SPECIAL ANNIVERSARY ISSUE

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THE CHINA BUSINESS REVIEW

THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL

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Shanghai Office Opening

Baker & McKenzie is delighted to announce the official opening of its Shanghai office - the firm's second office in mainland China. With the new office in Shanghai and offices in Hong Kong, Beijing and Taipei, Baker & McKenzie offers a unique platform from which to provide legal services throughout Greater China. With a history of over 30 years in China, Baker & McKenzie has extensive experience in assisting multinational, Hong Kong and mainland Chinese firms doing business both locally and abroad.

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贝克·麦肯思国际律师事务所
上海代表处

Unit 1601, Jin Mao Tower,
88 Century Boulevard, Pudong,
Shanghai 200121,
People's Republic of China
Tel: (86-21) 5047-8558
Fax: (86-21) 5047-0020
Email: chinalaw@bakernet.com

For further information on our China capabilities, please contact one of the following partners:

Beijing – Bing Ho
Tel: (86-10) 6505-0591
Email: bing.ho@bakernet.com

Hong Kong – Winston Zee
Tel: (852) 2846-1917
Email: winston.zee@bakernet.com

Shanghai – Danian Zhang
Tel: (86-21) 5047-1617
Email: danian.zhang@bakernet.com

Taipei – David Liou
Tel: (886-2) 2715-7238
Email: david.liou@bakernet.com

THE CHINA BUSINESS REVIEW

THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL

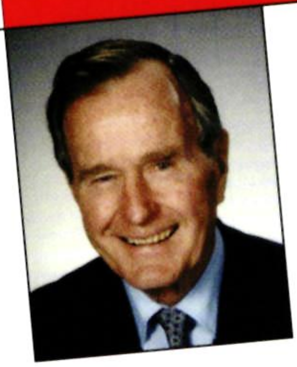
SPECIAL ISSUE:
THE US-CHINA BUSINESS COUNCIL'S 30TH ANNIVERSARY

CELEBRATING THIRTY YEARS

LOOKING BACK...AND AHEAD

DEPARTMENTS

Cover by Greg Berger Design



A Message from George H. W. Bush,

41st President of the United States

The US-China relationship has progressed much over the decades. Our diplomatic and economic contacts have grown and laid the foundation for continued expansion and cooperation. At the same time China has taken vast strides to provide a more prosperous environment at home and to play an increasingly important role in the world.

During these decades, US business has played an increasingly important role in helping China shape its economic future. At the center of this success has been the US-China Business Council, providing American companies support and guidance in helping to expand the economic contacts between our two countries. I congratulate the US-China Business Council on its work and continued commitment to strengthening the US-China relationship. Since my own days in China, I have seen what a valuable resource the Council has been to American business, and I am delighted that this strong tradition continues as the Council marks 30 years of service.

美中关系在过去数十年里有了长足的进展。双方的外交与经济联系日臻成熟，为将来持续的发展与合作打下了基础。与此同时，中国国内的经济环境大为改善，中国在世界上的重要性也在日趋增加。

在这数十年里，美国工商界在帮助中国推动经济方面起着越来越重要的作用。美中贸易全国委员会在这中间扮演了关键的角色。在促进两国经济往来的过程中，美中贸易全国委员会为美国公司提供了各种服务与指南。我在这里对美中贸委会为加强两国关系而作出的不懈努力及其成果表示衷心的祝贺。自我离开中国后，我不断地体会到美中贸委会对美国工商界意味着多么重要的价值。在美中贸易全国委员会成立30周年之际，我非常高兴能看到他们的传统正在继续发扬光大。

中华人民共和国国务院国务委员

吴 仪 的贺词

面向未来，发展中美经贸关系

——为美中贸易全国委员会成立三十周年题

二〇〇三年一月

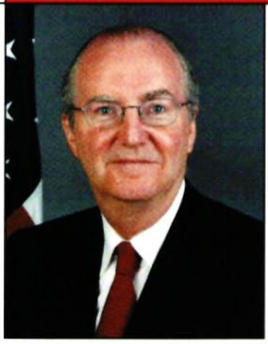
A Message from Wu Yi,

State Councilor, State Council, People's Republic of China

Face the Future: Develop China-US Economic and Trade Relations

—Written on the occasion of the thirtieth anniversary of the establishment of the US-China Business Council

Wu Yi
January 2003



A Message from Clark T. Randt,

Ambassador of the United States of America to the People's Republic of China

Thirty years to the day after President Richard Nixon's historic arrival in Beijing on February 21, 1972, when he emerged from his Boeing 707, hand extended, to grip Premier Zhou Enlai's hand in what Premier Zhou described as the longest handshake in history—across an ocean and a gulf of more than 20 years—President George W. Bush's Boeing 747 touched ground in Beijing. Trade was a key component of that 1972 rapprochement and, indeed, Premier Zhou requested that President Nixon establish a "peoples' organization" to deal with bilateral trade issues in the absence of diplomatic relations. Thus, 30 years ago this month, the National Council for United States-China Trade, as the US-China Business Council was then called, was born. Total two-way trade in 1972 amounted to $95.9 million. In 2002, this amount reached $120 billion. You must be doing something right!

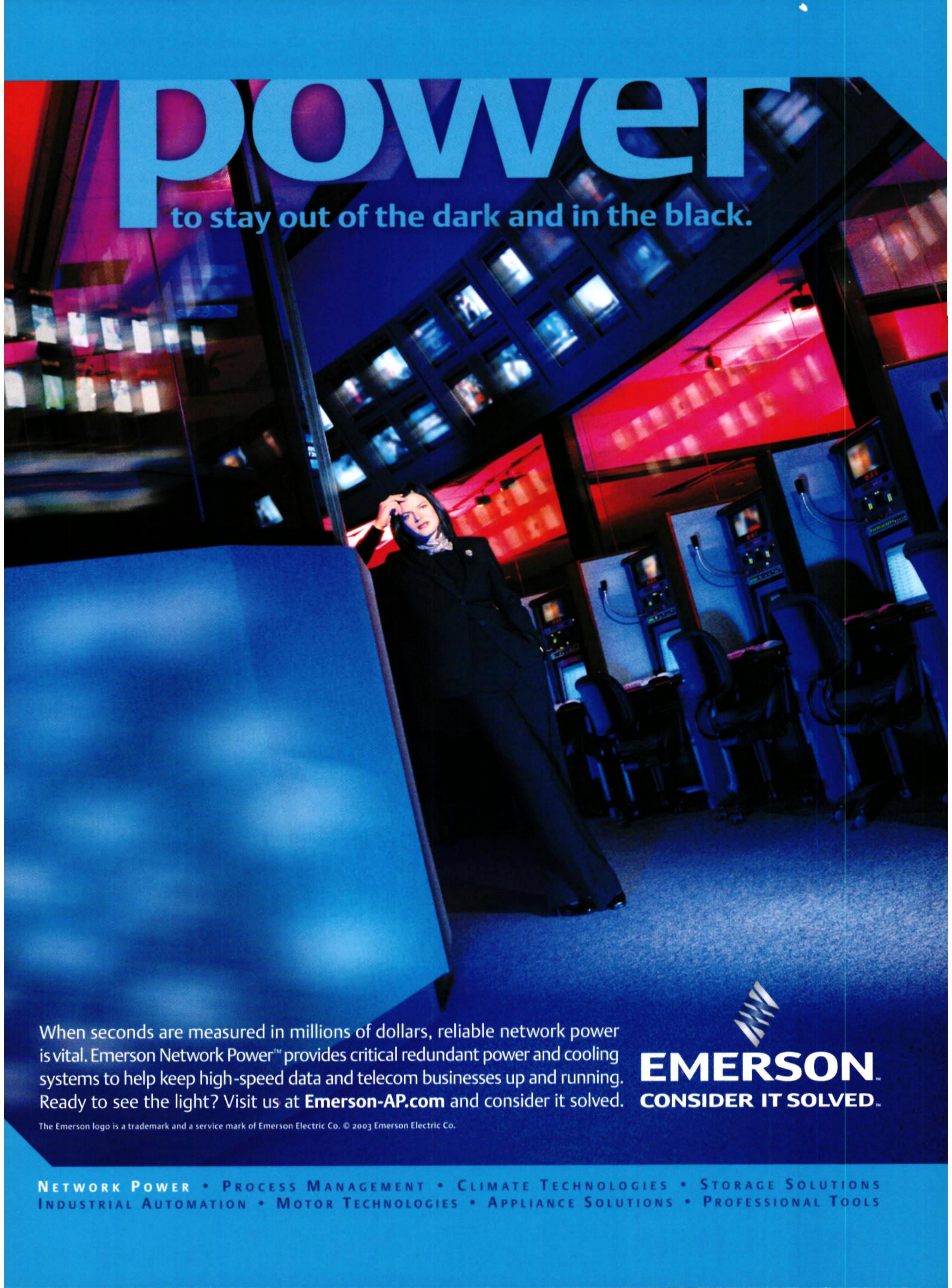
Ambassador Christopher H. Phillips, Melvin W. Searls, Jr., Eugene A. Theroux, Nicholas Ludlow, and myself were among those intrepid early pioneers at the National Council. I recall reading the *New York Times* article announcing the Council's establishment and Ambassador Phillips' appointment. I was in my second year of law school. In 1964, my dad had advised me that China was the future and, in 1968, the US Air Force had taught me Chinese. I was ready and immediately wrote to Ambassador Phillips to apply for a summer job.

The summer job researching and writing about the first technology licensing transactions between United States petrochemical companies and China's TECHIMPORT (now China National Technical Import and Export Corp., or CNTIC) and about early intellectual property rights issues in China turned into a full-time job when the China Council for the Promotion of International Trade (CCPIT), the Council's host organization in China, suddenly approved the Council's application to establish an office at the semi-annual Guangzhou (Canton) Trade Fair, then the conduit for the overwhelming majority of China's foreign trade. Would I consider dropping out of law school temporarily to travel to Guangzhou to establish the Council's trade facilitation office at the Dongfang Hotel for the Fall Tour of 1974 and, afterwards, travel to Beijing for meetings with the CCPIT, the eight Chinese foreign trade corporations, and the chief of the United States Liaison Office in Beijing, George H. W. Bush? I did not have to be asked twice.

I shall never forget departing the Hong Kong Peninsula Hotel in September 1974, on foot with a caravan of trolleys being pushed by a fleet of white-jacketed bellmen from the hotel. We followed the train tracks along the harbor's edge to Victoria Station. The train stopped at the Lowu Bridge, in those days a narrow wooden trestle separating Hong Kong from the mainland. We disembarked from the Hong Kong train and crossed the bridge on foot. On the mainland side, I was greeted by young People's Liberation Army soldiers in baggy uniforms and was quickly taken aside by Chinese Customs officers, curious to know what was in all my trunks and boxes. I recall that, as the Chinese soldiers and Customs officers led me and my cargo away for inspection, a traveler on the train from Hong Kong yelled cheerily in a thick British accent, "Lock the Yank up and throw away the keys!" I was not reassured.

Our bilateral trade and investment with China has been the cornerstone of the US-China bilateral relationship. When I first arrived in Beijing to take up my post as ambassador in July 2001, the question that every Chinese leader asked me was, "When is the US economy going to recover?" The direct link between the United States' economy and China's economic growth and reform is clear. For 30 years, the Council has ably shepherded this critical component of our bilateral relationship through good times and bad, bringing our two great nations and peoples closer together through mutually beneficial trade and investment.

Today, under the superb veteran leadership of Bob Kapp, the Council continues to serve its members through its permanent offices in Beijing and Shanghai and, of course, through its principal office in Washington, DC. I am proud to have played a small part in the Council's history, congratulate you on your thirtieth birthday, and wish you continued success for the future.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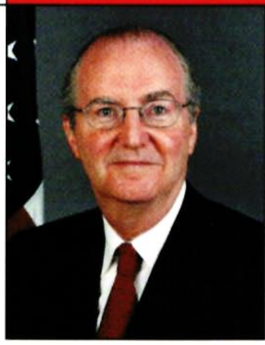

美国驻华大使

雷 德的贺词

1972年2月21日，尼克松总统抵达北京进行了历史性的访问。当他走下波音707座机时，他伸出手来，紧紧的握住了周恩来总理的手。周总理称之为历史上最长的一次握手，因为这只手越过了20年没有交往的辽阔海洋和鸿沟。30年后的同一天，乔治·沃克·布什总统的波音747座机也降落在北京。

贸易是促成1979年建交的一个重要因素。的确，周总理也要求尼克松总统在两国缺少外交关系的情况下建立一个处理双边贸易的"民间"组织。因此，三十年前的这个月，美中贸易全国委员会诞生了。1972年我们的双边贸易额为9590万美元。2002年这个数目达到了1200亿美元。美中贸易全国委员会肯定是走对了路子！

克里斯托弗·菲利普斯大使、小梅尔文·瑟尔斯、尤金·瑟罗、尼古拉斯·勒德洛和我本人都是该贸易委员会早期的先锋。我记得《纽约时报》有一篇文章宣布了该委员会的成立和菲利普斯大使的任命。当时我是法学院二年级的学生。1964年，我的父亲告诉我中国在未来将起重要作用。1968年，美国空军向我传授中文。之后我立刻向菲利普斯大使申请一份暑假工。

那份工作让我有机会就美国石化公司和中国技术进出口总公司之间的第一项技术许可交易及中国早期的知识产权问题进行了研究和报告。当中国的贸促会（美中贸易全国委员会在中国的接待单位）突然批准委员会在每半年举行一次的广东交易会（当时此交易会是中国对外贸易的一个主要渠道）设立一个办公室的申请时，我那份暑假工也转而成为一份正式工。我真的会考虑暂时离开法学院而到广州去成立设在东风宾馆的委员会的办公室，以赶上1974年的秋季交易会，之后又到北京与贸促会和八家中国外贸公司和当时驻北京的美国联络处主任乔治·布什会面？我当时可说是义无反顾。

我永远难忘1974年9月离开香港半岛酒店的那一天。我们跟着一列由一群身穿白上衣的半岛酒店的行李员所推着的手推车步行离开酒店。我们沿着火车铁轨挨着海岸边走到了维多利亚火车站。火车停在罗湖桥，在当年是一座架在把大陆和香港隔开的河上的狭窄木头栈桥。我们从来自香港的火车下来后步行过桥。在大陆这一端，几个穿着宽松制服的解放军小伙子迎着我们。我们立刻被中国的海关官员带到一旁。他们好奇地想知道我们的旅行箱和盒子里到底装了什么东西。我还记得，当中国的军人和海关官员把我和我的行李带到一边检查时，有一位从香港来的火车乘客带着很脓的英国口音喝斥说：『把美国佬关起来，再把钥匙丢掉！』我当时的心情真是七上八下。

我们与中国的双边贸易和投资是美中双边关系的基石。当我于2001年7月到北京就任大使职位时，每个中国领导人都给我提出同样的问题：『美国的经济何时复苏？』美国的经济与中国的经济发展和改革的直接关系是明显的。三十年来，无论是风平浪静之时，无论是多风多雨之时，美中贸易全国委员会都有效地维护了我们双边关系中这个关键组成部分，使我们两个伟大的国家和人民通过互利的贸易和投资更紧密的连接在一起。

今天，在柯白先生卓越和经验丰富的领导下，美中贸易全国委员会通过其在北京和上海的办事处，当然，也通过其在华盛顿的总部继续为其成员服务。我很荣幸能够在委员会的历史中起一个小小的作用。我在此恭贺你们成立三十周年，并祝愿你们在未来继续宏图大展！

THE *WJS* STOWELL COMPANY
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Christopher Stowell (left) was signing China's first Drill Pipe Joint Venture Contract with CNPC official Mr. Zhang and Jiangsu partner Mr. Xu

The WJS Stowell Company was a founding member of The US-China Business Council (USCBC) in 1973, which continues its membership and support today. Christopher Stowell, President, accompanied USCBC to host the first Chinese official delegation's visit to USA in 1977, arranged by China Council for Promotion of International Trade (CCPIT). At this celebration of USCBC's 30th anniversary, The WJS Stowell Company wishes to thank USCBC for its invaluable contribution to fostering US - China trade. At the same time, we wish to thank our Chinese friends in CNPC, Petrochina, SINOPEC, CNOOC and all of our friends working in China's oil fields for over 30 years of cooperation and business together. We have truly accomplished a lot together to build China's petroleum industry to such high levels!

美国大杰士施多威尔公司是美中贸易全国委员会（USCBC）早在1973年成立时的创始会员，并不断提供各项支持至今。而在1977年，公司总裁施多福先生就已经在中国国际贸易促进委员会的安排下，陪同美中贸易全国委员会的官员们一起接待了第一次正式访问美国的中国官方代表团！

值此美中贸易全国委员会成立30周年大庆之际，美国大杰士施多威尔公司在此衷心感谢委员会对于培育美中贸易所作的无价贡献；同时还要感谢与我们有着三十多年贸易合作关系中石油、中石化和中海油等公司以及所有中国石油工业界的朋友们。通过大家这么多年的共同努力，中国的石油工业已被发展到很高的水准！

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中国国际贸易促进委员会会长

俞晓松的贺词

值此美中贸易全国委员会成立30周年之际，我谨代表中国贸促会向30年来与我们携手共同促进中美贸易的合作伙伴表示最衷心的祝贺！

美中贸委会是促进中美开展经贸合作的先行者。从1973年美中贸委会成立到1979年中美正式建交，美中贸委会为两国贸易关系的恢复和发展作了大量工作，曾多次组织美国贸易团组访华，接待中国经贸代表团，包括贸促会代表团访美，积极促进中美进出口商之间的联系和信息的沟通。这些努力增进了中美两国人民之间的相互了解和友谊，有力推动了两国建交的步伐。

中美建交后，美中贸委会为两国经贸关系的持续、快速、稳定的发展做出了贡献，成为中美商界有益的桥梁。多年来，美中贸委会积极维护两国经贸发展的基础，为协助妥善解决两国在经贸合作中所遇到的如最惠国待遇等问题做出了不懈的努力，并支持中国加入世贸组织。这些工作无疑对中美经贸关系取得双赢具有积极的意义。

过去的三十年来，中国贸促会与美中贸委会彼此间密切合作，互相支持，互相鼓励，结下了深厚的友谊。在今后的岁月里，愿美中贸委会充分利用其在中美企业界的广泛联系和影响，以及其信息网络和专业知识，促进中美贸易和经济技术合作的进一步发展。

祝美中贸易全国委员会的工作更加兴旺。

中国国际贸易促进委员会
中　国　国　际　商　会 会长 俞晓松

二〇〇三年一月

A Message from Yu Xiaosong,

Chairman, China Council for the Promotion of International Trade

On the occasion of the 30th anniversary of the US-China Business Council (USCBC), I would like, on behalf of the China Council for the Promotion of International Trade (CCPIT), to extend the heartiest congratulations to our 30-year coworker in the advancement of US-China trade.

The USCBC pioneered the promotion of business and trade cooperation between the United States and China. Between 1973 when it was established and 1979 when diplomatic ties between the United States and China were officially launched, the USCBC did a great deal to help resume and develop bilateral trade, bringing American trade missions to China, hosting Chinese economic and trade delegations—including CCPIT delegations—in the United States, and actively facilitating business contacts and information exchanges between exporters from the two countries. All these efforts later translated into increased understanding and friendship between the two peoples and accelerated momentum toward the diplomatic relations of the two countries.

Since the forging of diplomatic relations, the USCBC has been committed to the continued, rapid, and steady development of bilateral business, making itself a salutary bridge between the business communities of the United States and China. Over the years, the USCBC has worked unremittingly to safeguard the foundations for further business engagement of the two countries, to look for proper solutions to problems cropping up in US-China business cooperation—such as MFN [Most Favored Nation] issues—and advocate for China's entry into the World Trade Organization. All these actions, unquestionably, were of great significance in achieving a win-win US-China trade relationship.

Over the past 30 years, the CCPIT and the USCBC have worked closely with, supported, and sustained each other and thus fostered a close friendship. In the years to come, it is CCPIT's most sincere hope that the USCBC will build upon its strong position and respected reputation in US-China business circles, and make full use of its extensive knowledge and expertise, to support the further development of bilateral trade, and economic and technological cooperation.

May the US-China Business Council enjoy progress and prosperity in the upcoming years!

Yu Xiaosong, Chairman
January 2003


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Reflections on Three Decades of China Business

David Tappan

David Tappan is retired chairman and CEO of Fluor Corporation, and former chairman of The US-China Business Council (1980-1981).

As our Boeing 747-400 gathered speed, rolling down the broad runway of the Shanghai Pudong International Airport, and lifted off to begin a leisurely climb to its assigned cruising altitude, I was certain of only a single fact—it was Sunday morning, October 20, 2002. I was heading home to California after a whirlwind 10-day visit to Beijing, Nanjing, and Shanghai. The sights and sounds of modern China had left me in a sort of breathless haze, suspended somewhere between the China of 25-30 years ago and the vibrant, energetic, and modern society of today.

Of course, I'd made many trips to China since the restoration of US-China diplomatic relations in 1978, but I must admit I was unprepared, although repeatedly forewarned, for what I'd just experienced. How does one adequately measure or describe the magnitude of the changes that have taken place in China in three decades, especially in the private business sector? How easy it would be to forget how different conditions were only 20 years ago and mistakenly assume that today's modern China had always existed.

However, that's not a mistake I could make, for I've been a first-hand participant in China's rapid modernization and recognize fully the staggering dimensions of China's economic revolution to date. So as I settled back in my seat for the long flight home, I couldn't help but let my mind drift back 30 years to the beginning of the US-China Business Council (then the National Council for US-China Trade) and its fledgling efforts to promote the establishment of US-China commerce. I'm sure none of us involved then could have envisioned today's reality.

In those early days, China's trading relations, like those of other countries under a communist system, consisted almost entirely of government-to-government barter arrangements. Centralized state planning determined what was to be produced and where, and at what price it was to be sold. If the Chinese Communist Party planners needed resources from abroad, a trade delegation was assembled, armed with the appropriate shopping list of domestic needs and goods which could be bartered, and dispatched abroad (usually to a member of the Communist bloc), where a trade agreement was negotiated and signed for the upcoming five-year plan. Then trade followed.

In the six years following the Shanghai Communiqué (February 28, 1972), the semi-annual Guangzhou (Canton) Trade Fair offered the only point of contact with China's procurement organization for US firms attempting to gain a toehold in that potential market. Shenzhen was the only point of entry into China, and I'll never forget my first trip by train from Hong Kong to Shenzhen, carrying my bag across the bridge over the Shenzhen River and clearing Chinese Customs and Immigration under the watchful gaze of People's Liberation Army soldiers armed with fixed bayonets. Then it was by Chinese train to Guangzhou and a General Administration of Civil Aviation of China (CAAC) plane to Beijing, or elsewhere, as arranged by one's government sponsor.

Transportation, communications, and accommodations were primitive by any standard. All activity was monitored, night and day. The government bureaucracy owned everything and operated at a snail's pace. Such common business terms as "profits" or "loan" or "interest" had no meaning to the Chinese officials with whom we dealt. Their only concern was performance under the terms of the current five-year plan mandated by the central government. In short, every aspect of what we call "business infrastructure" was missing.

Despite these formidable barriers to doing business as we knew it, contracts did get negotiated and signed, and US-China trade did start. Agreements were comprehensive because there was no body of commercial law for reference. Payment terms were excruciatingly difficult to negotiate and required Bank of China guarantees of currency convertibility, backed up by foreign bullion reserves, to be credible.

This was basically the situation in 1984, when Deng Xiaoping, then chairman of the Chinese Communist Party Central Advisory Commission, announced that China would open up to the world and reform its urban economy. Imagine the excitement! China's first reforms were agricultural: Farmers, once they had met state planning quotas, were free to sell any surplus at whatever prices they could realize and keep the proceeds themselves rather than return them to the central government. These incentives for farmers led to an explosion in farm output.

All principal Chinese leaders cautioned that opening urban markets would be significantly more complex than agricultural reform, but Deng stated that China's future depended upon taking the risk. These dramatic announcements took place during a three-day symposium sponsored by China International Trust and Investment Corp. in Beijing at the Great Hall of the People, October 4-6, 1984. Roughly 50 industrial leaders from Japan, the United States, and Western Europe were invited. David Scott, chairman of Allis-Chalmers Corp. and the US-China Business Council; Ambassador Christopher H. Phillips, president of US-China Business Council; and I, as chairman and CEO of Fluor Corp., were privileged to attend and make presentations on various aspects of US-China trade.

All of us present at the conference realized that we were witnessing a dramatic and revolutionary change (for the better in our view) in China's economic policies, and each of us had no doubt that this new direction would lead to greater foreign investment—so necessary to the country's modernization goals. Naturally, there were skeptics. Could foreign investors rely on such radical policies to remain in place long enough to realize reasonable returns on their investments? Deng stated that the new policies would remain unchanged for 50-70 years. "Were any change to occur," he stated, "it could only be that China would be open still wider." Deng further called for China—isolated from world commerce for decades—to quadruple its GNP (at that time roughly \$312.5 billion) by 2000. Though it seemed like wishful dreaming to those present at the time, by 2000 China had surpassed its target. What a stunning achievement without having the economic wheels come off! If China's GNP per capita were ultimately to equal South Korea's—surely a reasonable possibility—it would reach \$10 trillion, putting China's economy roughly on a par with that of the United States.

By the mid-1990s, the final chapter in China's transition from central planning to market competition lay in reforming its ailing state-owned enterprise (SOE) sector, long the weak link in the economy. Earlier steps to remove SOEs from under the various government ministries had begun the process. Now, China needed to complete the conversion of these organizations to stand-alone, profitable business units, as they were still a significant burden on the economy.

In 1998, China's newly appointed premier, Zhu Rongji, promised that within three years he would successfully reform these giant enterprises and eliminate their central government subsidies.

Whether that promise has been totally fulfilled is debatable, but there is no doubt that significant progress has been realized. In four years, state-sector employment in cities fell by 30 percent. Downsizing in SOEs and consolidation of small- and medium-sized state companies have streamlined operations. The state railroad system has slashed more than 4 million jobs, while the largest oil company cut its ranks by 600,000. This streamlining is essential for China to compete in the marketplace in the future. China's system of lifetime employment appears near an end.

