July–August 2009

The China Business Review

USCBC THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL

Mixed Signals

Interpreting China's M&A Regime 18

Also

Anticorruption Due Diligence for M&A 22

US$22/HK$220

China Foto Press

China begins to chip away at monopolies—in a way that raises some questions.

The China Business Review

USCBC THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL

Focus: Mergers and Acquisitions

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Cover design by Jesse Marth

Features

Departments

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Letter from the Editor

As we look back at the *China Business Review*'s (*CBR*) first year, we wonder what the US-China business community was concerned about in the summer of 1974. Articles from the July-August issue of the *CBR* show that companies were still learning the basics. The issue featured articles titled "How to Export to China," "Introduction to Exhibiting in China," "How to Open a Bank Account in China," "Health and Customs for Visitors to China," and a page on the *American Industrial Report,* a publication by the National Council for US-China Trade (as the *CBR*'s publisher was then known), listing and explaining US products to potential Chinese buyers in Chinese.

In those days, Chinese buyers had little knowledge of American products, and the articles on exporting to China and exhibiting in China stress the importance of getting enough copies of company materials into the right hands. They also explain the delay that could occur when sending English-language materials. In one case, a US company that sent its materials to China did not receive a reply for a year, even though the Chinese recipient was interested and set its translators to work on the materials as soon as they were received.

The July-August 1974 issue also reported on the first Annual Meeting of the National Council for US-China Trade. Giving testament to the excitement surrounding, and importance of, these first connections between modern China and the United States, Secretary of State Henry Kissinger delivered the keynote address, and the National Council received congratulatory letters from its counterpart in China, the China Council for the Promotion of International Trade, as well as from several prominent members of Congress.

Foreshadowing the ability of Chinese manufacturers to churn out items suitable for nearly every market on earth, "How China is Adapting to the Japanese Market" described how Chinese manufacturers changed food packaging, sold bicycles under Japanese brand names, and changed textile manufacturing processes to meet the specifications of their Japanese customers.

On a lighter note, the *CBR*'s "world sports reporter filed this colorful report":

"Skinned knees and elbows dripped foreign blood on Chinese soil one Sunday during the Spring Canton Fair as a team of beefy German businessmen defeated a spirited British club 2 to 0 at soccer on Canton's Provincial People's Football Ground....

"...The game was played...with a Shanghai-made Lion brand ball, which to the satisfaction of the China Light Industrial Products Corporation, retained its shape and bounce throughout the game. That was more than could be said for the players themselves."

The article had no byline, but one wonders whether it was written by the same person who wrote rather colorfully about prices at the Spring Canton Fair: Clark T. Randt, Jr., who joined the National Council's delegation to the fair that year and later served as US Ambassador to China under President George W. Bush.

Speaking of colorful coverage, we at the *CBR* would like to know whether, after 35 years, the magazine is still fulfilling our readers' needs for insightful coverage of China business developments. Please take a moment to fill out the survey on p.9 and mail it to *China Business Review,* 1818 N St. NW, Ste. 200, Washington, DC, or fax it to 202-833-9027. Of course, we love to hear from our readers on any topic; please write to me at vhulme@uschina.org.

Virginia Hulme

The China Business Review

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Short Takes

Economy

China ranked 20th in the International Institute for Management Development (IMD) *World Competitiveness Yearbook 2009*, a slight fall from its spot as 17th last year. The report identified the strong performance of China's domestic economy, international trade, public finance, labor market, and scientific infrastructure. But the country still struggles in areas of international investment, business legislation, management practices, health, and environment. The United States remained at the top of the list, but Hong Kong is swiftly closing the gap at second place.

A recent Pacific Economic Cooperation Council survey showed that opinion leaders in the Asia-Pacific region are optimistic about the Chinese economy despite the global crisis. Though leaders expressed low satisfaction with the economic stimulus packages of the world's largest economies, over 60 percent were "satisfied or very satisfied" with Beijing's actions. China also received the greatest positive feedback on expectations for future growth. Twenty-eight percent of respondents believed China's economic growth would be stronger over the next 12 months, compared with 19 percent for India, 16 percent for the United States, and 10 percent for Japan.

Top earners in Greater China remain cautious in their spending, according to a recent survey by Visa Inc. High-income households interviewed in mainland China save 28 percent of their earnings, followed by 26 percent in Taiwan and 24 percent in Hong Kong. Interest in growing investments was highest among mainland respondents, 42 percent of whom were willing to incur debt to do so, compared with only 25 percent in Hong Kong and 14 percent in Taiwan. But the overwhelming majority in all three regions cited increasing personal income and saving money as their primary financial priorities.

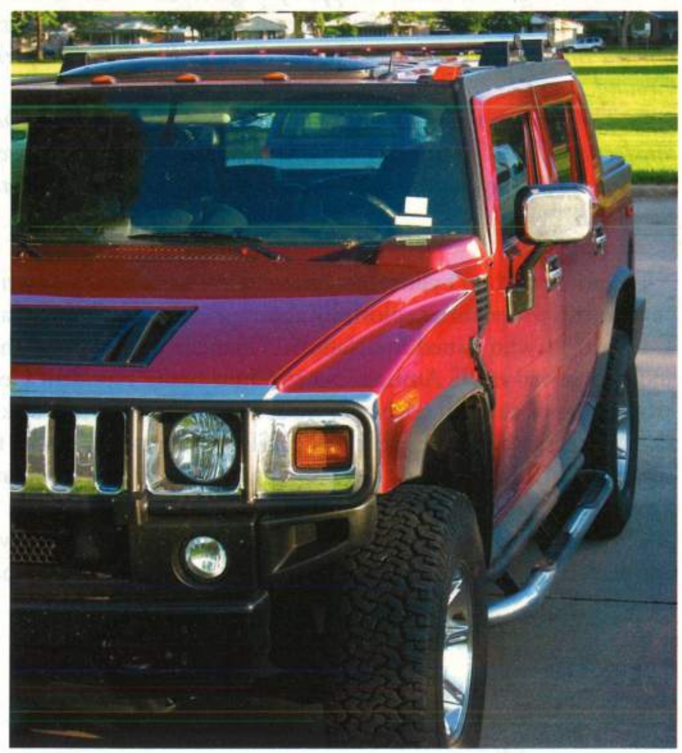
Foreign Investment

Beijing Municipality recently released new preferential policies to encourage multinational companies to establish regional headquarters in the city. The rules simplify procedures for establishing regional headquarters and reduce the minimum required cumulative registered capital invested by overseas parent companies from $30 million to $10 million. Regional headquarters, which have been established or relocated to Beijing after January 1, 2009 with registered capital of over ¥100 million, can also receive financial support from the municipal government to build, rent, or purchase office space. A trial of the new subsidies is currently under way in Beijing's Chaoyang district.

Autos

Following raised taxes last year on large vehicles and a recent price increase for gasoline, the PRC government continues to roll out policies that encourage use of smaller vehicles and alternative-fuel technology. Several PRC ministries recently jointly launched a pilot program in 13 cities nationwide to subsidize the use of hybrids and new-energy vehicles for public transport. In anticipation of the upcoming World Expo, car buyers in Shanghai will be eligible for subsidies of up to 20 percent on purchases of new-fuel vehicles from 2010 to 2011. In addition, the National Development and Reform Commission announced in June that consumers who trade in their mid-sized and small trucks or sell cars that no longer meet the government's emission standards are eligible to receive rebates on new vehicles.

Sichuan Tengzhong Heavy Industrial Machinery Co. has bid on General Motor Corp.'s Hummer brand. The little-known private truck maker intends to expand its presence in China and transform the Hummer into a global icon. As *CBR* went to press, the bid was drawing mixed reactions and could face difficulties in obtaining official approval, given Beijing's new fuel-efficient and environmentally friendly policies.



PC Industry

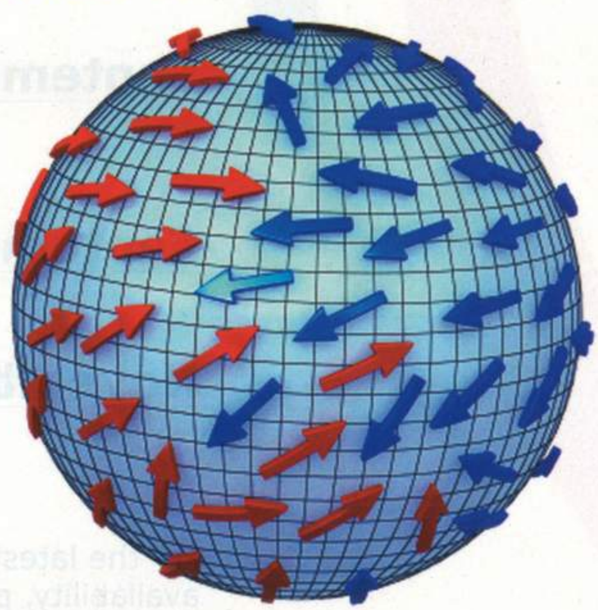
The PRC government may require all personal computers (PCs) sold in China to include a new software called "Green Dam-Youth Escort" beginning July 1. The software will block access to a regularly updated list of websites and will be provided free of charge by the government. According to the official notice, the measure is aimed at protecting young people from pornography and other "harmful content." The notice requires imported computers to have the software—a disc shipped with the computer will suffice—before they are sold in China. All PC producers must submit reports on their shipments of computers with the software.

These new regulations add to the growing concern over PRC government censorship of the Internet. There are additional worries that PC makers will not have ample time to make such a large production change and that the software could render computers more vulnerable to virus attacks and system crashes. Zhang Chenming, the general manager of Jinhui Computer System Engineering Co., which developed Green Dam, reportedly said that the user can turn off or uninstall the software.

Trade

The PRC State Council announced further support policies for exporters at its executive meeting in May. The government will provide $84 million worth of short-term export credit insurance to trading companies, tax breaks for labor-intensive and high-tech industries, and greater financial access to smaller companies. The State Council also said that it would keep the exchange rate stable to help exporters avoid exchange risks.

In a similar measure, the Ministry of Finance raised export tax rebates on more than 2,600 items on June 1. The list of items in the official announcement included TV transmitters, sewing machines, canned food, toys, plastic, porcelain, glass, and steel products. This is the seventh time China has raised export tax rebates since last August.



The China Business Review

READERSHIP SURVEY

Your feedback is important to us! ***The China Business Review (CBR)*** is conducting a series of brief surveys this year to gain insights into our readers' interests and preferences—and how to improve the ***CBR***. Please fill out the following survey and mail it to ***The China Business Review***, 1818 N St. NW, Washington, DC 20036, USA or fax it to 202-833-9027. You can also fill it out and submit it online at **www.chinabusinessreview.com**

1. Most articles in the *CBR* are... ❑ Too long (too much detail). ❑ About right. ❑ Too short (not enough detail).

2. Most articles in the *CBR* are... ❑ Too basic. ❑ About right. ❑ Too advanced and/or too technical.

3. Please indicate your degree of interest in reading about each of the following topics in the *CBR* and the amount of coverage *CBR* provides on each topic.

	Interest: Check one for each topic			Coverage: Check one for each topic			
Level of Interest/Amount of Coverage	Strong	Moderate	Little	None	Too little	Just right	Too much
Administrative licensing							
Competition and overcapacity							
Corporate administration/general management							
Economy							
Government relations							
Human resources							
Investment in China							
Intellectual property rights							
Legal issues							
Manufacturing							
Politics							
PRC Customs and trade administration							
Protectionism							
Sales & marketing							
Standards							
Telecom & information technology							
Transparency							
Transportation/logistics/distribution/retail							
Uneven enforcement of PRC laws							

4. For the topics that interest you, the *CBR*'s coverage is... ❑ Very helpful ❑ Helpful ❑ Not helpful ***Please explain:***

5. What topics should the *CBR* focus on in the next year that would be helpful to your China-related work?

6. What other information needs are currently missing from *CBR*?

7. Would you change anything about the *CBR*? ❑ Yes ❑ No ❑ If yes, what?

8. If *CBR* were to make changes, is there anything you would like to keep the same? ❑ Yes ❑ No ❑ If yes, what?

PLEASE DETACH HERE AND FAX OR MAIL

9. Please rate *CBR* in each of the following areas.

	Excellent	Very good	Neutral	Not very good	Poor	No opinion
Depth of analysis						
Ease of finding what you need						
Front cover as invitation to read *CBR*						
Relevance to you						
Quality of authors						
Use of sidebar materials (extras)						
Timeliness of topics						
Variety of topics covered						
Overall design of magazine						

10. We need your help with questions about other sources of China business information.

Source	Which 3 sources do you most enjoy? (check any 3)	Which 3 sources best satisfy your needs for China business information? (check any 3)	Which sources have a higher level of credibility than CBR? (check all that apply)	Which sources satisfy your needs for China business information better than *CBR*? (check all that apply)
American Chamber of Commerce				
Bloomberg.com				
Business China (Economist Intelligence Unit)				
Caijing				
China Business (Wall Street Journal Briefing)				
China Daily				
China Economic Review				
China business related blogs				
ChinaSuccessStories.com				
Far Eastern Economic Review				
Financial Times				
Inside US-China Trade				
The Economist				
The Wall Street Journal/Wall Street Journal Asia				
US Chamber of Commerce				
US Export Assistance Centers				
Xinhua				
Other (Please list)				

11. Are you aware that the *CBR* is published by the US-China Business Council (USCBC)? ❑ Yes ❑ No

If yes, does this make you feel more favorable about the magazine? ❑ Yes ❑ No

For the next two questions, choose from 1 to 5, with 1=significant influence and 5=no influence.

12. How much does *CBR* play into your decision to retain USCBC membership? ❑ 1 ❑ 2 ❑ 3 ❑ 4 ❑ 5

13. How much value do you place on *CBR* as a membership benefit? ❑ 1 ❑ 2 ❑ 3 ❑ 4 ❑ 5

Additional Comments/Suggestions

Please write any additional comments or suggestions you may have to make the *China Business Review* more helpful and useful to read. We are particularly interested in your thoughts about content and possibility of moving to a digital-only format.

The Role of China's Think Tanks in Policymaking

Unlike most Western think tanks, most Chinese think tanks are in some way affiliated with the government, which largely dictates their function and work. They range from government-funded policy research institutes to fully independent think tanks that receive no government funding. The majority, however, lie in between, supported by and working for the government but not considered government agencies. In 2008, China had roughly 2,500 policy research institutes, which employed about 35,000 researchers mostly drawn from the ranks of leading PRC academics and retired government officials, according to Xinhua News Agency. Western analysts—such as James McGann, director of the Think Tanks and Civil Society Program at the University of Pennsylvania—identify approximately 70 leading central-level think tanks comparable to think tanks elsewhere, with varying levels of influence on the policymaking process.

Most Chinese think tanks research economic and international relations issues, but a few engage in sensitive domestic political and military issues. Many groups distill international policy and experience into an applicable domestic policy package for government agencies to incorporate into their policymaking. Some think tanks have helped to identify politically sensitive issues that require attention from the authorities, such as rural social disturbances, and to get them on the policy agenda.

Government policy research institutes

Many key government bodies have established policy research institutes to research and draft policies for their parent agencies to ratify and implement. Some are extremely influential in establishing policy in their fields. Key government policy research institutes include

■ **The Central Party School (CPS)** CPS is the top education center of the Chinese Communist Party (CCP) and is responsible for training government officials at the county level and above in political theory, governance, and leadership.

■ **State Council Development Research Center (DRC)** The DRC conducts policy research on economic and social issues and provides policy frameworks, including long-term development plans.

■ **Ministerial policy institutes** Many ministries maintain entities to research and provide draft policies.

Official think tanks

These institutions report directly to government agencies or are housed within government-directed universities and conduct research for policymakers. This group constitutes the majority of China's think tanks. Leading examples include

■ **China Academy of Sciences (CAS)** CAS is China's top center for science and technology research and related policy research and development. Founded in 1949 and reporting directly to the State Council, CAS now has nearly 37,000 technical staff, including more than 1,000 PhD-level researchers.

■ **China Academy of Social Sciences (CASS)** CASS also reports to the State Council and includes 31 separate research institutes with more than 3,000 researchers. CASS provides input on a broad range of policy issues.

Though not generally considered think tanks, China's state-owned enterprises also influence policy in sectors in which they have a strong presence.

"Semi-official" think tanks

■ **China Center for International Economic Exchange (CCIEE)** This body, headed by former PRC Vice Premier Zeng Peiyan and established in March 2009, is tasked with examining the current global economic crisis and providing support to key government decisionmakers in crafting response policies.

■ **Shanghai World Trade Organization (WTO) Affairs Consultation Center** Founded in 2000 and headed by former WTO negotiator Wang Xingkui, the center trains company executives, collects information on WTO issues for PRC government and public consumption, and researches issues related to upcoming WTO negotiations.

Independent think tanks

A small group of entirely independent think tanks derive their funding from domestic commercial sources or international institutional and commercial sources, which shape their research work. Prominent independent think tanks include the Unirule Group, founded in 1993. As they are not associated with government agencies, these organizations can be the most critical of government policy.

Future trends

More think tanks have been established in the last decade than any previous period in PRC history, and the recent founding of the CCIEE indicates high-level government support for semi-official think tanks. It also suggests think tanks may continue to proliferate and gain influence as China's policymaking becomes more sophisticated, and that other specialized groups could be established to tackle high-profile policy issues. 完

This article is adapted from a report that first appeared in China Market Intelligence, the US-China Business Council's (USCBC) members-only newsletter. To find out more about USCBC member company benefits, see www.uschina.org/benefits.html.

China Conference Calendar

China-related events near you

August–November 2009

Please confirm dates and venues with the organizer prior to attending events. To suggest an entry for the next issue, send an announcement to Jesse Marth (jmarth@uschina.org). You can also post listings and view additional entries on the *China Business Review's* website at www.chinabusinessreview.com/conference-calendar.php.

China International Architectural Expo, October 14–16

China NGO Projects Exhibition

AUGUST 13–14

Location: Beijing: Tsinghua University, Gymnasium
Organizers: China Foundation for Poverty Alleviation; Narada Foundation; China Nonprofit Organization Promotion Association
Contact: Huang Shan
Tel: 86-10-5166-9502 x8021
shine.huang@csrconsulting.com.cn
www.gongyifair.org

China International Nuclear Power Industry Expo

SEPTEMBER 2–4

Location: Beijing: China International Exhibition Center
Organizer: Beijing Qifa Exhibit Service Co., Ltd.
Contact: Winder Wang
Tel: 86-10-8586-3866
winderwang@163.com
www.cine010.com.cn

China International Wind Power Expo

SEPTEMBER 2–4

Location: Beijing: Beijing China International Exhibition Center
Organizer: Beijing Qifa Exhibit Service Co. Ltd.
Contact: Zhang Feng
Tel: 86-10-6558-4386
wxqifazhl@263.net
www.bjwindpower.com

Medtec China

SEPTEMBER 8–10

Location: Intex Shanghai
Organizers: Canon Communications LLC; China Council for the Promotion of International Trade (CCPIT)
Contact: Keith Kwok-Ho Tsui
Tel: 852-2186-6939
keith.tsui@cancom.com
www.devicelink.com

China Incentive Business Travel & Meetings Exhibition

SEPTEMBER 8–10

Location: Beijing: China National Convention Center
Organizer: Reed Travel Exhibitions
Contact: Flora Liu
Tel: 86-10-8518-9070 x200
fang.liu@reedepo.com.cn
www.cibtm.travel

China International Fair for Investment & Trade

SEPTEMBER 8–11

Location: Fujian: Xiamen International Conference & Exhibition Center
Organizers: Fujian Provincial Government; Xiamen Municipal Government; PRC Ministry of Commerce (MOFCOM), Investment Promotion Agency
Tel: 86-592-266-9825
cifit@chinafair.org.cn
www.chinafair.org.cn

China International Tire Expo

SEPTEMBER 9–11

Location: Shanghai Everbright Convention & Exhibition Center
Organizer: Reliable International Exhibition Services Co., Ltd.
Contact: Wilko Fong
Tel: 86-10-8589-8181
citexpo@reliable.org.cn
www.citexpo.com.cn

Furniture China 2009

SEPTEMBER 9–12

Location: Shanghai New International Expo Center
Organizer: Shanghai UBM Sinoexpo International Exhibition Co., Ltd.
Contact: Mark Nee
Tel: 86-21-6437-1178
marketing@cmpsinoexpo.com
www.furniture-china.cn

Shanghai Art Fair

SEPTEMBER 9–13

Location: Shanghai: ShanghaiMART
Organizer: Shanghai Art Fair Culture Art Development Co., Ltd.
Contact: Annie Ho
Tel: 86-21-6090-1765
annieho@sartfair.com
www.cnarts.net

China International Energy Saving & Environmental Products & Technology Exposition

SEPTEMBER 10–12

Location: Suzhou, Jiangsu: Suzhou SND International Expo Center
Organizer: Suzhou Municipal Economic and Trade Committee
Tel: 86-512-6667-9008
nwd@etccn.com
www.etc-expo.cn

Automotive Testing Expo

SEPTEMBER 15–17

Location: Shanghai Everbright Convention & Exhibition Center
Organizer: UKIP Media & Events Ltd.
Contact: Renata Lengui
Tel: 44-1306-743744
r.lengui@ukintpress.com
www.testing-expo.com

