



Article by

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China Inroads supports innovative companies in their expansion to the Chinese market. "China belongs to the Chinese." This philosophy is the guidance for how we match companies with the right parties and markets in China, to create a successful and effective venture.



## → CHINA'S TRANSFORMATION INTO AN INNOVATION ORIENTED SOCIETY

How innovative is the Chinese economy? Not long ago the main concern of Western companies entering China was how to protect the intellectual property of their products. Today, China is innovating, becoming a global innovation leader already. In 2014, \$200 billion was spent on R&D (2 percent of the GDP) and each year over one million engineers graduate from Chinese universities. China is innovating in all possible ways and Westerners are working hard to keep up.

### Our Questions

How does China innovate and what does it mean for you, an entrepreneur entering the Chinese market? How can you benefit from these developments?

### Our Story In A Nutshell

China is transforming into a world leader in science and technology, aiming to produce its own innovative technological inventions, rather than relying on imported technologies. At present, still many Western companies have to offer advanced technological knowhow when entering the Chinese market. Competition from Chinese firms however is becoming fierce and it won't be long before they find their ways into Europe.

### Let's Look Back Into The 'Old' China...

From fake Apple stores to inexpensive Nike shoes and Gucci bags held together by glue, China had the reputation of counterfeiting any successful company or product. We can judge, but rather ask the question how this trend was developed.

Firstly, China's education system has contributed a great deal. For centuries Chinese students have copied their masters and were tested on the knowledge of their master's script, not leaving any room for creativity and new ideas. Chinese students were used to listen to their teachers and do not receive many opportunities to practice their opinions. This educational culture is still in place today, although a 10-year reform plan launched in 2010 by the Ministry of Education aims to liberalize the system. State controls over education are loosened and experimental middle schools or colleges with connections to foreign universities are allowed. The number of overseas students grew rapidly from 364.800 in 2013 to 459.800 in 2014, giving students the opportunity to get familiar with other teaching methods.

Additionally, China is still a developing country and its economy only started to speed up since the eighties. The current legal system was not in place yet and did not fully protect intellectual property rights (IPR), allowing counterfeited products into the market. Luckily there have been improvements in the system since China joined the World Trade organization (WTO) in 2001. It strengthened China's legal framework and amended its IPR laws and regulations with the WTO agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Since then China is continuously improving the protection of IPR in China.

### Innovation Is the Key Factor For Sustainable Economic Development

At present China has grown to be the second largest economy after the U.S. and its GDP growth is about 7 percent a year. Over the past three decades, China lifted over 500 million people out of poverty. China's Millennium Development Goals have been



reached or are within reach and now new objectives have been set, of which we listed the most important ones. China's 13th Five Year Plan (FYP 2016-2020) will be published next year. Premier Li Keqiang said that China will continue to invest in innovation and reform, seeking greater progress in the promotion of scientific development and transforming development patterns.

Also Zhang Guobao, former head of the National Reform and Development Commission (NRDC) and current Director of the National Energy Administration, made some predictions on the 13th FYP, China Business Review reported. Zhang says that the key challenge is to continue economic growth at a relatively fast pace while also maintaining a healthy development. Furthermore, Zhang expresses that even though government debt is piling, China should continue to invest in healthcare, elderly care, education and other emerging industries. Finally, Zhang states other areas of focus should be stimulating domestic demand, upgrading industrial infrastructure and reforming the country's energy pricing structure.

## **“China should continue to invest in healthcare, elderly care, education and other emerging industries.”**

Moreover, ambitious reforms aim to double 2010's annual incomes by 2020, and experts said this should be attainable if China keeps growing between 6.5 and 7 percent. These investments give Chinese firms the opportunity to implement innovative plans developing these emerging industries even further.

Besides the speculated 13th FYP there is the 15-year 'Medium- to Long-Term Plan for the Development of Science and Technology' (2006 MLP). Launched in 2006, this plan aims to have transformed China into an 'innovation oriented society' by 2020 and a world leader in science and technology in 2050. The 2006 MLP aims to reduce China's reliance on imported technology to more than 30% within a few years, increase domestic R&D funding and encourage strategic emerging sectors, such as equipment manufacturing, energy-efficient technologies, biotechnology, advanced materials and information technology.

