



China Currents



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Obama Gets Good Reviews in China

by Mary Lewis Grow and Rebecca Dong
Beijing



Views in China about America's new president range from the superficial ("He's so handsome!") to the thoughtful ("He's extremely smart but we worry that his policies may not help China"). While there is no unanimity in the reasons Chinese give for approving of the Americans' choice in the 2008 election, there does seem to be an almost-uniform lack of criticism of Barack Obama here that extends, often, to outright enthusiasm.

Several young women, graduate students at the University of International Business and Economics in Beijing, spoke effusively when the subject of Barack Obama was introduced. One, Yao Li, said, "He seems confident and competent to lead the U.S., and the reason is that he smiles a lot." Another, Sarula, said, "He is a peace-lover. [During the campaign] he said [that] if elected president, he would withdraw the majority of the armed forces [in Iraq] as soon as possible. It would be different from the policy of the Bush administration. He is making efforts to [have] his people live in a comfortable, peaceful environment."

Their friend, Liu Xin, liked the fact that Obama had succeeded on his own merit.

"U.S. presidents [often] come from a rich family, like Kennedy and George W. Bush," she said. "Often, they get help from their families when they begin their political careers. When they participate in a presidential campaign, their families support them, not only with money but also influence. I learned that Obama was born into a very ordinary family. His father divorced his mother when Obama was very young. Obama once lived a very difficult life. It can be said that he started from scratch...He strived to succeed bit by bit. In 2008, he participated in the presidential campaign [ran for president]. Depending on his wonderful speeches and his smile, he succeeded at last. During his whole career, he could not get any support from his family. All that he could depend on was himself. He started from the grassroots but ended as president. His story is a good example of the American Dream."

Yao Yao referenced her friend's view in her own reply:

"I think he is a very attractive man, with distinctive qualities. During the presidential campaign, he made a lot of amazing promises to the American people. We are looking forward to seeing how he will keep his promises in such a complicated and difficult international situation. The financial crisis is striking the whole world and Iraq is still not peaceful."

"My friend said that what Obama achieved depended on his own ability. I agree that he achieved a lot without [the benefit of] a prominent family background. We admire him for this. In China if you want to be successful, you must rely on relationships and networks. However, Obama cannot do without the support of the Democratic Party and his colleagues. You know, that's politics!"

A young man handing out flyers for his travel agency at the gate of the same university said that he thinks "Obama is very humorous." When asked if he thought that Obama would be good for the relationship between China and the United States, the young man hesitated, uncertain about whether Obama would act in China's interests. When asked why he harbored such fears, he said that he thought most leaders did what was best for their own country, and Obama would not be unique if he looked to U.S. interests first.

A Muslim restaurant owner in his forties gave verbal applause to Obama's stance on Guantanamo. Obama, he believes, is likely to release most detainees. He also expressed pleasure at Obama's conciliatory outreach to the Muslim world.

A shopkeeper in Dashenze, the cutting-edge arts neighborhood in the northeastern part of Beijing, smiled when asked for her views about the new American president: "He's very strong," she said, "and he will have to be if he is to help lead the United States out of its current crises."

A wide sampling of Beijing cab drivers offered a range of quick impressions: "Obama bi Bush hao." ("Obama is better than Bush.") Why? "Because he doesn't/didn't like the war in Iraq." Although "da Bush" (George Herbert Walker Bush) is always compared favorably with his son, "xiao Bush," at least one cab driver said that even "da Bush" liked war [the first Gulf War] too much. Several drivers gave a two-word answer: "Ting hao," "Very good," but were unable to say why they liked the new American president, some adding that they didn't really know enough yet about Obama to have an informed opinion.

One young Beijing cabbie was surprised to learn that Bush was no longer president, and, in fact, had left office three months earlier!

In Shanghai, a cab driver twisted around in his seat to be sure that his American passenger had understood his very positive opinion of Barack Obama. "I like him very much," he said, with strong emphasis. "He has a good heart."

Opinion in Shanxi Province differed little from that in the capital, even though opportunities for conversation with foreigners and exposure to the western press in Shanxi are extremely rare. The faces of a retired middle school principal and his wife lit up when asked about America's new president. They were very happy when

The same approval enjoyed by Obama in China appears to be widespread in other parts of Asia as well. Americans living in Djarkata report the near-ecstasy expressed by Indonesians following Obama's election. Travelers to a remote part of Myanmar encountered a street vendor, crouched on the ground in front of his cheap wares. Sensing the nationality of the visitors, the vendor looked up, flashed them a huge smile and, giving them a thumbs-up, said simply, "Obama!"

Tellingly, two cab drivers north of Bangkok had very different takes on Obama's election. One saw it for what it told him about the United States; one saw it in personal terms that he applied to his own circumstances. The first driver said that he was happy for the United States and what the election of a black man represented in terms of their history. The other said that Obama's election demonstrated that, with hard work, anything is possible. Before Obama's election, he might not have believed that his daughter would be able to overcome her background to make notable achievements. But with Obama's win, he said, he was able to urge his daughter to study hard in school because now he had dramatic evidence that individuals can rise above their circumstances and achieve anything and everything.

Obama was elected, they said. A young teacher of English and friend of the retired couple concurred, though none of the three could give issue-based reasons for their favorable impressions.

A rare criticism of Obama was expressed by a salesman in a small store in Pingyao, an old city in Shanxi famed for its well-preserved walls and watch towers and its former status during the Ming and Qing dynasties as the banking center of China. "He's too smooth by half," he replied when asked if he had an opinion of America's new president. Although unable to elaborate on this impression, and in spite of his store's prominent display of the iconic Shepherd Fairey portrait of Obama on a large package of matches (on sale in dubious company with other match boxes whose covers featured Hitler, Stalin, Che Guevara, and Mao), the young man's negative view was far from tentative.

Andrew Kaiser, a young American who has lived and worked for twelve years in Taiyuan, provincial capital of Shanxi Province, reported seeing an off-the-beaten-track shop named "Obama" even though its wares had no apparent connection to the new U.S. president. The naming of the store was, in Kaiser's view, most likely a marketing decision determined by Obama's widespread popularity.

Of three representatives of the Chinese media who offered their impressions of President Obama, two spoke very approvingly of him, but one echoed the reservations of the shopkeeper in Pingyao. Tao Libao, a former employee of CCTV, now in his thirties and running his own TV production company, said "When Obama talks in everyday life, he still talks as [if] making a speech to the public. I [feel] he might not know or be willing to expose his true feelings. So I feel he's not sincere, or he doesn't know what to do with the topic he's talking about."

The slightly older vice president of a Shanghai media group offered a much more positive take on the new U.S. president. Obama's energy, he believes, will kindle a corresponding energy in his compatriots, particularly among younger and middle-aged Americans. Younger people are more likely to be open to the kind of change that Obama represents and more willing to take a chance on going in new directions, said the Shanghai media executive. He expressed optimism about Obama's relationship with China and said that most Chinese are ready and willing to see him as a friend.



Forty-two-year-old film producer and former university professor, Wang Guangli, spoke of the youth, vigor, and confidence he sees in Obama, and he wishes the new president success. If Obama is not successful in addressing the huge problems that face the United States, Wang Guangli will not see his failure as a lack of competence but rather as a reflection of the enormous problems he is dealing with. And, he said, many of the Americans' difficulties are world issues as well.

