US-China Business Council

# 2017 Member Survey

# Two main takeaways

## 1. MARKET IMPROVEMENT (IF YOU HAVE ACCESS)

- Improved sales performance versus a year ago: 75 percent expect revenue to increase this year (versus 62 percent last year); 9 percent expect revenue to decline (down from 17 percent).
- Sales growth is slowing overall in line with China's rate of GDP growth slowing, but 40 percent of respondents still saw double-digit sales growth last year.
- Sixty-four percent of companies saw improved profitability of their China operations in the last year. Profit margins in China versus operations in the rest of the world are a mixed bag – one-third report their China operations do better than their operations in other markets, one-third worse, one-third the same.
- Biggest restraints on profitability? Domestic competition, for the sixth year in a row. No. 2 is government policies/regulation, No. 3 is Rising costs.
- Thirty-six percent have increased market share versus three years ago; 20 percent have lost market share.
- Rising costs are a concern for nearly 90 percent of companies. Clear cost driver of most concern: human resources.
- Forty-eight percent of companies are expanding resources in China; only 8 percent are contracting. But investment is focused on expanding current facilities, commercial footprint, and headcount, rather than investing in new facilities.
- Important context: 68 percent say growth prospects in China are better than in other markets around the world; only 9 percent said they are worse.
- The key question: Can you access the market?

## 2. POLICY ENVIRONMENT UNCERTAIN, REGULATORY BARRIERS UNCHANGED

- Forty percent of companies are less optimistic about the business climate than three years ago, only 11 percent are more optimistic.
- Main reason: China's policy environment. 57 percent have seen no impact from economic reforms announced 4 years ago.
- Tech transfer to gain market access is an acute issue for those who face it; nearly 20 percent have been asked to transfer technology during the past three years. JV requirements and government approvals provide leverage to China.
- Ninety-four percent remain concerned about IP protection.
- Eighty-two percent are concerned about the impact of China's cyber and data regulations on business operations.
- A high-standard bilateral investment treaty (BIT) with China would positively address each of the top 5 challenges.

# Top 10 challenges

1. Competition with Chinese companies
2. Licenses & approvals
3. Investment barriers
4. Uneven enforcement
5. IPR enforcement
6. Cybersecurity
7. Cost increases
8. US-China relations
9. Data flow barriers
10. Capital controls

# Competition with Chinese companies

The challenges of competition with Chinese companies has been a top concern for USCBC members for many years.

Competition has always been a top 10 issue, and ranked No. 1 in 2004, 2010, and every year since 2014. Issues related to competition – licenses and approvals, investment restrictions, and uneven enforcement – also consistently rank in the top 10.

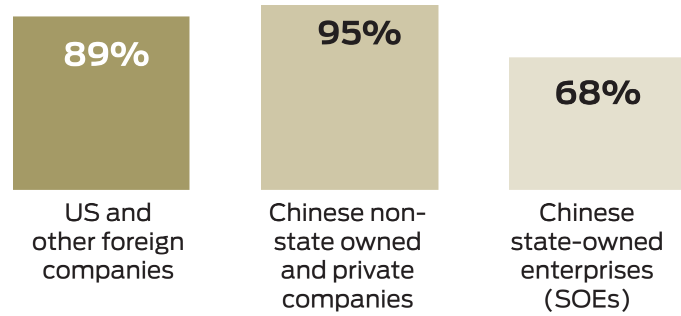
Competition concerns are not unique to having state-owned enterprise (SOE) rivals. Most companies are competing with private, non-state owned companies in China (and other foreign companies), in addition to SOEs.

SOEs are receiving benefits that foreign companies cannot, but half of companies report that their privately-owned Chinese competitors also are receiving benefits they cannot.

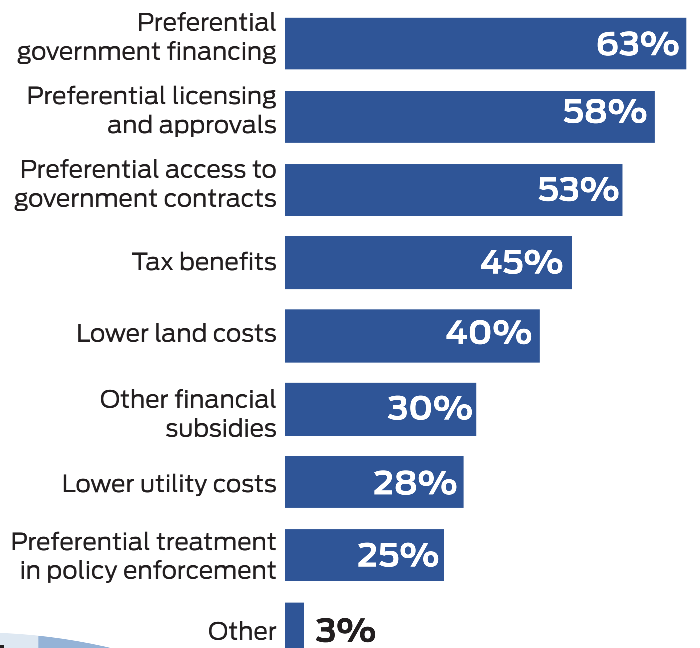
Increasing competition has led some companies to reduce or stop planned investments in China. Competition from domestic companies is the primary restraint on increased profitability in China, followed closely by Chinese government policies and regulations.

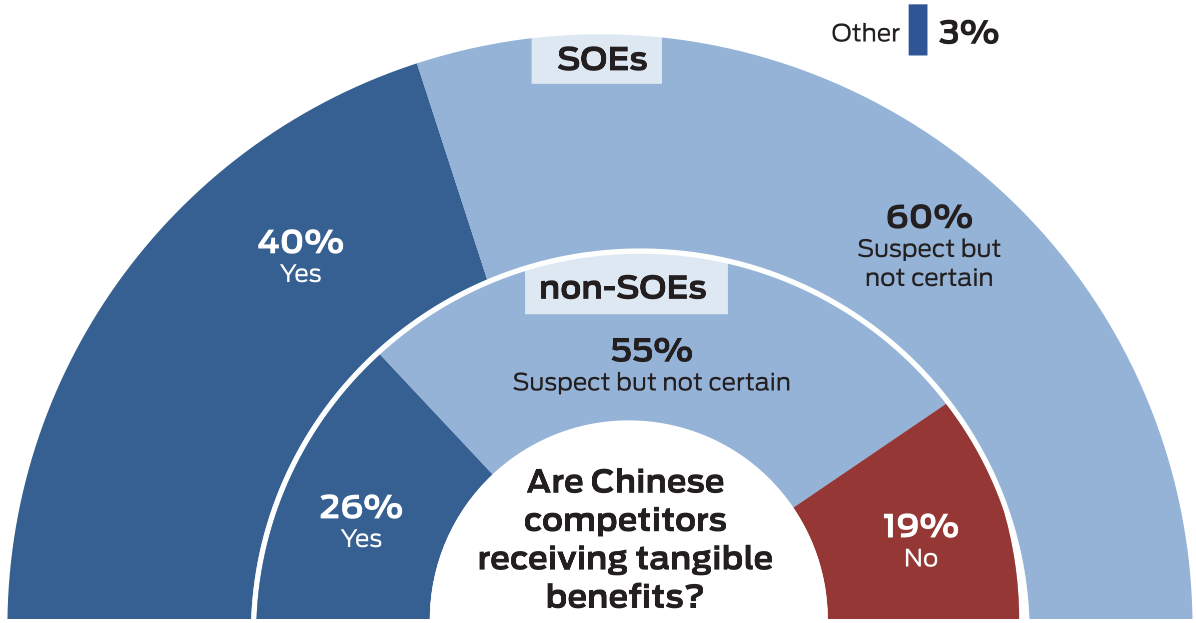
USCBC members seek a level playing field with all Chinese companies, not just SOEs.

### Who are your competitors in China?




### Types of benefits SOE competitors receive



# Operating Environment

Operating performance has improved versus a year ago as consumer spending has remained strong and a government "mini-stimulus" has helped industries and commodities. Seventy-five percent of companies are expecting a revenue increase this year, versus 62 percent in 2016. Only 9 percent expect revenue to decline, versus 17 percent in 2016.

