THE CHINA BUSINESS REVIEW

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MILITARY MATTERS

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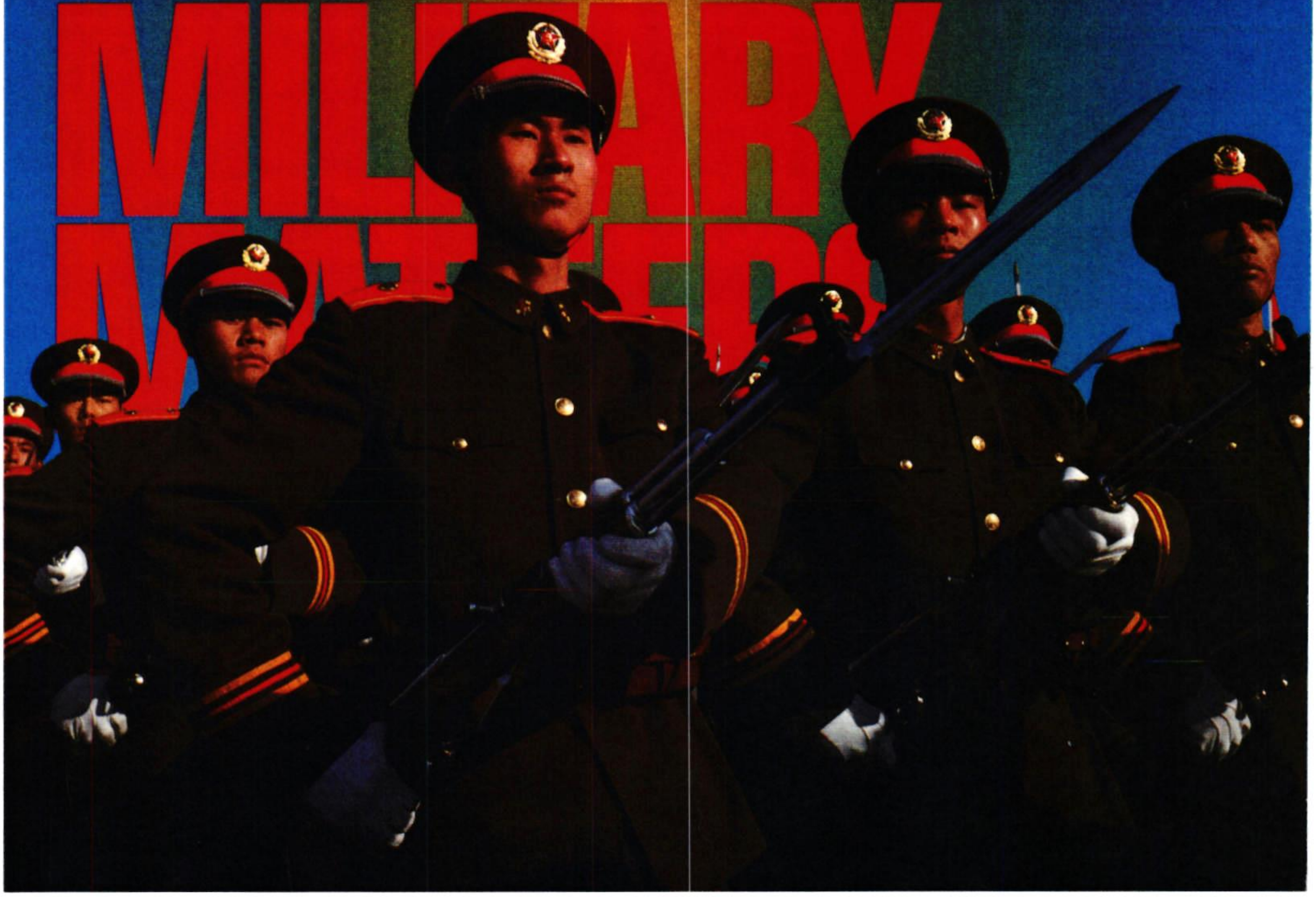

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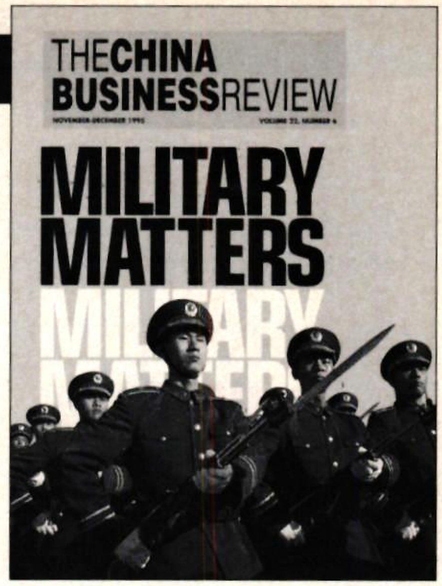

FOCUS: Military Matters

FEATURES

DEPARTMENTS

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On the Road to '97

An October 3 meeting in Britain between PRC Foreign Minister Qian Qichen and British Foreign Secretary Malcolm Rifkind proved upbeat and optimistic about the future. Qian's visit to Britain was the first by a senior Chinese official since 1992, when Hong Kong Governor Christopher Patten launched his democracy proposals for the territory. In addition to a British offer of £100 million ($157 million) in concessionary loans to help China buy UK exports, the two sides reached a four-point agreement on procedural matters regarding the transition of the colony to PRC control.

The accord calls for the establishment of a liaison office to facilitate contacts between the colonial administration and China's Preparatory Committee. Britain has feared that without close cooperation with the senior officials the committee selects for the post-1997 government, the transition could be chaotic. The two sides agreed to allow consultations between senior Hong Kong civil servants and Chinese officials to ensure administrative continuity. The two countries are also set to intensify their efforts to finalize plans for the development of Hong Kong's container port. China also agreed to Britain's request to open a consulate in Guangzhou.

Qian's visit followed on the heels of the first—and perhaps last—elections for all 60 Legislative Council (LegCo) seats on September 17. The pro-democracy Democratic Party (DP) emerged as the major force in the body, winning 19 seats. The DP should gain support from liberal-leaning independents and allied parties, meaning pro-democracy forces will occupy nearly half the chamber and will therefore play a critical role in shaping Hong Kong's transition to Chinese sovereignty. The Democratic Alliance for the Betterment of Hong Kong (DAB) party, a pro-Beijing group, won seven seats, but Liberal Party and conservative independents will strengthen DAB's position on certain China-related issues. Beijing has vowed to dismantle LegCo in 1997, though Qian avoided the subject in his meeting with Rifkind.

The elections raise the question of how the new legislature will approach sensitive political issues likely to irk Beijing, and how the PRC in turn will react. In a speech before LegCo on October 11, Patten vowed to veto any legislation he viewed to be contrary to Hong Kong's best interests. Ironically, it was Patten who, in 1992, introduced the election reforms that led to the victory of pro-democracy forces who now are likely to seek to amend past Sino-British agreements, such as the one relating to Hong Kong's legal system, and introduce immigration and social welfare reforms. Patten made clear in his speech, however, that he will quash bills that directly challenge the 1984 Basic Law or his government's reading of the law.

—Pamela Baldinger and Kirsten A. Sylvester

SHORT TAKES

Dollar Peg to Remain

A recent Goldman Sachs report maintains that the Hong Kong dollar will remain pegged to the US dollar after the 1997 handover. The peg is backed by Hong Kong's Basic Law. China may even use its own reserves to defend the link in order to keep the territory in the black, according to Goldman Sachs.

Examining Examiners

More than 1,800 overseas accountants took the China Accountant Certification Test in September, a sixfold increase over the candidates in 1994. Nearly 1,200 of the examinees were accountants from Hong Kong, Japan, Singapore, the United States, and other countries. Most of the overseas candidates were already certified accountants in their own countries, but needed to obtain Chinese certification to practice in China. The test covered financial management, auditing practices, economic law, and taxation law.

Fast-Moving Chicken Feet

American poultry producers have found Hong Kong and China to be lucrative markets for chicken feet, according to a report by the *Journal of Commerce.* Though discarded in the past or blended with feathers to produce feed meal, exports of US chicken feet, considered a delicacy in Asia, now fetch over $100 million annually—nothing to cluck at.

Out with the Old

Ministry of Civil Affairs official Tang Jinsu, speaking at a Hong Kong legal reform seminar in September, stated that 500,000 village committee leaders in 16 provinces in China will be directly elected by secret ballot by the end of this year. The village elections will be held for the posts of village committee chairman and vice-chairman. Previously, non-elected district committees selected people to fill these positions. The vast majority of China's more than 4.5 million village committee cadres were selected by the Chinese Communist Party.

Village committee chairmen are responsible for the daily affairs of government, including road building, management of local economies, and the implementation of national and provincial policies regarding taxation, grain quotas, and family planning. The 1987 Village Committee Organization Law specifies that office holders are to be chosen through direct election, but few villages have followed the law. Tang indicated that the heightened emphasis on grassroots elections is part of the drive to reduce political corruption.

Letter from the Editor

It's time again to wrap up another year at *The China Business Review.* We hope you've enjoyed the wide range of topics we've covered, including the WTO picture, an "A to Z" of investing in China, and this issue's special focus on Asian security and China's military transformation. Is China a threat to Asian security, and where is the PLA headed? See what the experts have to say.

And stay tuned for 1996—we have an action-packed agenda in the works for our 23rd year of publication. Forces for change on the labor front, new tax and tariff developments, a look at the true size of the Chinese economy, and what's happening in the electronics and telecommunications sectors—these are just a sampling of the topics we plan to cover. Have a nagging question about how to do business in the PRC? Let me know what's on your mind and how we can help. Want to share a funny adventure with our readers or contribute an article about your business dealings? Fax me your ideas! We look forward to working for you and with you in the coming year.

Best wishes,

Vanessa Lide Whitcomb

Vanessa Lide Whitcomb
Editor

More Tax Changes Loom

Council sources believe that China's central government has decided to make significant changes in the taxes that foreign investors must pay. Beijing appears likely to withdraw the long-standing tax exemption on imports of capital equipment for foreign-invested projects, effective January 1996. Although officials have suggested that projects signed before the end of the year would remain eligible for the exemption, the new policy could impair the viability of many foreign-invested enterprises now in the planning stages.

Foreign investors in heavy industrial sectors such as chemicals, autos, and power equipment estimate that capital equipment accounts for 50-60 percent of their China investment dollars. They also estimate that the average tariff on capital imports, from which they are currently exempted, is 25-30 percent. After adding a 17 percent value-added tax (VAT) assessed on imported capital equipment, calculated on top of the tariff, the cost of an investment in these sectors could jump by more than 25 percent. Because of their high equipment requirements, high-tech enterprises could find their costs rising by as much as 50 percent.

Persistent but unconfirmed rumors are also circulating in Beijing that the reimbursement rate for VAT on inputs used in products to be exported may be reduced further. The reimbursement rate was cut earlier this year from 17 percent to 14 percent on exports of most products (*see The CBR*, September-October 1995, p.4). Also under review is the duty-free status of imports used for export processing, reflecting official concern over the fact that many such imports are never actually re-exported.

The tax changes under consideration are part of a tax code overhaul mandated by China's top leadership to eliminate loopholes and make the tax system more consistent with World Trade Organization standards. The central government's moves to simplify the tax code likely will be accompanied by reductions—albeit modest ones—in tariff rates. While many business analysts support China's efforts to make its tax regime more predictable and uniform, the US business community in China remains opposed to the imposition of taxes on capital imports and the reduction of the VAT refund.

—Anne Stevenson-Yang

Anne Stevenson-Yang is director of the Council's Beijing office.

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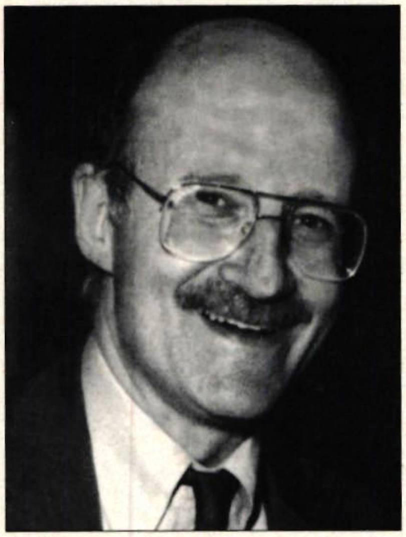

Robert A. Kapp

A Clean Slate

Clinton and Jiang have new trails to blaze

It's Sunday morning in Shanghai, and the hotel business center is crashing to the sound of a very labor-intensive remodeling. Drills grind, hammers clang, and everyone is talking. Just the atmosphere for a quiet contemplation of the dilemmas of US-China relations and the concerns of US business.

At this mid-October writing, a presidential summit meeting lies just over the horizon. The public acrimony of the past four months has not fully died down, but the layered process of mid- to high-level consultations has recommenced. At long last, the Chinese have agreed to accept former Senator James Sasser as the new US ambassador to Beijing once he receives Senate confirmation. Barring unforeseen catastrophes, Clinton and Jiang both will be in New York for the 50th aniversary of the United Nations, and will meet for talks on October 24.

Since US-China business ties, for all their frictions, have been a model of positive bilateral progress, and since the economic interests of the two nations are now unmistakably intertwined, US business perspectives ought to have a bearing on the outcome of any presidential meeting.

Some observers say the best we should hope for is the usual "frank exchange of views," lightly dusted with powdered-sugar reaffirmations of the importance of the bilateral relationship. I'm of a somewhat different view. After all the recent and accumulated unpleasantness between the two sides, a presidential meeting that produces nothing but stale rituals might be worse than no meeting at all. If the two governments progress to the point of summitry, however brief, their interests lie in achieving something of value for their respective nations—"deliverables," in Washington-speak.

What might US business like to see in a bilateral presidential meeting? Let's think out loud:

■ **A respectful and disciplined tone** A rancorous and dispiriting confrontation is hardly likely to produce useful results. The two nations must consciously remember why they have grounds to respect one another—and their leaders must carefully and publicly enunciate this mutual respect. It is not enough to have dignified or even cordial exchanges behind closed doors, only to posture stridently before the media. The leaders of both governments can and should work together to restore the basic grounds of mutual respect for each other's ideals, institutions, and achievements.

■ **No more "teaching lessons"** Nothing dulls the palate more quickly than a steaming dish of bilateral moralizing; it is deadly fare. Remodeling the other country's value systems and traditions should not be the explicit or implicit purpose of either government. The two nations diverge on many ethical issues, and neither is about to convert the other. Should we

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identify our differences? Absolutely. It's better to see them than to trip on them. But crusading and converting is a sure recipe for disappointment and failure.

■ **Progress on stabilizing the bilateral relationship** The past several years of US-China relations have been characterized by successive shocks and disruptions. Businesspeople, with their massive accumulations of on-the-ground experience, know better than anyone that change is a constant in today's China. Our Chinese friends have had some blunt reminders that the wind blowing from the United States can shift as well.

Nevertheless, there's a limit: business needs stability and predictability wherever it can find them. Some uncertainty lies beyond human or governmental control, but surprises can be minimized by conscious effort. The two governments can and must do a better job of identifying and averting destructive shocks to our bilateral relations, and managing the impacts of important changes as they take place. If this requires a willingness to discuss issues that until now have been rigidly defended as "internal" and beyond the scope of bilateral consultation, so be it. The two leaders should preside over a careful and determined effort to anticipate and prevent the sharp economic and political blows that have done so much damage in the last several years.

■ **Greater efforts to keep the issues in perspective** Tastes differ, of course. One person's bedrock issue is another person's minor irritant. But the two countries have increasingly failed to distinguish the major from the minor, and the results have been distressing. In Washington, the politicization of China policy has turned every momentary dissatisfaction into a loud clash of East and West. In Beijing, the increasingly widespread notion of an all-encompassing American "plot" to weaken and divide China provides a convenient but fallacious explanation under which to lump whatever some domestic political or economic interest group finds offensive about the United States.

The two leaders should work hard to reach a shared vision of the primary, the secondary, and the tertiary among their nations' disputes. The lesser issues—historical leftovers, failed gestures, annoying but ineffective bureaucratic obstacles to smoother relations—should simply be taken off the table to keep them from cluttering the roadway to better relations. On the middle-range issues, including the major disputes over China's accession to the World Trade Organization and allegations about PRC weapons exports, the leaders should lend their weight to prompt resolution through negotiation and compromise, with the explicit understanding that remaining static on the issues is itself corrosive and unacceptable. Those issues that the two sides concur are fundamental and presently irreconcilable should at least be carefully and publicly defined, so that all may know where the most dangerous diplomatic and economic hazards lie.

■ **A commitment to the future** While it is important that the US and Chinese presidents clean up as much of the debris from previous years as they can, it is equally vital that they look forward. Common sense tells most of us that the United States and China cannot and should not turn their backs on each other—for the sake not only of their own national interests but for the health of the world. It is time to "re-normalize" US-China relations, with a renewed commitment to cooperation in areas of mutual concern. After all, scientific and technical collaboration, legislative exchanges, and joint environmental efforts, among other areas, were the early building blocks of Sino-American government cooperation.

■ **A renewal of leadership** The standard wisdom today is that neither the US nor Chinese political leadership can afford to act boldly, least of all in relations with the other. But standing tall is only one component of leadership, and not a very elevated component at that. It's a long time ago, but in 1972, American and Chinese leaders alike really showed their skills. Of course, the times were different and so were the personalities.

Today, the two countries appear to be more adrift than diametrically opposed. There is more room for positive and constructive leadership, asserted in a calm and dignified way, than most observers seem willing to admit. Let the two presidents make at least one or two strong moves to improve US-China ties in the face of predictable domestic grumbling; they will, I believe, be pleasantly surprised at the results.

Will the upcoming presidential meeting follow this wish list? We can't expect miracles; indeed, something could always derail the summit at the last minute. But the US businesses that do the heavy lifting in US-China relations these days have a right to hope for—even to expect—results from their governmental colleagues these days; so, I believe, do their Chinese partners. If, thanks to a strong and positive meeting of the leaders of the US and Chinese governments, relations between these two giant economies can again face forward, trade and investment will provide the lion's share of the national benefits to each country and much of the glue needed to hold the structure together.

If the two presidents, however, recite mechanically the familiar statements of their own first principles and unalterable positions, the results of the October 24 meeting may well leave American firms wishing that 1995 had been the 49th, or the 51st, anniversary of the United Nations, and that the US and Chinese leaders had made other plans. 完

FOCUS

The Paradoxes of Asian Security

China confronts new challenges in a post-Cold War world

Roxane D.V. Sismanidis

For several years, China analysts have debated whether China constitutes a threat to Asia's security. Some scholars contend that the PRC's rapid economic growth, double-digit increases in defense spending, and ongoing military modernization program indicate that Beijing will become the new hegemon in Asia and confront the United States. By contrast, Chinese leaders argue that China's growing economic and military power is a normal development commensurate with its burgeoning economy and that Beijing's military expenditures and military modernization program are moderate. The debate over whether China constitutes a military threat, however, deflects attention from trends in regional security and their impact on Chinese policy.

A new world

Rather than focus solely on China's military buildup, a more productive approach is to look at Beijing's actions in terms of four current paradoxes of security in Asia. First, although East Asia currently enjoys its most benign security situation in decades, there has never been greater strategic uncertainty about the security environment. Security dialogue and "trust-building" figure prominently on bilateral and multilateral agendas and led to the establishment of the ASEAN Regional Forum in 1994 to provide a multilateral venue to address regional security issues. Nonetheless, uncertainty about the roles and intentions of the four major powers in Asia—the United States, China, Japan, and Russia—worries security planners and raises questions about long-term peace and stability in the region.

Second, much of the Cold War security structure in Asia has persisted despite the demise of the bipolar system. Though some bilateral alliances and friendship treaties provide stability and continuity in regional relations, others constrain dialogue and adjustments in the post-bipolar security environment. For example, although ASEAN has transcended its Cold War origins with the admission of Vietnam, deployments of military forces on the Korean peninsula and in Japan still reflect the absence of an end to the Korean War.

Bilateral and multilateral arms control treaties and institutions, such as the Nonproliferation Treaty (NPT) and the Missile Technology Control Regime (MTCR), continue to provide the only legal and institutional framework for dealing with the proliferation of weapons of mass destruction. Solutions to the problems of halting Indo-Pakistani nuclear competition, ending China's nuclear and missile cooperation with Pakistan and Iran, and implementing the Agreed Framework for ending North Korea's nuclear weapons program must be found within the existing arms control regimes.

Third, although East Asia's security environment is relatively tranquil, Central and South Asia face serious problems. Tensions between India and Pakistan, Iran's increasing regional influence, the civil war in Afghanistan, weak governing institutions in the poverty-stricken Central Asian countries, and the potential challenges to government authority from Islamic fundamentalists have heightened the instability of the region.

■ Roxane D.V. Sismanidis is a research associate at the Johns Hopkins University School of Advanced International Studies. The views expressed in this article are those of the author and do not necessarily reflect the views of the United States Institute of Peace, which provided funding for the author's research.

Fourth, economic growth in Asia has both stabilizing and destabilizing security implications. Economic development and growing trade have raised living standards and created a web of interdependence among nations, fostering both internal and cross-border stability. However, by promoting the mobilization of new groups into the political arena, economic growth carries potentially destabilizing domestic political consequences that threaten regional security. Sustained economic growth has also enabled Asian governments to devote greater resources to modernizing their military forces, which could entail the emergence of new arms races in the future (*see* p.12).

An eye on the United States...

Chinese security perceptions and policies reflect these four paradoxes. The Chinese leadership recognizes that the post-Soviet security environment in East Asia is relatively peaceful but views global trends as increasingly unstable because of the reemergence of ethnic, religious, and territorial disputes long suppressed by the Cold War. The leadership regards the United States as the dominant military power, trying to take advantage of the Soviet collapse to assert its global hegemony. Chinese analysts also believe that the emerging multipolar system offers China opportunities to become a global power because of Russia's weakness, declining American diplomatic and economic influence, and the rise of Europe and Japan.

The key to understanding Chinese security perceptions and policies lies in Beijing's assessment that the United States is obstructing the PRC's march to great power status. Since the Tiananmen Square crackdown in June 1989, domestic political concerns have driven Chinese policymaking, leaving Beijing convinced that Washington has targeted China as the next victim of American policies promoting "peaceful evolution" to capitalism—and the demise of the communist regime. Although it appears to contradict the view that US influence in the region is declining, this assessment predisposes the leadership to view Washington's differences with Beijing over arms transfers, nonproliferation, human rights, Taiwan, and trade issues as well-orchestrated American efforts to interfere in China's internal affairs, constrain the PRC's growing economy and military modernization, and prevent China from assuming its place as a major world power.

Beijing is convinced that Washington has targeted China as the next victim of American policies promoting "peaceful evolution" to capitalism.

US-China security relations, therefore, should be assessed in the context of Chinese threat perceptions and the vicissitudes of Sino-American relations on two fronts: military-to-military relations and nonproliferation. Washington's suspension of arms sales and military contacts following the Tiananmen Square crackdown effectively froze Sino-American defense ties for four years. Despite the freeze, the United States and China maintained bilateral dialogue—often fractious—over security issues relating to nonproliferation: China's adherence to MTCR guidelines, the 1992 sale of F-16s to Taiwan, allegations of shipments of chemical warfare components aboard the *Yinhe*, and the imposition of US sanctions on high-technology sales because of China's transfer of M-11 missiles to Pakistan.

Both military-to-military ties and productive dialogue over nonproliferation issues got back on track as Sino-American tensions eased following the delinking of Most Favored Nation trade status and human rights in June 1993. High-level military contacts were resumed after the Clinton Administration inaugurated its policy of constructive engagement with China and dispatched Assistant Secretary of Defense Charles Freeman to visit Beijing in December 1993. The engagement policy entailed the resumption of military dialogue through periodic visits of high-ranking officials, ship visits, participation in professional fora, and functional exchanges. In fall 1994, China agreed once again to abide by MTCR guidelines after the United States lifted its ban on high-technology exports. China also accepted the American argument that the M-11 missile had the "inherent capability" standard of missiles banned by the MTCR. Secretary of Defense William J. Perry visited China in October 1994 to discuss global and regional arms control and proliferation issues and the need for greater Chinese transparency on the defense budget and strategic planning, and signed an agreement establishing the US-China Joint Defense Conversion Commission (*see* p.16).

...and on US security priorities

Though Beijing has begun to cooperate in some areas of nonproliferation, China's full accession and commitment to the various arms control regimes are tempered by a fear that full acceptance of the regimes will leave the PRC vulnerable militarily. Beijing's concern that Washington opposes China's growing regional influence resurfaced in February 1995, when the US Department of Defense issued a strategy paper on the East Asia-Pacific region. The strategy review announced the US decision to maintain—rather than further reduce—its troop strength in the region at 100,000; to strengthen bilateral alliances and friendships; and to "engage" China, Russia, and Vietnam. Chinese analysts criticized the United States for strengthening its military position in the region and stated that this "buildup" was directed against China. Some cited the strategy review as evidence that the United States was trying to contain the PRC, because, they alleged, Washington viewed Beijing's increasing strength as a threat. Chinese criticism of the report also suggests frustration that key American alliances with Japan and South Korea are not being revised quickly enough to suit Beijing's post-Cold War regional ambitions.

