THE CHINA BUSINESS REVIEW

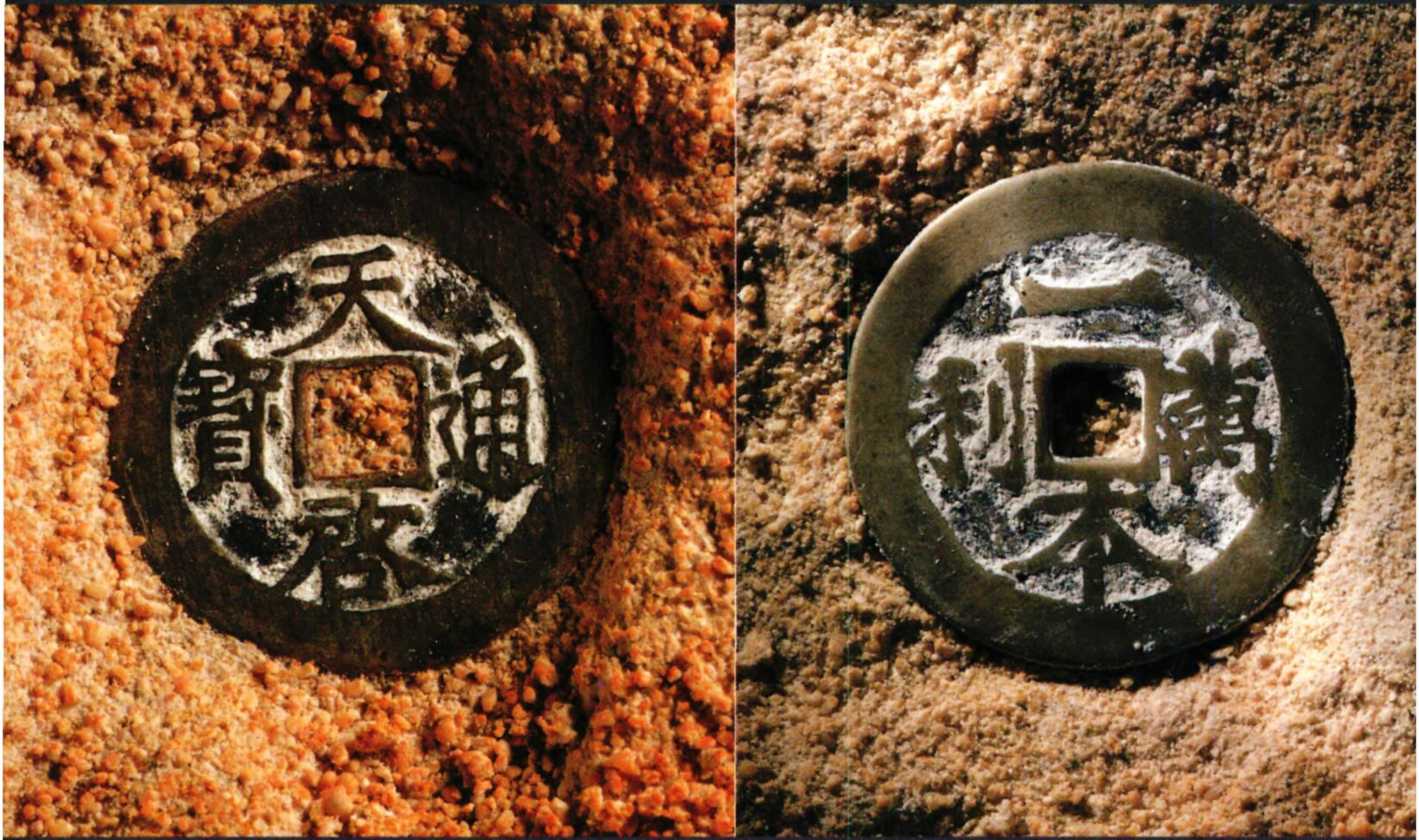
NOVEMBER-DECEMBER 1996 VOLUME 23 NUMBER 6

CHINA in the Electronics Age

IN THIS ISSUE:

- *China tackles the Internet*
- *A look at China's legislative process*
- *Hotel chains move inland*
- *Christmas in Beijing*

How can you value opportunities in China if you can't identify these coins?



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CONTENTS

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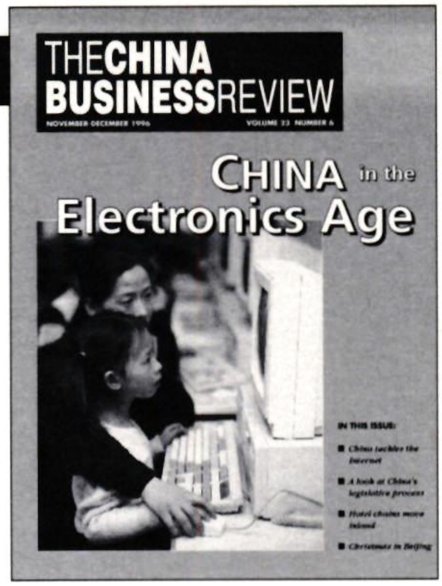

November-December 1996

FOCUS: China in the Electronics Age

FEATURES

DEPARTMENTS

Cover photo by Max Vision.

Sparks Fly Over Diaoyu Issue

Situated about 118 miles northeast of Taiwan and long a subject of disputed sovereignty, the Diaoyu Islands—or Senkaku Islands to the Japanese—once again have become a focal point for pan-Chinese nationalist sentiment. Ceded to Japan in 1895 during China's Qing dynasty, the islands remained a US protectorate after World War II until 1972, when Washington returned them, along with Okinawa, to Japan. Large-scale protests erupted in Hong Kong at that time, and both the PRC and Taiwan claimed sovereignty over the islands. The issue was effectively shelved until this summer, however.

In July, the right-wing Japan Youth Federation built a makeshift lighthouse and planted the Japanese flag on the otherwise uninhabited islands, which provide rich fishing grounds for Taiwan and Japanese fishermen. The Japanese government also included the islands, rumored to possess oil and gas reserves, in Japan's 200-mile exclusive economic zone. Together, these moves over the summer provoked a strong response throughout Greater China, uniting various Hong Kong political factions and creating links between pro-China camps in the territory and various groups in Taiwan.

Since the initial furor, both Taiwan and Hong Kong have seen frequent nationalist demonstrations, flag burnings, boycotts of Japanese goods, and calls for armed intervention. The atmosphere deteriorated further after the September 26 drowning of David Chan Yuk-cheung, the Hong Kong Chinese leader of the Alliance of Worldwide Chinese for the Protection of the Diaoyu Islands. When the Japanese coast guard prohibited their attempts to land on the islands, Chan and four others jumped overboard from their chartered boat, ostensibly to show the Japanese that Chinese could do whatever they wanted in their own waters. Subsequently, in an October 10 article in *China Daily*, Beijing warned Japan that it was provoking a confrontation, while ongoing protests prompted Hong Kong Governor Chris Patten to declare that continuation of such actions could hurt Hong Kong's image.

Mainland authorities also became concerned that the focus of such outpourings of emotion could easily switch to domestic issues. Thus, Chinese universities and local governments have been instructed to prohibit any gatherings, posters, or on-line bulletin boards or websites devoted to the Diaoyu dispute. Ironically, Beijing is finding the ultra-nationalist rhetoric it has fired at Hong Kong and Taiwan over the past year difficult to control. Residents of both Taiwan and Hong Kong have been far more emotional and combative over the issue than either the PRC, Hong Kong, or Taiwan governments, all of which have urged restraint and a diplomatic solution to the issue. Tokyo, also hamstrung by domestic politics, has neither criticized nor explicitly supported the activities of Japanese nationalists, though Japanese Prime Minister Ryutaro Hashimoto did reassert Japanese sovereignty over the islands on several occasions in September and October. None of the governments appears to seek a confrontation over the Diaoyu issue, but all fear that criticism from grassroots elements or a real clash between protesters and the Japanese coast guard could cause tensions to escalate.

—*TLK*

Four More Top Internet Sites

China watchers looking for the latest China-related Internet news may find the following websites useful:

http://www.chinabooks.com/—*China Books and Periodicals, Inc.*'s website is an excellent source of information on books and magazines from China. The company's 1996 catalogue, best-selling books, and new titles all are online, but the bookseller does not yet sell its books electronically.

http://www.asianenviro.com/—*The Asia Environmental Review*'s website offers a quick education on Asian environmental affairs, including a valuable list of other Asian environment-related websites. Browsers also can download one free back issue of this monthly publication and order subscriptions electronically.

http://itl.irv.uit.no/trade_law/—Ralph Amissah, a member of the law faculty at Norway's University of Tromso, has created an outstanding source of international trade law data. This website offers a subject index and search engine, with myriad topics ranging from dispute resolution to protection of intellectual property, as well as keyword search capability. In addition, this website is a superb hub for other trade- and law-related Internet addresses.

http://www.ustr.gov/—The *United States Trade Representative (USTR)*, like many other government agencies and departments, has its own website. Those in need of texts from USTR will find them here, along with press releases, and trade agreements—including the GATT/WTO Agreement.

—*TLK*

Flipper Reigns in Hong Kong

The Preparatory Committee celebration subgroup has selected the white dolphin to be the mascot for celebratory activities related to Hong Kong's transfer to Chinese sovereignty next July. The group apparently selected the wide-eyed, smiling dolphin because of its cheerful look.

1997 Holidays in Hong Kong and China

Businesspeople beginning to schedule meetings with Chinese government officials in the upcoming year should take note of the official holiday schedules. Government offices in Hong Kong and China will be closed on the following days in 1997:

Hong Kong

New Year's Day	January 1
Lunar New Year	February 6-8
Good Friday	March 28, 29
Easter Monday	March 31
Ching Ming Festival	April 5
Tuen Ng Festival	June 9
The Birthday of Her Majesty the Queen	June 28, June 30
Hong Kong SAR Establishment Day	July 1, 2
Sino-Japanese War Victory Day	August 18
Mid-Autumn Festival	September 17
National Day	October 1, 2
Chung Yeung Festival	October 10
Christmas	December 25, 26

China

New Year's Day	January 1
Lunar New Year	February 7-9
International Labor Day	May 1
National Day	October 1, 2

SHORT TAKES

Beijing Bans Smoking

China's capital city banned smoking in public places—including buses, trains, and public halls—earlier this year. The fine for violating the ban, at only ¥10 ($1.20), is unlikely to deter smokers, especially those who spend up to ¥50 ($6) on the more expensive domestic and foreign cigarette brands. Enforcement has been weak to date; few Beijingers have been slapped with fines for violating the ban.

Asia's Sugar Daddy

China, India, and Thailand are fast becoming major players in the global sugar market. Thailand, for example, ranks third in exports of raw and refined cane sugar after Australia and Brazil. But it has been the somewhat erratic trading patterns by China and India that have shifted the direction of the market in recent years, according to a recent report by Rabobank Nederland. China may produce 5 percent of global sugar exports one year but buy up 12 percent of global sugar production the next, switching from net importer to net exporter with some frequency. China will continue to require imported sugar until it is able to increase domestic production by an estimated 3.7 million tons, a target Beijing expects to meet by the turn of the century. And China clearly has a sweet tooth—in addition to its demand for sugar, China is the largest consumer and producer of saccharin.

Guangdong Goes Green

The effects of rapid economic development and high population growth over the past two decades have issued a wake-up call to the Guangdong provincial government. The province intends to spend over $1.7 billion over the next five years on projects aimed at protecting the ecology of the Pearl River delta. And the Guangdong People's Congress may soon follow suit by drafting environmentally friendly legislation, including a directive for local authorities to establish special funds to protect the environment.

THE CHINA BUSINESS REVIEW

The magazine of the US-China Business Council

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ISSN No. 0163-7169; USPS No. 320-050

Annual Subscription rates: $99 US/Canada; $150 international. Single copy issues: $20, airmail $25; issues over 1 yr: $10, airmail $12.50. DC residents add 5.75% sales tax.

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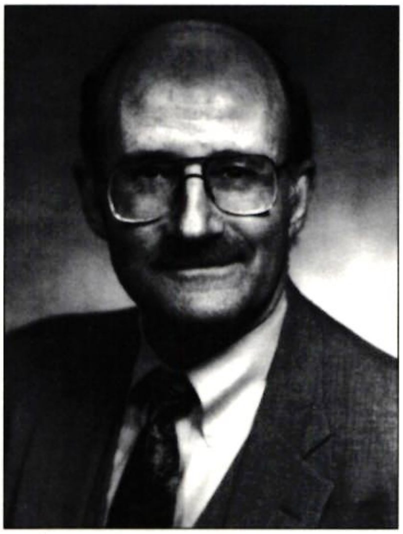

Robert A. Kapp

Talking Tough

It's time to put Beijing's fiery nationalist rhetoric in a historical context

The current tide of assertive nationalism emanating from China has caught the world's attention, and cannot have escaped the attention of American companies as they think long-term about China.

Twenty-five years after the initial Nixon-Mao breakthrough, twenty years after the end of the regime of the Gang of Four with its strident xenophobic rhetoric, and nearly twenty years into China's headlong plunge into global economic and political affairs, the world witnesses a colorful outburst of publications and statements proclaiming the dangers of contamination of "cultural garbage from the West," and the perils inherent in foreign (especially American) efforts to contain or block China's economic and political progress. The implication that China's security, both military and cultural, is challenged by outside forces is far more evident today than it was in the early years of the economic reform program.

This trend occurs simultaneously with Chinese authorities' return to an emphasis on the inculcation of political and social values drawn from the classical canon of Marx, Lenin, Mao, and Deng Xiaoping. What are American businesspeople to make of this, and what does it augur for the future of China's economic relations with the United States? And what, if anything, should US businesses—individually or collectively—do about it? Here are a few ideas:

■ Recognize that the elements of China's political and economic discourse we see today—concern over cultural contamination, fear of excessive foreign participation in the Chinese economy, the desire to protect domestic markets and industries from foreign competition, and the harsh rhetoric directed at perceived international malefactors—all form one dimension of a Chinese domestic dialogue that began in the 1850s and will continue long into the future.

■ Remember that, despite the striking staying power of the themes that are now so conspicuous in Chinese political rhetoric, the China of the 21st century is not the China of the 19th or even of most of the 20th century. Just as China is a far more significant factor in world power relations today than it has been at any time in the entire lifetime of the United States, it is far more enmeshed in the global system—of finance, science and technology, and even geopolitics—than it has ever been before. The realities of China's economic challenges simply require further progress in coming to amicable terms with the workings of global economic systems.

■ Take note that growing self-confidence on the part of American companies' Chinese counterparts is natural as China's economic strength increases. Obstructionism and diminishing cooperation with US and other foreign partners, if driven by fear of political harm at home, would be more worrisome. The current wave of nationalistic rhetoric and re-emphasis on strengthening the structures of State power may be tough on foreign ears, but do not remotely resemble the old-style campaigns against cooperation with foreigners. Any signs of the recurrence of that tragic syndrome would be cause for concern.

■ Understand, and help others to understand, that the playing out of domestic dramas in today's world has an impact offshore. The Japanese parliamentary leader who, several years ago in a provincial political speech, pronounced American workers "lazy and illiterate" was reportedly surprised at the furor that erupted in the United States; after all, he was speaking in Japanese to a Japanese audience! The smashing of a Japanese radio by a member of Congress on the steps of the US Capitol had a far deeper impact in Japan than it did in the United States, where political memories are short and electoral defeats quickly turn histrionics into ancient history. But no matter how domestically directed, China's tough talk regarding the United States inevitably has an effect on popular and political perceptions in this country.

We approach 1997 with a complex set of prospects: step-by-step improvement of communication and cooperation at the highest levels between the US and Chinese governments, but rising levels of nationalistic and US-focused political rhetoric within China; real opportunities for substantive negotiation and even agreement between China and major trading regimes over terms for Chinese accession to the World Trade Organization (WTO), but conflicting evidence on China's progress in the direction of fundamental WTO compatibility; and clear awareness in the US Congress that the dispiriting and dysfunctional annual MFN process has outlived its usefulness, but continued congressional susceptibility to external shocks over US-China relations, for example, as relates to Hong Kong.

The eminent historian of US-China relations, Michael H. Hunt, has done us a service with his recent book, *The Genesis of Chinese Communist Foreign Policy* (Columbia University Press, 1996), by putting in historical context many of the orientations and ideas that Americans in all walks of life perceive in China today. Reviewing the catastrophes that overtook the Qing (Manchu) dynasty in the 19th century and the ultimate failure of the Qing statesmen either to play one aggressive foreign nation off against another or (as in the case of the disastrous Boxer Rebellion of 1900) to simply sweep the foreigners out of China altogether, Hunt concludes:

"*The failures of the late Qing carried two powerful lessons for politically engaged Chinese in the twentieth century. First, they concluded that hopes for an advantageous and secure if not peaceful relationship with the Powers depended on the vitality of the state... None doubted that only with the state back in command, its power and legitimacy restored, could China emerge as a purposeful and secure international actor... Second, politically engaged Chinese looking back at the Qing record saw a compelling indictment of foreign behavior. When Qing officials sought strategic partners, particularly on the dynamic maritime frontier, foreign diplomats seldom responded as desired—with the result that sponsors of cooperation found themselves vulnerable to criticism and their policy displaced by other, more antagonistic approaches... The disasters that had shaken the Chinese state, imperiled the empire, and divided officialdom thus raised fundamental questions—about China's heritage and its future, its political and social system, and its relationship to the outside world. These questions were to echo in Chinese politics long after the empire had been reconstituted and the structural crisis reversed.*" (pp.49-50)

Hunt's insights are correct, and should provide, if not complete reassurance, at least a certain sense of continuity as we in the business community both watch and participate in China's monumental effort to transform itself while preserving its essential institutions and values. 完

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FOCUS

From Cold to Hot

China struggles to protect—and develop—a world-class electronics industry

Denis Fred Simon

The unprecedented sustained growth of the worldwide semiconductor industry is shaking up long-held expectations that boom-and-bust cycles could continue in this sector. Though world sales growth is not expected to surpass the 40 percent rate of 1995, industry analysts predict 1996 will be the fourth consecutive year of 20+ percent growth in the semiconductor industry. Strategic planning in the industry is changing to reflect what experts believe to be this new reality of smoothed margins.

Two trends account for the move away from the roller-coaster pattern of recent years. First, new personal computer (PC) software such as Windows 95 requires more memory, and thus more chips, than analysts had predicted. Second, semiconductor chips, the building blocks of modern electronics, are now in demand for much more than PC production. The rapid advent of advanced telecommunications, networking technologies, and consumer electronics—all of which require chips—allows the semiconductor industry to weather traditional market fluctuations.

As rival semiconductor companies start to discern the correlation between capital spending and market share, they are beginning to ante up huge sums to build wafer fabrication factories (fabs) around the globe. East Asian companies, in particular, are competing to redistribute the chip production percentages in their favor. According to press reports, US and Japanese firms together accounted for 80 percent of world semiconductor production in 1995, while Asian producers (excluding Japan) claimed 12.1 percent of the world market—up from 8.9 percent in 1994. As South Korean, Taiwan, and Singapore companies jockey for position, China has no wish to be left behind.

Indeed, Beijing would like Chinese firms to become major players in the global electronics industry. The PRC leadership's desire to develop a modern electronics industry crystallized in the aftermath of the Gulf War. Impressed, in part, by the utilization of so-called "smart weapons" by the American military, Chinese officials decided to provide more resources and give greater attention to the development of a state-of-the-art electronics sector. The informatics revolution that is occurring around the globe has further underscored to Beijing the importance of developing a modern electronics industry. The strong demand in China's domestic electronics market, which has become largely consumer-driven, is also fueling the industry. Output of several major electronic appliances increased substantially from 1994-95: production of air-conditioners was up 35.9 percent; refrigerators, 21.6 percent; freezers, 21.4 percent; color televisions, 15.9 percent; and electric fans, 15.2 percent.

Of particular interest to China's leaders—and to foreign firms—has been the growth in the microelectronics segment of

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the industry. China's semiconductor market is already expanding rapidly: by 2000, China is expected to account for 15 percent of the Asian demand for semiconductors, with projected annual semiconductor sales of over $2 billion, which would make it second only to Taiwan. Continued growth in China's PC, telecommunications, and general consumer electronics industries should help keep demand for semiconductors high.

Ambitious plans

Beijing has declared electronics a "pillar industry" in its Ninth Five-Year Plan (FYP, 1996-2000). In official rhetoric, "pillar" status paves the way for priority funding and State approval of foreign joint ventures and other forms of foreign direct investment (FDI). The Chinese government has allocated roughly ¥590 billion ($71 billion) in the 9th FYP to upgrade its overall electronics technology base. The country's strategic focus during the 1996-2000 period will be to develop advanced 0.3-micron chip technology in labs, produce 0.5-micron chips on a trial basis, and manufacture less sophisticated 0.8-micron chips on a mass production scale.

To enhance the development of specialized chips such as application-specific integrated circuits (ASICs), China plans to build one or two new integrated circuit (IC) fabs per year through the remainder of the decade. Pushing ahead in a sustained fashion with the "Golden Projects"—China's answer to the information superhighway—and creating large conglomerate firms upon which to focus that support are two tactics the government has adopted to spur the development of domestic suppliers (*see* p.10). To support all of these efforts, PRC government expenditures on overall technological modernization have risen substantially in recent years: from ¥90 billion ($10.8 billion) in 1990 to nearly ¥200 billion ($24 billion) in 1995. And annual output in China's electronics industry exploded during 1981-95, growing from ¥10 billion ($1.2 billion) to nearly ¥225 billion ($27.1 billion).

China's top leaders also are making a greater effort to bring the electronics sector firmly in line with national industrial policies. In general, Beijing has shifted away from comprehensive planning and toward implementation of industrial policies, a move that entails greater reliance on market forces while government resources and attention are targeted toward specific, priority sectors. China's 9th FYP grants priority status to FDI in several key electronics subsectors, including large-scale integrated circuits, photo-lithographic devices used in the wafer-manufacturing process, large and medium-size computers, high-end PCs, components for fax machines, advanced semiconductor materials, digital and high definition TV, liquid crystal displays, CAD/CAM/CAT/CAE (computer-aided design, manufacturing, testing, and engineering) equipment, satellite/earth station communications, air traffic control technology, laser printing, and large capacity disk storage.

> China plans to build one or two new integrated circuit fabrication plants per year through the remainder of the decade.

To encourage investment and growth in high-tech areas, China's Ministry of Electronics Industry (MEI) will continue to offer incentives to investors on a per-project basis—despite government restrictions on foreign participation in sectors such as telecommunications and services, and recent moves to phase out FDI incentives such as the duty exemption for capital equipment imports. For example, Marubeni Corp. subsidiary Marubeni Hytech Co. established a joint venture in May 1996 with Fenghong Microelectronics (Shenzhen) Co. to provide maintenance services for semiconductor factories. This joint venture appears to be an exception to the limits on certain types of foreign participation in high-tech services.

Goals vs. reality

In recent months, high-level discussions on the future of the electronics industry indicate that Beijing is attempting to formulate a strategy for the sector. The State Council reportedly is currently reviewing an electronics industrial policy. In January 1995, a National Work Conference on the Electronics Industry took place, with the goal of outlining a new policy emphasis on electronics. The January meeting was followed by a similar National Work Conference on Computers and Software in April 1995, which stressed the key role of electronics in developing a modern information industry. At an April 1996 conference in Guilin presided over by Minister Hu Qili, participants addressed the barriers to faster progress in China's electronics sector.

Indeed, all of China's ambitious electronics sector goals might not be entirely achievable. Bureaucratic squabbles and the lack of sufficient funds loom as large obstacles. Turf battles between the Ministry of Posts and Telecommunications (MPT) and MEI have slowed the scope and pace of the sector's development. MPT's previous monopoly over telecommunications-related production has diminished in recent years, as MEI-led or-

China's Integrated Circuit Market, 1990-2000

	1990	1995	1996*	2000*
VOLUME (million pieces)				
Domestic production	97	560	697	3,012
Imports	186	5,118	7,238	15,620
Exports	8	554	963	2,058
SALES ($ million)				
Domestic production	67	405	446	NA
Imports	144	1,949	2,642	NA
Exports	9	266	455	NA

SOURCE: Andersen Consulting
NOTES: * Projected NA = Projections not available

Golden Ambition

The Chinese government's "Three Golden Projects," launched in the early 1990s, aim to modernize the country's information technology (IT) infrastructure by creating an economic information and data communications network for both public and private use. The nationwide network is slated to span 500 cities, 12,000 large enterprises, and several key projects such as the Three Gorges Dam and the Daya Bay Nuclear Power Plant.

Though the Golden Projects—China's version of the information superhighway—involve coordination among more than 20 government ministries and hundreds of thousands of other organizations, they are essentially the brainchild of the Ministry of Electronics Industry (MEI). Anxious to become the major player in China's IT industry, MEI initiated the Golden Projects, establishing Jitong Corp. to spearhead project design and construction.

In addition to promoting the development of China's domestic electronic information infrastructure, the projects provide some investment opportunities for foreign companies. MEI and the Chinese government have not established any unified purchasing policies, so each project must find its own hardware and software suppliers. Companies participating in Goldens-related projects include AT&T, Compaq Computer Corp., Hewlett-Packard Co., Hitachi Ltd., IBM Corp., Intel Corp., MasterCard International, Motorola Inc., Toshiba Corp., and Visa International.

Each of the Three Goldens tackles a different aspect of the country's IT infrastructure:

■ **Golden Bridge** The national public telecommunications network, and the foundation of China's entire IT infrastructure, Jitong's Golden Bridge is designed to provide China with satellite and optical fiber cable networks for the financial, customs, foreign trade, tourism, meteorological, traffic service, State security, and other scientific and technological sectors, and is expected to be able to transmit data, documents, human voice, and pictures among networked organizations.

■ **Golden Customs** Considered a subset of the Golden Bridge project, Golden Customs is developing applied information system services to track quota permits, bank sales of foreign currency, and import and export trade statistics for China's General Administration of Customs. The project, also under Jitong's guidance, aims to link all foreign trade departments and firms in the near future and realize electronic data exchange and, eventually, paperless trading.

■ **Golden Card** The goal of this project is to use Golden Bridge telecom networks to replace cash transactions with an electronic service system for savings, withdrawals, and payments through credit and debit cards. The electronic currency system, directed by China Electronic Information Industrial Group (CEC), has already launched test operations in 12 major cities, issuing nearly 30 million cards; some 200 million credit and debit cards will be issued over the next seven years. Advanced "smart card" technologies are also being tested (*see* p.14).

Currently in various stages of implementation, the three projects have made significant progress over the last several years, and are scheduled for completion by 2003. Their success has served as an impetus for other government departments to map out their own "goldens":

• **Golden Enterprises** This production and marketing information system, backed by the State Economic and Trade Commission, is expected to link the country's 360,000 State-owned enterprises and 8.6 million other industrial and commercial firms with Chinese government offices. The project will offer online services and assist commercial and industrial firms in their efforts to make efficient use of personnel, capital, and natural resources.

• **Golden Health** The plan is designed to provide all Chinese citizens with an optical memory card containing personal health care data by the year 2002.

• **Golden Intelligence** A national science and technology information network, the Golden Intelligence project is intended for academic use.

• **Golden Macro** This project is intended to build macroeconomic tools, primarily for use by ministries and provincial-level information centers. There have been reports recently that the Golden Macro, Golden Bridge, and Golden Enterprises projects may be linked into a single unified economic information and data communication network.

