

“China: The Re-Emergence Of The Middle Kingdom”

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Mr Chairman, My Lord Mayor, My Lord, Sheriff, ladies and gentlemen, good morning.

It's a great pleasure to be invited to speak to you today on a topic that conjures up a variety of viewpoints: the re-emergence of China as a major world power.

I use the word re-emergence advisedly. For most of recorded history China was, after all, the world's leading civilisation. It is ironic that the country with perhaps the greatest history of all, and millennia of supremacy in the sophistication of its society, should today find itself branded a developing economy by the West, where the majority of people are completely unaware of China's illustrious past.

In the West there are some major challenges to law and order, and perhaps our governments could do worse than look to ancient China for inspiration.

I think, for example, of the Qing dynasty's approach to policing, *baojia*. This was a mutual-responsibility system which grouped households in clusters of 10 sets of 100 households; if any one member of the group committed an offence, the whole group was liable for the transgression.

Similarly, during the recent constitutional debate over the House of Lords I couldn't help recalling the ingenious system of aristocracy the Manchus devised.

The titles of Manchu nobility reduced in rank as they passed down the generations, disappearing entirely after the ninth. So a title of the first rank would be inherited as a title of the second rank, and then drop to third and so on. Unless the holder of the title won promotion on their own merit, the noble family would, in nine generations, re-enter the ranks of the commoners. I suspect this was not an option our Government considered.

But this is not surprising when you consider the huge imbalance in the world regarding understanding China. China knows far more about the West than the West knows about China. And the West's perceptions are based largely on the last 50 years of Chinese history.

Why do we know so little of a country which makes up a fifth of the world's people?

The first reason is a lack of education, plain and simple. I wonder how much you were taught about China, its

history, its culture, its social mores at school. I represent a sample of one, but I left a fine school in Britain in 1959 without learning a single fact about China. Sadly, my son's experience at the same school 35 years later was exactly the same.

And the second reason is that, for people of my generation, China was a closed society for the first half of our lives, visible almost exclusively through the eyes of other people.

When I joined The Hongkong and Shanghai Banking Corporation in 1961 my father gave me my first book on China, *Chinese Cavalcade*, which was the start of my learning experience. It continued with Edgar Snow's *Red Star over China*; Snow fell madly in love with China and communism and thought this was the best thing that ever happened. And at the other end of the spectrum was William Hinton's *Fanshen*, an uncompromising account of what the communist revolution meant in a rural village.

As for personal experience, we used to drive out to the border in the 1960s in Hong Kong, to a place called the Robin's Nest, where we would look down at the barbed wire, the PLA patrol guards, and behind a very forbidding Communist state.

So perhaps it is not surprising that perceptions of China are very polarised, ranging from rose-tinted spectacles to tunnel vision.

The only certainty is that none of the commentators of the 1960s and 70s predicted the China of today.

So there is plenty of room between the polarised views of the media and authors for someone like myself, who has travelled more or less continuously to China since 1972, to form my own view. And that is what I plan to share with you this morning.

Of course, my 40 year career is a mere blip in the historical perspective of a country whose society and culture dates back 5,000 years.

History shaped modern China; geography shaped China's history. Bounded by mountains to the west and south, desert to the north and the sea to the east, China developed a unique civilisation.

**perceptions of
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China's dynasties came and went for 5,000 years, and understanding the continuum of China's history, and the amazing civilization it achieved, is fundamental to understanding China in the 21st century.

In a country which attaches huge importance to ancestors, and therefore history, there is a special bond between the people of China today and the immense and ancient culture of their ancestors, which has been described as an "exclusive five-thousand-year-old club" which "gives the Chinese a sense of separateness and self-esteem".

Today, China has a fifth of the world's people but represents just four per cent of the world's GDP. So people forget that for 90 per cent of recorded history, China was the world's largest economy and, probably, its most advanced civilisation.

The seed drill was used in China 3,500 years before the West got there; they produced steel 1,500 years before Europe, iron a thousand years and used it for pots and pans, not weapons. Stirrups were produced about 500 BC, 1,220 years before Europe, and paper was used around the time of Christ, a thousand years before Europe. There is even some debate as to whether football originated in the Middle Kingdom!

China had a civil service based on merit which existed 200 years BC, open to anyone who passed the competitive exams - a true meritocracy. This Mandarin system endured for 2,000 years - hence the Mandarins stalking the corridors of Whitehall. The Chinese reportedly have the dubious distinction of developing taxation.

The Han dynasty was contemporary with the Roman Empire and comparable in size and population. The growth of the Roman Empire was by acquisition, China's growth was organic. And from the Han Dynasty until the 1911 revolution, the political structure of government remained essentially intact.

