HKUST IEMS
INSTITUTE FOR EMERGING MARKET STUDIES

NEWSLETTER FALL 2015

Jack Goldstone, Albert Park, Agnes Chan (EY Hong Kong), Wei Shyy (HKUST)

POLITICAL AND ECONOMIC CONSEQUENCES OF DEMOGRAPHIC CHANGE IN EMERGING MARKETS

HKUST IEMS – EY Hong Kong Emerging Market Insights Series (2015.06.25)

Albert Park, Director of HKUST IEMS, and **Jack Goldstone**, Professor of Public Policy at George Mason University, and incoming Director of HKUST's Institute for Public Policy, examined the political and economic ramifications of population challenges facing emerging markets. Prof. Park noted that demographic changes will boost growth in young countries like India and African nations, but slow growth in aging countries like China and nations in Latin America and Eastern Europe.

For China in particular, Prof. Park stated that of greatest concern to policymakers is China's explosion of elderly population, as this demographic group (those aged 65 and older) is forecast to more than double in size from 130 to over 300 million in the next 20 years, comprising over 1/4th of China's total population. Studies also show that this group is currently not faring well economically, physically, or emotionally: 23% are poor, 38% are somewhat handicapped, and 40% suffer from elevated depressive symptoms. China needs to act quickly to strengthen the social safety net supporting China's elderly, in particular though the integration of local and federal pension schemes and social welfare systems.

On the political consequences of China's aging population, Prof. Goldstone pointed to recent studies revealing a strong correlation between democratic governance and a country's median age– that is, the older a country's population becomes, the more likely it is to become democratic (as well as more educated). As China ages and achieves ever-higher levels of education, Prof. Goldstone predicts that China's population will incline increasingly toward democracy. By 2030, other emerging market countries such as Brazil, Russia, Turkey, and Vietnam also are likely to experience a gradual political shift toward democratization, as each country is forecast to reach a median age of 40 with increasing levels of education.

The talk was held at EY's executive boardroom in Central, Hong Kong, and organized by HKUST IEMS.

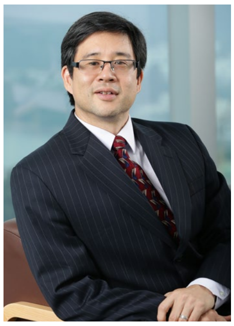
Video recordings available at
http://iems.ust.hk/insights

DIRECTOR'S MESSAGE

Albert Park

During the first half of 2015, HKUST IEMS was extremely active fulfilling its mission to provide thought leadership on a range of issues confronting emerging markets. The Institute organized a busy schedule of events, including 4 conferences, 4 policy and business talks, and 8 academic seminars, details of which you can read about in this newsletter.

The Institute awarded Research Grants to support 10 new faculty research projects, including collaborative grants among faculty from different departments at HKUST and with leading scholars outside the university. To disseminate faculty research findings in an accessible way, HKUST IEMS produced 6 new Thought Leadership Briefs. We also proudly launched a new academic working paper series to make our faculty's research papers more visible on line. We have increased the video content on our website and through social media to make our events and ideas more accessible to a global audience.



After two years of steady development, HKUST IEMS is now clicking on all cylinders. None of the Institute's success would be possible without an outstanding staff, strong support from HKUST's leadership team, and our donors at EY, and the extraordinary initiative and productivity of our Institute's Faculty Associates.

THE MARKET AND THE STATE IN CHINA'S ECONOMIC REFORMS

HKUST Business Insights Series (2015.04.22)

In a double-billed presentation on China's recent market reform efforts, HKUST IEMS Director **Albert Park** addressed the topic of China's latest labor market reforms, and HKUST Assistant Professor of Economics and IEMS Faculty Associate **Yong Wang** discussed reforms to China's state-owned enterprises (SOEs).

Prof. Park detailed China's phenomenal economic growth which has accelerated demand for labor and, in the process, pushed up wages. In considering ways in which employment in China has become more inclusive, he noted that since 2007, rural migrant workers have experienced faster wage growth than urban workers, contributing to lower inequality. In addition, analysis of labor survey data shows that labor markets have become more integrated over time, making jobs more accessible to workers around the country. Nonetheless, some occupations remain out of the reach of migrant workers, and many institutions hamper their mobility, such as unequal access to education and lack of clear and transferable property rights over agricultural land. China has also implemented new labor regulations to increase the availability of high quality jobs, but many migrants still lack social insurance coverage (e.g. pensions, health care).

To alleviate the problem, Prof. Park advised that central policymakers further reduce institutional barriers to labor mobility, correct skill mismatches in the labor market, and speed up industrial and service upgrading to create new jobs in an increasingly competitive economy.

On the topic of SEO reform, Prof. Wang addressed a puzzle related to China's SOEs, namely that their profits have exploded since 2000 despite consistently poor performance in the 1990s.

Prof. Wang's research shows that the strong recent performance of SOEs may paradoxically come at high cost to the overall economy. Because SOEs were unable to compete with private firms in downstream industries such as consumer goods, they retreated to

Jiatao (J.T.) Li (HKUST), Albert Park, Yong Wang

upstream, protected industries that provide key intermediate inputs such as energy, telecommunications, and financial services. This has created a vertical structure of ownership in China's economy. The success of China's private, export-oriented firms, which thrived thanks to abundant cheap labor and trade liberalisation following entry into the WTO in 2001, increased demand for intermediate inputs sold by SOEs, fuelling their profits. However, the inefficiency and market power of SOEs increases the costs of the inputs they provide, which may compromise the competitiveness of China's downstream producers. Thus, diversifying ownership of SOEs and promoting free entry in upstream sectors should be a top policy priority.

