



Impact of the BRIICS on International Markets Focus on China

Joerg Wuttke

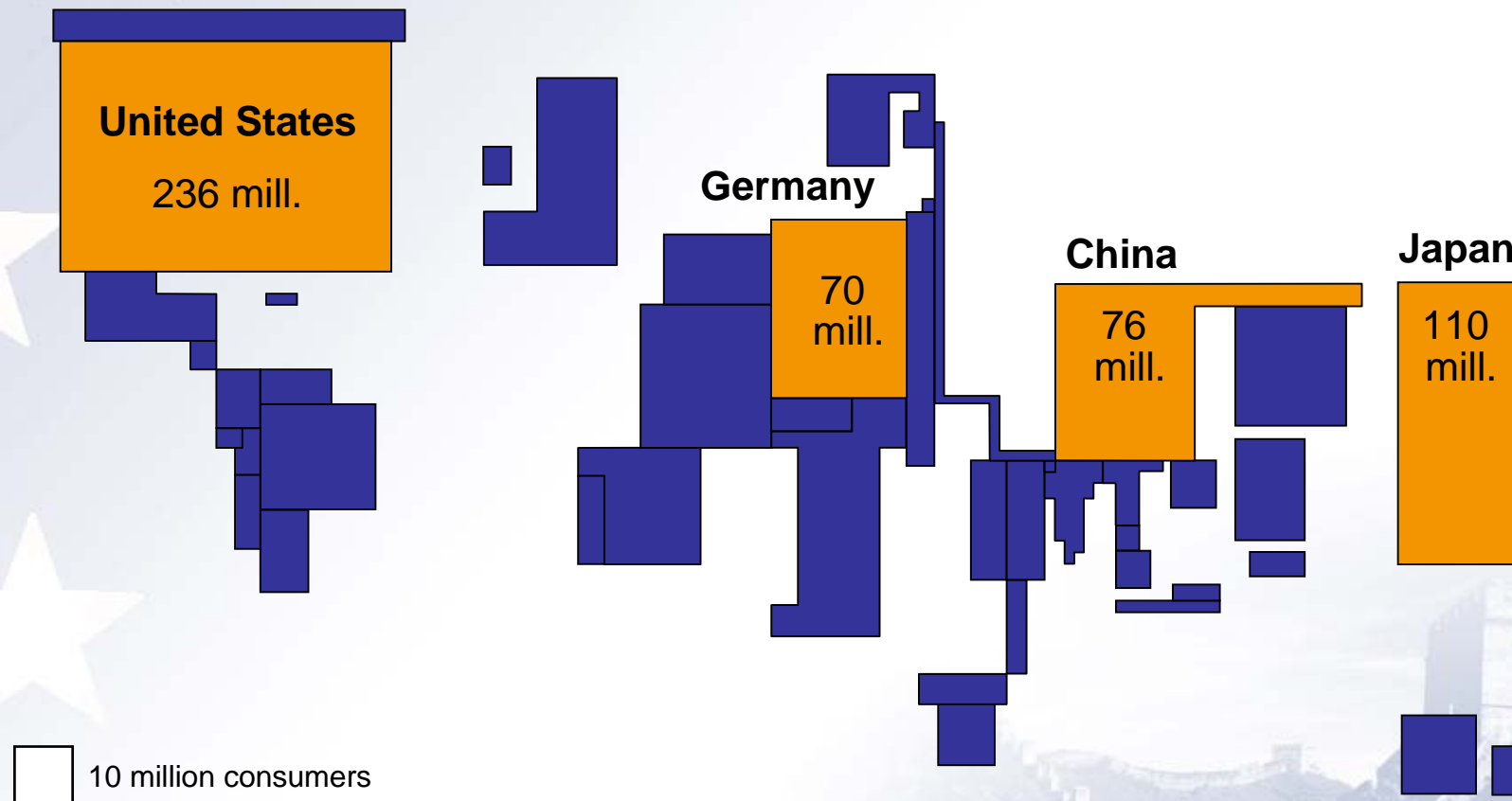
**President, European Union Chamber of Commerce in China
and**

