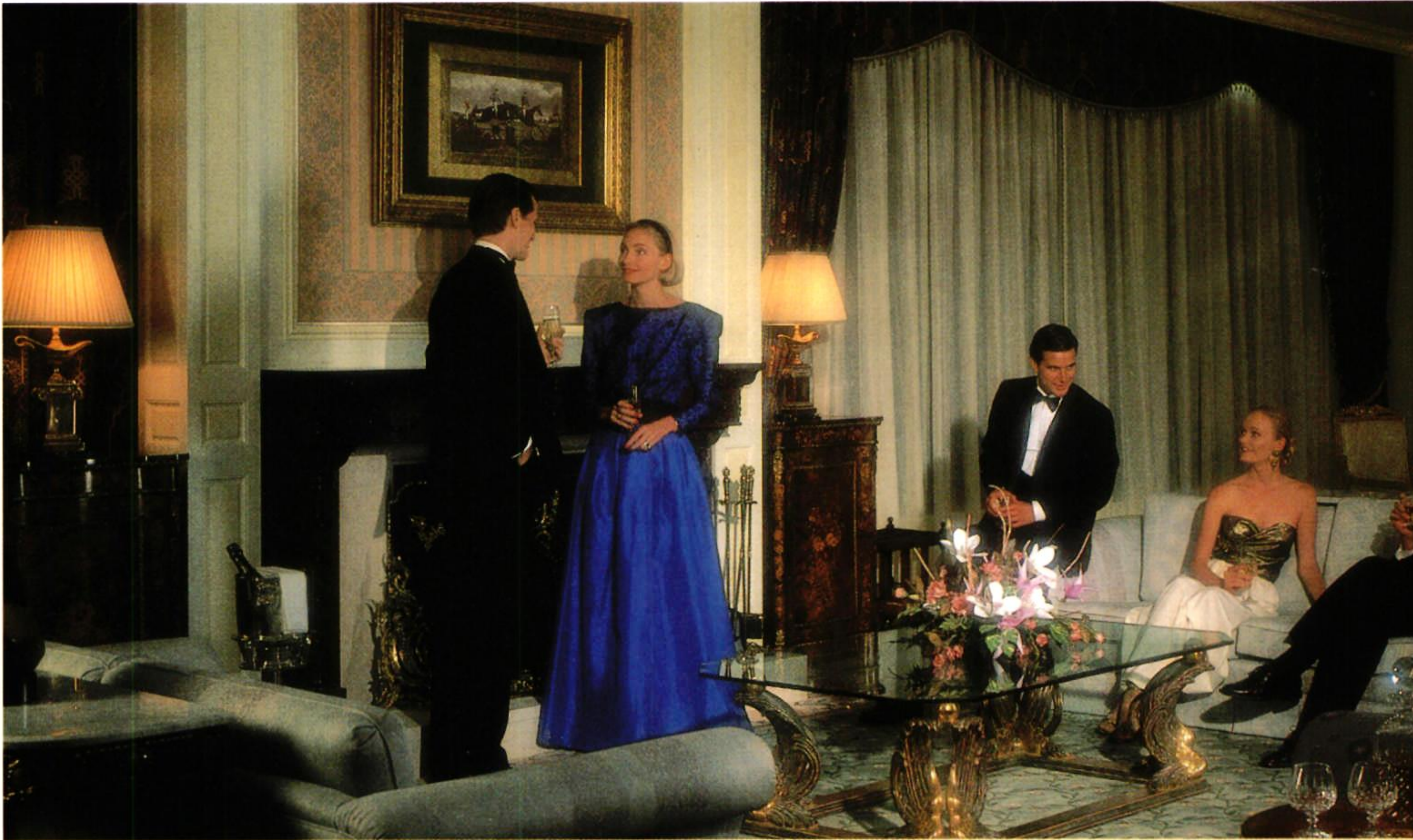
SEPTEMBER-OCTOBER 1991 VOLUME 18, NUMBER 5

Patterning Textiles' Future

- Rough waters for US shippers
- New tax and intellectual property legislation



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THE CHINA BUSINESS REVIEW

SEPTEMBER-OCTOBER 1991 VOLUME 18, NUMBER 5

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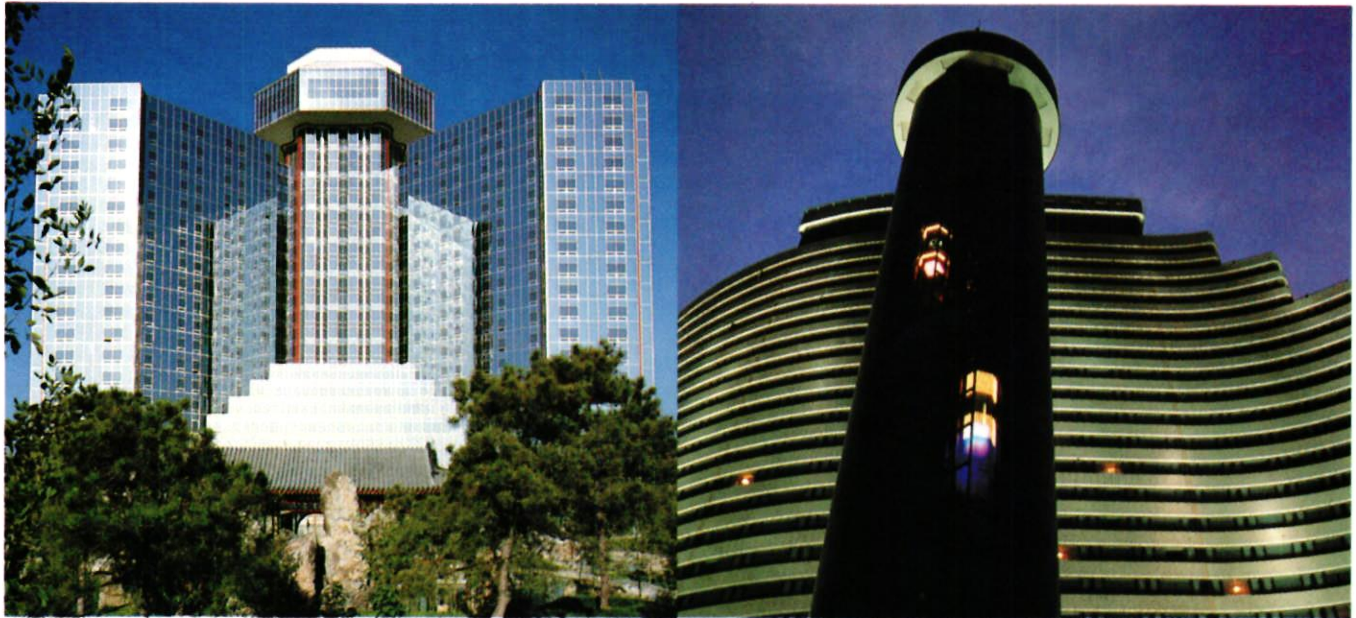

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Hong Kong Airport Project to Proceed

Chinese and British authorities agreed in July to an amended version of the proposed $16.2 billion ports and airport development strategy (PADS), ending a tense stalemate between China and Hong Kong (*see The CBR*, May-June 1991, p. 38). Chinese concerns that the high cost of the project would empty Hong Kong's cash reserves—and leave Beijing to foot any post-1997 bills—were allayed by an agreement that "Any decision [on financing] will give full weight to the Chinese government's views." The United Kingdom also conceded in a memorandum of understanding—to be signed later this year—that Hong Kong's governor will consult with senior Chinese officials on a regular basis on the status of PADS and other major issues, and that Hong Kong will retain at least $3.2 billion in cash reserves upon its return to China in 1997. —DR

Chinese Floods Take Heavy Toll

Heavy rainstorms during the past few months have caused major flooding along the Yangtze and other rivers, affecting more than half of China's provinces. An estimated 3.5 million people have lost their homes, while nearly 2,000 have died from the floods and flood-related illnesses.

Jiangsu, Anhui, and Hubei provinces were hardest hit in May and June, with heavy damage to both crop storage sites and farmlands; an estimated half of China's summer wheat crop was lost. Though Chinese agricultural authorities maintain that the crop losses will be counterbalanced by abundant harvests elsewhere, China purchased 1.5 million tonnes of French wheat in late July. Beijing has yet to announce a total estimate for flood-related crop losses, but officials have indicated this year's agricultural output is expected to drop 2 percent over last year's record levels.

Industrial output in several areas was slowed by the flooding, which forced some factories in Suzhou to close. Other factories located along the Yangtze River, including some foreign joint ventures, reported production slowdowns as a result of road and rail disruptions, which affected deliveries of raw materials. Accordingly, July 1991 industrial output was down about 14 percent from 1990 levels. Foreign economists estimate that the floods ultimately will cost the economy anywhere from $2-10 billion in industrial and agricultural losses. —VL

Chinese Economy Posts Gains

Although third-quarter statistics will likely reflect flood-related economic disruption, recently released figures reveal that China's economy recorded significant growth in the first half of 1990. On the foreign trade front, imports and exports were both up substantially. Total imports for January-June 1991 were $26.8 billion, up nearly 15 percent over the same period in 1990, while exports posted an even higher gain, up 18.5 percent over 1990 levels to $30.4 billion.

Domestic economic performance also improved, with industrial growth soaring 13.4 percent compared to the same period in 1990. Growth in State enterprise production was up almost 9 percent over last year's figures, but still lagged far behind the rates for collective enterprises (up 19.4 percent) and private and foreign-invested enterprises (up 43 percent).

These promising indicators, however, mask underlying structural problems. Growth rates are uneven throughout China, with the southern coastal areas enjoying an 18-30 percent boom in output, while production in the industrial northeast increased by only 4-8 percent. Inflation is also on the rise, averaging nearly 9 percent in urban areas—over twice the national rate for the first five months of 1991 and more than four times the official 2.3 percent rate in 1990. Many economists predict even higher inflation in the months ahead, given expanded credit in the first half of the year and the absence of any fundamental economic reforms since the last bout of rampant inflation in 1988. —VL

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China's Intellectual Property Legislation

New copyright regulations leave much to be desired

Morton David Goldberg and Jesse M. Feder

June saw the addition of two new pieces of copyright legislation in China. The Chinese Copyright Law (CCL) and its Implementing Regulations became effective June 1, while the Software Regulations under the CCL were announced June 4, and become effective October 1. The two sets of regulations do little to resolve the shortcomings of the CCL (*see The CBR*, September-October 1990, p. 24, and November-December 1990, p. 4), and will likely disappoint those hoping that they will enable China to accede to international copyright conventions and avoid US trade sanctions. Nor should the regulations be expected to encourage foreign companies that develop software and other works to become more active in the vast Chinese market.

China's new copyright legislation will likely disappoint those hoping it will enable China to accede to international copyright conventions and avoid US trade sanctions.

Fending off USTR

The new copyright law (which was promulgated last September) and software regulations are in large part the result of pressure on Beijing from China's trading partners—particularly the United States—to improve protection of intellectual property. Even though inadequate Chinese protection of valuable copyrighted assets has kept US firms' participation in the Chinese market to a minimum, piracy is estimated to cost them more than $400 million in lost sales annually—$300 million of that in software alone.

Such staggering losses led the US Trade Representative (USTR) in April to designate China a "priority foreign country" under Special 301 provisions of the 1988 Omnibus Trade and Competitiveness Act, and to begin an investigation of Chinese intellectual property practices one month later. By November 26, 1991 (or, if extended, February 26, 1992), USTR will determine whether China is providing adequate and effective protection of intellectual property, and if not, what action the US government should take. Trade sanctions are a likely option.

China released the new software regulations at the same time a US delegation was visiting Beijing for the Special 301 investigation. The final regulations contain few improvements over what was in earlier drafts and garnered a negative reaction from USTR. Joseph Massey, Assistant US Trade Representative for Japan and China, said at the time that "We have a great deal of concern that the protection is not up to international standards." A look at the regulations suggests that he's right.

Morton David Goldberg and Jesse M. Feder are copyright lawyers with the intellectual property law firm of Schwab Goldberg Price & Dannay in New York City. They have followed closely legal developments in China and other countries concerning computer programs and other copyrighted works.

Major gaps in protection

Both the implementing and software regulations are riddled with holes and inconsistencies. The Implementing Regulations deal with general issues under the CCL and overall administration of the system (see box). While the CCL itself states that computer software is to be protected, only the Software Regulations furnish any details of that protection. It is unclear whether Chinese courts and administrators will apply the Implementing Regulations and the CCL to software.

Foreign companies will also have major problems with other aspects of the new regulations, which almost totally fail to protect works of foreign authorship. Neither the CCL nor the Software Regulations protect foreign computer programs that are first published outside China unless China has a relevant agreement or treaty with the author's home country. But since China does not belong to any such international agreement or treaty—and is not likely to until considerable changes are made in its system of protection—foreign software first published abroad has no protection in China.

The Implementing Regulations, but not the Software Regulations, do have a "simultaneous publication" provision that deems a work to be first published in China if it's published in China within 30 days after actual first publication elsewhere. But as it's unclear whether the

Implementing Regulations apply to computer software, it may well be that software—alone among all copyrighted works—first published abroad is not protected even if published in China within the next 30 days.

While there may be some question about coverage of certain published software, unpublished foreign software is clearly not protected at all. Article 6 of the Software Regulations provides for possible protection only of foreigners' published works, although it explicitly protects both published and unpublished works of "Chinese citizens and units." Article 6 thus violates the basic "national treatment" principle of the major multilateral copyright treaties, the Berne Convention for the Protection of Literary and Artistic Works (Berne) and the Universal Copyright Convention (UCC). According to the principle of national treatment, a country must give the works of foreigners no less protection than it gives those of its own nationals.

Other problems with the Software Regulations include:

- **Failure to protect computer programs as literary works** In most countries, a computer program is protected as a "literary work." The CCL, however, places software in a separate category, giving it treatment different from all other works. This treatment creates a number of problems.

As with novels or textbooks, computer programs can be plagiarized not just by copying their literal text,

Key Provisions of the Copyright Law Implementing Regulations

- "Works" are defined as "unique results of intellectual creation in the fields of literature, art, and science." The word "unique" may mean that works must be novel, a concept typically applying to patent law, not copyright law. Listing the fields of literature, art, and science may narrow the list of copyrightable works in Article 3 of the Chinese Copyright Law (CCL).

- Of the various types of works covered by the CCL, notably missing is "compilation" (e.g., a work such as a directory or a database), although a similar term is defined in Article 5. Neither "computer program" nor "computer software" is defined, suggesting that the Implementing Regulations may not apply to them.

- What constitutes "reproduction" of copyrighted material is limited by references to current technologies, which may provide a loophole as new methods of copying are developed. Moreover, "distribution" includes rental, but it is not clear whether authors retain control over the rental of copies that have been legitimately purchased. US law, for example, gives copyright owners the right to ban the rental of legitimately purchased copies of phonorecords and computer software. In China, the rental issue is an important one, as shops exist where legitimately purchased copies of computer programs or sound recordings are rented solely for the purpose of making pirate copies.

- The definition of "news of current events" clarifies that the related exception in Article 22 of the CCL permits only the copying of "pure factual information" in published materials containing such news; no permission is needed to violate the copyright.

- In "work for hire" situations, the employee has the right to exploit a work created in the scope of employment if the employer doesn't exploit it within two years after its creation. The employee must get permission from the employer, who may refuse only for a "proper reason."

- Copyright protection begins on "the date on which creation of the work is completed." By implication, unfinished works may be unprotected. By contrast, the United States and most other countries protect a work (even if unfinished) from the moment it's in tangible form.

- Works first published in China or published there within 30 days after being first published abroad are protected. Translations or authorized revisions first published in China are protected even if the underlying work was first published abroad.

- Articles 28 and 29 limit the exceptions in Articles 22(3), 22(6), and 22(7) of the CCL for news reportage, translation for teaching or research, and government use.

- Article 31 limits the exception for unauthorized translations of works into minority languages to those texts originally published in the Han language. This provision should not impair the author's exclusive right to authorize translations of text in a non-Chinese language into the Han language, but it is unclear whether an unauthorized re-translation into a minority language may be made of an authorized Han-language translation.

- "Publication" under the CCL may encompass only a publication authorized by the owner. If so, a pirated version of a previously unpublished foreign work could not be considered the kind of "first publication" in China that would confer copyright protection. This provision may further prevent recourse against widespread pirate copying and distribution in China of works first published abroad.

- The Implementing Regulations limit the quotation right granted in Article 22(2) of the CCL for the purposes of introduction, comment, or explanation. Quotations must not constitute a substantial part of the work nor prejudice the quotation owner's rights.

- There is no indication that even by mutual consent parties may vary the terms of the State's standard-form license agreement. The Implementing Regulations do not specify the licensing rates.

- Various administrative punishments are provided for infringement, ranging from a warning to the infringer to imposition of fines. Copyright infringement is not treated as a crime.

- Local copyright administration departments may order infringers to compensate copyright owners for their losses.

but by copying their organizational details. Just as a plagiarist can infringe a novel by appropriating its plot while making minor changes in the dialogue or the names, the software plagiarist can appropriate the detailed structure of a computer program and camouflage the copying by superficially altering the coding. The plagiarist thus avoids the bulk of the development costs and takes a free ride on the author's work. Without protection under the principles that apply to literary works, this non-literal copying of software may well go unpunished in China.

Denying protection for software as a literary work will also make it difficult to apply one of the central principles of copyright laws worldwide—that a copyright protects the manner in which an idea is expressed, and not the idea itself. Articles 7 and 31(3) of the Software Regulations introduce this principle, but it is too early to tell how it will be applied. At this time, businesses considering investing in software development in China cannot be certain that traditional standards will prevail.

• **Insufficient term of protection** Failing to treat computer software as a literary work has another consequence: a different term of protection from other literary works. Article 21 of the CCL generally provides protection for the life of the author plus 50 years, or for a flat 50 years if the author is a legal entity. But Article 15 of the Software Regulations provides only for a 25-year term, renewable for a second 25 years—in violation of the Berne requirement setting life of the author plus 50 years as the standard.

The renewable 25-year term is a major improvement over the draft regulations, which contained a flat 25-year term. Nonetheless, 25 plus 25 does not necessarily equal 50, because the work may be placed prematurely into the public domain as a result of clerical oversight. Moreover, the renewal requirement burdens software producers with the additional formality of renewing their registrations in order to gain a term of protection that legal entities will have automatically for other works.

• **Berne-incompatible registration/formalities** Several other measures of the software protection regulations are incompatible with the Berne Convention. Most mandate registration-related formalities as a condition of copyright protection, which is expressly forbidden by Berne. These formalities demonstrate China's reluctance to give full protection to computer software. They include:

* Registration of software with an unidentified "national software registration administration department" (NSRAD) before a software owner can institute any administrative action or a lawsuit for infringement. NSRAD can invalidate the copyright if its owner has submitted registration information "acknowledged not to be authentic." To the extent the provision is a good-faith attempt to catch software pirates it is a welcome improvement, but it could be used to harass foreign software owners.

* Deposit of "software identifying material" of a nature that will remain unspecified until the software registration rules are made public. Those rules may well require developers to deposit some or all of their source code. The NSRAD is not permitted to use or disclose the deposit material except to carry out its "administrative responsibilities," but there is some concern that these responsibilities could include activities impairing the proprietary rights of foreign software developers. NSRAD employees, for example, could be asked to make proprietary information available to government bodies or Chinese software developers. Moreover, there are only administrative sanctions for improper use or disclosure, and not the mandatory criminal sanctions that were in the draft regulations.

* A three-month time limit on recording transfers of software rights (e.g., through an exclusive license) from other companies. Failure to record in time makes the copyright unenforceable. Transferring a Chinese software copyright to a foreigner not only requires recording it with the NSRAD, but also obtaining prior approval from the State Council.

• **No retroactivity** Registration is permitted only for software published after the Software Regulations are promulgated. Since registration is a prerequisite for enforcement, computer programs published before then will not be protected. In essence, all software in existence today will be in the public domain in China. Thus, piracy of that software will continue freely, supplying both the domestic market and world channels of trade. The lack of retroactivity is a major issue in the Special 301 investigation.

• **Inadequate enforcement provisions** Rights are of little value without remedies for infringement. If software is infringed, Article 30 of the Software Regulations enables the copyright owner to obtain an injunction against the infringement, a public apology, and compensation. Copyright owners are also permitted to "eliminate the effects" of the infringement, but it is not clear what this entails. The NSRAD may levy fines and confiscate the infringer's "illegal income."

Unlike the draft regulations, the final version of the Software Regulations has no provisions for imposing criminal penalties to punish and deter infringement. In addition, no preliminary remedies, such as seizure of the infringing goods or an injunction against the manufacture or distribution of such products, are provided to avoid irreparable harm to the copyright owner during the time a lawsuit is pending. With no preliminary remedies, the infringer can continue to reap the benefits of the infringement while the case wends its way through the administrative system and the courts.

