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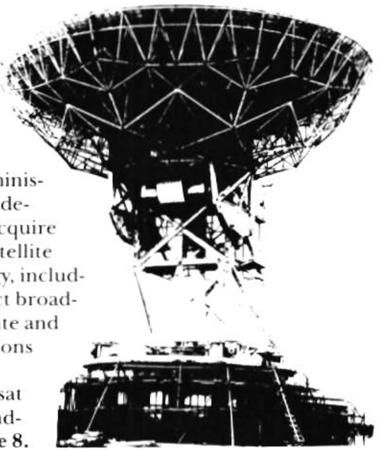
Advertising in China

The China Business Review

The magazine of the National Council for US–China Trade

January–February 1984 Volume 11, Number 1

Cover: US ad agencies believe a good match exists between their expertise in the US market and China's desire to increase the sophistication of its export marketing techniques. **Page 12.** *Cover is Dynasty wine label by Andy C. Neilson; developed by Meridian Advertising (Hong Kong) for Remy Martin Far East Ltd.*



Satellites: At least four Chinese ministries have decided to acquire foreign satellite technology, including a direct broadcast satellite and earth stations to link up with Intelsat V and Landsat V. **Page 8.**

Premier Zhao: China's first head of state to visit American shores emphasized to 300 business executives and government leaders at the Council's January 11 luncheon reception that "economic cooperation between our two countries is extremely important." **Page 28.**

Departments

摘要

CHINA'S SECRET OF SUCCESS

How does a country famed for its slow-moving bureaucracy continue to register such rapid rates of economic growth year after year?

In 1983 China's GNP reportedly increased by 7 percent as measured in Chinese yuan at current prices. This is the sixth year in a row that China's GNP growth rate has exceeded 5 percent. In 1980 and 1982 growth was 9 percent.

The value of agricultural output grew by 4 percent, continuing a strong upward trend that has averaged roughly 10 percent per year since 1978, the year China turned away from collective farming and began to experiment with individual incentives and de facto private land ownership.

The State Statistical Bureau also reported across-the-board gains in industry in 1983. Steel output rose by 8 percent, coal by 5 percent, electricity by 7 percent, chemical fertilizer by 10 percent, and cement by 12 percent. Even larger gains were achieved for consumer goods, especially bicycles, TVs, and household light bulbs. The production of luxury items such as washing machines and refrigerators exceeded 40 percent. China's most popular beverage, beer, continued to set production records.

Foreign trade, however, increased by only 2.2 percent in 1983, according to the Ministry of Foreign Economic Relations and Trade. This is better than the 5 percent decline suffered in 1982, but it falls far below the 32 percent per year growth rate achieved between 1978 and 1981. But in the third quarter of 1983, China's imports jumped 25 percent as compared with the same period the year before. This was the first upturn in a year and a half, and could signal China's willingness to begin spending part of the large foreign exchange reserves it has accumulated in recent years. —JBS

THE ITCA AGREEMENT: HELPING US FIRMS LEARN "WHAT CHINA REALLY WANTS."

The Industrial and Technological Cooperation Accord signed by President Reagan and Premier Zhao on January 12 "represents a major breakthrough in US–China commercial relations," the Commerce Department's Deputy Assistant Secretary for East Asia and the Pacific, Eugene K. Lawson, recently told *The CBR*.

"The accord could do for our commercial relations what the January 1979 science and technology agreement did for technical exchanges." That agreement led to 21 protocols, including the important hydropower protocol that opened the way for a $400,000 grant to the Harza Engineering Co. of Chicago for a feasibility study of the Tianshengqiao project in Guangxi. "We needed a similar framework agreement to promote commercial relations," Lawson said. "Now we have it."

Lawson will chair the ad hoc Working Group under the Joint Commission on Commerce and Trade (JCCT) that oversees official ties between the US Commerce Department and China's Ministry of Foreign Economic Relations and Trade. The JCCT first met in Beijing between May 23 and 26, 1983. The Working Group will hold its first formal consultation with the Chinese this May when the JCCT convenes its second meeting.

"We want to work very closely with the private sector and especially the National Council for US–China Trade and its industrial committees. Above all, we want US firms to participate in the early stages of planning so that they know what China really wants," Lawson said.

Apart from Commerce, the Working Group will also include representatives from the Overseas Private Investment Corporation, Treasury Department, US Exim Bank, State Department, and the State Department's Trade and Development Program. In fact, Article V section 1 commits the US side to "financial facilitation and funding on as favorable terms and conditions as possible," and stipulates in section 2 of the same article that TDP "shall consider the funding of feasibility studies of industrial and technological cooperation projects." This provision could substantially enlarge TDP's commitment to China, which has already funded 14 prefeasibility missions to China under the auspices of the National Council for US–China Trade. "Basically, the Working Group will coordinate and build on the current programs of US government agen-

Secretary of Commerce Malcolm Baldrige (left) recently received the first National Council for US–China Trade Award for his contributions to the promotion of commercial relations with China. Baldrige was in the forefront of efforts to liberalize US controls on high-technology exports to the PRC. Presenting the award is Council Board Chairman Walter S. Surrey.

cies," Lawson said, "not add another layer of bureaucracy."

Lawson hopes that the Working Group will soon sign follow-up protocols: "From four to five protocols could be signed this year, and more in 1985. These would cover such areas as coal, offshore oil, petroleum equipment, railways, electronics, telecommunications, posts, and airports."

A protocol could also be signed to facilitate direct ties between individual American and Chinese companies. Under such a "buddy system," Lawson explained, a US firm could more easily carry on direct trade, delegation exchanges, and technology transfer with the firm's counterpart in China. "Such a protocol would permit us to draw up the necessary standard form agreement to be used by participating companies. They could fill in the blanks and start doing business. Moreover, such an arrangement would reduce the bureaucratic impediments to doing business in China, and encourage medium and small US firms to become more active in the China market."

The two-year accord extends through January 31, 1986, and will continue indefinitely for successive three-year terms if neither party terminates the accord at least 30 days prior to the expiration of each term.

—JBS

MARRIAGE AND LONGEVITY: A SECOND LOOK AT CHINA'S 1982 CENSUS

China's July 1982 census produced few surprises at first. The population total of 1,008,175,288, released in October of the same year, came close to earlier projections and the natural increase rate of 1.5 percent suggested that the rate of growth of the population was slowing down, also as predicted.

But on December 13 Beijing released its long-awaited detailed breakdown of the 1982 census based on a 10 percent sample. Some of its more curious results:

▶ The vast majority of adult Chinese are married. Only about 5 percent of all Chinese men over 30 are still unmarried, while only about one-third of 1 percent of all women over 30 are unmarried.

▶ Of the 756 Chinese over 105 years of age, not one lived in Beijing, Tianjin, or Shanghai at the time of the 1982 census. But 415 reportedly lived in remote Xinjiang Province. The oldest Chinese was a 130-year-old Xinjiang peasant named Kuerbanyasheng, a resident of the Yingaleike production team in the Tashenlike commune in Xinhe County. How the authorities checked the veracity of these results is not discussed.

▶ Median ages vary enormously from region to region, and appear to be highly correlated with fertility and relative income. The median age is over 29 years in Shanghai, China's most developed city, which enjoys a per capita GNP of about $2,000, comparable with Malaysia or South Korea. It is only 18 years in poorer regions like Qinghai or Ningxia, which have per capita GNPs roughly on the order of $100 or less, comparable to Chad or Afghanistan.

—JBS

CHINA'S NEW "FED"

"China has no central bank," a Chinese official once lamented after visiting the Federal Reserve in Washington.

Then in early 1984, China established its own Fed by converting the People's Bank of China into a central bank. The September 28 State Council announcement indicated that the reorganization would be carried out in two steps. On January 1, the PBOC's branches nationwide were organized into the new Industrial and Commercial Bank, in charge of the nation's day-to-day banking business. Then on January 27 the authority of the PBOC's headquarters were substantially increased. It will "issue currency, coordinate and examine the operations of all monetary organizations, set credit ceilings, and act as the state's treasury," according to PBOC Vice-President Liu Hongru. Henceforth, all subordinate banks and financial institutions, such as the China International Trust and Investment Corporation, must assign up to 50 percent of their deposits with the new PBOC, which is empowered to adjust the deposit ratio to control money and credit, Liu further explained.

Of even greater significance was the decision to place the PBOC under a 14-member Federal Reserve-type board, chaired by the PBOC's current president, Lu Peijian. Liu is vice-chairman. Other members are drawn from the powerful State Planning Commission, the State Economic Commission (the SPC's sister planning agency in charge of annual plans), and the Ministry of Finance. The council's main task will be to resolve disputes between the PBOC and other banks.

The PBOC has clearly won a major bureaucratic victory over its rival, the Ministry of Finance, to become China's premier monetary authority. The new PBOC also seems determined to stop, even reverse, the decentralization of the banking system that one PBOC official blames for China's "burgeoning inflation."

How the new PBOC intends to exercise its authority is still unclear. In true Fed style, Chairman Lu cautioned reporters: "By tightening the money supply, we don't mean . . . we are going to raise interest rates."

—JBS

HOTELS, BONDS, AND THE PHILIPPINE TRADE GAP

The Philippines is among the countries pushing hardest to build hotels in China. A multi-million-dollar hotel and commercial center/office complex in Shanghai was proposed in June 1983 when Shanghai Mayor Wang Daohan signed a sister-city agreement with Metro-Manila. The International Grand Hotel project in Guangzhou, postponed in 1979, was revived in November 1982 when Guangzhou Mayor Liang Lingguang signed a second sister-city agreement with Metro-Manila, though no progress beyond site selection has been reported since then on the $40 million 350-room hotel.

The governor of Metro-Manila, First Lady Imelda Marcos, visited Beijing in January to promote these and other projects as a way to rectify the Philippines' worsening trade and investment balance with China. Accompanied by Jaime Laya, then governor of the Central Bank of the Philippines, their four-day trip included meetings with top party and state leaders Hu Yaobang, Wan Li, Li Xiannian, and Minister of Finance Wang Bingqian. A trade memorandum was signed that will attempt to balance each country's exports to the other at roughly $500 million. In 1982, two-way trade totalled $311 million, with the Philippines running a deficit of just over $100 million. In the first half of 1983, its imports were more than twice its exports to China. Since direct bilateral trade began in 1972, petroleum has made up the lion's share of Chinese exports, and another 650,000–900,000 tons of crude will be sold in 1984.

To pay for these imports, Imelda Marcos urged the Chinese to buy more coconut oil, bananas, sugar, and copper from the new refinery at Leyte opened last July. Significantly, the First Lady may have persuaded the Chinese to purchase several hundred million dollars worth of Philippine treasury bonds—a possible sign, if this occurs, that the Philippine hotel projects finally have Chinese approval. —MCR

THE IRREGULAR ARMY?

In the past, China's prestigious People's Liberation Army was virtually immune to charges of corruption.

But things are changing. The accusations recently leveled at the PLA range from using public funds for the lavish entertainment of visiting superiors and influence peddling to procure promotions for relatives, to bribery of civilian officials to obtain scarce supplies of equipment or materials.

A key element in most of the stories in the official media is the connivance of superiors in covering up such incidents. In one case, the leadership of a tank division in northeast China, one of the most sensitive of China's military regions, tried to force an inspector to drop his investigation of influence peddling and embezzlement. He was harassed, criticized, and finally fired before attracting the attention of high-level officials. The inspector has now been commended by the Central Military Commission and the tank corps' leaders face charges.

In another case, the deputy chief of supply for the Navy's Guangzhou command and an accomplice accepted more than $3,500 from a Shantou company to provide hard-to-find aviation kerosene. A local military tribunal acquitted them, despite the strong evidence against them. The prosecutor appealed to China's Supreme Court, which reversed the verdict and sentenced the culprits to two years in prison.

This sort of irregularity goes right to the top. The headquarters of the Ministry of Ordnance, which directs most of China's military-industrial complex, has been publicly criticized for issuing excessive bonuses and gifts to the tune of some $175,000. Worse yet, the ministry's bad example led subordinate factories to follow suit. A dozen enterprises in Beijing awarded bonuses worth more than half a million dollars, including washing machines, folding chairs, electronic watches, cloth, and electric fans.

In order to evade detection by the banking and auditing authorities, many of the offending units reportedly used extra-budgetary earnings from foreign trade. Of the $175,000 in bonuses awarded by the ministry's headquarters, some $144,000 came from foreign trade earnings not allocated by the central government, and therefore hard to trace.

The crackdown is clearly designed to convey a message: Beijing has no intention of limiting its current rectification campaign of the Party to just the civilian sector. —CMC

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(Signed) James B. Stepanek, Editor

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COMMENTARY

评论

High Technology Sales to China: the COCOM Connection

Though China has been moved from country group P to V under the Export Administration Act Regulations, a definite step toward liberalization, business people should not assume that all controls have now been dropped, that all licenses for high technology exports will be approved instantly, or that the international review process will always be as fast as the internal US review. High technology exports to China still must go through COCOM, the international export-monitoring structure established in 1950 and headquartered in Paris that coordinates the export policies toward communist Asia and Europe (minus Yugoslavia) of Japan and all NATO countries (minus Spain and Iceland).

On top of the US license period, an approval in COCOM usually takes 45–120 days, depending on the level of sophistication and how well the application was prepared. Your exports will certainly always have to wait between 30 and 45 days. If only one COCOM member objects, the case is vetoed; but very few cases for China are ever objected to, and despite the deluge of export requests caused by the new policy, US cases are being processed quickly by the other members.

If you are a subsidiary of an American firm, or a foreign firm operating in another country, your reexport will not require a reexport license if it gains full COCOM approval and is not covered by an administrative note to the Commodity Control List (CCL). In other words, if you fit in that category you are wasting time asking for a US reexport license, and are probably delaying your sale. Just ask your host government for its export license, and then go through COCOM. Especially complicated, state-of-the-art cases can take longer; so if your export is breaking completely new ground at levels far above what has ever been approved, you may wish to consider giving the US government a heads-up prior to COCOM review.

The Office of East–West Trade of the Department of State coordinates the US position on foreign and US COCOM requests. This is done through the Economic Defense Advisory Committee (EDAC), chaired by the State Department and made up of officials of the Defense, Commerce, and Energy departments and the intelligence community. I chair the case-processing subcommittee of Working Group One of EDAC, and on a day-to-day basis coordinate the US government's case processing. EDAC is a ladder organization; so if a case can't be resolved at my level, it can be escalated to other EDAC rungs, and even go to the president.

The Commerce Department answers technical questions on US cases (except for munitions exports, which are handled by State); however, if an American export gets into trouble, I coordinate the response directly, or it is handled through EDAC. Trouble can often be avoided if the US exporter thinks ahead and sets feasible deadlines. Almost 2,000 cases a year are handled in committee. Even more will be handled because of the recent liberalization. Other countries cannot always hasten their review. And every time we ask, we obligate ourselves to return the favor, something that we are not always able to do.

Full information is critical. When requesting permission to make an export, don't just list the trading organizations. Tell us the name of the real end-user, including the street address, phone number, and what the end-user intends to do with the export. Has the item been previously exported through COCOM? What were the previous license numbers (if any)? Provide us with a complete set of parameters, complete information on the system the equipment will be used with, and so forth.

The increasing number of joint ventures in China will likely have a major impact on COCOM case processing. Such ventures tend to involve packages of individual transfers of technology spanning several years, or a decade and more. I suggest that when applying for export licenses, a calendar be provided by the exporter that realistically describes each phase of technology transfer. This will cut valuable processing time, and could save a case.

In conclusion, I would say that the international process should not be feared. COCOM licensing protects all of us. It coordinates the export policies of industrial countries and presents a unified response to a common technological threat. This is a far more effective tool than a patchwork of individualized, unilateral policies, no matter how strong they might be. But so long as relations with China continue to improve and your export request is reasonable from a strategic point of view, the sale will be made. The things to remember are: Make a complete license request, allow enough time for it to be processed, and make your request reasonable.

—Larry Winter Roeder, Jr.
International commodities economist, Office of East–West Trade, US Department of State.

Readers are encouraged to send their commentaries, not exceeding 800 words, to: The CBR *editor, The National Council for US-China Trade, Suite 350, 1050 17th Street, NW, Washington, DC 20036. Deadlines are one month prior to the issue date that appears on the cover. Opinions do not reflect Council policy, unless indicated.*

China's Great Leap Skyward

Intelsat, Landsat, and a direct broadcast satellite will link Beijing and the rest of the country.

Madelyn C. Ross

Three new satellite systems are scheduled to get off the ground in China during the 1980s. The first could go into operation this year, and will involve an Intelsat lease to improve telephone and data transmission between Chinese cities. It will be followed by a broadcasting satellite primarily for television transmission, and a remote sensing satellite system to promote better land resource management. All three satellite systems will rely heavily on Western technology, at least until China upgrades its own satellite industry.

TELECOMMUNICATIONS

Five-year Intelsat lease

China will be the 25th country to modernize its domestic communications by leasing satellite space from Intelsat, the international consortium that handles most of the world's transcontinental telecommunications via its 16 satellites.

Beginning in late 1984—or possibly 1985, depending on the pace of ground station installation—Intelsat will allocate to China one-half transponder (18MHz bandwidth) on Intelsat Satellite V (IS-V) at C-band frequency (6/4 GHz). The annual charge for this five-year lease will be $400,000.

Several ministries and agencies in China, each operating its own telecommunications network, will jointly use Intelsat's satellite services. These include the Ministry of Posts and Telecommunications (MPT), the Ministry of Petroleum, Ministry of Coal, and Ministry of Water Resources and Electric Power, with MPT acting as coordinator for all ministries involved.

MPT will use the satellite to improve the sorely inadequate connections between Beijing and the more remote regions of the country. The microwave network that currently provides the basic links between the provinces requires relay stations every 50 kilometers, making it both expensive and impractical to extend the network to such remote regions as Xinjiang, Tibet, and Inner Mongolia. These areas remain linked to the rest of the country by open wire, if at all.

The new Intelsat-based system will introduce clear and direct one-hop transmission between appropriate ground stations anywhere in China. Not surprisingly, three of the first areas to be linked to Beijing via satellite will be Urumqi, Hohhot, and Lhasa, capitals of Xinjiang, Inner Mongolia, and Tibet. Most of these regional ground stations will have antennae of 10–13 meters in diameter. Below the regional level, most public telecommunications will continue to use terrestrial technology rather than satellites. However, small local earth stations with antennae 6–7 meters in size will be installed where terrestrial links are impractical.

Thirty-eight ground stations are planned for the MPT network, although only a handful of these will be operational when the Intelsat lease begins. Most of MPT's ground stations will be manufactured by the Ministry of Electronics, which may seek foreign assistance to upgrade the Nanjing Radio Factory for this purpose. A major exception will be the system's master station in Beijing, requiring an 18 meter antennae, which will be imported during 1984 at a cost of more than $1 million.

Though MPT's far-flung network may take a long time to fully implement, the Ministry of Petroleum Industry (MOPI) has more immediate plans for the Intelsat transponder. It intends to use the satellite to facilitate communications and rapid data transmission from numerous oil drilling locations throughout the country to Beijing and overseas. Because of the high national priority accorded offshore oil exploration and development in China, and the potential revenue if oil is found, MOPI is committed to a more urgent timetable than the other ministries. Accordingly, MOPI agreed in January to purchase 15 ground stations from Spar Aerospace (Canada). The purchase involves an 11-meter station for Beijing and ten 7.3-meter stations, three 9.3-meter stations, and one 6-meter station. Spar will also supply the 18-meter master station for Beijing and ten stations involving technology transfer for the Ministry of Electronics. The value of the entire package exceeds Canadian $20 million.

The Ministry of Coal plans to use the Intelsat system to improve com-

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December 4–10 in Shanghai. Contact Ms. Choy So Yuk, SHK International Services, Ltd., 3/F Admiralty Center Tower II, Hong Kong. Telex: 74782 SHKSC HX.

CHINA'S INTELSAT NETWORK

munications with isolated mining areas. First priority is the Pingshuo site in northern Shanxi province, where Occidental Petroleum will help China develop its largest strip mine beginning in 1984. Occidental's Island Creek Coal Company has already submitted a proposal to provide a small ground station for this site. According to the company, this is the first time that China has considered installing satellite ground equipment at a mine, but the isolation of Pingshuo makes such an arrangement necessary. The coal ministry may also consider placing mobile earth stations in areas where mines are clustered.

The Ministry of Water Resources and Electric Power will use the Intelsat lease to improve communications between major hydroelectric power stations, such as the Tianshengqiao and Lubuge facilities in southwest China. In 1980 the ministry bought two small ground stations from Scientific-Atlanta Inc., now installed in Beijing and Chengdu. These stations are still not operative, and industry sources feel that they were sold before administrative and technical requirements were fully understood.

Five channels on the Intelsat lease will be used for transmission of meteorological charts from Beijing to other major cities, and a weather satellite will be developed.

By the time the five-year Intelsat lease expires in 1988, China hopes to have its own operational communications satellites in orbit. An experimental communications satellite was launched on January 29, 1984, after being postponed several times since 1980. China has put 14 satellites into orbit since 1970, including three experimental space physics satellites launched in 1981, and a reconnaissance satellite in 1983. The 1984 launch indicates that China has now developed the advanced rocket needed to place communications satellites in geosynchronous orbit.

BROADCAST SATELLITE

China expands domestic TV service

Apart from the important Intelsat lease, China also intends to purchase a direct broadcast satellite system that will enable the country to enjoy truly national TV coverage for the first time. The system should be operational by 1986 or 1987, and will be purchased from a foreign supplier.

Direct broadcast satellites represent a relatively recent technological advancement, and are designed to broadcast directly to individual homes via rooftop receiving stations. In China, where home TVs are a rare luxury, the system will serve community-owned TVs in factories, schools, and communes. China's national TV network currently operates only 47 stations to retransmit television broadcasts, as opposed to more than 700 in the US commercial network. Thus, as many as two-thirds of China's citizens probably lack access to

National Council Trip Identifies Business Opportunities in Telecommunications

A recent trip to Shanxi, Shaanxi, Hubei, and Sichuan provinces by National Council staff member Richard E. Gillespie has turned up new information on China's telecommunications plans that should generate foreign technology and equipment sales over the next three to five years.

▶ Telephone switching equipment ranging from the most advanced digital systems to second-hand crossbar exchanges will be imported as part of a national effort to improve telephone service. Emphasis over the next five years will be on placing digital exchanges in China's major urban areas, including Beijing, Shanghai, Tianjin, Guangzhou, Xiamen, Qingdao, and Dalian. The first major contract, a 1983 sales and technology transfer agreement for the ITT 1240 digital switching system (*see The CBR*, September–October 1983, pp. 40–42) will be primarily for Beijing and Shanghai. Other cities, and several ministries that operate their own telecommunications networks, are also shopping for digital switching systems. Tianjin contracted in late 1983 to import Nippon Electric's NEAX-61 digital switch, and China is looking at other Japanese switches as well.

Meanwhile, China will consider importing some used crossbar equipment to speed up the improvement of networks in all towns above the county-seat level. China now produces its own local crossbar exchanges, but not in sufficient quantity to replace all the manual and other obsolete systems scheduled to be phased out.

▶ Western technology will be imported to improve a broad range of transmission media. On the high end of the scale, China seeks foreign help to manufacture optical fiber and cable in Shanxi and Wuhan. Tests of 8 and 34 megabit systems are being conducted over 13.3 kilometers in the Wuhan area. Shanghai is another major center of fiber optics research and testing. Fiber optics will be used primarily for inter-city transmission in conjunction with digital switching. These improvements represent a quantum leap in telecommunications technology for China, and will enable the country to take better advantage of its upcoming satellite-based network.

▶ Copper, coaxial cable, and microwave transmission media are all receiving emphasis as open wire is phased out throughout the country. US technology was chosen for plastic insulated copper cable in Chengdu in Sichuan Province under a 1982 agreement with United Technologies' Essex Group. Anticipated start-up of production in late 1984 has stimulated demand for foreign assistance to produce related compatible components such as plastic telephone connectors in Xi'an.

▶ Another new plant near Chengdu will seek foreign assistance to produce multi-channel carrier telephone equipment needed for the 6,000 km of long distance trunk lines to be added by 1985. Work on the east–west line, running from Chengdu to Shanghai, began in July 1982 and is proceeding eastward through Sichuan province. The north–south line, now complete from Beijing to Shanghai, will be extended south to Guangzhou.

▶ China will probably seek foreign assistance to miniaturize and modernize its frequency division modulation (FDM) systems. FDM currently performs the bulk of the work distributing message traffic over microwave and coaxial cable. China now conducts research and limited production of 30 and 120 channel pulse code modulation (PCM) systems mainly in Beijing and Shijiazhuang.

▶ The Ministry of Posts and Telecommunications has come to realize the difficulties involved in achieving a more thoroughly integrated national telecommunications system and may seek foreign assistance to improve network design and planning. The Ministry of Posts and Telecommunications has recently asserted its role as overseer and coordinator of the various telecommunications networks operated separately by such ministries as Petroleum, Coal, and Water Resources and Electric Power. The pending US–China Telecommunications Protocol, which could be signed before President Reagan's planned trip to China in April, should facilitate US involvement in China's network planning. —MCR and REG

television reception. Without direct broadcast technology, it would be prohibitively expensive to change this situation in the near future.

In short, the broadcast satellite will be a vital element in China's plans to achieve a comprehensive radio and TV network by the year 2000. Ambitious projections call for TV reception stations in each of China's 2,138 counties. The Nanjing Radio Factory, which has already turned out several three-meter Ku-band aluminum TVRO stations, will seek foreign technical assistance to increase production to 800–1,000 such stations per year.

The broadcast satellite's most important short-term application will be to boost educational television programming. With university space for only 4 percent of China's high-school graduates, the national TV University represents the only option for many who would otherwise have no further educational opportunities. A broadcast satellite will allow for significant expansion of programming hours. The World Bank, which approved a loan of about $50 million to the TV University in September 1983, predicts a rise in enrollment from about 300,000 students to 1.3 million by 1990.

Competition is keen among firms capable of supplying the broadcast satellite system, worth at least $200 million. More than one satellite will be purchased, and US industry experts feel that three or four may be needed to achieve national coverage. A new organization called the China National Broadcasting Satellite Corporation, formed in late 1983, will acquire the satellites and coordinate the earth-station network.

RCA, Ford Aerospace, Hughes, Rockwell, and Comsat have all indicated an early interest in the project. Stiff European competition comes from Messerschmitt-Boelkow-Blohm (MBB) of West Germany and Aerospatiale of France. Several of these firms may combine forces in the bidding, including a possible MBB-Aerospatiale-Ford Aerospace consortium.

These manufacturers have been following China's interest in a broadcast satellite since the late 1970s. NASA and the Chinese Academy of Sciences signed an agreement in 1979 stating China's intention to purchase a US broadcast satellite system "under suitable conditions."

The entire project was shelved in 1980 during China's economic readjustment period, only to be revived by the State Council in early 1983.

