

2019

China Business Survey



Juan Antonio Fernandez
Bin Xu
Dongsheng Zhou
Maria J. Puyuelo
Xin Huang

2019 China Business Survey

Juan Antonio Fernandez | Bin Xu | Dongsheng Zhou | Maria J. Puyuelo | Xin Huang

China Europe International Business School

Copyright ©2019 All Rights Reserved.
This research was supported by grants from CEIBS

TABLE OF CONTENTS

LETTER FROM THE RESEARCH TEAM	3
SECTION 1: DESCRIPTION OF THE COMPANIES PARTICIPATING	5
SECTION 2: BUSINESS INDICES	11
2.1. CURRENT PERFORMANCE INDEX – CPI	13
2.2. EXPECTED PERFORMANCE INDEX – EPI	16
2.3. BUSINESS CONFIDENCE INDICES – BCI	18
SECTION 3: CHALLENGES AND SUCCESS FACTORS	21
3.1. EXTERNAL CHALLENGES	22
3.2. INTERNAL CHALLENGES	25
3.3. SUCCESS FACTORS	28
SECTION 4: FOCUS BY AREA	31
4.1. HUMAN RESOURCES	32
4.1.1. Change in labor force, employee turnover and salary increase in 2018	32
4.1.2. Top Human Resources issues in China	33
4.1.3. Most effective measures to retain employees	35
4.2. SALES AND MARKETING	36
4.2.1. Competition	36
4.2.2. Market segments and mobility	37
4.2.3. Marketing, Sales and Distribution strategies	38
4.3. RESEARCH & DEVELOPMENT	44
4.4. GOVERNMENT & LEGAL ENVIRONMENT	47
4.4.1. Government relationships	47
4.4.2. Corruption	48

LETTER FROM THE RESEARCH TEAM

We are pleased to present the 9th annual CEIBS China Business Survey.

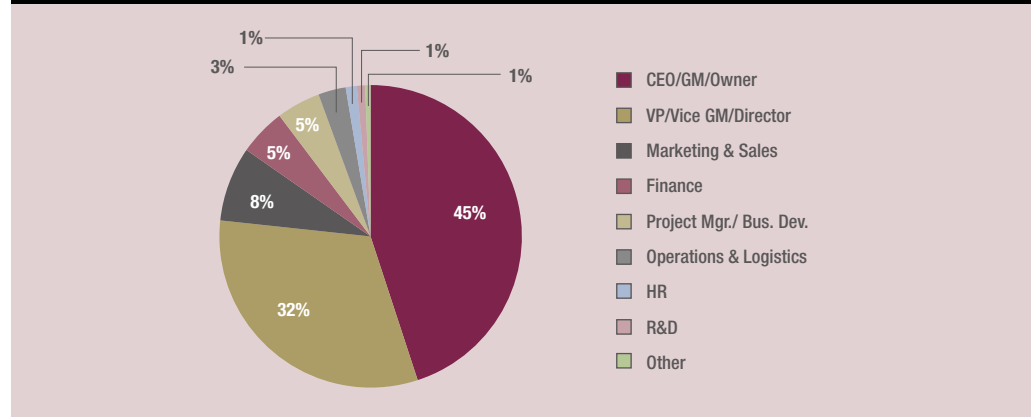
We want to sincerely thank all of the executives working in China who have participated in this survey for their time and valuable contribution. In particular we thank the CEIBS alumni community and current students who have given their support to this research. Our gratitude is also extended to the various Swiss organizations in China and its affiliated companies: Swiss Center China, Swiss Embassy in China, Swiss Business Hubs, Swissnex China, SwissCham, China Integrated. Ltd.

We also acknowledge the financial support from CEIBS Research Fund, support from the Alumni, MBA, EMBA, FMBA, HEMBA and Executive Education offices at CEIBS, and the many friends that helped us with their network. We are grateful to all of them.

Top management executives and also functional experts have given us a very valuable and rich perspective of the situation of their businesses in China in 2018 and their expectations for 2019 and the future.

The 2018 CEIBS Business in China Survey was completed by 1,018 executives between November and December 2018, with 683 from Chinese companies and 335 from foreign companies. Among them were 454 CEOs, GMs, and company owners; 315 Vice Presidents, Deputy General Managers or Directors. The rest represented all the remaining business functions: HR, Finance, Marketing, Sales, Operations and Research & Development. Of the respondents, 87% are from the Chinese mainland, 2% from Taiwan, Hong Kong or Macao, and 11% from other countries, 45% of the total sample has more than 20 years of work experience. The firms they work for are both Chinese owned (67% of them) and foreign owned (33%). This broad and experienced sample added rich and valuable perspectives to the survey.

FIGURE 1 - WHAT IS YOUR POSITION IN THE COMPANY? N= 1018



THE RESEARCH TEAM



Prof. Juan Antonio Fernandez

Dr. Juan Antonio Fernandez is a Professor of Management at China Europe International Business School (CEIBS) in Shanghai, China.

Prof. Fernandez has co-authored six books: *America Latina en China*, *CHINA CEO*, *Chinese SOEs Reform*, *China CEO: A Field Guide*, *China (Foreign) Entrepreneur* and *Chinese Entrepreneurs*. He has given presentations about his Chinese research in USA, India, Japan, Korea, UK, France, Italy, Spain, Vietnam, Mongolia and Ghana



Prof. Bin Xu

Dr. Bin Xu is Professor of Economics and Finance, Associate Dean (Research) at CEIBS. He received his B.A. and M.A. from Fudan University, and Ph. D. from Columbia University.

Dr. Xu's current research focuses on the global and Chinese economy, multinational enterprises in China, and trade and finance issues of emerging markets. He has published extensively in both international and Chinese journals, and is author of *International Trade* (Peking University Press, 2009). Dr. Xu has worked as a consultant for International Monetary Fund (IMF) and the World Bank.



Prof. Dongsheng Zhou

Dr. Dongsheng Zhou is Professor of Marketing at CEIBS. He is also the academic director of SEPC, a joint executive training program with Harvard Business School and Tsinghua University. He received his Ph.D. from the University of British Columbia (UBC), Canada.

Dr. Zhou's research focuses on marketing strategies, game theory, MNE strategies in China and China's private enterprises. His research has been published in the *Academy of Management Review*, *International Business Review*, *International Marketing Review*, and others. Dr. Zhou has conducted consulting services for a number of firms (e.g. IBM, DuPont).



Maria J. Puyuelo

Maria J. Puyuelo is Research Associate at CEIBS. She obtained her MBA from Stanford Graduate School of Business (USA) and her MSc in Engineering from the University of Zaragoza (Spain).

Maria started her career at Procter & Gamble and has held various senior marketing positions at L'Oreal Luxury Goods Division. She has also worked as a free lance consultant, helping businesses develop and grow their markets in China. She has co-authored the book *America Latina en China*. Most recently she has developed and taught courses in the leadership field.



Xin Huang

Xin Huang is Research Assistant at CEIBS. He received his M.A. in business management from School of Business and Management of Shanghai International Studies University (SISU). Prior to joining CEIBS, Xin Huang worked as a trainee in Vanke, a leading real estate developer in China. During his postgraduate years, he participated in a number of research projects including one funded by the National Social Science Foundation of China.



SECTION 1

DESCRIPTION OF THE COMPANIES PARTICIPATING

This section details the following information about the companies that have participated in the 9th edition of the CEIBS China Business Survey

- Type of ownership (Chinese or foreign), business sector, industry and type of activity
- Location of Global Headquarters
- Degree of internationalization
- Number of employees in China and globally
- Revenue level in China
- Legal form in China
- Years of operation

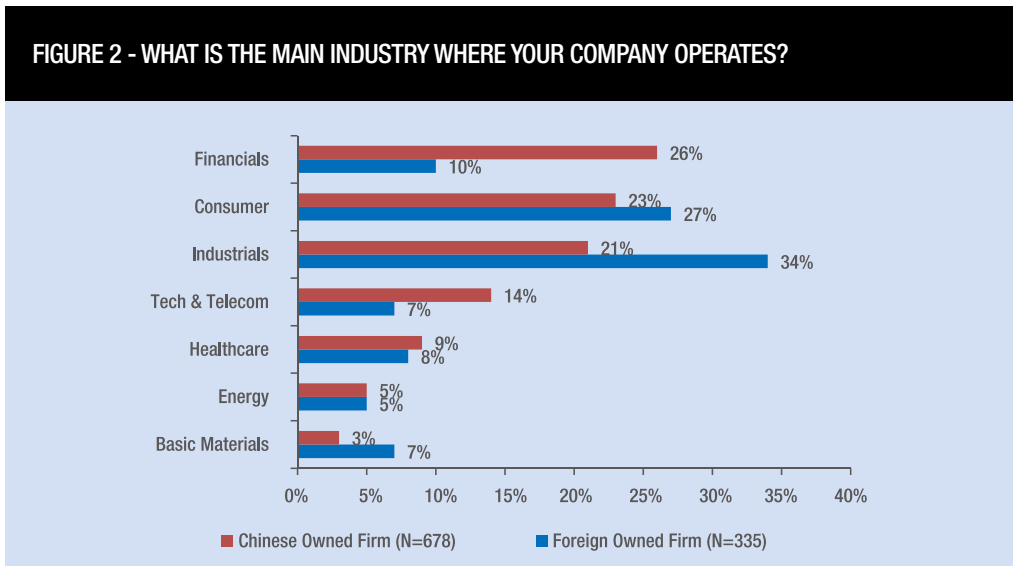
The purpose of the section is to give a general overview of the type of companies that took part in the survey. This information helps clarify the scope of the survey and provides background to interpret survey results.

SECTION 1: DESCRIPTION OF THE COMPANIES PARTICIPATING

A total of 1,018 companies operating in China have participated in the 2019 edition of the CEIBS China Business Survey. This sample of businesses includes 683 (67%) Chinese owned companies (i.e. with 50% or more Chinese ownership)¹ and 335 (33%) foreign-owned companies (i.e. with more than 50% foreign ownership).

In terms of business activity, 39% of firms have their main activity in manufacturing and 61% in services. 70% of the total samples of firms are B2B companies, having other businesses as main clients, while 30% are B2C companies, offering products and services directly to consumers.

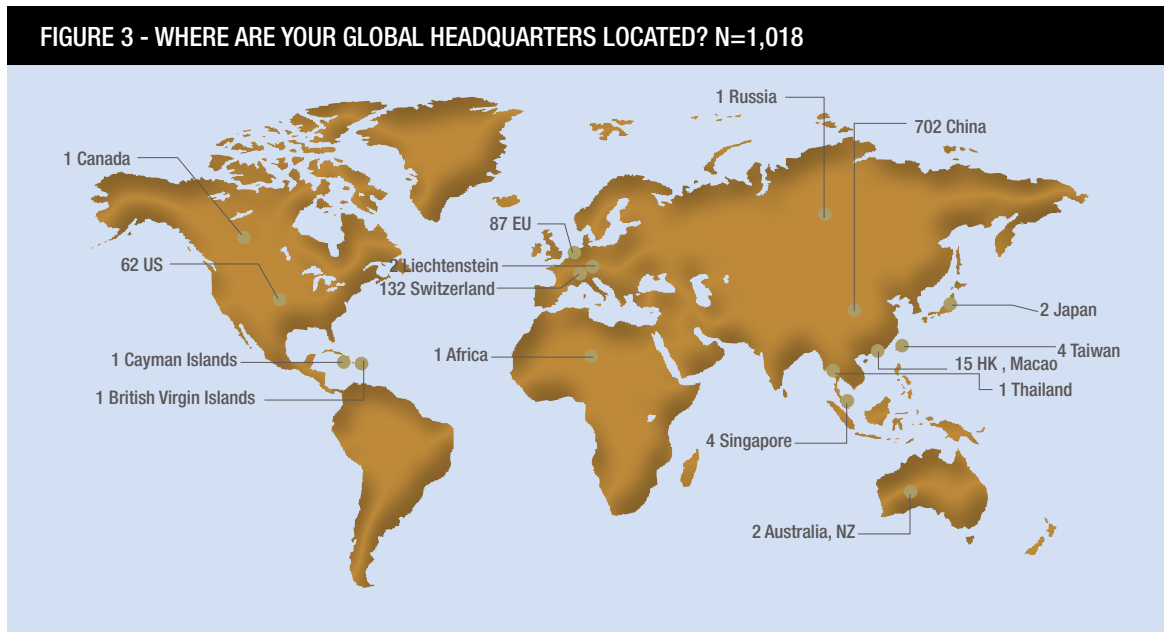
The industries represented are varied, topped by industrial products and services (254 firms, 25% of total sample), consumer goods and services (246 firms, 24%), Financials (209 firms, 21%), Technology and Telecommunications (118 firms, 12%), Healthcare (84 firms, 8%), Energy (49 firms, 5%), and Basic Materials like chemicals, forestry and mining (46 firms, 5%). We observe a considerably larger presence of financial companies within the Chinese-owned firms of our sample (26% versus 10% of foreign firms), a consequence of existing regulations limiting or constraining foreign investment in the sector. Foreign-owned firms are markedly more represented in "Industrials" with 34% of them vs. 21% of Chinese-owned firms in the industry.



In terms of market position, the firms surveyed operate mostly in the mid and high ends of the market. According to survey answers, 450 firms (50%) in our sample operate mainly in the premium segment, another 416 (46%) in the middle segment and only 36 (4%) in the low-end of the market. Moreover, 273 companies (30%) identify themselves as market leaders for their main business line and 395 (44%) consider to be in the Top 5. When splitting by type of company ownership, we do observe a considerable difference in market positioning between the two groups with 77% of foreign companies in the sample in the premium segment vs. a lower 38% of Chinese-owned firms. Inversely, 57% of Chinese-owned firms operate in the middle segment of the market, while 23% of foreign-owned do so.

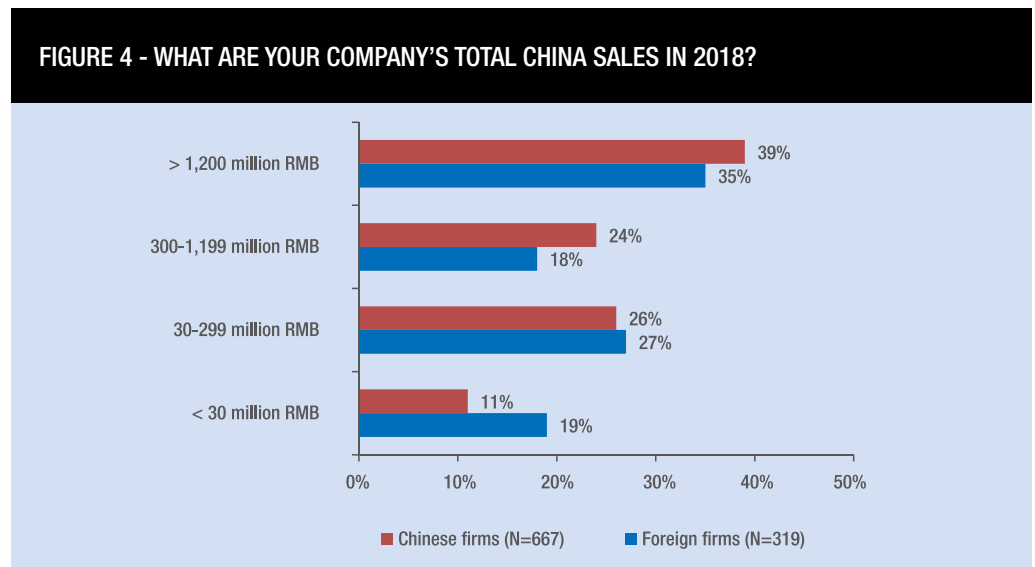
¹ Including Chinese controlled Joint Ventures

The location of their Global headquarters is shown in the following map:



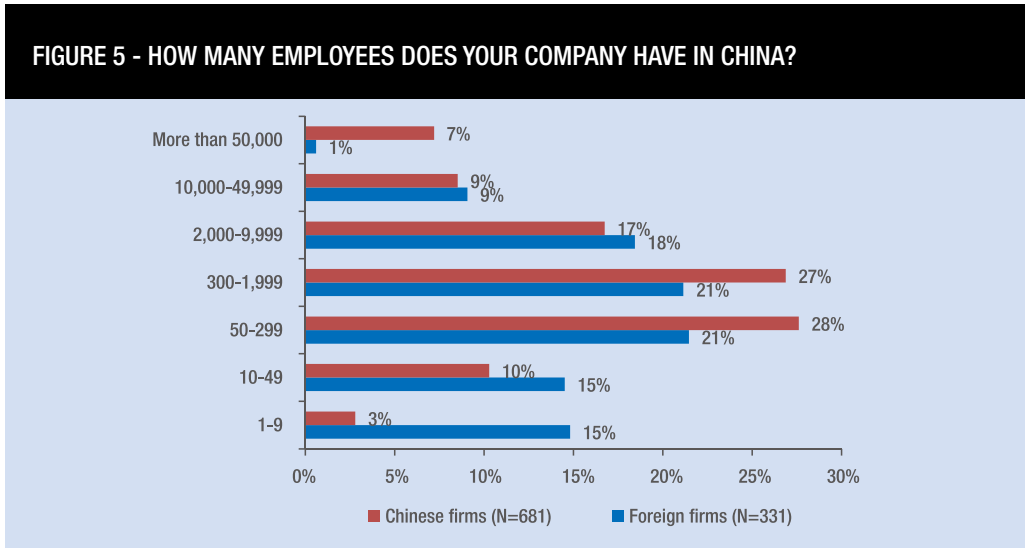
In 2018, participating companies had generated collective revenue of more than 650 billion RMB and were employing more than 6.5 million people in China alone.

Of participating companies, 63% of the Chinese-owned firms and 53% of the foreign-owned firms surveyed are considered large².

