Interview with Dirk Moens, , European Union Chamber of Commerce in China

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cently released this year's European Business in China Business Confidence Survey – what were some of its key takeaways?

There are four main points to the Survey. The first has to do with not only China but the rest of the world. China's growth has been stronger than the rest of the world's, and therefore companies are quite happy to have been part of the economy so far. They've been growing not only the top line, but seeing the bottom line going in the right direction. There was a hiccup with the economic crisis three years ago, and it is still a bit slow now, but overall they're quite happy to be here. The proportion of China in global revenues has been increasing, and that's another reason why managers here are under pressure, and that they feel the pressure from their headquarters on the importance of China for their global results. Overall, as of February 2012 when the Survey was conducted, they still believed in broadly positive growth aspects. I believe that if we asked the question now, they would be less outspoken, and more confidence in the long term. The simple reality is that China has an enormous need to continue to grow, in all industries and provinces, and there is little doubt that growth will continue. Our members will continue to defend themselves and compete despite the growing competitiveness of the market. It's maturing – and you can see signs of increased competition among both domestic and international players – but if anyone complains, as a Chamber we must say, "too bad!" If you cannot compete, you shouldn't be here. Competition means competing on a level playing field. That's the game, and we're in favor of it. Competition drives all the familiar buzzwords : consumer value, innovation, efficiency, and productivity. We stand for it in China as we stand for it in Europe. We fully support Chinese investment in Europe,

and it puts additional pressure on our companies – and that's a good thing. Our companies back home need to cope with it and make sure they can find a way to compete.

In any case, it's a fact that our companies tell us it's getting tougher to compete. The gap between the traditionally strong points for our companies and local companies – such as brand-building, sales techniques, and go-to-market strategy – is getting smaller and smaller every day, if it still exists. Although government relations is an area local companies still have an advantage in, they're closing the gap on the rest, and our companies feel the heat. There is also pressure on resources, and human resources above all else, not only cost, but availability, and finding the right people. It's a cliché as big as a house, but HR is back again to the number one priority for many companies. Overall, the second message can be summed up in the following : competition's up and therefore it's getting tougher.

The third is that the regulatory environment is not improving, and has not improved over the past two years. Many people, some 30% of our respondents, even said it's getting worse. However, what's more worrisome is that there is little hope of dramatic improvement in the coming two years. That's also a very clear message. Our companies would love to see more change and more reaction to what they have been saying for a long time. China's government must work on the rule of law and not only IP but property rights protection in general, and be more inclusive toward foreign invested companies, to involve them in dialogue. The question seems obvious : if you want to develop standards in a given industry, why not talk to all players in a market, rather than doing it in a corner with the Chinese companies and then coming up with huge potential surprises for the rest of the companies ? The latter approach results in gaps on how to react and be competitive.

Another aspect is how to get licenses and registration, and the whole administrative side of business. There is a perceived gap in how foreign companies are treated versus domestic companies. They need to submit enormous amounts of data and information, and they're not quite sure who is looking at it – or sometimes their competitors are sitting around the table with it, and this is hardly reassuring from an IP security standpoint. All that makes companies tell us that things are not getting better. If anything, it's getting tougher on the regulatory side. The metaphor I often use is soccer. If you take a very strong team and match them against a weak team, the referee is not that important. He can make mistakes and award penalties, but the stronger team is strong enough to win anyway. But when the teams are more evenly matched, the referee makes a big difference – especially when the referee is the same nationality as one of the teams! Even if the regulatory framework did not change dramatically and did not get worse, the relative weight and impact it has on competition increases, and regulatory inequalities begin to weigh upon business plans and performance.

The fourth message is that we've started to quantify all these effects on business. It's the first time we've asked what the impacts have been on our members' businesses. A considerable amount of companies have told us that it affects their top line, that they miss out on business. In fact, one out of two said it. Of that 50%, two-thirds say they lose out on more than 10%, and a small fraction say they're missing out of up to half of the potential turnover they could expect without current barriers, if there were an equal playing field.

