

Bloomberg Radio
“Bloomberg Big Picture”
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Zhejiang Province

Interview: Robert Lawrence Kuhn, Ph.D.



Kathleen Campion (Host):

We're talking this half hour about China. Robert Lawrence Kuhn is with us. He advises the Chinese government. He's senior advisor to Citigroup Investment Banking and author of *The Man Who Changed China: The Life and Legacy of Jiang Zemin*. Glad to have you with us in person.

Robert Lawrence Kuhn, Ph.D., China Expert:

A pleasure to see you, literally!

Campion:

We talked with Greg Anderson, who is a currency guy from ABN Amro. He said he thinks that the Treasury Department will dub China a currency manipulator. I wonder what you think about that.

Kuhn:

I don't think it helps anyone's interests to use pejorative terms. I do think the Chinese government has been responsible in allowing the yuan to appreciate gradually, consistent with maintaining stability in China's economy and good relations with other countries. China has national pride and will do things in its own independent way; it will not succumb to heavy-handed pressure. Pressure can be helpful, but it needs to be constructive, gentle, and perhaps subtle.

Campion:

And what do you think the Chinese government response would be to that pejorative?

Kuhn:

It wouldn't be dramatically problematic, but it would elicit nationalistic passions, the feeling that America is trying to "contain" China, which would not be helpful. America and China should be partners in building peace and prosperity in the 21st century. That's the key.

Campion:

We have a great deal to talk about. One of these things is the relationship between the State of New Jersey and a Chinese province, Zhejiang. You'll be doing some speaking on that subject. It seems, on the face of it, an odd relationship. New Jersey has a foreign policy? A trade policy? There is a large business delegation supporting Zhejiang Week in New Jersey.

Kuhn:

New Jersey is the "sister state" of Zhejiang, which is one of China's thirty provinces. It's a fascinating province in that it is a focal point of China's experiment to develop private business – it is one of the cradles of private business in China.

Zhejiang has 47 million people – modest in size for a Chinese province -- but its gross domestic product – on a per capita basis – is number one in China. The reason for Zhejiang's success is that 70 percent of the province's economic power comes from private companies.

Campion:

What kind of industries does Zhejiang have?

Kuhn:

It's light industry: textiles, clothing, agriculture [fisheries]. Also chemicals, electronics. It's not the industrial steel and cement factories that were part of China's initial industrial revolution. But those older enterprises – those massive state-owned enterprises – are not as economically efficient in the modern world of market economies. So Zhejiang, led by Party Secretary Xi Jinping, has had a remarkable resurgence, and it becomes a test bed, a microcosm, for all of China.

Americans have a problem understanding China because they envision China as one huge homogeneous mass – to us it all looks the same. In fact, China is heterogeneous, very different, very diverse, from region to region. For example, Zhejiang is entrepreneurial, while other provinces that rely on heavy industries of the past have more problems.

Campion:

Are the large privately-owned companies in China owned by wealthy individuals or foreign investors?

Kuhn:

Of the 500 largest privately-owned companies in China, 118 are located in Zhejiang, which is the largest number in any province. All are owned and controlled by Chinese, though many are now public companies and many have joint ventures with foreign companies.

Campion:

Western investors, of course, have been desperate for some time to participate in the booming Chinese economy. At the same time, they're uncertain about the statistics – like those on growth or per capita income or returns on investment – because there is no public regulator that seems to be outside official circles. How do you counter those concerns for an outside investor?

Kuhn:

Well, they're legitimate concerns. But as we all know risk and reward are related -- and in China there are tremendous reward opportunities. It is fair to say that the legal systems, the regulatory systems, are developing. There have been problems, but the country's leadership knows full well that maintaining economic growth requires sustaining investor confidence, which can only be solidly built on a stable legal and regulatory foundation -- and China's leaders are very focused on bringing this about. So it's improving.

In Zhejiang province, which is a great example, Secretary Xi Jinping has pioneered openness in government, more so than in many other provinces. In fact, just recently, Zhejiang eliminated China's long-established residency requirement [*i.e.*, *hukou*] so that people from rural areas can move into urban areas without having to go through formal procedures. In China, this is a very big deal. Secretary Xi has pioneered many such new initiatives that will continue to bring about the transparency of government.

Campion:

You're talking about this wonderful experiment in Zhejiang. It must be sanctioned by China's central government. You cite amazing sustained growth, better than 13 percent over 20 years. Why wouldn't China's government lift restrictions on all provinces and allow them to prosper similarly?

Kuhn:

The approach in China is always experiment carefully and assess the results before allowing widespread adoption. And when a new policy or process proves itself to work, it then expands. But it still expands gradually, because stability of the country is the most important criterion by which China's leaders judge everything. Economic growth is exceedingly important, as is improving the

standards of living of all the Chinese people, but maintaining the stability of Chinese society comes above all – since stability is a prerequisite for all good things.