BASF China Chief Representative

Paris, June 25th 2008



Consumers of Chemical Products* in 2001



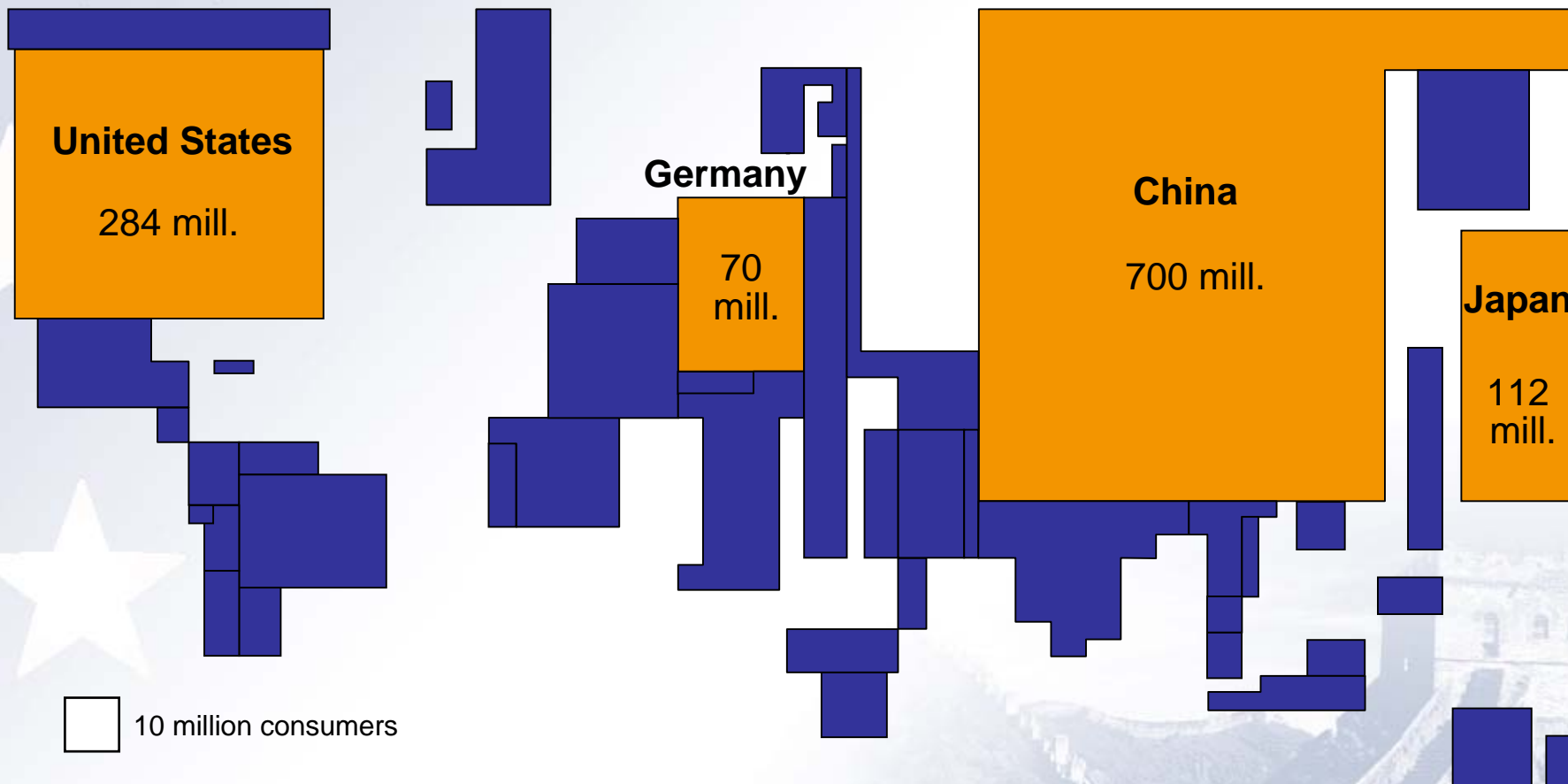
2001 = 1.1 billion consumers (17% world population)

Source: World Bank, EIU, US Census Bureau

* A potential consumer of chemical products is defined by an annual income of 10,000 USD in purchasing power parity



Consumers of Chemical Products* in 2020



2020 = 2.0 billion consumers (29% world population)

Source: World Bank, EIU, US Census Bureau

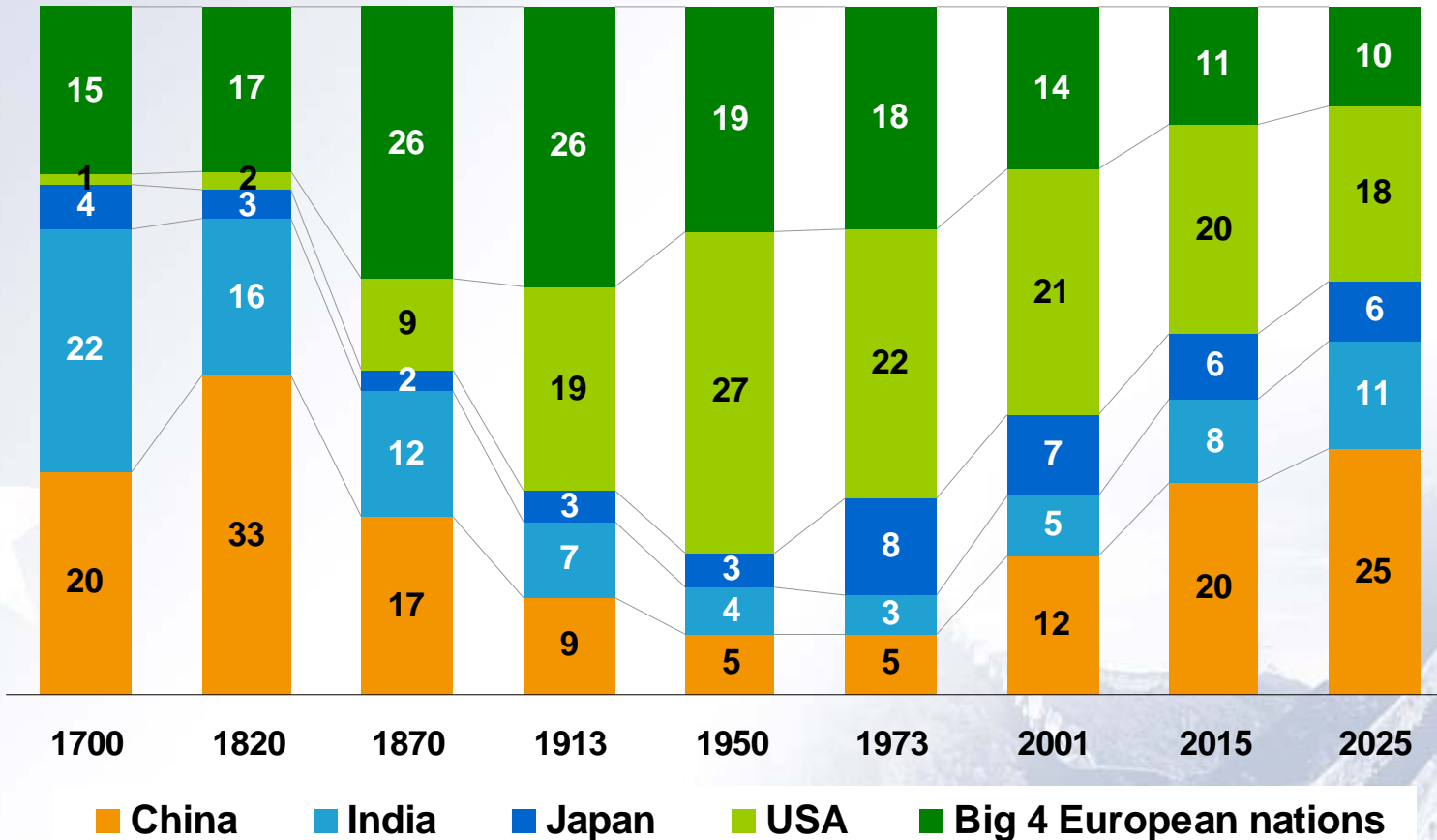
* A potential consumer of chemical products is defined by an annual income of 10,000 USD in purchasing power parity



