

On the other hand, Chinese people do not like to say “no”. In the western negotiation style, business people say no whenever necessary and will expect the same from their opponents. But for a Chinese person saying no is rude, so he (she) will prefer to divert the answer making it more vague. It is not convenient to force them to a “no”, because that may make them lose “face”.

2.4. Uncertainty and ambiguity

While it is certainly possible to succeed in business in China, it is necessary to proceed with caution. One cannot just take the usual way of doing business and apply it in China. It is important to take into account that the global corporate model will not necessarily fit here. “It is not good parachuting a few people in from elsewhere, no matter how good they are, and then have them move on after a little while, because things move so fast here and expectations are so high, clients want to be able to get answers to questions immediately”, commented business man Bill Austin of Halcrows giving his point of view for the China Briefing publication⁸³.

Westerners doing business in China need to learn to live with degrees of uncertainty somewhat greater than one does in his own country. This applies in many areas. Building relationships is important, but they are not primarily based on written contacts. China is more subtle than that. This is not just a question of language, difficult as it is. “Although speaking Chinese is an important step toward more effective communication, it is not the total solution, especially in China, where communication is as much about context as content. It’s not enough just to know what to say, but how to say it”⁸⁴. As Deng Xiao Ping said: “for most foreigners, China is and will continue to be a rushing river that must be crossed by carefully feeling for stones”.

Regulatory uncertainty is a large part of this. Companies have to confront a moving target when it comes to making sure they are compliant with relevant regulations, many of which have not yet been created.

Significant vestiges of the planned economy and the attitudes that go with it, still remain. Navigating the bureaucracy and getting things done are not as straightforward as one may think. In addition, local governments and development zones in many areas are often simply not as internationally experienced as they are

⁸³ CHINA BRIEFING MEDIA. *Business Guide to Shanghai and the Yangtze River Delta 2006-2007. China Briefing, the practical application of China business.* China Briefing Media Ltd. Dezan Shira China group. Hong Kong, 2007.

⁸⁴ CHINA BRIEFING MEDIA. *Business Guide to Shanghai and the Yangtze River Delta 2006-2007. China Briefing, the practical application of China business.* China Briefing Media Ltd. Dezan Shira China group. Hong Kong, 2007.

in Beijing, Shanghai, Tianjin or Guangdong. This will change and improve with time, experts agree, but in the meantime it is necessary to be aware of this fact.

One way of reducing business uncertainty has been cultivating good relationships with government agencies and business partners. The old patterns of *guanxi* remain in place. Large reserves of patience and perseverance are amongst the fundamental qualities one needs to do business in China (as we will confirm in the next chapters). However, there are signs that show that modernisation is taking place and more progressive and pragmatic practices are becoming usual: “while international standards are still a long way off, there is an increasing transparency in China, and improvements in rule of law that are providing a much more level playing field than companies have witnessed in the past” was what PR experts from Ogilvy commented for the China Briefing guide. As a matter of fact, the ground is shifting from *guanxi* into more pragmatic and accountable habits.

2.5 Difficulties to access talent

Firms that are doing business in China coincide that it is very difficult to recruit human capital in China. Moreover, once you have an employee on the pay-roll, it is very hard to keep him or her: it is common to move to another company to earn a bit more. Since salaries are growing so fast, employee turnover is soaring.

It is also difficult to find staff with certain knowledge of English or other foreign languages. Chinese employees who have studied abroad are rare and actively sought for. The result is a very high rate of *cannibalism* among western firms, all competing to recruit the same people.

One of the gaps western firms encounter often is the weakness in people’s skills, as we are used to finding in the West. China is an environment where workers are often single-skilled. Therefore, we need to adapt our manufacturing techniques, business models and practices to the available skills (and not the other way round). Service skills are often missing. It is also often commented that the education system and the Chinese society in general do not encourage initiative. Some people have it, some don’t.

The image of “Made in China” has changed enormously. According to Gao Wei, Director of the Promotion Centre of ACCIO in Beijing, Made in China used to be a symbol of bad quality, but not any more. “Quality has improved a lot. Of course there are still low quality products but in certain sectors they are capable of making a good product indeed”.

2.6 The brand “Spain” in China

The question to be answered is the following: is the brand of Spain today well known in China? The answers are multiple, from the absolute optimism and triumphalism to the most extreme pessimism. One could measure the brand of the country by the

image of its products, its companies and their businessmen and women, by its weight in the economy and in the trade, by the efforts made by the governments to promote their image, or even by their sports and sportsmen.

To start with a positive side, Spain is quite known in China by its commercial brands such as Zara or Alsa, or by the large corporations, such as Telefonica, Santander or BBVA. It is also known in certain high-tech sectors such as engineering, architecture, renewable energies, intensive farming equipment, machine-tools, etc. or even by the official Spanish Pavilion at the Expo in Shanghai in 2008 (one of the most visited pavilions, by the way). It is also known by the sports, like tennis or football and also by the gastronomy, culture, way of life and music.

However, there is unfortunately a negative side that shows the limited power of the image of Spain in China. Only one out of 1,100 foreign businesses in China is Spanish. China only buys 0.4% of its imports from Spain. Spain is only the country number 31 in the ranking of investors in China. We could continue citing different factors that show basically that Spain – number 12 or 13 in world GDP- does not hold that position when it comes to business in China. The reason behind is that, deep down, Spain is not convinced of the importance of this market. There is not a frame of mind that pushes businesses and policy towards a priority: China as the main growing world market. It seems urgent to get to know this vast country as soon as possible and act on it.

According to Marcelo Muñoz, consultant and business man operating in China since 1978 and author of different books on how to do business in China, there exist three lines of action that should be urgently tackled in order to improve the brand of Spain⁸⁵:

1. Improve the efficiency in all the promotional actions carried out by the public institutions and organisms operating in China. Quantify accurately how much is invested in each one of the activities: political promotion trips, business trips, visits and participation in trade fairs, representation offices of the different autonomous delegations, etc. Evaluate each one of these activities to know exactly how they have contributed to the brand of Spain, to the exports, to create wealth, employment, to establish a distribution channel, to increase sales, etc. This exercise would show which actions are actually being inefficient while other are worth reinforcing. It would be an exercise of transparency and efficiency.
2. Promote the exchange of students. It is estimated that there are one million Chinese students all over the world outside China, but only six thousand are actually in Spain. Each one of them can become an ambassador of Spain in his or her country when coming back.

⁸⁵ MUÑOZ, M. *España en China: ¿Tenemos marca país o no?* GLOBALASIA. *World Economic Forum*. Num. 24, marzo-abril 2012. Revista Económica, empresarial, tecnológica y cultural. Global Asia. P24-28.

3. Prioritize objectives by sectors: food, renewable energies, tourism, distribution, or even more concrete sub-sectors: wine, olive oil, etc. In this regard, he detects tourism as the largest opportunity, first, because it is Spain's strongest activity and, second, because it contributes directly to act on the brand of Spain. In tourism, Spain has a great deal of experience. The total number of Chinese tourists towards the world reached 70 million people in 2011 and the number will extent to 100 million by 2015, according to the WTO. However, only 100,000 of them come to Spain. Interesting enough, the profile of these tourists is persons who enjoy culture, visit cities, go shopping and, in general, have one of the highest spending levels. The Spanish offer has what it takes and could become one of the strongest brands if public and private efforts and united in the right direction.

To summarize, even if it is true that the brand of Spain has gained visibility and positions in the last years, there is certainly ground for improvement. Perhaps the first change that needs to take place is in the minds of the influential Spanish people (politicians, business people) to really believe in the importance of this market.

2.7. Difficulties to access distribution channels

Concerning distribution, expert in Asia Xavier Espasa explains that the main problem in China is the distribution channels: strategic sectors such as telecom, car industry, aeronautical, infrastructures or the military are over protected. Foreign companies cannot access these markets without a Chinese partner.

On the other hand, consumer goods require that the Spanish firm establishes the whole distribution channel, which is extremely expensive. The figure of the importer / stocker / distributor, as we know in Europe, does not exist. Therefore, the foreign firm has to create the whole distribution by itself: this is very costly.

2.8 How to tackle such a vast country?

Chinese firms willing to enter the European market often make the same mistake: they consider the EU as one large market, without taking into consideration national and regional differences. From our European perspective, this seems like an obvious observation. However, when it comes to accessing the Chinese market, European firms often make exactly the same mistake: they try to handle it as one huge marketplace.

According to all experts consulted on the matter,

1. China is a huge country, both geographically and in terms of population. Therefore it is impossible to try to cover the whole country at once. However, in spite of this fact being obvious, it becomes the temptation for all foreign companies: huge country and huge population, sales assured. Reality shows that efforts should at first concentrate in certain geographical areas.

2. Apart from being very large, and contrarily to what many people think, it is also heterogeneous. There exist deep differences of taste, income, habits, culture, etc. between the coast versus the interior provinces; urban and rural, North-South, etc.
3. The distribution channels are not very mature or developed enough at national level. But they do work better at a local level. Therefore, it is better to focus on one geographical area and grow in stages.
4. Since access to the whole marketplace is out of reach, it is advised to find a niche in the market and exploit it. Chances are it will be large enough to yield fruitful results.

China, like Europe, is a very diverse economy, as evidenced by an analysis of per capita GDP in PPP terms of its different provinces. "With the lowest estimates of PPP, three provinces (43 million inhabitants and 10% of Chinese GDP) would have a GDP per capita at least as high as five EU member states in terms of PPP. With a higher estimate of the PPP, nine provinces (420 million inhabitants and 55% of GDP in China) have a GDP per capita higher than the 14 EU member states, equalling that of Shanghai to Greece and the Fujian to Bulgaria"⁸⁶.

⁸⁶ ICEX, *Country Guide: China*. Updated May 2010

V. SPANISH BUSINESS STRUCTURE

After studying an introduction to China and its main macroeconomic prospects, it is time to take a look at Spanish businesses. These are the questions we are going to try to answer: in the first place how many firms are there, what is their profile, sectors they operate in, size of the firms, geographical location, etc. Afterwards, we will analyse with more detail the profile of the exporting businesses in Spain. Finally, we will make a brief summary of their main difficulties. We would like to note at this point that the purpose of our work here is not to analyze in depth the structure of Spanish businesses, which would be the objective of a reasearch on its own, but to make a general and summarised picture so the reader can understand later on the difficulties accessing the Chinese market.

In the last years, the world economy has suffered from a general deterioration, aggravated by the high uncertainty about the solvency of some financial entities. World trade has fallen, real estate market adjustments have been acute, and growth expectations are somehow limited. In this world environment, perspectives for the Spanish economy are pessimistic, with low confidence indicators for both consumers and businesses. The most worrying effects of the recession fall on the unemployment rate, at 24.4% in the first quarter of 2012.⁸⁷ Job destruction, which started mainly in the construction sector, has extended to industry and services. Households' disposable income has been reduced and families, worried about the general economy uncertainty, have increased their savings. As a result, domestic demand has fallen and the economy has reduced its pace.

1. Spanish businesses, mostly SMEs

Spain is a country made of SMEs: businesses, comprised in the definitions of micro-firms, small firms and medium-sized firms, that occupy a maximum of 250 employees and whose sales do not exceed 50 million euros⁸⁸. We choose to select this definition because it is an accepted one within the EU, which will enable us to make comparisons amongst European countries.⁸⁹

⁸⁷ INE. Spanish Statistical Institute. www.ine.es. June 2012.

⁸⁸ SMEs are **defined by the European Commission** (Eurostat) as having less than 250 persons employed. They should also have an annual turnover of up to EUR 50 million, or a balance sheet total of no more than EUR 43 million (Commission Recommendation of 6 May 2003). These definitions are important when assessing which enterprises may benefit from EU funding programmes aimed at promoting SMEs.

⁸⁹ Businesses are classified by size following the following criteria, agreed by the EU Commission and the EU Country Members:

- micro enterprises: with less than 10 persons employed;
- small enterprises: with 10-49 persons employed;
- medium-sized enterprises: with 50-249 persons employed;
- small and medium sized enterprises (SMEs): with 1-249 persons employed;
- large enterprises: with 250 or more persons employed.

Within the EU there are over twenty three million SMEs. They represent an important source of employment creation and innovation. They determine productivity in the EU, since they are the best at detecting the needs of the final user as well as the industry, at adopting new technologies, transferring the know-how, training their employees and finally, contributing to local development. SMEs represent more than 99% of the total number of businesses, employing over 75 million people in the EU.

According to the Central Directory of Businesses (DIRCE) in Spain on the 1st of January 2011 there were 3.25 million businesses, of which 99.88% are SMEs (between 0 and 249 employees).

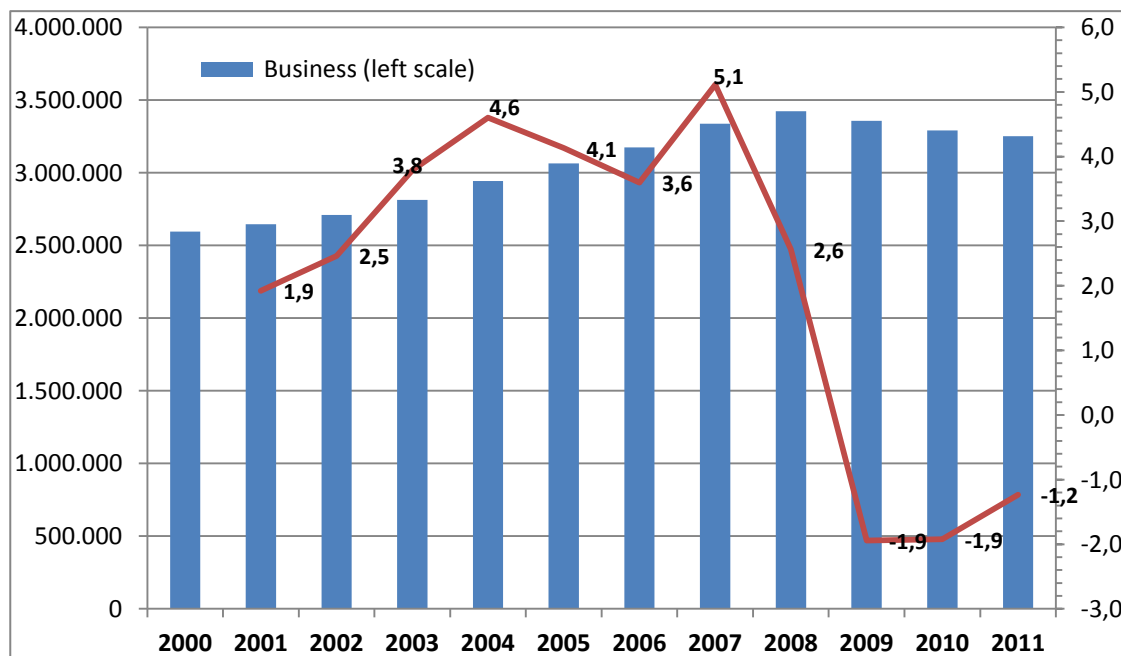
Table 34. Spanish businesses by size, 2011 (in absolute numbers –Spain- and in percentage - EU and Spain

	0 employees	Micro 1-9	Small 10-49	Medium 50-249	SMEs 0-249	Large 250+	Total
Spain	1,793,878	1,297,971	130,448	20,888	3,243,185	3,801	3,246,986
Spain %	55.2	40.0	4.0	0.6	99.9	0.1	100
EU-27 %	92.1		6.6	1.1	99.8	0.2	100

Source: INE, DIRCE, 2011 and European Commission.

The percentage of SMEs is slightly higher in Spain compared to the EU average. Between 2000 and 2010 the number of firms has increased in more than 650,000 which is an increase of 25% in that period.

Figure 50. Evolution in the number of businesses in Spain and annual variation. In %



Source: INE, DIRCE 2011.

As we can see, the size group with most business is concentrated in firms with no employees. In 1995 this group represented 57.6% of the total businesses. By 2010 their weight had decreased down to 55.2, a converging trend towards the EU. Unfortunately, the economic recession gives a again a heavier weight to those business without salaried staff (due to employment destruction).

In 2010 the number of SMEs decreased by 1.23%. Even if the structure of businesses is mainly made of SMEs, small ones are most predominant. This size makes them especially vulnerable when facing an increasing competition and the changes that are hapenning in today's global markets.

Regarding employment, SMEs employ in Spain 76.4% on the total employment, ten points more than the EU average (66.7%). Only Greece, Italy of Portugal, all southern European countries, have higher percentages of SME employment within the EU.

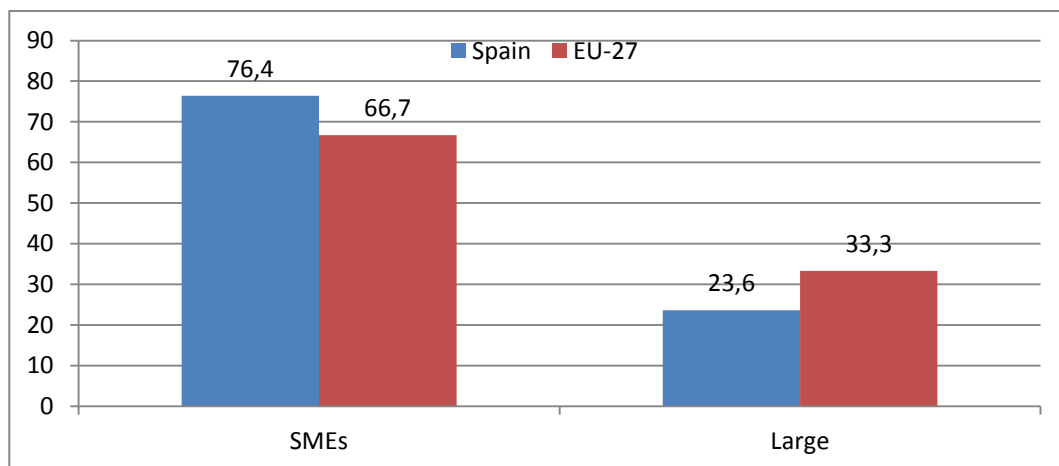
Table 35. Employment by businesses size, 2010, in Spain and the EU. In %

	Micro (0-9)	Small 10-49	Medium 50-249	SMEs 0-249	Large 250+	Total
Spain %	38.9	22.8	14.8	76.4	23.6	100
EU-27 %	29.0	20.5	17.2	66.7	33.3	100

Source: Eurostat.

Large Spanish businesses account for 23.6% of the employment, while it reaches one third in the EU.

Figure 51. Employment by business size: comparison Spain with the EU-27, 2010 (%)

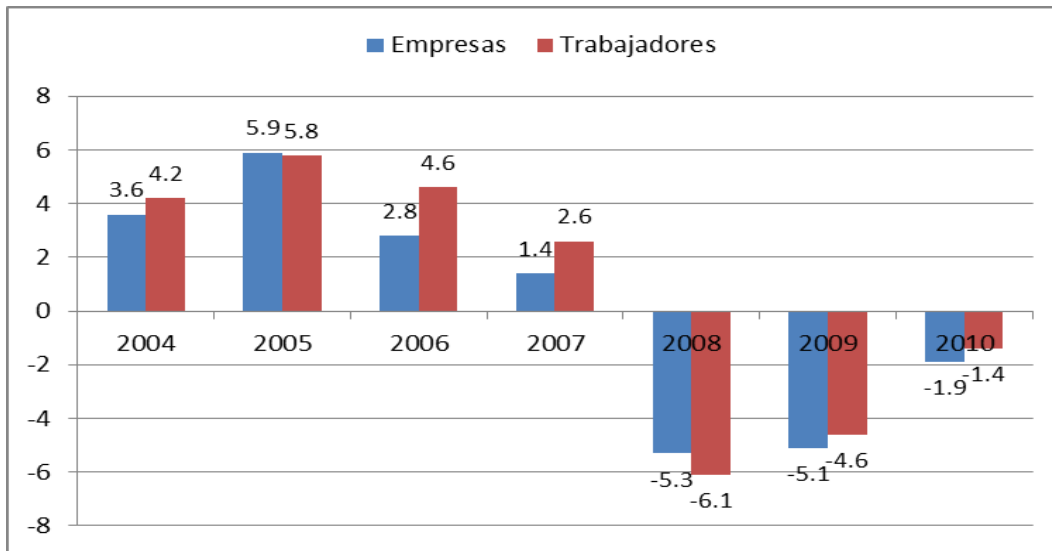


Source: Eurostat

Below, we can see the evolution of the number of firms and persons employed (as registered by the Social Security). Until 2007 the trend was to grow both the number of firms as the employment, especially in 2005 where both indicators grew by almost 6%. In 2008 the results of the economic recession start to become apparent, especially 2008 that was the worst years with employment falling in more than six

points. Although 2010 and 2011 present negative growth rates, the rhythm of the losses have diminished.

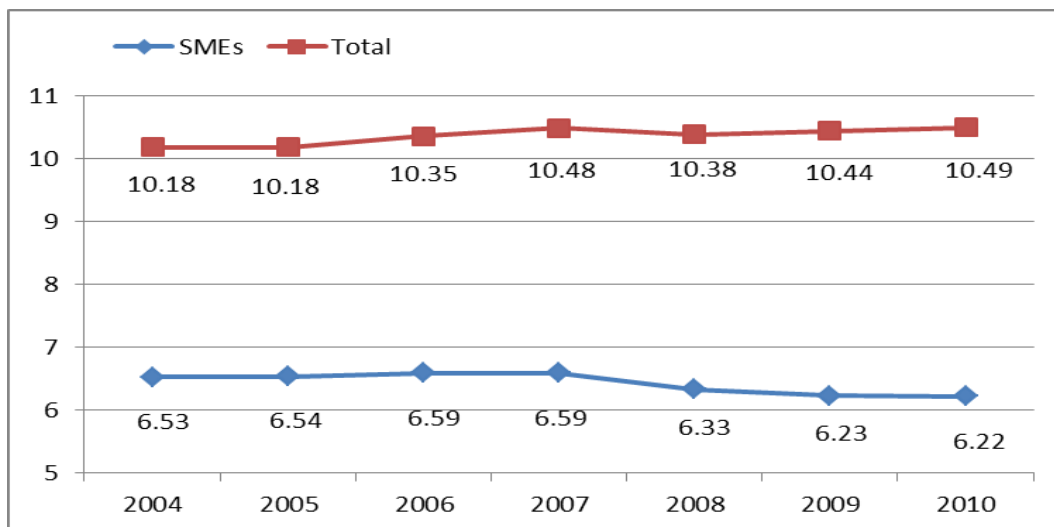
Figure 52. Evolution of the number of businesses and persons employed, Spain (2004-2010). Annual variation (in %)



Source: Spanish Social Treasury.

In terms of size, the smallest firms have lost the most employment within the SMEs. Moreover, SMEs have lost more employment than large companies. Below we can see the evolution of the average size of firms: SMEs employ on average 6.22 persons; all firms on average employ 10.49. In the last years, the evolution of employees has on average increased slightly. However, SMEs have seen their average size decrease (since 2008).

Figure 53. Evolution of average number of persons employed, by SMEs and by all firms. Spain (2004-2010)



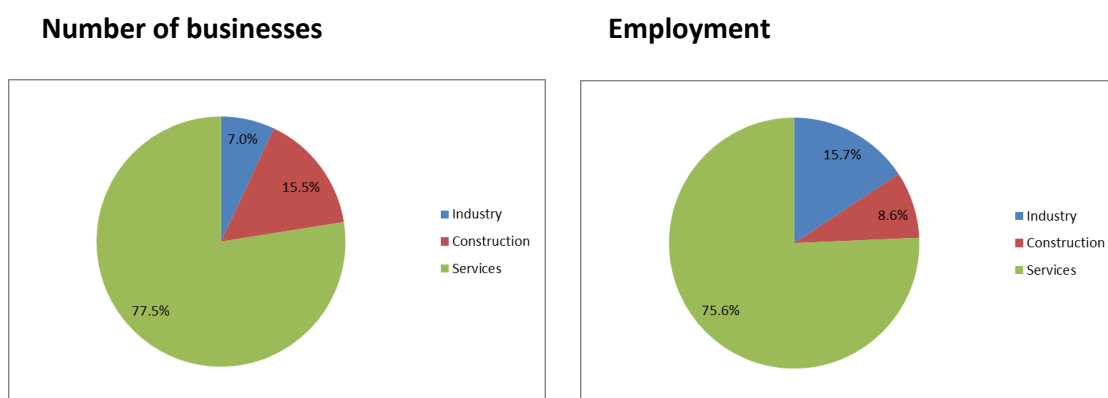
Source: Spanish Social Treasury.

The size of the businesses differed greatly by sector: most large firms are concentrated in the industry, while the smallest ones are found in services and retail.

2. Spanish businesses, mostly in services

If we said before that the weight of Spanish firms is mostly in SMEs, in terms of activities, services is the sector that concentrates most firms. As we will see in chapter 6, this coincides with the presence of Spanish firms in China, also mostly in services. For the purpose of this exercise, it is unnecessary to go further details.

Figure 54. Number of businesses and employment by sector, Spain, 2010



Source: INE, DIRCE, Social Security, and own calculations.

3. Spanish businesses by geographical structure

The regions or Autonomous Communities that have most businesses are Catalonia, Madrid, Andalusia and Valencia, these four regions accounting for 60% of the total firms:

Table 36. Number of businesses by regions, Spain 2010

Number of firms by Autonomous Community	Nb. Firms	% Total	Variation 2009/10 %
Andalusia	498266	15.2	-2.2
Aragon	92052	2.8	-1.1
Asturias	70292	2.1	-2.0
Balearic Islands	89443	2.7	-2.4
Canary Islands	135713	4.1	-2.4
Cantabria	38924	1.2	-1.5
Castille-Leon	168814	5.1	-1.0
Castille- La Mancha	131731	4.0	-1.9
Catalonia	609046	18.5	-1.6
Valencia	352012	10.7	-2.8
Extremadura	65487	2.0	-2.3
Galicia	198705	6.0	-1.2

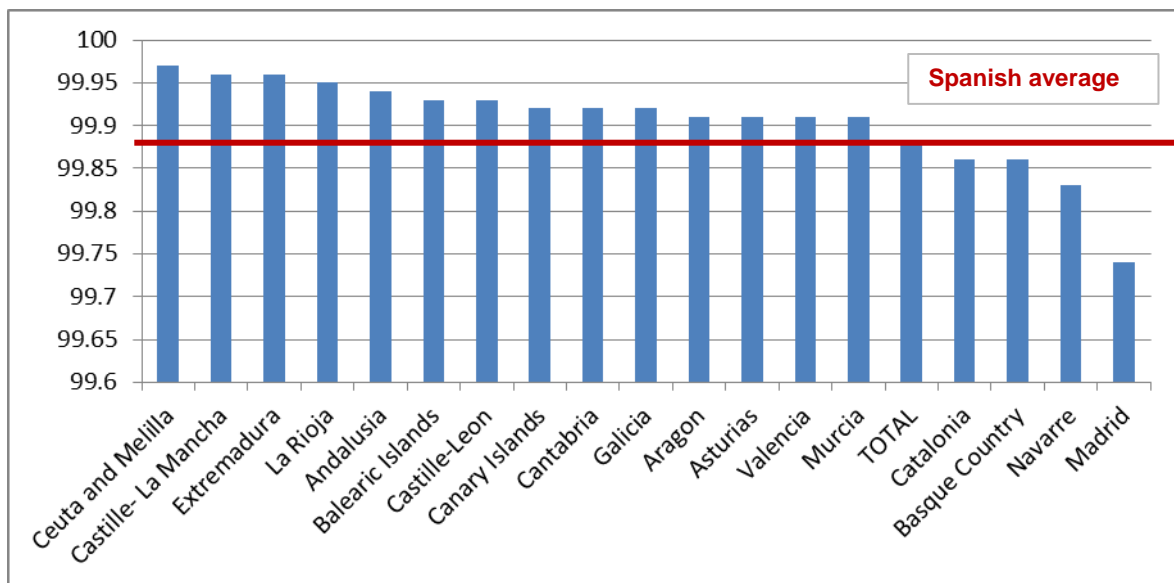
Number of firms by Autonomous Community	Nb. Firms	% Total	Variation 2009/10 %
Madrid	502973	15.3	-1.6
Murcia	92086	2.8	-3.5
Navarre	42268	1.3	-1.9
Basque Country	169206	5.1	-1.3
La Rioja	23106	0.7	-1.4
Ceuta and Melilla	7250	0.2	-1.2

Source: INE, DIRCE

The regions where the number dropped more in the last year was Murcia (-3.5%) and Valencia (-2.8%). The total number of business went down by 1.9% in Spain as a whole.

Spain, as stated before, is a country made of mostly small and medium-sized businesses. The regions that concentrate most large firms are those where the industry represents a heavier weight on the economy: Catalonia, Basque Country, Navarre and Madrid. The figure below shows the weight of SMEs on the total number of businesses, by region.

Figure 55. Percentage of SMEs on the total number of businesses, by region, compared to Spanish average, 2010. In %



Source: INE, Dirce and own calculations.

In terms of employment, the four regions with most firms concentrate also over 60% of the total employment: Catalonia, Madrid, Andalusia and Valencia.

Table 37. Number of persons employed by regions, Spain 2010

Persons employed by Autonomous Community	Employment (thousands)	% Total	Variation 2009/10 %
Catalonia	2,455.3	18.6	-5.2
Madrid	2,386.9	18.1	-4.2
Andalusia	1,818.8	13.8	-4.5
Valencia	1,280.6	9.7	-7.2
Galicia	729.1	5.5	-3.5
Basque Country	722.8	5.5	-3.0
Castille-Leon	680.8	5.2	-2.4
Canary Islands	561.9	4.3	-6.4
Castille- La Mancha	499.7	3.8	-3.8
Aragon	413.9	3.1	-3.8
Murcia	351.2	2.7	-6.8
Asturias	292.5	2.2	-2.4
Balearic Islands	273.7	2.1	-5.8
Extremadura	240.7	1.8	0.2
Navarre	207.3	1.6	-3.6
Cantabria	160.5	1.2	-3.3
La Rioja	89.2	0.7	-4.4
Ceuta and Melilla	31.9	0.2	0.8

Source: Social Security

Madrid is the region where the average number of employees is the highest (with 13) followed by the Basque Country, Navarre (almost 12), and Catalonia (10.5). These are the areas also where most industry is concentrated (industrial businesses are generally larger than services).

Table 38. Average size of firms by regions, Spain 2010.

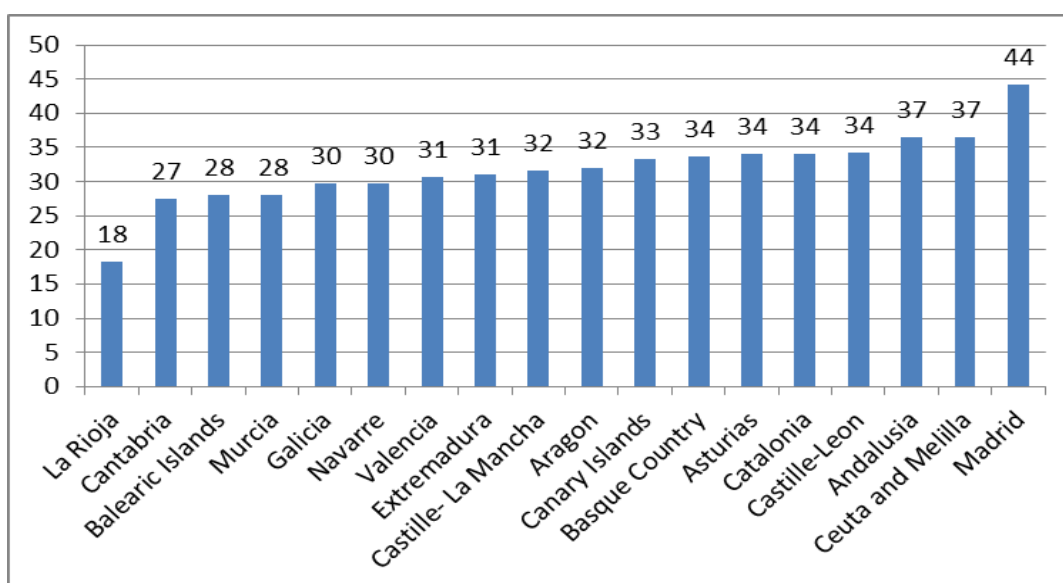
	Average nb. of workers per business	of which % SMEs	of which % Large
Andalusia	9.1	63.5	36.5
Aragon	9.7	68.0	32.0
Asturias	9.5	66.0	34.0
Balearic Islands	7.9	72.0	28.0
Canary Islands	9.8	66.7	33.3
Cantabria	9	72.6	27.4
Castille-Leon	9.3	65.7	34.3
Castille- La Mancha	9	68.4	31.6
Catalonia	10.5	66.0	34.0
Valencia	9.1	69.3	30.7
Extremadura	9	69.0	31.0
Galicia	8.6	70.3	29.7
Madrid	13	55.8	44.2
Murcia	8.9	71.9	28.1

	Average nb. of workers per business	of which % SMEs	of which % Large
Navarre	11.5	70.2	29.8
Basque Country	11.7	66.3	33.7
La Rioja	8.3	81.7	18.3
Ceuta and Melilla	9.7	63.5	36.5
Total	10.4	59.5	40.5

Source: Social Security.

Only in one area, Madrid, over 40% of the employees are employed by large firms. It shows that large businesses concentrate around the capital, which works as a magnet for many headquarters and multinationals.

Figure 56. Percentage of workers employed by large firms (%), Spain, 2010



Source: Social Security.

We shall now briefly compare the differences in productivity by Autonomous Community (the average for Spain being = 100).

Table 39. Productivity: GDP per person employed. Spain = 100, 2010

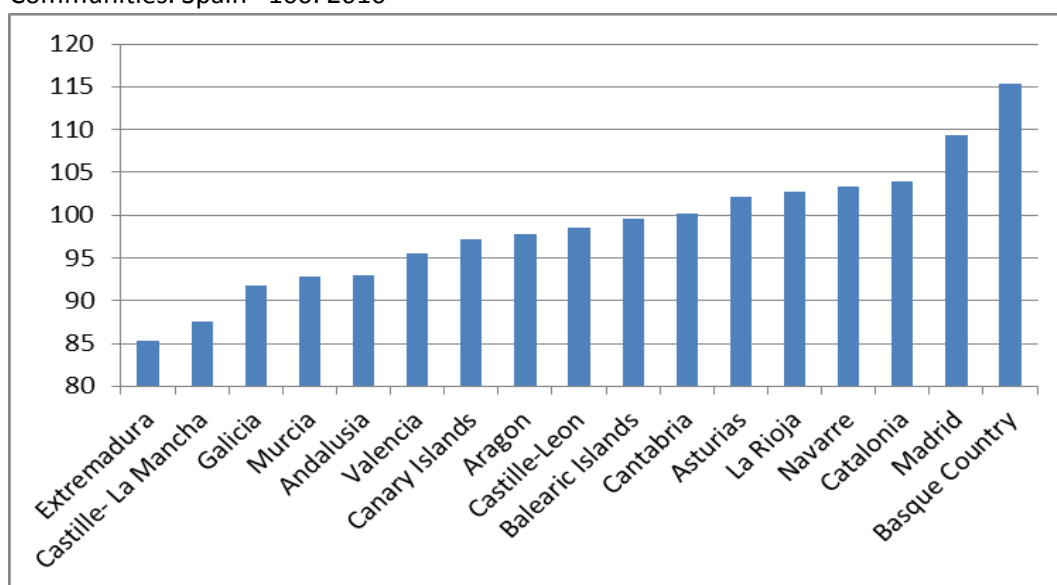
	GDP per worker Spain=100	Annual variation (%) 2009/10
Andalusia	92.9	4.1
Aragon	97.8	2
Asturias	102.1	0.2
Balearic Islands	99.6	2.9
Canary Islands	97.2	6.4
Cantabria	100.2	2.8
Castille-Leon	98.5	2.4
Castille- La Mancha	87.6	4

	GDP per worker Spain=100	Annual variation (%) 2009/10
Catalonia	104	2.9
Valencia	95.5	1.4
Extremadura	85.3	4.3
Galicia	91.8	0.3
Madrid	109.3	1.3
Murcia	92.8	6.7
Navarre	103.3	4.8
Basque Country	115.3	1.9
La Rioja	102.7	0.4
Total	100	3.1

Source: INE. Regional Accounts (CRE).

Productivity in Spain was almost 60,000 euros per person employed in 2010. The regions with highest productivity are the Basque Country, Madrid and Catalonia, with levels well above the average, as it can be appreciated in the graph below. The lowest ones corresponded to Extremadura, Castille-La Mancha and Galicia, the regions with least industrial development.

Figure 57. Productivity measured by GDP per person employed, by Autonomous Communities. Spain= 100. 2010



Source: INE. Regional Accounts (CRE).

4. Main characteristics of SMEs

Since the main characteristic of Spanish business structure is the strong predominance of SMEs, let's contemplate which their chief characteristics are. In the first place, their main peculiarity is their flexibility, that is, in itself, very often their competitive advantage. Flexibility understood as the ability to adapt the production

according to the fluctuations in the demand and according to the change in users' tastes and needs. SMEs normally have a light cost structure, superior responsiveness and innovation skills.

On the low side, SMEs often have difficulties to access domestic capital markets. Their lack of financing stops those small firms from investing in new technologies and new talent. Moreover, frequently, their total turnover and their low purchasing power do not allow them to negotiate the best conditions with customers and suppliers. To overcome this difficulty, they can sign long term contracts with such suppliers and customers, based on trust and mutual cooperation, so as not to erode their competitive advantage.

The table below compares the advantages and disadvantages SMEs find when competing with large businesses.

Table 40. Advantages and disadvantages of SMEs.

SMEs	
Advantages	Disadvantages
Flexibility	Difficult access to financing
Ability to adapt	Scarce resources
Responsiveness	Low negotiation power with customers and suppliers
Light cost structure	
Ability to innovate	
Large Businesses	
Advantages	Disadvantages
Economies of scale, economies of scope	Structural Inertia
Resource availability	Heavy and bureaucratic organizational structure
Own resources	

Source: FERNÁNDEZ, Z. AND NIETO, M.J.⁹⁰

SMEs are able to develop dynamic capabilities to generate new knowledge, alter their environment or react quickly to unforeseen changes. Innovation, learning and flexibility are sources of competitive advantage in all sectors, even more than the strong possession of resources or the negotiating power by volume. SMEs are prepared from the strategic point of view to focus on a market segment adapting its supply to the specific needs of that set of clients. SMEs are characterized by the concentration of capital, which implies the direct control of the property over the management, coinciding therefore the objectives of the direction with the property. The possibility of having demanding, well informed and stable shareholders, that control the company internally and have access to more information, allows SMEs to deal with risky investments that a large company would be slowing down by

⁹⁰ FERNÁNDEZ, Z.; NIETO, M.J. *Strategies and structure of SMEs. Can a small size become a competitive advantage?* Papeles de Economía Española, nb. 89-90. 2001.

different steering committees. Decision making is much more agile, not being necessary to wait for the boards of directors to reach an agreement that involves a very large group of people.

In terms of international trade, SMEs generally have a higher level of exports and greater diversification. The activities of R&D are more frequent and they undertake more initiatives aimed at the differentiation, whether through advertising and marketing or through product innovation.

In times of economic crisis, as the current one, SMEs miss the strategic planning, which is what really allows businesses, perhaps not to only predict the future, but be ready to deal with it. Strategic planning has evolved from the position to develop visions and strategic objectives, to face what is happening in the environment. To do this, large companies have central departments that allow them to address this aspect of the business. The question now is what happens in SMEs, who plans in SMEs. In this respect, there has been a significant evolution in recent years. Management has moved from strong entrepreneurs who did not have higher education in administration, to a more professional management style.

Spanish SMEs do not generally use strategic planning. The reasons given in different surveys are: lack of time, it is not considered needed due to small size, and is a long and expensive process. Furthermore, the lack of time translates into lack of knowledge and an excess of confidence in one's own abilities. The leaders believe that the planning is less urgent than the day-to-day running of the business. The length in time of the process and the cost translates into the same as lack of time: ignorance.

It is clear that the strategic planning in family-run SMEs is necessary and also that in some cases, their leaders are not prepared to do so. Some consultants accompany SMEs in this process, creating a series of easy-to-use planning tools that are designed especially for them. In addition, during a reasonable period of time, the so-called learning curve must accompany SMEs so that they can obtain the expected yields and cope with future developments, given current trends, with a higher degree of trust and security.

5. Spanish exporting firms

We shall first analyse briefly Spanish Foreign Trade. Spain occupies the 7th position of the ranking of EU exporters. Its position is quite naturally behind large countries such as Germany, The United Kingdom, France and Italy. But it is also behind other smaller, but more internationalized countries, like the Netherlands or Belgium.

On the other hand, it occupies exactly the same 7th position in terms of imports, after the same countries as mentioned before. The Spanish trade balance is negative, but the difference shifting more favourably towards Spain. While imports increased by 12.8% in 2010, exports went up by 13.7%. The weak internal demand is surely one of the reasons for this difference. Therefore, we can foresee a positive evolution of the trade balance.

Table 41. Imports and exports of the EU countries and some main partners.

