

SPECIAL SECTION

China

China: For U.S. Companies The “New World” Beckons

The Editor Interviews James L. “Jim” McGregor.

Editor’s note: James L. McGregor is an American author, journalist, media commentator and businessman who has lived in China for more than 20

years. He is a consultant and professional speaker who specializes in China’s business and political culture, and he speaks frequently with corporate audiences about doing business in China. He is the author of the book *One Billion Customers, Lessons from the Front Lines of Doing Business in China* (Simon & Schuster, 2005). He is the former CEO of Dow Jones & Company in China and The Wall Street Journal bureau chief in China and Taiwan. More information about McGregor is available on his Web site: www.onebillioncustomers.com.

Editor: Tell us about your background.

McGregor: I found myself in China through a circuitous route. I joined the army in the early ’70s. I ended up in Vietnam, which turned my head towards Asia and led to me to becoming a journalist. As a journalist going from the police beat in Los Angeles to covering Congress, I always watched Asia.

The rise of China captured my imagination, so I came here in 1985, and after backpacking around the country, I decided that it would be the country-happening of my lifetime.

In 1987, my wife and I got rid of everything we owned and with two suitcases moved to Taiwan to learn Mandarin. The *Wall Street Journal* hired me after I had been there for a few months. I came to China in the 1990s as *The Wall Street Journal* bureau chief where I had the privilege of tracking its growth and have been doing so ever since.

Editor: That’s fascinating. What motivated you to write the book?

McGregor: I wrote the book because I had a unique insight; I was lucky enough to have been both a journalist and a businessman in China when there were not many people who crossed that line. Journalists know a lot about China and get all over the country, but they are kept at arm’s length, and they really can’t get too deeply involved in what businesses are doing here. Because I was a business man and was chairman of the American Chamber of Commerce in China (AmCham) and served on its board for 10 years, I became familiar with how business was conducted here. With the book I tried to get below the surface of how things work here and to delve into how history influences the interest of the Chinese in business and how Americans can successfully pursue their business interests



James L. McGregor

here. It’s really a deep look at how China works and thinks.

Editor: What are the reasons for China’s success?

McGregor: This is a country that has all the ingredients for success. Its people will work day and night – they are ambitious, they are very capitalistic and business oriented and they are fantastic students. They study. What they don’t know they’ll learn. The government not only doesn’t get in their way, but it looks for ways of releasing their entrepreneurial energies. In fact, it is quite a good organizer and planner.

As I look at where the Chinese economy is going, I am confident that China will continue to grow – probably not at the present torrid pace, but it will continue to grow. They still have many hundreds of millions of people striving to reach the middle class.

Editor: Why do you think the rate of growth may slow?

McGregor: This is a country where today if the government needed to move five million people for a project, they could move them. Try that in a few years and you won’t be able to do it. As more and more people have assets and their own opinions, China is going to look like other developed countries

where progress will be slower because the government can’t just order everybody to do this or that.

Editor: The most important economic relationship in the world today is the one between the U.S. and China. Do you think that is going to continue?

McGregor: Yes, the U.S. and China have a very interesting relationship. China makes goods, we buy them. It gets the money and then they lend it back to us to fund our government. The relationship will change as China focuses more on building its domestic consumer markets and Americans get more responsible and save more and spend less. However, the U.S. and China will continue to be the dominant world superpowers, and it is unlikely that any major policy initiatives of global importance will succeed unless the U.S. and China at least see partially eye to eye just because they are the two biggest players and their economies are somewhat complimentary. But, the whole notion of a G2, of a totally dominant U.S. and China, is way overblown. There are other major players like Europe, Japan, Russia, Brazil and India to be taken into account.

HIGHLIGHTS

Law Firms

China Is Booming: M&A Opportunities Open The Door

Interview: Z. Alex Zhang JONES DAY* Page 44

A Focused Practice In An Ever-Burgeoning Market

Interview: Steven Xiang WEIL, GOTSHAL & MANGES LLP* Page 45

How A Combination Of Diverse Cultures Makes For A Dynamic Team

Interview: Ying Li, Yuval Tal and James F. Chapman PROSKAUER ROSE LLP* Page 46

The ABA Section Goes To China

Interview: Randy J. Alimont WILLIAMS KASTNER Page 47

A Chinese Company Takes The Initiative In Protecting Its Patents

Interview: Scott Stimpson and Kevin He SILLS CUMMIS & GROSS P.C.* Page 48

How A U.S. IP Lawyer Serves Chinese Clients

Interview: Jonathan Caplan KRAMER LEVIN NAFTALIS & FRANKEL LLP* Page 49

The Future Of Trade With China: A Two-Way Street?

