

How to Succeed in Business

And Why Washington Should Really Try

Alexander Benard

ON OCTOBER 19, 2011, the government of Afghanistan—acting in part on the recommendation of U.S. military advisers working with the Afghan Ministry of Mines—granted a license to the China National Petroleum Corporation (CNPC) to develop several oil fields in northern Afghanistan. Just three years earlier, another state-owned Chinese company, the China Metallurgical Group Corporation, won the rights to develop Afghanistan's Aynak copper deposit, one of the largest in the world, again with American acquiescence.

These economic wins for Beijing shocked many on Capitol Hill and in the broader policy community. Although it was no secret that China had been gobbling up strategically important resources in emerging markets, people wondered how a country that had not contributed to Afghanistan's transformation could now reap its mineral benefits—and how the country that had contributed more than any other could let it do so.

There should have been no surprise. The fact is that the United States has long lacked even the semblance of a strategy for competing with China in emerging markets. As a result, American companies are consistently beaten by Chinese ones in Central Asia, the Middle East, Africa, and even in nearby Latin America. Not only does the U.S. government offer American firms minimal help; at times, its own excessive regulations and reporting requirements actually discourage

ALEXANDER BENARD is Managing Director of Gryphon Partners, an advisory and investment firm focused on the Middle East and Central Asia.



U.S. firms from entering new markets. Apart from occasional lip service, U.S. policymakers have so far shown little desire to marshal government power on behalf of the private sector.

This aversion to corporate diplomacy is bipartisan, although the motivation differs. Liberals fear corporate influence over government, whereas conservatives disapprove of federal meddling in the free market. To a certain extent, wariness is justified, although for a third reason: taken to the extreme, full-throated advocacy of the private sector by Washington would come off as economic imperialism and provoke resentment abroad.

But emerging markets offer high-return investments and access to crucial natural resources that the United States cannot afford to pass up, as well as promising opportunities to deepen relations with strategically important countries. The U.S. government can no longer sit idly by as Chinese state-owned companies gain control over one

How to Succeed in Business

emerging market after another. If it does, U.S. businesses will lose out on many of these markets for the foreseeable future, hurting the country's economic and geopolitical interests.

Yet the game is not lost. Many developing countries are growing increasingly frustrated with Chinese business practices. At the same time, the U.S. government finally seems to understand the contours of the problem. The timing is thus ripe for the United States to get over its hang-ups about lobbying on behalf of American firms and rethink the way it helps them abroad.

DIPLOMACY, INC.

THE U.S. GOVERNMENT has not always been so timid in promoting commercial interests overseas. In 1794, Congress, in an attempt to defend merchant vessels from piracy in the Mediterranean Sea, commissioned six frigates "adequate for the protection of the commerce of the United States," creating what became the U.S. Navy. These ships were soon sent to attack North African pirates and free captive American merchants. The new navy protected U.S. merchant vessels from French corsairs in the Caribbean. And throughout much of the 1800s, U.S. naval squadrons patrolled the Mediterranean, the Caribbean, the Pacific, and the African coast, preventing the United States' enemies from inhibiting the flow of its goods.

American advocacy got even more aggressive around the early 1900s, when the government adopted "dollar diplomacy" as its guiding foreign policy principle. Washington encouraged U.S. investors to send capital abroad and foreign countries to stay open and hospitable to American businesses. It loaned money to foreign governments at generous rates, requesting that they provide special treatment to U.S. businesses in exchange. And it even used its military power to intimidate countries into adopting favorable trade policies: enforced by the U.S. Navy and the Marines, the Open Door policy ensured that China, with its vast mineral wealth and opportunities for large-scale construction projects, remained friendly to U.S. corporate interests.

In these early days, Washington encouraged U.S. companies to do business in far-flung parts of the world, and they could always count on their government for diplomatic and, at times, military support.

Alexander Benard

But in the second half of the twentieth century, the United States' priorities shifted toward strengthening ties among Western countries, containing the Soviet Union, and preserving global stability. Promoting commercial interests took a back seat. As for the U.S. private sector, when the world divided into separate U.S. and Soviet spheres of influence, entire markets were rendered off-limits.

The U.S. government became even less interested in commercial diplomacy after the fall of the Soviet Union. American leaders felt that government influence was no longer needed to further the interests of the private sector, and that as the world's sole superpower, the United States was above this sort of self-promotion.

