

Catching the Chinese tiger by the tail – very carefully

Liam Baldwin

A fresh import to Massey University's management school in Albany has a word of caution about New Zealand's strong economic relationship with China.

Usha Haley, a professor of international business, arrived in New Zealand a month ago from Harvey Kennedy School in Massachusetts in the US. She said that while free trade is a laudable goal, care must be taken.

The New Zealand China Free Trade Agreement (FTA) came into force nearly two years ago. Both countries have a goal of doubling two-way trade to \$20 billion over the next five years.

While the direct economic benefits of increased trade with China are obvious, Prof Haley said special care must be taken to protect what is most highly prized in New Zealand from being lost during the process.

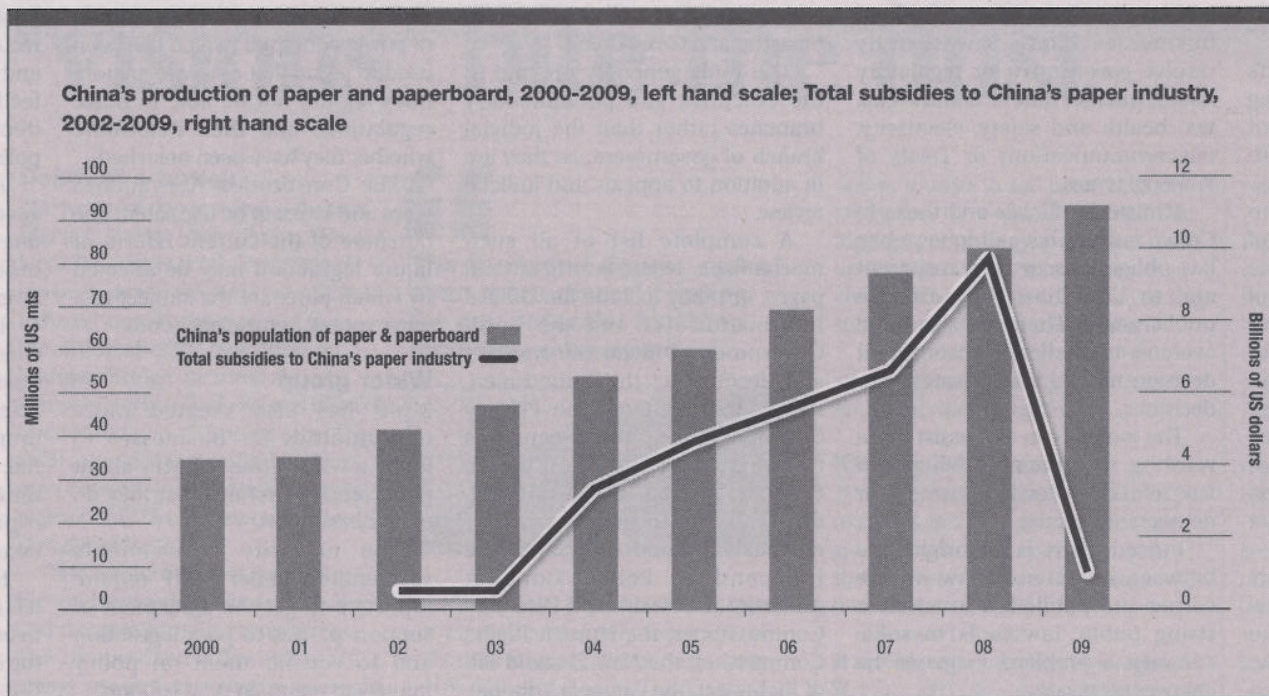
As an example, Prof Haley points to a research paper she completed for US-based think tank the Economic Policy Institute recently about



USHA HALEY: Warns about the Chinese threat to local business

the heavily subsidised paper industry in China.

Called "No Paper Tiger, Subsidies to China's Paper Industry from 2002-09," the document has been used to form the basis of a congressional plea to US president



Barack Obama, signed by 100 representatives.

China's paper industry is booming, despite the country having little in the way of raw resources to fuel the growth.

In addition, the growth of some individual companies has far exceeded what would be considered natural reflecting the injection of massive amounts of capital.

Since 2000, Prof Haley said China's paper manufacturing sector had tripled and in 2008 it overtook the US to become the world's largest producer of paper and paper products.

However, the country imports nearly all the raw materials to feed the manufacture of materials in the form of logs and wood pulp.

