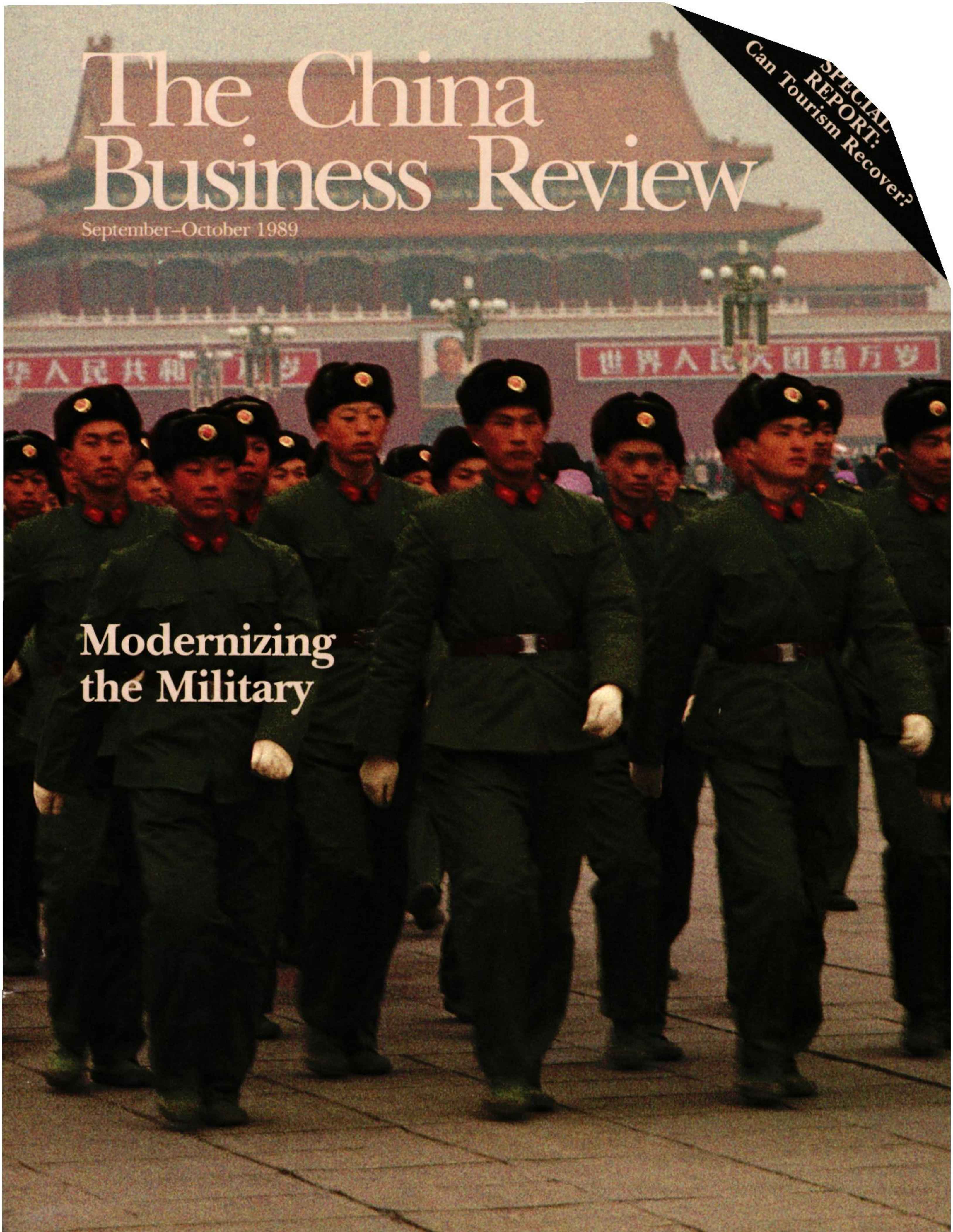
The China Business Review

September–October 1989

SPECIAL REPORT: Can Tourism Recover?



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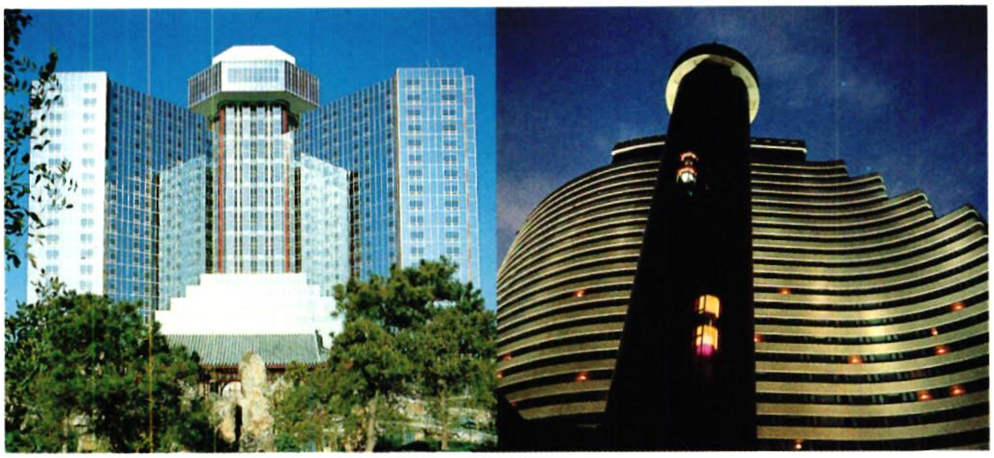

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The China Business Review

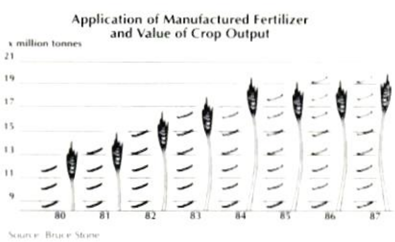
The magazine of the US–China Business Council

September–October 1989 Volume 16, Number 5

Cover: Chinese soldiers, December 1987. *Photo by Richard Wiseman.*

Tourism: Bad news that could get worse.

Fertilizer: A fast-growing industry.



Departments

RECENTRALIZING TRADE

Chinese authorities have announced several new measures to recentralize control over the trade regime and stabilize the rapidly deteriorating balance of trade. China's trade deficit—which mushroomed to \$6.56 billion in January-July and could exceed \$10 billion by year-end—has been compounded by the consequences of recent political instability, as tourism receipts, estimated to total \$2.2 billion in 1988, have declined drastically. Capital inflows via foreign equity investment and commercial and non-commercial credits have also been reduced following China's crackdown on pro-democracy demonstrators in June. According to a recent CIA report, foreign reserves, estimated to total \$17.49 billion in January (including gold), had dropped precipitously by the end of June.

Chinese authorities have always been quick to counter significant reductions in their reserve holdings, in part by restricting imports. Accordingly, they have announced the following measures:

- **Cutbacks on foreign trade authority.** Reducing the total of 5,000 enterprises authorized to trade directly with foreign companies is aimed at curtailing nonessential imports and limiting price competition between Chinese buyers and suppliers, in order to maximize the nation's foreign-exchange reserves.
- **Extending MOFERT's control.** Additional categories of first-tier goods, including grain, sugar, steel, fertilizers, plastic film for crop protection, crude and refined oil, timber, polyester fibers, tobacco, cotton, and pesticides, may only be imported by central trading companies under MOFERT.
- **Restricting imports.** New quality inspection requirements will effectively reduce imports of luxury goods. As of May 1, 1990 cars, motorcycles, motorcycle engines, refrigerators, air conditioners, compressors for air conditioners and freezers, televisions and television tubes, and 148 other items must be approved by the State Administration of Import and Export Commodity Inspection. Quality certificates must be obtained at least six months in advance of the final sales.

The Ministry of Machinery and Electronics has ceased issuing import licenses for television sets and assembly lines (excluding picture tubes), computers, videocassette recorders, integrated circuits and other electronic products.

Continued concern over the trade deficit and balance of payments will probably lead to even further tightening of import controls. Agricultural products and grain will probably be exempt, but consumer goods, industrial equipment, machinery, and raw materials imports may be further curtailed to conserve scarce foreign exchange.

Ironically, China's austerity program has perversely contributed to its trade problems. Exports have stagnated as the State-owned industrial sector has slowed production, in an effort to cool China's overheated economy. China's factories and farmers, however, have turned to foreign markets to supply them with locally scarce production materials, resulting in import growth almost five times that of exports. The need to further tighten import restrictions first announced last fall and the burgeoning trade deficit reflect an economy still out of control.

—PB, RB

TWO BIRDS WITH ONE STONE

In a famous scene from the film *Casablanca*, the French chief of police is ordered by Nazi occupation authorities to close Rick's bar. Looking for a pretext, the police chief—a regular winner at Rick's roulette tables—assumes a mock-indignant expression, blows his whistle, and scolds, "I'm shocked, *shocked* to learn that gambling goes on here!"

China's latest anti-corruption campaign, announced after a Politburo meeting ending on July 28, has some of the same serio-comic flavor. Confronted with a growing trade deficit, high inflation, and excessive growth in the maverick southern provinces, Beijing has decided to make a virtue out of the perceived necessity for greater central control. In the name of stemming bribery, nepotism, and profiteering, the new campaign will focus on reducing the number of foreign trade corporations and shutting down or cleaning up large trading companies notorious for their ties to top leaders and their off-the-books accounting practices.

Not coincidentally, official corruption was one of the most strident complaints of the pro-democracy demonstrators in May and June, and is one of the few issues that unites students and workers. The opening of the campaign seems timed to score points with critics of the central leadership, although many of the accomplishments announced in July—the closing of Kanghua Industrial Corp. and the China Industry and Commerce Economic Development Corp. (INCOMIC), audits of Everbright Industrial Corp. and China International Trust and Investment Corp. (CITIC), and merging of China Rural Trust & Investment Corp. into the National Agricultural Investment Corp.—had already gotten underway in October 1988 as part of the economic austerity drive. Stiff fines have also been levied on the five companies, which all come under the State Council's direct control. Everbright will pay the most—\$5.2 million—and CITIC is being fined \$5 million.

Other measures are still to come. The campaign pledges to bar children of senior officials from engaging in commerce as of September 1; to end high officials' access to special foods and imported sedans; to stop the use of public funds for entertainment and gifts; and to curtail official visits abroad, especially at the invitation of foreign companies. In addition, China will launch a drive to collect unpaid taxes from private businesses, about 70 percent of which, the government claims, have not paid up.

While these measures are the stiffest to be invoked in some years, anti-corruption campaigns come and go, generally with little effect. For example, when Zhao Ziyang announced last spring that the Party must curb corruption or "the reforms will not continue," not a single top-level official came in for criticism. Instead, such campaigns tend to become battlegrounds for intra-Party factions. This time around, Zhao's oldest son, Zhao Dajun, is rumored to have been arrested on charges of profiteering at the Shenzhen New Technology Development Co., where he is general manager. He may have to take the fall for children of other, more favored officials.

—ASY

SWAP CENTER SETBACK

It's hard to believe how optimistic *The CBR* sounded in an article on swap centers published exactly one year ago. The subtitle, for example, indicated that the centers "may be moving China down the road to full currency convertibility." In the face of China's current economic woes, that road now appears endless, and the swap system itself—far from last year's predictions of rapid expansion and easing of restrictions—may be running out of fuel.

First opened in Shenzhen in 1985 and totalling around 40 last August, swap centers were created to provide restricted access to foreign exchange, an alternative to devaluing the renminbi (RMB). The centers provided foreign investors with a foreign exchange balancing mechanism, and benefited Chinese exporters by allowing them to use their retained foreign exchange earnings to purchase RMB at a premium—the rates generally hovered between ¥6-7:$1, compared to the official rate of ¥3.7:$1—with which to bid up on often scarce raw materials in the interior.

The last few years have seen rapid growth in both the number of centers grow and the volume traded, and while the centers are not the answer to every investor's cash-flow problems, foreign companies were generally pleased with them, and hopeful that restrictions on access—individuals are only allowed to trade at the Xiamen SEZ center, for example—trading across provincial lines, among other things, would gradually be eased as more centers opened and competition thrived.

Last fall's austerity drive, however, and the consequent tightening of domestic credit has made RMB harder to come by, and increased demand for Chinese currency at the swap centers. The main foreign exchange pipeline to the centers—tourist hotels—may also be closed off by the dramatic drop in tourism. Trading volumes are down along with rates, which reflect the new scarcity of RMB. At the Shanghai center in August, for example, the supply of US dollars exceeded demand by $740,000.

US companies are already feeling the pinch. In August, one investor reported that his company is now restricted to swapping in its own province, whereas until recently it carried out swaps in centers all over China. As regions grow more reluctant to let foreign exchange out of their jurisdiction—special permission is required from Shanghai's mayor to take swapped money out of the city—differences between regional rates will continue to rise as arbitrage is curtailed. Recent adjustments in swap center policies reflect the Chinese government's renewed concern over superfluous imports: in some areas, swaps involving consumer products manufacturers are reportedly being restricted.

It seems clear that the lack of liquidity will slow down if not cancel the planned openings of new centers, and that trading volume will continue to be depressed. Whispers of devaluation are, as ever, in the air, which may further depress swap market business if foreign investors take the rumors seriously enough to hold onto their foreign exchange. —SER

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COMMENTARY

评论

Richard E. Gillespie

The following testimony was presented at a hearing of the House Foreign Affairs Committee on July 19, 1989.

The US-China Business Council has spent years promoting business and developing contacts with China under the assumption that reform was irreversible and that something like the events in Tiananmen Square on June 4 and afterward could not happen. Now that they have, the Council, along with the entire US business community in China, is struggling to pick up the pieces.

It should not come as a surprise that large American companies that have spent years developing markets in China are reluctant to walk away now. Most companies will try to maintain links with their Chinese counterparts in the hope that the environment in China will change for the better. Naturally, companies with existing investments in China are going to do their best under these adverse circumstances to keep their ventures operating and recover their investments. And at least some companies operating in South China seem thus far to have been spared the fallout of events in Beijing.

The fact that large companies are not making precipitous moves to cut their China ties by no means implies, however, that business is normal. It is not. Many US company representatives have yet to return to China, and those who have are finding their Chinese counterparts preoccupied with political study and in no position to entertain substantive talks about anything other than the most routine business.

Companies want reform, too

A number of American joint ventures in China are already noticing ominous signs of tighter government political controls extending into factories in the form of new Communist Party committees and Party-controlled trade unions. This is clearly not in the best interest of foreign companies operating there. And new US investment is drying up for the fundamental reason that China no longer appears to be the politically stable and economically vibrant country it was previously. It will take much, much more than verbal reassurances from the Chinese for foreign companies to return to their earlier assumptions about both the political and economic risk of doing business in China.

We believe, as do most companies we talk to, that China is going to face a severe foreign-exchange squeeze as a result of the Tiananmen events, which will exacerbate an already bleak economic situation. Tourism has evaporated; new World Bank lending, as well as most foreign governments' concessional lending, is on hold; commercial banks are wary of extending new loans; Hong Kong capital is skittish. Even with the best intentions, US companies cannot do business in China if there is no money.

Corporate America is waiting for the same things as Congress before resuming business as usual in China: a return to political stability and normalcy, and to economic liberalization and development.

Sanctions could backfire

The measured steps that the president and Congress have so far taken to demonstrate American outrage and deny China some of the benefits of the US-China relationship are entirely appropriate. We question the need for further unilateral economic sanctions, however, given the extent to which US companies have of their own accord reduced their economic activity with China. Sanctions have some general problems that are particularly acute when applied inappropriately to China.

First and foremost, additional unilateral sanctions will give the Chinese hardliners the opportunity to blame their economic woes on the US government, rather than on their own actions. Given the historic Chinese sensitivity to foreign domination, hardliners are quite capable of using the appearance of American interference as a nationalistic rallying point, which could have the unintended effect of further hardening their policies and prolonging their hold on power. Unilateral sanctions are also likely to diminish the reservoir of goodwill for the United States that is so evident in the Chinese people, and in the low and middle levels of the Chinese government.

Although I do not suggest that the current situation is exactly comparable, the Sino-Soviet relationship shows the effect of sanctions gone wrong. By suspending all economic aid to China in 1960, the Soviet Union effectively initiated a 25-year freeze in relations.

Furthermore, to the extent that further sanctions do have an impact, they are likely to hurt exactly the people we want to help. Higher tariffs on imports into the United States, for example, will chiefly affect the enterprises exporting labor-intensive products from southern China, which have been in the vanguard of economic reform. Some of these enterprises represent, in effect, China's private sector, and many of them are run by US or Hong Kong companies that would be sharply affected by a decline in China's exports.

The Council's stance on sanctions is based on the belief that China's integration into the world economy and contact with Western business have been a powerful force for political, economic, and social progress in China. If the US government moves to dismantle the structure of US-China economic coopera-

Richard E. Gillespie recently retired as vice president of the US-China Business Council, after serving with the Council since 1979.

tion, it will be shutting off the engine driving both political and economic progress. It seems logically inconsistent to do this while calling in the same breath for increasing political reform. It goes without saying, of course, that we must cut off support for China's repressive apparatus, including the military, the police, and the propaganda machine.

Actions must be unified

Where, then, should we go from here? The US government must continue to forcefully express its displeasure with events in China and continue to freeze military cooperation and high-level government contacts. We must bring home to the leaders in Beijing the damage they have inflicted on themselves.

Before adopting any further sanctions, the US government should continue consulting with other Western countries and Japan to ensure that reactions to events in China are coordinated and multilateral. Since US high-tech exports to China account for only about 10 percent of the worldwide total, and US credits to China comprise only a tiny fraction of those from Japan and Europe, further US government sanctions would not be effective unless Japan and other Western countries followed suit. For Congress to unilaterally suspend China's most-favored nation (MFN) status—along with activities of the Overseas Private Investment Corp., Export-Import Bank, and Trade and Development Program—without comparable actions by other governments would simply penalize US traders and investors without doing much to hurt China. Suspension of MFN would also invite Chinese retaliation against US exporters of grain, lumber products, and other commodities.

US companies competing in China are already hampered by the 10-year head start given to Japan and Europe by the United States' failure to recognize the Chinese Communist government early on, and it would be harmful to our competitive strategic interests to further widen the gap. Much more important, the US government should do its best to preserve what can be preserved of the framework of the US-China economic relationship, in recognition of the importance of this relationship to positive change in China. The administration and the Congress should act in the realization that companies on their own are already applying the most effective sanctions of all by making decisions to reduce economic activity with China based on negative perceptions of the business climate. If the US government acts with prudence and restraint, the Chinese government will reach the correct conclusions about the adverse consequences of its actions much more quickly, and the United States will be better positioned to play a positive role when China returns to the path of progress. 完

COUNCIL ACTIVITIES

我会活动

Companies Discuss Strategies at Roundtables

Over 100 manufacturers, contractors, and large equipment suppliers participated in three recent Council roundtables on "Doing Business in China's New Environment." The roundtables, held in Chicago, San Francisco, and New York on August 1, 3, and 8 respectively, gave member companies a chance to meet and compare notes on current operations and future plans. Council President Roger W. Sullivan, Martin Weil, manager of the Heavy Industry Program, and Richard Brecher, manager of Investment Services, directed the discussions.

A common theme at all the sessions was that although it is too early to make any final judgements, companies intend to maintain ongoing operations and continue exploring further business opportunities. Most companies indicated that initial commitments to China, based upon long-term, strategic objectives, remain valid, but most do not wish to increase their exposure—either economic or public—and are proceeding cautiously. The basic question is not whether or not to be in China, but how to make the best of a difficult and potentially dangerous situation.

Companies have found that the impact of China's political and economic clampdown varies with a project's location, sector or product line, and endusers or customers. This diversity will become increasingly pronounced, as companies shift from a "coping" phase to dealing with endemic practical problems.

A joint-venture investor that produces goods for the tobacco industry, for instance, remarked on the relatively minimal effect of recent events on his company's operations, which are located well outside the major industrial centers and suffered no setbacks from demonstrations or work stoppages. Moreover, the company's joint-venture partner stands solidly behind the project and has deep pockets to finance short-term deficiencies in construction and working capital. And finally, the chief customer, a monopoly corporation, is prepared to buy all output to minimize its own foreign-exchange commitments for otherwise imported products.

In contrast, nearly all large-scale real estate development projects have been hit hard by the steep decline in tourism and diminished business activity. The financial viability of nearly all of these projects is threatened, unless they are able to restructure and refinance the deals.

On the bright side, a number of companies commented on a surge in recent inquiries and sales. This "Indian summer" effect is due to the eagerness of Chinese enterprises to spend their foreign exchange now, before the government exerts greater control over such expenditures. Other firms noted a sudden willingness on the Chinese side to negotiate and resolve long-standing disputes and grievances. This may reflect the Chinese government's desire to reassure the foreign business community of its commitment to the open door.

The August roundtables differed markedly from similar meetings the Council held last spring in that companies did *not* complain about common, outstanding problems involved in doing business in China, such as balancing foreign exchange; bureaucratic interference; lack of transparent laws and regulations; and difficulty localizing materials, gaining access to the domestic market, and finding skilled and motivated workers. Although these problems remain unresolved, foreign companies have shifted their focus to broader strategic issues, such as their commitment to the China market. Despite reports to the contrary, business as usual will not return until these endemic constraints again assume center stage.

Export Controls Working Group

The Council's Export Controls Working Group met on August 3 in Washington, DC to discuss current US policy on dual-use high-technology exports to China. Joan McEntee, deputy undersecretary for export administration at the US Department of Commerce (DOC), and Christopher Hankin, DOC deputy assistant secretary for international trade controls, spoke to 25 member companies about the status of US export control policy toward China and China policy in the Coordinating Committee for Multilateral Export Controls (COCOM).

Since the Administration suspended military sales to China in early June, many firms have been uncertain how the suspension affects their commercial transactions (*see* p. 32). McEntee described the new enhanced review procedures at DOC—which handles export licensing for dual-use commodities—for all exports to China. The more stringent procedures are adding at least an additional week of processing time for most license applications.

Hankin, whose office represents the United States in COCOM, said that COCOM efforts to liberalize and restructure the export controls system to China, including implementation of a distribution license (DL) system, have been suspended. The United States has also put on hold its own liberalization efforts in these areas.

Travel and Tourism Committee

The Travel and Tourism Committee met on July 7 in New York City to discuss the impact of recent events on China's tourism industry. This summer, tourism traffic slowed to a virtual standstill. Most US operators canceled tours through August, and many major airlines flying into China reduced the frequency of their flights. Japanese airlines report that many Japanese tour companies have canceled bookings through December.

The committee also discussed the State Department's travel advisory to China and its legal ramifications. Companies planning to bring groups to China while an advisory is in effect should take special precautions, since there is no clear reading of the law in such situations. Companies should at the least notify customers in writing of the advisory, and they may want to obtain a signed waiver to be on the safe side.

Committee Chairman David Elmore of First Family of Travel initiated a discussion on refunds by the Chinese for trips canceled or cut short. Even though committee members had all been notified that CITS would issue refunds for unused land costs, some companies were told they would receive cash, while others were told they would receive credit. Committee members agreed on the need for clarification of CITS policies and inclusion of other Chinese tourism units, such as shipping companies, in the refund process.

Following the meeting the committee attended a luncheon hosted by Zhou Yanjun, director of the China National Tourist Office in New York. Zhou informed the committee that CITS will offer special discounts through the end of the year and that Tibet has been reopened to group travel.

The Travel and Tourism Committee will send a delegation to Beijing in September to discuss reviving US tourism to China.

Council Vice President Richard E. Gillespie Retires

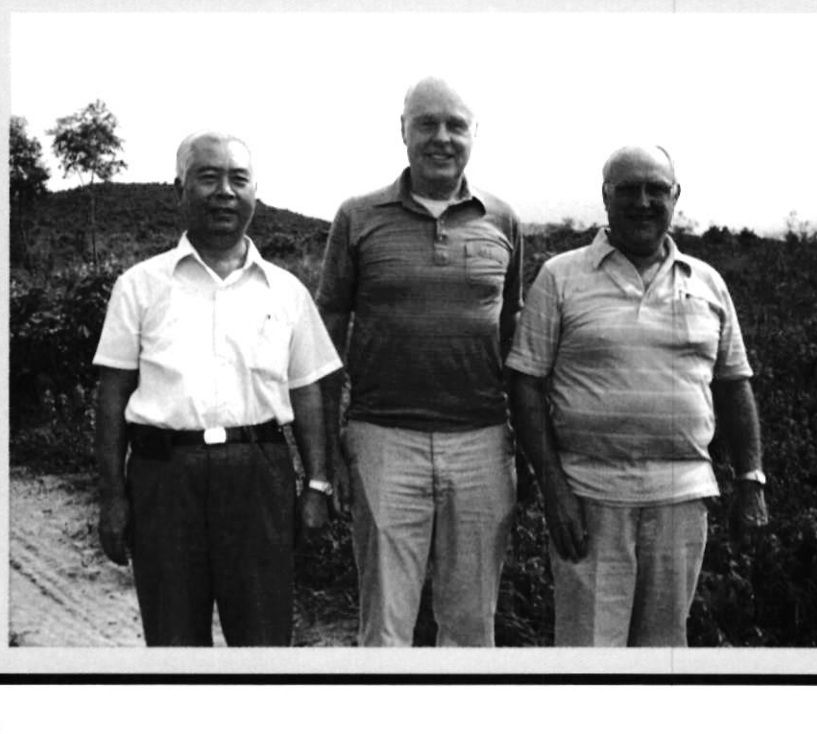
After 10 years of dedicated service to the Council, Vice President Richard E. Gillespie retired at the end of August. Although he held several positions during his Council career, member companies have come to know him best as manager for the project identification and development work that the Council performs under contract to the US Trade and Development Program (TDP), and for his advisory work in high-technology and defense-related industries, especially the aerospace sector.

Gillespie came to the Council in 1979 after 29 years in the US Army, much of that time as a China area specialist. Initially he worked part-time, escorting Council delegations to China and hosting Chinese delegations in the United States, and in 1980 he signed on full-time as assistant director of the Exporter Services department. During this time he served as adviser to numerous Council committees and working groups in various areas, including engineering, mining and metallurgy, machinery and equipment, telecommunications and electronics, and exhibition organizers.

In 1982 Gillespie became the assistant director of the newly formed Business Advisory Services (BAS: an amalgamation of the Importer and Exporter Services departments), and became BAS director in 1985. As director he oversaw the Council's business consulting services to member companies, and also played a key role in the export controls and military sales working groups, leading a delegation of defense contractors to China in 1985. Gillespie became Council vice president in 1987.

One of his primary responsibilities as vice president was administering the Council's TDP program, which he helped establish in 1982. Gillespie and the engineering committee, which he advised, convinced TDP officials that the Council was the most appropriate agency to conduct impartial, independent definitional studies for China projects TDP was considering funding. Since then, he has supervised nearly 50 studies in such diverse fields as energy, transportation, and petrochemicals, conducting some 15 himself.

During his retirement, Gillespie plans to write and do consulting work on China.



On his last TDP mission September 1988, Gillespie (center) visited Hainan Island, where he is pictured with a China Air official and the delegation's technical adviser.

What to Watch For

A guide to China's current business environment

John Frisbie and Richard Brecher

The climate has changed for foreign business in China. Here's a roundup of what companies may encounter in the coming months.

▶ **Preoccupied bureaucracy.** The current campaign to strengthen the role of politics and ideology is much stronger than many foreigners realize. Most companies report no change in personnel on the opposite side of the table, giving business the look of normality.

All is not as before, however. Government personnel—at least up to the vice ministerial level, if not higher—are participating in study sessions and undergoing substantial pressure to conform to the Party line. Although few of the bureaucrats involved in foreign business affairs are likely to be replaced, several companies report that their counterparts appear to be under stress.

Furthermore, the obvious leadership instability has made many bureaucrats unsure of the present and future course of official policy. As a result, functionaries are preoccupied with internal matters, and thus not inclined to take risks, such as approving new, complex deals. Companies should be prepared for a potential slowdown in decisionmaking, as more officials become involved in the review process.

▶ **Increased official interference.** Unsure of policy lines, bureaucrats at all levels may seek to spread responsibility for decisions by kicking them further up the ladder. One company was informed by its prospective partner—just prior to finalizing a joint-venture contract—of a unilateral decision by an unidentifed party that a majority partner to the deal, a Hong Kong-based Chinese firm, would not be permitted to participate.

If trade and investment authority is effectively recentralized, existing deals completed under local approval authority may require review by higher authorities, as will approval of such activities as import and export licensing, granting of loans and credit, etc.

▶ **Greater Party and trade union role.** With the current emphasis on ideology, Party cadres and trade unions are expected to take on a larger role in Chinese enterprises, and there may be efforts to extend this influence to joint-venture enterprises. Investors should be prepared to deal with such pressures.

Although joint ventures are required by law to set up labor unions, in the past the unions have played a minimal role in labor-management relations. Recently, however, some companies have reported pressure to grant the unions more say. In one case, the Chinese partner, at the behest of the department in charge of the venture, requested that the union representative assume a seat on the venture's board of directors.

Another company reported that the Chinese partner requested a local Party official's placement on the joint-venture board. The US partner responded that the Chinese partner was free to name the official as one of its board nominees when a position opened up, but that no special appointment would be made.

▶ **Continued propaganda**. Business has not stopped, of course, and companies are continuing to close deals in China. These new projects are the exception, not the rule, however. Most companies will maintain contact and move forward slowly on established or planned projects, but new signings will slow substantially. Announcements of concluded deals will be played up considerably by the Chinese—a case in point is the recent announcement of an agreement between Tianjin and the M. G. Malekpour Co. of the United States to develop property in the Tianjin Economic-Technological Development Area (TEDA). While a land-lease contract has been signed, financing has yet to be raised. This deal is far from complete, and would not have generated the attention four months ago that it has in the current climate.

▶ **Less reliable statistics**. Although Chinese statistics have become more reliable in recent years, they must always be read with caution. This is especially true now, when authorities must convince both the Chinese people and foreign businesses of their control over the economy. Independent, non-governmental evaluators will probably have less access to statistical data and will be pressured to toe the official line. The current propaganda campaign to bolster the Party and minimize the impact of this summer's political instability on the economy also necessitates that companies review official statements with care before making important decisions based on them.

▶ **Indian summer**. A few companies report that July and August were banner sales months. Chinese enterprises with foreign exchange want to spend it now in case controls are tightened or import policies changed. Two companies reported being asked by Chinese buyers to backdate contracts in order to avoid possible cancellation by authorities. This Indian summer effect is not expected to last, however, and even companies now enjoying it expect sales to slow by the fourth quarter.

The Indian summer is extending beyond sales to benefit other areas as

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John Frisbie, based in Beijing, is director of China Operations for the US-China Business Council. Richard Brecher is manager of the Council's Investment Advisory Program in Washington, DC.

well. With the Chinese anxious to win companies back, expect them to make efforts to smooth out problems. One company sent a delegation to China in July and successfully won final payment on a technology-transfer deal that had been in dispute for two years. Another reported more business accomplished in two days of negotiations in July than in the preceding three months.

But this doesn't mean that now is a good time to win major concessions from the Chinese. They will not be willing to compromise on the major issues plaguing negotiations (such as foreign exchange support for a joint venture), and any grand promises made now may not be kept later. Instead, press for resolution of ongoing problems that always seemed resolvable before, if the Chinese had wanted to make the effort.

▶ **Slow sales.** The ongoing austerity campaign, combined with a projected balance-of-payments deficit and corresponding tightening of foreign exchange, will slow sales to China by most—but not all—companies. Those that sell to organizations earning their own foreign exchange, for example, will have better opportunities for sales, and if they are selling priority goods and technology, they may actually register healthy sales in 1989-90. Most companies, however, should count on a downturn in sales in the near term, as the government tightens controls over imports and attempts to recentralize foreign-exchange spending.

▶ **More import controls.** China will post a large merchandise trade deficit this year. While this will not cause immediate balance-of-payments difficulties, a continued large deficit would create problems next year when coupled with the downturn in new loans, new foreign investment, tourism, bond issues, and remittances.

To control spending, the State has already moved to increase import controls, banning outright imports of certain consumer and industrial goods and processes and increasing its control over others through various approval mechanisms (*see* p. 4).

The key question is what practical effect these measures will have. In previous years, balance-of-payment deficits meant immediate cutbacks in imports. But with today's decentralization of the trade apparatus and foreign-exchange retention, can the central government still call the shots? The State's authority may be further undermined by the perception that the summer's events weakened the central government, which remains too preoccupied by political issues to exert much influence in the provinces—particularly in Guangdong, where the strong governor is developing a semi-independent, lively economy closely linked with international markets.

▶ **Emphasis on *force majeure* clauses.** Recent events have heightened the awareness of both Chinese and foreign businesspeople of the potential effects of political instability on contract implementation. While Chinese contract law permits *force majeure* clauses, definitions of and guidelines for dealing with disruptions from civil disobedience are vague. Companies should expect their Chinese conterparts to haggle over these points in new contract negotiations.

The Chinese will not be willing to compromise on the major issues plaguing negotiations, and any grand promises made now may not be kept later. Press instead for resolution of ongoing problems that always seemed resolvable before, if the Chinese had wanted to make the effort.

▶ **Reappearance of lending.** The current mutilateral halt in new lending by Western banks and the international development banks may develop cracks in the coming months, as one by one, banks creep back into the China market. The Japanese government announced in August, for example, that Japanese banks were welcome to return to China, although they will probably wait until the October World Bank/IMF discussions. Loan activity will increase only slowly, however, for political-risk reasons, and will climb only if stability is maintained over the longer term. Until the World Bank and Asian Development Bank resume consideration of new loans to China, commercial lending will be dampened and rates on the high side.

▶ **Regional differences.** The effects of the current ideological campaign are felt most strongly in Beijing, and to a lesser extent Shanghai. Expect the rest of China—particularly Guangdong and Fujian—to move along much as normal, while paying lip-service to the campaigns announced from Beijing.

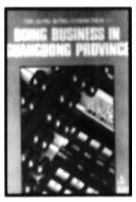
▶ **Decreased transparency.** The current political atmosphere is no longer conducive to making information about the formulation and issuance of policies, laws, and regulations more transparent, a direction in which China had been slowly moving in recent years. Companies may again run into problems with unresponsive negotiators constrained by *neibu* (forbidden) rules that are not explained to foreigners. Lack of fully public laws and regulations frustrates companies, wastes time, and adds to the risks of doing business. The tension and mistrust that result from seemingly arbitrary rules could further deteriorate the business environment.

▶ **Economics will drive politics.** The events of June 4 and afterward do not spell the end of pressures for political liberalization and reform in China. Years from now, the recent crackdown will appear as a single point on a longer evolutionary timeline. In the near term, however, numerous political scenarios, ranging from further violence to gradual change, all seem plausible.

Aside from the wild card presented by the failing health of Deng and other elderly leaders, it seems likely that the next set of political pressures will be fueled by economic problems. Most analysts believe that China is in for tougher economic times in the coming year, and those lean times may provide the opportunity for the current regime to jettison some of its less popular figures—Premier Li Peng is a likely candidate. Unlike democracy, which chiefly concerns intellectuals and students, economic issues strike the government and the Party in the heart—the working population—and cannot be be propagandized away. 完

BOOKSHELF

书刊介绍



Doing Business in Guangdong Province, by Katherine Forestier. Hong Kong: American Chamber of Commerce, 1989. 178 pp. $26 softcover.

