

Beware of Lanes Merging Ahead

Sometimes it is hard to draw a line between businesses cutting costs and cutting corners. But in the hands of the unscrupulous, business ethics becomes the issue. Judging from the generational time lapse from the turmoil of the 60s, we may witness the trough in terms of business ethics in the next 5-10 years. The current China product quality/safety crisis may just be the tip of the iceberg...

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When we visited Shanxi (which happens to be 'home' to the recent [slave labor scandal](#)) on our [10th outbound matchmaking trip last Nov.](#), we were treated with *Fenjiu*, a nationally-renowned local liquor, at a welcome banquet ([photo](#)) hosted by one of the province's vice governors. At the table, he showed us a trick to tell authentic *Fenjiu* from the fakes. (Yes, we had the real deal...)

Now fast forward to June '07. We left for [our 11th trip](#) amid the [Chinese product quality crisis](#) on the States side but came back to find the Chinese media themselves boiling over a series of latest food safety breach exposés, including the finding that [50% of the water supplied to coolers in Beijing is fake](#).

"'Made in China' with what and how" seems to be the " (*fill in the blank*)-dollar question" that every [China-marketeer](#) has to face nowadays. In fact, at MCB we have also noticed the steady increase in our members and clients' demand for our assistance in quality inspection and due diligence, a stark contrast to simply matchmaking earlier.

Although counterfeits and faulty products have flooded China for long (remember that \$5 Rolex watch you or your friend bought that stopped working in a matter of days?), but never did the problem seem to have been elevated to the level of [a crisis that we are witnessing today](#). What has changed?

One may argue that while a fake Rolex would never deliver any bodily harm (unless [its battery blew up in your shirt pocket](#)), poisoned food can kill you. But contaminated food or faulty products in China did not just start killing people recently. It has been going on there for years. For example, even as early as 2002, partial government data had already recorded thousands

poisoned by fake liquor made with methanol-containing industrial alcohol with hundreds of deaths.

Up until recently the Chinese government's tight control over most sectors of its economy had hindered Western companies - except perhaps the largest multi-nationals - from fully accessing and leveraging China's market opportunities. But in the meantime these very obstacles also served as a 'firewall' that helped shield the Western firms from many of the problems that constantly confounded Chinese businesses domestically.

For example, in the past all products had to be exported through a finite number of state-owned import/export monopolies. Up until at least the mid-90s, only the beer from Tsingtao's first brewery plant - the best among all of its plants - would be exported to the West, as per the government's mandate under a planned economy.

Since there was strict oversight and control, no American would have needed to worry about methanol poisoning. Credit risk was relatively low as well.

Now that the country is relaxing its grip in more and more areas, and that anyone can apply for a license and export products, it is only a matter of time when all these former 'internal' problems are 'exported'. And it is the mid-sized firms that tend to get hit first. Why?

Let me use an analogy. I have not yet seen an American who does not, upon arriving in China for the first time, get shocked by (and, in many cases, simultaneously marvel at) the road traffic scene there. It is like a school of fish (of different species, of course) swimming together. Nobody seems to care about, much less follow, any rules, signs, lines or lights - it is random, chaotic - but yet they don't seem to easily collide with each other either.

One can guess perhaps not too many Americans would dare to drive in China. On the other hand, if someone in the US were to drive like in China, s/he would surely get in an accident fast.

The larger firms, such as the multi-nationals, usually have all the resources needed, be it financial, human or time, to localize and adapt - that means re-learning and re-mastering new ways of doing things in the new environment and thus be in full control of all its local links in China. (A side note: depending on where you are coming from, this may not be all positive. A fully-localized corporate culture would more readily harbor predisposition and tolerance toward things that are usually considered off-limits in America, such as bribery and racial and sexual discrimination. From personal experience I'd also like to add that the quality of their products for the local market is also likely very compatible with the local consumer sophistication / cost of living / pricing).

In contrast, smaller firms tend to be overly conservative and thus don't dare to 'drive' much if at all. The mid-sized firms, however, may act differently from either of the above 2 approaches - they don't have enough resources to keep tabs on all the local links, yet they are big and bold enough to 'drive'. Then you wonder why they often 'collide'...

The current crisis may just be the tip of the iceberg, foreshadowing more issues to be 'exported' out of China as the country, while in the middle of a race to the bottom, continues to ['capitalicize' / depoliticize / deregulate the country's economic life](#), providing more opportunities to both the scrupulous and otherwise. Judging from the generational time lapse from the turmoil of the 60s, we may witness the trough in terms of business ethics, if nothing else, in the next 5-10 years.

A likely challenge to come, to which small biz is particularly vulnerable, is increased credit risk, both intentional (e.g., scams and rip-offs) and unintentional (due to China's intrinsic circular debt-prone - or ['triangular debt'](#) as it is called locally - commercial environment with weak securitization mechanisms and limited recourse options).

Like the US Dept of Commerce which promptly released its [new China Military "Catch-all" Regulation](#) upon China's recent pledge to open up its defense sector, US SMEs should be prepared to cope with the new reality of China Biz.