	Exports			Imports			Balance	
	2009	2010	2009-10 growth rate (%)	2009	2010	2009-10 growth rate (%)	2009	2010
EU-27 (1)	1,097.1	1,348.8	22.9	1,206.5	1,501.8	24.5	-109.3	- 153.0
Belgium	265.2	310.9	17.3	252.3	294.5	16.7	12.8	16.4
Bulgaria	11.7	15.6	33.3	16.9	19.2	13.5	-5.2	-3.6
Czech Republic	81.0	100.2	23.7	75.3	95.2	26.4	5.7	5.0
Denmark	67.3	73.7	9.4	59.3	64.0	8.0	8.1	9.7
Germany	803.0	957.1	19.2	664.1	804.7	21.2	138.9	152.4
Estonia	6.5	8.8	34.9	7.3	9.2	27.1	-0.8	-0.5
Ireland	83.1	88.1	6.0	45.0	45.3	0.7	38.2	42.8
Greece	14.7	16.1	10.0	49.8	47.7	-4.3	-35.1	-31.5
Spain	163.0	185.3	13.7	210.2	237.1	12.8	-47.2	- 51.8
France	347.4	392.7	13.0	401.5	456.9	13.8	-54.1	-64.2
Italy	291.7	337.6	15.7	297.6	365.0	22.6	-5.9	-27.4
Cyprus	0.9	1.1	18.2	5.6	6.4	14.1	-4.7	-5.3
Latvia	5.5	7.2	29.7	7.0	8.7	24.6	-1.5	-1.6
Lithuania	11.8	15.7	33.2	13.1	17.7	34.5	-1.3	-1.9
Luxembourg	15.1	14.8	-2.3	17.6	18.1	2.9	-2.4	-3.3
Hungary	59.5	72.0	21.0	55.8	66.5	19.2	3.8	5.5
Malta	1.6	1.9	18.4	3.0	3.2	6.2	-1.4	-1.2
Netherlands	357.0	432.5	21.2	317.7	389.9	22.7	39.2	42.6
Austria	98.2	114.9	17.0	102.6	119.8	16.8	-4.4	-4.9
Poland	97.9	117.5	20.0	107.2	131.0	22.2	-9.3	-13.5
Portugal	31.8	36.8	15.7	51.4	57.1	11.1	-19.6	-20.3
Romania	29.1	37.3	28.1	38.9	46.8	20.1	-9.9	-9.5
Slovenia	18.8	22.2	18.4	19.0	22.7	19.2	-0.2	-0.4
Slovakia	40.2	49.3	22.6	39.9	50.2	25.8	0.3	-0.9
Finland	45.1	52.5	16.6	43.7	51.7	18.4	1.4	0.8
Sweden	93.9	119.4	27.2	86.1	112.2	30.3	7.8	7.2
United Kingdom	253.0	306.0	21.0	346.2	422.5	22.0	-93.2	- 116.5

	Exports			Imports			Balance	
	2009	2010	2009-10 growth rate (%)	2009	2010	2009-10 growth rate (%)	2009	2010
Iceland	2.9	3.5	19.5	2.6	2.9	14.0	0.3	0.5
Norway	86.8	98.1	13.1	49.6	56.5	13.9	37.1	41.5
Switzerland (2)	124.1	147.4	18.7	111.9	132.7	18.6	12.2	14.6
Canada	226.1	291.0	28.7	230.2	295.1	28.2	-4.0	-4.1
China	861.5	:	:	720.9	:	:	140.6	:
Japan	416.3	580.7	39.5	395.7	522.5	32.0	20.6	58.2
United States	757.6	963.3	27.2	1,148.5	1,483.4	29.2	-390.9	-520.0

(1) External trade flows with extra EU-27.
(2) Including Liechtenstein.

Source : Eurostat

The number of Spanish firms exporting goods was 122,987 in 2011⁹¹, 40% more than the last decade. The number of businesses exporting services (except tourism) was around 35,000, 50% more than at the beginning of the 2000. This is what concerns internationalization in terms of trade. Concerning other ways of internationalization, such as direct investment (through the localization of the production or part of the production abroad), the increase has also been significant: about 17,000 Spanish firms have been involved in investment operations during the period 2003-2011. These investing plus productive activities have generally other positive results in the increase of trade, both imports and exports. So in this sense, we can notice a beneficial evolution on the trade and foreign direct investment.

Table 42. A comparison between Spanish firms that export with those that do not export

Total Firms								
	Size (nb. employees)	Qualified labor (a)	Ratio of temporary work (b)	Innovating intensity (c)	Debt ratio	% firms participated with foreign capital	% firms with foreign invest.	Productivity (gross value added / employee)
Exporters	12	16.3%	7.8%	2.7%	30.2%	3%	1.9%	50.4
Non-exporters	2	12.1%	3.5%	1.4%	29.8%	0.6%	0.3%	36.6

⁹¹ BANK OF SPAIN. *Annual Report 2011*. Spanish economy's Competitiveness. Page 55 onwards.

Goods								
Exporters	14	15.6%	8.3%	2.8%	30%	2.8%	1.9%	50.8
Non-exporters	2	13.4%	3.5%	1.4%	29.9%	0.7%	0.4%	37.4

Services (except tourism)								
Exporters	10	20.6%	6.2%	2.9%	31.6%	4.5%	3.0%	56.9
Non-exporters	2	12.2%	4.0%	2.3%	29.7%	0.7%	0.4%	39.3

Figures are the average of the period 2001-2011, for the total of firms (goods and -non-touristy-services)

- (a) % executives and technicians (and similar) over the total number of employees.
- (b) % temporary work over the total.
- (c) % of expenses in R&D over total gross added value.

Source: Bank of Spain. Based on a sample of 1.2 million firms.

However, exporting firms still represent a small percentage over the total number of firms: during the period 2001-2011 about 12% of the firms exported regularly. Regarding services (except tourism), the percentage went down to 9% of the firms. Compared to other countries in the EU, Spanish percentages are lower. Manufacturing firms with more than 10 workers reached 64.4 in Germany or 77.2% in Italy, compared to 61.1% in Spain⁹². Therefore, even if we can affirm that internationalization of Spanish firms is a fact and it has intensified in the last decade, the phenomenon is not yet generalized and exporting is still an activity unknown for the majority of businesses, mostly if small ones.

Another interesting fact quite peculiar for Spain is that exports are concentrated in a small number of firms: in 2011, 1% of the exporting firms accounted for over 67% of the total exports, while 10% of the top exporting firms accounted for 93% of such trade. The concentration is more acute in the services sector than in manufacturing. As a summary, it can be stated that exports are, in the first place, not generalized and, in the second place, rather concentrated in a small number of firms with a solid tradition for international trade.

⁹² EFIGE DATABASE. The global operations of European firms. The second EFIGE policy report. Fully harmonized and representative firm-level database on the international activities of European manufacturing firms. New data cover 7 countries (Austria, France, Germany, Hungary, Italy, Spain and the UK) in 7 policy relevant research areas concerning: firm size and productivity; firm organisation; geographical scope; skills and tasks; innovation; financial constraints; the euro. www.europa.eu and www.efige.org. October 2011.

Table 43. Degree of concentration of exports. Average 2001-2011.

Exports Concentration Degree				
	% over the total	TOP 1%	TOP 5%	TOP 10%
Firms exporting goods and (non-tourist) services	16.7%	64.3%	83.4%	90.4%
Firms exporting goods	12.0%	67.4%	86.5%	92.9%
Firms exporting (non-tourist) services	8.6%	74.5%	91.3%	95.9%

Source: Bank of Spain

According to A. Nagy⁹³, in Spain 73% of SMEs with international connection are firms whose internationalization was a long process and not a sudden decision. Most of the companies made this step following a client or customer who was expanding its activities to external markets.

The fundamental reason in general was strategic: the company realized that its own growth and expansion strategy, practically to survive on the market, needs an international presence, and every other reasons were secondary: diversifying risks, to get nearer to the customer, increasing the image of the company, getting faster access to high technology. Cost-reduction was not really relevant reason.

Spanish exporting firms are relatively larger, with a superior productivity than the average, with more qualified labour and higher technological intensity. According to the Efige project⁹⁴, productivity and propensity to export, grow with the size of the business, and so there is a deep gap between small businesses (10-19 employees) and large ones (over 249). It can be observed that those firms that are competing in international markets, have similar levels of productivity, have similar sizes and similar possibilities to export.

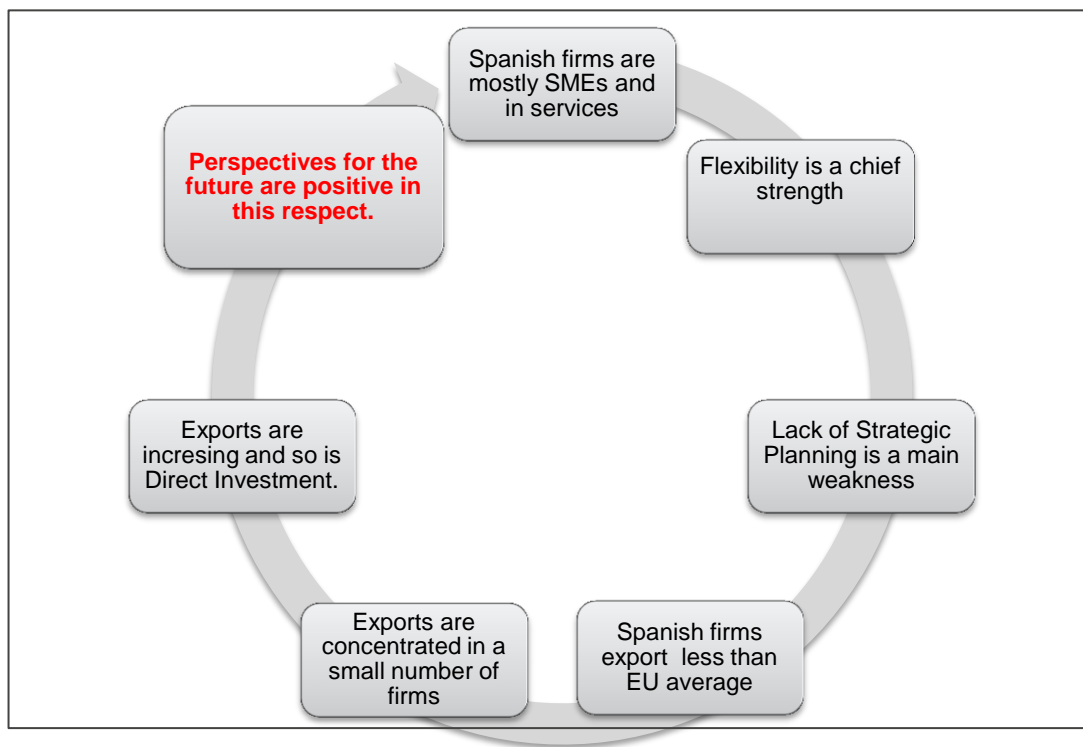
It seems necessary at this point to make a short summary of what has been seen in chapter 4, before moving into a very different matter, the peculiarities of the Chinese market. We have observed that Spanish firms are small, mostly SMEs and very much services-oriented. Spain is a relatively large country where regional differences are significant. SMEs have a great advantage, flexibility, but spend little time in Strategic Planning, which becomes a handicap namely in times of recession. Only 12% of Spanish firms export regularly. Out of those with more than 10 persons employed, only 61% export regularly. Both figures are below the EU average. Exports are growing annually by around 14%, slightly above the rise of imports, which is positive for balance trade. Firms that export are in general larger, more productive and more competitive. Unfortunately, exports are very concentrated in

⁹³ SÁNDOR G. N. The internationalization of the Spanish SME sector. Society and Economy (p. 46).

⁹⁴ www.efige.org. October 2011.

Spanish firms: only some export - but those that do export do so a lot. The diagram below summarizes the structure of Spanish firms:

Figure 58. A summary of Spanish business structure and characteristics



Source: own elaboration

6. Spain and its foreign trade deficit with China

Spanish exports to China in 2011 accounted for 4,519 million US\$, 32% more than the previous year. In the same period, the imports from China increased only by 2%. It shows finally a change in the trend: exports are growing at a faster pace than the imports. Spanish trade balance is starting to improve, although the foreign trade deficit is still very large.

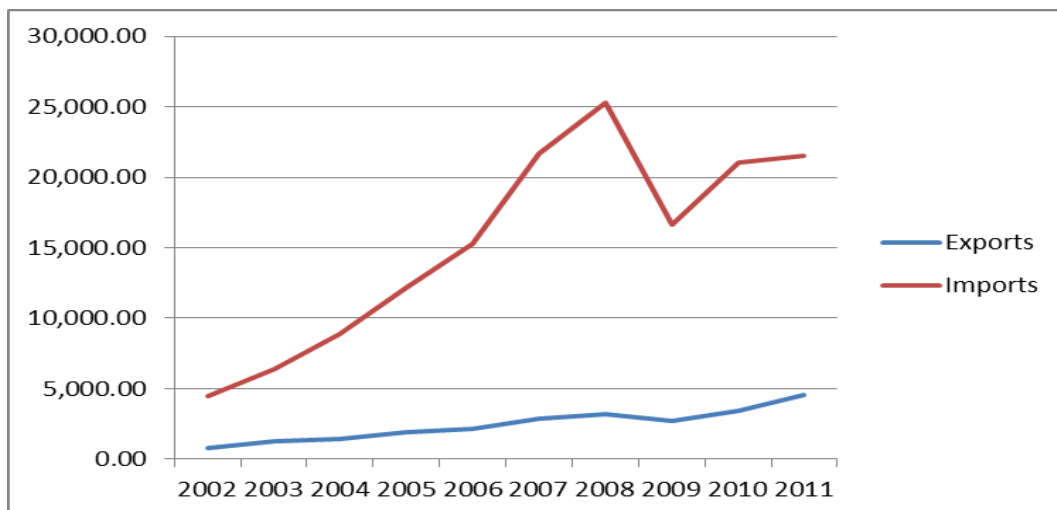
Table 44. Foreign trade of Spain with China, 2011

Exports Spain to China		Imports Spain from China		Balance (X-M)	
Value Mill US\$	Variation 11/10	Value Mill US\$	Variation 11/10	Value Mill US\$	Variation 11/10
4,518.57	32%	21,502.62	2%	-16,984.05	-3.70%

Source: IMF- DOTS Database (June 2012) and own calculations.

The trend can be appreciated in the figure below. Imports continue increasing slowly but steadily, while exports depend greatly from Spanish demand, which fell sharply in 2009. Although it is recovering, it has not yet reached the peak of 2008.

Figure 59. Trade in Goods, Spain with China, 2002-2011



Source: IMF- DOTS Database (extracted June 2012).

China remains the first supplier of the Spanish imports outside the EU. It is country supplier number four, with a market share of almost 7% of the Spanish imports. Imports from China in 2009 suffered a sudden drop by 28%, due to the recession suffered in Spain. Although the exports of Spain towards China also decreased, they did it in a much smaller proportion (8%).

In spite of that, the trade deficit of Spain with China is very large: in fact, it is the largest of the Spanish trade with the rest of countries. The value of Spanish imports from China is almost five times more than what it exports (but it used to be six times only two years ago, so the situation is slowly changing).

Only China represents half of the Spanish trade deficit with Asia and 25% of the total deficit. The cover rate of Spanish trade with China was 21% in 2011.

Main exports of Spain to China

According to Spanish customs data, the main sales from Spain to China focused on raw materials and semi-manufactures of plastics (11.6%), organic chemistry (5.8%), steel products (5.7%), automotive components (5.1 %), pharmaceuticals (4%), electrical goods (3.9%) and marble and construction materials (3%).

The most dynamic among the first items were electrical equipment and pharmaceuticals. It is noteworthy that the main item, raw materials and semi-finished plastic, grew by 17.1% in 2010.

Main imports of Spain from China

The major purchases in Spain in 2010 were female clothing (11.7%), computer and hardware (6.7%), telecommunications equipment (6.4%), footwear (3.9%), male clothing (3.5%) and electronics (3.4%). Imports dropped in all items, with the exception of telecommunications equipment. The large drop in electronic components, which happened to fall by more than 85%, was remarkable.

Evolution in the balance of payments

The Spain-China trade relations are characterized by a chronic deficit. What is most troubling is not the high volume of imports, in line with what happens in EU other countries around, but the low relative volume of Spanish exports. However, recent years show a gradual increase in Spanish sales to China, which has already become Spanish's most important Asian market.

The evolution of bilateral trade in 2009 reduced the trade deficit between the two countries in 5,875 million euro to reach 12,464 million euro in 2009, 32% lower than in 2008. In January and February 2010, an increase in exports compared to imports, has allowed a slight additional reduction of the bilateral deficit by 0.3%. Due to the larger fall in imports than exports, the coverage rate in 2009 has increased by over three%, although it is still very low (13.76%), compared to 10.5 % in 2008 and 11.5% in 2007.

According to ICEX, the trade deficit with China (12,464 M €) in 2009 is equivalent to the one with Germany (12,345 M €). However, the analysis of the business relationship with China differs from that of Germany, among other reasons, by the proximity, the existence of the euro and the free movement of goods, persons, services and capital, etc. In any case, the equivalence between both deficits is peculiar: the value of trade between Spain and Germany is three times the value of trade with China. Spanish imports from Germany more than double those from China. But Spanish exports to Germany in 2009 reached a value almost nine times higher than exports to China.

From these figures it appears that the access of Spanish exports to the Chinese market does not yield good results. It is important not to forget some characteristics of China's trade pattern. Foreign-funded enterprises account for 54% of Chinese imports, nearly a third of Chinese imports are for processing, and Chinese companies with foreign capital represent 84% of total imports for processing in China. That is, direct investment in China is a source of imports. This shows the importance of the Foreign Direct Investments (FDI) in exports: much of Chinese foreign trade is trade development. This circumstance is made clear, for example, in the producers of international automobile established in China.

7. Key success factors when accessing the Chinese market

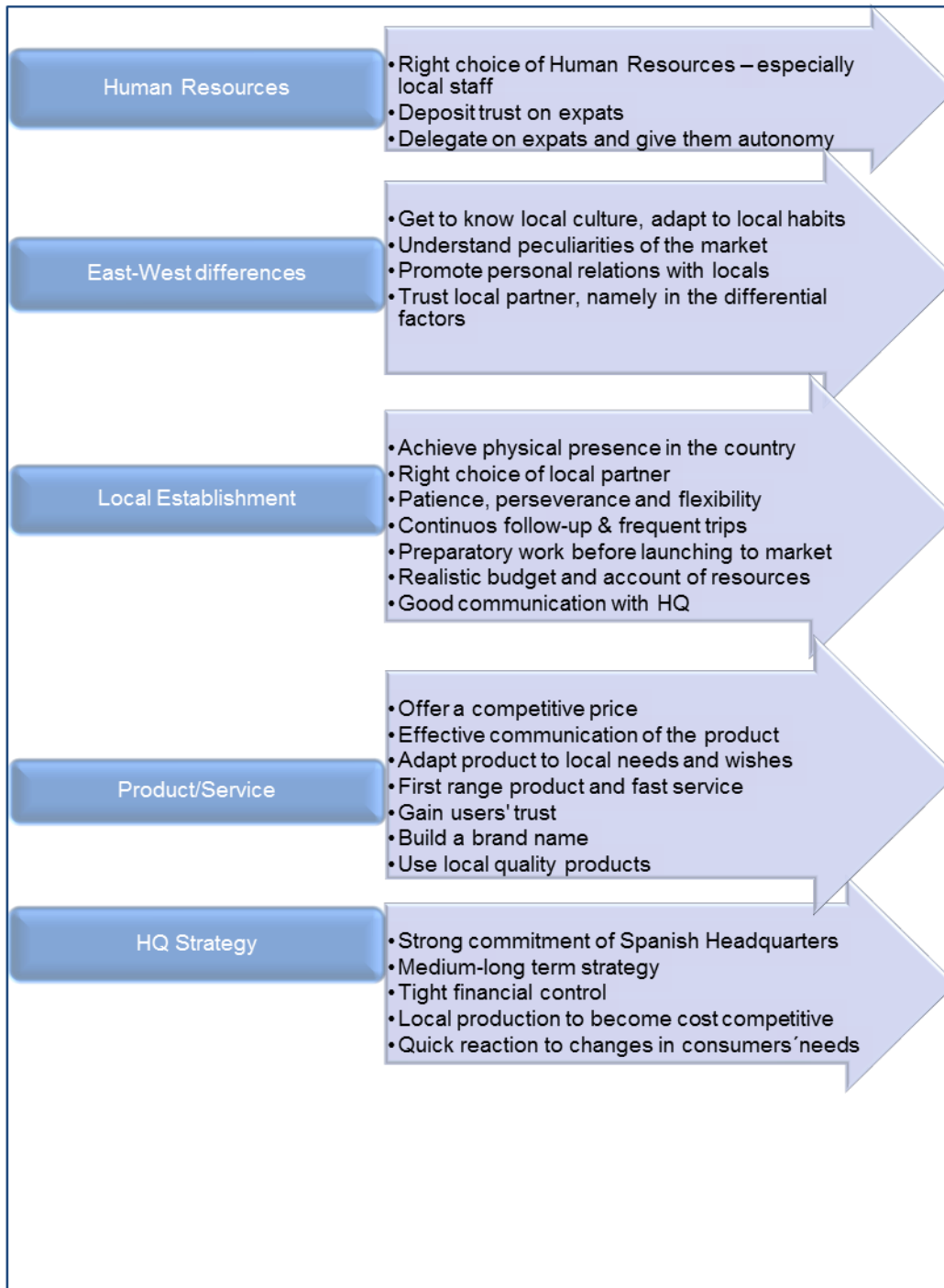
A survey carried out by Casa Asia⁹⁵ asked Spanish executives what they considered to be the key success factors when establishing in Asia. The diagram below has been constructed inspired by those results plus some own elaboration from experts' opinions. In the first place, five kind of main elements have been identified: human resources, east-west differences (cultural differences), establishment conditions, strategy from the headquarters and product and services characteristics. From each one of the elements, different factors have been identified.

Summarising, the most relevant keys for success are:

1. First, get to know the local culture and adapt to it;
2. Use appropriate human resources, which is especially difficult when we have to rely on local human resources;
3. Remain patient, flexible and persevere;
4. Choose the right local partner when we use this alternative;
5. Achieve and maintain competitive prices;
6. And last but not least, strong commitment from the Spanish headquarters.

⁹⁵ CASA ASIA. *Estudio sobre la presencia empresarial española en Asia*. Círculo de Negocios de Casa Asia. Everis S.L. 2006.

Table 45. Summary of the key success factors when accessing Asian markets

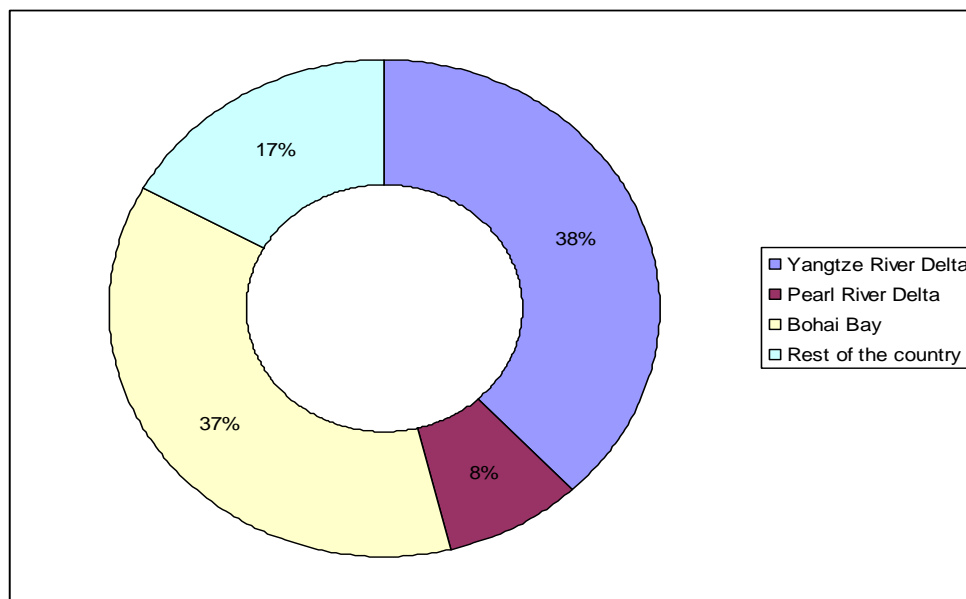


Source: Own elaboration from Casa Asia's survey. Even if the environment studied is Asia, most answers (78%) refer actually to China.

Another piece of advice frequently mentioned that may be of use is to focus on a specific part of China. Do not try to cover the whole country. It would be a hard and very expensive task. It is better to start in one location and expand as required with time.

The graph bellows shows where Spanish firms are located in China.

Figure 60. Geographical location of Spanish firms in China



Source: Casa Asia

Legal form

Until very few years ago, there were legal impositions affecting most sectors that obliged foreign firms to establish in China as joint ventures. Nowadays, the WFOE is already the most commonly used legal form to establish a business in China. For instance, since 2005 foreign publicity firms can establish themselves as WFOEs, according to information given by Casa Asia.

Sectors

When we consider the sectors, a clear evolution can be detected. While in the past foreign firms based their production and commercialisation in manufactured products, more and more the opportunities open in services.

Table 46. Evolution of the activity of Spanish firms in Asia

60s and 70s	80s	90s	2000 onwards
Food & Beverage	Machinery, capital goods and equipment	Textile, shoes and leather products	Renewable energies
Ceramic	Chemicals	Automotive and related	Telecommunications
Pharmaceutical	Banking & Finance	Cosmetics and healthcare	Cement
Industrial Engineering	Transport	Technology and software	Design
Leather products	Metallurgical	Furniture and street furniture	Architecture

60s and 70s	80s	90s	2000 onwards
	Electronics	Logistics and ports	
	Railway equipment	Water treatment	
	Construction material	Construction material	
	Hospital supply	Optical	

Source: Casa Asia

Expert in Asia Xavier Espasa explained that the main obstacle to access the Chinese market is the distribution channels: sectors considered *strategic* such as telecom, car industry, aeronautical, infrastructures or the military are sheltered by the government. Foreign companies cannot access these markets without a Chinese partner.

As it was stated before, distribution channels, as we know them, do not exist. To introduce consumer goods in China it is often required that the Spanish firm establishes the whole distribution channels, which is extremely expensive.

Therefore, experts recommend focusing on certain products where opportunities are found (food, wine, luxury goods, industrial products, fashion) and especially on services: "China's service sector is likely to become an emerging battlefield for many international corporations, as the opening of this sector offers enormous market opportunities (...) China will not become an economic giant until it opens its service sector and increases foreign trade and investment in services"⁹⁶.

Within services, some are particularly relevant for the Chinese market: telecommunications, technologies, software development, transport, logistics and communications, banking and finance, design, architecture, publishing, packaging, education and training. Above them all, tourism: Spain has a great opportunity to attract the growing Chinese middle-classes to visit Spain. The kind of tourism, far from being the classic low income, low-spending sun and beach kind of tourism, is bound to be a more cultural and shopping, city-oriented tourism.

Premier Wen Jiabao said in a speech at the Fifth Plenary Session in Beijing 6th March 2012⁹⁷

Expanding domestic demand in particular consumption demand is the fundamental for long-term steady economic development of our country and focus of this year. We will support and guide green consumption such as environment-friendly building materials, water-saving cleaning articles and energy saving vehicles. We will conduct good access and review in

⁹⁶ LUO, Y. *China's Service Sector. A new battlefield for International Corporations*. Copenhagen Business School Press. Copenhagen, 2001. P.17.

⁹⁷ Wen Jiabao Stresses that China will not Seek Economic Growth at the Cost of the Environment and Public Health at the Fifth Plenary Session of the 11th NPC. www.english.mep.gov.cn/News_service. March 2011.

terms of land, credit, energy saving, environmental protection, safety and quality. We will vigorously develop water-saving agriculture, facilitate rural environment control and deepen the reform of resources tax and expand the scope of collecting fee in an all-round way. We will improve the pricing mechanism for hydropower, nuclear power and renewable energy sources. We will conduct trial on trade of carbon emission right and pollution discharge right. We will speed up the establishment and improvement of ecological compensation mechanism. He said, we will expand the export of high-technology or high-value added products; control the export of products with high consumption of energy or heavy pollution; guide more foreign investment in advanced manufacturing industry, new and high-technology industry, energy saving and environmental protection industry, modern service industry and central and western parts of China.

Study the cultural differences

It cannot be stressed enough: it is extremely important to take care of the cultural aspects of the business relations. Never try to do business alone, but develop the *guanxi*, the connections. Another aspect that needs to be accounted for has been explained above, the concept of “face”: as explained to me by a Chinese student, Lu Ye Zhan, “*face* is something between honour and reputation. It is a set of rules that are not written but everyone knows. You cannot fail on those”.

Strategy

Perhaps this is the most important success factor. Getting in a new marketplace must be a decision resulting from a strategic plan. In the past, it has not been exceptional to try accessing the Chinese market because it is a trend, almost a fashion. Media have given the impression that China was a compulsory task for all firms and an easy one as well. Nothing is further away from reality. Expert in Asia Xavier Espasa says: “a myth has been invented in the last few years. One has to go to China. It is a must”. However, he corrects: “China is not for everyone. Media have been very light and *happy* tackling these subjects. But reality proves that accessing China is not easy: it can be extremely fruitful and rewarding, but it has to be decided after a very serious and committed decision”.

According to Emilio Mulet, consultant specialised in helping Spanish firms to enter China, “it is tiring to see how firms try to move in without giving enough resources”.

As a result, many firms have tried to access the market just like buying a lottery ticket: see if we can get fortunate. Others have planned some kind of “pseudo-holidays”, go for tourism and see at the same time if there are some business opportunities easy to grab.

These are the wrong reasons. One cannot get into the market hoping he or she will be lucky. It just does not work like that.

Instead, Joan Armenter, former executive at Roca gives the following pieces of advice for Spanish firms: “in the first place the firm needs to decide to become international. This decision changes the whole firm: its recruitment process, its

mentality, staff behaviour, etc. Then the firm can start by tackling *easier* countries such as Eastern Europe or Latin America. China will come after, like a *Masters' degree on internationalisation*". Moreover, there are certain things the business must have clear:

- there has to be a conscientious strategic plan;
- where the headquarters are very committed to the plan;
- resources are planned and given;
- products are tested in the market;
- and finally, there is certain physical presence in the country.

The whole plan must be thought of properly and must answer to a strategic decision. Otherwise, it will not be implemented properly and persons involved will be soon discouraged. Results will not happen and there will be a general sense of failure.

If this seems too burdensome for small businesses, or they cannot afford the investment and the effort, there are alternatives. For instance, go together in a group of firms, like a cluster. Or start with the help of institutions such as ICEX or autonomous regions' promotion authorities.

To end this chapter, we would like to add the following pieces of advice that were given by Gao Wei, Director of the Promotion Centre of ACCIO in Beijing: "First, one should count with a certain dose of adventurous spirit. You are going to need it. Then, try to earn your money as soon as possible. Avoid joint ventures, and go for the WFOE. Take care of the local authorities. Make friends with civil servants: it is vital to know where you stand and to make sure your project will get accepted. And finally, try to understand the cultural differences between both civilisations".

In any case, this is a fascinating subject that has only been introduced herewith. Our research continues in chapter 6 when we focus on concrete business answers to our survey and where we will try to analyse different reasons to establish in China, priorities for the Spanish firms, obstacles encountered in the way, etc. Finally, we will try to give a final set of "best practices" that will help Spanish firms in the future when trying to access this vast and fascinating market.

VI. SPANISH BUSINESSES IN CHINA. OUR SURVEY

Up to this point we have analysed the attractiveness of the Chinese market and the international trade between China and its main partners. Subsequently we reviewed a general picture of the Spanish business structure. Our objective in this section now is to analyse which of the Spanish businesses are operating within China, what are their reasons to be in China, study their difficulties, list out their priorities for the next years and, last but not least, try to find out what are their best practices. With this analysis and a keen outlook towards the future, we will close our research. In order to complete the study, we have carried out two complementary analyses:

1. Directory of the official Chamber of Commerce of Spain in China (2010) data exploitation. Completed with ICEX database of Spanish firms in China;
2. Our own survey directed to the population of the databases above, to provide with qualitative data.

The sections that follow will explain the methodology used in each case and the main findings.

1. Directory of Spanish Businesses in China: objectives of the analysis and methodology

The first problem we faced when analysing the Spanish businesses in China was to define exactly how to tackle the population objective of our research. We needed to select companies that:

- have been working in this specific geographic area for a certain period of time;
- have some sort of physical presence (an office, a production plant, facilities of any other kind);

That would therefore exclude those Spanish firms that have occasionally exported to China but have no facilities in the country

Taking this into account, we found that the most comprehensive and up-to-date database of Spanish firms in China is the 2010 Directory of the Official Chamber of Commerce of Spain in China. ICEX has another directory (the ICEX Database of Spanish firms in China) that has been used to complement the first one. Combining both and filtering the results by removing duplicates and Chinese or other foreign firms, we find that the in 2010 there were 360 Spanish companies established in China.

2. General picture of Spanish firms established in China

We have focused on six variables that could be extracted directly from the directories (or at least easily deduced from them), for which we have practically

100% of the data. These variables are descriptive and give a preliminary idea of who are the Spanish firms operating in China:

Figure 61. Selection of variables directly deduced from Directories

2.1 Sector of activity
2.2 Destination in China
2.3 Year of establishment in China
2.4 Origin of HQ in Spain
2.5 Contact person in China: sex and origin (Western or Chinese)
2.6 Objectives in China

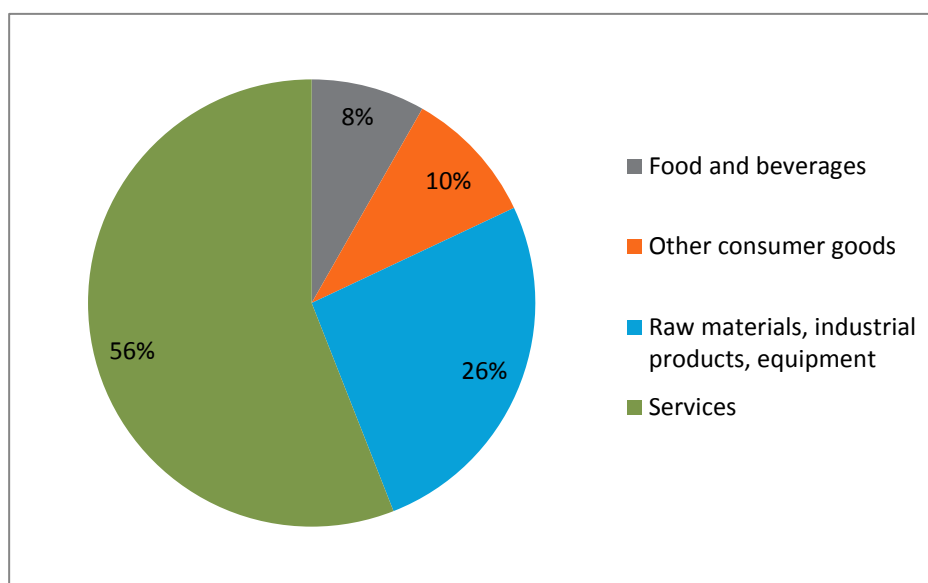
Source: own elaboration

2.1 Sector of activity

By way of a start, in what sectors are Spanish businesses operating? To answer to this question, first a broad classification has been carried out. It can be deduced that:

1. Most Spanish businesses are operating in the services sectors (56%) such as transportation and logistics, professional services, consulting, financing, legal, quality control, advertising and other services (health, education, art, culture, etc.,).
2. In the second place, we have industrial equipment and intermediate goods (26%), mostly supplies to the Chinese industry (metal, machinery, equipment, raw materials, etc.).
3. In the third position, we have other consumer goods (10%) such as textiles, fashion, footwear and other consumer goods. Not included in other consumer goods and in a category of its own, we find food and beverages, which occupy the fourth position with 8% of the total.

Figure 62. Spanish firms in China classified by large sectors: the great majority found in services. 2010



Source: own calculations

2.2. Destination in China

After a general overview of the main sectors, we can analyse the concrete activities in more detail and the specific area in China chosen to locate in. Although in most cases firms prefer the area of Shanghai, the following are sectors for which being around the capital is more preferable: building and construction, tourism, information and communication and energy and renewable energies. These are strategic sectors that require that firms to be established around the area of Beijing.

Table 47. Spanish firms in China classified by detailed sectors and geographical area

Geographical Areas (a)	BEIJING	SHANGHAI	SOUTH CHINA	TOTAL
Sector				
Food and beverages	9	14	9	32
Textile, fashion and shoes	7	8	8	23
Chemical industries, pharmaceutical and plastics	1	9	6	16
China, ceramics and glass, building materials	1	7	2	10
Metal, metal products, machinery and equipment	18	30	7	55
IT products, electronics and optical products	7	7	0	14
Vehicles and transportation. Train, car, aircraft and ancillary industry	6	9	0	15

Geographical Areas (a)	BEIJING	SHANGHAI	SOUTH CHINA	TOTAL
Other manufacturing industries (electric products, lighting, printing, fire protection, promotional sector, furniture, antiques, toys, others)	6	14	11	31
Water supply, sanitation, waste management and decontamination	3	0	0	3
Building and construction. Architecture and engineering	11	7	1	19
Transport, logistics and storage. Distribution and ports	9	19	6	34
Tourism, hotels, restaurants, sport activities	9	3	0	12
Information and communication	10	2	0	12
Financial activities and insurance. Real Estate	9	12	1	22
Professional services: advertising, legal and consulting business services, QC, import-export	32	48	15	95
Health, education, art, culture, administrative activities and other services	12	11	4	27
Energy and renewable energies	12	9	1	22
TOTAL	162	209	71	442(b)

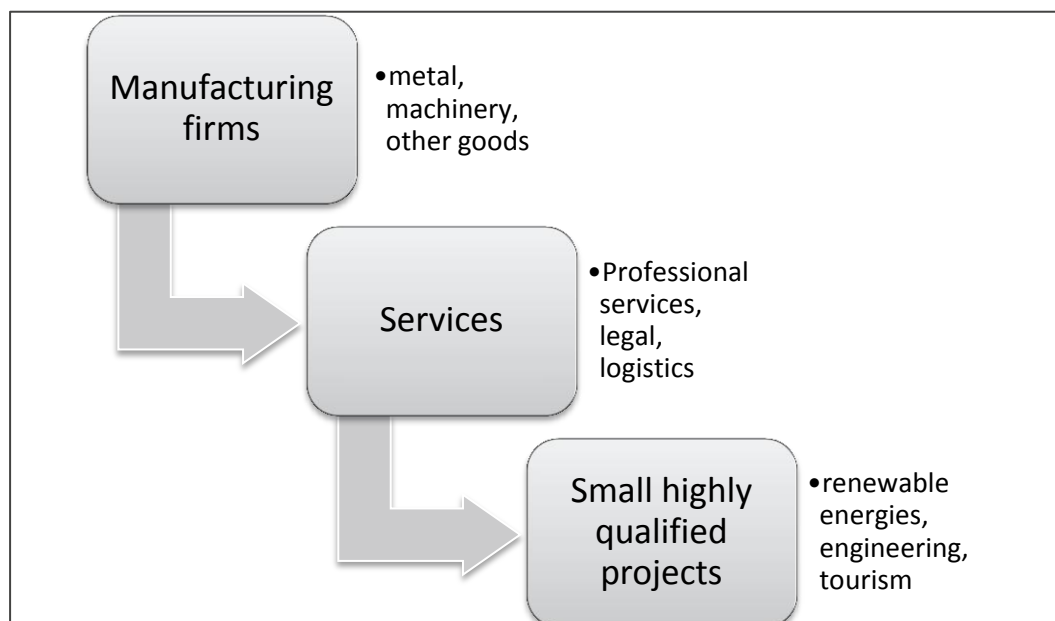
(a) Area of Beijing: Bay of Bohay; Shanghai: Yangtze River area.

(b) Totals can be over 360 when firms declare more than one answer.

Source: own calculations.

Looking at the above table, it can easily be seen that on one hand, there is a large number of firms that are dedicated to production: metal, machinery, textiles, other manufacturing industries, etc. Then there is another large group of businesses who give professional services to Spanish and Chinese firms: services related to consulting, advertising, legal matters, quality, trading, etc. Finally, there are some firms, smaller in numbers but growing in importance, that are highly professional, often technology-based, that are not so much linked to Spain, but are global start-ups.

Figure 63. Spanish firms in China in evolution



Source: own elaboration

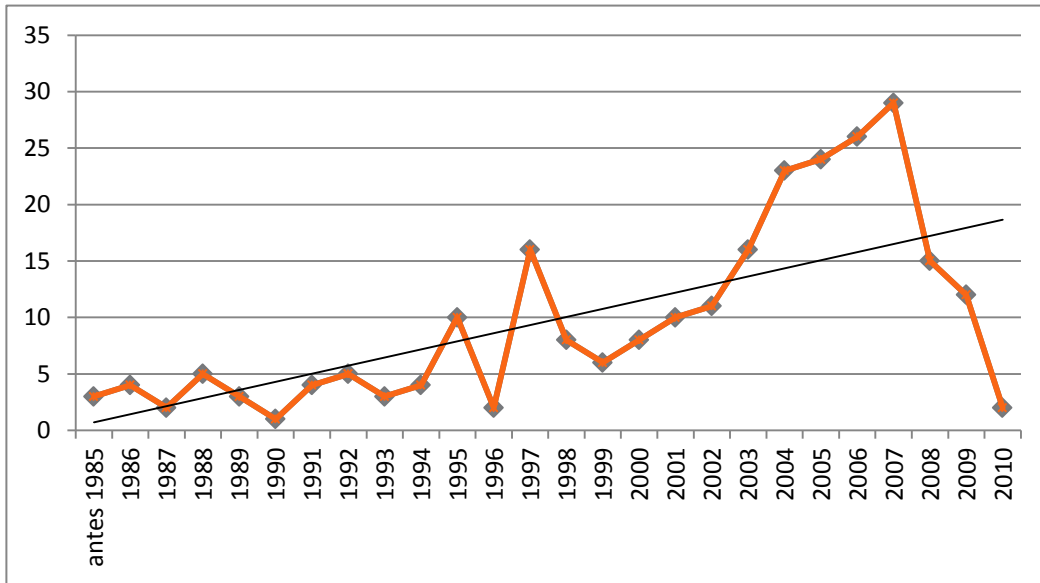
2.3. Year of establishment in China

We can now analyse the year of the incorporation of the firms in China. With the exception of a few early ones, most of the firms arrived in the 90s and then, more noticeably from 2000 onwards. There was a boom in the first years until 2007, when, with the economic recession many firms decided against such an endeavour. The risk was high as was the initial investment. Therefore, the unfavourable economic climate discouraged many. Although this fact seems quite negative, it involves a positive fact – and one that has been pointed out by several experts – that the firms that take the decision nowadays to invest in China or to try to access the market, do it more seriously, plan ahead better, involve more resources, support the decision strongly and therefore, increase their chances of success.

The figure below shows the trend of the establishment of Spanish firms in China. The numbers grow irregularly between 1985 and 1999, after which year the progression is fast and clear. This growth goes on for almost ten years reaching its peak in 2007, a year in which almost 30 new companies started operating in China. After that year, figures drop dramatically⁹⁸.