While southern Guangdong province had its share of demonstrations during the recent turmoil in China, for the most part its people express their differences with Beijing through quieter—and more productive—pursuits, thereby effectively protecting their economic autonomy. This book provides informative, practical answers to the most common questions companies ask in exploring various investment and trade options in the province.

The first eight of the book's nine chapters address the business environment in the major cities and regions of the province, such as Guangzhou; the Shenzhen, Zhuhai, and Shantou Special Economic Zones (SEZ); and the Pearl River Delta area. Each section begins with 2-10 pages of text describing the area's infrastructure, agricultural, industrial, or manufacturing background, trade and investment trends and incentives, infrastructure (including transportation), energy capacity, and areas of potential investment opportunity for foreign companies. Some of the chapters also include sections on labor conditions, wages, natural resources, and the advantages and disadvantages of each area.

In addition to background, most of these sections also contain listings of potential business contacts, which serve as excellent sources for locating Chinese investment or manufacturing partners. The contacts range from local foreign trade and Bank of China offices to Chinese enterprises, which tend to be diversified local trade and investment companies. Sections on export processing and the Canton Trade Fair will give companies a clear overview of the main types of commercial activities in the province besides agriculture, e.g., foreign trade and small light industrial manufacturing. The chapters on Guangzhou and Shenzhen also list hotels and guesthouses, and there is a short section on Guangzhou restaurants.

Chapter 9 contains six descriptions of foreign operations in Guangdong, termed "case studies,"though they are short on the kind of analysis that a truly useful case study contains. The descriptions of projects do not ignore problems, but they would probably not give a first-time China investor a realistic sense of the processes, time, and difficulties involved in setting up a viable venture (the chapter also describes the operations of three Chinese companies in Guangdong). The appendices listing forms of investment, procedures, and relevant Chinese legislation also represent more of a starting point than a comprehensive guide to investing. After reading the book, a newcomer to China might take for granted more than a prudent investor should.

Brief but thorough, the book is packed with good information that is generally well organized under subheadings within chapters. The lack of an index keeps the reader flipping back and forth between the table of contents and the chapters, though. Maps of Guangzhou and Shenzhen would also be useful to orient first-time visitors.

Perhaps the book's most helpful point is that much business in Guangdong can be successfully negotiated and managed from Hong Kong. The second part of chapter 1 describes advantages of using Hong Kong as a base and includes a list of advisory organizations for foreign businesses as well as the local offices of Guangdong enterprises. This information will help companies thoroughly explore the China option before crossing the border. —SER

China Business Strategies: A Survey of Foreign Business Activity in the PRC, by Nigel Campbell and Peter Adlington. New York: Pergamon Press, 1988. 252 pp. $250 hardcover.

This book is the product of a survey carried out by the University of Manchester Business School in the spring of 1988. Some 400 foreign companies with representative offices in China completed an extensive questionnaire covering such areas as perceptions of the Chinese leadership and the China market, costs of doing business in China, and future plans. Several supporting chapters were contributed by academics and businesspeople.

The book is divided into three sections, the first of which, "China and the China Market," is a concise introduction to China's economic reforms and the different types of foreign trade and investment conducted there. This part is clearly aimed at the newcomer to China business. Part II, "Doing Business in China," is based on the results of the survey, examining responses to some questions in more detail. Part III, "Succeeding in China," identifies key planning issues and includes brief case studies to illustrate successful and unsuccessful China strategies.

The survey is by far the most interesting and distinctive part of the book. Responses are tallied both by nationality—Japanese, European, and American—and by sector—manufacturing, trading, and services. Even though some answers would undoubtedly be different now, in the aftermath of Tiananmen, noting similarities and discrepancies among the responses of the various nationalities and sectors makes for thought-provoking reading. For example, an overwhelming majority of all three national groups believed that the Chinese view companies as resources rather than as partners. Interestingly, however much higher percentages of Americans and Europeans responded that China's top leaders are sincere in trying to improve conditions for foreign business and that incentives have improved steadily. Sixty-four percent of the American respondents reported that their company's China activities were running at a profit, compared to just 42 percent of the Europeans and 30 percent of the Japanese. Americans were also far more satisfied with the level of support extended by their parent companies than were the Japanese, with 51 percent of Americans responding support was good compared to only 7 percent of the Japanese. The survey appears complete with tabulated responses at the end of the book.

Campbell and Adlington use the results of the survey to discuss important strategic considerations for potential traders, manufacturers, and service companies, and introduce brief case histories to support their points. But the brief analysis leaves the reader starved for details, especially in the case studies. This is the book's major flaw—though clearly written and highly readable with valuable basic information, it merely scratches the surface of most issues and is bound to disappoint readers who seek a more probing analysis.

Nevertheless, *China Business Strategies* serves as a good all-around guide to the China market, and provides a solid base of knowledge to build on.

—PB

Taxation of Foreign Investment in the People's Republic of China, by A.J. Easson and Li Jinyan. Deventer: Kluwer Law and Taxation Publishers, 1989. 242 pp. $99 hardcover.

When China embarked upon its open-door policy a decade ago, the tax regime was one of the earliest targets of reform. This book provides a straightforward look at the tax laws that China has since adopted and how these laws apply to foreign investment.

After an introduction to the various types of foreign investment, the book offers a brief overview of the Chinese tax system both before and after economic reform. The core of the book, chapters 3-5, explains in detail how the individual income tax, the joint venture income tax, and the foreign enterprise income tax are applied. Chapter 6 describes other taxes that may also apply to foreign investment; the industrial and commercial tax, customs duties, local taxes, and land-use fees.

The slightly confusing nature of some of the explanations, such as that of the residence requirement, derives from the ambiguity of the tax law as well as to the fact that local tax bureaus are granted some latitude in interpreting the law. The text is well referenced to the applicable tax law articles, and the main tax laws are included in the appendices. As the book points out repeatedly, some laws are superseded by special investment incentives and tax treaties, which are described in greater detail in the last two chapters.

This book may not answer all questions about Chinese taxes, and the reader should keep in mind that the tax structure is still evolving and changes will occur. However, this readable book, with its detailed table of contents, is a handy reference guide for a general understanding of China's tax system. —Joel Greene

Communist Neo-Traditionalism: Work and Authority in Chinese Industry, by Andrew G. Walder. Berkeley and Los Angeles, CA: University of California Press, 1986. 302 pp. $42.50 hardcover, $11.95 softcover.

Anyone who wants to understand the mechanics of political control in China must be familiar with authority relations in work organizations, the basic units of both political and economic life in China. This study, based on interviews with Chinese emigres, details the hierarchies, compensation and promotion plans, and ways of organizing production that characterized Chinese industrial enterprises through Mao Zedong's death and the first years of reform.

Walder's argument recasts the conventional view that authority relations in revolutionary China arose through the routinization of Mao's charismatic leadership. Instead, this study argues that Chinese communism's stress on "permanent revolution" developed distinct status groups of activists in work organizations who had separate privileges and responsibilities. Maoist policies rewarded purist ideology rather than production success or other accomplishments, so that through their revolutionary zeal, activist factions won favor with the leadership and gained access to power. Thus, by a circuitous route over high moral ground, political activists became clients of factory leaders' patronage, forming what Walder calls a neo-traditional authority structure.

Walder dismisses the old argument of "cultural survival" as an explanation for the neo-traditional pattern of authority. Although Confucian and other traditional philosophies of government inform contemporary politics, Walder argues that attitudes of submission to authority did not automatically carry over into modern industry, which was built virtually from scratch. Unlike industry in Western industrialized nations, which developed authority patterns based on those that characterized trade organizations, the division of labor and authority in China's industries was simply devised and imposed by government fiat.

The most interesting part of this book lies in a subtext beneath the description of work in China. Walder's secondary theme, not fully articulated, reveals how China's leadership has been able to mobilize the people for back-to-back political movements over three decades, commanding widespread complicity in the government's darkest campaigns. He describes how workers' ill will focused on the activists within a work organization who informed on them and seemed to curry favor with the leadership, while the activists saw themselves as bound to a higher code of values. Walder describes how the growth of a new client class of activists divided work organizations down to the mailroom and switchboard, creating ready-made factions with personal agendas that complemented the political campaigns of the national leadership. He also shows how the persistence of "back-door" routes to advantage and of outright bribery reinforced individual rather than collective methods of promoting group interests.

Walder's study suffers from a few organizational weaknesses. However, it is a fascinating and readable contribution to Chinese industrial sociology. —ASY

China's New-Look Leadership

Some new faces in new places—but the power remains with Deng

The aftermath of Tiananmen has seen a shuffling of China's top party leadership, as former Chinese Communist Party (CCP) General Secretary Zhao Ziyang was summarily replaced by Jiang Zemin, and Deng loyalists were elevated. New members appointed to an expanded, six-member Politburo Standing Committee—the inner sanctum of political power in China—are Jiang, Song Ping, and Li Ruihuan, who join Qiao Shi, Yao Yilin, and Li Peng. Li Ruihuan and Ding Guanggen replaced Zhao associates Hu Qili, Rui Xingwen, and Yan Mingfu on the Standing Committee of the Secretariat, which handles the CCP's day-to-day work.

The new appointees appear to represent a careful balance of political factions, with Li Ruihuan representing the reform faction, Song Ping standing in for the conservatives, and Jiang Zemin representing the moderate, centrist faction. That such a prominent reformer as Li Ruihuan remains in the leadership suggests that Deng Xiaoping wants to maintain at least an appearance of continuing openness and economic change.

Nevertheless, the very evenhandedness of the appointments highlights their fundamental hollowness. The new Politburo members have clearly been chosen first and foremost for their willingness to obey orders from those who retain real power: Deng Xiaoping and the elderly, first-generation leaders around him. Chief among Deng's contemporary allies is Yang Shangkun, president of China and vice chairman, under Deng, of the Party and State central military commissions. Yang, 82, a conservative Long March-veteran, remains a vigorous champion of tight central political control, and is one of the most influential members of the Central Committee.

In the past, Deng has often proven himself a masterful political puppeteer, arranging factions and alliances from behind the scenes to buttress his own power. It appears that the June appointments represent merely another such manipulation, rather than a fundamental change in the leadership—which may come about only when Deng passes from the scene. —Anne Stevenson-Yang

NEW MEMBERS OF THE POLITBURO STANDING COMMITTEE

Jiang Zemin

As Shanghai Party general secretary during the pro-democracy demonstrations last spring, Jiang, 63, fired Qin Benli, editor of the outspoken journal *World Economic Herald*, for his support of the movement's ideals and then closed the newspaper. Those acts of political compliance marked Jiang, who speaks English, Russian, and Rumanian and has a pro-business reputation, as precisely the breed of official Beijing's top leadership was seeking: a supporter of economic reform who would not rock the political boat, and thus an appropriate choice to succeed the controversial Zhao Ziyang.

Jiang is the adopted son of a "revolutionary martyr" from Yangzhou, Jiangsu Province. He graduated from Shanghai's Jiaotong University, where he majored in electrical engineering. After training in the automotive industry in the Soviet Union—where he also served as a commercial counselor in the Chinese embassy—Jiang held various positions in automotive, machine-building, and electronics concerns before becoming director of the Foreign Affairs Bureau at the First Ministry of Machine Building. In 1981 he became vice minister of the State Foreign Investment Commission, and in 1982 he was appointed vice minister of the Ministry of Electronics Industry. That year he was also elected to the Central Committee. In July 1985 he became general secretary of Shanghai, in which position he earned the support of much of Shanghai's foreign business community.

Li Ruihuan

Also a member of the Secretariat, Li, 54, is known as a promoter of economic but not political reform. As mayor of Tianjin, one of China's three major cities that come directly under central government control, Li earned a reputation for efficiency and innovation in promoting urban renewal projects, improvements to the public transport system, and increased foreign investment in the city's economic development zone. His reputation is somewhat tarnished in China, however, by unconfirmed rumors that family members have profited from Tianjin's ambitious construction schemes.

Li, who has little formal education and speaks no English, began working in the construction industry at age 16, and went on to manage the construction of the Great Hall of the People in the 1950s. He is a close associate and probably son-in-law of the reformer Wan Li. He is reportedly in charge of propaganda.

Song Ping

Song, 72, is an experienced advocate and practitioner of centralized economic planning. He is reported to be a close political ally of Chen Yun, a conservative elder who framed much of post-1949 China's economic strategy, and to Chen's disciple Yao Yilin. As a new member of the Standing

Committee, Song will have the sensitive task of leading investigations into high-level corruption.

Song held Party educational and propaganda positions before 1949 and was political secretary to the late Premier Zhou Enlai. In 1952 Song went to Beijing to work with the State Planning Commission (SPC), where he rose to become vice chairman. After 1972 he held high political positions in the Lanzhou and Gansu military command areas, and in 1981 returned to Beijing as executive vice chairman of the SPC under Yao Yilin. He succeeded Yao as SPC chairman in 1983.

NEW MEMBER OF THE SECRETARIAT STANDING COMMITTEE

Ding Guanggen

Ding, 59, is the former minister of Railways who stepped down in March 1988 following a series of bad railway accidents. A close associate and bridge partner of Deng Xiaoping, Ding was named vice minister of the SPC in September 1988. Deng supported Ding for the SPC post over objections that he lacks sufficient background in economics. Ding also directs the State Council's Taiwan Affairs Office.

Ding and Li Ruihuan, the two new appointees to the Secretariat, replace Yan Mingfu and Rui Xingwen who, with Hu Qili, were responsible for the Party propaganda apparatus before the Tiananmen incident.

Born in Wuxi, Ding graduated from the transport department of Jiaotong University and worked for much of his career as an engineer in the Ministry of Railways.

NEW MINISTERS

Gu Xiulian, Chemical Industry

In 1983 Gu became China's first female governor, of Jiangsu Province, concurrently serving as deputy secretary of the Jiangsu Communist Party. Born into a peasant family in Jiangsu in 1935, Gu graduated from a technical college and worked as a technician and teacher in northwest China until 1970, when she became a State Council cadre and later vice minister of the SPC for textiles and light industry. In 1977 she became an alternate member of the 11th Party Central Committee, and in 1979 she became vice chairman of a committee to inspect incoming goods and equipment. Gu replaced the retired Qin Zhongda.

Li Tieying, State Education Commission

A Politburo member, Li took over from Zhao Ziyang as chairman of the Committee on Restructuring the Economy in April 1987, until he was replaced by Li Peng after the 1987 meeting of the National People's Congress. Li's previous posts include minister of Electronics Industry and Party secretary of Liaoning Province.

Ruan Chongwu, Labor

Ruan, 52, was born in Hebei Province and studied automotive engineering for four years in Moscow. He worked in the automotive industry before the Cultural Revolution. During his tenure as minister of Public Security from 1985-87, Ruan was credited with improving the agency's image by cracking down on police brutality. He is also said to have exercised restraint in controlling the 1986 student demonstrations. After the fall of Hu Yaobang, Ruan was removed and replaced by Wang Fang, Zhejiang Party secretary. Ruan replaced Luo Gan, who reportedly retired. 完

Worst-Case Scenarios

After the events of June, it's time to review legal options

T.K. Chang and Rolf Olofsson

The military suppression of student demonstrations in June and the subsequent changes in China's political leadership have forced many foreign companies to examine, if only as a worst-case scenario, the legal implications of suspending or terminating their business involvement in China. Although few companies to date have actually been forced to abandon their operations, the continued unpredictability of political developments, the prospect of diminished profits, as well as the possibility of shareholder and customer opposition to continuing to do business in China all make it essential for companies to analyze all possible scenarios and options so as not to be caught off-guard.

Contract nonperformance

Immediately following the June 4 massacre in Tiananmen Square, many foreign businesspeople carrying out contracts in China were forced to leave for reasons of safety. The legal principle of *force majeure* (in Chinese, *bu ke kanli*), which excuses nonperformance of a contract due to forces beyond the control of the parties, is clearly recognized under Chinese law, specifically in article 24 of the 1986 Foreign Economic Contract Law, which governs contracts between foreign and Chinese entities; article 20 of the 1987 Technology Contract Law, which governs technology transfer contracts; and articles 107 and 153 of the 1986 General Principles of Civil Law, which set forth the general framework of Chinese legal principles.

Force majeure certification

Most Chinese contracts contain language defining the circumstances under which *force majeure* would apply. For example, the standard Chinese technology-transfer contract allows extended time for performance as a result of "war, serious fire, flood, typhoon, earthquake, or other occurrences recognized as *force majeure* by both parties." To obtain the extension, the party prevented from completing the contract must provide "a certificate issued by the relevant authorities for confirmation by the other party." To satisfy the certification requirement, one US company that withdrew its personnel in June obtained letters from both the Hong Kong General Chamber of Commerce and the Swedish Embassy in Beijing (the contract was governed by Swedish law). In June, the US-China Business Council in Washington, DC also provided a letter to US companies noting that companies were forced to withdraw their personnel from China by external events beyond their control, and expressing hope that they not be subject to penalties for their actions.

Similarly, the Chinese standard-form joint-venture contract requires certification of an event of *force majeure* by "the notary agency in the area where the event occurs." Notary offices in China, however, are governmental agencies under the Ministry of Justice, and may be reluctant to issue such certification.

Certification of a *force majeure* event has already been a key issue for certain foreign hotel-management companies, which receive higher fees under their management contracts if a *force majeure* event is certified to have occurred.

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Terminating contracts

While *force majeure* may be a tenable basis for temporarily suspending performance of a contract, it may be difficult to use it to justify complete termination, as Chinese legal principles are quite underdeveloped regarding the non-performance or rescinding of contracts based upon changed circumstances or impossibility. US companies participating in high technology joint ventures or technology transfer contracts in China, however, may have a strong claim for *force majeure* or impossibility because of the strict controls on technology exports imposed by the US government after the Tiananmen massacre.

Even without invoking *force majeure*, it may be possible for joint ventures to terminate a contract if the joint venture is unable to continue operating due to heavy losses, if one party fails to fulfill its obligations, or if the venture fails to achieve its business objectives and has no possibility of doing so. A joint venture may also be dissolved by agreement of both parties, or under any other circumstances specified in the joint-venture contract.

The fundamental stumbling block to dissolving a joint venture is that approval must be granted by the Ministry of Foreign Economic Relations and Trade (MOFERT) or by the local foreign economic relations and trade commission that originally approved the joint-venture contract. Even if the situation in China should further deteriorate, it is unlikely that the Chinese government would approve the wholesale dissolution of many joint ventures.

Foreign companies that have signed joint-venture contracts but have not yet contributed capital may try to walk away from projects. Presumably, the 1988 Provisions on Contribution to Equity Joint Ventures, which authorize the Chinese government to cancel joint-venture approvals under such circumstances, would take effect. It should be noted, however, that both the Joint Venture Law and the Joint Venture Implementing Regulations state that a joint-venture party that fails to fulfill its obligations will be "liable to the joint venture for the losses caused thereby."

These provisions raise the disquieting possibility that Chinese courts may attempt to seek additional damages from the foreign parent corporation of the subsidiary that invested in the joint venture, although it is uncertain whether such judgements of Chinese courts would be enforceable outside China. Perhaps the most grave concern for foreign companies contemplating pulling out of China is that they must do so in such a way as not to damage their business reputation in China or foreclose the opportunity to reenter the market in the future, when circumstances improve.

A foreign company that has already made partial or total contribution to capital faces the most difficult dilemma. It would not be able to recover its capital contribution and retained earnings unless the dissolution is approved by the Chinese government, which would probably exert pressure in order to prevent a committed foreign investor from leaving China.

Of course, foreign companies may be able to take advantage of the current climate to gain concessions. Some companies have recently reported that negotiations which had been stalled for many months were suddenly revived by fresh concessions from the Chinese. Companies that do not really intend to pull out might nevertheless find it useful to analyze the grounds for dissolution—and to share that analysis with the Chinese partner.

Stockholm arbitration

Further down the road, issues relating to *force majeure*, contract termination, and joint-venture dissolution will inevitably generate disputes between Chinese and foreign parties, and thus companies should scrutinize the arbitration provisions in their contracts. Most Chinese contracts call for compulsory arbitration, and although Chinese standard form contracts still call for arbitration in Beijing under the auspices of the Chinese International Economic and Trade Arbitration Committee (as the Foreign Economic and Trade Arbitration Commission was renamed in January 1989), Chinese negotiators after some obligatory negotiations have usually agreed to arbitration in a third country, most often in Sweden before the Arbitration Institute of the Stockholm Chamber of Commerce (*see* box).

Perhaps the most grave concern for foreign companies contemplating pulling out of China is that they must do so in such a way as not to damage their business reputation in China or foreclose the opportunity to reenter the market in the future, when circumstances improve.

Last resort: bankruptcy

China does not currently have a law governing the bankruptcy of foreign joint ventures. The final version of the State Enterprise Bankruptcy Law, which went into trial implementation on November 1 1988, applies only to Chinese State enterprises. Nevertheless, failing joint ventures could try to argue that this law should apply to them by analogy. The law provides a maximum two-year reorganization period, during which the debtor and creditors try to work out a plan allowing the enterprise to continue to operate.

Of course, unlike Chinese State enterprises, whose losses are subsidized by the government, joint ventures are independent economic entities which do not need a bankruptcy law to go bankrupt. If a joint venture cannot repay its debts and has no hope of doing so, it will simply go out of business or be taken over by its creditors. The question then becomes: Will the principles of limited liability under Chinese law protect the foreign investor? Conversely, can lenders to the bankrupt joint venture force the Chinese government department in charge of the Chinese party to pay the debts in its stead? Given the uncertainty of the rights of debtors and creditors under Chinese law, it may be risky for a foreign company to trust its fortunes to the whims of a Chinese court of bankruptcy.

Hotels: prime battleground

While many foreign businesspeople have now returned to China, it is unlikely that tourists will soon return in the large numbers previously anticipated by the many hotel joint ventures in China (*see* p. 36). The steep drop in both the tourist and expatriate business population could not have come at a worse time. Thousands of hotel rooms, apartments, and offices will flood the markets in major cities next year, particularly in Beijing, and the long-predicted glut will now be exacerbated by the effects of martial law. The coming year will see many bitter disputes, even litigation in Chinese courts, between joint-venture real estate projects and their tenants, who will try to break their leases on the basis of *force majeure*, changed circumstances, and other defenses.

Unlike manufacturing joint ventures, many joint-venture real estate projects in China, premised on short payback periods, are highly leveraged. It will be only a matter of months before many projects will be unable to make their debt payments. Japanese banks, which have over $6 billion in exposure on Chinese projects (compared with less than $1 billion for US banks), mostly in joint-venture hotels and foreign housing projects, have already been warned by the Bank of Japan to reassess their China commitments.

The likely solution to short-term payment problems of real estate joint ventures in China—assuming that tourism recovers with the 1990 Asian Games in Beijing—is that lenders to the joint ventures will agree to extend the payment period, in return for higher interest rates, equity participation, or other improved terms. The lenders should try to involve the Chinese government in the negotiations in order to demand better terms for the joint ventures themselves. For example, the term of joint ventures, usually limited to 8-14 years for hotels, could be extended to allow for a longer period to generate revenues.

Overcommitted guarantors

Real estate investors will not be the only ones caught short—Chinese guarantor agencies will also feel immediate aftershocks from the real estate crisis. Because China has no national mortgage laws, foreign lenders to joint ventures have demanded guarantees from the Bank of China and other quasi-governmental agencies, such as China International Trust and Investment Corp. (CITIC), as well as provincial or local trust and investment corporations. Despite tight limitations on the total loans Chinese agencies can guarantee—the official ceiling is 20 times the entity's foreign-exchange fund—due to the lack of alternative sources, many guarantees in excess of the ceiling have been issued for joint-venture loans.

In the few past instances of defaulting borrowers, Chinese guarantors have generally honored their guarantee obligations. In February

US-CHINA ARBITRATIONS IN STOCKHOLM

As of July 1989, seven arbitration cases involving Chinese and US parties had reportedly been initiated before the Arbitration Institute of the Stockholm Chamber of Commerce. The only case to have reached a final award without being settled or withdrawn was won by the Chinese party. In that case, decided in December 1988, the arbitral tribunal ruled against Senitron, an Arizona-based electronics firm, which had initiated arbitration in October 1986 against the China National Machinery and Equipment Import/Export Corp. (MACHIMPEX) Not only did the ruling stipulate that Senitron could not collect over $1 million in nonpayment for a sale of equipment, but it reportedly also awarded damages—including $120,000 in attorney's fees—to MACHIMPEX.

It is popularly believed that Chinese parties prefer to resolve disputes through friendly consultation or conciliation, and are reluctant to resort to arbitration, particularly outside China. In fact, however, several of the cases arbitrated in Stockholm involving US and Chinese companies were initiated by Chinese parties, and a Chinese party's win in the only case decided to date may encourage the trend.

Unless the parties specify otherwise, the arbitral tribunal is composed of three arbitrators—one chosen by each of the two parties involved, and the tribunal chairman, who is appointed by the Stockholm Arbitration Institute and is usually a Swedish lawyer. In general, Chinese parties have preferred to be represented by Swedish lawyers in Stockholm arbitration, although they have appointed arbitrators of various nationalities, including one American lawyer. In the cases so far disposed, the proceedings have been conducted in English, sometimes with interpretation into Chinese for witness examinations.

Streamlined procedures

Arbitrations in Stockholm are comparatively speedy. According to the rules of the Arbitration Institute, awards must be granted within one year from the date on which the case is referred to the arbitral tribunal, which has generally held true. One reason for the relative speed of Stockholm arbitrations is that unlike U.S. courts, the rules do not authorize extensive powers of discovery—that is, the power to compel parties to procure documents, answer interrogatories, and submit to depositions prior to trial. Nor does the concept of discovery find any support under the Swedish Arbitration Act or the Swedish Procedural Code. A court order for producing documents may be obtained only if the document has been properly specified and it is clear that the document could be used as evidence. Even then, if the document is considered a business secret, the holder of the document may be entitled to refuse disclosure under certain circumstances.

Compared to US litigation, the Stockholm rules concerning admissability of evidence are much less strict. The arbitral tribunal is expected, however, to identify in its judgement each of the factors evaluated and found relevant to its ultimate determination.

Loser pays

As the Senitron case demonstrates, the losing party is usually ordered to pay not only all costs of the arbitral tribunal and the Arbitration Institute, but also the legal costs of the winning party. Thus, the expense of arbitration in Stockholm may not always deter a Chinese party from initiating arbitration if it believes it can win. Accordingly, despite the admitted Chinese preference for negotiation and conciliation, US companies should examine carefully their position under contract and under applicable law before embarking on any course of action that may force the Chinese to initiate arbitration.

Swedish legal principles

Foreign companies in China may find that in certain situations, principles of Swedish law will apply to their contracts. For example, under article 145 of China's 1986 General Principles of Civil Law, the parties to most types of Sino-foreign contracts (other than joint venture and oil exploration contracts) may designate the law of a foreign country as the governing law, and Swedish law is often designated. Also, a Swedish arbitrator or tribunal chairman is most likely to have been trained in Swedish law.

Although many principles of Swedish law applicable to the current situation in China, such as *force majeure* and impossibility, are similar to American legal principles, Swedish law also embodies concepts that may not be familiar to most American lawyers and businesspeople. For example, under the doctrine of underlying assumptions (*förutsättningsläran*), if parties enter a contract based on significant and mutually understood factual conditions, and if these conditions no longer exist, the arbitral tribunal can decide to terminate or modify the contract.

Similarly, under Section 36 of the Swedish Contracts Act, a contract term may be set aside or modified if it is found to be unfair in light of changed circumstances. (This legislation originated as a consumer protection statute, and its application to transactions between businesses may be limited to cases in which one party at the time of the making of the contract held a dependent or inferior position and subsequent circumstances make it unreasonable to require enforcement of the original contract.)

The legal doctrine of limitation of sacrifice (*läran om offergränsen*) may also apply, by allowing for modification or nullification of the contract if its fulfillment would entail unreasonable demands or sacrifice.—TKC, RO

1989, for example, the Guangxi International Trust and Investment Corp. repaid as guarantor a $14.5 million loan for the Guilin Garden Hotel.

If significant numbers of guarantees were called upon, however, it is unclear whether the many undercapitalized guarantors would be able to repay the often enormous debts that they have guaranteed. And if the guarantors lack sufficient capital, would the guarantees enjoy the full faith and credit of the Chinese central government or the local government that originally approved the joint-venture contracts? Foreign bankers have been particularly concerned about the political fortunes of CITIC, which has guaranteed many foreign loans. CITIC employees and the CITIC Institute on the Research of International Problems played various visible roles in the prelude to the imposition of martial law, and certain top officers of CITIC are generally seen as allied with former Communist Party leader Zhao Ziyang.

Window of opportunity

Although the events of May and June should prompt prudent investors to examine all of the worst-case scenarios, the current environment is not entirely bleak—in China, the term for "crisis" encompasses both the concepts of danger and opportunity. The Chinese government may be so desperate to hold onto foreign investors that it will make unprecedented concessions to improve the business environment. As one top executive for a major Japanese trading company remarked, "Now may be the window of opportunity for doing business in China." According to the "contrarian" philosophy of investment, when all your competitors are leaving, that is precisely the time to enter and dominate the market. Were it not for moral and ethical concerns, this might be sound business advice. 完

Covering All the Bases

Political risk insurance no longer seems like "optional" coverage

Elizabeth Keck

In May, an American business executive investing in China for the first time confidently claimed that putting money there was as safe as investing in France—a view shared by many experienced China hands. Today, this executive's company has purchased political risk insurance for its China project to protect against expropriation and damage caused by the kind of civil unrest that unexpectedly confronted the foreign business community in China in May and June.

Like this first-time investor, many companies generally consider political risk insurance optional when structuring their insurance packages—but demand for it soars as soon as a country's political situation unravels. Following the June 4 Tiananmen Square crackdown, political risk insurers reported a surge in inquiries from companies trading and investing in China.

While coverage for China projects was hard to come by for several days after June 4, commercial underwriters began offering it again as the threat of civil strife subsided. The other segment of the political risk market—the non-commercial, government-backed insurers—have been more cautious about offering new coverage to China projects, so as not to fall out of step with their countries' policies toward China. Of the government agencies, it appears that only the US Overseas Private Investment Corp. (OPIC)—the second-largest government-backed insurer in China with $100 million total coverage on 29 projects—will be barred by Congress from issuing new coverage for China investments. The US Foreign Credit Insurance Association (FCIA), which insures nonpayment of letters of credit, is still issuing China coverage and is not affected by congressional sanctions.

Even with OPIC temporarily out of the picture, however, US companies seeking coverage in China today should compare the offerings of both commercial and government providers. Coverage availability often varies, and coverage for China projects can sometimes be obtained from another country's government-backed provider, if the US company has a subsidiary incorporated in the insurer's country.

Two types of coverage

Political risk policies are usually tailored to specific transactions, and can be divided into two categories: those that cover investments and those that cover trade. Contract frustration and letter of credit insurance, for example, are primarily purchased for trade and short-term contract obligations when a company is concerned about government interference in a contract or payment of a letter of credit. A company making a capital-intensive investment with a long period before payback will want longer-term coverage for such risks as expropriation, political violence, or currency inconvertibility (*see* chart). The extent of a company's experience and exposure in China and comfort level with Chinese partners may also influence selection of a political risk policy.

Choosing a provider

Major commercial providers of political risk insurance for trade and investments include the American International Group Inc. (AIG), the Chubb Group, Lloyd's of London, and Citicorp International Trade Indemnity (CITI), which focuses primarily on trade insurance.

Commercial providers can cover companies of any nationality and any existing investment. Because private insurers also offer standard property and casualty coverage, they may give favorable terms for coverage packages combining political and commercial risk protection.

For investment, private insurers will commonly cover the risks of civil strife and expropriation, while only the government-backed insurers will offer the additional political violence coverage for war, revolution, and insurrection. Also, government investment insurers are willing to offer long-term coverage commensurate with the long-term risk exposure most investment decisions entail. OPIC, for example, provides coverage for 20 years, compared with the maximum three-year commitment of a private insurer.

For trade transactions, insurers of letters of credit may have underwriting restrictions. FCIA, for example, prefers to see the Bank of China as guarantor, while some private insurers, such as CITI, may consider others.

A company should also explore a carrier's subrogation practices for expropriation claims. Some insurers require a company to assign expropriated assets to them before paying a claim. In China, where joint ventures have restrictive assignment provisions, it may require special arrangements to transfer assets to insurers.

Government clout and constraints

One advantage of a government-backed insurer is that it carries the clout of the government behind it: A foreign government may be deterred from expropriating assets by the

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prospect of dealing with the insurer's government in the event a claim is made.

Despite the advantages they offer, government-backed insurers may be prevented by political constraints from providing adequate coverage in every instance. For example, most will cover only companies domiciled in that country. Some face additional policy constraints: OPIC, for example, has a mandate to provide an incentive for foreign investment, so it can offer coverage only on new investments. OPIC must also consider how each overseas investment it is asked to insure will affect the US economy and employment.

Moreover, the coverage provided by government insurers may be a matter of public record and disclosed to the foreign government. For example, once OPIC insures a project or pays a claim, the existence of insurance or paid claim information is a matter of public record, in contrast with private insurers, who keep confidential their records of insurance coverage and claim payments.

Along with some other government-insurers, OPIC has bilateral agreements with foreign governments that allow the governments to approve the issuance of OPIC coverage to an investment project. In China, the project approval granted by the Ministry of Foreign Economic Relations and Trade (MOFERT) has generally been accepted by the Chinese government as approval for issuance of OPIC insurance, making OPIC approval virtually automatic. More complex foreign government approval procedures can, however, delay issuance of coverage.

