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THE CHINA BUSINESS REVIEW

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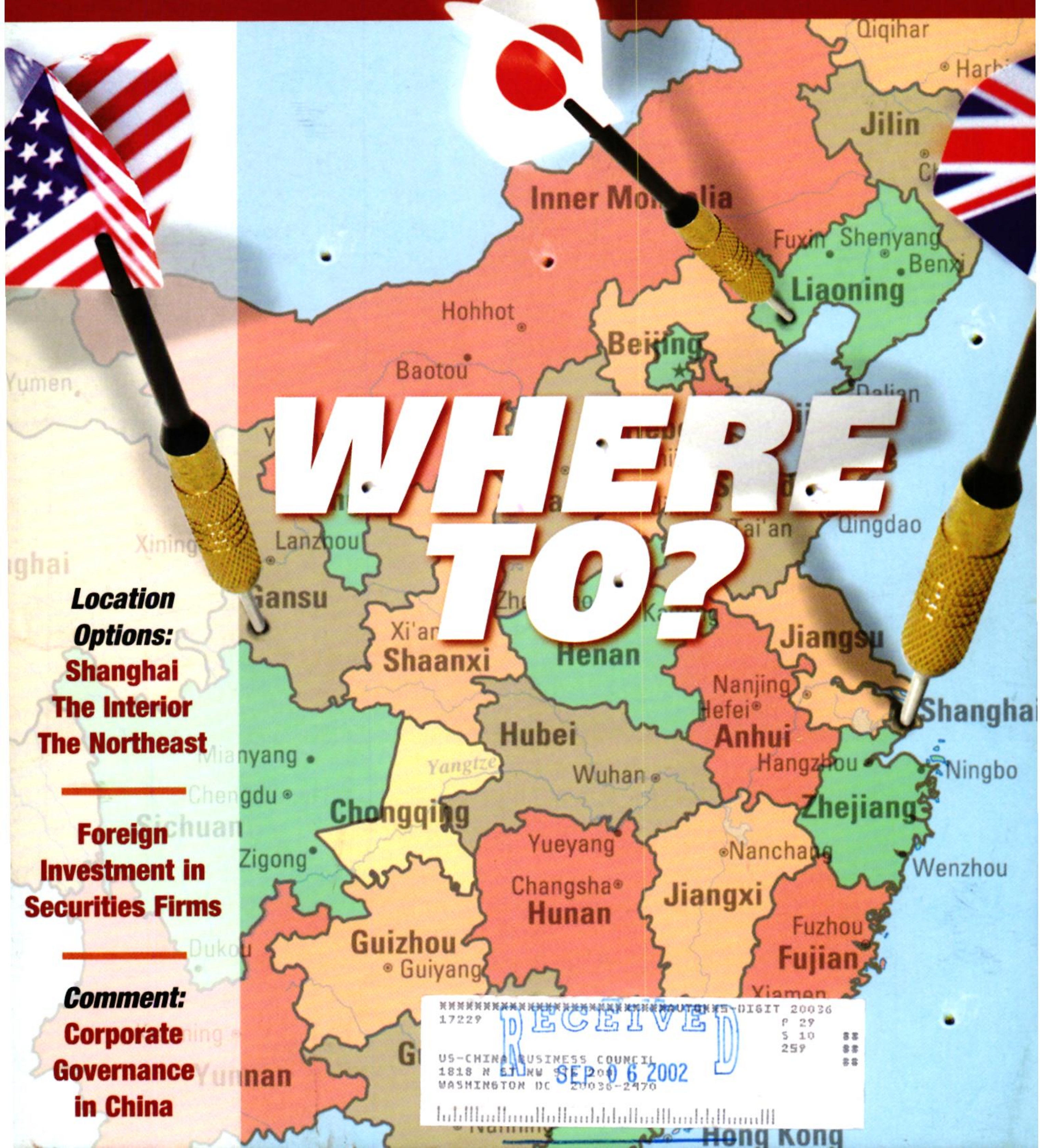

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THE CHINA BUSINESS REVIEW

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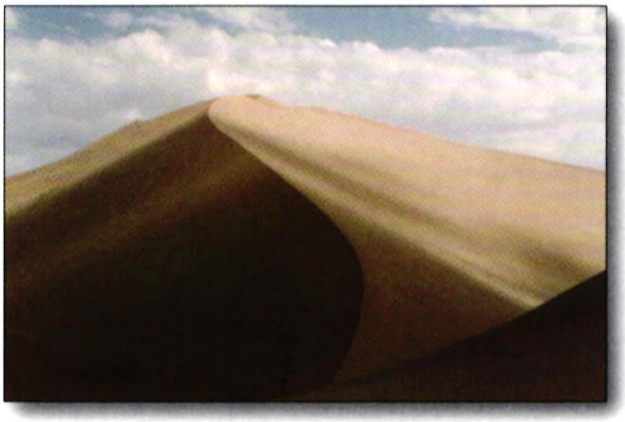
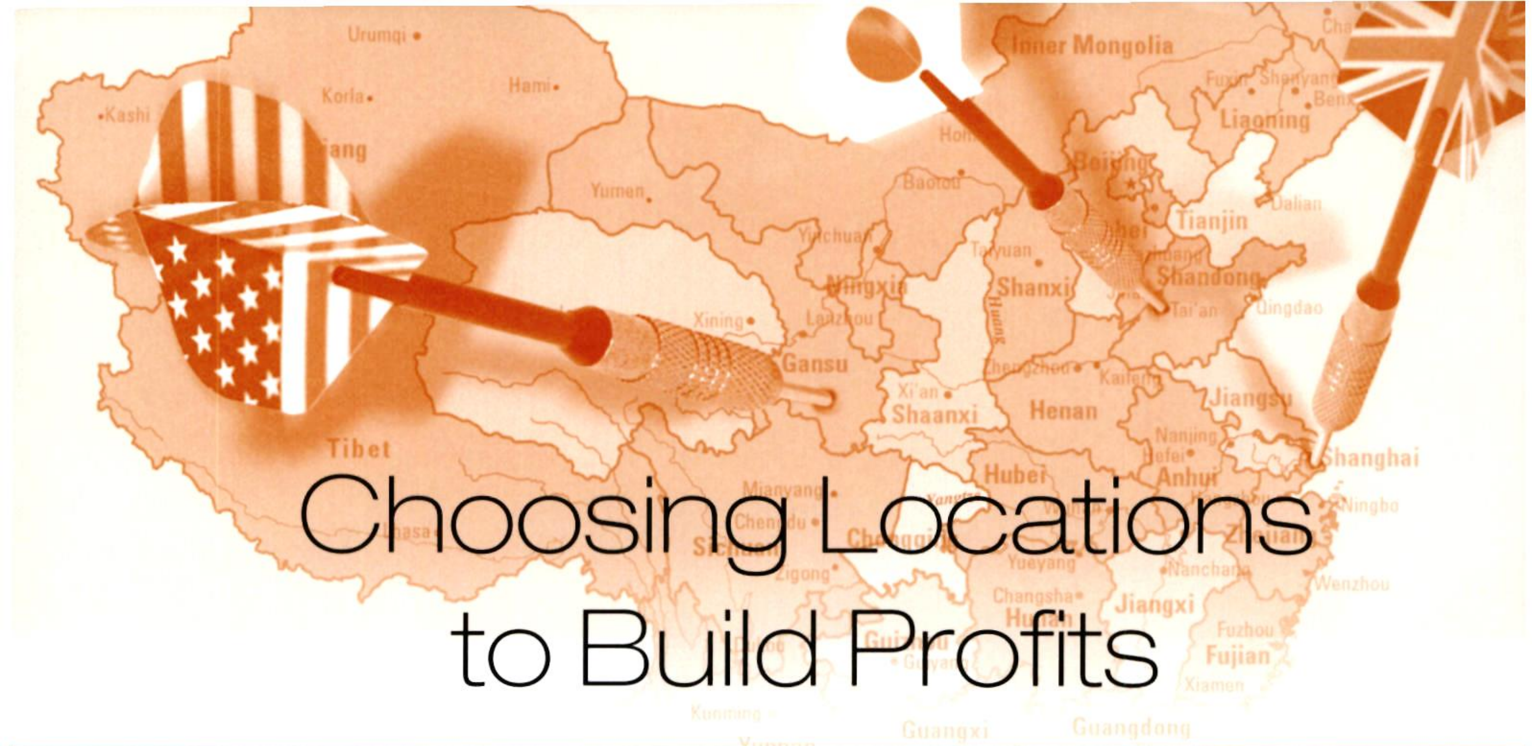