Most observers doubt that the 1979 agreement will give a significant edge to US suppliers. From the start, the Chinese have insisted that transfer of advanced satellite technology accompany the purchase, something the US government is not prepared to permit, or at least not yet. An interagency group within the US government prepared technical transfer guidelines for the broadcast satellite in January 1984. While willing to wait for US clarification, China is not likely to back down on the technology transfer question, since it views this expensive investment as a way to strengthen its own space and electronic industries.

LANDSAT LINK-UP
Awaiting COCOM approval

China has used remote sensing satellite technology in several isolated projects, but plans a far more ambitious use of the Landsat satellite system in the near future. China will join about a dozen other countries that own and operate their own Landsat ground stations, and receive, process, and store data from the US-operated remote-sensing satellite. China's planned Landsat station, to be located near Beijing, will aid in agricultural research, hydrological surveying, mineral exploration, and city planning.

The Chinese Academy of Sciences and NASA signed a Landsat agreement in 1980, but sale of a ground station by the Land Resources Management Corporation was cancelled due to the company's internal difficulties. Shortly thereafter the Chinese signed a contract with a second US firm, the Systems and Applied Sciences Corporation of Vienna, Va. This turnkey sale, valued at about $12 million, includes a receiving station to be located 100 kilometers outside Beijing and a processing, analysis, and storage center in Beijing.

The Systems and Applied Sciences Corporation applied for an export license in April 1983, and received approval from the Commerce Department in December, reflecting the more liberal guidelines issued by the US government on November 21. If also approved by COCOM, the sale will break new ground in technology approved for export to China.

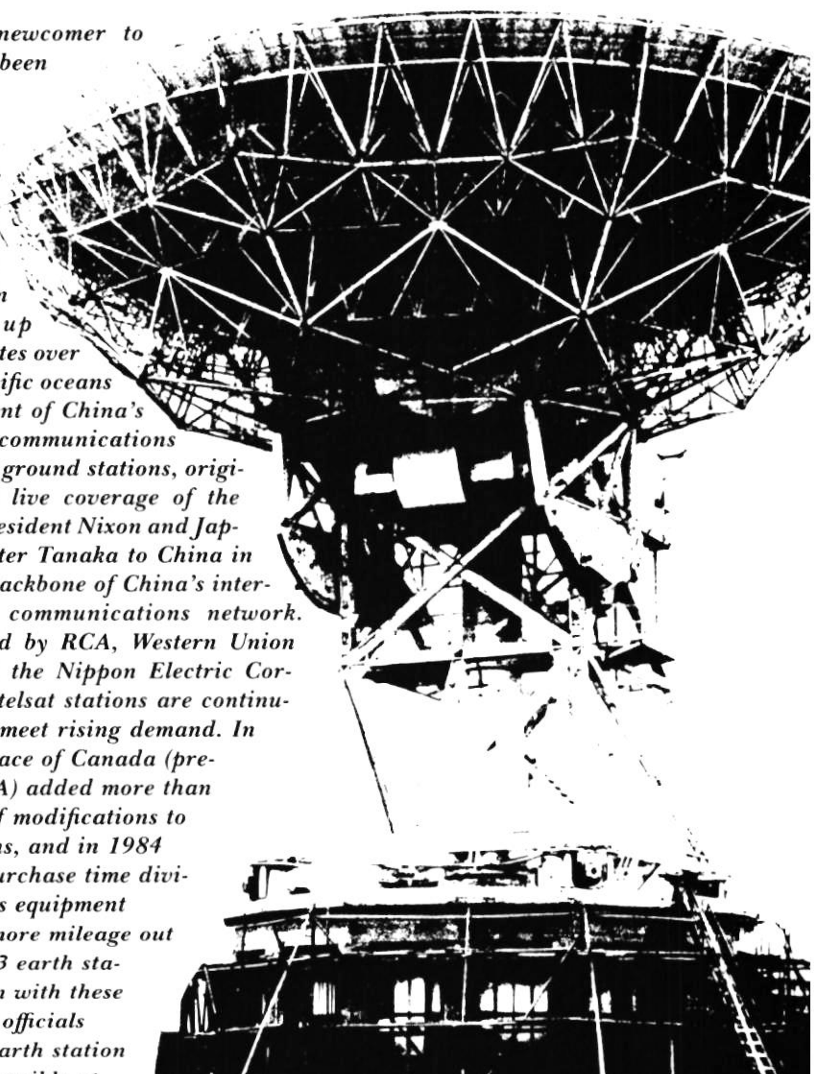
As with other satellite applications, China intends to go it alone as far as possible in the field of satellite remote-sensing technology. Research on remote sensing is a top national priority under China's current five-year plan, which extends through 1985. By then China hopes to have developed its first generation of domestically designed airborne remote sensors and digital-image analysis systems.

SATELLITE SPINOFFS
Terrestrial technology gets a lift.

These three new satellite systems are likely to produce an important ripple effect, stimulating improvements in terrestrial technology to support or link up with the satellite systems. The Intelsat lease, for example, will act as a spur to upgrade local telephone systems, including upgrading switching systems and transmission media. China's plan to install the latest digital switching equipment in 12 major cities and to install crossbar exchanges in smaller cities down to the county-seat level will help the local networks keep up with national improvements. The new emphasis on fiber optics is another logical outgrowth of these changes. Introduction of a broadcast satellite will lend impetus to plans to modernize radio and television transmitting equipment and increase television production. In short, China's leap into satellites seems certain to open new opportunities in terrestrial communications as well.

INTELSAT AND CHINA

Intelsat is no newcomer to China, which has been a member of the international organization since 1977. Three Intelsat Standard A ground stations in Beijing, and one in Shanghai, link up with Intelsat satellites over the Indian and Pacific oceans to handle 90 percent of China's international telecommunications traffic. These large ground stations, originally installed for live coverage of the historic visits of President Nixon and Japanese Prime Minister Tanaka to China in 1972, remain the backbone of China's international satellite communications network. They were supplied by RCA, Western Union International, and the Nippon Electric Corporation. These Intelsat stations are continuously upgraded to meet rising demand. In 1983, Spar Aerospace of Canada (previously part of RCA) added more than $5 million worth of modifications to two of these stations, and in 1984 China expects to purchase time division multiple access equipment (TDMADSI) to get more mileage out of the Beijing No. 3 earth station at Shahe. Even with these additions, Chinese officials admit that a new earth station may be required, possibly at Guangzhou. —MCR



Beijing 33-meter ground station purchased from RCA.

China's Fledgling Advertising Industry

The start of something big?

Scott D. Seligman

Advertising in China is an industry still very much in its formative stage. The Chinese have made notable efforts to set up an infrastructure for the development and placing of advertising. This includes establishing for-profit corporations to handle the business and developing regulations to guard against abuses. Foreign advertising is officially welcome, though it still accounts for only a small percentage of overall revenues; China has also consistently earmarked a small amount of precious foreign exchange for promotion of its products abroad. Though market penetration remains difficult for Western firms, some have met with successes, and major international ad agencies are now viewing China with cautious optimism. Advertising in China is already a business worth well in excess of $100 million annually, and as foreign trade continues to expand, it is certain to grow still larger in years to come.

Rehabilitating the Industry

Advertising only gained socialist respectability well after the close of the Cultural Revolution. Condemned as a capitalist tool with the sinister aim of deceiving the masses, advertising either became explicitly political or was shunned altogether. Advertising agencies that had existed in some cities prior to the turmoil of the 60s and 70s waited out the Cultural Revolution first by producing political posters and finally by ceasing activities entirely. Not until 1979 did the first local agency reopen for business.

The reemergence of advertising stemmed in part from an increasing willingness on the part of Chinese decision makers to rely on market forces to rationalize China's distribution system for goods and services. Editorials suddenly began to appear in the *People's Daily* touting advertising's ability to guide consumption and serve consumers; the former "capitalist tool" was restyled as "an important ground which will influence social morals and habits." Even brand consciousness and the use of trademarks have since been encouraged as part of the new emphasis on marketing.

If the decision to rehabilitate advertising was a difficult one, the idea of opening China's billboards and television stations to foreign ads must have incited fierce behind-the-scenes debate. A very pragmatic issue faced China's decision makers, apart from the ideological ones: Would rising expectations stemming from the Chinese masses' increased awareness of the outside world's standard of living be too high a price to pay for the foreign exchange revenue that taking advertising from abroad would easily bring in? The leadership may not have known the answers, but it was willing to take this calculated risk, and so in 1979 the gates were reopened to foreign advertisers.

Gearing Up for Business

Agencies in Shanghai and Tianjin were reportedly the first to reopen for business in 1979, with other localities following suit shortly. A year later the first organization charged with overseeing advertising activity nationally, the China United Advertising Corporation, was founded as an "integrated conglomerate." It officially opened for business in mid-1981.

China United was established under the auspices of the State Administration for Industry and Commerce (SAIC), the unit responsible for, among other things, licensing and registration of all enterprises in China (and for allocation of all billboard space as well). The corporation was set up in part as a placement agency to assist domestic units wishing to run newspaper, magazine, billboard, and broadcast advertising campaigns across China. It was also charged with conducting research on advertising literature and with training designers, technicians, and commercial artists. One of its other major tasks, however, was to bring under central government control through the SAIC's licensing authority all local corporations dealing in advertising, pointedly including many small agencies that until then had been operating more or less independently of regulation. These local units, which number more than 1,500 nationwide, are almost exclusively engaged in domestic business, which is the basic orientation of China United as well.

Not to be outdone, the Ministry of Foreign Economic Relations and Trade (now MOFERT, but then the Ministry of Foreign Trade) established the China National Foreign Trade Advertising Association in the second half of 1981. MOFERT saw the need to assert its authority over advertising that earned foreign exchange. Like China United, the association was charged with a coordinating role—regulating and overseeing about 21 local foreign trade advertising corporations (one per province, autonomous region, or municipal-

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Scott D. Seligman, director of Development and Government Relations for the National Council, also serves as the Council's sector analyst for the advertising industry in the PRC. He spent 1981 in China as the Council's Beijing Representative.

ity). It functions essentially as a trade association, on a not-for-profit basis, and undertakes activities designed to upgrade advertising in China, such as a recent national competition in export advertising photography. It is the agencies under the association's umbrella that are of principal interest to foreign advertisers.

The actual division of responsibility between China United and the Foreign Trade Advertising Association remains somewhat hazy, since both coordinate the work of local agencies, are empowered to accept foreign advertising, and assist clients in planning national ad campaigns. The chief distinction seems to be the association's power—which it derives from its close association with MOFERT—to appropriate foreign exchange for placement of Chinese advertising abroad.

The Chinese Media

Foreign companies wishing to advertise in China face a bewildering assortment of media—television, radio, newspapers, magazines, billboards, etc.—and precious little audience data. Often only sketchy profiles are given of target audiences (*e.g.* "20,000 responsible cadres in relevant work units"). Prices, however, remain relatively high. A 60-second prime time television network spot costs $5,500–$7,000, and only about 5 minutes of advertising time are available each day. Billboards are by far the most popular means of advertising because of their long duration, according to Jian Yaoxian, manager of China United Advertising, and can run as much as $12,500 for a 6 × 12 meter panel for six months in downtown Shanghai. For an ad in the *People's Daily*, which has a nationwide paid circulation of 2 million daily (and doubtless many times that number of readers), the charge is $90 per column centimeter. Full-page color ads in monthly magazines can run as much as $4,000, depending on the circulation; rates for technical journals can be less than half of that figure.

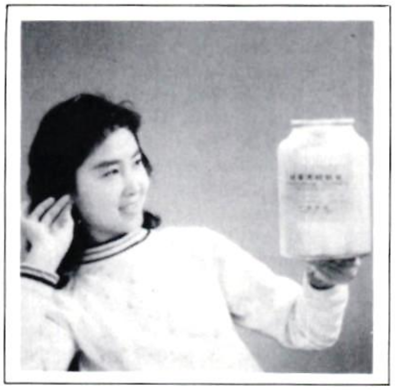
The array of services offered by the local agencies to the would-be advertiser is quite impressive, though quality of the finished product tends to vary from place to place. The Shanghai Advertising Corporation, generally conceded to be the most advanced, not only handles media placement, but also production (filmstrips, video tapes, photography, artwork, and printing), display work (especially for exhibitions), translation and publication, and even consulting for local manufacturers on marketing their products abroad. The agencies act as brokers for all media. According to the *China Daily*, the Beijing Advertising Corporation earned 37 percent of its revenues during the first half of 1982 on the sale of billboard advertising. Newspaper ads came next with 24 percent, followed by television (14 percent), store windows (7 percent), and magazines (6 percent).

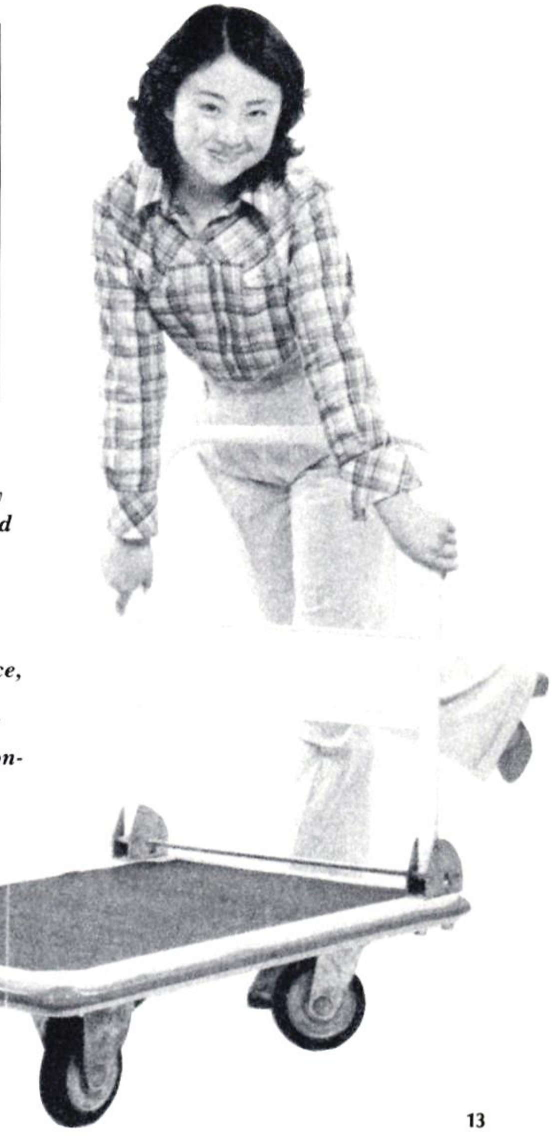
Still, foreign advertising accounts for only a relatively small percentage of China's total advertising revenue. According to Ying Xiuhua, secretary of China United's business department, only 10 percent of this revenue is attributable to foreign sources—a figure that amounted to about $7.7 million for all of 1982. The Shanghai Advertising Corporation earned fully one-third of the national take on foreign ads in 1982, with the Beijing and Guangzhou corporations bringing in about $2 million and $1.5 million respectively.

Regulating Advertising

Renewed activity in the advertising sphere brought with it the predictable backlash of criticism from unsympathetic bureaucrats. By early 1981, editorials in the *People's Daily* had begun detailing some of the abuses of unregulated advertising: exaggerated and even fraudulent claims, ugly and "sinister" displays, oversized or excessively lengthy ads, arbitrarily fixed prices in the ads, and promotion of goods unsuited to the Chinese market.

To address these and other concerns, and to supplement provincial-level efforts, the government issued a set of provisional regulations was issued in February 1982 and took effect in May of that year. The regula-





In details of two ads, one placed by the Hebei branch of SINOCHEM and the other by a hand-cart factory in Shandong, "sex, Chinese style" is used to sell some unlikely merchandise. At left, an attractive young woman gives a "come hither" glance, normally reserved in Western perfume ads for attractive members of the opposite sex, to an industrial container of streptomycin sulphate. At right, another's knowing look is intended to boost sales of Iron Bull brand hand carts.

tions limit authority to place ads to enterprises holding business licenses for this purpose, thus ruling out individuals and other units operating without the sanction of the central government. They stipulate that advertisements must be clear and truthful, and may not "hoodwink or deceive end-users and consumers." Nor may their content contradict state policies, divulge state secrets, be harmful to the dignity of China's nationalities, or be reactionary, obscene, crude, superstitious, or slanderous, according to the regulations.

Advertisers are required to obtain certification from a dizzying array of regulatory agencies: Public health agencies must pass on foodstuffs and medicines; quality control inspection agencies must testify to quality-grade claims; weighing and measuring instruments must be certified; and trademarks must be registered. The SAIC, named as the enforcement agency of the central government, may establish advertising fees through its local bureaus. It is also empowered to impose penalties on advertisers found in violation of the rules, including revoking licenses and even temporarily shutting down enterprises.

Market Access

A major constraint faced by foreign companies is that Chinese consumers lack access not to their ads, but to their products. As a result, few foreign firms are willing to advertise when ordinary Chinese generally are not permitted to buy their products. What little headway has been made is attributable to Japanese firms, which, according to C. Y. Chang, an account executive at Young & Rubicam, "have really paved the way in China." The Japanese have used mass advertising to stimulate demand for a range of consumer electronic products and appliances. Trademarks such as Seiko, Mitsubishi, Sony, and National are rapidly becoming household words in China.

Foreign tobacco, liquor, candy, cosmetics, soft drinks, and other consumer products have also made their way into China, but only as far as the shelves of the hard currency stores. Chinese authorities sell them on consignment, happy to pocket a convenient profit from the sale of foreign goods to foreigners. The various friendship stores and hotel lobbies where these products are sold do boast a considerable number of advertisements placed by the manufacturers, not an insignificant source of revenue. But with Chinese consumers by and large excluded from these stores, and in any case lacking the foreign exchange necessary to buy the products, the market remains restricted to outsiders.

Advertising Abroad

If a Chinese corporation wishes to promote its products abroad, it generally must work through MOFERT. A local branch of a foreign trade corporation (FTC) must submit an advertising budget to the ministry. This can be done either through the local foreign trade bureau (each province and municipality has one, which reports jointly to the governor or mayor and to MOFERT) or else through the FTC's head office in Beijing. It is the ministry's role to decide on the advertising budget (and it is no accident that the head of the Foreign Trade Advertising Association serves concurrently as the head of MOFERT's export–import bureau).

The only exception to this rule is when a Chinese organization or corporation has some foreign exchange of its own at its disposal—usually earned, in the case of a local factory or branch corporation, through exporting. In this situation the entity could theoretically go through China United to place advertisements abroad. Similarly, an autonomous government unit with access to foreign exchange of its own, such as CAAC, may deal directly with foreign corporations without reference to MOFERT. (CAAC has in fact just established a subsidiary firm that will handle the airline's promotion activities abroad beginning in January 1984.) But MOFERT remains the only entity in China with significant funds earmarked to spend abroad on advertising, and it is probably the only unit possessing the necessary expertise to do so effectively.

China actually spends far more in promoting its products abroad than its trading partners spend advertising in its media—perhaps as much as $100 million per year. More than half of this money is spent in Hong Kong, and probably only a few million dollars more are spent directly in Japan and the United States, according to Dr. Zou Siyi, the former head of the Foreign Trade Advertising Association who now directs the New York-based China United Trading Corporation (no connection with the China United Advertising Corporation). These figures seem high to a number of foreign observers, who estimate China's aggregate overseas expenditures in advertising as closer to $20–50 million. But the lion's

CHINA NATIONAL FOREIGN TRADE ADVERTISING ASSOCIATION

Aegis: Ministry of Foreign Economic Relations and Trade (MOFERT)

Established: August 1981

Address: No. 2 Dong Chang'an Street, Beijing

Telephone: 55.3031, ext. 397

Honorary President: Zheng Tuobin (Vice Minister, MOFERT)

Honorary Vice-President: Wang Pingqing (Minister's Representative, MOFERT)

President: Dai Jie (Director, Export-Import Bureau, MOFERT)

Advisors: Managing Directors of all professional advertising agencies and leaders of all large media agencies under the central government

Standing Committee of the Association: Beijing, Guangdong, Heilongjiang, Jiangsu, Shanghai and Sichuan Advertising Corporations and China Advertising Corporation (Hong Kong)

Members: Anhui Advertising Corporation, Anhui Foreign Trade Advertising Corporation, Beijing, Chongqing, Fujian, Guangdong, Guangxi, Hebei, Henan, and Heilongjiang Advertising Corporations, Hubei Foreign Economic and Trade Advertising Corporation, Hunan Foreign Trade Advertising Corporation, Jiangsu and Liaoning Advertising Corporations, Qilu Advertising Corporation (Qingdao), Guizhou Foreign Trade Advertising Corporation, Neimeng Advertising Company (Inner Mongolia), Shanxi and Shanghai Advertising Corporations, Sichuan Foreign Trade Advertising Corporation, Tianjin Advertising Corporation, Xinjiang Foreign Trade Advertising Corporation, Guangzhou Foreign Trade Center Exhibition Department, China Council for the Promotion of International Trade Public Relations Department, International Economic and Trade News, International Trade Magazine, Fashion Magazine, China Advertising Corporation (Hong Kong), Nanguang Trading Corporation, Exhibition Department (Macao)

The Japanese have used mass advertising to stimulate demand for a range of consumer electronic products and appliances. Trademarks such as Seiko, Mitsubishi, Sony, and National are rapidly becoming household words in China.

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share of the Chinese dollars that reach Western media do not take the form of direct expenditures, according to Zou, but rather of contract concessions earmarked for promotion activities.

Typically, a Chinese trading corporation will authorize an artificially high commission to an exclusive importer of a Chinese product in a Western market, with the proviso that a percentage of the commission be spent by the importer on advertising and promotion. This is the case, for example, with Bee and Flower Brand soap, distributed exclusively in the United States by Chinese Native Products, Ltd., an American company. The Chinese deduct 5 percent of the contract value on the condition that the firm use the funds—which amounted to about $40,000 this past year—on advertising. Sometimes the same result is accomplished through a gentleman's agreement, as in the case of Tsingtao (Qingdao) Beer, imported into the United States exclusively by Monarch Wines. Although the firm holds regular discussions with the Chinese on the advertising program, which was worth about $500,000 in 1983, there is no binding requirement to this end imposed in the contract. Such arrangements have proven to be an effective technique for Chinese corporations possessing little understanding of foreign media and even less of the Western consumer to mount quality promotional efforts abroad.

Indeed, Chinese attempts at placing ads directly in the US and Europe have been notoriously ineffective and at times even humorous. Brand names with unfortunate connotations for Western consumers abound ("White-Elephant" brand batteries, "Sea Cucumber" brand shirts, "Typical" sewing machines, and "Pansy" brand men's underwear, for example). Products have been pushed in amateurish magazine and newspaper ads. There is little understanding of targeting audiences through appropriate media: This past summer, for example, the *New York Times* carried an advertisement for dried vegetables from Fujian Province, and the *London Times* for "Snowflake" brand surgical dressings. Trade journals tend to be underutilized or improperly used. Not long ago *Chemical Marketing Reporter* carried ads promoting Shanghai-manufactured menthol crystals, even though virtually no opportunities exist for new buyers of this commodity.

CHINA NATIONAL UNITED ADVERTISING CORPORATION

Aegis: State Administration for Industry and Commerce (SAIC)

Established: February 1981

Address: Beijing Exhibition Hall, Beijing

Telephone: 89.0661, ext. 325

Manager: He Jingpei

Administrative Sub-managers: Ji Shun (Beijing), Wang Qingyuan (Shanghai), Zhu Yongan (Guangzhou)

Affiliated firms: 68 provincial and municipal advertising firms

The Role of Foreign Agencies

A number of international advertising agencies have been watching these developments since the 1970s, and some of them have already made significant inroads in China. The Western firms believe a good match can be made between their expertise in their home markets and Chinese exporters' desires to approach these markets in a more professional, sophisticated way. Many are interested also in assisting their foreign clients in spending their promotional dollars in China in the most effective way possible.

The agencies are not blind to the inherent limitations in the China market today. It is abundantly clear that as long as China's foreign exchange is so carefully husbanded, and the Chinese remain so cautious about spending large sums on "intangibles" like advertising (an attitude the domestic industry is trying hard to overcome), the country is unlikely to become the source of significant agency billings in the near future. Similarly, as long as China continues to restrict the importation of foreign goods and the amount of foreign exchange it makes available to its people to buy them, it is unlikely that the volume of advertising placed by foreign firms in China will grow significantly. Nonetheless, there is some business now and the promise of much more over the long run. The Japanese example of dogged investment in mass advertising and the limited market penetration that resulted is often cited as a reason for some optimism.

Apart from the Japanese agencies, three major American firms have led the pack: Young & Rubicam, Ogilvy & Mather, and Interpublic (the parent company of McCann-Erickson). The three have taken very different approaches to China, with Ogilvy & Mather forging exclusive agreements with local Chinese agencies, Interpublic (through its joint venture with Jardines) setting up an office in Beijing to place ads and solicit business, and Young & Rubicam preferring to bring importers and Chinese corporations together on joint promotions abroad. Other smaller agencies in Hong Kong and elsewhere have explored narrow areas such as selling Chinese TV and radio time, organizing video exhibitions, and employing direct mail marketing.

Young & Rubicam: Joint Promotion Building on China's penchant for cooperative efforts with its customers, Young & Rubicam (Y&R) pioneered the concept of promoting Chinese exports with joint funding from the Chinese and the major US importers

A comparison of two ads touting CAAC's service to Beijing illustrates the professionalism that a Western advertising agency can bring to China's promotional efforts. The ad at right, placed by Ogilvy and Mather, provides the reader with a detailed trans-Pacific schedule, lists fares, and emphasizes other selling points, while the one at left merely shows a traditional Chinese landscape painting—and not a very good one at that—with no information about the airline or its services.

(*see The CBR*, May–June, 1982, pp. 15–16). The idea was unusual in that the agency served to bring the other parties together. The first project, undertaken in cooperation with the Beijing carpet branch of CHINATUHSU and the Beijing Advertising Corporation, with three key carpet importers, involved the production of a series of films, ads, and brochures designed to educate the American public on how Tian Tan carpets are made in China. Now in its second phase, which involves increasing the amount of advertising and giving the films wider exposure, the arrangement has already proven profitable for all participants.

During 1982, with the cooperation of S. Shamash & Sons, Inc., a major US silk importer, Y&R proposed a communications program for the China Silk Corporation. In March 1983, China Silk, which purveys to the world silk market and oversees the mammoth Chinese silk industry, signed an agreement with Y&R to produce a film about silk-making. The agency choice derived in part from the successes of the Tian Tan carpet program.

Young & Rubicam, which has handled its China business through its Special Markets subsidiary in New York, has also done modest Chinese media placement for its American clients and US placements for some Chinese units as well. Y&R has also established formal contractual relationships with foreign trade advertising agencies in Beijing, Shanghai, Qingdao, Liaoning, Jiangsu, and other locations.

Ogilvy & Mather: Local Agency Agreements Ogilvy & Mather (O&M), which conducts its China business through its Hong Kong office and claims to handle the majority of China's spending overseas, has signed agreements with four local Chinese agencies—Beijing, Tianjin, Guangdong, and Qilu (in Qingdao)—to act as their primary agency in major world markets. The firm's China business is worth approximately $500,000, according to Harry Reid, regional director of O&M's Hong Kong office. In China, the firm represents such foreign clients as American Express, Rado watches, Boeing, and Phillips televisions. O&M is exploring a number of options for expanding its China business, including work in the direct mail area, possibly opening an office in Beijing, and perhaps following the Young & Rubicam model of foreign promotions financed jointly by PRC corporations and importers.

