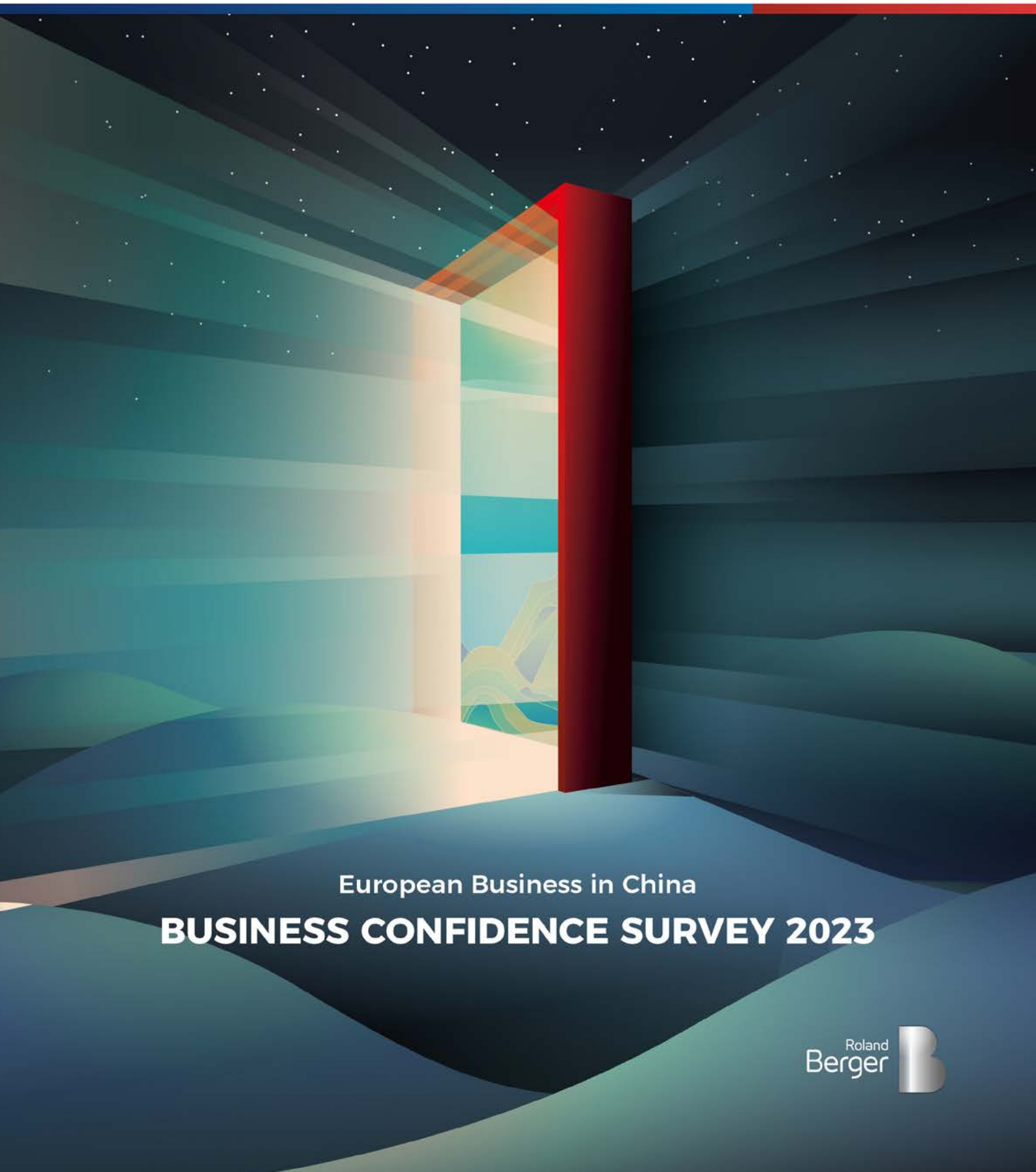
European Chamber
中国欧盟商会



European Business in China

BUSINESS CONFIDENCE SURVEY 2023

Roland Berger

EMBARGOED

European Union Chamber of Commerce in China

www.europeanchamber.com.cn

The information contained herein is based on input and analysis from February to May 2023.

The information is provided for informational purposes only and should not be construed as business or legal advice on any specific facts or circumstances. No users of this report should act or refrain from acting on the basis of any content included without seeking appropriate professional advice.

The European Union Chamber of Commerce in China does not assume any legal liability or responsibility for the accuracy and completeness of the information provided in the report.

© 2023 European Union Chamber of Commerce in China, all rights reserved. This study may not be reproduced either in part or in full without prior written consent of the European Union Chamber of Commerce in China.

Cover image © Harry Zhang, European Union Chamber of Commerce in China, all rights reserved.

TABLE OF CONTENTS

EXECUTIVE SUMMARY..... 1

1 DOING BUSINESS GETS MORE DIFFICULT AS BOTTOM LINES TAKE A HIT.....3

1.1 Record number report doing business in China became more difficult year-on-year.....3
1.2 Company revenues take a hit following a difficult 2022 4
1.3 Profitability down.....7
1.4 Importance of China for global profits falls.....7
1.5 Companies less optimistic about China's growth prospects.....8

2 MOUNTING CHINA CHALLENGES PROMPT EU BUSINESSES TO LOOK ELSEWHERE.....9

2.1 The top post-zero-COVID business challenges 9
2.2 Investments begin to shift out of China as de-risking strategies emerge.....10
2.3 Decrease of China expansion plans 12
2.4 One in 10 moving HQs out of Mainland China 13

3 DECOUPLING INTENSIFIES: COMPANIES LOCALISE AND SILO OPERATIONS.....14

3.1 HQ and China operations decoupling.....14
3.2 Some businesses localise to manage risks 15
3.3 Exodus of foreign nationals continues.....16
3.4 Supply chain strategies continue to evolve 17
3.5 More Chinese suppliers and customers move operations to other markets.....19
3.6 New EU and third-party regulations drive change.....20

4 ONE STEP FORWARD, ANOTHER STEP BACK: MIXED PROGRESS WITH MARKET ACCESS AND REGULATORY BARRIERS..... 25

4.1 Lost business due to market access and regulatory barriers highest on record.....25
4.2 Baby steps in market opening.....29
4.3 More investment waiting on increased market access.....31
4.4 Playing field becomes slightly more level.....33
4.5 Compelled technology transfers increase.....35
4.6 Effectiveness and enforcement of intellectual property rights laws and regulations remain a concern.....36

5 POLITICS CONTINUES TO SPILL OVER INTO BUSINESS.....37

5.1 Business became more politicised (again).....37
5.2 Politicisation of consumer demands.....39

6 GOVERNMENT ACTION NEEDED FOR EU FIRMS TO CONTRIBUTE FULLY TO CHINA'S 30/60 GOALS 40

6.1 European firms prioritising decarbonisation.....40
6.2 How European companies are achieving carbon neutrality.....41
6.3 Achieving 30/60 Goals requires immediate government action.....42

7 ABBREVIATIONS 45

8 ABOUT THE SURVEY MOTIVATION AND DESIGN 46

9 ABOUT ROLAND BERGER.....47

10 ABOUT THE EUROPEAN UNION CHAMBER OF COMMERCE IN CHINA.....48

EMBARGOED

TABLE OF FIGURES

Figure 1: Two thirds report doing business in China became more difficult....3
Figure 2: Doing business became more difficult across the board....4
Figure 3: Record number report revenue decreases....5
Figure 4: Revenue by industry: Mixed results....6
Figure 5: SME revenues acutely impacted....6
Figure 6: Profitability takes a hit....7
Figure 7: Percentage China contributes to companies' global EBIT margins declined....7
Figure 8: Outlook on growth deteriorates....8
Figure 9: Chinese and global economic slowdowns replace COVID-19 as top challenges faced by business....9
Figure 10: One in 10 shift current investments elsewhere, with ASEAN their top choice followed by Europe....10
Figure 11: Investments shifted predominantly for defensive reasons....11
Figure 12: Importance of China as an investment destination decreased....11
Figure 13: Attractiveness of China as an investment destination varies by sector....12
Figure 14: Less than half consider expanding their China operations....12
Figure 15: Increase in cost-cutting....13
Figure 16: One in 10 to move HQs out of China....13
Figure 17: More than a quarter report decoupling....14
Figure 18: The impact of decoupling....15
Figure 19: Staff, IT infrastructure and data storage, and supply chains all localised in last five years....15
Figure 20: 16% of members employ no foreign nationals in China....16
Figure 21: Decrease of foreign nationals comes at a cost....17
Figure 22: More than three quarters re-evaluating China supply chains....17
Figure 23: Many supply chains already shifted out of China....18
Figure 24: Companies review supply chain strategies to build resilience and save costs....18
Figure 25: Majority import critical components that they cannot easily replace....19
Figure 26: Four in 10 witnessed Chinese suppliers and/or customers move operations out of China....19
Figure 27: 44% expect EU's CSRD to impact China operations....20
Figure 28: One in five expect to be impacted by US export control policies....21

EMBARGOED

Figure 29: US' Uyghur Forced Labor Prevention Act to present a challenge for a minority.....21
Figure 30: 16% concerned by lack of ability to conduct independent third-party audits, 40% unsure.....22
Figure 31: Alarming number miss business opportunities as a result of market access and regulatory barriers 25
Figure 32: Members face market access and regulatory barriers across the board.....26
Figure 33: More regulatory obstacles expected.....27
Figure 34: Ambiguous regulations and unpredictable legislative environment top regulatory obstacles.....27
Figure 35: The top regulatory obstacles by sector (part 1).....28
Figure 36: The top regulatory obstacles by sector (part 2).....28
Figure 37: Market access restrictions faced by a third.....29
Figure 38: Market creaks open for some, closes for others.....29
Figure 39: Big fish welcome, small fry kept at arm's length.....30
Figure 40: More than a quarter see no chance of meaningful market opening.....30
Figure 41: Market access prospects vary substantially from sector to sector.....31
Figure 42: Majority would likely increase investments with more market access.....32
Figure 43: Over a fifth willing to increase investment by more than 10% of annual revenue 32
Figure 44: 60% say playing field is level.....33
Figure 45: Equal treatment varies greatly by sector 34
Figure 46: Where European companies experience differentiated treatment.....34
Figure 47: Enforcement of environmental regulations remains uneven.....35
Figure 48: One in six compelled to transfer technology.....35
Figure 49: Majority of compelled technology transfers occurred post-FIL.....36
Figure 50: Almost half find enforcement of IPR laws and regulations inadequate 36
Figure 51: Majority report increased politicisation in last 12 months.....37
Figure 52: Chinese Government and media top sources of politicisation.....38
Figure 53: Politicisation of business expected to continue.....38
Figure 54: More than a quarter note consumer demands becoming more politicised.....39
Figure 55: Majority of European companies decarbonising China operations.....40
Figure 56: Majority aim to decarbonise before 2050.....41
Figure 57: Decarbonising energy use and decreasing energy demand top strategies.....42
Figure 58: Companies face a wealth of decarbonisation-related barriers 43
Figure 59: Urgent need for government action if 30/60 Goals to be achieved.....44

EMBARGOED

EXECUTIVE SUMMARY

Since China abruptly ended its 'zero-COVID' strategy in late 2022, Chinese officials have been on a charm offensive in an attempt to restore the country's allure as an investment destination. However, as the results of the *Business Confidence Survey (BCS) 2023*—conducted from February to early March 2023, after the abandonment of 'zero-COVID'—illustrate, this will be no easy task. The deterioration of business sentiment that has taken place over the last three years has been significant and cannot be reversed overnight.

European companies have already shifted some investments overseas: 11% of respondents—the same number that said they were *considering* shifting existing investments from China a year ago—report they have done so; and a tenth of respondents have already relocated, or plan to relocate, their Asia headquarters (HQs) away from the country. It is not just European companies that are diversifying their investments. Almost four in ten (38%) have witnessed Chinese customers and/or suppliers shift investments out of China as well. With business running on cycles, these investments will likely not return any time soon.

Faced with growing risks and a more volatile operating environment (a record-high 64% of respondents reported that doing business in China become more difficult in 2022),[1] European companies are still reassessing how many eggs to keep in their China basket. While few are leaving the country altogether, there is a 13 percentage point (pp) year-on-year (y-o-y) decrease in the proportion of respondents that rank the market as a top-three destination for *future* investments (55%, the lowest figure on record).[2] In addition, more than half (53%, +15pp y-o-y) of respondents have no plans to expand their China operations in 2023.

Long-standing challenges persist and continue to weigh on business confidence. Market access and regulatory barriers remain widespread, with 62% of respondents (+20pp y-o-y) reporting having missed business opportunities in 2022 as a result. Marginal progress was made in some areas, including in the number that reported a level playing field between foreign and Chinese enterprises (+7pp y-o-y). However, backwards steps were taken elsewhere: there were increases in the number that reported both experiencing market closing (+5pp) and being compelled to transfer technology (+3pp) compared to the 2022 survey.

Politics also continues to impact business. Nearly six out of 10 (59%, +9pp y-o-y) respondents reported that the business environment in China became more politicised over the past 12 months, and over a quarter (26%) have faced challenges stemming from consumer demands becoming politicised. These include conflicting calls from separate sets of customers to either maintain or cease operations in politically sensitive regions of China, and to produce goods containing either no China- or no United States (US)-made components, depending on which of the two markets the goods are bound for. The fallout from Russia's invasion of Ukraine has also changed how many view the China market, by forcing businesses to seriously consider if/how they may be impacted in the event of an escalation of tensions in the Taiwan Strait.[3]

As a result of China's more challenging and unpredictable business environment, European companies' investment and operational strategies are being adjusted accordingly. There is now an increasing focus on making operations more durable—for example, through localisation or diversification of supply chains—as opposed to capturing greater market share.[4]

A notable three out of four respondents have re-evaluated their supply chain strategies over the past two years, driven predominately by defensive considerations, such as the need to increase resilience (reported as a key driver by 64%); geopolitical-related factors (31%); and to mitigate the impact of domestic policy developments such as China's self-sufficiency drive (24%).

1 This question was first asked as part of the *Business Confidence Survey* (BCS) in 2014 and has been asked annually since.
2 This question was first asked as part of the BCS in 2010 and has been asked annually since.
3 For more information on the impact that Russia's invasion of Ukraine has had on how European businesses view the China market see: *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, p. 22 & p. 28, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>
4 Kratz, Agatha; Barkin, Noah & Dudley, Lauren, *The Chosen Few: A Fresh Look at European FDI in China,* pp.3-4, Rhodium Group, 14th September 2022, viewed 5th April 2023, <https://rhg.com/research/the-chosen-few/>

EMBARGOED

A sizeable proportion are taking steps to decouple their China supply chains from the rest of world: 12% have moved parts of them out of China already,[5] while nearly a quarter of respondents (24%) plan to onshore their supply chains at least partially into the country. With new and forthcoming European and US legislation set to compel many companies to demonstrate greater transparency in their China operations—a challenge given that it is currently not possible to conduct independent, third-party audits—and with businesses having to carefully monitor a growing list of sanctions and export controls, both Western and Chinese, the trend of supply chain diversification and divestment is likely to strengthen in the medium-term.

Meanwhile, the exodus of foreign nationals, an issue exacerbated by China's 'zero-COVID' policy, continued throughout 2022. Nearly one in six (16%, +5pp y-o-y) respondents report having no foreign nationals working in their China operations, a figure that jumps to 21% for small and medium-sized enterprises, many of which experienced severe difficulties getting staff into China over the past three years. This has been accompanied by an erosion of the soft infrastructure that is vital for maintaining a vibrant foreign community in China, with international schools and medical clinics finding themselves short of both staff and customers, putting many under pressure to close.

These factors all come at a considerable cost, with members reporting a reduced transfer of know-how, communication difficulties, and even a need to defer investments. The disconnect between company HQs and China operations risks further damaging confidence in the China market, precipitating a negative cycle of disengagement. These factors are also challenging the efficiency of multinational companies' traditional operating models—which have historically relied on their ability to capitalise on synergies between business units to build global economies of scale—as businesses are increasingly pushed to further localise and create divergent systems, with one for China and one for the rest of the world.[6]

Nevertheless, despite mounting challenges, it would be premature to rule out China's ability to respond positively, or underestimate the impact this would have on foreign investment in China. A majority of respondents (63%) report they would be willing to increase their China investments if market and regulatory barriers were removed. There also remains huge scope for strengthening European Union (EU)-China ties in areas such as trade in services, which is significantly below potential given the size of their respective economies.[7]

China would benefit enormously from taking further steps to make its business environment more favourable to private enterprises, both Chinese and foreign, much as it did by implementing previous economic reforms, particularly those that paved the way for its World Trade Organization accession. At the same time, European companies are forging ahead in strategically important areas, such as decarbonisation, and can be key partners to facilitate China's carbon neutrality goals, provided they are given a fair chance to do so.

With China now 'reopening' to the world, following three years of isolation, there is a window of opportunity for the government to demonstrate that the pro-business promises recently made by its leadership are more than just words. Deepening cooperation with the international business community in China would help to swiftly restore the Chinese market's efficiency, reliability and predictability—characteristics that were eroded over the last three years—and provide a strong foundation for sustainable, long-term economic recovery.

EMBARGOED

5 This figure refers to 12% of those that report having reviewed their supply chains, see Figure 23 for more information.
6 This is leading to a loss of efficiency. It could eventually result in a situation in which only very large European multinational companies, which are already very localised, will be able to continue competing in the China market, albeit while operating increasingly as Chinese companies with foreign shareholders.
7 For example, EU-US trade in services was over five-and-a-half times greater than EU-China trade in services in 2021. Calculation based on annual trade statistics for 2021 from: *EU Trade by Country/Region*, European Commission, viewed 9th May, <https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions_en>

1 DOING BUSINESS GETS MORE DIFFICULT AS BOTTOM LINES TAKE A HIT

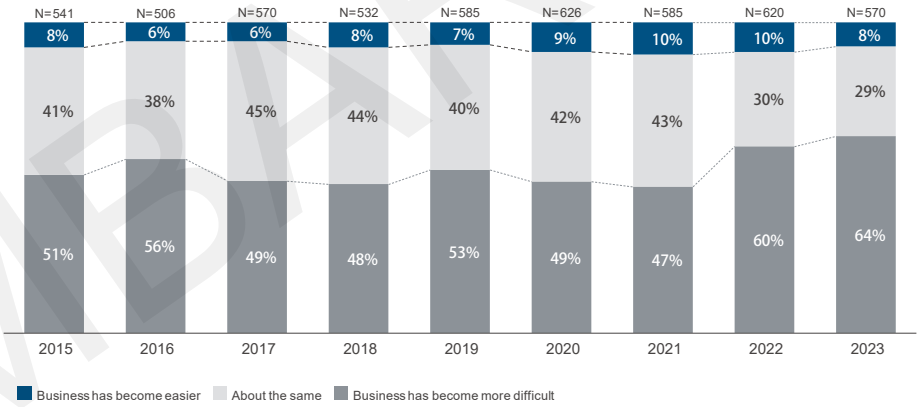
European firms found themselves operating in an even more challenging business environment in 2022. Revenue and profitability took a turn for the worst for many, as stringent COVID-19 containment measures disrupted operations and slowed China's economic growth.[8] The contribution of China revenues to companies' global revenues also decreased for a second year running, as much of the rest of the world returned to 'normality,' while the Chinese economy faced mounting headwinds.[9]

1.1 Record number report doing business in China became more difficult year-on-year (y-o-y)

Two thirds of respondents (64%, +4 percentage points (pp) y-o-y) reported that doing business in China became more difficult in 2022, the highest total on record.[10] By contrast, just 8% reported that doing business became easier y-o-y.

Figure 1: Two thirds report doing business in China became more difficult

How has your industry's business environment changed over the past year?



A majority of respondents in all industries surveyed reported that business became more difficult y-o-y, with the most pronounced results coming from medical devices (79%), automotive (73%), and transportation, logistics and distribution (73%).

For the medical devices industry, this was in no small part due to China's staunch protection of its domestic firms. Throughout the COVID-19 pandemic, the Chinese Government continued to provide direct financial support, tax benefits and research and development (R&D) support to local firms, while maintaining opaque approval processes and its centralised volume-based procurement (VBP) directive, to the detriment of foreign companies.[11] This not only negatively

8 China recorded a growth rate of 3% in 2022, far below its official growth target of 5.5%. See: Hale, Thomas and Sun, Yu, *China's economy expands 3% in 2022 after zero-Covid policies hit growth, Financial Times*, 17th January 2023, viewed 6th April 2023, <https://www.ft.com/content/ebe63075-32c1-46a0-8d49-570dfb654547>

9 *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, p.22, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>

10 This question was first asked as part of the *Business Confidence Survey (BCS) 2014* and has been asked annually since.

11 Erixon, Fredrik, Guildea, Anna, Guinea, Oscar & Lamprecht, Philip, *China's Public Procurement Protectionism and Europe's Response: The Case of Medical Technology*, European Centre for International Political Economy, December 2021, viewed 4th April 2023, <https://ecipe.org/publications/chinas-public-procurement-protectionism/>

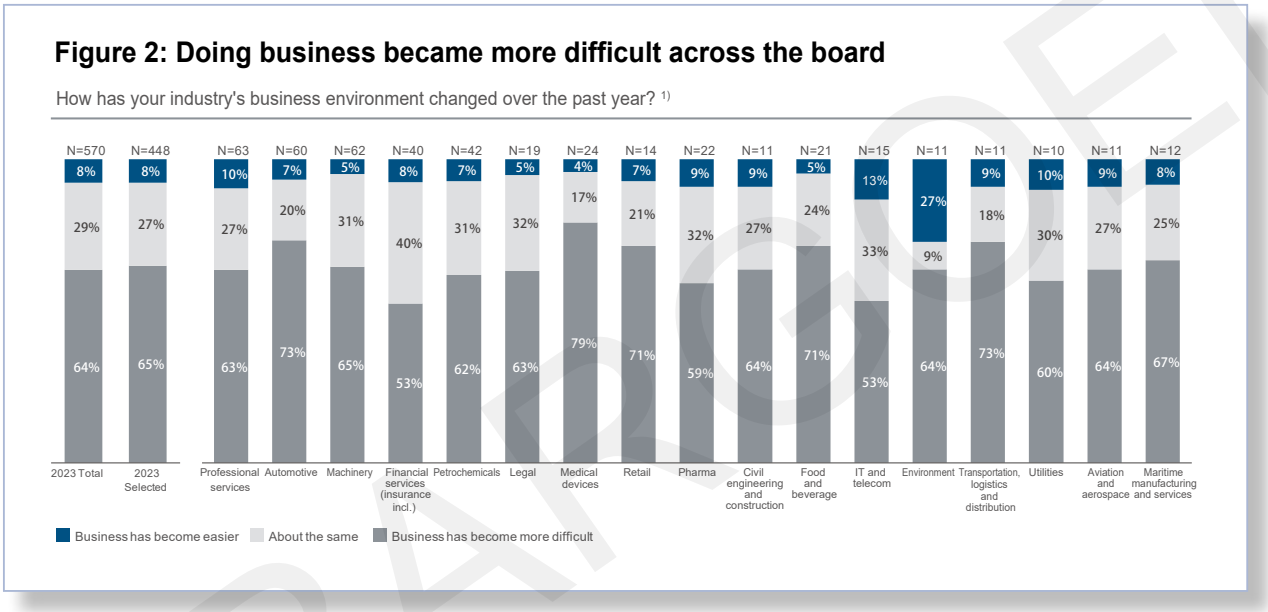
EMBARGOED

impacted the 2022 revenues of European firms, but also resulted in some having to make major staff cuts.