Stability and sovereignty were the key issues for the emperors; changing dynasties produced bouts of armed struggle, but in the interim China produced perhaps the world's most sophisticated society.

In 1820, when the USA was an emerging economy of four million people, China still accounted for 30 per cent of world GDP.

By 1950 its share of world output had fallen to less than five per cent, and it is one of history's great mysteries why China did not have its own industrial revolution.

Perhaps it was due to a century of foreign incursion, anarchy, warlordism, civil war and conflict with Japan –

a turbulent, difficult and humiliating period in China's history.

It was this humiliation that led Mao to claim in 1949 that his new People's Republic of China would "reverse the reversal of history". It did not turn out quite as expected, and there is some irony in the fact that it was a western ideology - Communism - that was used by Mao to reunite China half a century ago.

Communism unified and eventually clothed and fed a billion people. But autarky could not raise the standards of living beyond this and take Chinese society to the next stage.

It was Deng Xiaoping who recognised this.

When I first went to China in 1972, the lives of millions of 'ordinary' people were totally dominated by the Communist party and a voucher system. A voucher told you where to go to work, where to live, where your children went to school. You used a voucher to collect food. There is no doubt that at that stage the Chinese people had surrendered their lives to the state.

Deng's genius and courage allowed China to break with Communism and replace it with "socialism with Chinese characteristics". It was Deng who said "It doesn't matter whether the cat is black or white, as long as it catches mice", and his sweeping reforms ushered in a period of unparalleled growth.

Deng's creation of export zones was a clever idea. He had to show that the new approach to the economy worked, but to do that simultaneously across a billion people would have been impossible. By creating export zones where foreigners could come in with concessionary tax rates, create jobs, he showed that the system could work.

In the last 20 years China has been journeying from a voucher economy to a monetised economy with prices set by the market; from an economy where 100 per cent of the means of production was in government hands and subject to five year plans, towards an economy that is increasingly driven by the demands of consumers.

It is an unprecedented journey because, among other reasons, of China's sheer scale, as home to a fifth of the world's people. Or to put it in perspective, more Chinese people share the surname Chan than there are people in Germany.

And of course, while Harvard and Oxbridge professors may have a view on how China should manage its transition, the truth is that nobody has ever done it before. And it is hard to argue with the success that China has achieved.

an exclusive five thousand year old club

Today, China is the world's sixth largest economy - or if you look at it on a purchasing power parity basis, the second largest, after the US. Goldman Sachs forecasts that China will overtake the US as the world's largest economy by 2040, a prediction that might well be too cautious. In my industry, we estimate that the book value of China's banking assets could exceed the US's any time between 2013 and 2033.

The timing does not matter, but we in the West do need to prepare ourselves, particularly our young people, for a powerful and exciting re-emergence of China on the world scene. The first of the ancient, historic powers to return to glory.

China's success has been achieved by a peaceful revolution on an unprecedented scale. There has been a massive migration of people from rural areas to cities. China's urban population has grown from 172 million in 1978 to 460 million today - about a third of China's people live in cities.

And people have moved from subsistence living to working in productive industries where they are beginning to have a disposable income. In 1980, 86 per cent of workers hadn't changed jobs in their working lives; between 1990 and 2000, 54 per cent moved to new jobs.

Urbanisation and industrialisation have almost halved the contribution of agriculture to the Chinese economy to under 15 per cent of GDP since 1978.

Not for nothing is China described as the 'workshop of the world': manufacturing and construction are now the core of China's economy accounting for over half of GDP.

China is the world's largest producer of steel, coal, cement, fertilizers. Last year, China became the world's third largest trader of manufactured goods. It produces two thirds of all photocopiers, microwave ovens, DVD players and shoes and over half of all digital cameras in the world.

The numbers are dazzling, but we should not forget that what they represent are the transformation in people's lives and opportunities. Let me give you an example.

I wonder if anyone in this room has heard of Datang, a Chinese city that is known locally as Sock City. Many of us here today are probably wearing socks made in Datang. After all, the city produces nine billion pairs of socks every year - one third of the world's entire annual production, and more than one pair for every man, woman and child on the planet. Its annual sock fair attracts 100,000 buyers from all over the world. And yet, 25 years ago Datang was a small rice-farming community of around 1,000 people.

China is not just a major new producer, it's also a major emerging consumer market. Last year, China was the second biggest contributor to growth in consumer spending in the world after the US, contributing nearly 10 per cent of the increase, although its economy only accounts for 3½ per cent of global consumption. The growth of a Chinese middle class is creating a large consumer market which Western companies are keen to serve. A decade ago, it was impossible to buy Western toothpaste in Shanghai; last year the city's first Ferrari showroom opened.

