

China Business Forecast 2022

“China for China + Decoupling”

November 24th, 2021

China partner of  **CLEARWATER**
INTERNATIONAL

InterChina










英特华

www.InterChinaPartners.com

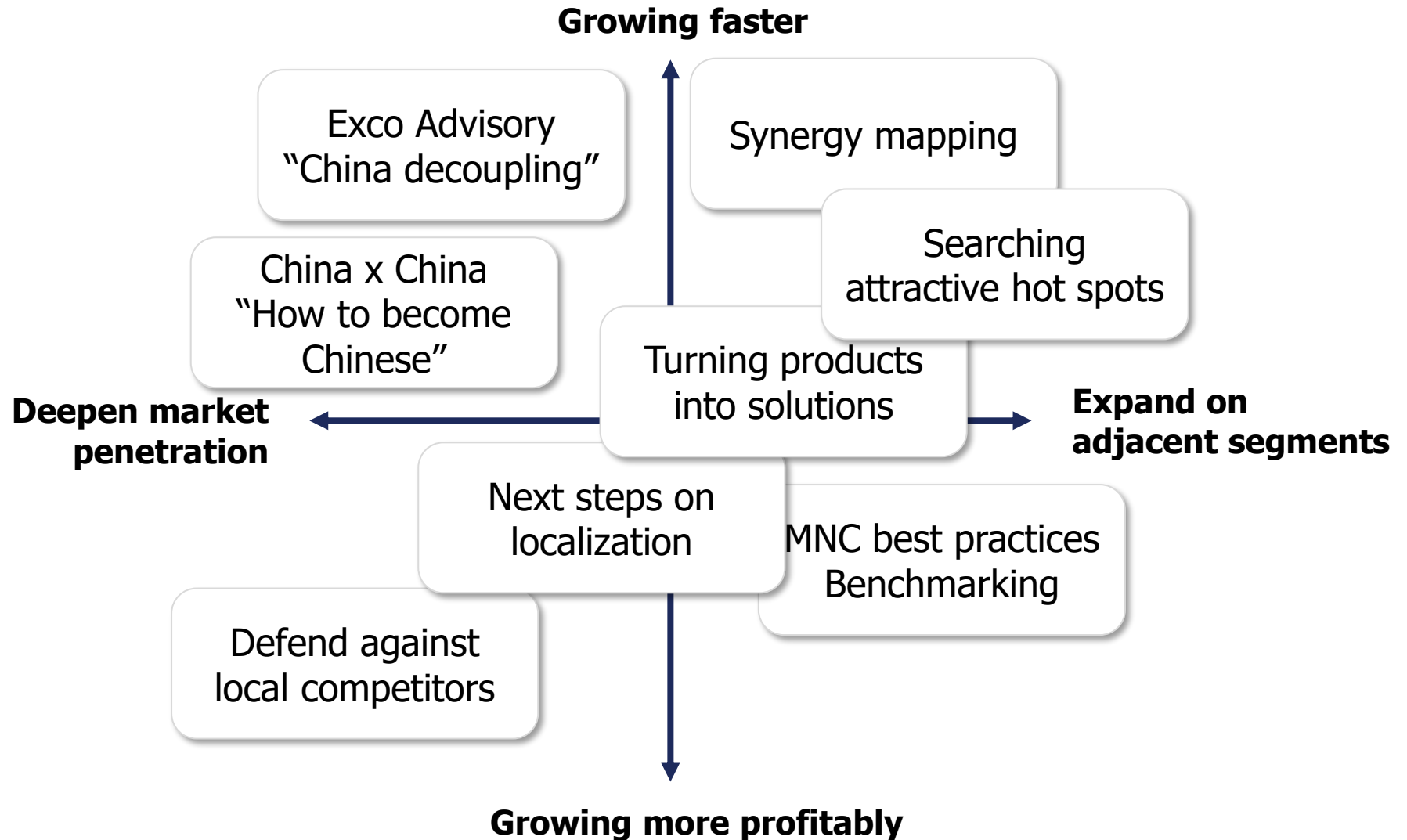
Sources of this report (1/3):

We surveyed 287 China country managers in Oct/ Nov 2021

Sectorial mix of survey respondents

287 co's			
Large equipment	20%	<ul style="list-style-type: none"> Power generation. Production machinery. Automation equipment. 	
		<ul style="list-style-type: none"> Mechanical/electrical parts. Assemblies. Light equipment. 	
Industrial parts	19%	<ul style="list-style-type: none"> Vehicle makers. T1 automotive parts. T2 automotive parts. 	
		<ul style="list-style-type: none"> Chemicals. Metals, Composites. Textiles. 	
Automotive	13%	<ul style="list-style-type: none"> Pharmaceuticals. Medical devices. Diagnostics. 	
Materials	9%	<ul style="list-style-type: none"> F&B, HPC. Durables. Services. 	
Healthcare	9%	<ul style="list-style-type: none"> Logistics. Certification, testing. Financial. 	
Consumer goods	8%		
Business services	8%		
Other	13%		

Sources for this report (2/3): Our recent Strategy Projects



Sources for this report (3/3): Learnings from our latest transactions

InterChina's deals closed in the past months

<p>A Leading China based Medical Product Brand China</p> <p>divested its equity holdings to</p> <p>A professional household medical device manufacturer China</p> <p><i>Signed in 2021 Buyer advised by InterChina</i></p>	<p>A leading global tank storage service provider China</p> <p>Divested its equity holdings to</p> <p>A China based company specializing in providing storage and transfer of liquid chemical products and logistics services China</p> <p><i>Signed in 2021 Seller advised by InterChina</i></p>	<p>A global leading automation supplier providing progressive moving solutions Sweden</p> <p>acquired</p> <p>A China based premium vacuum gripping system component manufacturer China</p> <p><i>Signed in 2021 Buyer advised by InterChina</i></p>	<p>SANDVIK Coromant</p> <p>Sandvik Coromant The global leading supplier of cutting tools and services to the metal cutting industry Sweden acquired</p> <p>Chuzhou Yongpu China based premium solid round tools manufacturer China</p> <p><i>Sandvik Coromant was advised by InterChina</i></p>	<p>MYCRONIC When passion meets innovation</p> <p>Mycronic A leading global electronics manufacturing equipment supplier Sweden acquired a majority stake in</p> <p>Shenzhen Huan Cheng Xin Precision Manufacturer Co., Ltd. A supplier of solder paste printing solutions in the SMT industry China</p> <p><i>Mycronic was advised by InterChina</i></p>
<p>Grupo Antolin Tier 1 Automotive Supplier Spain</p> <p>established a JV with</p> <p>Shanghai NAEN Auto Technology High-tech player in the Automotive electronics space China</p> <p><i>Grupo Antolin was advised by InterChina</i></p>	<p>REPSOL Energy & Chemicals Manufacturer Spain</p> <p>Entered a technology transaction with</p> <p>Shenhong Group Petrochemicals China</p> <p><i>Repsol was advised by InterChina</i></p>	<p>EVOLCA GROUP Evoca Group Coffee machine Manufacturer Spain</p> <p>Acquired a majority stake in</p> <p>Macas Guangzhou MACAS Electronics Technology Coffee Machines Manufacturer China</p> <p><i>Repsol was advised by InterChina</i></p>	<p>Bystronic Bystronic Sheet Metal Cutting And Bending Switzerland</p> <p>acquired the remaining 30% stake in</p> <p>DNE LASER Shenzhen DNE Laser Equipment Laser Cutting Machinery Maker China</p> <p><i>Bystronic was advised by InterChina</i></p>	<p>ODFJELL Odfjell Terminals China Leading Global Tank Storage Service Provider China</p> <p>divested its equity holdings in Odfjell terminals (Dalian) to</p> <p>VTti Fast-growing independent provider of energy storage worldwide The Netherlands</p> <p><i>Odfjell was advised by InterChina</i></p>

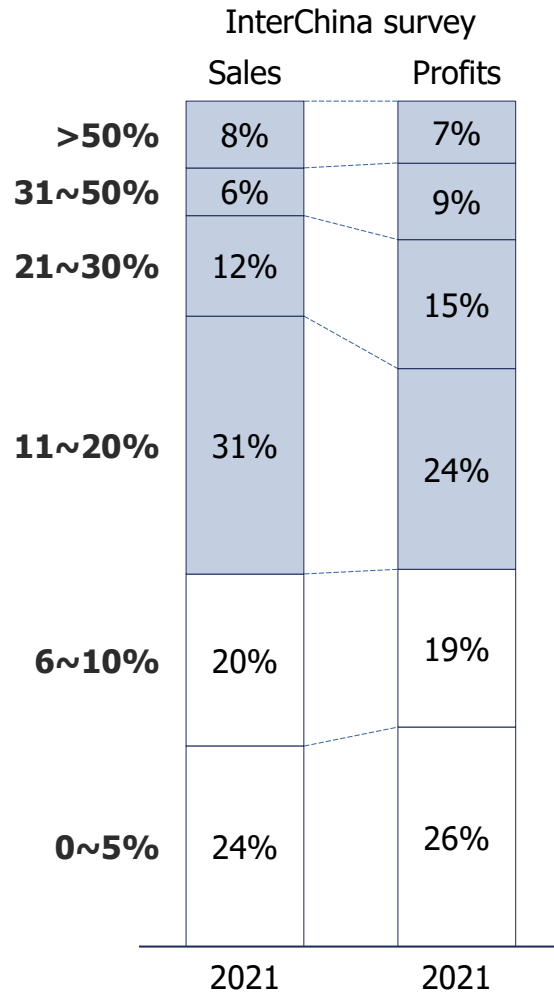
So far, very
good performance

MNCs are doubling down on their China businesses

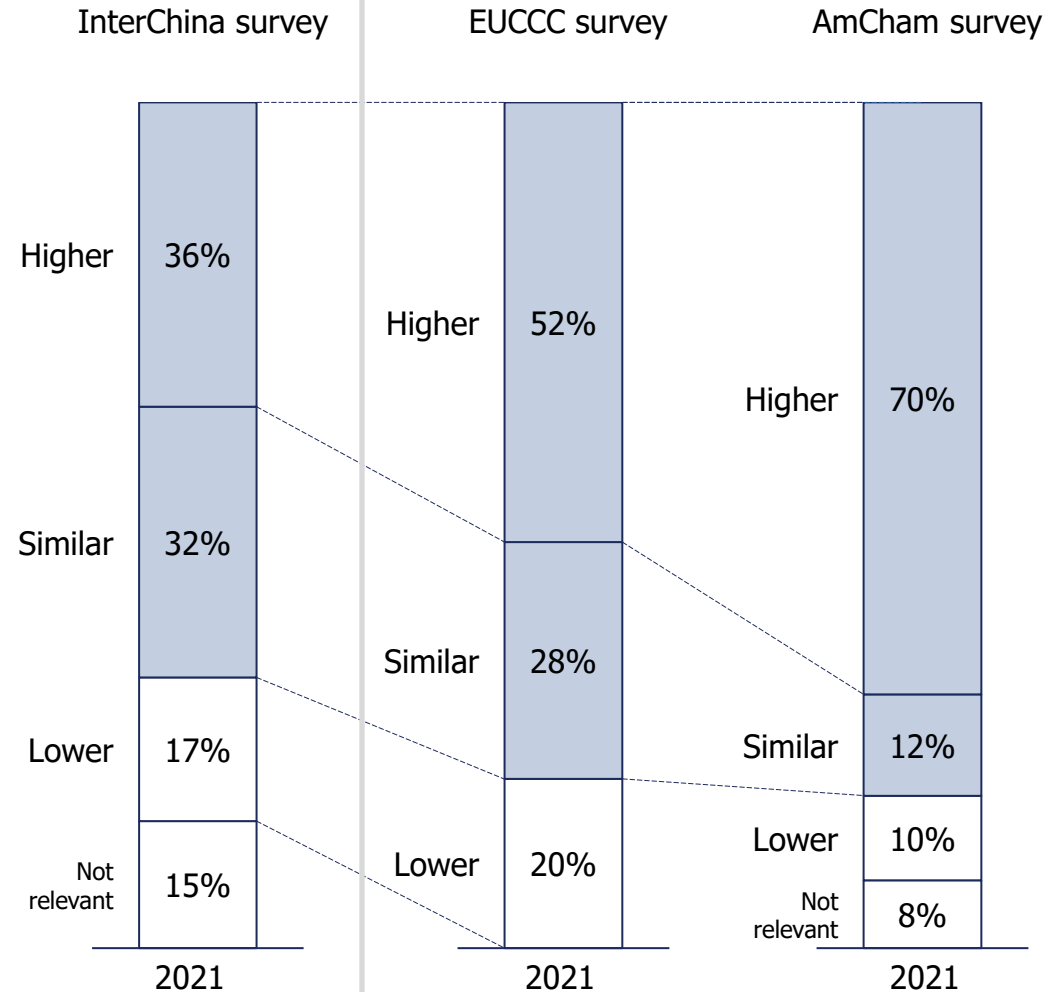
China forecasted to contribute more revenue and profit to HQ at scale.



