Journal of the European Union Chamber of Commerce in China

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The Luxury Experience in China

CLEARING THE AIR
China Moves Towards Private Aviation

HITTING THE TARGET
Marketing Luxury Goods in China

DAVID MARSH
A New Currency Constellation

JEREMY GALBRAITH
Rules for Lobbying the European Parliament

THE EXECUTIVE INTERVIEW
Miroslav Kolesar, PPF Group China

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How to Reach Us:

Mr. Simon Wan, President
China Team Cornerstone (欧信英才)
Email:sh@chinateam.com
Member of the Cornerstone International Group
135 member firm offices worldwide
Website: www.chinateam.com
Global Website:www.cornerstone-group.com

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TABLE OF CONTENTS

COVER STORY

14 THE LUXURY EXPERIENCE IN CHINA

A new report by accounting and advisory firm KPMG shows that luxury companies are pursuing very different strategies in China.

18 CLEARING THE AIR: CHINA MOVES TOWARDS PRIVATE AVIATION

That China would open its skies to more private planes was music to the ears of aviation industry executives and buffs around the globe.

22 INDUSTRY FOCUS: CHINA'S LUXURY MARKET OVERVIEW

According to the statistics of World Luxury Association, growth of China's luxury market has been the fastest in the world in recent years.

24 HITTING THE TARGET

Veteran China marketer David Wolf takes a look at Beijing's new restrictions on luxury advertising.

On the cover

Private planes have become the latest category of products in China's burgeoning luxury market. See pg. 18.

BUSINESS FEATURES

10 EUROPEAN CHAMBER LOBBYING REPORT

A summary of recent lobbying activities.

26 BUSINESS OUTLOOK

The European Chamber's *Business Confidence Survey 2011*.

30 LAW & REGULATION

China's new Social Insurance Law: What it means for European business.

34 MONETARY POLICY

David Marsh, co-chairman of monetary think-tank OMFIF speaks about the Euro's future and China's plans for it.

36 LOBBYING

Jeremy Galbraith, CEO of Burson-Marsteller Europe explains the difference between a good and a bad lobbyist.

38 RENEWABLE ENERGY

More than just hot air: wind power in emerging economies.

40 TRADE

How the iPhone distorts China's trade deficit.

44 OUTBOUND TRAVEL

Out, Out and Away: TUI China begins outbound travel services.

46 CITY FOCUS

Nanjing: lots of land and a high rate of growth.

48 IPR

Managing IP as a business asset.

50 SMEs

Opportunities for European SMEs in China's textiles & apparel market.

58 THE EXECUTIVE INTERVIEW

Miroslav Kolesar, Chief Representative of PPF Group China

REGULARS

09 PRESIDENT'S FOREWORD

53 EVENTS CALENDAR

54 EVENTS GALLERY

56 CHAMBER BOARD

59 ADVISORY COUNCIL

中国进出口商品交易会
CHINA IMPORT AND EXPORT FAIR
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European Chamber Chapters:

Beijing
Beijing Lufthansa Center, Office C412,
50 Liangmaqiao Road,
Beijing, 100125, P.R. China
北京市朝阳区亮马桥路五十号
燕莎中心写字楼C-412室
Tel: +86 (10) 6462 2066
Fax: +86 (10) 6462 2067
euccc@europeanchamber.com.cn

Chengdu
04-A, F16, Tower 1, Central Plaza, No.8 ShunCheng Avenue, Jinjiang District, Chengdu
成都市锦江区顺城大街8号中环广场1座16楼04-A
Tel: +86 (28) 6155 7184
Fax: +86 (28) 6155 7194
chengdu@europeanchamber.com.cn

Guangzhou – Pearl River Delta (PRD)
Unit 2817, 28/F, Tower A,
China Shine Plaza,
No.9 Linhe Xi Road,
Tianhe District,
Guangzhou, 510613,
P.R.China
广州市天河区林和西路9号
耀中广场A座2817室
Tel: +86 (20) 3801 0269
Fax: +86 (20) 3801 0275
prd@europeanchamber.com.cn

Shenzhen – Pearl River Delta (PRD)
Rm 308, 3/F Chinese Overseas Scholars Venture Bld,
South District, Shenzhen Hi-tech Industry Park,
Shenzhen, 518057,
P.R. China
深圳高新区南区
留学生创业大厦3楼308室
Tel: +86 (755) 8632 9042
Fax: +86 (755) 8632 9785
prd@europeanchamber.com.cn

Nanjing
Zhujiang No.1 Building, 30/F, E1
1 Zhujiang Road,
Nanjing, 210008, P.R.China
南京市珠江路1号
珠江1号大厦30楼E1座
Tel: +86 (25) 8362 7330 / 8362 7331
Fax: +86 (25) 8362 7332
nanjing@europeanchamber.com.cn

Shanghai
Unit 2204, Shui On Plaza,
333 Huai Hai Zhong Road,
Shanghai, 200021,
P.R. China
上海市淮海中路333号
瑞安广场2204室
Tel: +86 (21) 6385 2023
Fax: +86 (21) 6385 2381
shanghai@europeanchamber.com.cn

Shenyang
Room 20-10.
Office Tower 1, Shenyang Rich Gate Plaza,
No. 7-1 Tuanjie Road,
Shenhe District
Shenyang 110001,
P.R. China
辽宁省沈阳市沈河区
团结路7-1号
沈阳华府天地第一座20-10室
Tel: +86 (24) 2334 2428
Fax: +86 (24) 2334 2428
shenyang@europeanchamber.com.cn

Tianjin
Magnetic Plaza, Building 17,
Room 15A17,
Junction of Binshui West & Shuishang East Road,
Nankai district, Tianjin,
300381, P.R. China
天津市南开区宾水西道（宾水西道与水上东路交口）
奥城商业广场17座15A17室
Tel: +86 (22) 2374 1122
Fax: +86 (22) 2374 1122
tianjin@europeanchamber.com.cn

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Confidence & Success

Mr. Davide Cucino
President of The European Union Chamber of Commerce in China

Dear Members and Friends of the European Chamber:

The last two months have seen new levels of engagement and attention for the European Chamber.

At the end of May, we launched our annual *Business Confidence Survey 2011*, garnering unprecedented media attention for this important gauge of the business environment for European industry in China. As you will see from our coverage in this issue, the good news is that European companies in China are doing well. Of those that responded to our survey, 78% reported greater revenue in 2010, and 71% reported greater profit, although only one-third are generating better margins in China than elsewhere in the world.

That is the good news. The not so good news is that 43% believe that the operating environment in China is becoming increasingly unfair, and 46% expect that situation to deteriorate. However, our companies have proven that they can flourish in a difficult economic and regulatory environment and I am confident that we will continue to do so.

The European Chamber held some predominantly high-level meetings during May and June, in particular with European Council President Herman van Rompuy. Prior to his meetings with China's top leadership, representatives of the Chamber's Executive Committee met with President van Rompuy and EU Ambassador Markus Ederer to brief them on issues of key importance to European industry and to express our views on those issues. It again demonstrates our commitment to our members to take their key messages to the highest levels of both European and Chinese government.

The European Chamber has also recently commented to the National Development and Reform Commission on the revised draft of the Foreign Investment Catalogue. The draft presents some positive developments by lifting restrictions in some areas, however these positive changes are minimal and the current revised catalogue does not substantially differ from the previous one. The European Chamber and its members consider this a missed chance for China's strategic development and growth goals, particularly those stated in the 2010 'Several Opinions of the State Council on Further Improving the Utilisation of Foreign Investment' and the 12th Five-Year Plan.

Summer is traditionally a quieter period of the business cycle, but the Executive Committee and the Chamber staff will remain hard at work. During this period we will continue our lobby meetings and communications with all of our stakeholders as we prepare for the launch of our most important publication, the annual Position Paper. In September, we will set out on our European Tour. This year we will take the Position Paper to more European capitals than ever before. Along with disseminating key messages to major European leaders and legislators in Brussels, presenting the Position Paper in person allows us to connect with our stakeholders in their home countries and to underscore the importance of EU-China trade issues.

I wish you all a successful and pleasant summer.

EUROPEAN CHAMBER LOBBYING HIGHLIGHTS

Meeting with the President of the European Council, Herman van Rompuy

The European Chamber had two meetings with European President Herman van Rompuy during his trip to China. On 16th May in Beijing, European Chamber President Davide Cucino, along with Vice Presidents Jens Ruebbert and Miroslav Kolesar, held a private meeting with President van Rompuy prior to his meetings with China's President Hu Jintao, China's Premier Wen Jiabao and China's Vice President Xi Jinping to brief him on some of the Chamber's major current concerns. On 18th May in Shanghai, a delegation of European Chamber representatives were given feedback from President van Rompuy following his meetings in China and were invited to address questions to him. The delegation was led by Chamber Vice President and Chairman of the Board of the Shanghai Chapter, Piter de Jong, and was also attended by other Shanghai Chapter Board members, as well as representatives of the Cosmetics, Construction and various financial services Working Groups.

Position Paper Presentation Meeting with the Commissioner of the Chinese State Food and Drug Administration (SFDA), Shao Mingli

On 11th May, a delegation of the European Chamber led by Chamber President Davide Cucino met with Commissioner Shao Mingli of the Chinese State Food and Drug Administration to present the Position Paper. Working Group Chairs of the Cosmetics and Healthcare Equipment Working Groups, Didier Saint-Leger and Lance Niu, discussed views on a potential transition from emphasising pre-market registration controls to post-market surveillance; and on classification and standardisation issues, respectively. Pharmaceuticals Working Group Senior Representative, Liu Xiang, exchanged views with Commissioner Shao Mingli on the Chinese Pharmacopeia.

Position Paper Presentation meeting with the Assistant Chairman of the China Insurance Regulatory Commission (CIRC), Chen Wenhui

On 3rd May, a delegation of the European Chamber led by Chamber Vice President Miroslav Kolesar met with CIRC Assistant Chairman Chen Wenhui to present the Position Paper. Vice Chair Wang Qingqing and other representatives of the Insurance Working Group exchanged views with Assistant Chairman Chen on various issues pertaining to insurance and the meeting concluded with both parties agreeing to have more regular working level contact in the future.

Meeting with the European Commissioner for Research and Innovation, Máire Geoghegan-Quinn

The EU Commissioner for Research and Innovation, Ms. Máire Geoghegan-Quinn, had a breakfast meeting with a delegation of European Chamber representatives on 26th May. European Chamber President Davide Cucino presented the Business Confidence Survey 2011 and representatives from the Chamber Advisory Council and the Cosmetics and Renewable Energy Working Groups commented on China's conditions for innovation, as well as issues related to public procurement, access to R&D programs, opportunities for R&D and the IPR environment.

Submissions of comments on the Chinese Social Insurance Law and on the Foreign Investment Catalogue

The European Chamber recently submitted two sets of comments to the Chinese Ministry of Human Resources and Social Security (MOHRSS) regarding the current work being undertaken by MOHRSS on revising the Chinese Social Security system. On 20th May, the European Chamber submitted comments on Several Rules on Implementing Social Insurance Law and on 17th June the European Chamber submitted comments on the Interim Measures for the Participation in Social Insurance of Foreigners Employed in China. The European Chamber also submitted comments to the National Development and Reform Commission following the release of the draft Catalogue of the Guiding Principles of Foreign Invested Industries. Consultation with Chamber members showed that in some key areas the draft Catalogue falls short of expectations set by the 12th Five-Year Plan that was released just prior to the Catalogue.

Meeting with the French Minister of European Affairs, Mr. Laurent Wauquiez

The European Chamber hosted the French Minister of European Affairs, Mr. Laurent Wauquiez, in a meeting on 5th May. Joined also by Her Excellency, Madame Sylvie Bermann, Ambassador of France to China, a delegation of European Chamber Chairs and Vice Chairs of the Aerospace, Automotive, Energy, Human Resources, ICT, Insurance, IPR, Legal, Pharmaceuticals, Public Procurement, Rail and SME Working Groups and Forums raised issues regarding current business operating conditions in China for European companies. Minister Wauquiez stated that the European Chamber plays an important role globally and asked for a written summary of the issues raised in the meeting in order to relay these back to stakeholders in Europe.

Meeting with the Deputy Director General for Enterprise and Industry (DGENTR), Daniel Calleja

Prior to his meetings with the Ministry of Industry and Information Technology, Deputy Director General Daniel Calleja of DG ENTR met with European Chamber President Davide Cucino and representatives of the Renewable Energy, SME, Aviation and Travel Working Groups. Mr. Calleja stated that the information received from the European Chamber would help his preparations for joint EU-China policy dialogues that will take place in late July.

Other Lobby Highlights in Brief

Since late April, the Chamber has held 37 meetings with the Chinese government at various levels and with differing ministry-level administrations and organisations. In addition, the Chamber has submitted 10 comments on draft regulations and policies to the Chinese government and undertaken 10 other lobby actions, which include focused lobby letters to Chinese government offices. During the same period, the Chamber has taken part in 28 meetings with officials from the European Union and from Member State governments.

Most of these meetings were arranged through the Working Groups. These include meetings organised through some of the Chamber's financial services-related Working Groups, including a meeting with Deputy Director General Tang Xiaodong of the Department of Fund Supervision of the China Securities Regulatory Commission, organised by the Private Equity and Strategic M&A Working Group; a meeting with the Deputy Director General of the Credit Reference Centre of the People's Bank of China, attended by European Chamber Vice President and Consumer Finance Working Group Chair Miroslav Kolesar; and a meeting with - and follow-up submission of an analytical report about insurance conglomerates in the European Union to - Deputy Director Luo Yanjun of the China Insurance Regulatory Commission Development and Reform Department, organised by the Insurance Working Group.

European Chamber Secretary General Dirk Moens was invited on 19th May to speak at the Low Carbon Leadership Network Event. Other keynote speakers included Su Wei, Director General of the NDRC Department of Climate Change and China's lead climate change negotiator. At the event, Mr. Moens explored the challenges and opportunities for foreign companies during China's shift towards a Green Economy. Representatives of the Renewable Energy Working Group of the Chamber also met with the Deputy Director General of the National Energy Administration, Liang Zhipeng, to discuss the Interim Measures on Administration of Grid Connection Testing for Wind Turbine Generator Sets that has caused concern for members.

Healthcare Equipment Working Group members met with both the Director General of the SFDA Department of Medical Devices Administration, Wang Lanming, to discuss issues pertaining to the IEC 60601-1 standard, and with Deputy Director General, Yang Tiesheng of the MIIT Department of Energy Conservation and Resources Utilisation to discuss environmental legislation affecting medical devices. In Shanghai, European Chamber Vice President Piter de Jong met with Shanghai Customs District to discuss further cooperation under the Strategic Dialogue Mechanism.

On the European side, a meeting was held with Helena König, Head of Unit of DG TRADE for Trade Relations with the Far East. European Chamber President Davide Cucino, along with Paul Ranjard, Ronan Diot and Gilbert Van Kerckhove, the respective Chairs of the IPR, Legal and Public Procurement Working Groups, discussed issues pertaining to IPR, subsidies and Social Insurance Law. The meeting also allowed the Chamber to provide input to assist DG TRADE's preparations for the EU-China Joint Committee meeting that will take place in July to discuss market access issues and more technical issues on investment and trade. Another meeting was held between members of the Aerospace and Aviation Working Groups and Director Matthew Baldwin of DG MOVE to provide input to him on general market developments in China and to listen to updates from Director Baldwin on the ongoing EU-China bilateral meetings with the CAAC. The European Chamber also met with DG HOME in June. The meeting between Marcel Schneider, Chair of the Travel Working Group, and DG HOME's Head of Visa Policy, Mr. Jan de Ceuster, was the first European Chamber meeting with DG HOME. Representatives of the Aviation Working Group also met for the first time with the International Air Transport Association. In the meeting with Zhang Baojian, Regional Vice President of the International Air Transport Association, both parties discussed how they could work together to help push for improvements to the regulatory framework of China's aviation industry.

Media Highlights

The European Chamber received significant media exposure in May and June. This was led in part by reports on the Asia-Pacific Headquarters Study and the Public Procurement Study, both launched in April, still being picked up by press; but was mostly owing to the press conference which was held to launch the annual Business Confidence Survey on 25th May. Almost 100 journalists attended the press conference, leading to more than 60 articles being published on the day of the launch. In-depth reports from major news outlets continued to be released into June on the Business Confidence Survey 2011.

In addition to attention from first-tier printing media outlets and news agencies including the Associated Press and the Wall Street Journal, the Business Confidence Survey also caught the attention of International TV stations including CNN, Bloomberg and CNBC. European Chamber President Davide Cucino was interviewed on the primetime CNN news program World Business Today on 25th May, while European Chamber Vice President Piter de Jong appeared on CNBC's Asia Squawk Box on 27th May. Mr. Cucino was also interviewed by ifeng.com, the website of Phoenix TV, to discuss perceptions of the Chinese business environment from the perspective of foreign-invested enterprises.

In May, the Chair of the Legal Working Group, Ronan Diot commented on news that expats may be included in the scope of China's social security system in both the Financial Times and the Wall Street Journal; and Gilbert van Kerckhove, Chair of Public Procurement Working Group, was interviewed by China Daily Europe.

