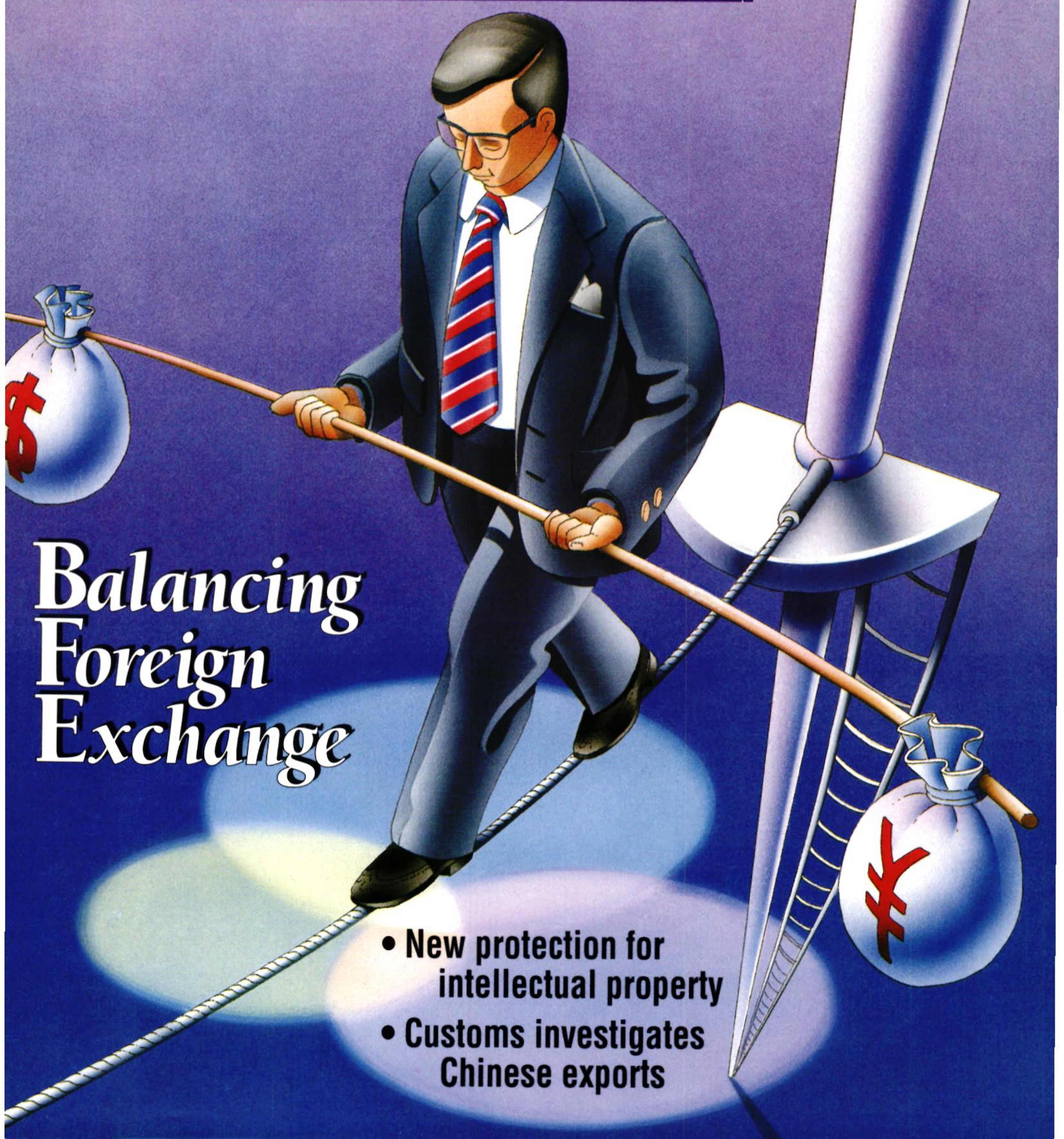
THE CHINA BUSINESS REVIEW

MARCH-APRIL 1992

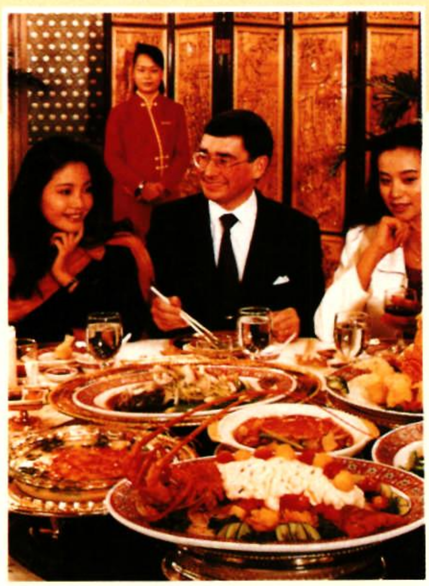
VOLUME 19, NUMBER 2



Balancing Foreign Exchange

- New protection for intellectual property
- Customs investigates Chinese exports

Zhang Xuan's "Lady Kuo-Kuo and her Sisters Setting Forth on an Outing" (Tang Dynasty, 8th century), reworked in 1989 by Sanna Shao in Hong Kong.



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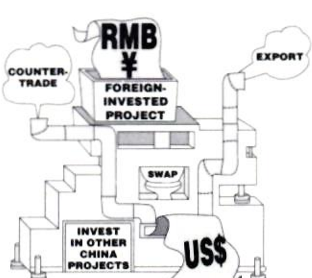
The magazine of the US-China Business Council

Features



Departments

OECD Countries Agree to New Limits on Concessionary Aid

In December, member countries of the Organization for Economic Cooperation and Development (OECD) agreed to new restrictions on mixed credits and concessionary financing to China and other developing countries. Following two years of negotiations, 23 OECD members—all but Iceland—agreed to abolish tied aid altogether for many newly emerging industrial economies (by UN definition), such as South Korea, Singapore, Brazil, Mexico, Uruguay, the Bahamas, Hong Kong, and most of Eastern Europe. For China, India, Thailand, Indonesia and other countries determined to be at "mid-level" economic development, commercially viable projects are no longer to be funded with concessionary funds. No restrictions were placed on projects in lesser-developed countries, such as the sub-Saharan African nations, which can continue to receive concessionary aid for any project.

Effective February 15, the agreement will likely require all new OECD lending to conform to the guidelines, though full details on implementation of the agreement have yet to be worked out. It is unclear, for instance, exactly how "commercially viable" projects are to be defined, and by whom. Concessionary aid programs announced prior to October 31, 1991 will be allowed to continue under previous guidelines.

The agreement is a victory for US government officials, who have long been dissatisfied by other countries' rampant use of concessionary aid, which routinely leaves US companies out of the bidding on major projects. The new agreement follows a 1987 OECD attempt to discourage tied aid for commercially viable projects by requiring each offer of mixed credit to provide at least 35 percent of the funds in outright grants. This "gentlemen's agreement," however, was widely acknowledged to have failed, casting some doubt on whether the latest OECD initiative can achieve its goals. If it can be successfully implemented, though, US companies may soon find it easier to compete with companies from other OECD countries. —VLW

Chinese Securities Markets Issue Foreign "B" Shares

Following record gains in 1991, both the Shanghai and Shenzhen securities exchanges took a further step toward marketization recently by issuing special shares for foreign investors. The Shenzhen exchange acted first, when China Southern Glass issued 16 million B shares at $5.30/share in December. Hoare Govett Asia, the underwriter, reported that the shares—the first in China to be issued to foreigners since 1949—were quickly purchased by US and Asian buyers.

The Shanghai Vacuum Electronic Device Corp. issued its stock to foreigners in January, bringing the Shanghai Stock Exchange into the international arena as well. Underwritten by SBCI Asia Ltd., Sun Hung Kai & Co., and Salomon Brothers Inc., the one million B shares with face value of ¥100 were sold at ¥420/share. Trading of both foreign-issue shares is to begin this spring.

A number of other Chinese companies have reportedly received government permission to issue B shares to foreigners, and a third official securities market is apparently planned for Guangzhou. In the meantime, the number of companies listed on the two official exchanges continues to grow. Demand is likely to outweigh supply for some time, however, leaving foreign and Chinese buyers alike scrambling for the shares available to them. Shanghai officials, for example, were forced to postpone the listing of two new stock flotations last year when traffic was stalled by huge crowds of would-be purchasers. With an estimated 10 percent of the city's population interested in playing the market, Shanghai officials even attempted to institute a lottery system to select a lucky few from among the many eager buyers. —VLW

China Broadens International Ties

In recent months, China's leadership has made efforts to expand its economic and political links with a number of countries. In December, Beijing and Seoul signed a bilateral trade agreement which will likely further spur trade between the two countries; according to South Korean estimates, two-way trade with China exceeded $5 billion in 1991. Other trade and investment accords planned for 1992 will add to the growing economic ties, though no formal diplomatic ties between China and South Korea currently exist.

China has, however, normalized diplomatic relations with Vietnam and Israel. In November, Premier Li Peng and Chinese Communist Party General Secretary Jiang Zemin met with Vietnamese leaders in Beijing to announce the re-establishment of full diplomatic relations between the two countries. In January, China and Israel established diplomatic relations for the first time, reportedly out of China's desire to join in the Middle East peace process. —VLW

Short Takes

Asian Development Bank Funds Energy Study

In January, the Asian Development Bank approved a $600,000 technical assistance grant for the analysis of energy supply and demand in China. The funds will help the Chinese government carry out integrated planning for the electricity sector and develop standardized forecasting models at the provincial level.

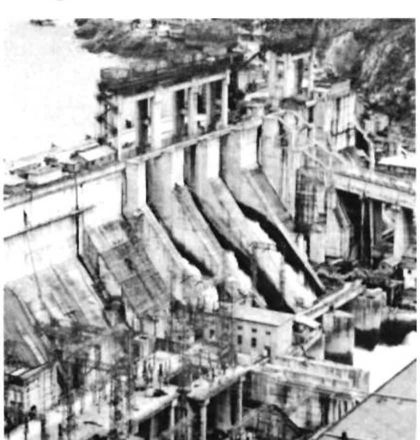
Commerce Postpones CVD Ruling

The US Department of Commerce postponed its preliminary ruling on the first countervailing duty (CVD) case it has accepted against China in a decade. The ruling on oscillating fans is now due March 10. In the meantime, another CVD case—involving Chinese lug nuts—has also been filed with Commerce.

World Bank Funds Power, Water Projects

The World Bank's executive board in January approved a $180 million loan for the Yanshi Power Project, the third power sector loan for China since the beginning of the Bank's 1991 fiscal year last June. The project will assist in the construction of two 300 MW coal-fired thermal power units near Henan Province's coal mines.

In February, the Bank approved a $110 million line of credit from the International Development Association to improve the water supply and sanitation facilities in Guangxi, Yunnan, Gansu, Xinjiang, and Inner Mongolia.



LETTER FROM THE EDITOR

Lean, Mean, and Green in '92

Although I am late by virtually all calendars, whether solar or lunar, I want to wish all of you a happy 1992—the year of the monkey. According to the Chinese zodiac, monkey years are supposed to be auspicious. Here at *The CBR*, we are instituting some changes we hope will improve our product and our fortunes.

Those of you with sharp eyes may notice some differences between this and previous issues of *The CBR*; for one, this issue is printed on recycled paper with post-consumer content. We have been striving to convert to recycled stock for some time now, and are pleased to be doing our small part to conserve the environment. We've been aided in this effort by our new printer, whose expertise and state-of-the art equipment will enable us turn out a consistently superior-quality product. Moreover, a significantly faster turnaround time should help us speed *The CBR* to your desks.

Other significant changes come in the area of personnel. I am pleased to welcome aboard Paula Nourse Ragland, who has assumed the position of CBR circulation manager. Paula comes to us from the *Dallas Business Journal*, where she was director of marketing and circulation. Her wealth of experience promises to keep us in the forefront of Asian business periodicals. With Paula in Washington we plan to re-locate Business Manager Daniel P. Reardon to Hong Kong within the next few months, in order to boost our coverage of the territory and reach out to a broader audience.

We believe these changes will make *The CBR* better than ever in 1992. We have a strong editorial package lined up for the rest of the year, with upcoming issues to examine such topics as the automobile component and pharmaceutical industries; the growing economic integration of China, Taiwan, and Hong Kong; housing for employees of foreign-invested enterprises; and of course, the 301 negotiations and debate over renewal of China's Most Favored Nation trading status. I welcome your thoughts on these and other areas of interest, as well as on our new paper.

Best regards,

Pamela Baldinger

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Letter from the President

Recent agreements on intellectual property protection and shipping illustrate that a case-by-case approach is the way to handle our various grievances with China.

Off to a Good Start

While soothsayers may be busy forecasting what to expect in the Year of the Monkey, the early signs in the business world indicate that both the United States and China are serious about resolving the many trade disputes that surfaced last year. January 1992 saw progress on several different fronts, bringing renewed optimism to some companies doing business with China. Though the laundry list of other trade grievances is long, there is reason to be hopeful that the breakthroughs so far are good omens for improved US-China business relations in 1992.

On intellectual property protection, an issue closely watched by much of the Council's membership, negotiators reached a last-minute resolution of the Special 301 investigation of China's protection of intellectual property rights (*see* p. 9). The Memorandum of Understanding signed January 17 in Washington provides for the first time a framework for applying international standards of patent and copyright protection to American products in China. The agreement was widely praised by a broad range of US companies, from designers of computer software to producers of pharmaceuticals and agricultural chemicals. Though these companies will likely face ongoing problems—and possibly, litigation—to ensure that their patents and copyrights are adequately protected in China, the agreement provides a firm basis of agreed principles with which to solve these problems. More important, by reaching agreement on this issue the United States and China avoided a potentially acrimonious round of sanctions and counter-sanctions that could have had serious long-term implications not only for bilateral trade relations, but for the broader political relationship as well.

Less attention was given to an important step taken by China to resolve the ongoing dispute over maritime affairs. Around the same time that US and Chinese negotiators reached the Special 301 agreement, the Chinese acted to honor an important aspect of the Memorandum of Consultation they signed last fall (*see The CBR,* January-February 1992, p. 5) by agreeing to let US shipping companies American President Lines Ltd. and Sea-Land Service Inc. establish fully operational branch offices in China. Just as the China Ocean Shipping Co. (COSCO) operates in the United States, these companies will now be able to conduct business in China without going through Chinese agents.

This move should be enough to stop the imposition of sanctions threatened by the FMC, as US shippers will have far greater access to the China market. US sanctions would probably have been matched by the Chinese, which would have resulted in less business for US and Chinese carriers and higher prices for US importers.

These successes should enable both Beijing and Washington to take on the next major trade hurdle in a more positive light. The US Trade Representative (USTR)'s Section 301 investigation of market barriers to American exports to China must be concluded by October 10 this year, though both sides indicate they would like to end the negotiations earlier. Preliminary talks on the transparency of China's trade laws and regulations, import bans and quotas, import licensing rules, and technical barriers (including phytosanitary and veterinary standards) have already been held. But with the Special 301 negotiations behind them, both sides can now focus on these broader, more complex, issues. Sources at USTR indicate that while they expect the negotiations to be long and difficult, they believe the intellectual property agreement has demonstrated that both sides understand the importance of avoiding a crisis in US-China trade relations.

Such understanding, however, apparently has not extended to the sensitive issue of alleged exports of prison-made products to the United States. Negotiations have stalled over the question of foreign inspection of Chinese labor camps suspected of infringing the ban on exporting to the United States. Failure to resolve this issue could lead to congressional action to strengthen US laws dealing with such exports (*see* p. 42), which in turn would increase risks and costs even for those companies importing legally from China.

Obviously, we have a long way to go in the 301, prison labor, and other negotiations to bring the overall relationship back from the depths to which it sank after Tiananmen. Nevertheless, the limited successes achieved thus far have demonstrated that the Bush Administration's targeted approach to our problems with Beijing are proceeding at a slow but steady pace. Certainly, such efforts will ultimately prove more effective than draconian measures such as outright denial of Most Favored Nation status for China.

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Improving Protection of Intellectual Property

The recent Sino-US accord should boost commerce in certain sectors

Joseph T. Simone, Jr.

In mid-January, the United States and China reached a last-minute agreement on intellectual property rights, lifting the threat of US sanctions against China for its failure to adequately protect American copyrights, patents, trademarks, and trade secrets. In a Memorandum of Understanding (MOU) signed on January 17, the US Trade Representative (USTR) agreed to terminate its Special 301 investigation into China's intellectual property practices in exchange for a number of commitments by the Chinese government.

Signed only hours after the January 16 deadline set by USTR, the accord was welcomed by both sides, as failure to resolve this dispute was expected to lead to the imposition of trade sanctions affecting an estimated $700 million worth of Chinese exports to the United States. In the final weeks of the negotiations, the Chinese threatened to retaliate in response to any US sanctions, a move which would have led to a significant—and perhaps irreversible—deterioration in US-China trade relations.

In the MOU, the Chinese government agreed to join two international copyright conventions within the next 18 months and to take necessary steps over the next two years to enact new laws and regulations that will expand the scope of protection for American intellectual property. Virtually all of these improvements will benefit Chinese and other foreign rights holders, not just Americans. Salient improvements include the following:

- Extension of copyright protection for the first time to foreign owners of software, books, films, sound recordings, and other subject matter;
- Removal of the prohibition against patenting of pharmaceuticals and chemicals; and
- Protection against various forms of unfair competition, including misappropriation of trade secrets.

Computer programs will be protected in China under the category of "literary works," as specified in the Berne Convention.

Conforming to international standards

China agreed to use "best efforts" to accede to the Berne Convention for the Protection of Literary and Artistic Works (Berne Convention) effective no later than October 15. Over 80 countries are members of this convention, which is administered by the World Intellectual Property Organization of the United Nations. According to the MOU, a bill authorizing accession to the Berne Convention should be submitted to the National People's Congress or its Standing Committee for approval prior to April 1.

The MOU provides for protection of American copyright works 60 days after its conclusion, or March 17, and the United States has agreed to ensure reciprocal protection for Chinese copyrights before this date. Thus, American works will be protected in China as long as seven months before other foreign works are protected.

China also agreed to use best efforts to accede to the Geneva Phonograms Convention by June 1, 1993. This convention provides standards for protecting the exclusive rights of producers of sound recordings, such as compact discs and records.

Under the MOU, computer programs will be protected in China under the category of "literary works," as specified in the Berne Convention. As a consequence of this change in categorization, software is to be protected for 50 years—without imposition of any mandatory formalities. Accordingly, the mandatory registration requirements currently imposed by China's Regulations for the Protection of Computer Software, which entered into effect on October 1, 1991, should eventually be lifted, at least for foreign software owners. The Ministry of Machine-Building and Electronics Industry (MMEI) was vehemently opposed to these concessions, but the Chinese government was reportedly swayed toward a compromise by the

Joseph T. Simone, Jr., a US lawyer with the Hong Kong office of Baker & McKenzie, advises on investment and intellectual property matters in China and writes regularly on these issues for a number of legal journals. The views expressed above are those of the author alone.

preliminary accord to protect software as a literary work reached by GATT member countries last December.