Similarly, US differences with China over adherence to its arms control commitments leave Beijing convinced that Washington is using nonproliferation issues to rein in PRC power. Beijing views current arms control regimes as dominated by the United States and rationalizes the PRC's ambivalent stance on nonproliferation issues in this context. China is a signatory to the NPT, adheres to the 1987 MTCR guidelines, and supports the nonproliferation goals of these regimes. But Beijing considers the MTCR an American-led suppliers' club lacking the international legal status of a multilateral treaty. This mindset leads the regime to view MTCR and other nonproliferation commitments primarily as bilateral, rather than global, arms control issues. This view has led Beijing to skirt the edges of the MTCR and NPT and to use missile and nuclear technology transfers as a tool to punish Washington when Sino-American relations deteriorate.

China's policies on other arms control issues also reflect its ambivalence about restricting its nuclear weapons capabilities when the United States and Russia retain much larger nuclear arsenals. Though a participant in the negotiations for a comprehensive test ban treaty, the PRC has continued to develop a second generation of nuclear warheads and missiles and refused to join the nuclear test moratorium observed by the United States, Russia, and the United Kingdom.

In 1995, China undertook two nuclear tests. The first was conducted on May 15, four days after Beijing voted for indefinite extension of the NPT, demonstrating Beijing's determination to upgrade its nuclear arsenal despite its own support for nonproliferation. In July and August, missile tests designed to intimidate Taiwan were conducted in the East China Sea near Taiwan. The nuclear explosions and missile launches were intended to signal that strategic nuclear arms control has yet to reach the stage at which China will accept limitations on its own arsenal, to show that the PRC's nuclear and missile prowess make China a force to be reckoned with in Asia, and to deter potential antagonists around the PRC's periphery and moves toward Taiwan independence.

Close tabs on Asian neighbors

In addition to warding off what it perceives as US policies of containment, Chinese actions reflect Beijing's perceptions of security matters closer to home. Beijing remains confident of its ability to maintain good or improving bilateral relations with South and Central Asian governments, but regards PRC security interests as challenged by India-Pakistan tensions and the possible expansion of Islamic fundamentalism. The crux of China's approach to Central Asia is to use economic integration—building close economic ties—to promote cross-border development to limit the appeal of Islamic fundamentalism, contribute to political stability, and advance Chinese influence.

At times, however, PRC policies toward South Asia appear contradictory: promoting regional stability and nonproliferation often conflicts with other PRC security objectives. China has rather successfully improved ties with India and reduced dramatically the Indian threat to China's security while maintaining a close strategic relationship with Pakistan and urging both countries to reduce mutual tensions. Beijing recognizes that if India or Pakistan declares an overt nuclear capability or deploys ballistic missiles, a destabilizing arms race would ensue, undermining Chinese security. But the leadership's worries about Islamic fundamentalism and desire to limit Russian, American, and Indian influence in South and Central Asia have prompted the regime to sell missile and nuclear technology to both Iran and Pakistan. Beijing claims that its nuclear assistance comes under international safeguards and flatly denies the provision of missile technology to either country.

Uncertain future

For now, tensions between the United States and China appear to be easing. High-level military contacts, which broke off during the summer as Beijing protested Lee Teng-hui's visit to the United States, resumed in September. Maintaining continuity in defense contacts and security dialogue over arms control issues will not erase all the differences between Washington and Beijing, but will help allay some of China's concerns about America's security objectives.

But additional instabilities remain, including the worry that conflicting territorial claims in the Spratly Islands and other maritime areas will erupt into regional conflicts. Beijing regards the Nansha (Spratly) and Xisha (Paracel) islands as indisputable parts of Chinese territory, but Brunei, Malaysia, the Philippines, Taiwan, and Vietnam have also laid claims to various parts of these islands. Recent statements by Chinese officials suggest that Beijing has temporarily backed away from its assertive stance to its claims and showed more flexibility in its willingness to negotiate a diplomatic solution to the conflicting claims. China's intentions toward the South China Sea nevertheless remain ambiguous because Beijing has neither altered its claims nor abjured the use of force to protect those claims. Although the PRC has re-emphasized a diplomatic solution to placate its neighbors, the continued military buildup serves as a reminder of China's coercive power.

This ambiguity, which pervades much of Chinese security policy as Beijing grapples with the security paradoxes it faces, stems largely from inconsistent security objectives. Contradictory policies—especially regarding Sino-US relations, arms control, and the South China Sea, are the hallmark of domestically driven policymaking that will continue as long as the post-Deng Xiaoping succession remains unsettled.

In formulating a strategy toward its new security environment, Beijing has often interpreted US policies that differ from China's as American attempts to constrain Chinese power and influence. Beijing's penchant for derailing security dialogue when bilateral relations deteriorate undermines its ability to see Washington's security objectives as non-threatening.

Sino-American relations will remain poor unless China starts realistically perceiving the United States as an integral part of the security landscape globally and in Asia rather than as a declining power trying to obstruct China's march to

Modernizing on a Shoestring

Despite recent press reports to the contrary, China is not in the midst of a massive military buildup. Although Beijing announced plans as early as 1985 to modernize the People's Liberation Army (PLA) force structure and upgrade its weaponry to fight limited regional conflicts, the PLA has not received priority in resource allocations from the central government. From 1986-94, the defense budget grew 159 percent in nominal terms, but only 4 percent in real terms. This modest increase came even as military expenditures increased at double-digit rates beginning in 1989. Furthermore, defense spending declined as a percentage of gross domestic product, from 1.9 percent in 1989 to 1.5 percent in 1994. (Official figures are suspected to understate the actual spending by at least 50 percent because some military expenses always have been included in parts of the civilian budget. Western assessments of Chinese defense expenditures vary, but insufficient information exists to prove that massive increases in spending are concealed elsewhere in the government budget or from other sources.)

Because of limited government allocations, the PLA has had to rely on supplementary income from PLA commercial activities and arms exports to cover costs (*see* p.14). Nonetheless, the PLA has not neglected weapons modernization. China continues to combine indigenous production efforts with selective imports of weapons systems and technologies from Russia, Israel, and other countries to upgrade its weaponry.

In the 1990s, Chinese military modernization efforts have focused on enhancing PLA air force and naval capabilities to conduct longer-range military operations and on upgrading the country's nuclear deterrence ability. China's modernization attempts encompass all of its armed service sectors:

■ **PLA Navy** Although China has established itself as a regional naval power with limited power projection capabilities, since the late 1980s the navy has added indigenously built destroyers, frigates, supply ships, landing ships, and missile patrol craft and acquired a small number of conventionally powered, conventionally armed Russian Kilo-class attack submarines. Blue-water capabilities remain restricted by the comparatively small number of modern combatants and deficiencies in anti-air defense, anti-submarine warfare, electronic warfare, and ship replenishment. Beijing has ambitions to build a world-class navy capable of providing a forward defense of its territorial waters. However, these ambitions, including the navy's interest in an aircraft carrier, are believed to be years away from fruition because of the financial, technical, and operational problems of naval modernization.

■ **PLA Air Force** The air force has obtained a squadron of Su-27 fighters, RD-33 aircraft engines for its F-7 fighters, 10 Il-76 transports, and 4 batteries of the SA-10 surface-to-air missile defense system from Russia. These acquisitions symbolize the air force's determination to assimilate advanced technology and improve airlift and air defense capabilities. The small number of available aircraft and deficiencies in command and control, early warning systems, and air defense, however, continue to hamper air force capabilities. Technological and financial obstacles will impede progress in modernizing air force training and education, developing strategy and tactics, and improving joint operations with the ground forces and the navy. The air force will remain the weak element in defensive or power projection capabilities well into the next century.

■ **PLA Ground Force** Beijing stopped giving budget priority to the PLA ground force when the Soviet military threat disappeared during the late 1980s. Instead, the PLA decided to modernize about a quarter of the ground force by creating rapid reaction or "fist" units, which have modern equipment and extra funds for training. Rapid reaction units have participated in the PLA's combined-arms and joint-service exercises, particularly those designed for potential regional conflict scenarios.

China has yet to reach its goal of making the entire PLA capable of conducting modern combined arms operations in limited regional conflicts. As military modernization has come only to selected units, PLA efforts to reshape force structure, revise military doctrine, and upgrade weaponry will continue for a long time. Despite Beijing's ambitions to become a global power, limited finances and ability to absorb advanced technology will likely constrain the growth of Chinese military power to a measured pace.

—Roxane D. V. Sismanidis

global power status. A more pragmatic Chinese approach would permit legitimate differences to be addressed through dialogue, instead of the current nonproductive policy of posturing and lecturing without listening. The PRC also has misread the subtleties of post-Soviet security relations in Asia by envisioning a rapid US disengagement from the region, then reacting with pique when that disengagement did not occur.

China's role in regional and global security, however, depends only partly on coming to terms with the continuing importance of the United States. To be a global power in arms control, China must demonstrate that its global nonproliferation commitments are more important than its bilateral interests in selling missile and nuclear technology to Pakistan and Iran. Beijing has already undercut its efforts to become a world player on arms control and disarmament issues by addressing MTCR/NPT problems as bilateral Sino-American, Sino-Pakistani, or Sino-Iranian issues rather than as global issues. However, there is little indication that

China's intentions in the South China Sea worry US and ASEAN officials.

Beijing will soon resolve its inconsistencies on arms control and proliferation issues, particularly with regard to South and Central Asia.

Finally, before China can take on its new role in the post-Cold War security environment, Beijing must devise a satisfactory approach to concerns about its growing economic, political, and military power. The PRC has muddied this question by turning the "China threat" issue into an either-or proposition. Beijing is disingenuous in denying that China's military buildup has raised concerns in Asia. Asian leaders are well aware that China's military modernization is the result of the rising level of economic development. The issue for Asian—and American—security planners is not the pace of Chinese military modernization so much as the context in which this modernization occurs. The ambiguity of Chinese actions and intentions regarding the South China Sea, the People's Liberation Army's focus on modernizing the force structure to meet potential threats on China's periphery, and missile tests near Taiwan prompted worries that the PRC will resort to force if it cannot obtain its objectives diplomatically.

ASEAN and American officials have made clear that while they do not view China as a threat, China itself needs to address these concerns. In the words of Singapore Prime Minister Goh Chok Tong, "It's not preordained that China's military power will turn into a threat. China must show through its attitude and action that, big as it will be, it intends to be a responsible member of the international community." Without a move in this direction, Beijing will diminish its international influence and likely will confront a security environment much more threatening than the one it currently enjoys. 完

From Machine Guns to Motorcycles

■ Maria Christina Valdecañas

Getting rich is glorious, especially for China's armed forces

■ **A former *CBR* assistant editor, Maria Christina Valdecañas is an analyst with the Economic Research Service of the Department of Agriculture.** **The author would like to thank Paul Godwin of the National War College and H. Lyman Miller, director of China studies at the Johns Hopkins University School of Advanced International Studies, for their assistance with this article.**

What were once small enterprises devoted solely to the maintenance and support of the People's Liberation Army (PLA) have quickly become a financial mainstay of China's armed forces. Though many PLA enterprises remain small operations intended only to support individual units, others have blossomed into multi-million-dollar endeavors, including such well-known Chinese companies as Polytechnologies, 999 Enterprise Group, China United Airlines, and Xinshidai Development Corp. These commercial activities fall under direct control of central, regional, or local units of the PLA and are involved in everything from pharmaceutical production to real estate development.

While the true extent of military commercialization in the PRC—including PLA non-military enterprises as well as defense industry operations—is difficult to discern, estimates suggest that China's commercial-military complex has some 50,000 companies employing as many as two million people. In 1993, these companies are thought to have earned more than $5 billion. Taken as a whole, the combined earnings of these activities would place China's commercial-military operations among the ranks of the top 100 corporations of the Fortune 500.

The depth of the military's commercial activities in the fast-paced China market is rivaled only by the breadth of activities these entities have chosen to undertake. PLA enterprises are now venturing into the entertainment business, while other enterprises within China's defense industry have shifted some or all of their production to make consumer goods ranging from bicycles to cleaning supplies (*see* box). These factories and companies are now jumping into the sea of free enterprise, taking their cues from the market rather than from central planners.

A servant of the people

Non-military activities are not a new phenomenon in China's armed forces. The PLA has a long history of self-sufficiency, beginning in the 1920s. Army enterprises were developed to take care of such needs as food, clothing, and shoes. When the Communist Party took control of the country in 1949, the PLA retained its farms and factories. By taking care of its daily necessities, the PLA proved it could emulate the communist ideal of self-sufficiency and be a true servant of the people.

Historically, PLA enterprises generally fell under the control of the PLA itself. Beijing granted these enterprises special tax benefits and allowed them to use the PLA's transportation infrastructure. With the beginning of the country's economic reforms in the late 1970s, control of some military enterprises devolved to collectives operated by PLA servicemen or PLA family members. These enterprises were not allowed to use defense budget funds or receive tax benefits, but could still use the PLA's transportation infrastructure and therefore minimize distribution-related obstacles. The number of enterprises directly under PLA jurisdiction continued to grow as units learned they could sell their wares to local consumers.

When Beijing began to demobilize troops and trim military expenditures in the mid-1980s, PLA enterprises were given greater control over their operations and were forced to take responsibility for their profits and losses. PLA enterprises then branched out into other areas to cover costs and provide employment for demobilized troops. Though the overall defense budget continued to increase, defense sector allocations as a percentage of the total State budget have declined relative to allocations to other sectors.

Scrutiny from the center

Although its authority over PLA-related commercial activities throughout the country is often tenuous, the central government has tried to impress upon PLA enterprises the need to choose activities that will serve the people. Some within the highest leadership worry that the concentration of PLA commercial enterprises on non-military endeavors is undermining the discipline of China's forces. In part to undo some of the damage done to the PLA's image after the 1989 Tiananmen crackdown, the Central Military Commission issued what came to be known as the "10 No's" later that year. The regulations, an attempt to elevate the PLA beyond reproach, prohibited any PLA enterprise from using military resources to take part in speculation, profiteering, or smuggling.

Some within the highest leadership worry that the concentration of PLA commercial enterprises on non-military endeavors is undermining the discipline of China's forces.

Because of ongoing allegations that PLA enterprises abuse military power and connections for commercial ends, Beijing has continued to monitor military-related commercial activities. The most recent crackdown, which began in the fall of 1993, required all PLA units to obtain permission from the regional military command or military authorities in Beijing to establish enterprises and sought to consolidate many of the smaller enterprises under some sort of regional or central-level control. The impetus behind these actions was a fear among the leadership that excessive concentration on commercial operations and growing competition for PLA resources would increase intra-unit rivalries. Beijing also hoped that in consolidating PLA operations, it could curb corruption.

However, in taking steps to control the PLA's burgeoning commercial sector, the leadership did not want to ban commercial activities altogether, fearing a backlash from officers turned entrepre-

Entering the Fray

In many of the defense industry factories that once produced the weapons and materiel to support China's three-million-man military, workers are churning out not tools of war but hundreds of types of consumer goods. Alongside the People's Liberation Army enterprises, many of the defense industries under the jurisdiction of the Ministry of Machine-Building Industry and the Ministry of Electronics Industry have also ventured into the budding market economy.

China's defense industries—unlike their counterparts elsewhere, such as America's General Dynamics Corp. or Lockheed Martin Corp., which have long maintained some civilian-oriented activities—only began to move away from weapons and ordnance production in the early 1980s. In some instances, Beijing encouraged the transition, setting some defense industries on their own in the hopes that market incentives from the civilian sector and the need to make up for their own losses would stimulate greater efficiency.

China Great Wall Industry Corp., China Petroleum Corp., China North Industries Corp., and many other defense industries have begun to gear their production toward non-military operations. Some formed joint operations with foreign firms to produce consumer goods. Other defense industries turned to foreign buyers for their wares (*see The CBR*, March-April 1994, p.47).

Following the dramatic demonstrations of high-technology weapons in the Gulf War, however, Chinese-made weapons have had waning appeal on international markets, and many Chinese defense industries have had to find other revenue-producing activities. Defense industry operations currently range from traditional dual-use industries such as high-technology and transportation ventures to factories making household appliances and companies offering real estate and financial services. In 1994, 30 percent of color televisions, 50 percent of refrigerators, 65 percent of motorcycles, and 75 percent of taxicabs made in China were produced by defense industry enterprises. The establishment of bilateral commissions, such as the US-China Joint Defense Conversion Commission, will likely result in an even greater shift toward civilian production in the years to come (*see* p.16).

—*MCV*

neurs. Beijing recognized that many PLA units have deeply vested interests in their enterprises and knew that closing down all non-military operations was not an option. The leadership worried that shutting down enterprises would result in a shortage of funds to support individual unit operations—and add to the ranks of the unemployed.

To make up for the re-orientation of some of the enterprises as a result of the new regulations, Beijing ordered an increase in PLA wages and lowered the retirement age. Nevertheless, few enterprises appear to be taking the regulations to heart. The number of new PLA enterprises continues to grow as existing enterprises find ways to skirt the regulations—either by under-reporting profits or establishing subsidiary enterprises without appropriate approval.

In 1994, PLA enterprises were engaged in foreign trading, marketing agricultural commodities, and managing hotels.

PLA, Inc.

Whatever the true extent of PLA activities, production from the recognized PLA commercial enterprises is said to have made up more than 90 percent of the PLA's annual output during the last

Trading Butter, Not Guns

The US-China Joint Defense Conversion Commission (JDCC), a bilateral initiative formally approved in January 1994, fits easily into the post-Cold War paradigm in which economics is the driving force in international relations. JDCC aims to promote private sector participation in the conversion to peaceful purposes of defense-related industrial, technological, and scientific facilities, as well as personnel no longer needed for national defense purposes. JDCC was conceived in 1993 by then-Deputy Defense Secretary William Perry and Chinese Vice Minister of the Commission on Science, Technology, and Industry for National Defense (COSTIND) Huai Guomo.

The commission entails no military cooperation or military technology transfer between the two governments, nor does it allocate US government funds for entities engaged in the conversion efforts. The agreement is between the two governments—JDCC is an interagency commission with representatives from several government agencies, including the commerce and state departments, Office of the Secretary of Defense, Arms Control and Disarmament Agency, the Joint Chiefs of Staff; and the PRC's COSTIND, State Planning Commission, State Economic and Trade Commission, and various ministries. The motivation on the US side included a desire to build better channels of communication with China's defense establishment and offer potential benefits to US businesses hoping to participate in China's defense conversion.

At the first JDCC meeting in October 1994 in Beijing, co-chaired by Defense Secretary Perry and COSTIND Minister Ding Heng Gao, both sides agreed to:

- Cooperate to help China unify its air traffic management (*see The CBR*, July-August 1995, p.12);
- Cooperate in the design and production of electric- and gas-powered vehicles at defense research institutes and factories;
- Publish specific PRC defense conversion projects open to bidding by American companies; and
- Exchange personnel engaged in defense conversion work in their respective countries.

JDCC includes no specific measures to promote US investment in China's defense industries; rather, the commission helps facilitate cooperation between US businesses and Chinese defense plants. While the Chinese aim to market abroad the goods produced in converted facilities, the United States entered the agreement hoping to boost prospects for additional Chinese markets for US goods. Pre-existing guidelines and export licenses for technology transfer between the countries still apply to projects initiated under JDCC auspices.

Fruits of cooperation

Though the commission is still in its infancy, it can claim some early successes. In May 1995, the Commerce Department published *China Defense Industry Directory*, which lists 49 projects in such areas as environmental protection, biotechnology, mechanical instrumentation, isotope and materials applications, communications, transportation, and engineering. Since publication of the directory, the Commerce Department has encouraged US companies to make proposals directly to the relevant Chinese officials.

Westinghouse Electric Corp. recently signed the first reported JDCC contract with the China Yuanwang (Group) Corp., a company under COSTIND. The agreement calls for the design, development, and demonstration of two battery-powered city buses, to be built at Yuanwang's Beijing facility and completed in time for demonstration at the National People's Congress in April 1996. The market for this type of bus is estimated to be 4,000 per year.

A long-term goal of the commission is reform of China's air traffic control system, which will allow increased air traffic in China, improve sales prospects for US aviation companies, and provide a safer airspace for all planes flying in the PRC. The US Federal Aviation Administration (FAA), working with the Defense Department, has set up an eight-step plan that will bring together Chinese military and civilian air traffic control officials to formulate an agenda for the integration of the country's civilian and military air traffic control structures. Integrating the two five years, with proceeds from PLA commercial activities making up as much as 20 percent of the PLA's official budget.

In 1994, PLA enterprises were engaged in foreign trading, marketing agricultural commodities, and managing such hotels as the Palace Hotel and Poly Plaza in Beijing. Some PLA units have also expanded operations into the service and entertainment industries. Press reports are often rife with stories highlighting PLA forays into the night club and karaoke business. Many of the military enterprises have invited foreign investment to complement their efforts—PLA enterprises were involved in more than 200 foreign-invested joint ventures in 1994.

Xinxing Corp. is involved in more than 50 foreign joint-venture projects.

Not all PLA enterprises are money-making ventures, but many are, and a few stand out as China's top earners. For example, China Poly Corp., founded in 1984 by the PLA General Staff Department, boasts more than 100 subsidiaries that earn in excess of $500 million a year in foreign trade revenues. Xinxing Corp., which is operated by the PLA General Logistics Department, has some 100 factories employing over 300,000 people, and is involved in more than 50 foreign joint-venture projects. Polytechnologies, 999

air traffic management structures has proven difficult due to the reluctance of PRC military officials to discuss any transfer of control with their civilian counterparts. COSTIND at times has seemed more interested in the short-term plans for its defense production facilities.

With considerable encouragement from the US Defense Department, however, COSTIND has recently exhibited a more positive attitude on air traffic control reform. The second JDCC meeting, to take place in Washington possibly in 1996, will provide a good opportunity to assess whether China is making a sincere effort to use the JDCC framework to revamp its air traffic management radically. In meetings thus far, Chinese officials continue to declare that they intend to adopt an air traffic control system modeled on the US system, which would mean substantial opportunities for collaboration with US air traffic radar manufacturers.

With the exception of a meeting between Perry and Huai in March, no technical personnel exchanges as outlined in the agreement have yet taken place. Other than the Yuanwang bus deal, few vehicle production cooperation projects have been discussed, even though this area was included as a result of a Chinese proposal.

Political fallout

In the year since the first JDCC meeting, diplomatic relations between the United States and China have changed significantly. Many in Congress have misinterpreted the commission's objectives and believe that the United States should steer clear of any projects involving China's defense industry. In late 1995, the Clinton Administration continues to face a Congress that is highly critical of China and a Beijing leadership that suspects the United States of trying to "contain" China.

The poor bilateral relationship has affected defense conversion cooperation in several ways. COSTIND postponed a visit to the United States scheduled for July, slowing general progress. The delegation has since been invited to visit the United States in December. The House National Security Committee, after heavy lobbying by those who criticize JDCC as providing undue financial and technological benefits to the Chinese defense industry, sought this summer to ban all telephone calls, travel, and man-hours relating to the commission's work. This sequence of events indicates the depth of misunderstanding of defense conversion cooperation with China and the hostility that some congressional members harbor toward the PRC defense establishment. While a new round of legislative actions on defense conversion cooperation with China cannot be ruled out, at least for the short term the commission's work is proceeding.

Standing firm on peace initiatives

China's defense conversion is arguably the most successful of any in the world—70 percent of goods produced by PRC defense plants are now civilian products. It is puzzling that negative feelings exist in Washington toward a cooperation agreement that encourages an emerging superpower such as China to convert defense production facilities to civilian-oriented ends. It is unlikely that China will convert its front-line defense facilities—production of advanced weapons will certainly continue in China. But helping to shrink the large State-sponsored defense production sector and allowing American companies to benefit from a comparative advantage in this sector clearly seems to be in the US interest. The troublesome diplomatic climate has perhaps skewed policymakers' views of China. With gradual improvement in Sino-American bilateral relations, however, JDCC will hopefully be allowed to achieve its worthy potential.

—Eden Y. Woon

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Enterprise Group, China United Airlines, and Xinshidai Development Corp. are likewise among the most successful, bringing in millions of dollars in profits each year.

Giving some, taking more

Since the beginning of China's economic reforms, Beijing has required all PLA commercial enterprises to remit a portion of any profits to their commanding units. The funds are to be used for improving the standard of living for the rank and file and, in some cases, modernizing the unit's weaponry. Recent estimates suggest that these profits are rarely spent on weapon improvements; rather, most of the remitted income goes toward troop upkeep.

On average, PLA enterprises retain roughly five percent of their profits, but for larger, wealthier enterprises, the take can be much higher. For many of the more lucrative enterprises, some of the retained earnings fund high-level management perks, including luxury cars and homes, while the remainder is reinvested into the initial enterprise or subsidiary organizations.

In the hope of retaining more of their profits, some PLA enterprises have been known to understate their true earnings. Beijing has tried to cut down on such abuse by requiring all military enterprises to undergo financial audits. Thus far, however, the results of the audits have been disappointing.