Video recordings available at
http://iems.ust.hk/bizy

GOING GLOBAL FROM AN EMERGING MARKET CFO PERSPECTIVE

FT/EY Global CFO Forum: Emerging Markets (2015.06.24-26)

In the inaugural Global CFO Forum on Emerging Markets, hosted by the Financial Times and EY in Singapore, and attended by over 100 CFOs and executives of major global corporations, Director of HKUST IEMS **Albert Park** was invited as a panelist—along with Jardin Matheson's Finance Director **James Riley**, and author and global strategist **Parag Khanna**—to discuss macroeconomic risks and international growth prospects in emerging markets.

With respect to macro-level challenges for emerging markets in Asia, Prof. Park and the other panellists pointed to ever-increasing cost pressures, especially with regard to labor, which create challenges for sustaining growth momentum in the region.

Another challenge is growing "economic nationalism" in the region such that, despite talk of strengthening bi-lateral and multi-lateral trade agreements, there is often poor follow-through in implementation as domestic interests work to maintain barriers to international investment rather than tearing them down. As such, the panelists recommended caution over optimism when hearing news of multinational trade deals.

Perhaps the largest challenge mentioned during the discussion was with respect to China, which in the near-future may experience slower growth for both cyclical and structural reasons. Structural factors matter most for growth in the medium and long terms. Structurally, China is rapidly aging, and has reached a tipping point where the absolute size of the workforce will be decreasing over time. This shrinking of the labor force will exacerbate labor cost pressures, creating challenges for China to maintain growth momentum through additional reforms.

Jennifer Hughes (Financial Times), Parag Khanna (Hybrid Reallity Pte Ltd), Albert Park, James Riley (Jardine Matheson)

Thus far, Chinese President Xi Jinping has focused on battling widespread corruption, which is essential for improving governance for the management of the economy in general. In other key reform areas such as reforms to China's state-owned enterprises (SEOs) and liberalization of the capital market, progress has been markedly slow. Ultimately, as Prof. Park argued, "the future success of China depends on what actions the government takes next." Despite efforts by China's central government against corruption, Prof. Park and the other panellists questioned whether China's SOEs can be reformed in the current economic and political environment.

Find out more about the event at
http://live.ft.com/CFOForum
or visit
http://emergingmarkets.ey.com

RESEARCH GRANTS AWARDED IN 2015

HKUST IEMS Research Grants support high-quality research that provides valuable insights into the challenges facing businesses and governments in emerging markets. In 2015 the Institute encouraged collaborative proposals among HKUST faculty and with researchers outside HKUST and awarded 10 grants for unique research conducted on a broad range of emerging market related issues.

Find out more about the research grants at http://iems.ust.hk/grants/

Research Topic	Principal (Co-)Investigator(s)
Suppression or Diffusion? Effects of Foreign Direct Investment on Labor Rights Protection in Emerging Market Countries	Hye Jee Cho (HKUST)
Equity Crowdfunding in China: An Exploratory Study	Sam Garg (HKUST), Kellee Tsai (HKUST)
National Expressway Expansion, Trade integration and Pollution: Micro-Evidence from 60,000 Industrial Plants in China	Guojun He (HKUST), Bing Zhang (Nanjing University)
Agglomeration, Competition, and Firm Capability: Evidence from China and India	Amber Yao Li (HKUST), Joseph Kaboski (University of Notre Dame)
A Model of China's Shadow Banks and Market Determined Interest Rate Reform	Xi Li (HKUST), Yikai Wang (University of Oslo), Tong Zhang (University of Zurich), Fabrizio Zilibotti (University of Zurich)
Value of Chinese Patents: Evidence from the Chinese Patent Inventor Survey	Naubahar Sharif (HKUST)
Evaluating Spillover Effects of the Trader Agent Intermediated Lending Scheme on Non-borrowers	Sujata Visaria (HKUST Department of Economics), Pushkar Maitra (Monash University), Sandip Mitra (Indian Statistical Institute), Dilip Mookherjee (Boston University)
Industrial Upgrading, Structural Change, and Middle-Income Trap	Yong Wang (HKUST), Justin Yifu Lin (Peking University), Shang-Jin Wei (Columbia University)
Place-based Policies, Innovation and Entrepreneurship: Evidence from China's Economic Zones	Jin Wang (HKUST), Yao Amber Li (HKUST)
Product Market Response to Corporate Governance Shocks: Evidence from India	Alminas Zaldokas (HKUST), Abhiroop Mukherjee (HKUST)

NEW HKUST IEMS THOUGHT LEADERSHIP BRIEFS

Providing thought leadership and policy recommendations on key issues facing emerging markets

Issue	Title	Author(s)
#4 (January 2015)	Foreign Banks in Emerging Markets: Advantage or Impediment?	Sasidaran Gopalan (HKUST)
#5 (February 2015)	Localizing Chinese Enterprises in Africa: from Myths to Policies	Barry Sautman (HKUST) and Yan Hairong (Hong Kong Polytechnic University)
#6 (March 2015)	How Do Minimum Wage Policies Affect Workers in Emerging Markets?	Albert Park and Qing Xia (HKUST)
#7 (April 2015)	Wage Discrimination in Urban China: How Hukou Status Affects Migrant Pay	Xiaogang Wu (HKUST) and Zhuoni Zhang (City University of Hong Kong)
#8 (May 2015)	The Employment Gender Gap in Urban China: Why Women Benefited Less from China's Privatization Reforms	Christina Jenq (HKUST)
#9 (June 2015)	Renminbi Internationalization: the Prospects of China's Yuan as the Next Global Currency	Edwin Lai (HKUST)