International Exhibition & Conference for Pulp, Paper & Forestry Industry

SEPTEMBER 16–18

Location: Beijing: China International Exhibition Center
Organizers: E.J. Krause & Associates, Inc.; China Paper Industry Development Corp.
Contact: Phoebe Ding
Tel: 86-10-8451-1832
phoebe@ejkbeijing.com
www.chinapaperexpo.cn

Shanghai International Franchise Exhibition

SEPTEMBER 19–20

Location: Intex Shanghai
Organizer: China Chain Store & Franchise Association
Contact: John Ho
Tel: 86-10-5191-6852
2004@ccfa.org.cn
http://sh.ccfa.org.cn

Chengdu Motor Show

SEPTEMBER 19–25

Location: Chengdu, Sichuan: New International Convention & Exposition Center
Organizers: Hannover Fairs China Ltd.; Chengdu International Exhibition & Convention Center Ltd.
Contact: Karry Wang
Tel: 86-21-5045-6700
karry.wang@hfchina.com
www.cd-motorshow.com

China (Beijing) International Exhibition on Liquid Natural Gas, Gas Filling Stations & Hydrogen Technology & Equipment

SEPTEMBER 23–25

Location: Beijing: National Agriculture Exhibition Center
Organizers: China Industrial Gases Industry Association; AIT Events Co., Ltd.
Contact: Mark Liu
Tel: 86-10-8586-8930
lng.china@ait-events.com
www.lng-expo.com

Aviation Expo

SEPTEMBER 23–26

Location: Beijing: China International Exhibition Center
Organizer: China Promotion Exhibition Co.
Contact: Shirley Gao
Tel: 86-10-8773-0641
cpbj@cpbjlf.com
www.cpexhibition.com/aviation/

Agrochemex

SEPTEMBER 27–29

Location: Shanghai Everbright Convention & Exhibition Center
Organizer: China Crop Protection Industry Association
Contact: Guo Wei
Tel: 86-10-8488-5907
ccpiagw@yahoo.com.cn
www.agrochemex.net

China International Architectural Expo

OCTOBER 14–16

Location: Beijing: China International Exhibition Center
Organizer: China National Building Material Exhibition & Trade Center
Contact: Nick Zhao
Tel: 86-10-8808-3839
nickstar007@gmail.com
www.iae-china.org

China Import & Export Fair

OCTOBER 15–NOVEMBER 4

Location: Guangzhou, Guangdong: China Import and Export Fair Complex: Phase I (Oct. 15–19), Phase II (Oct. 23–27), Phase III (Oct. 31– Nov. 4)
Organizers: PRC Ministry of Commerce; China Foreign Trade Center
Tel: 86-20-2608-8888
webmaster@cantonfair.org.cn
www.cantonfair.org.cn

International Trade Fair for Intensive Animal Production

OCTOBER 19–21

Location: Beijing: New China International Exhibition Center
Organizer: VNU Exhibitions Europe
Contact: Ruwan Berculo
Tel: 31-30-295-2879
ruwan.berculo@vnuexhibitions.com
http://sites.vnuexhibitions.com

International Conference & Fair for Measurement, Instrumentation & Automation

OCTOBER 20–23

Location: Shanghai Everbright Convention & Exhibition Center
Organizer: China Instrument and Control Society
Contact: Stephanie Shan
Tel: 86-10-8280-0621
zm@cis.org.cn
www.miconex.com.cn/en/web/index.aspx

China Yiwu International Commodities Fair

OCTOBER 21–25

Location: Yiwu, Zhejiang: Yiwu Meihu Exhibition Center
Organizer: Yiwu China Commodity City Exhibition Co., Ltd.
Tel: 86-579-8519-5526
yiwufair@hotmail.com
www.chinafairs.org/en

China International Pharmaceutical Industry Exhibition

OCTOBER 27–30

Location: Shanghai New International Expo Center, Hall W4-W5
Organizer: Messe Dusseldorf China Ltd.
Contact: Vivian Pan
Tel: 86-21-5027-8128
chinapharm@mdc.com.cn
www.chinapharmex2.com

World Scrap Metal Congress

NOVEMBER 2–4

Location: Shanghai: Intercontinental Pudong
Organizer: Terrapin Ltd.
Contact: Wen Hui Ng
Tel: 65-6322-2754
wenhui.ng@terrapinn.com
www.terrapinn.com/2009/scrap

Energy Show: International Exhibition on Electrical Technology, Power Generation & Distribution Technology

NOVEMBER 3–7

Location: Shanghai New International Expo Center
Organizer: Hannover Fairs China Ltd.
Contact: Denny Jin
Tel: 86-21-5045-6700
es@hfchina.com
www.energyasia.com.cn

Metal Working and CNC Machine Tool Show

NOVEMBER 3–7

Location: Shanghai New International Expo Center
Organizer: Hannover Fairs China Ltd.
Contact: Simon Shao
Tel: 86-21-5045-6700
mwcs@hfchina.com
www.metalworkingchina.com

China Trials: Global Clinical Development Summit

NOVEMBER 8–10

Location: Sofitel Wanda Beijing
Organizer: Lychee Group, LLC
Contact: Jon E. Liong
Tel: 1-732-917-0664
jon.liong@lycheegroup.com
www.chinatrialsevent.com

Info Comm China

NOVEMBER 9–11

Location: Beijing: National Agricultural Exhibition Center
Organizer: InfoCommAsia Pte Ltd.
Contact: Richard Tan
Tel: 65-6841-7478
rtan@infocommasia.org
www.infocomm-china.com

Money Fair International Exposition

NOVEMBER 20–22

Location: Shanghai Exhibition Center
Organizers: Shanghai Media Co., Ltd.; ImmixRed LLC
Contact: Jim Prince
Tel: 1-800-341-9488 x531
jprince@moneyfairchina.com
www.moneyfairchina.com

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Find more China-business events on the *China Business Review*'s website at www.chinabusinessreview.com/conference-calendar.php.

Event Wrap Up

WASHINGTON, DC

May

Issues Briefing on Trade Enforcement & China

Featured Timothy Reif, general counsel of the Office of the US Trade Representative (USTR), and James Bacchus, chair of the Global Trade & Investment Practice Group of Greenberg Traurig, LLP and former chair of the Appellate Body of the World Trade Organization.

June

US-China Business Council (USCBC) 36th Annual Membership Meeting

(See p.15)

Representatives Kirk and Larsen on US-China Engagement

Featured US House Representatives Mark Kirk (R-IL) and Richard Larsen (D-WA), co-chairs of the US-China Working Group.

Assistant Secretary Sandalow on US-China Climate Change

Sandalow, US assistant secretary for Policy and International Affairs, met with USCBC members after returning from discussions with US and PRC officials in Beijing.

BEIJING

May

China Operations Conference

(See below)

US-China Clean Energy Forum and Banquet

Senator John Kerry, chair of the Senate Foreign Relations Committee, and Representative Nancy Pelosi (D-CA) spoke at an event co-hosted by USCBC and the American Chamber of Commerce in China. Attendees also heard expert presentations on eight initiatives to promote energy efficiency and green technologies.

June

US-China Working Group Luncheon Roundtable

Featured US Representatives Kirk and Larsen, President of the National Committee on US-China Relations Stephen Orlins, and several other members of US government, nongovernmental organizations, and multinational corporations that do business with China.

Breakfast with William M. Daley

Daley, vice chair of JPMorgan Chase & Co. and former co-chair of President Barack Obama's election campaign and transition into the White House, spoke with members of the US business community in China and shared his thoughts on US-China trade relations, Obama administration priorities, and various economic concerns.

SHANGHAI

May

Workshop on Business Tax and High- and New-Technology Enterprise (HNTE) Certification Procedures

Featured Shanghai Commerce Commission Foreign Affairs Office Deputy Director Shen Qing, Shanghai Science and Technology Commission HNTE Certification Office Deputy Director Zhang Jianbo, and a representative of the Shanghai Tax Bureau's Indirect Tax Department. The officials reviewed tax policies and answered questions about recent changes to PRC business tax and HNTE processes.

USCBC Hosts China Operations Conference in Beijing

USCBC's China Operations Conference, held in Beijing on May 20, addressed current issues important to US businesses in China, including China's economic stimulus spending, business operations amid the economic downturn, and the Obama administration's China policy.

He Fan, assistant director of the Institute of World Economics and Politics under the Chinese Academy of Social Sciences, delivered the keynote address on China's economic recovery. David Dollar, then country director for China and Mongolia at the World Bank, gave a luncheon address on China's response to the global economic recession. Roberta Lipson, CEO of Chindex International, Inc., spoke on China's healthcare reform plans, and Gary Wan, director of Business Development for Asia Pacific Strategic Support at Caterpillar (China) Investment Co. Ltd., spoke on infrastructure development.

Attendees also heard presentations on high-tech investment and conducting government affairs in China from US Information Technology Office President and Managing Director John Chiang and USCBC Vice President of China Operations Robert Poole, respectively.

USCBC Unveils Board Election Results

Andrew Liveris, chairman and CEO of the Dow Chemical Company, was reelected as USCBC's chair for a second one-year term. The following new directors were also elected:

- Jeff Clarke, vice chairman of Operations and Technology, Dell Inc.
- William M. Daley, vice chairman and head of Corporate Responsibility, JPMorgan Chase & Co.
- Michael L. Ducker, president, International, FedEx Express
- David N. Farr, chairman, CEO, and president, Emerson
- Evan G. Greenberg, chairman and CEO, ACE Ltd.
- James W. Griffith, president and CEO, the Timken Co.
- C. Douglas McMillon, president and CEO, Wal-Mart International
- Richard L. Mucci, chairman and CEO, New York Life International

Also reelected to the USCBC board were directors William N. Dudley, president and chief operating officer, Bechtel Group, Inc.; William R. Rhodes, senior vice chairman, Citigroup Inc.; and Keith E. Williams, president and chief executive officer, Underwriters Laboratories Inc.

In addition to the re-election of Liveris as USCBC chair, the board appointed the following officers:

- Vice Chairs: Muhtar Kent, chairman and CEO, Coca-Cola Co., and Robert A. McDonald, chief operating officer, Procter & Gamble Co.
- Secretary-Treasurer: Keith E. Williams, president and CEO, Underwriters Laboratories Inc.
- Counsel: Andrew Shoyer, partner, Sidley Austin LLP

USCBC's 36th Annual Membership Meeting

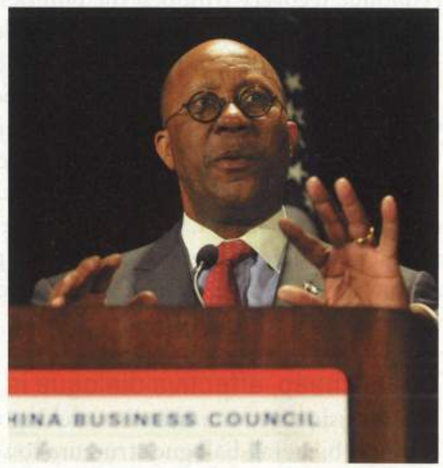
USCBC members gathered in Washington, DC, for the organization's 36th Annual Membership Meeting. USTR Ambassador Ronald Kirk delivered the keynote speech on "US-China Trade Relations Today and Tomorrow," in which he pledged to work with China to further open its markets to US goods, services, and investments. Kirk said that the United States is "seeking to grow better-paying jobs here at home" by "opening markets around the world to US goods and services." He also noted that China plays a central role in the international economy and that USTR will coordinate economic engagement with China through the Joint Commission on Commerce and Trade and the Strategic and Economic Dialogue. USTR will focus on the enforcement of trade agreements, primarily through dialogue and negotiation, but also through dispute settlement when necessary, so that American businesses and exporters are on a level playing field with their Chinese counterparts.

Companies listened to presentations on the latest business trends in China at the conference. FedEx Chief Economist Gene Huang reviewed recent economic data, emphasizing positive trends in China's economic recovery and the effects of various PRC government policies. Senior Partner and Managing Director for Boston Consulting Group David Michael provided an overview of China's stimulus package, focusing on how the package and related policies could affect US companies. National Practice Leader of Organization Effectiveness for Watson Wyatt Worldwide Ilene Gochman shared recent human resources trends and company best practices, highlighting the drop in voluntary turnover rates that has occurred as a result of the global economic downturn.

The meeting concluded with a luncheon panel, during which three senior executives that recently returned from China-based positions offered their views of China's current operating environment. Keith Davey, recently retired from Ford Motor Co., John E. Montgomery, recently retired from Hercules Asia-Pacific, and William E. Taylor of ITT Corp. provided perspectives on challenges faced and lessons learned from operating businesses in China.

USCBC President John Frisbie delivers opening remarks.

Gene Huang, chief economist, FedEx Corp., presents his views on China's economic recovery.



US Trade Representative Ronald Kirk delivers the keynote address.

Nearly 100 USCBC business executives, USTR officials, and members of the media listened to Kirk's remarks.

Kirk and Joann Piccolo, vice president, Global Government Affairs, Tyco Electronics.

Keith Davey and Frisbie.

sardari.com

Pragmatism Meets... What?

John Frisbie

The Obama administration's China policy approach is starting to take shape. So far, the word "pragmatic" comes to mind.

The administration has shown pragmatism in several ways. In February, Secretary of State Hillary Clinton visited Beijing, where she positioned human rights issues as no more important than security and economic issues in the relationship. In the Treasury Department's April report on exchange rates, the need for cooperation on global economic recovery trumped the pointless citing of China as a currency "manipulator." And President Obama nominated Republican moderate and Utah Governor Jon Huntsman, who has a strong background in business and China trade policy, as ambassador to Beijing.

The next signal of Obama's China trade policy will come in the decision on whether to apply punitive duties on low-end tire imports from China, as the United Auto Workers wants. If the administration lets this case go forward this summer, we can expect many more such cases and growing trade frictions.

Talk is cheap, effective dialogue is priceless

The business community is watching the development of a new bilateral dialogue structure to see if it will effectively address commercial issues. The first Strategic and Economic Dialogue (S&ED) will convene in Washington, DC, for two days during the last week of July. Clinton will lead the strategic side of the discussions opposite China's top foreign policy official, State Councilor Dai Bingguo; Treasury Secretary Timothy Geithner will lead the economic discussions with Vice Premier Wang Qishan.

The success of the dialogue over time will depend upon interagency coordination and participation—on both sides. Three vice premiers handle roughly equal shares of China's economic portfolio and the bureaucracies that line up underneath. On the US side, climate change and investment policies are just two examples of issues that cut across departments. Movement on the issues requires work from more than just the lead agencies involved.

Agenda crowding is also a concern. Global economic recovery and financial architecture discussions will likely dominate the "E" side of this first S&ED. Will there be room to also address commercial policy issues?

The Joint Commission on Commerce and Trade (JCCT) may be able to take on some of these commercial issues, adding a forward-looking policy component to the traditional (and necessary) negotiations over specific trade issues and disputes. Commerce Secretary Gary Locke and US Trade Representative Ronald Kirk bring a fresh opportunity to enhance the JCCT when it convenes for the first time under their leadership in late October.

Expanded engagement is important because the issues are many. As always, there is no shortage of industry-specific issues, but the growing concern is over systemic trends that could place a ceiling on foreign participation in China's economy. China's policies to promote "national economic security" and "indigenous innovation" are at the core of the concerns of US companies' China-based executives.

There is no doubt that China's World Trade Organization (WTO) entry eight years ago has reduced many market access barriers. American companies exported $72 billion in goods and services to China last year. US majority-owned affiliates in China racked up an estimated $63 billion in sales in 2006, the latest year of available data. Some of this "made in China, sold in China" revenue incorporates exports from the United States, but it is clear that China operations are now a significant part of global business health for many American companies and directly or indirectly support the job base in the United States.

Two kinds of champions

But the question is, where do China's reforms go from here? National champions? Apparently. Market-based reform champions? Not so clear.

The reforms that China is moving ahead with—healthcare and technological innovation, for example—address pressing domestic priorities but are not designed to push China further toward an open market economy. This trend comes when it is already clear that the three regulatory regimes that matter globally are those of the United States, European Union, and China—whether for emissions trading, safety standards, merger reviews, or transfer pricing. Moves by China to strengthen domestic preferences are potentially more troublesome for foreign companies now that China has become such a significant market.

The leverage of China's WTO entry terms to produce market openings is gone, of course. US credibility on

economic and financial policy advice is low in China, as it is elsewhere. Buy American policies and market restrictions imposed on the disposal of General Motors' Opel unit in Europe undermine prescriptions to China to limit government-mandated protections for domestic industry.

Public sentiment in China can't be ignored, either. The media and public support a harder-nosed, protective approach to the market—a feedback loop has been built on the continually reinforced premise that China and Chinese companies are being treated unfairly overseas, while foreign companies are welcomed and treated as privileged guests with extra incentives and support. Though China's central and local officials do not contend with electoral politics, the scrutiny of China's netizens places immense pressure on the government—and is a massive disincentive to showing any "weakness."

The bilateral discussion needs to be recast in this environment. The Obama administration will need to put parallel issues on the table: Chinese concerns about receptivity in the United States and the "level playing field" concerns of US companies operating in China. Investment policies and M&A approvals in the United States and China. Buy American vs. Buy China procurement policies. Competition policy. The government role in innovation and technology standards. Food and product safety. Most of the key issues can be addressed in this way.

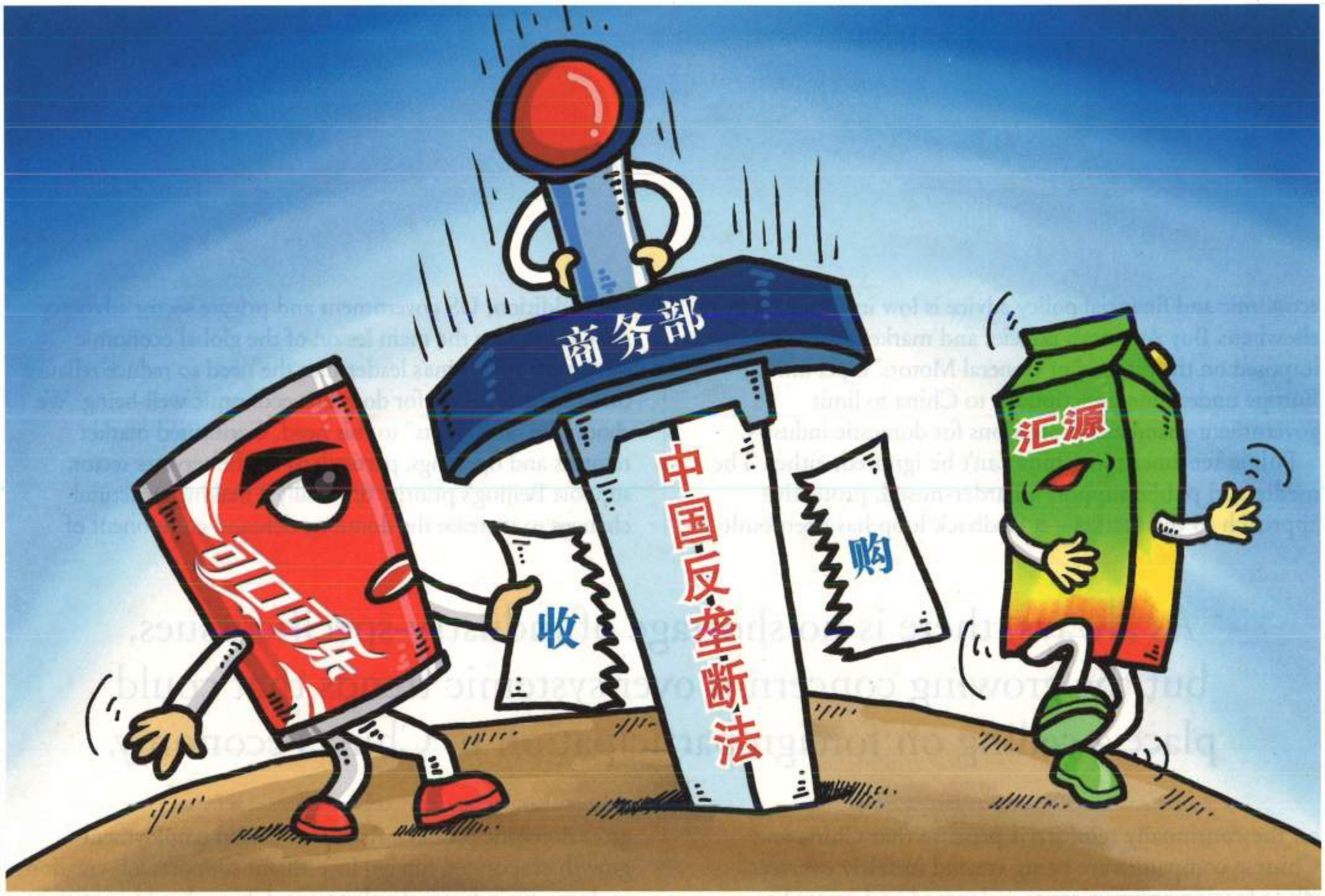
As always, there is no shortage of industry-specific issues, but the growing concern is over systemic trends that could place a ceiling on foreign participation in China's economy.

In addition, US government and private sector advocacy should leverage the main lesson of the global economic downturn for China's leadership: the need to reduce reliance on overseas markets for domestic economic well-being. We should tie our "wants" to this need. Continued market reforms and openings, particularly in the services sector, support Beijing's priority of (finally?) making structural changes to increase the domestic demand component of gross domestic product. As export-driven employment growth evaporates, foreign investment supports job-creation in domestic industry development. China should encourage employment-expanding foreign investment, not curtail it.

