
Exporter Guide

ICT MARKET IN CHINA

Market Profile
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1 MARKET STRUCTURE

1.1 Market overviewⁱ

The information and communications technology (ICT) industry in China is large and complex, covering a wide range of products. The overall industry and its sub-sectors are enormous in size and China is universally considered the manufacturing hub for most of the world's electronics. China is currently the world's fourth largest information technology (IT) market by spend after the United States, Japan and Germany.

Software

The Chinese software industry has undergone rapid development in the past 10 years. The revenue of the software industry in 2010 reached US\$11.1 billion, representing a compound annual growth rate (CAGR) of 14 percent for the period spanning 2007-2010. The total value of the Chinese software market is forecast to reach US\$12.9 billion in 2011. As of August 2010, China had 18,843 software enterprises and 67,912 software copyright registrations were handled in China in 2009.

The local market still lacks core technologies to develop, high-end software development talent and consistent high-quality software products. However this is beginning to change as local software developers start to bridge the gap by partnering and licencing foreign technology. This current situation may provide market opportunities for New Zealand's high-end software technologies and products in certain fields.

The China market has good prospects for customised software products from New Zealand such as software for cinemas, fleet management, healthcare, petrol stations, mobile marketing, agriculture and dairy applications. However, the retail market in China is also fraught with difficulties and unlikely to provide viable opportunities for many New Zealand software companies.

Hardware

According to BMI, the computer hardware industry revenue grew by 18.7 percent in 2010 to US\$62.9 billion, representing a compound annual growth rate (CAGR) of 13.4 percent for the period spanning 2007-2010. The roll-out of 3G mobile services by telecommunications network operators stimulated notebook sales. Recent government subsidy programs boosted demand for PC's in the rural parts of China. According to government figures, around 414,000 computers have been sold under the programme. As the market matures, hardware's share of the IT market is expected to decline to 65 percent due to the expected increase in IT services and software. China is the second



biggest PC market in the world and with low penetration in rural areas, the indication is that there will be strong growth prospects going forward.

ICT production output 2009

Hardware products	Production volumes (Millions)	Share of global production
Mobile phones	619	49.9%
Computers	182	60.9%
Televisions	100	48.3%

The main manufacturing areas for ICT hardware products are the Pearl River Delta in South China, the Yangzi River Delta in East China and the Bohai Bay Region in North China.

Telecommunications

The telecommunications market was restructured in May 2008 in order to make the market more competitive for the upcoming release of 3G technology. The market is large and consists of three main telecom service providers:

- China Mobile
- China Telecom
- China Unicom

The current telecommunications market is dominated by local companies. However, in line with China's obligations due to WTO accession, sizeable foreign investment has come into China. China Mobile, through its subsidiary ChinaNet, has over 50 percent of the broadband market.

As of June 2010, China had 420 million internet users, 277 million mobile internet users and 115 million broadband subscribers. China had approximately 823 million mobile phone subscribers as of 2009, consisting of 795 million 2G and 28 million 3G subscribers. Despite being dwarfed by 2G, the 3G service has been growing rapidly since its introduction in January 2009ⁱⁱ.

In 2007, foreign companies were permitted to enter into joint ventures with Chinese telecommunications companies. They are able to hold up to 49 percent of the company shares in mobile and/or fixed line services and a 50 percent stake in value added services. Areas such as data communication are relatively more deregulated than other areas such as fixed line services.



1.2 Market drivers

Economic growth

China achieved real GDP growth of 9.1 percent in 2009. China's has maintained consistent GDP growth above 8 percent throughout the last decade. As China grows quickly, demand for telecommunication services is predicted to expand over the coming years. Demand for IT products will come from major infrastructure projects, government, telecommunications, finance, energy, education and healthcare projects.

Government policy

The Chinese government has placed great emphasis on developing the high technology sector. Government measures include providing policy incentives, establishing high-tech zones and providing development funding. Enterprises that obtain national "High-tech Enterprise Status" are entitled to a preferential Enterprise Income Tax (EIT) rate of 15 percent, which is substantially lower than China's ordinary 25 percent company tax rate. High-tech Enterprise Status (HES) is awarded by the Chinese authorities to companies that consistently invest in the research and development of new technology and products or own proprietary intellectual property rights in some key areas supported by the Chinese government.

The government has focused on developing basic software industry capability, the development of integrated systems, large scale application software and on the development of next-generation internet projects. It has also announced plans to undertake many high-technology projects in the next few years:

- IC chip upgrade 909 project.
- LTE-4G development.
- Next-generation IPv6.
- Broadband upgrade.
- Biedou-2 satellite project.