Image is everything

The dilemma of choosing between the competing interests of additional revenue to make up for minimal central-government allocations versus maintaining the original spirit and ideals of China's military force has garnered much attention in the Chinese press. Most analysts suggest Beijing is afraid that without proper oversight, rampant commercialization of the military will undermine its troop readiness. As accusations of corruption and unfair advantages for PLA entrepreneurs proliferate, Beijing will have to weigh the benefits of continuing to cultivate a military capable of taking care of itself against the need to maintain the broader goals and image of the PLA—and the country's defenses. On the one hand, Beijing welcomes the added income generated by PLA enterprises; on the other hand, it cannot ignore the problems caused by the growing coffers of some PLA units. Tensions between China's military professionals and the emerging PLA entrepreneurs will likely cause rifts within the PLA. Moreover, the increasingly noticeable perks of military connections will likely spark new resentment within the civilian population.

As the country enters a more complicated stage of economic reform, some within the leadership have suggested that Beijing should nurture the PLA's commercial activities since the vested interests of PLA entrepreneurs in the transformation of the economy will likely foster support for future reforms. Others warn that military entrepreneurs instead may resist further liberalization, as the movement to a market economy will erode some of the benefits they currently enjoy. PLA entrepreneurs could decide that the status quo—complete with perks and connections—is preferable to a more open economy. If Beijing allows the PLA to get wealthy while the majority of the population remains stuck in a half-market, half-command economy, higher levels of civil-military tensions will likely result.

Yet, in making its decision, Beijing cannot ignore that what began as a survival industry has now blossomed into a major component of the Chinese economy. Whatever next step the leadership decides to take to resolve these competing interests, the intensity of current PLA commercial activities suggests that this sector will continue to be strong.

Although its supplementary income has helped the PLA to keep up with inflation, the growing preoccupation with non-military endeavors no doubt interferes with military professionalism and adds to corruption within the armed forces. PLA commercial undertakings have already led to what some see as a deterioration of discipline and morale among the rank and file. The long-term effect of the dichotomy between military professionalism and entrepreneurial spirit is likely to force Beijing to reconsider the PLA's role in the socialist market economy and take steps to prevent the armed forces from becoming too focused on getting rich. 完

The Fuss over Taiwan

■ Chas. W. Freeman, Jr.

Getting US-China relations back on track is important for business

■ **Ambassador Chas. W. Freeman, Jr. is currently a Distinguished Fellow at the United States Institute of Peace. As a foreign service officer, he participated in both the opening and consolidation of US relations with the PRC. His November 1993 visit to China as assistant secretary of defense helped reopen Sino-American military dialogue.**

The Taiwan question, which most Americans thought—or hoped—was behind us, is back as a major problem in US-China relations. So is military tension in the Taiwan Strait, at a level not seen since US-China normalization set the stage for trade, investment, and peaceful contacts between Taipei and Beijing. The immediate cause of these unwelcome developments was the private, but very political, visit of Taiwan's leader, Lee Teng-hui, to the United States in June. Lee's visit brought Beijing's mounting concerns about the direction of US China policy to a head.

The Chinese leadership now believes that the US government is straying from the basic understandings that made it possible for Beijing and Washington to build a normal relationship. They are convinced that the United States is in complicity with Taiwan's efforts to stake out an identity for itself separate from China.

A damaged framework

The return of tension in the Taiwan Strait and new strains in the US-China relationship carry obvious dangers. Both Lee Teng-hui, whose efforts to achieve a higher international profile for Taiwan provoked the crisis, and the Clinton Administration and US Congress, whose desire to accommodate Taipei made it happen, seriously misjudged the strength of nationalist reaction in Beijing to alterations in longstanding US policy toward Taiwan. Neither Taipei nor Washington sought or foresaw confrontation with Beijing. Nor did Beijing desire confrontation with Taipei or Washington. But Beijing is reacting to what it sees as a challenge to the status quo in the Taiwan Strait. PRC leaders see themselves as attempting to restore that status quo—and the framework that made it possible. It remains an open question, however, whether that framework and the benefits it generated can be put back into place.

The basic framework for Sino-American relations and peace in the Taiwan Strait took over a decade of delicate diplomacy to construct. The three agreements that built this framework have worked so well that few Americans, including officials in the Clinton Administration, bother to read them or remember their negotiating history (*see* boxes).

The Cold War context in which these agreements were reached, like China's favorable, pre-Tiananmen image in the United States, has disappeared. Now China fears the agreements themselves and the *modus vivendi* on the Taiwan issue they created may likewise vanish.

Back to basics

The 1972 Shanghai Communiqué ended over two decades of US containment policies and began a mutually beneficial strategic dialogue between Washington and Beijing. It marked the end of American backing for Taipei against Beijing in the unresolved Chinese civil war. In this communiqué, the United States made it clear that Americans stood for "a peaceful resolution of the Taiwan problem by the Chinese themselves."

In 1979, the United States shifted recognition from Taipei to Beijing as "the sole legal government of China." A key element in the normalization agreement was Washington's acknowledgment of China's position that "there is but one China and Taiwan is part of China." The communiqué committed Americans to maintain "economic, cultural, and other unofficial relations" with Taiwan "within this context." This tradeoff of form for substance allowed Americans to retain de facto ties with Taiwan while exchanging ambassadors with Beijing. Washington also continued sales of carefully selected defensive weapons to Taiwan to sustain the island's ability to defend itself. This policy, authorized by the Taiwan Relations Act (TRA) of 1979, was intended, in the words of the act, to assure that "the future of Taiwan [would] be determined by peaceful means." Beijing objected to both US arms sales and the TRA, but nevertheless proceeded with the normalization of its relations with the United States.

Sino-American differences over the level of US arms sales to Taiwan soon necessitated the conclusion of a third agreement. In the arms sales communiqué of 1982, Beijing accepted the continuation of US arms sales to Taiwan. The Reagan Administration agreed to cap the quality and reduce the quantity of US arms sales to Taiwan, with a view to eventually ending them. Beijing and Washington pledged to "adopt measures and create conditions conducive to the thorough settlement of this issue."

> Lee Teng-hui's visit, from China's perspective, added an unacceptable political element to US relations with Taiwan.

The view from Beijing

Beijing saw President Bush's sale of 150 advanced F-16 aircraft to Taiwan prior to the 1992 presidential elections—the largest arms sale in American history—as a blatant violation of the Sino-American understandings recorded in the 1982 communiqué. Beijing viewed the Clinton Administration's 1994 decision to open cabinet-level dialogue with Taipei as contrary to the 1979 communiqué's stipulation that the United States would maintain only "unofficial" relations with Taiwan. Lee Teng-hui's visit, from China's perspective, added an unacceptable political element to US relations with Taiwan.

Beijing does not now hide its concern that Washington may be returning to the hostile policies the United States abandoned 23 years ago in the Shanghai Communiqué. Many Chinese see the tough US stance on PRC membership in the World Trade Organization, along with US restrictions on technology transfer, as part of an effort to retard their country's modernization and block its rise to wealth and power. Chinese leaders view the continuing American focus on human rights as an effort to stir up opposition and to divide and weaken China politically. Virtually all Chinese are offended by congressional efforts to promote independence for Tibet. Many Chinese see this, like congressional initiatives toward Taiwan, as evidence that the United States hopes that China will collapse and break apart like the former Soviet Union. The Clinton Administration has yet to rebut convincingly these Chinese suspicions, which strike most Americans as far fetched.

Enter Lee Teng-hui

Lee Teng-hui's trip to the United States took place in this unpropitious context. Lee himself portrayed his visit as a major step toward unilateral determination of Taiwan's identity without regard to Beijing's views. On his return to Taipei, he offered the United Nations $1 billion for a seat in the body. Rightly or wrongly, Beijing has concluded that Lee's actions are aimed at breaking the delicate understandings that had made confrontation unnecessary in the Taiwan Strait, and at achieving Taiwan independence. Beijing now demands that Taipei, as well as Washington, show that it still sees Taiwan's de facto separation from the rest of China as a tem-

Excerpts from the Shanghai Communiqué of 28 February 1972

....The Chinese side reaffirmed its position: The Taiwan question is the crucial question obstructing the normalization of relations between China and the United States; the government of the People's Republic of China is the sole legal government of China; Taiwan is a province of China which has long been returned to the motherland; the liberation of Taiwan is China's internal affair in which no other country has the right to interfere; and all US forces and military installations must be withdrawn from Taiwan. The Chinese government firmly opposes any activities which aim at the creation of "one China, one Taiwan," "one China, two governments," "two Chinas," an "independent Taiwan," or advocate that "the status of Taiwan remains to be determined."

The US side declared:

The United States acknowledges that all Chinese on either side of the Taiwan Strait maintain there is but one China and that Taiwan is part of China. The United States government does not challenge that position. It reaffirms its interest in a peaceful settlement of the Taiwan question by the Chinese themselves.

porary and unnatural state of affairs—one that negotiators from both sides of the Taiwan Strait should seek to correct through agreement on a process of reunification, even if this takes decades to implement.

This summer, the People's Liberation Army began a series of unprecedentedly large military exercises near Taiwan. Chinese officials describe these exercises as routine, but clearly intend to send Taipei the message that Beijing will not tolerate Taiwan's secession from "one China," the concept of which both sides had long endorsed. China can live with Taiwan's de facto independence for as long as it takes the two sides to agree on the island's ultimate relationship with the rest of China. Chinese nationalism would, however, compel Beijing to take military action to block an effort by Taiwan at de jure secession. Such military action by Beijing, even if provoked by a declaration of independence from Taipei, would compel Washington to decide whether the policies set out in the TRA require US armed forces to come to Taiwan's defense.

Choosing the right track

Beijing has been taking steps to improve its dialogue with Tokyo and Southeast Asian capitals and to put its relationship with Washington on hold so as to focus its efforts on Taipei. The chill in official relations with Washington so far has not extended to business relationships with American companies. Beijing seems to have concluded that China's interests are best served by a strategy of strengthening people-to-people and commercial ties with Americans. The Chinese leadership hopes that, in time, broadened support in the United States might help produce less hostile American government policies.

> The upcoming elections are about Taiwan's domestic self-perception and the island's view of its international identity and status.

This approach, however, is not cast in stone. Business relations could be seriously affected by a further ratcheting up of the confrontation between Washington and Beijing. Congress may take further jabs at China over Tibet, human rights, arms control, or some other issue. An accidental outbreak of conflict in the Taiwan Strait could harm US-China business ties as much as provocative decisions by the Taiwan electorate. At their worst, such events could provoke a military confrontation in the Taiwan Strait from which the United States would find it difficult to remain aloof.

People power

Some of the business uncertainty involves events neither Beijing nor Washington can control. Taiwan faces two crucial elections over the coming months. On December 2, Taiwan's voters will elect a new Legislative Yuan, or parliament. In March 1996, they will—for the first time—directly elect a president. On one level, these elections are about who will represent the voters in the island's government. On another level, however, they are about Taiwan's domestic self-perception and the island's view of its international identity and status.

Some Taiwan politicians, including many Democratic Progressive Party (DPP) candidates for the Legislative Yuan and the presidency, espouse a Taiwanese nationalist cause at odds with the Chinese nationalist idea of "one China, but not now." They assert that Beijing lacks both the will and the power to forestall a move by Taiwan to formalize its de facto separation from China. Recent polls show that a third or more of Taiwan's voters interpret the

The Normalization Communiqué of 1 January 1979

The United States of America and the People's Republic of China have agreed to recognize each other and to establish diplomatic relations....

....The United States of America recognizes the government of the People's Republic of China as the sole legal government of China. Within this context, the people of the United States will maintain cultural, commercial, and other unofficial relations with the people of Taiwan....

....The government of the United States of America acknowledges the Chinese position that there is but one China and Taiwan is part of China....

The US government statement accompanying the Normalization Communiqué:

....The American people and the people of Taiwan will maintain commercial, cultural, and other relations without official government representation and without diplomatic relations.

The Administration will seek adjustments to our laws and regulations to permit the maintenance of commercial, cultural, and other nongovernmental relationships in the new circumstances....

The United States...continues to have an interest in the peaceful resolution of the Taiwan issue and expects that the Taiwan issue will be settled peacefully by the Chinese themselves.

Statement from PRC Chairman Hua Guofeng at a press conference following the issuance of the Normalization Communiqué:

Q: Can you say that after normalization China would object to a visit to Taiwan by an American official?

A:...the answer to your question is clearly stated in the joint communiqué which I quote: "....the people of the United States will maintain cultural, commercial, and other unofficial relations with the people of Taiwan."....There will be only unofficial relations.

The Taiwan Relations Act of 10 April 1979

....(a) The President having terminated governmental relations between the United States and the governing authorities on Taiwan recognized by the United States as the Republic of China prior to January 1, 1979, the Congress finds that the enactment of this Act is necessary—

(1) to help maintain peace, security, and stability in the Western Pacific; and

(2) to promote the foreign policy of the United States by authorizing the continuation of commercial, cultural, and other relations between the people of the United States and the people on Taiwan.

(b) It is the policy of the United States—

(1) to preserve and promote extensive, close, and friendly commercial, cultural, and other relations between the people of the United States and the people on Taiwan, as well as the people on the China mainland...

(2) to declare that peace and stability in the area are in the political, security, and economic interests of the United States, and are matters of international concern;

(3) to make clear that the United States decision to establish diplomatic relations with the People's Republic of China rests upon the expectation that the future of Taiwan will be determined by peaceful means;

(4) to consider any effort to determine the future of Taiwan by other than peaceful means, including by boycotts or embargoes, a threat to the peace and security of the Western Pacific area and of grave concern to the United States;

(5) to provide Taiwan with arms of a defensive character; and

(6) to maintain the capacity of the United States to resist any resort to force or other forms of coercion that would jeopardize the security, or the social or economic system, of the people on Taiwan.

TRA as committing the United States to go to war with the PRC to protect them, if Beijing sought to use force to prevent or reverse such a declaration of independence. Others, including some rivals of Lee Teng-hui's nomination by the ruling Kuomintang, favor a policy of negotiation and careful rapprochement with Chinese on the mainland. A third or more of Taiwan's voters believe the United States would not come to their aid if they sought to separate themselves from China.

Beijing's current military maneuvers and other actions are clearly intended to sway the electorate in Taiwan away from DPP candidates and toward candidates that seek dialogue with Beijing. Presumably, that is one reason that the mainland has continued to welcome investors and traders from Taiwan, despite the political pressure Beijing is putting on Taipei. No one can now say, however, how Taiwan citizens will vote in December and March. Still less can anyone be sure that Beijing's efforts to influence the elections will not backfire and result in a majority of Taiwan legislators who seek independence from the mainland.

> Businesspeople hope the Clinton Administration will go beyond the lip service it has given to the three communiqués and explain clearly how it plans to stand by them.

These types of uncertainties have already had a negative impact on Taiwan's investment climate, reflected in the plummeting prices on Taipei's stock exchange. Escalating tensions with Beijing have also damaged the confidence of Taiwan investors in the mainland. Most are now holding back, pending clarification of future cross-Strait relations. Similarly, American and other foreign companies that once looked to Taiwan as a launching platform and source of managerial and technical talent for activities on the mainland are looking elsewhere for the time being. Taiwan's ability to interact peacefully with the Chinese mainland could be in serious jeopardy, in the judgement of businesspeople. Consequently, Taiwan's plans to become a regional operations center for international business are now effectively on hold.

Meanwhile, most businesspeople in the United States, Hong Kong, Taiwan, and the China mainland are justly apprehensive about the mess their political leaders may produce. Businesspeople with a stake in good US-China and cross-Strait relations universally seem to hope that those concerned will take Henry Kissinger's advice. The former secretary of state has urged that Taipei stop testing the limits of Beijing's tolerance; Beijing stop threatening Taiwan; the US Congress stand down from further pro-Taiwan, pro-Tibet, or other anti-China gestures; Beijing resume dialogue with Washington; and the Clinton Administration go beyond the lip service it has given to the three communiqués and explain clearly how it plans to stand by them. At a minimum, such efforts from all sides are necessary to prevent a further deterioration in an already bad situation. 完

The Arms Sales Communiqué of 17 August 1982

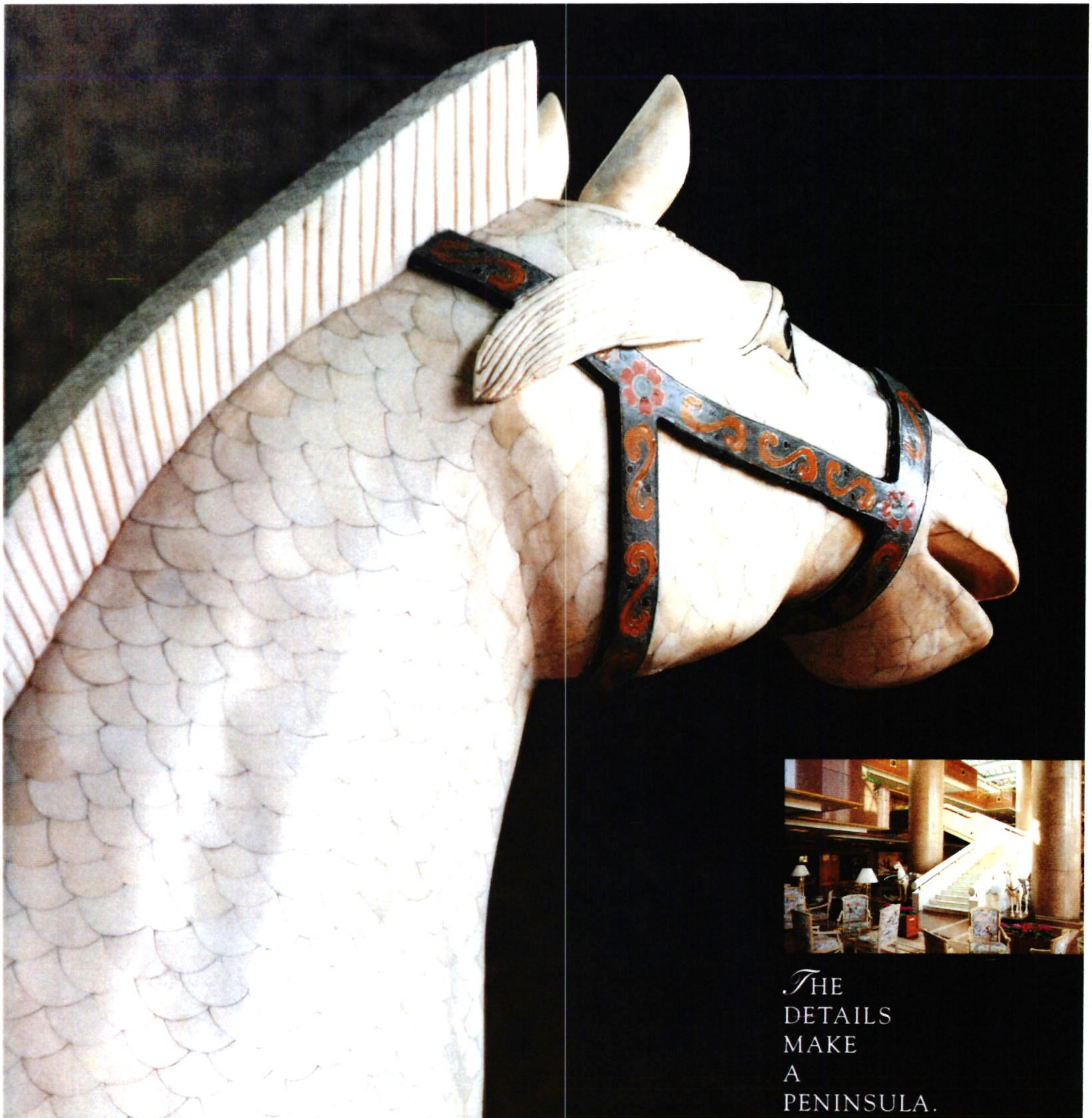
....on January 1, 1979...the United States recognized the People's Republic of China as the sole legal government of China, and it acknowledged the Chinese position that there is but one China and Taiwan is part of China. Within that context, the two sides agreed that the people of the United States would continue to maintain cultural, commercial, and other unofficial relations with the people of Taiwan. On this basis, relations between the United States and China were normalized....

....The Chinese government reiterates that the question of Taiwan is China's internal affair. The message to compatriots issued by China on January 1, 1979, promulgated a fundamental policy of striving for peaceful reunification...[and] a peaceful solution to the Taiwan question....

....The United States government attaches great importance to its relations with China, and reiterates that it has no intention of infringing on Chinese sovereignty and territorial integrity, or interfering in China's internal affairs, or pursuing a policy of "two Chinas" or "one China, one Taiwan." The United States government understands and appreciates the Chinese policy of striving for a peaceful resolution of the Taiwan question....

Having in mind the foregoing statements of both sides, the United States government states that it does not seek to carry out a long-term policy of arms sales to Taiwan, that its arms sales to Taiwan will not exceed, either in qualitative or quantitative terms, the level of those supplied in recent years...and that it intends gradually to reduce its sale of arms to Taiwan, leading, over a period of time, to a final resolution. In so stating, the United States acknowledges China's consistent position regarding a thorough settlement of this issue.

In order to bring about, over a period of time, a final settlement of the question of United States arms sales to Taiwan, which is an issue rooted in history, the two governments will make every effort to adopt measures and create conditions conducive to the thorough settlement of the issue.



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China Slips into Export Control Limbo

■ Erik C. Wemple and E. J. Prior

The international high-technology export control regime is changing, but China isn't part of the process

On September 17, the United States, a group of Western allies, and former Soviet bloc states—28 countries in all—reached a new trade control agreement that excludes China and, thereby, unofficially singles out the country as the world's premier export control pariah state. Dubbed the "New Forum," the agreement aims to link the world's foremost suppliers of conventional technology and arms in an alliance to restrict weapons transfers to rogue developing countries such as Iran, Iraq, Libya, and North Korea.

Though Clinton Administration officials have hailed the regime as an overdue adaptation of the forum's defunct predecessor, the Coordinating Committee on Multilateral Export Controls (COCOM), the New Forum is unlikely to alter existing patterns of high-technology trade to any measurable degree. China, for example, may never feel the effects of this new multilateral agreement because the New Forum lacks strict and well-defined rules on how its signatory countries are to control their exports. Moreover, the regime's failure to include China—an economic power and a potential military rival—from both the negotiations and the final agreement is a major drawback of the alliance and, in the short term, may well be its Achilles heel.

Washington claims that the New Forum will keep weapons, high-technology products, and dual-use items away from known proliferating states. Whereas the former COCOM regime sought to govern transfers from Western nations to the countries of the Soviet bloc, the New Forum seeks jurisdiction over transfers between industrialized and developing nations. Through a vaguely defined multilateral system of information sharing, consultation, and common policies of export restraint, the New Forum is designed to prevent its member states from selling conventional arms to proliferating countries in the developing world. According to Martha Harris, deputy assistant secretary of state for export controls, the agreement will require no amendments to existing US export control laws. Final details of the arrangement will be settled by the end of the year.

Whither China?

The founders of the New Forum initially intended to include China in the regime. The original blueprint for the COCOM successor regime—drafted in November 1993—cited Beijing as a critical partner in the multilateral mission to slow weapons proliferation. This decision was only logical: China boasts an extensive arsenal of conventional, nuclear, chemical, and biological weapons and has also been known to ship them to unsavory clients (*see The CBR*, March-April 1994, p.47).

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But during the actual negotiations for the establishment of the New Forum, neither Washington nor other New Forum principals approached China on joining the post-COCOM alliance. Instead, the allies focused on pulling in Russia, a country that, like China, has large stocks of weapons and advanced technology along with a questionable proliferation record.

The reasons for Russia's inclusion and China's exclusion are twofold. First, a lobbying force for China's participation never materialized among the New Forum partner countries, while a strong lobby emerged to include Russia. Second, the Clinton Administration was loathe to conclude an export control alliance with a country that it often viewed as ignoring US nonproliferation policies. Hence, in the final agreement, New Forum principals recoiled from listing China as either a partner in the new alliance or a target of its control efforts.

The decision leaves China as the only major trading power that is not a party to any of the four multilateral export control agreements.

The decision leaves China as the only major trading power that is not a party to any of the four multilateral export control agreements—the Missile Technology Control Regime (missile proliferation); the Australia Group (chemical and biological weapons proliferation); the Nuclear Suppliers Group (nuclear weapons proliferation); and the New Forum (conventional weapons proliferation). As an outsider, China technically is not obligated to abide by the guidelines contained in any of these international agreements, although participation in the New Forum would benefit China's standing in the international community by assuring other members that Beijing is willing to comply with global rules governing the transfer of conventional weapons.

Symbolism and high politics aside, however, the New Forum will not likely obstruct China's access to Western technology because it has no true enforcement power. For example, unlike COCOM, the New Forum has no list of controlled countries to which member nations are prohibited from selling arms. Rather, partner countries determine which countries should not receive arms and related technology on the basis of a hazy New Forum consensus. Members are required to maintain national export controls that guarantee the ability to

Computing Change

Although the New Forum fails to set out any clear guidelines listing which products can be exported freely by member countries, the Clinton Administration is relaxing many existing controls on US high-tech exports to China. The rationale for these changes is mainly technological: computer products which were once thought critical to weapons development are now readily available around the world. Products that will be affected by the Administration's new export policies include:

■ **Computers** The Administration on October 6 announced its second major decontrol of computer exports. The first, in September 1993, increased 40-fold the threshold at which computer exports require a license issued by the Department of Commerce (DOC). The latest decontrol links the degree of deregulation to the country of destination. Computer shipments to Western allies and Japan, for example, no longer require DOC licenses. For China and the former Soviet republics, however, a two-tiered licensing scheme will now apply. For computers with composite theoretical performance levels in excess of 2,000 million theoretical operations per second (Mtops), shipments to military endusers require a DOC license. For products destined for civilian endusers however, the licensing threshold has now been raised to 7,000 Mtops. The decontrol, which is predicated on a US government interagency consensus that computers are not useful in the development of unconventional weapons, should boost US exports of the next generation of computers to China.

