

recent years, may find it very difficult to generate the revenues needed to maintain debt payments. If non-performing loans (NPLs) rise and force banks into contracting their activities, or if rising inventories cause companies to cut production and investment, the banking system might find itself in a spiral of rising NPLs and declining asset prices.

The second channel involves changing risk perceptions. In recent years, China has been the recipient of a great deal of speculative capital seeking to take advantage of its rising currency and expected growth rates. However, if either expected returns decline or, more worryingly, if risk expectations rise dramatically (or both), investors who brought money into the country may decide to withdraw it just as rapidly. The just-released PBoC reserve numbers suggest that China may have seen its first month of hot money outflows in September.

Most analysts who focus on the risk of speculative outflows dismiss the problem by arguing that given China's reserve levels there is little chance of an attack on the currency that leads to the sort of crises experienced by Asian neighbors in 1997. Yet that argument, while correct, misses a critical distinction. The danger China faces with speculative outflows is not that of a collapse in its currency, as was the case in countries like Thailand a decade ago. The real danger is that fleeing capital is likely to be withdrawn either from the banking system, putting liquidity pressure on the banks, or after the sale of assets, putting more downward pressure on asset prices.

The past two years has seen the global crisis develop rapidly and in unexpected ways. Although it has been hard to predict linear extensions of the crisis, it seems clear that there are underlying causes for which to look. Specifically, systems characterized by rapid monetary growth and overextended financial systems have been brought into the storm one after another. We will not know until after the fact how shaky China's financial system has become in recent years, but recent events should make bankers cautious.

Michael Pettis is a professor of finance at the Guanghua School of Peking University.

First-Rate Talent in Second-Tier Cities

Companies need a strong HR strategy to succeed in China's provinces

By Gregory P. Gilligan



AmCham-China members on a recent provincial trip to Hubei

The push among many businesses in China is to move beyond the traditional economic bases of the Pearl and Yangtze river deltas in the coastal areas is well underway. These advances have increased pressure on the labor market's capabilities and have been accompa-

nied by increases in competition for quality workers. It costs more and more to get the right talent and can be difficult for companies to keep the best workers. Projected year-on-year wage percentage increases for the near future at many large multinational companies are in the mid-teens. Adding in social cost (mandatory benefit)

AmCham Staff

increases can adjust those estimates up even further. For companies, making the best use of talent is critical to achieving business success.

Well-run companies, both multinational and domestic, know that making the most of China's opportunities now means finding growth in China's second and third-tier cities. For companies focused on exporting products from China, the smaller cities can represent more cost-effective solutions to traditional hubs (including incentive for investment and lower labor costs). For companies focused on the domestic market, rising disposable income in China's second and third-tier cities presents immense domestic sales and profit potential. In order for companies to make good use of these critical cities, they must have effective talent management and development strategies for these unique markets.

At McDonald's China, we operate nearly 1,000 restaurants in more than 190 Chinese cities. We enjoy tremendous opportunity for growth and profitability operating in second and third-tier cities. Our fundamental practice is to develop opportunities for both crew and managers. Our growth strategy in China's second and third-tier cities is the same as McDonald's worldwide plan: we look for restaurant management both from inside and outside the company. Indeed, a tremendous number of regional, country-level and global McDonald's leadership positions are held by former crew persons. Our experience shows the benefits of developing our local talent in China and putting them in a position to succeed.


There is a common misperception that China's talent pool, particularly in smaller markets, is somehow not modern or up to the task of running a multinational business. On the contrary, because of the enormous change in China's economy over the past few decades, most successful people here have become highly adaptive.

A more important criticism of China's labor force is that its entrepreneurial spirit makes it somewhat more mobile and less constrained than managers see in other countries. This is one of the many challenges to meeting human resource needs that companies see in China, particularly

in its second and third-tier markets. Yet these are the very markets that now offer so much potential.

It is good human resource policy to implement practices designed to attract, motivate, reward and retain talented and engaged people. To achieve such a well-rounded approach it is important to understand the workforce at a fundamental level. Along these lines, it is critical to remember that secondary (and tertiary) markets are all different. A September 17, 2008 *Wall Street Journal* article highlights regional differences in consumer attitudes as more determinant than "tiers" or city boundaries.

In the past it was easy to approach compensation strictly along these "tier" lines, but just as consumers vary in different regions, to be competitive it is also necessary to rethink compensation along geographic lines. In the area of benefits, there are indeed differences, dictated both by local regulation and by market forces, and they vary across regions. Those looking for efficiencies need to be able to navigate the local differences in social costs. Companies should investigate remaining competitive on basic salary at the regional level, while accounting for local differences by addressing varying social desires in a targeted and cost effective manner.

At McDonald's we have developed a strategy for second and third-tier cities that has worked for us. We have focused on attracting, motivating, rewarding and retaining talent. One of the critical components has been ensuring that inside advancement opportunity is on par with outside hiring opportunities. We emphasize the importance of creating a work environment that provides a real chance for upward mobility, regardless of a worker's geographical location. And finally, we make sure that we always have leadership teams in place that are skilled enough to give young talent the chance to succeed. When designing a human resources strategy for China's smaller cities, it is critical to make sure that your company has strong fundamentals in place. 

Gregory P. Gilligan is general manager of corporate affairs for McDonald's China.

Common mistakes that managers make dealing with challenges in secondary and tertiary labor markets:

- **Delegating the task of hiring to inexperienced managers.** This might seem like a common sense issue, but the danger is real. Time and financial resources can be wasted if an unknowledgeable or ill-equipped manager is making human resource decisions.
- **Failure to develop talent properly.** Assuming a company manages to hire the right people, it is critical to have the resources available to let them succeed. Specifically, regional leaders should be experienced managers. In addition, companies should make sure to provide the new talent with formal training opportunities such as meetings, classes and seminars like they would their employees in first-tier cities.
- **Failure to give second and third-tier city workforces equal opportunity for recognition and advancement or financial reward.** There should be a process in place so that top internal talent gets consideration for prime job openings in first-tier cities regardless of their current geographical location. Access to this type of opportunity can be an important tool for training regional leadership and can help drive continued growth through incentives. Additionally, as employees return back to their home provinces, they will bring with them greater experience and know-how.