The main impacts of China's stringent COVID-19 restrictions on European automotive firms were dampened consumer demand and supply chain complications.[12] Members also faced regulatory challenges, including as a result of local authorities refusing to permit some European original equipment manufacturers (OEMs) to increase their shares in their joint ventures (JVs) (despite ownership restrictions in the sector having been formally removed from 1st January 2022),[13&14] and restrictions on data collection and cross-border data transfers.[15]

In the transportation, logistics and distribution industry, weak demand—both internationally and domestically—caused a significant reduction in trade, and pandemic control measures in China led to increased operational costs for companies operating in the sector.[16]

Figure 2: Doing business became more difficult across the board



1) Industries selected are those for which there were at least 10 responses

1.2 Company revenues take a hit following a difficult 2022

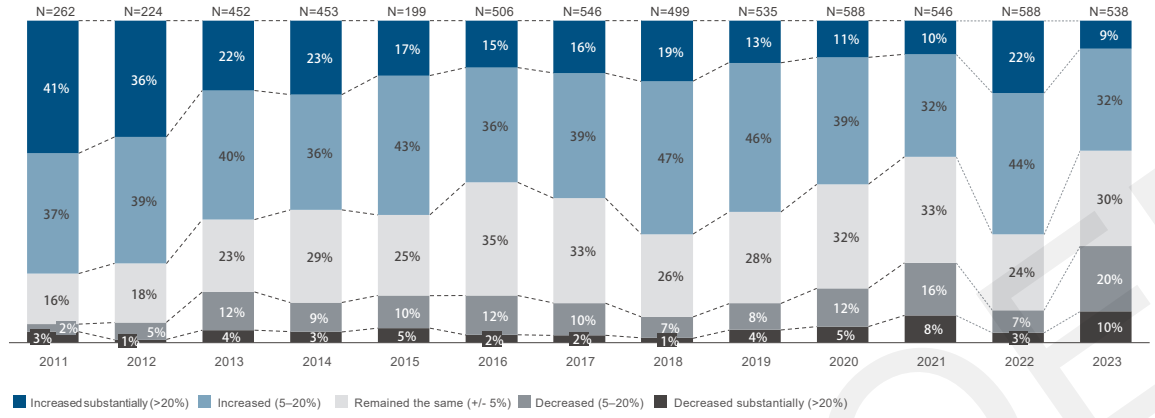
Revenue increases were reported by 41% of respondents in 2022 (-25pp y-o-y), while three in ten respondents recorded revenue decreases (+20pp y-o-y), three times the amount that reported the same the previous year.[17] These poor results are partly explained by China's relatively slow growth rate of 3% in 2022—the second slowest since 1976—as strict COVID-19 restrictions and the unravelling of China's property sector stifled economic activity, and consumer confidence plummeted.[18]

12 Wu, Sara & Norihiko, Shirouzu, *China's COVID curbs hit Toyota, Volkswagen and Apple supplier Foxcom, Reuters*, 14th March 2022, viewed 9th May 2023, <https://www.reuters.com/technology/foxconn-suspends-shenzhen-operations-adjusts-production-line-minimise-impact-2022-03-14/>
13 China pledged to lift restrictions on foreign entities obtaining more than a 50% stake in a JV in China, starting 1st January 2022. Despite this, some European Chamber members report facing difficulties getting approval to increase their shares in JVs.
14 Following the lifting of equity caps, some large European automotive multinational companies (MNCs) were permitted to increase their stakes in their JVs in China, most notably BMW, which in 2022 paid euro (EUR) 3.7 billion to increase its stake in its JV with Brilliance from 50% to 75%. Waldersee, Victoria, *BMW pays $4.2 bln to take control of Chinese JV, Reuters*, 11th February 2022, viewed 18th April 2023, <https://www.reuters.com/business/autos-transportation/bmw-receives-license-take-75-stake-china-joint-venture-bmw-brilliance-automotive-2022-02-11/>
15 This limits companies' ability to collect and store data for R&D and customer services purposes.
16 European Chamber members operating in the transportation, logistics and distribution sector reported that COVID-control measures were often inconsistently implemented across different regions, and in some cases even across different districts in the same city, leading to a significant loss in efficiency.
17 This question was first asked as part of the BCS 2011 and has been asked annually since.
18 China recorded a growth rate of 2.2% in 2020, following the onset of the COVID-19 pandemic. See: Yao, Kevin & Zhang, Ellen, *China's 2022 economic growth one of the worst on record, post-pandemic policy faces test, Reuters*, 17th January 2023, viewed 5th April 2023, <https://www.reuters.com/world/china/chinas-economy-slows-sharply-q4-2022-growth-one-worst-record-2023-01-17/>

EMBARGOED

Figure 3: Record number report revenue decreases

How has your industry's business environment changed over the past year?



At the sectoral level, more members recorded revenue decreases than increases in the aviation and aerospace, medical devices, legal, petrochemicals, retail, and food and beverage (F&B) industries. Growth in retail contracted sharply, with COVID-19-related prevention measures supressing consumer demand significantly.[19] Revenue decreases reported by petrochemical firms were also partly a result of dampened demand, with China's 'zero-COVID' policy resulting in a steep decline in manufacturing activities.[20]

Companies in the medical devices sector report that the drop in their revenues was attributable to several reasons. These include government procurement heavily favouring domestic businesses and stringent pandemic prevention measures, which limited the volume of surgeries and non-COVID-related medical treatments that took place in 2022.[21&22]

The main factors undermining revenues in the legal sector include the decreased number of mergers and acquisitions (M&A) compared to 2021,[23] leading to a drop in demand for services, as well as pandemic-related travel restrictions and difficulties obtaining visas for foreign lawyers, which made meeting clients nearly impossible.[24] Foreign counsels also lost out on business due to the fall in the number of Chinese initial public offerings (IPOs) in the United States (US) and Hong Kong in 2022.[25]

Revenues in the aviation and aerospace sector suffered considerably throughout 2022, due to the imposition of strict travel restrictions (the volume of international passenger flights in 2022 was just 2.6% of 2019 levels)[26] and quarantine policies for international travellers and crew. These measures caused significant harm to the operations of European carriers and hindered the movement of both people and cargo between China and Europe.[27]

EMBARGOED

19 Xie, Stella Yifan, *China Consumer Spending Slumps Under Covid and Property Restrictions, The Wall Street Journal*, 20th November 2022, viewed 5th April 2023, <https://www.wsj.com/articles/china-consumer-spending-slumps-under-covid-and-property-restrictions-11668953528>

20 Peng, Zhou; Simons, Theo Jan; Wallach, Jeremy; Youngman, Adam & Zhu, Yasmine, *Petrochemicals in 2022: A return to normalcy, with uncertainty ahead*, McKinsey & Company, 17th February 2023, viewed 18th April 2023, <https://www.mckinsey.com/industries/chemicals/our-insights/petrochemicals-in-2022-a-return-to-normalcy-with-uncertainty-ahead>

21 Tabeta, Shunsuke & Wakasugi, Tomoko, *China moves to shut out foreign medical device makers, Nikkei Asia*, 14th September 2022, viewed 9th May 2023, <https://asia.nikkei.com/Business/Companies/China-moves-to-shut-out-foreign-medical-equipment-makers>

22 Stanway, Dan, *COVID and bust: China's private health system hurt by tough coronavirus controls, Reuters,* 6th July 2022, viewed 9th May 2023, <https://www.reuters.com/world/china/covid-bust-chinas-private-health-system-hurt-by-tough-coronavirus-controls-2022-07-06/>

23 In 2022, M&A deals dropped to an eight-year low and were down 20% from 2021 levels. See: Wong, Echo, *Nikkei Asia, China M&A deals set for rocky ride after hitting near decade low: PwC*, 24th February 2023, viewed 6th April 2023, <https://asia.nikkei.com/Business/Business-deals/China-M-A-deals-set-for-rocky-ride-after-hitting-near-decade-low-PwC>

24 Foreign lawyers faced disproportionate difficulties obtaining visas due to stringent requirements for residence, stay and pre-residence, which, coupled with existing regulatory hurdles, resulted in a decrease in the number of foreign lawyers in China.

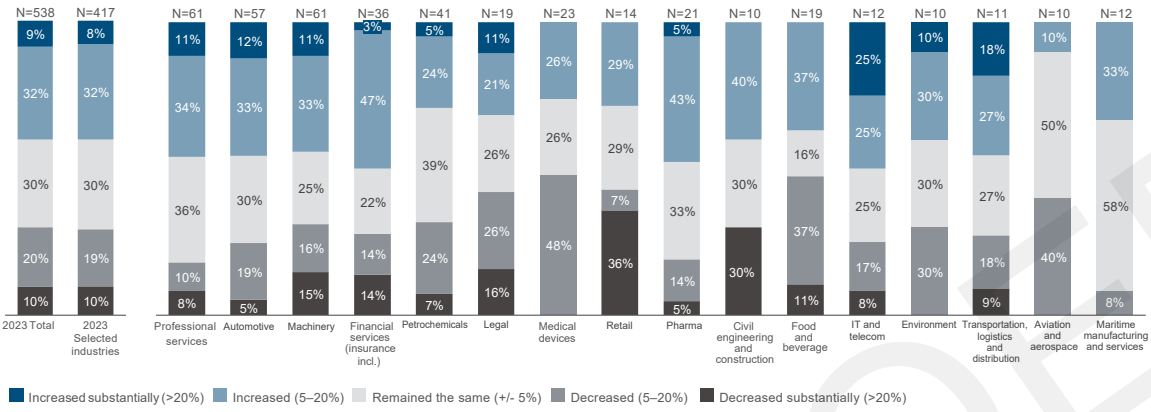
25 "As of the end of 2022, only six China-based companies had issued American depositary receipts in U.S. IPOs since the Didi fallout": Cheng, Evelyn, *Chinese IPOs are coming back to the U.S., CNBC*, 10th February 2023, viewed 6th April 2023, <https://www.cnbc.com/2023/02/10/chinese-ipos-are-coming-back-to-the-us.html>

26 *2022 National Civil Transport Airport Production Statistical Bulletin*, Civil Aviation Administration of China, 3rd March 2023, viewed 26th April 2023, <http://www.caac.gov.cn/PHONE/XXGK_17/XXGK/TJSJ/202303/t20230317_217609.html>

27 *European Business in China Position Paper 2022/2023,* European Union Chamber of Commerce in China, pp.15-19, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>

Figure 4: Revenue by industry: Mixed results

How did your company's total 2022 revenue in Mainland China evolve compared to 2021? [1)]

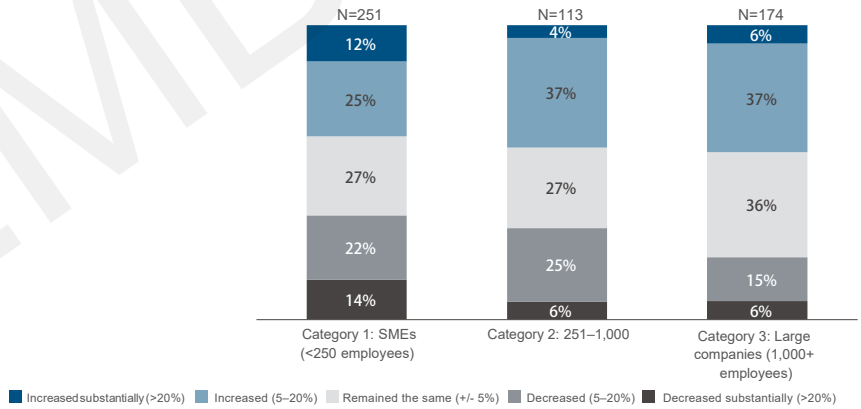


1) *Industries selected are those for which there were at least 10 responses*

Small and medium-sized enterprises (SMEs) saw the biggest changes to their revenues in 2022. At one end of the spectrum, a disproportionately high percentage of SME members reported y-o-y decreases in their bottom lines (36%), 15pp more than the proportion of companies with 1,000+ employees that reported the same. This reflects the fact that many SMEs, which often lack the resources to navigate unexpected changes in China's business environment, were substantially impacted by COVID-19-related containment measures.[28] At the other end of the spectrum, a higher percentage of SMEs recorded substantial revenue increases (>20% of their annual revenue), highlighting that opportunities remained for some.

Figure 5: SME revenues acutely impacted

How did your company's total 2022 revenue in Mainland China evolve compared to 2021?



28 For example, an East China Normal University survey of more than 2,000 SMEs based in Shanghai found that, following the city's spring 2022 lockdown, 89% of respondents had either lost confidence in their ability to conduct business or were preparing to close down. See: *Survey: Ninety percent of Shanghai's small and medium-sized enterprises are "lying flat" amid an official push for financial relief, Mingjing News*, 9th May 2022, viewed 5th April 2023, <https://mingjingnews.com/article/438560-16>

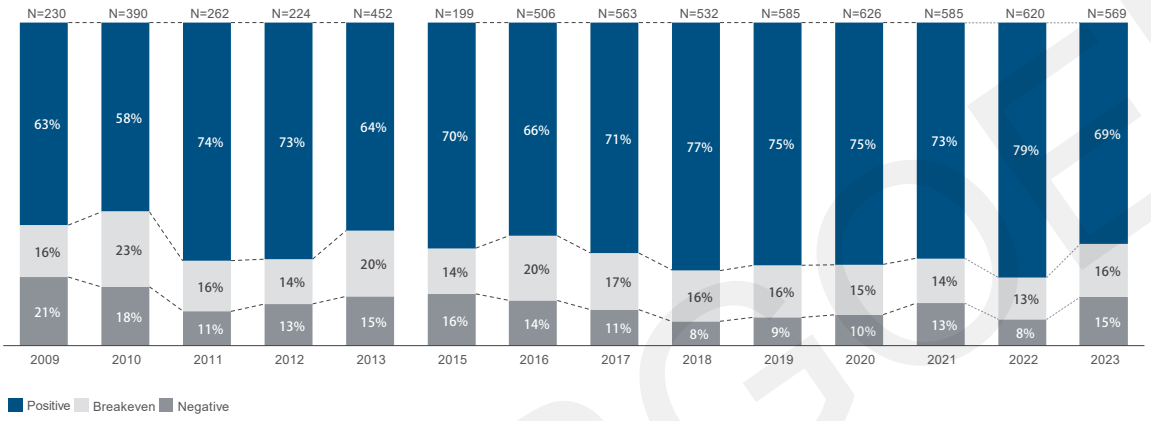
EMBARGOED

1.3 Profitability down

Overall, European companies' profitability also declined in 2022. Almost 70% recorded positive earnings before interest and tax (EBIT) (-10pp y-o-y), with another 16% breaking even. The number of those in the red (15%) increased by 7pp y-o-y, the worst performance since 2015.

Figure 6: Profitability takes a hit

Please describe your company's earnings before interest and tax (EBIT) in Mainland China in 2022

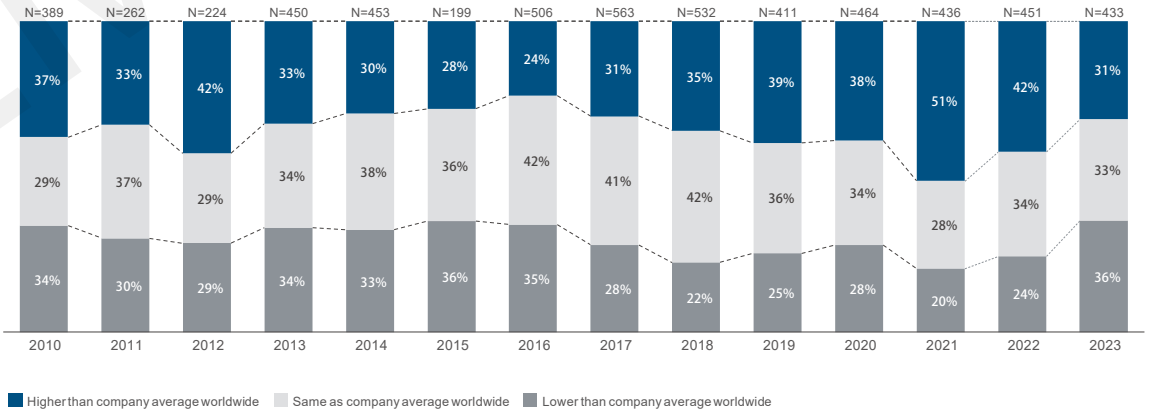


1.4 Importance of China for global profits falls

The importance of companies' China EBIT margins relative to the rest of the world fell in 2022 for the second consecutive year as COVID-19-related restrictions hampered company operations in China while much of the rest of the world returned to normality. For the first time since 2016, the number of respondents that reported a China EBIT margin lower than their average worldwide margin exceeded the number that reported a higher China EBIT (36% vs 31% respectively).

Figure 7: Percentage China contributes to companies' global EBIT margins declined

How did the EBIT margin of your company's Mainland China operations evolve compared to your company's worldwide average EBIT margin in 2022?



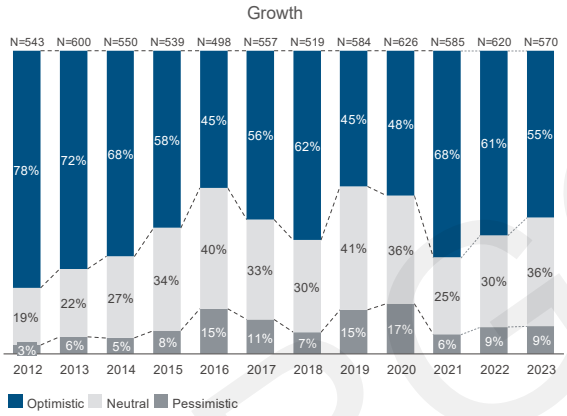
EMBARGOED

1.5 Companies less optimistic about China's growth prospects

Confidence in China's growth prospects over the coming two years deteriorated among respondents, with fewer (-6pp) reporting optimism than in 2022, despite the fact that companies were surveyed after China's 're-opening'. This reflects concerns that, following four decades of breakneck growth, China may be poised for an "age of slow growth" as it faces a host of economic headwinds.[29] These include the country's diminishing demographic dividend, dwindling productivity growth and rising debt levels, as well as the increasingly complex geopolitical environment.

Figure 8: Outlook on growth deteriorates

How would you describe the business outlook for your sector in China over the next two years?



29 Rosen, Daniel H., Vest, Charlie & Quinn, Rogan, *Now for the Hard Part: China's Growth in 2023 and Beyond*, Rhodium Group, 29th December 2022, viewed 6th April 2023 <https://rhg.com/research/now-for-the-hard-part/>

EMBARGOED

2 MOUNTING CHINA CHALLENGES PROMPT EU BUSINESSES TO LOOK ELSEWHERE

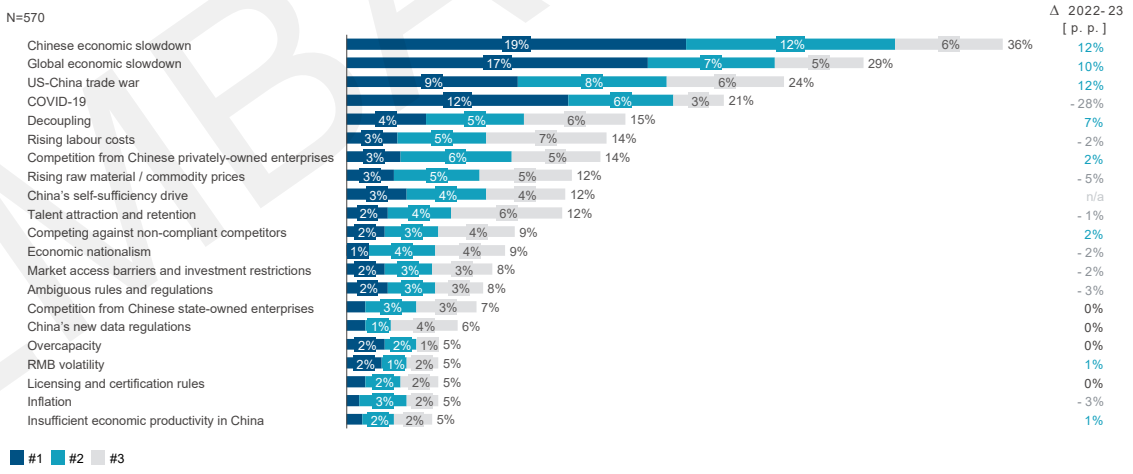
Heightened challenges to doing businesses in China, geopolitical tensions, and the Chinese and global economic slowdowns have eroded China's attractiveness as an investment destination.[30] Fewer European companies are looking to expand their current China investments and increasing numbers are considering making future investments elsewhere. Notably, several have already started relocating existing investments.