As China passes into its second year as a member of the World Trade Organization, economic policymakers must do all they can to maintain rapid growth. Thus, both domestic and foreign private firms are needed to shoulder the major responsibility of new job creation. The hosting of the Summer Olympic Games in Beijing in 2008, and the Shanghai Expo in 2010, will fit nicely into this job-creation objective.

Of course, a great deal remains to be done if China is to realize its goals of joining the ranks of major global economic powers. In my October 17 visit with Premier Zhu Rongji in Beijing, he stressed the importance of improving air quality and enhancing the aesthetics of city life by planting trees and establishing greenbelts. Because of environmental considerations, coal mining is to be discouraged and perhaps replaced with natural gas. Overall, he emphasized that the next phase of China's development is to modernize the western region and, specifically, inland cities—formidable challenges but no more so than those previously met. All were invited to spread the word about developing western China and to participate actively in its future.

Before dozing off on the return flight, I concluded that my experiences in modern China were not part of any dream, but definitely today's reality. If I were to dream about what lies ahead for this great country, I could only predict exciting developments, perhaps far exceeding those of the past several decades. If I am right, the US-China Business Council will be very busy fulfilling its role in promoting US firms' participation in China's future. 完

亲历变化的中国

—回顾中国三十年发展历程

David Tappan曾经担任弗劳尔公司（Fluor Corporation）的主席与首席执行官，一九八零至八一年担任美中贸易全国委员会主席。现已退休。

波音747不断加速，冲出了上海浦东国际机场宽阔的跑道，渐渐上升到了正常飞行高度。飞机上的我心里只有一个明确的念头：这是2002年10月20日，星期天。在经过了10天对北京、南京、上海旋风式的访问之后，我终于在飞回加利福尼亚的途中了。今日的中国令我眼花缭乱，目不暇接。这个生气勃勃的现代社会，与25年前的那个中国形成了鲜明的对照。

虽然自1979年美中建交以来，我多次到过中国，而且每次去之前都做好了思想准备，但我却依旧被眼前的一切所震惊。要描述中国过去二十多年的变化，特别是在私营经济上的巨变，恐怕是件费力不讨好的事。今日的现代化中国几乎令人难以设想二十多年前那个中国曾经存在过。

然而，那个中国是我曾经亲眼见过的。我曾亲身经历了中国这些年迅速现代化的过程，了解中国经济的革命性变化。在飞回家的途中，我的脑海里又浮现出30年前美中贸易全国委员会的成立及其最早推动双方建立贸易关系的情形。相信当时我们中没有人会预料到今天这番光景。

在美中贸易全国委员会刚成立的那些日子里，中国的对外贸易和其他共产党国家的情况一样，基本上只是政府之间以物易物的交易。中央集权的计划经济决定生产的产品、销售地点和价格。如果共产党的计划部门需要国外的货物，就会组织一个贸易代表团，带着采购清单和可供易货的货物清单到国外去(而且去的通常是另外一个共产党国家)，为下一个五年计划签订有关合同。贸易就是这样进行的。

在1972年2月签署《上海公报》后的六年里，春秋两季的广州交易会是美国公司涉足潜在的中国市场的唯一机会。那时要进入中国只能通过深圳。我一辈子也忘不了第一次从香港进入深圳的旅途。当时，我提着行李跨过罗湖桥，在海关和入境处办手续时，手持上了刺刀的步枪的解放军士兵在周围虎视眈眈。我先是乘坐中国的列车到广州，然后登上了中国民航的客机到北京等地。我的行程都是由中国政府的邀请单位来安排的。

当时的交通、通讯、旅馆设施等无论以什么标准来看都非常原始，而且我的行动日夜都遭到监视。政府机关拥有、掌握一切，效率出奇地低。至于商业中许多平常的用语，比如“利润”、“贷款”、“利息”等等，在和我们打交道的官员听起来如同天方夜谭。他们所关心的，只是在中央政府制定的五年计划里作出成绩。简而言之，我们所说的“商业基础”那时根本不存在。

尽管按照我们熟知的方式做生意存在种种障碍，美中之间还是通过谈判签署了各种贸易合同，就此开创了双方贸易的先河。由于当时中国根本没有商业法规可遵循，签订的贸易合同几乎是包罗万象。最难谈拢的是付款方式，因为需要有外汇储备作支撑的中国银行来担保货币的可兑换性。

到1984年，情形依然如故。这年，担任中共中央顾问委员会主席的邓小平宣布对外开放，进行城市经济改革。大家可以想象人们的兴奋。中国的改革始自农业，农民在完成国家征购任务之后，不用将剩余的产品卖给国家，可以在自由市场上以市场价格出售产品。在新政策的刺激下，农业生产迅速增长。

那时，中国所有主要的领导人都提醒说，开放城市市场要比在农村搞改革复杂得多。但是邓小平认为，不冒这个风险，中国就没有未来。这番惊人的讲话发生在1984年10月4至6日在北京人民大会堂由中国国际

信托投资公司主办的一次座谈会上。来自日本、美国、西欧等地大约50名工商界人士参加了会议。有幸与会并在会上就中美贸易关系各方面问题发言的人，包括时任Allis-Chalmers公司及美中贸易全国委员会主席的David Scott，美中贸易全国委员会会长Christopher H.Phillips大使，还有当时担任Fluor公司总裁和首席行政官的我。

所有与会的人都意识到我们正在见证中国经济政策的一场革命性的巨变。(在我们看来是朝好的方向的巨变。)我们也毫不怀疑，中国经济的新方向将为外国资本带来更多的机会，因为中国的现代化亟需外来投资。当然也有人在担心这种急转弯政策是否能够延续下去，并使外国投资者能有足够的时间得到合理的回报。邓小平说，新政策将维持50至70年不变。他还说，如果变的话，就是中国要变得更加开放。他又宣称，要让与世隔绝了几十年的中国经济在2000年将国民生产总值翻两番。当时中国的国民产值大约是3125亿美元。这个当时在场的人听来象是一厢情愿的目标在2000年不仅成了现实，而且还被超越了。在经济基本保持稳定的情况下实现这一目标，的确是令人惊叹的成绩。如果中国的人均国民产值能够达到韩国的水平（这并非不现实），中国的国民产值达到10万亿，经济规模将与美国相似。

到九十年代中期，中国自计划经济向市场经济转型的最后一环剩下了老大难的国营企业。长期以来，国企一直是经济的薄弱环节。国企改革开始于让这些企业脱离政府部门的控制，中国需要将这些仍然是经济沉重负担的企业改造为独立运作的盈利企业。1998年，中国的新任总理朱镕基许诺在3年内成功改造大型国企，并要取消中央对国企的补贴。虽说就这一承诺是否完全得到了兑现还有争议，毫无疑问，情况已经有了很大的好转。在4年中，国企雇员在总就业人数中的比例减少了30%。大型国企裁员以及中小型企业改造都进行得如火如荼。国营铁路系统裁减了400万雇员，最大的石油公司裁减了60万人。中国将来要在市场经济中竞争，这类裁员是关键的措施。中国过去的终身雇佣制度正在瓦解。

中国成为世贸成员已经是第二年。经济决策者必须尽一切力量来保持快速增长。因此，民营企业，无论本国还是外资，需要担负起创造就业机会的主要责任。北京在2008年主办奥运，上海在2010年主办世界博览会，都会给中国带来新的就业机会。

当然，中国要真正成为世界经济大国还有许多工作要做。10月17日，我在中国和朱镕基总理见面时，他重点提到了通过植树和建造绿化带来改善空气质量和美化城市生活。出于环境方面的考虑，中国正在减少煤炭生产，代之以天然气。总的来说，朱镕基强调，中国下一步发展的主要目标是推动西部和内陆城市的现代化建设。虽然这是艰巨的任务，但却并不比过去那些已经实现的任务更艰巨。朱镕基希望所有人都能向世界传达中国要开发西部的信息，并且积极参与其事。

回程飞机上，在入梦之前我断定，我所经历的现代中国的变化绝对不是梦幻，而是今日的现实。如果要为这个伟大的国家设想未来，我能作的预言只是未来会有更令人振奋的发展，可能发展的程度还要远远超过过去30年。如果真是这样的话，美中贸易全国委员会在推动美国公司参与中国未来建设方面必将发挥越来越重要的作用。

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THE US-CHINA BUSINESS COUNCIL
美 中 贸 易 全 国 委 员 会

Robert A. Kapp
PRESIDENT, THE US-CHINA BUSINESS COUNCIL

The US-China Business Council Turns 30

Thirty years ago, when I myself was thirty, every American under that age knew the saying, "Never trust anyone over thirty." That dark admonition was the legacy of the late 1960s, a time when young people in many countries had grown powerfully disenchanted with the world created by their elders. The age of thirty was the dividing line; above it lay the "old regime" and the old world, beset by hypocrisy and repression. Below it lay the makers of the new world, pure, honest, and free.

I never really subscribed to that world view, even as a student in the 1960s, and once I passed the age of thirty myself I didn't see much merit in it at all.

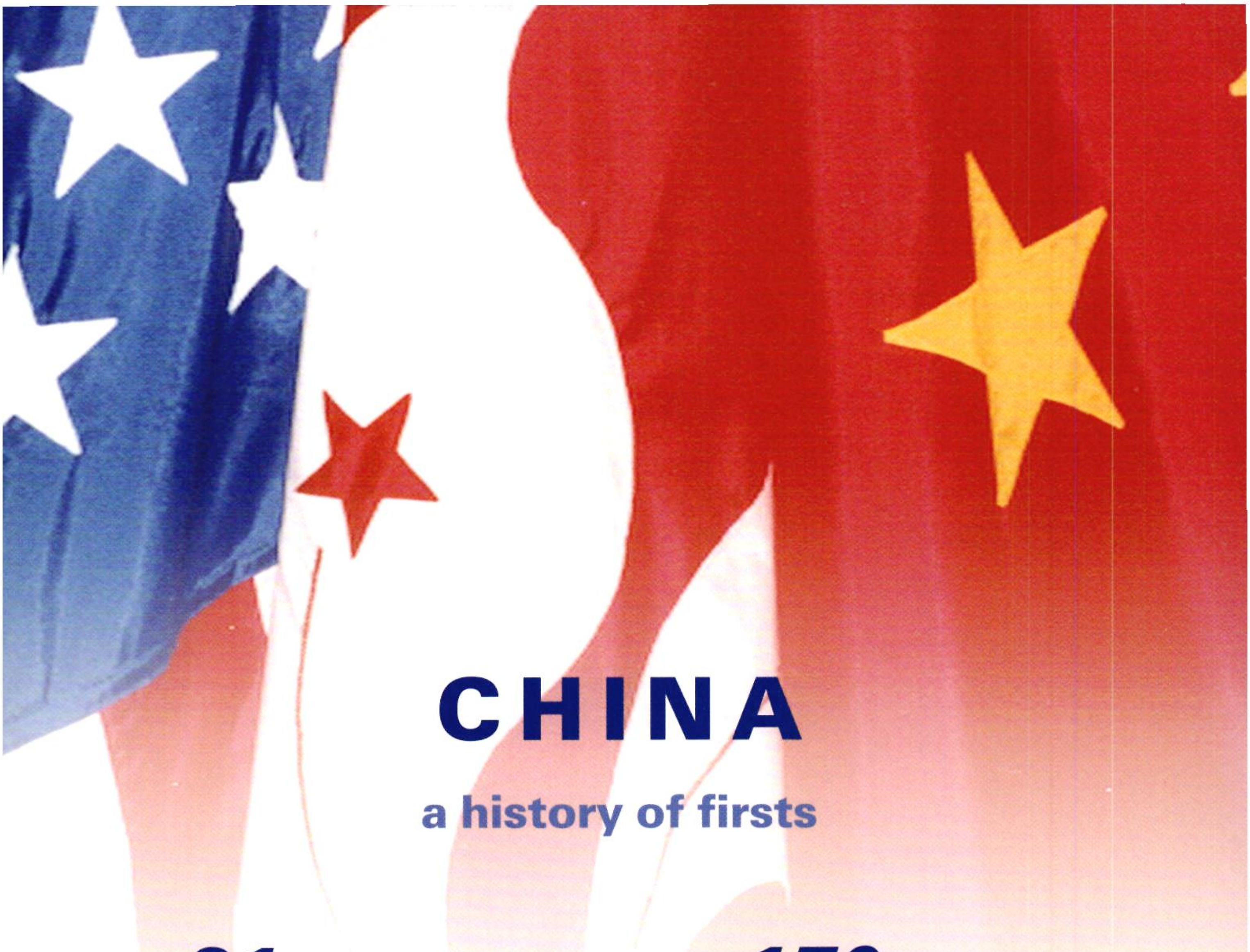
Now, thirty years later, as the US-China Business Council turns thirty, I think of the thirtieth birthday as the beginning of a rich and full stage of life. I like to think that the Council's thirtieth anniversary, which coincides almost exactly with the commencement of the contemporary US-China encounter, is an announcement of an even fuller and more productive era ahead, not only for the Council and its member businesses, but more broadly for the United States and China in global affairs.

The Council marks its birthday this spring with a visit to China by many members of its board of directors, leaders of renowned American companies that have built extensive activities in the PRC with Chinese customers, partners, and suppliers. As it happens, the Council chair under whose leadership we visit China is Philip M. Condit, chair and CEO of The Boeing Company, whose sale of ten 707 aircraft in 1972 boldly signaled the beginning of a new era of commercial engagement between the United States and China. The board's brief visit to China this spring, when new leading figures in China's central and provincial governments take up their posts, offers us a chance to reflect with our Chinese counterparts and hosts on what has been achieved thus far, and what new tasks confront us today.

It is appropriate, on this occasion, that our Council's magazine, *The China Business Review*, focus on the Council's thirtieth anniversary. In this special *CBR*, we look back, as Americans and Chinese involved in this long and complex relationship regularly do when milestones loom. But we also look forward—a riskier and more uncertain enterprise, perhaps, but one which Americans and Chinese alike need to undertake more intensely. Where are the United States and China going, separately and together, in a perilous world? What will China, now in the midst of such far-reaching economic and social changes, be by 2033? Will the intellectual and material forces in both countries that lead in the direction of convergent interests exert more weight than the forces that see friction and conflict as the inescapable destiny of our two countries? In the crude vernacular of America's western frontier, is the world "big enough for both of us"? Both in business terms and more broadly, Americans and Chinese should be thinking about such questions and seeing where and how they can contribute to greater harmony of interests between the United States and the People's Republic of China.

Now, there are different ways of looking at thirty years. If we start counting Chinese history from the beginning of the Shang Dynasty, supposedly 1122 BC, our little thirty years comes to less than one percent of the total sweep. On the other hand, three decades take up nearly 15 percent of the history of the United States.

In the context of the past century of more intensive US-China relations, this most recent thirty year period, with steadily increasing economic and commercial engagement at its core, is emerging as a longer and perhaps more stable phase than anything that came before, in spite of significant ups and downs. From the fall of the Qing Dynasty to Pearl Harbor and American


CHINA
a history of firsts

involvement in the Pacific War—29 years. From the start of the Sino-Japanese War in 1937 to the establishment of the People's Republic, with the accompanying estrangement of the United States and China—12 years. From the collapse of US-PRC relations in 1949 to the reopening of contact—23 years.

Will these past thirty years soon be interrupted by another radical change of direction? I, for one, think not. We are in a period of dynamic change, both domestically and internationally, but also of an underlying continuity that promises to endure, in spite of recurrent changes of pace. Again, the economic engagement of the United States and China, for all of its fluidity, is the key thread of continuity reaching into the future.

Look back for a moment in the other direction, from 1973 to 1943. What was happening in US-China relations in 1943? The United States and China under the Kuomintang were uneasy wartime allies against Japan. Much of China was under Japanese occupation. In 1943, the United States finally ended "extraterritoriality," the hundred year-old system that placed Americans (and other foreigners whose nations signed similar treaties with China after the Opium War) in China beyond the reach of Chinese law and came to symbolize to generations of patriotic Chinese the trauma of foreign intrusion and domination. In 1943 the great Honan Famine was petering out; millions had starved. The retail price index (1937=100) in Nationalist-controlled China passed 22,800, on its way to the 874,000,000 mark of late 1948 and the 1,000,000,000 level at the moment of regime change in 1949. Civil war lay just around the corner in China.

The three decades since 1973, when the US-China Business Council got its start, have been dynamic, and there is reason to expect that the next three decades will be, too. The emergence of China as an increasingly vigorous player in the world economy is a long process whose end is not in sight. The texture of the US-China relationship continues to change, with each side viewing the other through the prism of great-power requirements and aspirations in increasingly complex ways. The two countries have a long way to go in confronting the profound stresses that now define the human condition generally, as well as the challenges to each nation's distinctive economic and political systems.

But no one dreams of setting the clock back. The task for Americans and Chinese—in business, but especially in government and in the realm of public opinion—is to manage a future whose promise is real but not guaranteed; to pursue genuine, not simply rhetorical, "mutual benefit"; to accept the possibility that the other's interests are legitimate without discarding one's own; to prosper with, rather than at the expense of, the other. At the heart of this deepening and broadening interaction is the economic engagement embodied in the work of the US-China Business Council and its hundreds of member companies.

Our thirtieth anniversary *China Business Review* seeks to bring creative and knowledgeable writers to expound on the broad contours of US-China engagement since the US-China Business Council opened its doors, and to look to the future as well. We hope our readers in the United States, in China, and throughout the world will find food for thought, and grounds for optimism, in this *CBR's* reflections on where we have been, where we are, and where we can go in the future.

The US-China Business Council takes this opportunity to extend its deepest appreciation to the hundreds of American companies that have given the Council its life and its mandate for three decades, and to the countless Chinese friends who have worked so closely with our Council year after year. Our special thanks to our counterpart organization, the China Council for the Promotion of International Trade, which celebrated its own fiftieth anniversary in 2002.

The willingness of people of good will in American and Chinese government service has enabled us to serve our constituents and the broader cause of strengthened US-China relations; we extend our thanks and our welcome to them.

Finally, my personal thanks to all Council staff members, in Washington and in China, who serve the Council today, and to all those who have come before over three decades. The Council's soul is its great staff, and they will keep the Council strong tomorrow. 完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TOGETHER, WE SOAR.
Boeing congratulates the US-China Business Council on its 30th Anniversary. For its achievements, expertise and programs in US-China trade, we say thank you, and we look forward to the years ahead.
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THE US-CHINA BUSINESS COUNCIL
美 中 贸 易 全 国 委 员 会

Robert A. Kapp
PRESIDENT, THE US-CHINA BUSINESS COUNCIL

美中贸易全国委员会：三十而立

30年前，当我自己刚满30岁的时候，每个30岁以下的美国人都知道有这种说法："不能听30岁以上的人的话。"那是动荡的60年代后期留下来的遗产。在那个年代里，许多国家的年轻人对前辈所制定的社会规范和世界秩序感到全然失望。30岁成了分水岭：在年轻人看来·30岁以上的人组成了充满着虚伪与压迫的旧世界，而30岁以下的人拥有的则是一个纯洁、诚实的自由新世界。

哪怕是六十年代当学生的时候，我也不相信这种黑白两分法。过了而立之年，我就更觉得那荒唐不堪了。

30年后的今天，在美中贸易全国委员会庆祝而立之际，我要说的是，人过而立，生活才开始变得丰富多彩。委员会30年的历史，与美中关系解冻的历史基本同步。到了而立之年，在我看来意味着一个更为丰富、更具创造力的前途在等待着她。不仅委员会及其会员的前途灿烂，而且从更广阔的意义上看，美中两国在国际事务中也是前景辉煌。委员会成立30周年之际，不少董事会的成员、在对华贸易中与中方密切合作的美国著名公司的领导人在春天访问中国，其中包括本会主席暨波音公司的主席和首席执行官康迪。1972年，波音公司出售十架707给中国的举动，开创了美中经贸关系的先河。在这次短暂的访问中，董事会成员有机会和中央及地方一些新领导人接触，与他们共同回顾以往的发展，讨论今后的目标。

因此，委员会的刊物《美中商贸评论》(China Business Review)将委员会30周年成立纪念作为本期的主题。每当历史出现转折，那些参与了美中关系的美国人或中国人都经常会回顾这一关系那漫长而复杂的进程。这期特辑也将回顾历史，同时还要展望未来。虽然展望未来比回顾历史更不容易，但是美中双方都需要对此加以更多注意。在今天这个多事的世界上，无论是携手还是分离，美国与中国将往何处去？再过一个30年，今天这个正在经历着经济与社会巨变的中国将是个什么样子？美中两国关系最终是共同利益战胜分歧呢？或是相反？用美国西部开拓者的话来说，也就是"这个世界是否足以容纳我们两国"？无论是从狭义的商业利益还是更广义的角度，美中两国都应该考虑这些问题，并且探讨通过什么途径来促进美国与中华人民共和国之间的利益的更大和谐。

回顾过去30年能有各种不同的方式。如果我们将中国的历史从公元前1122年的商朝算起，这30年不过是历史长河的不到1%。不过，这30年却占了美国历史的 $^1/_7$ 时间。

在过去一个世纪里，美中双方有了频繁的接触。就这个世纪来看，随着双方经济与商业关系越来越紧密，这30年也就开创了美中关系历史上最具延续性的阶段，尽管这期间有过各种波折。自辛亥革命到珍珠港事件以及美国卷


MAERSK

入太平洋战争，这期间有29年。从1937年中日战争爆发到中华人民共和国成立以及美中关系恶化，这经过了12年。从1949年美中交恶到双方重新接触，又经过了23年。

那么，过去这30年的发展是否有可能又让另一次突然巨变所中断呢？我个人认为不会。我们正处于一个世界大变革的时代。变革的道路虽然曲折而漫长，但美中双边关系的不断发展却是总的大趋势。

如果我们让时光倒流，从1973年倒推回1943年，我们从当年的美中关系里看到了什么呢？中国大片土地这时沦陷于日本人的占领之下。基于抗日，华盛顿与重庆结成了不稳定的同盟。这年，美国最终废除了在中国的治外法权，从而结束了这种将在华的美国人置身于中国法律之外的制度。治外法权制度是鸦片战争后中国与西方列强条约的产物，它象征着中国被外国入侵的屈辱，一直在激发着中国人的爱国情感。这年在河南发生了严重的饥荒，数以百万计的人民衣食无着。在国统区，物价指数从1937年的100上升到22, 800，继而到1948年飙升至874, 000, 000，1949年政权更迭之际更超过了10亿大关。中国在1943年已经处于内战的边缘。

美中贸易全国委员会1973年成立。30年里美中关系的变化一直不断，而未来的30年恐怕也不会停滞不前。中国在世界经济中的地位日益上升，美中关系的内容形式也都在变化。双方都以世界大国的角度与期待来看待对方，其观察方式也日益精细复杂。在克服当今人类面临的各种深刻问题以及面对各自经济与政治体制的挑战中，两国都还有很长的路要走。

不过，谁也不希望让历史的车轮倒转。美中两国的工商界、政界、舆论界都要努力争取实现这样一个前景：使美中双边关系以追求真正的而不是表面的共同利益为基础，特别是各自在不损害自身利益的前提下也承认对方的利益。简而言之，理想的未来关系在于彼此互惠，而不是尔虞我诈。这种不断深化与扩展的互动关系的核心内容，正是美中贸易全国委员会及其众多成员所从事的双边经贸活动。

《美中商贸评论》在30周年纪念特辑中，试图汇集一批富有知识与创见的作者的文章，描绘出自美中贸易全国委员会成立以来美中关系的主线，并构想未来的图景。这期特辑展示了我们的过去、现在和未来。希望在大洋两岸与世界各地的读者能够从中找到思想的养料和乐观的依据。

另外，我们希望藉此机会，向我们的会员表示最深切的谢意。这数百家公司30年来赋予了委员会以信任与生机。我们也向年复一年与委员会密切合作的中国朋友致谢。我们还要特别感谢我们的合作单位中国国际贸易促进委员会。贸促会在2002年刚刚庆祝了成立50周年。

我们还要感谢热心帮助过我们的两国政府工作人员。他们的帮助使委员会及其会员受益匪浅。

最后，我个人谨向委员会大洋两岸所有过去与现在的工作人员表示感谢。这些优秀的员工是美中贸易全国委员会的灵魂，他们也是委员会的未来。

The State of US-China Relations

Lessons from the past, questions for the future

Lee H. Hamilton

The US-China relationship is the most complex bilateral relationship for the United States. Over the last 30 years, Sino-American relations have undergone an impressive transformation from animosity and conflict to candid dialogue and constructive cooperation. These two vast and complicated countries have found common ground on issues of trade, investment and, more recently, security. But key issues remain unresolved, and the potential for troubling divergence is real as China becomes an economic powerhouse, a military force in Asia, and a potential rival to US hegemony.

The future of Sino-American relations is fraught with questions. Will Taiwan declare its independence, or will it be integrated into the People's Republic of China? Will American missile defense trigger a Chinese arms buildup, or

Lee H. Hamilton
is director of the Woodrow Wilson International Center for Scholars in Washington, DC. He served as a member of the US House of Representatives from Indiana for 34 years and as chair and ranking member of the House Committee on International Relations and the Joint Economic Committee.

The war on terror has put the Sino-American relationship on more solid footing, but the potential for a negative turn remains.

will the two militaries strengthen their ties and cooperation? Can China's one-party system sustain itself in a market economy, or will China undergo drastic political change? Will China prove hospitable to human rights, or will it remain a rigid, state-controlled society? Uncertainty about these and other crucial questions is real, and momentous choices remain for Chinese and American leaders. If the last 30 years are taken as a guide, the leaders of tomorrow can best face these challenges by constructively engaging in pursuit of common interests.

The economic ties that bind

Overlapping interests between the United States and China have been predominantly in the economic sphere. China's drive to become an economic power has been simply astonishing. Growth rates have frequently approached 10 percent per year over the past 10 years, and in 2002 China was the recipient of more than $50 billion in foreign investment. There are now 2 million private companies in China, an emerging middle class, and ambitious infrastructure development projects. China is a global center for manufacturing and a regional economic power, particularly since the Japanese economy has stalled. This level of economic openness and growth in China was unthinkable 30 years ago and owes much to the relationship between the United States and China.