New technology projects are expected to contribute around 60 percent towards the country's economic growth. In June 2008, the State Council formally inaugurated the new Ministry of Industry and Information Technology (MIIT) which now oversees the IT sector. The MIIT is responsible for approving and promoting industry standards, pushing



technology innovation, guiding the development of information infrastructure and ensuring China's information security.

Internationalisation

The Chinese market has become more open since China joined the (World Trade Organisation) WTO. This has resulted in many local ICT companies facing severe competition from overseas firms. In response to this, some Chinese firms have begun to become global in size and focus; good examples of successful Chinese companies operating internationally include Lenovo, Huawei, ZTE and Haier. For example, the overseas market accounted for more than half of Huawei's total sales in 2009.

To be competitive, local companies have had to equip themselves with international standards systems. According to IDC's research, as a result of this increasing interest in international business, China will see great demand for IT consulting, enterprise management solutions, information storage, network security products and wireless application solutions.

1.5 Major players

Competition in the ICT space is fierce due to its large scale and large number of international firms present in the market. There are already many large foreign multinational corporations (MNC's) like Microsoft, HP, IBM and Oracle in the market. In addition to MNC's, domestic Chinese competition has increased and includes such firms as Huawei and ZTE in the area of telecommunication network infrastructure, Haier in electronics, Lenovo in personal computers and Neusoft in IT services.

Based on the above situation, it is important for New Zealand companies to position themselves carefully and strategically in the Chinese market. Most of the New Zealand ICT products and technologies are aimed at the middle and high-end market in China, which is also the target market for the MNC's. To be competitive in this market, many factors need to be considered including price points, manufacturing in China in order to lower costs, distribution channels and after-sales service and support.

The top 10 electronics and IT companies in 2009 are listed in the following table and are ranked according to combined measures of revenue, profit and research and development.



List of China's top 10 electronics and IT enterprises 2010ⁱⁱⁱ

Rank	Company	Website
1	Huawei	www.huawei.com
2	Haier	www.haier.com/index.asp
3	Legend Holdings	www.legendholdings.com.cn/
4	ZTE	www.zte.com.cn/en
5	Hisense	www.hisense.com/en
6	Founder	www.founder.com/en
7	TCL	www.tcl.com/main_en
8	BYD	www.byd.com.cn
9	Changhong	www.changhong.com
10	Great Wall Technology	www.greatwalltech.com/english.asp

1.6 Regulatory

Duties and tariffs

Since China joined the WTO, tariffs for imported ICT products have been gradually lowered and in some cases totally phased out. According to the “Customs Import and Export Tariff of the People’s Republic of China” the tariff for ICT related hardware products ranges from 0 to 35 percent. Among this range, most of the telecommunication equipment and computing products, parts and accessories are assessed at 0 percent. Value Added Tax (VAT) is currently 17 percent.

The standard company tax rate is 25 percent. Special rates apply to small scale enterprises, 20 percent and state encouraged new high tech-technology enterprises, 15 percent. From 2000 to 2010, the Chinese government has been implementing the following preferential tax policies for software enterprises:

- A regular VAT payer who develops and sells software products on its own is eligible for a VAT refund after the software products are registered in China. This reduces the effective VAT for a software company from 17 percent to 3 percent.
- After a newly-established software production enterprise is certified in China, Enterprise Income Tax (EIT) is exempted in the first and second profitable year and then reduced by half from the third to fifth year.
- Key software enterprises certified by the Chinese central government are eligible for a lower EIT rate at 10 percent, if they are not eligible for EIT exemption in that year. In 2009, Chinese central government certified 186 key software enterprises.
- Equipment imported by software production enterprises for self-use and supporting technology (including software), parts and spares imported with the equipment shall be exempted from import tariffs and import-related VAT.



The Chinese government is expected to launch new preferential tax policies for software enterprises by the end of 2010.

The registration of software products and certification of software enterprises in China are handled by China Software Industry Association (CSIA) and provincial software industry associations. For contacts details of the software industry associations in China, please contact New Zealand Trade and Enterprise (NZTE) or refer to the following Chinese website: www.chinasoftware.com.cn/transact_organ.asp.

Standards and regulations

- **Software:**

All registration of imported software products (including localised imported software products) is required to be processed by the CSIA. Following its examination/approval and subsequent approval by the MIIT, software product registration numbers and software product registration certificates are issued. Some specialised software for use in network security also needs approval from the Public Security Bureau.

- **Telecommunications:**

MIIT requires that all telecom equipment including terminal devices such as cell phones, phones, fax machines and network products such as switches and base station equipment be tested and certified. There are two kinds of certificates for telecommunication products:

a) Type of Approval (TA) for radio products.

b) Telecom equipment network access license for all other products.