China's contribution to MNCs' global business



China investment ROI forecast compared to other markets

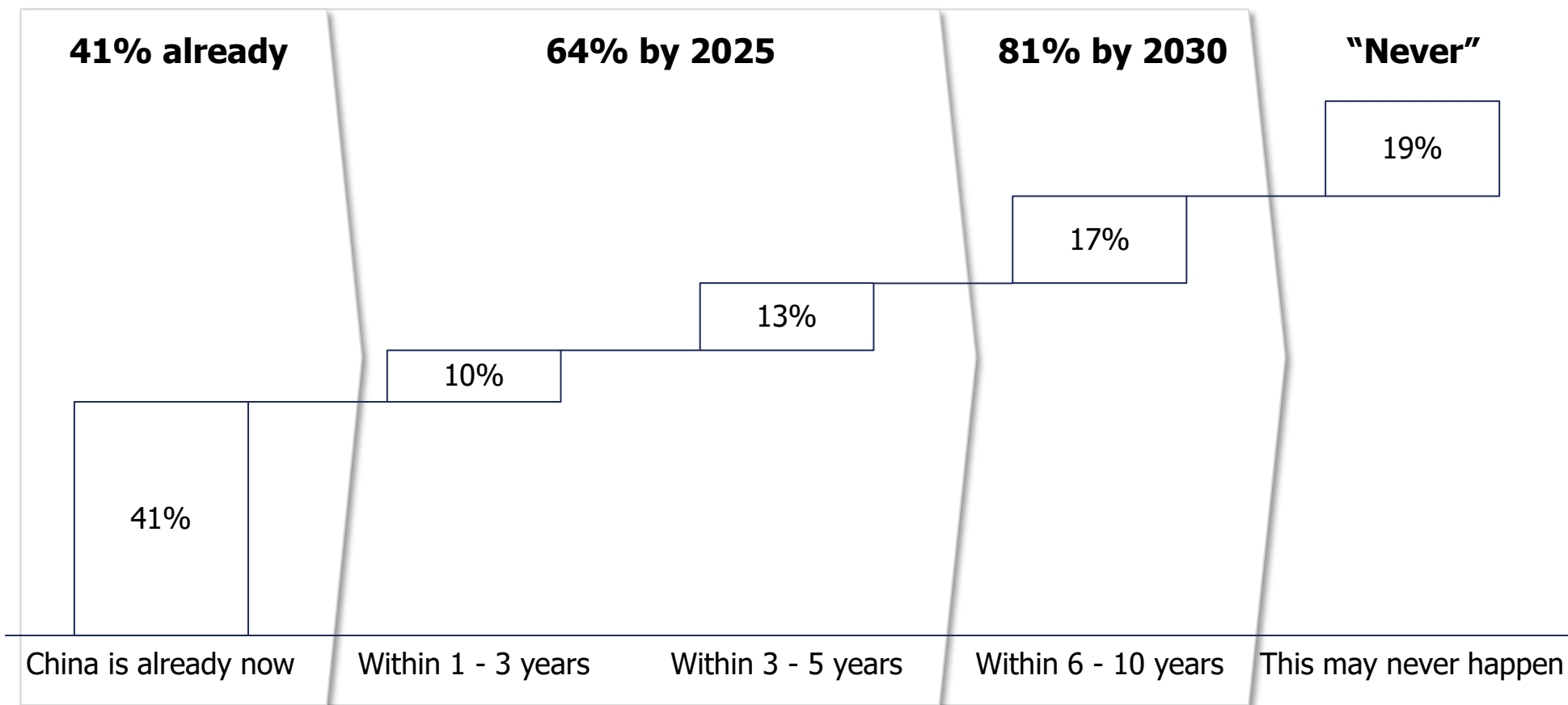




81% of MNCs say that by 2030 China is the top priority

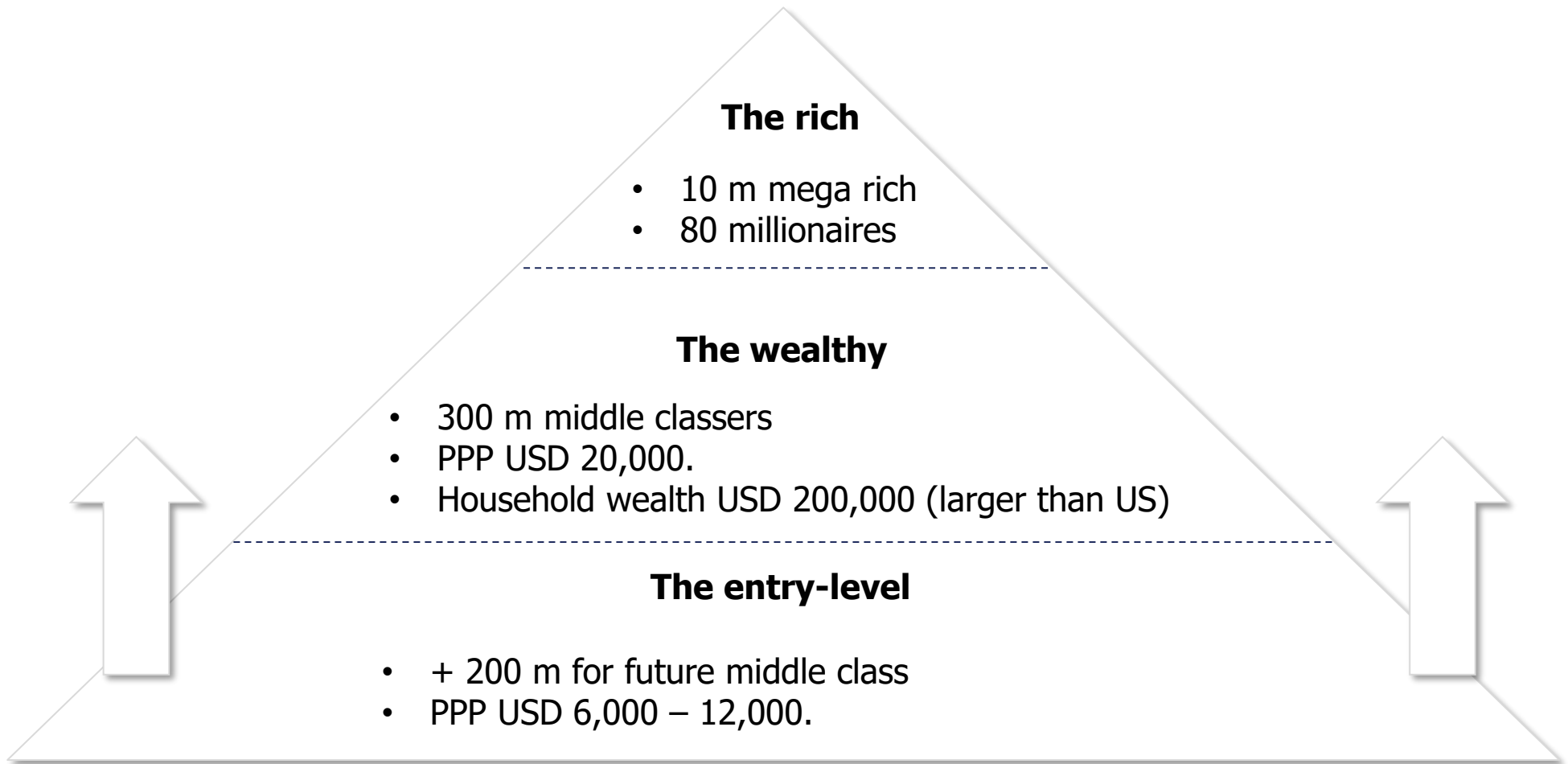
How long will it take until China is your company's global no. 1 or no. 2 market?

No. of respondents, as % of total respondents surveyed



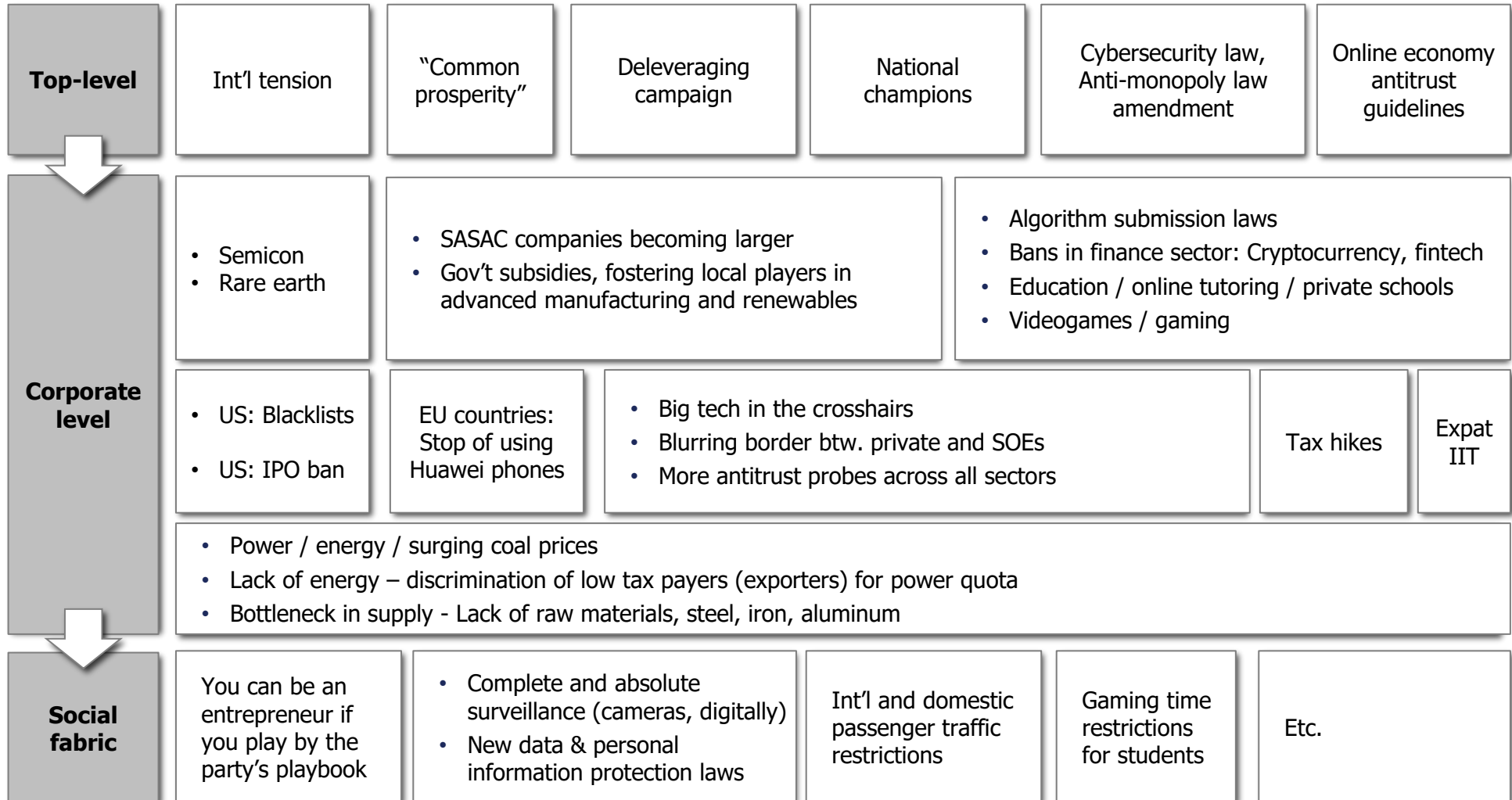
Simple but powerful reason:
Consumption growth and expansion of the middle class

**No other part of the world will see the emergence of
200 m extra consumers in this decade**



However, there are growing concerns about the many deep changes happening in China... Is winter coming?

(Some of the topics discussed by MNC c-suites)



We have a shared view on the overall direction

"China's train of development and innovation is departing quickly. **You are either on the train, or you're left back at the station.**"

President APAC
EU Techn. Conglomerate

"The opportunity is there for MNCs to take. **This country and market requires full commitment.** You are either at the table deciding on the menu... or you're on the menu.

President China
MNC Chemicals Group

Our view

- **China is the main growth opportunity at scale in the world for the next 10 years.**
- There is room and opportunity for global players.
- However, the **rules of engagement and the playing fields are changing fast.**
- Key concerns are geopolitics, local competition, new ecosystems, and business models.

→ **We need to adapt, quickly.**




Politics becomes business

CEO Takeaway

Know your playing field: Open or Restricted China?
Sensitivity, empathy and curiosity
more needed than ever

Business as usual' is gone forever... Decoupling is here to stay

Block's differentiation moving from Transactional to Value Items.

Scenario / Probability	Characteristics	Role of Foreign Investors
 <p>"Constructive decoupling" 70% (most likely)</p>	<ul style="list-style-type: none"> • Semi-friendly, gradual, pragmatic decoupling • Coop. and unilateral dev't simultaneously 	<ul style="list-style-type: none"> • Continued relevance • Techn. and know-how needed
 <p>Hardcore decoupling 20% (less likely)</p>	<ul style="list-style-type: none"> • Constant crises and antagonistic attitudes • Trade barriers increase fast • Speed up of regionalization 	<ul style="list-style-type: none"> • Increased uncertainty... • ... as MNCs are political targets
 <p>Conflict 10% (unlikely)</p>	<ul style="list-style-type: none"> • As above, plus military crises / armed conflicts • Trade blockade, radical disruptions of standards 	<ul style="list-style-type: none"> • Meltdown • Full-scale boycotts

Negotiation Moving from "Transactional Items" Into "Values"

Reshoring of key industries

Tariffs

Technology Decoupling

Human Rights

National Sovereignty

With me or against me

Standards War

Trade Balance

IP Self Sufficiency

Political Model

Empathy, Sensitivity and Curiosity will become critical soft skills required to understand the reality, and react to it.



Crackdown on Big Tech

- Destroys private initiative.
- Set back to SOE-era.
- Control of private capital and co's.

- Regulate an out-of-control industry.
- Protect national data vs. foreign entities.
- Protect users from data abuse.



996 work culture Condemned by Supreme Court

- Destroys private initiative.
- Limits co's growth and freedom of work.

- Supreme Court applying the labor law.
- Increase natality rate.
- Improve quality of family (life).



Gaming Limit play time for minors

- Attack on private corp's.
- Control of society.
- Limit individual's freedom.

- Regulate prev. unregulated areas.
- Protect society from gaming addiction ("mental opium").



Education Suspending pro- fit tutoring

- Destroys private initiative.
- Promotes separation from Western values.

- Recovers control over a sector out of control.
- Helps to promote family values, reduces educational costs, reduces pressure on children and improve quality of life.



KOLs, Fancubs Blacklisting

- Exert control over society.
- Impose a set of values.

- Avoid groups outside the system.
- Prevent bad values / fanaticism, and life without moral purpose.