Interpublic: Teaming Up with Jardines Interpublic has served China until now through a joint venture between its subsidiary, McCann–Erickson, and Jardine Matheson & Company, a Hong Kong trading firm with more than a century of experience in China. At this writing a new company is being formed, and McCann–Erickson–Jardine will become Interpublic–Jardine, thus bringing under the umbrella a number of other agencies owned by Interpublic. The company is the only US agency to have a registered representative office (though not a full-service agency) in Beijing. Through an arrangement with Jardines it offers an "on-the-spot presence" in Shanghai and Guangzhou as well.

McCann–Jardine's 1982 billings were about $760,000, according to Angela Newsome, manager of the joint venture, who began as the company's first full-time Beijing representative in October 1980. About 90 percent of this figure is attributable to China business. Newsome expects the final 1983 figure to show an increase of about 70 percent, to a bit over $1 million.

Chinese export business accounts for about 30 percent of Interpublic's China-related billings. The firm handles Chinese accounts in two basic ways: full-service, which includes all creative work and a complete marketing and PR plan (the firm has such an arrangement with the Beijing Embroidery Corporation, an account worth $85,000 in 1983); and simple placement of export advertising (the Chinese do the media planning and the agency books space, assists with creative input, and produces materials). In the latter, the firm works with seven major Chinese agencies (Beijing, Shanghai, Guangdong, Tianjin, Fujian, Liaoning, and Qilu). Interpublic has signed "primary agency agreements" with major Chinese advertising corporations, which Newsome describes as "basically agreements to work through each other and not directly go to media or try to cut each other out." The firm also boasts one exclusive agreement with a Chinese entity, a 1981 contract with Guangdong province appointing it sole advertising agency for the province in the US. Interpublic also represents an impressive list of foreign clients in China: Gillette, Texas Instruments, Richardson-Vicks, Remy-Martin, British-American Tobacco, L'Oreal, Ernest Borel Swiss Watches, Coca-Cola, S. C. Johnson, and Kodak, among others.

Non-Agency Business

Not all PRC advertising is channelled through ad agencies, because Chinese media are not restricted from dealing directly with principals. A number of recent contracts build on the Chinese penchant for offering "income in kind" to foreign partners in place of foreign exchange up front.

For example, a number of recent joint publishing ventures have relied on advertising sales to repay the foreign partner. *Discover* magazine, now published in a Chinese language edition through an agreement between Time, Inc. and China Popular Science Press, sells ads to Western firms to generate income. Among recent advertisers in the magazine were Rolex, Philip Morris, and Standard Oil of Indiana. Under similar agreements, *Computerworld* and *Scientific American* are also being published in China.

Another such arrangement was struck by China's Central Television Network and CBS International of the US. In exchange for providing 400 million Chinese viewers with 64 hours of news, documentary, sports, and entertainment programming a year, CBS agreed to share with CCTV revenues on the sale of 320 minutes of commercial time, which could be sold to as many as 10 foreign sponsors for as much as $300,000 per 32-minute package. The network took responsibility for marketing the air time, and as of this writing had signed on several Fortune 500 firms as advertisers. The arrangement was to begin in October 1983 but has been delayed for a few months. Each company will present an "infomercial" about its business or an educational spot when CBS goes on the air in China, probably early this year.

One firm that has dealt directly with the Chinese media is Stauffer Chemicals. Last year the firm aired 30 prime time commercials on Chinese television touting ordram, a rice field weed killer. The ads describe the product and emphasize the company name, and give viewers information about how to go about making purchases. The 45-second spots, which cost the firm $6,000 each, have reportedly been extremely successful. "Not only farmers, but everyone you meet, including taxi drivers and cooks, know Stauffer ordram," claims one observer. To target further the appropriate audience, the company is now diverting some resources into scientific magazines and local radio, where the ads are aired just before the morning farm news.

The Chinese haven't lacked visits by executives of foreign ad agencies who travel to China from time to time to fly the company flag and see the Great Wall. Even smaller agencies have gone this far. But it is significant that relatively few companies have been particularly active in China to date and the few that have are sizeable firms that can afford not to be terribly concerned with short-term profits. Foreign advertising agencies are likely to continue to view China with guarded optimism over the short term: not forthcoming enough to justify a great deal of activity, but too important over the longer term to ignore completely. Knowing the Chinese penchant for dealing with "known quantities," the far-sighted agencies will probably choose to remain involved in the PRC on a project-by-project basis, continuing periodic visits to the local agencies and to the Beijing umbrella organizations. But significant billings attributable to the PRC are probably still some years down the pike. ⊄

To Advertise . . . Or Not to Advertise

Amoco Alan Groh, manager of public affairs: "We ran a print campaign from mid-1981 until the end of 1983, with 10–12 insertions per year in technical journals. Aside from personal contacts, advertising has been our main means of contact."

Westinghouse John Kreuthmeier, manager of business development, Nuclear Operations Division: "You get better impact for the dollar by putting it into a direct relationship [instead of advertisements]. You don't drum up much business by running an ad that says, 'For your next nuclear power plant, call Westinghouse.' "

Combustion Engineering Ron Kurtz, manager of advertising services: "CE is just starting an advertising campaign, with insertions in *International Trade News, American Exports to China, South Magazine*, and others. As we begin to develop more business, we feel more of a need to communicate our message."

Texaco Phil Husband, vice-president, Texaco Orient Petroleum: "I'm not positive how effective any advertising campaign may be. You target a few individuals and hope that when you meet them they recognize your company. We're not marketing a product. If I were selling sewing machines I might have a different attitude."

Avon George Ittner, director of corporate strategic planning: "I don't think we feel compelled to launch it [a moisture cream for China's domestic market] the way we would a product here, because by nature of it being Western and produced in cooperation with the Chinese, it has some differentiation from local products. But I do feel there needs to be more promotion to get the product across."

Hewlett Packard Chining Liu, PRC general manager: "We use the local newspapers and technical journals, and shy away from international papers and magazines. The locals, we feel, have better market penetration."

Cummins Engine Dennis Kelley, director of China operations: "I wouldn't go through Western publications that circulate in China. You can spend $10,000 in a technical book and you never hear anything again."

Gould Carl Sandberg, vice-president, International Business Division: "People should advertise in *The CBR* and cooperate on articles. Even though most of the distribution is outside China, the Chinese read that damn thing. If our company is mentioned in an article, it's super."

—Carol S. Goldsmith

CHINAMAGS

The drop in advertising dollars has forced many magazines out of the China market

Carol S. Goldsmith

In its September–October 1981 issue, *The CBR* reported that US publishers were producing 27 Chinese-language editions of US industry magazines in order to sell trade advertising. Then came the Great Magazine Shake-Out of 1982–83. As the Chinese scaled down their ambitious modernization plans, American publishers either reduced the frequency of their magazines or pulled out of China altogether.

Recently PennWell Publishing, which produces the Chinese-language *Offshore Petroleum* magazine, updated *The CBR*'s list to gauge the current state of the publishing/advertising market. The findings: Of the 27 magazines being produced or planned in 1981, only 10 are still with us. Agriculture, engineering, construction, and transportation have been the hardest-hit publishing categories.

Certain industrial sectors, however, have been showing progress of late. Ray Leung, PennWell's planning systems manager, believes that the appearance of more publications on high technology, petroleum, machine tools, medical equipment, and scientific research "to a large extent reflects the reallocation of national resources in the latest Five-Year Plan." He adds, "I am surprised at the poor showing of agriculture and food processing titles so far, and expect better times ahead."

CHINESE-LANGUAGE PUBLICATIONS BY AMERICAN PUBLISHERS

PUBLICATION, PUBLISHER	YEAR ESTAB-LISHED	FREQUENCY (×/year) Then (10/81)	FREQUENCY (×/year) Now (1/84)	CIRCULATION Then (10/81)	CIRCULATION Now (1/84)	AD RATES Full-Page B/W
Agriculture, Food, Forestry						
Agribusiness Worldwide/China, Intercontinental Publishing	1980	6	CP	18,000	CP	CP
Food Processing Magazine, Putman Publishing	1984	—	1	—	10,000	$2450.
Forest Industries, Miller-Freeman Publishing	1981	1	CP	NA	CP	CP
Milling & Baking News, Sosland Publishing	1980	1	CP	10,000	CP	CP
Poultry International, Watt Publications	1981	1	1	7,500	10,000	$2415.
*US–China Agriculture**, China Translation & Printing	1981	1	CP	20,000	CP	CP
*World Farming**, Intertec Publishing	1981	1	CP	11,350	CP	CP
Healthcare						
International Hospital Equipment/Clinical Laboratory International, Pan-European Publishing	1980	1	6	8,500	25,000	$2170.
Transportation/Railway						
*Railway Age/International Railway Journal/Track & Structures**, Simmons-Boardman Publishing	1981	1	CP	8,500	CP	CP
National Development China[1], Intercontinental Publishing	1979	4	CP	30,000–35,000	CP	CP
Construction						
Engineering News-Record, McGraw-Hill	1980	1	CP	20,000	CP	CP
Construction/Mining Buyer's Guide, McGraw-Hill/China Consultants International	1983	—	1	—	10,000	$3100.
World Construction, Technical Publishing	1981	2	CP	30,000	CP	CP
Marine Engineering						
*Marine Engineering Log**, Simmons-Boardman Publishing	1981	1	CP	8,000	CP	CP
Broadcasting						
Broadcast Engineering, Intertec Publishing	1981	1	1	8,500	8,500	$2752.

PUBLICATION, PUBLISHER	YEAR ESTAB-LISHED	FREQUENCY (×/year) Then (10/81)	Now (1/84)	CIRCULATION Then (10/81)	Now (1/84)	AD RATES Full-Page B/W
Chemicals						
Chemical Industries Buyer's Guide, McGraw-Hill/China Consultants International	1983	—	1	—	10,000	$3100.
Computers & Electronics, Telecommunications						
China Computerworld, CW Communications	1980	24	24	50,000	50,000	$3000.
*Computer Design**, PennWell Publishing	1981	1	CP	20,000	CP	CP
*US-China Electronics**, China Translation & Printing	1980	1	CP	20,000	CP	CP
Instruments & Computers for Research & Development, East-West Trade Publications	1983	—	6; Alternates w/following magazine	—	50,000	$2800.
Instruments, Computers, & Control Systems for Industry, East-West Trade Publications	1983	—	6; Alternates w/previous magazine	—	50,000	$2800.
Telephony, Telephony Publishing	1983	—	1	—	8,930	$1860.
Machine Tools						
Machine Builder, East-West Trade Publications	1983	—	12	—	40,000	$1800.
Machine Tool & Metalworking Focus, East-West Trade Publications	1982	12	12	50,000	50,000	$3000.
Modern Machine Shop, Gardner Publications	1984	—	1	—	15,000	$2250.
Paper						
Pulp & Paper International, Miller-Freeman Publishing	1981	1	1	8,000	8,000	$2150.
Mining/Coal						
Construction/Mining Buyer's Guide, McGraw-Hill/China Consultants International	1983	—	1	—	10,000	$3100.
Mining Equipment International[2], Technical Publications	1979	2	CP	25,000	CP	CP
World Mining/World Coal[2], Technical Publishing	1979	3 issues published since 1979	CP	20,700	CP	CP
Petroleum						
Oil & Gas Industry Catalogue, Chilton International	1979	1	CP	25,000	CP	CP
Offshore Petroleum, PennWell Publishing	1981	1	1	8,500	10,000	$2350.
Petroleum Production & Processing, Gulf Publications	1976	6	6	7,734	7,800	$1900.
Petroleum & Gas Industry Focus, East-West Trade Publications	1983	—	6	—	12,000–14,000	$1500.
Asian Energy Bulletin, Onshore-Offshore Publications	1982	—	6	—	6,000	$1455.
Petroleum Industry Buyer's Guide, McGraw-Hill/China Consultants International	1983	—	1	—	10,000	$3100.
Scientific Research						
Scientific American, Scientific American Publishing	1980	12	12	25,000	110,000	$15,000.
Discover, Time, Inc.	1983	—	4	—	40,000	$2520.
Business & Industry						
International Industrial Report,[3] China Consultants International/McGraw-Hill	1973	12	5	40,000	20,000	$25,000.
Modern Asia, Johnston International Publishing	1978	4	11	2,000	36,000	$2405.
Western Technology & Management, East-West Trade Publications	1981	4	CP	50,000	CP	CP

CP = Ceased publication. NA = Not available. * One-shot publication. [1] Started in 1979 as *Modern Engineering Technology*—Chinese edition; changed name to *Infrastructure China* in 1982, then to *National Development China*, which was published twice. [2] Both publications were purchased from Miller-Freeman and combined into *World Mining Equipment* (English-language). A Chinese version is being considered. [3] The five editions for 1984 are: *IIR/Textile World* (Aug.), *IIR/Chemical Engineering* (Sept.), *IIR/Aviation Week & Space Technology* (Oct.), *IIR/Power* (Nov.), and *IIR/Engineering News Record* (Dec.)
Chart prepared by PennWell Publishing; additional research by *CBR* intern Molly McKibben.

Insuring the China Trade

Most US firms are either under-insured, or not insured at all.

D. C. Chan Wai-Kown, Mitchell E. Cohen, and Joseph F. Ladman, Jr.

Last summer the China America Insurance Company, Ltd., a 50/50 joint venture between the New York-based American International Group (AIG) and the People's Insurance Company of China (PICC), conducted an extensive survey of 590 US firms involved or interested in doing business with China. The goal was to gain a better understanding of their insurance needs.

Out of the diversity of information received, one thing held true across the board: American firms doing business in China are inadequately insured. While many rely on their worldwide covers for insurance, more than half the companies have no insurance at all.

The writing of domestic insurance in China has been permitted only since 1979, when the central government lifted a 21-year-old ban. Since 1980, the year the joint venture with AIG was formed, PICC has been the sole admitted carrier in China handling foreign and domestic risks. Foreign insurance firms are treated as "nonadmitted" carriers, meaning that they cannot solicit insurance under Chinese law in the PRC, though these firms can insure foreign investment in China other than true joint equity ventures. Moreover, foreign companies can use nonadmitted carriers, such as China America, when they perceive a potential conflict of interest, or see a need for worldwide representation.

Inadequate coverage

The survey indicated that more than half of the American firms doing business in China do not have any insurance at all. Of those that had insurance, fully 20 percent could not say what particular coverage they did have. Of the companies that do carry insurance, ocean marine and inland marine are the most commonly held coverages. Presumably, many firms depend on the adequacy of their worldwide marine coverage in China. But this may be unrealistic, since several types of risks are not covered. Most marine insurance is handled by PICC, as it is China's practice to purchase FOB (free on board) and sell CIF (cost, insurance, and freight) in order to control shipping and insurance and maximize its revenues from international trade.

The survey also indicates that two-thirds of all US firms with production facilities in China do carry some insurance. These tend to be coverages that are specific to each type of facility. Among firms providing services to China, less than 20 percent carry any insurance at all. Among those that do, coverages such as political risk, third-party liability, and other important service-related categories were rarely mentioned by the firms surveyed.

A worst-case scenario

Many companies undoubtedly are wondering why they need special coverages in China. A worst-case scenario offers a number of important reasons:

Suppose a US company builds a facility in China to produce electronic equipment. Some of the parts are imported. One night the plant burns down and some of the workers are injured. The company's PRC manager, who has been to a dinner party, hears about the fire and drives immediately to the plant. On the way he collides with another foreign driver, who has to be hospitalized.

The company learns that it has only a worldwide marine policy and PICC automobile coverage. Its plant is not covered for property loss; neither is the business interruption caused by the fire. Although the injured workers are cared for by the Chinese government, some of the injured foreign workers will sue in US courts. This liability is not covered. Finally, since the manager had a few drinks at the party, he finds that the auto accident is not covered because of an exclusion in the auto policy.

Suggested coverage

Though a hypothetical example, such incidents have actually occurred. This may prompt some US executives to wonder: "What insurance should the facility have had and where should the coverage have been purchased?"

When considering insurance in China, the differences between the US and PRC litigation systems becomes a major factor. There is no tort law in China. Consequently, third-party liability claims are settled through negotiations. A carrier with representation in China has a clear advantage in obtaining a favorable settlement. Claims also can be litigated outside China. Where multinationals are involved, the injured party can sue in the country of the firm's origin. Where this occurs, carriers should have worldwide experience.

Since most business relations with China involve trade, transportation coverage should include typical

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ocean cargo coverage. If purchased from PICC, then a difference in conditions (DIC) cargo policy—which includes inland transit and loading and unloading—can be purchased from a nonadmitted carrier.

If production or distribution facilities are located in China, then location coverage, business interruption, political risk, contract repudiation, and export credit should be purchased. Workers' compensation is also available, though not required since the PRC cares for injured workers. Nonetheless, there is a need for workers' and employers' liability and general liability coverages when a foreign enterprise employs PRC nationals or there is any risk to foreigners. Under the Jones Act, the injured worker can bring suit in US court for damages caused by a US company. Both the magnitude of settlements awarded in the US, and the need for a working knowledge of the US legal system, suggest purchasing workers' compensation from an international nonadmitted carrier.

Automobile coverage should be carried on vehicles owned or operated in China. PICC coverage has some exclusions not found on coverages of nonadmitted carriers.

Although many of these coverages are available from PICC, in those instances where the risk involves some action by the state, the insurance should be supplemented or bought from a nonadmitted carrier. Political risk coverage, for example, is readily written by PICC, but is likely to include some action against the facility by the state. Since PICC is state-owned, potential conflict can be avoided by obtaining the coverage through a nonadmitted carrier. Similar logic applies to coverage for contract repudiation, workers' compensation, and business interruption.

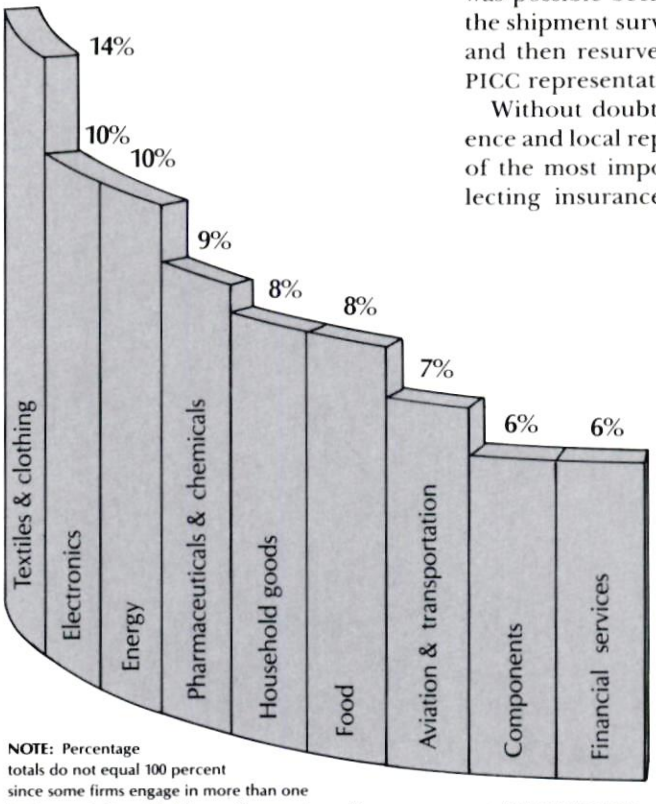
Another key factor in evaluating carriers is their ability to provide service for claims handling and settlement on a worldwide basis. In one instance, a chemical firm shipped a cargo of bagged chemicals to China via Hong Kong. The goods were damaged. An evaluation of the damage was possible because the carrier had the shipment surveyed in Hong Kong and then resurveyed in Shanghai by PICC representatives.

Without doubt, worldwide experience and local representation are two of the most important factors in selecting insurance carriers for business in China. In addition, company executives should seek carriers that can recommend, or offer, the following types of insurance: transportation or ocean cargo coverage extended to include a company's inland exposure; location coverage for such items as plant equipment and raw materials, obtained through PICC or a nonadmitted carrier; business interruption and loss of earnings; political risk, contract repudiation, and export credit (preferably written through a nonadmitted carrier); workers' compensation for expatriates employed in China; workers' and employers' liability (required for all firms employing PRC nationals); general liability; and automobile insurance.

PRINCIPAL BUSINESS ACTIVITIES OF FIRMS SURVEYED

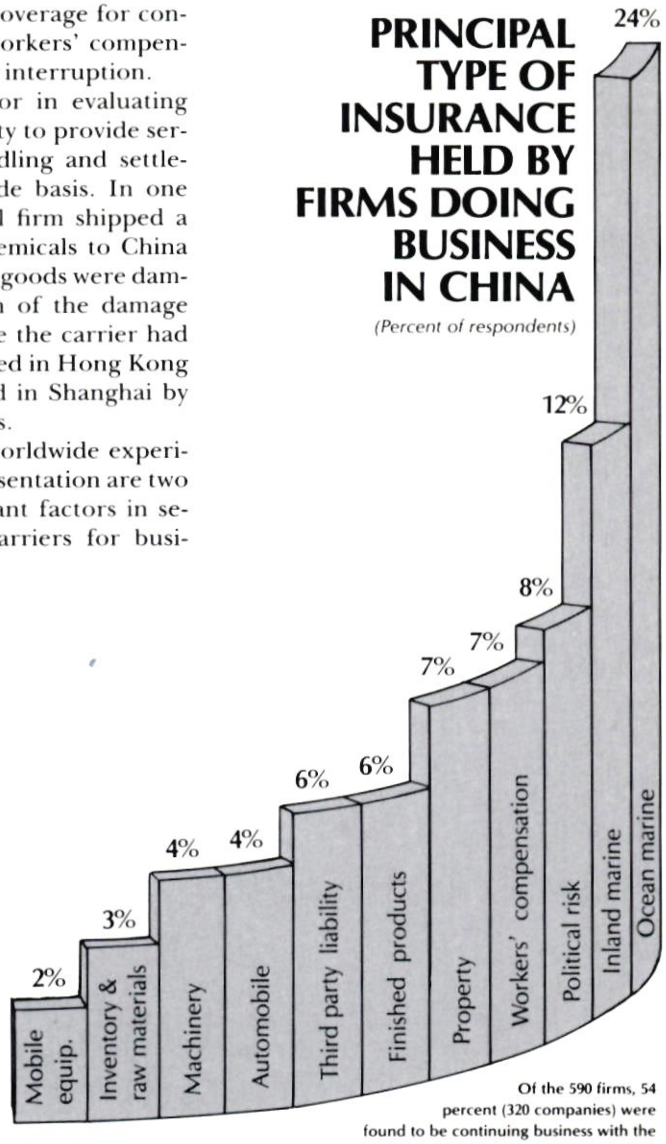
(Percent of respondents)

Artwork by John M. Yanson



PRINCIPAL TYPE OF INSURANCE HELD BY FIRMS DOING BUSINESS IN CHINA

(Percent of respondents)



NOTE: Percentage totals do not equal 100 percent since some firms engage in more than one business activity and hold more than one type of insurance coverage. **SURVEY METHODOLOGY:** For the survey, the American International Group identified 590 US companies either doing or contemplating business with China. Public information used to compile this list came from the National Council for US-China Trade, the State Department, and various articles and directories. In June 1983 a three-page survey was mailed to the risk manager or chief executive officer of each firm. The completion rate was 31 percent. Of the 590 firms, 54 percent (320 companies) were found to be continuing business with the PRC, while 8 percent were still planning to do business. The remaining 38 percent had discontinued any plans to enter the China trade. A follow-up mailing was sent in July, and a telephone campaign conducted in August. Answers were weighted to account for non-response. Mail responses received a weight of one and telephone responses a weight of four. Additional detail on methodology is available from AIG's Corporate Marketing Research and Development Department. Telephone: 212-770-5294.

Tax Treatment in China

Consider your tax liability when considering a venture or sale.

Timothy A. Gelatt and Eugene Theroux

Foreigners doing business with China find it increasingly necessary to analyze the tax implications of each transaction and to practice tax planning. The decision of whether to form a joint venture or simply license technology to China, for instance, may be influenced by the different results of each project under the foreign enterprise income tax. Similarly, the difference in tax treatment may be an important factor in the choice between an equity and a cooperative joint venture. These considerations will become apparent in the following review of the practical tax consequences of each of the common forms of doing business in China, from simple sales to equity joint ventures.

Individual Income

The general structure of China's individual tax system is found in the Individual Income Tax Law (IITL) as amplified by the regulations of 1980, and various supplementary documents and administrative practices.

Under the terms of the IITL, individuals who reside in China for 90 "consecutive" days or less are exempt from the individual income tax on compensation paid by an employer "outside China," that is, a foreign company that does not have a tax "establishment" in China. Individuals who reside in China for more than 90 days are subject to taxation in China on all income gained within China.

The 90-day rule is applied rather differently than the language of the IITL would appear to require. Holders of visas valid for more than 90 days are treated as residents of more than 90 days and are subject to taxation on all their wage and salary income for the entire period of the visa, even if they should leave China and return during the period of the visa. Only if a foreigner leaves on or before his 90th day in China without an intention to return on that visa, can he potentially rebut the presumption of residence and enjoy the 90-day exemption.

A foreigner who enters China on short-term visas, typically of 30–60 days' duration, becomes subject to taxation on all his wage and salary income from his initial date of entry if he accumulates a total of 91 days in China with no absence of more than 30 days between visas. An absence from China of more than 30 days has the effect of canceling time previously spent in China for purposes of calculating the 90-day period. The fact that accumulated days straddle more than one tax year is disregarded for purposes of this rule; that is, 60 consecutive days spent in China during November and December and a further 31 consecutive days spent there during January will be counted as 91 days' residence for individual income tax purposes.

Categories of income subject to the individual income tax are ▶ wages and salaries, ▶ compensation for personal services, royalties, interest, dividends, and bonuses, ▶ income from the lease of property, and ▶ other kinds of income as specified by China's Ministry of Finance. Most foreigners in China are affected only by the tax on wages and salaries.

Income taxable as wages and salaries includes base salary, per diem or other fixed subsidies, and bonuses. A foreign company's payment of personal expenses is taxable as part of wages and salaries. A foreign company's payment of business expenses—such as accommodation, transportation, communications, and the like—does not result in taxable income to the employee, but appropriate receipts and records should be maintained for verification. In some cases, payment of an employee's Chinese tax by his employer may result in taxable income to the employee. This may generally be expected to occur when foreign companies with tax establishments in China deduct their employee's wages for Chinese corporate tax purposes.

Only wage and salary income "gained within China" is taxable. The Chinese tax authorities, however, define income "gained within China" as all wage and salary income earned during a foreigner's "residence" in China. As previously indicated, "residence" in the Chinese definition may include time spent outside of China. Thus, a foreigner with a six-month multiple-entry visa who spends only four of those months actually in China is a "resident" for six months, and is thus taxable on six months' wage and salary income. A foreigner who, in the course of 125 calendar days, accumulates 91 days in China, with no absence of over 30 days, is taxable on his wages and salary for the entire 125 days, since he is viewed as a "resident" for that period.