⁹⁸ These figures need to be taken cautiously. For some reason unknown for us, many firms do not answer to this variable, therefore numbers are not as significant as with the other variables. What is interesting in this case is not so much the absolute numbers, but the trend they show.

Figure 64. Year of establishment of Spanish firms in China. Numbers of firms

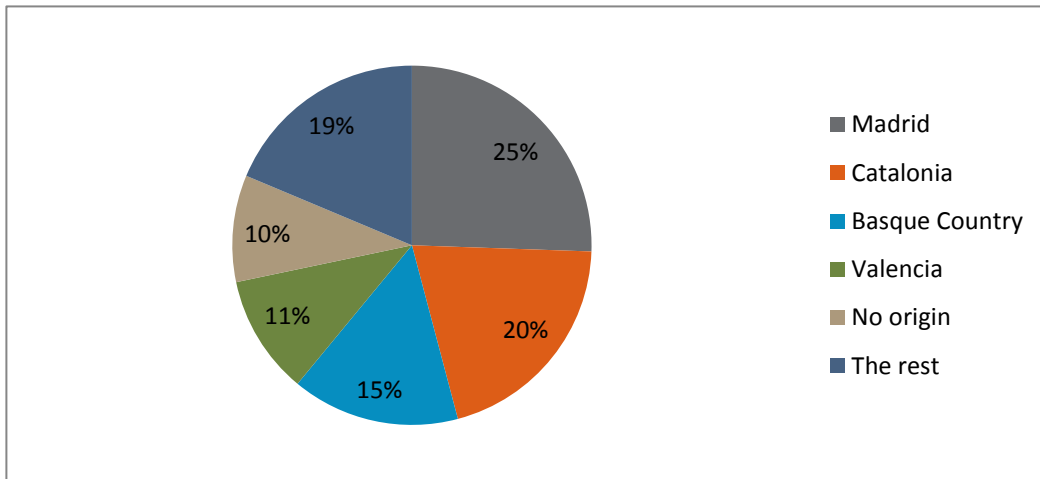


Source: own calculations.

2.4 Origin of HQ in Spain

According to the origin in Spain, most of the firms (over 70% of the total) come originally from four regional areas: Madrid, Catalonia, the Basque Country and Valencia.

Figure 65. Spanish firms in China classified by origin in Spain



Source: own calculations

Almost all Spanish firms, with few exceptions, establish themselves in one of the three main economic areas: Beijing, Shanghai and South of China. It is worth noting that, as follows logically, the chosen location in China is often a good reflection of the economic specialization that we can observe in Spain. In this sense, businesses from Madrid are very often related to strategic sectors operating in Beijing. Businesses from Catalonia are either dominated by the chemical sector, some

consumer goods and many professional services. Most of the Basque firms are operating with metal, machinery and industrial goods. Companies based in Valencia are often related to trade and consumer goods, and the Andalusian ones with food and food-related products.

It is interesting to note that there are more and more firms that declare no origin in Spain: these firms are global start-ups, founded by Spanish entrepreneurs who are based in China. They are mostly small businesses, dedicated to giving professional services to western firms in China and they are mostly placed in the area of Shanghai.

Table 48. Origin of the business: Headquarters' location by Autonomous Community (absolute numbers)

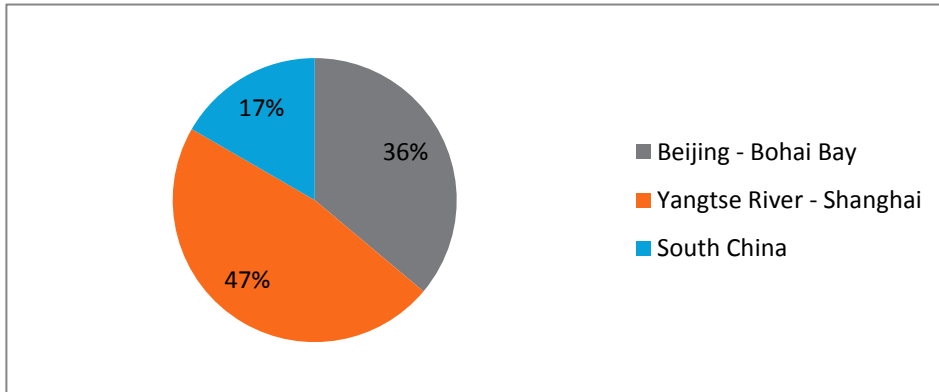
Origin in Spain (Autonomous community)	BEIJING	SHANGHAI	SOUTH CHINA	TOTAL
Madrid	47	39	7	93
Catalonia	17	46	11	74
Basque Country	25	24	6	55
Valencia	8	20	11	39
No origin is specified	8	17	10	35
Andalusia	6	5	1	12
Aragon	3	4	2	9
Castilla La Mancha	0	7	1	8
Castilla-León	4	2	2	8
Navarre	2	5	0	7
Asturias	1	3	2	6
Galicia	0	5	0	5
Cantabria	2	1	1	4
Murcia	2	1	1	4
La Rioja	2	1	0	3
Balearic Islands	0	1	0	1
Canary Islands	0	0	1	1
TOTAL	127	181	56	364(a)

(a) Totals can be over 360 when firms declare more than one answer.

Source: own calculations

Almost half of the Spanish businesses establish themselves in the Shanghai area, due to its economic power, but also thanks to the attractiveness of its cosmopolitan atmosphere and the high percentage of foreigners residing in this city. Although recruiting and retaining “expats” is a hard matter in China, it becomes an easier task when we talk about Shanghai. The area of Beijing offers many opportunities due to its capital status and it is certainly more relevant for certain strategic sectors where government contacts are especially important. As regards the south of China, we are referring mostly to the eastern coastal areas around Guangdong (Special Economic Zone). The proximity of the SEZ to Hong Kong has facilitated the development of production facilities with low labour costs and procurement and trade of goods addressing the demand of cheap products in the EU.

Figure 66. Spanish firms in China classified by destination in China

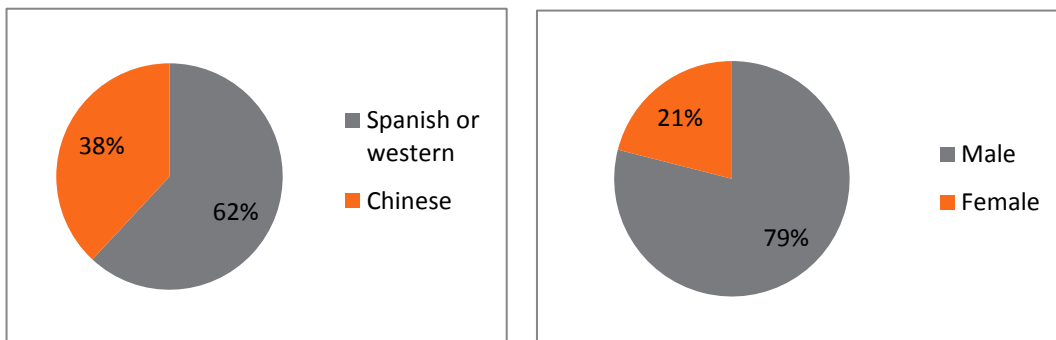


Source: own calculations

2.5. Contact person in China

Regarding the contact person in China, this is a very relevant fact to take into account. As we have seen in previous chapters, one of the difficulties found by western firms when doing business in China is to find the right human resources: on one hand, the right “locals” to work with and to develop the business with and, on the other hand, the right “expats” who move to China and work from there. As we can see from the graphs below, the typical responsible contact person of the Spanish firms in China is a man (80% practically), who can be Spanish (62% of the cases) or Chinese (38%). It is predominantly a male’s world.

Figure 67. Contact person of the Spanish firms established in China by origin and sex



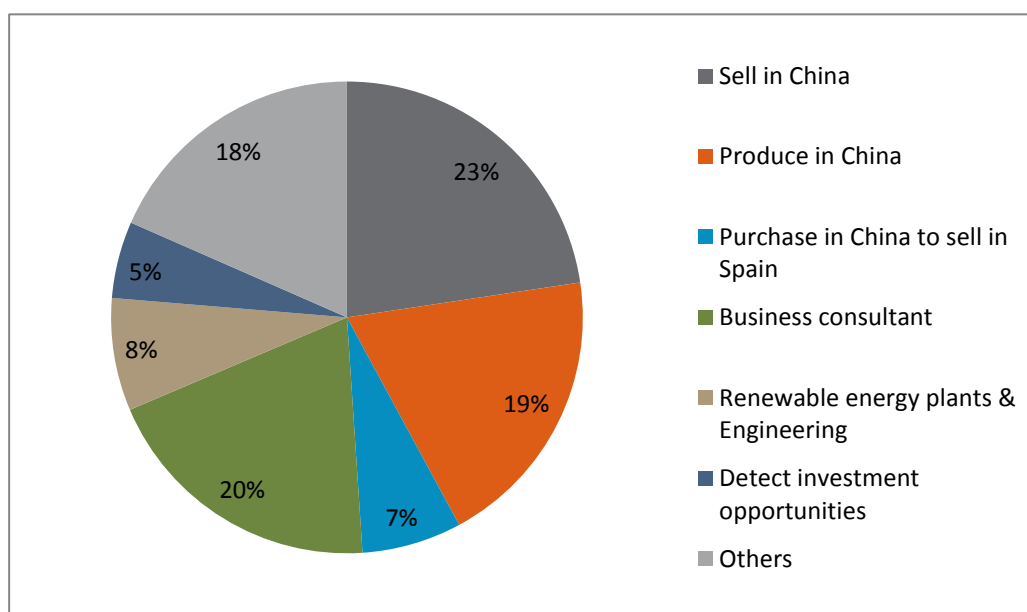
Source: own calculations

In most cases the “expats” are Spanish but exceptionally they come from other western countries, recruited due to their experience in the Chinese market.

2.6. Objectives in China

Almost one quarter of the firms have as their main objective to sell in China (whether they produce there or not). Only 7% of the firms' main objective is to purchase in Asia to export to the Spanish market for sale.

Figure 68. Main objectives of the Spanish firms operating in China



Source: own calculations

The following table shows with more detail the main objectives Spanish firms have when establishing in China. While in the recent past firms mostly moved to China to produce cheaply, nowadays, most firms are there to sell:

- Either to sell their products (consumer goods or capital equipment)
- Or to sell their services, mostly professional services in fields of trade, logistics, quality control, law services, advertising, etc.

Only a third of the businesses consider their main objective to be manufacturing. This represents a fundamental change in the point of view of the firms, who stop considering China as a source of cheap labour, to now consider it as an interesting market worth investing in.

Table 49. Origin of the business: location of the headquarters by Autonomous Community

Main objectives in China	BEIJING	SHANGHAI	SOUTH CHINA	TOTAL
Access Chinese market	47	57	25	129
Business consultant (in trade- logistics- HR - quality and certification - legal - marketing, etc)	29	66	17	112
Production in China (with own plant or not)	37	55	19	111

Main objectives in China	BEIJING	SHANGHAI	SOUTH CHINA	TOTAL
Procurement to export to Spain (or elsewhere)	11	17	11	39
Detect investment opportunities operations	15	12	4	31
Develop solar/ wind power plants/ projects and subsequent technology transfer	12	9	1	22
Engineering Consultancy Turnkey Projects incl. Railways	12	13	0	25
Environmental technologies and water treatment	12	4	0	16
Banking & Insurance projects	4	7	1	12
Promote the exchange and development of art, culture, language	5	4	2	11
Promotion of tourism in Spain	5	3	0	8
Organise events, sports events and promote sports	3	3	2	8
Develop IT Systems, software, mobile contents	7	0	0	7
Tours, tourism guides in China	4	2	0	6
Restaurants, hotels, hotel services	3	3	0	6
Strategic alliance with Chinese firms (eg..Telefonica, Roca, mining, elevators)	1	4	1	6
Promote training and research	3	1	1	5
Real Estate promotion	1	4	0	5
Removals	1	3	0	4
Passenger transportation	2	0	0	2
Internet business incubator	0	1	0	1
Cinema and TV production	0	1	0	1
TOTAL (a)	214	269	84	567

(a) Totals can be over 360 when firms declare more than one answer.

Source: own calculations

2.7. The proliferation of promotion offices of Spain in China

In the last years, several promotion offices representing different Autonomous Communities have opened their offices in Beijing, Shanghai, Guangzhou and / or Hong-Kong. This is the case of Aragon, Catalonia, Madrid, Valencia, Basque Country, Galicia, Andalusia, Castilla La Mancha and Castilla- León. These offices have as their main objectives to help the firms from their regions to establish themselves in China, to open opportunities for their products, to detect investment opportunities etc. The first regional offices to open were the ones representing the industrial regions, Catalonia and Basque Country, and when China became a media boom, many others followed.

These offices have a common objective: to promote the introduction of their respective regional businesses in China. However, what is the real situation? We will analyse it in the following section.

Even if we are aware that this is not the central objective of our research, it is perhaps interesting to consider the situation of the Spanish regional promotion abroad. We have seen in former pages that the brand of Spain is not very powerful in China. Also we have been able to acknowledge that the existing brand, albeit positive, is not associated with technology, design or quality. According to Jose Loira, Market Analyst of the Commercial Office of the Spanish Embassy in Shanghai, “as to the model of autonomous promotion, it is chaos in China. Perhaps this system works for other more mature markets, but in China it only generates confusion: dispersion of resources, overlaps, burning of contacts, unnecessary competition and loss of synergies. The Chinese authorities do not recognize these regional Representation Offices as valid partners. Above all it is really a shame, because these representations do not have the capacity to carry out how serious projects since they do not have sufficient means”.

It seems obvious that having so many different representation offices means that each one of them has not got enough critical mass to start strategic ventures. The offices are staffed by a very limited amount of people, some of them trainees with none or little experience of the country.

But it is not all bad news, Loira continues: “the food sector overall China Plan was created in 2007 and little by little we are getting certain achievements - not without sacrifices and efforts”. He adds “Sometimes what is considered ‘politically correct’ is one thing and the reality is a different one”.

Figure 69. Business Promotion Entities of the various Spanish Autonomous Communities in China



Figure 7: China's 23 provinces, autonomous regions, administrative municipalities and Special Administrative Regions (SAR).

Source: Google maps and own elaboration. Information extracted from web sites of the different Autonomous Communities' Governments.

As we can see, there are areas in China (Shanghai being the most extreme of the cases), where Spain is represented by about ten different public entities developing contacts and promoting their regions: ICEX representing Spain as a whole, ACC10 representing Catalonia, the SPRI network representing the Basque Country, IVEX representing Valencia, EXTENDA representing Andalusia, Aragón Exterior representing Aragón, IGAPE representing Galicia, IPEX representing Castille-La Mancha and EXCAL representing Castille-León. We hope we have not forgotten anybody in this extensive list. This is probably a world record, although it has not been proved.

Spain is a country with 47 million people. China has 1.3 billion. Common sense would indicate that promoting the country of Spain as a block would work much better than diluting the effort. A prove of this would be the Expo of Shanghai in 2008, where Spain was represented by one Pavilion (of course inside the different Autonomous Communities were present), and became one of the most successful and popular ones of the whole exhibition. Hopefully the work done by the different regions can be coordinated increasingly. One idea to develop this is to design common plans to promote specific sectors in China (normally called “Plan Sectorial”, for instance for the olive oil) or to organize the representation of a Spanish stand in the main Trade Fairs that take place in China.

Efforts are being made to increase cooperation and, as a matter of fact, at the time we are writing this document, some of the Autonomous Regions were reducing their number of offices, like Valencia, or even closing them down, like Castille-La Mancha. However, it must be said that the reduction of the number of offices is not the result of a rational decision to organize a common action, but forced by the lack of public resources in Spain.

The problem that lies behind is the lack of an industrial policy to promote Spanish exports. There is no strategy, no business policy sufficiently developed to coordinate actions. Without this long-term vision, the promotional activities have merely been *copy-cat* punctual short-term actions.

3. Objectives of our survey and methodology

A report was carried out in 2006 by Casa Asia⁹⁹ studying the Spanish business presence in Asia. The purpose of our work and our main contribution to this matter is to up-date the figures (since anything related to China changes so fast) and also widen the study, adding some more qualitative questions. To achieve this, a questionnaire¹⁰⁰ was sent to the 360 Spanish firms established in China.

⁹⁹ CASA ASIA. *Estudio sobre la presencia empresarial española en Asia*. Círculo de Negocios de Casa Asia. Everis S.L. 2006.

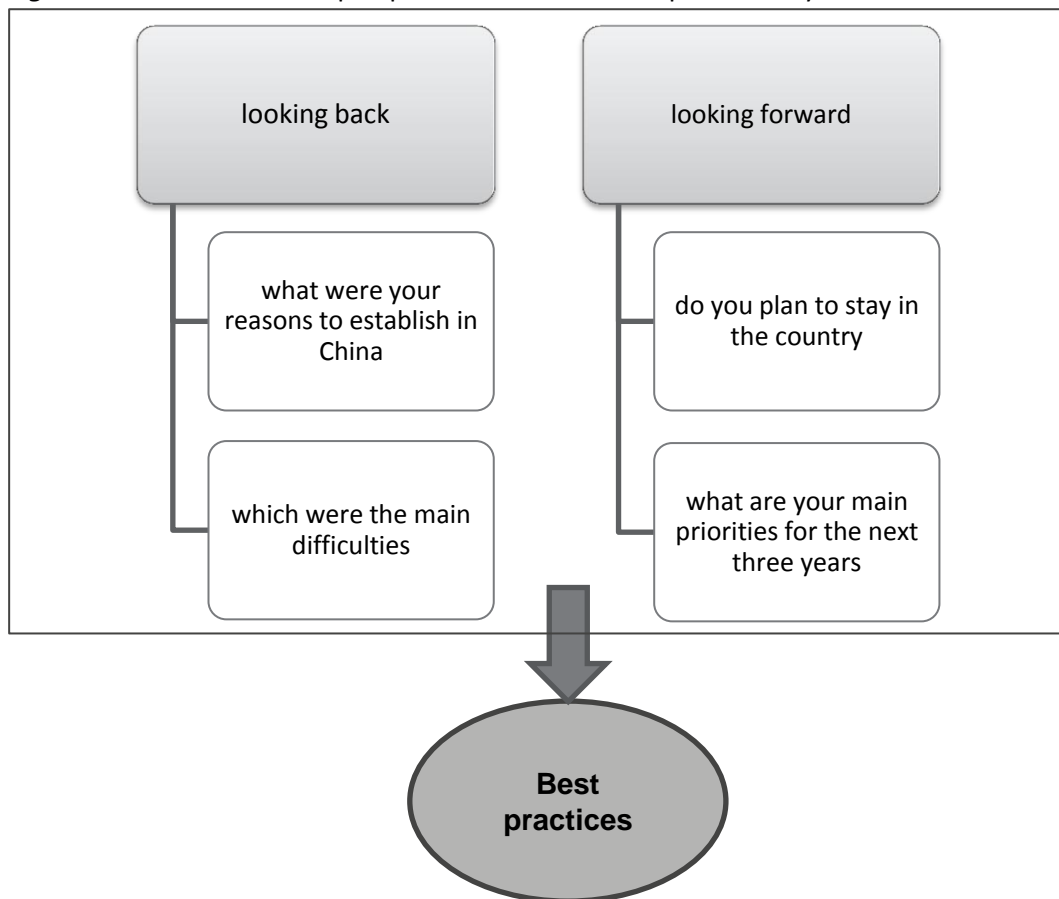
¹⁰⁰ The whole questionnaire can be found, both in English and in Spanish, in annexes 4 and 5.

Our research presents a threefold approach:

- a. From the present moment (first half of 2012) it **looks back** and analyses: what were your reasons to establish your business in China and what were your main difficulties.
- b. Next, **looking forward**, it inquires: what is your level of satisfaction after this period, do you plan to continue in the country and if you do, what are the priorities for the next three years in China.
- c. To conclude, the questionnaire attempts to **sum up** and requests: what do you think you have done right in China, with the intention to compile a set of best practices.

This perspective can be summarised as follows:

Figure 70. Definition of the perspective taken to develop our survey



Source: own elaboration

Methodology: the table below summarises the methodology and the different phases followed to achieve an acceptable number of answers, together with the dates when each phase took place.

Table 50. Summary of the methodology for the survey

Concept	Dates
Initial launch of survey	January 2012
Reminder Schedule	15 th February 1 st March 2012 15 th March Some preliminary results were sent to all to encourage further answers in May. During the whole period, telephone calls were combined with electronic emails to expedite responses.
Survey Population	360 firms from two databases: Spanish firms that belong to the Spanish Chamber of Commerce in China plus the ICEX Database of Spanish firms in China.
Chief Obstacles	The main hurdle to obtain useful answers from businesses has been their reluctance to give information. This difficulty has been surmounted by re-sending of the questionnaires, use of phone calls as reminders and sending some preliminary results to all, in order to encourage more answers.
Sectors	All sectors are represented, from industrial products, construction and civil engineering to services (all types)
Location in China	All firms in China are considered, regardless of the geographic area, although three areas are clearly more represented: Pearl River Delta (Beijing Area), Yangtze River Delta (Shanghai Area) and Bay of Bohai (South of China).
Alliances	Different institutions have helped to encourage answers: Casa Asia, Chambers of Commerce, etc.
Number of Questionnaires sent	360
Number of answers received	78

Source: own sources.

4. Results from our survey

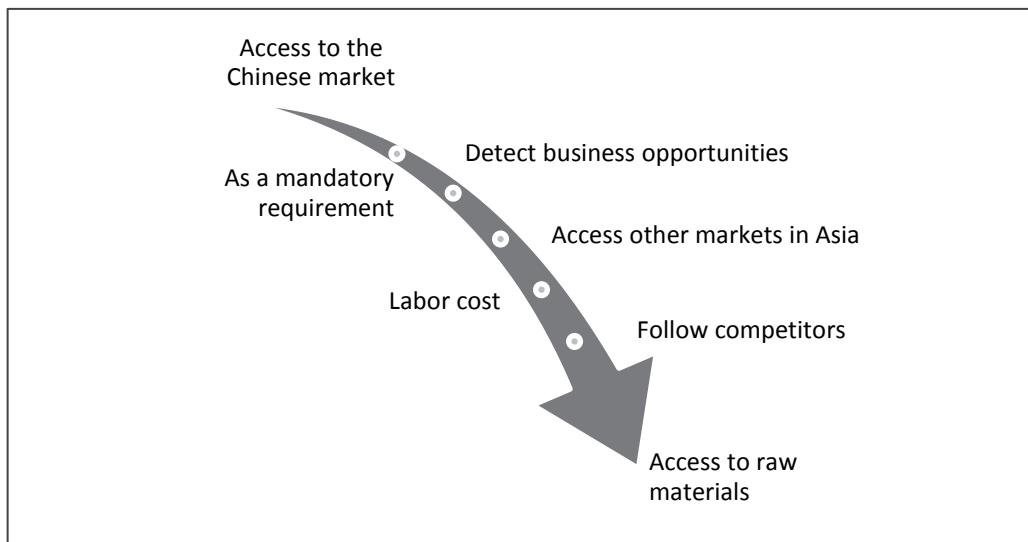
4.1. Looking back. Reasons to set up business in China

The reasons for a business to establish in a foreign country can be numerous. Normally the most common reasons can be either related to the access of resources (raw materials, intermediate goods, labour and / or technology) or the access to the market. In the case of China, the access of raw materials does not play a part, simply because it is not a country with significant natural resources. In general, it can be said that the two main reasons to set up business in China have been two: first, the access to cheap labour and second, the access to the market.

- In the past (the 1990s, 2000s), the main reason was to manufacture low-cost products using a cheap and unqualified workforce in China. After production, the goods were normally transported back to Spain for their consumption.
- Lately, the trend has varied whereas firms may or may not continue the production in China, but the main reason to be there is related to the access to the domestic Chinese market (the reasons are numerous and have been covered in previous chapters). This second reason has surpassed in importance the first one.

Our survey confirms this position. When asked for the reasons to be in China, reasons involved included the access to labor cost, access to raw materials, access to Chinese and other Asian markets, detecting business opportunities, follow competitors, or establishing in China as a mandatory requirement. The priority of the results is illustrated below:

Figure 71. Reasons to set up business in China by order of importance

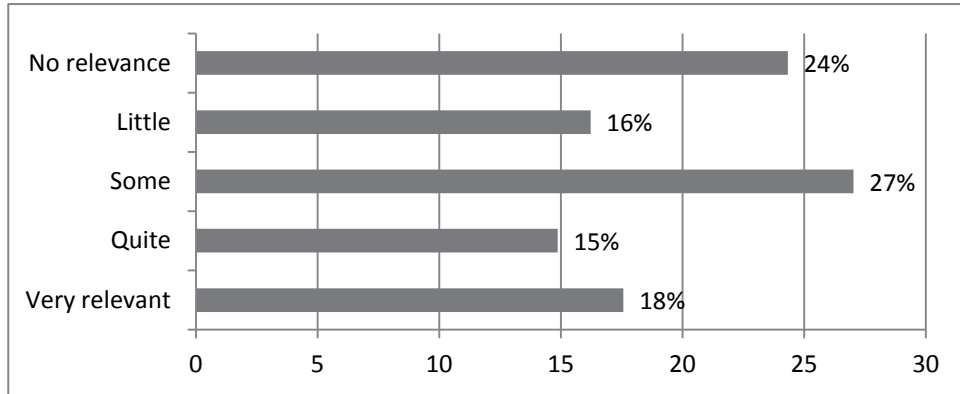


Source: own elaboration

a. Access to labour

We shall analyse in the following pages the importance of each one of the reasons. We shall start by the first one, access to labour, see graph below. While 40% consider this factor has little or no relevance whatsoever, that leaves 60% who believe that it has some or a lot of importance.

Figure 72. Reasons to set up business in China: the importance of labour cost

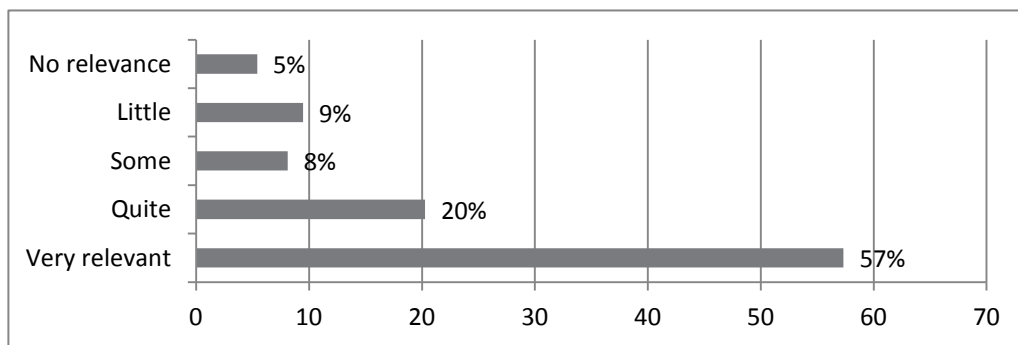


Source: own survey, 2012

For most companies interviewed, the cost of labour has some importance, but contrarily to what it is generally thought, its importance is somewhat limited. In fact, labour cost is only considered as the fifth most important reason, after market access, identification of business opportunities and so on. For a mere 18% of the companies is it considered very relevant: as it can be expected, the great importance has a direct correlation with manufacturing businesses, where labour costs represent currently a competitive edge. Years ago, the importance of labour cost was much higher, due to businesses externalizing their production to China. Nowadays, as the importance of services grows, other reasons become more relevant, as we will see shortly.

b. Access to the Chinese market

Figure 73. Reasons to set up business in China: the importance of accessing the Chinese market



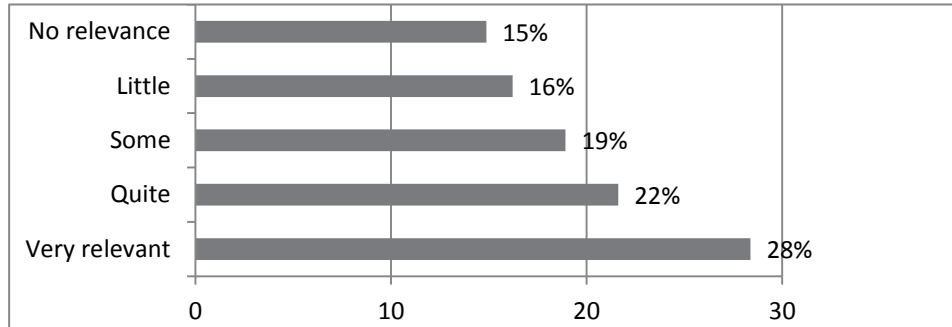
Source: own survey, 2012

Firms consider China as a market full of opportunities: that is why 77% of the firms contemplate market access as either relevant or very relevant when explaining why they set up business in this country. This represents that, more than a world factory, this kind of businesses view China as an interesting market where to commercialize their manufactured products (regardless of where this takes place). This point of view represents a change of mentality which is of enormous importance. From this point, the internationalization strategy will vary accordingly.

c. Access to other markets in Asia

Accessing the markets is always the priority for businesses, the market being China itself or other ones in Asia. For half of the firms surveyed, accessing other Asian markets is very or quite relevant, see graph below.

Figure 74. Reasons to set up business in China: the importance of accessing other markets in Asia



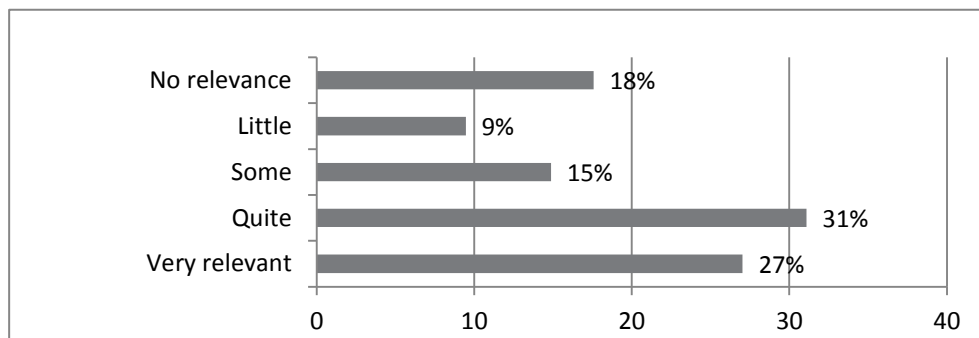
Source: own survey, 2012

d. As a mandatory requirement

The following reason refers to the requirement that is imposed on firms working in industrial strategic sectors in China, where the government or state firms require production or part of the production of foreign companies to be located in China, as a pre-requisite to buying the goods or equipment. Metalocaucho is an example of this requirement: they have set up production plants in China (and in India as well) to be able to access the train component sector. Sourcing directly from Spain was not allowed and the production had to be localised in China.

In this case the answers are more dispersed, because while in some cases this requirement may be crucial, in others (most services for instance) there is no mandatory requirement whatsoever.

Figure 75. Reasons to set up business in China: setting up as a requirement to sell in China

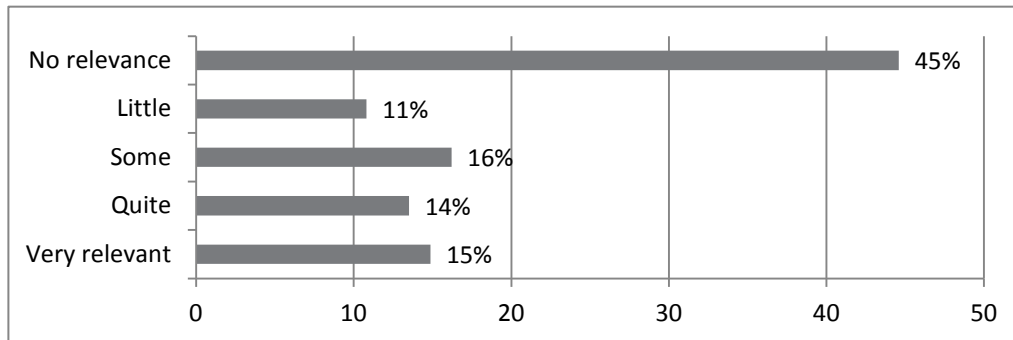


Source: own survey, 2012

e. Access to raw materials

This is the least important of the reasons for most companies. In fact, it is of no relevance or little relevance for over 55% of companies. China is not a country rich in raw materials and it is not the main reason to establish there.

Figure 76. Reasons to set up business in China: importance of accessing raw materials

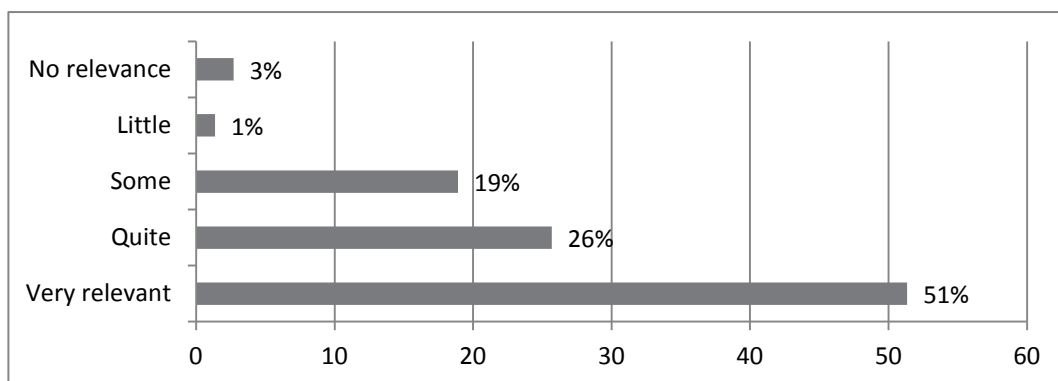


Source: own survey, 2012

f. Detecting new business opportunities

The importance of looking for business opportunities is, after the access to the Chinese Market, the second-most selected answer. It is understandable, because this is a very general reason, business opportunities, which could be related to the growth of the economy, the rising demand, specific businesses that appear at a certain moment, changes in technology, legislation, and so on.

Figure 77. Reasons to set up business in China: the importance of looking for business opportunities

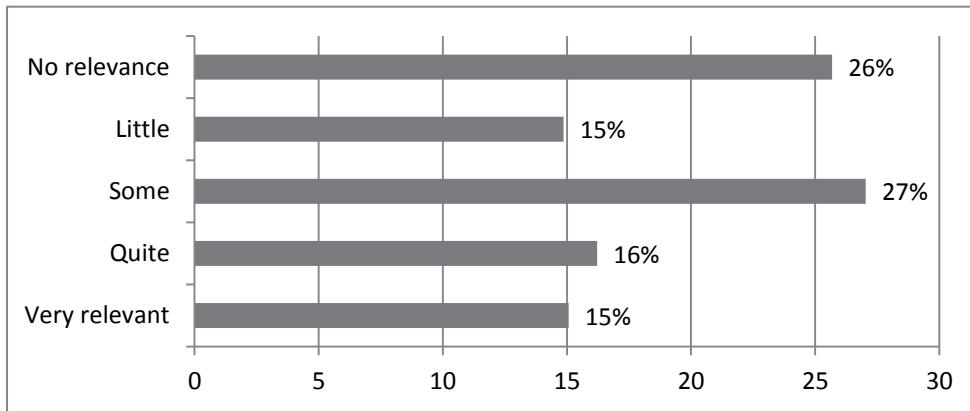


Source: own survey, 2012

g. Strategic move to follow competitors

As a strategy to follow competitors, for 15% it may be very relevant, but it is not considered so in most cases. It has some importance for many, which is natural, but this is not normally a sole reason to establish in a country. It would be an important reason to consider supporting the decision as an additional consideration, but not as the main rationale.

Figure 78. Reasons to set up business in China: the importance of following competitors as a strategic move



Source: own survey, 2012

h. Other reasons

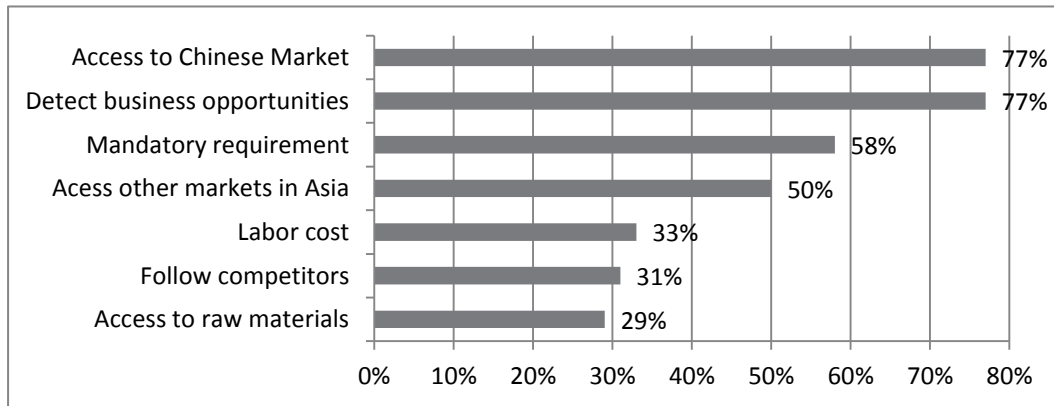
The survey included an open-ended question to give people the opportunity to add other reasons to be in China. Some answers included:

- To follow customers: if one wants to serve customers properly and they are located in China, the full-service supplier is often expected to be there too.
- To get to know new suppliers, that could be used for Spanish headquarters as well.
- To access the Chinese market and get to know it well by following its trends and habits, one has to be physically present.
- To develop projects (as a consultant or as a contractor) one has to be there, physically present and able to do the follow-up
- In the case of the toy sector, world production is centralized in China. All the main customers have their offices in China and purchasing headquarters in Hong Kong, so having a showroom in Hong Kong too makes business relations easier.
- For firms that have outsourced their production, or part of it, to China, it is advisable to have some physical presence in the country in order to follow up the production process and the quality control.

To conclude with the main reasons for setting up business in China, it can be stated that they are, by order of importance: first and most relevant, the market access, whether it is in China or via this country, other Asian markets. Together with this, have a base in China to be able to identify potential business opportunities in this vast country. For some firms, being there is a mandatory requirement to sell, without which, it would not be possible to access the market. On the contrary, accessing resources, whether they are labour cost or raw materials are not considered as relevant reasons for most firms.

The figure below summarizes the reasons given by the interviewees. The percentages represent the sum of each reason being “relevant” or “very relevant”.

Figure 79. Summary of the priorities to set up business in China (percentage= “relevant” + “very relevant” reason)

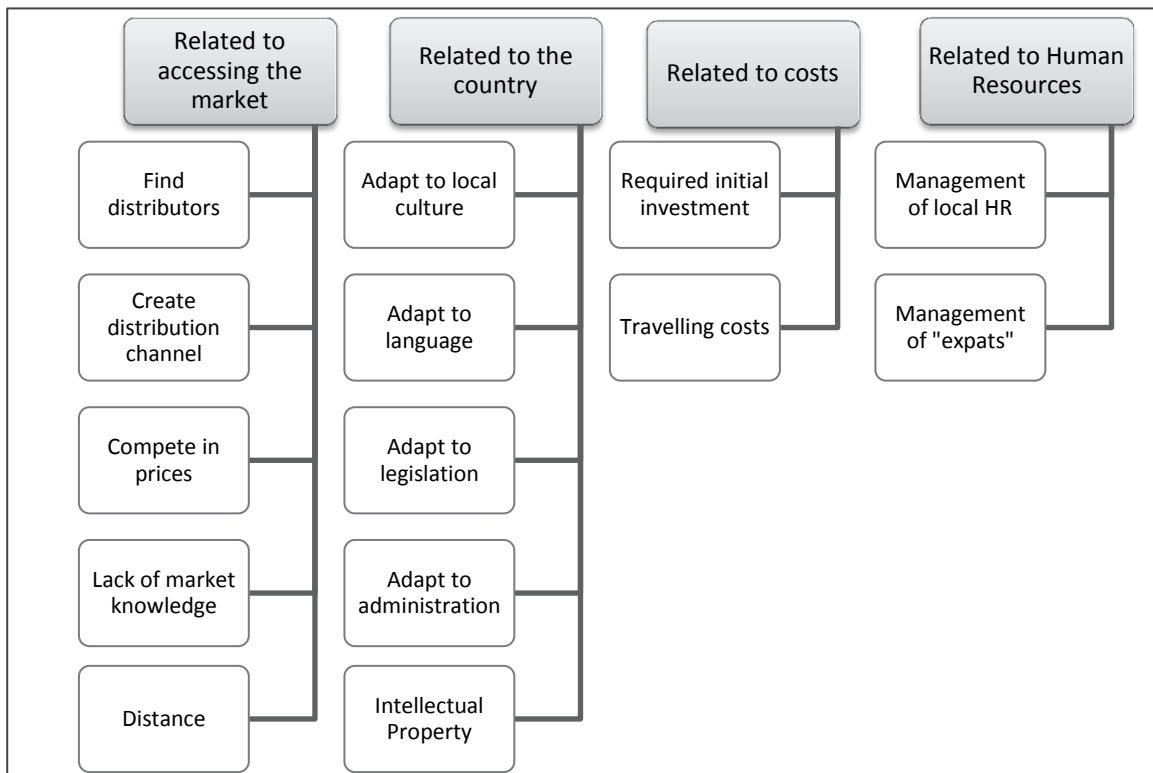


Source: own survey, 2012

4.2. Looking back. Difficulties found when doing business in China

When firms look back, they can identify which were the main complications when they first decided to set up business in this complex country

Table 51. Difficulties establishing business in China



Source: own survey, 2012

The difficulties can be organised around four different factors, as we can see in the figure above: difficulties accessing the market, troubles adapting to the country, cost management and issues concerning Human Resources.

Let's now analyse the answers given, by degree of importance¹⁰¹.