China by Region

Year: 2000 Region	Population (millions)	GDP (RMB million)	GDP per capita (RMB)	Exports ($ million)	Imports ($ million)	Foreign Direct Investment ($ million)
Anhui	59.86	303,824	4,867	2,119.42	1,570.41	318.47
Beijing	13.82	247,876	22,460	7,667.23	16,576.55	1,683.68
Chongqing	30.90	158,934	5,157	1,060.48	790.59	244.36
Fujian	34.71	392,007	11,601	13,622.82	9,334.44	3,431.91
Gansu	25.62	98,336	3,838	420.79	270.76	62.35
Guangdong	86.42	966,223	12,885	93,427.92	82,059.61	11,280.91
Guangxi	44.89	205,014	4,319	1,640.48	644.48	524.66
Guizhou	35.25	99,353	2,662	481.66	374.80	25.01
Hainan	7.87	51,848	6,894	608.53	485.67	430.80
Hebei	67.44	508,896	7,663	3,278.14	2,208.97	679.23
Heilongjiang	36.89	325,300	8,562	2,423.93	1,568.66	300.86
Henan	92.56	513,766	5,444	1,586.83	1,537.06	564.03
Hubei	60.28	427,632	7,188	1,899.77	1,992.87	943.68
Hunan	64.40	369,188	5,639	1,631.90	1,360.36	678.33
Inner Mongolia	23.76	140,101	5,872	1,114.00	1,272.27	105.68
Jiangsu	74.38	858,273	11,773	26,376.94	22,817.43	6,425.50
Jiangxi	41.40	200,307	4,851	1,188.37	863.69	227.24
Jilin	27.28	182,119	6,847	1,486.93	1,498.39	337.01
Liaoning	42.38	466,906	11,226	10,589.47	9,478.00	2,044.46
Ningxia	5.62	26,557	4,839	354.26	177.85	17.41
Qinghai	5.18	26,359	5,087	133.55	92.90	NA
Shaanxi	36.05	166,092	4,549	1,326.93	1,060.61	288.42
Shandong	90.79	854,244	9,555	16,092.67	12,157.30	2,971.19
Shanghai	16.74	455,115	34,547	24,639.61	30,063.75	3,160.14
Shanxi	32.97	164,381	5,137	2,090.94	700.60	224.72
Sichuan	83.29	401,025	4,784	1,433.60	1,343.92	436.94
Tianjin	10.01	163,936	17,993	7,674.27	9,481.98	1,166.01
Tibet	2.62	11,746	4,559	109.02	39.90	NA
Xinjiang	19.25	136,436	7,470	1,147.24	1,438.86	19.11
Yunnan	42.88	195,509	4,637	1,092.71	791.49	128.12
Zhejiang	46.77	603,634	13,461	20,482.14	11,039.56	1,612.55

SOURCE: *China Statistical Yearbook*, 2001
NOTES: NA=not available.
Local government statistics may differ from these official central-government figures.



Choosing Locations to Build Profits

Companies engage with China to reach a simple goal: growth in profitability. Over the last two decades, many companies from around the world have met this goal in one of three ways: by breaking into China's distinct regional markets to produce final goods for China or offshore; by improving productivity using more efficient and cost-effective factor inputs; and, more recently, by tapping into selected clusters of innovation to raise the value of final products and to diversify product and service offerings to meet the needs of China's corporate and household consumers.

Cities play a crucial role in all three of these forms of commercial engagement. Using North American definitions of urban markets, China's 668 cities and over 19,000 major towns and suburban areas hold around 45 percent of the country's population, not the 32-36 percent that official statistics define as urban using outdated conventions. (North American urban market statistics include suburban populations; China's do not because of the antiquated household registration system, which severely undercounts real urban consumers who, with a very few exceptions, cannot change their official registration from agricultural to non-agricultural.)

Consumers in urban and suburban areas—largely in the eastern provinces but also in some central and western provinces often generalized as "poor"—have the highest purchasing power in China. China's cities are the country's engines of production; they account for over 72 percent of GDP, have taken in more than 93 percent of actual foreign direct investment, and have attracted over 85 percent of fixed-asset investment during the past decade. Some cities, such as Beijing, Shanghai, and Shenzhen, are becoming the nation's incubators of innovation in technology, marketing, and management.

The sheer number of cities and towns, their diverse economic, social, and institutional characteristics, and the rapid pace of urbanization in China over the last decade have made locational decisionmaking by foreign companies increasingly difficult. The challenges will increase as China implements World Trade Organization (WTO) commitments over the next five years and more of the country, and more sectors, open up to foreign direct investment. Companies are now asking: Should production be focused in Beijing, Guangzhou, Hong Kong Special Administrative Region (SAR), Shanghai, Shenzhen, or Tianjin? How competitive are central and western cities—such as Changsha, Hunan; Chengdu, Sichuan; Chongqing; Wuhan, Hubei; and Kunming, Yunnan—for which more reliable information is becoming available? What advantages do smaller cities—such as Changde, Hunan; Deyang, Sichuan; Foshan, Guangdong; Kunshan, Jiangsu; Shunde, Guangdong; Suzhou, Jiangsu; Wuxi, Jiangsu; and Zhengzhou, Henan—have over their larger counterparts? These questions are as important to established foreign companies in China as they are to new entrants; under the WTO regime, firms are facing a much larger and more diverse China market than during the last two decades, when policy and poor infrastructure tightly circumscribed sectoral and geographic access.

Answers to locational questions depend on what companies see as the role of China's cities in their efforts to improve profitability and the timeframes for such improvements. Many established companies are gradually factoring next quarter contributions into global operations after years of patient business development. For others, medium- and long-term timeframes are most relevant, which means firms will need to project how far and fast individual cities will progress in meeting corporate expectations.

Competitiveness depends on a city's capacity to support a firm's profitability growth—within timeframes set by the company—in seven ways. A city can be competitive as:

- A market for imports of finished goods,
- A local market for domestic production,
- A production node for domestic markets,
- A production node for export markets (export processing),
- A source of intermediate inputs for production in other cities in China,
- A distribution node for domestic or export markets, and as
- A center for supporting services, including those fostering technological, marketing, and management innovation.

Shanghai is one of very few cities in Asia that can reasonably aspire to global competitiveness in all seven roles. Though 12 years ago such aspirations appeared naive, Shanghai has since undergone major changes that have altered the basic structure of the Asian regional economy. Strong momentum for continuing reforms, the growing empowerment of increasingly sophisticated consumers and enterprises, and major planned developments in infrastructure and supporting services could lead Shanghai to become a major node in the global economy by the end of this decade—if it can strengthen its inherent competitive advantages in contributing to profitability growth for both domestic and foreign companies.