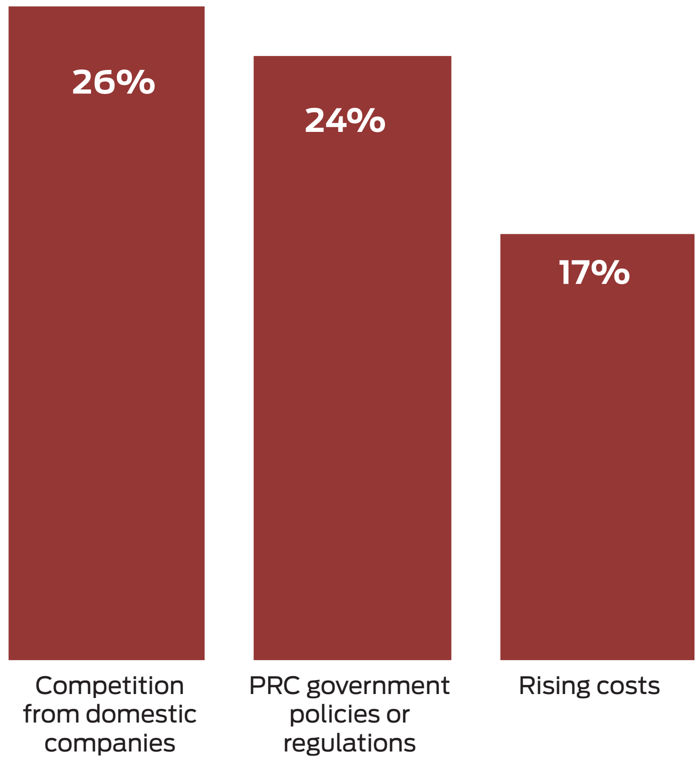
Thirty-six percent of respondents have increased market share versus three years ago; 20 percent have lost market share.

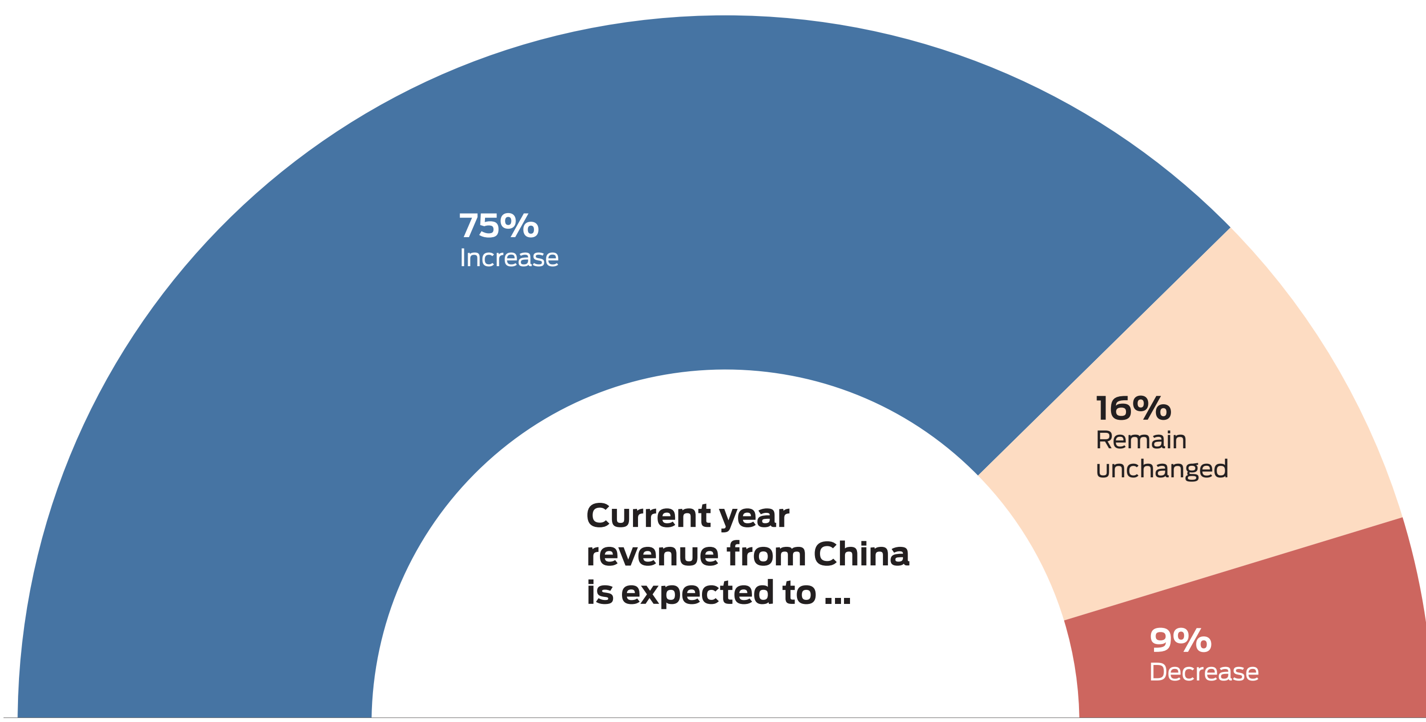
Ninety-five percent of companies are profitable in China (consistent with prior years), but profit margins in China versus operations in the rest of the world are a mixed bag -- one-third report their China operations do better than their operations in other markets, one-third worse, one-third the same.

What were the biggest restraints on profitability?

- Domestic competition, for the sixth year in a row
- Government policies/regulation
- Rising costs

**Biggest restraints on profitability**



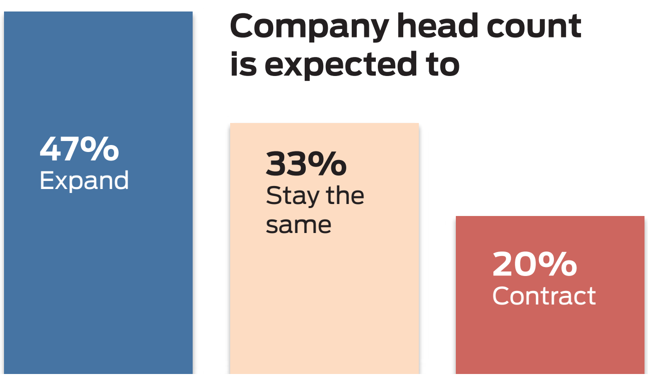
# Rising costs

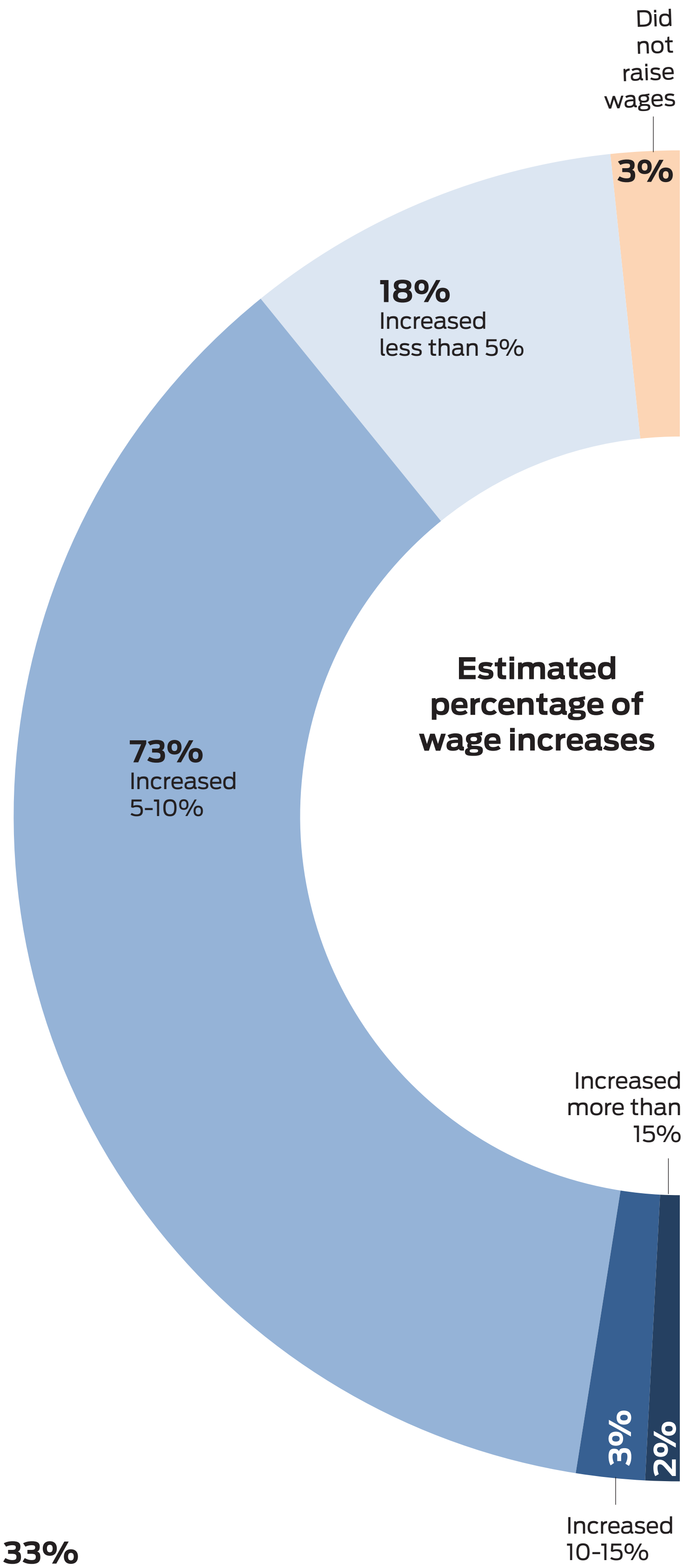
Rising costs were a concern in 2017 for nearly 90 percent of companies. The clear cost driver of most concern was human resources.