In recent months, China has said they will stop giving preferential treatment to foreign-invested companies. But it's important to note that we don't ask for preferential treatment. It's fair to say that if you want to attract FDI as a country, you must compete with other regions in the world, and you have to offer something, otherwise companies go elsewhere. That's one thing. Once companies are in, over the bump of investment and in cruise mode, they should be able to compete and they don't need any preferential treatment to do so.

Furthermore, we asked a now-famous question that made ripples in some countries and waves in others: Are you considering shifting new investment from China to other regions? And 22% of respondents said yes. That's it. We don't have a reference point, and it's the first time we've asked that question. In our traditional Business Confidence Survey, we don't have a reference. But we see that it's quite consistent with other surveys. I've had insight to other surveys and it was approximately the same level, 20-22%. I looked at the different nationalities, because some countries said, "that may be true in general, but not for us." However, even looking at those countries, the figures are the same. Across the board, it's fair to say companies are looking at their options, which I believe is healthy. The important question to ask about this particular result is whether or not 22% is a high figure, and I think it is. It's one out of five, in a country where there is enormous growth and market opportunity. When you ask the same question in Belgium, for instance, it's one out of 10.

Could this be a case of fair-weather friends – some come when there's opportunity, and leave when things begin to get tough?

That's true to a point, because of companies that have only entered recently, there's a slightly higher proportion answering in the affirmative to that question. But still, the percent among big companies which have been here for a while is still 17-18%. I talk to CEOs and senior management, and I know for a fact that even big companies are considering alternatives.

In your second point around competitiveness, you mention closing the competitive gaps, and that even companies which have been established for a long time, in cruise mode, are feeling the heat from domestic players. Is this because Chinese companies are mastering foreign methods of approaching the market, or are they doing qualitatively different things?

I think it’s both. They pick and choose and learn what is in their interest to learn, and develop their own way of doing business where it best suits them. It’s not just copying and pasting. It’s different from Western style models.

You’ve been here a decade. How would you assess the ability of people coming from abroad, the EU or elsewhere, to adapting to the mindset of guanxi and Chinese business culture?

Everybody pays their learning dues, and there are phases. If you look at the China market at entrants who wanted to move fast, 10-15 years ago it was important to look for a partner to hit the ground running and take advantage of the strength of your partner, to bring new ideas, technology, management techniques, and – at that time – money, though that’s not needed anymore. In exchange, you hoped your local partner would bring contacts and distribution, especially in consumer goods. This approach, however, has led to conflict and tension between partners, because invariably partners have different expectations, and China was not an exception. Over time, JV partners have learned that you need to spend time and align interests. They may have also tried to buy out partners or go at it alone, although today we’re in a phase where companies may be going back to the older model. Now our members know what we can do, we know the walls we have hit, and we know there are constraints. As a result, we really look at partners who can, for instance, penetrate public procurement, which is very difficult without a partner.

How would you gauge the relative importance of bilateral relations at a country level versus EU level?

It’s very difficult to quantify, but there’s a growing belief in Europe that it’s better to talk as Europe than as individual countries. Of course, there’s no unanimous position on that. Individual countries are in different phases as far as their economies are concerned. They can offer different things to China, and therefore naturally act and talk differently to China. They also know that no matter how strong they are today, they are probably not strong enough to be an equal partner to China in the future. While they might pursue their short-term interests today, they know they need the strength of Europe to stand on equal footing with China.

What is the importance of the pharmaceutical sector to the European Chamber?

Healthcare in general is quite a regulated environment, and where the Chamber is active is exactly there. On the interface between industries and the government, and where there’s a high level of regulation, we have a much more active role. In basic consumer goods with free competition, the chamber cannot add as much value. The Chamber is important in China in the pharmaceutical industry not only because of the high levels of regulation, but because the industry remains very close to the government. There’s still a huge hand of the government in that industry. Therefore, if there’s criticism to give, and constructive recommendations, our members prefer to do so via an

industry body, and use institutions such as the Chamber rather than stand in front of the regulators and make noise.