China's priorities are and will be mainly of domestic nature and drive the trends of going from quantity to quality

HIGHER EFFICIENCY

Financial Deleverage & Sustainable System

- **Debt control**
- **ForEx control**
- **Stock market revamp**

Consolidation & Capacity Decrease

- Mainly from closure of **private** co's and **"idle" capacities**.
- **Price spikes**
- **Supply problems**

HIGHER COMPLIANCE

Environ. Protection & Decarbonization

- **Top priority** (will NOT go away)
- **Further closure** of inefficient or polluting factories
- **Higher costs** – cheap capacity is closed down

Compliance & Governance

- Unified code and application for personal income tax and corporate tax
- Social credit systems (for co's and individuals)

CHINESE CHARACTERISTICS

Strengthen Party & Party Values

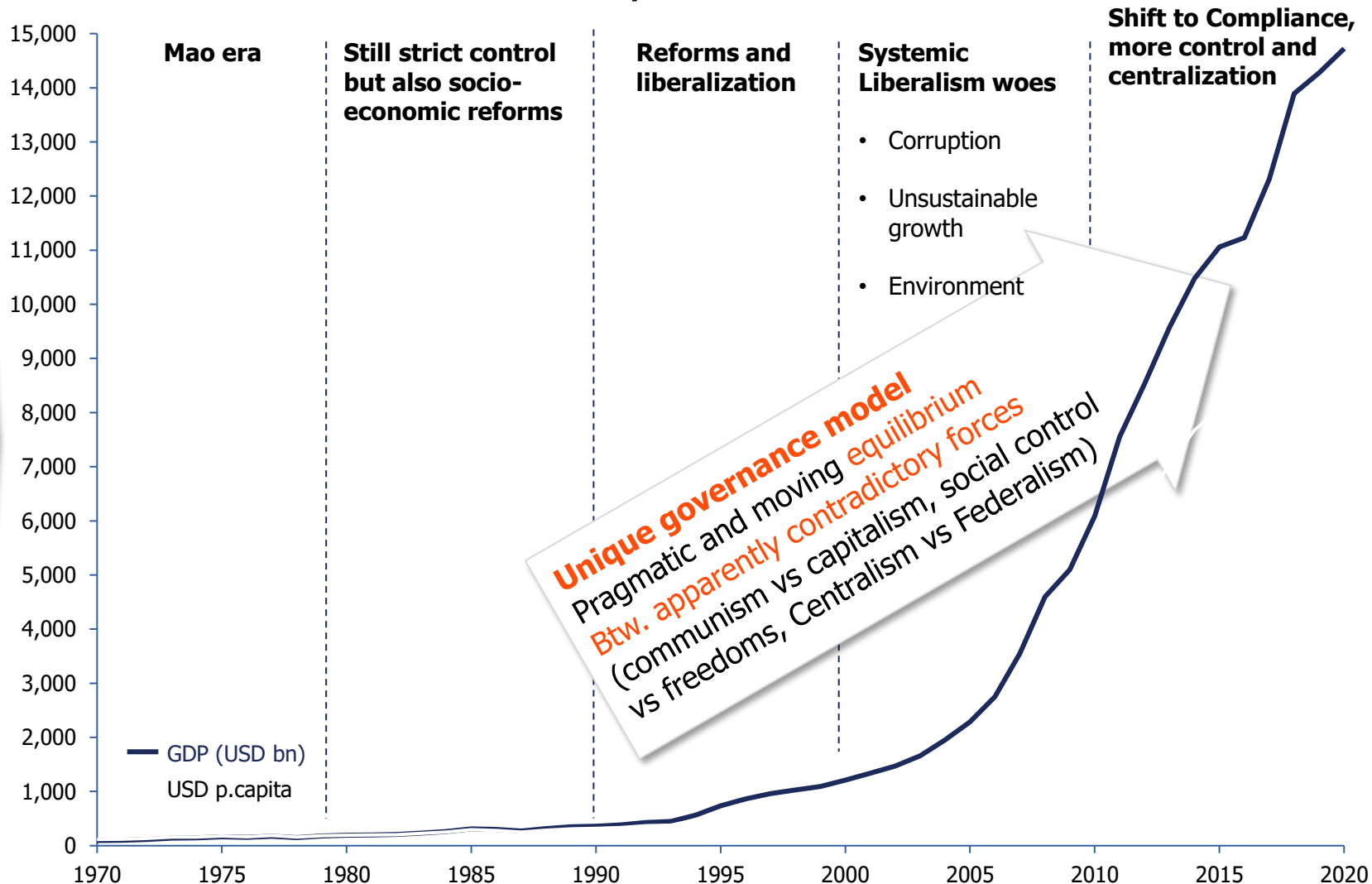
- Grassroot CP
- Anti-corruption
- Alignment
- Values: Common Prosperity

Regulated Corporate Ecosystems

- Big Tech: Avoid state within state. Ensure co's follow rules.
- Control/ regulate data economy
- Common prosperity: Donations, wealth distr., tax enforcement

Bottom line, China is developing into... something new, in its own terms

China's GDP development 1970 - 2020



China has broken a 200-year old Paradigm:

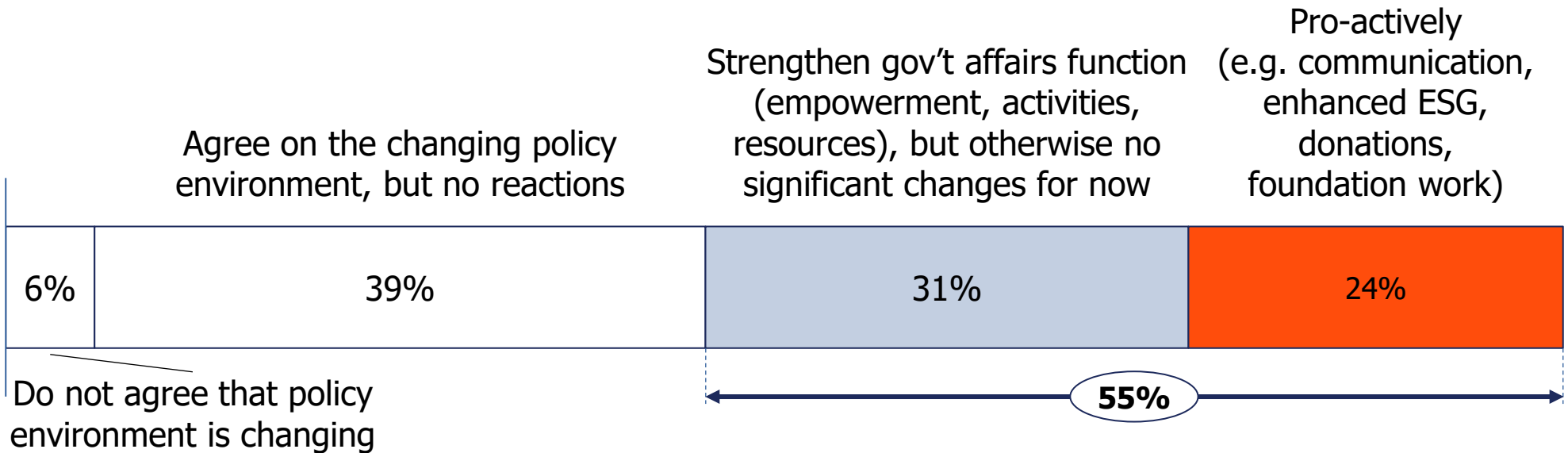
"Only liberal, democratic and capitalist systems which endorse fair distribution of power and free flow of capital, people and commodities can, in the medium to long term, **create wealth and provide a sustainable social system**".

MNC are taking actions already to changing policy environment

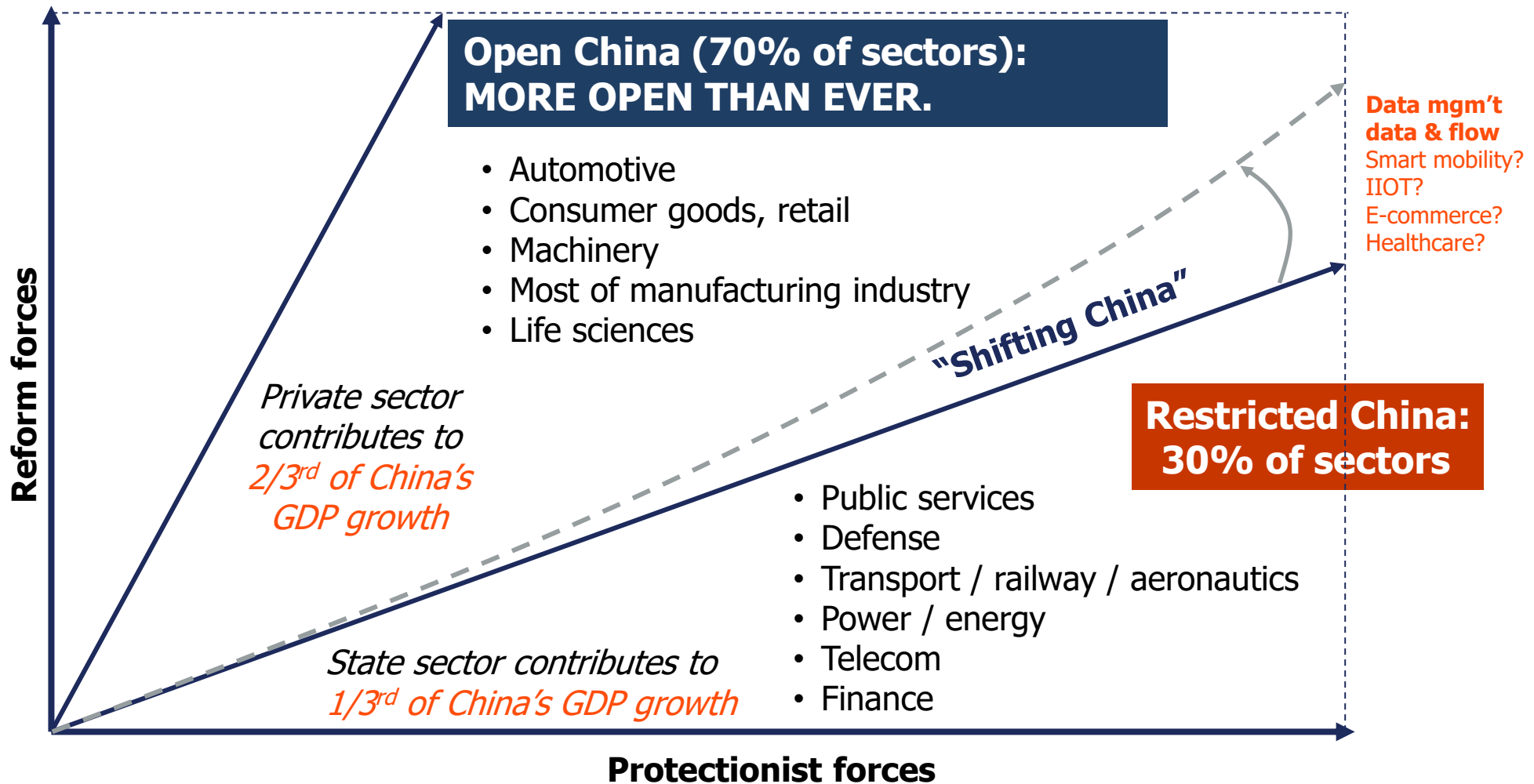
Over half of co's plan to adapt. 24% see this as an opportunity.



How will you react to a China that is more policy driven?



You may need to re-define where you are...
The “70/30 China” model describes a complex reality



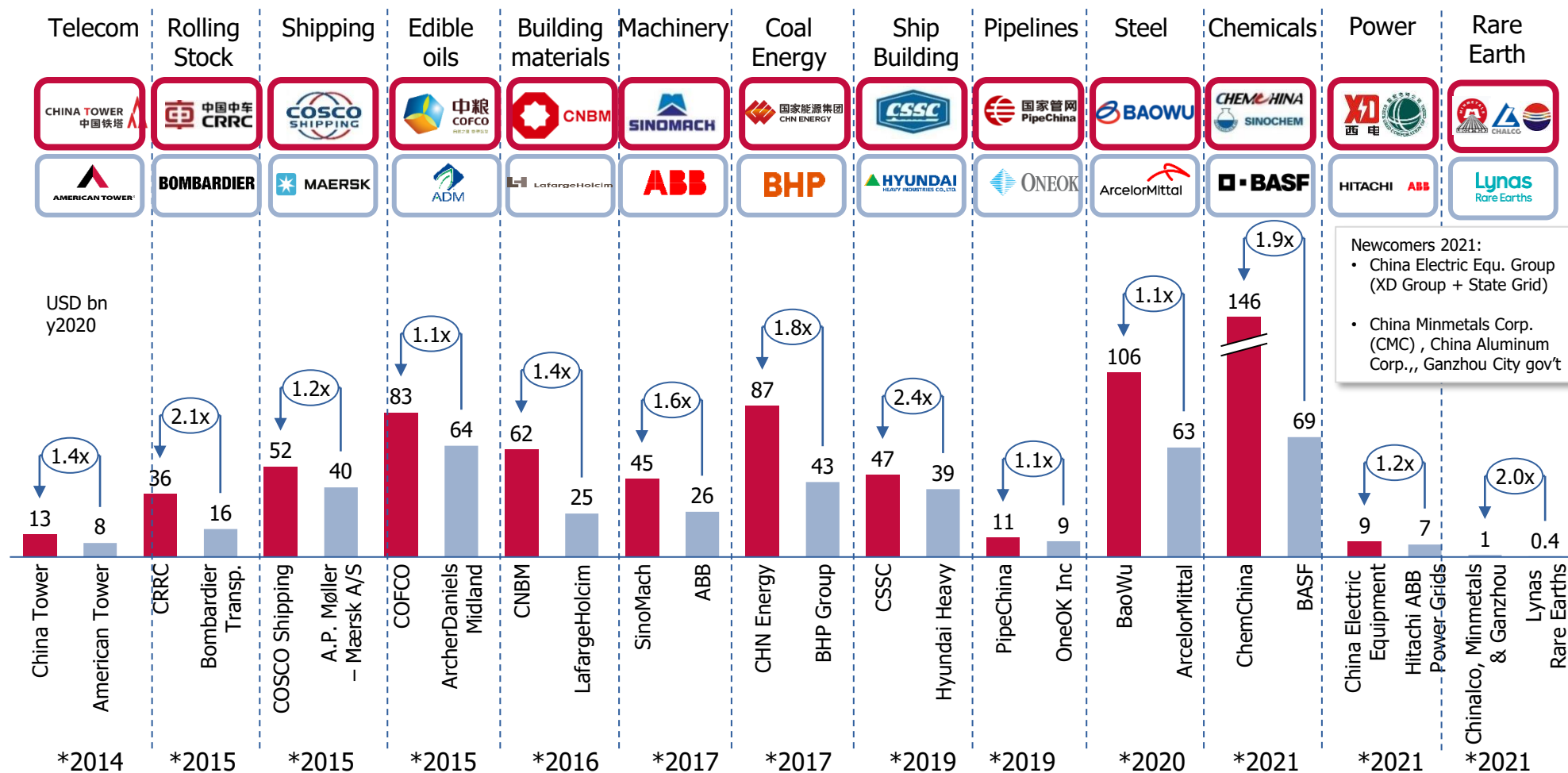
Competition & New Ecosystems

CEO Takeaway:

The Plug&Play-model no longer works.
What does?

