

China

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2015

China's Business  
Environment in 2015

Another Volatile Year in  
the Long March of Reform

InterChina  
15 November 2014

InterChina



英特华

Strategy | Corporate Finance

[www.InterChinaConsulting.com](http://www.InterChinaConsulting.com)

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# Introduction: opportunities amidst volatility and variance

2014 has turned out to be another volatile year in China, and looking ahead to 2015, we should expect this volatility to continue. These few years are a turning point, as Xi Jinping initiates his reform agenda, and turning points cause turbulence. But as reforms are implemented with increasing vigor, new business opportunities will arise. Indeed, many companies continue to do well within this more uncertain and challenging environment, although disparities between sectors have become stark. Companies need to avoid being distracted by this current volatility, adjusting their approaches to cope, and seeking out the opportunities as they arise.

When it comes to state-controlled sectors such as the Oil & Gas sector, we are already seeing the reform agenda making an impact. During 2014, the sector has been opened to private Chinese investors, which in turn has provided a multitude of cooperation and sales opportunities for international investors. State owned companies, in particular those that are controlled at the provincial and municipal level, are focusing more on performance and thus spinning off non-core businesses. We will see such reform measures gathering momentum through 2015 and providing new business opportunities.

However, the economy is now very heterogeneous, and different sectors will present very different opportunities. A recent InterChina survey of over 50 China country managers reflected how the prospects for the years to come vary wildly depending on the sector and even within sectors. More now than ever, prospects and opportunities need to be assessed at the sector level.

China has always been considered a complex and dynamic market. Despite the challenges ahead, there is again cause for optimism. International companies now have the opportunity to expand and consolidate their presence, and play a larger role in the new economy. The turbulence will be manageable, and while what worked in the past will no longer be enough, the better prepared companies will flourish as long as they focus on their sector opportunities and don't get too distracted by the volatility and uncertainty.



Jan Borgonjon  
President

### Our Value

- China specialist.
- Strategy and M&A advisory.
- Focused on 5 sectors.
- **20 years** of experience.

### Our People

- Located in Beijing and Shanghai.
- Multicultural partnership.
- 60 professionals.
- Chinese, senior, industrial background.



### Our Clients

- Medium-sized to Fortune 1000.
- 500 strategy projects.
- 165 transactions (USD 6 bn).
- 2/3 of projects are returning clients.

### Our Reach: IMAP

- Leading global mid-market M&A organization.
- 40 offices, 31 countries, 500 professionals.
- Over 200 transactions p.a.
- Exclusive China partner since 2006.



# Focused On 5 Sectors

Experience, insight and networks in China's major growth sectors

 <h3>Consumer &amp; Retail</h3> <ul style="list-style-type: none"> <li>• FMCG, F&amp;B</li> <li>• Consumer Durables</li> <li>• Retail, Food Service</li> </ul>	             
 <h3>Healthcare</h3> <ul style="list-style-type: none"> <li>• Pharmaceuticals</li> <li>• Medical Devices</li> <li>• Healthcare Services</li> </ul>	             
 <h3>Industrial</h3> <ul style="list-style-type: none"> <li>• Automotive</li> <li>• Machinery</li> <li>• Equipment</li> </ul>	             
 <h3>Chemicals/Materials</h3> <ul style="list-style-type: none"> <li>• Chemicals</li> <li>• Energy &amp; Cleantech</li> <li>• Infrastructure</li> </ul>	             
 <h3>Business Services/TMT</h3> <ul style="list-style-type: none"> <li>• Professional Services</li> <li>• Multi-sector Solutions</li> <li>• Outsourcing Services</li> </ul>	             

# InterChina In A Nutshell

**20 years**

...of doing business in China.

**55**

...dedicated staff members, in  
Shanghai and Beijing.

By 2014, we had been involved  
in over **200**  
transactions worth...

**USD +6 bn.**

**9**

M&A deals closed in 2014.  
7 closed in 2013.  
10 closed in 2012.  
9 closed in 2011.

**20**

...top-line growth strategic  
projects in 2014.

**Top 5**

...independent advisory firm in  
China.



# InterChina Strategy Practice, 2014

20 projects, closely following the needs of changing market forces.

## InterChina's sector groups, for 20 years...

- Tracking market trends: More than 2,000 Senior Interviews/year.
- Maintain Sector Network: Ongoing contact with China's top 20 players.
- > 50 advisors with relevant industry background
- Support both our Strategy and M&A projects.



Healthcare



Consumer / F&B



Machinery & Equipment



Automotive & Components



Chemicals & Energy

### Strategy Advisory

- Expansion strategies
- Market penetration
- Complexity Reduction



## Main client issues 2014



Identify **new opportunities** and develop **new roadmap** in China's transformation



**Restructure** sales channels and **way-to-market** to reach customers faster and better.



Find the right approach for **inorganic growth** in sector consolidation.



**Reduce the complexity** inherent in **market-facing functions** for profitable top-line growth



**Localize** operations and production, acquisition of local companies to be 'more Chinese'.



Deal with **cost inflation** for both short-term optimization and long-term strategic moves.



Access consumers in **T2 and T3** cities, profitably.



Enter mid-quality market segment; **2nd brand strategy** through acquisition or organically.

# InterChina & IMAP: 2014

InterChina: 27 ongoing mandates; 9 successful closings, both Inbound & Outbound

<p><b>Undisclosed Party</b>                  Leading Automotive Supplier                  Germany</p> <p>acquired 70% equity stake of</p> <p><b>Undisclosed Party</b>                  Automotive Components Manufacturer                  China</p> <p><i>Buyer advised by</i></p> <p><b>InterChina</b></p>	<p><b>ICBC</b> </p> <p><b>Industrial &amp; Commercial Bank of China</b>                  Leading Commercial Bank                  China</p> <p>provided project finance to</p> <p><b>MAG</b> </p> <p><b>Manchester Airport Group</b>                  Largest UK-owned Airport Operator                  United Kingdom</p> <p><i>Funder introduced by</i></p> <p><b>InterChina</b></p>	<p><b>OHUA</b> </p> <p><b>ZhongShan OuHua</b>                  Printing &amp; Packaging Company                  China</p> <p>acquired part of the Asian operations of</p> <p><b>RockTenn</b> </p> <p><b>Rock-Tenn</b>                  Leading Corrugated &amp; Consumer                  Packaging Manufacturer                  USA</p> <p><i>Seller advised by</i></p> <p><b>InterChina</b></p>	<p><b>REPSOL</b> </p> <p><b>Repsol</b>                  Energy &amp; Chemicals Manufacturer                  Spain</p> <p>licensed its technology to</p> <p> <b>神华集团有限责任公司</b>                  SHENHUA GROUP CORPORATION LIMITED</p> <p><b>Jilin Shenhua</b>                  Petrochemicals &amp; Industrial                  Conglomerate                  China</p> <p><i>Buyer advised by</i></p> <p><b>InterChina</b></p>	<p><b>Undisclosed Party</b>                  Leading Automotive Component Supplier                  Germany</p> <p>restructured its JV together with</p> <p><b>A Leading SOE Automotive Group</b>                  China</p> <p><i>Undisclosed Party advised by</i></p> <p><b>InterChina</b></p>
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**Neptune Marine Service B.V.**  
 Marine services  
 Hardinxveld-Giessendam, Netherlands