Wang Guangli draws on his film and media background to assess Obama's star power, which he believes Obama to have in abundance, more than many movie stars. While Obama's charisma may cause some people to judge him superficial,

notes Wang Guangli, it may give him a greater platform for success. So far, he says, Obama has not disappointed expectations. Other charismatic presidents have turned out to be successful, he adds, citing Ronald Reagan and John F. Kennedy, among others.

Obama's youth may be one of his biggest assets, according to the film-maker. Young people are willing to learn, he says; they are flexible in dealing with conflict. And young leadership is capable of dealing with old problems in new ways.

With access to many media sources, Wang Guangli has had frequent opportunities to observe Obama on television. In fact, he notes, he has taken for his own use one of Obama's most popular slogans: "Yes, we can!"

He Xiangmin, an economist and university administrator currently serving as Vice President and Executive Director of the China Association for International Education, spoke thoughtfully about Obama and American politics.

Chinese believe, he said, that Democrats are better for their country during hard economic times, but they worry that Democrats often are more confrontational with China over issues of human rights and protectionism.

Traditionally, he said, it usually takes two to three years for a new Democratic administration to adjust its relationship with China.

But he is hopeful that Obama's learning curve will be shorter since, unlike Bush, who tried to tell the rest of the world what [the U.S. thought] they should be doing, Obama seems more inclined to work collaboratively and listen to others.

He believes that Obama is less likely to use war as an instrument of foreign policy and thinks there is greater world-wide trust that he would use war only as a last resort.

He Xiangmin is relieved that Obama seems to have softened his protectionist stance, which makes China more amenable to helping the U.S. with its imbalance of trade issues. China's agreement to use some of its excess foreign reserves to purchase \$10 billion worth of American goods will work to both China's and the U.S.'s benefit, since it helps reduce China's dollar reserves and will help stimulate the U.S. economy. Even though the recent agreement works to the benefit of both countries, He Xiangmin believes that it also is a reflection of trust and goodwill towards Barack Obama and a recognition of his desire to work well with China.

While Bush said, in effect, "Do as we say, not as we do; Obama shows greater respect for other people and other cultures," says He.

China knows, says He Xiangmin, that unless the U.S. recovers, there will be no global economic recovery, so its policies will reflect a desire for the economies of both countries to be strong. But, he added, China wants – and should have – a bigger voice in World Bank and IMF policy formation.

Another Chinese economist, a prominent and influential policy advisor, Zhang Jianye (not his real name) made different points when talking about Obama and his administration's relationship with China. Contrary to many of his friends who said that the United States would never elect a black man as president, this economist

predicted Obama's win, saying that he believed that the United States had already changed enough to break the racial barrier in its electoral politics. And he knew, he said, that Americans very much wanted a change from the Bush years.

In general, he said, Chinese have a very favorable impression of Obama, in spite of their gratitude to George W. Bush for honoring his commitment to come to the Beijing Olympics [and, although he didn't mention it, GWB benefited from the affectionate memories Chinese have of the first President Bush, who served as first U.S. envoy to China, though unofficially, after the breakthrough in U.S.-China relations].

Much like his fellow-economist, He Xiangmin, Mr. Zhang noted that new American administrations often start out by picking a fight with China. That Obama did not start off this way has pleased China, the South China Sea incident notwithstanding. He spoke admiringly of the restraint demonstrated by both sides during and after that incident and said that Obama's sending Secretary of State Clinton to China so early in his administration was a positive sign.

Mr. Zhang believes that the make-or-break issues between the U.S. and China will be economic, not military. He acknowledged China's complicity in amassing so much U.S. debt, saying that just as an individual should not continue lending to a friend who is already deeply in debt, China contributed to the problem by continuing to lend to the U.S. long after it should have been apparent that the U.S. was spending far more than it was saving and would have trouble repaying its loans.

He expressed particular concern about the issue of whether the U.S. repays China in inflated dollars or amounts that equal, in real value, the amount of China's loans. He believes that the U.S. is morally obligated to guarantee that its repayments will not erode the real value of China's foreign exchange reserves.

"Don't create China as an enemy," he counsels. China does not have a history of territorial expansionism, he argues, even in the past when its naval fleet dwarfed those of any other country in the world. And China does not want to see the hegemony of the dollar changed, though they may not like it. But they do not propose to change it.

As Obama goes forward, Mr. Zhang observed, he may need seasoned and experienced economic hands such as Lawrence Summers and Timothy Geithner, but he also should reach out to more new people who perhaps have not been as deeply enmeshed in the financial structures and institutions that have failed so badly.

It is important for both China and the U.S. that our new president succeed. While Obama's foreign policy is still unfolding, Mr. Zhang believes that he has made a good beginning in reaching out to other countries.

Ending on a note of hope, he added, "Americans are adaptable and learn from their mistakes."

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Taiwan Strait Security Challenges

by Albert Willner



The recent thaw in relations between mainland China and Taiwan shows encouraging signs of producing results. Efforts by China's President Hu Jintao to reach out across the Strait, Taiwan's presidential election last year of Ma Ying-jiou and increasing economic ties have further improved communications and set the stage for even greater cooperation. Responses by the United States and neighboring states to improvements in cross-Strait relations and political change in Taiwan have generally been positive. Yet underlying these developments are pressures and suspicions that could exacerbate rather than relax tensions.

To be sure the transition in Taiwan from the nationalistic Democratic Progressive Party's Chen Shui-bian to the Kuomintang's Ma alone meant that the cross-Strait environment was bound to improve. After eight years of relatively continuous verbal challenges on the diplomatic, political, military, and information fronts, both sides were well positioned to take advantage of change brought about by the election of a new government in Taiwan. Following Ma's inauguration in May 2008, both sides have moved quickly to take advantage of new opportunities. The U.S. and others also breathed a sigh of relief that the 2008 election results would set the stage for easing of tensions.

Beijing and Taipei quickly agreed to address issues of importance to domestic and international audiences. Starting in July 2008, direct flights between China and Taiwan increased threefold, reducing costs and travel time for business people and tourists. Direct sea transport has expanded as has mail service, allowing for increased economic and cultural exchange opportunities. Interest in developing mechanisms for food safety oversight and resolving problems has gained traction to address, in part, concerns about tainted mainland China produced goods.

The two governments are looking to broaden exchanges in other areas as well. Beijing is allowing students, professional actors and state journalists to attend school, perform on stage, and work for extended periods in Taiwan. Top Chinese bureaucratic officials, including some military officers, have been given greater latitude to visit Taiwan although, to date, official visits by Chinese defense officials have been limited. An unprecedented call by President Hu for China-Taiwan military-to-military talks may also create new opportunities for engagement, although Ma has said serious military talks are not a priority at this point.

Both sides have sought to reinforce existing venues and foster new dialogue to advance the relationship. Beijing's leadership recently restated its commitment to using the Cross-Strait Economic, Trade and Cultural Forum by holding talks with Taiwan representatives in Shanghai in December 2008. The Forum's three areas are receiving the most attention in part because they are generally supported and less controversial among domestic constituencies and offer the best chance of early and visible success. Both governments can rightly point to the increased exchanges and dialogue as having enabled greater cross-Strait economic and cultural

communication and gains in these areas help to assuage concerns about the potential for conflict.

Indeed, China has also indicated that Beijing would be amenable to working with Taipei to expand the latter's international space. In late April 2009, Ma announced that Beijing would not object to Taiwan's participation as an observer in the World Health Organization, and specifically in its governing World Health Assembly. Taiwan has agreed to use the name "Chinese Taipei" and, while additional details continue to be worked out, this action indicates another positive step in the relationship. Underlying these advances, however, fundamental challenges remain.

