



Companies Awaiting Market's Decisive Role

■ Professors Xu Bin, Juan Antonio Fernandez and Zhou Dongsheng

The increasing role of the market and the decreasing role of the government is eagerly anticipated by both Chinese and foreign executives according to our poll of 773 executives from companies doing business in China.

Chinese and foreign executives who participated in the *CEIBS Business in China Survey 2015* are anticipating that the new round of economic reform which got underway in China in 2014 will further increase market openness and reduce government intervention. They are likely reacting to signals from the Third Plenum of the 18th Communist Party of China Central Committee which set the new reform agenda in November 2013. As outlined in the blueprint for comprehensive reform in China for the next ten years, *The Decision on Major Issues Concerning Comprehensively Deepening Reforms*, “the basic economic system should evolve on the decisive role of the market in resource allocation.” Chinese and foreign executives have heard this message loud and clear, based on their responses for this year’s *CEIBS Business in China Survey*.

The *Survey* is an annual poll of business executives working in China for both Chinese-owned and foreign-owned companies. Among the findings from this year’s poll: the types of reforms companies prefer, the roles of innovation and the Internet in China’s new business environment, as well as the competitiveness of Chinese private companies.

Chart 1: Do you think your company will benefit in the future from current reform policies?

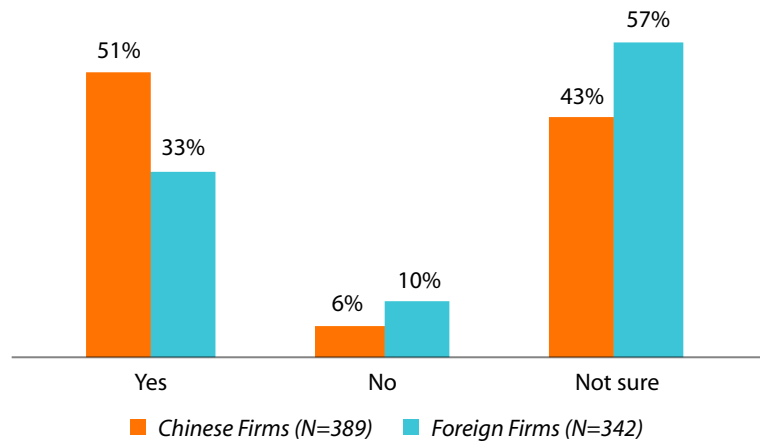
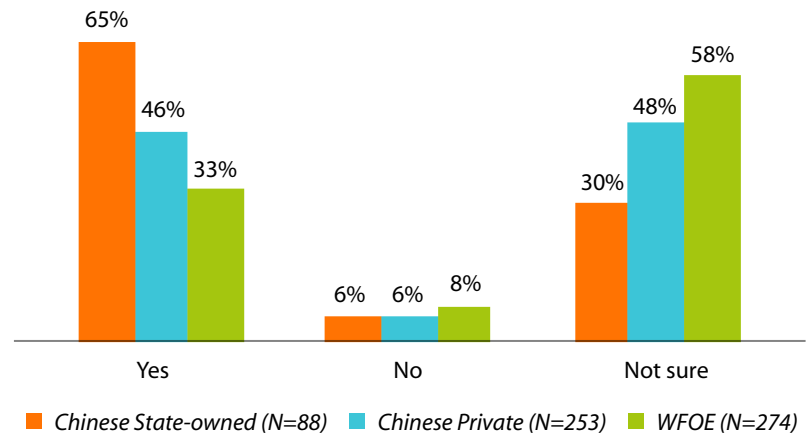


Chart 2: Do you think your company will benefit in the future from current reform policies?



“The benefits of government reform are yet to be felt by many companies.”

NEW REFORM POLICIES ANTICIPATED BUT UNCERTAINTY REMAINS

Despite the Chinese government’s efforts to kick-start new reforms in 2014, the benefits of these changes are yet to be felt by many companies. Among the 731 executives who answered the question “Do you think

your company will benefit in the future from current reform policies?”, 43% of Chinese company executives and 57% of foreign company executives said they were not sure (see chart 1). When we break down the sample by ownership, 48% of Chinese private company executives and 58% of foreign executives from wholly foreign owned companies said they were not sure



Professor Xu Bin



Professor Juan Antonio Fernandez

“*State-owned company executives felt that they would benefit from the current reform policies.*”

about the future benefits of the current reform policies (see chart 2). These data indicate that there is still a lot of uncertainty about the potential benefits of the new reform policies, especially among private and foreign companies in China. It is interesting to observe that 65% of state-owned company executives felt that they would benefit

from the current reform policies. While many new reform policies aim to reduce the power of state-owned enterprises, the majority of state-owned company executives in our survey (65%) expect to benefit from such policies which may breathe new life into these state-owned companies (see chart 2).

