

Canadian Business Views on China

- 2006 Survey of Canadian Manufactures and Exporters



Asia Pacific Foundation of Canada



Canadian Manufacturers & Exporters

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1. Introduction and Executive Summary

The re-emergence of China has transformed the world economy. China has become an influential global player in manufacturing and production chains, in exports and imports, as a destination and a source of foreign direct investment, and in commodity and capital markets around the world. What do these trends mean for Canadian businesses? Are they an opportunity or a threat? Should Canadian manufacturers and exporters have a China strategy to cope with a re-emerging China? What is an effective strategy for Canadian companies doing business with China?

In order to obtain answers to these questions, the Asia Pacific Foundation of Canada (APFC) and Canadian Manufacturers & Exporters (CME) jointly conducted a survey of Canadian companies in September 2006. The survey was targeted at CME members drawn from all sectors of Canada's manufacturing and exporting community and from every province. Together, CME's membership accounts for an estimated 75% of total manufacturing production and 90% of Canada's exports. In all, 986 companies provided valid responses to the survey, and the results are accurate within 3.5 percentage points 19 times out of 20.

This report presents findings of the survey. It covers three fundamental areas, namely corporate Canada's engagement with, understanding of and preparation for China. The main findings include:

- ◆ Canadian companies' have a moderate level of engagement with China. Over one-third of respondent companies report that they are currently doing business with China. Nearly one-third of companies have made investments in China. However, the level of engagement varies by industries and the size of companies.
- ◆ Canadian business activities with China are concentrated in international trading, including imports from and exports to China.
- ◆ Canadian companies are generally newcomers in the Chinese market. Just under two-thirds of companies doing business with China have been doing so for a period of three years or less. Only 8% of companies have been doing business with China for more than 10 years.
- ◆ Canadian companies are about evenly split in their view of China as more of an opportunity or a threat to their business. One-third sees China as an opportunity; slightly fewer companies see it as a threat.
- ◆ The more business engagement Canadian companies have with China, the more likely they are to see China as an opportunity rather than a threat.

- ◆ The three major business opportunities that respondent companies believe China offers is as a source of low-cost imports; as a new market opportunity; and as part of their global supply chain.
- ◆ Nearly one-third of respondent companies say that business with China has great or very great potential to reduce costs and boost revenue growth. More companies see China with great or very great potential if they are already engaged in business with China.
- ◆ China is also seen as the source of significant business challenges for Canadian manufacturers and exporters, whether as competition in Canada, the United States or other markets.
- ◆ Only 17% of respondent companies report that they have a formal China strategy. However, more companies have a China strategy in place if they are already doing business with China, see China as more of an opportunity than a threat, target global markets, or are a large company.
- ◆ Among those companies that have developed a China strategy, 66% say that their objective is to maintain global competitiveness and 65% say that they want to gain access to the Chinese market. China is also important in business strategies to lower production costs, outsource products and materials, diversify markets and follow the moves of customers as well as suppliers.
- ◆ The five most important components of a China strategy of those companies that have developed formal business plans with respect to China are: cost reduction; outsourcing; the need to move to higher value products; the need to develop partnerships with Chinese firms; and understanding political risk.
- ◆ China strategy is primarily a company's internal initiative. What leading global firms are doing and what competitors are doing with regard to China also impact on a company's China business plan.
- ◆ China still accounts for a small proportion of the total revenues earned by Canadian manufacturers and exporters. However, companies with a China strategy tend to have a higher proportion of revenues earned from business with China. Companies with a China strategy are more optimistic about their business outlook in the future.
- ◆ The next steps to expand business with China include making more visits to China; hiring local staff and agents in China; investing in China; and identifying proper Chinese or international partners.

2. Survey Findings

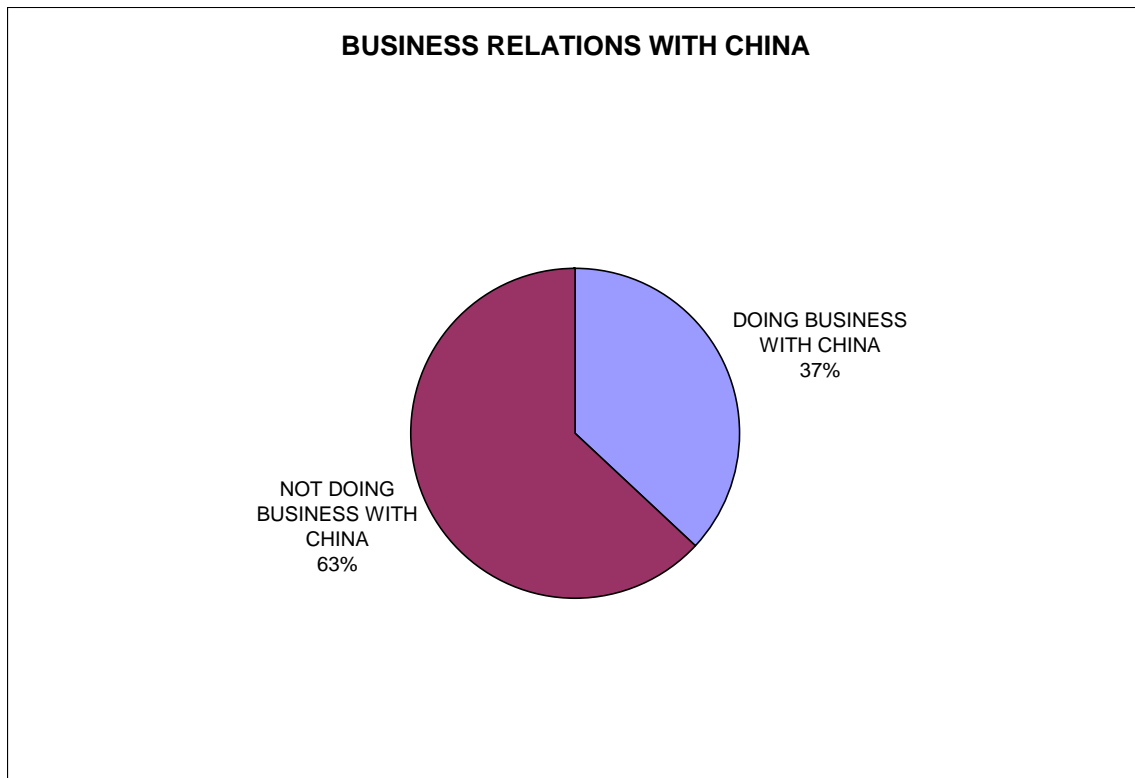
2.1 Engaging with China

Doing Business with China

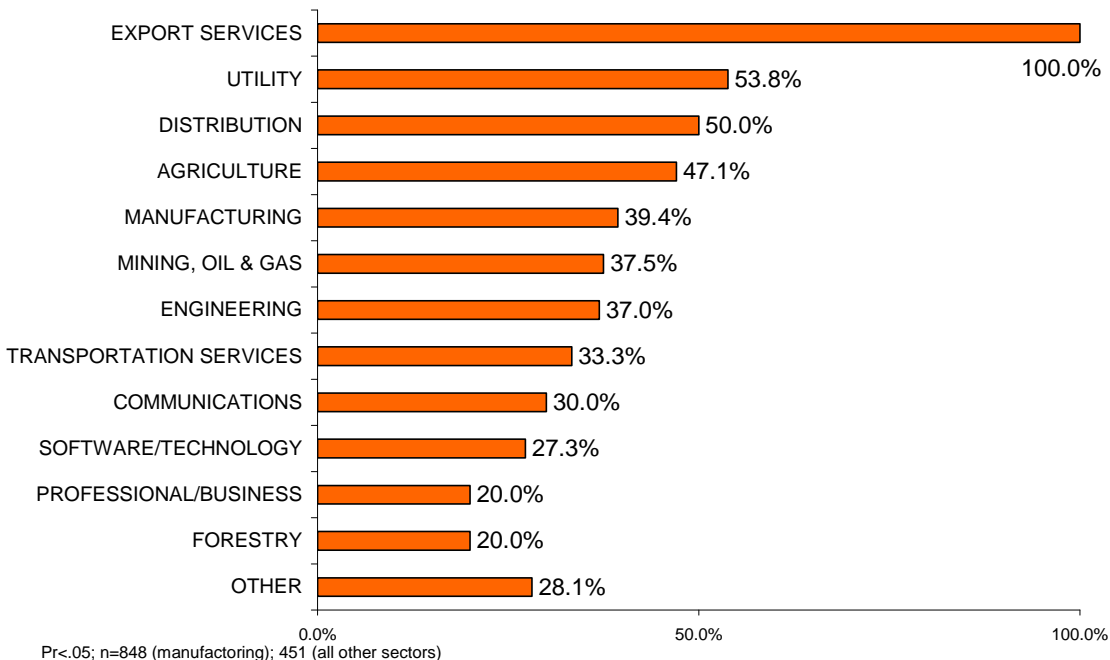
In general, just over one-third of respondent companies report that they are currently doing business with China.

The industry sectors of export services, utilities and distribution are the top three that are most actively engaged with China. Among manufacturing industries, primary metals; textiles, footwear, clothing; and automotive products are the active sectors doing business with China.