The wars in Afghanistan and Iraq only heightened this reluctance. Eager to dispel claims that both invasions were favors to politically connected corporations, the George W. Bush administration went out of its way to shut down initiatives that smacked of U.S. business promotion. When Afghanistan opened up the Aynak copper deposit to foreigners in 2007, Afghan President Hamid Karzai, in a meeting with Bush, noted that a U.S. company had made a bid and said he hoped the company would "make it very far along" in the process—a diplomatic way of offering his support. Bush bristled and told Karzai that all the United States cared about was a transparent competition. Beyond that, it was up to Afghanistan to decide the winner.

The notion that the United States should focus only on transparency, that anything more would be inappropriate, has inherent appeal. But the country's competitors—China, India, Russia, and Europe—are already meddling. Washington's restraint, although well meaning, is entirely unilateral and thus only puts it at a disadvantage in emerging markets, where politics and business intertwine at every step.

FALLING BEHIND

WASHINGTON MAY be feckless at business promotion, but Beijing has grown expert at it. Adopting policies that recall those of the United States in the early twentieth century, China has spent the last 20 years busily locking down opportunities throughout Central Asia, the Middle East, and Africa, employing a variety of tactics in the process.

How to Succeed in Business

For one, Beijing has used its massive foreign currency reserves to provide low-interest loans and other forms of financing to governments in the developing world, often in return for access to natural resources and infrastructure contracts. In the process, these emerging-market countries have become dependent on the Chinese government for their economic survival. China knows it and is not shy about wielding that leverage to obtain a lucrative contract, shape the structure of a resource sale, or freeze out Western companies. Before developing countries award mining rights or construction projects, China will often intervene in support of its firms through its foreign minister or even, in some cases, its prime minister.

China also subsidizes its state-owned companies in their bids for natural resources, allowing them to offer far more attractive terms than U.S. companies can. I saw this firsthand last year, when my firm advised a Western company competing against CNPC for several oil fields in northern Afghanistan. CNPC offered the Afghan government 15 percent of all revenues derived from these fields and was prepared to go higher, as well as offering other terms that would have made it nearly impossible for CNPC to profit from the investment. But as is the case with many natural resource investments made by China's state-owned companies, the motive was not to make money; rather, it was for the Chinese government to capture valuable resources to fuel the country's economic rise.

Another Chinese tactic is to bundle major infrastructure investments with natural resource bids by its state-owned companies. In 2008, for example, as part of a state-owned company's proposal for the Aynak copper mine in Afghanistan, the Chinese government promised to build a railroad and several major roads in the area. Later, when CNPC competed for oil resources in northern Afghanistan, it proposed building a large road and a massive oil refinery that, by all accounts, would far exceed what Afghanistan's meager reserves require. But the Afghan government was happy to accept the investment.

Among its peers, the United States is by far the least aggressive in promoting commercial interests.

Alexander Benard

These tactics have served China well. In Africa, Chinese trade and investment have skyrocketed, from around \$10 billion per year ten years ago to over \$120 billion today. Chinese companies are striking over \$50 billion worth of infrastructure deals there annually, signing dozens of lucrative hydrocarbon and mineral contracts as well. Beijing is also targeting Central Asia, where major state-owned Chinese companies are rapidly expanding their presence even in countries outside China's traditional sphere of influence. In the past few years, for example, Beijing has lent \$4 billion to Turkmenistan for the rights to develop the country's largest gas field for 30 years; offered \$10 billion to Kazakhstan in exchange for permission for a Chinese company to buy one of the country's largest oil producers; and bullied Kazakhstan, Turkmenistan, and Uzbekistan into approving a major gas pipeline that Russia and Europe oppose. Historically, these countries have fallen under Russia's influence, but now China is busy erecting pipelines on their soil and extracting oil, gas, copper, iron ore, lithium, and rare-earth elements from beneath it.

China is not the only country vigorously pursuing commercial diplomacy. Brazil, India, and Russia regularly throw their political weight behind their powerful state-owned companies, too. The United States lags behind even its European friends. The United Kingdom's foreign ministry has officially declared the promotion of British firms as a top foreign policy priority, and French President Nicolas Sarkozy regularly invites the CEOs of major French companies along during his international travels. In certain markets, German diplomats spend the bulk of their time accompanying German business executives to meetings with foreign government officials and working behind the scenes to give German companies a leg up. Indeed, throughout Central Asia, the German government pays professional lobbying firms to work alongside its diplomats. Among its peers, the United States is by far the least aggressive in promoting commercial interests.

