ONE PAGER

FTI JOURNAL
CRITICAL THINKING AT THE CRITICAL TIME™

July 2015

The Middle Kingdom at the Crossroads

By **Rod Sutton**, *Chairman, Asia Pacific*

China looms large in the West's imagination. The Middle Kingdom spent much of mankind's history as the world's most prosperous nation. Today, in terms of the sheer size of its economy, it is back on top.

But China is not yet the full partner the West hoped it would become when, at the turn of the century, it called for a shakeup of its state-owned enterprises ("SOE"), an end to business monopolies and the encouragement of foreign investment.

Nor has it become the rogue powerhouse some in the West feared it would become. Today, China remains focused on shoring up a somewhat faltering economy (gross domestic product growth, which reached 10.4 percent in 2010 has fallen since to 7.4 percent in 2014), taming an overheated property bubble and rebalancing its economy from low-end manufacturing to consumer goods.

China is at a crossroads, and the West should do more than wait to see which path it takes.

As at any crossroads, the signs point several ways.

Those SOEs, indeed, are being reformed. President Xi Jinping is rooting out corruption. The Shanghai and Shenzhen free trade zones and the Hong Kong-Shanghai (and soon Shenzhen) Stock Connect schemes will allow foreign and domestic investors to "dip their toes."

China also continues to fund projects in Vietnam, the Philippines and Indonesia, and the Asia Infrastructure Investment Bank, which China is organizing, is being embraced across the region as an alternative to the U.S.-centric World Bank and Asian Development Bank. Given the huge strides China has made in raising its standard of living, improving its infrastructure and developing new technologies, it's no wonder emerging economies look to China as a model.

But foreign investors continue to be wary despite the enormous size of China's market and the love of Chinese consumers for foreign brands. Well-founded doubts persist about how safe those investments may be when the foundational principles of economic freedom, at best, are embryonic. And the jury is still out on Xi Jinping's reforms. Are they intended to establish market transparency and fairness? Or are they motivated by a desire to consolidate power?

These uncertainties are shared by China's emerging middle class. China needs its people to invest in and spend more on the domestic economy, but, as is the case with foreign investors, people worry about the safety of their money. They also are concerned about their retirement and health. Social Security helped U.S. consumers feel secure enough to spend in middle life; China has to provide its people with retirement and healthcare benefits in order to replicate that demand.

Right now, however, China remains an enormous driver of world growth. If China does not succeed, the entire world will suffer.

What should the West do? Lecturing China won't work. It must develop its own way. But the West should seize every opportunity to engage with the Middle Kingdom. That's the surest way to promote the emergence of the liberties and freedoms upon which sustained economic success depends. And then, perhaps, the changes that need and want to happen will. ■

Rod Sutton is Chairman, Asia Pacific Region of FTI Consulting and he is based in Hong Kong and Singapore. rod.sutton@fticonsulting.com

The views expressed in this article are those of the author and not necessarily those of FTI Consulting, Inc., or its other professionals.

FTI CONSULTING