Acquired 100% of the shares in

**Stagro Hydraulics**

**Stagro Hydraulics B.V.**  
 Offshore and Dredging Industry  
 Rotterdam, Netherlands

*Advised the Seller*





**Hansol Paper Co., Ltd.**  
 Paper Producer  
 Seoul, South Korea

Acquired

**Telrol by**  
 the labelmakers

**Telrol B.V.**  
 Label Printer  
 Almere, The Netherlands

*Advised the Seller*



**GREIF**

has sold 100% of the shares in

 **pack2pack**  
 an EarthMinded® company  
 Packaging Industry  
 Halsteren, The Netherlands

to



**GILDE EQUITY MANAGEMENT**  
 Utrecht, Netherlands

*Advised the Seller*



**China Growth Equity Investment Ltd.**  
 A special purpose acquisition company  
 Beijing, China

Acquired



**China Dredging and Pingtan Fishing**  
 Provider of dredging services and  
 a growing fishing company in China  
 Fuzhou, Fujian, China

*Advised the Buyer*



2014 sets a pattern for  
the years to come



# 2014 Review: crossing the river by touching the stones; clear direction with short-term uncertainties





# Aggressive power consolidation: SOE's and some specific sectors are affected

## Power over the institutional framework

### 1 Anti-corruption campaign...

**842 officials** in the past six months.

**47 senior officials** (ministers and above) since 2013.

### 2 ...in the military and SOE's as well



### 3 Frequent Direct political interventions such as frugality campaign, downwards adjustment of SOE leaders' salary etc.

## Power over the public

### 1 Power over social media etc...



### 2 ...Appearing to address consumer concerns



## Global Projection

### 1 Stronger regional relations

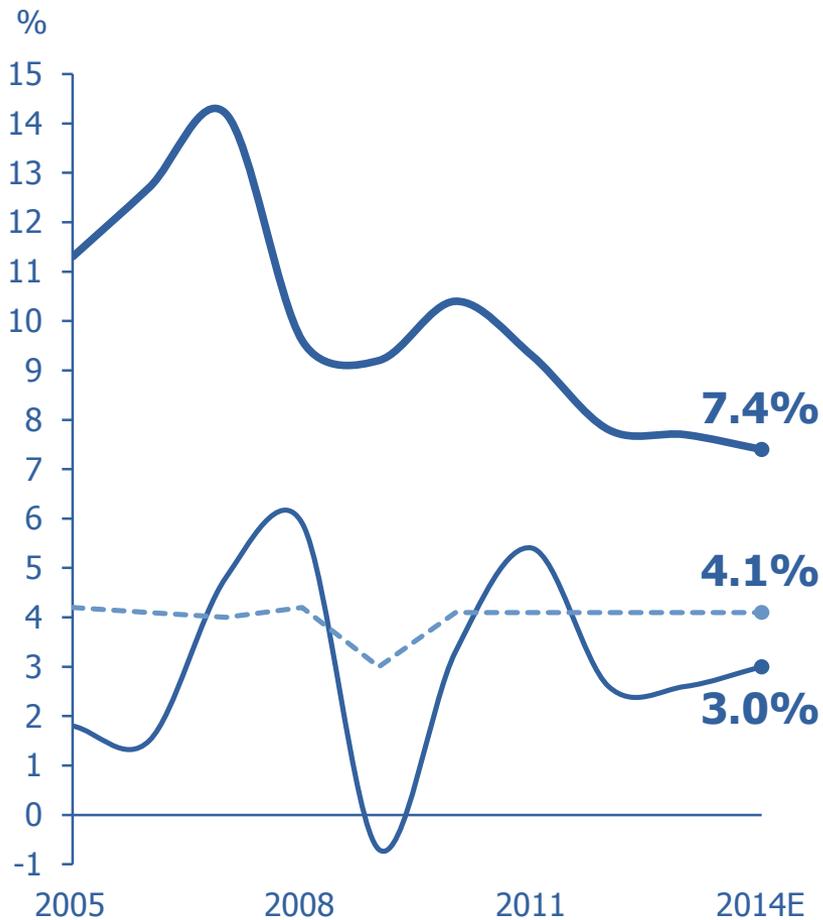


### 2 Persistent on global issues affecting China





# GDP growth is no longer the only priority...



**GDP growth**  
Official 2014 target :7.5%. Lower acceptable

**Unemployment**  
Official 2014 target: 4.6 %

**Inflation**  
Official 2014 target: 3.5%

**Environment**  
**Energy Consumption**  
**Innovation**  
**Newly emerging industries**  
**Etc .....**

# ...and economic risks are more or less under control

## Real-estate market

- **Trying to avoid a hard landing.**
- Stagnant market in 2014.
- Gov.'s intervention to boost the sales (e.g. 39 out of 45 cities discarded the Purchase Limited Policy in 2014/2Q-3Q) – the impact to be observed.

## NPL

- **Within a safe band**
- Slight increase (at 1.08% in 2014/1H).
- Meet the requirements of Basel III (Chinese Version).

## Debt / GDP

- **Increase but manageable**
- Around 250% in 2014/1H.
- Lower than USA/UK/Japan at 250%- 400%.

# Minimum growth is supported by contingency measures (Mini stimulus). Unpredictable, resulting in more difficult planning

## Stimulus: From “flood irrigation” to “drip irrigation” -

- More focused on **investment**, esp. infrastructure (rather than consumption) to ensure the growth.
- **Mini-stimulus policy is more efficient than RMB 4 trillion package from 2010**
- Some policies **encourage structural economic transformation** (e.g. policies on SMEs, the deferred taxation of R&D investment).
- **Likely to continue** in 2014 / 2015, but **specific timing and focus are less predictable.**

**“Government stimulus money is being more targeted than in the past and this is relatively positive since it avoids white elephant projects to a large degree”**

China GM of an industrial conglomerate

## Example: Automation improvement is strongly supported on the demand side

- Automation technology occupies a major place in China’s 12<sup>th</sup> FYP.
- This leads to prominence in the ministerial 12<sup>th</sup> FYP for different sectors, and down to local-level policies.