■ **Encryption software** For years, US software and computer companies have chafed under a regulatory regime that licenses exports of commonly available software programs with encryption features—including Lotus Notes and Norton Utilities—as munitions items. In practical terms, the requirements meant that exports of these items required a munitions export license issued by the State Department's Office of Defense Trade Controls (ODTC). Pursuant to the US arms embargo against China, ODTC rejected all China licenses unless the President signed a special waiver.

On August 17, the White House announced that it would reclassify many encryption software products as commercial goods and allow their export to most countries—including China—without any licensing requirements. Implementation of this decontrol is contingent upon a special agreement between industry and government to establish agents responsible for the decoding keys, should the US government need to decode communications encrypted by foreign terrorists and criminals.

■ **Equipment for personal use** Also awaiting implementation is a separate initiative to lift munitions licensing requirements on exports of hand-carried laptop computers equipped with encryption software programs. Currently, all such laptops require ODTC-issued munitions export licenses, and ODTC is enjoined from issuing licenses for China under the ongoing arms embargo. Elimination of this requirement, which is violated thousands of times each day by unwitting corporate travelers, would come as a tremendous relief to companies seeking to be in full compliance with US export controls.

—Erik C. Wemple and E. J. Prior

guard against destabilizing transfers. Partners are also required to be members in good standing of existing nonproliferation regimes and must adopt export policies for sales to proliferating states.

Moreover, the New Forum also has no list of controlled goods and technologies. The putative purpose of the arrangement is to prevent the export of conventional weapons and related technologies. While there is a notification requirement for arms exports, partners determine for themselves which items, based on their utility in developing weapons, should be controlled. This structure compares poorly to the previous COCOM rules, which defined a firm list of controlled items.

Because of this lack of enforcement mechanisms, compliance among member countries will be uneven. The New Forum lacks a strong secretariat—which COCOM had—to oversee implementation and execution of the agreements among partner countries. For example, COCOM rules required partners to review jointly particularly sensitive exports to countries of concern. One dissenting vote among COCOM's 17 partner countries was enough to block a proposed shipment; this veto power was often wielded over exports destined for China. The New Forum has nothing approximating this level of discipline.

Next steps

Lacking the strict enforcement and framework for international technology transfers afforded by the old COCOM regime, the New Forum will have little practical impact for US exports to China. What is now exportable to China will likely remain so after the agreement takes effect early next year. Given this scenario, it is unlikely that China will see fit to join the regime, especially since it played no part in forming the New Forum. Even if China does show a desire to accede to the New Forum, Beijing must first demonstrate some willingness to meet the requirements set forth by the agreement; namely, China must develop its own national export control laws and comply with the policies of the other multilateral nonproliferation regimes.

For its part, the United States appears to be moving toward easing export restrictions of certain goods regardless of China's status within the New Forum. Although Washington maintains its post-

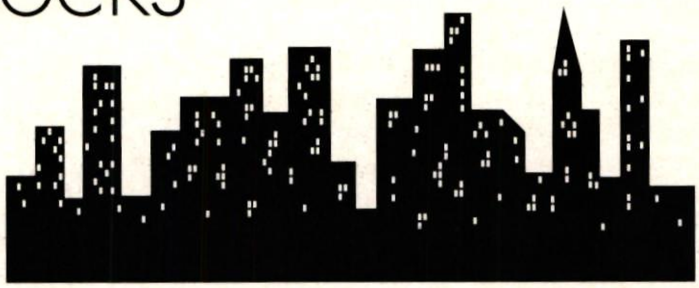
> The New Forum will not likely obstruct China's access to Western technology because it has no true enforcement power.

Tiananmen embargo on China, retains controls on some dual-use exports to China, and is considering a third round of export sanctions to punish Beijing for continuing its missile sales to Pakistan, the Clinton Administration is putting the finishing touches on a few regulatory changes that will make it easier to export high-technology goods to China (*see* box). The changes will deregulate exports destined for most countries—not just China—and stem from a Clinton Administration pledge that US export licensing threshold requirements keep pace with technological advances.

Barring a profound change in Beijing's proliferation activities and human rights record, US export control policy toward China is likely to continue with routine decontrols. No initiatives aimed at according China special technology access are expected, nor are post-Tiananmen sanctions likely to be dismantled. And if the past is any guide, Washington will continue to dangle—and periodically impose—its arsenal of trade sanctions against Beijing for any perceived exports of weapons technology to developing nations.

For whatever reasons, Washington's carrot-and-stick approach—the promise of greater access to technology and the threat of sanctions as punishment for transgressions—to securing Beijing's adherence to the various non-proliferation regimes has failed. The New Forum is unlikely to alter Beijing's cost-benefit analysis, for China's access to technology will remain largely unchanged. 完

Opportunity Knocks



■ Rosemary Gallant

Hong Kong's bold infrastructure plans look beyond 1997

■ **Rosemary Gallant is a US & Foreign Commercial Service officer in Hong Kong. The views expressed in this article are those of the author and do not represent those of the US government.**

Though the global spotlight on Hong Kong lingers on the territory's sometimes rocky real estate and stock markets—and other signs of the rough transition ahead to Chinese sovereignty—far less attention is paid to the many business opportunities there for US companies (*see* list). The territory's open, service-dominated economy grew by more than five percent this year—and 1995 was a slow year. While many companies overlook Hong Kong in their race to pursue larger infrastructure markets like China, the territory's absence of trade barriers and complete freedom of capital movement make it a desirable place to do business.

Bright prospects

With public- and private-sector spending on major infrastructure projects projected to exceed $45 billion over the next decade, Hong Kong's infrastructure sector is particularly promising for US suppliers of goods and services. Almost $21 billion of the projected infrastructure spending will be allocated to the Chek Lap Kok (CLK) Airport and related Airport Core Projects, which are already well underway. The Mass Transit Railway and Kowloon Center Railway will be expanded, at an estimated cost of at least $14 billion.

In addition, the Hong Kong government will allocate over $1 billion each year for the next five years for highway-related construction. The development of municipal sewage treatment projects, solid waste incinerators, and industrial wastewater treatment plants presents environmentally focused firms an estimated $2.5 billion in business opportunities over the next five years. Hong Kong also expects to begin the expansion of its container port facilities, a massive project that will require roughly $2.3 billion in investment. Deregulation of Hong Kong's telecommunications market, meanwhile, will likely result in at least $1.5 billion in investment opportunities for new telephone service providers.

While it provides public-sector funding for many major infrastructure projects, the Hong Kong government also invests in and operates infrastructure commercially where possible. Private funds are being tapped to develop airport services, container terminal facilities, telecommunications networks, landfills, highways, tunnels, and many other infrastructure projects. Government spending on public works has doubled since 1990; private sector financing has also grown. While it is difficult to calculate an exact breakdown of privately or publicly funded projects, the Hong Kong government counts on the private sector to finance many projects but generally maintains a role in the tendering process (*see* p.32).

While competition for a Hong Kong government procurement contract can be stiff, foreign bidders can expect to escape many of the bureaucratic delays or payment and currency problems that tend to plague sales efforts on mainland China. Moreover, as Chinese officials carefully study the choices made in Hong Kong, success on a Hong Kong project can translate into success on the mainland. Chinese subway planners look to Hong Kong's Mass Transit Rail Corp. executives for mass transit tips, for example, while Chinese and Hong Kong civil aviation officials compare notes on air traffic equipment.

In addition, new partnerships are emerging between US and Chinese firms in Hong Kong to work on infrastructure projects in both Hong Kong and China. AT&T Wireless Services, formerly McCaw Cellular Communications Inc., for example, is in a consortium with Hong Kong-based Sun Hung Kai, ABC (a local paging company), and a Chinese Ministry of Posts and Telecommunications subsidiary. Bechtel Enterprises A-P, which operates one of Hong Kong's four cellular networks and is bidding on both personal communications services (PCS) and cordless access services (CAS) licenses, is also working with Guangdong Enterprises, Guangdong Province's trading arm in Hong Kong, on the proposed Shenzhen Toll Road.

Several US companies have found strong Hong Kong partners as well. Over the past three years, Browning-Ferris Industries' joint venture with Swire Pacific Limited has won more than $750 million in Hong Kong landfill and refuse transfer station contracts. Motorola Inc. formed a joint venture operating a cellular network with Hutchison Telecommunications, a division of the property company Hutchison Whampoa. US West Inc. is working with New World, another Hong Kong property giant, to establish a new fixed-line telephone network in the territory.

Staking out a presence

Despite these successes, US companies are still under-represented in many major projects. For example, the Hong Kong government spent $120 million on the Tsing Yi Island Chemical Treatment Center to treat hazardous waste and has allocated another $1 billion for other sewage projects over the next four years. Of the 142 engineering consultants registered with the Hong Kong government to work on these projects, only seven are from the United States. Some US firms have shown an interest in the projects, but have not taken the next step of establishing a full-time presence in the territory, which is often necessary to bid successfully on large projects in Hong Kong. US firms are similarly trailing in the race for CLK airport contracts, winning less than three percent of the contracts to date. Although many reasons, such as the inexperience of US firms in the region, their lack of a Hong Kong presence, or the fact that US bids may not be competitive, may account for the small percentage of Hong Kong government contracts awarded to American firms, no US company even bid on either of the two major contracts—valued at over $2 billion—awarded this year for the CLK passenger terminal.

Although many reasons may account for the small percentage of Hong Kong government contracts awarded to American firms, no US company even bid on either of the two major CLK contracts—valued at over $2 billion—awarded this year.

Many US firms may have also shied away from bidding on other major projects, fearing a playing field tilted toward the United Kingdom. To date, Japanese companies, in fact, have won the largest share (25 percent) of the Airport Core contracts, which include bridges, highways, and other airport facilities. Hong Kong companies are a close second (23 percent), followed by UK firms (16 percent). Most of the major project winners have been consortia involving both foreign and local companies. Mainland Chinese companies are increasingly part of the winning consortia.

Promising sectors

To better their chances of winning bids, some companies, especially those with significant resources to invest, may want to form or join consortia, while other, smaller companies may seek to supply the Hong Kong government directly with goods or services. Whether joining consortia or soliciting the Hong Kong government directly, US firms have particularly strong sales prospects in several infrastructure-related sectors:

■ Construction

The construction and property sectors together contribute to Hong Kong's GDP as much as the wholesale, retail, import-export, restaurant, and hotel sectors combined. According to a recent Hong Kong government report, the territory spent $11.5 billion in 1994 on construction, an 18 percent increase over 1993. Public housing development, private residential and commercial development, and major infrastructure projects will continue to create demand for imported construction equipment over the next few years.

Hong Kong, which does not produce construction equipment locally, imported some $480 million worth of equipment in 1994. According to industry experts, about 50 percent of the construction equipment imported is not new. Major suppliers come from several European countries, but Japan, the market leader, has captured almost the entire used equipment market and 50 percent of the new equipment market. In contrast, the United States has captured only three percent of the overall construction equipment market. All kinds of construction equipment—including excavators, graders, loaders, bulldozers, cranes, and dumptrucks—remain in great demand.

■ Environmental equipment

Hong Kong's environmental projects have cost more than $2 billion over the last five years. The next round of environmental infrastructure contracts to be awarded by the government in coming years will include a $100-$150 million livestock slaughterhouse with significant allocations for air and water pollution control equipment; longer-term plans include spending up to $300 million for two municipal solid waste incinerators. US firms have captured approximately 10-15 percent of Hong Kong's $600 million in sewage disposal contracts and 80 percent of the $500 million in landfill and refuse transfer station projects, positioning the United States as a market leader. The value of public-sector projects related to environmental infrastructure is expected to drop beginning in 1996, but private-sector demand for environmental technologies is expected to grow because tougher regulations on wastewater discharge and chemical waste disposal are scheduled to take effect in the same year.

Additional opportunities in niche markets have emerged for several types of

The United States has captured only three percent of the overall construction equipment market.

Making the Short List

To qualify to bid as a prime contractor on Hong Kong government-funded works projects, interested companies must register with the department or the respective policymaking branch of the government secretariat. Evaluation criteria used in the approval process include the company's technical expertise, local experience, and financial position. The application procedure usually takes two-three months.

Works Branch

One of the branch's seven departments—Architectural Services, Civil Engineering, Drainage Services, Electrical & Mechanical Services, Highways, Waterwork, and Territory Development—evaluates the company's technical expertise, while the financial unit of the Works Branch evaluates the company's financial capabilities. As the company is required to prove its local experience in most cases, US companies should either maintain a presence in Hong Kong or team up with local consultants or contractors. Applications for inclusion in the Works Branch list should be addressed to:

Works Branch
Professional Services Unit
Tel: 852/2848-2122
Fax: 852/2523-5327

Hong Kong Government Supplies Department (GSD)

To bid on contracts from over 80 government departments, foreign companies must contact the GSD, the Hong Kong government's central purchasing, storage, and distribution arm. During the 1995 fiscal year that ends next March, GSD will tender offers with an estimated total value of $600 million. Tenderers usually have about six weeks to prepare their offers and are urged to submit bids valid for at least 30 days. American companies furnished nearly 32 percent ($173 million) of GSD's $540 million in purchases last year, including radar systems, computer hardware and software, medical equipment and supplies, and environment-related products.

Along with pre-registration, a direct presence in the territory or representation via a local agent or distributor is essential to sell successfully to the Hong Kong government. Over 90 percent of GSD contracts were awarded through selective or single tender bids, with notices going only to companies pre-registered with GSD. Only four percent of the contracts for US products went directly to US companies without representation in Hong Kong.

Tender invitations are provided to the foreign trade commissions in Hong Kong, and total bid prices and names of the winning tenderers are published weekly in the *Hong Kong Government Gazette* and in the major Hong Kong newspapers. The commercial service of the US consulate general also reports tender announcements to the Commerce Department's National Trade Databank. Suppliers seeking more information on the Hong Kong GSD should contact:

Government Supplies Department
Tel: 852/2802-6100
Fax: 852/2510-7904

In addition to registering directly with the Works Branch, parties interested in participating in specific Works Branch projects should register with the appropriate Hong Kong government department.

Civil Engineering Department

This department is responsible for administering environmental, transport, and civil engineering contracts, and makes referrals for consulting work on these projects. The department keeps a list of 200-300 pre-qualified consultants, 95 percent of whom have Hong Kong addresses. To register, contact:

Civil Engineering Department
Tel: 852/2762-5018
Fax: 852/2714-0064

Architectural Services Department

This department holds jurisdiction over the architectural consultants board, which is responsible for bidding out consulting work for government building projects. Its list includes over 100 pre-qualified consultants. To register, contact:

Architectural Services Department
Tel: 852/2867-3577
Fax: 852/2877-0594

Hong Kong Environmental Protection Department (EPD) Technical Support Unit

This unit keeps its own independent list of more than 80 environmental consultants pre-qualified to bid on EPD-developed consulting projects. To register, contact:

Hong Kong EPD
Tel: 852/2835-1330
Fax: 852/2591-6662

—*Rosemary Gallant*

environmental technology in Hong Kong over the next five-year period, including diesel particulate control equipment ($5-$10 million); energy-efficient building technology, including lighting, insulation, and air conditioning systems ($5-$10 million); indoor air pollution equipment ($5-$10 million); industrial air pollution control ($5-$10 million); and electric vehicles (an estimated $50 million). Companies interested in pursuing the market for environmental products are encouraged to contact the US-Asia Environmental Partnership at the US consulate general in Hong Kong (*see The CBR*, July-August 1994, p.44).

■ Telecom

Hong Kong, the first city in the world with an entirely digital-fixed network, has one of the world's most advanced telecommunications systems. Its fax penetration rate, or number of fax lines per person, is second only to Japan's. Hong Kong's 65 percent telephone density is second only to Japan's in Asia. Twenty percent of the population, or 1.2 million residents, subscribe to pagers. This summer, the government opened local voice service to three new companies, leaving international voice service as the sole telecommunications service under monopoly control. Deregulation of the local telecommunications industry is furnishing foreign telephone service providers, including many US firms, with an admission ticket to a multi-billion-dollar telecommunications market. Moreover, Hong Kong Telecommunications Limited is currently test marketing video-on-demand services over its telecommunications lines. As telecommunications and broadcasting technologies converge, the demand and possibilities for TV programming will likely increase for foreign firms. The Discovery Channel is now negotiating with Wharf Cable to begin joint operations in Hong Kong, and CNBC, which has already started operations, will soon be broadcasting 24 hours a day.

The Hong Kong mobile telecommunications market is undergoing tremendous change as well. The Telecommunications Authority, the body responsible for regulating this sector, will issue up to six PCS licenses and up to four licenses for CAS, the newest generation of communications services. A total of 14 interested parties, including four US firms, have tendered offers for PCS licenses, and two US firms have bid for CAS licenses.

Participating in a Hong Kong project gives US companies a solid base in the region as well as ready access to longer-term projects in other Asian countries.

Best Bets

The following sectors in Hong Kong are considered the top 10 prospects for US sales:

- Construction equipment
- Drugs and pharmaceuticals
- Electric power systems
- Electronic parts and components
- Insurance
- Plastic materials and resins
- Scientific and analytical equipment
- Telecommunications equipment
- Travel and tourism services
- Wastewater treatment technologies

—US Foreign & Commercial Service

Bureaucratic basics

The abundance of infrastructure projects in Hong Kong has kept the government's Works Branch and its seven departments responsible for administering government procurement contracts busy. In 1995, the Works Branch will issue approximately $2.5 billion in construction contracts—including land reclamation, maintenance of landfill, drainage service, bridge, airport-related, and highway projects.

The Works Branch maintains a list of contractors pre-qualified to bid on projects. The list is currently composed of about 400 firms, including 66 foreign companies. Only one American firm is on the list, although some US firms may be listed as Hong Kong companies if they provided a Hong Kong address as the company's headquarters. The Works Branch also maintains a list of approved suppliers of materials and specialist contractors for public works. Bids and contracts are handled by one of seven Works Branch departments. Architectural and construction services contracts, for example, are awarded through open bidding or the direct invitation to submit bids, processes which are arranged by the appropriate Works Branch department.

Hong Kong and beyond

Hong Kong's marketplace is as dynamic as any in the world, presenting American firms with new chances to win infrastructure contracts. Environmental regulations, the result of higher educational standards and quality-of-life concerns, are spurring the private sector's demand for electric vehicles and air pollution monitoring and control technology. Long-entrenched and protected telecommunications monopolies and oligopolies are facing deregulation and new competition.

Investing in Hong Kong's infrastructure market can increase the visibility of US firms. Participating in a Hong Kong project gives US companies a solid base in the region as well as ready access to longer-term projects in other Asian countries like China, Vietnam, and India. Though the bidding can be tough and the profits slim, there is no question that US companies benefit from the chance to showcase their technology and expertise in Hong Kong, a place with high international visibility. As Britain's influence wanes and 1997 approaches, increasing PRC involvement in Hong Kong's infrastructure market and a healthy Hong Kong government balance sheet suggest continuing infrastructure plans—making room for more active US participation in one of the territory's most thriving sectors. 完

Banking on Change

■ Lester Ross and Mitchell A. Silk

Reforms aim to put the financial sector on more solid ground

■ Lester Ross and Mitchell A. Silk are attorneys in the New York and Hong Kong offices, respectively, of Chadbourne & Parke LLP, where they specialize in project finance, banking, and environmental law.

Until recently, control of the money supply, bank supervision, commercial banking powers, and the conduct of commercial transactions in China were governed by a fragmented regulatory environment. For many years, the People's Bank of China (PBOC)'s regulation of the money supply and supervision of financial institutions was subject to political interference and required the use of cumbersome credit allocations. Banks themselves operated under severe pressure to extend credit to favored borrowers on preferential terms. Commercial transactions were conducted in an uncertain legal context that was largely silent with respect to penalties on defaulting borrowers.

Recent policy and legislative developments have laid the foundation for a more commercially oriented and comprehensive regulatory regime. This spring and summer, the National People's Congress (NPC) and its Standing Committee successively enacted a much-anticipated wave of banking reforms, including the People's Bank of China Law (PBOC Law), the Commercial Banking Law, the Negotiable Instruments Law, and the Guarantee Law. Though the new laws await clarification through implementing regulations and judicial interpretation, their enactment nonetheless constitutes an important milestone in the modernization of China's fiscal and monetary systems.

A new banking regime

Prior to the enactment of the new legislation, considerable progress had already been made in the banking sector—yet another indication of the limited extent to which the policymaking process in China is subject to legislative mandate. Changes in the PRC's leadership, beginning with the appointment of Vice Premier Zhu Rongji as PBOC governor in 1993, brought a new professionalism to the central bank, especially with regard to control of the money supply. Recent policy changes have accelerated the commercialization of the big four State-owned specialized banks—Agricultural Bank of China, Bank of China, Industrial and Commercial Bank of China, and People's Construction Bank of China. In addition, three new State-owned banks—Agricultural Development Bank of China, Export and Import Credit Bank of China, and State Development Bank—were established to assume the policy-lending functions previously held by the big four banks. Additional licenses have been issued to joint stock company banks, and some credit cooperatives are expected to be upgraded to banks, thereby creating increased competition in the banking industry.

As part of the PRC's determination to place policymaking on a legislative foundation, the PBOC Law was enacted and came into force on March 18, 1995. The PBOC Law resolves several issues governing the PBOC's internal organization, monetary policy, and bank supervision, and also gives the institution much firmer authority to exercise its mandated functions, including the formulation and implementation of monetary policy. The law fails to address the insurance industry, however, suggesting that the industry may be removed from central bank supervision.

The enactment of this law follows a series of shifts in the PBOC's mission. Since its founding in 1948, the PBOC operated as the nascent PRC central bank. For many years, the PBOC also exercised lending powers as one of the PRC's only banks, but its remaining lending functions were transferred to the four State-owned banks following the Third Plenum in 1978. In 1993, the PBOC was further ordered to terminate its involvement in commercial enterprises and its interests in various economic entities to enhance professionalism within the bank and prevent potential conflicts of interest.

In the past, the PBOC often came under pressure to tailor its credit and supervisory policies on behalf of favored interests. Article 7 of the new law authorizes the central bank to resist such pressure by confirming its autonomy from local governments, other government departments, enterprises, and individuals. Article 2, however, also expressly subordinates the PBOC to the State Council; Article 5 requires the State Council to approve PBOC decisions on monetary policy and exchange rates. Thus, as with laws pertaining to the central banks of Japan and many European countries, the PBOC Law enhances the PBOC's autonomy but does not insulate it from control by the State Council. In contrast to these central banks, the Federal Reserve System functions as an independent US government agency.

The PBOC's operations traditionally have been affected by fuzzy lines of authority and a tendency for its branches to act independently. The PBOC Law's Article 9 clarifies the lines of authority, stipulating that the central bank be led by a governor, who is assisted by one or more vice governors, all of whom are appointed by China's premier. Article 11 directs the PBOC to establish a monetary policy commission that will operate under regulations still to be promulgated by the State Council. Article 12 further re-

The PBOC Law creates the potential for the NPC to exercise quasi-democratic influence on the central bank and increases the potential for PBOC policy to become an issue in contests for political power.

duces the influence of local governments over monetary, credit, and bank supervisory policy, stipulating that the central bank exercises unified leadership and control over its branches which are agencies of the PBOC. As a check on integrity and policy implementation within the PBOC, Article 36 provides that the central bank will establish an internal audit and examination system, and strengthen its own internal organization and control.

One of the most controversial aspects of the new law is the power accorded to the NPC. Article 6, for example, requires the central bank to submit work reports on monetary policy and supervision to the NPC Standing Committee. The NPC actually rejected an earlier draft of the PBOC Law precisely because it lacked such a reporting requirement. Article 9 provides that the premier's appointment of the governor (but not of the vice governors) shall be confirmed by either the NPC or its Standing Committee. Thus, the PBOC Law creates the potential for the NPC to exercise quasi-democratic influence on the central bank and increases the potential for PBOC policy to become an issue in contests for political power.

More monetary tools

Much of the PBOC Law focuses on monetary policy. Article 22 gives the central bank indirect instruments to regulate the money supply, potentially reducing the PBOC's dependence on crude credit controls. Specifically, Article 22 authorizes the PBOC to establish the prime lending rate; operate a rediscount window; lend funds to commercial banks; require banking institutions to maintain reserve funds; trade treasury bonds, other government securities, and foreign exchange; and use such other instruments as may be approved by the State Council. Use of certain of these instruments, notably the rediscount window, is dependent on the promulgation of implementing regulations.

Moreover, Article 28 bars the PBOC from covering government budget deficits and acting as a primary purchaser or sales agent for government bonds. Chapter 5 of the PBOC Law provides a legislative mandate for the supervision of banking institutions. The PBOC Law's intent is to abolish direct credit controls and mandatory loan requirements while preserving the PBOC's power to establish interest rates or interest rate ceilings. Article 31 confirms the PBOC's licensing authority over banking institutions, thereby enhancing the bank's capacity to outlaw irregularly established financial institutions. Article 32 also confirms the PBOC's authority to conduct bank examinations—including compliance with the PBOC's interest-rate policies on loans and deposits. Article 33 gives the PBOC authority to require banking institutions to submit reports on their finances and operations to the PBOC, and further authorizes the PBOC to supervise the conduct of banking operations by State-owned policy banks.

