

Resetting Your China Strategy and Operations: Navigating the New Normal

April 2024

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China macro-economy outlooks and implications for MNCs doing business in China



Executive Summary

“The Next China is China” amidst evolving macro-environment dynamics

- Lower-than-anticipated figures have led to widespread concerns, primarily among the Western media, over the prospect of China's economic development
- China's post-COVID economic recovery has coincided with a critical period of economic transition, which poses multiple challenges simultaneously to China's economic growth
- China's contribution to world GDP is anticipated to remain significant, making substantial contributions to future global GDP growth
- The Chinese government has implemented a series of monetary, fiscal and commercial policies to ensure high-quality economic growth and still has “ample policy space”

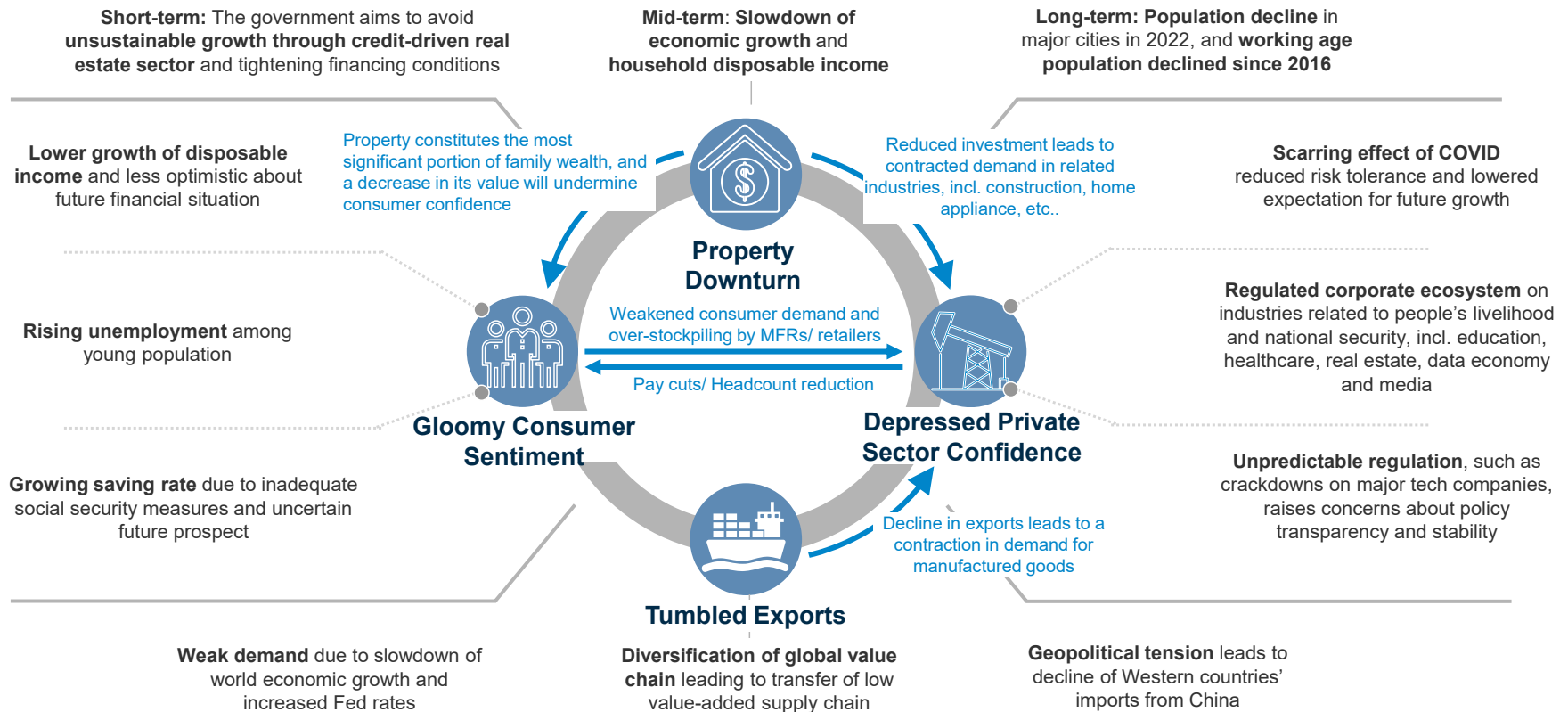
We see fundamentals and opportunities in place from mid to long term, underpinned by new macro-environment dynamics in China