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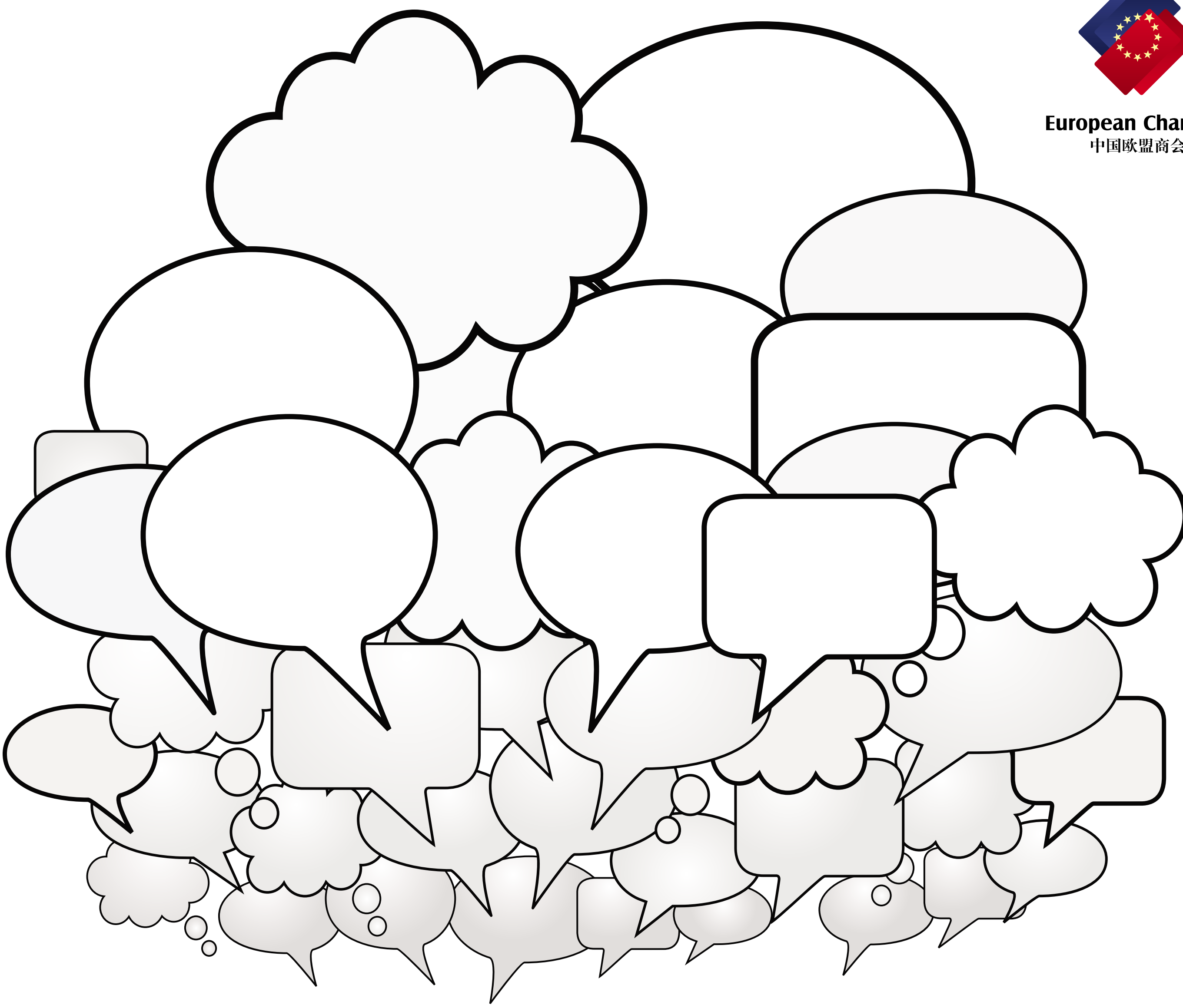

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The Luxury Experience in China

China's role in the global luxury market is becoming more significant year by year. Many international brands are starting to see a recovery in their global sales after three tough years, yet despite this China remains one of the brightest growth prospects. A new report by accounting and advisory firm KPMG shows that luxury companies are pursuing very different strategies in China, according to the scale of their operations and ambitions.

The traditional entry route for international companies into China's luxury goods market has been through partnerships with local franchises and distributors. In recent years, as the business landscape has become more open and transparent, many companies have fully acquired their retail operations in China - at least in the most developed cities such as Shanghai, Beijing and Guangzhou. For some, local partners are still important in tier-two and tier-three cities where market conditions are less familiar. However some Western brands have entered these markets directly with a wholly foreign-owned enterprise (WFOE) model.

A new KPMG study, entitled Luxury experiences in China, is based on a survey of 1,200 consumers in 24 tier-one and tier-two cities across China. Respondents were between 20-45 years of age, earning a minimum of RMB 7,500 (EUR 804.40) per month in tier-one cities and RMB 5,500 elsewhere. The consumer survey is complemented by case studies with 10 executives from companies including Bally, Cartier, Patek Philippe, Pernod Ricard, Salvatore Ferragamo, and domestic brands Hiersun and Shang Xia.

The study dispels the notion that luxury consumers in China are driven by status-seeking and overt demonstrations of wealth. It focuses on the rise of experiential luxury and how consumption is being driven by a desire for self-reward as well as status. The report also explores the role that the Internet and digital media can play in brand building and considers whether more domestic Chinese brands may succeed in the luxury sector as tastes change.

"China continues its march towards becoming the largest luxury market in the world", said Nick Debnam, Partner and Asia Pacific Chairman, Consumer Markets, KPMG China. "Year-on-year, as this market becomes more crowded, it is harder for luxury brands to enter this space. We see this in terms of rising brand recognition. In this year's study, consumers recognised an average of 57 brands, up from 45 last year. Brands therefore need to be innovative and explore new marketing avenues." [Fig 1]

The survey shows how China's luxury buyers are basing their purchasing decisions on a wider range of factors. Emotive factors such as experience and self-reward have now emerged alongside status-seeking and needs-based factors as key drivers.

"We have seen a gradual shift from status-driven to experiential consumption and luxury collecting, as consumers increasingly choose to reward or pamper themselves as opposed to seeking higher social status via their brand purchases. This could manifest itself in greater expenditure in five-star hotels or spas, for example. Meanwhile, Chinese consumers continue to place a lot of importance on the heritage of luxury brands", Mr. Debnam adds.

It seems that there is a new wave of connoisseurship in China which, although still less significant overall, is particularly evident among the wealthy inhabitants of tier-two and even tier-three cities. While the past year has seen an explosion of interest in fine wine, exemplified by the record sales of vintage Bordeaux wines at auctions in Hong Kong, the KPMG survey suggests that jewelry, fine art and antiques also have strong growth potential.

In many respects the consumption patterns of white-collar professionals and time-pressed executives in Beijing and Shanghai resemble their peers in other major capitals and financial centres as much as they do the wealthy business owners and entrepreneurs of second- and third-tier cities. However, it may be in these second and third-tier cities that the greatest share of wealth (and disposable income) lies and where consumption will grow fastest. This is another critical aspect for luxury companies planning their China expansion.

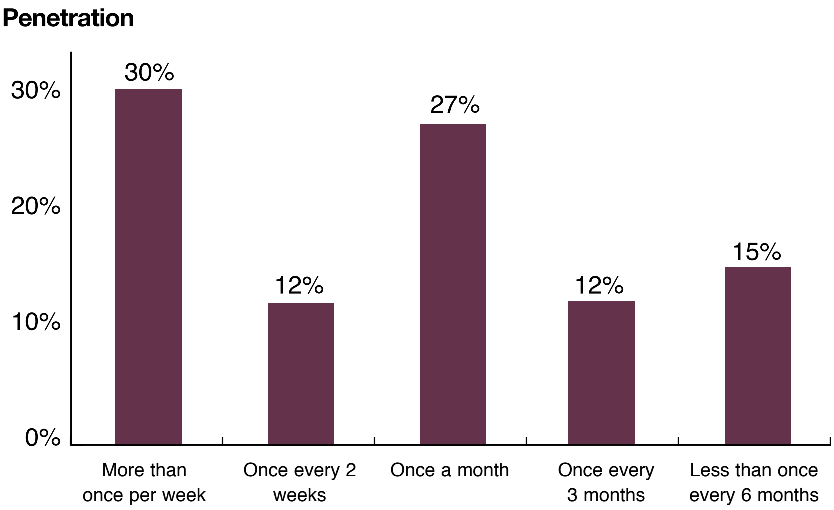
Another interesting message is that Chinese consumers distinguish very clearly among countries of origin, and associate certain countries strongly with certain products, such as Switzerland for watches, France for fashion, accessories and cosmetics, and Italy for footwear. French and Italian products grabbed the first and second positions, while Hong Kong products are the third-most popular. The territory's jewelry brands are popular with Chinese consumers, with several Hong Kong-owned premium clothing brands also doing well in China.

China meanwhile heads the list for alcohol, winning the top spot in this

Fig. 1 Brand Recognition (Total)

		Clothes	Bags and shoes	Watches	Jewellery	Import cars	Total
2011 survey	*Average number of brands recognized*	*13.5*	*15.9*	*8.8*	*5.6*	*13.1*	*56.9*
	As a percentage of brands listed	*35%*	*40%*	*34%*	*43%*	*77%*	
2010 survey	*Average number of brands recognized*	*9.8*	*11.9*	*7.5*	*4.9*	*11.3*	*45.4*
	As a percentage of brands listed	*27%*	*35%*	*31%*	*38%*	*66%*	
2006 survey	*Average number of brands recognised*	*9.3*	*4.7*	*7.6*	*2.5*	*10.1*	*34.2*
	As a percentage of brands listed	*28%*	*31%*	*30%*	*28%*	*60%*	

Fig. 2 How often do you search for luxury brands on Internet?



category (37%), thanks to the popularity of rice wine.

The Role of Digital Marketing

Unique to China is the large number of relatively young multimillionaires, far younger than their Western counterparts. This spells opportunities for brands using new technologies to interact with a younger consumer generation.

"The average age of Chinese millionaires is 39, whereas in the United States or Europe, the figure is over 50" - Rupert Hoogewerf, chairman of Hurun Report Inc., saying the demographic differences between Chinese and Western luxury travelers have led to different consumer behaviour.

While web channels can be effective in communicating promotions and special offers, they are still less effective in overall brand building and as a means of influencing choice of brands. Digital marketing and building online sales formats are being combined with the in-store experience. Luxury brands continue to focus on store image, location, floor size and store positioning, in order to gain competitor advantage in this market.

Nevertheless, it is clear that new forms of digital media are creating important new modes of interaction. "While the attitudes towards the web seem to be entrenched, technology can be a game-changer. The emergence of more innovative formats such as iPad apps are creating new possibilities to connect with consumers", said Mr. Debnam.

Philip Kuai, Director, Product & Strategy and Head of Mobile at AdChina, who has been interviewed in the report, also sees this trend. "In the past few years we have been surveying campaigns for a number of leading brands and we have seen some marked changes in user behaviour towards luxury brands. In the Internet age, it was very difficult for brands to occupy a user's desktop, but with apps it's different. They allow rich, eye-catching, interactive content and one-on-one communication between brands and their customers. This has been the turning point at which brands are spending far more on online marketing".

While the click rates for luxury are lower than for fast-moving consumer goods or consumer electronics, online publishers are nonetheless "very luxury-focused", according to Mr. Kuai. He also believes the importance of opinion leaders has increased. "The premium brands are increasingly focused on seeking out these leaders", he added.

The survey found that nearly 70% of respondents said they search online for information on luxury brands at least once per month, while 30% do so more than once per week. While official brand websites are often used as the first point of access for specific product information, celebrity blogs and other microblogs also play an important role when building a brand image in China.

Mr. Kuai notes that while luxury consumers most commonly browse the web for news or financial information, in certain categories there is a higher prevalence to visit luxury or lifestyle sites. "Among luxury alcohol consumers, we noticed far more tendency to browse luxury and beauty websites, compared to other categories", he explained.

According to AdChina's tracking of web activity, white collar senior managers are less attracted to these luxury and beauty sites, but show a higher-than-average inclination to click on web ads for financial products, watches and hotels. "Perhaps surprisingly these senior managers spend relatively more time surfing these sites between 9 am and 5 pm compared to some other segments, where we see more web activity at night time", Mr. Kuai adds.

Citing AdChina's own research, Mr. Kuai believes 17% of consumers are using mobile apps to search for lifestyle-related information, although at present only 5% are using apps to make purchases.[Fig. 2]

Prospects for Domestic Brands

One question that can polarise opinion among luxury executives is whether domestic Chinese brands have the potential to become more established in the luxury sector. Many executives feel that Western brands have a heritage and track record that serves as a barrier to entry and that Chinese brands cannot match.

However, others argue that China simply needs to rediscover its own history of craftsmanship and aesthetics and that the rapid growth of Chinese-born artists and designers bodes well for Chinese originated brands in the future.

KPMG's survey suggests Chinese brands are only weakly associated with luxury in most product categories (less than 10% in all categories except alcohol) at present. However, when asked about future potential of domestic brands, respondents saw alcohol, arts and crafts, and jewelry products having the strongest prospects for success. Certainly this appears to be good news for companies such as Shang Xia and Hiersun, two homegrown brands that are featured as case studies in the report.

Conversely, product categories where European brands dominate such as watches, clothes and accessories are seen as having the lowest potential for penetration by domestic brands. When asked specifically about watches, only 5% believed Chinese luxury brands had strong potential to rival international brands.

"Brands rooted in Chinese elements are gaining international recognition but are also sought after by Chinese customers" said Sandy Chen, research director with TNS. "There is a rising sense of national pride and cultural renaissance. In a consumer trends poll conducted in 2009, 75% responded 'I love my own country' compared to 25% who responded 'I love the whole world'. 83% said they were proud of the Chinese cultural heritage and felt guided by it".

Ms. Chen believes that categories that require strong technological capabilities (such as automobiles or watches) are less likely territories for Chinese luxury brands to excel. However, in these cases Chinese consumers' tastes are having an increased influence on new design. When it comes to products based on traditional fine craftsmanship or a secret recipe, she believes homegrown brands could do well. "Chinese luxury companies do possess a great opportunity to win the heart and mind of the Chinese consumers, especially when traditional Chinese elements are smartly blended with modern technology and marketing", she added.

KPMG is a global network of professional firms providing Audit, Tax and Advisory services. To read KPMG's new report entitled Luxury Experiences in China, visit: www.kpmg.com/cn

The European Chamber Comments on China's Luxury Tax

Recently, the Ministry of Commerce (MOFCOM) has indicated that import tariffs on luxury goods may be lowered prior to China's National Day celebrations on 1st October, 2011.

Approximately one year ago, MOFCOM submitted a proposal to the State Council regarding the revision of tariffs on imported luxury goods. This was called the 'Motion regarding the revision of Luxury Goods Import Tariffs'. The proposal included a wide variety of luxury goods.

On 15th June, 2011, a spokesperson for MOFCOM, Yao Jian, stated at a news conference that the government is considering a reduction in import tariffs to stimulate an increase in domestic spending. Earlier, Jiang Zengwei, the Vice Minister of Commerce had stated that reducing taxes on cosmetics and high-end watches would encourage domestic sales. It has been stated that a wide variety of goods, such as cosmetics, clothing, luggage, footwear, hats, alcoholic beverages and cigarettes will see a two to 15% cut in import tariffs, or will even become duty-free. Cigarettes and alcoholic beverages are expected to be among the first items to have their tariffs cut. In an effort to boost domestic demand and to attract Chinese citizens who make luxury purchases overseas to instead purchase these goods within China, these cuts are expected to be introduced prior to the national holiday that starts on 1st October.

Recent statements in the media have also indicated via MOFCOM's comments on a coordinated government action to lower relevant taxes on luxury goods. We welcome this initiative.

The European Chamber believes that as the Chinese market matures, domestic consumption levels rise and Chinese consumers spending habits change, the definition/classification of a luxury good also alters and consequently so should the tax levied on them. This will not just promote the healthy development of the concerned industries, but also encourage domestic consumption of these products and prevent the Chinese Government losing out on potential VAT revenue. Currently, some claim that Chinese consumers spend 4 times the amount abroad on luxury goods than they do at home, lowering the tax rate would encourage the purchasing of these goods domestically, thus likely raising tax revenue.

The Chamber also recognises that this initiative needs joint coordination from different government organizations and looks forward to the announcement of the practical policies and their implementation.

Clearing The Air:

China Moves Towards Private Aviation

That China would open its skies to more private planes was music to the ears of aviation industry executives and buffs around the globe. But the politics of private aircraft are far more complex, discovers EURObiz's **Steven Schwankert**, as he enters the world of the ultimate luxury product.

In its March 1 edition, state-run English-language newspaper China Daily published a curious photograph: police officers assisted an aviation enthusiast in dismantling his ultralight, small aircraft that essentially adds an engine to a hang-glider wing. The photo ran above the article, "City made into no-fly zone", which stated that "The skies above Beijing are to be made a no-fly zone as the city prepares to host meetings of the nation's highest bodies", the National People's Congress and the Chinese People's Political Consultative Congress.

The no-fly order not only closed Beijing's already highly restricted air space, but also instructed officials to work with aircraft owners to render their craft unusable, including removal of propellers and fuel tanks.

Although aviation officials have been quoted in recent months as offering support for "open skies", China's skies couldn't be further from open. Americans are accustomed to their president stepping out of the Marine One helicopter onto the White House lawn. But residents of Beijing still endure extensive and unannounced road closures when top leaders are driven, not flown, to the airport for domestic and international connections. During the 2008 Olympics, Beijing residents were surprised to hear helicopter rotors thumping overhead. Except for significant national celebrations, only birds have clearance to fly over China's capital city.

One major impediment to the expansion of private aviation in China is simply airspace. With one plane taking off and landing in Beijing every 40 seconds, anyone who has flown domestically in China in the last year can attest to significant delays and crowded aircraft. International airlines have complained of an inability to secure take-off slots, even when routes have been approved by CAAC. Bargain and regional airlines

have seized the opportunity taking late-night schedules to avoid midday congestion.