On trade and investment, there has been considerable common ground and many areas of mutual interest between the two countries. The United States has pursued commercial opportunities, exports, and profits in China; China has sought US investment, technology, and support for Chinese accession into global trade regimes. US support for trade and investment in China has matured from Most Favored Nation status in the 1980s and 1990s to China's integration into the World Trade Organization (WTO) in 2001. China has in return demonstrated a willingness to open up its state-owned economy, dramatically reducing tariffs, overhauling laws and regulations, and permitting greater private ownership, property rights, and transparency.

China still has a long way to go in reforming its economy, however. China's WTO compliance record so far is mixed, and it must continue to improve protection of intellectual property rights, remove import quotas on agricultural goods, eliminate regulations that discriminate against foreign products, and establish more efficient and vigorous independent regulatory agencies. China is also faced with ongoing problems with inflexible state-owned enterprises, bad loans in state banks, unfunded pension systems, and widespread corruption. But today's vibrant and developing China still bears little resemblance to the economy of the early 1970s. The ties afforded by this development have bolstered Sino-American relations beyond the balance sheet: Americans and Chinese now do business together, travel to each other's countries, indulge in common sports and entertainment, and shop for the same name brands.

Though economic cooperation has been increasingly robust, the lack of political reform in China has proven to be an impediment to strengthening Sino-American ties. The Chinese Communist Party (CCP) has opened the economy while maintaining a one-party state in which power is concentrated in a few dozen individuals, and dissent has been repressed. China is undergoing a stunning modernization, but ordinary Chinese have very little say in the process. This balancing act has raised difficulties as the incompatibility between a free market and one-party rule becomes evident; China could be approaching a crisis in governance, with a decay in the Party's authority, a deteriorating state capacity, and rising tensions between the regime and society. To many observers, it appears that China has to implement some strategy of political reform without delay, including legislative measures, legal system elections, and an empowerment of civil society. But the CCP is both determined and resilient, and the choice between working with a largely repressive entity or encouraging potentially destabilizing dissent has proven difficult for American policymakers.

Political reform

The United States has struggled to advance the cause of human rights and political reform in China. We have tried private diplomacy, public criticism, and economic sanctions—none of which have had particularly satisfying results. Human rights of all kinds in China—civil, political, women's, religious, and ethnic—remain among the most restricted in the world. The issue is a difficult one because Chinese and Americans approach it from different perspectives. Americans see a stultifying authoritarian government that denies—sometimes brutally—universal rights and freedoms; many Chinese counter that economic and social rights are more important than political freedoms, and that the economic progress of the last 25 years therefore represents an impressive advance of human rights. The growth in economic openness presents an opportunity for human rights in China—as new people and ideas flow across the Chinese border, the potential for accompanying political and social change grows. But until there is real political change in China, human rights will persist as a glaring concern for Americans and American policymakers.

Security

Other areas of concern for Chinese and American policymakers are principally in the security arena. Chief among these is the future of Taiwan, which remains the most volatile point of tension in the US-China relationship. China has been persistent in its claim on Taiwan, simultaneously pursuing military buildups across the Taiwan Strait and closer links in commerce and trade with the island. The United States formally embraces a "one-China" policy, and, despite statements made early in the Bush Administration, we have generally maintained strategic ambiguity with regard to Taiwan—we have dissuaded Taiwan from declaring independence, while keeping China guessing about a US response to an unprovoked Chinese offensive.

Taiwan arouses passionate and historically rooted sentiment on both sides, and this has periodically led to inflamed rhetoric and escalated tensions. A principal goal on both sides has been—and should remain—the avoidance of military conflict over Taiwan. The United States should avoid provoking China over Taiwan, and China should not pursue military coercion in seeking to unify the island with the mainland. The future of Taiwan remains in question, but it is a question that should be worked out quietly—not through war, but through negotiation, commerce, and the passage of time.

Another area of concern between the United States and China has been in weapons technology and proliferation. China is one of a few nations with the ability to inflict great nuclear harm on the United States, and has pursued a minimum nuclear deterrence capability. The United States has also accused China of exporting dangerous weapons and missile technology to countries like Pakistan and North Korea. Tensions have ebbed somewhat, as the 1990s saw the successful incorporation of China into several nonproliferation regimes, and China has recently announced a plan to limit its exports of missiles and other dual-use technologies. But US plans to build a missile defense system and China's goal of upgrading its nuclear capability ensure difficult times ahead. China will be provoked by any US attempt to eliminate its deterrence capability through a missile shield, while the United States will oppose a nuclear arms buildup in East Asia. Potential flashpoints such as the Korean peninsula and Taiwan could further complicate the situation. Dialogue between the military and civilian leadership of both nations is necessary to ensure that misunderstanding and mistrust do not escalate into something more dangerous.

The potential for a successful and sustained dialogue has been somewhat strengthened since the war on terrorism recast the US-China relationship. The common strategic concern of terrorism has led to tangible cooperation: Chinese support for the US-led campaign in Afghanistan,

intelligence-sharing, and US support for the Chinese crackdown on Islamic separatists in China's western territories. There is also a warmer tone between the two nations as of the end of 2002, as the United States has renewed military-to-military ties, and China supported the United Nations resolution on Iraq and has pledged cooperation in defusing the crisis in North Korea.

PRC President Jiang Zemin made it a priority to demonstrate enhanced relations and cooperation between the United States and China in the war on terror as China moved toward a change in leadership. In the coming months and years, incoming President Hu Jintao and the new Chinese leadership must resolve internal differences—if any—and formulate their own approach to the United States and foreign policy. It remains to be seen how this approach will differ from Jiang's approach, and to what extent Jiang will remain involved in diplomatic and security matters. For the time being, China seems to have accepted the reality of US preeminence, and the Bush Administration has decided to focus on working with China on areas of common concern.

Building on a strong, yet uncertain, foundation

The war on terror has put the Sino-American relationship on more solid footing, but the potential for a negative turn remains. One event, such as the downed spy plane or a statement by Taiwan's President Chen Shui-bian in favor of independence, could swing relations in the other direction. This instability remains a flaw in the relationship, and in US policy toward China in general.

The United States must have a multifaceted policy toward China because of the diversity of US interests regarding China. Too many Americans tend to think about the US-China relationship in terms of a single issue, such as trade, Taiwan, or human rights. Without diminishing the importance of these specific issues, American policymakers should not allow any one of these issues to dominate, drive, or derail the entire relationship. With so many questions ahead, there will surely be difficult times and differences of opinion. China is a vast and diverse country and economy, with a future that may be marked by both development and upheaval. If we pursue a policy that reflects the breadth of common interests between the two nations, then we can avoid the tumult that has afflicted relations between the two nations over the last 30 years.

The United States should always speak up for its interests and values in dealing with China—in commerce, international security, and human rights. But we should not fear a strong and prosperous China—the surest way to make China an enemy is to treat it as one. Despite serious and persistent differences, China and the United States have been able to construct a relationship that has benefited both countries and increased the stability of Asia and the world. Expanded ties and cooperation allow a flow of ideas that can break down mistrust and misunderstanding of China in the United States, while encouraging growth and, potentially, political change within China.

The future of China is the great unknown of the twenty-first century. The vital task for the United States is to encourage China to move toward greater prosperity, freedom, and international cooperation, while acknowledging China's important and evolving role in the world. The United States and China continue to alternate between connecting and colliding on a great many issues. If both sides commit themselves to engagement, then the United States and China can build on the foundation of the last 30 years to forge a relationship characterized by depth, candor, and common interest. 完

What Will the World Gain from China in Twenty Years?

Wang Zhan and Huang Renwei

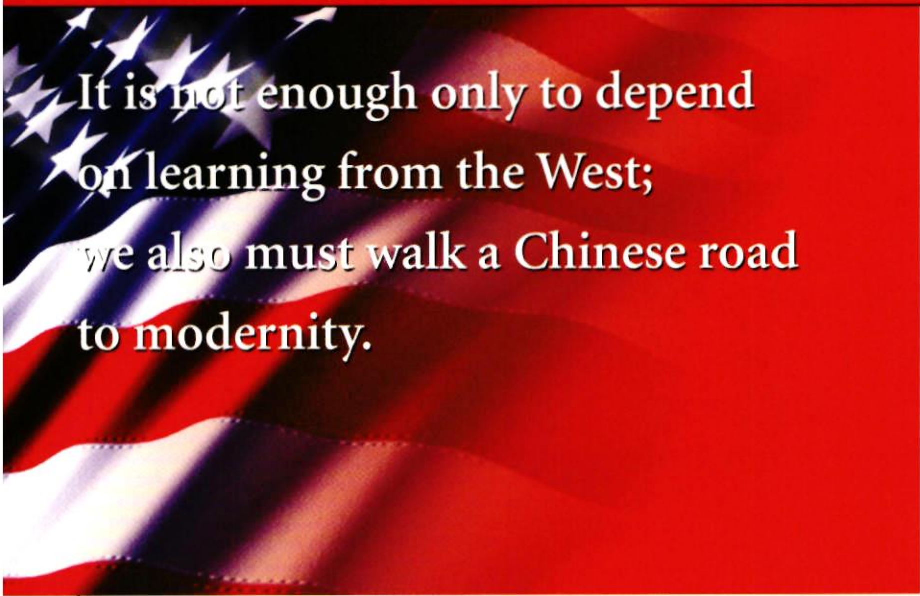
China has only been carrying out its "reform and opening" policy for twenty years. It has only trod the path of the market economy for ten. The changes that have swept China were unimaginable twenty years ago. The changes to take place in the coming twenty years are even harder to imagine.

In predicting the future one can't escape the question of history. For 200 years, from the end of the eighteenth century, China time and time again missed its historical opportunities to modernize. The three industrial revolutions of the West left China behind, until the Chinese nation finally came to the brink of extinction. In the name of their independence and freedom, people in China looked to the West to learn about technology, social and political systems, and culture, but nothing worked.

Wang Zhan
is president, Shanghai WTO Affairs Consultation Center.

Huang Renwei
is director, Pudong Institute for the US Economy.

This article was translated and adapted from the Chinese.



It is not enough only to depend on learning from the West; we also must walk a Chinese road to modernity.

When we sum up the lessons of China's 200 years of accumulated backwardness, the first is that China lacked independence and autonomy in the world. The second is that China lacked a system, and a spirit, of innovation.

The real opportunity to learn from the West has come to the Chinese people only in the last 20 years. "Reform and Opening" and the socialist market economy—these have opened for China a new pathway to innovativeness in the Chinese system, in technology, and in culture. What the most recent 20 years prove is that if China wants to modernize, it must innovate, and that in order to innovate, China cannot but learn from the West. Modernization, innovation, and learning from the West are neither separable from, nor contradictory with, one another. If we want to make the nation strong, if we want the two sides of the Taiwan Strait to be united, first we must innovate—we must create the new. We must continue to learn from the West. China's people must say clearly to the world: China is already taking the path of modernization, marketization, democratization, and globalization. There is no turning back. We can only advance. We cannot retreat.

In looking to the future, one likewise must not ignore the circumstances of today. Simply put, what we are embarked upon today is a kind of paying of overdue bills incurred in the past. To achieve that, it is not enough only to depend on learning from the West; we also must walk a Chinese road to modernity. China has 5,000 years of civilization behind it, but it bears the historical burdens of overpopulation and a deteriorating environment. The 1,200 years of increasing population ever since the Tang Dynasty [618-906 AD] created a wave of ecological exhaustion spreading north and south from the Yellow River valley. The Qing Dynasty [1644-1911] carried out a policy of exclusion and isolation from the rest of the world, with the result that the relatively high level of commercial economy and foreign trade achieved by the preceding Ming Dynasty [1368-1644] was smothered. In the first 30 years after the People's Republic of China was founded, the sudden advances we made in economic construction worsened the population, ecology, and resources problems while the gap widened between China's and the world's development. Today, China accounts for 8 percent of the world's cultivated land but must sustain 22 percent of the world's population. With only one-fifth of the population of China, the United States enjoys three times as much arable land, and its farmland has only been under human cultivation for one-tenth of the time that China's land has been worked.

China's historical burden is simply very difficult for Americans to grasp. It is a heavy load, which makes navigating China's ship through the seas of history extremely difficult. To promote a ceaseless improvement in the quality of life of the Chinese through the basic processes of preserving the very existence of the populace, distributing precious resources, and restoring China's ecological environment—this is what we of the present and future generations must face.

Time and space determine the existence of any system as well as the degree of freedom to reform any system. To meet the basic challenges of living standards for the world's largest population, in a highly constricted space, means not only solving problems of clothing and food, but having the power to improve the quality of life: the power to receive a modern education, for example, as well as information, health, housing, entertainment, and so on. To this end, China must all at once create a progressive model that weaves together collectivism and individualism; melds efficiency and equity; builds both law and democracy; and combines reform at the top with change at the bottom.

China, after all, is not without its own proof of the price of excessive "democracy." The ten years of the Cultural Revolution are evidence of those unbearably painful costs. And it is not as though China has never explored turning power from central authority over to local powerholders, either: the uncontrolled chaos of the "Warlord Era" in the first part of the twentieth century was a dark blot in our history. If China were to return to "Big Democracy," as it was called during the Cultural Revolution, or to warlord division of our territory, an estimate of several hundred million refugees on the move would be conservative.

Thus, to the people of China, the most persuasive option is to take a gradual approach to the building of our systems and to the orderly replacement of our institutions. This is, moreover, China's commitment to the people of the world. China's growth over the past twenty years makes clear that our path has been a rational choice for China in light of China's own conditions. In the twenty years ahead, China will continue to walk this pathway toward systemic development.

Urbanization, critical to changing the structure of China's immense population, is the key to China's modernization, its marketization, and its democratization. We simply cannot conceive that a society in which two-thirds of its population work as farmers, and in which two-thirds of farmers live in villages with people bearing the same family names, can be a society with highly democratic politics. Nor can we imagine that a China in which income and living standards in city and countryside vary by huge orders of magnitude can hope to retain a stable social structure. China cannot hope to keep one part of its economy, in which more than half of the labor force works as self-employed farmers, fully integrated with the other part of the economy that is more globalized. China's industrialization, its modernization, and its internationalization will all take shape according to the degree of China's urbanization. The so-called "well-off society" [which, since the recent 16th Party Congress, is on everyone's lips,] must be seen for what it is: a society that has fundamentally urbanized.

Thus in the twenty years ahead of us, the process of urbanization will accelerate. The process will radically change the model of economic growth and individual consumption behavior in China and finally alter the values and worldview of the Chinese people. As urbanization proceeds, the Chinese economy will once and for all move away from supply-dependent growth and into a pattern of development pulled forward by effective demand. The populace, driven above all by the core urban consumer population, will create a consumer economy with the greatest potential in the world, its magnitude may reach several trillion US dollars.

At the same time, a Chinese private capital market dominated by an urban middle class will take form; its size will dwarf the combined investment powers of today's Chinese governmental and foreign investors.

Urbanization will bring with it the systematic development both of transportation and information networks and will make possible for the first time the orderly physical movement of vast numbers of Chinese people within the country. The household registration system, which evolved in China over millennia, fixed the population according to place, on the land. Urbanization will decisively relegate this traditional system to history.

In China's most highly developed areas—the lower Yangzi River delta, the Pearl River delta, and the Beijing-Tianjin-Bohai region—we will see the emergence of three great "urban spheres" whose 5 percent of China's total land area and 20 percent of total national population will

As urbanization proceeds, the Chinese economy will once and for all move away from supply-dependent growth and into a pattern of development pulled forward by effective demand.

account for 65 to 70 percent of China's total GDP in twenty years. Drawn forward by these huge urban powerhouses, central and western China will produce their own respectable urban belts and concentrations of cities.

As half of China's population enters these highly developed urban environments, large portions of China's land and exhausted ecology can be allowed to rest and recover, and the environmental debts incurred over thousands of years can gradually begin to be repaid.

As its structure is thus transformed from a peasant core to an urban core, Chinese society will also move in the direction of a democratic society.

The nature of the tasks bequeathed to China by its development for the coming 20 years have already ordained that China will pursue a foreign policy of peace. China needs a stable international environment, including both stable borders and stable global markets. All international conditions that are favorable to stability and economic development will be actively supported by China, which will promote their constructive outcomes to the fullest possible extent.

At the very least, to link China's strength with the "China Threat," can be said to be ignorant of Chinese psychology and culture. Admiral Zheng He, in the Ming Dynasty, led what was at the time the largest fleet the world had ever seen on voyage after voyage into the Indian Ocean, but not once did his missions seize an inch of territory. Today's Chinese people understand even more clearly that China's development hinges on world peace and world development—that China's interests must help the interests of other countries, and that its security cannot be achieved at the cost of making other countries fearful. This is the meaning of the twin Chinese concepts of "Common Interests" and "The New Concept of Security," which will in coming decades define China's international conduct and identity.

China's commitment to international regimes and international rules will become even firmer in the decades to come.

The more the Chinese economy advances, the greater its dependence on the global market, and the greater the importance of its cooperative integration with the world's developed nations. China's commitment to international regimes and international rules will become even firmer in the decades to come.

In a similar way, a peaceful solution to the Taiwan problem can only be found through the process of China's own development. In recent years, the Chinese mainland and Taiwan have become conspicuously economically interdependent. The vertical industrial division of labor between the two sides is being replaced by a horizontal one. The movement of people has become huge; in Shanghai and the lower Yangzi delta region alone, several hundred thousand people from Taiwan now make their long-term residence. Taiwan's massive trade surplus with the mainland has already become a key source of Taiwan's foreign exchange reserves.

If we imagine that the two sides will carry out their "Three Links," we can see that the cost in time and money of trade between the two sides will plummet. According to World Trade Organization rules, Taiwan must open its investment markets and real estate markets to PRC investors; we can thus foresee large numbers of mainlanders going to Taiwan for visits or for long-term residence, and we can certainly envision much larger numbers of students from Taiwan heading for the mainland for academic degrees and training. The level of mutuality between Taiwan and the mainland will come to far overshadow the old relationship, with its characteristic preoccupation with the "two sides of the Strait."

Thus Taiwan's future lies in economic integration with the Chinese economy and in peaceful reunification. Confrontation and conflict between the two sides does not agree with the common interests of the people. We can speculate that twenty years from now the Taiwan Strait will not be a moat separating the people of Taiwan and the mainland from one another. Instead, airplanes may fly more frequently between Shanghai and Taipei than between mainland cities. Unification could happen by means we cannot even imagine at this moment. This historic transition will be a mixture of the gradual and the sudden.

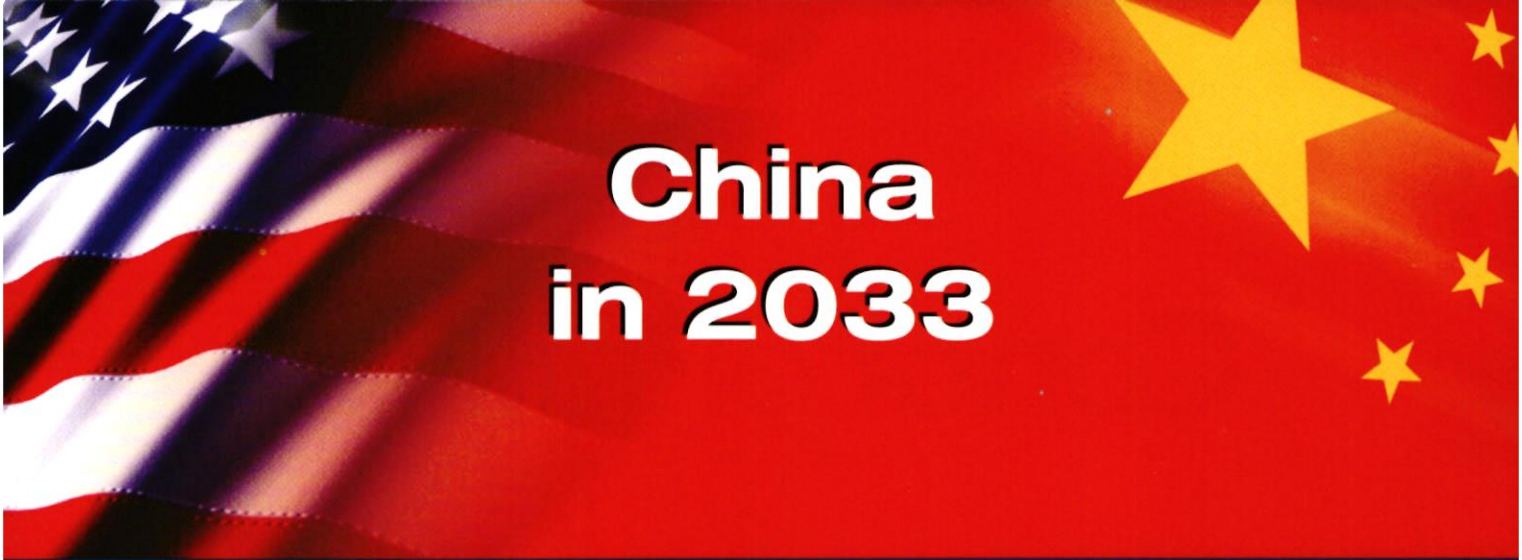
We should not deny that in the next twenty years China might face difficulties and challenges even greater than those of the last twenty years. The increasing diversification of interests within Chinese society could reduce the ability of political authority to control society. Divisions between rich and poor could cause new conflicts pitting class against class. Popular demands for greater political participation will ensue as people's economic well being increases.

All of these will create pressures for reforms of China's internal political structures and will, at the same time, impel such changes. As cross-Strait economic relations continue to deepen, failure to break the political impasse between the two sides could trigger a very serious crisis in the Strait. But such a crisis could itself become the vehicle of China's unification. The international political and economic influence stemming from China's rapid growth may have the effect of inducing deep changes in the pre-existing international order. New trends may emerge in the relative distribution of the world's markets and energy resources. The "status quo powers" may turn out not to be so naturally able to respond to these changes. China must learn the rules of this fluid and changing game in order to meet its international needs.

In short, economic and social transformation, dangers in the Taiwan Strait, and all sorts of international perils are the constant accompaniments to China's forward progress. But numerous international strategic thinkers have failed over and over again to see that the breadth and depth of China's development far exceed the constraints, and that in the course of China's development to date all sorts of lurking dangers have already been put to rest. This is why their predictions about the "collapse of China" and the "China threat" have missed the mark time and again. And Chinese strategists, for their part, read these gloom and doom predictions, take appropriate notice of the reasonable elements in such analyses, and thus are better able to avert strategic errors and frustrations.

What is needed is simply this: the uninterrupted continuity of China's market opening; the uninterrupted reform of China's basic systems; the Chinese people's continuing and uninterrupted innovativeness; the inevitable continuing progress and development of Chinese society; and the inevitable increase in the benefits that the world will draw from China's own improved fortunes.

That is the gift that China, over the next twenty years, can offer to the world. 完



China in 2033

What will China look like in 30 years?

Kenneth Lieberthal

China in the past quarter century has made astonishing progress toward economic development, market transition, and major power engagement in the international arena, and the pace of domestic transformation appears to be accelerating with World Trade Organization (WTO) implementation. Beijing has the ingredients necessary to sustain impressive growth through the coming three decades, but only if it effectively addresses the major domestic and international obstacles identified below. Success would mean that China in 2033 could become the second most powerful country in the world.

Kenneth Lieberthal
is professor of political science and William Davidson professor of business administration, and director of the China Program of the William Davidson Institute at the University of Michigan. He served as special assistant to the president for National Security and as senior director for Asia on the National Security Council during 1998-2000.

If all goes well from Beijing's perspective, China will be the dominant local power in Asia in 2033, with India as its only counterbalance within the region.

A successful China

If all goes well from Beijing's perspective, China will be the dominant local power in Asia in 2033, with India as its only counterbalance within the region. It will also be a major global player, with one of the world's largest and most vibrant economies and with a population age profile compatible with sustained growth and military power.

Should China achieve an average GDP growth rate of 6 percent per year in constant dollar terms, as of 2033 it will have a GDP of $6.95 trillion (in 2003 constant dollars at the current exchange rate). This level of GDP will make China a wealthy country in aggregate terms. But with a per capita GDP of only $4,600—in a world in which excellent communications bring knowledge of advanced standards of living into even remote areas—Beijing will face tremendous pressure to maintain strong economic growth to enable a population of more than 1.5 billion people to live well.

In comparison, assuming US GDP growth of 2.5 percent per year, America will have a $21 trillion economy in 2033. China will have progressed a long way, with great consequences for international economics, politics, and security, but it will still have less than one-third of America's GDP while having about five times America's population.

In 2033, China should still be a low-cost manufacturer in the regional and global economies. Ongoing migration from the interior will keep at least a portion of coastal production competitive in terms of labor costs, and Beijing is already making infrastructure investments to move industry inland as labor costs on the coast rise.

In 30 years, China will also have developed areas of excellence in high value-added, high-technology sectors, and some indigenous Chinese firms should by then be major global competitors. It is too soon to pinpoint the specific sectors in which China is likely to excel, but it has a natural regulatory advantage over Western countries in pushing the frontiers of research in some promising areas such as biotechnology. A great deal will depend on where investment funds flow.

In security issues, China will have the resources to sustain a defense budget second only to that of the United States, a population young enough and large enough to field a military of substantial size, and the technology necessary to remain relevant in a high-technology security environment. China's population growth and age pyramid will serve it well in comparison with most other countries in this regard. Of the major powers involved in Asia in 2033, only the United States (because of immigration), India, and China will have growing populations with age pyramids better balanced than that of Florida in 2003. This fundamental demographic reality will adversely affect the ability of the other industrialized countries engaged in Asia to devote large-scale resources to security (versus welfare) and to field major military forces.

Key hurdles

The above portrait assumes that China will successfully clear the key hurdles it faces between now and 2033. This will demand major initiatives and difficult choices. The core challenges are as follows:

- **System transformation**

The information revolution, marketization, increasing wealth, and a vastly loosened political straightjacket are already widening the gap between the responsiveness of China's political system and the demands of a more self-aware society. The challenge of making the political system more responsive will become far more important in the coming decades, forcing Beijing to adopt more fundamental reforms than its numerous current efforts to improve party and state administration.

Maintaining a 6 percent annual growth rate for several decades will require deeper transformation to a market economy, but even the initial stages of market transition to date have highlighted the necessity of changing and enhancing the government's systemic capacities. At a minimum, China's officials will have to develop a new social compact that meets the growing aspirations of the population for political input while maintaining sufficiently strong executive capabilities to concentrate resources to address major issues.