2.1 The top post-zero-COVID business challenges

In the last two editions of the BCS, respondents ranked COVID-19 as the most significant challenge to their future business in China. In the 2023 survey, this was supplanted by China's economic slowdown, which over a third of respondents (36%) ranked as a top-three challenge, reflecting just how concerned they are over the headwinds facing China's economy.[31] This was followed by the global economic slowdown, ranked as a top-three concern by 29%,[32] and the US-China trade war, ranked as a top-three challenge by 24% of respondents. COVID-19 ranked fourth (21%) and decoupling came in fifth (15%), emphasising the extent to which the business environment has become politicised (see Section 5).

Figure 9: Chinese and global economic slowdowns replace COVID-19 as top challenges faced by business

Please rank the top three business challenges that you selected as significant above [1) 2)]



1) *Respondents asked to rank the top three challenges selected in response to: "Please choose at least three challenges your company perceives as having the greatest impact on your future business in China."*
2) *n/a refers to a new option or an option that is different from the previous year*

30 For more on this point, see: *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, p.22, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>
31 Examples of headwinds faced include the unravelling of China's real estate sector, high levels of local government debt, high unemployment rates and fading favourable demographics.
32 The World Bank has projected that global growth will be lacklustre in 2023, with the global economy projected to grow at 1.7% - the third-weakest pace in nearly three decades, overshadowed only by the 2009 and 2020 global recessions. *Global Economic Prospects*, World Bank, January 2023, viewed 6th April 2023, <https://www.worldbank.org/en/publication/global-economic-prospects>

EMBARGOED

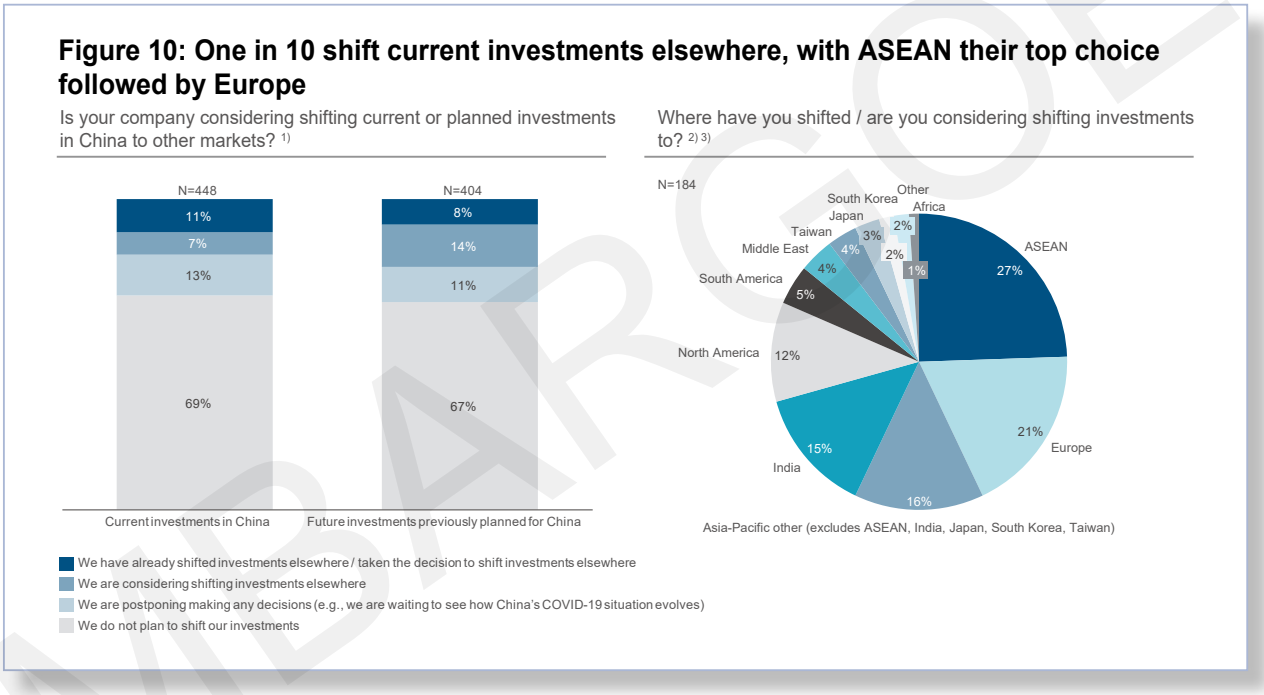
2.2 Investments begin to shift out of China as de-risking strategies emerge

A significant 11% of respondents—the same proportion that were *considering* shifting existing investments from China in the BCS 2022[33]—report they have already done so. A further 20% are considering shifting current investments elsewhere, or are postponing making any such decisions as they wait to see how China's businesses environment evolves in 2023.

Notable decisions on *future investments* previously planned for China have also been taken, with 8% of respondents reporting that they have either already moved or decided to move them to other markets. A quarter reported they are either considering shifting some future investments or postponing making any such decisions.

The Association of Southeast Asian Nations (ASEAN) region appears set to be the main beneficiary of this, with over a quarter (27%) of respondents that have either already shifted investments, or that are considering doing so, naming the region as their destination of choice. Notably, one in five (21%) have already shifted, or are considering shifting, investments to Europe.

Figure 10: One in 10 shift current investments elsewhere, with ASEAN their top choice followed by Europe



1) *Excludes respondents that responded 'Don't Know'*
2) *Question only asked to respondents that reported that they already have or are considering shifting China investments elsewhere in response to the question: Is your company considering shifting current or planned investments in China to other markets?*
3) *Multiple answers possible; percentages based on the total number of responses*

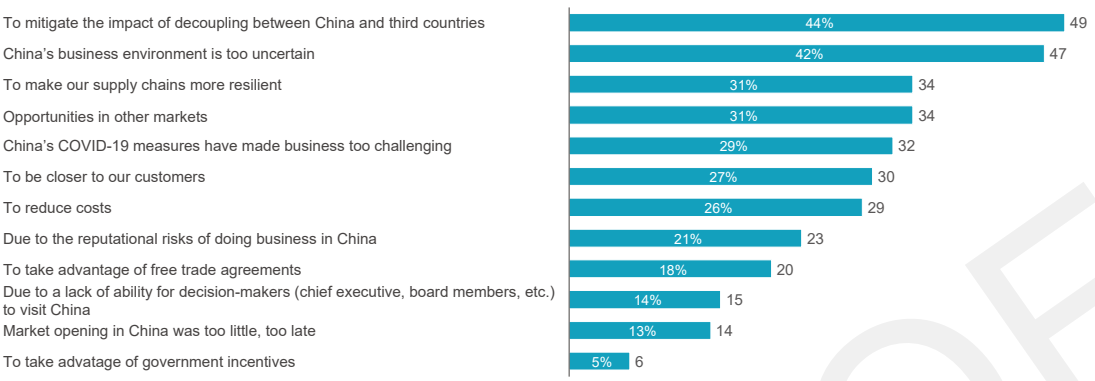
The key reasons that businesses have already shifted, or are considering shifting, investments are: to mitigate the impact of decoupling between China and third countries (44%); due to China's business environment becoming too uncertain (42%); to increase supply chain resilience (31%); and to take advantage of opportunities in other markets (31%). Nearly three in 10 (29%) report that it is because China's COVID-19 policy measures made business too challenging. This indicates that businesses are considering shifting investments predominantly to de-risk and build resilience, rather than for purely business reasons.

33 *European Business in China Business Confidence Survey 2022*, European Union Chamber of Commerce in China, 20th June 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-archive/1020/Business_Confidence_Survey_2022>

EMBARGOED

Figure 11: Investments shifted predominantly for defensive reasons

Why have you shifted / are you considering shifting current or planned investments in China to other markets? [1) 2)]

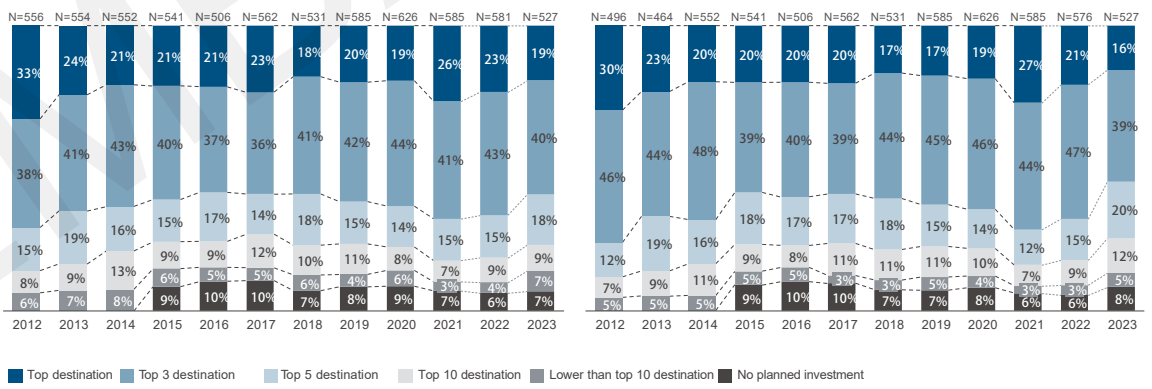


1) *Multiple answers possible*
2) *Question only asked to members that reported that they already have or are considering shifting China investments elsewhere in response to the question: Is your company considering shifting current or planned investments in China to other markets?*

In the BCS 2023, 59% of respondents reported that China is currently a top-three destination for investment (-7pp y-o-y), while 14% of respondents (+4pp) said that China is not a top-ten destination for present investments, or that they currently have no investments planned for the China market. Only 55% of respondents reported the country is a top-three destination for *future* investments, a 13pp drop y-o-y and the lowest total on record.[34]

Figure 12: Importance of China as an investment destination decreased

On a global scale, where does China rank as a destination for present and future investments for your company?



Respondents operating in the medical devices industry are the least willing to make future investments in China, with 24% reporting they have no plans to do so. This reflects the mass uncertainty caused by China's 'zero-COVID' policy, which led to both sudden closures of manufacturing facilities and supply chain challenges.[35] It is also a result of

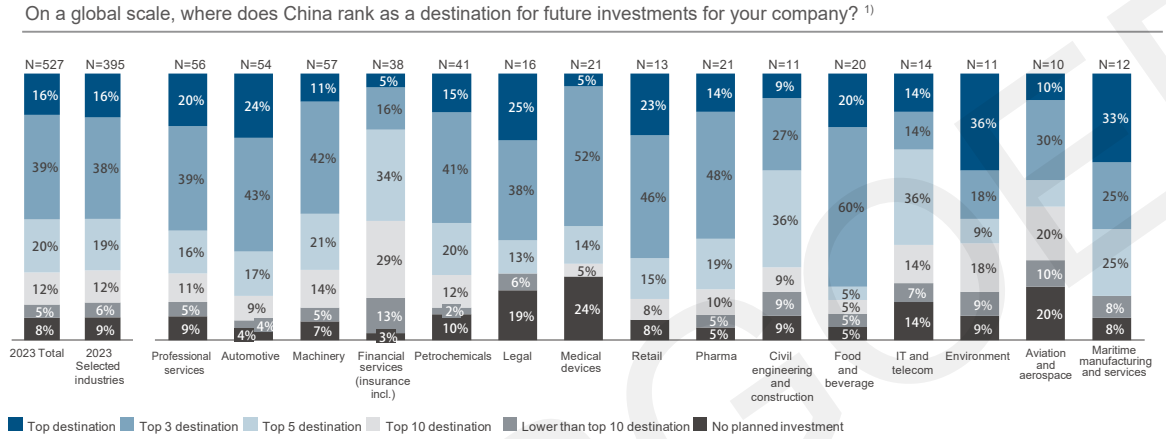
34 This question first featured in the BCS in 2010 and has been asked annually since.
35 For example, businesses experienced delays to imports of components at major harbours, and the reduction in road freight arising from the Shanghai lockdown led to disruptions in production all over China.

EMBARGOED

government procurement guidelines that require public hospitals to 'buy China'.[36]

Investor confidence was also relatively low in the aviation and aerospace sector, where one in five reported no planned future investment in China. Some members in this sector have attributed this to the impact of COVID-related travel restrictions in 2022—which limited the movement of goods and people between China and the rest of the world—China's self-reliance drive, and the hardening of attitudes in the European Union (EU) towards China.

Figure 13: Attractiveness of China as an investment destination varies by sector

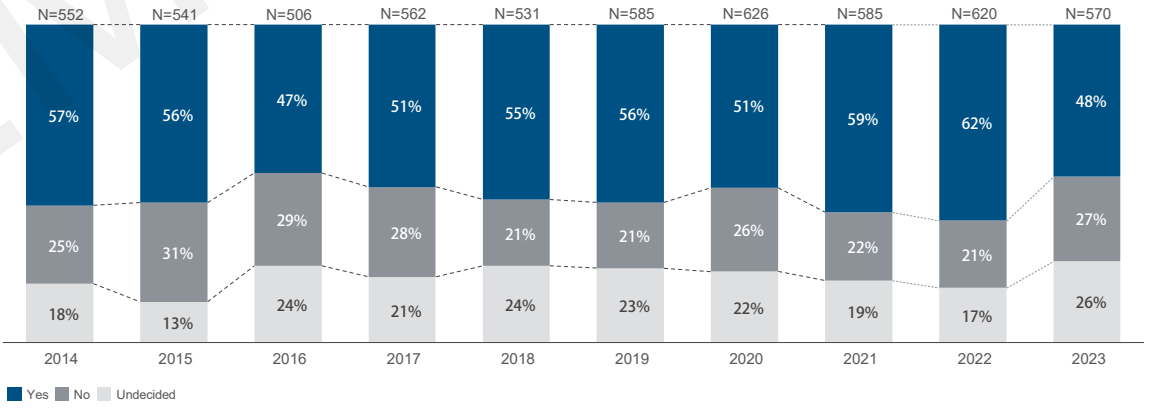


1) Industries selected are those for which there were at least 10 responses

2.3 Decrease of China expansion plans

Only 48% of respondents reported plans to expand their China operations in 2023, a drop of 14pp y-o-y, and the first time since 2016 that less than half of respondents reported having plans to do so.

Figure 14: Less than half consider expanding their China operations



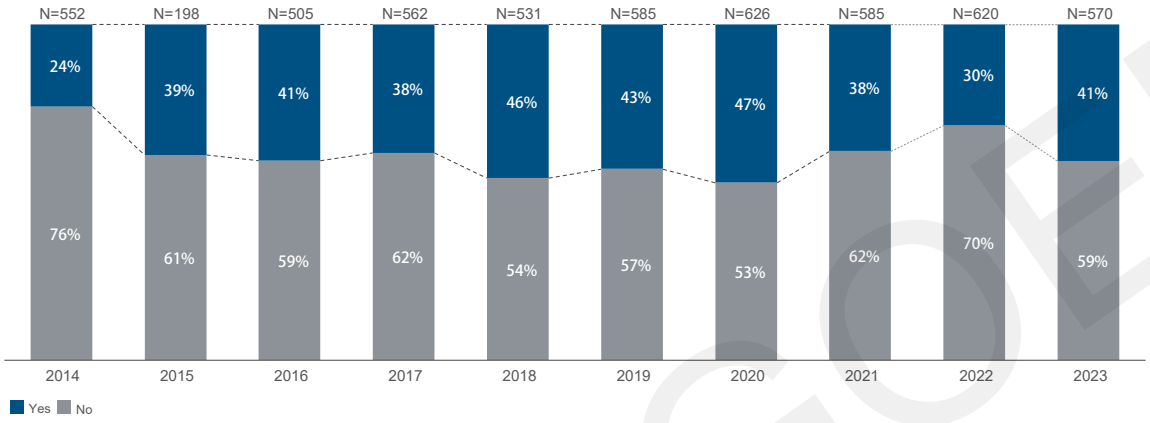
36 While the Ministry of Finance specified that products domestically produced in China by local and foreign manufacturers should receive equal treatment, procurement of imported medical devices became more restricted, and with concerns remaining over intellectual property right (IPR) protection in China, many manufacturers are reluctant to bring their production lines to the country: *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, pp.244–245, 21st September 2022, viewed 6th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>

EMBARGOED

More than 40% of respondents plan to cut costs in China in 2023, an increase of 11pp y-o-y, reflecting both the growing difficulty of doing business in China and the fact that members are increasingly considering expanding their operations elsewhere.

Figure 15: Increase in cost-cutting

Does your company plan on cutting costs in China in 2023?

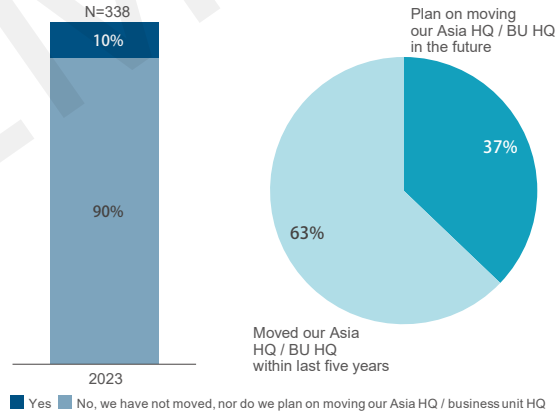


2.4 One in 10 moving HQs out of Mainland China

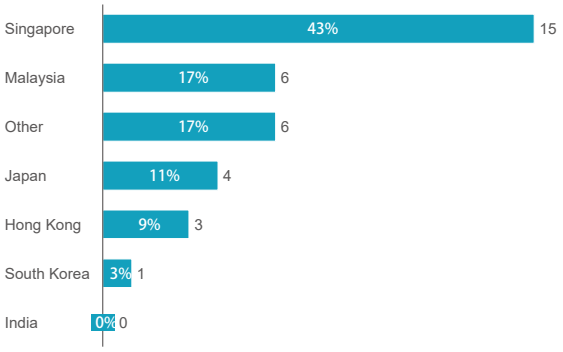
One in 10 respondents reported they have already moved or plan to move their Asia HQ / business unit (BU) HQ out of China, with two thirds of those having already done so. The top destination for those that have moved, or that are planning to, is Singapore (43%), with Malaysia coming second (17%). Only 9% have relocated, or plan to relocate, to Hong Kong.

Figure 16: One in 10 to move HQs out of China

Has your company moved your Asia HQ / business unit (BU) HQ out of Mainland China in the past five years, or do you plan to do so in the future? 1)



Where did you move your Asia HQ / business unit HQ to, or where do you plan to move to?



1) *Excludes respondents that responded 'Don't Know' or 'Not applicable (e.g., we do not have an Asia HQ / BU HQ in Mainland China)'*

EMBARGOED

3 DECOUPLING INTENSIFIES: COMPANIES LOCALISE AND SILO OPERATIONS

The growing list of challenges European businesses face when operating in China has pushed many to localise and silo their China operations. An increasing number are creating two separate systems, with one for China and one for the rest of the world—including for supply chains, data and information technology (IT) systems, and staffing—an expensive and inefficient solution.

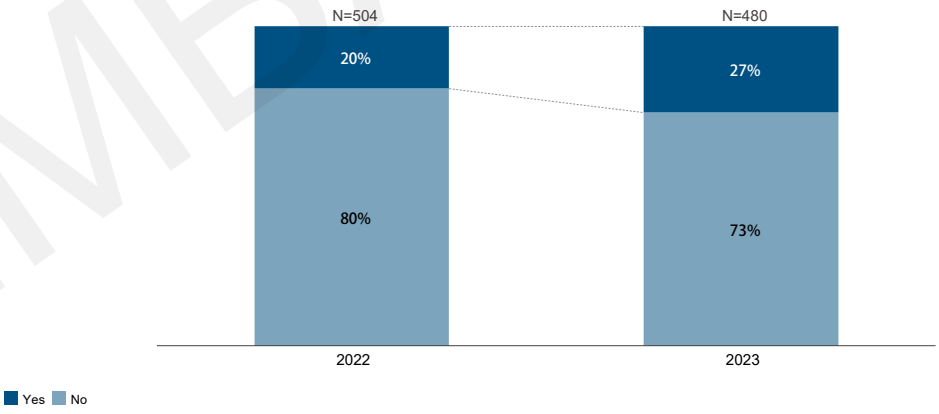
The exodus of foreign employees from China—which accelerated during the COVID-19 pandemic—continued throughout 2022, and members have been taking steps to both onshore and offshore parts of their China supply chains to build resilience and mitigate risks. With new and forthcoming EU and US legislation set to put further pressure on businesses to demonstrate transparency in their China operations by providing certification from independent, third-party auditors—which is not possible under current conditions in China—these trends are set to strengthen in the medium-term.

3.1 HQ and China operations decoupling

Decoupling between HQs and China operations was reported by 27% of respondents, an increase of 7pp y-o-y. The trend strengthened in the BCS 2023, due to stringent COVID-19 travel restrictions preventing European HQ executives from visiting their China operations and vice-versa, and the number of foreign nationals employed in China operations reducing even further (see Section 3.3).

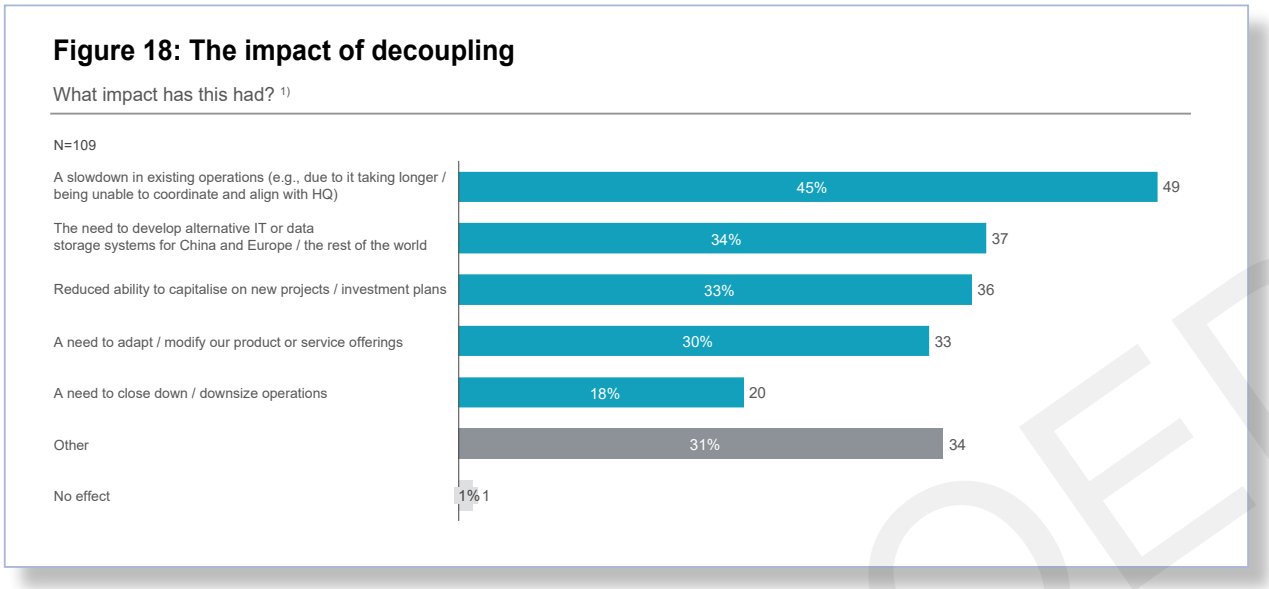
Figure 17: More than a quarter report decoupling

Has your company experienced any form of decoupling between your HQ and your China operations over the past two years?



