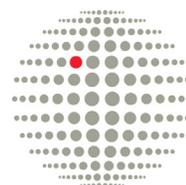


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NEW YORK & CHINA

Building a Global Partnership



Partnership for New York City

INTRODUCTION

China's emergence as an increasingly important player in global economic and technological affairs offers exciting opportunities as well as challenges for the United States. While much of America is focused on defending its job base and competitive advantage against China, both the government and business leadership in New York City and State are seeking to build economic development relationships with China and its emerging private sector. For New York, globalization is widely recognized as an opportunity rather than a threat, and China—along with India, Mexico, Brazil and Russia—is being pursued as a customer, client, investor and global partner.

China's economy has tripled in size since 1980 and continues to grow by an average of nine percent annually.ⁱ Currently, it is the world's third largest exporter and fourth largest economy.ⁱⁱ If these trends continue, on an overall GDP basis, China is projected to be the world's largest economy by mid-century.^{iii, iv} China's rise is simply one manifestation of the structural changes in the world economy associated with globalization.

During the past two years, the Partnership for New York City has worked with city and state officials to lay the groundwork for New York's emerging role as the U.S. center of Chinese commercial interests. A centerpiece of this effort is a "China Center," proposed to be an anchor tenant at the new World Trade Center. The China Center—a business and cultural facility representing China's dynamic business community—will serve as a hub for Chinese companies locating offices in New York and for international and U.S. firms interested in relationships with China. A successful economic development relationship between New York and China has the potential to bring billions in new revenues and to create thousands of jobs in New York—at all levels and across many industries.

Industries that are most central to the New York economy—financial services, insurance, professional services, media, tourism and, increasingly, science and information technology—are increasingly looking to China for future growth. New York-based companies in all these sectors must capture a major share of business opportunities emanating from China if the city and region are to remain the global center of commerce. Yet competition for China's business has become increasingly intense—in the U.S. and around the world.

Furthermore, New York is not a free agent. Its success in cultivating a mutually beneficial relationship with China depends on public policy decisions that are largely the prerogative of the federal government and international bodies. Trade, immigration, security, currency and intellectual property decisions made by both the U.S. and Chinese governments will set the parameters of business and trade relationships that New York City and State are able to establish with China and Chinese businesses. This paper outlines the current status of New York's relationship with China and suggests a "New York position" on important policy issues that need to be resolved in order for New York to:

- Maximize the benefits of a relationship with China;
- Compete with other localities to become the Western headquarters location of Chinese companies that are entering global markets; and
- Reinforce preferred customer relationships between New York-based international firms and China.