See the full list of the briefs at http://iems.ust.hk/tlb

UNDERSTANDING FINANCIAL INCLUSION IN ASIA

HKUST IEMS – CAG Workshop (2015.05.20)

Co-hosted by HKUST IEMS and the National University of Singapore's Centre on Asia and Globalisation (CAG) at the Lee Kuan Yew School of Public Policy (LKYSPP), the one-and-a-half day workshop was held on the HKUST campus and open to the public. The workshop included sessions on themes such as measurements and determinants of financial inclusion, country-specific cases in Asia on the topic of financial inclusion, financial literacy and development in emerging Asia, credit constraints and distributive impacts, monetary policy, and models of financial inclusion.

Laurent Weill, Professor of Economics at the University of Strasbourg, detailed his study of various Asian countries based on the World Bank's Global Financial Index (Findex) database, which finds major similarities and differences in financial inclusion across Asian countries. With respect to similarities, gender generally does not influence the use of formal banking/saving in Asian countries, although it does influence the use of formal credit. Age strongly favors financial inclusion, as does higher education and income levels. With respect to differences across countries, Prof. Weill found that ownership of bank accounts varies considerably across Asian countries (but is strongly related to GDP per capita in each country), and the use of formal bank credit was lowest amongst relatively developed regions such as China, Hong Kong, and Japan.

Regarding the distributive impacts of financial inclusion in Asia, **Anand Srinivasan**, Associate Professor of Finance at the National University of Singapore, and **Ashok Thampy**, Associate Professor of Finance and Control at the Indian Institute of Management Bangalore, presented their study on firm relationships with government-owned versus private banks in India. Analyzing data on publicly traded companies in India, they found that banking with a government-owned bank reduced investment sensitivity to cash flow (a measure of the degree of credit access) by approximately 30% compared to banking with private banks. These findings reveal a beneficial aspect of governmental involvement in corporate lending markets.

Sergio Schmukler, Lead Economist in the Development Research Group at the World Bank, presented his study of capital raising activity (issuing bonds, taking loans, selling equity) using data on 45,000 publicly listed firms in 51 countries over the period 2003 to 2011. He found that fostering capital markets tended to benefit only a small amount of very large firms, with little to no benefit for smaller firms. However, for both large and small firms alike, a direct, positive connection exists between the issuance of bonds and firm growth across countries.

Other speakers and participants at the workshop included **Albert Park** (HKUST), **Mandira Sarma** (JNU), **Ramkishen Rajan** (GMU and NUS), **Ji Yeon Jean Hong** (HKUST), **Peter Mackay** (HKUST), **Cyn-Young Park** (Asian Development Bank), **Sasidaran Gopalan** (HKUST), **Tony Cavoli** (University of South Austrailia), **Rabin Hattari** (Asian Development Bank), **Ganga Tilakaratna** (Institute of Policy Studies), **Xiao Geng** (Fung Global Institute), **Naoyuki Yoshino** (Asian Development Bank Institute), **Tomoo Kikuchi** (CAG), **Sujata Visaria** (HKUST), **Christina Jenq** (HKUST), **Aaron Mehrota** (Bank of International Settlements), **Kellee Tsai** (HKUST), **Rajesh Chakrabarti** (Indian School of Business), **Kaushiki Sanyal** (Indian School of Business), **Moekti Soejachmoen** (Mandiri Institute), and **Sujata Balasubramanian** (HKUST)

Video recordings, papers, and presentation slides are available at http://iems.ust.hk/fncl

RESEARCH FORUM ON CAPITAL FLOWS AND FINANCIAL DEVELOPMENT IN EMERGING MARKET ECONOMIES

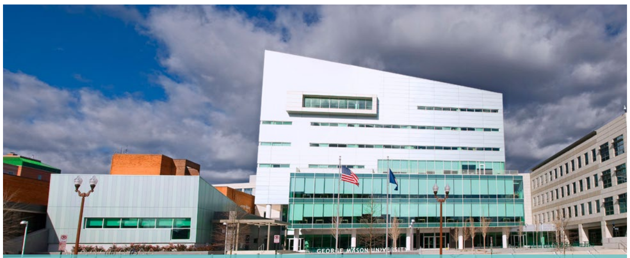
(2015.04.24)

Co-sponsored by HKUST IEMS and the Claremont Institute for Economic Policy Studies (CIEPS) at Claremont Graduate University (CGU), the Center for Emerging Market Policies (CEMP) at George Mason University's School of Policy, Government, and International Affairs (GMU-SPGIA) hosted its 5th annual research forum held at George Mason University's Arlington, VA campus focusing on the theme of capital flows and financial development in emerging market economies (EMEs).

The forum covered contemporary macroeconomic and financial policy issues of relevance to EMEs including the impact of quantitative easing policies on EMEs, implications of financial openness on financial development and volatility, exchange rate regimes and transmission of business cycles, as well as the impact of capital flow surges, reversals, and controls on EMEs.

A presentation by **Nicholas Coleman**, an economist at the Federal Reserve Board, provided empirical evidence on how different types of banks in Brazil managed liquidity internally among their municipal branches following a negative liquidity shock associated with the "taper tantrum" when the market began to anticipate the Federal Reserve's shift away from accommodative monetary policies. Following the liquidity shock, net intrabank borrowing by branches fell on average, but increased in government banks and in richer cities. Since such internal bank borrowing finances loans to clients, these patterns suggest that the operations of firms borrowing from government banks and in richer cities are better protected from external liquidity shocks.

