
China

country brief

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Key economic indicators

Economic Indicator	China
Population	1.32 billion (2007)
Nominal GDP	US\$3,429 billion (2007)
GDP Growth Rate	11.5% (2007)
GDP Per Capita	US\$2,460 (2007)
Inflation	4.5% (2007)
Total Imports	US\$956.26 billion (2007)
Total Exports	US\$1,218.16 billion (2007)
Currency	1 RMB/yuan = 10 jiao; NZ\$1 = RMB 5.73

Source: IMF, World Trade Atlas

Overview

Dramatic economic progress and relative political stability have marked China's history in the last 20 years. Economic reforms and the opening up of China to the outside world have unleashed forces that have transformed Chinese society. This has resulted in many more opportunities for Chinese to realise their potential, and to participate in, and benefit from, the rapidly developing economy. For foreigners the transformation provides unprecedented business opportunities.

Since the late 1970s, the Chinese leadership has attempted to move China away from its sluggish, Soviet style, centrally planned economy towards a more productive and flexible economy with market elements, while still remaining within a framework of communist control. Despite undoubted progress, the leadership has regularly encountered the worst effects of both socialism (bureaucracy, lassitude, corruption) and capitalism (windfall gains and increased inflation). Beijing, therefore, has periodically had to backtrack on the reform process, tightening central control.

As the State has moved out of the 'cradle to grave' social care system that had been provided via state owned companies, the Chinese population has been required to pay for an increased proportion of the costs of housing, education, medical care and pensions. In the late 1990s, this led to a slowdown in consumer spending as people started to save, resulting in two years of deflation. In the major cities housing and insurance markets are now emerging.

Particularly during the 1990s, economic restructuring resulted in major job losses in state owned enterprises (SOE's) as these organisations sought to become profitable in a true commercial sense and in the face of competition from foreign invested enterprises. In the late 1990s some 15 to 20 million workers were laid off, mostly in labour intensive industries. The same number is likely to be laid off over the next few years as the next round of economic restructuring and transformation proceeds. In truth, these layoffs are more about transferring people from SOEs to private companies or privatised SOEs, as the social dislocation and cost of having so many additional unemployed in the economy would be too great without this transition.

Entry into the World Trade Organization (WTO) has allowed greater volumes of imported foreign agricultural products into the main centres, predominantly around Shanghai, Beijing and Guangzhou. This continues to be a vexed issue for the Chinese leadership as it grapples with the need to revitalise its rural sectors and urbanise a large proportion of the rural population.

Already some 80 million people have left their place of registration to find work in the cities and more will likely follow unless economic development of the rural regions is achieved.

Social stability is, therefore, a major concern. Another key issue that could threaten the pace of economic growth is the deterioration of the environment. Years of mismanagement have led to air pollution, water pollution (75 percent of the water table is now polluted), water shortages and deforestation. It is estimated that at present environmental problems cost China 10 percent of its GDP. Healthcare is also a major cost, with 440,000 people in 2005 dying prematurely from respiratory conditions caused by air pollution.

Since it began its open door policy in 1978, foreign trade has become more important to China. China is now one of the world's largest trading nations and was the seventh country to achieve a US\$1 trillion economy. Low labour rates, an educated workforce and attractive investment policies have encouraged a large number of companies from other markets to move production to China, particularly Hong Kong and Taiwanese companies. The output of these enterprises now constitutes a large portion of China's total exports.

Although China's economy has quickly grown to become one of the largest in the world, a recent report by the World Bank indicates that the size of the Chinese economy has been overestimated by around 40 percent. This may have implications for companies looking to move into China, particularly into rural areas where the purchasing power is still relatively weak. However, using the purchasing power parity (PPP) method, the World Bank report still ranks China as the world's second largest economy, accounting for 9.7% of world GDP.¹

In examining the China market, it is important to break China down into regions and then within those regions break down the market to define those consumers that can afford to buy specific products or services. We are now witnessing a new generation of consumers emerging from China's years of economic hardship. They can be defined as young, well educated and familiar with non-Chinese cultures, with a high probability of becoming employees of multinationals or Chinese companies that are operating internationally. They are aware of the latest global consumption trends and have high purchasing power. They are looking for a new way of life – this manifests itself in the way they buy fashion, dine and in the digitally-connected lifestyles they lead. They are generally regarded as trendsetters and trend adopters in China. This growing middle class is typically located in the major cities on the Eastern seaboard of China and in particular in the following four cities - Beijing, Shanghai, Shenzhen and Guangzhou where GDP per person is now over US\$8,000. Business Week/Online at the end of 2007 estimated that China had 310,000 USD millionaire households (a 39% increase on 2005) and 180 USD100 million-plus millionaire households (a 74% increase on 2005).

Foreign investment

China is one of the world's largest recipient of foreign direct investment (FDI). According to the Economist Intelligence Unit, in 2006, FDI inflows totalled US\$78.1 billion, and the stock of FDI reached US\$699.5 billion. The major investors in China are Hong Kong, South Korea, Japan and the US, and most investment goes to the coastal provinces and provincial-level cities.

FDI inflows are forecast to remain high over the next few years, although the government is becoming more particular about the types of investments it approves. Higher priority is likely to be given to projects that promise a greater degree of technology transfer, or that can help promote sustainable, energy-efficient economic development. As one commentator noted

¹ World Bank International Comparison Programme (ICP). The PPP method corrects for differences in prices for the same goods across countries.

following the 17th Communist Party Conference in October 2007, "the door is still open for foreign investment in China, it's just that the red carpet has been rolled up".²

Demographics

Some major changes are expected to occur in China over the next decade, with the overall majority of the population being in the 40 years and above age group. In 2007, this age group accounted for 43 percent of the population, but by year 2017 this group will constitute approximately 52 percent of the population. In addition, China's population growth is forecast to slow significantly, growing at only 0.2 percent per annum until 2017, when it will reach 1.33 billion people. Consequently, the overall number of people of working age and the number of employed is likely to see minimal growth.

Education standards in China are improving rapidly, and it is projected that the proportion of the adult population with tertiary level qualifications will increase from eight percent in 2007 to 12 percent by 2017. A similar increase is also projected for those with technical and upper secondary qualifications. This improvement in education will impact on the urban population, which is forecast to grow by 10.5 million per annum over the next decade, when it will reach 53 percent of the total population (urban households will exceed the number of rural households in 2009). This will be accompanied by an increase in the proportion of the population in skilled and white collar occupations, which should in turn increase the productivity of the labour force and therefore the affluence of Chinese society.