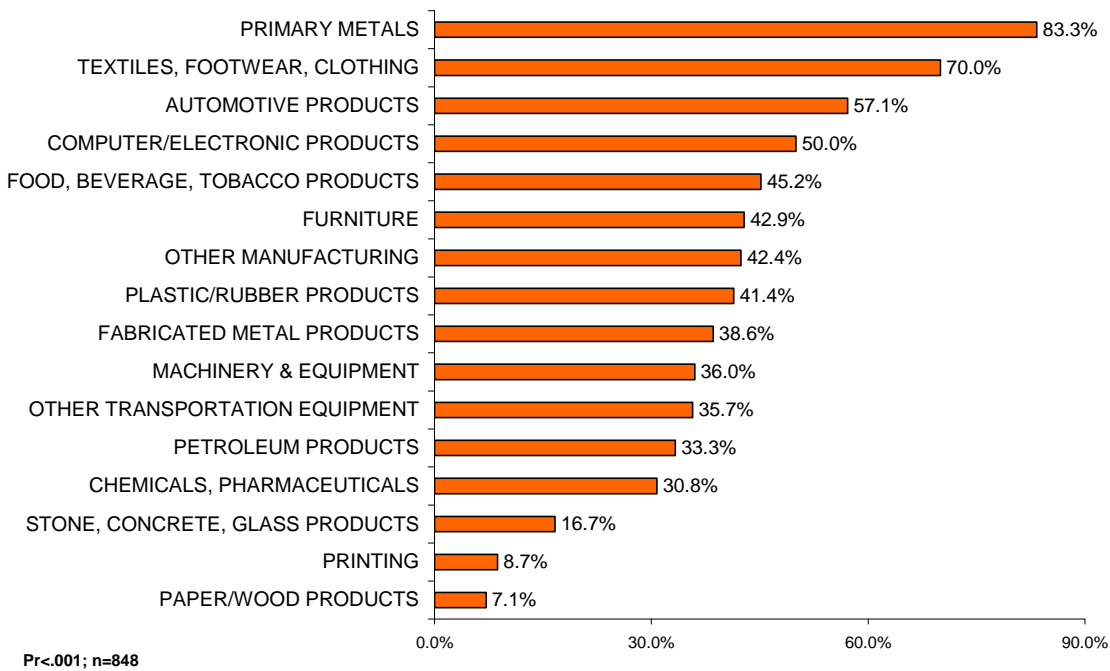
Larger companies are more likely to do business with China. The percentage of companies doing business with China increases from a quarter to over two-thirds as the size rises.

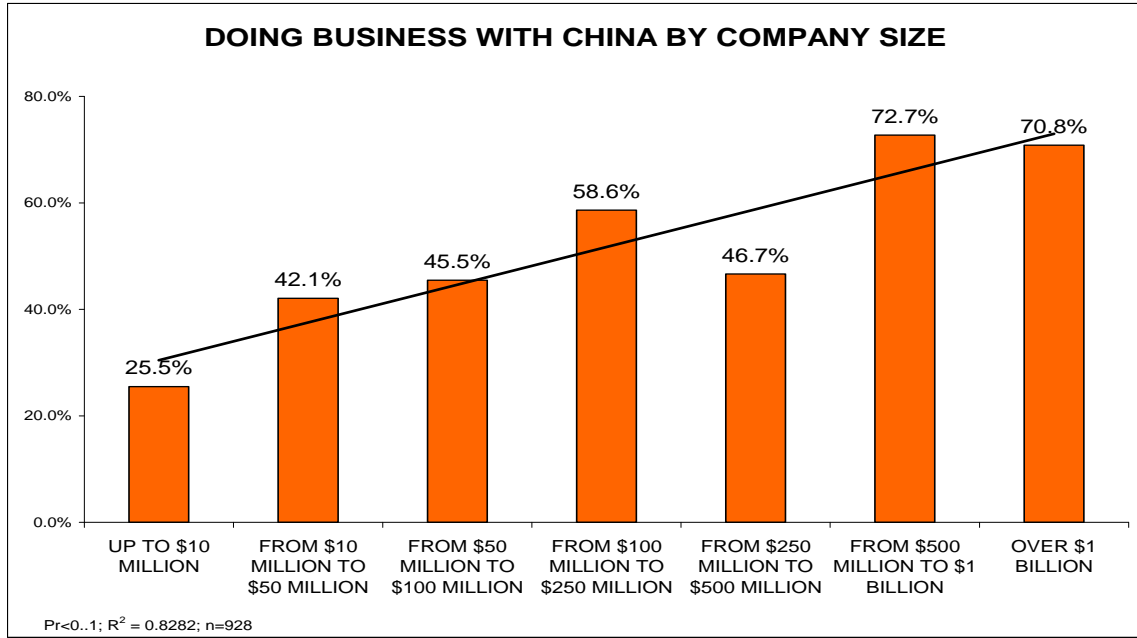


DOING BUSINESS WITH CHINA BY SECTOR: ALL INDUSTRIES



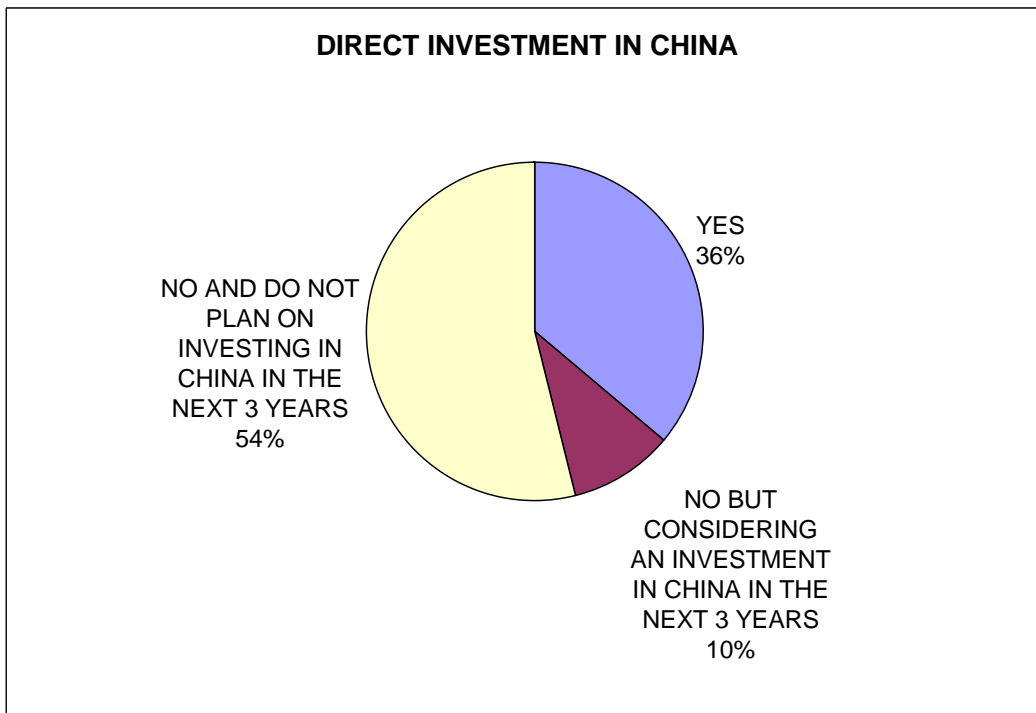
DOING BUSINESS WITH CHINA BY SECTOR: MANUFACTURING





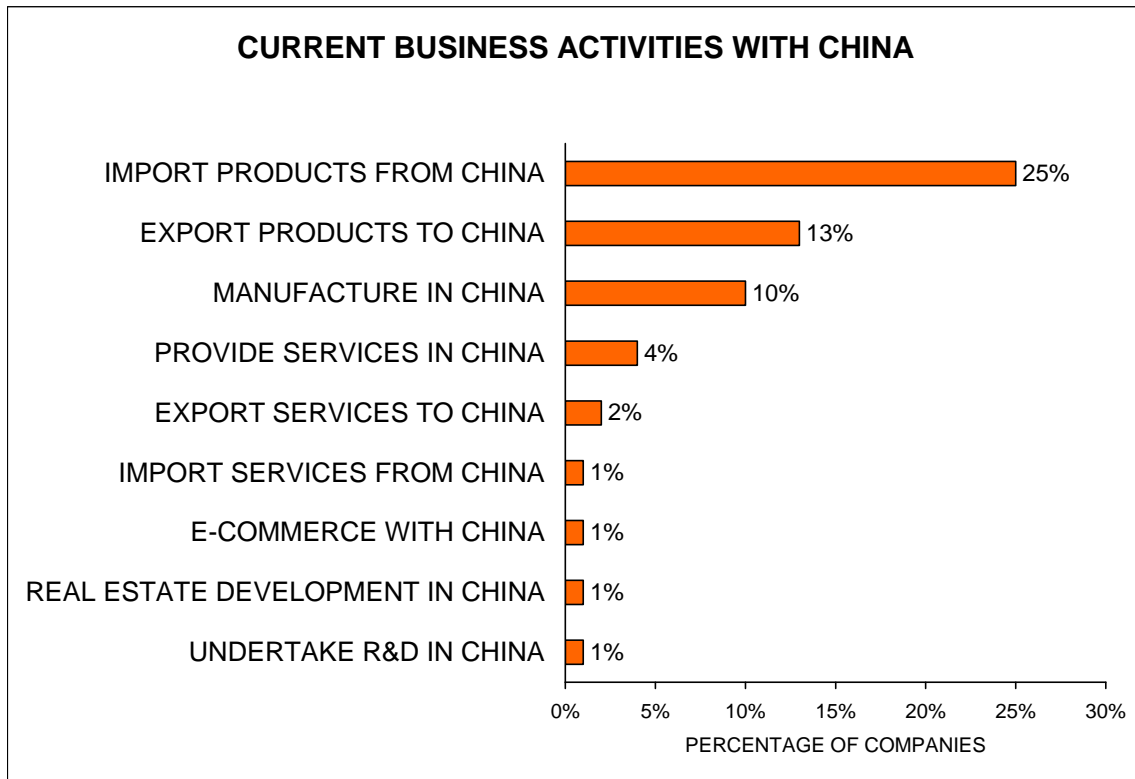
Direct Investment in China

Over one-third of respondent companies have made investments in China. Another 10% have not invested but are considering an investment in China within the next three years. Over half of respondent companies have not invested and do not plan on investing in China in the next three years.



