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Concerns for secondary cities

Urbanization is vital to China's development over the next decade. In fact, the secondary cities will be just as important as the first-tier cities, if not more so, because they will play a key role in fueling China's inland growth.

With a combined population of 43 million, nearly the size of Spain's, and a combined GDP of $550 billion, which would rank 20th in the world, China's two flagship cities have often determined the economic fate of the rest of the country. They are also prime examples of the challenges for megacities, such as escalating house prices, traffic gridlock, extensive air and water pollution, and overcrowding.

However, the megacities are no longer the only story. It is estimated that in the coming decades China's urban population will grow by 250 million.

The accelerating rural-to-urban population migration will increasingly impact China's secondary cities, those with populations between 1 and 10 million (some 135 cities in total). It is these cities that are expected to absorb much of the country's growth in the coming years.

The global emergence of the inland secondary cities in China is a result of shifting patterns of business investment, the lower costs of living, their healthier environments and ambitious local leadership. Reforms to the household registration system, such as those proposed by Chengdu, are also facilitating rural to inland urban migration as benefits are extended to the families of migrant workers.

In September, Premier Li Keqiang emphasized the importance of economic expansion in inland China, describing these areas as the "biggest space" for development.

The majority of China's rapidly growing second-tier cities are in the central and western provinces, and their proximity to large rural populations and low land costs will drive growth, as workers seek industrial jobs closer to their home regions.

This opportunity is already recognized in the international business environment. For example, since 2005, more than one-third of Changsha's foreign direct investment has come from Western countries.

This growth is partly the result of a new policy model. A common vision for urbanization is growth driven by the consumption of the middle- and high-income groups. Rising disposable incomes are expected to support domestic demand for locally manufactured products. According to the World Bank, domestic consumption accounted for only 36 percent of China's GDP in 2011. It accounted for 72 percent in the United States that year, 65 percent in the United Kingdom, and 59 percent in India. China's domestic markets have the potential to sustain the economic growth of secondary cities, even if the global economy continues to stagnate.

What makes secondary cities different from primary cities? Aside from being smaller and having less economic activity, second-tier cities represent unique opportunities. First, they can learn from the mistakes of the congested, crowded and poorly planned first-tier cities. These lessons include preserving historic buildings, planning for congestion, creating green spaces to enhance the urban environment, and maintaining clean air and water.

Second, they have greater flexibility to seize potential economic opportunities: They are closer to the untapped inland consumers and the inland labor markets, and their land costs are significantly lower than megacities. They also have more recently constructed infrastructure, which is better designed and more up-to-date. Communications technology, commercial parks, institutional structures, or enabling entrepreneurship, whatever it is, secondary cities are often in the early planning stages and do not have to work around legacy infrastructure and entrenched institutional and political systems. The inland cities are now witnessing the relocation of heavy industries from coastal areas and growth in the high-value technology sector.

However, such growth is not always rosy for secondary cities. In central areas large real estate projects spring up where much-loved historical neighborhoods once stood. At the suburban edges, a new wave of modern development is encroaching on farmland and villages. And as property values rise in the secondary cities, conversion of land into taxable residential and commercial properties is a common way for local governments to raise revenue.

Also rapid city-level economic growth is not always sustainable. Cities capturing fast growth at the margins of economic expansion risk losing it just as quickly. For example, Yantian, once an agricultural town on the fringes of the Pearl River Delta, experienced high growth from foreign industrial investment throughout the 1990s. Today, however, fewer than half of its manufacturing facilities are still operating. The faltering global economy, rising wages, and a stronger renminbi (up 34 percent against the US dollar since 2005) drove many local manufacturers to bankruptcy.

Cities losing manufacturing can experience rapid population decline, which weakens the consumer base. This is especially true for cities that fail to address the pitfalls of the household registration system, as workers denied social support services are increasingly transient.

China's secondary cities will also suffer a widening infrastructure deficit as population growth — both native and migratory — strains existing systems. Nearsighted urban planning strategies emphasizing speed over prudence have exacerbated this problem.

The benefits of urban real estate development are uncertain. Some inland cities are now experiencing an oversupply of housing. This undermines the strategy of "building to grow." Additionally, some farmers have aggressively protested at the seizure of agricultural land for commercial purposes when they were not been paid the market prices.

Finally, an ageing workforce and slowing population growth rate are creating economic headwinds in China, impacting not only secondary cities but all cities. Indeed, the UN projects that China's labor force is expected to shrink by 67 million between 2010 and 2030. By 2030, China will have more elderly people than the current population in the US.