Interview: Gilbert Kaplan and Christopher Cloutier KING & SPALDING LLP* Page 50

Doing Business In China Has Been Through Evolution, But It’s Still Not The Same As Home

Robert B. Silverman GRUNFELD, DESIDERIO, LEBOWITZ, SILVERMAN & KLESTADT LLP Page 51

Service Providers

Globalization, Information And The Business Law Marketplace In China

Gary Hornseth (Mr. Hornseth is a freelance writer, courtesy of THOMSON REUTERS.) Page 53

Some Of The Above Partner With Corporate Counsel By Providing Us With Financial And Editorial Support.

* Supporting Law Firms

James McGregor

Continued from page 43

Editor: Much of the recent focus has been on inbound Western investment in China. Now we are seeing more cross-border investment going in the other direction. What are the major implications of this, and how should those working in Western capital markets be reacting?

McGregor: In doing this, the Chinese face significant issues. Doing business in China is very local in that they have their own ways of doing things. Many of the Chinese companies that are making outbound investments are large state-owned companies that are very political. If you are the head of a state-owned company you are a politician as much as a business person. For them, managing foreigners and being able to deal with new regulatory environments is going to be a great challenge – which will take time.

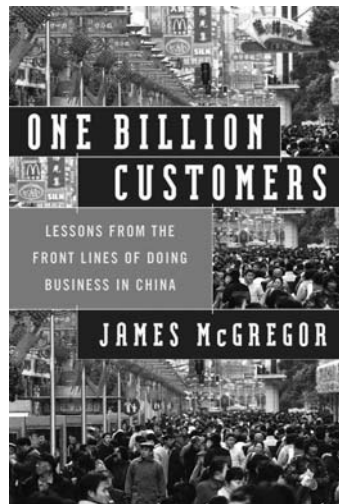
So far, the bulk of Chinese outbound investments has been in natural resources. Because China needs natural resources, they want to assure a continuing supply. The real test will come when they start buying more operating businesses in foreign countries – and this will inevitably happen because the Chinese are now placing a primary emphasis on encouraging their exports.

One way for them to do this is for Chinese companies to own U.S. companies that will buy Chinese products – not only consumer goods, but also business equipment. This means that U.S. law firms and the investment bankers who will be involved in both sides of these transactions should tool up for this coming wave of new business, and U.S. companies that are likely targets should get ready to receive offers that are hard to refuse.

Editor: Take a situation where a large Chinese company is negotiating a cross-border deal with a large American firm that is dealing with China for the first time. What should the American company take into consideration in order to have a good outcome from that?

McGregor: The American company should use a law firm that has China offices and knows what they are doing here. American law firms have extremely experienced people in large offices in China. Use consultants that can help you as middlemen, but make sure they are people who really know what they are doing. And, be sure to consult the Internet for information sources that will enable you to be up to date on the latest developments affecting investment in China. At the end of the day, no matter what the contract says, it is the relationship built during the negotiations that will save the business when times get hard.

Editor: Do you feel that U.S. companies are currently underrepresented in China?



McGregor: God no, they are all here. The *Fortune* 1000, are here in force. AmCham Shanghai has 3500 members and AmCham Beijing has 2500 and there are a dozen AmChams in cities around the country. What's new in China is that more and more American small and medium enterprises are coming in, but the big guys are already here.

Editor: What are the best cities in China for U.S. companies?

McGregor: That is tough because a lot of times from a business standpoint it is better to go to the secondary cities because they will appreciate you more. Beijing and Shanghai have so much foreign investment that they may not be as happy to see you, but if you go to a secondary city where your business matters more, there are cost advantages, and your business will be treated well.

For living conditions, Beijing and Shanghai are very good – lots of good housing, excellent international schools, and even good golf courses. On the other hand, life for expatriate U.S. families living in secondary cities can be more difficult. Among the secondary cities, the best cities for U.S. families are probably Tianjin, Hangzhou and Dalian – and they are rapidly getting better. For example, Intel has just moved a huge plant into Dalian and inevitably around that will form an international school and community of U.S. families. It happened in Tianjin when Motorola set up a big operation there.