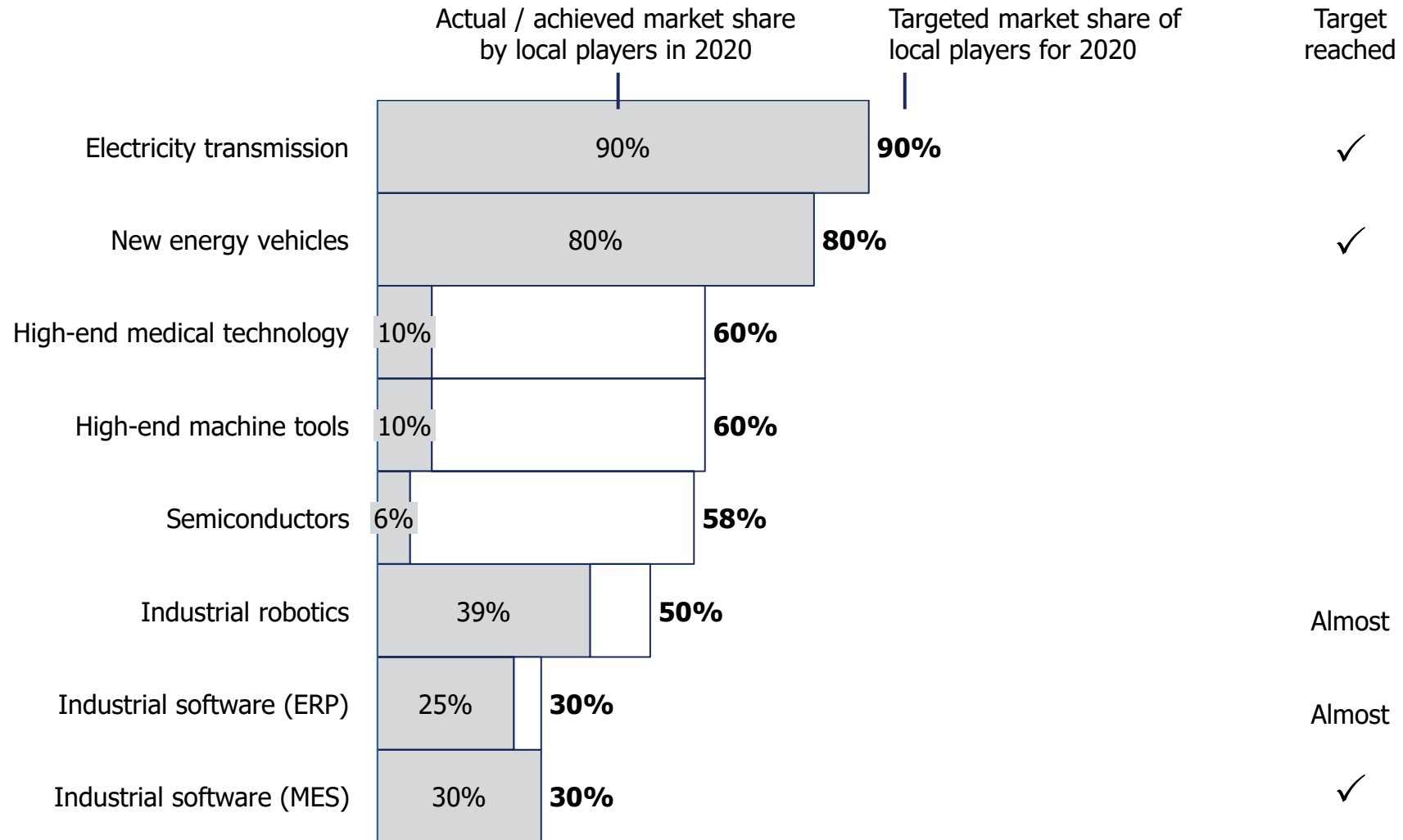
China keeps building national champions... Consolidation will be a key driver in 2022-2025

Chinese National Champions vis-à-vis their next global MNC competitors, USD bn sales (y2020)



The Chinese manufacturing sector is transforming and creates higher value-added, technology players...







China's Made In China 2025 Policy



New Chinese ecosystems are transformative – connecting the dots

Customer access points, solutions, services and values

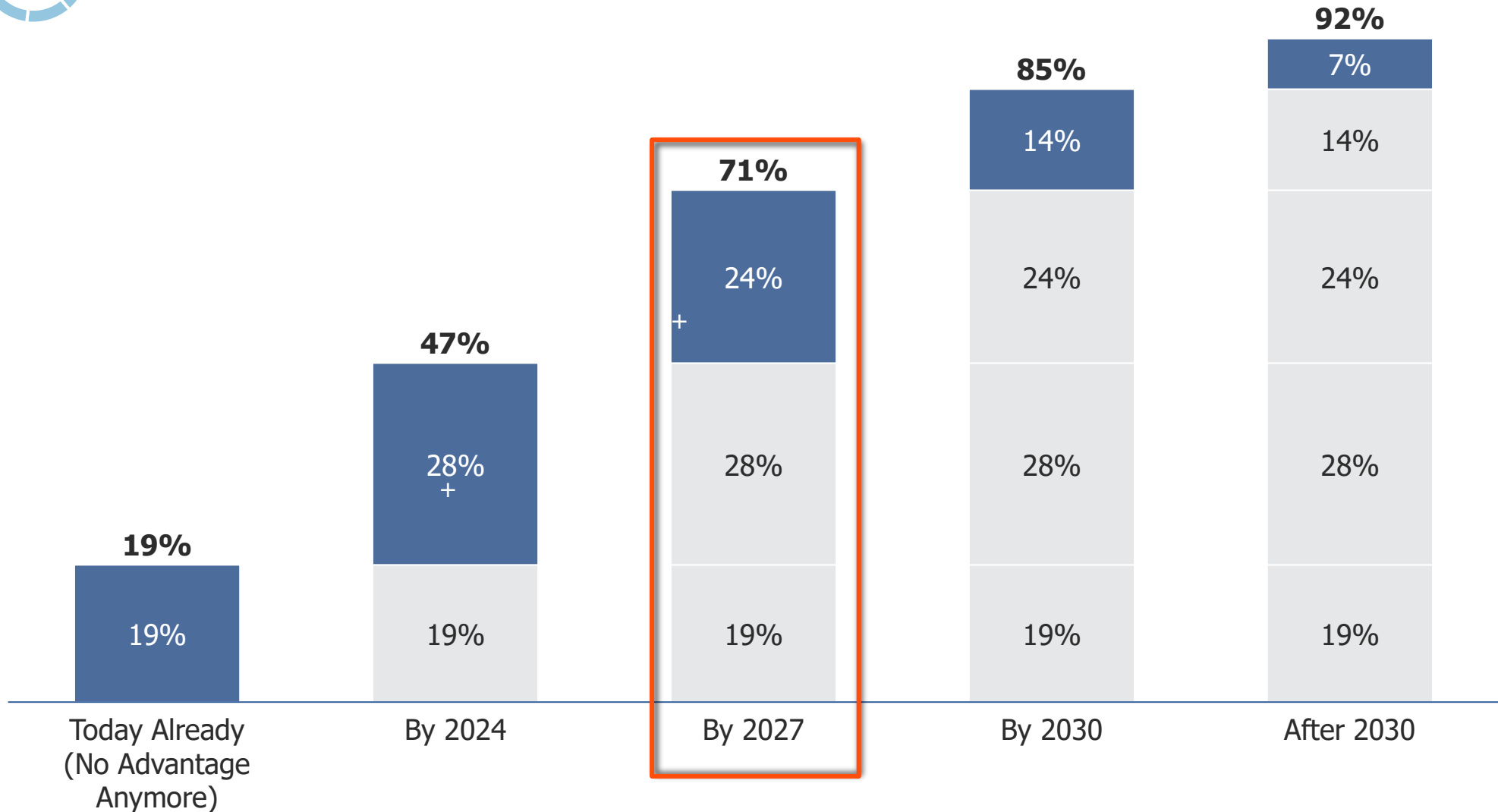
Leading Chinese groups **migrate across sector boundaries and create larger ecosystems**

 <ul style="list-style-type: none"> • C2C Taobao • B2C Tmall • Mobile payments Alipay • Ant Financial • Big data, cloud, mobility • Smart logistics / Cainiao • Health / diagnostics 	 <ul style="list-style-type: none"> • Telecom equ. • Consumer electronics • Enterprise / IoT • Supply chain / chips • Semicon prod. equ. 	 <ul style="list-style-type: none"> • Chemicals • Agricultural • Energy, EPC, logistics • Real estate, finance • Light-weight, mobility
 <ul style="list-style-type: none"> • Insurance • Finance • Property • Automotive • Healthcare • Smart city 	 <ul style="list-style-type: none"> • Online retail • O2O retail • Big data analytics • Logistics, drones • Financial services 	 <ul style="list-style-type: none"> • Rolling stock • Railway infrastructure • Water treatment equ. • Wind power • NEV. H2 buses • Logistics • Financial services
 <ul style="list-style-type: none"> • Social network • Gaming • Fintech • Business services • Online advertising • Retail 	 <ul style="list-style-type: none"> • Smart phones • Smart lifestyle IOT • Internet services • New retail formats • Mobility, cars 	 <ul style="list-style-type: none"> • Iron and steel • EPC • Gas, coal, chemicals • Hydrogen • Financial services • Production services
 <ul style="list-style-type: none"> • Search engine • Online advertising • Cloud business • Financial services • Autonomous driving • Medical & health 	 <ul style="list-style-type: none"> • Construction equ. • Mining equ. • Financial services • Material handling • Wind turbines • IIOT platform Rootcloud 	 <ul style="list-style-type: none"> • Cars – entry level • Cars - premium • On-demand mobility • Connected intel. vehicles • Shared ownership • Flying cars • Transport ecosystem

What is the impact for MNC? 71% of co's expect to lose their traditional advantage as a foreign / int'l co' within 5 years



By when will you have lost your "origin advantage" as a key competitive advantage in China?



How do MNC react to all of this?

CEO Take Away

Full commitment

Achieve Scale

Ecosystems Participation

Aggressive Localization

1. SCALE

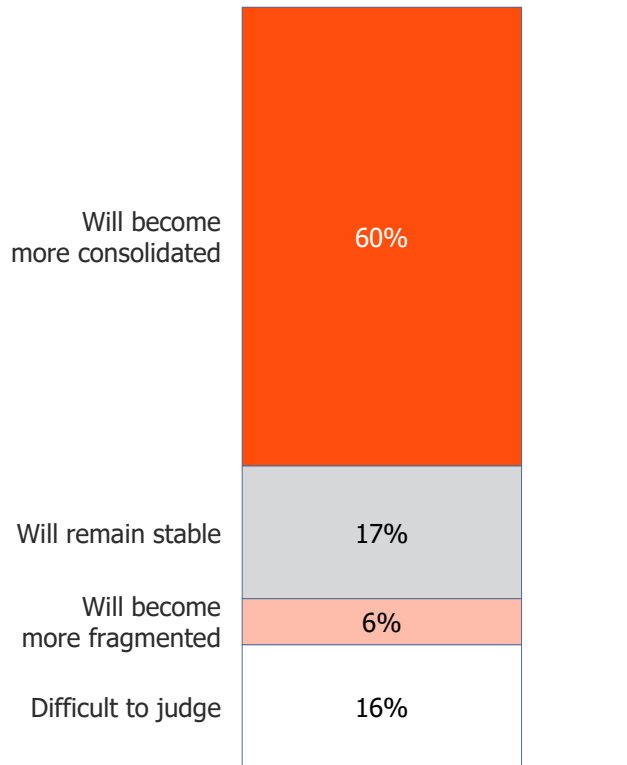


Sector consolidation is a main driver – and “scale” is becoming one of the main goals for most MNCs

Sector Consolidation

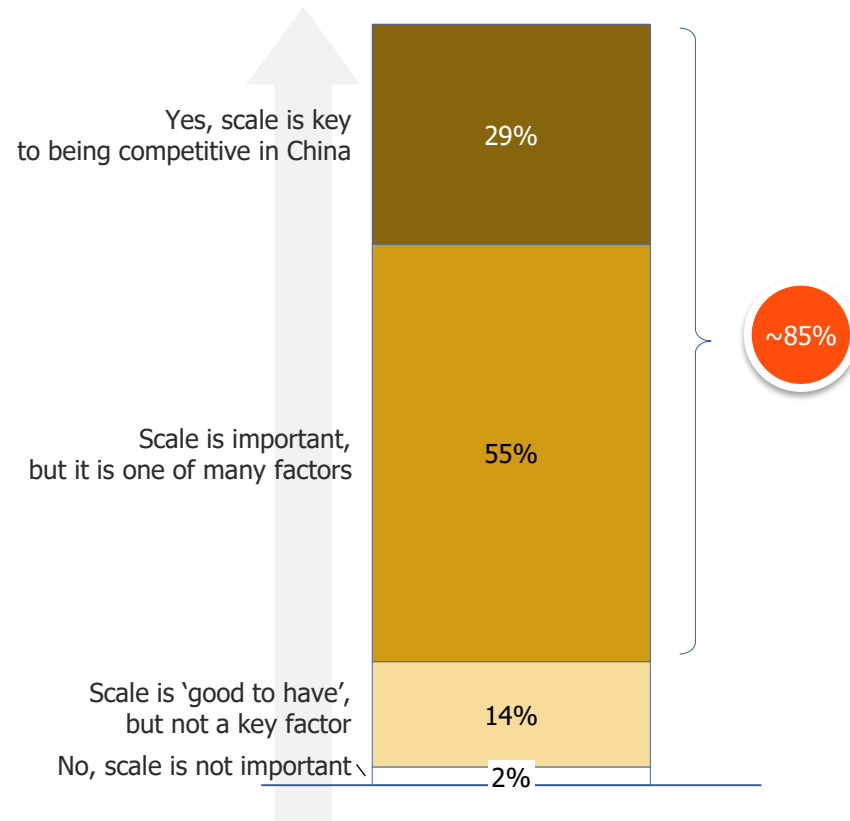
Sector Structure

Q: How do you expect the structure of your sector to evolve over the next 3 years?



Importance Of Scale

Q: With the rapid growth of the Chinese market and Chinese competitors, scale in China is an increasing concern for many international companies. Do you consider scale in China to be a KSF for your company?