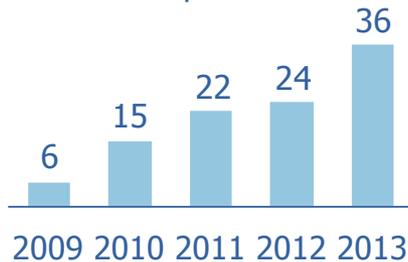
# Economic Transformation: initial success in 3 key areas

## Service Sector & Advanced Manufacturing: Early positive signals

The Service Sector increased its importance in GDP structure.



China shifted aggressively to advanced production



China's Industry Robot Sales (1,000 Units)

## Over-reliance On Real Estate: Political intervention to avoid bubble bursting

The real estate growth rate is close to historical low point.



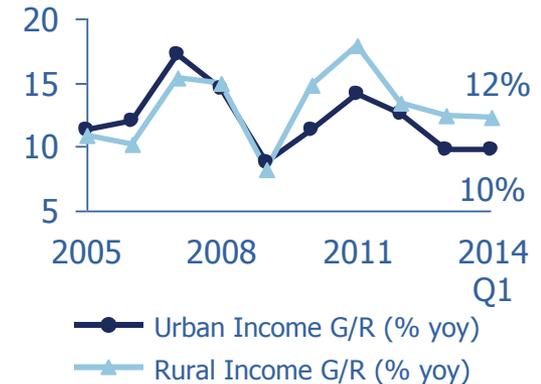
The slow-down implies significant economic risk



\*Including the real-estate and the related sectors.

## Consumption: Stable performance & targeted policies

Income growth rate lower but stable



- The consumption-related sub-sectors show mixed performance.
- Large-scale consumption incentives as in 2009/2010 less likely. More targeted initiatives.

# Reform is gradual and will take years

## Intense first year with initial progress

### Roadmap:

- The Reform Guideline in the 3<sup>rd</sup> Plenum
- Defined 60 key reform initiatives.

### Leading Org.:

- Restructuring Committee (深改组).
- Led by Xi Jinping, including all ministers and other senior officials.

### Milestone Revision:

- 7-year Reform Planning.



### Initial progress:

- 39 out of 60 initiatives kicked off.
- 130+ reforms announced were made from Nov. 2013 – August 2014.

**Gov. Function Reform:**  
Simplified gov. admin. Approval process

**Financial Sector Reform:**  
Approved private banks

**Open-up Reform:** Piloting measures in FTZ

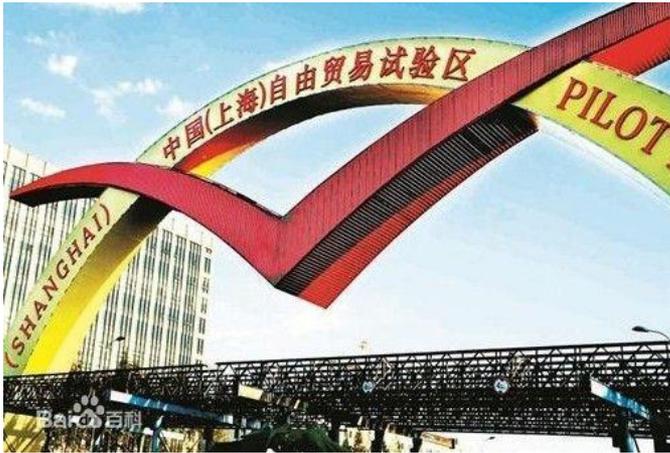
**Fiscal and Taxation Reform:** The Budget Law; VAT reform.

**SOE Reform:** Mixed ownership piloting (e.g. Oil & Gas)

**Urban / Rural Reform:** The new Hukou policy.

# SH FTZ: The reform avant-garde

## SH FTZ is one year old with the initial achievements...



12,000 newly registered co, including 10% FIE.

RMB 740 bil revenue (2014.01-06), with 11.2% g/r

## ...and some pilot practices are now implemented nationally

Negative List



- Suzhou Industry Zone
- Chengdu
- Shenzhen Qianhai

New Registered Capital System



- China since March 1, 2014

Interest Rate Liberation  
 Reform Of Small Foreign Currency



- Shanghai since June 2014.

Customs Administration Innovation



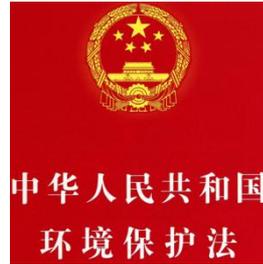
- Phased approach.
- Under implementation nationally in Sept. 2014

More FTZs are either planned (Tianjin, Chengdu, Hefei, Shenyang, Yinchuan etc.), or under initial review (Guangdong).

# “Popular” issues are a top priority: positive for the future - negative in the short term

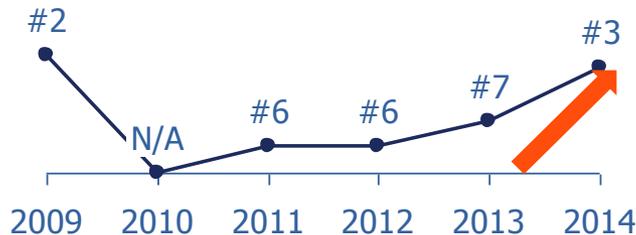
## Environment

- Environment as important as growth
- Basis for sustainable development.



- From “Policy” to **“Implementation”**.
- Effective on Jan. 1, 2015
- The 1<sup>st</sup> significant revision since 1989.

Ranking of “Food & Drug Safety” In Annual Consumer Survey by People’s Daily



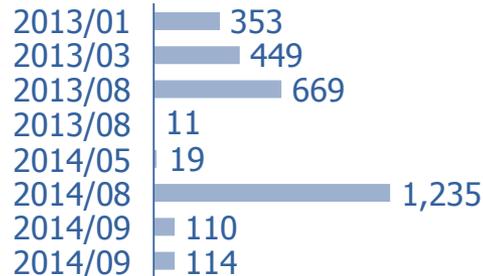
## Food Safety

- Top political concern
- Opportunities exist along the value chain.

## Pricing

- Attracts the attention of the NDRC.
- Both Chinese and FIE are on the radar.

### AML Penalty Since 2013 (RMB Mil)



Sector	# of CO	Examples
TV	6 (CHN+FIE)	LG
Baijiu Wine	2 (CHN)	Maotai
Milk Powder	6 (FIE+CHN)	Abbott
Gold Retail	6 (CHN)	LaoFengXiang
Glasses	7 (FIE)	Essilor
Auto Comp	12 (Japan)	Denso
Insurance	24 (CHN)	Zhajiang Ins.
Cement	3 (CHN)	Jilin Cement



# FIE's feel 'targeted': the end of 'positive discrimination' rather than a deliberate strategy

## Anti-Monopoly

- For non-pricing related AML, only 2 FIE cases of Microsoft & Tetra Pak out of 39 cases.