Respondents whose HQs have decoupled from China operations have been impacted in a variety of ways. Almost half reported experiencing a slowdown in their operations due to difficulties aligning their China operations with HQs. A third reported a reduced ability to capitalise on new projects and/or investment plans, while nearly a fifth reported having to close or downsize their China operations. More than a third also reported having to develop separate IT and/or data storage systems, with one for China and one for Europe / the rest of the world.

EMBARGOED

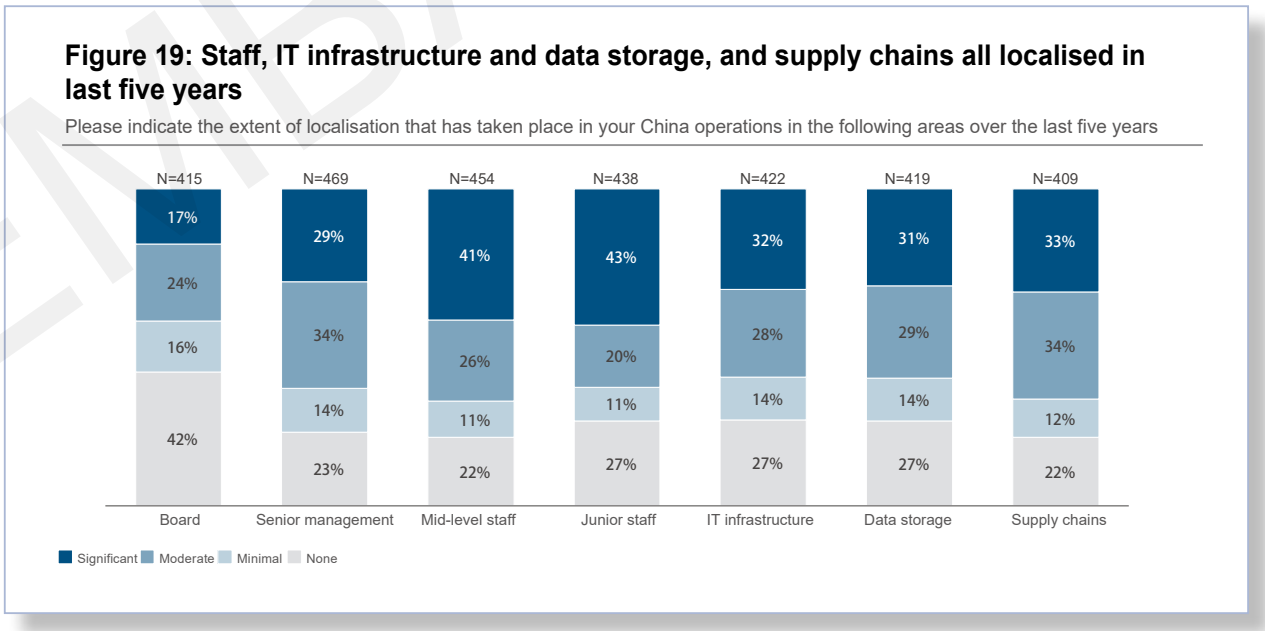


1) Multiple answers possible

3.2 Some businesses localise to manage risks

Most European companies are not planning on leaving the China market altogether. However, faced with mounting risks, an increasingly uncertain regulatory environment,[37] and heightened geopolitical tensions, a majority of respondents report having begun the process of localising their China operations over the past decade.

This has taken place with staff positions, all the way from junior recruits to board members. IT and data storage infrastructure have also both been localised to some degree by 74% of respondents, with this driven by China's 'secure and controllable' technology guidelines and increasingly stringent data governance regulations.[38] Eight out of 10 members have also separated their China supply chains from those for the rest of the world, a topic explored in Section 3.4.



37 For more on this point, see: *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, p.22, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>

38 *European Business in China Business Confidence Survey 2022*, European Union Chamber of Commerce in China, 20th June 2022, p. 37, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-archive/1020/Business_Confidence_Survey_2022>

EMBARGOED

3.3 Exodus of foreign nationals continues

The foreign national exodus, exacerbated by China's 'zero-COVID' policy, continued in 2022.[39] One in six respondents (16%, +5pp y-o-y) say they do not currently employ any foreign nationals, while foreign nationals make up 10% or less of overall staff for 78% of respondent companies. SMEs are particularly impacted: one in five (21%) report employing no foreign nationals in their China operations.

Aside from the challenges this creates for European businesses (see Figure 21), it also comes at a huge cost to China. Foreign nationals working in China are some of the best 'ambassadors' for the country—they frequently extol the positive aspects of their experiences when back in their home countries—something much needed at a time when geopolitical tensions are on the rise and negative public opinion towards China is at an all-time high in a number of EU Member States.[40]

Figure 20: 16% of members employ no foreign nationals in China



Some of the negative impacts of the decrease of foreign employees include a reduced transfer of know-how and best practices (44%, +6pp y-o-y); increased communication difficulties between HQs and China operations (41%, +7pp); deferred investment plans (13%, +5pp); and the need to close China operations (2%, -1pp).

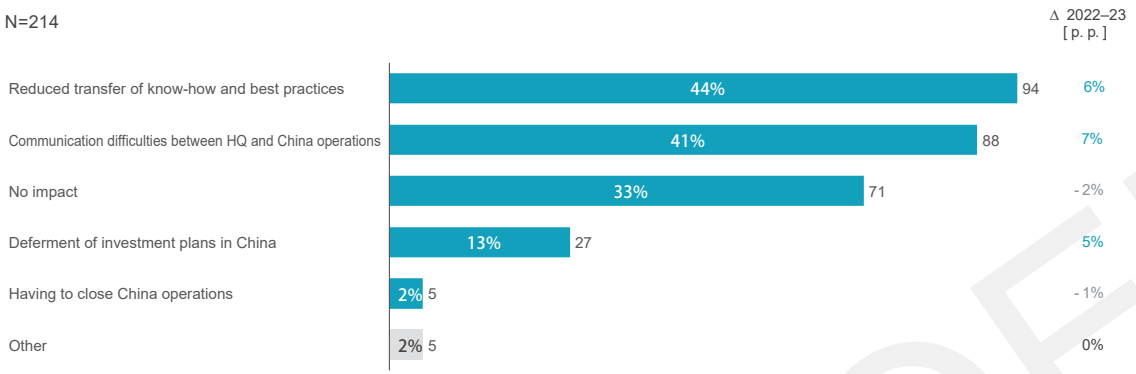
EMBARGOED

39 For more on the causes and impacts of this, see: *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, pp.15–19, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>

40 A Spring 2022 PEW Research Center survey found that that negative attitudes towards China in Europe were at the highest level on record in 10 out of 19 countries surveyed. Results are recorded annually and date back to 2002; *Large majorities continue to hold unfavorable view of China*, Pew Research Center, 27th June 2022, viewed 5th April 2023, <https://www.pewresearch.org/global/2022/06/29/negative-views-of-china-tied-to-critical-views-of-its-policies-on-human-rights/pg_2022-06-29_views-of-china_00-02/?utm_source=substack&utm_medium=email>

Figure 21: Decrease of foreign nationals comes at a cost

What is the impact of the decrease of foreign employees on your company? 1)



1) Multiple answers possible

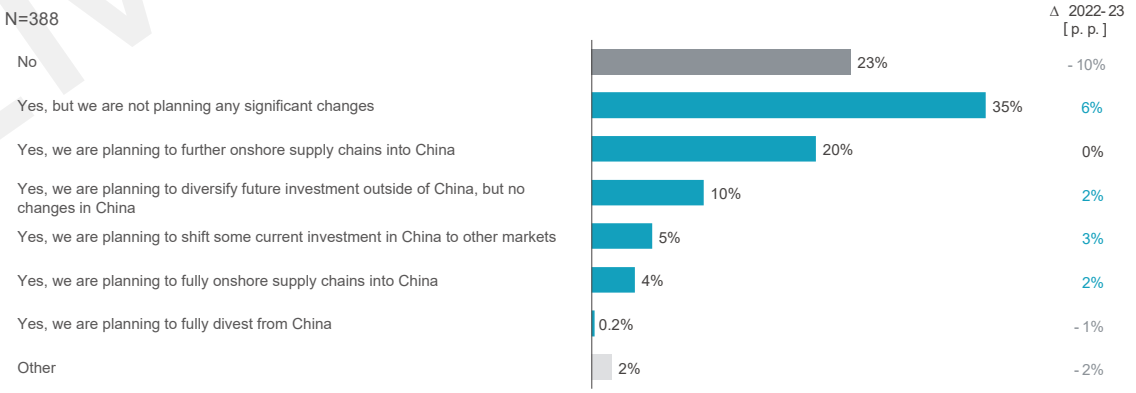
3.4 Supply chain strategies continue to evolve

Three quarters of respondents reported they had reviewed their supply chain strategies over the past two years. While just 0.2% are looking to fully divest from China, many members are exploring a range of strategies to increase their supply-chain resilience, including onshoring, offshoring and reshoring.

Almost a quarter of respondents are planning either to further or fully onshore their supply chains into China (24%, +2pp y-o-y). At the same time, 12% of those that have reviewed their supply chains report having already shifted parts of them outside of Mainland China, with Europe (44%), ASEAN (36%) and India (31%) being the primary beneficiaries (Figure 23). One in 10 respondents report that they will not make changes to their existing supply chains in China but plan to diversify future supply-chain-related investments outside of the country.

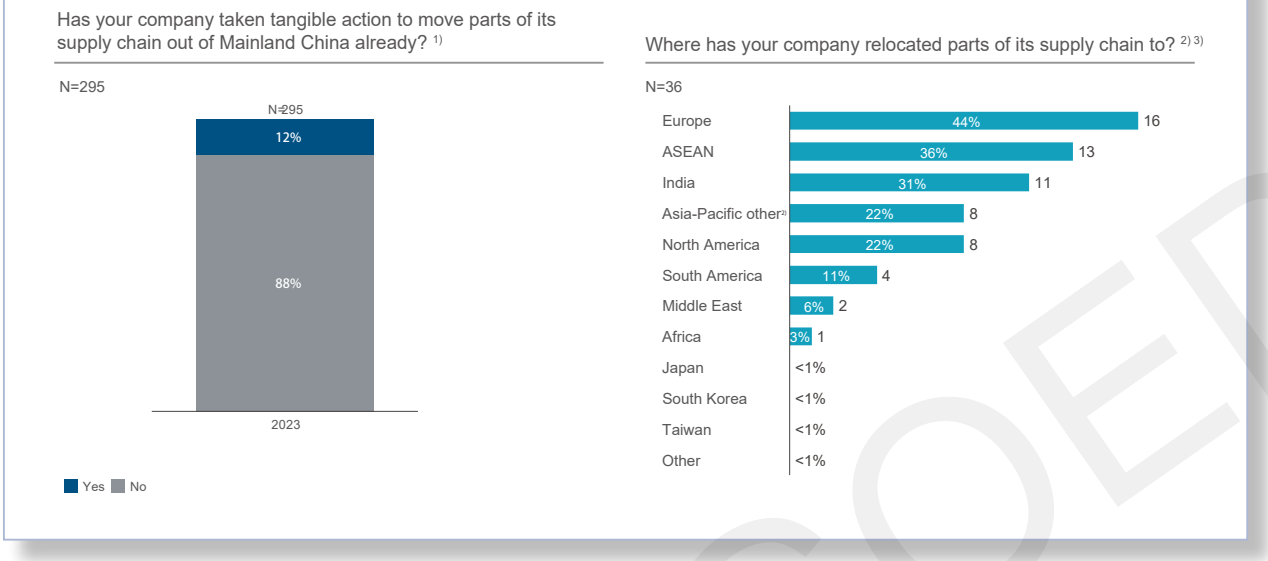
Figure 22: More than three quarters re-evaluating China supply chains

Has your company reviewed its supply chain strategies in the last two years?



EMBARGOED

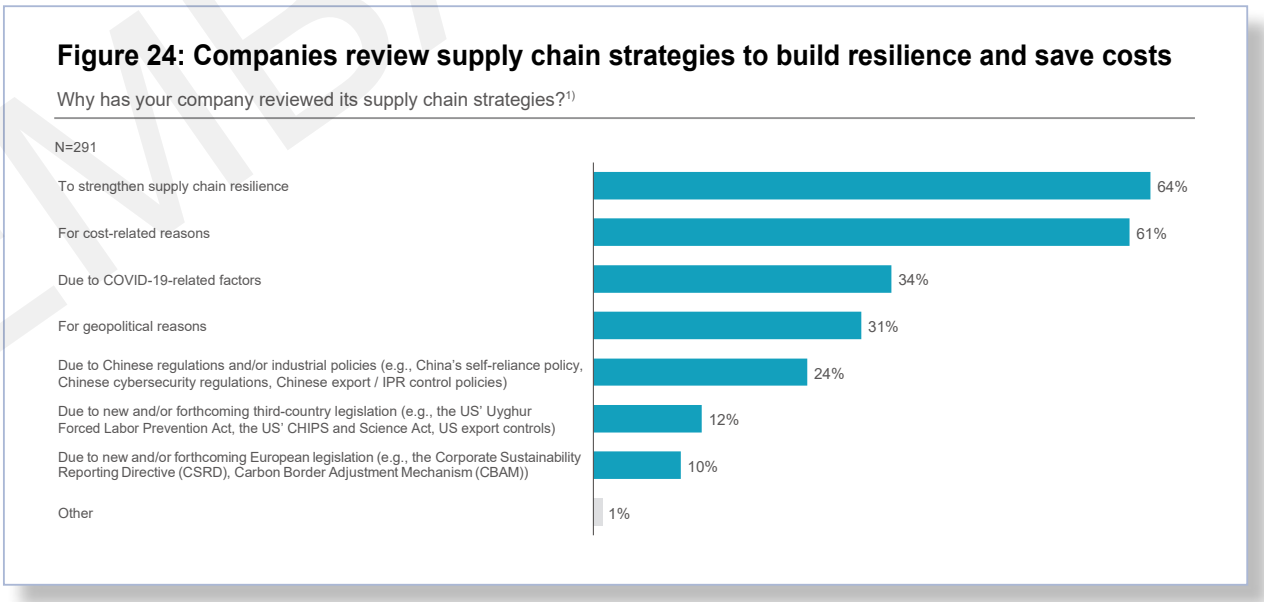
Figure 23: Many supply chains already shifted out of China



1) *Excluded those that responded 'no' to the question: Has your company reviewed its supply chain strategies in the last two years? Question only asked to respondents that report having supply chains in China.*
2) *Multiple answers possible*
3) *'Asia-Pacific other' excludes ASEAN, India, Japan, South Korea and Taiwan*

Respondents are predominantly reviewing their supply chains to mitigate current and potential risks: strengthening supply chain resilience is the top reason (64%); countering COVID-19-related factors (34%) ranks third; geopolitical reasons (31%) fourth; Chinese regulations and/or industrial policies (24%) fifth; new and/or forthcoming third-country legislation (12%) sixth; and new and/or forthcoming EU legislation (10%) seventh. However, with cost-related reasons ranking second (61%), a key reason for EU companies to adjust their supply chain strategies is to maintain profitability, as labour and production in China become increasingly expensive.

Figure 24: Companies review supply chain strategies to build resilience and save costs



1) *Multiple answers possible*

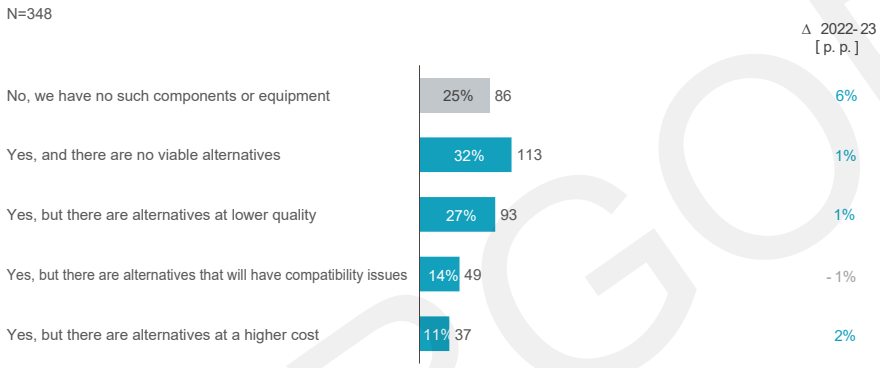
EMBARGOED

The adjustment of supply chains can be expected to continue, with many manufacturers still exposed to potential shocks. Only a quarter (+6pp y-o-y) of respondents do not import components or equipment into China that cannot be easily replaced in the event of a supply disruption; and a third of manufacturers (32%) import critical components for which they cannot source alternatives at all.

Over a quarter (27%) of respondents are able to source alternatives for equipment/components they currently import into China, but report that the substitutes are of lower quality; another 14% report that they can source replacements but will have compatibility issues; and 11% say the alternative products available come at a higher cost.

Figure 25: Majority import critical components that they cannot easily replace

Does your company import any equipment or components from abroad for which it cannot find comparable replacements? 1)



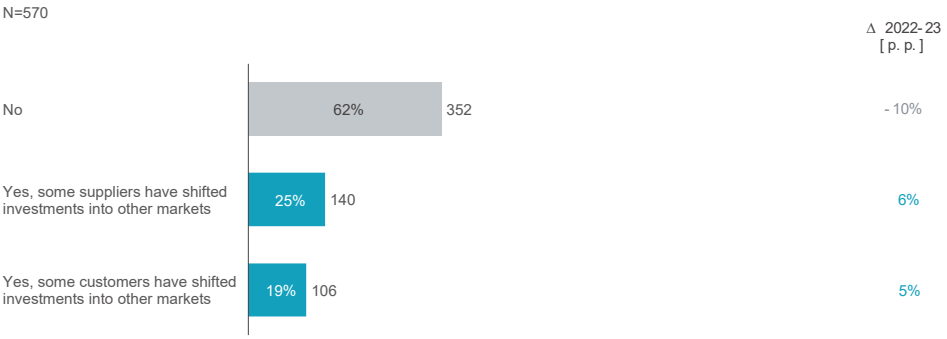
1) Multiple answers possible

3.5 More Chinese suppliers and customers move operations to other markets

The number of respondents with Chinese suppliers and/or customers that have shifted investments away from China also increased in 2022. A quarter (+6pp y-o-y) have seen suppliers move investments to other markets, while almost a fifth (19%, +5pp y-o-y) report that customers have done so.

Figure 26: Four in 10 witnessed Chinese suppliers and/or customers move operations out of China

Has your company seen Chinese suppliers / customers moving operations out of China and into other markets? 1)



1) Multiple answers possible

EMBARGOED

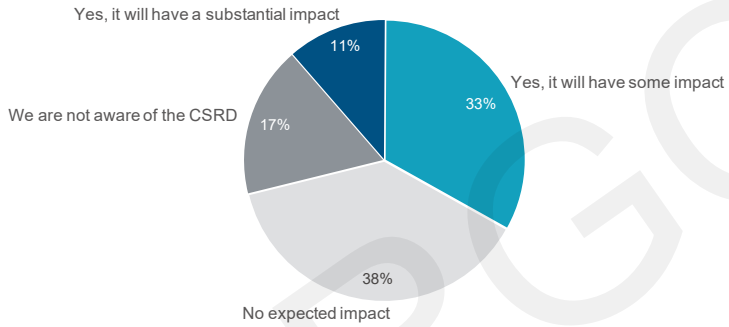
3.6 New EU and third-party regulations drive change

New legislation coming out of the EU and the US is set to increase pressure on companies and their suppliers/partners to demonstrate transparency in their China operations. The EU is in the process of introducing the Corporate Sustainability Reporting Directive (CSRD). This legislation will apply to all large European companies and listed European companies (including SMEs), as well as non-EU companies that have an annual net turnover in the EU of euro (EUR) 150 million and at least one EU-based subsidiary or branch.[41] A significant 44% of respondents say the directive will affect their China operations, with 11% expecting the impact to be substantial. For legislation that is so wide-reaching, it is concerning that nearly a fifth of respondents (17%) are not aware of it.

Figure 27: 44% expect EU's CSRD to impact China operations

Do you expect the EU's introduction of the Corporate Sustainability Reporting Directive (CSRD) to impact your China operations?

N=418



New and forthcoming US export control policies on advanced computing and semiconductor manufacturing are also set to impact a large proportion of EU companies operating in China.[42&43] Approximately a fifth of respondents expect consequences for their operations, while three in 10 are not yet aware of whether they will be impacted by the policies, highlighting that much uncertainty remains over how the regulations will be implemented.