All categories of income *other than* wages and salaries are taxed at a flat rate of 20 percent. Wages and salaries are taxed at the following rates:

Monthly income in Chinese renminbi (RMB)	Tax rate
0– 800	0
801–1,500	5%
1,501–3,000	10%
3,001–6,000	20%
6,001–9,000	30%
9,001–12,000	40%
More than 12,001 ($6,061)	45%

Note: dollar figure is based on year-end 1983 exchange rate of ¥1.98 to the dollar.

As indicated by the above table, taxpayers are allowed a standard deduction of ¥800 per month from wages and salaries. No other deductions of any kind are generally allowed.

Foreigners who are subject to individual income tax must register with the local tax authorities, submit a tax declaration form, and pay tax due within seven days after the end of each calendar month.

Sales to China

In the current view of China's tax authorities, the simple sale of products to China by a foreign company does not give rise to taxable income under the Foreign Enterprise Income Tax Law (FEITL), promulgated on December 13, 1981. Of course, a foreign company selling equipment or machinery to China may send employees to the end-user's site for a period of time to provide installation, training, or other services. The income from these services would be taxable at the FEITL's progressive rates, even though the sales income is not, if the foreign company is seen as having created an establishment under the FEITL. In a recent regulation, the Ministry of Finance stated that through 1990 companies in this situation will not be taxed on the establishment basis. If, however, the services a foreign company performs in connection with sales to China involve the transfer of proprietary technology, the company will become a taxpayer under the FEITL's "non-establishment" withholding tax, which covers "fees for the use in China of proprietary rights."

Technology Transfer

Companies transferring technology to China, while not taxed on the basis of having establishments in China, must pay the FEITL's withholding tax on income earned from "fees for the use in China of proprietary rights." This term covers not only licensing fees or "royalties," as the term has sometimes been translated, but also technical training fees, fees for technical documentation, or any other fees paid for the transfer of the right to use proprietary technical information or know-how.

In an attempt to counteract the dampening effect of the withholding tax on technology transfer to China, the Ministry of Finance issued regulations on December 13, 1982 that reduced the tax to 10 percent on fees earned in a broad range of technology areas. These include nuclear technology, certain types of computer technology, and technology used in agriculture, energy exploration, and conservation. The tax may be eliminated altogether when technology in these areas is "advanced" and offered at "preferential" terms.

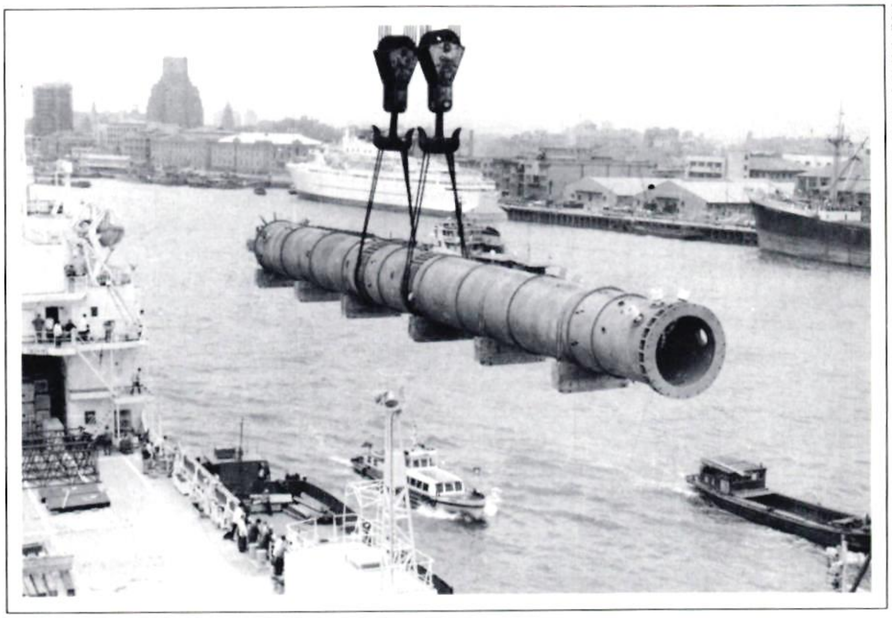
The local tax authorities must approve the 10 percent tax reduction upon receiving the opinions of the organizations that approve a technology transfer project. Total exemption from tax requires Ministry of Finance approval. According to Finance Ministry officials, the ministry evaluates the "advanced" and "preferential" nature of technology through a comparative process, taking into consideration the relative effectiveness of the technology in meeting China's needs, and the attractiveness of the entire contract package—including pricing and the provision of training and services—in comparison with other technology available to China.

Although these revisions in the withholding tax were certainly welcomed by foreigners, their implementation has been less than satisfactory. Thus far foreign companies have been unable to obtain advance rulings from the tax authorities as to whether their particular contract qualifies for a reduction or exemption in the withholding tax. Foreign companies are dependent on the Chinese party to initiate the tax review process—which apparently cannot begin until after the contract has been signed. Under these circumstances, a company might assume that it is subject to 20 percent withholding tax, and formulate its commercial terms accordingly.

Lending and Leasing

Foreign banks with representative offices in China are not considered to have taxable establishments. As a result, the interest earned by these and other foreign banks on loans to China is subject only to the FEITL withholding tax. Exemption from this tax is available to foreign banks lending to the Bank of China and other state banks and to certain Chinese trust and investment corporations at "preferential" rates. The FEITL defines "preferential" to mean rates at least 10 percent below prevailing international market rates. A 1983 set of Ministry of Finance regulations provides that foreign banks, upon the approval of local tax organs, may be exempt from the withholding tax on loans made to China's state banks, authorized trust and investment companies, and the China National Offshore Oil Corporation at the London Interbank Offered Rate (LIBOR) or similar interbank rates. In practice, loans carrying a margin of up to 0.5 percent over LIBOR may still qualify for tax exemption, depending on their term.

The regulations also reduce the withholding tax rate to 10 percent for all loan contracts signed between



New China Pictures Co.

Under the Foreign Enterprise Income Tax Law, the simple sale of products to China does not give rise to taxable income.

1983 and 1985 that do not qualify for complete tax exemption. Contracts signed and approved before the January 1, 1983 effective date of the regulations remain subject to the old 20 percent rate for the life of the contract.

In an attempt to ease further the tax burden of banks with representative offices, the Ministry of Finance permits representative offices that sign loan agreements "directly" with Chinese entities to pay their taxes at the FEITL's progressive rates, applied to a "deemed profit" of 15 percent of the interest income under the agreement. This should result in a lower tax than the withholding tax on gross interest income, even when the withholding tax is applied at the reduced 10 percent rate. For instance, if the highest FEITL rate of 50 percent including local tax were applied to the 15 percent deemed profit, the effective tax rate would be 7.5 percent. The theory behind this mechanism is to allow representative offices to offset, at least partially, their high costs of doing business in China.

The problem with this attractive-sounding approach is that when a foreign bank's representative office signs a loan agreement in China, it appears to be violating the regulations of the People's Bank of China that require bank offices to register in China. These regulations prohibit representative offices from engaging in "direct profit-making business activities." While the Ministry of Finance does not see this as a problem and claims that signing an agreement is not a "business activity" but merely a ministerial act the representative office performs on behalf of its parent bank, the People's Bank does not agree. Indeed, the People's Bank apparently intends to revoke the registration certificate of any bank office that signs a loan agreement to take advantage of the special tax treatment.

Also subject to the FEITL withholding tax is income derived from the rental of property used in China. Straight rental payments are generally taxable to the foreign lessor at 20 percent under the FEITL withholding tax. Special tax treatment, however, applies to "lease-sale" or "hire-purchase" transactions. In these transactions, a leasing company rents a piece of equipment to a Chinese unit that ultimately intends to purchase the equipment. Hence, this is not a pure rental transaction, as the payments under such "lease-sale" arrangements contain a portion attributable to payment of "principal", or the equipment's purchase price. These payments also include a component that can be called a "lease" fee, but actually represents interest—the leasing company's cost of funds borrowed to obtain the equipment. Finally, payments made to the leasing company include a service charge, or spread above the leasing company's cost of funds.

Under the Ministry of Finance's 1983 regulations concerning the tax on interest, the portion of lease-sale payments reflecting a contribution toward the purchase price is exempt from tax. In addition, the regulations reduce the tax on the interest component to 10 percent for transactions made between 1983 and 1985, and provide for a total tax exemption on interest in lease-sales when the interest rate is no higher than the rate the Chinese lessee pays to finance its payments under the transaction. The leasing company's spread is in any event taxable, but at the reduced rate of 10 percent for transactions between 1983 and 1985.

Representative Offices and Business Agents

A representative office is an "establishment" for purposes of the FEITL only if it engages in "production or business operations," according to the FEITL. Chinese tax officials have repeatedly stated that they do not view the representative offices of foreign industrial or manufacturing companies as "operating" establishments. Rather, they regard them as liaison centers, engaging in market development and exploration of business opportunities. As the tax officials point out, under the Chinese regulations governing the registration of representative offices, these offices cannot engage in actual "business activity." The fact that many of these offices do conduct business negotiations and even sign contracts in the name of their head companies does not seem to alter current Chinese thinking. Consequently, an industrial or manufacturing company having only a representative office in China is treated as a company without a China establishment. The company is taxed under the FEITL's withholding tax on technology transfer, interest, or other relevant income it earns from China.

Chinese tax officials regard the offices of foreign service companies such as consultants, accountants, and trading companies in a different light. These offices must be registered as "representative offices" under the same regulations that govern industrial and manufacturing companies. These offices, however, provide professional services to outside clients on a fee basis in addition to performing general liaison and information services for their home companies. Chinese tax officials regard these fees as income generated by an operating establishment, which should be taxed under the FEITL progressive tax.

The treatment of service company offices as establishments would presumably require that these offices also pay the industrial and commercial tax on service income. Whether or not a representative office is treated as a FEITL establishment, it pays the Consolidated Industrial and Commercial Tax, as well as import duties, on the importation of goods such as office equipment.

Some companies do business in China not through their own representative offices but through one of the many foreign trading companies or consulting firms that have set up representative offices in China's major cities. As indicated, these trading or consulting firms are viewed as being taxable on the commissions and other fees generated by their representative offices. More uncertainty surrounds the clients of these firms. According to one possible interpretation of the FEITL, any foreign company transacting business through another firm operating in China could be seen as having "set up a business agent in China," thereby having an establishment in China. Chinese tax officials, however, have expressed their intention to incorporate into the FEITL the common distinction between "independent" and "dependent" agents. If this distinction is adopted, a foreign company's use of a trading or other firm that acts for other companies will not create an establishment for purposes of the FEITL. On the other hand, the appointment of an agent that acts exclusively for the foreign company will create an establishment and subject the foreign company to the net income tax on any income covered by

The most advantageous tax holidays in Special Economic Zones are generally available to enterprises with an investment of more than $5 million involving relatively high technology.

the FEITL. Thus far, no clear policy has emerged regarding agents.

Consignment Sales and Service Centers

A foreign company that signs an agreement with a Chinese corporation under which the latter sells the foreign company's products on a consignment or agency basis, or under which the Chinese set up a service center to service and sell parts for the foreign company's machinery in China, may be subject to tax under the Consolidated Industrial and Commercial Tax, the FEITL, or both. A recent Ministry of Finance tax notice provides that in cases where an independent place of business is established with its sole or primary function being the agency sale of a foreign company's products or maintenance of and sale of parts for a foreign company's machinery, the foreign company will be subject to the Consolidated Industrial and Commercial Tax on any income it derives from the sales or service establishment as well as to the FEITL on any "profit" it earns from the establishment.

If, on the other hand, no business establishment is specially set up but the Chinese corporation simply sells a foreign company's goods on a consignment or agency basis, the foreign company will in no event be subject to the FEITL. It may be subject to the consolidated tax, depending on the nature of the consignment or agency arrangement. If the Chinese do not actually purchase the goods and sell them at a price set by the foreign company, or at a mutually agreed price—the parties sharing the sales proceeds according to an agreed ratio—the foreign company will be subject to the consolidated tax on its share of the sales proceeds. If, on the other hand, the Chinese import the goods from the foreign company and resell them at a price established by the Chinese party, the foreign company will be exempt from all tax as in the case of any sale to China.

Compensation Trade

Compensation trade can be viewed as a loan of machinery or equipment, with principal and interest repaid in kind, or as a lease-sale or installment purchase arrangement, with each in-kind payment including a lease fee and a contribution toward the purchase price. Compensation trade contracts involving the transfer of technology generate technology fees paid in kind.

To a Western legal eye, compensation trade projects would appear to fall under the FEITL's definition of an establishment. But Chinese tax officials have stated that they do not see compensation trade as creating an establishment under the FEITL. As a result, foreign companies are taxed on the in-kind payments representing interest, technology, or service fees under the 20 percent withholding tax. The amount of this tax is withheld in kind.

In its 1983 regulations on interest, the Ministry of Finance made a provisional exemption from the FEITL withholding tax, with the approval of local tax authorities, for both interest and leasing fees paid in kind. No explicit exemption has been made from the FEITL withholding tax for technology service fees paid in kind. However, under the 1983 regulations providing tax exemption for "advanced" technology offered on "preferential" terms, the fact that payments may be made in kind, saving foreign exchange, will in many cases be considered a "preferential" term. These, too, may be exempt from tax.

As a result of these various provisions, few foreign companies engaging in compensation trade are likely to be subject to Chinese taxation.

Cooperative Ventures

In cooperative ventures, also known as coproduction or "contractual" (non-equity) joint ventures, the Chinese and foreign parties contribute resources or technology and share profits according to a contractual formula. No Chinese legal entity is formed, as in equity joint ventures. In the typical cooperative venture, the Chinese and foreign parties calculate and pay their own taxes—the Chinese under relevant domestic tax legislation and the foreign party under the FEITL and other relevant tax laws.

Foreign companies engaging in cooperative ventures have an establishment in China and are taxable under the FEITL on their Chinese-source net income at progressive rates. Foreign companies receiving their profits from cooperative ventures in the form of goods produced by the venture calculate their gross income based on the sales price to a third party or, if no third-party sale takes place, by reference to the prevailing market price of the goods in question. The "market price" refers to the current sales price in China of the goods.

The foreign participant in a cooperative venture is generally subject to the Consolidated Industrial and Commercial Tax and customs duties on goods imported for the venture. Foreign companies participating in cooperative petroleum projects benefit from special exemptions from the consolidated tax and duties.

The consolidated tax is also imposed on the foreign party's sales or service income from the cooperative venture. If the foreign party receives its profits in kind, the consolidated tax is applied to the sales proceeds when the products are sold. If the foreign company does not immediately sell its in-kind distribution, but rather takes its in-kind share out of China for later resale on its home market or the international market, the Chinese may assess the consolidated tax in kind, or apply a "prevailing market price" criterion such as that used for purposes of the FEITL. In the case of cooperative offshore oil projects, the consolidated tax is levied in kind.

The Chinese have also stated that the industrial and commercial tax on the exports of cooperative ventures may be waived upon application to the tax authorities, if payment of the tax causes "difficulties." It is unclear whether this favorable treatment would be available only to the Chinese side on its share of export proceeds, or also to the foreign party. Foreign companies paying the industrial and commercial tax on sales or service income may, in any event, deduct the tax paid in computing their taxable income for purposes of the FEITL.

Before leaving the subject of cooperative or contractual joint ventures, it should be noted that the Chinese sometimes refer to a "type A contractual joint venture." Despite its name, this type of venture shares most of the characteristics of an equity joint venture. Indeed, for many purposes—including taxation—these ventures are treated like equity joint ventures. It is important for a foreign investor to clarify from the outset with its Chinese negotiating partner what kind of entity is under discussion, to avoid later surprises.

Contracted Projects

A foreign company with business activity that is what the Chinese call a "contracted project," such as a construction, installation, or assembly project, has an "establishment" in China by virtue of the project "site," and is therefore taxable under the FEITL on its Chinese-source net income at the progressive rates.

The definition of a contracted project site could encompass three situations that are common in China. The first includes the case of a foreign company that sells equipment to a Chinese entity and then sends employees to the customer's site to provide ancillary installation, construction, training, or related services. The second situation involves a foreign company that contracts with a Chinese entity, or a foreign entity operating in China, for a service project, with perhaps the incidental sale of some machinery or equipment. This situation includes foreign subcontractors hired by foreign operators in China's offshore oil development projects. The third situation covers a foreign company that provides on-site installation, training, or other technical services in conjunction with a transfer of technology.

The first situation has been explicitly exempted from establishment tax treatment through 1990. Also exempted through 1990 is the on-site provision of technical instruction, consultation, and other technical services to Chinese enterprises for the reform of their existing technology. In the case of a foreign company's provision of technical services in connection with a transfer of new technology, the Chinese have also not applied the usual taxes associated with having an establishment in China.

Only the second situation described above, in which the sole or primary purpose of the contract is to perform services in China, has been subject to the establishment tax under the FEITL. Companies that cannot adequately substantiate their costs and expenses for purposes of calculating taxable income under the FEITL have in the past been allowed to pay the FEITL rates applied on a deemed profit of 10 percent of their total receipts from a project. This deemed profit rate and the use of the deemed profit system in general are currently under reevaluation by the Ministry of Finance.

The Chinese have not set a minimum period within which a contracted project can be completed without creating an establishment for tax purposes. The FEITL regulations provide only that foreign enterprises that have operated in China for less than one year are taxable on the income earned during the actual period of operation. In addition, the regulation outlining the deemed profit tax system mentioned above states that this system is particularly intended to meet the needs of companies involved in "relatively short" projects, suggesting that no minimum period is contemplated for tax purposes. Chinese tax officials, however, have stated that they intend to set a minimum period within which a project can be completed without creating an establishment, an approach used by some other countries and often incorporated into tax treaties.

Service income earned by foreign companies from contracted projects in China is subject to the Consolidated Industrial and Commercial Tax. The Ministry of Finance has made the same exemptions under this tax, also valid through 1990, as those granted under the FEITL for service income earned in connection with equipment sales and technical reform projects for Chinese enterprises. Companies involved in contracted projects may deduct consolidated tax paid in calculating taxable income under the FEITL.

Although the consolidated tax is normally imposed on gross receipts, a recent regulation allows the deduction of certain expenses by companies engaged in contracted projects, for purposes of both the FEITL and consolidated tax. These include payments to a Chinese or foreign business to which part of the project work is subcontracted, amounts for the purchase outside China of equipment for the project, and amounts for data-analysis and processing done outside China.

Equity Joint Ventures

Equity joint ventures are taxed on their income under the Joint Venture Income Tax Law. The other major tax relevant to equity joint ventures is the Consolidated Industrial and Commercial Tax.

Exemption from the consolidated tax and customs duties as applied to imports of machinery, equipment, parts, and other materials are available when these items are imported:

- under an equity joint venture contract as part of the foreign party's capital contribution to the venture
- with funds within the total amount of investment of a joint venture
- with additional capital and the approval of the authorities that approved the joint venture when production and supply of these items cannot be guaranteed in China.

Raw materials, auxiliary materials, components, parts, and packaging materials are also exempt from the consolidated tax and duties when imported by a joint venture for the production of export products. To the extent a joint venture diverts any items imported tax free to sale in China or incorporates these items into products for sale in China, it must make up the appropriate tax payments.

Export sales are treated like any other "sale" for purposes of the consolidated tax. Consequently, a joint venture that exports its products is in principle subject to the tax. Joint ventures may be exempted from the Consolidated Industrial and Commercial Tax as applied to exports, with the approval of the Ministry of Finance, except in the case of export items restricted by the state. In addition, joint ventures that "have difficulty" at the beginning of their operations paying tax on products produced for domestic sale may apply for a reduction in, or exemption from, the Consolidated Industrial and Commercial Tax for a fixed period.

Under a new Chinese policy, equity joint ventures may pay tax according to the rates of the 1972 Industrial and Commercial Tax Act (which applies to Chinese domestic enterprises) when these rates are lower than those of the 1958 Consolidated Industrial and Commercial Tax Act.

On October 12, 1983, the Ministry of Finance issued a notice that provides that any joint venture previously approved to start operations but not yet doing business and earning profits may be exempted from income tax in the first two years starting from the year it begins to earn profits, and have a 50 percent reduction in tax in the following three years, increased from the one and two year periods, respectively, stipulated in the joint venture income tax law. Those ventures that have begun to do business and earn profits, if the originally stipulated tax-exempt period has not expired, may have an added one year each to the tax-exempt and 50 percent tax reduction periods. If the tax-exempt period has already expired, but the 50 percent tax reduction period has not, the ventures may have one year added to the 50 percent tax reduction period. In cases of those joint ventures whose originally stipulated tax-exempt and 50 percent tax reduction periods have already expired, and of those whose joint venture contracts were signed before the promulgation of the joint venture income tax law and whose income tax reduction and exemption periods are fixed in accordance with approved contracts, there is in no event to be further extension of tax reduction and exemption periods.

The extensions of the time limit for final income tax settlement by joint ventures and of the period for filing of the annual returns and accounting statements are to be implemented in 1984 beginning with final tax returns for 1983.

The other Chinese tax with which equity joint ventures need to concern themselves is the Provisional Urban Real Estate Tax. This tax applies to land and buildings and is levied on the owner. With respect to joint ventures, however, the tax is no longer applied to land, but only to buildings that the Chinese party contributes as part of its equity in the venture. The annual tax rate for buildings is 1.2 percent based on an assigned standard value.

Taxation in the SEZs

The same basic tax structure that governs the taxation of foreign business activity in the rest of China applies in China's four special economic zones, or SEZs, in Shenzhen, Zhuhai, and Shantou in Guangdong Province, and Xiamen in Fujian Province. The SEZs, however, have a number of special tax policies that operate in the framework of the national tax legislation. Some of these are embodied in SEZ legislation, but most exist on the basis of directives, or simply in practice.

The most obvious of these special tax policies is the flat enterprise income tax rate of 15 percent, with no local surtax, applicable in both the Guangdong and Fujian SEZs. This rate applies to equity joint ventures, as well as to foreign companies with SEZ contracted projects or cooperative ventures. In addition, the rate applies to "wholly owned enterprises" foreigners establish in the SEZs. Foreign enterprises without taxable establishments in the SEZs, such as those with only representative offices, are subject to the FEITL withholding tax on any relevant income. Thus far, the SEZs have not made any special provisions on the withholding tax.

In addition to the low income tax rate, foreign investors in the SEZs may in some cases benefit from more advantageous tax holidays than those offered under the national tax legislation. Depending on such factors as the amount of investment, nature of the technology, and length of the project, tax holidays of up to five years are available. The most advantageous tax holidays are generally obtained by enterprises with an investment of $5 million or more involving relatively high technology, and requiring a relatively long period for capital recovery.

An important issue of concern to foreign participants in equity joint ventures in the SEZs is the 10 percent withholding tax on repatriated profits under the Joint Venture Income Tax Law. Informal statements by Chinese officials that this tax will not apply in the SEZs have not been substantiated in writing. The general legal principle governing the SEZs is that national legislation applies in the absence of particular SEZ provisions to the contrary. As a result, the only safe assumption at this point is that the 10 percent withholding tax *does* apply in the SEZs.

Though the various SEZ income tax benefits are applicable to all foreign investment in the SEZs, these benefits are being denied to a very important category of projects—offshore oil service ventures. The position of the Ministry of Finance is that these ventures, though registered in the SEZs, derive their income from services performed offshore and they should not therefore enjoy the same tax advantages as enterprises actually manufacturing goods or performing services in the SEZs. It remains to be seen whether the ministry will develop guidelines distinguishing between oil service ventures that do perform activities in and derive income from the SEZs, and those that do not, rather than apply a blanket denial of SEZ tax benefits to oil service ventures.

Exemptions from the consolidated tax and customs duties are generally available to all types of foreign investment projects in the SEZs on the importation of means of production and inputs, though tax is levied if these items are later resold in China. Exemption from the consolidated tax is generally granted on exports.

Individuals residing in the SEZs also benefit from tax preferences. In the Guangdong SEZs, for example, tax rates of 3–30 percent apply, as opposed to the national rates of 5–45 percent. The Xiamen SEZ reportedly intends to tax individuals at 50 percent of the national rates, resulting in an even lower tax. Unclear at this stage is the question of what rules the Chinese will develop to cover the individual tax status of foreigners who spend time both in the SEZs and in other parts of China.

Timothy A. Gelatt is an associate with the law firm of Baker & McKenzie, specializing in Chinese legal affairs.

Eugene Theroux is a partner in the law firm of Baker & McKenzie, Washington, DC. He has made more than 50 visits to China for his firm, and was resident for Baker & McKenzie in Beijing during 1981. He is chairman of the National Council's Legal Committee.

Photos by Ray Crowell

Secretary of Agriculture John R. Block and Chinese Premier Zhao Ziyang.

Council President Christopher H. Phillips, Madame Shi Yanhua, interpreter, and Foreign Minister Wu Xueqian.

THE NATIONAL COUNCIL FOR US-CHINA TRADE HOSTS CHINESE PREMIER ZHAO ZIYANG

On January 11 Premier Zhao told more than 300 American business executives and government leaders at a National Council-sponsored luncheon that "China's opening up to the outside world is not a mere subjective wish but a reflection of objective necessity. China has opened its door and will never close it again." In the past five years, he added, "our total volume of imports and exports have almost doubled, and we have absorbed foreign funds to the tune of 12 billion US dollars, and have carried out or set up about 2,000 projects and enterprises with direct foreign investment."

Premier Zhao further noted the superiority of US firms in the oil, coal, power, communications, and transportation sectors. "They are in a good position to expand economic and technical cooperation with China," he said.

While in Washington, Premier Zhao signed a memorandum of understanding that will involve US firms in applied technology research conducted by selected Chinese ministries, as well as a two-year Accord on Industrial and Technological Cooperation between the US Commerce Department and China's Ministry of Foreign Economic Relations and Trade.

Premier Zhao's January 7–16 whirlwind tour also included a California Round Table discussion with top business leaders in San Francisco and a dinner hosted by IBM in New York. The first visit of a Chinese head of state to the US will be followed up in late April by President Reagan's visit to Beijing, the third visit by an incumbent American president to the People's Republic of China.

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Premier Zhao Ziyang being greeted at National Council luncheon by Council Chairman Walter S. Surrey (L), senior partner of Surrey & Morse, and Council President Christopher H. Phillips (R).

CHINESE L/Cs

What every executive should know about Chinese letters of credit.

R. Barry Spaulding

As China's sole foreign exchange bank, the Bank of China (BOC) maintains a relatively standard set of procedures for the letters of credit used in the country's foreign trade. Because these letters of credit possess certain unique characteristics, it is important that US importers and exporters understand how they differ from standard international letters of credit. This will save large amounts of time that could otherwise be wasted trying to negotiate terms that are unacceptable to the Chinese and contravene standard BOC practice. Knowing the common characteristics of Chinese letters of credit will also help US executives focus on the terms that *are* negotiable—which should help firms obtain the best payment terms possible.