Even without adding a single private plane to the sky, China expects to increase the number of commercial aircraft from 2,600 in 2010 to 4,500 in 2015, and build 45 new commercial airports, according to CAAC, resulting in 450 million passenger trips by 2015. All of that is backed by 1.5 trillion yuan (162 billion Euros) of planned investment in the aviation sector, Li Jiaxiang, head of CAAC, told Chinese media in February.

Flying the Not So Friendly Skies

It wasn not so long ago that when flight attendants announced that flights from Beijing to Hong Kong would pass over a string of cities including Jinan, Shanghai, Changsha and Guangzhou, they weren't kidding. Until a few years ago, all civilian and commercial aircraft were required to vector from city to city through fixed, narrow air lanes.

The boom in air travel, and growing number of air travel-related delays, has even spawned its own government-sponsored backlash. Congestion, especially during the spring and summer months when flights into and out of the Greater Shanghai area suffer severe disruptions due to thunderstorms and other inclement weather, has become such an issue that the government accelerated deployment of high-speed rail between Beijing and Shanghai, which began service in June.

The main obstacle to general aviation expansion is the one that is most widely known and least discussed: the People's Liberation Air Force (PLAF). Officially charged with protection and management of China's skies, the PLAF controls about 75% of Chinese airspace directly, leaving only 25% for the country's massive and growing civilian market. By contrast, in the U.S. only 20% is controlled by the military, and in Europe the percentage is even lower.

Foreign aviation representatives said that it's a problem they just can't solve, although they say at least the PLAF has acknowledged the situation in the face of growing airborne gridlock. "The [airspace] closures are arbitrary and of course are never announced in advance. But there is nothing we can do about it," said one foreign aviation official, speaking on condition of anonymity.

Cai Jun, head of the air traffic control department under the general headquarters of the PLA Air Force, told China Daily in an interview that airspace will be divided into "restricted" and "monitored" areas, although management of both areas will still require the filing of flight plans. Cai also indicated that while air management processes will become simpler, actual enforcement will become stricter.

In fairness to aviation officials, this all-or-nothing style of management is also employed along China's coastline. The People's Liberation Army Navy (PLAN) has similar sway over the nation's littoral and blue-water areas. A Hong Kong-based sailor wishing to captain his or her own vessel up the coast to an anchorage near Tianjin would require permission from approximately 60 different coastal jurisdictions, with assent from one not guaranteeing similar agreement with another.

Aircraft Sales: Up, Up and Away

Despite all of these restrictions, in the same way that choking traffic in many major cities has failed to dampen enthusiasm for automobile ownership, civil aviation is likely to grow 11% in the next four years, requiring 1,100 new aircraft to satisfy demand, according to a report China Daily. Airbus has sold 20 business jets in China since 2005, accounting for 25% of its total sales in that sector, the newspaper reported. Along with Gulfstream and Airbus, France's Dassault Falcon, the U.S.'s Boeing and Canada's Bombardier are all in the hunt for a share in China's growing market.

China's 12th Five-Year Plan calls for the development of general aviation – the term for flying activities by private citizens in their own aircraft – but that blueprint will not suddenly fill the sky with small planes.

Still, the development plans are good news for aircraft manufacturers and service providers interested in serving the most exclusive of markets: Chinese tycoons looking for the ultimate bauble, their own private plane.

"People here wouldn't let their mail travel on an airplane with a propeller", said Jeff Anastas, of Kansas-based general aviation manufacturer Hawker Beechcraft. Unlike their counterparts in Europe or the U.S., Chinese millionaires look down on propeller aircraft and have no interest in flying the plane themselves. For China's newly wealthy, owning a private plane is just like buying a limousine with wings: sit in the back and enjoy the ride.

Even under new, relatively more liberal regulation, private aviation in China still doesn't resemble that in Europe or North America. Even after purchasing an aircraft, the owner is still grounded until he or she hires an operator, such as Hainan Airlines, to manage and fly the plane. Flights can be arranged on the second day, especially between major cities. Same-day flights are also possible but more difficult.

"There are a lot of things holding aviation back here; most of it is perception", said Anastas. Some of the other obstacles include a lack of general aviation facilities. While building large airports are a symbol of prestige for up and coming Chinese cities, constructing a small airfield for non-military use is almost inconceivable.

General aviation plays more than just the role of giving the wealthy an additional playground. For China's massive population, it creates yet another possibility for travel, especially to remote areas. "China realizes they can't build train tracks to everywhere", Anastas said. "This is about connecting people who spend money, and about creating jobs."

While captains of industry could potentially use their aircraft for business purposes, for now, private planes in China are still just baubles with wings. "These aren't gaudy symbols of wealth, they are business tools", Anastas said, expressing a viewpoint that's gaining little traction here so far.

For the moment, general aviation in China remains for most a passive experience. Just as any nation's *nouveau riche* express their newfound wealth by buying a luxury car with a driver, making it in China so far means sitting in the back, not at the controls.

"Pilots fly the plane; the buyers don't identify themselves as pilots," Anastas said. "People wouldn't see themselves as pilots because they didn't go to university to learn to fly."

The First Private Pilot

Cyrill Eltschinger, a native of Switzerland's Freibourg and a long-time Beijing resident, is uniquely qualified to comment on the general aviation market: in 2000, he became the first foreigner since 1949 to be licenced as a private pilot in China.

After first earning his pilot's license in Germany in 1992, he has since sought endorsements in every country where he has been resident for any significant period of time – 10 in all – including countries in Europe, North America, Asia and Australia.

Hoping to do the same in China, Eltschinger began looking into the licencing regime. "Altogether, it took me five years to work my way through the system. There was a basic process, but no one had ever done it before", he said. "In some ways I was required to prove my qualifications. In other ways, I was helping to create the process itself."

Strangely enough, instead of testing for his licence on an aircraft designed for civilian use, Eltschinger qualified on a World War II-vintage, Russian-designed Yakovlev single-engine fighter-trainer, still in use to provide early flight experience to young Chinese pilots.

"It's a great aircraft. Unlike planes today with their digital read-outs, the Yak(ovlev) has analogue gauges, sometimes you even have to tap on the glass to get the needle to read correctly. That's real flying," he said.

Like many aviation aficionados, Eltschinger sees a greater opening of the skies as an opportunity to relieve commercial congestion elsewhere. Because general aviation aircraft fly at lower altitudes than commercial jets, and usually utilize different, smaller air fields than those where the major airlines are based, more of the


Hawker Beechcraft cockpit


Hawker Beechcraft inside cabin

sky can be used, and more effectively. Given the opportunity, Eltschinger would buy his own aircraft.

"In China, that is the only way to go, especially considering the traffic that has started to soar in most major cities, not just tier-one cities, but tier-two and tier-three cities as well," he said.

He also believes in the unique experience that private aviation can offer, more than just point-to-point luxury travel. "The best flying I've done has been along the Great Wall near Datong, four hours west of Beijing. The area also has a beautiful temple up on a high hill, and some man-made caves not too far away. In Anyang in Henan province, we did some formation flying training, with two other pilots, flying three Yak(ovlevs) together. Really cool", Eltschinger said.

Other experiences are more of a mixed bag. "At some air fields, you can only circle the area. You have to fly around in a circle within eight kilometers of the landing strip, and stay under 1000 meters. It's better than nothing I guess", he said.

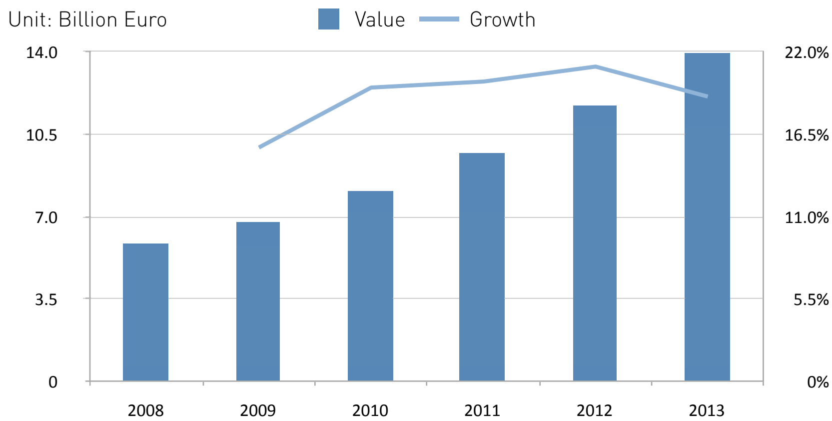
Eltschinger's mind soars far beyond eight kilometers from a landing strip when he talks about his ultimate flying adventure. "My dream flying trip would be to fly all around China, visiting all of the border provinces." Eb

China's Luxury Market

China's Luxury Market Overview

In recent years, Chinese personal disposable income levels have increased rapidly, which help release the consumption power of Chinese people, especially of the middle class. China's luxury market (referring to luxury watches, cosmetics, bags and suitcases, clothes, jewelry and shoes, not including luxury cars) has gradually increased during this period. The growth of China's luxury market has been the fastest in the world in recent years, reaching a total value of €8.07 billion in 2010, up 19.6% from 2009. Over the next several years, All China Marketing Research Co. Ltd. (ACMR) expects this sector to continue to increase at a rapid rate as the Chinese government makes great efforts to the expansion of the domestic consumption market.

Total value of China's luxury market, 2008-2013

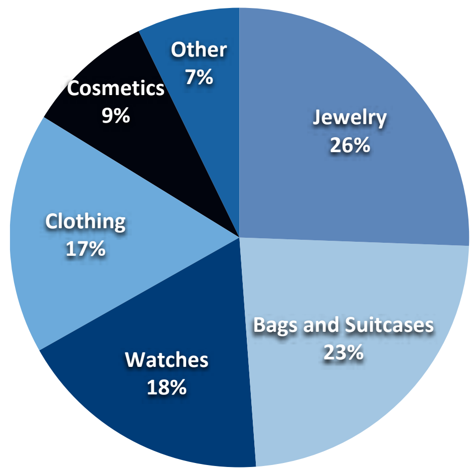


Data Source: World Luxury Association, ACMR Industry Research

Market Segmentation (in terms of Sale Value in 2010)

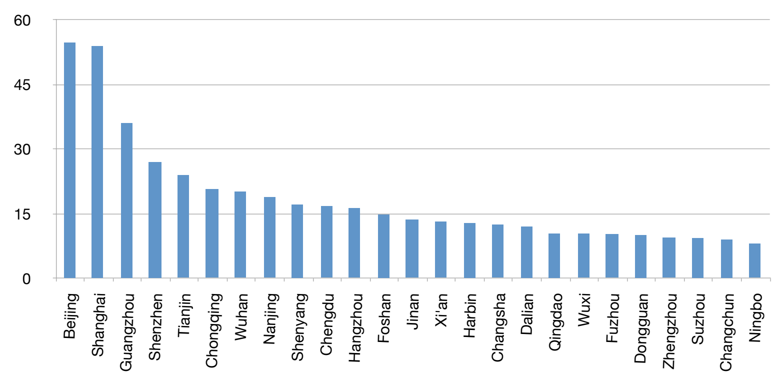
In terms of market share, jewelry remains at the top. With the rapid increase in demand for personal use and business gifts, bags and suitcases have been the second-largest luxury market segment. Watches come third, mainly supported by the strong sales of medium-priced watches and increasing collector demand for high-end watches among male consumers.

Data Source: World Luxury Association, ACMR Industry Research



Top 25 Cities in China in Terms of Total Retail Sales of Consumer Goods in 2009

Unit: Billion Euro



One of the major drivers behind the fast expansion of China's luxury market is the growth of consumer sales in China's major cities.

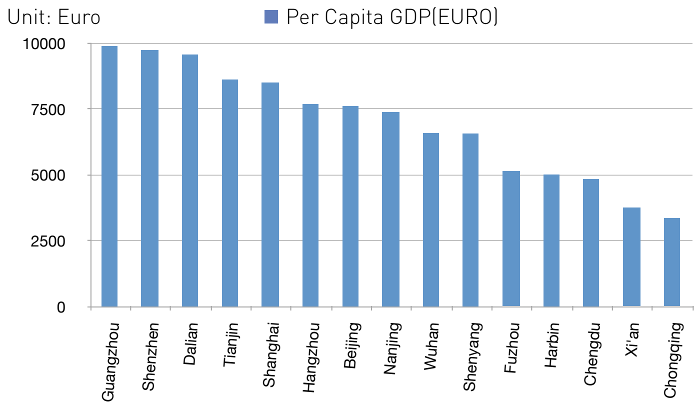
Total Retail Sales of Consumer Goods (Billion Euro)

Data Source: National Bureau of Statistics of China, ACMR Industry Research

Per Capita GDP in China's First and Second Tier Cities, 2009

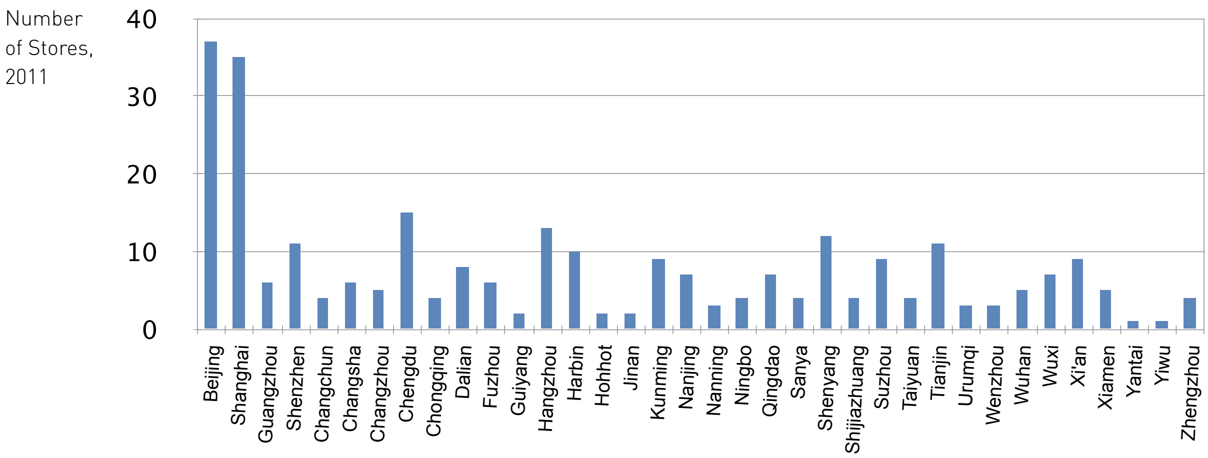
Commercial economies are developed and per capita GDP levels are comparatively high in these cities relative to the average.

Data Source: National Bureau of Statistics of China, ACMR Industry Research

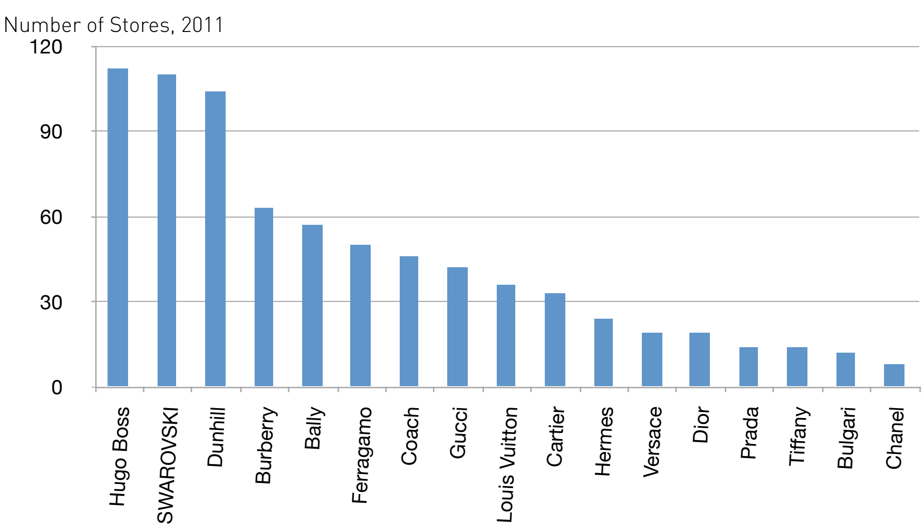


The Number of Stores of Luxury Brands in China, 2011

Major luxury brands have been entering and expanding rapidly in China to grasp the great potential of this emerging market. In 2010 and 2011, major brands accelerated their expansion in China. According to ACMR statistics, from August 2010 to May 2011 alone, six brands including Hugo Boss, Dunhill, Burberry, Bally, Gucci and Hermes have opened 64 new stores in China. They are expected to expand more rapidly in the near future. Burberry plans to increase the number of stores in China from 63 to 100 in five years, PRADA from 14 to 30 as of 2013, and Tiffany from 14 to 24, in five years.



Data Source: ACMR Industry Research, Public Information



Data Source: ACMR Industry Research, Public Information

All China Marketing Research Co. Ltd. (ACMR) is a leading provider of business information and market research, focusing on collecting, studying and analyzing data and information on the macro economy, industrial sectors, enterprises and business markets in China. www.acmr.com.cn

Hitting The Target

Veteran China marketer **David Wolf** takes a look at Beijing's new restrictions on luxury advertising, and how companies can turn them into better and more creative marketing messages.

Restrictions placed on luxury outdoor advertising in Beijing are aimed not at the goods themselves, but at ending ostentation. While it is too early to say whether the restrictions will be broadened to other cities or other media, there are several reasons that the measures should give pause to all in the business of marketing luxury items, whether they be gadgets, gold, leather goods, or private aircraft.