Most important, US negotiators need to recognize that the Wall Street financial implosion and Washington policy response have put US market-based credibility in a hole. The US economy will return to strength (and probably faster than the voices of vindication in China realize), but we need to be humble while also being firm on principles and the ultimate goal—a relationship that benefits both economies equally.

Even under this approach, breakthroughs will be hard to come by. But the "Fix China" camp in Washington and elsewhere should be aware that the days of dictation are over, and a new approach is needed. 完

John Frisbie is president of the US-China Business Council.



China Foto Press

The PRC Ministry of Commerce uses the Antimonopoly Law to prevent the Coca-Cola Co.'s acquisition of Huiyuan Juice Group Ltd..

Merger Control under China's Antimonopoly Law: The First Year

Three recent decisions indicate that China may be considering more than competition in its antitrust reviews

Matthew Bachrack, Cunzhen Huang, and Jay Modrall

China's new Antimonopoly Law (AML) took effect last August. The AML introduced a new mandatory regime for the review of mergers, acquisitions, and joint ventures. In the past year, guidelines and rules have been published that clarify the Ministry of Commerce's (MOFCOM) procedures for enforcing the new regime, and MOFCOM's decisions have been published in three high-profile cases. There are, however, still important uncertainties about MOFCOM's procedures and substantive analysis. In fact, the three published merger decisions—*InBev/Anheuser-Busch*, *Coca-Cola/Huiyuan*, and *Mitsubishi/Lucite*—have reinforced the notion that MOFCOM may use the AML to achieve goals unrelated to competition law. Now, roughly a year after the AML took effect, it is time to evaluate China's new merger-control regime and assess the implications of recent cases.

Notification: Unanswered questions

Although new guidelines and rules published in early 2009 clarify many questions about notifications under the AML, several concerns remain, especially for foreign multinationals:

■ Notifications require a significant amount of information. Although many jurisdictions require extensive up-front information in a merger notification, MOFCOM's rules do not provide for simplified notifications in cases that raise no substantive issues. This problem is exacerbated by the fact that notifications must be accompanied by vaguely but broadly defined categories of documents that are rarely relevant to the antitrust analysis of concentrations. For example, MOFCOM requires the production of "reports in support of the concentration agreement," including feasibility studies, due diligence reports, research reports on industry development, reports on the concentration plan, and forward-looking reports on the prospects of the parties after the transaction, all of which must be translated into Chinese. Locating such reports might require a search of thousands of files and e-mails, yielding enormous volumes of material that must be reviewed prior to translation and submission.

The breadth and vagueness of these requirements, in practice, give MOFCOM broad powers to claim that the notification is incomplete and halt the review. For example, the Coca-Cola Co. announced its proposed acquisition of China Huiyuan Juice Group Ltd. on September 3, 2008 and filed its pre-merger notification on September 18. At MOFCOM's request, Coca-Cola supplemented the filing four times before it was considered complete on November 19. The statutory review period finally began on November 20, two months after the initial filing. To mitigate the risk of such delays, notifying parties may be well advised to conduct pre-notification consultations.

The draft guidelines and rules also fail to resolve several additional ambiguities. These include

■ The definition of "control." The draft Provisional Rules on the Notification of Concentrations of Undertakings (draft notification rules), released for comment in January, create potential confusion because they define the term "control," which includes rights to influence an undertaking's management, but not "decisive influence." (A concentration arises under the AML when an undertaking obtains "control" or "decisive influence" over another undertaking.) MOFCOM's Antimonopoly Bureau has clarified that the acquisition of "protective" minority rights will not result in the acquisition of "control." The draft notification rules give some examples of "protective" minority rights, such as the right to veto modifications of articles of association, increases and decreases of capital, and liquidation.

■ Whether joint ventures, in the PRC corporate law sense of the term, are notifiable where no joint control exists. The draft notification rules confirm that the "joint establishment" of a "new entity" by two or more entities constitutes a concentration under Article 20 of the AML. The draft notification rules indicate that "specific function" joint ventures (joint ventures that only carry out specific functions for their parent companies, such as research and development, sales, and production of certain products) may not be notifiable—and that a joint venture will be notifiable only if it is established on a lasting basis and independently operated. The recently announced BHP Billiton/Rio Tinto transaction will be a good test case of MOFCOM's treatment of joint ventures. Interestingly, in a June 15 interview regarding the notifiability of this transaction, MOFCOM's spokesperson focused on turnover thresholds and did not mention a requirement that the joint venture be "full function." As *CBR* went to press, MOFCOM had not recieved a merger control notification regarding the BHP Billiton/Rio Tinto joint venture.

■ Whether a notification can be filed based on a letter of intent or similar document, or based only on a binding agreement;

■ The standards used to determine the confidentiality of materials submitted by parties to MOFCOM;

■ The level of protection afforded to materials deemed confidential by MOFCOM; and

■ The level of protection that will be afforded to materials subject to internationally recognized legal privileges.

Quick Glance

■ A year after China's new Antimonopoly Law (AML) took effect, several important questions about notifications, reviews, and market definitions remain.

■ Three decisions issued under the new AML indicate that the Ministry of Commerce (MOFCOM) may consider factors beyond those related to competition in its antitrust reviews.

■ The decisions also suggest that MOFCOM takes a flexible approach toward remedies.

Review: MOFCOM's role

The draft Provisional Rules on the Review of Concentrations of Undertakings (draft review rules) give notifying parties the right to make statements and to bring a defense. They also state that MOFCOM may seek the opinions of other government agencies, industry associations, customers, and other undertakings and that it may convene confidential hearings.

MOFCOM may decide to initiate a Phase II investigation after its preliminary review. If it does so, it must notify the parties in writing. In Phase II, if MOFCOM concludes that a concentration has eliminated or restricted competition or is likely to do so, it may send the notifying parties a statement of its objections that sets a reasonable time limit for the undertakings to submit a written defense.

If MOFCOM determines that a notified concentration would harm competition, it can prohibit the transaction or attach restrictive conditions. Both types of decisions (but not others) must be published in a timely manner. It appears that either the notifying parties or MOFCOM may suggest conditions, which may include structural remedies, behavioral remedies, and combinations thereof. It is unclear whether the proposed conditions need only alleviate, as opposed to remove, the anticompetitive effects of the transaction.

If MOFCOM issues a decision to prohibit or impose restrictions on a proposed concentration, the companies involved are entitled to ask MOFCOM to reconsider its decision. If they are dissatisfied with the outcome of the reconsideration, they may sue MOFCOM in PRC court or appeal to the State Council to reverse the decision.

Substantive review: Not entirely clear

MOFCOM must review the notification to determine whether a concentration "will or may eliminate or restrict market competition." It also retains discretion to permit concentrations that would harm competition if the notifying parties show that the advantages of the concentration outweigh the disadvantages, or if the concentration "is in line with the social and public interest." Several points remain unclear, however:

- The extent to which a concentration must restrict competition and the level of probability that a concentration would restrict competition that MOFCOM must establish before it can prohibit the transaction;
- Whether pure private efficiency gains will be a sufficient basis upon which to clear a concentration that would otherwise be prohibited; and
- The meaning of "social and public interest" in Article 28 of the AML.

Moreover, acquisitions of Chinese companies by foreign entities may be subject to additional scrutiny if the acquisition concerns China's national security, a key industry, or transfer of the de facto control of a domestic enterprise that owns a well-known trademark or an old Chinese trade name.

Market definition: Guidelines too formalistic?

The AML defines the term "relevant market" but does not provide any guidance on how MOFCOM will determine the relevant markets in a particular transaction. MOFCOM has issued draft Guidelines on the Definition of Relevant Markets (draft market definition guidelines) to help parties define relevant product and geographic markets. The draft market definition guidelines list a number of factors to be considered when defining relevant markets. When the definition of the relevant market is more complex, the draft market definition guidelines adopt the "hypothetical monopolist" test. This contrasts with EC and US practice, where this test provides a conceptual basis for the definition of relevant markets. In principle, the "hypothetical monopolist" test should apply to each case, not only the complex ones.

Recent precedents shed light on future reviews

As of March 18, 2009 (the most recent date on which MOFCOM announced statistics), MOFCOM had received 40 notifications under the AML and accepted 29 as complete. The ministry had reviewed 25 transactions, of which 23 were unconditionally cleared, one (*InBev/Anheuser-Busch*) was approved subject to conditions, and one (*Coca-Cola/Huiyuan*) was prohibited. Since that time, *Mitsubishi/Lucite* was also approved subject to conditions. Since MOFCOM is obliged to publish only prohibition and conditional clearance decisions, public information is available only for these three cases.

InBev/Anheuser-Busch

On November 18, 2008, MOFCOM approved, with conditions, InBev NV/SA's acquisition of Anheuser-Busch Cos., Inc. (AB). The ministry found that the acquisition would not eliminate or restrict competition in the Chinese beer market.

Because MOFCOM determined that the "transaction size is huge, the new entity after the merger will have substantial market share, and its competition ability will be sharply increased," the decision limited InBev's ability to expand its market share by placing restrictive conditions

Who Must Notify

China's Antimonopoly Law requires parties to a concentration to notify the Ministry of Commerce (MOFCOM) when mergers, share or asset purchases, or other transactions result in the acquisition of control or the ability to exercise decisive influence if the companies involved meet certain turnover thresholds. The Regulation on Notification Threshold of Concentrations between Undertakings, adopted on August 3, 2008, requires parties to notify MOFCOM if:

- In the previous accounting year, the worldwide aggregate turnover of the parties to the concentration exceeded ¥10 billion ($1.5 billion), and at least two of those parties each had individual turnover in China in excess of ¥400 million ($58.6 million); or
- In the previous accounting year, the aggregate turnover in China of the parties exceeded ¥2 billion ($293 million), and at least two of those parties each had individual turnover in China in excess of ¥400 million.

In addition, as in the United States (but unlike in many other countries), MOFCOM may investigate concentrations that do not meet the turnover thresholds but that might nonetheless eliminate or restrict competition. There is no time limit on MOFCOM's ability to investigate such concentrations. Parties to a concentration that need not be notified to MOFCOM but that raises competition concerns should consider engaging MOFCOM or filing voluntarily.

—Matthew Bachrack, Cunzhen Huang, and Jay Modrall

on its acquisition of AB. InBev must obtain MOFCOM's approval before increasing AB's equity interest in Tsingtao Brewery Co., Ltd.; increasing its equity interest in Zhujiang Brewery Co., Ltd.; or seeking any equity ownership in Chinese Resources Snow Breweries Ltd. or Beijing Yanjing Beer Group, Corp. In addition, InBev must promptly notify MOFCOM of any change in InBev's controlling shareholders and the shareholders of those controlling shareholders.

sufficient evidence to prove that the positive impact of the transaction on competition would outweigh the negative impact or that the transaction "conformed to the requirements of social and public interests." The decision appears to suggest that the notifying parties bear the burden of showing that efficiencies outweigh the adverse effect on competition, if any. The decision also indicates that Coca-Cola proposed remedies that MOFCOM judged insufficient.

MOFCOM's willingness to impose restrictive conditions on *InBev/Anheuser-Busch* and *Mitsubishi/Lucite*, and to prohibit *Coca-Cola/Huiyuan*, show that it is prepared to play an active enforcement role.

Coca-Cola/Huiyuan

MOFCOM on March 18, 2009 blocked Coca-Cola's planned acquisition of Huiyuan in the first prohibition decision adopted under the AML. This case had been closely watched as an indication of MOFCOM's approach to foreign companies' acquisitions of well-known Chinese companies.

In its decision, MOFCOM identified the following adverse impacts from the proposed transaction:

- Coca-Cola would be able to leverage its dominant position in the carbonated soft-drink market to the fruit-juice drink market, eliminating and restricting competition from current juice manufacturers and in turn damaging the lawful interests of juice consumers. Although the decision did not indicate how Coca-Cola could leverage its position in carbonated soft drinks, MOFCOM's press release referred to the possibility that Coca-Cola could engage in tying, bundling, or other forms of exclusive dealing.
- Coca-Cola's market power in the juice market would be markedly enhanced by controlling two famous juice brands, Meizhiyuan (Minute Maid) and Huiyuan. The transaction would significantly raise entry barriers for potential competitors in the fruit-juice drink market.
- The transaction would reduce the space available to domestic small and medium-sized juice manufacturers and negatively impact the ability of domestic enterprises to compete and innovate independently in the fruit-juice drink market.
- The transaction would have adverse impacts on the competitive landscape in China's fruit-juice drink market and the sustainable and healthy development of the domestic juice industry.

MOFCOM apparently considered claimed efficiencies, because the decision refers to the effects of the transaction on technological advances and on consumers. It determined, however, that the parties failed to provide

Mitsubishi/Lucite

On April 24, 2009, MOFCOM approved, with conditions, Mitsubishi Rayon Co., Ltd.'s acquisition of Lucite International Group Ltd. Notably, this decision provided significantly more detail than prior decisions.

MOFCOM identified the following negative impacts on a Chinese market for methyl methacrylate (MMA). The companies are horizontal competitors and would have had a combined market share of 64 percent after the transaction. In addition, since Mitsubishi competes in MMA and two downstream markets, after the completion of the transaction, the combined company would be able to restrict its downstream competitors' access to MMA thanks to its dominance upstream. As a result, MOFCOM determined that the concentration would eliminate or restrict competition and adversely affect competition in the Chinese MMA market and its downstream market.

Again, the parties proposed remedies. After negotiating the scope of the remedy, the parties and MOFCOM agreed to the following:

- The right to purchase 50 percent of Lucite (China)'s annual MMA production for five years at cost will be divested to a third party;
- Lucite (China) shall operate independently from the MMA monomer business operations of Mitsubishi Rayon in China with independent management and board of directors between the closing of the proposed transaction and the completion of the divestment;
- For five years after the transaction closes, Mitsubishi Rayon may not, without the prior approval of MOFCOM, acquire any producer of, or establish any new plant for, MMA monomer, PMMA polymer, or cast sheet in China.

Continuing the confusion as to whether remedies must "eliminate" or merely "reduce" negative effects on competition, the decision states that MOFCOM and the parties

Continued on page 26

Conducting Anticorruption Due Diligence in M&A Deals

Companies should investigate target companies to assess compliance risk under the Foreign Corrupt Practices Act

Richard Grime and Bingna Guo

The number of investigations under the US Foreign Corrupt Practices Act (FCPA), together with the number of prosecutions by the US Department of Justice (DOJ) and the US Securities and Exchange Commission (SEC), have hit record levels in the past few years. Huge fines have followed these investigations, including a record $1.65 billion in total fines and penalties imposed against Siemens Corp. from separate German and US prosecutions. Because of its broad application, the FCPA creates unique risks for multinational corporations (MNCs) and US companies doing business abroad, especially in high-risk countries such as China.

The FCPA is particularly important when considering mergers and acquisitions (M&A) because an entire transaction can fall apart if the risk is not discovered at the appropriate time or managed properly. In recent years, many FCPA cases arising from M&A transactions have yielded dramatic results, such as the collapse of Lockheed Martin Corp.'s proposed $2.2 billion acquisition of Titan Corp. in 2004. In another case, three Vetco International Ltd. subsidiaries were fined $26 million in 2007 because they made about $2.1 million in corrupt payments to Nigerian government officials. The large fine, in part due to one of the subsidiaries' prior 2004 FCPA conviction, raised issues of successor liability when General Electric Co. (GE) acquired

Vetco Gray in 2007. Further, the June 2008 DOJ opinion regarding FCPA liability in the context of a proposed corporate acquisition by Halliburton Co. underscores the importance of anticorruption due diligence of M&A targets that operate in high-corruption environments and sets forth key elements of a due diligence investigation that may, in appropriate circumstances, be sufficient to protect an acquirer from successor liability for FCPA violations.

M&A deals have been a common way for foreign investment to enter the Chinese market in recent years. As US companies' M&A transactions in China have increased, so has the risk of FCPA violations. Several high-profile cases of FCPA enforcement involving M&A transactions have been related to corruption committed in China. For example, in the GE/InVision case, InVision Investment Technologies Inc. allegedly violated the FCPA by making improper payments to local agents or distributors in China and other Asian countries. InVision disclosed these potential violations to the DOJ and SEC after GE announced its intention to acquire InVision in March 2004. InVision entered a non-prosecution agreement with the DOJ before GE acquired it and was fined $800,000. The post-merger company also reached a settlement with the SEC, under which GE-InVision agreed to disgorge the $589,000 in profits arising from the alleged FCPA violations and pay prejudgment interest of $28,703 and a $500,000 civil penalty.

FCPA risk in China remains high due to certain Chinese business practices and industry sectors that remain state-owned or controlled. With the US government's focus on the FCPA, US companies acquiring Chinese businesses should conduct anticorruption due diligence on the target company to identify potential FCPA risks (see p.24). The process of due diligence will help to establish the true value of the acquisition target and determine whether bringing the post-merger company into compliance could jeopardize the acquirer's profitability or result in criminal liability for past violations.

FCPA implications for key issues in the M&A context

In M&A transactions, successor liability for prior FCPA violations is an increasingly important issue. An acquirer that does not perform effective due diligence on a proposed target risks being held accountable for past FCPA violations. In a stock transfer or merger, the successor company is generally held liable for past violations of the target company. But in some circumstances, successor liability may attach in an asset purchase. For example, one of several broad exceptions to the general rule of no successor liability in the context of an asset purchase is when the purchasing entity is merely a continuation of the selling corporation. The parties may use the purchase agreements to specify which liabilities transfer with assets. Therefore, diligence requires a nuanced inquiry into the facts and circumstances regarding the specific M&A transaction.

Quick Glance

- Companies subject to the US Foreign Corrupt Practices Act (FCPA) should conduct due diligence on target companies that are not subject to the FCPA to avoid issues of successor liability.
- Conducting due diligence in China can be difficult because many companies there have a low appreciation of the importance of anticorruption compliance.
- Incomplete or falsified records, the lack of public information, and employee reluctance to aid investigations can hinder due diligence efforts.
- Companies conducting due diligence can create checklists and conduct interviews in a culturally sensitive manner to overcome these obstacles.

Acquirers should consider conducting anticorruption due diligence in various M&A contexts. If the acquirer itself is already subject to the FCPA anti-bribery provisions or the books and records provisions, it should consider due diligence because of concerns about liability for pre- and post-acquisition conduct. (If the acquirer is not subject to the FCPA, but the target company is, the acquirer should conduct anticorruption due diligence because it may be responsible for the past unlawful conduct of the newly acquired subsidiary.) Minority investors looking for short-term exit channels may want to consider the impact of FCPA noncompliance on IPOs, because once a Chinese company becomes an issuer under US securities laws, it is subject to the FCPA. Financial advisors to M&A deals should also consider FCPA due diligence for reputational reasons.

In most cases, sellers and buyers need to conduct anticorruption due diligence. Usually, buyers seek to avoid acquiring liability for past or present FCPA violations, ensure that the seller covers the costs of violations, and maintain the maximum value of the acquired entity by retaining key personnel, contracts, markets, and relationships. Sellers need to conduct due diligence to ensure that their disclosures regarding material contractual provisions, such as representations, are not misleading and to assess their FCPA compliance programs and other internal controls to determine whether the sales price could be challenged because of unknown FCPA problems.

The DOJ's opinion released in June 2008 regarding Halliburton's approach to an M&A transaction also indicates the DOJ's expectations of parties seeking to avoid potential FCPA liability in a proposed M&A transaction. Halliburton requested the release of the opinion procedure pertaining to its proposed acquisition of Expro International Group plc because, as a result of UK bidding restrictions, Halliburton had insufficient time and inadequate access to information to complete standard anticorruption due diligence before closing. The opinion indicates that the DOJ expects US companies in similar circumstances to go to significant lengths to avoid potential liability when entering into transactions, particularly when they are unable to establish that foreign transaction parties are free of corrupt behavior. At the same time, the opinion shows that the DOJ recognizes that US companies' due diligence may have to accommodate the legal restrictions of other countries.

Strategies for effective anticorruption due diligence in China

Conducting effective anticorruption due diligence is particularly difficult in China for several reasons. First, acquisition targets in China tend to have a low appreciation of the importance of anticorruption compliance. Second, with the high employee turnover of recent years, most Chinese companies have not kept complete records. Third, most Chinese companies have weak internal control systems and may have falsified accounting records. Often, different versions of accounting books are kept for different purposes. For example, one version of the accounting books may record every payment the enterprise makes for internal record-keeping purposes, while another version of the accounting books hides illegal payments and is shown to auditors or officials during inspections. Also, the lack of public information resources makes independent checking of relevant company information difficult. Nonetheless, there are ways to overcome or mitigate these difficulties.

Identify high-risk areas

The first step of effective anticorruption due diligence is to conduct an initial risk assessment of the target company to identify areas of high risk or actual corruption violations. It is important to identify and distinguish different types of M&A targets in terms of FCPA implications. For example, in China, if a target company is in a sector that is state-owned or -controlled, such as energy, oil and petrochemicals, telecom, transport, auto, construction, financial services, or healthcare, the businesses of the target may have frequent interactions with government agencies or government officials for regulatory approvals. In such cases, this aspect of the target business should be a focus of the due diligence.