The growing Chinese military buildup in the air, at sea and on land coupled with Beijing's refusal to renounce the use of force against Taiwan has the potential to detract from gains being made in other areas. China's development of combat aircraft carrying missiles with a greater range than any Taiwan equivalent, its expanded submarine program, announced interest in developing an aircraft carrier, and ever increasing number of improved missiles opposite Taiwan all continue to raise serious concerns and heighten the threat to peace in the region. Regular training missions by Chinese fighters, ships and submarines in and around the Taiwan Strait add to insecurity and increase the chance of an accident or a miscalculation. The lack of transparency accompanying this buildup, highlighted yet again in the most recent U.S. Defense Department China Military Power Report, further raises concerns in Taiwan and elsewhere not only about Chinese capabilities but about how Beijing expects to use its emerging military power. China's 2009 White Paper on Defense, designed to address transparency concerns and released on U.S. President Barack Obama's inauguration day, was widely viewed as insufficiently addressing questions about either Chinese capability or intent.

The military growth and lack of transparency do little to calm concerns of the United States and neighboring states. The potential for accidents and confrontation in the air and at sea remain high not only in the Taiwan Strait but with others as debate over the China's stated offshore zones and disputed islands remain unresolved. This was recently demonstrated again in March 2009 during a series of incidents in international waters in the South China Sea, when five Chinese ships and a Y-12 surveillance aircraft sought to repeatedly intimidate a U.S. research vessel by challenging it and trying to interfere with its freedom of movement. China claims a 200 nautical mile Exclusive Economic Zone, 188 miles beyond the internationally accepted 12 mile sovereign offshore limit. These incidents, coming just two weeks after the reopening of U.S.-China military to military talks, highlight the willingness of Beijing to take risks in order to make claims in favor of its perceived economic space and challenge others on the high seas. This may be due in part because the Chinese leadership feels the current international political, financial and diplomatic environment is favorable to taking such actions and that they will elicit little reaction. China's continuing disputes with Taiwan, Vietnam, the Philippines, Brunei, and Japan over various islands in the East and South China Seas increase the possibility of a crisis in the region, always with potentially far reaching implications.

Across the Strait, in addition to the external threat, President Ma faces internal defense challenges in Taiwan as well. The Taiwan government recently released its first ever Quadrennial Defense Review (QDR) highlighting the increasing international clout of mainland China at the expense of Taiwan, the need for Taipei to convert to an asymmetric doctrine to counter Beijing and the desire for greater defense transformation and organizational innovation of its own forces. The document also

states that while security tensions in the Taiwan Strait are gradually diminishing, mainland China continues to aggressively develop military weapons and systems and is conducting a three front war on the legal, media and psychological fronts, placing continuous pressure on Taiwan's interests. Taipei's stated defense priorities remain focused on war prevention and transformation.

Ma's plan to advance a proposal initiated by his predecessor to convert to an all volunteer force during the next five years brings with it the need to make some hard choices about how best to recruit and retain this new force as Taiwan has relied on draftees to do much of its soldiering over the past sixty years. At the same time, there remains much discussion within Taiwan as to how best to meet the China challenge. In late 2008, a debate arose between the Taiwan National Security Council and senior leaders in the Ministry of Defense about whether to focus more on an Army-centric hard shell defense of the island or whether to continue developing a joint air-naval-ground defense plan that had received extensive attention during the previous decade. The outcome of this debate has significant strategic implications in how Taiwan intends to defend itself, particularly in a place where time and space are extremely limited. Part of these debates centers on how best to make use of constrained resources, maintain public support for the military and properly adapt its defense while at the same time reaching out across the Strait. These issues are significant not only as Ma looks to rethink Taiwan's strategic plan but also as the executive branch deals with challenges from a legislative body balancing competing priorities. The deliberation process and increased accountability demanded of Taiwan's defense officials also reduce the chances that budget and strategic direction issues will be quickly resolved.

Recent news of a pay for promotion military scandal, independent prosecutor investigations of Taiwan defense contractors, military accidents, charges of Taiwan Navy personnel involvement in the murder of a prostitute, and the attempted suicide of the Taiwan's former top Marine have all affected morale and diverted attention of senior officials from the government's defense initiatives. As the Defense Ministry leadership works to respond to these investigations, Taiwan's ability to focus on QDR priorities and readiness could be negatively impacted. As serious discussions increase across the Strait, the need to have a strong and unified voice emanating from Taipei is exceedingly important. In a crisis, such a unified voice would be critical.

How best to resolve core sovereignty issues will remain the major challenge in the Taiwan Strait. Whether the relationship continues to improve or lurches toward crisis will depend heavily on what mechanisms are developed, accepted and implemented to address real areas of difference. China's concerns about continued U.S. arms sales and support for Taiwan's defense needs and Beijing's willingness to push back to solidify its own sovereignty claims bring potential risks to peace in the region. Taiwan's external and internal challenges in addressing broad defense requirements and Ma's own need to walk a political tightrope by reaching out to mainland China without appearing to sell out Taiwan interests offer additional opportunities but also potentially raise risks and increase strain.

The role of the United States, Japan, the Republic of Korea, Singapore, Australia, the Philippines and others in the region choose to play, especially as states adapt to the current global economic realities, will no doubt have an important impact on the outcome. These countries, through bilateral and multilateral exchanges and organizations, are working toward improved defense cooperation as shown by

actively pursuing military talks, disaster relief, search and rescue training and broader exercise programs aimed at meeting common interests and challenges. Timely signals and exchanges among the regional actors that address communication and in particular how best to deal with a crisis will be important in allowing the work of improving cross-Strait ties to continue. Mainland China and Taiwan are clearly seeking to advance common interests critical to maintaining peace and prosperity in the region. As Beijing and Taipei move forward, keeping the peace in the Taiwan Strait and surrounding areas will require careful attention and a renewed commitment by all involved.

In the end, significant questions remain which could dramatically affect process and outcome. For Beijing, if the end goal remains unification, what is the best way forward? President Hu and the senior leadership may be willing to work with Taipei and to assuage international concerns by taking a slow and measured approach to fully resolving differences, including possibly even an interim peace agreement. Would this approach be acceptable to those in China who are interested only in Taipei's capitulation, possibly along a much faster timeline? What kind of additional pressure does this place on a Communist Party already deeply concerned about maintaining its legitimacy in China? In Taipei, what are President Ma's own short and long term goals, and will he be able to make a supportable case within his own party and the broader Taiwan electorate? Will the Taipei leadership be able to craft a plan that addresses complex Chinese, American and neighboring states' interests and concerns? Will change in the status quo create its own momentum in fueling even greater expectations, or will it cause greater resistance to such moves? Fundamental change across the Strait clearly starts with realistic goals being set in Beijing and Taipei in line with their strategic interests. Achieving preferable outcomes will most likely, however, require managing expectations and interests well beyond the immediate control of both capitals.

Albert Willner is Associate Dean, School of Liberal Arts, Georgia Gwinnett College.

View from China: Is there a consumption problem?

by Penelope B. Prime



China saves, the U.S. consumes—or so the headlines say. Many analysts (including this author) have written about China's high savings rates and therefore low consumption, which reinforces China's dependence on exports for its growth.