At present, it remains unclear whether registration requirements for American software will be suspended as soon as bilateral copyright relations are established (March 17) or upon China's accession to the Berne Convention (by October 15). When other provisions of the MOU affecting US software companies become effective is also less than clear. Under China's current software regulations, software first published prior to June 4, 1991 (the date the regulations were promulgated) is effectively relegated to the public domain. The MOU relaxes this severe limitation by stating that copyrighted works—including software—which are not in the public domain in their country of origin will be protected in China pursuant to its accession to the Berne Convention. However, the MOU does not address whether American software that was published before June 4, 1991 will be protected as of March 17 or only after China's accession to the Berne Convention.

It is widely believed that most foreign software used in China today was copied without authorization from the copyright owner. The MOU deals with this situation by providing that copyrighted works which were "owned and used" in China before March 17, 1992 may continue to be used, provided that they are "neither reproduced nor used in any manner that unreasonably prejudices the legitimate interests of the copyright owner." This potentially over-broad exclusion has caused alarm among certain US software and entertainment companies, which hope that the Chinese will issue regulations in the near future to significantly restrict the scope of this exclusion.

Upgrading the Copyright Law

Chinese officials have acknowledged that certain provisions of China's new Copyright Law (*see The CBR*, November-December 1990, p. 4) are inconsistent with the minimum standards imposed by the Berne Convention. In the MOU, therefore, China acknowledged that pursuant to Article 42 of its General Principles of the Civil Code, the provisions of international treaties such as the Berne Convention will prevail over those of domestic legislation, such as the Copyright Law and its implementing regulations. In practice, however, it has proven extremely difficult to assert rights in China based solely on treaty provisions. For example, foreign trademark owners theoretically enjoy a number of rights under the Paris Convention for the Protection of Industrial Property (Paris Convention) which are not found in China's Trademark Law, but Chinese trademark officials at both the national and local levels are reluctant to apply the Paris Convention in disputes involving foreign trademarks because of the lack of corresponding provisions in domestic law. Addressing such concerns over the enforceability of treaty law, the MOU requires China to issue regulations—before October 1—which will provide foreigners the higher standards of protection imposed by the Berne Convention. The MOU also requires China to consult with the United States during the drafting of these regulations and to take American views "into consideration."

Many of the inconsistencies between the Copyright Law and the Berne Convention are of critical importance to US industry. For instance, the Copyright Law fails to provide exclusive rights for unpublished foreign works. The law also fails to provide exclusive rights over public performances of films and sound recordings, e.g., the display of films and videos to small groups and the broadcast of sound recordings in public places, such as restaurants and hotels. USTR has given the Chinese a long list of these and other copyright-related provisions it regards as inconsistent with the Berne Convention. The failure to mention many of these perceived inconsistencies in the MOU suggests that the Chinese have not yet agreed to incorporate all of USTR's concerns into future copyright regulations. It is possible that continued resistance by the Chinese on some or all of these issues could lead USTR to commence a new Special 301 investigation, although Chinese and American officials consider this unlikely.

The regulations to be issued before October 1 will temporarily result in two tiers of copyright protection in China: one for Chinese citizens and another, higher tier for foreigners. The MOU, however, requires China to amend its core copyright legislation "within a reasonable period of time"—possibly as long as three or four years—after which time the works of Chinese citizens and foreigners will likely be protected at identical levels.

New rights for patent holders

Aside from the copyright law revisions, China also agreed to amend its Patent Law before January 1, 1993, to permit patenting of new pharmaceutical and chemical inventions, including agricultural chemicals such as fertilizers and pesticides. Current law permits only the patenting of manufacturing processes relating to such substances. This new protection should lead to greater foreign investment in China's pharmaceutical and chemical sectors.

The MOU also expands the scope of protection for process patents. Currently, the infringement of such patents is defined to include manufacturing only; following amendment of the Patent Law, infringement will also be deemed to exist upon the unauthorized sale or importation of products manufactured with the use of patented processes. The amended Patent Law will also extend the duration of patents from the current 15 years to 20 years, though it remains unclear whether this extension will apply to patents issued prior to the amendment of the law.

Existing American drugs and agricultural chemicals, which will not qualify for protection under the amended Patent Law, receive special treatment under the MOU. The document states that such items will enjoy patent-like protection through administrative means if the following conditions apply:

- They were patented in the United States between January 1, 1986 and January 1, 1993;
- They have not been previously marketed in China, presumably by either the American patentee or an unauthorized Chinese enterprise; and
- They are intended to be manufactured or sold in China, as evidenced by a contract with a Chinese or foreign-invested enterprise.

This administrative protection will last for seven and one-half years, commencing from the date administrative authorities issue an approval certificate. It is uncertain whether this "pipeline protection" will be extended to drugs and agricultural chemicals patented by non-Americans.

The other major change to be made in the Patent Law involves liberalization of the terms defining patent use. Under the current law, if a patent is not "used" in China for three consecutive years, Chinese patent authorities may issue a "compulsory license" permitting a Chinese enterprise to use the patent upon payment of compensation to the patentee. Use which would preclude the issuance of such a license is defined to include only the manufacture of goods in China which incorporate the patent. The MOU relaxes this condition by permitting patentees to satisfy the use requirement by either importing the product or manufacturing it in China. In addition, the MOU provides an elaborate set of new procedural conditions for the issuance of compulsory licenses. Presumably, these conditions will be incorporated into the amended Patent Law.

Protecting trademarks and trade secrets

The MOU does not expressly mention trademarks in its text, in part because China has already made visible progress in this area. China is well along the path to amending its 1982 Trademark Law; drafts of a revised law have been circulating for the past two years. The most recent draft, dated August 1991, should make substantial improvements on the present law.

The current Trademark Law extends protection only to marks which have been registered with the PRC Trademark Office. Unauthorized use of another company's unregistered trademark and "trade dress" (e.g., designs and shapes of product packaging) are generally not actionable. However, the MOU requires China to enact an unfair competition law before January 1, 1994, which will address infringements covered by Article 10bis of the Paris Convention. Under Article 10bis, member countries are obliged to protect against acts of unfair competition which could lead to consumer confusion. Such acts are generally referred to as "passing off" and are considered by most countries to include infringements of trade dress and unregistered trademarks.

American industry groups have hailed the MOU as an important step in bringing China's intellectual property laws in line with international practice.

As a member of the Paris Convention since 1985, China, at least in theory, is already obliged to provide protection against passing off. However, the lack of domestic legislation in this area has made it difficult for Americans and other foreigners to take advantage of this supposed protection.

Under the MOU, however, China is required to enact trade secrets legislation by January 1, 1994. At present, limited protection of confidential business or technical information is available only in cases where the owner of secrets has entered into a written agreement with the company to which it wishes to disclose information. Expanded protection of trade secrets under the new legislation will likely increase technology licensing to China.

Staying informed

Both governments agreed in the MOU to publish and exchange copies of "guidance provided to [their respective] administrative or judicial bodies" which concerns laws or regulations relating to the MOU. These provisions are likely intended by the United States to ensure that the scope and enforcement of intellectual property in China will not be governed by internal (*neibu*) regulations which are normally unpublished and unavailable to foreigners. USTR has raised a general complaint about the Chinese government's use of *neibu* documents in the separate 301 market access investigation that is still pending.

For the most part, American industry groups have hailed the MOU as an important step in bringing China's intellectual property laws in line with international practice and in encouraging new types of high-tech investment by American companies. However, it remains to be seen whether US companies will be satisfied with China's progress in drafting new legislation over the next two years. If not, many may decide to delay investments or sales in China until legislation is further amended or proven effective in practice—processes which may take several years.

There is also some mystery over whether the Chinese are capable of adhering to the timetables indicated in the MOU for enactment of the legislation. The obligations set forth in the MOU were agreed to by the Ministry of Foreign Economic Relations and Trade (MOFERT) on behalf of the entire Chinese government, but it is uncertain whether MOFERT succeeded in obtaining a full consensus from the other relevant ministries before signing the MOU.

Finally, there is reportedly a high degree of disagreement and disarray among various ministries as to the methods to be employed to enforce new and existing legislation. For example, the National Copyright Administration and MMEI are reportedly at odds over which of the two entities is responsible for dealing with software infringements. Likewise, the National Copyright Administration and the Trademark Office have not yet begun consulting with each other to formulate procedures for addressing infringements of unregistered trademarks, product labels, and applied art—items that may be protectable under copyright but are more appropriately handled by regional administrations for industry and commerce.

Despite these potential problems, the Chinese government clearly deserves credit for its long-term efforts in encouraging respect for intellectual property. Major laws and regulations on intellectual property and technology transfer have been issued almost every year since 1982. Progress in both legislation and enforcement has been steady (if frustrating) and further improvements are clearly in the offing. Coping with the present, however, will remain a vexing task for Chinese and foreigners alike. 完

COMMENTARY

Developing a China Policy

Max Baucus

Over the last three years, US relations with China have been the subject of intense congressional debate. China's violation of basic human rights, its sales of dangerous weapons, and its unfair trade practices add up to a reprehensible record. China has clearly joined a short list of international renegade nations that includes Libya, Iraq, and Iran. Quite understandably, there have been frequent calls for sanctions against China.

In my mind, it is unfortunate that this debate has centered on whether or not we should extend Most Favored Nation (MFN) trading status to China. The heated debate over whether MFN is the appropriate tool for addressing our concerns with China obscures a broad consensus on the issue. The Administration and some in Congress—including myself—strongly oppose using MFN status as the tool to push for reform in China.

We oppose conditioning or withdrawing MFN because it would be exactly the wrong approach. Instead of encouraging reform in China, withdrawal of MFN would break the growing business ties between China and the United States, devastate US export industries, and push China further into the hands of hardline Marxists. A unilateral cut off of MFN would hurt the United States far more than it would hurt China—especially since no other nation would follow the US example.

But the debate over MFN is a debate over means, not ends. In fact, there is a consensus in the Congress, in the Administration, in the public, and in the business community that China's behavior is intolerable and that the United States must be a force for reform. The disagreement is about how we best achieve this goal, not over whether it is worth achieving.

A new consensus

One of the positive results of last year's congressional debate over MFN was the emergence of the foundations of a new consensus on policy toward China. Last July, at the urging of myself and other senators, President Bush articulated a comprehensive US policy for addressing US concerns with China. The essence of this policy is that the United States will pursue carefully-tailored policy tools to win reform in China. At the same time, the United States will continue to grant MFN status in order to nurture vital business ties with China.

This policy is often referred to as "constructive engagement." With this new policy in place for over six months and with the Senate once again moving to consider China's MFN status, it is appropriate to examine the results on three key issues: trade, weapons and nuclear proliferation, and human rights.

- **International trade**

Under the guise of an austerity campaign launched in 1988, China became the most potectionist nation on earth. China allowed—in fact, sanctioned—piracy of United States intellectual property, particularly pharmaceuticals and computer software. This piracy cost the US close to $1 billion per year in lost export opportunities. But the piracy of intellectual property is but the tip of the iceberg. China also imposed a web of new trade barriers, including import bans, import licenses, quotas, and discriminatory testing requirements to exclude the exports of the United States and other nations.

Not surprisingly, the US bilateral trade deficit with China ballooned. In 1991, the US trade deficit with China reached $12 billion—exceeded only by the US deficit with Japan. Last July, the Bush Administration articulated a new trade policy toward China. The central premise of this policy was that if China expected continued access to the US market for its exports, it must open its market to US goods. Two separate unfair-trade actions were launched—one on intellectual property protection and one on general trade barriers.

The case on intellectual property has now been successfully resolved. After the United States threatened to block some Chinese exports unless the piracy ceased, China agreed to sweeping new patent and copyright protections. The new agreement protects US films, computer software, drugs, agrichemicals, and other products.

Though we must carefully monitor implementation of this agreement before judging its results, all US intellectual property industries have hailed the agreement as a major breakthrough. The agreement is concrete evidence that the United States can win reforms in China if it pursues carefully targeted policies, rather than cutting off MFN. But much

Max Baucus is senator from Montana and chairman of the Senate Subcommittee on International Trade. He has played a crucial role in maintaining the 34 Senate votes needed to preserve unconditional MFN status for China. The text of this article was originally delivered as a speech at the February 5 conference "American Economic Relations with Greater China," co-sponsored by the China Business Forum and the American Enterprise Institute.

MFN is not the appropriate tool for demonstrating US disapproval of China

work remains to be done in the trade area. The broader trade action on Chinese trade barriers has still not been resolved. The case was formally launched last October. Under US trade law, the Administration has a full year to resolve the case before it is obligated to retaliate against Chinese exports to the United States. But I see no reason to wait that long. We have been negotiating with the Chinese over these trade barriers for many months. If an agreement is not reached by late this spring, the President should retaliate against Chinese exports to the United States.

On a related issue, the Administration has promised to stop allowing China to dictate US policy toward Taiwan. In particular, the Administration pledged to strongly support Taiwan's application to join the General Agreement on Tariffs and Trade (GATT)—a step that is clearly in the best interests of both the United States and Taiwan. The Administration has been working behind the scenes to prepare the way for Taiwan's application. But it is now time to launch a much more public effort. China cannot be allowed to dictate US policy toward Taiwan.

• Weapons and nuclear proliferation

For several years, the entire civilized world has shuddered at reports that China has been selling dangerous nuclear and missile technologies into unstable regions. Reports of Chinese sales of long-range missiles to Syria and Pakistan and nuclear technology to Iran raised the specter of nuclear conflict in the Middle East. The Western world demanded that China observe international accords limiting such sales. In particular, the United States pressed China to sign the Nuclear Non-Proliferation Treaty (NPT) and the Missile Technology Control Regime (MTCR). The Bush Administration also committed to continue and, if necessary, expand trade sanctions targeted at China's missile and nuclear materials industries.

As a result of pressure from the United States and other Western nations, China now appears ready to sign the NPT and to abide by the MTCR. But China has not finalized its commitment to either agreement. At his February meeting with President Bush, Chinese Premier Li Peng finally committed to an exchange of letters with the United States formalizing China's agreement to abide by the MTCR. But until the exchange is completed and reports of Chinese violations are fully investigated, the current sanctions should remain in place.

• Human rights

I am most disappointed with the progress that China has made on human rights. We all remember the horrible images of the massacre in Tiananmen Square. China has steadfastly refused even a full accounting of its political prisoners. The Administration agreed last July to continue sanctions and employ its diplomatic leverage to win freedom for China's political prisoners, including those from Tiananmen Square.

In the last few months—thanks largely to US pressure—we have seen the release of a few political prisoners and a rough accounting of the fate of most political prisoners. Hopefully, this is a sign that progress is being made. But make no mistake about it, China has a very long way to go. Until China releases the prisoners of Tiananmen Square, ties with the United States will remain strained. The only way for China to put the tragedy of Tiananmen behind it is to release all the Tiananmen prisoners. The United States must continue to put diplomatic pressure on China toward that end. This pressure should include continued opposition to multilateral lending to China.

In blatant violation of US law, China has also exported goods made by prison labor—including political prisoners—to the United States. Morally, the United States cannot allow itself in any way to support China's system of political oppression. Last summer, the President agreed to step up efforts to block Chinese exports of goods made with prison labor. These efforts have borne fruit. The Customs Service has seized exports of apparel, tools, and a number of other products suspected of being made with prison labor. It has also set up an office to investigate claims that imported goods may be made with prison-labor. The United States is also seeking to negotiate an agreement with China to end all exports of prison-labor goods and allow the United States to make inspections in China to enforce the agreement. Here again, more remains to be done, but we are making progress. Hopefully, we soon can be assured that the US consumer is not being made an unwitting accomplice to China's system of political oppression.

The real issue

I hope that the letter the President sent to Congress last summer outlining a new policy can provide the basis for a strong consensus on China policy. Advocates of employing MFN to address our concerns with China have done us all a service by drawing attention to China policy and Senator Mitchell, in particular, deserves praise. But I fear the continuing debate gives Chinese leaders the impression that there is support in the United States for China and its policies. There is no support for China's current policies. As I said at the outset, there is a consensus that China's behavior must change. I was very concerned over President Bush's recent meeting with Li Peng because I feared it further gave the Chinese leadership the impression that the United States was divided in its assessment of China's policies.

Unfortunately, the Congress seems headed for another round of debate over MFN for China, debate that may further obscure the underlying consensus. Barring some dramatic change, the outcome of this debate seems clear. The Congress will pass legislation restricting MFN. The President will veto it. And the veto will be sustained.

Perhaps this exercise is now inevitable. But once this debate on MFN is over I hope we can put the issue of MFN behind us and turn to the real issue: encouraging reform in China. There is already a basis for consensus. The Administration has demonstrated a willingness to address the issues that the advocates of restricting MFN to China have raised. I hope once the current legislative battle is over we can build a China policy that we all support instead of further debating MFN status for China. That policy should include continuing to engage China through trade. At the same time, we should vigorously use all appropriate policy tools to demand reform in China.

Balancing Foreign Exchange

Improvements in currency supply and exchange rates at swap centers have not eliminated the need for other strategies

Virginia Davis and Carlos Yi

The amount of newly contracted foreign investment in China exceeded $11 billion last year, a 68 percent increase over 1990 levels. This dramatic rise reflects the recovery of the Chinese economy since the events of mid-1989, the thawing of relations between the mainland and Taiwan, and a growing consensus among investors that prospects for solving what is arguably the most important issue facing joint ventures in China—balancing foreign exchange receipts and expenses—have improved. This is largely due to the experience gained by foreign companies over the past decade and increased flexibility on the part of the Chinese government in recent years. In the words of one foreign joint-venture executive, "Foreign-exchange balancing is now much less of an enigma to foreign enterprises."

Much of the improvement in the foreign exchange situation is due to the rapid development of foreign-exchange adjustment—or "swap"—centers. Exchanging *renminbi* profits for foreign currency at the centers is now more predictable and much less expensive than just a few years ago. In 1988, for example, the swap market exchange rate was nearly double the official rate; now, the average ¥5.9/$1 swap rate is only slightly higher than the official rate of ¥5.46/$1 (*see* graph). The gap between the supply and demand of US dollars and *renminbi* in the centers has therefore narrowed substantially, and business has been strong: from January to July 1991, a total of $10.4 billion was exchanged at the centers, a 57 percent increase over the same period of 1990.

The generally optimistic scenario in the swap centers, coupled with recent reports that China intends in the not-distant future to eliminate its two-currency system, have given many potential foreign investors new confidence in China projects. However, while these trends are certainly positive, balancing foreign exchange will continue to be a problem until China's currency becomes fully convertible.

While the trends are positive, balancing foreign exchange will continue to be a problem until China's currency becomes fully convertible.

Until that time, foreign companies manufacturing in China for sales to the domestic market will be particularly at risk to foreign exchange shortages, for though their sales revenue consists almost entirely of non-convertible *renminbi*, they must have foreign exchange to import raw materials, pay expatriate salaries and expenses, and remit profits. Although the Chinese government no longer strictly objects to foreign companies producing for the domestic market, it requires them to devise strategies for converting *renminbi* profits into foreign exchange without draining China's hard-currency reserves. Yet because such companies are not geared to exporting their products in significant quantities, they tend to have a hard time tapping steady domestic sources of foreign exchange. Though the increasing number—and declining cost—of swap centers has made this problem less acute than in the past, companies should not be lulled into a false sense of security.

