

Keys to Selling in the World's Fastest Growing Large Market

China is more than a low-cost manufacturing country, exporting billions of dollars' worth of increasingly sophisticated products. What is often overlooked is that China is already the fastest growing large market for most products and will become the leading industrial and commercial market in the world in a few short years. China is accelerating its transition from export domination to a balance of domestic consumption. By 2025, experts predict that China will have 600 million people living in families with the comparable purchasing power of USD 50,000 per year in today's value. That's a middle-class consumer market approaching twice the size of the entire U.S. population, and there will still be >800M Chinese working to join that middle class. This is a market that is too large to ignore and that will continue to grow in influence and importance in all aspects of commerce and technology.

| 2018 GDP Statistics | | |
|-----------------------------|----------|----------|
| | U.S. | China |
| GDP Purchasing Price Parity | \$ 20.6T | \$ 25.3T |
| Nominal GDP | \$ 20.6T | \$ 13.4T |
| Per Capita | \$ 62.9 | \$ 18.1K |

Source: CIA World Fact Book

Purchasing Power Parity

Statistically, China's nominal GDP is already over 60% of that of the U.S. according to the CIA's World Fact Book data reporting the most recent 2017 data available. But raw data can be misleading for anyone trying to make strategic business decisions. Consider the Purchasing Power Parity (PPP), a statistical process that adjusts economic data based on differences in relative costs in various countries. If a bicycle costs twice as much in the U.S. compared to China, it is still a bicycle with the same intrinsic/functional value in both countries. To get a true measure of comparison of industrial and economic statistics, economists use PPP adjusted data. In other words, PPP determines how much money would be needed to purchase the same goods and services in two countries. By

this PPP measure, China is already the largest national economy in the world.

The relative prices of many goods and services in China are different than in the West. Cars are more expensive in China than the West. Electronics (e.g. computers and consumer products) are essentially the same cost because they have been globally equalized. However, the staples of life, such as basic food, clothing, and utilities are often a fraction of the cost in the West. Middle class families in the West spend over half of their available income on these staples of life.

This perspective on the China market is important. You simply can't assume that consumer income is lower in China and therefore be discouraged about the market potential. Profiling the size and trends of markets and embedded opportunity takes analysis and perspective that is often not intuitively obvious. Here's the bottom line, according to the CIA's statistics, China is already the largest economy in the world on a Purchase Price Parity basis, exceeding the U.S. by 18.9% in 2017.

Local Content and Market Connection

When developing a sales strategy in China, don't plan to serve the market by solely exporting finished products from the U.S. for anything more than a short introductory period. If you do, your early success will most likely turn into longer-term disappointment. The preference of local content runs far deeper than simply avoiding foreign exchange requirements or import tariffs that will vary over time based on political policy. People in China may prefer a Western brand, but they also prefer the ease of doing business locally. This is not a China phenomenon. When you get your car repaired in the U.S., you generally don't go to a shop too far from your community. You get the work done locally because of convenience, ease of communication, and logistics. Even more importantly, if something is not right, you want the problem fixed quickly.

Local support, communications, and logistics are powerful drivers of supplier selection. In China, with the complications of a different language, different commercial paradigms, and a twelve-time zone difference, the advantages of local content are obvious.

Let's take the discussion one layer deeper. Many products that hit the target of consumer demand in China have different physical attributes (sizes, configurations, or basic features). For example, refrigerators in China are smaller than a U.S. kitchen sized model. Their refrigerator provides the same functionality as our standard products, but the size and feature set are very different. Most Chinese families do not have cars and therefore it is inconvenient to carry large amounts from the grocery store to home. Instead, most Chinese go to the neighborhood market multiple times per week by walking or public transportation. Add the fact that Chinese homes are a fraction of the average home size in the U.S., the extra size of a U.S. kitchen refrigerator simply has no utility to even a relatively affluent Chinese family.