Chart 3: Which reform policy benefited your company in 2014?

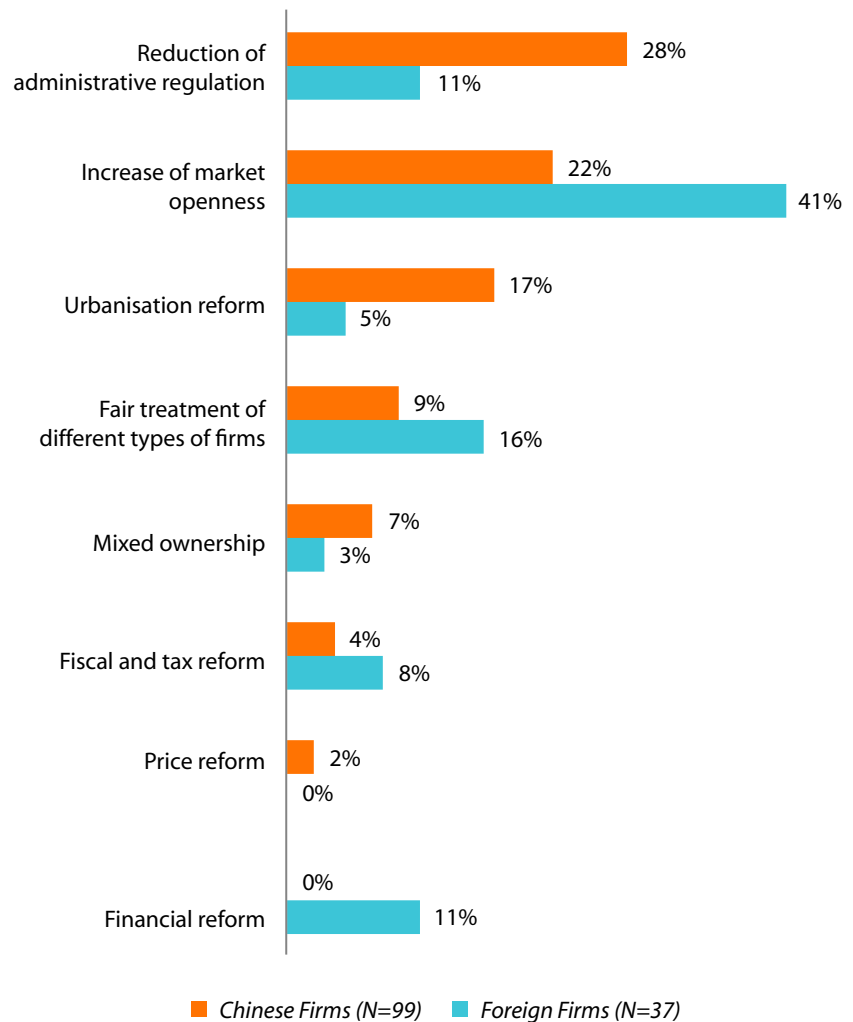
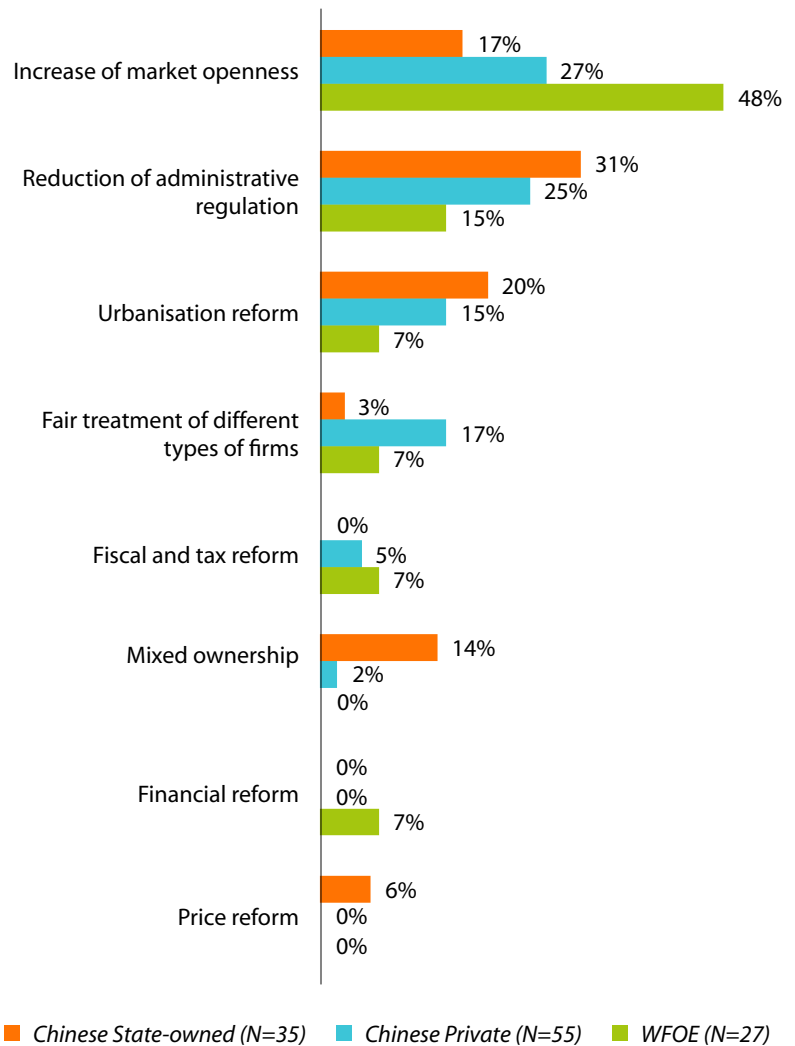