Wages continue to increase significantly year to year:

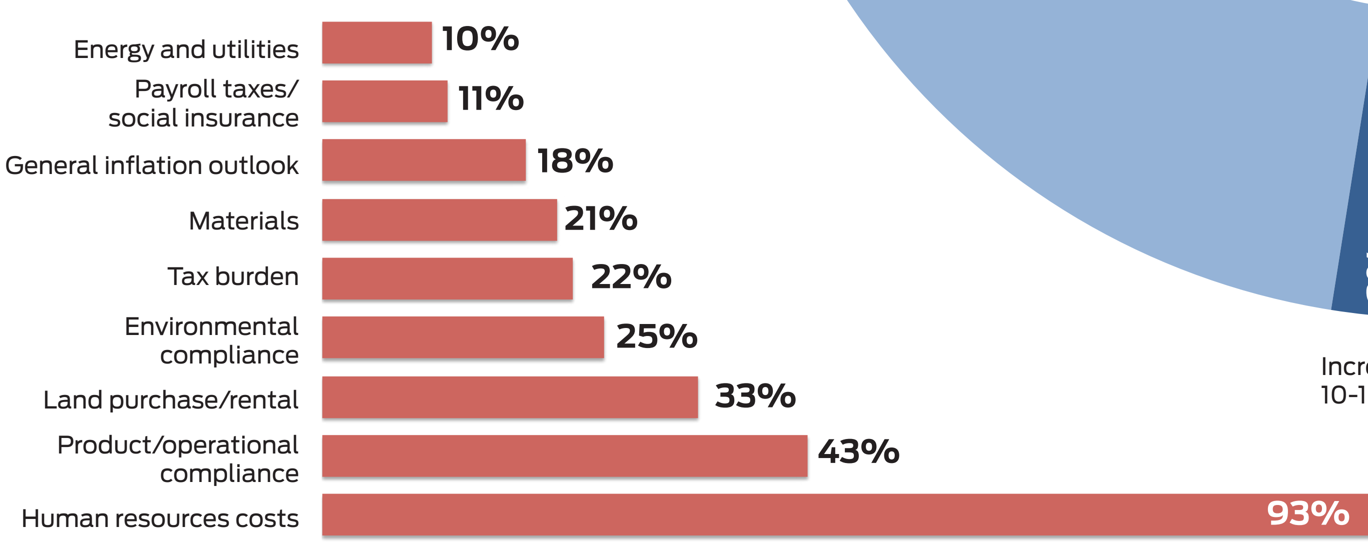
- Seventy-three percent raised wages between 5 and 10 percent in 2016, and another 5 percent raised wages over 10 percent last year.
- Companies have reported similar increases since 2012, meaning that most have increased wages by at least 5 percent every year for at least the last 6 years – a cumulative increase in labor costs of at least 34 percent over that period.

Despite these regularly increasing costs, about half of companies plan to expand head count in China in the next year – a reflection of the growing market.




## Top cost concerns



# Investment

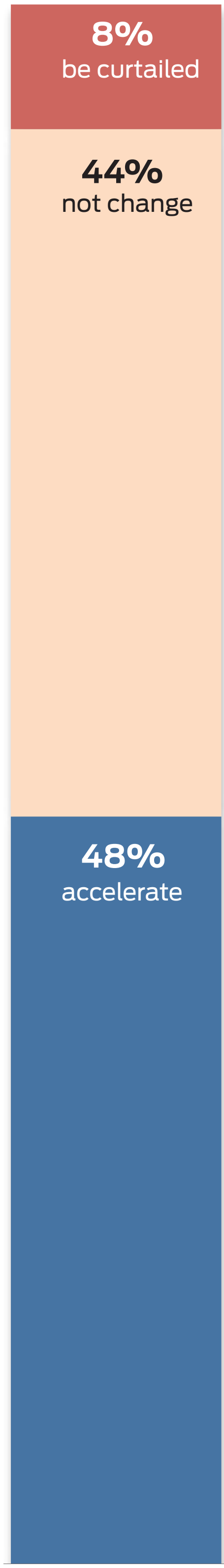
Most companies report that they will maintain or accelerate their resource commitment to the market in the coming year. Few companies reduced or stopped an investment in China in the last year.

Those accelerating their resource commitment plan to expand their commercial footprint, increase headcount, expand existing operations or introduce new products or services. What they're not doing: investing in new facilities in China.

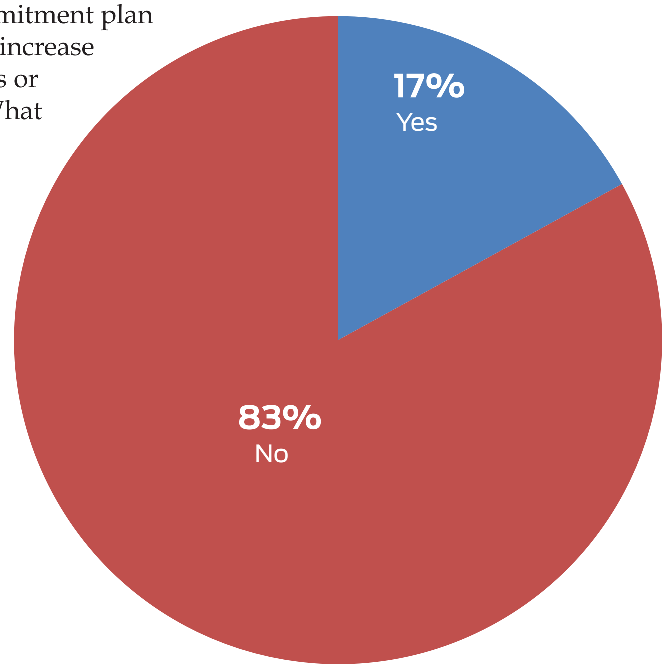
Companies that did reduce their investments in China had a variety of reasons for doing so:

- Global reductions in capital investment
- Increasing market access restrictions
- Better business prospects in other markets
- Competition from domestic companies