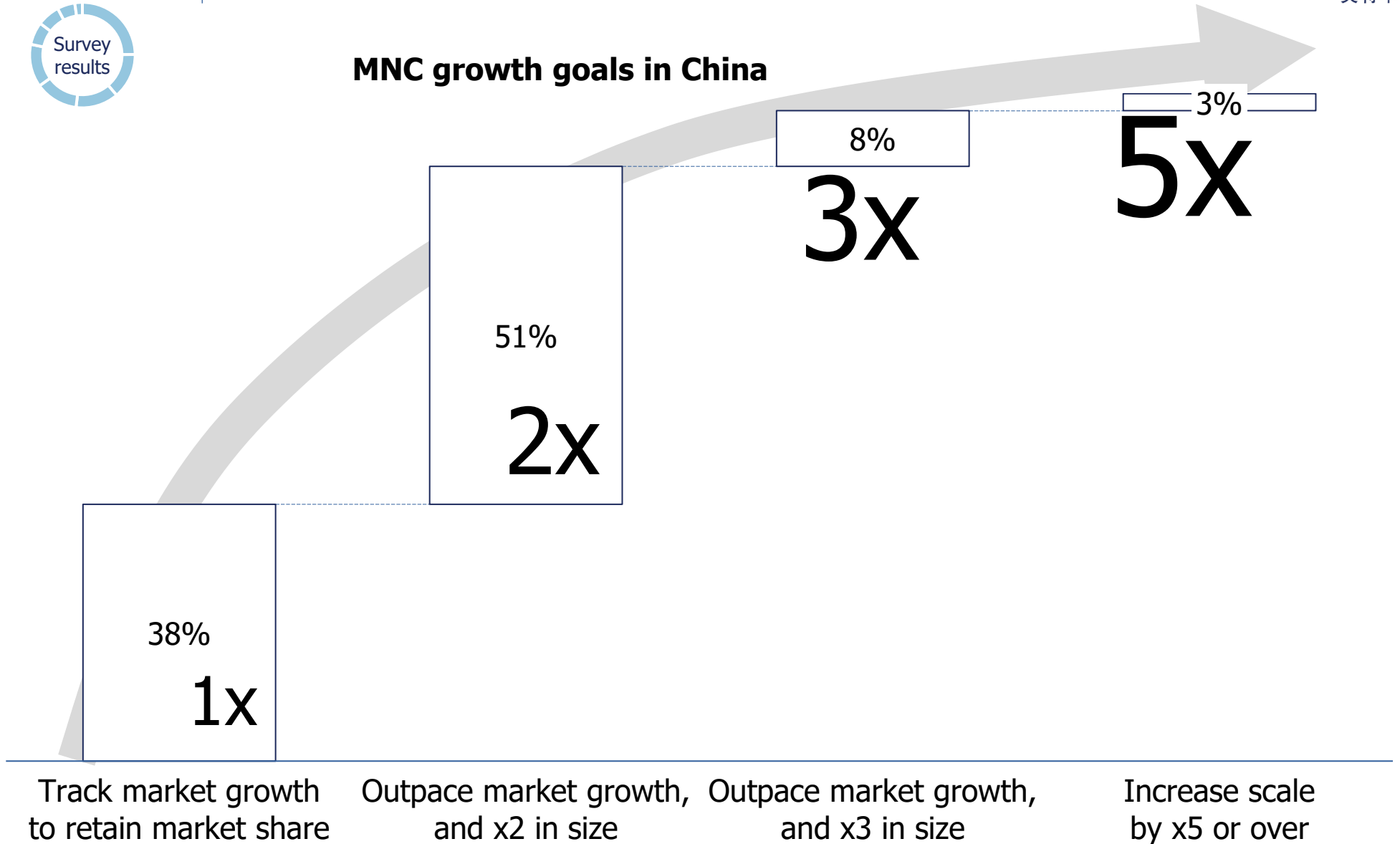


1
SCALE



As a result, **62% of MNCs are looking to scale up and outpace market growth** over the next 5 years

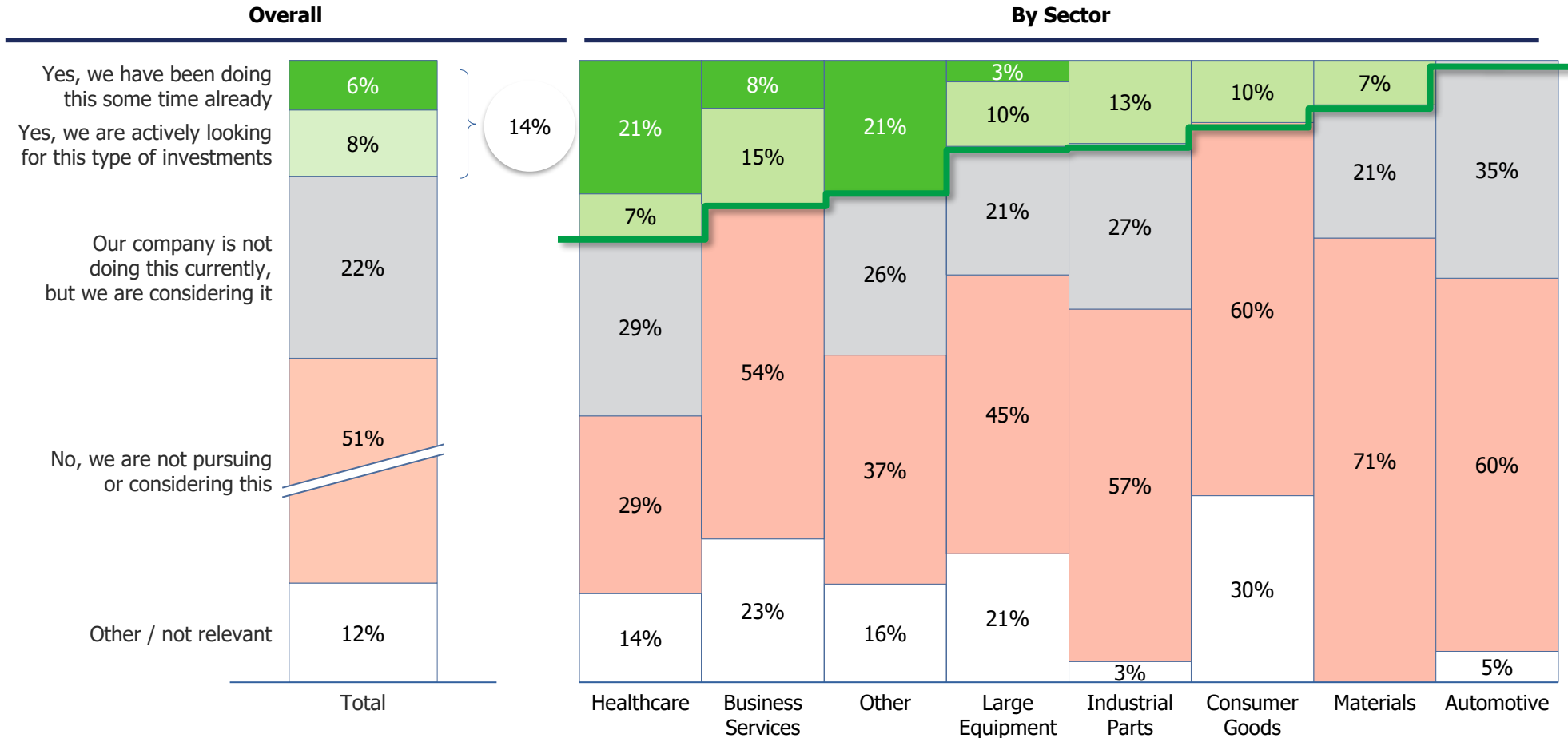
MNC growth goals in China



























Ecosystems: A small but meaningful share of MNCs are already active in the ecosystem playfield

Are you investing into new tech and ecosystem co's in China?

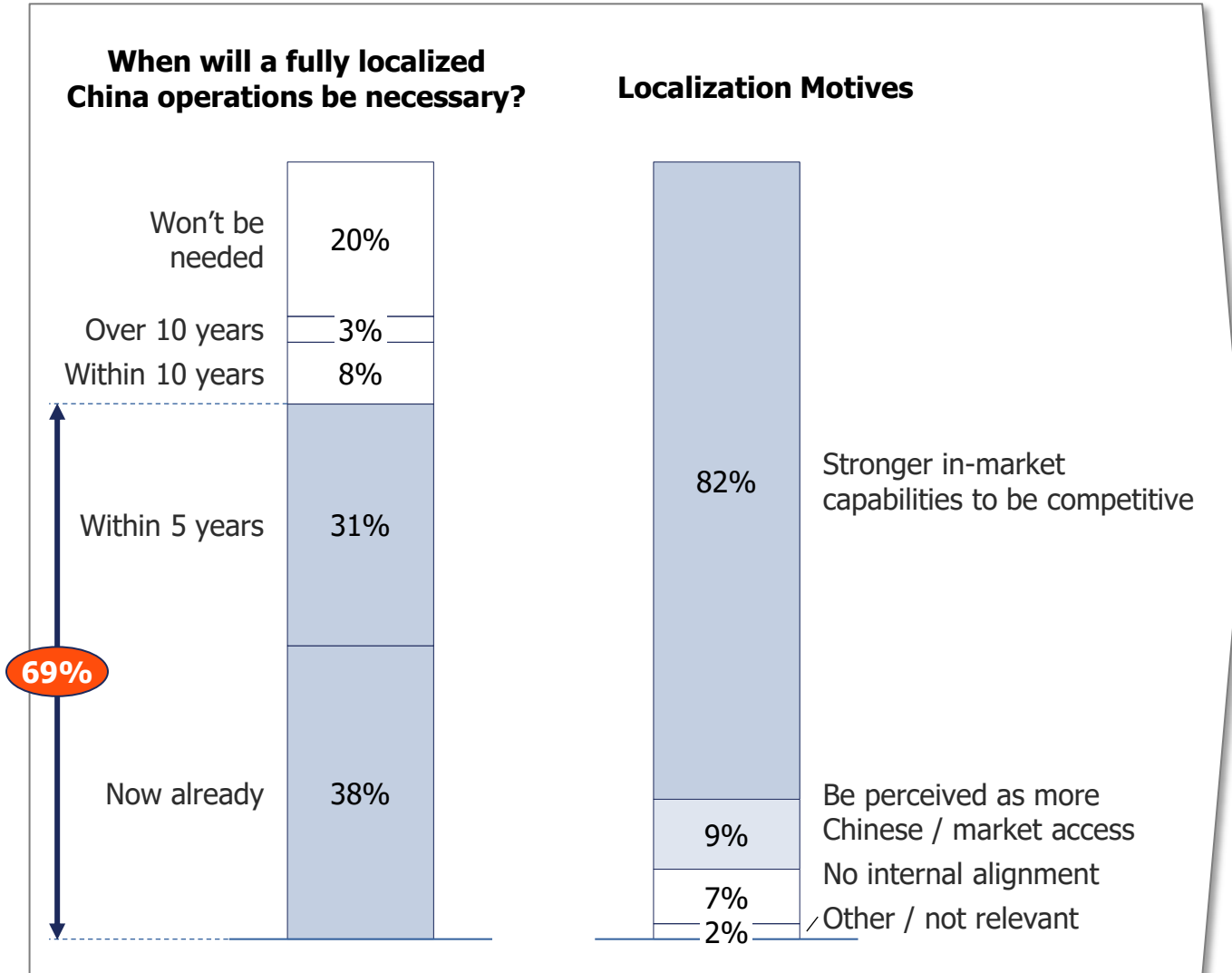


Ecosystems: MNCs invest in local tech players and become increasingly flexible in their acquisition modes

Tech-core	Data- Service	Access Eco-system
Acquisitions of product businesses Completing portfolio by cat. / segments	Acquisition of service delivery capacity Project access, local engineering team	Partnerships of co's that enable market access
 Eaton buys Huanyu High Tech and Jiangsu Yineng Electric (both 2021) Product: LV breakers, data center busways Target sales p.a. USD 106 m, USD 60 m Deal structure: 50% share in each target	  TFS and InnoForce to form Thermo Fisher Bio Pharmaceuticals (Hangzhou) (2021) Product: Pharma dev't & mfct services Deal size: USD 300 m Deal structure: JV, 51%	  Cisco partners with Inspur Yunke (2016) Product: Cloud for gov't customers Deal size: USD 280 m Structure: JV, minority share (49%)
  Thermo Fisher invests in WuXi Diagn. (2021) Product: Online diagnostics platform Deal size: USD 150 m (B round) Deal structure: Minority share, joined by 2 PEs	  Bosch invests into Momenta.ai (2021) Product: AI s/w for autonomous cars Deal size: USD 500 m (financing round) Deal structure: Minority share,	  TFS (Life Technologies) and DaAn Gene form Guangzhou LT DaAn Diagnostics. (2012) Product: Molecular diagnosis assays Deal size: USD 5.4 m (registered capital) Deal structure: JV, 57.5%
  ABB acquires Shanghai Chargedot (2019) Product: Charging stations Deal size: not disclosed Deal structure: 67%, rest in 3 years	  Honeywell (SPS) partners with Flux (2017) Product: Warehouse mgmt. software Deal size: not disclosed Deal structure: Minority share (25%) in Flux, + set up of new JV (75%)	  Microsoft JVs w. China Electronics Techn. Group → C&M Inform. Techn. (2015) Product: S/w (Windows 10) for gov't customers Registered capital: USD 40 m. Structure: JV, 49%.
  Schneider Electric partners w. Delixi (2006) Deal structure: JV, 50%. Rev. grow 4x since 2006. In 2019, the JV acquired 2 businesses from Delixi (wiring devices, meters for tariff, gas, and power)	 CapitaLand acquires Hyper Data Center Campus from AVIC (2021) Product: Data center (55MW capacity) Deal size: USD 564 m. Structure: 100%.	  Accenture Interactive buys Shanghai HO Communication (2018) Product: Digital marketing agency Structure: 100% acquisition

3 LOCALIZATION

~70% of MNCs will be fully localized in China within 5 years, ...
driven by the need to be locally competitive



