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CEO Briefing 2014 | The Business Agenda for China:

Competing in a Digital World

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According to recent Accenture research, business executives around the world are brimming with confidence, none more so than individuals leading China-based enterprises. Not only do Chinese executives see the global economy in a positive light, they are far more optimistic than their global counterparts about their own industry and organization, as well as their home market. However, this optimism stands in contrast to slowing growth in China—the primary market for Chinese companies in our survey—as well as a growing need to control costs, improve operating efficiencies, and boost overall productivity. Chinese executives overwhelmingly view digital technologies as a powerful tool to address those challenges, as well as to help them more effectively serve customers, especially those at home and in other emerging markets.

Chinese Business Executives Are Highly Optimistic

We examined the China data from the new Accenture research study, "CEO Briefing 2014—The Global Agenda: Competing in a Digital World,"[1] and found a majority of Chinese respondents are somewhat or strongly optimistic about the economic prospects for the economy of the country in which they are based (77 percent), their own organization (89 percent), their industry (91 percent) and the global economy as a whole (59 percent) (Figure 1). In all cases, these figures exceed by a considerable margin those of the global survey sample, suggesting Chinese executives are far more confident than their global counterparts.

Consistent with this broad optimism, nine in 10 Chinese respondents also expect increases in profit (93 percent) and revenues (91 percent) in the next 12 months.

Yet despite this optimism, there are concerns about the slowing of China's economy overall. Although the country expects to grow by 7.6 percent in 2013—the strongest of any major country—that rate is slightly less than the previous year's and half of what it was in 2009.[2] Slowing growth is expected to continue through the rest of the decade, with some analysts predicting annual growth rates to slip to 6.5 percent to 7 percent due to a decline in fixed asset investment, a move to service-sector jobs from more productive sectors of the economy, and an aging population.[3]

Respondents' profitability expectations also may be at odds with emerging trends. For instance, a large proportion of output in China is driven largely by state-owned enterprises (SOEs), which far outpaced private firms and are building on that lead every year.[4] However, that production has come at a price, as China now is looking to cut excess production capacity in certain industries (especially steel, aluminum, glass and cement). Furthermore, SOEs' return on capital and profitability has been decreasing since 2008, interrupted only by a temporary increase in 2009 due to the government's stimulus package, according to data from China's Finance Ministry.

Indeed, while most Chinese executives in our survey expect to increase profitability in the next year, a number of manufacturing sectors in China—including transport equipment, electronics, light industrials, and machinery and equipment—are seeing declining margins year over year. [5] In fact, according to other Accenture research, [6] 15 out of 19 sectors have seen compressed margins in a five-year time frame and 11 out of 19 sectors have experienced the same in a 10-year period.

Another concern is productivity. China's overall labor productivity is increasing steadily: It is forecast to grow 6.8 percent in 2014—far more than the US (1.4 percent), Germany (0.8 percent), Brazil (1.2 percent), India (-0.4 percent) and Japan (1.1 percent). [7] Furthermore, total factor productivity in China is projected to rise 4 percent in 2014, compared with 1.2 percent in the US, -0.3 percent in Brazil, 0.8 percent in Germany, 2.3 percent in India, and 3.6 percent in Japan. [8] However, despite this increase, China's labor productivity still lags many other industrialized countries—especially the US, where workers on average remain three times more productive than those in China. [9]

The preceding concerns, however, do not mute Chinese companies' enthusiasm for expansion. For instance, 84 percent of Chinese executives (compared with 65 percent of their global counterparts) expect to increase their company's workforce in the next 12 months. As they do so, they will have plenty of talent to choose from: According to data from the Economist Intelligence Unit, China scores a 5, or "very good," on its availability of skilled labor. [10] Furthermore, 78 percent anticipate an increase in total capital investment in the same timeframe—including increases in investment in human capital assets, physical assets (such as real estate, facilities, machinery and equipment) and intangible assets (including patents, copyrights, and trademarks) (Figure 2).