Editor: Given the decline of the dollar, has setting up a business in China become more expensive?

McGregor: The decline in the dollar increases the cost. However, even without that, everything in China has become more costly as the economy prospers. In earlier days, labor didn't have a lot of protections here. However, under the administration of Hu Jintao and Wen Jiabao, a new labor law was adopted that strongly favored employees and is reflected in rising wages and other business costs. For example, it limits the ability of management to dis-

charge workers. This increases retirement and health insurance costs.

Editor: Are there any problems about bringing in necessary U.S. staff?

McGregor: The government is good about granting visas to management people coming in. Many of the U.S. expats are Chinese who went to America and attended university there. After working in the U.S. for a number of years, they are now returning to China – in many cases to head an American company's Chinese operations. But, for U.S. companies there are huge costs involved in using U.S. expats because the tax rates here are very high, so companies have to bear the cost of tax equalization. The special schools for expat children cost about \$30,000 a year. Home leave travel tickets and housing in the communities favored by expat families are high – so it's plus, plus, plus. You end up spending about a half million dollars a year on an expatriate executive.

Editor: Are there restrictions on entering into certain businesses? In other words, are foreigners not permitted to do certain things in China in terms of business activities?

McGregor: The Ministry of Commerce (MOFCOM) has a list of favored, forbidden, encouraged and not encouraged investment areas. Generally, if you want to build a car plant here you have to have a 50/50 joint venture with a Chinese company. If you want to be in banking, huge restrictions apply. If you want to be in publishing or the media, forget it. It goes on and on. Generally it is quite open, but there are what they consider to be strategic and politically sensitive industries which are quite restricted.

Editor: Is corruption still a problem in China?

McGregor: China is not Africa. It is not a place where every official, at every level, is trying to get a bribe whether you're buying an airline ticket or trying to install a phone line. It's a very regulated, organized, civilized country in that way. However, if you're selling power equipment to government entities or telecom equipment or whatever, yes, it is rife with corruption. Nevertheless, the Foreign Corrupt Practices Act may be a godsend. Officials are aware that U.S. companies can't bribe, and so they may not ask for one. You may lose out on some business, but I'll tell you, once you start bribing you never can stop.

Editor: What is the effect in China of the emphasis being put on corporate social responsibility by U.S. companies?

McGregor: The big American companies have been here for a long time and they're very plugged in. Their corporate social responsibility programs are huge; everybody's doing CSR now. Companies are building schools all over China, they're fixing up hospitals, they've got education programs for poor kids and migrant workers, and whenever disaster strikes they are quick to help. The Europeans and Japanese are very good at that too.

In the case of U.S. companies those programs have undoubtedly had an effect. America and Americans are quite well regarded in China. It seems like half the urban elite have kids in U.S. universities. On the other hand there's a very strong nationalism here that has been ginned up by bloggers on the Internet.

Editor: What's the bottom line in terms of the future of U.S. business in China?

McGregor: America has its own nationalistic spasms, but we're basically regulated by law and quite fair to foreign companies. The jury's still out on China. Foreign products are quite well regarded here because of quality, and foreign companies are well liked, especially by Chinese employees, because they're very well managed – they are viewed, in many cases, as meritocracies where people can move up. This is a place where nobody had anything and everybody was for reform and openness. Today, there are many big Chinese companies that have made a lot of money in the local market and they may not welcome international standards or international companies. We are going to have to see whether China goes more towards continued openness or whether it goes towards crony capitalism and protectionism. It's kind of bouncing back and forth a bit right now. It's a very interesting time.

Editor: What can U.S. companies do to assure their future in China?

McGregor: When they come here, they have to be humble and respectful of China and need to get a lot of people as allies. They need to put money into government relations and public relations so that people will know that they are good corporate citizens. That's hard for companies because those are cost centers, but they need to be out there telling their stories. They need to be telling the government and the people who they are and what they do and why what they do is good for China.

Editor: How would you sum up your advice?

McGregor: If you are an American company looking to enter or expand China, think it through and do it for good reason and do it in a patient and careful way.

COMING IN FEBRUARY:

Focus on Private Equity

Please email the interviewee at mcmgregor.jl@gmail.com with questions about this interview.