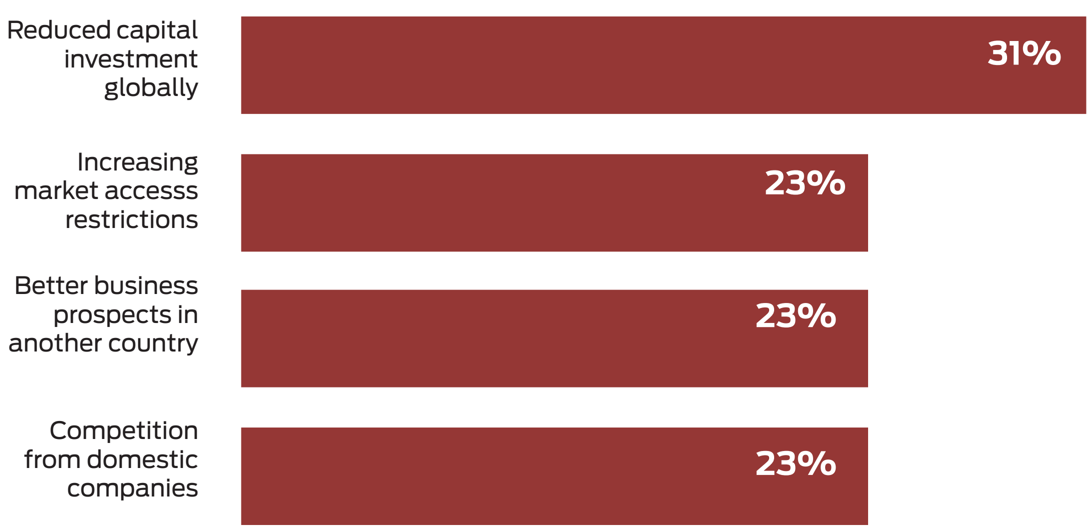
**Resource commitment for the next 12 months will**



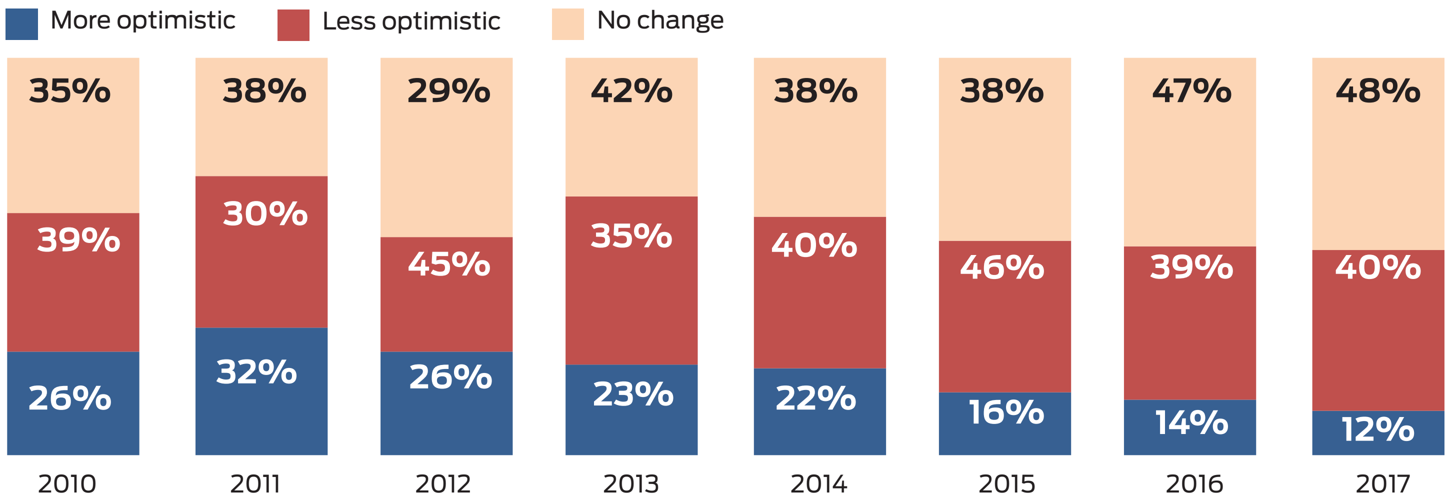

**Did your company reduce or stop planned investment in China in the past year?**




**Reasons your company reduced or stopped planned investment in China in the past year**



### View of the current business climate in China compared to three years ago

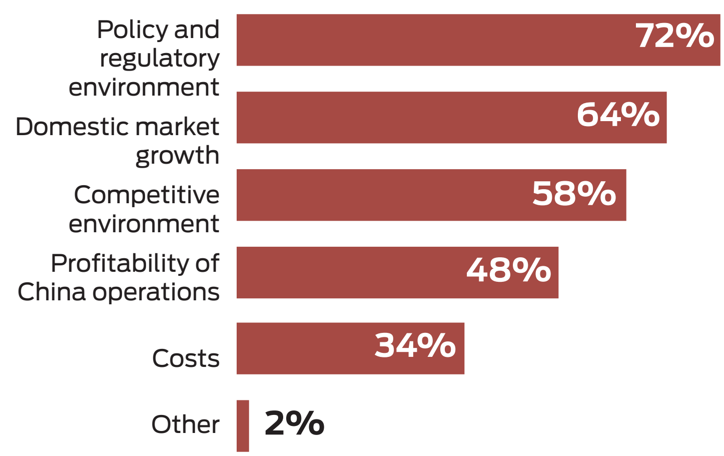


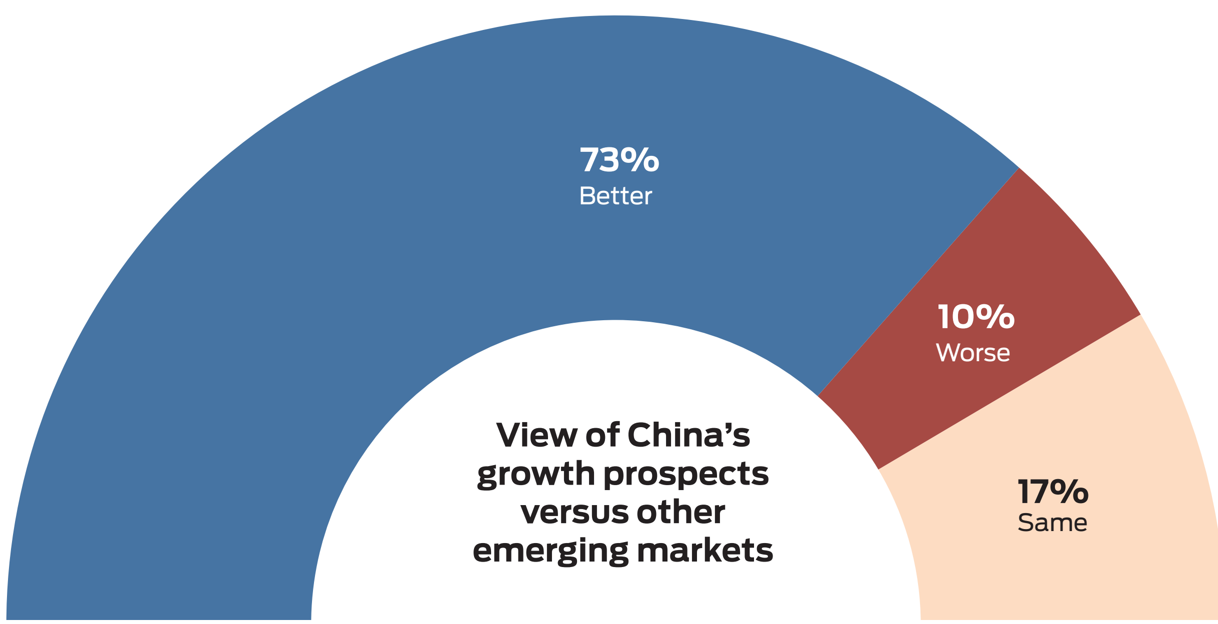

# Outlook on the China Market

China remains among the top 5 priority global markets for almost 90 percent of companies, but their confidence in their market prospects continues to soften.

While 84 percent remain optimistic or somewhat optimistic in their 5-year outlook, nearly half of those surveyed are less optimistic about the business climate than three years ago, versus 11 percent who are more optimistic.