Chart 4: Which reform policy benefited your company in 2014?

For the fraction of companies which already benefited from new reform policies in 2014, their answers reveal the areas of reforms that companies prefer. For Chinese companies, 28% of them listed “reduction of administrative regulation” (decreased government intervention) as the number one benefit. For foreign companies, 41% listed “increase of market openness” as the number one benefit (see chart 3). Chart 4 shows that the number one benefit listed by Chinese private companies was also “increase of market openness” (27%), while “reduction of administrative regulation” came a close second (25%). These answers reveal that companies prefer new reform policies that increase the role of the market and decrease administrative interventions.



Professor Zhou Dongsheng

“ Chinese companies listed decreased government intervention as the number one benefit. ”



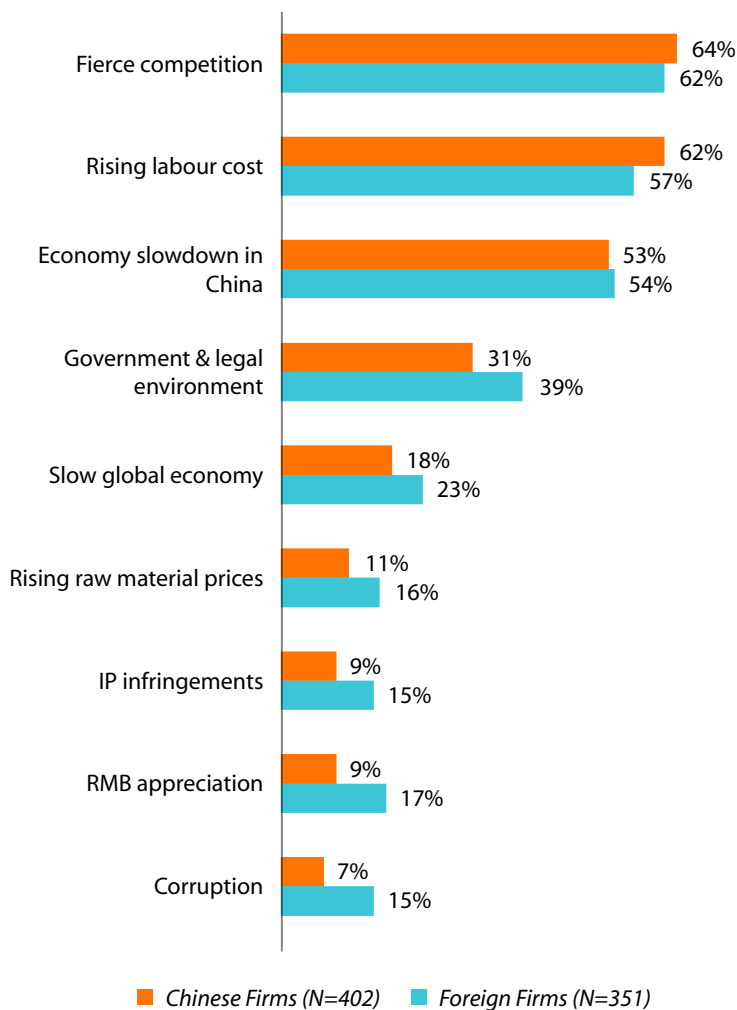
“ *Innovation is becoming increasingly important in China’s new business environment.* ”