Understand the target's business model

As part of the initial assessment, acquirers should seek to understand the operation of the target's business. For example, an acquirer should check whether the target relies heavily on sales through joint ventures with Chinese state-owned enterprises, distribution partners, agents, consultants, or other intermediaries because corrupt payments are often made to government officials through these channels. The acquirer needs to analyze the target's existing internal control and accounting systems, review the target's organization chart, and identify all employees who interact with government officials.

Interview employees with care

Interviewing identified employees (prior to the acquisition, if possible) is a vital step, especially since information is rarely recorded in written documents in China. Even if employees are made available, obtaining useful information from them may be difficult. This is because most Chinese companies are accustomed to doing business through a network of value-laden relationships, and cultivating such relationships through gifts and entertainment is not necessarily considered unethical in China. Under such circumstances, discussing potential corruption issues with Chinese employees, and sometimes even associating the word "corruption" with their familiar business practices, may offend and alarm

What Constitutes an FCPA Violation?

In broad terms, the Foreign Corrupt Practices Act (FCPA) prohibits corruptly promising, giving, authorizing, or offering anything of value to foreign government officials, political parties or party officials to obtain, retain, or direct business. The jurisdictional reach of the statute is broad—the anti-bribery provisions apply to "issuers," which include US public companies and non-US companies that issue American Depository Receipts, and "domestic concerns," which include corporations and other businesses that have their principal places of business in the United States or are organized under the laws of a US state or territory, US citizens and US resident aliens (wherever located), and non-US corporations and non-US citizens who commit acts in the United States in furtherance of an FCPA violation.

A "corrupt" payment can include any effort to improperly influence virtually anything that a foreign official does in his or her official capacity, from approving a contract to granting licenses related to investment services, issuing visas, acting on tax matters, or making decisions in connection with government approval of a merger or acquisition. "Something of value" is construed broadly and encompasses gifts, meals, entertainment, and travel and accommodations for foreign officials. Payments made indirectly to foreign officials through third parties, such as agents, are also prohibited if they could not be made directly.

The FCPA's "books and records" and "internal controls" provisions require issuers to keep accurate books and records in reasonable detail that reflect the true nature of all transactions, regardless of whether the transactions pertain in any way to corruption. Parent companies are strictly liable under the civil provisions of the FCPA enforced by the SEC for ensuring that their subsidiaries, affiliates, and controlled joint ventures comply with these books and records provisions.

—*Richard Grime and Bingna Guo*

them. To maximize the benefits of such interviews, interviewers should maintain good relations with the executives and potential interviewees and show sensitivity to cultural differences by, for example, clarifying the context of the investigation in the native tongue of the locality and engaging in a few pleasantries before asking formal investigation questions. It is also helpful for the investigator to appreciate and understand the accepted local business practices and not to appear judgmental.

For an investigation of Chinese companies, sometimes obtaining senior management's support may facilitate the investigator's interview work, as employees tend to defer to higher-level managers and officers. Interviewers will also need to understand local attitudes toward investigations, as anticorruption due diligence is a foreign idea to many Chinese employees, and they may see it as an adversarial proceeding more than a neutral internal investigation. And since some US legal concepts, such as attorney-client privilege, are not available under PRC law, interviewers should emphasize confidentiality to interviewees and give them clear instructions not to discuss the interview with others.

Create a due diligence checklist and look for red flags

Information from the initial assessment is critical for designing a due diligence checklist that is suitable for Chinese companies. Usually, the key areas of the target company to look into during due diligence include: sales and marketing expenses; travel and entertainment expenses; the shareholding structure of the target, its subsidiaries, and affiliates; employee records and the target's salary and bonus payment system; use of consultants and agents; corporate governance culture and structure; and charitable donations. Bribes in China can take many forms. In addition to traditional suspicious categories of expenses, such as rebates, sponsorships, and entertainment, gifts that come in the guise of traditional customs, such as elaborately packaged moon cakes, may entail FCPA risks.

The acquirer needs to check whether any shareholders of the target are government officials or associate directly or indirectly with government officials. Such indirect associations may take the form of beneficiary shareholding arrangements, such as using nominee shareholders to hold shares on behalf of the real beneficiaries through trust arrangements. Also, some Chinese companies may use fictitious tax receipts or salary payments to nonexistent "ghost" employees to mask bribery payments. All of these are red flags that merit investigation during the due diligence process.

In addition, conducting an independent check of red flag issues identified in the key areas and the target companies' legal compliance through public information sources is an important supplement to the due diligence process. Although China's public information search system is underdeveloped, releases from relevant PRC government agencies, such as the National Bureau of Corruption Prevention (www. nbcp.gov.cn/article/ English/Comprehensive Infomation/), can be valuable. Lists of convicted bribers are available for public search at most provincial-level procuratorial organs. Relevant industry regulatory authorities, such as municipal health bureaus, compile blacklists of companies caught in bribery. If public information is unavailable, employing private investigators may also be necessary. In all cases, companies should retain counsel familiar with common Chinese corporate practices.

Lists of convicted bribers are available for public search at most provincial-level procuratorial organs.

With all of this information in hand, due diligence can move to the next stage, which typically includes more detailed interviews with the principals and the use of forensic accounting firms to verify the financial records of the target. Effective due diligence findings should be concluded by combining the investigative results from the concerted efforts of various teams.

Due diligence is a "must"

Investors acquiring companies in China must conduct anticorruption due diligence to avoid successor liability for past or potential corruption violations. Without such diligence, past FCPA violations could affect the timing and successful completion of M&A transactions. The risk of regulatory enforcement action and the resultant impact on the liability and reputation of the successor company may also be high. With appropriate strategies, a well-tailored due diligence effort can elicit sufficient information to determine an acquisition target's real and perceived risk of FCPA violations and the true value of the transaction. It can also help the acquirer develop reasonable expectations of any post-acquisition compliance costs. Finally, in cases where concerns about a proposed M&A deal cannot be clearly resolved, sophisticated counsel familiar with SEC and DOJ practice and well-versed in Chinese business practices should be used to weigh different options, from voluntary disclosure to a DOJ opinion request. 完

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Merger Control under China's Antimonopoly Law: The First Year

Continued from page 21

negotiated remedies to "reduce" the negative effects of the transaction but then notes that the agreed-upon remedies "fully eliminate" the adverse impact of the concentration.

Implications cast doubt

The implications of MOFCOM's substantive appraisal of these high-profile transactions under the AML are significant:

- MOFCOM's willingness to impose restrictive conditions on *InBev/Anheuser-Busch* and *Mitsubishi/Lucite,* and to prohibit *Coca-Cola/Huiyuan,* show that it is prepared to play an active enforcement role under the AML.
- MOFCOM's imposition of limitations on InBev/AB acquiring additional shares in named competitors was highly unusual from a Western antitrust perspective, particularly given MOFCOM's failure to identify any anticompetitive harm caused by the transaction. Similarly, the stipulation that Mitsubishi may not add MMA capacity in China is contrary to generally accepted antitrust principles. It is unclear how future additions of capacity could result in harm to consumers. This requirement may fuel suspicion that MOFCOM will use the merger review process to achieve goals unrelated to its mission.

MOFCOM's prohibition of *Coca-Cola/Huiyuan* was also widely criticized. The decision's reference to leveraging suggests that MOFCOM applied a conglomerate effects theory of the kind abandoned many years ago in the United States and applied by the European Community only rarely, cautiously, and in situations where the evidence has been compelling.

- Although MOFCOM's spokesperson stressed that the *Coca-Cola/Huiyuan* decision was based solely on competition law, the decision's references to the transaction's effect on domestic small and medium-sized manufacturers and the sustainable and healthy development of the Chinese fruit-juice drink industry suggest that industrial policy considerations played a significant role. If so, MOFCOM's approach could be consistent with the AML requirement that MOFCOM take account of the "development of the national economy" and "other considerations that may affect market competition as identified by the AML enforcement authority." In this regard, MOFCOM may have been influenced by recent publicity in China regarding the alleged negative effect of foreign acquisitions on prominent national brands, such as Mininurse, Nanfu, and Lebaishi.

That MOFCOM would consider the broader implications of notified transactions should perhaps be unsurprising because the AML requires MOFCOM to take broad economic factors into account. Nonetheless, the decision may give pause to Western companies considering acquisitions of high-profile Chinese companies, particularly companies with prominent local brands.

In all three transactions, the outcome demonstrates MOFCOM's willingness to use the merger-control process to address the possibility of future non-merger-specific harm. Although the government would have the power to review the prohibited future transactions or behavior if and when the need arose, MOFCOM preferred to prohibit the transactions now.

- All three published decisions are short, and MOFCOM's analysis is less clear and complete than comparable decisions under the EC Merger Regulation and US regulations. (Though the United States does not typically publish details regarding clearance decisions, the agencies do provide details regarding decisions to block a transaction or to clear it with conditions.) Notably, in *Coca-Cola/Huiyuan,* the decision does not describe how MOFCOM defined the relevant market or discuss the market shares of the parties or their competitors or whether the parties are close competitors.
- More generally, none of the decisions articulates a clear theory of harm with supporting evidence that would justify the outcome. On the other hand, MOFCOM's decisions in these three cases suggest that, from a procedural perspective, it takes a flexible approach to remedies. MOFCOM apparently suggested remedies to Coca-Cola, and there is no suggestion in the decision or in press reports that the submission of remedies was subject to particular formal or standard timing requirements. From a substantive perspective, there is confusion between the decision itself and a follow-up press release as to whether remedies under the AML need only alleviate, as opposed to remove, the anticompetitive effects of the transaction. 完

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An Engine of GROWTH

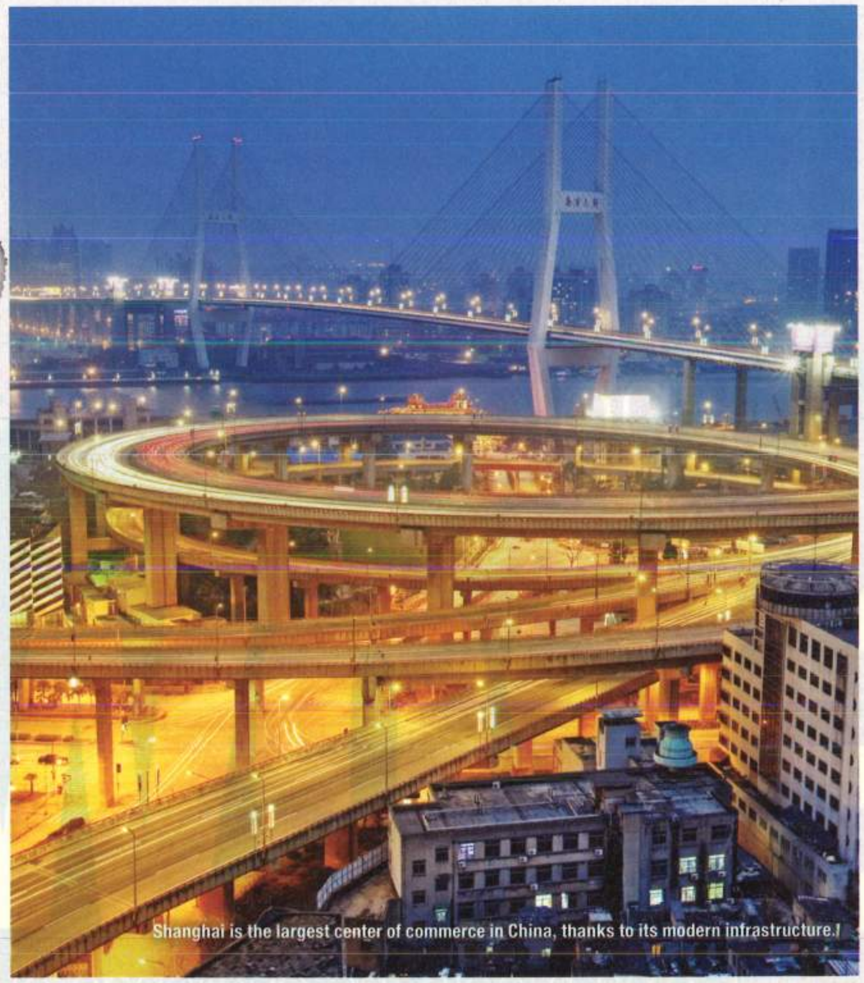
China meets the challenge of a global slump with a stimulus plan to kick-start its economy.

China

has responded to the effect of the world economic slowdown with enviable panache. Although exports plunged last year and millions of migrant workers went home to the countryside, China's government is forecasting 8% GDP growth in 2009. A first-quarter score of 6.1% indicates that the nation—aided by a far-reaching economic stimulus package—may be on its way to reaching that goal.

While GDP growth has stalled or fallen in most advanced industrialized countries during the global economic crisis, 8% would signal the slowest growth China has endured in a decade. In 2007, the economy swelled at a 13% rate, and in 2008, even as the world economy began to suffer the effects of the financial meltdown, the Middle Kingdom managed to eke out a 9% increase, its lowest since 2001.

China's climb to the No. 3 economy in the world, after the United States and Japan, may be the fastest such ascension in history. The world's most populous country remade itself by averaging real GDP growth of almost 10% a year since market reforms were launched in 1978. But by becoming the world's factory, China also exposed itself to the fluctuations of the global economy. As demand from China's major markets in the U.S. and Europe collapsed last year, export growth slowed by a third to $1.4 trillion, still $200 billion more than in 2007.



Shanghai is the largest center of commerce in China, thanks to its modern infrastructure.

Last fall, China's central government responded to the global slowdown with a $585 billion stimulus package designed to keep the economy growing. A lot of the money has been poured into infrastructure: railroads, highways, bridges, and airports. "Many economists say that China is the gold standard in stimulus packages," says John Frisbie, president of the U.S.-China Business Council (USCBC), an association of 220 U.S. companies that do business in China. He adds that the plan may offer great opportunities for foreign equipment manufacturers whose own domestic markets have slumped, especially markets related to infrastructure.

One reason for China's resilience, some economists say, is that the country is less dependent on the export market than is commonly assumed, because relatively little value is added to imported products on China's assembly lines. "China is not an export-led economy; it is a continental economy driven primarily by domestic investment and consumption," says Andy Rothman, China macro-strategist for CLSA Asia-Pacific Markets, a brokerage firm based in Hong Kong. His firm reported in May that manufacturing demand was up for a second consecutive month in China, driven largely by domestic consumption.

Despite China's relative success in weathering the economic storm, the country's leaders seek to reduce future vulnerabilities and want to grow a more robust service sector. Up to 70% of GDP in advanced countries depends on services; in China it's just 40%. In February, the central government ordered various

A Global Showcase

At 52, the China Import and Export Fair has become one of the world's grandest events.

In this vast land of 1.3 billion people, everything is done in a grand manner. Remember the more than 15,000 who performed at the opening ceremonies of the 2008 Summer Olympics in Beijing? The China Import and Export Fair, also known as the Canton Fair, is no exception. This twice-a-year exhibition has gotten so huge that the spring and autumn sessions are each divided into three phases, each lasting five days, to accommodate the tens of thousands who want to exhibit their wares in the cavernous Liuhua Complex in Guangzhou, capital of Guangdong Province in southern China.

This year's spring exhibition—the 105th fair—featured nearly 56,000 booths set up by more than 22,000 Chinese manufacturers who took turns occupying 1.1 million square meters of exhibition space over two weeks. The event, which ended May 7, attracted more than 165,000 overseas buyers, including 9,035 retail chains and other businesses from the United States. The 15-day session generated $26.2 billion worth of export contracts—the equivalent of 11% of the $245.5 billion that Chinese companies exported in the first quarter of 2009.

The Canton Fair is a magnet for international investors.

Huge as they are, the numbers are actually smaller than those generated at the previous session last autumn. "A modest decline of 5.2% was seen in the number of overseas buyers," says Mu Xinhai, the fair's deputy secretary general. Export sales were down 16.9%, which is not surprising given the global economic crisis and H1N1 swine flu problems in Mexico, the U.S., and other countries this spring. "In all, everything went well in a balanced way," reports Mu, "with better-than-expected results, which made great contributions to stabilizing foreign trade, maintaining economic growth, expanding domestic demand, and adjusting the economic structure."

Jostling for Attention

Launched back in 1957, the Canton Fair mirrors China's journey from basic manufacturer to the value-added export powerhouse it has become. At the latest exhibition, luxury Zhonghua sedans and snazzy Loncin Group motorcycles jostled for attention alongside gigantic flat-panel TVs, computers, and other consumer electronics. Export orders for machinery and electronic products topped $11.3 billion, nearly half the total, followed by light industrial products ($8.4 billion) and textiles and garments ($3.2 billion). An e-business platform called Canton Fair Online, a recent addition, had 190 million visits during the Fair, up 2.5% from last autumn, although online orders fell 13.7% to $510 million.

The spring fair was a buyer's market. Five years ago, suppliers declined to accept orders for fewer than five container loads, a foreign visitor told a Hong Kong newspaper. Now, they are willing to accept just one. Prices were generally lower, as well, as manufacturers passed the falling costs of materials, labor, and other expenses on to customers. Fair organizers also rolled out a plusher red carpet: a newly established customer service center helped trim the number of complaints to a fifth of last autumn's total.

Buyers will be expecting the same level of service, wide range of products, and attractive pricing at the 106th Canton Fair, which will run from Oct. 23 to Nov. 4 this year. The autumn event will be closely watched for another reason: Given China's central role in international trade, the volume of export orders will indicate whether the hints of economic recovery being seen today will produce more buying for the Christmas season, confirming hopes of a turnaround in the world's economic fortunes in 2010. ●

ministries to promote the development of the service sector in 20 Chinese cities. As incentives, the government offers a 15% corporate tax rate for enterprises that enter the sector, zero sales tax on outsourced services, and a $658 subsidy for the salary of every college graduate signed to a one-year contract.

Special enterprise zones that have traditionally hosted domestic and foreign manufacturers are also turning their attention to services. "Our focus is manufacturing," admits Ni Xiang Yu, vice chairman of TEDA (Tianjin Economic-Technological Development Area), located near China's third-largest city. TEDA hosts Toyota, Samsung, Motorola, and 4,600 other foreign manufacturers, "but we welcome tertiary industries like banking, insurance, and financial services."

Foreign companies in China are already finding opportunities in services. Amdocs, based in Chesterfield, Mo., won a contract in January to provide customer management and billing services to China Telecom's 35 million mobile phone subscribers. The world's largest landline company (220 million customers) acquired a wireless arm when the government rejiggered the world's biggest cellphone market (600 million customers). Job Brokers, a Tempe, Ariz. employee recruitment firm, announced in April that it would open an office in Beijing to serve U.S. companies operating there.

The renewed focus on services is one step in China's efforts to strengthen its economy. Some foreign experts propose a more ambitious "rebalancing" that includes liberalizing the financial sector and promoting higher consumer spending. CLSA's Rothman believes the government must provide more security before China's tight-fisted consumers loosen their purse strings. On average, Chinese consumers save around 25% of their income; the national savings rate is 47% of GDP. "Chinese households have been taxing themselves with a high savings rate to compensate for the absence of a formal social safety net," he says. "They save to ensure they have funds for education, health care, and retirement." It will take years, Rothman believes, to create a system that is well-funded and trusted.

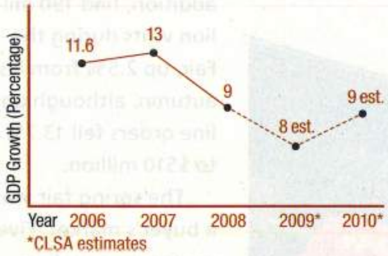
Nicolas Lardy, senior fellow at the Peterson Institute for International Economics, says manufacturers in China have a low tax burden. Although profits are up, most enterprises pay no dividends to their owners. "As a result, businesses have a lot of retained earnings, all of which are reinvested," says Lardy. "Some of that should be taxed away to reduce the rate of investment, which is an important part of rebalancing."

China's vast domestic market retains its appeal to foreign manufacturers. Foreign direct investment rose 23% to $92.4 billion in 2008 despite the global slowdown. For example, FlowServe, an Irving, Texas manufacturer of valves and flow-control equipment, announced in March that it had formed a joint venture with China's largest valve maker, Sufa Technology Industry Co. The new venture will manufacture products exclusively for China's growing nuclear power industry.

John Frisbie of the USCBC says China will continue to be an important business partner for U.S. companies after the global recovery. "The U.S. and China are already greatly interdependent," says Frisbie. In a survey last year, 88% of his members indicated they were turning a profit in China. Frisbie says USCBC has so far been encouraged by the Obama administration's approach to its third-largest trading partner. "America's current economic challenges may cause temporary shifts in U.S trade with China, but the long-term trends are clear—and the need for a clearheaded, stable approach to China is more important than ever."

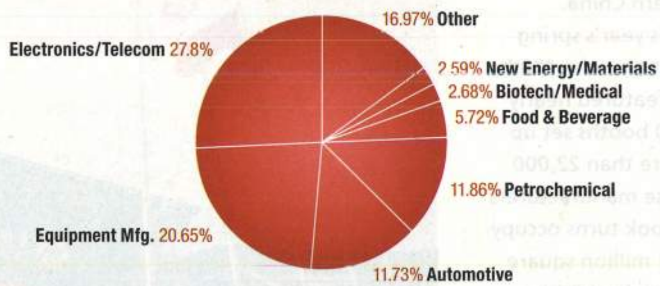
A lot of the focus in the past has been on imports from China, says Frisbie, but the economic slowdown has made Americans aware of another aspect of U.S.-China trade: "There's a realization now that we also sell a lot of products to China." In 2008, according to USCBC, U.S. exports to China totaled $71.5 billion. —**Joel Dreyfuss**

China's Economy: A Quick Rebound?