Comeback of China

GDP growth 1700 - 2025

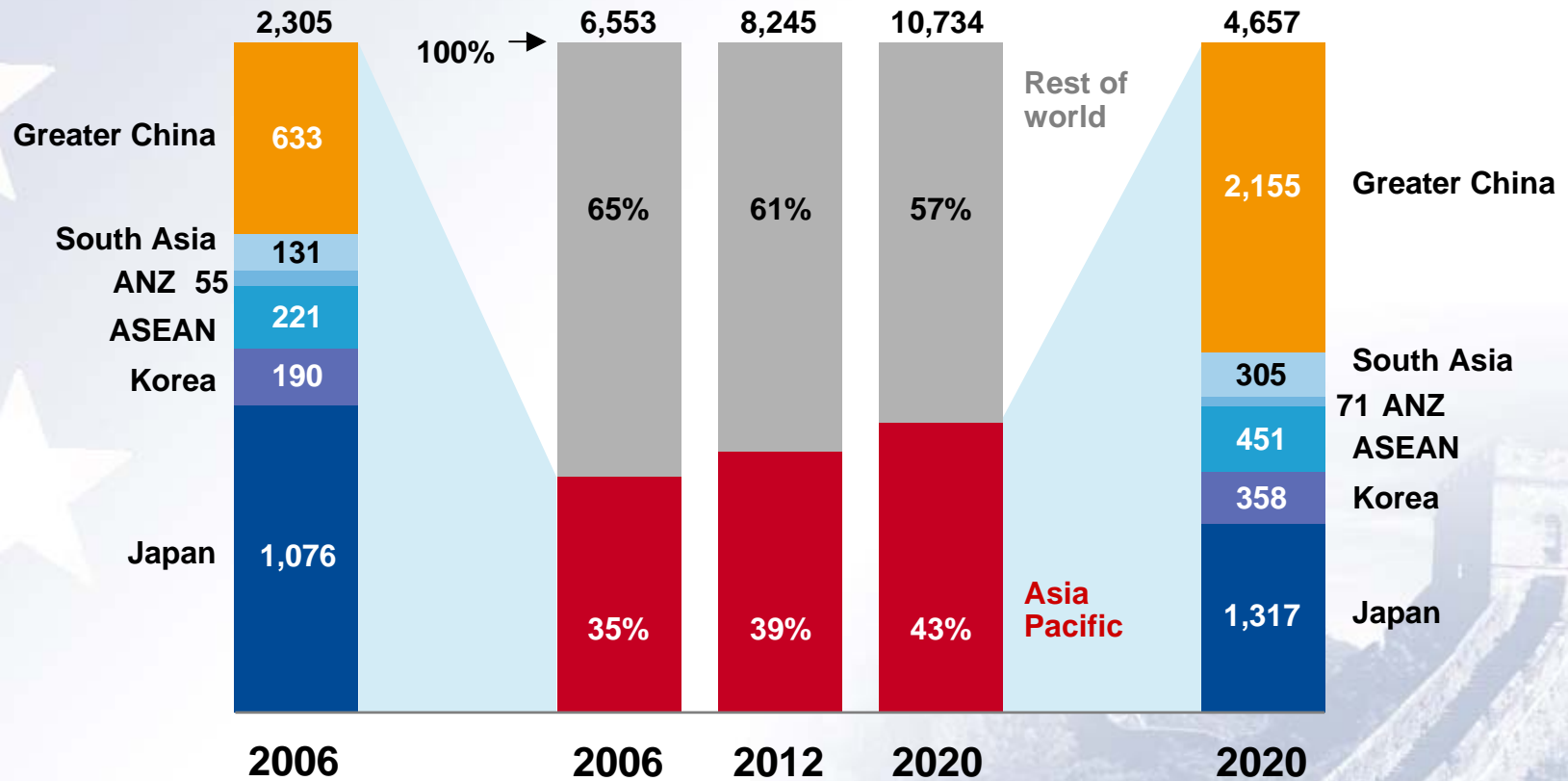
% of world GDP
at purchasing power parity





Asia Pacific will become the world's leading manufacturing hub by 2020

Industrial production (in billion USD)



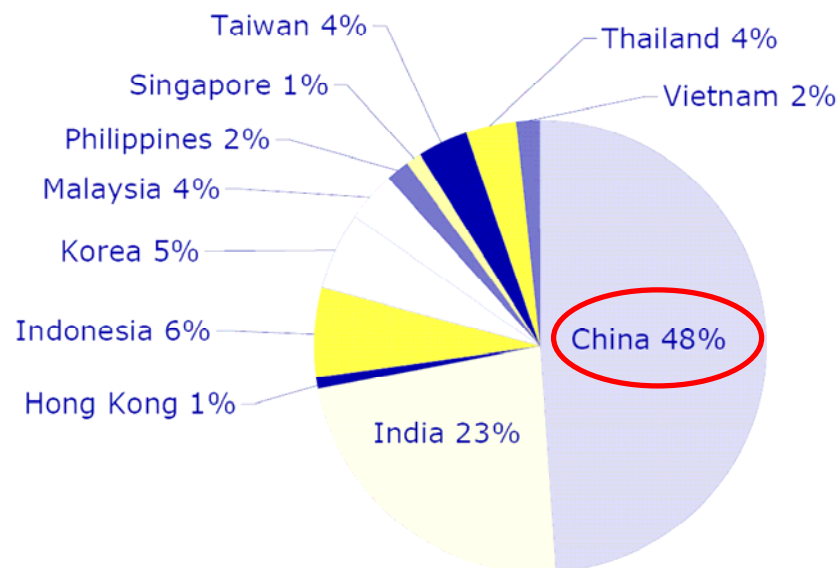


THE SCALE OF URBANIZATION IS UNPRECEDENTED...