• **Golden Medical** Sponsored by the Ministry of Health and Jitong, this project will create a network to connect large hospitals and research institutions, facilitating transmission of critical medical information and images among health organizations.

• **Golden Real Estate** Developed by the Ministry of Construction and local agencies, the network will allow real estate information to be exchanged across different regions of China.

• **Golden Tax** More than ¥10 billion ($1.2 billion) will be spent on this computerized tax collection system—sponsored by the Ministry of Finance, the People's Bank of China (PBOC), the State Tax Administration, and MEI—which calls for the installation of 85,000 computers at about 30,000 tax agencies around the country.

MEI's golden endeavors have also spawned several competing efforts by MPT and other organizations. The most prominent of these is the Green Card project, a network that utilizes MPT's communications web by installing PBOC transaction stations in post offices nationwide. The equivalent of an automated teller system, the network allows Green Card customers to make deposits and withdrawals regardless of proximity to a local bank branch. The Green Card project started up in seven cities in July of this year and is considered strong competition for Golden Card, given the multitude of post offices in China.

The Golden Projects should move the PRC much further down the road to modernization. The effect in China of the Golden Projects could be akin to the massive impact of the railway system built in the United States in the late 1800s.

—Denis Fred Simon and David Ashton

Denis Fred Simon and David Ashton are with Andersen Consulting's China strategy practice.

ganizations, particularly China United Telecommunications Corp. (Unicom), attempt to enter the telecommunications sector as a competing service provider (*see* p.22). This expansion of the sector beyond traditional production and service norms has blurred the lines of demarcation between the ministries' respective responsibilities, leading to conflicts between MEI and MPT. Through its key role in the various Golden Projects, MEI apparently is viewed as encroaching upon traditional MPT territory. The State Planning Commission (SPC) cannot seem to resolve the impasse, perhaps because it, too, is undergoing substantial change.

The rise of MEI

MEI, meanwhile, has been redefining its role in the last several years, and could eventually corporatize, as China's petrochemical and aerospace ministries have done. There has even been some discussion of creating a new "informatics" ministerial body that would oversee facets of the telecom, electronics, and computer sectors. For now, though, MEI's three priorities are research and development (R&D) projects requiring government assistance, projects which involve dissemination of technical expertise, and large-scale manufacturing projects. But MEI administrators face a twofold quandary: how to marshall sufficient resources to accomplish these goals; and how to utilize foreign investment without sacrificing the development of a domestic microelectronics sector.

MEI's Hu has spelled out a new plan of action designed to help the electronics industry grow from a simple manufacturing sector into a major player in China's informatics industry. Hu's vision rests on allowing the market to guide enterprise production decisions and developing domestic sources for critical technologies to avoid dependence on foreign suppliers. Nonetheless, China may have little choice but to welcome substantial foreign participation in this sector. MEI currently lacks the funds to create a modern microelectronics sector as the South Koreans did in the 1980s—there are no Chinese equivalents to Samsung Electronics Co. and Goldstar Semiconductor Ltd., companies that transformed South Korea's electronics investments into a world-class semiconductor industry.

Turf battles between MPT and MEI have slowed the scope and pace of the sector's development.

China's industrial policy for the electronics sector, meanwhile, could be released by the State Council soon. The policy apparently provides for the establishment of R&D funds for the development of new technologies. The policy has reportedly been revised several times over the past few years to eliminate components—such as localization and export requirements—that would be considered incompatible with World Trade Organization (WTO) rules.

Three drivers of growth

A closer look at China's electronics industry suggests that three major market sectors will also help shape the pace and thrust of future development: telecommunications, computers, and consumer electronics. The PRC telecommunications industry, for one, is growing even faster than the economy as a whole. The number of cellular phone users in China is expected to total 17.3 million users in 1998—a 1,000 percent increase over the 1994 level. In 1987, the number of pagers in China stood at 31,000. At year-end 1994, the number of pager subscribers reached 17.7 million, and rose to 26 million by the end of 1995. In more traditional forms of communication, China is seeking to add 70 million telephone lines by 2000, and intends to raise its current 3.2 percent telephone density to at least 10 times this level by 2020 (*see The CBR*, March-April 1996, p.8). The growth in telephones alone will spur IC demand for the next decade, as ICs are the programmable chips that drive the operation of telephones, switches, and pagers.

Not to be overshadowed by telecommunications, China's computer industry is also on the fast track. Approximately 1.1 million personal computers were sold in China in 1995, a 54 percent increase over 1994. According to press reports, by mid-1996, domestic firms in China had produced 512,000 PCs, a 123 percent increase over production during the first six months of 1995. Since 1990, computers have grown from 6 percent to 18 percent of total electronics output. Local Chinese surveys reveal large numbers of urban residents are becoming interested in purchasing a home computer. Only 1.6 percent of Chinese families reportedly own a PC, though roughly 4 per-

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Foreign-Invested Projects in the Semiconductor Sector (1995)

Company	Nationality	Product or Service	Location
Advanced Micro Devices Inc.	US	Assembly of flash memory and Programmable Logic Devices (PLDs)	Jiangsu
Advantest Corp.	Japan	Semiconductor testing and electronic measuring equipment	Shanghai
Alcatel Alsthom Compagnie Générale D'Electricité	France/Spain	Telecom integrated circuits (ICs)	Shanghai
Digital Equipment Corp.	US	Application-specific integrated circuits (ASICs)	Hunan
E.I. du Pont de Nemours & Co.	US	Photomask ICs	Shanghai
Eaton Corp.*	US	Electrical circuit protection devices	Jiangsu
Fuji Electric Co., Ltd.	Japan	Hybrid IC components	Fujian
Fujitsu Ltd.	Japan	Linear ICs and microprocessors	Jiangsu
Fujitsu	Japan	Assembly and production of software, printers, and communications and data transfer equipment	Beijing, Fujian, Jiangsu, Shenzhen
Harris Corp.	US	Complete digital microwave radio system	Heilongjiang
Harris	US	Semiconductor assembly and testing	Jiangsu
Harris	US	R&D, manufacturing, sales, and support for digital telephone switches and other telecom systems	Guangdong
Harris	US	Low- and medium-capacity digital microwave radios	Shenzhen
Hitachi Ltd.	Japan	Semiconductors	Jiangsu
Hewlett-Packard Co.	US	R&D center with State Science and Technology Commission	NA
Intel Corp.	US	386 sx chip sets assembly and testing	Jiangsu
Intel	US	Microprocessor assembly and testing	Shanghai
Kyocera Corp.*	Japan	Chip condensers	Shanghai
Lucent Technologies, Inc.	US	Telecom ICs	Shanghai
Matsushita Electric Industrial Co., Ltd.	Japan	Assembly of linear ICs and microprocessors	Shanghai
Micro Electronics	US	Multi-layer ceramic items	Jiangsu
Mitsubishi Electric Co.	Japan	Micro-controllers and ASICs assembly	Beijing
Mitsubishi/Mitsui & Co., Ltd.	Japan	ASICs for consumer electronics	Beijing
Motorola Inc.	US	Mobile telecom ICs (upgrade to 0.8 microns)	Tianjin
Motorola	US	Semiconductors	Tianjin
Motorola	US	PC production and assembly	Jiangsu
Motorola	US	R&D for advanced communications and computers	Beijing
Motorola	US	Semiconductors	Sichuan
NEC Corp.	Japan	4Mb DRAM chip assembly	NA
Philips Electronics N.V.	The Netherlands	Consumer ICs	Shanghai
Samsung Electronics Co., Ltd.	South Korea	Logic semiconductors, transistors	Jiangsu
Seiko Epson Corp.	Japan	ASICs design	Shanghai
SGS Thomson Microelectronics	Italy/France	Semiconductor assembly and testing	Shenzhen
Siemens AG	Germany	Telecom ICs	Jiangsu
Texas Instruments, Inc.	US	Design/technology center	NA
Thomson S.A.	France	ICs	Guangdong
Toshiba Corp.	Japan	Consumer ICs/TV chip sets	Jiangsu

SOURCE: Andersen Consulting, US-China Business Council files
NOTES: *1996 NA = Information not available. This list is not comprehensive.

cent are planning to buy one in the near future. In urban China, there are about 3-4 PCs per 100 households, leaving much room for potential sales. One estimate places China's PC market in 2000 at approximately 5.5 million per year. By contrast, US consumers bought 19 million PCs in 1995.

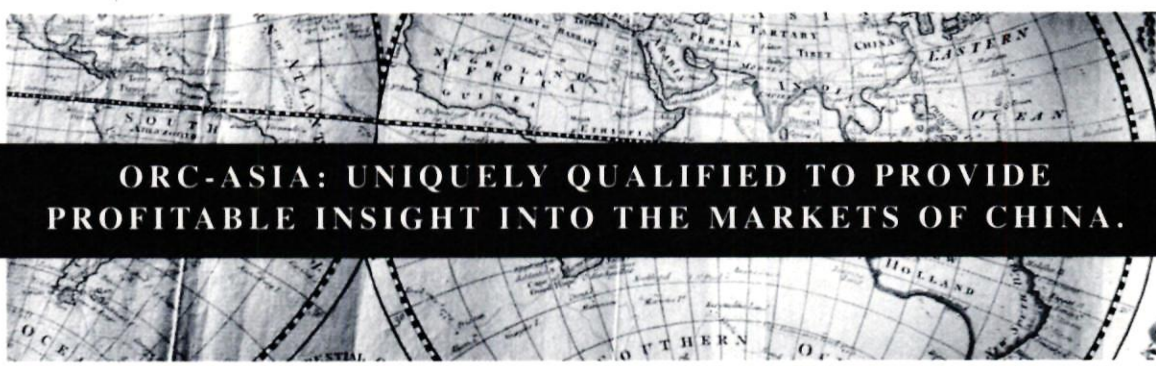
Policywise, one of China's 9th FYP goals is to expand the computer industry from its current ¥50 billion ($6 billion) in annual sales to ¥170 billion ($20.5 billion) by 2000. Specific 9th FYP goals for the computer industry include the development of massively parallel processing (MPP) computer systems, "supercomputer" systems designed to reach computing speeds of 50 billion floating-point operations per second (FLOPS). According to an MEI computer department report, "[The] speed of a single node computer will be more than 400 million FLOPS and the communication bandwidth among the node computers will be over 100 million bytes per second." Beijing intends to have one MPP system completed and in operation by year-end 1998, possibly for geological/meteorological applications.

Foreign-invested companies are responsible for over 50 percent of PRC electronics exports.

The third catalyst for PRC electronics industry growth is consumer electronics. In 1994, 22 percent of China's electronics output was in consumer goods. More than 15.6 million color television sets were produced that year. China is no exception to the worldwide trend of increased use of IC and memory chips in consumer products. From the mundane radio to the fancy color TV, advanced chips are everywhere, and China's growing middle class is demanding more whistles and bells on its consumer products. Consumer spending is growing, resulting in greater brand awareness and use of credit cards and automated teller machines (*see* p.14).

Balancing foreign firms

Providing advanced technologies throughout the industry, foreign companies have become significant players in China's electronics sector. For example, every major Japanese and Korean color television manufacturer has set up a factory in China. According to *China Daily*, about 52 percent of the PCs sold in the Chinese market in 1995 were domestically assembled, but less than 25 percent of the components for these machines were locally sourced. Foreign computer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industry companies such as Intel Corp. and Microsoft Corp. are the main developers of Chinese-language standards and software. In addition, IBM Corp. announced plans to invest $2 billion in China's computer market during the 1996-2000 period. IBM also recently provided $25 million to develop university computer centers across China—a philanthropic move that also should promote widespread use of its platform.

Just how China chooses to treat FDI in the electronics sector may have some bearing on future growth. As foreign-invested companies are responsible for over 50 percent of PRC electronics exports, MEI officials seem to worry that the more than 8,000 Sino-foreign electronics joint ventures are playing too significant a role in shaping the future of the country's electronics industry. Beijing is trying to limit certain types of foreign investment in the sector and encourage international firms to shift toward higher value-added pursuits. The PRC government recognizes that many foreign firms are merely carrying out assembly activities in China, transferring few technologies to the local economy—except perhaps in the area of management. The State Council's ban on the establishment of new Sino-foreign color television joint ventures, while allowing a select number of Japanese joint ventures to develop high-definition TV technologies in China, is a strong indication of the leadership's intention to restrict direct foreign involvement in the sector.

Smart cards are an integral component of the Golden Card project.

Given China's sensitivity to foreign involvement in infant industries, it is not surprising that the government is eager to make China's electronics sector more self-sufficient. The lack of advanced manufacturing technologies and processes is one of China's greatest weaknesses. Consequently, Beijing generally insists that foreign firms establish joint-venture operations in the electronics sector, though wholly foreign-owned enterprises (WFOEs) are not explicitly prohibited. Motorola Inc., for example, won permission to open a WFOE semiconductor testing and assembly operation in Tianjin in 1993, reportedly by agreeing to set up a semiconductor fab there. Similarly, many Japanese and South Korean plants that produce TV tubes, printed circuit boards, and other components have been established to meet local content requirements, which SPC sets on a per-product basis. Generally, SPC will not approve joint ven-

Smart Cards Leapfrog to China

Foreign technologies are flowing into China's electronics sector almost as fast as investment dollars. Among the most advanced innovations are "smart card" technologies being developed for use in China's banking and telecommunications sectors. In part an effort to overcome the slow pace of banking reforms in China, smart cards are an integral component of PRC efforts through the Golden Card project to set up a nationwide electronic payment system (*see* p.10).

A number of smart card projects are under way. One smart card issued jointly in late 1995 by Visa International, the local branch of the People's Construction Bank of China, and the Nanjing Posts and Telecommunications Bureau (PTB) can be used as a credit card, an automated teller machine (ATM) bank card, and a telephone credit card. The bank pays the PTB electronically and sends bills and receipts to cardholders. According to press reports, MasterCard International, with 11 million cardholders in China, recently announced plans to work with the Shanghai Pudong Development Bank to issue international-standard smart cards.

GPT Co. of Britain won a contract in May 1996 to install 500 smart card telephones in Zhejiang Province and has signed contracts with Beijing and Guangdong telecom authorities for 2,000 smart card pay phones each. German smart card powerhouse Meinen, Zeigel & Co. sold 15 smart card manufacturing systems to customers in China and elsewhere in Asia in 1995 (each system can produce up to 100 million cards annually). French manufacturer Gemplus Card International is setting up smart card plants in China, and one Sino-French joint venture, Tianjin Jiepu IC Co., is establishing a smart card production base in Tianjin. Schlumberger Smart Cards and Systems, another French company, also reportedly has signed a memorandum of understanding with Ministry of Electronics Industry subsidiary China Hua Xu Golden Card Co. to develop applications in China for smart cards.

Other US firms are also involved in developing China's smart card sector. IBM Corp. recently set up a joint venture with China Great Wall Computer Group and Kaifa Technology (Hong Kong) Ltd. The venture, Shenzhen GKI Electronics Co. Ltd., will develop, assemble, and test smart cards at its plant in the Shenzhen Science and Industry Park. And US firm Tandem Computer Inc. was chosen in early 1995 to provide the platforms for China's Golden Card project.

Some wrinkles need to be ironed out, of course. *China Daily* has reported that some stores and hotels will not accept cards from certain banks, while some banks have been unable to transfer funds between different credit card accounts. Nonetheless, the PRC's move to experiment with smart cards as part of the overall modernization of the banking sector represents a quantum leap in technology. As growing numbers of Chinese citizens jump from using cash for public phone calls and other consumer purchases to paying with plastic, the new technologies may help move some of China's hidden savings, or "mattress money," into the economy.

—Catherine Gelb

tures that do not intend to source locally a certain portion of inputs. Beijing also has explored the possibility of creating "inspection teams" made up of local officials to ensure that established joint ventures follow all laws and agreements. Several multinational corporations recently have run afoul of the government for perceived disregard of PRC policies, or for taking too much time to meet technology transfer or other commitments made at the time of project approval.

Further, China has phased out incentives for foreign investment in many industrial sectors. Included in the overall capital import duty change of April 1996 is equipment imported for the production of chips. Such equipment can no longer be imported tax-free, but incurs a 20-30 percent tariff as well as the 17 percent value-added tax (*see The CBR*, July-August 1996, p.32). And, though China reduced tariffs on almost 4,000 items in April, not all electronics products are included on the list. According to Zhao Wenzhi, MEI's deputy director of trade development, "The idea is to push foreign investors to move up-market. Approvals for joint ventures will now depend on how much research and development work the investor is bringing to China."

In addition, Chinese officials remain concerned about the ability of domestic electronics to compete with foreign brands. Chinese TV manufacturers such as Peony and Taishan have expressed strong concerns about the aggressive market entry of foreign firms such as Matsushita Electric Industrial Co., Ltd. and Sony Corp. Local brands, including the Legend Group Co., the largest domestic supplier of PCs in China, claimed only a 15 percent share of China's PC market last year. Foreign brands dominated, with IBM alone claiming an 11 percent market share. Beijing, however, has not responded directly to requests by domestic manufacturers for greater protectionism, most likely because of its WTO ambitions.

China's dilemma—the need for foreign technology and the desire for self-sufficiency—is highlighted in the case of Project 909, a State Council-sponsored microelectronics project in Shanghai's Pudong New Area. Project 909 is a "greenfield" manufacturing and testing facility for CMOS 8-inch wafers, and 0.5- and 0.35-micron very large-scale integrated circuits (VLSI). Shanghai was chosen as the preferred site for the project because it has become the center for microelectronics production in China. In 1995, Shanghai plants accounted for 21 percent of total Chinese production of semiconductors.

China needs foreign technology but desires self-sufficiency.

China's decision to pursue Project 909 came as a surprise to some foreign electronics firms because of the apparent difficulties of an earlier venture, Project 908. Another sub-micron electronics project in Shanghai, Project 908 stalled when funding conflicts arose between SPC and the Ministry of Finance. As a result, a number of the major foreign chip manufacturers steered clear of Project 908, which was slated to involve the Hua Jing Microelectronics Corp. In contrast, and reflecting the strategic importance of the current initiative, the major player in Project 909 is Hua Hong Microelectronics, whose board chairman is none other than MEI Minister Hu Qili.

Currently, the China Information Industry Holding Co. is Project 909's majority shareholder—with 52.5 percent of the project equity—while the Shanghai Instrumentation and Electronics Holding Co. owns the remaining 47.5 percent. The problem with the ¥10 billion ($1.2 billion) Project 909, however, is that in the aftermath of the Project 908 troubles, the Chinese side has been unable to attract a serious foreign partner to provide the technology. In return for the transfer of technology, the Chinese side is willing to offer the foreign supplier 20-25 percent of the equity. While focused discussions reportedly have been held with such firms as Advanced Micro Devices Inc., National Semiconductor Corp., and Siemens AG, these and other firms remain hesitant to participate because of questions about the reliability of the financing, the minority equity stake being offered, and the absence of a viable business plan.

Foreign companies respond

Some foreign producers claim China's current electronics plans make little sense for a country pursuing rapid electronics development, particularly in chip manufacturing. Further, some foreign firms argue, China's proposed 9th FYP goals are unrealistic given the constraints of tariffs, pressure on foreign ventures to export, and unequal treatment among FDI applicants. And, more recently, policies designed to block unwanted political, cultural, social, and economic information in an electronic format are sending a message that Beijing intends to keep a firm

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hand on the Internet and other electronic media in China (*see* p.18).

Because China's domestic semiconductor supply can meet less than 25 percent of the country's total demand, though, Beijing is forced to rely heavily on foreign investment and imports. One of the new centerpieces of foreign participation in the sector is the $2 billion IC factory in Beijing's Shangdi Information Industry Base (*see* p.12). The project is being launched by three partners: Mitsubishi Electric Co., Mitsui & Co., Ltd., and Beijing's Stone Group. The Stone Group, one of China's leading joint stock-holding companies, operates out of Beijing's Haidian "high technology" district near Beijing University and Zhongguancun, the base of the Chinese Academy of Sciences (*see The CBR*, January-February 1995, p.41). The joint venture, which is due to start production next autumn, has attracted political attention because Mitsubishi will own 60 percent of the equity, Stone 30 percent, and Mitsui 10 percent. In fact, Stone has been criticized for "marrying rich" to get into the semiconductor business. According to press reports, the initial capacity of the plant will be 11 million IC chips per month.

Another favored project in the semiconductor sector is a joint venture between Japan's NEC and Shougang Iron and Steel Corp. in Beijing. The joint venture began operating in 1994 and is primarily engaged in the design, development, production, and marketing of VLSI chips. The Beijing facility has a fully equipped diffusion production line and IC packaging line as well as a design center for new product development. In January 1996, NEC officials announced their decision to upgrade the technology used in the Shougang facility to 6-inch, 0.5-micron production technology. According to *China Electronics Daily*, NEC has increased its $230 million investment in the project by another $107 million. The venture's new products include dynamic random access memory (DRAM) circuits used for data storage; circuits for program-controlled devices; gate-array circuits; single-chip microprocessors; and ASICs. NEC officials believe that over the long term the project will position the firm strategically to respond rapidly to China's expanding need for advanced electronics devices and semiconductors.

Foreign firms, for their part, will have to decide quickly over the next few years how to build a sustainable position in the sector.

Motorola Inc. also has significant electronics operations in China through its wholly owned entity Motorola (China) Electronics Ltd. Since 1993, Motorola has manufactured pagers, cellular telephones and other communications components, and semiconductors at its Tianjin facility. Other Motorola China investments include a joint venture with Leshan Radio Factory in Sichuan to produce discrete semiconductors, and an agreement with Nanjing's Panda Electronic Group Corp. to produce home computers using its trademark PowerPC microprocessor. Motorola also is currently building a large-capacity, 0.8-micron IC fab in Tianjin, which should be operational by 1997. Motorola reportedly expects to produce approximately 14,000 IC wafers each month, to be used in the automotive, communications, and PC and peripherals markets.

Based on the successes of these and other foreign firms, a few general FDI trends seem to emerge. Foreign firms wishing to tackle China's electronics market would do well to keep a few pointers in mind when establishing projects in China's electronics sector: establish strategic partnerships with actors who can provide project sponsorship; sell solutions rather than products (solve problems for endusers); build a network of relationships in the middle levels of the PRC bureaucracy; develop an effective technology transfer strategy; and shift into higher value-added activities, such as R&D.

Joining the ranks of world players

In its effort to be a global force in the electronics industry, China is competing with its Asian neighbors, as well as with long-established Western companies. A comparison with two of its foremost Asian rivals illuminates the challenge before China. South Korea's top three semiconductor chip manufacturers, Hyundai Electronics Industry, LG Semicon, and Samsung Electronics Co. (a subsidiary of the Samsung Group) each boasted profits estimated to be over $1.3 billion in 1995. Among chipmakers worldwide, Samsung is ranked third overall and is currently ranked first among DRAM producers. China's semiconductor industry—while promising because of the high potential demand and the top priority Beijing has given it—still consists of relatively small-scale manufacturers with low productivity and low-level process technology. Poor infrastructure and immature peripherals industries also plague efficient operations.

By 2000, meanwhile, Taiwan expects silicon industry sales of $12 billion per year—which would require average annual growth of 46 percent from Taiwan's 1995 sales level of $2 billion. With 19 new front-end fabs installed in 1994, Taiwan's top 10 semiconductor manufacturers plan to build 11 new 8-inch fabs and one 6-inch fab before year-end 1997. China, with a more modest 1-2 fabs planned per year, will be hard pressed to keep up.

China has its work cut out to emerge as a force in the global electronics sector. Some of Beijing's initiatives to address overarching sectoral problems are beginning to yield results, however. It is clear, for example, that some progress has been made in improving quality control among domestic consumer electronics manufacturers.

Foreign firms, for their part, will have to decide quickly over the next few years how to build a sustainable position in the sector, especially given the apparent growth of the Chinese leadership's concerns about the foreign impact on the PRC economy. By establishing a strategic position in the electronics sector in the short term, however difficult, foreign companies can ensure for themselves a place in China's high-tech industry in the 21st century. Ultimately, though, the question is not whether China will succeed in creating a modern electronics industry, but when such an industry will make its impact felt worldwide and in which market segments. 完

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Up, Up, and Away—With Strings Attached

■ Paul S. Triolo and Peter Lovelock

China's Internet development has to overcome cultural, regulatory, and infrastructural hurdles

■ **Paul S. Triolo is the infrastructure policy officer at the US Embassy in Beijing. He covers the development of China's information infrastructure, including the Internet. Peter Lovelock, a Ph.D. candidate at the University of Hong Kong, is writing his thesis on telecommunications regulation in northeast Asia.**

China, like virtually every country rushing to be part of the global information age, is seeing rapid Internet expansion. With only a single commercial provider in May 1995, China has added a second national service provider and dozens of other Internet service providers (ISPs) offering a range of online services. Nationwide, interest in the Internet is keen, not least among businesses anxious to take advantage of the benefits afforded by electronic commerce. A detailed survey of ISPs by the authors found that as of late 1996, there were more than 25,000 commercial users in China, including individuals, businesses, and government departments (*see* p.20).

Meanwhile, of the estimated 1.7 million new personal computers to be sold this year in China, according to a recent industry survey, roughly 20-25 percent will be equipped with modems. Though some Chinese officials estimate the number of modems at a more modest 10 percent, the relatively low cost of adding a modem and the growing interest in online services means that the numbers of Internet users are sure to increase.

China's current installed base of personal computers is conservatively estimated at around 3 million. Of these, roughly one-third are older generation 286 and 386 machines that lack the minimum memory and speed requirements of Internet browser software such as Netscape Communications Corp.'s Netscape Navigator and Microsoft Corp.'s Internet Explorer. Most new computers sold in China, industry surveys say, are more robust 486 and Pentium processor-based machines that can accommodate browser software.

Forecasting numbers of Internet users is a difficult task, given the early stage of development of China's online services market. The Ministry of Posts and Telecommunications (MPT) predicts that by 2000 Beijing alone could have a million Internet users, though this figure seems high, given the many barriers to Internet use. Current statistics indicate that there are only about 11,000 registered domain names in China, which translates into roughly 2,000-3,000 servers or routers, the host computers that connect up to the Internet.

Individuals looking to link up to the Internet in China continue to face formidable barriers, particularly language, cost, and infrastructure. To overcome these difficulties and boost the appeal of online services, an increasing number of ISPs are trying to entice new users online through localization (*hanhua*) of software products and content, supplying users with Chinese-language browsers, search engines, and information. PRC government departments also are beginning to improve the country's online infrastructure by installing internal networks, or intranets, based on the

Internet's Transmission Control Protocol/Internet Protocol (TCP/IP) standard, which allows the transfer of data across different and otherwise incompatible software and hardware setups.

At the same time, a number of government bodies are grappling with the construction of a regulatory framework to govern Internet services in China. The PRC government is concerned, as are other Asian governments, about the socially harmful effects of unfettered access via the Internet to pornography, politically sensitive material, online gambling, and the recent phenomenon of unlicensed Internet radio broadcasts (*see* p.26). Indeed, in early September, Chinese authorities moved to block access from within China to a number of World Wide Web (WWW) sites, primarily Western news media sites, including the Cable News Network, *The Washington Post*, and *The New York Times*; Chinese-language publications from Taiwan and Hong Kong; potentially politically sensitive sites with material from Chinese dissidents living abroad; and sites offering pornographic material. It remains unclear how long these restrictions will remain in place or whether their scope will widen. During recent nationalism-inspired protests over Japanese activity on the disputed Diaoyu Islands, Chinese students for the first time used the Internet to try to organize a campus protest, an action which set off alarm bells in Zhongnanhai, the Chinese leadership compound (*see* p.4). Overall, though, at present Chinese authorities appear to value the positive aspects of Internet access, particularly expanded online access to Chinese government data sources.