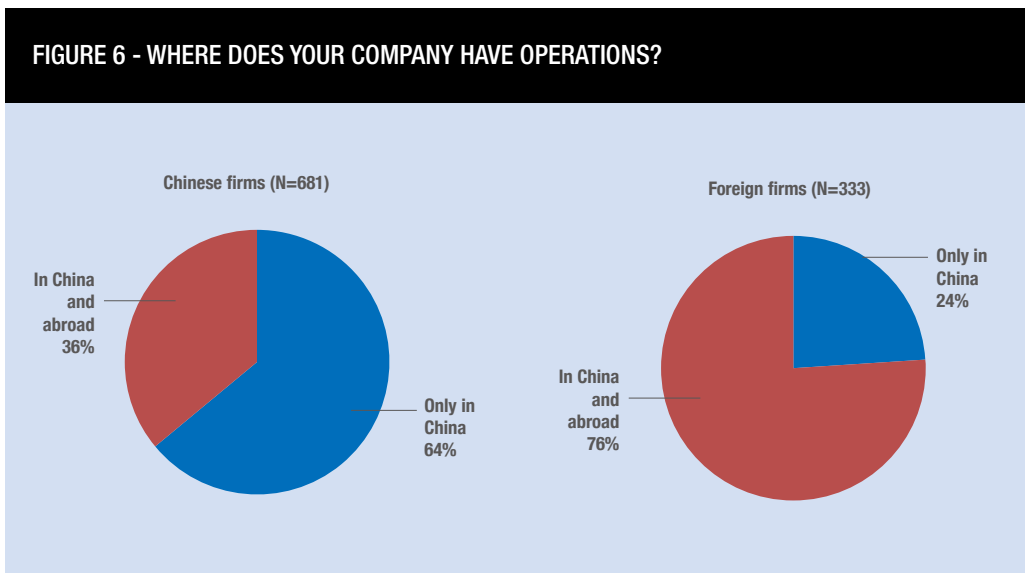


² According to China official definition companies with more than 300 million RMB are considered large.

The sample of companies varies widely in size, ranging from companies with less than 10 employees in China to those with more than 50,000. Surveyed Chinese firms tend to be larger than foreign ones with, in average, 4,800 employees in China or more, compared to 1,600 employees or more for foreign-owned firms. Moreover, 30% of foreign-owned firms surveyed have less than 50 employees versus only 13% of Chinese firms.



36% of the Chinese owned firms in our sample have operations abroad too. And although 76% of foreign firms in our sample are international, there is a non-negligible 24% of foreign owned firms that only operate in China. These are foreign entrepreneurs who have started their business ventures in China.



The internalization of Chinese firms is a development that has been captured in our survey over the past years. The following charts show the evolution of interest in overseas expansion for sampled Chinese firms in the past five years, as well as the variations in their preferred geographies for expansion.

FIGURE 7 - HOW IMPORTANT IS OVERSEAS EXPANSION TO YOUR COMPANY?

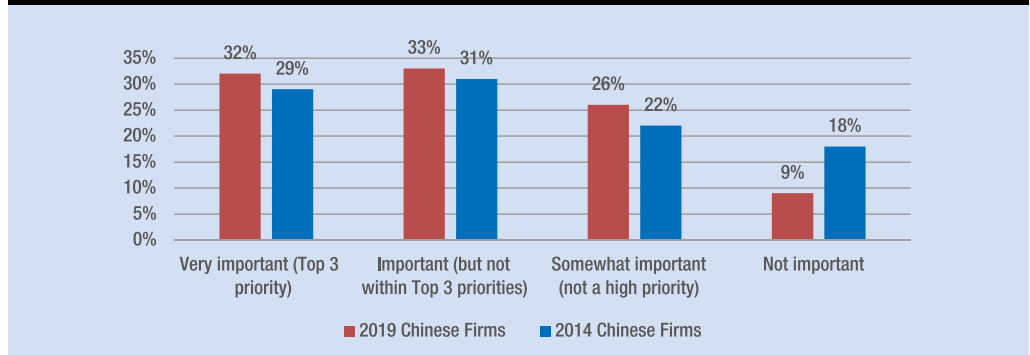
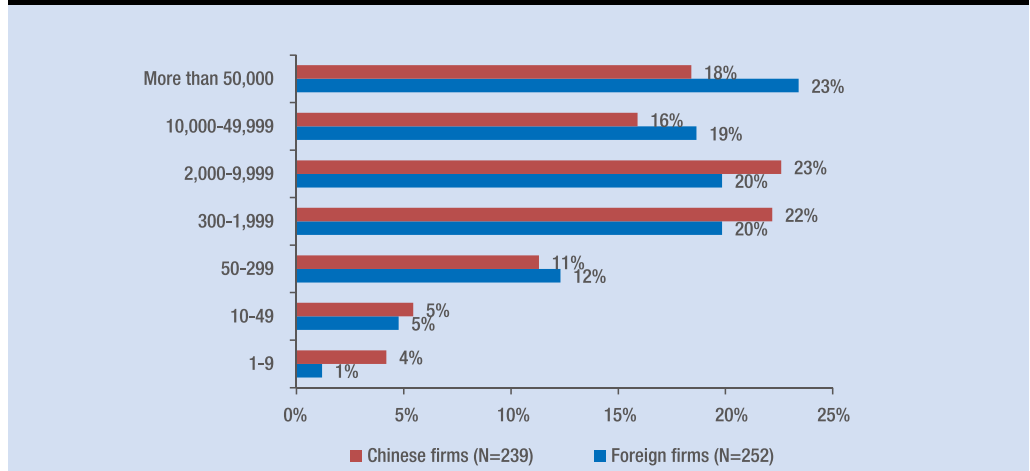


FIGURE 8 - WHERE OUTSIDE OF CHINA DO YOU PLAN TO INVEST IN THE NEXT 3 YEARS?

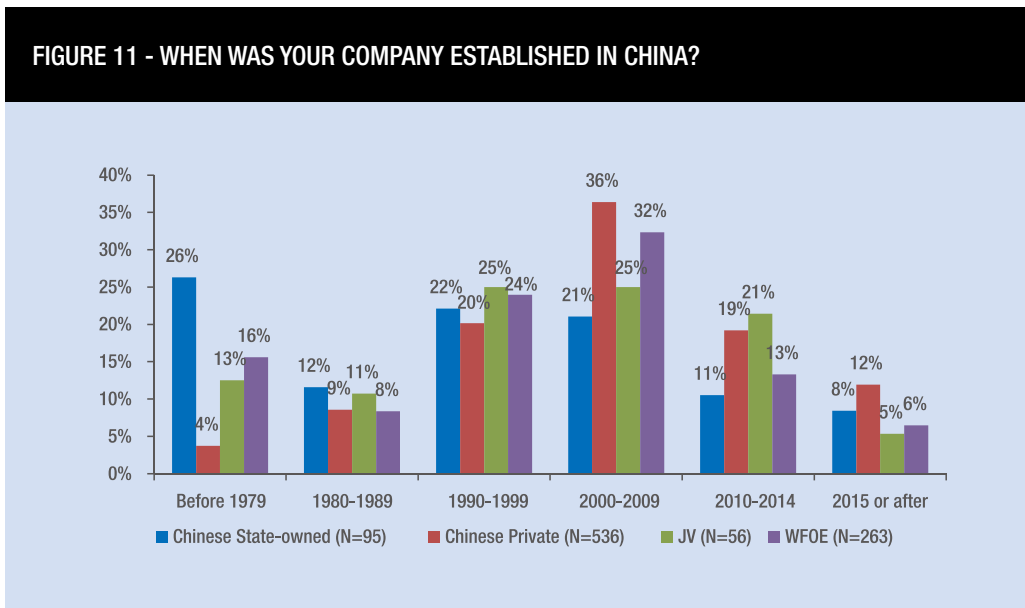
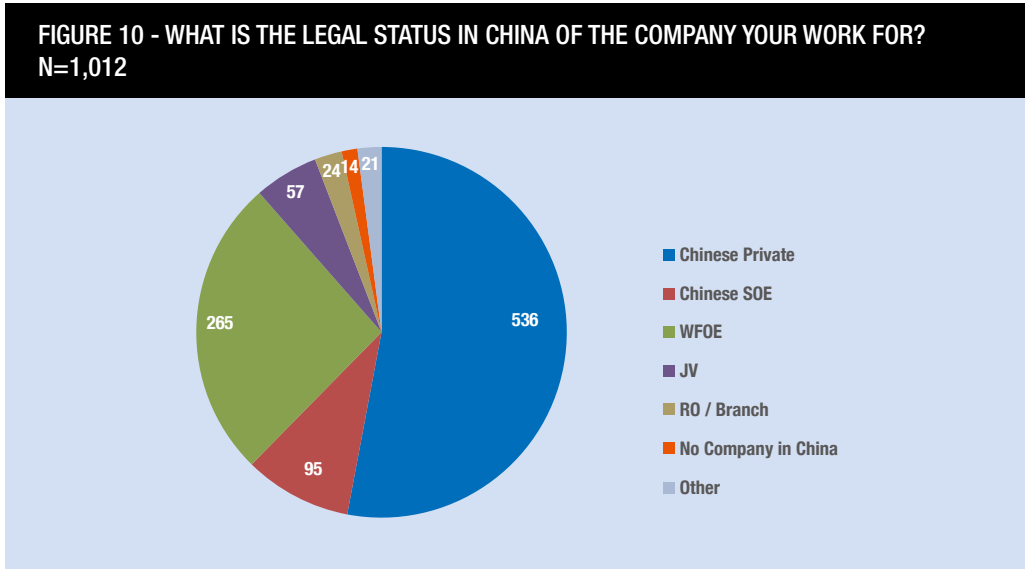


Within the surveyed companies that operate both in China and abroad, foreign-owned ones are overall larger in their global operations than Chinese-owned firms. 42% of the surveyed foreign companies with international operations have more than 10,000 employees globally vs. 34% of their Chinese-owned counterparts.

FIGURE 9 - FIRMS WITH INTERNATIONAL OPERATIONS- HOW MANY EMPLOYEES DOES YOUR COMPANY HAVE GLOBALLY?



53% of surveyed companies are Chinese privately owned or private-holding companies and 9% are state-owned or state-holding enterprises. Joint Ventures (JV) constitute 6% of the sample, with different levels of Chinese and foreign ownership. Most of the foreign-owned companies are Wholly Foreign Owned Enterprises (WFOE, 26% of total sample), with Representative Offices (RO) and Branches of foreign companies making up the rest.



Most of Chinese private companies in our sample, 88%, have been established after 1990 following the economic reforms initiated by Deng Xiaoping in the late 1980s and early 1990s, which triggered a remarkable growth of the private sector. In contrast, 38% of the SOE in our sample were established before 1990.



SECTION 2

BUSINESS INDICES

This section presents four Indices:

- Two Business Performance Indices that measure performance variation compared to the previous year, and expected performance for the next year. They are based on sales revenue and profit growth, realized and expected.
- Two Business Confidence Indices give reading on the optimism and confidence in business results declared by respondents.

Business Performance Indices are:

- Current Performance Index (CPI)
- Expected Performance Index (EPI)

These two directional indices were introduced in the 2013 report to measure variation both in current and expected performance of the surveyed companies. Each index (ranging from 0 to 100) is constructed similarly to the well-known Purchasing Managers' Index (PMI): an index reading of 50 means that performance is unchanged compared to previous year, a number over 50 indicates an improvement while anything below 50 suggests a decline. The further away from 50 the index is, the stronger the change over the period. The indices are based on multiple choice questions with 5 possible answers³.

Business Confidence Indices are:

- Business Confidence Index, for next year
- Business Confidence Index, for the next 5 years

The Business Confidence Index is a measure of the optimism stated by executives in our sample with respect to the evolution of their businesses for the next year (2019) and the next 5 years (2019 to 2023). These 2 indices have been part of the CEIBS Business in China Survey since its inception 9 years ago, which allows us to start recognizing emerging trends as well as current values.

The reading ranges from 0 to 10 (0 = Absolutely Not Confident, 3 = Not Confident, 5 = Neutral, 7 = Confident, 10 = Extremely Confident). The executives in our survey are asked to state their confidence level in the short term (next year) and in the medium term (next 5 years).

³ $INDEX = (P1*1) + (P2*0.75) + (P3*0.5) + (P4*0.25) + (P5*0)$

P1 = Percentage number of answers that reported a substantial improvement.

P2 = Percentage number of answers that reported an improvement.

P3 = Percentage number of answers that reported no change.

P4 = Percentage number of answers that reported a deterioration.

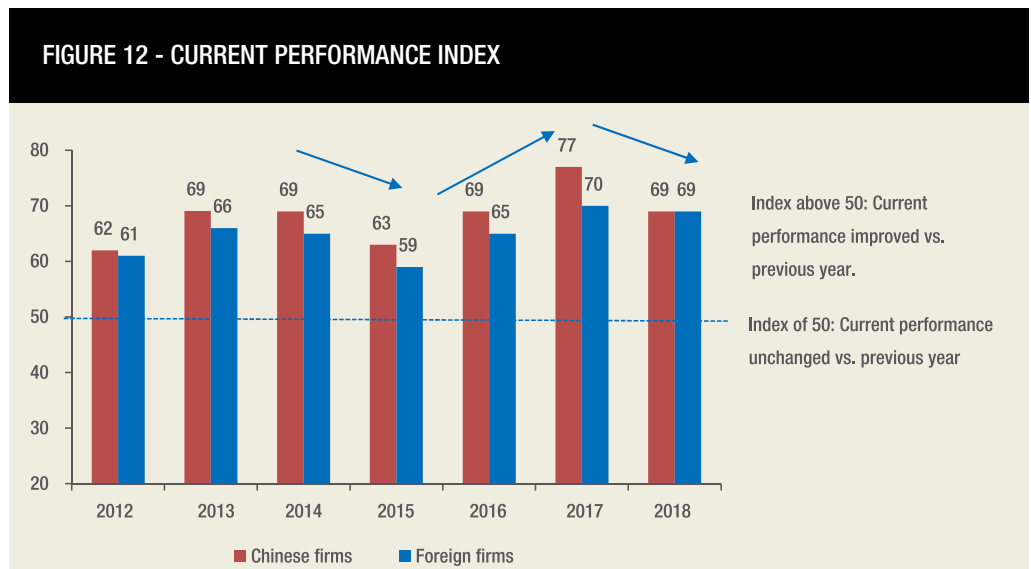
P5 = Percentage number of answers that reported a substantial deterioration.

2.1. CURRENT PERFORMANCE INDEX – CPI

2018 performance indices decrease compared to last year (which had shown the highest indices since the beginning of this measure in 2012). Despite this drop, companies in our sample still show robust growth of their businesses in 2018 when compared to 2017, and overall they expect to continue their growth in 2019.

The CPI Index is calculated as a composite of 2 survey questions: Revenue and Profit Level. Each variable is attributed the same weighting. An index above 50 indicates performance improvement vs. the previous year, the further away from 50 the index is, the stronger the change over the period. Performance is based on both revenue and profit evolution in 2018.

2018 Current Performance Indices (CPIs) are higher than 50 for both sampled Chinese and foreign firms, reflecting better business results in 2018 than in 2017. Chinese and foreign owned companies in our sample both show present a CPI of 69. However, the indices show a slight deterioration in 2018 performance when compared to 2017, as they revert back to levels close to 2016.



Given that the CPI integrates sales and profits results into one index, we can explore both business indicators separately to better understand the results in 2018.

Sales:

The following figures reflect the answers of our sample to the question “How do you expect your company’s China sales compared to last year?” as asked in 2018 and 2017. We observe that 70% of Chinese firms reported higher or substantially higher sales for 2018, vs. a higher 79% in 2017. Within foreign firms, 70% of our sample reports sales growth in 2018 vs. 69% in 2017.

FIGURE 13 - HOW DO YOU EXPECT YOUR COMPANY'S CHINA SALES IN 2018 COMPARED TO 2017?

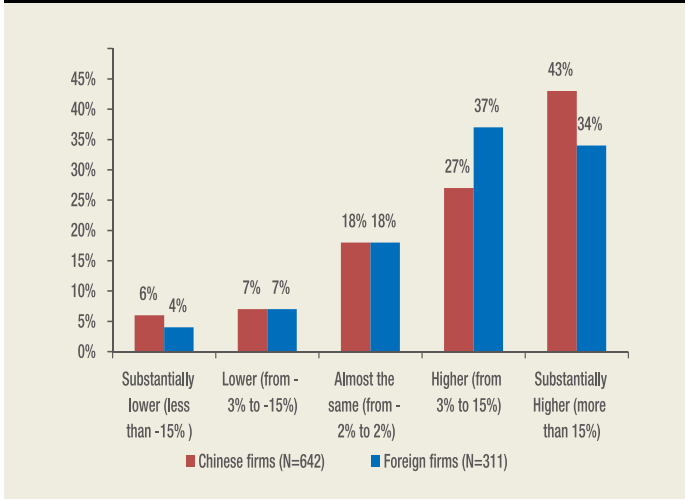
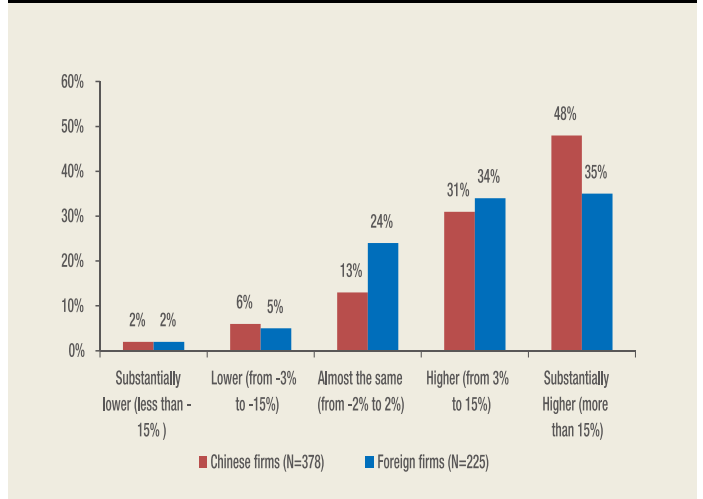


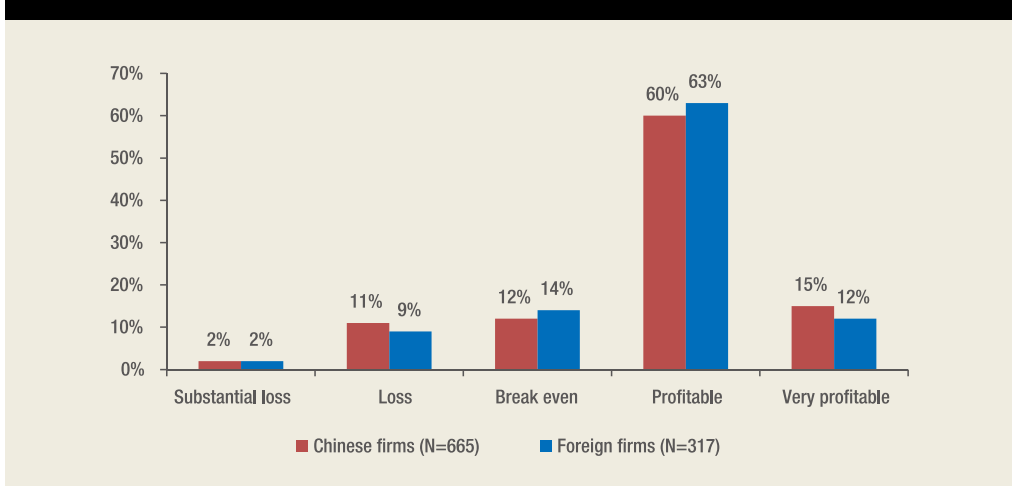
FIGURE 14 - HOW DO YOU EXPECT YOUR COMPANY'S CHINA SALES IN 2017 COMPARED TO 2016?