- In the last 17 years **156 cities more than doubled** their population ...
 - ... and **32 of those have now more than 6 times the population** they had in 1990
- Over the next 18 years, Chinese cities will add **more than 320 million** people ...
 - ... more than the **population of the entire United States**
- There will be **more than 220 Chinese cities by 2025** with more than a million inhabitants
 - ... in **Europe** today there are only **35 cities** of that size.
- By 2025, **two-thirds (926m urban)** of China's citizens will **live in cities** ...
 - ... **that's nearly one billion people.**



Infrastructure spending by country (ex-Japan, ex-Middle East), 2008-12



Infrastructure spending for the region is expected to cross US\$3tn over the next five years - approximately double the growth in spending in the previous five-year period.

China will account for US\$1.2tn, the Middle East US\$750 billion and India approximately US\$500bn. China and India together make up 70% of Asian infrastructure spending (ex-Middle East and Japan).

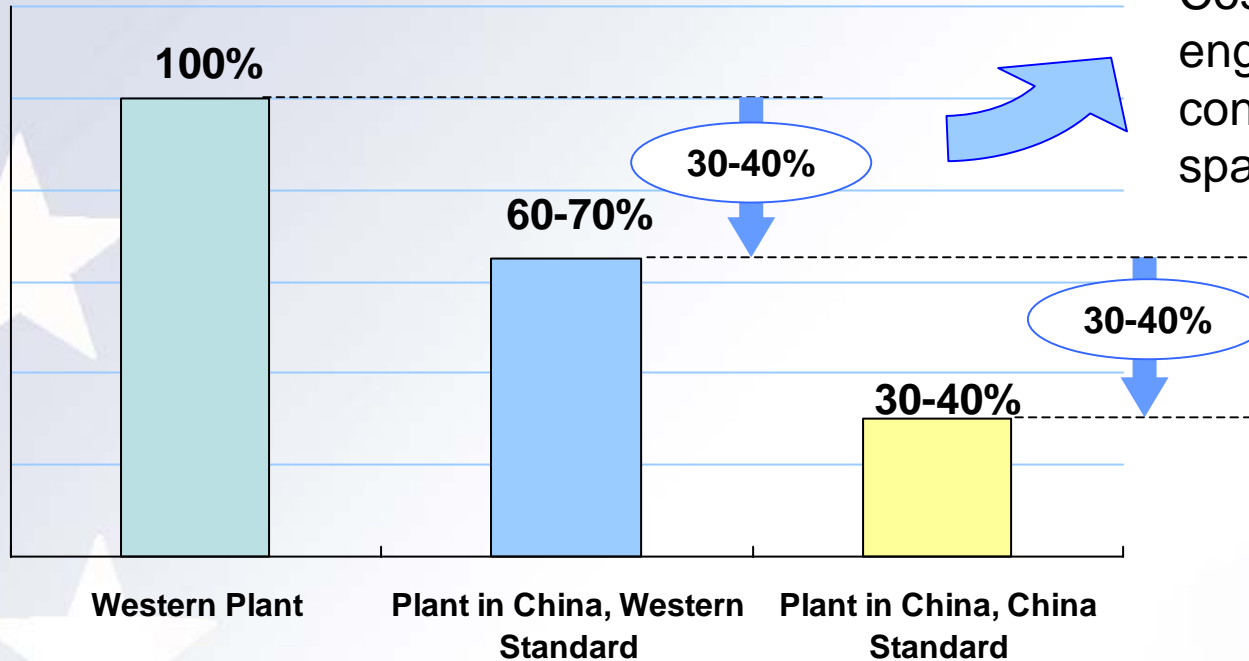
CLSA estimate growth in overall infrastructure spending over the next three years at approximately 50%, or a 15% Cagr.

Source: CLSA 2008



China builds plants cheaper than the West:

Plant investment cost in China



Cost savings in equipment, engineering, design, construction, piping and spare parts

- More pragmatic plant setup, configuration, instrumentation
- Substitution of capital by cheap labour



Environment: Sustainable Development?

- Cost of environmental degradations 5 to 7 % of GDP per year
- Only 40% of industrial waste water is recycled (OECD 80%)
- 70 % of China's largest rivers are severely polluted
- 300m people drink polluted water, 400 cities face water shortages
- Life expectancy in urban areas has declined in the past decades
- 7 of the world's 10 most polluted cities are in China

Consequence:

Health problems & strain on health system, growth impact in long run





Environmental challenges how to avoid disaster..

Situation:

- The elevation of SEPA to the Ministry of Environment Protection is a clear gesture of environmental policy execution.

Action by Chinese Authorities:

- Premier Wen promised to further reduce emissions, conserve energy and cut pollutions.
- Shut down backward production facilities in heavily polluting industries such as electricity, coal and steel.
- Redundant projects in energy- or pollution intensive industries will be barred.
- Urban sewage treatment ratio shall achieve 100% in 36 large cities within two years.



Environmental challenges how to avoid disaster..

- In 2007, the government announced a new system for measuring performance, which ties career advancement to success in achieving environmental targets.
- Promoted insurance for polluters and help expedite compensation for victims.
- Implemented green credit policy, yet it still falls far behind expectations
- From 1995 to 2005, only two projects that SEPA did not approve.
- In 2006, SEPA rejected about 110 of the projects submitted.
- In first nine months of 2007 it rejected 187 in spending that now won't happen. SEPA is now rejecting nearly 30% of the projects that submit an environmental-impact assessment.



Unemployment or Labor shortage?

Situation:

- The underlying unemployment rate in China's cities is probably 8%.
- Factories in coastal regions reported difficulties in hiring new workers and expanding capacity.
- Yet, China still has close to 200m excess working-age rural population.