—Edward Leman

Can Shanghai Compete as a Global City?

Edward Leman

Shanghai has gone through enormous changes over the past decade that few cities in history have experienced in such a short period of time. The city has succeeded on many fronts: economic growth, foreign investment, trade, improvement in living standards, infrastructure construction, and environmental improvement, to name just a few. But the job is not nearly finished, and Shanghai cannot afford to become complacent. Competition among cities around the world for investment capital, trade, technology, and knowledge is fierce and—thanks to the globalization of the economy—becoming fiercer. Key economic functions are increasingly concentrated among fewer and fewer cities.

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These cities are creating a strong and, as New York has shown during the last year, very resilient international network that meets the needs of the global economy—not simply those of their region or nation.

Shanghai may be able to compete as a global city if it is able to build up its competitiveness in seven key areas: as a market for imports of finished goods; as a local market for domestic production; as a production node for domestic markets; as a production node for export markets (export processing); as a source of intermediate inputs for production in other cities in China; as a distribution node for domestic and export markets; and as a center for supporting services, including those fostering technological, marketing, and management innovation.

Shanghai could become a major player in the global economy—but it needs to focus much more than it does now on developing its real competitive advantages.

In its 10th Five-Year Plan (2001-05), the Shanghai government declares its aim to become a "center of international economy, finance, trade, and shipping...a city with plentiful foreign and domestic business opportunities and low comparative costs." Though these intentions are laudable, they will amount to empty rhetoric if Shanghai does not sustain systematic, integrated, and consistent efforts to build on its considerable competitive advantages during this decade.

Shanghai as market

According to the 2000 national census, Shanghai's total population now exceeds 16.2 million, of which 3.8 million are migrants who have resided in the municipality longer than six months (see *The CBR*, May-June 2002, p.30). This makes Shanghai the second-largest metropolis in East Asia after greater Tokyo. The census count exceeds by 3 million the official municipal estimates made before the release of the census figures late last year; Shanghai's real consumer population base is therefore 20 percent larger than has generally been reported. Although this larger population dampens official per capita indicators of GDP, retail sales, and household savings deposits, this newly measured migrant population includes a growing number of highly trained, middle-income professionals and managers who have moved from other cities with the active encouragement of the Shanghai government.

The real market region of Shanghai steps well beyond its administrative boundary, which was drawn more than 40 years ago. Within a one-day drive from Shanghai is a regional market encompassing more than 100 million people. This one-day market region is the largest in East Asia: it is twice the size of Tokyo's or Jakarta's, two-and-a-half times the size of Seoul's, triple the size of Manila's, and four times that of Bangkok. Furthermore, Shanghai is the core metropolis in a large, rapidly urbanizing and industrializing corridor stretching from Ningbo through Hangzhou, in Zhejiang, to Shanghai, and then northwest through Suzhou, Wuxi, and Changzhou to Nanjing, in Jiangsu. This corridor—which is 250 km long but less than 50 km wide—constitutes China's largest megalopolis, with a concentrated population of 55 million.

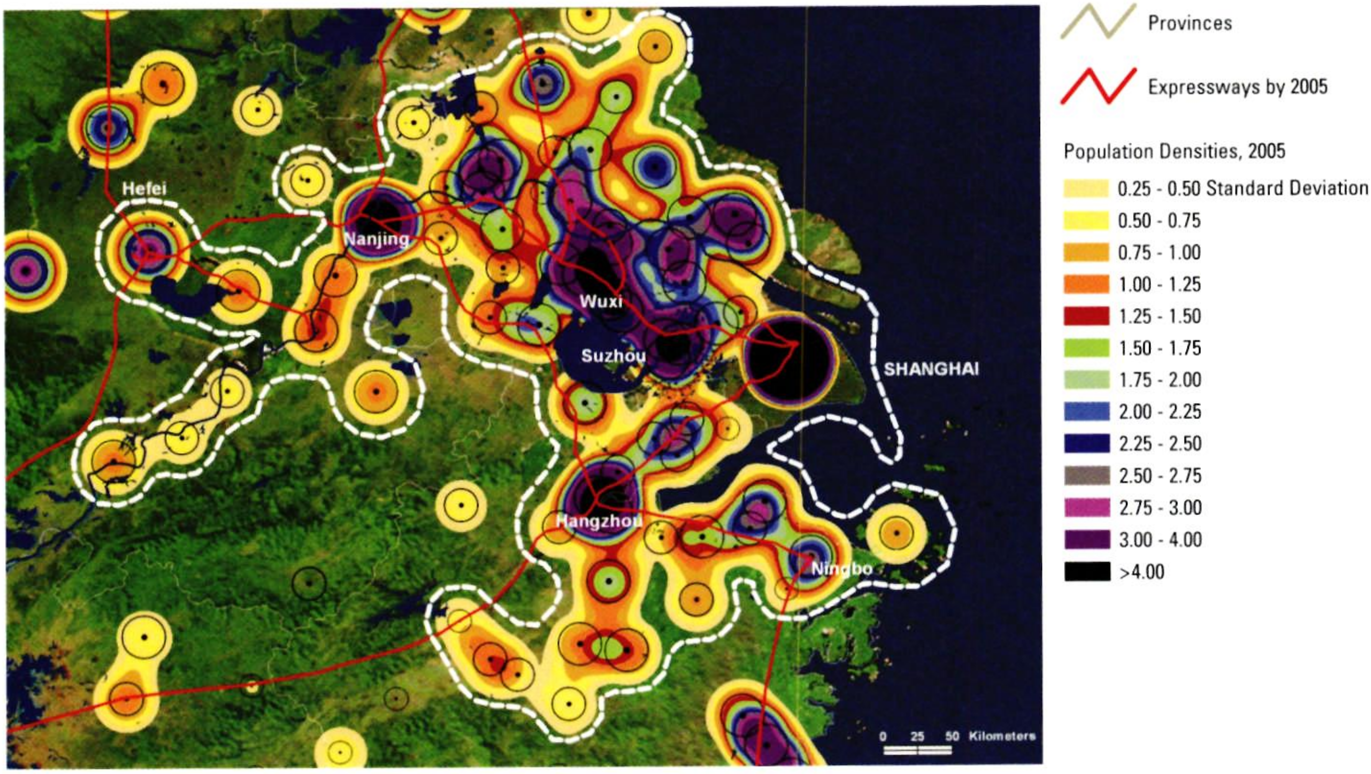
Around 43 million people in this narrow corridor are either fully urban or, while still living in suburban areas and officially classified as "agricultural," are quickly shifting to urban employment, lifestyles, and purchasing power. This group makes up a rapidly growing proportion of the megalopolitan population; its members have left farming to enter the manufacturing, construction, retail, and transportation services sectors of the wider urban economies. And by the middle of this decade, the Yangzi Delta megalopolis will merge with a smaller corridor of cities on the north shore of the Yangzi River in Jiangsu and a cluster of cities in southern Anhui to form an agglomeration of 75 million inhabitants, of which 52 million will be urbanized, according to Chreod Ltd. projections prepared for the World Bank (*see* Figure 1).

Links to consumers

Of major significance to this megalopolis are the impacts of China's ambitious intercity highway construction program. Started in the early 1990s, by 2015 the National Trunk Highway System will have connected all of the country's principal cities and provincial capitals. Many links are already complete in the Yangzi Delta region, and by the end of this decade, when the delta expressway network is complete, Shanghai will have access to a coastal and central-China market of just over 600 million consumers within a two-day drive by transport truck from China's largest port. This two-day market region will contribute 60 percent of China's GDP by that time, and will be home to 80 percent of China's enterprises.