The problems with this dependence are that China has been so successful with exports that most major buyers cannot absorb more of them and will not be a source of future growth, and secondly that such high exports make China's economy vulnerable to the business cycles of other parts of the world. Even before the current financial crisis, which has caused exports to decline substantially, there was a vigorous debate within China about how to stimulate domestic demand to get around these problems.

To date, very little has changed in China in terms of policy or institutions to address the domestic demand issue in sustainable ways. To be fair, the global financial crisis has caught the attention of policy makers everywhere, putting short term fixes out front. Stimulus packages are popular, and China has its own version, which in essence means funding infrastructure projects combined with low cost loans via the banking system for other government construction projects. Subsidies for rural families to buy consumer goods and a tax cut on auto sales have also been made available, but there is little evidence that many have taken advantage of the offers. The stimulus may be working to keep growth afloat, but in terms of changing the domestic-external demand imbalance, something more will be needed.

So what might that be? Thinking through this question from the view of a typical family in China sheds some light on the nature of savings and consumption in this transition economy. Savings is defined as earned income minus consumption in a given year. Three aspects of how a family participates in China's impressive growth and development could be thought of as: 1) access to a better life; 2) worries about losing that better life; and 3) defining what it means to have a "better life." The focus here is an average family, not one that has ties to government or party that provides access to exceptional opportunities. Some people in this second category live very well indeed, but their choices about employment, spending and saving cannot explain the overall trends in China's economy.

Access to a better life



If a person has a wage paying job, i.e., a formal job that earns a monthly paycheck, there is a base wage that has risen with growth in China's economy but still is considered basic pay. For an employee working on the line in a factory near Beijing, for example, that base pay averages 1,200 RMB to 2,000 RMB per month (\$177 to \$294). In addition, most people receive an annual bonus at Chinese New Year's that equals one month's pay or more. Many people do extra jobs or work overtime for additional

pay. In addition, both spouses in a married household are likely to work, increasing the options and income.

In the countryside, if a farming family is able to raise and sell a cash crop or have a small, side business such as trucking, a small store or restaurant, they can do better than subsistence. If a family member ventures out and finds a wage paying job in the city, the family usually receives part of this income as well, especially once a year at Chinese New Year's when the family member returns for a week or more.

Another way an average person can share in China's growth is to speculate in the domestic stock market. Since dividends are not paid on shares, making money in the market means being lucky enough to buy low and sell high, and hence the stock market is not considered a long term investment. Some people have made extra money—sometimes substantial amounts—in the market. One difference between

families in China and families in the U.S. in this regard is that Chinese families usually think of their market investments as money that is not essential for living. The market is for making an extra gamble that may or may not pay off, if they have money to lose. They continue to hold savings in cash in bank accounts rather than using their basic savings to buy stocks.

Borrowing to spend is not common or easy. Basic wage or earnings generally cover basic necessities and any extra income earned via bonuses, second jobs, remittances or stock market winnings are most likely treated as a lucky addition, and according to economic theory, a higher proportion of this income is probably saved as compared with the basic monthly income, at least for some time. Once savings has accumulated, it is often spent on big ticket items such as a condo or a car, a child's tuition or one's own or a family member's expenses after retirement.

One way that a generation of people came into wealth in China is related to housing reform. Before reform, people working in urban areas were assigned apartments by their employers. These apartments were owned by the enterprises or institutions they worked for, and so if they paid rent, it was very low. The apartments were part of the benefit package supplied under the former socialist system. As a first step in housing reform, government enterprises and institutions sold residents their apartments at highly subsidized rates. For example, a one bedroom apartment in Beijing now worth \$100,000 might have cost just \$10,000.

While some people have sold their condos, casual observations suggest that most have not. In fact, many families have saved money and then bought a bigger condo, keeping their older ones as an investment, to rent out, sell later or hold for their child when they will need a place to live to start a family. Surprisingly, many families earning basic wages of even 5,000 RMB (\$735, or \$1470 if both spouses work) per month own 2 to 5 condos, sometimes in multiple cities. The value of this real estate must be enormous, and represents "locked-in" savings that is not currently available for consumption.

People from small towns, inland areas or the countryside often create their own wealth by moving to urban areas to try their luck with a small business. Fast food stands, flower stalls, a vendor at Beijing's famous Hongqiao or "Pearl" market, are some examples. Local residents also open restaurants and other family companies. These companies need to bid for a license or permit to locate on a particular street or have a booth in one of the markets. They can often make a decent living in terms of generating income for their families and investors this way.

The Uncertainties of a Better Life

However, the uncertainties built into these new income generating opportunities are high. Change in China is very fast. Policy changes affect how one does business and neighborhoods can be demolished for the next high-rise. Both can quickly end the fortunes of the small business owner. The lesson is to earn as much as you can as fast as you can and save most of it so you can start again when needed. Every several years neighborhoods can change almost completely in terms of the restaurants and stores that are open, the vendors that are around selling snacks and fruit, and basic services such as dry cleaning and phone cards. Whole streets of businesses have disappeared within days when a new construction project is begun. With the lack of insurance policy options, saving for these rainy days must be a priority for most people.

Other major uncertainties for families that are officially recognized and supported by research, is the need for families to save for unexpected health expenses, education and retirement. The previous versions of these social services and systems under the time of Mao's leadership were eroded with reforms, and China's policy makers are in the midst of recreating them for their modernizing society. In the meantime, however, families indicate that saving for these future expenditures is one of the main drivers of a high savings rate from a household's point of view.

Of course, the more that people rely on the private sector rather than state enterprises for their employment, the more uncertainty is introduced into their lives. The insecurity associated with market business cycles is something that we understand in the U.S. even if households underestimate the risk at times. In China, however, these cycles are a new aspect of life that is part of the transition to a more market-oriented economy.

Defining a Better Life

In the midst of all the discussion of high savings and low consumption, the middle class in China seem to feel that they have much of what they need. Families eat out at restaurants many nights in a week; they have plenty of clothes; they are saving for or have already purchased a car; they have a place (or several) to live, they have taken more vacation trips than their parents could have even dreamed of, both within China and abroad. And so what do they want? Not much, it seems—except for intangibles such as good health, excellent education for their children, and security in retirement.

Creating a dynamic, domestic market would require a competitive, innovative business environment where companies would seek out and create home market niches based on new products, services and entertainment that would appeal to the Chinese consumer or business end-user or that would help reduce the uncertainties currently build into life today. This, in turn, may require more economic activity to be service and private led, rather than manufacturing and state led. Financial reform that allows for loans for small and medium sized companies, and for individuals and families, would help, as would new financial products such as basic insurance options for home, life and health.

In rural areas there are many families that cannot join the middle class with their current income options. The combination of land that is locked into state ownership and so cannot be sold to finance new livelihoods, and the difficulties of moving one's residence due to the household registration system keeps these families from gaining anywhere near as much as those who are lucky to live in urban areas and are educated. Chinese statistics put the average annual income of the 727 million rural residents at 4,761 RMB or \$700 per year (China Daily Business Weekly May 18-24, 2009, p.12).

Making Buyers Out of Savers?

Some of the factors that are suppressing consumption in China today may be temporary. The locked savings in housing, for example, should be whittled away as families take advantage of their investment for their children, retirement or other big ticket items. Consumption behavior is also known to lag increases in income, which

has happened for many families in China for many years. As growth rates level out, consumption spending is likely to catch up. And everyone talks about the younger generation and their willingness to spend.

