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From the Desk of...

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Chinese businesses do not compete unfairly. Just differently.

This is the second article in a series that precedes his new book '*The End of Progress*', to be published in June this year, wherein Graeme Maxton suggests that the Chinese are simply using an alternative business model which is not necessarily wrong, just different.

As Chinese and American officials hurl accusations of currency manipulation across the globe like clumps of mud, another battleground is looming. The turf this time is much less squishy, however. The next fight is over ideology.

Many people accuse Chinese firms of competing unfairly. They mutter about how former state-owned enterprises get access to low-cost finance and counterfeit technology. They complain about tough new Chinese laws which target foreign firms. They accuse Chinese businesses of hoarding valuable raw materials. They talk about uneven playing fields, unsustainably low profit margins and overly-cosy links between businesses and regulators.

Chinese firms are guilty of not playing by the rules, they say.

But they are wrong. The Chinese are not guilty of anything very much. They may have 'borrowed' a great deal of foreign technology without asking but they are not competing unfairly. Just differently.

It is not just a question of having supportive regulators, lower margins and someone else's intellectual property. The Chinese are using a different business model too.

In the US and Europe, businesses are expected to survive independently. They are expected to raise finance themselves, compete for resources and people, establish their own customer base and make a return on their investments, a profit big enough to reward shareholders and reinvest for the future. Businesses which fail to achieve this balance go bust.

There is another way.

In China things work differently. There is another sort of business model, partly a legacy of the country's communist past. Big businesses are not expected to stand in isolation. They are expected to retain close links to the state. They are often directed centrally, by the government, with senior managers moved between firms on the orders of Beijing. Many bosses remain active members of the Communist Party, with clear lines of loyalty and understood expectations. Although many large Chinese firms are listed on local and international stock markets, their presence there is mostly to gain access to cheap finance. Chinese businesses have much less need to make a profit or generate dividends. The rewards for investors are expected to come from how well they gamble on the market.

Chinese firms can also be provided with their customers by the state, as if on a platter. When big domestic tenders are up for grabs, an increasing number are only open to Chinese firms. This ensures skills, jobs and wealth are kept at home, not sucked away by foreign-devil employers.

Chinese firms are often given privileged access to new technologies too, removing hefty R&D costs. Leached away from foreign firms and then localised, Chinese companies have frequently acquired their capabilities without cost. While this breaks foreign laws, many Chinese firms see their actions differently. They see the foreign regulations as the unreasonable ones. How can it be right for American and European firms to restrict access to designs which are well-established and ubiquitous? Surely that is unfair. Besides, did Europeans not copy Chinese technology in the past? Why is it wrong this time? Moreover, if technology can be acquired without any cost, surely getting hold of it this way makes the most sense. That is how business is done. There is no wasted effort.

Similarly, when big Chinese companies go abroad, the state is often beside them, like a hand inside a puppet. When Chinese firms make a bid to build power plants or railways in Africa or Eastern Europe, the Chinese state, or one of its banks, will provide the customer with low-cost financing to ease the deal through. Government cadres will also help Chinese businesses gain access to valuable resources, smoothing the path through complex deals. They will offer schools, roads and bridges, built by Chinese workers, in return for coal, oil and iron ore. That way, the Chinese get the business, the jobs and the resources.

While rival European or US bidders complain that they are unable to compete, the Chinese government sees these deals as strategic. They are a clever blend of good business and good politics, a way to win contracts and geopolitical influence at the same time. If such deals incur losses along the way, so what? There are bigger issues at stake, and longer term implications.

Stamping your feet will surely help.

Despite the squawking of many foreign politicians and business leaders, the Chinese business model is not wrong. It is just different. It does not depend on the free market and profits to survive. It takes another approach, and perhaps a better one.

Since the late 1970s, the West has become obsessed with just one business model. The unrestricted free-market has been the mantra. Markets should be left to run themselves with minimal regulation. The invisible hand will fix any problems that occur, punishing the uncompetitive and supporting the strong. Many business leaders in America and Europe have been fooled into believing that this was the only way to compete, that this was the only way to achieve growth and economic superiority.

Western banks, governments and businesses have already discovered that their economic and business model was less reliable than they once thought. Now they are about to see that there is also another way to compete, which undermines their ideas further still.

It is the Western firms and their governments which have been misguided. Chinese businesses are simply using another way to take them on. If the Westerners can't handle that, think the Chinese, that's their problem.

In the ideological battle to come, count on China.

The article comes from a new book "The End of Progress" how modern economics has warped our ideas of social progress, to be published by Wiley in June 2011.

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About Graeme Maxton and The Insight Bureau

Graeme Maxton is a writer and commentator on world business, Asia and the automotive industry. The Insight Bureau represents a resource network of individuals, including Graeme Maxton, for speaking engagements and client events, as well as providing confidential, in-house briefings. Mr Maxton is an expert chairman and moderator of business dialogue at conferences and client forums around the world.

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