### Issues affecting five-year outlook

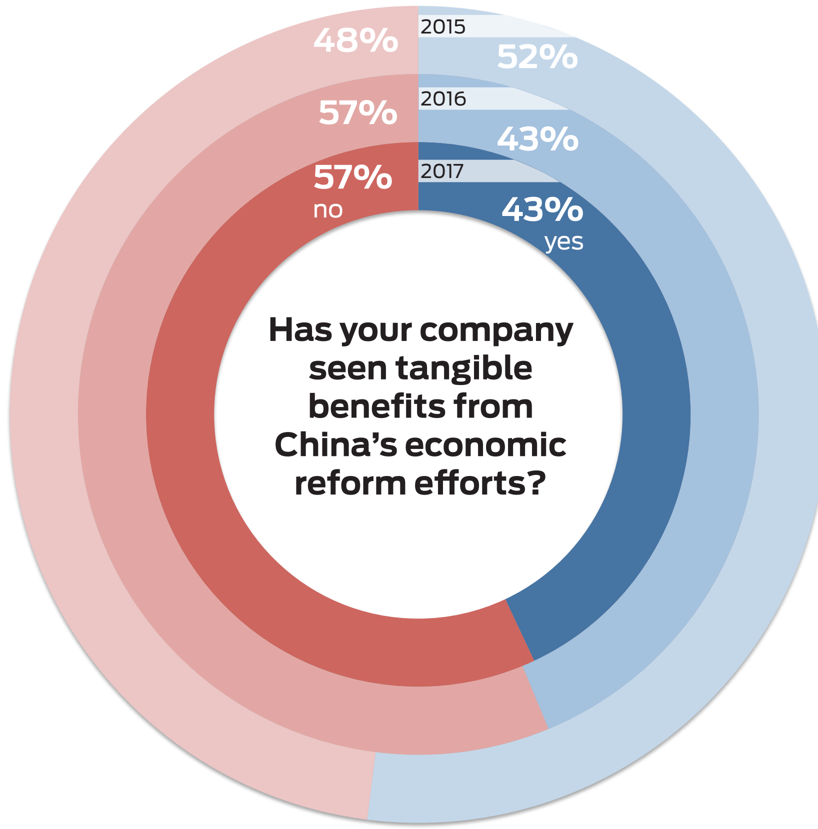


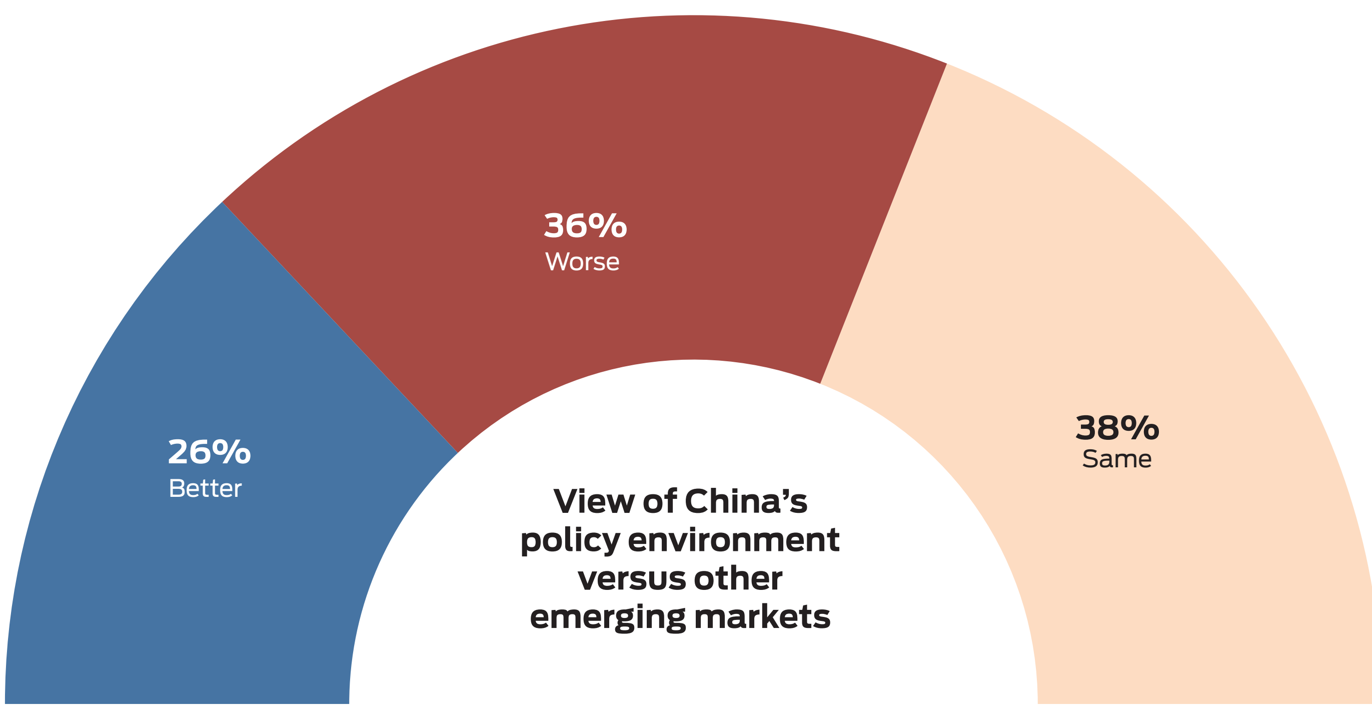



# Policy uncertainty is undermining confidence

China's policy environment is viewed as the same or worse than other markets. Policy issues cited as protectionist include foreign investment barriers, innovation policies, standards setting, and secure and controllable technology requirements.

- Fifty-seven percent have seen no impact from economic reforms announced four years ago.
- Twenty-four percent cite China's policies and regulations as the primary constraint on increased profitability in the market.



# Technology transfer

While most companies do not face outright tech transfer requests, it is an acute problem for those that do.

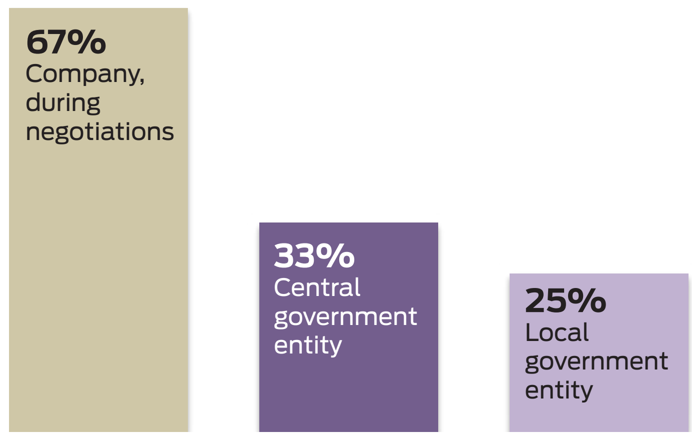
For companies that do receive direct requests for tech transfers:

- The request most frequently comes from a Chinese partner, rather than a government entity. While some of these requests may be a normal part of commercial negotiations, in many cases the hand of the Chinese government is behind these requests.
- Companies are sometimes able to mitigate the requests by either maintaining control of the technology or being paid an acceptable licensing fee. In other instances, companies are able to transfer only part of the technology requested.
- There are instances when companies are asked to transfer technology and they cannot either get an acceptable licensing fee or otherwise mitigate the request. In those circumstances, companies choose either to withdraw from the proposed transaction or transfer the technology, even though unacceptable.