Secondary cities must have diversified growth strategies and a sustainable competitive position to survive inevitable economic slowdowns.

Economic growth will produce many job opportunities in China's inland cities, as producers in the coastal megacities suffer lower productivity due to congestion and higher labor and land costs.

However, wise planning can help to mitigate these inevitable impact of problems in the inland cities. Decision-makers should start by heeding the lessons to be learned from the development experiences of the country's megacities.

China's inland secondary cities have a roadmap to achieve this goal, but it will require visionary leadership and comprehensive policies that address all dimensions of urban society.

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STEPHAN RICHTER AND NATHAN RICHTER

Two innovation models to learn from

The three nations that, one way or another, lead the global economy at the moment are the United States, Germany and China. For the US, it is innovation driven by a can-do spirit and an appetite for risk, with established corporations and startups introducing some of the world's most important and game-changing technologies. In Germany, a commitment to product quality and engineering excellence has been key to the success of both its multinationals and small- and medium-sized enterprises.

China's economic strength has been built on its cost competitiveness and the adoption of foreign-developed technologies and innovations since its opening-up, and its global impact has been due mainly to its massive scale. The global financial crisis, however, has ushered in a new phase in China's economic development, as it can no longer rely predominantly on foreign consumption as an engine for growth. It has to develop domestic consumer markets and orient its production towards them. Furthermore, rising wage costs make it highly unlikely that China will be able to continue to grow by being the factory for many of the world's simpler products.

To move forward and move up the value chain, China needs to begin developing a management system and, more importantly a culture, for technological and product innovation.

To catch up in innovation, China needs to learn from Germany and the US, which offer the two main — and quite contrasting — models for future success.

The US business community benefits from the long tradition of newcomers taking risks on entirely new product categories and technologies and leapfrogging companies that have lost their competitive edge. One need only look at Apple for a basic idea of how this plays out. Another trait of US firms is that decisions are usually made in a top-down fashion, requiring only one or at most a few people's approval, which allows for rapid adaptation and changes in direction.

The advantages of the US approach to managing innovation are quicker market penetration of new products, broad brand recognition in new markets, and attention to customer feedback, which can be used to improve future generations of products. The weakness, one could argue, is that product quality may suffer, leaving the door open for other companies (possibly from other nations) to step in.

German corporations have historically been big innovators in terms of technology and product quality. However, because of a cultural resistance to risk and a widespread preference for stability, larger German corporations of late have not been able to capitalize on new ideas to the same degree as US companies. Management in German firms is also more horizontally organized. If a decision is to be made, it must be approved in a time-consuming process by multiple individuals or groups. Even after it's been decided at the top, the process may be slowed by levels below. However, these traits are less pronounced with Germany's more nimble SMEs.

The advantages of the German approach to managing innovation are high product quality and well-thought-out services that accompany those products. The downside is that new products can be late to market, and truly disruptive innovations are few. Even when German companies come up with disruptive ideas, they can miss discovering their immense market potential, such as the German-invented MP3 player. Disruption and rapid scaling-up seem to fit better with the US psyche. It is important to keep in mind, though, that as far as market and sales potential are concerned, the German approach — while more restrained — can be lucrative and self-sustaining.

What does this mean with regard to China's future path? The argument is often made that the freer people are in a society or an economy, the more innovation is likely to result. Innovation is bound to happen when people are taught from a young age to challenge the norm. However, the democracy-innovation nexus should not be overstated. Historically speaking, German companies displayed an innovative spirit long before the country was a democracy. That suggests that democracy is not necessarily a requirement for innovation.

That part of the historical record sounds like potential good news for today's China. But it is crucial to recall what Germany did have as assets at the time — a strong engineering tradition, a strong adherence to the rule of law, as well as a quickly rising focus on intellectual property rights. On that basis, risk taking and innovation were properly rewarded. China does not yet have the engineering and legal traditions Germany has, and it also lacks other key ingredients in the innovation formula.

How about Chinese firms finding inspiration in the US model? The trait that Chinese firms share with US ones is the ability and inclination to bring a new products to market quickly, although generally at a low level of product sophistication. Where Chinese firms still have a lot of catching up to do in making adjustments based on customer feedback as well. Bringing a new product to market rapidly and improving its quality based on feedback from customers is the true value of the US' approach. There can be no doubt that Chinese companies will also adopt this approach before long. The size of the Chinese market and the increasing sophistication and quality demands of Chinese consumers will likely ensure that.

The big question for Chinese companies is whether they can find their own equivalent of the risk-taking spirit in the US that results in radical product innovation, or develop something more like the German model of technological excellence to give products a global advantage.