- **Three enduring trends:** China continues to be an appealing narrative for MNCs, remains a critical player in the global value chain, and is evolving into a premier global learning hub
- **Three emerging shifts:** China's growth trajectory is transitioning towards a slower yet qualitative pace, undergoing structural transformations, while global geopolitical tensions are on the rise

Opportunities always come with challenges for MNCs in China. MNCs now must make careful choices to re-adjust their China strategy. Strategic implications for MNCs are in the new era: 3 dimensions and 4 decisions

- MNCs meticulously evaluate three pivotal dimensions in their China strategy: **Transnational benefit / risk**, **Sector attractiveness and dynamics**, and **Ability to win / ability to contribute**
- Depending on their position within these 3 dimensions, MNCs can choose from 4 strategic options to navigate their business in China – **Localize to thrive**, **Carve out to compete**, **Diversify from China**, and **Exit China**. Leading MNCs have been recalibrating their China strategies
- Each decision underscores the imperative for MNCs to realign their equity structures, decision-making and governance, brand positioning, product innovation, supply chains, talent management, technology and data strategies in China

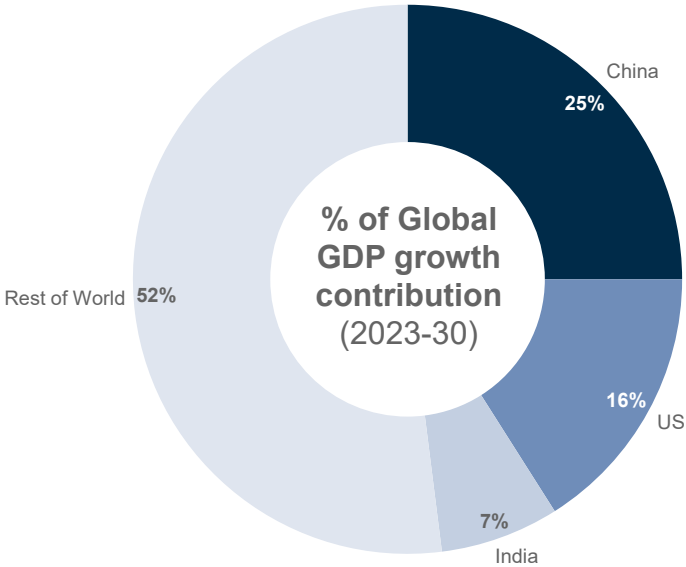
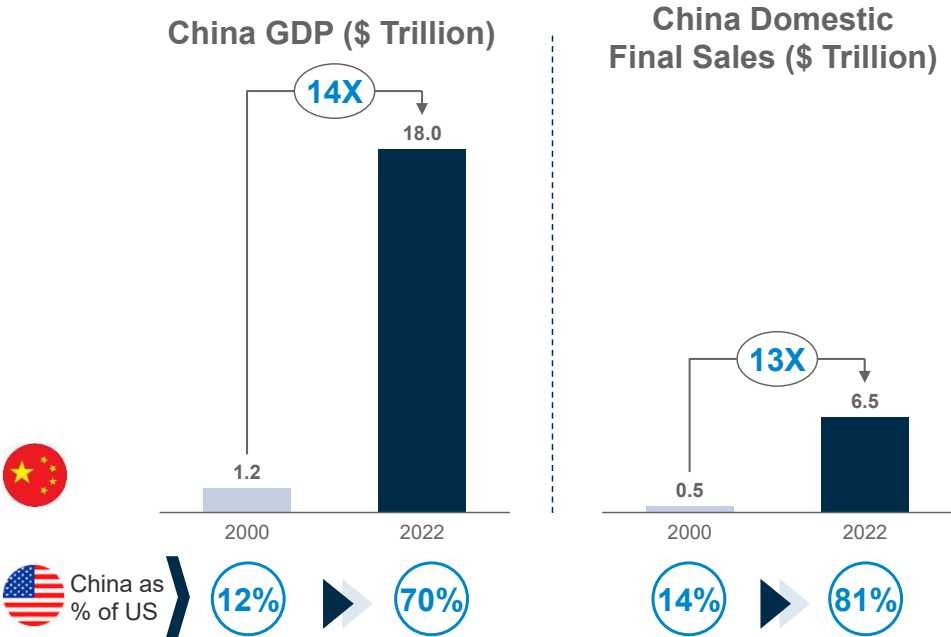
China's post-COVID economic recovery has coincided with a critical period of economic transition, which poses multiple challenges simultaneously to China's economic growth