Profits:

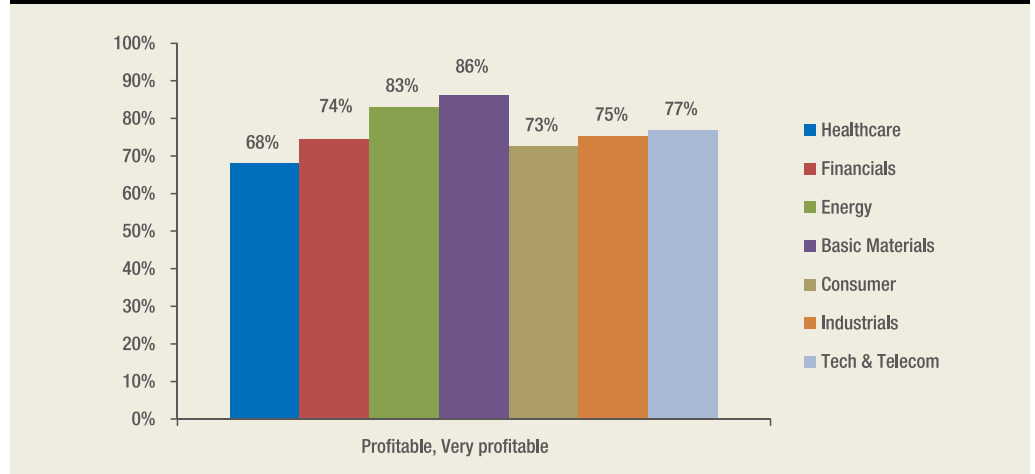
In our overall sample, 75% of the companies declared being profitable or very profitable in 2018, while 12% incurred losses. The following chart reflects the profit situation of our sample in 2018, separating the results of Chinese and foreign firms.

FIGURE 15 - HOW PROFITABLE DO YOU CONSIDER YOUR CHINA OPERATION IN 2018?



In terms of industry, Basic Materials and Energy sectors report the largest percentage of firms profitable or very profitable in 2018.

FIGURE 16 - 2019 SURVEY: HOW PROFITABLE DO YOU CONSIDER YOUR CHINA OPERATION IN 2018? PROFITABLE OR VEY PROFITABLE - BY INDUSTRY



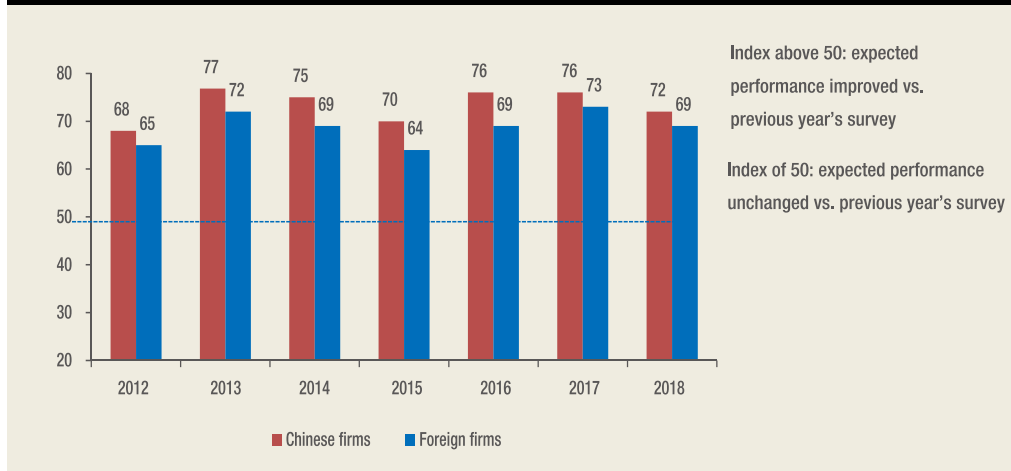
2.2. EXPECTED PERFORMANCE INDEX – EPI

Growth expectation for 2019 for both Chinese and foreign firms surveyed, however in levels lower to what was expected for 2018 in last year's edition of the survey.

A majority of the companies surveyed are optimistic for 2019. The Expected Performance Index (EPI) amounts to 72 (Chinese companies) and 69 (foreign companies), reflecting an expected growth for 2019 for both types of companies⁴. These EPI values are lower to those declared in last year's survey for both Chinese and foreign companies. Chinese firms had been particularly optimistic in their future in 2017 and 2016, and they now revert back to the levels shown in 2015. Foreign firms show the same EPI they did two years ago, in 2016.

The EPI is calculated as a composite of 2 survey questions: Revenue and Profit Level expectations for 2019. Each variable is attributed the same weighting.

FIGURE 17 - EXPECTED PERFORMANCE INDEX



⁴ An index above 50 indicates expected growth in sales and profit, the further away from 50 the index is, the stronger the change over the period

When we look at planned investments in China for 2019, which are closely related to growth expectations, a reduced optimism is observed for both Chinese and foreign firms.

FIGURE 18 - FOREIGN FIRMS: WHAT INVESTMENTS DO YOU PLAN FOR THE NEXT YEAR IN CHINA?

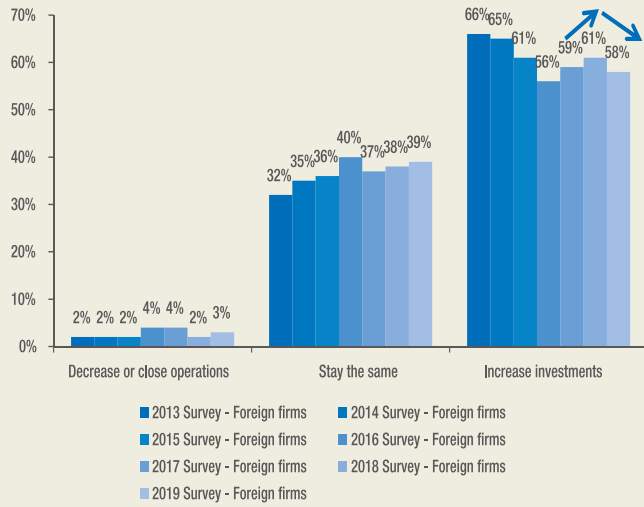
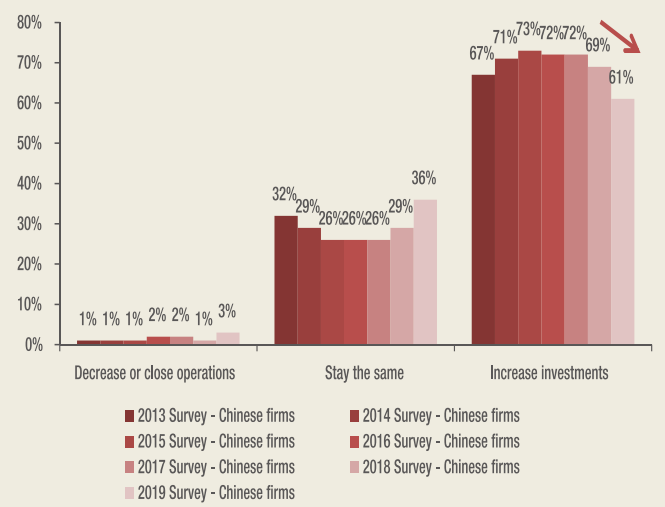


FIGURE 19 - CHINESE FIRMS: WHAT INVESTMENTS DO YOU PLAN FOR THE NEXT YEAR IN CHINA?



2.3. BUSINESS CONFIDENCE INDICES – BCI

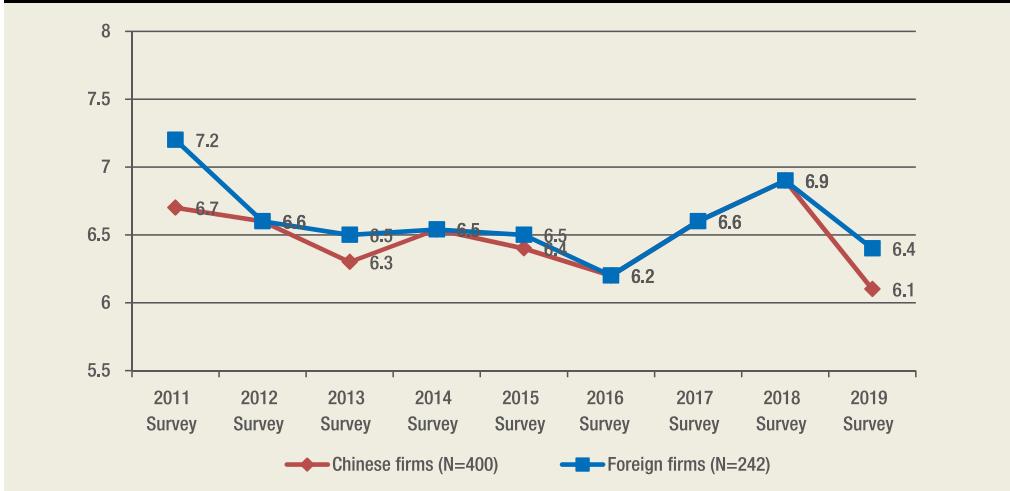
Confidence in the next year and in the next five years decreases for both Chinese and foreign firms sampled. Chinese firms show less optimism than foreign ones.

The annual survey provides two confidence indices based on the question, “How confident are you that your operations in China will be successful in the next year and in the next 5 years?” The scale is from 0 (no confidence at all) to 10 (maximum confidence).

In 2018, our sample of executives declare a loss of confidence in the future success of their businesses when compared to last year’s edition of this survey.

Confidence for the next year: Chinese companies’ confidence in the next year drops to 6.1, the lowest since the beginning of the index 9 years ago. Foreign companies declare a confidence of 6.4 for the next year, slightly higher than their Chinese counterparts. For reference, a level of 7 indicates “Confident” and a level of 6 indicates “Neutral”.

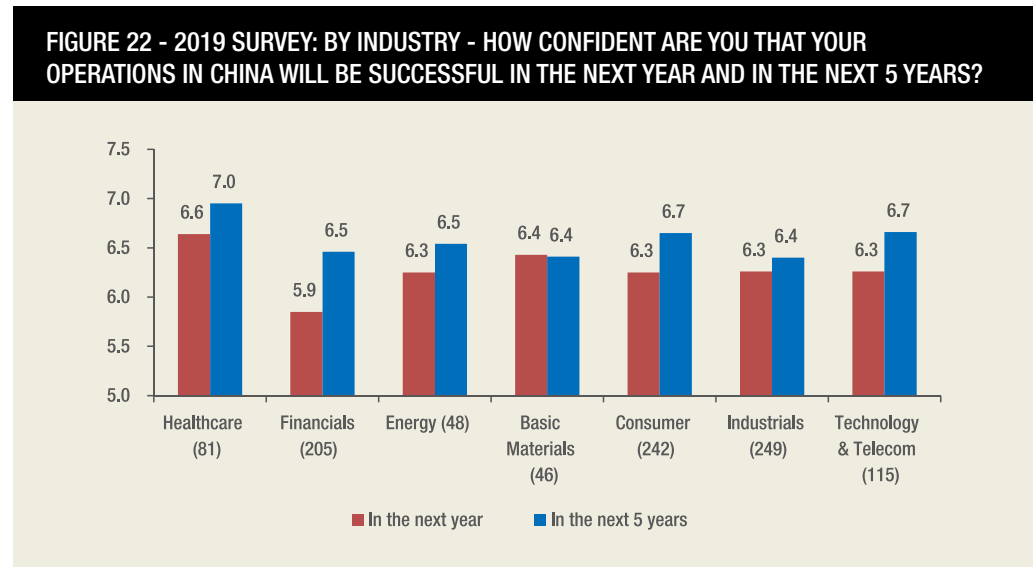
**FIGURE 20 - HOW CONFIDENT ARE YOU THAT YOUR OPERATIONS IN CHINA WILL BE SUCCESSFUL IN THE NEXT YEAR?
0=ABSOLUTELY NOT CONFIDENT, 3=NOT CONFIDENT, 5=NEUTRAL, 7=CONFIDENT, 10=EXTREMELY CONFIDENT**



Confidence for the next five years: We notice that the five-year confidence of executives in the success of their businesses descends following three consecutive years of increasing optimism. Both Chinese and foreign companies present a very close level of confidence of 6.6 and 6.5 respectively.



Analyzing by industry, we notice that companies operating in the Healthcare space exhibit the most confidence in the next year and the next five years (6.6 and 7.0 respectively).





SECTION 3

CHALLENGES AND SUCCESS FACTORS

This section details the difficulties encountered in China by the firms in our sample and the keys to their success:

- External Challenges
- Internal Challenges
- Success factors

The purpose of this section is to identify the main challenges faced in China by the companies surveyed, explore the relevant differences in the difficulties faced by Chinese companies compared to foreign companies, and learn how the companies in our survey deal with these challenges.

3.1. EXTERNAL CHALLENGES

For the first time in five years, “Fierce competition” is not the most pressing external challenge for our sample of firms as “Economy slowdown in China” takes the first position with 59% of total companies citing it as a key external issue. “Rising labor cost” is the second most pressing issue for the sample of companies and “Fierce competition” remains in the Top 3 of external worries.

Despite this change in the most pressing issue, the Top 4 External Challenges remain unchanged for both Chinese and foreign firms in the last 5 years: “Slowdown of Chinese economy”, “Rising labor costs”, “Fierce competition”, and “Government and legal environment”.

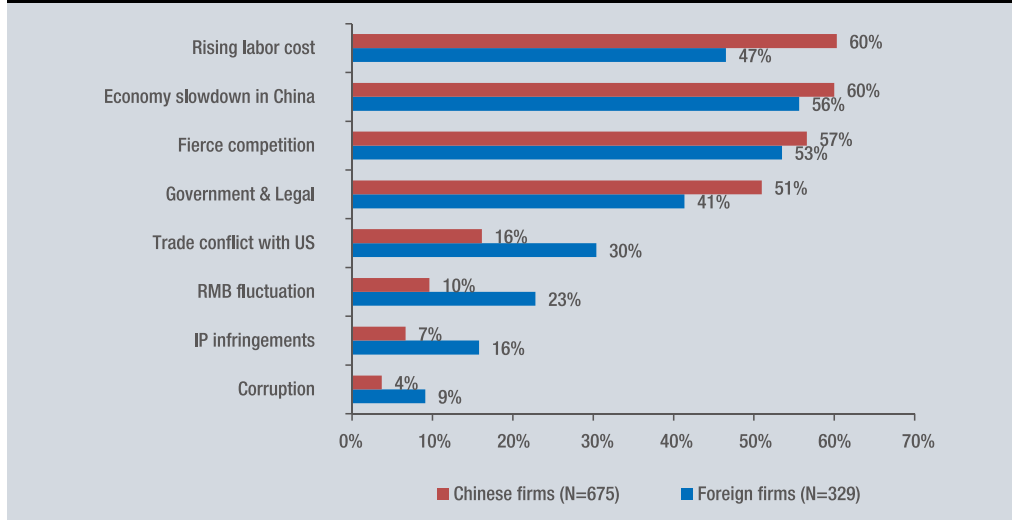
Chinese firms – Top 4 External Challenges

	2019 Survey	2015 Survey
1	Rising labor cost (60%)	Fierce competition (64%)
2	Economy slowdown in China (60%)	Rising labor cost (62%)
3	Fierce competition (57%)	Economy slowdown in China (53%)
4	Government & Legal environment (51%)	Government & Legal environment (31%)

Foreign firms – Top 4 External Challenges

	2019 Survey	2015 Survey
1	Economy slowdown in China (56%)	Fierce competition (62%)
2	Fierce competition (53%)	Rising labor cost (57%)
3	Rising labor cost (47%)	Economy slowdown in China (54%)
4	Government & Legal environment (41%)	Government & Legal environment (39%)

FIGURE 23 - 2019 SURVEY: WHAT ARE THE GREATEST EXTERNAL CHALLENGES FACING YOUR COMPANY IN CHINA?



We observe some differences when comparing Chinese State-owned firms, Chinese private firms and foreign firms. In particular, “economy slowdown in China” seems to affect more the SOEs than the private companies in our sample and “Rising labor costs” is a pressing issue for more Chinese private companies than SOEs or WFOEs.