Relying solely on swap centers is indeed risky; it means assuming that the supply of foreign currency will remain plentiful, and that one's company will always have access to it. Although China performed well financially in 1991, the central bank could again clamp down on credit as it did in 1989-90, thereby stifling the flow of *renminbi* available in the centers, or a particular company or industry could suddenly find that its needs are given last priority at the swap centers. In order to protect themselves from such unforeseen circumstances and ensure a measure of control over their own finances, foreign-invested enterprises (FIEs) should strive to diversify their foreign-exchange balancing methods.

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Planning early

There are numerous methods of generating foreign exchange in China, provided that FIEs use them skillfully and devote enough time and resources to implement them properly. Allocating adequate resources requires that companies examine the foreign exchange balancing issue early on, in the feasibility study stage of their projects, in order to realistically and thoroughly assess their ventures' foreign-exchange earning potential. Companies new to China—or those with particularly large foreign exchange requirements—may wish to invest with a foreign partner with some previous experience.

Businesses in the planning stages of a potential investment contract should keep in mind that their written contracts must be flexible enough to allow them to adjust to changing business conditions. For this reason, FIEs geared to the domestic market usually find that it is better not to be too specific in writing about how they will balance their foreign exchange. For example, a company may include an export target in its investment contract, but should avoid committing itself to meeting it. In such circumstances, the venture will probably be required to demonstrate to Chinese authorities an in-depth understanding of the other foreign exchange balancing options available to it; in no case should an FIE—especially one targeting the domestic market—expect to receive foreign currency from the Chinese government.

Legally, cross-border swapping is permitted, but regional protectionism is a problem.

Swap centers: fast and convenient

Currently, the most popular way of balancing foreign exchange is by using China's swap centers. The first such center opened in Shenzhen in 1985, and was initially limited to domestic enterprises. By 1986 FIEs started to participate, though in some cities they could trade only among themselves. In 1988, the swap center system was expanded from Shanghai and the special economic zones to include all provinces and major cities. Moreover, the centers were unified, allowing domestic and foreign enterprises to swap with each other in the same center (*see The CBR*, September-October 1988, p.10). Currently there are over 90 swap centers throughout China under the supervision of the State Administration of Exchange Control (SAEC).

Typically, FIEs in need of foreign currency and Chinese companies with excess foreign exchange apply to swap their money at the centers. The swap is carefully regulated, because the government views foreign currency owned by Chinese trading companies and enterprises as ultimately belonging to the State. The transaction is usually conducted by exchanging checks or arranging remittances to and from bank accounts; cash does not actually change

Surveying the Foreign Exchange Climate

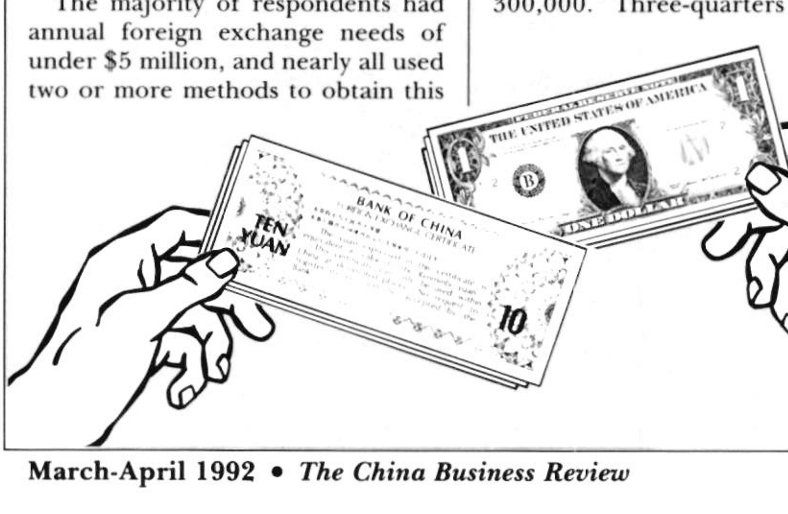
In the fall of 1991, the US-China Business Council conducted a survey of foreign-invested enterprises (FIEs) with manufacturing operations in China to gauge how they deal with the critical issue of balancing foreign exchange. Responses came from 31 (primarily American) FIEs, with average investment of $10-12 million and four years' operating experience. The survey results indicate that the environment for balancing foreign exchange has improved in the last few years, though some bureaucratic obstacles still remain.

The majority of respondents had annual foreign exchange needs of under $5 million, and nearly all used two or more methods to obtain this currency. The most common methods of balancing foreign exchange were to use a combination of swap centers (77 percent), exports (65 percent), and domestic sales in foreign exchange (48 percent). About a quarter of the respondents earn foreign exchange through official import substitution sales, and only one was balancing foreign exchange through multiple FIEs in China.

Of the FIEs using swap centers, most buy foreign currency on a monthly or quarterly basis, with the transaction size averaging $100,000-300,000. Three-quarters of these companies noted that their use of the centers is subject to restrictions, the most common being limitations on the use of foreign exchange that may be obtained at the centers. Half of the FIEs using swap centers have tried to trade currencies in other localities; about 50 percent of these succeeded in doing so. Opinions on access to and usage of the swap centers were similarly split, with nearly identical numbers reporting that conditions had improved, stayed the same, or deteriorated.

The majority of companies engaging in exporting reported that while their joint-venture contracts contained export targets, most were nonbinding. About a quarter of the respondents have been able to use *renminbi* generated from domestic sales to purchase Chinese goods for export, and most of these have been successful in purchasing the goods from outside their Chinese partner's bureaucracy. About half were successful in purchasing the goods from another province.

—John Frisbie, director, US-China Business Council China operations



Swap Centers: Past, Present, and Future

Since foreign exchange adjustment or "swap" centers were created in 1985, they have played an increasingly important role in the foreign-exchange balancing activities of foreign investors in China. As they are quasi market-driven, swap-market rates are a more realistic reflection of the value of China's currency than official exchange rates. They are thus strongly affected by China's domestic monetary policy, and have varied significantly over the years.

Narrowing the gap

Decentralization of China's trade regime in the mid-late 1980s significantly increased demand at the provincial and local levels for foreign exchange, keeping continuous upward pressure on China's few swap markets. By early 1989, the overheated economy pushed the average swap-market rate to a peak of ¥7.2/$1 (*see* graph), while the official exchange rate was only ¥3.7/$1.

Following the austerity program's clampdown on credit in mid-1989, however, the average swap-market exchange rate plummeted to around ¥5.5/$1, as Chinese enterprises sought to hold on to or buy *renminbi* to keep production going. The rate jumped back over ¥6/$1 in early 1990 when the Chinese government devalued the *renminbi*, but then dropped as the austerity program eased and the amount of foreign exchange available on the market increased with China's surging exports. By early 1992, the gap between the official and average swap market rate had narrowed to less than 10 percent, thanks to further devaluations of the *renminbi* and the steady supply of monies available at the centers.

Expanding volume

While the gap between the official and swap market rates has narrowed since 1985, total activity on the market—including FIE participation—has soared. The increase in volume both reflects and has contributed to the declining cost of foreign exchange on China's swap markets. Several other factors have also contributed to the increased activity.

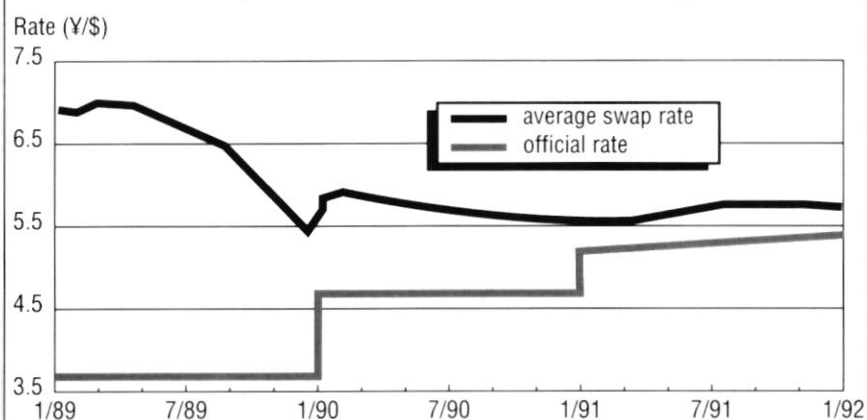
First, the number of swap markets in China has grown dramatically, rising from two in 1986 to nearly 100 currently. At the same time, the rapid growth in China's exports has provided an increasing amount of foreign exchange to swap, particularly since adjustments in foreign-exchange retention ratios for Chinese enterprises have left more foreign exchange in the hands of the localities. Retention rates were last modified in January 1991, leaving anywhere from 40 to 70 percent of foreign exchange earned from exports at the local level.

Foreign participation in the swap markets has grown both with the rise in the number of FIEs going into operation and with the rise in the number of swap centers open to them. Of particular significance in this respect was the 1988 merging of what had formerly been distinct swap centers for Chinese and foreign enterprises. The unified swap centers increased the amount of foreign currency available to FIEs using them, sparking FIE interest in the centers despite their formidable costs. The substantial leap in FIE swap-market activity over the last two years reflects the fairly low, stable cost of foreign exchange on the swap markets compared to the rates in 1988 and 1989.

China is likely to continue to devalue the *renminbi* in incremental steps this year, perhaps to ¥5.7/$1 by year's end. Even so, the swap-market rate will probably stay slightly higher, as there will always be someone willing to pay a premium for foreign exchange until the *renminbi* becomes freely convertible.

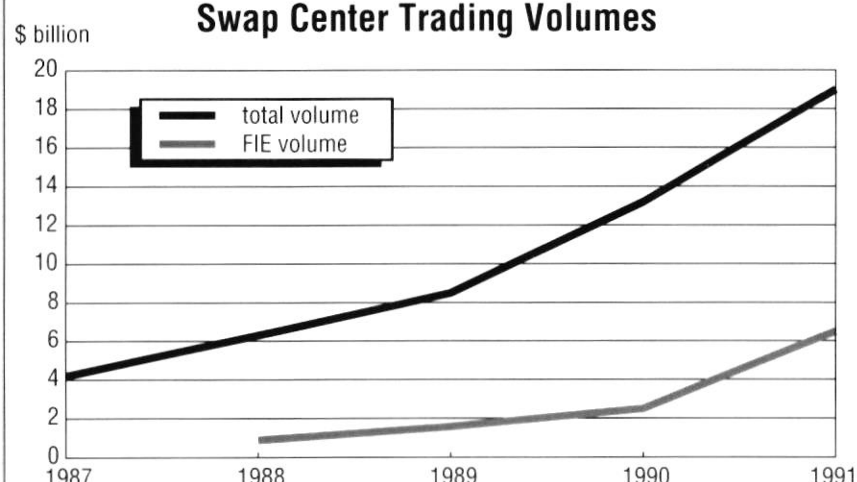
—Hutchison China Trade

China's Swap Market and Official Exchange Rates



Source: *Hutchison China Trade, International Monetary Fund*

Swap Center Trading Volumes



* estimate

Source: *US-China Business Council*

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'By staying at the Hotel New Otani Chang Fu Gong' Our Social Directors are there to help you get the most out of your stay. Whether it means calling our sister hotel in Los Angeles to secure ballgame tickets, or arranging a personalized sightseeing tour of Beijing. They, as with all our staff are ready to assist you by providing that little extra service that makes such a difference.

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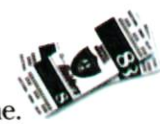

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Swaps are approved on a case-by-case basis, and applications are treated "in order of urgency." Only companies registered in China may swap; representative offices, traders, and most foreign financial institutions are prohibited from trading at the swap centers. Individuals are permitted to swap only under certain circumstances.

If the swap center in the city where an FIE is located does not have enough hard currency or *renminbi*, the FIE may apply to another city's center to swap currency. Legally, cross-border swapping is permitted, but approval of individual applications is up to local authorities, and regional protectionism is a problem. Authorities in the swap center in Shanghai, for example, may not be very receptive to applications from other areas, especially if their money supply is tight. In the cases where our company has been denied permission to swap in other provinces, we have been told that at the particular time we inquired the currency held by the center in question was available only to companies located in that city.

The local branches of the SAEC set policies for the swap centers under their jurisdiction. Different cities, therefore, often have different policies. In Guangzhou, for example, it is still permissible for joint ventures to prearrange exchanges with other parties before going to the swap center, but this is not the case in the centers in Shenzhen and Shanghai. In Shenzhen, all companies that wish to exchange currency at the center must go through a broker, which entails an additional fee; in Shanghai, large companies can swap on their own, but smaller companies must use brokers. These differences, however, are generally not significant enough that they should influence the location of a potential investment in China. Nevertheless, it is important to develop good relationships with local government and SAEC officials, in order to improve one's chances of getting approvals for various swapping arrangements.

Even though the Chinese government recognizes the necessity of having swap centers, it does not look favorably upon FIEs that drain large amounts of foreign exchange from these facilities, so caution is advised. Generally speaking, however, swapping is a very straightforward method that does not involve much additional cost, especially now that average swap rates are so close to the official exchange rate. Moreover, swapping requires a relatively short lead time (a matter of days or even hours), allowing an FIE great flexibility. Swapping is thus a very important method for solving short- to medium-term foreign exchange problems, and can be used as a back-up to other long-term strategies.

Exporting: the pros and cons

Though Chinese authorities have held varying attitudes toward swap centers over the years, their support of exporting has been unwavering. Few manufacturing FIEs aimed at China's domestic market, however, find exporting their own products a satisfactory method of generating significant quantities of foreign exchange. Many already have overseas subsidiaries that are more competi-

Photo courtesy of Procter & Gamble

China's swap centers have become increasingly popular with foreign investors over the past few years.

tive abroad, and exporting to one's affiliates does not usually yield a high profit. Although most FIEs try to export some of their output to help balance foreign exchange and meet contractual obligations, only those specifically using China as an export base rely on this as their primary method for earning hard currency.

FIEs with limited export markets for their own goods may wish to consider exporting Chinese products unrelated to their core business. Chinese law permits FIEs having temporary difficulties balancing foreign exchange to buy domestic products not under central control with their *renminbi* earnings and export them for foreign currency, provided they first obtain approval from the local foreign economic relations and trade commission (FERTC). Our company, for instance, exports chemicals to generate foreign exchange for our joint venture with Procter and Gamble (P&G). However, there are several problems related to this method that must be taken into account.

First, most of China's readily saleable goods are reserved for Chinese export corporations, which receive export licenses and quotas from the government to export certain products. Second, if a saleable good not subject to export controls can be located, the Chinese producer is unlikely to be willing to sell for *renminbi* if he thinks he can earn foreign exchange by exporting the good himself. Even if the Chinese producer is willing to sell his goods for *renminbi*, the FIE may have difficulty competing against State trading companies when selling abroad. These trading companies receive significant tax rebates—usually 8-20 percent of the domestic sales price—which enable them to sell the same products at lower prices than FIEs, which are not entitled to such benefits. As Simon To, managing director of Hutchison China Trade, explains, "When foreign joint ventures purchase products locally with *renminbi*, the price includes a number of taxes, such as value-added and sales taxes. These taxes may make exporting more expensive than swapping currency at a swap center. For example, we may purchase a product for ¥600 and sell it for $100, making the effective exchange rate ¥6/$1. We end up getting fewer dollars than we could have gotten at the swap center."

Import substitution status has not proven to be the foreign-exchange balancing panacea originally envisioned by some companies.

To counter this advantage, an FIE may seek to establish a relationship with a State trading company, whereby they export together and share some of the benefits that State companies usually enjoy exclusively. The advantage to the trading company is that it gets extra business—and foreign exchange—with comparatively little effort, since the product and overseas buyer are located by the FIE. The FIE, in turn, is able to export competitively and obtain a cost/revenue margin comparable to the swap center rate. Through such arrangements our company has been able to reduce prices on export goods by more than 10 percent; as a result, we ended up with a better ¥/$ ratio than was obtainable at the swap centers.

The final problem with exporting Chinese goods is that most foreign companies lack expertise in products and markets outside their core business. Such a situation exacerbates the risks commonly associated with importing from China, such as problems with quality and delivery. Moreover, crossing ministerial or jurisdictional boundaries can be problematic, as ministries and provinces tend to be highly protective of their bailiwicks. Foreign companies considering this option, therefore, may wish to ally themselves with a partner with diversified trading experience. If the obstacles can be overcome, exporting Chinese products can provide an FIE with good returns and a relatively consistent supply of foreign exchange.

Selling domestically for hard currency

Some foreign companies that lack the ability or desire to export may be able to get permission to sell their goods within China for foreign exchange. There are two ways to obtain this approval: by being awarded import substitution status, or by applying directly to the SAEC for permission to sell through certain outlets. Though several multinational companies, such as Coca-Cola and Continental Can, have been successful with the latter method, the market tends to be somewhat limited. Selling goods for foreign exchange to local trading companies who then sell the products for *renminbi* is an option, though most wholesalers and department stores prefer to deal directly with FIEs. Moreover, local trading companies are subject to sales taxes, which add to their costs and thus reduce the price they are willing to pay for FIE products.

Import substitution status, while used successfully by firms like Xerox and Foxboro, has not proven to be the foreign exchange balancing panacea envisioned by some companies when the policy was articulated in 1987. The idea behind the import substitution policy is that if an FIE makes a product that can replace one being imported under the State plan, the FIE may be entitled to receive some foreign exchange for its domestic sales (*see The CBR*, March-April 1988, p.24). In practice, the policy has been implemented inconsistently and has therefore been of limited use to most foreign companies.

FIEs seeking import substitution status must receive approval from the local branches of the State Planning Commission and FERTCs. The status is generally difficult to obtain, and must be re-approved on a regular basis. To qualify, a company's output must not be readily available from domestic sources, must be urgently needed by China, and/or must be made with technology superior to that available domestically. Generally, only high-technology products are approved. Products that do not qualify for import substitution status, however, may still be given "advanced technology status," which allows certain tax and land lease benefits. Alex Yu, deputy general manager of P&G's Guangzhou joint venture, notes "People have a fancy dream about this import substitution status. But a company can still get authorization to sell locally for foreign currency, even without such status."

Companies hoping to acquire import substitution status should seek to have this status written into their joint-venture contracts. The ability of potential endusers to pay in foreign exchange should also be verified before such status is sought. After import substitution status is attained, companies should be aware that they are very much subject to government requirements, as well as to customer whims; often Chinese companies prefer to import products from abroad rather than buy them locally, because importing may involve travel and additional perquisites. Import substitution should thus always be used in conjunction with other foreign exchange balancing strategies.