Average household income is forecast to grow from RMB 27,610 in 2008 to RMB 41,732 in 2018, an annual growth rate of 4.2 percent. There are significant differences between urban and rural household incomes. On average, incomes of rural households are less than a third of those in rural households (RMB 12,955 vs. RMB 42,734), and this difference is forecast to remain the same over the next decade.

The increasing affluence of the middle class and above will lead to the growth of discretionary expenditure categories, with this income going to housing related activities and subsequently to transport, communications, education and recreation and health.

Source: Global Demographics Ltd (www.global-dem.com)

Political

China's Government has a communist constitution. Following almost 30 years of political unrest the Chinese Communist Party (CCP) established China's current system of government in 1949. The country remained virtually closed to the world until a few years before the death of Mao Tse Tung in 1976.

A new era began when US President Nixon made a historic visit to China in 1972, ending Beijing's isolation from the non-communist world. Diplomatic relations with New Zealand were established shortly after on 22 December 1972; the United States achieved this in 1979.

Since the late 1970s, a series of five-year plans have aimed to modernise agriculture, industry, science, technology and national defence while expanding the production of consumer goods, housing construction, energy and transport. Reform of the finance, taxation, foreign trade and investment sectors was begun in the 1980s and has been ongoing since then.

² Report on the 17th Communist Party Congress, APCO Worldwide, October 2007

In March 2008, the 11th National People's Congress (NPC) in Beijing elected China's new government leaders. President Hu Jintao and Premier Wen Jiabao were confirmed for a second term (both have visited New Zealand – Hu in 2003 and Wen in 2006)

Imports and exports

China's Top Ten Exports

China's major exports for years ended December (US\$ billions)

Product	2006	2007
Computers	93.06	93.50
Telephone equipment	11.81	78.65
TV Receivers, incl. video monitors & projectors	12.96	36.60
Parts for office machines	33.03	32.75
Electronic integrated circuits	21.56	23.95
Liquid Crystal Devices n.e.s; Lasers	13.82	20.62
Printing machinery	0.40	18.72
Jerseys, etc	12.86	16.04
Electric transformers	11.01	14.22
Suits; women's or girl's (not knitted or crocheted)	12.47	13.45
Total exports	969.32	1,218.16

Source – World Trade Atlas – based on Chinese Customs statistics

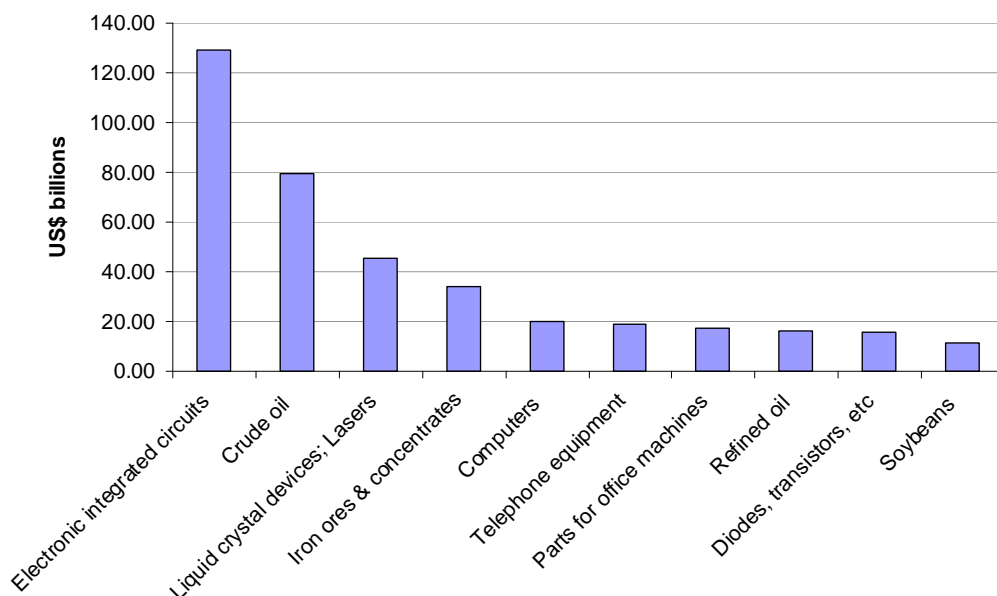
China's Top Ten Imports

China's top ten imports for year ended December (US\$ billions)

Product	2006	2007
Electronic integrated circuits	107.18	129.45
Crude oil	66.40	79.68
Liquid crystal devices; Lasers	35.90	45.19
Iron ores and concentrates	20.81	33.81
Computers	19.93	20.02
Telephone equipment	3.64	18.79
Parts for office machines	19.15	17.48
Refined oil	15.56	16.34
Diodes, transistors, etc	13.17	15.63
Soybeans	7.49	11.47
Total imports	791.79	956.26

Source – World Trade Atlas – based on Chinese Customs statistics

China's top 10 imports from the world, 2007



Recent Trends

China's imports tend to be capital plant and equipment, raw materials or semi-processed products for use by domestic industry for processing and re-export, and specialist products that Chinese companies cannot yet produce to the required standard. As the economy has developed and a middle class has emerged in the cities, demand for consumer products and food and beverages has grown. Though this demand has largely been met from domestic sources, there is a demand for imported products. The US Foreign Agricultural Service has estimated that there are currently 45 million people in China who can afford to buy imported foodstuffs. It is this group who can also afford other foreign services such as overseas holidays and education abroad for their children.