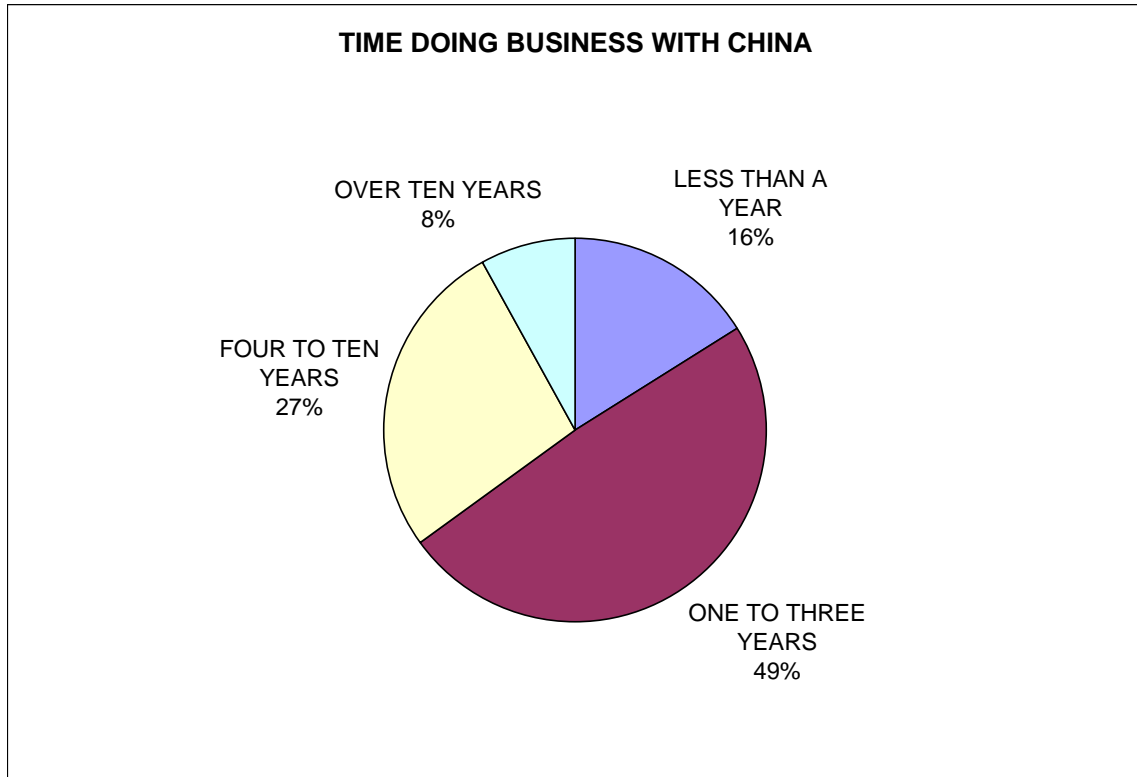
Current Business Activities with China

Current Canadian business activities with China are concentrated in international trading. A quarter of companies participating in the survey are importing goods from China while 13% report that they are exporting products to China, and 10% have set up manufacturing operations in China.



Time Doing Business with China

Canadian companies are generally newcomers in the Chinese market. Just under two-thirds of those companies that are doing business with China have been doing so for a period of three years or less. Only 8% of companies have been doing business with China for more than 10 years.



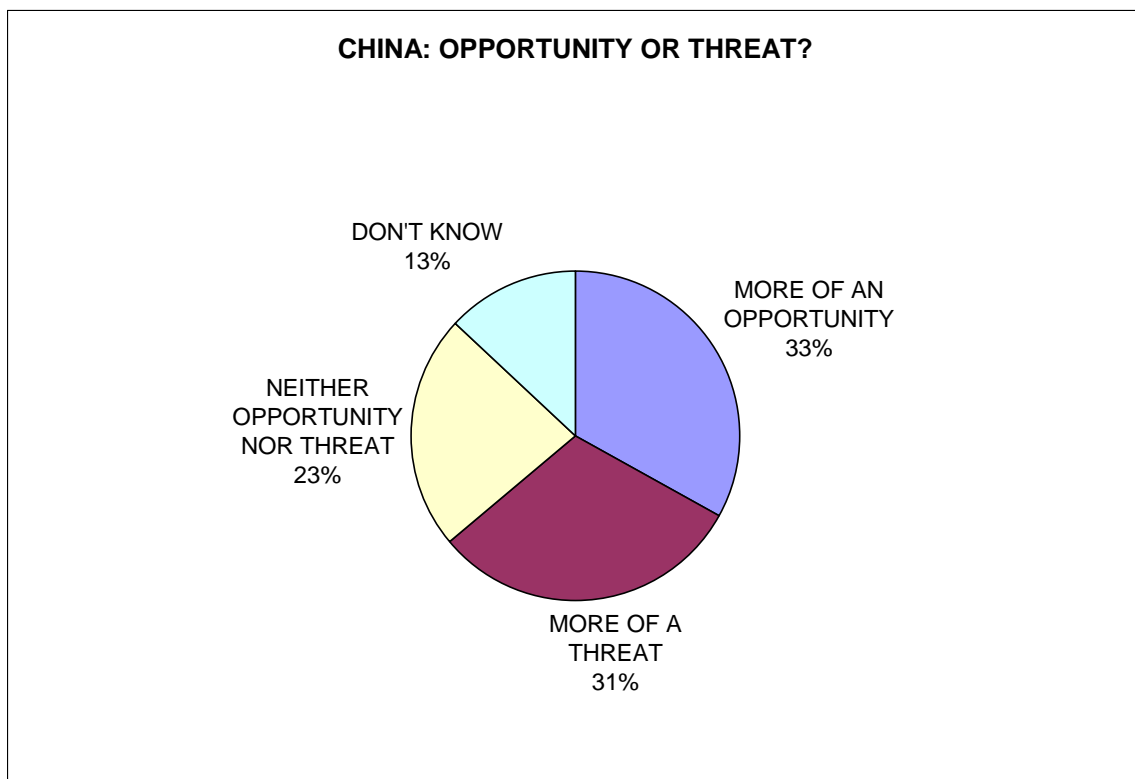
2.2 Understanding of China

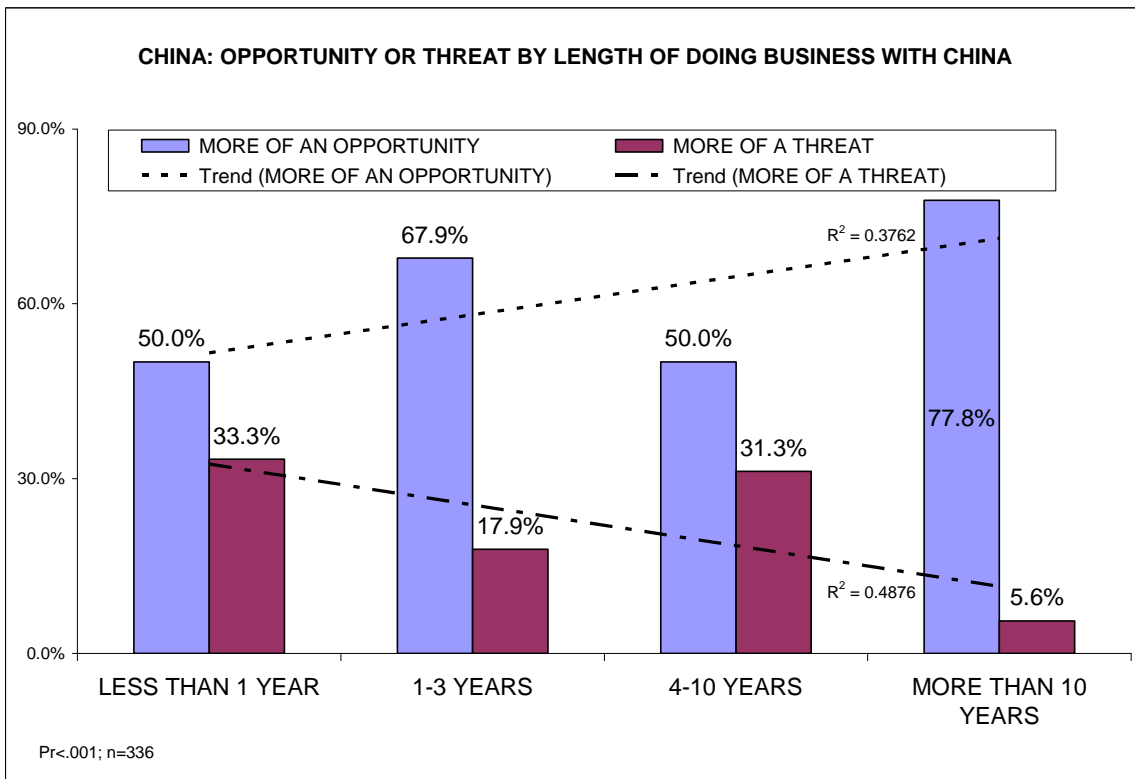
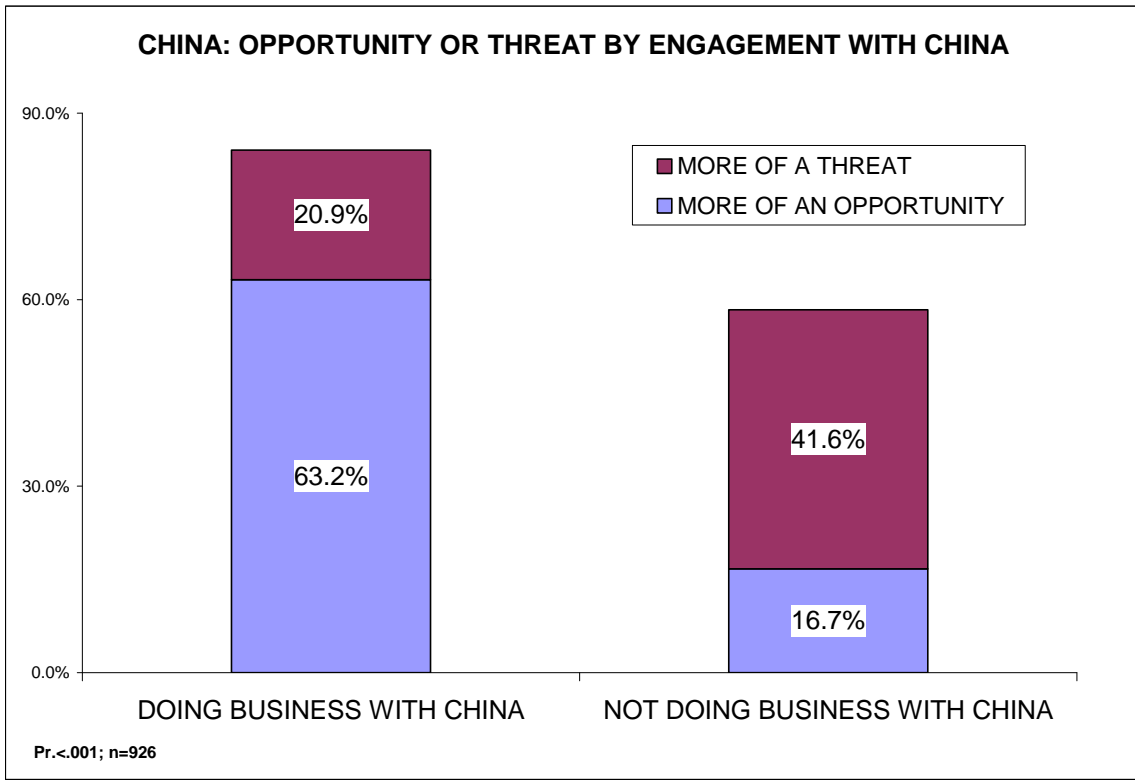
China: Opportunity or Threat?