Of course there is a sharp split in income, lifestyle and sophistication between the regions in China, roughly comparable to the differences across the expanded EU. But the seeds of what should become the world's largest consumer market have been sown.

That China has managed these huge changes in its economy while maintaining stability and employment is a remarkable achievement.

The single minded determination of the politicians to "make it happen" differentiates China from other emerging countries. Indeed, the World Bank says China is without peers in its ability to translate policy research into effective action.

That is not to dismiss the challenges ahead. Governing a country of 1.3 billion people is an enormous task. Many Western leaders proffer advice, but none have done it. Establishing the rule of law, a social security system, dealing with corruption, these are all massive challenges.

As is tackling inequality. Poverty is still a major problem with, according to UN estimates, nearly half of China's people still living on under US\$2 a day. 800 million people contribute roughly 15 per cent of China's GNP. But China is addressing inequality at a much earlier stage in its evolution than most countries.

The disparity of wealth between China's coastal regions and the interior provinces is being attacked with the "Go West" policy.

For Westerners trying to work with China, we must also avoid falling into the danger of oversimplification. It is naïve to think of China as a single market - it is really a collection of markets. Mainland China comprises 23 provinces, five autonomous regions, and four municipalities, as well as numerous special economic zones, open coastal and border cities, export processing areas, bonded zones, provincial-level economic and technological development zones, and new and hi-technology development zones. The greater Shanghai area has a larger population than Holland and Malaysia.

workshop of the world

Westerners also need to be aware of the diametrically opposed cultural differences in social and business customs. For example:

In the West black is the funeral colour, in China it is white.

Red signifies danger in the West, and good luck in China.

In China the groom's family pays for weddings, in the West the bride's family does. Married women in China keep their own surnames, while most in the West still take that of their husband.

In China, it is perfectly acceptable to be asked for personal information - whether you're married, what your salary is - in a way that would be considered impolite in the UK.

In the West, the most senior person will sit at the head of the dining table, in China they will sit in the middle.

Speeches in China usually happen towards the beginning of a meal, rather than the end.

In the West, it is polite to finish your meal, in China, this suggests that you are still hungry.

In China, giving clocks or watches as presents is a no-no, as the words for *to give a clock* sound the same as the words for *to take someone to their death*.

I could go on. Of course, allowances will be made for foreign visitors, but demonstrating an understanding of social mores is one way of showing respect to your hosts.

I called my remarks this morning, *China: the re-emergence of the Middle Kingdom*, and it is clear that the Middle Kingdom is moving to the centre of the world stage today.

Of course, HSBC takes a special interest in China's development. After all we were founded in Hong Kong and Shanghai in 1865 and have had a continuous presence in China since - through thick and thin.

In our view, it is inevitable that China will become a superpower. And indeed, desirable. And we are positioning our business for the decades ahead accordingly. We have invested over US\$4 billion in building our business both organically and by investments - reflecting our optimism for the future.

The Asian economic miracle produced a 40-year period of above average economic growth in countries like Japan, Taiwan and Singapore, we might reasonably expect China to do the same. This means that China is probably only half-way along its amazing economic journey.

It is already the world's sixth largest economy, in spite of the fact that less than half of its population are participating in its 'economic miracle'. Just think what might happen when the 800 million people in the countryside start contributing to China's economy.

As Premier Zhu Rongji once said to me, when you consider how successful Chinese people have been in places like Singapore and Taiwan, it would be ironic if they could not be successful in their own country.

In summary, ladies and gentlemen, the last 20 years have seen China open up and move from isolation to a position where it will exert a huge presence on the international scene.

An article in *Newsweek* magazine characterised it thus: "There have been two great shifts in global power over the past 400 years. The first was the rise of Europe, which around the 17th century started to become the richest, most enterprising and ambitious part of the world. The second was the rise of the United States, in the late 19th and

20th centuries, when it became the single most powerful country in the world. China's rise, along with that of India, represents the third great shift in global power - the rise of Asia."

The anxiety among Western nations about the re-emergence of the Middle Kingdom is palpable. But rather than batten down the hatches, we should remember that when the typhoon blows the oak breaks, but the bamboo bends and becomes stronger.

We could all learn something from the bamboo.

I'm reminded of an observation made to me by a senior Chinese diplomat. "If you want to understand 2,000 years of Chinese history go to Xian. If you want to understand a thousand years of Chinese history go to Beijing. And if you want to understand the last 150 years go to Shanghai."

Perhaps I should add if you want to understand the 21st century, you have to understand China.

Ends

the third great shift in global power – the rise of Asia