Moreover, neither the CCL nor the Software Regulations specifically address the question of unauthorized importation into China. Typically, copyright owners have control over importation (not just distribution) of their works, which allows them to stop unauthorized importation of copies at the border and prevent the illegal copies from entering the domestic stream of commerce, where they become harder to track down.

• **Overbroad exceptions from protection** According to the Berne Convention, exceptions to basic copyright provisions are permitted only if they don't conflict with the normal exploitation of the work and don't unreasonably prejudice the author's legitimate interests. China's software regulations, however, include broad exceptions incompatible with both of these criteria. Such exceptions fall into two general categories: outright exclusions legalizing otherwise infringing activities;

and compulsory licenses, which deem that the copyright owner is licensing the work for a fee prescribed by law or regulation. US law has limited examples of both exceptions, but nothing approaching the breadth of those in the Chinese Software Regulations.

A number of articles seem to legitimize seemingly infringing behavior. Article 22, for example, permits software users to make "a small number" (which is never defined) of unauthorized copies for a variety of "non-commercial purposes," such as classroom education, scientific research, and government activities. This exception may sanction the current practice of Chinese universities (with which many software developers are affiliated) and scientific institutions of compiling and using libraries of pirated software. At the very least, this exception will be a strong disincentive for foreign businesses to introduce educational or scientific software into China.

In addition, Article 7 contains a blanket exclusion from protection for "algorithms." The term is not defined, however, and could conceivably be used to describe elements of program expression protected under other legal regimes. Moreover, Article 31 provides that program similarities are not infringements if they are due to national policies or laws, or to technical standards adopted by the government. For example, China could mandate that all programs of a given kind must contain a certain valuable feature copied from an existing program. The holder of the existing feature's copyright, however, would not be permitted to claim infringement. The Chinese government thus conceivably could pick and choose elements of the world's most successful software packages and declare them to be "technical standards," in effect legalizing plagiarism.

The last example of overly broad exceptions is Article 13, which provides a compulsory license of extended scope for "software possessing major significance for national or public security" developed by Chinese government entities or, possibly, other Chinese legal entities. Any organization designated by the national or local government may also use the software without the copyright owner's permission for unspecified royalties that would be set by "relevant national regulation." This provision should concern foreign businesses that form joint ventures in China to develop software.

Too little, too late

China adopted its copyright system under pressure from its trading partners to comply with international norms for protection of intellectual property. Even though US trade sanctions were a known threat when China adopted its Implementing Regulations and Software Regulations, the regulations do not go far enough in recognizing the legal rights of software developers. And there is little evidence that even the inadequate protection offered will be effectively enforced.

Unless the system is substantially changed, China will probably be ineligible to join the international copyright community through Berne or the UCC. Foreign software by and large will not be protected, except for the few programs first published in China. If the United States imposes trade sanctions on China for the inadequacy of its protection of intellectual property, it should come as no surprise to anyone—neither US businesses wary of further piracy, nor the Chinese. 完

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Standardizing Foreign Income Taxes

China's new unified tax code will benefit most foreign companies

Joyce Peck

On April 9, 1991, China's National People's Congress passed the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (the Unified Income Tax Law). The Detailed Rules and Regulations for the Implementation of the Income Tax Law were approved by the State Council on July 30, 1991, and both the law and the regulations became effective July 1. The new legislation replaces both the foreign enterprise and joint venture income tax laws, which had governed foreign operations in China since the early 1980s. By far the most significant tax legislation of the last decade, the Unified Income Tax Law stipulates that all foreign investments be taxed under one system, eliminating prior distinctions between equity joint ventures and other foreign enterprises.

Though some foreign investments will fare better than others under the new legislation, on the whole, foreign enterprises in China should welcome the Unified Income Tax Law as a positive step. In the past, foreign investors were faced with a maze of tax legislation and often found it difficult to determine how or on what basis they would be taxed. The Unified Income Tax Law now provides much clearer guidelines on the tax liabilities of foreign investors and companies operating in China. By standardizing the application of the tax law for all foreign taxpayers and making the tax burden more equitable, the Unified Income Tax Law represents a major achievement in China's effort to improve its tax system.

> ***The Unified Income Tax Law stipulates that all foreign investments be taxed under one system, eliminating prior distinctions between equity joint ventures and other foreign enterprises.***

Two categories of taxpayers

The new tax law defines two distinct categories of taxpayers. Those in the first category, "enterprises with foreign investment," are identified as Chinese-foreign joint ventures, Chinese-foreign cooperative ventures, and wholly foreign-owned enterprises. The second category, "foreign enterprises," comprises other foreign businesses in China, such as management branches and representative offices, factories involved in foreign licensing arrangements, places for exploitation of natural resources, contracted project sites, and any companies providing labor services—a category that includes contractors or consulting firms that supply, service, or maintain equipment in China.

The distinction between the two categories of taxpayers is an important one, for in some cases the new legislation provides for different tax treatment. Outside of the Special Economic Zones, for example, only enterprises with foreign investment qualify for preferential tax rates and tax holidays.

With regard to taxing labor services, the new law will have a mixed impact on US companies. The Double Tax Agreement (DTA) between China and the United States allows US companies a six-month grace period before labor services are taxable. US firms operating through Hong Kong-based companies or subsidiaries, however, will find their China operations taxable at the standard 33 percent from day one, as Hong Kong has no such treaty protection.

The new tax laws broaden the definition of "permanent establishment," reflecting the wish of Chinese tax authorities to codify current tax treatment, under which the provision of labor services and the use of dependent agents—an individual representing a sole foreign company—in China constitute a taxable establishment for a foreign company. In contrast, foreign companies using independent business agents—i.e., those who represent more than one company—have generally not been considered to have a permanent establishment in China, and therefore have not been subject to taxes on sales profits. The Unified Income Tax Law, however, fails to distinguish between dependent and independent agents. Though the sales commissions of both types of agents have always been taxed, the new law leaves open the possibility that a foreign company conducting its China business through an independent agent will now have to pay taxes on its overall sales profits.

The lack of certainty contained in

Joyce Peck spent 1984-89 working for Price Waterhouse China in the Hong Kong office. She is now based in Raleigh, NC, where she serves as the company's director of China services.

the agency provisions may prove to be of much concern to foreign companies using independent business agents to sell or purchase in China. US companies, however, should be protected from the ambiguity of the agency provision since the US-China DTA stipulates that the use of an independent business agent does not create a taxable establishment.

The State Tax Bureau (STB), China's ultimate tax authority, has assured foreign investors from countries without a dual tax agreement that use of an independent business agent will not create a taxable establishment. Though there is no indication that protection will be afforded in the law itself, STB officials have indicated that a provision distinguishing between dependent and independent agents may be included in the implementing rules.

In cases where companies use a dependent business agent, STB officials have also verified that though the commission income of the agent and the sales profit of the foreign company are subject to tax, the manufacturing profit—the difference between the manufacturing cost and the wholesale price charged by the manufacturer—will not be taxed. In informal discussions, Chinese tax authorities have also given assurances that employees of a company travelling into China to promote sales will not fall under the agency rules. However, if a foreign company without a "sales" establishment—i.e., a fixed place of business—operates through a dependent agent, its tax status would be in jeopardy. To minimize creating a "sales" establishment, foreign companies should avoid having representative offices involved in sales-related activities. It is also advisable to sign sales contracts outside China, and pass titles to Chinese customers for equipment manufactured outside China. All equipment sold must be manufactured outside China for such sales to be tax free.

Significant changes

The new tax legislation incorporates a number of other major changes that will affect how foreign investors are treated for tax purposes:

• **Determining resident vs. non-resident companies** Article 3 of the new law uses the location of a company's head office to determine whether an enterprise is a resident of China. This distinction is important for tax purposes, since the worldwide income of a resident company is subject to tax, while the tax liability of a non-resident company is limited to China-sourced income.

The lack of certainty contained in the agency provisions may prove to be of much concern to foreign companies using independent business agents to sell or purchase in China.

According to the leaders of the tax bureau, two criteria determine residence: management and control, and registration ("incorporation"). Chinese law requires equity joint ventures, wholly foreign-owned enterprises, and limited-liability cooperative joint ventures to be registered and managed in China, which makes them Chinese legal entities subject to treatment as Chinese resident companies. Unlimited-liability cooperative joint ventures and foreign enterprises, however, operate through registered contracts and are not considered residents of China; therefore, only their China-derived income is taxable.

• **Flat tax rates for all** A flat tax rate has now replaced the progressive rate incorporated in the 1981 Foreign Enterprise Income Tax law (FEIT). The new rate of 33 percent of taxable income includes a 3 percent local tax.

Previously, foreign companies taxed according to the FEIT law came under its five-bracket progressive tax rate, ranging from a low of 20 percent (plus a 10 percent local income tax) of taxable income to a high of 50 percent (combined local and State taxes). Therefore, for foreign enterprises other than equity joint ventures—which have always been subject to a flat 33 percent rate as stipulated under the Equity Joint Venture Law (EJV)—the new tax law could either increase or decrease their effective tax burden.

Generally speaking, large-scale contracting projects, cooperative joint ventures, and wholly foreign-owned enterprises will come out ahead, since their tax rate may drop from 50 percent to 33 percent. The losers will be representative offices and small contracting projects which, for the most part, will bear a slightly heavier tax burden. Representative offices will also find that they are no longer eligible for exemption or reduction of local tax, a common practice under the old legislation.

• **No withholding taxes on profit remittance** Previously, the EJV law required foreign partners of equity joint ventures to pay a 10 percent withholding tax on profits remitted outside China. Article 19 of the new law removes this withholding requirement, thus enabling foreign investors to enjoy tax exemptions on remitted profits which were earned from their invested enterprises in China. In addition, profits distributed from an equity joint venture, cooperative joint venture, or wholly foreign-owned enterprise to another such enterprise in China will be exempt from withholding tax.

•**Tax holidays for more enterprises** Under Article 8 of the new law, productive foreign-invested enterprises with contracts of at least 10 years may enjoy tax holidays. Previously, tax holidays applied only to equity joint ventures and enterprises located in designated preferential investment areas or operating in specific lines of business. Under the new law, investments qualifying for tax holidays are tax exempt in the first and second profit-making years and allowed a 50 percent reduction in the third to fifth years.

According to the STB, enterprises with foreign investment that did not qualify for tax holidays under the old tax laws but qualify under the new law will be eligible for tax exemption or reduction if they were still within their first five profit-making years as of July 1, 1991. For example, if the enterprise is already in its third profit-making year on July 1, it would be eligible for two and a-half years of a 50 percent reduction in taxes. If the enterprise is already in its sixth profit-making year as of July 1, it would not be eligible for any tax

holiday or reduction, even if it qualifies under the new law—there are no provisions for retroactive tax holidays.

• **All enterprises with foreign investment can now get tax refunds for reinvestment** Though under the old tax laws only some enterprises—mainly equity joint ventures and preferred investments such as technologically-advanced or export-processing enterprises—could apply for reinvestment tax refunds, the new law enables all enterprises with foreign investment to receive a 40 percent tax refund for profits reinvested in an existing or new enterprise. Foreign investors, however, are unlikely to find the new law any clearer than previous legislation, as the Unified Income Tax Law similarly fails to address the specific steps to be taken by the enterprise in order to qualify for this type of tax. STB officials have indicated that further clarification of the rules regarding reinvestment tax refunds will be provided in the implementing rules.

• **An "OK" for combined returns** The new law permits a foreign company operating as a single legal entity in China to file a combined tax return for all its business activities constituting establishments in China. Projects that do not create establishments, however, need not be included in the combined return. Losses from one establishment may be used to offset income from an establishment with higher taxes, but these losses must be recaptured at the higher rate in the year they are recovered. For instance, a company with a $10,000 profit from a project in a 33 percent tax jurisdiction and a $5,000 loss from a project in a 15 percent jurisdiction can file a joint tax return for both operations, claiming a $5,000 profit to be taxed at 33 percent. If in the next year the first project again has a $10,000 profit, while the second also posts a $10,000 profit, the $5,000 loss from the previous year must be recaptured, yielding a taxable profit on the first project of $15,000, and a taxable profit on the second of $5,000.

Administratively, most foreign companies will find it extremely difficult to take advantage of this provision, since to gain approval to file a combined return, one of the establishments must assume supervisory and management responsibility over the others, and income from all projects must be calculated on a net-income basis. Many foreign companies, particularly contractors, have separate and distinct projects, and have no management offices in China that could take on a supervisory role. According to the STB, the requirements for "management responsibility over all projects" may be fulfilled if one of the offices assumes responsibility for the tax reporting of all projects, but most contractors will find the tax reporting requirements burdensome. On a short-term basis, the cost of keeping the books and tax records in China could prove expensive. Contractors may also be reluctant to open or designate a management office, and have their taxable income calculated on net income. Many contractors generally prefer to be taxed on a deemed profit basis, where profit is defined as a predetermined percentage of the gross contract amount.

Foreign investors now enjoy tax exemption on remitted profits.

The possibility of filing a combined return is good news for some foreign companies, however, particularly those in the oil and gas industry. The law allows profits and losses from upstream and downstream operations to be included in the same tax return, as long as the activities are in the same line of business—profits or losses from hotels, for example, could not be combined with profits or losses from commercial oil or gas production, even if the same foreign company operates both. An oil company with a petroleum contract, however, could combine the profits or losses of the contract with that of its Chinese petrochemical plant, as long as both operations are owned by the same foreign company.

• **No transfer pricing allowed** Though most countries have long had strict rules governing the transfer prices a company sets within its own subsidiaries or branches—either within a country, or internationally—China had not until now formally addressed the issue. Chinese tax officials, conscious of the potential for tax avoidance through transfer pricing, incorporated Article 13 into the new tax law to prevent taxpayers from shifting profits between associated companies for tax benefit.

The Unified Income Tax Law sets out the pricing policies to be adopted by related parties entering into business transactions. In essence, the law specifies that transactions between associated companies are to be conducted at arm's length prices—those at which the goods or services would be sold to a third party—and STB and local tax officials have the authority to make adjustments when they think such prices have not been used.

Since China does not have a statute of limitations, the tax authorities could conceivably go back to day one of a company's operations and raise questions about transfer prices. To minimize tax exposure, taxpayers should keep adequate records to support all transfer-pricing transactions, since the tax authorities will undoubtedly conduct in-depth investigations in the future.

• **Green light for dual pricing** Under the new tax rules, STB will accept a dual pricing system, where the prices of products for sale domestically and abroad can vary. This provision shows that tax authorities recognize that business—not tax—objectives control companies' pricing policies, and that lower prices are often required for joint venture-produced products to be competitive in the international market.

• **Strict penalties** Five of the 30 articles of the new tax law relate to penalties, which is indicative of China's continuing campaign to clamp down on what it perceives to be widespread evasion of taxes by foreign enterprises. Penalties for late payments have been reduced significantly, from .5% to .2% of the outstanding tax liability for each day in arrears. While a welcome reduction, the penalty still translates to a whopping 73 percent per year! Worse yet, penalties are not tax deductible, and are assessed from the original date the payment is due—even for adjustments resulting from tax audits, which in China often take years to complete.

Chinese tax authorities recognize that the penalty provisions are harsh, but state that in practice there will be "flexible application." To accommodate this flexibility the law provides

that for first violations, penalties "may" be assessed by the local tax bureau, which has traditionally been more lenient in assessing tax penalties than the stringent provisions in the tax law would seem to require. Local authorities are also to assess subsequent violations or cases in which there is non-compliance with the first assessment. Many foreign investors are leery at the prospect of sometimes inflexible local-tax bureaus having such a high degree of discretion over significant tax matters.

Problems remain

As might be expected, not all foreign investors are entirely satisfied with the new tax legislation. First and foremost, there are complaints that the law and regulations contain too many areas of subjectivity, such as the application of penalties or the determination of type of business agent. No investor wants the uncertainty of guessing what the interpretation of the legislation will be five or ten years down the road.

Investors are also distressed to see in Article 58 of the regulations that foreign companies cannot deduct management fees paid to associated enterprises. For US companies in particular, this provision may result in double taxes since US tax laws require that such costs be transferred to affiliates. Where possible, companies should charge their affiliates fees for specifically identifiable services, since these are deductible in China.

Furthermore, despite the numerous appeals of foreign companies to Chinese tax authorities to incorporate a statute of limitations in the new legislation, there is no such provision. However, the STB says such a statute may be included in the Implementing Rules. In the meantime, foreign companies may find themselves held liable for taxes from the first day of their business operations.

For some foreign companies in China, particularly those with small-scale operations, the new legislation may add a heavy administrative burden. To comply with its myriad requirements, taxpayers must obtain multiple approvals and provide stacks of supporting documentation for tax bureau review. Certain provisions—such as the articles granting tax refunds for reinvestment of a foreign enterprise's profits and the articles allowing combination returns—are exceedingly complex, and some companies may find them too cumbersome to even attempt to qualify. The benefits, however, may be well worth the effort. And, given time and experience, the Chinese tax authorities may well streamline the process.

There are complaints that the law and regulations contain too many areas of subjectivity.

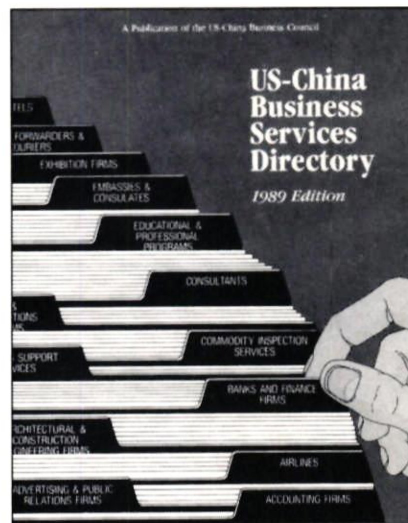
A step in the right direction

Despite these misgivings, most foreign investors view the new legislation as an improvement over existing tax laws, which often resulted in inconsistent and unclear tax applications. Participants in recent Price Waterhouse workshops by and large considered the Unified Income Tax Law an open, flexible law that generally conforms with international practice. Many of the participants had reviewed earlier drafts of the law and regulations, and were pleased to discover that the final legislation incorporated a number of their recommendations.

Yet in any country, changes in a tax system always bring uncertainty. China's tax authorities must now facilitate the implementation of the new tax system while addressing investor concerns about the interpretation, administration, and enforcement of the law. Perhaps the implementing rules, which the STB has promised to deliver within the next year, will clarify many of the gray areas.

All in all, Chinese tax authorities have made remarkable progress in the past 10 years. The new tax law is a big step in the development process. In the long term, the integrity of China's tax system has been strengthened by the establishment of a credible tax regime. Foreign investors, who found many of their concerns and comments incorporated into the new legislation, will no doubt benefit from this progress in China's tax system. 完

The US-China Business Services Directory
A Publication of the US-China Business Council



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Interview

J. Stapleton Roy, former ambassador to Singapore and executive secretary of the State Department, replaced James R. Lilley as US ambassador to China in August. Roy spoke with Editor Pamela Baldinger in Washington, DC, before leaving for Beijing, where he previously served as deputy chief of mission from 1978-81.

Moving US-China Relations Forward

Q *You will be assuming your post as ambassador to China at a time when relations between the two countries are under severe strain. What will your goals be?*

A My principal goals in China will be to try to move the US-China relationship in directions that serve US interests. I think that there are areas where both our interests and those of China provide a basis for movement in that direction. This covers a whole range of issues; some of them are global in nature, such as controlling nuclear and missile proliferation. Others are regional, such as trying to establish a Middle East arms control regime, or trying to produce a just and fair settlement in Cambodia. Others are bilateral issues, such as improving the investment climate for US businesses in China, improving conditions for our exporters, trying to address some of the non-tariff barriers that China imposes on imports, and dealing with specific concerns in such areas as intellectual property protection. Human rights questions are of great concern in this country, and those will certainly be an important part of my mission in China. So I see a panoply of issues that we need to work on together. My experience has been that when we are able to maintain an effective dialogue in China, we have always been more successful in moving our relationship in directions that are compatible with these interests.

Q *What will it take to maintain a successful relationship?*

A Well, the first thing we have to understand is that the United States cannot simply create favorable conditions in other countries. There are countries very close to the United States that have completely unsatisfactory human rights and other types of domestic environments, and where we haven't been able to shape their domestic situations to fit our ideals. But we can be a very effective force in reinforcing the aspirations of the people of other countries for universally recognized human rights and values. This is the basic underpinning of our policy approach. My task in Beijing will be to try to find the best ways for moving these processes forward.

Q *How receptive do you think the Chinese will be to these arguments? We're hearing a lot of rhetoric about evolutionism and the West's so-called desire to take over China through peaceful means. This doesn't sound very promising for bringing China to the negotiating table.*

A The Chinese are resistant to conditions imposed on them by outside countries, and I can understand that. But there is nothing that the United States seeks in its relationship with China that is not fundamentally in the interests of the Chinese people themselves. I do not see any incompatibility between what we want and what the Chinese people want. Our goal must be to work with the Chinese government in ways that will enhance movement in these directions.