Canadian manufacturers and exporters are about evenly split when asked if China is more of an opportunity or more of a threat to their business. One-third see China as an opportunity; slightly fewer companies see it is a threat.

However, the views vary significantly by the extent of business engagement with China. Nearly two-thirds of companies that are doing businesses with China see China as more of an opportunity, while only 17% of companies that are not doing business with China consider it as of an opportunity.

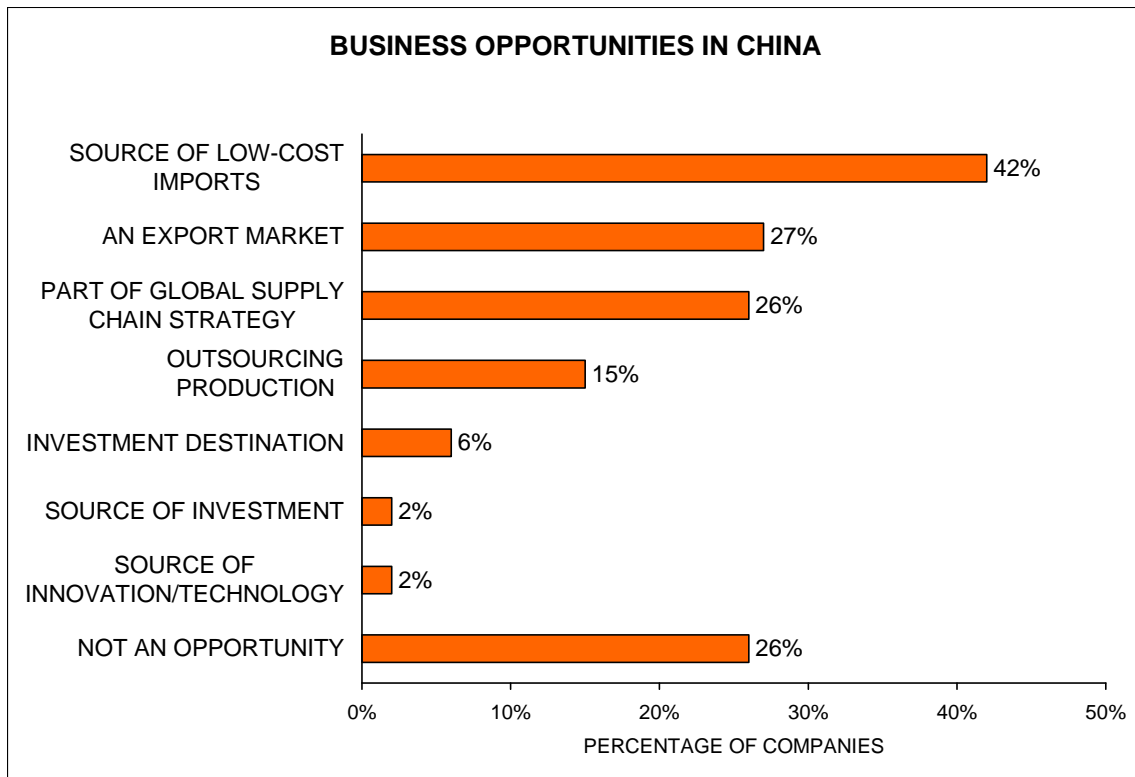
The opinions also differ among companies with different length of business involvement with China. The longer the time that the companies have done business with China, the more likely they are to see China as of an opportunity and less likely to regard China as a threat.





Business Opportunities in China

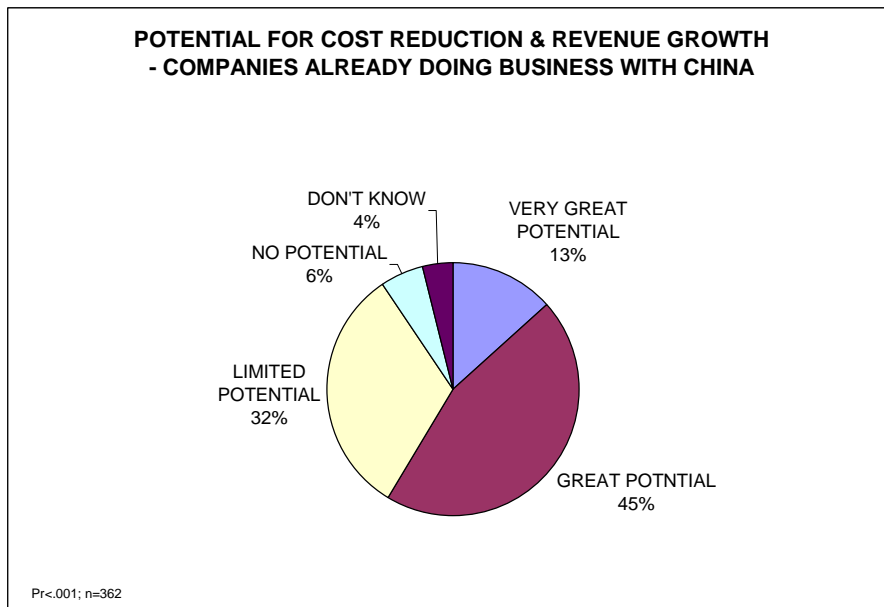
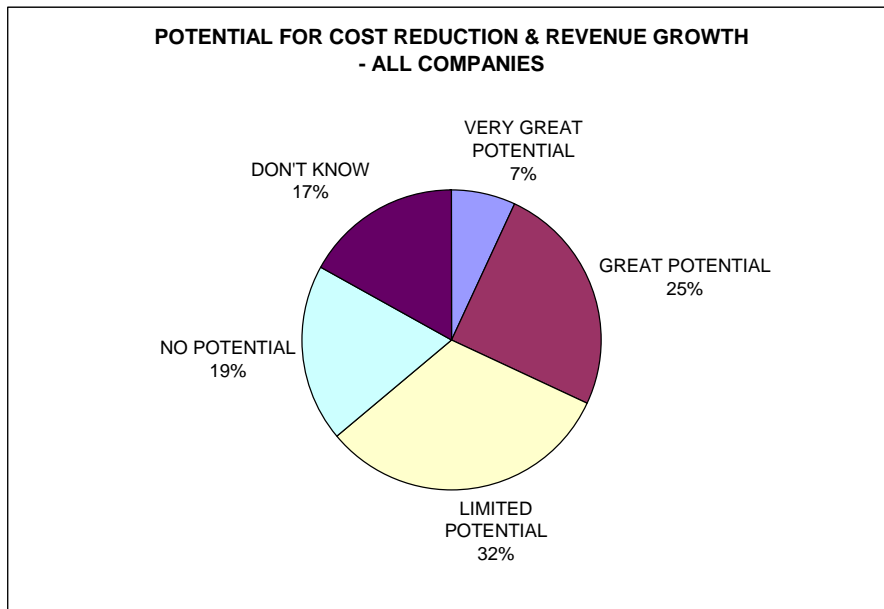
The greatest opportunity business Canadian business sees in China is as a source of low-cost imports. Just over a quarter of respondent companies say that China offers them new market opportunities or opportunities as part of their global supply chain. However, 26% of companies do not see China as a source of business opportunity at all.



Potential for Cost Reduction & Revenue Growth

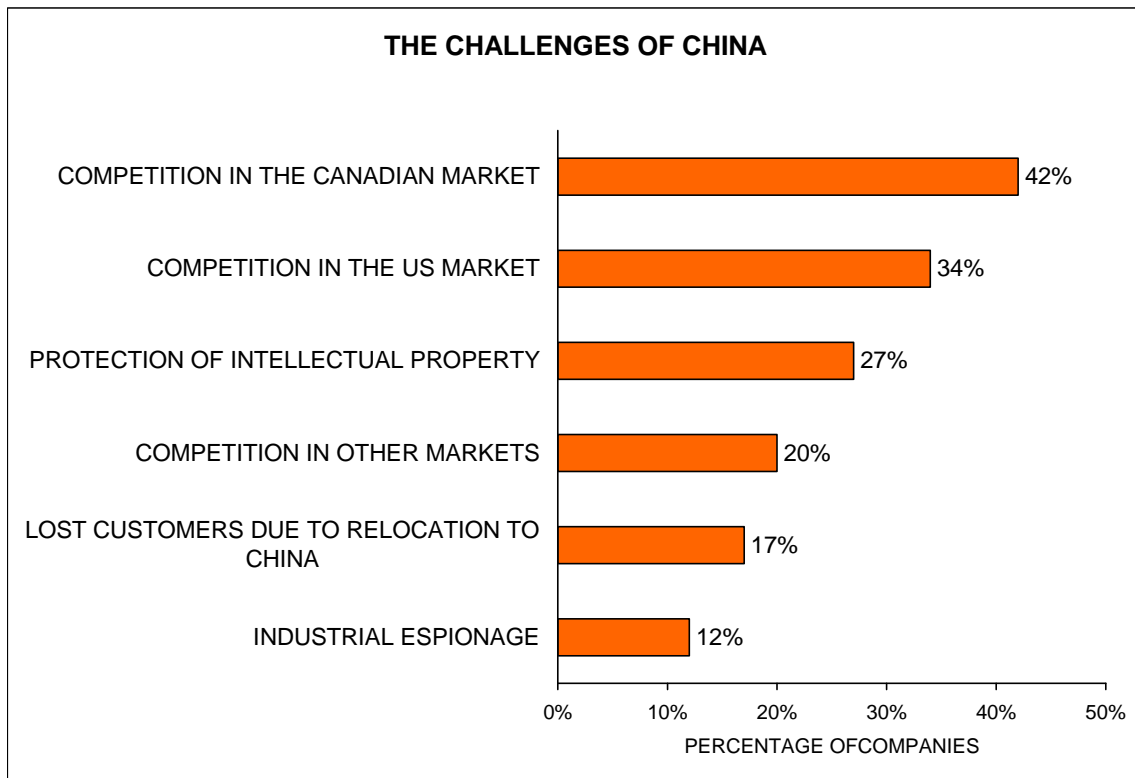
Nearly one-third of respondent companies say that business with China has great or very great potential to reduce costs and boost revenue growth. While 51% of companies say China holds limited or no potential for their businesses, a full 17% do not know.

