

The BCG logo is displayed in white, bold, sans-serif font on a dark background. The letters 'B', 'C', and 'G' are interconnected.

Executive  
Perspectives

JANUARY 2021

A detailed bronze dragon sculpture is shown against a red background. The dragon is intricately carved with scales, a long mane, and a fierce expression, appearing to be in a dynamic, coiled pose.

# The China growth opportunity

*Six things to know for business leaders*

A close-up view of traditional Chinese roof tiles, showing their curved shape and the decorative circular finials at the ends. The tiles are dark and appear to be made of ceramic or stone.

# Preface

*focus of this document*



A lot has been said and written about China and its relationships with the rest of the world, especially in light of the COVID-19 pandemic that unfolded in early 2020.

This document provides a fact-based, economic perspective on China. It discusses economic growth opportunities in China and highlights what we identify as key implications for business leaders.

Undoubtedly, the trajectory of the economic development in China has been very dynamic over many years. Despite COVID-19, the past year has been no different, and we expect this dynamism to continue in the years ahead.

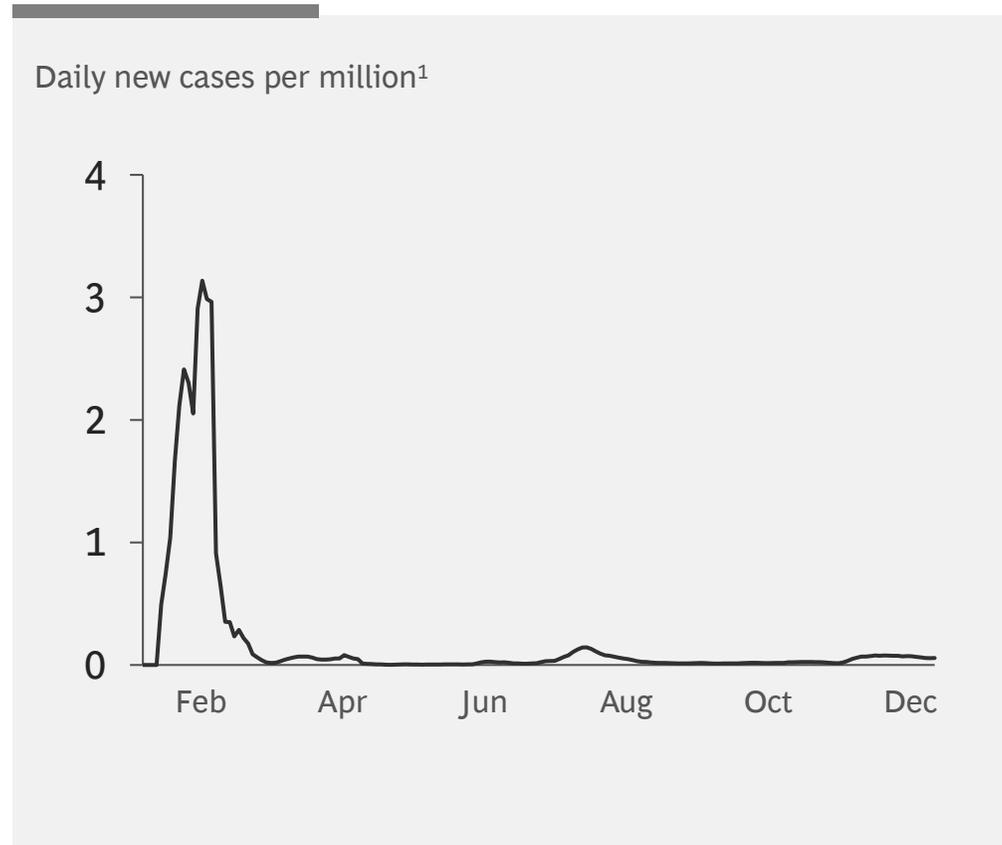
# Six things to know about the China growth opportunity

- 1 Specific COVID-19 steps have supported a quick rebound; the economy is back and will likely contribute **25-30% of the world's GDP growth over 2020-2030**
- 2 Behind the rebound is a structural shift in the economy towards **domestic consumption** – with 78% of the economy to be driven by consumer growth, **services, and innovation**
- 3 China has transformed from a low-cost manufacturing center to a **growing hub of business model and technology innovation**
- 4 **The trade war and decoupling** will have multiple consequences that will need to be managed but will not necessarily slow down growth
- 5 China's **commitment to the Paris Accord and the Net-Zero 2060 goal** will drive massive investment, innovation, and partnership opportunities
- 6 The **14th Five-Year Plan** will solidify focus on specific areas to drive growth

# China has taken a very different approach to COVID-19 and has largely contained the impact since the initial Q1 shock

As of 31 Dec 2020

*Cases in China peaked in February '20 but have been on a decline since with no major resurgence*