No other gateway city will have comparable access to such a large consumer and producer market. For example, the Pearl River Delta

Figure 1
Yangzi Delta Megalopolis, 2005, Projected Population Densities



SOURCE: Chreod Ltd.

region, anchored by Guangzhou, Hong Kong, and Shenzhen, will have access by intercity highway by the end of this decade to 340 million consumers, of which over a third will be in the less-developed western provinces of Guangxi, Guizhou, and Yunnan. The Pearl River Delta's two-day market region is expected to contribute just over 30 percent of China's GDP by 2010 (not including the GDPs of Hong Kong and Macao SAR), and hold 17 percent of the country's enterprises, according to Chreod projections.

Shanghai is preparing integrated environmental management plans covering the entire metropolitan area, including the suburbs.

Shanghai as producer

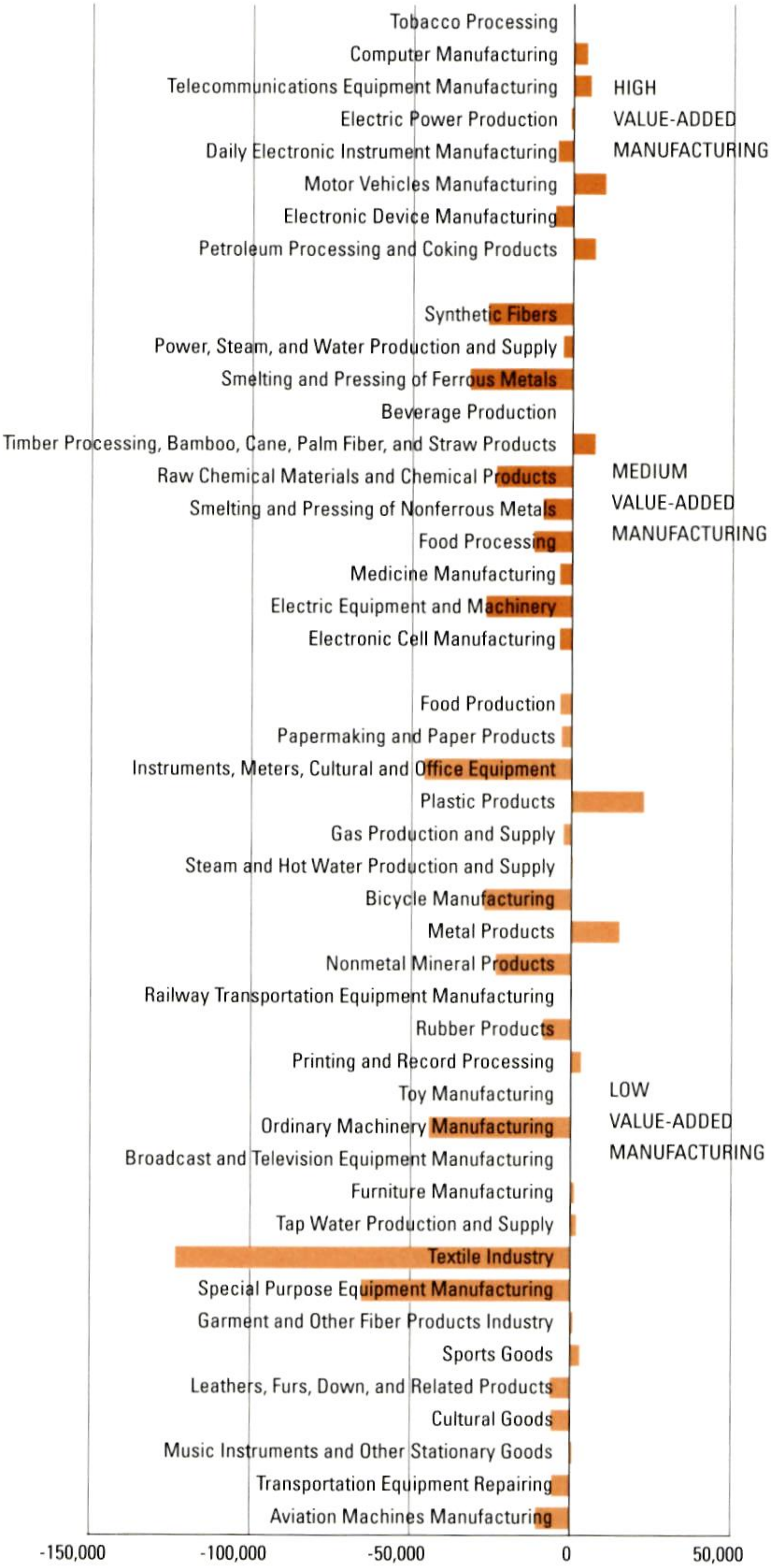
Shanghai is not only China's largest metropolitan market and gateway to the largest and fastest-growing regional consumer market in Asia. For most of the last century, Shanghai has also been one of China's key production nodes, particularly in manufacturing.

Shanghai's economic planners have scored major successes in industrial restructuring over the last 10 years. Low value-added manufacturing has decreased significantly, particularly in the antiquated textile and heavy-equipment manufacturing industries, both of which have relocated outside of Shanghai (*see* Figure 2).

Though low and medium value-added industries still account for the vast majority of Shanghai's industrial employment, the city has made significant advances in motor vehicle manufacturing, computer manufacturing, telecommunications equipment, and integrated circuit manufacturing and packaging (see *The CBR*, November-December 2001, p.8). Foreign companies have invested heavily since the early 1990s to help propel Shanghai into a national leadership role in the automotive, chemical, microelectronic, and advanced transportation sectors.

The process of industrial restructuring has had a dramatic impact on the urban structure of Shanghai (*see* Figure 3). Many large, old plants have relocated to outlying cities and towns in the Yangzi Delta megalopolis and even inland to lower-cost locations in central and western provinces. Medium value-added industries, such as food processing, have sprung up in suburban

Figure 2
Changes in Shanghai Employment by Type of Industry, 1996-2000 (persons)



SOURCE: Chreod Ltd.

towns, taking the form of township and village enterprises, relocated state-owned and urban collectively owned enterprises from the inner city, and foreign-invested ventures. Industrial restructuring has freed up considerable inner city land for residential and commercial redevelopment.

More importantly, medium value-added industrialization is dramatically transforming suburban towns and villages—until recently treated as "rural" county towns—into important extensions of the "city proper" within Shanghai's Outer Ring Road. Smaller cities and towns, such as booming Kunshan and Taicang just across the Shanghai border in Jiangsu, are also attracting medium-sized value-added firms. All counties in Shanghai (except Chongming Island) have recently been upgraded to administrative districts; they now have the same powers and responsibilities as traditional urban districts within the Outer Ring Road. Shanghai is therefore rapidly evolving into a poly-nucleated structure similar to Tokyo and New York. A range of competitive suburban locations are becoming available to firms; these will broaden significantly during this decade with the development of a light rail transit network that will dramatically improve labor mobility in Shanghai.

High value-added manufacturing is showing signs of economic and spatial clustering. Microelectronics firms appear to be congregating in the Zhangjiang High-Tech Park in the Pudong New Area on Shanghai's east side. Automotive firms and supporting services are clustering in the Anting area to the west. And large-scale chemical production and processing facilities are centered in Shihua Town on Hangzhou Bay.