I. CHINESE IMPORTS

At the outset, it must be remembered that only the BOC can open letters of credit for PRC imports. While standard import contracts vary, the form of settlement generally required in a contract with a Chinese foreign trade corporation is by a sight or usance draft, together with shipping documents under an irrevocable letter of credit opened by the BOC. Import letter of credit terms are based strictly upon the terms (including payment) specified in the underlying commercial contract, and the vast majority are denominated in US dollars. The Bank of China has several different letter of credit forms, and variations do occur between branches, but the format is generally similar to the example appearing on page 32.

China not a signatory of ICC

The Bank of China's letter of credit payment system generally operates efficiently and, although China is not a signatory member of the International Chamber of Commerce (ICC), it typically adheres to the ICC's Uniform Customs and Practices for Documentary Credits and Uniform Rules for Collection. One exception, however, is that the BOC sometimes permits Chinese importers to review documents before paying. This is not a standard policy, but it could lead to a refusal or delay in payment by the Chinese importer, who may argue that the contract terms were not adhered to. Such a practice is clearly contrary to ICC regulations, which state that payment should be made by the bank opening the letter of credit on the strength of its exclusive examination of documents.

No confirmation permitted

Another characteristic of a BOC letter of credit is that under no circumstances may it be confirmed. As China's sole foreign exchange bank with worldwide assets exceeding $45 billion, the Bank of China believes that its obligations ought to be beyond question. Naturally, this often poses a problem for the finance departments of certain firms that require, as a matter of policy, confirmation of letters of credit in new sales situations, or for sales to nations outside of North America and Western Europe. Of course, there are ways an American bank can shoulder Bank of China risk, should the foreign seller insist, but the BOC's reputation in the international financial community is excellent and to the best of my knowledge no default under a BOC letter of credit has ever occurred.

R. Barry Spaulding is vice-president and manager, China division, Chase Manhattan, New York. Spaulding has been involved in China finance since early 1980 and has lived in Beijing and Hong Kong.

Payment

BOC letters of credit nearly always stipulate that they are only payable at the counters of the BOC branch that opened the credit. Thus, all documents must be forwarded to that BOC office for review and subsequent payment. Standard processing time is approximately five days after the documents reach the Bank of China counters. To date, only grain companies have been able to negotiate a "telex reimbursement" clause in their BOC letters of credit as standard procedure. As a result, they receive payment the day following presentation of documents to their own bank, on the strength of that bank's telex statement to the BOC that the documents are in order. All BOC letters of credit issued to grain companies contain the following wording, which allows for such prompt payment: "*Upon receipt of the negotiating bank's authenticated cable confirming that the credit terms have been complied with and the documents called for have been airmailed to us we shall immediately meet your reimbursement claim by telegraphic transfer.*"

Clearly, this clause represents the best payment terms for the exporter. But next-day payment is generally impossible for most firms. The next-best alternative generally involves payment after 10–14 days: The US bank, after examination, express-mails the necessary documents to the BOC, which then effects payment by telex. Indeed, payment by telex transfer of funds should always be requested. The standard wording in the letter of credit would be as follows: "*We hereby undertake to effect* *payment by telegraphic transfer (or T/T) upon presentation of the above-mentioned drafts and shipping documents provided that the name of commodity, specifications, quantity, price, packing, and the name of manufacturer shown in the documents are found, upon presentation, to be in conformity with the relative contract."* It is also best to have "payment by telegraphic transfer" inserted directly in the contract, if possible, in addition to the standard letter of credit form that is usually provided as an addendum to the contract. Firms that fail to receive payment by telex will have to wait at least another 10 days for air-mailed payment.

Because of the need to return documents to China, a firm that wants its bank to advise and negotiate the documents under the letter of credit, and send them to China on its behalf, should note this in the contract, as well as in the letter of credit form that is normally appended to the contract. Alternatively, if the credit is advised through another bank chosen by the BOC, a firm can take the documents to the bank of its choice for examination and dispatch to China by the fastest means available.

Charges

Charges are negotiable. Generally, though, banking charges are borne by the buyer. China will usually seek to insert the clause "all banking charges outside of China shall be borne by the seller" or "all banking charges outside of China shall be borne by the beneficiary," which means the exporter must pay all advising and negotiating charges. Seldom does the BOC agree to the inclusion of a clause stating "all banking charges outside of China shall be borne by the buyer." However, standard banking practice dictates charges outside the opening bank's country are for the buyer and, more often than not, where charges are not mentioned the Chinese buyer does pay.

Draft purchase

Because of payment delays, a firm that wants to speed up payment under a BOC letter of credit can seek to arrange the sale of drafts. The following clause has been deemed acceptable by the Chinse and can be added to BOC letters of credit: *"We hereby engage with the drawers, end-users, and bona fide holders of draft(s) drawn under and in accordance with the terms of this credit that the same shall meet with due honor on presentation of the documents as specified to Bank of China. All drafts drawn under this credit must be endorsed on the back thereof."*

Documentation

While documentation requirements vary according to the nature of the transaction, some or all of the following documents are usually specified in BOC letters of credit:

1. Five copies of the commercial invoice with standard information such as contract number, letter of credit number, and relevant details from the contract. This should be made out to the Chinese importer.

2. Full set of on-board ocean or airway bills of lading made out to order and blank endorsed.

3. Packing list/weight memo. Two to five copies are usually required.

4. Certificate of quality. In some instances this will be included in the packing list/weight memo. In most instances it must be "issued by the manufacturer" in one to five copies.

5. Exporter's letter attesting that extra copies of documents have been dispatched according to contract terms.

6. Certified copy of the cable sent to the accountees either immediately or within several days of shipment, containing information regarding the vessel, date of shipment, and shipment details.

7. Specification of vessel nationality. Since Chinese importers prefer PRC vessels and assuming shipment is FOB, which is usually the case, a statement is required from the shipping agent certifying that the carrying vessel is chartered or booked by China National Foreign Trade Transportation Corporation, or China National Chartering Corporation. Sometimes a letter from the exporter confirming that the nationality of the carrying vessel has been approved by the buyer will suffice, providing that shipment is CIF and the seller can negotiate such a letter.

8. An insurance policy or certificate covering 100 percent or more of the invoice value against all risks of transaction, depending on the nature of the shipment.

9. Two to four copies of a US Department of Commerce export license, if required.

10. A "certificate of origin" or "manufacturer's certificate of origin." This is usually notarized by the local chamber of commerce.

Guarantees and bid bonds

Sales to China often require a standby letter of credit or bid bond. Usually this is referred to in the contract as a "guarantee." American exporters should always insist that this be referred to as a "standby letter of credit," or "performance letter of credit," since US banks cannot provide guarantees and this has led to problems in the past.

II. CHINESE EXPORTS

When instructing a US bank to open a letter of credit on behalf of a Chinese exporter, US importers would do well to keep in mind that the letter of credit should not be restricted, for example, to the Bank of China, Beijing Head Office, since the BOC, as the advising bank, reserves the right to transfer the letter of credit to the BOC branch nearest to the Chinese beneficiary. The US bank should also authorize the negotiating bank to directly reimburse the paying bank. This speeds up payment

1 ***The Bank of China uses several different letter of credit (L/C) forms to pay for Chinese imports, and variations do occur between branches. For example, the standard form L/C contract used by the Shanghai branch of the BOC in 1981 contained the clause "The credit is valid for negotiating in your country," which is contrary to the BOC's policy now, as it was then. But the formats currently adopted by the BOC's main branches in Beijing, Shanghai, Dalian, Nanjing, and Guangzhou generally conform to the example shown here.***

2 ***Under no circumstances does the BOC permit its L/Cs to be confirmed. As China's sole foreign exchange bank with assets exceeding $45 billion, it does not want its ability to pay to be questioned.***

3 ***The vast majority of the BOC's L/Cs are denominated in US dollars. Only in the 1970s did China encourage the use of its own currency, the Renminbi.***

4 ***The BOC usually requires 5 copies of the commercial invoice, though documentation requirements vary according to the transaction.***

5 ***To ensure that the documents are handled by a bank of the exporter's choosing, the exporter should include a provision in both the contract and L/C that designates the exporter's preferred bank as advisor and negotiator of the firm's export documents. If the credit is advised through another bank chosen by the BOC, the exporter can still bring the documents to the bank of its choice for examination and dispatch to China. Firms are well well advised to choose a bank carefully in order to take advantage of the bank offering the most rapid document courier service to China.***

营业部 1

中国银行

BANK OF CHINA

Head Office
Banking Dept.
Beijing

Irrevocable Letter of Credit No. LC 123456

Date
Feb. 1, 1984

Advising Bank	Applicant
The Chase Manhattan Bank, N.A. Export L/C Dept., P.O. Box 6004, New York, N.Y. USA	China National Packaging Import & Export Corporation, Beijing
2 (The advising bank is requested to notify the beneficiary without adding its confirmation.)	Latest date of shipment March 15, 1984
To beneficiary ABC Trading Co., Division of USA Corporation Toledo, Ohio 43607 USA	Expiry date for negotiation in the country of the beneficiary March 30, 1984 Documents must be presented within 15 days after the date of shipping documents

Amount

3 US $6,500,000 (U.S. Dollars Six Million Five Hundred Thousand and No/100 only.)

Dear Sir(s):
We hereby issue in your favour this documentary credit which is available by your draft(s) at sight for 100% invoice value on us marked as drawn under this credit and accompanied by the following documents marked with numbers:

4

(1) Signed commercial invoice in 5 copies indicating contract No. 80WMT-123456MR and L/C No. LC123456.
(2) Full set of clean onboard ocean bills of lading made out to order and blank endorsed marked "Freight to collect" notifying China National Foreign Trade Transportation Corp. at destination.
(3) Packing list/weight memo in 2 copies showing quantity/gross and net weight for each package.
(4) Certificate of quality in 2 copies issued by the manufacturer.
(5) Your letter attesting that the extra copies of documents have been dispatched according to contract terms.
(6) Your certified copy of cable dispatched to the accountees within 15 days after shipment advising name of vessel, date, quantity, weight and value of shipment.
(7) In case of F.O.B. shipment, certificate issued by the shipping agents certifying that the carrying vessel is chartered or booked by the China National Foreign Trade Transportation Corp., Beijing or China National Chartering Corp., Beijing (charter-party bills of lading are acceptable); In case of C and F or C.I.F. shipment, your letter attesting that the nationality of the carrying vessel has been approved by the Buyers.

Evidence shipment of:
50,000 metric tons U.S. No. 2 or better Yellow Corn to be certified by elevator's letter. The corn supplied by the Seller should be in conformity with the following specifications: Moisture: 14.5% maximum; Test weight: 54 lbs. minimum per Winchester bushel; and Broken corn and foreign material: 3% maximum. Delivery: to the end of elevator's leading spout at one/two safe berth(s), one safe U.S. Gulf of Mexico port, or one safe U.S. Atlantic coast port at Seller's option.

Special instructions

5 Negotiations of drafts under this credit are restricted to the advising bank, Chase Manhattan Bank, New York. Dispatch all documents to us in one lot by first available airmail.

6 All banking charges outside of China are to be borne by the beneficiary.

7 We hereby engage with the drawers, endorsers, and bona fide holders of draft(s) drawn under and in accordance with the terms of this credit that the same shall meet with due honour on presentation of the documents as specified to Bank of China, Beijing.

Partial shipments not allowed   Transshipment not allowed

8 We hereby undertake that all drafts drawn under and in compliance with the terms of this credit will be duly honored on presentation at this office by airmail transfer, provided that the detailed name of commodity specifications, quantity, price, and packaging shown in these documents are found upon presentation in conformity with the contract. 9

for BANK OF CHINA, HEAD OFFICE
BANKING DEPT., BEIJING

Authorized signature

6 *China normally insists on the unusual practice that banking charges outside of China be borne by the beneficiary. This requires that the exporter must pay all advising and negotiating charges. However, the BOC normally agrees that banking charges incurred in China must be paid by the buyer.*

7 *This clause is deemed acceptable by the Chinese and permits exporters to speed up payment under a BOC L/C by discounting their drafts.*

8 *BOC L/Cs nearly always stipulate that they are only payable at the counters of the BOC branch that opened the import credit. Thus, all documents must be forwarded to that BOC office for review and payment. Allow about 5 days for processing.*

9 *To date only US grain exporters have been able to negotiate a "telex reimbursement" clause in their BOC L/Cs. As a result, they receive payment the day after presenting documents to their own bank on the strength of that bank's telex statement to the BOC that the documents are in order. The next best payment procedure is by telegraphic transfer (or T/T), which obligates the BOC to make payment by telex after it receives the documents by airmail. The slowest form of payment is by airmail; it normally involves an additional payment time of at least 10 days to 2 weeks. It is best to have "payment by telegraphic transfer" inserted directly into both the contract and L/C.*

and lessens the chance of payment error.

Inspection certificates

Inspection certificates and certificates indicating quality and content analysis are done by the China Commodity Inspection Bureau, which should be specified in Chinese export letters of credit. This has historically been a problem area for US importers, and it is recommended that the certificate of quality or the inspection clause be made as specific as possible, especially if the imported shipment is to be resold. A "certificate of quality issued by the China Commodity Inspection Bureau," or a "certificate of quality issued by the China Commodity Inspection Bureau indicating quality must conform to the above specifications," may result in too general an opinion to be useful when a problem arises or the commodity is resold. More precise wording such as "certificate of quality issued by the China Commodity Inspection Bureau indicating *x* percentage of chemical composition (not above or below) according to the results of an inspection which must conform to the above specifications" can usually produce a more definitive quality statement.

Official documents

All notarization and certification of documents and issuance of certificates of origin is done by the China Council for the Promotion of International Trade (CCPIT). That organization should be specified where these functions are necessary.

Charges

Charges such as advising, negotiating, or amending letters of credit opened in favor of Chinese beneficiaries are usually paid by the opener, or buyer. The standard charges for documentary credits currently prevailing in China are as follows:

Advising credits: one-tenth percent/ (minimum ¥20; maximum ¥200).
Negotiation: one-eighth percent/ (minimum ¥20).
Pre-advising credits: ¥20 for each credit.
Confirming credits (including the advising commission): 1.5 percent for each period of 3 months or fraction thereof (minimum ¥20).
Amendment to credits: ¥15 per amendment.
Acceptance of bills: one-tenth percent per month (minimum two months or ¥20).
Transfer of credits: one-tenth percent (minimum ¥20; maximum ¥200).
Cancellation of credits: ¥20 for each credit.
Guarantees: one-fourth percent for each period of 3 months or fraction thereof (minimum ¥20).

Although Chinese letters of credit have many common characteristics, *any* letter of credit is, in a sense, a unique financial instrument that is tailored to a specific purchase or sale. Moreover, letter of credit procedures in China are changing as exposure to international practices increases, trade increases, and the Bank of China becomes more accustomed to standard international banking practices. To avoid problems after the negotiating session is concluded and the sale or purchase has been made, companies doing business in the PRC should consult the China representative office or China division of a bank experienced in Chinese letter of credit practices.

THE WAY AHEAD

China's balance of payments outlook to 1988

John Stuermer

The outstanding feature of China's balance of payments over the last several years has been the rapid accumulation of foreign exchange reserves, from \$2.3 billion at year-end 1980 to \$14.7 billion in September of 1983—a level comparable to that of many industrialized countries. Among non-oil-exporting developing regions, only Taiwan's foreign exchange reserves of \$11.5 billion approach the level accumulated by the PRC. Not until 1986 is this growth in China's foreign exchange reserves likely to be reversed.

This accumulation began with the "readjustment" program pursued from 1979 to 1982. The Chinese implemented this policy after deciding that the plans for rapid increases in production, investment, and foreign borrowing laid down in 1977 and 1978 were overheating the economy. The authorities began to relax readjustment in 1982 by allowing the heavy industrial sector—which had been the principal target of readjustment because of its excessive energy and capital equipment requirements—to grow by 9.3 percent, after it had grown by only 1.4 percent in 1980, and declined by 4.7 percent in 1981. Along with an 11 percent increase in agricultural output, due to the country's successful agricultural reforms also implemented in 1979, gross output value (a Chinese proxy for GNP) rose by 8.7 percent, compared with 6.7 percent in 1980 and 4.6 percent in 1981.

But readjustment was not relaxed in the foreign trade sector until mid-1983. In 1982 imports declined 12 percent from \$19.8 billion in 1981 to \$17.4 billion, while exports increased 6.5 percent from their 1981 level of \$21.5 billion. This resulted in the expansion of the trade surplus from \$1.7 billion in 1981 to \$5.6 billion, as well as a \$6.4 billion rise in foreign exchange reserves, from \$4.7 billion at year-end 1981 to \$11.1 billion at year-end 1982.

Imports on the rise

In 1983 imports were allowed to grow again. Most of this growth came in the second half of 1983. Imports during the first half of the year (\$8.7 billion) were identical to the level prevailing in the first half of 1982, but in the third quarter imports were 22 percent higher than in the third quarter of 1982.

The acceleration of imports resulted from a sudden upturn in manufactured imports, primarily steel and machinery, while imports of primary products, especially grain and textile fibers, declined sharply. During the first six months of the year manufactured imports increased by 20 percent, while primary imports fell by 27 percent. Iron and steel imports, which made up 14.3 percent of total imports during the first half of 1983, increased by 98 percent, while imports of machinery and transport equipment (which constituted 19.3 percent of total imports) grew by 10.9 percent. Among primary products, cereal imports fell by 17.8 percent and significant declines were recorded for other products such as wood and textile fibers.

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Japan and Europe have benefited most from China's increased imports. Their exports to China rose by 12 percent and 38 percent, respectively, during the first half of 1983. The most rapidly growing Japanese export item was steel, which increased 127 percent in volume terms to 2.9 million tons (from 1.3 million tons during the first half of 1982), and accounted for approximately 45 percent of total imports from Japan. Chinese steel imports from Japan may reach 7 million tons for the year as a whole, resulting in China overtaking the US as Japan's largest steel export market. West Germany, the largest European exporter to China, increased its exports by 10 percent, while the exports of France increased by 317 percent, and those of the United Kingdom, Belgium, and the Netherlands grew 42 percent. Most of these increases consisted of machinery, iron and steel, and chemicals.

The US was the principal loser in these recent developments. US exports to China fell by 35 percent during the first half of 1983, principally because of China's cutbacks in grain, chemicals, and textile fiber imports. The one area in which US exports to China increased was machinery, which doubled in the first half of 1983 to \$242 million, from \$113 million during the same period in 1982.

This general downturn in US exports to China in early 1983 reflected Chinese displeasure over American textile quotas that had been placed on Chinese exports during the summer. The real reason, however, was the success of China's agricultural reforms undertaken over the last several years and the significant increases in output they have generated. Consequently, while China is likely to raise its grain imports from the US in 1984, it is unlikely to import the 7–8 million tons it has in past years. After the current US–China grain agreement expires in 1984, China may very well reduce its annual grain imports from the US to less than 6 million tons.

The trend toward accelerated manufactured imports in the first half of 1983 is likely to continue in the second half, resulting in manufactured imports growing by 36 percent for the year as a whole, and total imports by 14 percent.

Exports increase slowly

Exports are estimated to have grown only marginally in 1983 to a level of $23.3 billion, up from $23.0 billion in 1982. This was due to an increase in non-oil exports that made up for the decline in both the value and volume of oil and petroleum products. The volume of crude oil exports may have declined by approximately 5 percent to 13.9 million tons, from 14.7 million tons in 1982. Since the average price has fallen 12.2 percent from $222 per ton in 1982, the total value of crude oil exports is estimated to have declined to $2.7 billion in 1983. On the other hand, petroleum product exports appear to have held to their 1982 level and to have fallen in price by a lesser amount, resulting in only a 7 percent decline in their export value in 1983.

China's textile exports are estimated to have grown slightly in 1983, mostly in the second half, after falling by 3 percent in the first half. But the largest export increase during the year came from the "other" category. This category is highly diverse, and includes mainly miscellaneous manufactured articles. These should provide a wide range of opportunities to develop exports outside of areas such as textiles, which are becoming increasingly sensitive and restricted in industrialized countries.

The modest growth of exports combined with the recent upturn in imports reduced China's 1983 estimated trade surplus to $3.5 billion from $5.6 billion in 1982. However, the country's current account still registered a $5.3 billion surplus because of the surplus on the service account, as well as remittances of approximately $600 million from overseas Chinese. The persistence of a large current account surplus, along with an estimated $400 million in direct foreign investment, substantial non-bank capital flows, and an estimated small increase in commercial bank borrowing (while China repaid $450 to the IMF), resulted in an estimated increase of foreign exchange reserves to $17.1 billion by the end of 1983.

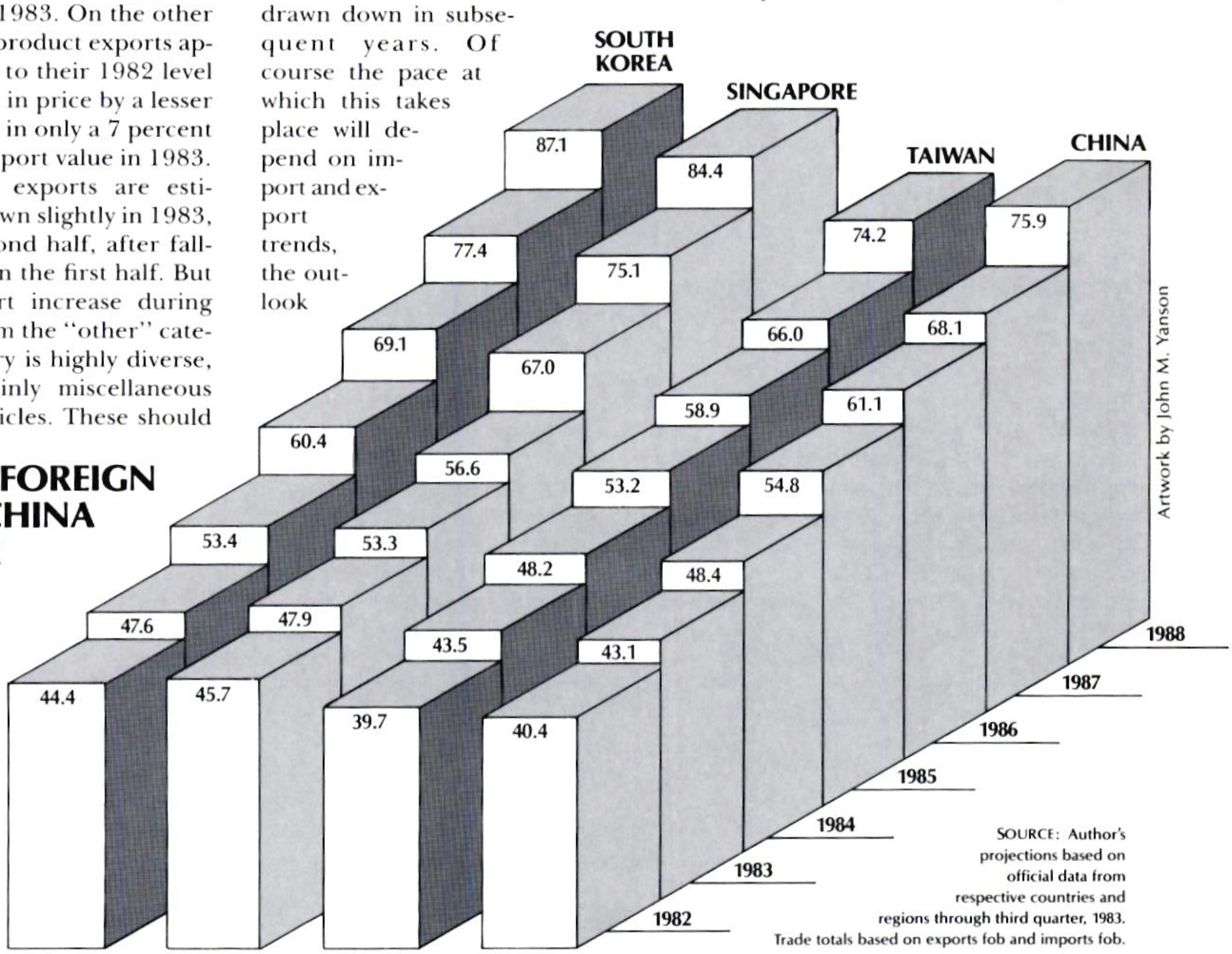
The apparent decision of the Chinese authorities to allow substantial import growth in 1983 suggests that the accumulation of foreign exchange reserves will come to an end by 1986, and these reserves will be drawn down in subsequent years. Of course the pace at which this takes place will depend on import and export trends, the outlook for further development of the service sector, and the availability of foreign capital at concessionary rates from the World Bank and Japan.

The 1984–88 outlook

The growth rate for China's imports is expected to rise to approximately 20 percent in 1984, but then decline to 12 percent by 1988. This scenario will leave the Chinese authorities with approximately six months' import cover in 1988. Manufactured imports are likely to continue as the most rapidly growing component of imports. Although primary exports probably will recover in 1984, they are projected to grow by only 4 percent per annum thereafter, and will not reach their 1982 level of $6.9 billion until 1988.

Total exports are projected to increase slowly during the next few years, largely as a result of a decline in oil exports. The volume of crude oil and petroleum product exports is expected to gradually decline over the next five years, but be offset by the growth of manufactured exports. The volume of crude oil exports was an estimated 14 million tons in 1983, a 5 percent decline from 1982, while

PROJECTED FOREIGN TRADE OF CHINA AND OTHER COUNTRIES AND REGIONS



SOURCE: Author's projections based on official data from respective countries and regions through third quarter, 1983. Trade totals based on exports fob and imports fob.

Artwork by John M. Yanson

BALANCE OF PAYMENT TRENDS

(In billion current US dollars)

	1982	1983	1984	1985	1986	1987	1988
China's exports (fob)	23.0	23.3	24.6	26.3	27.9	30.1	33.2
Crude oil and petroleum products	(4.7)	(4.0)	(3.7)	(3.5)	(3.5)	(3.4)	(3.3)
Textiles	(5.7)	(5.9)	(6.2)	(6.6)	(7.0)	(7.5)	(8.2)
Other	(12.6)	(13.4)	(14.7)	(16.2)	(17.4)	(19.2)	(21.7)
China's imports (fob)	17.4	19.8	23.8	28.5	33.2	38.0	42.7
Primary products	(6.9)	(5.5)	(6.0)	(6.2)	(6.4)	(6.7)	(7.0)
Manufactures	(10.5)	(14.3)	(17.8)	(22.3)	(26.8)	(31.3)	(35.7)
Trade balance	5.6	3.5	0.8	−2.2	−5.3	−7.9	−9.5
Invisibles (net)	1.3	2.8	2.5	3.0	3.1	3.0	2.9
Non-financial services (net)	0.3	0.4	0.5	0.6	0.7	0.8	1.0
Interest (net)	0.5	0.8	1.4	1.7	1.7	1.4	1.0
Remittances	0.5	0.6	0.6	0.7	0.7	0.8	0.9
Current account	6.9	5.3	3.3	0.8	−2.2	−4.9	−6.6
Capital flows (net)							
Direct investment	0.3	0.4	0.4	0.5	0.5	0.6	0.7
Non-bank borrowing	0.2	0.2	1.0	1.5	2.0	2.2	2.4
Bank borrowing	−1.0	0.1	0.3	0.4	0.5	0.6	0.7
Reserve usage*	−6.4	−6.0	−5.0	−3.2	−0.8	1.5	2.9
Memo items							
Foreign assets	15.9	21.9	26.9	30.0	30.8	29.3	26.4
Foreign exchange reserves	11.1	17.1	22.1	25.2	26.0	24.5	21.6
Gold	4.8	4.8	4.8	4.8	4.8	4.8	4.8
External debt	4.5	4.7	6.0	7.9	10.4	13.3	16.3

*SOURCES: Author's projections based on IMF and US government data, official PRC financial statistics, and estimates by private firms. 1982 and 1983 trade data based on official customs statistics corrected for omissions.