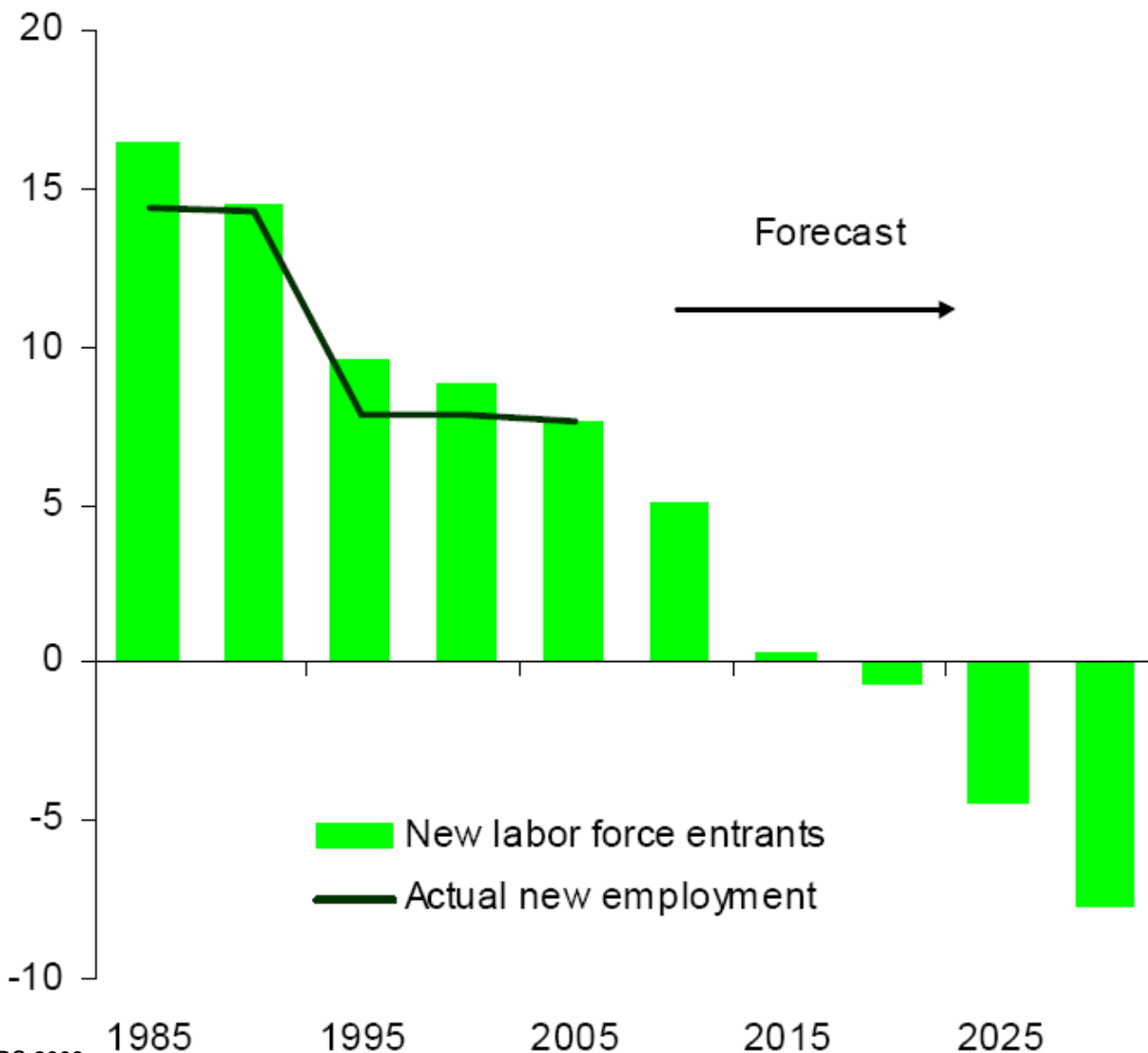
Outlook:

- Rising wages in 2008 and beyond.
- Projected growth of the labor force for the next 20 years: the mainland will still see some 5m entrants a year through 2010,
- After that the labor force starts to flatten ... and then fall after 2020 (One Child Policy Impact)