Given the financial instability in emerging markets associated with international capital flows, economists have argued that in



George Mason University - Fairfax Drive Arlington (VA) Campus.
Photo credit: Ron Cogswell. CC BY 2.0 https://flic.kr/p/b3mBFx

theory it may be welfare-enhancing to apply capital controls in a countercyclical fashion. **Andres Fernandez** from the Inter-American Development Bank presented new empirical evidence that capital controls on both inflows and outflows have actually been acylical, and have not responded in a systematic way to the business cycle. This suggests either that policy makers have not learned the lessons of theory, or that researchers are missing key considerations that affect the optimal timing of imposing capital controls.

The research forum hosted economists both from multilateral institutions like the Board of Governors of the Federal Reserve System, the International Monetary Fund (IMF), The World Bank and Inter-American Development Bank (IDB) as well as national and global universities including George Washington University (GWU), the College of William and Mary, Claremont Graduate University (CGU), Claremont Mckenna College (CMC), HKUST, and George Mason University (GMU).

Find out more about the event at
http://iems.ust.hk/cemp

HKUST CONFERENCE ON INTERNATIONAL ECONOMICS

(2015.06.12-13)

Organized by the HKUST Department of Economics and co-sponsored by HKUST IEMS, the 3rd Annual Conference in International Economics was held over a 2-day period at the HKUST Business School on the theme of research frontiers in international economics, including a set of presentations focused on emerging markets.

Detailing his study on the organizational barriers to technology adoption using a case study of soccer ball producers in Pakistan, **Eric Verhoogen**, Associate Professor and Vice Dean of the School of International and Public Affairs, and Co-Director of the Center for Development Economics and Policy at Columbia University, described his study of several dozen producers and exporters of soccer balls in Pakistan which examined their the lack of adoption of a lower-cost production technology that decreased unit production costs by reducing wasted materials. The new technology was made available by the research team to a random subset of firms for free. However, only a small number of "treated" producers adopted the new technology. The reason for their resistance was surprising: skilled workers were paid by piece-rate — i.e. based on the number of soccer balls they produced per day — and the technology led to slower production albeit at lower cost. They thus told managers that the new technology was ineffective. This outcome shows how existing labor institutions (in this case piece-rate wages) can inhibit accurate assessment and adoption of new technology.

In a presentation on trade liberalization, productivity, and export prices, **Yao Amber Li**, Assistant Professor of Economics at HKUST and HKUST IEMS Faculty Associate, examined the extent to which high- and low-productivity firms respond to trade liberalization (input tariff reductions) by upgrading product quality as captured by increasing export unit prices. Analyzing Chinese import tariff data, firm-level panel data, and product-level trade data from the World Trade Organization and China Custom's trade databases, she finds that when the scope for quality differentiation is small, the differences between low- and high-productivity firms diminish or even reverse. In industries with larger scope for quality differentiation, incumbent firms with lower initial productivity increase their export prices more under trade liberalization.

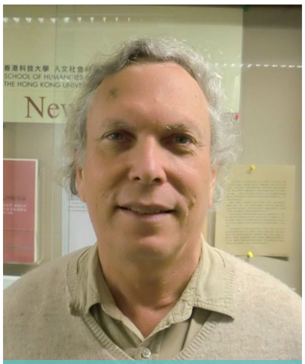
Other presenters at the conference included **Arpita Chatterjee** (University of New South Wales), **David Cook** (HKUST), **Jonathan Eaton** (Penn State University), **Charles Engel** (University of Wisconsin-Madison), **Edwin Lai** (HKUST), **Thierry Mayer** (Sciences-Po), **Jin Xie** (Chinese University of Hong Kong), **Vivian Zhanwei Yue** (Emory University), and **Jing Zhang** (Federal Reserve Bank of Chicago).

Video recordings, papers, and presentation slides available at
http://iems.ust.hk/econ

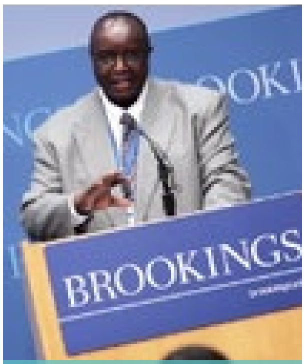
CHINA IN AFRICA: CHINA'S IMPACT ON AFRICAN EMPLOYMENT – WORLD BANK JOBS GROUP GOOGLE+ HANGOUT

(2015.02.23)

Haroon Bhorat



Barry Sautman



Mwangi Kimenyi

Stephen Golub

Exploring the role of China in Sub-Saharan Africa is a topic of increasing interest given China's ascendance and the fact that six of the world's top ten fastest growing economies are now found in Africa. These circumstances—plus an immense cache of natural resources in Africa and a rapid increase in the cost of labor in China—have led to heightened interest in Africa's potential to become the world's next major economic growth center.

Haroon Bhorat, Director of the Development Policy Research Unit (DPRU) at the University of Cape Town, moderated the discussion with a panel of experts including **Mwangi Kimenyi**, Senior Fellow in the Africa Growth Initiative at the Brookings Institution, **Stephen Golub**, Professor of Economics at Swarthmore College and Adjunct Professor at the Wharton School at the University of Pennsylvania, and **Barry Sautman**, Professor of Social Science at HKUST and HKUST IEMS Faculty Associate.