Table 52. Difficulties found when setting up business in China

Difficulty type	Concrete obstacle	Level of difficulty
[1]	Find distributor(s)	*
Related to accessing the market		
	Create a distribution channel	**
	Compete with competitors' prices	**
	Lack of market knowledge	**
	Geographical distance	*
[2]	Adapt to local culture	***
Related to the country		
	Adapt to the language	***
	Adapt to national / local legislation	***
	Adapt to administrative procedures	***
	Intellectual Property (IP)	*
[3]	Required initial investment	*
Related to costs		
	Travelling costs	*
[4]	Local HR	***

¹⁰¹ With the opinions collected by the survey, we have calculated a point system, where:

Difficulty level	Number of points
Not difficult at all	0 points
Little difficulty	1 point
Some difficulty	2 points
Quite difficult	3 points
Very difficult	4 points

Difficulty type	Concrete obstacle	Level of difficulty
Related to Human Resources (HR)		
	Expat HR	**

Level of difficulty:

*: not difficult or little difficulty

** : some or quite difficult

*** : very difficult

Source: own survey, 2012

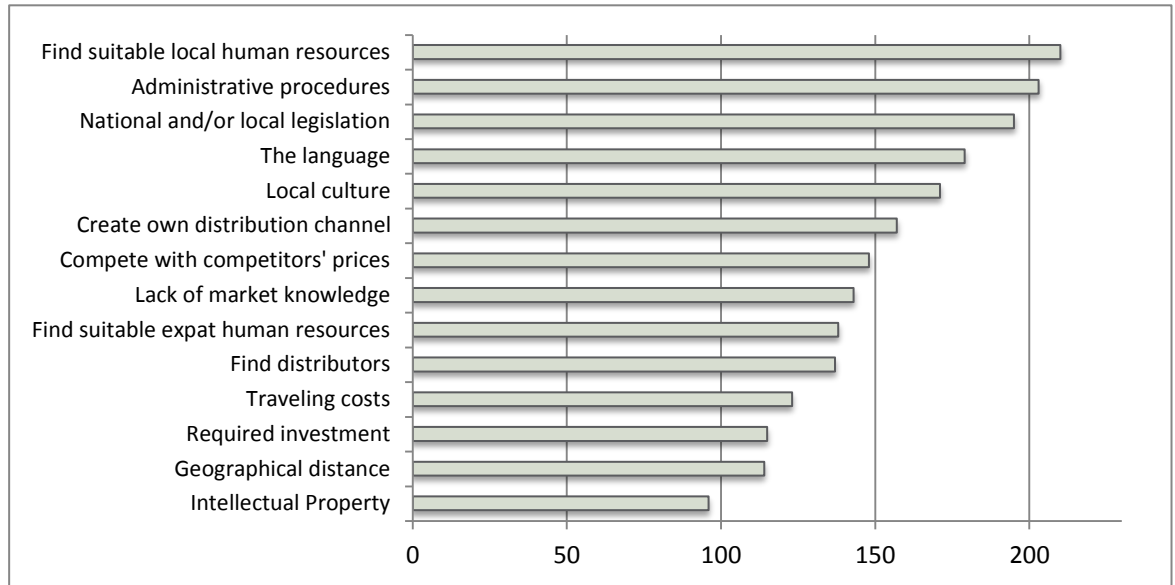
The results below show the level of difficulty of each one of the main obstacles. Concrete difficulties, such as the costs involved due to long geographical distance, or the initial investment, even intellectual property, are not the main concern of the Spanish business people. These are worries that are obviously there, but have solutions.

Any foreign company that wants to have a presence in China should be registered in that country, either as an extension of the national brand, or as a Chinese firm. Since one of the fears of Spanish businessmen is to be copied and counterfeited, registering the brand can be a good remedy. If done properly and timely (which is unfortunately not always the case), the risks are reduced considerably.

In certain sectors, it is imperative to enter via Joint Venture (JV). In that case, it is important to sign a confidentiality and exclusivity agreement for collaboration with the partner. Currently, the number of partners registered at the Spanish House in China exceeds 430.

However, other problems that are more related to the lack of knowledge of the culture, dealing with the legal system or the local authorities, are viewed as the most difficult obstacles. In the middle, we find problems related to the market access: distribution channels, competing in prices in one of the most competitive markets in the world, finding distributors or the lack of market knowledge.

Figure 80. Level of difficulty of the obstacles found when setting up business in China



Punctuation s based on own calculations, the sum of 0 to 4 points depending on the difficulty perceived.

Source: own survey, 2012

Other difficulties explicitly stated by the Spanish companies include:

- Very strong competition in our sector;
- This is probably the most demanding market in the world;
- Since we first set up business in China in 2002 until now, the country has changed enormously. Difficulties vary along time and the difficulty is to adapt to changing difficulties;
- Transferring technical know-how: identify good suppliers of mechanical and technical services that we need and are hard to find.
- Irregularity in the quality of supplies between batches of a same raw material from the same vendor;
- We came too late. By the time we got here, the market share was already allocated to American, German, Italian firms and others. Now it is difficult to break in and gain sales. They have to be stolen from competitors who are very well established in the market;
- If price is a relevant factor to consider in any market, in China this is even more true: price, price & price.

The main conclusion of the survey in this respect is that the main obstacles when setting up business in China are clearly related to the difficulties associated with the country: the culture, the language, the administrative procedures and the legislation. The lack of knowledge of such circumstances are the most important impediments when doing business in China. Related to this is the most difficult aspect of them all: recruiting (and then retaining) suitable local human resources.

Only through the knowledge of the culture, can a western firm be successful doing business in this market. If this is true when working with any new market, it is even more so with China, due to its complexity for Europeans.

4.3. Looking forward: Priorities of Spanish firms in China for the next three years

Thanks to the answers to our survey, twelve priorities are identified by the Spanish business people for the following three years. We will analyse one by one to which extent they were considered to be an absolute priority, not very relevant, or something in between¹⁰². To start with, the diagram below identifies the five top priorities perceived by our interviewees :

Figure 81. Summary of the top priorities as expressed by Spanish business people in China



Source: own survey, 2012

To enter more into detail, we shall present in the following table the different strategies that are planned to be developed in China in the next three years, organised by priority level, as expressed by our interviewees.

¹⁰² With the opinions collected by the survey, we have calculated a point system, where:

Priority level	Number of points
No priority at all	0 points
Little priority	1 point
Some priority	2 points
Quite some priority	3 points
Absolute priority	4 points

Table 53. Levels of priority for Spanish business in China, for the next three years

Priority	Level of priority
Divest from the country	*
Mergers & Acquisitions	*
Outsourcing	*
Invest in R&D	**
Distribution consolidation	**
Implement western culture	**
Expand initial investment	**
Optimise costs	***
Improve quality	***
Enter new markets	***
Brand consolidation	***
Improve customers' satisfaction	***

Level of priority:

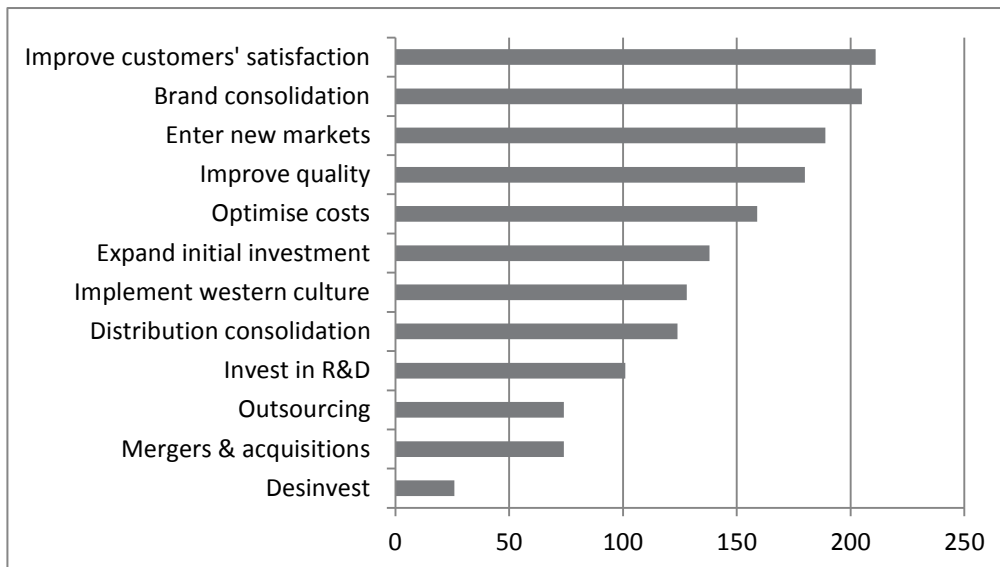
*: no priority at all or little priority

**: some or quite some priority

***: absolute priority

Source: own survey, 2012

Figure 82. Priorities for the next three years for Spanish companies in China



Punctuation s based on own calculations, the sum of 0 to 4 points depending on the priority perceived.

Source: own survey, 2012

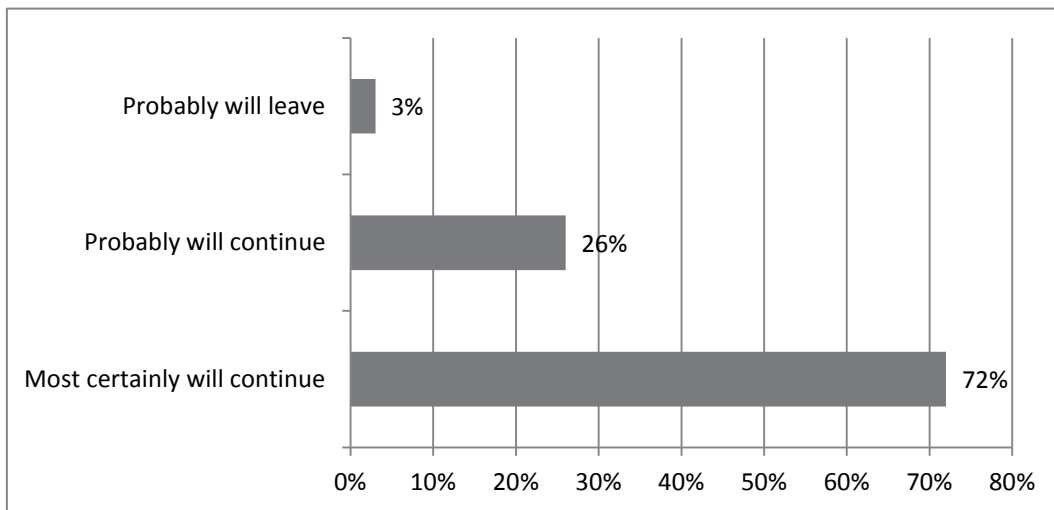
As we can see, main priorities are directly related to the market: improve customers satisfaction, consolidate the brand and open new markets. They are all related to increasing sales. The next ones are related to production subjects, like cost optimisation, quality improvement and expanding investment.

It is interesting to note that for most businesses divesting from China is not at all a priority (as we will see in the next section they want to remain in China), nor are ventures (merging or acquiring other firms), or even outsourcing. Investing in R&D comes quite low as a priority because it is directly related to industrial firms. Firms in services have all given very low (invest in R&D) priorities. However, for the industrial firms it is one of the highest.

4.4. Looking forward: Continuity plans and satisfaction levels

In terms of continuity, the answer is almost unanimous: most Spanish firms surveyed plan to stay in the country in the next three years. 72% think that they will remain for sure, while 26% think it is most probable that they will continue. Only 3% of those questioned have doubts. Perhaps those firms which are planning on leaving the country most likely did not fill in the questionnaire in the first place, but we can see that the level of optimism is rather high. For most companies, coming from a domestic market with a declining demand, to being in a growing market, albeit difficult, is already a remarkable advantage. We can affirm that, following our survey, Spanish firms are in China to stay.

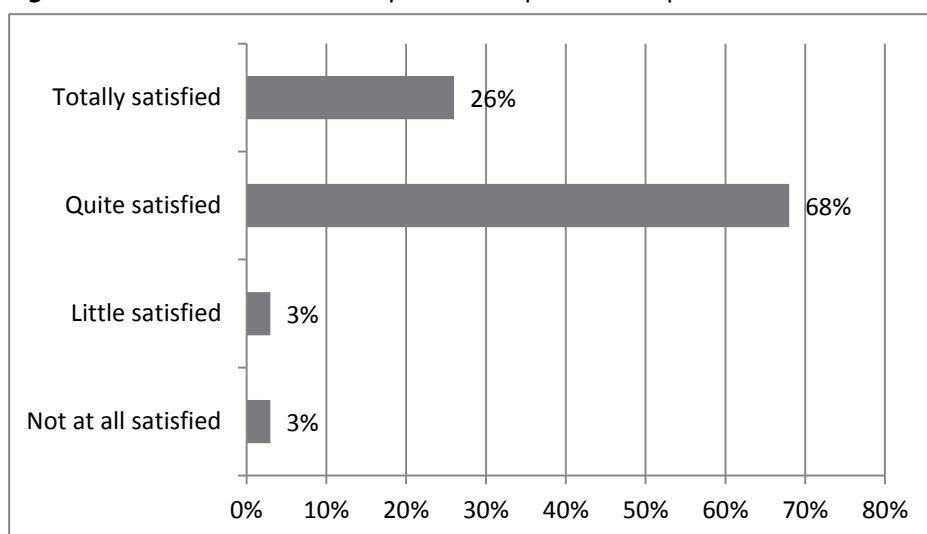
Figure 83. Continuity plans for the next three years. Surveyed Spanish companies in China



Source: own survey, 2012

Most firms will continue because their satisfaction level is high. While only 6% are either not at all satisfied or not satisfied, in general, they perceive the situation as satisfactory (68%) or even very satisfactory (26%). Therefore, overall, we can affirm that due to market opportunities, most firms are satisfied with their development in China and will remain in the country for the coming years.

Figure 84. Satisfaction level of Spanish companies set up in China



Source: own survey, 2012

It is interesting to analyse the reason why firms are satisfied / dissatisfied with the results obtained. The table below includes the answers given by Spanish companies. The reasons for dissatisfaction are related to the obstacles we saw before: high competition, very demanding market, difficult procedures, slowness in yielding results and quality problems.

Table 54. Reasons for satisfaction and dissatisfaction

Reasons for satisfaction with the results	Reasons for dissatisfaction with the results
Sales objectives achieved.	Country with great opportunities but huge price competition. Many difficulties in the beginning.
After a few years with the production in China mostly dedicated to exports, finally the distribution within the Chinese market is starting to develop.	We haven't been able to access the market. We do not sell in China.
We have kept our presence in China for already some 10 years. That is a success in itself.	Certifications for official public processes are very slow and unclear, so it requires a high knowledge of these organisms and very good contacts with the officials internal who draft them
Well-established roots + robust order process = right level of required quality and service	We have taken too long (18 months) to produce good quality with no excessive wastage
China has given us, for more than one quarter of a century, real business opportunities.	We have lost our train. We should have come here some years ago. Now the access is very hard because the market is mature.
Positive economic results.	

Reasons for satisfaction with the results	Reasons for dissatisfaction with the results
We have managed to adapt to the market.	
Expectations are being met, and we have not found significant variations, neither upward nor downward.	
The volume of Chinese business is not very important compared to other countries of the European environment, but we have seen the opportunity to not only consolidate our services but to attract Chinese customers with interests in Spain. This last option has a great potential for the future.	
Expectations have been met: not only to consolidate our services for the Spanish companies but the recruitment of a growing critical mass of Chinese investment in Europe and South America.	
Since our company moved production to China and we created a Trade Office in Hong Kong (the latter in 2005), the company turnover has multiplied by four.	
<ol style="list-style-type: none"> 1. Big network in China, covering tier 1,2,3 cities. 2. Development of a geographical advantage in China to explore new connections, e.g. China and East Europe. 3. Good brand reputation in China. 	
After the effort of many years now we are consolidating and reaping the benefits. The market is growing and it is an opportunity.	
Great market potential that translates into increases in sales and profits	
The project started in 2006 and by 2010 all the different product and service lines had consolidated.	
The growth of sales and profits, as well as opportunities for present and future business in the local market and markets of the Asian area	
Satisfied because we have achieved recognition as one of the main Spanish consulting firms specializing in China, along with the consolidation of a world-class team, and a volume of projects which are economically viable.	
The results are improving year-on-year, allowing us to increase our presence and there are good signs for growth for the next five years	
Production costs are under control.	
China has become the backbone of our activity.	
In our segment there was an unmet need that we have filled.	

Reasons for satisfaction with the results	Reasons for dissatisfaction with the results
Without support from any State agency or bank loans we have succeeded in turning a profit in 2 years.	
We have achieved the objectives in a progressive and serious manner.	
The benefits we have obtained are more intangible than money. You just have to be there.	
It has been an important opportunity for our company in Spain to become a reference in the management of Chinese projects but it is still difficult to compete in the local market here.	
This is not the goose that lays the golden eggs. Competing with local plus international companies is increasingly more difficult. The results are positive but not grandiose.	
Satisfied by positive results, in the sense that more investment is not required and production has improved. However, we are not satisfied because the yield is very low and quality is still a problem.	
Although the relationship with China began in 2005 through a representative office, in 2008 it became a WFOE (Wholly Foreign Owned Enterprise). The purpose of this company was the manufacture of certain components, but also the creation of a platform with all Chinese human resources and materials, for expansion in the country and elsewhere in the environment. To date, we believe that we have managed to create this necessary local platform, although it does still not give desirable benefits. All this is against the backdrop of the current global crisis.	

Source: own survey, 2012

In terms of reasons to be satisfied, the main ones can be classified as:

- In the first place, the opening opportunities that have allowed for increasing sales and profits. For many, being in China has compensated for a declining domestic market of Spain (or the EU);
- Interesting connections from China to other strategic areas of the world, such as other Asian countries, Eastern Europe or Latin America;
- Intangible results in terms of recognition, reputation, know-how, beneficial not just for the Chinese operations, but also for future business elsewhere.

4.5. Final balance of the Chinese business experience: best practices.

As a last question, Spanish firms were asked what they thought they had done right to access the Chinese market. The answers were extremely rich and varied. Most of them agree that the choice of the staff (whether it is the expats or the local Chinese staff) is the key factor to have a successful venture. The emphasis is mostly put on the local staff: choose the right people, train them, give them autonomy to develop projects, integrate the staff in a western approach of business, and make the most of local personnel to act on all the problems related to the Chinese environment, which is not readily-accessible to foreigners.

On top of having competent and trained local human resources, it is very important to develop a solid *guanxi*. In many cases establishing alliances with local partners is

also a great advantage. There has been an evolution in terms of the choice of legal form: it has always been very common to start doing business in China with a Representation Office. Afterwards, if a firm wants to invoice and grow, it will have to decide between establishing a WFOE (Wholly Foreign Owned Enterprise) or a Joint Venture (JV). A decade ago, it was more frequent to choose a JV, first, to have a local partner that would make business in the country easier but also because it was compulsory from a legal point of view. As the government allowed the creation of foreign capital firms in the next years, businesses chose the WFOE so as to be more independent and avoid potential problems with Chinese partners. However, the trend in the last few years, according to some experts, is to move back to the JV model. In a country like China, so different to the Western countries, with such a great importance of social relations, with a culture that impregnates all aspects of business, having a local partner can be invaluable.

Following the section above, another influencing factor that is repeated by most firms is related to culture: avoid a culture shock, elude confrontation and instead, choose an approach that enriches both cultures. Learn, immerse oneself in the Chinese culture, try to adapt to it, respect it and understand it, and, as it has been stated: “approach the country with respect and humility”. Moreover, realize that it is not about subtracting or even adapting totally to the Chinese culture. Instead, it is about keeping the original western business culture (especially concerning quality and efficiency) but adapting it to the Chinese culture, habits and uses.

Flexibility is another factor which has importance attached to it by the Spanish firms, and it refers to many fields, in particular, being flexible with the culture, with the pace of changes, with market peculiarities. In a world that is in a process of turbulent changes, the ability to adapt to changes can be the source of a competitive advantage. In China, where changes go much faster, it is the only way to survive.

Another value that seems to be particularly relevant for China and is frequently mentioned is patience: endurance in front of the obstacles and allow the project enough time because results in China take time to show. Related with patience is perseverance, to keep on going even when circumstances look adverse.

In terms of a concrete market approach, it also means to adapt the product and services to local habits. Plan a correct product diversification to match the needs of the Chinese market. Approach the customers candidly and openly, not taking anything for granted. Allow time for negotiations and search for mutual understanding. Aim for the correct positioning of the product or service. Guarantee at all times the quality and efficiency of the deliveries.

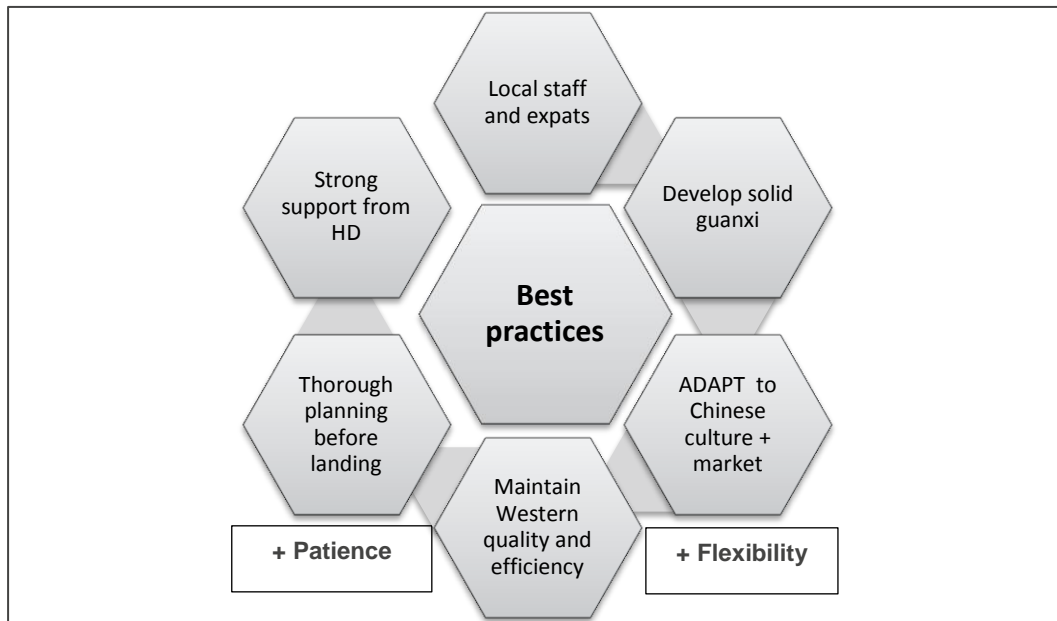
In terms of strategy from headquarters, we find two factors are the most relevant. In the first place, planning: plan the implementation strategy, program the project kick-off. Get the best assessment one can find to study the market, study the production alternatives, the partners and the implementation of the resources needed. The planning process may take a while and it will probably require some resources. It is important to invest the time and money in this first phase, which will generate future benefits. Secondly, it is very important to consider the Chinese venture as

something strategically aligned with the headquarters and the core objectives of the business. Believe in the project and firmly support it. Send experienced expats from the beginning. The support must be multi-functional: management, commercial, technical. Some large companies even implement a Helpdesk to allow frequent exchanges between China and Europe.

China is a complex and very competitive market. It is also a vast territory, and it requires a physical presence. To do regular business in China, frequent travelling is not enough: it is necessary to localize. Even if one chooses the most simple of legal forms such as the Representation Office, at the very minimum it provides the opportunity to the Spanish firm to have a first-hand market view, a foot on the ground so necessary to choose suppliers, find alliances, establish partners, create a distribution channel, etc.

The following best practice is perhaps the most difficult one, or even impossible to achieve, for companies which are not in China yet. Many firms consider it their advantage that having been in China already a few years is the key to their success today. Some believe that nowadays it is too late and the resources needed would be too high. The market is too mature and large multinationals are already very established. However, even if it is true that the East of China is a difficult territory to start with due to the competitiveness of the market, opportunities are still arising in second and third tier cities.

Figure 85. Summary of best practices setting up business in China, according to Spanish firms



Source: own survey, 2012

Many firms are established in China. Many are doing great business. Some others are struggling. What is sure is that it is not easy, but there are plenty of opportunities. Often we hear sentences like “China is only accessible by large firms”.

It is true that there are many large national champions earning money in China like Inditex, Gamesa, Roca, Mango, Torres, and many others. It is also true that they have more resources at their disposal to spend on an initial investment and to adapt to the very different Chinese business culture. Time spent planning and time allowed before expecting results is also a rare resource not always affordable for the small ones.

Small firms start with a different set of conditions: their resources are limited, both in time and money. Their access to expert human resources is limited. Their capability to adapt to such a vast country is somehow restricted. Do we have to conclude then that the Chinese market is only for the *big and the beautiful*? This writer does not think so. On the contrary, we have proved in this survey that:

- There are compelling reasons to have a physical presence in China, where accessing the market is more relevant than accessing cheap labour costs (this is especially true for services);
- There are many difficulties - that is for sure - but most firms want to continue in China in the coming years;
- The opportunities are there in many different sectors: food and wine, equipment and machinery, professional services, infrastructure, tourism, anything that involves technology, anything that offers a valuable brand, water treatment, renewable energies, gastronomy and hotel and restaurant management, education, and many more;
- There is a set of best practices that firms are advised to follow. Firms that do so can increase their chances of success enormously. These practices are not just for large firms, but applicable for small ones.

Accessing the Chinese market is not easy, as we have seen. But we feel we have proved that it can be done. We will finish with a sentence that represents very well the difficulty and dangers that it involves: “entering the Chinese market is like opening your first company. You have no idea of what is happening and everything looks like the Wild West”¹⁰³.

¹⁰³ From Bowei Gai, co-founder of CardMunch, later acquired by LinkedIn.

VII. CONCLUSIONS

China, most notably since its accession to the World Trade Organisation in 2001, has embraced the rules of a market-based economy (socialism with Chinese peculiarities). Even if there are still major reforms and challenges to be undertaken, it has become the world's second economic power with an important role to play on the international scene.

China no longer wants to be the world's factory, or at least it wants to be a lot more than that. The Chinese are very patriotic, they see themselves as "the middle kingdom" and that is how they feel towards the world. At the same time, that is how they wish for the world to perceive them: as the centre of the universe. The fact that China is becoming a global power comes as a very natural fact for the Chinese population, as they believe that this is the position they deserve to occupy.

Taking into account these previous considerations, we have studied the access to the Chinese market: the challenges and best practices of Spanish firms in this vast country. The present research has carried out an extensive literature review on China, followed by substantive research on quantitative and qualitative data. Other qualitative information has been collected from interviews done in China, Spain and Hungary to experts on Chinese economy, foreign trade, firms operating in China and public institutions. Last but not least, a survey has been conducted among the Spanish firms that are based in China.

With all these sources of information in place, **we have been able to answer to our three initial hypotheses:**

H1- Accessing the Chinese market requires that foreign firms in general, and Spanish ones in particular, adapt their products or services to this specific market. **This hypothesis has been confirmed.**

Contrary to T. Friedman's opinion, the world is not flat. In fact national differences still matter to a great extent. When a company tries to access a new market, it needs to adapt to it, and it needs to understand thoroughly the culture in which it operates. This statement is perhaps true in China more than anywhere else in the world.

The main obstacles when setting up business in China are clearly related to the difficulties associated with the country: the culture, the language, the administrative procedures and the legislation. The lack of knowledge of such circumstances are the most important impediments when doing business in China. Related to this is the most difficult aspect of them all: recruiting suitable local personnel. Only through a deep knowledge of the culture, can a western firm be successful doing business in this market. If this is true when working with any new market, it is even more true with China, due to its complexity for Westerners.

In terms of a concrete market approach, it is necessary to adapt the product and services to local habits. To plan a correct product diversification to match the needs

of the Chinese market, one should approach the customers frankly and openly, not taking anything for granted, allow time for negotiations and search for mutual understanding. It is extremely important to position the products (or services) correctly and guarantee at all times the quality and efficiency of the deliveries.

Failing to adapt correctly to the specifics of the Chinese market can result in failure and significant losses of money and time. The adaptation should not be restricted to the products or the services but should constitute a much wider approach: adapt to their culture, their negotiation peculiarities and their strategic management mindset.

H2- China offers an attractive market made up of many consumers and a significant emerging middle class. Spain is not taking advantage fully of this opportunity.

This hypothesis has been confirmed.

China represents today perhaps the most attractive potential emerging market in the world. Many indicators coincide on this: a thriving GDP, a growing urban population, a burgeoning middle class (estimated at 670 million persons by 2021) and an increase in both private and public spending. The image of the “little emperor” or the so-called “me-generation” comprising of the only-child-family is a good example of a middle class willing to spend and consume pretty much everything.

China is the world’s largest exporter, having overtaken Germany in 2009, and the second importer. In the world ranking, Spain occupies number 21 for China’s exports, while it occupies spot number 36 as an importer (a very low position in the ranking). In fact, imports to Spain are still five times larger than its exports. However, the difference is changing favourably towards Spain year by year, slowly but surely. Spanish exports grew by 32%, in 2011, and imports grew by only 2%. As such, even if the trade balance is still very negative for Spain, the situation is shifting. Along with this trade picture, we can appreciate an important growth of Foreign Direct Investment of Spain in China in 2010 and 2011 (after dropping dramatically in 2008 and 2009 due to the recession in Spain). This will be source of future exports.

It is true fact that many Spanish firms have been successful in China. It was not until the 90s, and even after 2000, when a significant amount of Spanish businesses decided to establish a permanent base in the country. Four veteran companies in this market - ALSA, Técnicas Reunidas, Nutrexpa and Bodegas Torres - and two companies that have arrived relatively recently - Gamesa and Inditex - constitute the core of a business presence that has produced some very positive results.

The presence of Spanish companies in China has grown by 70% in the last three years despite the legal insecurity, the geographical distance and other obstacles. Currently, it is estimated that more than 500 companies, mostly SMEs, are present in China or do regular trade with this country. They were forced to do so when they saw their domestic market vanishing to due economic recession. These include, in addition to the six mentioned above, other highly recognised ones such as Mango,

Roca, Cosentino, Santander, Telefonica, Mapfre, Acciona, Indra, Fagor, Nutrexpa, Simon or Freixenet, to name but a few.

However, apart from these highly recognised brands, there are many other smaller firms that operate in China and are not so visible to the public. The main sectors where they operate are related to fashion, design, habitat, food and wine, tourism and leisure, renewable energies, equipment and machinery, banking and finance or education. It is clearly not enough, but it is a good start.

In general, it can be stated that Spanish firms have been relatively late to access this market, if we compare them to other EU countries such as Germany, France, United Kingdom or Italy, physically present in the country many years before. Spain has generally been more connected to other world areas such as the EU, for geographical reasons, or Latin-American, for cultural reasons. Asia has been historically ignored, unknown, feared and neglected. Therefore we can conclude that Spain is not yet exploiting fully the opportunities that are opening in China. However, there is room for optimism when we look at the evolution and future potential.

H3- Accessing the Chinese market is full of obstacles: it requires a significant investment, skilled staff, a long time payback period, much patience and endurance. Therefore, it is a market only accessible for large firms.

This hypothesis has not been confirmed.

In order to be able to confirm or dismiss the above, a survey has been carried out to help draw a profile of Spanish firms operating in China: why they set up business in China, what were their main obstacles, sectors and sizes, their priorities for the next years and the best practices learned after the process.

As stated before, some large and highly recognised Spanish brands are being very successful in China. But there are also hundreds of smaller ones that operate fruitfully in China in all sectors. The survey has confirmed that there are important chances for success independently of the size. The crucial question is to have a very clear strategy for the start up. The strategy is captured in a set of best practices that we will see below. Therefore we can conclude that it is not mainly about size (even if that can help at times) but about having a clear strategy.

The next paragraphs summarize the main conclusions derived from the survey:

Spanish firms operating in China are mostly in the services sector (56%), and particularly in the areas of professional services, such as advertising, legal advice, consulting, quality control, etc. The remaining 44% operate in different industries: metal, machinery and equipment, food and beverages, textiles, vehicles and transportation and other manufacturing industries. Increased presence of Spanish firms is noticeable in hi-tech sectors, project management, engineering in energy and renewable energies, water treatment, waste disposal, and also in services, art, education and culture.

Companies' activity sectors are often correlated to their region of origin in Spain. Thus, businesses from Madrid are very often related to strategic sectors operating in Beijing. Businesses from Catalonia are either dominated by the chemical sector, some consumer goods and many professional services. Most of the Basque firms are operating with metal, machinery and industrial goods. Companies based in Valencia are often related to trade and consumer goods, and the Andalusian ones with food and food related products.

It is also interesting to note that there are more and more firms that declare no origin in Spain: these are firms born global, founded by Spanish business persons who are living in China. They are mostly small businesses, dedicated to give professional services to western firms in China and they are mostly active in the Shanghai area.

Almost half of the Spanish businesses establish themselves in the Shanghai area, due to its economic power, but also thanks to the attractiveness of its cosmopolitan atmosphere and the high percentage of foreigners residing in this city. Although recruiting and retaining "expats" is difficult in China, it becomes easier in the case of Shanghai. The Beijing area offers many opportunities due to its capital status and it is certainly more relevant for certain strategic sectors where contacts with the government are especially important. Regarding the south of China, we are referring mostly to the coastal eastern areas around Guangdong. The proximity to Hong Kong has helped the development of production facilities that manufacture goods that satisfy the demand for cheap products in the EU.

Why do Spanish companies establish a subsidiary in China? The main reasons for setting up business in China are, by order of importance: access to the market, whether it is China or other Asian markets using China as a base. Together with this, having a base in China is a platform to detect potential business opportunities in this vast country and Asia. For some firms, being physically here is a mandatory requirement to sell, without which it is not possible to access the market. On the contrary, accessing resources, whether they are labor cost or raw materials are not considered as relevant reasons for most firms.

Our survey assesses what are the priorities for Spanish firms in China for the next three years:

- In the first place, improve customers' satisfaction, consolidate the brand and open new markets. They are all related to increasing sales;
- In the second place, improve production related matters, such as cost optimisation, quality enhancement and increased investment;
- Finally, for most businesses divesting from China is not at all a priority.

In terms of continuity, the answer is almost unanimous: most Spanish firms plan to stay in the country for the next three years. 72% think that they will remain for sure, while 26% think it is most probable that they will stay. Only 3% have doubts. For most companies, coming from a domestic market (Spain) with a declining demand,

being present in a growing market, albeit a difficult one, is already a significant advantage. Spanish firms are in China to stay.

Most firms will continue because their satisfaction level is high. While only 6% are either not at all satisfied or only a little satisfied, in general, they perceive the situation as satisfactory (68%) or even very satisfactory (26%). Therefore, overall, we can state that thanks to market opportunities, most firms are satisfied with their development in China and will remain in the country for the coming years.

As a last question, Spanish firms were asked what they thought they had done right to access the Chinese market. The answers were extremely rich and varied. Most of them agree that the choice of the staff (whether it is the expats or the local Chinese staff) is the key factor to have a successful venture. The accent is mostly put on the local staff: choose the right people, train them, give them autonomy to develop projects, integrate the staff in a western approach of business, and make the most of local personnel to resolve the problems related to the Chinese environment, which is not accessible to foreigners.

As well as having competent and trained local human resources, it is very important to develop a solid *guanxi*. In many cases establishing alliances with local partners is also a great advantage.

Flexibility is another factor heavily weighted by Spanish firms, and it refers to many fields, in particular, being flexible with the culture, with the pace of change, with market peculiarities. In a world that is in a process of turbulent changes, the ability to adapt to change can be a source of competitive advantage. In China, where changes happen much faster, it is the only way to survive.

Another value that seems to be particularly relevant for China and is mentioned frequently is patience: endurance in front of the obstacles and to allow the project enough time because results in China take time to show. Related to patience is perseverance, to keep on going even when circumstances look adverse.

In terms of strategy from headquarters, we find two factors are most relevant. In the first place, to plan carefully the implementation strategy. Very often that implies getting the best assessment one can find to study the market, study the production alternatives, the partners and the implementation of the resources needed. Secondly, it is very important to consider the Chinese venture as something strategically aligned with the headquarters and with the core of the business. Believe in the project and firmly support it. That involves sending experienced expats from the beginning and giving a multi-faced support: executive, commercial and technical.

Finally, we conclude that the world is moving at a turbulent pace and firms try to adapt quickly to those changes. If in the recent past western firms moved to China to access their cheap labour, nowadays they try to access their growing market. Opportunities are opening thanks to a rising middle class that is ready to consume. The access is difficult and full of obstacles. At the same time, short term profits are

not easily available. But opportunities are there for Spanish firms of all sectors and sizes. With rigour and following the best practices mentioned above, objectives can be reached. China is there to stay and Spanish firms are in China to stay.

Three proposals to end the conclusions:

1. Country branding:

Countries compete daily with neighbours and regions for tourism, inward investment and sales. Spain is a country with 47 million people, while China counts with 1.3 billion. The brand of Spain is competing with all the other European countries, but it is insufficiently known in China. In order to boost Spain's commercial success, it is crucial to create a branding program that strengthens the brand of Spain. This requires the ability to act and speak in a coordinated and repetitive way about themes that are the most motivating and differentiating a country can make. Spain was late to come to China and it remains an unknown and far-away country, more recognised by its sports than by its businesses or technology. To change the perception and promote the country branding, it is necessary to have the cooperation and involvement of all stakeholders, including representatives of government, business, the arts, education and, very importantly, the media.

2. Tourism:

There are opportunities in many economic sectors, such as renewable energies; water; project management; technology and equipment, e-commerce, food, wine or olive oil. But moreover, there is a large opportunity in tourism, attracting Chinese visitors to Spain. Not so much the so-called *sun & sea* tourism, but a more quality, cultural and shopping kind of tourism towards the cities. In this sense all the efforts should be combined to steer Chinese tourists who wish to come to Europe, to consider Spain as a must-stop in their tour.

3. Business policy and Strategic Management:

The beginning of the decade 2000s saw a sudden "fashion" for Spanish businesses to move to China. Many SMEs went to China in "pseudo-business" trips to explore, look and do tourism. This gave way to genuine disasters: wrong contracts were signed, rush businesses with no future were attempted. Fortunately, the recession acted as a "cleaning" agent that made clear who was in China as a real business strategy, compared to those who were there for the wrong reasons. Businesses must set up business in China only if (1) that corresponds to a strategic decision, (2) the project is planned properly in advance, (3) resources are given and (4) the company leadership is therefore totally committed. Any other adventures are not at all to be advised.

VII. CONCLUSIONES

China, sobre todo desde su adhesión a la Organización Mundial del Comercio en 2001, ha adoptado las reglas de una economía basada en el mercado (un modelo socialista con peculiaridades chinas). Aunque es cierto que aún quedan importantes reformas y desafíos que deben emprenderse, China se ha convertido en la segunda potencia económica mundial, con un papel importante que desempeñar en la escena internacional.

China ya no quiere ser la fábrica del mundo, o al menos quiere ser mucho más que eso. Los chinos son muy patriotas, y se ven a sí mismos como "el reino del medio". Perciben su país como el centro del universo. El hecho de que China se esté convirtiendo en una potencia mundial se presenta como un hecho muy natural para la población china, que considera que ésta es la posición que se merece ocupar.

Teniendo en cuenta las anteriores consideraciones, se ha estudiado el acceso al mercado chino: los retos y las mejores prácticas de las empresas españolas en este vasto país. La presente investigación se ha llevado a cabo mediante una extensa revisión bibliográfica sobre China, seguida por una investigación a fondo sobre los datos cuantitativos y cualitativos. Se ha recogido información también a través de entrevistas hechas en China y Europa a expertos en economía china, comercio exterior, empresarios que operan en China e instituciones públicas. Por último, pero no menos importante, una encuesta se ha realizado entre las empresas españolas que cuentan con sede en China.

Con todas estas fuentes de información, hemos podido responder a nuestras tres hipótesis iniciales:

H1-El acceso al mercado chino requiere que las empresas extranjeras en general, y las españolas en particular, adapten sus bienes o servicios a este mercado específico. **Esta hipótesis ha sido confirmada.**

Contrariamente a la opinión T. Friedman, el mundo no es plano. De hecho, las diferencias nacionales y regionales siguen siendo importantes en gran medida. Cuando una empresa intenta acceder a un nuevo mercado, tiene que adaptarse a él, y es necesario entender a fondo la cultura en la que opera. Esta afirmación es cierta en China más que en ninguna otra parte del mundo.

Los principales obstáculos al establecimiento de empresas en China están claramente relacionados con las dificultades asociadas al país: la cultura, el lenguaje, los procedimientos administrativos y la legislación. La falta de conocimiento de estas circunstancias constituye el obstáculo más importante a la hora de hacer negocios en China. En relación con esto, el aspecto más difícil de todos es reclutar recursos humanos locales. Sólo a través de un profundo conocimiento de la cultura, una empresa occidental puede llegar a realizar un negocio exitoso. Si bien esto es cierto cuando se trabaja con cualquier mercado nuevo, es aún más cierto en China, debido a su complejidad para los europeos.

En términos de cómo acercarse en concreto al mercado, es necesario adaptar los bienes y servicios a los hábitos locales: planificar una correcta diversificación de los productos que satisfagan las necesidades del mercado chino, acercarse a los clientes de manera franca y abierta, no dar nada por sentado, dar tiempo a las negociaciones y buscar la comprensión mutua. Es muy importante colocar la oferta correctamente y garantizar en todo momento la calidad y la eficiencia de las entregas.

Si una empresa no logra adaptarse correctamente a las características específicas del mercado chino, puede acabar fracasando y perdiendo importantes sumas de dinero y tiempo. La adaptación no debe limitarse a los bienes o servicios, sino que constituye un enfoque mucho más amplio: adaptarse a su cultura, sus peculiaridades en la negociación y la gestión estratégica.

H2- China es un mercado atractivo compuesto de muchos consumidores y una significativa clase media emergente. España no está aprovechando plenamente esta oportunidad. **Esta hipótesis ha sido confirmada.**

China representa hoy en día quizá el mercado emergente más atractivo del mundo. Muchos indicadores coinciden en esto: un PIB próspero, una creciente población urbana, una pujante clase media (estimada en 670 millones de personas en 2021) y un aumento en el gasto privado y público. La figura del "pequeño emperador" o la llamada "generación del yo" son buenos ejemplos de una clase media dispuesta a gastar y consumir de todo.