With regard to banking operations, the new law calls upon the PBOC to perform a supporting role in commercial banking without itself assuming commercial banking functions. For example, the PBOC will be able to help banking institutions establish an interbank settlement system, once the PBOC promulgates regulations. As part of the effort to increase economic responsibility among borrowers and local governments, Article 29 limits the authority of the PBOC to make loans or issue guarantees except under limited circumstances. The PBOC may not extend credit to local governments, government departments, non-banking financial institutions, other enterprise units (*danwei*), or individuals. By its silence, Article 29 may authorize the central bank to extend credit to the central government, multilateral organizations, and foreign governments. The PBOC also may not guarantee loans to *danwei* or individuals. Again, the statute, by its silence, may authorize the central bank to provide credit support for loans to local governments and government departments. Present policy, however, discourages the PBOC from providing support for government loans.

Defining commercial powers

While the central bank professionalizes, the commercial banking sector is also getting its house in order. The ongoing conversion of specialized banks, the pending conversion of credit cooperatives, and the formation of new commercial banks rendered the need for a commercial banking statute acute. The lack of a statute facilitated the formation of unofficial banks, blurred the distinctions between commercial banks and other financial institutions, slowed the development of the banking system, and hampered the PBOC's ability to regulate the money supply.

The Commercial Banking Law, which came into effect on July 1, 1995, clarifies the powers of commercial banks. The law establishes regulatory barriers, prohibiting commercial bank involvement in non-traditional banking activities like insurance and securities—and inhibits the expansion of commercial banks in a manner similar to the US Bank Holding Company Act (BHCA) and Glass-Steagall Act. Ironically, these US laws are currently under attack in the United States.

Article 2 of the Commercial Banking Law defines commercial banks as enterprise legal persons established in conformity with the Company Law that engage in such businesses as taking retail deposits, making loans, and handling domestic and foreign settlements. Article 88 applies this statute to foreign-invested commercial banks, Sino-foreign equity joint-venture commercial banks, and branches of foreign commercial banks, except to the extent that it conflicts with applicable statutes and regulations. Under Articles 4 and 22, domestic commercial banks are held responsible for their own profits and losses, are free from interference by units or individuals, and are subject to enterprise-wide liability. The statute encourages commercial banks to be managed on a centralized basis. This provision should encourage head offices to supervise more closely the operations, particularly the international operations, of their various branches, which often appeared to operate as independent entities.

> Although commercial banks may engage in the government securities market and conduct certain activities in the financial bond market, the Commercial Banking Law prohibits them from engaging in investment banking or from investing in domestic real estate except for their own use.

Chapter 2 of the Commercial Banking Law also governs the formation of new commercial banks. All applicants require PBOC approval, strengthening the PBOC's authority to close down unregistered institutions. The minimum registered capital requirements are ¥1 billion for commercial banks, ¥100 million for urban cooperative banks, and ¥50 million for rural cooperative banks. Existing commercial banks are temporarily grandfathered. The establishment of branches and the acquisition of interests of 10 percent or more in any bank are subject to PBOC approval.

Chapters Three and Four of the new law impose new regulatory requirements and add a legislative imprimatur to existing regulatory requirements. Article 32 imposes a statutory reserve requirement, Article 36 requires borrowers to provide guarantees or collateral, Article 39 grants legislative status to existing risk-based capital requirements, and Chapter Four tightens regulatory requirements regarding lending.

Although commercial banks may engage in the government securities market and conduct certain activities in the financial bond market (*see* box), Article 43 prohibits them from engaging in investment banking or from investing in domestic real estate except for their own use. Article 43 further prohibits commercial banks from investing in domestic non-banking financial institutions. Commercial banks with interests in such enterprises are required to divest under regulations to be drafted by the State Council.

The big four State-owned banks are not treated well under the new statute, which retains State controls. Though the law requires that pre-existing banks, including the four large State-owned banks, be reorganized by an unspecified date in accordance with the Company Law, it is not clear to what extent they will be removed from direct State ownership. Article 18 also requires that each wholly State-owned commercial bank establish a board of supervisors comprised of representatives of the PBOC and concerned government departments, as well as experts and workers. State-owned banks must still issue policy loans if so ordered by the State Council, even though the formation of the policy banks in 1994 was supposed to free the big four from such burdens. The State Council is required to compensate the big four State-owned banks for any resulting losses under regulations that have yet to be adopted.

Furthermore, the divestiture provisions of the law particularly threaten the big four State-owned banks, all of which have generally profitable trust and investment or other subsidiaries engaged in the securities business. Compulsory divestiture or liquidation may be difficult to implement because few domestic entities have the means to absorb their interests.

Who Does What

Along with formulation and implementation of monetary policy, under Article 4 of the PBOC Law, the PBOC is authorized to issue currency and regulate its circulation; issue approvals to and supervise financial institutions; supervise and regulate financial markets; promulgate regulations and issue orders governing financial supervision and businesses; administer the State's foreign exchange and bullion reserves; manage the State treasury; supervise the orderly operation of the payment and settlement systems; assume responsibility for statistics, investigations, analysis, and forecasting in the financial sector; engage in international banking operations as the State's central bank; and perform such other functions assigned to the PBOC by State Council regulation.

Article 3 of the Commercial Banking Law limits commercial banks' powers to include receiving retail deposits; making short-, medium-, and long-term loans; handling domestic and foreign settlements; discounting negotiable instruments; issuing financial debt securities; functioning as the agent when issuing, redeeming, and underwriting government bonds; trading government bonds; engaging in interbank lending; acting as the agent in purchasing, selling and trading foreign exchange; providing letter of credit services and guarantees; acting as payment and collection agent and insurance agent; furnishing safe deposit services; and engaging in such other businesses as may be approved by the State Council.

Articles 34 and 37 of the Guarantee Law designate the kinds of property that can or cannot be mortgaged. Property that can be mortgaged includes improvements and fixtures on land owned by the mortgagor; machinery, vehicles, and other assets owned by the mortgagor; land use rights, improvements, and fixtures owned by the State; State-owned machinery, vehicles, and other assets for which the mortgagor has disposition rights; land use rights to wasteland subject to the owner's consent; and other property which is eligible for mortgage under law.

The following types of property cannot be mortgaged: property with granted or allocated land ownership rights (*see* p.40); property for which land use rights are mostly collectively owned; facilities of non-profit institutions; property for which ownership and/or land use rights are in dispute; property which the government has distrained or taken into custody; and other property which is ineligible for mortgage under law.

Article 42 of the Guarantee Law also lists numerous mortgage registration authorities and their jurisdictions, including the land administration bureau, which registers land use rights to unimproved land; local government-designated departments, which are in charge of urban real property and rural enterprise factory sites; the forestry bureau, which has domain over forests; relevant transportation departments, which are responsible for aircraft and other vehicles; and State Administration of Industry and Commerce branches, which hold jurisdiction over equipment and other movable enterprise property.

—Lester Ross and Mitchell A. Silk

Enhancing the payment system...

Intended to reduce fraud and bring order to the draft market and payment system, the Negotiable Instruments Law should facilitate modernization of the payment system in a manner comparable to that achieved by Article 3 of the Uniform Commercial Code in the United States. The statute, effective January 1, 1996, applies to all transactions in drafts, promissory notes, and checks in the PRC, including foreign-related negotiable instruments, defined as instruments for which draft, endorsement, acceptance, guarantee, or payment occurs in part within and in part outside the PRC. The statute also provides that international treaty and practice shall prevail regarding gaps in the statute or conflicts between the statute and a PRC treaty in force. Standard conflict-of-law provisions—such as the law of the place of draft and the law of the place of issue, rather than the law of the place of payment—are included in the new law. Thus, foreign law will apply to negotiable instruments drafted or issued outside China. A particularly welcome provision for foreign businesses in China is Article 97, which allows the parties to adopt the law of the place of payment with regard to the recordings on checks, making checks drawn in China but payable overseas subject to foreign law.

...and protecting property

The last of the four banking statutes passed this year, the Guarantee Law applies to guarantees, mortgages, pledges, liens, and deposits. Effective October 1, 1995, the Guarantee Law is intended to promote economic development by standardizing the secured loan process. The law undergirds the Commercial Banking Law's requirement that borrowers from commercial banks provide guarantees or collateral. Of particular importance is the wide scope given to the concept of security—including pledges of instruments, securities, and intangible property rights as well as mortgages of real property (land use rights but not fees), fixtures, and personal property.

The statute expands upon the law of guarantees. Government departments and non-profit institutions—which previously had the right to issue guarantees, but were prevented from doing so by administrative decree—are now prohibited from issuing guarantees, while branches of enterprise legal persons may issue guarantees only within the scope of their written authority. Guarantees issued by multiple guarantors are presumed to be joint and several rather than individual obligations, unless the guarantee contract specifies to the contrary.

The Guarantee Law specifies the kinds of property that can and cannot be mortgaged. Moreover, the statute also designates the government agencies responsible for mortgage registration, though registration as laid out in the law appears to have overlaps and gaps in coverage (*see* box). For example, coverage for individually owned property is not defined. Until now, registration has been available only in certain localities such as Shenzhen and only for certain types of property. Although the specifics of the registration system will not be known until the promulgation of implementing regulations, the new registration system will greatly reduce the risks faced by lenders. Other stipulations govern which Guarantee Law provisions will take priority and how the provisions will be enforced.

The new legislation constitutes a major step in the reform of the banking system by enhancing the authority of the PBOC, facilitating development of the commercial banking industry, and clarifying the rules governing commercial transactions.

International implications

The four statutes enhance the implementation of China's financial liberalization and internationalization policies. The Commercial Banking Law furthers China's commitment to the establishment of a banking system reliant on commercial, not policy, tools. The supervisory provisions of the PBOC Law and Commercial Banking Law solidify the foundation for the establishment of a regulatory and monitoring system for PRC financial institutions oriented toward the type of comprehensive worldwide banking supervision envisioned by the Basle international banking supervision regime. These developments are critical to the further international expansion of PRC financial institutions, as well as to the safety and soundness of China's own banking system. What is more, the impact of the Commercial Banking Law on the reform process will affect the competitiveness of Chinese banks as more foreign banks and Sino-foreign joint-venture banks enter the market.

The Guarantee Law and the Negotiable Instruments Law promise to bring substantial regularity to credit transactions in China. This is important for purely domestic transactions and also is critical to attracting participation by foreign financial institutions. On a macro level, the PBOC Law's impact on monetary policy will affect all foreign investors and lenders.

The new legislation constitutes a major step in the reform of the banking system by enhancing the authority of the PBOC, facilitating development of the commercial banking industry, and clarifying the rules governing commercial transactions. But progress also depends heavily on the promulgation of implementing regulations. Nonetheless, the creation of a statutory foundation, including the development of new regulatory instruments within the PBOC and the clarification of transactional rules, represents a long-awaited first step toward real reform of China's banking industry. 完

The Law of the Land

■ Nicholas C. Howson

Foreign investors should understand the technicalities of land use rights

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The scenario is now common to almost any joint-venture negotiation in China. A foreign investor, anxious to invest, sits opposite the leading personnel of a potential Chinese partner—most often a State-owned enterprise or former State-owned enterprise recently re-organized as a company. The cash-poor Chinese partner is eager to put forth as its in-kind contribution the hard assets it has operated for years—its buildings and what is often incorrectly referred to as "land." The parties seemingly strike a deal, leaving only the task of determining the exact value of the Chinese partner's contribution to be worked out.

At this juncture, one of the most crucial issues of joint venturing in China today arises: whether the potential Chinese partner has title, under Chinese law, to the land and buildings it proposes to inject into the venture; whether this title can be transferred or leased legitimately to the proposed venture; and how such property is to be valued. Given the wholesale changes in Chinese land law over the past five years and the sometimes chaotic transition from a State-planned economy to a partially market-based system "under law," more often than not the Chinese partner does *not* have title to the real estate it wishes to contribute; is not permitted by law to transfer rights to use the site to any party, Chinese or foreign; and may not fix a value upon such rights without undertaking a complex valuation and approval process.

The complexities of land use rights and real estate transactions in China clearly warrant more attention from foreign investors in the negotiation process. The lack of clarity regarding contributions of land and buildings to joint ventures, in most cases, reflects general ignorance about recent legal and policy changes in China—an ignorance which often extends to the local government or land and real estate authorities tasked with implementing the new laws.

Laying the foundation

Before 1988, the State or collectives owned all land and rights to use land in China. The alienation, or conveyance, of land ownership or use rights in the PRC lacked a legal basis and was therefore prohibited. Since 1988, China has made important changes in law and policy designed to recognize value in real estate and create a market for this commodity (*see The CBR*, September-October 1993, p.38). The results have been significant, but have also created nettlesome problems for foreign investors.

Amendments to the PRC Constitution and the Land Administration Law in 1988 allowed the alienation of long-term rights to use land and created a formal legal system for the transfer for value of long-term rights to use State- or collectively owned land. Thus, the PRC managed to avoid the ideologically prickly question of ownership; the underlying property continued to be *owned* by the State (or collectives), and only the alienation of long-term *rights to use* such land became permissible.

In May 1990, the State Council promulgated the Provisional Regulations of the PRC Concerning the Grant and Assignment of the Right to Use State-owned Land in Urban Areas (the 1990 Grant Regulations), which drew a distinction between rural and urban land. Under these regulations, rural land is to remain under the ownership and control of collectives for agricultural uses, and may not be placed into commerce (unless it is transformed into "urban" land). Conversely, land use rights covering some types of urban land were allowed to be placed into a new marketplace, and transferred for value between private parties. The regulations divide urban land use rights into "allocated" land use rights (those acquired without payment of value) and "granted" land use rights (those acquired for value). In principle, only granted land use rights can be transferred, sold, leased, or mortgaged.

In March 1992, the State Land Administration Bureau (SLAB) promulgated the Provisional Measures on Administration of Allocated Land Use Rights (the 1992 Allocated Land Measures), clarifying how allocated land use rights are to be held and transferred. The 1995 Urban Real Estate Management Law also addresses land use rights questions, but largely echoes the prior regulations.

Granted land use rights...

The 1990 Grant Regulations allow SLAB or its local bureaus to grant land use rights to foreign or domestic companies, enterprises, organizations, or individuals by auction, tender, or agreement. In all cases, the party receiving the grant of the land use rights (the grantee) must sign a land use rights grant contract with the relevant land administration bureau and pay a grant fee (*churang jin*) to the bureau. Only once such a contract is signed, and the grant fee paid in full, are the rights to use a particular piece of urban land deemed fully granted and transferable. The regulations stipulate that maximum terms for grants of land use rights range from 50-70 years, depending on whether the land will be used for commercial, industrial, or residential purposes. Upon full payment of the grant fee, the grantee receives a land use certificate (*tudi shiyong zheng*) issued by the granting land administration bureau.

> The grant fee can be very high—often reaching several million dollars for an undeveloped plot of land.

The grant fee can be very high—often reaching several million US dollars for an undeveloped plot of land—since authorities typically calculate the fee to represent some notion of the net present value of the revenues obtainable from the underlying property, once developed, over the full grant term. While the amount of the grant fee is determined by an appointed appraisal firm in conjunction with the relevant land administration bureau and any foreign investors involved, it also varies depending on the location of the underlying land and the identity of the grantee. Typically, the grant fee demanded from foreign-invested enterprises (FIEs) is higher than that from Chinese enterprises that have been in the locale for a long period of time. SLAB is in the process of promulgating laws and schedules that will dictate how grant fees should be calculated and which administrative body can establish minimum levels, ostensibly to forestall below-value transfers of State assets.

The land use rights grant contract usually contains certain conditions. The grantee may be required to pay the full grant fee within a certain time period (not to exceed 60 days by statute), or obliged to undertake a minimum amount of development or investment in the land before the land use rights can be transferred. Any subsequent purchaser or transferee of land use rights may hold the rights only for the remainder of the original grant term under the grant contract.

...vs. allocated land use rights

Notwithstanding the crucial market reform brought about by the creation of a system of granted urban land use rights, the great majority of land use rights enjoyed by domestic enterprises in China are not "granted," but rather "allocated." Most allocated rights were given to State enterprises long ago, allowing use of the subject land for an indefinite term without payment of value, subject only to the annual payment of a "land use fee [tax]" (*tudi shiyong fei [shui]*) to the local government.

The 1990 Grant Regulations dictate that allocated land use rights may only be made transferrable if they are transformed into granted rights, which entails payment in full of a grant fee with respect to such rights. Such rights may be transferred, leased, or mortgaged only upon the approval of the local land administration bureau (and the local real estate bureau if buildings on the land are to be included in the transfer). The potential grantee must obtain a land use certificate (and a building ownership certificate for any buildings on the land), enter into a contract for the grant of the right to use the land, and pay retroactively a fee to the local municipal or county people's government for the grant of the right to use the land. Once the transformation from allocated to granted land use rights is complete, the rights holder (the grantee or any subsequent transferee) is no longer legally liable for the land use fee. This mechanism affords the State an opportunity to capture value in land long held under allocated rights, rather than let the value flow to the transferor, who had previously used the land essentially for free.

The problem for joint ventures

Before Beijing issued the 1990 Grant Regulations, many Chinese partners to Sino-foreign joint ventures made in-kind contributions to particular ventures in the form of land use rights. Because these contributions of rights predated the 1990 Grant Regulations and, in some cases, the 1988 Constitutional and Land Administration Law amendments, land use rights were uniformly allocated, regardless of whether they were labeled as such. Valuation of this type of in-kind capital contribution was usually negotiated between the Chinese and foreign partners to the joint venture and the local government. Even in the early 1980s, however, a foreign investor was well advised to request evidence of the Chinese partner's claim to the land use rights it proposed to contribute to the venture. Such evidence usually consisted of a land certificate (*tudi zheng*)—not the land use certificate created by SLAB after 1990—in the name of either the Chinese partner or the joint venture itself.

The implications of the 1990 Grant Regulations and the 1992 Allocated Land Measures caused a conceptual difficulty with respect to the structuring of joint ventures. Both items of legislation state that land use rights may be transferred only if the holder (the transferor) has signed a grant contract and paid a grant fee for the land use rights in question. All relevant pieces of legislation, including the 1995 Urban Real Estate Management Law, are silent on the question of whether contribution of land use rights to a Sino-foreign joint venture constitutes a "transfer" for purposes of the 1992 Allocated Land Measures or the 1990 Grant Regulations. Until 1994, SLAB held that a Chinese partner to a bona fide *manufacturing* joint venture would not be required to convert allocated land use rights into granted land use rights, or pay the grant fee, before vesting such rights in the joint venture. SLAB changed its view in 1994, and indicated that allocated land use rights for *any* joint venture must first be granted by the State to the Chinese partner.

SLAB's formal position with respect to land use rights law is now clear. Any investment of land use rights by a Chinese

Coming into Compliance

Prior to 1990, when China created the land use rights grant system and the State Land Administration Bureau (SLAB), countless joint ventures were formed in which the PRC partners made in-kind contributions of allocated land use rights. Even after the regulations were passed, joint ventures continued to be formed in which the PRC partner contributed allocated land use rights. Joint ventures established before 1990 that did not verify that a grant fee was paid, however, were not acting in contravention of the law, since no law existed at the time of their establishment. Nonetheless, SLAB officials now want land use rights attached to all such projects to be "brought into conformity" with the law before the land use rights being held in, or the real estate developed on, the projects is able to be sold, leased, or mortgaged. SLAB has indicated informally that a remedial payment (*bujiao*) of a grant fee—"remedial" because the land use rights were already transferred to the joint venture in exchange for equity credit—must be paid with respect to previously allocated land use rights injected into a joint venture.

SLAB has blithely indicated that it will likely ease the burden of this retroactive application of the law by either lengthening the period over which such remedial grant payments must be made or assigning some portion of the value of the land use rights to entities representing the State, which would effectively add a new partner to the joint venture. SLAB has also indicated that such payments could be "reduced or exempted" upon negotiation with individual entities.

On January 1, 1995, SLAB started a campaign to regularize land holdings in China by requiring that all enterprises, including foreign-invested enterprises (FIEs) established before 1990, submit to SLAB or the local land administration bureau all documents relating to the granting of title, including joint-venture contracts, land certificates, and enterprise approvals. In effect, the notice requires all joint ventures established in the PRC to submit all documentary evidence showing how, and from whom, they obtained the right to use the site upon which their facilities stand. For most joint ventures established in the 1980s, such evidence will consist of the joint-venture contract and articles of association, which contain stipulations regarding the PRC partner's contribution of long-term land use rights to the joint venture as approved by the Ministry of Foreign Trade and Economic Cooperation or its local commission.

The clear implication of SLAB's call for such documents is that FIEs likely will be required to make a remedial grant payment to gain true title to the land use rights or negotiate an exemption or reduction in the amount of such a fee. Few, if any, FIEs have complied with the call to submit documents or even register their land use rights, since the various authorities concerned will certainly seek a substantial payment from any joint-venture investor who voluntarily seeks to normalize land holdings. Most FIEs will only undertake the land use rights grant process if they seek to use their land and buildings for financing purposes or raising capital based upon the joint venture's revenues, in which case they may be willing to pay a large price for such normalization. An FIE that fails to heed SLAB's directive, however, will be left with the uncertain status quo and a potentially dubious title to the site on which its investment sits.

—Nicholas C. Howson

partner into a Sino-foreign joint venture after May 1990 constitutes a transfer of such land use rights and, thus, if such rights were or are allocated, they must be transformed into granted rights and a grant fee must be paid before they can be contributed to the joint venture legitimately. The amount of the grant fee will be determined after formal appraisal by a qualified appraisal authority and through consultation between the foreign and PRC investors. For joint ventures established before May 1990, the land use rights situation must be "regularized," (*zhengchanghua*)—the rights to use land transformed into granted rights—and the relevant land administration bureau must receive a remedial payment (*bujiao*) of the grant fee (*see* box). The same is true for joint ventures established before 1990 with land use rights that were subsequently extended, through amendment to the joint-venture contract, after 1990.

A PRC partner to a joint venture may not contribute buildings as an in-kind contribution to a joint venture without first obtaining granted land use rights to the site.

Buildings and fixtures

What comes with the land is also open to scrutiny. Not surprisingly, many Chinese joint-venture partners already operate factories and seek to contribute these buildings along with land use rights as a component of their registered capital contribution to the joint venture. The 1995 Urban Real Estate Management Law confirms much of the law and doctrine contained in the 1990 Grant Regulations and the 1992 Allocated Land Measures, but focuses on the pre-existing or planned buildings on the sites subject to land use rights. The law holds that ownership of a building requires ownership of the underlying land use rights. Thus, a PRC partner to a joint venture may not contribute buildings as an in-kind contribution (or sell such buildings) to a joint venture without first obtaining granted land use rights to the site underlying such buildings. The 1995 Urban Real Estate Management Law, however, further complicates matters for joint ventures by permitting the leasing of buildings on land for which rights are allocated, but only if an unspecified portion of the rental payments goes directly to the State.

Asset appraisals

The State in China, once the holder of productive assets "on behalf of the whole people," is focusing increasing attention on how State assets are being placed into commerce. China has created a system whereby entities that have used assets for decades must have the same assets appraised or revalued before the assets are released into the private economy—and, in the case of land use rights and buildings, before they are granted or contributed to a Sino-foreign joint venture. As a result, as a Chinese partner sorts out the title and transferability of the rights to the land and buildings it has been using, the same land use rights and buildings must be appraised by the State-owned Assets Bureau (SOAB), an increasingly powerful government agency. SOAB's mission is to ensure that value derived from such assets is directed to the State, and not to the PRC partner who has merely used the assets for years.

So it is that the unsuspecting Chinese partner to a joint venture may be informed by counsel or real estate authorities of any of the following pieces of bad news: It cannot transfer, lease, or otherwise sell the land it has been using to the proposed joint venture without completing the burdensome appraisal and grant procedures and paying the required grant fee; it cannot transfer or otherwise sell the buildings on the land to the joint venture until it has sorted out the underlying land use rights that must be transferred with the buildings, though it may lease the buildings if a significant portion of the revenue goes to the local land or real estate administration bureau; or, the value it can obtain for such land and buildings, whether as credit against its required contribution to the registered capital of the venture or as lease payments, will be determined only after a formal consultation with SOAB, a watchdog that looks out for low valuations or illegal transfers of State assets. Each of these points, though supported fully by Chinese law, will come as a great shock to the PRC partner, especially if the entity has used the land and buildings—and made improvements therein—for several decades.

Risky business

The risks of not complying with the post-1990 enactments as now interpreted are threefold: condemnation of rights;

loss of value and liquidity; or large cash outlays and increased capital expenditure. A joint venture that holds allocated land use rights as a result of the Chinese partner's capital contribution to the venture, or purports to lease allocated land use rights from its Chinese partner, runs the risk that the land use rights will be confiscated, denied, or withdrawn, with only minimal compensation.