Spinning a wider web

That the Internet appears here to stay in China is good news for foreign companies specializing in Internet-related hardware and software, such as Sun Microsystems Inc. (servers), Cisco Systems, Inc. (routers), Microsoft (web browser/server software), and Netscape (web browser/server software). These firms currently dominate the sector worldwide and will continue, at least in the near term, to supply virtually all of the hardware and software, including routers, servers, and modems, as well as web-related software.

But foreign involvement in Internet services at present is limited to investing in an existing Chinese company or providing consulting services, which must be offered under the guise of a systems sale or a joint-venture agreement. Beyond this limited degree of participation, foreign companies currently are prohibited from operating or managing value-added telecommunications networks, and are not likely to be allowed greater entry into the area of service provision any time soon.

Nonetheless, China's need for Internet-related equipment is likely to be significant in coming years. MPT launched commercial Internet services in Beijing and Shanghai in 1995, with help from US firms. MPT offers full point-to-point protocol (PPP) accounts that allow WWW browsing, along with standard services like e-mail, telnet, and newsgroup access. But MPT has never offered users space on its servers for storage of WWW home pages, a service typically available in other countries.

In early 1995, a US company founded by Western-educated Chinese, AsiaInfo Services, Inc., subcontracted with Sprint Communications Co. L.P. to develop the first two nodes. A typical node configuration includes a router (linked via a leased-line connection to other routers and eventually to other networks that, taken together, constitute the Internet), several powerful computers to act as servers, modem banks for dial-in access, a large and steady power supply, a telephone switchboard, and other computers for special purposes such as maintaining a security "firewall" or monitoring system.

AsiaInfo subsequently won an MPT contract to install a nationwide Internet backbone expanding on the first two nodes. This network, known as ChinaNet, is slowly coming into operation in provincial capitals around China (*see* chart). As of September 1996, nodes allowing local access to the Internet were up and running in Beijing, Fuzhou, Guangdong, Hangzhou, Shanghai, Shenyang, Tianjin, Wuhan, and Xian. These nodes, the first of 30 planned for cities throughout the country, are now linked only to either Beijing or Shanghai directly, though eventually the nodes will be linked to each other as well. As of late October, AsiaInfo officials indicated that ChinaNet had 50 nodes under construction or operation, including 28 provincial capitals. By next April, they hope to have an additional 50 nodes operating. Once

ChinaNet: China's Internet Backbone (as of September 1996)

Province/ Municipality	Paying Customers	Provincial Intranet	System Integrator
Beijing	7,000	—	Sprint Communications Co. L.P. (Global One)
Fujian	500	10 nodes	AsiaInfo Services, Inc.
Guangdong	3,000	10 nodes	AsiaInfo
Heilongjiang	NA	6 nodes	AsiaInfo
Hubei	NA	—	NA
Jiangsu	800	11 nodes	Sprint (using frame relay)
Liaoning	500	4 nodes	AsiaInfo
Shandong	100	—	Sprint
Shanghai	3,000	—	Sprint
Shenzhen	500	—	AsiaInfo
Sichuan	NA	—	AsiaInfo
Tianjin	500	—	AsiaInfo
Xian	1,000	—	AsiaInfo
Zhejiang	1,000	—	AsiaInfo

SOURCE: Compiled by Paul S. Triolo from Chinese press reports and interviews with industry participants
NOTE: NA = Data not available

Internet Access/Content Providers

Those interested in hooking up to the Internet in China can choose from among several Internet service providers (ISPs):

Beijing

Beijing Telecommunications Administration (BTA) BTA is the largest access provider in Beijing. Though users report problems with line quality and access, local dial-up service has improved and is being upgraded. Connections are made through 14.4 kilobyte per second (Kbps) modems. Fees: ¥600 for 40 hours/month, ¥100 for 6 hours/month.
Tel: 8610/6601-0861

NetChina Infotech, also called 3CNet Located in the Beijing International Convention Center, this company was founded last year by a group of Qinghua University graduates with some $10 million in investment from a variety of Chinese investors, including Qinghua University. The NetChina Network Operation Center, one of the best equipped in China, has 600 dial-in lines and plans to develop a nationwide operation. The company currently shares a 64K line with the Beijing University of Chemical Technology and is trying to obtain additional bandwidth from MPT to improve service to its Internet customers. Eventually, NetChina could become one of China's best ISPs.

NetChina offers basic services such as e-mail and World Wide Web (WWW) access, as well as more advanced online services. The company also offers network management services, database services, and WWW home page design. The subscriber base is around 500. Fees: To be determined.
Tel: 8610/6493-3316; Fax: 8610/6493-3323;
e-mail: michael@netchina.co.cn
http://www.netchina.co.cn/

China GBNet This service, officially launched in early September, is operated by Jitong Corp. in cooperation with UTStarcom, a US-based telecommunications company that is providing investment and consulting services. At present, the company is offering primarily Internet access services. The application process is the smoothest so far of the Beijing providers, with same-day online hookup. Because GBNet's user base is still small and it is using an international circuit that does not have to go through BTA's slow Beijing gateway, service is currently faster than most of the other ISPs. Fees: Dedicated line service for corporations starts at ¥4,800/month for 220 MB of a 64K leased line. For individuals, the fees will be ¥200 for installation and ¥500 for 40 hours/month or ¥100 for 7 hours/month.
Tel: 8610/6236-6574; Fax: 8610/6236-6575

EastNet A cooperative joint venture with the Ministry of Communications, EastNet recently began offering Internet services, primarily to corporate customers. EastNet hopes to target companies interested in developing their own internal networks, or intranets. The company currently has a 64K leased-line connection to the Ministry of Posts and Telecommunications (MPT) for Internet connections and plans to expand to a 256K line soon. The company also sports 28.8 Kbps modems, the fastest available in China. The company is negotiating with MPT for lower prices, particularly the per-megabyte charge for large data transfers. EastNet offers traveling businesspeople temporary accounts for local access to CompuServe and America Online; local dial-in access; home page development; and intranet solutions. Fees: Start-up fee of ¥1,450 includes on-site installation, software, classes, and tech support. Individual "light" users: ¥120-¥150 per month for 6 hours/month, depending on length of contract (3, 6, or 12 months); ¥20 each hour over the 6-hour limit. "Heavy" users: ¥600/month for 40 hours/month.
Tel: 8610/6526-1610; Fax: 8610/6526-6059;
e-mail: info@eastnet.co.cn

CENPOK Intercom Technology Ltd. Established with investment from CENPOK Human Resources Ltd. and a subsidiary of China Central TV (CCTV), this new joint venture offers 28.8 Kbps modem service and a full range of Internet services including home page development, disk storage space, and host rental. Fees: Start-up fee of ¥1,500: ¥200 for 10 hours/month, ¥900 for 70 hours/month, ¥25/hour additional access charge.
Tel: 8610/6815-6888; Fax: 8610/6827-7230;
e-mail: sales@cenpok.intercom.co.cn

Unicom-Sparkice Formed in May 1996, this venture links a Canadian firm, Sparkice, with China's second national telecom carrier, Unicom. The company may begin offering dial-up access in November, but initially is concentrating on software development, assisting the State Planning Commission's State Information Center in developing online databases, and purchasing rights to other databases that it will make accessible via the Internet using its own Chinese-language platform, Sparkice 1.0. Unicom-Sparkice plans to open Beijing's first "Cybercafe" in late 1996. Fees: ¥600 for 40 hours/month; ¥100 for 6 hours/month.
Tel: 8610/6833-9691;
Fax: 8610/6831-2881;
e-mail: sparkic@public.bta.net.cn
http://www.sparkice.com

ICNet Formerly called IUOL, ICNet (Internet Commercial Networks, Ltd.) provides services for individuals and corporations. ICNet is linked to BTA via a 64K leased line. ICNET services include e-mail, Internet access, and home page design.
Tel: 8610/6492-3077; Fax: 8610/6492-2920;
e-mail: sales@iuol.cn.net

CINET Located only in Beijing at present, CINET currently is using a 128K dedicated link to BTA to provide e-mail and Internet access services. CINET also offers local access to CompuServe via ChinaNet.
Tel:8610/6494-1268; Fax: 8610/6494-1267;
e-mail: market@mailhost.cinet.co.cn

Masslink Technology Company One of the top four or five providers in Beijing, operating under the PANNET logo, their services include home page design, leased-line access, intranet development, and user training.
Tel: 8610/6607-7599; Fax: 8610/6607-7605

Yinhaiwei Primarily a bulletin board service, Yinhaiwei also offers Internet access to its 4,000 subscribers through the company's proprietary software. Services include Chinese-language online travel reservations, chat rooms, and cultural information.
Tel: 8610/6256-3610; Fax: 8610/6256-1610; e-mail: jasmine@space.ihw.co.cn

Fujian Province

Xindeco Based in Xiamen, Xindeco recently completed a project, *XiamenVista*, to put information on the Xiamen Special Economic Zone (SEZ) online. At present, Xindeco provides home page design services and online database access. It will soon have dial-up capabilities. Xindeco opened a new online presence in early September, *ChinaVista*. One of its anchor sites is Hyper-C, a China-specific browsing and search tool (http://www.chinavista.com/hyper-c/hyper-c.html). *ChinaVista* also contains a full-service web site for the Nanjing city government, called *NanjingVista* (http://www.chinavista.com/nanjing/home.html) and two other, limited sites for Beijing and Shanghai. Another new addition will be the ChinaVista Business Reference Desk (currently under development), which will offer access to real-time stock prices, currency exchange rates, business news, airline reservations, business law, and hotel information.
Tel: 86592/602-1666; Fax: 86592/602-3225; e-mail: kfarrall@xindeco.com
http://www.xindeco.com

Shenzhen

China On-line Though currently based in Shenzhen with a customer base of 500, China On-line aspires to become a nationwide service provider. The company, backed by the considerable financial resources of Chinese real estate developer Rayes Group Ltd., could emerge as a major player in the Internet market in China. China On-line presently has network nodes in Beijing, Guangzhou, Nanjing, Shenzhen, and Xian, and is working to build its network in cities across China. Services include local Internet access and a full range of Internet services, plus home page design.
Tel: 8610/6828-9601; Fax: 8610/6828-2725; e-mail: xiaoyan.long@bj.col.co.cn

Guangdong Province

Feijie Computer Networking Information Co. The company offers the full array of Internet services, from e-mail to WWW access. Feijie also offers access to stock market news from the Shenzhen exchange, a number of online newspapers, and educational materials.
Tel: 8620/8666-8727; Fax: 8620/8666-4870

Shiliantong Under the Guangdong Provincial Posts and Telecommunications Administration, the Shiliantong Service Center is part of GNET, a closed network in Guangdong. The center offers a number of Chinese-language services, including access to the Zhongshan University Library, and online Chinese newspapers such as the *Guangzhou Daily* and the *Hong Kong Macao Information Daily*. It also provides e-mail services.
Tel: 8620/750-8718; Fax: 8620/750-8718; e-mail: gnet@TDM.Gnet.com

Academic Networks

CERNET, the China Education and Research Network, now connects over 150 of China's top universities. Based at Qinghua University, the network is backed financially by China's State planning and education commissions. CERNET officials recently completed a deal to upgrade their international Internet link to an E1 line. Completed last year, the first phase of CERNET completes links between the network's 10 regional centers, Beijing University, Beijing University of Posts and Telecommunications, Dongnan University, the University of Electronics and S&T, Huanan University of Science and Technology, Huazhong University of Science and Engineering in Wuhan, Nanjing University, Northeast University in Shenyang, Qinghua, Shanghai Jiaotong, and Xian Jiaotong. CERNET engineers are working to develop and expand the applications available via the network.

Five main applications are currently being used: resource sharing, including sharing of databases and software applications; computer-aided instruction, using software developed by Qinghua; management information systems, including office automation applications; library retrieval systems; and communications applications such as e-mail. CERNET also offers such Internet services as WWW access, telnet, and gopher, and provides university web pages for member institutions. Most of CERNET's universities sport home pages. CERNET offers outside dial-in accounts, primarily to professors and students. Many students share accounts, on average 3-5 students per account. Qinghua University also sports the most popular bulletin board in China, with over 15,000 users worldwide, including overseas Chinese from the United States and Southeast Asia. The bulletin board can be reached via telnet at 166.111.1.11, or via the WWW at bbs.net.tsinghua.edu.cn.

CASNET, the Chinese Academy of Sciences Network, is much smaller than CERNET. Started with funding from the State Planning Commission and the World Bank, it includes the Beijing University network, the Qinghua University network, and a number of the networks of scientific institutions such as the State Science and Technology Commission network, the National Flood Control wide area network, the CAS Institute of Microbiology, and the Chinese Ecosystem Research network. CASNET has two international links: a 64K link through the Institute of High Energy Physics (IHEP) and a 64K link from the network's operation center. A key CASNET node, IHEP now publishes a Chinese-language online magazine, found at http://www.ihep.ac.cn/magzine/. IHEP and CASNET both offer outside dial-in accounts, primarily for e-mail. IHEP probably has about 1,000 such accounts, with perhaps 500 more from CASNET.

Taking aim at MPT on pricing

Chinese regulators (primarily from MPT-offshoot China Telecom and the State Council Leading Group on Informatization) are working to develop Internet-related service fee guidelines for ISPs. Apparently, the Leading Group and MPT, as well as ISPs, have reached an agreement that the user fees are appropriate. The main problems lie with the leased-line and international leased-line charges, controlled by the MPT. Most ISPs consider current rates for these lines to be excessive.

—Paul S. Triolo

the backbone is completed—likely some time in 1997—AsiaInfo will turn over full operation of the network to MPT's Data Communications Bureau (DCB). The DCB has established a Network Operation Center (NOC) in Beijing for this purpose. Many provinces, particularly the more developed coastal provinces of Guangdong, Fujian, and Jiangsu, are also currently working with AsiaInfo or Global One/Sprint to develop their own intra-provincial networks.

Currently, ChinaNet is connected to the global Internet through the two gateways in Beijing and Shanghai. In Beijing the connection consists of one-half of an E1, or 1.024 megabytes per second (Mbps) circuit, and a 256 kilobyte (K) circuit connected to Sprint. Sprint and MCI Telecommunications Corp. are the carriers on the US half of a satellite and a fiber-optic link, respectively. The companies each have a router on their end through which the China traffic passes. In Shanghai, Sprint provides a full E1 circuit. A third connection, linking Guangdong to Hong Kong, and a fourth potential link through Shenzhen to the United States currently await State Council approval.

While MPT trumpets ChinaNet as the nation's Internet backbone, the ministry's initial investment, roughly $30 million, was not very large. The nodes in provincial capitals also are not large, providing relatively limited dial-in capability and a small number of servers; and routing of

A Telecom Newcomer Challenges the MPT Monopoly

Since December 1993, the Chinese government has promoted the China United Telecommunications Corp. (Unicom) as a potential rival to the State-run monopoly Ministry of Posts and Telecommunications (MPT). The new telecom firm has faced both management problems and MPT resistance since its licensing, but foreign telecom firms, unable to make much headway with MPT in gaining access to the China market, have found Unicom a willing potential partner.

The Chinese government began to investigate widening the field of telecommunications service providers as early as 1988. The initial impetus for reform came from the Ministry of Electronics Industry (MEI), which had manufactured equipment for the industry but wanted a piece of the operations pie. MEI Minister Hu Qili led the drive in the early 1990s to create a rival to MPT operations control. Eventually, the ministries of electric power and railways, and 13 other partners joined MEI to form Unicom, which began operations in July 1994. MEI, lacking its own telecommunication lines or wireless systems, favored the alliance with the power and railway ministries, both of which had substantial private telecommunications networks. The Unicom members together represented a potentially powerful array of stakeholders to challenge the MPT monopoly.

The nascent company's goals were ambitious: by the year 2000, it intended to hold 10 percent of both domestic and long-distance service in China, and capture 30 percent of the country's mobile communications market. Unicom's charter encouraged the company to expand into areas where the public networks could not reach or where there were severe shortages of services.

A rocky start

The diffuse shareholding structure immediately created problems for Unicom, as did the attempt to keep the State shareholders out of Unicom's top management. Zhao Weichen, former vice minister of the State Economic and Trade Commission and vice governor of Guangxi Province, apparently won the top job at the company by default. Though he spent little time actually managing the company, Zhao sought complete control over Unicom and kept any potential rivals at bay during its early years of development.

In his desire to see the company expand nationwide, Zhao encouraged the proliferation of Unicom "branch companies." The three ministries, other original shareholders, and provincial and municipal entities thus set about targeting sites for mobile phone service across the nation. By the end of this year, Unicom plans to have more than 50 of these branches with operations in 22 cities. But the corporate headquarters has prohibited any of the branches from establishing itself as a legal entity, and each therefore requires approval from central Unicom officials to form a joint venture. Anticipating the iron grip with which Unicom is managed from the top, some shareholders had already struck out on their own: China International Trust and Investment Corp. (CITIC) and MEI had already formed wholly owned subsidiaries (CITIC Telecom and Chinacom, respectively) at Unicom's July 1994 launch. As these two subsidiaries lack operating licenses, however, contracts with CITIC Telecom and Chinacom are still subject to final approval from headquarters in Beijing.

The company also lacks a strong central capital base. The three ministerial shareholders contributed only ¥100 million ($12 million) each at the company's start-up, and the other 13 shareholders contributed ¥80 million ($9.6 million) each. The central government provided no other financial support, though the State Council allocated 6 megaherz (MHz) of radio frequency in the 900 MHz spectrum band to the new company, 50 percent more than the 4 MHz granted to MPT for its own GSM cellular network. And with so many branches, the central office now has little financial leverage over the entire organization.

MPT staunchly opposed the formation of Unicom, and the ministry continues to hinder Unicom's expansion, primarily through its control over the public network. Only after completing a seemingly endless series of forms was Unicom allowed to hook up its customers to the national network. MPT's predatory pricing of mobile handsets also weakened Unicom in 1995; MPT was quick to match or beat any attempts to undercut its prices in the markets Unicom pursued.

traffic through ChinaNet's internal nodes has been somewhat inefficient. Some of the new ISPs, such as NetChina Infotech, have better-equipped NOCs. Though MPT's original design plans called for major regional nodes to be linked by E1 lines, currently they are not, and the Guangdong node's links to Beijing and Shanghai have yet to be upgraded to E1 speed. The overall system bandwidth, meanwhile, may soon become insufficient as the growth in the number of users further outpaces the necessary system upgrading. The international links—plagued by bottlenecks—already represent the greatest drag on system performance. Industry observers estimate that at the present rates of user-base growth, the international bandwidth needs will hit 35 Mbps by the end of 1997. Currently, MPT—the only institution providing overseas connections—has only 3 Mbps in capacity and so far has shown reluctance, both for financial and other reasons, to expand international bandwidth.

As MPT builds up its network, other contenders hope to build their own national service platforms. In early June, Jitong Corp., a Ministry of Electronics Industry (MEI) subsidiary formed in 1994 to provide data communications services, received a license from MPT to offer commercial computer information services, including intranets for companies and Internet connections. Jitong has

MPT also has established a biased rate system for access to ministry lines (interconnection). In Shanghai, for example, a 10-minute mobile phone call costs the Unicom customer ¥4 (about $0.50). Of this, the Shanghai arm of the MPT collects 90 percent of the toll, leaving Unicom to receive less than $0.05 per transaction.

The only chance for Unicom would seem to be a division of the MPT conglomerate's regulatory and operational activities. In 1994 the government announced this type of decision, stating that the Directorate General of Telecommunications (now China Telecom) would serve as the national system operator, while MPT would act as regulator. Nevertheless, the two entities continue to work hand in hand. High-level leaders, in particular Vice Premier Wu Bangguo, have made the division of business and regulatory functions a top priority in the country's drive to reform State-owned enterprises. Real separation of the functions and the vesting of true financial powers in China Telecom—currently, all monies flow through MPT—are prerequisites not only for telecom sector reform, but also for the establishment of an effective legal framework and the development of real competition in the industry.

Unicom's future

Foreign firms have been looking to Unicom as a potential partner in China's telecom market because they generally have been rebuffed in attempts to team up with MPT's operational arm, China Telecom. Unicom has allowed foreign partners to build, transfer, and consult on network development. These experiments stop just short of operation, which is prohibited under largely MPT-composed regulations. Typically, a Unicom subsidiary forms a joint venture with a foreign company, which then contracts to build a network. The foreign companies are repaid through informal revenue-sharing arrangements not spelled out in the joint-venture contracts. Foreign partners do not hold equity in the deals, though many hope eventually to convert their debt to equity if and when the current regulatory regime changes.

Despite these efforts, by mid-1996 Unicom's four operational mobile phone networks collectively served some 35,000 subscribers, well below its early growth targets. But recent developments give foreign investors some reason to hope that Unicom's difficulties could be coming to an end. In July, Li Huifen, former vice mayor of Tianjin and a radio corporation engineer with long ties to MEI, rose from her post as Unicom general manager to take the company's newly created CEO position. Former MEI Vice Minister Liu Jianfeng, who recently assumed the Unicom chairman position, appears slated to play a more minor role. Li's past affiliation with MEI, along with MEI moves to consolidate control over Unicom by purchasing Unicom shares from other partners, indicate that control is becoming more concentrated. Though such MEI support is helpful, higher-level support is key: Li reportedly has convinced Premier Li Peng to force MPT to facilitate future Unicom connections to the fixed public network.

Unicom's recent moves to break into the Internet service market could also prove profitable for the firm. Unicom has set up a joint venture with Canadian firm Sparkice to provide nationwide Internet services. Currently the firm is working with the State Planning Commission's State Information Center to put its databases online and is purchasing rights to other databases that it will make accessible over the Internet. Moreover, Unicom-Sparkice President Edward Zeng plans to build a Chinese-language platform on a low-cost network computer aimed at cost-conscious Chinese consumers who may not have the English language skills necessary to make use of the global Internet.

Unicom's new leadership, top-level support from vice premiers Wu Bangguo and Zou Jiahua, and hard resources such as frequency allocation and the recent success in development of its own local-access networks in Beijing and Tianjin may be enough to assure the success of this experiment in telecom deregulation. Vested foreign participation in the Sparkice project as well as branch joint ventures with Ameritech International, Bell Canada, and other foreign telecommunications operators are also sure to help. If nothing else, the benefit that MPT derives from the appearance of competition in the sector should ensure Unicom's longevity. Though it probably will not reach its development goals for the year 2000, Unicom should survive to celebrate its sixth birthday that year.

—Eric Harwit and Jack Su

Eric Harwit is assistant professor of Asian Studies at the University of Hawaii. Jack Su is a telecommunications consultant based in Beijing. *This research was supported by grants from the University of Hawaii's Center for International Business and Economic Research and the United States Information Agency.*

teamed up with US-based UTStarcom to offer Internet services using as a platform Jitong's Golden Bridge (*see* p.10). UTStarcom, which has invested $10 million in the joint venture and is backed by Japanese investor Masayoshi Son's Softbank Corp., will provide consulting services. Jitong launched the Golden Bridge Network (GBNet) officially in September, rolling out a Beijing NOC and Internet access nodes in Guangzhou, Shanghai, Shenzhen, and Wuhan. A second tranche of cities, including Chengdu, Fuzhou, and Xian, will be hooked up by the end of the year. By June 1997, Jitong plans to have 24 cities linked to the Internet via GBNet.

Jitong will concentrate on attracting customers from large enterprises and government ministries. As of late September, Jitong had signed up nearly 400 GBNet customers. As its customer base grows, Jitong plans to expand its current 256K global Internet link (via Sprint to the United States) to the T1 (2.048 Mbps) or E1 level. Currently, GBNet is able to offer faster links with the global Internet because its international connection is free of some of ChinaNet's routing problems and its customer base is still small. For example, using GBNet, users are able to download a 3 megabyte file from a US web site in under an hour, an operation that currently takes considerably longer via ChinaNet.

Waiting in the wings

Under interim guidelines issued in January, only four entities are authorized to serve as managers of international Internet access in China. These interconnecting networks (*hulian wangluo*) are MPT and MEI (through Jitong), both of which serve the commercial side of the market; and the Chinese Academy of Sciences and the State Education Commission, which serve China's academic community through their two respective operations, Chinese Academy of Sciences Network (CASNET) and China Education and Research Network (CERNET). Though no other organizations are likely to be granted licenses to become interconnecting networks before the end of 1996, it will still be possible to establish new ISP companies.

Several other organizations, nevertheless, would like to join this group, including China United Telecommunications Corp. (Unicom), China's second national telecommunications carrier (*see* p.22). Unicom has formed a joint venture with a Canadian firm, Sparkice, to provide both Internet services and its own content. Working with the SPC's State Information Center (SIC), the company has worked with Jitong to develop software to access SIC databases on tourism and enterprise information. Unicom-Sparkice, in an aggressive bid to become a national Internet service provider, is trying to acquire stakes in local companies and push the regulatory authorities to permit Unicom to become a *hulian wangluo*. The joint-venture company also is working with Jitong to provide content for GBNet.

> MPT trumpets ChinaNet as the nation's Internet backbone, but the ministry's initial investment in the network was not very large.

Other would-be Internet service providers include Xinhua News Agency, which is currently petitioning the State Council for permission to offer Internet services. Xinhua already has started constructing a TCP/IP-based network that will use a satellite platform to link its bureaus throughout the country. Other PRC ministries with national telecommunications networks are interested in establishing an Internet presence, though some of these organizations lack the expertise and personnel necessary to enter the increasingly competitive market. One key player that could emerge as a significant force in the Internet service arena is the Ministry of Radio, Film, and Television (MRFT). MRFT has an extensive cable network, and already is testing plans to deliver data services, including Internet, via cable to endusers. MFRT's Shenzhen Cable Television Station and the Shenzhen Aoneng Software Systems Co., Ltd. have recently begun operating a cable service for delivering Internet within a small test area in Shenzhen using a hybrid fiber-coaxial (HFC) system. Independent companies such as NetChina, which is also applying to become an interconnecting network, and China On-Line Technologies hope to establish their own national networks.

Yet only Jitong and Xinhua, with satellite-based networks, and MRFT, with a wide-reaching cable network, currently are capable of providing network service without relying heavily on MPT's telecommunications infrastructure; and even Jitong and Xinhua must rely on MPT lines for local access. Not until Unicom establishes a second local telephone network—which will depend on the company's ability to attract investment for expansion—will ISPs be able to reduce their dependence on MPT. Under such a scenario, Jitong can be expected to team with Unicom to provide services. Such an arrangement would capitalize on Jitong's license as an interconnecting network and Unicom's growing telecom facilities. MEI's recent moves to assume greater control of Unicom also make such a link likely.

