When discussing China as a business prospect, the words "threat" and "opportunity" are often thrown into the discussion. Common misperceptions about China fuel fur-

Opportunities in an Expl

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Bio

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Bio

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We feel that one of these widespread misconceptions is that a slowing growth makes China a less attractive opportunity than previously. It is thus worthwhile to take a look at the Chinese market and its potential for the coming decade[1].

While in percentage China's GDP growth went down from an average of 10.4% a year from 2000 to 2010, the average growth rate of 7.9% for the 2010-2020 decade[2] still means that China will add USD 6 trillion to its GDP this decade. That is 50% more than the USD 4 trillion in GDP added during the previous decade!

«With rapid urbanization the middle class is literally exploding»

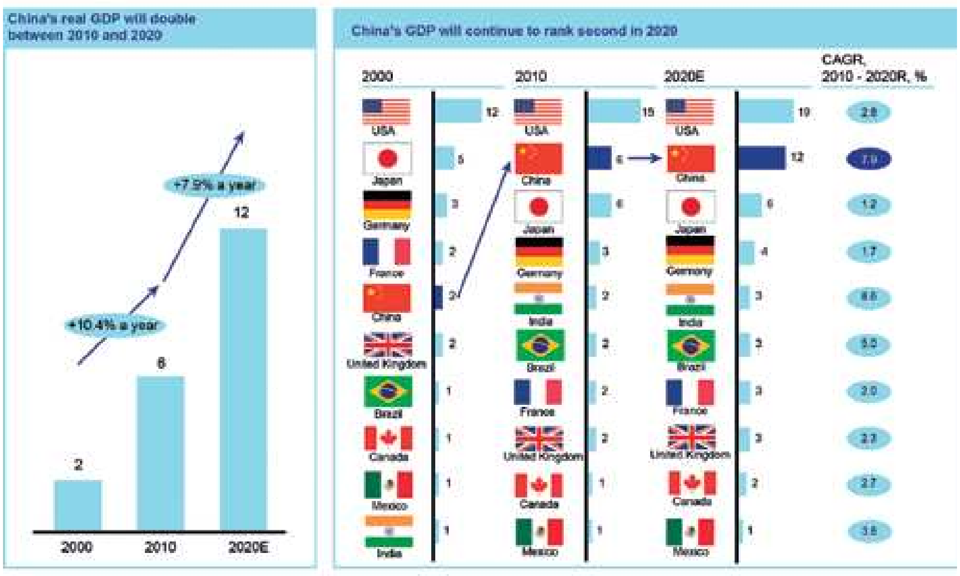
China's growth is only slowing down in percentage. In amount of dollars, China is in fact adding more GDP to its economy every year than it ever did in the past. This is simply due to the size that the economy has reached in the past year, making a slower percentage growth still a bigger amount in absolute numbers. For business, absolute numbers, not the percentage, are those that really count. Mongolia, for example, may grow 15% in 2012, but with a USD 6 Bio. GDP, the business opportunities remain limited. This level of growth means that, by 2020, the Chinese GDP will account for 19% of the world's economic output, compared with 9% in 2010, potentially closing the gap with the United States.

However, GDP *per capita* will remain low for some time to come, with wealth concentrated in the major cities. Indeed China's average GDP *per capita* in 2020 will come to USD 9'000 whereas the US average will be USD 57'000, leaving China still far behind and highlighting the enormous potential for growth also past 2020[3].

At a turning point: from export low cost labor intensive towards a consumer driven domestic economy

The difference between now and in 2020 is that consumption, in addition to investment, will be one more driving engine of China's GDP, aggressively pushed by the latest five-year plan. Indeed, with rapid urbanization the middle class is literally exploding. While in 2010 only 6% of urban households (about 13.5 Mio.) are "mainstream" in the McKinsey categories (see

China's continuing GPD growth – $ trillions, 2010 real term



Note: Exclude the impact of foreign exchange rate

Source: McKinsey Insights China - Macroeconomic model update (March 2011); Global Insight thermore this debate, and add an element of uncertainty for decision makers.

oding Consumer Market

chart below), this proportion will not only grow to more than 50% of all households in 2020, but at the same time the number of urban household will increase to 165 Mio mainstream households!

All in all, the Chinese middle class will be multiplied by 12 from 2010 to 2020 and the long awaited Chinese consumer market will finally be a reality.

Those who will benefit are those already in the market, ready to receive the business. In terms of sectors, consumer goods are of course the obvious one, though probably also the toughest one with growing competition of local and international producers. New opportunities, however, will arise: maturing consumers will want to differentiate themselves and should welcome more different and special products. This will provide new opportunities for smaller, more specialized, niche companies.

