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# LOGISTICAL FLOWCHART AND FEASIBILITY STUDY FOR DOING BUSINESS IN CHINA'S APPAREL AND ACCESSORIES MARKET

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## Abstract

*This research was designed to develop a logistical flowchart and feasibility study for an American apparel and accessories company. China is now regarded as the fourth-largest economy in the world, with an average annual growth rate of 9.8 percent--triple the world average. In contrast to other developed countries that are greatly affected by the financial crisis, China appears to have a favorable turn in its foreign trade starting from March. These achievements are primarily due to China's decision to join the World Trade Organization (WTO). This has led to rapid and sustained increases of U.S. exports to China, making China the second biggest foreign market for U.S. goods. Under the US-China WTO Agreement in 2004, China has not only phased out trading and distribution rights to US firms, but also eliminated all import quotas. This is significant since the agreement has made it possible for small and medium-sized US companies to import and distribute products without going through a state-trading enterprise or middleman; also business licenses for foreign investment are now easily obtainable.*

## Introduction

The boom of the economy has drawn various investors, including luxury brand companies. All the facts and data the researcher has illustrated clearly demonstrate that the performance of luxury items are still "solid" and strong, which means the current Chinese luxury market is thriving despite the recession. It also indicates that this market is far from mature, thus providing a huge opportunity to entrepreneurs.

Another opportunity is the driving force behind the luxury market. Although people in foreign countries are currently "tightening their belts", Chinese consumers are still spending. With the exponential growth of the Chinese middle class who are able and willing to buy luxury goods, China is predicted to consume 29% of the world's luxury goods by 2015. Compared with old people, young Chinese have a low savings rate and tend to dispose most of their income. Young ladies, in particular, are more likely to spend as long as the products are attractive to buy. They believe that possessing luxury goods are in accord with fashion and a high quality lifestyle.

Before investors start businesses, they must know how to distribute their goods. In this article, the author has gathered all the related information and put it into a flow chart; involving the application for a business license, representative office and import quota license, shipping, customs declaration, and distribution channels.

To make this plan more effective and concrete, the researcher also suggests the representative products and basic price level by analyzing customer behavior and disposable income.

The most impressive issue is her pioneering market strategy, which absorbs the virtues of online stores and shopping outlets. This unique strategy, also known as competitive advantage, endows the store a considerable power to carve out a market share.

On the whole, the business seems to be quite striking and feasible. However, the biggest threat one needs to address is that the competition in the luxury market has become quite fierce,

as a multitude of foreign investors saturate the Chinese market each year. It is difficult to acquire market share from existing competitors, who have already built up a loyal customer base. Therefore, how to broaden brand awareness rapidly and gain customer loyalty is the most noteworthy issue for the business owner.

## **Background**

### **Economy**

Following a multitude of economic reforms, China has achieved remarkable success in economic development. It is reported that China has maintained an average annual growth rate of 9.8 percent – triple the world average, over the past 30 years<sup>1</sup>. According to China's Xinhua news agency, the Chinese GDP soared from 53 billion USD in 1978 to 3.7 trillion USD in 2007, making China the fourth-largest economy in the world. U.S. companies are benefiting from this, as evidenced by rapid and sustained increases in U.S. exports to China. Over the past several years, increases of U.S. exports to China averaged well over 20 percent. In 2007, the U.S. exports to China increased by 5.7 percent, according to the Census Bureau, causing China to be the fastest growing foreign market for U.S. goods. As statistics show, the China-U.S. total trade is 354.1 USD billion, placing China as its second biggest trading partner behind Canada. Accurately, U.S. exports of goods to China are 58.3 billion USD for 2007<sup>2</sup>.

On account of the global economic recession, it was the fifth consecutive month of declines in both imports and exports in China, but the rate of decrease shrank by 6.3 and 9.2 percent in 2008 respectively, compared with the first two months of 2009. During March, China's import and export volume totaled \$162 billion and the trade surplus reached \$18.56 billion, up 41.2 percent year on year, as shown by Customs statistics. All of these figures signify a favorable turn in China's foreign trade starting from March<sup>3</sup>.

### **Distribution**

“Distribution” is a broad concept that encompasses wholesaling, retailing, maintenance, repair, and transportation.

Before the US-China WTO Agreement, U.S. companies had no right to distribute products other than those they made in China, or to own or manage distribution networks, wholesaling outlets, or warehouses. Also, the Chinese government severely restricted trading rights and distribution to foreign invested enterprises. Moreover, business licenses limited the ability of US firms to conduct marketing, after-sales service, maintenance and repair, and customer support.

Thanks to the agreements during China's WTO accession, US trade and investment have benefited from a more open and stable China. Basically, China has eliminated most foreign-equity restrictions, especially in sectors where the United States has a strong commercial interest. In terms of trading rights and distribution rights, Americans are permitted to trade, distribute, and sell goods themselves, allowing for better control and greater market access<sup>4</sup>. “As Chinese commitments are phased in, foreign firms are able to provide services auxiliary to distribution

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<sup>1</sup> China's Xinhua news agency reported, <http://www.cnn.com/2008/BUSINESS/12/18/china.economic.reform/index.html#cnmSTCVideo>

<sup>2</sup> Lynch, David J. "Makopolo Markets US Companies Directly into China". American Companies export to China. <http://makopolo.wordpress.com/2008/08/10/makopolo-markets-us-companies-directly-into-china/>

<sup>3</sup> By Huang Yingchuan, Canton Fair News <http://www.cantonfair.org.cn/en/info/news/detail.aspx?id=14885>

<sup>4</sup> Source: The White House Office of Public Liaison

including, rental and leasing, air courier, freight forwarding, storage and warehousing, advertising, technical testing and analysis, and packaging<sup>5</sup>.”

With regard to import quotas and tariffs, China has agreed to phase out quotas, and reduce average tariffs to 14.5% for US priority products, and 17% for all other products. Prior to this the average tariffs on US priority products was 31.5%. On the other hand, FIEs (Foreign Invested Enterprises) importing items subject to quota and licensing control for domestic sale in China directly should apply for the required import quota, import license or automatic import licensing, according to the New Foreign Trade Law amended in April 2004<sup>6</sup>.