All that can be reliably said at this stage is that China's new leaders recognize the challenge. They have begun to encourage innovation and are revamping the educational structures and priorities. Some of China's leading universities have launched programs dedicated to honing the innovation potential of the country's future managers.

It's also likely that both the German and US approaches to management are going to be practiced in China. The country's State-owned enterprises, whether partly privatized yet or not, are "German" in their character. They have to obtain a lot of buy-in, including from political stakeholders, and thus are likely to follow a more slow-moving, horizontal management approach. In contrast, privately owned firms in China are bound to follow the more nimble top-down US model.

The ultimate outcome of China's innovation journey of course remains highly uncertain. One thing is for sure, though — it will be fascinating to watch.

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LETTERS

All at risk from smog

Comment on "Report highlights smog effects" (China Daily website, Nov 5)

The report's result doesn't surprise me at all. It's obvious to everybody, even the kids, that heavy smog in many places in China leads to negative effects on citizens as well as society. But the report let people know how wide the heavy air pollution has spread in China, and how tremendous the heavy air pollution's negative effects are.

As the report says, the frequent smoggy weather is likely to cause extreme climate incidents, hinder traffic due to low visibility, and badly harm people's health. The cost of air pollution that China has paid, is paying and will pay in the future is uncountable, because many negative effects will appear gradually over the long term rather than at once. For example, air pollution leads to many severe chronic diseases and will harm the human reproductive system. It means in the future we will pay a lot for the damage that air pollution is doing to people.

The seriousness of air pollution should draw the attention of every one in society, especially related officials. Policymakers who care about short term profits should read this report and consider the significance of air pollution management to this country.

SHEN XIAOYAN, *via e-mail*

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FROM THE CHINESE PRESS

Higher wages for workers

An economics professor from the Capital University of Economics and Business found that people's spending power has shrunk by almost half within eight years. For most people that is not just because the value of the yuan has dropped but because they are underpaid, says an article from dahe.cn. Excerpts:

In developed countries, employees' wages generally account for about 50 percent of a company's overall costs. In China, the figure is less than 10 percent.

Also, the amount of labor remuneration in developed countries generally represents more than 55 percent of the country's national revenues. In China, the proportion is less than 42 percent. What's worse, people's incomes as a proportion of national revenue continue to show a downward trend.

The distribution of income in China has favored local governments and enterprises. For example, employees in State-owned monopolistic enterprises have enjoyed larger benefits compared with those working in small- and medium-sized private companies.

Considering the increasing costs of education, medical treatment and buying a house, no wonder people feel that their money is becoming less affordable.

Under current policies, increases in pensions and the threshold for individual income tax are both very limited.

To reverse the deepening wealth gap, the authorities have to continue carrying forward reforms to raise the proportion of earned income at the primary distribution stage. For one thing, local governments should provide policy support for ordinary employees to strive for better wages, and they need to make moves to reduce the burdens on enterprises and the public, and create more channels and space for people to increase their earnings.

Extravagant offices reflect mindset

The construction of the government office building in Changxing county, Zhejiang province, costs 2 billion yuan ($328 million); another government office building in the city of Jinan, Shandong province, costs 4 billion yuan. Such grand office buildings reflect local authorities' luxurious mindsets and ignorance of people's feelings, says an article from youth.cn. Excerpts:

Some local authorities have the wrong perception that the more extravagant their office compounds are, the more capable they seem.

But the construction of such grand office buildings has violated the central government's directives and regulations. Local authorities who build such luxurious office buildings get away with their wrongful behavior because they claim that the funds have been used for construction, and not gone into the pockets of officials. It is certainly rare that an official is investigated for constructing extravagant office buildings, even though it breaches regulations.

In fact, local officials' extravagant mindsets are not only reflected in their flashy work style, but also their deviation from the lives of ordinary people. Such behavior that goes against people's interests should be dealt with as seriously as other political misdeeds.

Governments exercise their powers for the people and they should share weal and woe with the people. To build up extravagant government office buildings using taxpayers' money obviously goes against people's interests, especially at a time when house prices are soaring and many can't afford to buy one. We must hold a "zero-tolerance" attitude towards such extravagant government buildings to prevent it from happening in the future and to nip the luxurious mindsets of officials in the bud.

To crackdown on the "four forms of decadence" namely: formalism, bureaucratism, hedonism and extravagance, such extravagant buildings should never be allowed. It is through the building up of frugality that a better image of the government will be built up in the eyes of the public.

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