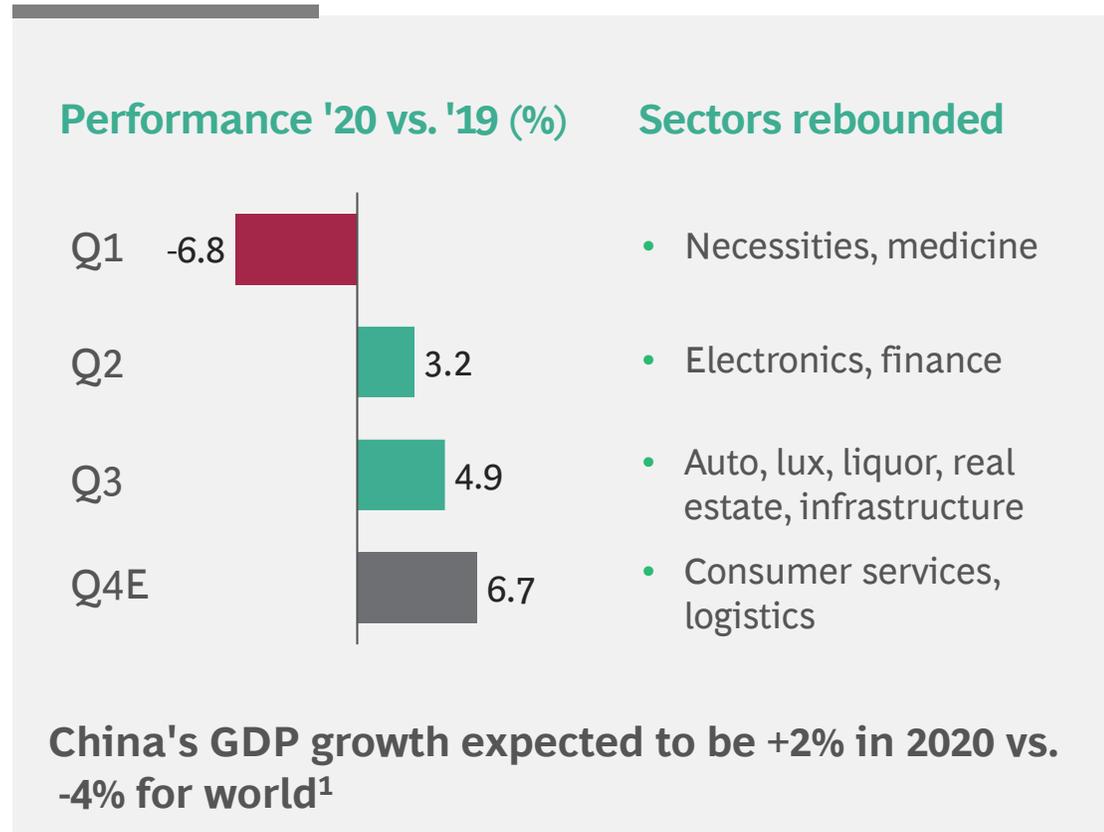
*The government established control measures that restricted the epidemic to a relatively low level of cases*

Dynamic regional & border control	<ul style="list-style-type: none"><li>• High-, medium-, and low-risk regions classified</li><li>• Border control: <b>quarantine</b> and <b>double tests</b><sup>2</sup></li></ul>
Rapid testing infrastructure	<ul style="list-style-type: none"><li>• <b>14K health checkpoints</b> in Wuhan &amp; Hubei</li><li>• <b>Immediate &amp; massive testing</b> in hotspots</li></ul>
Systematic multi-level isolation	<ul style="list-style-type: none"><li>• Special <b>hospitals for COVID-positive</b> people</li><li>• Close contacts: <b>home quarantine</b> for 14 days</li></ul>
Health code & monitoring	<ul style="list-style-type: none"><li>• Management of public areas with <b>QR codes</b></li><li>• <b>Efficient tracking</b> of close contacts</li></ul>
Change in health habits	<ul style="list-style-type: none"><li>• <b>People wearing masks in public</b> – even with 0 cases in many areas</li></ul>