Campaign for (Chinese) content

Along with China's rush to develop the infrastructure to provide Internet access comes a push to develop Chinese-language content, in some cases available online only within China. Subscribers to a particular ISP can tap into the provider's members-only supply of online news, research and entertainment resources, and "chat" areas. As much of the Internet's content is in English, Chinese would-be participants find the language barrier a huge obstacle to taking advantage of the Internet's resources. Many ISP companies seeking a toehold in the China market thus are developing a mix of content and services. Providers break down into several categories:

■ **Bulletin board services (BBS)** Last year, Zhang Shuxin, a Chinese entrepreneur impressed by the content and services offered by America Online, Inc. (AOL) and CompuServe Inc., founded a company called Yinhaiwei, also know as 1+Net. Zhang's company, the leading BBS provider in China, teamed with a Florida software firm to design a Chinese-language bulletin board interface to provide online travel information; book reviews, games, and selected news feeds;

and chat rooms where people can post messages and contact other people online. Like AOL and CompuServe, Yinhaiwei offers its BBS and Internet access through proprietary software—though, unlike the two US firms, Yinhaiwei users must purchase the software. As BBS charges are much cheaper than Yinhaiwei's Internet access charges, the majority of Yinhaiwei's more than 4,000 users avail themselves primarily of the bulletin board's Chinese-language services.

An MPT subsidiary and a company under the Ministry of Foreign Trade and Economic Cooperation each recently purchased roughly 33 percent shares in Yinhaiwei, an indication that Yinhaiwei is winning government support—and giving the company the green light to become China's answer to AOL and CompuServe. MPT recently granted Yinhaiwei a license to expand its operations nationwide. The company will continue to concentrate on customers interested in Chinese-language content who are neither interested in, nor able to pay for, full Internet services.

> The Ministry of Radio, Film, and Television could emerge as a significant force in the Internet service arena.

In addition to Yinhaiwei, there are some two dozen bulletin board services in Beijing alone, including China On-Line Technologies, which has 500-800 users. Most do not offer access to the global Internet, offering only direct dial-up access to the local BBS.

■ **Closed network (intranet) providers** In Guangdong Province, the provincial DCB operates both the open ChinaNet network, linked through Guangzhou to Beijing and Shanghai and then to the global Internet; and GDNet, a closed network that offers Chinese-language information to a growing local subscriber base. GDNet, which offers access through Feijie Computer Networking Co., a company established by the Guangdong provincial Posts and Telecommunications Administration (PTA), gives users access to databases from Zhongshan University, tourist information, and economic news. Though currently not linked with ChinaNet, Guangdong PTA officials are considering establishing such a link.

GDNet is also linked to a Hong Kong network operated by China Internet Corp. (CIC). CIC, which has formed a joint venture with Xinhua, hopes to establish a closed network for the China Internet market. Customers—both corporations and ISPs wishing to access networks such as GDNet—would have to register with CIC and agree contractually not to violate Chinese law. Such a requirement places the burden of supervision on the company, and makes it possible for the company to punish violations. For example, CIC could deny Internet access to a user who violates PRC law by bringing pornographic or politically sen-

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** Highly developed infrastructure
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sitive material into China via the Internet. In the meantime, though, users in China using CICNet have access to the company's extensive Hong Kong online databases and services, which are not subject to the PRC's restrictions. In October 1996, CIC announced plans to launch the China Wide Web (CWW), a Chinese version of the World Wide Web. CWW will establish partnerships with Dun & Bradstreet, Reuters, and other news services to offer financial and business information.

■ **Business and public data service providers** Chinese enterprises and local governments are rapidly waking up to the Internet's business potential. Already, a number of companies, including Cyberway in Shanghai, Chinese

Asia Meets the Internet

Many countries, including China and the United States, are struggling to regulate the use of the global Internet. In the United States, the 1995 Communications Decency Act attempts to guard against child pornography; in Singapore, users must register to access political and religious sites; and in Germany, government authorities are attempting to ban neo-Nazi websites. In Jordan, the concern is sexually explicit material; in Malaysia, the government is trying to monitor Internet use by students critical of government policy. For policymakers and regulatory authorities around the world, the Internet poses a basic problem of definition: is the global interlinking of computer networks a telecommunications service and therefore subject to regulation? Or is it an information service, requiring regulation of the content?

China's efforts to manage the Internet are often compared to developments in Singapore, where the government has attempted to restrict foreign content and foreign ownership of Internet service companies. Indeed, telecommunications and security authorities in Beijing have already hosted Singapore delegations to advise them on both of these questions. However, there are also dramatic differences—not the least of which is the state of the network infrastructure and the PRC's experience with online computer systems. A brief round-up of Internet policing efforts around the region may give some indication where China's efforts might be heading.

■ **Singapore** The city-state had roughly 100,000 Internet users by mid-1996. The government hands out annual licenses to Singapore's three Internet service providers (ISPs)—SingNet, Pacific Internet, and Cyberway—as well as to political parties that maintain websites, those who run discussion sites on politics and religion, and online newspapers. The licensing scheme, begun earlier this year and designed to "safeguard public morals, political stability and religious harmony," is consistent with the government's policy of regulating books, movies, and public discussion that "undermine public security, national defense, racial and religious harmony, and public morals." Two groups—those who provide or sell Internet access and those who provide information with business, political, or religious content—are deemed to be licensed automatically. But these groups are required to follow guidelines issued by the Singapore Broadcasting Authority (SBA) on what material can enter Singapore.

The SBA guidelines prohibit material that jeopardizes security or defense, or undermines confidence in the administration of justice; misleads and alarms the public; tends to hold the government in hatred or contempt, or excites disaffection against it. The kinds of material determined to fall under this last prohibition are "a matter of judgement on the part of the SBA." The vagueness in the rules encourages self-censorship and allows Singapore authorities to adjust the regulatory framework as the technology evolves—a point the authorities overtly recognize. At least 10 SBA officials surf the Internet daily looking for objectionable material. To register under the new Class License Scheme, service providers are required to divulge such information as the targeted readers, the names of the editors and publishers of websites, and the nature of the organizations behind them.

The three ISPs have begun construction of a high-speed E1 (1.024 megabyte per second [Mbps]) Internet backbone for distributing local traffic. Before the establishment of the backbone, Internet communication between Pacific Internet and SingNet came via a slower 128 kilobyte per second (Kbps) link, while e-mail and World Wide Web (WWW) access between them and Cyberway had to be routed via the United States. Under the new system, Internet traffic among the three companies can be routed directly within Singapore. The strength of Singapore's control model stems from the exclusive control of Singapore Telecom's public telecommunications international gateway. Once Singapore's international telecommunications services are liberalized in 2002, though, it is questionable whether the government will be able to enforce the same tight control over content. Even now, service providers such as CompuServe Inc. can provide Singapore residents with unimpeded access to the Internet.

■ **Hong Kong** In 1992, the Hongkong Academic and Research Network (HARNET) was established based on the Chinese University of Hong Kong's 64 Kbps Internet link. In 1995, Hong Kong's Internet development exploded. By the end of that year, more than 40 ISPs had been licensed by Hong Kong's Office of Telecommunications Authority and the estimated number of users had grown to 100,000. ISP companies were established by former bulletin board operators, paging companies, and even listed companies and large multinationals. By mid-1996, the number of licensed ISPs exceeded 70 and users had grown an estimated 50 percent. Most ISPs have direct links overseas. Others are piggyback firms that rely on ISPs with a local presence to conduct transit for them.

As in Singapore, the Hong Kong international telecommunications gateway is controlled by one exclusive license holder, in this case Hong Kong Telecommunications International. However, there is no monitoring of content, as the

Windows—based in Shanghai with branches in other cities—and Xindeco, a company in Xiamen, Fujian Province, offer business services such as WWW home page development to municipal governments and local businesses. Xindeco has set up a detailed online service to advertise the Xiamen Special Economic Zone. Called *XiamenVista,* the project provides online a wide array of information on doing business in Xiamen, from laws and regulations to profiles of individual companies and their products.

Government projects to disseminate information through the Internet also are springing up around the country. In a March 1996 speech, MPT Minister Wu

Internet is defined strictly as a value-added telecommunications service. To obtain a license, ISPs in Hong Kong must simply file for a public non-exclusive telecommunications license and pay service charges accordingly. The ease of obtaining a license has resulted in intense competition and a variety of services, as well as a proliferation of local content and information exchanges.

■ **India** If China is a somewhat underdeveloped version of the Singapore model, India is a chaotic version of Hong Kong. India has had Internet access for several years through the Department of Electronics' Education and Research Network (ERNET). However, as with China, full-fledged Internet connections began only recently with India's long-distance carrier, VSNL, providing access to subscribers in the major cities.

Unlike China, India has no explicit national initiative to develop high-speed data networks. Instead, India has taken a market-driven, piecemeal approach to infrastructure development, with VSNL competing against private ISPs. The existence of only one public international gateway has caused problems, however, because no discussions were held with the existing value-added service providers to plan for the country's major expansion in Internet services. Consequently, the private service providers are not clear about the kinds of online services they are permitted to provide through the Internet. The lack of coordination and political battles between the Department of Electronics, the Department of Telecommunications, the National Informatics Center, and VSNL is slowing down the growth of the Internet in India. In particular, for many companies the ISP market is a losing proposition until long-distance and international leased-line costs come down.

While the various existing networks are essentially addressing the same market segment for Internet access and are thus in competition with one another, India's Department of Telecommunications is restricting the growth of the Internet because of its long-standing monopoly over telecommunications in the country. The ongoing telecom liberalization in India is expected to change this gradually.

■ **Vietnam** Vietnam's data communications developments closely resemble China's top-down policies. The country's IT2000 plan, issued in 1993, mandates the development of data communications networks in government services; financial, banking, and commercial services; and networking for the education and research and development communities. As part of the telecommunications reform process, a Department of Posts and Telecommunications (VNPT) subsidiary, Vietnam Data Communications (VDC) was established in 1994. VDC set up the country's first domestic and international data backbone using the X.25 protocol, which is not compatible with the WWW's protocol, Transfer Control Protocol/Internet Protocol (TCP/IP). Without reconfiguration, areas of the WWW are inaccessible.

VDC soon voiced its desire to run the Vietnamese Internet, causing a heated, and ongoing, debate between the monopoly VNPT and Vietnam's other providers of networking services. These providers include VARENET (the Vietnamese Academic and Research Network), also set up in early 1994, and an associated network named Netnam that began offering services in November of the same year as a not-for-profit data communications provider for Vietnam's non-governmental organizations. The network was able to start up with an $18,000 grant from a European aid agency. By early 1996, Netnam had about 350 users online and was reaching the point of economic viability. Netnam has moved quickly away from its original non-governmental market: roughly 60 percent of its users are corporations.

Other private network startups have followed, including Toolnet and T-net, which connect to the Internet via dial-up lines to neighboring countries like Thailand. But Vietnam's telecommunications leadership has agreed that its telecom monopoly should extend to the Internet, which needs to be monitored for security and cultural risks. The Communist Party fears that free access to information could undermine its rule and is particularly concerned about access to websites established by opposition groups overseas.

Earlier this year, Vietnam's telecommunications authority issued a "temporary regulation" allowing Vietnamese enterprises to apply for licenses to provide Internet connections and services. Under the proposed rules, all ISPs and their customers are required to register with the Directorate General of Posts and Telecommunications (DGPT) under VNPT. Service providers will have to submit technical details to the Interior Ministry so it can police the Internet. Only telecommunications companies are allowed to offer Internet services and receive subscriber revenues, and charges and access to communications will be controlled by DGPT.

The 16 clauses in the draft regulation ban the transfer of any information that "damages national security, threatens public order or does not correspond with the traditions and moral values of the Vietnamese people." The majority of players appear to believe that Internet access is vital for Vietnam's sustained economic development, though. Some observers believe that the real issue standing in the way of greater Vietnamese access to the Internet is the conflict over which governmental organization will control access to the technology and charge user fees. Hanoi is said to be closely studying the system in China, where Internet access is allowed but all users are required to register with the public security authorities.

—Peter Lovelock

Jichuan articulated a policy to unify disparate government databases using a common interface to improve access to such resources. Though he did not mention TCP/IP specifically, this platform is fast becoming the PRC government standard and, as the principal set of Internet protocols, theoretically makes eventual connection to the Internet much easier. SPC's SIC has decided to move its National Economic Information Network (CEINet) to a TCP/IP system. SIC plans to offer a range of economic information through its network, including macroeconomic data, enterprise information and products, and tourist information. Most of the information is in Chinese, but SIC is also planning to offer English services. The Ministry of Agriculture also now has its own intranet, with a home page for each department.

The Shanghai municipal government has launched the ambitious Shanghai Infoport project, designed to offer Shanghai citizens access to a variety of information in an intranet format, including nine online databases on such topics as tourism and tax information. Internet access also is a key part of this project, which city officials claim will involve an investment of $40-$50 billion over the next 10 years. Other smaller localities are initiating similar projects. In Guangdong's Dongguan, for example, the local science and technology committee has spearheaded a project to link 33 counties into an information network to exchange business data and link with the Internet to allow potential investors access to information on the counties' businesses.

In many cases, researchers and engineers are using TCP/IP to put China's substantial number of information databases online for public and commercial fee-based access. But these databases represent only a fraction of the information that China could make available. Each of the central government's many ministries has an information center, each detached from the other and serving the respective ministry exclusively. These centers store up to 70 percent of all official information available in China, but 90 percent of their collections are kept secret, according to a recent report in China's *Economic Information Daily*. As a result, only about 7 percent of China's total government data is readily available online.

As much of the Internet's content is in English, many Chinese find the language barrier a huge obstacle to taking advantage of the Internet's resources.

Currently, just 300 of 800 known databanks are available online, and less than 60 of these are configured for public access. Wu Jichuan's dictum about unification of access to databases means, however, that more of these databases will be made available via the Internet in the future. If these databases use proprietary software that is not user-friendly, however, customers are unlikely to avail themselves of these resources. The PRC government no doubt is relying on TCP/IP and the development of good browser designs to make these databanks both accessible and attractive, whether over intranets or the Internet.

Regulators keep pace

Because of the government's security concerns about the rapid spread of online access and content, central-level leaders are trying to build a regulatory structure to keep up with the Internet's explosive growth. As in other countries in the region, Chinese regulators are struggling to keep ahead of the technology curve. But because so much of the technology has been developed just in the last few years, the knowledge base of senior officials involved in regulating China's information industry tends to be limited.

The current regulatory structure grew out of attempts in the early 1990s to coordinate development of standards and competitive guidelines for China's information infrastructure. The Economic Information Joint Committee was established in 1993, ostensibly to formulate policies for the development of a national information infrastructure, but quickly became focused on the Internet. The Joint Committee was responsible for the first attempt to establish regulatory guidelines for Internet development in China. The resulting Interim Regulations for Connection of Networks to International Networks were issued in late January 1996. These regulations authorized four organizations—MPT, MEI, CAS, and SEC—to manage Internet services and, most significantly, gave MPT sole power to operate and manage international Internet links. Subsequently, the Public Security Bureau issued regulations requiring Internet users to register with public security authorities. Though these regulations apply both to Chinese citizens and foreign individuals, they do not apply to employees of foreign companies who have Internet access through their own corporate networks. As long as they are not offering commercial services in China, such corporations can continue to access the Internet through their corporate networks, rather than through one of China's four interconnecting networks.

In March 1996, the Joint Committee was elevated to the status of a "leading group" under the State Council, and renamed the Leading Group on Informatization (also known as the Steering Committee for National Information Infrastructure). This group, which consists of a high-level panel of ministerial and vice-ministerial representatives from MPT, MEI, and other government departments involved in telecommunications, as well as public security departments, is charged with drafting and implementing policies to coordinate development of China's information infrastructure, including the Internet. The Leading Group also is in charge of approvals for organizations (such as Xinhua) looking to connect their nationwide networks to the Internet. Companies wishing to become ISPs or content service providers—offering either primarily content services or dial-up (Internet or intranet) access—currently must apply to the local MPT affiliate for a license.

Most of the companies now offering services do so as "agents" (*daiban*) of MPT. In fact, the capital's MPT affiliate, Beijing Telecommunications Administration, has licensed about 25 such agents. Only 10 or so licensees are currently offering services. Agents are divided into two types: those without their own equipment and domain name, and those with their own servers and domain name. Detailed implementing regulations, probably to be issued before the end of the year, will clarify some of the areas left unaddressed in the Interim Provisions.

Steady, controlled growth

China has quickly come quite far in developing its Internet infrastructure, but significant constraints on further growth remain. Though individual use will continue to expand as the barriers of cost, language, and opportunity drop over time, estimates of the actual user base in China vary widely. MPT estimates that it has sold around 20,000 accounts—not a large number for its more than one year of operation. Of these, 60 percent are corporate, 30 percent are individual, and 10 percent are foreign accounts. The growing number of new ISPs probably now account for another 5,000-10,000 commercial subscribers.

Estimates of the number of academic users vary widely, from 50,000-400,000. Theoretically, every student on a campus linked with CERNET or CASNET has Internet access. Yet these are not paying customers, and are probably for the most part using low-bandwidth services such as e-mail. Overall, though computer penetration rates remain low, industry forecasts project steady growth as household incomes rise and the emerging Chinese middle class begins to see the advantages of computer literacy for the younger generation. Online services will clearly benefit from this trend.

But China faces other difficulties in expanding access to Internet-related services. MPT charges an exorbitant leasing fee—$2 million per year for a 2 Mbps line, which, in the United States, would be around $500,000. Competitors such as Jitong and NetChina thus will have a hard time competing in the provision of international links to the Internet, barring major changes to MPT's leased-line pricing structure. MPT itself faces a dilemma typical of many quasi-monopolies: if it allows competition by lowering prices, it risks eroding its own customer base because many, given the chance, would willingly change to providers that offer a wider range of services, such as server space for a web page and faster dial-in access. MPT would then face the problem of paying for the growth of China's international links while it loses some of the revenue base it needs to fund the expansion. MPT's strategy appears to be to license more local providers and make money on the leased-line connections. But many ISPs believe that the charges for the leased lines, and particularly the per-megabyte traffic charge, are excessive, and are trying to persuade MPT to lower the rates.

> The State Council appears at present to favor heavy regulation of the Internet service market.

According to some industry observers, MPT did not anticipate devoting such a large amount of international bandwidth to the Internet and will have to figure out when and how to obtain and pay for the increased international bandwidth needed. MPT ultimately will be responsible for making substantial investments to upgrade nodes and expand node-to-node links. Another fundamental problem appears to be that both MPT and China's Internet participants have yet to embrace the Internet culture, which includes some degree of informal cooperation among the parties involved. For example, China still lacks an informal "peering" Internet exchange regime, which would allow for more efficient routing of traffic within the various networks in China. For example, an e-mail message from a node on CERNET must traverse the Pacific Ocean twice before arriving at a ChinaNet server to be delivered to an MPT customer.

There are some recent indications that MPT and CASNET may be moving toward a peering arrangement, however. A potential roadblock to this cooperation is CASNET's intention to retain the right to issue domain names in the face of MPT opposition. Jitong, meanwhile, will probably also eventually connect with both CASNET and CERNET. The Leading Group, for its part, may also take a more active role with regard to China's dealings with international Internet bodies such as the Asia Pacific Network Information Center.

Nonetheless, major regulatory obstacles could stunt China's Internet growth for some time to come. Foreign and PRC industry participants alike favor more openness and express doubt as to whether the State Council will be able to maintain MPT's position as sole controller of international links. Indeed, evidence already exists that some large enterprises that own international private lines, by offering to share bandwidth with local Internet providers, may be circumventing the restrictions on who can provide international access. This situation is likely to become more common as other companies discover the financial benefits of sub-leasing their private lines to Internet services. However, MPT will fight hard to avoid having to cede a portion of this new and highly lucrative source of revenue to competitors, and could crack down on such activity.

It is also unlikely that the State Council will give up control over what it views as a key part of China's information infrastructure. The State Council, through the Leading Group, appears at present to favor heavy regulation of the Internet service market, as evidenced by the recent efforts to censor certain websites. The Leading Group, which is currently drafting new detailed regulations governing the Internet, can be expected to make an effort to control the negative aspects of Internet information flow while fostering an environment conducive to Internet development as a whole, and commercial usage in particular. Under this scenario, indigenous companies such as Yinhaiwei, which are creating what amounts to a China intranet, are likely to flourish.

Yinhaiwei and other new ISPs, meanwhile, are eager to work with the government in regulating the Internet. They are concerned that without some control during the Internet's infancy in China, the government could find it necessary to hinder or even quash Internet development altogether. Such an outcome is improbable, though, since companies like Yinhaiwei are more inclined to facilitate the government's regulatory efforts, and online technology could fast be beyond the reach of government regulators. Rather, Chinese and foreign Internet users and providers should count on slow, steady expansion of the Internet in China for years to come. 完

Realizing Constitutional Potential

■ Michael Dowdle

The National People's Congress is beginning to assert its constitutional authority

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China in 1996 is witnessing another revolution, this time not in regime, but in governance. Over the past decade, China's government has made a significant swing away from the personal politics that characterized Chinese governance for two millennia and is moving toward a system of "emerging constitutionalism." This is not to claim that China has become a fully constitutional state; nor is it to imply that its constitutionalism is developed equally throughout all levels and branches of government. But, at least in some important respects, constitutional responsibilities increasingly are being administered by the appropriate constitutional organ in China.

One of the most visible facets of China's emerging constitutionalism so far has been the increasing ability of the National People's Congress (NPC)—China's highest legislative and constitutional body—to assert its constitutional authority. Over the past 15 years, the NPC has evolved from a position of political irrelevance to become a dynamic force for constitutional development in China, as evidenced not only by the voting independence of the delegates but also by its newfound control over the legislative agenda and process.

The rise of the NPC appears to be due to something other than personal politics, as it transverses the tenures of three NPC Standing Committee chairmen (Peng Zhen, Wan Li, and, since 1993, Qiao Shi) and two "paramount leaders" (Deng Xiaoping and Jiang Zemin). Instead, this change appears to have been in some part propelled by appeals over the last 15 years by NPC leaders, NPC research staff, and legal scholars to China's previously hortatory constitutional principles.

The ascent of the NPC has important implications beyond China's domestic politics. The fact that the institutional structures outlined in the 1982 constitution are becoming increasingly relevant to China's decisionmaking process has important implications for how foreign governments and businesses should best interact with China's central-level decisionmaking system. The better we understand the actual dynamics behind this decisionmaking process, the better we can work with that system.

Constitutional vs. party authority

Since the founding of the PRC, the legal authority and operations of China's constitutional bodies have been subject to the political authority of the Chinese Communist Party (CCP), resulting in what are in effect parallel governing structures in China. For almost four decades after the CCP assumed power in 1949, the formal constitutional structure, when it functioned at all, did so mainly to tailor legal clothes to fit the party's political directives. Since the late 1980s, however, control over central-level constitutional operation has increasingly migrated from the CCP to the appropriate constitutional structures, particularly the NPC and State Council. The CCP still exercises significant influence over governmental operations, most visibly through its control over policy initiatives, information flows, and personnel placement. But with the exception of personnel placement, the CCP's use of these tools seems increasingly confined to criminal matters and matters perceived to be threats to its continued political hegemony.

The constitutional role and development of the NPC

China's is a parliamentary system, which, like many Western European systems, is based on the principle of parliamentary supremacy rather than the principle of separation of powers that guides the American Constitution (*see* p.34). In a parliamentary system, the national legislature typically is not only the supreme legislative body but is also the highest constitutional body, and thus is responsible for supervising the work of the other constitutional organs. Therefore, the NPC actually wears two constitutional hats. As China's highest legislative body, the NPC sets the legislative agenda and enacts and amends legislation (including the constitution). As China's highest constitutional body, it also appoints persons to and recalls persons from the major constitutional offices, reviews and comments upon State plans and national budgets, approves and comments upon annual "work reports" from other central-level bodies, and investigates and oversees the constitutional operations of the other constitutional organs.

Elected for a term of five years, the almost 3,000 delegates of the NPC meet in plenary session once a year for about three weeks. Most of the work of the NPC is performed by a 150-member Standing Committee, which convenes for about two weeks once every two months and is authorized to carry out most of the NPC's responsibilities after the plenary session's adjournment. The Standing Committee itself is headed by a Chairmen's Group (consisting of the Chairman of the NPC Standing Committee, currently Qiao Shi, some 19 vice chairpersons, and the Standing Committee secretary general), which generally meets once every two weeks.

The almost 3,000 delegates of the NPC meet in plenary session once a year.

The NPC has been the principal beneficiary of the CCP's devolution of power. No longer a rubber stamp for CCP and State Council directives, the NPC increasingly is able to realize its constitutionally granted authorities, most notably in the area of legislative drafting (*see* p.36). Although the NPC's formal constitutional responsibilities overlap significantly with those of the State Council (which has also benefited from the receding power of the CCP), the NPC's more flexible and centralized organizational structure, combined with its more prominent constitutional status, has nevertheless allowed it to develop and assert its own unique and independent institutional role within China's political environment.

For many, the most dramatic demonstration of this institutional assertiveness occurred in the April 1995 Plenary Session, where, on three different votes, unprecedented numbers of NPC delegates strayed from the Party line. The nomination of Jiang Chunyun, the protégé of PRC President and CCP General Secretary Jiang Zemin, to the position of vice premier was rejected by one-third of the delegates. The education and banking laws both were rejected by one-fourth of the delegates. This independence continued into the 1996 Plenary Session, in which over a quarter of the delegates refused to grant approval to the work reports of both the Supreme People's Court and the Supreme People's Procuratorate.

Many might question the significance of such numbers, noting that the measures still passed—and by comfortable margins, by American standards. But in many Western parliamentary systems, such severe collapse in party discipline would almost certainly bring down the ruling party through a vote of no confidence. In Great Britain, for example, no majority party since the Second World War has failed to receive at least 75 percent of the votes of its own party members in a parliamentary vote in which that party took a position. Even though the CCP does not have to worry about losing the next round of elections, such breakdowns in party discipline still call into question the strength of the CCP leadership, thus adversely affecting the political respect (or fear) afforded these leaders by others both inside and outside the CCP apparatus.