In a sense, it is significant that the agreement opened new placements for small and medium-sized US companies to import and distribute products without going through state-trading enterprises or middlemen. In accordance with the existing laws in China, the procedures for the establishment of enterprises with foreign investments are quite simple. After the initial project application is approved in writing by the examination and ratification authorities, the investors may submit a formal application with articles of corporation and other required documents. Upon receipt of the Approval Certificate, they can proceed with the registration formalities by presenting the Approval Certificate<sup>7</sup>. Fortunately many provinces, autonomous regions, and municipalities directly under the control of the central government have established foreign investment service centers, which offer foreign investors one-stop service, providing investors with efficient and qualified services.

## **Apparel Industry**

With the rising purchasing power and increasing influence of Western culture, the domestic apparel market of China is still thriving, despite the global economic depression. Typically, the emergence of the middle class, growing young population, and rapid globalization of culture is fuelling the demand for branded apparel in the country.

According to export statistics released by China National Textile & Apparel Council (CNTAC), the total annual sales were above 660,000 USD in this last fiscal year. Currently, more than 2000 brands of clothing are available in China. Kurt Salmon Associates, an industry-focused management consulting firm, has forecasted that by 2020 the total clothing consumption of China will be about 120% of that of Japan, drastic jump from the current 10%. It is this speculation that has attracted many overseas investors to tap the rising demand of branded products in China. As a consequence, many international clothing manufacturers and retailers are now viewing China as a huge potential market.

Although people in the developed world have been tightening their belts and focusing spending on daily necessities, the Chinese market shows remarkable resilience in the financial crisis, and this is because of the increasing number of people willing to buy goods. Furthermore, consumers appear to prefer more fashionable and branded products as their purchasing power is stronger.

So far, China is considered to be the largest consumer market, and is expected to enter into a new era in the apparel and textile industry, which will be stimulated in the coming years.

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<sup>5</sup> <http://www.sinomania.com/CHINANEWS/china-wto.html#top>

<sup>6</sup> <http://www.marisglobal.com.cn/quota-and-licensing-control.html>

<sup>7</sup> <http://www.hongkong-company.org/news.aspx?id=11&tid=2>

## Luxury Market

China is the third largest consumer of luxury goods worldwide, and its appetite for the good life continues to increase in step with the rapidly growing economy. It is anticipated that China will consume 29% of the world's luxury goods by 2015, making it second worldwide to only Japan<sup>8</sup>.

Most economists and marketers agree that China will evolve into a nation of spenders<sup>9</sup>. Such expectation can be supported by savings rates, which are finally falling from the historic 40% rate, as Chinese consumers are increasingly optimistic about their futures and look to enjoy life by buying items from companies like Ralph Lauren (RL), Tiffany's (TIF), and Omega (SWGNF.PK). It is surprising to know that the spending power in China is spectacular. An estimated 415,000 Chinese had more than \$1 million in disposable assets in 2007, more than any other country, according to the Merrill-Lynch Asia-Pacific Wealth Report. The expanding middle class constitutes an important group of consumers who desire and can afford luxury goods. Recent data shows that up to 170 million people can afford luxury brands and the number will reach 250 million by next year<sup>10</sup>. Notice that women are more likely to buy luxury products for themselves than men, especially those aged between 25 and 40 and living in developed regions. These women are fashionable, mature, and passionate about lifestyle and quality. Therefore, the aspiring Chinese women are becoming increasingly valuable targets to luxury retailers.

Unlike the mature traditional market, the luxury products market in China is far from saturated either materially or psychologically. In other words, there is still plenty of room for the luxury market to expand. This month Gucci announced that China represented one of the most dynamic areas of retail growth for the firm, with a 2008 sales growth rate of 42 percent in the mainland. Likewise, LVMH claimed that business profit was up 2.1 percent from a year earlier to 3.63 billion Euros in 2008 while sales in USA and Japan declined. Furthermore, Bain & Company anticipated the Chinese luxury market would see growth of 20 to 35 percent in the next five years. According to the Ministry of Commerce, China is expected to be the world's largest luxury market by 2014, accounting for 23 percent of global business.

In spite of the financial crisis, China's impressive economic growth and rising number of new rich have drawn many luxury companies<sup>11</sup>. Coach currently has 17 shops in mainland China, in addition to eight stores in Hong Kong, and two in Macao. Gucci is looking to open its Shanghai flagship store in May, with 25 stores in 17 Chinese cities. Similarly, Cartier, the French jeweler and watchmaker, is planning more stores in Chinese cities.

All these phenomena strongly demonstrate that the Chinese market is so desirable that international luxury companies are speeding up their quest for a share<sup>12</sup>.

### Objective

Based on the investor's hobbies such as reading women's magazines, keeping informed of fashion news and helping others to figure out the best dress styles, she has decided to create a small business that sells women's apparel, including clothing and accessories such as hats, belts, jewelry, and handbags. These are all in increasing demand and are being updated all the time. It

<sup>8</sup> [http://www.marketavenue.cn/upload/articles/ARTICLES\\_1787.htm](http://www.marketavenue.cn/upload/articles/ARTICLES_1787.htm)

<sup>9</sup> Eswar, Prasad. "China's Growth and Integration into World Economy". International Monetary Fund. <http://www.imf.org/external/pubs/ft/op/232/op232.pdf>

<sup>10</sup> China Association of Branding Strategy

<sup>11</sup> Huang Siwei, director of the www.neeu.com website, a Beijing-based luxury and lifestyle portal

<sup>12</sup> Said Yan Jun

is a good opportunity because almost every woman has beauty and fashion needs. Besides, there is no denying that fashion is an ever-changing phenomenon that captivates the entire world. In particular, women aged between 25 and 40 in Shanghai are pursuing fashion, maturity, a passionate lifestyle, and quality. As a result, the investor determines to open a store that offers an extensive range of items inviting customers to mix and match while experimenting with their styles. By collecting the newest trends in the market today, and displaying them with an array of options, the business owner will assist customers in choosing the ensembles that suit them best. Whether she is a sophisticated, career-minded woman or the next Gwen Stefani the store will provide an arrangement of new styles to her, thus maximizing customer satisfaction. In a way, the entrepreneur aims to enable modern women to have an insider's peek into the future of fashion by researching the latest global fashion trends.

## **SWOT Analysis**

### **Strengths**

With China joining the WTO in 2001, China has agreed to lower tariffs and abolish market impediments. Foreign investors gained the right to import and export on their own, and to sell their products without going through a government middleman. By 2005, average tariff rates on U.S. exports dropped dramatically from 30% to 10%<sup>13</sup>. The agreement opens up new opportunities for U.S. firms since China has made significant progress implementing its WTO commitments. This will ensure that foreign investors' business costs are not wildly affected by trade regulations. It will also help expedite the transportation of goods as there will not be many government officials to deal with.

