CHINA BUSINESS CLIMATE SURVEY REPORT 2023

中国商务环境调查报告

This marks the 25th year that AmCham China has surveyed its members on the business environment in China. This year we again partnered with PwC for data collection and in-depth analysis. This survey was conducted between October 19 and November 16, 2022 and was completed by 319 AmCham China member company representatives, representing roughly 47% of eligible respondents.

After three full years dominated by the COVID-19 pandemic, our members reported a slightly more pessimistic outlook compared to previous years. This inflection toward pessimism reflected members' attitudes about their companies' financial performance and overall expectations around China's openness and business climate. Estimated performance results for 2022 showed a decline in the portion of member companies that saw increased revenue, profitability, and Earnings Before Interest and Taxes (EBIT) margins compared to last year. Much of the decline in 2022 performance was attributed to COVID-19 prevention measures. While many members still see China as a priority market, this year saw a sharp decline in members who rank China as a top three priority. The willingness to increase investment and strategic priority is declining as China becomes merely one of many investment destinations. Members continue to report uncertainty in bilateral relations as their top business challenge in China, along with increasing uncertainty about the regulatory environment and rising labor costs.

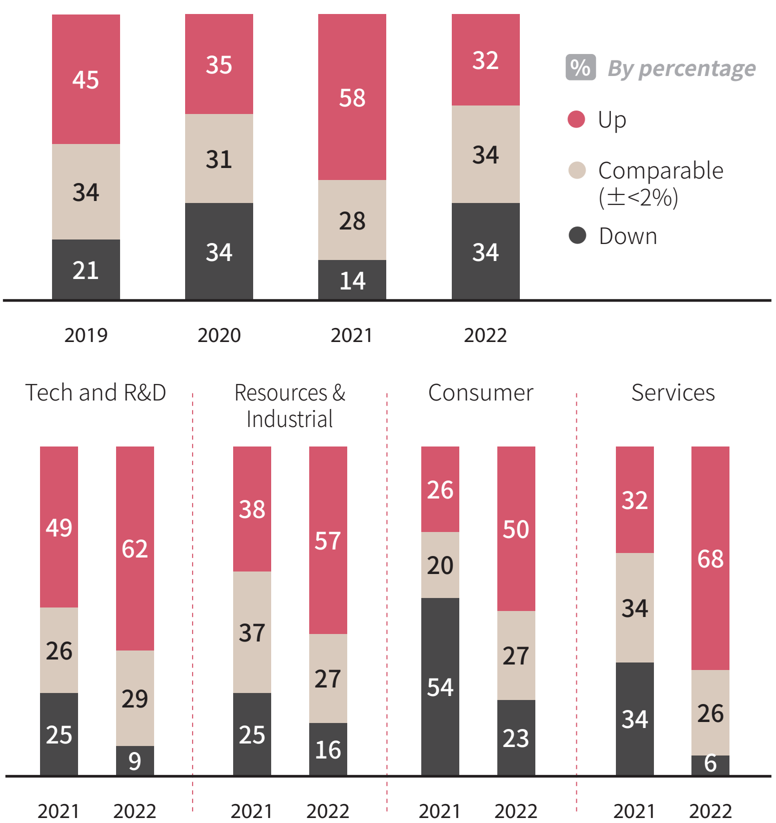
Financial Performance Trends Reversed in 2022, Estimated to Decline to 2020 Levels

34% of members estimated that their 2022 revenue will be lower than 2021. While 2021 saw a trend toward normalization of financial expectations and general market perception, 2022 results are similar to reported performance in 2020 – when the pandemic began. According to two-thirds

Figure 20. Top Five Business Challenges in China

	2019	2020	2021	2022	2023
1	Inconsistent regulatory interpretation and unclear laws & enforcement 55%	Rising labor costs 45%	Rising tensions in US-China relations 78%	Rising tensions in US-China relations 56%	Rising tensions in US-China relations 66%
2	Rising labor costs 48%	Inconsistent regulatory interpretation and unclear laws & enforcement 41%	Rising labor costs 40%	Inconsistent regulatory interpretation and unclear laws & enforcement 31%	COVID-19 prevention measures 55%
3	Rising tensions in US-China relations 45%	Rising tensions in US-China relations 41%	Inconsistent regulatory interpretation and unclear laws & enforcement 37%	Rising labor costs 29%	Inconsistent regulatory interpretation and unclear laws & enforcement 32%
4	Increasing competition from privately owned Chinese companies 58%	Regulatory compliance risks 23%	Increasing competition from privately owned Chinese companies 33%	Regulatory compliance risks 28%	Rising labor costs 25%
5	Shortages of qualified management 28%	Shortages of qualified management 23%	Concerns about data security 26%	Concerns about data security 23%	Regulatory compliance risks 25%

Figure 9. How does the estimated 2022 revenue of your company's China operations compare with 2021 results?



of members, much of 2022's financial performance issues can be explained by intermittent regional lockdowns to control local outbreaks. The proportion of companies forecasting profitability decreased from 59% in 2021 to 44% in 2022. One-in-five members faced losses in 2022. The proportion of companies in the Tech and R&D, Resources & Industrial, and Services sectors expecting to be profitable dropped significantly.