However, among those already involved with China, the percentage of companies saying that business with China has great or very great potential to reduce costs and boost revenue growth increases dramatically to 58%. Only 38% of companies say China offers limited or no potential for their businesses, and just 4% do not know.



The Challenges of China

China is seen as the source of significant business challenges for Canadian manufacturers and exporters. This may be because of competition in Canada, the United States or other markets; the need to protect intellectual property rights; because customers are being lost as a result of their relocation to China; or because of concerns over industrial espionage.

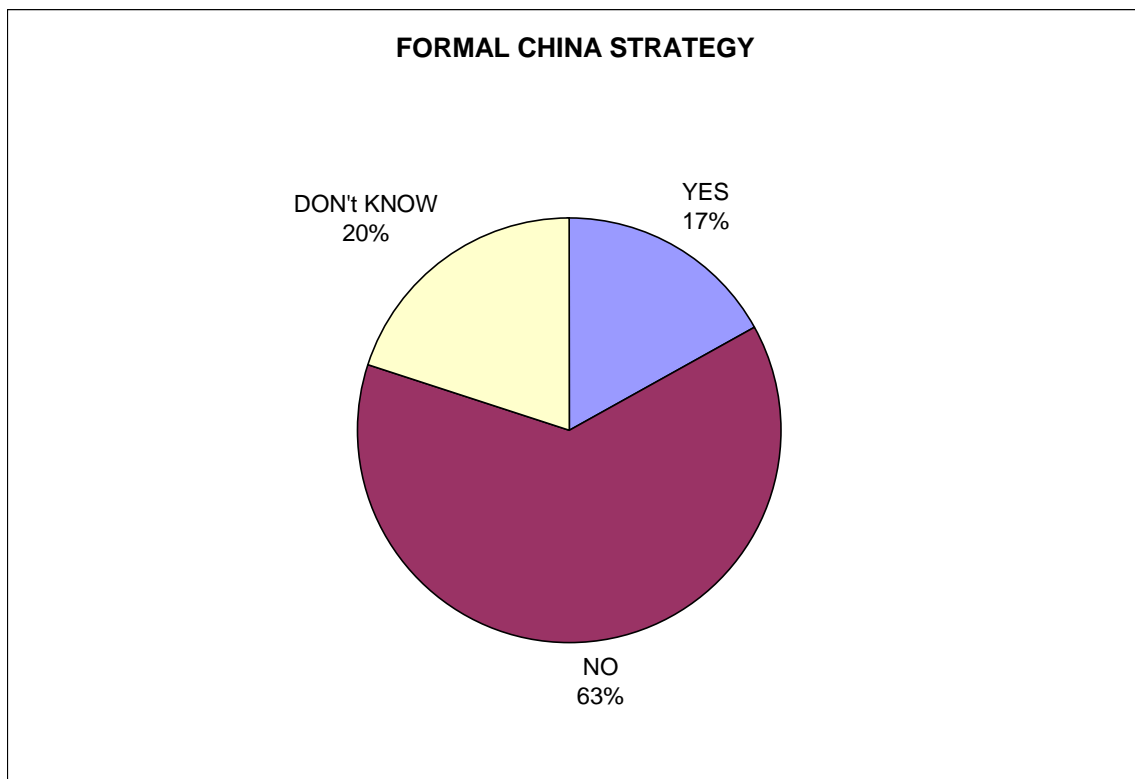


2.3 Preparing for China

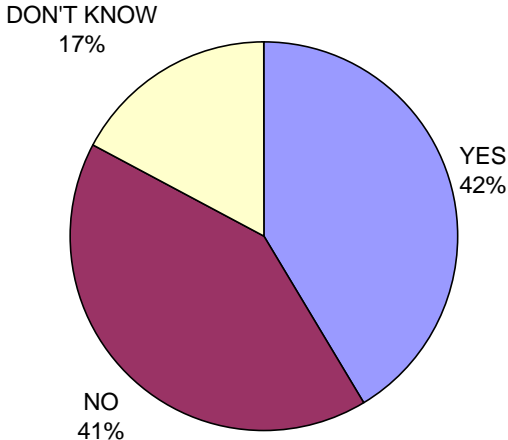
China Strategy

As important as China has become as a threat or as an opportunity to Canadian manufacturers and exporters, only 17% of all respondent companies report that they have a formal China strategy. However, among those companies currently doing business with China, the proportion having a formal China strategy increases to 42% and to 37% for those seeing China as more of an opportunity.

Whether or not companies have a China strategy also varies by primary markets and size of the companies. Nearly 42% of Canadian companies whose market is global have a China strategy and over 20% of those whose primary market is North America have such a strategy. Very few of those targeted at the Canadian market or local market have a China strategy. Larger companies are more likely to have a China strategy than their smaller counterparts.

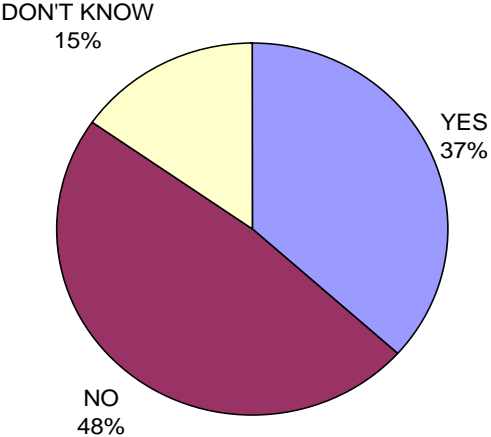


FORMAL CHINA STRATEGY IF DOING BUSINESS WITH CHINA



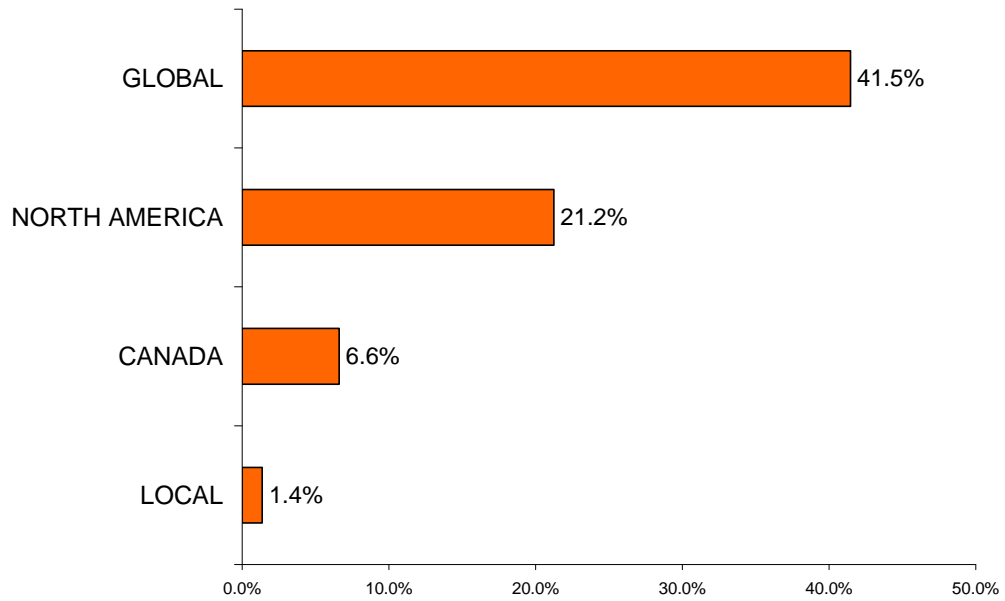
Pr<.001; n=338

FORMAL CHINA STRATEGY IF SEEING CHINA AS MORE OF AN OPPORTUNITY



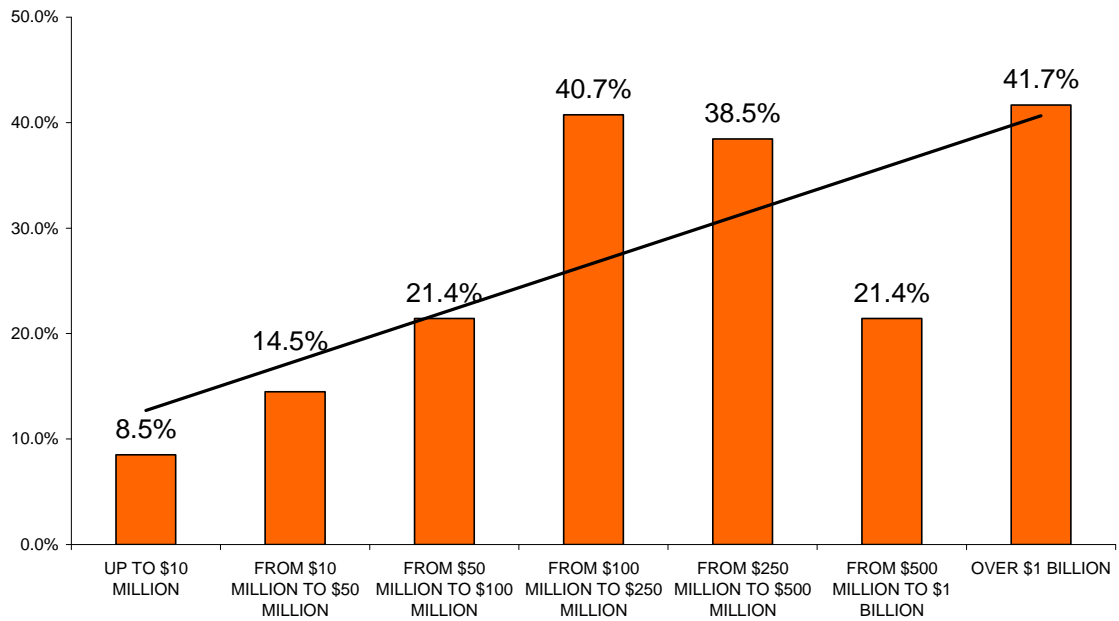
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COMPANIES HAVING CHINA STRATEGY BY PRIMARY MARKET



Pr<.001; n=908

COMPANIES HAVING CHINA STRATEGY BY SIZE



Pr<.001; R² = 0.5544; n=886

Strategy Objectives

Among those companies that have developed a China strategy, 66% say that their objective is to maintain global competitiveness and 65% say that they want to gain access to the Chinese market. China is also important in business strategies to lower production costs, outsource products and materials, diversify markets, and follow the moves of customers or suppliers.



