China Is Not Vulnerable, Part 1

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By GORDON STYLES, Engineer & Managing Director, Star Prototype

I am a manufacturing diehard. I love engineering. I am British, and for the last six years, I have lived and worked in China. I have my own 100 percent privately owned factory in Zhongshan [1] with 80 employees, and I have hands-on experience in dealing with Chinese regulation in many aspects of business.

I recently bought an American FARO laser-scanning arm for USD $100,000, and I imported it into China with a customs duty of $0. Yes, $0.

China has decided that the country needs to buy a lot of the world’s high-technology equipment, and it is helping its factories do so by raising the value of the yuan by 6 percent per annum and dramatically reducing import duties. Does this surprise you? It should. I am also guessing that Donald Trump missed that annoying little detail.

So, when I read Perry Sainati’s piece, “Why China is Vulnerable [2],” I felt compelled to respond to his many reasons for China’s vulnerability. Perry, my response is meant in good spirit and with the hope of developing a healthy debate between us.

Reason #1: The Lead Paint Factor

I have to buy from my Chinese suppliers all of the time, and it is absolutely true that China has a very long way to go on the product quality front, but this is changing very fast.

In 2010, the Chinese Premier Wen Jiabao pronounced, “Food safety and product quality should be our top priority." Since that time, there has been a huge push to ensure that China’s manufacturers deliver higher quality goods.

One of the effects of this is to ensure that all kinds of high-tech imported inspection and manufacturing equipment are duty free — hence the $0 duty on my new FARO arm.

On the issue of lead paint, it is true that some products were recalled as a result of excessive levels of lead in paint on Mattel products in 2007. The levels were higher than regulated, but not one single case of lead poisoning was reported in the U.S. as a result.

In contrast, the company at the center of the paint scandal was Lee Der Toy Company. As a direct result of Mattel and CNN complaining loudly about the lead-in-the-paint issue, the Chinese government took away Lee Der’s export license and 5,000 people lost their jobs. The manager of the factory, Zhang Shuhong [3], sold all of the machinery, distributed that money to his workers and then hanged himself shortly after the factory closed its doors. The paint had come from a number of his suppliers. Only one person died, and it wasn’t from lead poisoning.

Mr. Zhang’s funeral was held in the factory yard shortly after his death.

Most of the Mattel recalls in 2007 had nothing to do with lead. In fact, it was as a result of a faulty Mattel design and loose magnets.

From Wikipedia: On September 21, Mattel issued an apology to China over the recall of Chinese-made toys, taking the blame for design flaws and acknowledging that a "vast majority of those products that were recalled were the result of a design flaw in Mattel's design, not through a manufacturing flaw in China's manufacturers." *[4]*

Plus, the video of the infamous Mattel apology can be found on YouTube [5].

The apology was played at almost every opportunity on all of China’s news channels for days, and yet, I have been unable to find a single person outside China that saw it. Mr. Zhang paid the ultimate price and, as a result, became a Chinese national hero.

One piece of advice to all buyers of product from anywhere in the world: Make sure you have awesome quality control (QC). If you cannot measure it; you cannot make it**.**

China’s quality drive is in top gear at this time, and I receive standard letters from the government urging me to produce better products. Enforcement is the problem, though. That said, remember when 14 people were sentenced to jail [6] with terms of up to life for a melamine-tainted milk scandal? There is no shortage of desire on the part of the Chinese government to improve quality; but there is no end to the desire to cut corners to make more profit — and that is a human fault.

Reason #2: Market Knowledge

I do believe Perry’s assertion that U.S. companies are nimble and light on their feet because they have operated in an open and competitive environment for a long time. They also do not suffer overbearing government interference, and it makes American companies more responsive to customer needs. This is true, and it is part of the great American spirit.

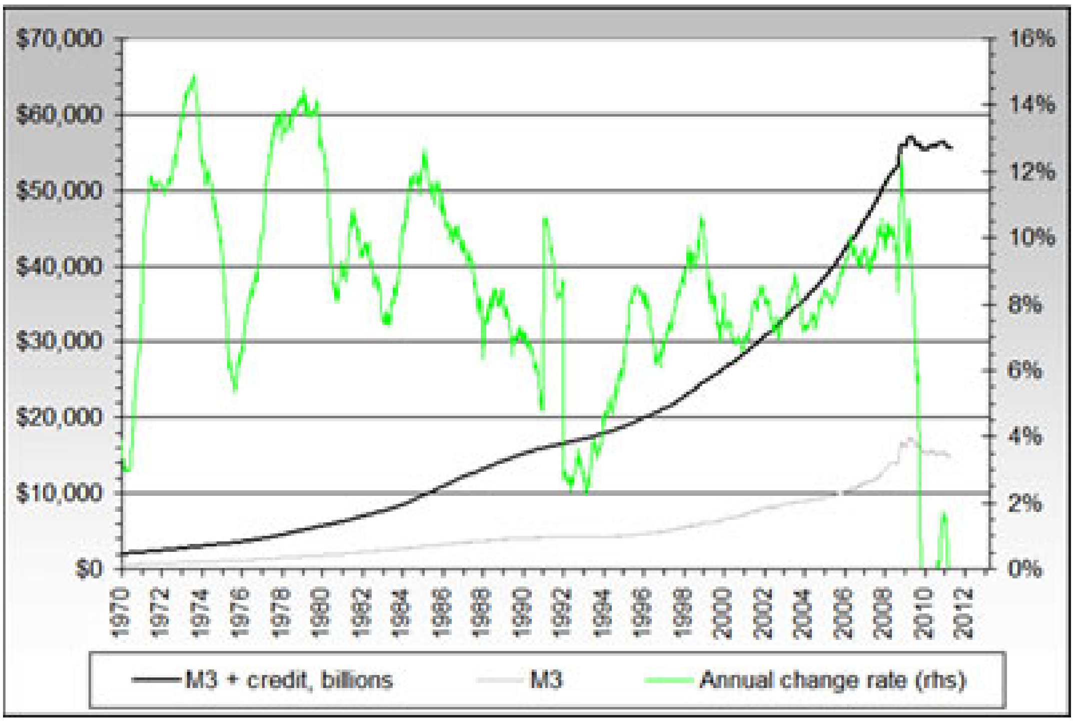
But, it was the lack of government interference in some very important areas of American and UK business that led to the world’s worst financial meltdown in history — and America’s worst environmental disaster in history (with more than a little help from the Brits, again). Regulation must not be too overbearing, but there must be enough functional regulation to ensure that greedy individuals and companies don’t wreck the joint.