First, the measures are a reminder that advertising luxury goods in China's mass media is wasteful. Too many of the impressions, or ad appearances, in outdoor advertising are received by people who not only have no intention or ability to buy the product advertised, they will likely never have the ability to do so. Media companies may argue that those impressions that are not wasted are worth all of the other waste, but do not forget that the waste factor is immense.

Second, the measures are a signal that there may be such a thing as negative effectiveness when making desirable the unaffordable and unreachable. It is assumed there is spillover, but the effects those spillover impressions have on the "wasted" audience are never actually tracked. Are the messages and ads simply ignored? Or do they engender a negative reaction? Are marketers, as the Beijing Administration of Industry and Commerce apparently fears, seeding resentment that undermines social harmony? How would anyone know?

Too many of the impressions, or ad appearances, in outdoor advertising are received by people who have no intention or ability to buy the product advertised.

Third, the measures are a reminder that the end (selling more baubles) does not always justify the means (any creative that gets the buyer to pay attention). There are ways to create mystique and value with an advertising campaign that are more imaginative than pairing a luxury good with a panorama of a luxurious lifestyle or with a half-naked supermodel. Are there ways to ensure that the results of the spillover are positive? And if so, shouldn't that be the course pursued?

Why Should We Care?

All of those questions can be dismissed by marketers as "not our problem", and a fair case could be made that we would be technically correct in doing so. After all, marketers are paid to deliver sales, not worry about people who are angry at being unable to buy the product. In fact, when thinking about it, such frustration might actually be a good thing.

Such rationalisation is perfectly true, right up to the point where the government decides that the ad upsets too many migrant workers. At that point, the ad may be cancelled, or the advertiser may lose access to a channel completely. The smart move is to think ahead, and that begins by buying into some basic principles.

Four Principles

Principle I:
There are more effective ways to market luxury goods in China than mass media.

A corollary: there are now more ways than ever to conduct effective luxury goods marketing. Even if with a fixation on paid media, using direct mail, flagship stores, relationship marketing, carefully selected online media and, when it comes, mobile media are better choices. In fact, luxury brands should be driving the push to online marketing that individually targets a user, rather than just takes space on a page.

In luxury goods more than any other industry, it is even possible to lead with below-the-line approaches like tightly-targeted public relations, trunk shows, store openings and other tactics that take a personalized, bespoke approach to marketing and eschew writing advertising checks altogether. The options continue to grow and they keep getting more tightly targeted. For example, Cartier sends a birthday card every year to a customer who made a single small purchase on the basis of word-of-mouth.

Principle II:
Learn to understand, measure and avoid "negative effectiveness" in marketing in a country with deep and active social fault lines, regardless of what is being sold.

This does not apply only to China, but to any country in which a luxury brand sells. Marketers are very good at understanding the positive consequences of communications, even if they do a mediocre job of measuring them. But they may also ignore the negative consequences until they blow up in the marketer's face. Until marketers learn to measure how many people are not only not attracted by an ad or message, but are actually upset by it, why it does so, and understand what that means for the brand, then it's possible marketing may well be doing more net damage than good.

On the other hand, if campaigns get the target audience to buy and also engender goodwill from people who will never buy the products, it lifts the brand and the products to an entirely new level.

Principle III:
In enlightened self-interest, those in the marketing profession need to behave with greater sensitivity to the people at the bottom of China's pyramid.

This requires no great explanation, just a thought. After nearly 34 years of reforming and opening, China is still home to hundreds of millions of people who live on less than 1 euro per day. Before submitting an ad for approval, picture it in a photograph: the ad, on a bus shelter, with a poor Chinese farmer in a threadbare blue Mao suit walking past. If that image looks wrong, rethink the ad, if not the campaign.

Alternately, imagine the ad copy or messages being read aloud to a meeting of senior Party ideologues. Does it still sound okay? If not, rewrite.

Rolex's ads have a distinct aura of class, style, and excellence, and have helped establish the company at the top of the luxury timepiece market, all without sex or decadence.

Principle IV:
Great luxury marketing goes for the brain.

It is a huge temptation to conduct marketing that appeals to baser instincts. It's easy, it gets attention, and it sells. Leaving aside any moral issues, using such an approach to sell luxury goods is probably what caused the current situation with the outdoor advertising restrictions. And it is just unnecessary.

Take, for example Rolex, a great luxury brand. For decades, the company has been running a campaign celebrating explorers, pioneers, and other people of noted excellence in their fields of endeavor. These are not people getting out of Bentleys or fondling the latest Victoria's Secret model. The ads have a distinct aura of class, style and excellence, and have helped to establish Rolex at the top of the luxury timepiece market, all without sex or decadence.

Not every luxury company can use the same strategy as Rolex, but marketers are paid for creativity. Any halfwit can conjure (or approve) an ad campaign that speaks to greed. Good marketers – and wise clients – know that they don't have to. That applies triple when selling high-margin merchandise like luxury goods.

Selling Baubles Better

There is a business case behind each of the four principles, such as maximising efficiency, minimizing the chances of blowback, or creating more memorable and meaningful campaigns.

When marketing luxury products, it creates the desire for the unnecessary. That is the hard truth. Doing so is defensible, though perhaps not a virtue, when the desire is created in people who have more money than they can spend. But it is indefensible when aimed at people who have less money than they need, and it is reprehensible to say that such accidents are not a problem.

Great companies, great brands, and great executives do not shy from that quandary. Instead, they let that struggle be a part of what defines them, not just because doing so offers great commercial rewards (it does), but because it is the right thing to do. That essence should be a part of every brand, but the obligation rests heavier on those who create and sell the finer things in life.

David Wolf is the CEO of Wolf Group Asia, a Beijing-based management advisory firm providing strategic communications counsel to companies. www.wolfgroupasia.com Eb

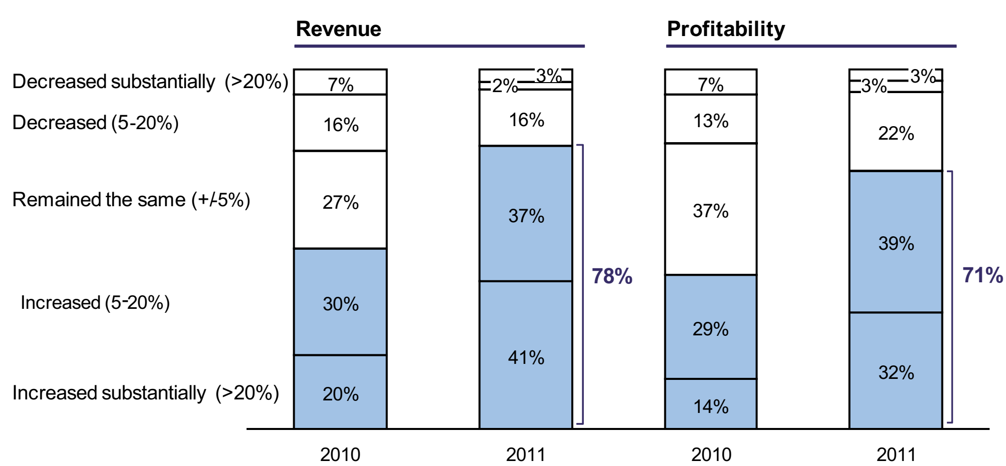
The European Chamber's Business Confidence Survey 2011

China has emerged from the global economic crisis as a key market for growth for many industries. This growth was mainly driven by public investment. Many industries have participated in it directly; such as through increased purchasing, indirectly as part of the supply chain, or through the trickle-down effect to the consumer level.

Earlier this year the European Chamber of Commerce in China surveyed its 1,600 member companies for its annual *Business Confidence Survey*. The results, published in May 2011, are the most comprehensive and wide-ranging set of data yet collated for the annual publication.

The survey reveals that European companies are doing well in China, with the vast majority of the almost 600 respondents reporting positive net profit in 2010 as well as impressive growth in both revenue and profit over the previous year. Most companies are confident about the future growth of China's market, spurred in part by optimism over the impact that China's 12th Five-Year Plan will have on the business environment and are willing to invest during the next two years to participate in this growth.

DEVELOPMENT OF REVENUE AND PROFITABILITY, 2010-2011



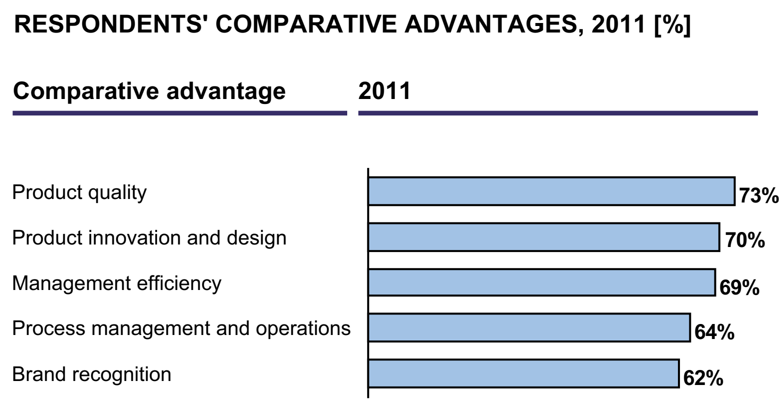
China is clearly becoming more strategic for our members. Performance in China has now become crucial for global success and failure is no longer an option. This does not mean it is getting easier to enter or operate in China. Competition is fierce and foreign-invested enterprises (FIEs) and domestic enterprises alike are stepping up their game. Scarce human and natural resources are leading to more pressure on recruitment for talent, as well as rising input costs.

The Survey also reveals that companies perceive a further deterioration of the playing field: more than a third of respondents signal that over the last two years, government policies have increasingly discriminated against FIEs; and nearly half of the respondents believe that discrimination will get worse over the next two years.

High Stakes

The European Union recently became China's largest trade partner, for exports as well as imports. Despite the imbalance in trade volume, this relationship is one of mutual benefit. Chinese goods serve European customers, and European industry participates in China's remarkable growth. The Survey shows that FIEs are aware of the growing strength of domestic companies in areas such as marketing and sales. They are however confident in their own ability to compete in China, based on quality, innovation and design, efficiency and process management. [1]

[1]



Furthermore, European companies are global leaders in many of the industrial areas that are closely aligned with China's macro objectives to promote high-tech, energy efficiency and sustainable growth. As such, they are well positioned to contribute to China's economic growth model as outlined in the 12th Five-Year Plan.

Healthy Competition Drives Excellence

According to the Survey, both the revenue and profit of European companies are growing. Profit margins in China are at about the global average with almost equal numbers of survey respondents noting that profit margins in China are either the same, lower or higher than their average worldwide margins.

Given the current high-growth stage of the Chinese economy and that approximately three-fifths of respondent companies are considering major new investments in the next two years, it's fair to assume that most of that profit is reinvested in China.

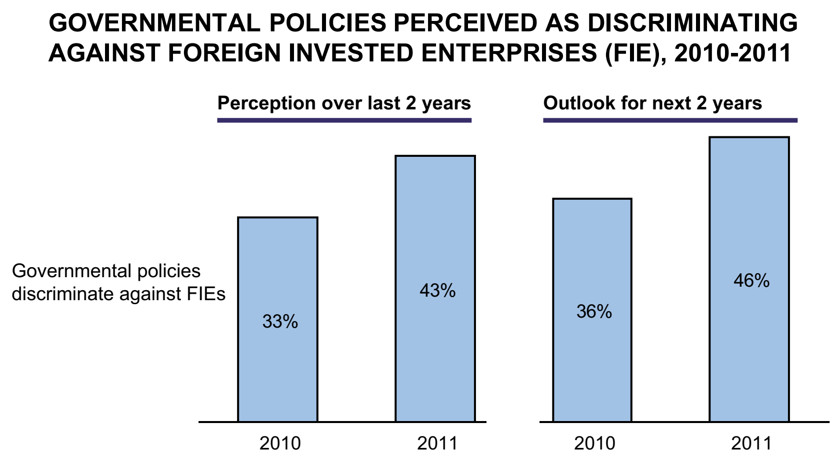
While European companies are confident in their ability to engage in fair and healthy competition, they also mention that Chinese companies retain competitive advantages in government relations, and access to subsidies and financing. With competition increasing and with costs rising, our members tell us that the need for a transparent and well-regulated market has become more important than ever before.

A Fair Deal?

43% of European companies perceive the Chinese regulatory environment to have become more unfair towards foreign companies over the last two years. [2] Moreover, an even greater 46% expect this trend to continue. Approximately one quarter of European companies believe that China is actively looking for loopholes in the World Trade Organization agreement to avoid making required changes. An even greater 31% believe that there is a regulatory willingness to make the required changes, but that implementation is lagging.

This perception of implementation problems is in alignment with the top two regulatory obstacles that were identified within the Survey, namely a discretionary enforcement of broadly-drafted laws and regulations and a lack of coordination between different regulators. [3]

[2]



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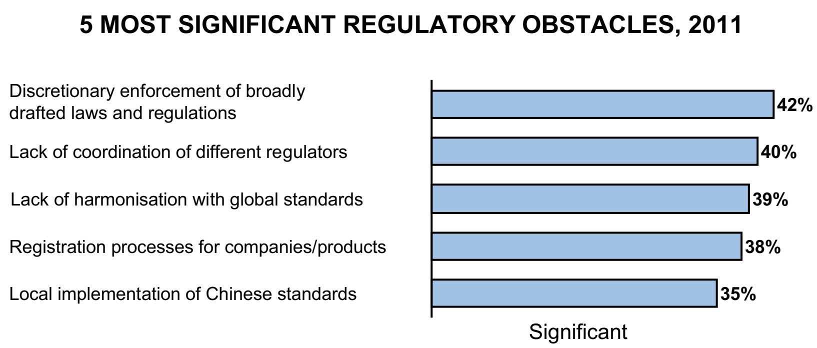


China must follow through, not only with improved and fairer regulation, but with implementation of regulation at all levels of government. Rule of law and predictability are imperatives for business planning for any well-run company. Due to perceived gaps in these enablers and as a direct result of anticipated government policies, one in five European companies has suspended or is reconsidering their investment plans.

The release of the draft form of the Foreign Investment Catalogue in April disappointed many foreign companies. While the European Chamber welcomes the opportunity to comment on the Catalogue, as the first major implementation document following the release of the 12th Five-Year Plan, it indicates few if any changes in terms of market access for foreign companies. This would have been a good starting point for the liberalisation of various industrial sectors to foreign investment and participation.

The *2011 Business Confidence Survey* demonstrates that despite an uneven competitive environment, European industry is doing well in China. A level playing field to both, face increasing competition and to drive excellence is in the interest of all companies in China, regardless of their source of funding. The biggest hurdle to achieve this is, as it has been for many years, the comprehensive and coherent implementation of the thorough legal and regulatory codes that have been enacted by the Chinese government. Given the size and the importance of the trade relationship between China and the European Union, closer cooperation towards building open markets can only benefit both sides. Eb

China's New Social Insurance Law:

What It Means for European Business

One of the most important business events of the summer took place on 1st July, when China's new social insurance law came into effect. Announced late last year, the impending inclusion of foreign employees as part of the scheme has made it a hot topic and a cause for concern among European businesses. **Grayson Clarke** explains the new act and what it means for companies operating in China.

European Chamber event on the New Social Insurance Law, 14th June in Beijing.

It has been 125 years since the first social insurance system came into being in Germany and 100 years since the United Kingdom passed its first National Insurance Act. Will China's law have the same momentous impact as these pieces of legislation had or will the law prove something of a false dawn?

At first glance, the law should not be expected to have the same impact. China's social insurance system has been around on a nationwide basis since the late 1990s, and without any primary law the system has expanded massively in terms of the number of schemes, participation, and funding. The main enterprise pension scheme alone has 250 million workers. That history is partly reflected in the nature of the law, which is evolutionary rather than revolutionary, codifying what is there already rather than introducing radical changes or new schemes.

Nevertheless it is easy to underestimate its potential impact. The law contains some important new provisions, in particular those relating to transferability of entitlement between different regulators, unified social insurance collection (which should reduce costs for business), improved financial management and transparency and legal recognition of social insurance fraud.

The article of the law that has particularly caught the eye of European business is the inclusion of foreigners for which the Ministry of Human Resources and Social Security (MOHRSS) introduced its first draft regulation under the law on 10th June. This regulation has immediately caused some concern around the possibilities of a situation akin to double taxation and a serious increase in the costs of employing foreign workers. There are likely to be a number of reasons why this regulation is the first one to be released. It is one that causes almost no dispute within the various interested government ministries. It is likely to spur the conclusion of bilateral agreements between countries for which there are only two at present, in place with Germany and South Korea. The Japanese government is believed to have deferred negotiation until the law was in place. It may also have an indirect but not unwelcome benefit for the Chinese government in accelerating the localisation of middle management positions, although the cost impact on foreign high-wage earners is likely to be constrained by the operation of upper earnings limits. On the other hand as China perhaps drafts in more international migrants in the future to make up for its declining labour force, many of these workers may appreciate the benefits of being in a better social protection system than offered by their home countries.

It is symptomatic of the lack of detail that pervades both primary legislation and regulations that there is still considerable uncertainty about how the new system will operate. For example, Article 97, which provided for the inclusion of foreigners, did not include explicit provision for Chinese working abroad to maintain their own social insurance regulations in China. Similarly the draft regulation makes no mention of how pension or other long-term service benefits (e.g. for work injuries) may actually be paid out if the foreign worker moves back to his home country. The application of unemployment insurance proposed by the regulation would appear to be illogical given that work permits are tied to specific employment, and there is no general right for unemployed foreign workers to remain to seek employment in China.