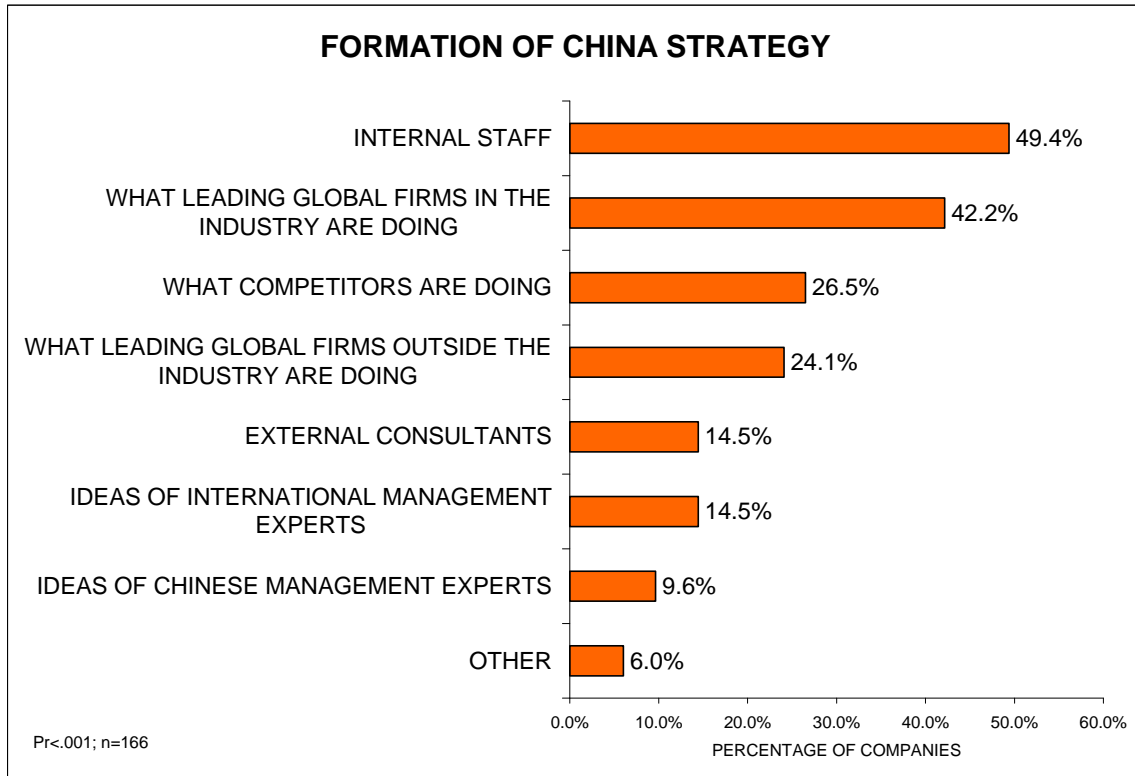
Components of China Strategy

The five most important components of the strategies of those companies that have developed formal business plans with respect to China are cost reduction, outsourcing, the need to move to higher value products, the need to develop partnerships with Chinese firms, and understanding political risk.



Formation of China Strategy

China strategy is primarily an internal initiative. Nearly half of respondent companies report that the idea of having a business plan for China comes from internal staff. What leading global firms are doing and what competitors are doing with regard to China also have impacts on the company's China business plan.

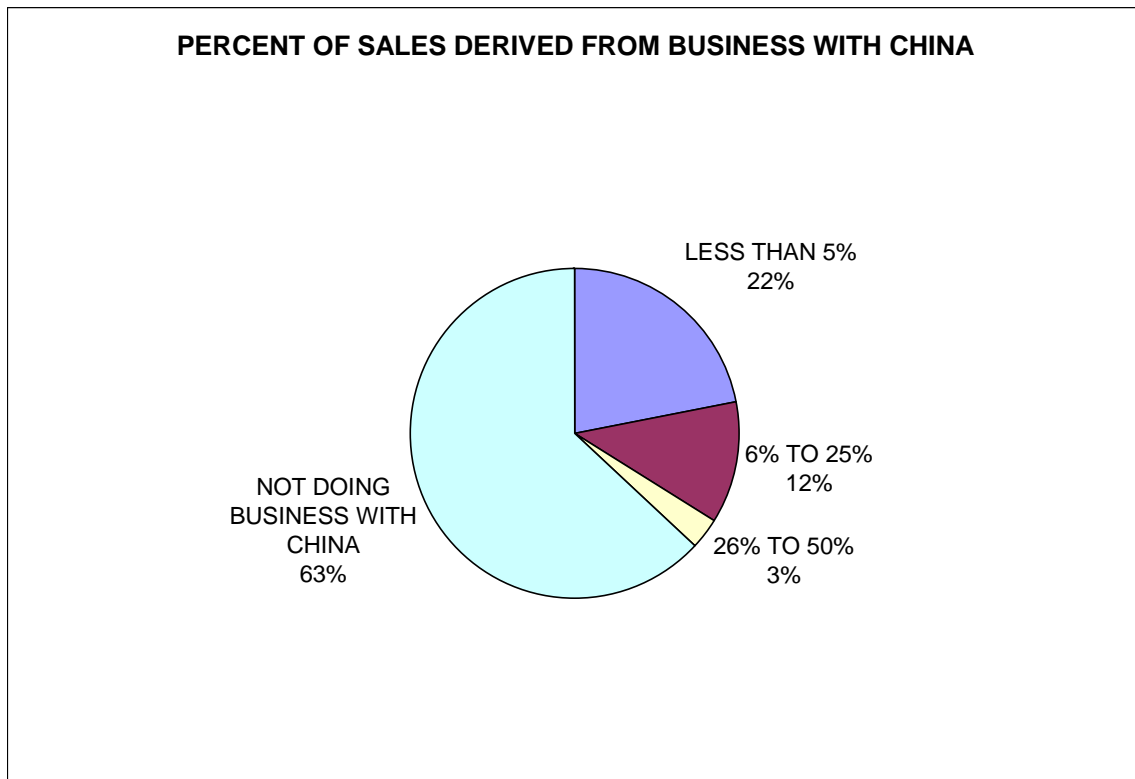


Effects of China Strategy

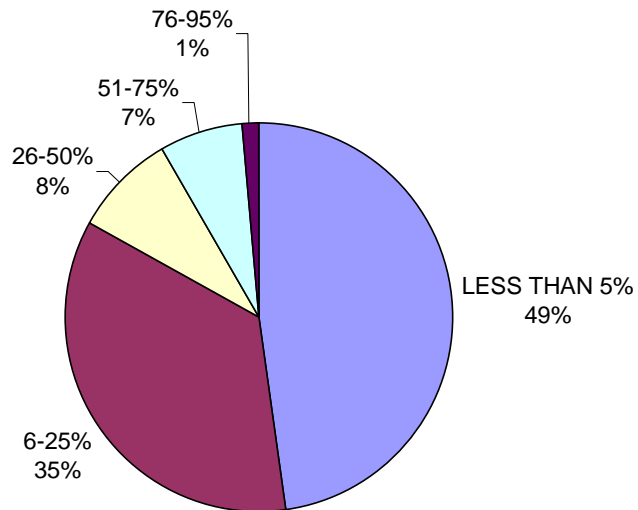
In general, China still accounts for a small proportion of the total revenues earned by Canadian manufacturers and exporters. With 63% of companies reporting that they do not do business with China at all, 22% report that China accounts for less than 5% of their total revenues. Another 15% of companies say that up to half their total revenues are derived from their China business.

Having a China strategy makes a difference. Nearly 8% of those with a China strategy report that China accounts for over half of their total revenues. Another 43% of companies say that up to half of their total revenues are derived from their China business, while nearly half of the companies report that China accounts for less than 5% of their total revenues.

Companies having a China strategy are more optimistic about their business outlook than those not having a China strategy.