Making additional investments

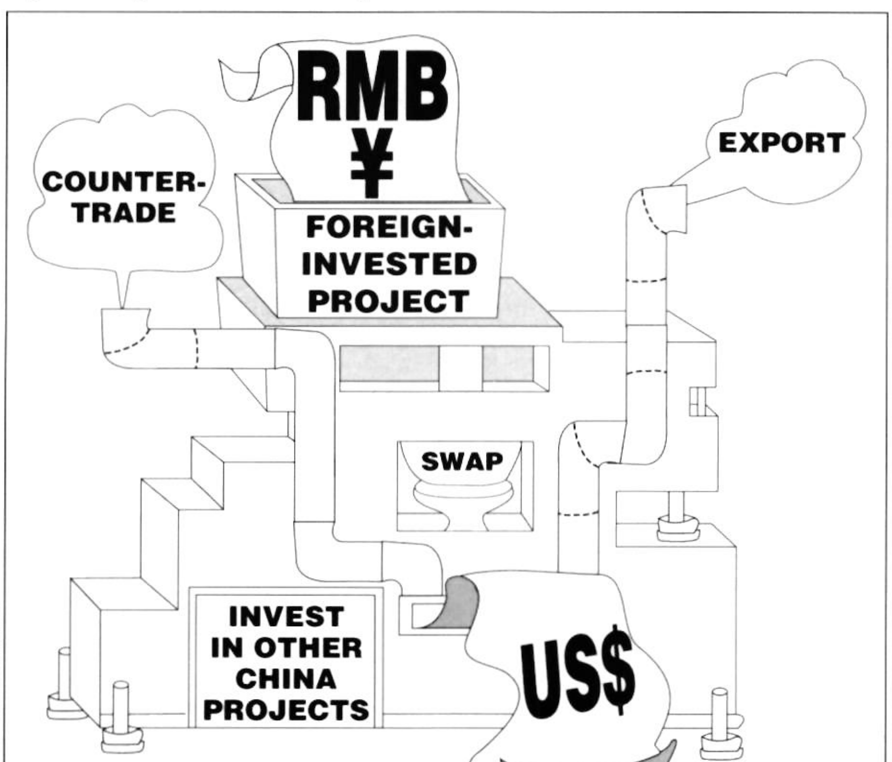
Companies seeking truly long-term strategies for balancing foreign exchange in China may wish to consider expanding into other investment projects. Though this strategy is complex and requires additional outlay of funds initially, it can provide a long-term solution to the foreign-exchange balancing issue, as well as new profit centers.

There are two basic methods for balancing foreign exchange through additional investment. In the first, an FIE reinvests its *renminbi* profits in a separate export-oriented enterprise.

Balancing between multiple projects can provide a long-term solution to the foreign-exchange balancing issue, as well as new profit centers.

The return from this investment would be in foreign exchange earnings, which could either be swapped with the parent FIE or remitted abroad in their entirety, provided both FIEs maintain favorable foreign exchange balances. Moreover, in accordance with the Joint Venture Law, companies reinvesting *renminbi* profits receive a 40 percent tax rebate on these monies.

On the negative side, this is not a method in which profits can be repatriated quickly. It can also be extremely difficult to find a partner whose product is of high enough quality to be internationally marketable and who is willing to share hard currency earnings in return for an investment in *renminbi*. In addition, setting up production facilities in an area unrelated to one's core business can be risky.



Artwork courtesy of HCT

Nevertheless, if the exporting enterprise is set up skillfully, it can generate a sizeable and fairly reliable store of foreign currency on a more-or-less permanent basis. Of course, as an FIE's domestic sales increase, it must ensure that the profits it earns from such export-oriented projects increase as well. Our company, for example, has invested in a towel-making joint venture to help balance foreign exchange for the P&G project. Towels were selected because those made in China can be highly competitive in world markets; labor costs are low, and the main raw material used in their production—cotton—can be sourced locally. In order to increase production volume to keep pace with the P&G venture, the towel enterprise is able to subcontract orders to other Chinese factories.

The other investment-related strategy also involves setting up a second FIE, but in this case, the equity contributed is in foreign exchange. As in the first strategy, the common shareholder in the projects may swap foreign exchange between them. In these cases, swaps can be prearranged, and obtaining approval for cross-border swaps is much easier. However, the transaction must usually still go through the swap center, even though it is arranged privately.

Technically, a company with multiple investments is limited to swapping foreign exchange from one FIE in an amount equivalent to the percentage of equity it owns in the other. Take, for example, a company which owns both a 25 percent stake in a food products joint venture that sells locally and a 50 percent stake in a factory which exports shoes. If the food joint venture has an excess of ¥100 million, that company has the right to swap only ¥25 million worth of foreign exchange—with the consent of the other shareholders.

Though few foreign companies targeting the Chinese market currently have multiple investments among which to balance foreign exchange, this method has some strong points. Specifically, it gives foreign companies more control over their foreign exchange reserves than they would have if they relied on swap centers or various other balancing methods requiring government approval. On the down side, this method requires a significant outlay of capital and a good deal of time before the various projects involved are foreign-exchange profitable and able to swap among each other.

Using local agents

In addition to thinking of creative ways to generate hard currency, FIEs should also consider methods for reducing foreign exchange expenditures. Decreasing imports by increasing the percentage of locally sourced inputs is one way to conserve hard currency, though in the short run it may actually end up costing more since most Chinese suppliers typically need an infusion of cash or technology to bring their products up to par. Another relatively new, untested method of conserving foreign exchange is to appoint a local agent to import raw materials on an FIE's behalf. The FIE pays the agent—normally an import/export company—in *renminbi* for the materials, including a handling charge of about 2-3 percent. This method presupposes that the FIE can locate an agent with an excess of foreign exchange who will accept *renminbi* in order to meet his foreign exchange spending quota.

Such an arrangement is usually more costly than importing on one's own or using the swap center, because a commission must be paid to the agent, in addition to any value-added taxes incurred upon entry of the goods to China. However, the FIE can conserve foreign exchange and enjoy the convenience of having the agent do all the work. Another advantage of this method is that it does not require government approval, because the goods are purchased with *renminbi* for use within China. As a comparatively recent phenomenon, however, this type of transaction could be vulnerable to changes in government policy.

Putting things in perspective

Although China modifies its joint venture and foreign exchange laws from time to time, the basic framework for balancing foreign exchange is not likely to change in the near future—at least, not until China makes the move to make the *renminbi* freely convertible on world markets. Though Beijing intends to do this eventually, full convertibility is not expected for some time, as China's developing economy is not yet sophisticated enough to cope with international currency fluctuations.

In the meantime, there are several factors which may prove critical to the success of an FIE's foreign-exchange balancing activities. These include support from top management—many companies underestimate the amount of time and resources they may have to devote to generate foreign exchange; accurate and timely information on the Chinese market; and marketing capabilities in export markets. And perhaps most important, strategies for generating foreign exchange require the same long-term view necessary for the success of any investment in China. 完

Closing Up Shop in China

Shanghai's regulations on the dissolution of foreign-invested enterprises could become the national norm

Norman P. Givant

During the last three years Shanghai has been used by China's central government authorities as a testing ground for a number of new regulations affecting foreign-invested enterprises (FIEs). Keeping with this role, central authorities worked with the Standing Committee of the 9th Municipal People's Congress of Shanghai on the "Regulations of Shanghai Municipality on the Liquidation of Foreign Investment Enterprises" (the Regulations). Adopted in August 1991, the Regulations—pending successful implementation in Shanghai—could become a model for national legislation regarding the FIE dissolution process.

The Regulations provide for two distinct forms of liquidation. "General liquidation" rules apply in cases where an enterprise has sufficient assets to satisfy its liabilities and a board of directors or management organization capable of organizing liquidation formalities. In cases where these attributes are lacking, "special liquidation" measures are to be used.

Until passage of the Regulations, there had been few formal rules to guide the dissolution process (*see The CBR*, November-December 1990, p. 42). The new rules cover liquidation of enterprises under three circumstances: when an enterprise's term of operation expires; when, with the approval of the original contract approval authority, an enterprise's contract and articles of association are terminated prior to their expiration date; or, when the approval authority rescinds its approval of the enterprise's contract and articles of association. The Regulations, however, do not apply to foreign-invested financial institutions, which remain under the authority of the People's Bank of China.

General liquidation procedures

The Regulations stipulate that on commencement of liquidation, an enterprise must cease production and other business activities. Its board of directors must then appoint a liquidation committee of at least three members, one of whom is selected by the committee to serve as its head. If members of the board are unable or "unsuitable" (a term not defined) to be members of this committee, the board may select Chinese-registered accountants or lawyers to serve in their stead.

The Regulations appear to recognize the need to expedite procedural formalities.

Restricting such professionals to those registered in China contravenes many joint-venture contracts, which allow foreign accountants and lawyers to serve on the liquidation committee. Foreign investors may have reason to be concerned if the new Regulations are interpreted narrowly in order to restrict them from appointing professionals of their choice to their liquidation committees.

More welcome news perhaps is that the Regulations appear to recognize the need to expedite procedural formalities. The board is required to submit the names of the members of the liquidation committee to the enterprise's department in charge or approval authority within seven days of the commencement of liquidation. The department in charge or the approval authority must then respond in writing within seven days from the date of such submission, failing which the names will be deemed to have been approved.

Once established, the liquidation committee has full authority to represent the FIE in the handling of litigation. It is charged with assessing the debts and assets of the enterprise, preparing and implementing a liquidation plan, discharging the debts of the enterprise, and distributing the remaining assets of the enterprise to the investors. With the approval of the board, the committee may set up working sub-committees to handle various aspects of the liquidation work. The Regulations, however, limit those eligible for appointment to the working groups to current employees of the enterprise and lawyers and accountants registered in China. Again, if strictly enforced, such restrictions may prejudice the interests of foreign investors.

Settling claims

Within 20 days of its establishment the liquidation committee must send written notices to known creditors of the enterprise requesting the submission of claims, and within 60 days of its establishment it must publish at

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least twice in one of four prescribed newspapers a notice specifying the name and domicile of the enterprise in liquidation, the reasons for liquidation, the date liquidation commenced, and the time limit within which creditors must submit claims. The first of these notices must be published within 10 days of the establishment of the liquidation committee.

Creditors of the enterprise must file their claims and any supporting documents with the liquidation committee within 30 days of receiving written notice from the committee; creditors who do not receive such notice must file within 90 days of the first newspaper announcement. Creditors who fail to submit their claims within the prescribed time limit will be deemed to have waived their claims to repayment, though provisions are made for creditors who are "truly unable" to file claims within the statutory time limit. The Regulations are ambiguous on the requirements in such cases, stating only that the tardy creditor may file a request for debt repayment prior to the distribution of the enterprise's remaining assets.

The liquidation committee is responsible for verifying the claims of creditors and notifying them whether their claims will be allowed either in whole, in part, or disallowed altogether. A creditor who disputes the contents of a verification notice has 15 days from the date of receipt of such notice to initiate proceedings challenging the liquidation committee's determination. While such legal challenges are pending, the litigation committee must suspend activities involving the distribution of assets.

Evaluating assets

While the committee is collecting creditors' claims, it must also evaluate the enterprise's assets according to the principles specified in the venture's contract and articles of association. In the absence of relevant provisions in these documents, the investors may agree on the principles to be applied, but any such agreement is subject to the approval of the initial approval authority. If the parties cannot agree, the Regulations specify that the relevant provisions of the State will apply, but no further clarification is given on which provisions apply. The tendency of

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Chinese negotiators is to push for evaluation of assets on a net book-value basis, which may result in the assessment of a very low value for a joint venture that has been in operation for many years. It is thus prudent for foreign investors to make sure that their investment contracts contain a more equitable standard for evaluation, such as current market value at the time of liquidation.

When the time comes to liquidate the enterprise's non-cash assets, the investors have the right of first refusal. If all the investing parties waive their rights to purchase the assets, the liquidation committee, with the approval of the enterprise's board of directors, may dispose of the assets by soliciting bids or by auction. After selling the assets and settling the debts of the enterprise, the liquidation committee is charged with distributing the remaining assets to the investing parties according to their respective contributions to the registered capital of the enterprise, unless the contract and articles of association provide otherwise. If the net assets of the enterprise (after the deduction of liquidation expenses and contributions to statutory funds such as the workers' welfare and benefit fund) exceed the enterprise's paid-in capital, the difference will be treated as liquidation income subject to income tax.

The Regulations specify that the entire process should take no more than 180 days, though extensions can be granted with the approval of the board of directors and approval authority. Normally, however, the 180-day liquidation period is to conclude when the liquidation committee's board-approved completion report is submitted to the department in charge and the approval authority.

Within 10 days of submitting the completion report, the liquidation committee must handle the formalities for the cancellation of the enterprise's tax and customs registrations. Once this is done, the liquidation committee has 10 days to cancel the business registration of the enterprise by submitting the liquidation completion report, the discharge certifications issued by the tax and customs authorities, and the original business license of the enterprise to the local administration for industry and commerce, which will then publish an announcement of the dissolution of the enterprise in the local newspapers.

Appeals against decisions of the board regarding the liquidation are allowed if creditors of the enterprise, members of the board, or members of the liquidation committee feel that a decision is manifestly wrong. In such cases, parties may, within seven days of the rendering of a decision by the board, file a written opinion with the enterprise's department in charge or approval authority requesting an examination of the decision. The examining authority must give a written response with seven days of receiving the written opinion. Given their experience with local bureaucrats in the past, foreign investors in Shanghai will be quite curious to see how quickly, smoothly, and equitably this appeals mechanism works, and how helpful and even-handed the approval authority will be in overseeing all aspects of the liquidation process.

Special liquidation

If an enterprise has insufficient assets to satisfy its liabilities or is incapable of organizing liquidation procedures on its own, the approval authority, at its own discretion or at the request of the enterprise or its creditors, may subject the enterprise to special liquidation procedures. The regulations also provide for a general liquidation procedure to be transformed into a special liquidation if serious obstacles are encountered and the liquidation committee or the creditors petition the approval authority to allow the change. To protect the remaining assets of the enterprise and its investors, tighter control is maintained over special liquidation procedures.

Special liquidation procedures are similar to administrative bankruptcy procedures. A liquidation committee made up of representatives from the investors and relevant Chinese authorities must be appointed; the committee may—but need not—include members of the enterprise's board of directors. In a special liquidation, the liquidation committee itself exercises the functions of the board of directors, and reports directly to the approval authority. The head of the liquidation committee is appointed by the approval authority and is authorized to function as the enterprise's legal representative during liquidation. Board members—whether asked to serve on the liquidation committee or not—are enjoined to assist the liquidation committee with its work, and the committee is empowered to convene and chair meetings of the enterprise's board and creditors.

In cases of special liquidation, where an enterprise's assets generally are insufficient to discharge its debts, all creditors may join a creditors' committee. Except for those creditors with debts secured against the assets of the enterprise and who refuse to relinquish their prior rights of repayment with respect to such assets, all members of the creditors' committee may vote at its meetings. This committee is tasked with verifying the debts of the enterprise, conveying the views of the creditors to the liquidation committee, and examining and approving the plan for the distribution of assets. The chairman of the creditors' committee is chosen by the approval authority from among the voting members of the committee, and granted the right to attend meetings of the liquidation committee as a non-voting member.

Meetings of the creditors' committee may be convened whenever its chairman—or the chairman of the liquidation committee—deems necessary, or when such a meeting is requested by creditors representing one-fourth of the total unsecured claims against the enterprise. Resolutions of the committee require a majority vote of the creditors representing more than 50 percent of the unsecured obligations of the enterprise, and resolutions so adopted are binding on all creditors of the enterprise. However, when the assets of an enterprise are insufficient to discharge its debts, creditors dissatisfied with the distribution plan approved by the creditors' committee can take their grievances to the People's Court.

Prioritizing claims

Under the Regulations, claims of secured creditors—whereby assets were pledged to secure the obligation under a specific debt—have priority against the assets securing their claims. If the proceeds of the enterprise's assets are insufficient to discharge the secured claim in full, the undischarged portion of the claim becomes an unsecured claim against the remaining assets of the enterprise. Any excess of collateral is added to the pot of assets available to meet the claims of unsecured creditors.

To protect these creditors against unethical transfers of assets by the debtor enterprise just prior to its liquidation, the Regulations invalidate the concealment, unauthorized distribution, or transfer of assets without adequate compensation if any of these actions occur in the six months prior to the commencement of special liquidation procedures for an enterprise whose assets are insufficient to discharge its debts. The granting of security interest to secure loans which were originally unsecured, the payment of unmatured debts, and the relinquishment of claims by the enterprise to monies owed it are also considered invalid.

The Regulations set forth a system of priorities for settling unsecured liabilities. Liquidation costs and the remuneration payable to members of the liquidation committee and liquidation working groups for their services have priority for payment out of the enterprise's existing assets. Given China's ideological commitment to the welfare of its workers and its desire to dampen possible social unrest, it is not surprising to find that workers' wages, labor insurance premiums, and worker discharge and resettlement payments come next. Taxes are third on the list, and all other unsecured liabilities have last priority.

As in general liquidation cases, on completion of a special liquidation, the liquidation committee must file a liquidation completion report with the approval authority. The committee must also cancel the tax, customs, and business registrations of the enterprise.

The Regulations reiterate the principles of enterprise liability set forth in the 1979 Joint Venture Law and in the 1988 Cooperative Joint Venture Law: enterprises which are considered Chinese legal persons are liable to their creditors to the full extent of the enterprise's assets. If the enterprise is a cooperative joint venture with legal person status, the investors will be liable to the creditors of the enterprise to the extent of the capital contributions repaid to them during the term of their cooperation. For cooperative joint ventures without legal-person status, the investors jointly bear full liability for the debts of the enterprise.

In cases where an enterprise's assets are insufficient even to pay liquidation costs and remuneration to members of the liquidation committee, the committee—with the approval authority's permission—can terminate liquidation procedures. Although the Regulations provide few specifics, under such circumstances the liquidation committee, with the assistance of the approval authority, presumably must still cancel the tax, customs, and business registrations of the enterprise with the relevant authorities. Following these procedures, the enterprise is effectively dissolved.

New movement on bankruptcy?

An interesting feature of the Regulations is that they intimate that China may once again be ready to deal with the sensitive issue of enterprise bankruptcy. Article 4 of the Regulations provides that when an enterprise with the status of a legal person cannot discharge its liabilities because of serious losses, the enterprise or its creditors may apply to the People's Court to have the debt-ridden enterprise declared bankrupt. As China does not yet have a general bankruptcy law—the current bankruptcy law applies only to State-owned enterprises and has been virtually ignored for the last three years—the references to bankruptcy in the Regulations suggest that new rules governing voluntary and involuntary bankruptcy proceedings for FIEs and their creditors may soon be promulgated.

Article 45 also refers to bankruptcy. It provides that in special liquidation situations where the assets of an enterprise are insufficient to discharge its debts, creditors who oppose the distribution plan approved by the creditors' committee have 15 days to file a petition with the People's Court requesting the court to declare the enterprise bankrupt. If the court accepts the creditors' application, the special liquidation procedures will be suspended and, if the court adjudicates the debtor to be bankrupt and orders it to enter bankruptcy procedures, the special liquidation procedures are terminated. In such cases, the disposition of the enterprise's debts and assets will be subject to the determination and supervision of the court.