Another strength is the fact that the clothing will be made in America. American clothing manufacturers have state of the art machines which can produce clothing at a much higher quality than Chinese companies can. Products "Made-in-USA" are preferred globally, and enjoy a reputation of high quality. The opposite is true for goods manufactured in China, which are perceived to be of low quality and based on out-dated designs. Demands in the market are very sensitive to changes, and as the apparel market changes, manufacturers are forced to adapt swiftly to each situation that arises. However, China still isn't adept at this due to its lack of innovation and conservation<sup>14</sup>. This provides US companies with an advantage when competing with Chinese apparel companies.

Lastly, the Chinese government aims to build "a well-off society" by 2020 with a per capita GDP of \$3,000. Developed regions such as Shanghai, Beijing, Guangzhou, Shenzhen, Suzhou, and Wenzhou with a total population of more than 300 million will see per capita GDP exceed \$15,000. The 250 million members of China's quickly growing middle and upper-middle classes with their increased disposable income provide foreign investors another advantage. Since no luxury brands dominate the market now, the next five years will be incredibly important for developing brand loyalty and a taste for luxury products. As for the target demographic, the upwardly mobile and aspiring women tend to be increasingly important to luxury companies. According to a recent CRM research project many women buy luxuries because they view these purchases as an investment, something that will help them get ahead at work or in their social circles.

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<sup>13</sup> exporting-to-china, "China Compulsory Certification". Export.gov.  
[http://www.export.gov/china/exporting\\_to\\_china/CCC\\_System.pdf](http://www.export.gov/china/exporting_to_china/CCC_System.pdf)

<sup>14</sup> "Clothing and footwear in Hongkong, China". EUROMONITOR INTERNATIONAL.  
[http://www.euromonitor.com/Clothing\\_And\\_Footwear\\_in\\_Hong\\_Kong\\_China](http://www.euromonitor.com/Clothing_And_Footwear_in_Hong_Kong_China)

## Weaknesses

The biggest disadvantage of conducting business in China is that the current legal and regulatory systems are still opaque, inconsistent, and often arbitrary<sup>15</sup>. Implementation of the law is often criticized as being inconsistent. Although China has made significant progress toward a market-oriented economy, its government still protects local firms. This is especially true for state-owned firms. In addition, thousands of foreign businesses have already failed in China due to a lack of market research conducted on their behalf. While China represents a lot of opportunity the waters are still untested for many new products. Therefore, it is absolutely essential for foreign investors to fully understand legal issues and evaluate risks clearly before they enter into the market.

The second weakness is that foreign investors must also assume the risk of currency exchange rates fluctuating wildly. Since the business owner manufactures products in America and makes a profit in China, the revenue will be exchanged back to dollars. Although the Chinese RMB continues to be appreciated, this does not necessarily mean that the profit will be guaranteed. There is still a possibility that the profit margin will be squeezed out when the value of Chinese currency declines.

Yet another disadvantage is that the preferences of Chinese customers can change faster than foreign investors can cope with. As the business owner is basing production in the USA, the transportation time required to move goods from the USA to local Chinese markets will take roughly two weeks alone<sup>16</sup>. By the time the retailer is able to analyze the shift in preferences and produce a new product it will have probably taken at least two weeks. This amount of time, however short, can be enough for some companies to crumble due to consumer abandonment. On the other hand, the designers already in China know the Chinese people better than foreign investors, which is an indisputable truth. Hence, the owner should pay careful attention to the needs and wants of the target customers in order to survive in the Chinese market. By and large, foreign investors are highly recommended to conduct a long research campaign before establishing their businesses in China.

## Opportunities

Although, the economic crisis is still in full swing, there are signs that the Chinese economic stimulus package is starting to increase manufacturing output and add jobs. Simultaneously, consumers in the country are finally starting to shop more. As a result, it is important that western luxury brands strike while they can, taking advantage of the fact that native luxury brands still lack the history and pedigree of their foreign counterparts, even though their quality is often comparable. Under such a circumstance, investors should have a keen eye for business, and be keen to gain a foothold in China now, in order to build up their own brand loyalties ahead of the native counterparts.

It is particularly noticeable that China's future high-end consumer market will be with the affluent, who are 20 years younger than their peers in the U.S. and Japan<sup>17</sup>. Those wealthy consumers are urban households earning over 37,000 USD annually. In contrast to the traditional Chinese characteristics, the young Chinese have a very low savings rate and are inclined to dispose of most of their income pursuing fashion, high taste, and high quality. That

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<sup>15</sup> Foreign Commercial Service and U.S. Department of State, "usembassy-china". US Commercial Service. [http://www.usembassy-china.org.cn/fcs/ccg\\_2008\\_secured.pdf](http://www.usembassy-china.org.cn/fcs/ccg_2008_secured.pdf)

<sup>16</sup> See *Shipping* section, page 26

<sup>17</sup> McKinsey report <http://www.forbes.com/2009/04/14/china-consumers-wealthy-markets-economy-luxury.html>

means foreign retailers, who want to gain a market share, have to convince young people to purchase their products and win brand loyalties from the youth. Typically, young shoppers are far more willing to drop their paycheck on the “semi-luxury” products that sell for \$100 or less. Therefore, it is a great opportunity for foreign investors. Needless to say, if they take advantage of it and do it in a correct way, their profit will be enhanced substantially.

## Threats

In China there are currently many different large retailers of globally popular brand names. Such include Coach, Gucci, Prada, Chanel, etc. As a multitude of foreign investors saturate the Chinese market each year the competition as a whole has become quite fierce. It is also difficult to acquire market share from the existing competitors, unless the products are differentiated or the market strategies are original.

Another competitor is from the domestic market. Some Chinese have a very strong national pride and are more comfortable with familiarity. One of the marketing strategies a business should consider would be to target peoples’ national pride. As China expands its economy, the domestic market is also progressing, and the Chinese are producing products at a relatively lower price. Thus, the domestic industry is actually gaining more market share in China and thus creating higher brand awareness<sup>18</sup>. Since newly-branded clothing will not be recognized in the Chinese market, it is possible that the owner will have low sales volume initially. All in all, the investor needs to take note not only of the competitors at same level, but also smaller local enterprises that will be gradually expanding in the years to come.