Successful products and services are optimized to the culture, economics, regulatory, and other commercial drivers of a specific market. It is wrong to assume that successful products from one market will also be optimized for another. If you want to start an operation – sales, service, trading, or manufacturing – you will also need to adapt to different legal, financial, human resources, professional skill sets and organizational dynamics that prevail in China. To be successful in a market like China, it is necessary to first understand these complex differences and the changes to your products and services that you will need to make.

Providing local content – even simply sales, stocking and distribution – also represents market commitment, which is important in China. The more strategically important a component or service is to the customer, the more likely they will look for long-term and local supply relationships. Our experience is that Chinese customers – local and foreign owned – want key suppliers who are committed to a long-term presence in China. They may start by importing from Western suppliers, but that does not last long. The benefits of shorter supply chains, local support, ease of communication, and often much lower costs, represent a compelling package to China based customers.

Creating a shorter supply chain doesn't have to be complicated. You can contract with a Chinese bonded logistics company to stage products in China (owned by the parent company). When you are ready to sell, your product is sold by the parent company and shipped from this in-country bonded stock. This approach reduces the shipment cycle by weeks and provides a limited local presence. The

inventory can also be used as a stocking hub to serve the rest of Asia.

China Is Not One Market

One major mistake many Western companies make is assuming that China is a single market. Geographically, China is nearly equal in size to the continental U.S. and much larger than the E.U. We would never think of either of these two developed markets as monolithic and you should not think of China that way either. In many respects, China is far more regionalized than the U.S. and more similar to the E.U. in terms of regional differences. France and Germany are very different in language and culture even though they are direct neighbors. A Parisian is likely less effective selling in Berlin as he or she can be in France. Similar regional differences exist in China and present challenges in establishing sales channels.

Languages and regional cultural differences exist to make it challenging to develop a “one size fits all” sales and marketing approach to China. You may hear claims from potential China partners that they can be your exclusive channel partner and give you nationwide blanket sales coverage. While there may be some rare examples where this could be true, it is not realistic in most product or service spaces.

Market Success in China Demands Different Skills

In many respects, China does not respond the way markets respond in the West. Managing the wide variety of relationships in China is different than managing comparable interactions in the West. Navigating through these differences is not difficult, but it does require the candid recognition that managing customers, suppliers, and employees in China requires different approaches for success. Companies that transfer their Western business practices to China, expecting them to transfer seamlessly, encounter problems. The issue is not that there are differences but identifying those differences and understanding how to navigate around them.

How Do You Get Started?

The first two years of a company's new entry into China are the most challenging. You must learn about a new environment that is target-rich, highly dynamic, with a different language (including interpersonal communication), culture, legal and regulatory structure.

These differences are spread across a range of interactions with customers, suppliers, and organizations with which you will interact on a daily basis.

Here are some recommendations to accelerate and de-risk China market initiatives:

- Actively seek out and build a solid base of local knowledge about your markets, products, supply chain options, and competitors.
- Don't underestimate the importance of local content and presence. Your customers will appreciate local support, communications, and logistics. Establishing local content does not have to be complicated. It can simply partner with distributors and/or stock product in bonded warehousing.
- Start with the assumption that the Chinese market will view and value your products and services differently than your Western customers. You may need to modify your products for China or change your sales pitch. De-featuring products may be necessary to take out costly features that have little to no China utility to meet target price points for market success.
- Resist the temptation to sign up a single China distributor who claims to have the ability to serve all of China. Even in a much more homogeneous market like the U.S., very few product or service markets can be served effectively by one market partner. Take your time to find the right distribution partners and build a sales network. Start in a high-potential geographical area like the Yangtze River Delta or the Pearl River Delta.
- Remember that Western business practices are optimal in the West. Market entry into China may require different approaches for successful navigation through their business environment.
- Keep an open mind to strategic options. There are many roads to establishing a successful strategic plan and vision for your China business. Once you have a focus on what you want to become in China there are a variety of alternative action sets you can take.