

SCI China Market Update – February 2014

Dear Friends,

China is celebrating the Year of the Horse with weeklong holidays but has reduced the quantity of fireworks so as not to aggravate the already choking air pollution. Chinese Central Television's Spring Festival Gala is a four-hour variety show. The gala features “wholesome family entertainment” - with a not-so-subtle patriotic message. There were more than 700 million people watching the show around the globe including us in Philadelphia. Today’s satellite TV and internet technology make this fairly easy to do. The Year of Horse officially began on January 31st. Happy Year of Horse!

The horse is one of China’s favorite animals. It provided reliable transportation for people before the automobile – which was not very long ago. So, traditionally, the horse has been a symbol for both traveling and speedy success. The Chinese love horses. Besides names like Gu and Li and Zhang, you may often hear the family name of “Ma” as well. Ma in Chinese characters means horse. Horses like to compete. They pursue freedom with passion and leadership. Most Chinese don’t use horses for farm work. Instead they use the ox. This is because Chinese have higher expectations for horses. Horses can help humans to win battles. Sitting on horseback implies that the person is from a noble or high ranking family. So people born in the Year of the Horse (it is said) tend to care about how they appear in the world – their dress, demeanor and speech.

Much like we celebrate Thanksgiving and Christmas here, The Chinese New Year means family get-togethers. That is the top priority for all Chinese whenever possible. This year a total of 3.6 billion trips are expected to be made during the Chinese New Year holiday as workers head home in the world's largest human migration and return. Officials anticipate 200 million more journeys will be made than last year and warn there will be significant strain on the transport system, with some travelers as usual struggling even to get a ticket. The railway system is expected to see 258 million passenger trips, up 7.9 percent from a year ago.

China’s huge population is often a big problem for Beijing - transportation, job opportunities, education, health care, power supply, food supply, water supply, retirement social benefits, and..., you name it. How to keep the world’s largest nation relatively stable and content? And this “problem” is also why China’s 1.3 billion population means great market opportunities for companies like GM, Ford, Apple, Starbucks, Wal-Mart, GSB, McDonald, Pizza Hut, Coke, Budweiser, Disneyland, Hollywood, “Ivy League” universities, United Airlines, Holiday Inn and thousands more U.S. companies. This year will provide new opportunities for many U.S. businesses, but things also continue to change fast in

China. It's not the same place that it was even a few years ago. We wish all our friends the best of luck in the Year of the Horse! Below is some of the latest news from various sources for your information.

China's economy grows 7.7 percent in 2013

China's economic growth decelerated in the final quarter of 2013 and appears set to slow further, adding to pressure on its leaders to shore up an expansion as they try to implement sweeping reforms. The world's second-largest economy grew by 7.7 percent over a year earlier, down from previous quarter's 7.8 percent, data showed Monday.

China's growth still is far stronger than the United States, Japan, or Europe. But an unexpectedly abrupt decline from the blistering double-digit rates of the previous decade has raised the risk of politically dangerous job losses and increases the challenges faced by the ruling Communist Party as it tries to rebalance the economy away from reliance on trade and investment.

China's manufacturing index falls in January

China's official gauge of its manufacturing sector slipped to a five-month low in January, confirming a slowdown in factory activity in the world's second largest economy. The monthly purchasing managers' index (PMI) declined to 50.5 in January after recording 51 in December and 51.4 in November, according to the government's National Bureau of Statistics and the China Federation of Logistics and Purchasing. Any figure above the 50 mark indicates expansion of manufacturing activity while anything below that signals contraction.

All major components of the PMI index, from new orders to production, declined, indicating downward pressure on the economy, state news agency Xinhua reported. The decline "could be largely due to the (Spring) festival effect," ANZ bank said in a note, referring to the annual Chinese lunar new year holiday when millions of migrant workers down tools and return to their homes.

