

IN CHINA, IT'S NOT JUST ABOUT THE ECONOMY. WILL CANADA GET IT?

by [Yuen Pau Woo](#)

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A shift by Chinese authorities from emphasizing exports to boosting domestic demand will create unprecedented opportunities for Canadians, from academics to exporters of more than just potash. It's an opportunity to make China and the rest of Asia loom as large in our imagination as the United States. Or, is the opportunity an imperative?

This article is adapted from a speech given by Yuen Pau Woo, President and CEO of the Asia Pacific Foundation of Canada, on November 25, 2009, at the Toronto campus of the Richard Ivey School of Business. The occasion was the inaugural Donald L. Triggs Lecture in International Business.

Many observers see Canada's hosting of the G8/G20 meeting next June in Toronto as that country's rightful turn in the limelight. However, I would argue that it is rather symbolic of Canada's new position not on the stage, but rather above it, in the balcony, looking down on the floodlights shining on a new set of global players, as represented by the G20. In something of a role reversal, Canada is part of the established order that is now making way for the emerging powers. To imagine otherwise would be like the line in the Beatles song that goes, "I don't why you say 'Good bye'; I say 'Hello'".

At the centre of the shift in global power is of course China, India, and in a broader sense the whole of Asia. Both China and India are part of the G20, as are Indonesia, Korea, and Australia – all part of a growing Asian community that has become stronger through the economic crisis, even as NAFTA and the EU have, in my view, become less united because of internal stresses brought about by the crisis. North American integration has stalled — indeed it has gone backwards because of heightened concerns in the U.S. about border issues to the north and the south. The EU project, for its part, appears to have stalled and is at its lowest ebb since the Lisbon Treaty, with Euroskeptics in the ascendency in many EU member countries. The recent election of two relative unknown figures as the EU President and the High Representative for Foreign Policy of the EU underscores the declining fortunes of European integration.

When I spoke to the Canadian Club here in Toronto a few years ago, my main message was about the need for Canada to fully appreciate the rise of Asia and to prepare accordingly. Six months ago, when I was invited to make the speech I am delivering now, I figured that I would have to give much the same speech, on the grounds that the only way to get a message across is to repeat it, ad nauseum.

Indeed, just six months ago, we were seeing what I would call silly articles in the mainstream Canadian media about how the global economic crisis might signal the imminent demise of the Chinese government, because of the widespread unemployment that would lead to social unrest and, eventually, the overthrow of the Communist Party. Can you believe that just over a year ago, The Globe and Mail concluded its reporting on the Beijing Olympics with the banner headline "The Potemkin Olympics"? Notwithstanding the recent talk about a global power shift, there is a deep vein of disbelief in Canada and the United States that there could be genuine economic and material progress in China under an authoritarian regime, and that there might be popular support for such a regime.

Don't get me wrong. I am not a fan of authoritarian governments. Nor should we ever forget the horrendous sacrifice of Chinese lives through one failed experiment after another from 1949 'til the opening of the Chinese economy in 1978, as well as the suppression of dissent that continues to this day. The more I think about China, the more I am inclined to a dialectical view of its recent development. Like many others, I am continually puzzled by the many contradictions in the Chinese economy, polity, and society – and increasingly persuaded of the durability of these contradictions.

Well, a lot has changed in the last year. There has been a transformation in the Canadian media's representations of China. A recent headline in The Globe and Mail on the Obama visit to Beijing read "A G2 of Nations – on China's Terms." This too is hyperbole, but it's impossible to notice how dramatically the message has changed.

I am not going to go as far as to say that when the Globe gets it, Canadians get it. But, I do think there is now widespread awareness of the rise of China in the world economy, and that this power shift is about more than just economics.

China's new economic focus: Boosting domestic demand

It is ironic that it has taken an economic crisis to awaken Canadians – and Americans — to the importance of China. The Chinese economy was last in and first out of the recession, and it is Chinese demand that has kept the world economy from plunging into a deeper slump. Indeed, Chinese growth is the single most important reason that Australia has been able to avoid a recession altogether. In fact, Canberra recently raised interest rates because of inflation fears. Likewise, Canada has weathered the recession relatively well, in part, because of Chinese demand for commodities. I am, however, sensitive to the fact that the benefits have favoured the resource-rich western provinces, and that the resulting upward pressure on the Canadian dollar has had the opposite effect on exporters of manufactured goods, many of whom are located in Ontario.

While I am happy that the level of awareness of China's importance for Canada has gone up significantly during the economic crisis, I am not so thrilled about the circumstances of our enlightenment. The commodity boom that is once again fueling economic growth in western Canada is a re-run of an old movie that desperately needs a remake. The newfound enthusiasm of oil sands and natural gas producers to sell their products to Asia is welcome,

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especially as it will likely mean the investment of billions of dollars in pipelines, terminals, and gas liquefaction facilities that run west rather than south. However, these projects are part of the old extractive industries and will not do much to prepare Canadian business for a very different set of opportunities that China will offer in the years ahead – not just for western Canada, but perhaps even more so for Ontario and Quebec.