Q *You just raised a whole list of issues you anticipate taking up with the Chinese. Where do business and trade-related issues fall on this list—what will take priority?*

A They'll be right at the top. I don't say, 'First we have to deal with the proliferation issues and then we'll get around to the business issues.' We will be pursuing all of these issues at the same time. At the moment, one of the impediments to the relationship has been that in the aftermath of 1989, we haven't been able to maintain high-level contacts with the Chinese, and we feel that certain improvements in such areas as weapons proliferation and human rights are necessary to move back to the resumption of such contacts. Once we are able to move back in the direction of contact, the business issues will be addressed along with these other issues. In fact, we are already addressing them at lower levels, and have been throughout the past two years.

Q *Are you saying there are specific criteria the Chinese will have to*

meet before normal high-level contact can be resumed? Are the Chinese aware of these criteria?

A We've already had an effective dialogue with the Chinese in which we've laid out the concerns that in our view are hindering our ability to move back toward a more normal relationship. So, I think they understand the areas where we think progress is necessary. On some of these key areas, we've gotten responses from the Chinese that suggest they see the possibility for movement.

Q *Such as?*

A On proliferation issues, for instance, the Chinese participated in the Paris conference on the Middle East arms control initiative. Under Secretary Bartholomew had talks in late June on proliferation issues that helped lay the basis for continuing talks with the Chinese on this matter. We haven't yet announced any breakthroughs in these areas, but we see a basis for continuing our dialogue with China, and there are specific purposes we're trying to achieve. We're not trying to achieve breakthroughs just on non-proliferation issues, we're trying to create a basis for moving back into normal, high-level governmental interaction with the Chinese that will improve our ability to pursue the full range of issues we have before us.

Q *So that would involve lifting the ban on visits by high-level government officials imposed after Tiananmen?*

A We don't consider sanctions as a permanent part of our relationship with China. They were measures taken in the aftermath of the Tiananmen event, and which reflected the strong feelings of the American people. We would like to work with the Chinese to move the relationship in a direction that would make those sanctions no longer applicable.

Q *What kind of leverage will you have with the Chinese, considering that the United States is acting unilaterally on trade issues right now? Why should the Chinese cooperate with the United States if they believe they can turn to Europe and Japan instead?*

A The Chinese should take our concerns seriously because it's in their interest to do so. The United States has become the number one market for China, to the tune of $15 billion last year, according to our trade figures. If our concerns are not addressed seriously, the Chinese can assume there will be growing pressure in this country for us to take even stronger measures against what we consider unfair trading practices. So, it's in their interest to give attention to our concerns. We're not seeking special favors from China—all we're asking is that they respect intellectual property rights; that they begin moving back in the direction of greater transparency in the governing of international trade; and that they move in the direction of international norms, reflected in GATT, and in their dealing with imports, so that exporters have some way of knowing what factors make their goods competitive or non-competitive in the Chinese market. Nothing we're asking of the Chinese represents a special favor; in fact, there's a basis of mutual interest in finding solutions to these problems.

Q *Your predecessor was very active with the US business community in Beijing. Do you also intend to adopt this style?*

A I do indeed. Ambassador Lilley's commitment to looking after and promoting the interests of US business in China is something I have every intention of continuing.

Q *What role will Hong Kong play in your dealings with China?*

A Essentially, my responsibilities in China don't cover Hong Kong per se; but to the extent that Hong Kong becomes an issue in US-China relations, then it is a matter I will have to pay attention to.

We have great concern about the future of Hong Kong, because we have had a very effective long-term relationship with Hong Kong. Many of our businesses are located there, and we have substantial trade, so the future of Hong Kong matters to us. I think that one of our specific goals should be to develop our relationship with China in ways that will facilitate a smooth transition for Hong Kong in 1997. This goal can serve as a strategic orientation point for us in terms of trying to address all of the issues that would contribute to a more favorable environment for that transition. And that includes trying to have an effective, constructive, and friendly relationship with China in 1997.

Q *The US is moving in a decidedly different direction from its G-7 partners in regards to China policy. Is the Administration concerned at going it alone?*

A We're not really concerned. Our concerns relate to the human rights environment in China, which is the real reason we put restraints on lending, and why we are still sticking to the position that we will support loans only for basic human needs in China. But we'd like to be able to move back toward a more flexible lending policy in China, and would like to see the improvements in human rights that would make that move possible. If other countries are pursuing their human rights interests in China via other ways, we can understand that.

Q *Will the US be willing to pressure its G-7 allies to approve only basic human needs loans to China?*

A We have had a dialogue with the major lending countries for the last two years, and I think they understand the concerns that form the basis of our policy. I sympathize with the desire in Congress and elsewhere to find better ways to mobilize international support for human rights concerns that matter to us. But whether or not trying to put specific pressure on other governments will be effective in accomplishing this purpose, I think is an open question.

Q *Is there anything you'd like to tell the American business community?*

A I would like to emphasize how important I think the engagement of US business is for our overall relationship. I see one of my prime goals in China as doing everything I can to improve the business environment, and I hope to have numerous contacts with the American business community during my term in China.

Stormy Seas for US-China Shipping

A pending FMC investigation could prove costly for both shippers and importers

Pamela Baldinger

While the boom in US-China trade has generally translated into increased business for shipping lines plying US-China routes, US-China maritime relations are at the lowest point since the signing of the current bilateral agreement in December 1988. Spurred by claims from US carriers that they are prohibited from conducting business in China according to the terms of the bilateral, the Federal Maritime Commission (FMC) officially launched an investigation of Chinese shipping practices in late July. Should it determine that US carriers are subject to barriers in China that Chinese carriers do not face in the United States, the FMC could impose a variety of sanctions, such as tariff or agreement suspensions, denial of access to US ports, or fees of up to $1 million a voyage. Such sanctions would not only seriously affect Chinese carriers, but would also have an impact on US shipping lines—which would inevitably lose favor with Chinese booking agents—and US importers, who might face increased prices, delays, and difficulty in receiving their products.

Sorting out the issues

Many of the concerns being examined by the FMC were supposed to have been addressed in the 1988 Agreement on Maritime Transportation between the United States and China. Differences in interpretation and legal regimes, however, have kept them from being solved to the satisfaction of US authorities. Based on the minutes of the April meeting between the Maritime Administration of the US Department of Transportation (MARAD) and the Chinese Ministry of Communications, as well as documentation submitted by the main US and Chinese carriers and other interested US parties, the FMC has selected five general areas to investigate: branch office activities, carrier tariffs, port service issues, intermodal and related services, and "doing business" costs.

• **Branch office activities** Perhaps the most significant of the five issues being addressed by the investigation, this one centers on what activities US firms may conduct through their representative offices in China. US maritime officials, claiming that representative and branch offices are the same, point to the bilateral agreement clause that states "US maritime carrier representative offices in China will be able to conduct all normal business activities." According to Chinese law, however, representative offices of foreign companies may conduct only "indirect business operations." Sino-foreign joint ventures must be created to conduct such operations as negotiating freight rates with shippers and consignees; accepting bookings of freight directly from shippers; issuing bills of lading; billing filed tariffs; and collecting ocean freight and charges from shippers. US carriers not wishing to form joint ventures must rely on Chinese agents for these services, with the result that they have little control over the booking or pricing of their services. Chinese carriers, in contrast, are not required to invest in the United States to carry out these tasks.

• **Carrier tariffs** This issue stems directly from the inability of US carriers to deal directly with Chinese customers. Virtually all Chinese cargo is booked onto US ships through two State monopolies: the China National Foreign Trade Transportation Corp. [(SINOTRANS), a unit of the Ministry of Foreign Economic Relations and Trade (MOFERT)] and PENAVICO, the agent of the China Ocean Shipping Co. [(COSCO), operated by the Ministry of Communications (MOC)]. US sources claim SINOTRANS and PENAVICO refuse to book cargo at tariff rates higher than those of the Far East Navigation Co. (FARENCO), which is owned by MOFERT's Hong Kong subsidiary and acts as a Hong Kong agent for SINOTRANS. According to the FMC order of investigation, the Chinese agents use their "control over collection of ocean freight money to assess and collect freight at less than the rates and charges established by the US carriers in their tariffs"—actions prohibited under US maritime law. Chinese carriers are not subject to US interference in their pricing policies.

• **Port service issues** US officials allege that the operations of US carriers are impeded by restricted on access to dockside facilities and equipment and excessive charges for various port services. For example, while 1990 MOC regulations contain a single set of port-related charges applicable to both Chinese and foreign vessels, US feeder vessels are assessed higher charges for many services than their Chinese counterparts. According to the Chinese, the higher charges "compensate" for harbor and energy taxes—which, according to Chinese law, are supposedly not applicable to US carriers. In the United States, port charges are

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not assessed according to carrier flag.

- **Intermodal services** Just as US carriers' ability to book freight is limited, so is their ability to handle it within China. Under Chinese law, US carriers are prohibited from owning or operating inland container yards and container freight station terminals, trucking services for inland transport of their containers, and "related warehousing activities" unless they form joint ventures for these purposes. Chinese carriers, in contrast, are not restricted from wholly owning such operations in the United States.
- **"Doing business" costs** US authorities allege that US carriers are subject to various charges that are excessively high or discriminatorily applied vis-a-vis Chinese carriers. For example, container-port on/off lift charges are 30 percent less per container for Chinese carriers than for foreign vessels—a situation described as "unacceptable" by one MARAD official. The Chinese claim that national carriers are given favorable rates because they must accept sometimes unprofitable State-assigned voyages and contribute to the fund for energy transport construction.

Looking for a compromise

The FMC has until November 22 to investigate these issues and make its ruling. It has ordered COSCO, SINOTRANS, American President Lines, Ltd., and Sea-Land Service, Inc. to submit motions detailing Chinese shipping practices in these five areas. No oral evidentiary hearings will be held.

Although the Chinese have not yet indicated any intention to re-open negotiations on maritime issues, representatives of US carriers are hopeful that the damage potential-FMC sanctions would inflict both on COSCO and Chinese export performance as a whole will bring them back to the table with serious proposals. Jurisdictional conflicts between MOFERT and MOC—SINOTRANS' business is guaranteed whether COSCO is punished or not—will make it difficult for the Chinese to attempt to address many of the issues being investigated by the FMC. Even if the Chinese do re-open negotiations, US government officials will likely take a hard line, given their perception of China's inadequate fulfillment of the 1988 accord.

The current dispute represents a significant setback for US-China maritime relations, which in many ways seem to be regressing rather than moving forward. While US officials had hoped to negotiate a treaty dealing with more sophisticated issues when the current bilateral agreement expires next year, they are now back to talking about the most basic market access topics. Should these fail to be resolved, both sides will lose—imposition of sanctions or the lapsing of the bilateral accord will only make it easier for third-country carriers to increase their share of US-China seaborne cargo.

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PORT OF OAKLAND

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Top US Ports in the China Trade

Shipping relations between the US and China have undergone significant changes over the past few years. While bilateral trade has risen significantly, it has also become increasingly unbalanced, with the growth in Chinese exports far outpacing that of imports. Reflecting this development, US vessels, though carrying more goods overall, are dealing primarily with US imports. Their Chinese counterparts have also been growing stronger, carrying more consumer goods and other higher revenue cargo.

To stay abreast of the changing trends, US ports involved in the China trade are pursuing closer ties with China and outfitting their facilities to deal more efficiently with the commodities they handle. This tends to vary with the geographic location of the port; those in the south handle large quantities of wheat and crude oil, while ports on the east and west coasts generally handle imports of clothing and toys and exports of cotton and other raw materials. The leading US ports in the China trade are profiled below.

The Port of South Louisiana

Situated between Baton Rouge and New Orleans, the Port of South Louisiana led all US ports last year in foreign trade tonnage handled (90,975,000 tonnes). It was also the US leader in trade with China, although total China trade slipped to 2,484,031 tonnes, a 38 percent drop from 1989. This figure includes 1,807,823 tonnes in exports, almost 94 percent of which consisted of wheat. Chief imports were crude oil and minerals. South Louisiana has no sister port or any special arrangements with ports in China.

The Port of Houston

With total bilateral trade reaching 1,692,140 tonnes—valued at nearly $729 million—in 1990, China became the Port of Houston's second-largest trading partner in Asia, behind only Japan. Imports from China totaled 1,100,570 tonnes, with crude oil accounting for an overwhelming 92 percent of that total. Houston's top exports to China were wheat, which made up 70 percent of the total 591,129 tonnes, and petrochemicals.

As the sister port of Dalian and sister city of Shenzhen, Houston maintains close ties with the mainland and is exploring opportunities for increased trade with China. In August, for example, a delegation led by Director of Trade Don Alli visited Shenzhen, Dalian, and Beijing to discuss plans for expanding trade.

The Port of New Orleans

The first American port to export goods to China after US-China trade relations were normalized, the Port of New Orleans has always played a key role in US-China shipping. New Orleans maintained its important trade position with the PRC in 1990, handling a total of 1,579,549 tonnes valued at $193,301,000. Wheat tops the list of New Orleans' exports, accounting for close to 92 percent of last year's 970,639 tonnes to China. New Orleans also imported 608,910 tonnes of goods from China in 1990, with minerals and crude oil topping the list.

In an effort to develop closer ties with China and sister port Shanghai, the port of New Orleans has been involved in several official and technical exchanges with China, including a delegation led by President Ron J. Brinson earlier this year. In addition, Shanghai Port Authority Deputy Director of Foreign Affairs Bao Hanmin is currently undergoing a four-month training program in New Orleans.

Port Authority of New York & New Jersey

The top port in US-China shipping on the East Coast, New York/New Jersey's total trade with China totaled 579,537 tonnes ($1.5 billion) last year. Imports jumped 16.4 percent from 1989 to 484,144 tonnes, making China New York/New Jersey's sixth largest source of incoming goods. Leading the $1.2 billion worth of imports were food products, plastic and rubber goods, and clothing. In contrast, exports to China slipped 36 percent last year, largely due to decreased sales of the port's leading export commodity, waste paper.

To prevent a further decline in exports, New York is attempting to forge a stronger trade relationship with China. Delegations from the Port Authority and Shanghai exchanged visits last year, and this year, Ministry of Communications Vice Minister Lin Zhuyi toured the New York facilities. Assistant Director of Marketing and Sales Roy Jaeger is currently involved in negotiations with officials from Shanghai to expand trade, and expects another delegation from the Port of New York/New Jersey to visit China early next year.

Port of Oakland

About 3 percent of the Port of Oakland's overall trade is with China. Exports handled by the port in 1990 leapt almost 70 percent over 1989 levels, reaching 44,000 tonnes. Though exports of some commodities such as iron and steel dropped sharply in 1990, Oakland was still a key gateway for China's purchases of textile fibers and raw cotton, organic chemicals, metal ores and metal scrap, and pulp and waste paper. Imports from China, in contrast, dropped about 12 percent in 1990 over 1989 levels, though most of Oakland's China trade remains import-oriented—the port handled over 119,000 tonnes from China last year. Chief imports were metal manufactures, telecommunications/sound equipment, appliances, furniture, textiles, and footwear.

The port's ties to northeast China are particularly strong. The city of Oakland is a sister city of Dalian, while the port of Oakland maintains a sister-port relationship with the Port of Dalian, the second largest in China.

The Port of Seattle

Quick to become one of the top US ports in China trade, Seattle serves as a transit port between China and North America for five major steamship lines: COSCO, Hanjin, American President Lines, Mitsui O.S.K., and Nippon Liner Systems. Total 1990 trade was 327,357 tonnes, valued at $1.4 billion—almost 5 percent of Seattle's overall business. Of the 242,499 tonnes of incoming goods last year, clothing and footwear accounted for about one-quarter of the $1.3 billion in total imports. Exports, which decreased slightly, consisted largely of fertilizers and organic chemicals.

Seattle historically has had strong trade relations with China, and in 1980 was the first to sign a sister port agreement with Shanghai. Seattle has participated in several promotional and educational exchanges with China, and expects a visit from Chinese port officials in September.

—Peter Kuo

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Hong Kong's Shipping Sector

Can the territory recapture its number one status?

Laurence Scofield and D. Peter Boyce

About 200 shipping lines and vessel operators from all over the world call on Hong Kong, offering services to virtually every port on the globe. Sea transportation, which is estimated to account for 90 percent of Hong Kong's international cargo movement by weight and over 50 percent by value, plays a vital role in the territory's economy. Transshipment of cargo, chiefly from China, now accounts for over 20 percent of Hong Kong's container traffic, reflecting the territory's importance as an entrepot for China trade. China's spectacular export performance of late has meant big business for Hong Kong's shipping industry —in 1990, $10.5 billion worth of goods destined for the United States alone were re-exported through Hong Kong.

A global powerhouse

Hong Kong is a natural shipping center, given the territory's deep harbor and emphasis on import/export trade. Hong Kong is also strategically located on many lucrative intra-Asian trading routes, and has long served as China's trading conduit with the outside world. In 1990, over 20,000 ocean-going vessels visited Hong Kong, along with millions of smaller vessels. Together, they loaded and unloaded some 79 million tonnes of cargo.

Although the territory lags behind Panama, Liberia, Taiwan, and Singapore (the latter two of which have significant government-supported fleets) in the number of ships registered, it is a leader in container handling. From 1987-89, Hong Kong ranked as the world's busiest container port, though Singapore overtook it in 1990. Hong Kong's seven container terminals at Kwai Chung provide 12 berths with a total capacity of approximately 5 million TEUs (twenty-foot equivalent units). Though these land-based facilities handle most container traffic, approximately 25 percent of all container loading is performed midstream by lighters that dock alongside ships at mooring buoys—at a cost averaging half that charged by the Kwai Chung terminals.

From 1987-89, Hong Kong ranked as the world's busiest container port, though Singapore overtook it in 1990.

China's entrepot . . .

Hong Kong's shipping industry is intricately linked to the US and Chinese economies and their trading patterns. As one pundit noted, "When China sneezes, Hong Kong catches cold." After the crackdown on demonstrators in China in mid-1989, there was an atypical slump in the volume of Chinese trade through Hong Kong, as China's customers maintained a "wait-and-see" attitude on future trade with the mainland. According to the Hong Kong Shippers Council, the number of containers discharged in Hong Kong was 1-5 percent lower each month of the July-December 1989 period compared to the same months the year before. In 1988, in contrast, the monthly throughput for the same period averaged about 25 percent over the previous year's levels. The decline lasted throughout 1990, but throughput was back up by 1991.

China's trade with the United States is particularly important to Hong Kong's shipping sector, as about 30 percent of China's re-exports through Hong Kong are destined for the US market. In 1990, slightly over 1 million tonnes of cargo was transshipped from Hong Kong to the United States, mostly in containers. Among the main goods transshipped were textiles, apparel, manufactured goods, and electrical appliances. A good third of the cargo entered the United States through the Port of Long Beach, California, while the ports of Los Angeles, New York, and Tacoma, Washington each took in over 100,000 tonnes of Hong Kong containers last year.

Despite this booming re-export trade, political tensions between the United States and China—especially the battle over renewal of China's Most Favored Nation (MFN) status—have been a source of growing concern to Hong Kong's shipping industry. Loss of MFN would likely result in the territory losing an estimated $6 billion—or 7 percent—of its total export earnings, according to the Hong Kong Shippers Council. Without MFN, China's exports to the United States could fall anywhere from 20-80 percent. Hong Kong, as the major entrepot for Chinese transshipments to the United States, would quickly feel the pinch, and its shipping sector would be hard hit.

. . . and gangway

Although Hong Kong relies heavily on the money and jobs its entrepot role afford, China's dependence on Hong Kong as the conduit to external markets is even more marked. About 20 percent of the exports China transships through Hong Kong enter the territory via road or rail, with the rest entering by ship. The preference for water transport has resulted in a host of shipping

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lines, both coastal and ocean-going, plying the waters between Hong Kong and China's major ports.

Most of the goods transshipped through Hong Kong are made in China from materials supplied by Hong Kong companies under contractual export arrangements, a process known as "outward processing." Over 60 percent of Hong Kong's imports from China are of this nature, while 80 percent of the territory's domestic exports are for outward processing in China. An estimated two million Chinese workers are employed in Guangdong Province by Hong Kong firms producing goods for export.

Hong Kong-based trading companies handle shipping arrangements for most of these goods, booking space on vessels and lining up import and consolidation services as required. Several thousand such companies thrive in the territory, ranging from small "one-telephone" operations to branches of large multinational trading companies. Their counterparts in China are far fewer, and typically consist of State-run or officially sanctioned trading companies such as SINOTRANS and PENAVICO, which can provide warehousing, vessels, and inland transport (*see* p. 18). Ensuring a smooth transit of cargo from Chinese factories to port generally requires considerable patience, and many Hong Kong shipping companies complain of delays over paperwork, corruption at border crossings, and inefficiency in the day-to-day operations of the Chinese trade intermediaries. Increasingly, Hong Kong trading companies are finding their own contacts within these agencies to help them better navigate the Chinese bureaucracy.

