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Strategy for Entering China's Regional and Provincial Domestic Markets

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1. China's Markets and Industries by Region

China's regional consumer markets can be classified under the following categories; the large-scale consumer market, the consumer market with high potential, the

rapidly rising consumer market and the restricted consumer market. The large-scale consumer market, while characterized by low growth rates, secures a sizable target and mainly consists of the developed coastal area covering Guangdong, Jiangsu, Zhejiang, Shanghai and Beijing.

Meanwhile, the consumer market with massive growth potential thanks to its considerable size and heavy population includes much of China's central and western region - Henan, Sichuan, Hubei, Hunan, and Anhui. Of these regions, Inner Mongolia (Nei Menggu), Shaanxi, Sichuan, Anhui, Hainan and Hubei are quickly emerging as areas recording rapid growth rates in terms of income and consumption. Projections are that during the next five years the most significant consumption growth will come from large markets like Guangdong, Jiangsu, Zhejiang, Shandong, Henan and Hunan. In an effort to boost domestic consumption, China has set up and initiated detailed action plans by region, incorporating central government policies that focus on improving consumer power, stabilizing consumer prices related to public welfare, and developing new consumer domains.

The industrial sector - manufacturing in particular - remains one of the most important drivers of China's regional economic growth, and serves as the basis for the development of the service sector. In terms of gross output, China's major manufacturing industries are ferrous metals processing, computers/communication/electronic equipment, automobiles and transportation equipment, chemicals, electric machinery and equipment, and agricultural food processing; major production bases are Jiangsu (12.8%), Shandong (11.8%), Guangdong (11.2%), Zhejiang (6.7%), Henan (5.5%) and Liaoning (4.9%). An examination of the concentration of companies by sector and gross output helped match specialized industries to certain regions - ferrous metals processing, automobiles and transportation equipment, agricultural food processing in northeastern China; automobile and transportation equipment, computer and communications equipment, chemicals in the Bohai Economic Rim; computer and communications equipment, electric machinery and

equipment, automobile and transportation equipment in East China; computer and communications equipment, electric machinery and equipment, chemicals, leather and fur in South China; ferrous, non-ferrous metals and non-metals processing, chemicals, automobiles and transportation equipment, agricultural food processing in central China; and resource processing (ferrous metals, non-metals, oil, etc.), agricultural food processing, chemicals in West China. Strategies for industrial advancement in China overall have been set in the direction of restructuring in key industries, efficient industry allocation by region, enhancing business technology standards, improving industrial concentration through M&As, and spurring SME development. And in each region, the above-mentioned policy directions have been applied to regional policies based on the corresponding specialized industry.

Based on an analysis of the consumer base indicator - indexed from 15 weighted statistical indicators related to China's consumer market - Chengdu, Wenzhou, Xi'an, Wuhan, Zhengzhou, Ningbo, Changsha, Jiaxing, Jinhua, Chongqing were selected as the top ten consumer bases. Meanwhile, an analysis of the production base indicator - indexed from 18 statistical indicators related to manufacturing and production - revealed Chengdu, Chongqing, Tianjin, Wuhan, Zhengzhou, Nanjing, Shanghai, Changsha, Wuxi, Qingdao to be the top ten production bases.

2. Export Market Targeting Domestic Demand

Since the late 2000s, the share of trade targeting domestic sales as a percentage of total exports to China has gradually moved upward to reach 33.7% in 2012. This is still low compared to the 56.3% accounted for by general trade in imports from China. By region, Ko-

rea's largest export target for domestic sales in China is East China, accounting for 35.1%, followed by the Bohai Economic Rim at 27.8%, South China at 20.4%, and Shandong at 8.9%.

In terms of the processing stage of Korea's exports to China targeting the domestic market, all regions displayed the highest percentage in intermediary goods. Compared to other regions, the three northeastern provinces and central China had a high share of primary commodities and capital goods; the Bohai Economic Rim displayed a high share of consumer goods; in East and South China intermediary goods were dominant. A look at the key target markets of intermediary goods, capital goods and consumer goods exported from Korea to China targeting the domestic market shows that eastern China is the largest market for intermediary goods, while the Bohai Economic Rim is the largest for capital and consumer goods.

In terms of the type of industry exported from Korea to China, the chemical products industry was the top export to the northeastern, Shandong, eastern and southwestern regions, automobiles and trailers to the Bohai Economic Rim, electric components and communications equipment to southern China, and machinery and equipment to the central and southern regions. Meanwhile, in terms of the main export market targeting domestic demand in the main industries, the market for the chemical products industry is concentrated in eastern China, electronic components and communications equipment in southern China, and automobiles and trailers in the Bohai Economic Rim.