Figure 1: Percentage of executives optimistic about

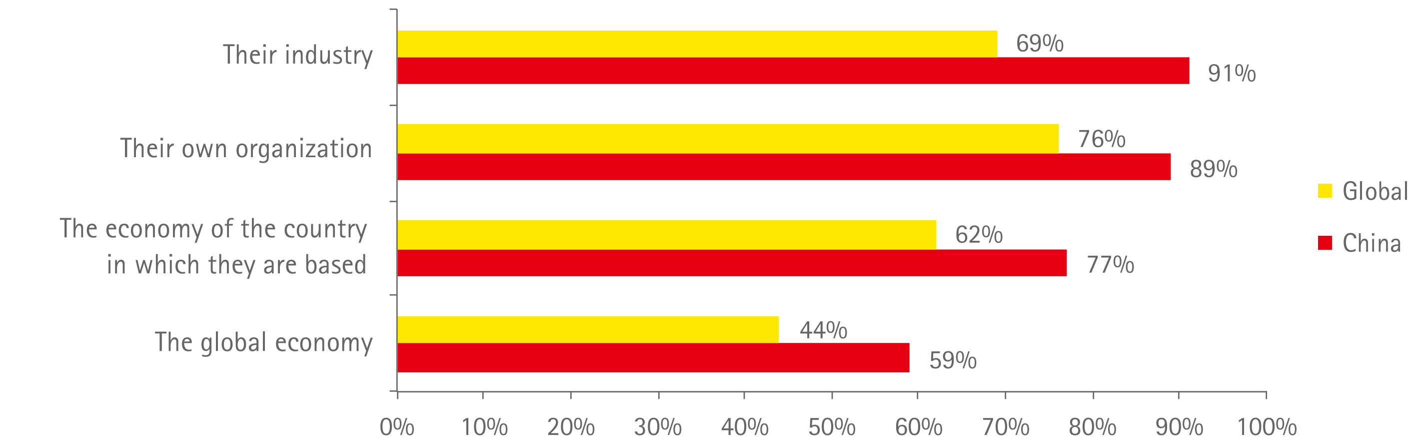
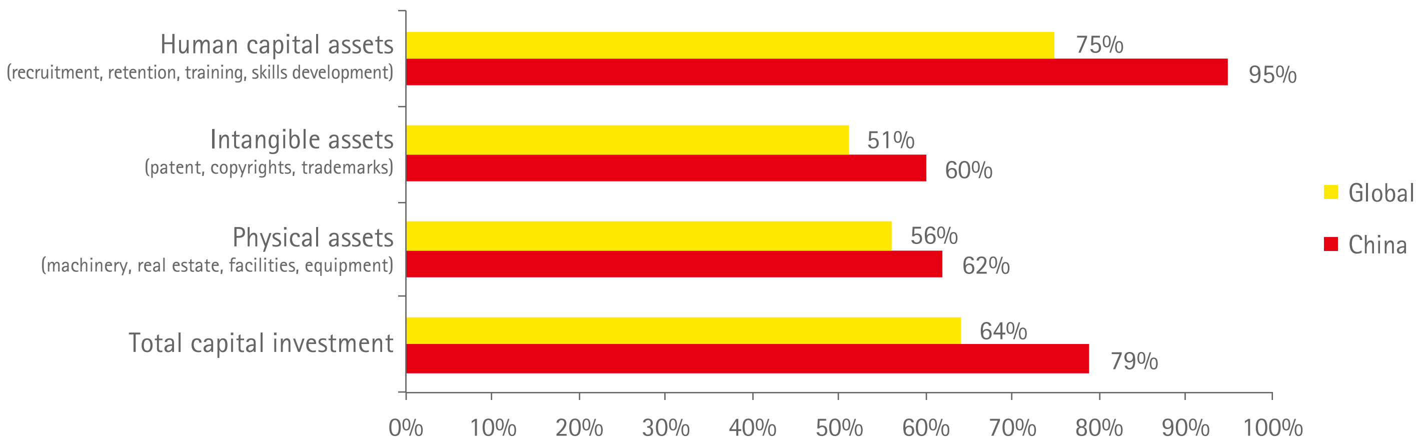