***FIEs takes less than 10% of AML cases by China's gov.***

***2014/09/09***



## HC Anti-corruption

- Selective?
- Worries by some FIEs – supported by others

***.....the anti-corruption campaign in the pharma industry.....has given an impression of rising economic nationalism.***

***Chairman of an Investment Group***

***The recent anticorruption moves in healthcare have actually helped our business by slightly leveling the playing field.***

***China GM of a Fortune 500 company***

# FDI: short-term slow-down, with long-term structural change

**China is likely to remain the 2<sup>nd</sup> largest FDI destination, albeit with lower growth**

**FDI remains important, but to different degrees for different sectors and companies**

## 1 FDI is stagnating

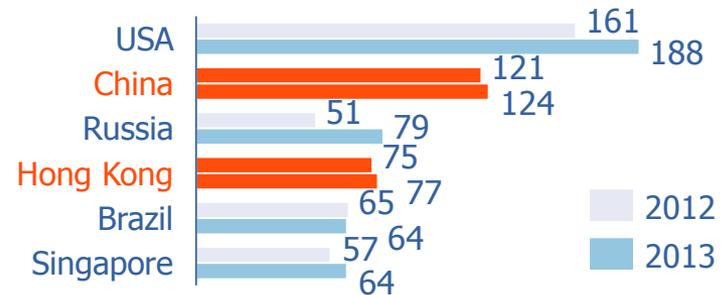


## 2 FDI's new trends

- FDI will shift to a mixture of new investments and profit reinvestment.
- China's Foreign investment policies are under reform as well: e.g. piloting reform measures in FTZ, simplification of company registration procedures, experimentations with "national negative list" etc.

## 1 China (incl. HK) remains the No. 1 FDI destination globally

Top 5 Economies by FDI Inflow (USD billion)



## 2 Shift from manufacturing to service

FDI In China (USD billion)



\*Service Sector includes wholesales & retail, rental, leasing, transportation, ICT, utilities etc.

# Uneven sector performance: in spite of slower growth most companies continue to report China sales growth

## Uneven sector performance

Oil & Gas  
 Digital Economy  
 Automotive  
 Medical  
 Imported food  
 Rail & Aero.....



Chemicals  
 Machinery  
 IT sector .....



Luxury  
 Construction  
 FMCG  
 Steel  
 Shipbuilding...



...

## Top-line Growth Of MNCs In China In 2014 1Q or 2Q

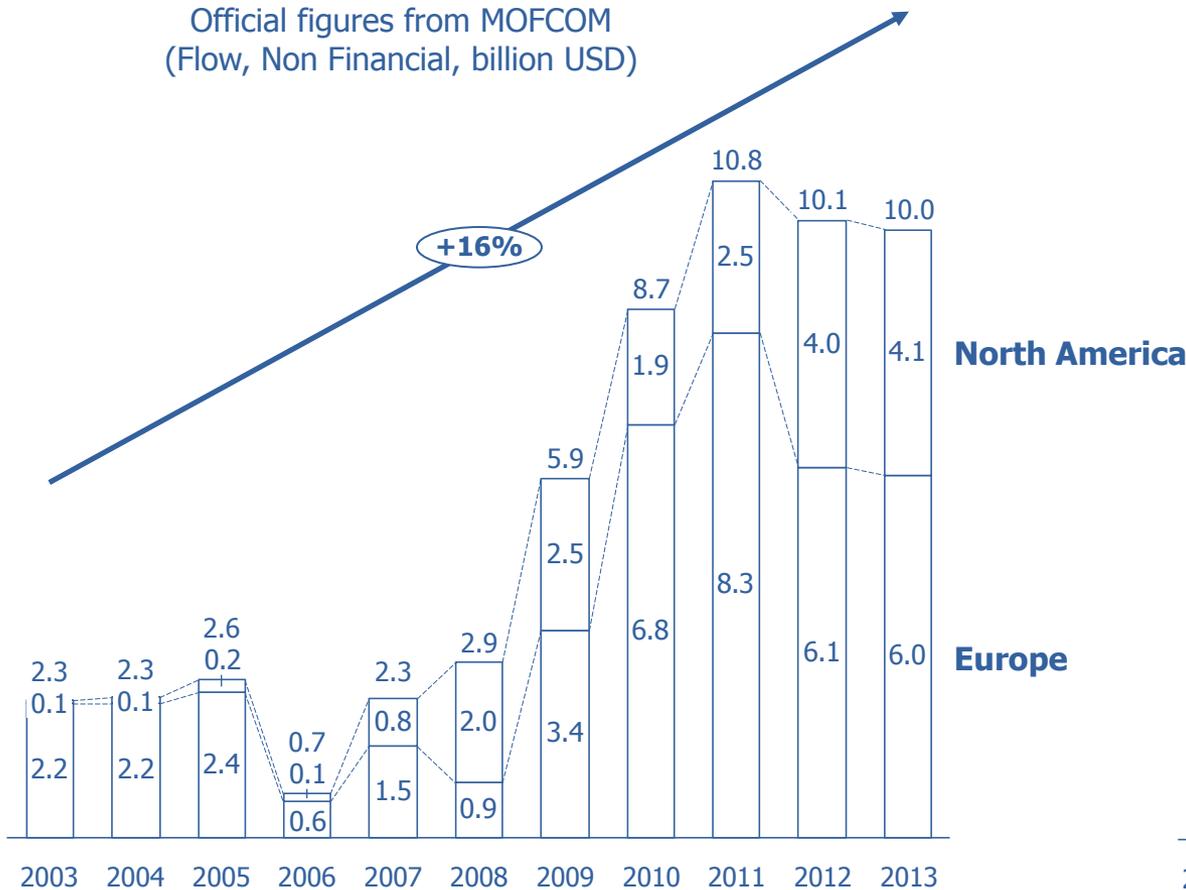
	Luxury	Constr. Eng.	HC	Chemical	FMCG	Industry	Auto & Comp
Fast Growth							Johnson Controls 
Medium Growth					     	     	
Flat Growth				 			
Large Decrease							

Note: This table only includes some listed foreign companies that disclose their China performance. If not listed, their China performance may be an estimate based on public info.