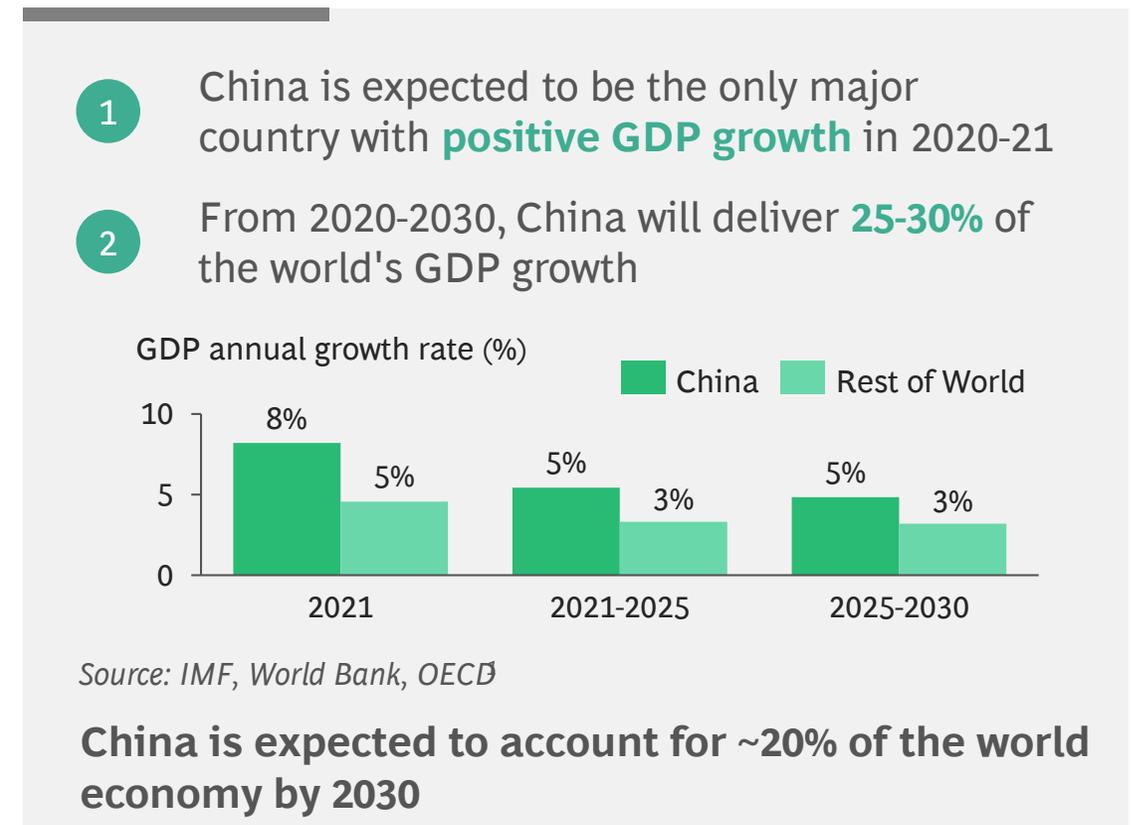
1. 7 day rolling average; 2. 14 days and two consecutive negative nucleic acid tests before being released from quarantine  
Source: Our World in Data; BCG analysis

# China's economy had a quick recovery in 2020 and is expected to be a major contributor to the world's GDP growth in the future

Although GDP took a hit in Q1 '20, sectors rebounded quickly in a phased manner



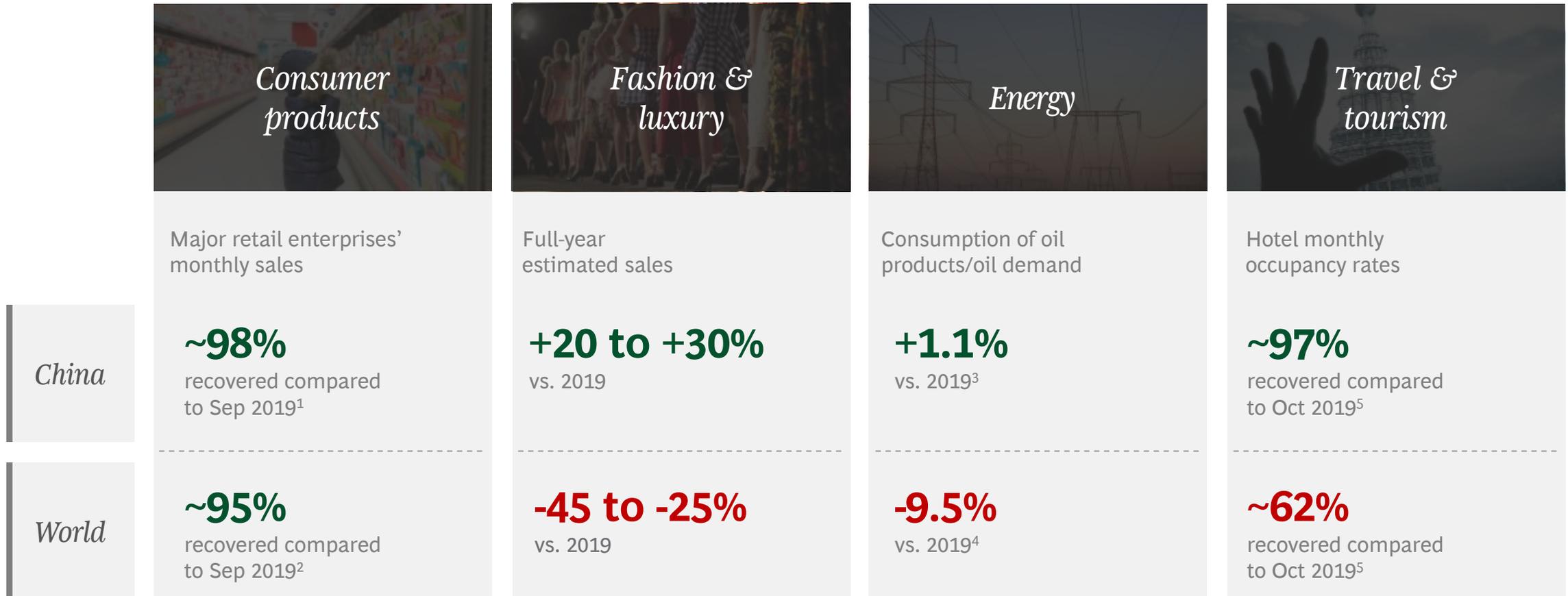
China's GDP is poised to demonstrate robust growth over the next decade