Figure 2: Percentage of executives planning to increase investment in



China's Businesses Are Focusing Their Growth Agenda on China and Emerging Markets

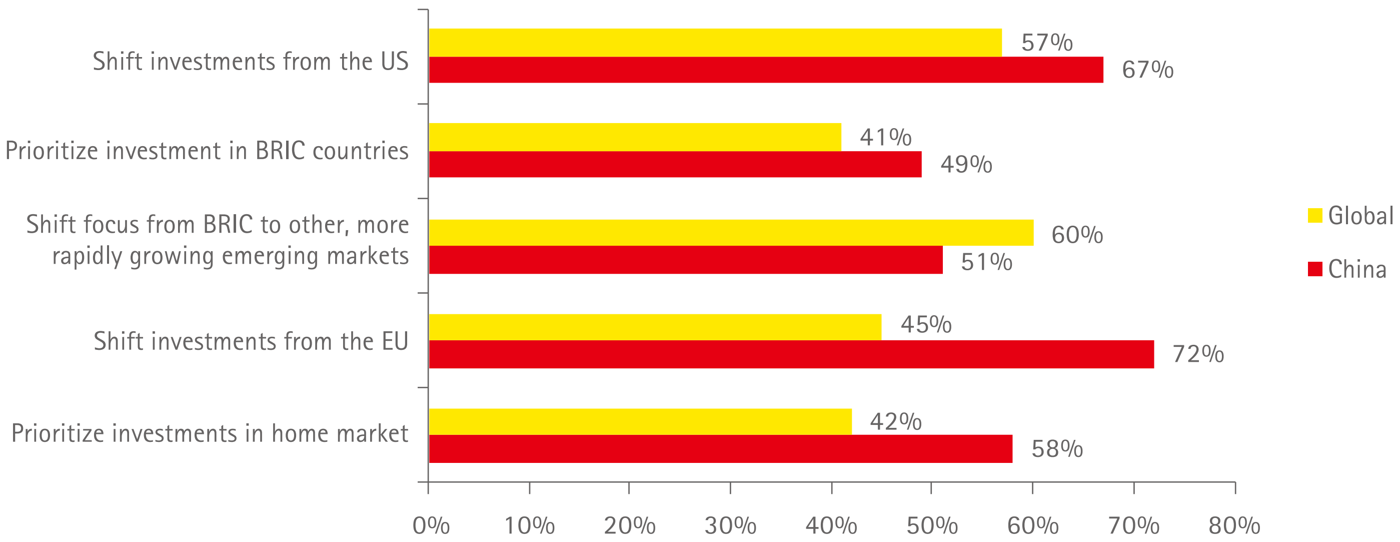
Finding and capturing growth can be a major challenge in today's volatile economy. That's especially true given the uncertainty surrounding the performance of the world's major markets. The ability to place the right bets has a dominant effect on how well companies can turn their optimism into reality.

According to our survey, the majority of Chinese companies appear to be betting primarily on their home market—which is understandable, given China's massive size and untapped growth potential. Just under six in 10 said they planned to prioritize investment in their home market, compared with 42 percent of global respondents (Figure 3). In addition, Chinese executives believe emerging economies will be their primary drivers of growth in the coming years: Forty-nine percent said they intend to prioritize investment in the BRIC countries over other emerging markets, while 51 percent expect to shift their focus from the BRICs to other, more rapidly growing emerging markets.

Chinese companies' focus on China and other emerging markets stands in marked contrast to their attitudes toward Europe and the United States (Figure 3). Just over seven in 10 (72 percent) Chinese executives believe the economies in the European Union will worsen and, thus, they will likely shift investments away from the EU in the coming year. Sixty-seven percent said the same about the United States. Although less-enticing growth prospects in the EU and US compared with emerging markets are at the root of Chinese companies' move away from these markets, that shift likely has been accelerated by ongoing difficulties overcoming political obstacles that have hampered success. For instance, many proposed acquisitions of US companies by Chinese firms have been blocked by the US government due to national security concerns.