While the Shanghai municipal government actively promotes these high value-added clusters, district governments are pushing the development of medium value-added industries in suburban towns. Foreign investors should keep two issues in mind when assessing the competitiveness of suburban towns as production centers. The first is the uneven institutional capacity of district governments to promote and sustain conditions that firms require to become and remain profitable. These include the provision of infrastructure to required standards, transparent regulatory approvals and fair enforcement, and the provision of sufficient residential accommodation for workers, including migrants. The second issue is the quality and future of the environment. Given the pace of industrialization, many suburban towns face serious water, sewage, and solid waste problems.

The Shanghai municipal government has recognized these vulnerabilities in suburban districts and proposes to address them as an important element of the 10th Five-Year Plan. With the support of the World Bank, Shanghai is preparing integrated environmental management plans covering the entire metropolitan area, including the suburbs. It is also embarking with the World Bank on a 10-year program to strengthen the institutional, environmental management, and fiscal capacities of suburban district governments. This is the first time that China will explicitly integrate suburban development into the urban management of a large metropolitan area.

Shanghai as service provider

By the late 1980s, the central and municipal governments had recognized that four decades of under-investment in human, technological, and financial capital had led to a steep decline in Shanghai's traditional industrial role. The governments expended considerable effort during the 1990s to shift the economy's reliance from the secondary (manufacturing and construction) sector to the tertiary services sector, and to jump-start much higher value-added manufacturing through foreign direct investment in key sectors.

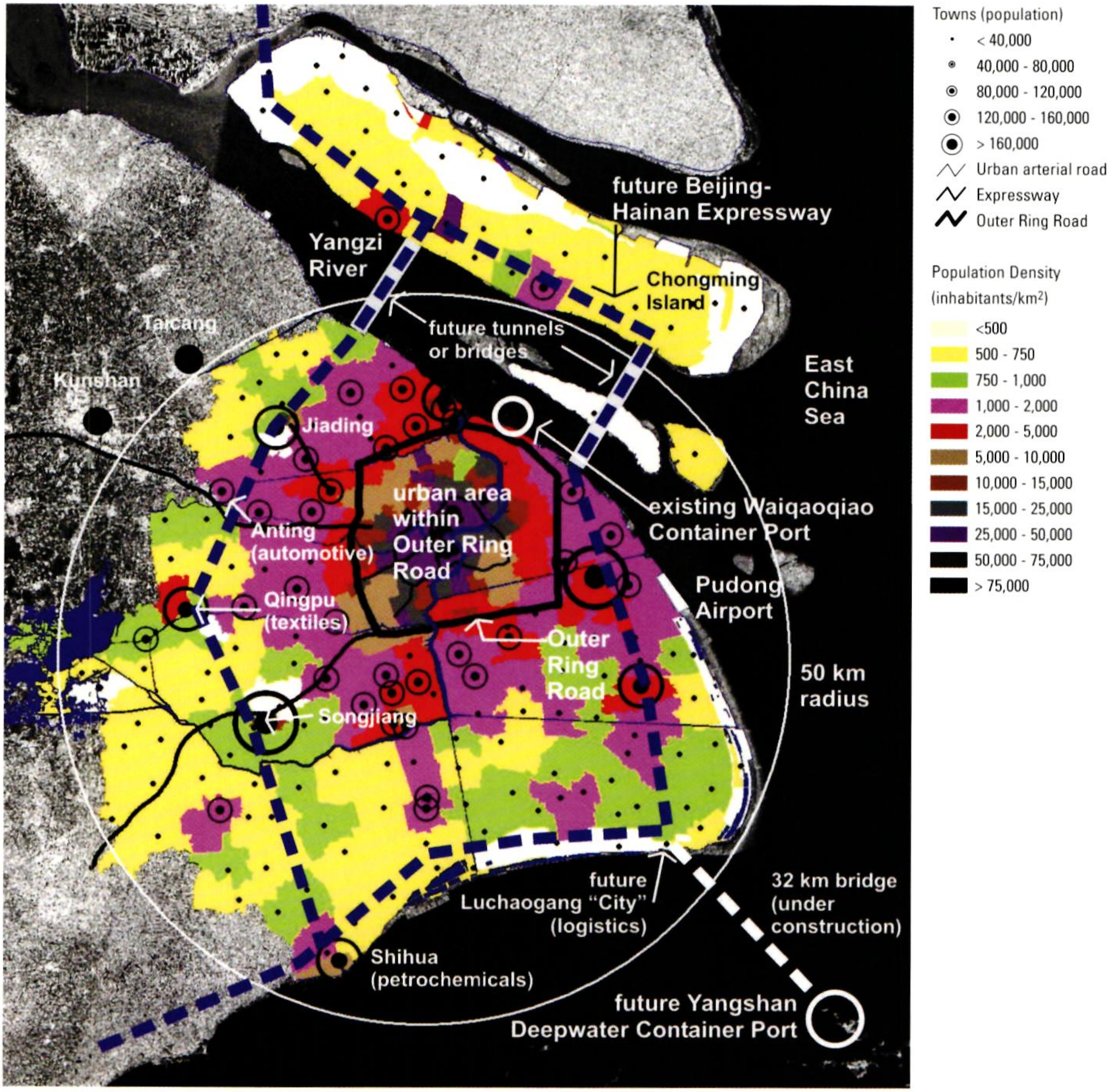
The secondary sector accounted for 64 percent of Shanghai's GDP in 1990. By the end of the decade this ratio had dropped to below 48 percent; the tertiary services sector was producing half of Shanghai's GDP. Though on the surface this is a remarkable achievement, digging a bit deeper into what constitutes "tertiary" services raises some important issues for Shanghai.

The services category, as measured by China's economists, lumps street vendors with luxury retailers, porters with lawyers, and pawn shops with accountants into a single tertiary sector. But a critical "quaternary" services sector exists, in which globally competitive cities excel, that is considerably more important to Shanghai, and that requires careful and sustained nurturing by government and business partners. The quaternary sector is knowledge- and information-intensive; it focuses on abstract transactions that create much higher value. Globally competitive cities provide such quaternary services as higher education, cultural and entertainment services, human resources and organizational management, information management, science and technology management, legal and regulatory services, and sophisticated financial services in capital formation, allocation, distribution, and monitoring. The lower value-added tertiary sector, in contrast, serves the needs of local consumers and producers; it includes distribution, communications, infrastructure, real estate, health, and basic education services.

New York, London, Tokyo and other global cities excel in quaternary services and provide them to three types of markets: extended regions in which they are the principal metropolis (for example, New York in the Eastern Seaboard megalopolis stretching from Boston to Washington, DC), to national or continental markets; and to each other in a global network of information and capital flows.

Disaggregating and reorganizing data on Shanghai's services sector provides a more instructive breakdown between lower value-added tertiary and quaternary sectors. In 1990, quaternary services accounted for 12 percent of the city's GDP; by 2000 this share had grown to just over 18 percent, according to the *Shanghai Statistical Yearbook*. Tertiary services accounted for 20 percent of GDP in 1990 and 32 percent in 2000. Therefore, the lower value-added tertiary sector grew faster and contributed more to Shanghai's economy than did advanced quaternary services. In economic terms, a metropoli-

Figure 3
Shanghai Municipality, 2000



SOURCE: Chreod Ltd.

tan and regional economy the size of Shanghai's clearly has a latent demand for more sophisticated higher-order transactions.

The demand is not being met yet in Shanghai, however, because of supply bottlenecks.

Systemic constraints to the development of quaternary services persist in law, finance, enterprise management, and information and knowledge management. Most are rooted in a culture of corporate statism that emerged in Shanghai during the last decade through widespread corporatization of government interests (most of which remain government owned and managed, at best indirectly). They are also rooted in thinly veiled protectionism that foreign companies will rigorously challenge under World Trade Organization (WTO) rules.