Reaching beyond Shanghai

The Regulations provide a well thought-out, systematic approach for the liquidation of FIEs in Shanghai. While some of the provisions, such as those dealing with appointments to the liquidation committee, smack of chauvinistic protectionism, it is hoped that the authorities will prove more liberal in their interpretation of the rules when it actually comes time to apply them.

Whether or not the Regulations will translate into legal guidelines for FIEs elsewhere in China will depend on their successful implementation. The potential for conflicts and for the work of the liquidation committee to become bogged down in squabbles among the parties is high, given the fact that the work of the committee can be second-guessed at every major stage by the board of the enterprise or by the approval authority. Moreover, if the parties disagree on the handling of the liquidation (which will likely be the case), the possibility of back-door maneuvering and administrative interference in all major aspects of the liquidation process is great. A license for such interference is expressly granted in Article 19, which gives the approval authority the right to have its officers participate in liquidation meetings or adopt other necessary measures to supervise liquidation procedures.

Regardless of the manner in which they are implemented, however, the Regulations still fail to address some important threshold issues. For instance, how will the approval authority deal with money-losing ventures or ventures beset by irreconcilable conflicts among the investors if the Chinese side refuses to agree to a dissolution requested by the foreign investor? Will the approval authority allow foreign investors to unilaterally apply for the dissolution of their ventures under such circumstances? The Regulations will not be of much use to foreign investors if the issue of easy termination of unsuccessful ventures is not satisfactorily addressed.

Though no FIE has yet filed for dissolution under the new Regulations, foreign investors in Shanghai and elsewhere in China will be watching for the first case. Those with existing enterprises will be particularly anxious to see how the Regulations are implemented in the coming months. 完

Hong Kong's Trade Show Industry

Business is good, but competition is growing fiercer

Simon Cooper

Despite its long history of busy international dealings, Hong Kong is a relative latecomer to the exhibition and trade fair industry. Until 1980, Hong Kong hosted only the occasional trade event, and served more as a transit point for local and foreign businesspeople headed across the Chinese border to the semi-annual Canton Trade Fair. Over the past decade, however, Hong Kong has come into its own as a leading site within the region for sophisticated and well-attended exhibitions and trade fairs.

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The advantages to locating trade gatherings in Hong Kong are many; its convenient location, highly developed infrastructure, and strong business climate make it a good venue for international trade events. An estimated 50 percent of the world's population is within five hours' flying time of the territory, for example, and Hong Kong has long been a focus point for business travelers within the region, as well as for multinationals seeking a foothold in Asia. The Hong Kong government has high hopes of making the territory the world's choice locale for trade shows and exhibitions, and actively promotes Hong Kong's trade show industry through the Hong Kong Trade Development Council (HKTDC) and the Hong Kong Tourist Association (HKTA).

Photo courtesy of Simon Cooper

Foreign exhibitors are becoming increasingly visible at Hong Kong trade shows.

Expanding facilities . . .

Until recently, Hong Kong had difficulty competing with other Asian cities for trade show business because it lacked adequate exhibition facilities. In the early 1980s, for instance, trade fairs were staged in such unlikely locations as the rooftop of the Ocean Terminal passenger-ship pier. The opening in 1983 of a small exhibition center as part of the China Resources building complex was a major step toward the development of full-scale international trade fairs, but larger exhibits could not be accommodated in the restricted space.

Seeing the need for larger facilities, the Hong Kong government in 1985 granted land expressly for this purpose to the Trade Development Council. In 1988 the new Hong Kong Convention and Exhibition Centre (HKCEC) was inaugurated, enabling the territory to compete more effectively with other popular cities for trade show business. Lo-

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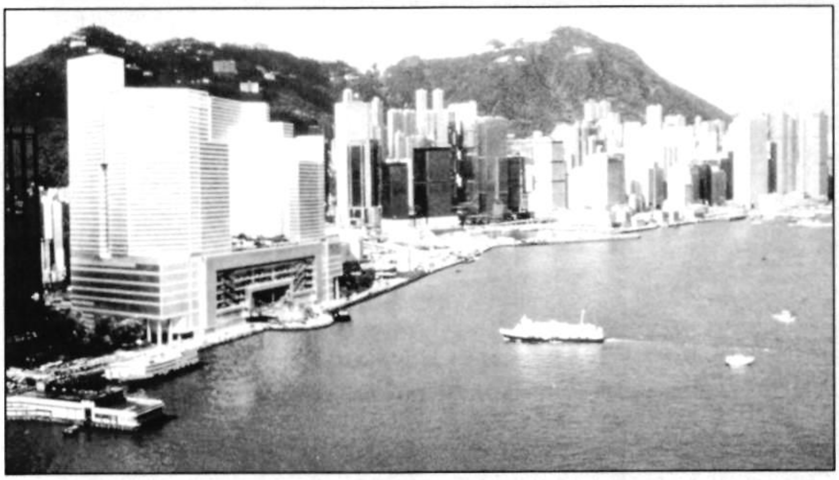

1992 Hong Kong Trade Shows and Exhibitions

Exhibition	Venue	Date
Clothing Industry Fair '92	Hong Kong Convention & Exhibition Centre	March 9-12
Hong Kong International Jewelry Show '92	Hong Kong Convention & Exhibition Centre	March 17-20
Hong Kong Linkage Industry International Machine Tool Exhibition '92	Hong Kong Convention & Exhibition Centre	March 26-29
COMMTEL ASIA '92 (Telecommunications equipment, networks, and services exhibition)	Hong Kong Convention & Exhibition Centre	March 31-April 3
Electrical Home Appliances Expo '92	Hong Kong Convention & Exhibition Centre	April 2-5
Ideal Home Expo '92	Hong Kong Convention & Exhibition Centre	April 2-5
Hong Kong Gifts & Housewares Fair '92	Hong Kong Convention & Exhibition Centre	April 13-16
Hong Kong Premium Show '92	Hong Kong Convention & Exhibition Centre	April 13-16
INTERFIT '92 (International fitness & health care exhibition)	Hong Kong Convention & Exhibition Centre	April 17-20
Hong Kong International Leather Exhibition	Hong Kong Convention & Exhibition Centre	April 27-30
ELENEX '92 (Electrical & electronic engineering show)	Hong Kong Convention & Exhibition Centre	May 6-9
LUMINEX '92 (Lighting, lighting technology, fitting, & systems show)	Hong Kong Convention & Exhibition Centre	May 6-9
AIRVEX '92 (Air conditioning, ventilation, heating, & refrigeration show	Hong Kong Convention & Exhibition Centre	May 6-9
SECURITEX '92	Hong Kong Convention & Exhibition Centre	May 6-9
Asia-Pacific Duty-Free Conference & Exhibition	Hong Kong Convention & Exhibition Centre	May 12-15
Auto-Id Hong Kong '92 (International automatic identification & bar code technology and equipment exhibition	Hong Kong Convention & Exhibition Centre	May 12-15
COMPUTER '92	Hong Kong Convention & Exhibition Centre	May 12-15
EIE '92 (International electronics industry, testing equipment, & instrument exhibition)	Hong Kong Convention & Exhibition Centre	May 22-26

PACK & PRINT ASIA '92 (International packaging & printing machinery & materials exhibition)	Hong Kong Exhibition Centre	May 22-26
Plastics Asia '92	Hong Kong Convention & Exhibition Centre	May 22-26
ECA '92 (Electronic component exhibition)	Hong Kong Convention & Exhibition Centre	May 22-26
MEX '92 (Machinery & materials exhibition)	Hong Kong Convention & Exhibition Centre	May 22-26
SMT '92 (Surface-mount technology exhibition)	Hong Kong Convention Exhibition Centre	May 22-26
World Jewelry & Watch Fair '92	The Regent Hotel	May 28-31
World Gems, Jewelry, and Watch Fair	Hong Kong Convention & Exhibition Centre	May 31-June 3
INTERTOUR '92 (International travel industry exposition)	Hong Kong Convention & Exhibition Centre	June 3-5
Airport Construction & Development Exhibition	Hong Kong Convention & Exhibition Centre	June 11-13
Conequip Expo Hong Kong '92	Hong Kong Convention & Exhibition Centre	June 11-13
Hong Kong Machinery & Electrical Exhibition	Hong Kong Convention & Exhibition Centre	June 11-13
International Building Exhibition '92	Hong Kong Convention & Exhibition Centre	June 11-13
Cosmetics, Hair, & Beauty '92	Hong Kong Convention & Exhibition Centre	June 14-17
Inter-Apparel '92 (International apparel fair)	Hong Kong Convention & Exhibition Centre	July 3-6
Stationery & Premium '92	Hong Kong Convention & Exhibition Centre	July 3-6
Fashion Accessories '92	Hong Kong Convention & Exhibition Centre	July 3-6
Sporting Goods '92	Hong Kong Convention & Exhibition Centre	July 3-6
GARMENTEC '92 (Garment machinery, materials, and accessories exhibition)	Hong Kong Convention & Exhibition Centre	July 8-11
Textile Machine Expo '92	Hong Kong Convention Centre	July 8-11
Hong Kong Book Fair '92	Hong Kong Convention & Exhibition Centre	July 23-27
Food Expo	Hong Kong Convention & Exhibition Centre	Aug 12-16
Hong Kong Watch & Clock Fair '92	Hong Kong Convention & Exhibition Centre	September 7-11
Hong Kong International Jewelry Show '92	Shangri-La Hotel	September 18-22
J Week '92 (Hong Kong jewelry & watch fair)	Hong Kong Convention & Exhibition Centre	September 19-23
Asian Toy Show '92	Hong Kong Exhibition Centre	October 7-9
Hong Kong Electronics Fair '92	Hong Kong Convention & Exhibition Centre	October 14-17
Hong Kong Industrial Trade Fair	Hong Kong Convention & Exhibition Centre	November 19-22
Exposhīp Far East '92	Hong Kong Convention & Exhibition Centre	December 1-4
Hong Kong Showcase	Hong Kong Convention & Exhibition Centre	December 16-20

cated on the Wanchai waterfront in close proximity to many international hotels and the Central business district, HKCEC has a total exhibition area of 194,000 sq ft and can accommodate several trade events at the same time, as different configurations can be made with sound-proof walls.

The convention hall and two theaters are equipped with state-of-the-art audio and visual equipment, a simultaneous interpretation system for up to eight languages, teleconference facilities, and sophisticated security and fire-safety systems. Trade exhibitors generally pay registration fees averaging $490 (HK$3,800), booth rental charges averaging $3,590 (HK$28,000), and about $718 (HK$5,600) in exposition service contract fees—somewhat higher than the rates generally charged elsewhere in the region, but slightly lower than the average rates in China. HKCEC is run as a private enterprise; the Centre's earnings are retained by the New World Group, which has responsibility for managing HKCEC, though 5 percent of the profits go to HKTDC.

... and attendance

The new facilities have boosted the number of trade shows held each year in Hong Kong. Statistics from HKTA show that there were 195 trade-related conferences and 77 exhibitions held in Hong Kong in 1990. HKTDC, Hong Kong's largest trade show organizer, oversees about a third of these events, while other events are organized by a handful of private firms. The number of organizers has grown with the number of events in recent years, though the high rental costs are now discouraging new organizers from entering the market.

Over 111,000 overseas participants attended trade events in Hong Kong in 1990, up about 5 percent over 1989 levels. Figures for 1991, when released, are expected to show that around 300 events were held last year, and that the number of attendees from overseas continued to rise. Visitors from Japan, Taiwan, the United States, China, Australia, and the United Kingdom—in that order—accounted for the bulk of the attendees.

A small percentage of the rise in trade show attendance last year may

Participating in a Hong Kong trade event may be cheaper than exhibiting in China in terms of travel and exhibition costs, and easier in terms of obtaining the necessary visas and customs approvals.

be attributable to easier entry procedures for visitors from Taiwan (Hong Kong's second largest market) and Eastern Europe. This was a particularly important development for the territory's larger trade fairs, which had been hampered in the past by the inflexible and lengthy immigration procedures for certain national groups. Prior to the relaxed entry procedures, for example, visitors from Taiwan and Eastern Europe were discouraged by the long period of time needed to apply for entry permits and the need to find a Hong Kong sponsor.

Access to Chinese buyers

Exhibitors at HKCEC events, in general, seem pleased by the new exhibition facilities. Though few statistics are available on the nationalities of the exhibitors, in recent years it appears that more European and US companies are displaying their goods at Hong Kong trade events.

For many of the exhibitors, Hong Kong's location remains a strong draw. Not only is the territory easily accessible to many potential purchasers, it also serves as a gateway to China. Over 400 Chinese organizations responsible for foreign purchases have business offices in Hong Kong and senior Chinese officials readily travel to trade events in the territory. For some foreign exhibitors, participating in a Hong Kong trade event may be cheaper than exhibiting in China in terms of travel and exhibition costs, and easier in terms of obtaining the necessary visas and customs approvals. Moreover, foreign exhibitors disenchanted with the large number of non-buying attendees at trade shows in China seem confident that they can attract the attention of the appropriate Chinese officials at Hong Kong trade events.

Constraints to growth

Despite these positive trends and the popularity of the new exhibition center, Hong Kong's trade show industry may not be able to maintain its current rate of growth. The exhibition center reached maximum capacity only a year after coming into use. During peak periods last spring and fall, HKCEC often booked two shows simultaneously, making it difficult for either to accommodate additional exhibitors. Some of the large trade shows, in fact, had already outgrown the space by 1990. The Hong Kong International Leather Fair, for instance, had to expand across the road into the China Resources Exhibition Centre to accommodate all companies wishing to exhibit at its 1991 show.

Other concerns about the existing space are being voiced by the Hong Kong Exhibition Organisers Association (HKEOA), a group formed in 1989 to enhance Hong Kong's image as Asia's exhibition and convention capital and to promote the highest standards of professionalism in the local exhibition industry. The association, representing almost 90 percent of the exhibition organizers, contractors, designers, freight forwarders, hotels, and others directly involved in the exhibition industry, has fought against HKCEC's high rental rates. Cheaper exhibition space is available elsewhere in the region, such as in the Singapore World Trade Centre, and HKEOA members fear Hong Kong will price itself out of the market. HKEOA complaints over the high rental rates have been lodged with the HKTA, HKCEC management group, and the government.

Criticism has also been levied against HKTDC as the owner of the HKCEC facilities and the territory's leading trade show organizer. Though HKTDC has organized Hong Kong manufacturers' trade exhibits at fairs all over the world, the council has rapidly expanded its Hong Kong-based activities and now organizes the biggest share of Hong Kong's trade fairs. Other trade show organizers would like to play a bigger part in the exhibition trade. Though technically anyone can organize a trade show in Hong Kong, HKCEC maintains some control over who uses its facilities. Moreover, HKCEC's management appears reluctant to approve applications for new trade events unless it is sure of the event's long-term potential for success.

Seeking progress on the space issue, in 1991 the Trade Development Council proposed to the Hong Kong government that the HKCEC facilities be doubled to cope with the growing demand for exhibition space. HKTDC suggested that an extension be added to the front of the existing building, using land reclaimed under the new Wanchai reclamation project. Like the initial HKCEC construction, the extension would be financed by private investors. A decision is still pending on the extension, which would incorporate all HKCEC facilities under one roof, including conference and exhibition facilities, offices, and shopping areas.

Even if the government agrees to the expansion, its support will be limited to the provision of land for the HKCEC facilities. Though it also promotes the territory through funding for HKTA, the Hong Kong government does not subsidize HKCEC operations as the governments of Malaysia, South Korea, and Taiwan fund their facilities. Hong Kong's trade show industry thus has a hard time matching the lower costs and modern facilities of some of its competition. While the industry may not be suffering yet, in the future the Hong Kong government's support—or lack thereof—could become increasingly critical.

Most important will be the government's decision on whether to expand HKCEC's facilities, as extra space is crucial to maintain growth in the territory's convention and exhibition industry, which has a large impact on the hotel and other tourist-related industries. According to 1991 statistics, the average exhibitor and convention delegate stayed in Hong Kong for 8.4 and 7.2 days, respectively, while the typical tourist stayed only 3.5 days. More striking, perhaps, are the figures for the income the trade show industry brings to Hong Kong: while the average exhibitor or convention delegate spends about $2,564 (HK$20,000) per visit, the average tourist spends less than $800 (HK$7,000). Last year's largest trade fairs, for instance, brought near-full occupancy rates to the Grand Hyatt Hong Kong (located in the HKCEC complex) and other nearby hotels.

Despite the many challenges facing the convention and exhibition business in Hong Kong, most sectors of the industry remain optimistic about the future up to and beyond 1997. What may ultimately prove to be Hong Kong's strongest point, however, is its location; the explosion in Pacific Rim business may mean that trade shows in Hong Kong are likely to attract a profitable mix of enthusiastic exhibitors and attendees. Assuming that the business climate remains favorable and that Hong Kong's trade show facilities grow to meet demand, prospects look good.

Forecast '92 Projects Slight Upturn in China's Business Climate

Although serious difficulties continue to cloud the business horizon, speakers and participants at the Council's annual Forecast meeting agreed that the overall outlook for China business seems to be improving. Representatives from nearly 70 companies attending the members-only meeting on February 4 in Washington, DC, found the sessions generally upbeat about the prospects for China business in 1992.

Donald M. Anderson, president of the Council, opened the afternoon meeting with an overview of the critical issues member companies must monitor in the year ahead. He noted that after a year of great tension in Sino-US bilateral trade relations in 1991, the tough stance taken by the Bush Administration on a number of trade matters appears to be having some effect. Recent progress on the protection of intellectual property and the dismantling of barriers to US shipping companies in China augur well for the resolution of other US-China trade disputes. But looming over the bilateral relationship, Anderson cautioned, is the annual fight in Congress over renewal of China's Most Favored Nation (MFN) trading status; the June deadline for the President to certify renewal of MFN for 1992 is fast approaching and the ensuing battle will be strongly influenced by the success or failure of ongoing efforts by the Administration to resolve outstanding trade disputes with China.

Professor Lyman Miller of Johns Hopkins discusses the upcoming CCP Congress.

Following Anderson's analysis of Sino-US political relations, Lyman Miller, director of the China Studies Program at the Johns Hopkins Paul H. Nitze School of Advanced International Studies, discussed the events that will shape China's domestic political agenda in 1992. Miller disagreed with the prevalent view in the Western media that dissension among China's leaders has left them paralyzed and without direction. Rather, Miller argued, the leadership, though embattled, has begun to confront some of the fundamental problems of reform. A turning point in this process was the December 1990 plenum, when economic reform and modernization were again proclaimed the keys to social stability and given high priority on the Chinese Communist Party agenda. Though the regime shows little sign of relaxing its tight grip over propaganda and security organs, there is evidence—such as the upgrading of reformist institutions like the State Commission on Restructuring the Economy—to suggest that the economic reform program is being revived.

China should enjoy another year of solid economic growth, reported Shahid Yusuf of the World Bank.