China created massive employment but faces a Labor shortage after 2020



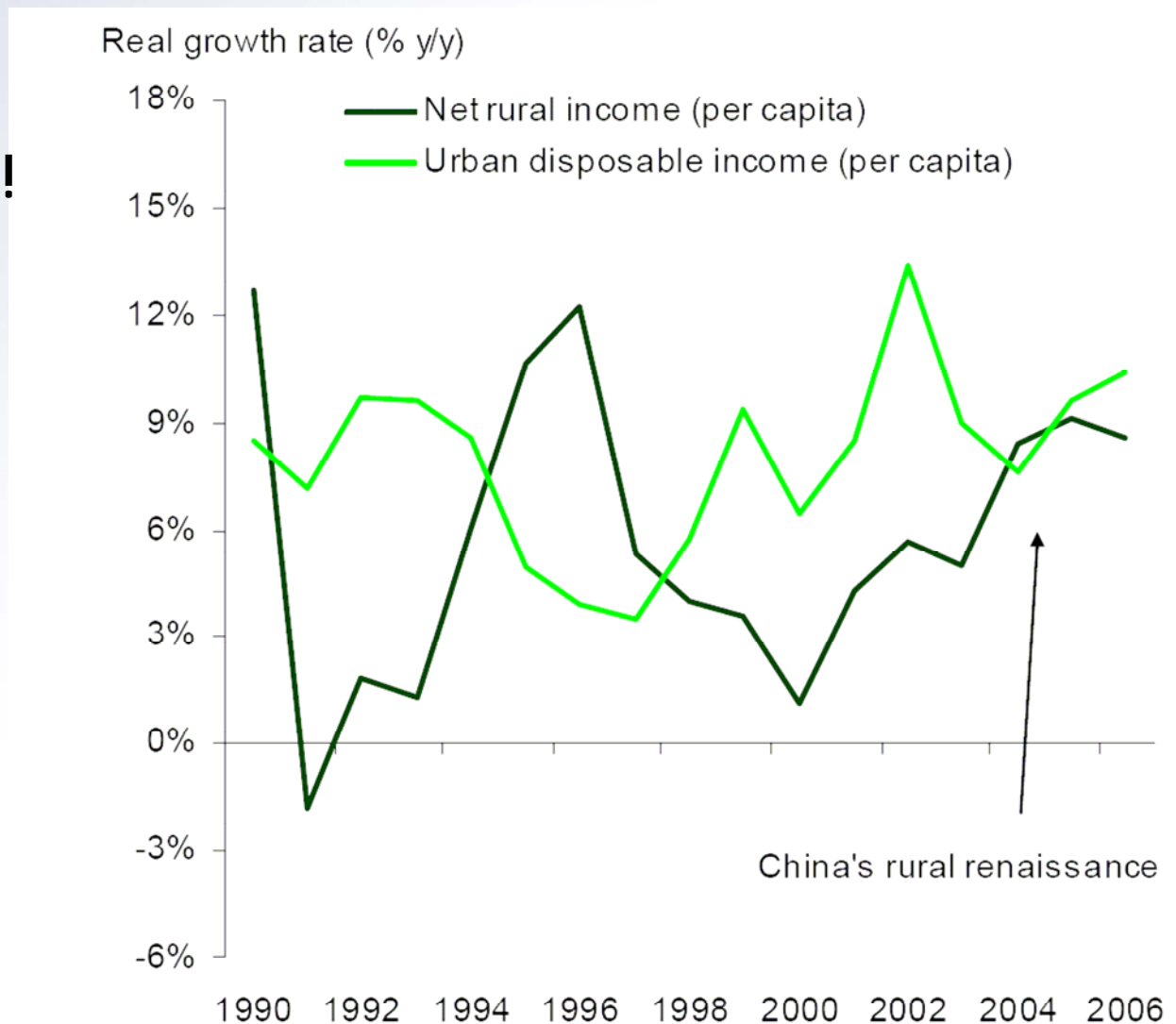
Million persons (annual average)





A (more) Harmonious Society

Rising rural wages !!





Business Growth Excellent in 2007

- Two-way trade between EU and China exceeded € 302bn in 2007, an increase of 17% from € 258bn
- **EU to China: € 72bn (+12%)** despite **depreciating** RMB vs € 16% since 2006 (RMB appreciated 12% vs USD since 2006)
- Europe is very competitive, exports more to Switzerland and Russia than China
- China share of total 2007 EU exports still small: 5.8% (USA 6.2%)
- EU exports to China as a share of EU GDP: 0.7% (USA 0.5%)
- **China to EU: € 230bn (+18%)** (20% of total China's exports!!)
- Trade imbalance: € 160bn , or € 18m a hour