China es el mayor exportador mundial, después de haber superado a Alemania en 2009, y el segundo importador. En el ranking mundial, España se posiciona como el país número 21 en cuanto a destino de las exportaciones de China, mientras que ocupa el puesto 36 como proveedor de China (es decir, una posición muy baja). De hecho, las importaciones de España siguen siendo cinco veces mayores que sus exportaciones. Sin embargo, la diferencia está cambiando favorablemente hacia España año tras año, sin prisa pero sin pausa. Si bien las exportaciones españolas crecieron un 32%, en 2011, las importaciones crecieron en solamente el 2%. Por lo tanto, incluso si la balanza comercial es todavía muy negativa para España, la situación está cambiando. Junto a este panorama comercial, se aprecia un importante crecimiento de la Inversión Extranjera Directa de España en China en 2010 y 2011 (después de caer drásticamente en 2008 y 2009 debido a la recesión en España). Esto será motivo de futuras exportaciones.

Puede afirmarse que muchas empresas españolas han tenido éxito en China. No fue hasta los años 90, e incluso después de 2000, cuando una cantidad significativa de empresas españolas decidieron establecer una base permanente en el país. Cuatro empresas veteranas en este mercado - ALSA, Técnicas Reunidas, Nutrexpa y Bodegas Torres - y dos compañías que han llegado hace relativamente poco tiempo - Gamesa e Inditex - constituyen el núcleo de oro de una presencia comercial que ha producido algunos resultados muy positivos.

La presencia de empresas españolas en China ha crecido un 70% en los tres últimos años a pesar de la inseguridad jurídica, la distancia geográfica y otros obstáculos. En

la actualidad, se estima que más de 500 empresas, la mayoría pymes, están presentes en China o comercian regularmente con este país. Se vieron obligadas a hacerlo cuando sufrieron la caída de la demanda interna debido a la recesión económica. Estas empresas incluyen, además de las seis mencionadas anteriormente, otras altamente reconocidas, como Mango, Roca, Cosentino, Santander, Telefónica, Mapfre, Acciona, Indra, Fagor, Nutrexpa, Simón o Freixenet, por nombrar sólo algunas.

Sin embargo, aparte de estas marcas altamente reconocidas, hay muchas otras empresas más pequeñas que operan en China y no son tan visibles para el público. Los principales sectores en los que operan están relacionados con la moda, el diseño, el hábitat, la gastronomía y el vino, el turismo y el ocio, las energías renovables, equipos y maquinaria, la banca y las finanzas o la educación. Evidentemente, no es suficiente, pero es un comienzo.

En general, se puede afirmar que las empresas españolas han acudido relativamente tarde a este mercado, si las comparamos con otros países de la UE como Alemania, Francia, Reino Unido o Italia, que estuvieron físicamente presentes en el país muchos años antes. Las empresas españolas han estado en general más conectadas con otras zonas del mundo, como la UE, por razones geográficas, o de América Latina, por razones culturales. Asia ha sido históricamente ignorada, desconocida, temida y descuidada. Por lo tanto, podemos concluir que España aún no está aprovechando plenamente las oportunidades que se están abriendo en China. Sin embargo, hay optimismo cuando nos centramos en la evolución y el futuro potencial.

H3- El acceso al mercado chino está lleno de obstáculos: se requiere una inversión significativa, personal capacitado, un período de recuperación largo, mucha paciencia y perseverancia. Por lo tanto, se trata de un único mercado accesible solo para las grandes empresas. **Esta hipótesis no ha sido confirmada.**

Con el fin de poder confirmar o descartar lo anterior, se ha llevado a cabo un estudio para ayudar a trazar el perfil de las empresas españolas que operan en China: por qué establecieron su negocio en China, cuáles fueron sus principales obstáculos, sectores y tamaños, sus prioridades para los próximos años y las mejores prácticas aprendidas tras el proceso.

Como se ha dicho antes, algunas marcas españolas grandes y altamente reconocidas gozan de gran éxito en China. Pero también hay cientos de otras más pequeñas que operan en China en todos los sectores, de forma fructífera. La encuesta ha confirmado que hay posibilidades importantes para el éxito independientemente del tamaño. La cuestión principal es tener una estrategia muy clara para la puesta en marcha de la empresa. Esta estrategia debe materializarse en un conjunto de buenas prácticas que veremos a continuación. Por lo tanto, podemos concluir que no se trata principalmente una cuestión de tamaño (aunque esto pueda ayudar), sino de tener una estrategia clara con ciertos requisitos.

Los párrafos siguientes resumen las principales conclusiones derivadas de la encuesta:

Las empresas españolas que operan en China son en su mayoría de servicios (56%), y en particular operan en las áreas de servicios profesionales, tales como la publicidad, el asesoramiento legal, la consultoría, el control de calidad, etc. El restante 44% opera en diferentes sectores: metal, maquinaria y equipos, alimentos y bebidas, moda, vehículos y medios de transporte y otras industrias manufactureras. Incrementa últimamente la presencia de empresas españolas en sectores de alta tecnología, gestión de proyectos, ingeniería en energías renovables, tratamiento de agua, eliminación de residuos, así como en los servicios, el arte, la educación y la cultura.

Los sectores de actividad de las empresas suelen estar relacionados con su región de origen en España. Así, empresas de Madrid están muy a menudo relacionadas con sectores estratégicos que operan en Beijing. Las empresas de Catalunya se encuentran en el sector químico, algunos bienes de consumo y muchos servicios profesionales. La mayoría de las empresas vascas están operando con productos de metal, maquinaria e industria. Las empresas con sede en Valencia están a menudo relacionadas con bienes comerciales y de consumo, y las andaluzas en agroalimentación y similares.

Es interesante notar que hay cada vez más empresas que declaran no tener un origen en España: se trata de empresas nacidas globales, fundada por empresarios españoles que viven en China. En su mayoría son pequeñas empresas, dedicadas a prestar servicios profesionales a empresas occidentales en China, y en su mayoría están activas en el área de Shanghai.

Casi la mitad de las empresas españolas se establecen en el área de Shanghai, debido a su poder económico, pero también gracias al atractivo de su ambiente cosmopolita y el alto porcentaje de extranjeros que residen en esta ciudad. Aunque la contratación y retención de expatriados es difícil en China, en el caso de Shanghai es más fácil. Por su parte, Beijing ofrece muchas oportunidades debido a su condición de capital y sin duda es más relevante para ciertos sectores estratégicos, para los que los contactos con el gobierno son especialmente importantes. En cuanto al sur de China, nos referimos principalmente a las zonas costeras del este alrededor de Guangdong. La proximidad a Hong Kong ha ayudado al desarrollo de medios de producción que fabrican productos de bajo coste para satisfacer la demanda de la UE.

¿Por qué las empresas españolas se establecen en China? Las razones principales son, por orden de importancia: el acceso al mercado, ya sea China u otros mercados asiáticos que usan a China como una plataforma. Junto con esto, tener una base en China es una base para detectar posibles oportunidades de negocio en este país. Para algunas empresas, estar físicamente aquí es un requisito obligatorio para vender, sin el cual no es posible el acceso al mercado. Por el contrario, el acceso a la mano de obra o a las materias primas no se considera razón relevante para la mayoría de las empresas.

Nuestro estudio evalúa cuáles son las principales prioridades de las empresas españolas en China durante los próximos tres años:

- En primer lugar, mejorar la satisfacción de sus clientes, consolidar la marca y abrir nuevos mercados. Todos ellos están relacionados con el aumento de ventas;
- En segundo lugar, mejoras en la producción, como por ejemplo la optimización de costes, la mejora de la calidad y la expansión de la inversión;
- Finalmente, para la mayoría de las empresas encuestadas, la desinversión en China, o abandonar el país, no son en absoluto una prioridad.

En cuanto a la continuidad, la respuesta es casi unánime: las empresas españolas tienen planes de permanecer en el país durante los próximos tres años. El 72% cree que se mantendrá con toda seguridad, mientras que el 26% cree que lo más probable que se queden. Sólo el 3% tiene dudas. Para la mayoría de las empresas, al proceder de un mercado doméstico (España), con una demanda estancada, el estar presente en un mercado en crecimiento, aunque sea complejo, ya es una gran ventaja. Las empresas españolas están en China para quedarse.

La mayoría de las empresas continuará debido a que su nivel de satisfacción es alto. Mientras que sólo el 6% no está en absoluto satisfecho o algo satisfecho, la mayoría percibe la situación como satisfactoria (68%) o incluso muy satisfactoria (26%). Por lo tanto, en términos generales, podemos afirmar que gracias a las oportunidades del mercado, la mayoría de las empresas está satisfecha con su progreso en China y permanecerá en el país durante los próximos años.

Como último asunto, consideremos qué han hecho correctamente las empresas españolas para acceder al mercado chino. Las respuestas fueron muy ricas y variadas. La mayoría de ellos coincide en que la elección del personal (si se trata de los expatriados o el personal local chino) es el factor clave para tener una empresa exitosa. El acento está puesto principalmente en el personal local: elegir las personas adecuadas, formarlas, darles autonomía para desarrollar proyectos, integrar al personal en un enfoque occidental del negocio, y aprovechar al máximo el personal local para actuar en todos los problemas relacionados con el entorno chino, que no es accesible a los extranjeros.

Además de tener recursos humanos locales competentes y capacitados, es muy importante desarrollar un *guanxi* sólido. En muchos casos, el establecimiento de alianzas con socios locales es también una gran ventaja.

La flexibilidad es otro factor muy valorado por las empresas españolas, y se refiere a diversos campos, en particular, ser flexible con la cultura, con el ritmo acelerado de los cambios, con las peculiaridades del mercado. En un mundo inmerso en cambios turbulentos, la capacidad de adaptarse puede ser una fuente de ventaja competitiva. En China, donde los cambios ocurren mucho más rápido, es la única manera de sobrevivir.

Otro valor que parece ser particularmente relevante para China y es frecuentemente mencionado por las empresas, es la paciencia frente a los obstáculos y permitir que el proyecto dure lo bastante para dar tiempo a obtener resultados. En cuanto a la perseverancia, es imprescindible para seguir adelante incluso cuando las circunstancias son adversas.

En cuanto a la estrategia de la central en España, nos encontramos con dos requisitos de mayor relevancia. En primer lugar, planificar cuidadosamente la estrategia de implementación. Esto implica obtener una evaluación a través de estudios de mercado, analizar las alternativas de producción, los socios y la aplicación de los recursos necesarios. En segundo lugar, es muy importante considerar a la filial en China como algo estratégicamente alineado con la sede y con el núcleo del negocio. Creer en el proyecto y apoyarlo firmemente. Esto implica el envío de expatriados con experiencia desde el principio, dotándoles de un soporte múltiple: ejecutivo, comercial y técnico.

Por último, llegamos a la conclusión de que el mundo se está moviendo a un ritmo turbulento y las empresas tratan de adaptarse rápidamente a los cambios. Si en las últimas décadas las firmas occidentales se trasladaban a China para acceder a su mano de obra barata, hoy en día tratan de tener acceso a su mercado en crecimiento. Las oportunidades se están abriendo gracias a una creciente clase media ávida de consumo. El acceso es difícil y lleno de obstáculos. Al mismo tiempo, los beneficios a corto plazo no son fácilmente obtenibles. Pero las oportunidades están ahí para las empresas españolas de todos los sectores y tamaños. Con rigor, y siguiendo las mejores prácticas mencionadas anteriormente, los objetivos pueden ser alcanzados. China está allí para quedarse igual que las empresas españolas se encuentran en China para quedarse.

Tres propuestas para finalizar las conclusiones:

1. La marca país:

Los países compiten a diario con otros países y regiones vecinos por el turismo, la inversión extranjera y las ventas. España es un país con 47 millones de habitantes, mientras que China cuenta con 1,300 millones. La marca España está compitiendo con todos los demás países europeos, pero no es suficientemente conocida en China. Con el fin de impulsar el éxito comercial de España, es fundamental contar con un programa que refuerce la marca de país. Esto requiere la capacidad de actuar y hablar de una manera coordinada y repetitiva sobre los temas que resulten más motivadores para los chinos y que nos diferencien del resto. España ha llegado tarde a China y sigue siendo un país desconocido y lejano, más reconocido por sus deportes que por sus negocios o tecnología. Para cambiar esta percepción y promocionar la marca país, es necesario contar con la cooperación y participación de todos los interesados, incluidos los representantes del gobierno, las empresas, la cultura, la educación y, muy importante, los medios de comunicación.

2. Turismo:

Se ha constatado que existen oportunidades en sectores muy diversos como las energías renovables, el agua, la gestión de proyectos, la tecnología y equipamientos, el comercio electrónico, la gastronomía, el vino o el aceite de oliva, por nombrar algunos. Pero, por encima de todo, existe una gran oportunidad en el sector del turismo: atraer a los visitantes chinos a España. No nos referimos tanto a un turismo del llamado *sol y playa*, sino un turismo de mayor calidad, orientado hacia la cultura, el ocio o las compras. En este sentido, todos los esfuerzos deben unirse para atraer al turista chino que viene a Europa: que considere España como un lugar de visita indispensable dentro de su recorrido europeo.

3. Política de Empresa y Gestión Estratégica:

El comienzo de la década de los años 2000 vio una repentina "moda" de las empresas españolas por ir a China. Muchas pymes acudieron a este país en viajes de "pseudo-negocios", viajes para explorar, conocer, y de paso hacer turismo. Esto dio lugar a auténticos desastres: se firmaban contratos nefastos, las empresas acometían negocios sin ningún futuro. Afortunadamente, la recesión actuó como un agente de limpieza que dejó en claro quién estaba en China como una estrategia de negocio real, en comparación con los que estaban allí por las razones equivocadas. Las empresas deben establecer un negocio en China sólo si (1) se responde a una decisión estratégica, (2) el proyecto se planifica adecuadamente, (3) se otorgan los recursos necesarios y (4) la sede en España está totalmente comprometida. Otro tipo de aventuras no son en absoluto recomendables.

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Annexes

Annex 1. List of interviews

We warmly thank the persons below for sharing their experience and knowledge with us. Their positions may have changed since the time of the interview.

Date	Name	Position at the time of the interview Experience in China
26 th January 2011	Lluís Lluch	Director International Promotion at Barcelona Chamber of Commerce. Years of experience traveling to China with Spanish business persons.
28 th January 2011	Emilio Mulet	Director at China Consultants. Consultant to China for Spanish firms.
2 nd February 2011	Amadeo Jensana	Director of Economic Programmes and Cooperation of Casa Asia. Many years of experience in bilateral Business and Cooperation relations between Spain and China.
Different dates February 2011	Lu Ye Zhan	Chinese entrepreneur living in Barcelona temporarily. Researcher in the business relations Catalonia- China.
3 rd March 2011	Gao Wei	Director CPN of ACC10 Beijing. Years of consulting experience with Catalan firms detecting business opportunities in the Beijing Area.
29 th March 2011	Xavier Espasa	Director Asia at ACC10. Years of experience promoting economic relations and Catalan Businesses in China.
5 th April 2011	Joan Armenter	Ex Director of Emerging Markets at Roca S.A. Expert in several markets, including China. Years working in the multinational accessing other markets.
12 th April 2011	Judith Padrós	Area Manager for Asia at Barcelona Chamber of Commerce. Several years of experience developing economic relations and helping Catalan firms access the Chinese market.
6 th May 2011	Juan Tugores	PhD in Economics at University of Barcelona (UB). Professor of Economics and former Dean of the University of Barcelona. Expert in international economy, globalization, emerging markets and China.
11 th May 2011	Jordi Singla	Economist and Analyst at La Caixa Expert in China's history and economics.
26 th May 2011	Evelyne Hollands	Director at Hong Kong Trade Center. Years of experience promoting the access of foreign firms in China through Hong Kong.
26 th May 2011	Silvia Fernández-	Investment Promotion Executive. Invest Hong Kong

Date	Name	Position at the time of the interview Experience in China
	Marcote	Years of experience promoting the investment of foreign firms in China through Hong Kong.
26 th May 2011	Alfonso Ballesteros	Managing Director. TradeWinds, Hong Kong Years of experience promoting the access of Spanish wine firms in China through Hong Kong.
8 th June 2011	Xi Xi Xia	Chinese researcher from Hangzhou living in Barcelona. Expert in cultural matters regarding China.
15 th July 2011	Sergi Escorihuela	TELSTAR. Director China Telstar. Responsible for the introduction of Telstar in China, including several years working in Shanghai.
20 th July 2011	Ivan Xu	Fagor Shanghai. Representing Fagor in the Area of Shanghai.
20 th July 2011	Dominic Lau	TEKA Shanghai. Director at TEKA at the Chinese Delegation in Shanghai
21 st July 2011	Lizzie Yang	TELEVES Shanghai. Director of TELEVES at the Chinese Delegation in Shanghai
21 st July 2011	Oscar Ramos	DAD Asia Founder and Director of the seed capital firm in Shanghai with several years of experience living in the country.
22 nd July 2011	Willy Trullas Moreno	Owner of El Willy, prize-winning Spanish Restaurant in Shanghai. Ex-employee at Torres in Shanghai. Many years of professional experience in China.
22 nd July 2011	Omar Puertas	Director and Lawyer at Cuatrecasas Law firm, Shanghai. Responsible for the initial establishment of Cuatrecasas in China, with several years living in the country.
22 nd July 2011	Jose Loira	Market Analyst. Commercial Office of Spain, Spanish Embassy. Shanghai. Several years advising Spanish firms in the accession to the Chinese Market.
25 th July 2011	Lijing Ye	Director at West-East Bridge Consulting, Shanghai. Consultant for Spanish firms doing business in China.
25 th July 2011	Jordi Camps	Co-Founder and General Manager at China a la Carta, Shanghai. Entrepreneur in China.
25 th July 2011	Alberto De Sarasqueta	Grupo Mondragon. Mondragon Cooperative Corporation MCC. Kunshan. Representative of the MCC in Shanghai and living in China for several years.
26 th July 2011	Lei Ren	Executive Director at Spanish-Chinese Chamber of Commerce in Shanghai. Years of experience with Spanish firms doing business in China.

Date	Name	Position at the time of the interview Experience in China
12 th Sept. 2011	Elena Liqueete	IESE. Director Global MBA. She travels to China yearly with her students.
21 st September 2011	Ferran Vilaclara	Commercial and Marketing Director at ROCA Former Managing Director Asia Pacific at ROCA. Responsible for the introduction of Roca in China, including several years working in Shanghai.
15 th October 2011	Pablo Fano	Analista Mercado Spanish Commercial Office in Shanghai. Years of experience advising industrial goods Spanish firms in China.
22 nd November 2011	Poli Eceizabarrena Antxon San Vicente	CEO and General Manager of Metalocaucho, Urnieta, Spain. Responsible for the introduction of Metalocaucho in China and India.
22 nd November 2011	Jaime Hernani	International Promotion. Bilbao Chamber of Commerce Several years advising Spanish firms in the accession to foreign markets.
November 2011	Zhixian Ruan	Deputy Director. Ningbo Education Bureau. Regional promotion in Barcelona.
25 th January 2012	Alfredo Pastor	Professor in the Department of Economics and holder of the Banco Sabadell Chair of Emerging Markets at IESE. His areas of specialization include the European Union, Spanish economic policy, the role of the state in a market economy and the Chinese economy.
15 th February 2012	Jacinto Soler	Emergia Partners. Senior Partner. PhD at University of Barcelona. Professor at the School of East Asia of the Pompeu Fabra University in Barcelona (UPF) and for many years advisor on emerging markets to large Spanish companies.
17 th March 2012	Name to be kept confidential	MANGO. Responsible for Expansion to China
20 th June 2012	Mihaly Simai	Research Professor at the Institute for World Economics of the Hungarian Academy of Sciences. Professor at Corvinus University in Budapest. Honorary President of the World Federation of United Nations Associations. He has lived several years in China.
21 st June 2012	Agnes Szunomar.	Research Fellow. Institute of World Economics. Research Center for Economic and Regional Studies of the Hungarian Academy of Sciences.

Annex 2. Interviews summary

About forty interviews were performed to research on the subject of accessing the Chinese market. Questions were opened, to gain insight, and interviews were in general lengthy, like an extended conversation. Persons who were interviewed ranged between business people, academics, consultants, representatives of public and private institutions, etc. Their point of view has been crucial to develop the chapters on accessing the Chinese market. The period when they were done covers over one and a half years, between January 2011 and July 2012.¹⁰⁴

Lluís Lluch

International Promotion Manager
Barcelona Chamber of Commerce
26th January 2011

China no longer wants to be the world factory. The cost of labour is rising rapidly and transportation costs and quality control processes add too much to the final cost of goods. Foreign firms producing in China will only find manufacturing in China attractive if the goods are going to be sold in China. Otherwise, it is not worth it.

The evolution of the situation has been incredibly fast: first, importing from China, after, investing in China; later on, selling to China. Now, finally, the Chinese invest in the rest of the world. This drastic evolution has taken place in a brief period of a few years.

As a result, Lluch foresees a process of re-industrialisation in the EU.

Difficulties for Spanish firms to set up business in China:

- Staff turnover is extremely high. No loyalty to remain in the business for a long period;
- The language;
- A close culture that keeps to itself;
- The political system, the communist government. However, ruling gets easier, not having to deal with democratic issues.

Brief historical development since the II World War. Isolation with Mao, followed by an opening process with Deng Xiao Ping. Access to the WTO in 2001. Liberalisation of trade. Industrial development.

Nowadays, the Chinese government is artificially keeping the Renminbi undervalued to increase their exports. This has an effect on the EU and USA economies. China is exporting now some quality products: Lin Ying, Haier, Lenovo, HTC, and many other brands. While in most of the countries the public expenditure has rocketed, the Chinese Government does not have a welfare state to maintain. In terms of private consumption, Chinese people save more than they consume. Therefore, China has

¹⁰⁴ The complete list of interviews can be found in Annex 1. The position may have changed since the time of the interview.

more resources than any other country in the world: this allows them to invest in strategic sources all over the world. China is a huge economy, with a great potential and wishing to be global: in telecommunications, natural resources, trains. It is expected that China will become the first world power in terms of GDP. In 2030 it will also be leader in strategic sectors worldwide.

Examples:

Huawei: Cisco systems en China, competing in all emerging markets,
Trains: China National Railway Corporation, competes with Bombardier,
Hutchinson at the Port of Barcelona,
China SinoPech, in carburant.

Emilio Mulet

Director at China Consultants.

28th January 2011

I met Mulet when he was on the process of re-orienting the strategy of his consultancy business. He was discouraged by the fact that, in his experience, accessing the Chinese market is difficult and expensive. He found more interesting the project of studying China as the main investing world power: he said that we are moving from western investment (XX century) to Chinese eastern investment (XXI century). China as the engine of the global economy.

He thinks China is operating as the world strategic investor: they buy part of the Port of Barcelona (BCN as an interest strategic point), they buy 40% of the resources of Repsol in Brazil, they plan to build a car manufacturing plant in Barcelona, they are developing the chemical sector in Israel, the Chinese car manufacturer number 25 buys Volvo, etc.

He sees the Chinese investing strategy in two phases:

- first, strategic investment in infrastructures and raw materials;
- nowadays, investment in clusters: they invest in each part of the world, in whatever they are specialists: they buy the leading business of each sector, without losing sight of the strategic vision of the investment.

The Ministry of Commerce CCPIT (China Council for the Promotion of International Trade), part of the Chinese Government, is divided in sectors. It is a macro-organism that employs the best talent of the country. They recommend and send reports stating where to invest. The decisions are taken easily, since the banks are public: they can control and execute quickly. Where are the investments going to? This is uncontrollable and unpredictable.

He is re-orienting his business because, in his opinion, Spanish small and medium-sized companies cannot move into China easily. He has lived through the experience of having business people asking him what to do, and he sees they have not got a chance. There should be a change in strategy: go in huge clusters, pulling all the companies behind. Otherwise we are sure we are going to fail. Therefore, from now, he is going to be an advisor for the Barcelona Trade Fair on all aspects concerning China.

There is a duality in Chinese law: their legal system is not based on the same ethics as our western system. Mulet believes that we cannot forget that they are “capitalist communists”. They have created laws just to satisfy the requirements of the western world (WTO) but in reality, there is always a “but”, objections that do not allow western companies to play in the same conditions as the Chinese businesses. For instance, one firm may think that they could do well in a town somewhere when the municipality comes with a new law just to make the firm’s life impossible.

Therefore his conclusion is that there are huge entry barriers, insurmountable for Spanish firms on their own.

Amadeo Jensana

Director for Business and Cooperation at Casa Asia

2nd February 2011

Jensana thinks that analysing Chinese direct investment in the world is interesting (for instance, large Chinese groups investing in energy and raw materials), but also analysing the access to the Chinese market is a good choice. The main issues concerning the market should be: consumer goods, brands, change of consumption parameters, or the evolution of the retailers' distribution. The sectors that are most interesting are in his opinion: fashion, luxury goods and food. During the last visit of the Chinese Prime Minister to Spain (in the autumn 2010) they bought 6 million litres of wine and 1 million litres of olive oil. However, they purchased at ridiculously low prices.

To get an idea of how the consumption is going to grow in China, we can compare with the US: in the US 70% of the GDP is dedicated to consumption, while the equivalent figure is only 38% in China. So this is probably going to change. Why? Because salaries are increasing by 20% annually: this is programmed by the Chinese Government. For example with Foxconn, it was not real that they were committing suicide in a very significant way. It was just the normal rate. But it was a strategy to force western companies to increase salaries.

"China is for the Chinese", this is Amadeo's verdict. They put a carrot in front of you, to make you think that the market is there for all to grasp, but in reality it is not true.

The government protects the market. At first, they open the market and they let you in, but only through alliances with Chinese firms. Once you are settled and they have acquired the technology, they try to send you out. So it is really hard. They want to be independent technologically from the western world. They do not want to pay royalties.

However, in spite of all the difficulties, there are around 600 Spanish businesses that are regularly selling in China. How do they do it? According to Jensana, there are several characteristics they have in common:

- Very good choice of HR: whether they are Spanish or Chinese. Sometimes they send too junior people and then it doesn't work. Also, it is very important to choose the right Chinese workers. They have no loyalty towards the employer;
- The Companies' Board usually don't know China and they are unsure of what to do. Only if the board is totally involved in the decision and the process to follow will it work. For instance, Cesar Alierta, Pt. of Telefonica, is involved in China, and he attends the Board of directors' Meetings of Unicon in China. But he is a bit of an exception: he studied in the US and he has an open mind. Normally high executives are not so open and they only support the long way to China half-heartedly.

- If you just go to China to “see what you can get”, you get nothing. It doesn’t work like that.
- One needs to allow one and a half to two years to collect any fruits.
- Of course as a pre-requirement for such a vast country, companies need a certain volume of production and investment,

Spain is not very established in China and that is a weakness we have compared to other countries:

- In Germany, 20% of the direct investment goes to China;
- In Spain, only 0.5%.

Jensana mentions some success cases: Mango, Inditex, Torres, Simon, Roca, Alsa, Gamesa, Nutrexpa (although the last ones have very low margins, local competition is too tight, and they have had to adjust prices too much).

Gao Wei

Director CPN ACC10 in Beijing

3rd March 2011

Normally, when Wei gives presentations to Spanish firms, people ask many questions regarding legal subjects and copyrights. Questions like “are my contracts going to be respected?” or “is my investments protected by the Chinese law?” The legal system is advanced, yes, but only on paper. Civil servants do not know how to interpret or apply the WTO laws. He gives me two examples where western companies lost against the Chinese laws:

- Danone had a Chinese partner and in the end lost its case. In cases of JV, the western multinational is the one that always loses. Nobody can guarantee anything.
- Google was in China and in the end had to move to HK.

“Made in China”: it used to be symbol of bad quality, but not anymore. Quality has improved a lot. Of course there are still low quality products but in certain sectors they are very capable of making a good product – at a still a competitive price.

Pieces of advice he would give to Spanish firms accessing the Chinese market:

- Have a certain dose of adventurous spirit. You’ll need it.
- Earn your money as soon as you can (even if some people say it is important to be patient).
- Avoid Joint Ventures, better go for WFOE.
- Look after the contacts and relations with local authorities. Foreigners are always under vigilance. If a civil servant gets angry with your company, you are out. Make friends with civil servants. You need to know that the Town Hall employees work on basis of objectives. You need to know when they have reached objectives. For instance, if you present a project at the end of the year and they have reached their objectives: your project gets rejected. But, if they haven’t reached objectives: they quickly accept your project. It is vital to know where they stand.
- Understand the culture. For instance, in the North of China they say “yes” to all, even when they mean “no”. In the South, perhaps with more foreign influence, if they say yes, they mean it. One has to know how to interpret what they mean.

Obstacles:

- There is a monopoly of estate companies in some sectors;
- Chinese companies do not open doors easily;
- It’s hard to sell because foreign firms face a very strong competition: their low prices and the power of the “made in China”.

Nutrexpa was a pioneer. They were market leaders but not anymore. Now they compete with national brands, so it is not so easy to sell. I ask, “is China just for the Chinese?” “Yes, it’s probably true, although I shouldn’t say so (being Chinese)”.

Xavier Espasa

Director Asia ACC10

29th March 2011

China is still the world factory. Since 1978, thanks to the employment creation and the exports, the middle class has become an upper class and the low class has become a middle class. Therefore, there is a huge population with some purchasing power that has emerged in the last decades. Having said that, there are still 1,000 million of poor people and 35 million of unemployed.

China is the 2nd world power and at the same time place 102 in rent per capita. It is a country of deep contrasts.

Even if prices are going up and labour costs rising, China is going to continue being a power in production. The government has controlled birth rates and the exodus towards the cities. There is also the fact of the currency appreciation. But it is true that, on top of manufacturing, China is moving to becoming a consuming country. Tourism is also growing (China as 2nd world destination).

Consumption is growing heavily thanks to the increase of the internal demand (the growing middle classes). That is the opportunity that we need to get advantage from.

But in which activities? That is the main problem faced by western firms. Many sectors are either closed or protected:

1. Strategic sectors are overprotected by the government. Telecom, car industry, aeronautical, infrastructures and military: western firms can only access China by establishing Joint Ventures with a Chinese partner.
2. Consumer goods: the western firms that could enter China have already done it. The problem is that distribution channels as we know them do not exist in this vast country. The profile of an importer + stocker + distributor is inexistent. Therefore firms need to create the whole distribution channel by themselves. That requires a huge investment, not available for all firms. Distribution is KEY: currently it is only local and informal, very young. There is a long way to go. Espasa advices to be careful with local opportunists who will pretend to help and instead take your money. He thinks that all foreign consumer goods companies that regularly serve this market have done a huge investment in marketing and logistics (for instance Mango or Inditex).
3. Banking: not so strategic, not so protected. But the number is very limited (Santander agreement, BBVA, La Caixa).
4. Business Schools: not any more, only CEIBS if certified.

5. Wine and oil: in theory the potential is there but the consumption is very limited, only as a deference to foreigners. It is not in their culture yet. It represents a nice projection towards the western world.

What to do when facing such unfavourable conditions? He thinks that it would be better to concentrate in only one part of China, not trying to cover all the country. Another possibility would be to try to access the country via Hong Kong or Taiwan, or use professional services to be assessed on the matter.

Espasa thinks that the more one knows about China, the less complex it gets. It is impossible to know enough, it is too large and complex.

He explains that the media have been misleading Spanish firms drawing a very easy picture to access the Chinese market. For years, it was said, "China, yes, or yes", meaning all firms MUST go. On the contrary, he thinks China is only for a few firms.

Joan Armenter

5th April 2011

(Ex) Manager at Roca Sanitarios

Expert in emerging markets, namely Brazil (where he lived for a period), Poland and China.

He is surprised when I say that I have been told there are not suitable distribution channels in China. He believes that is changing, with large distribution firms such as Carrefour. Before, some companies introduced their products via HK, who would enter China with the help of representatives.

His experience with Roca :

Manufacturing in China is only worth it for the bathroom faucets but not for the porcelain sanitary ware. In fact, it has not been the magic cure that was expected. Quality Chinese products are not cheap anymore. So if you produce porcelain sanitary ware in China with Roca quality standards and then you need to transport it back to Europe, it is not necessarily worth it. It means that for two months you have the product immobilised. For some products, you have to produce in China (moved by the pressure of your competitors) but for others, better not.

The demand for construction materials is potentially huge. The ambition of the people is, first, to have a car and second, proper housing. There are plenty of shanty towns outside cities due to people moving to the main cities.

Businesses need to have a double range of products: Roca quality products with Roca name, for the luxury market. And then a second brand name, made in China (with Chinese standards: in fact, the factory was an acquisition). They bought that factory and improved everything, including marketing, but still it was decided it would be better to keep it separate.

Xinle Bathroom Products (Foshan) Co., Ltd. a wholly owned subsidiary of the ROCA Group of Spain, focuses on the production and commercialization of sanitary ware products under the brand of Ying Sanitary Ware. It was founded in 1994. After more than a decade of growth, Ying Sanitary Ware has built a strong reputation with both the industry and end users. Today, Ying Sanitary Ware is one of the leading brands in the China sanitary ware market. In August 2006, the largest Spanish sanitary ware manufacturer, Roca Group acquired the Ying Sanitary Ware business unit, and formed the new Xinle Bathroom Products (Foshan) Co. Ltd, a wholly owned Chinese subsidiary of the Roca Group.

Social classes have a peculiar shape in emerging countries: very wide working class, small middle class and then a wider upper class: wide section for luxury. This is the typical shape of the social classes in countries like India, Brazil or China . That is why it is advised to have different brand names for different categories.

In terms of distribution, in Roca they have their own sales staff: Roca – sales men – shops (retailers) - final consumer.

It is peculiar how it is organised: geographically, they place shops by districts or neighbourhoods. Like it used to be in the old times, it is still done like that. So in one area one can find 25 / 30 construction shops.

New construction supermarkets are coming in: Leroy, Bauhaus, etc. There is a race among the big ones of the distribution to get there the first one. If we were to mention some differences, in Europe we use more prescribers: designers, architects, builders. In China, customers choose more themselves directly without the advice of the prescribers, and they require normally more exclusivity.

Roca took over 15 years of internationalisation before they moved to China. First they grew in Spain, and when their domestic market share was too high, then they moved to other countries. Concerning China, Roca did not rush in: instead they sent a team to China to do research for a whole year before they invested there. A SME cannot do that... That's why he suggests to use public support (ACC10) to help with first contacts, etc.

The Chinese market in general

People live in quite terrible conditions. They live in the factories, they eat there, the salaries are low (but increasing). As conditions improve, the attractiveness of the market is huge. Also it may be attractive as a base to export to other parts of the world. For instance from China to Russia, Southeast Asia (Asian triangle of Growth), Taiwan , South Korea , Indonesia , etc.

The market is very competitive, very demanding. There is no way a company can sell obsolete products, as he has seen done in Africa, for instance). In china there is a high level of requirement. However, perhaps if you produce there, you can use older technology (more labour intensive). Because that is your competitive advantage: the use of cheaper labour.

Chinese copy a lot. This is a fact. They copy and soon you see an identical copied product in the EU. There is very little you can do: you can denounce bad practices, put pressure on the distributors, etc. But there is not much you can do. It is also a shameless copy: the Japanese used to improve while they copied. The Chinese just copy and even try to confuse the consumer by putting labels with "EU" on them. Danone had problems in China (their Chinese partner cheated on them), the same as Nutrexp (the technical team left and set up a factory right in front).

One of the main obstacles when dealing in China is related to staff management:

- Expats do not normally drive in China (a local citizen may fall on you and force an accident to sue you). They need a driver. With family trips, private schools, rent, it gets very expensive for the firm to pay all the expenses. In addition, expats find it hard to adapt and they leave soon.

- Local managers: hard to find people who speak languages, they have no loyalty whatsoever to the firm, hard to keep them, salaries always rising.

Concerning having a local partner, one has to affirm that it makes life easier. You need a local to keep relationships going with the public powers, whether it is the mayor (or the province governor in higher levels). The legal system is very peculiar. When civil servants have a low salary but a lot of power, there is the danger of getting high levels of corruption. On the one hand, they do like foreign investors; on the other one, there is always the feeling that the westerners exploit them.

Chinese people accept happily western habits: luxury, wine. The rules of the game are different for us. Hard to understand for us. If you don't have a local partner, you need a consultant, a builder, an engineer, someone (and that's expensive too).

General view on internationalisation:

Moving to China or any country is not easy. The whole process requires a global change within the business: executives ready to expat, staff must learn languages, consultancy firms must be international.

Therefore, Armenter advises to start by easier countries like the EU, Latin-America, or Eastern Europe. In that sense, China would be later, the last one, as a Masters' degree. It is better to start by doing some trade, import / export, assess the risk, etc.

What about the possibility of some Spanish businesses getting together? For purchasing, it has more or less worked. Now for entering a market, we tend to be reluctant. It is not easy: it is not for everyone. Firms must be very aware of what they can do, how far they can go, what their resources are. But precisely because it is not easy, the prize may be also very big.

He advises to make a plan: a roadmap. Study in detail if there is an opportunity and if it is feasible. Examine the competitors to check if there is a competitive advantage. See if a local factory can be bought, and so on. Step by step very carefully.

Judith Padrós

12th April 2011

Barcelona Chamber of Commerce. Expert in China. International Promotion Department.

Is China for the Chinese? Mainly yes. But it is so huge that there is a place, a niche, an opportunity for everyone. If a Chinese person sees “made in China” versus a western product, he would probably choose the Chinese one. Why? Two reasons mainly: the national pride and the strong campaign launched by the government to promote Chinese products.

Chinese consumers do consider western products more advanced and something appealing, something to look forward to. The Chinese think of Europe as a unit. For instance, they may consider to access the “European Market” as if it was a unity. We do the same towards them: we consider “China” as a whole, although China is huge and there are many Chinas.

There is a so-called Tier 1: Shanghai, Beijing and Guangzhou: high rent per capita, all the foreign firms are already there. Growing salaries, growing prices. But then there is a Tier 2 and a Tier 3: there are growing opportunities in these areas.

The Government still grasps a huge hold on the economy. They sell themselves as an open economy but this is not totally true. The Government organises business trips to Europe and bring along a set of large public companies: they come under the government pressure, more due to a governmental strategy than a business strategy. They do that with Barcelona, for instance: business trip all sitting around a table at the Chamber of Commerce, without a clear idea of what they want to do.

About culture:

Typical culture misunderstanding: they say yes to everything, just to be polite and admit they are listening. But they do not mean yes. She has seen Spanish firms quite happy after a trip to China thinking they have done excellent businesses but in reality there is nothing behind.

China is the centre of the world. Their maps place China in the middle between Europe and America. One has to over compliment them, show them a lot of respect. Additionally, when selling our products, we can never compete in numbers: they are always bigger, more, larger. We need to compete in quality, image, brand, and differentiation.

For production, there are already cheaper countries: Vietnam, Cambodia or Indonesia. In China there is already a wide range of possibilities: from the cheapest to a bit more quality, to the highest range. All is possible.

Two main obstacles for Spanish firms:

- According to Padròs, the main obstacle is the dimension of the Spanish firm. The financial resources. It is absolutely necessary to have a budget and a strategy. Some people think that with two or three trips the question is solved. But this is not the case. You need time and resources: minimum one person in one office to do the follow up. So at least 5,000 euros a month for a couple of years. One needs to realise that the Germans are there, the Americans are there: it is an extremely competitive market. You need to travel to China every three months. It is all about making and keeping contacts.
- The other obstacle is the Spanish frame of mind. China requires time and money. Firms can lose all their capital. Small businesses need to be patient, spend time and money. Many lost money and left. Now they are trying again... An idea would be to get together some firms to share expenses. But it is not in our mentality: problems, frictions, who sells more, etc.

Success factors:

- Get there at the right time. We cannot get there early now (it is too late for that) but at least don't get there too late;
- Stable physical presence: with one person, preferably Chinese;
- Adapt your product (service). Chupa Chups had to adapt the taste, the brand, everything. Currently you don't need to change it all: it is good to keep a European look that may make your product more attractive;
- Choose the right distribution channel. See if your partner is well positioned. Establish your sales people. If you are small, you can find a local distributor (there are good ones). If you are well established in a couple of geographical areas it is fine. If you are large, then yes, you need to set up your own distribution;
- Find your niche in the market: China is very big, you don't need to be everywhere;
- Everything changes rapidly: distributors change their activity / contact / address / etc. You need to keep up with the changes;
- This is an extremely competitive market: the best products and also the best services are already there;
- They copy everything. That is true. On the other hand, if they copy you, that means your product is interesting. They are trying to change, in order to improve the image and reputation of China. You need to be faster than them. When a Spanish firm gets there, the first thing that needs to be done is to register the brand and product. It is very cheap

and will avoid problems later on. If you are very small, they will not bother to copy you.

The Spanish media are being kind of misleading: they see the big numbers, but they do not see the business reality. They see the large companies: Telefonica, Gamesa, Banks, Inditex, Mango. High range positioning, like luxury goods. That does not mean China is for everyone.

In terms of sectors, Padròs sees some opportunities:

- The Chinese do not know how to access the European market: how to sell, design the packaging, do the marketing, advertising agencies, etc. They need designers for this. Large Chinese companies do know, but small ones don't;
- Food, gourmet, wine, olive oil. At the moment these goods (for instance olive oil) are considered as presents, as a luxury: the best would be to enter through the *horeca* channel: hotels, restaurants. It would allow the firm to have smaller stocks and less marketing expenditure;
- New technologies services: mobile phones, internet. E-commerce web sites;
- Renewable energies, consulting, engineering. The problem is most of our companies are too small. They go to closer markets;
- Some industrial products too.

Juan Tugores

6th May 2011

PhD in Economics at University of Barcelona (UB). Professor of Economics and former Dean of the University of Barcelona. Expert in emerging markets and China.

Prof. Tugores introduces us to some important sources that prove very useful for the research:

In the first place, the Economic newsletter (Boletín Económico 2010) of the Bank of Spain, Exports of Services. The role of the Spanish firms in the exports of services (business services, large engineering firms, builders). The kind of analysis by Hoekman, world trading system, from GATT to WTO.

In the second place, the analysis of the emerging middle classes in China carried out by Homi Kharas. This researcher is a senior fellow and deputy director for the Global Economy and Development program. Formerly a chief economist in the East Asia and Pacific Region of the World Bank. Kharas currently studies policies and trends influencing developing countries, including aid to poor countries and the emergence of a middle class.