1. China and world GDP growth forecasts are based on base case, a combination forecast with most recent data, global institute reports and BCG analysis  
Source: IMF, World Bank, OECD, BCG analysis

# Industries in China are demonstrating resilience and faster recovery compared to the world

Non-Exhaustive



1. Major retail enterprises referring to 100 brands on the list of PRC Ministry of Commerce, recovery defined as YoY, data as of Sep; 2. Data as of Q2; 3. Consumption of refined oil products, cumulative value; 4. World oil demand; 5. Data for Oct 2020 compared to Oct 2019  
 Source: PRC Ministry of Commerce, Oxford Economics, 2020 BCG x Tencent Digital Luxury Report, OECD, J.P. Morgan PMI index, China National Bureau of Statistics, OPEC, STR Global, UNWTO, BCG

# China is shifting from being the "World's Factory" to a consumption-driven economy

## Before



Huge infrastructure investment by government



"Factory of the world," export orientation



## Future



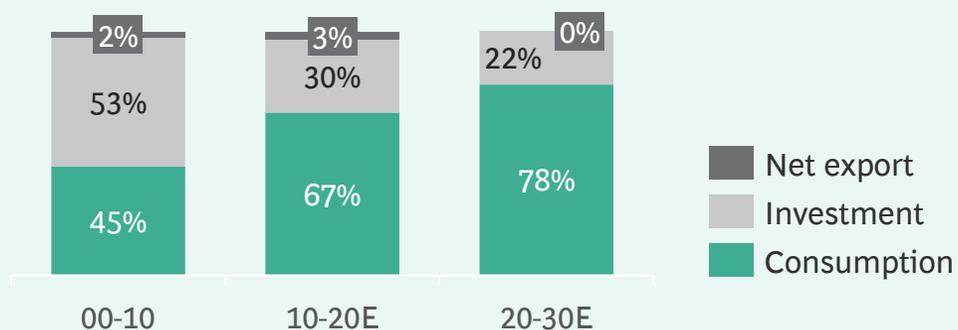
Growing middle class with increasing domestic consumption



Diversified industries with vital commercial services

## Increasing contribution of consumption to GDP growth

China GDP growth structure (%)



[...] As labor and land costs are growing [...], China is transitioning to a [...] services & consumption-driven economy.

- China Briefing: Leading Trends in China's Services Sector after COVID Disruption, 2020