EMBARGOED

41 *New rules on corporate sustainability reporting: provisional political agreement between the Council and the European Parliament,* European Council, Council of the European Union, 21st June 2022, viewed 5th April 2023, <https://www.consilium.europa.eu/en/press/press-releases/2022/06/21/new-rules-on-sustainability-disclosure-provisional-agreement-between-council-and-european-parliament/>

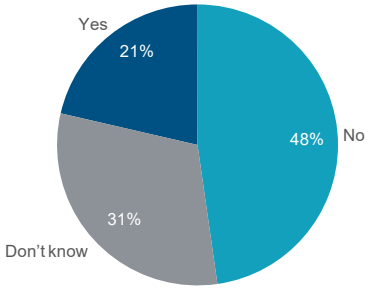
42 On 7th October 2022, the US Department of Commerce released new rules that prohibit American companies from exporting technology, software and equipment to China used in producing advanced computing chips and supercomputers. Under the new rules, Americans are also barred from supporting certain China-based chip companies without a licence from the US Government. See: *Commerce Implements New Export Controls on Advanced Computing and Semiconductor Manufacturing Items to the People's Republic of China (PRC)*, US Department of Commerce: Bureau of Industry and Security, 7th October 2022, viewed 6th April 2023, <https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/3158-2022-10-07-bis-press-release-advanced-computing-and-semiconductor-manufacturing-controls-final/file>

43 In January 2023, Japan and The Netherlands also agreed to restrict exports of advanced chip-manufacturing equipment to China. Hayashi, Yuka & Salama, Vivian, *Japan, Netherlands Agree to Limit Exports of Chip-Making Equipment to China, The Wall Street Journal*, 28th January 2023, viewed 6th April 2023, <https://www.wsj.com/articles/japan-netherlands-agree-to-limit-exports-of-chip-making-equipment-to-china-11674952328>

Figure 28: One in five expect to be impacted by US export control policies

Have your operations been, or do you expect your operations to be, impacted by new and forthcoming US export control policies / regulations?

N=570



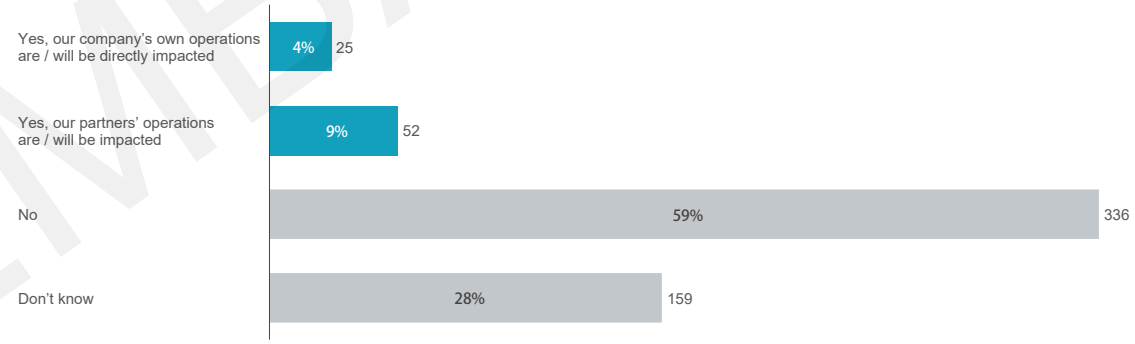
On 21st June 2022, the US introduced the Uyghur Forced Labor Prevention Act (UFLPA), which imposes additional restrictions on imports from China's Xinjiang Uyghur Autonomous Region on top of bans on tomatoes and cotton from there that were already in place.[44&45] The UFLPA has heightened both the risks and uncertainty faced by companies with direct operations in Xinjiang, as well as those with partners/suppliers based in the region.

As of March 2023, 4% of respondents to the BCS 2023 have already been, or expect to be, directly impacted by the UFLPA, while 9% say their partner's operations are already, or will be, impacted. A further 28% of respondents do not know if the UFLPA will affect their operations.

Figure 29: US' Uyghur Forced Labor Prevention Act to present a challenge for a minority

Have your operations been, or do you expect your operations to be, impacted by the US' Uyghur Forced Labor Prevention Act? 1)

N=570



1) Multiple answers possible; percentages based on the total number of responses

One of the most significant challenges for EU companies thrown up by the new EU and US legislation is the requirement to demonstrate the transparency of their China operations. For example, under the UFLPA, businesses are required to prove that they are not involved in forced labour practices; while the EU's CSRD has strict reporting requirements that

44 The UFLPA establishes a 'rebuttal presumption', which prohibits the import of goods from Xinjiang and puts the burden of proof on the importer to provide sufficient evidence that the goods being imported were not produced using forced labour.

45 *Implementation of the Uyghur Forced Labor Prevention Act*, US Department of State, 21st June 2022, viewed 5th April 2023, <https://www.state.gov/implementation-of-the-uyghur-forced-labor-prevention-act/>

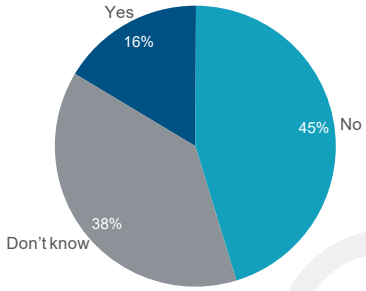
EMBARGOED

oblige large, public-interest companies to publish sustainability reports certified by independent, third-party auditors,[46] which is not possible under current conditions in China. This is a concern for 16% of respondents, and until the conditions are created that allow them to conduct third-party audits, they may come under increasing pressure to relocate the parts of their operations that are impacted. A further 38% are unsure of whether they will be impacted, highlighting again how much uncertainty remains over the manner in which this new and forthcoming legislation will be implemented.

Figure 30: 16% concerned by lack of ability to conduct independent third-party audits, 40% unsure

Are you concerned by the lack of ability to conduct independent third-party audits in China in light of new legislative requirements?

N=407



EMBARGOED

46 *New rules on corporate sustainability reporting: provisional political agreement between the Council and the European Parliament*, European Council, Council of the European Union, 21st June 2022, viewed 5th April 2023, <https://www.consilium.europa.eu/en/press/press-releases/2022/06/21/new-rules-on-sustainability-disclosure-provisional-agreement-between-council-and-european-parliament/>

THE RACE TO REBUILD AFTER THE STORM

EUROPEAN BUSINESSES WEATHERED THE STORM BUT THE DAMAGE IS CLEAR

64% reported doing business in China became more difficult in 2022 (+4pp y-o-y)

62% missed business opportunities due to market access or regulatory barriers (+20pp y-o-y)

30% reported y-o-y revenue decreases in 2022, three times as many as the previous year



BUSINESS CONFIDENCE IN THE CHINA MARKET HAS SUNK – EUROPEAN COMPANIES NOW DIVERSIFYING THEIR INVESTMENTS

11% already shifted current investments out of China to other markets, **8%** shifted investments previously planned for China elsewhere

10% already shifted or plan to shift their Asia / business unit HQ out of Mainland China



75% reviewed their supply chains in last two years:

- **12%** of these already shifted related investments out of China
- **24%** of these plan to onshore their supply chains at least partially into China

Majority not expanding China operations in 2023 (**53%**, +15pp y-o-y)

China now a top-three destination for future investments for just **55%** (-13pp y-o-y, the lowest on record)

'ZERO-COVID' HAS ENDED, BUT CHALLENGES ON THE HORIZON MUST BE CAREFULLY MANAGED TO RESTORE BUSINESS CONFIDENCE

Key challenges for 2023: China's economic slowdown (top-three challenge for **36%**); global economic slowdown (**29%**); US-China trade war (**24%**); and decoupling (**15%**)

Half expect regulatory obstacles in China to increase over the next five years

59% said business became more politicised in 2022 (+9pp y-o-y), and many expect this trend to continue; **26%** faced challenges due to politicisation of customer demands



New and forthcoming **EU and US legislation** set to compel further supply chain diversification:

EU's Corporate Sustainability Reporting Directive and new and forthcoming US export control policies expected to impact **44%** and **21%** of members respectively



4% have been or expect to be directly impacted by US Uyghur Forced Labor Prevention Act; **9%** report their partners' operations have been or are expected to be impacted

16% concerned by inability to conduct independent third-party audits in China, **38%** unsure



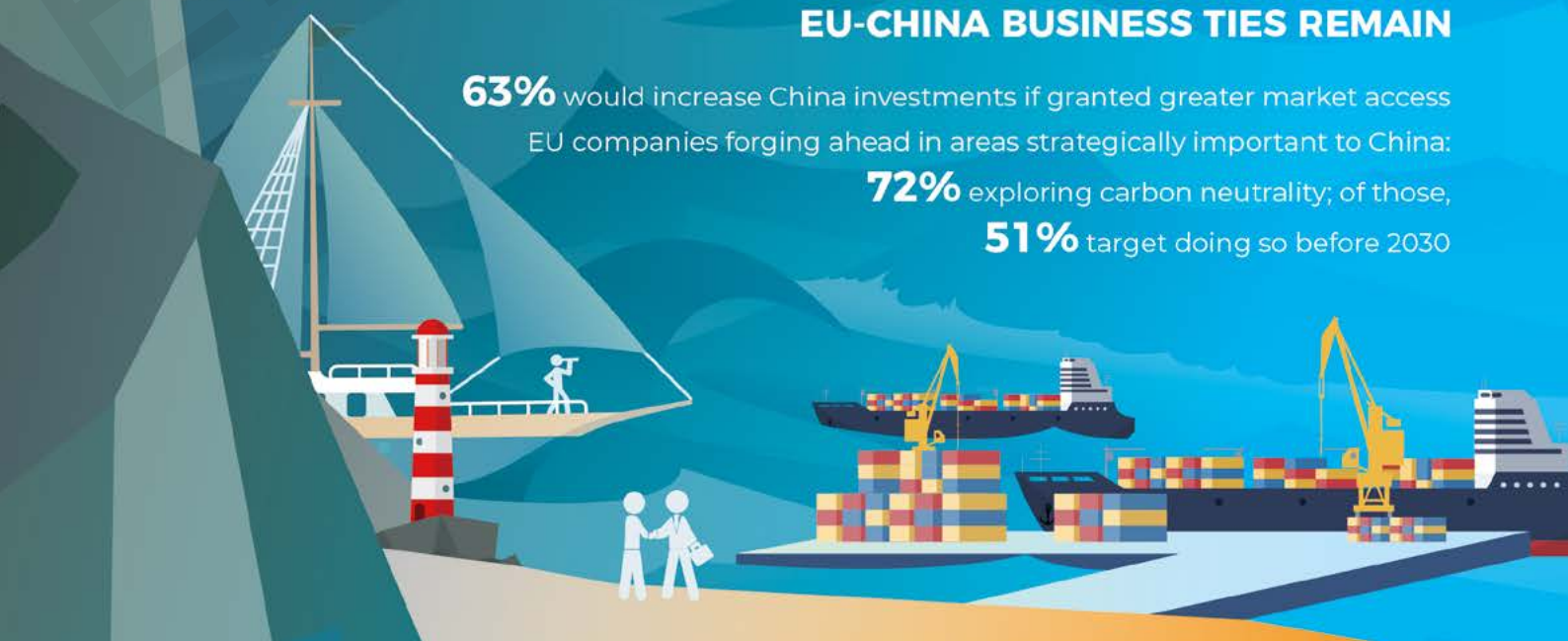
OPPORTUNITIES TO STRENGTHEN EU-CHINA BUSINESS TIES REMAIN

63% would increase China investments if granted greater market access

EU companies forging ahead in areas strategically important to China:

72% exploring carbon neutrality; of those,

51% target doing so before 2030



4 ONE STEP FORWARD, ANOTHER STEP BACK: MIXED PROGRESS WITH MARKET ACCESS AND REGULATORY BARRIERS

Although China's leadership has verbally signalled its readiness to further open its market and recommit to multilateralism and international cooperation,[47] European companies report limited evidence of this, with long-standing challenges of doing business in China continuing to impact a large percentage of survey respondents.

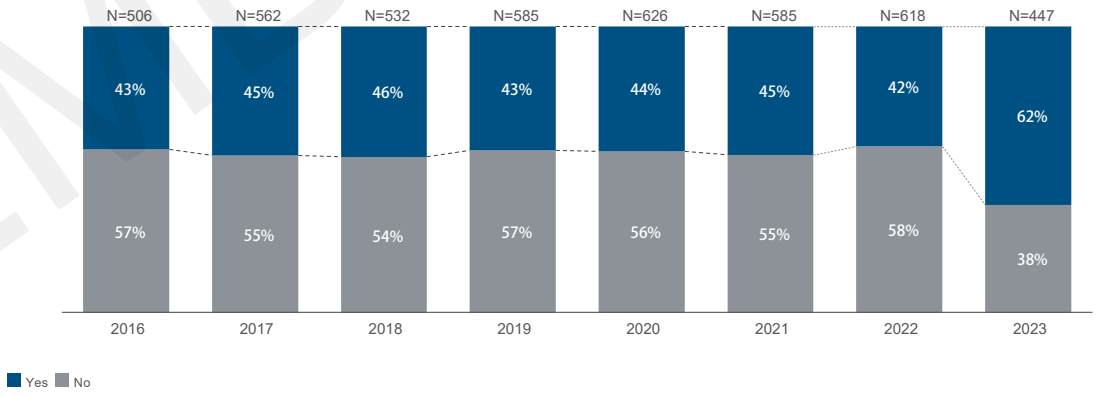
A certain degree of progress was made y-o-y in some areas, with the playing field for foreign and domestic companies becoming more level; however, regression was seen in other areas. Increased numbers reported market closing and/or being compelled to transfer technology in exchange for market access.

4.1 Lost business due to market access and regulatory barriers highest on record

A record number of respondents (62%, +20pp) report having missed business opportunities because of market access and/or regulatory barriers in 2022. Stringent pandemic control measures posed the most significant obstacle, as frequent and unpredictable lockdowns and quarantine requirements often resulted in business operations grinding to a halt.[48] Other key contributing factors included the persistence of long-standing administrative and regulatory barriers (see Figure 34), and the Chinese Government's push for technological self-reliance in strategic areas.[49]

Figure 31: Alarming number miss business opportunities as a result of market access and regulatory barriers

Has your company missed business opportunities in Mainland China as a result of market access restrictions or regulatory barriers?



47 *Vice premier reaffirms China's commitment to growth, int'l cooperation*, Ministry of Commerce of the People's Republic of China, 5th April 2023, viewed 20th February 2023, <http://gb.mofcom.gov.cn/article/chinanews/202302/20230203382657.shtml>

48 *European Business in China Position Paper 2022/2023*, European Union Chamber of Commerce in China, 21st September 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-position-paper>

49 See for example: *Xi stresses basic research for self-reliance in science and technology,* State Council, 30th April 2022, viewed 9th May 2023, <http://www.gov.cn/xinwen/2022-04/30/content_5688265.htm>

EMBARGOED

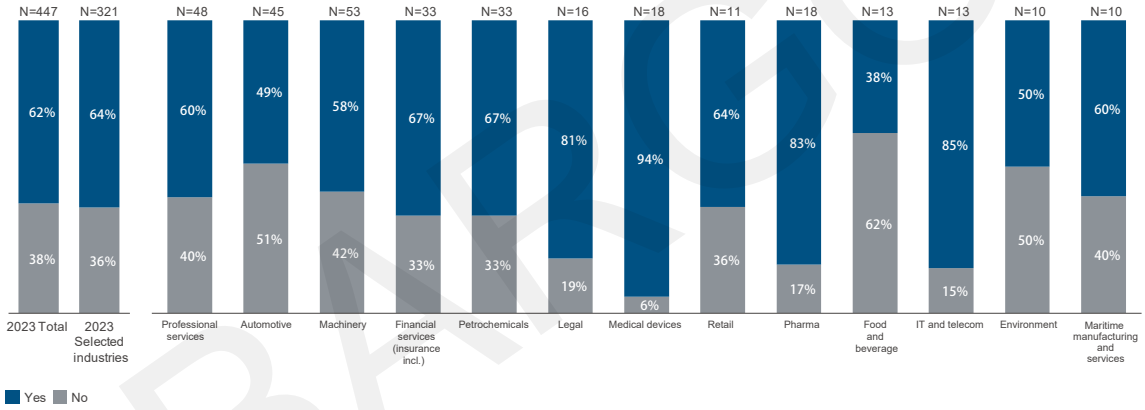
A significant majority of respondents in IT and telecommunications (85%, +47pp y-o-y) reported this to be the case. The introduction of a series of stringent laws, measures, standards and guidelines on the protection of personal information and important data in recent years is a contributing factor,[50] as is the imposition of excessive, non-transparent and at times arbitrary, supply chain controls.[51]

A large percentage of companies also missed opportunities in industries in which market access is permitted at least nominally, such as in the pharmaceutical sector, in which 83% of respondents (+25pp y-o-y) reported this to be the case. The introduction of China's VBP system,[52] as well as slower Chinese review and approval processes for drugs developed overseas,[53&54] partly account for this, illustrating how some barriers faced by firms are invisible.

Members operating across a range of sectors also missed business opportunities as a result of COVID-19-related restrictions. For example, members in the maritime manufacturing and services sector—in which 60% of respondents reported missing business opportunities (+40pp y-o-y)—were negatively impacted by China's extended suspension of international cruises, which was imposed as part of the country's 'zero-COVID' policy.[55]

Figure 32: Members face market access and regulatory barriers across the board

Has your company missed business opportunities in Mainland China as a result of market access restrictions or regulatory barriers?



1) Industries selected are those for which there were at least 10 responses

Overall, European companies are not optimistic about change within the next five years, with a third of respondents expecting no improvement and half expecting regulatory obstacles in China to increase.

50 While the European Chamber notes that the Chinese authorities have sought to improve China's data governance regulations in recent years, some requirements are overly stringent and cause operational burdens for business. These include regulatory security assessment thresholds that are relatively low, especially for larger MNCs that handle large volumes of customer or employee data, and the fact that data handlers may be unable to sign standard contracts or be certified for the cross-border handling of personal information, once a regulatory security assessment has been triggered.

51 *European Chamber Information and Communication Technology Working Group Position Paper 2022/2023*, European Union Chamber of Commerce in China, 9th September 2022, viewed 1st May 2023, <https://www.europeanchamber.com.cn/en/publications-archive/1038/Information_and_Communication_Technology_Working_Group_Position_Paper_2022_2023>

52 Under the VBP policy, a company that wins a bulk purchase bid on generic drugs secures a sizeable chunk of the Chinese pharmaceutical market and can reduce marketing outlays. However, the aggressive price-cutting required to win such bids puts a huge strain on profits, and in practice leads to a race to the bottom on pricing. This issue does not solely impact foreign firms: *Foreign Drug Giants Undercut by up to 95% in China Bidding War, Bloomberg*, 20th August 2020, viewed 5th April 2023, <https://www.bloomberg.com/news/articles/2020-08-20/foreign-drug-giants-undercut-by-up-to-95-in-china-bidding-war>

53 Gaps in harmonisation with international standards also hinder MNCs' efforts to introduce innovative medicines and vaccines in China in a timely manner.

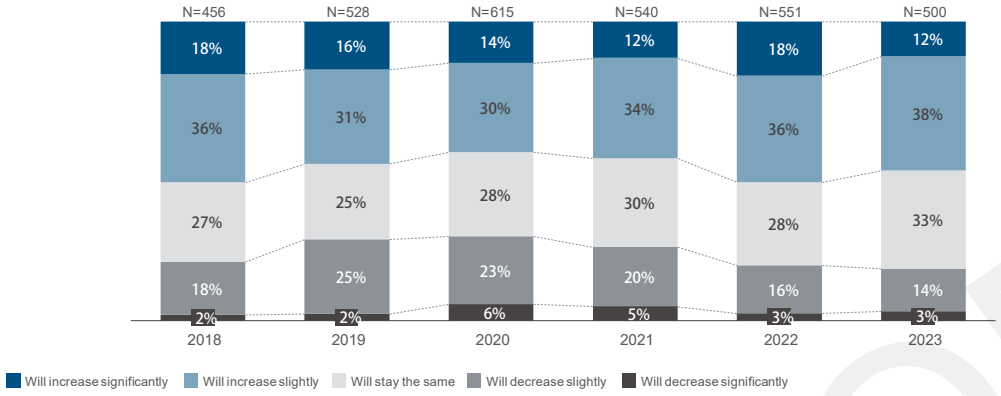
54 In China, the processing of drug review and approvals for pharmaceuticals developed abroad is slower compared to those developed by domestic companies, which has resulted in foreign pharmaceutical companies missing business opportunities. In addition, localised testing requirements for biologics and the quality of imported ingredients increase the relative time and financial costs of bringing drugs produced overseas to the Chinese market, which disproportionately hinders foreign firms: Atkinson, Robert D., *The Impact of China's Policies on Global Biopharmaceutical Industry Innovation*, Information Technology and Innovation Foundation, 8th September 2020, viewed 5th April 2023, <https://itif.org/publications/2020/09/08/impact-chinas-policies-global-biopharmaceutical-industry-innovation>

55 The impact of this was felt even more sharply among foreign-invested cruise operators, to whom China's cruise market was only partly open. European Chamber members operating in the sector reported more optimism about their prospects following the Ministry of Transport's announcement in March 2023 on the reopening of the cruise market, especially as the plan for resuming international cruises now provides equal access to Chinese and foreign-invested companies. Chan, Ho-him, *Beijing reaffirms zero-Covid commitment, Financial Times*, 7th November 2022, viewed 18th April 2023, <https://www.ft.com/content/0b699c06-08f4-4922-9b50-73c20c196738>; Zhu, Wenqian, *Chinese tourists ready to hop aboard cruise trips abroad, China Daily,* 10th April 2023, viewed 18th April 2023, <https://www.chinadaily.com.cn/a/202304/10/WS64334870a31057c47ebb91e7.html>

EMBARGOED

Figure 33: More regulatory obstacles expected

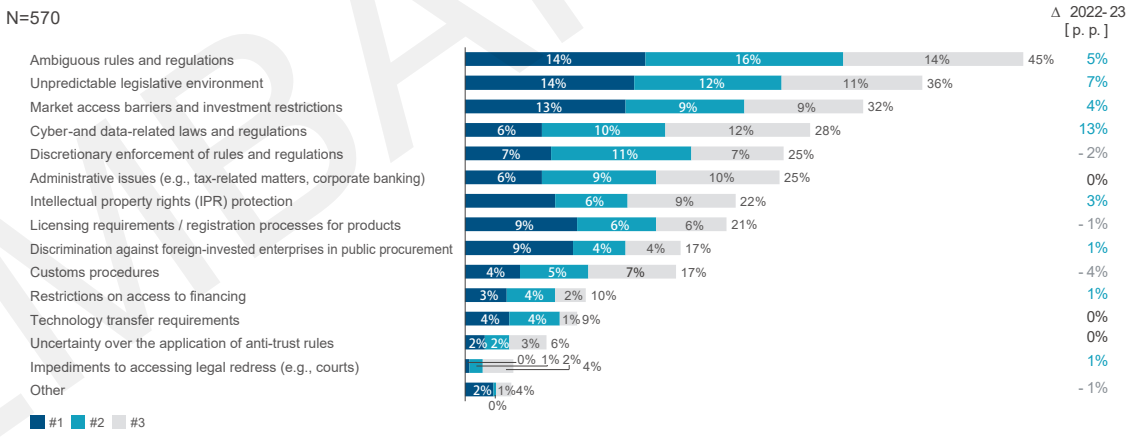
How do you expect the number of regulatory obstacles your company is facing in Mainland China to change over the next five years?