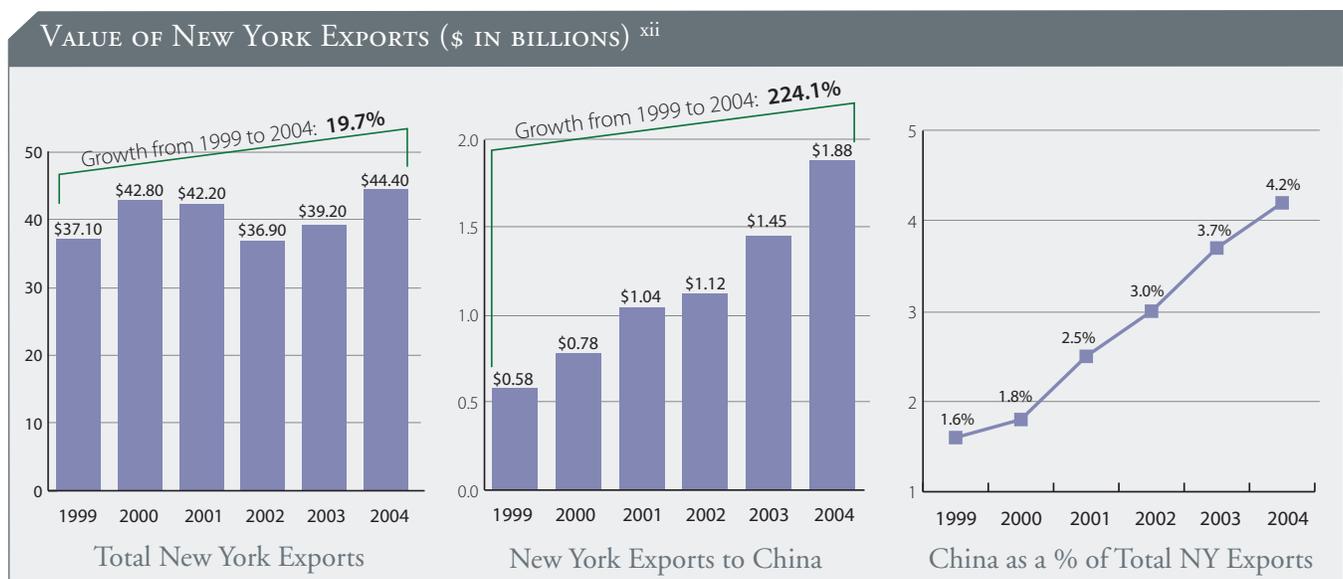
THE NEW YORK-CHINA RELATIONSHIP IS ALREADY STRONG

The New York Metropolitan Region is home to more than half of the 32 largest Chinese companies with offices in the U.S.^v Chinese companies locating in New York represent a broad array of industries including shipping, steel, energy and manufacturing firms, as well as those in the services sector. Many have chosen to open headquarters in New York in anticipation of eventual listing on the respective New York stock exchanges and entering U.S. capital markets.

The number of Chinese companies accessing the U.S. public capital markets has risen dramatically in recent years. For the period of 2001 through the second quarter of 2004, approximately \$60 billion of equity and debt issued for Chinese companies has been in the U.S.^{vi} By the end of 2005 there were already 17 Chinese companies listed on the New York Stock Exchange and 30 on the NASDAQ. Of these 47 companies, 15 have a U.S. presence and five of those are in New York.^{vii} In addition, in 2005, seven Chinese companies had IPOs on the NASDAQ.^{viii}

New York has a wealth of other advantages that attract Chinese firms and Chinese nationals. In addition to the known draws of New York City—including a high concentration of businesses with a significant presence in China, a strongly branded identity in China and the nation’s largest urban Chinese population (over 370,000)^{ix}—New York’s tax code differs from many other states in ways that substantially reduce the effective tax rate for many corporations, particularly foreign firms setting up U.S. headquarters. No other city or state in the country has as favorable a method of taxing investment income.^x Such incentives—compounded with the hub for Chinese culture, commerce, and migration that New York City has become—can play a critical role in strengthening relations between New York and Chinese businesses.

New York City currently boasts seven Chinese daily newspapers, two Chinese language television stations, and the largest Chinese neighborhood in the country. New York area airports provide 12 daily flights to Hong Kong and five to Beijing, the most flights out of the eastern half of the United States.^{xi} These resources facilitate business with all of New York State, and are important considerations



for Chinese firms expanding into global markets as well as for domestic firms doing business with China.

New York State is also increasingly reliant on China as a consumer of services and manufactured goods. In fact, China was New York's leading growth market over the past five years (see chart on previous page).