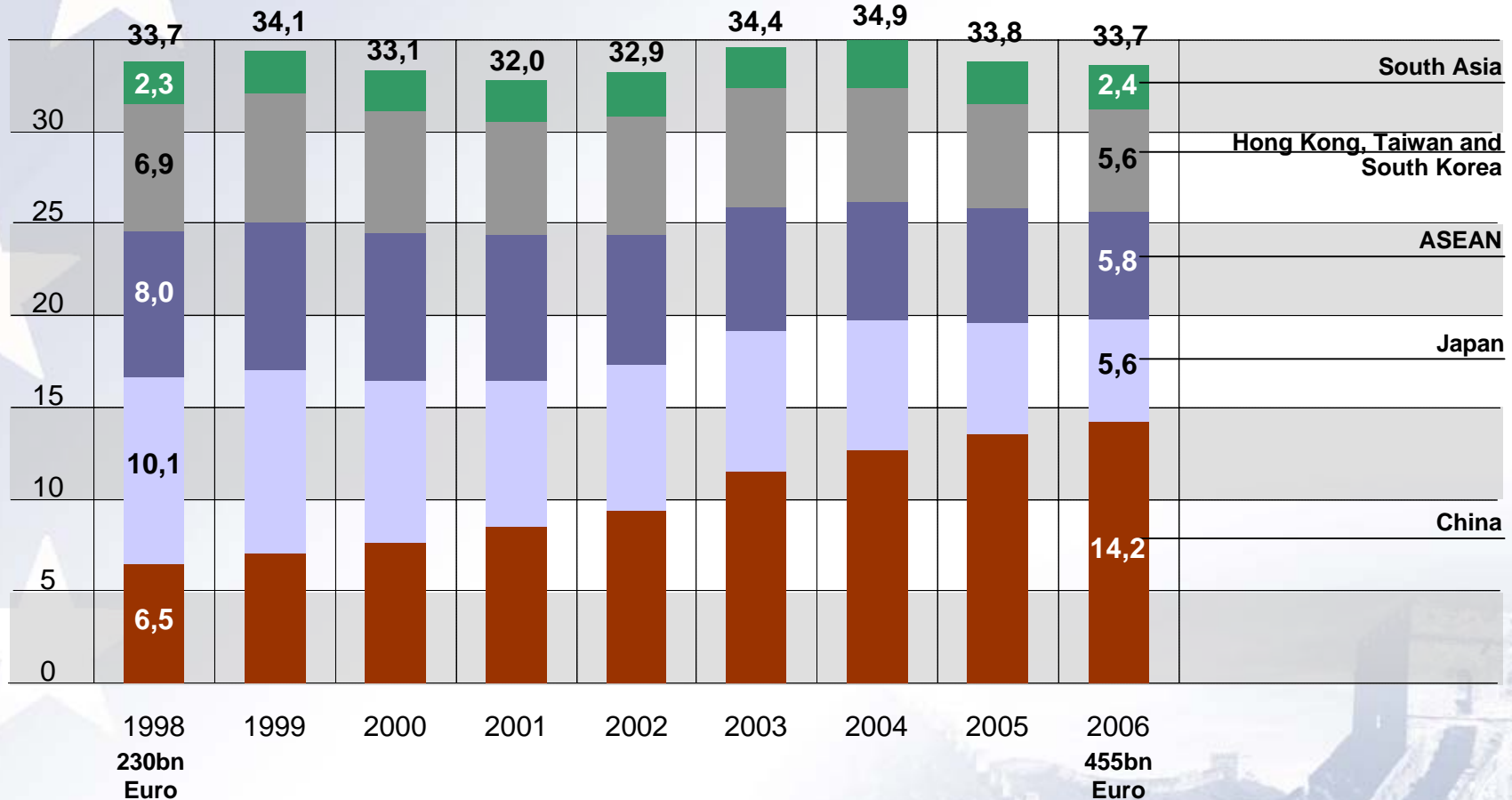


A Balanced Development Strategy Is Needed

- Overall, neither the European nor the Chinese economy is best served by protectionist measures
- The current trade imbalance is economically unsustainable for China and politically unsustainable in Europe.
- Chinese exports partly due to overcapacities and subsidies



Share of EU Imports from Asia 1998-2006



EU trade deficit with China grew from 54.7bn Euro in 2002 to 160bn Euro in 2007

Source: EU Commission



Trade imbalance vs. level playing field

- Study into the Future Opportunities and Challenges in EU-China Trade and Investment Relations 2006-2010
- There is also a growing perception in Europe that China and Europe do not trade on genuinely reciprocal, equal, terms; that China does not always trade fairly.
- This study shows that Chinese non-tariff barriers cost EU operators in **2006 no less than €21.4 billion a year** in lost business opportunities.
- We need to act to reap those benefits, not close the trade imbalance.



EUROPEAN CHAMBER



中国欧盟商会

Will China eat up the World?



Source: CLSA 2005

www.europeanchamber.com.cn



Made in China: Who Really Profits

A Chinese factory sells leather work boots for \$15.3 a pair, earning a profit of \$0.65.

The U.S. retailer sells them for \$ 49.99 a pair and expects a profit of \$3.46.

U.S. RETAILER

CHINESE FACTORY

Store profit before interest and taxes \$3.46

Factory profit before interest and taxes \$0.65



Retail costs based on industry averages for U.S. retail stores.

Sources: Forsan (factory and shipping costs), Kurt Salmon Associates (U.S. retailer costs) 2006



Electronics products

Windows-style laptops around \$1,000 in the United States

Retailer keeping less than \$50.

Where does the money go?

Intel and Microsoft together would collect about \$300

Makers of the display screen, the disk-storage devices, and other electronic components get \$150 apiece.

The keyboard makers \$15 or \$20.

FedEx or UPS \$10 or \$15.

Perhaps \$30 to \$40 — 3% to 4% of the total—would stay in China with the factory owners and the young women on the assembly lines.



10% to 20% remain in China....

A carrying case for an audio device retails for just under \$30

Where does the money go?

Chinese supplier \$6 per case, of which about half goes for materials.
The other \$24 stays with the big-name company.

An earphone-like accessory for audio device retails for about \$30.

Where does the money go?

\$3 stayed in China.

High-end Ethernet connecting cables retail prices are \$29.95 for the specialty brand, \$19.95 in the chain store, and \$15.95 on eBay. (Identical cables!)

Where does the money go?

The Shenzhen-area company that makes them gets \$2 apiece.