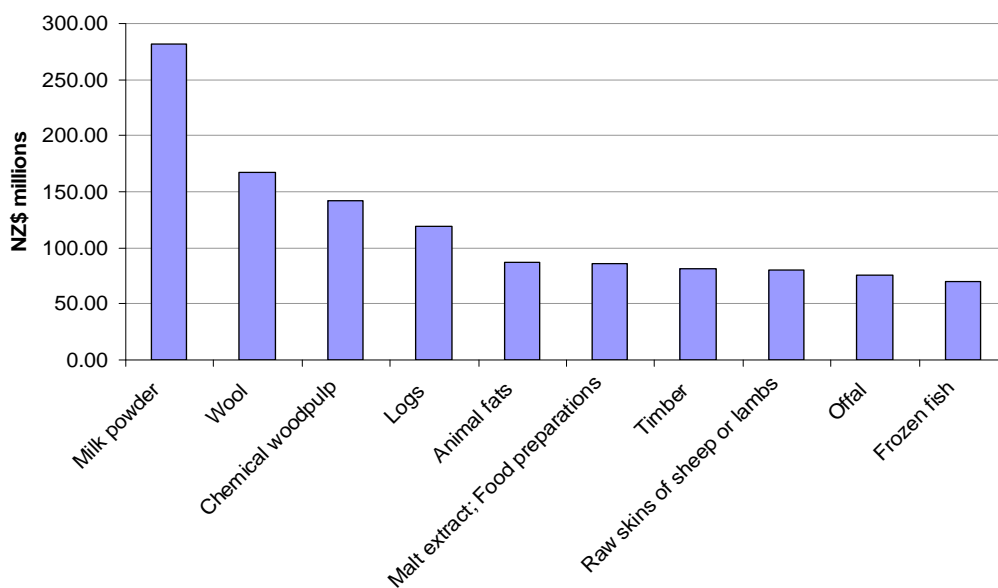
New Zealand's Top Ten Exports to China

New Zealand's top ten exports to China, for years ended December (NZ\$ millions)

Products	2006	2007
Milk powder	312.84	281.82
Wool	179.50	167.05
Chemical wood pulp	98.76	142.23
Logs	105.12	118.55
Animal fats	63.85	87.20
Malt extract, Food preparations	73.42	85.91
Timber	95.21	81.09
Raw skins of sheep or lambs	44.52	80.23
Offal	82.52	75.87
Frozen fish	73.05	70.27
Total exports	1,874.90	1,953.87

Source – World Trade Atlas – based on Statistics New Zealand statistics

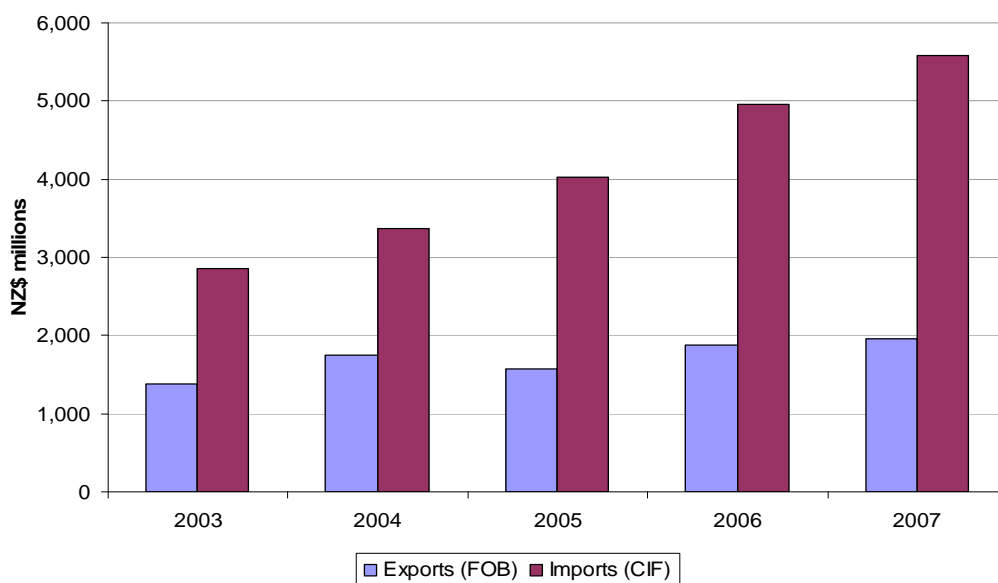
New Zealand's top 10 exports to China, 2007



Recent Trends

Exports have traditionally been primary sector products such as wool, dairy, meat, seafood and wood products. This is unlikely to change in the near future, though respective proportions may alter. A new trend has emerged whereby New Zealand high-tech products are starting to enter the Chinese market, often via third markets.

New Zealand's trade with China, 2003-2007



New Zealand exports to China have increased in recent years, and represented 5.3 percent of New Zealand's total exports in the year ended December 2007. China is the second largest

source of imports for New Zealand. Imports from China have increased substantially, growing to NZ\$5.6 billion in the year ended December 2007. This represented 13.3 percent of New Zealand's total imports for the period. China is now New Zealand's third largest trade partner, behind Australia and the United States. China is New Zealand's fifth most profitable export market.

Sector Opportunities

China offers significant business opportunities for New Zealand companies and New Zealand Trade and Enterprise (NZTE) is targeting the sectors where New Zealand companies may through product quality or differentiation have a value proposition that is commercially feasible in the China market. These sectors include;

Food and Beverages

Chinese consumers are looking for safe, quality products. As disposable incomes rise consumers can afford better quality products and are focused on wellbeing. They are increasingly looking for the healthiest, freshest quality foods, with food safety forming the ultimate and final buying decision. New Zealand's reputation as a clean and green environment, with an unblemished food safety record, means our products have an edge.

In addition, the Chinese are increasingly looking for value-added products and meal solutions in the quest for convenience. Wet markets and produce markets are losing their dominance as more consumers are drawn to hypermarkets and restaurants. This opens up significant opportunities for New Zealand's quality foods.

New Zealand already exports significant volumes of dairy products: mainly bulk milk powder but also cheese, butter and yoghurt. New Zealand also exports large volumes of meat, mainly low value lamb and offal; there are niche opportunities to supply higher value-added meat cuts to the retail and hotel, restaurant and institutional (HRI) sectors in major cities. Other finished products such as dairy products, fruits, wine, fruit juice and beer also have potential at the HRI level. Other opportunities exist for prepared foods targeting the retail sector. New Zealand exporters need to be aware of the need to support their products in-market with consistent marketing strategies and supply. As disposable incomes rise Chinese urban consumers can afford better quality products and there is both a growing demand for western food in major cities and a desire for more convenience type food solutions. The HRI sector also provides a key opportunity through the increasing number of international hotels catering to international guests and affluent Chinese.

Seafood

China is New Zealand's fifth largest export market for seafood. The market for seafood in China varies by region, the demand in the south being for high value live product while the north favours frozen product. Most high value product currently enters China through the south. The processing industry is primarily based in the north, where imports for processing and re-export enter China, with limited activity in other coastal centres in the east and south. There is domestic demand in the north-east for lower value New Zealand species (for example barracuda and jack mackerel). With the standard of living improving throughout China, the demand for high value frozen seafood and live seafood will continue to grow in line with expected economic growth. There are opportunities in the market to introduce new high value live species from New Zealand such as abalone, flat fish and fin fish. There are also new opportunities for high value processed fish products.