China's contribution to world GDP is anticipated to remain significant, making substantial contributions to future global GDP growth

China has grown into the world's second-largest economy with GDP and consumer market comparable to US

Looking ahead, China continues to make a substantial contribution to global GDP growth



Source: NBS, National Bureau of Statistics of China, World Bank, analyst reports, lit research, A&M analysis

The Chinese government has implemented a series of monetary, fiscal and commercial policies to ensure high-quality economic growth and still has “ample policy space”

Unveiled economy growth stimulus

Future policy space



The Central Bank
- Monetary Policy



1T

Loan Liquidity



25 basis point cut announced for the five-year loan prime rate (LPR) in February 2024.

Cash requirement ratio reduced in March and September 2023, and in February 2024, providing **1 trillion RMB** liquidity for commercial banks

Structural financing tools provided for lower-cost financing to support target industries like agriculture, green economy, and technology

Interest rates can be further reduced to boost investment and consumption

- Near-zero inflation allows for controlled inflation, maintaining a higher real interest rate than Western countries

China's major banks have a 10.5% cash requirement ratio, higher than Western counterparts, and can be **further reduced for liquidity**



The Ministry of Finance
- Fiscal Policy



1T

Bond

Tax reductions for small businesses and individuals extended until 2027, with further structural tax reductions expected post the central economic conference

Approval granted to issue an additional **1 trillion treasury bonds** in October 2023 and another **1 trillion** in 2024 for natural disaster reconstruction and catastrophe prevention

China's government debt remains low compared to Western countries, indicating room for growth financing

- Based on BIS¹, China general government debt-to-GDP ratio is around 79%, while western countries (US 110%, UK 101%, other EU around 92%) and Japan (229%)



Central Economic Work
Conference/State Council
- Commercial Policy



↑



China lifted foreign investment restrictions in 2021, removing barriers in auto, telecom, and planning to do so in manufacturing, medical, and professional services. **The 24-Point Guidelines and Action Plan** aim to attract foreign investment, facilitate data flows, and business travel

Efforts to promote **industrial innovation, digital economy, AI, and bio-manufacturing** are underway

Measures to boost domestic demand include **shifting consumption to tourism, entertainment, smart homes, and NEVs through tax reductions and fund withdrawals**

Focus on promoting 'New Quality Productive Forces,' especially in tech industries like AI, biotech, and green development




Government aims to streamline the Law of Government Procurement to **facilitate MNCs in securing government contracts**

Efforts to align with **high-standard international economic and trade agreements (CPTPP)** include further removing barriers to foreign investment, reducing tariffs and subsidies for fair competition, and relaxing data security regulations for foreign investment flexibility




Notes: 1) Bank for International Settlement
Source: China Government Websites, CITIC Securities reports, A&M analysis

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Enduring trends...

China is still your APPEALING STORY	China is still playing a vital role in GLOBAL VALUE CHAIN	China is evolving into a GREAT GLOBAL LEARNING GROUND
		
Vast consumer market, rapid urbanization, government support, and a significant P&L contribution	Global value chain still highly relies on China's supply chain, technology and raw materials, particularly under government's promotion of "new quality productive force"	The Chinese market has a huge consumer base, and the intense competition is a test field and playing field for innovative ideas and business models

Emerging shifts

China will experience SLOW BUT QUALITY GROWTH	China is undergoing STRUCTURAL CHANGES	Globally GEOPOLITICAL TENSIONS are on the rise
		