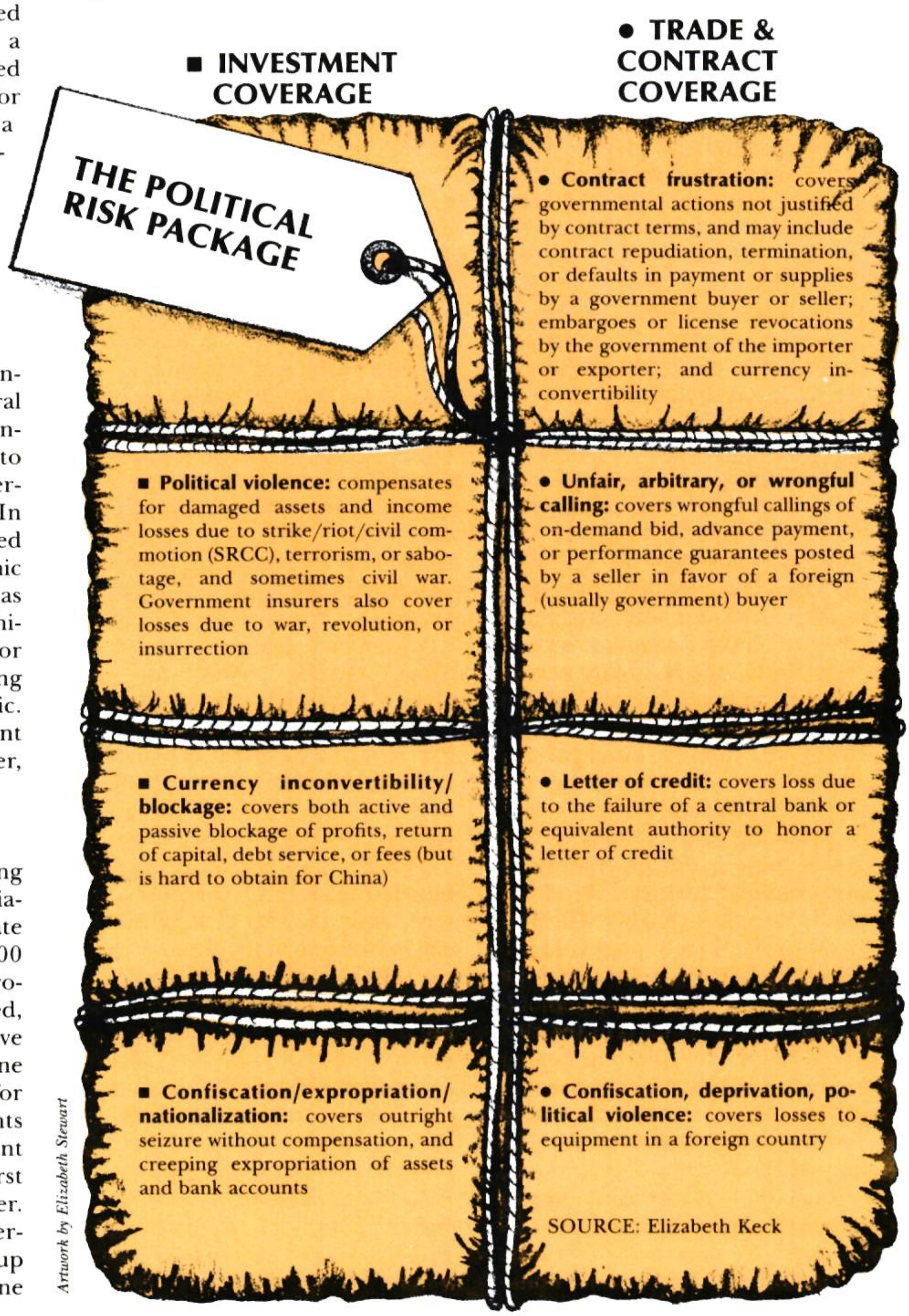
Rates rise with risk

Before June 4, companies insuring China investments against expropriation risks received rates from private carriers as low as 30 cents per $100 of insured investment. Now, expropriation rates have at least doubled, and first-time insurers may also have to pay more. After June 4, one private insurer offered a rate for expropriation coverage of 75 cents per $100, with an additional 75-cent surcharge per $100 during the first six months for a first-time buyer. Rates from CITI and AIG for coverage of letters of credit are also up about 30 percent from the pre-June 4 period. FCIA reported that its country rating of China has not substantially changed and that rates are about the same. However, FCIA is only extending coverage to the most secure transactions: those involving Bank of China letters of credit.

Back to basics

Companies seeking coverage for China projects can generally expect to find underwriters now placing more emphasis on the quality of the transaction, examining such aspects as financing, size, track record of the Chinese partner, and general economic viability. Companies with long experience and solid contacts in China will be preferred over newcomers, and shorter-term exposures will garner more favorable rates, as will ventures that Chinese officials are keen to support, such as export-oriented investments that bring in foreign exchange. Companies bringing repeat business to insurers will also have a better chance of securing coverage at favorable rates.

Ultimately, the availability of coverage may be determined by events beyond the control of companies. Underwriters are carefully monitoring the political situation in China. The political risk insurance market could again dry up, if the situation in China takes a turn for the worse. 完



Artwork by Elizabeth Stewart

Echoes from Tiananmen

As 1997 approaches, Hong Kong grows more sensitive to events across the border

Jamie P. Horsley

Hong Kong shared with the rest of the world the deep-felt shock, horror, and outrage at China's crackdown on dissent. In the aftermath of the Tiananmen Square massacre on June 4, Hong Kong restaurants were deserted, stock prices tumbled, and many companies put deals on hold. Three months later, the territory is slowly gearing up again, but uncertainty and caution continue to affect the economic, political, and social scene. It may be years before we can fully assess the impact of the events in China on Hong Kong and its future.

Political awakening

Hong Kong people watched with growing excitement and admiration the development of the student pro-democracy movement. In response to the Chinese government's declaration of martial law and attempted crackdown on the student movement on May 19-20, nearly 40,000 people defied the wind and rain of Typhoon Brenda on May 20 to rally in protest in front of China's quasi-governmental presence in Hong Kong, the New China (*Xinhua*) News Agency. The following day witnessed the largest political demonstration in Hong Kong's history. At least 500,000 people—roughly 10 percent of Hong Kong's population—marched peacefully through the street for almost 12 hours, immobilizing traffic in many parts of the city.

A week later, as tensions in Beijing mounted, Hong Kong staged a 12-hour pop concert on May 27, raising an estimated $1.5 million for the Beijing demonstrators. The next day, over 1 million Hong Kongers took to the streets again, the marchers accompanied by caravans of trucks, taxis, and other motor vehicles honking their support and sporting slogan-bearing banners.

The unprecedented outpouring of public sentiment was prompted partly by enthusiasm over prospects of increased democracy in China and partly by the growing perception that Hong Kong's fate—both political and economic—is increasingly tied to China's as the territory moves closer to 1997, when China will resume control.

The bloody crackdown of June 3-4 and its aftermath chilled Hong Kong to the core. Some 20,000 donned black or white as a sign of mourning and turned out for rallies and demonstrations on "Black Sunday," and much of Hong Kong supported a one-day strike of non-essential businesses on June 7 as an expression of mourning. However, organizers could not stir the same degree of public outrage and pro-democracy support in the wake of the Tiananmen massacre they had evoked on the previous two weekends. As the optimism that China might truly change and become more like Hong Kong itself was shattered and replaced with a general feeling of hopelessness, Hong Kong was stunned into relative immobility.

The Chinese government's cold-blooded murder of peacefully demonstrating citizens, its subsequent gall in insisting to the Chinese nation and the world that what had been witnessed by millions of people had not actually happened, and its condemnations and threats directed against Hong Kong's support of the pro-democracy movement in China irreparably destroyed Beijing's credibility in its dealings with Hong Kong—especially with respect to its promises for Hong Kong's post-1997 future. Calls for an accelerated timetable for the democratization of Hong Kong prior to 1997, and for increased safeguards of autonomy and freedom in the Basic Law that will govern post-1997 Hong Kong have now received support even from conservative local businesspeople who formerly asserted that Hong Kong was not ready for democracy, as well as from the British government itself. Lobbying has increased for Britain to grant Hong Kong's 3.25 million British nationals the right of abode in Britain, with Britain protesting its inability to absorb so many immigrants and appealing to other countries to formulate an "international solution" to Hong Kong's crisis of confidence. Hong Kong's people have been jolted into heightened political consciousness, and it will be difficult, if not impossible, for Beijing to lull them back into relative complacency about the future.

Voting with their feet

Perhaps the most visible expressions of Hong Kong's shattered confidence are the lines of visa-seekers that have increased exponentially since June 4 outside of Hong Kong's foreign consulates. Even many Hong Kong people who formerly placed some trust in the guarantees of the 1984 Sino-British Joint Declaration, the Basic Law, and China's own self-interest in maintaining Hong Kong's economic prosperity and political stability have succumbed to desperation at the prospect of living under China's rule. An estimated 45,000 people, and perhaps more, emigrated from Hong Kong in 1988. The numbers leaving

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in 1989 will depend on how many Hong Kong emigrants foreign countries are willing to absorb—but are predicted to rise to 50-60,000 annually over the next few years.

The economic impact

Local economists predict that an unexpected slowdown in the economy during the last half of 1989 will hold economic growth below the Hong Kong government's original 6 percent projection, primarily as a result of the Chinese political turmoil. Jack So, executive director of Hong Kong's Trade Development Council, predicts, for example, a growth rate of 5 percent for 1989, while a study published in late July by the Political and Economic Risk Consultancy forecasts overall growth of 4.5 percent. Most agree that it is still too soon after June 4 to make any accurate projection of the overall economic picture, but some initial trends can be examined in light of a variety of indicators:

▶ **Risk analysis.** The Political and Economic Risk Consultancy Survey, prepared every three months, reported a dramatic increase since June in risks associated with doing business in Hong Kong, attributable more to social and political than economic factors. The survey, which ranks risks on a 1-10 scale, reflects a jump in the risk of social instability from less than four to seven, and a tripling of risks associated with the possibility of political change, from two to six. More moderate risks associated with foreign investment and export credits were also measured, although those associated with revaluation of the Hong Kong dollar and foreign debt repayments remain low. The report concludes that Hong Kong's long-term future will depend on stability in China and a continuation of its open policy.

▶ **Property prices.** The plunging of confidence in China has also affected the prices and prospects for Hong Kong's volatile property market, considered the main indicator of business confidence since the early 1980s, when Britain began publicly discussing the return of Hong Kong to China. While the market for office space remains strong, with continued demand for central locations and a prime office vacancy rate of only 1 percent, rents have reportedly begun to weaken slightly, as some companies postpone moving into better or bigger space. In the first post-June 4 government land sale, which closed on July 21, local developers reportedly bid slightly less than the HK $3 billion (US $3.8 million) that analysts had expected for the centrally located site, resulting in a per square foot price some 33 percent lower than the previous sale of a similar site in January 1989.

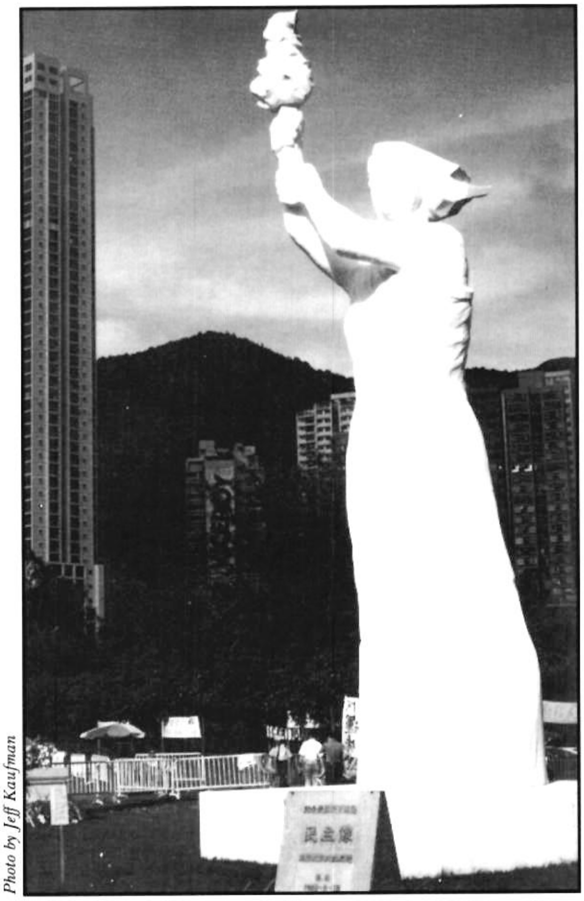

Photo by Jeff Kaufman

A "Goddess of Democracy" statue erected in Hong Kong commemorated the Beijing student demonstrations.

The price thus indicated that developers are not bullish on the market and do not expect demand for office space to increase between now and the date the building would be completed in 1992.

However, while the price was less than hoped for, it was not so low as to further dampen business confidence (or cause a plunge in stock prices). The property market had already slowed significantly since January due to fears that Hong Kong's economy was over-heating. Nevertheless, unless China can continue to attract new investment, lower office demand in Hong Kong for China-related business could add considerably to the general property slowdown.

The impact on the residential market has been more dramatic. Many families with mid- to upper-level incomes are shelving plans to upgrade living quarters or purchase a first home, instead saving their money to emigrate. Recent sales results indicate the market may have fallen more than the widely accepted figure of 25 percent since the Beijing troubles began. Rentals have reportedly begun to slide by some 10 percent, although they may rise in the short run due to increased demand from those who have decided not to buy.

▶ **Stock swings.** Hong Kong's stock market is known for swinging wildly along with political winds from China. Following the May 20 imposition of martial law in Beijing, the Hang Seng Index plunged from a 1989 high of 3,310 on May 15 by 339 points—or 14 percent—to roughly 2,800 on May 22. Although it staged a fragile recovery the following day, rebounding to a comfortable level back over 3,000 points, the June 4 events pushed the Index back down by some 600 points to approximately 2,049.

The results of the July 21 land sale further depressed the stock market—real estate holdings of local companies account for more than half of the stock market's total capitalization—although it did not prompt any panic selling. The Index has been gradually recovering, hovering around the 2,500 level throughout the month of July.

Together with the Index, price-earnings ratios fell below the historical average of the last 15 years of about 13.8 to roughly 8 immediately after the massacre, and to a more attractive level of 10 by mid-July. (The price-earnings, or P-E ratio, commonly used to measure a stock's value, compares a stock's price with earnings per share.) Although the P-E ratio has fallen below 10 during previous political and economic crises affecting China and Hong Kong, the mood on the financial markets has been decidedly glum since May.

▶ **Banking blues.** Prior to June 4,

Hong Kong-based and international bankers were already nervous because of China's late 1988 adoption of an austerity program to cool its over-heated economy, and because of the political upheaval that preceded the Beijing massacre. In the wake of the bloodshed, loans to several Hong Kong—as well as China—projects were suspended, and bankers are reportedly requesting that borrowers take out hard-to-obtain political and credit risk insurance for some of the deals going forward. Trade finance business may slow, as US purchases from Hong Kong have decreased and it is not yet known whether the drop-off is temporary or not. Several banks, including the Bank of China, reportedly cut by 20-30 percent their mortgage valuations of Hong Kong property. A run on the 13 Chinese-owned banks in the territory in the week following the Tiananmen Square massacre, causing an estimated 10-15 percent drop in deposits, was stopped within a couple of days by calls for restraint from the Hong Kong government and business leaders. While most of the funds were redeposited in other Hong Kong banks, some may have left the territory.

Bankers are taking a cautious approach to new financings in the territory, and because of the perceived increased risk in loans to Hong Kong, borrowers can expect to pay higher interest rates and be subject to even more onerous terms and conditions than those normally demanded, at least for some months.

In one example of the impact of recent events, Hopewell Holdings, a well-established Hong Kong firm with extensive business in China and the territory, was forced to cancel a massive $495 million rights issue on May 29, when some underwriters withdrew their support, sharing banks' reluctance to commit new funds to China even before June 4. Hopewell reportedly has had to halt construction since June 4 on its Shajiao "C" power station in the Shenzhen Special Economic Zone (SEZ) because of the failure of the rights issue and lack of willing financiers for the project. (However, Hopewell will go forward with a large hotel project in Hong Kong and construction of a power station in the Philippines.)

As a positive sign, the first rights issue to take place in the wake of China's political upheaval, by First Pacific Bancshares on July 21, was undersubscribed by only 12.9 percent. The shortfall was considered encouraging in view of the depressed state of the stock market, which has led other companies to call off or postpone planned rights issues after June 4.

▶ **Tourism troubles.** Hong Kong's hotel and tourism sector has suffered significant cancellations, primarily from tour groups heading into or out of China, as well as from businesspeople who cancelled trips to China. The industry has not been helped by international reports that Hong Kong itself was not a safe place to visit in the wake of relatively minor riots in Mongkok following June 4. Projections for the year's average occupancy rate in Hong Kong have fallen from above 90 percent to the mid-80s and as low as 75 percent. Some smaller hotels have reported occupancy rates as low as 40 percent in recent weeks. However, local hoteliers expect tourists to return in the fall and are planning advertising campaigns touting Hong Kong as a destination in itself rather than merely a gateway to China.

Hong Kong's people have been jolted into heightened political consciousness, and it will be difficult, if not impossible, for Beijing to lull them back into relative complacency about the future.

Hong Kong's fledgling airline, Dragon Air, which has been struggling against the well-established Cathay Pacific Airways, has been forced to reduce the number of flights to China just at the time it had hoped to expand its services, and it is being threatened with shareholder sellouts. Its passenger load reportedly has been halved since the start of the turmoil in China, and Dragon Air officials have reportedly stated that ticket sales are not expected to pick up substantially for another three months.

▶ **Sales slump.** Since June 4, large department and clothing stores have seen a 20-30 percent decline in retail sales, as Hong Kongers slow spending now to save against the future. While consumption of basic goods will remain strong, buying has fallen significantly for luxury and durable goods such as jewelry and household items. Automobile sales are plummeting, at least for new and luxury cars. Restaurants complain that people are staying away in droves—due either to little appetite for entertainment in the current climate or to the desire to save money to emigrate.

Reviewing investment

Paralleling the Hang Seng Index, Hong Kong industry's confidence both in China and the territory's future has dropped sharply. Prior to June 4, analysts and investors had generally assumed that Hong Kong would revert in 1997 to an economically and politically liberalized China anxious to preserve for at least 50 more years the territory's vitality and role as a conduit of Western capital and expertise. China's handling of the student movement demonstrated, however, that domestic power politics still prevail over economic interests and international considerations. Now investors are unwilling to look beyond 1997. And the worry is that foreign investors will tire of recurring volatility and uncertainty in Hong Kong and China and seek better value elsewhere.

Many foreign and local firms are reviewing investments in both places, more actively investigating opportunities elsewhere in Southeast Asia and the West—a trend toward diversification that has accelerated in the past year, as higher wages and rents force companies to relocate manufacturing operations. Others are looking for projects with shorter payback periods and are freezing or reducing staffing levels in the face of business slowdown.

According to a survey of some 85 industrialists conducted by the Hong Kong Federation of Industries, three-quarters of the respondents planned or considered emigrating after June 4, compared with 40 percent before that. Most of the Hong Kong businesspeople surveyed have investments in China of less than $1 million, most of which is in southern China, which was less affected by the turmoil than other regions. Their investments consist primarily of raw materials inventory for processing rather than plants or heavy equipment. About 70 percent of respondents with China-related projects stated that their operations were disrupted temporarily following June 4, primarily due to transportation and telecommunication problems. Others reported disruptions such as suspension of business talks and halts on order placements due to fears that China-sourced goods would not be able to meet delivery schedules. Still others, such as toy manufacturers, have reported receiving pressure from US and other customers to relocate China operations to avoid any future supply disruptions due to China's political and economic problems.

Nevertheless, all respondents reported that they intend to maintain existing China investments but are exploring ways to minimize their overall exposure by diversifying operations into other countries with relatively cheap labor, such as Thailand, the Philippines, Malaysia, Indonesia, India, and Vietnam, and seeking partners in China ventures to reduce their risk.

Companies based in Hong Kong generally withdrew foreign and Hong Kong staff from Beijing, Shanghai, and other troubled areas after June 4 but left all or a portion of their staff in the SEZs and southern China. While many of these personnel have now returned to China, others are reluctant to go back out of fears of danger or harrassment—or out of simple distaste. This reluctance also applies to technicians and salespeople who frequently travel to China while residing in Hong Kong. These concerns are exacerbated by the treatment some Hong Kongers have received from the Chinese authorities. For example, a Hong Kong political activist was detained for three days in Beijing for bringing funds raised in the territory to Chinese demonstrators. A Hong Kong student was arrested in Shanghai for his reported involvement in Shanghai's student movement and has been held virtually incommunicado, and a businessman from Hong Kong was imprisoned in Guangdong for putting up anti-government posters.

Facing the future

Many people question whether Hong Kong can retain its premier position as the headquarters for regional investment if the short-term decline in business with China continues and confidence in the territory's future cannot be fully restored. However, despite the uncertainties caused by China's turmoil, Hong Kong probably still remains the most attractive business center in Asia for the moment. Its relatively laissez-faire regulatory environment, low tax rates, amenities, and port facilities outweigh such factors as spiraling labor costs and labor shortages, high rents, and political uncertainty. Its proximity to southern China, which so far has been relatively buffered from the events shaking the rest of China and which boasts cheap labor and land, is still attractive to manufacturers and traders. Thus the territory is still viewed as a cost-effective operations center comparing favorably to South Korea and Taiwan.

China's handling of the student movement demonstrated that domestic power politics still prevail over economic interests and international considerations. The worry is that foreign investors will tire of recurring volatility and uncertainty in Hong Kong and China and seek better values elsewhere.

Very few foreign companies have physically relocated operations away from Hong Kong, although several large Hong Kong firms have reincorporated in Bermuda or Caribbean tax havens over the past couple of years and established offices elsewhere—a trend which undoubtedly will continue. When Union Carbide relocated its regional headquarters to Singapore in early 1989, it was feared that many more international organizations would follow, but this has not yet happened. Indeed, Dow Chemical Corp., which was rumored to be planning a similar move, reportedly signed in mid-July a 30-month lease for five floors of space and confirmed its intentions to retain its Pacific headquarters in the territory.

While the "brain drain" is a serious problem, some "recycling" of employees is already occurring—staff are sent abroad to obtain a foreign passport and return on expatriate terms, with housing and other allowances. This contributes to rising payrolls, but in turn these employees provide a measure of stability as well as expertise.

Nevertheless, one of the keys to Hong Kong's continued prosperity in the future may well be its ability to truly internationalize. Americans, Japanese, Australians, and businesspeople of other nationalities are moving into Hong Kong to replace the British who are slowly withdrawing. Their capital and expertise may become even more important to Hong Kong as more of its talented and educated people leave the territory, and the expatriates' presence will help ensure that other countries continue to take a keen interest in the fortunes of the territory leading up to and after the transfer of sovereignty to China in 1997. However, restrictions on obtaining work permits and enjoying the rights to land, residence in Hong Kong, practice of both law and medicine, and access to the local stock market will have to be eased. Hong Kong will have to curb racial and parochial tendencies underlying rights and hiring practices—which have understandably favored locals in recent times.

Hong Kong is blessed with many advantages, not the least of which is its resilient and adaptable populace. Since 1955, Hong Kong has weathered five recessions prompted by external events or economic misfortunes. Each time it has rebounded to greater heights of prosperity. The key to future success, of course, now lies outside Hong Kong's control. China must by its actions over the next months and years demonstrate to Hong Kong and to the world that it will honor its promises to preserve Hong Kong's political autonomy and laissez-faire economy. 完

The Military's New Muscle

A strengthened PLA emerges as the wild card in Chinese politics

Richard E. Gillespie

The suppression of the student movement at Tiananmen Square on June 4 greatly tarnished the image of China's military forces both at home and abroad. Yet during the weeks of unrest, the People's Liberation Army (PLA) saw its position in China's political hierarchy strengthened and its influence increased. Divisions in China's leadership brought the PLA to the fore as the most powerful source of support for the coalition of hard-liners surrounding Deng Xiaoping that regained political control. While the millitary does not appear to have exacted a high price for suppressing the prodemocracy movement—no money is currently available for reassignment to the defense sector—the armed forces could now emerge as kingmaker, if called into further service during the period of instability that will almost certainly last through Deng's passing.

As chairman of the central military commissions of both the Party and government, Deng is using the armed forces to maintain his preeminence within the current uneasy leadership coalition. Compounding his need of the military to quell potential unrest is his indebtedness for the PLA's undoubtedly reluctant participation in the bloody Tiananmen operation. In China's currently unstable atmosphere, a move by military leaders to seize political control cannot be ruled out, if they must again intervene in the leadership's power struggle. But in the immediate future military leaders, who presumably undertook the Tiananmen suppression out of loyalty to the Party and fear of political chaos, are unlikely to press for a direct role in governing China. Instead, they may promote other goals, including support for a strong central leadership with a tough stance against dissidence and corruption, backing for government recentralization programs to ensure better funding for defense programs, and greater emphasis on arms sales in support of foreign policy (*see* box p.29).

Deng's renewed dependence on the army is an ironic conclusion to a decade of military reform geared toward diminishing the PLA's role in politics. Military upgrading ranks lowest in priority of China's "four modernizations", and the PLA has seen its clout reduced, its ranks trimmed by 3 million since 1978, and its budgets reduced in the Deng era from 10 percent of GNP to 4 percent, according to CIA estimates. The PLA appears to care less about controlling China's politics than modernizing its forces. However, after a decade of restructuring, compounded by the replacement of many old, conservative PLA staff with younger, reform-minded professionals, the new PLA has developed several constituencies unfamiliar not only to foreign analysts but also to the elderly leadership in Beijing. Now the West must reassess its traditional view of China's military as a uniformly conservative force and try to identify groups within the armed services and defense industries that might promote reform and political opening.

Surrendering the 'people's war'

For a decade Deng has worked to shape a professional and depoliticized military equipped with modern weapons, supported by an upgraded defense industry, and armed with a new doctrine appropriate to China's current security needs. The armed forces have found it difficult to overcome the legacy of the Maoist "people's war" defensive doctrine against invasion, which focused on retreat to China's rural interior, enemy attrition, and final defeat of the invader with the support of spirited local forces and militias armed with conventional infantry weapons. In the 1960s China's "Third Line" of industries supporting national defense was built in remote areas deep in the interior to support this strategy. Maoist theory also gave to the PLA a role in China's political and economic development, principally in building civil and public works projects, which too often provided a rationale for PLA involvement in domestic politics.

A major shift away from Maoist military doctrine came with the disastrous setback sustained by the PLA in the 1979 Vietnam conflict—at least 20,000 men and half the air forces involved in the initial combat were lost—which underscored the urgency of developing new military doctrine and tactics, force structure, and military systems and equipment.

Building a professional, non-political military force equipped with modern weapons to fight with a revamped strategy called "people's war under modern conditions" thus became a key goal of the Deng leadership. Programs to upgrade the defense industries have called for applying idle production resources to civilian-sector needs, not to shift priorities to commercial production but to push toward more efficient use of the defense sector. In addition, the armed forces have been cautioned that military modernization can

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progress no faster than the civilian economy. Consequently, military spending as a percentage of national budgetary outlays has dropped steadily since 1979, from 17.5 percent in 1979 to 7.4 percent in 1989, according to official Chinese figures. China's officially reported military budget in 1989 is ¥24.55 billion ($6.6 billion), up 12.6 percent over the ¥21.796 billion spent in 1988, but down approximately 6 percent when adjusted for inflation. Such figures must be used with caution, however, even if only for identifying trends. Outlays for top-priority sectors, such as nuclear weapons, are classified, and foreign obervers believe China's military budget totals as much as three times the reported figure. Whatever the actual figures, it seems clear that defense spending has been politically restrained.

Pegging China's military modernization to the pace of the country's general economic expansion derives from China's belief that the Soviet Union constitutes a long-term rather than an immediate military threat, and that China is experiencing a period of relative invulnerability, allowing postponement of major spending programs until the economy has expanded and new military doctrine and force structure have been developed (*see The CBR*, March-April 1986, p.7).

US AND CHINESE MILITARY VISITS, 1985-89

1985

General John W. Vessey Jr., chairman of the Joint Chiefs of Staff, visits China with Commander-in-Chief, Pacific (CINCPAC) Admiral William J. Crowe.

1986

October: Defense Secretary Caspar Weinberger visits China.

General John Wickham, chief of Staff, visits China.

Chief of General Staff Yang Dezhi visits the United States.

1987

April: Chinese Air Force Commander Wang Hai tours the United States.

May: Central Military Commission Vice Chairman Yang Shangkun visits the United States with State Councillor Fang Yi; Zhu Qizhen, vice minister of Foreign Affairs and now ambassador to Washington; Xu Xin, deputy chief of staff of the PLA; and Ding Henggao, minister of NDSTIC.

September: Assistant Secretary of Defense for Production and Logistics Robert Costello and Air Force Secretary Edward Aldridge visit China, hosted by General Logistics Department Deputy Chief Zhao Nanqi.

October: Air Force Chief of Staff Charles Gabriel visits China.

1988

July: Commander of the US Army Training and Doctrine Command (TRADOC) General Maxwell Thurman visits China.

August: Chinese Vice Foreign Minister Zhu Qizhen meets in China with William Burns, director of the US Arms Control and Disarmament Agency.

September: Secretary of Defense Frank Carlucci visits China.

October: US Chief of Naval Operations Admiral A.H. Carlisle Trost visits China.

November: Zhu Guang, a lieutenant general and political commissar of China's Air Force heads a delegation to the United States.

1989

April: Air Force Chief of Staff Larry Welsh visits China.

May: Vice Admiral Henry E. Mauz Jr., commanding the US Seventh Fleet, visits the Port of Shanghai.

Canceled Visits:

June: Army Chief of Staff Carl Vuono

June: PLA Naval Commander Zhang Lianzhong

Compiled by Evan A. Feigenbaum

Removing the PLA from politics

Key to Deng's effort to professionalize the military has been a series of structural changes designed to lessen the PLA's role in politics, while making it more responsive to the central Party leadership. PLA leaders have been removed from Party and government posts at both central and local levels, while the PLA has been relieved of many nonmilitary functions. As its ranks were trimmed, the PLA's public-security functions were transferred to the People's Armed Police in order to downgrade the PLA's mandate to combat domestic dissent. The reforms reduced China's military regions from 11 to seven and transferred most regional commanders, restricting the political authority of their replacements. Party control over the military was strengthened by Deng's assumption of chairmanship of the government and Party military affairs commissions, his support from close colleague and Central Military Commission Vice Chairman Yang Shangkun, and by a network of loyalists in key defense posts. In addition, younger, better-trained professionals have assumed top posts in both Beijing and the military regions (*see* chart).

Too many chiefs

Competition among several key groups in the defense establishment has punctuated China's military modernization. Rivalry among the armed services makes it more difficult to determine operational requirements. Moreover, aims of the defense industries, intent on upgrading manufacturing facilities under their control for maximum possible economic gain, conflict with those of the armed services. Hampering the establishment of orderly lines of authority is the impotence of the Ministry of National Defense (MND), which actually has no operational control over the PLA. The Central Military Commission habitually bypasses MND—as in the Tiananmen operation—to issue orders directly to three MND subordinates, the General Staff, General Logistics, and General Political departments. MND's role in overseeing military modernization has also been usurped in practice by the National Defense, Science, Technology, and Industry Commission (NDSTIC), another ministerial level agency established in late 1982 to assist MND in providing a link between the PLA and defense industries. NDSTIC reports directly to the Central Military Commission, MND, and the State Council. The defense minister's participation in the Central Military Commission gives him a say in military operations, but he shares this authority with senior PLA leaders and the NDSTIC chairman. This helps explain why Minister of Defense Qin Jiwei, a Zhao Ziyang supporter who initially op-

Military Organizations of the People's Republic of China

Central Military Commission of the National People's Congress

Chairman	Deng Xiaoping
Exec. Vice Chairman	Yang Shangkun
Members	Chi Haotian, Hong Xuezhi, Lui Huaqing, Qin Jiwei, Yang Baibing, Zhao Nanqi

Military Commission of the Chinese Communist Party Central Committee

Chairman	Deng Xiaoping
Perm. Vice Chairman	Yang Shangkun
Secretary General	Yang Shangkun
Dep. Secretaries Gen.	Hong Xuezhi, Lui Huaqing

Ministry of National Defense of the State Council

Minister	Qin Jiwei
Foreign Affairs Bureau Director	Song Wenzhong

Peoples Liberation Army

General Logistics Department	General Staff Department	General Political Department	National Defense Science, Technology, and Industry Commission
Director	**Chief of Staff**	**Director**	**Chairman**
Zhao Nanqi	Chi Haotian	Yang Baibing	Ding Henggao

Service Arms

Navy	Air Force	Second Artillery Corps
Commander	**Commander**	**Commander**
Zhang Lianzhong	Wang Hai	Li Xuge

East Sea Fleet	North Sea Fleet	South Sea Fleet
Commander	**Commander**	**Commander**
Nie Kuiju	Ma Xinchun	Gao Zhenija

Military Regions and Districts

Beijing	Chengdu	Guangzhou	Jinan	Lanzhou	Nanjing	Shenyang
Commander	**Commander**	**Commander**		**Commander**	**Commander**	**Commander**
Zhou Yibing	Fu Quanyou	Zhang Wannian	Li Jiulong	Zhao Xianshun	Xiang Shouzhi	Liu Jingsong

SELLING ARMS FOR INFLUENCE

By 1987, sales of missiles and lower-technology weapons systems to both sides of the Iran-Iraq conflict had made China the world's fifth-largest arms trader: Rough estimates put the value of China's gross arms exports in the 1980-87 period at $11 billion. While Beijing has long used military aid and arms sales to promote its political position in the Third World, sales to Persian Gulf states and to Saudi Arabia have marked the culmination of China's double-edged export strategy of the 1980s: selling arms and exchanging technology as a quick source of foreign exchange as well as a building block for Beijing's burgeoning geopolitical ambitions.

Playing power politics

Today, China's sales of weaponry are closely linked to foreign policy objectives. Indeed, Beijing's choice of customers seems increasingly attuned to geopolitical and diplomatic goals. China's traditional arms clients in Africa and the communist world played a key role in Mao Zedong's "Third World foreign policy" of the 1960s and 1970s. However, as China's ambitions have grown, so too have its sales of arms, expanding into markets and areas of the world previously considered too entrenched in a superpower's camp. China's recent sales to Saudi Arabia, long one of rival Taiwan's staunchest allies, for example, have alarmed authorities in Taipei, who seem almost yearly to lose another nation's support to Beijing. When asked about arms sales to the Saudis, China's then-Foreign Minister Wu Xueqian replied with a diplomat's wish: "We want to see the earliest possible establishment of relations with Saudi Arabia."

While furthering fundamental national objectives, arm sales also meet more peripheral needs. In Egypt, at the height of that country's tensions with the Soviet Union, the Chinese used military exchanges as well as outright sales to advance their position in Cairo and further erode Moscow's hold. In a series of 1970s agreements with Egypt, Beijing received access to Soviet MiG-23 Flagger E technology in exchange for aircraft parts and weaponry. In Pakistan, analysts believe China has assisted Islamabad with its nuclear program in exchange for an unauthorized look at US Sidewinder air-to-air missiles, while close links between the two countries in aircraft development help Beijing shore up a potential buffer against Indian hegemony in South Asia and Russian and American encroachments in Afghanistan.

Beijing's first—however halting—steps in power politics have reaped significant rewards. With both the United States and the Soviet Union shut out of Iran for most of the last decade, China has emerged as a key go-between on behalf of the West in the Persian Gulf, leverage won for Beijing by its continued willingness to supply arms to both sides in the Iran-Iraq dispute.

Low costs, no questions

The details of China's sales strategy in the arms bazaar are sketchy, but competitive cost, quality, and spare-parts supply have helped to catapult Beijing into the ranks of the world's top arms traders. China's is a dual-track system of military exchange, emphasizing on the one hand simple cash sales and on the other complex materiel barter. Chinese technology is cheap, and for many developing nations, frustrated by stringent government oversight in most key supplier nations, simple cash-and-carry deals of the kind Beijing seems to prefer appear increasingly attractive. Weighed against the $2 million price tag on the Abrams M-1 tank, for example, China's $250,000 T-59, used in the army's move on Tiananmen Square, seems a bargain. In lower technology areas, the Chinese AK-47 Kalashnikov infantry assault rifle remains one of the most widely used rifles in the world today, though Beijing-backed governments and rebel movements increasingly rely on a newer variety of lightweight, high-range weapons.

Flexing military muscle

Though exports of Chinese small arms and missile technology have ruffled feathers throughout the West, official complaints seem unlikely to deter China's leaders from the military trade. If nothing else, Beijing's policy-makers regard Western protests as hypocritical at a time when American Stinger missiles arm the mujaheddin in Afghanistan, and French Exocet technology has wrought destruction in the Falkland Islands and in the Persian Gulf. Moreover, with China's prospects for trade with the West diminished in the wake of the June 4 Tiananmen Square massacre, arms sales may well serve as an attractive method of procuring needed foreign exchange.