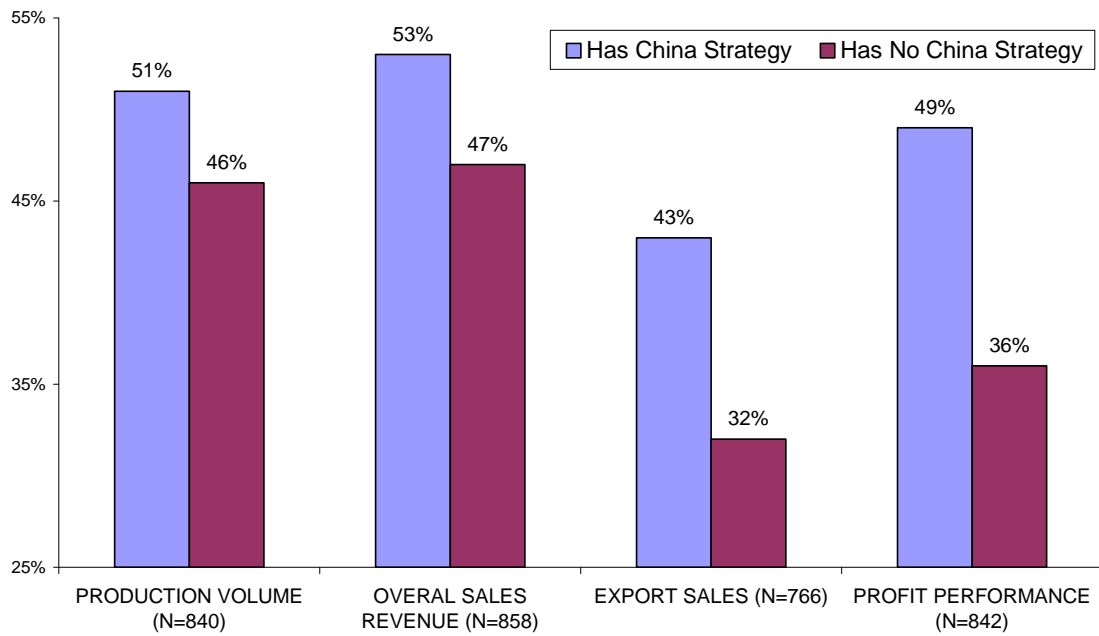


**PERCENT OF SALES DERIVED FROM BUSINESS WITH CHINA
IF HAVING A CHINA STRATEGY**



Pr<.01; n=142

BUSINESS OUTLOOK BY COMPANIES WITH/WITHOUT CHINA STRATEGY

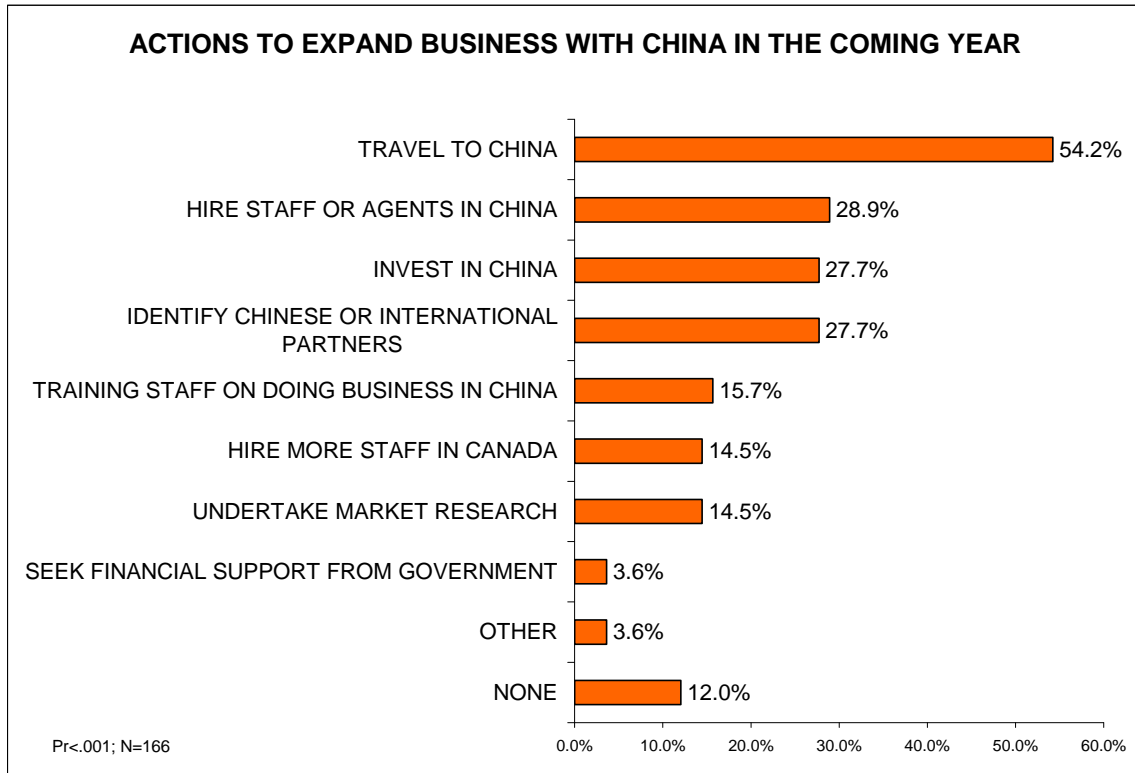


Pr<.001

PERCENTAGE OF COMPANIES SAYING BETTER IN 2007 VS. 2006

Next Steps Implementing China Strategy

Among those companies that have developed a China strategy, making more visits to China is the most common action that Canadian companies are considering in order to expand business with China in the coming year. Hiring local staff and agents in China, investing in China and identifying the right Chinese or international partners are also among the second-tier actions for expanding business with China.

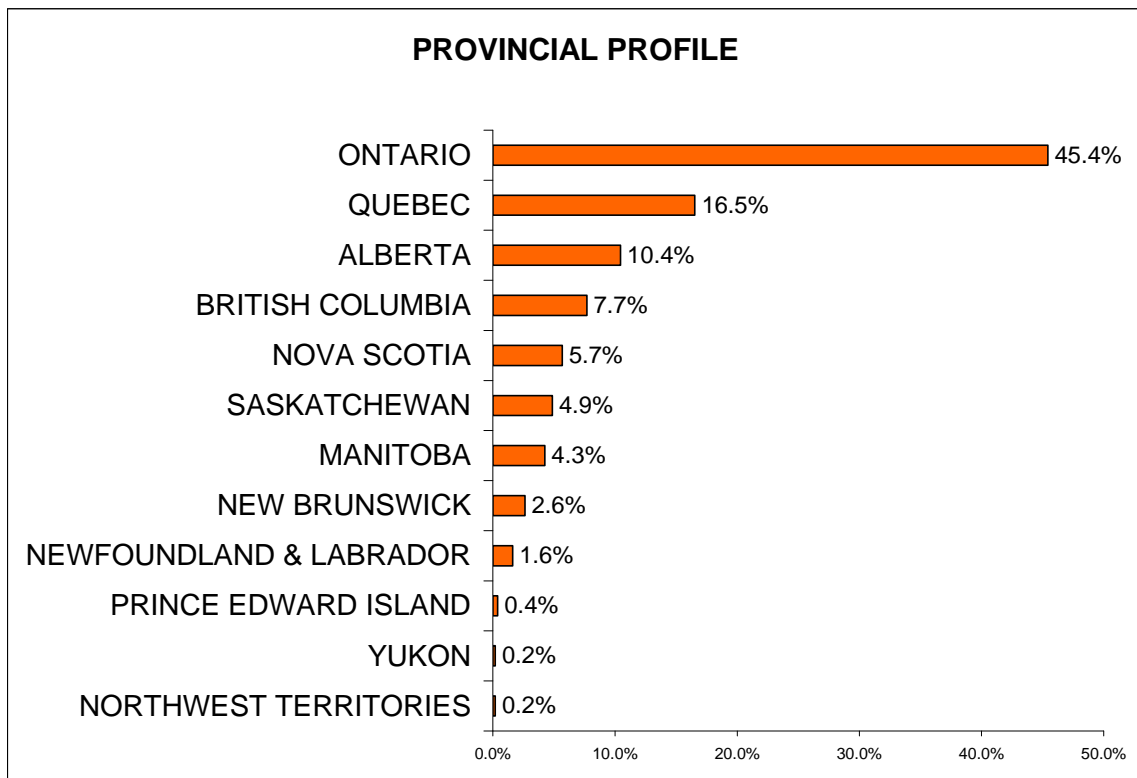


3. Description of Sample

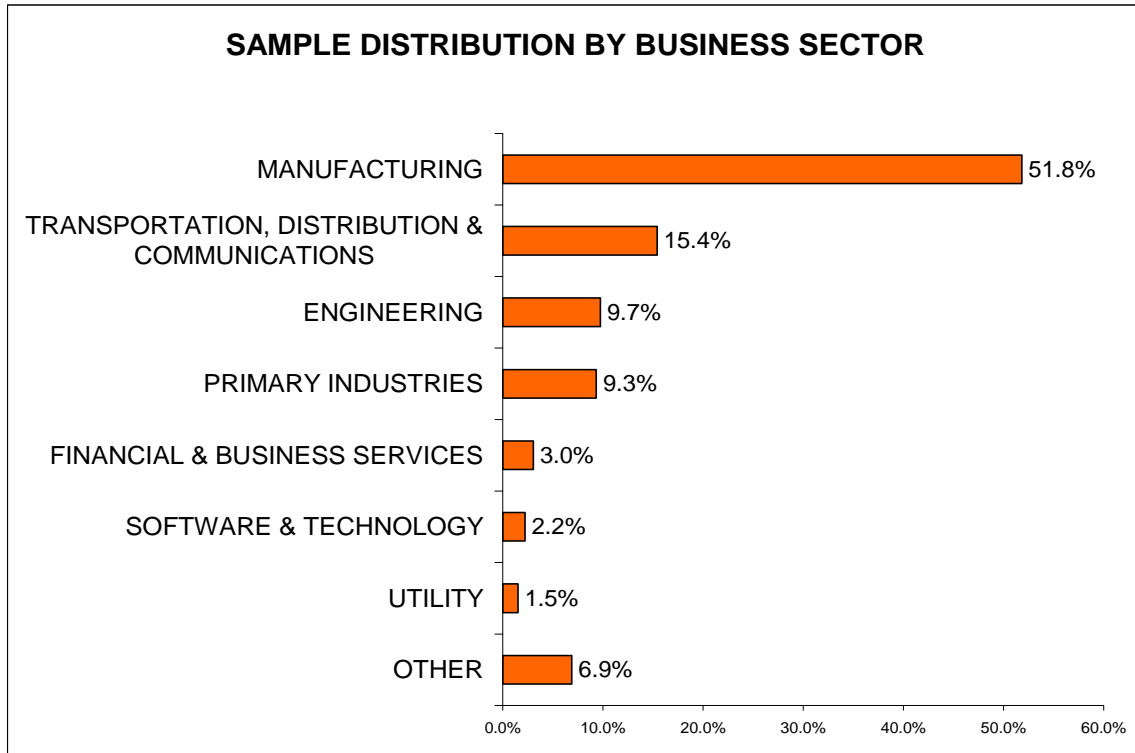
Sample Size

The samples are drawn from the CME membership representing all sectors of Canada's manufacturing and exporting community and every province. Together, CME's membership accounts for an estimated 75% of total manufacturing production and 90% of Canada's exports. There are 986 companies that provided valid responses to the survey, and the results are accurate within 3.5 percentage points 19 times out of 20.