This may be what happened to the McDonald's franchise in Beijing when authorities asked it to vacate its site on Wangfujing Street in late 1994. Whether the rights to the land used by McDonald's were contributed or leased to the joint venture, they most likely were not granted by, or the subject of a land grant contract from, the applicable land administration bureau. Thus, the transfer of such rights into the joint venture as a capital contribution or their leasing to the joint venture without some remedial payment of a grant fee would make the original transfer or lease ineffective and allow the Beijing government to reallocate the subject rights with only minimal compensation to McDonald's. Any joint venture that elects not to obtain granted land use rights for a new venture, pay the remedial grant fee for an existing venture, or obtain a grant contract leaves itself open to the troubles McDonald's has experienced.

The failure to obtain granted status for land use rights may also restrict a joint venture's ability to effect a subsequent transfer of such rights or employ the value of land use rights and buildings for financing by offering them as security. This problem will, of course, be most burdensome for real estate developers, but also for any joint ventures that find themselves holding allocated land use rights as an asset contributed as registered capital. The stipulation that allocated rights cannot be mortgaged restricts the ability of joint ventures that hold allocated rights to raise financing based on the joint venture's land use rights holdings. Land use rights are most often the first and easiest item to offer up as security to lenders because, despite the promulgation of the new PRC Mortgage Law in 1995, no real national system is in place to ensure the creation, perfection, registration, and notification of security interests in movable assets, personal property, or equipment. Security interests in buildings can be taken only in completed buildings that have been granted a completion certificate by relevant administrative authorities following construction.

For joint ventures such as manufacturing enterprises and hotels that operate on identified sites for long periods of time, the inability to hold allocated land use rights as a capital asset or as leased property may ultimately serve to deter potential investors. Most multinational investors will not commit to a joint venture that lacks an unassailable claim to use the land upon which it will build its industrial facilities.

Perhaps the most immediate problem for joint ventures posed by the 1990 and 1992 laws is that joint ventures (or their investors) will be required to make large cash payments to fund a grant fee to lock in the venture's land use rights for terms of 50-70 years. As is often heard in negotiation rooms in China, "someone must pay" the grant fee to obtain or effect transfer of the rights. Because in many cases the Chinese partner has little or no cash, often the foreign party will need to contribute additional cash to obtain granted land use rights for the existing or proposed joint venture.

Strategizing

How, then, is a foreign investor to ensure that its joint venture obtains the benefit of unassailable land use rights? There are several options, each with different levels of risk and expense. First, the foreign investor can insist that the PRC partner obtain granted land use rights from the relevant land administration bureau, and contribute or lease the same to the joint venture. This goal is often difficult to achieve, as it requires the PRC partner to pay the grant fee to the local land administration bureau to obtain the desired rights—an awkward proposition, given many Chinese partners' firm belief that they own the land they have used for up to several decades, not to mention their typically low cash reserves. In some cases, local land administration bureaus have taken into account costs borne by a PRC landholder in developing a site over the years, and have decreased the amount of the grant fee accordingly. Obviously, any such accommodation only happens if the PRC landholder and the land administration bureau enjoy a good relationship.

Alternatively, the foreign investor may choose to have the joint venture itself be the direct grantee of the land use rights by having the joint venture enter into a grant contract with, and pay a grant fee to, the land administration bureau. This has an immediate disadvantage for the foreign investor, because, in most cases, the local land administration bureau will expect a higher grant fee from a joint venture and thus the foreign investor will have to increase its cash contribution to the venture to fund the payment of the grant fee. While the foreign investor will benefit from a commensurate increase in its share of equity in the venture, obtaining and funding a direct grant of the land use rights will in most cases necessitate a significant readjustment in the foreign investor's capital budget for the project. This option is typically the least attractive to the Chinese partner, since it requires the Chinese partner to forfeit the benefit of the major asset it thought it had to contribute to the venture as registered capital—land use rights. Further, this option redirects a large payment of cash away from the Chinese entity and toward the land administration bureau as compensation for an asset the Chinese entity has used and developed for years. If the PRC partner really had the land use rights to transfer or lease, it could gain any transfer or lease payments—or equity credit and associated dividend flows—for such rights. Instead, the PRC partner is told that it lacks ownership of the asset and must watch as several million dollars go to the land administration bureau.

A third option for the foreign investor is to insist that the PRC partner obtain granted land use rights, but take a non-intrusive posture with respect to investigating and understanding the grant transaction. In this scenario, the foreign investor may ask only to see a valid land use rights certificate as proof that such rights have been granted and that a grant fee has been paid to the land administration bureau. The foreign investor should also seek explicit written assurances from the bureau that the rights have been *irrevocably* granted. This assurance is crucial, as applicable law makes clear that land use rights may not be transferred until the grant fee has been paid in full, which must occur within 60 days of signature of the applicable land use rights grant contract by the land administration bureau and the grantee. Failure to pay the grant fee in full within 60 days allows the land administration bureau to take back the land use rights at will.

Under this third option, the Chinese partner may strike its own deal with the land administration bureau, asset appraisal authorities, and SOAB to reduce or waive the grant fee, or extend the payment time frame. If such a strategy is pursued, the Chinese partner may offer to lease the land use rights to the joint venture, with lease payments from the joint venture neatly matching the Chinese partner's staggered land grant fee payments to the land administration bureau. The theory behind this approach is that the foreign investor and its joint venture are entitled to rely upon the land use rights certificate and related assurances produced by the land administration bureau, even if the Chinese partner has reached a special accommodation with the relevant authorities. While this strategy may not be one that provides the greatest security in law, it is increasingly being used as partners look for ways to solve the difficulties inherent in the transitional application of imperfectly understood laws coupled with cash shortfalls.

The situation with respect to the transfer of buildings seems to be the most insoluble problem. Unfamiliar with the law, most Chinese entities will refuse to believe that they do not own or cannot transfer buildings they have constructed, even if they are finally convinced that they lack transferable rights to use the underlying land. The Chinese partner will be no happier when told that it can lease buildings atop such land subject to allocated rights, but only if the State receives a significant portion of the lease revenue. In the current transitional period, the conundrum of transferring rights to land containing existing buildings to Sino-foreign joint ventures will likely be sorted out through special approvals given jointly by the local land administration and real estate bureaus—or new bureaucratic actors that are mergers of these bureaus, such as has occurred in Beijing, Shanghai, and Shenzhen.

Above all, foreign investors are well advised to understand from the start of any negotiation the exact status of proffered real estate and the ability of a Chinese partner to apply such rights to a future venture. The costs of any misunderstanding—in time, capital, and irritation—are too great for foreign and Chinese entities to overlook such characterizations as mere legal niceties. Land laws are unlikely to change dramatically; only the understanding of present laws described here is likely to improve. While China's land laws are met with a great deal of resistance throughout the country, a few Chinese partners are becoming conversant with the issues and addressing them unprompted. Some potential Chinese co-investors now even seek assurance from potential foreign partners that the foreign investors truly require granted land use rights for the joint venture. This is a positive development, as it indicates increasing compliance with the law and an understanding of the crucial needs of foreign businesspeople. 完

Council Formally Opens Hong Kong Office

At a festive reception at the Furama Hotel in Hong Kong on September 18, Council President Robert Kapp joined nearly 100 Council members and guests for the formal establishment of the Council's Hong Kong office, which opened for business in June. Hong Kong Office Director Pamela Baldinger, former editor of *The CBR*, pledged an intensive effort to bring the Council's wide-ranging services directly to the doorsteps of member companies with personnel in the colony and southern China.

In his remarks, Kapp offered the Council's thanks to the numerous Hong Kong-based organizations that have made him personally welcome over many years. Representatives from the Hong Kong government, the US consulate general, the New China News Agency, the American Chamber of Commerce, and other trade bodies attended the reception.

Delegation Focuses on Trade Secrets

On September 5-12, the Council hosted a delegation from China's State Economic and Trade Commission (SETC), which was visiting several cities in the United States to learn about trade secret laws. The 18-member delegation, led by Tang Haibin, division chief of SETC's Bureau of Economic Regulations, included officials from various ministries, law-related bureaus, and State-owned companies. The State Council, Ministry of Foreign Trade and Economic Cooperation, Beijing Municipal Intermediate People's Court, and China Petrochemical International Co. were among the organizations represented.

While in Washington, the delegation met with various Council member companies and US government officials to discuss methods of protecting US trade secrets, rulings on trade secret cases, and international trends in trade secret protection. Upon their return to China, the delegation will assist in drafting China's trade secret protection laws, scheduled to be promulgated in 1996.

Among those hosting meetings with the delegation were the law firms of Gibson, Dunn & Crutcher; Mudge Rose Guthrie Alexander & Ferdon; and Graham & James. Delegation members also met with officials from the Office of the United States Trade Representative, Federal Bureau of Investigation, and the state and commerce departments, as well as lawyers from Rohm & Haas and E. I. du Pont de Nemours & Co. to hear about company concerns relating to trade secrets.

Legal Committee Meets

Hosted by the offices of Chadbourne & Parke LLP, the Council's Legal Committee held one of its largest meetings to date in New York on September 27, 1995.

The meeting, chaired by Winston & Strawn's Ben Fishburne, focused on several recent Chinese regulations in the financial sector. Larry Greenwald of Aetna started the discussion with an overview of China's new Insurance Law. Lester Ross of Chadbourne & Parke then offered the group a thorough analysis of the People's Bank of China Law (*see* p.35). The Chase Manhattan Bank's Wilfred Chow presented a detailed synopsis of the new Commercial Banking Law, and Maurice Lynch of Soble & Associates discussed the new Guarantee Law.

Council Seminar Looks at Labor Issues

The Council's September 21 seminar on China's social insurance system, held in Beijing, provided members with a comprehensive look at compensation and benefits requirements at both the national and municipal levels. Speakers from the Ministry of Labor, Ministry of Health, State Council Leading Group on Housing Reform, and local labor bureaus of Beijing, Shanghai, Tianjin, and other cities outlined the emerging social insurance system and discussed efforts to move from an enterprise-based to a city-based system of administration.

Four US companies gave presentations on their human resource requirements and social insurance needs. Chinese officials detailed the liabilities borne by foreign-funded enterprises for employee pension, health insurance, maternity, housing, unemployment, accident and disability, and enterprise-based welfare funds.

Yu Xiuzhi of the Dalian Social Security Company talks about welfare reforms.

Jumping into Cyberspace

■ James Glasse

Is China ready for the Internet?

■ **James Glasse is proprietor of J.G.A. Information Services, a research and consultancy firm in West Sussex, United Kingdom. He has authored two books on China's economy and is currently researching ways foreign companies can identify sources of tied and untied aid for China investments.**

With more than 25 million people around the world already linked to the Internet's 20,000 networks, we live in the age of global computer communications. China, too, is poised to move into the fast lane of the information superhighway. For Western and Chinese companies, the prospect of increased Internet use in China should mean easier communications—and greater access to China-related resources (*see The CBR*, September-October 1993, p.14).

But access and information come at a price—one which Beijing may be reluctant to pay. In linking Chinese computer users to foreign information and ideas, the Internet will also likely pose a threat to the government's control apparatus. Although the Chinese leadership appreciates the benefits access to the Internet will afford the country, it also recognizes that such access will erode Beijing's ability to temper the spread of foreign ideas within the Chinese population.

The current attitude among the leadership appears to be one of "if you can't beat them, join them." By encouraging the growth of the Internet in China, Beijing hopes to channel resources to educational and business-related areas which it thinks are important. But once the necessary hardware is in place, Beijing's attempts to control the flow of data into China likely will be in vain. Whether Beijing will try other methods of censorship remains to be seen.

Getting wired

Currently, however, the biggest barriers to widespread use of the Internet in China are technical rather than political. China's data communications infrastructure lags far behind that of the industrialized world. Although recent estimates suggest that the country will be the greatest market for computer technology and services worldwide and will be the world's largest telecommunications market within the next five years, China is still in the early stages of developing a comprehensive data network. There are some two million personal computers now in use in China, and the numbers are increasing by approximately 30 percent per year. Recent estimates suggest that 60,000 of these computers are presently connected to the Internet, and this number is also increasing. With only seven servers offering public access to the Internet, access in China falls well below that available in the United States or other industrialized countries, where hundreds of Internet providers are now in operation.

China's two data communications lines connected to the Internet, the China Public Packet Switching Data Network (ChinaPac) and the China Public Data and Digital Network (DDN), service the entire country from Beijing and Shanghai. At present, terminals in more than 650 cities are connected to the Internet via ChinaPac, and 292 cities are linked to the information superhighway through DDN, with more cities coming on-line each month. Compared to satellite or fiber-optic links capable of connecting to the Internet at 40 million bits per second (bps) in other countries, ChinaPac—the fastest domestic link—can only connect to the Internet at a speed of 256,000 bps-2.04 million bps. Because of the large amount of traffic accessing the two public Internet connections, users report problems logging onto the Internet even in China's major cities.

As more people become interested in using the Internet, access in China will be constrained further by the shortage of telephone lines to transmit electronic data domestically to individual computer terminals. In 1994, China had only 2.14 main telephone lines per 100 people. This lack of available lines has already hindered China's ability to use the latest computer technologies. For example, some 90 percent of the hardware imported into China since 1992 to maintain more than 100,000 electronic mail (e-mail) boxes remains idle because phone lines are not available to provide reliable Internet connections. Other imported information technology has proved useless because it is incompatible with China's equipment.

Over the long term, though, China's underdeveloped telecommunications infrastructure may actually be an advantage. Unlike other countries, China will be spared the agony of trying to employ obsolete technology to establish connections between indigenous computer networks and the worldwide Internet. By starting from scratch, the country can "leapfrog" to the most current generation of computer equipment and build the bulk of its data communications infrastructure with state-of-the-art technology that can easily communicate with the global Internet.

To encourage the growth of the business-related aspects of Internet connections and other data communications applications, Beijing has launched numerous projects to boost satellite and fiber-optic cable links to facilitate banking, communications, and the exchange of information. Beijing hopes that the projects will form an integral part of the Internet in China and will serve as the

Getting Connected

Obtaining access to the Internet in China is complicated by the relative shortage of data lines and access providers—not to mention the added bureaucratic layers. The speed and quality of the connection are also impeded by the lack of hardware in China to accommodate the information flow.

Though additional Internet providers in Dalian, Hangzhou, Shenyang, and Guangdong Province are expected to become operational by the end of the year, the demand for reliable connections continues to increase. To set up an Internet account, China-based users have several options.

ChinaNet provides access to most Internet applications. China-based users must subscribe to ChinaNet's dial-up port services to connect to the Internet. The current start-up and installation fee for this service is ¥2,400 ($290) with a monthly port charge of ¥50 ($6).

For more information, contact:
Beijing Telecom
Tel: 8610/201-2994
Fax: 8610/201-2992
e-mail: noc@net.cn
or
Shanghai Telecom
Susan S. Zhu
Tel: 8621/327-1014
e-mail: admin@public.sta.cn

China Institute of High Energy Physics (IHEP) established full access to the Internet in May 1995 and now provides users in Beijing with access to most Internet applications.

For more information, contact:
IHEP Computer Center
Xu Rongsheng
Tel: 8610/821-3344 ext. 450
Fax: 8610/821-1215
e-mail: xurs@bepc2.ihep.ac.cn

Great Trend Electronic Information Services, Inc. (GTEIS), a subsidiary of the Shenzhen Securities Exchange, plans to provide stock and bond quotes through a full-service Internet node by the end of this year. GTEIS' lines support all Internet applications, and lease lines are available.

For more information, contact:
GTEIS
Wang Qiang
Tel: 86755/320-2236
Fax: 86755/320-2229
e-mail: zhaoe@shell.cninfo.co.cn

Fanda Electronic Information Ltd. (FEIL), developed by the Wuhan Foreign Investment Bureau, began providing Internet services in early August 1995. FEIL's current services are limited to dial-up and leased lines and cannot support graphics applications such as the World Wide Web. Subscribers to FEIL's dial-up service can access e-mail, telnet, and file transfer protocols.

For more information, contact:
FEIL
Liu Xun
Tel: 8627/284-0895
Fax: 8627/284-0896
e-mail: yamin@fanda.co.cn

Tianjin XianDao Information and Network Ltd., established in April 1995, aims to provide Internet access to all computer users in the Tianjin Economic Development Area via dial-up services or leased lines. Subscribers can apply for an e-mail account and various types of Internet access.

For more information, contact:
Tianjin Xiandao Information and Network Ltd.
Jiang Tao
Tel: 8622/730-8706
Fax: 8622/734-6615
e-mail: liangzx@istic.sti.ac.cn

Internet contact information provided by Lou Gallio and AsiaInfo Services, Inc.

cornerstone of China's emerging data communications network. A number of foreign companies have been providing technical expertise and foreign investment to establish the groundwork for efficient data communications within the country (*see* p.50).

A New Kind of Library

One of the many problems Internet users face is that it is still difficult to separate valuable information from electronic junk mail. Some of the more useful China-related sites include:

China News Digest (CND)
(http://www.cnd.org) This on-line news summary service provides ready access to the latest political and economic trends. Users can view CND information in either English or Chinese. (Chinese readers must, however, have the appropriate software to translate the files into characters.) CND also publishes two newsletters electronically over the Internet.

Hong Kong Supernet
(http://www/asiaonline.net/aol-home.htlml) Offers a directory of academic web sites in Hong Kong, a who's who of the Hong Kong business community, and *Asia Online*, a marketing and research service with information on economic developments in the region.

NetChina
(http://www.netchina.com) To obtain contact information for Chinese companies, users with hypertext ability can click on different NetChina web page names and access numerous China-related sites. Academic journals covering contemporary domestic and international topics are also accessible in both Chinese and English.

—Compiled by James Glasse and Maria Christina Valdecañas. Site addresses are current as of October 1, 1995. The list is not intended to be comprehensive.

Plugging in

The Ministry of Posts and Telecommunications (MPT) regulates China's data communications network, as well as other telecommunications matters. Last February, MPT granted its Beijing and Shanghai branches permission to offer public access to the Internet through ChinaPac and DDN. Technically, any computer user in China with the right computer equipment can now access the full range of services available over the Internet. Since February, additional cities have established Internet provider services, and MPT will probably finalize plans to grant other provinces permission to open Internet connections for public use before the end of the year.

China-based companies wanting to establish an Internet connection must register with MPT or a local MPT branch. A company can also set up its own dedicated data communications line connected directly to the Internet, but must obtain MPT approval (*see* p.48).

Once linked to the Internet, users have access to a wide range of information and services. For US-based companies, the Internet offers an efficient and inexpensive way to send e-mail and data files to their China offices. Although e-mail communications via the Internet are vulnerable to interception, readily available file-protection software makes e-mail communications as safe as regular fax or telephone communications.

The Internet also provides a desktop research tool for users in China and in other countries, allowing companies to explore the growing number of China-related Internet sites and contact other organizations or companies that may be pursuing similar or complementary work. With more individuals, universities, and organizations involved in China-related fields establishing their own Internet sites, access to the worldwide Internet provides a potential means to acquire market research data and other types of information that were previously difficult to obtain. Though much of this information has always been in the public realm, Internet connections have made accessing it as simple as clicking an icon on the computer screen.

For China-based Internet users, access to the Internet opens a window to information from around the world. Sites on the Internet contain everything from US government documents to news releases (*see* box). Some China-based companies and research institutes use their Internet sites as a vehicle for raising awareness for their China-based operations or current research projects.

Full speed ahead?

Although more efficient international communications are sure to aid China's development efforts by linking the country's scientists and researchers to their counterparts around the globe, public access to the Internet is likely to attract information and activities Beijing is not willing to condone. MPT can limit the number of Internet accounts serviced in the country, but has no way of controlling the information a user accesses once his account is operational. If the leadership attempts to place a ban on new accounts, resourceful users with sufficient funds will likely find ways to circumvent the ban, perhaps connecting to the Internet through providers outside the country.

The High-Tech Road

According to Chinese government sources, over 60,000 computer suppliers, information brokers, and information service companies with more than 1 million employees and revenues exceeding $1 billion were operating in the country in 1994. During China's Ninth Five-Year Plan (1996-2000), the government will invest approximately $29 billion in State funds to advance China's information systems infrastructure and is also strongly encouraging foreign investment in the form of technology transfers, equipment purchases, co-production, and management consulting services.

The race is on

Especially in China, there is fierce competition among foreign suppliers to get into the commercial Internet business. This year, with technical support from Sprint International and AsiaInfo Services, Inc., the Directorate General of Telecommunications (DGT)—the telecommunications arm of the Ministry of Posts and Telecommunications (MPT)—launched the country's first commercial Internet connection service—ChinaNet—through the China Public Packet Switching Data Network (ChinaPac) and the China Public Data and Digital Network (DDN). Beijing charged China Telecommunications Corp. (CTC), MPT's multi-billion-dollar marketing arm, with the task of acquiring foreign assistance to integrate existing Chinese computer networks with the worldwide Internet.

Foreign companies can bid for systems integration or facilities management contracts, and are encouraged to participate as joint partners in establishing network infrastructure to connect individual computer systems to the global Internet. Thus far, more than 10 major foreign companies have participated in CTC-sponsored projects. Beijing encourages foreign participation in the production of top-end microcomputers, synchronous fiber-optic systems, and microwave communications systems; software development and production; information and communications networking technology; and international economic, scientific, and technological information services. Foreign companies are prohibited, however, from controlling the operations of any portion of the country's telecom network without a Chinese partner.

China is also experimenting with domestic company-led data communications projects to coordinate the country's banking and financial operations electronically. In September 1994, China launched a composite of eight major, or "golden," information technology projects. Each of these projects will promote information processing around the country by linking economic, industrial, and human resource databases. The kingpin Golden Bridge project will result in a middle-speed data network designed to link multiple information sources into an information clearinghouse.

Jitong Communications Co., the appointed project management firm, is working with the Ministry of Electronics Industry to attract foreign participation. Network construction has already started in 24 localities. IBM Corp. is providing advanced networking and open systems technology. Intel Corp. signed a memorandum of understanding with the Shanghai municipal government to provide Pentium microprocessors in the city's key information projects. Isocor Software Co., is supplying an information management software system.

Similar and perhaps eventually related to the Golden Bridge project is the China National Economic Information System (CNEIS). This ambitious project received initial funding from a $200 million Japanese government loan. The objective of the CNEIS project is to build a nationwide computer network to link the State Planning Commission to each province in China and process national economic data on a real-time basis.

In the wake of the "Goldens" and CNEIS, the UNICOM project was set up in the summer of 1994 by the ministries of electronics industry, power industry, and railways. UNICOM, a State-owned telecommunications company authorized by the Chinese government to provide basic telecommunications services, will soon provide Internet connections.

Gold-rush mentality

With each new development, the number of Internet-accessible networks in China continues to swell—along with the fever to provide more Internet-related services. Many China-based organizations and companies will look to become Internet providers, offering individual computer users access to the Internet for a fee. As in the United States, this movement will likely create many spinoff companies providing information, hardware, software, and networking services.

Thus far, the companies offering Internet provider services have been Chinese owned. Sino-foreign joint ventures will likely assume a greater role in the development of the industry by providing hardware and software products, performing computer systems integration, and providing consulting and management services. DGT, which grants approval for Internet service provider operations, currently will not approve wholly foreign-owned enterprises, but may do so in the near future.

The World Resources Information Network (China) is a prime example of the type of information service company that will likely emerge. The $5 million project was jointly initiated by the Shenzhen New Era Enterprise Co., Ltd. and two American companies—World Resource Network, Co. Ltd. and Senford Co. Ltd. Since May, the network has been connected to other worldwide computer networks, allowing Chinese manufacturers and exporters to transmit product information electronically via the Internet.

Western companies interested in the information services industry in China should perform the usual fact-finding and due diligence exercises to map out a solid long-term market strategy. At present, the lack of regulations governing the industry can be an advantage for foreign companies, since few areas within the information systems industry are closed to foreign involvement—but this attitude may change over time. By claiming a strong market position, offering the latest technology, and designing a coherent business strategy, foreign companies are sure to find virtually unlimited opportunities in the Chinese information industry.

—*Lou Gallio*

Lou Gallio is executive director of AsiaInfo Services, Inc.

Despite the potential for uncontrolled flows, the consensus among the leadership seems to be that the information superhighway will take shape in China regardless of central-level actions. Decisionmakers in Beijing believe that the government's best chance of controlling the Internet will be by channeling resources to groups the leadership has designated as trustworthy. Previous attempts to censor incoming faxes or broadcasts were largely circumvented, and it is unlikely that Beijing will have effective control over Internet accounts once the hardware and physical infrastructure for Internet connections are in place.

For now, besides requiring all account holders to register with MPT, Beijing is trying to limit the number of Internet accounts opened in China by maintaining high connection fees. Future methods of control may include limiting distribution of telephone lines or restricting accounts to research or government-operated organizations that will be strictly liable for the types of information accessed or sent out through individual Internet accounts.

Treading carefully

For its maiden voyage into cyberspace, Beijing has chosen to concentrate on developing the country's data communications infrastructure to support educational exchanges and business communications via the Internet. On the educational front, Beijing initiated the China Education Research Network (CERNET), a countrywide educational network that aims to link more than 1,000 campuses and hundreds of schools to the worldwide Internet by the year 2000. Thus far, CERNET has attracted investment from several Western computer giants, including Digital Equipment Corp., IBM Corp., Intel Corp., Microsoft Corp., Oracle Corp., and Siemens AG.