RESERVES OF SELECTED COUNTRIES AND REGIONS

(In billion current US dollars)

China held the seventh largest gold and foreign exchange reserves in the world as of October 1983.

	Foreign exchange	SDRs	Reserve position in the IMF	Gold (Valued at market prices)	Total reserves
US	6.9	5.7	9.9	100.3	122.8
W. Germany	38.0	2.7	3.6	36.2	80.5
France	18.7	.9	.9	31.2	51.7
Italy	18.4	1.0	.7	25.4	45.5
Switzerland	12.2	—	.7	31.7	44.6
Japan	20.2	2.4	2.2	9.2	34.0
China	**14.7**	**.3**	—	**4.8**	**19.8**
UK	8.8	1.2	1.7	7.2	18.9
Belgium	3.8	.7	.3	13.0	17.8
Austria	3.9	.2	.4	8.1	12.6
Spain	6.4	.2	.2	5.6	12.4
Taiwan	11.4	—	—	1.4	12.8*
Canada	3.1	.3	.4	7.7	11.5
Australia	7.2	.1	—	3.0	10.3

*As of August 1983.

petroleum product exports are estimated to have remained near their 1983 level of 4.9 million tons. This decline in the volume of exports is expected to continue over the next five years as onshore production increases by only marginal amounts at best and domestic energy requirements increase, especially since the Chinese authorities have decided to allow the heavy industrial sector—which contains many energy-intensive industries—to grow in excess of 10 percent per year. Petroleum product exports also are expected to decline, though at a lesser rate. Prices are assumed to remain at current levels through 1985 and rise only by the rate of inflation thereafter. This scenario will result in a sharp decline of crude and product revenues from $4.7 billion in 1982 to $3.5 billion in 1985, but the gradual rise of prices thereafter will compensate for most of the projected decline in volume.

This decline in petroleum export earnings should be more than offset by manufactured exports. The growth of textile exports is expected to average 7–8 percent over this period. Though the volume of textile exports will be constrained by import quotas in the industrialized countries, the Chinese are likely to upgrade the quality of their textiles and increase export volume in categories not covered by textile quotas. The "other" category of general manufactured exports is likely to grow much faster, averaging 10–11 percent over this period, as the Chinese exploit their considerable possibilities for diversifying manufactured exports.

Overall, the growth rate of Chinese exports over the next five years is likely to fall behind the rates achieved in recent years by the "newly industrialized countries" (NICs) in Asia such as South Korea and Singapore. The decline in oil and petroleum product exports alone will make it difficult for Chinese exports to keep up with the NICs over the next five years. Another problem will be limited port capacity. Throughput at Chinese ports was estimated at 232 million tons in 1982, and current programs for port expansion will increase capacity by about 11 percent per year to 317 million tons in 1985. Bottlenecks are likely to persist until China mounts a broader effort of port expansion and modernization. If the Chinese authorities continue expanding imports at the pace projected above, the remaining port capacity available for handling exports is not likely to expand very rapidly. Consequently, a combination of rapid import growth and modest export growth is likely to produce a trade deficit of $2.2 billion in 1985, which could rise to $9.5 billion by 1988.

Services and transfers

China's current account surplus is not likely to turn into a deficit until 1986, and should remain several billion dollars smaller than the trade deficit owing to the large surplus China earns on its invisible accounts. The major components of invisibles are non-financial services (mainly shipping and tourism), interest from foreign exchange reserves, and remittances from overseas Chinese to relatives in China. The most rapidly growing component of invisibles is non-financial services, due to the rapid pace at which China is expanding its merchant marine and tourist facilities.

The surplus on invisibles is projected to grow rapidly over the next few years, from approximately $2.5 billion in 1984 to $3.1 billion in 1986. Interest income is likely to grow through 1984 and peak at $1.7 billion in 1986, before declining as China draws down its foreign exchange reserves. Finally, remittances are likely to continue growing at a modest rate over the next five years, increasing from $0.6 billion in 1984 to $0.9 billion in 1988.

Capital inflows to increase

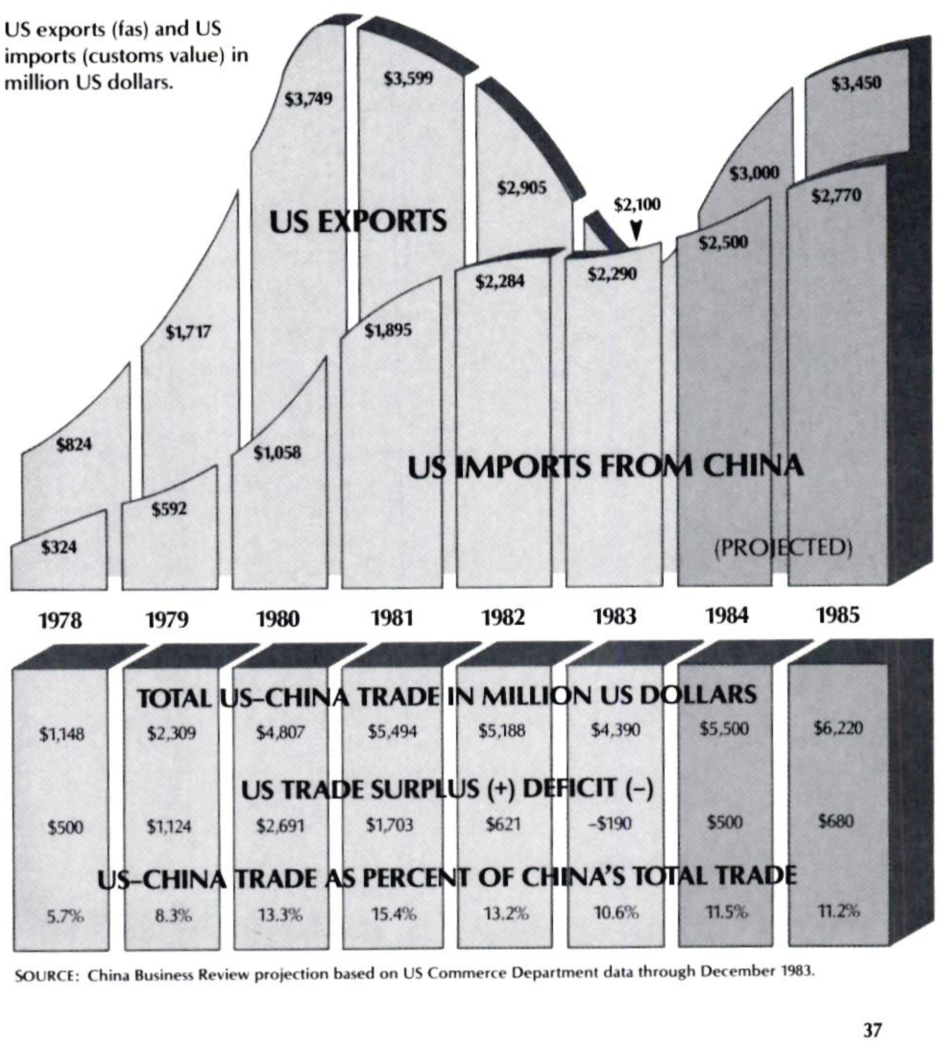
The reason foreign exchange reserves are projected to continue growing through 1986 and only begin to fall in 1987, despite the emergence of a current account deficit in 1986, is because of increasing capital inflows from foreign investment, non-bank borrowing (principally from concessionary sources such as the World Bank, Japan's Overseas Economic Fund and Exim Bank, and suppliers' credit), and commercial bank borrowing. A critical factor determining the rate of capital inflow will be China's ability to use its large concessionary loans. At the end of 1983, for example, the World Bank had committed approximately $1 billion to China, but China had drawn down only about $200 million. Most developing countries in Asia draw down about half of the commitments available to them from the World Bank in a typical year.

The World Bank could be committing $1–2 billion to China a year by the mid-1980s, depending on the volume of funds made available to the International Development Agency (the World Bank's soft loan window), and Japanese government sources could be committing an equal or larger amount. Commercial bank lending is likely to grow modestly, but would remain limited to trade finance, financing of joint ventures, and project finance, primarily for energy projects. The Chinese government is not likely to make significant use of the sovereign credit market owing to the immense volume of its foreign exchange reserves as well as the large volume of credit from official sources that will be at its disposal over the next several years.

Direct foreign investment (including equity as well as non-equity types of investment) is projected to grow modestly.

Looking over the entire 1984–88 period, we can see that large inflows of concessionary capital and the availability of a large stock of foreign exchange reserves would permit China to increase imports substantially over the next five years—assuming that China's financially conservative leadership does not reduce the pace of import growth below the levels forecast when the country's reserves begin to decline in 1987 and 1988. More rapid growth of imports would be possible if the authorities stepped up commercial bank borrowings or made greater use of concessionary loans than is forecast above. This final scenario would depend on the generosity of industrialized countries, particularly the US, in funding future replenishments of the International Development Association. Even more importantly, it assumes that China can increase the rate at which it implements projects and draws down its financial commitments.

PROJECTED US–CHINA TRADE



Artwork by John M. Yanson

SOURCE: China Business Review projection based on US Commerce Department data through December 1983.

WORLD BANK LOANS TO CHINA

Approximately $2,650 million in World Bank loans have been made to China or are currently under negotiation.

Project	Date Approved	Loan Amount (Million $)	Products to be Purchased (Partial Listing)
Approved in Fiscal Year 1982 (July 1, 1981–June 30, 1982): $260 Million			
University development I	Nov. 4, 1981	$100 IBRD $100 IDA	Computers; instruments; and professional training for 26 Chinese universities.
North China plains	June 15, 1982	$60 IDA	Fertilizer; agricultural chemicals; and rural electrification equipment.
Approved in Fiscal Year 1983: $613.5 Million			
Agricultural education and research I	Nov. 2, 1982	$75.4 IDA	Computers and scientific equipment
Ports I	Nov. 2, 1982	$124 IBRD	Quayside cranes; tractors; chassis; and transtainers for three new terminals at Shanghai, Huangpu, and Tianjin.
China Investment Bank	Dec. 21, 1982	$40.6 IBRD $30.0 IDA	CIB was established on Dec. 23, 1981 as "intermediary" of the World Bank and other international development institutions to make loans to medium and small export-oriented projects.
Daqing oil field	Jan. 25, 1983	$162.4 IBRD	Drilling rigs; cementing fracturing equipment; seismic equipment; computer centers; and technical assistance.
Zhongyuan-Wenliu oil field	Mar. 29, 1983	$100.8 IBRD	Drilling equipment including blow-out preventers, cementing equipment, workover rigs, oilfield trucks; seismic equipment; an LPG plant; and technical assistance.
Heilongjiang land reclamation	April 19, 1983	$35.3 IBRD $45.0 IDA	Tractors, combines, and backhoe excavators.
Already Approved or To Be Approved in Fiscal Year 1984: $800 Million			
Polytechnic/ TV university	Sept. 13, 1983	$85 IDA	Computers (20% of loan); TV production and transmission equipment (60%); and test equipment, optical fiber, micro antenna, transmitters, and monitoring equipment (20%).
Technical cooperation credit	Sept. 13, 1983	$10 IDA	Technical assistance and training for 25 subprojects at government institutions.
Rubber tree planting	Nov. 29, 1983	$60 IDA $40 IDA Special Fund	Chemical fertilizer; vehicles; agricultural machinery; and rubber processing equipment; US companies ineligible to bid on chemical fertilizer and forestry and rubber-processing equipment, which is financed by the Special Fund.
Railways I	Spring, 1984	$220 IBRD	Rails; switches; cables, telecommunication, and signalling equipment; and construction equipment.
Ports II	Spring, 1984	$70	Grain terminal equipment, engineering, and design services for Dalian.
Hydropower I	Feb. 21, 1984	$145	Power plant equipment for Francis hydro turbine, generators, transformers, and engineering design services for Lubuge.
Rural credit	Spring, 1984	$50	New lending institution modeled after CIB to assist agricultural organization.
China Investment Bank II	Spring, 1984	$120	Additional funds to CIB for medium and small Chinese enterprises.
Loans That May Be Approved in Fiscal Year 1985: $973 Million			
Luan and Jincheng coal mines	FY85	$120 (Luan) $120 (Jincheng)	Longwall mining equipment, vertical shaft-sinking equipment, coal handling, and washing equipment.
University development II	FY85	$200	Extension of projects begun in UDI with greater emphasis on technical assistance.
Railways II	FY85	$200	Modernization of electric locomotive plant in Zhuzhou, Hunan Province.
Agriculture research II	FY85	$25	Upgrading of selected regional research institutes and extension stations.
Agricultural education II	FY85	$73	Extension of projects begun under FY83 loan with emphasis on improving planning, technical schools, nonformal agricultural education, and library facilities at selected institutions.
Petroleum III	FY85	$100	Seismic exploration and development of heavy oil deposits at Karamay field in northern Xinjiang.
Forestry	FY85	$50	Road building equipment; lumber handling trucks; lumber cutting and processing equipment; and forestry research, education, and planning.
Rural health and medical education	FY85	$85	Modernization of health research and teaching facilities.

Projects Planned for Fiscal Year 1986 and beyond

Fertilizer I: Nitrogen production equipment, technology, and consulting services for plants of different sizes, using different feed stocks.

Petroleum IV: World Bank and Chinese petroleum authorities currently are discussing a wide variety of possible petroleum projects.

Machine tools I: Equipment, technology, and technical assistance to modernize and nationalize Shanghai's machine tool industry.

Hydropower II: Equipment and know-how for possible Shuikou, Manwan, or Manhuatan hydropower projects.

Drinking water: Project to run concurrently with UN's 10-year drinking water program.

Technical transformation of industrial enterprise: Projects to modernize medium and small enterprises in machinery, electronics, building materials, and chemical sectors.

SOURCE: National Council for US-China Trade. Chart prepared by Molly McKibben.

Lending to China

Basic legal protection is available to lenders who insert the right clauses in Chinese credit agreements.

Jerome Alan Cohen

Although the number of commercial bank loans to China is still limited, the PRC appears increasingly willing to extend legal protection to foreign lenders. This seems part of the broad legal development begun in 1978 to construct a formal legal system, after a false start in the 1950s and chaos during the Cultural Revolution of 1966–76. Since then the Chinese have made impressive progress in resurrecting their courts, law offices, public notaries, and other relevant legal institutions and in promulgating laws concerning taxation, foreign exchange, judicial procedures, equity joint ventures, and other subjects relating to the financing of foreign economic cooperation.

I. LEGAL SAFEGUARDS TO LENDERS

From the point of view of US banks, many important laws are lacking on the Chinese side. PRC legislators are currently preparing a law governing economic contracts with foreign entities, a civil code, corporation and banking legislation, laws regulating wholly owned foreign investments, contractual joint ventures, and compensation trade transactions, as well as a foreign trade administration law. All of these and more are expected to appear during the next few years. Until they do, however, many legal issues remain murky. For example, answers are still needed regarding such fundamental questions as: What is a legal person? What does the concept of limited liability mean? Can foreign lenders arrange—and enforce—mortgages or other security devices? and Which agencies must approve foreign loans to which borrowers? At this point we can only look to practice for whatever answers exist.

The availability of legal protection to foreign lenders thus far has depended on the identity of the borrower or guarantor; the type of loan made; bargaining power of the parties; differing attitudes of various lending institutions; and timing of the loan. A few words about each factor may be useful.

The borrower or guarantor

There was a day when the Bank of China (BOC) was widely thought to be China's only authorized commercial borrower of foreign funds. The BOC is still everyone's favorite borrower or guarantor (apart from the PRC itself), though it is less likely than other Chinese entities to offer the legal protection foreign investors desire. Precisely because it is the BOC, foreign banks tend to make fewer demands for legal protection upon it than they do upon lesser-known entities.

Under its 1980 Articles of Association, the BOC is "a socialist state-owned enterprise," namely, a wholly owned government entity that is separate from the government. As a distinct legal person, it can sue and be sued, maintains an independent accounting system, and is responsible for its own assets and liabilities. This confirmation of the BOC's formal independence from the Chinese state vindicated American bankers' treatment of the BOC and the PRC as separate borrowers for the purpose of applying relevant legal lending limits applicable to a single borrower.

Yet the relationship of the PRC to the BOC is closer and more complex than that of the PRC to most other state-owned enterprises. A little-known provision of the 1981 US Exim Bank agreement with the BOC refers to the BOC as "an agency" of the PRC with regard to loan obligations to which "the full faith and credit of China is pledged." "Full faith and credit" is not a concept generally used in China, and the representation in the Exim Bank agreement is contrary to the PRC's customary insistence upon clearly distinguishing the sovereign from its enterprises.

The special relationship of the BOC to the PRC became even more evident in 1982 when the State Council, the PRC's highest administrative institution, published a notice on the status of the BOC. It declared that, apart from its "own business," the BOC "may, based on authorization or request by the state, deal with credit business on behalf of the state." It also provided that "the state shall remain responsible for all loan agreements signed with foreign entities [by the BOC] on behalf of the state."

Many other borrowers have emerged in the PRC, such as ministries of the central government, state enterprises under central control (mainly ministry-run factories and import–export corporations), provincial governments, the China International Trust and Investment Corporation (CITIC), local "ITICs" established by provinces and cities, Chinese–foreign equity joint ventures, and even Hong Kong firms owned by the PRC.

When dealing with borrowers other than the national government, a local PRC government, or the BOC, foreign lenders usually have insisted upon and generally obtained greater legal protection than has been available in loan agreements and other financial instruments concluded with the government or the BOC.

Foreign lenders also have sought guarantors to cover the greater risks perceived in lending to the lesser-known borrowers. The preferred guarantors are units of government and the BOC. They play hard to get, though, and local trust and investment companies and other state enterprises have often been used instead. Generally, the less known the guarantor, or the less satisfactory its guarantee, the greater the legal protection demanded in the loan agreement. In situations where no guarantee is available, lenders have sometimes settled for lesser assurances, such as a "letter of introduction" written by a ministry on behalf of one of its enterprises or a company that it controls in Hong Kong, a "letter of awareness," or an "opinion" (in the days before PRC lawyers issued legal opinions) from the BOC.

Type of loan

The availability of conventional legal protection usually depends upon the type of loan as well as the nature of the borrower and guarantor. As might be expected, a straightforward general-purpose loan for a specified amount usually involves simpler documentation than a revolving credit or a loan extended under a foreign government's export credit agreement with the PRC. A "semi-syndicated" loan agreement to a Chinese entity, when the loan is made by a group of related banks rather than by a syndicate of unrelated banks, is much briefer and less comprehensive in its protection of the lenders' interests than standard Eurodollar documentation, and may contain even fewer legal protections than either revolving or export credits. Lease financing, by contrast, usually involves greater protection than some revolving or export credits. In several specific situations that occurred in 1982 and 1983, the negotiated documentation contained comprehensive Western-style provisions providing more of the legal protections customarily found in international financings.

Bargaining power of the parties

As the body of relevant PRC legislation and regulations grows and as China's experience increases, the flexibility of the parties is diminishing and documentation is becoming standardized. Nevertheless, there is still a great deal of room for bargaining in most negotiations, and the outcome of discussions over legal protection usually depends—as do other terms of the loan—on the relative strength of the parties. Factors such as how badly the loan is needed and how fierce the competition is among potential foreign lenders tend to be decisive. Generally, however, China is becoming more self-confident when dealing in international capital markets, and Chinese representatives are showing increasing interest in and acceptance of international loan documentation practices.

Differing attitudes of lenders

Lending institutions vary in the importance they attach to legal protection on loans to Chinese entities. Some banks have been very conservative, refusing to make loans until PRC entities accept many of the standard Eurodollar documentary terms. Others have been more venturesome. US and British banks tend to emphasize legal protection to a greater degree than their European counterparts. The latter tend to rely more on China's desire to maintain a good credit rating than on documented legal protection.

Timing

Some banks were less cautious about documentation during 1978–80 than they have been recently. The PRC's ambitious development plans, combined with the glamour of the new China market, prompted certain banks to make loans on little more than good faith, relying on the admonition of Chinese representatives to "trust us."

In one 1979 case, on the strength of a letter of introduction from the local branch of the BOC, a European bank reportedly made a loan to a local investment corporation before the borrower had actually completed the registration formalities prerequisite to establishment of its legal identity and receipt of its business license. After the registration formalities had been completed but before approval of the borrower's articles of association, a substantial loan was made to the same borrower by another European bank on the basis of a simple loan agreement and a brief "opinion" from the BOC. The BOC "opinion" confirmed that the borrower had the legal power to make and perform the agreement, that its general manager had the power to sign the agreement and bind the borrower, and that the borrower had obtained approval of the agreement from the municipal government. Similarly, neither the 1979 $2 billion loan to the BOC by a group of Japanese banks nor the 1980 $300 million loan to the BOC by a group led by UBAF was based on standard Eurodollar loan documentation.

None of the above arrangements has as yet encountered difficulties. But it is worth noting that, as the euphoria of the early years wore off, Japanese and European banks began to demand greater legal protection.

In view of the above, a final introductory comment should emphasize the difficulty of generalizing not only about how the following problems have been dealt with but also about how they will be dealt with during future negotiations, for the situation is dynamic and the PRC's attitude and practices are not yet entirely standardized.

II. PROVISIONS FOR DISPUTE RESOLUTION

A short article cannot discuss all the legal protections that might be inserted in a credit agreement with a PRC entity; what follows is an analysis of some key problems that might arise under such an agreement. These problems are often difficult largely because they involve the sensitivity of PRC officials to China's pre-1949 political and economic domination by foreign powers and the PRC's determination to prevent the recurrence of any perceived infringement upon its sovereignty.

I should emphasize at the outset that I know of no court proceeding or arbitration, in China or elsewhere, that has dealt with alleged nonpayment of loan obligations incurred by PRC entities (as distinguished from pre-1949 Chinese entities, such as in the Huguang and other railroad bonds cases). Nevertheless, all parties to a loan agreement recognize the importance of having appropriate provisions for dispute resolution in their credit agreements.

The issue of foreign court jurisdiction

PRC borrowers have in the past often rejected any provision that would subject them to the jurisdiction of a foreign court, whether the loan is linked to a specific project to be carried out in China or is for unspecified purposes. Chinese borrowers are in most instances ready to accept a clause calling for submission to the jurisdiction of PRC courts, and they probably would agree to submission to a court in the jurisdiction of the defendant, which, in the situation lenders worry about, would be China. Foreign lenders are not enthusiastic about either possibility, for they lack confidence in Chinese courts. This is because Chinese courts have as yet no track record in handling foreign loan disputes and little known experience with other international commercial disputes.

In some recent instances, however, certain PRC borrowers have agreed to submit disputes to the nonexclusive jurisdiction of foreign courts. New York court jurisdiction was accepted, for example, in a loan agreement with a New York bank; Japan has been accepted in recent Japanese origin loans; and Hong Kong court jurisdiction has been accepted a number of times in loan agreements entered into with Hong Kong branches of foreign banks. In some of these instances a provision was made appointing an agent within the foreign jurisdiction for service of process, with the borrower often appointing an affiliated entity. In other cases no agent was appointed, on the ground that the borrower has no subsidiary or other affiliate within the jurisdiction. Accordingly, the legal effectiveness of the jurisdictional grant must be tested by that jurisdiction's rules on commencement of actions.

In a side letter that is part of the US Exim Bank agreement with the BOC, the BOC agreed to submit to the jurisdiction of any US federal court sitting in New York or the District of Columbia and appointed the BOC representative in New York City as its agent for service of process.

Neutral arbitration

Because PRC entities are often reluctant to accept foreign court jurisdiction and foreign banks do not accept Chinese court jurisdiction, most loan agreements provide for the arbitration of disputes that cannot be settled through friendly negotiations between the parties or through informal conciliation.

Of course, if a loan agreement does not provide for arbitration as the exclusive means of settling a dispute that cannot be resolved through mediation or other informal means, either party may bring suit in a PRC court (or in a foreign court, assuming that jurisdictional and venue prerequisites can be met in the absence of the PRC entity's explicit submission in the loan agreement to foreign jurisdiction and service of process). The 1982 PRC Civil Procedure Code confirms that the PRC courts generally are to be open to foreign nationals, entities, and organizations.

Since foreign lenders wish to avoid the risk of litigation in China, they turn to arbitration when it proves impossible to obtain PRC submission to foreign court jurisdiction. Foreign lenders, especially US and British banks, are not happy about accepting arbitration, for they fear that arbitration may lead to some sort of compromise decision rather than to the straightforward vindication of their right to full payment of principal and interest. Yet, foreign lenders prefer the risks of arbitration to those of a PRC court.

But where should arbitration take place and under what institutional arrangements? The PRC would prefer to have arbitration before its own Foreign Economic and Trade Arbitration Commission (FETAC), or in the country of the defendant. Foreign lenders, however, resist both arbitration in China and arbitration in the country of the defendant, which, in the case that concerns them most, would be China.

Foreigners have had relatively little experience with arbitration by FETAC, an ostensibly nongovernmental organization under the China Council for the Promotion of International Trade (CCPIT). FETAC places great emphasis on mediation and informal efforts at settlement that tend to produce compromises rather than the clear-cut decisions preferred by lenders. FETAC also provides for an arbitration panel composed of Chinese only, rather than a more balanced panel, and some foreigners believe that its procedures offer them less opportunity for a fair hearing than do counterpart institutions in Stockholm, London, Zurich, or New York. Foreigners also worry that, if the political climate changes, the atmosphere in which a PRC arbitration would take place might prove coercive.

As a result, foreign lenders, investors, and capital equipment vendors generally seek arbitration outside China. But since Chinese entities usually refuse to accept arbitration in the country of the other party, the parties ordinarily agree on a clause calling for arbitration in a neutral jurisdiction before a neutral institution. This generally means that the borrower is to select one arbitrator, the lender a second, and either the two arbitrators are to select the umpire of their three-person panel or the umpire is to be selected by the arbitration institution designated in the loan agreement to handle the dispute. The applicable rules of procedure are usually agreed to be those of the designated institution, although the parties may make other rules applicable, as when the loan agreement provides that the Rules of the United Nations Committee on International Trade Law (UNCITRAL) are to be applied by the Arbitration Institute of the Stockholm Chamber of Commerce, in lieu of the Rules of the Institute.