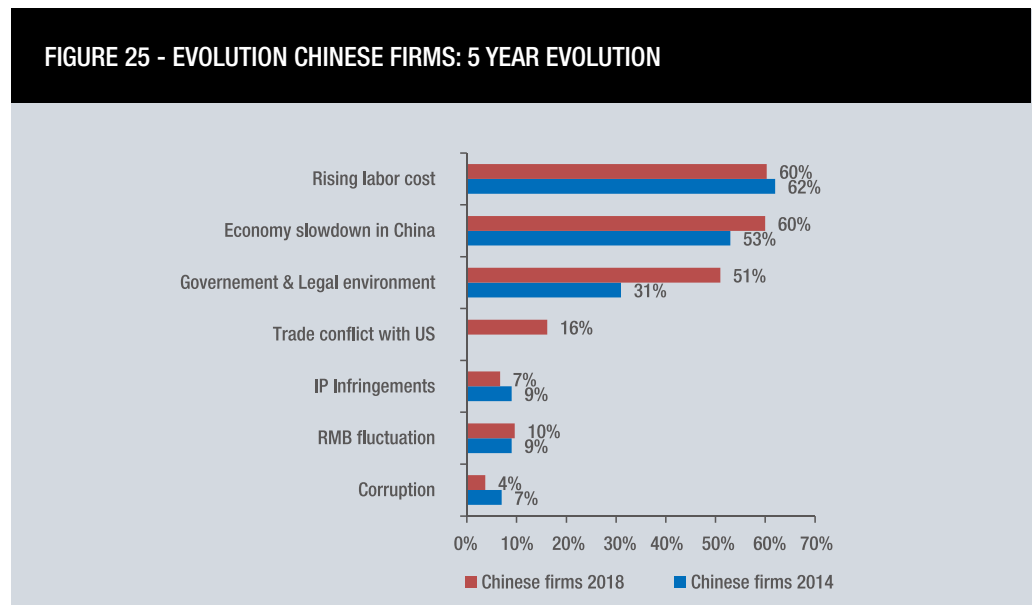
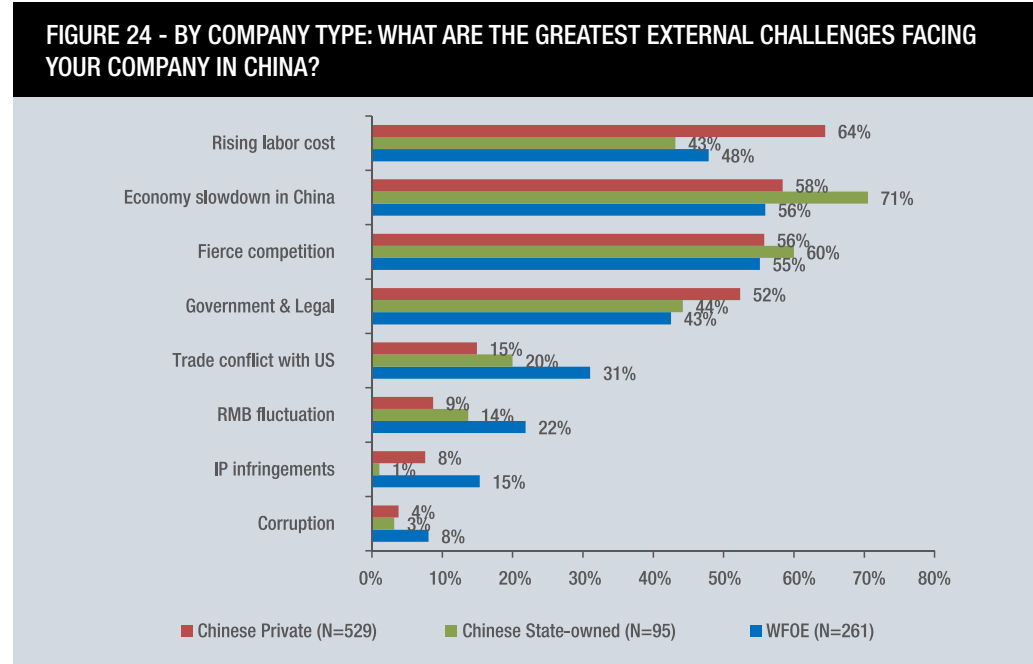
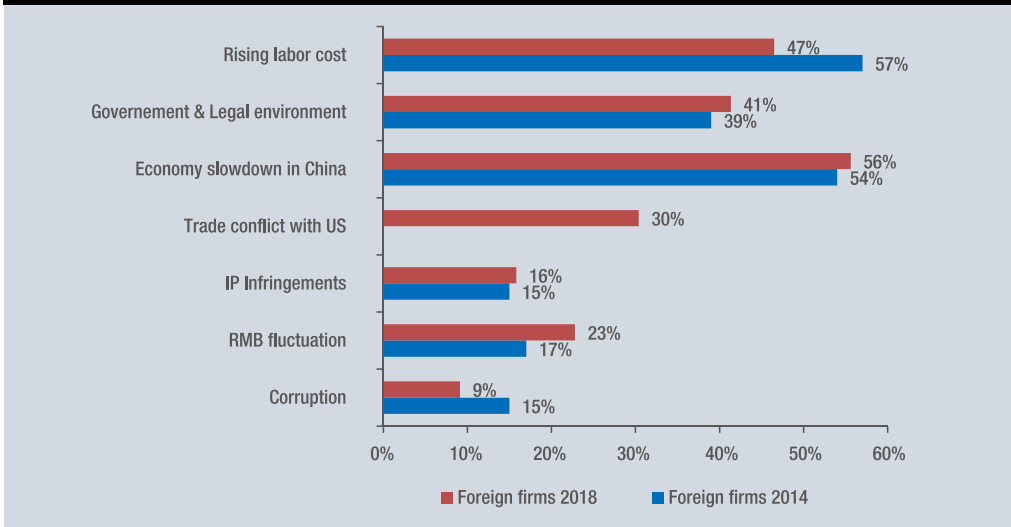


FIGURE 26 - EVOLUTION FOREIGN FIRMS: 5 YEAR EVOLUTION



3.2. INTERNAL CHALLENGES

Three top internal challenges are shared by both Chinese and foreign owned firms and remain unchanged from previous years' polls: Finding and retaining talent, innovation, and marketing capabilities.

The Top 3 internal challenges of Chinese and foreign firms in our sample remain unchanged over the last five years: "Finding and retaining talent" (65% of them), "Innovation Capability" (50% of them), and "Marketing Capability" (42% of them). The 4th challenge on the top list differs for both groups. "Corporate governance" is a concern relatively more prevalent in Chinese firms with 41% of the executives working them selecting it vs. a lower 29% of those working for foreign companies. This effect is consistent with previous editions of this survey. On the other hand, for executives working for foreign-owned companies "Support from Head Office" is one of the top issues more frequently mentioned, cited by 36% of them (vs. a much lower 9% of Chinese firms). This is also consistent with previous polls and with the physical and cultural distance with their global headquarters.

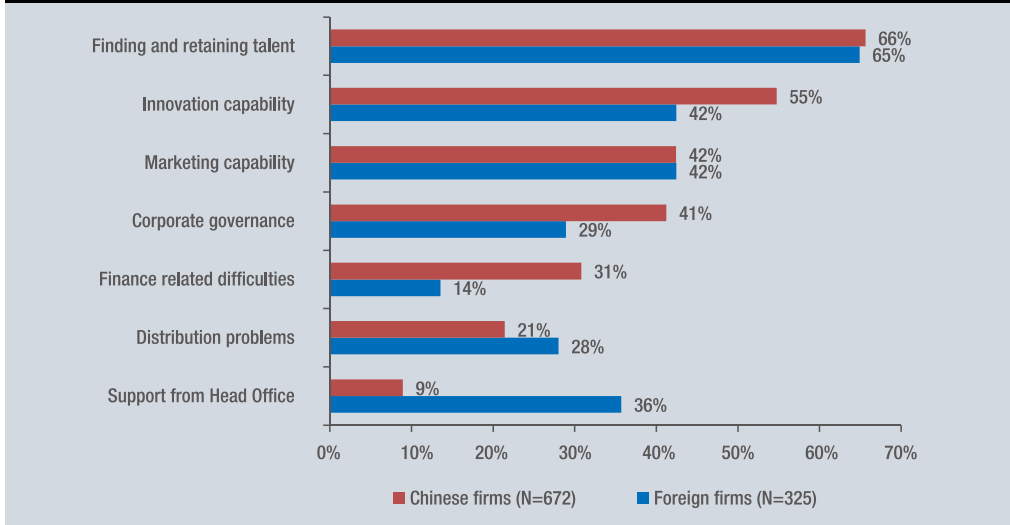
Chinese firms – Top 4 Internal Challenges

	2019 Survey	2015 Survey
1	Finding and retaining talent (66%)	Finding and retaining talent (61%)
2	Innovation capability (55%)	Innovation capability (51%)
3	Marketing capability (42%)	Marketing capability (40%)
4	Corporate governance (41%)	Corporate governance (36%)

Foreign firms – Top 4 Internal Challenges

	2019 Survey	2015 Survey
1	Finding and retaining talent (65%)	Finding and retaining talent (58%)
2	Innovation capability (42%)	Marketing capability (36%)
3	Marketing capability (42%)	Innovation capability (35%)
4	Support from Head Office (36%)	Support from Head Office (26%)

FIGURE 27 - 2019 SURVEY: WHAT ARE THE GREATEST INTERNAL CHALLENGES FACING YOUR COMPANY IN CHINA?



Another group-specific challenge is “Finance related difficulties” which worries 34% of the Chinese private firms vs. a much lower 19% of SOEs and 12% of foreign firms. Innovation capability is a top concern for 69% of the Chinese state-owned companies, contrasting with a lower 52% of Chinese private companies and 45% of WFOEs.

FIGURE 28 - BY COMPANY TYPE: WHAT ARE THE GREATEST INTERNAL CHALLENGES FACING YOUR COMPANY IN CHINA?

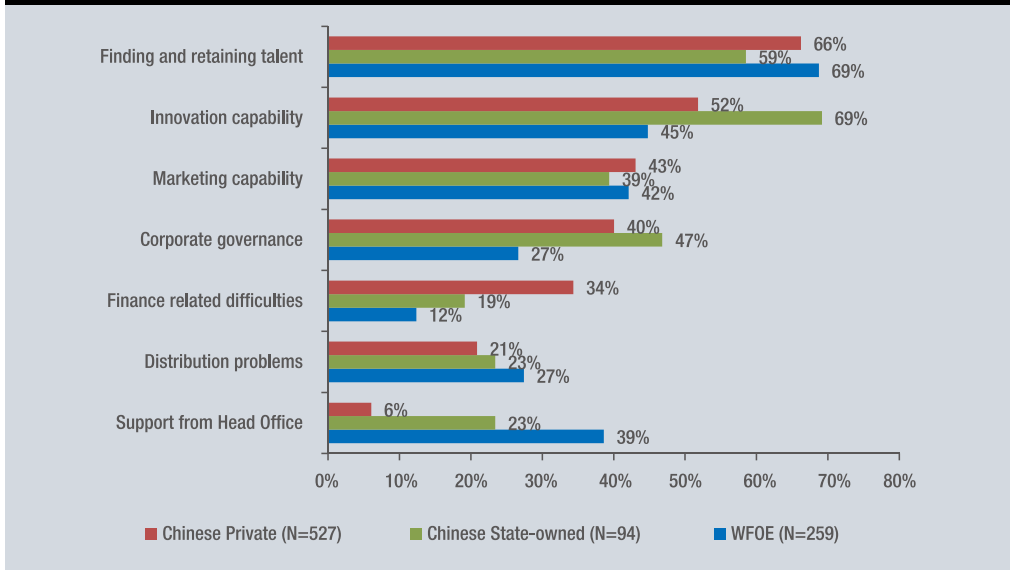
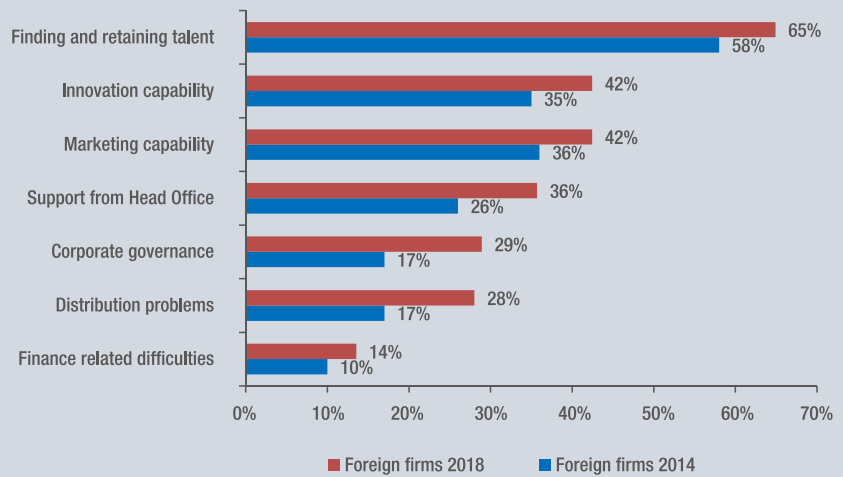


FIGURE 29 - EVOLUTION CHINESE FIRMS: 5 YEAR EVOLUTION



FIGURE 30 - EVOLUTION FOREIGN FIRMS: 5 YEAR EVOLUTION



3.3. SUCCESS FACTORS

Product and service quality and the ability to control costs are key success factors in the current economy. Brand creation and product innovation follow closely.

Both executives from Chinese and foreign-owned companies in our sample believe that success in China is linked to product and service quality superiority. Chinese firms select cost control and operations efficiency in second position and the capacity to innovate in third position. Foreign companies give slightly more importance to brand awareness and creation, although it is followed closely by cost control. The fierce competition in the current economy forces companies in China to be careful with their operating expenses if they want to survive and be profitable.

Soft factors such as company culture & values also make the Top 4 Success Factors in the 2018 survey. “Employee selection and training”, although not in the Top 4 lists, stands out as a factor more frequently considered key to success by foreign companies than by Chinese companies, 26% of foreign firms vs. 18% of Chinese firms.

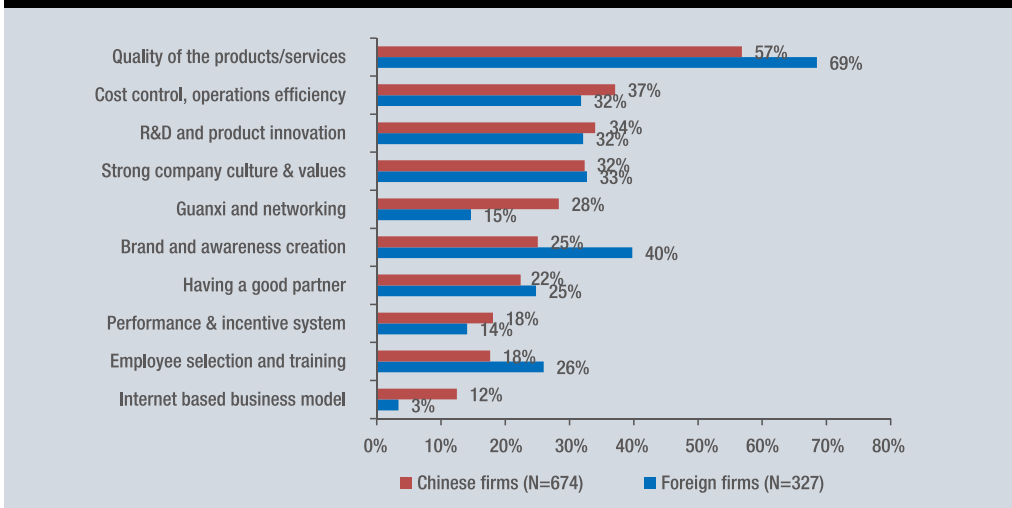
Chinese firms – Top 4 Success Factors

	2019 Survey	2015 Survey
1	Quality of the products/services (57%)	Quality of the products/services (55%)
2	Cost control, operations efficiency (37%)	Strong company culture & values (45%)
3	R&D and product innovation (34%)	Quality of the management team (44%)
4	Strong company culture & values (32%)	R&D and product innovation (42%)

Foreign firms – Top 4 Success Factors

	2019 Survey	2015 Survey
1	Quality of the products/services (69%)	Quality of the products/services (68%)
2	Brand and awareness creation (40%)	Brand and awareness creation (48%)
3	Strong company culture & values (33%)	Quality of the management team (46%)
4	Cost control, operations efficiency (32%)	Cost control, operations efficiency (44%)

FIGURE 31 - 2019 SURVEY: WHAT ARE THE MOST IMPORTANT FACTORS FOR YOUR COMPANY'S SUCCESS IN CHINA?



When analyzing success factors by type of industry, some differences are revealed: According to our sample of surveyed companies, cost control and operations efficiency is considered a success factor more often for companies operating in the Energy sector (51% of them). R&D and product innovation are key concerns for companies in Technology & telecom and Healthcare (51% and 41% of them respectively).

FIGURE 32 - BY INDUSTRY: WHAT ARE THE MOST IMPORTANT FACTORS FOR YOUR COMPANY'S SUCCESS IN CHINA?