Prof. Sautman noted that, while China and Africa have been trade partners for over 600 years, trade between the two regions only began to take off since the 1990s. The level of investment is difficult to estimate because no one really knows how much of the money China moves through foreign banks actually ends up in Africa, but it is widely agreed that China's financial investment in Africa is only a small fraction of what China invests in the rest of the world.

Prof. Golub simplified the discussion by stating that, like any rational investor, Chinese investors are searching for profits, the most lucrative of which are likely to be found in manufacturing industries. There is no shortage of entrepreneurs in Africa and China, he stated, and the Chinese are expert exporters. Additionally, Africans have a great need for manufactured goods. These goods are largely smuggled as uncovered in Prof. Golub's extensive research on Chinese trade with the African countries of Nigeria and Benin.

While Prof. Sautman also pointed out that Chinese investment in infrastructure in Africa is quite substantial, there is relatively little investment in manufacturing. Oil and minerals, so-called primary products, offer a huge potential for international entrepreneurs, and Africans are beginning to be cautious about how their resources are distributed worldwide. Concurring with Prof. Golub's earlier assessment, Prof. Sautman further stated that, while China grew through manufacturing and growth, manufacturing is becoming less competitive in China, Africa may indeed provide China with opportunities in manufacturing.

The conversation became more animated when Prof. Bhorat asked Dr. Kimenyi about the possible threat to the U.S. economy of this type of China-Africa partnership, who noted that high-ranking American officials are regularly critical of China in Africa. American officials have repeatedly warned Africans that China may take resources from Africans without providing employment opportunities for locals, and rather may be importing the majority of their labor force from China (see opposite page for Prof. Sautman's criticism of this claim). Ultimately, however, both the U.S. and China really just want access to Africa's mineral resources.

Prof. Sautman advanced the conversation with discussion of the cultural constraints that may be slowing the development of China's economic relationship with Africa. Chinese people generally do not speak Portuguese or French, nor do they practice African religions like Islam and Christianity. Although these cultural constraints cannot be ignored, there is a new trend among young Chinese people to move to Africa to start families and businesses. Moreover, a relatively large number of African-born ethnic Chinese are now coming of age. There are also thousands of Africans living and working in China. While Americans look to Africa as a place to begin businesses, they do not seek to assimilate with the population to the same extent as many Chinese do. As Prof. Sautman speculated, this may ultimately prove to be the reason why China wins in Africa.

Prof. Golub concluded the discussion on the topic of Africa's problems in infrastructure—such as regular power outages, protectionism, and unregulated trade—which provide challenges for Chinese investors. Ultimately the question for African leaders is simple: will the China-Africa relationship create jobs and opportunities for Africans in Africa? While Prof. Golub does not seem to think so, the other speakers were more optimistic.

Video recording available at
http://iems.ust.hk/hgot

LOCALIZATION OF CHINESE ENTERPRISES IN AFRICA

HKUST IEMS Academic Seminar (2015.02.09)

On the question of whether Chinese enterprises in Africa contribute to employment by localizing workforces, **Barry Sautman**, Professor of Social Science at HKUST and HKUST IEMS Faculty Associate, critiqued the myths surrounding Chinese enterprises in Africa, in particular that these firms have failed to significantly integrate themselves into local African economies.

Contrary to much of the mainstream discourse on the subject, Prof. Sautman's field studies of dozens of Chinese enterprises in various African countries such as Ethiopia, Zambia, Namibia, and Kenya, as well as his in-depth analysis of over 400 Chinese enterprises and projects in Africa, all indicate that Chinese enterprises in Africa are often highly localized, and are becoming increasingly so over time.

While the vast majority of Chinese enterprises in Africa had workforces comprised of at least 80% local workers, Prof. Sautman cited a few standout industries on both sides of the spectrum. Chinese enterprises with the lowest rate of local African employees (with local employees comprising 50-65% of the total workforce) were in the telecommunications industry, where host countries suffered an acute shortage of qualified engineers and technicians. On the other end of the spectrum, Chinese enterprises involved in extractive industries, manufacturing, and construction often had over 90% of their workforces localized, with some even exceeding 99% such as Kiluwa Mining Group in Tanzania, Akosombo Textiles in Ghana, and Beijing Geophysical Prospecting in Nigeria.

To facilitate further localization, Prof. Sautman recommends that African states further systematize their approach to the localization of Chinese and other foreign enterprises, so that these enterprises can more easily expand their businesses in Africa. Chinese enterprises themselves should also increase their labor standards by increasing pay and providing better working conditions, in order to close the gap with other foreign enterprises in Africa who can and do offer higher wages, benefits, and working conditions as a result of their higher profitability and longer experience in Africa. Finally, African governments can further local employment by encouraging Chinese companies to increase their investment in labor-intensive manufacturing and service sectors which currently enjoy the highest proportion of localization.

Video recordings available at
http://iems.ust.hk/afrb

GOVERNMENT OFFICIALS' POLITICAL INCENTIVES, THE STATE'S BUREAUCRATIC CAPABILITY, AND CORPORATE DIVERSIFICATION IN AN EMERGING ECONOMY

HKUST IEMS Academic Seminar (2015.04.13)

Ever since Deng Xiaopeng initiated a decades-long process of market reforms, China's formerly Communist economic system has gradually become more and more capitalist in nature. Simultaneously, Chinese bureaucrats have also become increasingly accountable for generating economic growth in their jurisdiction, sometimes at the expense of social stability.