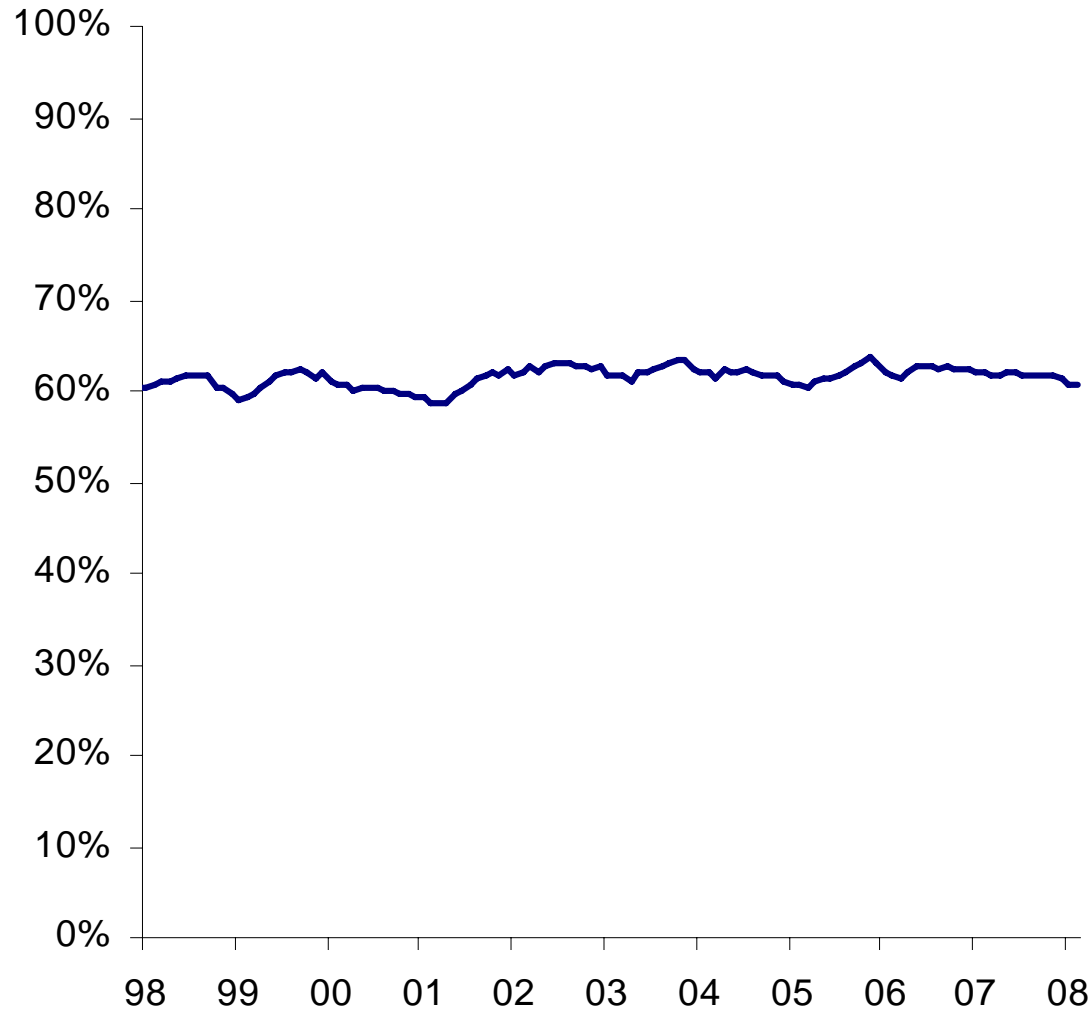
No competitive disaster

EUROPEAN CHAMBER



中国欧盟商会

Coastal share of total exports (3mma, %)



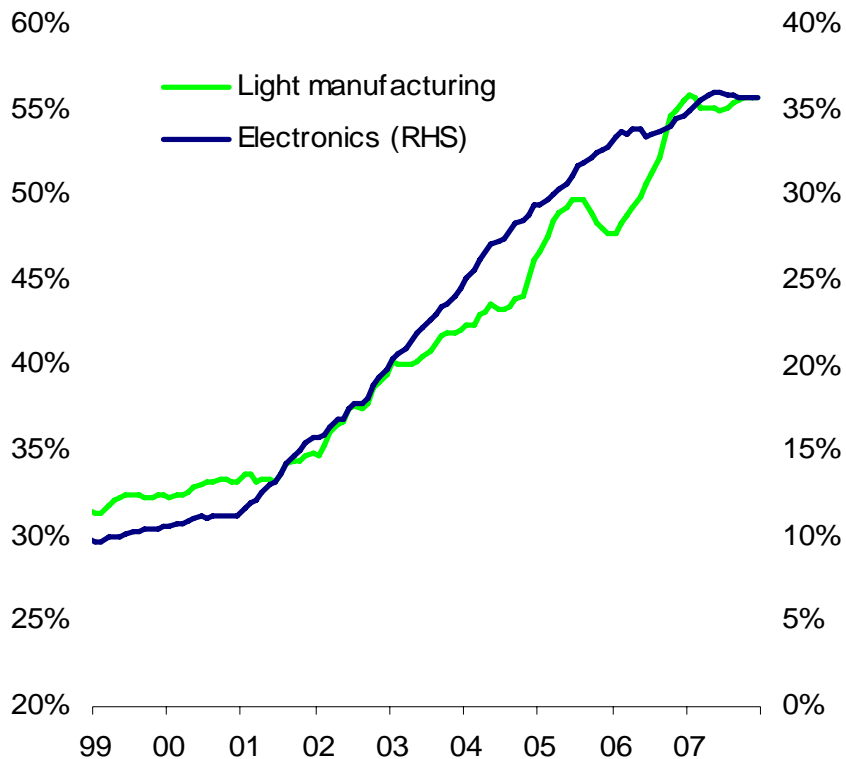
Source: CEIC, UBS estimates



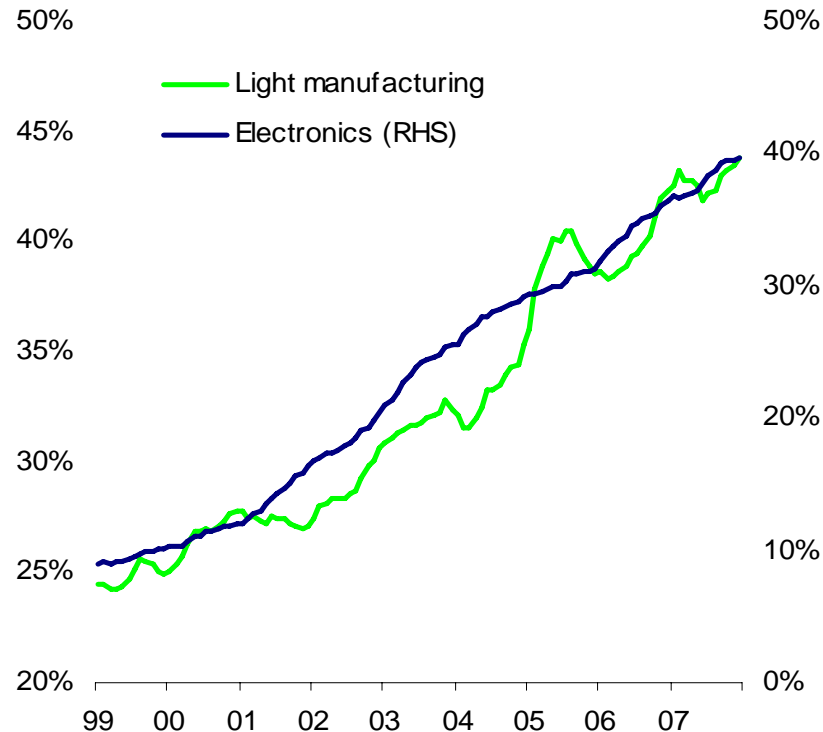
And: No competitive disaster here, too



Chinese share of US imports (%)



Chinese share of EU-27 imports (%)





In Summary, China....

- ..is the largest economic comeback story.
- ..will be the factory of the world..
- ...and builds the infrastructure for it!
- ..will eventually get a cost structure like us.
- ..is not a trade threat but a huge domestic market that will take off soon.
- ...puts up trade and investment hurdles that make China's integration in global system tough.
- ..will remain competitive for a long time.