As China's economic size grows, economic growth will inevitably slow down, as reflected by the Japan and Korea's growth pattern	China is undergoing structural changes marked by a transformation from Quantity to Quality growth, which will reshape the business environment for MNCs	US-China decoupling, Taiwan tensions, Russia-Ukraine war, Israel-Hamas war, energy crisis, China's unique positioning in a multi-polar world

MNCs must carefully assess three key dimensions in their China strategy

- Emerging dimensions
- Established dimensions

Transnational Benefit / Risk



- **Geopolitical and Economical tensions:** Trade restriction, tariff and cross-border capital flows across sectors
- **Consumer behavior:** The rising importance of reciprocal perception and corresponding behavior between China and foreign consumers toward each other's products
- **Technology transfer / data privacy:** Restrictions on core tech collaborations, cybersecurity and data transfers
- **Cross-border capital outflows:** Challenges in capital exchange affecting MNC financing

Sector Attractiveness and Dynamics







- **Regulatory environment:** Government regulations on foreign ownership, technical standards, supply / demand dynamics, and investment restrictions
- **Sector attractiveness:** Diverse sector behaviors in market size, growth levers, Chinese ecosystem and competitiveness
- **Unique “rule of games”:** China's distinctive success factors, business culture, and regulatory environment compared to other countries

Company's Ability to Win / Ability to Contribute



- **Strategic position:** MNC strategic positioning based on market share, margins, brand leadership, competitiveness, and financial strength
- **Local empowerment:** HQ empowers local offices with a China-centric operating and governance model
- **Resilience and active risk management:** Ability to adapt to challenges and prepare for uncertainties
- **Corporate citizenship:** Contribution to the Chinese government's agenda through taxes, job creation, R&D, and ESG initiatives

Depending on their positioning within these dimensions, MNCs have four strategic options for managing their China operations

STRATEGIC OPTIONS BASED ON BRAND AND BUSINESS LINE ANALYSIS				
	1 Localize to thrive 	2 Carve out to compete 	3 Diversify from China 	4 Exit China 
Transnational Benefit / Risk	Low risk / More favorable	Medium risk/less favorable	High risk / least favorable	High risk / least favorable
Sector Attractiveness and Dynamics	Highly attractive with minimal regulatory/market constraints	Moderately attractive with some regulatory/market constraints	Moderately attractive with some regulatory/market constraints	Least attractive with unique regulatory and market constraints
Company's Ability to Win / Ability to Contribute	High	High	Medium	Low
SCENARIOS	<ul style="list-style-type: none"> Compete in an open sector Integrate China and global operations for research, production, and market access 	<ul style="list-style-type: none"> China is a significant business contributor, but mindful of its unique characteristics and regulatory challenges Prioritize "China for China" as a key success factor 	<ul style="list-style-type: none"> Demonstrate industry capability in selected segments Maintain control over the Chinese market while mitigating risks 	<ul style="list-style-type: none"> Regulatory barriers discourage foreign investment Domestic competition intensifies, impacting competitive advantage Limited HQ management capacity and reach
STRATEGIC IMPLICATIONS AND PATHS	<ul style="list-style-type: none"> Act Locally: Scale to become leader through organic growth, JVs, and tech investments; Establish full China P&L Benefit Global: Leverage China experience for global market benefits 	<ul style="list-style-type: none"> Carve-out part / all the operations and preserve business value Sufficient autonomy to think, act and compete like local companies 	<ul style="list-style-type: none"> Refocus business as a niche player with a meaningful China presence Reduce capital risk through JVs with local partners; Consider HKEX/China-A listings De-risk supply chain with a "China+1" strategy 	<ul style="list-style-type: none"> Consider majority stake sale to domestic firms or private equity Closure of China operations

China has been the MNC story over the past two decades. Now is the time to rethink holistically about **navigating a profound shift** in Chinese business landscape

Assess your starting line

Analyse your strategic position, opportunities and risk exposure in China, considering dynamic shifts in your sector in real time

Refine your ambition and approaches

Redefine China's role in your global strategy and align your goals, capabilities, and operations with current realities

Plan and execute the implementation

Take a future-focused lens to sequence proactive measures and invest for long-term growth



Who to reach out to



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