New Zealand's wood exports to China are skyrocketing, up 38% this year to 4.8 million cubic metres. Last year China was the top destination for radiata logs from New Zealand, for the first time.

Prof Haley pointed to a single company, Nine Dragons

Paper, which was expecting to double its production over the next year. "If announced capacity expansion takes place, the company will move from a mid-size global player to among the five largest in the world," she said.

Subsidies

Massive injections of capital in the form of cash, gifted land, free electricity and even free saplings to establish plantation forests have been provided to the sector over the past decade, according to Prof Haley. She said between 2002 and 2009, more than \$US33 billion worth of subsidies has been injected into the industry – and that's a conservative estimate based only on what she could actually prove.

It's this massive growth revealed in Prof Haley's "No Paper Tiger" paper that prompted members of Congress to write to President Obama.

"We write to bring to your attention the damage caused

to US manufacturing by the subsidies that China's paper industry receive, which are significant and market-distorting," the members wrote on July 28. "It is clear to us that the rise of China's paper industry is less related to market forces than to a decision by China's government to implement an industrial policy that promotes domestic paper production."

It highlights declining production in the US while China's industry surges ahead and pointed to the loss of nearly 160,000 jobs in the years between 2002-09.

For the US, Prof Haley said it was probably too late to arrest the decline, and possibly even for New Zealand.

However, there were lessons to be learned in dealing with China and the protection of what is considered important – both economically and intrinsically.

What about New Zealand? Prof Haley said she was a proponent of free trade but

it was about economics. Free trade, she said, did not exist where there were heavy subsidies.

She said that China's way of thinking in terms of economics was quite different from how things were considered in the west.

Paradigm of domination

She said because there is government influence, if not control, of large companies, the end goals and world views could be different. Instead of striving to be the most competitive and make the most profit, a paradigm of domination was more important.

And, as demonstrated in the paper industry and other sectors such as the glass industry, the push for domination forced other major players from the market.

New Zealand needed to be extremely cautious.

"[Prime Minister John] Key's suggestion that trade will triple to China is a pipe-dream," she said. "There is no basis for that comment."

Prof Haley pointed to her birth country, India, which has substantial trade with China and is an importer of many manufactured goods, but the opposite flow is based on raw materials rather than valued added.

Similarly, the US would become an exporter of pulp and recycled paper to China rather than of actual paper – at least until plantation forests were established there, drying up even that flow of trade.

"And this is just the tip of the iceberg."

Prof Haley estimated that within the next five to 10 years, the need for China to import wood pulp would diminish.

Important industries in New Zealand, such as dairy, needed to be protected from similar fates.

Prof Haley said government policy also needed to be

sensitive to the needs of the manufacturing industry.

It wasn't just the threat of China working to dominate in any particular sector, there were also fundamental issues over protection of all the work behind the industry such as intellectual property.

Although China has highly sophisticated laws for IP protection, Prof Haley said it was also the largest violator of IP in the world.

As a broad example she referred again to the paper industry and a Swedish company called Arctic Paper, which markets its trademarked brand of glossy book paper – Munken – around the world.

However, after branching out into Asia with a headquarters in Singapore and exporting to China, it failed to trademark the word "munken."

As a result, Prof Haley said "munken" is now a Mandarin term that now means glossy book paper and the company is now in danger of losing its export markets.

"A slipup can have irrevocable results because of China's size. Size matters."

China can be ruthless. Prof Haley explained that foreign direct investment is banned in some sectors there as a form of protectionism and the discernable industry subsidies equate to between 20%-25% of its gross domestic product.

At the same time China was exploiting the weaker rules for foreign direct investment in other countries and grabbing substantial assets.

"I'm interested in looking at the relationship between New Zealand and the rest of the world and the effects of the free trade agreement [with China]," she said.

"New Zealand has to exhibit some caution and make reasoned choices. It has a small economy but is often dealing with very much larger economies. Understanding the history, culture and goals of partners is the key to successful global relationships."

Prof Haley said a broad understanding was part of a cautious approach.

"I am a great believer in free trade but it is important for the world to more fully understand China's development and incredible rise in so many industries. We have to understand to compete more effectively. In the US many did not see the ramifications of China's state capitalism on domestic industries."

"The effects on US' industries I have studied, including paper, steel and glass, have been irrevocable and the speed of change has been unprecedented in modern times."

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