CASnet, the China Academy of Sciences Network linking some 20,000 researchers and professors in 30 PRC research institutes, makes up one segment of CERNET. Other CERNET segments include the Institute of High Energy Physics Net, the National Computing and Networking Facility of China, Beijing University's PUnet, and Qinghua University's TUnet. The State Science and Technology Commission also maintains a data network known as SSTCnet.

> Foreign corporations increasingly will be able to advertise projects and services in China over the Internet.

The Chinese leadership hopes that Internet connections and the development of information systems will also help forge cities like Beijing and Shanghai into international trade and financial centers. Certain service industries, particularly advertising, banking, insurance, market research, and publishing, will benefit from increased Internet access, allowing them to reach more customers and potential customer bases and exchange information with branches throughout the country in an efficient and timely fashion.

What next?

As recently as 15 years ago, finding dependable market intelligence was practically impossible in the Middle Kingdom. With the arrival of the Internet, those who know where to look can access reliable information on where to buy and source many products and services in China from any workstation in the world. China-based computer users can now communicate with others around the globe through e-mail or file transfers, and computer users around the world can send messages to their Chinese counterparts. Foreign corporations increasingly will be able to advertise projects and services in China over the Internet—as well as access information about competitors and potential markets.

That Beijing is somewhat alarmed by the unlimited proliferation of data communications is understandable. What Beijing decides to do with this window to the world, however, remains to be seen. Initial indications suggest that the Chinese government will continue to encourage use of the Internet for educational and business purposes. If Internet access appears to be getting out of control or moving in directions not welcomed by Beijing, the Chinese government may try to shut down Internet accounts.

Short of Beijing severing all connections to the Internet, however, excitement over the types of information and services available on the Internet will continue. Internet use is likely to rise dramatically during the next three-four years as purchases of personal computers and relevant hardware increase, particularly among affluent citizens in the developed and coastal cities. 完

Growing Out of the Plan: Chinese Economic Reform, 1978-1993

by Barry Naughton. Cambridge, UK: Cambridge University Press, 1995. 379 pp. $49.95 hardcover.

While many recent books and articles address aspects of Chinese economic reform in the post-Mao period, few tackle the reform era in a comprehensive fashion. In *Growing Out of the Plan*, economist and China expert Barry Naughton provides a complete picture of China's macroeconomic and industrial changes from 1978-93. Applying the Chinese metaphor of "groping for stones to cross a river" to the reform process, Naughton argues that Chinese reformers did not shift to a market economy under the direction of a carefully crafted, meticulously implemented plan. Rather, wading through a "swamp" of bad decisions and facing treacherous and conflicting political currents, China's leaders did not begin to develop a coherent policy on economic reform until the early 1990s.

Part narrative and part analysis, *Growing Out of the Plan* is neither overly praiseworthy of the Chinese leadership nor unnecessarily fixated on problems that have arisen from the reforms. The book offers instead a level-headed, concise study of China's ongoing transition from command to market economy. Rife with economic data, the book is written for an academic audience, but remains accessible to a general readership. The story unfolds on the eve of reform and addresses the question of why China chose to make the changes it did in 1978. The heart of the book is divided into three sections covering distinct reform phases. In the final chapters, Naughton documents how China has nearly grown out of the plan altogether and is moving decisively toward a free market. The book concludes by suggesting that China's gradual, somewhat blind approach to reform has proven largely successful, despite lurking concerns over economic and social instability.

A main theme in the book is that the disagreement over basic macroeconomic approaches, fueled by cycles of high inflation and retrenchment, resulted in a compromise strategy: gradual abandonment of the centrally planned economy. As conservatives and reformers were unable to agree whether a planned or free market approach better served the interests of a developing China, the strategy that emerged was to freeze the size of the existing planned economy and let newly established free markets outside of the plan grow in accordance with demand. In this way, the protectors of State-owned industries and the champions of expanding competitive enterprises each helped to mold a uniquely Chinese approach to reform.

Growing Out of the Plan is an important work for those interested in understanding the full complexity of China's economic transformation over the last decade and a half. More important, the book represents a breakthrough study in modern economic development patterns by challenging the theory that socialist economic reform must be quick, merciless, and carefully targeted. *—Paul Lamb*

Paul Lamb is program manager at the US-China Business Council.

Textiles and Clothing in China: Competitive Threat or Investment Opportunity?

by James Glasse. London, UK: Economist Intelligence Unit, 1995. 353 pp. $525 softcover.

Vacillating between good and bad news, this extensive report covers an incredible array of issues pertaining to China's textile industry and trade, though it lacks definitive answers to the sector's problems. A highly readable, practical, and fascinating resource, this book can be used to identify potential investment opportunities in textiles in China.

The report provides copious details about China's textile and apparel industries by region, product, and fiber, as well as a critical review of the role of central- and provincial-level governments in the development of these industries. Glasse's analysis of the US-China bilateral textile trade, though elementary, emphasizes the problem of illegal transshipments of PRC exports through third countries and the potential benefits to China from World Trade Organization membership.

The extended discussion of China's relationships with the European Union, Eastern Europe, Japan, and other Asian nations provides new and interesting comparisons. Foreign investors from these countries see China as a market for their goods and as an export-processing base. The PRC also has found significant opportunities in these countries for PRC textile products. The extent of these trade relationships leaves the reader with the impression that investors who are willing to bear the considerable short-term risks posed by uncertainties in the industry must believe that long-term gains will be substantial.

—Brenda A. Jacobs

Brenda A. Jacobs is an attorney with Powell, Goldstein, Frazer & Murphy.

A Guide to Successful Business Relations with the Chinese: The Opening of the Great Wall's Gate

by Huang Qianyu, Richard S. Andrulis, and Chen Tong. New York, NY: International Business Press, 1994. 254 pp. $49.95 hardcover.

A Guide to Successful Business Relations with the Chinese distinguishes itself from other China business guides by its in-depth analysis of Chinese cultural attitudes and history. The information included in the book is useful and fascinating and, although directed toward businesspeople with little experience in China, should prove interesting even to seasoned China hands. Huang and Chen are both native-born Chinese who are experts on China's cultural and social history; Andrulis is a management consultant and industrial psychologist at Villanova University. The fusing of their ideas creates a unique perspective from which to assess the cultural aspects of Chinese-Western business relationships.

The first part of the book focuses on the relevance of Chinese sensibilities, world views, and history to the conduct of modern business. The chapters include references to literature and ancient events that put modern Chinese ways of conducting business in historical context, and discuss China's national and regional cultural characteristics. The authors also present the results of surveys they conducted in China on such issues as lifestyle priorities and job preferences. Though the authors' argument that historically Chinese culture has viewed commerce negatively is interesting, the heavy reliance on historical sources in a guidebook on modern business practices seems misplaced.

The second half of the book is devoted to conversing, negotiating, and dining with Chinese—what the authors label the "skills necessary to associate with Chinese people." This section contains practical pointers for businesspeople entering the China market for the first time who may be fearful of offending their Chinese colleagues, as well as for veteran businesspeople who have suffered through embarrassing moments at the negotiating or banquet table. In short, reading *A Guide to Successful Business Relations with the Chinese* is time well spent for anyone expecting to forge long-term business relationships in China.

—*Caitlin Stewart Harris*

Caitlin Stewart Harris is business manager of The CBR.

To Steal a Book Is an Elegant Offense: Intellectual Property Law in Chinese Civilization

by William P. Alford. Stanford, CA: Stanford University Press, 1995. 222 pp. $35 hardcover.

In the wake of the recently concluded US-China intellectual property rights (IPR) protection agreement, William Alford's book provides a concise background of the history of the conceptualization of IPR in China. Alford's approach to the topic is unusual. Rather than present the usual laundry list of Chinese offenses, he explains the cultural and historical determinants of China's approach to IPR and suggests that such determinants are the reason China has not fully adopted Western standards of IPR protection.

The bulk of the book details how China's leaders, from imperial times to the present, have viewed intellectual property. During imperial times, China had codes prohibiting the copying of certain texts or use of certain symbols, yet these were designed to protect the legitimacy and power of the emperor rather than act as a copyright. After 1949, similar restrictions were also imposed, this time to maintain Communist Party control of communications and publicly voiced ideas.

Alford's main theme is that China never developed a "sustained indigenous counterpart" to Western-derived intellectual property law because the Chinese did not recognize a need for such protection. He suggests that without reconciling Western views of IPR protection with the cultural and political legacy of China's past, US attempts to force Beijing to abide by Western rules will be less than successful. Alford predicts that a better tactic would be to reformulate the US approach and find common ground between Chinese and Western conceptions of IPR protection. He does not endorse giving in to Chinese violations, but urges those pushing for greater IPR protection in China to look beyond Beijing's seeming intransigence to the reasons for Chinese officials' reluctance to concede to US demands.

While Alford's discussion provides a wealth of information and analysis on Chinese views of IPR, it provides little practical advice for US companies that find their intellectual property rights violated in China. The strength of Alford's book, however, is its ability to step back from the heated debates surrounding China's actions to protect IPR and look at the subject in its entirety. The reader is thus able to gain a deeper understanding of the issue and the obstacles that both China and the United States must overcome if a long-lasting and mutually beneficial solution is to be found.

—*MCV*

Energy in China: Foreign Investment Opportunities, Trends and Legislation

by James P. Dorian. London, UK: Financial Times Energy Publishing, 1995. 150 pp. $560 softcover.

For years, the East-West Center in Honolulu has served as the focal point for research on China's energy industry. Center analysts, including James P. Dorian, are among the foremost experts on energy in China. With the release of Dorian's *Energy in China*, those without the time to peruse thousands of pages of analysis now have an abridged volume on the subject.

Energy in China is an excellent introduction to the world of oil, coal, gas, electric power, and petrochemicals in China. The many organizational charts, graphs, and statistical tables offer an impressive assessment of the PRC's current energy situation. The volume contains much valuable data, such as China's percentage of coal reserves under production and the country's projected regional electricity supply mix in the year 2000. Also included are detailed compilations of foreign investment activity in energy-related ventures along with lists of major laws that affect foreign investment in this sector. Dorian's work incorporates year-end 1993 information as well as some forecast data.

Dorian's concise, clear style makes downstream petrochemical production as easy to comprehend as a high-school textbook. The breadth of coverage, however, prevents detailed analysis. For example, the section on Occidental Corp.'s failed Antaibao endeavor in Shanxi Province, while accurate, fails to elaborate on several reasons for the project's demise, including the resistance of local authorities and the death of Occidental CEO Armand Hammer. The organizational charts for China National Petroleum Corp., China National Petrochemical Corp., and other energy-related agencies also would be more useful for analytical purposes if they offered more details.

Overall, this book would be a valuable addition to the libraries of major oil, petrochemical, electric power, and mining companies. Consultants, lawyers, and other professionals working in these industries might also want to purchase the book for their reference shelves. At $560 a copy, however, the book may be out of reach to all but the most serious players.

—*Daniel Martin*

Daniel Martin is manager of the Council's investment program.

China Telephone Directory 1995

Beijing, China: China Telephone Directory Corp. of the PRC Ministry of Posts and Telecommunications, 1995. 1,165 pp. $79 softcover. Distributed by Volt Asia Enterprises.

A new addition to the growing stack of phone books for China, this directory's distinguishing feature is the imprimatur of the Ministry of Posts and Telecommunications. This comprehensive guide offers listings for obscure local government offices, major foreign companies, and travel service providers—definitely a good investment for businesspeople with activities in China.

The directory's listings are divided into three sections—government and non-commercial, industrial and commercial, and travel and tourism. Within each section, listings are divided according to major municipal areas and provinces. Categories within each regional subheading vary according to the section. In the government section, headings include government organizations, parties and organizations, and universities and colleges. Foreign enterprises in China appear in the commercial pages. All listings in the book include the organization's address in English and Chinese characters, phone number, and, in some cases, fax number.

The book's strongest selling point is the number of cities and towns covered. While other China phone directories include listings for a few cities in each province, this book has listings for an average of seven cities per province, and 21 cities for Sichuan Province alone—a plus for businesspeople with interests in China's more remote regions. A distinct drawback of the two-inch thick directory is the lack of a comprehensive index. Finding the listing for a specific organization may entail wading through different sections and subheadings if it is not immediately obvious how the organization is likely to be categorized.

Certainly a phone directory for China is a must for doing business with Chinese entities. *China Telephone Directory* will fit the bill for the increasing numbers of foreigners with dealings in the PRC's major metropolitan areas and smaller cities.

—KAS

Taiwan's Economic Role in East Asia

by Chi Schive. Washington, DC: Center for Strategic and International Studies, 1995. 104 pp. $14.95 softcover.

Taiwan's Economic Role in East Asia is a valuable background guide for those without prior knowledge of the region and those seeking a quick overview of Taiwan's economic dynamism. Schive explores various issues in Taiwan's economic development, including rapid industrialization during the 1980s, the influence of regional cooperation and competition, and the role of trade in the development of cross-Strait relations. Touting Taiwan's successful pattern of development, Schive proposes the idea of Taiwan as a future regional operations center for foreign companies.

While Schive valiantly makes a case for Taiwan as a leading regional economic power, he covers too many issues and brushes over many specifics. Though seeking to be comprehensive, Schive leaves the reader questioning the value of attempting to cover so much in such a short monograph. For example, Schive barely mentions the political challenges to Taiwan's drive to become a regional operations center, such as the lack of direct shipping and air links to mainland China and Beijing's ability to restrict Taiwan investment on the mainland.

Nonetheless, Schive's statistics on the island economy's investment in the mainland are wide ranging. The real value of the book lies in the more than 30 tables and charts depicting Taiwan's foreign commercial relations over the last 40 years. Covering all aspects of Taiwan's foreign trade and foreign direct investment, these statistics are a handy resource for anyone needing quick and easy access to such data. As a statistical reference—not an analytical tract—*Taiwan's Economic Role in East Asia* hardly disappoints.

—Meredith Gavin

Meredith Gavin is an associate in the Council's business advisory services.

■ Alan R. Kahn

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.

SALES AND INVESTMENT July 3 - September 3, 1995
Foreign party/Chinese party **Arrangement, value, and date reported**

Accounting and Insurance

OTHER

Aon Corp. (US)
Established representative office in Beijing. 8/95.

CIGNA Corp. (US)
Will open representative office in Shanghai. 8/95.

Swiss Life Insurance and Pension Co. (Switzerland)
Opened representative office in Beijing. 8/95.

Transamerica Life Cos. (US)
Opened representative office in Tianjin. 8/95.

American International Group, Inc. (US)
Received license to sell life and non-life insurance products in Guangzhou and opened full-service branch office in Beijing. 7/95.

Agricultural Commodities and Technology

OTHER

World Bank/Tujia-Miao Autonomous County (Sichuan)
Provided $1.1 million loan to construct waterweed-growing technology center and goose hatchery. 7/95.

Banking and Finance

CHINA'S IMPORTS

NEC Corp. (Japan)/PBOC
Sold 300 VSAT satellite communications systems to aid banking settlement business. $36 million. 7/95.

Abbreviations used throughout text: BOC: Bank of China; CAAC: Civil Aviation Administration of China; CNAIEC: China National Automotive Import-Export Corp.; CATIC: China National Aero-Technology Import-Export Corp.; CITIC: China International Trust and Investment Corp.; CITS: China International Travel Service; CNOOC: China National Offshore Oil Corp.; ETDZ: Economic and Technological Development Zone; ICBC: Industrial and Commercial Bank of China; MPT: Ministry of Posts and Telecommunications; NA: Not Available; NORINCO: China North Industries Corp.; P&T: Post and Telecommunications; PBOC: People's Bank of China; SEZ: Special Economic Zone; SINOCHEM: China National Chemicals Import-Export Corp.; SINOPEC: China National Petrochemical Corp.; SINOTRANS: China National Foreign Trade Transportation Corp.; SPC: State Planning Commission; UNDP: United Nations Development Program.

CHINA'S INVESTMENTS ABROAD

Bank of China
Will establish branch office in Ho Chi Minh City, Vietnam. 8/95.

Agricultural Bank of China
Opened its first overseas branch office in Singapore. 7/95.

OTHER

Bank of Tokyo (Japan)
Established representative office in Chengdu, Sichuan Province. 8/95.

Citibank (US)
Opened branch office in Beijing. 8/95.

Commercial Bank of the Republic of Korea
Opened branch office in Shanghai. 8/95.

Dai-Ichi Kangyo Bank (Japan)
Established representative office in Wuhan, Hubei Province. 8/95.

Deutsche Bank AG (Germany)
Established representative office in Shanghai. 8/95.

Fuji Bank (Japan)
Established representative offices in Tianjin and Nanjing, Jiangsu Province. 8/95.

Industrial Bank of Japan
Established representative office in Wuhan, Hubei Province. 8/95.

Nanyang Commercial Bank (HK)
Will open branch office in Beijing. 8/95.

Royal Bank of Canada
Established representative office in Guangzhou. 8/95.

Asahi Bank (Japan)
Opened branch office in Shanghai. 7/95.

Bank of Tokyo (Japan)
Opened branch office in Beijing. 7/95.

First National Bank of Boston (US)
Opened representative office in Shanghai. 7/95.

Hong Kong & Shanghai Banking Corp. (HK)
Opened branch office in Beijing. 7/95.

Nasdaq (US)/Shanghai Stock Exchange
Will provide dual listings on both stock exchanges and will jointly oversee trading activities on China's securities markets. 7/95.

Sakura Bank Ltd. (Japan)
Opened branch office in Tianjin. 7/95.

San Francisco Pacific Stock Exchange (US)/Shanghai Stock Exchange
Formed agreement to provide dual listings on both stock exchanges. 7/95.

Tokai Bank Ltd. (Japan)
Opened branch office in Tianjin. 7/95.

Chemicals, Petrochemicals, and Related Equipment

INVESTMENTS IN CHINA

Ciba-Geigy Ltd. Group (Switzerland)/Shilou Town Economic Development (Guangdong)
Established Guangdong Ciba Polymers Co. Ltd. in Panyu, Guangdong Province to produce and market Araldite epoxy resins used in manufacturing electronics, power equipment, and airplanes. (Switzerland:95%-PRC:5%). $21.7 million. 8/95.

Hercules Inc. (US)/Shanghai Chlor Alkali Chemical
Established joint venture to produce chemicals used in manufacturing high-quality paper. $7 million. 8/95.

Kao Corp. (Japan)/Shanghai Yu Long Enterprise
Will establish joint venture to produce surface-active agents for toiletries. (Japan:75%-PRC:25%). $10.3 million. 8/95.

Sumitomo Corp. (Japan), Dovechem Holdings PTE Ltd. (Singapore)
Established Dovechem-SC Co. wholly foreign-owned venture in Guangdong Province to produce plasticizer for PVC resin. (Japan:30%, Singapore:70%). $10 million. 8/95.

Borealis Holding A/S, a subsidiary of Neste Oy (Finland)/Qilu Petrochemical Co. (Shandong)
Established joint venture in Shandong Province to produce polyethylene. (Denmark:50% -PRC:50%). 7/95.

E. I. du Pont de Nemours & Co. (US)/China National New Chemical Materials Corp., Pacific Chemical (Group) Corp. (Shanghai)
Formed joint venture to produce Delrin acetal polymer used for automobiles, manufacturing, and appliances. (US:50%-PRC:50%). $100 million. 7/95.

Royal Dutch/Shell Group (Netherlands)/Zhejiang Transport Goods & Materials Co., Zhapu Harbor Administration (Zhejiang)
Established Zhejiang-Shell Asphalt Co. to produce asphalt and Zhejiang-Shell Chemical Petroleum Co. to produce lubricating oil. (Netherlands:85%-PRC:15%). $50 million. 7/95.

Snamprogetti SPA, a subsidiary of ENI SPA (Italy)/China National Technical Import & Export Corp. (Beijing)
Will establish plant in Nanjing, Jiangsu Province to produce fertilizer from Texaco Inc. and Haldor Topsoe Co. residual oil products. $120 million. 7/95.

Consumer Goods

INVESTMENTS IN CHINA

Avon Products Inc. (US)/NA (Guangdong)
Will build manufacturing plant in Conghua, Guangdong Province to produce cosmetics. $40 million. 8/95.

Fedders Corp. (US)/Ningbo Air Conditioner Factory (Zhejiang)
Established joint venture to manufacture air conditioners. $24.1 million. 8/95.

Henkel KGAA (Germany)/Shanghai Kemeng Group
Established Henkel Kemeng Cosmetics Ltd. to produce and sell personal care products. (Germany:60%-PRC:40%). $15.5 million. 8/95.

LG Group (S. Korea), General Electric Co. (US)/Tianjin Refrigerator Industrial Co.
Established joint venture to produce home appliances. (S. Korea:55%, US:25%-PRC:20%). $99 million. 8/95.

McQuay Asia Co. (US)/New World Refrigeration Industry Co. (Hubei)
Formed Wuhan McQuay Air Conditioner and Refrigeration Co. joint venture to produce air conditioning and refrigeration equipment. $20 million. 8/95.

Mitsubishi Corp. (Japan), Dai-Ichi Kosho Co. (Japan)/China Record Corp. (Beijing)
Formed Shanghai United Optical Disc Factory joint venture to produce compact discs. (Japan:60%-PRC:40%). $1.98 million. 8/95.

WCP International (Holding) Co. Ltd. (NA),Winul International (Holding) Co. Ltd. (HK), Chofu Seisakusho Co. Ltd. (Japan), Philco International (US), Nichimen Corp. (Japan)/Swan Air Conditioner General Co. (Anhui)
Established air conditioner factory joint venture in Hefei, Anhui Province. $110 million. 8/95.

Bosch-Siemens Hausgerate GmbH, a joint venture of Robert Bosch GmbH and Siemens AG (Germany)/Wuxi Small Swan Corp. Ltd. (Jiangsu)
Established Boxiwei Household Electric Appliances Co. joint venture to produce washing machines and other household appliances. $30 million. 7/95.

Kimberly-Clark Corp. (US)/Beijing Economic Technological Investment and Development Corp.
Will form joint venture to manufacture personal care products and Kotex feminine care products. (US:95%-PRC:5%). 7/95.

Merloni Elettrodomestici SPA (Italy)/Haire Group (Shandong)
Established joint venture in Qingdao, Shandong Province to produce washing machines. (Italy:10%-PRC:90%). $29.8 million. 7/95.

Thomson SA (France)/Changhong Television Corp. (Sichuan)
Will establish joint venture to produce large-screen color television sets. 7/95.

OTHER

GLF Investments Ltd., a division of Golden Sky Ventures International Inc. (Canada)/Qingdao Engineering Co. Ltd. (Shandong), Guangzhou Fuguang Co. Ltd.
Formed agreement to distribute parking control devices manufactured by Canadian Parking Equipment Ltd. 7/95.

Simon's Furniture Group (US)
Will open retail branches in Guangdong Province, Beijing, and Tianjin. 7/95.

Electronics and Computer Software

CHINA'S IMPORTS

Motorola Inc. (US)/Hangzhou Telecommunications Equipment Plant (Zhejiang)
Sold total access communications systems (TACS) and ground station equipment. $268 million. 7/95.

INVESTMENTS IN CHINA

Harris Semiconductor, a division of Harris Corp. (US)
Will establish facility in Suzhou, Jiangsu Province to perform final assembly and tests of integrated circuits. 8/95.

Loral Corp. (US)/National Huayun Technology Development Corp., a unit of the Chinese Meteorological Administration (Beijing)
Formed Beijing Huayun & Loral Radar Systems Co. joint venture to produce advanced weather radar systems and Doppler radar. (US:51%-PRC:49%). 8/95.

Polyclad Co., a subsidiary of Cookson Group PLC (UK)/NA (Liaoning)
Established Dalian-Atlantic Co. joint venture to produce laminates for printed circuit boards. (UK:65%-PRC:35%). $15.5 million. 8/95.

Alps Electric Co. Ltd. (Japan)/Tianjin Zhonghuan Electric & Machine-Electric Component Corp.
Established joint venture to produce computer keyboards and electronic components. (Japan:80%-PRC:20%). $5 million. 7/95.

Apple Computer, Inc. (US)/Legend Computer Group (Beijing)
Will jointly establish Apple Software Development Research Center to develop software for educational and personal use. 7/95.

Matsushita Electric Industrial Co. (Japan)/NA (Shandong)
Established joint venture to manufacture television sets for export and formed research and development center for video products. (Japan:50%-PRC:50%). $29 million. 7/95.

NA (Switzerland)/Beijing Zhongan Electronics Group
Established Beijing Zhongan Fire-Control Electronics Co. Ltd. joint venture to produce 511-series electronic products for fire control. 7/95.

NEC Corp. (Japan)/NA (Beijing)
Will establish semiconductor plant to produce microchips. $140 million. 7/95.

Nippon Sheet Glass Co. Ltd. (Japan)
Established Suzhou NSG Electronics Co. Ltd. wholly owned subsidiary in Jiangsu Province to produce sheet glass for LCD displays, copy machines, and fax machine lenses. $23.5 million. 7/95.

OTHER

Compaq Computer Corp. (US)
Will open representative offices in Shaanxi, Liaoning, and Guangdong provinces. 8/95.

IBM Corp. (US)/Beijing Institute of Computer Application and Simulation Technology, an affiliate of China Aerospace Corp.
Will jointly develop and sell Lotus Notes software. 8/95.

MapInfo Corp. (US)
Established office in Beijing for sales, marketing, and customer support. 8/95.