### **Which Tangible Results Can We Detect In the Market?**

The government plans and policies do have positive effects on the development of the Chinese economy. Below we listed tangible developments analyzed by McKinsey:

- Multinationals are encouraged through subsidies and other incentives to set up R&D centers in China where Chinese graduates can learn to innovate.
- China limits its internet restrictions, the government has allowed for internet champions to arise.
- China's talent pool to work in R&D has been deepened with the higher education expanding from 1 million to 7 million graduates over the past 15 years.
- A RMB 40 billion venture capital fund was launched to support startups in emerging industries.

Great focus lies in developing the countryside. China aims to increase its number of large cities, therefore entrepreneurship is encouraged for migrant workers, college graduates and army veterans who are returning to their home villages.

## “China’s R&D talent pool deepened with higher education expanding from 1 to 7 million graduates over the past 15 years.”

### How Does China Define Innovation?

Since October 2005, the Chinese government made ‘indigenous innovation’ a national strategy that emphasized science and technology development. China’s 12th Five Year Plan (2011-2015 FYP) was set with clear objectives to promote this kind of innovation. The next phase has just started with the ‘Made in China 2025’ plan, where China continues to focus on indigenous innovation, which plays an important role in the future Chinese economic reforms and influences medium term economic initiatives greatly.

Indigenous innovation consists of three different types of innovation:

- Innovation that is original, genuinely new and independent;
- Integrated and combining existing technologies in a new way;
- Assimilated, making improvements to imported technologies.

Products that are considered indigenous innovations in China are mainly developed by domestic companies. The IPR are owned domestically and there is a leap in technology compared to existing products. The development of modern China is focused on Chinese companies to independently develop high tech innovative products, tangible and intangible.



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### Case Studies: Examples Of Innovative Chinese Companies

*So, give me some examples of successful innovative Chinese companies.*

In the telecommunication industry China is competing with the global giants. Lenovo ranks this year as the third largest smartphone vendor after Samsung and Apple, taking 5.6 percent share of the world market. Fifth on this list ranks Huawei, with a 5.2 percent market share. After Lenovo established a partnership with Motorola in 2014, its two-brand strategy focused on innovative phones gave a boost to its global reach. Now 7.9 million Motorola smartphones units have been shipped, which takes 41.8 percent of the Lenovo group with a value of 1.9 million euros. It is not difficult to imagine that Lenovo soon becomes China’s first global consumer brand.

In China, a smartphone without the mobile chat apps QQ and WeChat is nearly unthinkable. Although not yet widely known in the West, Tencent is the developer of QQ and WeChat, and is China’s largest and most used internet portal as well as one of the largest internet companies in the world. Tencent rated number one on the most valuable Chinese brands list of the China Daily with a market value of 190 billion euros, it is competing with Amazon, eBay and Alibaba.

Another example of an innovative China is the development of its railway lines on which trains can drive with the speed of over 350 kilometers per hour. China will invest \$300 billion to realize the construction of the largest, fastest, and most technologically advanced high-speed railway system in the world by 2020. China’s high-speed railway network is made up of four components: upgraded pre-existing rail lines that can accommodate high-speed trains, a national grid of mostly passenger-dedicated HSR lines (PDLs),

certain regional intercity HSR lines, and the Shanghai Maglev High-Speed Line.

The project includes several topics related to the technology of high speed. China studied and developed its own technology of traction power supply, operation control, transportation organization and the relevant facilities without the support of foreign companies.

It won't be long before a great number of Chinese companies become global players and Chinese brands concur the world. If Western firms want to have their share of this development, a sustainable relationship with a win-win perspective is of essence.

## How China Inroads Can Help To Reach That Goal?

From our local offices in Amsterdam, Shanghai and Beijing, China Inroads aims to be your independent strategic partner locally present at all times. Together we work towards your successful and sustainable business venture in China. Our services consist of a detailed market survey; searching long-term reliable business partners; maintaining relations with local partners and clients; and providing the necessary follow-up on daily activities. We are locally present, providing you with the needed insights to successfully expand your business.

*You are welcome to visit us for a free consultation at one of our offices.*

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China Inroads supports innovative companies in their expansion to the Chinese market. "China belongs to the Chinese." This philosophy is the guidance for how we match companies with the right parties and markets in China, to create a successful and effective venture. We believe that companies doing business with Chinese, making use of local resources, will be the most successful and effective. Based in Amsterdam, Beijing and Shanghai, we have our local Chinese team ready for you.

We think proactively and offer (un)solicited advice on various issues that companies encounter before, during and after entry to the Chinese market. China Inroads believes in a local, long-term relationship. We like to act as your important local strategic partner. You are welcome to visit us for a free consultation at one of our offices. We are of course happy to visit your office as well.