

Letter from CH-ina #3

Shanghai, 13 August 2009

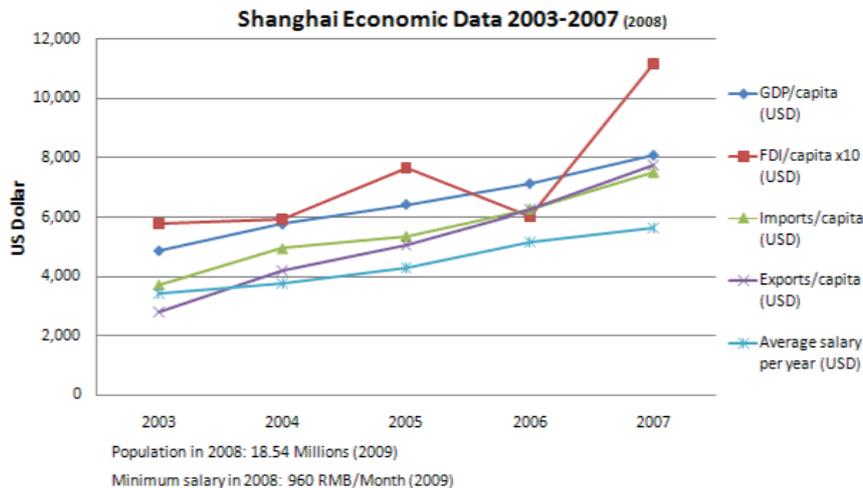
(whole or part of this article published in "China Contact", "Wirtschaftsblatt" and "Finanz und Wirtschaft")

The Inland Coast – China's Interior Development and Competition to Low-Cost Asia

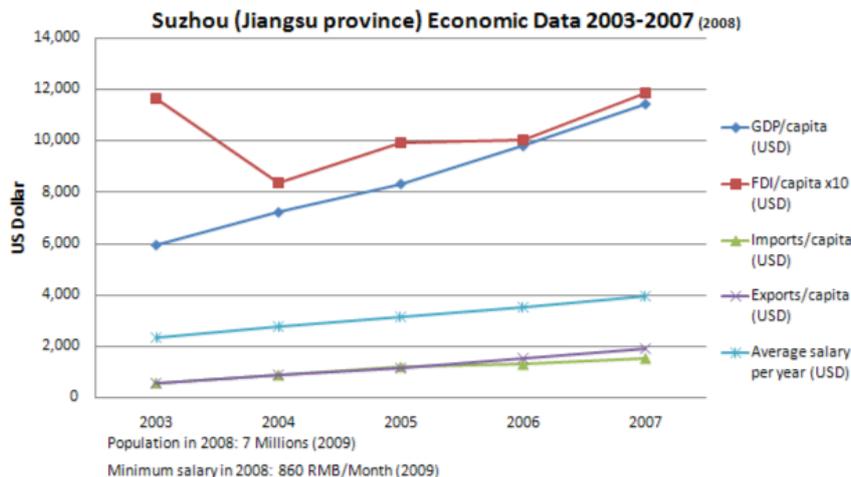
The recent crisis has made it even more important for China to depend less on the rest of the world for growth and to develop quickly the interior markets. While exports contribute to only 20% of China's GDP, export growth accounted for half of 2008's economic growth.

Yet, due to difficult or expensive logistics, over 90% of China's exports are produced within 250 km of the seashore. These exports, the foreign investments and the know-how that foreign enterprises brought have been the growth engines of the coastal regions of China. Meanwhile, the interior has mostly developed through infrastructure financed by the government and consumption growth, partially fueled by the income that migrants working on the coast send back home.

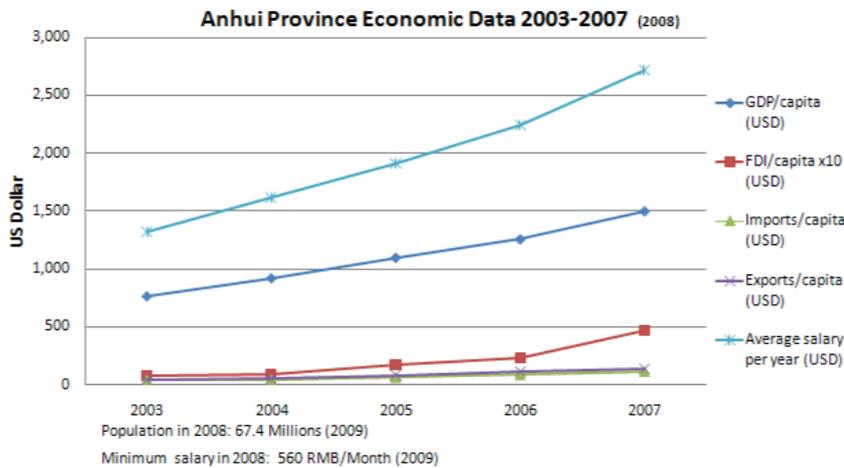
As a result, disparities between regions are quite extraordinary. Shanghai's average salaries are twice those of neighboring Anhui province. Minimum salaries in Hefei, Anhui's capital city, are 35% lower than those of Suzhou (the international manufacturing center of choice, next to Shanghai).