More generally, the law is very short and primarily framework-based, leaving much difficult detail to be resolved and implemented through State Council and inter-ministerial regulation. A number of difficult territorial disputes exist, particularly between the Ministry of Human Resources and Social Security and the Ministry of Finance over social insurance collection from the employment-based schemes, and also the investment of accumulated funds and with the Ministry of Health over responsibilities for rural health insurance. A key element in the success of the new law will therefore be how quickly some of the differences between stakeholders can be resolved and new implementing regulations issued. At present the timetable for finalizing the regulations remains very unclear, and the recent Round Table in Prague the government representatives said it could be two or three years before all the regulations were in place even at the national level, which would seriously dent the impact of the law.

The most fundamental problem with the law is that it fails to resolve a number of big picture issues that remain as pertinent today as they were in 2006, when the European Union-China Social Security Reform Co-operation (EUCSS) Project began.

The first is the cost of social insurance. Joining all five social insurances plus (for those with local hukou) the local housing funds is expensive, taking up well over 50% of the payroll in most localities, which is a high figure in international terms and particularly for developing countries. This represents a formidable deterrent to enroll for both employees and employers particularly in the face of rising wage costs.

Grayson Clarke and interpreter Zheng Xijun at a social insurance office in Shenzhen looking at individual contribution records on screen.

Reducing this figure to a more acceptable figure of about 35% requires sorting out the local housing funds and pensions, which contribute the bulk of the total cost for employers. Limiting the employer contribution to a small percentage aimed at raising funds for public housing schemes and combining a smaller individual account, perhaps with the medical insurance individual account on a Singapore-type model, could reduce percentage contributions to housing to no more than 7%.

For pensions, a key issue has been that the funds have gone to pay for the past generation of those workers who retired from state-owned enterprises in the 1990s and before. While the Ministry of Finance contributes large subsidies to the pension system (156 billion RMB in 2011) these have never been properly matched and adjusted to take care of these legacy costs leaving the social insurance funds struggling to provide for the current generation of workers and the past generation of retirees. Increasing the level of subsidy to fully fund these legacy costs could allow a cut of perhaps 5% in the employers' pension rate. These two measures together may in the longer term raise the level of participation and overall amount of contribution.

The second issue that is linked to the legacy cost issue is the question of what to do about the individual enterprise account that is part of the urban enterprise scheme. This has become more acute since the introduction of the new style rural pension, with individual accounts in 2009. In the urban enterprise pension system, most individual accounts are kept nominally on a bookkeeping basis, with the funds that should have gone into them used to pay existing pensioners. There was something of a half-hearted attempt to refinance these, but since 2006 this has been in abeyance and funds restricted to low interest-bearing bank deposits have been losing money in real terms. Since the government has sanctioned the individual account in the rural system, because it appeals to the culture of individual saving, one strong possibility for the government would be to externalise the management of these funds to licensed fund management companies as has happened in much of Eastern Europe. This would

A team photo from the recent EUCSS Round Table in Prague.

save the government the responsibility and cost of managing the funds directly and through providing additional tax or matching incentives could increase the volume of private pension saving.

A third problem relating to the financial sustainability and administrative cost of the scheme concerns the level of pooling and the number of small local schemes that run into the hundreds. Although the government has a target of raising the pooling level through the law to national level for pensions and provincial level for other insurances, in practice this has largely meant that municipal and county level local governments run the schemes as they have always done but with more fund transfers to plug gaps. This is neither fair nor efficient. It has meant that the level of benefits is somewhat dependent on location (the postcode lottery as it is called in the United Kingdom). It also makes the administration of the schemes inefficient with multiple non-communicating IT systems; and many small-scale local schemes exist under the radar of effective supervision with the ever-present danger of fraud and theft. It will be a critical test of the new legislation to set down regulations that will enforce higher level pooling and scheme unification.

Finally, and linked to the administrative organisation issue, is the capacity of civil servants. Our project has been proud to sponsor training for over 8000 participants from social security agencies. Yet it remains a drop in the ocean. For example, the central actuarial division in consists of only three staff, none of whom are fully qualified actuaries. Social security needs to be recognised as a proper career in government and its civil servants at all levels trained in appropriate disciplines. Only a systematic and well-financed capacity building programme supported by both central and local government can give China the administrators it needs and deserves.

With the world economy still uncertain and with an ever-increasing proportion of the working population likely to change jobs on a regular basis in the future, social security is not a luxury but a necessity for the development of a harmonious society. As the EUCSS project comes to its conclusion at the end of July, we have been proud to contribute in whatever small way to the development of China's system and look forward to seeing its progress in the next decade.

Grayson Clarke ITAT Expert for Fund Management EUCSS Project. The EU-China Social Security Reform Co-operation (EUCSS) Project is a five year forty million Euro co-operation project, launched in April 2006 which has the overall objective of supporting the transition to a sustainable social security system in China. The Project consists of two interlinked components: The 1st component works with central government on policy related reforms; and the 2nd component supports the implementation of selected reform initiatives in 6 pilot provinces.

ALLEN & OVERY

Disclaimer: Allen & Overy LLP's introduction and contact information have been amended as below.

Allen & Overy LLP, Beijing Office
Legal Services

Firm introduction:

Allen & Overy is one of the largest world's international law firms and has a global integrated practice of approximately 490 partners and more than 2,000 lawyers in 36 offices located in 26 countries in the Asia Pacific, Europe, the US, South America and the Middle East. We provide first-tier legal expertise in all major areas of commercial law, including banking and finance, energy, infrastructure and projects, M&A, FDI and joint ventures, private equity, real estate, capital markets, competition and antitrust, restructuring and insolvency, intellectual property, and dispute resolution (including litigation, international arbitration and mediation).

CONTACT INFORMATION:

Peter Thorp
Managing Partner, Mainland China

Address: Suite 522, China World Office 2,
No.1 Jian Guo Men Wai Avenue, Beijing 100004, China

Tel +86 10 6505 8800
Fax +86 10 6505 6677

email: allen&overychinamarketing@allenovery.com
website: www.allenovery.com

David Marsh: A New Currency Constellation

As the Euro continues to travel on shaky ground due to financial crises in countries like Greece, some observers are speculating about the future of the unified currency. Simultaneously, China is increasing its Euro holdings to offset its reserves of other currencies, to the delight of European regulators. In this dynamic environment, EURObiz's Steven Schwankert talks to **David Marsh**, Co-chairman of monetary think-tank Official Monetary and Financial Institutions Forum (OMFIF) about the Euro's future and China's plans for it.

EURObiz's Steven Schwankert interviewing David Marsh after the European Chamber's Breakfast event on May 20th, in Beijing

EURObiz (Eb): You've used the phrase "new currency constellation". What do you mean by that and what is the Euro's role in it?

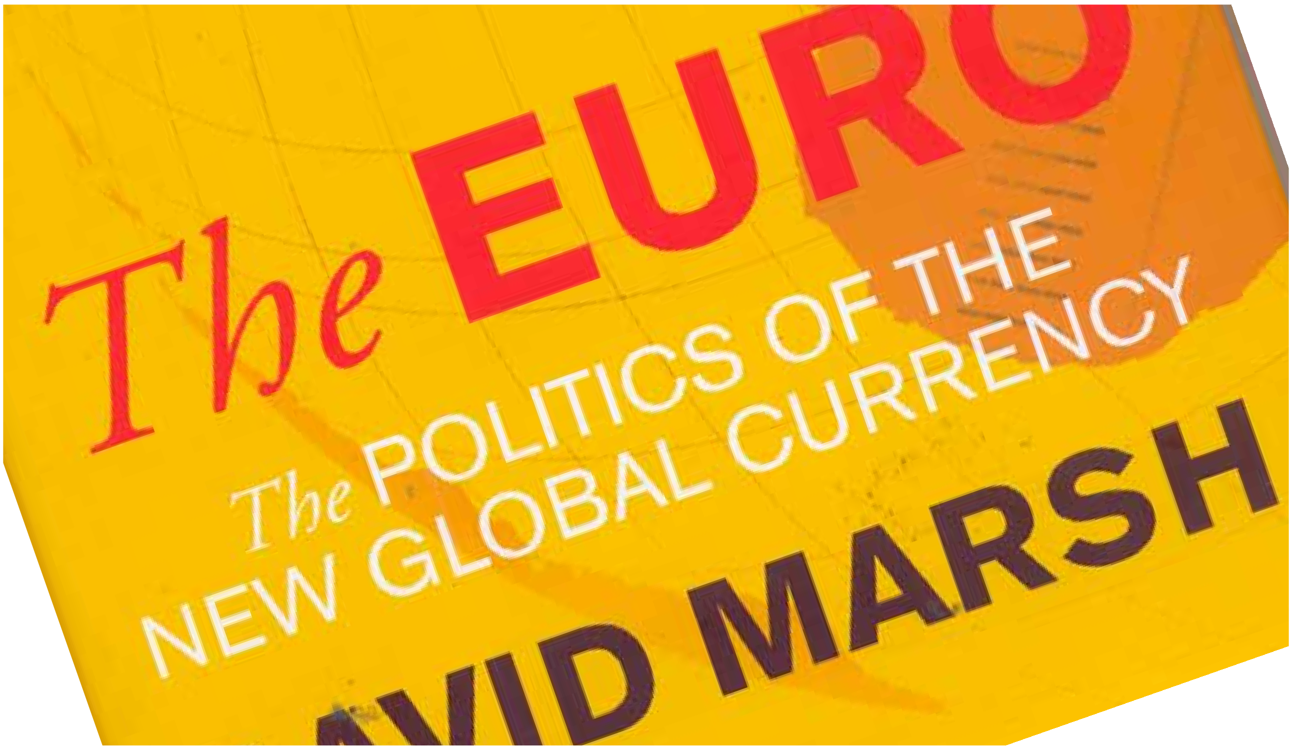
David Marsh (DM): The dollar's weight in the world is bigger than it should be, in relation to total dollar-settled trade. About 60% of the world's foreign reserves are held in dollars, the Euro, about 27%, and then the rest is in other currencies. Currencies are moving to a point where they will co-exist in world trade and in world money. More currencies are now jostling with each other. This could make the overall situation possibly unstable but can be handled with capital controls.

This transition involving the dollars, the Euro and the Chinese renminbi (RMB) will only take place over the next 10 years. We will also see some kind of rise in the use and convertibility of currencies from the BRICS countries (Brazil, Russia, India, China and South Africa), and perhaps even the rupiah from Indonesia.

Eb: You've also talked about the concept of a new Euro. What do you mean by that?

DM: One way that countries and governments can handle financial crises like we have seen is to devalue their currency, but as part of the Eurozone, that is not possible. Given what we have seen in places like Greece, Ireland and Portugal, it's difficult for small countries to remain part of the Euro with the austerity measures that need to be put in place. There are signs with some of the larger countries, namely Germany, getting fed up with having to provide the amount of loans and guarantees that they have had to in order to shore up the currency.

It is possible that we may see some of the Euro's larger participants suggesting to some smaller countries to leave quietly and go back to their own currency, in exchange for some kind of economic support package. That is something those countries would have to decide to do of their own free will and it is a very delicate economic



David Marsh's book "THE EURO – THE POLITICS OF THE NEW GLOBAL CURRENCY".

game, but we could see it happen in some form.

Eb: Do you think that currency will become a political issue in Sino-European trade, the way that the value of the RMB has in trade between the U.S. and China?

DM: I don't think so. Europe has a more positive view of China as a partner and friend. People there don't worry as much about currency issues until it begins to affect them much more directly.

Europe is a big destination for Chinese goods – the Sino-European trade relationship is larger than that of Chinese trade with the Americans. And China most likely will want to increase its relationship with Europe's smaller nations.

Eb: How can the two sides improve currency and economic ties?

DM: There needs to be, and I think there will be, more cooperation between the two sides, specifically between the People's Bank of China and the European Central Bank, along with more swap lines, more lending, more training and more technical exchanges.

Ultimately, this relationship offsets American dominance. That doesn't have to be a bad thing for the rest of the world.

The Euro gives Europeans, especially smaller nations, the ability to form a cohesive unit where it would be otherwise difficult for them to get an equal seat at the table with China.

Anything that China can do to upgrade its processes benefits Europe. China still needs a lot of technology from Europe.

It is also worth noting that intra-European trade has dropped in relation to Europe's trade with Asia, so the relationship takes on added importance.

Eb: Tell us about the release of your updated book "The Euro – The Politics of the New Global Economy", which is not only available in a new edition in English, but also now for the first time published in Chinese.

DM: I've been lucky, or unlucky depending on how you look at it, with the timing of my books. My first book was about Germany, and the book came out on Nov. 5, 1989, just four days before the Berlin Wall fell. Then I wrote a book about the Bundesbank, which was published in Sept. 1982, and shortly afterwards the U.K. left the European exchange system. My latest book came out in 2009, and predicted some of the failures that we've seen. I guess I'm like a pilot fish swimming ahead of the shark.

As for China, it has been a transition economy, not so badly hit by the financial crisis and leading the world out of recession. The U.S. is in the middle, with unbalanced growth. Europe has been stuck in the doldrums, although Germany has been growing, with 5-6% growth. It could, however, face inflation.

The biggest problem I see is that banks are still very weak in Europe, and public deficits are still very high. The best thing to do is try to avoid having another crisis while still recovering from the previous one.

Lobbying Europe:
Start Early and Maintain Transparency

Jeremy Galbraith is the CEO of public relations firm Burson-Marsteller for Europe, the Middle East and Africa. In an interview with EURObiz's Steven Schwankert, he explains why many remain "Euro-skeptic", the difference between a good lobbyist and a bad lobbyist, and why any European business person should care what legislation comes out of the European Parliament.

EURObiz (Eb): How are Chinese companies doing lobbying for themselves in Europe, especially at the European Parliament?

Jeremy Galbraith (JG): The lobbying companies in Brussels at the European Parliament are mostly British. The Americans and British were the forerunners in lobbying and they are still the strongest. There are few Eastern and Southern European lobbyists in Brussels.

Therefore, it is no surprise that Chinese companies are not engaged in lobbying. What they need is to have a full-time representative there. Using an agency makes sense, but it is not enough just to have a senior executive parachute in once per year.

In some ways, it is like the Chinese concept of guanxi. You have to build trust and you do that by making connections, and you make connections by visiting Members of the European Parliament (MEPs) from different countries. It is a process that takes time and regular attention, they need to get to know you and you them.

In the last six months, Burson-Marsteller has been approached by two Chinese companies. Nothing has been signed, but it is clear that at least some people are beginning to understand the process.

The European Commission can have a big impact on trade and business legislation – you need to engage.

Eb: What about the flip side: how are Chinese companies perceived in Europe, and at the European Parliament?

JG: There is a recognition that Chinese companies are going to increasingly be under scrutiny by European regulators and European consumers. That puts a lot of pressure on shareholders and creates a lot of heat. Chinese companies need to have a permanent presence in Brussels that will represent their interests and lobby on their behalf. This is particularly true for standards. Standards for products and services are areas that may keep companies, including Chinese companies, and others out and those interests need to be represented regularly.

For example, the EU sets global standards for product manufacturing. Its products tend to follow the highest possible standard in order to be sold everywhere without requirement for further qualification.

The average European consumer and uninformed opinion leader thinks China makes cheap plastic products. They don't think their iPods were made here. So there needs to be an education campaign. Also, the brands of Chinese companies need to be separated from that of their government.

European consumers trust most their local government, and their suspicion grows as you move farther and farther away from their home. That suspicion extends to the European Union and EU legislation, so therefore it is only natural that consumers reserve a certain amount of suspicion for foreign companies, including those from China.

Eb: What is the difference between a good lobbyist and a bad lobbyist?

JG: The research shows that bad ones are considered bad because they are not transparent. Sometimes companies or organisations will establish front groups that are not clear about their intentions, and in the end, it is never good for the company or companies that initiate it.

We have found that trade associations are the most effective of all lobbying groups, in terms of communicating their message clearly, asking for appropriate action and maintaining constructive relationships with the right people. Ultimately for lobbying, compromise is the name of the game. The other problem we see is people who are way too late to the process. Sometimes we get calls from a prospective client who says, "The European Parliament is about to ban our product, please help us."

On average, a piece of legislation takes about six years to work its way through the Parliament, so if it's gotten that far, by then it's too late. It would have been so much easier if we had been engaged at the beginning of the process.

Take for example chemicals and chemical additives. For chemicals, science doesn't always matter. The European Commission will consider the science. The Parliament is much more emotional.

Eb: How are MEPs making decisions today? What influences them?

EU politicians mostly do their own research, they are not particularly reliant on staff for that, and that research comes mainly now from digital media. As mentioned earlier, trade associations had the best results. Non-Governmental Organisations (NGOs) were less effective than industry. NGOs are too emotional.

In terms of communications, meetings remain the best form of engagement. Get in early when policy is being formed, don't risk engaging either on the issue or with the MEPs too late.

Eb: What do European consumers respond to? Should companies be engaging in corporate social responsibility (CSR) activities?

JG: In Europe consumers respond to companies that are seen as being honest, trustworthy and offering good value, more than any CSR programmes the company may undertake. Consumers want to hear about company values not from the CEO, who are seen as being motivated by personal profit, but from their frontline staff.

Eb: Why should companies target the European Parliament, rather than trying to establish relationships in the major markets in Europe where they operate or sell?

JG: It's not that they shouldn't try to build relationships in those markets, especially if they have manufacturing in a particular area. But 90% of the legislation that affects business in Europe comes from Brussels. As such, companies would do best to concentrate their lobbying resources there.

Eb: You said in your presentation that China just doesn't necessarily care that much about its relationship with the European Union. Why would that be?