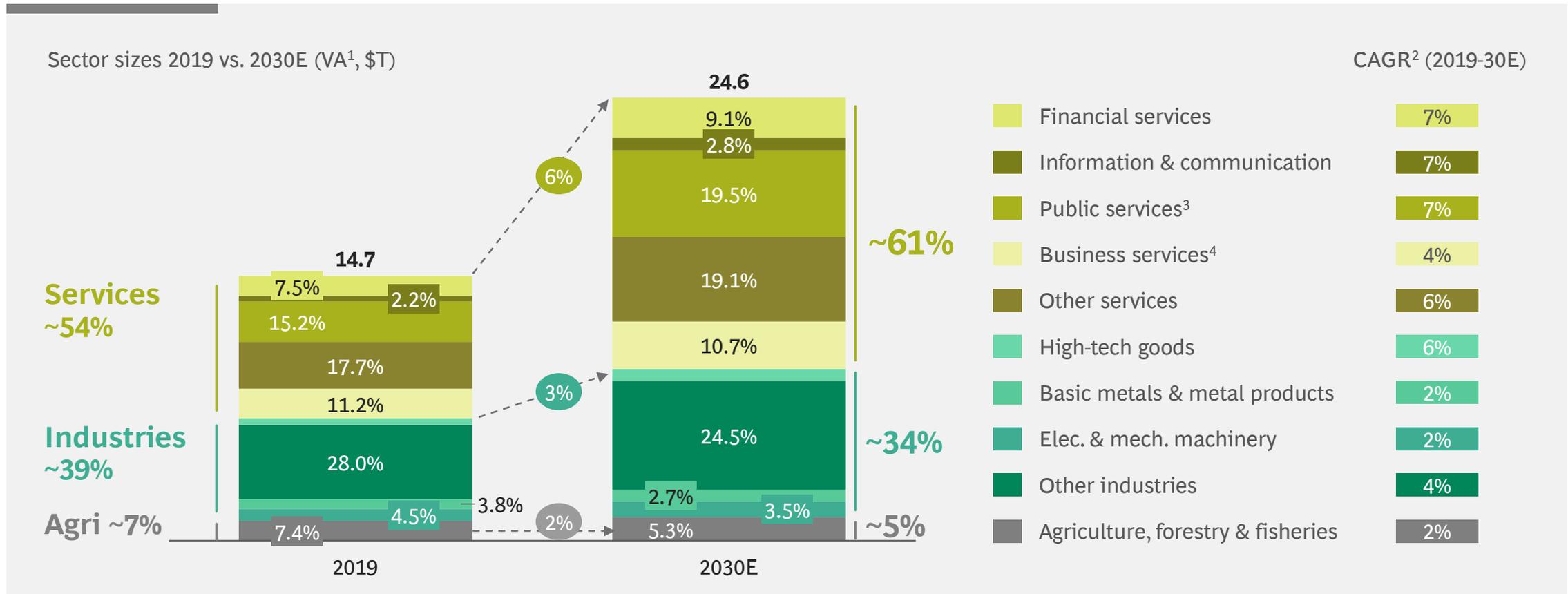


Benefiting from rising household income and technological advances [...], consumption & services have emerged to be the new engines for [...] economic growth.

- S&P Global: China's New Economy Sectors: How Are They Doing?, 2020

# Services sector is expected to play an important role in driving China's growth over the next decade

Services estimated to contribute ~61% of GDP in 2030, up from ~54% in 2019; financial, information & communication, and public services fastest growing



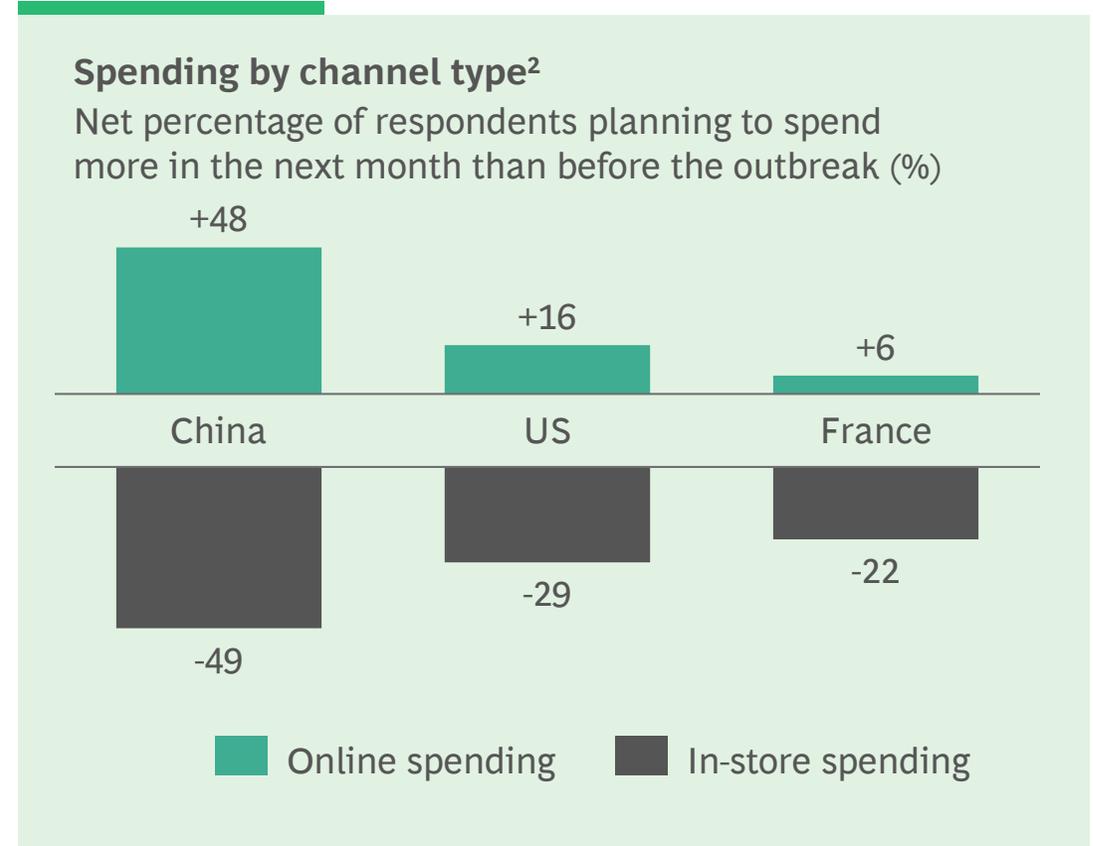
1. Value-added output is a measure of the value of all the goods and services produced in a sector or industry, excluding the value of intermediate consumption. Real value-added is expressed in constant prices (adjusted for inflation and exchange rate movements); VA is in USD billions at 2015 prices; 2. CAGR is based on value-added output; 3. Public services includes public administration, defense & social security, education, health care & social work; 4. Business services includes real estate activities, R&D, leasing, legal, professional & maintenance services  
 Source: Oxford Economics