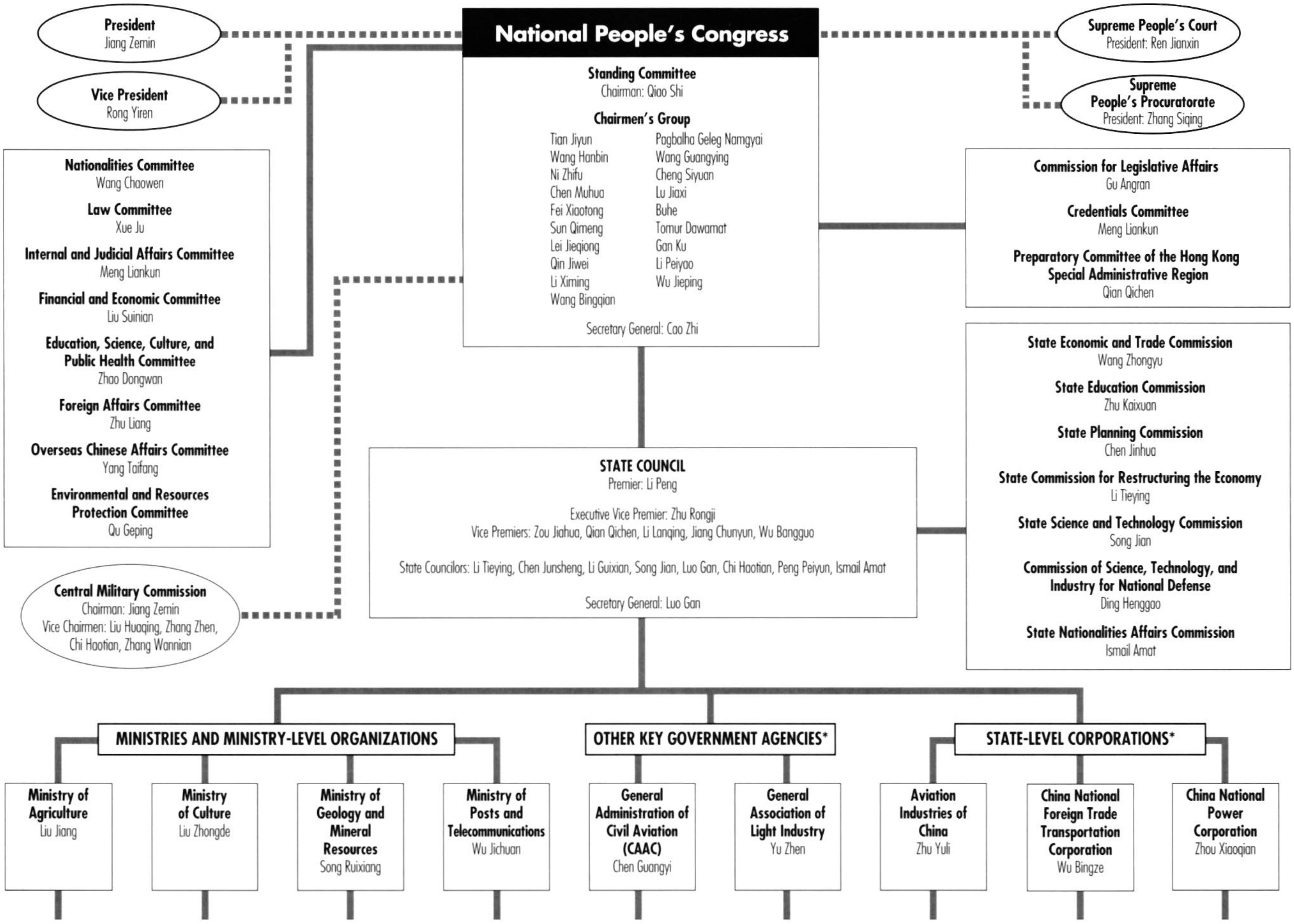
Another, perhaps less dramatic, indication of the NPC's new institutional strength has been its increasing ability to control China's legislative agenda. The full extent of the NPC's power in this area was first confirmed in 1993, with the drafting of the Company Law. Like almost every other previous piece of major legislation dealing with the economy, the Company Law was originally drafted and tendered to the NPC by the State Council. In this case, however, the NPC Standing Committee refused to consider the draft, and instead drafted and enacted its own Company Law. A similar fate befell the State Council's version of a draft Securities Law tendered to the NPC in early 1994 (although the NPC's draft of that law has yet to be considered on the Standing Committee floor).

The crown jewel of the NPC's legislative independence to date, though, has been the recently issued Amendments to the Criminal Procedure Code, passed by the 1996 Plenary Session. These amendments, which greatly liberalize criminal procedure in China, were drafted by the Standing Committee and passed by the 1996 Plenary Session in the face of concerted opposition from the Ministry of Public Security (MPS) and the Supreme People's Procuratorate. MPS in particular strongly objected to some of the amendment's more liberal provisions, including, for example, the abolition of administrative detention (a widely used procedure that allows local security organs to incarcerate a person indefinitely without trial or access to a lawyer). Even though MPS is one of the most powerful political organs in China, one which has traditionally enjoyed very strong support from the CCP leadership, the NPC's drafters were nevertheless able to overcome that ministry's opposition and basically dictate the principal terms of these amendments.

More than an experiment

Changes in China's constitutional operations have occurred in the past, so there is

CHINA'S GOVERNMENT STRUCTURE



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* These listings are not meant to be comprehensive

a temptation to dismiss the NPC's ascendence as merely another political "experiment," perhaps as something akin to the Hundred Flowers campaign of 1956-57 or the Democracy Wall movement of 1978. But these earlier experiments lasted only short periods of time and resulted in brutal political retribution for many of the participants. The strengthening of the NPC, in contrast, has been under way for more than a decade, despite the fact that, like these other movements, the NPC has on a number of occasions caused significant political embarrassment to powerful persons, such as when NPC delegates

China's Constitutional System

China's is a constitutional system which, while significantly different from that of the United States, strongly resembles those of Western Europe. In particular, China's parliamentary system, like those of many European countries, revolves around the principle of parliamentary supremacy rather than the separation of powers. Moreover, China—somewhat like France—is a unitary rather than a federal system, meaning that, unlike in the United States, provincial governments in China enjoy no independent constitutional authority, but only such authority as has been designated to them by the national government.

China's constitution divides constitutional authority among six bodies (*see* chart): the National People's Congress (NPC); the State Council; the presidency; the Supreme People's Court; the Supreme People's Procuratorate (an independent branch responsible for prosecution of criminal cases); and the Central Military Commission (CMC).

The State Council, currently headed by Premier Li Peng, is China's principal executive body, and is the constitutional organ most closely affiliated with the CCP (the State Council Standing Committee members are typically among the most influential Party members). The 83-member State Council generally meets once a month, while the 14 members of its Standing Committee meet twice weekly. The State Council has relatively broad legislative powers, similar to those enjoyed by the French cabinet, which allow it to draft and promulgate regulations on a wide variety of matters without requiring a parliamentary grant of legislative authority. Since the NPC began only recently to exercise its full range of legislative powers, State Council regulations still form the backbone of China's legal system.

With the CCP's diminished role in social and economic micromanagement, many State Council organs, including ministries and other administrative bodies, have increasingly been able to develop their regulatory functions with little CCP interference. This devolution of regulatory responsibility, however, also has resulted in increased confusion and conflict between agencies over administrative jurisdiction.

China also has a second executive institution, the presidency. In China, however, the president has traditionally been a ceremonial position (as it was in Germany's post-World War I Weimar Republic) with no real influence over political operations. However, it is interesting to note that the current president, Jiang Zemin, is concurrently the CCP general secretary, and that much of the president's formal authority—namely the power to nominate persons to high office—coincides with the CCP's de facto oversight of government personnel placement. Thus, Jiang's dual service could forebode the development of an institutional linkage between the office of the presidency and the CCP, particularly now that both the State Council and the NPC are escaping the CCP orbit. Were this linkage to develop, it would greatly increase the influence of the presidency as an independent constitutional office, perhaps resulting in a true dual-executive system similar to that called for in the French constitution.

In contrast to both the State Council and the NPC, China's judiciary has yet to benefit significantly from the CCP's receding authority. Even in Western systems, the judiciary is naturally a decentralized body, since it must rely on a diffuse string of regional and local-level courts for its effectiveness. Though the NPC elects the president of the Supreme People's Court, the emerging constitutional and professional development evident in China's central-level government has yet to permeate very far into the lower levels of governance. As a result, lower-level courts remain particularly susceptible to unconstitutional interference, especially from powerful local interests. This is severely hampering the institutional development of the judiciary as a whole, which, in turn, prevents it from assuming its proper constitutional responsibilities.

The same is true of the Supreme People's Procuratorate, whose procurator-general is elected by the NPC. Like the judiciary, the procuracy is a diffuse body that must rely on local agents for its institutional effectiveness. Moreover, prior to the promulgation of the Amendments to the Criminal Procedure Code earlier this year, most of the procuracy's principal responsibilities had been usurped by the public security organs, leaving little incentive for the procuracy to develop professionally. These new amendments, however, place significant and institutionally distinctive responsibilities on the procuracy. When and if the procuracy is able to shoulder these new responsibilities is one of the most crucial questions confronting China's legal and constitutional development.

The other major constitutional organ in China, the Central Military Commission, is responsible for directing China's armed forces and exercises its not-insignificant power primarily within and through the CCP. The NPC elects the CMC chairman, and the Standing Committee supervises CMC work. Except for its influence over the CCP, however, this commission has little apparent direct influence over the operations or development of China's other constitutional organs.

—Michael Dowdle

failed to extend overwhelming support for Jiang Chunyun. In fact, the NPC's development has not been without critics—even in the highest levels of the CCP. Both Jiang Zemin and former CCP General Secretary Zhao Ziyang before him have complained about and campaigned against this new parliamentary independence. As recently as last spring, Jiang Zemin repeated a warning, similar to one articulated eight years ago by Zhao Ziyang, against China's adopting a "Western-style parliament," but to little apparent avail.

Some analysts may also attempt to explain the new authority of the NPC as merely a temporary reflection of the immense political power of its current leader, NPC Standing Committee Chairman Qiao Shi. But the NPC's political emergence began well before Qiao Shi assumed the Standing Committee mantle in 1993. In fact, the NPC had undergone significant organizational development for more than a decade before Qiao Shi became chairman. According to studies conducted by Murray Scot Tanner of Western Michigan University's Political Science Department, by 1990—three years before Qiao Shi's affiliation with the NPC began—the NPC's permanent staff had grown to almost 2,000 from less than 12 in 1978. Concurrently, the NPC's support structure had also undergone significant professionalization. By 1993, almost all of the research staff for the Commission for Legislative Affairs (CLA, the Standing Committee's principal drafting body) were law graduates, and most NPC research staff members had advanced degrees of some sort. Also by that time, the NPC had already developed more extensive contacts within China's scholarly and professional communities than had other government bodies.

Moreover, the NPC's support services have undergone much greater rationalization and specialization than those of other constitutional organs in China (*see* chart). By 1993, the NPC was supporting three distinct and well-developed sets of legislative research services, each focusing on a different aspect of legislative development. The State Council, by contrast, has only one such body, the Bureau for Legislative Affairs. Within the NPC, CLA focuses on drafting legislation; each of the eight special standing committees works on a particular area of policy development; and the General Office Research Department concentrates on issues of legal, governmental, and constitutional structure and coordination.

These resources vest in the NPC, not in the person of Qiao Shi. As such, they will continue to benefit the NPC well after Qiao Shi's tenure ends, as will the prestige and institutional confidence that persons within the NPC say have been Qiao Shi's primary contribution to that institution. Though eligible for one more term, Qiao will likely retire after his present term expires in 1998.

Constitutional implications

But perhaps even more fascinating than the NPC's development per se is the fact that the development appears in significant part propelled by constitutional arguments. Starting in the mid-1980s, these arguments began appearing in internal CCP speeches by then-NPC Standing Committee Chairman Peng Zhen, who many within the NPC regard as the most influential figure in the legislature's development. Peng's general thesis, which has since become canon for the NPC and its scholars, consisted of the observation that the NPC is both the government's supreme constitutional body and the only representative body in a constitutional system that bases its legitimacy on its "democratic" character. Peng reasoned that the NPC is the foundation for the constitutional legitimacy of the Chinese government and, therefore, the stronger, more independent, and more assertive the NPC, the greater the legitimacy enjoyed by the government as a whole. Today, Peng's view is the centerpiece of the NPC's ongoing campaign to develop further its institutional capabilities and refine its role in China's constitutional and political operations.

Of course, this reasoning could be taken as merely more Party propaganda from the CCP leadership, were it not for the fact that during the 1980s this argument's principal audience was the CCP leadership itself. Moreover, the NPC has also directed this argument internally, consciously using it to guide the development of its own operations. Procedures developed in the late 1980s have given the NPC delegates, particularly those on the Standing Committee, and a limited but notable range of social interests, greater opportu-

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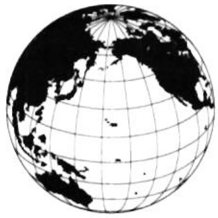

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The NPC Legislative Process

Currently, the NPC Standing Committee promulgates the overwhelming majority of the statutory legislation issued by the NPC and the rest is promulgated by the plenary session. The bases for all proposed legislation are the one- and five-year legislative plans, which, until recently, were compiled by the CCP but are now compiled by the NPC Chairmen's Group. The Standing Committee's General Office Research Department compiles both plans, which are then passed to the Standing Committee Chairmen's Group for amendment and approval.

In addition to listing pieces of legislation to be drafted, each legislative plan designates which particular governmental organ will serve as the "lead drafter" for each piece of proposed legislation. Lead drafters frequently engage other governmental organs to work with them in the drafting process, but co-drafters are not specified in the legislative plan—they participate at the discretion of the lead drafter. Generally, the lead drafter will be either the NPC Standing Committee, an NPC special standing committee (similar in function to US congressional committees), or the State Council or one of its subsidiary organs. The Supreme People's Court, the Supreme People's Procuratorate, the Central Military Commission, and individual NPC delegates also have the legal capacity to sponsor new legislation, although in practice they never do so. The CCP, though, *cannot* sponsor legislation, and on one occasion in 1993 the NPC refused to accept a draft constitutional amendment tendered directly by the CCP.

Currently, either the NPC Standing Committee or an NPC special committee serves as the lead drafter for most major pieces of proposed legislation. Legislation sponsored by the Standing Committee is drafted by the NPC's Commission for Legislative Affairs (CLA), often working with other co-drafting government organs from the State Council. When assigned responsibility for drafting legislation, CLA sets up a small "drafting group" consisting of selected CLA staff members, noted academics, and/or selected staff from other co-drafting governmental organs. The drafting group, which can consist of as few as 3-4 persons or might include whole institutions, first conducts research and, in the case of controversial pieces of legislation, may float proposals in scholarly journals or newspaper articles in an effort to garner support, before drawing up a rough draft.

CLA then circulates the draft for comment among other relevant government and Party organs, relevant semi-private interest groups, and numerous consultants drawn from related professional and academic circles. For example, a bill with specific implications for women might be given to the All-China Women's Federation for comment. CLA also convenes a series of meetings to discuss the draft with relevant special committees and governmental organs, and selected academics and professionals.

Based on input from these sources, CLA then produces the first official draft of the proposed legislation. This draft, together with a drafting report from CLA highlighting the major issues that arose in the drafting process, is then forwarded to the Chairmen's Group for approval. The Chairmen's Group may approve the draft, in which case it proceeds to the floor of the Standing Committee; send the draft back to CLA for further revision; or kill the draft by tabling it indefinitely. Thus far, this last option has only been used on proposals from the State Council or from the special standing committees, not on CLA drafts.

The drafting process for drafts submitted by the special committees or non-NPC organs is somewhat different. In this case, the Chairmen's Group typically sends the draft to CLA for independent evaluation before deciding whether to send the draft to the Standing Committee for floor debate; send it back to the lead drafter for further revision; or allow the bill to die in committee. CLA's evaluation has great influence on the NPC leadership, but the special standing committees sometimes can convince the Chairmen's Group to forward a bill to the floor of the Standing Committee despite a negative CLA evaluation. In any event, the drafters generally will hold a series of meetings with CLA to try to win its support before sending the draft to the Chairmen's Group.

If approved by the Chairmen's Group, the legislative draft proceeds to the Standing Committee floor for a series of discussions by Standing Committee members. According to NPC sources, the NPC Law Committee and the Chairmen's Group take these discussions very seriously. For example, the Standing Committee resolution approving the Three Gorges Dam project was significantly influenced by a small but determined group of opposing delegates from the Three Gorges region.

After these discussions conclude, the draft is sent to the Law Committee, along with transcripts of the Standing Committee's discussions. The Law Committee's principal responsibility is to revise legislative proposals along the lines of major points raised in Standing Committee discussions (as filtered through the Chairmen's Group).

The Law Committee revises every legislative proposal, including those originating from CLA, at least once. If significant objections remain, the bill is sent back to the Law Committee for further amendment, resulting in a second revised draft. The Standing Committee sent the Three Gorges Dam project bill back for revision four times before sending it up for vote.

The NPC Standing Committee's control over the legislative process has spawned a new form of political activity in China—lobbying. At present, CLA is the primary focus of most lobbying efforts, particularly for draft legislation that originates from non-NPC bodies. CLA seems to encourage such activity and views its own role, when reviewing the legislative drafts of others, as one of giving voice to interests that may have been overlooked by the legislation's sponsor. While government bodies, including provincial governments and ministries, conduct the most intense lobbying, professional organizations are also becoming more active. Lobbying by public interest groups has not yet become apparent, however.

—Michael Dowdle

nity to affect the legislative process. For example, the Standing Committee now vets each legislative draft twice, rather than just once, to give delegates more opportunity to influence legislative content. The NPC drafting process now also includes a series of hearings at which competing social interests can express their opinions about legislative drafts.

The NPC has consciously modified its own internal operations to conform better to its intended constitutional role, suggesting that constitutional thought has played and continues to play a significant role in the NPC's institutional development. That the two principal targets for the NPC's constitutional arguments have been the Chinese leadership and the NPC itself also suggests that constitutional arguments can now significantly affect the highest levels of China's political behavior. Together, these two points indicate that foreign governments and companies can no longer ignore the constitutional aspects of China's government.

Toward constitutionalism

Of course, there is no doubt that most of China's governance is still "business as usual"—overt political dissent by ordinary citizens is still repressed, and personal rights and freedoms, including those guaranteed in the constitution, receive little apparent respect. Nevertheless, the development of the NPC suggests a fundamental shift in the *way* that China performs "business as usual." In particular, it suggests that more and more activities in China take place not because of some singular, individual political will, but instead are guided by institutional—and even sometimes constitutional—dynamics.

Constitutionalism may be the safest form of government, but it is not necessarily the most efficient. Foreign firms, for example, may sometimes find that China's developing constitutional culture does not tend to their immediate interests. In many ways, it is much easier to understand and deal with Party leaders than with the complex dynamics and systemic inadequacies of a developing constitutional system.

For example, in the past, when US businesses discovered violations of their intellectual property rights (IPR) in China, the US government could simply demand that China's "leaders" use their authority to close the offending factories. But in a constitutional system, even an emergent one like China's, such violations do not necessarily reflect shortfalls on the part of the central leadership. The problems are likely the result of systemic failings within China's emerging constitutional structure: not enough money to regulate the explosion of emerging private and local interests; not enough experience with administrative enforcement in a judicially overseen regulatory environment; and/or severely underdeveloped local judiciaries under the influence of powerful local interests. Moreover, foreign demands may fall outside of the constitutional jurisdiction of the Chinese leadership. In China, as in the United States, ultimate constitutional authority to close a factory permanently vests in the judiciary—not in the executive, and not in a political party.

Even if the leaders with whom we deal lack the necessary constitutional authority, they nevertheless possess political clout sufficient to close down a factory, regardless of any intervening constitutional niceties. But if our problems are indeed primarily due to systemic difficulties arising out of China's fledgling constitutional operations, rather than to simple bad faith on the part of those leaders with whom we deal—a possibility few Americans have stopped to consider—what are the implications of our demands? Can we honestly expect China to become a law-abiding member of the international community, while at the same time demanding that its leaders ignore its own constitutional framework merely because our interests are not being adequately served?

We need to begin taking China's constitutional system and operations into account when plotting our negotiations and relations with China. To the extent that IPR or any other injury to American interests might be the result of dysfunctional rather than non-functional constitutional processes, a more appropriate response would be to work with and through the constitutional system, not against it. If the problem is lack of appropriate enforcement experience, for example, then we should seek to assist China in developing such experience. If the problem is one of local interests controlling a weak local court, then we should find ways to help China's judicial system develop means for combating local protectionism. Of course, such efforts will take time—they will not afford the immediate financial gratification of direct Party intervention. And there is a price to pay for such patience. But the return would be the increasing solidification of constitutionalism in China—a move that will result ultimately in a fairer and more stable economic and political environment. It would appear to be a prudent investment. 完

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People, Politics, and Profits

■ Bryan Batson

Hong Kong's post-1997 dynamism depends largely on its workers

Hong Kong government promotional materials proudly proclaim that "an industrious population and one of the world's finest deep-water harbours" are the tiny territory's only natural resources. Nonetheless, Hong Kong has transformed itself from a lonely colonial outpost to one of the world's most vibrant and competitive economies. Its achievements in the global business arena are many and laudable: the world's fifth-largest financial center; seventh-largest foreign exchange reserves; eighth-largest trading economy; and busiest container port. And, at $25,300 per capita, income in Hong Kong surpasses that of either Britain or Canada—not bad for a territory of just over 1,000 sq km.

The intelligence, elbow grease, and entrepreneurial enthusiasm of Hong Kong's populace—a vibrant mix of people from both East and West—have made the territory the prosperous place it is today. The Institute for Management Development proclaimed Hong Kong the world's third most competitive economy in 1996, ranking behind only the United States and Singapore. To a large degree, it was the rule of law imposed by the British administration that provided the framework for the territory's success. Hong Kong could never have become such a truly international city without a transparent business environment. Will it be able to retain the companies that make it thrive?

With all eyes on Hong Kong's political transformation from a British colony to a special administrative region (SAR) of China next July, public confidence in Hong Kong's ability to remain free of corruption and retain the rule of law is at a low point. But the political changeover may not pose as serious a threat to Hong Kong's global commercial role as could rising costs and the changing skill needs of global business. Whether Hong Kong can remain a competitive regional economic and financial center into the 21st century depends largely on its ability to attract and retain skilled executives. Both foreign companies already in Hong Kong and those contemplating investments there must be concerned with human resources, since this, simply, is what makes Hong Kong work.

Adaptability, though, is another of Hong Kong's strengths. In the 1950s, when the Communists failed to find a place in the new socialist order for Shanghai textile manufacturers, Hong Kong business leaders gladly received these refugees. The entrepot trade that had sustained the colony was in rapid decline at that time because of the United Nations embargo on the export of strategic commodities to China imposed during the Korean War. With little left of their previous wealth, these mainland entrepreneurs helped transform Hong Kong into a low-cost, labor-intensive production base for textile and electronics exports. According

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to Hong Kong government figures, the value of Hong Kong's exports grew from HK$3.7 million ($479,000) in 1950 to HK$232 million ($30 million) in 1995.

When China opened its doors to the outside world in the late 1970s, these former Shanghai industrialists, successful once more, began investing much of their new wealth in China's Pearl River delta. In contrast to the other "little dragons" of Asia—Taiwan, South Korea, and Singapore—that responded to rising wage pressures by moving into higher value-added production, Hong Kong was able to stick with its successful formula of low-cost, labor-intensive production by expanding its manufacturing base into southern China. This strategy worked extremely well: Hong Kong's GNP increased nearly fivefold from 1984-96. Hong Kong firms now employ roughly 5 million people in China, mainly low-skilled laborers.

Hong Kong's professionals

With much of the production of its firms now occurring on the PRC side of the border, Hong Kong once again thrives as an entrepot, mediating a large portion of China's participation in the global economy. Hong Kong handles half of the mainland's exports, while roughly 60 percent of all foreign direct investment in China flows through Hong Kong. And, while many labor-intensive industries have shifted into South China, Hong Kong itself has retained higher value-added functions such as procurement, product design, quality control, marketing, and management. As a recent Harvard Business School study notes, Hong Kong has become an information- and knowledge-based economy. Hong Kong government sources indicate that the service sector accounts for roughly 83 percent of the territory's GNP.

Yet the skill levels of the Hong Kong labor force may not be keeping pace with the needs of an increasingly service-based economy. As Ian Perkin, chief economist with the Hong Kong General Chamber of Commerce, observes, "There has been a huge influx of expatriates into Hong Kong because the demand is so great in the service sectors." Though Hong Kong is not short of schools—the colony boasts seven public universities—managers at some Western firms believe the Hong Kong education system fails to develop the analytical skills of its graduates. Memorizing an essay from a test preparation book rather than writing an original composition for an exam is not uncommon among Hong Kong students, for example.

Many Hong Kong citizens send their children abroad to university—in 1995, over 13,000 students left to attend universities in Australia, Britain, Canada, and the United States. But, according to some human resources professionals in Hong Kong, many of those who study abroad do not return with the necessary language and other skills. In many cases, it seems, Hong Kong students go in groups to attend foreign universities, spending little time developing an awareness of Western business culture or practicing their English language skills. The lower level of English language skills in Hong Kong contrasts sharply with the situation in Singapore, which boasts excellent English language skills among its populace and competes directly with Hong Kong as a site for regional headquarters and international financial services. "This is a serious issue going forward for maintaining Hong Kong's competitive edge," notes Richard Margolis, first vice president for equity research for Merrill Lynch Hong Kong.

The result is a lack of home-grown managers in Hong Kong. Douglas R. Stanton, director of human resources consulting for Towers Perrin in Hong Kong, describes the typical situation US companies face in Hong Kong. Seeking to hire a general manager to sell its product in South China, the company looks for someone with proficiency in Cantonese, Mandarin, and English; preferably a US education; a graduate degree; and solid experience. "People with those qualifications can simply name their price. There just aren't enough of them," states Stanton (*see The CBR*, May-June 1996, p.26).

And naming their prices they are: multilingual, Western-educated managers can easily command base salaries of $250,000 in Hong Kong. While only a manager of a fairly large operation in the United States might earn such a salary, in Hong Kong this level is the norm for someone managing sales—not manufacturing—operations of about $10 million and a staff of 20. Mark Nechita, director of human resources-Asia Pacific for FMC Corp. and chair of the American Chamber of Commerce (AmCham) Human Resources Committee in Hong Kong, worries that wage costs will drive business out of Hong Kong to more competitive locations (*see* chart). "Wages have increased at least by half, if not more, every five years in Hong Kong...It's a cost of doing business, but you have to reach some sort of equilibrium. [Otherwise] businesses start to vote with their feet," warns Nechita.

Hiring expats...

With wages increasing 10-13 percent a year, it is little wonder that a recent AmCham survey shows US companies find the relatively high costs of doing business to be one of the most unsatisfactory aspects of Hong Kong's commercial climate. Though many companies in Hong Kong would prefer to keep costs down by hiring more people from the mainland, the Hong Kong government rarely approves long-term work visas for PRC citizens. And

Comparison of Salary Packages in Asia, April 1996

	Basic Package Salary Range			
	Hong Kong	Shanghai	Singapore	Taipei
Expatriate financial manager	$271,774–$402,484	$308,304–$429,690	$224,609–$321,733	$211,840–$251,427
Local sales manager	$89,297–$110,004	$6,293–$9,469	$89,489–$138,494	$61,519–$78,014
Senior secretary	$25,883–$30,575	$4,746–$5,684	$27,344–$32,670	$17,475–$21,157

SOURCE: Towers Perrin/Conatus
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NOTE: All figures are US dollars.

expats with the necessary skills command large benefits and salary packages. Thus far, the market has resisted any downward pressure on expatriate compensation.

While employee costs in Hong Kong are roughly comparable to those in Singapore, Singapore does not have to overcome visions of impending doom to attract business. With such keen competition for job candidates with the right skill mix, it is not unusual to meet people in Hong Kong who have held five jobs in the last 10 years. Because of this situation, retention tools are particularly important for foreign companies. According to Stanton, top managers can easily be poached, a process that only adds to wage inflation. Managers often are readily lured by competitors offering significantly higher wages—executives routinely receive offers of salary increases of about 25 percent to induce them to switch jobs, Stanton comments.

Retaining top workers is crucial to maintaining a competitive edge in Hong Kong, but its new mandatory pension fund may not make employee retention any easier. To provide security to Hong Kong workers, the government is planning to enact a Mandatory Provident Fund (MPF) Schemes Ordinance in late 1997. The scheme is expected to apply to all employees between the ages of 18 and 65 and will require the employer and the employee to contribute 5 percent of the employee's monthly cash income to the pension fund. An employee earning less than HK$4,000 ($517) will reportedly not be required to contribute (though the employer is), while contributions in excess of HK$20,000 ($2,587) per month will be non-mandatory.