Since 1999, New York's net dollar increase in exports to China has been higher than that of any other international market. With manufactured machinery as its top export category to China, New York State's exports to China grew by 29 percent from 2003 to 2004, compared to national growth in exports to China of 22 percent.^{xiii}

FUTURE OPPORTUNITIES FOR NEW YORK & CHINA

As important as China is to New York today, it will become even more so in the future. For example, China is the largest trading partner for the seaport of New York and New Jersey, accounting for 20 percent of the port's activity in 2004—a 30.5 percent increase over 2003 trade volumes. Given the pattern of recent years—increases of over 20 percent each year since 2001—it is expected that the tons of Chinese cargo flowing through the port will continue to increase.^{xiv} Importantly, two-thirds of the employees of the China Ocean Shipping (Group) Company (COSCO), China's biggest shipping company, are Americans.^{xv}

Governor George Pataki returned from a trip to China in late 2005 that was specifically focused on increasing trade and investment opportunities between China and New York State. One result from this trip is that the Empire State Development Corporation will soon open an office in China to facilitate this increase in trade and

investment.^{xvi} Earlier this year, the State University of New York also opened an official liaison office in Beijing to coordinate student recruitment and facilitate research collaboration among U.S. and Chinese experts. The Levin Institute at SUNY has established China as a priority in its graduate and professional education programs. In addition, the New York City Economic Development Corporation recently hired a business executive who is dedicated to attracting Chinese businesses.

The size of the Chinese market presents an opportunity for New York companies to capitalize on economies of scale to bring down costs and develop new and innovative technologies. U.S. companies in the Metropolitan Region that are already seizing this opportunity include: General Electric, IBM, Eastman Kodak, Corning, Pfizer, Bristol Myers Squibb, and Bausch and Lomb (see box on the next page).

Manufacturers are not the only New York firms that have found a significant market in China. The second largest foreign insurer in China, the first foreign bank to open its doors to Chinese customers, and the largest accounting firm in China are all New York-based companies. The firm with the leading market share in traditional voice and data services between the U.S. and China, the first and second ranked leaders of Chinese equity offerings, and one of the largest foreign pharmaceutical enterprises operating in China are also all New York-based.

In addition to being a leading growth market for New York State's services and manufactured goods, China is also an important source of future tourism for New York. The U.S. Department of Commerce estimates there are currently 40 million people in China with the financial ability to travel overseas; this number is expected to surge to 100 million by 2020.^{xvii} With the second greatest market share of Chinese visitors to U.S. cities, New York stands to gain significantly

if the U.S. is granted “Approved Destination Status” (ADS) by the Chinese government.^{xviii} Such status is required in order for Chinese citizens to travel to a country as a tourist—currently only those Chinese citizens coming to the U.S. for business, education or in a governmental capacity are allowed to travel freely with a visa. A Memorandum of Understanding regarding the granting of ADS to the U.S. has been signed and it is projected that once the U.S. is added to the list, New York—and New York City, in particular—will be a top destination for group tours by Chinese tourists.^{xix} Among U.S. cities, Los Angeles currently holds the greatest share of the Chinese tourist market with 28.8 percent, followed by New York City with 27.3 percent, and San Francisco with 24.1 percent.^{xx} If Chinese tourists follow current visitor spending patterns, an increased volume of Chinese tourists would have a significant

impact on the New York economy. International visitors to New York City make up only about 15 percent of overall visitor volume, but account for 40 percent of all visitor spending.^{xxi}

NEW YORK FACES SERIOUS COMPETITION FOR CHINESE TRADE AND INVESTMENT

As the world’s fourth largest economy and third largest exporter (behind Germany and the United States),^{xxii} China is actively looking for opportunities to trade and invest around the world. New York must seize these opportunities or face the prospect of sitting on the sidelines while other regions, both domestically and internationally, capitalize on the increased number of jobs and improved economic output.