# Chinese consumers recognize the benefits of technology and are optimistic and ambitious

## Top 10 attitudes among Chinese customers<sup>1</sup>

1	I live a richer life because of technology	90%
2	Important to be respected by others	89%
3	Work-life balance is important	89%
4	Children will have a better life than me	86%
5	Plan finances independently	86%
6	Optimistic about future	86%
7	Connection to cultural heritage	85%
8	Structure my time to meet commitments	84%
9	Career is important	84%
10	Relaxed and easygoing	83%

## High digital & online spending is a strong dynamic in China's rebound



1. Based on the question "How strongly do you agree or disagree with the following statements?" across 56 statements, % of consumers who agree with the statement

2. Question text: "In the next month, what do you expect your spend to be relative to before the coronavirus outbreak?"

Source: BCG CCI Global Consumer Attitudes and Needs research, China (N = 9100), September 2020; BCG COVID-19 Consumer Sentiment Survey, July–August, 2020 (N = 3,100–3,800), unweighted, representative within ±3% of census or national demographics

# Manufacturing supply chain shifts are visible – some sectors are moving out of China whereas others are being reinforced

*Export-oriented manufacturing industries diversifying supply chain*

*Selected examples, non-exhaustive*



**Consumer durables**

Korean white goods maker moved production of refrigerators for US from China back to South Korea



**Apparel**

US apparel maker moving supply chain **out of China**; US imports from China dropped from ~40% to ~22%

*High-end manufacturing industries reinforcing footprint to meet domestic demand*

*Selected examples, non-exhaustive*



**Automotive vehicles**

German auto OEM increased production in China instead of exporting from US to meet demand



**Telco equip. & semiconductors**

Japanese electronics company expanding production in China to meet local demand esp. for 5G infra.

# Three potential trade and geopolitical scenarios that need to be carefully observed to understand implications

	<i>Pessimistic Scenario</i> <b>Decoupling</b>	<i>Base Scenario</i> <b>Perpetuation of status quo</b>	<i>Optimistic Scenario</i> <b>De-escalation of trade war</b>
<b>Situation</b>	<ul style="list-style-type: none"> <li>• <b>Trade war escalates</b>, Chinese companies blacklisted</li> <li>• Escalation in South China Sea &amp; Taiwan</li> <li>• EU ends up leaning on US</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Less aggressive protectionism</b> by US &amp; China for global leadership</li> <li>• <b>Europe &amp; China</b> continue ties</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Trade war de-escalates</b>; globalization rebounds</li> <li>• <b>Competition</b> to become world leader in next-gen technologies continues between US &amp; China</li> </ul>
<b>Trade Flow</b>	<ul style="list-style-type: none"> <li>• Strong <b>decrease of trade flows</b> between blocs</li> <li>• <b>China trade decreases</b></li> </ul>	<ul style="list-style-type: none"> <li>• Trade more resilient than expected</li> <li>• Trade with US and EU decreases, <b>compensated</b> for by trade <b>with ASEAN</b> nations</li> </ul>	<ul style="list-style-type: none"> <li>• Trade flows continue to grow</li> <li>• <b>More diversified trade</b>, more intra-Asia trade &amp; nearshoring</li> </ul>
<b>China GDP Growth</b>	<ul style="list-style-type: none"> <li>• Estimated at <b>1.6% in 2030</b></li> </ul>	<ul style="list-style-type: none"> <li>• Estimated to be <b>3.5-4.5% in 2030</b></li> </ul>	<ul style="list-style-type: none"> <li>• Stabilizes at <b>5.5-6% in 2021-2025</b> &amp; at <b>4.5-5% in 2025-2030</b></li> </ul>
<b>Impact on Sectors</b>	<ul style="list-style-type: none"> <li>• <b>Increased import restrictions</b> on multiple industries</li> <li>• Encouraged local consumption</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Electronics</b> most exposed</li> <li>• Other manufacturing faces moderate risks</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Continued boom in tech.</b>, healthcare, consumer sectors</li> </ul>

# The 14th Five-Year Plan is under development and will shape priorities

As of 05 Jan 2021

## Innovation-driven development



President Xi's New Year Address clearly underlines the direction for Chinese economy to **focus on innovative growth**

## Dual-circulation policy



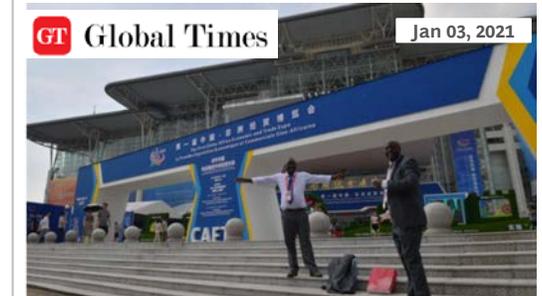
China to promote its dual circulation strategy by boosting consumption, forming strong domestic market

## Opening up to foreign investors



EU and China announced the political approval of an agreement to open the Chinese market further to EU investors

## International cooperation



China launched its 1<sup>st</sup> free trade agreement with an African nation, expanding its network of trade partners

## Green agenda



Chinese President announced at the UN General Assembly that China aimed to go carbon neutral by 2060

## Rural vitalization



Chinese government would undertake “a historic shift” to focus on comprehensively improving the rural economy in 2021.