# Chinese Investment in North America and Europe is rising rapidly... and will continue to do so

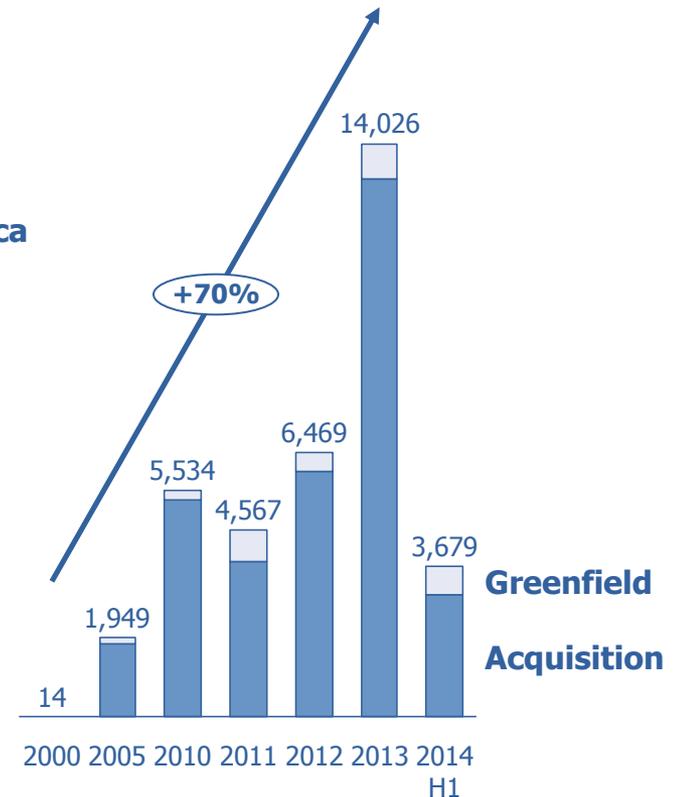
## China ODI to Europe and North America

Official figures from MOFCOM  
(Flow, Non Financial, billion USD)



## China ODI to the US\*

Figures from Rhodium Group, US  
(Flow, All Industries, million USD)



Source: MOFCOM, Rhodium Group China Investment Monitor

\*Note: Not comparable with MOFCOM data due to different data scope.

# China 2015 Forecast



# 2015: extension of 2014, but more intense reform

Scenario	Probability	Possible Outcomes
<p><b>Progress With Reform</b></p> <ul style="list-style-type: none"> <li>• Sustained consolidation of power, sufficient to push reform agenda.</li> <li>• Roll out of reforms will be patchy ... but with initial results.</li> <li>• Trial and error approach means that uncertainty will continue.</li> </ul>	90%	<p><b>Economic Performance</b></p> <ul style="list-style-type: none"> <li>• <b>GDP Growth:</b> around <b>7%</b>.</li> <li>• <b>Inflation:</b> 2.5% - <b>3%</b>.</li> </ul> <p><b>Rebuilding Of Momentum</b></p> <ul style="list-style-type: none"> <li>• <b>Slow Un Freezing on investment</b> decision-making.</li> <li>• <b>Partial privatization</b> of provincial SOEs. More competitive.</li> <li>• Steady financial reform</li> <li>• <b>Consolidation</b> to continue, but over-capacity will remain.</li> <li>• Another <b>mini-stimulus</b> (investment, liquidity, subsidies)</li> <li>• <b>Deregulation</b> in several new sectors. Less government approvals</li> <li>• Strengthening of <b>consumer confidence</b>.</li> <li>• <b>Evolving consumption</b> patterns.</li> <li>• <b>Social reforms crawl along</b></li> </ul>
<p><b>Reform Program Stalls</b></p> <ul style="list-style-type: none"> <li>• Vested interest groups exert resistance.</li> <li>• Xi meets political deadlock.</li> <li>• Investor and consumer confidence levels drop.</li> </ul>	10%	<p><b>Dark Clouds Forming</b></p> <ul style="list-style-type: none"> <li>• Economic growth slows to &lt;5%.</li> <li>• Investment paralysis, drying up of access to capital.</li> <li>• Increase in capital flight.</li> <li>• Exacerbated competition and price battles.</li> </ul>



# Increased Reform Measures will bring more trial-and-error: surprises and more volatility

## Market Voices

**"The uncertainty in 2015 will be similar or more than 2014, but we expect that all the reforms related to social and environmental issues will lead us to a more fair competition"**

*Asia GM of Int'l auto comp Co.*

**"Salary inflation is decreasing, and will be between 5-10%; lower than before"**

*China President*

**"Definitely more focused on efficiency of capital deployment ...rather than chasing market share or topline growth."**

*China CEO of Fortune 500 HC Co.*

**"Vicious circle among int'l players as they will lower their prices, too"**

*GM of a leading German MT Co.*

## 2015 Outlook

### Greater Sector Differentiation

- E.g. industrial vs consumption-related sectors.
- Incl. different sub-sector performance.

### Fiercer Competition

- Difficult to maintain premium.
- Demand concerns.
- Complex value chains.

### Consolidation

- Changes the dynamics of many sectors.

**More volatility in the short run; Good for Medium Term** **2015**

### Cost Increase

- Continued cost increases...
- ...though more moderate.
- Margin pressure.

### Continued Imbalances

- Excess capacity.
- Real estate bubble.
- Regional debt tensions.

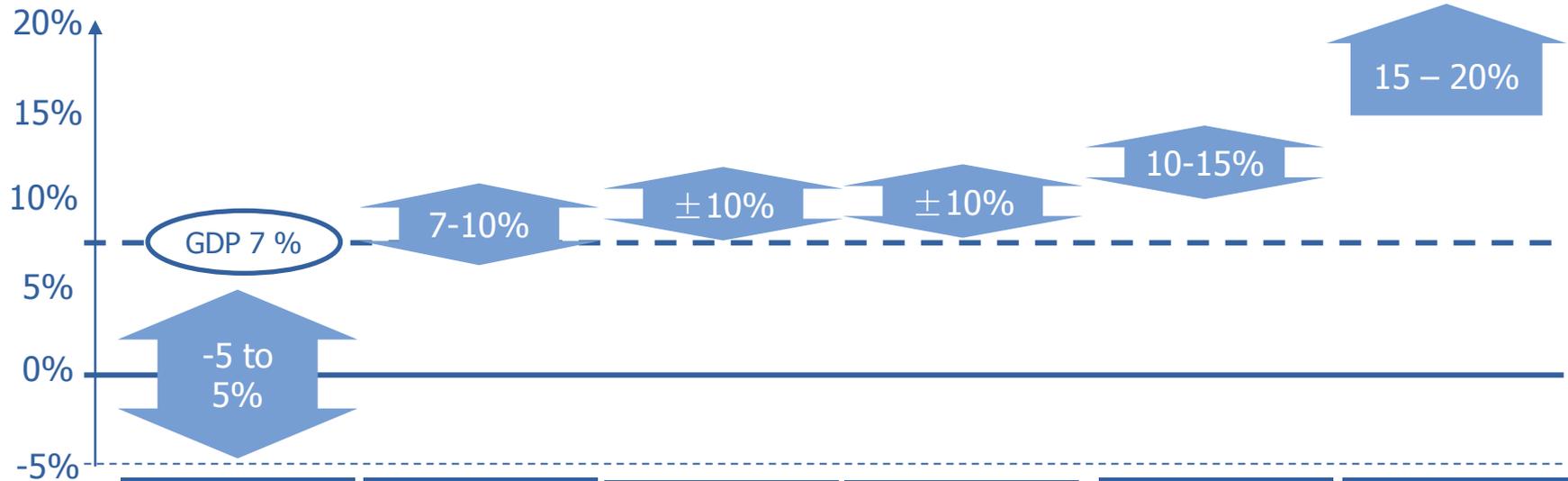
### Perceived Uncertainty

- Continued mini-stimulus, but uncertain in scope and timing.