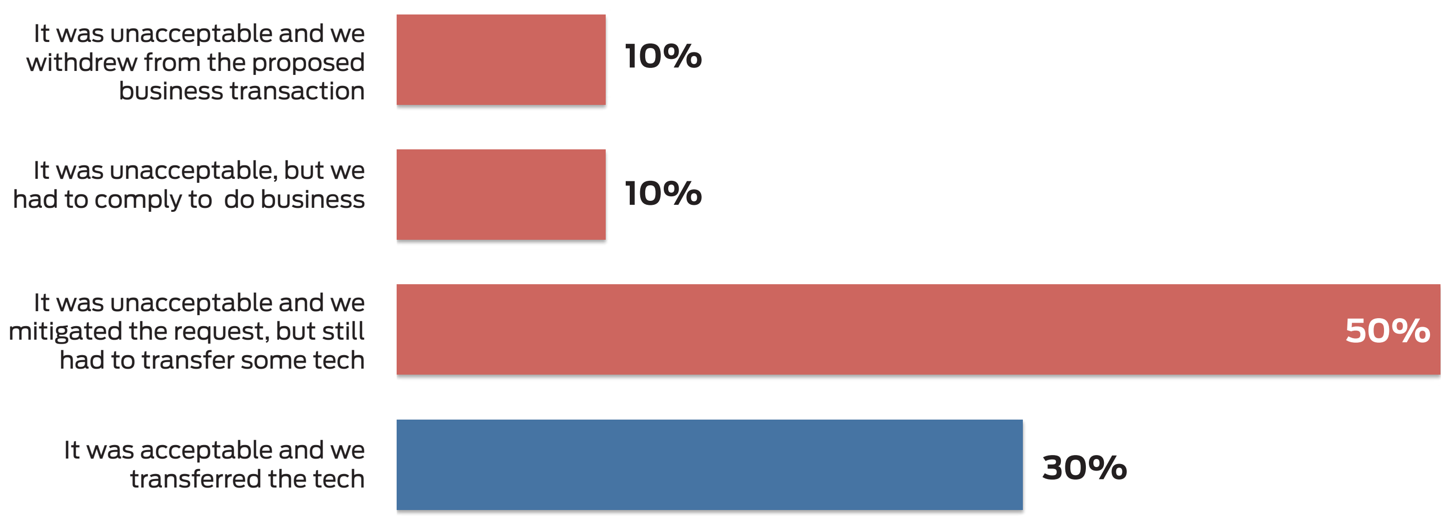
**19%**

said they have been directly asked to transfer technology to China

### Who asked for your technology to be transferred?

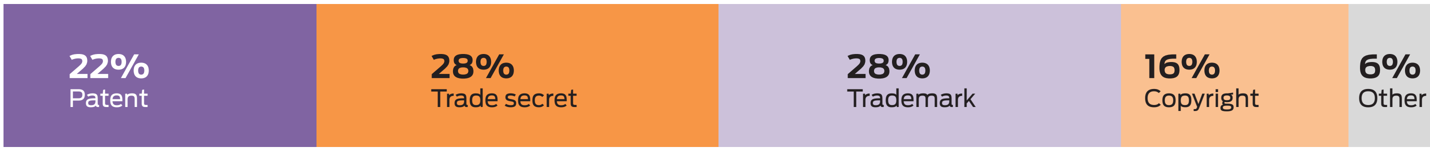



### How did your company respond?



### IP infringement of greatest concern




# Intellectual Property Rights protection

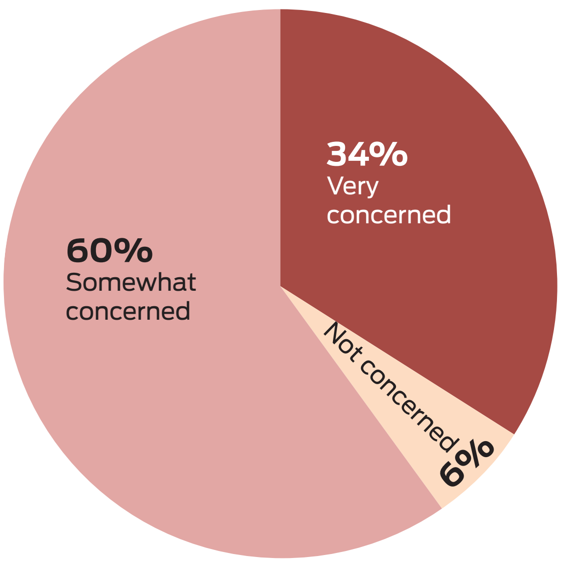
The vast majority of companies are concerned about protecting their IP in China.

Those concerns lead companies to make business decisions to limit their risk exposure in the market by limiting the types of products they sell in China and the R&D they do there.

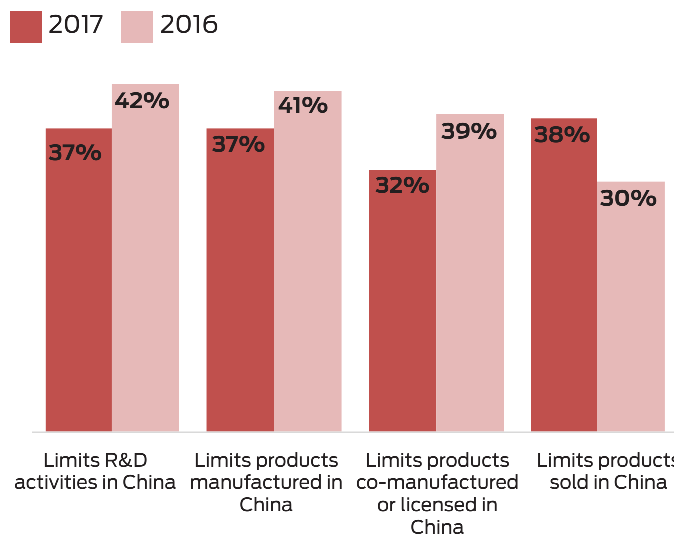
IP protection is slowly improving in China, but it remains the fifth highest issue of concern.

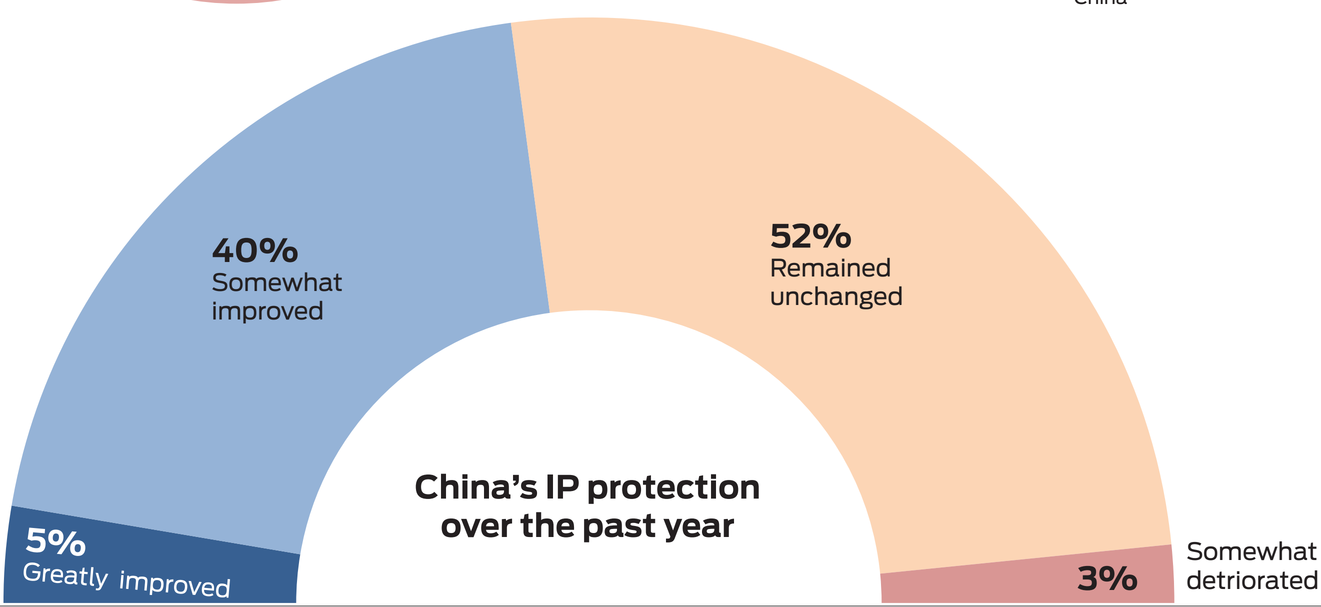
IP protection would be improved if China adopted a tougher deterrent against piracy, such as criminal penalties in cases of theft on a commercial scale.