That system must incorporate, and respond to, the interests of the poor, as well as resonate with middle-class and wealthy individuals and officials. This new social compact will also have to reduce the strains with China's minorities, especially among Muslims and Tibetans.

The Beijing-Tianjin area cannot continue to grow even beyond the end of this decade without major new sources of water, in addition to far greater efficiency in water utilization.

Otherwise, terrorist, separatist, and independence forces could threaten national cohesion.

The only type of fundamental stability that can be sustained, therefore, is the dynamic stability that comes from institutional change that keeps pace with the rapid social and psychological changes that reforms are continuing to unleash.

In years past, Beijing delivered social services to city inhabitants primarily via state-owned enterprises (SOEs), and it used a household registration system to constrain sharply the ability of peasants to move into urban areas. The reforms of the last three decades have dramatically reduced the percentage of urbanites who work in SOEs, created labor mobility, opened up increasing opportunities for rural-to-urban migration, and produced substantial underemployment and unemployment as SOEs furlough and lay off workers. All of these phenomena will increase greatly, especially in the coming two decades.

China must therefore develop government-based, rather than enterprise-based, social safety net provisions: health coverage, pension plans, welfare payments, unemployment compensation, and so forth. The current financial system provides inadequate opportunities for low-risk investments of insurance and pension funds. And the present tax system does not effectively tap the wealth of the rapidly growing private sector for public purposes.

Developing such a social safety net is thus a complicated and expensive process. Though PRC leaders recognize this fact and are experimenting with numerous systems, the country is changing so rapidly that the government lacks reliable models of likely urban population growth, configuration, and needs. The additional urban influx from the countryside will range between 150 and 300 million people by 2033, but the pacing and ultimate magnitude of this mass migration is unclear to China's planners. What is clear is that China will have to cope with a very rapidly growing population of city dwellers demanding social services for decades to come.

In short, China must develop a great deal of institutional capacity in order to cope with the type of urban society that is well on its way to realization. Significant failures to develop this capacity can undermine the country's social stability and economic progress.

Burgeoning bad debts and ongoing deficit spending have added major financial restructuring to the systemic issues that must be addressed. Competition for the funds to resolve the debt issue, to address social safety net development, and to deal with the environmental and security issues explained below will require improved institutional capacity to make and implement decisions on very difficult trade-offs.

China's political system must thus adopt key institutional changes that address the responsiveness, quality, and reach of the country's public institutions. Increasing overall sophistication and urbanization will require major reconfiguration of the political system itself and of the basic linkages between that system and the population, all without raising unrealizable popular expectations.

● The environment

Environmental constraints could seriously disrupt the growth trajectory that underlies the year 2033 description above. The north China plain has, since around 1960, seen its water table drop by roughly three feet per year. Severe water shortages plague this entire area. Subsidence, increasing soil salinity, and other problems are already becoming acute, and global warming will exacerbate them. The Beijing-Tianjin area cannot continue to grow even beyond the end of this decade without major new sources of water, in addition to far greater efficiency in water utilization. In many areas of China, declining water quality, shrinking lakes, spreading deserts, and disappearing ground cover are challenging the sustainability of even current population levels and land use.

Air pollution also poses dramatic challenges. China already contains nine of the world's 10 most polluted cities. Chronic respiratory disease has become the leading cause of death in the country. Acid rain afflicts roughly one-third of the arable land, and dirty air and water present growing problems for various types of manufacturing efforts.

China's air pollution stems primarily from its reliance on coal for energy. Despite efforts to increase energy efficiency and diversify energy sources, as of 2033 China's carbon emissions will be more than 300 percent of present levels, with coal contributing nearly 70 percent of this figure.

China thus faces severe environmental challenges that will, at a minimum, require costly investments and substantial population movements. At worst, these challenges may make it impossible for sections of the country to continue to grow or even to support the populations that now live there. Large-scale environmentally induced tears in the social and economic fabrics and resulting migrations cannot be ruled out.

- **National security requirements**

The Asian regional security situation will change by 2033. If China is successful, it will be the most powerful Asian country. The Korean peninsula will almost certainly no longer be divided. Japan's relative strength will decline. India's regional position and influence will grow. The United States will likely still be the strongest actor in the region militarily. All other Asian countries will take these basic changes into account in structuring their foreign and security policies.

A "successful China" scenario will only come to pass if Beijing achieves three security objectives over the next three decades. First, it must avoid a major war. Second, it must reach a peaceful resolution (even if in the form of a long-term *modus vivendi*) with Taiwan. And third, it must manage its relations with the United States in a way that allows it to avoid pouring funds into outsized defense budgets. These three are related, and failure in any one would arguably increase the chances of failure in one or both of the others. China's present leaders are correct, in short, when they assert that the country must avoid major international conflict if it is to realize its fundamental economic and social objectives over the coming three decades.

China's success over the next 30 years is by no means certain. Managing foreseeable problems will require astute decisionmaking, along with some luck. Additional debilitating challenges, such as the potential spread of HIV/AIDS to several tens of millions of citizens, would reduce the margin for success. And currently unpredictable obstacles are bound to arise and add to the difficulties.

Alternative futures

Given the above uncertainties, the realistic array of possibilities for China's system as of 2033 remains wide enough to be sobering. Taking into account the potential for various types of failures, in broad terms there are five possible configurations for China in 30 years:

- **A successful country that has domestic political and electoral competition, but probably with one party dominating the system at the national level** (possible variants might look like the Mexican Partido Revolucionario Institucional before the 1990s, the Kuomintang on Taiwan at the end of the 1980s, or the

China's success over the next 30 years is by no means certain. Managing foreseeable problems will require astute decisionmaking, along with some luck.

Japanese Liberal Democratic Party since the 1950s). This China should boast vibrant markets, a strong state economic role, impressive qualities of government administration, a more effective legal system, and success in government programs to reduce regional and social inequalities. It will have a high savings rate and over additional decades should become more fully democratic.

- **An authoritarian one-party system that is closely linked to domestic business elites and keeps the lower classes engaged through promoting nationalist commitment.** This would be the likely result if China manages well all the above challenges except in the security arena.
- **A soft and corrupt authoritarian system.** In this system, government predation would hold down the rate of growth, diminishing China's international stature and power. The authoritarian system would be devoted largely to keeping itself in power and serving the material desires of officials and their business cronies. Failure to address effectively the current sources of corruption and to improve the legal system would increase the risk of this outcome.
- **A weak democratic system.** This could result if unmanageable popular demands produce a breakdown of the political system itself. This system might prove too institutionally weak to direct scarce resources to economic growth, environmental protection, and security. China could become in 2033 in some ways similar to Indonesia in 2003.
- **Prolonged fundamental instability.** This nightmare scenario, likely triggered by open elite division at a time of financial or other crisis, would make China look in basic ways like Russia of the mid-1990s, including potential loss of major territories, a contracting economy, shrinking life expectancy, environmental degradation, unmanageable ethnic divisions and conflict, institutional inability to control domestically based transnational criminal activities, terrorism, proliferation, and illegal migration. This is the possibility that has the greatest adverse consequences for the international arena.

China's future lies primarily in its own hands. Astute, forward-looking decisionmaking can steer the country through the above shoals to the "successful China" outcome described above.

China is too large and complex for America to play a major role in fostering its success, although offering open markets, technical advice, and security cooperation would be helpful. More important, US actions that dramatically worsen China's trade and security environments could have a big impact, increasing the chances that one of the final four scenarios will come to pass. Which one of the four would occur, though, is beyond America's ability to determine. 完

How Will China Build a Well-Off Society for All of Its Citizens?

Hu Angang

The 16th Chinese Communist Party (CCP) Congress reported in November 2002 that China has become a well-off society overall but that the nation's development level remains low and unbalanced. To begin a discussion of this issue, we must answer the following questions: What is a "well-off society"? What are the indicators of such a society? How does a vast country like China build a well-off society for every citizen, given its existing regional and developmental disparities? What are the main points of focus and main obstacles to building such a society?

The notion of a "well-off society" *(xiaokang shehui)* was first raised by Deng Xiaoping. In December 1979 the visiting Japanese prime minister, Ohira Masayoshi, asked Deng in Beijing: "What will China's future be like?" and "What is the blueprint of its modernization?" Deng used the term "well-

Hu Angang
is a professor at Qinghua University's School of Public Policy and Management, and director of the Center for China Study at the Chinese Academy of Sciences in Beijing.

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off society" to describe the future. Shortly afterward, he indicated that China will have achieved a well-off society once China's per capita GNP reaches roughly $1,000. According to Deng, China would be able to approach the level of the developed world by the mid-twenty-first century. At China's current level of development, "well-off" indicates a living standard between survival and affluence.

What, then, is an "all-around well-off society"—that is, a society where the wealth is evenly distributed among all citizens? It was explained at the 16th CCP Congress that such a society should promote the development of the economy, democracy, culture, social harmony, and prosperity. Many methods can be used to calculate whether a society is well off. At least four important indicators can be used: per capita income, Engel coefficients, the UN human development index, and poverty rates.

Measuring wealth

● Per capita income

The World Bank categorizes countries into four income groups. According to 2000 data, low-income economies have a per capita purchasing power parity (PPP) gross national income (GNI) below $1,980; lower-middle income economies have a PPP GNI of $4,600; upper-middle income economies have a PPP GNI of $9,210; and high-income economies have a PPP GNI of $27,770. [The World Bank now uses "GNI" in place of gross national product and defines PPP GNI as gross national income converted to international dollars using purchasing power parity rates.]

According to the conclusion reached by the 13th CCP Congress in 1987, China's basic, national characteristics included high population density, lack of cultivated land, low capital accumulation, and low per capita GDP. China was a low-income economy then. According to the World Bank's *World Development Indicators, 2002* database, in 1978 China's per capita PPP GNI was $340, or 13.6 percent of the average international level. By 1995, the number had risen to $2,650, indicating that China had entered the lower-middle economy group. In 2000, China's per capita PPP GNI was $3,920, ranking China number 124 in the world, or 53 percent of the average global level. It took China 22 years to narrow its income gap from 7.3 times to 1.9 times below the international level. Because half of China's population remains in the low-income economy group, it will take decades to elevate China's income to a middle level.

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To achieve this advancement, China's first step should be to reach a GDP equivalent to three-quarters of the world average in the next 10 years. The second step should be to match the world's per capita GDP level in the decade that follows. By that time, China, with less than one-fifth of the world's population, will account for about the same proportion (i.e. less than one-fifth) of global GDP.

The third step is to spend two to three decades to catch up with the developed world. Because of China's high development potential, it should be able to reach that goal. Based on World Bank statistics, from 1965 to 1999, the GDP growth rate in China was four times the world average—and it is well to keep in mind that the Cultural Revolution [during which China's economy suffered severe disruptions] occurred during this period.

● Engel coefficients

Engel coefficients estimate levels of prosperity by examining the proportion of income that is spent on food. According to the theory, the proportion of income a family spends on food falls as family income rises. As a supplemental indicator of per capita income, Engel coefficients reflect both the structure of consumption and a society's development level. When a nation spends 60 percent or more of its income on food it is labeled poor; when a nation spends 50-59 percent it is labeled basic; 40-49 percent, well-off; 30-39 percent, affluent; and 20-29 percent, rich. For example, in 1998, the percentage of income spent on food in the United States, Great Britain, and Japan was 13, 14, and 12 percent respectively; South Korea spent 18 percent; Mexico, 30 percent; the Philippines, 37 percent; Indonesia, 47 percent; and Vietnam 49 percent.

Looking back at 1978, China's urban and rural areas spent 57.5 and 67.7 percent of their income on food, respectively. This means that rural families remained in poverty, or even in starvation, and that the urban population was only able to meet basic needs. In 1995 rural families had an Engel coefficient of 58.6 percent, which indicates that only basic needs were met. Urban families had an Engel coefficient of less than 50 percent and thus, had entered the well-off stage. In 2001, the Engel coefficient of rural families dropped to 47.7 percent and that of urban families fell to 37.9 percent. In a little more than two decades, the wealth levels of both rural and urban residents improved by two levels.

Nevertheless, the structure of consumption is far from balanced. In areas like Tibet, Guizhou, Hainan, and many western provinces, Engel coefficients remain high. Several million poor people still live in China's rural areas—the country must develop to get rid of poverty. There are also more than 20 million poor people in China's urban areas. Their poverty is caused mostly by China's ongoing economic transition. With large numbers of both rural and urban poor, China still cannot be called a universally well-off society. The government needs to provide both training and social security.

The structure of consumption in China has also changed. In the early 1980s, the focus of consumption was mostly on basic needs, such as food and clothing. Later, when the proportion of income spent on food declined, the proportion of income spent on clothing also fell. Meanwhile, the amount of income spent on human investments such as education, culture, hygiene, housing, and healthcare increased. The difference between the consumption structure of urban and rural areas is clear. While the consumption structure of urban residents has approached that of the middle-income level, the consumption structure of rural residents has remained at a low level.

● Human development index

The United Nations Development Program's (UNDP) human development index (HDI) is a universal indicator that measures quality of life and social equality. The HDI is a composite index of three variables: real per capita GDP (in PPP$), educational attainment (including school enrollment and adult literacy), and life expectancy (which reflects the development of healthcare facilities). The UNDP publishes annual reports on international human development. Depending on their HDI value, countries are categorized as having low human development (0-0.5), medium human development (0.51-0.79), or high human development (0.81-1.0). In 1950, China had the lowest level of human development (0.159) of all countries in the study—even lower than India, which had an HDI value of 0.160.

In the past 20 years, China has improved rapidly. Its level is now above the world average, and the gap between China and the developed world is narrowing. In 1980, China's HDI value was 0.554. The value increased to 0.625 in 1990, and to 0.726 in 2000, ranking China 96 among 174 countries and regions. China's HDI value remains much lower than those of the United States and Japan, and a little lower than that of Russia, but much higher than India's HDI value.

It is conceivable that in the next two decades, China will raise its HDI value to 0.8 or higher, and then, in the following 10 years, raise it to 0.84. Why an HDI value of 0.8? Because it is the dividing point between the medium and high human development levels. It is more significant to raise HDI than to increase GDP because the former indicates increased social equality in addition to economic prosperity. Accordingly, our core task is to promote the education and life expectancy of more than a billion people, since this is what actually reflects improvements in quality of life and social equality.

To this end, first let's examine the average years of schooling in China. According to my estimates, in 1950 the average amount of schooling for those 15 years or older was 1 year; based on PRC government data, I estimate that in 1980 it was 4.5 years; and in 2000 it was 7.11 years. In another 20 years, we may be able to raise the figure to 10 to 11 years of schooling for each child. In fact, the average amount of schooling for China's urban population today is 9.4 years. If half of the population lives in urban areas in 20 years, will it be possible to raise the amount of schooling to 13 or 14 years? That is the average educational level in developed nations today. Therefore, I raise this issue: achieving a well-off society not only requires increasing per capita income, but also requires raising the human capital of the entire population. Only when the human capital of the populace—especially rural, poor, minority, and powerless populations—is increased, can

With large numbers of both rural and urban poor, China still cannot be called a universally well-off society.

productivity and per capita income be raised. One of the key ways to increase human capital is to increase the number of years young people attend school. China, therefore, should establish the largest pro-learning society.

Second, we should examine China's life expectancy—which in 1950 was 35-36 years. Life expectancy increased to 65 years in 1980—a dramatic improvement. Yet it has not improved a great deal since then, as China's current life expectancy is merely 72 years. China's life expectancy is better than the average levels of lower-middle and upper-middle income countries. Infant and child mortality rates in China are also lower than rates in lower-middle countries. China may be able to increase its life expectancy to 75 in the next 20 years, and then raise it to 78—which is the rate of wealthy nations today.

● **Poverty rates**

Poverty rates indicate the percentage of a population that lives under national and international poverty lines. In 1978, 250 million rural residents lived below the national poverty line in China [which the government sets at about $0.66 per day]. By 2000, the number had fallen to fewer than 22 million—an estimated 2.5 percent of the total rural population. In 1997, 880,000 urban residents lived below the national poverty line—accounting for 0.2 percent of China's total urban population. By 2001, urban poverty numbers had actually increased, to 11.7 million urban residents below the poverty line—2.4 percent of the total urban population. In 2002 there were 20 million urban residents in poverty, making up 4 percent of the urban population. According to World Bank calculations in 1990, 360 million people lived below the poverty line in China [the World Bank sets the international poverty line at about $1 a day]; in 1999 215 million people lived below the poverty line—the poverty ratio had dropped from 28.2 to 17 percent. It is estimated that in 2015, the number of poor people in China will decrease to 53 million.

● **Other indicators**

In addition to the indicators mentioned above, many more methods can be used to determine an all-around, well-off society. For instance, the UNDP uses a technology achievement index (TAI) that measures technological innovation achievements by examining technology creation, the diffusion of innovation, and human skills. China's TAI value is 0.3, which puts China in the category of "dynamic adopter" rather than the higher levels of "leader" or "potential leader," or the lowest level of "marginalized." In comparison, the United States' TAI value is 0.7—classifying it as a leader.

The World Bank uses other indicators as well, including environmental indicators that measure water pollution, deforestation and biodiversity, and air pollution; and public health through reproductive health indicators such as maternal mortality rates. By 2015 China expects that maternal mortality rates will decline 75 percent and that all people will be able to obtain safe and effective birth control methods.

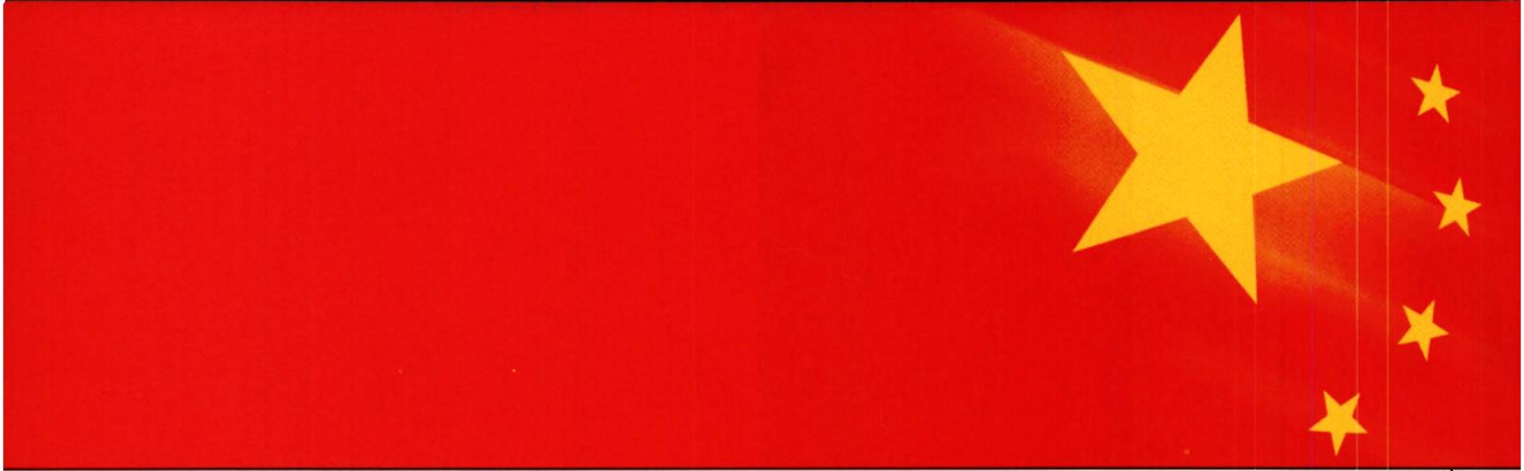
The World Bank has also established a system of governance indicators whereby governments are evaluated by six basic governance concepts: voice and accountability, political stability, government effectiveness, regulatory quality, rule of law, and control of corruption.

Goals for the future

In the past 20 years, the main focus of China's development strategy has been to allow part of the population and some regions to get rich first. In the next 20 years, China's main focus, namely, to build an all-around well-off society, will lead the entire population to march toward getting rich together. In his 16th CCP Congress address, Jiang Zemin stated: "We need to emphasize and pay attention to the less-developed regions and the professions or the people who are experiencing difficulties. Especially, we should guarantee the basic living of the poor people, and actively help them to get employed and to improve their living conditions. We should let them feel the warmth of a socialist society." This is what we mean by "getting rich together."

China's coastal and urban areas have already become well off. Some regions have dramatically narrowed their gaps with developed nations in terms of purchasing power, consumption, structure of consumption, and actual living standard. But our reality remains "one China, four worlds." As mentioned above, by the World Bank's GNI standard, China ranks 124 among 206 nations and remains in the lower-middle economy level. About 2.2 percent of China's population—mainly those living in cities like Shenzhen, Shanghai, and Beijing—have reached a high-economy income. A large proportion of coastal regions, such as Guangdong, Zhejiang, Jiangsu, and Liaoning, have reached the upper-middle economy level—21.8 percent of China's population resides in those areas. In Hebei, Hubei, Jilin, Heilongjiang, and some areas of central China, 26 percent of the population lives in the lower-middle economy level. China's "fourth world" includes the central and western regions. Unfortunately, 50 percent of China's population lives in these areas, where the income level parallels the poorest regions of the world.

According to the UNDP's *China Human Development Report, 2002*, in 1999 the HDI indicators for Shanghai, Beijing, and Tianjin exceeded 0.8. These three cities ranked 32, 33, and 48 in the world, and can be classified as "high human development" regions. The HDI figures for Guangdong, Liaoning, Zhejiang, and Jiangsu reached 0.75 or higher, which put these provinces



among the best 70 regions. Meanwhile, China's central and western regions ranked below 100.

Therefore, the main strategy in building an all-around well-off society should be to focus on the third and fourth worlds in China, especially the fourth. Some regions of China's fourth world rank very low when compared internationally. For instance, Guizhou's per capita GDP ranks 177 among 206 nations and regions. The per capita GDP of Gansu, Shaanxi, Tibet, and Guangxi is 157, 155, 154, and 155, respectively. These areas, in my view, should be the focus in building our well-off society.

Generally speaking, China has eliminated absolute poverty, can now meet the basic needs of its people, and has begun to enter the well-off stage—but is not yet universally well off. As Jiang Zemin stated in his 16th CCP Congress address, "The well-off life we are leading is still at a low level; it is not all-inclusive and is very uneven. The principal contradiction in our society is still one between the ever-growing material and cultural needs of the people and the backwardness of social production." This is an honest evaluation and fits the reality of China today. In the first two decades of this century, we should continue our struggle by concentrating our forces to build an all-around well-off society that benefits more than one billion people. 完

China's Next Decade of Reform—The Hard Choices

Five areas in which China's choices will significantly affect the outcome of its reform program

Kenneth J. DeWoskin

It is with a certain nostalgia that I think back to the days when each issue of *The China Business Review* included a fairly complete list of all the joint ventures announced or concluded in China during the preceding months. Today, the magazine's listing can only capture a fraction of the total commercial activity between Chinese and foreign firms. In those early years, the pace of change seemed formidable but manageable. The formation of foreign-invested anything was particularly arduous. The growth of entrepreneurship in China was immediately impressive; enterprise was everywhere but on a very small scale. What fate awaited China's large-scale enterprises was highly uncertain, and the ability of China's leaders to manage the kind of hybrid economy they contemplated was widely doubted. Throughout the early 1980s, officials and managers pressed upon all visiting potential investors the official line that China

Kenneth J. DeWoskin
is a partner at PricewaterhouseCoopers and Professor Emeritus, University of Michigan.

Planning and Markets Question: At what pace will China's leaders moderate the intensity of regulatory activity, recognizing that the risks and inefficiencies of planning and direct administrative control of many factors in commerce may outweigh the risks of submitting to market forces?

was committed to economic reform and would not turn back. The door was open and would not be closed.

I don't know anyone who imagined, much less predicted, the tidal wave of changes that followed, including compendious drafting of laws and regulations, profound restructuring of the regulatory apparatus, a globally unprecedented engagement of foreign direct investment, mobilization of massive domestic capital through the banks and equity markets, and, most important, the happy, prosperous engagement of most of urban China in building what turned out to be the very real, if indefinable, socialist market economy.

One year after accession to the World Trade Organization (WTO), China presides over increasing growth in exports and foreign exchange holdings; looks out over a glistening skyline in Pudong that is beginning to fill; scoops up the manufacturing business of Japan, South Korea, Taiwan, and much of Southeast Asia; anticipates more than a doubling of world-class residential, hotel, and office space in Beijing by 2006; proudly prepares for the Beijing Olympics in 2008 and the Shanghai Expo in 2010; lays claim to 60 million Internet users; and urges its nearly 200 very large state-owned enterprises (SOEs), many of which hold large capital reserves, to go overseas, invest, and acquire. Investment promotion agencies of developing countries from Vietnam to Nigeria contact our offices asking, "How did China do it?" while calls from would-be investors in North America, Europe, and the rest of developed Asia ask, "What comes next?"

History makes a convincing case that we really cannot answer the question "What comes next?" in China's remarkable reform process. But China has shown, from the onset of the Asian financial crisis in 1997 and recessions in its major export markets, that it can chart a course apart from its regional neighbors and the rest of the world because of its size, development policy, and administrative tools. As a way of framing questions for the future, I have tried to identify five areas in which China's policymakers will have to make hard choices that involve balancing priorities and desired outcomes. These bear on planning and markets, transitions, fragmentation, ownership, and value chain positioning, and all will have a major impact on the direction and success of reforms, growth, and investment over the next decade.

1. Planning and markets

One of the most critical balancing acts shaping China's future economic growth pits regulatory practices that intrude into commercial decision space against genuine liberalization and withdrawal of regulators from business and commerce. The process of restructuring critical sectors into duopolies or oligopolies of domestic competitors, begun in the early 1990s and accelerating in 1997 and 1998, was designed to strengthen Chinese domestic enterprises sufficiently to face international competition after WTO entry. But by 2003, this environment of "controlled competition" has not been fully successful in bringing China's banks, insurance, telecommunications, and oil and gas companies, among others, to international levels of competitiveness. As more WTO commitments kick in, and competition intensifies in key service and strategic sectors, regulators will feel intense pressure to assure and even enhance the prospects of the state's commercial assets through regulation.