JG: On a geopolitical level, the United States is still viewed as the global power. There is concern about dealing with the European Union as a whole, rather than the relationships that China can have with individual member states.

Ultimately, the European Union is driven by France and Germany, and especially by the elites in those countries and elsewhere in Europe. Eb

Jeremy Galbraith: Rules for Lobbying the European Parliament

1. Be transparent.
2. Be part of the thinking process.
3. Understand the process.
4. Know the range of people with whom you need to discuss the issue.
5. Think politically.
6. Back up arguments with evidence.
7. Identify the ultimate audience and set clear objectives.
8. Mobilise people.
9. Use all relevant communication channels, including the media.
10. Recognise diversity.
11. Be prepared to compromise.
12. Be creative and memorable.

More than Just Hot Air: Wind Power in Emerging Economies

Green energy and wind power are among the hottest topics in China and the environmental movement today. China has become a world leader in wind power technology, but issues remain regarding market participation and the opportunity for expansion of the industry, both in China and elsewhere. **Steve Sawyer**, Secretary General for the Global Wind Energy Council, examines the issues for wind power in emerging economies, including both the opportunities and barriers for European companies.

In 2010, for the first time ever, more new wind power capacity was installed in developing countries and emerging economies than in the traditional wind markets of the Organisation for Economic Co-operation and Development (OECD). This puts an end to the assertion that wind power is a premium technology only for rich countries that cannot be deployed at scale in other markets.

It is also testament to the inherent attractiveness of wind power for countries striving to diversify their energy mix, improve their security of supply in the face of rapidly growing demand and to relieve their national budgets of the burden of expensive fossil fuel imports at volatile prices. Environmental factors such as improving air and water quality, public health, and carbon reductions to fight against climate change also play an important role in many of these new markets.

There is also a noticeable shift in attitudes towards wind power in many countries. While the technology would have been dismissed as too expensive by most developing country energy planners just a few years ago, the continuing success of the technology in an ever widening group of countries has changed that attitude to one of dramatically increased knowledge about wind generation and the role that it can play in a country's power mix.

Wind Power In China – a Booming Market

The growth of wind power outside of the OECD has been primarily driven by the continuing boom in China. The Chinese government has a clear commitment to developing the country's massive wind resources, partly driven by the need for increasing its power generation capacity to fuel a growing economy and to spur rural economic development. Furthermore, the Chinese government is committed to slowing down the country's increasing greenhouse gas emissions and reducing air pollution. This political commitment is underpinned by favourable policies to boost wind power development, and this has led to exceptional growth in this sector.

After four years of doubling its installed wind capacity each year from 2006-2009, a record capacity of 18.9 gigawatt (GW) were added to the Chinese wind fleet in 2010, taking the total up to 44.7 GW. China is now the country with the largest installed wind power capacity in the world. Wind power now represents nearly a fifth of all yearly net power generation capacity additions in China, nearly on par with hydropower.

Beyond wind power's environmental and energy security benefits, the Chinese government also recognises the economic opportunity of building a strong domestic manufacturing base. In 2009, out of the world's top ten wind turbine manufacturers, four were Chinese, and annual domestic production capacity is now at least 30 GW. Chinese manufacturers are increasingly looking at international markets and it is expected that Chinese wind turbines will soon be fully competitive in the global market place.

The Chinese Wind Power Sector

The commitment by the Chinese government to fulfil the country's wind power potential also provides unprecedented opportunities for the domestic wind energy industry. Although still in its infancy, the Chinese industry has seen dramatic growth over the last five years, and in 2010, four domestic wind turbine manufacturers - Sinovel, Goldwind, Dongfang Electric and United Power - are now in the top ten largest global wind turbine manufacturers and beginning to expand into overseas markets.

China's wind power generation market is mainly shared among the 'Big Five' power producers and several other major state-owned enterprises. These firms account for more than 70% of the total wind power market. There were no significant changes in the status of the ten largest wind power developers during 2010. The largest wind power operators, Guodian (Longyuan Electric Group), Datang and Huaneng expanded their capacity by 2-3 GW each during the year, while Huadian, Guohua and China Guangdong Nuclear Power are following close behind. Most of the local state-owned nonenergy enterprises, as well as foreign-owned and private enterprises have retreated from the market. Access to finance is generally not a problem for wind power projects.

Offshore Wind Power In China

Offshore wind power's attractiveness stems from strong policy support and the desire to access large electricity markets along the eastern coast of China. The first offshore wind power demonstration project, which is also the first offshore wind project outside of Europe, the Shanghai Donghai Bridge Offshore Wind Farm, began generating power in June 2010.

At the same time, the government launched public bidding for the first round of offshore wind concession projects in May 2010, and this was completed in November 2010, adding 1 GW of planned capacity in four projects along the coastline of Jiangsu Province. The winning prices for these projects ranged between 0.62 and 0.74 RMB/kWh (USD 9.4-11.2/EUR 6.9-8.2 cents). These projects must be finished in four years.

In 2010, the National Energy Administration and the State Oceanic Administration jointly published 'Interim Measures for the Administration of Development and Construction of Offshore Wind Power', which should give impetus to China's offshore wind power development. The Interim Measures set out provisions for project approval procedures, as well as criteria for project development and construction. They also stipulate that tender procedures will be the preferred method for selecting project developers for offshore projects and that foreign investors can only hold a minority stake in offshore wind developments.

The Potential For Wind Power in China

Despite the recent boom for wind energy in China, the current developments have barely scratched the surface of the country's wind power potential.

According to the "Detailed Survey of Wind Energy Resources" carried out by China Meteorological Administration, China's total exploitable capacity for both land-based and offshore wind energy is around 2,580 GW. Compared to the other leading global wind power markets, China's wind resources are closest to that of the United States, and greatly exceed resources in India, Germany or Spain.

The Chinese government report "Development Planning of New Energy Industry" optimistically projected that the cumulative installed capacity of China's wind power will reach 200 GW by 2020 and generate 440 TWh of electricity annually, creating more than RMB 250 billion (EUR 28 billion) in revenue.

Due to varied wind resources across China and differing technical and economic conditions, wind power development to date has been focused on a few regions and provinces in China, including: Inner Mongolia, the northwest, the northeast, Hebei province, the southeast coast and offshore islands.

Wind Power In Other Emerging Economies

A similar picture to the Chinese wind power boom is emerging in India, albeit on a smaller scale. A rapidly growing economy has created a growing demand for power and supply struggles to keep up with demand. Electricity shortages are common and a significant part of the population has no access to electricity at all. In order to address this problem, the Indian government created a target of an additional 78.7 GW from 2007-2012, 10.5 GW of which will be new wind generation capacity. The Indian Ministry of New and Renewable Energy (MNRE) estimates that there is a potential of 48.5 GW of wind power, but industry experts estimate that a minimum of 100 GW could be realised in India. At the end of 2010, India had 13.1 GW of installed wind capacity.

Apart from Asia, we are also seeing encouraging signs from Latin America, which has some of the world's best wind resources. Home to many growing economies with increasing electricity demand, this part of the world is considered prime territory for the deployment of wind power.

Wind power is making the most progress in Brazil, the region's largest economy. This country has many areas with tremendous wind resources, combined with a growing electricity demand and solid industrial and grid infrastructure. As a country with a large share of hydropower, this combination forms an ideal basis for large-scale wind power development. More than 1,000 MW are now operating in Brazil, with a further 4,000 MW in the pipeline. Mexico, too, has an outstanding wind resource, especially in the Oaxaca region, but also in Baja California as well as in other regions. Mexico's installed wind capacity has increased more than 6-fold since the end of 2008, and 316 MW of new capacity were added in 2010 to reach a total of 519 MW. Other promising markets in the region include Chile, Argentina and Uruguay.

In Africa, the wind resource is best around the coasts and in the eastern highlands, but it is only in Mediterranean North Africa that wind power has been developed at scale. 97% of the continent's total wind installations are located in Egypt (550 MW), Morocco (286 MW) and Tunisia (114 MW).

While there are strong economic, supply security and environmental drivers for wind power in developing countries and emerging economies, a key determining factor for realising the vast potential will be the political will of governments to make this happen. Favourable support schemes, financial incentives, adequate grid infrastructure and access to financing are some key conditions required for allowing wind power to thrive in these countries.

GWEC is the global wind industry trade association, providing a credible and representative forum for the entire wind energy sector at the international level. Our mission is to ensure that wind power establishes itself as one of the world's leading energy sources, providing substantial environmental and economic benefits. http://www.gwec.net/

How the iPhone Distorts China's Trade Deficit

While not a luxury item per se, the iPhone 4 became the must-have bauble in the early part of 2011. Aside from establishing a new high benchmark for the electronics maker's products, it also sparked a new wave of smugglers and even a new import tax. **Dr. Xing Yuqing** from the National Graduate Institute For Policy Studies, Japan, examines how the smartphone has gone from being a fetish product to a trade war weapon.

What can the iPhone tell us about the trade imbalance between China and the United States (U.S.)? Current trade statistics greatly inflate the value of China's iPhone exports to the U.S., since China's value-add accounts for only a very small portion of the Apple product's price. Given this, the renminbi's appreciation would have little impact on the global demand for products assembled in China.

At the centre of global imbalances is the bilateral trade imbalance between China and the U.S. Most attention to date has been focused on macro factors and China's exchange-rate regime. Little attention, however, has been paid to the structural factors of economies and global production networks that have reversed conventional trade patterns, transformed the implications of trade statistics and weakened the effectiveness of exchange rates on trade balances.

Today's trade is not that experienced by the British economist David Ricardo 200 years ago. It is almost impossible to define clearly where a manufactured product is made in the global market. This is why on the back of an iPhone one can read "Designed by Apple in California, assembled in China". The smartphone in your pocket can help to argue that current trade statistics have distorted the reality of the Sino-U.S. trade imbalance and the appreciation of the Chinese renminbi would have little impact on the imbalance.

How iPhones are Produced

The iPhone is designed and marketed by Apple. Apart from its software and product design, the production of iPhones primarily takes place outside of the U.S.. Manufacturing iPhones involves nine companies, which are located in China, South Korea, Japan, Germany and the U.S. (Table 1). All iPhone components produced by these companies are shipped to Fox-

Table 1

Manufacturer	Component	Cost
Toshiba (Japan)	Flash Memory	$24
	Display Module	$19.25
	Touch Screen	$16.00
Samsung (Korea)	Application Processor	$14.46
	SDRAM-Mobile DDR	$8.50
Infineon (Germany)	Baseband	$13.00
	Camera Module	$9.55
	RF Transceiver	$2.80
	GPS Receiver	$2.25
	Power IC RF Function	$1.25
Broadcom (USA)	Bluetooth/FM/WLAN	$5.95
Numonyx (USA)	Memory MCP	$3.65
Murata (Japan)	FEM	$1.35
Dialog Semiconductor (Germany)	Power IC Application Processor Function	$1.30
Cirrus Logic (USA)	Audio Codec	$1.15
Rest of Bill of Materials		**$48.00**
Total Bill of Materials		**$172.46**
Manufacturing costs		**$6.50**
Grand Total		**$178.96**

conn, headquartered in Taiwan and with factories in Guangdong province, for assembly into final products, and then exported to the U.S. and the rest of the world. By any definition, the iPhone belongs to high-tech products, where the U.S. has an indisputable competitive advantage and China does not domestically produce any products that could compete with it. The manufacturing process of the iPhone illustrates how the global production network functions, why a developing country such as China can export high-tech goods, and why the U.S., the country that invented the iPhone, becomes an importer.

iPhones and the Sino-U.S. Trade Imbalance

The shipment of ready-to-use iPhones from China to the U.S. is recorded as part of China's exports to the U.S.. Using the total manufacturing cost of $178.96 as the price of the iPhone, China's iPhone exports to the U.S. amounted to $2.0 billion in 2009. Assuming that the parts supplied by Broadcom, Numonyx and Cirrus Logic, valued at $121.5 million, were imported from the U.S., the iPhone alone contributed $1.9 billion to the trade deficit with the US, about 0.8% of the U.S. trade deficit with China.

On the other hand, most of the export value and the deficit due to the iPhone are attributed to imported parts and components from the third countries and have nothing to do with China. Chinese workers simply put all these parts and components together, and contribute only $6.50 to each iPhone, about 3.6% of the total manufacturing cost (e.g. the shipping price). The traditional way of measuring trade credits all $178.98 to China when an iPhone is shipped to the U.S., thus exaggerating the export volume as well as the imbalance. Deconstructing the value added along the value chain of iPhone manufacturing suggests that, of the $2.0 billion worth of iPhone exports from China, 96.4% is actually the transfer from Germany ($326 million), Japan ($670 million), Korea ($259 million), the U.S. ($108 million) and others ($542 million). All of these countries are involved in the iPhone production chain.

If China's iPhone exports were calculated based on the value added, e.g. the assembly cost, the export value as well as the trade deficit in the iPhone would be much smaller, at only $73 million, just 3.6% of the $2.0 billion calculated with the prevailing method (Table 2). The sharp contrast of the two different measurements indicates that conventional trade statistics are inconsistent with trade where global production networks and production fragmentation determine cross-country flows of parts, components and final products. The traditional method of recording trade has failed to reflect the actual value chain distribution and painted a distorted picture about the bilateral trade relations. The Sino-U.S. bilateral trade imbalance has been greatly inflated.

iPhone Trade and the Appreciation of the Chinese renminbi

Many believe that appreciation of the Chinese renminbi would be an effective means to solve the Sino-U.S. trade imbalance. Appreciation proponents ignore the fact that the appreciation can only affect a small portion of the cost of made/assembled-in-China products. If the Chinese renminbi appreciated against the U.S. dollar by 20%, the iPhone's assembly cost would rise to $7.80 per unit, from $6.50 and add merely $1.30 to the total manufacturing costs. This would be equivalent to a 0.73% increase in total manufacturing costs. It is doubtful that Apple would pass this $1.30 on to American consumers. Even a 50% appreciation would not bring a significant change in the total manufacturing costs, as the appreciation would only affect the assembling costs. Therefore, the expected pass-through effect of the renminbi's appreciation on the price of the iPhone would be zero and the U.S. consumers' demand on the iPhone would not be affected. The appreciation of the renminbi would have little impact on the Sino-U.S. trade imbalance in this regard.

Could the iPhone be Assembled in the U.S.?

There is no doubt that U.S. workers and firms are capable of assembling

Table 2

Year	2007	2008	2009
iPhone Sales in the US* (million Units)	3	5.3	11.3
Shipping Price/unit** (the US dollar)	229	174	179
China's Export to the US in iPhone (million US dollar)	687	922.2	2,022.70
China's Trade Surplus with the US in iPhones	N/A	N/A	1,901.2[1]
China's iPhone exports to the US based on value added (million US dollar)	19.5	34.35	73.45
Value added / total exports	2.80%	3.70%	3.60%
China's trade surplus with the US in iPhones based on value added	N/A	N/A	73.45[2]

[1] When calculating trade deficits between PRC and the U.S. in iPhones, we assume that all parts supplied by Broadcom and Numunyx were imported from the U.S.

[2] The parts provided by Broadcom and Numunyx are shipped back to the U.S. within the ready-to-use iPhones. They are "round tripping" exports, which should not be considered as actual exports in the value-added approach.

iPhones. If all iPhones were assembled in the U.S., the $1.9 billion trade deficit would not exist. There are two possible reasons for Apple to use China as an exclusive assembly centre for iPhones. One is competition, the other is profit maximisation.

The gross profit margin of the iPhone was 62% when the phone was launched in 2007, then rose to 64% in 2009 due to reductions in manufacturing costs. If the market were perfectly competitive, the expected profit margin would be much lower and close to its marginal cost. The surging sales and high profit margin suggest that the intensity of competition is fairly low and Apple maintains a relative monopoly position. Therefore, it is not the competition but profit maximisation that drives the iPhone's assembly to China.

An interesting hypothetical scenario is one where Apple had all iPhones assembled in the U.S.. Assuming that the wage of U.S. workers is 10 times higher than those of their Chinese counterparts, the total assembly cost would rise to $68 and total manufacturing cost would be pushed to approximately $240. Selling iPhones assembled by American workers at $500 per unit would still leave a 50% profit margin for Apple. In this hypothetical scenario, the iPhone could contribute to U.S. exports and reduce the U.S. trade deficit, not only with China, but also with the rest of world. More importantly, Apple would create jobs for U.S. low-skilled workers.

In a market economy, there is nothing wrong with a firm pursuing profit maximisation. Governments should not restrict such behaviour in any way. However, corporate social responsibility has been adopted as a part of corporate values by many multinational companies, including Apple. Employing U.S. workers to assemble iPhones may be an effective way to practice corporate social responsibility. Eb


European Chamber
中国欧盟商会

OUT, OUT AND AWAY:
TUI China Begins Outbound Travel Services

In late May, the Chinese government announced the launch of a pilot programme that for the first time granted foreign tour operators access to China's outbound travel market. Among the three companies participating in the programme is TUI China, the local operation of the German travel giant. EURObiz's Steven Schwankert spoke with **Marcel Schneider**, Chief Executive Officer of TUI China travel Co. Ltd about the opportunity presented by the new programme and the Chinese travel market.

EURObiz (Eb): Please introduce TUI China for those of our readers who may not be familiar with your operations.

As an affiliate of World of TUI, the global leading tourism group, TUI China was established in late 2003 as the first joint venture with foreign majority share in the Chinese tourism industry. We established our headquarters in Beijing.

With a dedicated and experienced team that combines international expertise and Chinese in-depth destination knowledge, we provide high quality services for inbound, outbound and expat consumers as well as professional M.I.C.E (Meetings, Incentives, Conferences and Exhibitions) solutions for multinational and Chinese companies alike.

