

CHINESE FIRMS, GLOBAL FIRMS

Industrial policy in the era of globalization

Peter Nolan

Chinese Firms, Global Firms

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Chinese Firms, Global Firms

China has achieved remarkable, sustained economic growth under the policies of 'reform and opening up' put into place since the late 1970s. Its industrial policies have nurtured a large group of firms with high profits and a high market capitalization. However, few people in the West can name a single Chinese firm. During the modern era of capitalist globalization, firms from the high-income countries have spread their business systems across the world. This has presented a profound challenge for industrial policy in developing countries, including even China, the world's second-largest economy. China is unique among large latecomer developing countries in having reached the position of being a huge, fast-growing economy, with a tremendous impact on the rest of the world but lacking a substantial group of globally competitive firms. This volume explores this paradox. Fully understanding the industrial policy challenge that the era of capitalist globalization has produced for China is essential for harmonious international relations.

Peter Nolan holds the Chong Hua Chair in Chinese Development and is Director of the Centre of Development Studies, University of Cambridge, UK. He has spoken at the Chinese Government's annual China Development Forum since its inception in 2000. He has testified at the US–China Economic and Security Review Commission of the US Congress and lectured to the Board of the US–China Business Council. He is a member of the UK Government's Asia Task Force. He holds an honorary doctorate from the Copenhagen Business School. He was awarded the CBE (Commander of the Most Excellent Order of the British Empire) 'for services supporting China's integration into the global economy'. The *Financial Times* commented: 'Nolan knows more about Chinese companies and their international competition than anyone else on earth, including in China'.

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- 52 **The East Asian Computer Chip War**
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For Ajit Singh

Tables

1.1	Some indicators of the competitive capability of selected leading Chinese aerospace companies and selected leading global companies, 1997	5
1.2	Some indicators of the competitive capability of selected leading Chinese pharmaceutical companies and selected leading global companies, 1997	6
1.3	Some indicators of the competitive capability of selected leading Chinese power equipment companies and selected leading global companies, 1998	7
1.4	Some indicators of the competitive capability of selected leading Chinese oil/petrochemical companies and selected leading global companies, 1997	8
1.5	Some indicators of the competitive capability of selected leading Chinese auto companies and selected leading global companies, 1998	9
1.6	Some indicators of the competitive capability of selected leading Chinese auto component companies and selected leading global companies, 1998	10
1.7	Some indicators of the competitive capability of selected leading Chinese steel companies and selected leading global companies, 1998	11
1.8	Dominance of firms based in high-income countries of the global big business revolution	17
1.9	Global oligopoly in the business revolution	19
3.1	Mergers and acquisitions in the information technology sector, 2007–09	57
3.2	Mergers and acquisitions in the beverage industry, 2007–09	58
4.1	Industrial concentration among system integrator firms, 2006–09	67
4.2	Industrial consolidation among selected firms within global value chains, 2006–08	68
4.3	Industrial concentration and the global business revolution: Global 1400 R&D investment, 2007	69
4.4	The global financial crisis and industrial concentration: pharmaceuticals mergers and acquisitions of over US\$1 billion, 2007–10	71
4.5	Increase in stock of FDI during three decades of globalization	72
4.6	Selected indicators of FDI and international production, 1982–2008	73
4.7	Foreign operations of the world's 100 largest TNCs and the 100 largest TNCs from developing economies, 2007–08	74
4.8	China's FDI stock in comparative perspective	75
5.1	Projections for CO ₂ emissions	83
5.2	Energy efficiency and carbon efficiency under 'new policies'	83