Shahid Yusuf, lead China economist at the World Bank, gave further details of these reforms. He claimed that the abolishment of export subsidies and price reforms for some commodities should be taken as positive indicators that China is again moving its economy toward full marketization. Though Beijing is calling for the economy to grow by 6 percent in 1992, Yusuf noted that this figure is low, and real growth rates are likely to be somewhat higher; industry alone grew by 14 percent last year, and should increase at a similar rate in 1992 as long as there is no drop in credit. Despite the generally optimistic outlook for stable economic growth in 1992, Yusuf cautioned that problems remain. In particular, State enterprises, which comprise 54 percent of the industrial sector in China, continue to be a drain on economic growth, though the number of such industries run-

Import Committee to Draft White Paper

The Council's Import Committee met on the morning of February 4 in Washington, DC, to discuss a number of key issues threatening the bilateral trade relationship. The overall theme of the meeting was that US importers are at a critical juncture in their relations with China, and that the committee as well as individual members must take a number of steps to protect their interests. Specifically, committee members were urged to contact legislators thought to be wavering in their support of unconditional MFN for China. Sandy Berger of Hogan & Hartson assessed the current MFN situation, pointing out that China's MFN status remains threatened by issues such as the US trade deficit, human rights and missile proliferation concerns, and the 301 market access discussions.

The second half of the meeting focused on a white paper to be presented to Chinese authorities. The current draft outlines eight major concerns of US importers, including a perceived decline in Chinese quality control and growing barriers to resolution of legitimate claims. Committee members were urged to keep current on these and other issues by logging into the Council's electronic bulletin board.

ning in the red is down to about 30 percent.

John Frisbie, director of the Council's Beijing office, wrapped up the session with insights into prospects for US companies in 1992. Frisbie suggested that China's continuing economic growth and large foreign exchange reserves should lead to an increase in China's imports in 1992, perhaps by around 10 percent. Suppliers of only some products—such as raw materials, grain, machinery, and aircraft—will benefit from this increase, however; no increase is likely in imports of consumer goods or products China can make itself, such as soda ash.

R. John Clark of Hoechst-Celanese Corp. shares some thoughts with Paul J. Mehalso, Amoco Corp.

Xerox Corp.'s James W. Garrity, Frans K. Ryckebosch, and Mary Jean Duran took special note of the afternoon's proceedings.

On the investment side, Frisbie noted that foreign investment in China posted its highest gains ever in 1991, exceeding 1990 levels by over 60 percent. Much of this investment, however, reflects a shift from Taiwan and Hong Kong of small, low-technology manufacturing. But US companies also signed a larger number of projects last year, and the sharp increase in the number of US companies visiting China seems to indicate that many US executives now feel it is possible to have successful projects in China. Though problems still exist, Frisbie suggested that 1992 may be a good time for companies to investigate investment opportunities in China.

Forum Explores Impact of "Greater China" on US Policy

After examining current developments in China and the short-term business outlook at Forecast '92, Council members joined their counterparts from business, academia, and the government for a second day of meetings to examine the growing links between China, Taiwan, and Hong Kong, and the implications of these links for US policy. The meeting, *"American Economic Relations With Greater China: Challenges for the 1990s,"* was held in Washington, DC, on February 5, and was co-hosted by the Council's China Business Forum and the American Enterprise Institute. Over 350 people attended the event, which was made possible by corporate support from American International Group, Inc., Ford Motor Co., Monsanto Co., Xerox Corp., Cargill Inc., Fluor Daniel, Inc., and S.C. Johnson & Son, Inc.

After a welcome by Council President Donald Anderson, the day-long conference opened with comments by Montana Senator Max Baucus on the importance of preserving MFN status for China (*see* p. 12). Though adamant that it is important for the United States to set a moral example and take a stance on China's human rights violations, Baucus urged Congress to use more rational means than withdrawing or attaching conditions to MFN renewal to influence China's behavior.

The rest of the morning focused on the key factors that will affect US relations with Hong Kong, Taiwan, and China in the years ahead. Anderson led off with an analysis of China's growing significance in the global economy, a development due in part to the transfer of manufacturing operations from Hong Kong and Taiwan. Other experts included Kerry Dumbaugh of the Congressional Research Service, who explained Congress' evolving view toward Hong Kong. Rather than being viewed solely as an element of US-

Senator Max Baucus (D-Mt) stressed the importance of using targeted policy tools to address grievances with China.

China or US-United Kingdom relations, Hong Kong is beginning to be seen in its own right on Capitol Hill. Clearly, with over 900 US companies maintaining offices in the territory and $7 billion in US investment in 1991, Hong Kong is of vital business interest to the United States. The challenge is to preserve Hong Kong's ability to compete globally, which will be key to the territory's viability in the years up to—and after—it reverts to Chinese rule in 1997.

David Laux, president of the US-ROC Business Council, talked of the growing role Taiwan has played in the global and East Asian regional economies. US ties with the island, though unofficial, are strong, and the US trade deficit with Taiwan has fallen as the territory has sought to increase its imports of US goods. Laux believes "it is only a matter of time" before official contact between Taiwan and the mainland takes place; already, Taiwan's business organizations are working with their Hong Kong counterparts to explore opportunities on the mainland. US companies, according to Laux, are well positioned to work with Taiwan firms to develop business with the PRC.

Wrapping up the morning panel was A. Doak Barnett, professor emeritus of Chinese politics at the Johns Hopkins Paul H. Nitze School of Advanced International Studies. Barnett argued that the economies of Hong Kong and China—both impor-

Experts at the morning panel answer audience questions on the growing economic integration of China, Hong Kong, and Taiwan.

Over 350 participants gathered to learn about US policies toward "greater China."

tant to the United States—have become increasingly intertwined, leaving Hong Kong vulnerable to US trade policies toward China. In order to strengthen US economic ties to all three areas, Barnett urged the US government to work to get all three into key international organizations such as the General Agreement on Tariffs and Trade (GATT).

Lunch featured a speech by Harry Harding of the Brookings Institution on the "natural economic territory" comprised by China, Taiwan, and Hong Kong. Seconding Professor Barnett's remarks, Harding stressed that growing links between the three mean the United States can no longer think in purely bilateral terms when dealing with any one player. Instead, the United States should seek to ensure that the removal of administrative barriers between these areas does not lead to new barriers being erected against other countries. This goal could be accomplished by seeing that all three areas belong to multilateral institutions; Harding proposed that the US government link the issue of GATT accession for China and Taiwan to resolution of the ongoing 301 investigation of China's market access policies by the US Trade Representative.

During the afternoon, participants broke off into separate workshops to focus on specific issues influencing US economic ties to China, Taiwan, and Hong Kong. Topics discussed included market access, GATT and other multilateral institutions, export controls and technology transfer, intellectual property protection, and the treatment of US investment. Roger W. Sullivan, former president of the US-China Business Council, concluded the day's activities with the warning that further deterioration of US-China relations would have adverse effects on Hong Kong in particular. He argued that the United States should continue to take a tough stance with China's leadership, with the objective of speeding the process of change to a new generation of leaders. Sullivan urged US companies to keep their "feet in the door" in China, but to hedge themselves against the risks of investing there.

Kerry Dumbaugh of the Congressional Research Service discussed Hong Kong's strong economic links to the United States and China.

Will China Follow the USSR?

China is destined for far-reaching change, but the communist regime is unlikely to disintegrate

by A. Doak Barnett

The collapse of communism in the Eastern bloc and the disintegration of the USSR have altered the world scene in fundamental and irrevocable ways. Will the winds of change soon sweep away the remaining communist regimes, including the only one that still rules a nation of global importance—China?

China certainly has not been immune to the spreading winds of change. Recent trends and events indicate that China has entered an important transitional period which is inherently unstable, leaving its future inevitably uncertain. The Tiananmen massacre in 1989 discredited the octogenarian party elders and their proteges, and the country is now holding its breath, waiting for the succession to occur and for new leaders to emerge.

In this situation, could some dramatic development trigger a collapse or disintegration comparable to the events in Eastern Europe or the Soviet Union? In light of the fact that virtually no one accurately predicted the course of events in those areas, how can one say that a comparable cataclysm, no matter how unexpected, would be impossible in China?

China and the USSR: the differences

Possibilities, however, are one thing; probabilities are another. Although there are similarities between China and the former East European and Soviet regimes, there are also crucial differences. There are many reasons to believe that although China is undergoing a period of historic change, its regime is not on the verge of collapse or disintegration, and its future evolution is likely to follow its own distinctive path.

Recent trends and events indicate that China has entered an important transitional period which is inherently unstable, leaving its future inevitably uncertain.

Most important, unlike the Soviet Union, China did not suffer a disastrous economic decline during most of the 1980s; instead, it achieved remarkable economic growth which more than doubled average living standards, and it took major steps toward reform that began to transform the structure of its economy. In China there is food on the table and there are consumer goods in the stores. In contrast to both the Soviet Union and several East European nations, moreover, China has not been threatened by ethnic fragmentation; it does face serious problems with its minority groups, but these groups make up less than one-tenth of the country's population.

The Chinese regime also differs fundamentally from the former communist regimes of Eastern Europe, which always lacked legitimacy because they were imposed by a foreign power; the Chinese communist regime, in contrast, was homegrown and rose to power by appealing to nationalism, as well as to peasant dissatisfaction. Although the strength of the Chinese communists' ideology, organization, leadership, and popular support have weakened with time, the regime's legitimacy has by no means been destroyed. The communists continue to maintain sufficient control over the army and the public security apparatus to enforce order. Popular dissatisfaction has not been translated into effective organized opposition, and fear of chaos, which is widely shared even among opponents of the present leadership, has inhibited open challenges to the legitimacy of the system.

For these and many other reasons, it is unlikely that the Chinese communist regime will experience the same fate, or follow the same path as the regimes in the Soviet Union and Eastern Europe, though it clearly will be affected by the changes in those countries. The Chinese regime's initial response has been to try to restrict the impact of these events by strengthening its mechanisms for domestic political control, but this could well change, especially after the next generation of leaders in China takes power. Such leaders are likely to recognize that even if they are able to contain some problems through tightened controls, the long-run solutions to basic problems will

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require more extensive reform. Whatever influences play on China from abroad—whether from East or West—Chinese leaders can be expected to search for a distinctive "Chinese road." However, that road will almost certainly involve far-reaching changes, dictated by the dynamics of domestic forces now at work within China.

The approaching succession

What China now faces is a generational succession—the passing from the scene during a very brief period, either through death or incapacitation, of all the surviving revolutionary "founding fathers." These men are all in their eighties. No one can predict exactly how long this "rolling succession" will take, but it cannot be more than a few years. However, it will not be complete—and therefore, the characteristics of the "post-Deng" period will not become clear—until this entire group no longer exercises decisive influence.

Apart from Deng himself, the most powerful of the surviving founding fathers is Chen Yun. A number of others are also very influential because of seniority and the special legitimacy derived from their revolutionary roles. They include Yang Shangkun, Li Xiannian, Peng Zhen, Wang Zhen, and Bo Yibo. The most important struggles about policy in China still take place among these elders. The next generation of leaders, who currently occupy the top formal positions, are proteges of particular Chinese Communist Party (CCP) elders. No one in this successor generation—including CCP General Secretary Jiang Zemin and Premier Li Peng—has yet built a strong power base of his own.

Paramount leader Deng Xiaoping has already seen two of his proteges toppled by conservative forces.

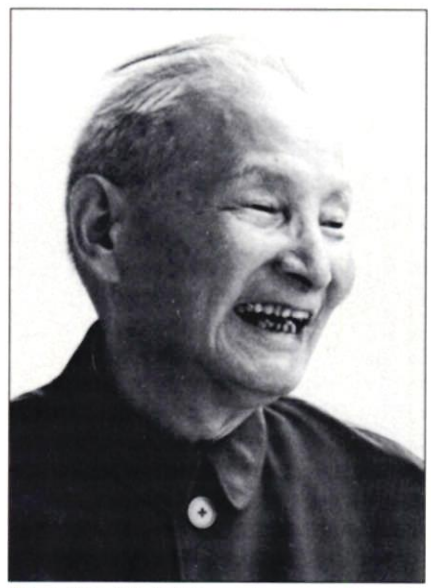
Although there are significant differences of views among the Party elders, as a group they have tended to be conservative or at least cautious about reform, and they all have placed extremely high priority on maintaining political stability. At present the views of the elders are reflected in those of their likely successors, but there is reason to believe that the spectrum of views among the latter is broader, and is almost certainly weighted more toward active economic reform.

When all of the elders pass from the scene, the dynamics within the top leadership will change fundamentally. With their sponsors gone, the successors will be compelled to define their own positions, build their own bases of power, find their own sources of legitimacy, and work out new relations among themselves. In the meantime, as each of the Party elders passes from the scene, the balance within the leadership will shift to some degree, depending on the order in which the elders depart. Most important in this respect will be the timing of the deaths of Deng and Chen Yun. If Deng goes first, cautious or conservative views could well be strengthened temporarily, whereas if Chen's death precedes Deng's, the impetus toward further economic reform could well gain strength.

Current leadership views on economic reform . . .

Today, on the eve of the succession, what are the characteristics of the existing coalition? Could there, at some point, be a basic long-term reversal of the reform process initiated a decade ago? One cannot say that this is impossible, but it is unlikely, at least for the foreseeable future. Virtually all of China's top leaders favor—albeit in varying ways and degrees—the regime's commitment to Deng's policies of "economic reform and opening." It is difficult to identify any top leader as an economic reactionary or arch-conservative (i.e., an individual who would favor moving backward toward a Stalinist-model command economy or toward Maoist populist policies). Certainly, no leader has publicly tried to define any comprehensive conservative economic program. Therefore, virtually all of them can be labeled economic reformers of one sort or another. However, they can be grouped, very roughly, into three categories on the economic reform spectrum: cautious reformers, moderate reformers, and bold reformers.

The disagreements among these groups concerning the pace and extent of economic reform, although not as great as some observers have argued, have been of tremendous importance. Such differences have been at the heart of policy debates within the leadership for many years. These debates will unquestionably continue, and their outcome will determine China's future economic course—and its degree of economic success—in the years ahead.



Chen Yun, 86, is the most powerful man in China after Deng.

Cautious reformers will favor only very gradual movement toward marketization and privatization, and will insist on the continuation of a significant measure of State planning and a predominant role for State enterprises. Moderate reformers will push toward market socialism, but they too, will argue for incrementalism. Although the mix of planning and market mechanisms endorsed by these leaders calls for a substantial increase in the role of the market, they probably will continue to argue against rapid change because of their fear of instability. The boldest reformers will push for a much more rapid and far-reaching transformation of the economy, seeking to establish market predominance and encouraging more extensive privatization of enterprises.

Renewed movement in 1991 on certain reforms—such as the development of securities markets—indicates that the influence of the moderate reformers has already started to grow. Bolder reformers will likely gain influence at a later stage, especially after a new leadership emerges.

. . . and political liberalization

The spectrum of political views within the Chinese leadership re-

Jiang Zemin does not yet have a strong power base of his own...

quires a different classification, and can best be categorized as follows: political conservatives, moderate political reformers, and political liberals. The surviving Party elders—including Deng—have clearly been conservative in their views on political reform. Although Deng has gone along with some steps toward political liberalization, in every period of tension or crisis he has re-emphasized the "four cardinal principles," which assert the importance of the socialist road, ideology, the State, and, most important, CCP leadership.

The main trends during the succession phase will likely be toward cautious or moderate economic reform, combined with political conservatism or limited political reforms.

Most of the other elders have been even more politically conservative than Deng. They have been willing to endorse some limited political reforms, including rationalization of the bureaucracy and greater consultation with non-Party groups, but have opposed major structural reforms and have placed highest priority on the maintenance of political stability. A few of the oldtimers—such as Deng Liqun—are clearly reactionary, but they constitute a small minority and their efforts to revive ideological and political indoctrination have not been effective, except in the most superficial sense.

The successor generation includes some individuals who are politically very conservative, but a sizable number could in time prove to be either moderate political reformers or political liberals. Of six men currently serving on the CCP's Standing Committee (the top decision-making body in the Party), three men—Li Peng, Yao Yilin, and Song Ping—are almost universally viewed as conservative, but some well-informed Chinese believe the other three—Jiang Zemin, Li Ruihuan, and Qiao Shi (who currently is responsible for China's security apparatus)—could eventually prove to be moderates or liberals.

In varying ways and degrees, the political moderates and liberals in China are likely to favor less Party intervention in day-to-day government affairs and enterprise management, significant loosening of ideological and political controls, greater freedom of expression, some movement toward increased pluralism in society, and a gradual increase in genuine political participation. Such views were among the reasons that former CCP general secretaries Hu Yaobang and Zhao Ziyang ultimately were ousted by more conservative Party elders.

Though a significant number of Chinese intellectuals and students have called for major steps toward democratization in the Western sense, at present they have neither a strong political base within China nor a well-defined program. It is not possible to identify anyone—even among the most liberal reformers—in the leadership likely to support this kind of democratization in the near future. Even many reform-minded Chinese intellectuals now seem to fear that political change that is too rapid might result not in sustainable democratization, but in increased political instability, which could produce a reactionary backlash.

The spectrum of political views among China's elite suggests, therefore, that major progress toward multiparty democracy is unlikely in the near future. Trends are likely to be either toward a conservatism that seeks to maintain stability through political controls, or toward a more liberalized form of authoritarianism that would loosen controls in order to repair relations between the State and society, and thus more effectively mobilize support for modernization. The imminent generational change in leadership would seem to slant the scales toward some degree of liberalization, though an extremely reactionary trend could not be ruled out if China were to suffer some crisis that led to greatly increased instability.

Although policy trends throughout the rolling succession will vary with leadership changes, it seems plausible that the main trends will be toward cautious or moderate economic reform, combined with political conservatism or limited political reforms. After the succession is complete or near-complete, however, it is extremely likely that there will be more far-reaching shifts affecting both the leadership and the regime's policies. Although theoretically these shifts could move the regime in any of several directions, the leadership is likely to be pressured to carry reform much further in the 1990s. There are many reasons for this judgement, but several are particularly important.

Pressures for change

First, while China's economic situation is by no means disastrous, the country faces serious problems which cannot be solved without moving economic reform forward—a fact recognized by a large percentage of Chinese leaders in the successor generation. Politically, pressure will come from the large percentage of China's intellectuals and educated youth who feel alienated from—and bitter toward—leaders such as Li Peng, on whom they blame the Tiananmen massacre. Moreover, a sizable part of the general population, especially in urban areas, is cynical because of growing economic inequities and the pervasiveness of corruption and nepotism. These attitudes make it difficult for the leadership to maintain social stability and mobilize active support for modernization efforts, and will result in growing pressures on the Chinese leadership to liberalize the political system.

Many other pressures from below will be exerted by a variety of powerful forces working for change—forces that were first released in China during the initial decade of reform. These include the gradual pluralization of Chinese society, the revolution in communications, the flow of ideas and influences from abroad, and the erosion of traditional ideology. The full effects of trends that were initiated in the 1980s will take time to be felt, but they will have a profound impact on China's society, economy, and polity in the coming years.