While the MPF is good news for Hong Kong pension fund managers—it is expected to generate between $3.9 billion-$5.2 billion per year in new investment funds—many multinational companies in Hong Kong are less than pleased. The problem is not that the MPF will impose an added cost to doing business—most multinational companies already pay more in benefits than the government minimum—rather, firms feel the MPF contributes further to job mobility, as the accrued benefits are completely portable from job to job. Explains FMC's Nechita, "We have certain vesting points for our schemes, an important retention tool in a place like Hong Kong. The MPF undermines the vesting component." While companies can dictate vesting points above the mandatory government scheme that are not portable, such benefit changes make their funds more complex and costly to administer.

...or hiring Chinese

Poaching of highly qualified expatriate executives will no doubt remain a human resources problem long past 1997, but, in the short term, many firms are likely to hire more Chinese executives. Paul Cheng, chairman of Inchcape Pacific and NM Rothschild Hong Kong, notes that Hong Kong firms probably will go through a period of hiring fewer expatriates in 1997, 1998, and, possibly, into 1999, but "once we pass through this highly emotionally charged period, you will see a resurgence of a more balanced way of looking at things." With the British governing establishment moving out and PRC administrators moving in, almost all the top civil service positions are now filled by Hong Kong Chinese. "The British hongs were 'the Establishment' under British colonial rule," but those days are over, says Cheng. "The shift of influence is toward local groups like Hutchison and CITIC Pacific, the mainland Chinese company. They will become 'the Establishment.'"

Thus, the employee of choice for top positions in more and more companies clearly is someone who can help Hong Kong-based companies solidify their contacts with China: a well-educated Chinese with superb management skills who speaks excellent English and has business connections in the PRC. As Perkin and other economists in the territory point out, Hong Kong has become closely linked to the Chinese economy and Hong Kong companies are fast expanding their operations in China. Says Perkin, "Hong Kong companies used to say that they were not going to put more than 5 percent of their assets in China. That's gone by the boards. Many now have 10-15 percent of their assets in China. Some even have as much as 25 percent." All this increases Hong Kong's exposure to sudden policy shifts on the mainland and the vagaries of China's volatile economic cycles—and increases businesses' need for people with China savvy.

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The nationality question

For the transition, though, many issues related to personnel and staffing have yet to be resolved. Though Hong Kong clearly needs to attract and retain qualified professionals, including expatriates and PRC citizens, to maintain its competitive edge, residency and immigration rules for the future SAR remain unclear. Most of the changes stem from the fact that China's Nationality Law, which specifically prohibits dual nationality, will apply to Hong Kong after July 1, 1997. For the bulk of Hong Kong's Chinese residents, their right of abode (ROA)—the right to enter and remain in Hong Kong without any condition or time limit imposed, the right to vote and occupy certain political and civil service appointments, and freedom from deportation—is secure. PRC citizens residing in Hong Kong at the time of the transition also will have ROA in Hong Kong and will be able to obtain a SAR passport.

The area of uncertainty concerns the roughly 700,000 "non-Chinese" nationals who have ROA in another country. They include "returning emigrants" as well as "genuine expatriates" who are long-established residents of Hong Kong. Beijing's concept of how the Basic Law provision on ROA for "non-Chinese nationals" would be applied currently is under negotiation, but reportedly involves several criteria. Returning emigrants (those who were formerly Hong Kong permanent residents) who have acquired foreign nationality status and return to settle in Hong Kong *before* July 1, 1997, will be eligible to claim both ROA and their foreign nationality status. But to retain access to foreign consular protection in Hong Kong and China, these people will have to declare their foreign nationality by registering at the Immigration Department. By failing to declare a foreign nationality, returning emigrants would be considered Chinese nationals and would lose their right to foreign consular protection.

Returning emigrants who have acquired foreign nationality and return to Hong Kong *after* July 1, 1997, likely will face a choice: they may elect not to register as foreign nationals and thereby retain ROA, or they can declare themselves to be foreign nationals (thus retaining foreign consular protection) and thereby forfeit ROA. As the situation currently stands, by declaring themselves foreign nationals, emigrants who return after July 1, 1997, would have to live in Hong Kong for seven more years to claim ROA. In the meantime, they would be given an appropriate immigration status that would allow them to live and work freely in Hong Kong, but they will need to obtain work visas.

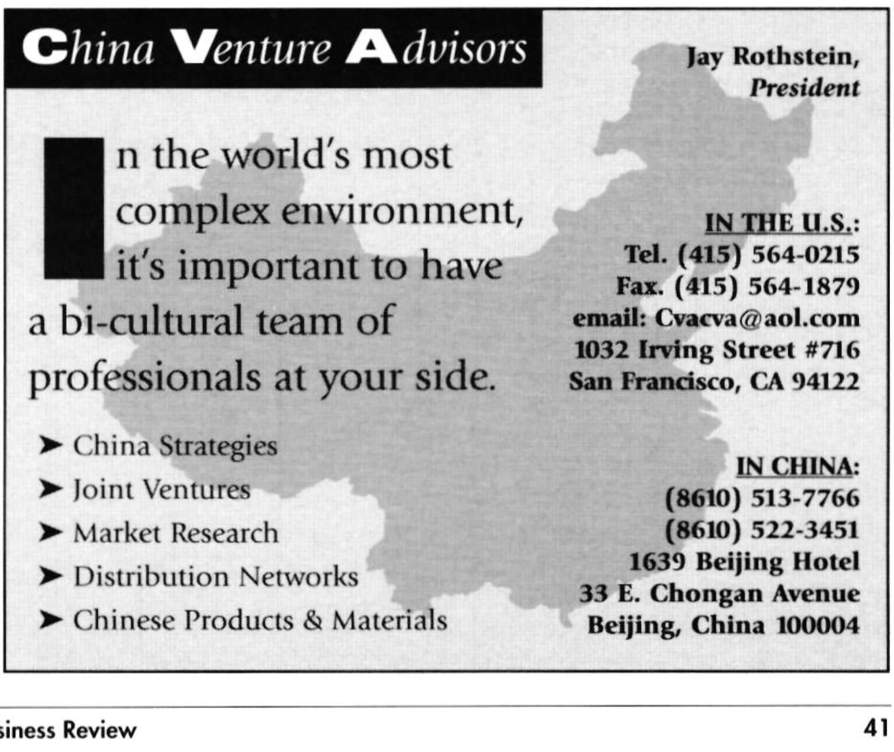
Non-Chinese foreigners likely will have to follow the same procedures they do currently, but it is possible that they will be able to obtain ROA, something non-Chinese foreigners currently cannot obtain, if they can show that they have resided in Hong Kong for seven years immediately before applying for ROA and declare Hong Kong to be their place of permanent residence.

Mutual faith

The right of abode issue, of course, has implications for businesses in Hong Kong, since a major human resource concern is that abrupt changes in Beijing's policies regarding the Hong Kong SAR could prompt an exodus of those who hold foreign passports, leaving a much smaller pool of skilled workers. But according to the most recent AmCham survey in Hong Kong, US companies are more confident about Hong Kong's business prospects this year than they have been in several previous years: 84 percent of the respondents with regional headquarters in Hong Kong indicated that they will either maintain or increase the size of their offices there over the coming year.

Nonetheless, stiff competition from other locales serving the China market—Singapore, Taiwan, and, to some extent, Shanghai and Beijing—is on the rise. All of these competitors are increasingly capable of supplying the capital and management that China needs. Hong Kong lies at a critical juncture, and its people must address the most immediate problems—competitive skills and competitive costs—to continue to participate in the PRC economy's expansion. If these problems are not resolved, the perceived political threat to Hong Kong from China will matter little.

As usual, Hong Kong appears to be taking the bull by the horns. The Hong Kong government has commissioned studies from world-class business schools on the territory's competitive position. Local businesspeople also have formed commissions and organizations dedicated to investigating ways to keep Hong Kong vibrant and competitive. If Hong Kong can improve its skill base to meet the needs of the China market, it will have the strength to meet the challenges of the global market head on. 完



Home Away from Home

■ Kirsten A. Sylvester

From Beijing to Beihai, hotels are multiplying in China

With visitor arrivals in China up 13.6 percent in 1995 and foreign business travel to China showing little evidence of leveling off, international hotel developers and operators have not lacked incentive to keep their China development plans on the front burner. Though the market for feeding and housing travelers in some cities, including Beijing, Guangzhou, and Xian, appears somewhat saturated at present, many international hotel companies have set their sights further afield and are forging ahead with ambitious expansion plans.

Between 1985-95, the number of foreign tourist arrivals to China increased 330 percent. In 1995, 5.9 million foreigners and 40.5 million other visitors (a category which includes overseas Chinese and people from Hong Kong, Macao, and Taiwan) entered China, generating roughly $8.7 billion in foreign currency earnings. The country was ranked sixth worldwide as a holiday destination in 1995, according to China National Tourism Administration (CNTA), and Beijing hopes that the "Visit China '97" campaign will further boost the number of overseas visitors.

Travel-related revenues continued to rise in 1995: CNTA recorded a 16 percent jump in aggregate revenues for tourist hotels, with total receipts amounting to ¥63.6 billion ($7.6 billion). For the Ninth Five-Year Plan (FYP, 1996-2000), Beijing projects an increase of 3-4 percent in annual overseas visitor arrivals. China's more than 600 joint-venture hotels hope that this steady growth in arrivals will boost their revenues. Business travelers, in particular, will likely continue to comprise the lion's share of customers at China's joint-venture hotels. *The Wall Street Journal* has reported that in the first nine months of 1996, business travel to China was up 30 percent over the same period in 1995, suggesting a strong business climate that will continue to fill rooms at these hotels.

At the same time, hotel developers in China have been keeping a watchful eye on the increasing numbers of domestic Chinese travelers. In 1995, domestic tourism was up 20 percent over the previous year and an estimated 629 million PRC travelers spent a total of ¥137.6 million ($16.5 million), according to CNTA. During the 9th FYP, the government projects domestic tourism to increase 8-10 percent annually.

The saturation of five-star hotels in major cities, together with projected increases in domestic travel, suggest that China's hotel market appears to be heading into a second stage of development aimed at cultivating business in secondary cities. Many international hotel investors and management executives have been doing some traveling around China themselves, scouting out new locations for hotels. And where previously foreign visitors to China could choose between a

■ **Kirsten A. Sylvester is associate editor of *The CBR*.**

lavish four- or five-star joint-venture hotel or an inexpensive, domestic Chinese establishment with few, if any, Western-style amenities, many hotel chains now are attempting to fill this yawning gap by opening two- and three-star facilities.

Tracking the business traveler

Industrial metropolises like Wuhan, Shenyang, and Changchun may not be featured in every sightseeing guide to China, but foreign businesspeople have already beaten paths to these and other inland cities to pursue trade and investment opportunities (*see The CBR*, January-February 1995, p.19). And companies like Hong Kong-based Shangri-La Hotels & Resorts have not been far behind. Under Malaysian trading magnate Robert Kuok's leadership and the abundant finances of the Kuok Group of Hotels, Shangri-La aims to have 14 hotels in operation in China by 1998 and 20 by 2000.

Shangri-La has targeted the industrial northeast, where auto manufacturing and heavy industry dominate, as the site for several new properties in the next three years. The company recently cut the ribbon on a five-star hotel in Changchun, Liaoning Province, the city's first joint-venture hotel; opened a three-star hotel in Shenyang, Liaoning Province; and is preparing to open five-star properties next year in Qingdao, Shandong Province, and Dalian, Liaoning Province. Further south, the company also has a new five-star facility in Beihai, a popular beach resort and a one-hour flight from Hong Kong, that caters to business and leisure travelers alike, and will open a 856-room, $111 million property in Wuhan, in central Hubei Province, next year.

Holiday Inn International, which finds 70 percent of its guests are business travelers, has been on the forefront of hoteliers' push into the interior. The company opened a three-star property in Lhasa in 1986, and four-star hotels in Chongqing and Urumqi in 1989 and 1992, respectively. With a five-star property already operating in Chengdu, the capital of Sichuan Province, the company recently announced a new contract to open a second hotel there in 1997. The company now has 18 China properties.

New World Hotels International, which also manages Ramada China hotels, has ventured into far-flung provinces, too.

> Hoteliers are turning their attention to economy-class accommodations to serve both foreign and domestic travelers in China.

New World has operated a 252-room hotel in Shenyang since 1994, and last year set up a 329-room hotel in Harbin. Some of New World's other locations include Hangzhou, Xian, and Tianjin.

Accor Asia Pacific, a Sydney, Australia-based firm with financial ties and rights to the lodging brands of France's Accor S.A., recently announced its plan to open four-star hotels in Hefei, Anhui Province; Jinan, Shandong Province; Hangzhou, Zhejiang Province; and Beijing.

In southwestern China, the German hotel management company Kempinski Hotels S.A., owned by Thailand's Dusit Thani Group, is looking to operate a five-star property in Kunming, Yunnan Province, a city where Thai businesspeople are frequent visitors. Despite the remote location, Kunming is also the site of a planned Club Med, to be part of a proposed holiday village built by a consortium led by the Singapore firm Straits Steamship Land Ltd. The 400-bed vacation village would be part of the larger Spring City resort that the consortium is developing, which, upon completion, will feature two 18-hole golf courses, three hotels, and condominium rental units.

ITT Sheraton Asia Pacific Corp., which now operates five hotels in China, expects to operate 20 hotels in the country by 2000. ITT has plans already in the works for new facilities in Dongguan and Guangzhou in Guangdong Province; Shenyang; and Suzhou and Wuxi in Jiangsu Province. Hilton International, currently with two China hotels, recently announced plans to develop 20 five-star hotels in China over the next 20 years.

Settling in

In addition to expanding geographically, hotel companies are also broadening their China product lines, developing economy-class accommodations to serve both foreign and domestic Chinese travelers. Though Accor operates five types of hotels worldwide catering to different market sectors—Sofitel (deluxe), Novotel (first-class), Mercure (mid-market), Ibis (economy), and Formula 1 (budget)—its push in the next several years will be in the middle range of the market. Of the company's four existing China ventures, three are under the four-star Novotel label, and one is a five-star Sofitel. But Accor Asia-Pacific Chief Executive for China, Hong Kong, Taiwan, and the Philippines Patrick Basset has stated that developing mid-scale hotels aimed at domestic travelers under the two-star Ibis and three-star Mercure brands, with room rates between $30-$35 per night, will be the company's focus in China in the next two to three years. According to Basset, the company's strategy of marketing a European product to the Asian hotel market has changed—the new focus will be adapting the product to local needs.

Like Accor, Intercontinental Hotels & Resorts appears to be changing its China

Top PRC Destinations for Foreigners in 1995

	Number of foreign tourists
Beijing	1,665,246
Dalian	105,575
Guangzhou	489,599
Guilin	285,025
Hangzhou	249,418
Kunming	304,616
Nanjing	127,680
Qingdao	130,178
Shanghai	1,075,439
Shenzhen	353,152
Suzhou	182,679
Xiamen	114,928
Xian	383,242
Yanbian	103,926

SOURCE: *The Yearbook of China Tourism Statistics 1996*, China National Tourism Administration

NOTE: "Foreign tourists" excludes overseas Chinese (those holding PRC passports who live abroad), and people from Hong Kong, Macao, and Taiwan.

strategy. Having recently announced a joint venture with Hong Kong-based Dynasty Group, the company plans to develop the mid-market Forum line in China, along with the higher-scale Dynasty and Intercontinental lines. Intercontinental already operates the Forum Hotel in Shenzhen and a five-star property in Harbin. Joint-venture company executives have stated that they expect Forum hotels to be established at a faster rate than the luxury lines.

Shangri-La, which offered only luxury properties in China up until two years ago, realized that not every business traveler to China required the abundant amenities of these hotels and introduced its mid-market "Trader's" brand to China in 1994, when Trader's Hotel Beijing opened. The immediate success of that property prompted an expansion, scheduled for completion by the end of this year, to almost double the size of the hotel to 567 rooms. The Shenyang property that opened this year is the company's second Trader's hotel in China.

Out on a limb

As the joint-venture hotel "pie" expands and the Chinese economy cools down from the high growth rates experienced in the early 1990s, nationwide occupancy rates appear to have reached a plateau. Indeed, Holiday Inn executives expect the nationwide occupancy rate for the company's properties, most of which fall in the three- and four-star categories, to be about 75 percent, comparable to last year's rate. In Beijing and Shanghai, several five-star hotel executives stated that year-end occupancy rates at their facilities will come in only about 5-10 percent higher than last year, and prices have tended to remain constant.

The 26 percent increase in the number of two-, three-, four- and five-star hotels in China in 1995 had many international hotel firms eager to see how profitable the hinterland would be for new properties. So far, success seems to vary from region to region. In Wuhan, home to numerous foreign ventures in the automotive, steel, and brewing industries, Ramada Hotel Wuhan General Manager David Yip expects year-end average occupancy at his hotel to reach 80 percent—a 15 percent increase over 1995. The hotel, with a customer mix of 95 percent corporate and 5 percent leisure travelers, has room rates ($79) that are about 10 percent higher than last year's.

Many existing five-star hotels in the major cities have been adding new flourishes.

For the four joint-venture hotels in the far northern city of Harbin, the story is quite different. The hotels have a combined total of 850 rooms, but overall occupancy has been only about 50 percent this year, according to Norman Ng, general manager of New World's Bei Fang Hotel. And occupancy levels could drop further next year, as four new hotels are due to be completed that will add 1,000 rooms. New World's Bei Fang Hotel, currently offering a rate of $58 per night, expects to end the year with a 40 percent average occupancy rate.

More than a bed

While international hotel investors expand their China portfolios, many existing five-star hotels in the major cities have been adding new flourishes to attract deep-pocketed travelers—and keep profits healthy. The standards for China's luxury hotels are already very high: most have at least 5—and some as many as 12—different restaurants serving various types of Asian and Western cuisine; fully equipped health clubs; business centers complete with secretarial services and computer, fax, and Internet access; and at least one "executive" floor with a private check-in desk, business lounge and services, and private meeting rooms. While many five-star hotels are expanding their convention and exhibition spaces, others are attempting to attract leisure travelers and local residents. Some Beijing hotels make a special effort to attract locally based expatriates and their Chinese colleagues by offering high tea with lobby performances by string orchestras.

In 1995, Beijing had 13 star-rated hotels, including many of the best-known foreign hotel names. Shangri-La's China World Hotel, situated in the heart of Beijing's business district and alongside the China World Trade Center's 38-story office tower, offers 5,135 sq m of conference and banquet space, with a conference hall that accommodates up to 2,000 people. The 715-room Shangri-La Beijing, meanwhile, has sought to market itself as a prime spot for conventions as well, since its location in Beijing's western suburbs means visitors do not have to contend with the congestion and traffic of the downtown area. Through an arrangement with Global Vision Satellite Network, the hotel now offers two-way satellite video teleconferencing.

The Kempinski Hotel Beijing Lufthansa Center, in eastern Beijing, has high hopes that the new embassies going up in its neighborhood will boost the number of foreign business and government travelers. The 530-room hotel recently added four "diplomatic suites," which include a combined parlor and dining room and two bedrooms. The combination of a separately managed business center and separate meeting rooms available free of charge for "executive floor" guests is meant to entice the business traveler who does not require permanent office space, but does need short-term office facilities and business services. The hotel recently opened its own brewery on the premises in an attempt to capitalize on the growing fondness among expatriates for "home-brewed" beer. The center is also counting on its adjoining You Yi Shopping City department store to attract large numbers of expatriate and Chinese shoppers. Kempinski General Manager Robert Barsby hopes that the hotel complex will become a "nerve center" for the Chaoyang district.

In an attempt to attract more leisure travelers, the China World, the Palace Hotel, the Great Wall Sheraton, and many others have developed "theme" package parties. At the Great Wall Sheraton, for example, a group of guests can have "Dinner with the Emperor," complete with waiters dressed in Qing dynasty costumes, tables set with period silver and porcelain, a traditional eight-piece ensemble, and a banquet menu featuring food fit for—who else—an emperor of China.

Hot—and not so hot

Shanghai, currently with seven five-star properties, remains a bright light for the hospitality industry. As the city attempts to regain its former prominence as an Asian financial center and an entire district is being constructed from the ground up in the Shanghai Pudong New Area, it perhaps is not surprising that hotel developers continue to devote resources to Shanghai investments. Local government offices, the Shanghai Stock Exchange, the Shanghai Cereal & Oil Exchange, and the Shanghai Real Estate Trading Market are all in the process of moving their offices across the Huangpu River to Pudong.

Among the hotels that already have staked out ground in Pudong, Shangri-La will open a five-star hotel there in 1998. Holiday Inn is also scheduled to open a luxury property and Accor Asia Pacific currently is negotiating to open a two-star Ibis hotel in the zone. Hyatt International's Grand Hyatt, which will occupy the top 36 floors of the 88-story Jin Mao Tower in Pudong, will be the highest hotel in the world when it opens in 1998. The four-star, $55 million New Asia Tomson Hotel, a joint venture between Shanghai New Asia (Group) Co. and Tomson (China) Co. of Hong Kong, was recently completed in Pudong.

By contrast, Guangzhou hotel managers are having to adapt to new market conditions such as an increased number of direct air flights between Hong Kong and other mainland destinations. Shenzhen's *Securities Times* reports that between 1990-95, 83 hotels serving foreign guests opened in the city. But with flat occupancy rates in recent years, no new five-star properties are likely to go up before 1999. New World's China Hotel has moved to increase the hotel's meetings and exhibition space by 35 percent this year and hopes thereby to bolster its standing as a convention venue. The hotel also received a cash injection this year of $1 billion for renovations and gained a new tenant in the Hard Rock Cafe, which property investors hope will attract more customers to the hotel's other restaurants and retail shops.

Local appeal

Five-star glitz and glitter aside, most international hotel developers recognize that budget-minded domestic travelers will be a critical part of the PRC hotel industry. CNTA, eager to keep its own slice of the market, recently approved 11 new Chinese hotel management companies and announced plans to build 1,000 hotels over the next five years. With the establishment in 1995 of a five-day work week, many joint-venture hotels have already started to offer weekend packages to entice local customers to sample the amenities available at their establishments. Such packages typically include a one-night stay for a family of three, a buffet dinner, breakfast, and lunch. As these offers become more popular, international hotel executives expect the standards of Chinese travelers to rise, which should prove an advantage when competing with locally managed hotels. Five-star properties may put a company's name in lights, but international hotel executives are realizing that the mid-range market offers not only faster investment returns, but also the key to long-term success in China. 完

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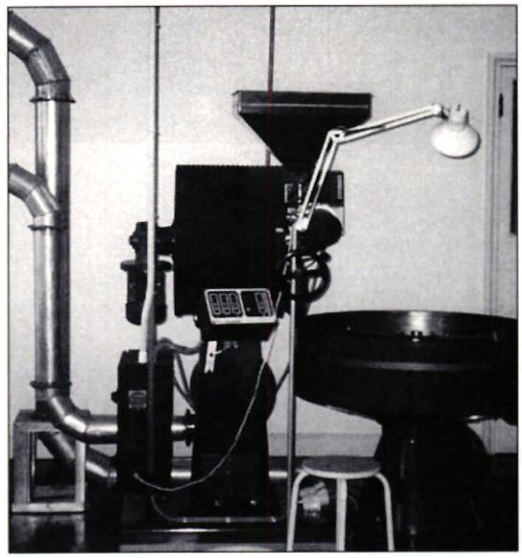
All the Coffee In China

■ Anne Stevenson-Yang



Beijing's Arabica Roasters sets out to create a market

At the top of a narrow, icy flight of metal stairs clinging to the side of one of the drafty buildings making up the Western Suburbs Dairy Products Factory complex are two rooms thick with the odor of roasting coffee that represent the life savings—and a little more—of two young Americans and an Australian who have made Beijing their home. Licensed in October 1994 as a wholly foreign-owned enterprise, Arabica Roasters is one of a few small, entrepreneurial companies in China aiming to serve the expatriate community.

Arabica was formed to fill a void in Beijing's daily life: good coffee. China places import tariffs of 40 percent on unroasted and 60 percent on roasted coffee, plus a 17 percent value-added tax. Its own domestic production—principally from Yunnan Province, though some coffee is grown in Hainan Province as well—is both meager and of poor quality. Fresh coffee, virtually unobtainable in the past, now sells in supermarkets catering to foreigners for anywhere between about $6.50 per pound for a standard American blend like Maxwell House to $20 per pound for high-end coffee. While instant coffee has been widely available in China since the mid-1980s, until Arabica and a handful of other coffee companies arrived in Beijing, fresh coffee outside the five-star hotels was rarer than a good Brie.

Creating a market

Believing they could capitalize on the need for premium fresh coffee in Beijing, Ronald Thompson and Stuart Eunson, former roommates at Colby College, decided to go into the coffee business in early 1994. Thompson left his job as a legal assistant at Skadden, Arps, Slate, Meagher & Flom, and Eunson quit his position teaching English to hotel employees in Beijing. They teamed up with Richard Wilson, 34, an Australian plumber and electrician who had developed an interest in the roasting business. Wilson's fascination with China, sparked by meeting Chinese scientists while doing plumbing work in Antarctica, had led him to Beijing to study Chinese. The three used their combined savings of $75,000, along with an additional $25,000 from parents and friends, to rent space and buy equipment.

Wilson, Thompson, and Eunson start each day at the back of the roasting room pressing boiling water through a loam of Indonesian Sumatran Mandheling or Puerto Rican Yauco Selecto and sampling the brew from well-stained espresso cups. Hard work and the necessity of tasting the blends show in their tremors. The two Americans, Thompson, 27, and Eunson, 26, originally planned to open a cafe that would serve fresh coffee and pastries. In investigating sourcing options, however, they learned that obtaining a reliable supply of good coffee would be

■ Anne Stevenson-Yang is director of the Council's China Operations.

extremely difficult, and so they shifted their sights to stimulating demand by providing a steady supply of coffee, primarily to Beijing expatriates. As they learned about coffee farming, roasting, blending, and trading, they resolved to make their firm a wholesale supplier rather than a retailer of coffee. "If there's no premium coffee on the market, there's no market," says Thompson. "Previously, we thought, there's no premium coffee on the market so there's a great market." Instead, they argue, the availability of a particular product begins to create the market. "If you opened a hamburger shop now, you'd have a far easier time than you would have had five years ago, because of McDonald's. Now, you can sell hamburgers anywhere in Beijing."

Arabica generally purchases beans on overseas markets and roasts them at its factory in Beijing just hours before delivering the order to its customers in Beijing or Tianjin. The company has also recently added a mail-order business, sending the roasted, ground coffee in vacuum-sealed bags. Because Arabica roasts on its premises, the company boasts the freshest coffee available in town. The roasting and grinding also allow the business to qualify as a manufacturer, with the relative ease of approval and tax benefits this status entails.

Arabica works through three coffee brokers in the United States and Australia to buy coffee beans from countries where premium quality coffee is grown, including Costa Rica, Ethiopia, Guatemala, Indonesia, and Kenya, and then imports the coffee through Tianjin. The partners also travel frequently to coffee-producing areas in China, seeking coffees of acceptable quality and trying to find coffee farms with which to sign exclusive purchasing contracts. Several foreign coffee producers that sell domestically sourced coffee beans under brand labels such as Nescafé and Maxwell House have entered China's coffee market, greatly spurring domestic demand for coffees from Yunnan Province.

