

CHINA'S GREATEST CHALLENGE: DOES A MARKET ECONOMY MEAN PROFITS AT ANY COST?

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ABSTRACT

China gained the tag "Economic Miracle" as it transitions from Mao's closed-door ideologies, via a centrally planned economic system to today's market economy. Although amazing, this transformation has come at a cost and the People's Republic of China ('PRC') face many new challenges. Furthermore, this economic success now means the PRC is now perfectly positioned to recognise and own past errors and set new World standards in sustainability.

This short essay addresses several key issues by asking; does a market economy mean profits at any cost? To explore this question, John Elkington's Triple Bottom Line model is utilised to assess some of China's new challenges and examine their balanced scorecard. As a model, Triple Bottom Line worthy of consideration by all emerging nations. Particularly, a nation like China, who are in the process of re-establishing the rule of law, education, public utilities, the judiciary and food security.

I INTRODUCTION

China and Chinese culture predates Christ. Early recordings such as the Bamboo Annals date the Xia Dynasty (China's first Dynasty) prior to 2000 BC. Since then, China has survived different leadership, varied leadership styles and policies, and enjoyed unprecedented successes.

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Many of these successes in the arts, technical design, exploration and foreign trade are attributed to the effective leadership and sustainable governance of the Ming Dynasty (1368 - 1644). Today, China has advanced through the isolation and turbulence of Mao's closed-door ideologies via a well-executed and centrally planned economic system to a more market oriented economy. China's outstanding success in economic development has gained it the label of the 'economic miracle'! The other side of the economic success is the cost to the environment and increasing gap between the wealthy and poor.

This essay will examine China's massive economic successes, social reforms, and environmental protection policies by considering the headline question:

Does a market economy mean profits at any cost?

To evaluate this proposition and draw conclusions this paper will overlay China's economic performance on the Triple Bottom Line ('TBL') model. The TBL is a refinement of the United Nations 1983 Brundtland Commission recommendations and later refinement by Elkington.¹ Simply, the TBL measures non-economic performance factors, the people (social responsibility/social outcomes), the plant (the environment in which we operate), the economic measure profit and establishes a 'costs – benefit' ratio that is not measured solely in Dollars, Euros, Kroners, Yen, Francs or Renminbi. The TBL removes the paramount focus of maximising returns to shareholders (a western doctrine) at all costs and places a value for all stakeholders including suppliers, clients, owners,

¹ Brian Murphy and Rongmei Wang, 'An evaluation of stakeholder relationship marketing in China' (2006) 18 *Asia Pacific Journal of Marketing and Logistics* 1: citing John Elkington, *Cannibals with Forks: the Triple Bottom Line of 21st Century Business* (Capstone, 1998). John Elkington is considered by many to be the father of sustainable development and corporate responsibility.

employees, governments and the communities in which they operate. It is not a socialist ownership by the state model, or a model 'to rob the organisation of its profits' but promotes the desired outcome of sustainable profits, improved lifestyles and better environments (within and outside the organisation). These desirable outcomes should fit naturally with Chinese 'can do' culture, the 'Confucian teaching ...to achieve social order and harmony'² and the internal motivation of the people to achieve.

The TBL model has gained popular acceptance among many of the Fortune 500 companies in the USA and widespread acceptance in India. The following will examine each element (the three 'Ps') of the TBL (II) Profits, (III) People, and (IV) Planet with available information on China.

II PART ONE: PROFITS

The TBL assumes that profits can be in many forms and not all profits need necessarily be economic profits. Michael Baye describes economic profits as the 'difference between total revenue and total opportunity cost' and further notes, 'it is common for most firms to maximize profits as a primary goal.'³ Some argue that profits are based on self-interest and greed. Others understand that profits are required for a business to exist. Regardless of your perspective, without profits businesses are unable to expand, unable to meet their financial commitments and ultimately unable to exist. So, is this good or bad for the communities in which they operate? The TBL model suggests that profits are good. When profits are high, organisations can reinvest in improving plant and equipment (their

² Hong Xiao, 'Values Priority and Human Rights Policy: A Comparison between China and Western Nations' (2005) *Journal of Human Values* 11, 89.

³ Michael Baye, *Managerial Economics and Business Strategy* (McGraw-Hill Irwin, 2006) 5-8.

operating environment) and assisting the people (the staff and broader community, the external environment) while providing a fair return on investment to the shareholders. A win/win/win situation. As the TBL and Michael Baye are from free trade backgrounds, can these theories and practices add value to China's evolution?