Toshiba Corp. (Japan)
Established Toshiba (China) Co. Ltd. wholly owned subsidiary in Beijing to assist in investment, sales, and marketing. $30 million. 8/95.

Hewlett Packard Co. (US)/Shanghai Analytical Instrument Factory
Formed Hewlett Packard Shanghai Analytical Products joint venture to conduct research on computer components. 7/95.

Mobil Oil Hong Kong Ltd., a subsidiary of Mobil Oil Corp. (US)/Ningbo City (Zhejiang)
Will donate $35,000 to establish computer center. 7/95.

Motorola Asia Manufacturing Research Center (AMRC), a unit of Motorola Inc. (US)/Qinghua University Computer Integrated Manufacturing Systems-Engineering Research Center (Beijing)
Established project to jointly research and develop intelligent machine maintenance tool software. 7/95.

Packard Bell Electronics (US)/Beijing Wired #738 Communications Factory
Established Beijing #738 Factory Baili Computer Systems Co. joint venture to distribute Packard Bell products in China. 7/95.

Packard Bell Electronics (US), Cheflink (HK)/Seastar Group (Shaanxi)
Will form representative office, service center, and retail stores to sell Packard Bell computers. 7/95.

3Com Asia Ltd., a division of 3Com Corp. (US)/Baoshan Iron and Steel Complex (Shanghai)
Will supply computer network products to Baoshan Iron and Steel factories. 7/95.

Tulip Computers (Netherlands)/Sun Tendy Software Co. (Beijing)
Agreed to sell its computers bundled with Sun Tendy Chinese Star 2.0 Chinese language operating system. 7/95.

Unisys Corp. (US)/Founder Group Corp. (Beijing)
Authorized Founder Group Corp. to become general distributor for Unisys personal computer products in China. 7/95.

Unisys Corp. (US)/Huayang Co. (Beijing)
Opened computer specialty store to sell and service Unisys personal computers. 7/95.

Engineering and Construction

INVESTMENTS IN CHINA

Boral Ltd. (Australia)/Shanghai Building Materials Industry Investment Development Corp.
Established Boral Shanghai Building Materials joint venture to produce and sell plasterboard. (Australia:60%-PRC:40%). $66.5 million. 8/95.

Toshiba Corp. (Japan)/Shenyang Elevator Works (Liaoning)
Established joint venture to manufacture elevators and escalators. $10 million. 7/95.

Yungtay Engineering Corp. (Taiwan), Hitachi Ltd. (Japan)
Established Shanghai Yungtay Engineering Corp. to produce elevators. (Taiwan:74%, Japan:26%). $10 million. 7/95.

OTHER

Asea Brown Boveri (Holdings) Ltd. (Switzerland)
Established Asea Brown Boveri (China) Investment Ltd. holding company in Beijing. 9/95.

Arinc Inc. (US)
Received contract to procure $30 million worth of products and services for expansion of Harbin International Airport. 7/95.

Export-Import Bank of South Korea
Will provide $118 million in loans to support Chinese government-sponsored infrastructure projects. 7/95.

Food and Food Processing

INVESTMENTS IN CHINA

IBP Inc. (US), Sand Livestock Systems (US)/NA (Shandong)
Formed joint venture to develop integrated pork production, processing, and marketing operation in Zaozhuang, Shandong Province. 8/95.

Nestle Dairy Farm Holdings SA, a division of Nestle SA (Switzerland)/Guangzhou Peoples Food Factory
Established joint venture to produce and market ice cream and chilled dairy products. (Switzerland:60%-PRC:40%). $6.1 million. 8/95.

Cadbury Schweppes PLC (UK)/NA (Beijing)
Formed joint venture to produce candy. $50 million. 7/95.

Coca-Cola Co. (US), Sire Pacific Ltd. (HK)/CITIC
Established BC Development Co. joint venture in Hefei, Anhui Province to bottle soft drinks. $13.5 million. 7/95.

Ueshima Coffee Co. (Japan)/Dalian Food Industry Co. (Liaoning)
Established joint venture to can coffee grown in Yunnan Province. (Japan:70%-PRC:30%). $5.3 million. 7/95.

Weiquan Group Co. (Taiwan)/Heilongjiang Dairy Farm
Established Heilongjiang Weiquan Dairy Products Co. equity joint venture to produce fresh and powdered milk. (Taiwan:70%-PRC:30%). $9.2 million. 7/95.

OTHER

Franx Supreme Restaurants, a division of Golden Sky Ventures International Inc. (Canada)
Opened Wonton Noodle House restaurant in Guangzhou. 7/95.

Foreign Assistance

United Nations Children's Fund
Will provide $20 million per year for the next five years to enhance childhood immunization and education programs. 9/95.

Government of Sweden
Will provide $70 million loan and $5 million grant to fund training and participation for 19 projects in China, including telecommunications, construction, and metallurgy. $75 million. 7/95.

NA (Taiwan)
Donated $400,000 in medicine and other relief for flood victims. 7/95.

World Bank/China National Salt Industry Corp. (Beijing)
Approved $27 million loan for iodized salt production to help eradicate iodine deficiency disorders in China. 7/95.

Machinery and Machine Tools

CHINA'S IMPORTS

Mitsubishi Heavy Industries Ltd. (Japan)/Shanghai Theater Co.
Sold machinery and computer systems for stage equipment. 7/95.

INVESTMENTS IN CHINA

Kobe Steel (Japan), Shinsho Corp. (Japan)/Yiyang Rubber Machinery Co. (Hunan)
Established joint venture to produce tire presses. (Japan:35%-PRC:65%). $2.1 million. 8/95.

Komatsu Ltd. (Japan), Marubeni Corp. (Japan), Teijin Seiki Co. Ltd. (Japan)/NA (Jiangsu)
Formed Komatsu Changlin Foundry Corp. joint venture in Changzhou, Jiangsu Province to produce construction and forestry machinery. (Japan:65%-PRC:35%). $21 million. 8/95.

NSK Ltd. (Japan), Nichimen Corp. (Japan)/Guizhou Hongshan Bearing General Corp.
Established Kunshan NSK Hongshan Co. Ltd. joint venture to produce ball bearings for appliances and machinery. (Japan:90%-PRC:10%). $45 million. 7/95.

Metals, Minerals, and Mining

CHINA'S IMPORTS

Long-Airdox Co., a subsidiary of Marmon Group (US)/Huaneng Coal Corp. (NA)
Sold mining equipment to develop the Shenfu-Dongsheng coal field in Inner Mongolia. $6.3 billion. 7/95.

INVESTMENTS IN CHINA

Sumitomo Electric Industries Ltd. (Japan)/NA (Guangdong)
Established Zhongshan Sumiden Hybrid Products Co. Ltd. joint venture to produce aluminum for rice cookers and cooking stoves. (Japan:95%-PRC:5%). $4.5 million. 8/95.

China Strategic Holdings (HK), MRI Co. (Australia)/NA (Beijing)
Established joint venture to upgrade China's major coal mines. $200 million. 7/95.

Kaiser Aluminum & Chemical Corp., a subsidiary of Maxxam Inc. (US)/China National Nonferrous Metals Industry Association (Beijing)
Formed Yellow River Aluminum Industry Co. joint venture to smelt aluminum in Gansu Province. (US:49%-PRC:51%). $60 million. 7/95.

OTHER

Industrial Bank of Japan, Sakura Bank Ltd. (Japan), Dai-Ichi Kangyo Bank (Japan), Sanwa Bank (Japan)
Provided $20 million loan to China International Iron and Steel Investment Co. to help finance modernization of China's steel industry. 7/95.

Packaging, Pulp, and Paper

INVESTMENTS IN CHINA

Sinocan Holdings Co. (HK)/Shanghai CFC Development Co.
Established Shanghai Sinocan Lianxing Metal Containers and Printing Co. joint venture to produce two- and three-piece cans for the domestic beverage, food, and chemicals industries. (HK:90%-PRC:10%). $15.5 million. 7/95.

Petroleum, Natural Gas, and Related Equipment

INVESTMENTS IN CHINA

Linde AG (Germany)/China Petroleum Technology and Development Corp. (NA)
Formed venture to build plant at Tazhong 4 Oil Field in Xinjiang Autonomous Region to process liquefied natural gas used to generate electricity and produce chemical fertilizer. $8.9 million. 9/95.

Nissho Iwai Corp. (Japan), Petronas (Malaysia)/NA (Jiangsu)
Formed Zhonghai Petronas NIC Oil and Gas Co. Ltd. joint venture in Jiangsu Province to market and distribute liquefied petroleum gas. (Japan:15%, Malaysia:20%-PRC:65%). $13.4 million. 8/95.

Asian Infrastructure Development Co. (US)/Jinzhou Petrochemical Co. (Liaoning)
Established joint venture to produce oil byproducts. (US:50%-PRC:50%). $120 million. 7/95.

OTHER

Chevron Corp. (US)/CNOOC
Will jointly explore for oil in the South China Sea for a two-year period. 8/95.

Honeywell Inc. (US)/SINOPEC
Agreed to be sole supplier of advanced automation controls for SINOPEC oil refineries. $75 million. 8/95.

Royal Dutch/Shell Group (Netherlands)
Will move its regional office headquarters to Beijing by 1997. 7/95.

Pharmaceuticals

INVESTMENTS IN CHINA

Becton Dickinson and Co. (US)/Suzhou Pharmaceutical Group Co. (Jiangsu)
Established joint venture to produce health care and medical products. $25 million. 8/95.

Allergan, Inc. (US)/NA (Zhejiang)
Will establish joint venture in Hangzhou, Zhejiang Province to produce eye medicine. $27 million. 7/95.

Bayer AG (Germany)/Beijing Economic Technological Investment and Development Corp.
Established Bayer Healthcare Co. Ltd. joint venture to produce health care products. (Germany:95%-PRC:5%). $16.9 million. 7/95.

ICN Pharmaceuticals, Inc. (US)/Tuobin Chemicals & Pharmaceuticals General Corp. (Guangdong)
Will form joint venture to manufacture pharmaceuticals. (US:75%-PRC:25%). 7/95.

Ports and Shipping

CHINA'S IMPORTS

Tai Chong Cheang Steamship Co. Ltd. (HK)
Will build 73,000 dwt Panamax ship for Jiangnan Shipyard in Beijing. 8/95.

INVESTMENTS IN CHINA

GATX Terminals PTE Ltd., a division of GATX Corp. (US)/SINOCHEM, Shandong Import & Export Corp.
Established Lanshan GATX Terminals Co. Ltd. joint venture to store and transport petroleum and chemical products. (US:60%-PRC:40%). 8/95.

Asian Infrastructure Development Co. (US)/Jinzhou Harbor (Group) Co. (Liaoning)
Will jointly develop Jinzhou Port and related facilities. (US:50%-PRC:50%). $700 million. 7/95.

Hutchison Delta Ports, a unit of Hutchison Whampoa Ltd. (HK)/Jiangmen Shipping Co. (Guangdong)
Formed joint venture at Gaosha Port to operate cargo terminals. 7/95.

OTHER

DHL Worldwide Express (US)/SINOTRANS
Will open training center and 26 DHL drop-off offices in Ningbo, Chengdu, Nanjing, Fuzhou, Xian, and Shijiazhuang. 7/95.

Nisshin Transport Co., a subsidiary of Hitachi Transport System Ltd. (Japan)
Will provide long-distance shipping services for Japanese companies based in Liaoning Province. 7/95.

Power Generation Equipment

INVESTMENTS IN CHINA

CGC (France)/NA (Jiangsu)
Formed joint venture thermal power plant in Jiangsu Province. $28.7 million. 8/95.

American Community Energy Alternatives Inc. (US)/State Development Investment Corp. (Beijing), Gansu Electric Power Construction Investment & Development Co., Gansu Electric Power Corp.
Established Jinguan No. 2 Power Plant joint venture to add two Chinese-built 300,000KW generators to existing plant. (US:30%-PRC:70%). $302 million. 7/95.

Mitsubishi Electric Corp. (Japan)/Xian High Voltage Apparatus Works, a unit of China Xian Electric Group (Shaanxi)
Established Xi Ling Electric Power Products Manufacturing joint venture to produce electric-generation machinery and established Xidian Mitsubishi Electric Transmission & Distribution Products Development joint venture to market, distribute, and sell the joint venture's products. $1 million. 7/95.

Toshiba Corp. (Japan), Mitsui Co. Ltd. (Japan)/Changzhou Transformer Works (Jiangsu)
Formed Changzhou Toshiba Transformer Co. Ltd. joint venture to produce extra-high voltage transformers for power transmission systems. (Japan:61%-PRC:39%). $18 million. 7/95.

OTHER

World Bank
Will provide $400 million loan for the Ertan II hydroelectric power project. 8/95.

Property Management and Development

INVESTMENTS IN CHINA

Chicago Airport Group (US)/Hainan Airport Co.
Established joint venture to build and manage Meilan Airport in Haikou, Hainan Province. (US:49%-PRC:51%). $450 million. 8/95.

First Pacific Davies Ltd. (HK)/China Shanghai Foreign Trade Center
Established property services joint venture to manage the Jin Mao Building. 8/95.

Global Development Management Corp. (US)/Beijing Vantone Industry Co. Ltd.
Formed Beijing Vantone Commercial Management Co. Ltd. joint venture to manage Vantone New World Plaza shopping center. (US:30%-PRC:70%). $1 million. 8/95.

Obayashi Corp. (Japan), Camprenon Bernard SGE (France), Chevalier Development International Ltd. (HK)/Shanghai Construction Engineering Group
Will jointly construct the Jin Mao Building. $440 million. 8/95.

Safari World (Thailand)/Changping Tourism Administration (Beijing)
Established joint venture to build and operate Great Wall Wonderland theme park in Beijing. (Thailand:90%-PRC:10%). $16.1 million. 8/95.

Yaohan International Holdings (Japan), East Light Investment Corp. (Singapore), International Merchandise Mart (Singapore)/Shanghai Nanfang Market
Established Shanghai Yaohan Nanfang Market joint venture to manage 77,600 sq m store and wholesale distribution center in Shanghai's Minhang district. (Japan:40%, Singapore:30%-PRC:30%). $70 million. 8/95.

Sogo Co. (HK)/Beijing Junefield Real Estate Development Co.
Will jointly build China's largest department store in Beijing. (HK:49%-PRC:51%). $60 million. 7/95.

Telecommunications

CHINA'S IMPORTS

ADC Telecommunications Inc. (US)/Hunan Posts and Telecommunications Administration
Sold digital transmission systems to upgrade Hunan Province's cable television equipment. $14 million. 8/95.

Martin Marietta Overseas Corp., a subsidiary of Lockheed Martin Corp. (US)
Awarded contract to build ChinaStar-1 A2100 advanced communications satellite for China Orient Telecom Satellite Co. Ltd. $100 million. 8/95.

Scientific-Atlanta Inc. (US)/MOFTEC
Will sell satellite equipment to upgrade information exchanges with companies. $10 million. 8/95.

IBM Corp. (US)
Will supply ATM digital telecommunications network for use by China National Cereals, Oils and Foodstuffs Import & Export Corp. $2 million. 7/95.

Northern Telecom (Canada)/Shanghai Posts and Telecommunications Administration
Sold three DMS-STP systems to speed construction of CCS7 voice and data network. 7/95.

Siemens AG (Germany)/Nanfang Transmission Systems Co., Ltd. (NA), MPT
Will jointly supply synchronized digital hierarchy (SDH) equipment to expand service between Shanghai and Guangzhou. $14 million. 7/95.

INVESTMENTS IN CHINA

Ameritech China Co., a subsidiary of Ameritech Corp. (US)/Zhonghua Telecom System Co. (Beijing)
Established Beijing Huamei Tech Telecom Engineering Co. joint venture to build a telecommunications network and establish exchange office in Taiyuan, Shanxi Province. $20 million. 8/95.

Ameritech Corp. (US)/China Communications System Co. Ltd. (NA)
Established joint venture to provide both cellular telephone systems and conventional telephone lines in Shanxi Province. 8/95.

AT&T (US)/Hisense Electronic Corp., a unit of Qingdao Electronics Instrumentation Industrial Co. (Shandong), Shandong Posts and Telecommunications Administration, Qingdao Posts and Telecommunications Bureau (Shandong), CITIC, China Electronics Corp. (Beijing)
Established AT&T Qingdao Telecommunications Systems, Ltd. joint venture to design, develop, market, and produce the 5ESS switching system. $100 million. 8/95.

Datacraft Asia (HK), Network Equipment Technologies Inc. (US)/Shaanxi Posts and Telecommunications Administration
Will build digital data network and establish network support office in Xian, Shaanxi Province. $2.5 million. 8/95.

IBM Corp. (US)/Shanghai Posts and Telecommunications Administration
Will jointly build telecommunications network using IBM's broadbelt switchboard and other components. $21 million. 8/95.

NEC Corp. (Japan)/Benxi Communications and Electrical Appliance Industry Corp. (Liaoning)
Established Benxi NEC Communications Co. joint venture to produce telecommunications lines and exchanges. (Japan:40%-PRC:60%). $4.2 million. 8/95.

Alcatel Alsthom Compagnie Générale d'Electricité (France)/Beijing Telecommunications Administration
Will build 1000AX experimental multimedia and high-speed data transmission communications network. 7/95.

OTHER

AT&T Microelectronics, a division of AT&T (US)
Established microelectronics business office in Shanghai to provide technical support to Chinese partner companies. 8/95.

Société Générale (France)/People's Construction Bank of China
Will supply $27 million loan to support Wuhan Posts and Telecommunications Bureau purchase of Alcatel 1000E 10 switching equipment in Hubei Province. 7/95.

Telefon AB LM Ericson (Sweden)/Shandong Posts and Telecommunications Administration
Will deliver and install GSM mobile phone systems throughout Shandong Province. $17 million. 7/95.

Textiles and Apparel

INVESTMENTS IN CHINA

Asahi Chemical Industry Co. (Japan), Itochu Corp. (Japan), Wacoal Corp. (Japan)/NA (Zhejiang)
Formed joint venture to process polyurethane thread. $8.2 million. 8/95.

E.I. du Pont de Nemours & Co. (US)/China Worldbest Development Co. (Shanghai), Huayuan Industrial Co. (Shanghai)
Established Du Pont Fiber (China) Co. joint venture to produce spandex fiber. (US:90%-PRC:10%). $90 million. 7/95.

Toray Industries, Inc. (Japan), Itochu Corp. (Japan), Toray Industries Hong Kong, Inc. (HK), Hexa Chemical Corp. (Japan)
Established LIBI Plastic Compounding Co. wholly foreign-owned enterprise in Shenzhen to manufacture plastic compounds. (Japan:95%, HK:5%). $11 million. 7/95.

Transportation

CHINA'S IMPORTS

Airbus Industrie (France)/China Eastern Airlines (Shanghai)
Sold five A340 long-distance airplanes. 7/95.

INVESTMENTS IN CHINA

Ford Motor Co. (US)
Purchased 40 percent share in Jiangling Motor Corp., a manufacturer of trucks, vans, and minibuses in Jiangxi Province. $40 million. 8/95.

Itochu Corp. (Japan)/Beijing Light Automobile
Will jointly expand production of trucks and automobiles at Beijing Light Automobile Co. (Japan:20%-PRC:80%). $19.3 million. 8/95.

Kymco Co. (Taiwan)/Summit Motor Co. (Tibet)
Established Summit-Kymco Motors Co. in Lhasa, Tibet Autonomous Region to produce motor engines. (Taiwan:50%-PRC:50%). $48 million. 8/95.

Mitsui Mining and Smelting Co. Ltd., an affiliate of Mitsui Co., Ltd. (Japan)/Chinese General Aeronautics Co. (NA)
Will establish joint venture in Guiyang, Guizhou Province to produce automobile parts. (Japan:60%-PRC:40%). $2.7 million. 8/95.

MP International Corp. (US)/First Automotive Works (Jilin)
Established joint venture to produce lead and zinc die castings for automobiles. (US:80%-PRC:20%). $14 million. 8/95.

Robert Bosch Corp. Ltd. (Germany)/Zhonglian Automobile Electronics Corp. Ltd. (Shanghai)
Formed joint venture to produce controlling systems for automobile engines. $320 million. 8/95.

Siemens AG (Germany)/Dongfeng Motor Corp. (Shanghai)
Established Shanghai Siemens Automobile Motor Co. in Pudong to manufacture automobile motors. $14 million. 8/95.

Yamaha Motor Co., Ltd., a subsidiary of Yamaha Corp. (Japan)/China National South Aeroengine Co. (Hunan), Xiangling Machinery Factory of Aviation Industry (Hunan)
Established joint venture in Zhuzhou, Hunan Province to produce motorcycle shock absorbers. (Japan:50%-PRC:50%). $9.98 million. 8/95.

Airbus Industrie (France)/China Aviation Supplies Corp. (Beijing)
Formed joint venture to establish training and service center at Beijing Capital Airport. $50 million. 7/95.

Coslink Pd (Singapore), Air Express International PTE (HK)/Shanghai United International Air Freight Co., Beijing International Ocean Freight Forwarding Co.
Established joint venture in Shanghai to handle international air transport, storage, and transfer services. $1.4 million. 7/95.

DAF Trucks NV (Netherlands)/MPT
Established joint venture in Guangdong Province to assemble postal delivery vans. 7/95.

Daimler-Benz AG (Germany)/Nanfang South China Motor Corp. (Guangdong)
Established joint ventures in Hainan and Guangdong provinces to build mini-vans. (Germany:45%-PRC:55%). $1 billion. 7/95.

Daimler-Benz AG (Germany)/Yangzhou Motor Coach Manufacturing Co. (Jiangsu)
Established joint venture to produce touring coaches and bus undercarriages. $50 million. 7/95.

Ford Motor Co. (US)/First Automotive Works (Jilin)
Established First Automotive Works-Ford United Aluminum Radiator Co. Ltd. in Changchun, Jilin Province to produce radiators for Volkswagen and Audi cars produced in Shanghai by First Automotive Works. (US:50%-PRC:50%). $22.2 million. 7/95.

ITT Automobile Industry Co., a division of ITT Corp. (US)/Shanghai Automotive Industry Corp.
Formed joint venture to produce advanced braking parts for automobiles. $25 million. 7/95.

Kia Motors Corp. (S. Korea), Kia Service Co. (S. Korea)/NA (Jilin)
Will establish joint venture in Yanchi, Jilin Province to sell spare automobile parts. $2.6 million. 7/95.

Kumho & Co. (S. Korea)/Nanjing Tire Works (Jiangsu)
Will establish joint venture to produce tires. $120 million. 7/95.

Mitsui Co. Ltd. (Japan)/Huayang Electrical Engineering Plant, a unit of Guizhou Aviation Industry Group
Formed Mitsui-Huayang Automobile Parts Co. Ltd. in Guiyang, Guizhou Province to produce car locks and other automobile parts. (Japan:60%-PRC:40%). $4.5 million. 7/95.

Nissan Diesel, an affiliate of Nissan Motor Co. (Japan), Sumitomo Corp. (Japan), Tan Chong Group (Malaysia)/ Dongfeng Motor Corp. (Shanghai)
Established joint venture in Hangzhou, Zhejiang Province to produce buses, trucks, and automobile parts. $34.3 million. 7/95.

Philips Electronics NV (Netherlands)/Hubei Automotive Bulbs Factory
Established joint venture to produce lighting fixtures for automobiles and motorcycles. (Netherlands:70%-PRC:30%). $29.8 million. 7/95.

Porsche AG (Germany)/Zhongyuan Internal Combustion Engine Plant (Henan)
Established joint venture to produce automobile engines. (Germany:40%-PRC:60%). $72 million. 7/95.

Rolls-Royce PLC (UK)/CAAC
Will establish joint venture to produce components for Rolls-Royce engines. 7/95.

SAIAG Joint-Stock Corp. (Italy)/Shanghai Automobile Industrial Corp., Shanghai Yongying Industrial Corp.
Formed joint venture to produce rubber sealing elements for Volkswagen and other cars. (Italy:30%-PRC:70%). $36 million. 7/95.

Sikorsky Aircraft Corp., a subsidiary of United Technologies Corp. (US), Embraer Corp. (Brazil), Mitsubishi Heavy Industries Ltd. (Japan), Gameas Corp. (Spain), Taiwan Aerospace/Jingdezhen Helicopter Group (Jiangxi)
Will jointly manufacture S-92 Helibus helicopters for civilian use. 7/95.

OTHER

The Boeing Co. (US)/China Civil Aviation College (Sichuan)
Donated two Boeing-737 flight simulators for aircrew training. $36 million. 7/95.

Rolls-Royce PLC (UK)
Established wholly owned subsidiary investment company. $30 million. 7/95.

Miscellaneous

INVESTMENTS IN CHINA

Mitsubishi Corp. (Japan), Li and Fung Ltd. (HK), LG Group (S. Korea)/NA (Guangdong)
Will establish Lifung Distribution Centers Ltd. in Guangzhou. $120 million. 8/95.

OTHER

American Express Co. (US)/China International Travel Service (Beijing)
Opened American Express Business Travel Center in Beijing to sell airline and rail tickets, and book tours. 7/95.

Simmons & Simmons Law Offices (UK)
Granted license to open office in Shanghai. 7/95.

City of Osaka (Japan)
Will establish "Business Partner Cities" relationship with Shanghai. 7/95.

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