A CHANCE TO COMPETE

BEIJING MAY have taken the lead in commercial diplomacy, but Washington can catch up if it changes course now. Many countries in the developing world are growing resentful of China's domination over

How to Succeed in Business

their economies, and some are looking to diversify their relationships—an opportunity the United States should exploit. In private meetings, Kazakh officials have admitted that they are starting to take strategic diversification into account when evaluating foreign bids. Mongolia, meanwhile, has excluded Chinese companies from investing in several of its coal and copper mines and is trying to break existing contracts for other resources with Chinese companies so that it can bring in more Western ones.

Developing countries are also increasingly frustrated with Chinese business practices. Chinese companies have earned a reputation for using their own (imported) laborers instead of hiring locals, ignoring environmental considerations, and employing subpar technologies. And when it comes to less high-profile projects, the firms are likely to lack relevant experience, since Chinese officials see these as a chance to dole out favors to politically connected companies that may be technically unqualified.

To make matters more complicated, sometimes the attractive economic terms offered by Chinese businesses turn out to be illusory. For example, a Chinese company might offer a government a far higher percentage of future revenues for the lease of an oil field than will a U.S. company (say, 20 percent versus 10 percent). But then, the winning company will use inferior technology to cut costs—two-dimensional rather than three-dimensional seismic surveying, for instance, or outdated rigs and drills. As a result, the operation will end up extracting less oil than the Western one would have and sometimes will even permanently damage the reservoir. The 20 percent royalty rate applies to a smaller pie—and may come with a higher cost.

Chinese companies also take much longer to extract resources than their Western counterparts. Most Chinese oil, gas, and mining firms operate at the behest of the Chinese government, which cares more about securing long-term access to natural resources than maximizing profit. So they may move slowly on purpose to save the resource for later, when Chinese demand for it has increased. When a mining or drilling operation lies dormant for years, the host country earns no revenue at all.

China's corporations also sometimes try to renegotiate the original terms of agreements once they have established a presence on the

Alexander Benard

ground. At that point, it becomes difficult—politically, legally, and logistically—for the host governments to revoke the contracts and sell the resources to someone else, especially if Beijing, as it is wont to do, applies additional pressure during the renegotiations.

American companies would have a much harder time getting away with such behavior. They are accountable to boards of directors and public shareholders and must publicly disclose their dealings, requirements that make a strategy of over-the-top promises followed by blatant contract violation nearly impossible. They use superior technologies that can find and extract more resources and cause less damage to reservoirs and mines. And they are motivated purely by profit, which aligns their incentives with those of the host governments and gives them reason to develop the resources quickly.

It is no surprise, then, that emerging-market countries are hungering for more investment from the West, particularly from the United States. As any U.S. businessperson who has worked in emerging markets will confirm, officials there are eager to roll out the red carpet for U.S. companies and investors. The American brand is still strong, and the presence of U.S. businesses in these countries is still perceived as the ultimate validation of their commercial legitimacy, as well as a step toward stronger ties with the U.S. government itself.

CUTTING THE RED TAPE

BY OVERPLAYING its hand, China has given the United States a good chance to compete. To take advantage of the opportunity, however, Washington must entirely rethink the way it promotes U.S. businesses abroad.

There are signs that it is starting to do so. Secretary of State Hillary Clinton has highlighted "economic statecraft" in recent speeches, and in February, she hosted a two-day conference on "jobs diplomacy," saying, "we will not rest until the U.S. government is the most effective champion of business and trade anywhere." But past officials have made similar promises, only to see the resulting initiatives fizzle out. If Clinton wants to make sure her efforts actually last, she will have to launch a top-to-bottom reexamination of U.S. commercial diplomacy across all parts of the government.

How to Succeed in Business

As it stands now, the Commerce Department generally takes the lead in facilitating U.S. business activities overseas, but other parts of the government, including the State Department, are supposed to be involved, and an interagency process exists to coordinate all the players. The reality, however, is that these departments and initiatives are low level and are strewn across the bureaucracy, with various offices sometimes working at cross-purposes. Furthermore, the U.S. government program that allows American companies to request Washington's help in particular transactions is complicated, arduous, and usually results in little more than a letter from a U.S. agency to its foreign counterpart—hardly vigorous advocacy. These various initiatives need to be consolidated into a single office, housed in the State Department, that can coordinate efforts across all the relevant agencies and departments.

