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Viewpoint: Robert Lawrence Kuhn



## Behind China's Investment in Blackstone

**Yes, Beijing has a master plan, but it's not a nefarious one to dominate the world. It's aimed at addressing China's own serious problems**

by [Robert Lawrence Kuhn](#)

The announcement that the Chinese government would invest \$3 billion of its massive \$1.2 trillion foreign reserves in the Blackstone Group has triggered hair-raising rumors of China's "real reason" for doing so, speculations that expose American naiveté more than Chinese perfidy. Most center on a darkly imagined Chinese "master plan," if not to dominate the world (quite yet), at least to control foreign assets in an insatiable desire to expand. China does indeed have a master plan, but it is not this.

This year, no major matter of Chinese policy can be understood outside the context of the Seventeenth National Congress of the Chinese Communist Party, scheduled for the fall. Held every five years, Party Congresses are the events at which senior leaders set the political agenda and reshuffle the lineup of current and future leaders. Social stability is critical to the success of these events, since social unrest could disrupt carefully nurtured plans for political transition, consolidation, and succession. That's why we now see more control over the media. This is also why China eschews rapid appreciation of the yuan, which could throw millions out of work and on to the streets.

### **Nothing to Fear Here**

China's investment in one of America's leading private equity firms, consistent with its overarching objectives, serves multiple purposes, none of which are conspiratorial:

- diversifying foreign holdings (especially with the dollar falling with respect to the yuan);
- increasing yield above Treasuries (which includes a yield boost thanks to a pre-IPO discount on the price of the principal);
- testing alternative investments through private equity;
- experiencing from the inside the intricacies of Wall Street, consistent with China's increasing participation in international capital markets;
- encouraging a world-class investor to become more active in China;

- developing a low-risk mechanism for seeing a large number of international private companies through a recognized leader;
- exploring a model based on the Singapore government's enormously successful investment arm (Temasek);
- keeping its foreign reserves in the U.S. in order not to exacerbate existing friction; and
- aligning with a powerful American financial force as a partial counterbalance to pressure by the U.S. Congress to revalue the yuan.

As for China's real master plan, one must start by recognizing that, notwithstanding its remarkable development, the country has serious systemic problems: income disparity, fragile financial systems, unemployment, migrant workers, corruption, energy constraints, unsustainable development, environmental pollution, and more. Some problems come from rapid economic growth, some come from transition to a market economy, and some are a result of political stagnation.

China's most intractable problem is an addiction to growth perilously combined with a widening gap between rich and poor, imbalances that the Communist Party calls China's "most serious social problem." China must grow because, with millions of unemployed farmers, workers laid off from moribund state-owned enterprises, and legions of young people entering the workforce, unemployment could threaten social stability.

### **Avoiding Twin "Nightmares"**

According to insiders, China's senior leaders speak of twin "nightmares." One is the economic nightmare of slowing growth and environmental damage, exacerbated by energy shortfalls and unsustainable development. The other is a political nightmare of erupting clashes that are the result of social disparities made impossible to ignore by the uncontrollable flow of information on cell phones, the Internet, and other media. Some leaders worry that the country's financial system is China's weakest link in its chain of development.

When Chinese leaders ruled by fiat, they could solve problems peremptorily, whether by commanding the centralized economy, instituting political mass movements, or whipping up xenophobic nationalism. But past patterns of state behavior are no longer viable. Since China's economy is integrated into the world economy and the private sector generates much of the country's growth, the government cannot wield arbitrary power without unacceptable disruptions. China is no longer exempt from the norms and practices of great nations.

President Hu Jintao's vision is summarized by three slogans: "Harmonious Society" and "Scientific Development Perspective" domestically and "Peaceful Development" internationally. Harmonious Society seeks fairness and equity across China's diverse populations and geographies. Scientific Development Perspective stresses integrated sets of solutions to economic, social, and environmental problems; seeks the rectification of economic imbalances; and promotes the institutionalization of sustainable development. Peaceful Development conveys that no matter how strong China becomes, it will remain a bulwark of stability in the world and never threaten its neighbors.

### **Hu's Pragmatic China Model**

Western criticism of President Hu, particularly regarding human rights, exposes his hypersensitivity to social stability but misses his fresh commitment to addressing China's

multifaceted problems. Hu's pragmatic agenda has three core values—maintaining social stability to further economic development; instituting social fairness and rectifying imbalances; and sustaining Chinese culture to secure national sovereignty and enrich people's lives. Such realism increases confidence that China, notwithstanding its problems, will maintain its remarkable development.

What emerges in the view of President Hu is the "China Model," a systematic approach to national structure and development that combines dynamic economic growth, a free market energized by a vigorous "nonpublic" (i.e., private) sector, unrelenting political constraints and media control, personal but not political freedoms, concern for the welfare of all citizens, cultural enrichment, and a synergistic effort to rectify economic imbalances and ensure social fairness. All of which lead, in Hu's vision, to the Harmonious Society. Beijing sees its China Model as an alternative to Washington's Democracy Model, particularly for developing countries.

This China Model is China's true master plan, and its investment in Blackstone is one small element in this very large endeavor.

How should we react?

### **Aligning Interests**

China's investment in America is more opportunity than threat. Chinese enterprises, including those controlled by the Chinese government, should be rewarded, not punished, for following the rules and norms of international business. As more conforming behaviors are positively reinforced, China will continue to mature into a responsible nation.

American politicians have a choice: to allow market forces to work equally for Chinese companies or to create exclusionary hurdles that will undoubtedly inflame passions. Whenever we consider America's best interests, our policy prescriptions should shape behaviors and reinforce actions that guide China toward responsible statecraft. The more aligned Chinese companies are with American companies, the more truly aligned our common interests will be, and the greater the perception of alignment will be.

The benefits are not only economic efficiencies that increase standards of living worldwide but also political and social reforms that energize China's increasingly pluralistic society.

Dr. Kuhn, an international investment banker and senior adviser at Citigroup, is the editor of *China's Banking and Financial Markets: The Internal Research Report of the Chinese Government* and the author of *The Man Who Changed China: The Life and Legacy of Jiang Zemin*, China's best-selling book in 2005.