

# Observations from China: Working Together to Drive Corporate Growth



## An Interview with T. Patrick Hurley, Jr.

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“Our driver in Beijing attributed the quite heavy traffic to it being “close to the end of another hectic week” in the thriving city of nearly 10 million with a strong capitalist pulse.”



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**Q** MidMarket Capital Advisors recently served as a co-sponsor of a unique, live, interactive Videoconference for companies interested in partnering with Hong Kong to do business in China. How did this session stimulate in finding out more about opportunities within Mainland China?

**A** I participated as the Videoconference moderator with the panel in Hong Kong. This trip provided a tremendous, firsthand opportunity on several fronts: First, to better understand the distinctions and similarities between Mainland China and Hong Kong, and how both play vitally interdependent roles; secondly, to confirm traditional opportunities

China and USA Superimposed



for midmarket companies in securing the manufacture of goods in Mainland China, based on the attractive labor and cost advantages; and finally, to understand how a stronger dialogue between US, Hong Kong and Mainland connections could lead to success for everyone.

**Q** What were your firsthand observations and experiences?

**A** You are struck by the tremendous concentration of labor that can create opportunity and growth. We had traveled to Mainland China, focusing, among other regions, on the area of South China between Guangzhou and Hong Kong known as the Pearl River Delta, one of several industrial zones in China. The sheer density of available labor resources in these zones is almost beyond comprehension. As an example, in a 100-mile radius of Hong Kong, the Pearl River Delta has 60,000 businesses employing 15 million workers in integrated clusters of suppliers and assemblers. The area has a total population of

85 million people—the same as Pennsylvania, California, Florida and Texas combined. CEO Alan Wong of VTech Holdings, one of the Videoconference participants, described this region as a “paradise for manufacturing companies.”



**Q** Much has already been written about the shifting in manufacturing to China for production of goods to export to Western markets. What are some of the other patterns that you see from your conversations with business leaders in Hong Kong and China?

**A** Attention is beginning to turn to the expanding Mainland population of 200 million people who can now afford to purchase many of U.S. products and services. Chinese consumers have much more purchasing power than most U.S. middle market companies realize.

**Q** What about economic reform in China? Is this helping to middle market companies as well?

**A** It is interesting to note that the economic reforms launched in 1979 have only recently shifted in to high gear—the result of China's acceding to the World Trade Organization in late 2001. The January 2004 implementation of the Closer Economic Development Partnership Arrangement, or CEPA, eliminates tariffs for Hong Kong companies. Many of those companies based in Hong Kong and benefiting from the new trade agreement have significant Western ownership.

**Q** How do these new agreements help to tap into the Chinese population as a market for products produced by Western companies in China?

**A** The World Trade Organization and CEPA agreements mean that products manufactured in China can be purchased by people in China as well as exported. And players can pursue joint venture opportunities, move past the restrictions applicable to representative offices and to more readily operate wholly owned foreign subsidiaries, all of which encourage investment and increased activity focused on the domestic market. This is certainly supported by the Chinese population's affection for American brands.

**Q How does Hong Kong play a key role in encouraging solid contacts between the midmarket companies and businesses in Mainland China?**

**A** There are important interdependencies for all of the players. Hong Kong can serve as a key bridge between the very different cultural landscape within Mainland China. A trip to Hong Kong is similar to traveling to London. Entering Mainland China requires a visa and the differences with the west are more striking as you venture farther away from the large coastal cities, such as Beijing or Guangzhou. In many respects, Hong Kong may well be the most important entrée point to the Mainland. During his Videoconference participation, Jim

Thompson, CEO of Crown Worldwide, cited Hong Kong's designation as the freest economy in the world by the Heritage Foundation, which consisted of 357 cities. The tax structure and legal system in Hong Kong, as well as the British-based law and order system, offer advantages of familiarity to Western companies.

**Q How can this affect the success of business deals?**

**A** Understand that when you go into a business venture in China, you cannot rely upon contracts in the same manner that you do here in the United States. Nearly half of the contracts written in China each year are not honored. Dispute resolution in Hong Kong is much more predictable than in China. So, once, again, it is important to via Hong Kong as a conduit to success in launching and completing deals successfully.

**Q What other precautions can you share?**

**A** K.O. Chai, another Videoconference panelist, heads up Asia for Walden International, a \$1.8 billion venture capital firm. He cautions that we need to view the China market as 27 provinces with widely varying demand characteristics. Another concern is the theft of intellectual property rights. Many companies protect their proprietary R& D activity within Hong Kong. A third issue is one of currency. Concern has been expressed that floating currency could actually drive the cost of exports down rather than up. Remember that we are still looking at a trade imbalance of \$125 billion.

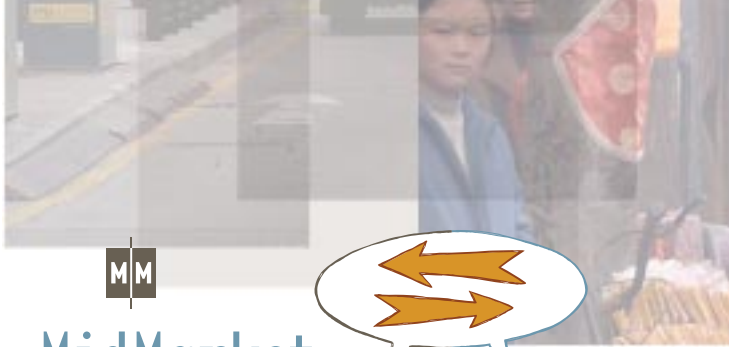


**Q How about advice for the future?**

**A** China is very much a work in progress. However, programs such as the Videoconference are examples of the stronger steps being taken to increase the dialogue between the players. Organizations such as the Hong Kong Trade Development Council are looking for ways to create “win-win” scenarios between Mainland China and the U.S.

There is no doubt that smart midmarket companies must factor China in to their strategic plans for both short-term and long-term growth.





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