China's industrial profit up 12.2% in 2013

Chinese industrial businesses saw their profits rise 12.2 percent year on year in 2013 according to Beijing's official data. Total profits of industrial companies with annual revenues of more than 20 million Yuan (\$3.28 million) reached 6.28 trillion Yuan in 2013, the National Bureau of Statistics said in a statement. The growth rate was higher than that in 2012, but lower than that in 2011. The companies' profits rose a mere 5.3 percent in 2012, compared with the 25.4-percent surge registered in 2011. In December 2013 alone, those companies' combined profits climbed 6 percent year on year to 942.53 billion Yuan. The monthly growth, however, was 3.7 percentage points lower than that in November.

Foreign direct investment in China rebounds 5.3% in 2013

Overseas investment into China rose 5.3 percent last year, bouncing back after declining in 2012 for the first time in three years. Foreign direct investment (FDI), which excludes financial sectors, totaled \$117.59 billion last year, the commerce ministry said. The figure is up from the \$111.72 billion posted in 2012, when it skidded 3.7 percent in the face of economic weakness in developed markets and a growth slowdown at home.

8.8% salary hikes expected for 2014

Salary increases are expected to hit 8.8 percent in 2014, a slight rise on the 8.6 percent for 2013, according to a survey issued by 51job.com, a human resources service provider. More than 3,400 enterprises and 4,600 employees were interviewed in the survey from September to November 2013, covering sectors including real estate, high-tech, consumer products, and manufacturing. It found that the highest salary increases occurred in the financial sector, reaching 10.4 percent, followed by real estate (10.1 percent), high tech (9.9 percent), and bio-pharmaceuticals (9.2 percent).

Although enterprises try to increase salaries to retain expertise, the attrition rate reached 16.3 percent in 2013, from 16.7 percent in 2012, according to the report. The traditional service and manufacturing industries have the highest attrition rates, of 19.4 percent and 19.1 percent. The survey showed that about 54 percent of Chinese employers said their salary increase will reach 6 to 10 percent, and 12 percent of employers said their pay rise will exceed 10 percent. China will see the strongest salary growth among all Asian countries in 2014, even though the nation's economic growth rate has been slowing down.

Chinese become world's top tipplers of red wine

China has overtaken France and Italy to become the world's number one consumer of red wine, although the United States remains the world's biggest tippler of all types of wines, the wine and spirits trade association VINEXPO said recently. China drank 1.865 billion bottles of red wine last year, or in trade terms 155 million nine-liter cases, contributing to a 136 percent increase in consumption over five years. That beat France into second place for red wine and Italy into third, VINEXPO said, based on figures compiled by the London-based International Wine and Spirit Research firm.

Google sells Motorola Mobility unit to Lenovo for \$3bn

Google has sold struggling US mobile phone company Motorola Mobility to Chinese computer maker Lenovo for \$2.91bn (£1.8bn), in a surprise move. Google had paid \$12.5bn for the company less than two years ago. Lenovo plans to build up its smartphone unit through the Motorola purchase, which may help offset its slowing personal computer business. However, Google will keep the majority of Motorola's lucrative patents, which include one for Android software.

This is the second major acquisition for Lenovo in the same number of weeks. Last Thursday, the Thinkpad-maker announced it had acquired IBM's low-end server business for \$2.3bn, in what was then China's biggest technology deal.

China now has half a billion mobile web users, 618 million total internet users

China now has 618 million internet users and 500 million mobile web users, according to new figures today from the China Internet Network Information Center (CNNIC). The new numbers from CNNIC are for December 2013.

France Total to invest \$4b in coal chemical project

France's Total SA, an international oil and gas company, confirmed it has received approval from the Chinese government to invest \$4 billion in a coal chemical project in the Inner Mongolia autonomous region, according to Reuters. In an effort to reduce the country's reliance on oil imports, the petrochemical project of the French oil giant together with China Power Investment Corporation, one of the five largest State-owned electricity producers, will convert China's rich coal into gas and generate raw materials for plastic production.

China world's largest auto production site in 2013

China became the world's largest auto production site in 2013 with the most dynamic growth, a Frankfurt-based institute said recently. Of the 82.5 million light vehicles produced globally last year, 18.7 million, 22.7 percent, were driven out of factories in China. Auto production in China saw an increase of 12 percent in 2013, the most dynamic growth around the world, PricewaterhouseCoopers (PwC) Germany said in a report.