Regardless of the countries in which China is operating, however, the route to growth in the next three years largely will involve selling new products or services—to existing customers in China (49 percent) and developed markets outside China (51 percent), and to new customers in other emerging markets (46 percent). Consistent with that approach, virtually all Chinese companies in our survey (98 percent, versus 80 percent of global respondents) plan to increase their investment in R&D in the next 12 months. In fact, while China still lags the United States considerably in R&D investment (the US is the world's largest spender on R&D at about 2.8 percent of GDP), the country has been increasing its investment at a high rate. China's R&D investment is expected to reach 1.95 percent of GDP in 2014 and 2.2 percent in 2015. That trajectory is projected to continue through the rest of the decade, resulting in China's surpassing the US by 2022. [11]

Figure 3: Percentage of executives expecting to



Enthusiasm Is High for Digital Technologies Among Chinese Companies

As they pursue growth, Chinese companies increasingly are looking to digital technologies for help. A majority of Chinese executives believe all six major digital technologies we asked about in our survey will be important to their company in the next 12 months: ecommerce, machine-to-machine communication, cloud computing, data analytics, social media, and mobile (Figure 4). In fact, Chinese executives were far more likely than their global counterparts to view these technologies as not only important, but extremely important, to their business. Furthermore, more than three-quarters of Chinese executives (compared with 62 percent of others) are convinced that digital technologies will have a major impact on their industry in the next year, with 62 percent describing that impact as a significant change and 15 percent saying it will be a complete transformation.

Chinese companies are far more likely than others (77 percent versus 59 percent) to be focusing on using digital technologies to help them achieve process efficiencies and cost reduction. This is consistent with the fact that 78 percent said they expected their companies to increase their efforts to reduce costs in the coming year. In fact, efficiencies and costs have become a major concern for most Chinese companies (especially SOEs, which have lost much of their efficiency gains from prior to 2008 and continue to lose ground to the private sector).[12] The cost of doing business in China has continued to rise, and nowhere is that increase more prevalent than in labor. The average Chinese wage has been rising significantly—from $.72 in 2001 to an estimated $6.31 by 2015.[13] This increase, coupled with productivity that lags many other industrialized countries, could make Chinese companies less competitive and be a major impediment to growth in the coming years.[14]

Yet Chinese executives in our survey are not limiting their use of digital to streamline their operations. On the contrary, a large majority of them also acknowledge digital's potential to help foster growth. As illustrated in Figure 5, about half of participating executives said digital technologies are extremely important to helping their companies grow sales, improve the customer experience, and create new products and services, and four in 10 said they are extremely important to enabling them to open new sales channels. These figures far exceed those among respondents globally.

Importantly, Chinese companies appear to be backing up their perspectives with action. Sixty-two percent of Chinese executives, compared with only 36 percent of global respondents, said at least half of their business processes are supported by digital technologies.

That said, Chinese companies also still face challenges in adopting digital technologies, the most prevalent of which are difficulties managing change (cited by 66 percent, far more than respondents globally) and a shortage of required skills to implement them (36 percent). On the other hand, some challenges are less common among Chinese firms. For instance, Chinese executives were less likely than their global peers to say their companies have difficulty with cross-functional collaboration, lack of executive support, insufficient funding for digital initiatives, and lack of customer demand for digital solutions. This last point is not surprising given the high degree of interest in digital among Chinese consumers, who are among the world's most aggressive adopters and users of such technologies.

Interestingly, Chinese companies were far more likely than others (51 percent versus 23 percent) to have the chief technology officer in charge of digital innovation, and half as likely (16 percent versus 35 percent) to have the chief executive officer responsible.