As a result, against the long-declared policy of deregulation, a persistent counterpoint of immediate and specific regulatory actions remains. These actions seek to "strengthen management," "maintain healthy development," and "preserve order and stability." Against a determined policy of deregulation, a kind of contrary momentum has emerged in the publication and administration of new measures that is driving toward micromanagement and re-regulation. In spite of the declared direction of reform, toward market forces as the main regulator of commerce—as new People's Bank of China Governor Zhou Xiaochuan recently stated eloquently and unequivocally—in actual regulatory practices there is wavering, an uncertain back and forth.

Investors will be watching the forthcoming ministerial reorganization. Rumors suggest that the Ministry of Foreign Trade and Economic

Transitions Question: In conjunction with the restructuring of regulatory bodies and reorientation of their missions, will the Chinese government find a rhythm to its regulatory activities that balances the need to adjust and refine the emerging commercial code with the need to digest it and improve compliance?

Cooperation (MOFTEC) is slated to be reformed into an organization more like the Office of the US Trade Representative (USTR). In fact MOFTEC, with the State Council, just issued a new set of regulations extending its approval authority to foreign investment of less than 25 percent in any sector and circulated other regulations capping foreign investment in logistics and other sensitive sectors. This expands, rather than reduces, MOFTEC's domestic role, most significantly into important new merger-and-acquisition (M&A) opportunities for foreign investors. It also underscores China's continued interest in differential regulation based on source of capital and ownership, an interest ideologically inconsistent with the concept of national treatment.

Almost across the board, regulators are moving to strengthen management in their sectors, of everything from job fairs to telephone rates. Many of the recently published reports from governments and trade organizations on China's first year of WTO compliance point to a renewed intensity of regulation in key areas since WTO entry. This is not a surprise to observers who predicted China would struggle mightily in meeting its commitments. But for the coming decade, the most critical mission may not be compliance with WTO commitments. Rather it will be China's ability to continue its own essential effort to deregulate and leave markets to market forces. The conceptual shift is from controlled competition to fair and assured competition.

2. Transitions

For years, most articles in China's official newspapers marched to the beat of words such as "new," "milestone," "unprecedented," "record," and "reform." China's leadership and ministry heads are typically quite frank about many of the weaknesses in its transitional economy, and the main response is to acknowledge that the entire framework of law and regulation, as well as the structure of enforcement agencies, remains a work in progress.

The direction of regulatory developments aside, China faces an issue with the pace of change and with the concept of an unending era of transition. Although the domestic press is inclined to report impressive numbers and boast about the thousands of legal and regulatory documents produced in 2001 and 2002, there is nothing inherently virtuous about a continuous avalanche of new circulars, pronouncements, guidelines, laws, and regulations. It can create a sense that the central government is continually tinkering with every element in the legally defined investment environment, so that the pace of change confounds the ability of government to enforce consistently, and of business to comply with, the law. The pace of change itself impedes development of a serious respect for the law. To cite just one example: more than 20 significant amendments and clarifications were issued in the first year of implementation for China's new Accounting System for Business Enterprises.

This constant tinkering is arguably important for a deeply reforming system of enormous complexity, so the impulse to want to improve it is understandable. And in fairness, serious reforms are barely two decades old, the economy has grown in size and complexity, and China's technical skill at the national level in building the legal framework for industry and commerce has improved at an impressive rate. Still, one effect of these rapid and incessant changes is to make timely compliance both difficult and costly for domestic and foreign firms. For domestic firms, this prolific production of an array of new requirements makes compliance with any single one less compelling. For foreign investors, the pace of change itself increases compliance cost and risk and affects the fundamental calculus of investment in China.

3. Fragmentation

Fragmentation of authority into some 300,000 jurisdictions is arguably an advantageous feature that helps local administrations address local issues, a component of elasticity in China that provides stability in a country of such diversity. But in profound ways, the decentralization of regulatory and commercial power, fostered in the early decades of economic

Fragmentation Question: Can the government maintain a stable commitment to the clarification and consolidation of regulatory authority, with an appropriate degree of independence and administrative restraint, focused on fostering real competition and broad, fair compliance with commercial law?

reform, is increasingly at odds with the growth of foreign business activity and the emergence of genuine national markets and commercial players. It has stymied efforts to bring order to key parts of the business environment that need to be consistent on a national basis. Even the China Securities Regulatory Commission (CSRC) loses cases to local companies in local courts when it has tried to enforce uniform listing requirements.

Above I talked about the intensity of regulation; the consistency of regulation offers another set of issues. Fragmentation presents a formidable obstacle to the improvement of China's legal and commercial environments. Foreign-invested businesses can be audited by local, provincial, or national tax authorities for tax compliance, and by provincial bureaus of industry and commerce or the central-level State Administration of Industry and Commerce for business scope compliance. With different levels of authority, targeted companies face different agendas and different outcomes. At the provincial level, domestic interests frequently trump the most basic implementation of PRC economic contract law, banking laws, and joint venture agreements. This reality has tarnished China's commitment to rule of law and depressed foreign investment in a range of critical infrastructure areas. So far, there are few signs of improvement.

The competition between local and central authority in China is a historic reality that reaches deeply into the dynastic era. What is new in the last half decade is the emergence of significant economic power under the control of nongovernmental, even nondomestic, commercial and industrial actors. Consumer product companies have national markets and seek consistent practices for product testing, approval, registration, and the like. Leading technology companies now operate networks that span China for sourcing, manufacturing, and research and development (R&D), and seek uniform personnel, labor, salary, and benefit practices. Business service firms operate on a national basis, exchange information on policies and practices, and attempt to implement uniform systems for financial reporting, tax compliance, and the like.

These powerful commercial players, which are more effectively organized on a national basis than the government itself, pose a risk to the government's administration of the economy, and even its revenue, because they exploit some very basic regional discrepancies in practice. Examples include customs optimization, labor optimization, earnings tax efficiency, and business scope inflation. Municipal governments failed to keep up meaningfully with the national household registration (*hukou*) system, which companies nationwide disregarded as they moved personnel from office to office: engineers from Beijing to Shenzhen, accountants from Shanghai to Wuhan, managers from Tianjin to Shenyang. The central government repeatedly demonstrates its understanding of the need to improve the consistency of practice on a national scale, but effective remedies remain unclear.

The management of state assets within sectors is challenged by the banes of fragmentation. One recent response has been to reconsolidate several key industries—for example, automotive, oil and gas, telecommunications, nonferrous metals, and commercial aviation—and to try to strengthen central regulation by delocalizing and reducing the number of leading management groups. Regulatory authority over industrial and commercial sectors has tended to drift up from the ministries to the State Council and even from the Chinese Communist Party over to the State Council, concentrating in entities like the Commission for the Management of Large State Enterprises. There are indications that the State Development Planning Commission may become the home of many of the regulatory bodies soon to be fashioned, and that MOFTEC may actually turn out to be more like the US Department of Commerce and USTR combined.

This trend addresses the issues of structural fragmentation and inconsistency, but the efforts at recentralization and strengthening of regulatory practice, influenced by state ownership interests, have their own potential pitfalls, many the classics of monopoly. The Ministry of Information Industry has just fined China

Unicom for the first time for illegally reducing telephone rates, fighting the state's losses from declining revenues per user and the weakening profits of all the major state-owned operators. Similar issues are brewing in power, aviation, energy, and water.

Some pressures incline toward increase in the fragmentation of actual regulatory practice, especially the mixing of local regulatory authority with political power, driven by the mixing of local regulatory authority with local commercial interests, which are often nontransparent. Local commercial interests might reside in assets that are state-owned, or assets converted to shares, with some held in the private hands of local leaders. An important component in improving consistent and commercially successful regulation will be achieving some independence for regulators at all levels from pressures that distort policy and practice. In China, strong examples of regulatory independence at the central level could have salutary effects at the local level, but they are not yet evident.

In Western democracies, we think of the independence of telecommunications, insurance, banking, securities, and similar regulatory bodies as essential protection from the vicissitudes and whims of party politics. But ironically in a one-party system, in which neither judiciary, media, nor competing parties check excesses of influence, such independence may be even more salient. The recent restructuring of the PRC telecom sector resulted in an awkward combination of players that runs somewhat counter to available solutions that were demonstrably better from a technical and competitive standpoint. There are, in other words, two kinds of independence issues that are critical to China's future. One has been the focus of China's *zhengqi fenkai* campaign, which is separating regulators from business operators. But the other is independence from political forces and even personal interests of powerful leaders.

State Ownership Question: Will the processes of corporatization, shareholding, and governance improvement lead to a material and meaningful separation of regulation, operation, and politics to reduce state ownership as a distorting force in the regulation of China's business environment and a brake on productivity growth?

4. State ownership

Nothing is more important to China's future economic development than the search for solutions to the state-owned enterprise (SOE) performance problem and the influence of asset ownership on government behavior. With the state continuing to own major assets in many commercial and industrial sectors, and strengthening its administration of the largest 200 or so enterprises, the challenges to let markets work and permit level playing fields will remain far into the future.

From the standpoint of the state's ownership interests, China's leaders have been active and creative in fostering an evolution of ownership and governance structures, key elements in realizing the socialist market economy. The diverse objectives of this process have included protecting the state's assets, improving the competitiveness of SOEs, monetizing a substantial share of the state's assets, and fighting corruption and illegal conversion of state assets. The dilemma implicit in the process of strengthening control to relinquish control is reflected in moves like the rumored establishment of a State Asset Management Commission, on one hand, and, on the other, the promulgation by CSRC of minority shareholder protection guidelines that stipulate limits on government agencies in exercising control over enterprise activity, even when they own a majority share. In several sectors, the central government and Party can exert a leading influence in appointing top executives and regulators across the sector, setting development objectives and allocating financial, regulatory, and physical resources.

The well-documented history of different ownership structures and productivity since reforms began shows how SOEs continue to enjoy advantages in regulation, access, and capital allocation at the expense of both foreign investors and privately managed Chinese companies. We tend to think of protectionist measures in China as aimed primarily at foreign investors. But because of the state's overall control of the largest companies in China and appointment power for the top executives and regulatory agencies, such

Value Chain Question:
Will core policymakers recognize that the hard infrastructure necessary to achieve growth in high value, knowledge-driven business development is only a part of the picture, and that success also requires a soft infrastructure that provides efficient access to information and secure protection of IPR to justify R&D investment and reward creativity and achievement?

practices tend to protect the state's assets from private sector competition as well. Whole sectors where SOEs reign are legally or practically closed to China's own entrepreneurs. And as the central government cedes control of state-owned small and medium-sized enterprises to provincial and municipal governments, rather than resolve these protectionist practices, it may over time aggravate them. This is because the unchecked regulatory power of the local levels frequently acts expropriatively toward private assets and motivates regional protectionist actions.

Still, the growth of privately managed companies has been a driving factor in China's rapid growth, in spite of an unsupportive financial and regulatory environment that keeps them overtaxed, undercapitalized, and fragmented. If anything, this proves the potential of the private sector for China's future, should the playing field be levelled. Private enterprises, even the 10 largest, are dwarfed by SOEs in assets and revenue, but ironically they may be the best hope in many sectors for preserving market share in domestic hands.

Some SOEs and many of their descendant localized enterprises and shareholding companies have proven to be competitive as manufacturers and exporters of all manner of goods, and China's incoming leaders are committed to keeping China intensely competitive in global markets. Given that commitment, we can expect that SOEs and other state-controlled or -assisted enterprises may be willing to earn less from export sales to expand market share and keep the wheels of domestic industry spinning, maintaining employment, and assuring cash flow in the state's companies. The ideal is to have SOEs grow quickly enough to justify high employment levels as they become increasingly commercial. The best of the large Chinese enterprises should be able to sustain a tight margin process and do just that, even those enterprises that might not prove commercially viable in a fully competitive, nonsubsidized marketplace in the near term.

Fortunately for this agenda, few of China's enterprises are closely accountable for their financial performance on a quarter-by-quarter basis in the same way as foreign companies. And as the debate continues as to whether the large state banks are creating more nonperforming loans (NPLs) than they are eliminating, it is now apparent that even new and relatively commercial smaller banks have accumulated substantial NPL ratios by financing local industrial growth. The NPL story is the story of the shortfalls in competitiveness of these enterprises.

Thus there are new pressures on the horizon for many of China's exporters, especially the larger players. Exposure to shareholder scrutiny in domestic and international markets, new accounting procedures that disclose values and flows more realistically, and new credit risk measures in the banks are among key forces that increasingly will press SOE managers to commit themselves to real profits. This could have the effect in the next three to five years of reducing their export competitiveness, to the extent that it derives from various forms of assistance, transfer pricing of goods and services within groups, and a lack of pressure for earnings.

Liberalization of ownership categories and facilitation of commercially driven M&A activity will be among the most important reform steps. Recent initial public offerings indicate that even prestigious SOEs may be facing a more difficult time acquiring large infusions of capital on world markets. A more open and fluid M&A marketplace will reinvigorate direct and portfolio investment from abroad, as well as stimulate the appetite of CEOs to achieve earnings in their enterprises.

But building that marketplace will also require some liberalization of capital account convertibility, and that plays into leadership fears that are rooted in the Asian financial crisis. Liberalization of capital account management is just beginning to happen, primarily in the custodial processes being developed to superintend funds used by Qualified Foreign Institutional Investors (QFIIs). QFIIs bring hard currency for investment in China's A-share markets and presumably will be able to withdraw funds and repatriate them in hard currency as well.

The pressure to dispose of the massive nonperforming asset holdings of the asset management companies has led to pioneering M&A activity, such as the recent approval of bundled asset sales and the purchase of legal-person shares in several banks by foreign financial investors. But the weaknesses bred into many of these enterprises by the state ownership system will make evaluation difficult and even approved deals hard to close.

5. The value chain

Driven by national pride and strategic purpose, China has for a decade declared itself committed to climbing the value chain, becoming a knowledge-driven economy and a technology producer, as well as the factory for the world. For several years, foreign investors have significantly increased their investment in technology manufacturing, focusing on chips, screens, mobile terminals, and other high-technology component manufacturing and assembly operations, as well as R&D, product design, and remote software facilities. Universities at all levels across China have mobilized resources to graduate more students in technology areas, and China has also established more high-tech zones, including a network of 10 designated software centers. Two domestic issues loom as threats to China's aspirations to move up the value chain: the state's efforts to manage information and the poor enforcement of intellectual property laws and regulations.

Nothing exemplifies this potential climb up the value chain more succinctly than China's claimed Internet user base, which according to official sources surged 70 percent in 2002 to reach 59 million. And yet nothing better exemplifies the deep dilemma China faces in achieving its value chain aspirations than the struggle to manage the Internet, or more precisely the citizens who use it and the information that flows through it. China's management of the Internet has been explored from social, political, and technological perspectives in several recent books and articles. The economic impact has not been discussed in depth and may be more difficult to assess.

What we can say is that there appears to be a substantial diversion of technology talent and other resources into the state's effort to manage both access to and content on the Internet, and the intensity of regulation itself constitutes a substantial tax on information traffic. The pressure on Internet cafés and a strong push to limit the computer time of young people, based on uncertain research, will work against China's need for the kind of innovative young professionals who create new technology value.

The cost of the intense surveillance of traffic at international gateways is also hard to quantify, but tests indicate that a surveillance delay of up to 7,000 milliseconds for packets coming into and out of China is not uncommon, and many important sites, including major universities abroad, appear to be blocked, at least intermittently. The costs of such control in terms of efficient use of the Internet are inestimable. Internet-based information access appears to have been curtailed significantly in just the last six months, a trend that could be damaging to the prospects of China's technology-related developments. It is significant that the constraints on Internet surveillance are only technical, and as better technology has been deployed, surveillance has become more intense.

There are no signs yet of an internal policy debate about the impact of surveillance on China's plans to build a knowledge-based economy. It is apparent that the fourth and fifth generations of Chinese business leaders are increasingly part of an international mindset that attaches high value to efficient global communication and the free flow of information. The extent to which China is able to build a knowledge-based economy affects not only the efficiency of knowledge-driven businesses. It also bears heavily on issues as critical as China's ability to attract the large group of overseas Chinese with technical educations to return, work, and contribute.

Finally, intellectual property rights (IPR) experts seem generally satisfied with the laws and regulations that China has put in place, but they are just as disappointed in their weak and inconsistent enforcement. Among encouraging signs have been some high profile cases in which the IPR of foreign broadcasters, designers, and trademark owners have been upheld in Chinese courts, but a more ubiquitous reality is the flood of counterfeit goods easily accessible in any major Chinese city, including clothing, shoes, designer leather goods, pharmaceuticals, health-care products, software, music, and videos. As the supply builds, some brand names are even available in "good," "better," and "best" fakes, and the printing and packaging of digital video discs now approaches that of authentic goods. As *The CBR* goes to press, Huawei Technologies Co. Ltd., probably China's most prestigious high-tech company, is being sued in a US District court by Cisco Systems Inc., a case likely to be a watershed in the development of IP-intensive sectors in China and the outbound investment of leading Chinese companies.

If China succeeds in commercializing some of the technologies under development in China, such as TD-SCDMA for mobile telephony, Linux-based applications that support the adoption of open source operating systems, or domestically developed central processing units, for example, its own stake in protecting IPR and harvesting IPR-driven revenue will grow. But even as increasing internal pressure and political will to improve enforcement grow stronger, strict enforcement will be challenged by the sum of many of the factors discussed above, especially the fragmentation of enforcement authority and local interests in revenue from locally owned assets.

Making the right choices

Stark differences exist among prominent forecasts of China's economic and development future, from collapse to regional dominance. Pessimists focus on intractable weaknesses in China's fiscal and financial underpinnings, organizational problems, policy implementation sluggishness, the poor distribution of resources, and potential social turbulence. Optimists focus on the unexpected, unprecedented, and sustained success of China's economic growth, strength of China's external debt and foreign exchange positions, the enthusiasm and growing competencies of the fourth- and fifth-generation government and business leaders, and China's continued vocal commitment to continuing the reform process.

In the hard choices ahead, if China's decisionmakers press onward toward a more marketized economy—and provide genuine growing room to the more advanced SOEs, private enterprises, and foreign-invested enterprises—solid growth will continue, and a rising number of the Chinese people will be well served. 完

First Hand

Conversations with foreign businesspeople who came to China in the early 1980s and stayed

Catherine Gelb

They may be hard to tell apart from the thousands of other foreigners living, working, and competing in the China of 2003. But engage them in conversation and it becomes rapidly clear that these members of the small band of foreigners who first arrived in China in the late 1970s and early 1980s—and have stayed on for most of the past 20 years—have a first-hand and nuanced perspective about the China market. This perspective is instructive not only for businesspeople looking at China for the first time, but for the not-so-recent arrivals as well.

Back in time

Roberta Lipson, president of Chindex International, Inc., remembers landing at the airport in Beijing for the first time in 1979 (flying a route that took her through Paris and

Catherine Gelb
is editor of *The CBR.*

The US-China Business Council office in the Beijing Hotel was an "oasis" where foreigners would gather to vent their frustrations.

Dhaka) and walking into a one-room building with a floor flooded from the rainstorm in which they had landed. She and her fellow passengers retrieved their luggage as it was pitched through a hole in the wall.

From there, it was on to the Beijing Hotel—for years, the center of foreign business in the capital city. In those days, the telex was the lifeline of business. One had to book overseas telephone calls far ahead of time. (Forging good relationships with telephone and telex operators appears to have been vital during the early 1980s.) The US-China Business Council office in the Beijing Hotel was an "oasis" where foreigners would gather to vent their frustrations.

And the frustrations were considerable. Clinton Dines, an Australian who has worked in China since 1978 and is now president of BHP Billiton China, says: "Twenty years ago everything was opaque, everything was nontransparent, and your [business's] ability to make progress was very, very limited. You were subject to a range of controls on your every breath, on your every activity."

Examples of the kinds of difficulties early foreign investors faced emerge in conversations about one of the earlier foreign investments in China. In the early 1980s Occidental Petroleum took a 25 percent stake in what would be the largest open-pit coal mine in the world, located in rural Shanxi. A few of the foreigners who worked on that project, before Occidental Petroleum sold its stake, are still in China.

One of them is Carl Crook, now managing director of his own importing company, Montrose Food & Wine. Crook was born in Beijing in 1949. His parents were university teachers, his mother the daughter of missionaries and his father an aspiring writer. They met in China in the 1940s.

After growing up in Beijing and finishing high school during the Cultural Revolution, Carl and his brothers went to work first in a small farm tool factory that made parts for hand tractors and rice threshers and later in a truck overhaul plant. After leaving for graduate school in the United States in the 1970s, Crook found himself back in China representing Occidental Petroleum in Beijing in the mid-1980s.

"Thinking back on it, those were real pioneering days. There was no particular system. We weren't sure who was responsible for solving problems." Often, the problem-solver turned out to be the foreigner who spoke Chinese.

"It was a very interesting experience because everything was very unstructured in terms of what could and could not be done. There were no precedents. For example, this project had to bring a corporate airliner into China to get people into and out of this remote mine site. That was quite an experience. I remember trying to get this airplane inspected in China. It was a state-of-the-art little plane but it sure didn't meet the standards of the inspectors, Beijing representatives from CAAC [the General Administration of Civil Aviation of China]. So we had to make all kinds of changes."

Patrick Powers, the US-China Business Council's director of China Operations, worked on the Occidental mine project for Island Creek Coal of China, which was owned by Occidental. Powers, who had studied Chinese in Taiwan after college and had been working for Bechtel Inc. in the pipeline and petroleum technology group, was hired as the assistant to the training manager. When the training manager was promoted, Powers found himself promoted as well—a month after arriving at the project site in Antaibao.

Both Crook and Powers describe the difficulty the project faced in setting up an overseas satellite communication link from the mine site. Crook explains that the ministry in charge wanted the signal to pass through its own hardware. Powers recalls how, because the satellite hookup was delayed, the managers at the mine were sending hundreds of telexes each day. One day the project's telex machine went down. Powers sought out the telex in the local village and was eventually allowed into the telex room to type the message himself on a 1930s-era machine.

Crook also recalls that the coal project ran into problems of inadequate infrastructure in Shanxi. "The railway was instrumental in this project in that the coal was being produced in Shanxi but needed to be transported to Qinhuangdao Port [in Hebei]. But the railway line was very feeble and it couldn't carry much weight. For one thing, it was designed for passenger traffic, not for heavy trains. So the plan was made to build a dedicated rail line to move coal from Shanxi to the port—though they only managed to finish it by the time that Occidental pulled out of the project in 1988." The project also had trouble with the rail cars. "The equipment of the mine, which was first class, could load a rail car in something like 20 seconds. But the impact of the coal coming into the car was very damaging to many of the cars, which tended to stretch out because they had wooden sides."

The Canton Fair

In those early days, much Sino-foreign business took place further south—at the Guangzhou (Canton) Trade Fair. Most commercial interaction consisted of trade since foreign direct investment in China was minimal. For two weeks every six months, foreigners would flock to the city just over the border from Hong Kong. They sat at tables across from officials from Chinese ministries carrying order books filled with requests from Chinese entities for foreign products.

Chindex Executive Vice President Elyse Silverberg, in charge of the company's Capital Medical Equipment division, which is responsible for the export and after sales service of medical equipment, says that the challenge at these first meetings was deciphering what products the hospitals and other facilities actually wanted. Often, in the early 1980s, by the time the order requirements from the doctors made their way through the system to the foreign trade corporations, they were several years old and for obsolete products. The problem was further compounded by the fact that four overworked negotiators processed medical equipment orders for the entire country and no direct contact between the enduser and the equipment supplier was permitted.

Chinese speaker

All of these veterans will tell you that when they started working in China their primary value to their employer was Chinese-language ability. Indeed, Frank Hawke, president of IMC Asia Ltd., and Carl Walter, managing director and China chief operating officer at JP Morgan Chase, were on the same plane to China in 1979—part of a group of Stanford University graduate students who were the first Americans to travel to the PRC to study since 1949. Walter left China for a few years but returned as an investment banker and handled the New York Stock Exchange listing of Brilliance China Automotive in 1992, the first overseas listing of a Chinese firm. Hawke became a commercial and investment banker before going to work for IMC and was involved in early landmark deals such as the Great Wall Hotel and Beijing Jeep, among China's first batch of approved joint ventures.

Walter and Hawke and the others were young Chinese speakers who found themselves able and willing to work under difficult conditions in China. A few of them spoke almost with nostalgia of the camaraderie that arose among the residents of the Beijing Hotel and of the willingness to endure relative hardship that is much less evident among expatriates today.

They seem acutely aware that their position as foreigners in China comes with a certain responsibility to respect the way things work there. All referred to instances in which they found themselves acting as interpreters not only of the language but also of the culture and society. One remarked that one of the challenges of living in China was to avoid seeing everything through a foreign lens.

Fast forward

When it came to discussing what had changed most since they first arrived in China, the veterans all agreed that there has been progress toward greater openness, in varying degrees, at every level—as Dines put it—from city to city, industry to industry, and enterprise to enterprise. They also stressed that China has become an extremely competitive market—in sectors in which foreigners are permitted to operate. It has also become a more complicated place to do business. And corporations large and small have the same expectations for their China businesses as they have for their businesses anywhere else.

- **Access to markets**

More specific changes include "proximity to the customer," says Elyse Silverberg, when asked about what has changed most about doing business in China. She recalls the "amazing" occasion when she was finally shown the list of her Chinese customers. Chindex had to notify all of its Chinese customers about a manufacturer's recall on one of the products it had sold, but the company didn't know where in China the products had ended up. After explaining the problem to the government representative responsible for processing these orders, he finally agreed to open the book and show her the long list of customers and products.

Some industries have also evolved significantly over the years, among them the oil and gas industry: "It's really become more sophisticated, more globally oriented, more technically and commercially adept," says Dines.

- **Access to government**

Another change has been the increase in foreign businesses' interaction with government officials. In the early days, foreign firms would interact with a small number of designated government representatives. Today, foreign companies can, and must, talk to members from every branch of the government. And many of these bureaucrats are impressive. Dines describes the officials in Beijing as "technically well qualified, sophisticated, worldly—chances are they will have a language skill, and [there is] a very high chance that they will have a broad comprehension of the issues in their industry and the issues in their industry that are related to China."

- **Access to talent**

Perhaps the most dramatic change in the business environment, particularly in coastal cities, has been the emergence of a large pool of skilled Chinese employees and coworkers compared with 20 years ago. There are many well-educated, bilingual, or trilingual Chinese, and many capable of assuming managerial positions. Don St. Pierre, a former auto executive who now owns and operates another leading wine importing operation in China, ASC Fine Wines, attributes the growth of his business, in part, to his ability to "find and keep good people."