Recognizing the impact and potential benefits of China's WTO commitments, the Shanghai government has made the support of quaternary services a key element of its 10th Five-Year Plan. The city will give considerable attention to increasing human capital through support of medium and higher education, promotion of research and development by both domestic and foreign enterprises, and acceleration of reforms in the financial and legal sectors. The reforms are still subject to central government control and, notwithstanding China's WTO entry, continue to be hampered by central ministries' periodic ambivalence about reform; in many instances, central agencies far removed from the dynamics of China's largest metropolis are holding back the development of Shanghai's quaternary services.

If Shanghai can maintain its momentum, by the end of this decade the structure of the metropolitan economy could be markedly different. Thirty percent of the city's GDP could be in quaternary services, up from 18 percent in 2000, and 28 percent of GDP could be in tertiary services, down from 32 percent, according to Chreod projections (*see* Figure 4). The contribution of high value-added manufacturing could triple by 2010, medium value-added manufacturing could rise to 20 percent, and low value-added manufacturing could all but disappear.

Shanghai as distribution hub

Much of Shanghai's growth during the past decade has resulted from an explosion in foreign trade. Imports through Shanghai more than tripled from 1990 to 2000, while exports grew fivefold. In 1990 Shanghai's trade was principally focused on Hong Kong, Japan, the United States, Germany, and Singapore; in 2000 the top five trading partners were Japan, the United States, Germany, Hong Kong, and South Korea, according to the *Shanghai Statistical Yearbook*. Trade with Japan grew by a factor of eight, to over $9 billion, from 1990 to 2000; with the United States by seven times, to over $7.5 billion; with Germany by five times, to almost $3 billion; with France by 12 times, to just over $1 billion; and with Taiwan by a factor of 37, to reach $1.7 billion (part of which flowed through Hong Kong in the early 1990s). Direct trade with Hong Kong—once Shanghai's principal trading partner—only doubled during the decade, to $2.6 billion. Shanghai clearly managed to weather the Asian crisis by significantly diversifying and expanding its trade with markets minimally affected by the financial turmoil and subsequent trade contractions.

Shanghai's port now ranks fourth in the world in terms of tonnage. It is China's largest container port after Hong Kong, and ranks fifth in the world in container throughput, up from seventh place in 1999. The port is expected to handle 7 million twenty-foot equivalent units (TEUs) in 2002 and reach 10 million TEUs by 2005; container throughput growth averaged 27 percent per year during the past decade, according to the *Shanghai Statistical Yearbook*. The existing container port is a joint venture between the Shanghai Port Authority and Hutchison Port Holdings of Hong Kong, which has invested heavily since the mid-1990s in berth construction, technological improvements, and management upgrading. The reach of Shanghai's port is

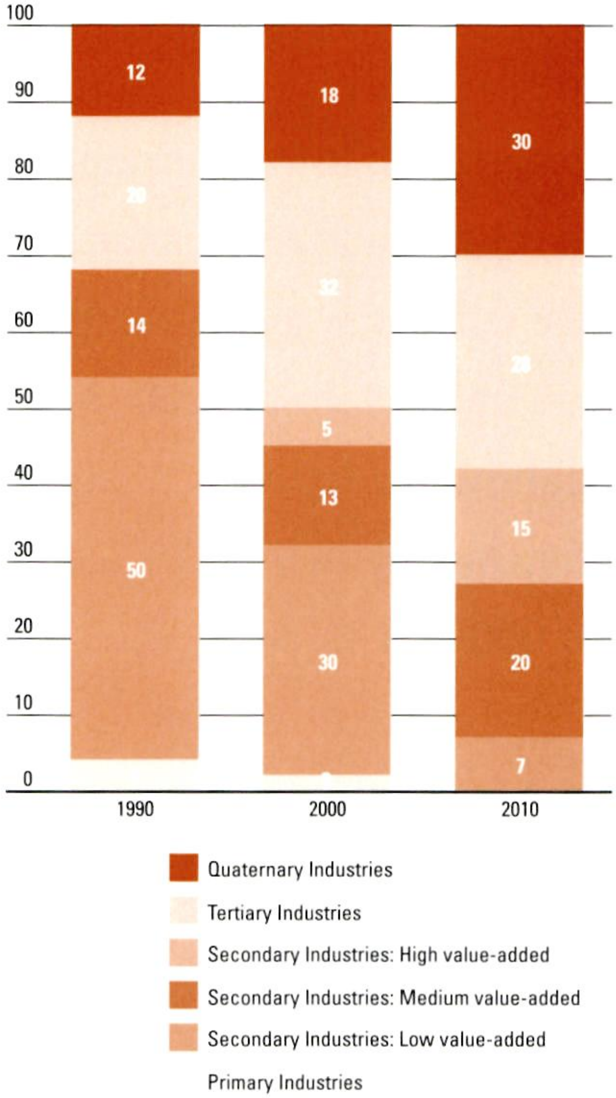
Despite the improvements to Shanghai's container facilities, the city still faces major bottlenecks, due, in part, to the relatively shallow depth at the Waigaoqiao terminal, which limits access to 50,000-ton ships.

formidable: Shanghai is a major national railway hub, a principal node of the National Trunk Highway System, and the ocean port for the Yangzi River Basin stretching to Yunnan on the border with Myanmar. Upon completion of the Three Gorges Dam, 10,000-ton ships will be able to reach inland as far as Chongqing.

Despite the improvements to Shanghai's container facilities, the city still faces major bottlenecks, due, in part, to the relatively shallow depth at the Waigaoqiao terminal (12.5 m when dredged), which limits access to 50,000-ton ships. After years of debate between Shanghai and Zhejiang on the location of a new deepwater container port, the State Council last year gave final approval to Shanghai to construct a new 50-berth port on the Yangshan Islands in Hangzhou Bay that will serve fourth- and fifth-generation container vessels. The port will be connected by a 30 km, eight-lane bridge to a new town to be built in Shanghai's Nanhui District. The town, Luchaogang, will hold between 200,000 and 300,000 residents by 2020, and will be the principal logistics facility for the new port. The scale of the project, to be completed around 2015, is unprecedented; Hong Kong, the world's largest container port in terms of throughput, today holds 18 berths; second-ranked Singapore has 16 berths. Construction of Yangshan Port will start this year.

Shanghai's expressway connections have, to date, focused on developing links westward

Figure 4
Shanghai's Changing Economic Structure, 1990-2010



SOURCE: Chreod Ltd.

along the Yangzi and northwards through central Jiangsu to the Bohai Gulf. A major new initiative during this decade will be the construction of the Shanghai portion of the Beijing-Hainan north-south expressway. This link will integrate with the new Yangshan container port: two highway links will cross the Yangzi across Chongming Island to the northern shore in Jiangsu and, to the south, across Hangzhou Bay via a new causeway. A significant bottleneck in north-south movement, particularly from eastern Jiangsu and southern Shandong, will therefore be removed.

Most of the hardware will likely be in place by the end of this decade to support Shanghai's aspiration of becoming China's principal distribution node. Nevertheless, considerable work lies ahead: China continues to lag in efficient truck freight transport, river transport, rail transport, general and specialized warehousing, containerization and packaging, transshipment, freight forwarding, and logistics information management. Intermodal transport remains seriously stymied by interprovincial and intersectoral protectionism and an almost complete lack of coordination in investment planning and operational management of ports, rail, air cargo, and highways. WTO membership may facilitate consolidation, technological upgrading, and management improvements in many of these sectors through foreign involvement. However, WTO provisions alone are unlikely to rid the transport and distribution sectors of a long legacy of local protectionism and chronic inefficiencies. Though Shanghai can, and likely will, reform within its boundaries, many of the institutional changes needed to make it a global distribution hub will require firm central government leadership of sustained interprovincial and national action.