Although luxury products are considered to have high profit margins, the total costs are actually high. Such costs consist of high labor, costly raw materials, transportation freight, and tariffs which exacerbate the business risk substantially. Hence, once the business has failed, the investor will suffer a tremendous loss.

## Summary

With China joining the WTO in 2001, China has agreed to lower tariffs and abolish market impediments. Foreign investors, therefore, have gained the right to import and export on their own and to sell their products without going through a government middleman. This agreement has resulted in great increases in US-China trade, as proved by the fact that China is currently the third largest export market for US goods. In a sense, it is a significant advantage to US investors because the agreement opened a new entry for small and medium-sized US companies to import and distribute products without going through a state-trading enterprise or middleman. Besides, the procedures for the establishment of enterprises with foreign investment are quite simple, which means that the business licenses are now easily accessible. The background, as a whole, is a bright and promising stage that attracts various foreign businesses.

However, the reform is not completed in every respect and some serious problems remain. At the root of problem is excessive Chinese government intervention in the market through an array of trade distorting measures. This government intervention is a reflection of China’s historic, yet unfinished transition from a centrally planned economy to a free-market economy governed by rule of law. Moreover, some Chinese government agencies and officials have not yet fully embraced key WTO principles of market access, nondiscrimination, and

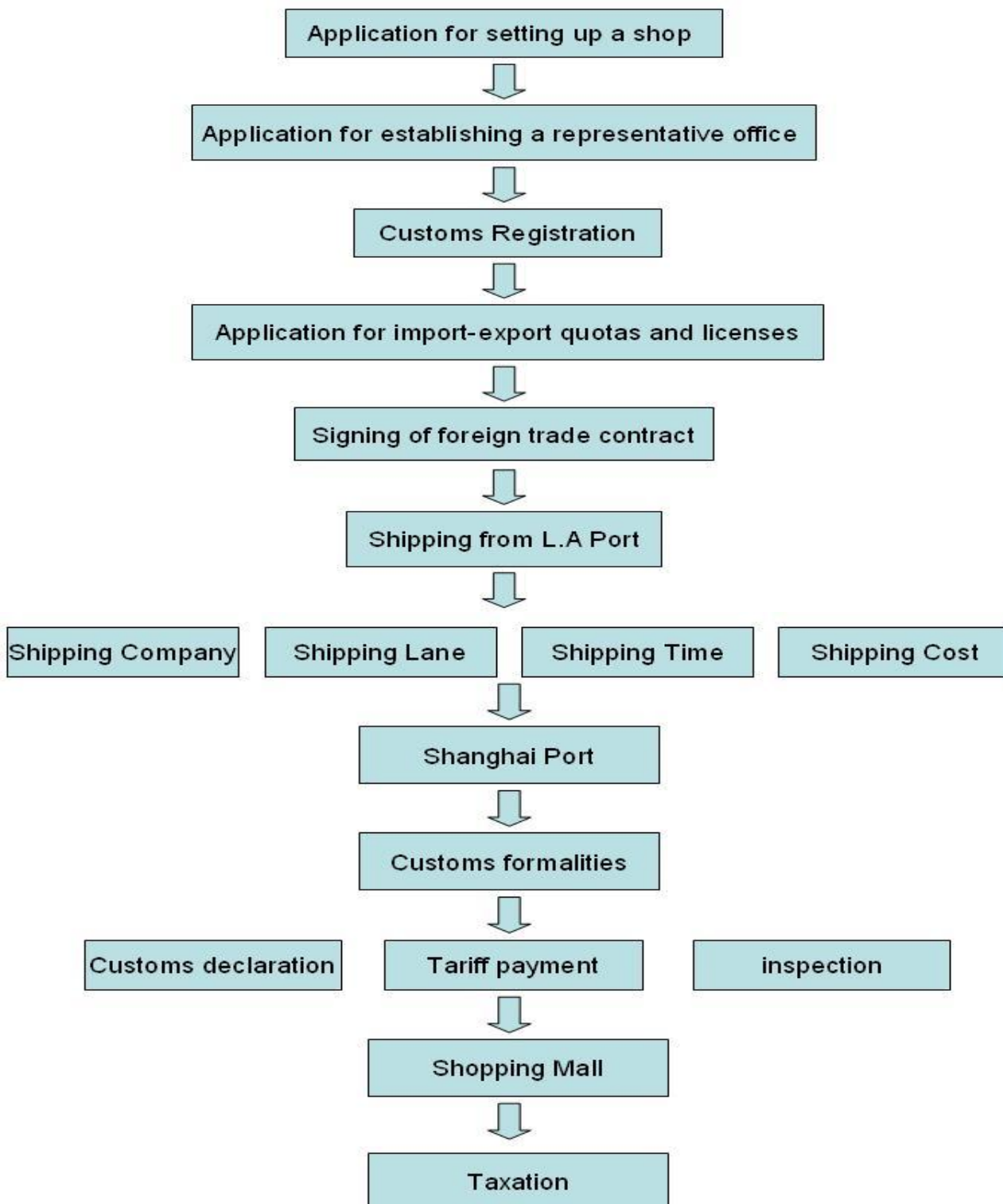
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<sup>18</sup> Xi, Xiao Zhai. "Brand Growth in Shanghai Leads Sales". HKTDC. <http://info.hktdc.com/imn/06030701/clothing200.htm>

transparency. Lack of necessary transparency is still a core problem, frustrating efforts of foreign businesses to achieve the full potential benefits of China's WTO accession.

## LOGISTICS

### Flow Chart



The increasing number of middle class able and willing to buy luxury goods appears to be a remarkable opportunity to foreign entrepreneurs, who intend to seize the great time and grab a piece of the huge potential market. Unlike the mature traditional markets the luxury market still has plenty of room to grow. On the one hand, the performance of luxury items in China is “solid” and strong, and little affected by the financial crisis. On the other hand, China’s impressive economic growth and rising number of new rich have drawn lots of luxury firms. As to the target segment, the Chinese high-end consumer market will be affluent with the youth who have a low savings rate and tend to dispose most of their incomes. This trend implies that how to locate and launch new products to catch young people is the crucial lesson for US firms.