The typical Chinese manager in a state-owned enterprise used to boast about how many sets of machinery, how many employees, and how much land their enterprise took up. But in China today, many of these same managers talk about net earnings, price-to-earnings ratios, and how to reduce employment and improve operating efficiency.

For foreign businesspeople, the vast supply of skilled Chinese has meant that it is no longer enough for a young, energetic foreigner looking

"I think that now, *guanxi* is still a useful term, but I think its meaning has changed quite significantly."

—Carl Crook

Several of these veterans insist that despite China's reputation as an impenetrable market for foreign companies, it is possible to run a profitable business in China.

for work in China to speak the local language. Professional skills and a business background are far more important. It has also meant a very different life for the typical expatriate in China. Frank Hawke notes that in the large coastal cities it is possible to live and work in a cocoon in which Chinese language fluency is unnecessary.

- **The new *guanxi***

This new competition and professionalism in the business environment has contributed to a decline in the importance of relationships (*guanxi*), in the view of some verterans—or, in the view of others, a shift in the meaning of the Chinese term. Crook observes, "In the beginning the foreign company would seek out some offspring of some high official who would promise to fix a certain deal.... And I think that now, *guanxi* is still a useful term, but I think its meaning has changed quite significantly. I think it now means being well informed and having some personal rapport. That is very different from saying 'can pull strings with people in office,' which is what it used to mean."

Profits are possible

Several of these veterans insist that despite China's reputation as an impenetrable market for foreign companies, it is possible to run a profitable business in China. Powers says, "One of the great myths is that no one makes money here. Many companies make significant profits, particularly those that have a balance of exports and domestic sales." Carl Crook notes that despite Occidental's decision to pull out of the coal project (after the price of coal plummeted and the market for the product failed to materialize), the Chinese took it over and run it profitably today.

Don St. Pierre makes a similar point about the Beijing Jeep venture, which he oversaw as an AMC executive in the 1980s and which was immortalized in Jim Mann's book of the same name. He notes that the book's negative tone obscures the fact that Beijing Jeep turned out to be a viable operation.

There may be another, more selfish motivation for downplaying one's profitability in China. James Spear, who heads up the logistics and consumer side of Chindex's operation, observed that foreigners who entered China early on have an incentive to "play up" the opacity of the system as a way to discourage their competitors from following them. Spear is adamant that it is possible and necessary to run a business in China based on profit and loss and return of value to shareholders.

Still China

For every striking change these foreigners have observed, they can cite something that hasn't changed about doing business in China. Among them:

- **Real barriers exist**

As Dines puts it, "In virtually no sector do foreign companies have totally unfettered access to the domestic market. There are a lot of sectors where you have far more flexibility than you used to have, but there is no sector where you have unfettered access to do what you like. The nature of the game is control." Powers adds, "It is still not an open market, even if there is more freedom."

Powers points out that the government plays a role in the market as both regulator and competitor, which often, though not always, puts foreign companies at a disadvantage. He notes that foreigners rightly complain that there are still "too many administrative and procedural regulations aimed at foreign firms that work in favor of domestic companies."

The veterans agree that foreign companies that manufacture for export, provide professional services, and operate hotels—and to some degree those that develop property—have generally had more success. Those involved in sectors in which foreign investment is more restricted, such as power generation or beer, have had a tough time.

- **Time has stood still in some regions and industries**

The sectors and parts of the country that have been closed to foreign business have not achieved the level of professionalism that foreign businesses encounter on the coast. The inherent altruism of government officials declines dramatically the further one moves from big cities and coastal provinces toward the interior and from cities down to the township and county level.

Several investors also pointed out that there are still industries in which the old state-owned enterprise mentality is strong. One told of a plant manager who boasted that his factory's output was sold in numerous provinces around the country—even though basic market research would have told him that there was a market for the plant's entire output just within the factory's home province.

Even in these cases, though, there are exceptions. Dines makes clear that even in industries like coal, that have not opened up as much as oil and gas, it is possible to find "leaders and laggards" among Chinese enterprises.

- **A generation gap persists**

Companies also run up against stubbornly small pools of qualified people for certain specialized positions. Although foreign companies in China today can find highly qualified Chinese able to work as managers, there is an experience gap in the managing class, especially in industries such as finance. Carl Walter notes that the pool of people who have had experience in both commercial and investment banking overseas and in China, and can then represent all of a foreign company's interests in China, is extremely small. Interestingly, this is true of both the Chinese and foreign talent pools.

Powers notes that there have been several waves of localization over the past 20 years. Ten years ago foreign companies generally wanted an expatriate manager in China, but today they want a local Chinese manager. Such localization, when undertaken for cost cutting purposes, "can lead to difficulties, especially if the local managers have not been properly trained to take on higher-level assignments." He adds, "There is much to be gained from a harmonious balance of local Chinese and expatriate staff within an operation" to meet both internal and external needs. "The Council sees cases where the real value of an experienced expat is to keep the company from making hasty or poorly thought out investment decisions." Yet he acknowledges that this is a role whose value is hard to quantify.

Doing your homework is still crucial

Due diligence is, has been, and always will be indispensable for any China business assessment. Finding out whether, for example, a potential Chinese business partner has any competing interests is only one of the many evaluations a foreign firm must make before investing in any project.

As has always been the case in China, it is difficult and time-consuming to find the necessary information about potential partners. This fact has made conducting thorough due diligence in China extremely challenging. Dines says a businessperson today will "still find situations where your ability to make progress or get information is as limited as it was 20 years ago."

Powers notes that many failure stories can be traced back to an inadequate due diligence process with regard to strategic planning, partner selection, and market research.

Hawke echoes this opinion. It is essential for a company to "run the numbers" for China projects the same way it would for any other market. The ultimate decision may take into account the fact that China may be a good investment for strategic reasons. But there is no excuse for not evaluating potential projects according to standard criteria.

Despite three decades of dramatic change, these veteran investors know that daily life in China still requires resourcefulness and creative problem-solving ability. This challenging climate first brought them to China, keeps them there now, and continues to attract others.

Don St. Pierre sums up what may be the ultimate constant about the China market. "There is a foreign investor born every minute—that hasn't changed." 完

Investment Pioneer

The first US-Chinese high-technology joint venture is alive and well

Catherine Gelb

Edmund J. Tarala, chief engineer of Shanghai-Foxboro Co. Ltd., didn't think he would return to China after his first tour of duty, helping to establish the very first US-Chinese high-technology joint venture in 1983, was over. But he was convinced to come back—and still shows up for work each day at the southern Shanghai plant, eight years later. A conversation with Tarala reveals the progress the pioneering joint venture has made over its 20-year history, and reveals just how much the business environment has changed, not just for this particular company, but for foreign-invested enterprises (FIEs) along China's coast in general.

Shanghai Foxboro Co., Ltd. (SFCL) is a joint venture between The Foxboro Co. (purchased in the mid-1990s by Britain's Invensys) and Shanghai Instrumentation and Electronics Holding (Group) Co. (SIEC), a state-owned

Catherine Gelb
is editor of *The CBR*.

CHINA BUSINESS SUMMIT 2003

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China under New Leadership: The New Dynamics of Trade and Development

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BEIJING, CHINA 14-15 APRIL

China is currently in the midst of a seminal transition that changes the top leadership, central ministries, and provincial and municipal governments. Many say that the new leadership will not alter China's overall policy direction. However, for sure, the new leadership is already putting its own imprint on the shape of China's emergence as one of the world's largest trading, manufacturing and consuming forces.

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For more information and a preliminary list of confirmed discussion leaders, please contact Ms Beatrice Laenzlinger
E-mail: chinasummit@weforum.org
Tel.: +41 (0)22 869 1242
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Website: www.weforum.org

The World Economic Forum is an international organization committed to improving the state of the world. The Forum provides a collaborative framework for the world's leaders to address global issues, engaging particularly its corporate members in global citizenship.

Photographs courtesy of Shanghai Foxboro Co. Ltd.

conglomerate of more than 100 enterprises. The joint venture manufactures, sells, engineers, and provides technical services for process control instruments and advanced distributed control systems for power plants and other utilities, and large manufacturing facilities in industries from steel to food processing. Of the 180 active nuclear power stations around the world, Tarala estimates that SFCL has supplied reactor shut-down controls for 120 of them.

The plant consists of nine buildings, 10,000 square meters, and seven workshops that manufacture printed circuit board assemblies, test component quality, and assemble final systems, among other tasks. Each system is designed to customers' specifications, at a cost of anywhere from \$300,000 to \$3 million. Around 70 percent of SFCL's systems are made for the local market; the rest are exported. The staff of 380 includes 140 on the manufacturing side. Of these, 125 are engineers. The rest are corporate staff, responsible for sales and marketing and finance. The venture, which employs only two expatriates, even has its own photographer and complete dining facilities.

Once in the top ten —not anymore

Foxboro's total investment in 1982 was \$5.53 million, which gave it a 49 percent stake in the venture and made it one of the top 10 foreign investments in China. The company injected additional cash into the venture in 1995 to take a majority position (51.5 percent) though Tarala says that having majority ownership hasn't changed daily operations at the plant. The joint venture's total cash investment has been \$17.26 million over 20 years—this excludes the value of the process- and manufacturing-control technology they have transferred during this period.

Nevertheless, the joint venture is a small FIE compared to the large investments since made in China by General Motors Corp., Motorola Inc., and others.

The value of technology—and training

Transfer of technology has been continuous. "Back when we started, the technology in use today didn't exist," Tarala says. "Though we had lower levels [of technology], that technology was state of the art at that time. We continually transfer new technology to meet market needs here in China." The rapidity of change in the industry means that technology becomes obsolete before it can be copied, he asserts. This is the principal reason why the company has had no problems with intellectual property rights infringement, despite early concerns.

One reason the transfer of technology has gone so smoothly, Tarala says, is constant training. "E-mail only goes so far," he notes. The joint venture has sent 700 customers and staff to 11 countries on training programs ranging from two weeks to six months. The abilities of the engineers at the plant have also expanded. Technical skills have improved, and many of the staff are bilingual or even trilingual.

Sourcing in China

The joint venture purchases computers and many other parts that run its systems within the Asia Pacific region; many are sourced in China. The joint venture, like most in China before the country's World Trade Organization (WTO) entry, had no choice but to find sources for its components from within China. Tarala says that this was not such a bad thing. "In China, PCBs [printed circuit boards] are 30 to 50 percent cheaper to buy, but it took us seven years to get suppliers qualified on our sourcing list." He says, though, that once you explain to a Chinese supplier what you want, you may have to work with the firm for a while but you will get the component you need, and it will be of good quality.

The parent company has full-time purchasing staff in New York, Boston, and Shanghai but the joint venture still has some trouble finding certain component suppliers able to deliver within reasonable periods of time. One electronic device has a 40-week lead time, which means the company must keep an inventory of this and other critical parts, which ties up working capital.

Keeping up with competition

Such concerns as excess inventory have become much more important over the years, as market demands have grown more sophisticated. "PRC customers are very demanding—

Chief engineer and director of Technology Edmund J. Tarala.

demanding more than in the past. They want a lot for their money, lots of after sales service, startup assistance."

This mirrors the changes in the China market as a whole, says Tarala. "Obviously the situation in China has changed dramatically in the 20 years we have been here." He explains, "In the beginning, we really didn't have to do any sales and marketing. Customers would line up outside our door wanting to buy our products, we didn't have to think too much about how to sell in China or market in China. Over the last 20 years, our competition has moved in, the Chinese equivalent of what we do here has improved substantially, so not only do we now compete with other foreign companies but also with Chinese companies, because they absorb technology quickly."

Competing against the likes of Rosemont, Honeywell, ABB, and Siemens AG, not to mention emerging Chinese firms, has meant pressure to cut costs. The venture has adopted the Six Sigma "lean manufacturing" program, which has resulted in more efficiency and shorter product cycle time, and significant cost reductions. The plant was also the first one in China to obtain ISO 9000 certification of its management processes.

The ability to hire and keep highly competent staff can be crucial to maintaining competitiveness. Tarala estimates that fewer than 10 staffers have left the venture in the past eight years. The Chinese managers at the venture today are younger, better educated, and more flexible than ever before. Managers measure results and make reports using the same benchmarks as those used in the US headquarters.

Tarala says that the fact that SFCL has had rising sales (and proportionally rising profits) since its first year of operations, except for 1994-95 during China's recession, has had a lot to do with the plant's in-country manufacturing—and service—capabilities. Chinese customers like the fact that the venture makes its systems in China, no doubt in part because this enables the company to dispatch repair teams anywhere in China within 24 hours. There is also an upside to the venture's large store of spare parts. Other competitors may not have parts on hand, or may only be assembling in China, meaning that repair expertise has to be flown in from elsewhere.

New complexities

The joint venture today must perform to the same standards as its counterparts around the world. There are no longer special exceptions for the fact that the plant happens to be in China. SFCL must achieve sales and market share goals as well as goals for cost control, inventory turns, defect levels, and customer satisfaction.

It is too soon to tell what effects China's WTO entry will have on the venture's ability to meet

Shanghai Foxboro Co. Ltd. engineers at work.

these goals. Tarala says that as of late 2002, WTO hadn't affected the plant's daily operations much, except perhaps in speeding up Customs clearance of imported material, and in new rules on infrastructure projects in which the venture is involved. He is already seeing some changes in the government's rules on standards, and anticipates that these changes will have a noticeable impact. "Any time you get something new in China, it tends to be difficult until people up and down the ladder learn what they can do, what they can't do, and how flexible they can be."

Tarala's job has grown more complicated. Making the right decision is harder because there are more options to choose from. Also, his job as chief engineer used to be 20 percent managing and 80 percent teaching in the early 1980s. That ratio is now reversed. "Now," Tarala says of his engineers, "They have learned so many management concepts from exposure abroad and from management in the company, they challenge many things—which is good."

Reminders of the past

Tarala is still a foreigner working in an organization made up largely of Chinese. His staff is free with the good news but not always inclined to tell him about setbacks. As a result, he has found that "management by walking around" is still the best technique to find out what is actually going on in the plant on a daily basis.

The plant is also, of course, still a joint venture, though many other foreign investors have bought out their Chinese partners and taken on the often more profitable form of a wholly foreign-owned enterprise. The Chinese partner of SFCL, SIEC, is happy to hang on to its share because it is so profitable. The relationship between the partners is nevertheless a good one, Tarala says, and the Chinese partner has been helpful in the joint venture's dealings with the local government.

The government, in fact, still has the power to affect daily operations. For example, when the Shanghai power bureau decided to undertake routine maintenance at the plant one day in late October, they were able to shut off the plant's electricity—even during the middle of the week.

A long way since 1983

The venture will likely see further growth in the next five years, though achieving its growth goals will be a challenge. Tarala anticipates increasing price pressure and competition in its existing markets. Thus, the joint venture is working to break into transportation and other new market segments in which some of its competitors are well established and is looking not just in China but elsewhere in Asia for new projects. Tarala says he has told his staff that the company must be "lean" and "cautious" in the future and cannot take anything for granted—or the venture will find itself out of business. He's certainly not the only manager in China telling this to his staff. It's as good an example as any of how far the China market has come since 1983. 完

The Demise of the Hong Kong Dollar Peg

A prolonged period of global deflation may cause Hong Kong to abandon its currency peg

Chi Lo

The Hong Kong Dollar Link, as the local currency peg to the US dollar is officially called, was set up in 1984 to guarantee currency stability in the run-up to the handover of Hong Kong to China in 1997. No one doubts the fundamentals behind the peg in the short term: Foreign exchange reserves are ample, government debt is small, and Hong Kong is a net external creditor *(see* p.78*)*. But there are signs that the government is losing faith in the currency peg, and it may be considering delinking the

Chi Lo,
former chief economist at Standard Chartered Bank and research director at HSBC, is an independent economic strategist based in Hong Kong.

currencies in the medium term to escape the effects of what is becoming a widespread expectation of prolonged deflation in the world economy.

The single most important factor that makes a strong supporter of the Hong Kong dollar peg, including myself, rethink its viability is the threat of entrenched global deflation. The Achilles heel of the peg is the Hong Kong government's worsening fiscal position, which is tied to unfolding deflationary forces. Crucially, the recent rise in Hong Kong's fiscal deficit reflects the government's unwillingness to suffer more economic adjustment pains than it already has under the peg.

Why deflation makes the peg a burden

Since the share of land premiums and stamp duties account for a big chunk of total fiscal revenues in Hong Kong, the collapse of the property market since the 1997 Asian crisis has significantly slowed government revenue inflows. In the current climate of deflation, the days of rampant property price growth are unlikely to return soon. The shrinking of revenues from the local property market suggests that Hong Kong's budget deficit has become structural under the peg.

The rising fiscal deficit and consequent erosion of fiscal reserves are undermining the foundation of the Hong Kong dollar peg. This is because the fiscal reserves form a major part—almost 40 percent as of late 2002—of the Exchange Fund that underpins the peg. If the annual fiscal deficit remains at around HK$70 billion ($8.98 billion), as the current trend indicates, Hong Kong's fiscal reserves will be depleted in four years. But investor confidence will crumble before the fiscal reserves run out, causing massive capital outflows that will pressure the peg.

The view that a complete depletion of the fiscal reserves, which will still leave HK$570 billion ($73.11 billion) in the Exchange Fund, will not necessarily crush the peg is naïve. When it comes to defending the Hong Kong dollar peg, it is not what the Hong Kong Monetary Authority (HKMA) expects to commit in case of a crisis that matters. Rather, it is what the HKMA eventually would have committed—defined as the amount that depositors would withdraw from the banking system in case of a loss of confidence—that matters.

The Exchange Fund (excluding fiscal reserves) amounts to 240 percent of Hong Kong's monetary base, which includes notes and coins in circulation, banks' aggregate balance with the HKMA, and Exchange Fund securities. But the survival of the peg in a crisis of confidence would involve the whole Hong Kong dollar deposit base. Yet, the Exchange Fund covers only 30 percent of all Hong Kong dollar deposits. So if every holder of Hong Kong dollars were to convert their deposits into US dollars or other hard currencies, there would not be enough foreign reserves to meet demand; the Hong Kong dollar peg would break. Local public confidence is indeed fragile—the growth of Hong Kong dollar deposits has fallen steadily since the Asian crisis and has been negative since January 2002. As a result, falling fiscal reserves will erode public confidence and the margin of safety provided by the Exchange Fund and impede the authorities' ability to deal with contingencies effectively.

The rising fiscal deficit and consequent erosion of fiscal reserves are undermining the foundation of the Hong Kong dollar peg.

If the government resorts to borrowing to plug the deficit hole, the rise in public debt will only exert more stress on the Exchange Fund and erode public confidence further. The fund will either act as a direct lender or a guarantor for borrowing. Both acts will require it to commit more resources to fund the fiscal deficit, thus reducing its ability to protect the peg.

Forcing a choice

The combination of deflation and Hong Kong's structural fiscal deficit are forcing the government to choose between lowering the external price of money (un-pegging the Hong Kong dollar) and lowering asset prices (chronic asset price deflation). Re-setting the peg is not an option because re-setting the peg once would create expectations that the government would re-set it again. The currency link system would lose credibility and speculative attacks on the peg would follow, leading to its eventual collapse.

The survival of the peg thus depends on the political will to tolerate the economic adjustment pains that are necessary under the currency peg. This means the government cannot intervene in the economy even at times of economic stress. The persistent rise in Hong Kong's public spending to boost growth is the most notable sign of recent interference. Since 1997, fiscal spending has risen from 17 percent of GDP to 24 percent—one of the highest ratios of non-defense public spending to GDP in Asia.

Large fiscal spending looks likely to stay, as government policy has shifted from laissez-faire to hands-on. From the currency peg perspective, however, any market-supporting measures distort the peg's adjustment mechanism. To keep the territory competitive when other Asian currencies depreciate, Hong Kong prices need to fall under the currency peg. But the government's supportive measures are preventing the necessary decline in the city's domestic prices, thus distorting the peg's adjustment mechanism.

These supportive measures also show that the authorities are hitting their tolerance limit for economic pain caused by the peg and, hence, may be mulling a policy shift. All this is best summarized by Antony Leung's anti-peg comments since he took over as financial secretary in late 2000—in essence, he has said that the peg is an obstacle to Hong Kong's development.

No constitutional backing

Indeed, it would be easy for Hong Kong to sever the peg because the Hong Kong dollar peg does not have robust constitutional backing. Article 111 of the Basic Law only guarantees the Hong Kong dollar as the legal tender in the Hong Kong Special Administrative Region and ensures that the issuance of Hong Kong dollars is fully backed by a reserve fund. It does not guarantee the Hong Kong dollar peg and its convertibility rate of HK$7.80 per US dollar. On the other hand, the Argentine peso peg unraveled under severe economic stress, even though it was enshrined in the constitution and approval from both houses of Congress was needed to scrap it.

The fate of a currency regime is more a political choice than an economic one, and the advent of a new era of prolonged low inflation, with periodic deflation, has cast doubt on the desirability of the Hong Kong dollar peg. The govern-

Hong Kong's Peg

Hong Kong has had a fixed exchange rate system since 1983, when the value of the Hong Kong dollar was fixed at HK$7.80 per US dollar in response to currency instability and general uncertainty about Hong Kong's future in the years before its return to China. Under this system, all notes and coins in circulation are backed by US dollars. The three banks that issue notes in Hong Kong—Hong Kong and Shanghai Banking Corp. Ltd., Standard Chartered Bank, and Bank of China—must, for each 7.8 Hong Kong dollars they issue, deposit a US dollar in what is known as the Exchange Fund. In return, they receive a Certificate of Indebtedness, which allows them to redeem US dollars when they pull Hong Kong dollars out of circulation.

Good pegs have currency boards. Currency boards keep a fixed exchange rate, ensure that every note and coin of local currency issued is backed by the anchor currency, and exchange the local and anchor currencies on demand. They do not participate in monetary policy and are independent of the government. The Hong Kong Monetary Authority (HKMA), set up in 1993, oversees the Hong Kong peg system. But because HKMA performs some of the functions of a central bank, such as regulating banking and financial systems, it is not a true currency board.

In addition, most currency boards have a firm legal base—that is, their role is written into law. Hong Kong has no such law, other than the Exchange Fund Ordinance. This ordinance gives the financial secretary not only control of the fund (no separation from government) but also rather broad, but vague, powers: "...the Financial Secretary may...use the fund as he thinks fit to maintain the stability and the integrity of the monetary and financial systems in Hong Kong." On the other hand, HKMA is not a true central bank either, as it does not issue notes or act as a banker to the government.

How the peg works

As HKMA explains, "Under the currency board system, ...interest rates rather than the exchange rate ... adjust to inflows or outflows of funds. The monetary base increases when the foreign currency ... to which the domestic currency is linked, is sold to the currency board for domestic currency (capital inflow). It contracts when the foreign currency is bought from the currency board (capital outflow). The expansion or contraction of the monetary base causes interest rates for the domestic currency to fall or rise respectively ...[causing investors to move funds]..., while the exchange rate remains stable. This process is very much an automatic mechanism, which does not require the HKMA to exercise any discretion." *(Hong Kong's Linked Exchange Rate System)*

Benefits of the peg

In Hong Kong's case, one of the most important benefits of the peg is still the guaranteed currency stability in a time of political uncertainty over Hong Kong's future. Though Hong Kong has now been a special administrative region of China for more than five years, new sources of uncertainty—such as interpretation of the Basic Law, recent proposals for an anti-sedition law, and lack of confidence in the current Hong Kong government's ability to keep the economy running smoothly—show that the peg is still useful.

As a center of international trade and finance, Hong Kong is extremely vulnerable to external economic shocks. The linked exchange rate guarantees a stable currency, which eliminates much of the foreign exchange risk faced by actors in Hong Kong's small, open economy. According to HKMA, local markets respond quickly to economic pressures: Prices adjust fairly rapidly to restore competitiveness without changing the exchange rate. Yet the smaller number of economic levers available to policymakers in Hong Kong compared to economies with floating exchange rates means that Hong Kong's economy must make structural changes to cope with economic pressures. Though painful in the short run, such changes benefit the economy in the long run.

Drawbacks

On the downside, internal wage and price adjustments may be more wrenching than they would be if the exchange rate were free to adjust. The linked exchange rate also effectively links the interest rates of the US and Hong Kong economies, which prevents HKMA from using interest rate adjustments as levers on the Hong Kong economy. And when the economic cycles of Hong Kong and the United States are out of synch, US interest rates may not be at levels appropriate for Hong Kong. Indeed, a few years ago, the United States raised interest rates to cool down its overheating economy just when Hong Kong was struggling to recover from a recession brought on by the Asian financial crisis.

Another drawback is that the Exchange Fund ties up reserves that, some have argued, could be put to better use—invested in the local economy or spent on improving Hong Kong's education, health, and welfare systems, for instance.

—Virginia A. Hulme

Virginia A. Hulme is associate editor of *The CBR*.

ment is increasingly uncomfortable with the long-term burden the peg imposes on the economy under deflation. But it will likely do nothing in the short term, if only because of the difficult steps that would be required, among them reforming the HKMA into an independent monetary policy manager.

Rationale remains

The above argument does not deny the merits of the Hong Kong dollar peg for Hong Kong's small, open economic system. After all, scrapping the peg will not solve Hong Kong's structural problems, among them a rising skills mismatch, an education system in dire need of reform, and an outdated economic model based on asset trading.

Moreover, the alternative currency regimes are unlikely to be any better for the Hong Kong economy. The volatility that characterizes a floating exchange rate would hurt the city's competitiveness as a financial center, while a managed float (which would entail frequent government interventions to keep the exchange rate from moving freely) would risk over-politicizing the exchange rate.

If the peg goes

Given the signs of wariness about the peg, investors would be wise to prepare for its demise. The immediate effect would likely be a sharp drop in the Hong Kong dollar-US dollar exchange rate. In such a case, how would Hong Kong's asset prices behave? As a reference, we can look at stock market behavior in Argentina and the United Kingdom, both of which have broken their currency pegs in recent years.