Eb: TUI China was recently awarded one of only three outbound travel pilot program licences for China. Why do you think TUI was selected?

On 23rd May 2011, TUI China was granted with the pilot outbound license by the China National Tourism Administration (CNTA). We feel honoured, privileged and also proud and take it as a token of appreciation from CNTA for our contribution towards the Chinese travel industry.

Regarding why we were selected, we do not have the official information from CNTA; however, the three companies, TUI China, JTB from Japan and American Express from the United States have the following points in common: First, the three companies are all joint venture companies; second, we are all global players in the tourism industry; and finally, by spreading the licences over the three continents of Europe, Asia and North America, it is likely that CNTA was motivated by comprehensive global coverage for the Chinese outbound travel market.

Eb: Why is the Chinese outbound market important? Why did TUI

China want this licence?

Given the ever-increasing outbound numbers and the strong economical fundamentals in this country, continuous growth of the China outbound tourism market in the years to come is almost a given. With the World Tourism Organization's forecast that China will source 100 million outbound arrivals by 2020, I believe there is enough space for existing players and newcomers such as TUI China to strive for excellence by offering more quality service and innovative products to the Chinese consumer.

Eb: How are the needs and wants of outbound Chinese travelers different than those of other travelers?

We have been in China since 2003 and ever since as an observer tried to obtain a first-hand impression of the fast development of China's outbound industry. We have found that the market is comparatively immature and at the beginning of a long and hugely interesting journey. Consequently, we can see that many of the products currently available to Chinese customers are relatively shallow in what they offer and the market competition boils down quickly and almost exclusively to price.

However, as the market matures, customers will become more and more discerning, wishing to immerse themselves more in the local culture of the country they are visiting. And that is clearly where we see ourselves to be in a great position to contribute to the Chinese outbound market.

Eb: How can a foreign tour operator hope to compete in China? Is it possible to compete on price? How does TUI China distinguish itself?

To make ourselves truly excellent in the marketplace, we cannot just copy what our competitors are doing and compete directly on price because I believe that traveling has a lot to do with emotions, passion and feelings, hence quality, service delivery and product innovation are equally

important. Price will always be an important factor but instead of being the cheapest we aim at offering the best value for money for all our products.

The company has its own airline, cruise ship fleet as well as hotels and resorts, which ensure our quality of service and make an extensive product range available to our customers.

Our clear aim is wherever possible to make use of our World of TUI global network and all our experience and to feed our Chinese outbound business in this well proven TUI infrastructure around the world. In an ideal scenario the entire holiday experience will come out of one and the same hand, which is TUI. We consider our future products as complimentary to the already existing ones and hence do not feel that we are on a head on collision course with the current Chinese outbound travel agencies. Last but not least we consider competition as necessary and beneficiary. Healthy competition keeps our organization sharp and on the edge and the biggest beneficiary will be the Chinese traveler that can choose in the future whether he or she wants to travel with a domestic or an international brand.

Eb: TUI China also offers packages within China. What advantages does TUI offer domestic travelers, both Chinese and foreign?

Prior to the outbound license, our business segments included inbound travel (providing services for foreign travelers to China), expat travel (providing tour products within China and Southeast Asia to the expat community in China) and solutions for M.I.C.E events in China and abroad. So, we did not engage in Chinese domestic travel market in the leisure segment.

As for our advantages, I would like to summarise here as follows:

- Decades in the travel industry means that our reputation precedes us as a key account holder with airlines and top hotels worldwide.

- Our long and deep European heritage guarantees a high quality approach in all activities and business fields in which we operate.

- Our unique combination of Chinese in-depth destination knowledge and Western expertise stands for innovation, creativity and reliability.

- Our multilingual staff and competent tour guides are trained according to European standards and they are true ambassadors of the hospitality industry.

It will not be the foreign-invested companies that will be a threat to the Chinese outbound market. I truly believe the market with its incredible growth potential is big enough for all competitors, whether Chinese or foreign invested. The biggest issue in the Chinese tourism industry in general is that existing rules and regulations are not always properly implemented and executed. What will happen once there is more emphasis from the official side on complying with them is that the companies following them will not only continue to flourish and grow, but could do so in an even faster and more sustainable manner. The ultimate consequence will be that there will remain only travel companies that sincerely want to contribute to the Chinese travel industry in the long term. It would become a self-regulating process. Eb

NANJING

In the first of our series on cities and regions where the European Chamber serves its members, we look at business opportunities in Nanjing. **Tony Brooks** reports on a city with lots of land and a high rate of growth.

According to a recent report by the McKinsey Global Institute, Nanjing ranks eighth globally for the predicted fastest GDP growth between now and 2025, ahead of cities such as Delhi, Moscow and Chengdu. Nanjing's municipal government is certainly preparing for rapid growth, and Director General Kong Qiuyun from the city's investment promotion commission, brims with enthusiasm over 12th Five-Year Plan blueprints for turning the municipality into a critical driver of regional growth. While Nanjing is often overlooked by investors, especially in comparison to Shanghai, during the next 10 years it will become an economic engine that is too important to ignore.

Potential

One of Nanjing's biggest assets is space, lots of it. The municipality has a total land area of 6,600 square kilometres, however, Nanjing city proper accounts for less than 15% of this area, which means there is ample room to locate and expand. Nanjing also has strong tax revenues with which to develop the land around the city. In 2010, GDP and tax revenue rose 18% year-on-year, to RMB 500 billion (EUR 54.6 billion) and RMB 107 billion, respectively. According to Patricia Enzmann, General Manager of the European Union Chamber of Commerce in Nanjing, there are currently about 80 Fortune 500 enterprises in Nanjing, and as such the city government is able to offer more attention to companies wanting to invest here long-term.

Human Resources

Some of the nation's top universities and research centres are located in Nanjing. According to Professor Liu Cheng from Nanjing University, which itself ranks between third and fifth in various domestic university league tables, the city now has a critical mass of leading scholars in many fields, which has already proved highly beneficial for the business community in terms of cooperation on research. Almost 10% of the population of Nanjing (around 760,000) is either studying towards a degree or possess one, which bodes well for industrial research and companies that thrive on a highly-qualified workforce. Nanjing is geographically close to the less prosperous provinces of Anhui and Jiangxi which rank 14th and 22nd, respectively, in provincial GDP tables, compared to Jiangsu's third position). This relative wealth disparity means that there is a stable and steady supply of migrant workers from Anhui and Jiangxi, many of whom find they like Nanjing and stay long-term.

Clusters and Logistics

As a provincial political capital and a major Yangzi River commercial centre, Nanjing serves a regional cluster of cities in southern Jiangsu and eastern Anhui. Officials in the Nanjing municipal government estimate that this "city cluster" serves a population of almost 200 million people, which is why it makes sense for them to invest in Nanjing as a logistics center. Money has been spent dredging Nanjing harbour (China's largest inland port) to a minimum depth of 12.5 meters, and the city is soon to be home to Asia's largest passenger railway station. Put differently, Nanjing is a large, rapidly expanding, entrepreneurial city that can reach other urban centers in the "Nanjing cluster," such as Zhanjiang (Jiangsu) and Chuzhou (Anhui), at minimal extra cost.

Emerging Industries

The main pillar industries in Nanjing are information technology, steel, automotive manufacturers, who currently produce around 1.5 million units per year, and petrochemicals - the city is home to the second-largest petrochemicals complex in the country. With respect to IT, the city has recently cooperated with the electronics giant Sharp, in order to design and produce state-of-the-art liquid crystal displays (LCDs), just the sort of investment which is needed to turn the city and its environs into a "second Silicon Valley". Nanjing has also been very successful at attracting clusters of companies in emerging

Skyline of Nanjing, picture taken at the Mochou Lake by Bjoern Walter

"Nanjing is an excellent location for our company. The city combines a well-developed infrastructure and accessibility, one of the leading education systems in China and offers an attractive living environment. At all times our investment has been fully supported by the local Government and we are looking forward to expanding our activities in Nanjing."

Dr. Bernd Blumenberg,
President BASF-YPC Company Ltd., Nanjing

industries, involved in the design and production of "smart" electric grids, power automation equipment, communications technology and environmental protection.

The service sector, which includes banking, insurance, logistics, retail, tourism and e-commerce, is expected to grow from 51% of the local economy in 2009 to 56% by 2016, further emphasising a long-term shift towards a knowledge dominated economy. A 2010 report by PricewaterhouseCoopers on the investment environment in Nanjing gives more detail on specific industries.

Comparison with Shanghai

Nanjing's biggest disadvantage is that it is only 270km from Shanghai. One manifestation of this problem is that whereas Nanjing has only one medium-sized air terminal, served by a small number of international carriers such as Lufthansa and Dragonair, Shanghai is served by two large international airports. Another manifestation of this problem is that the volume of Foreign Direct Investment (FDI) into Shanghai is much greater than that for Nanjing. For example, in 2009 Shanghai signed new contracts with foreign investors worth EUR 9.4 billion, compared to only EUR 3.24 billion in Nanjing. However, many people in Nanjing feel that despite Shanghai's economic importance it is too much of a showcase city, and they think that their home is more representative of "real" China away from the east coast.

Nanjing is not Shanghai, however, many Nanjing residents think that it is right for the city to focus on its strengths (e.g. available land, a highly educated workforce) rather than trying to imitate its larger neighbour. The municipal government's Director Kong offers four tips to any potential investor, "firstly, think about the opportunities Nanjing has to offer; secondly, don't think about problems; thirdly, come in person; and fourthly, be nimbler and more flexible than your competitors."

Living Environment

Nanjing is a city that is proud of its history as one of the six ancient capitals of China, and because of this rich cultural heritage, there is much to do and see. For example, Nanjing has one of the longest and best preserved city walls in the world (of which just over 21km still stand today), and millions of visitors flock every year to see the imposing mausoleum of Sun Yat-sen, the founder of Republican China. Besides these "must see" sites, Nanjing is full of ancient temples, 1920s villas, lakes and leafy small lanes where you can get away from the crowds. It is also an attractive place to live because its housing is relatively affordable. According to a survey by ECA International, in 2009 the cost of living in Nanjing was cheaper than in Xiamen, Qingdao, Chongqing, Xian and many other major Chinese cities. Eb

Tony Brooks is currently a PhD candidate at the University of Cambridge. For more information on Chinese politics, business and government relations please contact Tony at adb57@cam.ac.uk.

Managing IP as a Business Asset

For new knowledge-driven businesses, it's not hardware or products that create value for the company, it is intellectual property and rights to the creativity and ideas produced. IPR Helpdesk's Phillip Healey discusses protecting that output in the same way a company would register and handle physical products.

For most businesses, intangible assets represent more than 50% of the value of the enterprise. The most significant group of intangible assets are those protected by intellectual property (IP) such as inventions, designs and brands. Since they form such a large part of the overall value, their management as financial assets is important to the success of the business. Businesses that actively manage their IP as a financial asset outperform their peers by up to 30%. They do so by maximising the effectiveness of investment in the business, driving performance in areas that produce the best return and managing operational risk. They may also use their IP assets as security to obtain various forms of funding. Moreover, there are opportunities to gain strategic advantage in relation to the sale or purchase of a business.

A good IP management strategy enhances the ability of the business to raise funds by managing the issues that affect valuations of IP assets.

Understanding the financial value to the business of specific IP assets is of particular importance when moving into a new market – product or geographic – because there will be new risks as well as opportunities.

China presents some special challenges and practical steps to protect the value of IP assets are often as important as legal ones. There are several explanations as to how IP assets matter from a financial perspective and allow a business to manage them to their greatest business advantage.

Managing Return on Investment and Improving Performance

Where there are several IP assets, knowing the comparative return on investment of each one allows the overall business strategy to focus on those that will give the best return. It also means that the risk to the viability of the business if certain IP rights are lost can be assessed. This is important in deciding how to structure commercial relationships and operations in China.

As with tangible assets, measuring the return on investment requires knowledge of their monetary value and of the amount of investment made in them over a given time period. Ascertaining individual IP assets consists of identifying the technology and brand in each separate product and any brand that is used for more than one product.

Provide Security for Financing

IP assets can be used to provide security for a wide range of methods of raising funds. China has been at the forefront of the use of patent mortgages and a variety of fundraising structures are readily available from Chinese financial institutions as well as European ones.

The range of fund-raising options includes:

1.Providing security for existing bank borrowing. It is not unusual for a company's IP to be covered by the general charge taken by its bank but at a nominal or nil value. Valuing it separately often increases the value of the security covered by the charge. This can be used either to increase the borrowing or to reduce the interest charged on it. If the IP assets are to be used for another form of security it will be necessary to get them released from any bank charge. This will be easier if they are included at only a nominal value.

2.Providing security for new debt. This can be to support new bank borrowing for cashflow or for longer-term debt to fund investment in new products or markets. Lending against IP assets is a specialised form of lending usually carried out by dedicated teams within larger lending organisations or by smaller specialist lending houses.

3.Patent (and other IP) mortgage. A patent mortgage is one form of lending against patents or other IP assets. The significant difference between this and security under a charge is that a mortgage will usually transfer title to the lender immediately on default. It is a well-established form of lending by some Chinese banks who may have more familiarity with it than their international counterparts.

4.Creating a vehicle for raising equity. If IP assets are owned by a company created for that purpose and generate a royalty income then shares can be issued in that company to raise new equity finance.

5.Securitisation (bond issue). An alternative to issuing shares in an IP holding company is to use the company's assets as security for a bond issue in the market. This is more likely to be an attractive option for medium-sized businesses with brands or technology that is reasonably well-known in its own market-place.

6.Secure assets to benefit a third party. A further use of an IP holding company is to provide security to benefit a third party such as the company's pension fund or a new venture on the same group of companies.

IP assets are often undervalued in company accounts. However, identifying and valuing them can result in a worthwhile increase in the value that existing lenders will put on them as security for current lending. This can be very useful in a credit crunch.

The acceptability of IP assets for fund-raising will depend to a considerable extent on what valuation is put on them and whether they are owned by an appropriate entity.

There are several considerations that impact valuation, including whether the IP assets are clearly identified, consolidated in one ownership rather than dispersed, protected from insolvency risks associated with operational activities, protected by appropriate registrations, subject to a structured enforcement programme, licensed to group businesses and/or third parties to generate income and being used to increase the profitability of the business.

Devising an IP Strategy

A well-managed IP strategy makes a significant difference to the valuation of a company's IP assets. A valuer will assess the economic impact of the IP on the company's business. Although there are several different valuation methodologies, all take account of the risk to the IP. A realistic IP strategy that is documented and demonstrates effective support for the overall business strategy will always enhance the ultimate valuation figure for the IP.

The IP strategy reinforces the overall business strategy and will change as the business moves through different stages of its development. It will often also differ from one market to another as the business will be at different stages of its life-cycle in each. The balance of which IP rights are most useful and so should get priority in investment and management time will vary accordingly.

For example, in establishing a new market, registration of trademarks and patents, designs or copyright to protect the product is likely to be more significant than enforcement against infringers. Once a business is established, enforcement is likely to take a higher priority. Where it seeks to increase market share compared with its competitors, then the focus may well be on defending litigation.

It is essential that the management of the company is involved in drawing up the IP strategy and understands how it will support the business objectives. The key people to be engaged are the chief executive, finance director, tax advisor, general counsel, chief technology officer and chief operating officer.

The IP strategy should be reviewed whenever the business strategy changes and at least once a year.

With a strategic IP management approach and the appropriate identification, valuation and protection of IP assets, intangible assets can be used to a company's advantage to provide security for financing and improve your company's overall performance. However, to best use IP assets as business tools, IPR Helpdesk experts strongly recommend that SMEs ensure that their key IP asset are protected by registration, adequately prevent IP from being exposed by current and former employees and business partners, and structure IP ownership so that it is most appropriate for any planned use as security for raising finance.

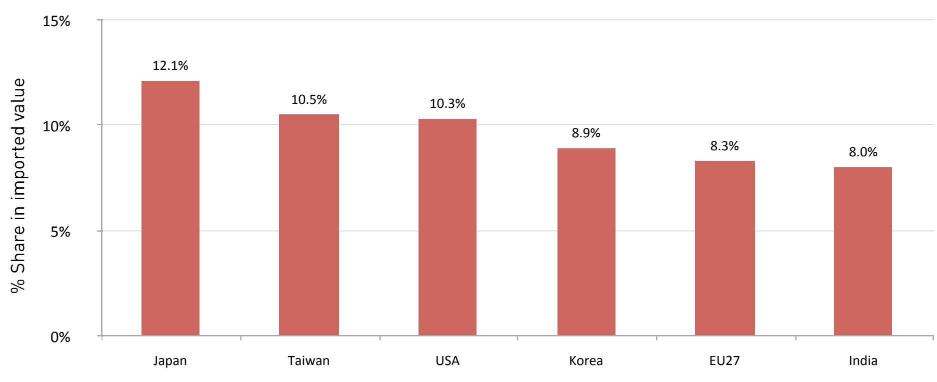
The China IPR SME Helpdesk is a European Commission funded project that provides free, practical, business advice relating to China IPR to European SMEs. To learn about any aspect of intellectual property rights in China, visit our online portal at www.china-iprhelpdesk.eu

Quality, Innovation and Technology:

Opportunities for European SMEs in China's Textiles and Apparel Market

While European consumers would quickly and correctly think of China as the world's leading textile and apparel exporter, the development of that industry has created unique opportunities for European Small and Medium-sized Enterprises (SMEs). **Chris Cheung** and **Lisa Kim** of the EU SME Centre show how Europeans can break into a market segment believed to be dominated by China.