### Level of concern about IPR enforcement




### Impact of IPR enforcement on the type of activities undertaken in China

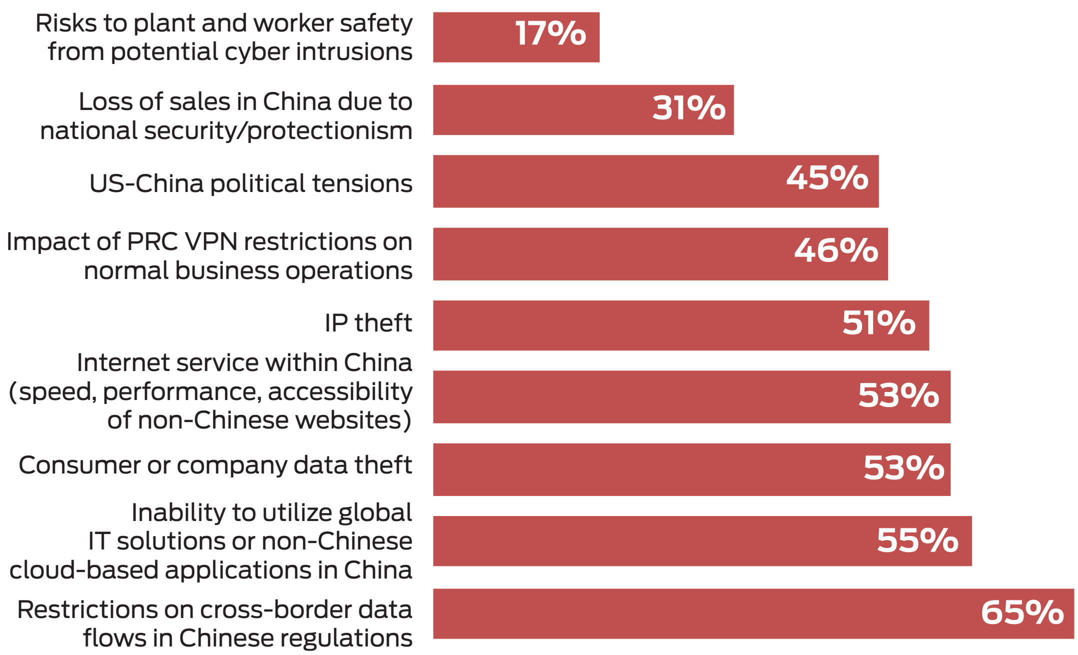


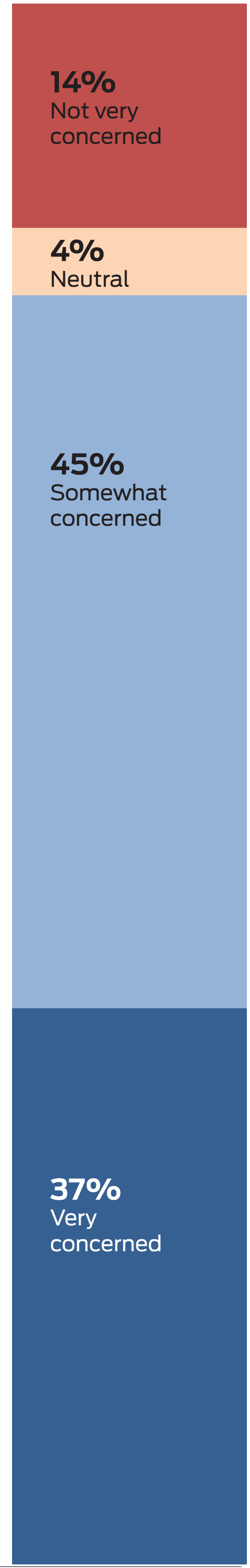
# Cybersecurity and IT issues

The overwhelming majority of companies (82 percent) have some level of concern about China's policies on data flows and technology security. 55 percent of respondents said China's internet regulations and VPN restrictions affect their companies' normal business operations.