In the third place, the Efige studies: Efige.org. European Firms Global Economy Publications. Efige 1: Mayer and Ottaviano. "The happy Few". Efige 2: extensión of 1. At first the idea was that going into foreign markets was done by a limited number of large firms (so called intensive way). Afterwards, the approach is that many small businesses get international, not just the large ones (or extensive way).

Small firms are often afraid to go into large markets such as China. But growth is coming from the implication of many more firms, that is, large numbers of small firms. Imports from China have grown at amazing rates. Perhaps China is for the Chinese (the core part of the market, the control of the domestic market), but it is possible to get a piece of the cake, especially in services.

It is difficult for small firms to go to China on their own. However, there are other ways, other more creative formulae, like for instance vertical integration, where we are not sufficiently represented. Spain needs to be more active in this field. (Production Global Networks research on this concept).

Germany for instance is better connected with the demand of the Chinese market thanks to the so-called *Hidden Champions* (a concept by H. Simon): small and medium-sized businesses that are more resilient and more competitive than the rest.

The Chinese are the second economic power in the world, and soon they will be the first one. This is normal, because they feel they need to regain the control over their destiny, not as an emerging power, but as a normal situation (Maddison table of historic evolution of different regions' GDP as % of world total, from 1700 to 2015).

However, China suffers from some internal weaknesses that can affect their future. These issues are the following:

- Unequal income distribution
- Demography (only child policy)
- Pollution
- Political dilemma: will the wealthy be happy having the economic power, but not the political one, or will they try to get the political rights too and fight for a democracy?

A certain level of economic development should take to a higher democratic level, but that is not common in history. To grow under a dictatorship is quite normal. Productivity is growing thanks to rural population moving towards the cities. Activities with increasing value are producing a rise in the economic growth.

Jordi Singla

Economist Analyst of La Caixa. Specialist in China

11th May 2011

Great specialist in Chinese economy and history, Singla did a tour of the latest historical movements in the country.

This is the first time in history when the greatest power (USA) goes into a recession and other countries do not necessarily follow suit. Normally, it has been stated that when the US sneezes, the rest of the countries get a pneumonia. This time, however, emerging countries have coped well and have resisted. The growth in China is such that they are presently buying 30% of the steel, aluminum, ores and copper in the world. Should these raw materials get more expensive, China would have a serious problem.

In the 60s and 70s, Japan was able to move from a heavy industry to consumer goods. China, in the 21st century, still has not been able to do such jump. In fact, the services sector is still highly underdeveloped. However, they are moving fast from a bicycle economy to computers and internet, with no intermediary phases.

According to Singla, China presents four main advantages:

First, increasingly there is a stronger component of high technology in China's exports to the world. They are perfectly aware that being "cheap" is not going to be enough, so they are developing technology rapidly;

Secondly, China believes in itself. Moreover, China means "the kingdom of the centre", and that is how it is perceived by the Chinese. In their cultural vision of the world, their country is the greatest, "the country under the sky", and it is full of promises. They are very patriotic indeed. The diaspora is going to be key in their development: Chinese people who left the country are now getting wealthier and trained all over the world. Those emigrants (contrarily to what happened to the Japanese, Spaniards or Jewish) will return to China and will help in the progress of the country.

Thirdly, the pragmatism of Chinese politicians. The objective of the Chinese governors has been to provide a sound and widely spread economic development for the whole population (that is where Mao failed, not being able to solve the misery and the hunger, and with a cultural revolution that was highly negative). From Den Xiao Ping onwards, the accent has been placed on the economy, in making sure the basic needs of the population are covered. While the political changes will probably come later with a slower pace, there is no feeling of hurry for that.

Fourthly, Chinese business people, unlike the Japanese, are small business-oriented. They are traders, small company people. That means that they will be able to develop a wide network of flexible and middle class firms that will allow opportunities for all the population.

Obviously, there are certain risks. But according to Singla, there is no and there will not be a real estate bubble. The growth is a natural growth, due to the general increase of salaries. No artificial growth is detected that may seriously threaten the economy. The risks are more related to a social unrest due to an aggressive capitalist that does not provide with health cover to the citizens. Another worry is the weak protection of property, where expropriations can take place with practically no public compensation. The Chinese people, with no social protection and no clear property guaranties, are naturally inclined to save as much as possible.

According to Singla, there is no risk of a revolution. The middle class is not going to claim political rights simply because that is not how they think (we are judging from our point of view, which is different to theirs). Now, a different matter will be the diaspora coming back: they may well have a more westerner point of view. Perhaps it will be them who will question the lack of democratic rights. Only time will tell.

Silvia Fernandez-Marcote

26th May 2011

Investment Promotion Executive, Invest Hong Kong

Hong Kong is the second world receptor of investment in the world. The reasons to give Hong Kong such advantage are: strategic location, free economy, convertible currency, British common law, equal opportunities, international finance centre and simple fiscal system. There is more legal security than in China, which makes that many investors prefer to enter China via HK. The key is "trust", westerners feel they can trust HK.

Fernandez Marcote detects six business opportunities in HK and in China:

- The sector concerning testing, certification, accreditation. Quality management in general.
- Medical services: cardiology, traumatology, and biomedical.
- Technology and innovation in several clusters: biotechnology, electronics, IT and Telecom, precision technology, green technologies.
- Creative and cultural industries: architecture, design, games, mobile applications, video games, digital entertainment. Public institution "Create Hong Kong"
- Environmental industries: promotion of renewable energies.
- Education, universities, alliances. Professional training.

Hong Kong acts as a window-shop for China. It is an effective way to enter the China, with more guaranties, more similar to us, safer and simpler.

The flow of tourists from China to Hong-Kong is growing with over 21 million in 2010. The luxury goods sector is increasing rapidly. The Mainland and Hong Kong Closer Economic Partnership Arrangement, or Closer Economic Partnership Arrangement (CEPA), is an economic agreement between the Government of the Hong Kong Special Administrative Region and the Central People's Government of the People's Republic of China, signed on 29 June 2003. This agreement is helping matters for foreign companies that want to invest in China through HK.

Hong Kong's appeal is threefold: it is a dynamic city with strong growth prospects; it is a gateway to opportunities in Mainland China; and it is a regional base for expansion across Asia. Moreover, it is stable, business-friendly and cosmopolitan.

Alfonso Ballesteros

24th May 2011

Managing Director

Tradewinds

Ballesteros believes that firms should get ready to access the Chinese market strategically, putting the emphasis in the planning: geographical areas, marketing mix, positioning, brand development, distribution, etc. He believes that, for many firms, Hong Kong may be an easier option as an entry gate than China:

1. China and Hong Kong are two very different but complementary economies. Hong Kong is a small territory with 7.8 million inhabitants and an ex-British colony. The economy is liberalized, the GDP per capita is very high (US\$ 31,600) and the market is totally developed and mature. Summarizing, Hong Kong creates brands. China, on the other hand, is the 4th world country in extension, with over 1.3 billion inhabitants, politically communist in transition with a planned economy, a growing middle class, and an emerging market with huge desire for European products. China consumes brands.
2. Hong Kong is a business city that maintains and consolidates its condition as a gate for China. Selling to HK means sales for the whole region, especially China.
3. Peculiarities of China: in this growing momentum, it would be better to try to create a brand now. The later the more difficult it will become. But each geographical region is totally different to the others. The coast cities are very different to the rural interior. Distribution is still inefficient and in development. Secondary cities are expanding, and could be the access point now. Do not attempt to cover the whole of China, and try to focus instead in one of the three large areas.
4. Opportunities can be found in consumption products of high range with competitive prices, coming from Europe and with a European look and brand. The Spanish company must be prepared to help the distributor and invest in the promotion and advertisement. Sectors that are at the top of the opportunity range, especially when they can combine quality, design and safety, are: food (and food safety and health), wine, fashion including shoe wear, cosmetics (and safety in chemical products) and home furnishings (cosmopolitan decoration).

The wine market in Hong Kong and China:

Hong Kong: Sales over US\$895 million and growing (increases by 80% in 2008, 41% in 2009 and 73% in 2010). Mostly red wine but also white wine on the rise. The main countries of origin are France, Australia, Italy, Spain, Chile and USA. Estimates foresee an annual growth of 25% until 2014.

China: Sales over US\$276 million and growing (market has multiplied by 20 since 2003). Red wine totally predominant. The main countries of origin are France, Australia, Italy, USA. Lower prices per bottle than in HK.

First move could be to identify a trade fair and go there. Stay several days more either after or before the fair. Avoid just doing punctual sales, but develop a consistent strategy thinking long term. Planning is crucial: events, which ones, which partners, etc. Consider internet as a valid tool for distribution.

Spain has a visibility problem in terms of wine in China. It is not well-known by the Chinese consumers, who cannot tell the difference between D.O. and brands. On the Spanish side, there is a lack of planning and the spending in promotion is not efficient. There should be more analysis, and a serious positioning: the brand perfectly aligned with the quality and the price, so the consumer can identify the wine and remain loyal to it.

It would be crucial to realize that one is not just selling to the importer, but to the importer, the restaurants and the final consumers.

There are also Purchasing Centers in HK that act as prescriptors and then sell to China. Remember that the extension of China is too wide to be covered by any one firm. Try to establish in one region: it is very possible that one wine-producer cannot harvest for more than that.

As a conclusion: emphasis in the planning: of the resources, the geographical areas, the marketing mix, the positioning, brand development, distribution, etc. The objective is to sell in a systematic way, not just one off.

Sergi Escorihuela

Telstar Group - Operations Unit Manager

15th July 2011

Escorihuela has spent several years in China opening and consolidating Telstar's operations in this country. He affirms that the experience has been extremely enriching, both personal and professionally.

A brief introduction to the company: Telstar is the only firm in the world that can supply fully-equipped laboratories and Pharmaceutical Industries for drug production and research, including process critical equipment with in-house technologies. Telstar is one of the top 10 pharmaceutical process equipment manufacturers worldwide, and it is number one supplier of pharmaceutical process Equipment in Spain. The sector is growing, namely in emerging countries:

- Consumption of pharmaceuticals continues to rise with an increasing share for biopharmaceuticals including vaccines.
- Substantial growth in countries like China, India etc. mainly for existing drugs mainly low cost, i.e. market expansion.
- Big Pharma has started to move production to low cost countries, mainly India, China, South America or Middle East, all currently mainly market driven.

According to Escorihuela, In the year 2000, when a foreign firm established in China, the most common way was to launch a Joint Venture (JV) with a Chinese firm. Later on, as the sectors were liberalized, there was a trend to establish Whole Foreign Owned Enterprises (WFOEs). Lately, the trend is returning to the JV format, in order to gain assessment on market knowledge and also to transfer some of the responsibility to the Chinese firm.

Following Escorihuela, there are some factors that have to be taken into consideration to be successful in China:

- First, patience. Firms have to be able to spend a long period without expecting fast returns;
- Second, related to the first one, firm corporate support. The headquarters must be committed and believe in the project, or it will not succeed. The expansion strategy must be very well defined and transferred;
- Third, it is very important to count with enough financial resources. To get credit in China is very difficult, therefore the funding must come from the headquarters;
- Fourth, the organization in China must be very flat. The definition of the tasks has to be very detailed, in order that each worker knows exactly what is expected from them. Communism mentality is still predominant, so

creativity, proactivity, or imagination are not values very widely spread among Chinese workers;

- Fifth, in the West, the quality is defined jointly between the manufacturer and the supplier. In China, the manufacturer must define the quality level: there is a higher need to define and explain very well the quality requirements;
- Finally be aware of the cultural differences. Especially keep in mind the concept of “face”, and never, for instance, tell a worker off in front of other people or damage someone’s reputation.

China is creating a new model of a country. Strategically, they try to keep only what creates value: innovation, technology. Strategic decisions are taken in all areas, like the building of a fast train that joins Beijing-Shanghai and the South of China.

Chinese attach strong importance to their ancestral land, their origins, the place they come from. They try to go back to where they were born before they die. In nature, they believe in a process where the leaves when they fall nurture the roots. The trees are fed by the leaves. When a company is born, they plant a tree outside as a symbol of the estate of the business and is supposed to give good luck.

To conclude, to establish a successful business in China, it is essential to know the cultural peculiarities of the country.

Dominic Lau

20th July 2011

Director at TEKA Chinese Delegation in Shanghai

Kitchens are very different in China compared to Europe. In China households use the cookers a lot more frequently and they use a lot more oil. In Europe the oil filter is enough to cook normally. In China, such filter would have to be cleaned every five days, that's why they use oil collectors. The materials used for the production must be different by legal requirements, because they need to resist higher temperatures in China. Ovens are not used in China, but they use instead sterilisers and also they cook by steaming.

Mr. Lau thinks that to be successful in China, one must offer a combination of EU brand and prestige, but adapted to the Chinese tastes and needs.

The tastes of middle classes have evolved a lot in the last ten years. First, their main concern about the house was the sitting room, which they showed to the visitors. After, in a second phase, they liked to show off their bathrooms. Nowadays, there is a third phase where they like showing their kitchens. There are many people (the new rich and the second rich generations) buying cars, luxury goods and expensive kitchens.

The most famous brands are German and they are also the priciest ones. Teka is positioned in a mid-high range. Teka is supposed to be the best luxury kitchen, but two or three times less expensive.

According to Lau, one needs to ask, what makes us special?

The Certification process is a nightmare. It takes a long time and money to complete it. The government finds all possible ways to stop the foreign company.

The sales are still growing with the real estate development. The Government is trying to slow down this rapid growth to avoid a real state bubble and they are trying to make housing prices go down. He estimates that in Shanghai prices have multiplied by ten in the last ten years.

Teka is going through a dilemma: on the one hand, they have a product that needs to be adapted to Chinese tastes and uses. They estimate that once they do it they can have large sales. However, on the other hand, the headquarter is reluctant to do such an investment before making sure they can realise the sales. In the meantime, they are losing a lot of money. He asks himself, what comes first, the chicken or the egg? Lau thinks that without adapting the kitchens, their sales in China will be small. He says "In China everything is possible. But nothing is easy".

Chinese people have their own habits their own demand. One has to be a combination of Chinese and western to be successful.

He does not think there'll be a demand for democracy or social unrest. As long as people have a home and food, they will not ask for more rights.

There seems to be a certain clash between headquarters in Spain who come to visit twice a year and expect big results, and the Chinese delegation, who demand investment to produce a product that is adapted to Chinese tastes.

Lizzie Yang

21st July 2011

Director at Televes Chinese Delegation in Shanghai

Televes is a leading global company focused in the design, development and manufacture of equipment for distributing telecommunication services throughout the infrastructures of buildings and homes.

The company is headquartered in Santiago de Compostela (Spain), where it keeps its state-of-the-art manufacturing facilities. It has a commercial presence in more than 90 countries, and it manufactures and sells in China too.

Yang explains that Televes does sourcing, purchasing, quality control and shipment inspection of parts in China that are afterwards sent to Spain. The sector is considered strategic for the government and so they have to give the permits for all the projects. The Government has a list of providers, and they are all Chinese. It is therefore, very difficult to access this market. Yang went to the government in Beijing several times to try to get on the list of suppliers, but it did not help. Televes manufactures in China and sells to the EU and Dubai.

She believes that the reasons for not being able to sell in China are a combination of two: on the one hand, the lack of support of the government, and on the other hand, the prices, that are very competitive.

In theory private people are not allowed to set up their own satellites in their homes. It is forbidden by law. But people do it anyway.

As a conclusion, it can be stated that when a sector is considered strategic by the government, like this one is (telecommunications and satellites) it is very difficult to enter the market due to the protection given to the national brands.

Oscar Ramos

21st July 2011

Co-founder and CEO DAD Asia

Oscar and his wife left Madrid three and a half years ago with a business in mind (a quality control consulting company that in the end never saw the light) and instead established a seed capital company in Shanghai. DAD Asia is an investment mechanism to simplify the investment in Chinese internet startups: diversifying the risk and having a team to take care of the deal sourcing, projects analysis, due diligence, and monitoring.

DAD replicated its model outside of Europe... “We have a “Glocal” strategy—with a global vision and execution that’s as local as possible”. The first thing they did when they arrived was to learn some Chinese (or rather, *Chinglish*, a mix of Chinese and English that is the new modern business language). At that moment there was some capital risk in China but no seed capital at all. Those entrepreneurs who had some money from their families could start the business; those who had none, simply couldn’t.

In China the culture gives much importance to safety, belonging to the party, a work for life: the people who are worth most look for a job in the Communist Party and that is the essentially the wide definition of success for Chinese young and old people. There is fear to failure. People are afraid to talk for fear of saying something that is not convenient. Therefore the idea of being an entrepreneur is not something that appeals to everyone.

DAD Asia sponsors events to meet with new entrepreneurs. They evaluate projects and choose some to invest in. First they check the competitive advantage of the project. Then the interest the market may have in it. They always ask two questions:

- First, does it solve any problem?
- Second, do I know people who would pay for it?

If you do not answer affirmatively to both questions, it is not worth continuing.

DAD invests normally 50 to 200 thousand euros, and on average they invest 100,000€ per project. They help with the management but without interfering.

Sometimes the Chinese find it hard to believe that they are not Americans. Ramos thinks that being in China has allowed them develop a business differently to what they would have done in Madrid. They work 14h a day, everyday of the week. They have no pressure from their families. They feel more freedom and fresh to do whatever they want. They have been born global, and that makes the whole thing different.

E-commerce has a spectacular future. And now a new idea: e-commerce combined with social networks.

Willy Trullas

22nd July 2011

Chef, founder and owner of "El Willy"

Spanish restaurant in Shanghai

Contemporary Spanish food restaurant specialized in modern tapas and rices. They used to be in the French Concession and now (since fall 2011) it is located in a historical 1906 building in the Bund. Ranked #16 of 6,502 restaurants in Shanghai according to Tripadvisor.

The place is beautiful, the decoration special, different, sophisticated. Willy himself is a peculiar man wearing peculiar hats. A natural public relations. The menu is original, creative and extremely imaginative. Everything is special and the mix is brilliant.

According to Willy, to be successful in China, one must adapt to their habits. For instance, many high class Chinese people come to the restaurant. "I could offer sticks or just European cutlery: I offer both. Many snob restaurants would only offer forks and knives, but many Chinese people cannot deal with them comfortably. You don't want successful business people struggling with their cutlery in front of their customers. So I adapt: sticks and food cut in small pieces."

Willy came to China some years ago and started working for Torres, the wine producer. That gave him the knowledge of the country, the contacts, and he got used to the business culture. He also learned at Torres (now second wine distributors in this country) that in China everything is about public relations and contacts: being a good chief is not enough, is not even the most important fact. One needs to go out a lot, talk to people, drink with them, sing karaoke with them. That's the way to establish business in China. A very intelligent person in China, locked in her or his office would get nowhere in China.

His restaurant is crowded, mostly with westerners, Japanese people and wealthy Chinese. The Japanese act as a magnet for the Chinese. Willy speaks some Chinese and talks a lot to his employees. He says that establishing a friendly relation with them, creating a good atmosphere, is crucial to retain the staff. Often, even more important than the salaries.

Competing in price would be impossible for him: many products have to be imported, there are tariffs and many high costs. Therefore it is better to focus on differentiation and offer something really special. He concludes: "this is the most competitive market in the world. Everybody is here. You need to have very clear ideas".

Willy emphasizes two factors over and over again: first, adapt to Chinese tastes and second, the importance of relations and contacts.

Sr. Omar Puertas

Cuatrecasas Shanghai

22nd July 2011

Omar's speech is very simple but effective.

His first idea is that we judge the Chinese following our own principles and points of view. Expats come to China, they do not like it, it's dirty. One needs to reset totally and try to start learning from scratch.

The sensibility of the Chinese is different ours. For certain things they are hyper-sensitive according to us: who picks up whom from the airport, who you talk to, never to be late, presents, cards, "face", etc. However, for other things, we find them insensitive, mainly for "manners".

He thinks Spanish businesses that want to be successful need to visit China every two months and learn some Chinese (he is himself learning and has flash cards to remember the characters).

Bad practices: to save some money, too many companies don't do things properly: do not use professional advice, do not register the IP. Too often, firms sign contracts not knowing what they are signing, so as to save in resources, so as not to pay a lawyer...

It is not too late to come to China. But it has to be done properly. Business men think of him as a civil servant: "what is he going to teach me about doing business". And then fail.

Successful firms as Fagor: they take huge decisions and carry them out. They think big and go on with it. They have an advantage: they come with contracts already signed for Europe. Flamagas is another successful firm (look for it).

Spanish infrastructure large firms are not in China because they find it hard, due to lack of legal security. There is not a central system for public tenders, it has to be done by municipality, one by one. They protect themselves: they give you 15 days to bid: that means there is not enough time to do it.

Businesses should take a strategic decision about China: to be there (and then how), or not. But not ignore it.

Sr. Jose Loira,
Market Analyst
Commercial Office Spanish Embassy in Shanghai.
22nd July 2011

Spanish companies (Alsa, Agroaliment, Nutrexpa etc) started to come to China in the 80s. There was no a stable legal system then. Judges were not law professionals but military men. After 2000 it's when it became generalized, namely in the period 2005-2006. The disembarkment was not only of Spanish companies but French, Dutch, Japanese, Taiwanese, Korean, HK, etc.

Only six years ago, if a foreign firm opened a business in Shanghai the major would come. Now they ask you, what do you want to do. If they like it, they let you do it. If you come to China to buy or to invest, you get red carpet treatment. If you come to sell, they bite you. For 20 years the economy was based on production through cheap labour and then exports. 60% of the Chinese exports did not come from Chinese businesses but foreign ones. In practice, companies that threaten them get mostly non- barriers: scaorbic acid problems, wine labels regulations, substances for Inditex. They are only interested in buying raw materials.

Loira thinks that the Chinese way of thinking of "circular" thinking: for instance, a Chinese person may start a business that may not be profitable in the short term. But they think: through this business I create a network (guanxi), I learn a technology, and it may generate ideas for a new business.

For the Chinese, quality is different than for us. For them 75% right is total quality. For instance, if they paint a room, why paint behind the furniture? It's not necessary. You ask a Chinese, 1 unit, 1 euro. OK. 1 euro 100 units, they say OK too! They have all the quality levels that you want, they will always say yes. All the businesses produce in China, with the only exception of Hermes.

Our culture is mostly based on Greek logic and on Jewish-Christian ethics. They share none of it and have their own Confucius system. Education based on repetition. "If a nail sticks out, we hammer it down". We don't understand each other. What we have been doing for centuries, they have needed to learn in 10 years.

Chinese believe in constant change. Negotiation is "water", it changes continuously and it never ends. The negotiation process is extremely long. Once you sign, it starts changing again. Negotiation never ends, therefore one has two options: either to adapt, or to give up.

China has never been aggressive in a military dominant way, but always commercially. There are many millionaires now, many 25-30 years old. They want to show it off.

Minimum rules according to Loira, when trying to establish in China:

1. Get sound market information in the specific sector

2. Register intellectual property. It only costs US\$300 , This is the firsts and most important thing to do as you come in China.
3. Do not bring into China the most strategic and crucial productive part of your production
4. Continuity: Spanish managers should travel to China at least every 1 or 2 months. They suffer what he calls the “Barajas effect”: once back in Spain, they get all these calls and emails, and they do not return for months.
5. Human Resources. You need to mix your own resources with Chinese labour. But when you recruit the best, prices are very high, and get cannibalised among western companies. Expats are extremely expensive. Loira stresses that expats do not need to be Spanish (they are scarce, they recruit inexperienced stagiaires), they can be English speaking.

Minimum requirements for Spanish firms: you either count with the four of them or do not even try (except if it is a certain type of service, very special food, technology, software, architecture service, etc):

1. A certain level of financial volume
2. A certain level of productive capacity
3. Quality Human resource
4. A certain exporting experience. If the business has no experience in international contracts, logistics, you can make a very expensive mistake

Common Mistakes:

Loira has seen hundreds of Spanish businesses trying to settle in China through very poor associations: mostly with Chinese translator (who is good at languages but not in business) and Chinese Restaurants in Spain. They come for a week with the foolish hope to bring back a signed agreement. That means they are ready to accept enormous risks without checking: what they would not do in Spain ever they are ready to do here. Why?

Try not to have a Chinese partner. If you do, he will have the power to grow (ampliación de capital) or to dissolve the business

When the business is established in an industrial estate, it is so boring and tedious for us westerners. Very hard to keep the best people.

China is not a market. It is a “market of markets”. Differences between the north and the south are huge. They do not even like each other. Also China can be seen as a “hub” towards Asia. This is also a very interesting possibility to take into account.

One cannot come to China to just “sell”. One comes to “invest”: in promotion, in distribution channels, advertising, etc.

Lijing Ye

25th July 2011

Partner at West-East Bridge Consulting

Lijing Ye is a consultant who has helped many Spanish firms set up business in China. She has seen Spanish business people make the same mistakes: first, they misunderstand the size of China. Shanghai has 20 million people registered, but 30 million really living. Only one city has half of the population of Spain. Spanish firms aim to tackle the whole country and that is practically impossible. Even large companies like Alsa or Nutrexa are more present in the north than in the whole country. Another common mistake is not to contract professional services to help them settle down in the country: they prefer to see by themselves (and fail by themselves). They are reluctant to pay for the services ("I'll pay you only if I get results"). They tend to lack perseverance: they spend some time and money trying to enter the market, and then give up. Often they trust their businesses to any Chinese person they meet in Spain, sometimes even the manager of their local Chinese restaurant, who knows very little about business anyway. Finally, Spain is represented by many independent regional offices that do not work co-ordinately. They lose many resources on the way and make huge amounts of effort that are inefficient. Results are not achieved as a result.

For a firm to try to establish its own distribution channel is an enormous investment. The answer would be to choose a small part of the country and focus in it. For that, it would be advisable to do some previous market research. This is what most small and medium-sized businesses are not ready to do.

She does not think that the Chinese are protectionist or they create problems with bureaucracy. She thinks those are excuses of firms who have not been successful, because they did not do a good preparatory work.

Another reason for the lack of visibility of Spanish firms is that Spain has not got many products that could be of interest for China: the economies are not complementary. China's trade matches better other with economies such as the USA or Germany.

She believes that China is going through a deep process of changes. Business people have closed down their businesses to invest in real estate. They want big money and they want it fast. Before, the government told citizens what to do, where to live, where to work. Now it is no longer like that. Citizens are waiting for the next government to solve their problems, because they are not used to fighting for their rights. Everything is changing now, in terms of the political, social, economic situation. Also the families are evolving. With all this turmoil, the older people are left behind; they cannot catch up with so many changes.

One does not see these problems in Shanghai so much, because this is a city full of opportunities. But if one goes to other parts that are not so developed, then the contradictions and the problems are a lot more obvious.

Jordi Camps

25th July 2011

Founder of China a la Carta

In his years in China, he has seen many Spanish firms fail, and he finds that the reasons are quite simple. He can think of executives sitting in their offices in Spain, comfortably, sending *expats* to China: go and sell there. As if you could do business like that in China. He believes that often Spanish men feel they are colonisers: "let's teach the Chinese how to do business". Some other times, the Spaniards have been cheated by the Chinese partner. "It serves them right for doing business with the first person they meet", Camps thinks.

The Chinese have it very clear: they look at business from the angle of "volume": quantities and margin. Very simple but effective. The concept of differentiation is a lot more difficult to grasp for them, it's not in their culture.

Camps's business, *China a la Carta*, is a tourist agency that takes Spanish wealthy customers who want to see a real China, very different to what the tour operators sell. His key is precisely that: the differentiation. He does not want to compete in prices, for that, go to the Chinese agencies.

He finds that in China the Maslow pyramid of needs is inverted: A person who earns 2000 RMB/month can spend half in rent and also save all the rest for six months to buy an Ipad. They do not have the basics, but they still want the "aspirational products", like the Louis Vuitton handbag. And they will never buy fakes.

The Chinese, according to Camps, are very Latin: noisy, messy, they are all together, all linked, a bit kind of gipsy-like.

Camps does not think Chinese people want more freedom. They are not annoyed for being under control. Anyway, he reasons: "in the west we are more controlled by Facebook".

The Chinese do not have great ambitions. They want to be able to buy a flat, a car and have a child before they are thirty. Other than that, they do not want anything. It is not a model of society with great aspirations.

He thinks many jobs are totally useless and people are employed to do nothing. Receptionists, secretaries, accountants, etc paid to do nothing, to spend the whole day daydreaming. But they are quite happy like that and it would not occur to them to try to find other jobs to do. It's not on their mindset, quite simply.

Alberto de Sarasqueta

Executive at Grupo Mondragon. Mondragon Cooperative Corporation MCC. Kunshan
25th July 2011

Mondragon Corporation has been in China since 1990. They have several business models in the country and in Kunshan in particular:

- In the first place, they manage the purchases for the group, obtaining savings up to 25-30%
- Consulting firm for projects: they provide services for any firm that wants to establish in China
- Industrial park. They have the best location, they give services for expats, they retain talent better than other multinationals. Being only 50km from Shanghai helps keeping the Europeans who are fine living in Shanghai but would rather not live in the interior of China.

In China size matters: it gives you a better position to negotiate in front of the local government. They get a better treatment. Better prices for the land.

Mondragon Corporation did the landing in China in three phases: first the founders, with Orkli, Orbea, Oiaso, etc. Then Fagor Arrasate, Fagor Industrial and Batz. And then a third phase with more cooperatives (Fagor Ederlan, Ormazabal, etc) and other businesses that are not cooperatives: Agi, Camaño.

This complex is, according to Sarasqueta, the largest industrial park of only one group in the world. It also represents the largest Spanish investment in China.

According to him, if labour cost is more or less 17€/hour in Spain, in China it is 1 or 1.5€/hour. However, it is also true that salaries are increasing by 10-15% yearly.

Following his experience, investment is normally amortised around year 3 or 4. Foreign companies in China can clearly not compete in prices, so they need to add value added and brand value. For instance, Orbea produces bicycles, each one costs 650€ for the Chinese market, which is not cheap. But they offer quality and brand. It is crucial to build a name and educate the Chinese consumer.

Good Chinese workers are “cannibalised” by western firms who “steal” them from each other causing salaries to rise. This is not allowed in the Mondragon Corporation. The Chinese workers have a civil servant mentality, oriented to the task, no interest in multi-tasking, they don’t look for solutions but report problems to supervisor, high level of power-distance. Causes for this can be found in an education system based on subordination.

On the other hand, expats in this park remain longer than the average expat in China. Reasons for that can be found in the fact that here they have common services, a dining room for the 31 expats, contact amongst them, and an atmosphere where they feel at home. Expats are young, mostly men, global oriented and very highly qualified.

Mondragon Corporation maintains very good relations with the political powers, local as well as at the national level. "*Guanxi* is very important in a country where bureaucracy is as heavy as it is in China".

Ferran Vilaclara

21st September 2011

Commercial and Marketing Director at ROCA

Former Managing Director Asia Pacific at ROCA.

Roca has been present in Asia for 40 years already. Ten years ago, while visiting a customer in Hong Kong, they detected a great potential in China and decided to invest in the country.

According to Vilaclara, the key for success was that, right from the beginning, they did not establish in the country to manufacture, but to sell. The products are different to the ones used in Spain, so they need to be adapted. The offer must be complete: a firm cannot access the market with only part of the portfolio. That means that it has to be a very firm decision from the start. In other countries, you may be able to start testing some of the offer. In China this is not possible: you have to go for all.

As it is not possible to compete in price, Roca had very clear that they needed to compete on three levels:

- Quality product;
- The brand;
- Certain customer “pull”: the consumer, who perceives the advantage of a differentiated product, requests it and pulls it through the delivery channel.

The investment in marketing is increasingly more expensive. Television, boards, all kinds of publicity are becoming a huge barrier of entry. Ten years ago it was still affordable, while now those who try to access will have it pretty hard. The initial investment is also enormous. We can conclude then that the barriers of entry are considerable and not reachable for everyone.

For Roca, the distribution was done through distributors, which were former estate companies reconverted into dealers. Vilaclara estimates that Roca’s market share is 25% (not of the total sanitary products but the top segment). In fact, the positioning of Roca in China is at a higher level than in Spain, top range. This is the strategy followed by Inditex Group and other firms.

The growth potential is very high, with twenty million newly built housing every year. To serve such market, it is not possible to produce in Spain and transport the goods to China: it would be too expensive. One needs to produce in situ.

At first, they sent twelve “expats” to manage the facilities in China, but now the number has been limited to four, due to budget restrictions. It is extremely expensive to have expats in China, so it is much better to give authority to the Chinese organization, giving them training and capabilities. It is key to deliver clear ideas and a certain level of adaptation to the culture. This is quite an interesting concept: Vilaclara believes that firms have to adapt to the country, but should avoid becoming “too Chinese”. This would lead to a loss of quality level. The Chinese

would naturally move towards less costs and less quality (and if you are positioned in the top range, you cannot let that happen).

Some difficulties have been found in terms of values of the staff: there is a general lack of discipline, loyalty to the firm and commitment. They think short term, and after three years ahead there is nothing. Vilaclara has observed a lack of creativity in Chinese workers. On the one hand, the education system is based on repetition. On the other hand, Confucianism is based on the values of authority, superiority and the search of harmony above all. All these facts undermine the sense of creativity.

The State Statistics are unreliable and often made up. The prices of flats and food are rising enormously, which may lead to social conflict, strikes and general unrest. The workers are no longer ignorant peasants coming from rural areas, but on the contrary, they are open minded, have access to internet, are trained and have a more modern perception of the world. They know that there are rich people out there and expect a higher level of consumption for themselves.

China is a country that has moved from the paper letter to the email, without passing through the fax, as opposed to our western countries. The Chinese Government needs to control the situation and for that, it has become the largest marketing firm of the world.

Finally, as a conclusion, Vilaclara affirms that, to be successful in China, the General Manager must be surrounded by the best people he can find. Only then can they achieve their objectives in a difficult but attractive market. Retaining talent is difficult, but important.

Pablo Fano

15th October 2011

Specialist in Industrial goods. Commercial Office of Spain. Spanish Embassy in Shanghai.

There is a before and an after in the access to China by Spanish firms: before 2007 and after 2007. The way Spanish firms approach China has varied significantly in the last five years. Before, firms came with subsidies and nowadays there is no more public aid. Before they came without a proper clear objective, just because it was a "fashion". There were many firms that gave a go at China

Nowadays the situation is very different: the number of Spanish firms is limited to a small number, but they are more professional and they come more prepared. Some are large businesses but the majority are SMEs. Nowadays they register their brand (while before they did not). The crisis has enabled a "cleaning process" that has eliminated those businesses that were not totally committed. The process to access market is slow and firms need to be ready to wait for investment to give fruitful results. The owners are, more often than not, Chinese.

There is no longer such a thing as "opportunity sectors". The sector is not important, but how you do manage to manage the business. There are industrial sectors that are doing well, in energy, environmental industries, automotive, metal products, etc and the sector of luxury in the consumer goods.

The process of implantation in China is long and slow. The first piece of advice is to register the brand, which is something businesses do now, but not some years ago. Every week, at the Spanish Commercial Office, they receive complaints of Spanish firms that have been cheated in China. One has to be cautious and also firms have to contract professional services. Many firms, wanting to save those costs, have made costly mistakes.

He mentions some companies that are doing fine: Mondragon Corporation, Metalcaucho, Eurolaton, Telstar, Germans Boda or Icor.

As a conclusion, while some five years ago (and before that) many Spanish firms came to China unprepared and without clear objectives, nowadays the numbers have gone down but those companies who do try to access China are better prepared, more committed and have more possibilities of success.

Poli Eceizabarrena, CEO Metalocaucho (MTC)

Antxon San Vicente, General Manager Metalocaucho (MTC)

22nd November 2011

Since 1982, MTC designs and produces elements of rubber and metal for suspension and control of vibration systems of railway and automotive industries. More than 1,600 projects carried out in collaboration with the departments of world leader design firms guarantee its unstoppable path.

Metalocaucho is a provider of train components for the top world train manufacturers: Alstom, Bombardier, Talgo and Siemens, to name a few. 55% of their sales go to exports, which helps the company to enjoy being in a sector of rapid growth. The process of launching a new product takes between three and four months. The level of technology and complexity is very high.

The first time MTC went to China was in the framework of a trade mission with the Chamber of Commerce of Guipuzcoa. When they started negotiations to provide the Chinese market, they learned that the Chinese request as an imperative that at least 70% of the production is located in the Asian country. As a result, Metalocaucho had to take a decision: to establish a production plant in China in order to access this market. Later on (in 2011) the same decision was taken for the Indian market. Nowadays they count with three plants in the world: Urnieta in Spain, Suzhou in China and India.

Major difficulties found were:

- Adapt to difficult negotiation processes;
- Difficulty to access market because there is a reluctance to change providers, due to lack of technical knowledge;
- Costs are increasing in China: labour cost and raw materials are both in the rise;
- Risk is much higher when tackling a new market like this;
- The Renminbi is artificially undervalued;
- Governmental obstacles: legal, auditing or environmental requirements are imposed on foreign firms (often these requirements are more strictly applied to foreign firms compared to Chinese ones). Frequently there is not a sound technical basis for them;
- In China there is no concept of “customer” as in the west. Once a Chinese firm gets a new customer, they start failing in quality and putting prices up. But the customer is by now trapped and it is difficult to change providers. The only way to compete with them is therefore to give excellent service and be better than the Chinese competitors.

The major opportunity is the size of the market, which is truly large. MTC offers a high quality level while still competing in price: that is difficult to beat. Very high quality can be found at very high prices (Japanese firms) but MTC offers more competitive prices. A firm based only in Spain would find difficulties to survive: the development of new products and prototypes is expensive. Such a high investment can only be amortised if one can gain economies of scale: a large market is required.

So, in conclusion, we can affirm that only by establishing in large markets like China or India, can a firm survive in Spain.

The keys for success according MTC have been the following:

- being able to contact directly their prescriptors, like Alstom.
- Most of the managers are Chinese. The Production Manager should actually be Chinese
- Keep a very close contact with the plant: emails, conference calls, visits.

Cultural differences matter: Chinese people must always keep the “face”, their reputation is very important. Often they like to say they know high-ranking governmental officials, or they find it hard to accept they do not know something.

Comparing Indian and Chinese workers they do find major differences. The Chinese can be more active and plan more than in India, where there is a less ethical approach to working.

While it is true that in general the Chinese are cheaper at first because they still have lower labour costs, in the medium term they know that they have some weak points, namely lower technical knowledge and lower ability to develop new products. Salaries have increased enormously in the last years and are still going up (typical worker costing now over 200 euros a month). The peculiarity of this sector is that once the moulds have been done, they have the customer trapped. It is difficult for the client to change customers. Then they put prices up but they do not lose the business. To compete in China one must offer a competitive price, a high quality and the best service, just like MTC has done.

In the medium term, then, with the rise in salaries, the increase of the prices of raw materials and the appreciation of the local currency, China is no longer going to be able to continue being the low-cost country that is now.

As a conclusion, we can say that the railway industry requires a very high investment to develop a new product. Such initial cost can only be amortised if one can gain economies of scale. For that, a large and growing market is required. Only by establishing in vast markets like China or India, can a firm survive in Spain. This statement, which is true for the railway sector, can also be transferred to many other industrial and consumer sectors. Expanding to China can become a strategic decision that will constitute the opportunity to survive as a global firm..

Jaime Hernani

22nd November 2011

International Promotion Manager.

Bilbao Chamber of Commerce

The Chamber of Commerce organises different activities to promote the internationalization of Basque firms, in this case towards China, through trade missions, training, spread the knowledge about this vast country etc.

Hernani states that producing in China, if it is not to access their market, is no longer attractive. There are two reasons for this: in the first place, costs are rising fast. It is no longer cheap to produce in China. In the second place, quality is still very poor. Western firms are having many quality problems. The problem is that the Chinese are not increasing their prices to offer higher quality, but simply to increase their margins. Therefore their competitive position loses attractiveness.

China is a very peculiar case where they have moved from the bicycle to the Ferrari in one step. There is occultism from the public powers. Private property is not talked about openly and with transparency. Human rights have a different consideration compared to the west: there is a huge population of 1.4 billion and the priority is to feed them, not the civil rights.

It is true that Spanish firms have found themselves in situations where they have been copied (in an unrefined way). According to Hernani, the best policy to fight this bad practise is not so much to spend large amounts of money in lawyers' fares, but more to educate the Chinese consumers to value the quality and the brand: to notice the difference in spending money in a good product.

Hernani believes that is a difficult task to access the Chinese market. He gives some examples where the venture did not happen smoothly: Chupa Chups failed, Cola-Cao got copied, Panrico had to establish a very strict control in the distribution process, Volvo and Toyota have had huge quality problems... He concludes that It is not so much about selling, but about educating and teaching the Chinese our consumption patterns.

Alfredo Pastor

25th January 2012

Professor in the Department of Economics at IESE. Expert in China.

There is this futile, according to Pastor, discussion about China's GDP surpassing USA's. Of course it is going to happen. If the population is four times that of the US, so it is very logic that the Chinese GDP will be larger. On the other hand, the very high rate of growth of the last decades cannot be sustained for a very long time. It is quite normal that it is slowing down.

The growth is being pushed by the public investment and the exports. But the exports are limited by increasing labour cost and lower levels of labour reserves. So China is becoming increasingly less competitive. The situation of the families is deteriorating and the inequalities are increasing: there may be social problems in the future.

Even Wen Jiabao said "China's economic growth is unsteady, unbalanced, uncoordinated and unsustainable".

There are certain opportunities to access China's market, but "China is indeed for the Chinese": the market has not been properly liberalised and they have their own protectionist ways to make western firms' lives difficult.

- Exporting from Spain to China is very difficult; it is almost impossible to manufacture in Spain to sell in China;
- Produce and sell in China is easier. However, if the government may see you are earning good money, they can certainly complicate matters.

Already Saint Francisc Xavier demanded to send to China the best and cleverest of the people. The situation remains the same: apply your best human resources if you want to be successful in China.

Spain has given too often an image not serious enough. Some business people have not been professional, some airlines have established regular trips Spain-China to remove them quickly afterwards. The Chinese have a good memory and remember this kind of things. It would be better to go slowly but surely.

Pastor thinks that examples such as Mondragon Corporation are good examples to be followed in China. A mix of seriousness combined with "a capitalism without tears", the cooperative model, that is looked upon favourably by the Chinese Government.

In the process of accessing the Chinese market, the support of the government would be crucial. Pastor does not see this commitment, neither in this government nor in the previous one.