Lastly, the primary threat the investor will face comes from both the existing luxury brands and the expanding domestic brands. Since current brands have already established an amount of loyal customer basis and those designers undoubtedly know more about their target customers, new investors are confronted with a challenging, stressful beginning to spread their brand awareness in the market. Considering the huge cost of production and distribution potential entrepreneurs would be subject to substantial loss if they could not survive in the fierce brand battle. In a nutshell, the market represents a combination of uncertainties.

## Business License

Obtaining a business license (pictured below) is one of the most important requirements to starting a business in China. First an application form must be submitted to the provincial commerce authorities in the province where the foreign-invested commercial enterprise (shop) is registered. Then the provincial commerce authorities would forward the application to the Ministry of Commerce, who would decide whether or not to approve the application within three months from the receipt of all the related documents. The process includes doing all of the paperwork, obtaining photocopies of passport, visas and other business licenses<sup>19</sup>. Specifically, the cost of obtaining a business license will be around \$1000 USD in Shanghai.



- The required documents for setting up shops by foreign-invested commercial enterprises include an application letter, a new contract and articles of association(if revised), a

<sup>19</sup> Runckel & Associates, "Company Registration in Asian". Business in Asian. [http://www.business-in-asia.com/china\\_invest\\_documents.html](http://www.business-in-asia.com/china_invest_documents.html)

feasibility study report on setting up shops, the resolution of the board of directors to set up shops, an audit report for the latest year by an accounting firm, a credit report on the enterprise (photocopy), proofs of registration (photocopy) and proofs of statutory representatives (photocopy) from each of the investors<sup>20</sup>.

If the application is approved, the Ministry of Commerce is to issue an Approval Certificate for Foreign-invested Commercial Enterprises to the successful applicant (picture below). In addition, it is regulated that the business area should not exceed 300 square meters for single shop. After receiving the approval certificate, the investor must go through relevant registrations, such as opening up a bank account for both Chinese and foreign currencies. Also, the company must do tax registration, customs registration, foreign currency registration, business inspection and recruitment procedures<sup>21</sup>.

| 企业名称                                       |  | 中文                        | 长沙德康地产(集团)有限公司        |     |
|--|--|---------------------------|-----------------------|-----|
| NAME OF ENTERPRISE                         |  | CHINESE                   |                       |     |
|  |  | 英文                        |                       |     |
| 企业地址                                       |  | 深圳市福田区莲花西路1001号           |                       |     |
| ADDRESS                                    |  |                           |                       |     |
| 企业类型                                       |  | 外商企业                      | 经营年限                  | 贰拾年 |
| TYPE OF BUSINESS                           |  |                           | DURATION OF OPERATION |     |
| 投资总额                                       |  | 美元伍佰万元                    |                       |     |
| TOTAL INVESTMENT                           |  |                           |                       |     |
| 注册资本                                       |  | 美元伍佰万元                    |                       |     |
| REGISTERED CAPITAL                         |  |                           |                       |     |
| 经营范围                                       |  | 项目投资咨询、国际科技信息咨询、国际经济信息咨询。 |                       |     |
| BUSINESS SCOPE                             |  |                           |                       |     |
| 投资者名称(中、英文)                                |  | 注册地                       | 出资额                   |     |
| NAME OF INVESTORS (IN CHINESE AND ENGLISH) |  | PLACE OF REGISTRATION     | CAPITAL CONTRIBUTION  |     |
| JOHN HANNU BEHAEL PATTINEN                 |  | 美国                        | 伍佰万美元                 |     |
|  |  | 芬兰                        | 伍佰万欧元                 |     |

## Representative Office

A representative office is necessary for the entrepreneur to begin business activities in China. It enables the investor to do a market survey, analyze the local customer base and adjust market strategies swiftly.

The first step for application is to appoint an agent, which can be a foreign investment services company in China or a representative from the investors' own company. Next, the agent will submit all the required documents to the provincial foreign trade and economic cooperation department. Once approval is granted, applicant should proceed to the provincial administration for registration. Other formalities that should be included are the opening of a bank account, applying to Customs for permission to import office equipment, and completing tax payment registration and so on<sup>22</sup>.

<sup>20</sup> <http://www.marisglobal.com.cn/required-documents-2.html>

<sup>21</sup> "Doing business in Shanghai". Ministry of Commerce of the People's Republic of China.

<sup>22</sup> <http://www.marisglobal.com.cn/procedure-3.html>

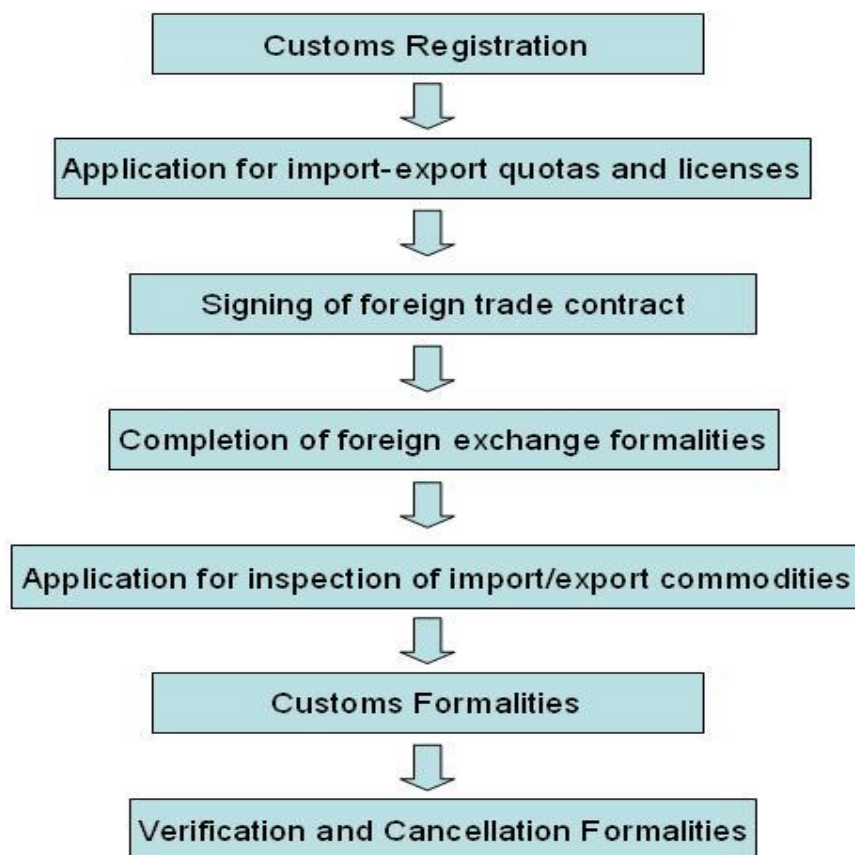
## Import Policies and Tariff Rates

It is essential for importers to be kept informed of Chinese import policies prior to the shipment. Over the past thirty years, China has enacted many quotas, tariffs, taxes, and antidumping laws, in an attempt to control its own development. Such policies actually undermined its growth and development. After China joined the World Trade Organization (WTO) in 2001, it agreed to lower tariff rates and show more transparency with its customs operations. Within five years of joining the WTO, China lowered its tariff rate by 15% to 20%. It has also agreed to bind its tariff rates which prevents it from raising those rates without compensating its trade partners. The elimination of import quotas has also been a major concession on the part of the Chinese government since it joined the trade organization.