The big question is whether major policy and institutional change will be required to stimulate China's domestic market, and whether these changes are feasible. Reforms might include building a competitive financial services sector, revaluing the Chinese currency that would make exports relatively expensive and imports relatively cheaper, ending the household registration system, and adding a property tax while lowering the value added tax that keeps the prices of goods high. Or will the political base of the production sector dominate such that production-oriented policies will continue? Hopeful signs exist. Reforms targeting benefits to the average person, such as the new labor contract law, have been designed and implemented. Others such as a national pension system and requiring listed companies to pay dividends to shareholders are in the works.

On top of these moves, ironically, the current economic crisis, bad as it is for everyone, may give China a push to move aggressively to make the necessary changes to build a domestic demand engine. If there was any question that continued export growth was questionable, the current global business environment has shown China the vulnerabilities of their past export dependent growth.

Penelope Prime is Professor of Economics at Mercer University, Atlanta, and director of the China Research Center. She participated in the Carleton College Beijing Seminar and the Mercer University EMBA International Residency in China this spring, and would like to thank the students on these programs for their enthusiasm, curiosity and insights, all of which added greatly to the content of this article.

Building a Comprehensive Strategy for China's Environmental Clean-up

by Baogang Guo



Last year's Beijing Olympic Games witnessed an breathtaking makeover of the city's environment. Beijing's sky became blue almost overnight. Anyone who had visited the Chinese capital just a few months before would be amazed to find out that the thick smog that hung over the city disappeared nearly completely, like a miracle. However, what they did not know was how much effort the Chinese government had put into the environmental cleaning-up in order to fulfill its promise to the International Olympic Committee (IOC) about environmental protection. It is estimated that China spent nearly \$10 billion on improving Beijing's environmental quality. Many drastic measures were taken in the months prior to the Games. Coal-fired power stations in the city were converted to gas-burning stations. More than 1,400 old gas stations and 10 oil depots were closed down for good. Another 200 major polluting factories were ordered to shut down

temporarily. Capital Steel and Iron, one of the largest steel makers in China, was ordered to relocate its mills to a new industrial park far away from the capital city. Car drivers were told to drive only on alternate days according to their car's tag numbers. Despite the measures, the air remained foggy and unstable just a month before the games. The authorities ordered an expansion of the strict air quality control measures to cities adjacent to Beijing and asked some of their heavy-polluting factories to shut down their production operations temporarily as well. As a result, during the first half of 2008, Beijing's sulfur dioxide emission level decreased nearly 13% compared with the same period of 2007. During the month of August when the games were held, the air quality in Beijing was rated as excellent for almost half of the month, and the remaining days were rated as good.

These massive clean-up efforts are unparalleled in the history of the Olympic Games. They demonstrate not only the determination of the Chinese government to meet its Olympic obligations but also the ability of the authorities to use administrative muscle to fight pollution. After years of liberal reform, it is noteworthy that the state still has so much power at its disposal. This administrative capability is almost beyond imagination in a typical western democracy. However, the desire to present to the world a clean image is only part of the story. Since 2005, "scientific development" has become the new buzz phrase in China's political lexicon. Leaders in Beijing have apparently realized that the single-minded pursuit of economic growth at the expense of environmental and human development is not sustainable. Indeed, China has already paid a huge price for decades of neglect in its environment. In just a few decades, China quickly became one of the most polluted countries on earth. Air was filled with dirty particles, rivers and lakes became filthy and stinky, and underground water became undrinkable. Industrial pollution contributed greatly to the environmental nightmare. A report issued by the World Bank on China's environment points out that "Many of China's waterways are close to biological death from excessive discharge of organic pollutants. In many urban areas, atmospheric concentrations of pollutants such as suspended particulates and sulfur dioxide routinely exceed World Health Organization safety standards by very large margins. Hundreds of thousands of people are dying or becoming seriously ill from pollution-related respiratory disease each year." As a result, sixteen Chinese cities were on the World Bank's most polluted city list, and Linfen City in Shanxi Province was cited as the world's most polluted city in 2007. The Chinese government has no choice but to develop a comprehensive strategy to toughen its environmental policy.

Beijing's clean-up prior to the Olympic Games followed the traditional "command-and-control" approach involving the identification of sources of environmental pollution, setting emission standards, inspecting for non-compliance, and forcing the shutdown of polluting factories. Since 2005, the State Environmental Protection Administration (SEPA) has launched several waves of an environmental "New Deal." On January 18, 2005, SEPA ordered 30 major construction projects, mostly new power plants, to suspend construction for lack of required environmental impact reports. Among the projects put on hold were the 12,600 MW Luoqi Du Hydroelectric Power Station and the underground Hydroelectric Power Station connected with the Three Gorges Dam project. On January 27, 2005, SEPA launched another strike. This time, 46 existing power plants were ordered to install SO₂ reduction devices within a fixed time period. Three subsequent "storms" followed. On February 7, 2006, SEPA announced that it would inspect 127 chemical projects. On January 7, 2007, SEPA used a regional ban on new investment projects against four cities and four enterprises for their violations of some regulatory requirements. On July 3, 2007,

SEPA put the ban on new projects for six cities, two counties and five industrial parks to punish their pollution to the Yangtze, Yellow, Huai and Hai rivers. This new power of "limiting approval of area development projects" gave the state environmental agency and local environmental protection bureaus veto power on new construction projects.

Aside from taking these drastic administrative measures, Chinese environmental regulators are also actively seeking a new market approach that emphasizes the use of incentives such as emission quotas, pollution levies, emissions trading, green credits, green capital markets, ecological compensation, and environmental liability insurance to force enterprises to comply with environmental standards. This approach calls for an active role of the state in the creation of a system of environmental economy but not on direct interference with business decisions. Since 2008, the government has shifted its focus from punishing polluters to institution building. As part of the environmental "New Deal," SEPA introduced a number of new systems to help enterprises and consumers deal with environmental disputes. First, SEPA issued a circular about liability insurance on environmental pollution. The hope is that the insurance system can help enterprises deal with monetary compensation in cases of environmental disaster without causing too much financial burden on an enterprise. It also is designed to help protect the interest of victims and prevent the government from having to pay compensation in pollution cases. A pilot program has been implemented in several provinces. It is hoped that by 2015 the trial will be completed, and the system will be promoted nationwide.

Second, SEPA has initiated a new pilot project on emissions trade. The concept of emissions trade was introduced to China by Dr. Daniel Dudek, the chief economist of the American-based Environmental Defense Fund. In September 1999, the fund signed an agreement with SEPA to complete a pilot project on total emissions control (TEC) and emissions trading under the framework of Sino-U.S. cooperation. Benxi and Nantong were selected as the first demonstration cities. In September 2001, the first sulfur dioxide emissions trade was successfully completed in Nantong, Jiangsu Province. In March 2002, SEPA and the fund cooperated in launching the "4+3+1" project, an endeavor to initiate an integrated TEC and emissions trading policy in Shandong, Shanxi, Jiangsu and Henan provinces, and the cities of Shanghai, Tianjin and Liuzhou, along with the China Hua Neng Group. Each of the jurisdictions completed quota allocations, trading regulations and policy demonstrations. In December 2007, Jiaxing city in Zhejiang Province established China's first emissions trading center. Beijing and Tianjing are in the process of setting up the nation's first carbon trading centers. Shanghai and Beijing have also established Environmental Energy Exchanges.