Spain could export food products and technology. We are competitive enough. The problem is that Spain has not got a reputation in the field of innovation or R&D: that is where the political support could be key.

Jacinto Soler

15th February 2012

Founder of Emergia Partners S.L. (corporate finance business specialised in joint ventures, mergers and acquisitions, business development and fundraising related to emerging markets, namely China and India).

Lecturer in the Master of Chinese Studies by the Pompeu Fabra University, in Barcelona.

In the beginning the firm Emergia did a lot of market research in China (around twenty studies per year). With internet and the relatively easy access to information, firms do not demand so much this kind of service, so Emergia has specialised in inverse operations: mixed firms, technology transfer, etc.

Networking is so vital that he thinks Chinese population living in Spain are the ones who can pull the process of accessing the Chinese market by Spanish companies. Chinese people in Spain are more mobile than us, know the language and the culture and the second generation is very well trained. We miss the contacts with the Chinese elite

There is a lobby group called China-American Young Leaders: they meet every six months in the US, or in China, alternatively. The American Government organises and pays for it. This kind of promotional activity really works.

The Spanish-Chinese Forum (Foro España-China www.fundeschina.com/foros.asp) would be the equivalent for Spain, but in this case, it is more like a cool destination for former top political figures. It is not effective.

When asked about the possibilities of accessing the Chinese market, he feels optimistic for the food sector, mostly wine and oil. But he believes that it is better to let the Chinese lead the processes: otherwise, Chinese authorities give problems concerning customs, certification processes, etc. Statistics show an increase of 60% of oil consumption. The Chinese are so protectionist, they want to pack it in China.

Spanish firms, according to Soler, are not systematic enough and no professional enough. They throw themselves into the first arms they can, doing often bad deals. According to his experience, too often they also lack of perseverance.

Chinese are over-protectionist: they promote their own brands, Made in China, forcing westerner firms to produce the goods in China.

Regarding staff, Soler thinks that it is more convenient to have Chinese people in China to solve the cultural barriers.

The negotiation process is very different in China compared to the west: it is necessary to see each other a lot, get to know each other thoroughly. They take months to sign a contract. They have a different working system. In the public

sector, they are reluctant when it comes to giving data, information. Hierarchy is very important. President of the Generalitat Montilla went to China to gain a contract so that China would build a car factory in Catalonia and ended up coming back without signing anything. Soler thinks the Chinese signed with Turkey in the end instead.

The key for success in business with China is the connections. To develop the network we need the Chinese population living in Spain.

Name to be kept confidential

MANGO

Responsible for Expansion to China

17th March 2012

Mango follows a global strategy, but adapted to each country (products need to be adapted in terms of the climate, size, colour, etc.). Mango organises an important event, a fashion catwalk every season in China. They try to give it the largest media exposure possible, through blogs, press and VIPs.

Chinese consumers love brands. That is a fact. The brand of Mango is very well considered now in China, but it was not the case only a few years ago. She explains the development of their expansion, in different steps. In 2002 Mango accessed the Chinese market through franchises. They grew rapidly, but they had serious problems coming from the mismanagement of the establishments: they were neglected, clothes on the floor, prices pushed down. This provoked a severe weakening of the Mango brand. By 2008, the positioning of the brand was negative.

Since then, the firm has made a huge effort to retake the management of the brand by regaining the property of many of the branches. For that, some drastic measures were taken, for instance, the “flag shop” in Nanning Road in Shanghai was closed down, which was a shock. In order to restore the brand, a re-launch of the shops and a reposition of Mango in a higher segment were required. The idea currently is that there are as many own shops, as there are franchises, 50/50, in order to retain the power. Nowadays there are 200 Mango establishments in China and the plan is to have as many as 700 in five years. That means that 100 shops are opened every year. Openings are mostly planned for Tier 2 cities, with more potential growth expected than the mature markets of the Tier 1 cities.

Some years ago, companies did not take China into account. Now, it is one of the main markets, and the one that grows the most. But one needs to invest heavily in advertising: through events, billboards, on-line marketing, digital tv, banners in web sites, showrooms, shootings, interviews, etc. The last campaign with Kate Moss has been very successful.

The market is extremely competitive, with many brands competing ferociously: Inditex, Mango, H&M, Vero Moda, Uniclo (a Japanese brand that is coming very strong), and many others, even local Chinese chains. She believes that, as an example of best practice, Massimo Dutti is doing a great expansion in China, with an impeccable image, shop windows, styling, all following a very coherent and solid strategy.

Mango is specialised in the design of the fashion, but does not produce the clothes themselves. They outsource all the production to countries such as Turkey, China, Cambodia, Vietnam, Thailand, and many others (while most of the shoe wear is made in Spain). All the world production goes to Barcelona, where it is controlled and re-sent all over the world.

Mihaly Simai

20th June 2012

Economist. Professor at Corvinus University

Professor Simai is a member of the Hungarian Academy of Sciences. Currently he is working in the Institute for World Economics of the Hungarian Academy of Sciences as a Research Professor. He is also a Professor at Corvinus University in Budapest. He is the Honorary President of the World Federation of United Nations Associations.

When I explain the subject being researched upon, he makes three notes:

1. qualify the market: are we talking about the consumer goods or investment goods.
2. China is not an integrated unified market. Different provinces, different parts of China have different types of consumers. Farmers in the west vs urban population in the east (not just along the coast but in the urban agglomerates covering 2,000-2,500 km inland). Also the international suppliers are different for each part: Russia along its border and Japan, US, Germany and France towards the east.
3. The interesting subject is the consumer habits of the Chinese middle class, about 250 million people. He proposes to study the demand and the supply.

The main opportunities he detects are the following:

- consumer goods such as wine, although competition is ferocious
- High-tech or even mid-tech for certain special products, such as the defense industry (companies such as Indra)
- Tourism: Attract Chinese middle class tourists towards Spain, not so much the sun and sea tourism but more cities with culture and left overs of the Arab culture. This is in his opinion, the most important opportunity.

Main challenge for China: according to him, the political future is the main worry, in two senses:

1. How to cope with increasing inequalities and social tensions. Uprisings are possibly going to increase.
2. How to cope with the increasing power of regional centres. Two institutions keep the country together: the Communist Party and the army. However, these two are evolving and who knows how they will do so. In the past there were war lords.

He does not see likely a Chinese version of the Arab spring, because in these countries there was a large group of unemployed youth with no hope and no family support. In China there is employment for all so far, and the *social lift* works.

Who wants democracy in China? the middle class is pragmatic and therefore not interested. The rural class neither being to focus on their own basic needs. Only the intellectuals are willing, and that is not enough to start a change process. Simai

refers to a book he edited: "Democratic process and the market". UN University. 1999. Takashi Inoguchi or similar.

Certain conditions were detected for sustainable democracy:

- highly educated population who understand problems and cannot be easily manipulated
- tolerant and enlightened political leaders
- resilient and flexible institutions
- standard of living that creates an increasing cake that satisfies most people.

Out of these, Simai considers that China only fulfills the last one: the cake is big and growing enough. However, even that condition is doubtful since China gets affected by the world crisis: because of the demand crisis in the west plus an economy based mainly in exports, China has lost more than 14 million salaried employees, who must have gone back to their villages.

The direction in which the political power will go is still uncertain and will depend on two factors: first, if the economic development continues. Second, if it does, will the growth be integrative, will the economic development favor the majority of the population.

Agnes Szunomar

21st June 2012.

Research Fellow. Institute of World Economics. Research Center for Economic and Regional Studies of the Hungarian Academy of Sciences.

She thinks that Hungarian firms have the same difficulties as Spanish firms, but more, due to the small size of the country. She is aware of companies doing business successfully in the fields of water treatment and environmental solutions. The best example would be Organica, that started with a plant and has now some more. She knows of firms that have had intellectual property rights problems.

She thinks that China still is the world's factory, perhaps not the whole of the country but the western part. She thinks the country is large enough to have different roles in different parts. In her view, China is not an emerged economy, but still an emergent one.

The development of China was intended to go more towards the promotion of domestic consumption, promoted by the government. However, China is got enough internal problems that will not allow the domestic demand to grow. So GDP increases will have to depend on exports for some more years. With a developed world in recession, exports will have to go towards emerging and developing countries. Probably China feels more comfortable with these countries (and vice versa). Already two thirds of Chinese Direct Investment goes to developing countries.

No revolution is expected. Changes are coming, people know it and they know how to be patient. The problem is that annual growth of at least 7-8% annual growth is the minimum required to sustain employment, and therefore, the system.

Her thesis is about China as a new superpower: are we attending a process where a new superpower is appearing? Is China going to replace the USA, or are they going to rule the world together through a bi-polar world? She thinks neither: the world will be multi-polar: US, China, Brazil, Russia, the EU. She believes that China does not want to be the world superpower. Maybe the "soft power" but never the "hard power" in US style. Chinese model will differ greatly from the US: it will be based in economic relations, trade and investment, but not in political decisions, army interventions, or even cultural domination.

Annex 3. Contacts of interest in China / about China)

In alphabetical order:

Institution / Company	Interest	Internet address
Asian Development Bank (ADB)	<p>Multilateral development bank, dedicated to reducing poverty in Asia and the Pacific region through inclusive economic growth, environmentally sustainable growth, and regional integration.</p> <p>Good source of Working Papers, Research and data on macroeconomics, poverty, trade and investment, etc for 45+ country members in the Asia Pacific Region (Statistical Data Base).</p>	www.adb.org
Cámara Oficial de Comercio de España en China	<p>The Chamber of Commerce of Spain in China is officially a single entity, which through a network of three offices, Beijing , Shanghai and South China, aims to cover the vast territory of the R. P China to promote trade relations between Spain and China, and the interests of its members.</p> <p>Good contact for trade fairs, business trips, publications, list of members, contacts, etc.</p>	www.spanishchamber-ch.com/
Casa Asia	<p>Casa Asia was created with the will to strengthen the knowledge and dialogue about Asia in Spain, with the analysis and discussion of civic, political, social, cultural, economic and environmental issues, supporting activities and projects that contribute to a better knowledge between Asian and Spanish societies, and to promote the development of relations among them.</p> <p>Casa Asia was created in 2001 with a consortium made up of the Ministry of Foreign Affairs and Cooperation, through its Spanish Agency for International Cooperation for Development (AECID), the Government of Catalonia and the Barcelona and Madrid City Councils.</p> <p>Great for courses, training, library and advice.</p>	www.casaasia.es

Institution / Company	Interest	Internet address
<p>China Council for the Promotion of International Trade</p> <p>It has a simultaneous name: China Chamber of International Commerce (CCOIC).</p>	<p>Established in May 1952, China Council for the Promotion of International Trade (CCPIT) comprises VIPS, enterprises and organizations representing the economic and trade sectors in China. It is the most important and the largest institution for the promotion of foreign trade in China.</p> <p>The aims of the CCPIT are to operate and promote foreign trade, to use foreign investment, to introduce advanced foreign technologies, etc.</p> <p>Good source of data as well.</p>	<p>In Chinese: www.ccpit.org In English: www.bizchinanow.com</p>
<p>China Today</p>	<p>General news on China: entertainment, cities and provinces, education, diplomatic missions, import & export, people & society, and a whole variety of general and specific subjects. Interesting articles and subjects, in a widespread sense.</p>	<p>www.chinatoday.com</p>
<p>Culture Asia World News Network</p>	<p>Popular approach to culture and news from Asia: Culture Asia provides Asia World News from the most comprehensive global news network on the internet. Searchable news in 44 languages from WorldNews.</p>	<p>www.cultureasia.com</p>
<p>Electronic Commerce E-commerce pages most widely used in China</p>	<p>Useful to know the products, compare prices, look for buyers, find suppliers. Benchmarking in general.</p>	<p>www.alibaba.com www.b2bbyte.com www.made-in-china.com www.diytrade.com www.busytrade.com www.taobao.com (only in Chinese)</p>
<p>Generalitat de Catalunya ACCIO Or ACC10</p>	<p>ACC1Ó is the agency set up by the Catalan Government to make Catalan enterprise more competitive throughout the world. Its key aims are to drive innovation, internationalisation and attract inward investment.</p> <p>ACC1Ó is based in Barcelona with an international network of a further 35</p>	<p>www.acc10.cat</p>

Institution / Company	Interest	Internet address
	Business Promotion Centres covering some 70 markets worldwide. It provides advice and practical help for businesses with a vocation to expand worldwide.	
ICEX Instituto Español de Comercio Exterior (Spanish Institute for Foreign Trade)	<p>The Spanish Institute for Foreign Trade (ICEX) is a national public company whose mission is to promote the internationalization of Spanish companies to contribute to their competitiveness and add value to the economy as a whole.</p> <p>It provides its services through a network of 31 Provincial and Territorial Trade in Spain and nearly 100 Economic and Trade Offices overseas. It also has of 13 business centres abroad, offering temporary infrastructure Spanish companies as an incubator of internationalization.</p> <p>Great for publications, trade data and contacts with offices overseas.</p>	www.icex.es
International Monetary Fund IMF	<p>The International Monetary Fund (IMF) is an organization of 187 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world.</p> <p>Main Databases: World Economic Outlook (WEO), Data on Trade Statistics (DOTS) and Financial data (IFS).</p>	www.imf.org
Invest in China (part of the Ministry of Commerce)	Information for those interested in investing in China	www.fdi.gov.cn
Ministry of Commerce, People's Republic of China	<p>Main mission: to formulate development strategies, guidelines and policies of domestic and foreign trade and international economic cooperation.</p> <p>Good source of data, statistics on trade, investment, significant news, etc.</p>	http://english.mofcom.gov.cn/

Institution / Company	Interest	Internet address
	They have an interesting and comprehensive report “Doing business in China” for each province.	
National Bureau of Statistics of China	Contains and updates the most reliable statistical data available for China. In English, searches can also be done in English.	http://www.stats.gov.cn/english/
Search engine in internet Baidu	The relations between Google and China have always been tense. In 2010, searching via all Google search sites was totally shut down in Mainland China. Nowadays, the most popular search engine in China is baidu.com.	www.baidu.com
The US-China Business Council (USCBC)	<p>The US-China Business Council, Inc. (USCBC) is a private, nonprofit organization of roughly 220 American companies that do business with China. Founded in 1973, USCBC has provided unmatched information, advisory, advocacy, and program services to its membership for more than three decades. It favors constructive engagement with China to eliminate trade and investment barriers and develop a rules-based commercial environment that is predictable and transparent to all parties.</p> <p>Good source of trade data.</p>	www.uschina.org
World Bank	<p>The World Bank is a source of financial and technical assistance to developing countries around the world. Its mission is to fight poverty for lasting results and to help people help themselves and their environment by providing resources, sharing knowledge, building capacity and forging partnerships in the public and private sectors. It counts with 187 member countries.</p> <p>Good source for indicators of all sorts.</p>	www.worldbank.org

Annex 4. Questionnaire sent to Spanish businesses in China

Your business experience in China | PhD Research at University Abat Oliba CEU

Dear Mr, Ms.

My name is Eva Perea. I lecture in Strategic Management at the Abat Oliba CEU University in Barcelona, within the Department of Economics and Business, where I am also currently doing a PhD. My research aims to analyse the opportunities for Spanish businesses in the Chinese Market. It aims to highlight also the difficulties that such businesses find to set up in China and doing business there. I need to find out how executives of these firms (whether Chinese or expats) perceive their experience in doing business in China. It is for this reason that I would like to ask you for your kind collaboration, through this simple and easy-to-fill questionnaire that will not take you more than five minutes to fill. On my side, I commit to behave following the International Code of Conduct CCI/ESOMAR for social and market research, so all the data you supply will be treated in an anonymous and confidential way.

To thank you for your help, I commit to send to you a summary of the aggregated results as soon as the survey is completed. For any additional questions, please contact me by telephone +34 932 540 900 or by email (epeream@uao.es).

Thank you in advance for your help.

Yours sincerely,

Eva Perea

ID Card nb: 30583233H

First and last name:

Company name:

1. Which is the main sector where your firm operates?(if it operates in more than one, choose the one that generates higher sales)

2. Approximately, how many employees has your firm worldwide?

3. And approximately, how many employees has your firm in China?

4. Which year did your company start to operate in China? We refer to the moment when trade relations started.

- In which region or regions did your company settle?
- Pearl River Delta
 - Yangtze River Delta
 - Bohai Bay
 - Other(s)

- What legal entity did your firm choose in China?
- Representation Office
- Joint Venture
- WFOE
- Other

7. Approximately, what was your company's initial investment in China?

8. When trying to access the Chinese market, to what extent was or is now a difficulty for your company each of the following factors?

	Not at all difficult	A little	Some	Quite	Very difficult
Find distributors	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Create own distribution channel	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Local culture	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
The language	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
National and/or local legislation	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Administrative procedures	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Find suitable local human resources	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Find suitable expat human resources	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Lack of market knowledge	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Required investment	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Intellectual Property	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Geographical distance	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Traveling costs	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

	Not at all difficult	A little	Some	Quite	Very difficult
Compete with competitors' prices	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

9. Next, you will find different reasons for a company to set up business in China. Please indicate, according to the scale, to which extent each reason was or not relevant in your case:

	No relevance	Little	Some	Quite	Very relevant
Access to the Chinese market	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Access to other markets in Asia	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Setting up as a mandatory requirement to sell in China	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Access to raw materials	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Detection of business opportunities	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Strategy to follow	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

10. Please answer this question if you plan to remain in China. Think now what are the strategic priorities of your business in China for the next three years and value each one of the list below according to its importance.

	No priority whatsoever	A little	Some	Quite	Absolute priority
Brand consolidation	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

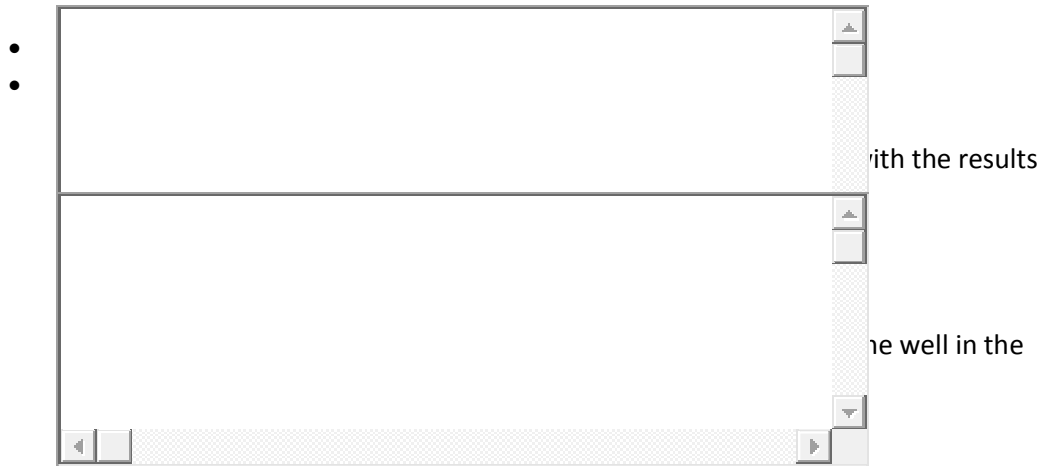
	No priority whatsoever	A little	Some	Quite	Absolute priority
Improve customers' satisfaction level	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Expand initial investment	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Optimise costs	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Enter new markets	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Mergers and acquisitions in China	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Invest in R&D	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Implement western culture in business	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Product and / or services outsourcing	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Distribution consolidation	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Improve quality	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Desinvest in the country	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

11. Regarding the continuity of your company in China in the next three years, choose one of the following options:

- You will continue most certainly
- You will probably continue
- Perhaps
- You will probably quit the country
- You will quit most certainly

12. To what extent are you satisfied with the results obtained in China for your company so far:

- Totally satisfied
- Quite satisfied
- A little satisfied



Thank you very much for your cooperation. Soon we will send you a summary of the results obtained.

Annex 5. Cuestionario enviado a las empresas españolas en China

Su experiencia empresarial en China- Doctorado Universitat Abat Oliba CEU

Estimado Sr. / Sra.

Mi nombre es Eva Perea. Soy profesora de Dirección Estratégica en la Universitat Abat Oliba CEU de Barcelona, en el Departamento de Ciencias Económicas y Empresariales, donde además me encuentro realizando el Doctorado. Mi investigación analiza las oportunidades para las empresas españolas en el mercado de China. Por otro lado, intenta detectar también las dificultades que dichas empresas encuentran para implantarse y para hacer negocios en este país. Necesitaría conocer de primera mano cómo piensan los directivos de las empresas y cuál ha sido su experiencia en China. Es por ello que solicito su amable colaboración a través de una corta encuesta de muy sencilla cumplimentación que no le llevará más de cinco minutos. Por mi parte me comprometo a actuar según el Código Internacional de Conducta CCI/ESOMAR para la práctica de Investigación social y de mercados, por lo que todos los datos proporcionados se tratarán de forma anónima y confidencial.

Como agradecimiento a su ayuda, me comprometo a enviarles un resumen de los datos agregados recogidos una vez finalizada la encuesta.

Para cualquier consulta adicional que precise puede contactar conmigo en el tfno. +34 676 826 828 o por correo electrónico (epeream@uao.es).

Agradeciéndole de antemano su colaboración,

Atentamente,

Eva Perea

D.N.I. 30583233H

Nombre y apellidos:

Nombre de la empresa:

1. ¿En qué sector de los que aparecen en el listado opera principalmente su empresa en China?(si opera en varios sectores cite el que genere más volumen de facturación)

2. Aproximadamente ¿cuántos empleados tiene su empresa en todo el mundo?

3. Y aproximadamente ¿cuántos empleados tiene su empresa en China?

4. ¿En qué año empezó a operar su empresa en China? Nos referimos al momento en que comienzan las relaciones comerciales.

5. ¿En que región o regiones de China se ha implantado su empresa?

- Delta del Río Perla
- Delta del río Yangtse
- Bahía de Bohai
- Otro:

6. ¿Qué tipología de establecimiento han escogido a la hora de implantarse en China?
- Oficina de Representación
 - Joint Venture
 - WFOE
 - Otro:

7. Aproximadamente, ¿Cuál fue la Inversión inicial de su empresa en China?

8. A continuación verá diferentes motivos por los que una empresa puede tomar la decisión de instalarse en China. Será Ud. tan amable de indicar, conforme a la escala, hasta qué punto cada motivo fue o no importante en su caso para instalarse en China.

	ninguna	poca	alguna	bastante	mucha importancia
El coste de la mano de obra	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
El acceso al mercado de China	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
El acceso a otros mercados asiáticos	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
La implantación como requisito obligatorio para poder vender en China	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
El acceso a materias primas	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
La detección de oportunidades de negocio	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
<div style="border: 1px solid black; height: 100px; width: 500px; margin-bottom: 5px;"></div>					<input type="radio"/>
					arse en China y no or.

9. A la hora de tratar de acceder al mercado de China, ¿hasta qué punto fue o es en la actualidad una dificultad para su empresa cada uno de los siguientes factores?

	Nada	Poca	Alguna	Bastante	Mucha dificultad
Encontrar distribuidor	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Crear una red de distribución propia	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
La cultura local	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
El idioma	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Legislación nacional y/o local	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Los procesos administrativos	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Encontrar el personal local adecuado	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Encontrar el personal expatriado adecuado	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Desconocimiento del mercado	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Volumen de la inversión necesaria	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
La propiedad intelectual	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
La distancia geográfica	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
El coste de los desplazamientos	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Competir con los precios del mercado	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>



el listado anterior,

10. (Por favor, conteste esta pregunta solo si su empresa tiene intención de permanecer en China). Piense ahora en las prioridades estratégicas de su empresa en China para los próximos tres años y valore cada una de las que aparecen en el listado según su nivel de importancia.

	Nada	Poco	Algo	Bastante	Muy prioritario
Consolidar la marca	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Mejorar el nivel de satisfacción del cliente	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ampliar la inversión actual	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Optimizar costes	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Entrar en nuevos mercados	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Adquisiciones o fusiones de empresas presentes en el país	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Invertir en I+D	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Implementar cultura empresarial occidental en la empresa	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Externalizar la producción	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Consolidar la distribución	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Mejorar la calidad	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

	Nada	Poco	Algo	Bastante	Muy prioritario
Desinvertir en el país	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

11. Respecto a la continuidad de su empresa en China en los próximos tres años, escoja una de las siguientes opciones:

- Con toda seguridad continuará en el país
- Probablemente continuará
- Quizás sí o quizás no
- Probablemente se irán del país
- Con toda seguridad se irán

12. Hasta qué punto está Ud. satisfecho con los resultados obtenidos en China por su empresa hasta el momento:

- Muy satisfecho
- Bastante satisfecho
-
-
-
-

nsatisfecho con los

presa en el proceso

Muchas gracias por su colaboración. Próximamente le enviaremos un resumen de los resultados obtenidos.

Annex 6. Main business events in China

US-China Business Council Links List¹⁰⁵

- [Business Services](#)
- [Education, Academia, & Sinology](#)
- [China Internet Networks](#)
- [Events—Trade Shows & Conferences](#)
- [Finance & Economics](#)
- [Government, US](#)
- [Government, PRC-National](#)
- [Government, PRC-Regional](#)
- [Human Resources](#)
- [Laws & Regulations](#)
- [Living in China](#)
- [Media, International](#)
- [Media, PRC](#)
- [Organizations, Business](#)
- [Organizations, Other](#)
- [Security](#)
- [Statistics & Data](#)
- [Trade](#)
- [Travel](#)
- [Zones/Regions](#)
- [Other/Miscellaneous](#)

If you would like to add your company to the *China Business Review's* new US-China Business Services Directory, please visit <https://www.chinabusinessreview.com/directory/>.

Business Services

- [China Business Review Business Services Directory](#)

Education, Academia, and Sinology

- [Asian Studies WWW Virtual Library](#)
- [Australian Center of the Asian Spatial Information and Analysis Network](#)
- [China Education and Research Network](#)
- [China Europe International Business School \(CEIBS\)](#)
- [Institute of Asian Research—University of British Columbia](#)
- [John Fairbank Memorial Chinese History Virtual Library](#)
- [Los Angeles Chinese Learning Center](#)
- [Zhongwen Chinese Etymological Dictionary](#)

China Internet Networks

- [China Today](#)
- [Yahoo Chinese \(Simplified\)](#) and [Yahoo Chinese \(Traditional\)](#)
More than 10,000 websites in Chinese, divided into 14 main categories by a team of Yahoo! surfers who are native Chinese speakers from China, Hong Kong, and Taiwan. The sites feature general interest content for topics relevant to Chinese speakers anywhere in the world, including arts, sports, astronomy, culture, and Chinese medicine.

¹⁰⁵ US-CHINA BUSINESS COUNCIL. WWW.USCHINA.ORG. NOVEMBER 2012.

Events—Trade Shows and Conferences

- [China Business Review China Conference Calendar](#)
- [The Adsale Group](#)
- [China Business World—Exhibitions & Trade Show Info](#)
- [China International Fair for Investment and Trade](#)
- [China International Exhibition for Surface Finishing and Coating Products](#)
- [Chinese Export Commodities Fair \(Canton Fair\)](#)
- [Institute for International Research Conferences](#)
- [Business & Industrial Trade Fairs](#)
- [Trade Show Central](#)
- [USTDA](#)
- [China East-West Cooperative Trade Forum](#)

Finance and Economics

- [AsianBondsOnline](#)
- [Asian Development Bank \(ADB\)](#)
- [China Economic Information Network](#)
- [China Quota](#)
- [ChinaSite.com's venture capital page](#)
- [CNN Financial News Network](#)
- [Economist Intelligence Unit \(EIU\)](#)
- [Export-Import Bank, US \(Ex-Im\)](#)
- [Interfund Capital Corp.](#)
- [International Finance Corp. \(IFC\)](#)
- [International Monetary Fund's China page](#)
- [Investment Promotion Network \(IPAnet\)](#)
- [People's Bank of China](#)
- [Securities and Futures Commission of Hong Kong](#)
- [The World Bank](#)

Government — US

- [Central Intelligence Agency, \(CIA\)](#)
Includes a thorough history of China as well as up to date facts and statistics in the [CIA Factbook: China](#)
- [Copyright Office, US](#)
Provides information about copyright laws and procedures
- [Department of Agriculture, US \(USDA\)](#)
This site includes [Foreign Agricultural Service](#), which provides statistics on US exports and imports for numerous agricultural commodities over the past five years. Visitors can search by commodity, country, or specific regional groupings, such as the [Association of Southeast Asian Nations \(ASEAN\)](#).
- [Department of Commerce, US \(DOC\)](#)
DOC's website includes US census, defense conversion, budget statistics and the [Patent and Trademark Office](#).

- DOC's Advocacy Center, which interacts with foreign governments to enhance US exports abroad.
- DOC's Commercial Service (USCS), which helps small and medium-sized businesses by performing market research, holding trade shows, introducing buyers and distributors, as well as providing counsel and advocacy services
- Department of State, US (DOS)
The DOS website contains links to China-related pages including the US Embassy in China, General Consular Affairs, and the US consulate in Hong Kong. Other links include The Bureau of East Asian and Pacific Affairs and the State Department's Human Rights Reports on China, Hong Kong, and Macao.
- FBIS--Foreign Broadcast Information Service
The material in the World News Connection (WNC) is provided to the National Technical Information Service by FBIS, a US government agency. For a low monthly fee, WNC subscribers can search FBIS articles.
- Fedworld
At the US government-run Fedworld's main site, visitors can search all US government sites. It includes links to NTIS and FBIS, among others.
- Govt. Printing Office (GPO)
GPO Access permits full-text searching of such publications as Commerce Business Daily, Congressional Record, Federal Budget, and Federal Register.
- International Trade Administration, US (ITA)
Includes ITA's China Gateway Homepage
- Library of Congress
Visitors can access library services, the US Copyright Office, and the Thomas Register, which includes comprehensive legislative information.
- Thomas: Legislative Information
The website of the US Congress.
- United States Embassy in China
Provides access to all of the embassy sections, including the US Foreign & Commercial Service, which offers trade statistics and industry sector briefs.
- Bureau of International Information Programs (USIA)
The parent of the Voice of America (VOA), USIA's site include news of US-China and East Asian affairs in the USIA: Daily Washington File, among other sources.
- United States Trade Representative (USTR)
The USTR site provides prepared speeches and USTR reports, trade agreements--including the GATT/WTO Agreement--and press releases.
- US Trade and Development Agency, which is responsible for advancing US trade interests in developing countries.
- Voice of America (VOA)
This site contains useful information from VOA broadcasts, such as Chinese texts and broadcast schedules.

Government — PRC, National

- [China Bidding](#) — the official site for PRC government and public sector tendering notices
- [China Insurance Regulatory Commission \(CIRC\)](#)
- [China Certification and Inspection \(Group\) Co., Ltd.](#)
- [China Securities Regulatory Commission \(CSRC\)](#)
- [China's Eleventh Five-Year Plan](#)
- [Ministry of Agriculture \(MOA\)](#)
- [Ministry of Communications \(MOC\)](#)
- [Ministry of Finance \(MOF\)](#)
- [Ministry of Foreign Affairs \(MOFA\)](#)
- [Ministry of Commerce \(MOFCOM\)](#)
- [Ministry of Information Industry \(MII\)](#)
- [Ministry of Labor and Social Security \(MLSS\)](#)
- [Ministry of Science and Technology \(MOST\)](#)
- [National People's Congress \(NPC\), Supreme People's Court, and more.](#)
- [People's Bank of China \(PBOC\)](#)
- [PRC Embassy in Washington, DC](#)
- [PRC Organization Chart \(CBW\)](#)
- [State Administration of Foreign Exchange \(SAFE\)](#)
- [State Administration of Radio, Film, and Television \(SARFT\)](#)
- [State Administration of Taxation \(SAT\)](#)
- [State Development Planning Commission \(SDPC\)](#)
- [MOFCOM's China Trade Remedy Information](#)
- [State Intellectual Property Office](#)

Government — PRC, Regional

- [Hong Kong—Bilingual Laws Information System](#)
- [Hong Kong—Government Information Centre](#)

Human Resources

- [ChinaHR](#)
- [Dragon Surf Careerwise](#)
- [Job China Net](#)
- [Wang & Li Asia Resources](#)
- [Zhaopin](#)

Laws and Regulations

- [China Court](#)
- [Sino Laws](#)
- [LawinfoChina.com](#)
- [PRC Ministry of Commerce](#)
- [State Intellectual Property Office](#)

Living in China

- [China Insight](#)
- [Expats in China](#)
- [Expats in Shanghai](#)

Media—International

- [AllYouCanRead](#)
- [Asia Observer](#)
- [China Books and Periodicals](#)
- [China Business Review](#)
- [The China Business Show](#)
- [China Development Gateway](#)
- [China Economic Review](#)
- [China Online](#)
- [China Success Stories](#)
- [China Today](#)
- [Chinability](#)
- [Chinadotcom Corporation](#)
- [CNN World Index](#)
- [The Economist](#)
- [Economist Intelligence Unit \(EIU\)](#)
- [The Economist's China Briefing](#)
- [Far Eastern Economic Review \(FEER\)](#)
- [Foreign Affairs](#)
- [Harvard China Review](#)
- [Inside China Today](#)
- [Muzi News](#)
- [PR Newswire](#)
- [SinaNet](#)
- [Sinofile](#)
- [SN Web](#)
- [South China Morning Post](#)
- [Voice of America](#)
- [World Bank Publications](#)
- [World News Connection \(WNC\)](#)
- [Yahoo Chinese \(Simplified\)](#) and [Yahoo Chinese \(Traditional\)](#)

Media—PRC

- [Beijing Youth Daily](#)
- [China Central Television \(CCTV\)](#)
- [China Daily](#)
- [Chinapages](#)
- [Guangzhou Daily](#)
- [People's Daily \(in Chinese\)](#)
- [People's Daily \(in English\)](#)
- [Xinhua News Agency](#)

Organizations—Business

- [American Chamber of Commerce in China](#)
- [American Chamber of Commerce in Hong Kong](#)
- [Asian Development Bank \(ADB\)](#)
- [Asia-Pacific Economic Cooperation](#)
- [Business for Social Responsibility](#)
- [China-Britain Business Council](#)
- [Canada-China Business Council](#)
- [China Council for the Promotion of International Trade](#)
- [Chinese Manufacturers' Association of Hong Kong](#)
- [Hong Kong Chamber of Commerce](#)
- [Hong Kong Chamber of Commerce's "WTO Corner"](#)
- [Hong Kong Software Industry Information Centre](#)
- [Hong Kong Trade Development Council](#)
- [Interfaith Center on Corporate Responsibility](#)
- [International Chamber of Commerce \(ICC\)](#)
- [International Standards Organization—ISO Online](#)
- [US Chamber of Commerce](#)
- [US-China Business Council](#)
- [World Cargo Alliance](#)
- [World Trade Organization \(WTO\)](#)

Organizations—Other

- [Asia Foundation](#)
- [Asia Pacific Foundation of Canada](#)
- [Asia Society](#)
- [Business for Social Responsibility](#)
- [Center for Strategic & International Studies \(CSIS\)](#)
- [China Education and Research Network](#)
- [China Institute](#)
- [China Rural Villager Self-Governance Information Net](#)
- [Council on Foreign Relations](#)
- [East-West Center](#)
- [Fair Labor Association](#)
- [Human Rights in China](#)
- [Human Rights Watch](#)
- [Interfaith Center on Corporate Responsibility](#)
- [International Labor Organization](#)
- [International Monetary Fund's China page](#)
- [International Organization for Standardization](#)
- [International Labor Rights Fund](#)
- [Human Rights First](#)
- [National Committee on US-China Relations](#)
- [State Council Development Research Center](#)
- [UN Global Compact](#)
- [United Nations \(UN\) organizations in China](#)
- [United Nations High Commissioner for Human Rights](#)

- [US-China Policy Foundation](#)

Security

- [CSIS](#)
- [RAND](#)
- [Stimson Center—Henry L. Stimson Center](#)
- [Taiwan Security Research](#)

Statistics & Data

- [China Dimensions](#)
- [China Statistical Information Network](#)
- [PRC National Bureau of Statistics](#)
- [STAT-USA/Internet Site Economic, Trade, Business Information](#)

Trade

- [Asia Pacific Economic Cooperation \(APEC\) Forum](#)
- [APEC Small and Medium Enterprise Service Alliance \(SMESA\)](#)
- [APEC Tariff Database](#)
- [Asian Sources Online](#)
- [ITA's China Gateway Homepage](#)
- [Easysourcing](#)
- [EU-China bilateral trade](#)
- [Ministry of Commerce \(MOFCOM\)](#)
- [Sinoprojects](#)
- [United States Trade Representative \(USTR\)](#)
- [US-China Business Council](#)
- [World Cargo Alliance](#)
- [World Trade Organization \(WTO\)](#)
- [WTO Agreement on Technical Barriers to Trade](#)

Travel

- [Chinese Business World \(Travel, Air Schedules & Visa Information\)](#)
- [Fodor's Guide](#)
- [Lonely Planet](#)

Zones/Regions

Economic and Technological Development Zones

- [Beijing Economic and Technological Development Zone](#)
- [Changchun Economic and Technological Development Zone](#)
- [Changsha Economic and Technological Development Zone](#)
- [Chongqing Economic and Technological Development Zone](#)
- [Dalian Economic and Technical Development Zone](#)
- [Fuzhou Economic and Technological Development Zone](#)

- [Guangzhou Economic and Technological Development District](#)
- [Guiyang Economic and Technological Development Zone](#)
- [Hainan Yangpu Economic and Technological Development Zone](#)
- [Harbin Economic and Technological Development Zone](#)
- [Hefei Economic and Technological Development Zone](#)
- [Hohhot Economic and Technological Development Zone](#)
- [Kunming Economic and Technological Development Zone](#)
- [Kunshan Economic and Technological Development Zone](#)
- [Lanzhou Economic and Technological Development Zone](#)
- [Lianyungang Investment Development Page](#)
- [Nanchang Economic and Technological Development Zone](#)
- [Nanjing Economic and Technological Development Zone](#)
- [Nanning Economic and Technological Development Zone](#)
- [Nantong Economic and Technological Development Zone](#)
- [Ningbo Economic and Technological Development Zone](#)
- [Ningbo Daxiedao Economic and Technological Development Zone](#)
- [Qingdao Economic and Technological Development Zone](#)
- [Qinghuangdao Economic and Technological Development Zone](#)
- [Shanghai Hongqiao Economic and Technological Development Zone](#)
- [Shanghai Jinqiao Economic and Technological Development Zone](#)
- [Shanghai Minhang Economic and Technological Development Zone](#)
- [Shanghai Pudong Economic and Technological Development Zone](#)
- [Shenyang Economic and Technological Development Zone](#)
- [Suzhou Economic and Technological Development Zone](#)
- [Taiyuan Economic and Technological Development Zone](#)
- [Tianjin Economic and Technological Development Zone](#)
- [Urumchi Economic and Technological Development Zone](#)
- [Weihai Economic and Technological Development Zone](#)
- [Wuhan Economic and Technological Development Zone](#)
- [Wuhu Economic and Technological Development Zone](#)
- [Xi'An Economic and Technological Development Zone](#)
- [Xiaoshan Economic and Technological Development Zone](#)
- [Xining Economic and Technological Development Zone](#)
- [Yinkou Economic and Technological Development Zone](#)
- [Zhanjiang Economic and Technological Development Zone](#)
- [Zhengzhou Economic and Technological Development Zone](#)

Free-Trade Zones

- [Dalian Free Trade Zone](#)
- [Fuzhou Free Trade Zone](#)
- [Haikou Free Trade Zone](#)
- [Ningbo Free Trade Zone](#)
- [Qingdao Free Trade Zone](#)
- [Shanghai Waigaoqiao Free Trade Zone](#)
- [Shantou Free Trade Zone](#)
- [Shenzhen Free Trade Zone](#)
- [Tianjin Free Trade Zone](#)
- [Zhangjiagang Free Trade Zone](#)

- Zhuhai Free Trade Zone

Export Processing Zones

- Beijing Tianzhu Export Processing Zone
- Dalian Export Processing Zone
- Guangzhou Export Processing Zone
- Hangzhou Export Processing Zone
- Huichun Export Processing Zone
- Kunshan Export Processing Zone
- Suzhou Export Processing Zone
- Tianjin Export Processing Zone
- Weihai Export Processing Zone
- Wuhan Export Processing Zone

Other/Miscellaneous

- Australian Center of the Asian Spatial Information and Analysis Network
- China Site
- Scanweather

Annex 7. Description of legal business forms in China

A summary of the various forms of doing business in China¹⁰⁶

The vehicles most commonly used by foreign companies for doing business in China are:

- 1) representative offices,
- 2) processing and assembly operations,
- 3) technology transfer,
- 4) equity joint ventures,
- 5) co-operative joint ventures,
- 6) wholly foreign-owned enterprises,
- 7) joint stock limited companies,
- 8) holding companies and
- 9) additional operating vehicles.

1) Representative offices

Representative offices allow a foreign company to engage in certain limited business activities. A foreign company may find it useful to register a representative office in China in order to create a permanent base from which its resident personnel may conduct local sales and purchasing activities, to have a contact location in China for the convenience of its Chinese buyers and sellers and to signify its commitment to the Chinese parties with which it has business dealings.

The most common locations for a foreign company to register a representative office in China are Beijing, Shanghai or Guangzhou, although representative offices may be opened in other cities as well.

Representative offices are prohibited from engaging in 'direct business operations'. Permitted operations are: liaison for business purposes within the enterprise's scope of business, introduction of products, market research and technical exchanges.

2) Processing and assembly operations

As labour costs continue to rise in South Korea, Taiwan and Singapore, companies from Japan, Taiwan, the United States and the UK are now entering into processing and assembly transactions with Chinese companies with greater frequency.

The Chinese government has recognised the important role that processing can play in the development of the country, in terms of foreign exchange earnings, foreign equipment imports and production and management technology. As a result of the expansion in processing operations in China, national and regional legislation has been promulgated to regulate and encourage Chinese processing and assembly. Incentives include no requirement for import licenses for parts, materials and equipment used directly in the processing and assembly operation, no import taxes upon importation and no export permission required for the export of products processed with supplied materials assembled with supplied parts.