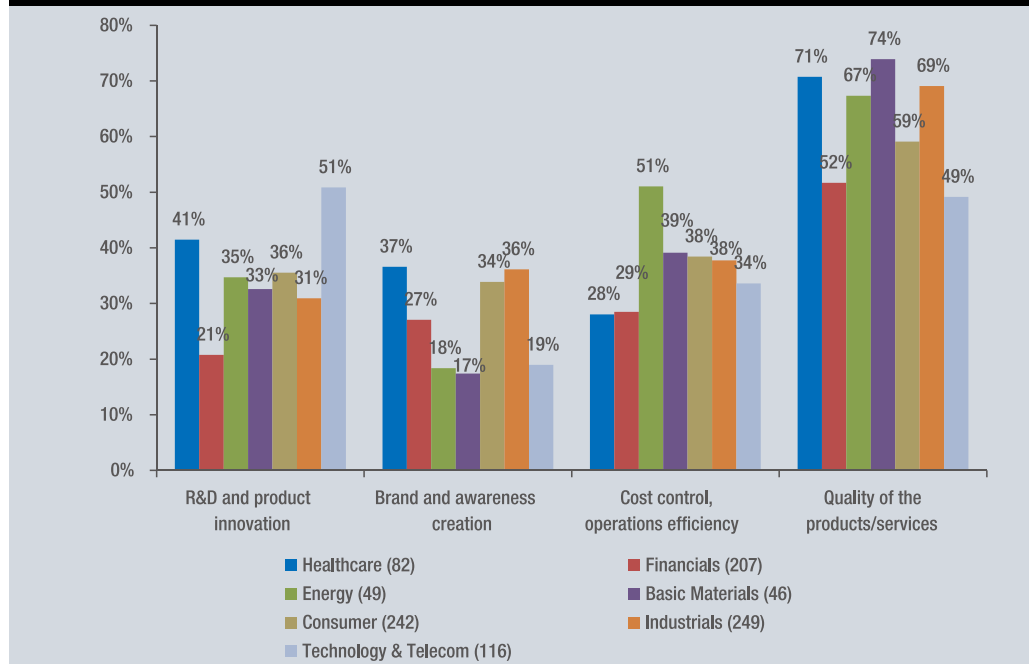


FIGURE 33 - EVOLUTION CHINESE FIRMS: 5 YEAR EVOLUTION

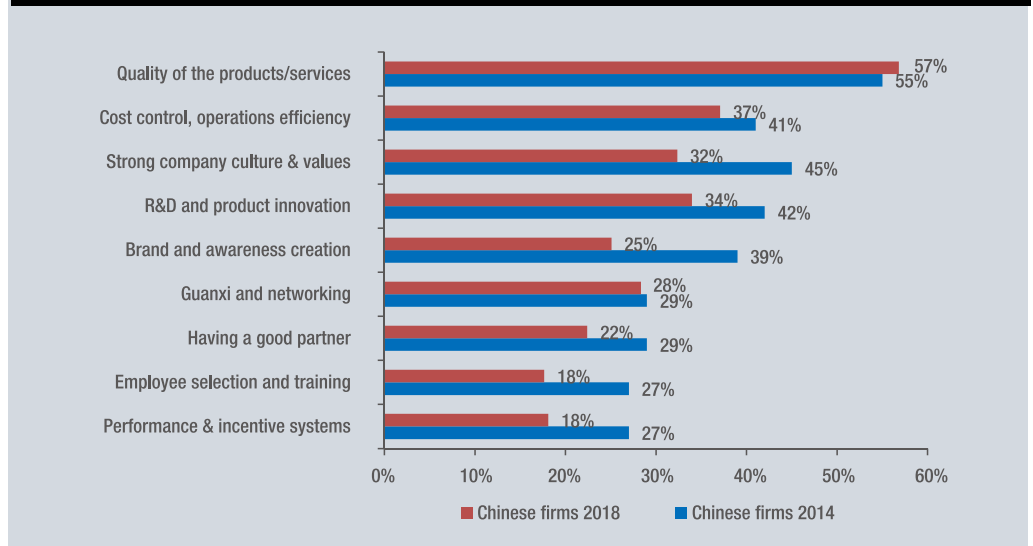
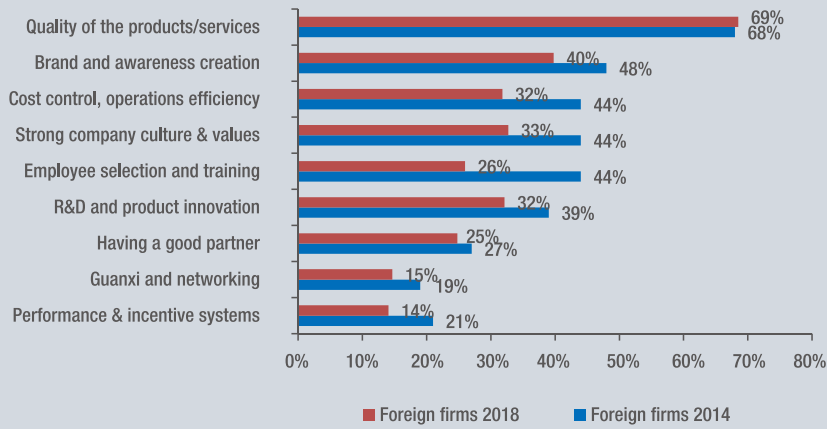


FIGURE 34 - EVOLUTION FOREIGN FIRMS: 5 YEAR EVOLUTION





SECTION 4

FOCUS BY AREA

This section gives an overview of the following topics:

■ Human Resources

The chapter covers the top HR issues that companies in our sample face in China. It also gives a commentary on what the executives in our sample think are the most effective measures to retain employees.

■ Sales and Marketing

This chapter describes the competitive landscape and includes an overview of the market segments where companies in our sample operate. It also details which are the most effective sales and marketing strategies for the companies in our sample.

■ Research & Development

This chapter presents a summary of main learning's on R&D trends from our sample of surveyed companies.

■ Government and Legal Environment

This chapter discusses the perceived important of establishing relationships with the Chinese government as well as polled executives' outlook on corruption in their industries and in general.

4.1. HUMAN RESOURCES

Labor force increased in 2018 for 56% of the sample, a lower proportion of companies than last year (64%), however in line with the earlier editions of this survey. Chinese private companies and firms in rapidly growing sectors (Healthcare, Technology & Telecom) lead the workforce expansion. Finding talent and rising labor costs are cited as the top HR issues for managing businesses in China. Developing a feeling of belonging to the company is cited most often as a key to retain employees by private companies, whereas SOE companies rely more often on offering a good career path to their employees.

4.1.1. Change in labor force, employee turnover and salary increase in 2018

More than half of the surveyed sample has increased their labor force in 2018, 56% of total firms. However, and in line with the more cautious attitude towards the Chinese economy of our sample in 2018 (see Section 2.1 of this report), the proportion of companies increasing their labor force is lower than in the previous year: 53% of Chinese SOE, 57% of Chinese private and 51% of foreign firms (vs. 67%, 69% and 58%, respectively in 2017).

Analyzing the data by industry, we discover that it is firms in Healthcare that have proportionally increased their labor force the most in 2018, with 72% of them expanding in number of employees. Also, in line with the economy transformation of China, we note that 59% of firms dealing with services increased labor force in 2018 compared to a lower 49% of firms in the manufacturing side of their industries.

In terms of salary increase and employee turnover, it is Chinese private companies that show the highest numbers, when compared with Chinese SOEs or foreign companies.

FIGURE 35 - BY LEGAL STATUS - THE CHANGE IN YOUR COMPANY LABOR FORCE IN 2018 VS. 2017 IS

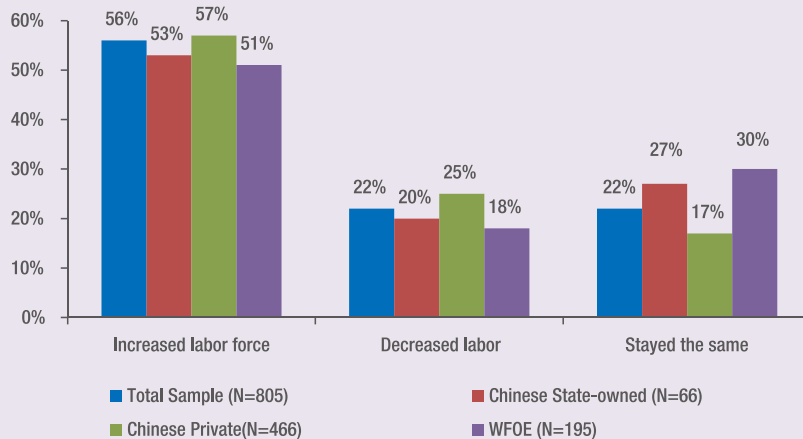


FIGURE 36 - BY INDUSTRY - THE CHANGE IN YOUR COMPANY LABOR FORCE IN 2018 VS. 2017 IS:

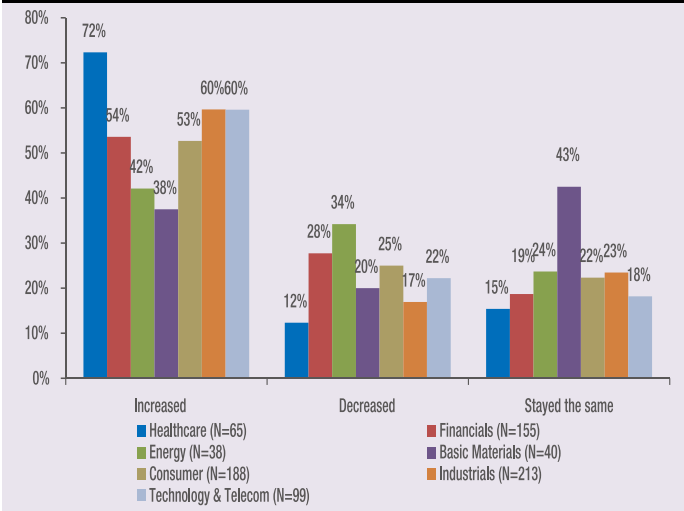


FIGURE 37 - BY SECTOR - THE CHANGE IN YOUR COMPANY LABOR FORCE IN 2018 VS. 2017 IS:

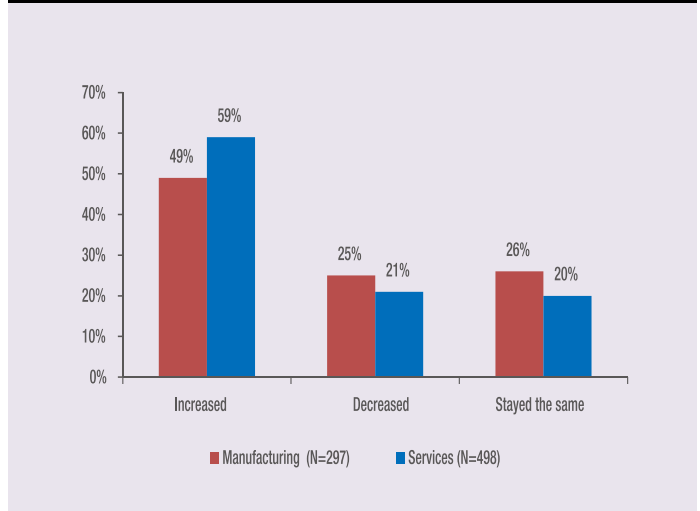


FIGURE 38 - THE TOTAL SALARY INCREASE IN 2018 COMPARED TO 2017 IS:

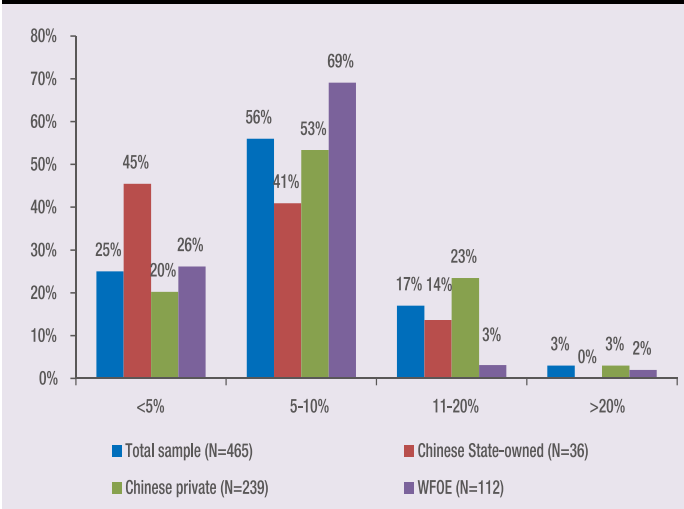
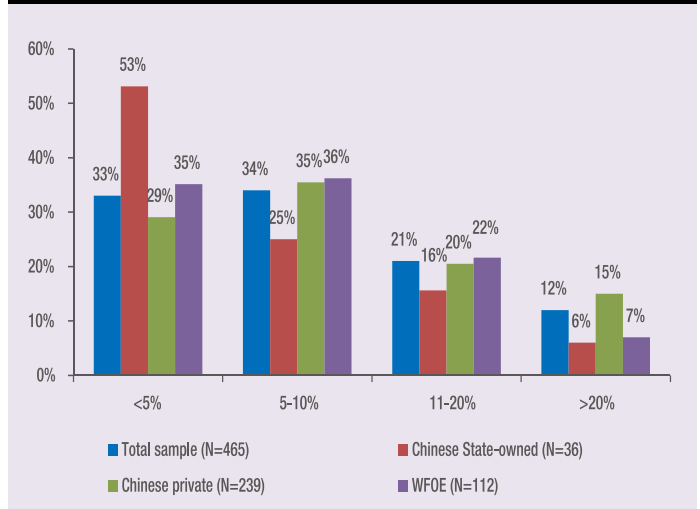


FIGURE 39 - THE TOTAL EMPLOYEE TURNOVER IN 2018 COMPARED TO 2017 IS:



4.1.2. Top Human Resources issues in China

Consistent with previous years, “Finding and hiring suitable talent”, “Rising labor costs” and “Generating commitment and loyalty” are the top HR concerns for surveyed Chinese and foreign companies. Foreign firms and Chinese private firms have more issues finding and retaining talent than SOEs (84% of foreign firms and 81% of Chinese private firms, vs. 76% of SOEs and declare issues in hiring suitable talent). The differences by industry are captured in the chart below.

FIGURE 40 - BY COMPANY TYPE: WHICH ARE THE MAJOR HUMAN RESOURCES ISSUES FACING YOUR COMPANY IN CHINA?

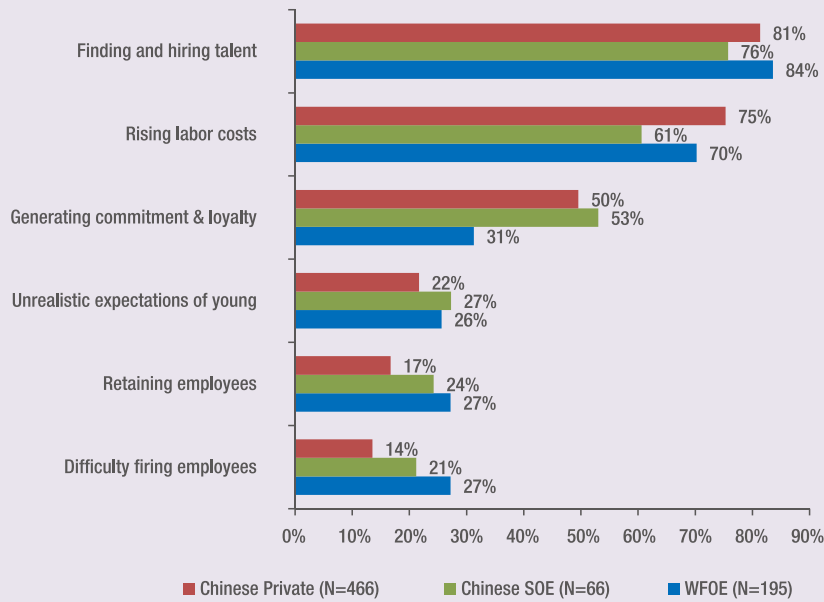
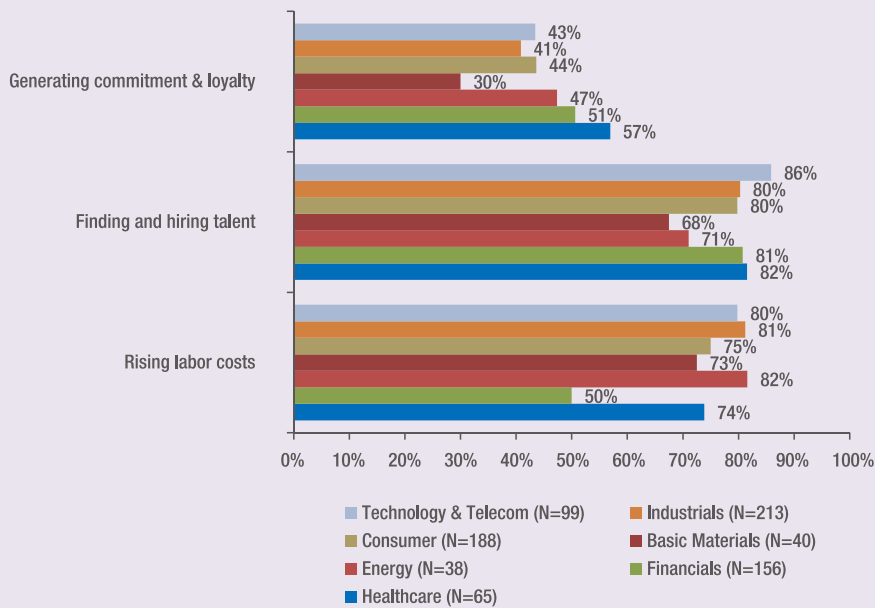
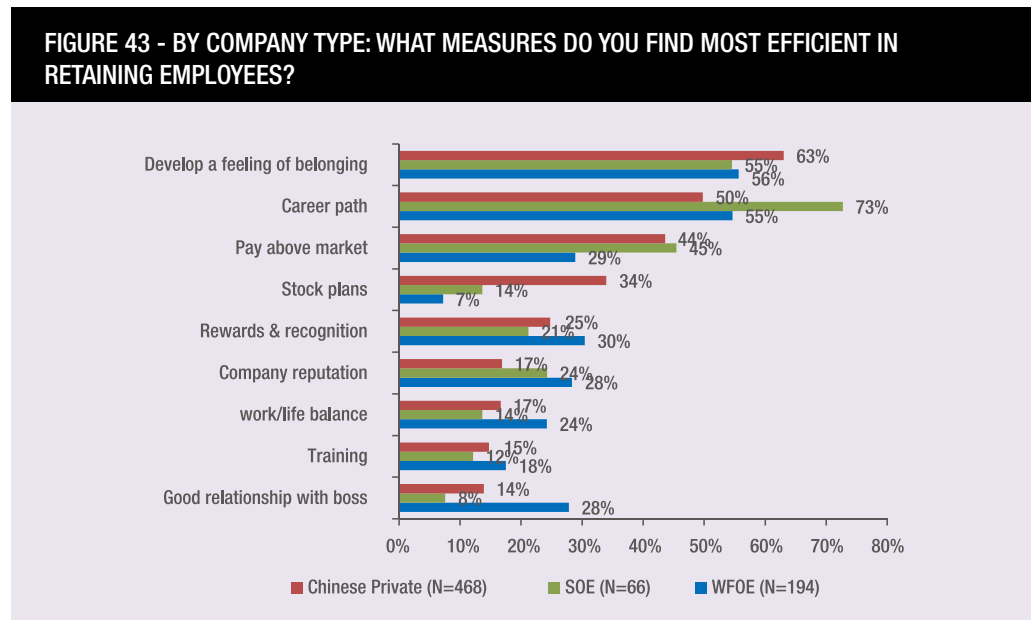
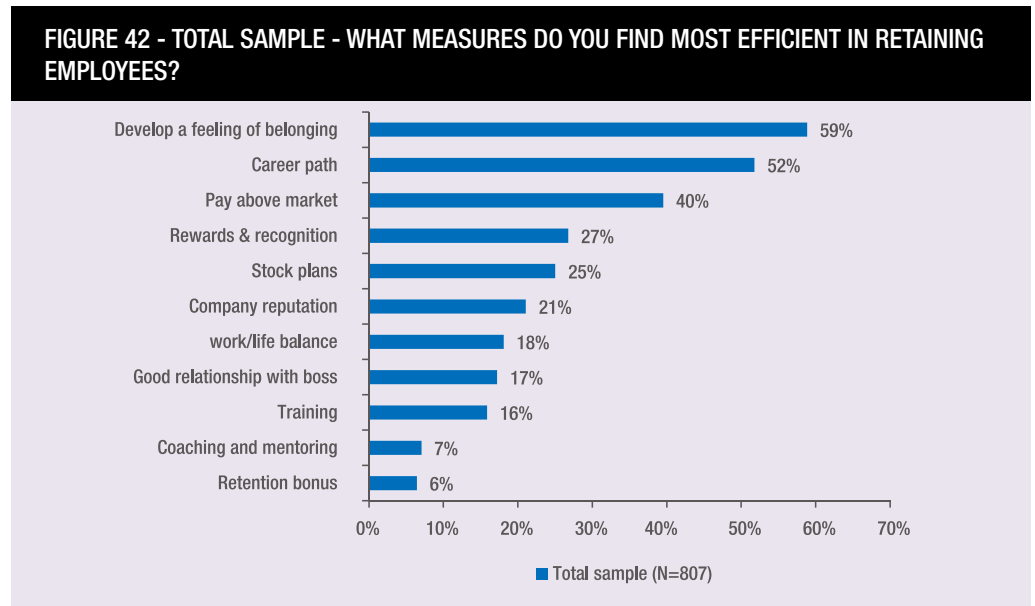


FIGURE 41 - BY INDUSTRY: WHICH ARE THE MAJOR HUMAN RESOURCES ISSUES FACING YOUR COMPANY IN CHINA?