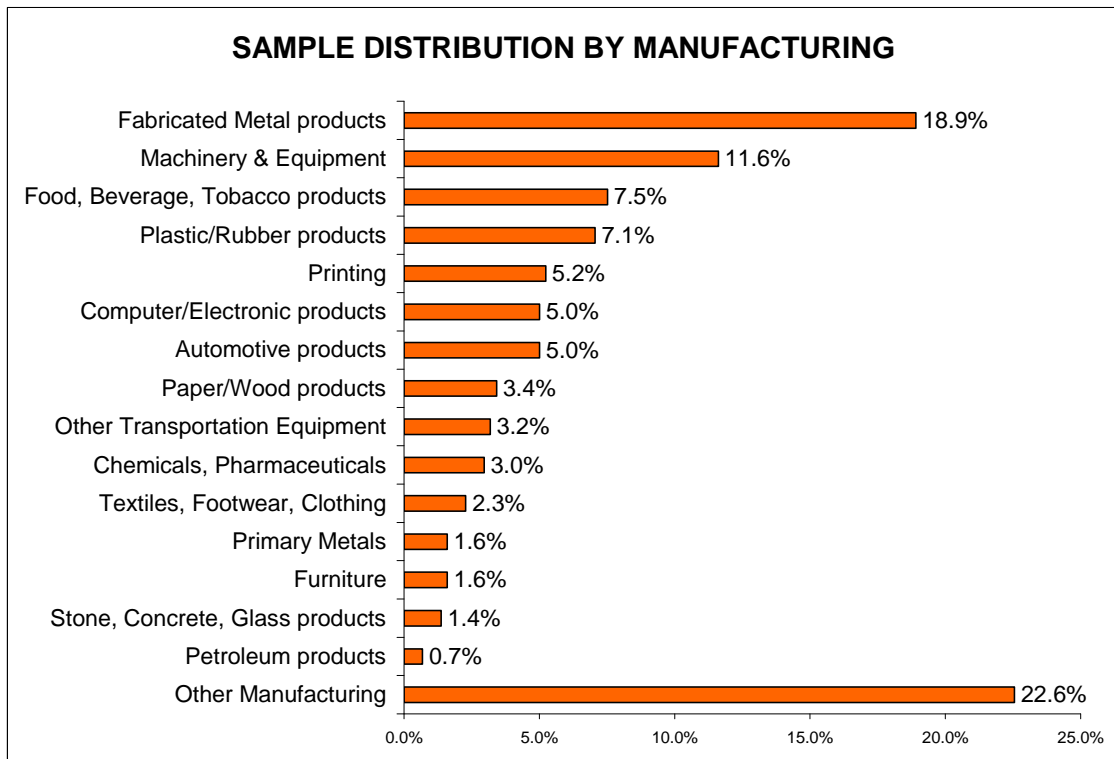
Business Location



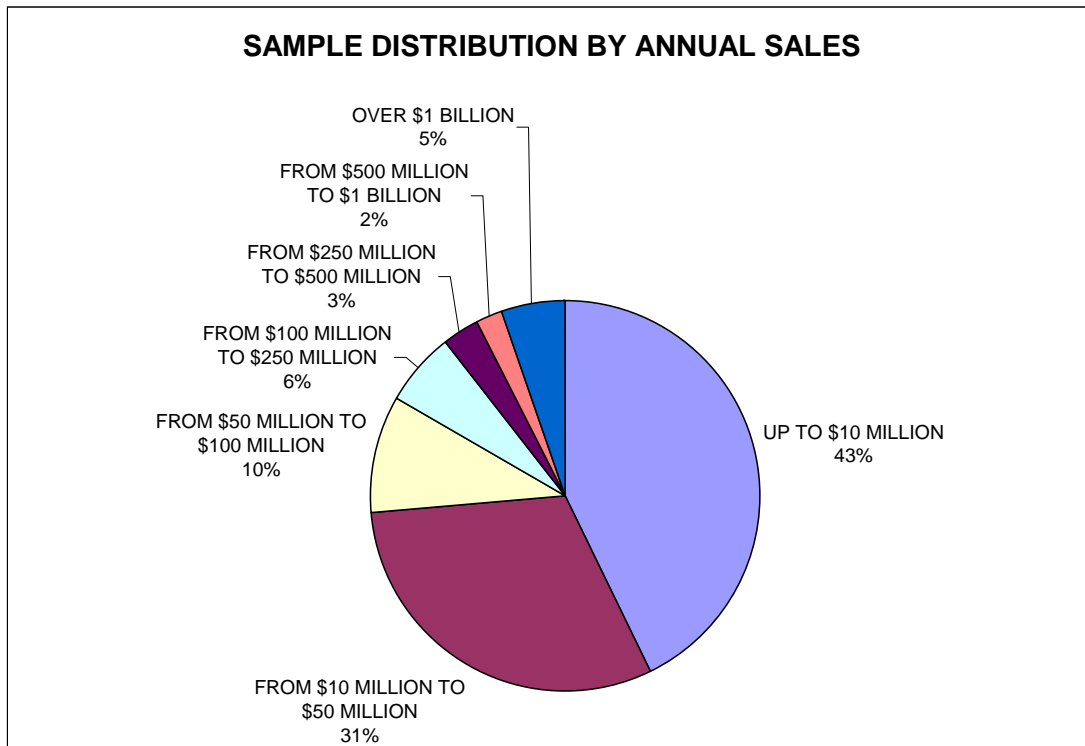
Business Sector



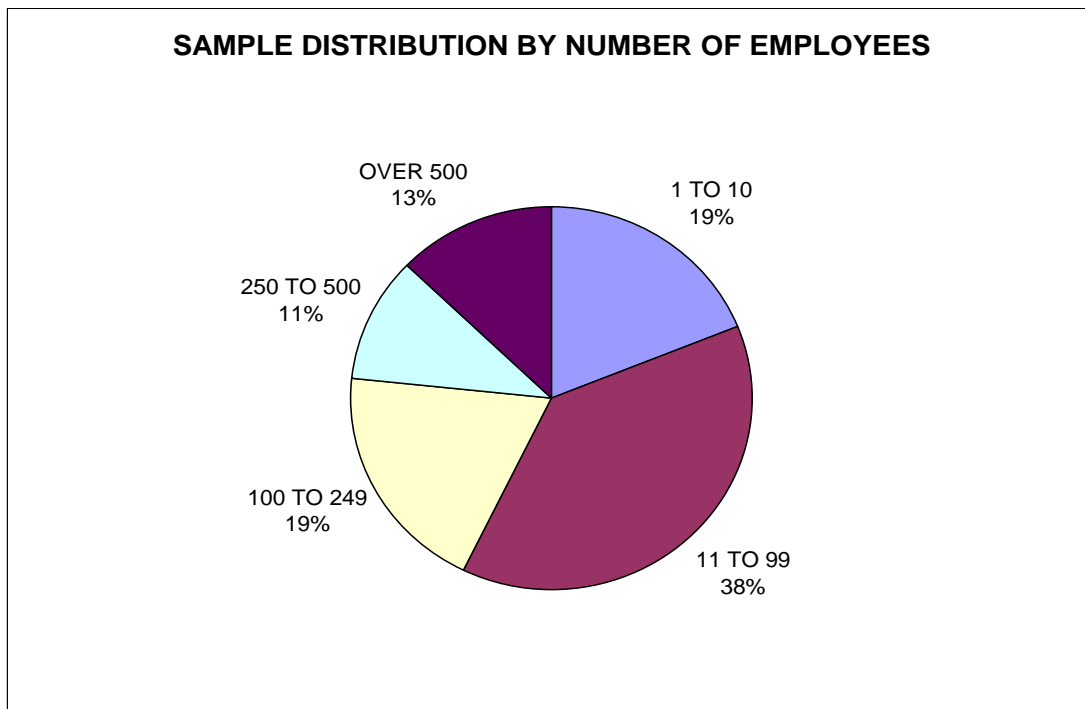
Profile of Manufacturers



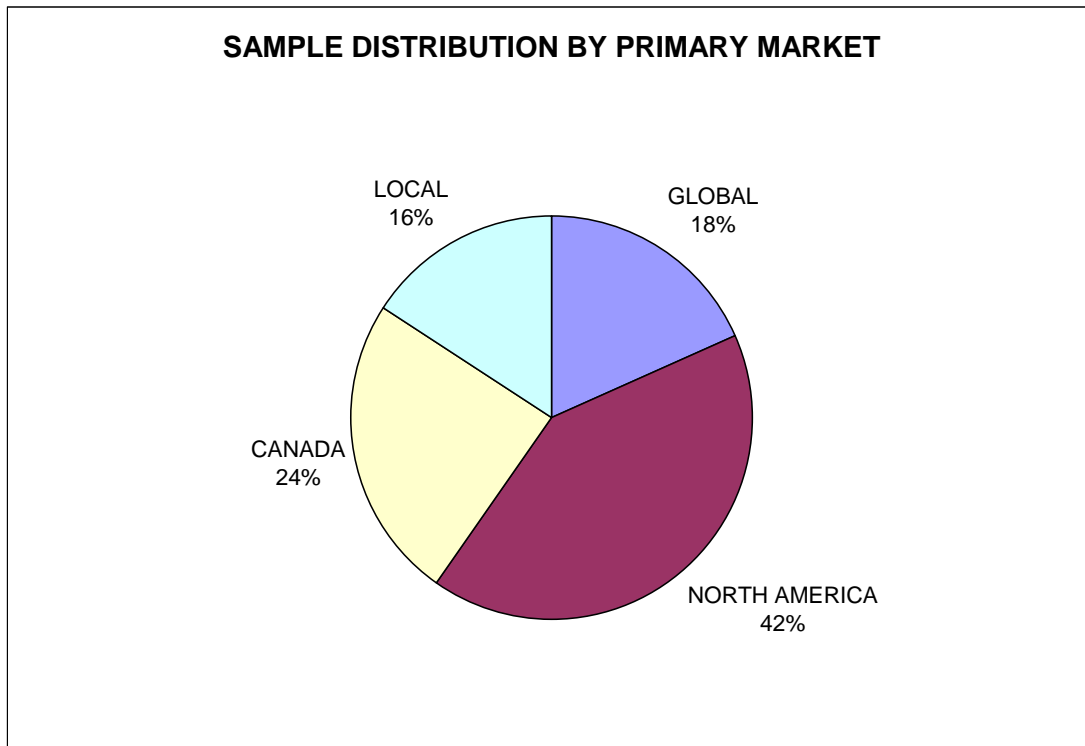
Business Size: Annual Sales



Business Size: Employees



Primary Market



Ownership Structure