Under the US-China WTO agreement in 2004, China has made its commitments to phase in trading rights and distribution rights progressively within 3 years. Consequently, US companies are allowed to distribute the imported goods and establish foreign-owned enterprises. This agreement significantly stimulates the global economy and bilateral trade. As evidence, China is currently the third largest export market for goods from the U.S.

However, FIEs (Foreign Invested Enterprises) importing items that are subject to quota and licensing control for domestic sale in China directly, have to apply for the required import quota, import license or automatic import licensing, according to the New Foreign Trade Law amended in April 2004.

### Import-Export Flow Chart



## Tariff rates

Sales and state taxes, and in some instances customs fees will often be levied as well. Before the foreign investor export goods to China, she needs to determine what the tariff rate is on them as well as any import fees for the country<sup>23</sup>. The current import tariff rate is 12% and China's WTO concession will render the tariff even lower according to the agreed time line.

Additionally, China started to implement unified Value Added Tax, consumption tax and business tax in FIEs while simultaneously abolishing industrial and commercial consolidated tax since 1st January 1994.

Here are the tariff rates for women's or girls' blouses, shirts and shirt-blouses, knitted or crocheted<sup>24</sup>:

The tariff rates for women's or girls' suits, ensembles, jackets, blazers, dresses, skirts, divided skirts, trousers, bib and brace overalls, breeches and shorts (other than swim wear), knitted or crocheted:

Women's or girls' blouses, shirts and shirt-blouses, knitted or crocheted:

| Tariff Item | Goods Description            | Import Tariff Rate   |         | value added tax | Excise Rate |
|-------------|------------------------------|----------------------|---------|-----------------|-------------|
|             |                              | Most Favoured Nation | General |                 |             |
| 61061000    |                              | 16.0                 | 90.0    | 17.0            | .           |
|             | - of cotton                  |                      |         |                 |             |
| 61062000    |                              | 19.4                 | 130.0   | 17.0            | .           |
|             | - of man-made fibres         |                      |         |                 |             |
| 61069000    |                              | 18.3                 | 130.0   | 17.0            | .           |
|             | - of Other textile materials |                      |         |                 |             |

<sup>23</sup> US Commercial Service, "Export Licenses, Standards and Legal Considerations". Export.Gov. <http://www.export.gov/mrktresearch/index.asp>

<sup>24</sup> Chinese Office of Customs. "Customs Tariff of Import of the People's Republic of China". China Customs Information Network. <http://english.china-customs.com/customs-tax/>

| Tariff Item | Goods Description  | Import Tariff Rate |         | VAT Rate | Excise Rate |
|-------------|--|--------------------|---------|----------|-------------|
|             |  | M.F.N              | General |          |             |
| 61041100    |  | 19.4               | 130.0   | 17.0     | .           |
|             | - Suits:<br>-- of wool or fine animal hair   |                    |         |          |             |
| 61041200    |  | 17.5               | 90.0    | 17.0     | .           |
|             | -- of cotton   |                    |         |          |             |
| 61041300    |  | 25.0               | 130.0   | 17.0     | .           |
|             | -- of synthetic fibres   |                    |         |          |             |
| 61041900    |  | 19.4               | 130.0   | 17.0     | .           |
|             | -- of Other textile materials  |                    |         |          |             |
| 61042100    |  | 19.4               | 130.0   | 17.0     | .           |
|             | - Ensembles:<br>-- of wool or fine animal hair   |                    |         |          |             |
| 61042200    |  | 17.5               | 90.0    | 17.0     | .           |
|             | -- of cotton   |                    |         |          |             |
| 61042300    |  | 25.0               | 130.0   | 17.0     | .           |
|             | -- of synthetic fibres   |                    |         |          |             |
| 61042900    |  | 18.5               | 130.0   | 17.0     | .           |
|             | -- of Other textile materials  |                    |         |          |             |
| 61043100    |  | 18.3               | 130.0   | 17.0     | .           |
|             | - Jackets and blazers:<br>-- of wool or fine animal hair                                   |                    |         |          |             |
| 61043200    |  | 16.0               | 90.0    | 17.0     | .           |
|             | -- of cotton   |                    |         |          |             |
| 61043300    |  | 19.0               | 130.0   | 17.0     | .           |
|             | -- of synthetic fibres   |                    |         |          |             |
| 61043900    |  | 18.3               | 130.0   | 17.0     | .           |
|             | -- of Other textile materials  |                    |         |          |             |
| 61044100    |  | 18.3               | 130.0   | 17.0     | .           |
|             | - Dresses:<br>-- of wool or fine animal hair   |                    |         |          |             |
| 61044200    |  | 16.0               | 90.0    | 17.0     | .           |
|             | -- of cotton   |                    |         |          |             |
| 61044300    |  | 19.4               | 130.0   | 17.0     | .           |
|             | -- of synthetic fibres   |                    |         |          |             |
| 61044400    |  | 18.3               | 130.0   | 17.0     | .           |
|             | -- of artificial fibres  |                    |         |          |             |
| 61044900    |  | 18.3               | 130.0   | 17.0     | .           |
|             | -- of Other textile materials  |                    |         |          |             |
| 61045100    |  | 16.8               | 130.0   | 17.0     | .           |
|             | - Skirts and divided skirts:<br>-- of wool or fine animal hair                             |                    |         |          |             |
| 61045200    |  | 14.0               | 90.0    | 17.0     | .           |
|             | -- of cotton   |                    |         |          |             |
| 61045300    |  | 18.3               | 130.0   | 17.0     | .           |
|             | -- of synthetic fibres   |                    |         |          |             |
| 61045900    |  | 16.8               | 130.0   | 17.0     | .           |
|             | -- of Other textile materials  |                    |         |          |             |
| 61046100    |  | 18.3               | 130.0   | 17.0     | .           |
|             | - Trousers, bib and brace overalls, breeches and shorts:<br>-- of wool or fine animal hair |                    |         |          |             |
| 61046200    |  | 16.0               | 90.0    | 17.0     | .           |
|             | -- of cotton   |                    |         |          |             |