Figure 4: Percentage of executives who consider digital technologies important to their business

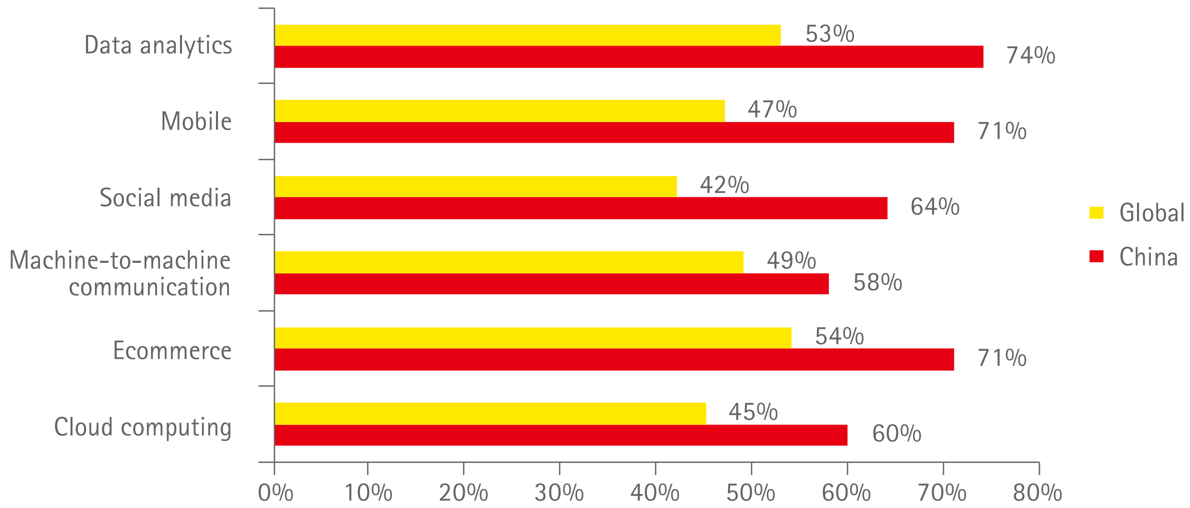
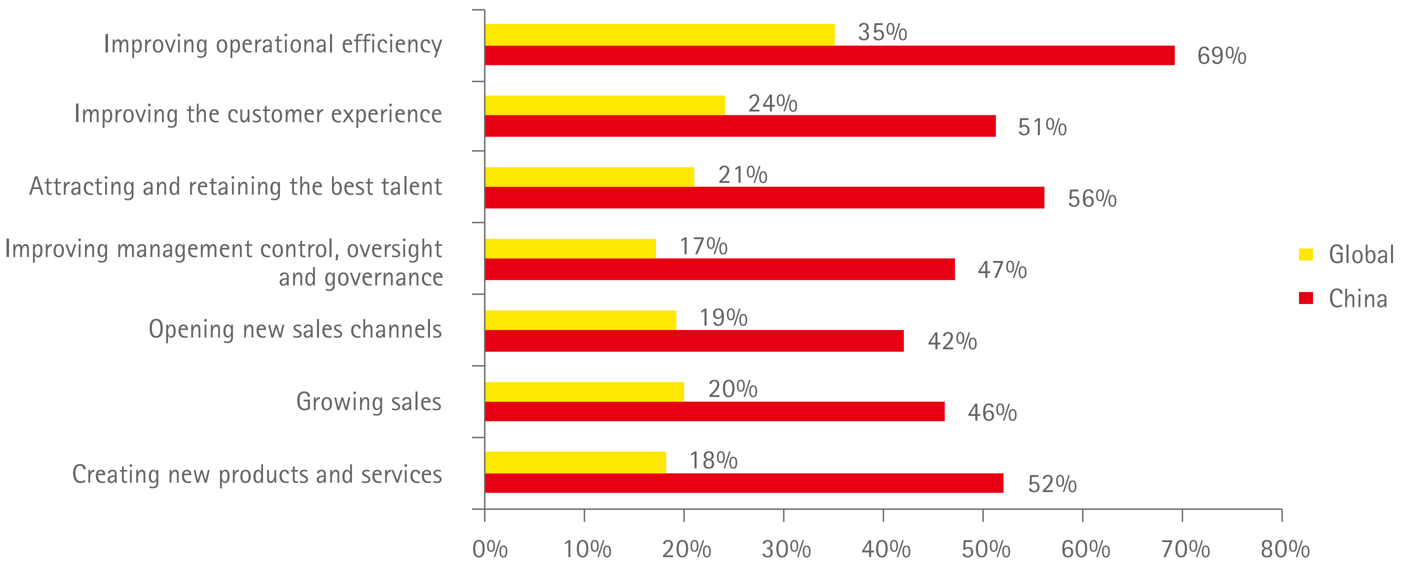