Additionally, the Chinese government is beginning to incorporate cooperative governance into its grand strategy of environmental regulation. This approach emphasizes transparency of decision making and participation by civic organizations. In 2004, SPEA issued a circular on the administrative hearing process regarding environmental protection issues. The scope of the hearing ranges over small, medium and large projects that have an impact on the environment. In 2005, the Beijing government decided to invest 30 million yuan (\$4 million) to install plastic at the bottom of a lake at Yuanmin Yuan, the remains of the Qing Dynasty imperial garden widely known as the Summer Palace, in order to prevent water leakage and save money. SEPA responded to the public criticism of the project by calling the first public environmental hearing on April 13, 2006. Seventy-three representatives were allowed to attend the hearing, and many of them were professors and experts.

Several representatives from non-governmental organizations (NGOs) also appeared in the hearing. SEPA eventually decided to order the project to uninstall the finished anti-filtration plastic film at the lake.

Beginning in 1998, the World Bank and SEPA established GreenWatch, a public disclosure program for polluters. It uses the Environmental Performance Rating and Disclosure System to rate firms' environmental performance from the best to the worst in five colors -green, blue, yellow, red and black. The ratings are disseminated to the public through the media. The pilot program was initially tried in Zhenjiang, Jiangsu Province, and Hohhot, Inner Mongolia, with funds from a grant from the Bank's Information for Development Program. After pilot GreenWatch projects proved successful in 22 Chinese municipalities in seven provinces, the Chinese national government decided in November 2006 to extend the program to every city in the country by 2010.

Environmental NGOs and activists have played a role in this area as well. Currently, there are about 2,000 registered environmental groups in China. Many more are probably unregistered. A good example of cooperation among government, NGOs, entrepreneurs and citizens is Alxa's sandstorm treatment project. Alxa is located in the west of Inner Mongolia, which is the main source of China's sandstorms in northern China. The ecological deterioration in the area has threatened the livelihood of 196,300 herdsman and created many ecological displaced persons. On June 5, 2004, 100 Chinese entrepreneurs pledged to donate 100 million yuan (\$70 million) to the Environmental Protection Public Welfare Fund to Control Sandstorms. The Alxa SEE Ecological Association was established, based on this initiative. The SEE Ecological Association has engaged in several pilot projects, including the "alternative energy and natural haloxylon woods zone protection" project and the "improving the sustainability of ALEXA ecological migrants" project. Its investment models call for multilateral cooperation on the part of the association, government agencies, herdsman, entrepreneurs, and international organizations. The government of Alxa Meng (Meng is an administrative unit seen in Inner Mongolia) launched a "migration and transfer, centralized development" project to relocate herdsman from Helan Mountain and Tengger to Barunbielli Town of Alxa and built 100 greenhouses for them. The SEE Ecological Association was invited to be a partner of this project, and provided technology training to herdsman and support for the relocation.

International non-governmental organizations (INGOs) also have been closely cooperating with the Chinese government in recent years in the area of environmental protection. Since the mid-1990s, the number of international NGOs and philanthropic foundations conducting or funding environmental conservation campaigns has grown at an extraordinarily rapid pace. While the number of INGOs with offices in China has grown slowly, the size and resources of these offices has grown dramatically since 2000. The World Wildlife Fund (WWF), for example, has worked constructively with government officials at various levels to protect pandas and other endangered species, to preserve ecologically sustainable development, and to promote environmental education. It currently has over 40 projects in many provinces. In recent years, another U.S.-based INGO, the Nature Conservancy has been invited to help guide a nationwide assessment of China's conservation priorities and help manage over 50 of China's 2,400 natural reserves because of its successful partnership with the Chinese Government.

In January 2007, under the instruction of SEPA, the China Environmental Culture Promotion Association (CECPA) compiled and released its first environmental

protection index. The index is intended to reflect public sentiment on environmental protection. China's first corporate responsibility index focused on the environment, called the Taida Environmental Index, was released on January 3, 2008. Forty listed companies from 10 environment-related industries compiled the index. As the first social responsibility index for China's capital market, the index is mainly aimed at evaluating listed companies' social responsibilities. Companies with a strong focus on social responsibility will be heralded by government and are likely to gain more opportunities for sustainable development.

To strengthen the administrative capacity of environmental regulation, the Chinese National People's Congress (NPC) recently elevated SEPA to the Ministry of Environmental Protection (MEP). As one of five new super ministries, MEP's responsibility, departments and staff all significantly increased. From command-and-control strategy to market-based environmental economics, and from state governance to cooperative governance, the new regulatory policies in China represent a new direction in China's environmental protection. It mirrors a fundamental shift in China's developmental strategy. The combined efforts should help produce some significant improvements in China's environment in years to come. One thing is clear, in the prolonged battle against the environmental degradation, the state is no longer the monolithic actor, and decision-making process has become more open, with a greater degree of civic participation, which could help foster a participatory culture in China and educate people how to be a partner in the governing process.

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China Lessons: Getting Started in Business

by Reiko Feaver

Throughout 2007 and 2008, I served as Counsel for Asia for a US public company. During that period, we negotiated contracts with both private and government joint venture partners, as well as established our own operations and subsidiaries in China. This article attempts to set out very basic 'lessons learned' from our experiences. Some of the observations are based on our specific business and the special challenges we faced within the confines inherent to a foreign company setting up operations in our industry in China. Even given these specifics, however, our experiences and resultant actions translate to any foreign company starting out in China. Hopefully, the insights provided here will ease the way for other foreign companies new to China.

Picking Your Partner

The importance of vetting your partners and conducting basic due diligence has been discussed in numerous recent articles. Suffice to say here that it is a mandatory and relatively easy process for companies doing business in China. Rather than repeat basic advice covered in more detail elsewhere, I would like to specifically address circumstances we faced surrounding picking a partner for political relations or picking a government agency itself.

There are two broad situations where foreign companies may find themselves facing the challenges that come with this decision. In the first instance, many industries in China remain heavily regulated by the government. This control necessitates that many foreign companies coming into China partner with a government agency or with a private company with strong government relations. In the second situation, a foreign company, although not directly regulated, may believe that the growth and success of its business depends on establishing strong government connections.

In both instances, a foreign company is well served to prepare itself for potential difficulties that come along with the benefits of such a partner. Foreign companies often choose their partner based upon people that the foreign company is familiar with in the government agency or private company. A current constant in Chinese governmental agencies is that people at the top are subject to rather arbitrary and immediate removal or transfer. As well, top personnel are often rotated at regular periods of eighteen to twenty-four months. A change in top personnel can directly impact the foreign company's status. Although contracts are now generally widely used in China, they are best thought of as setting forth a foundation for the relationship and not necessarily as representing the fully negotiated partnership. In this reality, a change in leadership is often seized upon as an opportunity to reevaluate the commercial deal. A foreign company with ongoing operations at the time of such a change may be forced to agree to new, detrimental demands by its partner. A foreign company in the middle of negotiating a contract can face significant delays in the completion of its contract, or a complete restart of discussions, regardless of the length of time already spent by either party.

Foreign companies must also appreciate an additional risk arising from the fluidity of top government. As in all governments, not every civil servant has the same

allegiances. Even while a foreign company is conducting negotiations, or has already signed and sealed a contract, its competitors are most likely continuing to hold their own discussions with other members of the same government agency. If personnel from these other 'factions' are placed into decision making positions, the foreign company can find itself out of a deal completely. An individual government official can exercise significant power.