4.1.3. Most effective measures to retain employees

In terms of most efficient measures to retain employees, “Develop a feeling of belonging to the company” is cited as most efficient measure by 59% of the total sample, followed by “Offering good career path” (52% of the sample). Both sets of measures come before salary as “Pay above market” is cited by a lower 40% of sampled companies. However, when observing according to type of company, we note that “offering a good career path” is a strategy particularly relevant for SOEs, much more than for Chinese private firms or foreign firms. The differences in the relative weight of some of the strategies between types of firms are captured in the chart below.



4.2. SALES AND MARKETING

4.2.1. Competition

87% of Chinese firms and 88% of foreign firms polled consider the competition in China to be intense or very intense, which is consistent with competition being a top external challenge faced by our sample of companies (Section 3.1).

A majority of respondents cited their main competitors to be Chinese private enterprises (80% of Chinese firms and 67% of foreign firms). Chinese-owned respondents cite state-owned enterprises as a distant second (44%). In contrast, foreign companies measure themselves also amongst each other, citing WFOE (57%) as their second major type of competitor. These results are consistent with previous editions of this survey.

The top strengths of foreign firms according to their Chinese competitors are related to their capability to create brands, the superiority of their products and their technology. In contrast, foreign-owned firms perceive that their main weaknesses vis-à-vis their Chinese competitors lay in Chinese firms' superiority in "Cost advantages", "Price", and "Relationships with Government and other guanxi".

FIGURE 44 - HOW INTENSE IS THE COMPETITION YOU ARE FACING IN CHINA?

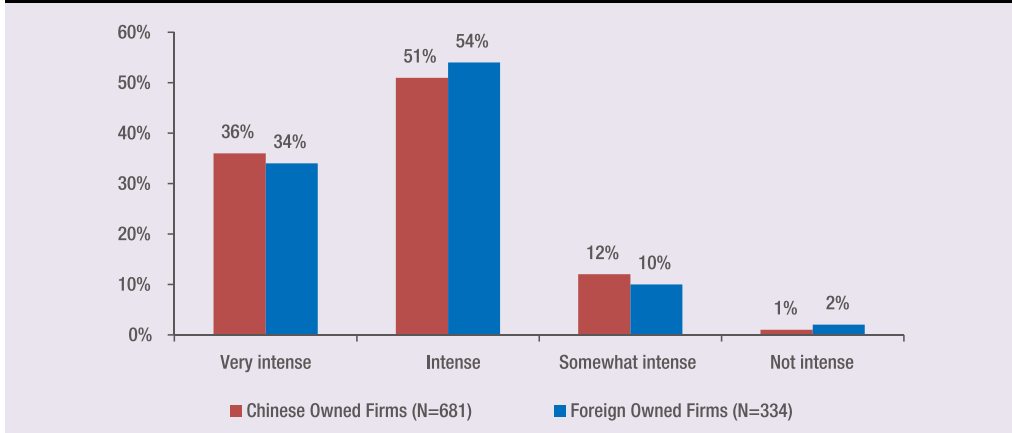


FIGURE 45 - WHO ARE YOUR MAIN COMPETITORS IN CHINA? MULTIPLE ANSWERS

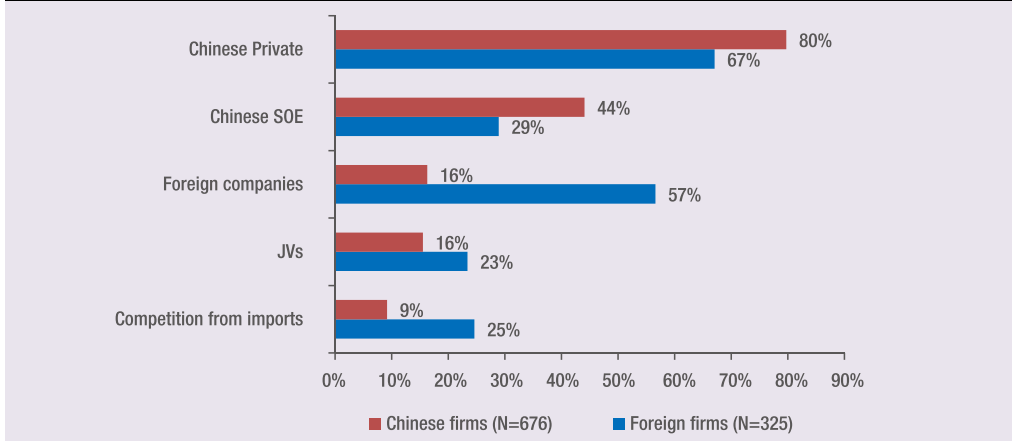


FIGURE 46 - BY INDUSTRY - HOW INTENSE IS THE COMPETITION YOU ARE FACING IN CHINA?

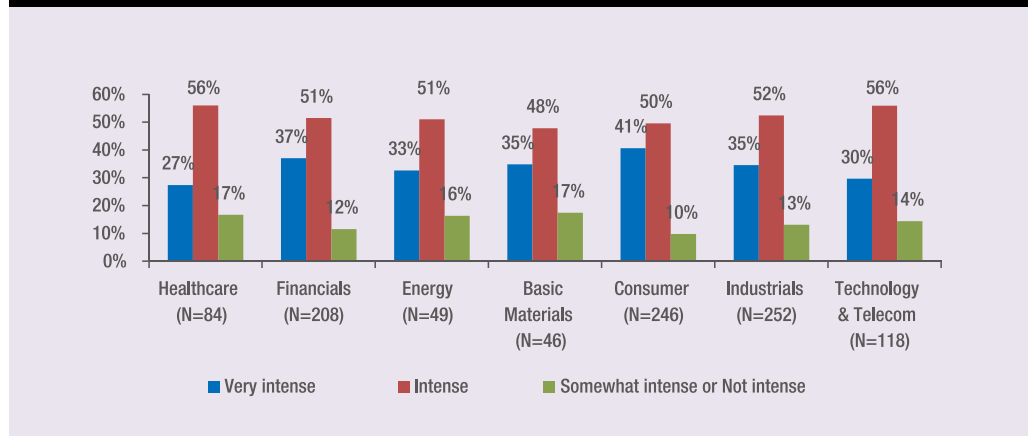


FIGURE 47 - WHAT ARE THE COMPETITIVE ADVANTAGES OF YOUR MAIN FOREIGN COMPETITORS IN CHINA? MULTIPLE ANSWERS

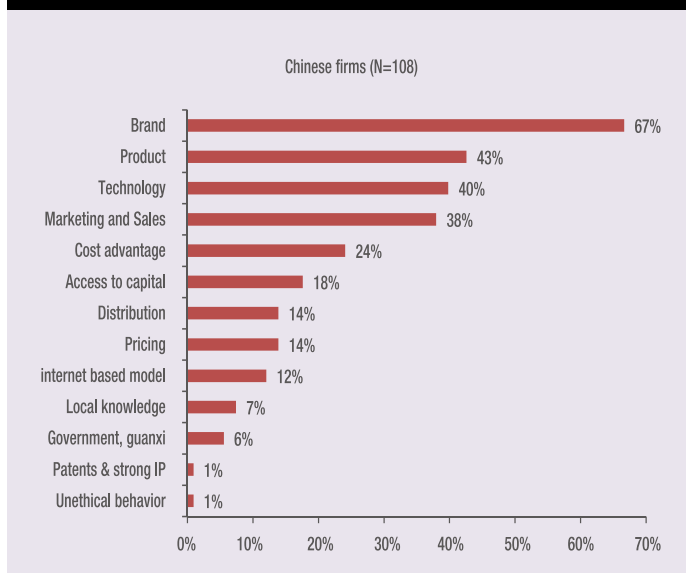
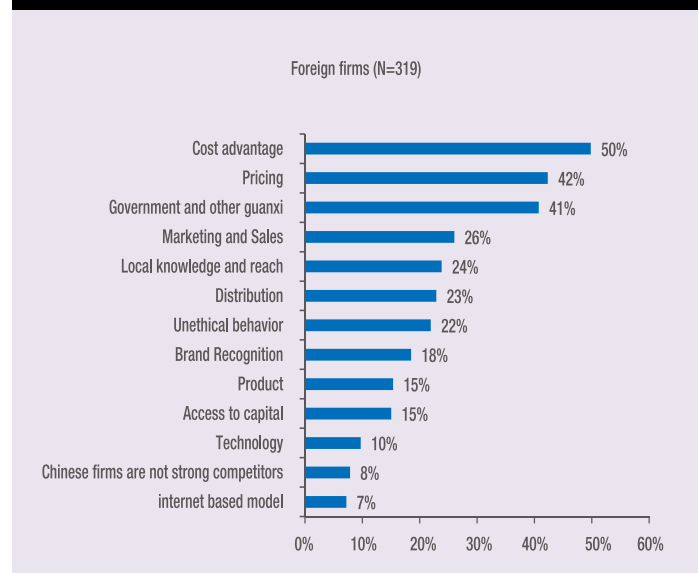


FIGURE 48 - WHAT ARE THE COMPETITIVE ADVANTAGES OF YOUR MAIN CHINESE COMPETITORS IN CHINA? MULTIPLE ANSWERS



4.2.2. Market segments and mobility

Our sample of companies operates mainly in the premium and middle segments with 50% and 46% of companies respectively, and only a small 4% in the low-end. The foreign firms sample is more skewed towards high end markets than the Chinese sample: 77% of foreign firms declare to operate in the premium market vs. 38% Chinese firms. In terms of segment mobility, we see that even if a majority of companies plan to grow future sales within their existing segment, there is still a significant amount of companies that plan to grow outside of their current segment. This trend is stronger for companies in the lowest segment of the market.

FIGURE 49 - WHICH IS YOUR MAIN MARKET SEGMENT IN CHINA?

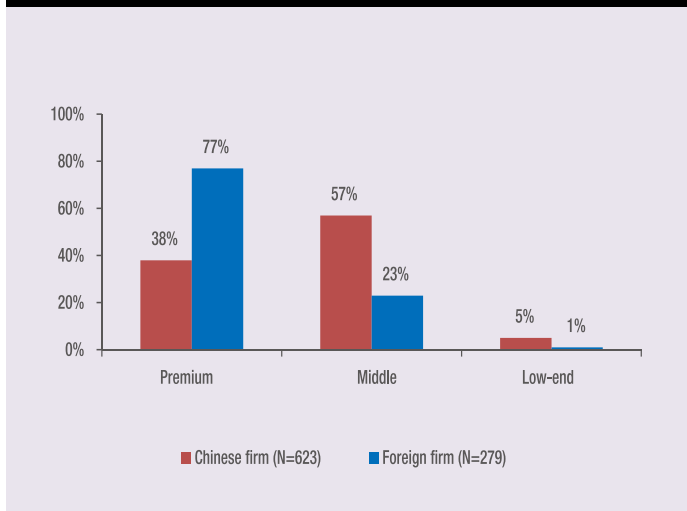
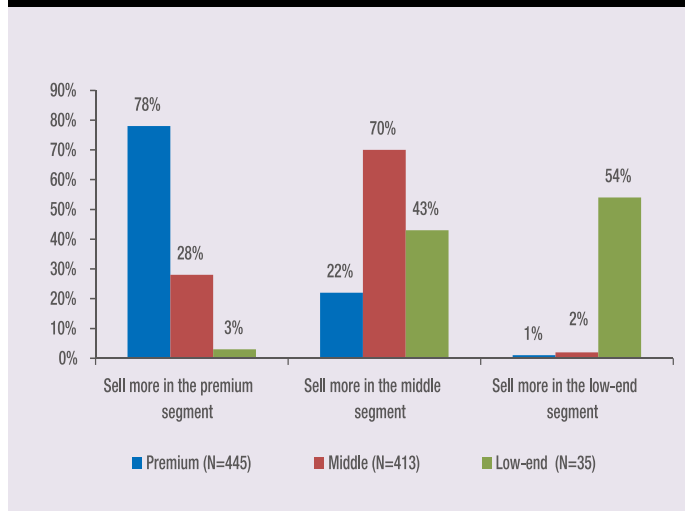


FIGURE 50 - WHAT ARE YOUR PLANS FOR THE FUTURE?



4.2.3. Marketing, Sales and Distribution strategies

Marketing & Sales spending: There is no significant difference in marketing and sales spending for Chinese owned and foreign-owned firms and they show similar intentions regarding their investments in the coming year. B2C firms in our sample dedicate more important budgets to marketing and sales activities than B2B firms.

In terms of industry, Healthcare seems to be the largest investor with 59% of sampled firms spending above 10% of yearly revenues in marketing and sales, followed by firms in the Consumer goods and services sector (38% of them) and financial companies (35%). Companies operating in the medium and low-end segments of the market tend to have larger marketing & sales spending than those in the premium sectors.

Sales strategies: B2B companies in our sample emphasize providing service and high quality above other factors. Executives in B2C companies consider their distribution network and service most often as a key success factor for their sales.

Marketing strategies: Most cited marketing expenditures for B2B companies in our sample are visits to clients or prospective clients, followed distantly by organizing seminars and attending conferences. In contrast, B2C firms favor mostly social media, internet marketing and traditional advertising.

Distribution network: 20% of the total sample considers their distribution network in China to be bad or very bad, 51% consider it sufficient and 29% of them label it efficient or very efficient.

FIGURE 51 - WHAT % OF YEARLY REVENUES DO YOU SPEND IN MARKETING & SALES?

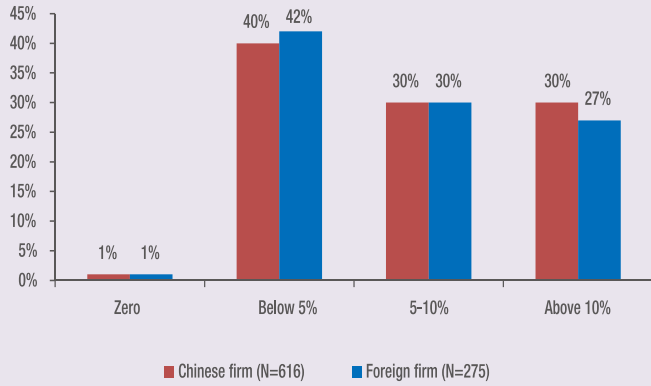


FIGURE 52 - WHAT ARE YOUR PLANS FOR NEXT YEAR?

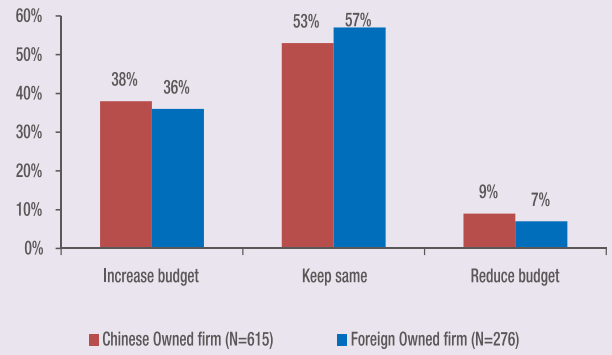


FIGURE 53 - BY B2B/B2C: WHAT % OF YEARLY REVENUES DO YOU SPEND IN MARKETING & SALES?