The tariff rates for other clothing accessories, knitted or crocheted; knitted or crocheted parts of garments or of clothing accessories:

## Shipping

Shipment is the main part of logistics, since the cargo is regarded as the core investment.

| Tariff Item | Goods Description  | Import Tariff Rate |         | VAT Rate | Excise Rate |
|-------------|--|--------------------|---------|----------|-------------|
|             |  | M.F.N              | General |          |             |
| 61171000    | - Shawls, scarves, mufflers, mantillas, veils and the like | 16.8               | 130.0   | 17.0     | .           |
| 61172000    | - Ties, bow Ties and cravats                               | 16.8               | 130.0   | 17.0     | .           |
| 61178000    | - Other accessories  | 16.8               | 130.0   | 17.0     | .           |
| 61179000    | - Parts  | 16.8               | 130.0   | 17.0     | .           |

Only with the goods landing on the mainland safely could the investor start her business in China. The shipping company plays a critical role in the whole shipping process. Therefore, finding a qualified shipping company is the first thing the investor needs to do.

## Shipping Company

China Shipping Container Lines Co. Ltd. (CSCL) is owned by the China Shipping Group. CSCL is principally engaged in container transportation and related diversified business ventures. These involve the container transportation business, ship leasing, cargo booking, transportation customs clearance, warehousing, container yards, container manufacture, repair, sales, trading and other fields. Founded in Shanghai in 1997, the company has been ranked the world's sixth largest company in terms of carrying capacity in dollars. It was also the first shipping company in China and now dominates the Chinese container shipping industry.

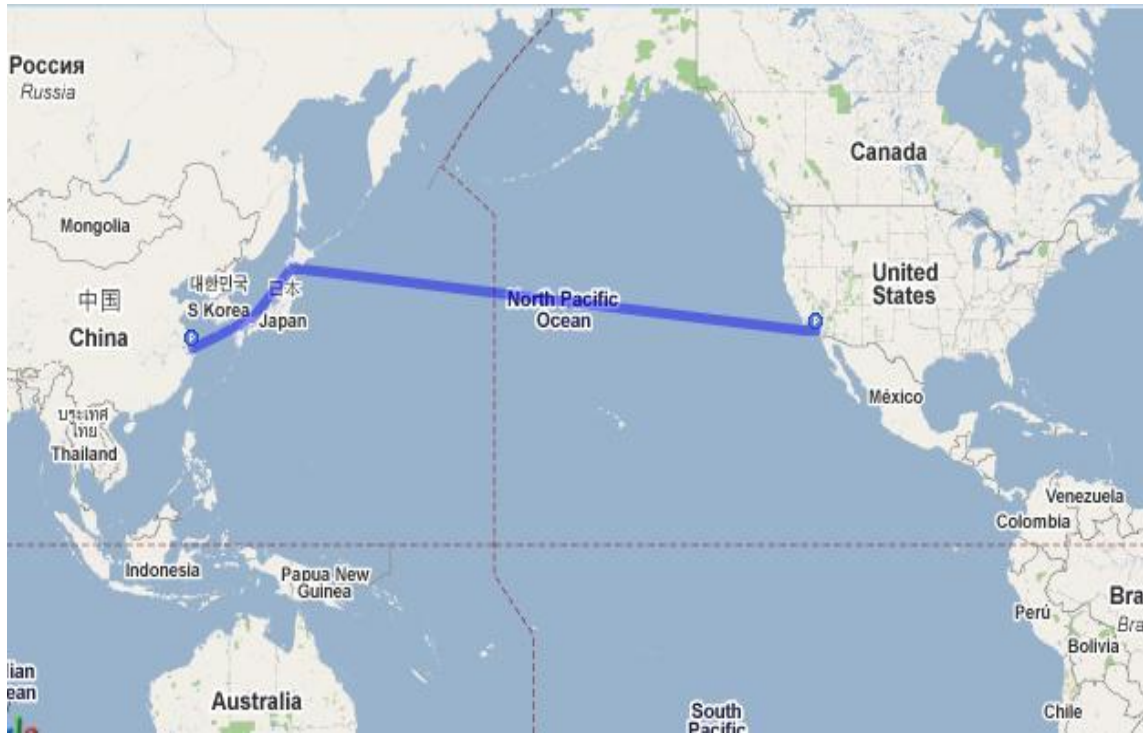
CSCL has a modern, large-scale, rapid, and young fleet of 136 ships. Its overall carrying capacity is about 350,307 containers. Each of its 52 large vessels has a carrying capacity of more than 4,000 containers and averages an age of only 1.9 years. The advantages of fast delivery, high efficiency, and low-cost make CSCL more competitive in the international shipping container industry. The firm has opened up 10 international and domestic container ship routes. Chinese internal trade has increased along with the increase in foreign trade from Chinese ports to Japan, Korea, Southeast Asia, Australia, Europe (Mediterranean), the Americas, West Africa, and the Persian Gulf. Among these routes, the route to the United States has 30 container ships dedicated to it alone. CSCL conducts business in over 40 Chinese inland points, and also has a market share of more than 50 percent in Chinese domestic trade routes<sup>25</sup>.

## Shipping Lane

Once the exporter finishes all the required work, such as packing, labeling, documentation, and insurance, the goods can be shipped from Los Angeles Port.