For all the bluster China has shown in response to Western outrage at the events of June, signs continue to point to continued Chinese reliance on the West's technology, if not its ideas, in building the power of the People's Liberation Army. Doing so will require the foreign exchange that arms sales provide. Moreover, diplomatic objectives, ambitions, and the desire for status in an increasingly competitive world also contribute to Beijing's failure to heed pleas for non-proliferation. With its own interests foremost, China will undoubtedly continue to seek an international political role, even if it means as arms merchant to the world. — Evan A. Feigenbaum

posed involvement of the PLA in the Tiananmen operation, was forced to back down.

Procurement turf wars

Such jurisdictional conflicts have hampered the evolution of a cohesive force development program for the armed services. The branches of the armed forces compete for acquisitions and funds with the ground forces—the largest component of the PLA and the force that has supplied most senior military leaders—garnering the lion's share of resources for better tanks and anti-armor and anti-airborne systems. Needs identified by the Second Artillery Command for nuclear weapons, however, continue to pull weight in Beijing. Over the past decade, the Navy—long the neglected service—has received greater visibility and pressed its claims more successfully, especially for anti-submarine warfare systems and systems needed for extended naval operations. Finally, the Air Force has insisted on greater funding for its fighter-interceptors. Too often, procurement decisions within the PLA itself represent a compromise rather than a clear set of priorities.

Inter-branch rivalries are compounded by competition between the PLA and the defense industries, whose desire to acquire and apply the latest military technology for both defense and civilian purposes, as well as to develop exports, can conflict with PLA operational requirements. Because political leaders strongly support the defense industries' push for foreign exchange through military exports, their acquisitions choices often prevail. Since the defense industries may keep much of the foreign exchange they earn, they tend to favor purchases of equipment they can modify and resell to Third World countries rather than use in the field in China. For domestic use, the defense industries favor purchasing not equipment itself but the advanced technologies needed to improve their own production. Their penchant for buying a minimum of foreign military equipment while obtaining the maximum possible technology often irritates PLA leaders, since this strategy inevitably extends procurement negotiations and slows the process of getting new equipment to the troops.

Economic and commercial issues distort the decisions on upgrading military doctrine, force structure, and equipment. PLA officers do not participate directly in the weapons development and procurement process, forcing the armed services to rely on NDSTIC's judgement. The NDSTIC is meant to mediate conflicts between services while validating requirements they identify. In practice, however, the NDSTIC, whose key personnel are principally military technicians rather than operational officers, is a close ally of the defense industries. Emergence of a new generation of profit-minded liberals in key posts within the defense industries, as in the PLA, undoubtedly makes consensus on acquisition even more difficult to achieve.

From missiles to motorcycles

Entrepreneurialism within the defense industries, a byproduct of military modernization, has created a powerful faction with a large stake in China's economic reforms. The 1980s policies encouraging defense industries to harness production for commercial purposes arose from the need to utilize idle capacity within defense plants. The leadership reasoned that applying unused capacity toward production of commercial and consumer goods would help develop the civilian manufacturing sector, using the more advanced technologies available to the defense industries. Producing for profit would also help promote reform of the defense industries, which, because of heavy subsidization and the classified nature of much of its production, lagged behind the civilian sector in enterprise reform.

A major stimulus for the program came from the consolidation or reorientation of some 30,000 defense plants built deep in China's interior to support Mao's "people's war" strategy. Dispersal of the plants, lack of adequate infrastructure, and low productivity made them prime targets for conversion to civilian manufacturing. For selected priority projects, notably the Second Automotive Works near Wuhan in Hubei Province, the government has devoted considerable energy to upgrading production with foreign help.

Production for the civilian economy, after a slow start, has expanded rapidly over the past five years. Military industries, initially producing a limited number of consumer goods such as motorcycles, refrigerators, and cameras, reportedly had shifted 40 percent of their production from military to consumer goods by 1987. Defense plants have lately applied their top-of-the-line technology to manufacture quality export goods ranging from industrial machinery and nuclear-power generating equipment to the Long March satellite-launching rocket. Other defense-related industries, such as the communications industry have also increased output of civilian products.

Military modernization has also meant ridding the armed services of superfluous facilities and improving the efficiency of those remaining. Since the mid-1980s the military has turned over to civilian use airports, rail lines, and ports. Military hospitals have even begun accepting paying civilian patients—sometimes to the detriment of enlisted men, who reportedly receive inferior care because they cannot pay cash. In Hainan the PLA runs gasoline service stations, with soldiers dispensing gasoline to civilian customers.

Well-connected corporations

The acquisitive urge has affected much of the PLA, which sees commercial operations as a way of supplementing limited budgets. The Air Force's *Lantian* (Blue Sky) trading company in 1985 launched its own commercial airline, which now competes with new regional air carriers along a number of lucrative domestic routes. Economic reform has also caused the proliferation of trading corporations handling military exports and imports to compete more aggressively to purchase technology and equipment and also to sell both domestically and abroad. Foreign trade corporations (FTCs) within the various ministries producing military hardware have come to vie with the traditional trade corporations under the Ministry of Foreign Economic Relations and Trade (MOFERT) for military sales and purchases. In addition, the armed services themselves have spawned several FTCs (*see* list). Some of these agencies, established initially to purchase "quick fix" equipment, have become involved in the overseas sale of both military and civilian products. These corporations have demonstrated more flexibility than the traditional FTCs in concluding foreign purchases, and a number of the procurement companies—probably because of their connections with top-level defense officials—have successfully withstood State efforts to abolish them.

The most visible of the military FTCs is Poly Technologies, which has now become a major exporter, in addition to importing military systems and equipment. Close connections between its major figures and those of China's defense establishment buttress Poly's power. Although Poly operates as a subsidiary of the China International Trust and Investment Corp. (CITIC), it actually works for the powerful Equipment Department of the PLA General Staff Department (GSD). In 1985 the heads of the two organizations swapped positions: General Li Guang became chairman of Poly, and former Poly Chairman He Pingfei—son of PLA Marshal He Long—took over for Li as head of the Equipment Department. He Ping, Deng Xiaoping's son-in-law, now serves as Poly's president.

The commercialization of the military has undoubtedly exacerbated social and ideological animosity between older, high-ranking defense officials and younger field officers and defense industry cadres. Many leaders have used their positions for personal and family gain, stirring resentment among their subordinates. Tensions have also reportedly arisen between richer, entrepreneur-

CHINA'S MILITARY PROCUREMENT ORGANIZATIONS

China North Industries Corp. (NORINCO)
Aegis: China North Industries Group Corp., Ministry of Machinery and Electronics Industry (MMEI)
President: Zhou Peide

One of China's largest defense conglomerates, NORINCO imports, exports, and manufactures military products, including weapons, tanks and armored vehicles, and ammunition, as well as chemical products, mechanical products, light-industrial goods, and optoelectronic products.

China National Electronics Import-Export Corp. (CEIEC)
Aegis: MMEI
President: Ouyang Zhongmu

CEIEC's military-related activities entail providing avionics and flight instrumentation for military aviation in cooperation with other defense contractors.

China State Shipbuilding Corp. (CSSC)
Aegis: State Council
Chairman: Chai Shufan

CSSC handles the Navy's shipbuilding but has recently turned its attention to commercial shipbuilding. CSSC also imports technology and is a partner to about 30 joint ventures.

China Great Wall Industry Corp.
Aegis: Ministry of Aeronautics and Astronautics
President: Tang Jinan

Established in March 1979, Great Wall provides satellite launch services for foreign countries. The company also manufactures electronic instruments, ground radar, and computers. Great Wall's military role is to handle missle import and export.

Poly Technologies (Poly)
Aegis: China International Trust and Investment Corporation (CITIC) and PLA General Staff Department
President: He Ping

Poly deals almost exclusively in defense-related products, such as radar and specialized technology. Poly handles sales and purchases on a government-to-government basis and maintains worldwide contacts through Chinese embassies and consulates.

China Aviation Technical Import and Export Corp. (CATIC)
Aegis: Ministry of Aeronautics and Astronautics
President: Sun Zhaoqing

CATIC functions as the foreign-trade arm of the Ministry of Aeronautics, specializing in exporting aviation industrial products and importing advanced technology for the aviation industry. The 200 factories for which CATIC is agent have begun producing aviation products, tools, and motorcycles for civilian use.

China Jingan Materials and Equipment Import/Export Corp.
Aegis: Ministry of Public Security
President: Liu Zhaoxiang

Jingan is the only government-authorized dealer of police equipment. It handles the import and export of instruments for criminal detection, security devices, fire-fighting and traffic-safety equipment, and police vehicles, among other things. It also offers consulting services.

China National Machinery Import/Export Corp. (MACHIMPEX)
Aegis: The Ministry of Foreign Economic Relations and Trade.
President: Gu Yongjiang

Because MACHIMPEX is not affiliated with a specific industry, it procures all types of military equipment for the PLA, frequently importing airplanes and aeronautics equipment.

China Nuclear Energy Industry Corp. (CNEIC)
Aegis: China National Nuclear Corp., Ministry of Energy
President: Zhang Jinduo

CNEIC is an import/export company that buys and sells equipment for the study and use of nuclear energy. CNEIC was established to speed the transition to manufacture of nuclear equipment for civilian use.

China Precision Machinery Import/Export Corp. (CPMIEC)
Aegis: Ministry of Aeronautics and Astronautics
President: Zhang Tong

CPMIEC is responsible for the development, production, and export of defensive tactical missile weapon systems; precision machinery, equipment, and tools; medical instruments; vehicles; satellite receiving antennae, and household appliances.

China Xiaofeng Technology and Equipment Corp.
Aegis: NDSTIC
President: Yang Shaojing

Established in January 1981, Xiaofeng imports computers, instruments, and components for scientific research.

Xinshidai (New Era) United Trade Corp.
Aegis: NDSTIC
President: Li Xiaolin

Established in 1980 as the commercial arm of NDSTIC, where many of Xinshidai's cadres also hold key positions, Xinshidai is responsible for the overall planning and coordination of China's defense industries.

China Xinxing Corp.
Aegis: General Logistics Department of the PLA
President: Zhang Zhuqiao

Xinxing acts as the military procurement arm for the General Logistics Department of the PLA. It is China's only import/export corporation openly under direct PLA leadership. Xinxing imports advanced technology and equipment and also oversees businesses and institutes attached to the PLA.

China Yanshan United Foreign Trade Co.
Aegis: Yanshan Petroleum Corp.
Manager: Liang Chihui

Yanshan is the foreign-trade arm of the Yanshan Petrochemical Corp. While no record of purchases exists, Yanshan has approached foreign firms for military or high-tech imports.

China Zhihua Trading Corp. Ltd.
Aegis: MOFERT
President: Li Li

China Zhihua is the arm of the Chinese military responsible for communications products. Its scope of business includes radio communications equipment, mobile earth satellite stations, teletypewriters, spare parts, and test facilities, among many others.

Pinghe Electronics Co. Ltd.
Aegis: Everbright Industrial Corp. (also affiliated with the PLA General Staff Department and NDSTIC)
President: Zhao Xuguang

Established in 1983, Pinghe originally handled the export and import of weapons, technology, and equipment. Now it is involved with a wide range of businesses, including medical equipment, textiles, chemicals, and even two hotel joint ventures.

SOURCE: *China's Trade and Investment Organizations,* US-China Business Council, 1989, and Council files. Compiled by James M. Kingsbury.

ial military units and those without money-making enterprises, as well as between more affluent military regions and those in poorer, rural areas.

The Tiananmen loyalty test

Military leaders clearly viewed the PLA's role in suppressing dissent in May and June as an unwelcome diversion from military modernization programs. However the suppression operations in Beijing and the provinces decisively proved the PLA's loyalty to the Party. While senior military figures, including former and current Defense Ministers Zhang Aiping and Qin Jiwei, spoke out initially against violent suppression of the pro-democracy movement, their objections fell well short of mutiny, and top-level military leaders kept their jobs in Tiananmen's aftermath. The army's apparent vacillation in dealing with the demonstrators before June 4 derived in large measure from the conflicting guidance troops were receiving from above. Once the decision was made to silence the demonstrators, the PLA moved quickly and ruthlessly. Units involved in the June 4 operation, which included the 27th and 38th Group Armies and the 15th Army Airborne Division, were among those deployed to Beijing from six of China's seven military regions. The decision to deploy troops from throughout the country came not because of widely rumored reluctance of units in the area to comply with the order, but to spread responsibility and quell future dissent within the armed forces.

Although the reports of brewing rebellion among army troops in Beijing in June proved false, the post-reform PLA no longer resembles the conservative and xenophobic military leadership of the 1960s and 1970s. The emergence of a vibrant private sector in China has spawned an increasing number of younger PLA officers and defense industry officials who see economic reforms as crucial to obtaining adequate funding for their programs and improving the standard of living for themselves and their subordinates. They are prepared to argue that curtailing the reforms would harm the military's interests. They believe that expansion of military cooperation with foreign nations—especially in the West—is also crucial to acquiring the advanced technology, leadership and management skills, and knowledge essential for their modernization goals. While the PLA and defense industries do contain extremely conservative, ideological leadership factions, particularly in the PLA ground forces, constituencies of younger professionals committed to reform are emerging more aggressive than ever before. Divisions have opened up within the military—as in the Party—as a result of Tiananmen. What factions or constituencies will rise to prominence within the military will depend largely on the course of the power struggle within the leadership. The possibility that China's military could in the end emerge, as in other Third World countries, allied with the forces of modernization should not be discounted, should China's liberal, pragmatist leaders have their way. 完

Losses on both sides go beyond the military deals

The Military Sales Ban

Richard E. Gillespie and Kelly Ho Shea

The suspension of US military exports to China, announced by President Bush on June 5 and backed by US allies, is already affecting US companies through lost sales, suspension of technology transfer, and halted coproduction ventures. Commercial sales are feeling a trickle-down effect, as dual-use commercial technology with potential military applications undergoes tougher screening procedures in the export-licensing process. Liberalization of the licensing system for such technology will also be stalled. Within China, the multilateral ban on military sales will hurt several major military programs and, to a lesser extent, civilian projects requiring advanced technology. The bans will also inhibit future military and political cooperation with the West.

While President's Bush quick application of such sanctions deflected stronger, potentially more restrictive congressional action in the early summer, there is as yet no indication that the measures have drawn any reaction from China's leaders beyond expressions of frustration and anger. Preoccupied with its own political survival, the current Chinese leadership appears undisturbed by the damage done to China's foreign political and economic relations by the Tiananmen massacre and subsequent leadership struggle. It may take some time for China to examine the long-term implications of the military sanctions, which are unlikely to see reversal in the near future. During the current hiatus in the US-Chinese military relationship, both countries would do well to evaluate the fruits of 15 years of cooperation—how the relationship has been used, and what further moves would best promote US interests and China's political and economic progress.

Ending government contracts

The sanctions imposed by the Bush Administration banned military sales to China of all items controlled by the State Department and cited on State's Munitions Control List (MCL). The ban led to suspension of work on about $600 million in Foreign Military Sales (FMS)—government-to-government contracts—and about $425 million-worth of MCL commercial sales. Separately passed House and Senate sanctions, a version of which is almost certain to become law in the fall, would essentially codify measures the Administration has already taken, although a further deterioration in China's internal political situation could trigger more severe sanctions. The pro-

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posed measures, which add requirements to suspend sales of crime-control equipment and nuclear materials, can be waived by the president for reasons of "national security" or "national interest."

The June 7 *Federal Register* notice published by the US State Department's Office of Munitions Control suspended "all licenses and approvals," including manufacturing licenses and technical assistance agreements. Affected are all licenses already granted since June 1987 and those pending review at the time of the suspension. All items manufactured but not shipped are being stored in the United States at Chinese expense. DOD has suspended all Chinese engineers and technicians working on FMS projects in the US, while the handful of US engineers and technicians working on the four FMS projects in China have been sent home.

The largest FMS contract is more than $500 million for the F-8 fighter upgrade (Project Peace Pearl), for which Grumman Aerospace Corp. is the prime contractor. Suspension of the Peace Pearl project could cost Grumman $257 million to cover a development program, parts, and support systems, though Grumman is still developing initial design on the avionics system at Bethpage, NY. Westinghouse Electric Corp. stands to lose a large piece of the Peace Pearl project—its $41.4 million contract for fire-control radars. Among other projects suspended are a US Navy contract valued at $8 million to supply the Chinese Navy with four Honeywell Mark 46 anti-submarine torpedos, and a General Motors Hughes $60 million contract for four ANTPQ 37 anti-artillery radars, only two of which have been delivered. The artillery fuze and primer milling equipment supplied by the United Technology subsidiary Hamilton Standard in accordance with its $28 million contract is already in place. Only the services part of the contract remains unfulfilled.

Suspending private sales

In addition to FMS sales, the military sales ban has also affected many commercial sales of items that fall on the MCL. The value of affected licenses totals about $425 million, of which $300 million is for licenses already granted, but these figures reflect only the value of the banned component and not the total value of the equipment sale. The total value of sales affected may exceed $700 million, including the costs of the equipment, such as aircraft, on which MCL components are installed.

Suspension of military exports has affected a number of non-governmental sales of military systems and hardware. Most prominent among these is the sale to the Chinese military of six Boeing Chinook cargo helicopters valued at over $100 million the license for which was pending at the time of the suspension. Sikorsky has voluntarily stopped supplying spare parts for servicing 24 Sikorsky C70C helicopters (civilian versions of the Blackhawk helicopter) sold to the People's Liberation Army (PLA) in the mid-1980s. The cutoff comes at a time when the PLA is starved for helicopter parts and has already cannibalized two of the C70Cs for parts. Also stopped is a coproduction venture involving manufacture of proximity fuses with Ferranti International Signal (formerly ISC Technologies) and the development of new tank engines by North Industries Corp. (NORINCO) with the Textron subsidiary Cadillac Gage.

China's options

Mindful of the disastrous pullout of Soviet advisors in 1960, Chinese leaders have developed alternative foreign suppliers for most military technologies over the last 15 years to help them weather withdrawal of foreign military support. China's armed services will certainly be hurt, but to what extent depends on the duration and multilateral character of the ban. Providing it can can bring about peace and stability in China, China's central leadership expects European defense contractors to pressure their governments to resume military business. If European countries break ranks and sell to China, the damage to China's military programs will be slight. As long as US allies remain united in barring military sales to China, the effects will go deeper. However, China may be prepared to entertain another option—approaching Moscow for equipment the West refuses to supply. Currently China seems little interested in buying the technology and equipment the Soviets have to offer, but the USSR is beginning to promote sales of military equipment in China, and China's attitude could change.

The military sales bans effectively sever China's military-industrial links with at least eight military powers—Great Britain, France, Italy, Australia, Sweden, Israel, Austria, and Switzerland—and could over time seriously retard China's military modernization. Although it has spent only modestly on military purchases, China has relied increasingly on bilateral military cooperation to obtain crucial defense and civilian dual-use technology over the last 15 years. China prefers to acquire technology rather than equipment, through licensing, coproduction, reverse engineering of foreign prototypes, and modification of foreign equipment, but it also has resorted to direct purchase of crucial "quick fix" equipment. This policy has substantially improved China's defenses in the short term, laid the groundwork for a long-term upgrading of weapons manufacturing capability, and helped expand China's soft-currency arms exports to countries in Africa and Asia.

The suspension of military exports by the United States and Europe will be felt in several priority programs designed to upgrade China's conventional capabilities. The impact will be felt most by China's Air Force, which is seeking Western technology to upgrade Soviet Mig-19 and Mig-21 aircraft designs into a new generation of agile, extended-range fighter-interceptors. As part of this effort, China has been working with Great Britain and the United States to provide new avionics for its F-7 fighter and the F-8 interceptor, and with Italy for similar help with the A-5 ground-support aircraft. The F-7 and F-8 also need more powerful engines. In its search for jet engines that incorporate Western designs emphasizing higher operating temperatures and composite materials, China has sought help from the four largest Western jet engine manufacturers, anticipating that COCOM restrictions in this area sooner or later would be lifted.

Programs utilizing foreign assistance to help China's high-profile "blue water" navy to defend the coast, protect shipping lanes, and conduct extended-range operations will also be hurt by the ban. The need for modern anti-submarine warfare and fire-control systems for surface craft has prompted the Chinese into talks with the United States and Europe over procurement of modern sonars, radar-controlled rapid-fire cannon, anti-ship missiles, and anti-submarine torpedos. For US firms, this has meant contracts for anti-submarine torpedos and diesel engines; for Italy and France, sales of fire-control systems and cannon have been modest but lucrative. The suspension will set back China's plans to design and build domestically state-of-the-art destroyers, frigates, and other surface combattants.

The ban will stymie, at least temporarily, China's plans for upgrading its armor capability and troop mobility. Its Soviet-design tanks need better cannon, fire-control systems, and engines that operate better in cold weather, so termination of tank programs with US and British companies will hurt. Expansion of China's fledgling helicopter force with US, French, and West German assistance will suffer a setback, as will development of mechanized forces with foreign jeep, truck, and armored personnel carrier technology.

Paired with the suspension of high-level military exchanges and the interruption of China's military cooperation with European countries, the sanctions could also have significant impact on China's high-technology civilian industries. Foreign technology to upgrade China's civilian and military electronics industries is still badly needed.

Commercial goods affected

On the US side, the ban is having repercussions on unintended areas of business; licenses for non-military equipment and components valued at $425 million are getting caught in the suspension. Sales in the high-profile aersopace sector have been hardest hit, with big-ticket items such as communications satellites and commercial aircraft delayed.

To minimize the suspension's impact on commercial sales, the United States may grant waivers to the ban. By mid-August about 16 requests for exemptions on licenses granted had been submitted, totaling $10-12 million. Exemptions to date have been granted only in the aerospace sector, with Boeing receiving a waiver in July for delivery of four 757s to the Civil Aviation Administration of China-Guangzhou (CAAC). Although the aircraft, valued at $200 million, is a civilian item licensed by the Department of Commerce (DOC), the sales had been suspended because the aircraft contain Honeywell inertial reference systems, which are necessary to secure safe and accurate flights and fall on the MCL. The navigation system, 50 units of which are already installed on foreign aircraft sold to China, is not applicable for military use. A preliminary decision has also been reached on the export of the refurbished Westar VI satellite to China. Hughes Aircraft Co. currently has sales agreements with Asiasat, a British/Hong Kong/Chinese consortium, to ship the Westar VI and with Australia's Aussat to manufacture and ship two new satellites to China for launch on Long March rockets in 1990-92. While licenses granted for the Aussat satellites, valued at about $200 million, remain suspended, Hughes has obtained permission to exchange technical data with the Chinese on the Asiasat, valued at about $40 million. The decision on the Asiasat, however, merely enables Hughes to keep its contract on track. A final decision on whether to grant the license awaits further discussion.

As long as US allies remain united in barring military sales to China, the effects will go deeper. However, China may be prepared to entertain another option—approaching Moscow for equipment the West refuses to supply.

Automatic teller machines (ATM) and other equipment for China's banking industry have also been affected by the ban. NCR Corp., which contracted in 1988 to sell 70 ATMs in China, found the sale blocked, because the ATMs include MCL-controlled data-encoding devices. After the ban, NCR removed the encoding systems and shipped the modified ATMs. Another company that has been selling computer banking products, including ATMs, to China for about four years is trying to obtain a waiver for several sales.

This is the first time the United States has granted waivers to sanctions imposed on foreign countries and indicates the Administration's desire to preserve commercial ties while limiting the sanctions' effects to the military.

Tight export controls

The sales ban did not include dual-purpose high technology controlled by the Department of Commerce and contained on the Commodity Control List (CCL). Nevertheless, dual-use goods have not escaped unscathed. The Administration moved in early June to suspend efforts to relax export restrictions for China. It has indefinitely suspended the implementation of a distribution license (DL) for China, originally set for summer 1989, permitting a US exporter to ship a range of commodities to China under a single license.

The US also suspended an upcoming move to further liberalize the export control system for China through the development of a "core list" that would identify items barred to China, allowing export of all other, unspecified goods. Currently, the China Green Zone system identifies for exporters items that can easily be licensed for export to China, while exports of other items must undergo time-consuming reviews.

Export controls on dual-use items have also been tightened multilaterally by the Coordinating Committee on Multilateral Controls (COCOM). In line with US government moves, COCOM members informally agreed to suspend individual implementation of a distribution license for China and negotiations for core-list liberalization.

Formally, COCOM's policy to control exports to China only for strategic purposes has not changed. Senior-level COCOM meetings scheduled for the fall are expected to raise the issue of the DL and continuing liberalization for China. However, even if Congress presses the Administration to ask for a suspension of high-tech exports, COCOM is unlikely to depart from precedent and impose punitive sanctions.

Lengthy reviews

The Administration's sanctions have indirectly affected the sale of high-technology, dual-use commercial products to China by increasing scrutiny of export applications at DOC and thus lengthening processing time. The average processing time at Commerce has increased by at least one week, with additional time undoubtedly spent by Defense and other referred agencies.

Under Commerce's enhanced review process, all license applications are being reviewed case by case, only after approval by several levels within Commerce's Bureau of Export Administration (BXA). Particularly sensitive cases are referred daily to the undersecretary of BXA and other top department officials. These cases include license applications for the export of equipment with potential military or police applications, equipment previously subject to a significant interagency dispute, or equipment valued at more than $5 million. No sale to the armed forces or police has been approved since June 4.

Ripple effect

US companies are exercising additional caution in pressing for new high-technology licenses in light of the unfavorable business climate in China and because of the uncertainty of future US policy toward China. DOC estimates prior to June indicate that the department would have approved a record $3.5-4 billion in dual-use licenses in 1989, up from $3 billion in 1988. However, in the wake of China's military crackdown on student demonstrators, the number of new license applications being submitted to DOC has dropped significantly from the average 570 new export applications received each of the first five months of 1989. In June and July, Commerce received 425 and 338 applications respectively. Companies' reassessment of their China activity in the current political and economic environment partly accounts for the decline. Uncertainty over the impact of US government actions on high-technology sales and increasing pressure from Congress to curtail such sales also appear to have bred caution among American companies.

Although the Administration has indicated it does not intend to roll back existing export-controls policy on dual-use technology, the more severe sanctions being considered on Capitol Hill would in effect cut back Green Zone levels and restrict items readily available to China.

Damper on high technology

Paired with the suspension of high-level military exchanges and the interruption of China's military cooperation with European countries, the sanctions could have significant impact on China's high-technology civilian industries. Foreign technology to upgrade China's electronics industry is badly needed, for example, and the civilian and military electronics sectors have been asked to exchange the technologies they develop or purchase abroad, where feasible. The military suspension already is increasing foreign governments' caution in authorizing the sale of civilian electronics equipment and technology, for fear the equipment will be adapted to military use. If this trend should become more pronounced, other civilian industries could be hurt, including petroleum, metallurgy, and petrochemicals, as well as factory automation programs in almost all civilian sectors.

The ban is having repercussions on unintended areas of business; licenses for non-military equipment and components are getting caught in the suspension.

Undermining strategic goals

The US government hopes its ban on military exports and high-level government exchanges, through the negative impact on China's military programs, will help promote reform in China. Indeed, the Administration's support of continued commercial ties suggests that those parts of the economy key to the reform process may be spared the effects of the ban. However, the sanctions will take a toll both on US business and on the relationship with China that five administrations have nurtured.

Stopping work on the four current FMS sales contracts, while undeniably hurting key Chinese modernization programs in the long run, may also impede pursuit of Washington's strategic objectives. The Grumman Peace Pearl project, the MK-46 torpedo sale, the GM Hughes ANTPQ-37 anti-artillery radar sale, and the Hamilton Standard armor-piercing ammunition coproduction venture were intended to improve China's conventional air, naval, and anti-armor capabilities needed for its defense—which the US government perceives as important to national interest. If China's ability to defend itself against attack remains a key US strategic objective, the US government needs to distinguish between sales that contribute to China's deterrent and defense posture and sales that improve PLA capabilities to suppress its citizenry. The Bush Administration is also well aware that the current ban, if long extended, may severely damage the still-important US policy of bolstering China as a counter to the Soviet Union and as an influential actor in regional politics.

The wrong enemy?

The current sanctions merit a final caution: China's military—particularly the Navy, Air Force, and defense industries—contains important constituencies that support reform and the open-door policy. The armed forces clearly showed their opposition to the violent suppression of pro-democracy dissidents—although the PLA, once the decision was taken, performed its task both brutally and effectively. Military leaders, who had been reluctant to reenter the political arena, can be expected to resist future efforts to intervene on behalf of political leaders. The long-term isolation of China's military leadership enforced by a ban could penalize the efforts of the reformist military professionals.

While the length of the US military suspension will depend primarily on China's ability to achieve political stability, the Bush Administration will need to be flexible in its reactions, and Congress and the American people should allow the president room to maneuver. 完

Back to Square One?

China's tourism industry may take years to recover from a disastrous summer

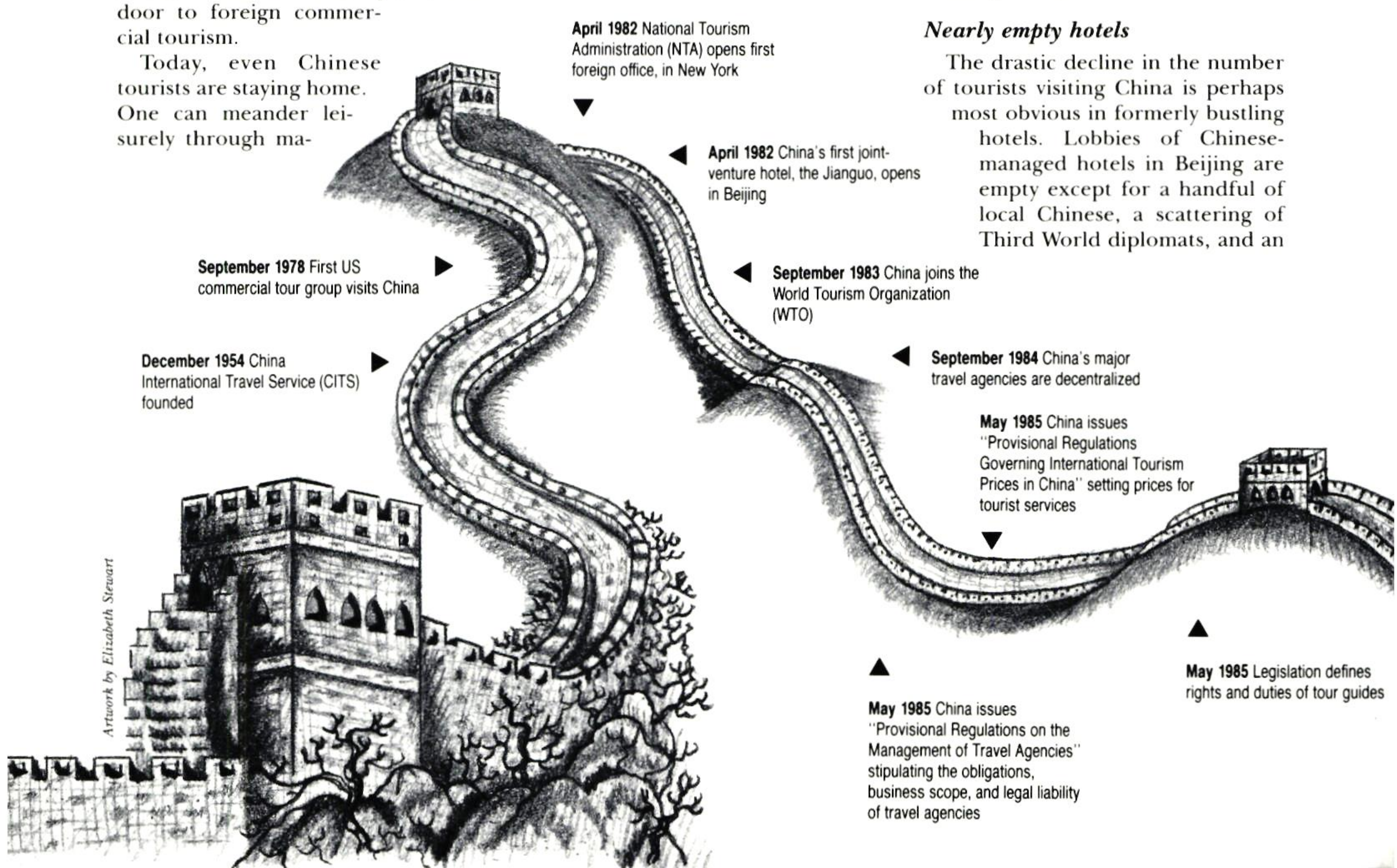
Anne F. Thurston

Widespread revulsion against the Chinese government's violent suppression of its own citizens and a US State Department advisory against travel to China have led to a virtual collapse of China's tourism industry. Figures recently released by the Chinese National Tourism Administration (NTA) indicate that 22,000 foreigners (mostly journalists and businesspeople) visited China in June—81 percent fewer than in June 1988—and more than 90 percent of scheduled tour groups were canceled. After 10 years of impressive growth, the recent numbers have declined to 1979 levels, when China first opened the door to foreign commercial tourism.

Today, even Chinese tourists are staying home. One can meander leisurely through major tourist attractions like the Forbidden City free from the usual jostling crowds. In Xi'an, visitors to the huge hangar housing the terra-cotta warrior exhibit are so sparse that the breathtaking view of the army is unimpeded. The throngs that once jammed the Great Wall have been reduced to a trickle, and many of today's visitors are soldiers from Beijing. On one July weekend, for example, the only noontime guests in the foreign tourists' dining hall at the Great Wall's Badaling section were three Russians, and the only foreigners to be seen on the wall itself were a Middle Eastern family. No foreign tourists were spotted at the Ming Tombs, and the vendors who ordinarily hawk everything from furs to fake antiques and Coca-Cola have disappeared. A ticket seller at the Ding Ling tomb said that normally there are 20,000-30,000 visitors a day at this time of year; now there are several thousand. As a result, 400-500 staff at the Ming tombs have been let go. Even the formerly ubiquitous "Hello, change money?" is rarely heard.

Nearly empty hotels

The drastic decline in the number of tourists visiting China is perhaps most obvious in formerly bustling hotels. Lobbies of Chinese-managed hotels in Beijing are empty except for a handful of local Chinese, a scattering of Third World diplomats, and an



Artwork by Elizabeth Stewart

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occasional prostitute. Lobbies at a few joint-venture hotels—the Jianguo, the Lido, and the Palace—are slowly coming to life, but the guests are mostly businesspeople, journalists, and overnighting airline crews—not tourists.

Occupancy rates at Beijing joint-venture hotels, inflated by long-term leaseholders who in many cases have not yet returned, by late July were up from lows of around 15 percent just after June 4 to a high of 45 percent at the Palace and Jianguo hotels, 35-40 percent at the Jinglun (Beijing-Toronto) and Lido Holiday Inn, 30 percent at the Great Wall Sheraton, and 25 percent at the Shangri-La. Occupancy rates at Chinese-managed hotels—such as the CITS-run International Hotel in Beijing, which has only a 10 percent occupancy—and of joint-venture hotels outside Beijing are generally lower. In Xi'an, where business travelers are rare and the number of tourists declined from 35,000 in June 1988 to 5,500 in June of this year, hotels have been very badly hit—the Bell Tower Hotel, run by Holiday Inn, reportedly had a 1 percent occupancy rate during the first week of July. In Shanghai, occupancy in June averaged about 40 percent, with the Huating Sheraton running at 30 percent occupancy and the Shanghai Hilton somewhat higher.