Washington must also rewrite the rules that guard against favoring certain U.S. companies over others. The guiding principle behind these rules should be simple: if a company meets certain eligibility criteria and is the only U.S. company bidding for a project, it should get government support; if multiple U.S. companies are competing, then the government should find a way to promote all of them, rather than none.

U.S. diplomats must also become more nimble advocates for U.S. businesses. Today, the State Department generally fails to inform foreign governments about the benefits of working with U.S. companies and the drawbacks of doing so with their Chinese counterparts. Promoting U.S. business interests should be part of ambassadors' job descriptions, and they should be evaluated on how well they do it. Diplomats should highlight the United States' superior technologies and business practices, convey the importance of strategic diversification, and, in particular, explain that higher royalty percentages do not guarantee greater revenue. For large projects, the secretary of state should weigh in.

Diplomats should also spend time convincing their host governments to level the playing field between Western companies and Chinese ones. Right now, many deals are simplistically structured, favoring the bidder offering the highest royalty rate on a resource or,

China has managed to plant its commercial flag even in countries that are U.S. allies.

Alexander Benard

in the case of an infrastructure project, the lowest cost. Processes such as these inevitably favor inferior companies that employ no locals. Washington needs to deliver the message that when awarding contracts, officials should take into account such factors as the company's technological prowess, its environmental track record, and its plans for local employment.

Another area for improvement is the United States' confusing and cumbersome web of regulations. The Foreign Corrupt Practices Act (FCPA), which outlaws bribing foreign officials, and the Treasury Department's Office of Foreign Assets Control, which enforces economic sanctions, place immense burdens on U.S. businesses in emerging markets. Today, businesses often don't know the answer to such basic questions as what qualifies as a foreign official, how responsible a U.S. company is for the actions of its local partners, and what constitutes knowledge that bribery has occurred. Things have only gotten more confusing since the Obama administration decided to step up its enforcement of the FCPA, prosecuting twice as many cases in 2010 as it did in 2009. The government needs to issue clearer guidelines regarding exactly what types of conduct are and are not covered by these regulations, as it has indicated that it may do later this year.

At the same time, the U.S. government should try to find ways to derive strategic value from its regulations. For example, it should push countries to require bidders for projects to have in place strict anti-corruption procedures, which would give already compliant U.S. companies an advantage over Chinese ones. Indeed, Chinese businesses are among the most corrupt in the world; a recent report from Transparency International ranked them more likely to pay a bribe than anyone but their Russian counterparts. And for other regulations concerning everything from construction to telecommunications, Washington should also try to make U.S. standards the international norm. Doing so would not only help developing countries by ensuring top quality and best practices; it will also tip the scales in favor of U.S. firms, which by default already comply with such standards.

Finally, the United States must make it easier for U.S. companies to partner with government agencies that disburse foreign aid. Chinese companies routinely coordinate with the Chinese government to bundle commercial proposals with aid projects, thereby enhancing the

How to Succeed in Business

perceived value of their bids. For example, a Chinese company will bid on a coal mine and pledge to build a major highway, too. Infrastructure investments like these take the form of aid and so are financed by the Chinese government. But the Chinese company can still take credit for the highway to make its bid look more attractive. It is very difficult for U.S. companies to do the same, and this must change. U.S. aid agencies should allow themselves to coordinate more with the private sector, so that American firms can make reference to aid projects in their bids or bundle their bids with proposals for USAID development projects. Only then would Washington be deriving commercial value from its aid budget.

NO TIME FOR TIMIDITY

THE UNITED STATES has many competing foreign policy interests: national security, human rights, the rule of law, and so on. The country cannot revert to the days of dollar diplomacy, when all of these interests were subordinate to those of big business. Indeed, as China itself proves, such an approach can backfire.

But the pendulum has swung too far in the other direction. For too long now, Washington has almost entirely neglected commercial diplomacy, ceding too many economic battles to China. The consequence of such timidity has been that the United States' rising competitor has managed to devour market share in emerging economies throughout the world, securing strategic resources, winning infrastructure contracts, and planting its commercial flag even in countries that are strong U.S. allies. The United States needs to find a happy medium in which business promotion again becomes a strong pillar of its foreign policy, although not its sole focus.

The declining popularity of Chinese companies in the developing world has given the United States an opening to regain the initiative in these critical markets. Developing countries are eager to work with U.S. firms, so Washington needs to clear away the red tape that prevents them from doing so. Any reforms will likely be met with political and bureaucratic opposition. But perhaps the weakness of the U.S. economy, if nothing else, will finally help convince the country's leaders that it is well past time to make such changes.©