Source: 2006–2008 OECD Economic Outlook; CLSA Asia-Pacific Markets

TEDA's Industrial Output



Source: TEDA Report Q1 2009

China's Boomtown

For a glimpse of one of the world's fastest-growing manufacturing zones, visit the Tianjin Economic-Technological Development Area.

Ni Xiang Yu, the voluble vice chairman of the Tianjin Economic-Technological Development Area, recently delivered a pep talk to his hometown soccer team. "You have to rank first," he says he told the players for China's third largest city. "You cannot be sixth or eighth; that is not our culture."

The TEDA soccer team has yet to reach the top spot in China's fledgling professional soccer league, but Ni's tone provides a glimpse of the competitive spirit that drives TEDA to retain its status year after year as the most productive of China's special economic zones. Last year, companies in the zone produced $55 billion (377 billion yuan) in sales, up 9.6% over 2007.

TEDA is a sprawling area that nearly surrounds Tianjin, a city of 11 million. Covering 100 square kilometers (39 square miles), the zone hosts more than 10,000 companies, including 4,600 foreign enterprises such as Motorola, Otis Elevator, John Deere, Coca-Cola, GlaxoSmithKline, Samsung, and Toyota. TEDA is a 90-minute drive from Beijing and well-served by major highways, trains, and the Port of Tianjin.

The special area reports that direct foreign investment in the first quarter of 2009 totaled $1.4 billion, up 16.5% over the same period last year, and 25 new foreign enterprises signed contracts to set up in the zone, including Japanese dairy manufacturer Yakult. Another 35 foreign companies already in TEDA have indicated they will expand their operations, including U.S. tractor maker John Deere, which broke ground for a test center earlier this year, and Toyota Motor, which began rolling Rav4 SUVs off its assembly line. Ni says the goal for TEDA this year is to reach 25% growth. "We cannot slow down," he says. "China needs investment."

TEDA's sales pitch is centered on customer service. "We're all about: 'How we can support the customer?' "says Ni. He points out that key Chinese ministries, including the tax authorities and foreign registration offices, operate branches at TEDA. It also helps that Tianjin is one of several Chinese cities administered directly by the central government, and that it happens to be the hometown of Chinese Premier Wen Jiabao. Ni promises foreigners help in navigating Chinese government bureaucracy. "We are the fastest," he says. "If all the documentation is ready, according to laws and regulations, we are the best [in speeding approvals]." One measure of customer satisfaction, says Ni, is repeat business. About 40% of new investment in TEDA, he says, comes from existing customers like Samsung and John Deere.

TEDA'S botanical garden is a natural retreat from the urban landscape.

TEDA

Originally set up as a manufacturing center, TEDA is determined to broaden its base. Earlier this year, Chinese leaders announced a series of measures, including lower corporate taxes and a sales tax moratorium, to promote the development of a services industry. "We welcome tertiary industries like banking and insurance," Ni assures.

As China begins to embrace green technologies, TEDA is well positioned to benefit. The zone already hosts a number of solar- and wind-power manufacturers, including Danish wind turbine maker Vestas, which recently announced a $90 million expansion of its facilities in China. "We are proud to host so many of the best businesses from all over the world," says Ni.

China Foto Press

Reforms will focus on improving care at the grassroots levels, such as this medical reimbursement office in Gansu.

China's Healthcare Reform

Reform plans promise significant change, but what does that mean for foreign healthcare players?

James A. C. Sinclair

Whenever Wang Hui, a product manager in Shanghai, needs to consult a doctor, it means hours queuing for a few minutes of an overburdened doctor's attention. Yet Wang Hui is relatively well off. His father, a factory worker in Shanghai's suburbs, does not trust his local clinic and prefers to make a day-trip to a downtown hospital. His uncle, a farmer on the outskirts of Shanghai, worries about being able to afford medical expenses and puts up with physical discomfort instead.

China's healthcare system is deeply flawed, and Chinese citizens increasingly expect rapid improvement in the accessibility and affordability of healthcare. With the release of the new healthcare reform plan in early April, China is at a turning point. Even though its implementation will be an arduous and prolonged struggle, the reform plan has important implications not just for China's healthcare sector but also for the country's economic development. Only when Chinese citizens stop worrying that sickness means impoverishment will there be less precautionary saving and a greater readiness to spend. This makes the healthcare reform plan another building block in support of a sustained consumption boom in China.

China's reform plan

China released two healthcare reform documents in early April. The first, the State Council's Opinions on Deepening Healthcare System Reform (Framework Plan), is a broad document that sets the reform framework through 2020. The second, the Ministry of Health's Implementation Plan for Immediate Priorities in Healthcare System Reform, 2009–11 (Implementation Plan), provides a more detailed roadmap for the next three years. The Implementation Plan is comprised of five major programs.

Universal coverage of basic medical insurance

The government aims to extend each of the three main medical insurance schemes to cover 90 percent of the population by 2011 (see p.34). In particular, the Urban Employed Basic Medical Insurance scheme will be expanded to cover students, migrant rural workers, temporary contract workers, and retirees from closed-down and bankrupt enterprises, in addition to the urban employed.

In 2010, The government will also raise subsidies for health insurance premiums to ¥120 ($18) per participant in the Urban Resident Basic Medical Insurance and New Rural Cooperative Medical Insurance schemes, which together cover 900 million people. The schemes' service scope, reimbursement level, and maximum amounts payable will gradually be raised to narrow the huge differences in benefits provided by the various schemes.

Finally, China will gradually integrate the three main medical insurance schemes to accommodate population mobility. Medical insurance handling bodies will negotiate with healthcare providers to contain costs, and direct settlement systems between medical insurance handling bodies and healthcare providers will be created.

Establishment of an essential drug system

The government will publish a National Essential Drug List (NEDL), expected to contain 400–700 items with many low-cost generics and traditional Chinese medicines. The central government will guide prices, provincial governments will be responsible for procurement and distribution, and basic medical insurance will cover prescriptions. The government also aims to step up supervision and sampling to ensure a safe supply of drugs.

Provincial governments will run open tenders for drug procurement and drug distribution in their region. The tenders will be open to private and foreign participants, supposedly in fair competition. Provincial governments may replace up to 10 percent of the drugs on the NEDL to tackle diseases that are more prevalent in their locality.

Quick Glance

- China's ambitious healthcare reform plans aim to provide coverage to 90 percent of the population by 2011.
- The plans focus on improving healthcare at the grassroots level and include a list of essential drugs.
- To take advantage of this shift in focus, foreign companies may need to think about how they can provide medical goods and services to the mass market.

Purchasing prices of all drugs on the NEDL will be set within central-government guided retail prices. Grassroots healthcare providers may not levy a surcharge on drug sales. (In rural areas "grassroots healthcare providers" includes county hospitals, township health centers, and village clinics. In urban areas they include community health centers and community health service stations.) Basic medical insurance will cover prescriptions of drugs on the NEDL at a much higher reimbursement level than non-essential drugs.

The government will require all healthcare providers and retail pharmacies to stock and retail drugs on the NEDL, and grassroots healthcare providers may stock and retail only drugs on the NEDL. All other healthcare providers will be encouraged to use drugs on the NEDL as their "primary choice remedy." Thus, the NEDL is expected to largely define the drug market in all but the urban hospitals.

Improved primary care infrastructure

China will construct and renovate county hospitals and health centers, as well as train and rotate healthcare professionals to staff them. This activity will focus on grassroots healthcare providers.

To improve the quality of China's grassroots healthcare professionals, a training program will cover 360,000 healthcare professionals for township health centers, 160,000 for community health centers, and 1.4 million for village clinics. The university fees and student loans of medical graduates who choose to work in township health centers will be subsidised, and doctors in urban hospitals will earn promotions only if they have practiced one year in rural regions. Moreover, urban hospitals must support county hospitals on a long-term basis to transfer expertise.

To strengthen the primary care system, patients will be encouraged to visit health centers as a first point of consultation, or receive visits from mobile medical teams, and be referred to hospitals only if they have secondary or tertiary care needs. In addition to improving accessibility, the health centers will ensure the affordability of their primary care services by using "appropriate" techniques, equipment, and essential medicines.

Pilot reform of public hospitals

The government will attempt to improve the governance of public hospitals and gradually reform their revenue structure. Critical here will be the reduction in drug surcharges and shift to government subsidies and fees-per-service only. The proportion of "non-public" (or private) hospitals, although not necessarily for-profit hospitals, will also increase.

Equitable access to public health services

The government will strengthen the prevention and control of disease with various community-level programs, as well as the launch of a new television station for health education.

To strengthen mother, infant, and elderly care, pregnant women will receive prenatal and postnatal checkups, and those younger than 3 and older than 65 years old will be entitled to regular examinations. (As these checks are considered public health efforts, the government will likely fund them directly.) China will also continue or launch major public health programs to prevent or control major diseases. Programs to be continued include the national immunization program and the prevention and control of HIV/AIDS, while programs to be launched include the provision of folic acid for pregnant women to help prevent birth defects and supplementary vaccination against hepatitis B for those under 15 years old.

Implications for multinational healthcare players

Once the reforms get under way, opportunties for multinational healthcare companies will likely remain centered around drugs, devices, and services offered in Grade 3 hospitals (see Figure). For companies that can provide low-cost medical products and services, however, China's plans to make healthcare accessible and affordable to its vast population may offer significant potential.

Pharmaceuticals: A switch to low-cost generics

When the NEDL is published, pharmaceutical multinationals will scan the list for matches against their own portfolios but probably will not find many patented or innovative drugs. Instead, the real opportunity will be in generics. As basic medical insurance will cover drugs on the NEDL, more Chinese citizens will purchase drugs, creating a high-volume demand for low-cost generics. Tapping this demand will require pharmaceutical multinationals to reconfigure their portfolios and adjust their pricing strategies, as well as rethink their target customers and means of reaching and serving those customers. The scale of the challenge should not be underestimated. Even China's largest drugs distributors, SinoPharm Group and Shanghai Pharmaceutical Co., do not have the infrastructure to cover grassroots healthcare providers thoroughly. Few pharmaceutical multinationals will have the appetite for such a thin-margin, mass-market play.

When NEDL is released, domestic generic drug makers will perhaps be best positioned to benefit from the reform. They will likely strengthen their portfolios and rapidly expand sales and distribution networks to reach grassroots healthcare providers and rural regions. As larger players strive for economies of scale to drive down costs and improve competitiveness, the industry will consolidate.

For most pharmaceutical multinationals, China accounts for a relatively small share of their global business. In the short term, most will likely take a cautious approach to the reform and continue to focus on the 1,200 Grade 3 hospitals. These hospitals may still impose drug surcharges and will still cater to the high end of the market, which can better afford patented and innovative drugs. The introduction of the NEDL is unlikely to have an immediate impact on business with these hospitals, and the reform of their revenue structures will be slow and incremental.

Medical devices: Domestic players to benefit most?

The reform plan is generally good news for medical device makers. The growth in public spending, especially on the construction and upgrade of healthcare facilities, will be an obvious demand driver for medical equipment, including

China's Main Basic Medical Insurance Schemes

China has three main basic medical insurance schemes, which vary greatly.

■ **Urban Employed Basic Medical Insurance (UEBMI)**, established in 1998, is employment-based and covers urban workers only. It consists of a pooled fund for inpatient stays and individual medical savings accounts for outpatient visits. Payroll taxes paid by employers and employees finance the UEBMI. Contributions are equivalent to 14 percent of annual salary in Shanghai, but only 8 percent in western provinces. About 200 million out of a total of 250 million urban employed participate in UEBMI.

■ **New Rural Cooperative Medical Insurance (NRCMI)**, established in 2003, consists of a pooled fund for inpatient stays and is financed by various government bodies and participants. Contributions are commonly ¥50 ($7) in western provinces, split ¥10 ($1.50) from participants, ¥20 ($3) from provincial government, and ¥20 from the central government. Benefits are limited, with reimbursement rates that can be as low as 30 percent for impatient expenses, and operated on a "pay first, claim later" basis. Nevertheless, the scheme has expanded rapidly, and an estimated 800 million out of a total of 850 million rural citizens participate in NRCMI.

■ **Urban Resident Basic Medical Insurance (URBMI)**, established in 2007, covers the urban population not covered by the UEBMI scheme, such as children and students. It consists of a pooled fund for inpatient stays and does not cover outpatient visits, except in wealthy regions. Various government bodies and participants finance URBMI, with total contributions per participant standing somewhere between UEBMI and NRCMI levels. Benefits are limited, and significant co-payments are required. Coverage is supposed to be available in all cities by the end of 2010, and an estimated 100 million urban residents already participate in the URBMI.

—*James A. C. Sinclair*

medical devices. But with the government generally encouraging the substitution of expensive imported medical devices with cheaper domestic versions, domestic medical device makers will perhaps benefit most from the reform.

Nevertheless, healthcare reform may still generate new demand for advanced medical devices. As drug surcharges are phased out in public hospitals, these hospitals will look to fees-per-service to compensate for lost revenue. As a result, there will be greater use of diagnostic, therapeutic, and surgical devices and technologies that command relatively high services fees.

Healthcare IT: Sooner or later

Information technology (IT) investment in China's healthcare sector has been relatively weak, and the current level of computerization is lower than in many other countries. This is because market-oriented reforms led to healthcare providers investing in medical equipment and devices that could directly generate revenues. IT is set to play a much more important role, however, as China's healthcare system will not achieve accessibility and affordability without it.

One of the first priorities will likely be the establishment of an electronic medical record system, which will facilitate patient data sharing among healthcare providers. Next up could be the establishment of regional health networks that would integrate the hospital, clinical, and radiology information systems of China's highly scattered and fragmented healthcare providers. Numerous pilot projects are already under way in different parts of the country, such as the Shanghai Hospital Union project, which covers 23 hospitals and numerous health centers in Shanghai. Further down the road, a nationwide, unified health network that integrates health administrators, healthcare providers, medical insurers, and the public health system, among others, is a possibility.

Healthcare provision: Is this really privatization?

Private hospitals currently account for less than 15 percent of China's total. While public hospitals will remain dominant, the proportion of private hospitals will rise. The Implementation and Framework plans remain vague on the opportunities for private and foreign healthcare providers, however. Though it is clear that private investment in non-profit hospitals will be encouraged and diversity of ownership—including foreign ownership—is envisaged, the plans do not directly encourage private investment in for-profit hospitals. Moreover, the reform plan does not address the significant entry barriers that exist for foreign healthcare providers. (Because foreign investment in healthcare provision is restricted, foreign ownership is limited to 70 percent, a minimum investment of ¥20 million [$2.93 million] is required, and branch organizations are prohibited.)

Healthcare provision with public health functions, such as preventive services and infectious disease treatment, will likely remain in the hands of the government, as will healthcare provision toward the top end of the scale (Grade 3 hospitals) and the bottom (health centers and village clinics). Apart from the small but growing market for premium care, the main opportunity for foreign healthcare providers could be hospitals that handle routine patient care, such as

Continued on page 52

Levels of Healthcare Providers

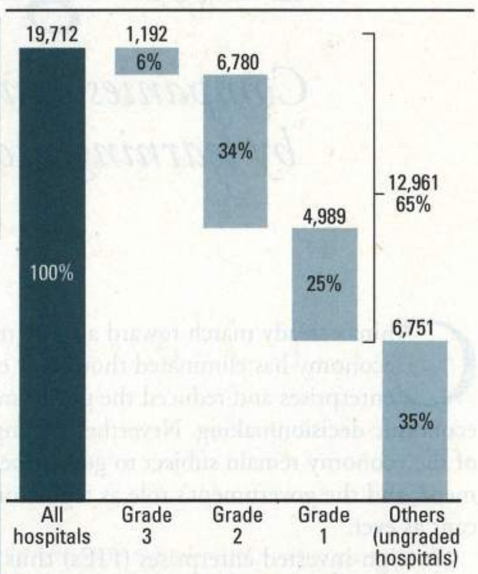
Healthcare providers	Rural network	Urban network
Province	—	Provincial hospitals
Prefecture	—	Municipal hospitals
County	County hospitals	District hospitals
Township	Township health centers	Community health centers
Village	Village clinics	Work unit clinics, community health service stations

Source: PRC Ministry of Health

China's Hospital System

Hospital tiers	Definition
Grade 3 (highest)	■ These hospitals provide comprehensive medical services, including clinical specializations, integrated with teaching and research functions. ■ Catchment area covers multiple communities with >500 beds. ■ Generally includes provincial hospitals and municipal hospitals in bigger cities.
Grade 2	■ These hospitals provide comprehensive medical services plus basic teaching and research functions. ■ Catchment area covers several communities with 100–500 beds. ■ Generally includes municipal hospitals in smaller cities, as well as district and county hospitals.
Grade 1	■ These hospitals provide basic medical services. ■ Catchment area covers a <100,000 people community with <100 beds. ■ Generally includes township hospitals in small towns.

Hospital Number Breakdown by Tier, 2008



China Foto Press

Officials in Jinan, Shandong, meet with local doctors.

Understanding China's Changing Civil Service

Companies can improve their government relations by learning more about China's new civil servants

Kenneth Jarrett and Lie Huihan

China's steady march toward a more market-based economy has eliminated thousands of state-owned enterprises and reduced the government's role in economic decisionmaking. Nevertheless, important sectors of the economy remain subject to government management, and the government's role as regulator is as significant as ever.

Foreign-invested enterprises (FIEs) thus still need to work with PRC government stakeholders. This interaction takes multiple forms since the government wears many hats: regulator, competitor, partner, and customer. In addition, more government bodies now intersect with foreign entities than ever before. Foreign affairs was once the exclusive province of China's ministries of Foreign Affairs and Commerce, or was relegated to the network of foreign affairs offices scattered across the country. Today, virtually all government bodies—including those with specialized functions and at lower levels—find themselves in contact with FIEs, foreign residents, and even foreign governments.

But today's government officials differ from their predecessors. FIEs should understand China's civil service reform process and the varying degrees to which it has penetrated the Chinese bureaucracy, so that they can interact effectively with government officials, especially at the central and provincial levels.

Civil service reform: An incremental process

The gradual professionalization of the PRC government reflects a dynamic interplay of social, economic, and political factors. To respond to the massive social changes of the last 30 years, the government has made major efforts to enhance its legitimacy and governing capability by promoting efficiency, meritocracy, and transparency—and reducing secrecy and favoritism. Reform efforts have accelerated as the government has become composed of and scrutinized by an increasingly well-educated and vocal population with ever-growing and ever-diverging interests.

Quick Glance

- The PRC government has implemented many changes to upgrade its civil service, including making recruitment and promotion merit-based and improving training.
- Companies should understand China's civil service reform process so that they can interact effectively with government officials.
- Companies should learn more about the officials they meet, understand their backgrounds, and know how they are evaluated.
- Officials from any generation may hold traditional views.

Recruitment and promotion

In recent years, China's recruitment and promotion procedures have become more meritocratic.

Recruitment China reinstated the civil service examination for all junior positions in 1993, an important milestone in the movement toward a transparent and meritocratic recruitment process based on clearly defined criteria. Today, the exam attracts huge numbers of applicants. In 2008, about 775,000 people took the exam, competing for roughly 13,500 positions and marking a 21 percent increase in test takers over 2007. The ministries with the largest number of applicants include the Ministry of Commerce, Ministry of Foreign Affairs, and National Development and Reform Commission.

Promotion Promotion decisions, too, are now less dependent on personal connections. Once accepted into the civil service, officials are subject to more professional evaluation processes as they move upward. For example, the government has made limited use of peer review and public-opinion polling and added a more comprehensive assessment process in a 2006 Chinese Communist Party (CCP) Organization Department document (The Method of Comprehensive Cadre Evaluation that Embodies Requirements of the Scientific Development Concept). This is a marked departure from the PRC's early years, when class background and ideological correctness were the main criteria for promotion. CCP membership is still an important factor—indeed, most senior-level officials, whether in municipal, provincial, or central government, are party members. But there are some notable exceptions, such as Health Minister Chen Zhu and Science and Technology Minister Wan Gang.

In 2002, the party's Central Committee introduced Regulations on Selecting and Appointing Party and Government Leading Cadres, which allow public consultation in the promotion process for leadership positions. Under the regulations, government agencies should announce decisions on newly promoted leaders throughout the relevant government agency, providing peers with an opportunity to object to the promotion. Since the opportunity for peer review occurs only after a decision has been announced, public rejection and rescinding of promotion decisions are rare. Another change in 2002 was the addition of a new "public bidding" procedure for vacant leadership positions that allows any interested candidate to apply for a new vacancy. The government uses the procedure infrequently and mainly for mid-level positions.

The application of more rigorous standards has also been apparent for senior appointments at the local level. Candidates for leadership posts at the county-chief level or higher must meet standardized minimum requirements—such as a bachelor's degree, specified training programs at the CCP Central Committee School, and experience in two posts at a level of leadership immediately lower.

Performance assessment In the early 1980s, as China began to pursue economic reform and modernization, job performance was judged largely on economic performance as defined by gross domestic product (GDP) growth. Growth still counts today, but less than in the past.

