

# China's emerging financial markets challenges and global impact

[Countries](#), [China](#)



China over the last decade has experienced high levels of economic growth and consequently there has been an explosion of growth in the Smartphone mobile Industry with China becoming the largest smartphone mobile market in the world and recently the largest producer of smartphones, producing 224 million smartphone units in 2012. This essay aims to examine how China has become an important player in the Smartphone Market.

In the context of this essay it is important to define innovation and globalisation as these two words have helped to shape the Chinese smartphone industry, turning China into a serious competitive player in this growing industry. Innovation is defined as “ the process of making changes to something established by introducing something new that adds value to customers and contributes to the knowledge store of the organization” Whilst Globalisation in the context of innovation is defined as “ the increased international integration of economic activities and the raising importance of knowledge in economic processes”.

It is clear that Chinese companies have been able to develop an established idea such as the Smartphone and make themselves leaders in the production of the hardware. The smartphone industry has become an important engine of growth for the economy, with the smartphone users in China set to double by the end of 2013 to 500million. Leading Chinese Mobile Phone makers such as ZTE and Huawei are making inroads into the mature Western markets at the same time cementing their position as some of the largest players in the Chinese Smartphone market, occupying three out of the top five slots for Smartphone manufacturers.

It is clear Chinese Smartphone makers are able to produce their phones at a much cheaper cost than foreign companies, with the cost of processor chips falling greatly in price helping to reduce production costs. This essay examines how China has become a competitive and innovative global player in Smartphone production, examines the current growth trends and future trends of the Smartphone market in China, and how it is slowly evolving into a mature market with the adoption of more Smartphones amongst a greater proportion of the general population.

The role of foreign investment and technology in developing the Smartphone Industry in China is examined, with large companies such as Samsung setting up Research and Development (R&D) centres in China, to help facilitate innovation in the sector. Finally I will discuss the possible advantages and disadvantages of China becoming more competitive and innovative within the Smartphone industry. Since 2000 the Chinese Mobile Phone market has enjoyed phenomenal levels of growth, from having a customer base in 2000 of 95.22 million to 1.06 Billion in 2012.

Out of this figure currently only 330 million subscribers use a Smartphone showing massive growth potential for companies operating in the market. This gives China a 26.5% share of the World Smartphone market. This figure should grow to 500 million by the end of 2013 as more subscribers are persuaded to sign onto 3G services of which only 150 million do so and the number of Chinese who access the internet via their phones also increases. Currently the figure stands at 420 million for 2012 representing around 74.5% of the internet population.

In the last twelve years Chinese Smartphone manufacturers have become the leaders in the Volume of smartphone units sold. The Chinese Market overtook the USA as the largest by Volume sold in 2011. The vast majority of this growth has occurred in China. A good example of Chinese company that has emerged as a winner has been Lenovo. Although it's known for its manufacturing of Personal computers, it has launched a mobile phone division and found notable success in China becoming the second largest player in the Chinese Smartphone Market.

By launching a variety of Models ranging in price, moving away from the normal model followed by most Chinese manufacturers which is " one-size fits all. " This has been beneficial as it has built market share at the expense of rivals such as Apple, with its share increasing from 5% to 14. 4% in 2012. Its expansion in China is allowing Lenovo to push its products into more emerging markets, slowly increasing the global profile for its Smartphones. This is ultimately the strategy Chinese firms should pursue, as it allows them to increase brand awareness of their Smartphones.

Western Firms have seen their market share fall, because Chinese firms have been able to launch more products which are similar but have a few exclusive features for the Chinese market. The other big factor is price. Although Chinese mobile operators such as China Unicom subsidise the cost of products such as the Apple iPhone, the cost is still beyond the vast majority of Chinese mobile phone users whose average salary is around ? 5, 000 a year. In 2011 smartphones costing less than \$200 made up 40% of

Smartphones, whereas for devices costing in excess of \$700 accounted for only 11% of the market.

This shows that the low-margin cheaper products made by Lenovo and other Chinese manufacturers are clear winners, over the higher quality products made by Apple and Samsung. It is also apparent that there is also a clear preference for the Google produced Android Operating System over rival ones such as IOS by Apple. The Android System between 2011 and 2012 has built a dominant market share making up 86. 1% of the total Smartphone operating systems in China. The Smartphone Industry in China is structured in a number of ways. Firstly the actual market is dominated by a few firms however there are over 100 Chinese Smartphone manufacturers.

Samsung is the clear leader, followed by Lenovo, ZTE and Huawei and then finally Apple. These five firms' products make up the vast majority of Smartphone sales in China. The actual market itself is divided into a two tier pricing structure, with an entry-level tier where Smartphones costing \$200 and a high end tier costing in excess of \$300. There has been an explosion of growth in the Entry-level tier. This is because more of China's population is expected to switch from their current 2G phones to 3G capable ones and see the \$200 priced phones as the most reasonable ones to buy.

In addition internet firms such as Baidu Inc are developing their own branded products and are using their brand appeal to attract customers. For Chinese manufacturers the low-margin approach which many of them are taking means the market is becoming highly competitive. The majority of Smartphones sold in China are manufactured and assembled in Guangdong

province around the Pearl Delta economic zone. Chinese companies including Lenovo, Huawei and ZTE have headquarters, production facilities and R&D centres located here.

In the case of Lenovo it has chosen to forego the strategy of outsourcing operations to specialist equipment manufacturers like the majority of Chinese Smartphone manufacturers. Instead it has focused on vertical integration to set up its own manufacturing plant in Beijing, Huiyang, Shenzhen and Shanghai. This helps to reduce manufacturing costs and allow them to charge less for their smart phones.