The Stockholm Institute is the arbitration organization most frequently selected in PRC loan agreements, so long as no Swedish lender is involved. The London Court of Arbitration has been selected on several occasions when no British lender was involved, and the arbitration tribunal of the Zurich Chamber of Commerce is sometimes chosen in the absence of a Swiss lender. PRC loan agreements do not authorize resort to the arbitration facilities of the International Chamber of Commerce because Taiwan is still represented in that organization.

To reduce delays, the foreign side normally succeeds in inserting a provision that permits either party to resort to arbitration at any time after a dispute occurs or within a certain period thereafter such as 30–90 days.

Foreign lenders agreeing to arbitration outside China should be alert to this problem: Under the Civil Procedure Code, if the loan agreement provides for the submission of any disputes to a tribunal other than one convened by "a foreign arbitration organization of the PRC" or if a dispute under the agreement has already been arbitrated by such a non-PRC tribunal, it is not clear whether a party is prevented from escaping its commitment to arbitration by bringing suit in a PRC court. A literal reading of the apparently carefully worded language of the code would suggest that the many foreign banks that have signed loan agreements

Banks became more insistent about documentation after the late 1970s. At that time the PRC's ambitious development plans and the general glamour of the new China market prompted some banks to make loans on little more than good faith. Instead they relied on the admonition of the Chinese to "trust us."

calling for arbitration outside of China may, much to their surprise and dismay, be exposed to the risk that, despite such a clause, the PRC borrower will have the option to sue them in Chinese courts.

Yet none of the PRC judicial and trade officials consulted about this question believes that Chinese courts will interpret the code literally, because to do so would yield an outrageous result that would strike a blow against not only loan transactions but also virtually all investment contracts and many major trade contracts with China. The 1983 Regulations for the Implementation of the Joint Venture Law support the view of these PRC officials, for the regulations preclude the parties to a joint venture contract from bringing suit in China if they have entered into a written arbitration agreement; they do not specify that the agreement must call for arbitration by a PRC organization. Until the code is tested in this respect, however, one cannot be certain, and this problem offers another good reason why banks should try to win the borrower's consent to submission to foreign court jurisdiction instead of foreign arbitration.

Waiver of sovereign immunity

If Chinese officials sometimes bristle at the thought of submitting loan disputes to foreign courts or foreign arbitration, they often—but not always—have even greater difficulty approving language that explicitly waives sovereign immunity from suit, arbitration, or enforcement of a court judgment or arbitration award. Chinese unversed in banking practice tend to believe that such language constitutes an infringement of national sovereignty that harkens back to the era of imperialist "unequal treaties."

Yet even the most ardent Chinese nationalists preach the principle of "equality and mutual benefit" in dealing with foreigners, and recognize that a loan agreement that could be enforced by the Chinese borrower but not by the foreign lender would violate that principle and be unfair. Therefore they do not oppose giving the lender a remedy. The problem is how to phrase the loan agreement in a way that is inoffensive but that nevertheless complies, for example, with relevant principles of US sovereign immunity law.

In the view of the PRC the issue of sovereign immunity should arise only when a loan agreement involves an arm of the Chinese state, such as a central government ministry or a provincial government. Because state-owned enterprises such as CITIC, trading corporations, or factories—and, of course, equity joint ventures with foreigners—are regarded by the PRC as independent legal entities distinct from the government, the PRC does not insist on immunity for them, and its officials are often puzzled about why foreigners request a waiver. This Chinese view, of course, is different from that reflected in US practice and in the US Foreign Sovereign Immunities Act of 1976, which include state-owned enterprises among the instrumentalities of a foreign sovereign that are entitled to immunity unless they are engaged in commercial activities. This, of course, is why American lenders worry about the problem.

In negotiations regarding sovereign immunity, as in other respects, Chinese practice is not consistent, although the trend appears to be in the direction of agreeing to waivers of immunity. In some cases phrases are inserted in agreements emphasizing the "commercial" nature of the transaction, or in other ways leaving no doubt that the parties intend to waive immunity without using the term, thereby avoiding any risk of interference or criticism from higher-ups in Beijing who may not be knowledgeable about banking but are sensitive to national slights. Yet in a growing number of agreements, including some with the BOC, which is sometimes the toughest negotiator in resisting standard documentation, Chinese borrowers have given a full waiver.

Governing law

Just as Chinese borrowers have generally rejected the jurisdiction of foreign courts, so too do they usually reject the choice of foreign law—whether that of the lender's jurisdiction or of a third country—to govern the determination of any disputes that arise under the loan agreement. Because Chinese law is sparse and little-known, foreigners ordinarily reject its selection as the governing law. Again some form of compromise is ordinarily worked out. In most cases it consists of an understanding between the parties to make no reference to governing law in their loan document, thereby leaving it to the arbitrators to decide whether and how to invoke the law of a given country in deciding the dispute.

In some instances the loan agreement offers at least modest guidance to the arbitrators by making a reference in one form or another to international banking or finance law.

On some occasions PRC borrowers have agreed to foreign governing law. Japanese, New York, and Hong Kong law have each been chosen as the law applicable to various loan agreements. In transactions in which the jurisdiction of New York courts has been accepted, some PRC organizations have readily agreed that New York law should govern, and the BOC itself has accepted such a clause in certain cases. Sometimes, however, a PRC entity will only agree to a more general provision to the effect that the governing law is to be determined by the court that takes cognizance of the dispute.

There have also been some instances in which a foreign governing

There is still a great deal of room for bargaining in most loan negotiations, and the outcome of discussions over legal protection usually depends—as do other terms of the loan—on the relative strength of the parties.

law provision has been agreed to in conjunction with a foreign arbitration clause. For example, some European export credit agreements have prescribed Swiss law and Zurich arbitration. In another transaction New York law was agreed to, along with Zurich arbitration.

Enforcing foreign awards

A favorable foreign arbitration award or court judgment may be worthless to a lender to a Chinese entity unless the lender can enforce the award or judgment in China and levy upon the borrower's property there. Moreover, even if the loan agreement contains the borrower's explicit waiver of sovereign immunity, consent to enforcement of the award or judgment, and consent to attachment of and execution against its property, such provisions cannot override the standards and procedures officially prescribed by the PRC. These are controlled by the Civil Procedure Code, any relevant treaties made by the PRC, and the principle of reciprocity, according to which PRC courts will reciprocate the actions of courts in the country of the foreign entity seeking relief in China.

The US-China trade agreement of July 7, 1979, like some other bilateral treaties the PRC has concluded, obligates the participating governments to strive to ensure that arbitration awards are recognized and enforced "by their competent authorities where enforcement is sought, in accordance with applicable laws and regulations." Nothing is said about court judgments, and such a provision is in any event a general expression that lacks specific assurances and procedures. The PRC has not joined any international convention for the enforcement of foreign arbitral awards or court judgments, but has long been studying the implications of participating in such conventions. Now that the Civil Procedure Code is enacted, some Chinese officials maintain that the way is clear for China to adhere to such conventions.

In the interim, foreign lenders must rely exclusively on the Civil Procedure Code, which for the first time opens up the prospect of enforcing foreign awards and judgments in China. Article 204 authorizes PRC courts, "when requested by a foreign court," to recognize the legal validity of a foreign award or judgment and to execute it "if the judgment or award does not violate the basic principles of the laws of the PRC or the national or social interests of the country." More generally, Article 202 authorizes compliance with any request of a foreign court unless to do so would prove "incompatible with the sovereignty or national security of the PRC" or would exceed the power of the Chinese court. It remains to be seen how difficult it will be for foreign lenders to get foreign courts to "request" enforcement by PRC courts.

Prior to the promulgation of the code in March 1982, Chinese officials offered assurances that Chinese enterprises would execute foreign arbitral awards so long as they were fair and not in violation of Chinese laws and policies. In the event of failure by a Chinese party to execute an award, foreigners were advised by officials of the CCPIT not only to petition the appropriate Chinese government departments, but also to request the assistance of the CCPIT in persuading the Chinese party to carry out the award, or to seek enforcement through the people's courts.

It was also theoretically possible before the code appeared for a foreign lender to directly request a Chinese court to enforce a foreign award, without having to ask a foreign court to serve as intermediary. Article 195 of the code, however, seems to preclude direct judicial enforcement by PRC courts, limiting that to awards made by "a foreign arbitration organization of the PRC."

Assuming that a PRC court is "requested" by a foreign court to enforce a foreign award or judgment, what kind of award or judgment might be deemed unenforceable on the ground that it violates the basic principles of PRC law or the national or social interests of China? These criteria give great latitude to Chinese courts. It is to be hoped that China, in applying them, will observe the narrow "public policy" exception applied by other countries, and thereby provide effective relief to lenders whose rights have been violated. Some Chinese officials predict that this will prove to be the case.

If seeking enforcement of a foreign award through a foreign court seems too burdensome or proves impossible, the only formal alternative open to the lender would be to initiate a regular civil suit in the PRC and to rely on the award as evidence in support of its claim.

There are still many difficult questions of law and practice not yet answered by the Chinese authorities on this subject, but at least a framework has now been established for enforcing foreign awards and judgments.

Enforcing Chinese awards

Although foreign lenders usually do not agree to arbitration in China, the situation might change if FETAC revises its rules of procedure in order to offer the prospect of a more unbiased hearing. At present FETAC renders only a small number of awards each year. Chinese officials assert that since the founding of the PRC there has not been a single case in which China's courts have decreed enforcement of an award involving foreign interests. This is reportedly because Chinese foreign trade entities are state enterprises, which recognize that a Chinese award has the force of law and must be executed within the prescribed time. Thus there has been no need to seek judicial enforcement. Even before promulgation of the Civil Procedure Code, Chinese officials claimed that, should a PRC enterprise fail to respect a Chinese award, the people's courts would accept a petition for enforcement from the other party. Indeed, the legislation establishing FETAC authorizes enforcement in these circumstances. Article 195 of the new code confirms this arrangement.

III. CONCLUSION

The China loans field is new and dynamic. Lessons learned yesterday are frequently outdated tomorrow. Yet it is already clear that foreign lenders can obtain basic legal protection concerning the settlement of disputes.

How successful a foreign lender is in obtaining such protection of course depends on the factors discussed above, as well as the personal impression that the lender's business and legal representatives make upon the Chinese borrower. If the foreign parties are knowledgeable about China and its progress and problems, and if they generate feelings of trust, confidence, and understanding in their Chinese counterparts, this will enhance prospects for a mutual accommodation. In meeting the needs of each transaction, experience, imagination, and flexibility are also essential.

Moreover, mastery of Chinese legal concepts and legal language is increasingly important. Some loan agreements are now embodied in equally authoritative Chinese and English texts. Even when English is the only text, the borrower will prepare, or ask the lender to prepare, a Chinese text for internal distribution. In either case, it is indispensable that the English and Chinese texts be identical, and that Chinese and foreign negotiators share a common understanding of the meaning of the terms used in both languages. During negotiations this often requires the lender's representatives to give a detailed exposition in Chinese of international financial and legal terminology and practices.

Of course, there has as yet been no real test of the adequacy of the protections obtained in loan agreements, because Chinese borrowers have thus far fulfilled their obligations to repay. Nevertheless, this fact in itself should surely offer some assurance to prospective lenders.

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BOOKSHELF

书刊介绍

US-China Business Services Directory, compiled by Christopher M. Clarke and Erin McGuire Endean. Washington, DC: National Council for US–China Trade, 1983. 74 pp. $36 for members; $46 for nonmembers, plus $1 postage and handling for all mail orders.

If your firm is looking for support services for your China business, this new National Council directory can help you locate suppliers. American and Chinese firms in 18 service categories are listed, with services ranging from accounting firms and law firms to shipping companies and translation and printing firms. Hong Kong firms are listed only if there are very few American suppppliers or if these firms offer special expertise. Directory information includes names, addresses, telephone and telex numbers, cable addresses, parent companies, and contact names. Company offices in China, Hong Kong, and Japan are included, along with a brief description of the company activities. The 950 entries in the directory are arranged by service category, with an alphabetical company index at the end of the book. —MG

Guide to China's Foreign Economic Relations and Trade: Investment Special, edited by the Policy Research Department and Foreign Investment Administration, Ministry of Foreign Economic Relations and Trade. Hong Kong: Economic Information & Agency, (342 Hennessy Rd.), 1983. Bilingual, 346 pp.; 158 pp. in English text. US$34 airmail.

This volume, subtitled *Investment Special*, is the first of three volumes to be issued under the title *Guide to China's Foreign Economic Relations and Trade*. Volume 2 will deal with import and export trade, volume 3 with international economic cooperation.

This first volume is particularly important in that it brings together recent major policy statements on investment in China; the full texts of foreign economic laws, including the implementing regulations to the joint venture law promulgated in September 1983; and reports and statistics on the status of foreign investments in China. Statements by Chinese officials on investment policy and planning, customs, foreign exchange controls, and investment regulations help clarify relevant laws and regulations, as does the summary of the question and answer session at the Economic Information & Agency's symposium on China's Foreign Economic Relations and Trade held in July 1983.

The sections, "Laws and Regulations Concerning External Economic Relations," which contains major legislation, and "Laws and Regulations Concerning Taxes and Tax Administration" are up-to-date and extremely useful. Prospective investors will find reports on 24 joint venture, coproduction, and compensation trade ventures especially interesting. Despite uneven coverage, much valuable information is provided. Appendices include a table of foreign capital absorption 1979–82; a list of joint equity ventures in China containing each venture's name, participants, economic activity, total investment, foreign equity share, foreign investment in US dollars, date of approval, and duration; and statistics on coproduction by region, foreign investment in offshore petroleum development, and compensation trade agreements.

The book is an excellent update to *Guide to Investment in China*, edited by China International Economic Consultants, and also published by Economic Information & Agency.

—MG

Statistical Yearbook of China 1983, compiled by the State Statistical Bureau, PRC. Hong Kong: Economic Information and Agency (342 Hennessy Road), 1983. 596 pp. US$30 airmail.

This second edition of the invaluable yearbook of official Chinese statistics is even better than the 1981 edition. In addition to updating the 1980 statistics contained in the first edition through 1982, the new edition has filled out many of the earlier tables, which included only data for selected years, to include data for every year since 1949. Moreover, a number of new tables have been included, some related tables consolidated, and a few tables from the first edition omitted.

As in the previous edition, the book begins with a general survey of main economic indicators, production statistics, national income, fixed assets, and economic data for key cities. Subsequent sections cover population (including fairly detailed coverage of the 1982 census); agriculture; industry; transportation, posts, and telecommunications; capital construction; domestic trade; foreign trade and tourism; public finance; prices; people's livelihood; education, science, and culture; and sports and public health. Appendices include economic indicators for Taiwan; international comparative statistics; an expanded section of explanatory notes; and tables of comparative weights and measures. As in the first edition, the absence of an index makes the volume more difficult to use, but the difficulty is somewhat offset by the complete list of tables in the table of contents. —CMC

China's Financial System: The Changing Role of Banks, by William Byrd. Boulder, CO: Westview Press, 1983. 187 pp. $17.

This very useful primer on China's banking and finance sector has come out at a time when the role of banks in China's socialist economy is undergoing substantial change. Byrd lays out the organizational and policy context of these changes, discussing institutional proliferation and decentralization; enhancement of the position of banks *vis-à-vis* their clients; introduction of credit financing of fixed investment; and rationalization of the structure of interest rates. With conditions in China changing almost on a daily basis, every author's greatest fear is that the time taken to research, write, edit, and publish almost anything on China will result in an outdated product almost immediately. Although a few of Byrd's organizational and statistical data have been overtaken by events, on the whole this book represents a welcome addition to a fairly sparse literature on the role of banks in post-Mao China. —CMC

China Coal Industry Yearbook 1982, English edition, compiled by the Compiling Committee of *China Coal Industry Yearbook*, Ministry of Coal Industry, PRC. Hong Kong: Economic Information & Agency, 1983. 316 pp. US$32 via airmail.

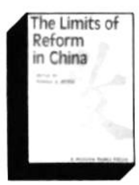
This new reference handbook contains a wealth of information on China's "black gold." Particularly important is the extensive organizational material on the Ministry of Coal Industry, its subordinate bodies, local mining authorities, mine design and research institutes, societies, colleges, and schools, and the directory of plants and mines. Data focus on 1980 and 1981, with summary statistics for 1949–79. The full text of the "Technical Policy for Coal Industry" is presented along with discussions of additional regulations and procedures. The book contains major statements on policy and planning, but these do not provide details on mine development priorities. There is a list of coal products for export with specifications, but specifications of the coal produced by specific mines are not provided. Other lists include mining machinery produced and major standards, specifications, and regulations. The *Yearbook* is an excellent resource for those doing business with China's coal industry. —MG

China as a Maritime Power, by David J. Muller, Jr. Boulder, CO: Westview Press, 1983. 277 pp. $30.

China's emergence as a major world maritime power during the 1970s and 1980s has dramatic implications for the international economic system and the military balance in East Asia. Lt. Cdr. David Muller has given us a first-class, concise, yet comprehensive account of this emergence.

Muller, a career naval officer and China expert attached to the Office of Naval Intelligence, has skillfully utilized publicly available Western and Chinese sources, as well as recently declassified intelligence reports to examine five aspects of China's maritime development since 1945. He looks at naval history, naval strategy, maritime economics, naval politics, and maritime foreign relations in each of three time periods: from 1945 to the Sino–Soviet split, from 1960 to the fall of Lin Biao, and from 1971 to the present. A final chapter considers the implications of China's new maritime status for possible naval conflict with the Soviet Union, for the Taiwan issue, for economic growth and the development of offshore oil, and for regional territorial conflict.

Muller's arrangement of material provides a continuous narrative but makes it possible for the specialist to zero in on the sections of greatest interest. —CMC



The Limits to Reform in China, edited by Ronald A. Morse. Boulder, CO: Westview Press, 1983. 155 pp. $16 paperback.

This book is a collection of papers from a conference sponsored by the Wilson Center of the Smithsonian Institution in May 1983. The authors each address a different aspect of the conference's central theme: "What factors are likely to limit the success of China's current wide-ranging and ambitious plans for reform?"

Specifically, three authors address limitations on reform of management and three discuss limits to intellectual and cultural reform. Hong Yung Lee notes that factionalism and post-Cultural Revolution cynicism have obstructed and continue to obstruct reform of the Chinese bureaucracy. Andrew Walder points out that industrial reforms have been less than completely successful because of the existence of contradictory incentive systems for managers (such as the demand for efficient use of capital and energy without raising the cost of these inputs to the factory), and the "politically deformed reward system of past decades" (page 55) that left managers technically and psychologically unprepared for the problems they now face and more attuned to making a good political showing than a profit. Walder expects reform to be a slow process, taking decades to complete.

By contrast, David Zweig argues that rural reform exceeded the expectations, even the desires, of the reformers who instituted them. This was because the attempts to raise agricultural productivity and to link remuneration to effort more closely in the countryside enjoyed both sustained high-level commitment and low-level enthusiastic approval. Obstruction came mainly from mid-level bureaucrats whose positions were threatened or from central ideologues who opposed the reforms on principle. The congruence of the responsibility system with peasant desires, and its manifest success in raising production, made it very hard to oppose.

Three authors discuss the limits to reform in the educational, artistic and cultural, and political systems. None is optimistic that "liberalization" will occur in the Western democratic sense. Each places different emphasis on the weight of Marxist-Leninist-Maoist dogma, the role of the Communist Party in a one-party system, and the existence of an undemocratic, even anti-democratic, "feudalistic" and "legalistic" thread in the Chinese political and cultural tradition. Each, writing before the start of the current campaign against "spiritual pollution" from the West, might have predicted just such a movement to denounce "liberalism," "humanism," and the corruption of Marxist theory with such ideas as the existence of citizens' "alienation" under a socialist system. —CMC

Books and business guides submitted for possible review in The China Business Review *should be sent to the National Council's book editor, Marianna Graham.*

中外貿易

Jennifer Little
Research Assistant

The following tables contain recent press reports of business contracts and negotiations exclusive of those listed in previous issues. Joint ventures, licensing arrangements, and other forms of business arrangements are included if classified as such in Chinese and foreign media reports. For the most part, the accuracy of these reports is not independently confirmed by *The CBR*.

National Council members can contact the library to obtain a copy of news sources and other available background information concerning the business arrangements appearing below. Moreover, member firms whose sales and other business arrangements with China do not normally appear in press reports may have them published in *The CBR* by sending the information to the attention of Jennifer Little.

CHINA'S IMPORTS THROUGH DECEMBER 1

Foreign Party/ Chinese Party	Product/Value/ Date Reported
Agricultural Technology	
Barry F. Neal & Associates Pty Ltd, Toft, Bonal Brothers Pty, Napaer Cos., and Simpson Pope Ltd (Australia)/China National Agricultural Machinery Import and Export Corp., Guangdong branch	Machinery for a sugarcane farm near Zhanjiang. $690.000. 10/3/83.
Deere & Co. (US)	Farm equipment, waiting approval by World Bank. $26 million. 12/1/83.
Chemicals	
Rhone-Poulenc (France) SINOCHEM	Signed protocol to help develop Chinese phosphate mines. 10/14/83.
(Japan)	11,000 metric tons of acrylic fiber. 11/3/83.
Toray Industries, Teijin Ltd, & others (Japan)	2,000 tons of polyester filament for shipment in the first half of 1984. 11/15/83.
(Japan)	1,500 tons of nylon filament for shipment in the first half of 1984. 11/15/83.
Chemical Plants and Equipment	
C-E Lummus, subsidiary of Combustion Engineering (US)	Three process control systems for ethylene plants in Nanjing and Shengli. 9/15/83.
Toyobo Co. and Sumitomo Corp. (Japan)/MACHIMPEX, Tianjin branch	Contract to improve the spinning section of a Tianjin polyester staple plant. $4.9 million (¥1.2 billion). 11/22/83.
Construction and Construction Materials	
Nikko Trading Co. (Japan)/Shanghai Investment & Trust Corp.	32 pre-fabricated housing units to be located in Hongqiao. $2 million (¥500 million). 9/83.
CRS/Sirrine Inc. (US)	Signed a contract to provide planning and design services for development center in Lo Wu, Shenzhen. $23 million (HK$180 million). 11/29/83.
Consumer Goods	
Baum Bros. (US)	Has expanded its dinnerware production base to a second factory in Hunan. 10/10/83.
IRE (Italy), subsidiary of Philips/Beijing Refrigerator Plant	Know-how and equipment to update the plant and increase its production. 11/7/83.
Electronics	
Quest CAE (UK)/Shanghai Instrument Research Institute, East China Research Institute of Computing Technology, and Sichuan Electronic Co.	PCB design systems based on the Q-1600 minicomputer. Each: $135,000 (£90,000). 9/83.
Datac Controls (Ireland)	Microbased monitoring and remote control systems to control water supply. $75,000 (£50,000). 9/15/83.
(W. Germany)/Tongji University, Shanghai	Gift of a Siemens model-7536 computer. 10/6/83.
Food Processing	
Gokai Kogyo Co. (Japan)/CEROILS, Hebei branch	Have set up a cold store for chestnuts in Qinhuangdao. 9/83.
(Sweden)	Signed agreement to establish a dairy training and product development center in Beijing. 11/21/83.
Fuji Oil Co. and C. Itoh & Co. (Japan)	Chocolate plant. 11/22/83.
Hisaka Works Ltd (Japan)	Sterilizers for retort food, sausage, and canned goods production. 11/22/83.
Machinery	
State Institution for Equipment Testing (W. Germany)/Research Institute for Machine Building	Will sign a cooperation agreement. 9/6/83.
Saunders Valve (UK)	Signed contract for industrial diaphragm valves. $1.2 million+ (£800,000+). 9/22/83.
PML Machinery Co. (US)/Tianjin Miniature Micro Motor Works	12 machines to modernize the Tianjin plant. $4 million. 10/83.
Munekata Bussan Ltd (Japan)/Tianjin International Economic and Technical Cooperation Corp.	Discussing equipment and training for plastic mould technology. 10/10/83.
Medical Equipment	
Toshiba Electrical Corp. and Sanko Trading Corp. (Japan)/Shanxi Provincial Foreign Trade and Import Co.	23 sets of ultrasonic diagnosers, a computerized axial topographer, an X-ray machine, and an ultrasonic wave machine. $1.3 million. 10/31/83.

NA = Not Available

NOTES: Contracts denominated in foreign currencies are converted into US dollars at the most recent monthly average rate quoted in *International Financial Statistics* (IMF). Contracts concluded over two months ago are also included if they were not reported in the last issue of *The CBR*.

Metals and Minerals

University of Kentucky, Institute for Mining and Minerals (US)/Central Coal Mining Research Institute	Signed technical information exchange agreement to improve coal production. 9/83.
NA (US)	25,000 tons of phosphate rock. 9/26/83.
Showa Denko Co. Ltd (Japan)/Tianjin International Economic and Technical Cooperation Corp.	Discussing provision of aluminum wire and aluminum alloy technology. 10/10/83.
Sandvik AB (Sweden)/ CITIC	Signed agreements to modernize a cemented carbide factory in Hunan and for seamless stainless steel tubing for use in medical equipment. $15.2 million (Kr120 million). 10/24/83.
Minerals and Metals Trading Corp. (India)	Negotiating supply of iron ore. 10/24/83.
Societe Generale (France)	Signed agreement to carry out financial and technical studies for developing a coal field near Shenmu, Shaanxi. 11/24/83.
Kaiser Steel Corp. (US)	Discussing possible sale of equipment from its closed steel mill in Fontana, CA. 11/30/83.
Isaacson Steel Co. (US)	Will ship equipment from a closed Seattle steel mill to Shanghai. 12/1/83.

Petroleum

China Nanhai Houlder Drilling Corp. (UK)/Nan Lian Food Co. (HK-PRC joint venture)	Contract for catering, food supplies, and other services for the Houlder rig in the South China Sea. 10/2/83.
Chung Wah Shipyard (HK)/Guangdong Shipbuilding Corp. and Shenzhen Navigation Bureau	Reached agreement to build a repair facility in Shenzhen to service rigs and other offshore oil vessels. 10/21/83.
Western Geophysical, subsidiary of Litton Industries (US)	Has begun operation of a seismic data processing center near Beijing to help develop China's oil and gas resources. 11/18/83.

Power

Teshmont Consultants Inc. (Canada)/ TECHIMPORT and Ministry of Water and Electric Power	Signed contract to provide consulting services for a power transmission system. 9/83.

Scientific Instruments

Zeiss (W. Germany)/ INSTRIMPEX	Opened the Zeiss Products Service Center in Beijing. 10/24/83.

Shipping

Lash Carriers Inc. (Liberia)	Two barge carriers. 9/8/83.
Howaldtswerke Deutsche Werft (W. Germany)/ COSCO	Order for three 1,300 TEU-capacity vessels. $37 million+. 9/15/83.
Wah Chang International Group (Singapore)/Bohai Oil Corp.	Three anchor-handling supply boats for offshore exploration in the South China Sea. $15 million. 10/16/83.
Osaka, Kawasaki & other shipbuilders (Japan)	14 cargo ships. 11/7/83.
(Yugoslavia)	Three multi-purpose vessels. 11/7/83.