Members are Less Willing to Invest in China

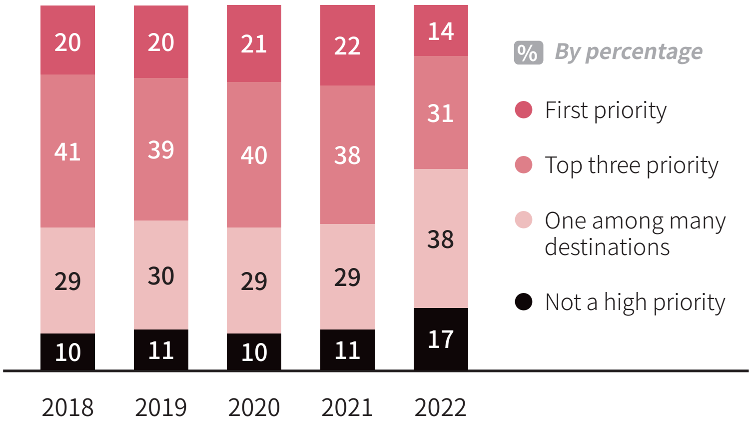
This year, less than half of members ranked China as a top three investment priority, marking a significant shift. Nearly half of members (45%) reported that China's investment environment is deteriorating, a 31pp uptick from last year and the highest response rate on this answer choice in the last five years. Most members report that they are revising their investment plans for China, opting to make no additional investment or even to decrease investment overall. Uncertainty around China's policy environment, the expectation of slower economic growth in China, and overall uncertainty in the US-China economic relationship were cited by members as the top reasons for decreasing investment.

Members Show Restrained Confidence in China's General Openness to Foreign Companies

Nearly half of respondents still report feeling "less welcome" in China, a trend that has risen by 11pp since 2020. This may be related to more restrictive technology and cybersecurity-related regulations or rising tension in the US-China relationship. More than one-third of respondents reported that foreign companies are treated unfairly by government policies and enforcement actions compared to their domestic competitors, which is a 5pp increase since 2021. Additionally, for the second year in a row, uncertainty and lack of confidence rose across all sectors, as members consider whether the government is committed to further opening China's market to foreign investment.

85% of respondents believe that innovation and R&D are important for business growth in China, increasing from last year. Members identified the top three barriers to innovation as technology decoupling, restrictive cybersecurity policy, and insufficient IP protection. There is declining sentiment and growing uncertainty about IPR enforcement across all sectors during the past five years, although over one-third of respondents reported that China's enforcement of IPR improved in the past year. Nearly one-quarter of members say that inadequate IP protection limits investment in China, with difficulty prosecuting IP infringements and insufficient IP protection as the top two challenges.

Figure 26. China's rank in near-term global investment plans



Most Members are Not Considering Supply Chain Relocation, Though There was a 10% Increase of Those Considering Relocation

Most members have no plan to move their supply chain outside of China. However, for the first time since the pandemic, we see a 10pp increase in the number of companies considering or reporting having already started to

Figure 35. Is your company considering, or has it already begun the process of relocating manufacturing or sourcing outside of China?

