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One of China’s best state enterprises shows need for reform

Peter Fuhrman, China First Capital | Oct 05 |

China’s ruling State Council last month released a much-anticipated plan meant to kick the country’s huge state-owned enterprise (SOE) sector into shape. No small amount of kicking is required. Not all but many of China’s 155,000 SOEs are inefficient and often loss-making. Where SOEs do make money, it’s usually because of markets and lending rules rigged by the government in their favor.

Finding a truly good SOE, one that can take on and outcompete private sector rivals in a fair fight is hard. Gong He Chun is one. Customers throng daily to buy its high-quality products, often forming long queues. The employees, unlike at so many SOEs in China, are helpful and enthusiastic and take evident pride in what they are doing. Though local private sector competitors number in their hundreds, Gong He Chun has them all beat.

Gong He Chun is a small restaurant chain, with just four shops in the ancient and Grand Canal city of Yangzhou, about 300km up the Yangtze river from Shanghai. It specializes in preparing and serving meticulously-prepared versions of dishes that have for over 1,000 years made Yangzhou synonymous with fine eating in China.

It’s a rather long and mouth-watering list, including crab and pork-stuffed xiaolongbao dumplings (below centre), potstickers (below right), steamed shrimp dumplings, shredded tofu and of course Yangzhou’s most famous culinary export, Yangzhou fried rice.

  

Gong He Chun was founded in 1933 as a private concern, but was then, like almost all other private businesses, expropriated in 1949. It's been an SOE ever since, its shares owned by the Yangzhou government branch of SASAC, the government agency now responsible for holding shares and guiding the management of all SOEs. Gong He Chun somehow held on through the long dark years during Mao Zedong's rule when most restaurants in China were shuttered, and investment in the SOE sector was directed toward Stalinist heavy industry – steel mills, coal mines, power plants, railroad rolling stock and the like.

Yangzhou, Yangzhou cuisine and places like Gong He Chun represented just about everything that Chairman Mao Zedong most detested. Since at least the Tang Dynasty (618-907), the town has had a reputation for its mercantile traditions, beautiful women and traditional culture. To eradicate such bourgeois roots, Mao and his planners crammed the city in the 1950s and 1960s with ugly sooty chemical factories and smelters.

I remember first visiting Yangzhou in 1981 and being shocked by the sight of once-splendid Ming Dynasty temples and courtyard homes converted to makeshift factories and communal dwellings. In those days, finding anything to eat, even at the few hotels where foreigners were allowed to stay, was no simple matter. All food, including dumplings, was available only with ration coupons.

Things have improved over the last twenty-five years. One not-unimportant reason for this is that Jiang Zemin, who ran China from 1989-2002 is a native son of Yangzhou while his successor, Hu Jintao, was raised in the next door town of Taizhou. Jiang still visits Yangzhou at least once a year, usually during Qingming Festival when filial Chinese return to their home to sweep the graves of their ancestors. Yangzhou this year is celebrating with pomp the 2,500th anniversary of its founding.

Gong He Chun (see photo) still hews closely to the recipes and cooking methods perfected in the 1930s by the founder Wang Xuecheng. This means cutting thin soup noodles by hand, preparing the dumplin skins in such a way as to create tiny pores and air pockets that allow flavor to seep in.

Ever wonder exactly how a properly prepared potsticker should look?

At Gong He Chun, as all its many cooks are taught, they must fulfill Wang's precise prescription: the overall outward appearance of a sparrow's head, with its slender sides resembling a lotus leaf and its bottom fried to the color of a gold coin. If only the management and workers at China's huge substandard SOE oil refineries took as much care, China's polluted skies would surely improve.

While the quality of what comes out of the kitchen is world class, there are places where the dead hand of state ownership can be detected. The toilets are primitive, plastic plates and bowls are old and chipped, and the overall décor looks like a 1950s US high school lunchroom.

Though its brand-name and reputation are known nationally, Gong He Chun has no apparent intention to expand outside Yangzhou. The three-tiered system of SOE management in China, with ownership spread among national, provincial and local branches of SASAC, makes it both rare and difficult for any local SOE like Gong He Chun to expand outside its home base.

Meantime, a Taiwan company, Din Tai Fung, has taken Yangzhou cuisine, especially the crab xiaolongbao, and built a high-end chain of global renown, with Michelin-starred restaurants across East and Southeast Asia as well as the US, Australia and Dubai. Its China outlets sell dumplings at three times the price of Gong He Chun.

I'm lucky to know the China chairman of Din Tai Fung, and have spent time with him inside Din Tai Fung restaurants. Every detail is sweated over by the chairman, from the starched white tablecloths to the polish on the bamboo steamers to the precise number of times a xiaolongbao dumpling should be pinched closed. Gong He Chun's state owners are utterly devoid of the drive, vision and hunger for profits and expansion that only a private proprietor can bring.

A newly-announced government policy on SOE restructuring has already come in for criticism in China. Xi Jinping and his State Council – once keen to expose SOEs to more market rigor and competition – have opted for a more "softly-softly" approach, with no specific targets for improving the woeful performance of many SOEs. One reason is that a fair chunk of China's SOE system is in chaos, thanks to a more high-priority policy of the Xi government. Every week brings new reports about bosses and senior management at China's largest SOEs being investigated or arrested for corruption.

If there was ever an economic rationale for a small chain of traditional dumpling shops to be owned by the state, no one seems able to recall it. What profit Gong He Chun makes is not being reinvested in this rare SOE jewel, but is used instead to prop up SOE losers in Yangzhou. As China's new SOE reform policy now begins its tentative roll-out, it looks certain Gong He Chun will for years to come remain a rare bright spot in a blighted SOE landscape.

Peter Fuhrman is Chairman & CEO China First Capital. He has no business relationship with Gong He Chun.

http://blogs.ft.com/beyond-brics/2015/10/05/one-of-chinas-best-state-enterprises-shows-need-for-reform/