Scratching the surface of the Chinese Government Procurement mountain

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Western firms, and European in particular, are looking increasingly east to revive their dormant profits. China's massive government procurement market seems like the ideal outlet to do just that. Nevertheless, foreign investors are still handicapped when competing in the Chinese government procurement giant

By Javier Delgado Rivera

Last year marked China's 10th anniversary of its accession to the World Trade Organisation (WTO), a development doomed to stir up the corridors of the body's headquarters in Geneva. Such a prediction has not let anybody down. One of the latest chapters of China's fussy dealings with its WTO partners was last year bid to join the body's Government Public Agreement (GPA) - a pact among 42 WTO member states easing the signatories' access to their respective Government Procurement (GP) markets.

This offer, the third since 2007, has been dismissed by GPA members on the grounds of its apparent poor scope and dismissal of most infrastructure ventures. "The list of covered services remains extremely limited and the Chinese offer explicitly excludes a number of important sectors… including civil aviation, ports, urban transportation, electricity, water resources, energy, postal services, and telecommunications," pointed out the EU *Chamber of Commerce in China in an exhaustive study of EU business bidding for public contracts in the country.* Some observers maintain that it deliberately prevents foreign firms from competing into the juicy arena of China's utilities.

A roadblock for investors

Against common wisdom, China is not that centralised when it comes to allocating its GP undertakings, as 80% is dealt at provincial and municipal level. The Chinese "central government has delegated approval authority for all foreign-invested projects below $100 million to local authorities," said two associates of Reed Smith, a global relationship law firm. The result is a sometimes two-levelled array of requirements, regulations and bidding procedures, making it a nightmare for foreign investors to keep path with potentially attractive business opportunities.

Futhermore, "there is no centralized platform [www.ccgp.gov.cn, the main online source, only covers central level tenders under one set of rules] to find out about new tenders... contracts can be announced on different media for different levels of government," warned the EU Chamber of Commerce in China.

Yet, even for a company capable to soak up the extensive collection of bidding outlets, submission deadlines are frequently so tight –Chinese firms often face the same time constrain- that the applicant has little room to grasp the underlying nature of the tendering, who more often than not ensues weak proposals.

In its study, the EU *Chamber of Commerce in China asked several EU companies about their key complains when competing in the Chinese GP market. The resulting findings may put prospective investors in the Middle Kingdom off. Even if a business proves to be competent and patient enough to handle the rough waters of the Chinese Public Procurement, the time and money invested run the risks to go wasted. A European manufacturer working in China stressed that "it is sometimes difficult to get detailed evaluation criteria"* of the bidding process. In many instances, the applying company is left clueless about what went wrong, unable to better outline prospective biddings. If the foreign business suspects that an irregularity has been committed, there is not a single, unified body through which channel an appeal against the disputed tendering conclusion.

The inherent complexity of a GP market worth nearly $1 trillion a year is regulated by two laws: the Government Procurement Law (GPL) and the Bidding Law (BL). Whether a tendering is regulated by one or the other depends on a series of factors: the value of the project, the industries covered, the end-users, scope, etc. This creates two parallel systems with, in some instances, overlapping definitions and conflicting provisions that binding companies frequently struggle to navigate through. For instance, under the GPL, a domestic product is one "made within China's borders and for which domestic manufacturing costs exceed a certain percentage of the final price," normally set at 50%. If the tendering offer falls under the BL, this proportion can go up to 70% of locally-generated value.

Keeping the cash cow at home

However, the most contentious single piece of policy regulating the Chinese GP market could easily be the Indigenous Innovation strategy – a scheme envisaged to boost home-grown technology. As overseas investors are more likely to employ foreign equipment in their manufacturing, such a policy is perceived as discriminatory to foreign enterprises. Referring to the rail sector, Philippe Citroën, Director-General of the European Rail Industry, put it bluntly: “In China no contract is signed without technology transfers.”

As a result of the years-long pressure exerted by the EU and other major trade players, the Chinese Finance Ministry removed last summer three measures of its indigenous campaign. Early this year, Michel Barnier, the European Commissioner for Internal Market and Services, left no doubt about the EU’s dissatisfaction with Beijing’s decision when told reporters "we're still not there" referring to the Chinese move.

Glass half empty for the time being

As Chinese provinces are granted greater competences to manage and dish out their own projects, China’s vast body of GP regulations is becoming increasingly intricate and stretched, and therefore, harder to grasp. In a recently-published position paper, the EU Chamber of Commerce in China echoed it when admitting the “lack of Western awareness and confusion with China’s own definition of government procurement.” Another commonly cited flaw of overseas investors in China is failing to seize the enormous role played by Chinese state-owned enterprises in carrying out the country’s procurement. Needless to say, it places foreign capital in a disadvantage position in the tricky business of scrambling for the most lucrative bids.

As we have seen, the gigantic market of China’s GP is arranged and administered in a way still far off from fully complying with the GPA’s requirements. Nonetheless, China is not alone among large economies in refraining from embracing the WTO’s government procurement drive. Notably, the remaining BRIC countries (Brazil, Russia, and India) are also proving reluctant to wholly vow their relatively-untapped government procurement markets to Geneva’s imperatives.

China joined the WTO on the premise of adhering to the organisation’s GPA, so Beijing’s trade partners and foreign investors are right to see the glass half empty. However, neither should not disdain the enormous gains obtained in accessing the fledging Chinese market since the country joined the WTO. “Failure to appreciate the great value of what is already on the table could risk missing a great opportunity to close the [GPA] deal,” pointed Zhenyu Sun, Chairman of China Society for World Trade Organization Studies.

China-bond companies should not expect much action over the course of the year. As the Chinese Communist Party leadership –and with it, the country’s-renovates, 2012 will be a transition year in the Middle Kingdom. In the run up to its October congress, the cautious mood of the party’s inner dealings trickles down all policy spheres. Last year’s improved offer to enter the GPA’s club is likely to be the last move to open up China’s government procurement for time to come. Once Xi Jinping -today’s Vice-president and tomorrow’s probable commander in chief- takes over, Beijing’s reluctant capitalism shall be ready for further compromise.

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