From the perspective of China's import market - imports targeting the domestic market - by region, aside from Shandong Province Korea is at a comparative disadvantage in all re-

gions. Major competitors in the northeastern region, the Bohai Economic Rim and the midwestern region are Japan, the US and Germany, while in the central region Taiwan joins in the competition. Japan, the US and Germany are also key competitors in East China; Taiwan, Japan and the US in South China; and the US in Shandong. On the positive side, key competitors do not pose that much of a threat in areas other than the Bohai Economic Rim, where the US takes the lead, East China, dominated by Japan, and South China, where Taiwan is the top competitor.

3. Korean Companies in China

A regional analysis of Korea's investment in China from 1989 to 2012 with a focus on investment for entry into China's domestic market revealed that from 2002, the share of investment aimed at the local market jumped significantly in all seven regions. Apart from the northeastern region, manufacturing remains the top area of investment.

Meanwhile, according to a survey conducted from September to October 2013 on the business performance of and difficulties faced by Korean companies in China, the automobile, medical and healthcare, and business service sectors showed the highest levels of satisfaction, along with the most positive prospects for the future. By region, companies in East China displayed above-average satisfaction levels and prospects, while the northeastern, central and western regions also had higher prospects for the future.

In terms of purchases and sales, the share of local subsidiary materials procurement and product sales was 13 to 17.5 percentage points higher than calculated in existing studies, leading to the conclusion that the surveyed companies were more successful in local procure-

ment and sales compared to the overall average of Korean companies operating in China. Localization was especially advanced in the food and beverage and automobile sectors by industry, and in the Bohai Economic Rim and Shandong Province by region.

As for competitiveness, Korean companies in the manufacturing sector had an advantage over their Chinese counterparts in terms of quality, technology and design; the gap was not significantly wide in the non-manufacturing sector. Compared to foreign companies, the competitiveness of Korean companies was found to be on a similar or lower level.

Out of the four P's of price, product, promotion, place (distribution), companies placed a focus on product and distribution strategies, led by the food and beverage industry and the northeastern and southern regions. Although active discussions are taking place on CSR activities, not many of the surveyed companies were deeply engaged in this direction.

Common difficulties faced by the companies were human resource affairs and labor services regardless of industry or region, specifically problems with securing high-quality professionals and dealing with rapid wage increases. Also, the biggest obstacle faced in the course of transition from export-orientation to China's domestic market was the recovery of payments and excessive competition in the local Chinese market, mostly solved independently or through guanxi.

Opportunities found in the Chinese market were the New Urbanization Strategy and the Great Western Development Strategy, infrastructure expansion, service sector development, and strategic development policies for fostering new industries. Meanwhile, 66% of the survey respondents answered that the Ko-

rea-China FTA would play an assistive role in entering China's domestic market.

4. Strategies on Entering China's Domestic Market

Entry into China's domestic market, by region, requires a tailored strategy that takes into account the nature of the region's consumer market and industries, import market, major investment sectors, competition with Chinese or foreign companies, and so forth.

Taking the Bohai Economic Rim as an example, Beijing and Tianjin are already home to large consumer markets; Beijing, especially, is a representative consumer market accounting for 36.5% of the nation's import of consumer goods targeted at China's domestic market. Hebei Province is a potential consumer market that uses Tangshan, a coastal city, and Shijiazhuang, the province capital, as bases.

As an import market for industrial products targeting the domestic market, Beijing shows potential in the areas of automobile-related products, professional machinery and equipment, and medical equipment. However, items like motor cars (HS 8703) and motor parts and accessories (HS 8708) have recently been faced with intense competition from major countries, calling for efforts to expand market share. Promising export items to Tianjin are IT or electronic products, although relevant items such as electronic integrated circuits (HS 8542) or telephones (HS 8517) are likewise challenged with stronger competition. In Hebei Province, export items with potential are petrochemical products and auto parts, etc.

Investment in the Bohai Economic Rim should take into account the different characteristics of each province and city. For Beijing, investment should be centered on the service

sector, while in Tianjin the IT and electronics industry remain the most promising but call for efforts on the side of Korean companies to pull up falling competitiveness by securing an advantage in quality, brand, price and so forth. The ferrous metal processing, light and textile industries show the highest potential for investment in Hebei Province.

It is essential to formulate these tailored strategies based on data specific to local markets

and industries. To select a location, the very first stage of market entry, basic - but also key - information on China's regional market and industry infrastructure, imports targeting the domestic market, investment conditions and competition is needed. Once the location is selected, and the production or sales branch is established and open for business, it is important to make a timely, or early, identification of China's market or policy shifts. 