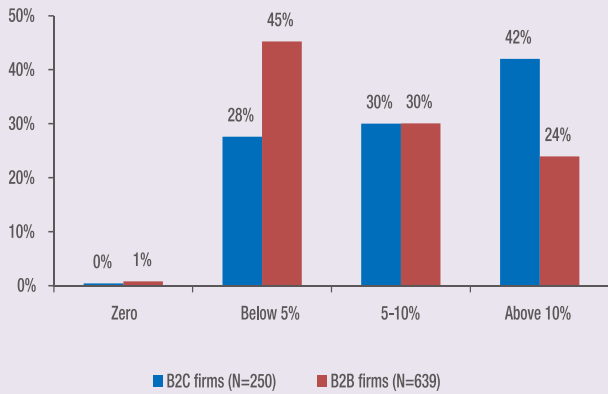


FIGURE 54 - WHAT ARE YOUR PLANS FOR NEXT YEAR?

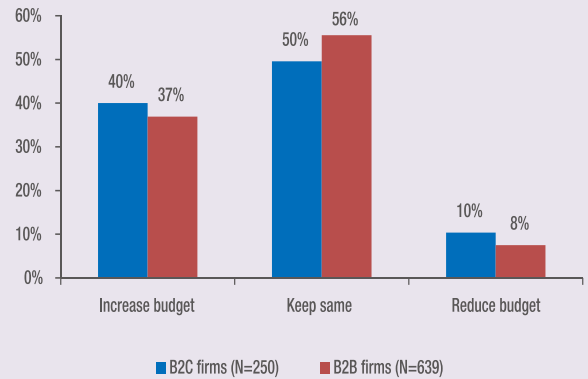


FIGURE 55 - BY INDUSTRY - WHAT % OF YEARLY REVENUES DO YOU SPEND IN MARKETING & SALES?

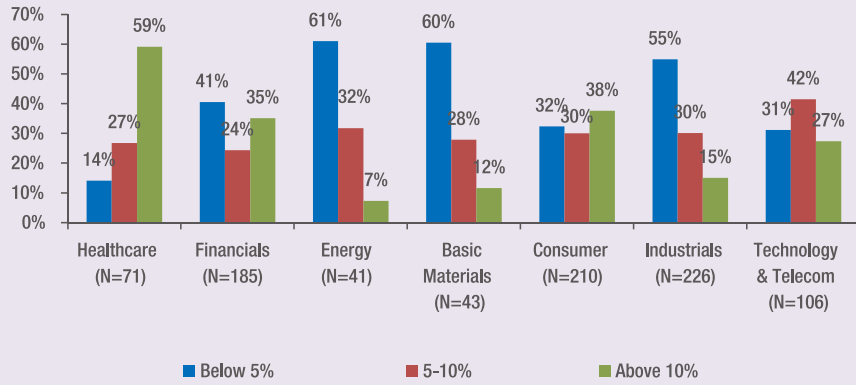


FIGURE 56 - BY MARKET SEGMENT - WHAT % OF YEARLY REVENUES DO YOU SPEND IN MARKETING & SALES?

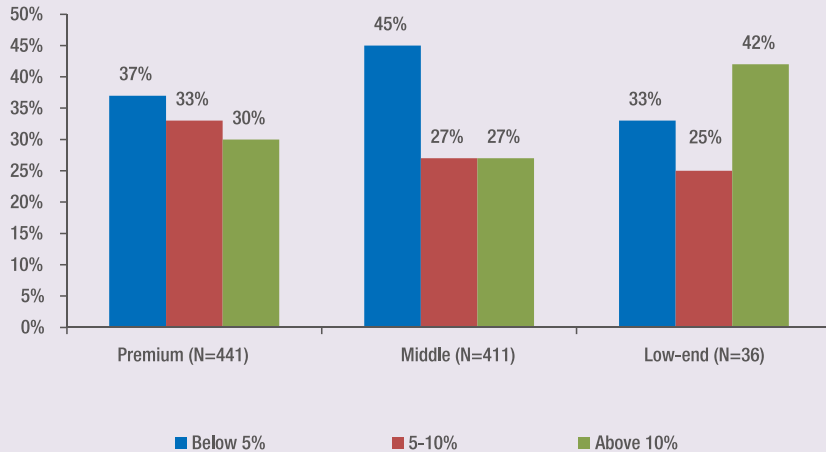


FIGURE 57 - BY B2B / B2C: PLEASE CHOOSE THE MOST IMPORTANT FACTORS ON THE SUCCESS OF YOUR SALES IN CHINA. MULTIPLE ANSWERS POSSIBLE

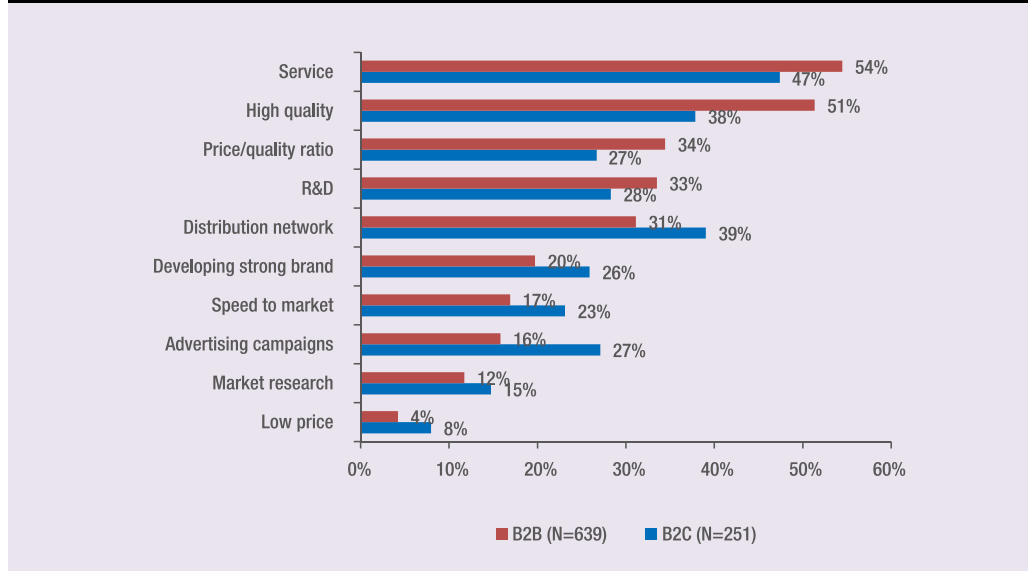


FIGURE 58 - BY B2B/B2C: WHICH MARKETING ACTIVITIES ARE MOST EFFECTIVE FOR YOUR MAIN BUSINESS?

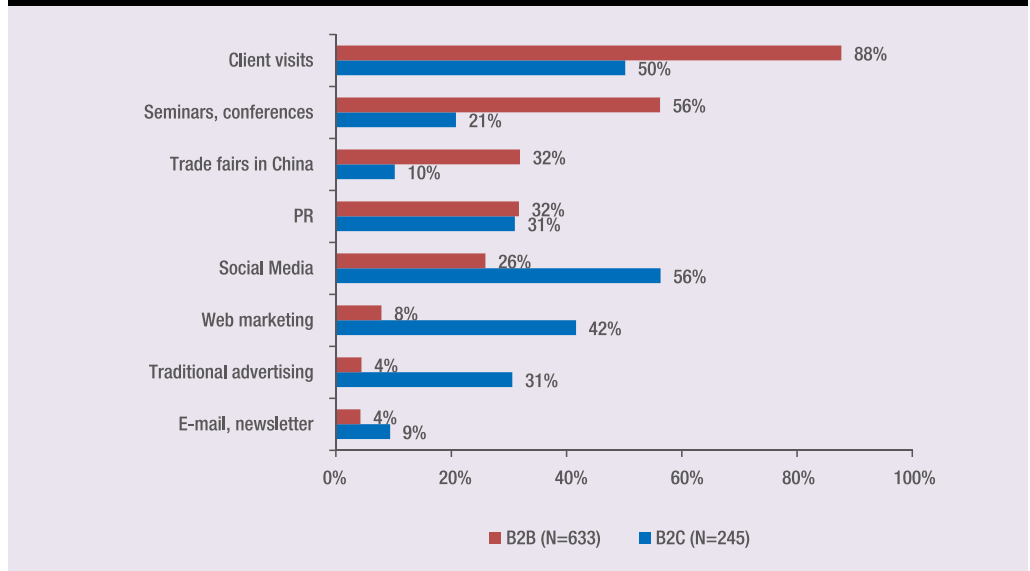


FIGURE 59 - BY MARKET SEGMENT - WHICH MARKETING ACTIVITIES ARE MOST EFFECTIVE FOR YOUR MAIN BUSINESS?

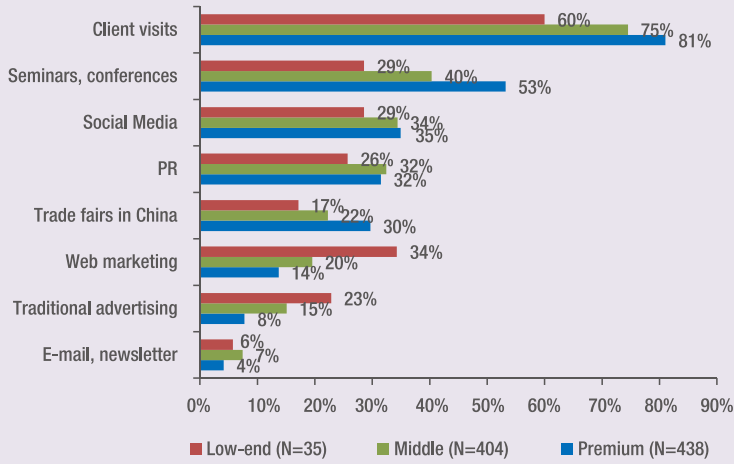


FIGURE 60 - HOW DO YOU EVALUATE YOUR COMPANY DISTRIBUTION NETWORK IN CHINA?

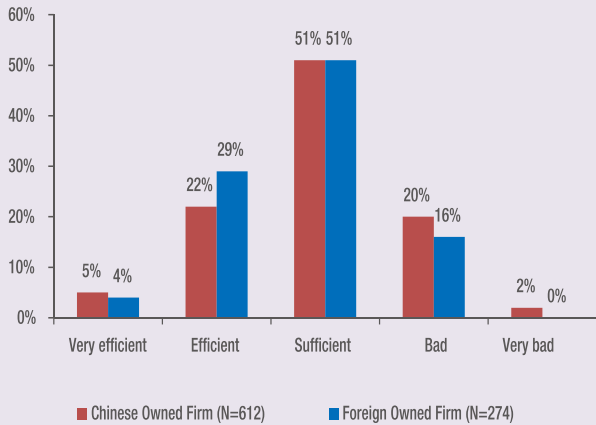


FIGURE 61 - BY B2B/B2C - HOW DO YOU EVALUATE YOUR COMPANY DISTRIBUTION NETWORK IN CHINA?

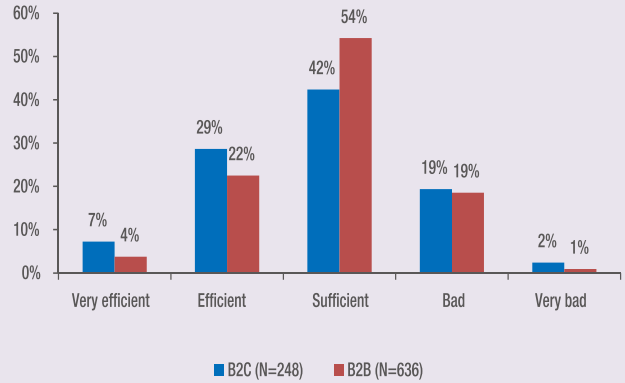


FIGURE 62 - BY MARKET SEGMENT - HOW DO YOU EVALUATE YOUR COMPANY DISTRIBUTION NETWORK IN CHINA?

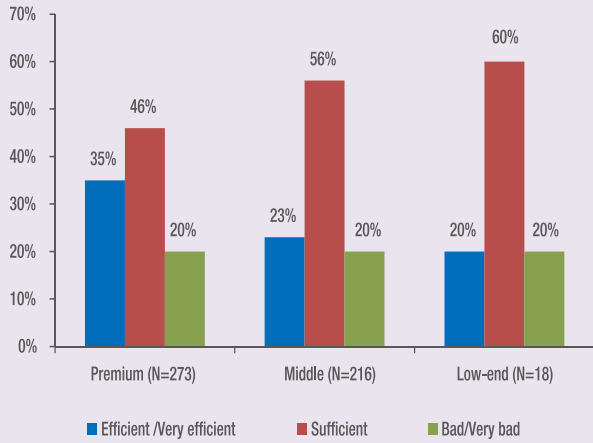


FIGURE 63 - BY INDUSTRY - HOW DO YOU EVALUATE YOUR COMPANY DISTRIBUTION NETWORK IN CHINA?

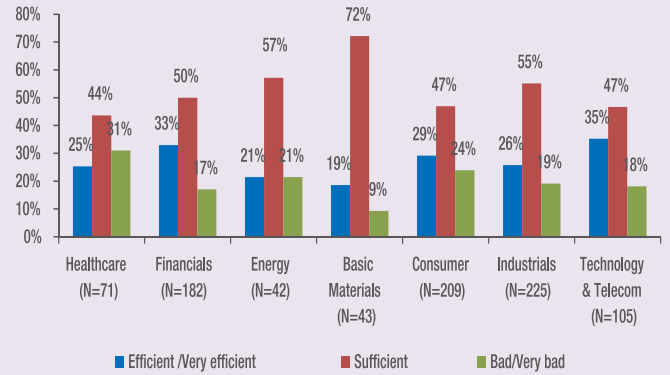


FIGURE 64 - MARKET LEADERS - WHY ARE YOU IN THAT POSITION? N=452

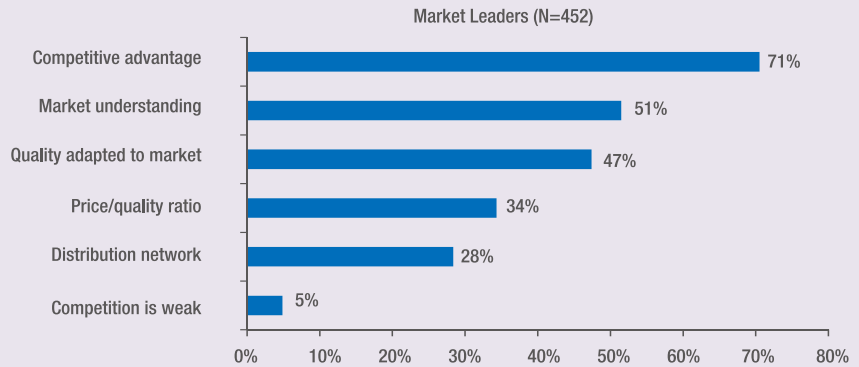
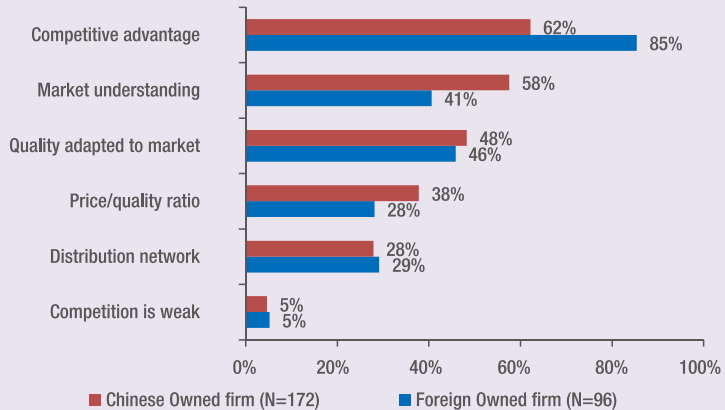


FIGURE 65 - CHINESE / FOREIGN MARKET LEADERS - WHY ARE YOU IN THAT POSITION?



4.3. RESEARCH & DEVELOPMENT

Chinese and foreign executives who participated in this year's survey report high levels of innovation for their companies as 67% of them have introduced new products or services in 2018. Introducing new managements techniques has also been a popular improvement for our sample, especially for Chinese owned firms.

Levels of R&D investment are similar for Chinese and foreign companies in our sample. However, more Chinese companies declare intention of their company to increase R&D spending in the next three years, 58% of them vs. a lower 44% of foreign firms. Within Chinese companies, it is private firms that take the lead in intention to expand R&D investment.

In terms of industry, we observe that Technology & Telecommunication have the highest percentage of "big R&D spenders" in our sample, with 73% of them, followed by Healthcare with 68% of them devoting more than 5% of their sales revenues to R&D.

FIGURE 66 - WHAT TYPES OF INNOVATIONS HAVE YOU INTRODUCED IN 2018?

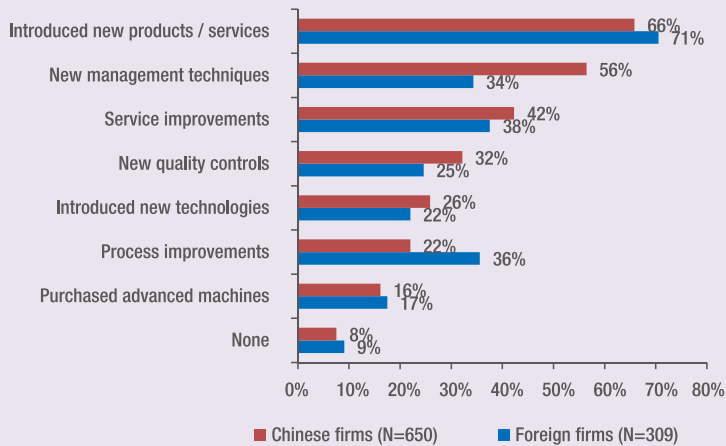


FIGURE 67 - WHAT IS YOUR ANNUAL EXPENDITURE IN R&D AS A % OF REVENUES?