## Urban development



China promotes high-quality development of cities in 2021, while building livable, green, resilient, smart and cultural cities

## Economic system's quality



Beijing has rolled out more measures aimed at increasing efficiency of China's capital markets & quality of its companies

# Key implications for business leaders in light of the China growth opportunities



**A**

## Increase focus on new drivers for economic growth

- 01 Tailor offerings to evolving demographics (e.g., fresh e-commerce for digital natives)
- 02 Rethink China strategy in line with opening up of sectors to foreign investors
- 03 Ride the consumption boom in China and evaluate potential offerings and opportunities

**B**

## Keep pace with changing consumer behaviors

- 01 Learn best practices on innovative retail formats and digital use (online & offline)
- 02 Double down on growing demand consumption areas (e.g., health and wellness)

**C**

## Use innovation as a growth engine

- 01 Leverage China as a source of tech innovation (e.g., by establishing innovation centers)
- 02 Adapt business model toward increasing tech-driven consumer behaviors

**D**

## Drive a sustainability agenda

- 01 Explore sustainable investment & partnership opportunities emerging out of Net-Zero 2060 goal

# A.02

## Rethink China strategy in line with opening up

Focused agenda to improve business environment

Policy reforms to attract foreign investors

Foreign companies increasingly entering & expanding

Joint ventures commonly used for localized approach



Leaders need to evaluate opening-up opportunities & adjust China strategy

### Improvement in business environment

Ease of doing business ranking:

2018 No. 78 > 2019 No. 47 > 2020 No. 31

8 key business reforms for better business climate

### Systemic interventions to attract foreign investors

Non-exhaustive

**Regulatory:** Foreign Investment Law, 2020, National & FTZ<sup>1</sup> Negative Lists (2020)

**Financial:** Tax cuts and direct financing

**Economic:** 18+ new Free Trade Zones

### Joint ventures utilized for localized approach

- Ease of navigating local formalities, cultural know-how
- Access to partner's existing network



#### Examples | China announces plans for 3 new FTZs in Beijing, Hunan & Anhui (Sep'20)



- ~25% of Beijing FTZ to host a global startup innovation center
- **Advanced manufacturing clusters** to be set up in Hunan & Anhui

#### Examples | International players increasing presence in China



- **US auto player** opened first non-US factory in Shanghai (Sep'20)
- Leading financial institution held "**cloud opening**" in Shanghai (Mar'20)

1. Free Trade Zone; lists imply fewer restrictions  
Source: Doing business report 2020, World bank; BCG analysis

# B.01

## Learn best practices on innovative retail formats & digital use

Accelerated adoption of digital sales channel

Strong penetration of digital in offline retail

Innovative formats arising for e-commerce sales



Leaders need to experiment with innovative formats to succeed in China and be at the digital forefront

*Strengthening the customer experience through a variety of innovative digital and offline channels and formats*

<b>Livestreaming shows</b>	KOLs/KOCs <sup>1</sup> recommend, consumers place orders live	<b>Short video</b>	Consumers watch KOL/KOC <sup>1</sup> videos, click link & place orders
<b>Online to offline</b>	Consumers place orders online & product is delivered to door	<b>Unmanned retail</b>	Consumers purchase in vending machines
<b>Community e-commerce</b>	Community leaders initiate group purchase, consumers join	<b>Social customer to cust.</b>	Direct peer selling through social e-commerce platforms



### Example | China's shopping center group places AI robots



- Shopping group replaced info center staff with **AI robots**
- Wide range of services through robots (e.g., **store navigation**)

### Example | Chinese electronics company demonstrated products in a livestream show



- **2-hour livestream show** with founder (Aug'20)
- **50M viewers & \$30M sales** in smartphones & TV

1. KOL - Key Opinion Leader, KOC - Key Opinion Consumer  
Source: BCG analysis

# B.02

## Double down on growing demand consumption areas

Increasing consumer preference for health & wellness categories

Companies launching products into these categories based on shifting consumer demand



Leaders need to refresh their product portfolio in line with changing consumer demand

*Chinese consumers, especially younger shoppers, focus more on health*

**70%**

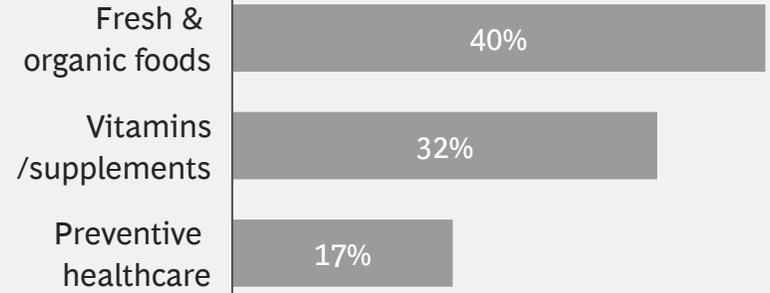
of Chinese internet users consumed more health products during the pandemic<sup>1</sup>