Joint-venture hotels are divided about how to respond to the drastic decline in their clientele. Several in Beijing—the Sheraton, the Jianguo, and the Jinglun—have concluded that the precipitous drop in business is market-wide and that no amount of advertising or reduction in room prices will increase business. Thus, except for the Jinglun's additional inducements of a free breakfast and cocktail, these hotels have not lowered their rates. The Holiday Inn Lido and the Shangri-La, on the other hand, are trying to attract business by cutting their standard room prices in half, at least until September. Even so, business has not noticeably picked up.

Staff and salary cutbacks

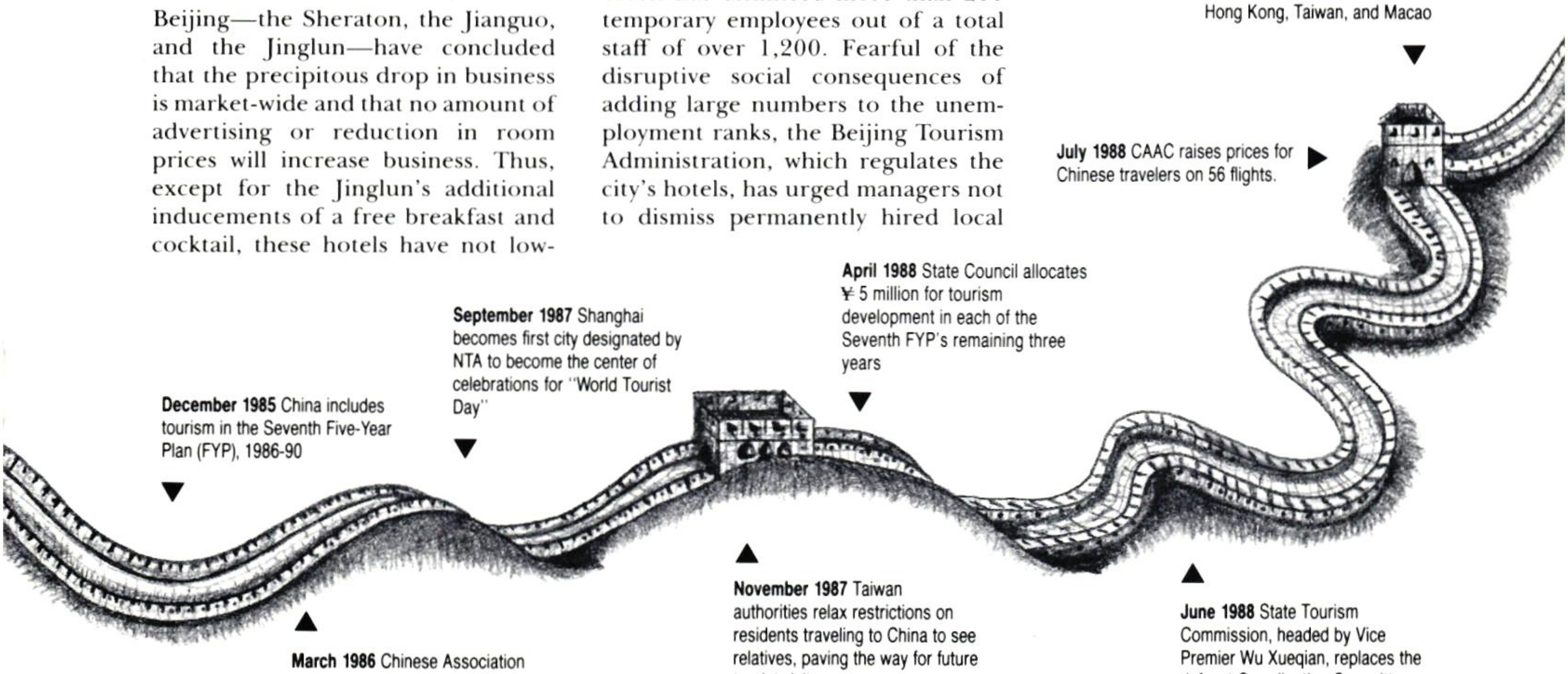
Both Chinese and expatriate staff at all hotels have been considerably reduced, although hotels are handling staffing problems somewhat differently. At joint-venture hotels, some expatriate staff who left after the massacre have not returned—some have quit; others have been fired (in some instances because they fled without permission); some were let go before their contracts expired; and others are not yet needed because business is still so slow. This last group is waiting outside China—unpaid—until business expands enough to warrant their return. In some cases ill feeling remains between foreign management and expatriate staff who fled without permission and between some disillusioned Hong Kong staff and local Chinese. Many Hong Kong Chinese returned to China only reluctantly and are now applying for jobs at home.

Among the local staff, temporary employees, who are often pensioned retirees working at housekeeping jobs, have been released from most hotels. For instance, the Jinglun Hotel has dismissed more than 200 temporary employees out of a total staff of over 1,200. Fearful of the disruptive social consequences of adding large numbers to the unemployment ranks, the Beijing Tourism Administration, which regulates the city's hotels, has urged managers not to dismiss permanently hired local Chinese staff. Most hotels, rather than releasing permanent staff, are reducing salaries and finding other ways to keep employees busy—in English training classes, on vacations, and in political study sessions.

With the exception of the lowest-paid workers, whose wages by and large have not been reduced, most employees in the hotel industry are currently working at some 65 percent of their normal wage package (usually consisting of a base salary plus bonus, which for most workers has become virtually a part of their salary). At the International Hotel, however, only 700 of the total 2,000 staff work on any given day. The income of those who are working has been reduced from a monthly average of ¥300 to ¥120-130. The other 1,300 employees continue to receive ¥60-70 per month while participating in training programs outside the hotel or working on a hotel-run farm in the Beijing suburbs.

If the number of tourists visiting China should pick up, dismissed hotel staff could be recalled quickly, and currently suspended services could be rapidly resumed. For now, however, tourist hotels are still operating at well below capacity with many of their restaurants, bars, and auxiliary services closed.

Taxi companies, too, are suffering.



No staff have actually been dismissed, but work days are staggered, with only a certain percentage of the entire pool at work on any given day. Taxis still line the block around joint-venture hotels, but business is so slow that the drivers often spend the day playing cards. While some companies continue to pay their employees full salaries and bonuses, some drivers say that their bonuses have been dropped and their salaries cut. For both hotel employees and taxi drivers, the decline in tips must take another considerable bite out of their normal income.

The official line

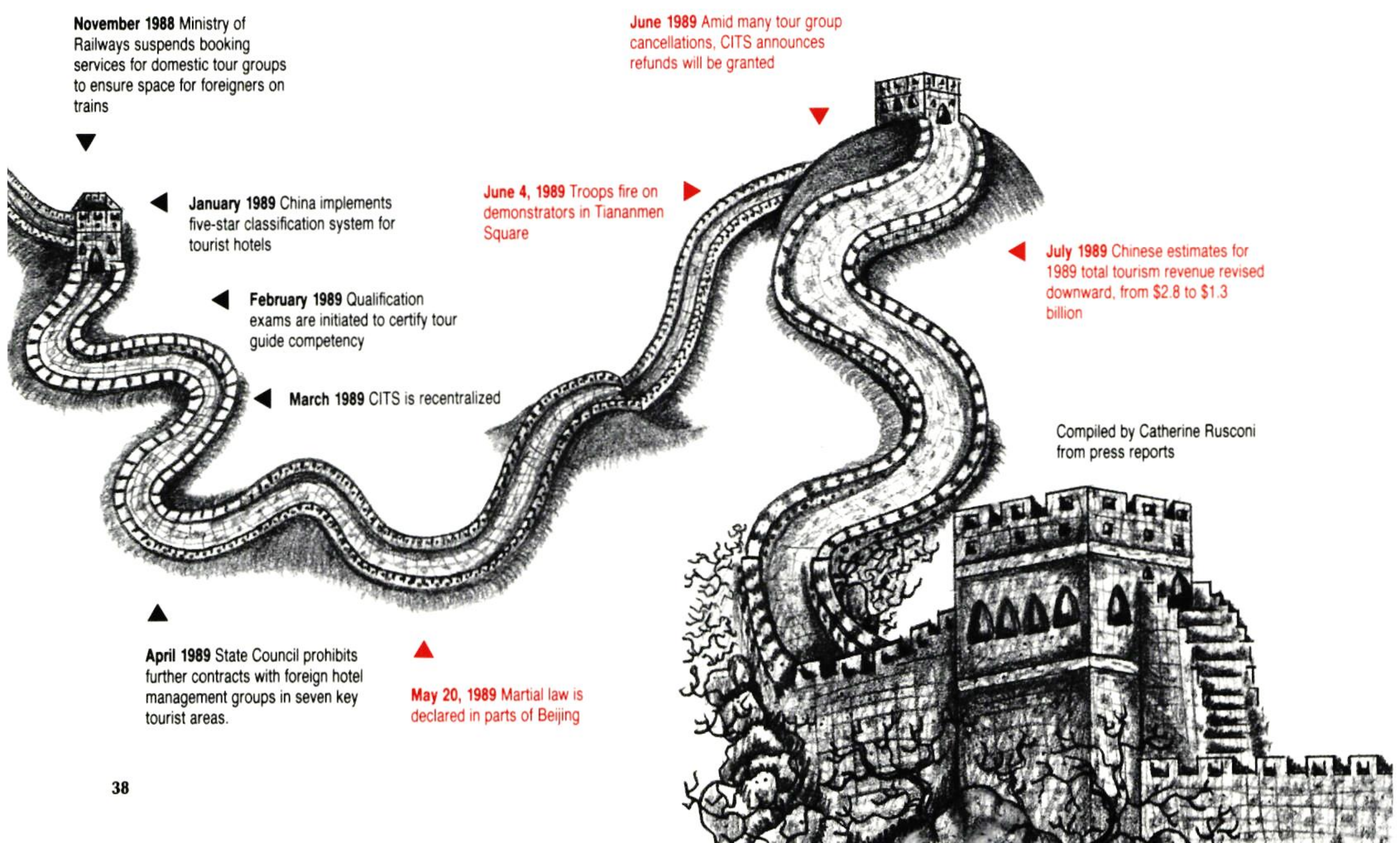
The NTA, the Beijing Tourism Administration, and the head office of CITS began encouraging the return of tourists a few weeks after the violence in Beijing. The precipitous decline in tourism, they argue, is due to foreigners' mistaken fears that China is not safe and that major sites remain closed—misperceptions blamed on the international media, which Chinese officials claim is distorting the truth about the situation in China. Tourism officials are attempting to allay such fears by telling US tour operators that everything has returned to normal. The NTA has repeatedly guaranteed the safety of foreign visitors, assuring them that all tourist sites are now open, and encouraging them to come to China to see with their own eyes. All tourist facilities are ready to serve even better than before, tourism spokesmen say, and CITS is ready to accept bookings for 1990 tours.

Less publicly, both the NTA and CITS are anxious to solicit whatever information they can on how long the drastic decline in tourism is likely to last and what can be done to encourage tourists to return. On July 11-12, the Beijing Tourism Bureau held a two-day seminar for foreign tour operators, and participants were given the chance to suggest what the Chinese must do before the tourism industry can be revived. Approximately 440 people (including trade journalists) from 29 countries attended the seminar. Senior representatives from nearly all major travel-related orgainizations in China (i.e., CITS, CAAC, etc.) also attended the seminar.

The meeting confronted Chinese tourism officials with a double bind. In addition to giving obvious advice (i.e., martial law is an impediment to tourism), tour operators argued that the tourism industry in China needs a major pricing overhaul, and both transportation service and the quality of guides must be improved significantly before tourism can be fully revived. As a result of this and other discussions, the Chinese government privately estimates that it will take at least two years for tourism to recover fully, and the NTA has reportedly scaled down 1989 total tourism revenue projections from $2.8 billion to $1.3 billion.

'Rectifying'—and reviving—the industry

While waiting out the slump, the NTA is using this "special" period as an opportunity to "rectify" the industry. The small, semi-independent travel agencies that sprang up throughout China after the 1984 decentralization of the industry will be investigated, and those deemed "unqualified" will be dismantled. The investigation will focus on whether agencies are undercutting State pricing policies, whether they are making a profit, whether they have maintained "illicit" relations with tour operators overseas, and on the quality of tour guides. The period of investigation has just begun, however, and no decisions have yet been made.



Compiled by Catherine Rusconi from press reports

A major focus of the rectification will be on the training of guides. The NTA reports that no guides have yet been dismissed, and their salaries—in contrast to those of hotel employees—have not been cut. Training is being conducted within each local travel service by older, experienced staff and is said to focus on language, Chinese history and culture and "how to treat foreigners." In July, all guides were required to take a certification exam in order to continue their position. Some 16,600 guides nationwide participated in the exam, and 11,900 passed. More than 3,200 guides were considered sufficiently knowledgable and experienced that they did not have to take the exam, bringing the total number of guides recognized as qualified by the State to over 15,000. Those who did not pass the July exam will be given another opportunity in April of next year.

At the same time, the NTA is permitting travel services to introduce fairly substantial price reductions in order to attract customers. CITS, whose business has been devastated, is offering both financial and promotional inducements to encourage the return of American tourists. Land prices (i.e. food, CITS hotel rooms, guides, and intra-city transportation) have been reduced by 20 percent through November, and will go down by 30 percent from December 1 to the end of March 1990. In addition, groups of between 6-10 people will receive the rate usually offered to groups of over 10 people. Domestic CAAC fares were also reduced 20 percent August 1. CITS has also announced that there will be no increase in its 1990 prices. Moreover, CITS has agreed to refund all unused land costs paid by individuals or groups who either left in the midst of the turmoil or who had made reservations but did not come as planned.

As a further inducement to tour operators, the head office of CITS invited a number of American travel agencies to participate in an all expense-paid familiarization tour of Beijing, Xi'an, Shanghai, and Hangzhou designed to demonstrate that everything has returned to normal and that the travel service is functioning well. Both this and the two-day travel seminar were duly covered by Chinese television as part of the government's campaign to convince the Chinese people that everything has returned to normal and that foreign friends are returning to China.

Only six companies—Abercrombie and Kent, American Express, Japan and Orient Tours, Lindblad Travel, Lotus Tours, and TBI—participated on the July 10-19 trip. One participant described the trip by saying that it "was successful in that it convinced me that travel in China is safe, but reaffirmed my feelings that most people would not choose to go there for a vacation right now."

Far from 'normal'

Indeed, although all the major tourist sites—with the exception of Tiananmen Square and its immediate environs—have reopened, the situation has clearly not returned to normal. In Beijing, the military presence has been reduced but is still pervasive, with machine-gun carrying soldiers standing guard at most bridges and at many intersections, at many work units, and in Tiananmen Square. A curfew is still in effect, and cars are regularly stopped and searched at night. Gunshots can occasionally still be heard after dark, and rumors persist of both soldiers and citizens being killed. One group of US student tourists who dared to visit Beijing in July found their van stopped six times between the airport and their hotel.

Not only does Tiananmen Square remain closed to all but officially guided tourists, but pedestrians are not permitted anywhere near the square, and bicycles, cars, and buses are not allowed to stop as they pass by. While officially escorted tour groups may now obtain permission to visit the square, the first group (some 100 Japanese tourists) to take advantage of the opening was stopped and detained shortly after leaving the square by armed soldiers who boarded their buses and confiscated their film. Two who were reluctant to hand over their film were detained for several hours before being released. The NTA says that tourists are now permitted to take pictures in all sites that are open to foreigners, but explains that these orders are taking some time to reach the soldiers patrolling the streets. Foreign tour operators who participated in the NTA seminar found the square still scarred by burn and tank marks, slogans that had not been completely

TOTAL FOREIGN TOURISTS TO CHINA, 1979-88

	Total	Overseas Chinese	HK, Macao, Taiwan	Non-Chinese Foreigners	% Δ (Foreigners)
1979	4,203,907	20,910	3,820,602	362,389	
1980	5,702,536	34,413	5,138,999	529,124	
1981	7,767,096	38,856	7,053,087	675,153	
1982	7,924,261	42,745	7,117,019	764,197	
1983	9,477,005	40,352	8,564,142	872,511	
1984	12,852,185	47,498	11,670,420	1,134,267	
1985	17,833,097	84,827	16,377,808	1,370,462	+17.2%
1986	22,819,450	68,133	21,269,041	1,482,276	+7.5%
1987	26,902,267	87,031	25,087,415	1,727,821	+14.2%
1988	31,694,804	79,348	29,773,250	1,842,206	+6.2%

SOURCE: NTA

NUMBER OF FOREIGN TOURISTS TO CHINA BY COUNTRY

					% Δ		
	1985	1986	1987	1988	86/85	87/86	88/87
Japan	470,400	483,500	577,700	591,929	+2.7%	+16.3 %	+2.4%
US	239,600	291,800	315,300	300,900	17.8%	7.45%	−4.8%
UK	71,400	79,400	83,700	96,590	10.0%	5.1 %	13.3%
Australia	78,100	73,200	58,600	61,049	−6.7%	−24.9 %	4.0%
Singapore	46,500	48,600	64,100	65,413	4.3%	24.1 %	2.0%
W. Germany	43,100	48,200	60,100	69,007	10.5%	19.8 %	12.9%

SOURCE: NTA, China State Statistical Yearbooks effaced, and cloth ground into the pavement.

The situation outside Beijing is far more relaxed. Reports from participants in the recent CITS-sponsored familiarization trip suggest that the tour guides remain remarkably open and frank, that the atmosphere is free of any expression of xenophobia, and that travelers are facing no more than the usual snags. American embassy sources caution, however, that several tourist cities could soon become tense during the second, less publicly touted wave of the crackdown now underway. Xi'an, which experienced considerable violence during April and May, is expected to be particularly tense as arrests proceed. Shanghai, too, while calm on the surface, is likely to feel the effects of an intensified crackdown.

There are also the less obvious indications that things are still far from normal for tourists. Cable News Network (CNN) broadcasts, which formerly kept joint—venture hotel residents in touch with the world outside, have been suspended in Beijing, although not in other cities. All foreign newspapers and magazines, including the *International Herald Tribune*, *Time*, and *Newsweek* have been prohibited, leaving foreign tourists in China's capital with only the now highly censored *China Daily* for news. (The ban on foreign periodicals is not as well observed outside Beijing.) Some Beijing vendors said that distribution would begin again by the end of the summer, and some Beijing hotels have reportedly already begun to re-broadcast CNN. Airline passengers have been photographed by both camerapeople and by permanently mounted cameras as they go through entry formalities. Security personnel and cameras in hotel lobbies are also more in evidence now. While hotel staff often attribute the increased security to the need to protect foreign visitors against theft and unpleasant encounters, many Chinese believe it is an effort to prevent contact between Chinese and foreigners. While most foreign embassies remain guarded by the usual contingent of two or three pistol-carrying soldiers, the three buildings which comprise the American Embassy in Beijing are being patrolled by numerous machine-gun carrying soldiers. Furthermore, while official government statements encourage the return of foreign businesspeople and tourists, the propaganda presented to the Chinese is increasingly anti-American, with reminders of the "monstrous" but unspecified crimes the United States has committed against China. In this atmosphere, contact between Chinese, who fear getting in trouble, and Americans—even between longtime friends—is extremely difficult.

Roadblocks to recovery

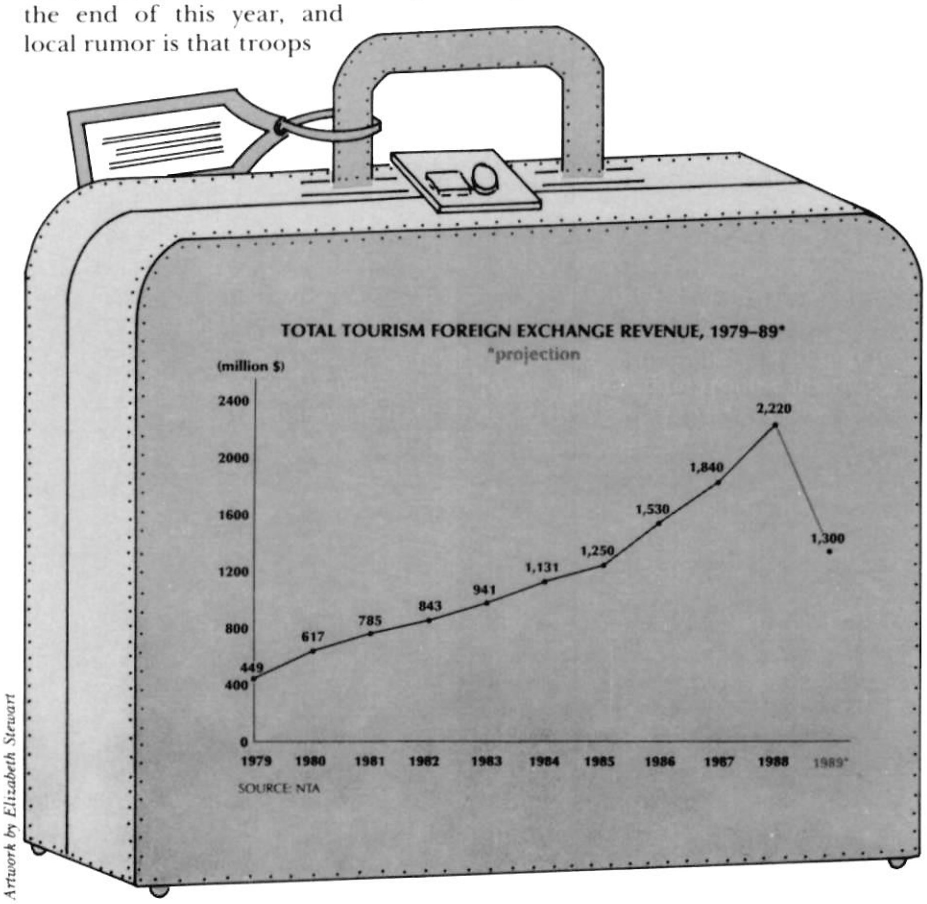
How long a revival of the Chinese tourist industry might take depends on several factors. A few adventurous tour groups, curious to see martial law in effect, have already begun to straggle in, and more will probably go this fall. The prerequisites for any revival of American tourism to China, however, are the end of martial law, or at least the removal of the military from the streets, and the lifting of the State Department travel advisory against visiting China.

Estimates about when martial law might end vary. Many believe that if the military withdrew now, the city would once again become ungovernable—so deep is the anger against the current regime. At a minimum, martial law will continue through Chinese National Day on October 1. Many believe it will continue through the end of this year, and local rumor is that troops will be here until after the end of the Asian Games in the fall of 1990.

American embassy officials in Beijing refuse to speculate on when the State Department advisory may be lifted, though they do not see it as linked to martial law and do not believe it will last indefinitely.

As long as the current regime remains in power, even the end of martial law and the removal of the travel advisory are unlikely to persuade American tourists to return to China in anything like the high numbers of 1987. The memory of the brutality with which China's democracy movement was crushed is not likely to fade quickly, and some proportion of potential tourists will resist contributing American dollars to a regime they regard as fundamentally repressive.

In addition, before a full recovery can be expected, Chinese tourism officials will have to make substantial progress in correcting the deficiencies, such as high prices and poor service, that had caused a decline in American enthusiasm for travel in China even before the events of May-June (*see* chart). Major changes in the scheduling and service on Chinese airlines and in Chinese airports are imperative. The on-time record of



Artwork by Elizabeth Stewart

the airlines needs substantial improvement, as does communication between the airlines and the passengers. Concerted attention must be given to the safety and comfort of passengers, and airport procedures need a major overhaul, beginning with the provision of luggage carts and porters for foreign tourists, many of whom are elderly. Guides need to be trained not only in language but also in etiquette and service. They should also be given basic courses in the culture and history of their country. Tipping guides for good service should be officially permitted, while at the same time every effort should be made to eliminate and prevent the corruption that currently pervades every level of the Chinese tourist industry. Major price reductions must also continue.

How quickly any of these conditions might be met ultimately depends on the stability of the Chinese government. The death of Deng Xiaoping, a major worsening of the current economic situation, or the collapse of the current political coalition could plunge the country into chaos, obviously bringing a stop to tourism as well.

Thus the prognosis for an early return of tourism in China to the level of 1987 is bleak. Recovery can be expected to take place in unevenly spaced spurts and will remain particularly sensitive to shifting political winds. Tourists will continue to come in a trickle until the State Department advisory is lifted, with the first spurt in American travel taking place after its removal. Tourist spots in the southern part of China, such as Guilin and Guangzhou, which were never greatly affected by the turmoil, will recover more quickly. Short tours organized through Hong Kong will be an important component of the tourist trade.

The second spurt in tourism is likely to take place after the end of martial law. But even if the political situation remains stable, and the influx of tourists increases at a steady pace, the high numbers of 1987 are not likely to be reached again until the fall of 1991. The special relationship that existed between China and the United States is not likely to return under the current regime, and rebuilding all aspects of the relationship—including tourism—will take time, patience, and level-headed sobriety. 完

HOW THE TOURISM SECTOR IS ORGANIZED

Realizing that tourism offers excellent potential to earn foreign exchange, the State Council decided in 1985 to include tourism development in the Seventh Five-Year Plan (1986-90). The Plan set a goal of 5 million non-Chinese foreign visitors and $3 billion in foreign exchange by 1990, and targeted key tourist areas for development, including Beijing (and part of Hebei Province), Shanghai, Guilin, Jiangsu (Suzhou, Nanjing, Wuxi, Changzhou, and Zhejiang), Hangzhou, Xi'an, Guangzhou, and Hainan Island. Since then, the key players in the industry have been reorganized several times.

National Tourism Administration

The National Tourism Administration (NTA) is the State agency charged with developing and implementing tourism policy. It was established under the current name in 1983, when CITS and the China Travel and Tourism Administration were separated into distinct commercial and governmental organizations; NTA is essentially a renamed, revamped version of the former Travel and Tourism Administration. A department directly under the State Council, NTA is currently headed by Liu Yi and in January 1989 was expanded and reorganized into 10 departments.

State Tourism Commission

NTA has long been hamstrung in its efforts to develop tourism, since many of the sector's needs cut across bureaucratic organizational boundaries. In order to lend coherence to tourism planning, the State Council last June created a State Tourism Commission, headed by Vice Premier Wu Xueqian, and composed of the heads of NTA; the State Planning Commission; the ministries of railways, construction, transportation, light industry, and culture; the People's Bank of China; the Construction Bank of China; the State Administration of Commodity Prices; the Civil Aviation Administration of China (CAAC); and the Overseas Chinese Affairs Office of the State Council. The commission develops basic policy and coordinates the work of the various departments that play a role in developing tourism.

Travel agencies

Until 1984, the tourism industry was heavily centralized and bureaucratic, and plagued by poor service. There were only three grade A travel agencies (those authorized to handle foreign tour groups)—China International Travel Service (CITS), China Travel Service (CTS), and China Youth Travel Service (CYTS), with CITS handling the lion's share of business. Grade B agencies may subcontract foreign business from grade A agencies, and grade C agencies deal only with domestic tourists.

To spur competition, the three agencies were decentralized in 1984, and the branch offices, formerly restricted to hosting trips arranged by the head office, were permitted to promote their services and sell tours independently. In addition, 13 new travel services were granted grade A status, and provinces, autonomous regions, municipalities, Special Economic Zones, and certain open cities were also permitted to establish travel agencies to contract with foreign groups, bringing the current total to 61.

The decentralization was intended to increase efficiency and service—not to lower prices, which are State-set. Fierce competition arose between head and branch offices of CITS, which still dominates the market. Branch offices are charged with illegally cutting prices up to 10 percent or promising extra services to gain customers. Some of the new travel agencies, including some in the grade B and C categories, tried to gain foreign business with creative but unorthodox marketing ploys, reportedly agreeing to accept payment in renminbi (RMB) or foreign exchange based on black market rather than official exchange rates. Branch offices also tended to lack the staff and ability to arrange accommodations or transportation in other cities, occasionally leaving tours arranged by foreign operators with no place to stay in—or no way out of—distant cities.

To stem the chaos and eliminate undercutting and intra-agency competition, CITS was reorganized into the China International Travel Service Group in March 1989. The group consists of the CITS head office, to which sole responsibility was restored for foreign bookings, and 120 branch and sub-branch offices located in provincial capitals and major tourist cities, which host the groups. Other national grade A tourist agencies were supposed to form similar groups, to compete for foreign customers against one another and with the provincial level grade A agencies, but given the current status of China's tourism industry, some of these agencies will undoubtedly be shut down. —PB

American travel-related companies are struggling to regroup and rebuild the China market

Picking Up the Pieces

Pam Baldinger

For US firms in the travel industry, the events of the last two months in China have been a nightmare. After spending a largely successful decade developing and promoting the China travel market, travel-related businesses were expecting in 1989 to welcome China's top tourism official to the United States to officially sign the Bilateral Tourism Agreement. Instead, they have watched China's robust tourism industry collapse virtually overnight, threatening to take a number of American companies along with it. At least three US tour companies specializing in travel to China are rumored to have already gone bankrupt, and many more are facing serious financial difficulties. Confronted with bleak short-term prospects, American companies in the travel sector—including tour operators, hotels, and airlines—are banding together to try to limit the damage and restore confidence in China as a travel destination.

Safety first

Following the imposition of martial law in Beijing, tourism levels to China decreased by about 10-20 percent in May. Although some US companies canceled a few departures, as long as the demonstrations were not violent, most trips took place as planned, with minor changes made to avoid hot spots like Tiananmen Square. Since the violence of June 4, however, the market has virtually dried up, with only a few tours trickling back during late July and August.

Initially, tour operators were preoccupied with safely evacuating staff and tour groups in China at the time of the Tiananmen massacre, with little concern for the financial implications of cutting trips short. Once all groups had been evacuated safely, however, travel companies were left with the thorny question of how to deal with future summer departures.

Refunds: cash, credit, and nonexistent

Concerned for the safety of their customers after Tiananmen, and faced with negative public opinion and a US State Department travel advisory strongly recommending that Americans avoid travel to China, tour operators immediately canceled numerous departures, with large, China-dependent companies such as Pacific Delight and InterPacific making decisions weekly, while companies with more diversified tour schedules canceled planned China trips for months ahead. Even for companies trying to hold off canceling peak fall departures, however, continued negative publicity and the travel advisory have nearly eliminated customer demand.

Mass cancellations, whether customer- or company-initiated, necessitated quick decisions about granting refunds for trips canceled or cut short. Most US tour operators, along with airlines and joint-venture hotels, agreed to issue full refunds with no penalties to their customers even before it was clear whether they themselves would be refunded by Chinese travel agencies.

Within two weeks after June 4, the China International Travel Service (CITS), through which most foreign companies book tours, announced that CITS would issue full refunds with no penalties on canceled tours or the unused portion of tours cut short. Such a favorable and quick response came as a great relief to operators forced to dole out large amounts of cash from their own coffers.

The CITS refund process has been anything but consistent, however. While some companies have received cash refunds, others have received only credit against future departures—an unattractive arrangement for many companies given both their immediate need for cash and dampened customer demand. In addition, other major travel-related enterprises in China, such as CAAC and shipping lines offering Yangtze River cruises, have not made similar offers, leaving companies that had already purchased tickets in the lurch. Furthermore, CITS has apparently told some companies that it will only refund canceled June-August tours, and that operators who cancel prepaid fall departures will be assessed penalties. Although CITS probably lacks funds to repay all its creditors, such tactics will undoubtedly cancel out the goodwill its previous announcement engendered, and tour operators may well set resolution of the refunds issue as a prerequisite to conducting any future business with China.

Writing off the season

Since fall is the peak travel season for most US tours to China, the June violence could not have happened at a worse time, effectively killing the season before it really started and offering no chance to recoup before its end. Most tour companies offered to rebook canceled passengers to other Asian destinations, though few report much success. "Most of our customers to China would rather wait a few years than go to other parts of the Orient to the exclusion of China," says Sidney Pease, director of product development for China, the Orient, and the South Pacific for American Express. Pease estimates no more than 30 percent of American Express's canceled passengers were rebooked onto other tours.

The allure China holds for such potential customers makes the US travel industry hesitant to simply write China off. A few companies, such as InterPacific and Oriental Clipper Travel, have offered special cut-rate trips at about one-half the usual fare, which were unexpected hits. "We closed the tour at 70

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people," says Gerry Kerr, vice-president of corporate development at InterPacific, "but we probably could have booked 100. I could not have been more pleasently surprised." Kerr acknowledges, however, that if the price is right, there will always be people willing to travel to any destination. But recovering the traditional market at normal rates is bound to take a while, as many potential China tourists cite moral reasons for refusing to visit China at this time, and large numbers are also frightened by the State Department's travel advisory.

The advisory has appeared in several forms over the last few months, and the latest version, announced August 9, still advises against "non-essential" (i.e., tourist) travel to China, placing companies offering tours to China in an awkward position and raising sensitive legal questions as well, as operators may apparently be held liable, if a customer is injured in China while a travel advisory is in effect. According to Amy Hendricks, legal counsel for the American Society of Travel Agents (ASTA), "The law in such situations is not clear or consistent and varies from state to state and court to court." Hendricks therefore recommends that while an advisory is in effect all companies should have their China-bound customers sign a waiver releasing the company from liability. Many companies, balking at the implication that they may put clients at risk, have canceled all tours through the end of 1989, in hopes that the advisory will be lifted by 1990.

Such long-term cancellations are bad news for hoteliers already confronted with room gluts in major cities. The drastic decline in travel to China has already led many developers to try to renegotiate contract terms and loan repayment periods for existing projects and put all future plans on hold. US airlines have been forced to reduce the number of their flights to China just as they were to negotiate for increased frequency during bilateral civil aviation negotiations held this summer.

NEW STRATEGIES FOR A NEW HOTEL

The managers of the China World Hotel and Traders Hotel were prepared to face a buyers' market upon opening in 1990, but we have had to revise our strategies to cope with new market conditions created by the events of May and June. For example, since the Traders Hotel is scheduled to open during the 1989-90 winter low season, we are considering revising our published opening rates and implementing a much stronger advertising campaign with a substantially increased budget. Furthermore, while typically both spring and fall are considered high seasons in China, the Traders' 1990 rate structure will likely include only one high season, during the fall, by which time we expect that the number of travelers to Beijing will increase.

Business travelers a bright spot

Although the average Beijing hotel occupancy rate was approximately 27 percent in July, most of the joint-venture hotels catering specifically to business travelers were operating at 25-50 percent. Given that this was a weak month immediately following the Tiananmen crisis, we see such levels as a good sign.

Over 70 percent of our designated target market for the China World and Traders hotels are business travelers, and as these are the first people returning to China, our market segmentation has not changed radically. Moreover, rather than basing their offices in China, a number of businesses have opted to temporarily use Hong Kong or other Asian cities as home bases and instead make periodic trips to Beijing. Consequently we see more business for hotels catering to the needs of business travelers.

Both the Traders and China World Hotels' initial marketing efforts will focus more intensively on the regional market than previously planned, as Asians—especially Japanese and Taiwan residents—seem to be returning sooner to China than Europeans or North Americans.

Group travel discounts

During this summer's unexpectedly low season, some—but not all— major Beijing hotels offered special discounts of 30-40 percent off published rates. Other hotels have featured complimentary breakfast, airport pick-up, or other incentives. Our surveys show that no joint-venture hotels in Beijing expect to drastically reduce their published room rates for the remainder of 1989 or for 1990. Only group travelers are likely to be offered significant discounts, as they will be the hardest market segment to reattract to China. Hotels competing for this business could slash prices by as much as 50 percent, as room rate reductions for tour groups may help make China a more attractive destination.