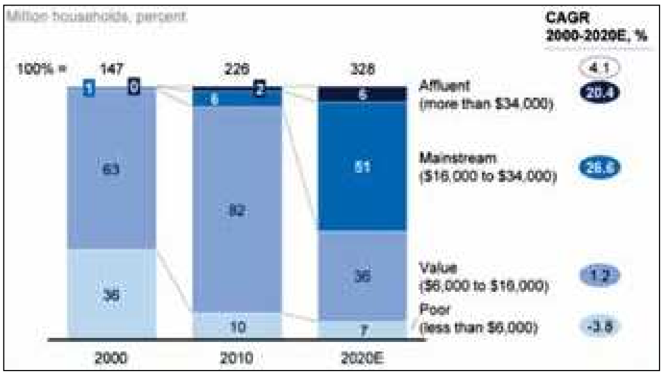
Naturally, the increase in domestic consumption, will allow enabling and production industries such as machinery, manufacturing and IT, to ride the wave, also compensating for the relative decrease in exports. In general, with the increase in wages and demand for more sophisticated and quality products, technology and automation will be big winners of this development.

Not to be forgotten, the service industry will gain enormously from this new pool of middle class consumers, creating strong demand for healthcare, education, recreation and financial services, just to name a few.

This ongoing literal explosion of mainstream consumers will change China fundamentally, one more time, bringing our economies a new set of opportunities. For international businesses, China at this turning point might just be the business opportunity of the decade!

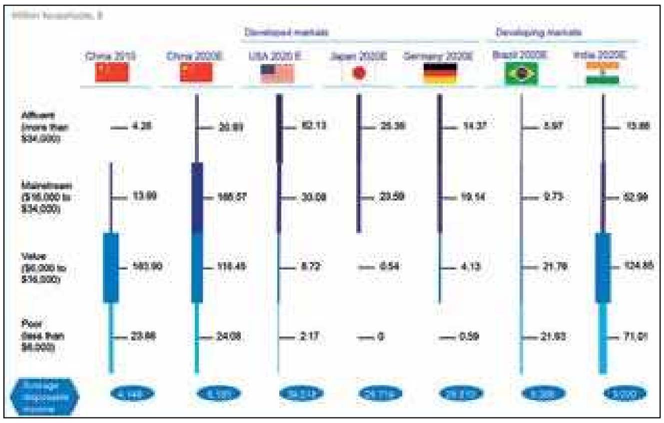
We hope that the above can be of support for your China strategy and plans. For more information about this topic, do not hesitate to contact n.musy@ch-ina.com.

Number of urban households by annual household income



SOURCE: McKinsey Insights China – Macroeconomic model update (March 2011)

Numbers of Chinese households by income level compared with other countries



SOURCE: McKinsey Insights China - Macroeconomic model update (March 2011); Canback Dangel for United States, Japan, German and Brazil data

Appendix

China: Projected growth pattern assuming steady reforms and no major shock

Indicator	1995-2010	2011-2015	2016-20	2021-25	2026-30
GDP growth (percent per year)	9.9	8.6	7.0	5.9	5.0
Labor growth	0.9	0.3	-0.2	-0.2	-0.4
Labor productivity growth	8.9	8.3	7.1	6.2	5.5
Structure of economy (end of period, %)					
Investment/GDP ratio	40.4	42	38	36	34
Consumption/GDP ratio	48.6	56	60	63	66
Industry/GDP ratio	46.9	43.8	41.0	38.0	34.8
Services/GDP ratio	43.0	47.6	51.6	56.1	61.1
Share of employment in agriculture	38.1	30.0	23.7	18.2	12.5
Share of employment in services	34.1	42.0	47.6	52.9	59.0

Source: DRC

[1] *Like all predictions, external shocks might confound any forecast, but our understanding and analysis, based on McKinsey projections, serves as a useful lens through which to assess opportunities of the Chinese market for the coming decade.*

[2] Meet the *2020* Chinese Consumer, *March 2012 by McKinsey* and China 2030*:* Building a Modern, Harmonious, and Creative High-Income Society, *February 2012 by the World Bank and the Development Research Center of the State Council (DRC). See table in Appendix for details and projections up to 2030.*

[3] *Actually, under the assumptions of the World Bank and the DRC (5.9% in 2021-2025 and 5.0% 2026-2030), computing the growth of China shows further increases in absolute GDP (USD 8 trillion added from 2020 to 2030).*