The most important takeaway from the crisis, after all, is not that China is still growing at the rate of 8-9 percent this year. It is that China – and much of Asia — has embarked on a shift in its economic development model, a shift from exports to a model that is driven more by domestic demand. Don't be misled by the headlines about the U.S. and China squabbling over the value of the Renminbi and the refusal of Beijing to allow a floating exchange rate. The Chinese currency will appreciate in the years ahead and that will shift spending towards imports. But far more important are the policies to increase domestic demand in China, both directly, through expenditures on infrastructure, education, health care, and social safety nets, as well as indirectly, by reducing the amount of precautionary savings needed by Chinese households for health-care.

The need to boost domestic demand in China is usually presented in terms of the so-called “global rebalancing” debate – namely how to maintain global growth when the United States is reducing consumption, and hence imports from the rest of the world. It is an arithmetic truism that rebalancing will require China (and other surplus countries) to increase domestic spending in order for the U.S. to reduce debt and increase savings. China, of course, has an interest in contributing to the rebalancing of the world economy as a “responsible stakeholder”, however reluctantly. But it has an even more powerful interest to investing in domestic priorities that have been neglected for many years. These include the provision of public health care, rural infrastructure, and social safety nets for the millions of workers who have been made redundant by the collapse in export demand due to the crisis.

We all understand that successful international policy boils down to successful domestic policy. This is true even for China, which is a one-party state that is top-down in its instincts and which does not tolerate dissent. When President Hu Jintao says that China is not a superpower and cannot yet shoulder a wide range of global responsibilities, he is not being modest. China faces major challenges of poverty and income inequality, as well as inequality of access to basic services such as quality health care and education. These problems breed discontent, which undermine the legitimacy of the government, which is, when all is said and done, a socialist government founded on the promise of social justice. There is a huge incentive for the Chinese Communist Party to provide better access to health care, housing, and education, to improve the welfare of rural Chinese, and to redress the extreme inequalities that are emerging in Chinese society. I am not predicting that this will happen quickly or automatically, but I am saying that the Chinese government will be motivated to work in this direction not because of external pressure but because of domestic imperatives.

Don't take my word for it. Let me share with you the results of a poll that I am in charge of and which was launched in Singapore at the APEC Leaders' meeting two weeks ago. Every year, the Pacific Economic Cooperation Council sends a questionnaire to about 400 opinion leaders from around the Asia Pacific region. When we put forward the proposition that “Slower growth in the western industrialized economies will encourage a shift to domestic demand growth in Asian economies”, we found that 77 percent of respondents agreed. Another 53 percent of opinion leaders concurred with the statement that “China is doing enough to encourage domestic demand.” And when we suggested that “the global crisis will accelerate the pace of Asian economic integration and cooperation,” we again found a strong majority in support of the statement, 68 percent of respondents.

Increased demand equals increased opportunities

It's very reasonable to ask what a focus on domestic demand in China will mean for Canadian companies. Generally, increased domestic spending power will translate into a larger set of spending categories in a wider range of markets across China. The opportunities will not only be limited to Beijing and the coastal cities, but will also occur in so-called second “tier cities” and well into the inland regions. In particular, there will be rapid growth in the demand for high-end services. In my view, the most interesting Canadian success stories in China today are not to be found in the record volumes of potash or pulp exports to the mainland, but in the large and small firms across Canada providing services in the areas of education, advertising, retail, engineering, logistics, food processing, and in many other non-traditional sectors. What is characteristic of these companies is that while they are very much part of Canada's export community, they provide services by establishing a commercial presence in China and by thus dealing with all the political, cultural and social challenges that come with serving the domestic Chinese market. In any case, they operate on a business model that is very different than the one used by the more traditional exporters of commodities and manufactured goods.

Something new: High-end Chinese products and services

The rebalancing of the Chinese economy will take many years, which means Chinese exports of manufactured goods will continue to flood the world for the foreseeable future. Canada does not worry too much about the threat from Chinese manufactured imports because our firms generally do not compete in industries that are characterized by low-wage, cost production. But one of the implications of “global rebalancing” will be a change in the terms of trade that encourage Chinese firms to go up market. Be careful what you wish for: The same forces that will boost domestic demand in China and create new opportunities for Canadian exporters will also force Chinese firms to innovate and produce higher-end products and services to compete on a global scale.