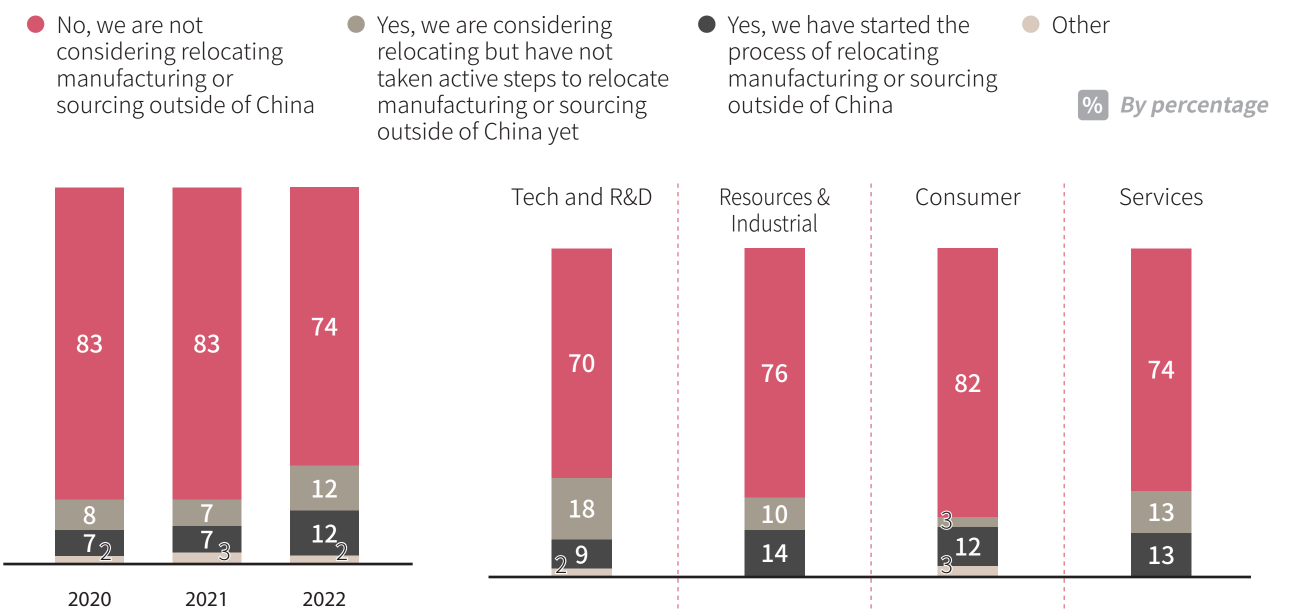
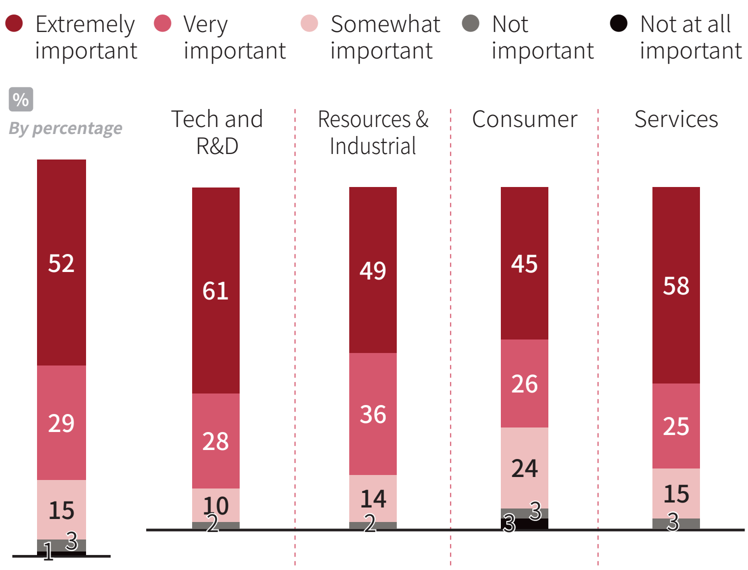


Figure 49. Top three human capital challenges

	2022	2023
1	Total labor costs 44%	US-China tensions and geopolitical concerns 43%
2	Rising salary and wage expenses 42%	Total labor costs 37%
3	US-China tensions and geopolitical concerns 28%	Rising salary and wage expenses 31%

Figure 65. Importance of positive bilateral relations between China and the US to your company's business growth in China



relocate manufacturing and sourcing outside of China. Among the 24% of members considering moving capacity outside of China, one-third plan to move operations back to the US, up 6pp from 2021. This may be related to rising tension in US-China relations.

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The Top Three HR Challenges Include US-China Relations and People-related Costs

Members report that their top three human resources challenges are US-China tensions and geopolitical concerns (43%), labor costs (37%), and rising salary and wage costs (31%). In this year's survey, 51% of members reported that their top expatriate candidates were unwilling to move to China, up 21pp from last year. As quarantine for international arrivals officially ended on January 8, 2023, it is expected that the travel situation will improve once international flights return to pre-pandemic levels. It remains unclear whether increased ease of travel will be able to reverse the trend of expatriate staff unwilling to move to China.

Members are Leveraging ESG Strategies in China Operations

80% of respondents report that they are taking or plan to take action to implement Environmental (E), Social (S), and Governance (G) strategies in China (Figure 23). Members believe such efforts will improve their brand image and help with talent recruitment and retention. 73% of members ranked Diversity, Equity, and Inclusion (DEI) as their top ESG strategy in China, followed by Governance and business ethics (72%). Around 60% of members report that the ESG strategies focused on climate change.

US-China Tensions Remains the Top Business Challenge, and Improved Relations are Vital for Business

Members report that uncertainty in bilateral relations is their top business challenge in China, according to 66% of respondents. This is especially true in the Tech and R&D sector, as the US and China are facing off over semiconductors. Such a contest may be a harbinger of further deterioration in their relationship. About half of members believe bilateral relations will deteriorate, nearly twice the proportion of members compared to the previous three years.

Many hope that high-level bilateral engagement and the brokering of new agreements between the US and China will benefit the business community. Regarding implementation of the Phase One Trade Deal, at least one-third of members remain uncertain about how it impacts their business. 60% of members hope that future bilateral trade talks will result in further opening of Chinese markets to foreign companies, up 17pp from last year, and 43% are looking for further reductions in tariffs, up 17pp from the previous year.

Both the US and the Chinese governments have a critical role to play. Members' priority suggestions for the US and China governments are to refrain from aggressive rhetoric and tit-for-tat actions towards each other in order to establish a floor under the deteriorating relationship.