Uncertain prospects

It is too early to guage the effect of this summer's tensions on our 1990 market. Many new projects scheduled for completion during this time appear to be continuing, and our Conference and Exhibition Centre is negotiating six major 1990 international exhibitions. Ultimately, however, our success depends on China's political and economic climate—and we cannot predict the future.

—Al Wymann, general manager,
China World Hotel/Traders Hotel

What about 1990?

Many tour companies and most hotels, suffering substantial losses, have cut staff to help reduce expenses. New York-based Pacific Delight, for example, the largest US tour wholesaler to China, has lost over $20 million in revenue and reduced its staff by over 50 percent. Some tour operators have also lost thousands on brochures printed prior to June 4 and outdated overnight. The most pressing question for such companies is how—or whether—to market 1990 tours, as itineraries and brochures must be planned now. But since operators cannot predict what the political situation will be in China next year, planning 1990 itineraries is a tricky proposition, complicated by the fact that Beijing—China's top tourist destination—is virtually impossible to exclude from most itineraries. Yet as long as martial law remains in effect, tourists will be wary of visiting the city and may hold back from traveling to China altogether. According to Joseph Hallissey, deputy chairman of the international committee of ASTA, "martial law immediately says to people—don't go there."

Currently there does not seem to be any consensus on how to market China next year, with different companies adopting different strategies. Some, like Pacific Delight and InterPacific, will continue to market

China-only tours, at reduced levels, while others, such as the US-China People's Friendship Association, plan to offer China trips only in conjunction with other Asian destinations, so that China can be easily cut out of the itinerary if necessary. Still others are considering dropping China altogether in 1990.

One thing operators can be sure of is that the structure of the China market has changed significantly. Over the past several years, the China travel market had been growing increasingly sophisticated and diverse, with sub-sectors such as foreign independent travel (FIT), incentive travel, and special-interest travel growing far more rapidly than standard group tours, which still made up the majority of the market. In 1988, for example, FIT travel grew by 17.8 percent over the previous year, compared to only 1.2 percent for group travel. Given the current atmosphere, however, leisure travel will once again be overwhelmingly dominated by groups, while the incentive travel market has probably been wiped out for the foreseeable future. "We know the timing just isn't right now to promote incentive travel to companies," says Kerr. FIT travel, which last year accounted for 36 percent of total foreign arrivals, will be less significant, as the number of businesspeople and their dependents visiting China has decreased.

Taking action

Although traditional problems in China's tourism industry, such as pricing and service, will become even more important as foreigners eye travel there more critically, the greatest obstacle to rebuilding the industry is the public's negative perception of China's government and repressive political environment. The Chinese official line, that the "counter-revolutionary rebellion has been put down" and the government can guarantee the safety of "misled" overseas tourists—or compensate them $100,000—shows little understanding of American public opinion and the problems travel-related businesses face in trying to market China.

To help ensure that the Chinese clearly comprehend the obstacles to rebuilding American tourism to China and to display their commitment to the China market, a number of US tour operators, airlines, and hoteliers are forming action committees. The Travel and Tourism Committee of the US-China Business Council, for example, is sending a delegation to China in late September to discuss with top tourism officials how to overcome the obstacles to reviving American tourism to China. A group of primarily New York-based companies has recently formed the Temporary China Tourism Action Committee, also to help restore China tourism.

Some members of the industry, however, are skeptical about the chances of reviving tourism, even if the Chinese should adopt industry-specific suggestions, such as undertaking a massive promotional campaign and further cutting prices. As John Felber, editor of *American's Tourist Manual for the People's Republic of China* believes, "The problem is beyond the tour operator's ability to change. The problem is diplomatic; until relations between the United States and China improve and the advisory is lifted, I don't see how anyone can expect to revive the industry."

Waiting and hoping

Despite a fairly bleak overall picture, there have been a few positive signs. CITS's quick decision to provide price reductions of 20 percent through November and then 30 percent through next March, coupled with a rare 20 percent price reduction on internal CAAC fares, though probably insufficent in themselves to boost tourism, demonstrate that the Chinese recognize that it will take more than rhetoric to rebuild the industry. Moreover, the willingness of both Chinese tourism officials—who thus far seem unaffected by Party purges and reorganizations—and foreign companies to maintain links and contact should help speed the industry's recovery when the current tensions ease. Just how long that will take, however, remains an open—but all important—question. 完

Fertilizer's Greener Pastures

Chemical fertilizers are more plentiful, but obstacles still stand between the product and the farmer

Bruce Stone

Since the 1950s, when it almost exclusively used natural fertilizers, China has increased supplies of manufactured fertilizer faster than almost any other country in the world, by expanding both imports and production capacity. Now the world's largest user of manufactured fertilizers, China is again planning a decade of rapid growth. In 1987 alone, which saw a shift toward higher-quality products, China's fertilizer consumption rose 3.4 percent, and production increased 22 percent. In 1988, production grew by another 3.1 percent.

During the 1950s and early 1960s, the national and key provincial governments distributed the growing supply of fertilizer under their control with a certain degree of efficiency. During this period, the State limited the number of eligible users and allocated the chronically scarce supplies of fertilizer to farming areas with high yield potential. During the late 1960s and 1970s, small, county-owned plants provided the largest increments to aggregate supplies. This brought fertilizer use to a wider spectrum of localities and farmers, but growth was still concentrated in market-oriented areas with high-yield potential. However, during the late 1970s and 1980s, fertilizer availability began to grow so quickly that continued annual allocation of large quantities of fertilizers (especially nitrogen fertilizers) to the same areas became problematic, yet China was not able to direct the fertilizer to new areas. The resulting market crisis in 1985 left dozens of county governments with rapidly deteriorating inventories of volatile ammonium bicarbonate (ABC) products.

With the farm goods and fertilizer market in disarray, the government declared an import moratorium and scrapped plans for several new production facilities. However, central planners reconsidered their fertilizer policy when poor grain harvests followed this retrenchment. This situation was exacerbated by a rural credit crisis (*see The CBR*, January-February 1985, p. 43). The Agricultural Bank of China, created to facilitate government purchase of farm products, depends on rural credit cooperatives for the bulk of its deposits. The financial needs of the grain and cotton purchase stations—which disproportionately rewarded surplus deliveries—broke the Agricultural Bank after bumper harvests in 1983 and 1984. But with the Agricultural Bank closed, local credit cooperatives could not extend loans to farmers for fertilizer purchases, and farmers in many cases had trouble withdrawing their savings to buy fertilizer.

Just as sustained rapid growth in foodgrain and cotton production overloaded and rendered obsolete China's scarcity-oriented farm goods purchase system, a decade of very rapid growth in production and imports of fertilizer overloaded the fertilizer purchase, allocation, and distribution systems. In both cases, administrative headaches caused by sustained successful production precipitated the sudden introduction of reform measures, including contract systems, which replaced unlimited commitments by the State to purchase.

Comprehensive improvements

China's Seventh Five-Year Plan (FYP, 1986-90) shows a vigorous recommitment to rapid development of domestic fertilizer production capacity and implies continued willingness to allocate large quantities of foreign exchange for fertilizer imports. Ambitious production targets also characterize plans for the upcoming Eighth FYP (1991-95), although financing arrangements for large-scale capacity expansion and appropriate policies to ensure adequate input supply to the small-plant sector are not yet well established.

In addition to commitments aimed at increasing supplies of fertilizer, China has undertaken a series of initiatives to promote wider availability and greater returns to fertilizer use. These measures include increased fertilizer distribution by plan to medium- and low-yield areas; various efforts to achieve greater allocational efficiency through limited operation of markets; extensive soil testing and diversification of fertilizer production to counter soil deficiencies and fulfill crop needs for balanced nutrients in various regions; new encouragement of small-plant production; and better control of fertilizer quality.

Ambitious expansion goals

Following a major commitment of financial resources to import 13 large synthetic ammonia/urea complexes in the early 1970s (eight of them from America's M.W. Kellogg Co. or its European joint venture), investment in new capacity was allowed to decline, leading to a fall in

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additions to capacity during this decade. But the perceived benefits of increased fertilizer application during the 1965-84 period and the inability to control farmer allocation of surplus grain for feed ultimately encouraged planners to commit more resources to fertilizer production in the Seventh FYP (*see* chart 1). Expected additions to capacity include 11 new medium- and large-scale diammonium phosphate (DAP) plants, two plants to produce compound fertilizers (NPK), and one large potassium chloride complex. Complete production lines for perhaps eight of these facilities will be in operation by 1990-91. By November 1987, a nitrophosphate plant and three other facilities for producing DAP or NPK had been added to the list of upcoming projects.

In 1988, a single superphosphate plant with 400,000 metric tonnes per year (tpy) capacity was completed in Gansu; large synthetic ammonia/urea complexes were opened in Ningxia and Xinjiang; and a 300,000 tpy synthetic ammonia plant was opened in Shanxi. The status of the remaining facilities for the 900,000 tpy nitrophosphate plant in Shanxi and a 120,000 tpy ammonia phosphate plant in Shaanxi, both scheduled for 1988 completion, is unconfirmed. A phosphate plant scheduled for completion in Anhui last year is expected to start up in 1989, along with new ammonia phosphate production capacity in Liaoning and Nanjing. In addition, at least five medium-scale plants are being converted for production of urea and DAP, as are 30 smaller ABC and single superphosphate plants, with an additional 70 being planned. The Qaidam Basin facility in Qinghai is expected to produce 140,000 tonnes of potassium chloride and 80,000 tonnes of magnesium chloride this year.

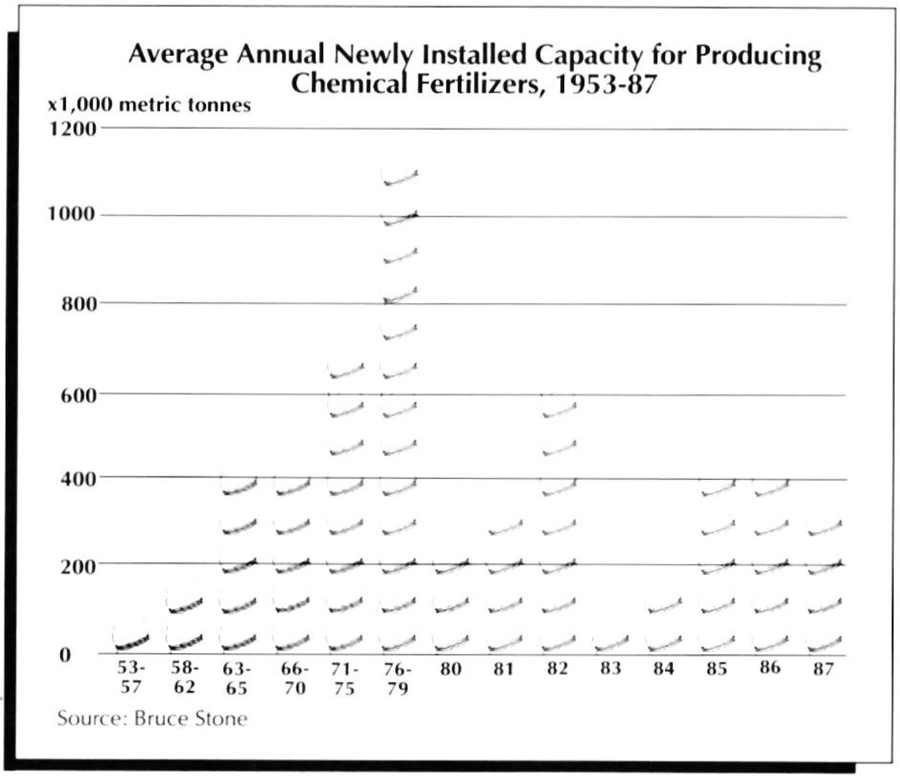
With capacity expansion proceeding with some speed at the medium- and large-scale facilities, attaining the production goal of 100 million tonnes within a year or two of the original 1990 target date is not out of the question, particularly if adequate raw materials and energy can be guaranteed to the small-plant sector. The production goal for 1995 was raised last summer from 120 million standard tons of product to 130 million tons, with 150 million tons, or approximately 32 million tons of nutrients, targeted for the year 2000.

Detailed plans for the Eighth FYP, however, seem to be changing almost monthly. In 1988, they included completion of 10 large DAP projects. But financing still poses a major obstacle; the year-2000 target would require an annual rate of construction investment 4.5 times the current level, if achieved primarily via large-scale plants. Recent cutbacks in capital construction plans coupled with credit restrictions to address inflation, will further impede domestically financed capacity. International organizations are helping a little, and some foreign governments, particularly Japan's, are providing assistance. But despite recent reforms, Japanese assistance has typically been organized around Japanese industrial ability to provide nitrogen production facilities, whereas higher proportions of phosphates and potash will be required in China's future. In any case, continued high levels of production and even capacity expansion in the small plant sector are probably indispensable if China is to reach the year-2000 targets.

Surpassing expectations

With a boom in capacity utilization within the small-plant sector and a portion of the capacity expansion planned in the Seventh FYP coming onstream, domestic fertilizer production reached record levels for each of the major nutrient groups in the late 1980s. In 1987, total production surpassed the State plan by 14 percent, leading to a substantial upward revision in the 1988 target. Nitrogen production in 1987 totaled 13.423 million metric tonnes, 16 percent over 1986 and 11 percent higher than the record 1984 total. Phosphate production was up 39 percent over 1986, to 3.259 million tonnes, surpassing the 1983 record by 22 percent. And potash production, though still small relative to requirements, grew 60 percent, to 40,000 tonnes, surpassing the 1984 peak by 29 percent.

According to preliminary compilations, nitrogen fertilizer production grew 1-3 percent in 1988 and phosphate by 17-23 percent. The industry as a whole recovered from raw material and energy shortages during the summer to exceed even 1987 production (by 3-7 percent) as well as its initial production target, but may have remained almost 2 percent short of the ambitious 1988 revised target of 85 million standard tons. Furthermore, production problems in the small nitrogen plant sector in the late spring of 1988 spread to the small phosphate sector by early 1989. While there was some recovery in the nitrogen sector by early spring this year, complete resolution is no doubt being delayed by the political crisis following the pro-democracy move-



Artwork by Steve Fleshman

ment in May-June.

Preliminary production figures for the first six months of 1989 showed a respectable increase (to 42.98 million tonnes or 9.05 million tonnes of nutrients), but the large gap remaining to reach the 1990 target is evidence of both incomplete resolution of small-plant problems and delays in large-plant completion.

Surge in imports

The reacceleration in production in the late 1980s was not accompanied by a cutback in imports (*see* chart 2). As was the case during most of the 1977-84 period, fertilizer imports grew rapidly along with domestic production capacity. In 1987, China's fertilizer imports (10.9 million metric tonnes of product, or around 4.7-4.9 million tonnes of nutrients) rose 18 percent over peak year 1984 and 114 percent over the 1986 level, which had been artificially restrained by an import contract moratorium commencing in the second half of 1985. Preliminary compilation of 1988 imports suggested an 18 percent increase over the record 1987 level in nutrient terms, but the final figures released by China's Customs Bureau actually show 14.7 million tonnes of product weight imports, for a 35 percent increase. These figures imply imports of around 6.6 million tonnes of nutrients and a considerable increase in last-quarter deliveries. Yet even with this replenishment of inventories, 1989 imports may not be reaching adequate levels to compensate for production and distribution problems, compounded by the government's distraction by other issues, including the possibility of major policy revisions. But China's leaders will inevitably realize that increasing fertilizer imports to support good harvests will assist any government's effort to secure or maintain legitimacy.

Promoting grain gains

Increased applications of fertilizer in the late 1980s restored harvests that had suffered from the 1985-86 import restraints and from confusion in the farm goods, fertilizer, and credit markets. Following a 1986 increase in fertilizer supplies, foodgrain production in 1987 recovered 3.4 percent to 404.73 million tonnes, within 0.64 percent of record year 1984, despite a decrease in foodgrain sown area of 1.43 percent. Paddy production recovered to within 2.2 percent of peak year 1984, when sown area was 3.1 percent greater. Corn and soybean production reached new output records, and sweet and white potato output grew 11.4 percent over 1986, reflecting a movement of both land and fertilizer resources toward the country's most land-efficient major feed and industrial crops. Complementing substantial developments in water control and extended use of high-yielding crop varieties from 1950-80, increased fertilizer supplies—not prices, incentives, or the responsibility system—were primarily responsible for the remarkable performance in foodgrain production during the last decade, from 285 million tonnes (1975-77) to an average of 400 million tonnes (1987-88) (*see* chart 3).

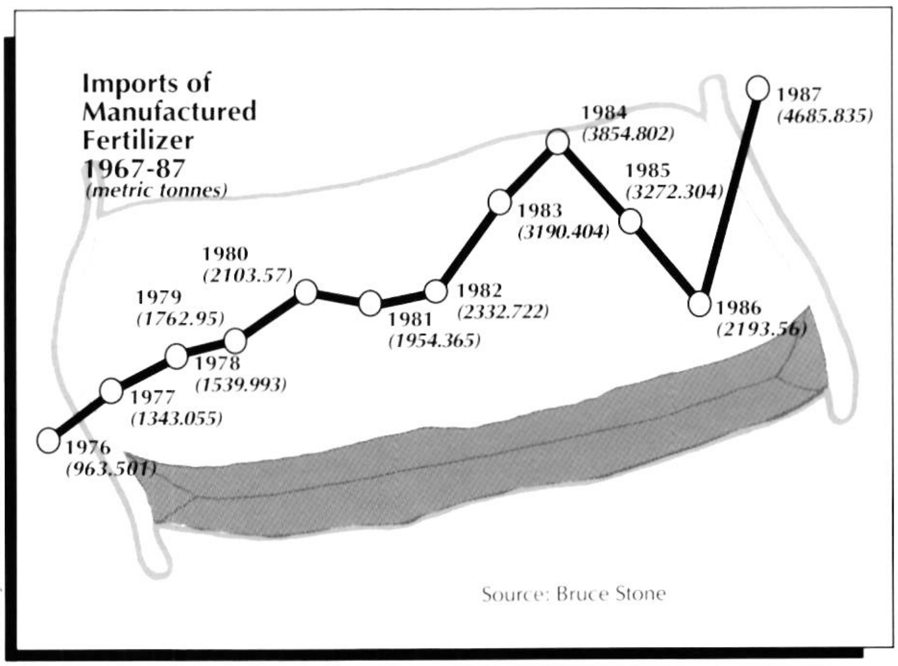
Increased fertilizer application also partially compensated for the negative effect of unusually severe natural disasters on national foodgrain output in 1988. Although droughts in central China and floods throughout the northeast kept foodgrain production from reaching 1984's record of 407 million tonnes, timely and plentiful fertilizer supplies provided bumper harvests elsewhere, allowing the national grain harvest to reach 393.79 million tonnes in 1988, surpassing the target of 390 million tonnes. At the same time, growth in fertilizer use has been instrumental in generating rapid and continuous growth in crop value for non-grains during the last decade.

Conversely, inadequate production of fertilizers by the small-plant sector, insufficiently offset by imports, could, if left uncorrected, begin to have noticeable aggregate impact on output beginning with the 1989-90 over-wintering crop.

Redirecting supplies

During the early decades of severe fertilizer supply shortage, throughout even high-potential farming areas, country and provincial governments restricted access to high-quality fertilizers to farmers who sold large quantities of agricultural goods to the State. China's system of distribution ensured that dynamic farming areas would receive increasing supplies of fertilizer to continue growth of farm yields, secured high average returns to fertilizer application, and guaranteed the State's ability to purchase large shares of the increments to food production from growing fertilizer use.

With rapidly increasing fertilizer supplies, however, the advantageous system of concentrating incremental supplies of fertilizer in the same market-oriented areas became a liability, as more and more fertilizer was directed to localities with farm yields already approaching their potential or at least experiencing rapidly declining marginal returns to nitrogen use. Lower-yield areas, on the other hand, that might have benefited substantially from more nitrogen fertilizer, were unable to obtain supplies. Skewed distribution



Source: Bruce Stone

Artwork by Steve Fleshman

of specific fertilizers has also exacerbated soil nutrient imbalances.

China is now working to correct these imbalances by making more fertilizers—especially nitrogen—available to low- and medium-yield areas and providing more phosphates, potash, and micronutrient fertilizers to areas already receiving plentiful supplies of nitrogen products. Both efforts are essential.

Balancing nutrients

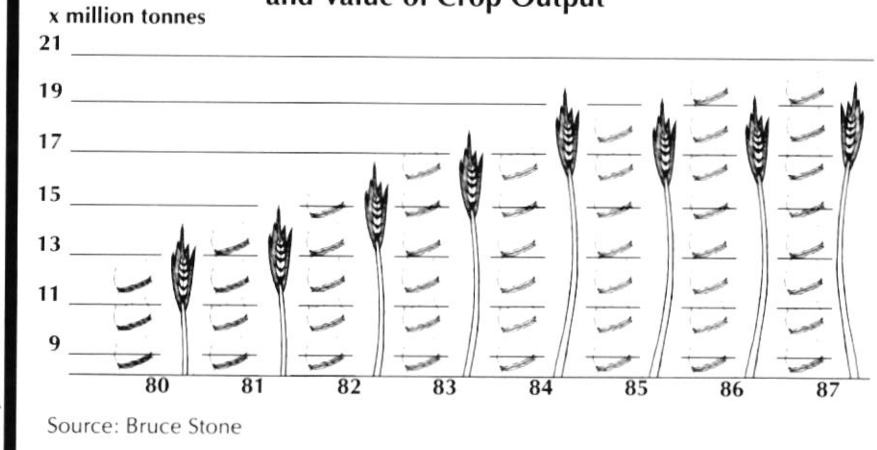
Soil nutrient deficiencies, which have held back yields in many farming regions, are only partly due to uneven distribution of fertilizer. The application of fertilizer overall has not been sufficient to prevent nutrient depletion, and capacity investment and import policies have historically stressed nitrogen fertilizers, neglecting phosphates and especially potash (*see* chart 4). As a result, growing deficiencies threaten to hinder future harvests and are already raising the per-unit costs of continued yield growth in high-application areas.

According to national tests done in 1981-83, almost all Chinese soils are deficient in nitrogen, and soils throughout 73.4 percent of the country's cultivated farmlands lack phosphate, including 54.2 percent with serious deficiencies. Potash deficiencies are found on 23-47 percent of the farmlands, depending on how the deficiency is defined. According to a study by the Soil and Fertilizer Institute in Beijing, fertilizer application targets for the year 2000, even if fulfilled, would not eliminate net annual losses in major soil nutrients.

The Chinese Academy of Agricultural Sciences estimates that China's appropriate application ratio of nitrogen to phosphate to potash—the NPK ratio—is 1:0.5:0.2. Some Chinese scientists suggest a preferable ratio of nitrogen to phosphate would be as high as 1:0.7, while others argue that 1:0.4 will be adequate during the 1990s. Applied nutrient ratios in none of China's provinces fall within this range; only Heilongjiang and a few other low-application provinces where use of *all* nutrients is deficient are approaching the preferred ratios.

Aware of the problem, China has established a national soil test network and surveyed soils in almost all counties. The basic information from such tests is being made available to

Application of Manufactured Fertilizer and Value of Crop Output



Artwork by Steve Fleshman

local planners and, increasingly, to farmers. China has also begun to shift emphasis toward phosphate and potash fertilizers. By preliminary estimates potash imports rose by two-thirds in 1988 to a new record of 1.35 million tonnes, some 25 percent greater than the 1984 record. About 200,000 tpy of domestic potash production capacity should be completed by 1990. Both mining and production capacity for phosphates is undergoing rapid, though unsteady, development (*see* box).

Encouraging small plants

China's recent decision to resume limited encouragement of small-scale fertilizer producers partially reverses a decade-long campaign aimed at controlling the growth of this subsector and weeding out the least efficient plants. Some planners at the national level would prefer to do without China's 1,800 small plants, which have nevertheless provided a useful supplement to large- and medium-scale facilities and have protected many local economies from the vagaries of policy regarding foreign exchange allocation for imports and State and provincial allocation of fertilizers.

Despite periodic central government opposition during the last decade, local governments have continued to develop small-plant capacity. Small plants accounted for around 10-11 million tonnes of nutrients in 1987, including roughly 7-8 million tonnes of nitrogen and 3 million tonnes of phosphates. The small-plant nitrogen sector reportedly has the capacity to produce more than 8.2 million tonnes of nutrients.

Pressure from local governments and recognition that a healthy small-plant sector would inevitably continue to be key to achieving agricultural targets finally resulted in a change in both strategy and tactics toward small plants. China now not only permits the sector's development but also provides a portion of the investment and technical assistance necessary for a number of facilities that currently produce volatile, low-quality ABC to convert to DAP, MAP, or urea production. The Seventh FYP provided ¥1 billion to local plants to partially support capacity expansion and conversion from ABC to urea, despite efficiency potentials substantially below those for larger-scale facilities. The largest portion of investment required for such conversion or expansion, however, must be raised locally.

Marketing reforms

Marketing reforms predated the attitude adjustment toward small plants. The immediate catalyst was the inability of the State's bureaucratized distribution system to handle continuous growth in supply, particularly during a crisis in rural finance. In 1985 small- and medium-scale ABC plants were forced to organize marketing for up to 50 percent of their output. Until that time, such plants sold virtually all their output to the local branch of the Agricultural Inputs Corp. (AIC). The AIC distributed it, along with fertilizer purchased from outside the county, to local marketing and supply cooperative outlets and, to a minor extent, to AIC branch offices in other counties, all ostensibly according to annual allocation plans drawn up by the local planning commission in consultation with agricultural departments.

As part of the deal, provincial and local governments were supposed to hold down official intra-county factory fertilizer prices but could negotiate prices elsewhere. However, provincial and national governments would guarantee only a portion of required inputs at preferential prices. Plants would have to arrange purchase for the remainder themselves, at prices to be negotiated with suppliers.

In addition, the government legalized fertilizer trade among farmers. This move allowed farmers, legal distributors, and farm produce purchasers to recapture a greater share of former—and substantial—black-market profits. China also attempted to resolve some of the most severe geographic imbalances in fertilizer use within regions by permitting plants to sell their surplus anywhere within the country at negotiable prices.

Bureaucratic recentralization

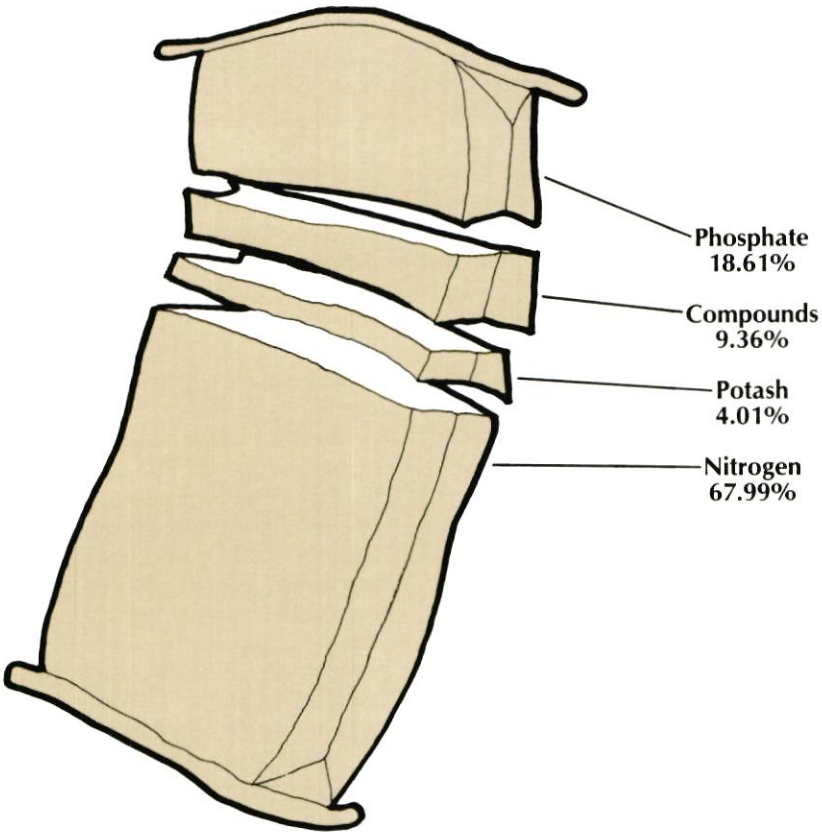
To better control the fertilizer trade, China in the mid 1980s recentralized imports through the China National Chemicals Import and Export Corp. (SINOCHEM). In October 1987, the government attempted to recentralize the domestic fertilizer trade through the AIC, an organization better equipped than factories and farmers in warehousing, transport, and communications facilities to market and distribute fertilizers. But the intrinsic responsiveness of AIC outlets to local government and the structure of incentives related to their operation suggest that this recentralization of trade is as handicapped in improving allocative efficiency as the previous arrangement.

The recentralization of fertilizer imports was ostensibly undertaken to prevent unscrupulous traders and criminals posing as traders from taking advantage of unsophisticated local governments and farmers and to prevent irresponsible local authorities from contracting for excessive imports. But the recentralization has not eliminated imports through non-SINOCHEM channels, only reduced their flow and made such flows illegal. And by reducing competition from legal suppliers, especially those operating most directly from foreign sources, leverage to extract exorbitant prices is increased in the hands of corrupt officials, resource-hungry local governments, and the smaller and less responsible corps of illegal traders. The answer to this problem is wider, not narrower, local access to alternative suppliers.

There is no question that both imports and domestic production had increased at rapid rates since the late 1970s. But there is no evidence that the rate of increase in early 1985 was excessive relative to previous years and no evidence of building stocks of imported products. There were, however, accumulating inventories of ABC at some AIC locations, which prompted local outlets to reduce further purchases of ABC from local plants. Small plants, however, with only a few production days of warehouse capacity, were even less equipped to handle inventory buildups, and many ceased operation. The national government, fearful of permanent deterioration in the idle nitrogen plants, eventually ordered them to resume production.

The attempted and partially successful recentralization of imports, the 1985-86 import contract moratorium, and the market reform allowing local plants to sell their output directly once local AIC quotas were fulfilled all arose out of this situation. While local plants had a hard time initiating their fertilizer marketing activities on short notice, when the reform was introduced in 1985, they seemed to have little trouble in 1986 after several months of preparation, and even in 1987, when imports recovered to record levels. There were cases of substantially higher prices charged to farmers, but on the whole, price increments required for fertilizer to reach demand surplus localities were modest, and exceptionally high prices were no higher than previous black market rates. If anything, the exploitation of farmers with extremely high prices or by shorting their contracts seems to have accelerated along with attempted recentralization.

China's Nutrient Application Proportions, 1986



Artwork by Steve Fleshman

So why is recentralization of domestic distribution deemed necessary? There seem to be several reasons. First, when fertilizer plants sell directly to townships in other counties, as well as to county AIC offices themselves, they are generally taking over existing markets from higher-cost local producers. This naturally irritates plant managers and county governments accustomed to controlling local supply, although distribution alternatives usually exist: exporting to markets served by even less efficient producers and developing the distribution system and marketing arrangements in more remote areas of the county where fertilizers are scarce. National and provincial planners cannot have it both ways. If markets are to be expanded to remote areas, there probably must be considerable supply pressure. If markets are to raise production and allocative efficiency, unwelcome pressure on high-cost suppliers is inevitable. In any case, greater quantities of fertilizer provided by competitive suppliers is the only final answer to exploitation of farmers through exorbitant fertilizer prices.

But a more fundamental State concern is that freer access to fertilizer means less leverage over farmers, considered necessary for a variety of reasons. Farmer compliance with local and national government policy has been an important constraint on administrators for at least 15 years. Control of access to fertilizers is one of the only—and often the most important—means to secure compliance. Of course, it also allows large additional charges on deliveries to be assessed with impunity, for either private or public gain. While the national and provincial governments emphatically oppose illegal accumulation, they inevitably depend on the cooperation of the local elites.

There is the illusion that with fertilizer distribution recentralized through the AIC, responsibility will be established, and illegal price escalation or diversion of fertilizers can be identified and eliminated. But this has not proven to be the case. As efforts to recentralize have intensified in 1987-89, problems in fertilizer distribution have increased, not abated. The crux of the difficulty is that county branches af the AIC are more responsive to county governments than to the provincial and national AIC leadership. And county governments operate with increasing independence, especially during periods of national and provincial budget retrenchment.

Finally, the national government has typically preferred limiting foreign exchange expenditures on agricultural goods and inputs. Recentralizing distribution underwrites the attempted recentralization of imports, which, it is hoped, will help the State gain greater control over foreign exchange expenditures for fertilizer.

THE FUTURE IN PHOSPHATE

After a decade of struggling to fill an urgent need for nitrogenous fertilizers, China is now turning its attention to two categories of less used but equally important nutrients: phosphate and potash. China's imports of these fertilizers, as well as construction of plants to produce them, may provide US companies with the major channel for market growth in the 1990s.

For generations, Chinese farmers relied on manure, oil cakes, and night soil, as well as crop rotation and cultivation of "green manure" crops, to replenish the minerals depleted from the land by farming. These practices gradually leached out the soil's nitrogen content, and when chemical fertilizer came into use in the 1950s, the land responded to nitrogenous fertilizers with dramatically higher yields. Application of manufactured fertilizers in China from 1970-87 rose from about 3 million to 20 million tonnes of nutrients per year, with nitrogen forming the great majority of the fertilizers applied.

Higher yields from land fertilized with nitrogen, however, masked a slow drain of other nutrients, particularly phosphate and potash, which eventually inhibited crop response to nitrogen. Chinese scientists estimate the optimal ratio of nitrogen fertilizers to phosphates at 1 to 0.4-0.7, but current ratios average a much lower 1:0.27.

Until recently, production of phosphates was limited to small producers, with little central government involvement. However, large-scale production became feasible with recent advances in beneficiation—a process for extracting usable rock from the layers of sand and clay that couch most of China's abundant but low-grade phosphate deposits. Underway in the Seventh FYP (1986-90) are projects to develop five large new phosphate mines and several small ones, partly aided by a $62.7 million World Bank loan. Output at four pyrite mines will be increased to fill a need for sulfuric acid, which is an ingredient of high-quality phosphate fertilizers. These raw materials will feed several new production facilities opening in the Seventh and Eighth FYPs, with the goal of increasing phosphate production capacity by 1.54 million tonnes per year (tpy) of nutrient weight by 1993. Currently China produces about 3.5 million tpy of phosphate.

The China National Chemical Construction Corp. has begun discussions with the World Bank on another batch of projects, which could include development of three phosphate mines and construction of fertilizer installations. In total, planners hope to raise capacity to 9 million tpy of pure phosphate fertilizer by the year 2000.

However, experts on China's fertilizer industry believe China will continue to depend on imports to supplement domestic production through the mid 1990s. Already the United States' biggest phosphate customer, accounting for 32 percent of US diammonium phosphate (DAP) sales in 1988, China may continue looking to US exporters to supply its growing need.

In plant construction, China is working to build facilities for the manufacture of DAP, which supplies both nitrogen and phosphate to the soil, and new plants will almost certainly seek internationally experienced consultancy.