Tesla has announced the price of the Model S in China, and it's much lower than expected

Tesla, the electric car company founded by Elon Musk, just announced that its Model S vehicle will retail for RMB 734,000 (about \$120,00) in China.

That's much lower than many observers expected – upon the opening of Tesla's showroom in Beijing last November, China Daily reported that company reps estimated the car would likely be priced between \$146,000 and \$195,000. For comparison's sake, in the US, the Model S retails for the base price of \$81,070.

What's the significance here? International cars will always retail for more in China than in domestic or Western markets, partly due to taxes, and partly due to their perceived status as luxury goods (also, the cars' target demographic in China is likely wealthier than the target demographic in developed markets). The Mercedes S 400 Hybrid, for example, retails in the US at the sticker price of about

\$90,000, while the same model in China sells for over RMB 1.4 million (about \$230,000), according to the official website for Mercedes China.

In a lengthy blog post, Tesla lays out the math and claims that other than shipping costs, import taxes, and value-added taxes, the company imposes no market-specific markup on the Model S for China. It adds: 734k CNY is a big risk for Tesla. We know it's unconventional. We know we could charge more. We know that our competitors will try to convince Chinese consumers that our relatively lower price tag means the Model S is a lesser car, when the real reason their car costs more is that they make double the profit per car in China compared to the United States or Europe.

Samsung SDI signs deal to build e-car battery factory in China

Samsung SDI said that it had signed a preliminary deal to build an electric car battery factory in China, betting on the growth potential of the country's electric car market. Samsung SDI also said it will form a joint venture by April this year to invest a total of \$600 million in the factory and other electric car battery businesses over the next five years. Samsung SDI said the joint venture consists of Chinese parts maker Anqing Ring New Group and an unidentified company owned by China's Shaanxi province.

China faces PX shortage in 2014

China will see a wider shortage of paraxylene (PX) supply in 2014, a research report warned recently. The supply gap will be up to 9.5 million tons in 2014, said a report by the economics and technology research institute under the China Petroleum and Chemical (Sinopec) Corp, the State-owned oil refining giant. The domestic PX industry managed to meet only 47 percent of China's demand for PX in 2013. China's PX demand topped 16.41 million tons in the 12 months, up 18.5 percent year on year, while imports of the chemical hit 8.7 million tons, up 42 percent year on year, the report said.

Construction to add PX production capacity has proven difficult. The self-sufficiency rate has been dwindling due to improving public awareness on environmental protection and inefficient communication of information on proposed plants, said Luo Hongjing, a researcher with the institute. Since 2007, PX projects planned in Xiamen, Dalian, and Kunming have been shut down after residents took to the streets in protest, as they believed the facilities would threaten the local environment. China is the world's largest PX producer, accounting for about a quarter of the global PX production capacity, according to the report. PX is a major raw material for making polyester products. Traditionally, PX production lines are attached to petrochemical engineering projects.

Beijing to build 16 water reclamation plants in 2014

Beijing will begin construction on 16 new water reclamation plants this year to ease the thirsty capital with a stable "second water source," said water authorities on Saturday. In addition to the 16 projects, Beijing will complete another 14 under-construction reclamation plants, said Jin Shudong, director with the Beijing Water Authority.

Beijing will make efforts to upgrade the quality of reclaimed water with low-noise and non-polluting processing technologies, he said. To date, there are already 16 reclamation plants in Beijing. It is estimated that the consumption of reclaimed water in the city will reach 860 million cubic meters in 2014. Use of reclaimed water supports the sustainable development of the Chinese capital by effectively reducing fresh water consumption. In 2013, Beijing used a total of 3.6 billion cubic meters of water, including 800 million cubic meters of reclaimed water.

For more information about today's China market and opportunities, please visit our website at www.s-c-i.com or call me at the number below, or Dr. Tim Weckesser at 610-828-8060.

Best regards,

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