



***Perspectives on
Doing Business
with
China***



Presentation

Will talk about:

- Why China?
- Alberta's and Canada's involvement
- Opportunities for engagement
- Doing Business with China
- Observations and Conclusions



China's Economy - Everything is Relative

- China has suffered along with other world economies
- Probably been less affected than most
- Impacts highly regional, more sector specific
- Still has vast capital reserves for strategic positioning
- May emerge stronger than before



Overview of China Economy

- China has world's second largest economy after USA, with a GDP of over \$6.9 trillion in 2007.
- China accounts for 9.7% of world's GDP.
- Its annual growth has averaged more than 10% since early 1990's.
- China's growth has been driven not only by export but also by domestic demand.



China's Strategic Asset

- China's foreign reserves close to US \$2 trillion
- Pre economic meltdown, China was accumulating foreign reserves at a rate of US\$100M per hour
- Created the China Investment Corp., a US \$200 billion sovereign fund
- China acquiring strategic foreign assets with over 55 foreign acquisitions worth more than US \$25 billion
- Estimated 5,000 Chinese companies have established direct investments in 172 countries



China's Impact on World Economies

- Remains the factory of the world
- The demand for natural resources will continue to push world commodity prices
- The demand for natural resources will continue as its economy is forecasted to rebound quickly and continue to grow by close to double digit growth



Challenges for China

- Need to create jobs – even before the financial crisis there were 30 million new workers joining the labor force
- Secure a long term energy supply
- Address environmental issues
- Continue reformation of state-owned enterprises



Our Relationship with China

- Alberta shipping grain to China in 1960's
- In the 1980s, exports expanded to oil & gas equipment and services and other industrial products
- Alberta twinned with Heilongjiang, Edmonton with Harbin, and Calgary with energy capital of Daqing
- China is Alberta's 2nd largest trading partner, averaging over \$4 billion since the early 2000's
- In 2006, Alberta exports to China totaled about \$2.2 billion and imports from China totaled about \$3.5 billion



Opportunities that Could Influence Alberta's Economy

- Alberta currently has a number of co-operation and partnership agreements with China.
- Chinese companies have acquired a number of Alberta energy companies
- Over twenty Alberta energy companies operating in China
- China Alberta's 2nd largest trading partner and 4th largest export market for agricultural products
- China could influence Alberta's economy on many fronts, especially in:
 1. Energy Supply
 2. Services and Equipment Procurement
 3. Education
 4. Labor



Energy Supply:

- China is the world's second largest consumer of oil behind the US
- It is the third largest net importer of oil after the US and Japan
- From 2003 – 2030, China's annual average growth rate for oil consumption is projected to increase by 4% per year accounting for 25% of the total global increase in demand
- The US currently imports 22% of its energy from Canada
- China could become a large customer for Alberta's petroleum products
- Gas emerging as a potential export opportunity



Services and Equipment Procurement:

- China is migrating from low-end manufacturing to high-end manufacturing with value added products
- Opportunity for Alberta companies to source services and equipment from China
- Opportunity for Canadian companies to work with Chinese companies to produce equipment specifically to meet their needs



Education:

- Currently, China has 218 million children and 94% are getting at least nine years' education
- China has 43 times more children to educate than Canada but has only twice as many universities
- Due to insufficient space and with the desire for foreign education, there has been a strong growth in Chinese students studying abroad
- For many Chinese students, Canada is the preferred destination for foreign study – second only to the US
- Probably one of the greatest long term strategic relationship building opportunities



Doing Business with China

- Many ways to access the China opportunity
- Need to carefully think through your China strategy

- What do you want to achieve?
 - A potential market for your products or services
 - A potential investor in your business
 - Opportunity to source products or services
- Your needs should drive your approach



China as a Potential Market?

- Clearly not for the faint of heart
- Must understand your product offering and its positioning in China
- How can you protect your offering?
- What are the barriers to entry?
- What vehicle should you use to establish a presence in China



China as a Potential Investor?

- Strategic offshore investment encouraged by the Central Government
- Difficult to identify and engage key decision makers - often not who are out in front
- Takes a long time – just to discover the rules of engagement
- Often requires influential intermediaries - but be cautious
- Generally not leaders in developing new opportunities
- Potential significant governance issues



China as an Opportunity to Source Products and Services?

- There is clearly a China cost structure that is compelling
- Requires substantial due diligence to confirm quality and qualifications
- If a supplier arrangement appears too good to be true, it usually is!
- Many product or service failures as much the responsibility of the entity sourcing as it is the supplier



So You Want to Do Business in China

- What vehicle will you use?
 - Representative Office
 - Joint Venture
 - Wholly Foreign Owned Enterprise
 - Foreign Invested Commercial Enterprise
- Have different strengths and weaknesses and levels of engagement
- All have significant issues in accounting, audit and compliance, human resources, intellectual property, repatriating profits, liquidation, etc.
- Key is to get good advice



So You Want to Do Business in China

- Connections and relationships are important in Asian business culture
- Be cautious of individuals who rely only on connections – connections can be fleeting
- Ensure that local representatives can deliver on the fundamentals and know the business environment
- Ensure that corners have not been cut to get approvals – you are still liable for errors or omissions
- The arrangement that is too good to be true, usually is!



So You Want to Do Business in China

- China is complicated and bureaucratic, but it is improving
- Legal protections are beginning to mirror developed countries, but enforcement still needs work
- Intellectual property protection is improving, but a long way to go
- Labor legislation is getting stronger and is being more commonly enforced
- Still significant regional variations in application and enforcement



One approach to China

- Personally been engaged with China almost 25 years
- First established and oversaw a Representative Office for an investment company
- Decision to establish a WFOE in southern China and build a manufacturing plant
- In our case decision was to take advantage of a China cost structure while minimizing issues around intellectual property protection and quality control
- Cost structure applies not only to China produced products



Conclusions

What must Governments do?

- Work with industry to develop a comprehensive China strategy
- Encourage China to invest in Canada so they have a vested interest in our success
- Recruit more China students to Alberta as a strategic economic development initiative – forges relationships and builds a great source of skilled workers for the future
- Develop a more thoughtful and co-operative foreign policy with China
- There is a reason why Canada is one of the few developed countries that do not have Approved Destination Status (ADS) with China



Conclusions

What must Industry do?

- Develop a realistic China strategy – it is a great market, but a tough market
- Due diligence is critical – beware the promoters and the hype
- Develop reasonable expectations
- Develop clear measures of success
- Engage with people you can trust implicitly