In the longer run, China could become an importer of phosphate rock, which the United States has in plentiful supply. Although China's phosphate deposits are large, most lie inland, far from the plants being built along the east coast, suggesting that imports may become cost competitive with domestic rock. "In the United States we have probably the lowest-cost production of phosphate located close to the water," says John Douglas, president of the consulting group Douglas Associates.

China's need for potash, which now accounts for only 2.3 percent of total fertilizer consumption, is also chronic, but the United States, which imports about 88 percent of its potash, is unlikely to capture this market. Chinese importers will probably turn instead to Canada, where potash deposits are virtually unlimited.

—ASY

FERTILIZER GLOSSARY

▶ *Nitrogen*

Garbage, sewage, and manure are natural sources of nitrogen, but most nitrogen fertilizers come from synthetic ammonia, often converted into salts, such as **ammonium sulfate, ammonium nitrate, monoammonium phosphate (MAP)**, and **diammonium phosphate (DAP)**. Tests conducted in 1981-83 indicated that all Chinese soils were deficient in nitrogen. Given proper moisture, corn, wheat, and rice respond very well to applications of nitrogen fertilizers.

Most nitrogenous fertilizer plants in China are small facilities, each producing 3,000-5,000 tonnes per year of fertilizer. Almost all produce ammonium bicarbonate, containing 17 percent nitrogen. Some also produce ammonium nitrate or ammonium chloride.

Ammonium bicarbonate (ABC): More than 1,000 plants in China produce this low-quality fertilizer, from which the average uptake of nitrogen into the soil is only 28 percent, as opposed to 43 percent for urea. ABC deteriorates quickly, which causes storage and shipping problems. China sustained immense losses of ABC as a result of inventory accumulation during the market difficulties of 1985.

Metacresol: a colorless, poisonous, isomeric phenol obtained from coal tar and used in organic synthesis, especially in making urea.

Urea: One of the most efficient sources of nitrogen, urea, also called carbamide, is a soluble, 46 percent nitrogen compound that is expensive to produce but convenient to transport and use because of its solid form. China imports about 1 million tonnes per year of urea, or roughly half of overall consumption.

▶ *Phosphates*

Obtained from phosphate rock or bones, these phosphorous-yielding fertilizers have been especially effective for corn, wheat, and millet. The fertilizer most commonly produced in small phosphate plants—which account for more than 95 percent of China's phosphate production—is calcium phosphate, containing 12-14 percent phosphorous pentoxide.

Calcium magnesium phosphate (CMP): a low-quality, low-nutrient fertilizer made principally in small plants.

Diammonium phosphate (DAP): a high-grade fertilizer that provides both nitrogen and phosphate nutrients to the land. DAP manufacture requires sulfuric acid, most of which China imports from abroad. The United States exported 2 million tonnes of DAP to China in the 1988 fertilizer year, which runs from July through June, accounting for 32 percent of total DAP exports from the United States.

Single superphosphate: More soluble than calcium phosphate, superphosphate is obtained by treating calcium phosphate with sulfuric or nitric acid. The final product contains 12 percent each of nitrogen, phosphoric acid, and potash. Although China has abundant supplies of phosphate rock, much of it is not suitable for manufacturing fertilizer, and sulfuric acid is in short supply.

Triple superphosphate (TSP): China now imports virtually all of its TSP, a highly concentrated fertilizer, with 46 percent P_2O_5. China's 1988 TSP import figures are not yet available, but 1987 imports totaled 229,800 tonnes.

▶ *Potash*

The most common fertilizers mined from potash deposits are potassium chloride and potassium sulfate. Although potash production in 1987 nearly doubled the 1986 figure, bringing the total to 50,000 tonnes, this represents only a fraction of China's low consumption: In 1987 China imported 1.78 million tonnes of potassium sulphate and potassium chloride, the two major potassium fertilizers.

SOURCE: Council files

Plant closures

By the second half of 1988, China's inflation rate had accelerated to around 30 percent, which, coupled with aggregate shortages of coal, natural gas and electricity, led to rapidly escalating prices for these inputs to small nitrogen plants. But with recentralization of distribution through AIC channels, the opportunity for small plants to cover additional expenses with higher incremental charges for fertilizers was considerably inhibited. Consequently, the number of plants operating in the red increased from 122 in 1987 to 272 by September 1988. Many plants operated well below capacity due to lack of capital to finance the higher prices, or else to sheer inability to secure the inputs or freight transport permits. In many cases, even the government-guaranteed input levels were not supplied. By January 1989, almost 400 medium- and small-scale plants had ceased operation. Several interrelated factors contributed to plant closings: the inability to procure adequate coal, electricity, natural gas, sulfuric acid, and freight transport, and the economic bind of inconsistent price and allocation policies.

A number of small factories have seen the handwriting on the wall—in the world of frequent policy change and partial regulation, fertilizer ex-factory prices will be under greater regulatory pressure than input and transport prices. Their response, when possible, has been to diversify horizontally into manufacture of other products whose output prices are apt to be under less downward pressure from governments. This of course exacerbates production shortfalls in fertilizer facilities, with more profitable production lines competing within the same company for similar scarce inputs.

The situation worsened after the 1988 autumn harvests, and the Ministry of Chemical Industry took up the matter in urgent terms with the State Planning Commission, which responded with emergency directives to provinces to provide priority guarantees of coal and electricity to small plants, prevent further closures, and reopen idle plants to avert permanent deterioration. Local response, while less than ideal, seems to have been significant. In Jiangsu, 29

FOREIGNERS IN FERTILIZER

Foreign companies have been highly active in China's fertilizer business since the late 1970s. Below is a partial list of agreements made to date.

United States

• **1973-present:** The **M.W. Kellogg Co.**, formerly a subsidiary of Pullman; now part of Dresser Corp.

Since 1973, Kellogg and its European joint venture have designed and engineered nine ammonia/urea plants, upgraded five plants, and engineered energy-conservation retrofitting at three plants. In 1986 Kellogg formed a joint venture with the China National Petrochemical Corp. (SINOPEC) in Lanzhou, Gansu.

• **1986: Jacobs Engineering Group Inc.** won contracts to complete studies on three phosphate mines in China to determine whether the deposits were suitable for fertilizer production.

Calma Co., then a subsidiary of **General Electric Co.**, signed a $1.4 million contract to supply CAD systems for the 1985 World Bank Fertilizer Rehabilitation Project.

Permea Inc., a division of **Monsanto**, signed a $3.5 million contract to supply gas separators to recover hydrogen at a refinery in Shandong, as part of the Fertilizer Rehabilitation Project.

Phos Chem Co., with Hong Kong's Sinochem International Oil, signed a $2.6 million contract to provide 12,000 tonnes of fertilizer.

Transamerica Delaval Inc. signed a $2.1 million contract to supply equipment to upgrade the Luzhou Natural Gas Chemical Plant in Sichuan Province, as part of the World Bank Fertilizer Rehabilitation Project.

• **1987: Cooper Energy Services International** signed a $1.1 million contract to provide an air compressor as part of the China Fertilizer and Energy Saving Project.

Worthington Compressor signed a $1.6 million contract to provide a compressor to the China Fertilizer and Energy Saving Project.

Xytel Corp. signed eight contracts worth $3.8 million to design and construct computer-controlled pilot plants for energy and fertilizer research.

• **1988: Impex Group Ltd.** sold chemical fertilizers to China.

• **1989: USX Corp.** sold parts of its phosphate fertilizer business to SINOCHEM's US affiliate. The business consists of phosphate fertilizer production and marketing operations in Florida and Atlanta.

Canada

• **1984: Canadian Potash Exports Ltd.** exported 750,000 tonnes of potash and planned to export 5 million tonnes in 1985-90.

• **1985: Novacorp International Consulting Ltd.** was awarded a contract to design a gas pipeline to Cangzhou Fertilizer Plant in Hebei.

• **1987: Canpotex Ltd.** agreed to provide 500,000 tonnes of potash for fertilizer at $31.8 million.

Denmark

• **1986: Haldor Topsoe** signed a contract to reconstruct an ammonia plant, for $4.4 million.

Finland

• **1986: Kemira Engineering** was awarded a contract to supply $7.8 million of fertilizer.

France

• **1985: Laboratoires Goemar** signed a joint-venture agreement with a Shandong concern to develop a factory that could make fertilizer from seaweed and algae.

• **1987: Technip Co.** agreed to provide equipment worth $90 million to a Sichuan plant.

Spie Batignolles was awarded a contract to build a Sino-Arab joint-venture fertilizer plant in Qinhuangdao.

Hong Kong

• **1986: China Resources Machinery Co.** signed a contract to supply wire, steel channels, and other equipment for the World Bank Fertilizer Rehabilitation Project.

Indonesia

• **1985:** Shipped 10,000 tonnes of urea. $1.29 million.

Italy

• **1987: FBM Hudson Italiana Spa** signed a $2.1 million contract to provide high-pressure heat exchanges for a urea plant.

Japan

• **1984: Japan Urea & Ammonium Sulfate Industry Association** signed a $21.3 million agreement to ship 130,000 tonnes of urea and ammonium sulfate.

Six Japanese partners agreed to provide 100,000 tonnes of urea.

• **1986: Mitsui & Co.** signed an $840,000 contract to sell 4,000 tonnes of phosphate fertilizers.

• **1987: Sumitomo Corp.** was awarded a $3.3 million contract to provide compressors to the Fertilizer Development Project.

Mitsubishi Corp. signed an agreement to supply 20,000 tonnes of urea for use in the World Bank-supported Red Soil Development Project.

Kuwait

• **1986:** The Ministry of Chemical Industry and Tunisia's **Siope Corp.** formed the **Sino-Arab Chemical Fertilizer Co.**, a joint venture with 40 percent Chinese investment, to build a DAP and NPK plant in Qinhuangdao.

New Zealand

• **1986: China-New Zealand Agricultural Consultants and East Coast Fertilizer Co.** signed a letter of intent to study prospects for manufacturing superphosphate fertilizer.

Pakistan

• **1984:** Sold 200,000 tonnes of urea to China for $40 million.

Philippines

• **1986: Philippine Phosphate Fertilizer Corp.** won a $14 million contract to provide 80,000 tonnes of fertilizer.

Saudi Arabia

• **1986:** Agreed to provide 200,000 tonnes of urea fertilizer.

Trinidad

• **1984:** Sold 40,000 tonnes of urea.

Tunisia

• **1986:** Formed a joint venture with Kuwait to produce fertilizer in China.

United Kingdom

• **1986: Humphreys and Glasgow Ltd.** signed a $3.7 million contract for modification of an ammonia plant under the World Bank Fertilizer Rehabilitation Project.

USSR

• **1987: Balakovo Chemical Works** sold 880 tonnes of double superphosphate to China, with the Khabarovsk regional fishing and consumer cooperative as agent in Sino-Soviet border trade.

West Germany

• **1986: Uhde GmbH** and **Italy's Snam Progetti Co.** signed a contract to supply a production line for an ammonia/urea complex.

• **1987: Uhde GmbH** and **Imperial Chemical Industries Plc** agreed to license Imperial Chemical technology in a new ammonia plant.

SOURCE: Council files and company interviews.

of the province's 43 closed plants had reopened by January. In Henan, 20 of 30 had reopened by early March. But 22 of Shaanxi's 30 plants were still closed in February, and 30 of the 89 small-scale plants in Shandong had not reopened by mid-spring.

Obstacles to increased use

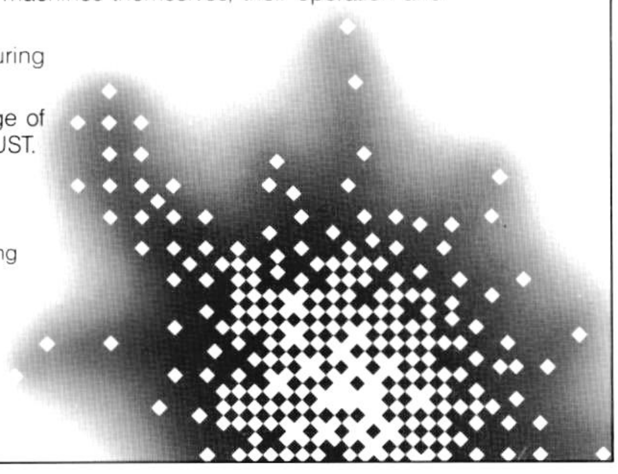
Despite considerable efforts to make fertilizer more available, China must still overcome several impediments to increased applications of fertilizer. The State must more effectively control or certify quality. Reported cases of fraud and sale of defective or ersatz fertilizers increased along with the legalization of additional suppliers.

The effectiveness of chemical fertilizers in high application areas are possibly being reduced, as dwindling amounts of organic fertilizers are used. Many farmers in suburban areas are applying less manure to their land, because the value of their labor in off-farm and non-foodcrop farming acitivities is much higher than it was a decade ago—so much so that even the increase in crop prices cannot justify the large labor expenditures required for organic manure application.

The traditional Chinese practice of hand-weeding has also fallen off, reducing returns to fertilizer use (since fertilizers stimulate weeds, which compete with crops for soil and fertilizer nutrients). More herbicides are being used, but China's chief alternative to hand-weeding has been the application of plastic sheeting around seedlings. Unfortunately, plastic sheeting has also been in short supply, and the overall availability of herbicides is still very low.

On the distribution side, the results continue to be less than ideal. Circulars were issued recentralizing distribution through AIC channels in October 1987, again in fall of 1988, and again in January 1989, suggesting a lack of administrative success in accomplishing the policy objective. It is clear the fertilizer plants have, to a significant extent, complied with the policy. But various departments of many local governments have taken advantage of the previous few years of non-unified prices to pile on additional charges and divert fertilizer to more favored or profitable locations themselves. With supplies restricted, profits are centered in local government departments, where, as the sole legal buyers and sellers of fertilizers, surplus value is concentrated, rather than with farmers, fertilizer plants, or competitive traders. Although many farmers pay high prices and contract guarantees are not always honored, fertilizer plants have not prospered, and abnormal scarcities have been artificially generated.

Currently, the most important policy changes would include less import centralization and competitive access to local markets and fertilizer plant production for all quantities beyond contracted requirements of each county government. But with the policy orientation of the currently emerging government, the most that may be hoped for is a crackdown on local governmental and corrupt official abuses. A second important policy objective is inflation control, which would reduce the asset demand for fertilizers and the instabil-



ity induced by hoarding.

Changing patterns of use

Nevertheless, the obstacles to increasing fertilizer use are not insurmountable, and China's growth rate in aggregate demand for fertilizers shows no fundamental signs of flagging, despite temporary and location-specific problems of adjustment. In fact, the need for fertilizers will increase even more rapidly, as a number of economic changes place higher demands on the land's productivity. First, aggregate growth in irrigated area has stagnated since 1979, partly because of a retrenchment in State investment in water control and growing operation and maintenance costs of the large and aging systems already in use. The lack of net growth in irrigated area means both irrigated and non-irrigated farms will be under even greater governmental pressure to become more productive through increased and more efficient use of fertilizers. Second, agricultural research has continued to provide highly productive crops that respond to greater concentrations of fertilizer.

Perhaps more important, China's development pattern strongly suggests a shift toward more land-intensive food production. Caloric intake per capita is increasing rapidly, and large portions of this increase are composed of non-staple foods such as meats, aquatic products, milk, eggs, oils, sugars, and fruits and vegetables, which ultimately require more fertilizers to produce (*see The CBR*, November-December 1988, p. 20). Raising livestock, in particular, requires much more grain than is needed to supply equivalent calories via direct consumption.

Seeds of recovery

The long-term prospects continue to be good for both foreign fertilizer products and production equipment and technology. This conclusion rests on the fundamental dynamism of the rural economy, the decreasing ability of the central government to control it, and the necessity of any Chinese government, regardless of political orientation, to attach great importance to resolving problems with food supplies. But one can expect continued instability with both domestic fertilizer production and import contract behavior for the foreseeable future, as well as temporary problems in making timely contractual commitments, while governmental control is being consolidated. Ultimately, however, such delays sow the seeds of recovery, as governments that aspire to remain in power cannot ignore indefinitely the signs that crops need fertilizer to grow. Conversely, further erosion in central control would ultimately mean relatively independent provincial or local decision-making, and this in many locations would considerably enhance fertilizer import growth. 完

Guangdong's Dynamic Inner Delta

Flexible local initiatives make this small area an industrial giant

Ezra Vogel

In February 1985, Guangdong's Inner Delta counties and cities were officially grouped together as the "Pearl River Delta Economic Development Zone" (*see* map). Counties in this zone were allowed to offer special incentives to attract foreign investment and encourage foreign trade. Long the richest part of the province and closest to Hong Kong, the Inner Delta had already begun to benefit from China's opening to the outside in the mid-1970s. Compared to the Shenzhen Special Economic Zone (SEZ), which had a great deal of central government guidance and help, the Inner Delta counties and cities were left to their own devices, but they had many favorable geographical and historical factors that helped them move ahead of the rest of the province to take advantage of opportunities that had been dormant in the decades before.

Reopening the Inner Delta

As reforms began in 1979 the Inner Delta had almost 9.5 million people in 21,500 sq km, over half the size of Taiwan and almost as densely populated. At the time it was overwhelmingly rural, with 7.3 million still living in the countryside. Wealthy by Chinese standards, the Inner Delta had 16 percent of the provincial population but 25 percent of provincial income. Yet it was still backward by the standards of newly developing economies. Almost three-fourths of the population earned its living by agriculture without benefit of mechanization, and even the richest counties had an annual per capita income of only ¥400-500.

Even during the Cultural Revolution (1966-76), Inner Delta income had remained substantially above the provincial average. The superior soil, the opportunity to market some agricultural products in Hong Kong and Guangzhou, the ease of water transport, and technical know-how all helped the Inner Delta maintain its lead over other areas. But officials at all levels understood that these same factors in a freer reform period would give the Inner Delta an even greater edge over other areas. In addition, with more overseas relatives and compatriots in Hong Kong and Macao, Inner Delta counties could attract more investment and more modern equipment.

In the early 1980s the province, in line with new national policy guidelines, gave new leeway to counties, reeestablished townships and administrative village governments, and established new metropolitan regions to facilitate the growth of commerce and industry.

Country cousins on their own

Compared to the national funds and talent poured into Shenzhen SEZ, the Inner Delta counties were rustic country cousins encouraged to rely on their own strength. But these disadvantages had their positive side, which the country cousins turned to their advantage. The counties and cities in the Inner Delta each had an average of almost 600,000 people, but the circle of cadres administering a county numbered at most several hundred. In line with policy, most were local, and with their history and proximity to Hong Kong had a good sense of how to use the opening to the outside. They shared a long-standing identification with their local community, a knowledge of its history, and a commitment to its future. The new openings gave them a chance to work toward long-cherished dreams of local development.

The county officials did not have the SEZ problem of highly diverse strangers working together, nor the Guangdong Province and Guangzhou City problem of bureaucratic layers and compartments each with its own ethos. Nor did they need to clear as many things with higher authorities, for they were mostly working outside State plans and even if higher-level permission was required, higher officials could generally respond more quickly, since county requests were for smaller sums. Compared to higher levels of government, the counties and small cities of the Inner Delta were like small companies run by a single owner embarking on a new venture without established rules—not always thorough in their staff work, but ready to respond quickly and flexibly.

Growth plans and patterns

Economic growth in the Inner Delta was a disorderly process going in many directions, but it is possible to identify several different patterns that help clarify the dynamics and structure of change. One pattern of growth that has not required a great deal of planning was developing markets in agricultural products. The other patterns, focused on industrial development, have required more capital and planning. They include: township and village enterprises, such as those in Shunde; export

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processing, as in Dongguan; comprehensive planning, as in Foshan; and large modern factories such as those in Xinhui.

SHUNDE: Township success story

Within the Inner Delta, Shunde County is known for having successful township enterprises. All 10 of Shunde's townships are relatively prosperous, but Beijiao's enterprises are particularly successful *(see* box).

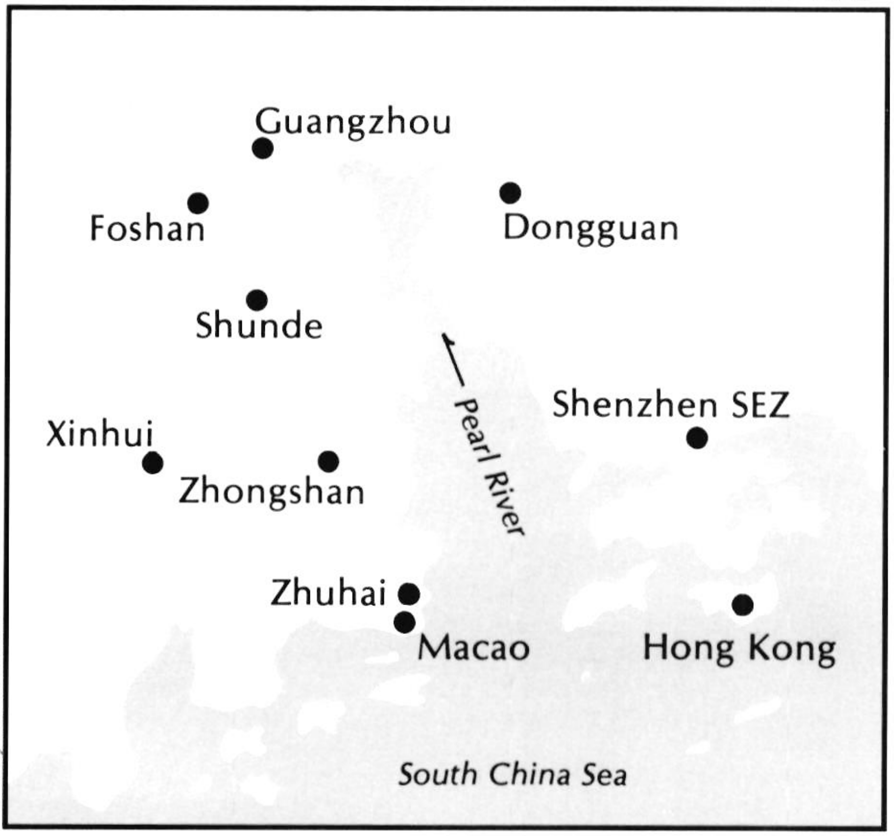
The best-known factory in Shunde is Beijiao's Yuhua Electric Fan Factory, which in 1987 employed some 1,200 people, producing some 1.2 million fans a year—about 4 percent of the 30 million-odd electric fans produced in all of China—with a total output value of approximately ¥100 million. Factory manager Ou Jianchang was honored in 1987 in Beijing as one of the 10 great national entrepreneurs from a peasant background.

The factory had originally been a commune factory making soy sauce and hot water bottle lids. Yuhua had expanded into more plastic goods while still a commune factory, but in the 1970s it lacked a sales outlet for its plastic products. In the late 1970s, therefore, Ou decided to move into plastic electric fans, and by 1982 Yuhua was producing 70,000 fans a year. They originally learned the basic technology from a State factory in Guangzhou, but have since gained new technology from Hong Kong.

In the early 1980s some 3,000 firms in China produced electric fans, but as some like Yuhua expanded and competition grew keener, the number of such firms had fallen to 500 by 1987. Some of Yuhua's fans were sold to a State import-export company for export to Southeast Asia. Although the factory itself did not receive foreign currency directly, it was allowed in 1984 to use some of the foreign currency it earned to purchase foreign-made machinery. With this new machinery it was able to produce 1.2 million fans by 1985, a level it has maintained. Having achieved success with electric fans, Ou is moving ahead to produce air-conditioners and microwave ovens.

In addition to Yuhua, Beijiao has the Meide Electric Fan Factory with some 700 workers and the Nanfang Electronics Factory with some 800 workers. In addition there is a Pige furniture company linking five factories which together employ some 2,000 people.

GUANGDONG'S INNER DELTA



Artwork by Elizabeth Stewart

Beijiao Township is unusually successful and is one of the few townships with a considerable amount of imported manufacturing equipment. However, all townships in the Inner Delta now have industrial enterprises that play a similar role in providing employment to local workers freed from agriculture, in earning local township income, and in helping meet the demand for consumer products. By Western and even Hong Kong standards, most of these township and village enterprises are not well-run or very efficient, but the rate of growth and change in one short decade is fast even by the standards of the fastest growing newly industrializing economies. The better factories, like those in Beijiao, are rapidly upgrading their technology and expanding their scale of production.

Many of the township and village enterprises in the Inner Delta, like Beijiao, have developed from local initiative. But many of the township and village workshops on the Inner Delta represent a confluence of local and Hong Kong initiatives. The classic case is Dongguan County, which, because of the success of its workshops, became Dongguan City in 1987.

DONGGUAN: Model export processor

By the late 1980s all the counties in the Inner Delta had export processing factories making goods using materials received from Hong Kong and shipping the finished products back to Hong Kong for sale on the world market. Dongguan City has so many such factories that it has become a national symbol for export processing. In 1987 Dongguan's population of some 1.2 million, distributed among 32 townships, manufactured ¥2.98 billion worth of industrial product. Of this, 82 percent was produced in "collective" enterprises, the vast majority of which were processing factories. Industrial production in Dongguan during the reform decade beginning in 1978 grew at over 40 percent per year.

Small and middle-sized Hong Kong companies in labor-intensive sectors, unable to continue competing internationally with increasingly high-priced Hong Kong labor, began in the early 1980s to seek cheap labor in China. With planning, designing, marketing, and sales done in Hong

BEIJIAO TOWNSHIP: ECONOMIC PROFILE

	Industrial Production	Agriculture Production	Rice Acreage	Fish Pond Acreage	Sugar Acreage
	(¥million)		(mou)		
1979	14	30	37,000	16,000	21,000
1989	305	55	236,000	21,000	18,000

SOURCE: Ezra Vogel

Kong and labor intensive work done cheaply in China, the companies have been able to continue faring well in international competition. Once townships in China in the late 1970s saw that such arrangements provide good jobs for their cadres and their people, good income for their township governments, and rapid progress in enriching their community, they sought Hong Kong partners. Each of the 32 townships in Dongguan has export processing contracts.

Dongguan has several advantages. Only Baoan County is closer to Hong Kong, and transportation there is now readily available, by ship and especially by truck. Roughly 600,000 people in Hong Kong who were born in or are descended from Dongguan County residents provide easy and reliable links between Hong Kong and their native county. Even Hong Kong businessmen not from Dongguan sometimes find a worker in their company from Dongguan and ask him to help smooth relations with Dongguan officials.

How the deals work

Export processing contracts are relatively simple. The Hong Kong side supplies the *lai liao* or *san lai*—the materials, the model of what is to be done, and the equipment that must be imported into China. To train the workers and ensure close hands-on management, the Hong Kong side commonly sends in managers who remain there or commute daily or weekly. When necessary, the Hong Kong side sends in personnel to repair machinery or redesign the product to fit changing market conditions. The Chinese side supplies the building and other local facilities, electricity, and labor. The Hong Kong side does not pay workers directly, but makes lump-sum payments for a certain quantity of goods contracted, final payments being made when the products are completed. The managers on the Chinese side therefore hire the workers. The contract usually covers the production of a certain specified item for a year or so. The contracts are commonly renewed, and separate contracts are used for additional items. In some contracts the machinery brought in from Hong Kong reverts to Chinese ownership after a specified period, commonly about 10 years.

The factories are generally simple brick structures several stories high that appear from the outside much like apartment buildings. Most factories do not require heavy machinery, but if they do it is generally located on the ground floor. Inside, the building is usually divided into large rooms, typically holding 50 to 100 desks. Some work, such as the making of plastic bags or the assembling of simple radios, may require assembly line work, but a more common pattern is that each person working at a desk turns out single pieces and is paid on a piecework basis. Typically in each room, all people are engaged in the same work. For example, young women might take a specially shaped sponge and sew a small piece of material onto it, making a furry toy animal. In another workshop people sew shirts or blouses. In other workshops, young women comb hair for wigs or artificial hair for dolls.

Labor and management

Many of the factories produce toys, apparel, and electronic products, areas where women are considered more nimble, and make up slightly more than half the work force. Average income in the mid-1980s was around ¥200 per month.

Dongguan managers at that time earned much more than workers, commonly ¥350-400 per month. Most local cadre managers had previously supervised people, but few had experience in business.

In the initial formation of a factory, local managers play a very important role. With plenty of local contacts, they know how to locate appropriate factory sites and how to arrange for electricity, water, and other equipment needed for the factory. A loan from a local bank is generally required to finance the building and the equipment on the Chinese side, and cadres know how to arrange them. They also know whom to contact to get the most reliable labor force and how to select workers and lower level managers from among them.

But once these very essential formative steps have been taken, the local managers do not necessarily have a great deal of day-to-day responsbility. The actual managment of the work is commonly done by experienced business managers sent in from Hong Kong.

Profits and prospects

Since most of the profits from the work processing fees go to the townships, villages, and to Dongguan City, these entities have become far richer than neighboring counties with less export processing. Dongguan has been paving roads—mostly cement—so quickly that it now enjoys more miles of paved road than any other county in the province. From a county that was considered poor a decade ago, Dongguan has become one of the richest in Guangdong.

The wealth coming to Dongguan has enabled the towns to build new hotels and restaurants in addition to roads. They had no trouble financing a 36,000 kw power station and contracting with the provincial electricity grid for some 50,000 kw in the early stages of financing the large Shajiao Electric Power Station. Thus they have fewer electric power shortages than poorer counties.

Many, however, question the future of export processing. What happens if a community has tailored a large factory site to a Hong Kong manufacturer and then after a year the Hong Kong manufacturer does not renew his contract? A decade later, when the workers are in their 30s and even older, will they still be welcome in these factories, or will they be replaced by younger workers? As Dongguan wages go up and transportation improves within Guangdong, will they be replaced by cheaper workers further inland—and if so, can they find a new niche?

Dongguan processing is therefore not nearly as attractive to planners in Guangdong and Beijing as the more modern factories being put up elsewhere. But as much as Guangdong wants to leap to modern technology, the brutal fact is that in the short run its most promising niche in the world economy is in labor-intensive industry. By 1988, top leaders in Beijing were acknowledging the value of export processing. Most poorer counties in Guangdong do not expect to build large modern factories quickly. For them, the Dongguan model is the best to which they can reasonably aspire, and they are working hard to prepare their transport and power infrastructure so they can attract Hong Kong companies to process exports in their county.

FOSHAN: Overall modernization

Unlike Dongguan, Foshan had long been a leading center of light industry and government administration. As early as the Song Dynasty, Foshan was known as one of the four great Chinese market towns, famous for ceramics and metalwork. In modern times the harbor on the Fen River could dock ships of 1,000 tons, linking it with other ports in the delta area. At the beginning of the 20th century, it became the midpoint in a short railway linking Guangzhou and Sanshui. It remained a major market town with a sizable ceramics industry into the 1950s, and then continued to grow as a major political center. With a new highway linking Guangzhou and Foshan, started in the late 1970s, it had considerable potential when reforms began.

In 1954 Foshan became the capital of the Foshan Prefecture, which oversaw most of the Inner Delta counties. By the late 1970s the city population approached 300,000, second only to Guangzhou in the Inner Delta. Though its markets lost vitality during the Cultural Revolution, the Foshan area remained more prosperous than most areas of Guangdong.

Innovative leadership

Foshan was the first large community in Guangdong to take off after reforms began in 1979. Its consumer industries had already gotten a good start in the latter part of the Cultural Revolution. Foshan was run by a collective leadership, headed by Party First Secretary Tong Mengqing, who strongly supported reforms. But its entrepreneurial mayor, Yu Fei, who served 1979-84, was a catalyst for development. Bold and controversial, Yu was not afraid to push projects even when not everyone was aboard. Assuming power just as reforms began, he had an opportunity to carry out his visions, first in Foshan City and then in the metropolitan region.

For counties that were slightly slower in getting started, betting heavily on certain larger factories—a strategy pioneered in Xinhui—became in effect a late developer's approach to achieve economies of scale and catch up with some of the more advanced counties.

Financing finesse

Foshan was not the only delta community to go to Hong Kong for financing. But Yu Fei did it with a keener understanding of the Hong Kong business mentality, better-prepared public relations, a carefully tailored tax and incentive program, and on a bigger and more professional scale. In one large meeting in Foshan alone, some 100 Hong Kong businessmen were shown investment opportunities. During his tenure as mayor, he received estimated commitments in foreign currency of some $710 million, of which $512 million was actually used during his tenure. Perhaps these are not huge amounts by American or Japanese standards, but they are huge by Chinese standards, especially for a small city. Because of his initiative and flexibility, Foshan attracted and was willing to use more capital investment than Guangzhou, which had 10 times its population. However, by the late 1980s, though still growing and prospering, Foshan was straining to meet its debt servicing.

Yu Fei, thoroughly familiar with banks and finance, boldly borrowed before others thought it safe. Foshan was the first to borrow funds for building a major bridge, charge tolls, and use the income from tolls to repay loans and finance further construction projects.

It was known that some products imported from abroad were resold at higher prices, with profits going for investment. In Yu's view, the profits had gone for a good cause, the financing of industry. As higher officials began to take a dim view of this practice, Foshan immediately ended the practice, escaping criticism. In new situations, when it was not yet clear what was and was not acceptable, Yu Fei dared to move ahead where others feared to tread.

Strategic imports

The essence of Yu's industrial investment strategy was to import the least amount of production equipment necessary to make modern products. Foshan built factory facilities using whatever acceptable local machinery it could and then imported equipment needed to create a full production line. Rather than have a single foreign company supply all needed foreign equipment, Foshan hoped to save money by getting the best buy for each machine. Since Foshan lacked technical personnel, it contracted with foreigners to train local people to operate all new equipment purchased abroad. Foshan insisted on clauses that the machinery be installed and operate successfully for some months before final payment. Yu Fei also insisted that some products be used as compensation trade to ensure that products met international standards. Even several years after opening, however, local technical people still did not have the breadth of training and experience to continue to improve and adapt machinery purchased from abroad.

Outperforming State enterprises

Foshan, under Yu Fei's guidance, pioneered a new approach [for enterprises], stretching the category of "collective" to include enterprises with up to thousands of employees

GROWTH OF COMBINED INDUSTRIAL-AGRICULTURE OUTPUT, 1980-85

(¥million/year)

Tier One Counties

	1980	1985	% change
Baoan	158	494	312%
Dongguan	902	1941	215
Doumen	204	372	183
Panyu	599	1268	212

Tier Two Counties

	1980	1985	% change
Foshan	861	2623	305%
Nanhai	992	2546	256
Shunde	997	2772	278
Xinhui	584	1334	230
Zhongshan	927	2329	251

Tier Three Counties

	1980	1985	% change
Enping	188	336	179%
Gaoming	98	144	146
Heshan	154	324	210
Jiangmen	653	1261	193
Kaiping	358	635	178
Taishan	431	1019	236
Zengcheng	233	378	162

TOTALS

	1980	1985	% change
Inner Delta	8341	15293	237%
Guangdong	36732	69449	189

SOURCE: Ezra Vogel

that were often larger and more modern than many State enteprises. In his view it was the only way to attain the flexibility needed for enterprises to adapt to market forces. In 1986, within Guangdong Province, 60 percent of the value of industrial production was from State enterprises. In Foshan Metropolitan Region it was 29 percent, with 66 percent produced by collective enterprises and the rest by small private enterprises.