CxC+D

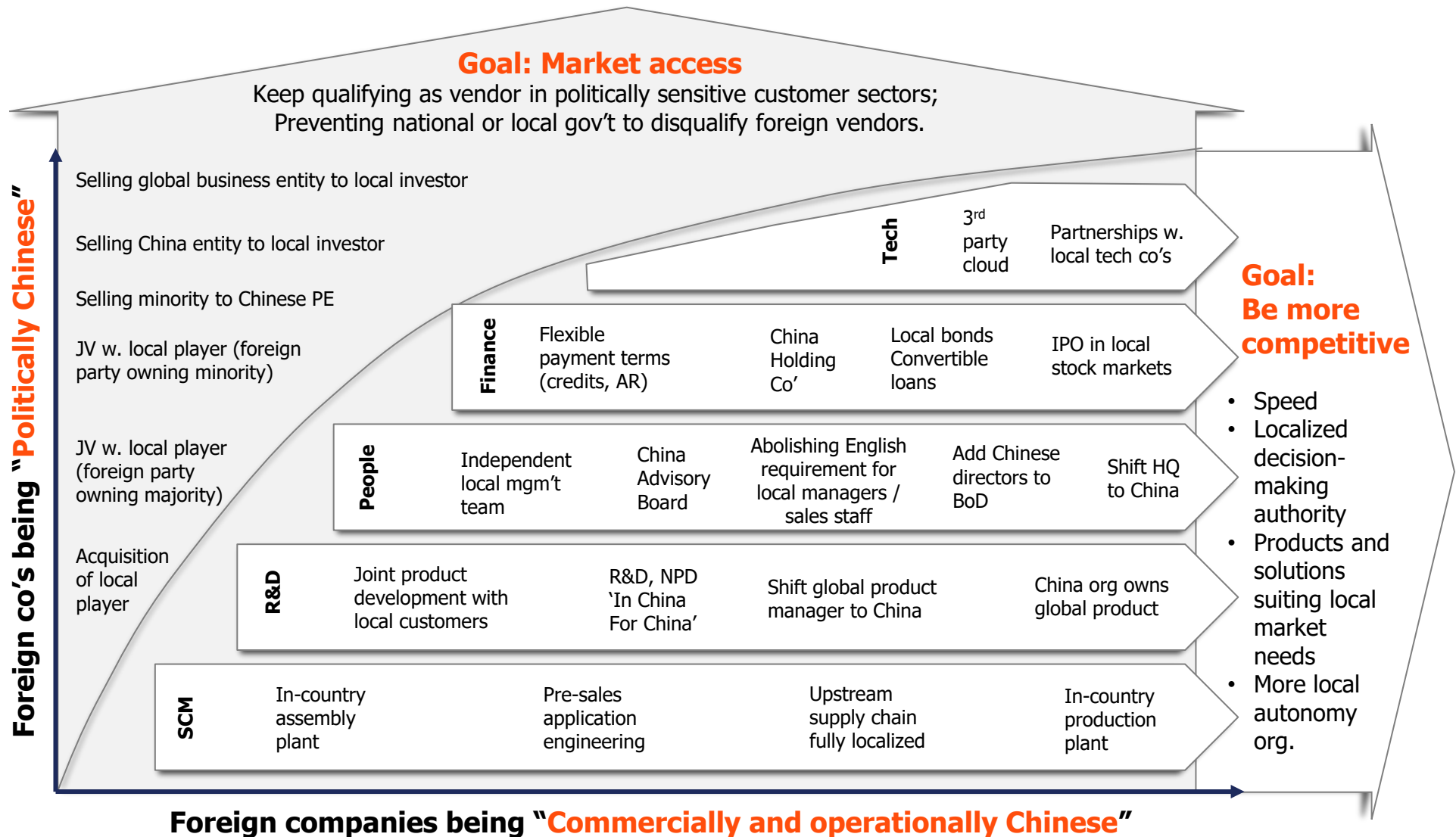
**“China for China (for all)
+ Decoupling (for some)”**

“From a MNC in China, to a Chinese with Int.

Characteristics”

3 LOCALIZATION

The **key** issue for the coming 3 years:
What does it mean to be “More Chinese”, for me?



In this context,
Inorganic growth becomes relevant

CEO Take Away

New questions on the Acquisition Playbook

Open to minority JV?

Ready to play the IPO road map?

Acquisition of Listed Co in China?

How to bring in Corporate VC?



Localization and ecosystem integration becomes a KSF in the pursuit of scale - M&A is a key tool to achieve this rapidly

Does M&A work for MNCs in China?

65% of companies had positive or very positive experiences.

19% of companies had a "neutral" experience

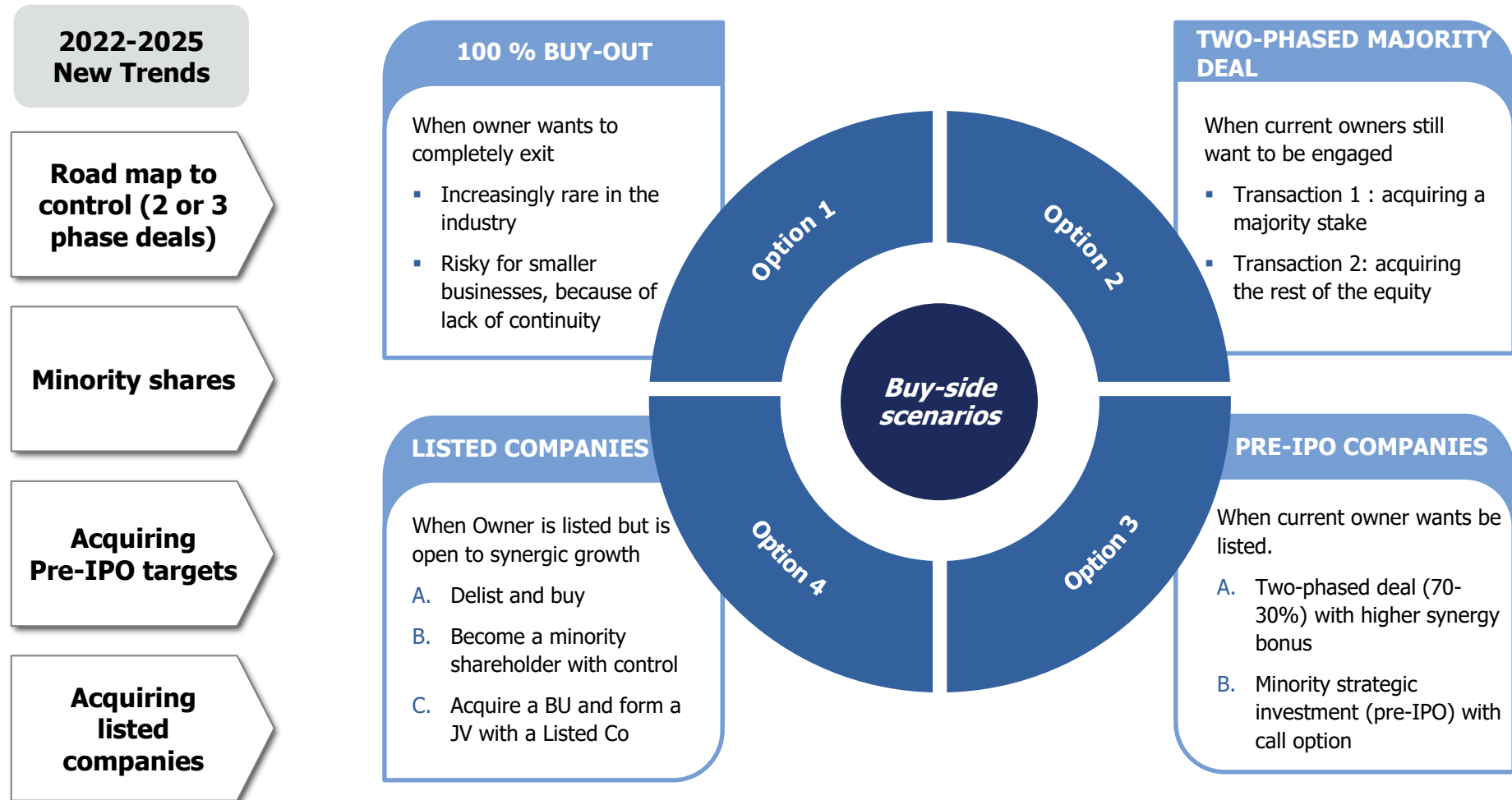
16% of companies had "bad" experiences

Is inorganic (M&A) an option for the future?

76% ..say **yes**, in order to:

- Expand market share
- Build new businesses
- Better WTM or market access
- More localized offering

A new China M&A Playbook is required: Deal structuring is becoming more innovative..



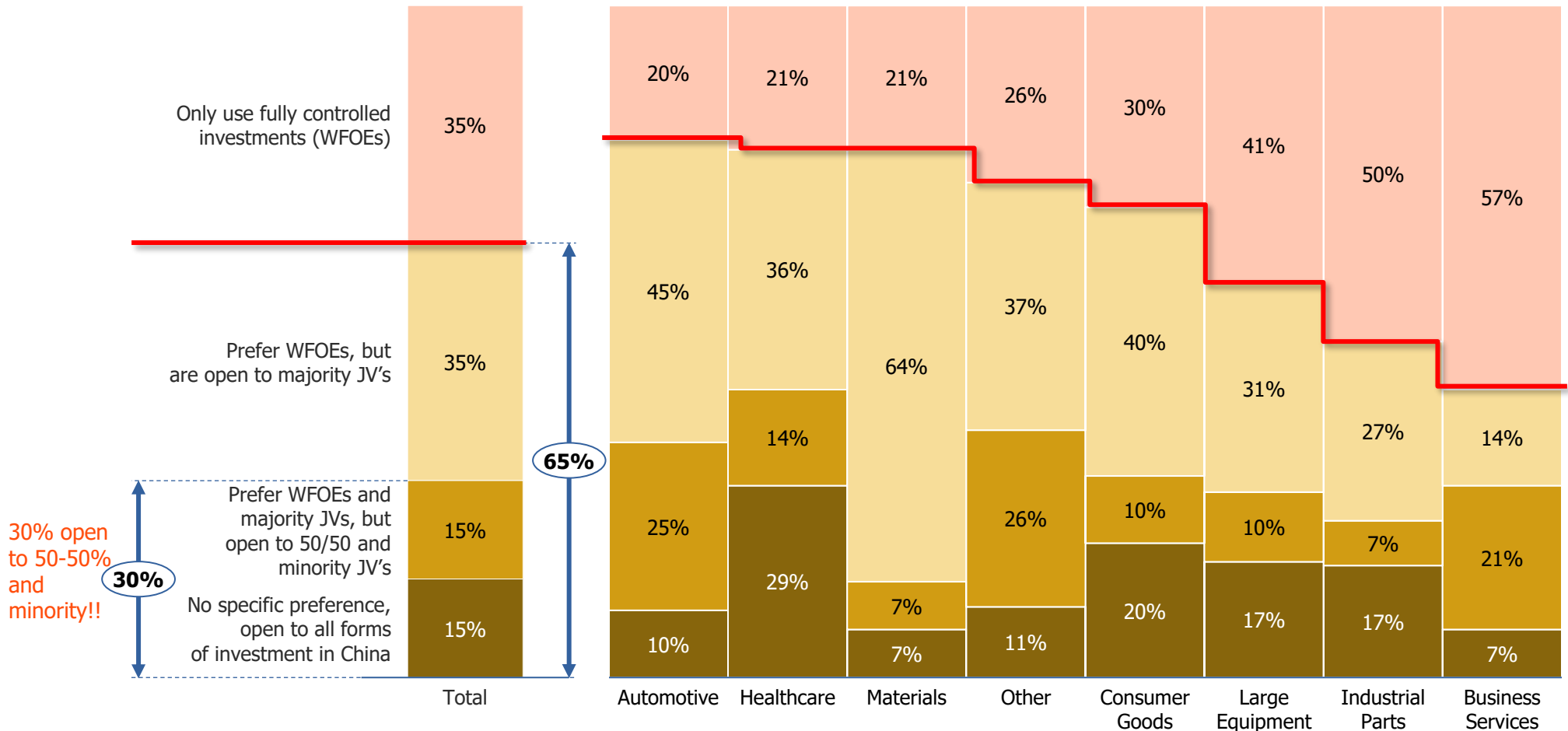
The Re-emergence of JVs: 65% of MNCs are ready to enter into partnerships (in 2018, only 25%). 30% open to 50-50 JV and minority



Equity Share: What is your approach to equity partnerships with Chinese companies?