Coffee economics in China dictates that the small, entrepreneurial farms harvest coffee cherries as quickly as possible—whether or not the cherries are ripe—process the cherries themselves to keep as much of the value-added work in house as possible, and sell to coffee brokers. China has yet to develop large coffee farms and large, reasonably priced processors, nor does the Chinese government subsidize coffee farmers through bad years, as do governments of other important supplier states such as Kenya and Ethiopia. As a result, farmers have an even greater incentive to set up their own processing mills so that they can pick the coffee cherries early, store them until prices peak, and then process them on demand. These factors combine to spell mediocre Chinese coffee, used principally as a filler in other brews. In part because of the high tariff barriers, though, companies like Arabica are working hard to encourage the cultivation of a better cup of coffee from Yunnan Province. Arabica now offers a blend called "Morning Cup" that includes Yunnan coffee and is marketed as a second-grade coffee for hotel functions.

> Arabica, which began to break even at the beginning of 1996, roasts about $16,000 worth of coffee per month.

Reading the coffee beans

Given the difficulties involved in bringing fresh coffee to the Chinese marketplace, Thompson, Wilson, and Eunson hoped to identify a specific market segment to target. In mid-1994, they distributed a consumer survey at supermarkets and expatriate haunts in Beijing. The more than 100 responses they received suggested that the average expatriate living in Beijing drinks about three cups of coffee a day, and that about 40 percent of this coffee is brewed from coffee brought in from overseas. About 51 percent of those surveyed were unhappy with the quality of coffee available in China. The respondents also expressed a willingness to buy locally if the price were right. The survey results led the partners to believe they could capture a good portion of the 40 percent of coffee that expatriates were bringing in from abroad.

The partners imported roasting equipment for $30,000 in 1994 and then spent $5,000 and months of hard labor on putting in a new wall and plumbing, painting, rewiring, and generally refitting the two large rooms they rent from the dairy factory for their roasting and managerial operations. Wilson even repaired the elevator. They imported $20,000 worth of coffee beans and made their first sale in February 1995. At first, Arabica focused on the individual retail—rather than the institutional—market, offering 16 varieties of coffee and four of the company's own blends ranging from ¥75 ($9) for 250 g for a house blend delivered monthly to office subscribers, to ¥135 ($16.20) per 250 g for high-end Hawaiian Kona.

Wilson, Thompson, and Eunson had hoped to sell 100 kg of coffee per week, selling principally to individual customers, who would place orders by telephone and receive their freshly roasted blend free of charge the same afternoon. But demand did not develop quite as they had envisioned, and individual customers turned out to be only a small portion of their business. Part of the problem, it seemed, were the ambitious projections they extrapolated from the survey results to the whole expatriate market—despite the fact that the survey was exclusively in English and therefore returned mostly by North Americans, Britons, and Australians.

They found that they had failed to account for differing national preferences. For example, they learned that the very term "gourmet" coffee seemed offputting to Swiss customers, for whom the word implied American, and therefore inferior, coffee. To Italians, "espresso" was suspect, since they considered that any coffee should be espresso. Japanese customers like lighter roasts, while Africans want full-bodied, acidic coffees and are accustomed to the lower prices at home. The partners learned that they would have to adapt to this segmented market by offering different blends to different customers. After adjusting their menu of coffees, though, they still found it hard to compete with the long-time expatriate habit of carrying in several pounds of coffee from abroad after each trip. And even when purchasing in Beijing, expatriates tended to buy coffee in the super-

> The company boasts the freshest coffee available in Beijing.

market rather than place a special order. All these factors combined to diminish greatly the retail market Arabica had expected to target.

Branching out

Thinking they would deliver a lot of retail coffee "was a bad assumption, but we rebounded," says Thompson. The rebound came from winning standing accounts with hotels and restaurants. Now, institutional customers account for 80-90 percent of Arabica's sales. The company currently has more than 40 commercial accounts, including five hotels in Tianjin, and the Jianguo, the Palace, Cafe Cafe, and Justine's restaurant in Beijing. Arabica, which began to break even at the beginning of 1996, roasts about $16,000 worth of coffee per month and hopes to double sales by the end of the year.

When companies place a standing order that totals out at three metric tons, Arabica will lend them an espresso machine against a deposit and provide training and service. The machine-with-your-coffee system—which allows Arabica to provide equipment without getting a special license to sell it—will enable the company to compete with the big players like Melitta and Starbucks. Arabica's shortage of capital, however, means that the company is only able to loan machines, rather than give them out for free. This could make buying from Arabica less attractive than from a company well-heeled enough to hand over an espresso machine with a three-year coffee purchase contract.

A long day

At times, Arabica has a hard time supporting its six full-time Chinese employees and three partners, as well as importing half a metric ton of coffee beans per month. The partners live in inexpensive local housing and sometimes work around the clock. Most of Arabica's problems, however, tend to be conventional problems of business strategy and management rather than obstacles erected by the Chinese bureaucracy. The biggest problem for the company's partners came from overestimating the individual, expatriate market for coffee. Once they realized they could not build their business on individual sales, they had to recast their marketing strategy to capture institutional clients. The other major problem for their business is undercapitalization, which makes it hard to compete with other coffee suppliers.

Arabica nevertheless has had its share of bureaucratic miseries. The new currency-exchange system, which technically represents a step closer to trade-account convertibility for the *renminbi*, has made it more difficult for Arabica to swap money. Banks now require bills of lading before they will allow a swap—something swap centers did not require—and bills must be paid before the bill of lading can be delivered, presenting new cash-flow problems for a little business such as Arabica. And, when Beijing introduced a rule restricting the use of certain types of jeeps, sedans, vans, and minibuses to even or odd days, Arabica had to buy a new delivery vehicle.

Still, the fact that the three partners spend their time refining their corporate strategy instead of cultivating relationships with local officials suggests a sea change in business in Beijing: while Taiwan and Hong Kong entrepreneurs have long been investing in niche businesses on a shoestring, only recently have Westerners had sufficient experience in China, as well as confidence in its economy, to risk their own money in small ventures.

Quietly, but steadily, the expatriate-services bubble continues to grow. In addition to Arabica Roasters, the businesses started by and catering to foreigners in Beijing include Frank's Place, a bar and restaurant established by an American; Mozzarella Italiana, a cheese shop started by an Italian couple; Dragon Entertainment, founded by an American who arranges cultural events; Richmond Brewery, a Canadian joint venture; Lantian, a children's clothing store opened by an American-Taiwan couple; a graphic design and computer services firm called Red Fish; and the expatriate weekly *Beijing Scene*.

In its own corner, Arabica is facing competition from big international coffee companies, notably Germany's Melitta, which provides its own equipment to large customers and offers high-quality products at reasonably low prices. Starbucks has been advertising in China as well, apparently in preparation for entering the market. Arabica believes it can hold its own, though, and is working on expansion plans. The next step for Arabica may be to open its own cafe, perhaps together with a roasting shop and showroom.

Thompson, Wilson, and Eunson believe that coffee houses could emerge as welcome sanctuaries in large cities like Beijing, where people live in small quarters, and that, given time and a supply of good coffee, the coffee house concept will catch on in Beijing as it has in Taipei and Seoul. Arabica is positioning itself to become a supplier to chain coffee shops and plans soon to establish a "private label" division for this purpose. That might be just what is needed to bring coffee out of the expatriate bubble and into Chinese daily life.

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People's Republic of China Yearbook 1995/96

Beijing, China: PRC Yearbook Ltd.; and Hong Kong: N.C.N. Ltd., 1996. 710 pp. $128 hardcover.

The People's Republic of China Yearbook 1995/96 is a comprehensive collection of information and statistics on China. Though neither the most detailed nor timely yearbook available—the data presented are from 1994—the volume offers a general overview of China's government and social structure, economy, provinces and special economic and development zones, recent laws, labor practices, and major events of 1994.

Published annually since 1981 in English and Chinese, the yearbook's greatest value lies in the background information on various government organs. For instance, there is an excellent outline of the functions, committees, and committee members of the National People's Congress. Similar information is provided for the State Council, Central Military Commission, and provincial governments. The book also offers useful—though of 1994 vintage—information on various industrial sectors, including the automotive, aviation, chemical, electric power, electronics, and petroleum industries. The chapter on labor includes recent labor-related laws and an analysis of changes in the composition of China's work force. Of particular interest to business readers is the section on foreign trade and international arbitration, which includes the full text of China's June 1995 "Catalogue Guiding Foreign Investment in Industries." Other chapters treat social and cultural topics, health and medicine, and provide a chronology of landmark events that took place in 1994.

Unfortunately, many chapters read like propaganda speeches, perhaps because one of the co-publishers, N.C.N. Ltd., is the sole agent of the centrally controlled Xinhua News Agency. Several chapters begin with speeches made by Communist Party leaders, followed by less-than-objective reporting of events. For instance, the chapter on reunification and overseas Chinese affairs contains PRC President Jiang Zemin's January 1995 speech about Taiwan entitled "Continuing to Promote Reunification of the Motherland," together with official commentary on political developments in Taiwan in 1994.

The political overtones notwithstanding, the comprehensive background information on various PRC ministries, organizations, and industrial sectors makes the volume a useful addition to any office library.

—*Meredith Singer*

Meredith Singer is a business advisory services associate at the Council.

World Development Report 1996: From Plan to Market

New York, NY: Oxford University Press, 1996. 241 pp. $45.95 hardcover, $22.95 softcover.

The focus of the World Bank's 19th annual report on world development is the transition economies of central and eastern Europe (CEE), the newly independent states of the former Soviet Union (NIS), and China and Vietnam. In addition to the focus, the report includes 70 pages and 17 tables of world development indicators, ranging from per capita GNP to external debt, for more than 133 countries.

For those with first-hand experience of the problems China faces in shifting from central planning to a more market-based economic system, the report provides insightful comparisons of how other command economies approached each step in the transition process. Throughout the text, concise sidebars explain unique aspects of different countries' transitions. For instance, one box explains the emergence of China's town and village enterprises. The experiences of the CEE/NIS countries are measured throughout the book against those of China and Vietnam, and the results are revealing: China generally has succeeded where many have failed, particularly in price liberalization, growth, and investment. Where China has been less successful, for instance in reforming State enterprises or the financial sector, the experiences of the CEE countries in particular are held up as models that China would do well to follow. For example, Poland's tough—and successful—banking reforms are described in detail.

The sidebars, along with the many graphics comparing the transition economies, break up what would otherwise be a long, dense read. Among the graphs and charts are comparisons of housing ownership by type in six transition economies; cumulative foreign direct investment inflows; stock market capitalization and turnover; and government expenditures by category and government revenue by source. Each chapter's conclusion lays out a recommended agenda for further reforms.

The business reader likely will find particularly valuable the chapters on "Property Rights and State Enterprise Reform," which includes sections on privatization and a box on the "do's and don'ts" of privatizing natural monopolies such as public utilities; the short chapter on "Legal Institutions and the Rule of Law;" and the chapter on "Building a Financial System." China's "triumphant return to international markets" is held up as a model for others in the chapter entitled "Transition and the World Economy." One comes away from the report with the impression that the World Bank, which lends more to China than to any other nation, is clearly a great admirer of China's achievements. —*CG*

Heirs of the Dragon: China's New Entrepreneurs in the Aftermath of Tiananmen Square

by Satoshi Tomisaka. San Francisco, CA: Cadence Books, 1995. 206 pp. $21.95 hardcover.

Seven years after the Tiananmen Square demonstrations and 20 years after the Cultural Revolution, Japanese journalist Satoshi Tomisaka finds that a renewed patriotism has replaced many people's memories of the dark days of recent Chinese history, as more Chinese begin enjoying the prosperity brought about by economic reforms. In his book, *Heirs of the Dragon*, Tomisaka finds that many Chinese today dwell little on the 1989 crackdown on dissidents, focusing instead on achieving financial security and taking charge of their own destinies.

For businesspeople with experience in China, *Heirs of the Dragon* provides a fresh perspective on the opportunities that entrepreneurs face in China. Through interviews with people from various parts of China, Tomisaka reports on unusual business pursuits that blossomed with government reforms in the early 1990s. In Shanghai, Tomisaka spoke with Yuan Baiwan, nicknamed "Baiwan Yuan" or "one million *yuan*," an entrepreneur who made his fortune off of the inconsistencies in China's bond market. In Shandong Province, he visits a village where peasants entrusted their hard-earned capital to a local community leader to start a township enterprise. Tomisaka's interviews and observations give the personal side of the trend toward private enterprise in China. As market reforms take root, it is no longer impossible that street peddlers could one day become corporate CEOs.

While the book fails to include any numerical data on the extent or output value of private enterprise in China, Tomisaka's conclusion is important: in the wake of the Cultural Revolution and events such as the Tiananmen Square crackdown, a deep-rooted insecurity over returning to a period of hardship underlies China's growing prosperity. This insecurity, combined with a fear of massive layoffs and political unrest that could accompany State enterprise reform, may fuel much of the tireless ambition of China's new entrepreneurial class.

—Piper Lounsbury

Piper Lounsbury is a business advisory services associate at the Council.

China Industrial Sector Reports

Somerset, NJ: China Communications Center, Inc., 1996. About 20 pp. $390 softcover.

Based on the 1995 industrial census conducted by the PRC State Statistical Bureau (SSB), the China Communications Center's *China Industrial Sector Reports* offer information on various sectors, ranging from coal mining and food processing to medical products. According to China Communications Center staff, the sectors that attract the greatest number of requests for information are infrastructure, computers, and consumer goods. Businesspeople can request reports on some 750 industrial sectors in China, but the center also can produce customized reports to meet a company's needs.

In a sample report on the vegetable oil industry, for example, the reader finds a wealth of useful information, including a summary of PRC provincial statistics such as per capita income and annual GDP growth. What makes this report particularly valuable are the profiles and contact information of 10 major firms in the sector. This sample report also details the total number of firms in the vegetable oil industry, total employees, total after-tax profits, and industry revenue growth, along with the average profit margin, average return on assets, and average productivity.

Data on productivity and profitability—often difficult to obtain for PRC companies—abound. For this report, the China Communications Center used data from SSB's census, the *China Statistical Yearbook*, and the *China Population Statistics Yearbook* to assess productivity and profitability of PRC vegetable oil firms. Firm demographics and performance by size, location, type of ownership, and degree of capital intensity are surveyed in detail.

The information presented in this type of report can help an investor compare his joint venture partner against the average Chinese firm in the sector, learn about growth trends or typical ownership structures, or evaluate possible geographic locations for starting a venture. What is missing, at least in the sample report on the vegetable oil sector, are written analyses of the many statistics provided. Nonetheless, for consultants and financial analysts, these sector reports are likely to be invaluable resources. *—TLK*

ADVERTISERS IN THIS ISSUE:

Telecommunications in Asia: Policy, Planning and Development

edited by John Ure. Hong Kong: Hong Kong University Press, 1995. 285 pp. $HK120 softcover.

Telecommunications in Asia: Policy, Planning and Development, aimed at those following or considering Asia telecom investments, provides a non-technical and concise introduction to the regulatory framework, financing options, and main players in the industries of several East and Southeast Asian economies. For China investors, the book includes current and useful China-specific data, combining statistical and graphical information with long-term analysis to facilitate comparison of China's telecom sector with those of other economies in the region.

The book's first three chapters describe the regulatory environments and general course of telecom development to date in the region. Ure, director of the Telecommunications Research Project at the University of Hong Kong, maintains that the development of the telecom sector in Asia has differed widely from the path taken in the West. Because the public networks in developing countries, including China, charge relatively high user fees to subsidize rural telecom development, many more affluent, urban users turn to private networks. These private and regional networks divert funds from national public networks, thus slowing rural telecommunications and economic growth.

Ure also details the functions of the various Chinese telecom authorities tasked with controlling foreign telecom investment and limiting foreign participation in certain types of equipment manufacturing and sales. Ure then guides the reader through the complicated relationships between China's central government and semi-independent telecom entities such as China United Telecom Corp. (Unicom) and Jitong Corp.

An excellent summary lists common investment financing structures for the sector. In China, where foreign operation of telecom networks is prohibited, build-and-transfer arrangements have been popular, especially in mobile phone network projects. Such arrangements have allowed foreign investors to establish valuable relationships with major Chinese telecom players and, in some cases, make immediate returns on their investments.

The book concludes with some analysis of trends in intra-Asian telecom services trade; broadcast media in Asia, including a discussion of China's control over broadcast satellite and cable systems; and equipment sources for the region. Practical features of the book include a glossary of technical terms and a list of industry information resources. In short, *Telecommunications in Asia* presents a regional perspective on the industry without losing sight of the unique aspects of telecom development in specific Asian countries.

—Jacqueline P. L. Teoh

Jacqueline P. L. Teoh, a postgraduate law student at the University of Sydney in Australia, recently completed a clerkship in the Beijing office of Graham & James.

Taiwan: Nation-State or Province?

by John F. Copper. Boulder, CO: Westview Press, 1996. 220 pp. $63 hardcover, $19.95 softcover.

As the title suggests, the unique and still undecided identity of Taiwan and its 21 million inhabitants is the focus of John Copper's *Taiwan: Nation-State or Province?*. The book offers a comprehensive introduction to the island's past and present politics, economy, and society. From colonial tutelage under the Dutch and Japanese, to its loss of full representative status in the United Nations to the PRC, and the roots of its economic dynamism, Taiwan's turbulent history is well chronicled in this concise volume.

Far from an in-depth study, though, the work is rather a series of snapshots of the island, with sections on geography, history, and society, along with coverage of standard political, economic, and foreign policy issues. The discussion of Taiwan's diverse cultures touches on the island's long-standing connection to South China as well as the numerous foreign and internal influences that have kept China and Taiwan divided. The wide scope of this book, however, does lead to some quick generalizations about complex and pressing political issues and social trends.

Copper nonetheless provides a first-class description of the territory's rise to a global powerhouse from relative impoverishment in the 1950s, and the emergence from dictatorial rule and martial law to a system of full participatory democracy. Copper also analyzes the contentious debate over whether Taiwan's historical record and economic and political stature merit a move toward full independence from China. Rejecting the temptation to favor one side of the debate over the other, Copper instead highlights the irony of Taiwan's dual role as paragon of economic development and political pariah, recognized diplomatically by only a handful of nations.

In the end, Copper predicts that Taiwan will continue to hover uncomfortably between full autonomy and interdependence with China in the short term. Never directly answering the question of whether Taiwan is a province of the PRC or its own nation-state, Copper suggests that the island's increasing economic integration with the mainland will coincide with a growing popular sense of independence and a yearning for "separate but equal" treatment in international political and trade organizations. While Copper and countless other analysts may refrain from answering the question of whether Taiwan's expanding web of economic links with the mainland will result ultimately in political ties, one thing is certain: Taiwan will remain a "special case," unlike the Koreas and formerly divided Germany. It is exactly this status that makes the Taiwan dilemma so difficult to resolve.

—Paul Lamb

Paul Lamb is the Council's program manager.

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Zhao Yong Yuan, Chairman of the Board, **Beijing NTC Telecommunications Technology Consulting Corporation,** Former Director, Planning and Construction, **Ministry of Posts and Telecommunications, Beijing,** Vice Chairman, **Association of Telecommunications Scientists**

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Conference Explores the Evolving Chinese Legal System

The China Business Forum, the educational and research arm of the US-China Business Council, held its first-ever conference focusing on Chinese legal issues on September 20 in San Francisco. Attracting nearly 150 lawyers, corporate representatives, academics, and law students, the full-day conference, "China Today: Law, Justice & Business in the People's Republic," briefed participants on developments in China's dynamic legal environment.

Giving the keynote address, Susan Esserman, general counsel for the Department of Commerce (DOC), discussed the Clinton Administration's China policy. Esserman asserted that the US government remains committed to a policy of comprehensive engagement with the PRC, stating that "engagement does not mean ignoring our differences; it means actively working to resolve our differences, while protecting our vital interests." Esserman noted that the Administration's policy of engagement has realized some important results, including a 27 percent increase in US exports to China in 1995, conclusion of the Intellectual Property Rights (IPR) Agreement, the opening of a US commercial center in Shanghai, and progress on the implementation of the Market Access Agreement of 1992.

Esserman also outlined some of the fundamental principles DOC believes are necessary for the further development of the rule of law in China, noting first the need for greater legal transparency. Though China has passed more than 150 laws and regulations governing trade and investment since 1979, other regulations on foreign investment and taxation of foreign ventures exist but are not made public. Esserman also expressed concern about China's implementation mechanism for new laws, as well as the lack of both effective dispute resolution forums for foreign businesses in China and enforcement of arbitral awards.

Gareth Chang, president of Hughes International, spoke of the US corporate experience in China since 1979. Chang emphasized the importance of understanding the PRC's market, government policy, and legal system. China's investment markets are becoming increasingly localized and sophisticated, but will remain volatile for some time to come, Chang said. Chang urged the US government to pursue expanded ties with China through increased engagement.

Zhang Yuejiao, director general of MOFTEC's Treaty and Law Department, delivers the luncheon address.

Luncheon speaker Zhang Yuejiao, director general of the Treaty and Law Department at the PRC Ministry of Foreign Trade and Economic Cooperation (MOFTEC), provided a thorough review of China's foreign trade laws and practices. Zhang highlighted steps that China has taken since 1979 to insure a free and fair investment environment, including passing more than 900 laws and regulations and signing on to numerous international conventions. Beijing is encouraging foreign investment in a few priority areas, Zhang said, including agriculture, energy, environmental protection, raw materials development, and transportation.

Turning to intellectual property rights (IPR) issues, Zhang stated that China attaches great importance to IPR protection and has done much in recent years to combat IPR infringement. In addition to passing patent, trademark, copyright, and unfair competition laws, China has beefed up its enforcement efforts through administrative and judicial channels. IPR tribunals have been set up in all People's Courts; compact disc production lines now are fully protected to prevent illegal production; and systems for the use of source identification codes, inspections, and title verification have been implemented.

With regard to commercial dispute resolution, Zhang cited the success of the China International Economic and Trade Arbitration Commission in handling over 900 cases in 1995 and noted the passage of the Arbitration Law last year. Overall, maintained Zhang, China has a solid record in the enforcement of arbitration awards.

Zhang concluded by discussing ways in which China continues to improve its foreign trade and investment environment. A national legal education plan began this year under the Legal Information Office established by MOFTEC. PRC lawmakers currently are drafting implementing regulations for laws governing dumping, countervailing duties, technology import and export, and foreign trade; and redrafting China's contract, bankruptcy, and anti-trust laws. Zhang suggested that more tariff reductions are on the way, to add to the reductions on over 4,000 goods that took effect this year, and that liberalization of the banking, insurance, and retail sectors will continue. In closing, Zhang said the United States should do its part to provide a fair economic and trade environment in China by doing away with the annual MFN renewal process.

Afternoon workshops covered taxation issues, corruption, dispute resolution, law and justice in Hong Kong after 1997, the trend among foreign companies to develop an in-house counsel specifically for China, protection of IPR, environmental law, telecommunications investments, contract negotiations, and corporate responsibility. The program concluded with a special session on careers in China law.

Wu Yi Addresses Council

The Council hosted a luncheon in honor of PRC Minister of Foreign Trade and Economic Cooperation Wu Yi on September 27 in Washington, DC. The Chinese trade minister, in Washington to participate in the 10th session of the Joint Commission on Commerce and Trade (JCCT), expressed confidence that the wide-ranging commercial talks had created an improved atmosphere for Sino-American relations and provided a forum to reiterate trade and investment issues of mutual concern.

Discussing bilateral trade relations, Wu urged the US Congress to grant China permanent Most Favored Nation status. Noting that China is the fifth-largest trading partner of the United States and that foreign companies had invested roughly $12 billion in China as of August, Wu lauded the evolution of economic and trade relations between the United States and China. With respect to China's domestic economic situation, Wu pointed out that China remains the world's largest developing country. Despite rapid economic growth and Beijing's desire to develop native electronics and aviation industries, China also must focus on agricultural and infrastructure development. Wu expressed confidence that US-China relations will "grow to maturity" in handling trade-related conflicts, citing as evidence the consensus reached on intellectual property rights in June. In closing, the Chinese trade minister urged both countries to adopt a long-term view of the bilateral relationship.

Donald L. Staheli, chairman and CEO of Continental Grain Co. and chairman of the Council's Board of Directors, welcomes MOFTEC Minister Wu Yi.

Hong Kong Office Welcomes New US Official

The Council's Hong Kong office hosted new US Consul General Richard Boucher at a luncheon meeting September 10. Boucher stated that US-China relations are on an upswing, and reaffirmed the US government's interest in seeing a smooth handover in Hong Kong. Boucher expressed willingness to meet with the Council's Hong Kong Advisory Committee at regular intervals to stay abreast of members' concerns.

In another Hong Kong meeting, China's accession to the World Trade Organization and the possibility of the US extending permanent MFN to China in 1997 headlined Council Vice President Richard Brecher's talk to Hong Kong members October 2. Brecher claimed that the time frame for action on these issues is determined, in effect, by the presidential election on one side of the Pacific and the Hong Kong transition on the other, leaving the spring of 1997 as the most opportune time for business to make its case.

The legal and marketing/distribution committees also met in September, discussing labor and packaging issues, respectively. While some members claimed they were being pressured to establish unions or sign collective labor contracts, others reported no such demands on their operations. All agreed, however, that China is applying labor regulations more strictly since passing the 1995 Labor Law.

Implementation of PRC rules that require Chinese-language package labels, however, is still arbitrary and varies from region to region and official to official. Joseph Simone of Johnson, Stokes & Master advised all companies to apply for trademark protection in China and use the registered trademark symbol on their packaging there; failure to do so, he claimed, is an "invitation to get ripped off." Matthew Leung of Landor Associates, meanwhile, explained that many companies are putting too much emphasis on adapting their labels to the cultural specifics of the China market. In reality, Leung said, most Chinese consumers are attracted to the same qualities as consumers elsewhere. The current trend in China labeling, he claims, is for global packaging that changes only to accommodate the recently implemented legal requirements.

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■ Christopher V. Harris

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 1 – September 15, 1996
Foreign party/Chinese party **Arrangement, value, and date reported**

Accounting and Insurance

OTHER

National Mutual Asia, Ltd., a holding of AXA (France)
Will launch fund to invest in consumer-driven companies in mainland China. $500 million. 9/96.

Advertising and Public Relations

INVESTMENTS IN CHINA

Saatchi and Saatchi Advertising Worldwide (US), Bates Worldwide, a subsidiary of Saatchi and Saatchi Advertising Worldwide (US)
Established Zenith Media Greater China joint venture to conduct media planning and buying in China and Hong Kong. $80.2 million. 9/96.

Agricultural Commodities and Technology

CHINA'S INVESTMENTS ABROAD

Fletcher Challenge Ltd., Brierley Investments Ltd. (New Zealand)/CITIFLOR Inc., a wholly owned subsidiary of CITIC (PRC)
Acquired 188,000-ha forest in New Zealand. (New Zealand: 37.5%, 25%-PRC:37.5%). 8/96.

OTHER

ABN-AMRO Holdings N.V. (Netherlands)
Will provide export credit to Agricultural Bank of China. $60 million. 7/96.

Banking and Finance

CHINA'S INVESTMENTS ABROAD

Bank of China
Will open Bank of China International investment bank in London. 9/96.