**What cyber-related issues are of concern to your company?**




**Concerns about data flow restrictions and cybersecurity**

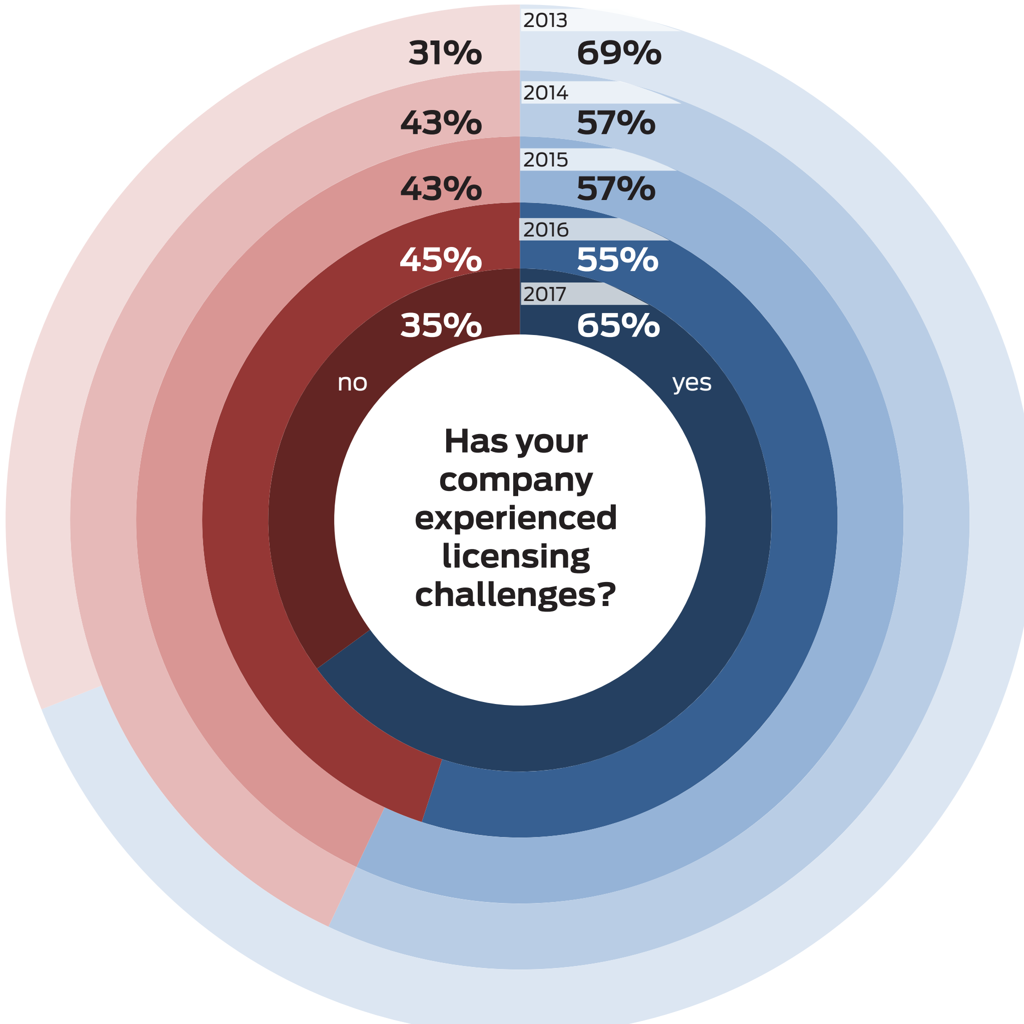


# Licensing

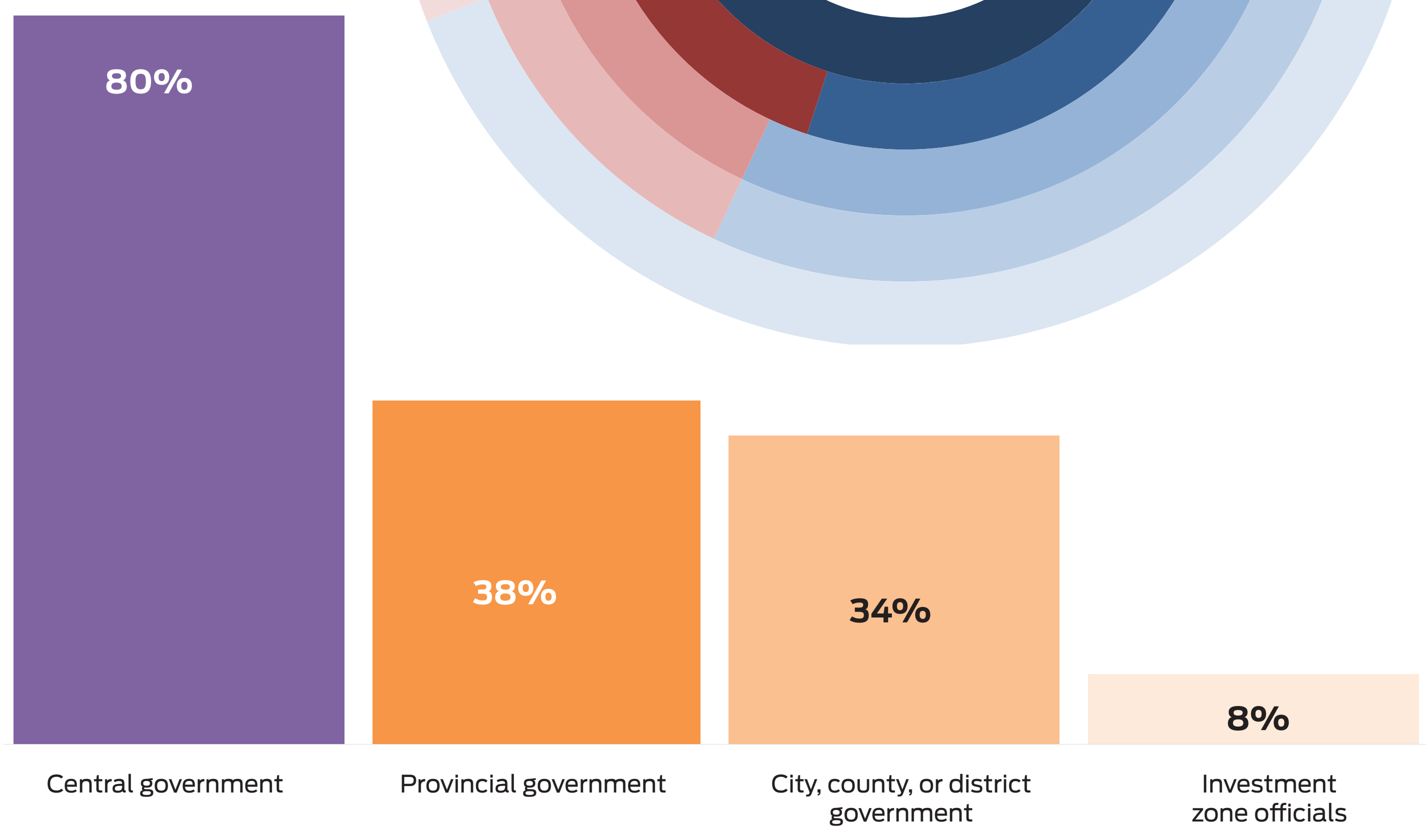
Most companies (65 percent) experience challenges with licenses and approvals in China.

Eighty percent report those problems are occurring at the central government level.

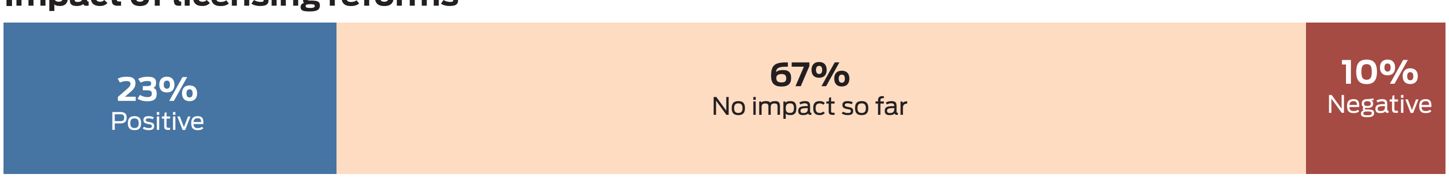
Almost three-fourths report that China's licensing reforms have had no impact to date.




## Where licensing problem occurred




## Impact of licensing reforms



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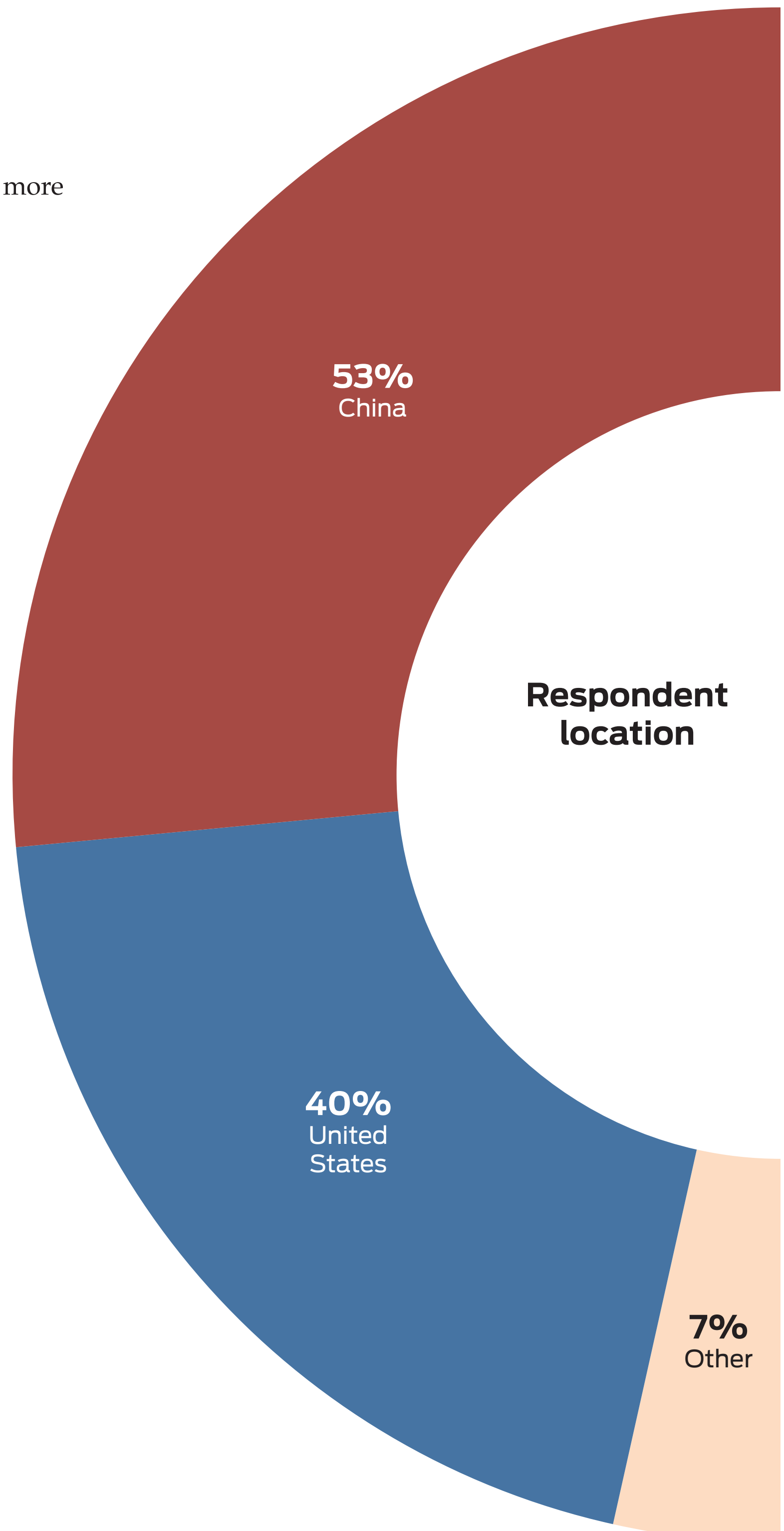
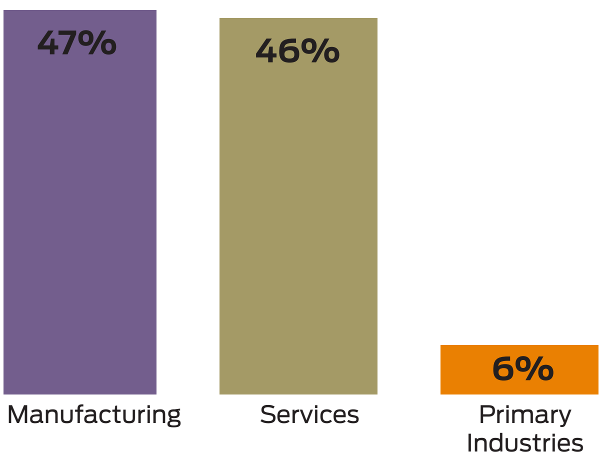
2017 MEMBER SURVEY

# Respondent profile

- US and China-based perspectives
- Balance of industry sectors
- Experienced — 80 percent in China for 10 years or more




## Type of operations in China




## Years doing business in China