Nutraceuticals/Health Products

The one-child policy combined with an increasingly ageing population will ensure that the demand for healthcare and related products will continue to rise. Natural health products, like calcium-based, marine-derived and bee products, have undoubtedly good prospects in China, both in terms of supplying bulk ingredients for re-branding and for launching New Zealand-branded product into the retail sector. Stiff competition from United States, European and Australian suppliers can be expected in this sector. New Zealand companies will need to pay particular attention to the strict regulations that apply to nutraceuticals and related health products in China. In 2007, China was New Zealand's 5th largest health product market.

Food Processing Technology

While only about 30 percent of food in China is processed, compared to about 80 percent in most western nations, the market for processed food is growing, particularly in urban areas. According to the USDA the annual revenue from the food processing sector was US\$248 billion in 2005 (the latest available full year data), and the sector is estimated to be growing at 10-12 percent per annum.

International companies that have established food-processing facilities in China are constantly looking to expand or upgrade their existing production facilities to meet increased demand and international health standards. There may also be opportunities in this sector through targeting the more profitable local companies, particularly those gearing up to meet the demands of their export markets in Japan, the EU and the United States.

Wood Products

By the year 2010, it is projected China will demand 360 million cubic metres of wood with only half of this amount coming from domestic sources. While our exports to China have historically been dominated by log and lumber, there are also opportunities for New Zealand companies to add value to their offering to China. The building boom continues across many of China's main cities, opening up opportunities around interior fit outs and landscaping for both residential and commercial purposes.

New Zealand pine logs have traditionally been used in the construction industry, mainly for concrete forming, packaging and for the core of plywood. In recent years however, better quality New Zealand pine logs have been processed in China and the timber is being used in furniture and other value-added wood products for re-export and domestic market applications.

Traditionally New Zealand pine timber has been sold to China's growing furniture and finished goods industry with a high percentage of the finished product being re-exported to the United States, European and Australian markets. The anti-dumping tariffs imposed by the United States on solid wood Chinese furniture certainly had an impact on the furniture industry in China but in reality did not result in a decline in New Zealand pine timber sales to China. This was mainly due to Chinese furniture manufacturers turning more to the top end of the domestic market for increased sales as well as looking to diversify markets, for example to Europe, or to transfer manufacturing to a third country like Vietnam.

While China's furniture and finished goods industry will remain a key market for New Zealand pine timber, the rapid rise in China's fit out and construction markets offers opportunities for New Zealand pine timber to provide higher margin solutions to two fast growing sectors in China. There is also a growing demand for treated timber, especially for landscaping.

Agri-technology

China's budding dairy industry has been identified as one of the largest future markets of opportunity. New Zealand's style of dairy farming lends itself to the Chinese situation, particularly in southern China, with farmers seeking on-farm techniques to help develop their farming models and improve animal health. As a world-leader in agricultural technologies, New Zealand is ideally placed to provide dairy production and processing technologies and to become a long-term business and investment partner in the development of China's dairy industry.

Education

China has been a market for the New Zealand education sector since 1999 when all quotas were removed. China is the number 1 source of international students in New Zealand (approximately 40,000 in 2007 or 40%). The China market's characteristics - ageing population, one child policy, and no welfare support meaning that children are viewed as the sole providers of security for the parents and grandparents alike - results in a narrow focus on English language study, flowing through to tertiary studies, mostly in either management/commerce, or IT.

Most interest from Chinese students is around undergraduate, postgraduate and vocational study. New Zealand providers, especially tertiary institutions, are increasingly being asked to deliver programmes in China.

Institutions may consider the strategic investment of time and resources into the building education relationships with Chinese counterparts for the long term, with the aim of developing steady business opportunities and cooperation.

E-business³

The internet population in China reached 143 million in 2007, and is forecast to grow to 183 million by 2010. Internet usage is currently concentrated in the wealthy eastern provinces, and the number of internet users is still only around 10 percent of the total population (compared to around 66 percent in New Zealand). The number of broadband connections has increased rapidly in recent years, from 46 million in 2005 to more than 95 million in 2007.

In 2007 total IT spending was worth US\$46 billion, of which 76 percent was spending on IT hardware, 16 percent was spending on IT services and the remainder was sales of packaged software. Total IT spending is forecast to grow by 11 percent up until 2010, and the fastest growing segment is forecast to be spending on IT services, with a forecast annual growth of 17 percent.

The number of mobile subscribers has grown rapidly from 145 million in 2001 to more than 493 million in 2007. The growth in subscribers is forecast to continue, although at a slower pace, reaching 588 million by 2010. Statistics from the Ministry of Information Industry show that Chinese cell phone users sent more than 592 billion text messages in 2007, with a daily volume of more than 1.6 billion.

Environmental Technology

The environment is the number one concern for many local Governments in China. Initial focus is on treatment of waste water, sewage and solid waste but also on the growing noise and air pollution. Cities are being greened up with 'instant parks' appearing. The key requirement is to identify projects that match New Zealand capability and understand how these projects are financed. Many projects in this sector will require local partners. China has in the past received substantial loans (for example from the World Bank) aimed at correcting the degradation of

³ Statistics in this section are sourced from the Economist Intelligence Unit.

China's environment but despite this, huge problems remain, thus generating significant opportunities.

Manufacturing

For New Zealand companies, manufacturing in China is not merely about cutting costs, increasing profits and moving jobs overseas. It is about taking a strategic position to enhance competitiveness and value added opportunities by way of developing the company's international relationships. The reasons for considering manufacturing in China generally hinge around reducing manufacturing costs for some products, especially 'sunset' products or product lines in order to maintain competitiveness in existing market segments. In other cases, some companies have invested in manufacturing in China to supply their China based clients. Strategies can also be positioned around reducing component costs in existing or future product lines, while retaining R&D, design and other high end manufacturing in New Zealand.

For New Zealand companies, the initial emphasis should be on strategic engagement in manufacturing with Chinese partners, making the investment into people and structures, and determining involvement based on indirect as well as all direct costs. Companies will gradually need to develop language and cross-cultural skills in-house (or outsource), and to be looking at a staged process over time, not a 'great leap forward'. This is arguably less difficult for larger companies, but it is critical for small to medium enterprises (SME) to determine up front the benefits versus the costs.

Sustainability Issues

After several decades of intensive industrial development the impact on the environment has become increasingly evident. This has focussed attention on environmental sustainability issues leading up to the Beijing Olympics in 2008. The Chinese government has strengthened environmental laws and is taking steps to realise the opportunities for sustainable development. In 2002 China ratified the Kyoto Protocol but as China is regarded as a developing nation, it is not required to curb emissions but is eligible to earn credits by setting up emission reducing projects and other clean development mechanisms. China is also working with several western governments on initiatives to promote Corporate Social Reporting.