There are two types of processing and assembly operations: processing with supplied materials and processing with imported materials. Under the 'processing with supplied materials' arrangement, raw materials or semi-processed goods are shipped to a Chinese workshop or factory which then processes them and re-exports the finished products back to the foreign party. Typically, the Chinese factory receives a fee for its work, computed on a unit or lot basis. The foreign party will usually agree to supply certain production equipment, which is either sold, leased or provided to the Chinese party without charge.

¹⁰⁶ PINSENT MASONS. www.pinsentmasons.com. November 2012.

'Processing with imported materials' is a new arrangement that has emerged in the last decade-or-so. Local enterprises set up to import their own materials to manufacture goods for export. The cost of purchasing and importing materials is borne entirely by the local enterprise and is exclusively in foreign exchange.

3) Technology transfer

China's policy of co-operation with foreigners emphasises the transfer of technology to Chinese enterprises. Specific regulations stipulate the required contents and maximum term of technology transfer contracts and set out the centralised approval procedures.

They also prohibit the imposition of various restrictions by the licensor on the use of technology by the Chinese licensee and provide assurances regarding the protection of the licensor's technology in China. Transactions subject to these regulations include the transfer and licensing of patents, the right to apply for a patent, licence for patent exploitation and unpatented know-how and other forms of proprietary technology, as well as the provision of technical services.

4) Equity joint ventures

The key feature of an equity joint venture is that profits, risks and losses are shared in proportion to the parties' respective contributions to the registered share capital. Equity joint ventures must take the form of a non-share issuing 'limited liability company' incorporated and registered in China and are seen as Chinese legal persons in Chinese law. A substantial body of law governs the establishment and running of equity joint venture companies.

5) Co-operative joint ventures

Although the co-operative joint venture law (1988) does not explicitly recognise the distinction, in practice, there continues to exist two types of co-operative joint venture: the 'true co-operative joint venture' and the 'hybrid co-operative joint venture'.

The 'true co-operative joint venture' doesn't involve the creation of a legal person that is separate and distinct from the contracting parties. Each party is responsible for making its own contributions to the venture, paying its own taxes derived from the venture and bearing its own liability for risks and losses. Each party's rights, liabilities and risks are clearly stipulated in the underlying contract.

The 'hybrid co-operative joint venture' combines the characteristics of the true co-operative joint venture and the equity joint venture. A separate business entity is established and each party's liability is generally limited to their capital contributions.

6) Wholly foreign-owned enterprises

Since 2000, the law has changed regarding the establishment of wholly foreign-owned enterprises ('WFOE's') and the law no longer requires WFOEs to favour domestic suppliers when sourcing their raw materials. This, coupled with the fact that a WFOE may be easier to establish than a joint venture (as no negotiation with a Chinese party is required), means there has been a significant increase in the number of WFOEs established in China over recent years.

As with other forms of foreign investment, restricted or prohibited investment categories are outlined in the 'Catalogue for the Guidance of Foreign Investment Industries'.

7) Joint stock limited companies

China adopted its first national 'Company Law' in 1993 which provides foreign investors with an additional form of investment vehicle: the joint stock limited company (also known as a company limited by shares). The aim of the Company Law is to transform China's state-owned enterprises into limited liability companies and joint stock limited companies that are commercially viable in an emerging market economy.

The key difference between joint stock limited companies and other common forms of direct investment is the fact that joint stock limited companies are able to issue shares. Recently, a 'New Company Law' (replacing the old law) was promulgated and came into force in October 2005, (see <http://www.pinsentmasons.com/media/1186002219.pdf> and <http://www.pinsentmasons.com/media/729151186.pdf>).

8) Holding companies

In recent years, a number of foreign companies have established wholly foreign-owned or Chinese/foreign joint venture companies, the main purpose of which is to hold equity interests in subsidiary enterprises in China and to provide a range of centralised services to these subsidiaries. These are formally known as 'investment companies' and informally as 'holding companies'.

A holding company may be established as an equity joint venture or wholly foreign-owned enterprise, meaning the laws that apply to each also apply to holding companies, as do the general provisions of the Company Law.

9) Additional operational vehicles

Branch offices: In many countries, it is possible for foreign companies to establish brand offices engaging in business activities without the need to establish a foreign subsidiary. However, in China, the situation is different. The Company Law introduces the legal possibility of foreign brand offices but no specific regulations have yet been promulgated. Currently, only foreign companies in a limited number of business sectors, such as banking and insurance have been permitted to open branches in China.

Service centres: Foreign parties may enter into agreements with Chinese counterparts where the Chinese party is authorised to establish a service centre in China. These centres may provide after-sales service, maintenance and spare parts for machinery and equipment sold to end-users in China. They may not, however, market the main products they service.

Bonded zone and export processing zone enterprises: The Chinese government has set up these zones to facilitate import and export trade and encourage activities such as trading, warehousing, trade financing, transportation, packaging and export processing. Goods can be imported into and exported from these zones duty-free and are subject to very few import and export licensing restrictions.

SUMMARY TYPES OF ENTERPRISES:

Adapted from ecovis.com, November 2012

1.1 Equity Joint Ventures

A Chinese-foreign equity joint venture is a JV structured in the form of a Chinese limited liability company to which a Chinese enterprise and a foreign party each contributes its shares of capital.

- Law on Sino-Foreign Equity Joint Ventures
- One of the most comprehensive and extensive pieces of legislation relating foreign investment in China
- Advantageous to work with a Chinese partner who is familiar with the local market and who has a well established network with Chinese businesses and government authorities
- Parties jointly invest and manage the JV
- Parties share profits and risks and losses according their contributions to the registered capital
- Enterprise income tax law applicable

1.2 Cooperative Joint Ventures

- A Chinese-foreign cooperative joint venture provides a flexible structure for foreign investors.

- Can be run as a legal entity, either as a limited liability company or as an unincorporated business (corporation or partnership)
- Rules are less stringent
- Terms of the contract are negotiable, e.g. profit distribution
- Enterprise income tax law applicable

1.3 Wholly Foreign-Owned Enterprise

- A wholly foreign-owned enterprise is a Chinese limited company, wholly owned by one or more foreign investors and established entirely with foreign capital.

- Encourages from the Chinese Government for high and new technology and equipment, development of new products as well as energy preservation
- Certain industries could be restricted or prohibited
- Popular business structure
- Cost and time saving due to not having a negotiation process with a Chinese partner
- Intellectual Property Rights(IPR), trade secrets, technologies can be saved
- More flexible and streamlined management systems
- Limited liability company
- Enterprise income tax law applicable
- Suitable for production and manufacturing

1.4 Foreign-Invested Commercial Enterprise

- Relatively new structure (since 2004 after China became a member of WTO)
- Is in principle a type of WFOE
- Primary usage: for trading and distribution of goods as well as for retain business, franchising, import/export in general

- No limitation for opening retail stores in China (with some restrictions, e.g. books, periodicals, foreign investor's share is then limited to 49%)
- Same advantages as a WFOE

1.5 Foreign-Invested Holding Company

- Foreign-invested holding companies are foreign investment holding companies in China.

These may take the form of WFOE or JV.

- No engagement in production operations themselves
- Hold interests in other foreign investment enterprises and provides certain services
- Umbrella structure arrangement, which enables a foreign company to hold together its foreign investment enterprise investments in China
- To set up a holding company, foreign investors shall satisfy at least some requirements (e.g. for registered capital, subsidiaries in China)
- As a holding the scope of activities has several restrictions

Taxation: no difference to other foreign invested enterprises; dividends received by holding companies from their invested enterprise are generally exempt from enterprise income tax at the holding company level

1.6 Foreign Enterprises with or without Establishment in China

- Foreign enterprise incorporated outside China/ establishment:
 - non-resident enterprise with establishment in China
 - production or business operations
 - subject to tax to the extent for income connected with its establishment in PRC
- Foreign enterprise incorporated outside China/ no establishment:
 - non-resident enterprise with no establishment in China
 - no production or business operations
 - subject to withholding tax on income which is derived from China

Definition "establishment"

i.e., double taxation treaty between German and China:

- a place of management, operation or administration
- a farm, factory or place of extraction of natural resources
- a place where services are rendered
- a place of construction, installation, assembly, repair and exploitation etc.
- other establishments engaged in manufacturing and business operating activities

Definition "permanent establishment"

- a place of management, a branch, an office, a factory, a workshop
- a mine, an oil or gas well etc.
- a building site, construction, assembly or installation project > 6 months within any consecutive 12 months period
- rendering of services, including consultancy services > 183 days within any consecutive 12 months period

1.7 Representative Office

General

- Important structure to be present on the Chinese market
- Cannot operate as businesses in terms of manufacturing or production, or engaging on sales and marketing

- allowed to conduct other activities such as customer liaison and market research, or to provide certain services

Taxation

- Deemed as permanent establishment
- Application for tax levying method (most are based on expenses and deemed profit rate)
- Different kind of regulations for Individual Income Tax, employment regulations

1.8 Branch Offices

- Foreign companies are generally not allowed to set up an entity named branch office in China alone
- The legal entities for foreign enterprises in China are joint venture (equity & cooperative), WFOE, FICE, and representative office
- Of course, e.g. a WFOE may open branch offices throughout China on basis of this legal entity

1.9 Domestic Enterprises

- Established within the territory of the PRC
- State-owned enterprises
- Collectively-owned enterprises
- Private enterprises
- Cooperative enterprises
- Share-formulated enterprises

Annex 8. The XII Five-year Plan

*Adapted summary of the XXII Five-year Plan*¹⁰⁷:

INTRODUCTION

China's 12th Five-Year Plan (FYP), released in March 2011, attempts to restructure the Chinese economy by encouraging domestic consumption, developing the service sector, shifting to higher value-added manufacturing, conserving energy, and cleaning up the environment. Three key aspects of the 12th FYP's industrial policy are (1) a focus on scientific development, (2) government support for seven —strategic emerging industries , and (3) construction of transportation and energy infrastructure. However, some business leaders and academic experts are skeptical that the 12th FYP will solve China's structural problems, primarily due to the misalignment of central and local government priorities.

SUMMARY OF THE 12TH FIVE-YEAR PLAN

The People's Republic of China began implementing five-year plans in 1953 in order to align the economy with top policy goals and to communicate this directive throughout the government bureaucracy. Five year plans are designed to be roadmaps for regulators and provincial officials, who are responsible for their implementation. Five year plans can thus be understood as —key indicators of the directions and changes in development philosophy at the highest levels of Chinese leadership, according to Cindy Fan, a professor at the University of California, Los Angeles.

The emphasis of both the 11th and 12th FYPs has shifted from enumerating hard production targets to describing broader principles. For example, the infrastructure projects and scientific development targets laid out in the 12th FYP are directed at achieving —long-term, steady and relatively rapid economic development (*jingji changqi pingwen jiaokuai fazhan*). Both the 11th and 12th FYPs placed a high priority on improving their citizens' overall well-being through wage increases, education opportunities, and healthcare. While the 11th and 12th FYPs include clear industrial goals and policies, they have fewer numerical production targets than earlier five-year plans and rely more heavily on market mechanisms to achieve these industrial goals.

The 11th and 12th FYPs still rely upon —key indicators to help achieve broader principles. In contrast to earlier five year plans, the 11th FYP began to distinguish between —restricted (*yueshuxing*) and —expected (*yuqixing*) targets among its key indicators. This distinction continued in the 12th FYP. Restricted targets are hard targets that local officials must meet in order to progress in their careers. Expected targets are soft targets to be carried out primarily through market forces with government support.

Special Characteristics of the 12th FYP

The 12th FYP is distinctive in its heightened focus on economic restructuring, the environment and energy efficiency, and scientific development. Differences between key targets and how these key targets are categorized in the 11th and 12th FYP reflect changing government priorities. These indicators reveal that the 12th FYP places greater emphasis upon economic development versus simply growth, scientific education, and improving overall welfare. The 12th FYP also places a greater emphasis than the 11th FYP on expanding domestic demand. Underscoring this focus on domestic consumption, on March 5, 2011, Premier Wen Jiabao delivered his annual Government Work Report (organized around the key themes of the 12th FYP) and separately listed the expansion of domestic demand as a

¹⁰⁷ U.S.-CHINA ECONOMIC AND SECURITY REVIEW COMMISSION. November 2012.

key aspect of the government's work in 2011. These changes signify a critical shift in government priorities because the career progressions of local officials are tied to meeting these goals. According to Willy Shih, professor at Harvard Business School, —Meeting targets for a city, region or province, for example, is the path to advancement for officials in the Party. Those who do a superlative job get chosen for prime leadership positions. Those who fail to meet those targets get sidetracked. So the motivation is really quite powerful.

Experts like Hu Angang, director of the Center for China Studies at Tsinghua University, have hailed the 12th FYP as China's —greenest FYP ever. In his words:

Population goals aside, resource and environmental targets account for 33.3 percent of the total, up from 27.2 percent in the 11th FYP.... Also for the first time, the new plan puts forward an 'ecological security' strategy. In areas where development is limited or banned, ecological protection will be rigorously enforced and green buffer zones will be used to shield vulnerable land. There will also be funding for specific ecological restoration projects, so that our children and grandchildren will be able to enjoy a beautiful China.

The 12th FYP includes a number of new key indicators meant to help China achieve this —greening initiative. According to Qi Ye, director of The Climate Policy Initiative at Tsinghua University, —Emission reduction is emphasized [as a key indicator] for the 12th Five-Year Plan for the first time, not just energy efficiency... and also for the 12th Five-Year Plan we're looking at the consumption side management and not just production.

Among the 12th FYP's environmental goals, there is a restricted target for non-fossil fuels to reach 11.4 percent of total energy consumption by 2015, as a step towards achieving 15 percent of total energy consumption by 2020. According to Chinese government statistics, non-fossil fuels accounted for 8.3% of total energy in 2010. According to Trevor Houser, partner at the Rhodium Group, in order to meet this goal, China would have to generate between 320 and 480 gigawatts of nonfossil fuel energy over the next decade; that would be between a third and a half of new global non-fossil energy capacity.

Xu Chenggang, "The United States and China: The Next Five Years" (The Brookings Institution, Washington, DC, May 19, 2011). *I would be very surprised if Beijing was successful in meeting the kind of upper bound of this. It's just a dramatic expansion of capacity in a very short period of time, but even if they get halfway there, this will transform, fundamentally, the global market for clean energy technology... It will change its price points. It will change the relative economics of low-carbon technology versus high carbon technology, and not just in China, but other places.*

The economies of scale in alternative energy that China would need to achieve to meet this goal would have the potential to transform radically global energy markets and enable China to offer unmatched prices on alternative energy to the rest of the world.

Despite these differences, there are also many similarities between the 11th and 12th FYPs. Both attempt to address challenges that have emerged from the breakneck pace of economic growth China experienced in the 1980s and 1990s.¹⁷ According to Xu Chenggang, a professor at the University of Hong Kong, the 11th and 12th FYPs identify the same underlying structural problems in the Chinese economy: (1) export-led growth is not sustainable; (2) consumption as a share of China's gross domestic product (GDP) is too low due to the low income-to-GDP ratio, weak demand, and an unsustainably high savings rate; (3) socioeconomic inequalities are growing; and (4) manufacturing needs to be upgraded to allow China to move up the value chain in light of rising labor costs and environmental protection issues. According to Professor Xu, these problems worsened between the 11th and 12th FYPs, indicating that measures adopted by the 11th FYP either were not attained or were ineffective even when they were implemented.

Faced with this worsening situation, China has placed a key focus in the 12th FYP on the country's need to transform its economic development pattern, according to Huang Yiping, Peking University professor.

This heightened focus may have been partially fueled by the global recession and a loss of faith in America's market-oriented economic model. The 12th FYP can therefore be understood largely as an extension and acceleration of the themes of the 11th FYP. For example, although transforming the economic development model was a theme of the 11th FYP, accelerating the transformation of the economic development model was designated the primary line in the 12th FYP. Similarly, although the —scientific development concept (*kexue fazhan guan*) was unveiled in the 11th FYP, the goal of thoroughly applying the —scientific development concept is given prominence in the 12th FYP along with the —primary goal of scientific development (*yi kexue fazhan wei zhuti*).

Transformation of the economic model' is a codeword for the increasing emphasis China has given domestic demand as a driver of economic growth since the onset of the global financial crisis in 2008. Premier Wen reiterated China's current policy slogan calling for 'accelerated economic growth driven by the coordination of consumption, investment, and exports.'

The —scientific development concept-, a slogan associated with CPC Chief Hu Jintao, emphasizes balanced, sustainable development tempered by concern for social justice, and for raising standards of living. Scientific development is, in essence, a euphemism that Chinese leaders use for economic growth that takes into consideration the welfare of disadvantaged people and regions as well as environmental concerns.

The government hopes to increase the total of urban households living in partially government state-subsidized housing from 11 percent in 2007 to 20 percent by 2015. Of the ten million units, two million will be discounted, market-available units; two million will be low-priced, rent-to-buy units; 1.6 million will be —low-cost rental housing; and four million will be new or renovated units in —shanty areas. Jamil Anderlini, —Housing subsidies at heart of Beijing's _new deal', *Financial Times*, May 31, 2011.

A number of key goals in the 12th FYP are directed at moving the economy away from export-led growth, raising domestic consumption, and narrowing income inequality. These goals include:

- 7 percent annual GDP growth;
- 4 percent expansion of the service sector as a percentage of GDP by 2015;
- an increase in annual urban disposable income to >26,810 renminbi (RMB) (US\$4,143) and annual rural disposable income to >8,310 RMB (US\$1,284) by 2015. For the first time, this increase would equal or exceed projected GDP growth for the same period;
- an expansion of urban insurance coverage by 100 million people by 2015; and
- construction of 36 million new housing units to increase the availability of affordable urban housing.²³ The central government has already pledged to build 10 million units of government-subsidized housing in 2011, allocating 103 billion RMB from the central government budget, 400-500 billion RMB from the local governments, and expecting commercial developers to contribute 500-900 billion RMB for the 1.3 trillion RMB project.
- The 12th FYP includes a —well-being target for the first time, with a goal of increasing the average life expectancy by a year over the next five years.

Some of these goals, such as building affordable housing for poor urban residents, are expected to be met. The availability of affordable housing should increase disposable income for lower-income citizens and promote broader consumer spending. According to a report by the auditing firm KPMG China, the Chinese government may also raise minimum wages substantially (by no less than 13 percent on average) in the next five years and hold inflation at or below 4 percent per year.

For example, following the release of the national 11th FYP in 2006, the Beijing Municipality released its own 11th FYP that incorporated national 11th FYP objectives such as energy efficiency and innovation.—Beijing’s 11th Five-Year Plan: Outline (translated by the Beijing Association of Enterprises with Foreign Investment), March 29, 2006. For an example of a longer-term goal, the State Council announced targets on November 26, 2009, for energy reduction, carbon reduction, and nonfossil fuel energy by 2020. The 2015 targets laid out in the 12th Five-Year Plan are only an intermediate step in achieving these goals. For details on these 2020 targets, see Xinhua, —China announces targets on carbon emission cuts, November 26, 2009.

The 12th FYP will also promote scientific development to upgrade China’s manufacturing sector, boost local research and development (R&D), and increase the global competitiveness of Chinese firms. Key indicators include raising R&D spending from 1.75 percent to 2.2 percent of GDP (by contrast, the United States spent 2.7 percent of GDP on R&D in 2007, ranking eighth globally); increasing the number of patents per 10,000 people; and boosting educational attainment, all under the rubric of —scientific education.

PROSPECTS FOR IMPLEMENTATION OF THE 12TH FYP

Following the release of the national FYP, provincial and municipality governments and industry regulators draft similar outlines and special plans. In practice, five-year plans are only a link in policy documents promulgated by the central government, in between longer- and shorter-term documents, and are constantly reviewed and revised over the course of five years. These outlines and special plans allow for more concrete implementation of the objectives in the national FYP, working implementation down to the industry and issue level. These outlines and special plans are followed by implementation measures (such as policy documents) by the departments named in the special plans.

In addition to the five-year goals, China has set annual targets to implement the plan through yearly government work reports. The following targets were set for 2011 (the first year of the 12th FYP) in Premier Wen Jiabao’s Report on the Work of the Government, adopted by the National People’s Congress on March 14, 2011:

- 8 percent GDP growth;
- 42.3 billion RMB (US\$6.53 billion) for Employment Assistance and Job Creation;
- 16 percent increase in broad money supply (M2);
- capping Consumer Price Index growth at 4 percent to stabilize prices; and
- expanding use of the RMB in crossborder trade and investment and pressing ahead with making the RMB convertible under capital accounts.

According to Chinese government figures, the 11th FYP met or exceeded seven out of eight restricted goals and 11 out of 14 expected goals. The only restricted goal the 11th FYP failed to meet was reducing energy intensity per unit of GDP, despite what Derek Scissors, research fellow at The Heritage Foundation, calls —belated discoveries of additional GDP and a dubiously sharp shift in energy consumption and what APCO Worldwide describes as —forced electricity brown-outs in several cities in late 2010 to meet those targets. Since the energy intensity reduction target was —around 20 percent, and energy intensity reduction

reached 19.1 percent, China officially claims that it met this indicator as well, enabling it to hit all of its restricted targets. According to APCO Worldwide, expected goals do not carry as much weight as restricted goals because local officials are highly incentivized to meet restricted goals since these are —closely tied to the official’s career progression within the Community Party of China (CPC). The same is not true of expected goals.

The three expected goals that were not reached in the 11th FYP were (1) service sector as a percentage of GDP, (2) service sector as a percentage of employment, and (3) R&D as a percentage of GDP.

Despite meeting most of its targets, the 11th FYP was nevertheless unsuccessful because of its failure to address underlying structural problems. Even its overwhelming success in far exceeding its projected GDP goals can be seen as a failure, since the 11th FYP meant to rein in growth, and instead the GDP growth objectives for 2010 had already been met by 2007. As Derek Scissors sums up the outcome of the 11th FYP:

The [11th] FYP reflected Chinese President Hu Jintao’s stated goal of greater income balance. On official figures, however, income inequality appeared to worsen through 2009, and any gains in 2010 were insufficient to recover lost ground. In other words, both specific targets and grand goals of FYPs should be taken with many grains of salt.

To better address the range of targets beyond GDP growth, the central government has begun to provide additional incentives to local officials to achieve other five-year plan goals. For example, the central government began to send out teams of officials to the provinces at the end of the 11th FYP to ensure that energy intensity targets were met and adopted other metrics (e.g., setting up the —China’s Top-1000 Energy-Consuming Enterprises Program) to make local officials prioritize reducing energy intensity. The government appears prepared to unveil similar mechanisms to promote the completion of 12th FYP goals, at least as related to environmental goals. According to Qi Ye, —[T]he 11th Five-Year Plan was the five years when we saw considerable change in the mix of the incentives, the structure of the incentives. Take the environment, for example... for the pollution reduction, not really in this energy saving, but for the pollution reduction part, that really changed quite considerably.

Nevertheless, there are reasons to suspect that the 12th FYP will not be any more successful than the 11th FYP, even if it does manage to meet most of its expected and restricted key indicators. Although the 12th FYP calls for economic restructuring and a preference for quality growth over growth at any cost, it is unclear whether the provinces really understand or appreciate this. For example, despite the 12th FYP’s call for a reduction in projected GDP growth, —every province and major city have growth goals that exceed the lower seven percent target. Shanghai’s 12th FYP posits eight percent growth, and several provinces already have announced growth targets of 13 percent or higher. Therefore, a critical disconnect remains between central government planners and the local governments responsible for implementing the 12th FYP. Moreover, the political transition underway in Beijing may make it more difficult to make major changes to the incentive structure than it was for the 11th FYP.

BREAKDOWN OF THE 12TH FYP INDUSTRIAL POLICY

The 12th FYP establishes Chinese industrial policy for the next five years. The 12th FYP seeks to make scientific development a primary objective, strengthen strategic emerging industries, and build up infrastructure. These areas of focus provide a layout for future, large-scale government investments and indicate which industries will receive preferential government support.

Scientific Development as a Primary Objective

Scientific development and a move up the value chain sits at the heart of the 12th FYP. Jia Qinglin, chairman of the Chinese People's Political Consultative Conference National Committee, notes that —the success of the 12th FYP (2011-2015) rests on science and technology and indigenous innovation capacity. Although the concept of —indigenous innovation and a focus on science were already present in the 11th FYP, the 12th FYP's increased focus upon scientific development can be seen in the four key indicators that are now categorized as —Scientific Education : (1) R&D as a percentage of GDP; (2) patents per 10,000 people; (3) rate of nine-year compulsory education enrollment; and (4) rate of high school enrollment.

1) R&D as a percentage of GDP was categorized as an economic structure indicator in the 11th FYP and was one of three nonrestrictive indicators that China failed to meet in the 11th FYP. R&D in China accounted for 1.75 percent of GDP in 2010, far below the government's expected goal of 2 percent for 2010.

2) A patent per 10,000 people is a key goal that was not present in the 11th FYP. This reflects China's focus on Chinese companies obtaining their own intellectual property so that they can create their own products rather than simply assembling products for multinational corporations. The anticipated 3.3 patents per 10,000 people in 2015 would nearly double the number approved in 2010.

3) and 4) The two new educational indicators replaced —average educational attainment in the 11th FYP. These new indicators reveal the government's emphasis on providing more sophisticated, higher-level education with an emphasis on scientific achievement.

Supporting Strategic Emerging Industries

The 12th FYP designates seven strategic emerging industries (SEI) as the drivers for China's future economic development from low-end manufacturing to higher-value industries and creating sustainable growth. These industries include clean energy technology; next-generation information technology (IT); biotechnology; high-end equipment manufacturing; alternative energy; new materials; and clean energy vehicles. Four of these industries (biotechnology, high-end equipment manufacturing, new materials, and next-generation IT) were previously identified as target industries in the 11th FYP.

As a reflection of China's broader development goals, three of these industries align with sustainable growth (alternative energy, clean energy vehicles, and clean energy technology), and four industries align with moving up the value chain (biotechnology, new materials, next-generation IT, and high-end equipment manufacturing). The central government established a clear goal to grow these seven industries from 5 percent of GDP in 2010 to 8 percent by 2015 and 15 percent by 2020. According to a report by the consulting firm APCO Worldwide, the central and local government and private sector are expected to spend approximately 14 trillion RMB (US\$2.16 trillion) over the next five years to achieve this target. While the 12th FYP does not specify subsidies, standard subsidies like preferred financing, tax breaks, subsidized electricity and utility fees, free or subsidized land, etc. may be made available to SEIs by local governments. According to the Ministry of Finance Chief of Staff Hu Jinglin in December 2010, the Ministry of Finance will use finance and taxation policy to support the development of the SEIs, including providing multiple channels for financing. The Ministry of Finance will also encourage its regional offices to develop local policies and will urge local governments to take a share in SEIs and develop investment funds. This commitment was reiterated in the National Development and Reform Commission's (NDRC) draft, —Major Tasks and Measures for Economic and Social Development in 2011, released in March 2011.

Smart grid technology focuses on increasing the efficiency of utility companies through grid automation, communications infrastructure, IT systems and hardware, systems integration, smart meters, and home area network equipment. *PKWeb UK*, —Ten Countries will account for 80% of global smart grid investment by 2030, February 14, 2011.

We will quickly formulate and implement a development plan and supporting policies for strategic emerging industries, set up a special fund for promoting their development, expand the scale of venture capital investment in them, formulate a guiding list for developing them, and work out industry standards for major emerging industries.

Preferential government policies have previously been helpful in establishing —national champions in industries such as telecommunications, steel, and railway.⁵¹ However, there are claims that some of this past success has been predicated upon forced technology transfer and technology theft.

Most of these seven strategic industries are expecting high levels of growth in the next five to ten years. For example, smart grid technology, which focuses on increasing the efficiency of current utility companies, has enormous growth potential, with utilities companies worldwide expected to invest \$375 billion by 2030.⁵³ According to Catherine Viola, a senior analyst at Innovation Observatory, —China’s plans for wide-scale smart meter deployment will see it install over 360 million smart meters by 2030... We expect China’s overall spending on smart grid development to reach US\$99 billion by that date – more than a quarter of the global total. This high demand will provide a strong, growing market for the emergence of Chinese enterprises.

China has been the largest solar cell producer since 2008. In 2009, four of the ten largest photovoltaic cells and modules producers in the world were Chinese — Suntech Power, Yingli, JA Solar, and Trina Solar.

Class 2 highways are double-lane highways that can handle an average daily transportation volume of 5,000-15,000 vehicles. Ministry of Communications of the People’s Republic of China, —Technical Standard of Highway. Chinese government support for at least one of these industries has been successful in the past. During the 11th FYP, China designated clean energy technology (solar, wind, bio, and nuclear energy) for government support, spending approximately 2 trillion RMB (US\$309 billion) on energy efficiency and environmental protection measures. Currently, Chinese companies have emerged as global leaders in wind⁵⁶ and solar power. More specifically, Chinese solar manufacturing companies have become the world’s largest producer of photovoltaic solar cells and modules and control approximately 17 percent of the global market for the production of silicon. The 12th FYP expands upon these developments to support more resource usage technologies such as the smart grid. The Chinese government also appears set to take measures to bolster demand for its SEI products. For example, China plans to invest US\$100 million to build power projects using Chinese solar panels in 40 African nations. As with clean energy, over the next five years, the Chinese central and local governments are expected to devote significant resources to all seven SEIs, creating both potential opportunities and challenges for foreign firms.

Building Infrastructure

The 12th FYP devotes significant resources to expanding China’s transportation and energy infrastructure. In regard to transportation, China will seek to relieve traffic congestion by expanding its express railway network, constructing larger capacity roads and highways, and expanding current port capabilities. In addition, the improved infrastructure will promote

interregional trade and facilitate the growth of underdeveloped inland regions. The 12th FYP specifies:

- a 70 percent or a higher percentage of Class 2 standards or above for its national highways;
- 83,000 kilometers (km) worth of available mileage on its National Expressway Network, with seven radial lines, nine longitudinal, and 18 transverse lines;
- an addition of 42 national integrated traffic hubs; and
- 440 10,000-ton and above deep berths to expand the capacities of its current ports;

The new energy infrastructure will increase China's alternative energy capabilities, improve current electrical power capabilities, and expand access to oil and natural gas in an effort to answer the growing demands of its economy. This construction will also meet one of the central goals of the 12th FYP—establish a resource-conserving environmentally friendly society... deepen the thorough application of the basic national policy of conserving resources and protecting the environment... take the path of sustainable development. To achieve this goal, the 12th FYP calls for:

- a 120 million kilowatt (kW) increase in hydropower capacity;
- a 70 million kW increase in offshore, large wind power bases capacity;
- a 40 million kW increase in nuclear power capacity, though Japan's recent nuclear crisis has led to a temporary suspension of new construction;
- a 5 million kW increase in solar energy installed capacity;
- a 200,000 km increase in power transmission lines of 330 kilovolts or higher; and
- a 150,000 km increase in the total length of its oil and gas transmission pipelines.

CRITICAL ASSESSMENT

If the 12th FYP is fully implemented, some experts believe that —by 2015, China will be a fairer, greener society. Rising incomes will have boosted consumption and industry will have clambered up the technology ladder. Economist Stephen Roach claims that the 12th FYP *is likely to go down in history as one of China's boldest strategic initiatives. In essence, it will change the character of China's economic model -- moving from the export- and investment-led structure of the past 30 years toward a pattern of growth that is driven increasingly by Chinese consumers. This shift will have profound implications for China, the rest of Asia, and the broader global economy.*

However, many scholars are doubtful that China will achieve the fundamental changes to the environment, scientific development and the economy proposed in the 12th FYP. Some analysts are skeptical that the plan will prove to really make China a greener place. According to the environmental activist group Greenpeace, the 11th FYP was successful in leading to —the closure of thousands of inefficient power plants among the numerous energy saving and emission reduction measures that were implemented. Greenpeace therefore sees the 12th FYP's call for a 16 percent reduction in energy intensity a step back from the 20 percent reduction goal in the 11th FYP and believes that the new target —is not high enough to encourage local governments and industry to change their growth models.

According to Mr. Houser, the success or failure of the 12th FYP's energy efficiency goals can be tied to its more general mandate to restructure the economy. If China can develop its service sector and reduce its reliance on heavy industry, then a 16 percent energy reduction will be easy to achieve. However, China's more ambitious goal of having nonfossil fuels account for 11.4 percent of all energy used by 2015 will be much more difficult to achieve.

Approximately half of all Chinese patents filed in 2009 were utility models, which are less-rigorous, more-affordable forms of patents that provide 10 years of protection (versus 20

years for invention patents). The use of utility model patents in China has grown at a rate of 18 percent per annum since 2001.

The 12th FYP states that scientific development should be a primary support for accelerating the transformation of the economy. However, some critics doubt that increasing the number of patents in China will boost domestic innovation because of the large number of minimally innovative —utility model patents applied for within China. These —utility model patents are alterations or upgrades to existing technology that may be registered without an inspection. While the 12th FYP calls for a large increase in the number of these patents, David C. Schmittlein, dean of the Sloan School of Management at the Massachusetts Institute of Technology, has stated that China's focus should be on quality innovation over large numbers of low-value patents.

As for economic restructuring more generally, the 12th FYP does not indicate how the economy will become less reliant on capital spending, have more liberalized financial markets, or fundamentally shift China's global trade balance. According to Stephen Green, regional head of research at the Standard Chartered Bank in Shanghai, although the 12th FYP claims that it wants growth to slow and be more equitable, —[t]here's absolutely no sign that the percentage of investment in GDP is slowing. And there are no signs of liberalization of the service sector to allow the private sector to take a bigger share of the economy. Moreover, Dr. Green does not believe that the plan will enable labor to acquire a significantly larger share of GDP, which would, in turn, enable the sort of boost in consumer spending called for by the 12th FYP.

According to Eswar Prasad, professor at Cornell University, one reason that the FYP is a bit —skimpy on details related to major structural changes--especially related to shifting to a consumption-driven economy and opening up financial systems--is the inherent tension between China's short- and long-term objectives. For example, while significantly raising wages would certainly boost domestic consumption, it would also drive up inflation. Moreover, structural change would not be to everyone's benefit. As Dr. Prasad stated, —...the present system works very well for a lot of people in China. For the politically well-connected state-owned enterprise bosses, for many of the bank chairmen, this is actually a very good system because it keeps profits flowing into the state enterprises, into the banks... Perhaps as a result of these tensions, Steve Dickinson, a lawyer with Harris & Moure, has noted in a well-regarded legal blog that rather than promoting real structural transformation, the plan continues to put China on an —infrastructure/industry/export led growth model... The focus of the entire project is [still] to transform China into a modern industrial powerhouse on the model of Japan/Germany/Korea.

Key Indicators in China's 11th and 12th Five-Year Plans

N/A indicates that this was not a designated key indicator in the relevant five-year plan.					
Economic Targets					
Target	11th FYP (2010 Target)	11th FYP Category	2010 (Actual)	12th FYP (by 2015)	12th FYP Category
Average GDP Growth	7.5% (E)	Economic Growth	11.2%	7%ii (E)	Economic Development
Average GDP Growth Per Person	6.6% (E)	Economic Growth	10.6%	N/A12	N/A
Service Sector as % of GDP	43.3% (E)	Economic Structure	43%	47% (E)	Economic Development
Service Sector as % of Total Employment	35.3% (E)	Economic Structure	34.8%	N/A	N/A
Urbanization (%)	47% (E)	Economic Structure	47.5%	51.5% (E)	Economic Development
R&D as % of GDP	2% (E)	Economic Structure	1.75%	2.2% (E)	Scientific Education
Patents per 10,000 People	N/A	N/A	1.7	3.3 (E)	Scientific Education
Strategic Industry as a % of GDPiii	N/A	N/A	N/A	+8.0%	N/A
Population Targets					
Target	11th FYP (2010 Target)	11th FYP Category	2010 (Actual)	12th FYP (by 2015)	12th FYP Category
Population Cap	1.36 billion (R)	Population, Resources, and the Environment (PRE)	1.341 billion	1.39 billion (R)	People's Life
Life Expectancy	N/A	N/A	73.5	74.5 (E)	People's Life
Average Educational Attainment	9 Years (E) (+0.5 Years)	Public Services and People's Life (PSPL)	9 Years	N/A	N/A
Rate of Nine-Year Compulsory Education Enrollment	N/A	N/A	89.7%	93% (R)	Scientific Education
Rate of High School Enrollment	N/A	N/A	82.5%	87% (E)	Scientific Education
New urban jobs created (5-year total)	45 million (E)	PSPL	57.71 million	45 million (E)	People's Life
Transfer of rural labor (5-year total)	45 million (E)	PSPL	45 million	N/A	N/A

Major Objectives in China's 11th and 12th Five-Year Plans	
11th FYP	12th FYP
Holistically and thoroughly implement the Scientific Development Concept (<i>quanmian guanche luoshi kexue fazhan guan</i>)	Deepen the thorough application of the Scientific Development Concept (<i>shenru guanche luoshi kexue fazhan guan</i>)
Steady and relatively rapid economic development (<i>jingji pingwen jiaokuai fazhan</i>)	Long-term steady and relatively rapid economic development (<i>jingji changqi pingwen jiaokuai fazhan</i>)
Primary line – Adjust the economic structure (<i>tiaozheng jingji jiegou</i>)	Primary line – Accelerate the transformation of our economic development model (<i>jiaokuai zhuanbian fazhan fangshi</i>)
Basic anchor point (<i>jiben lizudian</i>) – Expand domestic demand, especially consumer demand (<i>kuoda guonei xuqiu tiebie shi xiaofei xuqiu</i>)	Primary objective – scientific development (<i>yi kexue fazhan wei zhuti</i>), as a primary support for accelerating the transformation of the economy, strengthen indigenous innovation (<i>zengqiang zizhu chuangxin nengli</i>)
Basic national policy (<i>jiben guoce</i>)/ Point of Strength (<i>zhuolidian</i>) - Conserve and make efficient use of resources, transform the economy to achieve sustainable development	Main direction of the offensive (<i>zhugong fangxiang</i>) – Strategically adjust the economic structure, establish a long-term mechanism of expanding domestic demand (<i>goujian kuada neixu changxiao jizhi</i>), develop the Strategic Emerging Industries, accelerate the development of the service sector, coordinate urban and rural development, and promote urbanization.
National strategy (<i>guojia zhanlue</i>) – Strengthen indigenous innovation (<i>zengqiang zizhu chuangxin nengli</i>)	Basic starting point (<i>genben chufadian</i>) - Protect and improve the lives of the people (<i>baozhang he gaishan minsheng</i>), common prosperity (<i>gongtong fuyu</i>)
Coordinate urban and rural development	Major Point of Strength (<i>zhuyao zhuolidian</i>) – Establish a resource-conserving, environmentally friendly society, deepen the thorough application of the basic national policy of conserving resources and protecting the environment, take the path of sustainable development.
Source of Power (<i>dongli</i>) Continuously deepen reform and opening up (<i>buduan shenhua gaigekaifang</i>)	Mighty Source of Power (<i>qiangda dongli</i>) - Deepen reform and opening up (<i>shenhua gaigekaifang</i>)
Strengthen the establishment of harmonious society (<i>hexie shehui</i>), put people first (<i>yiren weiben</i>), increase employment by all means available, focus upon social justice.	Harmonious and stable society (<i>shehui hexie wending</i>), protect and improve the lives of the people
Encourage cultural production to increase China's –soft power (<i>tisheng guojia ruan shili</i>)	

The 12th FYP's Seven SEIs and 37 Projects for Sub-industries

Clean Energy Technology

- High-efficiency and energy saving
- Advanced Environmental Protection
- Recycling Usage
- Reusing Waste Products

Next-Generation IT

- Next-generation mobile communications
- Next-generation core Internet equipment
- Smart devices
- Internet of Things
- Covergence of telecom/cable TV/Interentnetworks
- Cloud Computing
- New Displays
- Integrated Circuits
- High-end Software
- High-end Servers
- Digitization of culture and creative industires

Biotechnology

- Bio-pharmaceuticals
- Innovative pharmaceuticals
- Biomedicine
- Bioagriculture
- Biomanufacturing
- Marine biology

High-end Equipment Manufacturing

- Aerospace and space industires
- Rail and transportation
- Ocean engineering
- Smart assembly

Alternative Energy

- Nuclear power
- Solar power
- Wind power
- Biomass power
- Smart power grids

New Materials

- New function materials
- Advanced structural materials
- High performance composites
- Generic base materials

Clean Energy vehicles

- Electric hybrid cars
- Pure electric cars
- Fuel cell cars

Annex 9. List of acronyms

ACCIO10	Competitiveness for Catalonia. Government of Catalonia
ADB	Asian Development Bank
AECID	Spanish Agency for International Cooperation for Development
BCG	Boston Consulting Group
BRIC Countries	Brazil, Russia, India and China
B2B	Business to Business
B2C	Business to Consumer
CCP	Chinese Communist Party
CCOIC	China Chamber of International Commerce
CCPIT	China Council for the Promotion of international Trade
CRE	Regional Statistics of Spain (Spanish Institute of Statistics).
C2C	Consumer to Consumer
DIRCE	Directorio Central de Empresas. (Central Directory of Businesses that belongs to the Spanish Institute of Statistics).
DOTS	Direction of Trade Statistics (IMF)
ECLAC / CEPAL	Economic Commission for Latin America and the Caribbean Comisión Económica para América Latina y el Caribe
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HED	EU-China High-Level Economic and Trade Dialogue
HK	Hong Kong
ICEX	Spanish Institute for Foreign Trade
JV	Joint Venture
IFS	International Financial Statistics (IMF)
IMF	International Monetary Fund
INE	Spanish Institute of Statistics
IPR	Intellectual Property Rights
MOF	China's Ministry of Finance
MOFCOM	China's Ministry of Commerce
NGOs	Non-governmental Organizations
NPC	National People's Congress
OECD	Organization for Economic Co-Operation and Development

PRC	People's Republic of China
RMB	Renminbi
RO	Representation Office
SEZ	Special Economic Zones
SMEs	Small and Medium-Sized Enterprises
UAO CEU	Universitat Abat Oliba (University Studies Centre)
UN	United Nations
USCBC	United States-China Business Council
WB	World Bank
WEO	World Economic Outlook Database (IMF)
WFOE	Wholly Foreign-Owned Enterprise
WTO	World Trade Organization