One could imagine a development model where the coastal areas' continued growth generates enough wealth to drive the development of the interior. However, in this case the wealth gap between regions will not be reduced, or will even increase. Besides, China's middle class is only about 2 to 300 Mio. strong. To count on their consumption to raise the living standard of the Inland's 800 Mio. low income citizens will take too long.

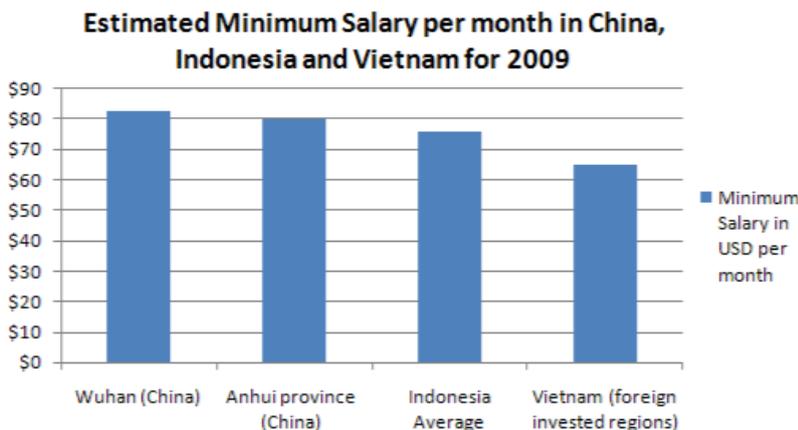


On the other hand, the direct Inland's development is also an opportunity to maintain exports levels: while the coast has become expensive, minimum wages in Anhui and Hebei (the Chinese provinces along the Yangtze River West of Shanghai) are competitive with those of Indonesia.



Besides, Vietnam's minimum wages are catching up with this region's too. This is mainly due to very high inflation in Vietnam in 2008 (23%), and an expected 10.5% price increase in 2009 while China's CPI will stay around zero this year. As a result, Vietnam's labor costs are not low enough to give it an important production competitive advantage, particularly when one takes into consideration China's superior supply chain. (The range of components and

materials available domestically is close to what is available in Europe. Additionally, their quality/price ratio is most competitive.)



To make good on the opportunity, large container ports are being built along the Yangtze River that will make shipping of goods almost as convenient as they are from the coastal cities. Wuhan (capital of Hebei) already has one while Chongqing (2'500km inland!) is building its own.

In addition, to ensure access to all the soft skills (management, knowledge of international

markets and cultures, financial and insurance services), Shanghai, at the mouth of the Yangtze River, is building one of the largest people transportation hubs in the world. It will bundle conventional and magnetic levitation very high speed trains (up to 400 Km/h), 5 metro lines, and the newly expanded Hongqiao airport. The hub will start operating for the World Expo in May 2010 and, by 2020, it is planned to handle the extraordinary amount of 400 Mio. passengers per year!

In addition to linking Beijing to Shanghai by rail in under 5 hours, Chengdu (in the far west of China, at the end of the Yangtze valley) will be reached in just 7 hours. Hefei and Wuhan, now too far to be considered as part of the Shanghai area, will be within 3.5 and 1.5 hours reach of Hongqiao. The new trains will allow day trips and actually make these large cities of almost 5 and 7 Mio. inhabitants part of the Yangtze Delta. Alone, these two Yangtze River capital cities and their provinces will add populations of 130 Mio. inhabitants to the Greater Shanghai area.

As it develops, the Yangtze valley will add an inland coast of more than 2'500km, with Shanghai as its bridge head to the world. In the coming decade, the Shanghai Greater area will become a formidable region gathering populations the size of the USA or Western Europe and be able to compete internationally both in the low-cost and high-tech exports.

Watch out for China's interior development and the new opportunities that the Inland Coast emergence will bring in the coming years!

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