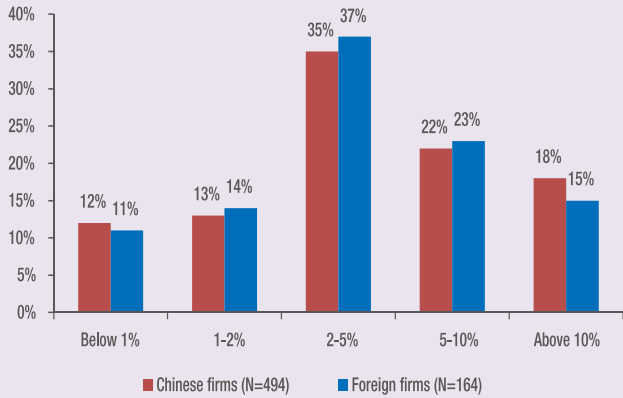


FIGURE 68 - WHAT ARE YOUR PLANS FOR THE NEXT 3 YEARS?

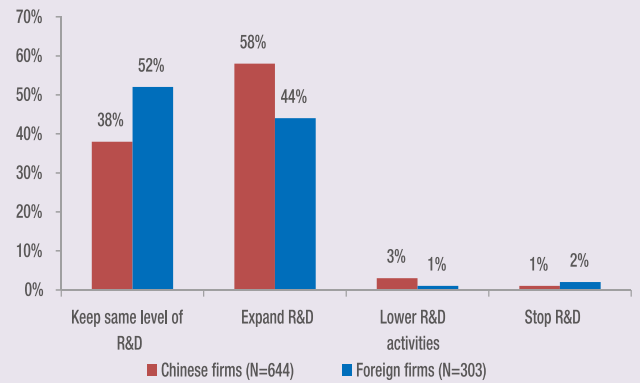


FIGURE 69 - BY COMPANY TYPE - WHAT IS YOUR ANNUAL EXPENDITURE IN R&D AS A % OF REVENUES?

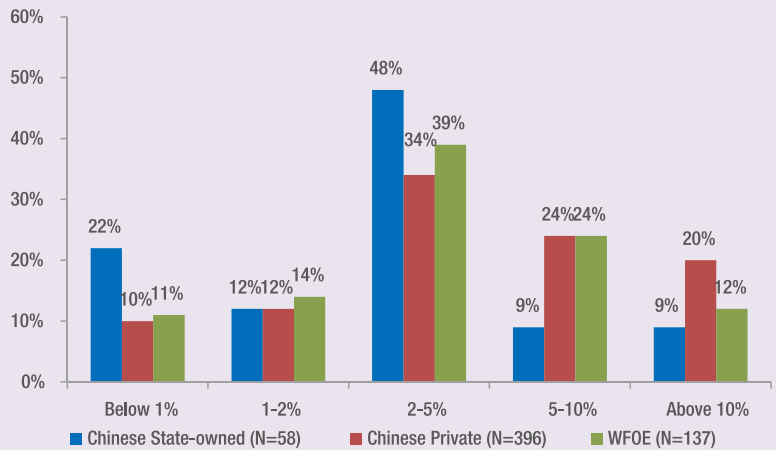


FIGURE 70 - BY COMPANY TYPE - WHAT ARE YOUR PLANS FOR THE NEXT 3 YEARS?

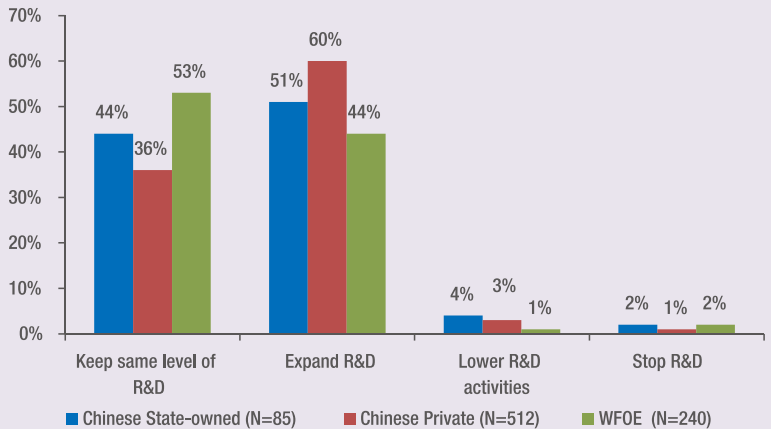


FIGURE 71 - BY INDUSTRY - HAVE YOU INTRODUCED NEW PRODUCTS OR SERVICES IN 2018?

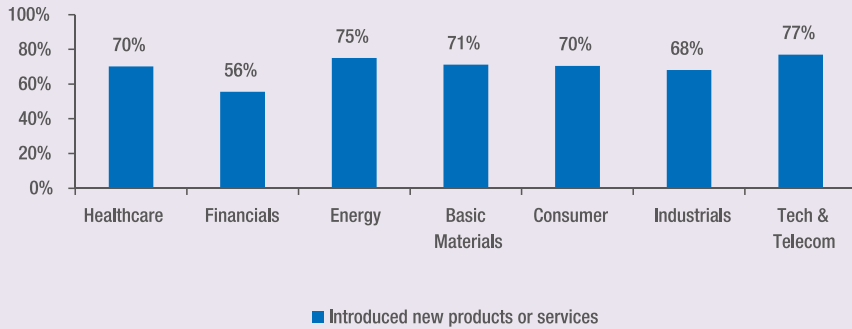


FIGURE 72 - ZOOM BY INDUSTRY: ANNUAL R&D EXPENDITURE ABOVE 5% OF SALES REVENUES

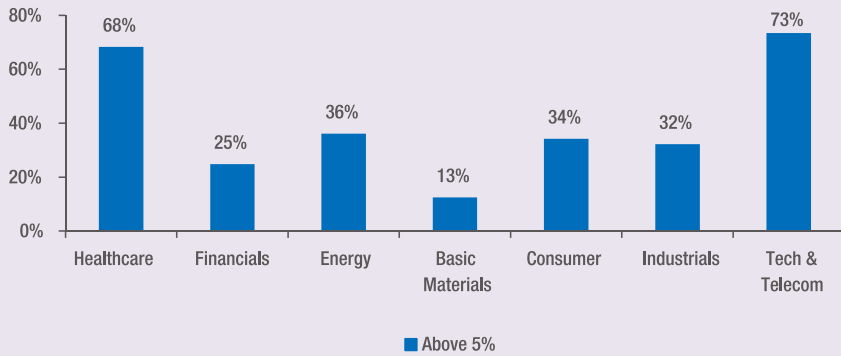
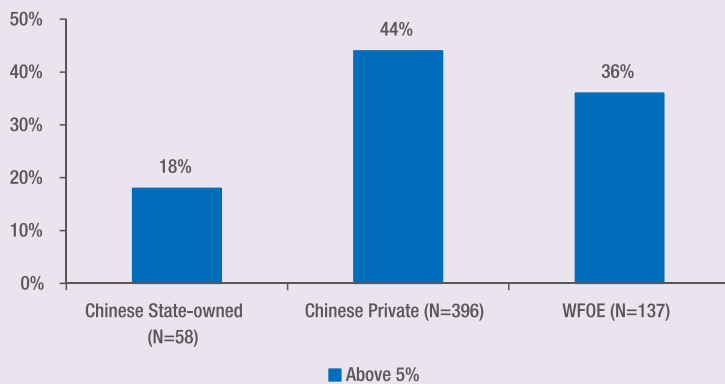


FIGURE 73 - ZOOM BY COMPANY TYPE: ANNUAL R&D EXPENDITURE ABOVE 5% OF SALES REVENUES



4.4. GOVERNMENT & LEGAL ENVIRONMENT

4.4.1. Government relationships

69% of the sample executives view the relationship with the Chinese authorities as important or very important to their businesses, regardless of whether they work for a Chinese or foreign firm. However, it is Chinese state-owned firms that emphasize most the importance of this relationship, with 53% of them labeling it critical for business success.

When analyzing by industry, we observe differences. Our polled sample would suggest that government relations may be more significant for companies operating in Financials, Energy or Healthcare, where 88%, 81% and 77% of their executives in our sample have labeled them important or critical.

FIGURE 74 - HOW IMPORTANT ARE THE RELATIONSHIPS WITH THE AUTHORITIES?

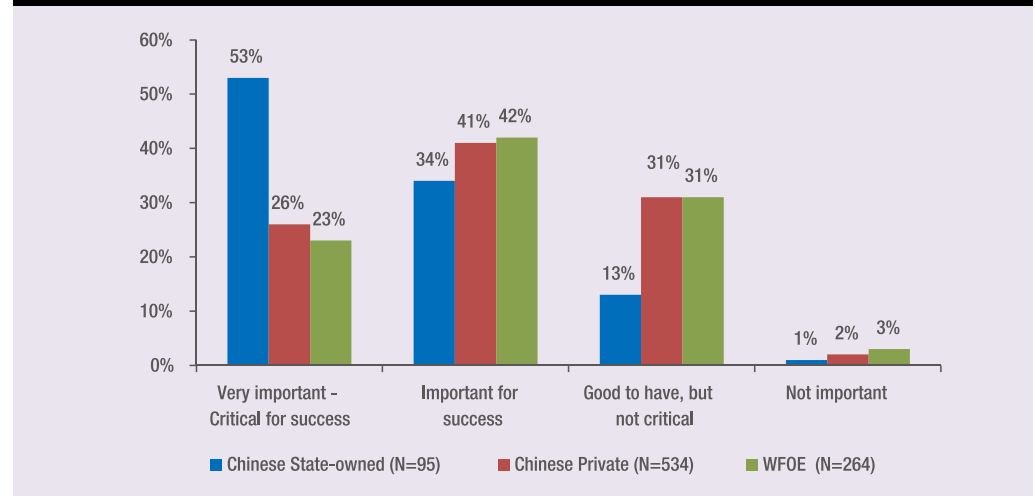
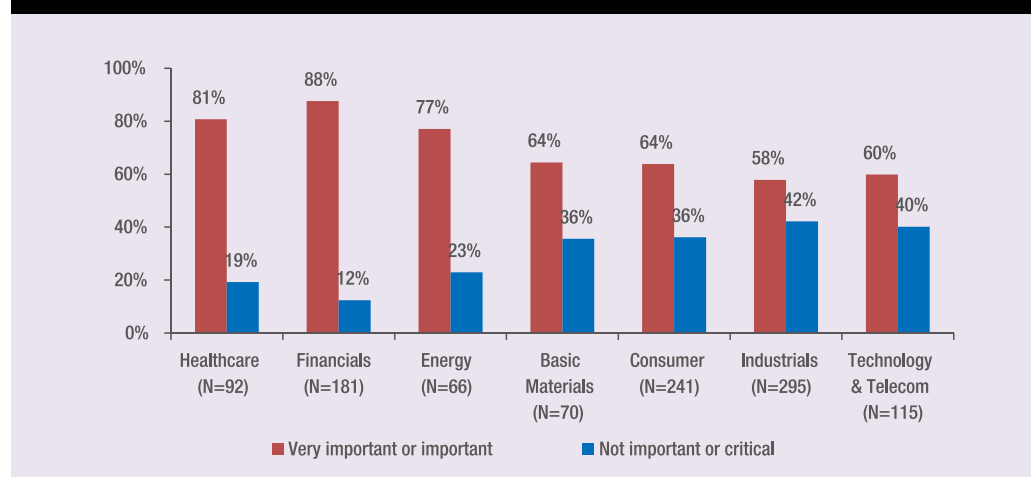


FIGURE 75 - BY INDUSTRY HOW IMPORTANT ARE THE RELATIONSHIPS WITH THE AUTHORITIES?



4.4.2. Corruption

The Corruption Improvement Index is based on the multiple-choice question “In your view, how is corruption in your industry compared to last year?” and it is built in similar way to the well-known Purchasing Managers’ Index (PMI). A reading of 50 means that corruption is unchanged; a number over 50 indicates an improvement while anything below 50 suggests a worsening of the situation in the past year. The further away from 50 the index is, the stronger the improvement or worsening over the year.

After four years (from 2012 to 2015) observing the Corruption Improvement Index get better year after year from, 2016 showed a slight deterioration that continued in 2017 and in 2018, it continues this downward trend, albeit modest. The index is still larger than 50, meaning that our sample perceives an improvement in the corruption situation in 2018 vs. 2017. However, its value is smaller than what it was in previous years.

An interesting phenomenon that we have been observing in all editions of this survey is that respondents perceive corruption in China as being less acute when asked about one’s own industry than when asked about the country in general. When we ask our sample about general corruption in China, a majority (62% of respondents) view corruption in China to be a problem (moderate to serious). However, when asked about corruption in their industry, the number of respondents seeing it as a problem drops to 31%. This circumstance is observed with respondents from all types of companies (Chinese private-owned firms, WFOEs and Joint Ventures), and across industries.

Different industries seem to perceive different levels of corruption, as well as different types of company in terms of their legal status. The charts below provide details on these perspectives.

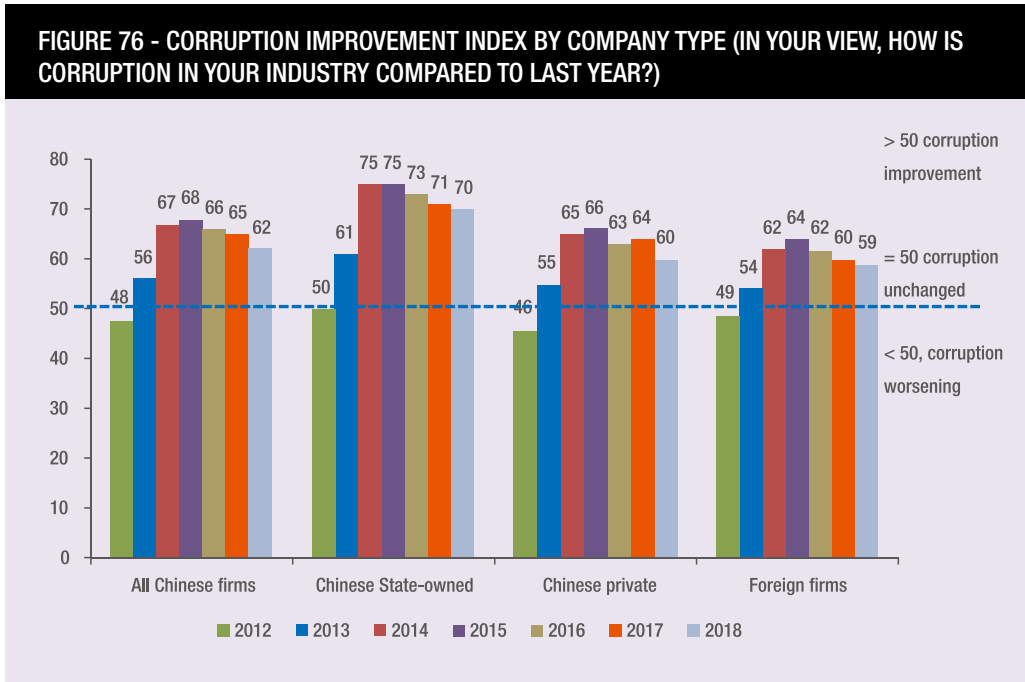


FIGURE 77 - IN YOUR VIEW, HOW SERIOUS IS CORRUPTION IN CHINA, IN GENERAL, AND IN YOUR INDUSTRY? N=1,013

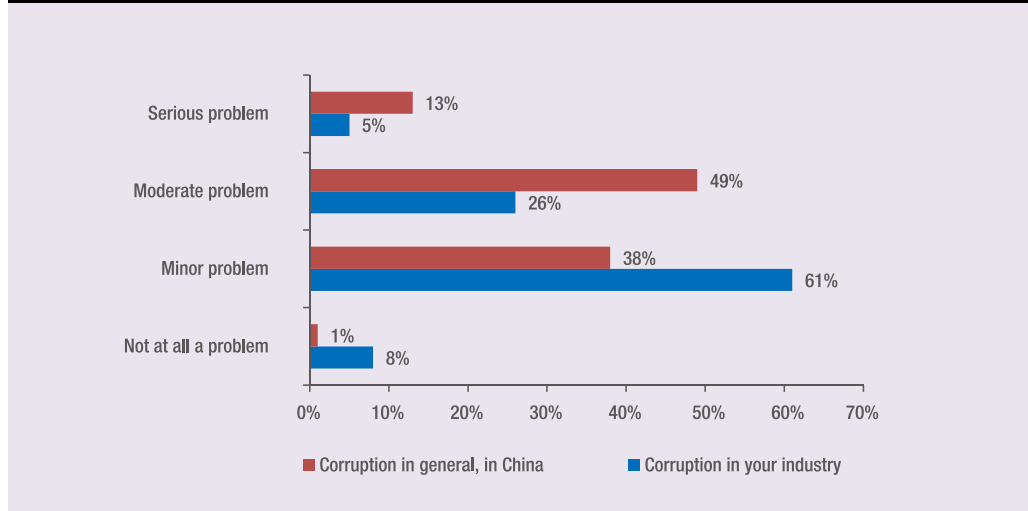


FIGURE 78 - BY COMPANY TYPE - IN YOUR VIEW, HOW SERIOUS IS CORRUPTION IN YOUR INDUSTRY?

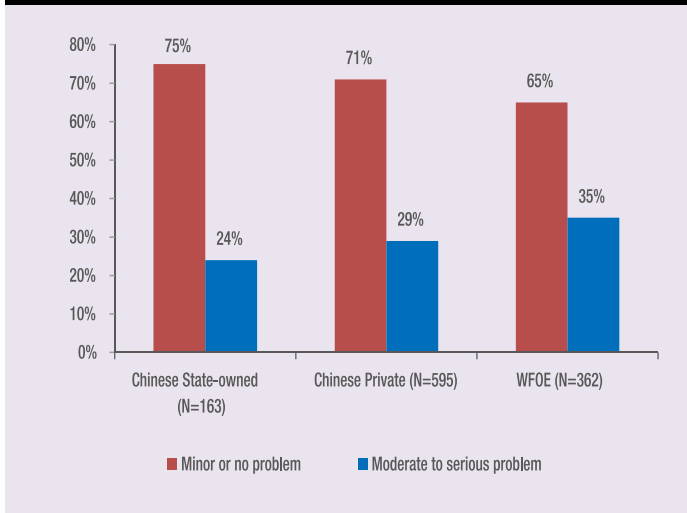


FIGURE 79 - BY INDUSTRY - IN YOUR VIEW, HOW SERIOUS IS CORRUPTION IN YOUR INDUSTRY?