The above considerations arise even with 'private' companies in China with strong governmental ties. These types of companies are usually not fully 'private' companies. They are often owned at some level and in some proportion by an actual government agency, or staffed with government personnel. This fact not only requires the foreign company (particularly, if a public company) to conduct a level of due diligence of the 'private' partner commensurate to that it would conduct if considering a government partner, but also to be cognizant of consequences attendant to a change in top government personnel. Previously established or long standing commercial partners and relations may be abruptly terminated or altered by such a change. As well, the current interconnection of private and governmentally held companies in China may limit a foreign company in its ability to make independent choices in its suppliers, customers, or other business relations.

Finally, while many government agencies in China have reached a certain level of commercial sophistication, not all have experience in conducting business with foreign companies. Where a foreign company has a choice, it benefits itself to evaluate the experience or inexperience of a governmental or private company in working with foreign companies. An inexperienced partner can cause headaches to the foreign company ranging from relatively minor – daily interference and questioning of business decisions – to extremely major – unethical and corrupt behavior that can put the foreign company at substantial risk in its own jurisdiction.

Establishing Your Operations

Picking the right partner is not enough, of course. At the same time a foreign company is conducting its diligence and discussions with potential partners, it must also be considering the establishment and structure of the future joint venture or subsidiary. In the United States, the technicalities of establishing a company are relatively straightforward. In China, even Chinese use agents whose sole job is to interact with the government agencies charged with approving and registering a company. (As an aside, foreign law firms are not authorized themselves to make these applications on behalf of their clients, and must use Chinese agents.) The Chinese government exercises broad control over the establishment of foreign invested enterprises or partnerships. This control extends not only to larger matters such as the amount of capital required and timing of capital injection, but also to what might be considered minutia by companies unfamiliar with the Chinese regulatory environment, such as the name of your company. There are also several different government bureaus that a foreign company must deal with to establish its partnership or subsidiary, and these bureaus may reach different conclusions and impose different requirements. It is common for one bureau to approve a name application or scope of business, for instance, only to have it rejected by the higher level and the process sent back to step one.

To oversimplify, a foreign company looking to establish operations in China must at least consider three fundamentals: (1) scope of business; (2) optimal investment; and (3) most beneficial tax structure. Unfortunately, each of these factors may in

fact be subject to regulations imposed by the government which curtail the foreign company's flexibility.

A company's scope of business determines its permissible commercial activities. This is not to be taken lightly, as it is subject to government approval and can be closely monitored. Specific wording can be quite crucial. And, again, this is an area which will require at least two levels of approval by different government bureaus. Finally, future changes in business scope will require new rounds of application and approval.

The scope of business often determines the amount of required investment. Capital investment in China is broken into two categories: registered capital and total investment. The amount of registered capital is dependent on the total investment and each amount must be made according to timing mandates. As well, Chinese law imposes restrictions on the ability of a company to extract previously invested capital. Faced with these rules, foreign companies sometimes make the choice to capitalize their Chinese companies at the lowest level possible. This can be a mistake. A company desiring to make an increase in its total investment is required to reapply and this process is at best lengthy and at worst results in a rejection. These somewhat conflicting considerations create a dilemma for foreign companies in trying to determine the true level of capital required for operations, without unnecessarily tying up capital. Again, this is an area where advance detailed and realistic planning will help the foreign company avoid future headaches.

The regulated schedule for the injection of capital requires a foreign company to proceed simultaneously on several fronts. For a foreign company, opening a bank account is not a simple process. A foreign company must commence the banking procedures at the earliest possible time, although it will be hampered by the attainment of prerequisite government approvals. All investments must be verified by an authorized accounting firm and engaging this firm is also a process that must proceed hand in hand with the applications for the company's establishment. Finally, the timing of all internal processes and required transfers from external banks must be considered; and, depending on the final corporate structure of the investment into China, this may require injections at several corporate levels which may add significant time.

The length and complexity of the application and approval process involved in a foreign company establishing operations in China makes upfront tax planning crucial. It is important to get the tax structure right from the outset to avoid further rounds of new applications or hostage capital. In some instances, the most beneficial structure may involve establishing several layers of related companies in various jurisdictions.

A not insignificant last consideration is the scope of the paperwork that must be submitted in a foreign company's application. Corporate documents from the parent company, and/or from various related companies depending on the structure of the foreign company, must be submitted to the Chinese government. These documents generally must be notarized by a Chinese consulate in the jurisdiction of the company and this can take weeks. A complicated corporate structure in the foreign company may also cause delays, additional paperwork, and discussions and explanations to the Chinese approval authorities.

Other Considerations

So far, this article has discussed several basic considerations surrounding the technicalities of initiating operations in China. Based on my experiences, I would also like to make several additional observations which I expect are common to companies starting to conduct operations in China.

As mentioned, establishing a company in China involves lengthy government applications and approvals. A foreign company's Chinese partner may want to 'assist' in the necessary paperwork to ease the approval. It is imperative that the foreign company remain actively involved in the preparation and filing of this paperwork, even to the extent of ensuring that a company representative attends the actual filing. This is necessary no matter how trustworthy a partner may be or how long-standing the relationship. Foreign companies, unfortunately, have been victims in situations where a signed contract was not the contract actually filed with the authorities or where changes were unknowingly made to previously filed documents. Active participation and communication between the foreign company and its Chinese partner must continue throughout the life of the relationship to avoid these types of discrepancies between what was apparently agreed to and what appears in the government file. Officially registered documents are extremely difficult to revise, even if the Chinese partner is amenable to so doing. A foreign company must always remember that the official company documents will be those that have been filed with the authorities and no company exists until all of the approval procedures and filings have been completed. This is true no matter how many contracts have been signed between the foreign company and its partner.

The structure of corporate governance is crucial in a foreign invested partnership or company in China. Of course foreign companies will adopt different processes to protect themselves, but there are basic areas which any joint venture corporate structure must handle.

The 'legal representative' of a Chinese company, foreign invested or not, is the person who carries legal authority to bind the company. The preferred position for a foreign company is to possess the right to appoint its own representative to fill this position. Practically, a Chinese partner will be highly reluctant to acquiesce to this request, and, in some cases, applicable industry regulations require that the position be held by a Chinese national. If the legal representative position is not held by the foreign company's representative, an alternative protection is ensuring that the financial officer be appointed by the foreign company. In many situations, for foreign invested companies to withdraw or pay money, both the signature of the legal representative and the financial officer are required. While this will not protect the foreign company from contracts entered into without authority by the legal representative, it will offer some protection from unauthorized expenditures.

In a similar vein, a company's seal or stamp is extremely important in China. Although more recent practice requires both a signature and a seal, contracts and agreements can be made with only a stamp. These stamped contracts can bind a company even if such agreements were not authorized through internal corporate approval procedures. Unfortunately, control of the stamp often rests in the hand of the legal representative and many foreign companies will have no success in negotiating to retain control of the stamp. If so, the foreign company must ensure that it carefully and constantly monitors use of the stamp and the actions of the person maintaining possession.

These practicalities aside, a foreign company cannot afford to neglect contractual

corporate governance and decision-making procedures. Basic ways include the right to appoint a majority of the directors; or requiring supermajority decision making. Don't be fooled by a Chinese partner claiming that only a 'form' contract (the Chinese form) will be accepted by the government approval authorities. Acquiescing to resistance from a Chinese partner, or abandoning common sense corporate formalities, for the sake of signing a deal may be disastrous for the foreign company in the future. Sometimes it is necessary to walk away if no control is granted by the Chinese partner.