Shanghai as center for innovation

Ultimately, cities become and stay globally competitive through constant innovation by individuals, enterprises, knowledge institutions, and governments. Innovation occurs not only in the development of technology and its applications, but also in the identification of latent needs of customers; in the mobilization and organization of human, financial, technological, and information resources to meet these needs; and in the creation of effective institutional mechanisms that ensure fairness and protect the public interest. Innovation cannot be legislated or put into five-year plans; ideas that matter cannot be neatly programmed. Similarly, though outside ideas can spark innovation, it is not an importable commodity.

Shanghai's biggest challenge during this decade is not to build ports, highways, or high-speed rail lines. It is to develop a resilient culture of innovation among its domestic and foreign enterprises, among its students and teachers in centers of higher learning, among its cadres in the municipal and district governments, and among its political leadership in the Municipal People's Congress and the local Chinese Communist Party apparatus. Shanghai must be at the leading edge of innovation in finance, law, logistics, trade, science and technology, governance, urban management, and environmental protection if it is to compete successfully on a global scale. Innovation requires the acceptance of risk, sufficient rewards, superb human capital, mechanisms through which human capital can converge to exchange knowledge and ideas, the free flow of information, and access to sufficient financial capital that is tolerant of prudent risk.

Shanghai has most of the elements needed to become a global center of innovation. Traditionally, Shanghai has been China's foremost commercial city; it has a strong business heritage and latent mercantile orientation, outshining any other metropolis in China. Shanghai has one of the best-trained and hardest-working pools of human capital in the country; the city has 45 colleges and universities and 34 research academies specializing in science, engineering, economics and finance, the social sciences, and business management, including the China Europe International Business School in Pudong's Jinqiao area, a joint venture of Shanghai Jiaotong University and the European Foundation for Management Development. Work is currently under way on a new "university city" in Songjiang Town in the western suburbs, an "Oriental College Town" as a joint venture of Fudan and Tongji universities, and similar consolidated higher learning clusters in Nanhui District and Jinqiao.

Shanghai's biggest challenge during this decade is not to build ports, highways, or high-speed rail lines. It is to develop a resilient culture of innovation.

Shanghai has made major progress over the last 15 years in opening itself to information and knowledge from throughout China and from other countries; the city now has formal academic exchanges with more than 400 universities in 30 countries, and a growing number of students trained overseas are returning to live and work in the metropolis.

Some foreign companies in Shanghai have started to branch out into research and development in a number of sectors, including microelectronics, information technology, and health sciences. Over 50 venture capital firms have established operations in the city, several with seed financing from the Shanghai government (see *The CBR*, July-August 2002, p.26).

Shanghai prides itself on having the most advanced regulatory regime in China for the protection of intellectual property rights, although, as elsewhere in the country, progress is required in consistent enforcement. Shanghai has been a test area for a number of national institutional reforms in social security, land leasing, public infrastructure, public and corporate finance, and the marketization of state-owned housing. It continues to test innovations in these and other sectors—innovations that will be replicated throughout China as further examples of the "Shanghai model."

Though all of these factors have contributed to Shanghai's growth over the last decade, much more effort is needed to integrate systems of innovation that produce concrete results. Government alone cannot—and should not—be responsible for fostering innovation. Shanghai's companies, both domestic and foreign, need to be much more active partners than they are today, since growth in their profitability ultimately depends on maintaining an edge over competitors in other cities in China and elsewhere in the region.

Shanghai 2010

Shanghai could be a very different metropolis by the end of this decade. Economic restructuring and financial reforms could lead to growth in advanced quaternary services, and to a far greater role for higher value-added manufacturing serving domestic and global markets. The city could equal and perhaps surpass Hong Kong and the Pearl River Delta to become China's main distribution hub for external trade. If interprovincial trade barriers fall, linkages to the rest of the Yangzi Delta megalopolis could strengthen to the point that Shanghai's municipal boundary blurs and eventually becomes irrelevant. Transport and commercial connections to cities in central and western provinces, particularly along the Yangzi River, will improve significantly; improvements in logistics and transport services could lead to Shanghai's consolidation as the gateway to the largest market region in China. By the end of this decade—if it continues to build upon its many inherent competitive advantages through the consistent pursuit of innovation—Shanghai could well become China's principal nexus to the global economy.

Not all foreign companies will need to locate in this nexus. Each company's business case will differ; profitability growth will depend on the specialized roles that individual companies expect from a wide range of cities in China—as markets, production locations, distribution nodes, and centers for supporting services. Yet one thing is certain: wherever individual companies focus across the Chinese landscape, Shanghai will play an increasingly important role in growing corporate profitability if, as seems likely, it eventually becomes China's first globally competitive city.

Snapshots of China:

A New US-China Business Council Report

The US-China Business Council has regularly published research reports on a variety of Chinese commercial topics, especially in areas such as distribution, retail, human resources, and the environment.

Now that China has entered the World Trade Organization (WTO) and is promoting the development of areas beyond the coast, a forthcoming Council report reviews China's provinces, autonomous regions, and province-level cities in an attempt to answer one of foreign investors' most frequently asked questions: "Where can we find information on different regions of China to help us evaluate, and plan strategically, where our companies should set up operations after China's WTO phase-ins take place?"

China-based company representatives who have tried to obtain such information can appreciate how difficult it is to find. So far the primary options have consisted of hard-to-read provincial brochures, expensive specialist research reports, or, for the less commercially oriented, the *Lonely Planet* guidebooks.

A handy reference

The report aims to be a reference for the experienced China trader as well as the new market entrant. Each profile features key information on the region and its major cities, as well as statistics and contact information for relevant provincial and municipal officials.

Our researchers sought information from the respective authorities as if they were corporate staff taking a first look at potential investments in or trade with China. After jumping the initial hurdle of gaining the mandatory National Bureau of Statistics approval for our study, they sent a lengthy questionnaire in Chinese to each provincial and major city government. They followed up with countless phone calls to clarify submitted information. All conversations took place in Chinese.

The researchers had to deal with a matrix of officials at a variety of bureaucratic levels and systems (*xitong*) in each region. Some of these officials were prompt and professional in their responses. Others were surprisingly reluctant to provide even the most basic information; in many cases providing such information was among these officials' responsibilities. Moreover, the Council's Beijing office regularly hosts visitors from the governments of all of China's provinces and major cities who are anxious to promote their local investment opportunities.

Tempting as it may have been at times, the Council deliberately did not reach out to its contacts in the regional leadership to make the lower levels of bureaucracy respond. Such an approach would have defeated the basic premise of the research. Rather, we contacted the specific departments in charge, just as any company would have to do.

Contrary to popular belief, not all Chinese data are incorrect. The Council compared the numbers provided by each region with central-level information. In the event that there were significant discrepancies, we used the central government's numbers, all of which were checked and re-checked from multiple sources. Skeptical readers, however, might opt to consider the numbers as indicative of trends.

The report refrains from regaling readers with war stories and colorful anecdotes, because the Council has found that every business has a different experience in China based on its approach. Indeed, China is what you make of it—with a well-planned strategy, the right people on the ground, and above all, persistence, a company can be successful even in the toughest PRC commercial environments.

—Patrick J. Powers

Patrick J. Powers is director of China Operations at the US-China Business Council in Beijing.