The government has introduced or revised 120 laws, rules and regulations since 2003 under the Programme of Action for Sustainable Development in China in the Early 21st Century. The new laws for the environment, health and safety are stringent but many companies do not comply with them and enforcement is difficult due to the many often conflicting standards established by the local governments of the provinces, regions and municipalities.⁴

Sustainability reporting for companies is still new in China. Eighteen companies published sustainability reports in 2006. External stakeholders including foreign investors have been pressuring companies to disclose their sustainability performance. Plans are underway by the China Securities Regulatory Commission (CSRC) and the State Environmental Protection Agency (SEPA) that would require listed companies to disclose their environmental protection activities. This would support reputation and brand benefits to those companies who publish a Corporate Sustainability Report.⁵

⁴ PriceWaterHouseCoopers. Sustainability issues in China. 2008

<http://www.pwc.com/extweb/service.nsf/docid/594B48D63C9E0E9D852570D8000999AC>

⁵ Miles, Katherine. Sustainability reporting: China's latest import. 13 November 2007

<http://www.chinasuccessstories.com/2007/11/13/sustainability-reporting-chinas-latest-import/>

China is building a sustainable new city, or eco-city called Dongtan which will occupy Chongming Island near Shanghai. It will be the first in the world and businesses and residents will start moving to the city in 2010. By 2050 the city is expected to have half a million residents. This project will be followed by three more eco-cities which will also be built around Shanghai.⁶

Amongst China's affluent population there is a growing demand for products that are environmentally friendly. A 2008 report by MasterCard shows that 48 percent of China's affluent consumers listed environmental considerations as an important factor in determining brand choice.⁷

Market Entry

China can seem daunting to New Zealand exporters and it is paramount that companies take time to research and understand the market before making any commitments.

Many New Zealand companies are successfully exporting to China or have an established presence in the market. One of the key elements of engaging in successful business with China is to understand the various distribution options available and know which option is best suited to your needs. The options are discussed below.

Trading Companies

For many years until changes in legislation in the late 1990s, foreign companies were not permitted to engage directly in trade and distribution within China. In recent years wholly foreign owned trading companies have been permitted.

In the majority of cases however, New Zealand exporters will still need to use domestic Chinese entities for the importation of product and possibly for sales and marketing within China. Previously, these companies were all state owned but in recent years, privately owned Chinese companies have also had this capability. It is critical to check the credentials of prospective Chinese partners, especially those that are undertaking the importation of product.

Some import/export trading companies also extend their business scope and represent New Zealand companies as their distributors. A number of New Zealand companies have developed good relationships with trading companies in China, many of which have a network of affiliated companies throughout China.

Local Agents

This mode of market entry has been popular in China as the economy and business opportunities have increased. Typically a local sales agent will handle internal distribution and marketing. Many of these companies do not have the necessary import licences and, therefore, form relationships with those companies that do, for example large trading companies. They may be representative offices of Hong Kong companies or domestic Chinese companies. It is often these large trading companies that local agents use in order to secure Letters of Credit to meet the payment terms of the New Zealand supplier.

⁶ Koroluk, Korky. China's unlikely green leadership. 22 February 2008
http://www.dcnonl.com/article/id26509&search_term=green%20leadership

⁷ MasterCard. Brand Preference of the China Affluent. First Quarter 2008
<http://www.masterintelligence.com/upload/188/122/ChinaBrandPref-S.pdf>

There are risks for international companies when they register products through their agents, specifically the risk that the foreign company will pay for the registration, but the agent will end up, either intentionally or by accident, owning the rights to the registration. If the relationship with the agent deteriorates, there is a chance that ownership of the licence will be used as a bargaining chip. It is recommended that legal advice is sought when registering brands or products in China.

There is no such thing as 'the China market'. China consists of many different markets broken down firstly by region, then by city, then by niche market. Each of these markets can be different in many ways and, in almost all cases, a New Zealand company will require separate agents for each region, a challenge in itself as different agents sell outside their approved territory.

Hong Kong as an Option

Importing and distributing out of Hong Kong is an option, although distribution into China and payment then become key issues. Hong Kong's current trading relationships relate more often to the trade within the Pearl River Delta, than to the whole of China.

Some New Zealand export companies make their sales to China from Hong Kong and leave the responsibility for getting the product across the border into China in the hands of the Chinese client. Payment in such cases would be made in Hong Kong in hard currency.

Another option is to run the sales operation out of Hong Kong but with product being shipped direct to China. It is important that the importer has the required rights to undertake such foreign exchange transactions and raise Letters of Credit, or that they have access to an import/export corporation (trading company) that can fund the transaction on their behalf.

Representative Office

Establishing a representative office (RO) in China has traditionally been a popular move for those New Zealand companies that have started to generate good sales into China. Traditionally the establishment of an RO was the fastest and most cost effective way to establish an on the ground presence in the market. It remains a viable option, however given recent changes in Chinese regulations New Zealand companies should also weigh up the option of establishing a Wholly Foreign Owned Enterprise (WFOE) consulting company, which in many cases may in fact be a more viable choice.

Activities an RO can and cannot engage in:

It can	It cannot
Undertake business liaison work and support local distributors/sales teams	Receive fees or generate income
Undertake market research	Manufacture or produce
Provide product recommendations	Issue commercial invoices
Provide technological exchange and training	Trade in RMB, or other currencies
Provide a relatively easy exit (compared with other options), although some companies are registering their company through Hong Kong companies as an easier exit model	Set up an office in just any building – usually it must be in an A grade building
Provide a format for a foreign company to place their international manager in China	

WFOE Consulting

WFOEs are now typically the investment vehicle of choice for foreign companies wishing to establish a presence in China – whether consulting or manufacturing. As mentioned above New

Zealand companies wishing to have a non-manufacturing presence in China should look at whether they would qualify to set up a WFOE consulting company.

Laws around the registration of a WFOE have changed recently, so companies should check with local lawyers or business development consultants to get updates on these changes.