# 2015: Bigger differences in growth patterns across sectors

## Our clients' consolidated forecast for next year



Construction	Machinery	Consumer/F&B	Chemicals	Automotive	Healthcare
 <ul style="list-style-type: none"> <li>• Re-structuring capacity.</li> <li>• M&amp;A outbound.</li> </ul>	 <ul style="list-style-type: none"> <li>• POE customer shift</li> <li>• Services as a business</li> <li>• Slow consolidation</li> </ul>	 <ul style="list-style-type: none"> <li>• NPD.</li> <li>• Imports.</li> <li>• Online.</li> </ul>	 <ul style="list-style-type: none"> <li>• NPD, S&amp;D Revamp, local R&amp;D.</li> <li>• Consolidation thus M&amp;A.</li> </ul>	 <ul style="list-style-type: none"> <li>• Scale / Quality/ Service (aftermarket)</li> <li>• Consolidation thru M&amp;A.</li> </ul>	 <ul style="list-style-type: none"> <li>• Partnerships (access to market, to complete offerings)</li> <li>• Reinventing of WTM models</li> </ul>



# Automotive components: more pressure from competition, vertical and horizontal integration, aftermarket, NEV

## Market: High-speed growth, greater challenges.

- Still driven by China's megatrends (urbanization, individual consumption growth); will grow at near double-digit speed.
- Continuous pressure on cost/price, quality, service and R&D.
- New market entry will be increasingly difficult (challenge for new entry or horizontal expansion).

- **Improve efficiency to maintain profitability.**
- **Develop dual organic and inorganic growth track.**

## Consolidation: Driven by state owned OEs; vertical and horizontal

- SOEs will drive growth (e.g. SAIC-Huayu's series of transactions, Dongfeng internal appliance project, etc.).
- Local private OEs and suppliers are obviously under-performing.
- Vertical integration to improve cost and scale; horizontal integration to gain better access to OE through JVs.

- **Be selective about possible target/partner.**

## Aftermarket: Tomorrow's battle field

- Likely to be a main growth point in the next 3-5 years.
- Regulatory environment improving; OE-4S monopoly disbanded in the long-term.
- Distribution and service capability will be the key to success.

- **Invest in capacity early on.**
- **Be systematic instead of opportunistic.**

## NEV: Possible speed up

- More practical and realistic gov. goals and support will accelerate development; BEV / PHEV is likely the key focus.
- The supply chain development is lagging, asking for the trade-up.

- **Build initial presence in this eco-system.**





# Machinery sector: uneven growth heavily impacted by stimulus policy, consolidation and development of services

<b>Market: Uneven development</b>	<ul style="list-style-type: none"> <li>• Large differences between client sectors – growth, stagnation, and contraction can all be seen.</li> <li>• Automation is key - cost increases and quality requirements.</li> <li>• POE clients now more dominant than SOE, but have different demands (more efficiency oriented)</li> <li>• Financing more difficult – increase in leasing</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Review client focus and portfolio.</b></li> </ul>
<b>Competition: Sales and services, adaptation key</b>	<ul style="list-style-type: none"> <li>• Foreign competitors are main source of competition.</li> <li>• Services and solutions will drive sales.</li> <li>• Key competitive parameters: customer orientation (pre-sales, solution offers, post-sales service), product adaptation, market references.</li> <li>• Adaptation to local market trumps production localization.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Benchmark and restructure; focus on structure of all sales</b></li> <li>• <b>2nd brand not workable?</b></li> </ul>
<b>Policies: Impactful and transformative</b>	<ul style="list-style-type: none"> <li>• Many sectors that consume machine tools are sensitive to policy change: e.g. construction, railways, windpower</li> <li>• Opportunities change with each policy change</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Monitor closely, maintain high flexibility</b></li> </ul>
<b>Consolidation: Losers leave, Chinese look abroad</b>	<ul style="list-style-type: none"> <li>• Concentration of sales among successful companies, both foreign and Chinese. Weak will exit as opposed to being bought.</li> <li>• Some specific opportunities for acquisition.</li> <li>• Chinese companies more active internationally</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Identify targets early on</b></li> <li>• <b>Look at global opportunity</b></li> </ul>



# F&B Sector: In tougher conditions, seeking new sources of growth

<b>Offering: New product development</b>	<ul style="list-style-type: none"> <li>• Many categories slowed through 2014 because of slowing economy, lower consumer confidence, frugality campaign.</li> <li>• NPD has become key growth driver for F&amp;B.</li> <li>• Premiumization is new, hot trend, but more than just pricing, branding, or origin. NPD needs to better connect with local consumers.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Run in-country NPD to meet local consumer needs.</b></li> </ul>
<b>Origins: Imports outpace local</b>	<ul style="list-style-type: none"> <li>• Since 2008 melamine crisis, imported food has CAGR of 32% in ~5 years.</li> <li>• Demand for safe foods and diversifying diets drive growth.</li> <li>• This presents strong potential for food-producing countries.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Opportunities for exporters to China.</b></li> </ul>
<b>Channels: The rise of online</b>	<ul style="list-style-type: none"> <li>• 2013 Online retail reached USD 300 bn in China, ~8% of total.</li> <li>• Growth of online sales of food will be rapid as purchasing behavior develops and logistics improve.</li> <li>• This will impact a diverse range of categories, from already-advanced infant formula to perishable goods.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Factor online retail into channel strategies.</b></li> </ul>
<b>Consolidation: Starts now, ends with new global 100</b>	<ul style="list-style-type: none"> <li>• Consolidation process is just beginning, starting with the dairy category and spreading throughout the F&amp;B industry.</li> <li>• Consolidators will be multi-category players, leading to the emergence of strong national groups that enter the global 100.</li> <li>• Multinational F&amp;B players need to have a pro-active strategy to ensure they come out on top.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Come out on top of the multi-category consolidation</b></li> </ul>



# Chemical sector: Shift from quantity to quality development; revamp sales & distribution strategy.

## Market: Slow-down, uneven downstream development

- Demand structure change and growth rate slowdown.
- The promising downstream sectors, related to new materials and green technology, are likely to outpace.
- Volume might bounce back, but may feature price pressures.

- **Review client sectors.**
- **Proactive NPD.**

## Demand: trade-ups and greater needs

- Further demand trade-up asks for new chemicals or applications.
- Customer are requiring more help from Chemical companies – Chemical companies will need to exceed specifications.

- **More frequent opportunity reviews.**
- **Proactive NPD.**

## Route-to-market

- Hybrid of direct and indirect sales might become mainstream.
- Technology service (pre- and post-sales) becomes more important.
- Value-added distributors likely to emerge, chance to restructure distribution model.