On this issue of emphasizing economic growth vs. social stability, **Danqing Wang**, Assistant Professor of Strategy and International Business at the University of Hong Kong, spoke on her research into how a given bureaucrat's career-level and career concerns affects their choice of policies, based on data she assembled from the resumes of all of China's provincial leaders serving as "Party Secretary" or "Provincial Governor" during the years 2001-2008.

Prof. Wang analyzed their career trajectories in relation to the performance of over 2,000 firms in their jurisdictions during the same time period. She posits that when there are large numbers of laid off workers, leaders pursuing social stability will encourage local firms to acquire failing state-owned enterprises, often in new industries.

The most intriguing finding of Prof. Wang's research is that retiring government bureaucrats prioritize social stability far more than bureaucrats with a long career ahead of them, indicating that promotion incentives for Chinese bureaucrats favour economic growth far more than social stability. Another finding is that a government official's length of tenure has a strong positive effect on his ability to mobilize businesses to pursue activities leading to greater social stability. In addition, private Chinese firms with executive managers who belong to the Chinese Communist Party's People's Congress and/or Political Consultative Conference are much more likely to enter new industries unrelated to their core competency presumably to help promote social stability.

Video recording available at
http://iems.ust.hk/dngq

BUSINESS AND WEALTH IN RUSSIA AND CHINA

SKOLKOVO-HKUST Joint Workshop (2015.03.09-10)

The Moscow School of Management (SKOLKOVO) and HKUST IEMS co-organized a 2-day joint workshop at HKUST covering four key themes: wealth possessors in Russia and China; entrepreneurship in Russia, Hong Kong, China's Pearl River Delta Region; microfinance in Russia, China, and India; and business education for the future.

Ruslan Yusufov and **Marianna Slutskaya**, both with the SKOLKOVO Wealth Transformation Center (SWTC), presented findings from a recent survey of dozens of Russia's wealthiest business owners. One of the most interesting results was that only 20% of respondents involved children and relatives as business managers, which indicates that nepotism is not as large a factor in Russian family businesses as many may believe.

Roger King, Director of the HKUST Tanoto Center for Asian Family Business and Entrepreneurship Studies, and **Winnie Qian Peng**, Associate Director of the Center for Asian Family Business and Entrepreneurship Studies at HKUST, presented their research findings countering the ancient Chinese adage, "Wealth does not go beyond 3 generations." In China, family succession of firms is much more common than in Russia, with some succeeding beyond three generations. Based on their case study research, Drs. King and Peng concluded that the 3 major success factors for Chinese businesses to endure past 3 generations of family ownership were having a sustainable business model, maintaining a balance between Western and Eastern values, and an occasional pruning of high-level management.

Steven Lee, Director of the HKUST Entrepreneurship Center, discussed his observations on the current state of entrepreneurship in Hong Kong and China's Pearl River Delta. Along with a strong desire of most educated local youths to seek stable employment in large companies as opposed to starting a business, Dr. Lee stated that Hong Kong's astronomical housing costs are a main factor in the recent decrease in the "quality" of the Hong Kong's entrepreneurial pool. In contrast, in Beijing and the Pearl River Delta region, entrepreneurial interest amongst local youths is incredibly high, buoyed by support for such entrepreneurial activities from both private enterprises and the government at municipal, state, and federal levels. Venture capitalists thus have flocked to the region, investing heavily in start-ups in areas such as precision manufacturing, robotics, and automation.

Vladimir Korovkin, Head of Digital Research at SKOLKOVO IEMS, presented research on Russian attitudes toward China based on a textual analysis of a sample of over 16,000 Russian social media followers commenting on topics involving the two countries. Generally speaking, Russians have a positive attitude towards the Chinese, with increasing discourse on Russia using China as a "replacement for the West". Dr. Korovkin stated that this rhetoric increased substantially after the Ukrainian-Russia conflict and the resulting US and EU sanctions against Russia.

On the topic of microfinance, presentations were given by Dr. Korovkin on the future of microcredit in Russia; **Albert Park**, Director of HKUST IEMS, on the impact of microfinance on poor villages in China; and **Sujata Visaria**, Assistant Professor at the HKUST Department of Economics, on how to improve the effectiveness of microfinance schemes in rural India. Today most microcredit in Russia and some in China is profit-oriented. India and China also have a diversity of microfinance programs led by NGOs or government agencies that pursue poverty alleviation.

SKOLKOVO's **Andrey Shapenko** and HKUST Business School's Associate Dean **Sean Ferguson** offered their insights on the future of business education, with both agreeing that the future may see less emphasis on traditional MBA programs and more emphasis on blending careers and education, for example through part-time programs. Successful business schools must continuously assess how their programs can better create real value for their students in both the short and long term.

Video recordings, papers, and presentation slides are avaiable at
http://iems.ust.hk/skol

CAN THE BEAR AND THE DRAGON BE BOSOM BUDDIES?

Forum on the Current and Future State of Sino-Russian Relations (2015.04.20)

Held at HKUST Business School Central in Central, Hong Kong, the forum started with remarks by **David Zweig**, Professor in the HKUST Division of Social Science, Director of HKUST's Center on China's Transnational Relations, and HKUST IEMS Faculty Associate, who emphasized the timeliness of the topic as China continues to rise as a world power, Russia's President Vladimir Putin makes efforts to look eastward to expand the country's sphere of influence given recent tensions with the West, and as American and EU policymakers debate how to respond to Russian aggression even as Europe struggles to manage economic crises and recovery.