Some of the advantages of a WFOE consulting company:

Advantages	Permitted Activities
Complete management control – no need for a Chinese partner	May formally carry on business in China
Far more tax efficient than an RO (pay tax on profits only vs. actual overheads for an RO)	May receive RMB and issue invoices
Use the initial registered capital as working capital – money that would have to have been allocated to set up an RO anyway	May convert RMB profits into US\$ for remittance offshore
Chinese legal entity status	
Protection of IP (more relevant for WFOE manufacturing companies)	

WFOE Manufacturing

WFOE manufacturing companies enjoy the same advantages and permitted activities as a WFOE consulting company. The minimum registered capital requirement for a WFOE manufacturing company is normally US\$200 000.

Establishing a Joint Venture/Strategic Alliance

A joint venture (JV) with one or more Chinese partner(s) or a WFOE is possibly the final step in developing the China market for New Zealand companies. The establishment of JV's are regaining popularity as a means of China market entry after having been discredited during the 90's.

There are typically two main reasons for establishing JVs or strategic alliances in China:

- To gain access to the domestic market which may be limited by high tariffs, quantitative restrictions, high production costs in New Zealand or lack of distribution.
- To take advantage of more competitive cost structures or availability of raw materials to export to third markets, and/or expand sales and distribution in the market.

A key consideration to include in a JV contract as part of the strategy is an exit clause. Make sure that you can exit, while remaining in a position where you can still develop business operations in China.

Licencing

Technology transfer and manufacturing under licence are other initial market entry approaches used by companies. Both options raise the issue of IP protection. However, one strategy often employed is to licence older technology first with the intention of giving access to newer technology at a future date should the relationship go smoothly. This approach is quite common in the telecommunications and high-tech industries. The licencing approach requires a significant commitment to research and putting systems in place to protect not only your IP but also quality and many other aspects.

Franchising

China's Ministry of Commerce issued new administrative measures covering business franchising on 1 February 2005. This regulation is in keeping with the requirements made by China at the time of its accession to WTO in 2001 to open its franchising market to foreigners. This market has been totally open to foreign investment since the end of 2005.

Franchising is now becoming a popular business model in China, employing about 20 million people. It may also become another entry option for New Zealand companies.

E-Business

The Chinese Government has adopted an open attitude towards the advent of e-business in China. There is already a considerable amount of interest from both Chinese and international companies in establishing online sales channels. There are still many issues to overcome, in particular the lack of clear regulatory guidelines addressing e-commerce in China, a secure and reliable online settlement system, an efficient delivery system, and so on.

Sites that have more detailed information on the various options are: www.dezshira.com, www.lehmanlaw.com. www.BJConsultingGroup.com.

Regulatory issues

The following is an outline of some of the regulatory issues New Zealand exporters need to be aware of.

Anti-Dumping

The Ministry of Commerce is responsible for investigating allegations of dumping, working together with the General Administration of Customs.

Currency Restrictions

The Chinese currency is the renminbi (RMB) or 'people's currency'. The RMB is a non-convertible currency so it cannot be readily exchanged outside China. Foreign exchange controls are administered by the State Administration of Foreign Exchange along with the banking sector. The exchange controls relate to foreign exchange transactions by foreign invested enterprises as well as by companies with import/export licences. Exchange controls also relate to remittances by foreigners working in China and to payments for services overseas (for example education).

Some financial institutions in Hong Kong and in other countries are providing Forex exchange services, but only for small amounts. They are not able to change large amounts for trading purposes.

Environmental

Though China has a range of environmental laws, enforcement is variable, especially if the social cost of not enforcing a law (especially in terms of local employment) is considered to outweigh the economic cost of enforcement.

At central government level in particular, there is a commitment to improving the environmental conditions in China. There are a range of problems with air pollution, soil pollution and water pollution from industry, deforestation, over-grazing of grasslands and overuse of chemicals in the rural sector.

Health Regulations

Imported foods, food additives, food vessels, food-packing materials, and tools and equipment for food cannot clear Customs without an 'Entry-Exit Inspection and Quarantine Certificate'. The Certificate is issued by the State Administration for Quality Supervision and Inspection and Quarantine (AQSIQ).

It is normal practice for samples to be taken from a consignment for health and quarantine testing. Products may be cleared physically but until they pass health and quarantine inspection (usually two to three days) they may not be distributed or used. All pre-packaged imported foods should have a 'Certificate of Examination and Verification of Imported and Exported Food Labels'.

Trademark protection

China is a member of the World Intellectual Property Organisation, the Paris Convention for the Protection of Intellectual Property, the Berne Convention (covering copyrights) and the Madrid Agreement (covering trademarks). As a WTO member, China is also signed up to the Trade-Related Intellectual Property Rights Agreement (TRIPS), which requires member states to provide strong protection for intellectual property rights

The laws and regulations around this are being constantly updated, especially following China's accession to the WTO, however enforcement and consistency of application throughout the country is still an issue that will take time to improve.

Patents in China are issued for 20 years for inventions, and 10 years for utility models and designs. Registered trademarks are valid for 10 years and are renewable for further 10-year periods. Foreign companies must register trademarks through one of the agencies designated by the State Administration for Industry and Commerce.

Generally it is important to get the trademark registered before the products are exported to or manufactured in China. China is a 'first to file' country, which means that rights in a trademark are only obtained by registering a mark at the local Trademark Office.

Within 12 to 18 months of filing the application for registration, the Trademark Office of the Administrative Department of Industry and Commerce will notify the agent as to whether the application has been rejected or accepted.

Accepted applications are published in the official journal, but are not registered until a three-month 'opposition period' has expired. During this period, anyone who believes the mark should not be registered may oppose an accepted mark. The Trademark Review and Adjudication Board can, for a fee, review the rejected applications. A third party can cancel a trademark registration if it is not used in China for a continuous period of more than three years.

The New Zealand company Baldwins has produced a guide to brand protection in China (*Baldwin's Newsletter*, September 2005), covering issues to consider for releasing a product in the Chinese market.

See the E-Library on the Baldwins website: www.baldwins.com. Other sites to visit are: www.lehmanlaw.com and www.iprights.com.

Import Quotas and Licenses

To trade with China, foreign companies need to deal with a Chinese entity that has import/export rights. These companies have grown from a few dozen Ministry level import/export corporations 20 years ago, to many thousands today. Many of these are JV or foreign invested enterprises that have limited rights to export their own products and to import raw materials for their own use. Under the WTO there will be a further easing of the regulations of who can do international business.

China maintains tariff quotas on a limited number of commodities, wool being the only one that affects New Zealand.

Marking and Barcodes

Information regarding marking and barcodes is available from NZTE on request.