China has moved from communism, to the planned economy, to a market economy⁴. This transition has not been as easy to manage and will face many fresh challenges in the future. As the Chinese Government divests many State Owned Enterprises ('SOE') to provincial or private ownership, many aspects of the businesses functions will require re-evaluation. Many of the older communist SOE have old plant and equipment, are set up for mass production with little variety, questionable quality, and in most situations only one customer (the State). These businesses have been sustainable to date: due in part, to the low cost and abundance of labour. As China's economy evolves and the middle class emerges, these labour rates will rise while the plant and equipment will continue to age. This is evidenced by large SOEs like Anshan Iron and Steel Complex⁵ who are having difficulties adapting from high volume government backed orders and low cost mass production, to a focused differentiation strategy⁶ more suited to a market economy. Likewise, the Government themselves have experienced problems in exercising managerial economics⁷ as

⁴ Wenlie Yu, 'China's Socialist Market Economy' (2009) 12 *Nature, Society, and Thought*, 447.

⁵ Chung Kui Jin Pao, 'Steel giant departs from the planned economy' (1990) *China Daily North American ed*, 3.

⁶ Arthur A Thompson Jr., A J Strickland III and John E Gamble, *Crafting & Executing Strategy The Quest for Competitive Advantage* (McGraw-Hill Irwin, 5th ed, 2005) 153.

⁷ Baye, above n 3, 5.

demonstrated by the cabbage crisis where they simply got the numbers wrong.⁸

Plainly, businesses must make a profit. Likewise, Governments ought to stay in surplus (a Governments equivalent to profit) if the economy is to continue to grow. The balancing act is in the reinvesting of the profits. Having large amounts of money in Government or a few people's hands is clearly not helpful if the workers are dying from respiratory decease, drinking polluted water and generally have a low quality of life. Likewise, the business/governments future is bleak if profits are unsustainable or if demand for goods suddenly drops.

The TBL offers concepts worthy of consideration.

III PART TWO: PEOPLE

In economic terms people are a resource. People can provide knowhow (intellectual capital), or labour (human capital).⁹ The CIA World Fact Book estimates China's population at 1,336,718,015 at the July 2011 with 73.6% of this population being between 15 - 64 years of age (i.e. working age) and 47% of the population living urbanely.¹⁰ This means that China is rich with human capital that provides a significant competitive advantage in labour intensive industries. However, the new challenge for the PRC is to keep this human capital working and working on

⁸ Adi Lgnatius, 'Wanted: an Enterprising Person With a Whole Lot of Corned Beef' (1989) *The Wall Street Journal* 1.

⁹ Baye, above n 3, 210; Phillippe Lasserre and Hellmut Schutte, *Strategies for Asia Pacific Meeting New Challenges* (Palgrave Macmillan, 3rd ed, 2006) 258-63.

¹⁰ Central Intelligence Agency, 'The World Factbook', <<https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html>>.

meaningful tasks in fair and proper conditions with fair and proper reward.¹¹

As China returns to its proper position as a global citizen, they will have to move past the 'Post-Mao' period where the new leaders tended to blame the 'gang of four' for all the violations of human rights and said that they were on the path of reform.¹² Likewise, Chinese officials may have to soften their claim that in China economic prosperity is the major concern of the people and an emphasis on social order versus individual freedom is good for economic growth.¹³ Mao's China will haunt China's leaders for some time yet. The one child policy for example means that China now has an aging population. Likewise, as the emerging middle class gain more and more information, exposure and understanding of foreign lifestyles, working conditions and practices through television and the internet their attitude to collectivism and subservience to government may change.

Until recently, foreign leaders have avoided public reference to China's human rights practices. It was widely accepted within the bureaucracy that the People's Republic of China ('PRC') was not an appropriate target of human rights initiatives¹⁴ and politically viewed as unwarranted intervention in China's internal affairs.¹⁵ This proposition is also changing. Kurt Lewin the popular German-American psychologist is widely considered the father of social psychology and organisational

¹¹ R Schuler, *Human Resource Management* (John Wiley and Sons, 1995) 4.

¹² Yeshi Choedon, 'The Human Rights Factor in US-China Relations: The Carter Period' (2000) *China Report* 36, 215.

¹³ Xiao, above n 2, 88.

¹⁴ US Congressional Research Service report published in 1979 as cited in Choedon, above n 12, 201.

¹⁵ Choedon, above n 12, 216.

development defined his change model named the Force Field Analysis.¹⁶ This model suggests that change begins when the driving force of the desired change exceed the restraining forces acting against the change. Since China's open-door policy commenced, China has sought to recommence its position as a global citizen and thereby the driving forces for social reform and adoption of human rights has increased and will continue to increase at an expedient rate. Tiananmen Square, the 1997 handing back of Hong Kong and the Beijing Olympic games has focused the wWorld press and media more critically than ever before. Likewise, China has joined the World Trade Organisation (WTO), the International Labour Organisation (ILO) and the United Nations (UN). On the other side, the main restraining forces are lack of technical knowhow and the operant conditioning toward communist party conformity. When these external driving forces merge with China's emerging middle class and the general broader population are exposed to outside sources will ultimately overpower the restraining forces and change will follow out of necessity, sustainability and external pressure. Lewin's change model may well indicate that for China to survive major reforms it may well have to change to a more TBL aligned practices, whether intentionally or inevitably.