● **Argentina**

Argentina pegged its currency to the US dollar in 1991 to combat hyperinflation and stabilize the economy. The peg succeeded for a few years, but because of imprudent economic policies, it came under pressure in the late 1990s. The peso peg severely damaged Argentina's export competitiveness and its ability to repay foreign debt. The government eventually defaulted in November 2002 and abandoned the peg in January 2003. Argentina's stock market surged 100 percent in the month before the peso-dollar peg was scrapped, as the markets expected major relief from the economic pains of deflation, bankruptcy, unemployment, and economic contraction that the adjustment mechanism was inflicting.

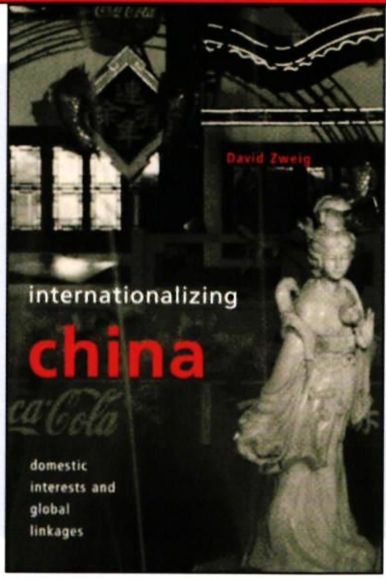
For the same reason, Hong Kong's asset prices could also start rising if signs emerge that the government may decide to sever the peg. What would happen next to asset prices would depend on whether Hong Kong was able to restructure to survive in the new economic era. In Argentina's case, hesitation to eliminate structural woes in the economy caused asset prices to plummet after the peso peg was abandoned. The Argentine government imposed strict capital and deposit controls and created a dual exchange rate to skirt full devaluation and restructuring pressures. But these measures have only postponed thorough adjustments, and thus have haunted the markets.

● **United Kingdom**

Britain's experience was very different. Britain had joined the Exchange Rate Mechanism (ERM), which fixed European currencies' cross-exchange rates within specific bands, in 1990. During a speculative attack in September 1992, the Bank of England decided to drop out of the ERM. UK stock prices rose steadily after the British pound dropped out of the ERM. The ascent of UK equity prices lasted until late 1999, when the global investment bubble burst. This sustained rise of British asset prices after the break of the peg from the ERM was a result of successful economic restructuring, notably in the rigid labor market. Britain's productivity and economic growth have consistently outperformed many other European economies and thus supported asset price growth.

The upshot

What all this means is that though severing the peg may give an initial push to Hong Kong's asset prices, what happens in the post-peg era would depend on the city's restructuring efforts and the macroeconomic environment. Because the macroeconomy is outside of Hong Kong's control, the territory's ability to reinvent itself would determine whether Hong Kong's asset markets would revive in a post-peg era. 完



Internationalizing China: Domestic Interests and Global Linkages

by David Zweig
Ithaca, New York: Cornell University Press, 2002
290 pp. $45.00 hardcover, $22.50 softcover

International businesspeople who have found themselves suddenly swimming in the surf of China's economic and commercial explosion at any point since the early 1980s may have wondered just exactly what was going on. Few in business have failed to sense that something bigger was under way, of which their venture, sale, or contract was somehow just a tiny part. But the architecture of those larger changes remained obscure.

David Zweig calls this process "internationalization" and defines it as "the expanded flows of goods, services, and people across state boundaries, thereby increasing the share of transnational exchanges relative to domestic ones, along with a decline in the level of regulation affecting those flows."

He examines four sectors of Chinese life in which internationalization proceeded after the end of the Cultural Revolution and the return of Deng Xiaoping to supreme power: urban life, the rural economy, higher education, and—in a different vein—what he calls "the struggle over overseas development assistance."

From the start, internationalization spelled opportunity (including the opportunity for financial gain) for many Chinese. The chance to recruit foreign investment, export to foreign buyers, get a fellowship and study abroad, receive assistance from the World Bank or some enterprising foreign nongovernmental organization was instantly compelling. It changed minds, perspectives, lives. And it wound up changing the dynamics of China's economic and bureaucratic order.

Central government policy changes played their roles: If Deng had not personally encouraged foreign investment, or the establishment of special economic zones, or study abroad, processes that led to the weakening or dissolution of the old-time instruments of control and monopolization of power would not have started bubbling. But Zweig's book makes clear that, once the notion of opportunity and self-promotion began to ferment, a collective momentum drove China toward a culture of opportunistic entrepreneurialism.

Bureaucrats and officials at various levels of Chinese administration discover economic opportunities falling into their hands. Some thrive on "rents," Zweig's lingo for unearned or illegitimate income, including corrupt payoffs. Others take a piece of the business they are supposed to regulate.

Zweig's portrayal of a closed and politically hamstrung society evolving helter-skelter into a remarkably more fluid one should be encouraging to the many observers of China who wonder whether, for example, foreign business plays a constructive role in the development of a more institutionally and ethically progressive society in the PRC. While most of China's increasingly market- and law-oriented behavior has resulted from the needs and wishes of the Chinese themselves, Zweig leaves no doubt that international commercial engagement with China was critical in pushing changes forward.

One of the most interesting of Zweig's observations is that the process of internationalization, so corrosive to so many established economic and bureaucratic interests, proceeded without the emergence of decisive opposition, despite periodic bursts of concern. Zweig notes that China's entry into the World Trade Organization (WTO) in 2001 finally sounded the alarm for economic sectors and bureaucratic champions who could see extreme danger in China's WTO laundry list of commitments to liberalization. He notes, as well, the political significance of some of the side effects of internationalization, such as the opening of immense gaps in living standards between the dynamic internationalist coastal region and the far more conservative noncoastal areas of China.

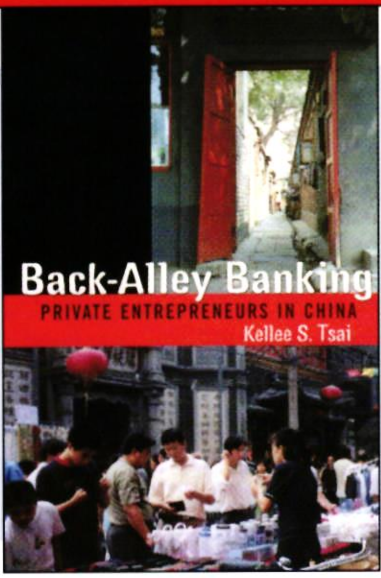
Zweig notes, too, the dangers of incomplete transformation, in which the internationalizing process undermines the institutions of governance and social control, but new guarantees of government integrity and social discipline fail to emerge in time to prevent society from falling into unending corruption and abuse of power by privileged elites.

But in the end, Zweig argues that internationalization is irreversible and more likely to conduce to increasingly positive social and political development; on this he is, in his scholarly way, very optimistic.

Internationalizing China will appeal heavily to scholars and social scientists bent on dissecting the complex phenomena that swept over the Chinese economy in the 1980s and 1990s. And for businesspeople who lived and worked their way through these transformations, and who have a long air trip or other interval for quiet, concentrated reading, Zweig's book will offer valuable insights and perspectives.

—*Robert A. Kapp*

Robert A. Kapp is president of The US-China Business Council.



Back-Alley Banking: Private Entrepreneurs in China

by Kellee Tsai
Ithaca, New York: Cornell University Press, 2002
316 pp. $35 hardcover

Through most of the 1990s, China's average annual economic growth ranked first in the world, based upon World Bank figures, with an astonishing 11.2 percent rate. Questions concerning the how and why of China's two-decade-long economic expansion abound. The "why" explanation brings us back to classic neoliberal economic theory: a convergence of abundant labor and capital. But the more salient question is *how* does China keep its economic engine humming? Given the oligarchic nature of Chinese politics and policy directives to state banks to lend to large, inefficient state-owned enterprises, we ought to witness tremendous market distortions. Yet, such distortions are not apparent. Kellee Tsai, an assistant professor of political science at Johns Hopkins University in Baltimore, has found a partial answer to this question in her research on informal financing networks.

Tsai's scholarship is the culmination of two years of thorough field work. She digs deep into China's commercial life and takes the pulse of the informal financial arteries that trace their genesis to imperial China. In *Back-Alley Banking*, Tsai argues that informal financing networks are the bedrock of China's economic robustness. Tsai is primarily concerned with an economic policy paradox in China: though growth increasingly depends upon the private sector, in particular the 30 million new private businesses that have sprouted in post-Mao China, burdensome and restrictive lending requirements for private enterprises discourage borrowing through official channels. In one humorous account, a Chinese entrepreneur, who was forced to turn to an informal financing network for a loan, tells Tsai, "A state bank wouldn't give me a loan if Chairman Mao himself rose from the dead and told them to give me one!"

Tsai reveals that, as of 2000, *less than one percent* of loans from the entire national banking system are allocated to the private sector. *Hui*, or unofficial rotating credit associations, are thus the main source of financing for most of China's entrepreneurs. Various types of *hui* have existed in China since the Tang Dynasty (618-907 AD) but their prominence in China's credit market today is remarkable.

Informal credit networks vary greatly even among similarly situated entrepreneurs. Tsai argues that the entrepreneurs have different political and social identities. Those with stronger social or political ties, such as the businesses that have successfully curried favor with government officials, have an opportunity to borrow through more institutionalized finance channels and pay lower rates of interest.

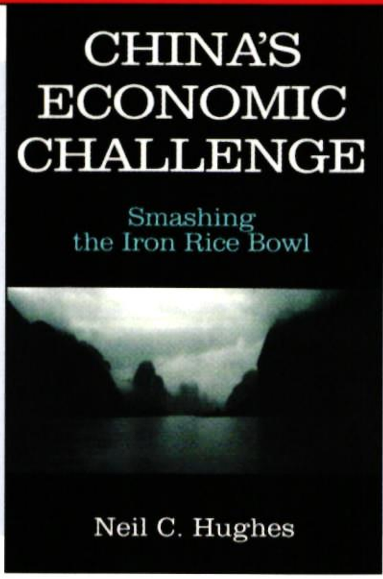
Tsai also attempts to explain why "localities with comparable economic structures and, presumably, comparable levels of demand for private finance exhibit dramatic variation in curb market activity." Her answer is one that is often overlooked—the developmental policies of the first three decades under Mao contributed, ironically, to the financial success of certain areas because the dearth of investment and industrial policies compelled those areas to turn to entrepreneurial activities to survive. The prime example is Wenzhou.

Wenzhou, a district in the southern coastal province of Zhejiang, was neglected by state planners under Mao (because of its proximity to Taiwan) but thrives under capitalism today. "Although Wenzhou accounts for 11 percent of the province's land mass and 15 percent of its population, it received only 1 percent of Zhejiang's fixed capital investment throughout the Mao era," Tsai writes. But by the mid-1980s, "Wenzhou's private economy flourished...in tandem with its informal financial sector, which both defied and competed with formal financial institutions." In Wenzhou, the so-called "Red Hat Disguise," in which a private entrepreneur associates his or her business with a state-owned business or registers as a collective enterprise to tap into the formal financing networks, was rampant. As access to capital became easier for private entrepreneurs, informal lending institutions, such as *hui*, competed aggressively to lend money. Wenzhou's dynamism, it seems, springs from an instinct for survival, as seen in the hours kept by informal lending institutions, some of which are open 24 hours a day, seven days a week.

This book should be required reading for faculty and students focusing on China's political economy. Private entrepreneurs venturing into China should also avail themselves of this work. It is replete with statistical data on the macro effects of the informal finance network in China. Tsai has done academic and business interests a tremendous service by documenting how private entrepreneurs use informal financial networks.

—*Mark T. Fung*

Mark T. Fung is a PhD candidate in China Studies at the Paul H. Nitze School of Advanced International Studies at Johns Hopkins University and is on the Term Member Advisory Committee at the Council on Foreign Relations in Washington, DC.



China's Economic Challenge: Smashing the Iron Rice Bowl

by Neil C. Hughes
Armonk, NY: M.E. Sharpe, 2002.
235 pp. $24.95 hardcover

Smashing the iron rice bowl is more than an economic challenge for China. Economic reform and liberalization initiated by Deng Xiaoping in the late 1970s has opened the gates for a flood of economic, political, and social challenges for the government and its people—insolvent banks, limited cropland and bulging cities, a deteriorating environment, booming telecommunications and information industries that test the government's ability to filter information, and waning political legitimacy. In *China's Economic Challenge: Smashing the Iron Rice Bowl*, Neil Hughes provides a sweeping account of all that ails China today. Hughes is not a China expert, but spent several years helping Chinese officials and state-owned enterprise managers implement economic reforms as an industrial and financial specialist with the World Bank. His book is a quick read, packed with information and analysis, and suitable for those new to the China scene as well as those already immersed in it.

After a short analysis of China's banking structure and reforms, Hughes concludes that the government must break the dependency of inefficient, unprofitable state-owned enterprises on China's banks. Hughes moves on to discuss agriculture, recounting the story of rural decollectivization and exploring the debate, popularized by the agricultural economist Lester Brown, about China's ability to feed itself in the coming decades.

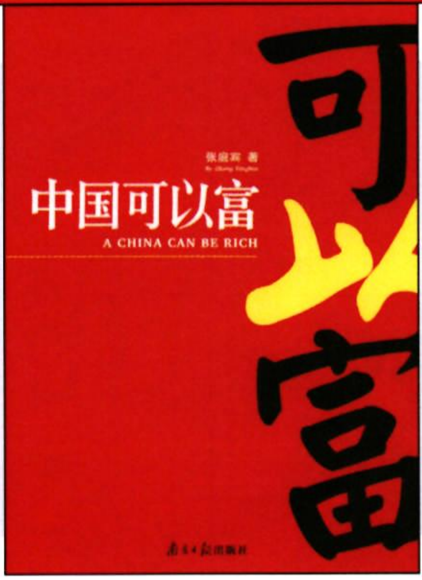
Environmental problems, some of which are a consequence of current economic reform and others of long standing, pose considerable challenges to economic reform as the PRC government prioritizes development needs. While Hughes praises China for its recent focus on environmental issues, he points out areas that need still more attention. The chapter on urbanization makes the point (among others) that—contrary to the plans of the PRC government and domestic and foreign automakers—"there is no place in China's crowded cities for the private automobile." Continuing on the theme of environmental degradation and its human costs, a chapter on the Three Gorges Dam revisits the debate over the assertion that the benefits of electric power and flood control provided by the dam outweigh the damage to the environment, the money spent on construction, and the costs of relocating millions of inhabitants. (Hughes does not come down on one side or the other of this debate.)

Telecommunications and access to information round out the range of issues in the book. Beginning with the first telegraph line installed in China in 1877, guiding the reader through the reshuffling of China's telecom giants in the 1990s, and ending with the rise in Internet use, Hughes implies that China will move in fits and starts down the information highway as the PRC government struggles with its role as "Cyberspace Gatekeeper." Hughes concludes the book with a quick look at political and legal reform and the looming question of the future of the Chinese Communist Party.

With tidbits ranging from the historical use of cowrie shells as a medium of exchange to municipal sewage and industrial effluent ratios, Hughes's detailed book gives context to China's current reform efforts. And throughout, Hughes cites the lack of regulatory structures and accountability as a source of continued difficulty in reform. Though he is optimistic about the effect of China's World Trade Organization membership on the issues he addresses, Hughes points out that the future of politics in China will also be a major determinant in the ultimate success of economic reform.

—Rebecca Karnak

Rebecca Karnak is *The CBR's* research assistant.



China Can Get Rich

by Zhang Tingbin
Guangzhou: Nanfang Daily Publishing House, 2002
468pp.¥29.80 ($3.60) softcover

Amidst all the questions about the quality of China's economic growth and the concern over increasing inequality in Chinese society, up-and-coming journalist Zhang Tingbin has produced a book with an eye-catching title that affirms that, yes, China indeed can become a rich country—an aspiration targeted in the century-old slogan "*fuguo qiangbin*" (rich country, strong military).

China Can Get Rich profiles rags-to-riches entrepreneurs and professional businesspeople from the mainland that have made millions. The author, a member of the editorial board of the *21st Century Business Herald* newspaper, published by the leading *Southern Daily* newspaper group in Guangzhou, uses interviews with 23 Chinese business elites as the basis of this book. These interviewees are members of a group he calls the vanguard of the rich—a sharp contrast to the "vanguard of the proletariat" of less than 50 years ago.

Before delving into case-study interviews, Zhang argues that China is on the brink of becoming a wealthy society. Focusing only on the period since 1995, Zhang argues that China has the momentum to propel itself into the ranks of rich nations, as Chinese entrepreneurs are now reaching the end of the long road to success, which took them through difficulty, exploration, and breakthrough, and is culminating in creation. In the individual profiles, the author provides glimpses into the business elite's secrets of success. Zhang categorizes these success stories into two groups: self-made businesspeople and those thriving in professional positions.

One individual profiled is 43 year old Wang Licheng, chair of the board of Zhejiang's Holley (Hua Li) Group. Wang reached the pinnacle of success from humble small village beginnings. He started his career as a technician, finished university through distance learning, and worked as a foreman in the then-small Holley Group factory at the age of 27. Thanks to perseverance and good investments, Wang, in the course of only eight years, expanded Holley from a small collective to a $300 million joint-stock company that is China's largest producer of electric meters. Wang has recently led Holley into pharmaceuticals and telecommunications with a high-profile acquisition of the technology rights to Royal Philips Electronics NV's CDMA technology. Other individuals profiled include Zhang Shengman, the youngest general deputy chair of the World Bank, and Fred Hu Zuliu, managing director for Asia Pacific Economics at Goldman Sachs Group.

Zhang concludes with a call for optimism about China's ability to become rich for four reasons. First, China's entry into the World Trade Organization offers the country tremendous opportunities for growth. Second, many of China's industries possess global competitive advantages in labor and technology. Third, China is going through a period of financial innovation that will lead to stronger fundamentals for growth. Finally, the Chinese people's cooperation with, and achievements in, the world economy will help boost China into the ranks of developed countries.

Though Zhang identifies factors that hinder the realization of China's growth potential, such as the prevalence of fraud and lack of investment opportunities, his study generally relies on the evidence of individual success stories to support his optimistic view. In many ways the book parallels the Horatio Alger stories that fed American rags-to-riches dreams a hundred years ago.

One must wonder, though, if China's true path to wealth ultimately lies in an institution that allows most Chinese to become "well-off"—as the Chinese Communist Party's latest slogan puts it—rather than rich. Time will tell if books such as *China Can Get Rich* continue to fly off the shelves or if stories focusing on middle-class prosperity take their place.

—Brian Goldstein and Sharon Liu

Brian Goldstein is research manager at the Council's Beijing office. Sharon Liu is an intern at the Council's Beijing office and will work for KPMG after graduating from Beijing University.

Sales and Investment

NOVEMBER 16, 2002 – JANUARY 15, 2003

Compiled by Rebecca Karnak

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 rate quoted in the International Monetary Fund's International Financial Statistics.

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 editor.

Accounting and Insurance

INVESTMENTS IN CHINA

Aviva plc (UK)/COFCO (Zhejiang)
Formed insurance joint venture, AVIVA COFCO Life Insurance Co. Ltd., and began operations in Guangzhou. $60.5 million. 01/03.

CIGNA Corp. (US)/SDZ Investment Consulting Co., Ltd., a unit of China Merchants Group (Guangdong)
Will form joint venture, CIGNA & CMC Life Insurance Co., Ltd., in Shenzhen. (US:50%-PRC:50%). $24.2 million. 12/02.

ING Groep NV (the Netherlands)/Bejing Capital Group
Will form life insurance joint venture, ING Capital Life, in Dalian, Liaoning. (the Netherlands:50%-PRC:50%). $24 million. 12/02.

OTHER

Aon Corp. (US)/COFCO (Zhejiang)
Received approval for insurance brokerage license for its joint venture, Aon-COFCO, to be based in Shanghai. 01/03.

AIU Insurance Co. (US), China Pacific Insurance (Group) Co. Ltd. (Beijing), People's Insurance Co. of China (Fujian), Ping' An Insurance Co. Ltd. (Guangdong)
Signed $4 billion policy to insure integrated petrochemical complex of BASF-YPC Co. Ltd. of Jiangsu, a joint venture between BASF AG and Sinopec. 12/02.

Advertising and Public Relations

INVESTMENTS IN CHINA

Tom.com Ltd. (Hong Kong)/Charm Art & Advertising Co. (Beijing)
Will form advertising joint venture. (Hong Kong:60%-PRC:40%). $2.4 million. 11/02.

Tom.com Ltd. (Hong Kong)/Henan Ming Sheng Advertising
Will form advertising joint venture. (Hong Kong:51%-PRC:49%). $123,000. 11/02.

OTHER

Nike, Inc. (US)/Sina.com (Beijing)
Formed an alliance for an online sports channel. 12/02.

Agricultural Commodities and Technology

INVESTMENTS IN CHINA

Nissho Iwai Corp. (Japan)/Zhangzi Isle Fishery Group Co. Ltd. (Heilongjiang)
Will form a tunny-processing joint venture, Xiangxiang Foodstuff Co. Ltd, in Dalian, Liaoning. (Japan:51%-PRC:49%). $8.6 million. 01/03.

CK Life Sciences International (Holdings) Inc. (Hong Kong)/Nanjing Red Sun Co. (Jiangsu)
Set up joint venture to promote and distribute eco-fertilizer products. (US:40%-PRC:60%). 12/02.

Pioneer Hi-Bred International Inc., a unit of E.I. du Pont de Nemours & Co. (US)/Denghai Seed Group (Shandong)
Will form a joint venture, Shandong Denghai Pioneer Seeds Co., to produce corn hybrids. 12/02.

OTHER

Governments of Belgium, France, Italy, Spain, and the Netherlands/Hebei Provincial Government
Signed 10-year agreement on agricultural cooperation, covering the fields of technology, investment, farm produce, personnel, and information. 12/02.

Banking and Finance

INVESTMENTS IN CHINA

Daiwa Securities Group Inc. (Japan)/Shanghai International Group Corp.
Will set up brokerage joint venture. (Japan:33%-PRC:67%). 01/03.

Citigroup Inc. (US)
Will purchase a 5% stake in Shanghai Pudong Development Bank. $72 million. 12/02.

Abbreviations used throughout text: ABC: Agricultural Bank of China; ADB: Asian Development Bank; ASEAN: Association of Southeast Asian Nations; AVIC I and II: China Aviation Industry Corp. I and II; BOC: Bank of China; CAAC: General Administration of Civil Aviation of China; CATV: cable television; CCB: China Construction Bank; CCTV: China Central Television; CDB: China Development Bank; CDMA: code division multiple access; CEIEC: China National Electronics Import and Export Corp.; China Mobile: China Mobile Communications Corp.; China Netcom: China Netcom Corp. Ltd.; China Railcom: China Railway Communications Co., Ltd.; China Telecom: China Telecommunications Group Corp.; China Unicom: China United Telecommunications Corp.; CIRC: China Insurance Regulatory Commission; CITIC: China International Trust and Investment Corp.; CITS: China International Travel Service; CNOOC: China National Offshore Oil Corp.; CNPC: China National Petroleum & Gas Corp.; COFCO: China National Cereals, Oils, and Foodstuffs Import and Export Corp.; COSCO: China Ocean Shipping Co.; CSRC: China Securities Regulatory Commission; ETDZ: economic and technological development zone; ICBC: Industrial and Commercial Bank of China; MII: Ministry of Information Industry; MOFTEC: Ministry of Foreign Trade and Economic Cooperation; MOU: memorandum of understanding; NA: Not Available; NORINCO: China North Industries Corp.; P&T: Post and Telecommunications; PBOC: People's Bank of China; PetroChina: PetroChina Co., Ltd.; RMB: Renminbi; SARFT: State Administration of Radio, Film, and Television; SEZ: Special Economic Zone; SINOCHEM: China National Chemicals Import-Export Corp.; SINOPEC: China National Petrochemical Corp.; SINOTRANS: China National Foreign Trade Transportation Corp.; SDPC: State Development Planning Commission; UNDP: United Nations Development Program; WFOE: Wholly foreign-owned enterprise

Chenery Capital, Inc., Distressed Asset Consulting LLC (US)/China Oriental Asset Management Co. (Beijing)
Will set up an offshore joint venture to dispose of nonperforming loans. 12/02.

Crédit Lyonnais Securities (Asia) Ltd., a unit of Crédit Lyonnais (France)/Xiangcai Securities Co., Ltd. (Hunan)
Will set up securities joint venture, China Hua-ou International Securities Co., Ltd. (France:33%-PRC:67%). $60 million. 12/02.

Goldman Sachs & Co. (US)/Huarong Asset Management Co. (Beijing)
Set up joint venture, Rongsheng Asset Management Co., to dispose of nonperforming loans. 12/02.

ING Investment Management, a unit of ING Groep NV (the Netherlands)/China Merchants Securities Co., Ltd. (Guangdong), China Power Finance Co., Ltd. (Beijing), China Huaneng Finance Co., Ltd. (Shandong), and COSCO Finance, Ltd. (Beijing)
Will set up mutual fund joint venture, China Merchants Mutual Fund Management Co., in Shenzhen. (the Netherlands:30%-PRC:70%). $12.1 million. 12/02.

Morgan Stanley (US)/Huarong Asset Management Co. (Beijing)
Set up joint venture, First United Asset Management Co., to dispose of nonperforming loans. 12/02.

United Overseas Bank (Singapore)/Shenzhen Capital Group Co., Ltd. (Guangdong)
Set up offshore fund, UOB Venture (Shenzhen) Ltd., in Mauritius to raise money for technology projects in China. 12/02.

OTHER

China Merchants Bank (Guangdong)
Approved to set up a New York City representative office. 12/02.

National Bank of Labor (Italy)/BOC
Signed a cooperation agreement for the extension of credit services and for advisory and information purposes. 12/02.

Bausparkasse Schwaebisch Hall AG (Germany)/CCB
Won approval for savings bank joint venture, Sino-German Housing Savings Bank Co. Ltd., which will open in Tianjin this year. (Germany:24.9%-PRC:75.1%). 11/02.

Fortis NV (Belgium)/Haitong Securities (Shanghai)
Won approval for fund management joint venture. (Belgium:33%-PRC:67%). $12.1 million. 11/02.

Chemicals, Petrochemicals, and Related Equipment

CHINA'S IMPORTS

Chicago Bridge & Iron Co. NV (the Netherlands)
Won design and construction contract for Shanghai Ethylene Cracker Complex (SECCO) storage facility. $40 million. 11/02.