<sup>25</sup> "About CSCL Shanghai". China Shipping Container Lines CO., LTD.  
<http://www.cscline.com/zhweb/pages/en/aboutus/aboutus.asp>

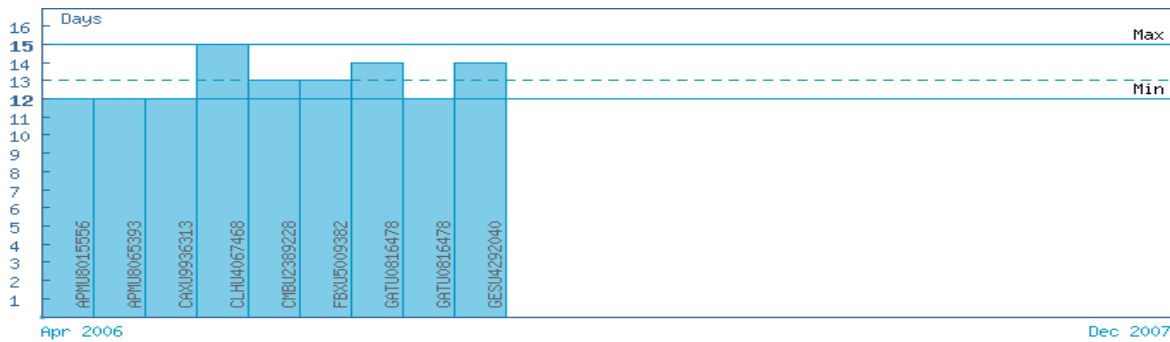
### The Los Angeles to Shanghai Shipping Lane



**Shipping Time**  
The following graph shows that the average transit time from Los Angeles to Shanghai

is 13 days, with a range of 12 to 15 days.

The shipping time is also an important factor to the business. The investor should take shipping time into consideration to ensure that items in the store won't be out of stock. Should that happen, customers would switch to substitutes, thus greatly affecting the sales revenue.



## Shipping Cost

The cost of tariffs are based on the following conditions:

*Cargo*

*Commodity: Garments, apparel, new*

*Equipment: Shipping Container*

|             |              |              |                     |                      |
|-------------|--------------|--------------|---------------------|----------------------|
| <i>Qty:</i> | <i>Size:</i> | <i>Type:</i> | <i>Weight (kg):</i> | <i>Volume (cbm):</i> |
| 2           | 20'          | Standard     | 20,000              |                      |

*Route*

*From location: Los Angeles, CA, US*

*To location: Shanghai, 31, CN*

*Receipt date: 06-Mar-2009*

*Validity*

*One or more freight elements are due to expire 25-Mar-2009.*

| Charge type   | Type   | Details | Valid to    | Local currency | USD               |
|---|--------|---------|-------------|----------------|-------------------|
| » <a href="#">Basic Ocean Freight (BAS)</a>             | Tariff |         | 25-Mar-2009 | 552.00 USD     | \$552.00          |
| » <a href="#">Bunker Adjustment Factor (BAF)</a>        | Tariff |         | 31-Mar-2009 | 90.00 USD      | \$90.00           |
| » <a href="#">Handling Charge - Destination (DHC)</a>   | Tariff |         |             | 300.00 USD     | \$300.00          |
| » <a href="#">Handling Charge - Origin (OHC)</a>        | Tariff |         |             | 780.00 USD     | \$780.00          |
| » <a href="#">Carrier Security Charge (SER)</a>         | Tariff |         |             | 12.00 USD      | \$12.00           |
| » <a href="#">Documentation Fee - Destination (DDF)</a> | Tariff |         |             | 125.00 CNY     | \$18.27           |
| <b>Total</b>  |        |         |             |                | <b>\$1,752.27</b> |

According to the above data, every 2 20'\*20' containers cost \$1752.27.

## Shanghai Port

The destination of shipment is the famous Yangshan Deepwater Port. Shanghai started the construction of the deepwater port in 2002. On December 10, 2005, the first phase of Yangshan

Deepwater Port was completed. Five 70-100 thousand tonnage berths of the first phase have been built and gone into operation so far. With a capacity to deal with over three million shipping containers each year, it offers all-weather service to the largest of containerships. Yangshan Deep Water Port, also houses the Yangshan Bonded Zone, which is the first of its kind in China<sup>26</sup>. It integrates all the functions as a port, a bonded zone, an export processing zone and a bonded logistics zone.

In the East Sea, about 30 KM away from Shanghai, there are two islands, Little Yangshan Island, and the other is called Big Yangshan Island. These two islands combined offer the largest shipping port in China.

### **Customs Declaration**

Next, the importer needs to go through the necessary clearance procedures for the imported goods. Prior to the landing of the goods, all documents and invoices for declaration purposes should be prepared and checked. Once the goods have landed at the port, the date of landing of the goods should be noted and the details of the shipment should be promptly checked by the Customs. In the event of failure to make customs declaration within 14 days from the date of landing, the imported goods will be subject to a fine from the 15<sup>th</sup> day onward at a rate of 0.3% of the price of the goods calculated on a daily accumulative basis<sup>27</sup>. The required documents for customs declaration include product manual, copy of letter of credit, quarantine certification and trade agreements. As soon as the customs duty demand note is issued, the importer should pay the customs duty and other relevant charges before the deadline. Upon inspection and release by the Customs, the goods should be promptly delivered to minimize warehousing or transfer charges.

### **Distribution Channel**

Once the goods are released by the Customs, CSLC will discharge and unpack the containers, and load the goods onto a truck. They will then be transported to the Grand Gateway Plaza, which is one of the biggest shopping malls in Shanghai. This plaza is located in the Xujiahui area, one of the most prestigious living areas, and a busy commercial and residential centre. Known as an upper class living area with many luxurious villas and upper class apartments, Xujiahui is very densely populated and has lots of traffic.

The shopping mall, Grand Gateway, has 7,000 square meters of shopping area stretched out across seven floors. There are also 94 elevators and almost 1,400 parking spaces in the mall giving it optimal accessibility<sup>28</sup>. Among the many stores in the mall are Gucci, Coach, Slice, and more that offer popular brand name merchandise.

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<sup>26</sup> Wang, Jian shuo. "Visited Yangshan Deep Water Port". Discover Shanghai.

[http://home.wangjianshuo.com/archives/20060420\\_visited\\_yangshan\\_deep\\_water\\_port.htm](http://home.wangjianshuo.com/archives/20060420_visited_yangshan_deep_water_port.htm)

<sup>27</sup> Customs Clearance for Imported Goods in China,

[http://en.ec.com.cn/article/tradingabc/encustoms/200901/713730\\_1.html](http://en.ec.com.cn/article/tradingabc/encustoms/200901/713730_1.html)

<sup>28</sup> Shanghai Times Square Property Management (Shanghai), "Shanghai Times Square". Shanghai LongXing Property Development Company Limited. <http://www.shtimesquare.com/en/shopping/main/aboutus/index.htm>

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