Overall

By Sector

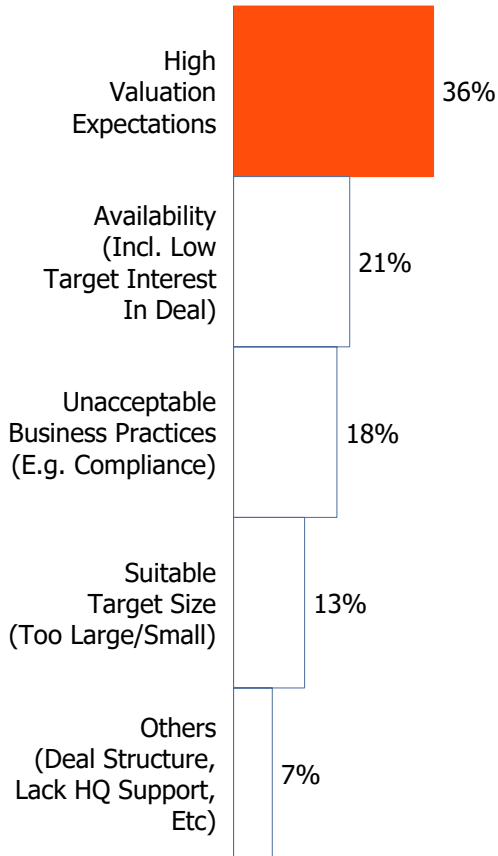




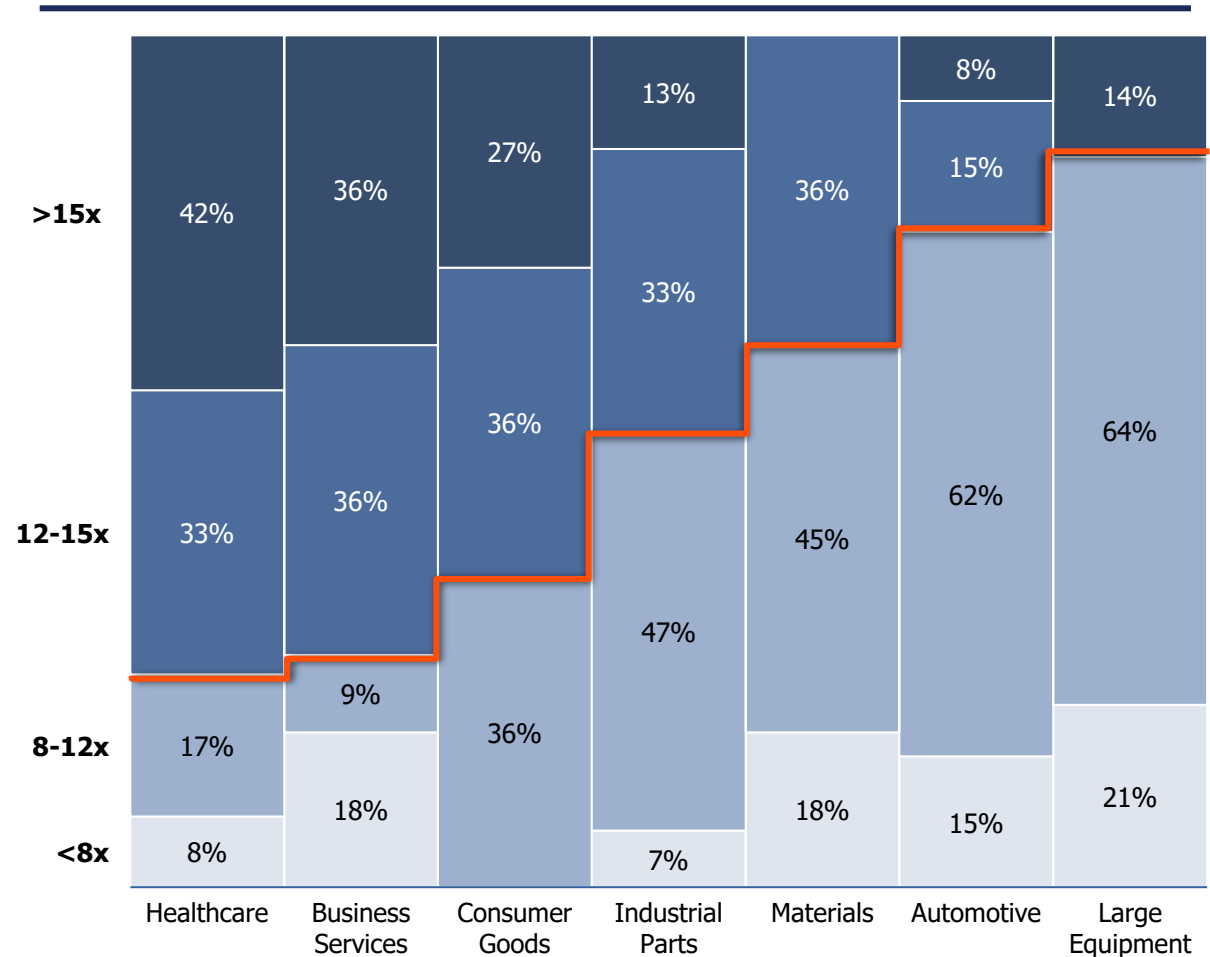
Valuation is still one of the top challenges

Multiples range from EBITDA 9-12x to >12x in many sectors

Main Deal Challenges

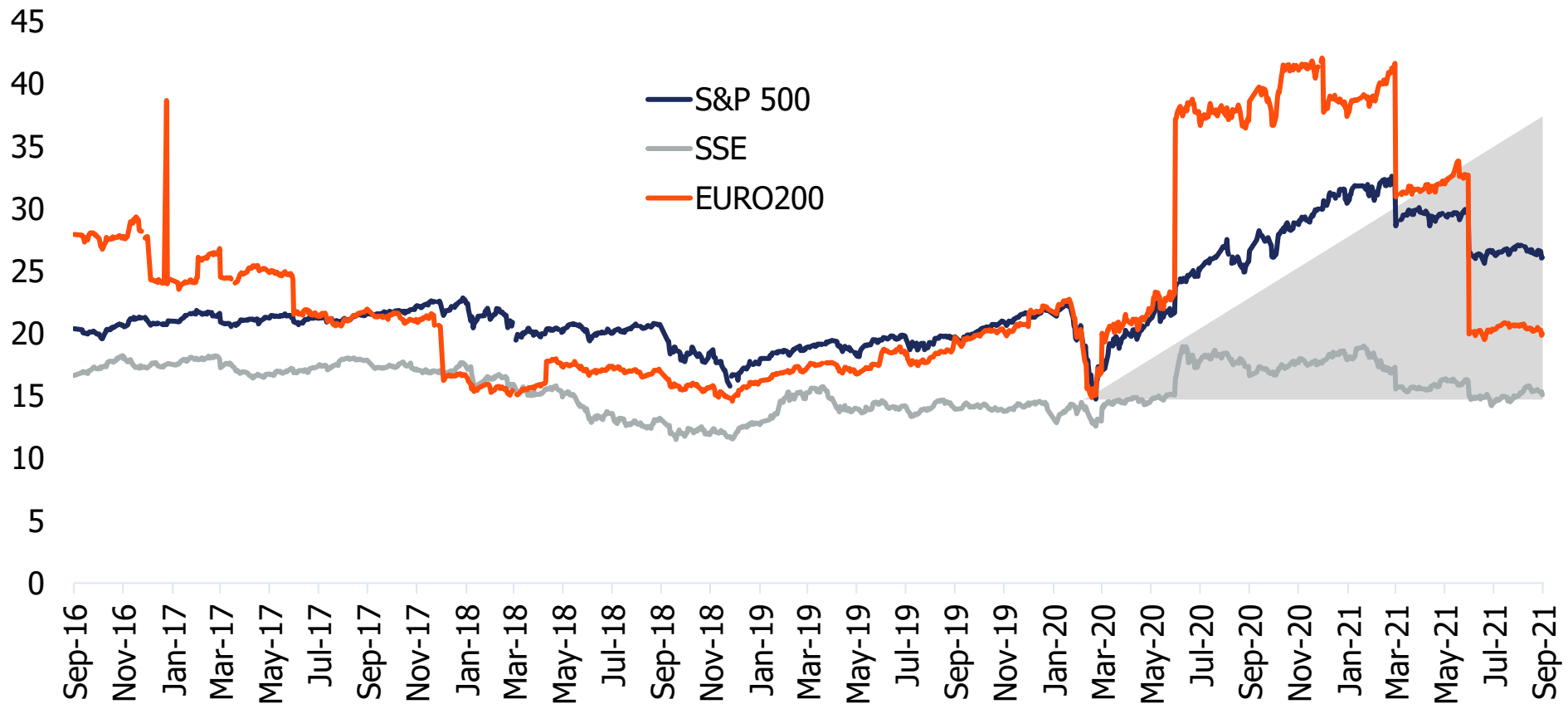


Average Valuation Multiples Estimations In Respective Sector 2021



However, the valuation of Chinese listed companies is no longer at premium - will set the tone for 2022 valuation trends

PE Ratio of S&P (US), EUR 200 (EU), and SSE (Shanghai)



Multinational Best Practices

CEO Take Away

Spend time to align global & China teams.

Bring China talent into your global Board.

Bring your Global Boards into China.

Reshape Organization Chart to achieve flexibility, speed and responsiveness in China.

Best practices that most MNCs are executing or planning for

Investment

Ad-hoc
China
investment
channel

Acquisitions:
B-brand / Local
Premium/
Platform x
growth

JV with
market access
partner

IP

Register IP
locally

Acquire local
R&D center /
team

Move from
"product" to
"service solution"

Put your global
R&D champion
into China org

Governance

Recruit Chinese
national as real
leader from
external sources

Incentivize local
leader-ship with
stock options

Make China CEO
part of global
Exco

Full China P&L
responsibility
DM authority
grid

Appoint
China Based
Talent in global
BoD

Create specific
China Advisory
Board

New governance tools: Adding China talents to global boards
(Chinese nationals or foreigners with long China experience)

Schneider
Electric

adidas



SWIRE

GOODYEAR

Samsonite

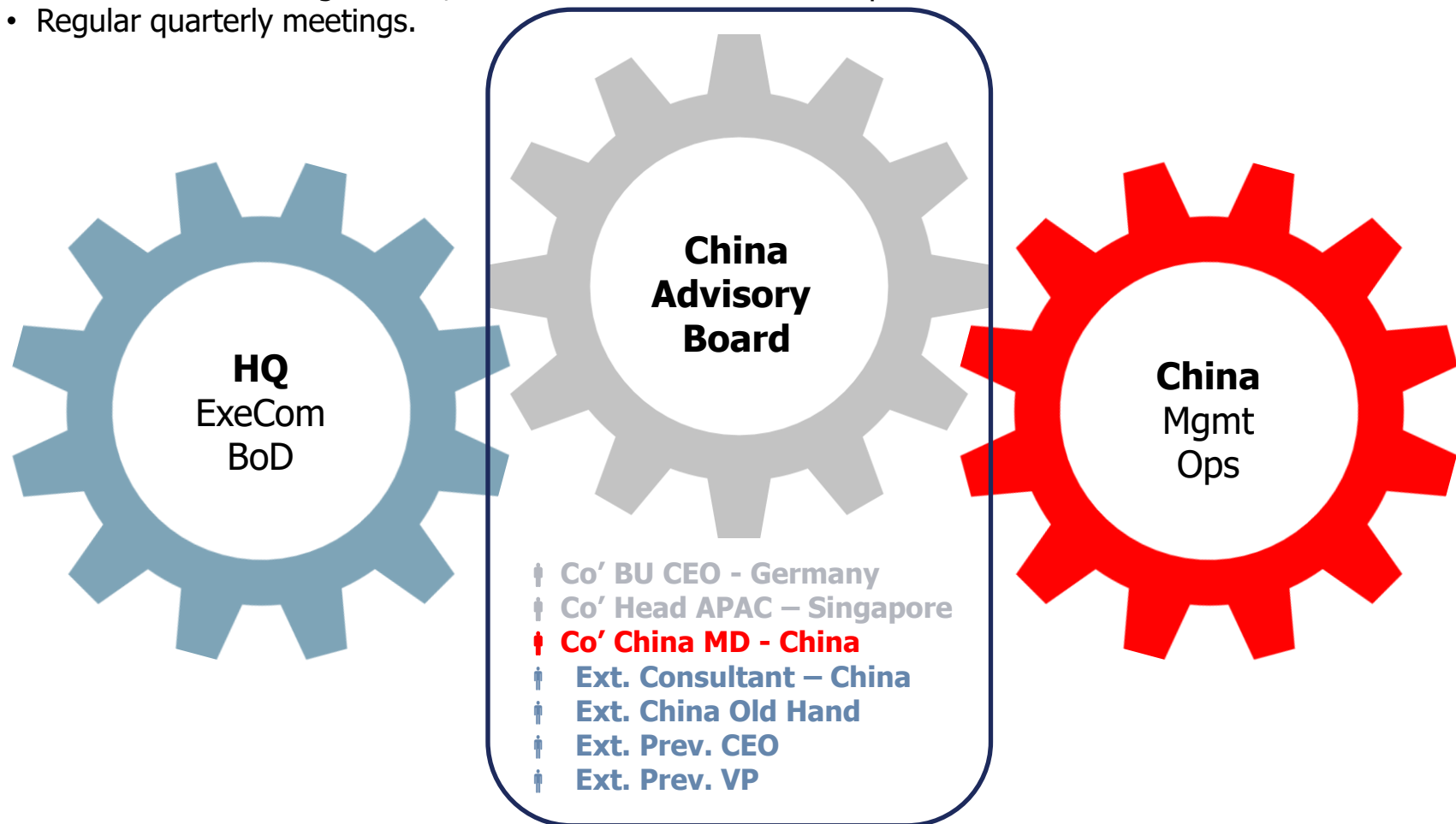
WPP

CLARIANT

Johnson
Controls

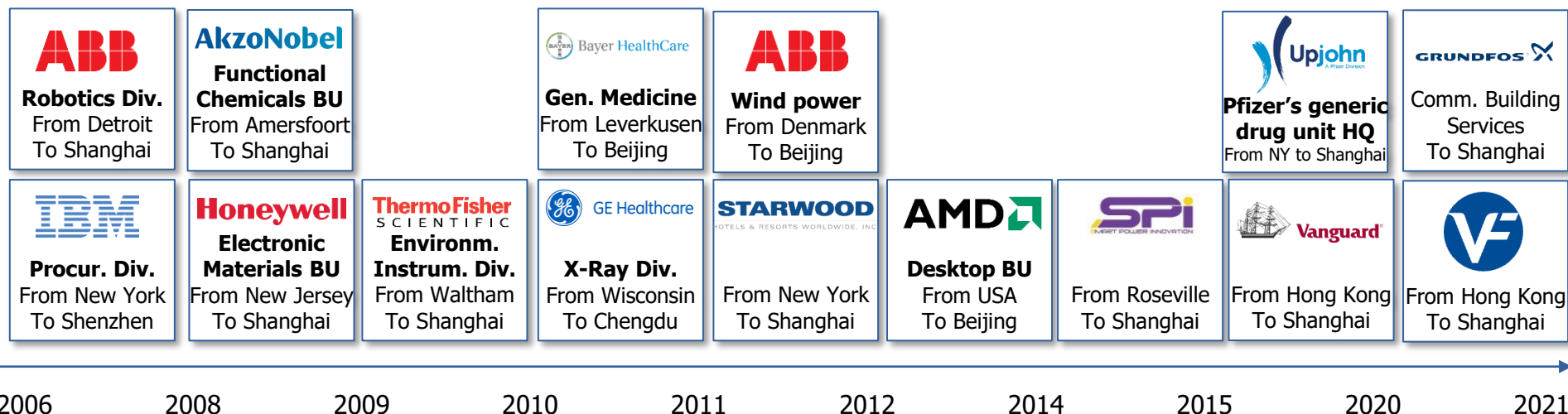
New governance tools: Creating “China Advisory Boards”

- To facilitate China growth related issues in a more focused and systematic way
- Three Mandates: 1) Bridge with HQ; 2) Sharper China Strategy; 3) Deeper Access/Network
- Board composed of both corporate representatives and external “old China hands”.
- 2 to 4 externals is a good mix, to ensure external voices are predominant.
- Regular quarterly meetings.