CONSUMER MARKET IN CHINA PRESENTS A MAJOR OPPORTUNITY FOR N.Y. BUSINESS

- China is the second largest energy consumer in the world, surpassed only by the United States. It is the largest user and producer of coal, second largest consumer of petroleum, and Chinese consumption of natural gas is expected to double by 2025. In order to diversify and fill growing needs, China is moving aggressively to boost energy from renewable sources. GE Energy has already built wind turbines all over the country. In the next five to 15 years, the wind power industry is expected to grow more than 100 percent per year in China.*
- Chinese consumption of high technology, and personal computers specifically, is rapidly expanding. China continues to drive a significant share of growth in the PC market. In fact, 45.7 percent of the total PC units expected to ship in 2005 are China-bound. IBM accounts for a 45 percent share of the Chinese market for business computers—its largest market globally. Earlier this year, Lenovo—a Chinese company—acquired the PC division at IBM. The Chinese government announced in November 2005 that it would purchase more than \$20 million worth of computers from IBM, providing IBM with the largest Unix installation project in Asia.**
- China’s photographic film and paper market is one of the world’s largest. Although Eastman Kodak only began exporting products for sale in China on a major scale in the mid-1990s, it already claims a majority share of the Chinese roll film market. In its process of shifting focus towards the digital film industry, Eastman Kodak has been able to continue making sales of traditional cameras and roll film in markets such as China’s secondary cities, towns, and vast rural areas that are home to more than one billion people. China’s demand for such products that are declining in the U.S. consumer market has helped to soften the transition in technology development and bolster the stability of upstate manufacturing firms.***

* Source: Energy Information Administration; U.S. Department of Energy.

** Source: May 1, 2005 Press Release, IBM.

*** Source: Levin Graduate Institute; BBC News, Brighter Future for Eastman Kodak, April 21, 2004; china.org.cn, Kodak’s China Strategy Not Black-and-White, May 10, 2004; Digital Photography Review, Kodak to stop making APS, some film cameras, January 13, 2004; EastmanKodak 2004 Summary Annual Report.

As the tourism example illustrates, New York is competing with other regions in the U.S. for the jobs that increased Chinese economic activity will bring. Other states, including South Carolina, have already made strides in recruiting investment from and fostering trade relationships with China. South Carolina not only has an economic development officer who speaks fluent Chinese, but in October of this year, the South Carolina Department of Commerce opened a trade office in Shanghai. Chinese investment in South Carolina now totals \$126 million and has created 1,250 jobs in the state. The Haier Group, a manufacturer of appliances and electronics, has its U.S. headquarters and 110 employees in Manhattan. It also employs 200 people at its plant in South Carolina. Haier has already invested at least \$75 million in the United States and has plans to open four more new U.S. factories. This expansion could translate into future jobs for New York State; however, other states like South Carolina, which has already given more than \$250,000 in incentives to Haier, will be competing for this business.^{xxiii}

In November 2005, California Governor Arnold Schwarzenegger visited China with a delegation of nearly 80 California business leaders, including representatives from Universal Studios, Qualcomm, Walt Disney, and Chevron Global Gas, in the hopes of luring more Chinese firms to the West Coast and increasing California exports to China. Because of its geographic location, California is the most accessible gateway to U.S. trade with China and remains a key competitor to New York as a result.

The most formidable competition, however, is not within the U.S. but from London, which is closer to Beijing and has the added benefit of having its business day overlap with both Beijing and New York. London is competing aggressively for business and trading relationships. London's efforts reflect an overall attempt by the European Union to

develop a more intimate economic and technological relationship with China. London has opened offices in Beijing and Shanghai in order to foster closer ties and encourage Chinese firms "going global" to settle in London.^{xxiv} In addition, the London Stock Exchange recently opened its Asia Pacific headquarters in Hong Kong and has developed relationships with both the Shanghai and Shenzhen exchanges. As the Beijing Summer Olympics of 2008 makes way for London in 2012, this is likely to advance London's relationship with China and Chinese tourism.

HOW THE FEDERAL GOVERNMENT IMPACTS THE NEW YORK-CHINA RELATIONSHIP

The biggest obstacles to Chinese expansion and investment in New York are political in nature and related more to U.S. foreign policy, rather than to New York's cost of doing business or cost of living, which are comparable to other world cities.