**76%**

of affluent millennial Chinese consumers focus more on wellness than their parents do<sup>2</sup>

*Health-based categories saw an uptick during COVID-19*

% of consumers who claimed they purchased more expensive brands or products due to the virus<sup>3</sup>

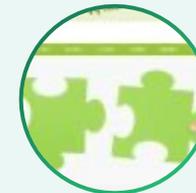


### Example | Leading F&B multinational launched healthy superfood drinks in China



- Uses technology to enable personalization of **healthy superfood drinks**
- Made with **100% natural ingredients** & recyclable packaging

### Example | Chinese dairy giant launched new products to meet evolving consumer needs



- Launched **enhanced-nutrition** & sugar-free milk variants due to rise in consumer focus on health
- Developed **own big data platform** to use consumer purchase data to support R&D

1. As per April 2020 report by iiMedia Research; 2. As per 2019 survey by Singapore-based market research firm Agility Research & Strategy; 3. Question text: "How do you expect your spend to change in the next 6 months across the following areas?", exclude categories with N <~100; 15 BCG COVID-19 Consumer Sentiment Survey, May 22-25 (N=2,963 respectively, unweighted, representative within ±3% of CN census)

# C.01

## Leverage China as a source of tech innovation

China evolving from low-cost manufacturing hub into a source of technology innovation

Attracting tech capital, and foreign companies establishing innovation centers

Focus on building new use cases of latest technologies



Leaders should consider leveraging innovations in China (R&D, tech hub)

### Attracting tech capital

High-tech investment<sup>1</sup> (incl. seed/VC/PE), 2017-2020H1

Guangdong-Hong Kong-Macao Greater Bay Area

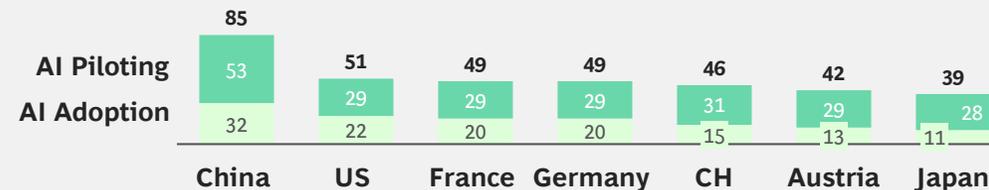
\$313B

US Bay area

\$231B

### China is leading in AI progress

Share of active players in AI<sup>2</sup>



### Examples / International players fostering innovation from China

#### German industrial manufacturing player set up innovation hub, including:

- **Digital innovation:** Implement & upgrade digital transf. for Chinese partner companies
- **Intelligent manufacturing:** Generate smart solutions through converging IT & manuf.
- **Internet of Things (IoT):** Collaborate with Chinese tech giant to build IoT infrastructure

#### US industrial conglomerate opened innovation center, including:

- **Joint product build:** Cooperate with Chinese company to build cheaper aircraft type
- **Smart logistics:** Provide smart solutions to increase productivity
- **Talent access:** Leverage additional high-skilled talent in China

1. Including AI, big data, AR, autonomous cars, life sciences, etc, 31 high tag vertical categories tags; 2. BCG Report "Mind the (AI) Gap". BCG surveyed more than 2,700 managers in September and October 2018, from a broad and representative spectrum of industries including consumer, energy, financial services, health care, industrial, technology, media and telecom, as well as professional services and the public sector. Source: Pitchbook, press search, BCG analysis

# D.01

## Explore sustainable investment & partnership opportunities

China emphasizing sustainability

Net-Zero 2060 goal & Paris Accord commitment

Opportunities arising across sustainability areas



Leaders should leverage green investment options in China and learn best practices

### Selected sustainability opportunities



**NEV<sup>1</sup>:** Push R&D, product strengths & penetration



**Renewable energy:** Scale up alternative power generation



**Process optimization:** Increase efficiency of energy utilization

### International agreements, EU examples

NEV cooperation: Chinese & German companies co-build 100k charging stations

EU-China Energy Cooperation Platform (ECECP)

Chinese-European-Emission-Reducing Solutions (CHEERS)



#### Example | German car manufacturer

JV on R&D and production of **hybrid vehicles** in China

JV's **fully electric small car** to be **introduced** in 2022

#### Example | UK platform for energy & technology

JV between **UK & Chinese research centers** for offshore energy

Agreement to apply **UK technologies** in Chinese market

#### Example | Australian resources company

Knowledge sharing with Chinese steel producer to **reduce emissions**

Australian player to invest **\$35M**

1. NEV = New Energy Vehicles, Source: Press search, BCG analysis



*“ China’s fast recovery continues thanks to resolute measures in combatting the virus, mitigating its impact, and supporting growth... China will secure the recovery and ensure balanced and high-quality growth, which will benefit China and the world.”*

**—Kristalina Georgieva, MD of the International Monetary Fund**

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