Looking at the 12th FYP, we were excited to see the government identify biotechnology as one of the seven "Strategic Emerging Industries." How important is the FYP vis-à-vis locals or MNCs?

If you were excited, we were even more excited! When we read it, we said this is exactly complementary to what Europe can offer: green, technology, healthcare, social security and systems, and the service industry, and our companies had very high expectations. But there was a reality check when we saw, after the publication of the Five-Year Plan, the investment catalogue. Because we would have expected the investment catalogue, which defines how welcome or unwelcome foreign investment is, to be a follow-up to the Five-Year Plan. But that was not the case. In some industries there was a minor opening, and in others this was not the case at all, which came as a disappointment. If you say you want to develop the service industry, and the first topic that always pops up is financial services, for instance, you would expect more welcoming opening of FDI in that industry. After a year or 18 months, the companies confirm that disappointment. They would have expected to be much more involved and seizing opportunities because of that opening up and the strategic importance of those industries. In reality, and for many reasons – and the crisis and stimulus program is one of them – many of the incentives to develop those industries are going to domestic industry. This may not be surprising. I also think it's a missed opportunity for China, because European companies can offer a lot to accelerate development of local industry. There doesn't seem enough readiness or willingness to open that door more widely and bring in more foreign expertise.

Are there any case studies or highlights you'd like to share about European companies doing that kind of helping and development?

The classic example is in new energy, where Europeans and others have developed an industry, including bringing in and developing the supply chain, only to later be put under pressure because market access was limited and de facto given to local players, who subsequently took advantage of the newly-developed supply chains to build their businesses and take the lead. The industry switched from 80% foreign investment companies market share and 20% domestic to exactly the other way around in just a few years. That caused quite a chill, not only in that industry, but in other industries, because the companies realized that if that's the model – to import technology and build up a whole infrastructure, to transfer knowledge and technology and train human resources – only to be shut out of the market, then it suddenly becomes less attractive to try that again.

Of the three big issues you have identified in the pharmaceutical sector – pricing, market access, and IP protection – which is the most important?

I’m not an industry specialist, but I believe there are critical angles on each of the three. I am particularly sensitive to pricing, because it’s very similar to other phenomena we see in public procurement. If you only look at prices you miss out on a big chunk of the picture, because one medicine can be more expensive though much more effective, and the total cost of the treatment can be much lower. That’s the same for machinery or for any other equipment supplied through public procurement. If you only look at pricing, foreign-invested companies are not as competitive. But qualitatively, the same way that in equipment the lifecycle cost is much more important, so too is total treatment cost. The tendency to look only at pricing is very shortsighted and de facto excludes a lot of foreign-invested companies. Meanwhile, one never knows what happens in the background on pricing and what kinds of compensations are given. Therefore I believe pricing is critical because it can squeeze you out of the market. However, to be squeezed out of the market, you must have access in the first place! And when it’s difficult to get access, clinical trials, and registrations, these can be just as big issues.

What’s your final message to our readers about the pharmaceutical industry here in China?

It’s the same as with other industries : China is a very promising market, because there is much need and still so much to do. There is a clear willingness, plan, and policy to work on healthcare from the government, and obviously the pharmaceutical industry has very important role to play. However, it won’t be a slam dunk. The government has ideas to democratize and lower cost, and there’s a lot of education to explain and work together with the relevant government bodies to determine where it is best to drive costs out of the system to bring healthcare within reach of the entire population. I believe that the solution is not to go after producers to reduce prices. It’s too easy – it’s shortsighted, and it’s a shortcut. But the pharmaceutical industry has an important role to play to talk with those relevant bodies, to examine the whole cycle, and to work concertedly to come up with best practices to prove there are better ways and to convince the government to focus on the cost of their total system. It’s a great opportunity, and it won’t be easy, but it can be done.

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