Shipping between China and Hong Kong is dominated by small feeder vessels, which bring cargo from areas deemed uneconomical by large shipping lines. Often, the volume of exports from Chinese ports is too unpredictable to attract large ships, which typically prefer full loads. In addition, common cargoes such as agricultural commodities, food, or bulk items are often too low in value to interest large vessels, except for those of Chinese carriers.

New competitors

Aside from the potentially huge

China's spectacular export performance of late has meant big business for Hong Kong's shipping industry.

impact China's strained relations with the United States might have on Hong Kong's shipping industry, changing relations between China and other regional players may also have damaging consequences. For instance, Hong Kong will lose out if the mainland and Taiwan reach a direct trade agreement, since virtually all trade between the two sides is currently transshipped through Hong Kong. In 1990, for example, nearly 20 percent of the ships departing Hong Kong headed toward Taiwan as their first country of call. Direct shipping links between South Korea and China may be less of a threat, since cross-border trade between South Korea and China has been going on for some time.

Both of these areas are also in the process of expanding their port facilities. Taiwan is planning to build a new container port on the southern end of the island by the end of the century, in order to handle the increased trade expected to result from a thawing of relations with China. South Korea is building a massive container port to the east of Pusan, while beefing up existing facilities at its major ports. US vessels in particular could conceivably bypass Hong Kong for these transshipment hubs, since transit times there are faster and the new facilities could prove much cheaper than those in Hong Kong. In addition, new facilities in Thailand, Malaysia, and Indonesia could be active players by the end of the decade, particularly in intra-Asian trade.

Closer to home, the improvement of port facilities just across the Hong Kong-China border in the Shenzhen Special Economic Zone may bring new competition to Hong Kong's entrepot role. Shenzhen's port of Shekou, for example, is scheduled to begin expanded operations in late 1991, making it possible for carriers to make a direct call in southern China and bypass Hong Kong altogether. In addition, the costs of using Shekou's container terminal and general cargo services are projected to amount to just half of Hong Kong's port costs.

Hong Kong should not lose too much business to its new Chinese competitors, however, at least not in the near term. Hong Kong exporters prefer to use warehouses and storage facilities in Hong Kong rather than in China, since local forwarders and shippers can personally view the goods and oversee quality control before the products are packaged for export and shipped out. This preference is unlikely to change in the near future, though the costs of warehousing operations in the territory could eventually prod companies into setting up such facilities across the border.

Surging costs

A greater financial threat is the rising cost of the territory's container terminals, which could potentially price Hong Kong's facilities out of

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the market. Though Hong Kong's container facilities are among the fastest and most efficient in the world, the percentage of box cargo handled mid-stream is increasing because of rising costs and the reluctance of terminals to cater to the needs of small feeder vessels. Alarmed by these trends, Hong Kong shipping lines and terminal operators have urged the Hong Kong government to assist in financing lower-cost container-handling facilities to help maintain a healthy volume of container traffic. The government, however, maintains that the mid-stream operations—which are cheaper to use but less efficient than the land-based terminals—actually help lower shipping costs, and will help ease congestion at the terminals until additional privately financed facilities come on line. Even if this is true, the high costs of Hong Kong's container-handling facilities will threaten the position of the territory's shipping industry in the meantime.

In addition, general port charges in Hong Kong are higher than at many competing Asian ports, some of which have not increased their fees in several years. Singapore, for example, is known for its low charges, and gives carriers rebates for quick turnaround in loading and unloading. Though some Hong Kong terminals argue that shipping lines are not concerned about port charges because they can pass these costs on, higher freight costs tend to encourage the proliferation of small, independent carriers who use smaller, cheaper facilities to keep their costs down. In addition, simply passing on port charges to importers might encourage them to look elsewhere for cheaper goods and shipping services. Low-value cargo is unlikely to be shipped via Hong Kong, where the average rate of HK$1000 for handling a TEU could be more than the value of the cargo.

Flying the Hong Kong flag

Aware of these potential dangers, the Hong Kong government is actively seeking other ways to protect the territory's shipping industry. Hong Kong's Port and Airport Development Scheme (PADS) includes the construction of new container facilities on Stonecutters, Tsing Yi, and Lantau islands, though most of the capital and infrastructure costs are to be borne by private investors (*see The CBR*, May-June 1991, p.38). While many of the financial details have yet to be worked out, Beijing's approval of the project will likely encourage investors to support the new container terminals and the infrastructure necessary to link them to the mainland.

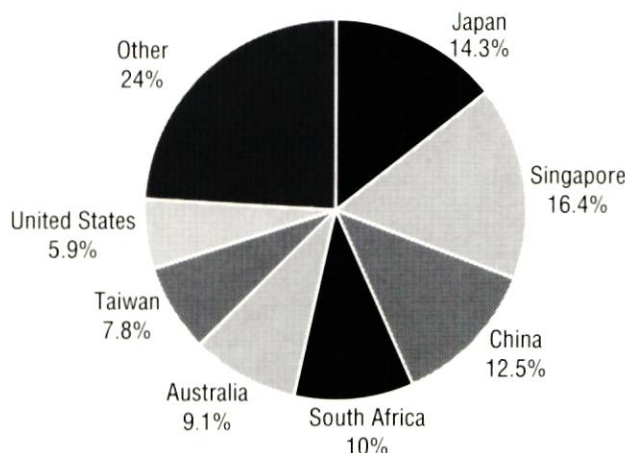
At the same time, government officials are optimistic that the newly established Hong Kong shipping register, which opened in December 1990, will encourage the territory's many shipping lines to continue to operate out of Hong Kong even after it reverts to China in 1997. Members of the Hong Kong Shipowners Association own or manage over 1,300 ships, though many are registered elsewhere—in as many as 30 different countries. This is partly the result of previous laws, which stipulated that Hong Kong ships be registered under the United Kingdom's shipping register. Many of the territory's ships, however, sought out ports of registry that were closer to home or offered lower fees. Even though Hong Kong-registered vessels will continue to be considered British ships until 1997, the establishment of the Hong Kong shipping register should encourage more Hong Kong shipping lines to seek the ease and convenience of registering their vessels locally.

The new register may also help Hong Kong retain the custom of the major lines serving the Hong Kong-North America and Hong Kong-Europe routes, since it is open to any incorporated body in Hong Kong, as well as to overseas companies registered in the territory. Staying competitive will require Hong Kong to make further efforts to strengthen its shipping sector and cargo facilities; otherwise it risks losses to its shipping lines and its port—both of which would have severe repercussions on the quality of life in the territory. 完

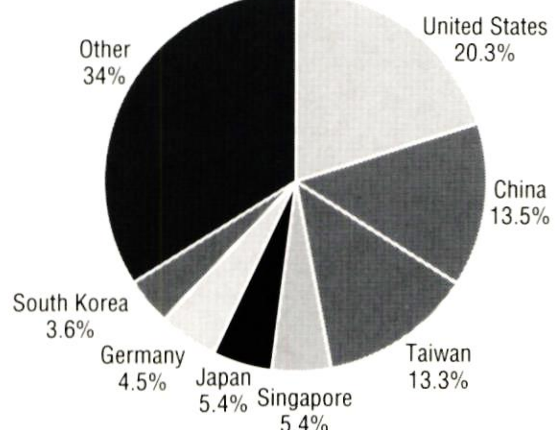
Major Countries of Loading/Discharge for Port of Hong Kong

Share of 1990 tonnage

Seaborne imports



Seaborne exports (including re-exports)



SOURCE: Hong Kong Shippers Council

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Air Cargo Takes Off

US airborne trade with Hong Kong and China is soaring to new heights

Charles D. McKee, Jr.

Expanding trade between the United States, Hong Kong, and China has meant big business for air carriers connecting these three areas—the volume of cargo transported by air has risen at or near double-digit rates over the past decade. Good prospects for continued growth hold forth the promise of even better business in the future, though competition among airlines is increasing apace. In addition, political uncertainties, such as the possibility of changes in the bilateral agreements governing air services between these areas, could dim this bright picture. Such factors will necessitate careful planning and prudent deployment of aviation resources to profitably exploit demand for air-cargo lift in the next decade.

The growth in demand for air-cargo lift between the United States, Hong Kong, and China parallels that between the United States and other Asian markets; total trans-Pacific volume averaged 23 percent annual growth from 1980-89. This growth reflects the dynamic economies of the Pacific Rim countries, the move toward "just-in-time" manufacturing and retailing systems in the United States, and the increasing competitiveness of US exports as the dollar weakened against most currencies in the region.

Demand for air cargo may also be traced to the growing diversification and sophistication of the trade of Asian countries, which typically import high technology and telecommunications equipment in addition to perishable foods by air, and export consumer goods, electronics, and perishables to the United States. Shipping by air is not cheap; changes can be as much as 300 percent more per pound than sea rates. Accordingly, there must be the need for immediate market delivery or sufficiently high mark-ups on the goods shipped to warrant the extra cost.

Shipping by air can cost as much as 300 percent more per pound than shipping by sea.

The Hong Kong-China link

Hong Kong's share of air trade with the United States is the third largest in the Asia-Pacific region, after Japan and Taiwan. Goods from Hong Kong currently account for 15 percent of the US-trans-Pacific market, compared to 30 percent in 1970.

This downward trend in market share is the result of faster relative expansion in the markets of other Asian countries—notably Taiwan and South Korea—and not an omen of Hong Kong's demise as a trading center. Airborne trade between the United States and Hong Kong has more than doubled in volume and quadrupled in value since 1980, with total trade reaching over 130,000 tons and $8.05 billion in 1990.

An increasing amount of this trade is in goods originating in China, for which Hong Kong serves as a gateway. Estimating the exact value of Chinese goods re-exported through Hong Kong is difficult, since goods originating in China but assembled in and shipped out of Hong Kong are sometimes listed as Hong Kong domestic exports. Official Hong Kong statistics value China's 1990 re-exports through Hong Kong to the United States at $6.1 billion, a 14.7 percent rise over 1989, though the actual value is undoubtedly higher. An estimated $1 billion worth of these exports were transported to American markets by air. Re-exports from China should continue to increase as Hong Kong's direct investment in Chinese manufacturing facilities continues.

Not all air cargo between the United States and China is shipped through gateways like Hong Kong; an increasing amount is being shipped direct. Air cargo trade between the two countries grew from a mere 4,700 tons in 1980 to 54,320 tons in 1988, and may exceed 70,000 tons this year. (This volume is calculated on the basis of US customs declarations listing China as the country of origin.) The directional balance of this trade, however, is also growing more lopsided.

Evening out cargo flows

With the exception of China, the United States' improved export performance since the late 1980s has helped even out directional imbalances in air-cargo traffic with the Pacific Rim. An imbalance—particularly for an all-freight carrier, which cannot allocate unused cargo space to passenger baggage—wastes the profit-earning potential of the flight sector. Throughout the 1970s and early 1980s, bilateral trade flows favored Hong Kong's exports 4:1, making for under-used, often unprofitable services from the United States (*see* table).

Since 1985, however, US air exports to Hong Kong have grown faster than Hong Kong's to the

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United States. In 1990, for example, the value of US exports to the territory climbed 11 percent over the previous year, while the value of Hong Kong's exports to the United States slid 6.3 percent. Should growth in Hong Kong's imports from the United States continue to rise at current levels, parity will soon be reached in the value of goods transported in each direction.

In the case of China, the small but burgeoning air trade with the United States continues to be dominated by Chinese exports, in line with the general trade imbalance between the two countries. The dominant westbound products—US exports of fertilizers, synthetic materials, wood, and agricultural products—are all more suitable candidates for sea travel. Therefore, the directional imbalance in air cargo markets between the United States and China is unlikely to change soon, even though the overall market will continue to grow at one of the fastest rates in the Pacific.

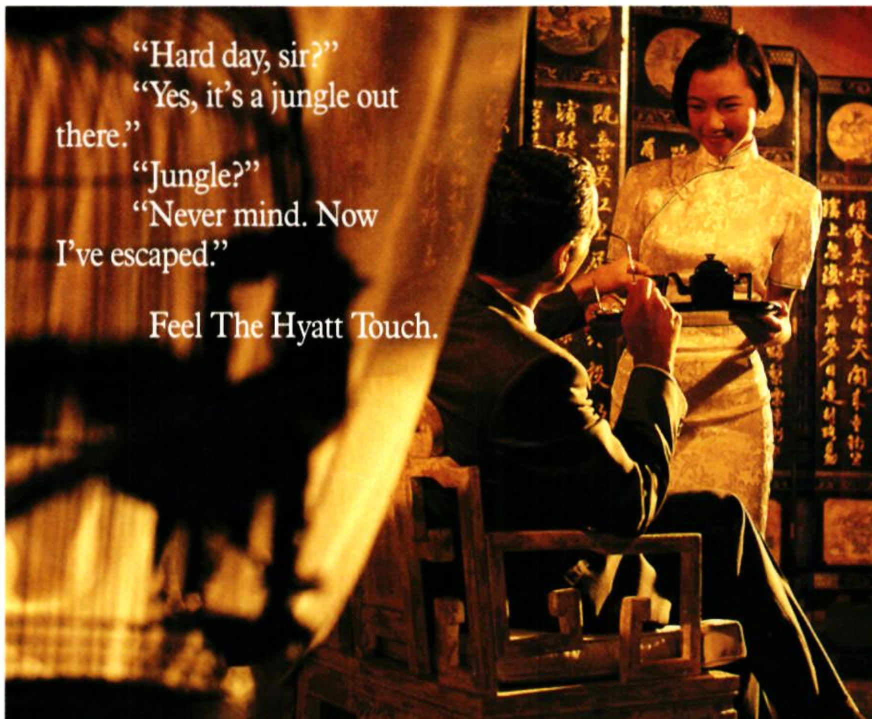
Increasing competition

An expanding group of airlines is seeking to capitalize on the growing US-Hong Kong-China market, offering cargo lift either on all-cargo flights or in the aircraft belly of passenger flights. Currently, eight carriers offer 52 direct flights a week from Hong Kong to eight US cities—a 200 percent increase over the number of trans-Pacific flights and carriers 10 years ago. In the last year, heavyweights American Airlines Inc. (in conjunction with Cathay Pacific Airways Ltd.) and Delta Air Lines Inc. have started freight and passenger service to Hong Kong, and US freight carriers are increasing the number of ad hoc flights they are flying to the territory.

Though competition for the China market has been less intense, service there has also increased to keep pace with rising demand. Direct air cargo services between the United States and China began in 1981, with CAAC and Pan Am each offering two flights a week between Beijing/Shanghai and San Francisco/New York. Today, United Airlines, Air China, Northwest Airlines, and China's new China Eastern Airlines all provide service between the United States and China.

Competition for trans-Pacific routes is increasing not just among US airlines, but also among Asian airlines offering indirect services to the United States through their home country airports. The US Department of Transportation estimates that US carrier market share on trans-Pacific routes out of Hong Kong slipped from 56.9 percent in 1980 to around 50 percent by the end of the decade. The downward trend is largely due to increasing competition from Asian carriers, but also reflects the reduced cargo capacity and passive marketing efforts of US airlines.

Of the major US carriers plying the Hong Kong route, only Northwest



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Airlines has a fleet of all-cargo freighters in addition to conventional passenger aircraft. United Airlines sold its all-cargo aircraft in 1984, about the time it purchased Pan Am's Pacific division. United has been unable to fill the cargo void left by Pan Am, a problem exacerbated by payload range restrictions on the low-capacity, ultra-long range Boeing 747SP United has used on the important Hong Kong-San Francisco route. This problem has now been eased somewhat with the introduction of the larger-capacity Boeing B747-400 on this route.

Asian carriers, in contrast, have made substantial commitments to acquiring freight capacity. Japan Airlines, with more than 10 freighters, has the largest all-cargo aircraft fleet in the Pacific. But Cathay Pacific, Air China, Thai Airways International Ltd., Singapore Airlines Ltd., Korean Air, Malaysia Airline System, and China Airlines Ltd. (Taiwan), among others, also have all-cargo aircraft. Hong Kong-based Cathay Pacific currently has three wide-body freighters, and expects delivery of two more by 1995.

Cathay Pacific's all-cargo aircraft have been deployed primarily to Europe and Australia, while its passenger planes fly the Hong Kong-Los Angeles route. Air Hong Kong, an all-cargo airline owned by Stanley Ho-controlled Shun Tak Enterprises, has also targeted Asia and Europe, flying only an occasional charter to the United States. The airline plans on acquiring two B747 freighters in the near future, and last March applied to Hong Kong's Air Transport Licensing Authority (ATLA) for scheduled route rights to the United States and other countries. ATLA, however, enacted a "one route-one airline" policy in the mid-1980s, which has effectively denied Hong Kong-based airlines the opportunity to compete against one another on virtually all routes. As many of Air Hong Kong's requests are for cities already served by Cathay Pacific, it is unlikely that the carrier will obtain most of the scheduled rights it desires.

Until it secures scheduled route rights to the United States and obtains larger-capacity aircraft, Air Hong Kong will not become a significant player in US-Hong Kong air cargo services. Cathay Pacific, given its limited services to the United States, only holds about 3 percent of this market. While the two carriers command greater shares of other Hong Kong routes, Cathay Pacific claims more than 70 percent of total Hong Kong air cargo is transported by foreign airlines.

US integrators score big

Although US carriers now transport a smaller percentage of US-Hong Kong cargo than they did 10 years ago, strong performance in new cargo-market niches may help reverse the decline. For example, in the fastest growing segment of the market—express letters and small packages—US "integrators"(companies offering door-to-door services) are the dominant players. By using "hub-and-spoke" routings and advanced computer tracking systems, small package integrators can offer services to more cities faster than carriers using traditional freight systems. Thus far Federal Express and United Parcel Service (UPS) have captured the lion's share of Hong Kong's trans-Pacific express letter/small package market, which is estimated to be growing at 25 percent in volume per year.

The market in China is considerably smaller, and therefore has received less attention. In addition, such problems as customs clearance delays, lack of reliable ground support, and uncertain eastbound demand for premium delivery services

Air Cargo Between the United States and China/Hong Kong

By volume (x 1000 pounds)	1980	1985	1988
US imports from China	6,729	34,954	93,873
US imports from Hong Kong	92,791	175,042	179,734
US exports to China	2,775	13,986	14,676
US exports to Hong Kong	27,343	38,943	67,749

By value ($ million)	1980	1985	1988
US imports from China	86	337	1,001
US imports from Hong Kong	1,410	2,713	3,903
US exports to China	90	670	775
US exports to Hong Kong	778	1,061	2,543

SOURCE: *US Department of Commerce*

have kept some integrators away from China, although DHL International Ltd. and TNT Ltd. offer express mail services via commercial airline flights to major Chinese cities.

Expanded Fifth-Freedom rights?

Airlines offering service between Hong Kong/China and the United States via their own countries do so by exercising Fifth-Freedom rights. These rights are obtained only after holding a series of bilateral negotiations between the governments of the origin, destination, and interim-stop countries.

Fifth-Freedom is a coveted right, as it allows an airline additional revenue-generating potential by permitting it to discharge and pick up cargo or passengers in an interim country before proceeding to a destination country. Given Hong Kong's regional commercial and tourism appeal, airlines have long valued having Fifth-Freedom rights to or through the territory. The major Fifth Freedom carriers in the Hong Kong-trans-Pacific market are All Nippon Airways, Japan Airlines, China Airlines, Korean Air, Singapore Airlines, and to a lesser extent, Philippine Airlines. All offer daily cargo services as an adjunct to their passenger flights between the United States and Hong Kong. Of the US carriers, United operates Fifth-Freedom flights through Hong Kong to Bangkok, while Northwest holds, but does not use, Fifth-Freedom rights through the territory.

> ***It is possible that additional carriers flying trans-Pacific routes to/from Hong Kong and China will be granted Fifth-Freedom rights in the future.***

Fifth-Freedom carriers are also very important for services between China and the United States. The major Fifth Freedom airlines in this maket are Japan Airlines, All Nippon Airways, and Lufthansa German Airlines, which provides onward service to the United States through its Frankfurt base. While no statistics are publicly available, Japan Airlines' market share of China-US cargo is probably at least equal to Air China's.

It is possible that additional carriers flying trans-Pacific routes to/ from Hong Kong and China will be granted Fifth-Freedom rights in the future. Hong Kong, with nods from both the British and Chinese governments, has begun negotiating its own air service agreements with foreign countries—something previously

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done on its behalf by the United Kingdom. Article 189 of the Basic Law will allow the territory to continue to negotiate such agreements even after 1997. Currently, the Hong Kong government is discussing with the United States a bilateral agreement on future air services between the two destinations. Chances are the number of Fifth-Freedom carriers serving the two will not change greatly; nor is it likely that any major discord will result.

As the United States is also close to concluding a new air service agreement with China, however, it is possible that provisions will be made for a Chinese carrier like Air China to begin Fifth-Freedom services through Hong Kong to the United States. Air China has no such rights at present, but vaguely worded Article 138 of the Basic Law appears to allow for this provision. The question is whether the matter will be addressed now or deferred for later rounds of talks. Although perhaps inevitable, the granting of Fifth-Freedom rights to China is certain to be an emotional issue, as some residents of Hong Kong will be uncomfortable with the idea of Air China operating international services from the territory prior to 1997.