Figure 5: Percentage of executives saying digital technologies are extremely important to



Conclusion

Chinese executives' optimism about the economy and their own businesses is not unfounded. The country is still generating growth at a rate other countries dream of achieving and its domestic consumption continues to outpace other markets, including Japan, Germany and the United States. In fact, China's consumer market remains the fastest-growing in the world, largely because of very low household debt and rising incomes.[15] Yet growth is no longer at the double-digit level, and rising prices and lagging productivity threaten to erode Chinese companies' competitiveness going forward.

To translate their optimism into reality this year and in the years ahead, Chinese executives need to recognize that significant work lies ahead. Chinese companies will need to continue strengthening their innovation capability so they can develop the new products and services that are vital to ongoing competitiveness and growth. And they must make progress in closing the productivity gap between themselves and competitors. Digital technologies can play a critical role in both areas, and Chinese companies must continue to invest in these powerful tools and apply them throughout their operations to reduce costs, improve efficiencies and help reach and expand in promising new markets.

Source

1. This research was conducted by the Economist Intelligence Unit and sponsored by Accenture. It included 1,041 C-suite executives around the world representing companies from 20 countries,

2. http://news.yahoo.com/china-estimates-2013-growth-slowed-032626155.html;_ylt=A2KJ3Cb8vL1SXjoAaQ3QtDMD

3. http://ireport.cnn.com/docs/DOC-946412

4. CEIC, Gavekal Data

5. Wind Data, Accenture analysis

6. "The Power of Three: How a new approach to labor, capital and productivity can transform China's economy and businesses," Accenture Institute for High Performance, 2013

7. Economist Intelligent Unit

8. Total factor productivity (TFP or multifactor productivity), as measured by the Economist Intelligence Unit, is the part of economic output growth not accounted for by the growth in inputs (labour and capital).

9. http://smallbusiness.foxbusiness.com/entrepreneurs/2013/12/20/american-factory-revival-not-manufactured-hope/

10. The Economist Intelligence Unit's business environment rankings quantify the attractiveness of the business environment. The availability of skilled labor rating scores countries between 1 and 5, with 1 being "very poor" and 5 being "very good."

11. "2014 Global R&D Funding Forecast," Battelle, December 2013, http://www.battelle.org/docs/tpp/2014_global_rd_funding_forecast.pdf?sfvrsn=4

12. CEIC, Gavekal Data

13. http://smallbusiness.foxbusiness.com/entrepreneurs/2013/12/20/american-factory-revival-not-manufactured-hope/

14. CEIC, Gavekal Data

15. "Sinology—China Macro Strategy," Andy Rothman, CLSA, January 20, 2014

About Accenture Greater China

Accenture is a global management consulting, technology services and outsourcing company, with approximately 281,000 people serving clients in more than 120 countries. Combining unparalleled experience, comprehensive capabilities across all industries and business functions, and extensive research on the world's most successful companies, Accenture collaborates with clients to help them become high-performance businesses and governments. The company generated net revenues of US$28.6 billion for the fiscal year ended Aug. 31, 2013.

Accenture has conducted business in Greater China for more than 20 years. Today, it has about 9,400 people working in Greater China, throughout offices in Beijing, Shanghai, Dalian, Chengdu, Guangzhou, Hong Kong and Taipei. With a proven track record, Accenture is focused on leveraging local best practices and successes, and is dedicated to delivering premium client value and results. Accenture helps clients define strategy, streamline business processes, integrate systems, promote innovation and enhance overall competitive advantage to ultimately attain high performance.

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