- **Benchmark and restructure.**
- **Revamp distribution model.**

## Consolidation: faster, backwards integration

- Consolidation will accelerate, weak will exit instead of sell.
- Increasing Chinese competition brings more invisible champions in niche sectors as potential targets.
- Likely more backwards integration into the suppliers for enhanced value chain efficiency.

- **Identify targets early on.**



# Healthcare sector: Trend towards bottom-line instead of top-line



## Pharma: Continued compliance scrutiny, price control, tighter portfolios

- Market growth: 10 – 15%.
- Access to doctors / decision-makers remains difficult.
- Price control and biddings eroding profits,
- Patented drugs as the winner, branded generic as the loser
- Continued registration barriers / uncertainties.
- Tighter portfolios with new / efficient WTM approaches.
- Opportunity TAs: Diabetes, respiratory, mental disorders.

- **Focus on key TAs.**
- **Better pipelines.**
- **Efficient sales ops.**
- **Commercial partnerships.**

## Medical Devices: Looming concerns on discrimination of imports

- Market growth: 15 – 20%.
- China aiming at lowered dependency on import products.
- NDRC investigating device profit margins.
- Central tenders.
- Product registrations remain difficult, increased requirements on Class II products.
- Enhanced pressure on compliance and WTM models.

- **Managing regulatory costs and process**
- **S&D streamlining**
- **Product localization**
- **M&A**

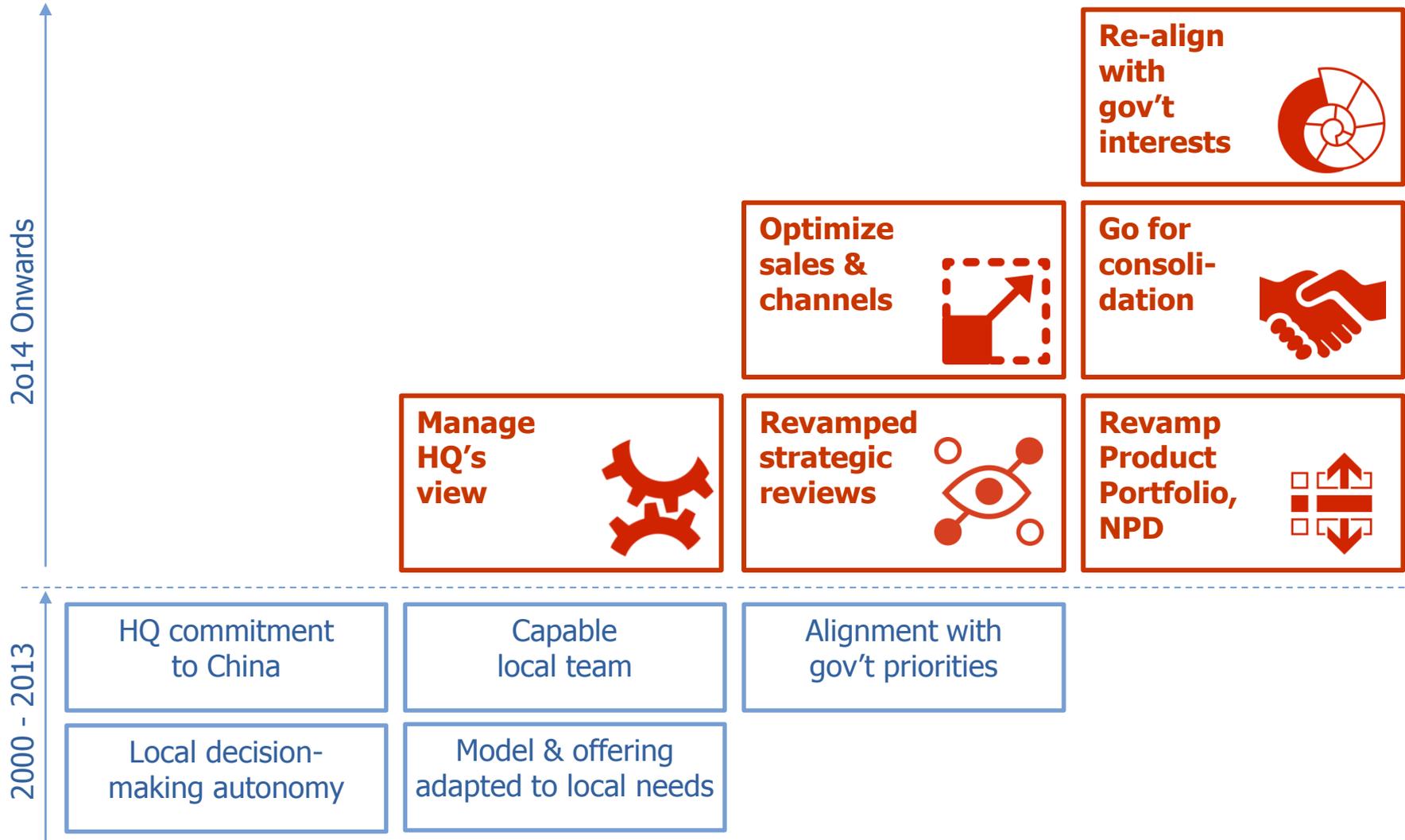
## Healthcare services: Dawn of the private segment

- Further deepening of reform
- MoH privatization scheme
- Gov't pilot for wholly foreign-funded hospitals in 7 cities
- More institutions set up in Shanghai FTZ.
- Institutions drive towards higher profitability.

- **Better market access**
- **Vertical integration**
- **Int'l best practices**

How are our clients  
reacting to these  
challenges?

# China strategies need to be more responsive: New success factors are being added, while the old ones become even more important





# InterChina Survey of >50 China CEO's: Key Directions

## Sales & Service Revamp

- "Overall growth will continue with a certain slowdown... and we will focus on distribution channel consolidation and re-organization"
- "The increasing complexity in the organization with both client and product matrix creates problems...we are planning sales optimization, especially on KAM level"

## Acquisitions and Divestitures

- "We need to be part of the Consolidation Process... We are planning several acquisition for 2015, and building a pipeline for next years"
- "Focus on core business units and best performing products... get rid of the rest"

Top 4

## Profit Protection / Operational Excellence

- "It is truth that cost are increasing, but our profits are still the same... economies of scale and efficiency gains are coping with the gap"
- "We are confident to compete on a high cost environment... most of our Chinese competitors do not know how to face this challenge"

## Product Portfolio Strategy

- "We are planning to develop new applications ... to become known in the market as a development partner more than as a "commodity" supplier"
- "20% g/r is planned in China. More on services"



# Non-traditional Portfolio Development: Unlock your growth potential

## To unlock your growth potential

- Decide on where to fight and where not – not all segments are relevant.
- Alliance with KA / joint NPD.
- Piloting and adapting.
- Operational efficiency (esp. distribution).
- Enhance cross-selling.