5.3 Energy and CO ₂ emissions savings under 'new policies'	84
5.4 Global electricity investment under the International Energy Agency's 'new policies' scenario, 2011–35	87
5.5 Total final consumption of energy in transport, buildings and industry under 'new policies' scenario	88
5.6 Globalization and Schneider Electric: distribution of revenues and employment, 2011	94
5.7 Share of top 5/10 firms in R&D spending in selected sectors among the world's 1,000 largest companies by R&D spending (Global 1000), 2009–10	95
6.1 Relative growth of trade and FDI, 1990 and 2009	99
6.2 Increase in FDI during globalization	100
6.3 International operations of selected US companies: foreign (non-US) assets, sales, and employment as a proportion of the total, 2008	101
6.4 China and the world turned upside down	104
6.5 Balance between China's inflows and outflows of FDI	106
6.6 Distribution of China's outward stock of FDI, 2009	106
6.7 Revenue and R&D expenditure of leading aerospace sub-systems integrators, 2008–09	112
7.1 Stock of inward FDI in developing countries, 2000 and 2011	133
7.2 China operations of selected US firms	135
7.3 Foreign-invested enterprises (including firms from Taiwan, Hong Kong and Macao) in the Chinese economy, 2007–10	141
7.4 Market share of foreign-invested enterprises (including firms from Taiwan, Hong Kong and Macao) in the Chinese economy, 2010	141
7.5 Distribution of China's stock of FDI by country and region, 2011	144
7.6 Globalization and FDI: outward stock of FDI, 1990 and 2011	145
7.7 Distribution of China's FDI by sector (stock, end 2011)	145
7.8 International assets compared: China and individual global firms, 2011	146
7.9 FDI stock of American, Japanese and German firms in China, compared with the FDI stock of Chinese firms in the US, Japan and Germany, 2011	146

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Preface

China has achieved remarkable, sustained economic growth under the policies of 'reform and opening up' put into place since the late 1970s. It has risen to become the world's largest exporter and has the world's second largest gross domestic product. China's industrial policies have nurtured a large group of firms with high profits and a high market capitalization. However, few people in the West can name a single Chinese firm. Chinese firms have a negligible business system within the high-income countries. During the modern era of capitalist globalization, market forces have been unleashed in an unprecedented fashion. Firms from the high-income countries have spread their business systems across the world through both merger and acquisition and organic growth. This has radically distanced the global firm from its home base, producing severe social and political difficulties within the high-income countries. However, it has presented a mighty challenge for industrial policy in developing countries, including even China, the world's second largest economy. China is unique among large latecomer developing countries in having reached the position of being a huge, fast-growing economy, with a tremendous impact on the rest of the world but lacking a substantial group of globally competitive firms. This book explores that paradox. Fully understanding the industrial policy challenge that the era of capitalist globalization has produced for China is essential for harmonious international relations.

This book contains unpublished essays that were written between 2000 and 2012. This foreword was written in December 2012. At the Eighteenth Party Congress, held in November 2012, China confirmed the changes in the country's top leadership. The 'fourth generation', with President Hu Jintao and Premier Wen Jiabao at the top, handed the leadership baton to the 'fifth generation', Xi Jinping and Li Keqiang. At the centre of China's industrial policy is the relationship between China and the global business system. Chinese leaders have consistently expressed the intention to nurture a substantial group of globally competitive large indigenous Chinese firms. In his report to the Eighteenth Party Congress on 8 November 2012, President Hu Jintao said: 'Chinese companies should expand their overseas presence at a faster rate, enhance their cooperation in an international environment and develop a number of world-class multinational corporations'. The chapters in this book address this issue from different angles and at different points in time.

Chapter 1 ('China and the World Trade Organization: the challenge for China's large-scale industry') was prepared for the first annual China Development Forum, held in Beijing in March 2000. Between 1994 and 1999, Dr Wang Xiaoqiang¹ and I conducted research on the transformation of China's giant state-owned enterprises. This research took place under the auspices of the System Reform Institute of the System Reform Commission of the Chinese State Council. We conducted fieldwork in leading Chinese state-owned enterprises in key industries, including aerospace, pharmaceuticals, power equipment, oil and petrochemicals, automobiles and auto components, steel and mining. Our research attempted to benchmark China's giant state-owned enterprises against the world's leading firms in each of these sectors.² As well as analyzing Chinese giant state-owned enterprises, the research involved fieldwork inside leading global corporations. Our central conclusion was that the challenge of the 'global business revolution' for firms from developing countries, including those from China, was far greater than most scholars and policy makers appreciated. It is widely argued that the revolution in information technology has created a 'post-modern', 'networked' and 'flat' world, in which nimble, small and medium-sized firms are replacing the traditional large, cumbersome corporation. Instead, we concluded that the era of globalization has witnessed intense industrial consolidation at a global level, not only among the leading 'system integrator' firms with global brands and leading technologies but also deep inside the supply chain. Industrial consolidation within the supply chain has come about mainly through downward pressure from system integrator firms. This 'cascade effect' was analogous to the pressure exerted on the rocks by water cascading down a waterfall.³ The global business revolution since the 1970s produced a structure with intense oligopolistic competition across large swathes of the value chain. The global business structure today looks remarkably similar to that predicted by Karl Marx in the mid-nineteenth century, driven by the 'law of concentration of capital'.