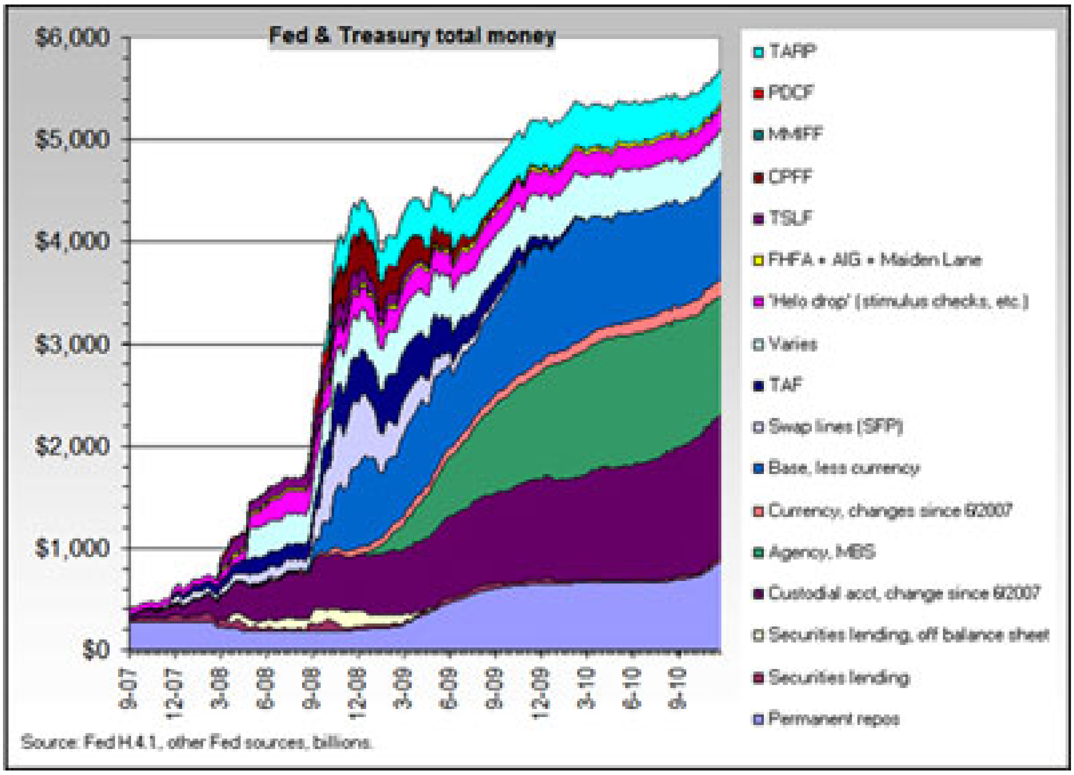
China does have tight control over its state-owned enterprises. Frankly, I could not agree more with their strategy in many instances. I will give you one example. It is a fact that economies expand and contract as the Money – Supply + Credit expands and contracts. If you can control the precise amount of Money – Supply + Credit, you stand a chance of controlling the growth of the economy.

China’s Central Bank, and a plethora of state-owned banks, have the most draconian controls over Fractional Reserve Requirements and creation of credit. As a result, China’s GDP has grown at a straight line 9.91 percent per annum for 30 years (or 15.2 percent in today’s prices). Even at the height of the global financial crisis in 2009, GDP grew 9.2 percent.

In contrast, the UK and U.S. allowed its banks to do whatever they wanted — and they did. Just before the crash, the money supply in the U.S. was about USD $1 trillion against credit of about USD $50 trillion+, a real reserve ratio of about 2 percent. The UK had a similar situation. When the big banks realized they were all disastrously overstretched, they pulled around USD $4 trillion out of the credit supply, leading to the largest economic crash in history. The fed and government had to fill a USD $4 trillion hole (about 30 percent of the U.S. economy).

The two graphs [7] below demonstrate what happens when Government does not interfere appropriately:





Please tune into the Chemical Equipment Daily for part two of this two-part series. What's your take? Please feel free to leave a comment below or contact Styles at gordon.styles@star-prototype-china.com [8]. For more information, please visit www.star-prototype-china.com [9].

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