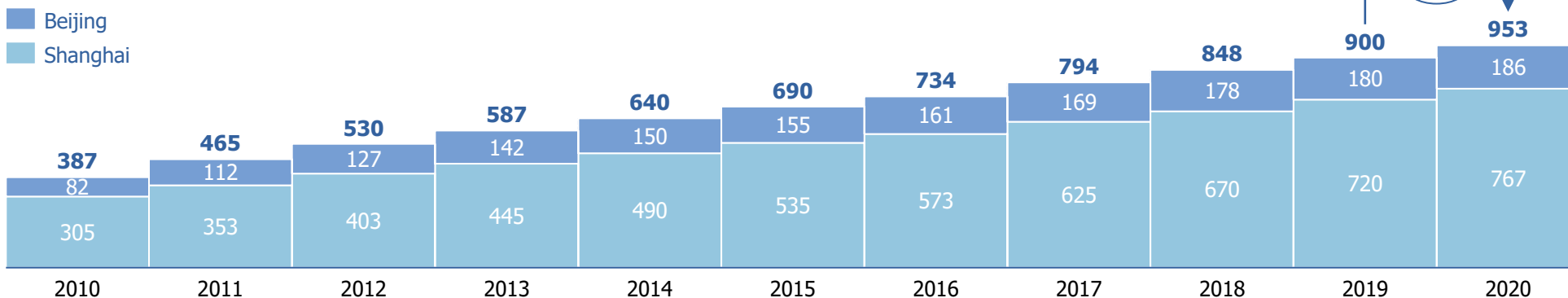


Shifting HQ gravitas to China: Relocating global, division, or APAC to China

Examples of MNC's global HQs (or, global division HQs) that shifted to China

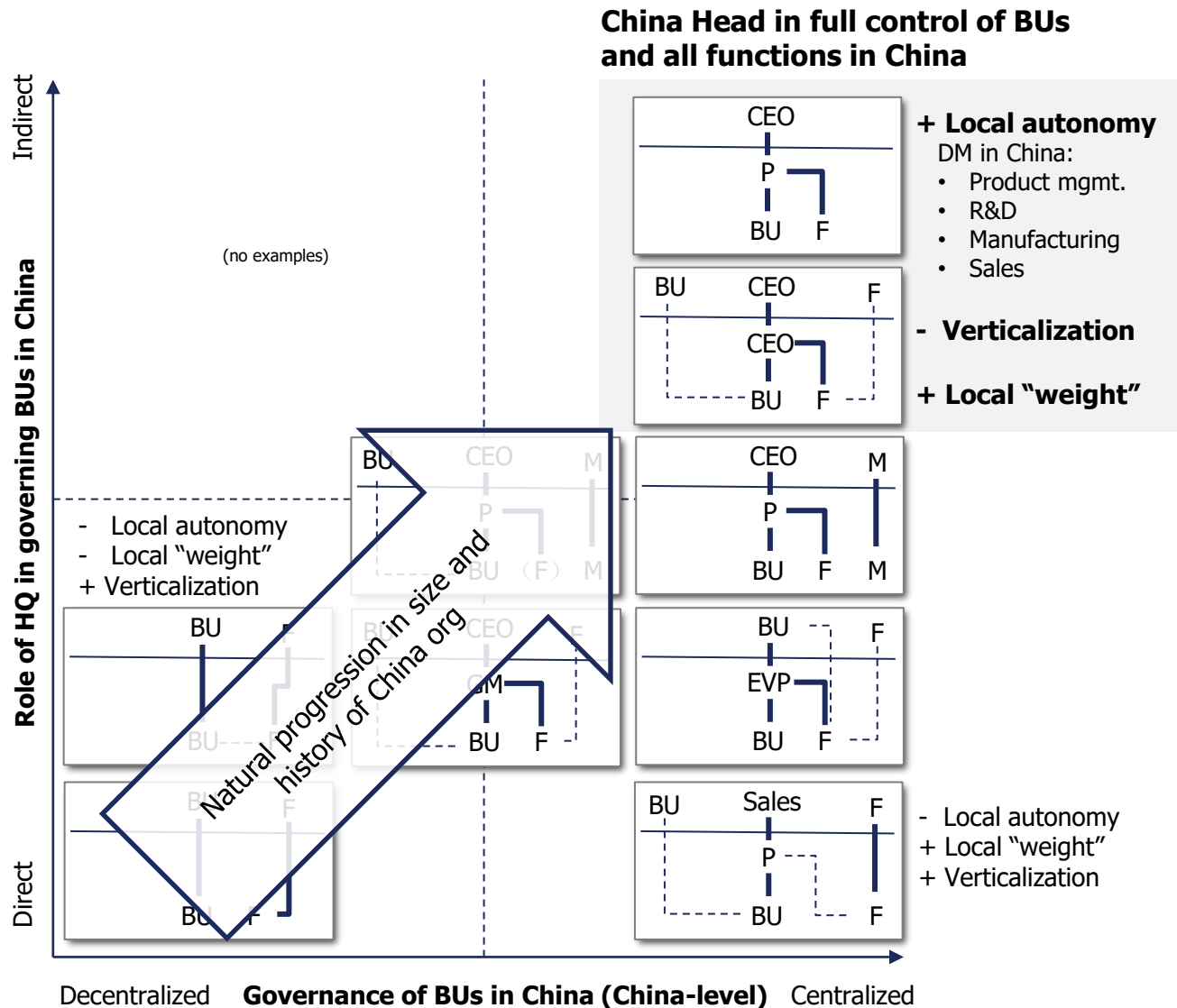


No. of totally established MNC regional HQs in China



Reshaping Corporate Reporting Lines:

A new balance btw. key stakeholders: HQ, BU and China CEO.



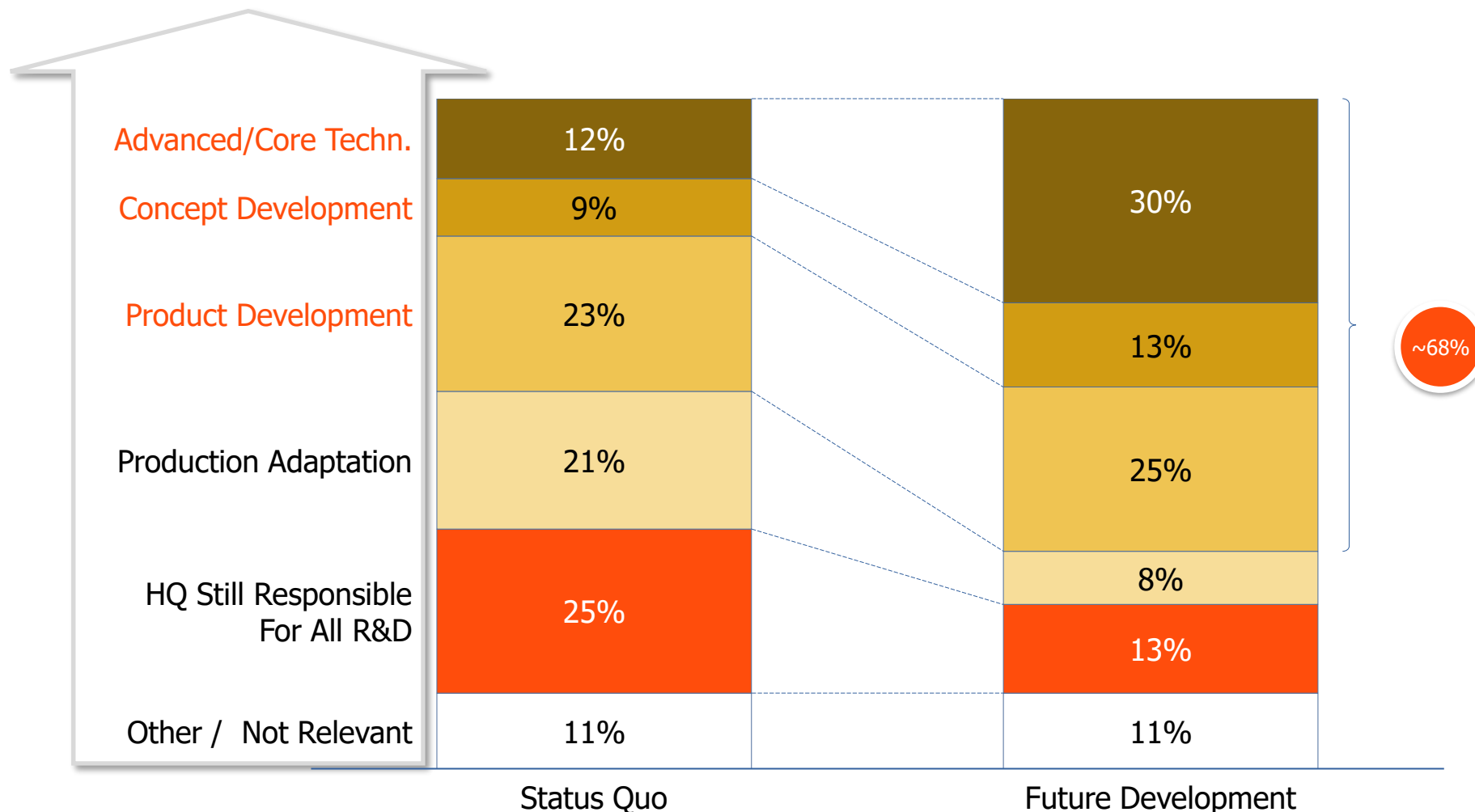
- China CEO / President part of global ExCo
- China head reporting directly to global CEO.
- More global mgm't moved to China.

"I agree with the idea that our China org should have full autonomy but not that it should be fully independent. The strength of an MNC in China is to be very local, yet also still a part of a larger group".

Revamp from an **innovation perspective**, MNCs are already reacting – only few will remain reliant on HQ-driven R&D



How advanced will your R&D activities in China be?



Conclusion & CEO Agenda 2022

CEO Agenda 2022

1

Where does the “New China” stand in my global strategy?

(Market and competitors - source of innovation? Partner for global growth?)

2

What does it mean “to be Chinese” for my company?

Do I need to **decouple**, or should we focus on normal business **localization**?

3

Am I fully capturing the Chinese innovation boom?

Do we **understand the New Chinese Ecosystems**? Can we be part of it?

4

What is the **role of inorganic growth for us**?

Should I consider **alternative models** such as minority participation, listed co's, corporate VC?

5

How can I achieve **alignment btw. HQ and China** teams?

What **governance model** allows us to be close to China, but still retain our corporate DNA?

It has never been more pressing than now
to have a clear alignment between HQ and China teams

Remember: None of your Chinese
competitors are facing this challenge

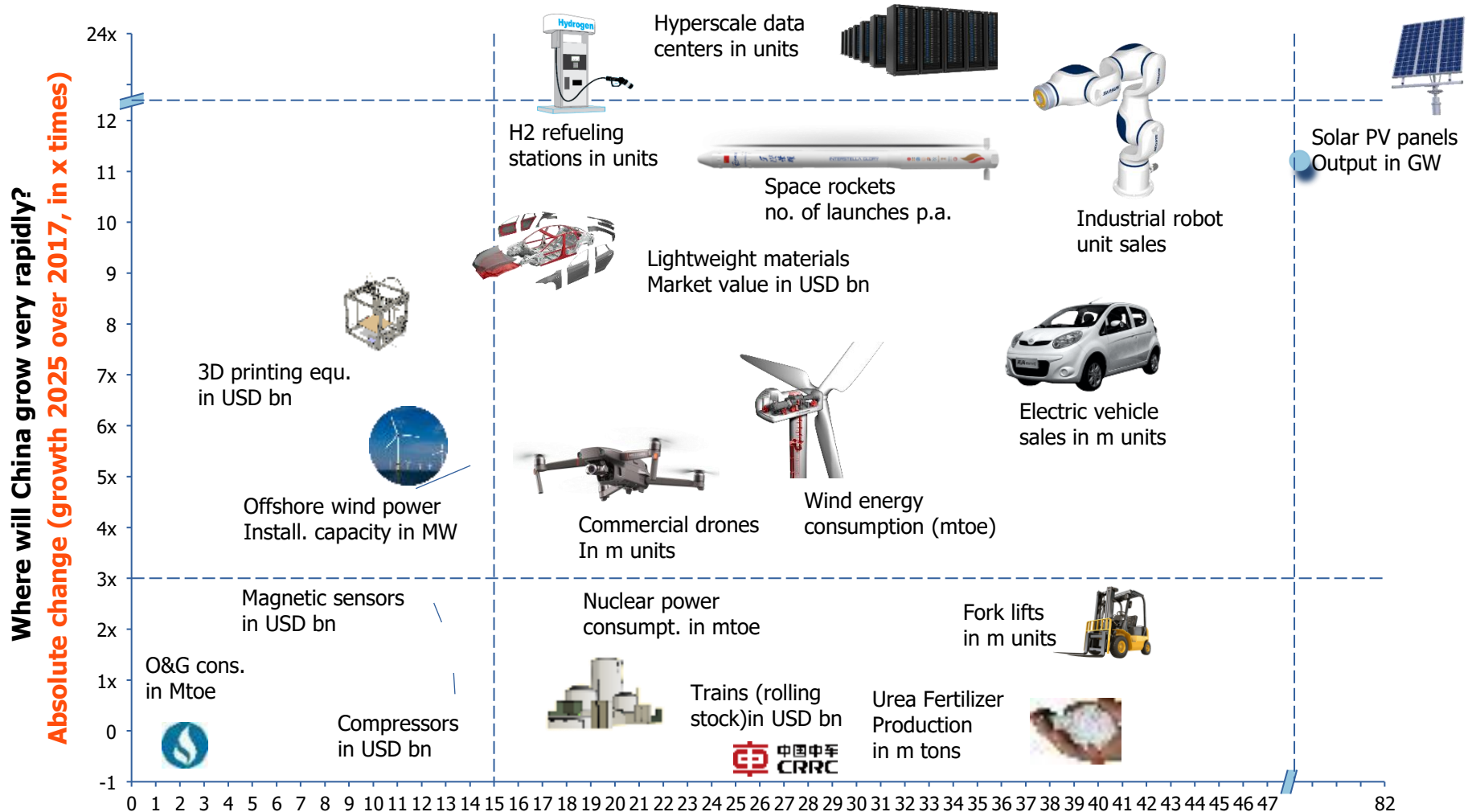
BU Matrix **HQ** Global Division



Food for Thought...What's coming in the next 3 years?

The new Chinese industrial global leadership

China's future global relevance vs China's future absolute growth (2017 – 2025)



Contact Us

Reach out to us to learn more about our experience and capabilities

Corporate Finance

Barry Chen

Partner in Charge, Head of Corporate Finance

T: +86 (21) 6341 0699

E: Barry.Chen@InterChinaPartners.com



Shanghai

Eduardo Morcillo

Managing Partner, Head of Shanghai

T: +86 (21) 6341 0699

E: Eduardo.Morcillo@InterChinaPartners.com

Suite 1201, 100 Bund Square, 100 South Zhongshan Road
Huangpu District, Shanghai 200010
P.R. China



Hong Kong

Kent Ng

Partner, Head of Divestment Advisory

T: +852 28248324

E: Kent.Ng@InterChinaPartners.com

66/F, The Center, 99 Queen's Road
Central, Hong Kong
P.R. China

Follow us for more information



www.InterChinaPartners.com



Beijing

Jan Borgonjon

President

T: +86 (10) 8451 2088

E: Jan.Borgonjon@InterChinaPartners.com

Suite 1106, Golden Land Building, 32 Liangmaqiao Road
Chaoyang District, Beijing 100016
P.R. China