Little turbulence ahead

Forecasting experts throughout the aviation industry predict everything from solid to spectacular growth rates for the Pacific Rim air-cargo market over the next decade. At The Boeing Co., analysts estimate that eastbound traffic will grow 7.2 percent annually and westbound traffic 9.1 percent per year through the year 2000. Analysts at Airbus predict that bi-directional cargo growth across the Pacific will average 7 percent per year. While helpful for market planning, such forecasts cannot adequately weigh the important influences changing trade composition, competitive environments, and political directions will play on demand and capacity for air-cargo services.

One of the most important issues in future air trade between the United States, Hong Kong, and China will be the continuation of China's Most Favored Nation (MFN) status; its presence or absence could act either as a stimulus or a depressant on future growth of air trade. Non-renewal of MFN would probably increase the number of Chinese goods slipping into the United States under the Hong Kong label, which would increase demand for air service from Hong Kong, but retard air service growth to China. Alternatively, the continuation of MFN would probably result in the China air-services sector growing at current levels for the foreseeable future.

Other concerns center on the ability of Hong Kong's airport to cope with increased demand for air cargo services. Cargo facility at Kai Tak is being doubled by the Hong Kong Air Cargo Terminals Ltd. (HACTL), but runway and ramp space congestion will probably result in the airport as a whole hitting capacity sometime in the next three years. The new airport at Chek Lap Kok, meanwhile, will not be ready until the end of the decade (*see The CBR*, May-June 1991, p. 38). Should Kai Tak's shortage of capacity become dire, cargo traffic undoubtedly will be diverted to surrounding airports, such as the new facilities in Macao and Shenzhen. Airline planners from some of the large US carriers have already been spotted inspecting the Macao site.

In China, the issue is not so much capacity as basic aviation infrastructure. Although airport infrastructure is improving and some airlines have noted increasing efficiency in Chinese airport operations, improvements are required in air-traffic control equipment and procedures.

From a commercial standpoint, a host of "doing business" problems also plague development of the aviation sector in China. Matters ranging from the remittance of foreign exchange to the import of essential aircraft and office supplies all require patience and contacts within the Chinese bureaucracy. Perhaps more important, some foreign airlines charge that they are restricted in their ability to market cargo and passenger services, to the benefit of Air China. These questions must be addressed before air service can be expanded and market growth exploited.

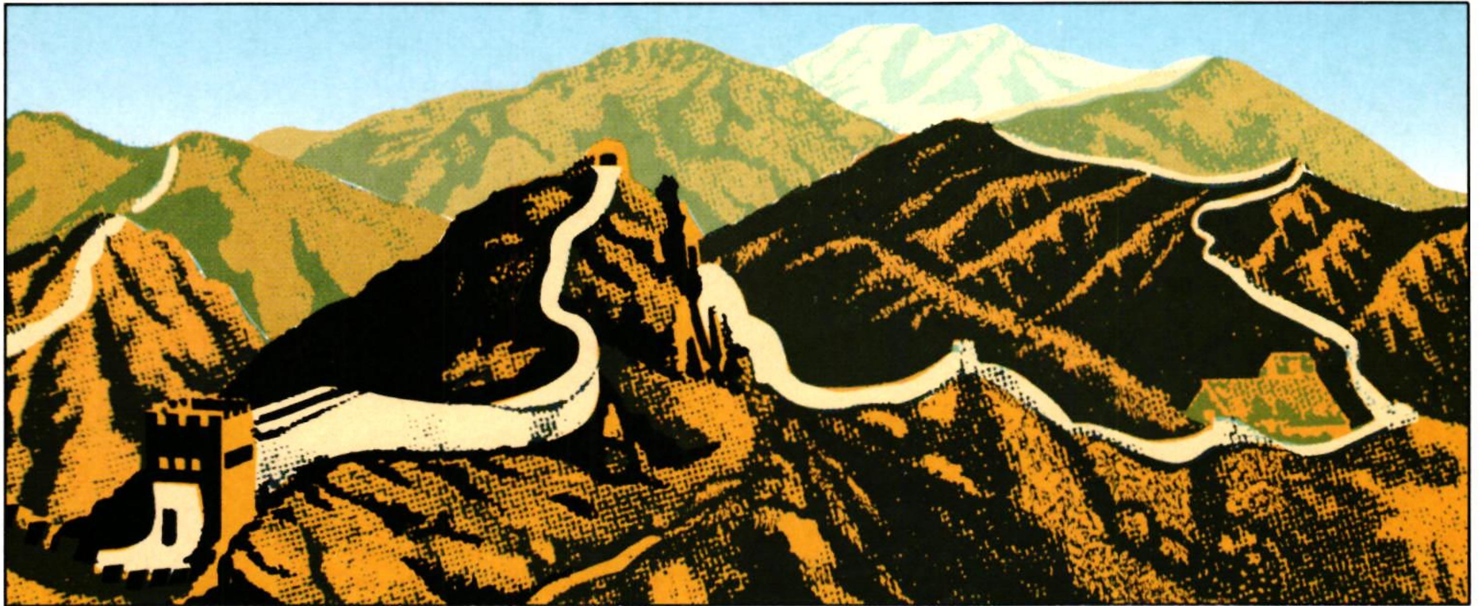
Whatever the outcome of China's business practices or Hong Kong's airport problems, it is likely that more carriers will be vying for business in the coming years. On average, this increased competition will not result in dramatic price decreases, except perhaps in the express integrator market, where carriers are aggressively pursuing battles for market share—and even there low prices can be expected only in the short run. It is more likely that prices will gradually be raised as the recession lifts in the United States. Service, however, should improve. Therefore, both carriers and shippers stand to profit in the long term.

Hong Kong-US Air Cargo Rates*

	Japan Airlines		Northwest Airlines		United Airlines		Korean Air	
Weight	East Coast	West Coast	East Coast	West Coast	East Coast	West Coast	East Coast	West Coast
under 45 kg	$9.70	$8.27	$9.07	$7.73	$9.70	$8.27	$9.70	$8.27
45-99 kg	$7.46	$6.39	$6.97	$5.97	$7.46	$6.37	$7.46	$6.39
100-299 kg	$6.56	$5.60	$6.13	$5.23	$6.56	$5.60	$6.56	$5.60
300 kg- up	$3.75	$3.21	$3.50	$3.00	$3.75	$3.21	$3.75	$3.21

*Published rate per kilogram(kg)

Compiled by Christa A. Rogers



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Home Office Computing in its May '90 issue about TianMa

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Off and Running

Growth in China's textile production will continue to outpace that of the rest of the economy

Steve Rasin

China will become the world's most influential textile player in the 1990s, directly and indirectly affecting global markets as both a buyer and a seller. The past 10 years of open trade and investment have been very good for the Chinese textile industry, which had been shackled by years of neglect, technological isolation, and government mismanagement. With the advent of economic reforms in the early 1980s, textile production took off at a rapid pace, growing by 18 percent annually throughout the decade.

Foreign trade liberalization and the expanding role of foreign investment and sourcing, particularly from Hong Kong, have played an important role in revitalizing the industry. Between 1980-90, Chinese exports of textiles and garments grew 13 percent per year, and are now the country's most important foreign exchange earners (*see* graph). In 1990 textile exports generated $13.8 billion, nearly a quarter of total export earnings. Some 11 percent of global textile output now carries the "Made in China" label.

Maintaining this rate of growth in the decade ahead will mean confronting new challenges—but barring unforeseen political upheaval, the textile sector will likely outpace the rest of the rapidly expanding economy. According to a study of the Asian textile industry recently completed by Technomic Consultants Far East Ltd. in Hong Kong, China's textile and garment output is projected to expand at a healthy 7-10 percent annually through the end of the decade.

Industry growth during the 1990s will be driven by rising demand both at home and abroad. Strong domestic demand, led by increasingly sophisticated urban consumers, will underpin production volume, while continued export growth will improve overall industry efficiency and help raise quality standards. The demand for higher quality raw materials, such as synthetic fibers and processed fabrics, will drive domestic and selective foreign investments to upstream industries, thus adding important breadth to an industry still dependent on imports for even medium-quality production.

Foreign trade liberalization and the expanding role of foreign investment and sourcing, particularly from Hong Kong, have played an important role in revitalizing China's textile industry.

Boosting production . . .

Several critical developments over the last decade set the stage for the Chinese textile industry's rapid growth. The most important factor was probably decentralization, which transferred investment and production decisionmaking from central planners to local enterprises (*see The CBR*, September-October 1986, p. 31). Decentralization allowed the textile industry, increasingly dominated by small- and medium-sized rural and collective enterprises, to respond more flexibly to market conditions. Improved market responsiveness led to the growing concentration of textile factories along China's eastern seaboard, particularly in the southern provinces. Domestic pricing and distribution practices became increasingly market driven, especially among garment assemblers, who require less technology and financial support from the State. This trend was less prevalent in the spinning and weaving sectors, which are still dominated by State-owned enterprises.

At the same time, rapidly rising disposable incomes increased domestic demand for textiles, fueling the industry's growth. By 1989, the average rural resident spent about $7 annually on clothing, while urban residents spent nearly $30, up from $4 and $13 respectively in 1981.

. . . and foreign investment

Reforms in the foreign trade regime had an equally dramatic effect on textile production, particularly in the south. Foreign participation through investment, technology transfer, and trade has grown in tandem with the liberalization of the industry. Though still accounting for a small portion of overall industry output, foreign-affiliated textile and garment production has had a disproportionate impact on industry development and export performance.

As the industry has developed, it has increasingly looked abroad to

Steve Rasin is a senior associate with Technomic Consultants Far East Ltd., the Hong Kong office of Technomic Consultants International. Technomic Consultants Far East recently completed a comprehensive analysis of Asia's textile industry.

supply necessary inputs. Given the inability of the spinning and weaving sectors to meet the surging demand of downstream garment makers, China has become a growing importer of synthetic and blended yarns and fabrics; printed, dyed, and specially processed fabrics; and other critical inputs not locally available in sufficient quantity or quality. China's yarn and fabric imports, for example, have increased 13-fold since 1978, reaching $2.7 billion in 1990. Import volumes of these goods have fluctuated, however, and the resulting global swings indicate that China has become an important player on the global market. Chinese purchases of acrylic fibers, for instance, pushed global prices to a peak in 1988, but prices slumped a year later when Chinese imports of the fibers were halved.

On the export side, foreign trade liberalization resulted in a wide array of Chinese trading companies licensed to trade in textile goods, which facilitated both imports of raw materials and exports of finished goods. At the same time, factories in the south benefited from the comparatively free markets in foreign exchange, which allowed them easier access to critical imports. The textile industry also benefited from export subsidies during the early 1980s, though decentralization gradually decreased the role of these subsidies. Although this year State-mandated subsidies have supposedly been removed, some provinces seem to be taking up the slack to buoy exports. In any case, garment exports are likely to remain strong in the future.

China's export drive will continue to be fueled by an increasing amount of foreign investment in the textile sector. Led by Hong Kong companies—which now account for nearly 70 percent of total foreign investment in China—the first wave of foreign investment was directed toward low-capital and labor-intensive projects, primarily in export garment assembly. Though a precise measure is not available, the Technomic study estimated the territory's share of investment in the textile industry to be over 85 percent. Some industry analysts feel that as much as 65 percent of China's total garment exports are tied to Hong Kong manufacturers.

The dominant role of Hong Kong

Most foreign investment has been decidedly low risk and low tech.

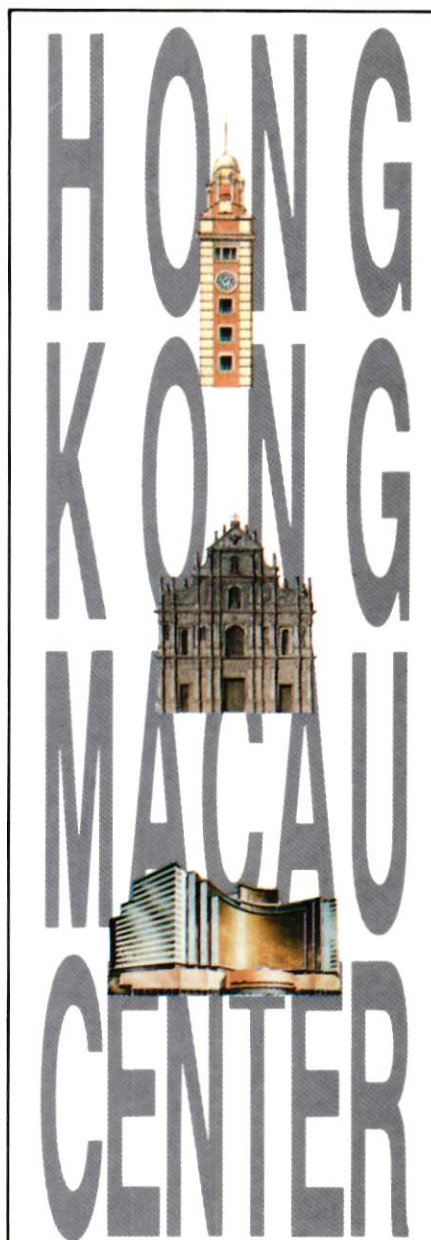
in China's textile sector comes as little surprise, given its long history as the world's garment powerhouse. Since the mid-1980s, however, much of Hong Kong's production capacity has moved into southern China, particularly Guangdong Province. Entire Hong Kong factories have been known to move overnight to new Chinese locations where land and labor costs are only a fraction of those in Hong Kong.

Hong Kong textile companies are not the only ones taking advantage of China's low labor costs. Since the mid-1980s Taiwan companies fleeing rising production costs at home have also moved to the mainland. To date, total Taiwan investment in all sectors is estimated at over $2 billion, and is expanding rapidly as Taiwan-China relations thaw. About 20 percent of Taiwan investment is estimated to be in textiles.

Japanese trading houses and garment manufacturers are also looking to China for low-end products such as socks and underwear. The involvement of Japanese firms is significant, since they typically purchase only high-quality products and should thus help raise overall quality standards in the Chinese industry.

Most foreign participation in the textile industry thus far has been in the form of joint ventures or contract export-processing, whereby the foreign contractor supplies all required raw materials and pays the commissioned Chinese factory a processing fee, usually based on volume. Most joint ventures are valued at less than a million dollars, reflecting the low risk of Hong Kong investments; even less investment is required in contract export-processing ventures. In some cases contracting companies merely supply machinery, usually transferred fully depreciated from factories in Hong Kong, and accept payment in the form of finished goods for export.

During the most recent round of trade disputes between the United States and China, Beijing argued that Chinese firms add only 7-8 percent in



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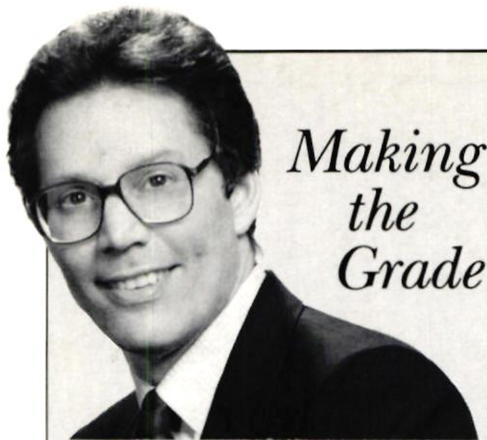


Making the Grade

William N. Simon is managing director of Odyssey International Pte. Ltd., a Hong Kong-based company with subsidiaries in 15 countries, including the United States. Comprised of manufacturing and design operations in Asia, the United States, and Europe, the group's subsidiaries include such outdoor and sports companies as The North Face, Sierra Designs, Frank Shorter Sportswear, and Head Sportswear Japan. Simon recently spoke with Associate Editor Vanessa Lide about the company's operations in China.

CBR: *When did your company start buying from China? Where else do you source your products?*

Simon: Odyssey started buying from China in 1978, and now works with 75 factories in nine provinces. We specialize in very high quality, labor-intensive products—primarily garments and outdoor sportswear—for which we supply 80 percent of the raw materials to the Chinese. For the past three years, we have been manufacturing a steady 30 percent of our products in China. The rest are made in Malaysia, Hong Kong, Arizona, Texas, Utah, and Scotland. Odyssey also subcontracts production to factories in Thailand, Indonesia, Sri Lanka, South Korea, Singapore, the Philippines, and Macao.

Though we have no direct investment in China, we are currently involved in two compensation agreements there, through which we have supplied $3.5 million in machinery and equipment to new factories in Guangdong Province. The Chinese have met their export commitments in an honorable and timely fashion.

CBR: *What are the benefits—and the drawbacks—to sourcing in China?*

Simon: We prefer China for the most complex, labor-intensive production. We find Chinese factories, when properly informed about our needs, to be responsive, cooperative, and able to produce extremely high quality products. We also find the integrity level of Chinese officials and factory managers to be higher than that found in most other third-world countries.

The drawbacks relate to the relatively high degree of supervision required to achieve the quality and production timeliness we need. Odyssey operates seven official production control offices in China, staffed by Hong Kong and Chinese nationals. In addition, we maintain a large logistics and service staff in Hong Kong to purchase and transport raw materials; make samples, patterns, and cutting markers; test materials and accessories for quality before shipping them to China; prepare detailed contracts and instructions for factories; and schedule production for each factory.

CBR: *What is your perception of China's textile sector?*

Simon: In general, the garment and textile sector in China is steadily improving. While the standard of buildings, equipment, and management skills are behind those of many other Asian countries, remarkable progress has been made during the past 13 years. Individual initiative and profit incentive schemes for businesses within China are spurring advances every day. The only thing missing is foreign training to improve efficiency and productivity. However, as more foreign companies invest directly, the opportunities for Chinese workers to become exposed to foreign technology will increase. I am optimistic about the future of China's garment and textile industry.

CBR: *How do you deal with the complex textile quota system, which can leave importers stuck if quotas on their products are filled after they've initiated shipment?*

Simon: Quotas and their management continue to be a serious problem for the Chinese government. Invariably, "hot" categories for products bound for the United States and Europe get overused. Often more quotas are issued than are actually available, and merchandise either gets embargoed or enters only because China borrows from the following year's allocations. The following year's plans are then disrupted. Thus, we do not rely on China's ability to monitor the use of quotas, but consult US agencies tracking the actual entry of goods in each quota category into the United States. To be on the safe side, we normally do not schedule production in hot categories for the last three to four months of the year.

CBR: *What's in the future for your company's operations in China?*

Simon: We intend to continue producing approximately 30 percent of our group's overall production needs in China—this amounts to approximately $60 million at FOB value annually. If MFN were to be removed, we would be forced to move 70-80 percent of that production out of China. If MFN were to become permanent, not an annual renewal battle, we would invest substantially in China, perhaps establishing four or five new factories over the next three years.

value to such processed goods, yet the US Customs Service credits the entire value of the good to China. Though the Chinese value-added figures may be on the low side, Hong Kong companies paying minimal processing fees do account for a significant share of Chinese exports.

The second investment wave

Most foreign investment in China's textile industry has been decidedly low risk and low tech. However, rapid expansion of export processing is forming the basis for a second wave of foreign investment in weaving, fabric processing, and the production of other inputs. Export processors who experience difficulty in obtaining adequate and consistent quality inputs in China are increasingly sourcing from foreign-invested factories, most of which have been transplanted from Hong Kong. This second wave of investment is pro-

ceeding rapidly; weavers and fabric processors have been the first to move, while spinners—most of whom moved to Hong Kong from Shanghai when their factories were nationalized in the 1950s—have been more reluctant to return, preferring to invest in Southeast Asia.

This deepening and broadening of foreign investment will enhance the textile industry's competitiveness, reduce its vulnerability to fluctuations in world market prices and supply, and contribute to sustainable growth. Technomic's trend analyses suggest that during the next decade a third wave of foreign investment will occur, one that will require higher levels of technology transfer and capital commitment. Rapidly expanding downstream demand for raw materials such as synthetic fibers, textile chemicals, and high-quality dyes will encourage larger scale, more capital-intensive investments, primarily in the chemical industry. In this area, Hong Kong companies will play a much smaller role; American, Japanese, and European investment will dominate because of the higher technology and capital requirements. Taiwan and South Korean investors are also likely to be active players, particularly in synthetic fibers and high-quality fabrics.

Shell's proposed $2.5 billion petrochemical joint venture in Huizhou, Guangdong Province, is the most ambitious example of this third wave of foreign investment. The proposed plant, approved by Beijing in early 1991 and now in the feasibility stage, will convert five million tonnes of crude oil into a wide range of chemicals for distribution in South China. The core of the project will be an ethylene cracker with a production capacity of 450,000 tonnes per year, which will produce a key feedstock used in the production of many chemicals, plastics, and synthetic fibers.