To cite some diverse and perhaps idiosyncratic examples: The Chinese telecom network giant, Huawei, has won major contracts around the world, not just in developing countries that may be beholden to Chinese aid and investment, but in advanced markets such as the United States, Singapore, Norway, Sweden, and the United Kingdom. In the field of international education, China is now the 6th-largest destination for foreign students, ahead of Canada (But how many Canadians choose to study at Chinese institutions of higher learning?). And even when it comes to wine – a subject in which I have no expertise – I can tell you that Chateau Lafite (of Rothschild family fame), which has been in northern China since the late 90s, is set to produce its first bottle in a few years. Can it be that China might emerge as an exporter of world-class wines?

Which brings me to my closing point – whether Canada is ready for a post-crisis world in which Asia will play a more central role, led by China and India? As you all know, our prime minister was in Singapore last week for the APEC meeting, followed by a visit to India. On the margins of the Singapore meeting, Mr. Harper said the following: “While Canada's economy was built through trans-Atlantic trade, our future prosperity will increasingly depend on our ties to the Pacific. This region is home to some of the most dynamic and fastest growing economies.”

I am encouraged by this statement. If nothing else, it reminds Canadians that we are an Asia Pacific country, and that we are connected, in his words, to “the most dynamic and fastest growing economies.” But declarations are not enough, and it struck me that there was a sharp contrast between the PM's bold statement and the lightweight outcomes of his Singapore and India visits. Whatever the results of his Asia travels, it is important to remember that Canada's long-term success in Asia depends less on what the PM does “over there” than on what he does right here. Having articulated the importance of Asia for Canada, he should now work on an Asia policy for the whole of government. The rise of Asia is not just a “foreign policy” issue or a “trade policy” issue, even though it is critical that we get right those aspects of our international policy. Asia policy is also about the regulation of foreign investment, including investment from Chinese and other Asian state-owned enterprises; it is about immigration and citizenship policies that take into account the extensive two-way flows of talent across the Pacific; it is about building an Asia expertise in Canada so that we can participate

fully in the debates that are shaping the new Asia; it is making sure that Canadians have the appropriate language and cultural skills to connect with Asia. A decade or two ago, having a set of comprehensive, long-term, and strategic policies on Asia would have been seen as forward-looking. Today, not having such policies would be almost retrograde. Previous prime ministers have, to varying degrees, articulated the importance of Asia for Canada, but for each of them, the potential of Asia was mostly that — potential. They did not face the imperative of a rapidly rising Asia — in the face of a global economic downturn — that Prime Minister Harper faces today. He is not the first PM to talk about how Canada's future depends on its relations across the Pacific, but he could be the first PM to bring about the change that is needed across the country to make Canada truly part of the Asia Pacific region.

Asia penetrates the Canadian imagination

For too long, Canada's connection to the Asia Pacific region has rested on two comfortable notions: a) the fact that the west coast of Canada borders the Pacific Ocean, and b) that there is a significant population of Canadians — notably in Toronto and Vancouver — who are originally from Asia. These are two important facts that establish a level of credibility for Canada in Asia, but they are not sufficient in positioning Canada as a serious and committed player in the Asia Pacific region. It is not enough for British Columbia to say that it is Canada's Pacific Gateway (which it is); Canada has to say that it is part of the Asia Pacific region, and Canadians across the country must learn to incorporate Asia into their mental maps. In the same way, our human ties across the Pacific cannot be based chiefly on the relationships that immigrants have with their native countries. Canadian across the country (especially young Canadians) should be given the opportunity to consider Asia as part of their educational and career development, in much the same way that many Canadians see New York, London, and Paris as natural destinations for their personal and professional development. At the Asia Pacific Foundation of Canada, we are trying to get young Canadians to think about how Asia affects their lives. On the occasion of our 25th anniversary, we have launched a contest for Canadians between the ages of 18 and 35 to submit videos on what they think are the most important issues in Canada-Asia relations. We'll pick the top 25 ideas and feature them on YouTube and on our website. Check it out — www.25@25.ca

Now, I realize that I am making this speech in Toronto, some 4500km from the Pacific Ocean, and that it may be a tad difficult for most Canadians in this part of the country to feel connected to the Pacific, let alone to the land mass across the water that is Asia. So let me close by making a simple proposition. I have always been struck by the importance of the Great Lakes in the Canadian imagination and how these massive bodies of water, in modern times, are seen as connecting Canada to our great trading partner to the south rather than separating us from the United States. In the same way, the completion of the St. Lawrence Seaway 50 years ago connected the Great Lakes to the Atlantic Ocean, and beyond to Europe. I am not about to say, as Premier Campbell is fond of saying, that the Asia Pacific Gateway in British Columbia is Canada's St. Lawrence Seaway of the 21st Century. That would be a BC-centric way of comparing the two projects. Rather, what I would say to you is that the Pacific Ocean is nothing more than Canada's Great Lake to the West. Canada conquered the Great Lakes to the East many years ago, ushering in a golden period of business, diplomatic, and people linkages with the U.S. and Europe. We can do the same again with the Great Lake to the West.

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