When it comes to the textiles and apparel industry, people inevitably think of China's large volume of world exports. China has been the biggest textile and apparel exporter in the world since 1994, with 2010 statistics showing the country occupying 40% of global exports. However, while China dominates the global low to medium end market, European Union (EU) member states have the upper hand when it comes to the global market for high-end and high-quality textiles and clothing. It is innovative design, quality and application of the latest technologies that give European SMEs the advantage when entering the Chinese market.



Source: International Trade Centre & EU SME Centre

The EU member states were the fifth largest source of Chinese T&A imports, making up 8.3% of China's T&A imports by value in 2010.

Among these member states the following were the largest contributors to the 8.3% of imports by value:

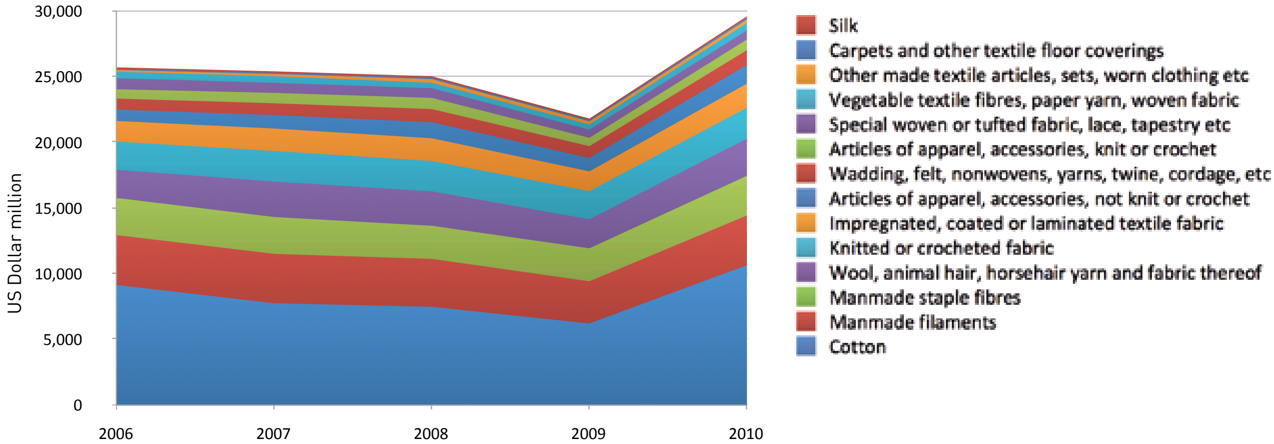
- Italy (3%), Germany (1.6%) and France (1%)
- The UK (0.7%), Austria and Belgium (0.4% each)
- Spain and Netherland (0.3% each)
- Portugal, Romania and Luxembourg (0.2% each)

Growth Drivers

Despite its strength in manufacturing, China imported EUR 20.7 billion of textile and apparel products in 2010, making up just over 2% of its total imports. This 2% presents a multitude of opportunities for European SMEs in the industry.

Disposable income, particularly in China's first and second-tier cities, is increasing at a fast clip and Chinese consumers are spending more on clothing in order to keep up with fashion. Chinese urban young adults (aged 18-30) are particularly fashion-conscious and are willing to spend more on foreign brands that promise style and chic. Women, in particular, should be considered a target market not only because of their penchant for the latest styles, but also because they are the key decision makers when it comes to clothing purchase decisions for the whole family.

Another strong driver of growth in the apparel market is the explosive popularity of Chinese e-commerce. Online purchases have grown by an average of over 100% each year between 2005 and 2010. According to iResearch, a Chinese Internet research and consulting company, in the fashion sector the growth of online B2C retail was over 130% between 2005 and 2010. While many powerful new uses and applications for textile fibres and products in industries such as aerospace, automobile, healthcare, construction and architecture, transportation and personal protection are huge potential growth areas.



Source: International Trade Centre

China's main imports include cotton (36%), manmade filaments (13%), manmade staple (short) fibres (10.2%) and wool, animal hair, horsehair yarn and fabric (9.8%).

Impacted by the financial crisis, textile and apparel imports in China declined from EUR 17.9 billion in 2006 to EUR 15.2 billion in 2009, hitting the bottom at a negative growth rate of 12.9%, but bounced back to a positive 36% in 2010 to EUR 20.7 billion because of a mild recovery in the developed economies and an expanding domestic market.

Online clothing purchases

	2007	2008	2009 1H	2010	2012e
Total value of online clothing purchases in CNY billion	22.3	36.6	30.87	n/a	80
% of total clothing retail	3.23%	4.68%	9.70%	12.8%	17%

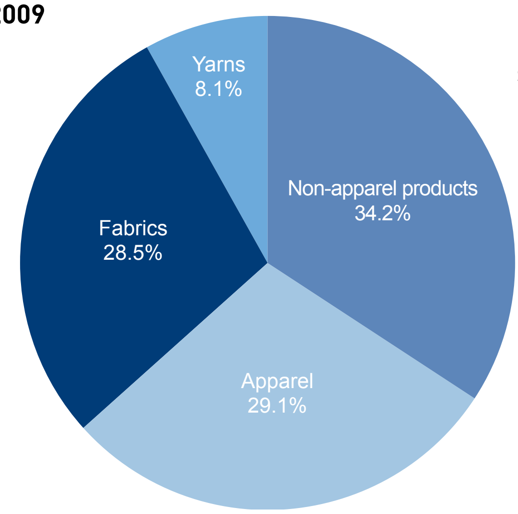
Note: 2007-2008 data from China intelliConsulting Corp.; 2009-2012e from iResearch
In the table, 20091H means the first half of 2009, while 2012e means 2012 estimated.

brick-and-mortar retailers have been laggards in their online efforts, more independent online branded fashion retail companies are quickly gaining new market share.
The trend for online clothing purchases shows a steep climb, occupying 3.23% of all clothing purchases in 2007 and this looks set to rise to 17% (CNY 80 billion) by 2012.

'Sexy' Textiles

However, despite the growth in the fashionable apparel market, it is really the less sexy or glamorous textiles market that presents the most profitable opportunities for European SMEs. In this regard, development of

China textiles market segmentation: percentage of share by value, 2009



Source: Datamonitor

Increased use of technical textiles is driving the demand for high-tech content fibres and yarns with special performance characteristics such as high tenacity, extreme strength, special elasticity, UV resistance, high filtration rate, high durability against erosion, moisture resistance and flame retardant ability. European companies are in a prime position to exploit these opportunities: among the world's top 20 exporting countries of functional and industrial use fabrics, 10 are EU member states.

European High Quality and Innovative Design

For both textiles and apparel it is the high quality standards and innovative design of products that will allow European SMEs to access opportunities in the fast-developing Chinese market and provide them with a defendable competitive advantage.

Among the opportunities emerging in the Chinese textiles and apparel market, the following are worth highlighting:

- Special Fibres and Yarns for Functional Textiles

China's high growth in car ownership, transportation, healthcare and clean energy sectors, and its focus on energy saving and pollution reduction in the manufacturing sector will generate opportunities for increased use of technical textiles.

- Eco-Dye for Eco-Friendly Textiles

Stricter environmental requirements posed by both government and clients are encouraging manufacturers to look for greener raw materials to improve products' environmental performance.

- High-End Fabrics

As income levels rise in China, more people are seeking higher quality garments to demonstrate their good taste and status. Fabrics from Europe are viewed as high quality and more stylish.

- Textile Machinery/Equipment

Industry upgrade in the traditional textile clusters and new clusters forming in the middle and western parts of China are driving demand for more advanced textile machinery.

- Design and Development

Both Chinese companies and foreign companies in China need to invest more in the development of new fibre, fabric and garment innovations to move up the value chain and be better positioned for a world market.

- Specialty Apparel Boutiques

Small, quality manufacturers who specialise in particular product lines have the opportunity to occupy a niche market. For example, in the kids wear segment that is benefiting from a recent uptick in the birth rate.

- Online Apparel Boutiques

The success of many independent online brands indicates that the high growth of online apparel purchases looks set to be an ongoing trend.

The EU SME Centre and the Textile and Apparel Sector Report

The newly established EU SME Centre in Beijing provides a comprehensive range of hands-on support services to European Small and Medium-sized Enterprises (SMEs), assisting them to establish, develop and maintain commercial activities in the Chinese market.

The textiles and apparel sector report, due to be published on the centre's website this month, includes information on market size, key growth drivers, market structure, distribution channels, opportunities and challenges. The report will be freely downloadable from the centre's website following registration: www.eusmecentre.org.cn. Eb

EURObiz Events

Event information is subject to change. For full details, please visit our website: www.europeanchamber.com.cn/view/events

July

Sat 2ND Site Vist to Sheme Factory, Chengdu

Tue 5TH Discussion & Debate on Key HR issues in the R&D sector, Shanghai,
11:40-14:00, Sofitel Hyland Hotel, 505 Nanjing East Road

This event will address issues that aim to enlighten Human Resources in R&D area:

Talent Definition: What sort of capability & quality we source from the Chinese market?

Sourcing: Channel management & internal alignment

Evaluation: How to identify & validate candidate's capabilities. Who is taking the leading role in talent acquisition, HR Directors or Hiring Managers?

Wed 6TH Company Turnaround and Interim Management in China, Beijing,
16:00-19:00 Hilton Beijing Hotel, 1 Dongfang Road, East Third Ring North Road, Chaoyang District

Professional interim managers Viktor Arak and Max Braendli speak on the subject of "Company Turnaround and Interim Management in China" on

- Why and when do companies deploy an interim manager?
- What roles do interim managers play in reversing major corporate setbacks?
- How can troubleshooters turn around a company's fortunes?

Thu 7TH Outbound Conference, Shanghai,
8:00-12:30, The Longmont Hotel

Wed 13TH GM Briefing: latest trends in labour market, Tianjin

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Wed 13TH Successful European SME entrepreneurship in Foshan-ASYTEC FACTORY TOUR, Foshan,
11:15-14:00, Foshan Asytec Metal and Plastic Products Limited

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Fri 29TH Effective Customs Compliance Management, Tianjin

August

Thu 18TH VIP-Dinner, Chengdu

Sat 27TH 4th European Chamber Human Resource Mixer - Wine & Snacks, Calming Atmosphere & Networking, Nanjing

This year's HR mixer will again provide an opportunity to make friends, to network, and to share experiences with each other. The participants come from different backgrounds, cultures, and companies. And what better common ground to we have than our lovely city, Nanjing. The event will include a unique photo exhibition from a Nanjing based artist as well as delicious wine and snacks.

Sat 27TH European Chamber Summer Party, Beijing

Tue 30TH Member Speed Meeting, Guangzhou,
18:30-21:00

Wed 31ST International Mixer, Chongqing

European Chamber
中国欧盟商会

EUROPEAN CHAMBER EVENTS GALLERY

BEIJING


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4

1.SME Conference on 12th May - the first large-scale Chamber conference in Beijing to provide a platform for European SMEs to receive expert advice and insight on the key issues that SMEs have to face in China.

2."The Future of the World Monetary System: Three Currencies in Search of a Future – Perspectives for Euro, Renminbi and Dollar Co-existence" on 20th May with David Marsh, co-chairman of monetary think-tank Official Monetary and Financial Institutions Forum (OMFIF) and Steven Schwankert, Chief Editor of EURObiz.

3."The impact of China's New Social Insurance Law" on 14th June - questions including the impact on overall staffing costs and the treatment of expatriates in the scheme were discussed.

4.European Chamber's Business Confidence Survey 2011 on 25th May in partnership with Roland Berger Strategy Consultants. This year's survey draws on feedback from nearly 600 European companies and offers insight on European business confidence in the Chinese market at a time of impressive growth, rising competition, and the release of China's 12th Five-Year Plan.

CHENGDU


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2

1.Seminar on Advertising in the 21st Century: Why everyone needs to think differently on 19th May - top executives, marketers, agencies and media people attended; more than 300 member and non-member companies participated in the event.

2.European Day Party on 20th May - more than 300 participants attended.

NANJING


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3

1.Europe Day Photo Exhibition was hold on 11th May - more than 120 member and non-member companies participated in the event.

2.Spring Garden Party on 28th May - participants enjoyed the Jinling Dragon World Music Band to celebrate the arrival of spring in Nanjing.

3.Second Badminton Tournament on 18th & 19th June - 12 companies' teams had strong competitions in these two days. BASF-YPC won the 1st place of the tournament, DT Travel won the 2nd place and Nanjing International School won the 3rd place.

PEARL RIVER DELTA



1.Member Speed Meeting on 19th May in Grand Mercure Shenzhen. This business networking event provides a good opportunity for members to get to know each other better.

2.Europe Day on 28th May - a family celebration, that was organized at the Sheraton Shenzhen Hotel.

3.Business Confidence Survey 2011 and Business Cocktail on 14th & 15th June in Guangzhou and Shenzhen.

SHANGHAI



1.Breakfast event with the President of the European Council, H.E. Mr. Herman Van Rompuy on 18th May at the Hyatt on the Bund in Shanghai.

2."Shanghai International Financial Forum – Internationalization of the RMB" on April 12th with the Shanghai Municipal Government Financial Services Office - a half-day conference focusing on recent trends towards the greater internationalization of the RMB.

3.European Business Confidence Survey 2011 Shanghai on 27th May in partnership with Roland Berger Strategy Consultants.

4.R&D Conference on 26th April - bringing together a range of experts to cover topics including tax, indigenous innovation and IPR.

5."Where Experts Advise and Develop Business" on 13th May - for the 3rd time the Business Solutions Clinic, together with the Italian and Spanish Chamber, brought together expert service providers and companies looking for free business advice.

TIANJIN




1.EU Commission visit in TianjinSite visit in Airbus & Vestas on 9th & 10th June.

2.GM Briefing: Insight into European business confidence in the Chinese market on 2nd June.

3.Exhibition: ICE, Journey to the land of Icebergs on 28th May - 30th June.

4.Europe Day Celebration on 28th May - a sunny afternoon in the Victorian Lounge, Astor Tianjin.

5.Investment Tour Series: WuQing visit on 22nd April - a state-level development area and hi-tech area between Beijing and Tianjin.

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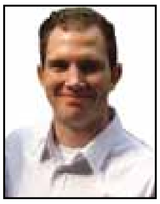
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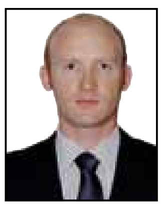
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THE EXECUTIVE INTERVIEW: MIROSLAV KOLESAR

Miroslav Kolesar, Chief Representative of PPF Group China and Vice President of the European Chamber of Commerce in China.

One of the founding members of PPF Group's presence in China in 2004, he was elected as Vice President of the European Chamber in April.

EURObiz (Eb): Do you think Eastern European companies are viewed differently than other foreign companies in China? If so, how?

Miroslav Kolesar (MK): Eastern European companies coming to China may still enjoy some benefits arising from the fact that there have been close traditional ties between their countries and China in the past. By that time, Eastern Europe in many cases represented the only foreign business presence in China. This translates not only into natural knowledge of some Eastern European brands among local people, but also into personal relations that are always important for business efforts. Sharing common positive history always helps to build the future. Meanwhile, it is fair to say that it is equally important for Eastern European companies to adjust their approaches to local market according to the changing competitive landscape in China.

Eb: Since April you are a Vice-President of the European Chamber. What goals have you set for yourself to reach with this opportunity?

MK: I strongly believe in the importance of EU-China relations and ongoing engagement between both sides. It is truly a personal honor and professional privilege for me to have the opportunity to utilise my Chinese language skills together with more than a decade of experience in communication with Chinese government officials and partners. I am pleased to work for the benefit of the wider European business community in China, building on the solid ground established by the previous leadership of the European Chamber.

Primarily, I would like to support the European Chamber to further consolidate its position to be the first choice for every European business entering China and to become the leading Chamber of Commerce in China vis-à-vis the Chinese government and officials, with respected and well-perceived "European Voice" that it represents.

Furthermore, I would like to assist Working Groups in obtaining even better access to their Chinese counterparts, including government agencies, regulators and other officials, so that their voice can be better heard and their needs can be better reflected.

Eb: What suggestions would you give to European companies on their lobbying strategy?

MK: Lobbying should be an integral part of the company's overall development strategy in China, especially in the situation when the company is engaged in a strategic industry or an industry with a higher level of supervision. In terms of practical suggestions, it is important to understand existing regulations and what impact they have on business development, and which regulators and departments are directly and indirectly overseeing the industry. Then comes the crucial step that is to engage in systematic institutional and interpersonal interactions with them on an on-going basis and see for win-win solutions.

Eb: How do you view the consumer finance market in China? What changes do you see coming up this year?

MK: Consumer finance market in China has seen noteworthy development in the past few years. Not only traditional products such as credit cards and mortgages, but also new credit products offering unsecured small loans for daily consumption purposes for mass consumers have been on the rise recently. That trend also shows that growth momentum of Chinese economy is shifting from primarily export and investment oriented position into more consumption driven model which is in line with new 12th Five-Year Plan's objectives to restructure national economy.

Nowadays it is not only the traditional commercial banks, but rather increasing number of non-banking based consumer finance specialists that are building business presence in emerging consumer finance market across China. This is also expressed in that a specialised non-banking financial entity – the consumer finance company -- has been operated in China since 2010 on a pilot basis under the supervision of the China Banking Regulatory Commission. PPF is proud to be the only foreign and European player selected for the pilot through our consumer finance subsidiary Home Credit. Eb

THE ADVISORY COUNCIL OF THE EUROPEAN CHAMBER

The European Union Chamber of Commerce in China is driven and funded by its members. The 26 members of the Advisory Council are particularly active in representing and advising the Chamber, and make an enhanced contribution to the Chamber's funding.

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