The 2006 Organization Department document modified the cadre evaluation system significantly by linking it directly to President Hu Jintao's "scientific development" concept—a guiding principle that advocates comprehensive, sustainable economic and social development that fosters more balanced and equitable growth. The document ushered in two changes. First, it outlined a six-step evaluation process that included democratic nomination and assessment, public opinion polling, analysis of achievements, interviews, and comprehensive evaluation. The evaluation process parallels the peer-review elements described above, though "democratic" refers to the selective solicitation of the views of local party officials and representatives from local National People's Congress and Chinese People's Political Consultative Conference offices. Second, the 2006 document clearly stipulates that GDP growth is no longer the sole criterion for performance. Rather, the document provides a long list of considerations that define excellent performance, including not only GDP growth but fiscal revenue, per capita income, worker safety, education, employment, social welfare, family planning, conservation of land and natural resources, environmental protection, and investment in scientific and technological development. More recently, talk of holding local officials to a "green GDP" standard, even if difficult to define and therefore not actually utilized, has been another manifestation of Hu Jintao's emphasis on smart growth.

Staff development and training

Training for government officials is not a new phenomenon, but it has become more systematic. The CCP Central Committee has made training guidelines more detailed, practical, and quantified by, for example, introducing in 2006 Trial Regulations on Cadre Education and Training.

Before China's reform era began in 1978, the government largely limited training to political and ideological indoctrination. Though instruction for government officials still includes political education, it is far more likely to focus on providing officials with the skills they need to perform their duties effectively. This change is even apparent in the network of CCP schools that play a key role in educating future leaders. These schools—especially the central party schools in Beijing and Shanghai—increasingly focus on economics, business, and management, instead of ideology. Moreover, they routinely invite foreign experts to present lectures. To narrow the quality gap between officials from inland and coastal provinces, the State Administration of Civil Service, created in 2008, issued guidelines last year that encourage deputy division directors and higher officials from inland provinces to attend training in China's more developed coastal regions.

More civil servants also receive training overseas. Since 2007, China has sent around 40,000 officials overseas for training each year. Among the most common destinations are Denmark, France, Germany, Great Britain, the United States, and Singapore. More than 90 percent of cadres at the ministerial level have had some instruction abroad. Overseas training ranges from a one-week course to a year-long degree and is occasionally provided at prestigious schools such as Harvard University's John F. Kennedy School of Government and the University of London's London School of Economics and Political Science. In addition to improving the quality of officials, overseas instruction is used as a tool to retain qualified officials, who appreciate such opportunities and may otherwise be tempted to move into the private sector to pursue higher salaries.

Characteristics of officials

■ **Higher educational achievement** The average educational level of government officials today is considerably higher than it was 30 years ago. In 1978, 9.3 percent of central-level officials had a junior college degree or higher; by 2007, the number reached nearly 90 percent. This is due to the vast expansion of China's tertiary education sector and to the PRC government's conscious effort to enhance the educational background and overall quality of officials. Since 2007, the government has required candidates to hold junior college degrees to participate in the national civil service exam. The government also recruits most of its officials straight out of college and must compete against FIEs and local companies that often offer far more attractive salaries. At times, the brain drain has been acute. From 1999 to 2001, MOFCOM lost 72.8 percent of all new recruits within the first three years of employment. The 2006 Civil Service Law helped address this problem by allowing more flexibility in salary levels.

■ **More diverse background** Today's civil servants are not just better educated than those in years past, they also have more varied academic and professional backgrounds. Research by Cheng Li, senior fellow at the Brookings Institution's John L. Thornton China Center, has shown

Table 1: Post-2007 Academic Backgrounds of CCP Standing Committee Members in Beijing, Guangzhou, Shanghai, and Tianjin

Academic major	Percent
Economics and management	34.6
Social sciences and law	28.8
Engineering/natural sciences	21.2
Humanities	11.5
Military education	1.9
Unknown	1.9

Adapted from Cheng Li, "The Leadership of China's Four Major Cities: A Study of Municipal Party Standing Committees," *China Leadership Monitor*, Summer 2007: 21. (Published by Stanford University's Hoover Institution on War, Revolution, and Peace)

Table 2: Generations and Profiles of PRC Government Officials

	Socialist Generation	Cultural Revolution Generation	Technocratic Generation	Globalized Generation
Age today	60+	45–60	30–45	Under 30
Context when coming of age	Recent founding of the People's Republic of China; egalitarianism	Cultural Revolution, red guards; went to the countryside	China's opening up; greater exposure to foreign influence	Little emperors from China's one-child policy; Internet age; overseas experience; better educated
Context during formative years in government	Chinese Communist Party ideology and central planning	Class struggle; instability; economic backsliding	Technocracy and economic growth; pragmatism	Balanced growth and harmonious society; globalization; economic nationalism

Source: APCO Worldwide

that in contrast to the 1990s, when senior government officials typically had a scientific or technical background, municipal party Standing Committee members in Beijing, Guangzhou, Shanghai, and Tianjin now come from more diverse academic backgrounds, including law and economics (see Table 1). The same shift is reflected in the current Politburo, which is no longer the exclusive province of engineers.

Beyond the renewed focus on educational credentials, the government now seeks a candidate pool with a broader range of professional experience. Previously, candidates often lacked experience or expertise on issues outside the direct scope of the relevant ministry that recruited them. Today, the government attracts individuals from a wider range of backgrounds, including those with work experience in state-owned enterprises, law firms, and multinational corporations.

Professionalization: How deep and how broad?

Despite its advances, China's civil service reform has not spread evenly across the country. Less-developed provinces, especially at the lower local-government levels, have lagged behind coastal provinces in terms of government professionalization. Local-government training budgets in less-developed regions are considerably smaller than budgets in most coastal areas, and poorer provinces still tend to recruit most of their officials from outside the civil service examination system to create jobs for local residents.

Professionalization can also vary depending on the approximate age of an official. Officials of different ages have been subject to wildly different formative experiences, as China has gone through some extreme socio-political developments in the last 60 years (see Table 2). Awareness of these differences is crucial to understanding an official's likely attitude toward concepts such as professionalization, modernization, and internationalism.

Professionalization—good news for FIEs

Foreign companies should welcome the trend toward a more professional Chinese civil service. If government officials are better educated, better traveled, more efficient, and more accountable, FIEs will find them easier to work with. Companies should consider the following recommendations as they build relations with government stakeholders.

■ **Understand the diverging levels of professionalization** Compared to officials from inland areas, officials in coastal areas have had more opportunities to engage with foreign businesses and governments and have introduced institutional changes that support economic growth more quickly. Thus, they typically act in ways that are more consistent with Western professional practices. Among central government officials, the level of education and training is generally high, but here too, differences remain. Some ministries, such as MOFCOM, have moved faster than more traditional ministries, such as the Ministry of Railways.

■ **Understand how government officials are evaluated** FIEs in China must understand the method and criteria by which PRC government officials are assessed to understand what motivates them. In past years, a project that would guarantee a certain level of economic growth might have sufficed to obtain government approval and support. Today, government officials face a wider range of social, political, and economic challenges, and their performance is judged accordingly. Understanding the 2006 Organization Department guidelines is a good way to learn more about the process; asking local officials how they are assessed may also help.

■ **Understand the official's personal background and profile** Officials of different generations see the world differently. Younger officials may be more professional and worldly, but that does not mean they will automatically support a foreign company. They will still have a deep commitment to China's development and its growing political and economic influence. This means that FIEs should emphasize the wider benefits that they bring to China, ranging from technical or managerial expertise to new jobs or energy efficiency.

■ **Build strategic relations with the leaders of tomorrow** Companies should systematically track rising stars in government (see the *CBR*, March–April 2008, p.20). Municipal and provincial-level officials are relatively accessible, and companies should get to know them before they are elevated to senior positions in the central government. FIEs may also wish to find opportunities to meet with party secretaries, mayors, governors, and vice governors to introduce their companies. One way to start is to arrange a meeting with the senior local official responsible for foreign trade. Companies should also make use of executive visits and commercial milestones to request meetings. These will be good investments in the future and will also help companies in the present, since localities enjoy considerable decisionmaking authority.

Not everything has changed

China is adopting many features of a Western civil service, but its system still retains important Chinese characteristics. Most notable, China's civil service remains loyal to the CCP—hence the leading role that the CCP's Organization Department plays in the assessment of officials. In addition, traditional Chinese concepts such as "face," hierarchy, and the importance of personal relationships still apply (see the *CBR*, July–August 2008, p.48). Even when meeting with the new breed of Chinese civil servant, FIEs should be attentive to these traditional norms and be sensitive to how they discuss problems and press for results. 完

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A New Welcome for Venture Capital

China's emphasis on indigenous innovation and several other developments have created a more welcoming environment for venture capital

Calvin Ding and Tony Zhang

Structural defects in China's economy, including over-reliance on low value-added manufacturing and export-led growth, have led the PRC leadership to emphasize the importance of indigenous innovation as a national development strategy to sustain China's competitiveness and economic growth. In turn, the government has also begun to view venture capital (VC) as an important means of fostering indigenous innovation.

VC has played an important role in the economic development of many countries, especially in fostering the stunning growth of the Internet and high-tech sectors. Venture capitalists can assume this vital role because they focus on entrepreneurs, who are the driving force behind indigenous innovation. Through advisory, selection, and investment capacities, venture capitalists provide valuable commentary on the feasibility of entrepreneurial endeavors and absorb much of the risk involved in entrepreneurial experimentation.

Venture capital pours into China

Against the backdrop of the global economic downturn and the concomitant decline in investment, VC investment in China remains a relative bright spot. According to Dow Jones VentureSource, venture capitalists invested a record $4.2 billion in 245 deals in China in 2008, up from $2.8 billion in 290 deals in 2007. Information technology (IT)-related investments led the way as investors injected $1.6 billion in 86 IT deals in 2008, up 60 percent from the $1 billion invested in 117 deals in 2007. At $10 million, China's 2008 median VC deal size was the largest in the world.

Quick Glance

- Venture capital in China faces many restrictions, but investors can use onshore and offshore strategies to structure successful investments.
- The Growth Enterprise Market, China's newest bourse, provides a new exit route for investors in smaller companies.
- New rules make obtaining approval for onshore funds involving less than $100 million easier.

China's domestic VC market

China has relatively limited domestic sources of VC funding—it comes mostly from government investment, enterprises, and wealthy citizens. PRC law limits the scope of financial services and securities companies. For example, it prevents financial institutions, such as banks and insurance companies, from engaging in VC investment. This contrasts with developed Western economies, where large institutional investors, such as pension and mutual funds and financial institutions, constitute significant sources of VC investment in nonfinancial sectors. The result is that large institutional investors and high-net-worth individuals are the primary sources of venture-capital funding in the United States and Great Britain, but the PRC government, enterprises, and foreign funds account for the vast majority of venture-capital funding in China.

Though government investment can play a vital role in the development of a healthy VC market, the issue of governments acting as venture capitalists has stoked heated debate. Much of the concern stems from questions about whether the government is capable of selecting investments that will lead to the most profitable returns. Critics of governmental VC investment have argued that bureaucratic funding decisions are sometimes removed from market concerns and may result in the subsidization of unviable enterprises, impede development of private sector VC, and, in the long term, dampen entrepreneurship. In addition, because many Chinese enterprises that make VC investments are partially or wholly state-owned, whether corporate investors can make independent investment decisions is a significant concern.

The relative absence of domestic sources of VC funding has led many Chinese companies to seek foreign VC. For example, successful Chinese companies such as Baidu.com, Inc.; Suntech Power Holdings Co., Ltd.; and Focus Media Holding Ltd. all received funding from foreign VC sources in their early developmental stages. Though government restrictions on pension-fund investment in the VC market were recently lifted for two companies, and though there have been reports of greater relaxation of VC regulations, substantive changes have been gradual and their long-term effects remain unclear.

Hurdles for VC funds in China

Despite growing VC investment in China, venture capitalists still face many challenges, including the lack of an efficient exit route by which they can recoup their initial investments. In the United States, one of the most frequently used exit mechanisms is to sell shares through an initial public offering. In China, this option is limited because listing requirements for China's stock exchanges are high and regulatory approval is difficult to obtain. Domestic companies also require approval from the China Securities Regulatory Commission (CSRC)—China's regulator of stocks, bonds, futures, and mutual funds—before they may list overseas, and the criteria for CSRC approval in these cases are even more stringent than those for listing on the domestic stock exchanges.

To circumvent CSRC restrictions, Chinese enterprises have historically taken what is known as the "red-chip" route to obtain an overseas listing. The red-chip route refers to the listing of an offshore special purpose vehicle (SPV) through which the shares of the Chinese enterprise are owned. When making the VC investment, foreign VC funds and Chinese companies and individuals jointly invest in an SPV, which then acquires the shares or assets of the Chinese business concern, effectively transferring ownership overseas. The SPV subsequently applies for listing on an overseas stock exchange, such as the New York or Hong Kong stock exchanges, effectively evading PRC approval of the overseas listing. Yet the viability of the red-chip route has diminished significantly since 2006, when China passed regulations on mergers and acquisitions and foreign exchange filing rules that aim to promote the listing of promising Chinese companies on domestic exchanges (see the *CBR*, September–October 2007, p.36).

Strategies for foreign VC investment in China

Since foreign VC funds first entered China in the early 1990s, companies have adopted various investment strategies to conform to changing PRC regulations with an eye toward maximizing investment returns. Currently, the "offshore" and "onshore" structures are the two most popular investment strategies, and foreign VC funds sometimes pursue both strategies concurrently by adopting offshore and onshore structures to obtain greater investment and exit flexibility.

Offshore VC funds

Many offshore VC funds have invested in Chinese high-tech companies through SPVs under the red-chip structure and exited with handsome profits following the listing of the portfolio company. The primary benefits of the offshore structure are that its establishment and fundraising are free from PRC regulatory oversight, investors can invest in SPVs and China-based companies, and offshore funds generally enjoy a lower income-tax rate than onshore funds. As PRC regulations on mergers and acquisitions and foreign exchange filing rules have restricted the listing of SPVs overseas, however, offshore funds have invested directly in China-based portfolio companies by converting them to foreign-funded equity joint ventures with a plan to exit through initial public offerings in the Chinese stock market.

Foreign VC funds sometimes adopt offshore and onshore structures to obtain greater investment and exit flexibility.

Onshore VC funds

The onshore structure—except in cases where only renminbi (RMB) funds from domestic sources are used—refers to a RMB-denominated equity joint venture fund (EJV fund) or contractual joint venture fund (CJV fund) with Chinese investors or a RMB-denominated wholly foreign-owned enterprise fund (WFOE fund). (All of these are known as foreign-invested venture capital investment enterprises [FIVCIEs] under PRC law.) The establishment and operation of FIVCIEs are subject to the approval of the PRC Ministry of Commerce (MOFCOM) or its provincial counterparts, and investments must be reported to PRC regulators for approval and filing purposes. PRC foreign-exchange controls limit FIVCIE investments to only China-based portfolio companies, so the primary exit strategies are an initial public offering on a Chinese stock exchange or a transfer to other entities or other funds through an acquisition.

Because foreign-invested limited partnerships are not recognized as a corporate form under Chinese law, establishing a CJV fund in a non-legal-person form has become the most preferred onshore strategy for foreign VC funds. A CJV fund's major strengths are its similarities to a limited partnership fund—both have similar management, contractual profit allocation, and pass-through taxation structures. In contrast, WFOE or EJV funds can be incorporated only as limited liability companies, which face more restrictions under PRC law. Under current PRC practices and stock exchange rules, however, it is difficult for a CJV fund in a non-legal-person form to open a securities account (*zhengquan zhanghu*), meaning that a CJV fund in a non-legal-person form cannot exit from the portfolio company through an initial public offering on the Chinese stock market.

If a foreign VC fund expects China's RMB appreciation to continue and is familiar with the Chinese stock market, a CJV fund formed with a sophisticated Chinese partner could be worthwhile. Several foreign VC funds have already established CJV funds or WFOE funds and invested in China-based companies in combination with parallel offshore funds, with the expectation that they will eventually exit through the Chinese stock market or future acquisitions.

Welcome developments

Two recent developments may facilitate VC investment in China: a new bourse and a relaxation of onshore fund rules.

China's Growth Enterprise Market

In March, CSRC published its long-awaited Interim Measures for Initial Public Offerings and Listings on the Growth Enterprise Market. Pursuant to the measures, the Growth Enterprise Market (GEM) will be created on the Shenzhen Stock Exchange. The new board has lower listing requirements than Shenzhen's main board and is expected to make it easier for smaller Chinese private enterprises to list. This will also benefit foreign VC funds by providing a new exit. To list on the GEM, a company must have

- Operated in China for at least three years and be in the form of a company limited by shares;
- Been profitable in the past two years, with total net profit of at least ¥10 million ($1.5 million), or a net profit of ¥5 million ($732,000) and revenue of ¥50 million ($7.3 million) in the most recent year with at least a 30 percent annual growth rate in the most recent two years;
- At least ¥20 million ($2.9 million) in net assets and no non-recovered loss; and
- At least ¥30 million ($4.4 million) in equity after the offering.

Several questions remain unanswered, however. First, CSRC has not yet indicated what the implementing standards for verification will be. Given the low listing requirements, CSRC will likely implement detailed verification standards to determine which companies, among the possibly hundreds of qualified applicants, may list on the GEM. Shenzhen Stock Exchange officials have previously indicated that candidates engaged in high-growth, high-tech fields, as well as those in new economy, service, agriculture, materials, energy, and commercial modes, are most welcome to list on the GEM. CSRC may give leading high-tech companies that specialize in encouraged industries priority status for listing. The timeframe for listing also remains unclear, though CSRC Deputy Chair Yao Gang has noted that each listing verification could take roughly three months. Because listing decisions for initial public offerings are often a function of China's macroeconomic policy, wait times may be industry-specific.

Relaxed rules for onshore funds

In addition to the creation of the GEM, the PRC government has adopted new incentive policies to encourage the establishment of onshore funds. In March, MOFCOM authorized its provincial-level counterparts to approve the establishment of onshore funds that involve less than $100 million and has allowed all onshore funds to report their investments to provincial authorities rather than to MOFCOM in Beijing. This move shortens the approval period from several months to several weeks. At the local level, municipal governments in Beijing; Shanghai; Shenzhen, Guangdong; and Tianjin have enacted local rules to support the establishment of onshore funds, including more relaxed formation procedures, tax holidays for onshore funds and high-level managers, cash bonuses on establishment, and lower capital requirements, compared to national rules published in 2003 by MOFCOM.

Given the current global recession and the resulting cash drought that many Chinese companies face, the PRC government will likely hasten reform by publishing the final revised onshore funds measures and new foreign-invested partnership enterprise measures that permit the establishment of onshore partnership-fund structures. Presumably, upcoming measures would encourage more foreign VC funds to establish onshore funds.

With the opening of the GEM and the implementation of central- and local-government support measures, foreign VC funds face fewer legal restrictions and gain many new investment opportunities in China. By initiating VC investments in China during the current global economic downturn, investors will likely reap handsome rewards when the economy recovers. 宪

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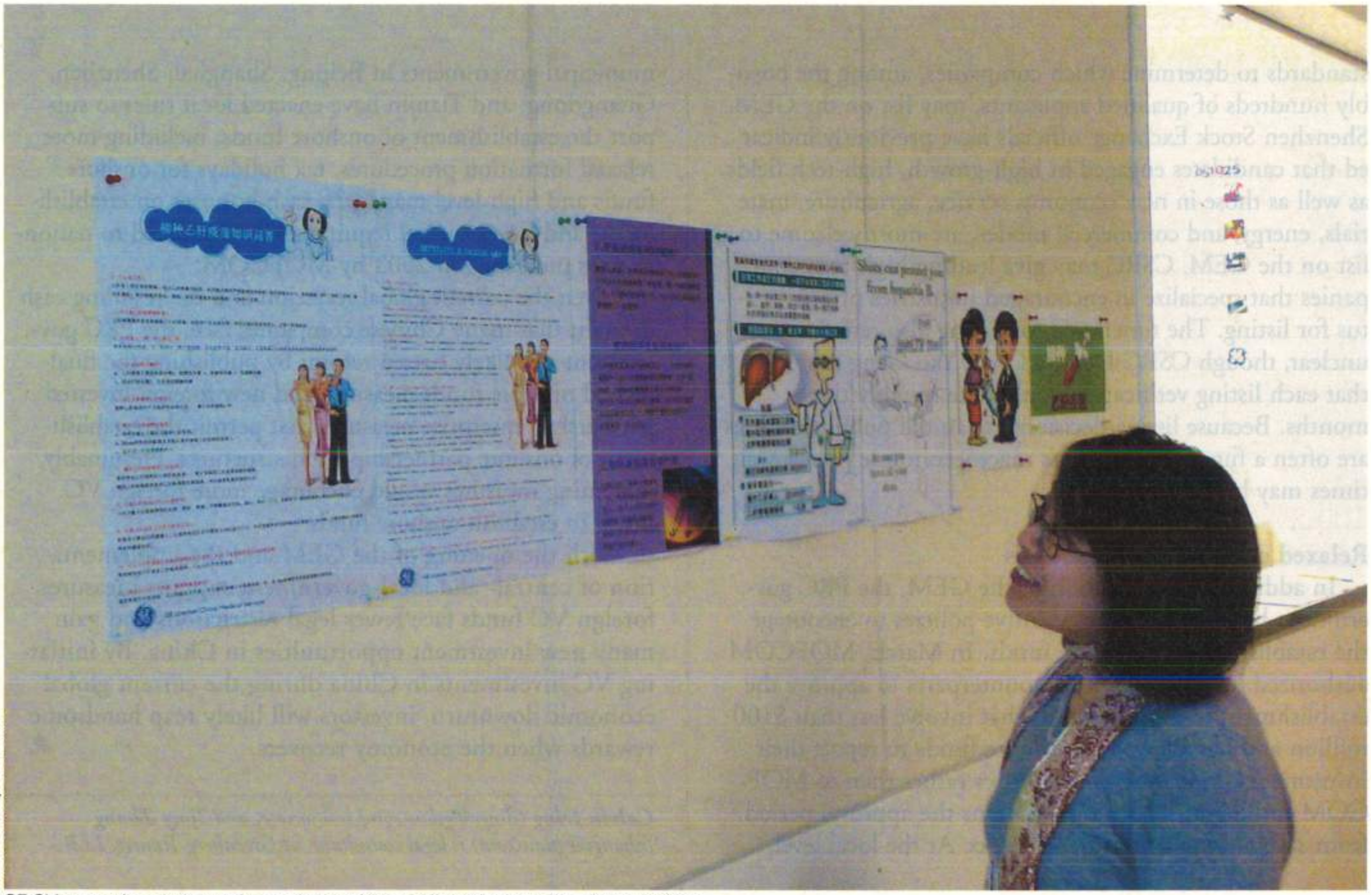

Photo courtesy of GE China

GE China used posters to educate its employees about the benefits of vaccination.