In order to obtain TA certificates, radio products need to be tested by testing agencies designated by MIIT's Radio Regulatory Department. Network access licenses for telecom equipment are issued by MIIT's Telecom Administration Bureau.

- **Other ICT Products:**

China applies different requirements for other ICT products. For instance, some may only need an import license certificate while others may be subject to China Compulsory Certification (CCC) or other regulations.



Fully effective since 1 August 2003, the CCC (China Compulsory Certification) Mark is required for a wide range of manufactured products (in 19 product groups divided into 132 product categories, including some electrical and electronic products) before being exported to or sold in the China market.

It is recommended that consultants, customs brokers, importers and distributors specialised in ICT products be approached for more detailed information regarding the requirements for other ICT products.

New Zealand China FTA Agreement

The New Zealand China Free Trade Agreement (NZ-China FTA) entered into force on 1 October 2008. The FTA provides for the removal over time of tariffs on 96 percent of New Zealand's exports to China.

If a New Zealand exporter wishes to take advantage of provisions within the FTA, the exporter is required to submit a China FTA Certificate of Origin with their outgoing consignments from 1 October 2008. These preferential provisions include tariff reductions and guaranteed clearance of the goods through Chinese Customs within 48 hours if all documentation is complete and correct.

The FTA also includes an Electrical and Electronic Equipment Mutual Recognition Agreement (EEEMRA), which facilitates conformity assessments of a range of electrical and electronic products traded between New Zealand and China. New Zealand exporters will be able to apply the CCC mark to products before the products are exported to China. Accreditations and conformity assessment procedures will need to be carried out by New Zealand agencies which have been formally accepted in China and to have their products recognised as meeting Chinese requirements on importation.

For detailed information on the FTA, please visit: www.chinafta.govt.nz

New Zealand China ICT Cooperation Agreement

On 15 April 2009, the Governments of New Zealand and China signed an Arrangement for cooperation in the ICT sector. The objective is to promote exchanges and cooperation in a number of areas such as:

- development and application of new ICT technologies and services
- use and governance of the internet and control of spam
- ICT standards and e-government and e-commerce.



The co-operation is likely to take place through exchanges, visits, delegations, seminars, forums and events.

2 MARKET ENTRY AND DEVELOPMENT

2.1 Market entry strategies

- Due to the nature of the OEM/ODM industry, it is essential to understand the following.
 - Understand where your product should be positioned in the market.
 - Define your product's competitive advantages.
 - Understand the industry trends, where new product development opportunities are.
 - Understand the importance of the ability to maintain a consistent supply of products.
- Visit the market.
 - A visit to China is highly recommended in order to understand the competitive environment and to start establishing a meaningful relationship with potential Chinese partners.
 - Timing your visit to coincide with a trade fair can give some very useful insights.
- Use capable and reliable distributors.
 - Successful entry to the Chinese market will require an effective distributor with good connections in the industry.
 - Take time to evaluate the performance of a distributor before offering exclusive rights for the whole of China. It could be better to start regionally first and expand in time according to agreed measures.
 - NZTE can assist in identifying and/or qualifying a potential distributor.
- Optimise the opportunity to leverage the message of New Zealand's innovative and creative environment.
- China should be considered not as one market, but as many markets with different idiosyncrasies with differences from one province to another. It should not be assumed that what is applicable in one province applies to another.



- Monitor and check the outcomes of the New Zealand China Free Trade Agreement (FTA) as it may lead to opportunities for New Zealand companies to gain an advantage over competitors from other countries.

2.2 Points of differentiation

In general, the Chinese ICT market continues to provide good commercial opportunities as China continues to develop at a relatively high speed (it's average GDP growth rate in the last ten years is above 8 percent) and the government has issued a series of policies to encourage the development of the ICT sector supported by direct government investment. Furthermore, the government, telecommunications, health and finance sectors have all been identified by the government as key focus areas for ICT investment.

- According to the 11th Five-Year Plan, government spending will reach new highs in the area of IT procurement.
- Investment for telecom appliances has increased after 3G licenses were issued in January 2009.
- Securities companies, local and international banks will all need to enhance their hardware and software as China's stock market develops in size and complexity.
- The Olympic Games in Beijing increased spending in areas of basic infrastructure such as digital TV, systems management and 3G appliances.

Since China opened its door to the world in 1978, a lot of MNC's like IBM, Microsoft, HP and Dell have entered China and occupied a large percentage of the market place. In addition, many new and well funded domestic Chinese companies are becoming more competitive in both the domestic and international markets.