BUSINESS CLIMATE REFLECTING CHINESE ECONOMY’S “NEW NORMAL”

The Chinese economy was said to be in a “new normal” stage in 2014 as characterised by slower economic

growth, higher labour cost, and more competition. When asked “What are the greatest external challenges for your company?”, both Chinese and foreign companies listed “Economic slowdown in China”, “Rising labour cost” and “Fierce competition” as the top three challenges, which reflect the “new normal” characteristics of the Chinese economy (see chart 5).

Chart 5: What are the greatest external challenges for your company?



The “new normal” status of the Chinese economy posed new management challenges to companies in China. When asked “What are the greatest internal challenges facing your company in China?”, 61% of Chinese company executives and 58% of foreign company executives said it was “Finding and retaining talent”, which reflects the increasingly tight conditions of China’s labour market (see chart 6). It is worth noting that 51% of Chinese company executives saw “Innovation capability” as a top management challenge, which indicates the rising importance of innovation in China’s new business environment.

One pronounced feature of China’s new business environment is the increasingly competitive power of Chinese private companies. When asked “Who are your major competitors in China?”, 76% of Chinese company executives and 68% of foreign company executives pointed to Chinese private companies (see chart 7). Notice that less than 30% of Chinese company executives considered wholly foreign

Chart 6: What are the greatest internal challenges facing your company in China?

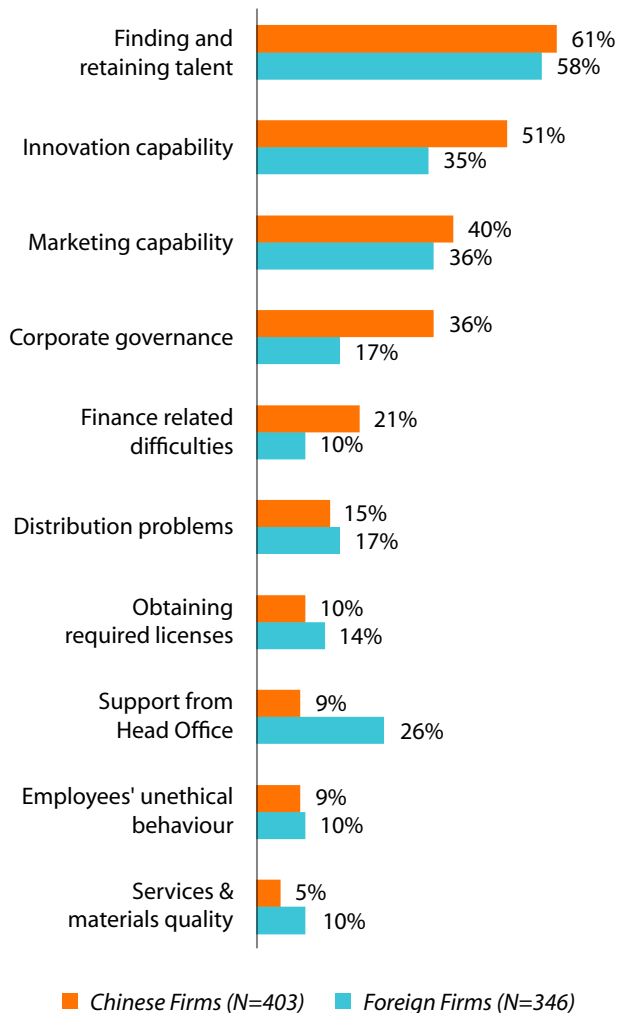
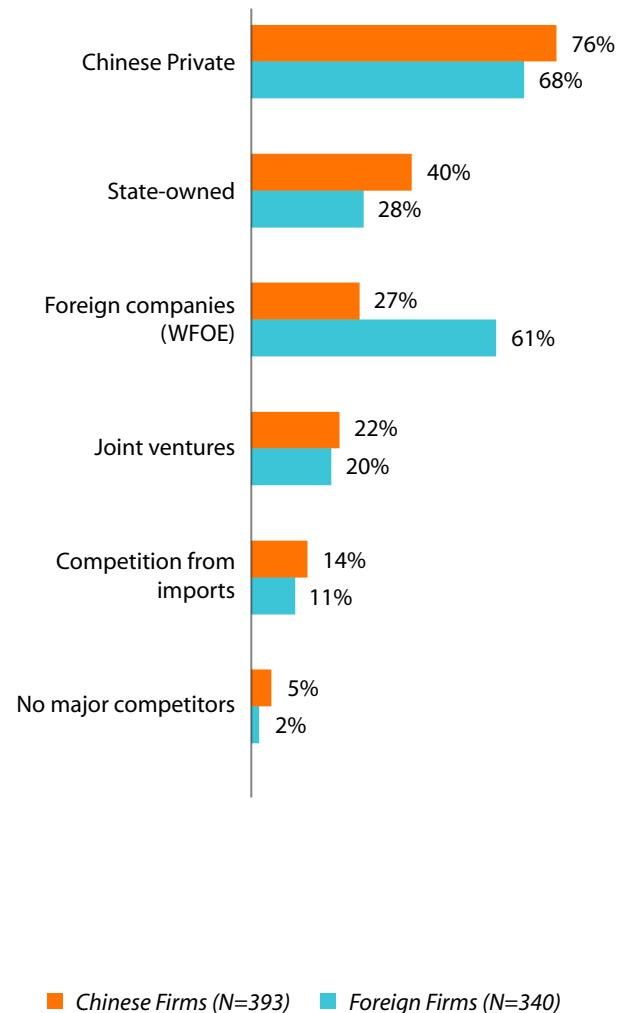