Ambiguous rules and regulations ranked as the top regulatory obstacle members face for the seventh year running, demonstrating just how little has improved in China's regulatory environment.

Figure 34: Ambiguous regulations and unpredictable legislative environment top regulatory obstacles

Which are the top three most significant regulatory obstacles for your company when doing business in Mainland China? 1)



1) Figures represent the proportion of respondents who rated each issue their #1-3 most significant regulatory obstacles;

While some challenges are almost universal—such as the persistence of ambiguous rules and regulations and market access constraints—others are sector-specific. For example, licensing requirements / registration processes are less of an issue for those in professional services, automotive and retail, but are a significant problem for the medical devices, petrochemicals, F&B, and aviation and aerospace sectors. Similarly, while discrimination against foreign-invested enterprises (FIEs) in public procurement does not pose a significant barrier for many industries, it is a key challenge for members operating in the medical devices, civil engineering, and IT and telecommunications sectors.

EMBARGOED

Figure 35: The top regulatory obstacles by sector (part 1)

Which are the top three most significant regulatory obstacles for your company when doing business in Mainland China? 1) 2) 3)

N=570	Professional services N=63	Automotive N=60	Machinery N=62	Financial services N=40	Petrochemicals N=42	Legal N=19	Medical devices N=24	Retail N=14
Ambiguous rules and regulations	3	1	1	1	2	5	4	5
Unpredictable legislative environment	4	2	4	3	1	3	4	4
Market access barriers and investment restrictions	1	3	12	2	4	1	2	3
Cyber-and data-related laws and regulations	6	4	5	4	7	3	7	1
Discretionary enforcement of rules and regulations	6	6	3	7	5	5	7	6
Administrative issues (e.g., tax-related matters, corporate banking)	2	8	8	6	7	2	9	6
Intellectual property rights (IPR) protection	10	5	2	10	10	9	9	1
Licensing requirements / registration processes for products	9	11	9	5	3	7	3	8
Discrimination against foreign-invested enterprises in public procurement	4	10	6	8	9	11	1	14
Customs procedures	14	6	6	13	6	11	9	8
Restrictions on access to financing	8	14	11	9	11	8	12	8
Technology transfer requirements	10	9	10	13	11	15	6	8
Uncertainty over the application of anti-trust rules	14	12	14	12	13	13	14	8
Impediments to accessing legal redress (e.g., courts)	12	15	15	11	15	9	14	13

Figure 36: The top regulatory obstacles by sector (part 2)

Which are the top three most significant regulatory obstacles for your company when doing business in Mainland China? 1) 2) 3)

N=570	Pharma N=22	Civil eng. N=11	Food and beverage N=21	IT and telecom N=15	Environ. N=11	Transportation N=11	Utilities N=10	Aviation and aerospace N=11	Maritime manufacturing and services N=12
Ambiguous rules and regulations	2	1	1	3	4	1	1	2	1
Unpredictable legislative environment	3	2	9	11	1	3	2	8	3
Market access barriers and investment restrictions	1	13	10	3	9	3	4	8	5
Cyber-and data-related laws and regulations	3	9	4	1	9	8	3	4	12
Discretionary enforcement of rules and regulations	6	3	6	3	11	2	4	7	7
Administrative issues (e.g., tax-related matters, corporate banking)	8	7	8	6	8	5	14	12	12
Intellectual property rights (IPR) protection	3	9	6	8	3	10	6	8	7
Licensing requirements / registration processes for products	10	6	1	7	6	5	8	1	11
Discrimination against foreign-invested enterprises in public procurement	6	3	13	2	4	11	10	5	4
Customs procedures	12	9	3	14	11	7	13	3	7
Restrictions on access to financing	12	3	10	9	2	11	10	12	5
Technology transfer requirements	12	9	12	11	6	8	6	5	2
Uncertainty over the application of anti-trust rules	9	13	4	11	14	11	8	12	7
Impediments to accessing legal redress (e.g., courts)	15	15	14	14	11	11	10	12	14

1) *Numbers in the table give the relative ranking of each issue to the others for each sector. The importance of each issue is ranked by the weighted total.*
2) *Not all challenges are listed.*
3) *Industries selected are those for which there were at least 10 responses*

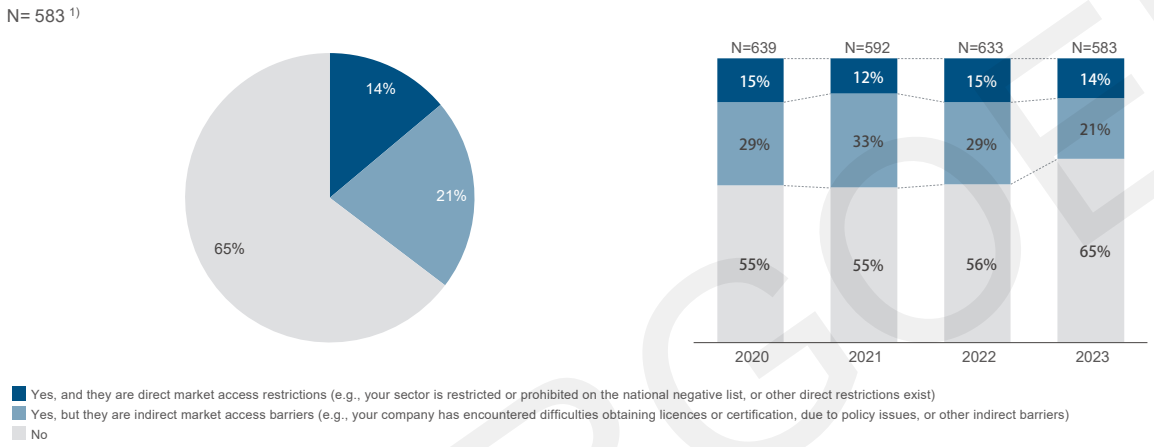
EMBARGOED

4.2 Baby steps in market opening

One in seven respondents face direct market barriers, such as China's negative lists,[56] while indirect barriers—which include complex and time-consuming administrative approval requirements and *de facto* obstacles to obtaining operating licences—are encountered by 21%. The continued existence of indirect market barriers illustrates that, for many industries, nominal market opening is not necessarily meaningful.

Figure 37: Market access restrictions faced by a third

Does your company face market access restrictions in China?

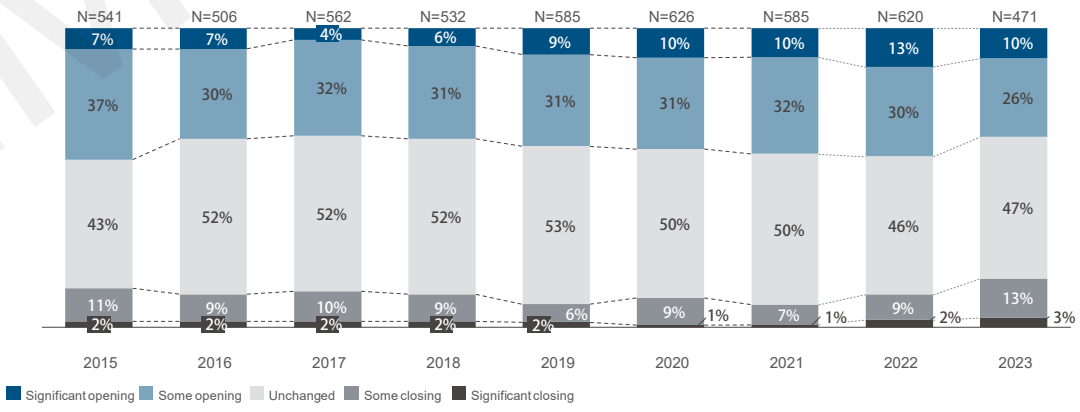


1) Multiple answers possible; percentages based on the total number of responses

Access to China's market improved for just over a third of respondents in 2022, (36%, -7pp y-o-y). At the same time, one in two respondents saw no changes to market access during 2022, and a record-high proportion (16%, +5pp y-o-y) said their industry became more closed.[57]

Figure 38: Market creaks open for some, closes for others

Has there been any market opening in your industry in Mainland China for foreign companies (y-o-y)?



56 China's negative lists are released annually by the Ministry of Commerce and National Development and Reform Commission. They outline the country's restricted and prohibited sectors for investment and market access: *Special Administrative Measures for Foreign Investment Access (Negative List) (2021 Edition)*, National Development and Reform Commission and Ministry of Commerce, 27th December 2021, viewed 22nd April 2022, <https://www.ndrc.gov.cn/xxgk/zcfb/fzggwl/202112/t20211227_1310020.html?code=&state=123>; *Notice on the issuance of the Negative List for Market Access (2022 Edition)*, National Development and Reform Commission and Ministry of Commerce, 25th March 2022, viewed 22nd April, <https://www.ndrc.gov.cn/xxgk/zcfb/ghxwj/202203/t20220325_1320231.html?code=&state=123>

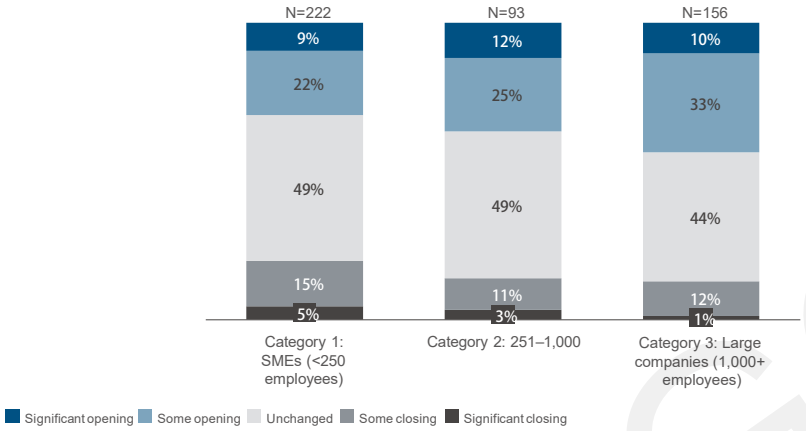
57 This question first featured in the BCS in 2015 and has been asked annually since.

EMBARGOED

The picture varies by company size, with a far higher proportion (43%) of multinational companies (MNCs) reporting improved market access y-o-y compared to SMEs (31%). A higher proportion of SMEs also experienced market closing, with 20% reporting this to be the case compared to 13% of MNC respondents.

Figure 39: Big fish welcome, small fry kept at arm's length

Has there been any market opening in your industry in Mainland China for foreign companies (y-o-y)?

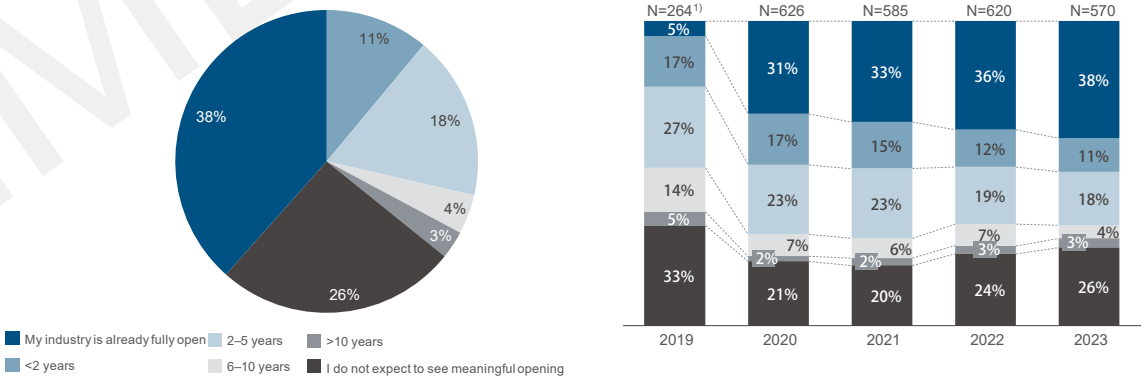


Expectations of when meaningful market opening will occur vary substantially. Almost four in 10 respondents reported that their industry is already fully open; a further 29% reported they expect full opening to take place in the next five years; 7% do not expect meaningful market opening to occur within the next five years; and 26% do not expect to see meaningful market opening at all.

Figure 40: More than a quarter see no chance of meaningful market opening

When do you expect to see meaningful opening in your industry?

N=570



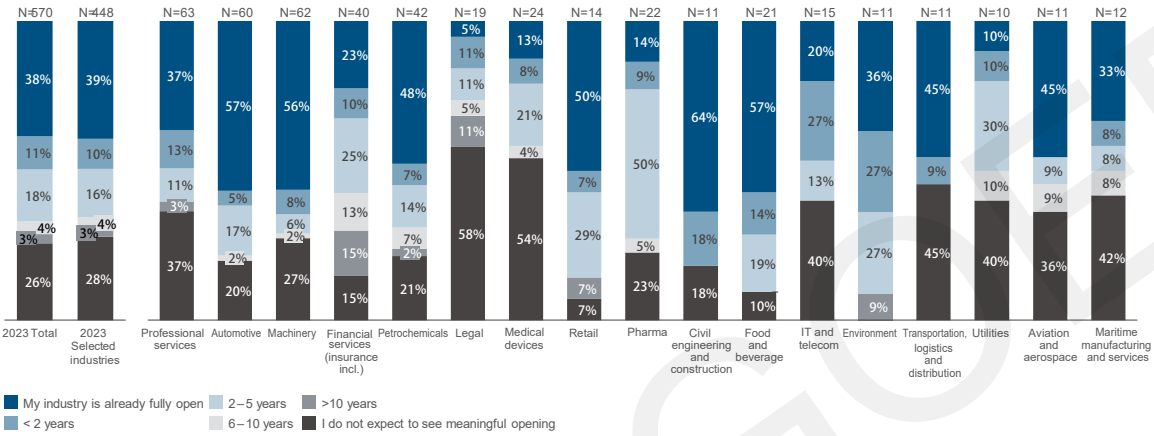
1) *Numbers in 2019 not fully comparable, due to question only being asked to respondents that did not answer "No" to the question "Does your company face market access restrictions in China?" that year*

EMBARGOED

At the sectoral level, a majority of respondents in civil engineering and construction (64%), F&B (57%), automotive (57%) and machinery (56%) reported that their sector is already fully open. By contrast, a majority of members operating in the legal (58%) and medical devices (54%) sectors never expect to see meaningful market opening.

Figure 41: Market access prospects vary substantially from sector to sector

When do you expect to see meaningful opening in your industry? [1)]



1) *Industries selected are those for which there were at least 10 responses*

4.3 More investment waiting on increased market access

The market access and regulatory barriers that European companies face have a detrimental impact on investment flows. As was the case in the past two years, almost two thirds of respondents would be willing to increase investment in China, should they be granted greater market access.

This is already happening in industries where market access has been expanded. For example, in the automotive industry, the lifting of ownership restrictions resulted in one large European automotive manufacturer increasing its stake in its JV partner in the first half of 2022, an investment that accounted for over 50% of total EU foreign-direct investment (FDI) into China during that period.[58] Large investments have also been made in the petrochemicals industry, after European companies received approvals to invest as wholly foreign-owned enterprises.[59]

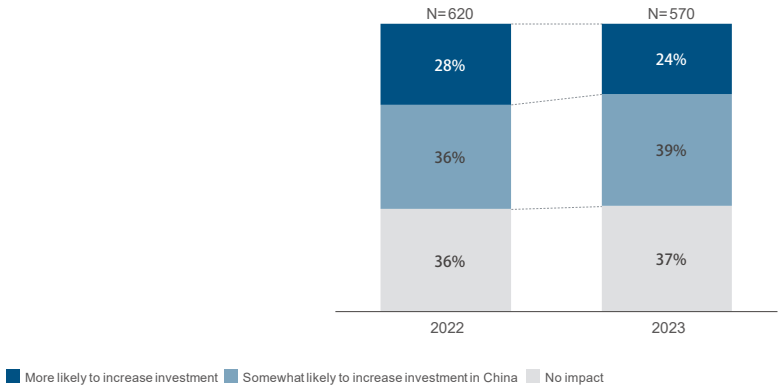
58 Kratz, Agatha; Barkin, Noah & Dudley, Lauren, *The Chosen Few: A Fresh Look at European FDI in China*, Rhodium Group, pp. 3–4, 14th September 2022, viewed 5th April 2023, <https://rhg.com/research/the-chosen-few/>

59 *European Business in China Business Confidence Survey 2021*, European Union Chamber of Commerce in China, pp. 20–22, 8th June 2021, viewed 6th April 2023, <https://www.europeanchamber.com.cn/en/publications-archive/917/Business_Confidence_Survey_2021>

EMBARGOED

Figure 42: Majority would likely increase investments with more market access

If greater market access were to be granted to foreign companies in your industry, how would this impact your company's investment decisions in Mainland China?

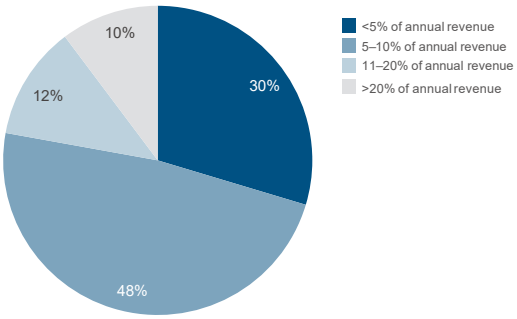


If China did increase market access for foreign companies, the untapped investment is not inconsiderable. Nearly half of respondents would likely increase investments by between 5–10% of their annual revenue, 12% would likely increase investments by 11–20%, and one in 10 by more than 20%.

Figure 43: Over a fifth willing to increase investment by more than 10% of annual revenue

By how much would you be likely to increase your company's investments into China? [1)]

N=361



1) Question asked to respondents that did not answer 'No impact' to the question, "If greater market access were to be granted to foreign companies in your industry, how would this impact your company's investment decisions in Mainland China?"

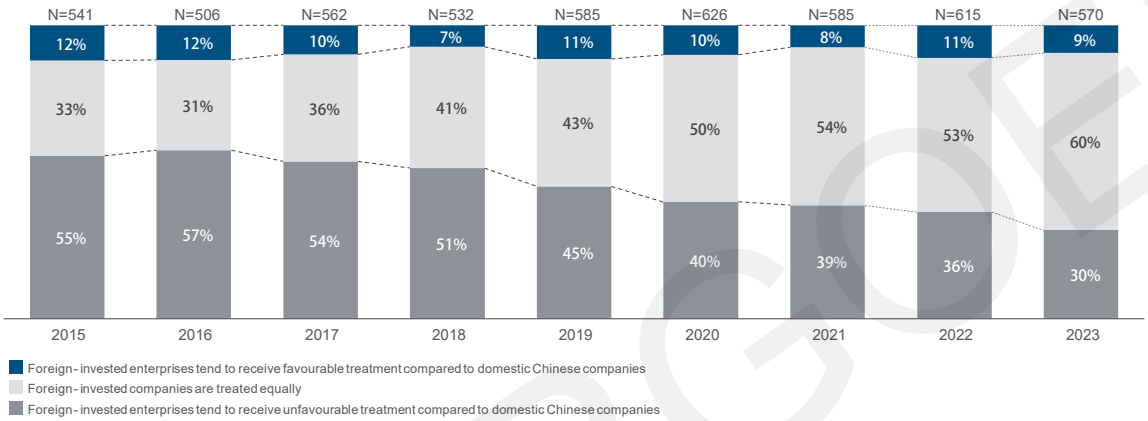
EMBARGOED

4.4 Playing field becomes slightly more level

There was a 7pp increase in the proportion of European companies that report experiencing equal treatment for foreign companies in China. At the same time, three in 10 continue to find the field tilted against them, and a further 9% say they are actually treated more favourably than domestic Chinese companies.

Figure 44: 60% say playing field is level

How does your company perceive foreign-invested enterprises' treatment in your industry compared to that of domestic Chinese companies?



At the industry level, companies operating in strategic sectors, or sectors with high concentrations of Chinese national champions—such as environmental, transport, logistics and distribution, medical devices, and IT and telecommunications—find the playing field substantially tilted against them. By contrast, sectors not deemed strategic by the Chinese Government—such as F&B or retail—or industries in which foreign expertise is needed to help China break technological bottlenecks and climb value chains—including machinery, aviation and aerospace, and petrochemicals—the picture is more balanced.[60&61]

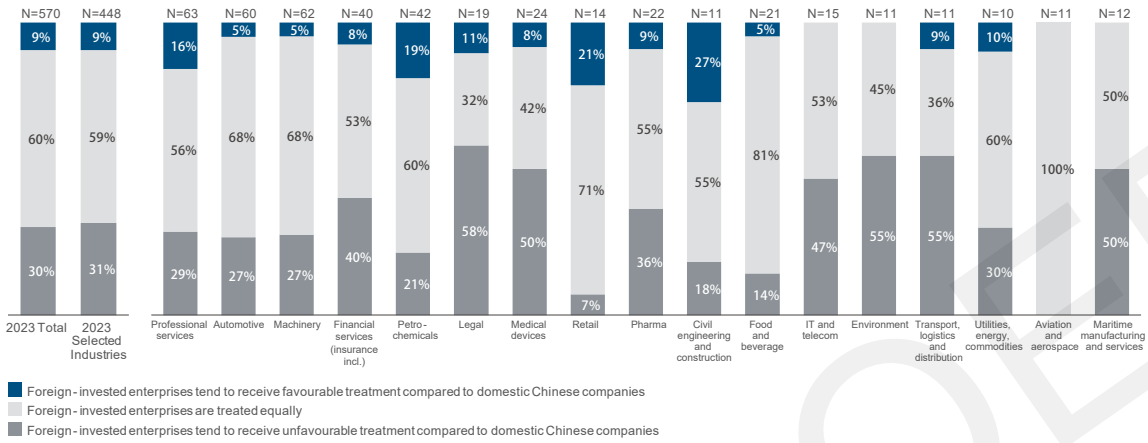
60 For more on this point, see: *Decoupling: Severed Ties and Patchwork Globalisation*, European Union Chamber of Commerce in China and MERICS, 14th January 2021, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-decoupling>

61 For a deep dive on how the differing treatment of foreign firms in China, as well as other market and regulatory barriers, impacts European companies' R&D strategies in the country see: *China's Innovation Ecosystem: The Localisation Dilemma*, European Union Chamber of Commerce in China and MERICS, 21st April 2023, viewed 9th May 2023, <https://www.europeanchamber.com.cn/en/publications-archive/1077/China_s_Innovation_Ecosystem_the_localisation_dilemma>

EMBARGOED

Figure 45: Equal treatment varies greatly by sector

How does your company perceive foreign-invested enterprises' treatment in your industry compared to that of Chinese companies? 1)



1) *Industries selected are those for which there were at least 10 responses*

The main area in which respondents report experiencing differentiated treatment remains market access (43%), with other common areas including communication with the Chinese Government (30%), government procurement (28%) and access to subsidies (27%).