During contract negotiations and commercial discussions a foreign company must keep in mind the hierarchy of the Chinese government and private company system. Titles in China can be misleading and levels of authority and company structures may be non-transparent. This can cause an unprepared foreign company to believe they are negotiating with a final decision maker, when, in fact, the person with the true authority has never been introduced.

Expect unanticipated, and potentially substantial, costs. Of course, as in any well-planned international transaction, legal and tax fees may be high. However, in China, additional expenses must be incurred that might not be necessary in other countries. Even among 'sophisticated' private companies or high level government agencies, English is not widely spoken, whether in reality or as a negotiating tactic. This necessitates frequent use of translators and translations; the official language of almost every contract in China is Chinese. Transportation in country can be expensive; private cars and drivers are often required, particularly, if larger groups of people are traveling or extended periods of time are required. Visas can be difficult to obtain, and generally an outside service must be used for efficiency and ease.

To repeat the cliché, China is a diverse country – not only geographically and culturally, but also in basic ways, such as infrastructure and telecommunications, which can substantially affect a company's operations. A foreign company will save itself significant start up time, expense and hassle if it invests in upfront evaluation and investigation to understand the peculiarities of the areas in which it intends to conduct operations. Differences from region to region may mean negotiations of commercial terms and contracts on a one-by-one basis, with very different results (even within the same 'national' company).

Professional consultation and careful initial planning will also save a foreign company in the area of staffing its operations. As many know, China has recently changed its labor laws, and, in theory, at least, employees enjoy greater employment protections. In particular, once an employee has passed the probation period – the length of which is mandated by law – it is difficult to terminate the employee and, even if termination can be accomplished, a severance payment will most likely be required. These employment laws are similar to those existing in Europe, although in some areas can be less restrictive. It is useful to establish a staffing plan and employment policies, including levels of compensation and benefits at a very early stage. Employment in China can be more 'equalitarian' than in other parts of the world. Giving early hires higher than market salaries or benefits may create morale difficulties with later hires, or may restrict a company's ability to set future rates and benefits. Foreign companies should be prepared to extend benefits that are not now widely provided outside of China, including, for instance, car or transportation allowances, housing allowances, food allowances, and education contributions for employees' children. Many companies in China offer company transportation as well;

and the company may need to budget for a company van or bus. Finally, foreign companies should now be aware that compensation and benefit levels in China for highly qualified and upper level management are on par with those outside of China. A foreign company may be surprised at what it must pay to attract top level candidates.

One last consideration is to be aware of challenges that may be faced by those foreign company personnel 'on the ground' in China and those back in the home countries. Management in the home countries and parent companies may find the extremes of Chinese regulation and rules to be beyond the pale and may dispute the advice of even their professional counselors simply because they cannot fathom the extent of the regulatory processes. Communication and emphasis on advance planning in areas such as those discussed in this article can avoid delays which might result from such confusion. The notion that 'China is different' still remains quite prevalent, not only within government agencies and private companies closely associated with the government, but even among newer and more entrepreneurial companies.

This article presents a high level summary of certain challenges facing a foreign company looking to move into China. At many levels, it has oversimplified the laws, rules, regulations and approval processes involved, as well as the practical realities. My previous company struggled through each one of the above discussed areas from the negotiation phase through start-up operations. While foreign investment in China has certainly become more streamlined and widespread, and is not to be feared (our operations resulted in US\$30million of weekly sales), it still brings with it significant challenges even for multinational companies. Upfront internal planning and consultation with experienced advisors is necessary for a company's success. But even the most carefully prepared company must brace itself for several harsh reality checks along the way.

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Center News

AI Willner to take director position in Washington, D.C.

Center Associate, AI Willner, has taken a position as Director, China Security Affairs Group, [CNA China Studies](#), in Alexandria, Virginia, to begin this fall. The CSA Group is part of CNA's federally funded research and development center which supports U.S. government efforts on China and other issues. His new contact email address will be Willnera@cna.org.

Shanghai Internship Now Recruiting

A small US export company, Shanghai American Direct Import & Export Co. Ltd. (www.xmftrade.com), seeks a motivated intern to help with all aspects of the business. This opening is for fall 2009 for a minimum of four months and can be extended. The company would like to work with someone who is interested in

helping to build a China based business, learning Chinese, and living in China. The company will provide housing and a modest food allowance. Please send a letter of interest and a resume to humanresources@xmfttrade.com.

A New Resource for Chinese Investors



Our Advisory Board member Guanming Fang recently co-authored a book titled (in Chinese) Invest in Private U.S. Companies, a Special Edition of the Growth Company Guide. This book builds on the existing book Growth Company Guide, 4th Edition, and introduces the concept and the terminologies of venture capital and private equity investment, a tool commonly used in the United States to make investments in private U.S. companies.

Since its first publication in 1987 as The Venture Magazine Complete Guide to Venture Capital, the fourth edition of the Guide written by Womble Carlyle partner Clinton Richardson is being hailed by investors and entrepreneurs alike as "a masterpiece," "the best corporate finance guide on the market today," and an "incredibly comprehensive resource." This special edition, with the contribution of Womble Carlyle partner Guanming Fang, is "full of tips and strategies" and a "fantastic resource" for Chinese investors interesting in learning U.S. venture capital methods.

To contact the authors or receive a copy of the book, please e-mail investUS@wcsr.com.

A New Cross-disciplinary treatment of China's Rise



Global Giant: Is China Changing the Rules of the Game? Edited by Eva Paus, Penelope B. Prime, and Jon Western (Palgrave Macmillian, 2009). In this book leading scholars and practitioners from different disciplines and perspectives analyze how China's phenomenal transformation and growth over the past two decades is challenging the rules of the game, internally and globally. They focus on three critical areas: the internal economic, environmental and political sustainability of China's development strategies; the economic development options for the rest of the developing world; and the continued economic and geo-political

dominance of the United States. With its breadth of coverage and attention to the interconnections among these pivotal issues, this book makes a unique contribution to our understanding of the implications of the rise of China.

Successful Forum on China's legal and economic environment held

Womble Carlyle LLC jointly sponsored a public forum with the China Research Center on June 25th, 2009, held at the new offices of the firm at Atlantic Station. Guanming Fang reviewed the major aspects of China's new labor contract law and how it has been implemented in the last year, and Penelope Prime discussed China's current economic situation in light of the global crisis based on her recent three month visit there. Click [here](#) for the presentations in PDF format and the video.

The CRC Welcomes our new webmaster

The Center is pleased to announce that Dr. Feng Liu will join us as our IT consultant and Webmaster. Dr. Liu is assistant professor of Information Systems at Mercer University, Atlanta.

Events

June 25th: "China Luncheon Briefing: Labor Contracts & a Changing Economic Environment," Thursday, June 25th, 2009, 11:30-1:30; Organized and Sponsored by: Womble, Carlyle, Sandridge & Rice, LLC & the China Research Center. Join us for lunch and discussion about the implementation and implications of China's new labor contract law, and an update on the effect of the global crisis on China's economy. Please see detail [here](#).

November 16th: Save the date! CRC 2nd Annual Event, Monday, November 16th, 2009, 7:00 p.m.

Speaker: Dr. Susan Shirk, Professor, University of California, San Diego

Topic: "US-China Relations: The Challenge of Domestic Politics"

Co-sponsors: The Confucian Institute, the National Association of Chinese Americans, and the Georgia Institute of Technology Center for International Business Education and Research

Location: The Carter Center

Notable Link

China Analysis: (Refer to: <http://www.chinaanalysis.com/>)