Another push toward greater reform is likely to come from China's technocrats—the younger generation of officials who occupy posts at almost all levels beneath the very top. Mostly in their fifties or even younger, these leaders and bureaucrats did not participate in the revolutionary struggle for power, have little interest in ideology, and are essentially technocratic and pragmatic. Their prime concern is economic development. Although again there is a range of views about specific reforms (their reactions are strongly influenced by how they think specific reforms will affect their own local and institutional interests), most can be expected to favor moving the economic reform process forward.

Because no individual will soon be able to assume the kind of leadership role that Deng has enjoyed, the leadership will of necessity have to be even more collective than it has been in the last few years.

The political predispositions of these leaders are less clear, although most of them are likely to favor some liberalization because they recognize it is necessary for modernization. Apart from a very small number of Zhao Ziyang's closest associates, few of the reformist technocrats who emerged in the 1980s were purged after June 1989, and most are still in place. This is also true of most reform-minded intellectuals in universities and research institutions. Though many people in these categories have been quiescent and passive since 1989, in private some are remarkably frank about their support for further reform and in their criticism of conservative leaders. Their views undoubtedly still influence some top members of the leadership and, if and when the balance at the top changes significantly, they will probably reemerge as a very important constituency pressing for further reform.

Contenders for the top post

Though there have been remarkably few changes in China's top leadership since the period immediately following the crisis of 1989, in the second half of 1991 there were a few new appointments which may prove harbingers of future changes. Most notable of the appointments was the elevation of Shanghai's reform-minded mayor, Zhu Rongji, to a vice premiership, and the partial rehabilitation of Hu Qili, who was one of the top reformers in the CCP Standing Committee and was purged along with Zhao Ziyang. Hu now holds the post of vice minister of the Ministry of Machine Building and Electronics Industry. At some point, a general reshuffling of the top leadership will also occur. Conceivably, the process could begin this year, as the CCP is scheduled to convene its next congress (the first since 1987) in 1992. If the congress makes major changes in the central committee and Politburo, the National People's Congress can be expected thereafter to reshuffle the top government leadership.

If asked to specify the ideal qualifications for China's next top leader, many Chinese would probably say that he (it will almost certainly be a

...while Li Peng is tainted due to his role in the Tiananmen crackdown.

man) should be an individual untainted by the Tiananmen massacre, identified with Deng's commitment to economic reform and an open policy, and acceptable to both the People's Liberation Army (PLA) and the country's most influential provincial leaders. He should be able to work effectively in a coalition that includes people with different views, and should be committed to maintaining political stability and unity while moving gradually toward political liberalization and reconciliation between State and society. No one on the horizon, however, fully meets these qualifications. Because no individual will soon be able to assume the kind of leadership role that Deng has enjoyed, the leadership will of necessity have to be even more collective than it has been in the last few years.

Jiang Zemin may well continue as CCP general secretary, at least in the immediate post-Deng period. Deng has strongly supported him as the "core" of the successor generation. Even though Jiang does not have a history of close relations with the military, with Deng's backing he has become—unlike former proteges Hu Yaobang and Zhao Ziyang—the formal head of the Military Affairs Commission. Yang Shangkun, who is close to Deng (and who, together with his younger brother Yang Baibing, supervises day-to-day military affairs), seems likely to support Jiang, mainly because he is Deng's choice.

Essentially a pragmatic technocrat (he formerly headed the electronics ministry and then became mayor and subsequently party secretary of Shanghai), Jiang has important links both with central and provincial-level leaders and bureaucrats. Jiang would probably favor more active reform, especially in economic areas. He has not yet built a strong political base of his own, however, and there is no certainty that he will be able to do so—being designated successor certainly does not guarantee long-term political survival. If Jiang demonstrates that he can exercise effective leadership on his own, he could retain his position for some time, but many Chinese doubt he has the qualities necessary to stay at the top. If this proves to be the case, he could end up simply a transitional figure, similar to Hua Guofeng, who succeeded Mao.

President Yang Shangkun clearly will be a transitional figure because of his age, but he could play a very important role as a kingmaker. If an intense power struggle were to split the leadership wide open Yang might conceivably assert primacy, but this does not seem likely; even if it did occur, it would probably not last long. It is more likely that Yang will back Jiang Zemin.

Premier Li Peng seems very unlikely to rise higher, or, in fact, to retain his present position for long. Although in some respects he may have strengthened his position since the Tiananmen crisis, his base of support remains relatively weak, as he is very dependent on the support of Chen Yun and other elders. Moreover, because he played such a prominent role in the Tiananmen crackdown, he is one of the most widely despised political figures in China. After the Party elders who have supported him pass from the scene, he is likely to be pushed aside or "promoted" to a position with less power. The chairmanship of the National People's Congress is rumored to be one possibility.

Li Ruihuan could conceivably rise to a top position.

One cannot totally exclude the possibility of a comeback by Zhao Ziyang, who remains a leading symbol of reform for many people in China. (Deng himself, of course, was able to make two comebacks from political disgrace). In early 1991, rumors circulated among Chinese intellectuals that Zhao might be rehabilitated. If he were to regain power, this would signal a dramatic shift in the leadership balance, and Zhao probably would try to accelerate the reform process more than most other potential successors. However, Zhao's return to power does not seem probable, in part because of his age and in part because such a comeback would be extremely controversial. It would inevitably evoke some strong opposition, and might impose severe strains on the leadership.

The identifiable pool of others who could conceivably eventually rise to the top includes a number of individuals currently in the leadership, as well as some who have been excluded since 1989. Those who seem to be at or near the reformist or liberal end of the political spectrum appear to outnumber those who seem to share the conservatism and caution of most Party elders. Men such as Li Ruihuan, formerly mayor of Tianjin and currently a member of the CCP Standing Committee; Zhu Rongji, who as noted earlier has recently moved from Shanghai to Beijing; and Ye Xuanping, former governor of Guangdong and now vice chairman of the People's Political Consultative Council, are all strongly identified with reform and have the potential to rise to (or near) the top. So too does Qiao Shi, who, despite his present position as security chief, is regarded by some Chinese as a potential reformer, perhaps of the Yuri Andropov type. (There were reports in 1989 that Qiao was seriously considered for the position of general secretary but was not chosen because he opposed the use of force in the Tiananmen crisis). Others in this category who, though perhaps less likely to rise to the very top, might rise higher than their current positions include Hu Qili, Vice Premier Tian Jiyun, and the head of the State Council's Taiwan Affairs Office, Wang Zhaoguo.

Those belonging to the conservative pool of potentially important post-Deng leaders appear to be less numerous, and also tend to be older and therefore less likely to rise to the very top. The most notable men in this category are Standing Committee members Yao Yilin and Song Ping, though few Chinese regard them as serious candidates for the top leadership position.

It is very possible, of course, that during the succession process some little-known leader will emerge. One cannot be confident, therefore, about predictions concerning specific individuals. However, the chances seem better than even that general trends will favor the emergence of reform-minded individuals, either technocrats or strong provincial leaders. 完

US Law and Convict-Produced Imports

Prior cases provide little precedent for predicting how Customs will deal with allegations of illegal Chinese exports

James Michael Zimmerman

In several separate instances in the last quarter of 1991, US Customs Service Commissioner Carol Hallett ordered Customs agents throughout the country to detain imports of Chinese goods suspected of being manufactured by forced or prison labor. Relying primarily on evidence accumulated by human rights and labor organizations, Hallett invoked Section 307 of the 1930 Smoot-Hawley Tariff Act, which forbids the import of such goods. Until recently the provisions of this section had been largely ignored by Customs, as past efforts to apply it were unsuccessful due to insufficient evidence. The current Chinese cases have re-opened debate on Section 307, and may lead to tightening of the law. Such a move would be a further blow to US importers of Chinese products, which are increasingly subject to charges of illegal entry and pricing.

Section 307

Section 307 of the Smoot-Hawley Tariff Act prohibits the importation of goods produced, in whole or in part, by forced, slave, or prison labor. "Forced labor" is defined as "all work or service which is exacted from any person under the menace of any penalty for its nonperformance and for which the worker does not offer himself (or herself) voluntarily." This language is consistent with that used in the International Labor Organization's Convention Concerning Forced or Compulsory Labor. Article 2 of the convention states that the term "forced or compulsory labor" refers to "work or service which is exacted from any person under the menace of any penalty and for which the said person has not offered himself (or herself) voluntarily."

Section 307 of the Smoot-Hawley Tariff Act prohibits the importation of goods produced, in whole or in part, by forced, slave, or prison labor.

In addition to banning the import of goods produced with convict labor, US federal law stipulates that persons "knowingly" importing such goods may be subject to criminal penalties. These penalties include fines of up to $1000, imprisonment for not more than one year, or both. To prove that an importer has such knowledge is difficult, though Customs is currently proceeding with a criminal investigation into allegations that the owner and president of a Michigan company were aware that the machine presses they imported from China were produced in a prison factory.

The primary purpose of Section 307 is to protect domestic producers and workers from the artificially low prices of goods produced by convict or forced labor. The legislative history indicates that Congress also was concerned about the inhumane treatment of workers forced to produce goods in certain developing countries. Implementing regulations for Section 307 were developed in 1963 by the Treasury Department, which in turn has delegated authority for their enforcement to the commissioner of Customs.

Under Section 307 and applicable federal regulations, the Customs Service must actually determine that suspected goods are produced with prison, slave, or forced labor in order to prohibit their entry into the United States. Customs, however, generally gives little credibility to evidence that does not constitute first-hand knowledge of alleged forced labor practices. The lack of eyewitness accounts, for example, was an issue in allegations in 1988 that certain categories of goods from the Soviet Union were produced by forced labor. Though evidence compiled by the Department of State, Central Intelligence Agency, and the International Commission on Human Rights concluded that the Soviet Union "continues the deplorable practice of forced labor in manufacturing," the Treasury Department refused to deny entry to Soviet exports because there was insufficient evidence to demonstrate that the goods being imported had actually been produced by forced labor.

The implementing regulations for Section 307 permit the commissioner, upon receipt of reliable information, to order Customs' district directors to withhold merchandise

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suspected of being produced by forced labor. The Customs Service is then required to conduct an investigation in which it must consider evidence offered by foreign interests, importers, domestic producers, or other interested parties.

After the investigation, the commissioner must determine whether the goods in question were produced—in whole or in part—with forced labor, and must publish a finding to that effect in the *Federal Register* and *Customs Bulletin*. Only those specific products found to be produced in violation of the law may be prohibited entry; the Customs Service may not deny entry to an entire class of goods.

Merchandise detained pursuant to the regulations may be voluntarily exported at any time by the importer. Absent voluntary exportation, the Customs Service must withhold the merchandise for three months after publication of the final ruling or for three months after the date of importation of the merchandise, whichever is later. If the importer fails to offer satisfactory proof within this period that the merchandise does not violate the statute, Customs is required to notify the importer in writing that the merchandise may not enter the United States. Sixty days later the merchandise is destroyed unless the importer re-exports it or files an administrative protest to challenge the final finding of the Customs commissioner. If the decision on such a protest is unfavorable to the US importer, the company may then file a lawsuit with the US Court of International Trade in New York.

Exceptions to the rule

Importers whose goods are withheld entry to the United States by the Customs Service under Section 307 also have the right to apply for an exemption under the Hendrick Rule. Formulated in 1956, this rule echoes the unfair competition argument used in Section 307 and allows considerable leeway when imports do not threaten US manufacturers. According to the Hendrick Rule, merchandise produced by convict labor may be imported if the following factors are met:

- The convicts who produced it work voluntarily, and on their own time;
- The government of the country in question receives no pecuniary benefit from the export of the merchandise; and
- The wages paid the workers are comparable to those paid to nonconvict labor.

US importers should investigate where their products are manufactured and avoid doing business with labor-reform facilities or Chinese firms under scrutiny by the Customs Service.

In order to argue that the Hendrick Rule is applicable to his or her case, the importer must provide Customs with information from the manufacturer to prove compliance with these requirements. Customs has previously allowed prison-made goods into the United States upon presentation of such evidence, including Mexican handicrafts in 1968, Canadian automotive exhaust parts in 1979, and Portuguese hand-made rugs in 1980.

Goods that do not qualify for exemption under the Hendrick Rule may do so under other provisions of US law. Because the intent of Section 307 is to protect US industries from foreign producers who obtain a competitive advantage by using forced labor, it does not apply in cases where US production of the goods in question is insufficient to meet demand. The Customs Service applies this exception only in situations where there is no domestic production of the particular product or where what little production there is cannot be significantly expanded, even if the selling price is increased significantly.

Typically, the Customs Service applies this exception after issuing a determination that the goods in question were produced by forced labor. Although the Customs Service is required to explore the applicability of this exception each time it issues such a determination, importers of suspect goods should provide Customs with information from the Commerce Department and private-sector sources that might prove that domestic production of the goods they import does not meet US demand.

Similarly, the Customs Service will not deny entry to goods if only a small portion of the product is produced using forced labor, and that portion is too small to affect the cost of the merchandise. In addition, merchandise produced by voluntary labor will not be denied entry even if

Photo courtesy of the US Customs Service

Socks produced by the New Life Cotton Cloth Mill have been denied entry to the United States pending investigation by the Customs Service.

the inputs used in the production process—including energy and tools—are produced with forced labor.

The Chinese cases

The Chinese goods withheld by Customs during 1991 due to allegations that they were produced by convict labor include small diesel engines, socks, machine presses, steel pipe, socket wrenches, and spanners. The manufacturers under question are the Yunnan Jinma Diesel Engine Works, the New Life Cotton Cloth Mill, the Qinghai Hide and Garment Factory, the Shanghai Laodong Machinery Plant, the Shanghai Laodong Machinery Factory, the Shanghai Laodong Steel Pipe Works, and the Shanghai Complete Set of Labor Tool Co. Several export companies are suspected of being front companies for the prison facilities, including the Shanghai branch of the China Machinery Import and Export Corp., the Shanghai Hardware and Machinery Corp. Tool Branch, and North Science and Technology Co. of Beijing. As *The CBR* went to press, no final rulings in these cases had been issued by Customs.

The detention and possible denial of entry of these goods will result in financial loss to US importers who might have been unaware that the goods were produced under exploitive conditions. To avoid being caught in such a position, US importers should investigate where their products are manufactured and avoid doing business with labor-reform facilities or Chinese firms under scrutiny by the Customs Service.

Tightening the screws

Such cautionary measures will become imperative if new legislation is passed to tighten the existing laws. Election-year politicking could give new steam to two bills introduced last year by Senator Jesse Helms, as well as the concurrent resolution introduced by Representative Sam Gejdenson.

Senator Helms' Anti-Forced Labor Act of 1991 (S.1365) seeks to put bigger teeth into Section 307. The Act would establish a complaint and appeal process and set forth the evidentiary standard necessary to determine a violation of the law. It further provides that private individuals, including human rights orga-

Election-year politicking could give new steam to two bills and a resolution introduced in Congress last year.

nizations, may file a civil action in federal district court to request that the court enjoin the importer from violating the law and compel the Department of Treasury to impose civil penalties.

The second Helms bill, S.1366, seeks to prohibit entry into the United States of "any product, growth, or manufactured article" from China that is produced with forced labor. This bill requires the Secretary of Treasury to obtain a certification from the importer that the goods were not produced with forced Chinese labor. Following the text of S.1366 is an extensive list of alleged exports produced by Chinese prison-labor facilities in a number of provinces. The list is aimed at specific brands (e.g., "Golden Sail" tea), as well as entire classes of goods (e.g., cotton from Xinjiang Province and graphite products from Shandong Province). The inclusion of this list, though not part of the bill itself, creates a presumption that the enumerated items are prohibited from entry unless the importer obtains a certification to the contrary. This bill would also require the Treasury Department to negotiate with the Chinese government to allow US access to suspected prison-labor facilities to ensure that forced labor is not employed in the production of goods for export. However, because the list of forced labor products is based largely on second- and third-hand information and is likely to upset many US-based importers, passage of the bill is unlikely.

More likely to pass, however, is the Gejdenson resolution (H.Con.Res. 216), which demands that China allow international inspections of suspected prison-labor sites and urges the Chinese government to publicly detail the steps it will take to stop the exportation of forced labor products. The resolution is largely symbolic, though, and lacks enforcement means such as sanctions or import restrictions.

Political impasse

Much of what Congress decides to do on the prison labor issue this year may hinge on the Bush Administration's own efforts. Specifically, the next few months will likely reveal whether agreement can be reached on the Memorandum of Understanding (MOU) announced by Secretary Baker during his November visit to China. The State Department is currently in the process of negotiating the MOU, which will allow the United States to gain more information about Chinese exports of forced labor-produced goods—sales supposedly forbidden under Chinese law. The terms of the MOU provide that the State Department have access to suspected labor-reform facilities in order to confirm or dismiss allegations that prison-made goods are destined for US markets. Progress on the MOU, however, appears stalled by the Chinese refusal to allow such inspections on the grounds that they violate China's sovereignty.

The Chinese government, in the meantime, continues to state that labor-reform factories are not allowed to produce goods for export, and that factory managers of such facilities will be punished if they sell their merchandise outside China. However, no commitment has been made to allow US officials access to prison facilities to verify these claims. Nor has the Chinese government agreed to release suspected political prisoners who may be unwilling participants in the prison-labor system. This impasse may lead to greater US scrutiny into allegations of Chinese prison-made products entering the United States, which, coupled with concern over the growing US trade deficit with China, may put the issue of alleged Chinese prison-labor exports high on the political agenda. Although just one of several China-related issues of concern to the Bush Administration, the loose wording of the Smoot-Hawley law leaves the convict labor issue open to political manipulation. The end result, conceivably, could be a greater burden thrust upon US importers. 完

中外贸易 China Business

Val Huston

The following tables contain recent press reports of business contracts and negotiations exclusive of those listed in previous issues. For the most part, the accuracy of these reports is not independently confirmed by *The CBR*. Contracts denominated in foreign currencies are converted into US dollars at the most recent monthly average rate quoted in *International Financial Statistics (IMF)*.

US-China Business Council member firms can contact the library to obtain a copy of news sources and other available background information concerning the business arrangements appearing below. Moreover, 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 the Business Information Center at The US-China Business Council.

中外贸易

SALES AND INVESTMENT THROUGH
January 15, 1992

Foreign party/Chinese party
Arrangement, value, and date reported

Agriculture

Other

Department of Agriculture (US)/Ministry of Agriculture
Signed agreement to cooperate on 18 agro-technology projects, including exchange of plant genetic resources, grassland assessment, and animal feed processing. 12/91.

World Food Programme (WFP)
Will provide aid to increase food production and improve soil and water management through afforestation and construction of dams and river embankments in Shanxi Province. $12.2 million. 12/91.

World Bank
Will provide loan to increase fish and fruit production, bring new land into agricultural production, and improve river-flow conditions in the Pearl River delta. $162 million. 11/91.

Automobiles

Investments in China

General Motors Corp. (US)/Jinbei Automobile Co.
Will establish a joint venture to produce 50,000 light commercial vehicles per year in Shenyang, Liaoning Province. $100 million. (US:30% - PRC:70%). 12/91.