While the China market potential is substantial, close attention needs to be paid to the complexity of the market, costs of entry, establishment of distribution channels, Chinese business culture, identification of suitable local partners and familiarisation with Chinese government policies applicable to the ICT sector.

In addition, considerable planning needs to be made in developing a programme of support for software or equipment that goes into China. It is not always enough to expect that the Chinese buyer will accept remote support out of New Zealand.



2.3 Intellectual property

Protecting intellectual property (IP) – including products, design and processes, trademarks and patents, brand names and promotional material, user manuals, trade secrets and domain names – is one of the biggest issues New Zealand firms face when entering China.

There is a considerable although somewhat diminishing risk of piracy, counterfeiting and reverse engineering in China. The United States Government estimates that on average 20 percent of consumer products sold in China are counterfeit.

There are laws to protect and enforce IP rights, but China's businesspeople do not have a long tradition of intellectual property compliance. There can also be inconsistencies of court proceedings on IP.

In addition, China's IP laws are different from New Zealand's. China has a first-to-file system that requires no evidence of prior use or ownership, leaving registration of popular foreign marks open to third parties.

These legal differences and the risk of IP breaches mean that a New Zealand company entering the market needs a well researched and executed strategy to protect its IP.

But you shouldn't let fears of IP losses alone dominate your decisions on entry into the Chinese market. The business opportunities are huge, the risks can be managed and the situation – both in terms of the dangers and the remedies – is improving.

For more information on IP protection, download the document *Navigating China For New Zealand Businesses* from the New Zealand Trade and Enterprise website:
www.nzte.govt.nz/explore-export-markets/North-Asia/Doing-business-in-China/additional-resources



2.4 Distribution channels

In China, ICT products are mainly sold through distributors, systems integrators or directly into the retail market. Only limited sales are currently made via the internet.

Distributors

In 2008, the following five ICT distributors in China achieved sales revenue exceeding US\$732 million:

1. Digital China:
www.digitalchina.com.hk
2. ESC Technology China:
www.ecschina.com
3. Ingram Micro China:
www.ingrammicro.com.cn
4. Tsinghua Unisplendour:
www.unisdigital.com
5. VST Holdings:
www.vst.com.hk

The top 100 ICT distributors in North, East and South China represent 23.6 percent, 21.0 percent and 19.4 percent of the total national sales revenues respectively (64 percent of the total). The industry has very low profit margins, 90 percent of the top 100 distributors reportedly operated with an average profit margin lower than 5 percent, while 23 percent of the distributors made losses in 2008^{iv}.

System integrators

In 2008, the size of China's system integration service market reached US\$3.1 billion. As of October 2009, 3,422 companies in China obtained system integration qualifications. Only 6.3 percent of the above companies obtained first grade qualification, 15.9 percent obtained second grade, while 77.8 percent obtained third or fourth grade.



Leading Chinese system integrators include:

1. Digital China:
www.digitalchina.com.hk
2. Teamsun:
www.teamsun.com.cn
3. Global InfoTech:
www.git.com.cn

Direct sales

The traditional international model of direct sales for ICT products has not yet been as successfully applied in China. For example, Dell has applied its direct sales model in many other countries, but in China it has signed a distribution agreement with VST Holdings (one of the top three IT distributors in Asia) which covers 12 of China's provinces. Consumers can shop for Dell laptops / desktops in various retail outlets, such as Gome Appliances (one of the biggest electrical appliance retailers in China). Some research suggests that direct sales has more commonly been used as a business model for companies in the initial stage of entering the China market which typically suits small businesses.

3 MARKET RESOURCES AND CONTACTS

ASSOCIATIONS	WEBSITE
China Association of Communications Enterprises	www.cace.org.cn
China E-Commerce Association	www.ec.org.cn
Internet Society of China	www.isc.org.cn
China Software Industry Association	www.csia.org.cn
TRADE EVENTS	WEBSITE
Expo 2010 Shanghai	www.en.expo2010.cn
P&T Expo Comm China	www.ptexpo.com.cn/jnzh/index.aspx
China Hi-tech Fair	www.chtf.com/english
China International Software & Information Service Fair	www.cisis.com.cn



GOVERNMENT

WEBSITE

Ministry of Industry Information and
Technology (MIIT)

www.miit.gov.cn

State Intellectual Property Office

www.sipo.gov.cn/sipo_English/index.html

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ⁱ BMI

ⁱⁱ Ministry of Industry and Information Technology (MIIT), China

ⁱⁱⁱ MIIT

^{iv} China Computer News, May 2009