Packing and Labelling

Imported food and beverage products to be marketed in China must have Chinese language labelling or it can be refused entry. Labels can be dual-language but the Chinese lettering must not be smaller than the lettering in the other language. The regulations state that the standard label must contain:

- the name of the food
- list of ingredients
- net contents and drained weight
- name and address of manufacturer and distributor
- date marking and storage instructions
- quality grade
- code of the product standard
- specific labelling.

AQSIQ is in charge of administration of the labelling of pre-packaged imported and exported food. It is also responsible for the examination and verification, approval and issue of certificates for food labels. Inspection and quarantine organisations appointed by the State Administration for Entry-Exit Inspection and Quarantine (SAEIQ) receive applications for examination and inspection of food labels and organise preliminary inspections.

Businesses importing or exporting pre-packaged food, or their agents, must submit a food label for examination by an appointed (provincial or municipal) inspection and quarantine authority on entry, but close discussion with the importer/distributor is recommended in advance to make sure all necessary documentation is ready and procedures followed.

State Regulations

Though China is moving more and more towards a market economy, it is still quite heavily regulated, and a number of government organisations are involved in regulating trade. Some of the main ones appear below.

- The Ministry of Commerce, formed from the merger of the Ministry of Foreign Trade and Economic Cooperation and the State Economic and Trade Commission, is now responsible for all of China's foreign economic relations, foreign trade, formulating industrial policy and monitoring economic development.

- The Ministry of Finance oversees China's financial activities.
- The State Administration of Foreign Exchange regulates foreign exchange control.
- The State Tax Bureau supervises and administers all tax matters.
- The State Administration of Industry and Commerce is responsible for the registration of all businesses and for issuing business licences.
- The Bank of China is China's main foreign exchange bank and handles all international transactions.

Tariffs and Duties

The customs law of China is complex because the Government has used tariff concessions to stimulate investment in certain sectors of the economy, for example duty and VAT exemptions are regularly granted to foreign invested enterprises. Following China's accession to the WTO in December 2001 a wide range of tariff reductions were made on 1 January 2002. A number of items have continued to be reduced further on 1 January each year for the past few years.

China operates an eight-figure two-column tariff with import duties being assessed on normal Cost including Insurance and Freight (CIF) values. The preferential import duty rate applies to all countries with which China has diplomatic relations (including New Zealand), while the general rate applies in other cases.

VAT affects all goods other than exports, and operates in a very similar way to New Zealand GST. The general VAT rate is 17 percent. VAT applies to both imports and local trade, and tidies up a previous raft of product and production taxes. VAT for imported products is calculated on the duty paid CIF value.

On top of VAT, a consumption tax is imposed on 11 kinds of consumer goods including tobacco, alcohol, cosmetics, skincare and haircare products, precious jewellery, precious jade and stones, firecrackers and fireworks, gasoline, diesel oil, motor vehicle tyres, motorcycles and motor cars. The purpose of the consumption tax is to guide the direction of consumption and ensure fiscal revenue.

NZTE can provide free basic information on tariffs at an indicative level to assist companies in assessing viability of market entry.

Taxation

China has a complex taxation system. Individual income tax is paid by foreign individuals and Chinese nationals. This is normally deducted by the employer and paid monthly to the local tax bureau.

Company tax is administered by the local branch of the State Tax Bureau and covers both company tax and VAT. The level of taxation depends upon the type of enterprise, and the situation is made further complex by various tax concessions designed to encourage investment in particular regions or sectors. But in general, corporate tax is levied at 25%.

Freight

Air Freight:

In November 2006, Air New Zealand introduced direct flights from Auckland to Shanghai, starting out at three days per week (for updates on this visit: www.airnz.co.nz). From July 2008 it will also

have direct flights from Auckland to Beijing twice a week. In addition Air New Zealand started a freight service between Auckland and Shanghai via Melbourne in 2005. Alternatively the following list details countries and areas through which transition on to direct flights can be made.

- Beijing from - Australia/Hong Kong/Japan/South Korea/Malaysia/Thailand/Singapore
- Shanghai from - Australia/Hong Kong/Japan/South Korea/Singapore/Thailand
- Guangzhou from - Australia/Hong Kong/Indonesia/Malaysia/Philippines/Singapore/Thailand

Air New Zealand and Cathay Pacific offer direct flights between New Zealand and Hong Kong.

Air China, China Eastern and China Southern operate from Australia to different parts of China.

Sea Freight:

COSCO (New Zealand) Ltd offers weekly sailings through Japan from Auckland, Lyttleton and Napier to Hong Kong, Shanghai, Xingang (Tianjin/Beijing), Dalian, Qingdao and Huangpu (Guangzhou). Other shipping lines provide transit services to China through most Australian and South East Asian ports. Approximately one month is required for shipments between New Zealand and China.

NZTE has basic information on air and shipping freight options to this market, but for details on rates and schedules, exporters will be referred to a range of appropriate service providers.

Tips on business culture

- Creating a favourable impression in China depends largely on exhibiting common courtesy, respect and a degree of modesty. There are no religious taboos for foreigners to be concerned about, although there are political sensitivities.
- Chinese respond well to New Zealanders; they see us as open, frank, modest and non-threatening. In terms of country stereotypes we rate well. This may be on account of our relative informality, and the fact that we come from a small country that has undertaken its own economic reform process. We are perceived to be empathetic and respectful of China and its modern day achievements.
- Building up a good relationship is important to conducting business in China. Known as 'guanxi', personal relationships and connections permeate the business and bureaucratic arenas, forming an invisible network which often provides the most expedient way of getting things done. Using one's guanxi to understand the informal systems beneath the formal rules may help one interpret policy.
- Trust has to be established. Chinese people traditionally do business on the basis of mutual trust, rather than on the basis of written contracts. In this environment you will need to gain the trust of the key people among those you meet. You will need to be perceived as being worthy of this trust. You will also need to develop an accurate opinion on whether you can trust your counterparts.
- Business attire should be conservative. Dark coloured or grey suits, conventional ties, white or blue shirts and black shoes are most acceptable for business meetings. But also be aware to dress for the conditions, heat in summer and cold in winter. There is not as much heating in Eastern and Southern China in winter, while in the north they tend to overheat rooms in winter.