Akzo Coatings International BV (Netherlands)/Beijing Red Lion Coatings Corp.
Established the Akzo-Red Lion Automotive Coatings Corp. Ltd. to produce automotive finishes and related products. $500,000. (Neth:51% - PRC:49%). 12/91.

Chia Thai Group (Thailand)/Luoyang Jialing Motorcycle Factory
Established the Luoyang Norinco-EK Chor Motorcycle Co. joint venture to produce 145cc and 250cc motorcycles. $70 million. (Thailand:55% - PRC:45%). 12/91.

Other

Subaru Inc., a subsidiary of Fuji Heavy Industries (Japan)/Guizhou Aviation Industry Corp.
Reached preliminary agreement to provide technology and machinery to produce 10,000 minicars. 1/92.

Nissan Corp. (Japan)/China National Automotive Industry Import/Export Corp. and China National Automotive Trade Corp.
Opened two cooperative training centers in Beijing and Guangzhou to teach auto repair, maintenance, and manufacture. 12/91.

Isuzu Corp. (Japan)/NA
Began trial operation at the Chengdu Engine Co. joint venture to produce 4JB1 diesel engines for light-duty vehicles. 12/91.

Toyota Corp. (Japan)/Jinbei Automobile Co.
Conducting feasibility study for an automobile manufacturing plant in Shenyang. 11/91.

Banking and Finance

Investments in China

C & C Joint Printing Co. (HK)/Shanghai Press and Publication Development Corp., Shanghai Second Printing Factory, and the Shanghai branch of Bank of Communications
Will jointly fund the Shanghai Printing Co., which will print bank cheques, share certificates, bonds, receipts, and credit certificates. $2.2 million (HK:37% - PRC:63%). 11/91.

Other

China Nationalities International Trust and Investment Corp. (China)
Established Muslim-dominated trust company to attract Arab funds to help finance development of the country's minority regions. $18.5 million. 1/92.

Credit Lyonnais (France)
Opened branch office in Shanghai. 11/91.

Abbreviations used throughout text: BOC: Bank of China; CAAC: Civil Aviation Administration of China; CAIEC: China National Automotive Import-Export Corp.; CATIC: China National Aero-Technology Import-Export Corp.; CCTV: China Central Television; CEIEC: China Electronic Import-Export Corp.; CEROILFOODS: China National Cereals, Oil, and Foodstuffs Import-Export Corp.; CHINALIGHT: China National Light Industrial Products Import-Export Corp.; CHINAPACK: China National Packaging Import-Export Corp.; CHINATEX: China National Textiles Import-Export Corp.; CHINATUHSU: China National Native Produce and Byproducts Import-Export Corp.; CITIC: China International Trust and Investment Corp.; CITS: China International Travel Service; CMC: China National Machinery Import-Export Corp.; CNCCC: China National Chemical Construction Co.; CNOOC: China National Offshore Oil Corp.; CTIEC: China National Technical Import-Export Corp.; ETDZ: Economic Technological Development Zone; ICBC: Industrial and Commercial Bank of China; INSTRIMPEX: China National Instruments Import-Export Corp.; MLI: Ministry of Light Industry; MMEI: Ministry of Machinery and Electronics Industry; MOE: Ministry of Energy; MOTI: Ministry of Textile Industry; MPT: Ministry of Posts and Telecommunications; NA: Not Available; NDSTIC: National Defense, Science, Technology, and Industry Commission; NORINCO: China North Industries Corp.; SEZ: Special Economic Zone; SINOCHEM: China National Chemicals Import-Export Corp.; SINOPEC: China National Petrochemical Corp.; SINOTRANS: China National Foreign Trade Transportation Corp.; : Shanghai Investment and Trust Corp.; SPC: State Planning Commission.

Asian Development Bank (ADB)
Provided grant for consulting services to improve China's auditing procedures. $389,000. 11/91.

Chemicals, Petrochemicals, and Related Equipment

Other

Spain/People's Construction Bank
Will provide soft loans and export credits for equipment and technology for the 140,000-tonne Tianjin Ethylene Project. $76.5 million. 12/91.

Norsk Hydro Corp. (Norway)/Ministry of Chemical Industry
Signed long-term cooperation agreement for development of agrichemicals and petrochemicals. 11/91.

Monte dei Paschi de Siena Bank (Italy), Barclays Bank (UK), Credit Lyonnais (France), and six other French banks/People's Construction Bank
Will provide concessionary loans for Italian and Dutch companies to sell equipment and technology for the 115,000-tonne Beijing Ethylene Project. Includes $106 million in credit loans for Italian buying party, $26 million in credit loans for Dutch buying party, and $30 million in commercial loans. 11/91.

Montecatini Tecnologie, a subsidiary of Ferruzzi-Montedison Group (Italy)/Beijing Institute of Chemical Industry
Signed a research cooperation agreement to collaborate on projects for the development of chemicals, petrochemicals, and intermediate products. 11/91.

Computers and Computer Software

China's Imports

Unisys Corp. (US)/CAAC
Will sell a 2200-600ES series mainframe for processing airline reservations and ticketing. $13 million. 1/92.

Digital Equipment Corp. (US)/Tianjin Port Authority
Sold 12 DEC 5200 systems, six LANs, 150 terminals, 60 printers, and related systems application software. $1.2 million. 11/91.

Investments in China

Nippon Electric Corp. (Japan)/Beijing Capital Iron and Steel Corp.
Established the Shougang NEC Electric Co. Ltd. joint venture in Beijing to produce integrated circuits. $195.5 million. (Japan:40% - PRC:60%). 12/91.

Imaje Ltd. (France)/Nanjing Light Industrial Machinery Factory
Established the Imaje-Jinling Ink Jet Coder Ltd. joint venture to produce code printers in Xiamen, Fujian Province. $1.58 million. (France:60% - PRC:40%). 12/91.

AST Research Inc. (US)/NA
Will establish a joint venture to produce 100,000 microcomputers/year . 12/91.

Bull HN Information Systems Inc., a joint venture between Honeywell Inc. (US), Compagnie des Machines Bull (France), and NEC (Japan)/NA
Will establish a joint venture to produce UNIX application software in either Beijing or Guangdong Province. 12/91.

Digital Research Inc. (US)/Beijing Stone Corp.
Will establish a joint venture to develop and market computer software and conduct research for a Chinese-character input system. 12/91.

Word House (Netherlands)/NA
Will establish a joint venture to develop and market computer software in Guangzhou. 12/91.

Other

International Business Machine Corp. (US)/Vanda Computer International
Opened customer service center in Guangzhou to display the PS/2 computer series and related software. 12/91.

European Community (EC)/China
Established the China-EC Biotechnology Center (CEBC) to work on the China National Online Information retrieval network and an optical fiber communication project. 11/91.

China's Investments Abroad

Shenzhen Electronics Group (China)/Hong Kong
Signed lease for 3.4 hectare site at the Tai Po Industrial Estate to build a plant for production of integrated circuits and computer chips. $312 million. 1/92.

Engineering and Construction

Investments in China

Price Brothers Co. (US)/China Building Material Academy, Suzhou Concrete and Cement Products Research Insitute, and the China Building Material Industrial Corp.
Signed agreement to establish the Zhonglian Price Pipeline Co. Ltd. joint venture to manufacture equipment for making pre-stressed concrete cylinder pipes (PCCP). 11/91.

Environmental Technology and Equipment

Other

Asian Development Bank (ADB)
Will provide technical assistance grant to upgrade Environmental Management Information Systems (EMIS) in Shanghai, Dalian, and Nantong. $600,000. 12/91.

Asian Development Bank (ADB)
Provided grant for consulting services to improve Dalian's water resource development. $576,000. 11/91.

World Bank
Will provide loan for multipurpose environmental project that addresses water, air, and solid waste pollution in Beijing. $125 million. 11/91.

Food and Food Processing

Investments in China

President Enterprises Corp. (Taiwan)/Beijing Great Wall Food Factory
Established the Beijing President Food Co. Ltd. joint venture to produce instant noodles. $5 million. (Taiwan:50% - PRC:50%). 12/91.

China First Merchandising Co. of California (US)/Beijing United Agricultural Corp.
Established the Beijing Bud's Ice Cream Co. Ltd. to produce ice cream in Beijing. $5 million. 11/91.

Medical Equipment

Other

World Bank
Will provide loan to support the Infectious and Endemic Disease Control Project to reduce the incidence of schistosomiasis and tuberculosis. $129.5 million. 12/91.

Project Hope (US)/Shanghai Second Medical University
Announced agreement to develop a modern pediatric hospital and medical training center in Pudong. 11/91.

Metals, Minerals, and Mining

China's Investments Abroad

China/Iran
Signed agreement to cooperate in mining Iran's coal fields, with China to provide engineering plans and all equipment for extracting coal. $2.6 million. 11/91.

China/Iran
Signed letter of understanding for China to help Iran build a 200,000 tonne copper-producing plant. 11/91.

Packaging, Pulp, and Paper

Other

Pan Pacific Trading Corp. (US)/Anhui Province
Signed agreement to plan, manage, and provide technology for a 700,000-acre pulpwood plantation to supply a joint-venture pulp mill in Shanghai. 12/91.

Petroleum, Natural Gas, and Related Equipment

Investments in China

Air Liquide Group (France)
Opened its wholly owned liquid gas venture, the Liquid Air Shanghai Co., to produce nitrogen, oxygen, and argon gases for industrial use. 11/91.

Other

Texaco Inc. (US) and BHP Petroleum Inc. (Australia)/CNOOC
Signed agreement for oil and gas exploration in 5,000 sq km area of Bohai Bay near Tianjin. 12/91.

Dai-Ichi Kanyo and four other Japanese banks (Japan)/SINOCHEM
Will provide loan for the West Pacific Petrochemical Co. Ltd., a Sino-HK-French joint venture, to build an oil refinery in Dalian. $30 million. 12/91.

The Acts Operations Group (US, Italy, Netherlands)/CNOOC
Began operation of the 26-1 oilfield in the South China Sea. Annual production capacity is estimated at 1.5 million tonnes. 11/91.

Pharmaceuticals

Investments in China

Cansia Trading Co. (Malaysia)/Beijing Huafeng Medicines Factory
Beijing Liling Chinese Medicines Co. Ltd. joint venture began production of drugs to cure impotence and other male sexual disorders. $950,000. (Malaysia:20% - PRC:80%). 11/91.

NA (Ireland)/NA
Beijing Ji Ai Pharmaceutical Co. Ltd. joint venture began production of sardine amine alcohol aerosol, a new cough medicine. $150,000. 11/91.

Power Plants

China's Imports

Voith Corp. (Germany)/China National Technical Import/Export Corp.
Will sell 2 water turbogenerators for the Wuqiangxi hydroelectric power station in Hunan Province. $80 million. 12/91.

Other

World Bank
Will provide loan to construct two 300MW coal-fired thermal units in Yanshi, Henan Province. $180 million. 1/92.

Siemens AG (Germany)/CTIEC
Signed contract to provide power dispatching system used to monitor the operating conditions of nationwide networks. 11/91.

World Bank
Will provide loan to support construction of Daguangba hydropower station in Hainan Province. $67 million. 11/91.

Property Management and Development

Investments in China

99 Group Inc. (US) and two Shanghai companies/Shanghai municipal government
Signed 50-year land lease at $900 per sq m to build 34-story World Trade Center in Pudong. $7.3 million. (US:94% - PRC:6%). 11/91.

Dalian Industrial Park Project Committee (Japan)/Administrative Committee of the Dalian EDTZ
Signed 50-year land lease agreement for 2.17 sq km to establish the Dalian Industrial Park Development and Management Corp. (Japan:80% - PRC:20%). 11/91.

Ships and Shipping

China's Imports

Germany/China Ocean Shipping Corp.
Will provide soft loan for Bremer Vulker AG and Matthias-Thesen-Werft to sell three containerships. $380 million. 11/91.

Other

Asian Development Bank (ADB)
Will provide loan for construction of additional berths and facilities at Liaoning ports of Yantai, Yingkou, and Dandong. $88.8 million. 12/91.

Telecommunications

China's Imports

Siemens Telecommunications SPA (Italy)/China National Instruments Import/Export Corp.
Will sell 35 microwave stations for the Beijing-Shenyang trunkline. $5.1 million. 12/91.

Italtel Corp. (Italy)/Chongqing Communication Equipment Factory
The Chongqing Italtel Communication Equipment Ltd. joint venture will supply 140 Mbit/sec fiber optic transmission system for 1,200 km project connecting Fuzhou and Guangzhou. 11/91.

Other

Motorola Inc. (US)/Hangzhou Communication Facility Plant
Signed agreement to transfer cellular phone manufacturing technology. 11/91.

Siemens AG (Germany)/Beijing Telecommunications Administration (BTA)
Will arrange preferential commercial loan for the Beijing International Switching System Corp. Ltd., a Sino-German joint venture, to sell a 200,000-line and 100,000-line switching system to the BTA. 11/91.

Textiles

Investments in China

Toray Industries (Japan) and Wah Cheong Textiles (HK)/Shaanxi No. 2 Printing and Dyeing Mill
Established the Shaanxi Wah Cheong Textiles Printing and Dyeing Co. joint venture to dye textiles. $10 million. (Japan:13.3% - HK:26.7% - PRC:60%). 1/92.

Other

Asian Development Bank (ADB)
Will provide loan for the Anqing petrochemical plant, a 50,000 tonne/year acrylic fiber plant in Anhui Province. $105 million. 11/91.

Transportation

China's Imports

Pratt & Whitney (US)/Shanghai Airlines
Will sell 12 PW2000 engines and spares to be used in five Boeing 757 airliners. $72.5 million. 12/91.

The Boeing Co. (US)/Shanghai Airlines
Will sell five 757 airliners. $275 million. 12/91.

Thomson-Link Miles Co. (UK), a subsidiary of Thomson CSF Group (France)/China Aviation Supply Corp.
Will sell flight simulators, visual systems, flight training devices, and computer-based training for the Boeing 747-400, 737-300, and 767-757 aircraft. $60 million. 11/91.

Investments in China

Aerospatiale (France) and Singapore Aerospace/CATIC
Began cooperative manufacturing of parts for a single-engine, 2-tonne class P120L helicopter. (France:61% - Singapore:15% - PRC:24%). 11/91.

Other

World Bank
Will provide loan for construction of motorway project between Guangzhou and Shenzhen. $800 million. 12/91.

China's Investments Abroad

Singapore Aerospace and Roscund Co. (HK)/China Aviation Supplies Corp.
Will establish the Asia-Pacific Aviation Supplies Co. joint venture in Singapore to expand exports of Chinese-developed aircraft materials, components, and aviation technology. (Singapore:40% - HK:20% - PRC:40%). 12/91.

Miscellaneous

Omnicom Group Inc. (US)/China National United Advertising Corp., a unit of Xinhua news agency
Established the BBDO/CNUAC advertising joint venture which will have offices in Beijing, Shanghai, and Guangdong Province. (US:51% - PRC:49%). 11/91.

Singapore/China Chamber of Internation Commerce and the Ningxia Chamber of Commerce
Established the Sino-Malay Investment Holdings Pte Ltd. joint venture to promote economic cooperation and expand trade. $600,000. (Singapore:51% - PRC:49%). 11/91.

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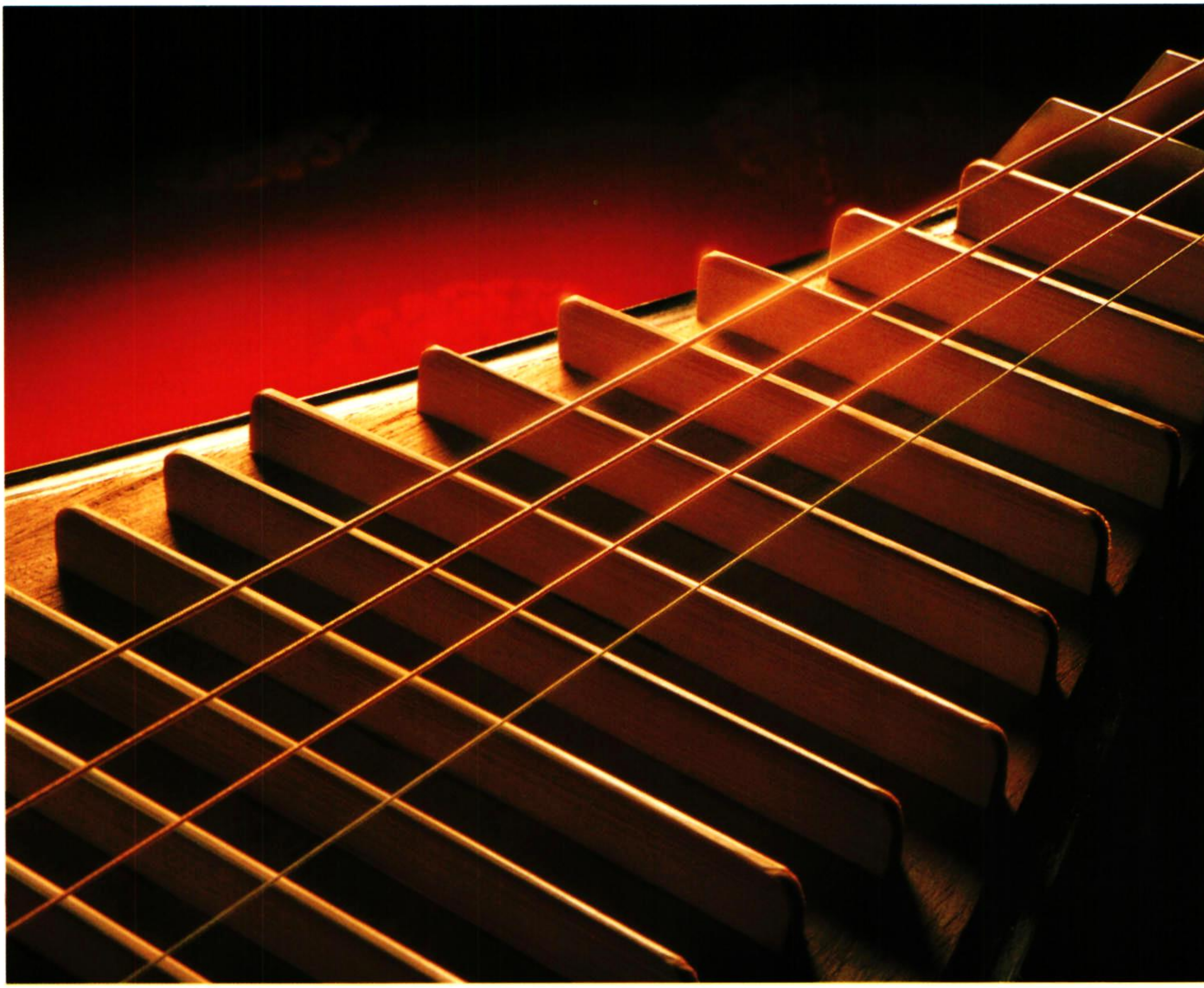

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