China joined the World Trade Organization (WTO) in 2001. The decision to do so was immensely controversial in China, with intense debate about the capability of China's large firms to compete on the 'global level playing field' established by the rules of the WTO. In 2000, the Chinese government established the 'China Development Forum'. It brings together international business leaders with Chinese government ministers and the heads of the country's leading state-owned enterprises for a three-day meeting devoted to better understanding the issues arising from China's deepening integration into the global economy. Each meeting of the Forum concludes with a long meeting with the Chinese Premier, initially with Zhu Rongji and latterly with Wen Jiabao.

The opening address to the first forum, held in March 2000, was delivered by Wen Jiabao, the (then) Vice-Premier of the State Council, followed by a response from Maurice (Hank) Greenberg, the (then) Chairman of AIG Group. The first working session of the first Forum was entitled 'China's SOE Reform and International Experience'. There were two presentations at this session. The first was from Minister Chen Qingtai, Vice-President and Party Secretary of the Development Research Centre of the State Council. The second was my own (Chapter 1), which summarized the conclusions of the research that Dr Wang Xiaoqiang and I had

undertaken during the 1990s. It concluded that China's giant state-owned enterprises were still far from ready to compete on the global stage with the world's leading firms from the high-income countries. Since 2000, China has made great efforts to nurture a group of internationally competitive state-owned enterprises. Today, China's firms in the *FT 500* are second only to those of the USA in terms of their total market capitalization. However, as later chapters in this book demonstrate, establishing a large group of heavily protected state-owned enterprises that benefit from a fast-growing domestic economy is not the same thing as establishing a group of globally competitive firms with world-leading technologies, leading global brands and high international market share in the high-income countries. Despite enormous progress, there is still a wide gap between the operational mechanism of China's giant state-owned enterprises and the world's leading firms that have their headquarters in the high-income countries.

Chapter 2 ('Technical change and firm-level catch-up in developing countries: the case of telecommunications', with Jin Zhang) was prepared for the China Development Forum in 2007. We looked in detail at the telecommunications industry, examining not only the 'systems integrators' in this sector but also looking at the different segments of the industry's supply chain. It showed that the global business revolution in the telecommunications industry has been accompanied by a process of intense industrial consolidation far down into the industry's supply chain, including transmission equipment, mobile handsets, semiconductors, semiconductor equipment and silicon wafers. A crucial part of the competitive capability of the leading system integrators is the skill they have developed in coordinating the activities of the entire value chain. In other words, 'catch-up' at the level of the firm involves comprehensive analysis of the whole value chain and the role of the systems integrator firms within that structure.

Chapter 3 ('Globalization and industrial concentration: the challenge for firms from developing countries', with Jin Zhang) was prepared for a meeting of the Chinese Government's Ministry of Commerce in 2009. We examined the evidence on global industrial consolidation and technical progress in several sectors, including aerospace, automobiles, telecommunications, beverages, pharmaceuticals, information technology and financial services. We demonstrated that, across a wide range of different industries, the process of global industrial consolidation has advanced unrelentingly since the late 1990s and has continued to do so even during the global financial crisis. This chapter highlights the striking extent of concentration in global technical progress. The world's top 1,400 firms spend around US\$545 billion each year on research and development (R&D). This constitutes the core of the world's technical progress. Almost all of this R&D spending is undertaken by firms with their headquarters in the high-income countries. Among these 1,400 firms, the top 100 firms account for over 60 per cent of the total spending on R&D. In other words, the world of technical progress is anything but 'flat'.

Chapter 4 ('Globalization and China's large firms', with Jin Zhang) was prepared for the China Development Forum in 2010. It was presented at the session entitled 'Globalization of China's large corporations and its prospect', which was chaired by former Minister Chen Qingtai. The other speaker at the session was Minister Li