China's Transforming Economy: Opportunities and Challenges for European SMEs

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There have been many changes in the Chinese economy over the past decade.

From an average of 10 percent annual GDP growth in the years after China joined the World Trade Organisation in late 2001, the prediction for 2014 is 7.4 percent. Implied in the drop is the need for the Chinese economy to restructure itself, away from export-led manufacturing, which has limitations on adding value to the economy and which is adding to China's environmental woes.

The economy needs to move toward a more sustainable model based on consumption and services being a greater part of GDP growth, and toward greater productivity.

With technologies, products and services, Europe's small and medium-sized enterprises (SMEs) have the opportunity to play a part in China's economic transformation and restructuring, be it in China's strategic emerging industries, in innovation-led growth or in the need to make Chinese workers more productive and skilful.

From research carried out by the EU SME Centre in Beijing, significant opportunities have been identified in a wide array of market sectors.

The information and communications technology industry, for example, considered by the government a national priority and therefore strongly supported in 12th Five-Year Plan. It presents good prospects for European SMEs, especially in high-value niches such as mobile app development, information technology consultancy and outsourcing for financial and healthcare institutions seeking to upgrade their systems, and data integration and quality software, a segment that has shown recent growth rates of around 32 percent.

Similarly, in the food and beverage sector, SMEs can leverage the quality of their products to capitalise on the growing spending propensity of the new, and more health-savvy, Chinese consumers. Not to mention the burgeoning Internet and mobile commerce markets, whose share on the GDP has already reached 5.5 percent and is set to continue growing in the foreseeable future.

Healthcare, in addition, is offering good opportunities to EU SMEs on account of an aging population and the authorities' focus on social welfare.

It is also not only a question of 'what' but 'where'. China's second and third tier cities, and generally the inlands, have been the targets of specific policies by the national and local authorities since the early 2000s aimed at reducing economic imbalances and closing the wealth gap between the coastal and inner parts of the territory. Heavy investments in infrastructure and social safety have resulted in sustained growth rates and enhanced cross-regional market integration. As a result, an expanding middle class has emerged, which, together with the local governments' eagerness for FDI, makes second and third cities appealing business prospects for EU SMEs.

New and Remaining Challenges

While the opportunities are significant, so are the challenges.

From the many business consultations that the EU SME Centre has provided, the primary challenges faced by European SMEs have also evolved. In addition to regulation and market access barriers and macroeconomic changes, HR issues and competition in the Chinese market have become even more prominent in recent years.

Based on surveys conducted by different chambers of commerce in China, the table below summaries the top challenges in the Chinese market identified by European companies.

EU SME Centre	EU Chamber of Commerce in China (EUCCC)	German Chamber (AHK)	French Chamber (CCIFC)	China-Britain Business Council (CBBC)
Business Service Survey 2014	**Business Confidence Survey 2014**	**Business Confidence Survey 2013**	**Business Climate Survey 2013**	**Business Climate Survey 2012**

Language and culture	Chinese economic slowdown	Raising labour costs	Chinese economic slowdown	Labour shortages
Attracting and retaining talent	Raising labour costs	Finding qualified staff	Raising labour costs	Bureaucracy
Market access barriers	Attracting and retaining talent	Retaining qualified staff	Skill staff shortage	Increased Chinese competition
Ambiguous rules and regulations	Market access barriers	Bureaucracy	Delinquent payments from customers	Increased Chinese protectionism
Financing	Ambiguous rules and regulations	Corruption	Global economic slowdown	Rising labour costs

HR Issues: China's reputation for unlimited, cheap labour will soon become a thing of the past with more and more SMEs identifying raising labour costs and talent retention as a major problem for doing business. Finding, attracting, training and retaining staff is also expected to become even more difficult in the next years. This is caused on one hand by raising labour cost for local staff as well as by challenges faced by foreign experts. Difficulties in obtaining visas, the rising cost of living and issues related to high pollution are amongst the main deterrents for expatriates in China.

Increasing Competition: It has also been recognised that the competition in the Chinese market is getting stronger, which arises from the growth of domestic Chinese companies and an increasing number of international businesses. Domestic competitors have the advantage in gaining deeper understanding of local customer behaviours, establishing closer government relationships and often adapting more quickly to the market and regulation changes than European SMEs.

Regulation and Market Access Barriers: Bureaucracy has remained a constant challenge over the years and few companies report significant improvements. As the Chinese market has become more and more competitive, barriers to market access are increasingly noticeable to SMEs looking for new opportunities. Lack of transparency and ambiguous rules and regulations are also reported to be major challenges on the market.

Macroeconomic Changes: As China makes the transition to an economy more driven by internal demand, the legacy of the export driven model, paired up with the global economic slow-down has been felt in the country's slowing economic growth. The 10% year to year growth rate of the 2000s is now accepted as a thing of the past as Chinese leaders are preparing for the new "normal".

Helping SMEs Make Informed Business Decisions

To continue being successful in the Chinese market, European SMEs will need more support particularly in the areas that present the biggest challenges, such as market access and HR management.

The EU SME Centre in Beijing recently launched its second phase, running from 2014 to 2018, in which it will reassess the primary needs of European SMEs and will add new services to help them deal with more complex business issues.

At the Centre's Phase II launch event in Beijing, Director Chris Cheung introduced the project's new structure to stakeholders and partners, and unveiled three core service centres –Knowledge Centre, Advice Centre and Training Centre – which will deliver more in-depth business support and technical solutions to EU SMEs allowing them to make more informed business decisions.

Advocacy for SMEs – Giving a Voice to Small Businesses

In collaboration with the European Chamber of Commerce in China, the EU SME Centre is also launching an advocacy platform for European SMEs. Companies will have the opportunity to join a new inter-chamber SME working group to share their business challenges and voice common concerns to EU and China policy-makers on improving the investment and trade environment. Meetings will address practical business issues to ensure that SMEs are given the right channels to provide feedback in their industry sectors.

About the EU SME Centre Phase II

The EU SME Centre officially launched its second phase at the EU Delegation in Beijing on November 26th, 2014, having secured funding from the European Union for another four years. The Centre's second phase is implemented by six partners – the China-Britain Business Council, the European Union Chamber of Commerce in China, the French Chamber of Commerce in China, the China-Italy Chamber of Commerce, the Benelux Chamber of Commerce and EUROCHAMBRES. To learn more about the services that will be available in the new phase, contact the Centre at info@eusmecentre.org.cnor visit www.eusmecentre.org.cn