Shaolei Feng, Dean of the School of Advanced International and Area Studies at East China Normal University, offered his insights into the Russia-Ukraine crisis. Western sanctions have brought many difficulties to Russia, but do not seem to have led to a resolution to the core issue of Russian aggression. Prof. Feng pointed out that China has sought to maintain constructive relationships with Russia and the West and has taken the position that, while Ukraine has a right to territorial sovereignty, its history involving Crimea is "complicated".

On the topic of the scope and limits of the Sino-Russia relationship, **Jeremy Paltiel**, Professor in the Department of Political Science at Carleton University, offered an explanation for why the BRICS countries seem to support Russia while the G7 tend to support Ukraine with respect to the Crimean conflict, the primary reason being that BRICS countries have initiated a soft alliance acting as a counter-balance to the G7. This understanding informs Sino-Russian relations as China, by and large, attempts to take a neutral stance on conflicts between Russia and its former Soviet Union-era territories.

Providing a Russian perspective to the discussion, **Elaine Sushkova**, Research Lead at the Asian Studies Center at the Moscow School of Management SKOLKOVO's Institute for Emerging Market Studies, expressed her view that Western sanctions against Russia after its annexation of Ukraine accelerated the development of economic ties between China and Russia as seen in the more than 40 business agreements across a variety of sectors signed after the sanctions came into effect. Dr. Sushkova also felt that, while Russia needs China as an economic and political ally, China does not need Russia nearly as much. On this note, Dr. Sushkova pointed out the trade balance between the two countries is trending in such a way that China's need for Russia is largely stagnant while Russia's reliance on Chinese imports, investment, and other business related activities is increasing at a rapid pace.

Russia's increasing business activities with China are not without obstacles, however. As Dr. Shushkova detailed, the biggest challenge to Russia further strengthening its economic ties with China is that, despite China's close proximity, after the end of Soviet Union, Russian businesses tended to seek partnerships with Western companies, resulting in a dearth of experience working with China and a wide cultural gap between Russian and Chinese businesses.

Also speaking was **Baohui Zhang**, Director of the Centre for Asian Pacific Studies at Lingnan University, on whether Beijing and Moscow shared the same strategic aims in light of recent geopolitical shifts. China and Russia currently have a number of overlapping, long-term strategic goals. While many scholars believe a large degree of mistrust exists between the two nations, a lack of trust which may eventually corrode their ties, Dr. Zhang instead thinks that the countries will continue to have close ties, as many public opinion surveys indicate a high degree of solidarity between the citizens of each country. Dr. Paltiel agreed with Dr. Zhang, adding that as Russian economic fortunes fade and as Russian leadership moves further and further away from the West, Russia will see China as an increasingly indispensable economic and strategic partner.

The half-day forum was co-hosted by HKUST's Center for Transnational Relations, HKUST IEMS, the Moscow School of Management SKOLKOVO's Institute for Emerging Market Studies, and the Center for Asia and Pacific Studies at Lingnan University.

Video recordings available at
http://iems.ust.hk/cctr

REGISTRATION STATUS, OCCUPATIONAL SEGREGATION, AND RURAL MIGRANTS IN URBAN CHINA

HKUST IEMS Academic Seminar (2015.03.23)

Xiaogang Wu, Director of the Centre for Applied Social and Economic Research (CASER) at HKUST and HKUST IEMS Faculty Associate, presented his research on income inequality in urban Chinese cities as related to China's urban-rural household registration ("hukou") system. His research focuses on the question: why do some occupations in urban China pay more than others?

Although there have been many studies pointing out the earnings disadvantages of rural citizens compared to their urban counterparts, Prof. Wu's study is unique in that it differentiates between social exclusion based on hukou status and direct wage discrimination. Using comprehensive data from China's 2005 mini-census, Prof. Wu analyzed the disadvantage of being a rural migrant by estimating linear regression models for the determinants of workers' earnings to test whether having a rural hukou increased or decreased earnings after controlling for education, experience, and gender. He further tested both within-occupation and between-occupation pay differences for workers with urban versus rural hukou status.

Surprisingly, within a given occupation, Professor Wu's results showed that, in the private sector, rural migrants earn even more than locals, perhaps because they work longer hours or are more willing to take extra wages instead of other benefits. However, rural migrants were found to work in lower-paying occupations on average, likely due to government regulations denying them equal access to some jobs. Thus, Professor Wu concludes that rural workers are disadvantaged primarily because of occupational segregation as opposed to within-occupation discrimination.

While Chinese policymakers are making progress in loosening some of the more burdensome restrictions of the hukou system, Prof. Wu stated that future reforms to China's hukou system should focus on the reduction in hukou-related occupational segregation, and the removal of other social barriers hindering rural migrants from gaining equal access to occupations and social services.

Watch Prof Wu explain the key takeaways from his seminar at
http://iems.ust.hk/xggw

2015: IS CHINA ABOLISHING THE HUKOU SYSTEM?

HKUST IEMS Academic Seminar, co-organized with the Division of Social Science (2015.03.16)

Kam Wing Chan, Professor of Geography at the University of Washington and a leading expert on China's urban-rural household registration ("hukou") system, presented his views on the current state of China's hukou system and its potential for reform.

Prof. Chan began his talk with a short history of China's hukou system, which has been in place since the 1950s, beginning as a form of systematic segregation between rural and urban populations to solve demographic and logistical problems. This early form of the hukou system controlled not only physical migration but also a person's opportunities in general, as persons without an urban hukou were prohibited from the higher-quality jobs, education, and government benefits found in China's urban areas.