Existing Portfolio

New Solution

New Application

New Product



**Natural Gas (NG): To extend the core product know-how into providing a solution.**

- Case: As a leading supplier of rotating equipments to the oil & gas sector, Company C developed mobile LNG liquefaction systems **based on its world-class compressor and its reengineering know-how** to serve the emerging offline NG sector.



**Chemical NPD to satisfy new downstream sectors.**

- Case: Company B identified the **emerging policy-driven demand** for **environmentally-friendly** products in the tire sector and acted upon the trend.

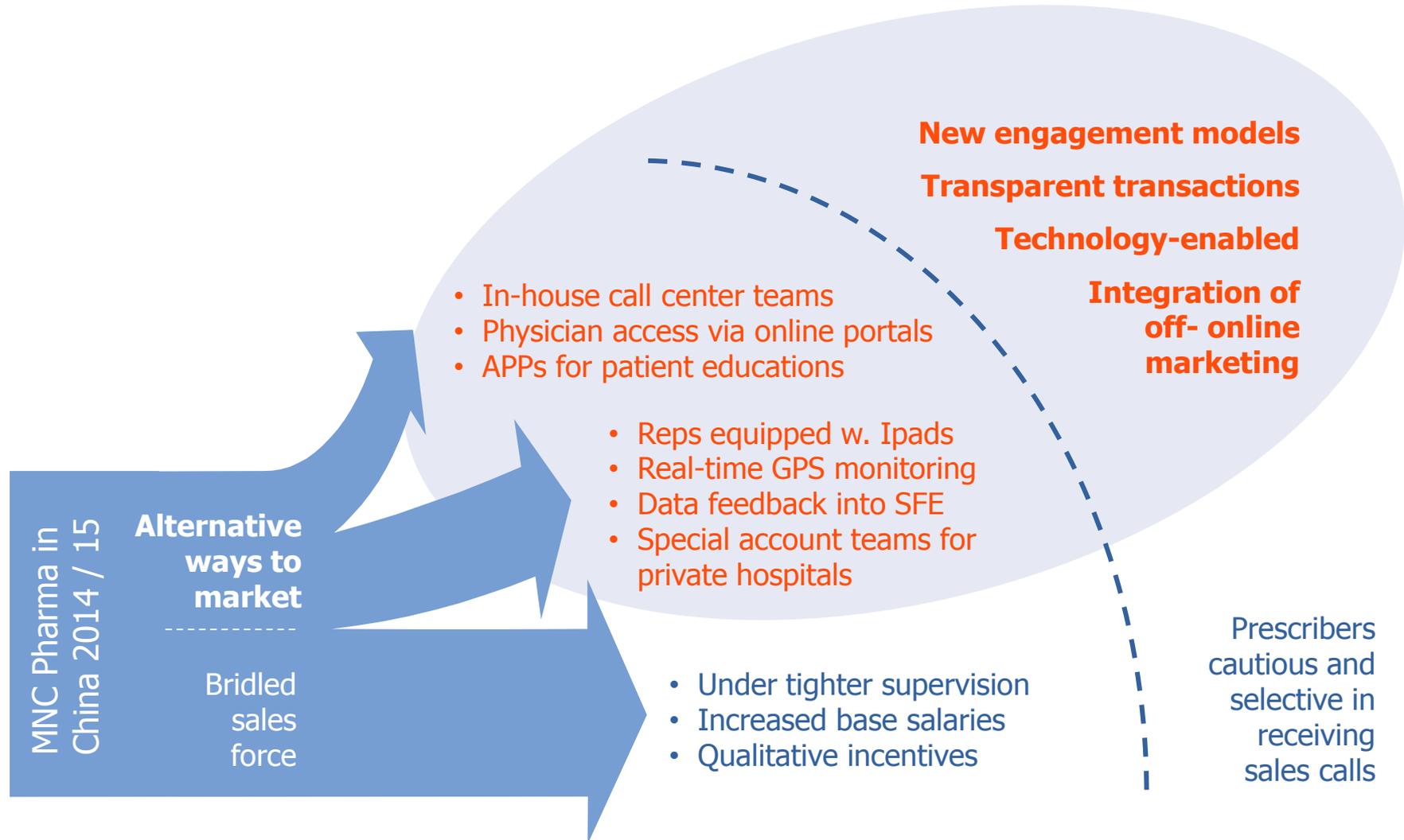


**F&B NPD to meet local needs, capture new sources of growth, and capture higher margins.**

- Case: In the beverages category, introduction of a **new “recruiter” product** with a milder taste that attracted **consumers from adjacent categories previously put-off by the bitter taste.**



# Sales & Marketing Revamp: MNC pharma in China are adapting their approach to market their products towards customers



# Consolidation: Leverage consolidation trend to accelerate growth

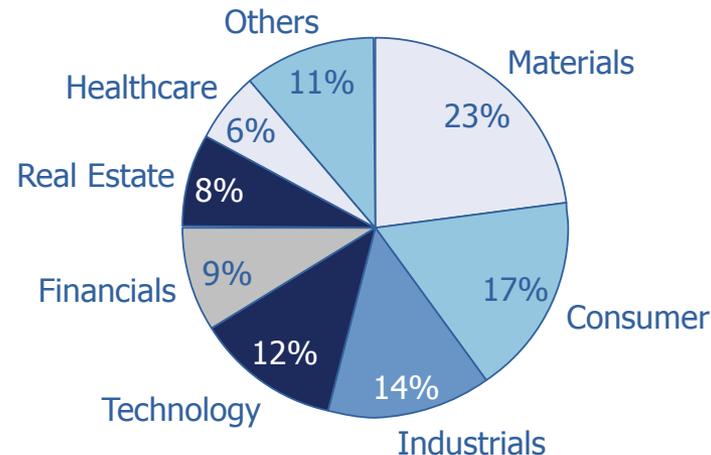
## Current Themes

- With GDP growth at 7% China remains attractive; a hunting ground for MNCs looking to further expand and seek more revenue-generation.
- Most active sectors for inbound M&A – Materials (incl. Energy & Power), Industrials, Technology; over 50% of total deal volume.
- Divestments by MNC are increasing too, due to challenges in strategy, culture, and profitability

## InterChina Forecast 2015

- Divestments to increase, as some MNCs look to exit and readjust their portfolios.
- SOE reforms: promote economic growth and reduce inefficiencies. This will spur restructuring and investment opportunities.
- The capital markets will impact domestic M&A activities. Assuming bullish equity markets, we anticipate increased M&A activity.
- More relaxed regulatory (approval) environment, availability of acquisition financing, and emergence of buyout funds will increase transaction volume.

Most Active Inbound M&A Sectors Over The Last 5 Years, and likely in the future



InterChina



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