Both Huawei and ZTE both have headquarters and Production facilities in Shenzhen but they also outsource some operations, however in recent years they have begun to focus on opening R&D centres and production facilities abroad. In the case of ZTE, in 2006 it opened a R&D and production centre in Pakistan and in the case of Brazil built a manufacturing plant encompassed in an industrial park backed financially by ZTE, whilst Huawei has set-up R&D centres in Stockholm, Dallas and Bangalore. These allow the companies to sell their products at cheaper prices as import duties are bypassed and also to learn more about these new markets. It is a lot more cost effective to produce in china, as in the case of Apple.

It uses Foxconn which is a contract manufacturer based in Taiwan, with 13 production facilities in China to produce its iPhone. This is due to the company already having supply chain networks set-up and with access to cheaper labour in China, it makes cost-sense to base production here. In the case of selling the Smartphones, Chinese firms can take advantage of pre-

existing distribution networks to sell their phones. In the case of Chinese Manufacturers, expanding abroad has meant opening new factories and facilities in new markets. This has helped make Chinese firms global companies.

The Smartphone Industry is also financially more stable as many of the big players such as Huawei, ZTE and Lenovo are former state run companies that have evolved into standalone companies but enjoy a close relationship with the government. This means that subsidies and financing can come easily for these firms as well as additional subtle market power. In the case of mobile phone contracts, as the Chinese government subsidises the cost it is cheap for Chinese consumers to buy smartphones. For Western firms especially Apple, this is proving a challenge as their handsets have higher costs.

In addition it seems the Government is helping the local Smartphone industry by preventing China mobile and Apple from reaching an agreement to sell the iPhone on its network. By making the subsidy China mobile pays to Apple an issue, it helps to stop Apple distributing its products to a greater percentage of the Chinese population, in this case 65% of the Chinese mobile market. In terms of innovation and global competitiveness within the Smartphone Industry, Chinese companies have not been as innovative and competitive as their international peers.

This has been the case for the majority of the last decade, but as foreign players have begun to take a greater slice of their home markets, these companies have started to realise the mass-market model is no longer the

best to pursue. The actual technology in use in the Smartphone market in China is by no means the most advanced. In fact companies like Huawei, ZTE and Lenovo are starting to launch high-end products with large screens and 1080p cameras, such as Huawei Ascend Mate and the ZTE Grand S only now. Such features have been the norm on international companies' phones. However where the innovation could come from is designing software exclusively for the Chinese population, for example Tencent Technologies is working to create its own voice-recognition software to provide key services such as Map, Weather and Enquiry services for Chinese consumers. Although this type of software is available on Apple and Samsung phones, it has yet to be fine-tuned to the needs of the Chinese consumer.

It is here I feel that Chinese firms can really become market leaders; by using their advantage of being located in China they should look to release Smartphones products and software exclusively for the Chinese market. A key competitive advantage China currently has in Smartphone production is the fact it produces around 91% of the worlds' Rare Earth Metals, as well as sitting on around 50% of the worlds' known reserves. These metals are important in producing the specialist components of Smartphones.

As China is the main supplier, Chinese firms have an advantage in that they can acquire these materials at a substantially cheaper cost than their international competitors. This helps to make Chinese Smartphone production costs lower than international competitors, as the government has imposed quotas on Rare-Earth Metal exports, limiting the access of international companies to them. However due to the environmental



destruction caused by the mining of these metals, the Chinese government has signalled that it wants to become a net importer of these metals.

This may reduce the competitiveness of Chinese Smartphone manufacturers as their advantage in acquiring these metals cheaply is eroded. A massive inhibitor to innovation and development by Chinese firms is the absence of any strict Intellectual-Property Rights law. This has allowed smaller companies to just produce cheap blatant knockoffs of various Chinese and International companies' models. This is big problem because the lack of punishment means firms are reluctant to develop new ideas and plough lots of resources into R&D.

In addition for Chinese firms need to start to develop their own unique Smartphone software platform. As currently they are open to potential legal disputes over intellectual property violation as several important patents are held by international companies including Google and Microsoft. Chinese companies on the other-hand just own patents to do with physical designs of their handsets. This is true especially as these firms seek to expand overseas, such legal disputes will become regularity as international competitors seeks to limit the competition from these Chinese firms.

Another potential problem for the future is that Real wages are rising in China, and the low-cost advantage that has helped Chinese Manufacturers is being eroded slowly and some companies especially international ones may seek to move manufacturing to cheaper locations. Advantages the Chinese Smartphone industry has enjoyed include seeing the strengths and weaknesses of international competitor in launching new Smartphone

products and software. Rather than having to plough resources and capital in R&D, Chinese firms have been able to just use the Android Platform and adopt it into their phones.

In addition the actual cost of producing phones has been greatly reduced as chip companies such as MediaTek and Qualcomm which specialise in making chips, have decided to make entire handset designs, for these firms allowing them to spend more on sales and marketing. The downside is the lack of incentives for these firms to spend more on R&D to create original products. Another advantage China's smartphone industry and especially the Chinese companies have are the already established distribution networks for companies like Lenovo, as they sell other products like PCs via them which allow them to market their products to a wider population.

International firms need to create networks from scratch for example building standalone stores to sell and advertise products. This takes time and as a result only Tier 1 cities like Beijing and Shanghai enjoy Apple and Samsung exclusive stores. In Tier 2 cities with a population of 3 million or more and a total population of 300 million, these cities are not as big markets for international companies and it is here where Chinese firms are making huge gains as they can advertise and distribute their products to this huge market without much competition.