So, indeed, this ability to do private business, this spirit of entrepreneurship, exemplified in Zhejiang [called the “Zhejiang Model”] has expanded over a great deal of the country. It turns out, though, that Zhejiang has particularly prospered for two major reasons. First, the province didn’t have the embedded base of massive (and now archaic) state-owned companies from the past planned economy, and second the Zhejiang people have an entrepreneurial energy and intensity – this is a combination that gives Zhejiang competitive advantage. Growth in Zhejiang has been tremendous -- you can see it – and it is not just economic but it is also the cultural richness of the province, the new roads, the enhanced school systems.

Zhejiang now provides its children with 15 years of universal schooling – all its children get a complete education: three years of preschool through 12 years of high school. Zhejiang is the first province in China to do this. All of the social and cultural elements of a civilized society are being built as well. And it is spreading over all of China.

Campion:

Western investors have been beating on China’s door for some time, even though they are often confronted with evidence of official corruption. Do investors see evidence that China is making progress on that front?

Kuhn:

They do, but corruption certainly is a problem, as are economic imbalances between rural and city, east and west; environmental issues; and energy constraints. China does have its slew of problems, no question about it, and corruption is definitely one of them. The government is very concerned about it, but change will take time -- investors need to factor that into their analysis.

Campion:

I was intrigued when you told me that piracy issues are now becoming an issue for Chinese companies. How is that?

Kuhn:

This is a significant change in China. When foreign companies put pressure on China to eliminate counterfeit products, it’s important for these foreign companies but it generally affects only a small percentage of their worldwide revenues. But now branded Chinese companies have emerged, such as in software, in clothing – so that when their branded products are pirated, they’re losing 100 percent of their revenues! Branded Chinese companies are a new pressure group in China to pressure federal and local governments to crack down on piracy.

We have this combination of factors that are coming together to require the Chinese government to respond more strongly to piracy, and Zhejiang province, for one, is definitely listening, because not only do they want to follow the law and protect foreign companies but also they have developed some very good local brands that they want to protect. The Zhejiang government has taken an aggressive stance against piracy. Piracy has become an increasingly important issue for government at all levels in China. And that’s good news for everyone.

Campion:

Very interesting to see the evolution. Now everybody wants to sell into China. The big banks, the big retailers, manufacturers, media companies – these are the industries we always hear about. How will that be done, big picture? Will a few of each be allowed in and then we’ll see?

Kuhn:

It’s largely no longer a question of “allowed,” it’s a question of the market making its own decisions.

And that's the very best possible way. There are some continuing restrictions, of course, obviously in defense industries, also in financial institutions, media.

But, broadly, there are few restrictions. The only real restriction in many industries is the marketplace – the relevance and quality of your products, the strength of your commitment, with whom you partner, how you negotiate. It's quite free. And there's even competition between provinces, just like we have in the U.S. between states -- when companies want to build a new plant, provinces or municipalities will compete for it with tax dollars, grants, and the like. Just like in the U.S., when different states compete to be the home of a large new manufacturing facility. Local Chinese governments are learning how to compete.

Campion:

There's too much to talk with you about! China has been very frank on the subject of pollution; they're concerned that double-digit growth is not an unalloyed positive.

We've been following a story that the U.S. now has some really nice clean technologies – I'm thinking of clean coal – that we've been forced to develop. Is selling that sort of technology to China a deal worth doing?

Kuhn:

I can't think of anything more important for America and China to cooperate on than clean energy. Clean coal is indeed the best example. Coal contributes a quarter of our energy needs, but about two-thirds of China's. It's vital that China develop clean technologies for coal.

I absolutely subscribe to the idea that energy technologies should be a key area in which America and China work together. We can sell current technologies to China, and we develop new technologies with China.

Campion:

China's government has also been frank about the gap between rich and poor – something that's true here as well. It may be more stark in China because of their recent, remarkable growth. How might relations with the U.S. ameliorate this problem?

Kuhn:

Imbalances between rich and poor, usually characterized as between urban and rural areas (or coastal and inland areas) is the singularly most volatile issue facing contemporary China. China's senior leaders are acutely concerned about this bifurcation of society. China went from the most egalitarian society, 30 years ago, where everyone was equal – equally poor of course, but equal – to a country which has one of the greatest gaps between rich and poor in the world. The ratio between urban and rural income is like 3.3 to 1.0, a very large disparity. China must make progress in rectifying these imbalances, a policy that leads to broad areas of economic opportunity for those with vision and insight. Media is a good example, since media can reach the whole country instantly, elevating quality of living, rebalancing educational levels (which will eventually translate into rebalancing economic power) and even providing reasonably equal entertainment options. America and China should work together on helping China rectify its economic imbalances, because this is China's biggest problem.

Campion:

Always a pleasure to talk with you: Robert Lawrence Kuhn, who advises the Chinese government. He's senior advisor to Citigroup Investment Banking. And he wrote *The Man Who Changed China: The Life and Legacy of Jiang Zemin*, the best-selling book of 2005 in China.

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Dr. Robert Lawrence Kuhn speaking about Zhejiang Province with Kathleen Campion, Bloomberg



Dr. Robert Lawrence Kuhn with Mr. Ye Tong, Zhejiang Province Information Office, at Bloomberg