Figure 46: Where European companies experience differentiated treatment

In which areas have you experienced differentiated treatment? 1)2)

N=226

		Δ 2022–23 [p. p.]
Market access	43%	-2%
Communication with the government	30%	-2%
Government procurement	28%	n/a
Access to subsidies	27%	2%
Administrative issues (e.g., registering a business, tax-related matters, corporate banking)	22%	3%
Licensing (product / service licences)	18%	-3%
Access to policy and standard-setting groups	17%	-3%
SOE procurement	16%	n/a
Accountability on compliance issues	15%	0%
Environmental enforcement	14%	-3%
Access to finance	13%	0%
Tax issues	12%	-2%
IPR enforcement	9%	2%
Labour enforcement	9%	-1%
Customs procedures	7%	-6%
Other	5%	4%
Forced relocation of offices / factories	5%	-3%
Access to legal redress (e.g., courts)	4%	-2%

1) *Multiple answers possible*

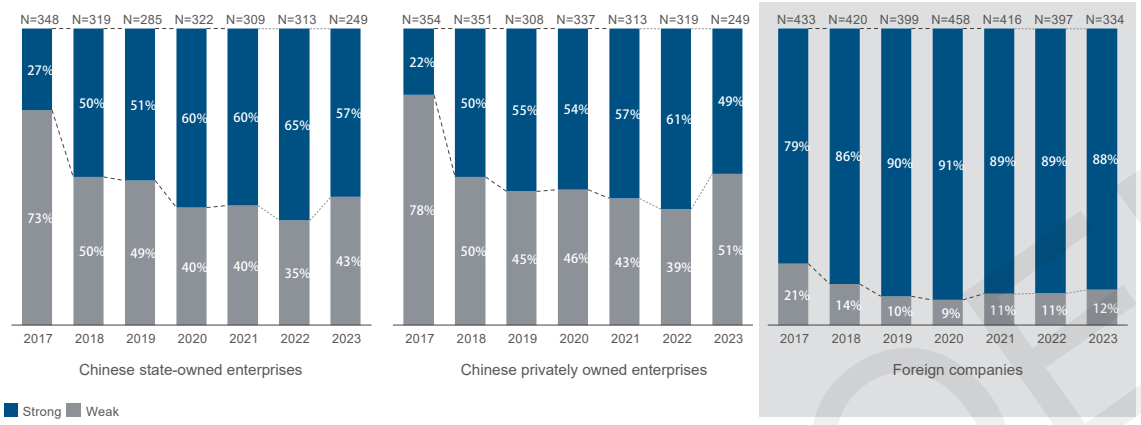
2) *n/a refers to a new option or an option that is different from the previous year*

Unequal enforcement of environmental regulations is another area in which foreign businesses report experiencing differentiated treatment. Some believe the reason they are singled out for a disproportionate number of environmental assessments is in part because FIEs typically meet or exceed compliance standards—meaning officials can complete their quota for checks quickly and maintain good environmental track records—and in part to deliberately disadvantage foreign firms.

EMBARGOED

Figure 47: Enforcement of environmental regulations remains uneven

How does your company assess the enforcement of environmental regulations in China against different companies?



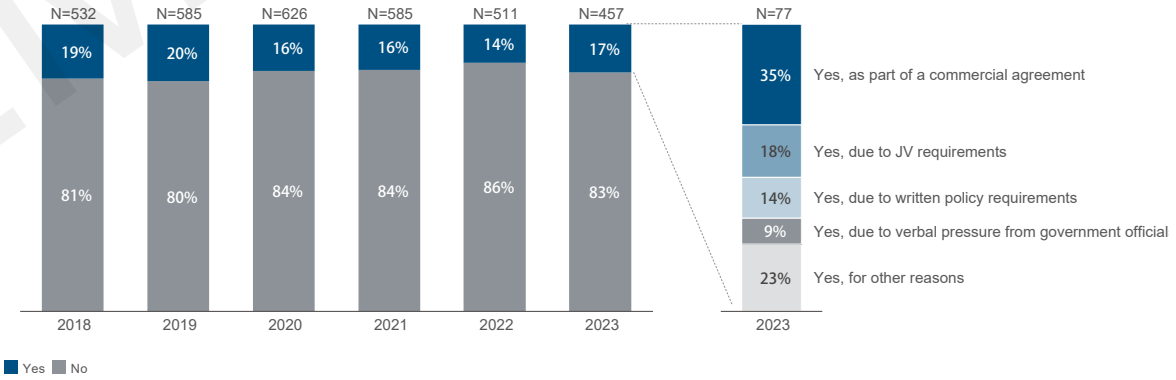
4.5 Compelled technology transfers increase

In 2022, there was a slight increase in the number of respondents that report having been compelled to transfer technology and/or trade secrets in exchange for market access (17%, +3pp). It is concerning that 53% of those report that the compelled technology transfer either happened within the previous year or was still taking place at the time of the survey.

Of those compelled to transfer technology or trade secrets, over half say instances were due to a commercial agreement or JV requirements. However, 23% report that it happened due to written policy requirements or verbal pressure from government officials. Although this is an 8pp y-o-y improvement, it indicates that the 2020 Foreign Investment Law—which prohibits technology transfers by administrative means—is not being fully enforced.[62]

Figure 48: One in six compelled to transfer technology

Has your company felt compelled to transfer technology and/or trade secrets in order to maintain market access?

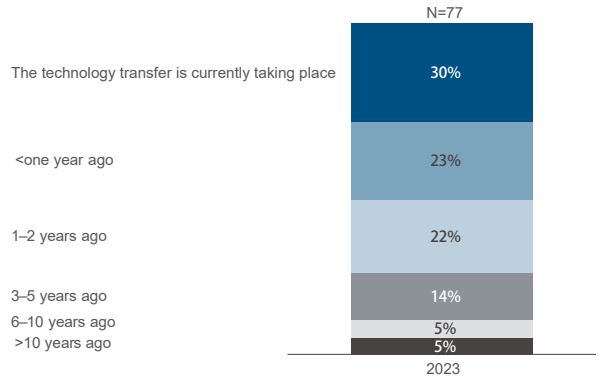


62 *Foreign Investment Law of the People's Republic of China*, National Development and Reform Commission, 24th February 2021, viewed 9th May 2023, <https://en.ndrc.gov.cn/policies/202105/t20210527_1281403.html>

EMBARGOED

Figure 49: Majority of compelled technology transfers occurred post-FIL

How long ago did the compelled transfer take place?

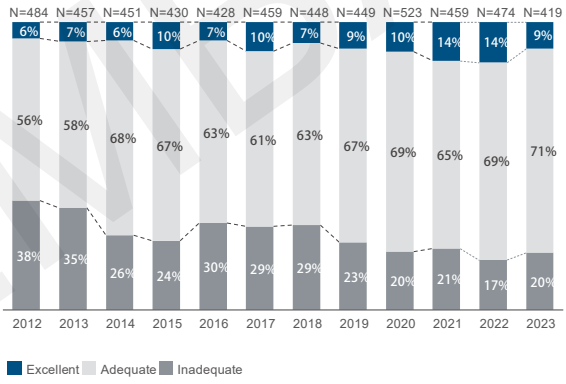


4.6 Effectiveness and enforcement of intellectual property rights (IPR) laws and regulations remains a concern

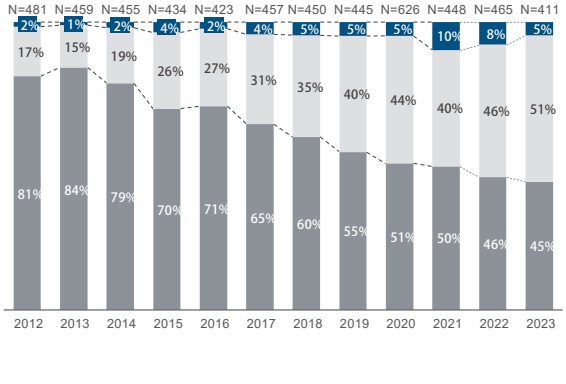
One in five report that China's written IPR laws and regulations are inadequate (20%, +3pp). Close to half of all respondents (45%) view this to be the case when it comes to the enforcement of IPR laws and regulations, a 1pp improvement y-o-y.

Figure 50: Almost half find enforcement of IPR laws and regulations inadequate

How does your company rate the effectiveness of China's written intellectual property (IP) protection laws and regulations?



How does your company rate the enforcement of China's IPR laws and regulations?



EMBARGOED

5 POLITICS CONTINUES TO SPILL OVER INTO BUSINESS

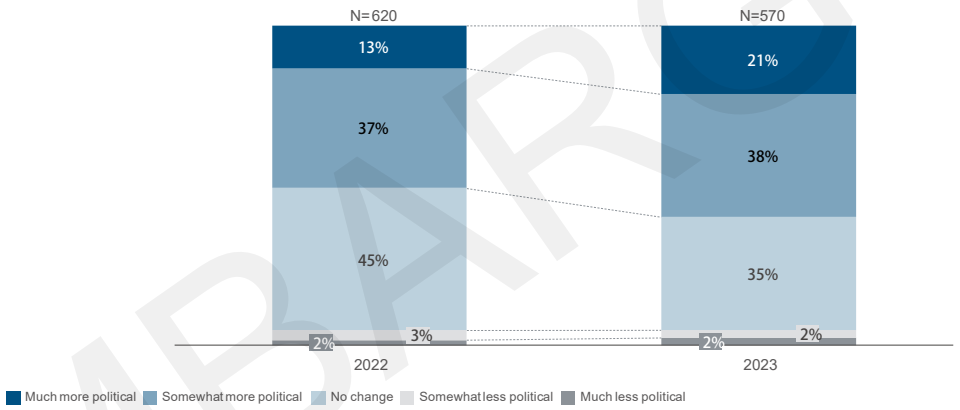
There was a wealth of geopolitical developments in 2022 that negatively impacted business. Russia invaded Ukraine,[63] a diversification debate gained traction in the EU,[64] and US-China tensions were ratcheted up.[65] As a result, European companies are facing increased political pressure from Chinese, European and third-party stakeholders, and are being pulled in different directions as consumer demands become increasingly politicised.

5.1 Business became more politicised (again)

In the BCS 2023, 59% of respondents (+9pp y-o-y) reported that China's business environment became more politicised in 2022, with only 4% saying it became less so.

Figure 51: Majority report increased politicisation in last 12 months

Has the business environment in China become more political in the last year?



The Chinese Government is perceived as the main source of increased political pressure, as reported by nearly two-thirds of respondents, followed by the Chinese media (46%) and international media (45%).

63 The invasion sparked widespread supply chain complications and promoted scenario planning to take place in European companies' HQs, following increased concern that China could take similar actions against Taiwan. An April 2022 flash survey conducted by the European Chamber found that 65% of respondents had experienced logistical challenges as a result of the war in Ukraine. *Flash Survey: COVID-19 and the War in Ukraine: The Impact on European Business in China*, European Union Chamber of Commerce in China, 5th May 2022, viewed 5th April 2023, <https://www.europeanchamber.com.cn/en/publications-archive/973/Flash_Survey_COVID_19_and_the_War_in_Ukraine_The_Impact_on_European_Business>

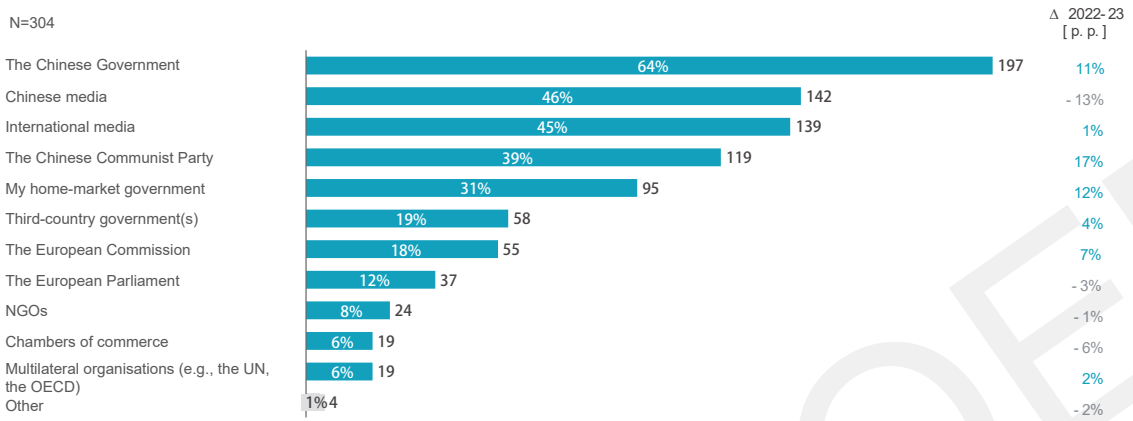
64 Foy, Henry, *EU ministers advised to take tougher line on China*, *Financial Times*, 17th October 2022, viewed 6th April 2023, <https://www.ft.com/content/b83615cb-6db0-4e67-85a3-7aab131abeb5>

65 Flash points in 2022 included US House Speaker Nancy Pelosi's August 2022 visit to Taiwan, and the introduction of legislation, including the US UFLPA and a series of export controls aimed at curtailing China's ability to develop advanced semiconductor technology.

EMBARGOED

Figure 52: Chinese Government and media top sources of politicisation

How has your industry's business environment changed over the past year?

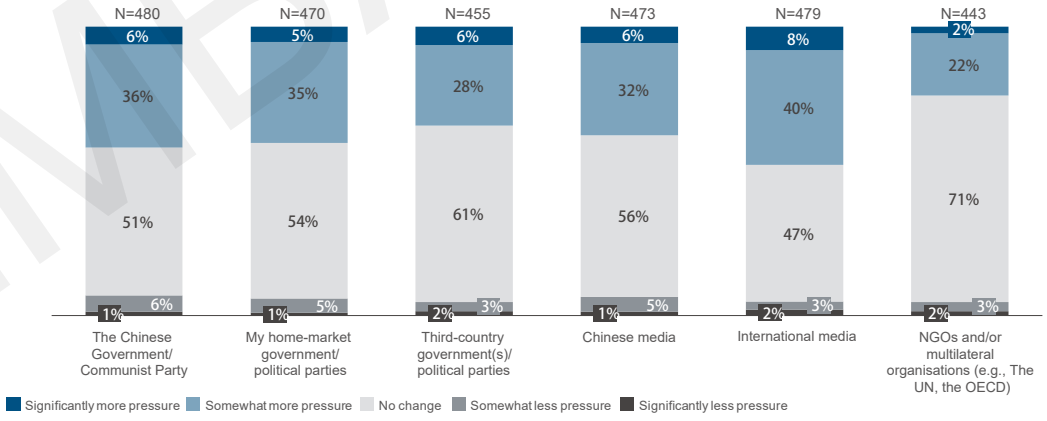


1) Excluding answer "None of the above"

A large percentage of respondents foresee the situation getting worse before it gets better. Nearly half (48%) expect increased pressure from international media. Similarly high numbers expect increased pressure from the Chinese Government/Communist Party (42%), their home-market government/political parties (40%) and Chinese media (38%). A third of respondents expect increased pressure from third-country government(s)/political parties (34%).

Figure 53: Politicisation of business expected to continue

Does your company expect to see its business operations put under more or less political pressure by the following over the next 12 months? [1)]



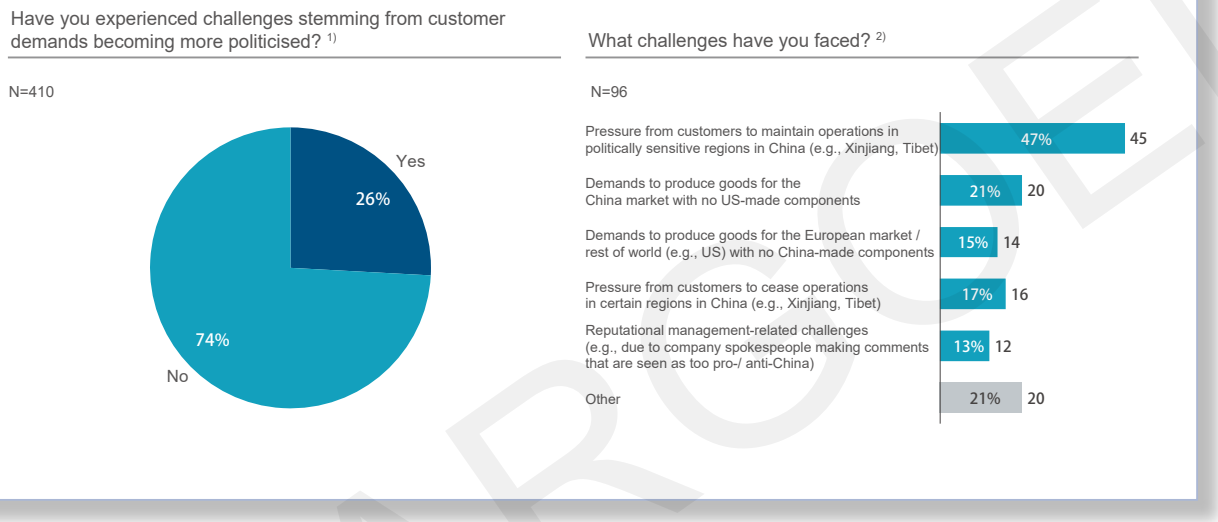
1) Excludes respondents that responded 'Not applicable'

EMBARGOED

5.2 Politicisation of consumer demands

Over a quarter of respondents (26%) reported challenges as a result of consumer demands becoming more politicised, with some facing conflicting requests from Chinese and Western stakeholders. Of those that faced challenges, almost half (47%) reported pressure from customers to maintain operations in politically sensitive regions of China, while almost a fifth (17%) experienced pressure from customers to cease their operations in those same regions. Competing demands to produce goods containing either no China- or no US-made components has also emerged as a challenge as US-China tensions escalated.

Figure 54: More than a quarter note consumer demands becoming more politicised



1) *Excludes respondents that responded 'Don't Know'*
2) *Multiple answers possible*

EMBARGOED

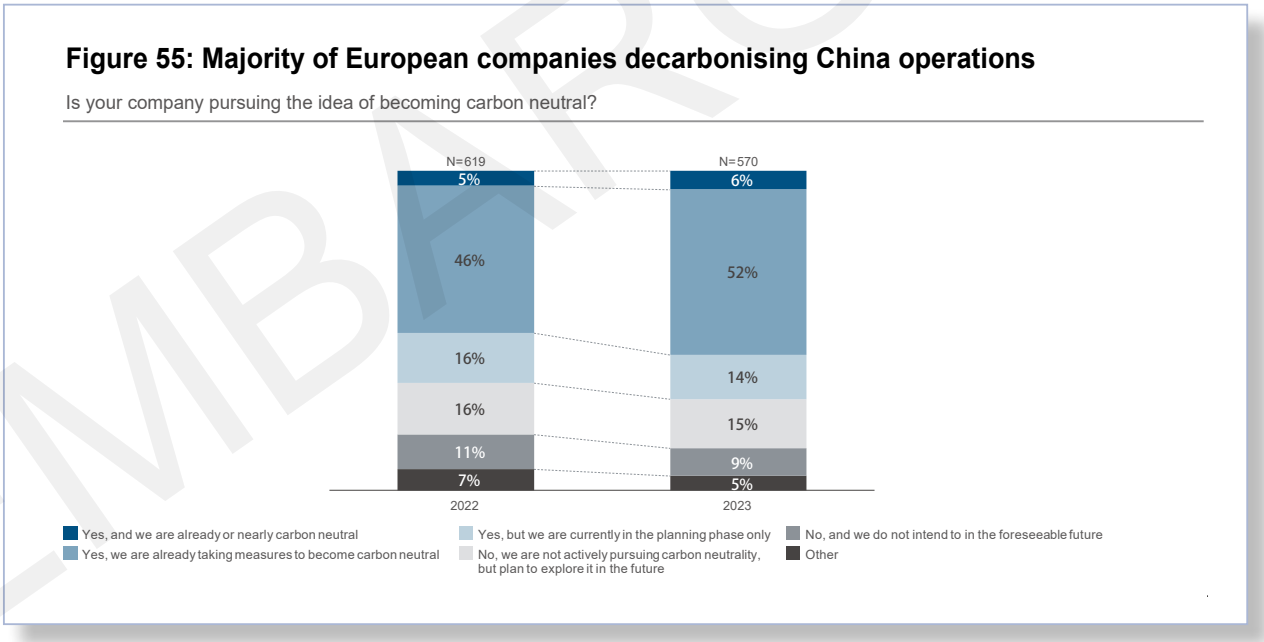
6 GOVERNMENT ACTION NEEDED FOR EU FIRMS TO CONTRIBUTE FULLY TO CHINA'S 30/60 GOALS

Decarbonisation is a key policy priority for the Chinese Government, which targets peaking carbon dioxide emissions before 2030 and achieving carbon neutrality by 2060 (30/60 Goals).[66] However, while China is making some progress towards 2060, European companies—a significant number of which target carbon neutrality by 2030—face barriers that could prevent them from both meeting their corporate pledges and contributing fully to China's 30/60 Goals. Key challenges include limited access to renewable energy, a lack of clear policy guidance, the need for China to reform its energy system, a lack of necessary technology and issues relating to China's emissions trading system (ETS).[67]

6.1 European firms prioritising decarbonisation

A total of 6% of respondents (+1pp y-o-y) have already or nearly achieved carbon neutrality. A further 52% are actively taking measures to become carbon neutral, a 6pp y-o-y increase, while less than a tenth do not intend to pursue carbon neutrality in the foreseeable future.