Other large western chemical companies such as E.I. du Pont de Nemours & Co., Atlantic Richfield Co., and Amoco Corp., for example, have enjoyed very lucrative markets in China for critical raw materials used in a wide range of industries, including textiles. However, development of the chemical industry is a high national priority under the Eighth Five-Year Plan and this import window is likely to close over the next decade as indigenous capacity comes on-line. Foreign suppliers hoping to maintain a long-term presence in the domestic market will have to consider local production arrangements through joint ventures or licensing agreements.

Rapidly expanding downstream demand for raw materials such as synthetic fibers, textile chemicals, and high-quality dyes will encourage larger scale, more capital-intensive investments.

Avoiding pitfalls

Although China's textile industry is still underdeveloped and will certainly expand, the pace and stability of future growth will depend on how well several structural barriers are addressed. In particular, the on-again, off-again implementation of economic reforms during the last decade has led to serious imbalances in the structure of the industry. Rapid, uncoordinated growth in the fragmented downstream sectors, particularly garment assembly, has outpaced expansion of the more capital-intensive raw materials sector, which remains under central control. Production capacity has been expanded without concern for meeting market demand and without first securing sources of raw materials.

Though Beijing began an aggressive petrochemical and feedstock expansion plan in the late 1970s and has increased ethylene production 22-fold since 1975, imports of chemical intermediates used in polyester and nylon fiber production grew from an estimated $100 million in 1980 to $330 million in 1990. Several large projects have been approved to help reduce the imbalance between demand and supply, including a $154 million plant in Nanjing to produce caprolactum, which is used in the production of nylon. Amoco Corp. is also considering a major investment in Jiangsu Province to produce raw materials for polyester production. Although some improvement can be expected in the next decade, shortages of a number of raw materials—ranging from raw cotton to synthetic fibers—are expected to cause production bottlenecks into the next century.

Lack of critical inputs is not the only deterrent to increased textile production. Ineffective control of garment processors and synthetic fiber spinners has led to blind imports of advanced production machinery that Chinese factories are often incapable of operating and maintaining. As a result, much imported spinning, weaving, and fiber capacity is critically underutilized even while substantial imports of synthetic fiber continue. Although Beijing has successfully curtailed machinery imports under the austerity program, this problem is likely to reappear again in the future.

Balanced industry development has also been hindered by uneven efforts at decentralization, which have led to increased rivalries among the many ministries involved in textile production. The problem of conflicting jurisdictions is acute—the Ministry of Chemical Industry and the China Petrochemical Corp. (SINOPEC), for example, both maintain control over production of various synthetic inputs for the textile industry. Over the past decade, the two organizations have fought for limited investment capital, even at the cost of efficiency and duplication, and little change appears imminent on this front.

In a similar vein, regional rivalries also pose a threat to the textile industry's future growth. The growing power of provincial governments and bureaus increasingly circumscribes the central government's ability to ensure efficient national allocation of resources. In 1988, for example, Hunan Province actually set up road blocks to prevent the export of raw silk to Guangdong. Though the situation may not be this extreme in the future, hoarding—particularly of cotton and silk—by provinces anxious to develop processing industries is likely to become more common.

Unless the central government can

rein in the competitive tendencies of provinces to build self-sufficient, integrated textile industries, rivalries between them will further exacerbate problems of fragmentation and overcapacity. Resources will be wasted and efficiency lost because production scales will not be economically sized, and provinces may try to establish barriers against products from other areas.

Even if resource allocation can be improved, infrastructure bottlenecks will remain a critical obstacle to more comprehensive textile industry development. Electricity and water shortages will continue throughout the country, while transportation bottlenecks will force the industry to concentrate in increasingly wealthy coastal areas, where labor costs tend to be higher than in the interior. This development will likely exacerbate interregional rivalries.

Facing the challenge from abroad

All these structural and systemic problems will continue to hamper China's efforts not only to expand production and export volumes, but to improve quality. Despite a decade of expansion and foreign investment, the quality of China's textile exports remains among the lowest in the world. For the most part, only goods produced by Hong Kong-affiliated export-processing ventures—which rely on imported raw materials—have seen notable improvement in quality. Exports using Chinese inputs tend to be low quality and unable to command high prices in the global market. A truly comprehensive and well-integrated textile industry will depend on China's ability to develop the domestic capability to produce high-quality inputs.

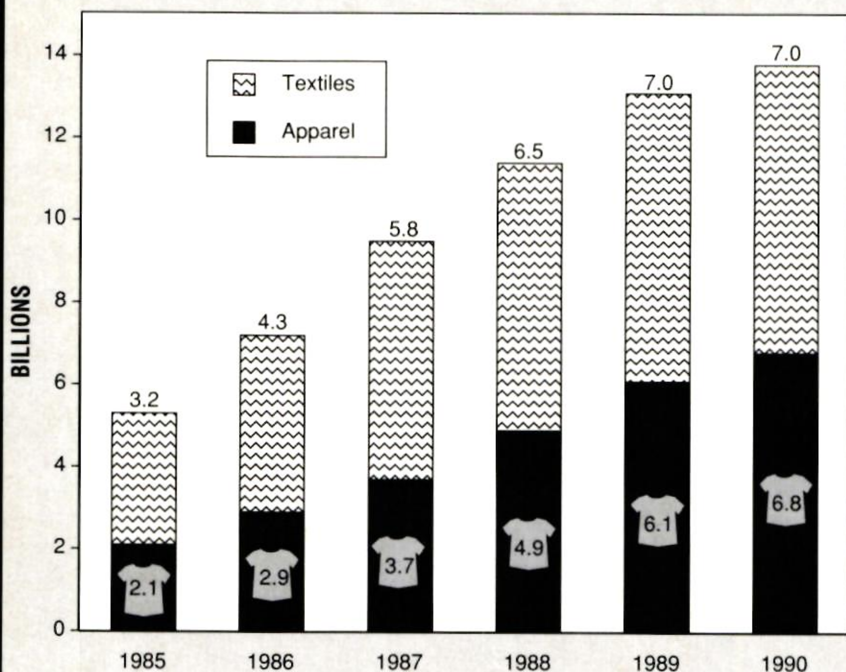
Increasing quality is an imperative if Chinese textile and garment producers are to compete with other emerging low-cost producers in Southeast Asia, South America, and perhaps even Eastern Europe. Indonesia, Thailand, and Pakistan, for example, offer increasingly attractive investment incentives with the added advantage of greater political stability. Labor costs may be somewhat higher than in China, but workers in these countries have reputations for being more efficient. Although textile wages in China are still only a fifth of those prevailing in Hong Kong and two-thirds of those in Thailand, they are rising quickly in key garment export regions such as Guangdong. For the next decade, however, China's textile producers should remain competitive.

The greatest external threat to the continued rapid expansion of China's textile industry is protectionism in its export markets. China is now the largest exporter of clothing to the United States, supplying 12.6 percent of US imports of garments and textiles in 1990. Although quota allocations set through Sino-US bilateral textile negotiations under the Multi-Fibre Arrangement have been generous during most of the 1980s, US quotas for Chinese textile exports have become increasingly restrictive since 1988 (*see* p. 40).

Aiming for number one

China's growing strength in global textile markets constitutes a significant threat to existing textile producers—including those in the United States. During the 1990s textile disputes with the United States will certainly be a key issue in what is likely to become an increasingly rocky trade relationship. Within Asia, China's competitive cost advantage will continue to accelerate changes in the structure of textile industries in Taiwan and South Korea. Hong Kong's textile industry has already responded by moving low-value, labor-intensive production into China and elsewhere in Asia, using factories at home to produce high-end fashion items which command higher prices on the world market. Though buyers will continue to diversify sourcing to protect themselves from quota and trade restrictions, China will likely remain a highly competitive and desirable source of textiles and garments.

Foreign suppliers may also find China a desirable market, as the textile industry's many technology gaps should provide significant opportunities. The new investments in spinning, weaving, and fabric processing, for example, are dependent on such high-quality inputs as specialty synthetic fibers and processing chemicals. While exporting products China's industry currently is unable to produce in sufficient quantity or quality may remain a viable strategy for foreign companies in the short and medium terms, in many sectors investment will be the only strategy foreign companies can depend on to protect long-term market positions. 完



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US-China Textile Relations

Textiles could be the casualty of increasingly tense Sino-American commercial relations

James L. Kenworthy

Since China "opened its door" anew in 1979, textiles/apparel have been its most significant export, and the United States has become its largest export market. But along with spectacular rates of growth have come disputes that threaten to derail this burgeoning trade. Tension over alleged Chinese evasion of US textile/apparel quotas and use of convict labor in textile production (*see* box), as well as lack of progress in multilateral negotiations for reforming regulation of the international textile/apparel trade, have put strains on the relationship. Although the recent announcement to extend the bilateral textile agreement for two years has helped to restore some stability, US-China textile relations will probably remain tense for some years to come.

China's growing strength

Although many of China's textile-related imports from the United States rose last year—for example, purchases of raw cotton were $277.2 million compared to $258.8 million in 1989, while purchases of filament tow hit $87.6 million, up almost $6 million from the year before—the bilateral economic balance in textiles/apparel continues to grow strongly in China's favor. US textile/apparel imports from China grew nearly 13 percent in 1990 over 1989 levels, from $3.1 billion to $3.5 billion. China is now the United States' largest foreign supplier of textiles/apparel, providing nearly 13 percent of all US clothing imports.

Although imports of textiles/apparel as a percentage of total US imports from China have declined, both the volume and dollar value of such imports have increased (*see* chart). China profits not only from the high number of jobs the labor-intensive textile sector provides, but also from the considerable hard currency its exports generate. In the historical pattern of third-world economic development, textile manufacturing is a preliminary stage of economic and industrial development; early exports of Asia's "four tigers"—Hong Kong, Singapore, South Korea, and Taiwan—were largely textiles. China's economic development is thus increasingly dependent on open foreign markets to which it can export its goods.

The bilateral textile agreement was due to expire on December 31, but US and Chinese authorities agreed in late April to extend it for two years.

Controlling textile trade

In order to prevent excessive market disruption and injury to competing domestic producers, however, developed nations (which are the major importers of textiles/apparel) have insisted on establishing an international regulatory regime to manage international trade in textiles/apparel; the Multi-Fibre Agreement (MFA). Negotiated under the auspices of the General Agreement on Tariffs and Trade (GATT) in 1974, the MFA provides an international framework under which its 52 signatories manage the orderly development of trade in textiles and textile products—current global trade of which approaches $200 billion a year. The MFA framework is implemented through a network of bilateral agreements between signatory nations. The bilaterals establish specific annual quotas for covered products, which are allocated among 147 MFA categories and administered by individual nations (for the most part) according to the Harmonized System of Tariffs.

The MFA seeks to prevent domestic market disruption from import surges by controlling imports through quotas. It operates as an exception to the trade liberalization provisions of the GATT, which basically holds that domestic markets should be shielded from disruption only by tariffs—and that such tariffs should be applied without discrimination, at least among GATT member nations.

While the MFA sets an overall minimum growth level of 6 percent a year for quotas, individual signatories may specify lower levels in their bilaterals. The MFA does not prohibit imposition of standard national tariffs or import duties on imports of textiles/apparel. Thus, even when permitted entry under MFA quotas, textiles/apparel are still subject to such tariffs until the volume in any controlled category reaches its annual quota ceiling. At

James L. Kenworthy is the author of A Guide to the Laws, Regulations & Policies of the People's Republic of China on Foreign Trade and Investment *and former counsel to the Department of Commerce's Office of Textiles.*

that point, subject to certain flexibility provisions, further entries are blocked for the rest of the quota year.

The MFA flexibility provisions allow certain categories to exceed quota limits by up to 7 percent a year, as long as the excess is charged to other quota categories (a process known as "swing" or "shift") and the aggregate annual limit on all controlled categories is not exceeded. MFA provisions also permit "carry over" of quotas unused in one year to a subsequent year, as well as the borrowing of quotas from a succeeding year for use in the current year ("carry forward").

Most MFA bilateral agreements, in addition to imposing quotas on specific categories, also provide that the importing country may request consultations with its trading partner to prevent surges of imports in uncontrolled categories from disrupting domestic markets. If no agreement is reached, the importing nation may unilaterally set quotas in these "called" categories. However, these limits may not be imposed at levels less than those of actual imports over the preceeding 12-month period, and must permit annual growth rates of 6 percent.

Though designed to foster stability in the international textile/apparel trade, MFA textile quotas generate economic costs to consumers and retail firms in importing countries. The US International Trade Commission (ITC) has estimated the costs of MFA quotas by figuring them in terms of tariff equivalents. According to the ITC, in 1987 the quotas on man-made fiber textiles/apparel effectively added 29.8 percent to the lowest—or Most Favored Nation (MFN)—tariff rate of 20.7 percent, for an effective overall duty of 50.5 percent. If China lost its MFN status, the standard US duties would increase. In the case of men's pants, for example, the duty would rise from the current rate of 17.7 percent to the non-MFN rate of 90 percent—which still would be subject to the MFA tariff equivalents. The exhorbitant costs of non-MFN tariffs on top of MFA quotas would almost certainly cripple US-China bilateral trade in textiles/apparel.

US–PRC Textile/Apparel Trade

	1985	1986	1987	1988	1989	1990
US imports by volume (billions of sq m)	.88	1.4	1.5	1.3	1.7	1.7
US imports by value ($ billions)	1.3	2.1	2.4	2.2	3.1	3.5
Textile imports as % of total US imports from China	31.0	40.4	38.1	25.9	25.8	23.2
Textile imports from China as % of total US textile imports	7.4	10.4	10.1	9.5	12.0	12.6

SOURCES: *Department of Commerce, International Trade Commission*

Extending MFA

The original MFA lasted from 1974 until 1977. Since then it has been renegotiated three times: MFA II (1977-81); MFA III (1982-86); and MFA IV (1986-91, (*see The CBR*, September-October 1986, p. 26). Since resumption of Sino-American diplomatic relations in 1979, Washington and Beijing have signed three bilateral textile agreements under the rubric of the MFA. The current agreement, which became effective January 1988, sets quotas on all imports of Chinese textiles/apparel except for a few handicraft items, and limits China's exports to an average annual growth rate of 3 percent. The agreement includes flexibility for swings, carry over, and carry forward, and provides for data sharing and customs cooperation. It provides for consultation over any goods threatening to impede the orderly development of trade due to market disruption, though such requests must be accompanied by detailed evidence thereof. The bilateral was due to expire on December 31, but US and Chinese authorities agreed in late April to extend it for two years.

Shortly after MFA IV was signed in 1986, 105 countries, including China, began the Uruguay round of multinational trade negotiations under auspices of the GATT. Various working groups were established to conduct negotiations in different sectoral areas, including textiles. The textile working party endorsed, in principle, the gradual re-incorporation of the MFA regime into the GATT upon conclusion of the Uruguay round, which was scheduled to end in December 1990. The Uruguay round, however, dissolved into an inconclusive stalemate over such highly charged issues as agriculture and intellectual property protection. As a result, the world's major textile-producing and importing nations were faced with two options: letting MFA IV expire on July 31—and risking the chaos that might result

China as Friend...

As China's importance as a supplier to US and global textile/apparel markets has grown, so has the controversy surrounding its trade practices. To obtain a better idea of where various sectors of US industry stand on these issues, Editor Pamela Baldinger spoke with representatives of two large textile-related trade associations. Speaking for the retailers and importers was Julia K. Hughes, divisional vice president of government relations for Associated Merchandising Corp., the world's largest retail marketing organization. Hughes is also a member of the steering committee of the Retail Industry Trade Action Coalition (RITAC).

CBR: *What is RITAC's opinion of the recently extended US bilaterals with China and Hong Kong?*

Hughes: RITAC supports the bilateral process because it improves reliability of trade and the ability to predict the future. Our response to the Hong Kong accord, however, is somewhat negative, since in reducing Hong Kong's quota to help offset increases in Turkey's—a reward for its support in the Gulf War—the government has linked foreign policy with trade policy in textile areas. Moreover, this action de facto creates a global quota—something we have fought against in the past. If the government wants to increase Turkey's quota, there's no reason to take away quota from anyone else.

CBR: *As importers, how do you deal with recent charges that China is shipping mislabeled textiles to the United States?*

Hughes: RITAC takes a strong position on this issue—we oppose illegal transshipments. We support the government's decision to take action against illegal shipments, since they injure those of us who import legally. We have requested the US Customs Service and the Committee for Implementation of Textile Agreements (CITA) to provide us with basic guidelines on what we as importers should be looking for, to ensure that we are not dealing with the perpetrators of illegal shipments. Should we look for unusual labels? Unusual shipping sequences? Unfortunately, we have not had any response so far, as the Justice Department is concerned that releasing such information will damage the fraud cases it has pending.

CBR: *Do you believe that the textile talks at the GATT Uruguay Round will get moving again? What is your position on phasing out global textile quotas and reincorporating textiles under the GATT?*

Hughes: I think there will be a breakthrough in the agriculture talks by the end of the year, which would enable the textile talks to go ahead. RITAC supports the phasing out of quotas, though we'd like to see it accomplished faster than the proposed 10-year timeframe. In addition, certain goods not produced in large quantities in the United States should be removed immediately from quota and returned to GATT rules. Ultimately, we believe that phasing out textile quotas will benefit manufacturers as well as consumers. While some segments of the US textile industry may be affected negatively in the short term, they will be reinvigorated as markets overseas open up. In the long term everybody will profit.

...and Foe

On the other side of the spectrum is Charles Bremer, director of international trade at the American Textile Manufacturers Institute (ATMI). ATMI's 160 members turn out about 75 percent of total US textile output.

CBR: *How does ATMI feel about the renewal of the China and Hong Kong textile bilaterals?*

Bremer: The bilateral with Hong Kong was generous. Reducing their quota by 9 million sq m per year—out of a total allowance of about 1 billion—is like giving a dime to a homeless person; it doesn't amount to much. Besides, in return Hong Kong was allowed more shift than under the previous agreement.

We were against the Bush Administration's decision to renew the China bilateral. China is one of this country's worst trade outlaws. The Chinese consistently violate the terms of both the Multi-Fibre Agreement (MFA) and our bilateral. They have already been caught illegally transshipping millions of dollars worth of textiles, and what's documented is certainly only a portion of what's actually gotten in. The US Customs Service must have irrefutable evidence before they call for consultations, and that evidence is not easy to obtain.

CBR: *What can the United States do to stop illegal transshipments from China?*

Bremer: Currently, when the United States determines that goods have entered illegally, all we do is deduct the items from the current or next year's quota. The end result is that they still get to ship as much as if they hadn't transgressed the bilateral. We think that quotas should be reduced by twice the amount of the illegal shipment in order to actually penalize the offenders.

CBR: *What is your attitude to extension of the MFA and continuing talks under the Uruguay Round of the* GATT?

Bremer: While we feel that the MFA is not properly administered—the government usually acts too late, when trade is already at damaging levels—we prefer it to the direction the Uruguay Round appears to be taking, which could be disastrous for US textile producers.

without an international regulatory framework—or extending the agreement in the hope that talks under the Uruguay round would revive. In late July the MFA signatories agreed to extend MFA IV for 17 months (until December 31, 1992), to enable the Uruguay talks to get back off the ground.

There is some indication that the United States and the European Community may formally restart the agriculture talks—conclusion of which the United States has set as a precondition to finalizing agreements in other areas—by the end of the year. If and when the textile talks resume, the major issues likely will be the length and nature of the transition, given the basic acceptance of phasing out the MFA and reasserting GATT regulatory principles. Importing nations in particular have asserted concerns regarding protection against market disruption, growth rates, and enforcement procedures.

Textiles and the GATT

The United States—despite strong objections from the US textile industry, which claims that ending the MFA would devastate the domestic industry and lead to the loss of three million jobs over 10 years (*see* interview)—has advanced a plan that would phase out MFA bilateral quo-

The Transshipment Question

Ever since the United States and China resumed economic relations, US officials and the domestic industry have expressed concerns over Chinese efforts to evade US textile/apparel quotas established under the Multi-Fibre Agreement (MFA). The issue arises in part because of trade accounting differences between the two nations.

The United States, in calculating its trade figures, includes all goods manufactured in China as Chinese exports, regardless of whether shipped to the United States directly or indirectly through Hong Kong, Macao, or another entrepot. The Chinese, however, insist that US-bound goods shipped first to a third country or territory—like Hong Kong—where value may be added through finishing, packaging, marketing, or shipping—are Chinese exports to that country. If these goods are eventually re-exported to the United States, they constitute exports from the third country, not from China. In the case of textiles/apparel, Chinese officials argue that goods originating in China but re-exported through Hong Kong to the United States should be considered Hong Kong exports and charged to Hong Kong's MFA quotas.

Differences in methods of calculating trade data account for only part of the problem, however. US officials assert that Chinese shippers regularly attempt to evade US textile/apparel quotas either by fraudulently mislabeling their goods as to point of origin before shipping them, or by transshipping them through third countries where they are re-labeled as originating therein and then shipped on to the United States. Upon entry in the United States, the transshipped goods are charged to the third country's textile quotas. Guangdong Province in southern China has been identified as the center of such transshipments, because of its close proximity to Hong Kong and Macao.