Onerous Financial and Accounting Regulations

Currently, there are six Chinese firms listed on the London Stock Exchange (LSE), but that number is expected to rise with the opening of the LSE Hong Kong headquarters.^{xxv} Regulations emanating from the Sarbanes-Oxley Act of 2002 are making it tougher for New York and the U.S. to compete for this business. Corporate governance laws and restrictive listing requirements are disadvantaging the U.S. in the competition for foreign international business.

Tariffs and Restrictive Trade Policies

The U.S. trade deficit with China (\$161.9 billion in 2004) continues to increase, but the often hidden context is that overall U.S.-China trade has expanded by the largest margins in a decade—in both directions. U.S. exports to China grew by 23 percent between 2003 and 2004, and in agriculture and trade

services, the U.S. actually ran a surplus with China in 2004. Today, China accounts for roughly 13 percent of U.S. imports, while the EU accounts for 19 percent.^{xxvi} China's average tariff rate dropped to 9.4 percent from 10.4 percent on January 1, 2005 and tariffs on products such as computers, semiconductors and telecom equipment dropped from an average of 13.3 percent to zero.^{xxvii}

The challenge to the U.S. and China is to avoid imposing protectionist tariffs or import quotas, and move instead toward policies that reinforce domestic strengths. For the U.S., key areas for concentrated investment include technology and life sciences. The need for academic cooperation will increase in these fields especially at a time when U.S. universities are producing fewer native-born engineering graduates than 20 years ago; and Chinese universities are now producing 300,000-plus engineers every year.^{xxviii}

Immigration and Cumbersome Visa Regulations

Increased attention to homeland security has led to more restrictive visa policies. Currently, international business travelers face excruciatingly long waits in order to obtain visas. These regulations are leading to delays and cancellations for travel to the U.S. The result has been damaging to U.S. global competitiveness and is making it difficult to move employees around the world. Setting up a preferred business traveler program could help ease travel restrictions that hinder global businesses. Similarly, cumbersome visa regulations restrict the flow of foreign students and faculty that are vital to U.S. research and academic institutions. As a result, many of the best and brightest foreign talent is heading to other countries.

Impact of Chinese Government Policy

The Chinese government also has many policies and practices that limit economic development relations with the U.S. Bureaucratic hurdles for investment and

business activity in China, deficiencies in protection of intellectual property rights, continued limitations on personal freedom and freedom of the press, and human rights abuses are all issues that make global partnerships more difficult. Improvements in these areas would provide businesses with the stability and certainty they need to make investments that will lead to economic growth for both nations.

CONCLUSIONS

China has been New York's leading growth market for exports over the past five years and will continue to be an important consumer of the services and manufactured goods produced by New York companies—but only so long as national policies encourage this relationship. If protectionism triumphs, New York will not be able to capitalize on its current advantage and become one of China's primary economic development partners. This would hurt New York and the rest of the U.S. while allowing other global cities and nations to capture the jobs and economic activity that China will provide in the coming years. Not only businesses, but educational, health care and cultural institutions in the New York region also stand to benefit from Chinese business relationships and tourism. All stand to suffer significant losses if U.S. and Chinese policies do not support these efforts.

New York already has strong ties with China and enjoys a growing Chinese contribution to its economy. While much of America sees China as an economic threat, New York is seeking a partnership that leads to mutual economic benefits. To achieve this partnership, New York's public officials, civic and business leaders must become the foremost advocates of laws and policies in the United States and China that support open and productive economic relationships.

ENDNOTES

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ABOUT THE PARTNERSHIP FOR NEW YORK CITY

With a mission to maintain the city's position as a global center of commerce, culture and innovation, the Partnership for New York City is an organization of the leaders of New York City's top corporate, investment, and entrepreneurial firms. They work in partnership with city and state government officials, labor groups, and the nonprofit sector to promote economic growth and address major challenges facing the City. Through its affiliate, the New York City Investment Fund, the Partnership directly invests in projects that contribute to job creation, economic development and other civic objectives.

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