Figure 55: Majority of European companies decarbonising China operations



Driven by growing consumer demand for green products and services, global corporate targets and strict EU regulations,[68] 95% of BCS 2023 respondents currently pursuing carbon neutrality aim to decarbonise their China operations by 2050. Furthermore, almost half (46%) of this group aim to achieve carbon neutrality by 2030, while 5% report having already done so.

66 Farand, Chloé & Darby, Megan, *Xi Jinping: China will aim for carbon neutrality by 2060, Climate Home News*, 22nd September 2020, viewed 4th April 2023, <https://www.climatechangenews.com/2020/09/22/xi-jinping-china-will-achieve-carbon-neutrality-2060/>

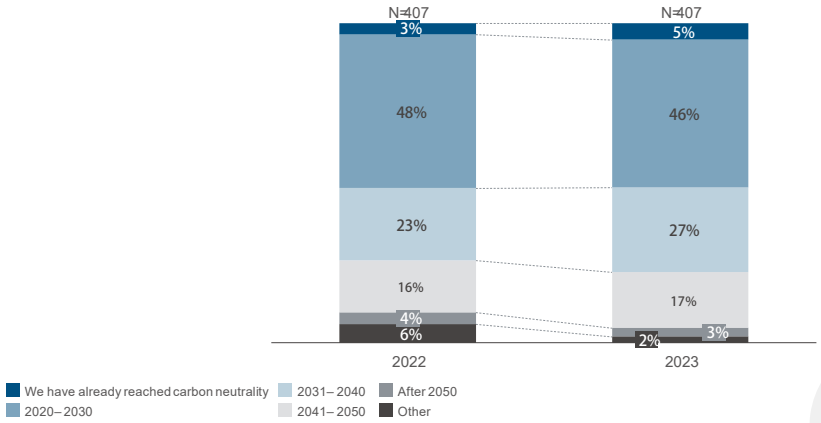
67 *Carbon Neutrality: The Role of European Business in China's Race to 2060*, European Union Chamber of Commerce in China, 25th March 2023, viewed 4th April 2023, <https://www.europeanchamber.com.cn/en/publications-carbon-neutrality-report>

68 Ibid.

EMBARGOED

Figure 56: Majority aim to decarbonise before 2050

When does your company aim to reach carbon neutrality? 1)2)



1) *Asked only to members that answered 'Yes, and we are already or nearly carbon neutral'; 'Yes, we are already taking measures to become carbon neutral', or 'Yes, but we are currently in the planning phase only,' to the question "Is your company pursing the idea of becoming carbon neutral?"*
2) *The disparity in the percentage that reported 'Yes, and we are already or nearly carbon neutral' in Figure 55 and 'We have already reached carbon neutrality' in Figure 56 is attributable to differences in wording of these two responses*

6.2 How European companies are achieving carbon neutrality

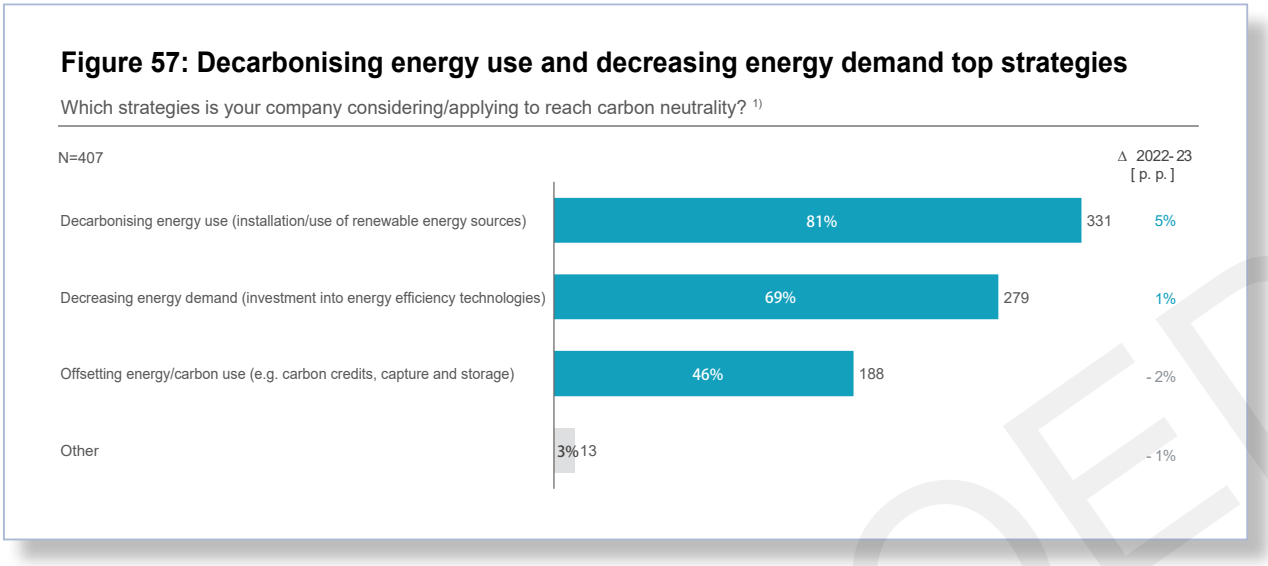
European companies are employing or considering a number of strategies to achieve carbon neutrality: access to reliable sources of green energy is imperative, with 81% of respondents looking to decarbonise their energy use (+5pp y-o-y) as part of their overall strategy; almost 70% are looking to decrease their overall energy use by improving their energy efficiency; and just less than half (46%) are investing in offsetting strategies, such as carbon credits and carbon capture, utilisation and storage technologies.

This fits with China's priorities to increase renewable energy capacity and access, and improve energy efficiency and conservation, through the promotion of production and manufacturing excellence.[69] China has an opportunity to accelerate its decarbonisation drive by fully opening its market to European companies that are aggressively pursuing carbon-neutral strategies, as well as those that can introduce cutting-edge products and management systems that promote decarbonisation.

EMBARGOED

69 *Xi Focus: Xi announces China aims to achieve carbon neutrality before 2060, Xinhua*, 9th September 2020, viewed 4th April 2023, <http://www.xinhuanet.com/english/2020-09/23/c_139388764.htm>

Figure 57: Decarbonising energy use and decreasing energy demand top strategies



1) Multiple answers possible

6.3 Achieving 30/60 Goals requires immediate government action

Limited access to renewable energy, an issue for 71%, continues to be the main barrier that risks preventing European companies from achieving their carbon neutrality targets in China. This challenge is underpinned by China's reliance on fossil fuels for power generation,[70] as well as the lack of coordinated power infrastructure and a well-functioning market for green energy in the country.[71]

More than half of respondents (54%) report that a lack of industrial guidance and best practice references risks derailing their efforts, underlining the need for a clear roadmap to 2060 for all sectors of the economy. Companies need a full understanding of the technologies that will be prioritised to advance towards carbon neutrality to enable them to start making informed investment decisions now.[72] One example of this is in the maritime manufacturing and industrial services sector, in which there are currently no policies or regulations geared toward integrating international technology into China's domestic shipping industry. Members in the sector lack clarity on which fuel sources can be expected to prevail in the industry in the future. As a result, few shipowners are prepared to invest in new fuels sources and technologies—such as synthetic fuels, hydrogen, biofuels and electrification—currently being piloted for the shipping sector, which will have a knock-on effect on China's decarbonisation efforts.[73]

Uncertainties over China's national ETS was reported as a top-three issue by 53% of respondents. China's lack of a low carbon culture also ranked as a top challenge, impacting 46% of respondents. Key hurdles in this regard include limited consumer awareness of green products, and the limited promotion of more holistic green practices, such as developing a circular economy.[74]

As identified in the European Chamber's report *Carbon Neutrality: The Role of European Businesses in China's Race to 2060*, measures that the Chinese authorities could adopt to address these challenges include facilitating the promotion of green value chains and shared international standards to help reduce both the costs of innovation and the risks of bringing new technologies to market; instituting consultation platforms between local government and industry to ensure decarbonisation-related policies are well understood and fit for purpose; and optimising China's ETS by introducing a

70 Rogers, Jason, Chen, Qian, Chen, Sarah & Zhu, Winnie, *China Posts Record Fossil Fuel Output as Security Trumps Climate*, *Bloomberg*, 17th January 2023, viewed 9th May 2023, <https://www.bloomberg.com/news/articles/2023-01-17/china-posts-record-fossil-fuel-output-as-security-trumps-climate#xj4y7vzkg?leadSource=uverify%20wall>; Wells, Wendy, *CHINA DATA: 2022 power demand growth eases to 3.6% in 2022 from 10.3% a year earlier*, S&P Global, 19th January 2023, viewed 20th April 2023, <https://www.spglobal.com/commodityinsights/en/market-insights/latest-news/coal/011923-china-data-2022-power-demand-growth-eases-to-36-in-2022-from-103-a-year-earlier>

71 *European Chamber Energy Working Group Position Paper 2022/2023*, European Union Chamber of Commerce in China, pp. 216–217, 21st September 2022, viewed 20th April 2023, <https://www.europeanchamber.com.cn/en/publications-archive/1043/Energy_Working_Group_Position_Paper_2022_2023>

72 *Carbon Neutrality: The Role of European Business in China's Race to 2060*, European Union Chamber of Commerce in China, pp. 7-13, 25th May 2022, viewed 4th April 2023, <https://www.europeanchamber.com.cn/en/publications-carbon-neutrality-report>

73 Ships built today can be expected to be operational for 25–30 years. They therefore need to be built with the technology and fuels of the future in mind if China is to decarbonise its shipping sector, and to deliver on the International Maritime Organization's target of reducing greenhouse gas emissions from shipping by 50 per cent by 2050: Ibid.

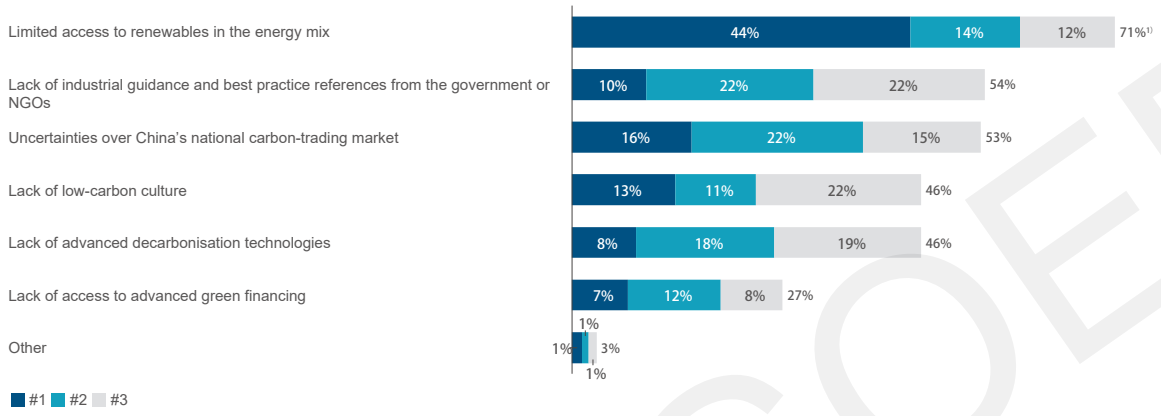
74 Ibid.

ENDORSED

total emissions cap, setting a higher carbon price and addressing emissions-reporting issues.[75]

Figure 58: Companies face a wealth of decarbonisation-related barriers

What are the top three issues/challenges that may prevent your company from achieving its decarbonisation goals in China?



1) *The disparity between the sum of the individual bars displayed for this option (70%) and the 71% total figure cited is due to all figures being rounded to the closest whole integer.*

The key challenges faced by European companies reflect what they require from the Chinese Government to realise their carbon neutrality goals. Transparent and reliable green energy access continues to be the top priority, with 67% (+15pp y-o-y) expecting the Chinese Government to take action in this area. The promotion of a low-carbon culture in China ranks second, with almost half (48%, +38pp y-o-y) expecting more in this regard. This is also the action item that has seen the largest increase in importance, highlighting just how significant a role educating both the public and businesses will play in achieving carbon neutrality.

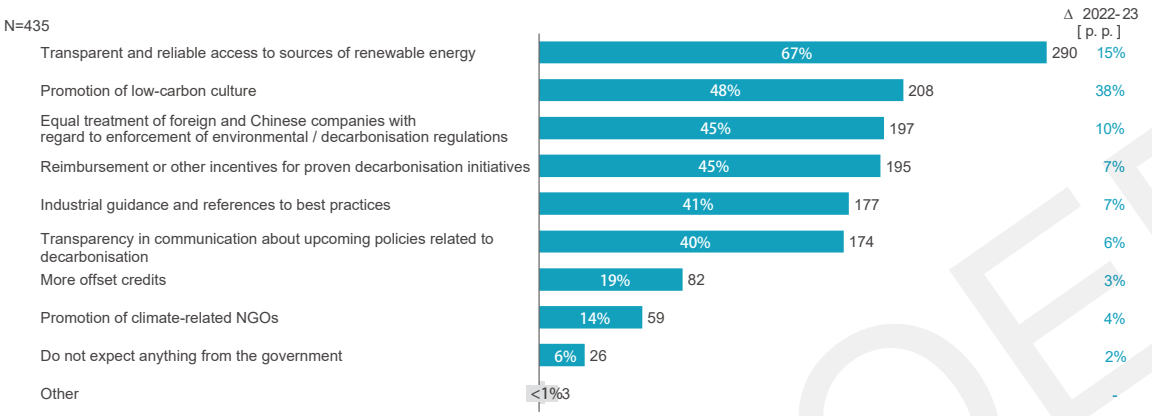
Close to half of respondents also expect further steps to be taken to level the playing field between foreign and Chinese companies with regard to the enforcement of environmental regulation (45%), and for the Chinese Government to provide more reimbursement or other incentives (45%). Two fifths of respondents expect further industrial guidance and references to best practices (41%), and more transparent communication on upcoming decarbonisation-related policies (40%).

EMBARGOED

75 *Carbon Neutrality: The Role of European Business in China's Race to 2060*, European Union Chamber of Commerce in China, 25th May 2022, viewed 4th April 2023, <https://www.europeanchamber.com.cn/en/publications-carbon-neutrality-report>

Figure 59: Urgent need for government action if 30/60 Goals are to be achieved

What does your company expect from the Chinese Government in order for you to realise your decarbonisation and/or carbon neutrality goals in China? [1)]



1) Multiple answers possible

EMBARGOED

7 ABBREVIATIONS

30/60 Goals	China's pledge to peak carbon emissions before 2030 and achieve carbon neutrality by 2060
ASEAN	Association of Southeast Asian Nations
BCS	Business Confidence Survey
BU	Business Unit
CSRD	Corporate Sustainability Reporting Directive
EBIT	Earnings Before Interest and Tax
ETS	Emissions Trading System
EU	European Union
EUR	Euro
F&D	Food and Beverage
FDI	Foreign Direct Investment
FIE	Foreign-invested Enterprise
FIL	Foreign Investment Law
HQ	Headquarter
IP	Intellectual Property
IPO	Initial Public Offering
IPR	Intellectual Property Right
IT	Information Technology
JV	Joint Venture
M&A	Mergers and Acquisitions
MNC	Multinational Corporation
OEM	Original Equipment Manufacturer
pp	Percentage Point
R&D	Research and Development
SME	Small and Medium-sized Enterprise
UFLPA	Uyghur Forced Labor Prevention Act
US	United States
VBP	Volume-based Procurement
y-o-y	year-on-year

EMBARGOED

8 ABOUT THE SURVEY MOTIVATION AND DESIGN

The purpose of the European Chamber's *European Business in China Business Confidence Survey* is to take an annual snapshot of European companies' successes and challenges in China. Published annually since 2004, the survey has enabled the European Chamber to build a rich dataset that serves as a broad indicator of how European companies judge the business environment in China.

The European Chamber invited its members to take part in the 2023 survey over a five-week period during February and March 2023. The survey was conducted in cooperation with Roland Berger and published in June 2023. With 570 respondents completing the survey, the 2023 survey achieved a response rate of 46%.

In order to obtain a high response rate, which is an essential feature for high-quality results, the survey was condensed as much as possible, while keeping the appropriate questions to make comparisons over time. An online and individual password-required survey platform was set up for eligible European Chamber members.

Consistency was one of the key factors that guided the design of the questionnaire and data analysis, so that the development of company strategies and perceptions could be tracked and understood in relation to data gathered in previous years. The survey focussed on capturing the key, ongoing challenges and opportunities for European companies operating in China, and included questions on emerging topics that may have had a significant impact on European companies' China operations in the last three years.

The survey comprised 57 national questions and around a dozen unique questions for each European Chamber chapter. The national questions were grouped under three general and four thematic themes:

- Company Profile and Financial Performance
- Outlook on the Chinese Business Environment
- Outlook on Company Strategy
- Outlook on Supply Chains
- Outlook on the Politicisation of Business
- Outlook on Digital and Data
- Companies' Environmental Strategies

This report highlights the survey results for selected questions of note. For simplicity and consistency, all results are rounded to the nearest whole number. As a result, the percentages contained in some bars and figures displayed in the report sum to 99% or 101%.

EMBARGOED

9 ABOUT ROLAND BERGER

Roland Berger, founded in 1967, is the only leading global consultancy of German heritage and European origin. With 3,000 employees working in 35 countries, they have successful operations in all major international markets. Their 51 offices are located in the key global business hubs. The consultancy is an independent partnership owned exclusively by 320 partners.

Roland Berger supports leading international corporations, non-profit organisations and public institutions in all management issues – ranging from strategic alignment and introducing new business models and processes to organisational structures and IT strategy. They are based on global Competence Centres that are organised along functional and industry lines. This allows them to offer tailormade solutions devised by interdisciplinary teams of experts drawn from different Competence Centres.

The Chinese market is a key pillar of Roland Berger's international expansion. Since their first project in China in 1983, the consultancy has grown rapidly: its five Chinese offices (Shanghai, Beijing, Hong Kong, Taipei and Guangzhou) now have hundreds of consultants dedicated to working extensively with both leading Chinese and international companies.

As the only consulting firm of European origin among the global top five, Roland Berger has built its expertise on its extensive experience working with clients on complex business cases for over 50 years. Outstanding strategic analysis and in-depth knowledge on implementation measures are the strengths of the company's consulting approach. Roland Berger consultants combine their analytical and strategic know-how within a diverse company setting to help clients in Greater China successfully master their unique challenges.

EMBARGOED

10 ABOUT THE EUROPEAN UNION CHAMBER OF COMMERCE IN CHINA

The European Union Chamber of Commerce in China (European Chamber) was founded in 2000 by 51 member companies that shared a goal of establishing a common voice for the various business sectors of the EU and European businesses operating in China. It is a member-driven, non-profit, fee-based organisation with a core structure of 26 working groups, 13 sub-working groups/desks and nine fora representing European business in China.

The European Chamber now has more than 1,700 members in seven chapters operating in nine cities: Beijing, Nanjing, Shanghai, Shenyang, South China (Guangzhou and Shenzhen), Southwest China (Chengdu and Chongqing) and Tianjin. Each chapter is managed at the local level by local boards reporting directly to the Chamber's Executive Committee. A company must purchase an additional membership(s), offered at a discounted rate, or a national membership, if it wishes to be a member of and enjoy Chamber services in more than one chapter. The Advisory Council, which includes the chief executives and presidents of some of the largest European companies with investments in China, influences the priorities and line of action to be taken by the Chamber by providing advice on its strategic direction.

The Chamber is recognised by the European Commission and the Chinese authorities as the official voice of European business in China. It is registered as a foreign chamber of commerce with the Ministry of Civil Affairs.

The European Chamber is part of the growing network of European Business Organisations, which connects European business associations and chambers of commerce from 45 non-EU countries around the world.

Principles:

- We are an independent, non-profit organisation governed by our members.
- We work for the benefit of European business as a whole.
- We operate as a single, networked organisation across Mainland China.
- We maintain close, constructive relations with the Chinese and European authorities, while retaining our independence.
- We seek the broadest possible representation of European business in China within our membership: small, medium and large enterprises from all business sectors and EU Member States throughout China.
- We operate in accordance with Chinese laws and regulations.
- We treat all of our members, business partners and employees with fairness and integrity.

EMBARGOED

European Chamber
中国欧盟商会

Beijing
Tel: +86 (10) 6462 2066
Fax: +86 (10) 6462 2067
Email: euccc@europeanchamber.com.cn

Nanjing
Tel: +86 (25) 8362 7330
Fax: +86 (25) 8362 7331
Email: nanjing@europeanchamber.com.cn

Shanghai
Tel: +86 (21) 6385 2023
Fax: +86 (21) 6385 2381
Email: shanghai@europeanchamber.com.cn

Shenyang
Tel: +86 (24) 3198 4229
Fax: +86 (24) 3198 4229
Email: shenyang@europeanchamber.com.cn

South China - Guangzhou
Tel: +86 (20) 3801 0269
Fax: +86 (20) 3801 0275
Email: southchina@europeanchamber.com.cn

South China - Shenzhen
Tel: +86 (755) 8632 9114
Fax: +86 (755) 8632 9785
Email: southchina@europeanchamber.com.cn

Southwest - Chengdu
Tel: +86 (28) 8527 6517
Fax: +86 (28) 8527 6517
Email: chengdu@europeanchamber.com.cn

Southwest - Chongqing
Tel: +86 (23) 6308 5669
Fax: +86 (23) 6308 5669
Email: chongqing@europeanchamber.com.cn

Tianjin
Tel: +86 (22) 5830 7608
Fax: +86 (22) 5830 7608
Email: tianjin@europeanchamber.com.cn