The Chinese are accused of targeting smaller countries for illegal transshipment, usually nations that either do not have MFA quotas or whose annual quotas regularly go unfilled. Such countries include Lebanon, Lesotho, Macao, Mozambique, Panama, the Philippines, Portugal, Tanzania, Taiwan, and Zimbabwe, as well as the Persian Gulf states of Kuwait, Oman, and Qatar.

To help identify illegal textile/apparel shipments, the US Customs Service in July 1990 initiated "jump teams" of US government commodity and trade experts. These teams are dispatched without notice to suspected transshipment locations to determine if textile/apparel producers there really exist and have the plant capacity to warrant the volume of shipments attributed to the country. One such team sent to Honduras early this year found that 24 million shop towels that had entered the United States labeled as Honduran products represented more than twice that country's relevant manufacturing capacity. According to US officials, more than $85 million worth of Chinese textiles shipped to the United States in 1990 were fraudulently mislabeled as to country-of-origin. The goods most commonly involved were jeans, shirts, and jackets.

The United States has held consultations with China on the transshipment issue nearly half a dozen times within the past 10 months. In December 1990 and February 1991, the Committee for the Implementation of Textile Agreements (CITA), the interagency government body that supervises US implementation of the MFA and US bilaterals, officially determined that China had illegally shipped textiles/apparel to the United States and directed the Commissioner of Customs to charge the amounts involved against China's 1990 quotas in some 19 categories. Goods for which 1990 quotas were filled were charged against 1991 quotas.

Chinese authorities branded the action "high-handed" and hinted at negative consequences for US companies in China. Nevertheless, in early March a Ministry of Foreign Economic Relations and Trade (MOFERT) spokesman, while not explicitly admitting any wrongdoing, announced that Chinese officials had issued a series of instructions to the textile sector. One of the primary directives was a ban on shipping textile products—including those made with a foreign partner—to the United States via third points.

But there is already doubt over how effectively this directive can—or will be—implemented. In late June, the United States called for yet another consultation over an additional 210,000 dozen pieces of allegedly mislabeled goods that originated in China. In the meantime, the US government, in order to help deter illegal transshipments, has reportedly been considering seeking criminal indictments against American importers accused of conspiring with Chinese manufaturers to ship falsely labeled clothing to the United States. —James L. Kenworthy

tas over a 10-year period. This period would be divided into three tranches, each of which would see quotas liberalized according to a fixed formula. The proposal conditions the elimination of the MFA on exporting nations' implementing enforceable measures to prevent dumping, intellectual property infringement, and use of export subsidies. It also requires them to open their markets to US products.

The developing nations, supported by China, would prefer quotas to be phased out more quickly. The European Community, however, has proposed an even slower timetable than the United States. It thus appears probable that a 10-year plan will eventually emerge as a compromise.

A 10-year phase out of MFA quotas will probably emerge as a compromise when GATT textile talks resume.

Rocky road ahead

With no imminent breakthroughs expected from the Uruguay round, US-China textile/apparel trade, cushioned by extension of the MFA and the bilateral, should be fairly stable in the short term. Nevertheless, difficult times still lie ahead for the US-China textile trade, and many investors/exporters are worried (*see* box). The White House has stated that the United States will closely monitor Chinese textile shipments for fraudulent labelling and illegal entry, and will charge such goods to China's current and future quotas. In addition, should the US Trade Representative's Special 301 investigation—or potential 301 investigation (*see* p. 50)—result in the imposition of US sanctions against Chinese exports, textile/apparel goods could be a likely target. Thus, US firms sourcing textiles/garments from China will have to monitor the situation closely. 完

Defending Hong Kong's Textile/Apparel Industry

Tension between the United States and China over textile/apparel trade inevitably affects Hong Kong, one of the world's leading apparel exporters and the largest foreign investor in China's textile industry. The garment industry is Hong Kong's top export earner, with domestic exports bringing in over $9 billion in 1990. As US companies are the largest foreign investors in the sector, they stand to lose should US displeasure with both China's and Hong Kong's trading practices materialize into concrete sanctions.

To help protect the Hong Kong textile/apparel industry's interests, the Hong Kong Exporters' Association early this year solicited contributions from textile, shipping, and other service companies to form the Fair Trade Fund. As originally envisioned by founder Thomas Goetz, the fund would be used to defend Hong Kong's exports against various external threats. Chief among these were potential US withdrawal of China's Most Favored Nation (MFN) status, expiration of the Multi-Fibre Agreement (MFA) and the Hong Kong-US bilateral without an alternate international agreement, anti-dumping charges against Hong Kong exports, and accusations that Hong Kong companies collaborate with the Chinese to avoid US textile quotas.

Two of these issues now no longer require direct action. The MFA has been extended through 1992, and Hong Kong and the United States in July agreed to extend the textile bilateral for four years. Hong Kong accepted a slight decrease in its overall quota to help offset a quota increase for Turkey, which was rewarded for its cooperation during the Gulf War. The MFN issue, meanwhile, now appears to be on the back burner of US lawmakers (*see* p. 50).

As far as quota evasion is concerned, US Customs Service and government officials have reportedly stated that they are satisfied with the Hong Kong government's efforts to prevent illegal transshipments from China through the territory. Under Hong Kong law, local manufacturers must apply for licenses both to import goods from China and export them abroad. This documentation can be checked by Hong Kong customs agents if illegal transshipments are suspected. The maximum penalty for giving a false country of origin when applying for an export license is two years in jail and a $500,000 fine.

Dumping charges are now probably the chief concern of Hong Kong textile/apparel exporters. In a 1990 case, US officials determined that Hong Kong manufacturers were dumping man-made fiber sweaters in the United States, and assessed a 5.86 percent dumping duty on such imports. Goetz claims the duty resulted in the loss of well over $400 million to Hong Kong industry, including manufacturers, shippers, and finance houses. In late July 1991, the Hong Kong government referred the case to the General Agreement on Tariffs and Trade (GATT) anti-dumping committee, which must make a determination within three months if the two sides have not settled the issue themselves in the meantime.

The Fair Trade Fund, which collected just shy of HK$500,000, is now being transformed from a private-sector to a public-sector initiative. Two schemes are being considered by the government and leading players in the industry. The first involves increasing the fee Hong Kong companies must pay the government to buy, rent, or sell textile quotas. The additional money would go into a special fund administered by the government to deal with textile-related issues; i.e., dumping cases, which are expensive to defend against. The second scheme would involve increasing the export levy, which already funds official Hong Kong lobbying efforts. Now that negotiations over extension of the bilateral and MFA are over, the government and private sector should soon reach a decision on which scheme to adopt. —PB

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Project Notebook

Sewing Up the China Market

Novel marketing and promotion techniques are making McCall's patterns synonymous with home sewing

Paul Condrell

There are more sewing machines in China than there are people in the United States—a tantalizing fact if you are the world's largest pattern designer. Perhaps even more striking, patterns are a relatively unknown—but increasingly welcome—commodity, thanks to the New York-based McCall Pattern Co. Starting from near scratch in 1988, McCall has steadily increased sales and now offers over 300 current styles from which China's newly fashion-conscious population can choose. Though the company's China operations are not yet profitable, its management takes a long-term view of the market. President Robert L. Hermann sums up the McCall attitude with a Chinese proverb: "He who uses a long line catches a big fish." Currently, McCall expects to break even in 1994.

Low profit margins . . .

In China, McCall perceives one of the final frontiers of growth for its products, given rapidly rising incomes and demand for modern, stylish clothing. But before devoting itself to developing the China market, the company conducted a market test in July 1987 to gauge its patterns' sales potential. Twelve designs were placed in two department stores—one each in Beijing and Shanghai—and sales activity was monitored for two months. Sales topped 300 units per month in both stores, prompting McCall to launch its first full-scale sales effort in April 1988.

McCall is targeting urban women between the ages of 20-40, and its strategy calls for gradually building distribution and sales while vigorously promoting use of patterns. Currently, all patterns are printed in the United States. McCall has registered its trademark in English and Chinese in both the clothing and printed matter categories. Its designs are not copyrighted, but the speed with which new designs are introduced and the large economies of scale of printing presses act as disincentives to potential pirates.

Thus far McCall has invested over $1 million in training and supervision, sales, inventory, supplies, and promotion.

Patterns are shipped from the United States via a Chinese import agent to McCall's appointed distributor, the Beijing Garment Research Institute. The Institute sells directly to department stores and fabric retailers, on a consignment basis only. Each store pays the Institute once a month for the patterns it has sold; the Institute deducts its margin and pays the importer, which in turn pays McCall in foreign exchange.

Paul Condrell is president of the New York-based U.S. China Investment Corp., a company specializing in the marketing of consumer goods in China. Condrell and his wife, Stacy Henderson Condrell, have managed McCall's business in China since its inception in 1987.

The Chinese distributor is responsible for warehousing, locating and selling to new stores, shipping and filling stores' orders, ordering patterns from the United States, fulfilling mail orders, and completing sales reports. To ensure that these tasks are performed well, McCall has hired two Americans to train Institute staff and supervise every aspect of the operation from the start.

McCall patterns retail for ¥9.90, or about $2—only one-third the average US retail price. The low price is one of many factors contributing to McCall's negative cash flow. Thus far the company has invested over $1 million in training and supervision, sales, inventory, supplies, and promotion.

. . . but high potential sales volume

The fundamentals of the pattern market in China are resoundingly positive. An enormous selection of inexpensive fabrics is available in most cities, and nearly every Chinese home has a sewing machine—yet no domestic company specializes in pattern production. Although in the past, Chinese-made patterns have appeared in stores in Guangzhou and Shanghai, they were of crude design and short-lived. The manufacturers could print patterns, but were unable to make them in styles customers wanted.

McCall's only competition are the ubiquitous tailors who camp out in the free markets. Government-

owned tailoring stores cannot effectively compete for the Chinese fashion customer because they are slow (orders can take up to three months to finish) and tend to work in only a few styles, which are often outdated. Though some private tailors do an acceptable job at a reasonable price, they generally have a dubious reputation for quality. Patterns, in contrast, afford users control over time, quality, and fit, not to mention lower costs and the satisfaction of accomplishment.

Given such conditions, it would be natural to expect sales to skyrocket. But lack of competition does have its downside—consumers and vendors are unfamiliar with the product. Over the last three years, therefore, McCall's has had to work one on one with everyone from the distributor to the customer to educate them about the benefits of patterns.

The Beijing Garment Institute's staff had no sales or distribution experience, and needed instruction not just in the practical aspects of running the business, but also in instilling a professional work ethic and dealing with customers. At first, Institute directors were skeptical that patterns were a viable project, but recent sales volume has erased any doubts.

Convincing managers of Chinese fabric and department stores to carry the patterns was the next task. Unlike most of their counterparts around the world, Chinese fabric store managers tend to resist the notion of marketing patterns, claiming they should be carried by stores selling books or paper products instead. To convince them of the hows and whys of selling with fabric, McCall's expatriate staff personally pay the first sales call to each store, meeting first with the fabric department manager and then proceeding to the store's general manager. (The contract itself is made between the store and the distributor). To clinch the deal, the stores are offered start-up stock, free use of display case and cabinet, and free posters and advertising support. Even then, many managers complain that patterns don't bring in enough money given the counterspace they require. Eventually, however, they learn that along with each $2 pattern, they will likely sell $10-15 worth of fabric.

Once the retailer has agreed to carry its patterns, McCall next works with the sales staff. Each clerk receives individualized training, and a McCall representative actually stands behind the counter with him or her on the first day to get the clerk comfortable with the product. Managers are strict about what kinds of incentives they will allow McCall to offer their staff, for fear of arousing the jealousy of other sales clerks in the department. But with persistence they often allow some perks, such as free or below-cost patterns, free posters, or McCall's glossy counter catalogues.

The best clerks tend to be women who have made a number of garments from McCall patterns and enjoy selling them. Chinese consumers are often skeptical of new things, since there are many fake and shoddy products on the domestic market. Experienced clerks, however, can address concerns about sizing, product quality and ease of use, and reinforce customers' confidence in their sewing ability. To help back them up, McCall has implemented a nationwide public relations campaign.

Prospective customers examine a McCall's catalogue.

Photo courtesy of Paul Condrell

Reaching the masses

The purpose of the campaign is to increase knowledge not only of McCall's products, but of home sewing in general. The campaign is run by the local representatives, based on an annual budget set by US-based management.

To begin with, moonlighting Chinese journalists have placed hundreds of articles in local—and sometimes national—newspapers, covering the product from every angle. Some stories appear on the business page, discussing how well patterns fit domestic market needs, while others appear on the style/life pages, forecasting trends or recommending home sewing as an inexpensive way to dress well. Occasionally articles appear on the front page, announcing the patterns' arrival in a city or describing the mob scene at the local department store when a foreigner sold from behind the counter for a day.

In addition to the newspaper articles, several dozen video segments have been produced in cooperation with local TV stations. The 3-8 minute segments have in turn been syndicated to other local stations around the country. (National stations have generally been avoided, as they offer a more narrow range of programming under less favorable conditions.) The segments are broadcast on each local station's version of a prime-time show for women.

On these shows, TV personalities discuss design choices while paging through the McCall catalogue. They then lay out a McCall's pattern, cut the fabric, sew the garment, and model it. Sometimes the host will mention where the patterns are on sale locally. These soft-sell ads, or "info-mercials," have been very successful to date. The day after such a broadcast in Tianjin, customers thronged to the local department store and bought 239 patterns—probably a one-day record for the company anywhere in the world. Sales in Kunming Department Store averaged over 1,500 patterns per month during a three-month series of broadcasts, making it the top-selling store in China. Mail orders

from elsewhere in Yunnan Province have also jumped since the programs began.

In order to reinforce the newspaper articles and television spots, McCall is also trying to set up public relations events with domestic and foreign manufacturers of sewing machines. Given the intense competition in the sewing machine arena, however, most manufacturers want to publicize the uniqueness of their machines rather than the craft of sewing in general. Joint promotional efforts, therefore, have yet to get off the ground.

Selling by mail

Although McCall's patterns are currently available in 48 stores in 38 cities, much of the potential market lies outside serviced areas. In order to cater to these individuals, McCall instituted mail-order service in 1989. Today, mail orders account for 20 percent of the company's business.

Mail order is not a widely accepted way of doing business in China, so McCall is working hard to establish a reputation for speed, accuracy, and fairness. Staff are trained to care for each order as if it came from a friend or relative. They offer free technical assistance by mail and handle customer inquiries, though less than one percent of customers report any problems.

To publicize the mail-order business, ads displaying best-selling designs are placed in top Chinese fashion magazines, and a 60-page color catalogue, featuring over 100 designs and a discount coupon, has been distributed via book stores and by mail.

To order a pattern from the catalogue (or from a magazine ad), Chinese obtain postal money orders, which cost only four cents and one percent of the amount spent. The customer writes the pattern's design number and desired size right onto the money order, and the postal service delivers the money orders directly to the Beijing Garment Research Institute. Patterns sold through mail order cost the same as those sold in stores; the extra profit the distributor makes by cutting out the retailer more than covers the postage and handling charges. Currently, the Institute receives about 100 orders a day, which are processed and shipped out via registered mail within 24 hours. McCall hopes its mail order business will help it gain access to the large population of Chinese who live outside the 80 largest cities, where it plans to market its patterns directly.

McCall has produced several video segments in which TV personalities lay out a McCall's pattern, make the garment, and model it. After a broadcast in Tianjin, customers set a one-day sales record for the company.

A pattern for success

McCall's perseverance and promotional efforts in China are paying off. Sales per store are averaging well ahead of US rates, with the best Chinese stores world leaders on a units-sold-per-year basis. The total number of patterns sold in 1990 hit 100,000—up from just 30,000 in 1989—and is expected to hit 150,000 this year. Nevertheless, it will take staying power, continued promotion, and improvements in product and marketing strategy to continue this rate of growth.

Currently, McCall patterns in China carry generic sewing guides that explain how to use the patterns with pictures and symbols, rather than words. There are no Chinese instructions specific to each pattern. But after hosting a promotional fashion show attended by some 1,000 guests—many wearing clothing they'd made from McCall patterns—last spring, Hermann instructed McCall's China team to translate specific sewing guides into Chinese and begin printing Chinese characters on the patterns themselves. These measures should help Chinese sewers get the most out of their patterns and boost the confidence of first-time buyers. The guides will be printed in China, while the presses in the United States are being retooled to add Chinese to each pattern. The new line of translated patterns will be on the market in March 1992.

Another innovation in the works is to begin merchandising patterns in China independently of those available in the United States. Currently, McCall ships only women's designs in certain categories, and carries those designs only as long as they remain current in the United States. Beginning next year, McCall will use sales information from China to select which of its 800 designs are most in demand there; pattern sales have shown that there is a remarkable correlation between trends in the United States and China, but there remain significant differences which make it folly to carry exactly the same line as in the United States. A line specially picked for China will allow more efficient use of warehouse and store counter space, less obsolescence, appeal to a broader number of pattern uses (such as children's and craft designs), and the ability to retain best sellers even after they go out-of-date in the United States. The same number of designs will be available, but they will be those most responsive to demand. Once these product improvements are in place, McCall will expand distribution into stores in 40 more cities and undertake more national promotions.

There is no doubt that sales to date have barely scratched the surface. The Chinese government, at times hostile to other consumer-product imports, has generally been supportive of McCall's efforts, recognizing the pattern as a technology that can be used to absorb fashion trends and cutting techniques. Moreover, use of patterns promotes use of Chinese fabric, thread, and sewing notions. With both government and public support, McCall believes that China will eventually become a major marketplace for its patterns.

A partner in China's future

"United Technologies Corporation
is a high-technology partner in China's
economic development.
As a leader in international markets,
we have made a commitment to a
long-range business strategy for China.
We are using technology transfer
in support of economic reform, and
have broad-spectrum involvement
in China through our operating units."

Jonathan M. Schofield
President
United Technologies International Corporation

Pratt & Whitney aircraft engines **Carrier** heating and air conditioning

Otis elevators and escalators **Hamilton Standard** aerospace systems **Sikorsky** helicopters

Letter from the President

To ensure Senate support of unconditional MFN renewal for China, President Bush committed the Administration to take strong action on other trade-related China issues. US business must thus deal with the possibility of new impediments to trade even while the MFN debate lingers.

MFN Fight Not Over Yet

The first round in the battle over Most Favored Nation (MFN) trading status for China is over, and prospects for eventual success look good. But we're not home free yet. Both the House and Senate voted to attach a long string of conditions on renewal of MFN next year, but the 55-44 vote in the Senate is far short of the two-thirds majority neccessary to override a promised presidential veto. The anti-MFN forces actually turned out to be fewer in number than most analysts predicted.

A key factor in the Senate vote was the exchange of letters between Senator Max Baucus (D-MT) and the President. The Baucus letter, which was co-signed by 15 senators, conceded that denial of MFN was the wrong way to influence China's behavior, and in lieu of withdrawing it requested a tough US action plan on human rights, arms and nuclear proliferation, trade practices, and other issues. In response, the President promised vigorous action in these areas as well as support for Taiwan's accession to the GATT, another item on the Baucus agenda.

These commitments indicate that there will be more difficult times ahead for US-China relations. For example, on the trade imbalance, the letter states that if consultations "fail to produce Chinese commitments to take substantial measures to improve market access, the Administration will self initiate further action under Section 301 of our trade laws." Further tough measures are promised in the areas of intellectual property rights, illegal textile shipments, and exports of products made by prison labor. High-tech sales to China, particularly high-speed computers and satellite equipment, will be not be authorized until the United States is satisfied that China adheres to "accepted international nonproliferation standards."

The House and Senate bills may now be taken up in conference committee, from which a reconciled bill will be sent to the President. Such a bill will almost certainly be vetoed. At that point the scenario becomes less clear. Currently, Senator Mitchell clearly lacks the support to override a veto. Therefore, he may elect to just sit on the bill and wait for China to make a serious blunder; i.e. sell missiles to Syria—the possibility of which unfortunately cannot be ruled out. By not taking action on the bill, Congress can also put pressure on the Administration to ensure it takes a tough line and abides by the promises the President made in response to the Baucus letter. Congress can hold off on voting to override a presidential veto until the end of this session of Congress in November 1992.

Should Mitchell pursue such a wait-and-see strategy, the American business community will continue to face the prospect of losing MFN and seeing the entire US-China commercial and economic relationship suddenly thrown into turmoil. Yet while the US-China trade relationship hangs in limbo, the rest of the world is moving toward normalization of relations with China. The European Community and Japan have resumed concessionary lending, World Bank and Asian Development Bank loans have been approved for other than basic human needs, and such heads of state as Japan's Prime Minister Kaifu and Britain's Prime Minister Major have recently visited or plan to visit Beijing. Once again, the US business community risks losing its competitive position in a major export market while the government wrestles with what has become a largely partisan political fight.