IV PART THREE: PLANET

In 2004, 16 out of 20 of Worlds most polluted cities were in China and of the 412 sites tested on China's seven main rivers over 58 per cent were too dirty for human consumption.¹⁷ Birkin et al further claims; one third of China suffers sever soil erosion, an estimated 75 per cent of waste

¹⁶ Steven McShane and Tony Travaglione, *Organisational Behaviour on the Pacific Rim* (McGraw-Hill Irwin, 2005) 566-74.

¹⁷ F Birkin et al, 'New Sustainable Business Models in China' (2009) 18 *Business Strategy and the Environment* 64.

water is discharged untreated, 60 per cent of the drinking water does not meet World Health Organisation's minimum acceptable standard and that one in four people die of respiratory diseases.¹⁸ The CIA World Factbook states: Soil erosion and the steady fall of the water table, especially in the north, loss of arable land because of soil erosion and economic development. Likewise, China's air pollution problem in Beijing was broadcast worldwide in the lead up and during the 2008 Olympic Games. These problems are the most serious challenges for China. Like Fukushima Japan, and the omission of carbon in other countries, the problems are not contained. Our planet is everyone's and everyone's responsibility.

Worldwide, private companies are held to account for their environmental disasters,¹⁹ in my view it is only time until governments are held accountable and responsible for their emissions. Whether this responsibility is ever levied upon governments or not, China is now in the perfect position to set new Wworld standards in environment protection. China's massive economic growth and building of new infrastructure is the ideal opportunity to build new super environmentally friendly cities, factories, public places, private and public transport and for the introduction of new low emission technology in delivering services such as power and water. China has an added advantage of autonomous authority and influence²⁰ that could implement new standards quickly and easily by behaviour modification.²¹ Chinese collectivism is more likely to

¹⁸ Ibid, 67.

¹⁹ Stathis Palassis, 'Reconciling the international and United States approaches to civil liability for oil pollution damage' (2007) 24 *Environmental and Planning Law Journal*, 2.

²⁰ Birkin et al, above n 17, 67.

²¹ McShane and Travaglione, above n 16, 45.

emphasize the power and responsibility of the state²² and the state has the available money to make this environmental revolution reality. If the PRC follow through with their proposed *Jeuqi* reforms²³ and make a genuine and serious approach to pollution control and sustainability, China will leave their old image behind and become the new World leader in environmental protection and sustainability. This type of development should meld the Taoism, Daoism and Confusion values that reside within the broader community.

China can learn with the benefit of hindsight from the Ethiopian experience of soil degradation, the New Zealand experience in decimating their Orange Ruffly fish stocks to the point of extinction and the Australian experience of soil salinity from clearing too much broad-acre farmland. Similarly, positives ought to be extracted from processes such as Western Australia's well-managed fisheries.

Businesses, governments and communities cannot exist in a vacuum. The inputs of business and societies come from our environment; life and our environment are interdependent.

V CONCLUSION

China is home to 1.3 billion people and the population is aging. The CCP as the governing body of China has embarked upon a course to global citizenship by embracing new ideas and technologies and making considerable progress on social and economic reforms. However, there is still a long way to go if the 'economic miracle' is going to continue to grow and prosper.

²² Xiao, above n 2, 87.

²³ Birkin et al, above n 17, 67.

For China to continue to grow and prosper they must embrace a holistic approach to business, governance and the people.

The wWorld's focus is currently on China, and China is now in the perfect position to recognise and own past errors and set new World standards in sustainability. The renewing of infrastructure is providing the opportunity to build new environmentally sustainable businesses, cities and utilities. The renewing, and in many cases creation of new legislation allows freer adoption of contemporary World standards such as the WTO, ILO and UN's charters, conventions and treaties. Further, China's enormous economic success means their government has the cash reserves necessary to make the preceding ideas possible. The Triple Bottom Line as a model is worthy of consideration by all emerging nations, particularly, a nation like China, who has so many people to care for.

The three 'Ps'

PROFITS

Profits drive growth; provide livelihoods and communal infrastructure. They are necessary for sustainability and not evil greed and self-interest but a necessary element of sustainability.

PEOPLE

Our people require clean food and water. They require sunshine, clean air, relaxation, safe working conditions with

fair reward and have a right to enjoyment
of life.

PLANET

Our planet is a finite resource and requires our nurturing.

Profits must serve the People and the Planet.