On the question of the abolishment of the hukou system, Prof. Chan does not see the hukou system being repealed or replaced any time soon, even if it does appear to be getting less and less strict over time. Prof. Chan stated that, while the modern-day hukou system does indeed allow some rural citizens to work and live in urban areas, the system still prevents them from receiving the basic social services offered to urbanites.

As Prof. Chan succinctly put it, these migrants to urban areas "are in the city, but not of the city". In no other aspect are these distinctions more evident than with issues concerning children. To illustrate this point, Prof. Chan quoted a portion of China's official hukou policy, which states that "all migrant children are our children, but don't really belong…They should return to their hometowns to have their education." This, along with urban-rural cultural differences, has led to unrest and even violence.

To the central government's credit, however, recent actions and policies issued by the central government in Beijing seems to indicate that China's policymakers realize that the hukou system is unsustainable, and will have to be gradually phased out. Modern technology is allowing cities to sustain levels of growth that were impossible fifty years ago, and efforts to better integrate and assimilate rural migrants into urban areas may help ease the transition to a hukou-less society.

That said, while Prof. Chan is pessimistic that China will dispose of the system in the near future, he's nevertheless optimistic that reform will happen in a fashion unique to the Middle Mingdom: slowly, but surely.

Find out more about the event at
http://iems.ust.hk/kmwg

OWNERSHIP-SPECIFIC HUMAN CAPITAL AND THE EMPLOYMENT GENDER GAP IN URBAN CHINA

HKUST IEMS Academic Seminar (2015.05.07)

Christina Jenq, a Post-doctoral Research Fellow at HKUST IEMS and the HKUST Jockey Club Institute for Advanced Study, presented her research on the growing inequality in wages and employment outcomes in urban China over the past two decades. This growth in inequality has coincided with the restructuring of China's state-owned enterprises (SOEs) and other reforms affecting the urban labor market.

Before these reforms, wage and employment inequality in urban China was relatively low. Virtually all urban enterprises were state- or collective-owned. Moreover, the labor market was centrally regulated, making it nearly impossible to fire unproductive workers. However, following reforms in the 1990s, inequality—and gender inequality in particular—increased significantly.

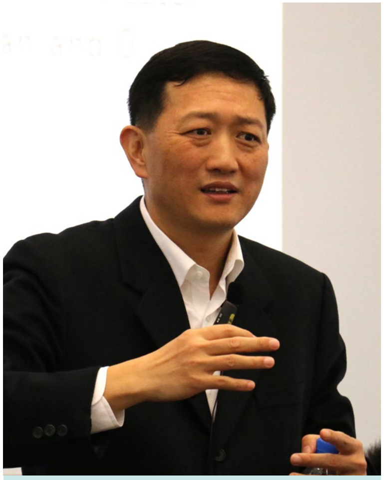
Dr. Jenq's research focuses on the impact of widespread privatization of state-owned enterprises on rising gender inequality. In her analysis, Dr. Jenq exploited regional variation in the composition of industries in China to analyze the causal effect of the privatization rate (which varied across industries) on changes in the gender gap in urban employment, and used a multivariate regression analysis using a carefully chosen set of controls.

Based on the results of her analysis, Dr. Jenq postulates that 30-50% of the increase in gender imbalance in urban employment can be explained by gender-asymmetric industry-level privatization. Dr. Jenq cautions against quota-based employment policies aimed at reducing the employment gender gap (as there was scant evidence of gender discrimination found in her analysis), and instead recommends increases in both skill training programs as well as childcare and education benefits to allow more urban women the opportunity to enter the labor force.

Dr. Jenq's research on the employment gender gap in urban China has also been featured as an HKUST IEMS Thought Leadership Brief (see link below), which provides further detail on her methodology, findings, and policy recommendations.

Watch Dr Jenq explain the key takeaways from her Thought Leadership Brief at http://iems.ust.hk/chrq

OTHER ACADEMIC SEMINARS



2015.02.16

Once an Enemy, Forever an Enemy? The Long-run Impact of the Japanese Invasion of China from 1937 to 1945 on Trade and Investment

Zhigang Tao (University of Hong Kong)

* Video recording available at http://iems.ust.hk/zhig

2015.03.02

Is the PDS Already a Cash Transfer? Rethinking India's Food Subsidy Policies

Sujata Balasubramanian (HKUST)

* Video recording available at http://iems.ust.hk/sujb

2015.05.04

The Structure of Economic Globalization: It's a Small World After All

Joon Nak Choi (HKUST)

* More about the event at http://iems.ust.hk/jcgl

HKUST IEMS is proud to announce the launch of its new Working Paper series, featuring the latest academic research papers written by our Faculty Associates and visiting speakers, covering a wide range of topics and disciplines. The series is registered online with the Social Science Research Network (SSRN) and Research Papers in Economics (RePEc) databases, increasing the reach and visibility of the Institute's research.

See all the papers at
http://iems.ust.hk/wp

TWO NEW FACULTY ASSOCIATES JOIN IEMS

IEMS welcomes two new Faculty Associates: **Jean Hong** and **Alminas Zaldokas**.

Jean Hong, Assistant Professor of Social Science at HKUST, earned her PhD from New York University, and is an expert on comparative political economy, authoritarian regimes, and East Asian politics.

Alminas Zaldokas, Assistant Professor of Finance at HKUST, received his PhD from INSEAD, and is an expert on corporate governance, family firms, innovation, and corporate finance. He's also the recipient of a 2015 HKUST IEMS research grant on the topic of product market response to corporate governance shocks in India.


Alminas Zaldokas


Jean Hong

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