How to Reduce Hepatitis B in the Workplace

The success of GE China's HBV vaccination program offers an example for companies considering similar programs

Stephen A. Maloy

General Electric China Co., Ltd. (GE China) offered a voluntary, free hepatitis B virus (HBV) vaccination program to all employees between February 2007 and March 2009, in what may have been the first time a major foreign employer in China attempted a company-wide HBV inoculation program. GE China believes the program reduced the risk of new HBV cases among staff and reduced associated work time lost, boosted staff morale, and improved employees' opinion of the company. Other companies in China may wish to consider similar vaccination programs.

About the virus

HBV is a viral liver disease estimated to have affected 2 billion people worldwide, of whom more than 350 million continue to live with chronic HBV, according to the World Health Organization (WHO). The disease is particularly prevalent in China, where more than 7 percent of the total population is affected by chronic HBV, according to the PRC Ministry of Health (MOH). (WHO puts the number at 8 to 10 percent.) The disease is transmitted through body fluids, such as blood, semen, and saliva. WHO estimates that the HBV virus is 50 to 100 times as infectious as HIV/AIDS and can survive outside the body for at least seven days. Over a lifetime, unprotected residents of China have more than a 60 percent chance of contracting HBV, according to the Hepatitis B Foundation.

The disease does not have a particularly high mortality rate, but it often requires a long recovery period and is difficult to cure completely. In addition, chronic HBV victims have other serious health issues related to the disease. Globally, 25 percent of chronic HBV sufferers who contracted HBV during childhood will later die from cirrhosis or liver cancer caused by the chronic condition, according to WHO.

Recent studies in Shanghai suggest that the average direct and indirect medical cost of a case of chronic HBV is about $3,000. Using more advanced and effective interferon-based treatment can raise the medical cost from $5,000 to $15,000 per person, based on US data. The economic impact of the disease on employees and employers in terms of absenteeism, reduced productivity, and emotional distress is probably considerably greater.

A vaccine against HBV became commercially available in 1982 and has been continuously improved to the point where it can offer about 95 percent protection against the disease. Though the vaccine is widely available, the vaccination process requires an initial test to determine whether the antigen is already present, followed by three separate injections at fairly precise intervals over a six-month period. In the United States, the full HBV vaccination program typically costs $75 to $165 per person. The cost of missed time from work to visit the doctor's office often exceeds the cost of the vaccinations.

Quick Glance

- Company-sponsored vaccination programs can reduce the risk of illness, reduce work time lost because of related illness, and improve staff morale.
- The hepatitis B virus vaccination requires a series of three shots at specific intervals; carefully planned and efficiently run vaccination programs have a good chance of success.

HBV discrimination and the law

Given the seriousness of the HBV problem in China, many Chinese and multinational corporations (MNCs) have adopted measures to reduce the spread of the virus within their workforce. In the past, some employers attempted to screen out all HBV carriers through pre-employment physicals, while others aimed to screen out employees with active HBV that would affect their fitness for work.

HBV sufferers in China frequently face discrimination in many areas of life—at school, at work, eating out, and dating. During the last few years, numerous periodicals have highlighted the plight of HBV sufferers, and several HBV action groups have formed. Though Chinese press reports often focus on foreign companies' discrimination against HBV carriers, anecdotal evidence suggests the problem is at least as acute among Chinese employers. A May 2007 survey conducted by the Chinese University of Political Science and Law found that 49 percent of 3,500 respondents in 10 Chinese cities would be unwilling to work with HBV carriers and that 55 percent would not hire them.

MOH and the PRC Ministry of Human Resources and Social Security in May 2007 co-issued the Notice on Protection of Hepatitis B Surface Antigen (HBsAg) Carriers' Right to Employment. According to the notice, which took effect May 18, 2007, labor and social security and health bureaus at various levels are responsible for protecting HBsAg carriers' right to employment and their privacy. (HbsAg is a protein antigen test which is used to determine whether an individual is a carrier of HBV.) The notice states:

- HBV carriers' right to employment shall be protected. An employer shall not refuse to employ or dismiss an HBV carrier because the person is a carrier, unless the carrier is banned from the job by laws, regulations, or MOH rules.
- An employer's physical examination standards shall be strictly regulated to protect the privacy of carriers. An employer may categorize liver function as one of the physical examination standards but shall not use Hepatitis B Virus Serology Index as one of the physical examination standards unless the carrier is banned from the job by laws, regulations, or MOH rules. Medical institutes at various levels shall protect carriers' privacy during the physical examination.

GE China's vaccination programs

In China, GE operates through more than 50 Sino-foreign joint ventures and wholly foreign-owned enterprises. GE China serves as a holding company for many GE investments and as a platform company for the corporate support functions of GE in China. GE China has about 11,900 employees, with about 6,800 employees in Shanghai, 1,800 in Beijing, and 850 in Hangzhou, Zhejiang. Annual sales exceed $5 billion.

GE's first experience with employee vaccination programs in China took place during the 2003 severe acute respiratory syndrome (SARS) crisis. Though GE had no SARS cases among its workforce, several employees contracted the common flu. The early symptoms of the flu and SARS are quite similar. Though flu vaccines provide no protection against SARS, after considerable discussion, the corporate medical operation decided to offer all employees a voluntary flu vaccination program. The rationale was as follows:

- If the incidence of flu could be reduced in the workforce, the number of false alarms about the possibility of a SARS case, with attendant efforts to isolate potentially affected staff, could be reduced;
- Reduction in flu cases would have some payback in terms of reduced absenteeism during the flu season; and
- During a time when employees were under great emotional stress, the vaccination program sent them an important message about company concern for their health and well-being.

The program enjoyed broad employee participation. There seemed to be fewer absences than usual during the flu season, though no serious effort was made to measure the reduction. As a result of the program's popularity with staff, GE China offers flu vaccinations to employees annually.

GE responds to China's notice on testing for HBV antigen

GE requires a pre-employment physical for all new employees. Prior to the May 2007 notice that prohibits testing for the HBV antigen, GE tested for the HBV antigen. Having the HBV antigen did not affect a candidate's employment prospects, unless the candidate was suffering from active HBV and could not safely perform the job. Once GE's legal team advised its medical department of the notice, however, GE immediately discontinued pre-employment testing for the HBV antigen. Dr. Wu Jin, GE's medical director for China, began to consider the steps the company could take to protect employees from HBV. An educational program that emphasized the importance of good hygiene was an obvious first step. Wu, however, asked: "Why not further protect employees by offering vaccination against HBV to all employees on a voluntary basis?"

In February 2008, Wu raised her proposal with the GE China Human Resources Council, which was sympathetic but concerned about the cost. Wu took her campaign to the corporate leadership, and in early 2008, the company agreed to provide the first $25,000 in funding for the program. Shortly thereafter, all of the GE businesses in China agreed to participate.

Steps to a successful HBV vaccination program

Because an HBV vaccination program requires a blood test, followed by three separate vaccinations on a fairly rigid schedule, the program demands a greater level of management and communication than a flu vaccination program. It also requires a higher level of employee commitment. GE China's Managing Nurse Zuo Wenxiu developed a system to implement the vaccination program and ensure that it ran smoothly and efficiently. The system included a checklist to confirm that employees received timely communications for each step of the program. Thanks to efficient procedures, most employees were able to be vaccinated and return to work in less than five minutes.

The medical department and human resources and communications groups developed a program to educate employees about HBV and the vaccine. The team created posters and displayed them around the facilities. It also used the employee magazine to urge employees to participate by including a personal letter from a senior manager about HBV and the importance of vaccination.

Critical to any vaccination program is a process to ensure that employees make an informed and voluntary decision to participate. The medical and legal teams devel-

Reasons to Support Workplace Vaccination Programs

General Electric China Co. Ltd. (GE China) believes the hepatitus B virus (HBV) vaccination program was an unqualified success and is considering offering free vaccinations to all new employees. The company may also offer employees who declined the initial program or who were unable to complete the course of vaccinations because of scheduling issues a second chance to complete the program.

The company believes that many factors contributed to the success of the program and can improve the effectiveness of workplace-based vaccination programs:

- Multi-shot programs often founder when busy patients cannot fit the shots into their work schedules. Since most people spend more waking hours at work than anywhere else, appointments for employer-run inoculation programs are easier for employees to keep.
- Individuals usually acquire vaccinations at "retail rates," but the scale of a corporate program reduces costs dramatically. Bulk purchases and the use of workplace healthcare resources that are already mandated by PRC law kept GE's per-patient cost low.
- Management engagement and leadership helps company vaccination programs succeed. When employees see their leaders taking the time to walk down to the clinic, they often follow.

Though the analysis of the data from the GE China experiment is rather crude, the results are striking. Other employers may wish to consider similar programs for their employees.

To cover the large population over 15 years of age that is not currently covered by vaccination programs, the PRC government could subsidize the cost of vaccines for employer-run HBV inoculation programs. This is a good idea for three reasons:

- Avoided healthcare treatment costs and productivity losses make the program an investment with immediate returns for China's future.
- Because most large employers already run government-mandated health clinics in their factories, and employees can more easily attend vaccination programs at their workplaces, such programs can be completed at lower cost and with higher participation rates.
- The program sends a clear message of joint government and industry concern for the health and well-being of workers.

Finally, affiliates of the All-China Federation of Trade Unions, China's official labor union organization, could also assist in educating workers about HBV and the benefits of participating in vaccination programs.

—Stephen A. Maloy

oped information fact sheets and consent forms that were signed by all participating employees.

Program results

The first round of vaccinations began on July 1, 2008 and ran for 15 days at eight GE locations in Shanghai and two locations in Beijing. Plant nurses or local clinic staff administered vaccinations at other sites. The second round of vaccinations occurred at GE locations between August 4 and 26 in the same sequence as the first round. The final round took place between January 4 and February 3, 2009.

Program records indicate that of the 3,212 employees who began the program, 2,569 employees completed it, or about 21.6 percent of GE's workforce in China and 80 percent of employees who began the program. (No employees reported adverse reactions to the vaccinations.)

Because much of its workforce is urban and relatively well-educated, GE expected a substantial number of employees to have been previously vaccinated against HBV through other programs. But managers were surprised to find that in a high-tech business in Shanghai, almost one-quarter of the employee population was able to benefit from the program.

GE tracked costs closely throughout the program. To minimize costs, company medical staff from on-site company clinics administered most inoculations, and volunteers from the human resources department handled much of the paperwork. In the final account, the program cost $40,000—the largest part of which was for the cost of the vaccines. Though the cost of the regime varied from city to city, all locations paid between ¥100 and ¥120 ($15 and $18) per employee for the three-dose regime. The net cost of the program per employee protected was a little under $16.

Benefits outweigh costs

A simple analysis of the program would suggest the following:

2,569 employees vaccinated × 95% effectivity rate × 7 to 10% risk of contracting chronic hepatitis = 170 to 244 cases of chronic hepatitis prevented.

170 to 244 chronic HBV costs avoided × $3,000 average treatment cost = $510,000 to $732,000 saved.

170 to 244 chronic cases avoided × up to 25% fatality rate from complications (for example, liver cancer or cirrhosis) = up to 40 to 60 lives saved.

The numbers above are admittedly crude, and a few factors may result in the value being somewhat overstated. For example, the incidence of HBV in Shanghai and other major GE locations is lower than the national average, and the GE workforce is better educated than the national average and presumably better trained in hygienic practices. Also, the 25 percent fatality rate applies to those who caught HBV as children. Reliable data on fatality rates for those who caught HBV as adults is unavailable, but the rate is likely to be lower.

For a few reasons the results may also be understated. For example, no benefit was ascribed to work time gained due to HBV infections avoided, the number of HBV cases avoided that would have developed into chronic HBV, the incremental protection to employees who had only one or two vaccinations but did not complete the program, or the benefit of having a high percentage of the workforce protected from HBV to workers who had declined vaccination.

Another significant benefit was the impact on employee morale. Many employees who participated in the program expressed the view that GE management looked at big problems and was unafraid to try novel and "big" solutions. Employees felt that the company was concerned about their health and welfare. A post-vaccination survey of participating employees showed a 96 percent satisfaction rate with the program.

Further validation of the positive employee reaction was noted in a recent edition of *China Business News Weekly*, which conducted a survey of employees of roughly 30 Chinese and MNC companies, including GE, early in 2009. One of the questions in the survey was: "During the past year, what was the most considerate benefit your company provided to you?" The answer from an unidentified GE China employee was "The company arranged for vaccinations several times.... We could see the company cares for the employees."

GE's positive experience developing and implementing an HBV vaccination program for its staff has resulted in a range of benefits to the employees and the company itself in terms of health, goodwill, and avoided costs. Other companies, and even governments, could benefit from offering similar programs. 完

Critical to any vaccination program is a process to ensure that employees make an informed and voluntary decision to participate.

***Stephen A. Maloy** (Stephen.Maloy@ge.com) is general counsel-Asia Pacific at General Electric Co. He is based in Hong Kong and Shanghai. GE has posted detailed material on its vaccination program to further assist organizations considering similar programs.*

Target the China Market to Ride out the Recession

In a slowing global economy, foreign-invested enterprises in China should refocus on China's domestic market

Sigmund Floyd

The United States and large parts of the developed world are struggling through financial crises, and the global downturn has severely affected China and developing countries as well. Yet China is positioned to emerge relatively unscathed and as a greater power than ever before (see p.50).

Nevertheless, companies operating in China must find ways to deal with the recession. Attempts to treat China investments like US investments—using the standard US playbook to cut costs and staff—could prove counterproductive. On the other hand, companies must navigate through these difficult economic times. Given the need to manage costs through the downturn, companies should balance short-term priorities with long-term objectives and avoid actions that will damage their future stakes in China.

Companies that export from China to the United States should be realistic—the US market will remain relatively weak for the foreseeable future. To stabilize China-based ventures in trouble, companies should look to China's domestic market or other markets that have been less affected by the economic crisis.

Companies taking a long-term approach have already introduced their best technology, good manufacturing practices, and management expertise to their China operations. These companies should resist any urge to cut back on their commitment to the China market. By recognizing that China is just as important as, or even more important than, their home market, US companies can use the current crisis as an opportunity for long-term change. They should pay attention to several areas when revamping their China operations.

Companies that currently do not focus on China's domestic market will find it tough to adapt, but these are precisely the companies that need to make the transition and expand their customer base relatively quickly. They must reexamine their business models, develop relationships from scratch, and thoroughly review assumptions inherent in the North American business model they may be using. Success or failure in China's domestic market often hinges on the ability to make deep changes in fundamental thinking. Such companies also need to recognize that change takes time and that the sooner they begin, the better positioned they will be in the future.

Learning the hard way, one US company applied its business model—based on outsourcing production that required highly skilled blue-collar labor—to China without considering labor-market differences. Unfortunately, the required skills were in short supply in China, and the company struggled with training and retention, losing money over a two-to-three-year period. In this case, the company's situation improved after switching to a business model based on domestically sourced raw materials and readily available unskilled labor. The company would have saved a lot of time and money had it developed a better understanding of local conditions before constructing a multimillion-dollar production facility.

Foreign companies should also remember that business decisionmaking within Chinese companies can be different from US practices, especially in the state-owned sector, and may require a simpler or more flexible commercial approach. For example, the above-mentioned company's commercial package offer was composed of product, application equipment, and service personnel. Many US customers are favorably disposed toward such package offers, which enable them to outsource entire operations. But for Chinese companies, in which separate functions handle purchasing decisions for different types of products, separate offers for each component are often easier to negotiate.

Quick Glance

- Foreign-invested enterprises (FIEs) should take steps to protect the value of their assets and ensure long-term success in China's market.
- In China, FIEs should adopt a flexible business model with low manufacturing costs and provide products tailored to meet local needs.
- Companies seeking to reduce costs in China should cut travel expenses and bonuses rather than personnel, who will be essential to weathering the downturn.

It is also important to target market niches—a "one-size-fits-all" approach is no more likely to work in China than anywhere else. Though "trawling for interest" is necessary in the early phases of selling to China's domestic market, it is easy to lose focus while trying to meet the conflicting needs of many customers. Concentrating on a limited number of strategic accounts will usually bring better results.

In the initial phase of targeting the Chinese market, companies should make liberal use of conferences and host seminars. China is one of the few countries in the world where industry competitors will willingly attend a supplier-sponsored "discussion group" (*yantaohui*)—a tremendously valuable and cost-effective way to meet many customers, learn about real market needs, and build reputation. Chinese companies are interested primarily in products and technology that are unavailable from Chinese suppliers, so foreign companies should emphasize their high-tech products and technological know-how. Once the foreign company has narrowed down the customer base to a select group that is seriously interested in the company's offering, it should work closely with those customers and develop products and services tailored to their needs.

Low-cost, flexible production and research and development (R&D)

Though Western best practices, such as Six Sigma and International Organization for Standardization (ISO) certification, are good manufacturing practices to follow, the two things that are essential for success in China's domestic market are flexibility and low production costs. It is difficult for foreign companies to outmaneuver the local Chinese competition, which is highly responsive to customer demand. To do so, a company must keep working capital low, emphasizing short-run, made-to-order production with fast turnaround times. During a downturn, when a company may have surplus capacity, this is a realizable objective, provided production staff has not been cut too much.

Products and services for the Chinese market are needed at Chinese price points. With hundreds of small entrepreneurial enterprises and state-owned enterprises in almost every industry sector, China may be the most competitive market in the world. Just because a product offers the best performance in the field does not mean it can be sold in China at the same price as in markets with less competition. Thus, R&D teams must be tasked with developing products at a realistic price while maintaining a performance profile that comfortably exceeds that of local competition. This will typically require companies to use local raw materials or parts, some of which may not meet the standards of overseas markets. Developing such products can be greatly facilitated by having an R&D presence in China, something the PRC government actively encourages. With general uncertainty prevailing in the employment market, the timing for hiring technical personnel probably could not be better.

make sense in the US business environment, in China it increases the supply chain's vulnerability to corruption.

Human resources: A development opportunity

During a restructuring, companies in China should take a different approach to human resources than they might in the United States. A company that conducts layoffs in a manner perceived as insensitive could give PRC government regulators, employees, and customers a negative image of the company and endanger its future in one of the most important markets in the world. Because Chinese employees tend to value organizational stability, reducing work hours across the board and cutting bonuses for management-level employees are preferable to paying costly severances.

Lower consumer demand in the short term can free up employee resources, and the current downturn is an excellent time to develop the capabilities of local staff. Many local managers in China have come of age without ever facing a recession and have little idea of what it means to downsize operations or stabilize losses. Having spent much of their working life in "boom conditions," some local staff may have an entitlement mentality that must be challenged. To develop local staff capabilities, senior managers must coach their younger counterparts and take on a more active leadership role.

Whether in production, marketing, or other functions, it is extremely important to recognize the benefits of reten-

> Companies should balance short-term priorities with long-term objectives and avoid actions that will damage their future stakes in China.

Localize the supply chain

Companies need to shift their supply-chain management focus to support the localization of the company's output for the domestic market. Though supply-chain management has received enormous attention, it has come primarily from the overseas-sourcing standpoint. To ensure quick turnaround and minimize costs, raw materials for Chinese products need to be sourced in China as much as possible. Though competent supply-chain professionals in China do not come cheaply, their expertise is critical.