INVESTMENTS IN CHINA

Saudi Arabia Basic Industries Corp./Dalian Shide Group (Liaoning), Jinxi Chemical Corp. (Liaoning), China Oriental Assets Management Co. (Beijing), Huajin Group (Shandong)
Will form joint venture to build petrochemical production units. $5 billion. 01/03.

Consumer Goods

INVESTMENTS IN CHINA

Shinsegae Co. (South Korea)/Shanghai Join Bui Co., Shanghai Trade Center Co.
Will form joint venture, Shanghai E-Mart Super Center Co. (South Korea:49%-PRC:51%). 11/02.

OTHER

China Enterprises Ltd., a unit of China Strategic Holdings Ltd. (Hong Kong)
Will sell its 51% stake in Yinchuan C.S.I. (Greatwall) Rubber Co. to Ningxia Yinchuan Rubber Manufacturing. $4.23 million. 01/03.

Nu Skin Enterprises (US)
Opened 120 retail outlets in Fujian, Guangdong, Jiangsu, Shanghai, and Zhejiang in December 2002. 12/02.

Hitachi Ltd. (Japan)/Hisense Group (Shandong)
Will form joint venture to produce air conditioners for commercial use. (Japan:50%-PRC:50%). $24 million. 11/02.

Electronics and Computer Software

CHINA'S EXPORTS

Semiconductor Manufacturing International Corp. (Beijing)
Will provide Elpida Memory Inc., a joint venture between NEC Corp. and Hitachi Ltd. of Japan, with 10,000 DRAM chips. 01/03.

INVESTMENTS IN CHINA

Infineon Technologies (Germany)/Semiconductor Manufacturing International Corp. (Beijing)
Will form joint venture to produce DRAM chips. 12/02.

LG Electronics Inc. (South Korea)/Longqing Group (Tianjin)
Will expand its home appliance joint venture, LG Electronics (Tianjin) & Electric Appliances Co., to build plants to make air conditioners and motors. $300 million. 12/02.

Mitsui & Co., Ltd. (Japan)/SVA Group Co. Ltd. (Shanghai)
Will form a sales joint venture, SVA Trading Co. Ltd., to focus on liquid crystal display panels and TVs. (Japan:40%-PRC:60%). $20 million. 12/02.

NCsoft Corp. (South Korea)/SINA (Beijing)
Will form joint venture to operate and market Lineage, an online game, in China. 11/02.

OTHER

Agilent Technologies Inc. (US)
Opened Agilent China Communication Technology & Product Development Center in Beijing. 12/02.

BEA Systems Inc. (US)
Will set up an R&D center in China. 12/02.

IBM Corp. (US)/Zhejiang University Innovation Technology
Signed agreement to explore IT application and service market. 12/02.

LG Electronics Inc. (South Korea)
Set up research and development center in Beijing. 12/02.

Matsushita Electric Industrial Co. (Japan)
Will move its TV production base from Osaka to Jinan, Shandong. 12/02.

PalmSource Inc. (US), Group Sense (International) Ltd. (Hong Kong)/Legend Group (Beijing)
Signed licensing agreement. 12/02.

Tengtu International Corp. (Canada)
Signed an agreement to give Legend a discounted license fee on certain educational software in exchange for its pre-installation on servers sold in the education market. 12/02.

Engineering and Construction

INVESTMENTS IN CHINA

Fututech Bhd (Malaysia)/DNP Engineering Co., Ltd.
Will form joint venture to produce outdoor lighting products. (Malaysia:70%-PRC:30%). $483,000. 01/03.

Tensar International Ltd. (UK)/Kaile New Material Science & Technology Co. (Hubei)
Will form joint venture. (UK:49%-PRC:51%). $14.5 million. 01/03.

Compagnie Saint-Gobain SA (France)/Xuzhou General Iron and Steel (Jiangsu)
Will form joint venture to produce flexible tubes. (France:75%-PRC:25%). 12/02.

OTHER

IVG Enterprises Ltd. (Canada)
Sold its 55% stake in its Baise Asia Pacific Concrete joint venture in Baise, Guangxi. $300,000. 11/02.

Environmental Technology and Equipment

OTHER

The Netherlands
Signed agreement with China to improve urban environmental infrastructure in western China. $14.7 million. 12/02.

Food and Food Processing

INVESTMENTS IN CHINA

Want Want Holdings Ltd. (Singapore)/Beijing Huachen Food Co.
Will form joint venture, Beijing Mingwant Foods Ltd. (Singapore:75.6%-PRC:24.4%). $4.8 million. 01/03.

China Resources Breweries, a joint venture of SABMiller plc (UK) and China Resources Enterprise (Hong Kong)
Will purchase remaining 10% stake in three Shenyang breweries to raise ownership to 100%. $18 million. 11/02.

OTHER

Leprino Foods Co., Ltd. (US)
Received approval to build a cheese production enterprise in Shijiazhuang, Hebei. 12/02.

Machinery and Machine Tools

CHINA'S IMPORTS

Valmet-Xian Paper Machinery Co. Ltd., a joint venture of Metso Corp. (Finland)
Will supply Dongguan Jian Hui Paper Co. Ltd. of Guangdong with a machine for the production of coated white lined chipboard. $34 million. 12/02.

INVESTMENTS IN CHINA

FACB Industries Inc. (Malaysia)/Tianjin Pipe Corp.
Will form a joint venture to manufacture stainless steel pipes and fittings. (Malaysia:60%-PRC:40%). $4.2 million. 11/02.

Medical Equipment and Devices

CHINA'S IMPORTS

Varian Medical Systems, Inc. (US), Toshiba Medical Co., Sanko Medical Co. (Japan)
Signed a cooperative agreement to operate an X-ray tube service center in Beijing. 12/02.

Bioneer Corp. (South Korea)
Supplied biotech equipment and test drugs to Gansu Agricultural University. $500,000. 11/02.

Metals, Minerals, and Mining

INVESTMENTS IN CHINA

Afcan Mining Corp. (Canada)
Will acquire 85% stake from Sino Gold Ltd. of Australia in Qinghai Dachaidan Mining Co. $5.6 million. 01/03.

Engelhard Corp. (US)
Bought a controlling stake in state-owned Anping Kaolin Co. in Shanxi. $12 million. 12/02.

Ivanhoe Mines Ltd., Pacific Minerals Inc. (Canada)/Yunnan Provincial Bureau of Geological and Minerals Exploration
Will form copper exploration joint ventures, Yunnan Xinzhao Copper Mineral Co., Ltd. and Yunnan Xindian Copper Minerals Co., Ltd. $11 million. 12/02.

Mitsui and Co. Ltd. (Japan)/Shanghai Baosteel Group Corp.
Set up steel distribution joint venture, Shanghai Bao-Mit. (Japan:35%-PRC:65%). 12/02.

Miscellaneous

CHINA'S INVESTMENTS ABROAD

Xinhua Financial Network Ltd. (Beijing)
Signed an agreement to acquire Asian financial news operations of Agence France-Presse. 12/02.

INVESTMENTS IN CHINA

Vivendi Universal (US)/Shanghai Waigaoqiao Group Co., Shanghai Jinjiang Holdings Co. Ltd.
Will form amusement park joint venture, Shanghai Universal Studios Theme Park. 12/02.

PR Newswire Association LLC (UK)/Xinhua Financial Network (Beijing)
Will set up joint venture, Xinhua PR Newswire, a corporate financial information service aimed at Western audiences. $4 million. 11/02.

OTHER

CDMI Productions Inc. (US)/China Film Group Corp.(Beijing)
Signed letter of intent for an entertainment equipment rental joint venture in Beijing. 01/03.

Heidrick & Struggles International Inc. (US)/Beijing Leading Human Resources Consulting Co.
Formed headhunting joint venture. 12/02.

Newsweek Inc. (US)/SinoWorld CNW Publishing, a subsidiary of Vertex Group (Hong Kong)
Will launch a Chinese-language edition on the mainland and in Hong Kong. 12/02.

Star Group, a unit of News Corp Ltd. (Australia)/Hunan Radio, Film, & Television Group
Will form alliance for programming and financing. 12/02.

RTKL Associates Inc. (US)/Beijing Institute of Architectural Design and Research
Won design competition and broke ground for the Chinese Museum of Film in Beijing. 12/02.

World Bank
Contributed $11 million to commercial forestry project in Shandong. $22 million. 12/02.

***Lianhe Zaobao*, owned by Singapore Press Holdings (Singapore)**
Signed agreement to provide news to the Shanghai edition of *Cankao Xiaoxi*, owned by Xinhua News Agency of Beijing. 11/02.

Packaging, Pulp, and Paper

OTHER

Stora Enso Oyj (Finland)
Will move its Asia-Pacific headquarters from Singapore to Shanghai. 12/02.

Petroleum, Natural Gas, and Related Equipment

CHINA'S IMPORTS

Hyundai Heavy (South Korea)
Won contract from ACT-OG, a joint venture of CNOOC, Chevron Overseas Petroleum, Texaco China BV, and Operators Group, for construction of offshore crude oil extraction, refining, and storage facility. $160 million. 01/03.

Stone & Webster, Inc., a subsidiary of The Shaw Group Inc. (US)
Won contract from CNOOC and Shell Petrochemicals Co. Ltd., a unit of Royal Dutch/Shell Group of the Netherlands, to construct an ethylene plant in Huizhou, Guangdong, with JGC Corp. 01/03.

Stewart & Stevenson Inc. (US)
Will supply three sets of fracturing equipment to China Petroleum & Equipment Corp., under CNPC, for oilfields in Qinghai, Sichuan, and Xinjiang. $21 million. 12/02.

JGC Corp. (Japan)
Won contract from CNOOC and Shell Petrochemicals Co. Ltd. for construction of ethylene plant in Huizhou, Guangdong. $500 million. 11/02.

Technip-Coflexip (France), Chiyoda Corp., Mitsubishi Corp. (Japan)
Won contract from CNOOC and Shell Petrochemicals Co. Ltd., a unit of Royal Dutch/Shell Group of the Netherlands, for engineering, procurement, and construction of petrochemical complex in Huizhou, Guangdong. 11/02.

INVESTMENTS IN CHINA

Xinao Gas Holdings Ltd. (Hong Kong)/Shijiazhuang Gas Group Ltd. (Hebei)
Formed a joint venture to operate a gas distribution network in Shijiazhuang, Hebei. (Hong Kong:70%-PRC:30%). $15.7 million. 01/03.

General Electric Power Systems (US)/Shenyang Blower Works (Liaoning)
Will form a joint venture to provide maintenance equipment and services for oil and gas equipment. (US:75%-PRC:25%). $13.6 million. 12/02.

Husky Oil China Ltd. (Canada)/CNOOC
Signed agreement on oil exploration in South China Sea. 12/02.

China Gas Holdings Ltd. (Hong Kong)
Will invest in China City Gas Construction Investment Co. Ltd. of Henan. $5.45 million. 11/02.

Pharmaceuticals

INVESTMENTS IN CHINA

Ethypharm (France)/Conba Pharmaceuticals Group Co. Ltd. (Zhejiang)
Will form joint venture, Hangzhou Ethypharm-Conba Chinese Medicines R&D Center Co. Ltd., to develop new Chinese medicines. $1.2 million. 11/02.

OTHER

AstraZeneca plc (UK)
Set up its East Asia clinical research center in Shanghai. 12/02.

Ports and Shipping

CHINA'S IMPORTS

Samsung Heavy Industries (South Korea)
Will provide five container vessels to China Shipping Container Lines, through Seaspan International of Canada. 12/02.

INVESTMENTS IN CHINA

Cosco Pacific Ltd. (Hong Kong)
Will purchase a 17.5% stake in Shekou Container Terminals Ltd. from China Ocean Shipping of Shenzhen. $19.9 million. 11/02.

OTHER

Keppel Logistics Foshan, a joint venture between Keppel T&T (Singapore) and Sinotrans Guangdong Co.
Received the Non-Vessel Operating Common Carrier license to speed up operations. 12/02.

Power Generation Equipment

INVESTMENTS IN CHINA

Evercel Inc. (US)
Will acquire the remaining 49.5% stake in its joint venture, Xiamen Three Circles-ERC Battery Corp. of Fujian. 01/03.

OTHER

Korea Electric Power Co. (South Korea)
Signed MOU with Luoyang Shengsheng Power Co. of Henan to build two thermal power plants. (South Korea:51%-PRC:49%). $11.5 million. 01/03.

Steel Industrials Kerala Ltd. (India)/Hunan Chenzhou Electric International Development Corp.
Signed an MOU to form a turbine manufacturing joint venture. (India:30%-PRC:70%). 01/03.

Enron (US)
Will sell its share in Enron International Chengdu Power Ltd., a joint venture with Sichuan Electric Power Co., to Lin Feng Group of Beijing. 12/02.

Telecommunications

CHINA'S IMPORTS

Telefonaktiebolaget LM Ericsson (Sweden)
Will supply an additional $25 million in CDMA2000 1X equipment and services to China Unicom under existing contract. 01/03.

Cisco Systems, Inc. (US)
Won contract to provide China Unicom with packet networking equipment, WLAN routers, LAN exchanges and firewalls. 12/02.

Oy Nokia AB (Sweden)
Won contract for expansion of Gansu Unicom's GSM network. 12/02.

Nortel Networks (Canada)
Won contract from China Unicom for expansion of CDMA and GSM networks. $65 million. 12/02.

Unity Wireless Corp. (Canada)
Won contract to provide ZTE Corp. of Guangdong with power amplifiers for use in their CDMA network. 11/02.

INVESTMENTS IN CHINA

Qualcomm Inc. (US)/China Unicom
Will form joint venture to promote Binary Runtime Environment for Wireless (BREW) technology. 12/02.

OTHER

Alcatel SA (France)
Set up research center in Shanghai. 12/02.

Korea Association of Information & Technology, a subsidiary of Korea's Ministry of Information and Communication/Xinhua Financial Network (Beijing)
Signed an MOU for better cooperation among IT and telecommunications firms in both countries. 12/02.

Transportation

CHINA'S IMPORTS

AB Volvo (Sweden)
Will provide more than 2,000 new buses to Shanghai Sunwin Bus Co. to modernize its fleet for the 2010 Expo. $169 million. 12/02.

INVESTMENTS IN CHINA

Carlson Wagonlit Travel (US)/China Air Service Ltd., a unit of China Sport Industry Co. (Shanghai)
Will form a tourism joint venture, China Travel Management Service Ltd. 01/03.

ET-China (Hong Kong)/China Southern Airlines (Guangdong)
Will form an e-ticket joint venture, China Southern Et-china.com E-Business Co. Ltd. (Hong Kong:49%-PRC:51%). $710,000. 01/03.

Avis Europe plc, a unit of Avis (US)/Shanghai Automotive Industry Sales Corp.
Will form a car rental joint venture, Anji Car Rental & Leasing Co., Ltd., to set up more than 70 car rental outlets across China. (US:50%-PRC:50%). $66 million. 12/02.

Embraer (Brazil)/Harbin Aircraft Industry (Group) Co. Ltd. and Hafei Aviation Industry Co. Ltd. (Heilongjiang), units of China Aviation Industry Corp. II
Will form joint venture to produce regional jets. $25 million. 12/02.

Gammon Skanska Co. Ltd. (Sweden)/Beijing Zhuzong Group Corp.
Formed tunnel construction joint venture to bid for construction of Beijing subway lines 4 and 10. $7.9 million. 12/02.

General Motors Corp. (US)/Shanghai Automotive Industry (Group) Corp.

Will purchase an assembly plant in Shandong through their joint venture, Shanghai GM. 12/02.

Honda Motor Co. (Japan)/Guangzhou Auto Group Corp. (Guangdong), Dongfeng Motor Corp. (Hunan)

Will form export-oriented car production plant in Guangzhou. (Japan:65%-PRC:35%). $194 million. 11/02.

OTHER

China Motor Corp. (Taiwan)/Fujian Auto Industry (Group) Co.

Approved to expand production to sedans through its joint venture, Southeast Motor Co. Ltd. 12/02.

Far Eastern Air Transport Corp. (Taiwan)

Received approval from Beijing and Taiwan governments to operate direct flights (with a stopover in Hong Kong) between Shanghai and Taiwan during the Lunar New Year. 12/02.

Los Angeles World Airport (US)/Beijing Capital Airport Group

Signed agreement to expand information exchange in air traffic and airport operations. 12/02.

Pratt & Whitney, a subsidiary of United Technologies Corp. (US)/China Aviation Supplies Import & Export Group Corp. (Heilongjiang)

Opened their joint venture, China Customer Training Center in Beijing, for maintenance and engineering management training for operators of Pratt & Whitney engines. 12/02.

Governments of Singapore and China

Signed an MOU to further cooperation in civil aviation. 12/02.

Classified

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COUNCIL BULLETIN

UPCOMING EVENTS

Annual Meeting
June 5, 2003
Washington, DC

EVENT WRAP-UP

Washington

January

Issues Luncheon: Business Guidance to the US Government on Integrated Federal Support Services in the China Market Featured Jeffrey Miller, senior vice president for export finance, Export-Import Bank; Geoffrey Jackson, regional director for Asia and assistant to the director, US Trade and Development Agency; Karen Zens, US Foreign and Commercial Service; Jeri Jensen-Moran, director, Trade Promotion and Policy Coordination for the Undersecretary of the International Trade Administration

February

Forecast 2003 Reception Featured US government officials and representatives from China's embassy to the United States

Forecast 2003 Featured Ambassador of the People's Republic of China to the United States, H.E. Yang Jiechi

Issues Luncheon Featured Clifford A. Hart, director for Asian Affairs, National Security Council

Houston

February

China Business 2002: Navigating Changes in China's Energy and Power Sectors Workshop featured Patrick Powers of The US-China Business Council, Mitchell Silk of Allen and Overy, and Xiaolin Li of Songbin Systems International Corp.

San Francisco

February

China Business 2002: Workshop covering the current business climate, options for US firms in China, and marketing and intellectual property protection strategies Featured Patrick Powers, Karen Sutter, and Ann Weeks of The US-China Business Council

Beijing

February

Meeting: Roundtable discussion on the state of business affairs in China and on export control issues Featured Kenneth Juster, US Undersecretary of Commerce for Export Administration

Council's Forecast 2003 Conference Features PRC Ambassador H.E. Yang Jiechi

Council President Robert A. Kapp and Minister Counselor for Commercial Affairs Dai Yunlou of the PRC Embassy at the Council's Forecast reception.

The Council kicked off its annual Forecast conference with a reception on the evening of February 12 that featured guests from the Chinese embassy and the US government.

The next day, the conference began with a panel on political and economic change in China that featured Lyman Miller of the Hoover Institution and the US Naval Postgraduate School and Robert Sutter of Georgetown University. Stephen Roach of Morgan Stanley and Carla Hills of Hills & Co. discussed the future of China's economy. Patrick Norton of O'Melveny & Myers LLP and Eric Altbach of the US State Department spoke on trade strategies. During lunch, H.E. Yang Jiechi, Ambassador of the People's Republic of China to the United States, gave the keynote address on US-China relations and China's view of current global events.

The afternoon panel focused on China's business climate. Patrick Powers, the Council's director of China Operations, provided a general overview of what to expect in 2003. Allen and Overy's Mitchell Silk discussed opportunities and challenges in China's energy sector, followed by David Weller of the Office of the US Trade Representative who spoke about openings in the service sector in China. After the last panel, member company representatives met with Council staffers for tailored, individual strategy sessions.

Deputy Secretary of Commerce Samuel W. Bodman addresses guests at the Council's Forecast reception.

THE CHINA BUSINESS REVIEW

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EDITOR Catherine Gelb

ASSOCIATE EDITOR Virginia A. Hulme

ASSISTANT EDITOR Paula M. Miller

BUSINESS AND MARKETING MANAGER Kattie Lee

ART DIRECTION & PRODUCTION Jon Howard/JHDesign, Inc.

PUBLICATIONS ASSISTANT Naziha Hassan

RESEARCH ASSISTANT Rebecca Karnak

1818 N St., NW Suite 200 Washington, DC 20036-2470
Tel: 202-429-0340 Fax: 202-833-9027
www.chinabusinessreview.com

All commercial inquiries and renewal/purchase orders should be sent to the headquarters address above.

Editor's Note

This issue went to press during a busy and uncertain—and wintry—time in Washington, DC. The US-China Business Council prepared for and held its annual, nearly two-day Forecast conference, demanding the time and attention of every member of the Council staff. The US government announced a heightened terror alert, to the bemusement of some and the anxiety of others among the Washington-based staff of the magazine. Then, a massive snowstorm dumped more than two feet of snow on the Eastern Seaboard. Several inches of rain soon followed.

Despite these obstacles, the staff of the magazine and the Council pulled together and contributed mightily to getting this issue out the door. I would like to take this opportunity to thank everyone involved.

In particular, I would like to thank Gong Xiaoxia, who took on the bulk of the substantial Chinese-English and English-Chinese translations required for this issue. This was a bigger job than we had anticipated, and I cannot thank her enough for her time and effort. Thanks are due to Bob Kapp as well, for lending his language expertise to this effort, among countless other invaluable contributions (not least of which were suggesting the theme of this anniversary issue and identifying possible contributors).

I would also like to thank Eric Lam and Helen Huang, of Insty-Prints in Bethesda, Maryland, who handled the Chinese typesetting for us. Dennis Chen and Brian Goldstein, of the Council's Beijing office, helped with the Chinese editing and proofreading, and Sandra Kauffman with English proofreading, on extremely short notice. (It goes without saying that any remaining errors are the responsibility of the *CBR* staff.)

Finally, I would like to thank our designers, Greg Berger and especially Jon Howard, without whom this redesigned issue would not have been possible.

Catherine Gelb

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Program Director: Gloria González-Micklin
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Business Advisory Services: Karen M. Sutter
1818 N St., NW, Suite 200
Washington, DC 20036
Tel: 202.429.0340
Fax: 202.775.2476
E-mail: info@uschina.org
Websites: *www.uschina.org*
www.chinabusinessreview.com

BEIJING OFFICE

Director of China Operations: Patrick J. Powers
CITIC Building, Suite 10-01
19 Jianguomenwai Dajie
Beijing 100004
Tel: 8610.6592.0727
Fax: 8610.6512.5854
E-mail: info@uschina.org.cn

SHANGHAI OFFICE

Deputy Director of China Operations: Iain K. McDaniels
Jinjiang Hotel, 2312 West Building
59 Maoming Lu
Shanghai 200020
Tel: 8621.6415.2579 Fax: 8621.6415.2584
E-mail: info@uschina.org.cn

US GOVERNMENT OFFICES IN CHINA

EMBASSY

Ambassador: Clark Randt Jr.
Deputy Chief of Mission: Michael W. Marine
Counselor for Economic Affairs: Bob Wang
Agricultural Counselor: Larry Senger
Commercial Counselor: Thomas Lee Boam
3 Xiushui Beijie
Beijing 100600
Tel: 8610.6532.3831
Economic Section Fax: 8610.6532.6422
Website: *www.usembassy-china.org.cn*
Commercial Office: 31st Floor, North Tower, Beijing Kerry Center, Beijing 100020
Tel: 8610.8529.6655
Fax: 8610.8529.6558/6559
E-mail: beijing.office.box@mail.doc.gov
Visa Office Tel: 8610.6532.3431
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CHENGDU CONSULATE GENERAL

Consul General: David. L. Bleyle
Economic/Political Officer: John Fogarty
Political/Economic Officer: Susan Thornton
Commercial Officer: Helen Peterson
4 Lingshiguan Lu
Chengdu, Sichuan Province 610041
Tel: 8628.8558.3992
Fax: 8628.8558.3520
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Tel: 8620.8121.8000
Fax: 8620.8121.9001
Website: *www.usembassy-china.org.cn/english/home/consulate-info.html#guangzhou*
Agricultural/Commercial Office: China Hotel Office Tower, Suites 1262-64
Guangzhou, Guangdong Province 510015
Tel (FCS): 8620.8667.4011
Fax (FCS): 8620.8666.6409
Tel (FAS): 8620.8667.7553
Fax (FAS): 8620.8666.0703

SHANGHAI CONSULATE GENERAL

Consul General: Douglas Spelman
Political/Economic Officer: John Hoover
1469 Huaihai Zhong Lu
Shanghai 200031
Tel: 8621.6433.6880
Fax: 8621.6433.4122
Website: *www.usembassy-china.org.cn/consulates/shanghai*
Agricultural Director: Scott Sindelar
Principal Commercial Officer: Catherine Houghton
Agricultural/Commercial Office:
Shanghai Centre, Suite 631
Shanghai 200040
FCS Tel: 8621.6279.7638 Fax: 8621.6279.7639
FCS E-mail: shanghai.office.box@mail.doc.gov
FAS Tel: 8621.6279.7630 Fax: 8621.6279.8336
FAS E-mail: atos@public.sta.net.cn

SHENYANG CONSULATE GENERAL

Consul General: Mark R. Kennon
Economic Officer: Bruce Hudspeth
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Heping Qu
Shenyang, Liaoning Province 110003
Tel: 8624.2322.1198
Fax: 8624.2322.2374
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Website: *www.usembassy-china.org.cn/consulates/shenyang/index.html*

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Fax: 852.2845.1598
Website: *www.usconsulate.org.hk*
Commercial Tel: 852.2521.1467
Commercial Fax: 852.2845.9800

PRC GOVERNMENT OFFICES IN THE UNITED STATES

EMBASSY

Ambassador: Yang Jiechi
Minister Counselor for Commercial Affairs: Dai Yunlou
2300 Connecticut Avenue, NW
Washington, DC 20008
Tel: 202.625.3350
Fax: 202.337.5848
Website: *www.china-embassy.org*
Visa Office
2201 Wisconsin Avenue, NW, Room 110
Washington, DC 20007
Visa Tel: 202.338.6688
Fax: 202.588.9760
E-mail: chnvisa@bellatlantic.net
Office of Commercial Affairs
2133 Wisconsin Avenue, NW
Washington, DC 20007
Tel: 202.625.3380
Fax: 202.337.5864/5845
E-mail: chinacom@erols.com

CHICAGO CONSULATE GENERAL

Consul General: Xu Jinzhong
Economic/Commercial Consul: Tian Deyou
100 W. Erie Street
Chicago, IL 60610
Tel: 312.803.0109
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Commercial Tel: 312.803.0123/0115, 312.873.0649
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Consul General: Wang Yunxiang
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