Chart 7: Who are your major competitors in China?



owned companies (WFOE) and joint ventures as their major competitors, which reflects a significant change of China's business climate.

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). Chart 8 shows the confidence index regarding the next year from the 2011 survey to the 2015 survey. In the 2011 survey, the confidence index was 7.2 for foreign firms and 6.7 for Chinese firms, which was relatively high and also divergent between domestic and foreign companies. In the past four years, the value of the one-year confidence index moved down and converged to a level of around 6.5 for both Chinese and

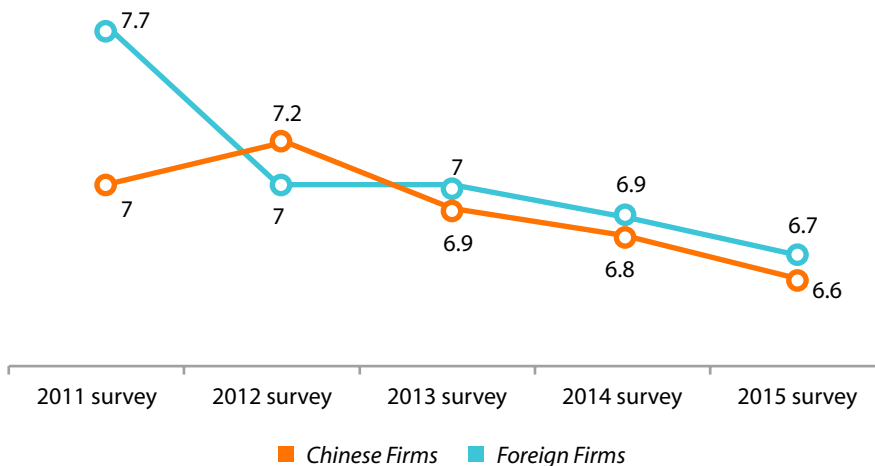
foreign companies, which reflected the fact that all companies operating in China had adjusted their expectations and accepted the "new normal" status of the Chinese economy (see chart 8).

The confidence index regarding the next 5 years shows a steady downward trend (see chart 9). The values of the confidence index in the 2011 and 2012 surveys are equal or above 7, but they are equal or below 6.7 in the 2015

Chart 8: How confident are you that your operations in China will be successful in the next year?



Chart 9: How confident are you that your operations in China will be successful in the next 5 years?



survey. As a result, the values of the one-year confidence index and the five-year confidence index become closer, which may reflect the fact that company executives had gradually learned from their business practice that the “new normal” situation of the Chinese economy would indeed continue in the foreseeable future.