The supply chain is probably the function that is most prone to internal corruption issues (followed by sales and marketing). Local managers who have cozy relationships with suppliers can easily increase a company's entire cost structure by a few percent. Companies should therefore maintain strict oversight of the supply chain, with at least one non-local manager who interacts directly with key suppliers and conducts frequent audits of key transactions. A mistake some companies make is to assign supply-chain management to a remote office near the supplier rather than centralizing this function within their China headquarters. Though this might

Why China Will Be Less Hard Hit by the Global Economic Downturn

- The "toxic assets" that have shaken US and European governments and brought their financial systems to the brink of collapse have had little effect on China.
- Rapid declines in global commodity prices have benefited China's manufacturing base, helping to cushion the drop in demand. China is taking advantage of lower prices and aggressively acquiring companies that produce raw materials. Lower international prices have also relieved inflationary pressures in China's domestic economy.
- As a proportion of gross domestic product, the PRC government's ¥4 trillion ($585 billion) stimulus package is nearly three times larger than the United States' initial $789 billion stimulus. On February 1, China launched a program that offers rural consumers a 13 percent subsidy to buy certain computers, television sets, refrigerators, and mobile phones. The PRC State Council, China's highest-ranking administrative body, has also announced a similar program for several cities and various subsidies to promote industry revitalization.
- China has accrued nearly $2 trillion in foreign-exchange reserves and can easily afford further stimulus, if needed, without relying on external borrowing.
- High personal savings rates mean that China's consumers are much better positioned to weather a temporary economic slowdown than their debt-strapped US counterparts.
- China has ample opportunity for industrial consolidation and can continue sidelining antiquated or inefficient capacity.

—Sigmund Floyd

tion even in difficult times. Retention has never been easy in China, but in the current downturn, local employees are realizing the benefits of staying with their employer. It would be shortsighted of foreign employers to cut their ties with key employees when talent is needed to get through the downturn and to develop a strong local customer base for the future. Instead of cutting training, development, and meeting budgets, companies should reduce costs by reducing travel expenses and bonuses in a way that is proportional to the level of actual business activity and, therefore, understandable to local staff.

Just because a product offers the best performance in the field does not mean it can be sold in China at the same price as in markets with less competition.

Maintain environmental, health, and safety (EHS) standards

The government and general public have become deeply concerned about the toll of indiscriminate development on the environment, and this is one area where US firms possess an undisputed competitive advantage. Companies should ensure that their EHS efforts in China are world-class and promote them vigorously among employees and customers.

Good EHS practices can also play an important role in product marketing. For example, one wholly foreign-owned enterprise in China's refractory materials sector initiated programs for employee safety and housekeeping practices based on US standards, a practice that was extended to its employees working at customer sites. After about a year, the company became known for its program, and customers began to request that the company teach them its safety-management practices. The company held seminars at customer sites and for groups of customers at the company's plant. The program was directed by a strong local EHS manager with full support from senior management in China and functional experts in the United States. Training seminars strengthened customer-supplier relationships, facilitating the introduction of the company's cost-effective products for safe maintenance. Companies should select their "EHS champions" with care, because these employees can become some of the company's best marketers.

Refocus on China's domestic market

Companies that seek long-term success in China must maintain an investment mentality despite the tough times. This does not necessarily mean the time is right to make new investments, but companies should certainly continue to spend to protect the value of the assets that are in place. Companies need to take a hard look at their domestic and overseas customer bases and make necessary adjustments to succeed in China's domestic market. It will not be easy, but companies that approach this task with a clear purpose and commitment to China's future stand to benefit greatly. 完

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China's Healthcare Reform

Continued from page 35

Grade 1 or Grade 2 hospitals. These are the middle of the market, upon which the majority of the population will increasingly rely. It is unclear, however, whether these would be attractive opportunities for multinationals.

Commercial medical insurance to supplement basic

To date, Chinese citizens have had few medical insurance options. Now, insurance companies will be encouraged to develop and introduce commercial medical insurance products, with commercial medical insurance used to supplement basic medical insurance, and thereby cater to the diversity of needs in China's market. In addition, the government will explore purchasing medical insurance management services from commercial insurers. Many domestic and multinational insurance companies are already seeking such opportunities in China, looking at participating as either policy providers or third-party administrators.

Takeaways for multinationals

The plans set a clear course for China's healthcare reform, but the implications for multinational healthcare players are not so obvious. On the one hand, the healthcare sector will grow significantly. On the other, the limelight is about to shift from urban hospitals to grassroots healthcare providers, and a share of healthcare expenditure with it. As such, multinational healthcare players need to understand that the reform's emphasis is not on expanding demand for high-end products and services or finding mechanisms for private or foreign participation. Indeed, access for multinational healthcare players is at best a backburner concern for PRC policymakers right now.

Many multinational healthcare players will continue to focus on the Grade 3 hospitals that have been their main market to date and where the high-end opportunities will continue. With more patients encouraged to consult their local health centers in times of illness, the strengthening of the primary care infrastructure combined with a functioning referral system could boost demand for secondary and tertiary care hospitals. This would have positive implications in terms of high-end opportunities for multinational healthcare players.

Meanwhile, the drive to improve the accessibility and affordability of healthcare will create an immense market opportunity for low-cost solutions. To take advantage, most multinational healthcare players would have to rethink their approach to China and realign themselves with the PRC government's initiatives, at least to some extent. This could involve having stratified portfolios with less-sophisticated products at lower price points, expanding sales and distribution networks to reach grassroots healthcare providers and rural regions, and being sufficiently savvy to pick the right pilot projects in which to participate and influence. Companies could make a strong case for examining acquisition targets in China that could fulfill these needs.

Such strategies must be considered in the context of the next five or ten years. This is not easy. Using the healthcare systems of other countries as indicators of China's future direction would be misleading. China's unique circumstances, including the fact that it is home to a fifth of the world's population, are reasons why China will inevitably follow its own path. Over the next decade, innovations and lessons from China's healthcare sector reform that have relevance to other countries will emerge. In addition, some Chinese healthcare players will almost certainly become multinational players in their own right. The current healthcare reform plan will be a major milestone along the way. 完

The drive to improve the accessibility and affordability of healthcare will create an immense market opportunity for low-cost solutions.

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China Deals

Sales and Investment

April 2009

The following listings contain information from recent press reports of business contracts and negotiations exclusive of those listed in previous issues. For the most part, the accuracy of these reports is not independently confirmed by the *CBR*. Firms whose sales and other business arrangements with China do not normally appear in press reports may have them published in the *CBR* by sending the information to the attention of the editor (publications@uschina.org). The full list of deals will no longer be printed in each issue; *CBR* subscribers with online access and members of the US-China Business Council can now access complete China Deal Database listings from 2000 to present at www.chinabusinessreview.com.

Julia Zhao

Automotive

CHINA'S IMPORTS

Comesys Europe Ltd. (UK)
Will supply Jiangsu-based Yangzhou Yaxing Motor Coach Co., Ltd. with 2,500-3,000 Mini Hybrid TK systems for use in eco-friendly buses. $15 million. 04/09.

INVESTMENTS IN CHINA

Continental AG (Germany)
Opened automatic tech center in Jiading Industrial Zone, Shanghai, to develop and test products for the Chinese market. 04/09.

The Renault-Nissan Alliance, a partnership between Renault SA (France) and Nissan Motor Co., Ltd. (Japan)/PRC MIIT
Signed MOU to promote the use of electric cars and maintain battery recharge networks in China. 04/09.

Aviation/Aerospace

OTHER

Federal Aviation Administration (US)/CAAC
Signed MOU to cooperate on best environmental practices at airports in both countries. 04/09.

Government of Taiwan/ Government of the PRC
Signed agreement to open regular direct flights across the Taiwan Strait. 04/09.

Mesa Air Group, Inc. (US)
Will sell its 49% stake in Chinese Kunpeng Airlines, a JV between Mesa Air and Shenzhen Airlines Co., Ltd. $4.5 million. 04/09.

Banking & Finance

INVESTMENTS IN CHINA

European Investment Bank (Luxembourg)
Will provide loan to the Government of the PRC for Sichuan earthquake reconstruction. $160 million. 04/09.

MoneyGram International Inc. (US)
Will offer money transfer services in 200 BOC locations in Beijing. 04/09.

OTHER

BOC
Abandoned plans to buy 20% stake in France-based La Compagnie Financiere Edmond de Rothschild. 04/09.

Central Bank of Argentina/BOC
Signed currency swap agreement with aims to stabilize regional currency. $10.25 billion. 03/09.

Government of Taiwan/ Government of the PRC
Signed framework agreement to set up a currency cleaning and supervisory system for financial initiatives to establish branches in both jurisdictions. 04/09.

Inter-American Development Bank (US)/CDB
Signed MOU to cooperate on financing projects in Latin America. 03/09.

Philippines Stock Exchange/ Shenzhen Stock Exchange
Signed MOU to forge strategic alliance for mutual cooperation and sharing of information. 04/09.

Chemicals, Petrochemicals & Related Equipment

CHINA'S INVESTMENTS ABROAD

Sinopec Yizheng Chemical Fiber Co., Ltd. (Jiangsu)
Acquired remaining 50% stake in Yihua Unifi Fiber Industry Co., Ltd., a 50-50 JV between Sinopec Yizheng Chemical and Unifi Asia Holding SRL, a wholly owned subsidiary of US-based Unifi, Inc. $9 million. 04/09.

OTHER

Mitsubishi Rayon Co., Ltd. (Japan)
Won MOFCOM approval to purchase UK-based Lucite International, Inc. $1.6 billion. 04/09.

Education

INVESTMENTS IN CHINA

Asiapharm Group Ltd. (Singapore), National Health Service of Scotland, University of Edinburgh (UK)/PRC Ministry of Health
Will establish training program for hospital managers and pharmacists in China, funded by Chinese partners. 04/09.

Sun Microsystems, Inc. (US)/PRC State Administration of Foreign Experts Affairs (Beijing)
Signed MOU to cooperate on series of educational programs to improve quality of Chinese university staff and IT. 04/09.

OTHER

Belarusian State University (Belarus)/Lanzhou University (Gansu)
Signed cooperation agreement for student and professor exchanges and information and research sharing. 04/09.

ChinaCast Education Corp. (Beijing)
Signed MOU to acquire a 100% interest in the holding company of an accredited, private university in Southwestern China. 04/09.

Government of Singapore/ Government of the PRC
Signed MOU to cooperate on twinning programs, teacher exchanges, and conferences. 04/09.

Hong Kong University of Science & Technology/Kunming Institute of Botany, Chinese Academy of Sciences (Yunnan)
Signed agreement to set up joint lab to conduct research on natural medicine and neurobiology. 04/09.

Mahatma Gandhi University (India)/Jinan University (Shandong)
Signed MOU to cooperate on joint research, teaching, and staff and student exchanges. 04/09.

University of Arbertay (UK)/Peking University (Beijing)
Signed MOU to collaborate on curriculum design, teaching and learning methods, and strengthening graduate employability. 04/09.

China Deals

Electronics, Hardware & Software

CHINA'S IMPORTS

Hitachi Global Storage Technologies (US)/Lenovo Group Ltd. (Beijing)
Signed one-year MOU to continue shipment of hard drives to Lenovo. 04/09.

INVESTMENTS IN CHINA

Advanced Micro Devices, Inc. (US)/Hisense Co. Ltd. (Shandong)
Signed agreement to establish joint design center to optimize software and hardware design of digital home products. 04/09.

United Microelectronics Corp. (Taiwan)
Will acquire 85% remaining stake for full ownership of Jiangsu-based Hejian Technology Co., Ltd. $285 million. 04/09.

Energy & Electric Power

INVESTMENTS IN CHINA

Kazatomprom Natsionalnaya Atomnaya Kompaniya Ao (Kazakhstan)/China Guangdong Nuclear Power Group Co., Ltd.
Will form JV to construct nuclear power plants in China and supply Guangdong Nuclear Power with 24,000 tons of uranium. 04/09.

Westinghouse Electric Corp. (US)/State Nuclear Baoti Zirconium Industry Co., Ltd. (Shaanxi)
Will form JV to construct and operate a plant to produce nuclear-grade zirconium sponge in Nantong, Jiangsu. (US:50%-PRC:50%). 04/09.

OTHER

Kinmac Holdings Ltd. (Taiwan)/Jinzhou Yangguang Energy Co., Ltd., a subsidiary of Solargiga Energy Holdings Ltd. (Liaoning)
Formed JV, Jinzhou Jinmao Photovoltaic Technology Co., Ltd., in Liaoning to produce photovoltaic modules and systems. (PRC:51%-Taiwan: 35%-Other:14%). $5.9 million. 04/09.

Pebble Bed Modular Reactor (Pty.) Ltd. (South Africa)/ Chinergy Co. Ltd. (Beijing), Institute of Nuclear and New Energy Technology of Tsinghua University (Beijing)
Signed MOU to collaborate on strategic and technical areas related to high-temperature reactor projects in both countries. 03/09.

Q-Cells AG (Germany)/ LDK Solar Co., Ltd. (Jiangxi)
Formed JV to build large solar power plants in Europe and China. 04/09.

Food & Food Processing

CHINA'S IMPORTS

Marubeni Corp. (Japan)/China Grain Reserves Corp. (Beijing)
Signed LOI to import 4 million tons of soybeans to China per year. 04/09.

Milk Link Ltd. (UK)
Will supply Inner Mongolia Yili Industrial Group Co., Ltd. with stilton and cheddar cheese for the PRC market. 04/09.

INVESTMENTS IN CHINA

DSM Nutritional Products, Inc. (US)
Signed investment contract with the Changchun Economic & Technology Development Zone to establish in Jilin its fourth feed premix plant in China. $5 million. 04/09.

Healthcare Services & Investment

INVESTMENTS IN CHINA

Bill & Melinda Gates Foundation (US)/Government of the PRC
Established partnership to detect and treat tuberculosis with Gates Foundation funding. $33 million. 04/09.

OTHER

Government of Turkey/ Government of the PRC
Signed health cooperation protocol and will establish working groups to examine and improve each other's health systems. 04/09.

Infrastructure

CHINA'S INVESTMENTS ABROAD

Government of the PRC
Established "China-ASEAN Fund on Investment Cooperation" to develop infrastructure in the ASEAN region. $10 billion. 04/09.

Internet/E-Commerce

INVESTMENTS IN CHINA

The Penguin Group (UK)/Beijing Founder Apabi Technology Co., Ltd.
Signed distribution agreement to make Penguin e-Book titles available for download in China. 04/09.

Legal Services

OTHER

Government of Germany/ Government of the PRC
Signed MOU to cooperate on Legal Field Dialogue Forum with German financing. $6.2 million. 04/09.

Machinery & Machine Tools

OTHER

China-Africa Development Fund (Beijing), First Tractor Co., Ltd. (Henan)
Will form JV to export agricultural and engineering machinery to Africa. $36.6 million. 04/09.

Medical Equipment & Devices

OTHER

Bayer AG (Germany)/Tsinghua University (Beijing)
Will establish joint research center at Tsinghua. 03/09.

Abbreviations used throughout text: ABC: Agricultural Bank of China; ADB: Asian Development Bank; ASEAN: Association of Southeast Asian Nations; ATM: automated teller machine; AVIC I and II: China Aviation Industry Corp. I and II; BOC: Bank of China; CAAC: Civil Aviation Administration of China; CATV: cable television; CBRC: China Banking Regulatory Commision; CCB: China Construction Bank; CCTV: China Central Television; CDB: China Development Bank; CDMA: code division multiple access; CEIEC: China National Electronics Import and Export Corp.; China Mobile: China Mobile Communications Corp.; China Netcom: China Netcom Corp. Ltd.; China Railcom: China Railway Communications Co., Ltd.; China Telecom: China Telecommunications Group Corp.; China Unicom: China United Telecommunications Corp.; CIRC: China Insurance Regulatory Commission; CITIC: China International Trust and Investment Corp.; CITS: China International Travel Service; CNOOC: China National Offshore Oil Corp.; CNPC: China National Petroleum Corp.; COFCO: China National Cereals, Oils, and Foodstuffs Import and Export Corp.; COSCO: China Ocean Shipping Co.; CSRC: China Securities Regulatory Commission; DSL: digital subscriber line; ETDZ: economic and technological development zone; GSM: global system for mobile communication; GPS: global positioning system: ICBC: Industrial and Commercial Bank of China; IP: Internet protocol; IT: information technology; JV: joint venture; LNG: liquefied natural gas; LOI: Letter of intent; MIIT: Ministry of Industry and Information Technology; MOFCOM: Ministry of Commerce; MOU: memorandum of understanding; NA: not available; NDRC: National Development and Reform Commission; NORINCO: China North Industries Corp.; PAS: personal access system; PBOC: People's Bank of China; PetroChina: PetroChina Co., Ltd.; RMB: renminbi; R&D: research and development; SARFT: State Administration of Radio, Film, and Television; SASAC: State Assets Supervision and Administration Commission; SEZ: special economic zone; Sinopec: China Petroleum & Chemical Corp.; SINOTRANS: China National Foreign Trade Transportation Corp.; UNDP: United Nations Development Program; SME: small and medium-sized enterprise; Wi-Fi: wireless fidelity; WFOE: wholly foreign-owned enterprise.

Metals, Minerals & Mining

CHINA'S INVESTMENTS ABROAD

Oz Minerals Ltd. (Australia)/ China Minmetals Corp. (Beijing)
Signed second deal to address Australian government national security concerns about selling a mine on a sensitive military site. $1.2 billion. 04/09.

Miscellaneous

INVESTMENTS IN CHINA

SK Telecom Co., Ltd. (South Korea), Cisco Systems Inc. (US)
Signed MOU to develop business models and projects to aid in earthquake reconstruction in Sichuan. 04/09.

OTHER

Government of Peru/ Government of the PRC
Signed free-trade agreement. 04/09.

National Fire Authority (Fiji)/ Chinese Fire Service (Beijing)
Signed MOU to cooperate and provide technical assistance in fire fighting. 04/09.

Nepal-China Executives Council (Nepal)/ Chinese People's Association for Friendship with Foreign Countries (Beijing)
Signed MOU to promote trade and investment between Nepal and China and form a committee to help companies find bilateral trade partners. 04/09.

Petroleum, Natural Gas & Related Equipment

CHINA'S IMPORTS

Petroleo Brasileiro SA (Brazil), Unipec Asia Co. Ltd., a subsidiary of Sinopec (HK)
Signed agreement to export 150,000 barrels of oil per day to China beginning 2009 and 200,000 barrels per day from 2010 to 2019. 05/09.

CHINA'S INVESTMENTS ABROAD

Kazmunaigas Torgovy Dom Ao (Kazakhstan)/CPNC (Beijing)
CNPC will lend $5 billion to Kazakhstan-based Kazmunaigas Torgovy Dom Ao, and the two firms will jointly purchase Kazakhstan-based Mangistaumunaigas from Indonesia-based Central Asia Petroleum Ltd. (Kazakhstan:51%-PRC:49%). $3.3 billion. 04/09.

Kuwait Oil Co./Sinopec
Signed five-year contract to build five oil rigs in Kuwait. $402 million. 04/09.

OTHER

Government of Pakistan/ Government of the PRC
Signed MOU for energy cooperation and exploration in Pakistan. 04/09.

Government of Russia/ Government of the PRC
Will jointly construct oil pipeline from Skovorodino, Russia, to Daqing, Heilongjiang, and provide China with 15 million tons of crude oil per year from 2011 to 2030 in exchange for loans to Russian oil firms. $25 million. 04/09.

StatoilHydro ASA (Norway)
Will transfer its 75% interest in the Lufeng oil field project in the South China Sea to Hong Kong-based CNOOC Ltd. 04/09.

Pharmaceuticals

OTHER

Gvk Biosciences Private Ltd. (India)/Excel PharmaStudies Inc. (Beijing)
Formed strategic alliance to conduct clinical trials in Asia. 04/09.

Sanwa Kagaku Kenkyusho Co., Ltd. (Japan)/Shanghai ChemPartner Co., Ltd.
Formed strategic alliance. 04/09.

US Pharmacopeial Convention, Inc./National Institute for the Control of Pharmaceutical and Biological Products (Beijing)
Signed second MOU to collaborate on drug testing and professional exchange. 03/09.

Research & Development

OTHER

Government of Serbia/ Government of the PRC
Signed agreement on scientific and technological cooperation. 04/09.

Telecommunications

CHINA'S INVESTMENTS ABROAD

JSC Kazakhtelecom (Kazakhstan)/BOC (Beijing), Huawei Technologies Co., Ltd. (Shenzhen)
Signed MOU to finance telecom development in Kazakhstan. 04/09.

INVESTMENTS IN CHINA

Alcatel-Lucent (France)
Will provide Beijing-based China Mobile with wireless networking equipment, optical, microwave and IP transmission offerings, IP service routers, application platforms, and related services. $1 billion. 04/09.

Alcatel-Lucent (France)
Will provide Beijing-based China Telecom with networking equipment, application platforms, optical and IP transmission platforms, IP service routers, and network maintenance services. $700 million. 04/09.

Megatech Engineering Ltd. (Canada)/ZTE Corp. (Guangdong)
Signed MOU to expand CDMA 2000 1x next generation network in China. 04/09.

Motorola, Inc. (US)
Won contract to provide China Unicom with W-CDMA radio access network equipment, packet switched core network, and interoperability functions that will enable integration of GSM and W-CDMA networks. 04/09.

OTHER

Nokia Corp. (Finland)/ China PTAC Communication Service Co., Ltd. (Beijing)
Renewed strategic partnership agreement and agreed to expand ties in 3G and operator business. 03/09.

Textiles & Apparel

INVESTMENTS IN CHINA

Uniqlo Co., Ltd. (Japan)/ Taobao.com (Zhejiang)
Will launch online sales of Uniqlo's casual wear products in China. 04/09.

Tourism & Hotels

OTHER

Municipal Government of Seoul (South Korea)/Municipal Government of Tianjin
Signed MOU to strengthen exchanges and cooperation in tourism, economy, culture, and environment. 04/09.

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