Telecommunications

Sigma Instruments Inc. (US)	Signed exclusive agreement for production of five PCB-relay products. 10/17/83.
Star Paging (Holding) Ltd (HK)/Shanghai Telecommunications Bureau and NA, Beijing	Two contracts for computer-controlled radio paging systems. $240,000. 11/83.
Northern Telecom International Ltd (US)	A digital switching system for a Guangzhou Hotel. $400,000. 11/3/83.
Minnesota Mining & Manufacturing Corp. (US)	Signed an agreement in principle to set up a wholly-owned factory in Shanghai, to make telecommunications, power distribution, and electrical machinery products. 11/16/83.

Transportation

Suzuki Metal Industry (Japan)/Tianjin Steel Wire Factory	Negotiating supply of a tire bead wire manufacturing plant. $1.2 million (¥300 million). 9/83.
Kamigumi Co. (Japan)/ China Ocean Shipping Agency	Have agreed on a sea-land through transport contract between Japan and China. 10/6/83.
ASG Co. (Sweden)	Training 50 managerial personnel in coordinated transport and containerized traffic. 10/24/83.
General Electric Co. (US)/ MACHIMPEX	Signed contract for 220 diesel-electric locomotives. $200 million+. 11/10/83.
Petroleum Helicopter Inc. (US)/China Ocean Helicopter Corp.	Signed contract to use the US company's fleet of helicopters for offshore oil exploration. 11/11/83.

Miscellaneous

Sanwa Bank (Japan)/Tianjin and Bank of China	Have agreed to cooperate in the modernization of Tianjin's small enterprises. 9/27/83.
Japan International Cooperation Agency/China Enterprise Management Association	Signed agreement to set up an enterprise management training center in Tianjin. $1.7-2.2 million. 10/9/83.
Price Waterhouse (US)/ China Consultants of Accounting and Financial Management, Inc.	Signed memorandum of understanding to cooperate in auditing, taxes, and other related consulting services. 10/24/83.
(Italy)	Grant for construction of a first-aid center in Beijing and a clinical radiology center in Tianjin. 11/83.
SGV-Byrne & Co. (HK)/ MOFERT, International Trade Research Institute	Signed agreement to cooperate on conferences, seminars, consulting work, and training programs. 11/19/83.

CHINA'S EXPORTS THROUGH DECEMBER 1

Foreign Party/ Chinese Party	Product/Value/ Date Reported
Agriculture	
Chori Co. and Unitika Ltd (Japan)	500 tons of high-quality ultrafilament cotton. $1.44/lb. (¥350/lb.). 10/4/83.
Chemicals	
NA (Japan)/Jinshan Petrochemical Plant, Shanghai	Signed agreement to purchase acetic acid, vinyl acetate monomer, and polyvinyl alcohol. 10/16/83.
Mitsui Co. (Japan)/China Jinshan Association Trading Corp.	3,000 tons of pentane fraction oil. 11/14/83.
Construction	
NA (Saipan Island)/ Guangdong Architects	Contract for construction of 300 houses. 9/18/83.
(Rwanda)/China Road and Bridge Engineering Co.	Signed contract to build a road between Butare and Cyangugu. 10/10/83.
(Egypt)/China State Construction Engineering Corp.	Are negotiating construction of a housing project in the Sixth of October New Town, a water treatment plant, and an urban building and irrigation projects for West Nobaria Development Works. 10/17/83.

(Yemen Arab Republic)/ China State Construction Engineering Corp.	Signed contracts for: 1) Drilling a well for the San'a Mineral Water Plant. $57,000 (261,000 rials); 2) Constructing a health center. $61,500 (280,343 rials); 3) Constructing 100 dwellings in San'a. $5.3 million (24.3 million rials). 10/31/83.

Consumer Goods

Asics Corp. (Japan)	Ordered 100,000 running shoes and 200,000 items of sportswear. 10/6/83.
Marubeni Corp. (Japan)/ Shanghai and Jiangsu	Signed agency contract for 8 million pairs of rubber boots and casual shoes per year. 10/6/83.
Marubeni Corp. (Japan)/ Liaoning	Signed agency contract for 1 million pairs of rubber-soled socks. 10/6/83.

Electronics

Distan Co. (UK)/Shanghai No. 1 TV Sets Factory and China National Electronics Import & Export Corp., Shanghai branch	20,000 'Golden Star' 14" color TV sets. 10/3/83.

Food Processing

Pearl River Chinese Food Mfg. (US)/Guangdong Provincial Food Industry Corp.	Technology and ingredients for preparation of canned Guangdong-flavor goods. 10/17/83.

Foreign Aid

(Benin)	Medicine and medical equipment. $238,000 (RMB120,000). 9/16/83.
(Sri Lanka)	2,000 tons of rice. 10/14/83.
(Uganda)/Red Cross Society	20 tons of rice. 11/1/83.

Machinery

Multifarms Agro-Industrial Development Corp. (Philippines)/Dalian Refrigerator Plant and Harbin Oxygen Producer Plant	Contract signed for cold storage equipment and are negotiating purchase of oxygen producers and cylinders. 10/17/83.

Minerals

Nunes & Son Co. (Colombia) and A-B Oriental Food Imports Inc. (US)/ China National Coal Development Corp.	Agreed to cooperate on development of Colombia's Tasajero coal mine. 10/31/83.
(Colombia)/China National Coal Development Corp.	Signed agreement to build a honeycomb briquet factory. 10/31/83.

Petroleum

Petroleum Corp. (Brazil)	Signed a 5-year crude oil supply agreement. 10/31/83.
British Petroleum/China Nanhai Offshore Joint Service Co. and Taylor Diving Pte. Ltd (US)	Contract for services aboard BP's first drilling rig in the South China Sea. 10/31/83.
Wah Chang International Marine Industry Co. (Singapore)/Huangpu Shipyard	Oil drilling and production rig, Wah Hai No. 1. $30 million. 11/16/83.

Power

Westinghouse Electric Corp. (US)/EQUIMPEX	Signed memorandum of understanding to sell small Chinese hydroelectric turbine-generators. 11/10/83.

Shipping

(Bangladesh)/Wuhu Shipbuilding Factory	A 3,000 hp ocean rescue tugboat. 9/25/83.

Textile Plants and Equipment

(Mali)	Signed agreement for Chinese to overhaul the Sikasso textile mill. 9/2/83.

Transportation

Impex Spring Industries Inc. (US)/Zibo Spring Factory, Shandong	Chevrolet and Ford truck leaf spring. 10/3/83.
(UK) and (US)/Beijing Aeronautical Engineering Institute	Ultralight single and twin seat aircraft. 11/5/83.
(Libya)/Ministry of Railways	Signed agreement to build a railway from Tripoli to Ras Gader. 11/22/83.

Trade Agreements

(Canada), (Nepal), (Sudan), and (Thailand)	Signed trade and economic cooperation agreements during October.

Miscellaneous

Palette and Chen's Garden (US)/Shanghai Corp. for International Economic and Technical Cooperation and China National Complete Plant Export Corp., Shanghai branch	Signed contracts to hire 10 Shanghai chefs. 10/83.
NA (US)/Landscape Architecture Co., Shanghai branch	Are negotiating construction of a Chinese-style garden in San Francisco. 11/14/83.

中外
贸易

DIRECT INVESTMENT/PROCESSING/ COUNTERTRADE THROUGH DECEMBER 1

Foreign Party/ Chinese Party	Arrangement/Value/ Date Reported

Joint Ventures

Biotech Research Laboratories Inc. (US)/Shanghai Cancer Institute	Agreed to develop monoclonal antibodies for the diagnosis and treatment of cancer. 8/11/83.
NA (HK)/Shenzhen Municipal Catering Co.	Formed the Friendship Restaurant Enterprise Co. and will build the Asia Hotel complex in Shenzhen. $25.6 million (HK$200 million). 9/83.
Japan Nanotronics/NA, Shenzhen	Plan to produce liquid crystal devices in early 1984. 9/83.
Chukyo Automobile (Japan)/NA, Shenzhen	Have received approval to set up a joint taxi and repair company, Hua Ri Automobile Co. 9/83.
Middle Systems (US)/ China State Construction Engineering Corp.	Won a contract to build a hospital in the US. 9/18/83.
S. Shamash and Sons Inc. (US)/China Silk Corp., Liaoning branch	Reached agreement to set up a tussah silk dyeing and finishing plant in Haicheng. 9/23/83.
Italmacchine (Italy)/China Chuandong Leather Industry Co.	On Sept. 24 signed 10-year contract to set up the Cogeca and China Chuandong Co. Ltd. in Wanxian County, Sichuan, which will design, produce, and sell leather and sports shoes. (Italy:40%–PRC:60%). 9/28/83.
Well Trading Co. (HK)/ Guangzhou News Photo Society	Opened the Photo Art International Equipment Center on Aug. 28, which will provide technical information, lectures, and purchase foreign photo equipment. 10/3/83.
Nan Hing Investment Co. (HK)/Hainan No. 3 Guesthouse	Will open the Qiongyuan Restaurant. 10/10/83.
BN and ACEC (Belgium)	Will set up a factory in Xiangtan City, Hunan, to produce light rail stocks for urban use. 10/16/83.
Yuan Da Co. (HK)/ Greatwall Wine Co., Hebei and CEROILS	Signed 15-year contract to set up the China Greatwall Wine Corp. Ltd, Shacheng, Hebei, to produce and market wine. (HK:25%–PRC:75%). 10/17/83.

Tokoshoji Co. Ltd (Japan)/Heilongjiang Curved Wood Furniture Factory, Harbin	Signed a contract to sell wood furniture on the international market. Japanese company provided equipment and technical cooperation. 10/17/83.
NA (Sweden)/Beijing Electrothermal Alloy Wire-Drawing Plant	Negotiating an agreement. 10/24/83.
Chiyu Banking Corp. Ltd, Nanyang Commercial Bank Ltd, Hua Chiao Commercial Bank Ltd, Bo Sang Bank Ltd (HK) and Nantung Trust and Investment Co. Ltd (Macao)/Xiamen Construction and Development Co. and Bank of China	Have set up the Xiamen SEZ United Development Corp. to facilitate development of Xiamen. 10/25/83.
Japan National Oil Corp., Getty Oil International Inc., Sun Orient Exploration Co., and Texas Eastern Orient Inc./CNOOC	Have signed contracts for oil exploration in the Pearl River mouth basin. 10/31/83.
Cluff Oil PLC (UK)/CNOOC	Signed oil exploration contract for the northern part of the South Yellow Sea. 10/31/83.
Sinli International Ltd (HK)/Tianjin Municipal Service Co. and Tianjin International Trust and Investment Corp.	Reached an agreement on Oct. 12 to rebuild the Jindong Hotel. 10/31/83.
Whalsay Enterprises Ltd (HK)/Shanxi Corp. for International Economic and Technical Cooperation	Have established a 50-50 venture to help seek investment opportunities in Shanxi, to undertake construction projects overseas, and aid in development of the SEZs and offshore oil exploration. Offices in Taiyuan and Shenzhen. Registered capital: $128,000 (HK$1 million). 10/31/83.
Sinli International Ltd (HK)/Tianjin International Trust and Investment Corp.	Signed agreement to construct the Tianjin International Trade Center. 10/31/83.
IBM (US)/Ministry of Machine Building Industry	Discussing a computer application venture. 10/31/83.
Brown & Root (US)/China Ocean Engineering Services Ltd	Set up the COES Brown & Root Construction Co. to engage in loading, towing, unloading, and installation of equipment for offshore oil exploration. 10/31/83.
Hong Kong Nuclear Investment Co. (China Light & Power Co. and others)/Guangdong Power Co.	Preliminary protocol to jointly construct and manage a nuclear plant at Daya Bay. (HK:25%–PRC:75%). $4.6 billion (HK$36 billion). 11/11/83.
Millie's Group (HK)/China Light Industrial Corp. for Foreign Economic and Technical Cooperation, the Economic Cooperation Dept. and Kunshan County Leather Products Factory, Jiangsu	Signed a 15-year agreement to set up a leather shoe factory in Suzhou to produce 300,000 to 350,000 female leather shoes annually. Registered capital $440,000. (HK:25%–PRC:75%). 11/14/83.
Pennzoil Co. and Sun Co. (US), Ampol Exploration Ltd (Australia), and Hispanica de Petroleos (Spain)/CNOOC	Signed contracts for oil exploration in the southern part of the Beibu Gulf. 11/16/83.
Societe General (France) and Bank of East Asia (HK)/Bank of China	Will set up Trilease International Ltd. in Hong Kong which will lease heavy industrial equipment to China. Paid up capital: $1.3 million (HK$10 million). (France:40%–HK:20%–PRC:40%). 11/16/83.
Utahloy (HK) Ltd/China Nanhai Oil Joint Services Corp. and Guangzhou Suburban District Development Corp.	Signed a 17-year contract to construct the Golden Lake Residential Complex near Guangzhou to house foreign offshore oil personnel. $300 million. 11/29/83.
Phillips Petroleum Co. and Pecten Orient Co./CNOOC	Signed contracts for offshore oil exploration in the Pearl River Mouth Basin. 11/30/83.

Compensation Trade

Mitsubishi Heavy Industries (Japan)/CEROILS, Jiangsu branch	Will build an eel processing plant in China. 9/28/83.
Wing Sun Co. (HK)/Xinhui County, Guangdong	Set up a polyester filament mill. HK investment: $10 million, PRC investment: $8.75 million. 9/30/83.
Eurofil Sas-Pieve Dicentd (Italy)/Laiwu Hemp Mill, Shandong	Are negotiating supply of hemp spinning and weaving equipment in exchange for hemp yarns. 10/10/83.
Daisy Fishing Co., Ltd (Japan)/Jinan Canned Food Factory, Shandong	Negotiating continuation of a 1979 agreement in which Daisy would provide asparagus processing and canning equipment in exchange for canned asparagus. 10/10/83.
Walter Lutsens (W. Germany)/Jinan Canned Food Factory, Shandong	Bottle-sealing machines in exchange for bottled asparagus. 10/10/83.
Soya Bean Products Co. Ltd (HK)/Guangdong Overseas Chinese Farming Bureau	Renewed contract to operate the Guangming Farm in Shenzhen, a dairy farm. 10/30/83.

Licensing

Bergey Windpower (US)	Negotiating production agreement for the BWC 1000 wind turbine. 10/83.
Cargill Inc. (Australia)/China National Seed Corp.	Contract to acquire Chinese hybrid rice technology. 10/83.
Yamaha Motor Co. (Japan)/China North Industries Corp.	Technology to produce small motorcycles. 10/27/83.
Honda Motor Co. (Japan)/Sichuan Xinguang Industrial Products Import and Export Corp. and Jialing Machine Factory	Signed extension of its motorcycle agreement and will provide parts and production equipment. 11/1/83.
Officina Stampaggi Industriali, Sociata Filtri, and Universal Filter (Italy)/Bengbu Tractor Accessories Factory, Anhui	Signed agreement to sell filters for agricultural engines, two filter production lines, and technology. 11/18/83.

Coproduction

Lesnina (Yugoslavia)/Jilin Provincial No. 2 Light Industry Bureau	Signed a contract for joint production of chairs at the Jilin Wooden Goods Factory. 11/7/83.

Leasing

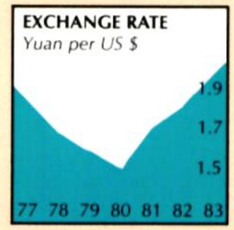
Jikai Chuan Wu Co. (HK-W. German joint venture)/Zhongji Offshore Petroleum Shipping Service Co. Ltd (a joint venture between Jikai Chuan Wu Co. and China-Nanhai Joint Petroleum Service Corp.	Supply boats for offshore oil exploration. 9/83.
Teikoku Denshi Kogyo K. K. (Japan)/China Orient Leasing Co. Ltd and the Anyang Picture Tube Factory, Henan	17" black and white TV picture tube production equipment. $1.42 million. 9/19/83.
Torii Winding Machine Co. Ltd and Endai Bussan Co. Ltd (Japan)/China Orient Leasing Co. Ltd	Plastic bagging and weaving equipment for a plastics factory in Baotou City, Nei Monggol. $700,000. 9/19/83.
Yuasa Trading Co. Ltd (Japan)/China Orient Leasing Co. Ltd and Anyang No. 1 Rubber Plant, Henan	A bicycle tire production line. $220,000. 9/19/83.

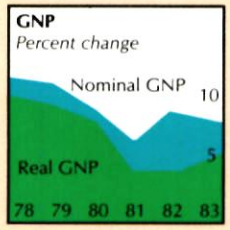
中国数据

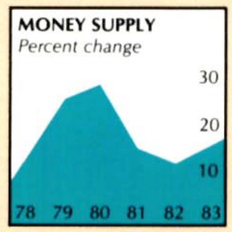
KEY INDICATORS

	1977	1978	1979	1980	1981	1982	1983*	% change 1983/82
Exchange rate (yuan per US $)	1.8578	1.6836	1.5550	1.4984	1.7050	1.8887	1.9770	—
GNP (bil. ¥, current prices)	314.4	350.2	389.1	425.4	450.4	488.7	523.0	7.0
(bil. $, current prices)	169.2	208.0	250.2	283.9	264.2	258.7	264.5	2.2
GNP deflator (1976=100.0)	99.1	100.5	104.5	108.7	111.9	114.2	116.5	2.0
Population (year-end, million)	956.7	969.6	982.2	994.9	1,007.8	1,012.0	1,024.0	1.2
GNP per capita (current $)	176.9	214.5	254.7	285.4	262.2	255.6	258.3	1.1
Gross value of industrial output (bil. ¥, current prices)	360.6	412.4	449.4	497.4	517.8	550.6	609.5	10.7
Of which:								
Heavy industry	209.1	236.3	255.7	263.9	251.5	274.0	309.6	13.0
Light industry	151.5	176.1	193.7	233.5	266.3	276.6	299.9	8.4
Gross value of agricultural output (bil. ¥, current prices)	142.2	156.6	195.1	218.7	244.8	278.5	289.6	4.0
Grain output (million metric tons)	282.75	304.75	332.115	320.52	325.02	353.43	370.0	4.7
Cotton output (million metric tons)	2.049	2.167	2.207	2.207	2.968	3.598	3.8	6.5
Consumer price index (annual % change)	0.2	0.7	2.0	6.0	2.4	2.0	—	—
State budget revenues (bil. ¥)	87.5	112.2	110.3	108.5	109.0	112.4	—	—
State budget expenditures (bil. ¥)	84.4	111.1	127.4	121.7	111.5	115.3	—	—
Currency in circulation (billion ¥)	19.5	21.2	26.8	34.6	39.6	43.9	47.0	7.1

* Year-end projection based on January-November data.



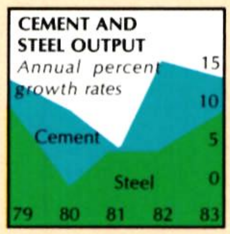


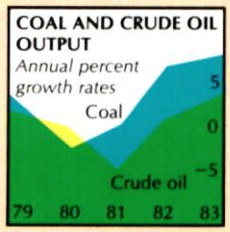


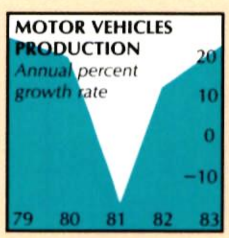
INDUSTRIAL PRODUCTION

(Million metric tons unless otherwise indicated)

	1978	1979	1980	1981	1982	% change 1982/81	1983	% change 1983/82
Cement	65.24	73.9	79.86	84.0	95.2	14.8	106.4	11.8
Chemical fertilizer	8.693	10.654	12.32	12.39	12.781	3.2	14.0	9.8
Chemical insecticides (thousand metric tons)	533.0	537.0	537.0	484.0	457.0	−5.6	340.9	−25.4
Coal	618.0	635.0	620.0	620.0	666.0	7.1	700.3	5.2
Crude oil	104.05	106.15	105.95	101.22	102.12	0.9	106.0	3.8
Electricity (billion kilowatt hours)	256.55	281.95	300.6	309.3	327.7	5.9	351.9	7.4
Ethylene (thou. tons)	380.3	434.9	489.9	504.8	564.9	11.9	667.7	18.2
Locomotives (units)	—	573	512	398	486	22.1	582.7	19.9
Machine-made paper and paperboard	4.39	4.93	5.35	5.4	5.89	9.1	6.5	11.2
Medium and large tractors (thou. units)	113.5	125.6	97.7	52.8	40.0	−24.5	34.3	−14.3
Motor vehicles (thou. units)	149.1	185.7	222.3	175.6	196.3	11.4	239.0	21.8
Natural gas (billion cubic meters)	13.73	14.51	14.27	12.74	11.93	−6.4	11.9	−0.3
Pig iron	34.8	36.7	38.0	34.2	35.5	3.8	37.4	5.3
Plate glass (million standard boxes)	20.0	23.3	27.7	30.6	35.5	16.0	40.9	15.1
Power generating equipment (thou. kw)	4,838.0	6,212.0	4,193.0	1,395.0	1,645.0	17.9	1,903.7	15.7
Rolled steel	22.08	24.97	27.16	26.7	29.02	8.7	30.7	5.8
Rubber tires	9.4	11.7	11.5	7.3	8.6	17.8	12.6	47.0
Steel	31.78	34.48	34.2	35.6	37.16	4.4	40.0	7.7
Walking tractors (thou. units)	324.2	317.5	217.9	198.9	298.0	49.7	478.0	60.4





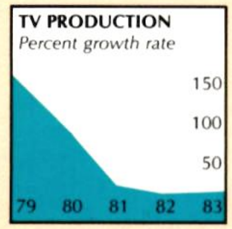


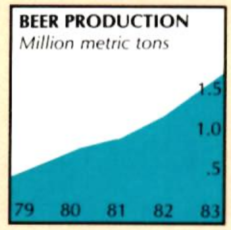
CONSUMER GOODS PRODUCTION

(Million units unless otherwise indicated)

	1978	1979	1980	1981	1982	% change 1982/81	1983*	% change 1983/82
Bicycles	8.54	10.09	13.02	17.54	24.2	38.0	28.0	15.7
Sewing machines	4.86	5.87	7.68	10.39	12.86	23.8	11.0	−14.4
Wristwatches	13.51	17.07	22.16	28.72	33.01	14.9	36.1	9.5
TV sets	.517	1.329	2.492	5.394	5.92	9.8	6.6	11.6
Radio sets	11.68	13.81	30.04	40.57	17.24	−57.5	18.8	9.3
Cameras (thou. units)	178.95	238.0	373.0	623.0	742.0	19.1	824.4	11.1
Light bulbs	760.3	850.0	950.0	970.0	1,070.0	10.3	1,246.6	16.5
Cotton cloth (billion square meters)	10.286	11.43	12.80	13.4	14.92	9.4	14.68	−1.6
Silk textiles (million meters)	610.35	663.45	759.0	835.0	910.0	9.5	964.6	6.0
Beer (thou. tons)	—	—	688.0	910.0	1,170.0	28.6	1,657.0	41.6
Cassette recorders (thou. units)	—	—	743.0	1,546.0	3,471.0	124.5	4,810.0	38.6
Household washing machines (thou. units)	—	—	245.0	1,281.0	2,533	97.7	3,640.0	43.7
Household refrigerators (thou. units)	—	—	49.0	55.6	99.9	79.7	197.6	97.8

* Year-end projection based on January-November data.



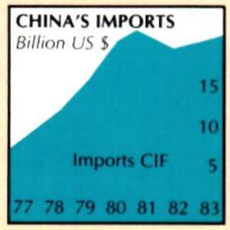


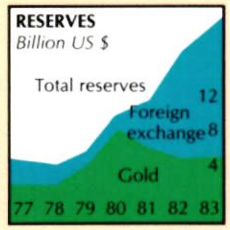
CHINA'S FOREIGN TRADE

	1977	1978	1979	1980	1981	1982	1983**	% change 1983/82
Exports (bil. ¥, fob)	13.97	16.79	21.17	27.12	36.76	41.43	43.5	5.0
(bil. $, fob)	7.52	9.97	13.61	18.10	21.56	21.94	22.0	0.4
Imports (bil. ¥, cif)	13.28	18.75	24.39	29.88	36.77	35.77	39.9	11.5
(bil. $, cif)	7.15	11.74	15.69	19.94	21.57	18.94	20.2	6.6
Total trade (fob/cif)	27.25	35.54	45.56	57.00	73.53	77.20	83.4	8.0
	14.67	21.11	29.30	38.04	43.13	40.88	42.2	3.1
Total reserves (period end, bil. $)	4.85	4.03	6.08	10.04	10.61	15.90	19.3	21.4
Of Which:								
Foreign exchange	2.35	1.56	2.15	2.26	4.77	11.13	14.5	30.3
Gold (bil. $*)	2.50	2.47	3.93	7.78	5.84	4.8	4.8	0.0
Gold reserves (million fine troy ounces)	12.8	12.8	12.8	12.8	12.7	12.7	12.7	0.0

* Gold valued at current market prices based on IMF period average commodity price indices.

** Year-end projection based on January-November data.





FOREIGN TRADE WITH SELECTED COUNTRIES

(Million US dollars)

	1977	1978	1979	1980	1981	1982	1983	% change 1983/82
United States								
Exports (fas)	171.3	823.6	1,716.5	3,749.0	3,598.6	2,904.5	2,100	−27.7
Agricultural)	(40.0)	(565.0)	(492.1)	(2,279.4)	(2,112.4)	(1,707.8)	(700)	(−59.0)
Nonagricultural	(131.3)	(258.6)	(724.4)	(1,469.6)	(1,486.2)	(1,196.7)	(1,400)	(17.0)
Imports (customs value)	202.7	324.1	592.3	1,058.3	1,895.3	2,283.7	2,290	0.3
Total	374.0	1,147.7	2,308.8	4,807.3	5,493.9	5,188.2	4,390	0.3
Share of China's total two-way trade	2.5	5.4	7.9	12.8	12.7	12.7	10.3	—
Japan								
Exports (fob)	1,955	3,074	3,674	5,109	5,075	3,500	4,661	33.2
Imports (cif)	1,560	2,045	2,933	4,346	5,283	5,338	5,117	−4.1
Total	3,515	5,119	6,607	9,455	10,358	8,838	9,778	10.6
Share of China's total two-way trade	24.0	24.2	22.6	25.1	24.0	21.6	22.8	—
Hong Kong								
Exports (fob)	44	63	382	1,249	1,964	1,939	2,312	19.2
Imports (cif)	1,735	2,249	3,021	4,401	5,272	5,397	5,487	1.7
Total	1,779	2,312	3,403	5,650	7,236	7,336	7,799	6.3
Share of China's total two-way trade	12.1	10.9	11.6	15.1	16.8	17.9	18.2	—
W. Germany								
Exports (fob)	501	995	1,493	1,145	1,017	853	1,053	23.4
Imports (cif)	288	367	534	808	769	702	770	9.7
Total	789	1,362	2,027	1,953	1,786	1,555	1,823	17.2
Canada								
Exports (fob)	347	442	507	742	776	1,005	1,201	19.5
Imports (fob)	77	83	143	132	183	165	214	29.7
Total	424	525	650	874	959	1,170	1,415	20.9

SOURCES: State Statistical Bureau, Beijing; IMF, *International Financial Statistics*; IMF, *Direction of Trade Statistics*; and National Council for US-China Trade.

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