By relying on collective plants which had the flexibility to make decisions without the interference of higher levels, Foshan developed a highly diversified group of modest-sized factories. The diversity reduced the risks of a small city—with little money and cautious banks—producing for unknown markets being tested for the first time. But it also made it difficult to achieve economies of scale. Foshan's strategy was to move ahead of other localities wherever there was a promising new market to enter. It was not clear how this strategy would look in the 1990s, when Foshan would face competition from larger factories with larger economies of scale, but for the first decade after reforms it worked very well, and by 1988, despite some strain to meet its debt service, Foshan was still planning to expand.

A wide range of products

By far the largest group of factories built in Foshan was in textiles and apparel, a sector where Hong Kong had very good advice to offer. The factories made use of a broad range of materials, including polyester fibers, cotton, and silk. They covered all phases of clothing production, from spinning and weaving to dyeing and assembly.

The next largest group of factories is in electronics. These include factories for assembling TVs, videocassettes, liquid crystal displays, cassettes, personal computers, circuit boards, and lower technology products such as electric fans and radios. Many of the more complex components are still bought from abroad or produced in cooperation with foreign companies, but when possible Foshan enterprises buy foreign production machinery and produce the goods themselves.

The third-largest area is in plastic goods, including handbags, gloves, and shoes. They also make many household consumer goods, especially watches, light bulbs, cans, wine, and toys.

Ceramics, the area of Foshan's traditional strength, has also grown, although production value has not kept pace with that of textiles, apparel, and electronics. Realizing that it was not immediately possible to reach international standards in ceramic tableware, Foshan enterprises concentrated in two areas: handicraft ceramics and ceramic tiles for construction. After the Cultural Revolution, ceramic factories began to resurrect traditional handicraft objects, but they also created many new designs for international markets. With technical assistance from Italy they advanced very rapidly in ceramic tiles as the booming construction industry in Guangdong and other parts of China opened a large new market. By the late 1980s there were several tile factories with a total of several thousand employees and a nationwide sales force.

Rewards for risks

Foshan's industries soon generated enough profits that by the early 1980s, in addition to reinvesting in industry, Foshan used its profits to transform the city. Not rich enough to afford the huge modern buildings built with national financial help and designed by famous architects in Shenzhen, Foshan expanded the city into former farm areas, building broad boulevards with bike lanes and vast numbers of what, for China, are relatively modern apartment buildings. By the late 1980s—far ahead of Guangzhou—virtually all apartments in the city enjoyed running water. With apartments up in new areas, Foshan could provide temporary housing for people in the old part of the city, as their areas were torn down and rebuilt. Throughout the 1980s urban renewal far outpaced similar efforts in Guangzhou and other medium-size and large cities.

Yu Fei could not have acted alone, of course, without strong support from higher levels, but Foshan was also granted the same room for flexibility and local initiatives as the local counties. It was simply the largest of such units, pioneering approaches later used around the province as well as in the Inner Delta.

XINHUI: Large factory breakthrough

In 1979 Guangzhou City was negotiating with a foreign company for the establishment of a polyester fiber plant. A Chinese-Indonesian businessman, Chen Yunkang, was prepared to provide financing, and with the advice of Hong Kong textile specialists, modern European manufacturing machinery had been selected. But the Guangzhou City discussions were stalled in bureaucratic red tape and Provincial Economic Commission officials who wanted to see plans move forward were frustrated by the delays. Whereupon officials from Xinhui, a county of some 800,000 people, offered to take over negotiations and locate the plant in their county. It was a perfect illustration of the advantages of the quicker response time of Inner Delta counties.

Xinhui was especially ready to move in 1979 for several reasons. It could see that nearby Foshan, Nanhai, Shunde, and Zhongshan had organized much more quickly and were already one or two steps ahead, and it wanted to catch up. Although Xinhui had many overseas relatives, most were far away. Xinhui had been just far enough from Hong Kong that in the 1960s and 1970s it had not been as easy to escape from there as from Dongguan, Baoan, and Zhongshan. And for the same reasons it was also not as convenient for Hong Kong businesspeople just beginning to expand export processing factories across the border.

The move to automation

In the mid-1970s, many Chinese planners doubted whether, given China's excess population, it was wise for China to move to automated plants. However, by 1979 Chinese planners had decided that improving the standard of living required modern plants, and if necessary, they would solve the employment problem by increasing employment in the tertiary sector. Therefore, when the opportunity for the polyester plants came up, Xinhui was ready to move immediately.

The agreement came quickly. The Indonesian businessman Chen Yunkang agreed to invest $10 million for modern machinery, imported primarily from Switzerland with some from West Germany and Japan. Chen Shuihong, who negotiated the Chinese side, got Chen Yunkang to agree to take 30 percent of the product each year to ensure that the Chinese would be able to pay off the debt, just in case the domestic market developed slowly. By 1981 construction began on the site of a *kui* [palm-leaf used for hand fans] fan factory that had been closed down.

The opening ceremony was held on September 27, 1983, and the plant began to produce 5,000 tons of *dilun* (dacron). By the end of 1986, the original investment in the plant had been repaid, Chen Yunkang was earning substantial income, and an additional plant producing 7,500 tons of dacron a year was in operation. When the two were completed they had a total investment of ¥127 million, including a total foreign investment of $19 million. In 1986 it produced ¥256 million of product, and the entire original investment was expected to be repaid by 1989.

The polyester fiber plant proved so successful that by 1985 a small factory in Xinhui making other fibers brought in new modern equiment and by 1986 was producing 5,000 tons a year of *binglun* (polyethylene fiber). In November 1985, a Xinhui nylon factory with the capacity of 4,000 tons a year of synthetic fiber went into operation. Even Beijing, observing Xinhui's success, turned to similar technology, and by 1987 some 17 synthetic fiber plants had been established elsewhere in China.

Eggs in one basket

What Xinhui did was to bet heavily on a large modern plant, which turned out to be extraordinarily successful. These new polyester fiber plants alone brought wealth to Xinhui. And elsewhere in Guangdong, in places like Haikou and Lechang County in Shaoguan, similar plants went up that brought employment and wealth to their communities. With the wealth from these plants, Xinhui could afford to build modern hotels, expand its roads, improve the upkeep on its parks, and with this vastly improved infrastructure, look to Hong Kong and elsewhere for further joint ventures.

Perhaps no other kinds of factories have had such a large impact on the Inner Delta as these polyester fiber plants. But there are several cases where a particularly successful plant has had a very large impact on the success of an entire county. For counties that were slightly slower in getting started, betting heavily on certain larger factories—a strategy pioneered in Xinhui—became in effect a late developer's approach to achieve economies of scale and catch up with some of the more advanced counties.

Layers of change

Among the 12 counties and the four cities in the Inner Delta one can distinguish three tiers. The first is those closest to Hong Kong, where the economy is most integrated with Hong Kong's. This tier includes Dongguan, Baoan, Zhongshan, Doumen, and is beginning to include Panyu. The ready accessibility by truck and boat from Hong Kong (and in the case of Doumen, from Macao) and the presence in Hong Kong of recent migrants from these counties has made it easy for these counties to develop export processing arrangements with Hong Kong.

All these counties have made rapid advances, but how quickly and thoroughly they took advantage of their opportunity appears to depend most on the *sixiang* (thoughts, attitudes) of the county leaders. Counties like Dongguan, with a unified leadership committed to make the best of the opportunities, moved more quickly than those like Panyu. The growth in the first tier (*see* chart), especially in Dongguan, is understated, because in export processing only process fees are counted, not the total value of the product.

In the second tier are places like Foshan, Xinhui, Nanhai, Shunde, and Zhongshan, which are relatively close to Hong Kong but not as close as the first tier. They are centrally involved in the dynamism of the Inner Delta and have good transport by water and road.

These places initially found it less easy to attract simple processing plants. Being slightly further away, they took more initiative and aimed higher than processing industries. They have tried to run their own factories and to develop locally initiated programs to attract and build industry. Just how they have done this has varied considerably from county to county. Nanhai moved early and established a lot of fairly small village industries. Shunde relied heavily on large townships and with the help of Hong Kong capital established several industries on a larger scale than those in Nanhai. Zhongshan, with a much larger county capital than any of the others, relied more heavily on larger, county-run State factories.

In the late 1980s Zhongshan and Shunde began to converge in their approach. Zhongshan, impressed with the vitality and local initiative of neighboring Shunde's town industries, decided to set up more town-led industries. Shunde County, impressed that Zhongshan government had more income from State industries and was therefore able to carry on more large public county projects such as road building, decided to develop more State enterprises.

In the third tier are counties further away (Taishan, Heshan, Kaiping, Enping, Gaoming, Zhengchen). They have had less convenient transportation and fewer county migrants working in Hong Kong. Although all but Gaoming had sent migrants to North America, the stimulus from there in the 1980s was not as great as the stimulus of Hong Kong to nearby counties. The cadres were initially slower than those in the middle tier in taking initiatives to bring industry to their areas. Being poorer, they were often less willing to take risks for fear that they would be in deep trouble if the projects failed.

However, by the mid-1980s, as transportation improved, making them more accessible to Hong Kong, and as the cost of labor rose in the first- and second-tier areas, they sensed more opportunities and built up their infrastructure. By the late 1980s they too had been infected by Delta dynamism, and their industry was growing at double-digit rates. They carefully studied the example of the first two tiers, and though a half a step behind, followed in their footsteps.

By the mid-1980s most Hong Kong businessmen found the Inner Delta, with its lower-cost labor and more responsive local cadres, more to their liking than Shenzhen. And local communities elsewhere in Guangdong and throughout China found the Inner Delta a more appropriate model than Shenzhen. Thousands of cadres from all over China took the standard tour, from Guangzhou through Nanhai, Foshan, Shunde, Zhongshan, Zhuhai, across by boat to Shenzhen, and back to Guangzhou through Dongguan. Many cadres came to the Inner Delta to serve internships in government and enterprise, and many others originally assigned there were sent out to bring the same dynamism to other parts of the province. 完

CHINA BUSINESS

中外貿易

Joel Greene

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

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

中外贸易

SALES AND INVESTMENT THROUGH
July 15, 1989

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

Advertising and Public Relations

China's Investments Abroad

Asahi Tsushin (Japan)/China Television International Service Corp.
Established television advertising joint venture in Tokyo to promote the exchange of programs and films. 4/89.

Agricultural Commodities

China's Imports

China Resources Machinery Co., Ltd. (HK)
Will supply fishmeal through World Bank Coastal Lands Development Project. $1.8 million. 6/89.

U.S.
Sold 1.2 million tonnes soft red winter wheat. 6/89.

NA (Taiwan)
Will sell 10,000 tonnes cotton. 5/89.

U.S.
Sold 300,000 tonnes soft red winter wheat. 5/89.

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.; 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; 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.

Agricultural Technology

China's Imports

Henry Simon (UK)/CTIEC and Shanghai International Trading Co.
Will build 1,200 tpd flour mill at the Shanghai No. 3 Mill. $14.5 million (£8.45 million). 6/89.

Worthington GmbH (FRG)
Will supply reactor ammonia pumps through World Bank Fertilizer Rationalization Project. $1.6 million. 6/89.

Investments in China

NA (Taiwan)/Xiamen Construction and Engineering Co.
Established Xiamen Yuxin Enterprise Co. Ltd. to cultivate shrimp. 5/89.

NA (Holland and Hong Kong)/Zhaonan Saltworks, Jiangsu
Established joint venture to produce aquatic fodder and cultivate prawn. $4 million. 4/89.

Other

USSR/Heilongjiang
Will conduct joint survey of fish resources in Xingkai Lake, Heilongjiang. 6/89.

Iran/Shanghai Foreign Economic and Technological Co.
Will expand cooperation between fishing companies in the Persian Gulf. 5/89.

UNFAO/Qinghai
Will provide $1.5 million grant to develop fishing industries on Qinghai Lake. 5/89.

Chemicals, Petrochemicals and Related Equipment

China's Imports

Bangladesh
Will export chemical fertilizer. 6/89.

BASF Holding Co., Ltd. (FRG)/Jinling Petrochemical Company, Nanjing
Established the Jinling-BASF Resins Company Ltd. joint venture to produce unsaturated polyster resin. $16.12 million (¥60 million). (50-50). 5/89.

Technip Corp. (France)/CTIEC
Will supply equipment, material, design, and technical assistance for an ammonia and urea plant in the Jinxi Chemical Complex in Liaoning. 5/89.

NA (Japan)/China Petroleum International Undertaking Co.
Will construct 1,500 tpy polystyrene plant in Lanzhou. 5/89.

Investments in China

BP Chemicals America (US)/Shanghai Petrochemical Complex
Agreed to form joint venture to produce polyethylene compounds for wire and cable industries in China. 6/89.

Amoco Chemical Co. (US)/Yizheng Chemical Complex, Jiangsu
Will establish joint venture to build a polypropylene fabric plant in Yizheng. 5/89.

New Brunswick Scientific Inc. (US)/East China University of Chemical Technology, Shanghai
Will establish E-N United Biotechnology Laboratory to develop new equipment and products for the chemical, agricultural, and pharmaceutical industries. 5/89.

China's Investments Abroad

Himont Inc. (US)/International Multi Petrochemical Enterprises Ltd. (a consortium of Chinese companies)
Established joint venture to operate two existing polypropylene plants in Lake Charles, La. 6/89.

Construction Materials and Equipment

China's Imports

Pexim Ltd. (US)
Will supply 23,537 cu m of squared logs through World Bank Third Railway Project. $5.7 million. 5/89.

Weyerhauser Co. (US)
Will supply 20,000 cu m of fir logs through World Bank Third Railway Project. $2.46 million. 5/89.

Investments in China

Jurong Cement (Singapore) and Reliance Agency Holdings (HK)/Hainan Sihuan House Landed Property Development Corp.
Will establish a cement production joint venture in Hainan. $8 million. 7/89.

Onoda Cement Co. (Japan) and Mitsui & Co. Ltd. (Japan)/China Huaneng Raw Materials Corp. and Dalian Cement Plant
Will establish a joint venture to produce 4,000 tpd cement using an advanced dry production line. $155 million. 5/89.

Other

Council of Forest Industries of British Columbia (Canada)
Constructing three demonstration buildings in Beijing to promote wood frame construction. 4/89.

Consumer Goods

China's Imports

Carpeting Concepts (US)/Shanghai China International Enterprises Inc.
Signed letter of intent to sell carpet manufacturing technology and equipment. 5/89.

Videocolor, subsidiary of Thomson S.A. (France)
Sold complete television factory to be disassembled and shipped to Guangdong Province. 5/89.

Investments in China

NA (Japan)/Miyun Furniture Factory, Beijing
Established Miri Friendship Furniture Co., Ltd. to manufacture 100,000 trunks and wardrobes annually. $5.67 million. (JP:33%-PRC:67%). 6/89.

3D Media (US)/CITIC and Wuxi Magnetic Tape Plant, Jiangsu
Established joint venture to produce video and audio tapes. $20 million. Registered capital: $6 million. 5/89.

NA (Japan)/Dafeng Bicycle Flywheel General Factory and Bank of China, Yancheng branch
Established the Fengdong Heat-Treatment Co., a hot rolling mill, to produce bicycle parts. $1.29 million (¥4.8 million). (JP:40%-PRC:60%). 5/89.

NA (Taiwan)/Anqing, Anhui
Established the Qianshan County Youwei Handicraft Co., Ltd. joint venture to produce mats and bamboo chopsticks. $25,500 (¥950,000). 5/89.

NA (Taiwan)/Yiren Daily-Use Chemical Factory, Beijing
Signed letter of intent to invest in the packaging and marketing of Yiren 909 Hair Regenerating Liniment. 4/89.

Electronics and Computer Software

China's Imports

MTC Electronic Technologies (Canada)
Received orders for 48,000 12-inch monochrome and 150,000 13-inch color television tubes. $9.4 million. 5/89.

Tecnomatix Europe, N.V., subsidiary of OSHAP Technologies, Ltd. (US)
Received order for ROBCAD workstations used to evaluate robot installations. $450,000. 5/89.

Investments in China

Hitachi Ltd. (Japan)/Shenzhen Electronics Group
Signed agreement to produce color television picture tubes. $36 million. (JP:25%-PRC:75%). 5/89.

NA (Japan)/Two radio factories
Began operation of AAA Electronics Co. Ltd. joint venture to produce resistors. $543,000 (¥2.02 million). 5/89.

Swiss Potentiometer Ltd. (Switzerland)/Yongxing Radio Element Factory
Established Huarui Pot Ltd. joint venture to produce precision potentiometers. $1.45 million (SFr2.33 million). Registered capital:$996,000 (SFr1.6 million). 5/89.

Casper Hi-tech (HK)/Zhong Huan Computer Corp., Tianjin
Signed agreement to build factory to produce color monitors. 4/89.

Philips N.V. (Netherlands)/Huadong Electron Tube Factory, Nanjing
Established the Feidong Lighting Co. joint venture to produce lighting products. Philips' investment: $25 million. 4/89.

China's Investments Abroad

Orion Electric Co., subsidiary of Daewoo Group (South Korea) and Zhejiang Fuchen Co. (HK)/Hangzhou Television Factory
Will establish joint venture in the Kumi Industrial Complex to produce color television picture tubes. $20 million. (SK:80%-HK:6%-PRC:14%). 6/89.

Other

Inforum Ltd. (HK)/BOC
Signed agreement to conduct a feasibility and design study for automating BOC operations. 5/89.

Numerix Corp. (US)
Signed agreement granting Brighton Keytech Industries Ltd. (HK) product distribution rights in the PRC. 5/89.

Dekuai Company (US)/MMEI's Electronic Science and Technology Information Institute
Established the China Dekuai Information Co. to promote the exchange of electronic technological and market information. 4/89.

NEC Corp. (Japan)/INSTRIMPEX and China-Japan Software Center
Opened computer service center in Beijing to provide installation, maintenance, and technical consulting services for NEC clients. 4/89.

Electronics (Consumer)

Other

International Finance Corp., affiliate of the World Bank
Approved loan for the Shenzhen Crown Electronics Co., a manufacturer of consumer electronics. $15 million. 6/89.

AIWA Co., Ltd. (Japan)
Opened service center in Beijing. 5/89.

Engineering and Construction

China's Imports

Ingra (Yugoslavia)/China Metallurgical Construction Corp.
Will jointly construct 113 km Nanchang-Jiujiang highway in Jiangxi with partial funding from the World Bank. $31.5 million. 5/89.

Environmental Technology and Equipment

China's Imports

Trans American Chemical Corp. (US)/Shanxi Import/Export Corp.
Signed contract to transfer technology for treating acid pollution. 5/89.

Food and Food Processing

China's Imports

Laco, Van Aarsen, Hypeco, Pas Reform, Zeddam and Meyn (Netherlands)/CTIEC, Shenyang branch
Will supply completely integrated broiler chicken project. 3/89.

Investments in China

Nichu Enterprises Co. (Japan)/Dalian
Established the Dalian-Nichu Marine Co. joint venture to process prawn. $1.8 million (J¥230 million). 7/89.

E.D.& F. Man Pacific Holdings (HK), subsidiary of E.D.& F. Man Ltd. (UK) and API (HK), subsidiary of Swire Pacific Ltd. (HK)/Shantou Cannery
Established a joint venture to process frozen vegetables. (50-50). 6/89.

Oboyi Corp. and Nichimen Corp. (Japan)/CHINATUHSU, Liaoning branch
Established the Liaoning North Food Co., Ltd. to process pickled vegetables, wild herbs, and mushrooms. $1.38 million (J¥180 million). 6/89.

Bond Corp. International Ltd. (HK)/Huizhou Beverage Co., Guangdong
Bought an 85% shareholding in the Huizhou Brewing Co. Ltd. for 25 years. $10.5 million. 5/89.

Kyotaru Co., Ltd. (Japan)/Capital Hotel, Beijing
Opened Japanese restaurant in the Capital Hotel. 5/89.

Technip (France)
Signed agreement to design and build a 600,000 hectoliter/yr brewery in Shenyang, Liaoning. 5/89.

NA (Japan)/CHINATUHSU
Will establish the Yufeng Co., Ltd. joint venture to produce condensed honey in Henan Province. $510,000 (¥1.9 million). 5/89.

Maruichi Shoji Co. (Japan)/Yantai Mugong Co., Shandong
Established Yantai Livestock Products Development Co. to breed cattle and market beef. $200,000. (JP:49%-PRC:51%). 4/89.

USSR/Hainan Provincial Reclamation Corp.
Signed an agreement to jointly finance the establishment of coffee and tea production bases in Hainan. 4/89.

Other

Colombia
Signed agreement to exchange 1,500 tonnes of high-quality coffee for 1,000 Beijing jeeps. 6/89.

Poland/Shenzhen
Signed protocols to develop chicken, ham, and pork processing industries. 5/89.

Machinery and Machine Tools

China's Imports

Bryant Grinder Corp. (US)/CMC
Will supply internal and external grinders for manufacturing refrigeration compressors at the Shanghai Refrigeration Compressor Works. 6/89.

Pressflow Ltd. (UK)
Supplied two L-type robots used with plastic injection-molding machinery. $172,000 (£100,000). 4/89.

Sulzer Pumps (UK)
Will supply water cooling pumps to the Yueyang coal-fired power station in Hunan Province. $1.7 million (£1 million). 4/89.

Other

Michigan Manufacturing Technology Association/China Machine Tool Builders Association
Signed five-year agreement to cooperate in initiating trade. 6/89.

THK Co., Ltd. (Japan)/CTIEC and Beijing Numeric Control Technology Development Center
Opened service center to provide technical renovation, design, and training services. 5/89.

Medical Equipment and Devices

China's Imports

European Technology Center, division of Technica Systems Ltd./Beijing Technological Import/Export Corp.
Will supply pharmaceutical testing equipment, medical equipment, and water purification systems through a World Bank loan. $1 million. 4/89.

Investments in China

Vitreous Plastic Isolators Pty. Ltd. (Australia)/Beijing Laboratory Animal Research Center, Tianjin Poultry Diagnostic Center, Harbin National S.P.F. Poultry Facility
Will provide equipment and technology for the production of germ-free chicken eggs for use in vaccines. $5.7 million (A$7 million). 4/89.

Metals, Minerals, and Related Equipment

China's Imports

Summa Group (US) and Hoesch Export A.G. (Austria)
US will supply Austrian steel; 3,140 tonnes deformed steel bars, 2,450 tonnes flat steel bars, and 1,800 tonnes spring steel through World Bank Third Railway Project. $3.7 million. 6/89.

Hylsa (Mexico)
Will supply 1,200 tonnes of galvanized steel sheet through the World Bank Third Railway Project. $1,019,000. 5/89.

Nippon Steel Corp., NKK Corp., Kawasaki Steel Corp., Sumitomo Metal Industries Ltd., Kobe Steel Ltd., and Nisshin Steel Ltd. (Japan)
Signed contract to supply 1.5 million tonnes of steel products during July-November. 5/89.

Nisshin Steel Ltd. (Japan)/China Metallurgical Import/Export Corp.
Sold hot-rolling mill which will be installed at Taiyuan Iron & Steel Corp., Shanxi. $3.83 million (J¥500 million). 5/89.

Paradip (India)/MINMETALS
Will supply 240,000 tonnes iron ore. 5/89.

Sms Concost Inc. (US)/Chengdu Seamless Tube Factory
Will supply arc-type continuous casting machine. $15 million. 5/89.

Somisa (Argentina)
Will supply 2,800 tonnes cold-rolled steel through the World Bank Third Railway Project. $1.9 million. 5/89.

Villares (Brazil)
Will supply 7,500 tonnes spring steel through the World Bank Third Railway Project. $4.4 million. 5/89.

Investments in China

Always King Ltd. (HK)/Shanxi Energy Corp. and Yuanping Iron & Steel Works
Signed agreement to build 150 cu m puddling furnace and 24 cu m sintering machine. 5/89.

Top Winner Co., Ltd. (HK)/Four Chinese companies
Opened the Jinxin Granite and Marble Co., Ltd. in Tianjin. $3.68 million (¥13.7 million). 5/89.

Wrought Copper Ltd. (Chile)/No. 1 Copper Tube Plant, Beijing
Started operation of the Jingsheng Copper Tube Co., Ltd. joint venture to produce red copper tube. $10.64 million. (50-50). 5/89.

Other

Australia
Will set up a center at the Wuhan Iron & Steel Institute to train managerial personnel in the metallurgical industry. $6.9 million (A$8.5 million). 5/89.

Bolivia
Signed cooperative agreement to protect the world market price of antimony. 5/89.

Military Equipment

China's Imports

Société Nationale d'Etude et de Construction de Moteurs d'Aviation (France)/CATIC
Will supply technology to renovate combustion chambers of F-7 engines. $348,000. 5/89.

Packaging and Pulp and Paper Equipment

China's Imports

Cloeren Co. (US)/Coextrusion Plastics Sheet Co., Beijing
Headed consortium to supply equipment for manufacturing barrier aseptic packaging materials. $3.5 million. 6/89.

Voith (Austria) and Valmet Paper Machinery Inc. (Finland)/Guangzhou Paper Mill and CTIEC
Will supply equipment and technology to renovate and expand production capacity. Austria: $13 million. Finland: $3.45 million. 5/89.

Investments in China

China Paper Partners, affiliate of Conservatree Company/Tianjin Marine Shipping Co.
Will establish joint venture to build a waste paper sorting plant in Tianjin and plans to ship Los Angeles' waste paper to China for processing. $25 million. 5/89.

China's Investments Abroad

Intraco Trading Firm (Singapore)/CHINAPACK
Established Sintrapack Pte. Ltd. joint venture to trade packaging materials. $2.58 million (S$5 million). (SP:51%-PRC:49%). 7/89.

Other

New Fibers International Ltd. (Canada)
Will expand production capacity of its Fujian pulp mill with financing from the Chinese Navy's Eastern Fleet. 5/89.

Petroleum, Natural Gas, and Related Equipment

China's Imports

IRI International (US)
Will supply 30-ton, self-propelled well servicing rigs through the World Bank Daqing Petroleum Project. $4.2 million. 5/89.

Maloney-Crawford Inc. (US)
Will supply mechanical equipment and spare parts for CO_2 and polymer injection plant funded through the World Bank Daqing Petroleum Project. $3.42 million. 5/89.

Prime Computer (US)/Zhong Yuan Petroleum Exploration Bureau and Design Institute
Will supply software and hardware used to design engineering equipment. $600,000. 5/89.

Metrotect Ltd. (UK)/MOE Pipeline Scientific Research Institute
Will supply West Qurna oilfield with pipeline coating materials; coal tar enamels, primers, and WR650 outerwrap. $8.6 million (£5 million). 4/89.

Petrotherm (US)/Bohai Oil Co., Tianjin
Sold electric tank heating systems. $100,000. 4/89.

Pharmaceuticals

China's Imports

Glaxo Hong Kong Ltd., subsidiary of Glaxo Holdings PLC (UK)/No. 3 Southwest Pharmaceutical Factory, Chongqing
Agreed to build pharmaceutical factory to produce asthma drugs. $10 million. (50-50). 5/89.

Investments in China

Capsugel, subsidiary of Warner-Lambert Co. (US)/China Corp. of Pharmaceutical Economic and Technical International Cooperation
Began operations at Suzhou Capsugel Ltd. joint venture to produce hard gelatin capsules. (50-50). 6/89.

Huashun Co. (HK)/Guangzhou Pharmaceutical Plant No. 1
Established 10-year Zhongfu Pharmaceutical Co., Ltd. joint venture. $256,000 (HK$2 million). (50-50). 5/89.

Pfizer Inc. (US)/Dalian Pharmaceutical Factory
Established the Pfizer Pharmaceuticals Ltd. joint venture which will employ advanced technology to produce primarily antibiotics. $35 million. (US:55%-PRC:45%). 5/89.

UN Fund for Population Activities and UNICEF/State Pharmaceutical Administration and Hubei
Set up workshop to produce L-18 methylnorethindrone, a contraceptive drug, at the Hubei Pharmaceutical Plant, Xiangfan City. $6.6 million. 5/89.

Ports

Investments in China

Hanpei Engineering Company (US)/Dalian Port Bureau
Established Dalian Harbor Development and Construction Consultative Corp. to plan, design, and develop harbors in China and other countries. 5/89.

Power Plants and Equipment

China's Imports

C. Itoh & Co., Ltd. (Japan)
Will supply aluminum conductor steel through World Bank Lubuge Hydroelectric Project. $3.9 million. 6/89.

Other

Credit Lyonnais S.A. and three other banks (France)/BOC
Signed loan agreement for the construction of a pump storage power station at the Daya Bay Nuclear Power Plant. $196 million. 6/89.

Property Management and Development

Other

Bank of Tokyo, Dai-Ichi Kangyo Bank Ltd., and Fuji Bank Ltd. (Japan)
Headed bank syndicate that provided loan to the Beijing New Century Hotel, a joint venture between All Nippon Airways and C. Itoh Corp. (Japan)/Beijing Xiyuan Hotel and BOC Trust and Consultancy Corp. $72.75 million. 5/89.

3M China Ltd., subsidiary of 3M (US)
Signed contract to lease 52,000 sq m in Caohejing New Technological Development Zone to expand 3M's Shanghai operations. 5/89.

Ships and Shipping

China's Imports

Austal Ships (Australia)/Nantong High Speed Passenger Ship Co., Jiangsu
Signed contract to supply a 430-passenger catamaran. 6/89.

Investments in China

Dong-Nam-A Shipping Company Ltd. (South Korea)/SINOTRANS
Established Sino-Kor Company Ltd. to operate direct shipping service between the South Korean ports of Pusan and Inchon and the Chinese ports of Dalian, Tianjin, and Shanghai. $500,000. (50-50). 5/89.

Other

American President Lines (US)
Began weekly container cargo service to Whampoa and Chiwan ports. 5/89.

Telecommunications

China's Imports

L.M. Ericsson (Sweden)/INSTRIMPEX and Jiangsu Foreign Trade Corp.
Will supply AXE-10 program control telecommunications equipment to 11 cities in Jiangsu. $27 million. 6/89.

Standard Telephone and Cable (Norway)/INSTRIMPEX
Will supply 26,000-line telephone exchange facility and transmission power equipment to Baicheng and Siping in Jilin. $6.36 million. 6/89.

Italtel S.p.A. (Italy)
Will supply digital telephone network to Liaoning Province. 5/89.

L.M. Ericsson (Sweden)/Posts and Telecommunications Bureau, Chongqing
Will supply 50,000-line AXE-10 exchange system and related equipment to Sichuan. $26.8 million (¥100 million). 5/89.

L.M. Ericsson (Sweden)/MPT
Signed agreement to supply Beijing computer center with software to maintain the AXE system. $5 million. 4/89.

Siemens A.G. (FRG) and Standard Elektrik Lorenz A.G. (FRG)/Shandong
Will supply telephone switchboards and microwave equipment. 4/89.

Investments in China

AT&T Network Systems International (US) and Philips B.V. (Netherlands)/ Shanghai Optical Fiber Engineering Corp. and Shanghai Telecommunications Equipment Factory
Signed agreement to establish factory to produce fiber optic digital telecommunications equipment. $14.5 million. (50-50). 5/89.

Farmstead International Corp. (US)/Weihai No. 1 Radio Factory, Shandong
Signed joint venture agreement to re-manufacture old AT&T telephone equipment for sale and installation in China. 5/89.

Olex Cables, division of Pacific Dunlop Ltd. (Australia)/Shenzhen Science and Industry Park Corp. and China National Post and Telecommunications Appliances Corp.
Established Shenzhen Olex Cables Ltd. joint venture to manufacture plastic-insulated telephone and power cables. $21 million. (AUS:75%-PRC:25%). 5/89.

Textiles

China's Imports

NA (FRG)/Zhenhua Woolen Spinning Mill, Wujiang County, Jiangsu
Signed contracts to sell mixed rabbit hair/wool spinning equipment. $4.8 million (DM9 million). 5/89.

NA (Japan)
Sold 5.6 million sq m high-grade polyester crepe. 5/89.

Investments in China

USSR
Plans to establish flax processing joint venture in Baotou, Neimonggol. 7/89.

NA (Japan)/Liaoning Provincial Silk Import/Export Corp.
Will establish the China-Japan Huayou Knitwear Co. joint venture to produce women's sweaters. $1.21 million (¥4.49 million). (JP:40%-PRC:60%). 5/89.

Other

NA (Poland)/Shenzhen
Agreed to cooperate in designing, producing, and marketing garments. 5/89.

Transportation

China's Imports

McDonnell Douglas Corp. (US)/China Eastern Airlines, Shanghai
Signed purchasing agreement for five MD-11 long-range jetliners. 6/89.

Volkswagen of America, subsidiary of Volkswagen A.G. (FRG)/First Automobile Works of Changchun, Jilin
Will sell tooling and production equipment from closed New Stanton, PA factory. 6/89.

Boeing Co. (US)/Guangzhou and Shanghai
Will sell three 757-200 aircraft. 5/89.

Piper Aircraft Corp. (US)/CAAC
Plans to sell Cheyenne IIIA turboprops for pilot training. 5/89.

Toyota Motor Corp. (Japan)/Shenyang, Liaoning
Will sell technology for automobile production. 5/89.

Investments in China

NA (Hong Kong)/Xiamen
Established the Golden Dragon Automobile Corp. 20-year joint venture to manufacture luxury buses. $11.3 million (¥42 million). Registered capital:$4.03 million (¥15 million). 5/89.

Lufthansa Airlines (FRG)/Air China, subsidiary of CAAC
Will establish maintenance and technical joint venture at Beijing Capital Airport to provide engine and general maintenance for all types of aircraft. (FRG:40%-PRC:60%). 5/89.

China's Investments Abroad

Jardine Airport Services Ltd., subsidiary of Jardine Pacific (HK)/China National Aviation Corp.
Formed a joint venture to provide ground handling services. (HK:74%-PRC:26%). 5/89.

Other

MVA Consultancy (UK)/Beijing Research Institute for Traffic Engineering
Will participate in two-year study to improve traffic conditions in Beijing. 5/89.

Citroen (France)/CMC, CTIEC, Second Automobile Factory, Hubei
Negotiating agreement to supply design and production technology. 4/89.

Miscellaneous

Investments in China

Tai Heng Hong (Singapore)/Beijing Arts & Crafts Import/Export Corp.
Established the Jing Ta Trading joint venture to trade arts and crafts, light industrial products, and traditional Chinese medicine. $500,000 (SP:51%-PRC:49%). 6/89.

China's Investments Abroad

Chinese Consulting in Scandinavia AB (Sweden)/Shanghai Light Industrial Corp.
Established China One AB to promote economic and trade cooperation between China and Nordic countries. 3/89.

Other

Bulgaria
Signed agreement to expand bilateral economic cooperation and to discuss forming joint ventures. 7/89.

Asons Tobacco Corp. (US)/China Tobacco Import/Export Corp., Shandong branch
Obtained worldwide distribution rights for General and Double Horse brands of cigarettes. 6/89.

Arthur Andersen & Co. (US)/China International Economic Consultants
Will jointly offer consulting services to foreign-invested enterprises experiencing financial and/or operational problems. 5/89.

Chicago Forward Trade House (US)/China International Trade Institute
Signed agreement to send experts to present lectures and train trade personnel. 5/89.

Greenwich Workshop Inc. (US)/Ministry of Culture and China Artists Association
Signed agreement to produce and distribute Chinese artists' signed oil paintings. 5/89.

Rado Watch Co., Ltd.
Designated official timekeeper of the 11th Asian Games. Will supply software, output terminals, and scoreboard facilities. 5/89.

Shawmut National Corp. (US)/China Industry Commerce and Development Corp.
Renewed contract to promote business between New England states and China. 3/89.

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