Abbreviations used throughout text: ADB: Asian Development Bank; 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.

INVESTMENTS IN CHINA

CP Group, Ming-Thai Group, Thai Farmers Bank (Thailand)
Established the headquarters of TM International wholly foreign-owned bank in Shanghai. 8/96.

OTHER

Daewoo Securities Co. Ltd. (S. Korea)
Launched the Asia Access 2000 Investment Fund in China. $50 million. 9/96.

Price Waterhouse L.L.P. (US)
Will provide financial advisory services to the Bank of China. 9/96.

Export-Import Bank of China
Opened Guangzhou representative office. 8/96.

Thai Military Bank (Thailand)
Opened office in Hefei, Anhui Province. 6/96.

Chemicals, Petrochemicals, and Related Equipment

INVESTMENTS IN CHINA

Air Products and Chemicals, Inc. (US)/Guangzhou Fuel and Gas Co. (Guangdong)
Establish Nanfang Air Products Guangzhou Co., Ltd. joint venture. 5/96.

Consumer Goods

INVESTMENTS IN CHINA

Amcor, Inc. (Australia)/Yunnan Tobacco Import and Export Co. (Yunnan)
Established joint venture to produce cigarette boxes in Kunming, Yunnan Province. $20 million. (Australia:60%-PRC:40%). 9/96.

Revlon Consumer Products Corp., a subsidiary of MacAndrews and Forbes Holdings Inc. (US)/Samstar Group Corp. (Beijing)
Established joint venture to produce Revlon products in Shanghai. 9/96.

OTHER

Avon Products, Inc. (US)
Opened Beijing branch. 8/96.

ABN-AMRO Holdings N.V. (Netherlands)
Will provide export credit to Nanjing Huafei Color Display System Co., Ltd. in Jiangsu Province for purchase of Dutch equipment. $265 million. 7/96.

Fuji Photo Film Co., Ltd. (Japan)
Will open 200 additional service locations in China. 7/96.

Electronics and Computer Software

CHINA'S IMPORTS

G.E. Information Services, a joint venture of General Electric Co., Tandem Computers Inc. (US)/China Telecommunications and Broadcast Satellite Corp. (Beijing), China National Postal and Telecommunication Appliances Corp. (Beijing)
Signed a contract to build an electronic data interchange network for banks, government organizations, and local traders. 8/96.

INVESTMENTS IN CHINA

Sharp Corp. (Japan)/Panda Electronics Group Corp. (Jiangsu)
Established joint venture to manufacture consumer electronics in Nanjing, Jiangsu Province. $57.8 million. (Japan:70%-PRC:30%). 8/96.

Rosemount Inc., a subsidiary of Emerson Electric Co. (US)/Beijing Far-East Instrument Corp.
Formed joint venture in Beijing to produce transmitters. $9.5 million. 7/96.

OTHER

Time-Warner Inc. (US)/Shenzhen Advanced Science Enterprise Group (Guangdong)
Signed agreement to manufacture and market laser discs of Time Warner's programs. 9/96.

Engineering and Construction

OTHER

Gammon Construction Ltd., a subsidiary of Tralfagar House PLC (UK)
Opened representative office in Shanghai. 8/96.

Pudong Development Bank (Shanghai)
Will provide loan to Armstrong World Industries Corp. (US) to import mineral wool insulation. $12 million. 8/96.

Environmental Technology and Equipment

CHINA'S IMPORTS

Pollution Controls International Corp. (US)
Will sell 5,000 filtered positive crankcase ventilation valves to Shanxi General Automotive Trading Group Corp. 9/96.

OTHER

ADB
Will provide planning support for agricultural development in western Henan Province. 9/96.

Landcare Research New Zealand Ltd. (New Zealand)
Won ADB contract to consult on land use and tenure in Fujian Province. $580,000. 9/96.

Lincoln International Ltd. (New Zealand)
Won ADB contract consulting for soil and water conservation project in Fujian Province. $530,000. 9/96.

Food and Food Processing

INVESTMENTS IN CHINA

Cheiljedang Corp. (S. Korea)/Changning Group (Beijing)
Established CJ Changning Foods Co., Ltd. joint venture to produce soda beverages. $20 million (S. Korea:60%-PRC:40%) 9/96.

Coca-Cola Co. (US)
Opened bottling plant in Zhengzhou, Henan Province. $18 million. 9/96.

Foreign Assistance

OTHER

ADB
Will extend loan to finance construction of Baodi-Shanhaiguan section of Beijing-Shenyang highway. $26.4 million. 9/96.

Tennessee Valley Authority (US)/Ministry of Water Conservancy (PRC)
Will cooperate to develop water resources on the Hanjiang River. 9/96.

World Bank
Will provide $10 million loan and $20 million credit for Vocational Education Reform Project in Guangdong, Jiangsu, Liaoning, and Shandong provinces, and Tianjin munincipality. $30 million. 7/96.

Metals, Minerals, and Mining

INVESTMENTS IN CHINA

Nisshin Steel Co., Ltd., Hanwa Co., Mitsui & Co. (Japan)/Baoshan Iron and Steel Group Inc. (Shanghai), Sheyong Iron and Steel Investment Co. (Zhejiang)
Will build plant to manufacture stainless steel in Ningbo, Zhejiang Province. $150 million. 9/96.

Essex International PCL (Thailand)/NA
Will build Shenyang Panasia Gold and Products joint venture to produce gems in Shenyang, Liaoning Province. $25 million. 9/96.

Petroleum, Natural Gas, and Related Equipment

INVESTMENTS IN CHINA

Amoco Corp. (US)/Fuhua Group, China National Chemical Construction Corp. (Guangzhou)
Established Amoco Zhuhai Chemical joint venture to build purified terephthalic acid plant in Zhuhai, Guangdong Province. (US:80%-PRC:15%, 5%). 9/96.

Neste Oy (Finland)/China Oil and Gas Pipeline Bureau
Established Qingdao Dragon Gas Co. joint venture to build and operate liquid petroleum gas terminal on Huangdao Island, Shandong Province. $20 million. (Finland:50%-PRC:50%). 8/96.

OTHER

Export-Import Bank of Japan
Will provide loan to finance natural gas pipeline project in Shanghai. $120 million. 8/96.

Chinese Petroleum Corp. (Taiwan)/CNOOC (Beijing)
Agreed to pursue joint exploration project off the Pearl River delta. 7/96.

Esso China Upstream Ltd., an affiliate of Exxon Corp. (US)
Signed agreement to explore Block 02/16 in Liaodong Bay. 7/96.

Enron Oil and Gas Co., an operating company of Enron Corp. (US)/China National Petroleum and Natural Gas Corp. (Beijing)
Signed an agreement to evaluate area in Sichuan Province. 6/96.

Pharmaceuticals

INVESTMENTS IN CHINA

MDS Health Group Ltd. (Canada)/Ministry of Public Health (PRC)
Established drug research and development joint venture in Beijing. $8.8 million. 9/96.

Ports and Shipping

INVESTMENTS IN CHINA

Samsung Group (S. Korea)
Established shipping venture to contract for shipbuilding and assembly of marine, port, and building machines in Ningbo, Zhejiang Province. $300 million. 8/96.

OTHER

Hutchison Ports Xiamen Ltd., a unit of Hutchison Whampoa, Ltd. (Hong Kong)
Signed an agreement to build and operate two berths in Xiamen, Fujian Province. 9/96.

Power Generation Equipment

CHINA'S IMPORTS

Mitsubishi Electric Corp. (Japan)
Will provide boilers and turbine generators to Baoshan power plant project in Shanghai. $120 million. 8/96.

Siemens AG (Germany), Foster Wheeler Energy Corp., a subsidiary of Foster Wheeler Corp. (US)/Yangcheng International Power Generating Co. (Shanxi)
Will provide equipment and services to coal-fired power plant in Shanxi Province. $700 million. 8/96.

Babcock and Wilcox Power Generation Group, unit of McDermott International, Inc. (US)/Huaneng International Electric Power Development Corp. (Beijing)
Will supply coal-fired boilers, related accessories, and balance-of-plant equipment and technical assistance to the Nantong Power Project in Hangzhou, Jiangsu Province. $275 million. 8/96.

Korea Heavy Industries & Construction Co., Ltd. (S. Korea)
Will provide nuclear power plant facilities to nuclear plant in Guangzhou, Guangdong Province. $150 million. 7/96.

Framatome SA (France)
Signed agreement with Eastern China Electric Group to produce parts for nuclear power plant in Chengdu, Sichuan Province. 7/96.

Atomic Energy of Canada Ltd.
Will supply two heavy water reactors to the Qinshan nuclear plant near Shanghai. $2.6 billion. 7/96.

INVESTMENTS IN CHINA

Deutsche Babcock AG (Germany)/Tangshan Boilers Factory (Hebei)
Established joint venture in Tangshan, Hebei Province. $25 million. 9/96.

International Energy Group (US)
Will build two power generators and support facilities at the Changsu No.2 power plant in Changsu, Jiangsu Province. $1.2 billion. 7/96.

OTHER

Export-Import Bank of Japan
Will provide loan for construction of power plant in Zhuhai, Guangdong Province. $403 million. 9/96.

Bank of Tokyo-Mitsubishi (Japan)
Will provide loan for construction of power plant in Zhuhai, Guangdong Province. $267 million. 9/96.

Siemens AG (Germany)
Will open office in Urumqi, Xinjiang Uygur Autonomous Region. 9/96.

People's Insurance Property Co. of China, Bank of China, Harbin Power Engineering Co., Ltd.
Will provide guaranties and insurance for export credits for Pakistani thermal power project. $80 million. 8/96.

Westinghouse Electric Corp. (US)
Opened Guangzhou representative office. 8/96.

Export-Import Bank of the United States
Will provide loan to State Development Bank of China to finance sale of American equipment for Yellow River dam project in Henan Province. $55.8 million. 7/96.

Export-Import Bank of the United States
Will provide loan to finance sale of American power plant equipment and services to Huaneng International Electric Power Development Corp. (Beijing). $260 million. 7/96.

Property Management and Development

INVESTMENTS IN CHINA

Bank of East Asia Ltd., Marlin Land Ltd. (HK)
Established East Asia Marlin Land joint venture to advise clients on China's property market. 9/96.

CP Group (Thailand)
Will build a shopping mall specializing in food products in Shanghai. $300 million. 8/96.

Jusco Stores (Hong Kong) Co., a subsidiary of AEON Group (Japan)/Guangdong Teem Department Stores (Guangdong)
Opened a large-scale commercial complex in Guangzhou, Guangdong Province. 7/96.

OTHER

Koll Asia Pacific, a unit of Koll Co. (US)
Will provide property management services for the China Merchants Tower office building in Shanghai. 9/96.

Singapore Housing Development Board (Singapore)
Will plan and design housing project in Shanghai. $144 million. 9/96.

First Pacific Davies Ltd., a subsidiary of First Pacific Co., Ltd. (HK)
Opened Shanghai office. 8/96.

Telecommunications

CHINA'S IMPORTS

Oy Nokia AB-Nokia Group (Finland)
Signed agreement to expand digital switching for mobile phones in Zhejiang Province. 9/96.

France Télécom, Tomen Corp. (Japan)/Guangzhou South China Telecommunications Investment Corp. (Guangdong)
Will build two global systems for mobile communications networks in Guangzhou and Foshan, Guangdong Province. $57 million. 9/96.

Telefonaktiebolaget LM Ericsson (Sweden)
Will expand Shanghai's telecommunication system. $35 million. 7/96.

Telefonaktiebolaget LM Ericsson (Sweden)
Will provide SDH equipment to Fujian, Zhejiang, Guizhou, Sichuan, Guangxi, Guangdong and Hainan provinces. $28 million. 7/96.

Telefonaktiebolaget LM Ericsson (Sweden)
Will build mobile phone roaming systems in Beijing and Guangzhou, Guangdong Province. $1.4 million. 7/96.

INVESTMENTS IN CHINA

Pirelli S.p.A. (Italy)/CITIC Pacific (HK)
Established Wuxi Tong Ling Co. Ltd. joint venture to update technology and produce optic fiber. $30 million. 9/96.

Showa Electric Wires and Cables Co., Ltd., a subsidiary of Toshiba Corp. (Japan)/Hangzhou Futong Group (Zhejiang)
Established Futong Showa Wires and Cable Co. joint venture to produce cables and telecom facilities. 9/96.

Inter Far East Engineering PCL (Thailand)/United Telecom Satellite Co.
Established Unicom Far East Network System Co. joint venture to build and operate satellite-communication network. $12 million. 9/96.

France Télécom, Tomen Corp. (Japan)/China United Telecommunications Corp. (Beijing)
Established joint venture to offer mobile phone service in China. $460 million. 8/96.

ADC Telecommunications Inc. (US)/Panda Electronics Group Corp. (Jiangsu)
Established Nanjing ADC Broadband Communications Co. Ltd. joint venture to produce telephone and data-transmission products in Nanjing, Jiangsu Province. $17.5 million. 8/96.

Telefonaktiebolaget LM Ericsson (Sweden)/Wuhan Research Institute, a unit of the Hubei provincial MPT
Established joint venture to develop and manufacture SDH equipment. 7/96.

Transportation

CHINA'S IMPORTS

Groen Brothers Aviation Inc. (US)
Will sell 200 commercial gyroplanes to Shanghai Energy and Chemicals Corp. 8/96.

The Boeing Co. (US)
Will sell three 747-400s to China Air. $510 million. 7/96.

INVESTMENTS IN CHINA

Freightliner Corp., a subsidiary of Daimler-Benz AG (Germany)/Shanghai Zehai, Shanghai Xijie
Established a joint venture in Shanghai to build heavy-duty trucks. 9/96.

Ford Motor Co. (US)
Signed an agreement to develop a low-cost catalytic converter in China. 9/96.

Daewoo Corp. (S. Korea)/Xian No.2 Motor Transport Co. (Shaanxi)
Established joint venture to offer passenger coach services in northwest China. $4.8 million. (S. Korea:50%-PRC:50%). 9/96.

Cummins Engine Co., Inc. (US)/Dongfeng Automobile Corp.
Established joint venture to manufacture Cummins C-series engines in Xiangfan, Hubei Province. (US:50%-PRC:50%). 8/96.

Jardine Transport Services, a subsidiary of Jardine Pacific Ltd. (HK)/Dongguan Foreign Trade Development Corp.
Formed joint venture to provide daily river feeder service between Hong Kong and Dongguan. 8/96.

Mitsubishi Motors Corp. (Japan)/Aviation Industries of China, Taihang Instrument and Meter Factory (Shanxi)
Established joint venture to produce 1,300cc gas engines in Harbin, Heilongjiang Province. 8/96.

Mitsubishi Motors Corp. (Japan)/China Aerospace Automotive Industry Group (Liaoning)
Established joint venture to produce 2,000cc and 2,400cc engines in Shenyang, Liaoning Province. 8/96.

Ek Chor Industry, a subsidiary of CP Group (Thailand)/Shanghai Automobile Industry Corp.
Established joint venture to produce motorcycles in Shanghai. $70 million. (Thailand:50%-PRC:50%). 8/96.

Daimler-Benz AG (Germany)/Yangzhou Coaches Factory (Jiangsu)
Established 5 Star-Benz Co. to produce high-speed buses in Yangzhou, Jiangsu Province. $100 million. 8/96.

MOOG Inc. (US)
Established a representative office and repair/service center in Shanghai. 7/96.

China Eastern Airlines/AlliedSignal Inc. (US)
Established joint venture in Shanghai to produce aircraft landing gear maintenance company. $2 million. 7/96.

Rockwell Automotive Heavy Vehicle Systems, a division of Rockwell International Corp. (US)/Xuzhou Construction Machinery Group Co. (Jiangsu)
Established Xuzhou Rockwell Axle Co., Ltd. joint venture to supply heavy-duty axle products. 7/96.

Hino Motors Ltd. (Japan)/China National Heavy Duty Truck Corp. (Shandong)
Established joint venture to produce truck engines in Hangzhou, Zhejiang Province. 7/96.

OTHER

Hong Kong Dragon Airlines (HK)
Began service from Hong Kong to Qingdao, Shandong Province. 8/96.

Bombardier Inc. (Canada)
Set up representative office in Beijing. 8/96.

ABN-AMRO Holdings N.V. (Netherlands)
Will provide export credit to Yunnan Aviation Industrial Co. in Yunnan Province for airplane purchase. $270 million. 7/96.

Miscellaneous

Carnival Corp. (US), Hyundai Merchant Marine Co., Ltd., a subsidiary of Hyundai Corp. (S. Korea)
Established joint venture to develop cruise line between China and S. Korea. 9/96.

Webster University (US)/Shanghai University of Finance and Economics (SUFE)
Established joint venture to offer Webster's Master's of Business Administration degree on the SUFE campus. 9/96.

Beachport Entertainment Corp. (US)/CITIC
Reached an agreement to produce live arena shows, sports shows, live musical concerts, and television productions in China. 8/96.

Paul Ray Barndtson (US)
Opened executive search office in Beijing. 7/96

Haythe and Curley (US)
Granted license to open office in Beijing. 7/96.

The Walt Disney Co. (US)
Signed an agreement for a new children's radio program to be aired on China National Radio. 7/96.

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- **China's Securities Markets**
  Can lagging B shares snap back?
- **Banking Reforms**
  The roles of China's new policy banks

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Yes, Virginia, Santa Claus Lives on Wangfujing

It turns out that 5,000 years of history are no match for commercialism and the come-all-ye-faithful thrill of Christmas. While the average Chinese does not know when Christmas Day falls or what it celebrates, China's big coastal cities turn into virtual Santa's villages during the Christmas season. The Christmas boom has been fed in equal parts by the growing expatriate market for local celebrations, the overflow of toys and Christmas decorations from factories in China's southern assembly heartland, and, perhaps, a dearth of really good holidays, the grinch of communism having frowned upon the religious, the lavish, and the just plain fun.

In mid-November, wholesale shops on Beijing's central shopping thoroughfares of Dongdan and Wangfujing start selling wreaths of pine cones and plastic pine boughs, Christmas tree balls and strings of lights, snow-frosted Santas, and "traditional" hand-embroidered stockings. All the upscale department stores open counters or whole shops devoted to Yuletide decorations of the sort we all thought were still being crafted lovingly by artisans in the mountains of Austria. Young Chinese couples crowd the Yaohan Department Store, choosing between imitation and real Christmas trees. Chinese yuppies hurry out of the office to finish Christmas shopping before the traditional Christmas Eve karaoke gathering, because, as one friend in Shanghai remarked, "China doesn't have enough holidays."

The heart of downtown Beijing, meanwhile, turns into an ocean of lights bestowing season's greetings on passers-by. At the entrance to the Friendship Store in Jianguomenwai, a jolly, hot-air-filled Santa nearly the size of a Macy's Thanksgiving Day Parade balloon beams over two small elf-houses, while stuffed reindeer graze on the astroturf in a sidewalk manger scene. Hotels compete to make their lobbies at once festive, for Chinese visitors, and evocative of warm nostalgia, for the benefit of Western clients. They erect gingerbread cottages big enough for a child to set up housekeeping, tableaux of elves dancing through styrofoam snowfalls, and enormous pines wreathed in strings of popcorn and colored lights. Red velvet bunting and holly boughs deck the halls.

On Christmas Eve, all the big hotels throw no-holds-barred parties that are well attended by both foreigners and well-to-do Chinese. Hybrid Christmas traditions start to emerge: masquerade balls; dinners of turkey, accompanied by champagne, funny hats, and confetti; entertainment by night club singers who wear white suits and sit at pianos floating on islands in the middle of hotel ballrooms, while they sing tunes from "Cats." Office buildings and hotels host Christmas carolers and marching bands that belt out "Jingle Bells" to lobby lingerers. Last year, the Beijing Concert Hall offered a "Silent Night" concert starting at 10:30 on Christmas Eve that was sold out two weeks in advance. Wary of anything too religious, the organizers alternated a choral "Silent Night" with a barber shop quartet singing "Old Home Alabama," Mazursky dances performed by a string ensemble, and a soulful clarinet rendition of "A Man and a Woman."

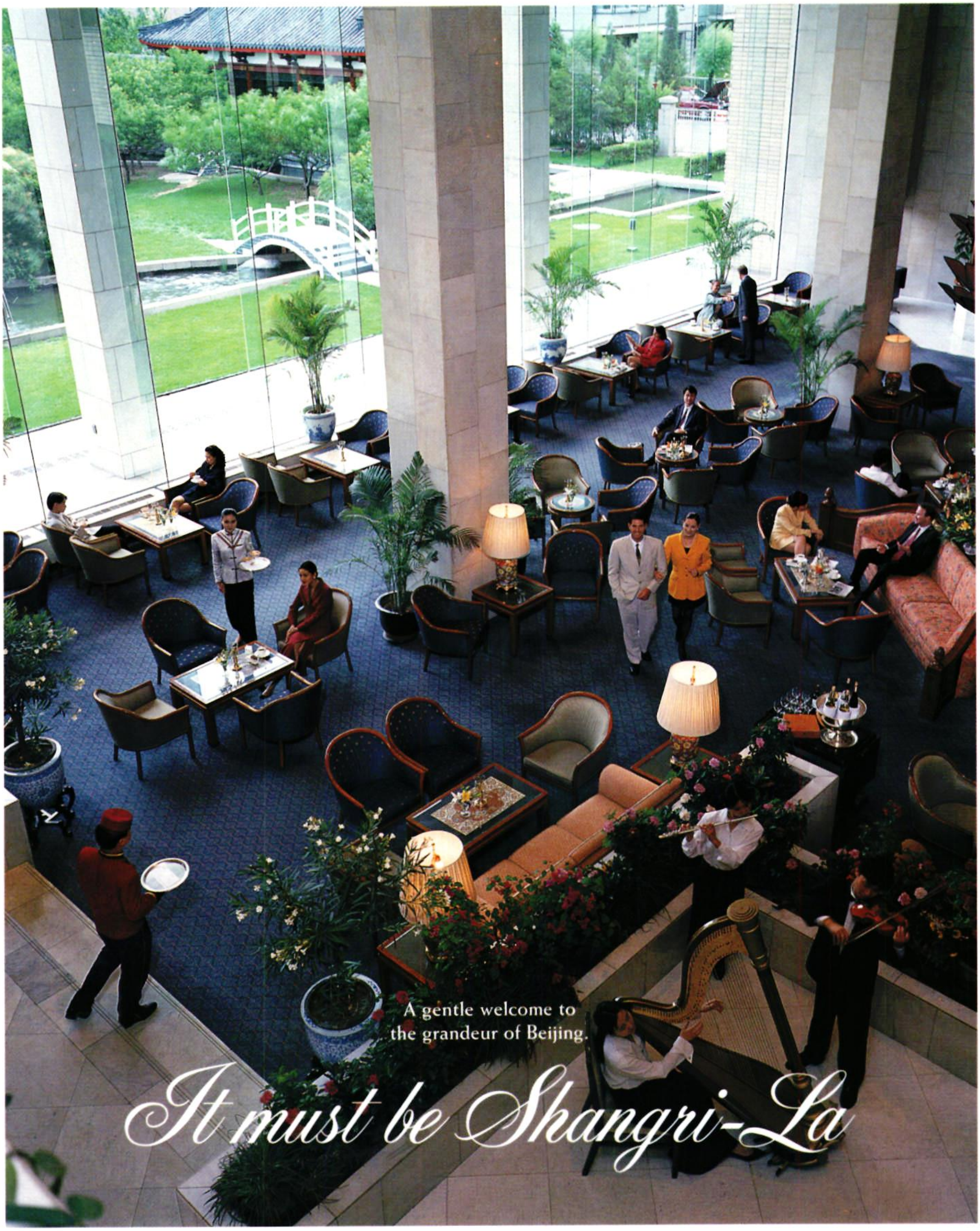
As has been the case for a decade in Beijing, the major Chinese churches hold midnight masses to standing-room crowds. Last year, the Nantang Cathedral resorted to issuing tickets in advance to control the crowds, while visitors had to line up for an hour in front of the Wangfujing Catholic Church to fight for standing room. Most of the pews are filled by young people for whom it has become fashionable to make an appearance at church on Christmas, just as they visit Buddhist temples on the Buddhist holidays. Chinese authorities keep a wary eye on these churches, however, which are prohibited from proselytizing, lest vulnerable young Chinese lose their atheist convictions. For foreigners, from whose congregations Chinese citizens are barred by law, there is the huge Christian Fellowship, which meets at the Sino-Japanese Youth Center; the Good Shepherd congregation at the Great Wall Hotel; an inter-denominational group at the Lido; Catholic services at the Canadian, Philippine, and several African embassies; and many other, smaller services.

Even the cathedrals of Beijing set up tables in the yard to sell Santas and Christmas balls. Seeing the tables groaning with Christmas gilt, it is easy to imagine the girls from Hunan and Sichuan sitting in their humid factories in Shenzhen or Shantou, stitching the gold piping on Santa's pants and dreaming not of chestnuts on an open fire but of the refrigerators they will buy with their monthly earnings. And yet these factory workers, to whom Christmas means no more than does Mid-Autumn Festival to a factory worker in Detroit, produce most of America's toys.

Does this mean that the Spirit of Christmas Present merely follows the wave of cheap labor—that, if Tasmania becomes the world's next big production base, then Christmas will go, too, to Tasmania? The ubiquitous toys and decorations do help popularize Christmas, but I think there is more to it. Christmas is the perfect holiday: It involves family reunion, friends, intricate observances stretching over several days; it represents regeneration and hope. The big festivals as now observed in Beijing entail mostly cooking, eating, and playing mah-jiang. They just can't compare. So think about staying in China for Christmas. Pretty soon, there may be more celebrations in Beijing than in Detroit.

—Anne Stevenson-Yang

Anne Stevenson-Yang is the director of the Council's China Operations.



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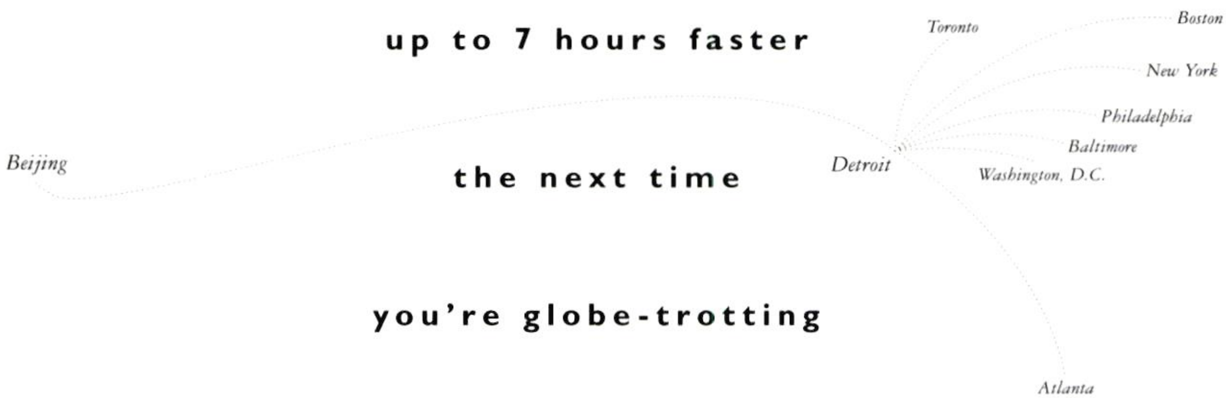

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