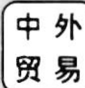
If the United States is going to remain competitive in China, it is imperative that the uncertainty brought on by the annual fight over MFN be eliminated. Legitimate concerns over human rights, trade, and proliferation issues are better dealt with on a targeted, case-by-case basis by using existing mechanisms. Therefore, even after this year's MFN battle is over, the Council will continue to pursue and explore measures that will help restore and stabilize the US commercial relationship with China.

中外貿易 China Business

Peter Kuo

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

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



SALES AND INVESTMENT THROUGH
July 15, 1991

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

Agricultural Technology

Investment in China

International Development Board of Canada/China
Established joint project for research and transfer of dry farming techniques in Hebei Province. $1.13 million (C$1.3 million). 5/91.

Other

Asian Development Bank
Approved technical grant for study of tropical crop development in Guangdong Province. $402,000. 5/91.

International Fund for Agricultural Development
Provided soft loan to finance development of farm production, forestation, and animal husbandry in five counties of Shanxi Province. $23.5 million (17.85 million Special Drawing Rights). 5/91.

United Nations' World Food Program
Will provide five-year agricultural assistance project to Yunnan Province. $25 million. 6/91.

World Bank
Will provide loan for agricultural projects in Anhui, Jiangsu, and Shandong provinces. $335 million. 5/91.

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

Banking and Finance

China's Investments Abroad

Luxembourg/Bank of China
Established Bank of China Luxembourg S.A. subsidiary. 6/91.

Singapore/Hainan Province
Will establish Hainan Province Investment Service Co. in Singapore. 6/91.

Other

The Bank of East Asia (HK)
Opened branch office in Xiamen, Fujian Province. 6/91

Huachiao Commercial Bank Ltd. (HK)
Will open branch office in Shantou Special Economic Zone. 6/91.

James Capel International Ltd. (UK), a subsidiary of the Hongkong and Shanghai Banking Corp. (HK), and Standard Chartered Finance Ltd. (HK), a subsidiary of Standard Chartered PLC (UK)/China Venturetech Investment Corp
Established China Assets Holding Ltd. (CAHL) investment fund in Hong Kong to support industrial development in China. $39 million. 6/91.

Chemicals and Petrochemicals

China's Imports

Toyo Engineering Corp. (Japan), a subsidiary of Ishikawajima-Harima Heavy Industries Co. Ltd. (Japan) and United Technical Corp. (Spain)/China National Technical Import-Export Corp.
Will sell technology and equipment for construction of a 140,000 tpy ethylene complex in Tianjin. $150 million. 6/91.

Canadian Chemtics International Co. (Can), a subsidiary of Trafalgar House PLC (UK)
Will supply engineering and processing equipment for a fertilizer plant in Anhui Province and a chemical plant in Hubei Province. $16.2 million. 5/91.

Snamprogetti Ltd.(UK), a subsidiary of Ente Nazionale Idrocarburi (Ita)/China National Technical Import-Export Corp.
Will provide principal equipment for a 140,000 tpy ethylene project in Xinjiang. 5/91.

Investments in China

The Chia Tai Group (Thailand)
Will establish Guo Cheng Petrochemical Co. $16.07 million. 6/91.

C. Itoh & Co. Ltd. (Japan) and Toyo Engineering Corp. (Japan)
Will build a 520,000 tpy urea plant in Xian, Shanxi Province. $5.8 billion (J¥ 800 billion). 6/91.

C. Itoh & Co. Ltd.(Japan), Mitsubishi Corp. (Japan), Mitsui & Co. Ltd. (Japan), Marubeni Corp. (Japan), and Sumitomo Corp. (Japan)/NA
Will build a 1.2 million tpy naphtha cracker and 450,000 million-tpy ethylene complex to produce downstream petrochemical products in Liaoyang, Liaoning Province. $3 billion (Japan:50%-PRC:50%). 6/91.

Technimont (Ita), a subsidiary of Gruppo Ferruzzi-Montedison (Ita), and Intecsa-Udhe Industrial (Spain)
Will build 70,000 tpy polypropylene plant at Dushanzi in Xinjiang. $60 million. 6/91.

China Paint Manufacturing (HK)
Will begin construction of an automated paint factory in Shenzhen. $25.64 million. (HK $200 million). 5/91.

Pan Pacific Ocean Group (US)/Guanghan City, Sichuan Province
Opened Guanghan Pan Pacific-Ocean Metal and Chemical Co Ltd. joint venture to produce additives for the metallurgical industry and raw materials for the chemical industry. 5/91.

Construction Materials and Equipment

China's Imports

Deutsche Babcock AG (Germany)/Shandong Dedashen Furniture Materials Co. Ltd., a joint venture between Schenck Ltd. (Germany) and Dezhou Furniture Materials Industrial Co.
Sold equipment for manufacturing decorative surface for cotton-stalk particle board. 6/91.

King, Taudevin, and Gregson (UK)/Shanghai Foreign Trade Corp.
Won contract to design and supply equipment for a lighting plant at Nan Xian, near Shanghai. $1.45 million (£830,000) 5/91.

Investments in China

Mitsubishi Metal Corp. (Japan)/Yantai Building Material Industry Co.
Established Yantai Mitsubishi Cement Co. joint venture. $90 million. 6/91.

Hong Kong firm/Manshan Iron and Steel Co.
Established joint venture to produce 1.2 million miniature screws annually. $700,000. 5/91.

Schenck Co. Ltd. (Germany), a subsidiary of AG fur Industrie and Verkehrswesen (Germany)/Shanghai Machinery and Electric Industry Co.
Agreed to establish 50-year German Shanghai Schenck Test Equipment Joint Venture Co. Ltd. $5.4 million. (DM 8.6 million) (Ger:50%-PRC:50%). 5/91.

China's Investments Abroad

Peru/China
Signed agreement to build 30,000 tpy cement plant in San Martin. $7.5 million. (Peru:23%-PRC:77%). 5/91.

Consumer Goods

Investments in China

Australian Origenes Enterprises PTY Ltd. Investments (Australia)/Langfang Lancheng Industrial Products Co. Ltd.
Established Langfang Lan-Ao-Jin Plastics Co. Ltd. joint venture to manufacture plastic bags. $671,200. (Aust:30%-PRC:70%). 6/91.

Hoechst Celanese Corp.(US)/China National Tobacco Corp.
Will establish a joint venture to produce cellulose acetate tow and flake for cigarettes with annual production of 25,000 tonnes. 5/91.

Electronics and Computer Software

Investments in China

Cogitate Computer Software Engineering Co. Ltd. (HK)/NA (Yantai, Shandong Province)
Will establish joint venture to manufacture high-end printers. $10 million. 6/91.

Contac Co. (Japan)/Changjiang Computer Group Corp.
Established Shanghai Contac Electronic Co. joint venture. 6/91.

NA (Japan)/Shanghai Ship Technique Institute
Established Shanghai Xiyou Information Technology Co Ltd. joint venture to design computer hardware and software. 6/91.

NEC Corp. (Japan)/Beijing
Signed contract to produce large-scale integrated circuits. 6/91.

Hewlett-Packard Co. (US)/Shanghai East China Computer Corp.
Established the Hua Pu Information Co. joint venture to manufacture computer terminals. $9 million. 6/91.

Chukyo Ceramic Co. (Japan)/Suzhou High Frequency Ceramics Factory
Will form Suzhou Chukyo Ceramic Co. joint venture to produce ceramic electronic parts for televisions and microwave ovens. $750,000 (Japan:80%-PRC:20%). 5/91.

Kawasaki Steel System Research and Development Corp. (Japan), a subsidiary of Kawasaki Steel Corp. (Japan)/Beijing Beike Information Processing Corp., an affiliate of the Beijing Science and Technology Research Institute
Established Beijing Kebao Systems Engineering Company Ltd. to conduct research and development of computer software for engineering applications. $1.5 million. (Japan:51%-PRC:49%). 5/91.

China's Investments Abroad

Moscow Power Engineering Institute (USSR)/Jinghai Computer Group Corp.
Will establish joint venture to develop high technology products. $1 million (USSR:50%-PRC:50%). 6/91.

Other

Business Plus Corp. (US)
Opened representative office. 6/91.

Lucky-Goldstar Group (ROK)
Opened Beijing office. 6/91.

Samsung Co. Ltd. (ROK)
Opened Beijing office. 5/91.

Environmental Technology and Equipment

Other

Asian Development Bank
Approved technical grant for feasibility study of the Dalian Multi-Purpose Water Resources Development Project. $600,000. 5/91.

BCA Industrial Control Ltd. (Can) and Dresser Pump, a division of Dresser Canada Inc. (Can)
Will supply process-control equipment and process pumps for water-treatment project in Wuhan. $5.65 million. (C$6.39 million). 5/91.

Canada/Fujian Province
Provided loan for the expansion of a water-treatment plant in Fuzhou, Fujian Province. $5.1 million (C$5.85 million). 5/91.

Food and Food Processing

Imports

De Danske Sukkerfabriker A/S (Denmark)/China National Technical Import-Export Corp.
Sold equipment and technology for sugar refinery in Hailun County, Heilongjiang Province. $20 million (Dkr135 million). 5/91.

Investments in China

Huamin Pharmaceutical Co. Ltd./Fuding Pharmaceutical Plant
Established Fuding Huamin Pharmaceutical Corp. to produce 250 tonnes of caffeine annually. $1.7 million.

Kuang Ta Grain Co. (Taiwan)
Will build vegetable-oil plant near Shanghai. $3.6 million. (T$100 million). 6/91.

San Miguel Brewery Ltd. (HK), a subsidiary of San Miguel Corp. (Philippines)/Guangzhou Brewery
Established Guangzhou San Miguel Brewery Co. Ltd. joint venture. $5 million (HK$39 million). 6/91.

Singapore
Established East Asia Food Co. joint venture to produce 10,000 tonnes of biscuits annually. $10.75 million. 6/91.

Foreign Assistance

Credit Agricole (Fra)/Shanghai Investment and Trust Corp. (Sitco)
Will provide export credit for projects and technical renovations in Shanghai. $35 million (Ffr200 million). 6/91.

United Nations Development Programme
Will provide five-year assistance program for China. $170 million. 6/91.

Belgian Government
Will resume interest-free loan. $5.7 million. (BFr 200 million). 5/91.

Japanese Government
Will provide loans for 14 projects in agriculture, transportation, and energy infrastructure. $400 million (J¥ 55.4 billion). 5/91.

Leasing and Insurance

Investment in China

Korea Industrial Leasing Co., a subsidiary of The Korea Development Bank (ROK), Crown Leasing Corp. (Japan), a subsidiary of The Bank of New York Co. Inc. (US), and The Nippon Credit Bank Ltd. (Japan)/People's Construction Bank of China and China National Chemicals Import-Export Corp.
Established International Far Eastern Leasing Co. joint venture in Shenyang. $410 million (ROK:10%, Japan:40%-PRC:50%). 6/91.

Other

Sumitomo Life Insurance Co. (Japan)
Opened office in Beijing. 6/91.

Machinery and Machine Tools

China's Imports

Sulzer Bros. Ltd (UK), a subsidiary of Gebruder Sulzer AG (Switzerland)
Will supply pumps and technical expertise for the Peng Yue Pu sewage pumping station at Shanghai. $4.2 million (¥ 2.3 million). 5/91.

Investments in China

NA (ROK)/Shanghai High-Pressure Container Plant
Will establish Shanghai Tianhai High Pressure Container Co. Ltd. joint venture. $17.24 million. 6/91.

NA (US)/Nanjing No. 2 Machine Tool Works and Jiangsu Machinery and Equipment Import-Export Corp.
Established Nanjing Sumeida Machine Tool Manufacture Co. Ltd. joint venture to design and produce cutting machines and accessories. 6/91.

Medical Supplies and Equipment

Investments in China

Germany/China
Will establish secondary school to train technicians in producing artificial limbs. 6/91.

Japan/China
Established Shanghai Houcheng Stomatological Hospital. 6/91.

Medtronic Inc. (US)/Industrial Corp.
Will establish Medtronic Medical Devices Ltd. Ningbo joint venture to focus on long-term development of cardiovascular medicine in China. 6/91.

NA (Japan)/Beijing Furui Biological Engineering Co.
Established Beijing Wantai (Panavita) Biological Co. to develop biological products and medical equipment. 6/91.

Pan Asia Trading Co. Ltd. (Japan) /Beijing Jiandu Pharmaceutical Factory
Will establish joint venture to market Sanhuang Pearl Cream burn medicine. $600,000 (Japan:50%-PRC:50%). 6/91.

Other

United Nations Children's Fund and UN Fund for Population Activities
Will provide grant for tetanus innoculation of women of childbearing age in 300 remote counties. $15 million. 6/91.

Japan
Pledged aid for the International Peace Maternity and Child Health Hospital in Shanghai for the purchase of medical equipment. $1.15 million. 5/91.

Packaging, Pulp and Paper

China's Imports

A. Ahlstrom Corp. (Finland) and George Chiang Associates (US)/China National Machinery Import-Export Corp.
Sold machinery for paper pulp production plant in Hexian County, Guangxi Province. $6.22 million. 5/91.

Sunds Defibrator AB (Sweden), a subsidiary of Svenska Cellulosa AB (Sweden)/China National Machinery Import-Export Corp.
Sold paper pulp production equipment for plant in Hexian County, Guangxi Province. $18 million. 5/91.

Investment in China

NA (Japan)
Established Shanghai Longying Color Printing Co. Ltd joint venture. $4.4 million. 6/91.

NA (Taiwan)
Established Xingrong Bamboo Co., a wholly-owned project in Susong County, Anhui Province. $1.5 million. 5/91.

Petroleum and Natural Gas

Investments in China

Japan National Oil Corp./China
Signed agreement to cooperate in oil exploration in southern Jiangsu Province. 6/91.

NA (ROK)/Shanghai High Pressure Container Factory
Will establish joint venture to produce 600,000 gas cylinders annually. $17.1 million (¥90 million). 6/91.

TOTAL Compagnie Francaise des Petroles (Fra)/Dalian Economic & Technical Devlopment Corp., China National Chemical Import-Export Corp., City of Daqing, Liaoning Province, and a unit of the Ministry of Chemical Industry
Will establish Dalian West Pacific Petrochemical Co. joint venture to build and operate a 100,000 barrel-a-day, 5 million tpy refinery in Dalian, Liaoning Province. $470 million (Fra:20%-PRC:80%). 6/91.

Japan National Oil Corp. (Japan)/China National Petroleum Corp.
Will conduct four-month joint operation for geophysical prospecting in the southwestern part of the Tarim Basin. 5/91.

Other

Mitsubishi Corp. (Japan)
Will provide loans for developing new oilfields in Xinjiang Uygur Autonomous Region. 5/91.

Power Plants

China's Imports

Fragema G.I.E. (Fra), a subsidiary of Framatome S.A.(Fra)/ China National Nuclear Corp.
Will provide technology and equipment needed to upgrade production at the Yibin Nuclear Fuel Fabrication Factory in Sichuan Province and to increase nuclear fuel reloading ability for the Daya Bay Nuclear Power Station in Guangdong Province. 5/91.

Other

British Engineering Co. (UK)/China National Technical Import-Export Corp.
Provided mixed loan for construction of the Fuxun Heat and Power Plant project in Liaoning Province. $55.38 million. 6/91.

Property Management and Development

Investments in China

Shangri-La Hotel Ltd. (Singapore) and Gaviota Ltd., a subsidiary of Kuok Ltd. (Singapore)/Shenzhen Asia Industry Development Co.
Will build Shangri-La Hotel in Shenzhen. 6/91.

Yaohan Department Store Ltd. (HK), a subsidiary of of Yaohan Departmentstore Co. Ltd. (Japan)/Shenzhen Sha Tou Kok Import-Export Trading Corp.
Will establish Shenzhen Sha Tou Kok Yaohan Department Store joint venture in Shenzhen. $1.9 million (HK$14.9 million) (HK:49%-PRC:51%). 6/91.

Ricoh Corp. Ltd. (Japan)
Began construction of an industrial district for the Japanese Ricoh Industrial Development Co. in Shenzhen. $16 million (J¥ 2.2 billion). 5/91.

Yaohan Department Store Ltd. (HK), a subsidiary of Yaohan Department Store Co. Ltd. (Japan)/Shanghai No.1 Department Store
Will build Shanghai No.1 Yaohan Shopping Center in Pudong. $100 million (HK:51%-PRC:49%). 5/91.

Scientific Instruments

China's Imports

Input/Output Inc. (US), a subsidiary of Kidde Inc. (US)/China National Technical Import-Export Corp.
Sold two I/O System One XL land seismic-data acquisition systems. 6/91.

Investments in China

Moscow Power Engineering Institute/Beijing Jinghai Computer Group Corp.
Will establish joint venture aimed at turning scientific research achievements into commercial products. $1 million. 5/91.

Other

Brazil/China
Will build two earth exploration resource satellites for mutual use. $150 million. 5/91

Ships and Shipping

China's Imports

General Electric Information Services Unit (US), a subsidiary of General Electric Co. (US)/China Ocean Shipping Co. (COSCO)
Will provide communications and electronic data interchange (EDI) facilities for COSCO's fleet. 5/91.

Investment in China

Heung-A Shipping Co. (ROK)/China Ocean Shipping Co. (COSCO)
Began operation of Cohung Shipping Co. joint venture with direct container service between China and South Korea. $2 million (ROK:50%-PRC:50%). 5/91.

China's Investments Abroad

Hongkong International Terminals Ltd.(HK), a subsidiary of Hutchison Whampoa Ltd. (HK)/COSCO
Established COSCO-Hit Terminals (Hong Kong) Ltd. joint venture to construct two berths at Hong Kong's Kwai Chung container port. $897 million (HK$7 billion). 5/91.

Telecommunications

China's Imports

SESA Co. (Spain)/Shanghai
Sold program-controlled telephone exchange equipment financed by Spanish government mixed loan. 5/91. $34 million.

Investments in China

NEC Corp. (Japan)/Tianjin
Signed contract to develop computer-controlled telephone exchanges. 6/91.

Textiles

Investments in China

Marubeni Corp. (Japan) and Chemtext Inc. (US)/Guangzhou Synthetic Fiber Plant, Guangzhou International Trust & Investment Corp., and Guangzhou Economic & Technical Development District Construction Corp.
Will establish Asian American Polyester Ltd. joint venture to produce materials for synthetic fibers. $20 million (Japan:25%-US:25%-PRC:50%). 6/91.

Hong Kong/NA
Established Shanghai Zhongxin Textile Printing Co. joint venture. $12 million. 5/91.

National Technology Export Corp. of the Soviet Union and three other Soviet enterprises/Baotou Linen Textile Mill, Ltd.
Agreed to establish Baotou Cymeht Linen Textile Co. in Inner Mongolia. $24.2 million (¥129 million). (USSR:37.1%-PRC:62.9%). 6/91.

Ming Hsing Textile (Taiwan), a subsidiary of Lai Sun Garment Co. Ltd. (HK)/Shanghai No. 10 Dyeing and Finishing Factory
Will establish a textile finishing and dyeing joint venture. $5.8 million (Taiwan:50%-PRC:50%). 5/91.

Transportation

China's Imports

Nationale Industrielle Aerospatiale (France)/China National Machinery Import-Export Corp.
Sold eight 2 tonne-class helicopters for fighting forest fires. $13 million (Ffr 70.9 milllion). 5/91.

Investments in China

ALA Ltd. (Ita), a subsidiary of Boffa Group Ltd. (Ita)/Hubei Asbestos Product Mill
Established joint venture to produce car disc-brake pads in Xiangafan, Hubei Province. $2.1 million (Ita:25%-PRC:75%). 6/91.

Chia Tai Group (Thailand)/Shanghai Storage Battery Factory
Will establish joint venture for the production of storage batteries for vehicle and industrial use. $29 million. 6/91.

General Motors Corp. (US)/NA
Will establish joint venture to produce 50,000 small trucks a year in Liaoning Province. 6/91.

NA (HK)/Yangzhou Bearing Factory
Will establish joint venture to supply bearings required by vehicle manufacturers. $2.74 million. (HK:49%-PRC:51%) 6/91.

McDonnell Douglas Corp.(US)/China National Aero Technology Import-Export Corp.
Established joint venture to design and manufacture dual-tandem landing gear for the MD-90 twin-engine jet airliner assembled at the Shanghai Aviation Industry Corp. facility. $2 million. 5/91.

Other

Ameco, a joint venture between Deutsche Lufthansa and Air China
Will build aircraft maintenance hangar for Lufthansa. $82 million (¥430 million) (Ger:40%-PRC:60%). 6/91.

Asian Development Bank
Approved loan and technical assistance grants for a 141-mile, single-track railway between Yaogu and Maoming in Guangdong Province. $1.2 million. 6/91.

Sofrasia (HK)
Opened representative office in Shanghai as the sole agency for General Motors Corp. (US) in China. 6/91.

World Bank
Provided loan for a 120-mile kilometer highway linking Zhengzhou and Luoyang in Henan Province. $90 million. 6/91.

Asian Development Bank
Approved loan and two technical assistance grants for Nanpu Bridge project in Shanghai. $71.68 milliion. 5/91.

CLASSIFIEDS

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