NEW OPPORTUNITIES, NEW STRATEGIES

China became a high-middle income country in 2010 when its per capita gross national income reached USD4,000. In this new development stage, China’s economic growth rate has slowed down to 7.4% in 2014, while the country’s economic structure has seen an expansion of the service sector (whose size exceeded the industrial sector in 2012) and the rise of the Internet-led new economy. In our survey, when asked about the change in employment, 60% of the surveyed Chinese companies and 48% of the surveyed foreign companies indicated an increase of their labour force in 2014, compared with 16% of Chinese companies and 20% of foreign companies which decreased their labour force in 2014 (see chart 10). Therefore, despite the further slowdown of the Chinese economy in 2014, the majority of the companies in our sample still expanded their business operations.

In recent years, China has seen an increasing emphasis of the role of innovation. Our survey indicates that this trend will continue. When asked about their R&D plans for the next 3 years, 71% of Chinese company executives and 59% of foreign company executives said that their companies will increase R&D intensity (see chart 11). Another trend observed in China in recent years is the increasing use of the Internet for business operations.

The 2015 CEIBS Business in China Survey was completed by 773 executives between November and December 2014, with 412 from Chinese companies and 361 from foreign companies. Among them were 339 CEOs, GMs, and company owners; 220 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, 77% are from the Chinese mainland, 2% from Taiwan, Hong Kong or Macao, and 21% from foreign countries. Most of them (93%) have more than 10 years of work experience, with 53% of them having more than 20 years of work experience. This broad and experienced sample added rich and valuable perspectives to the survey.

When asked about their plan to expand the digitisation of their businesses, 90% of Chinese company executives and 82% of foreign company executives said that their companies will have a plan to expand the digitisation of their businesses (see chart 12). These trends highlight the new business opportunities that have emerged as China moves up in its economic structure, which call for the design and adoption of new business strategies for companies operating in the country.

Xu Bin is Professor of Economics and Finance at CEIBS, Juan Antonio Fernandez is Professor of Management, while Zhou Dongsheng is Professor of Marketing. The authors would like to acknowledge the support of a CEIBS research grant, and excellent research assistance from Maria Puyuelo and Jenny Li.

Chart 10: What is the change in your company labour force in 2014 vs. 2013?

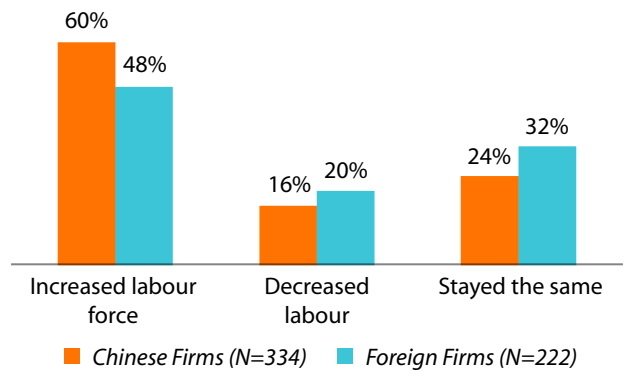


Chart 11: What are your R&D plans for the next 3 years?

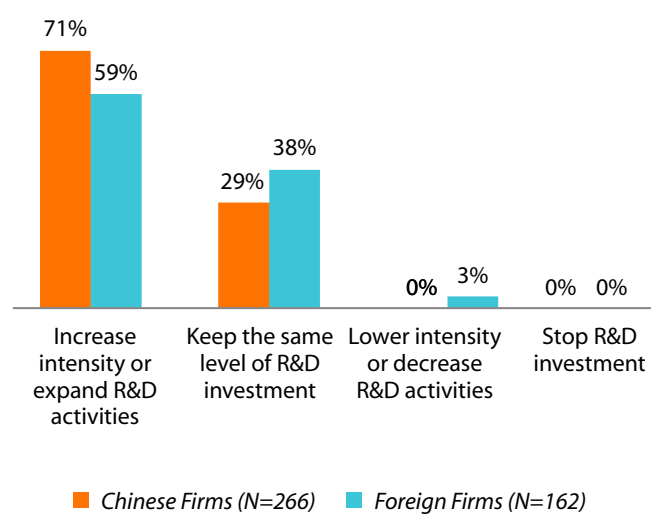


Chart 12: Do you plan to expand the digitisation of your business?