- Asians and Chinese have a particular regard for those older than them. An extra show of courtesy and visible acknowledgement of the presence of an older person will reflect well on you.
- Chinese do not like to 'lose face' and in this context it is important to avoid embarrassing individuals in front of others.
- A little bit of Mandarin goes a long way. Make the effort to learn a few words of Mandarin before your trip. Surnames are placed first in Chinese. Mr Chen Jia Qi is therefore addressed as 'Mr Chen'. Check with your host to determine how they wish to be addressed.
- A handshake is the normal greeting for men and women irrespective of age or seniority. When meeting genuine old friends, a handshake clasped in both hands may be used.
- Business cards are an absolute must in China. Printing your name in Chinese on the reverse side is a worthwhile exercise if done correctly. Designations are also important. Chinese prefer to do business with senior managers and above. Business cards should be received and presented with both hands. It is also a sign of respect to keep hold of the card, not put it away immediately in your pocket or holder. This practise is strongly observed by older people but less so by younger people. Never throw or flick a business card across a table. When greeting a number of people you may shake hands and present a card to each individual in turn or shake hands with the group first, then present cards to each person. In very senior meetings, for example with a Minister or Vice Premier it is inappropriate to hand out cards. However, you may leave one at the end of the meeting with one of the officials.
- When entering a room or meeting a group of people, the most senior Chinese person will be the first to greet you, followed by others in approximate descending order of seniority. You should follow suite if there are several people in your group. However, if one member of your group is well known to them (regardless of seniority) they should escort the senior representative in and introduce the remainder of the group. The interpreter will also help introduce the group.
- A great deal of business in China, as in the rest of Asia, is conducted after hours. Two kinds of entertainment dominate – dinners and karaoke – often with both on the same evening.
- Meeting rooms for formal meetings are generally laid out in a horseshoe shape, with the most senior representative seated beside interpreters at the top with others ranging down each side of the room in approximate order of seniority. As with 'greetings' if members of the group are known to the Chinese, they should take a position near the leader to assist with discussions. Chinese tea is usually served. It will not cause offence if you do not drink; however if your host motions for you to try it, then you should do so. If the meeting is held around a conference table then the leader should take up a position in the centre directly opposite the main host. In formal or senior meetings, it is common for the two leaders and perhaps one or two others to speak with the remainder being spectators. It is appropriate for the leader to call on other members of the team to make specific comment or provide an answer.
- Traditional Chinese banquets are usually 10-12 courses and last about an hour and a half. At senior level or formal banquets, food is served for guests by staff. In less formal situations, plates are put on a 'lazy Susan' and guests help themselves, however it is common for the host to serve small quantities of food (especially from the first course) onto the plates of guests. This is usually done with chopsticks. It is preferable to use a communal chopsticks or a serving spoon to transfer food onto your plate. You should try to taste all the dishes served. If there is something you don't like, just leave it (if the courses are being served it will be removed by the waitress) or place it to one side of your plate. If your host insists that you try something, you should do so, but the remainder can be left on the side of your plate. If you finish your bowl it is usually taken as a sign that you would like a second helping. The Chinese are intensely proud of their food and it will cause offence to turn

something down completely. If you have a strong aversion to something or an allergy then you should explain this and it will be accepted.

- Dinner speeches and toasts are standard. At the beginning of a formal banquet, a brief speech and a toast of introduction will be made by the host. Following this the main guest should reply with a brief speech and a toast. Throughout the meal it is customary for toasts to be made on both sides. Whoever proposes a toast is responsible for setting the pace on how much is to be drunk: a sip, half glass, or 'bottoms up'. Others will watch that person's lead. In more formal situations it is usual to sip and it would be impolite to challenge a host to 'bottoms up'. It is usual to clink glasses with those immediately beside you, but not obligatory for each toast. When toasting, connecting the rim of your glass below the rim of your guest's glass will again pay them respect. At the end of the meal (once the fresh fruit dish has been eaten) it is customary for the main guest to thank the host on behalf of the group. The host will then respond. To signal the end of the banquet, the host will rise and thank the guest. This is a signal for everyone to rise. The Chinese like to have a clear beginning and end, not have things drag on. For a banquet to be over in an hour to two hours is common.
- Gift giving is standard. Gifts may be small and inexpensive. New Zealand natural products (greenstone or woodcarvings) are most appropriate. If the meeting is at a banquet, gifts should be given at the end. It is common for Chinese to not open the gift in front of you, however they may do so if you indicate that you would like them to or wish to explain something about the gift. It is unnecessary to present the whole group with gifts, rather present gifts to the senior person only or maybe one or two others. If you wish to present a junior person or interpreter with a gift this should be done privately rather than in front of the senior person.

Visa requirements

We recommend travelling to China on a business visa. In most cases exporters will require a letter of invitation from a Chinese company. For more information, contact the Chinese Embassy in Wellington or the Chinese Consulate in Auckland.

Consular Section, Embassy of the People's Republic of China

Address: 2-6 Glenmore Street, Wellington or
PO Box 17257, Karori, Wellington, New Zealand
Tel: 04-472 1382-600 or 474 9649
Fax: 04-474 9632
Email: visa@chinaembassy.org.nz (visa, passport)

Consulate General of the People's Republic of China in Auckland

Address: 588 Great South Road, Greenlane, Auckland, New Zealand or
PO Box 17123, Greenlane, Auckland, New Zealand
Tel: 09-525 1785
Fax: 09-525 0733
Website: www.chinaconsulate.org.nz

Visa application forms can also be obtained from the Chinese Embassy's website www.chinaembassy.org.nz/eng

Time difference

China is four hours behind New Zealand except during daylight saving (October-April) when it is five hours behind. For the current time in China visit: www.timeanddate.com. There are no separate time zones in China.

Contacts

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New Zealand Trade and Enterprise Shanghai

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New Zealand Trade and Enterprise Guangzhou

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Phone	+86 20 8667 0253
Fax	+86 20 8666 6420
Email	info@nzte.govt.nz

useful websites

- www.ccpit.org
This is the website for the China Council for the Promotion of International Trade. It contains a lot of information about doing business in China, regulations, tariffs and a useful listing of trade fairs in a number of cities.
- www.chinadaily.com.cn
This is the website of the major English-language newspaper in China
- www.fdi.gov.cn
Invest in China – This is the website of the Investment Promotion Agency of the Chinese Ministry of Commerce.
- www.aqsiq.gov.cn
General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China
- www.customs.gov.cn
China Customs

Doing Business in China

- www.china-briefing.com
- www.dezshira.com
- www.tdctrade.com/chinaguide/index_e.htm
- www.mahonchina.com
- www.baldwins.com
- www.lehmanlaw.com
- www.iprights.com

FDI Statistics, Regulations, Projects etc

- www.sinoprojects.com/english/index.htm

Global Demographics

- www.global-dem.com

New Zealand China Trade Association

- www.nzcta.co.nz

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