Gansu Province

A province in China's poor interior sets its sights on foreign trade and investment

Most of sparsely populated Gansu Province sits between 1,000 and 3,000 meters above sea level. With more than 30 percent of its area covered by grassland, Gansu is a rural, agricultural province as well as the country's second-largest producer of traditional Chinese medicines, with over 9,500 types in production, according to the Gansu Development Planning Commission. It is also one of China's five bases of animal husbandry.

Gansu's agricultural industry produces primarily melons, vegetables, and the beer ingredients hops and barley. The agricultural centers are located in eastern Gansu, the Yellow River valley, and the northwestern Hexi corridor. The Hexi corridor, on the old Silk Road, is Gansu's most prosperous agricultural area and one of 12 national bases of commodity grain production. The corridor is the site of both the Northwest Seedlings Production Base and the Northwest

This provincial overview is an excerpt of a forthcoming US-China Business Council report.

Gansu, 2000

Population: 25.57 million
Per capita GDP: $464 (+7.8%)
Average urban disposable income: $594 (+9.9%)
Average urban spending: $498 (+12.1%)
Average rural spending: $131
Urban-rural resident ratio: 24:76
Number of administrative areas: 87
Mobile phone users: 650,000
Number of cars: 220,000

Gansu accounts for:

2.0% of China's total population
1.1% of China's total GDP
0.2% of China's total contracted foreign direct investment (FDI)
0.2% of China's exports
0.1% of China's imports

Economy

GDP: $11.88 billion (+5.5%)
Fixed-asset investment: $5.33 billion (+14.9%)
Value-added industrial output: $3.97 billion (+10.2%)
Retail sales: $4.38 billion (+9.4%)
Government revenue: $1.31 billion (+5.22%)
Government expenditures: $2.27 billion (+27.4%)

FDI

Number of contracts: 76 (+12.0%)
Amount contracted: $123.4 million (+15.0%)
Amount utilized: $62.4 million (+22.2%)
Top five investors (amount contracted):

1. United States	$54.1 million
2. Hong Kong	$20.4 million
3. South Korea	$18.3 million
4. Israel	$8.9 million
5. Canada	$4.0 million

Foreign Trade

Total trade: $569.5 million (+40.0%)
Exports: $415.0 million (+31.0%)
Imports: $154.6 million (+73.0%)
FIE exports: $38.8 million (9.4% of total exports)
Top five trade partners (total trade):

1. Japan	$170.0 million
2. United States	$57.0 million
3. South Korea	$48.1 million
4. Australia	$48.0 million
5. Singapore	$28.2 million

SOURCE: Gansu Trade and Economic Cooperation Office, Foreign Investment Administration Department
NOTE: All growth rates are compared to the same period in 1999 except where indicated.

Seeds Breeding Base, a 253-hectare area open to foreign investment in seed supply, technology, and related equipment.

The Hexi corridor is also home to Jinchuan, the location of China's largest—and the world's second-largest—nickel reserve, containing 5.5 million tons. The corridor, which yielded 40,000 tons of nickel in 2000, also has major deposits of copper, gold, iron, lead zinc, and tungsten. Other Gansu mineral reserves include 8.6 billion tons of coal and 80.6 million tons of oil.

Gansu's major industries derive from these natural resources and include nonferrous metals, petrochemicals, energy, machinery, food processing, and building materials.

Gansu Investors

Major Corporate Investors

1. CEA Co.	$80.2 million
2. Hong Kong China Tourist Group Co.	$54.3 million
3. GT International Co., Ltd.	$42.3 million
4. Hong Kong Golden Gulf Investment Co.	$38.6 million
5. US Lubrizol International Management Co.	$32.4 million

Major US Investors

1. CEA Co.	$80.2 million
2. US Lubrizol International Management Co.	$32.4 million
3. Alltes International Inc.	$20.0 million
4. Now International Inc.	$10.4 million
5. Tang Energy Group, Ltd.	$2.5 million

SOURCE: Gansu Trade and Economic Cooperation Office

Economy highlights

- Gansu's GDP reached $12.96 billion in 2001, up 9.4 percent over 2000. Gansu's consumer price index fell 0.5 percent in 2000.
- Gansu's 2000 grain output fell to 7.13 million tons, a 12.5 percent decrease from 1999. In contrast, output of medicinal ingredients rose 107.5 percent, to 159,000 tons.

Foreign direct investment

In 2001, Gansu's contracted foreign direct investment (FDI) rose 29.7 percent over 2000, to $160 million, while utilized FDI grew 19.3 percent, to $74 million. According to the Gansu Trade and Economic Cooperation Office (GTECO), US companies account for 183 of the 1,619 foreign-invested enterprises (FIEs) in Gansu. FIE exports rose 12 percent in 2000 to reach $38.8 million—9.4 percent of Gansu's total.

Attracting foreign investment

To increase foreign investment and satisfy existing investors, the Gansu provincial government has opened several centers to serve investors' needs. The FIE Consulting Center, the FIE Complaint Center, the FIE Dispute Resolution Center, and the Gansu Foreign Business and Investment Promotion Joint Service Center offer assistance from knowledgeable staff.

Trade

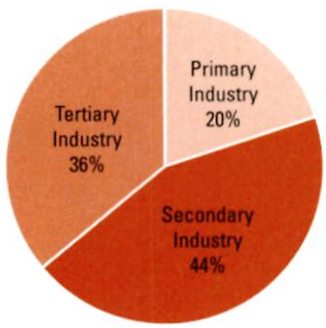
Gansu's total trade in 2001 rose 36.8 percent to $779 million, buoyed by annual import growth of 95.7 percent. While imports hit $303 million, exports rose a more modest 14.8 percent to $476 million. Export growth was spurred partly by government efforts to create 10 new industrial export bases in the province.

Because of Gansu's inland location, the provincial government provides transport subsidies for qualifying domestic and foreign exporting enterprises. Interested enterprises may contact the provincial department of finance for more information.

Tourism

Perhaps because of its remote location, Gansu does not rank among the top tourist destinations in China. In 2000, the province attracted 210,000 foreign tourists, less than 8 percent of the 2.8 million foreign tourists who paid visits to the country's leading tourist destination, Beijing. Yet Gansu has significant unrealized potential as an outpost of China's tourism industry, thanks to its UNESCO World Heritage-listed Dunhuang Mogao grottoes and

Gansu Industry Makeup



Population of Major Cities in Gansu

Baiyin	*www.by.gansu.gov.cn*	1.72 million
Jinchuan	*www.jinchuan.gansu.gov.cn*	0.45 million
Lanzhou	*www.lz.gansu.gov.cn*	2.93 million
Tianshui	*www.tianshui.gov.cn*	3.38 million

Goals for 2002 and Beyond

Major Investment Goals

- Comprehensive natural resource development
- Infrastructure construction: In 2001, the Gansu government declared that it would invest around $80 million over the next three years in the province's water supply system. The province is also planning major upgrades to its rural electricity grids as well as the laying of fiber optic cable to upgrade the provincial telecommunications network.
- Ecological construction and environmental protection
- Science and technology education

Tenth Five-Year Plan (2001–05) Highlights

- Annual GDP increase of 8-9 percent
- Fixed-asset investment up 10 percent per year
- Value-added industrial output up 9 percent per year
- Value-added agricultural output up 5 percent per year
- Foreign trade exports up 10 percent per year
- Unemployment rate below 5 percent
- Population growth below 0.9 percent

SOURCES: Gansu Trade and Economic Cooperation Office, press reports

Major Development Zones

National-level Zone:

Lanzhou State New and High-tech Industrial Development Zone
Email: gxqzsj@sina.com;
Tel: 0931-826-7574

Provincial-level Zones:

Jinchang New and High-tech Industrial Development Zone
Tel: 0935-821-2340
West Baiyin Area
Tel: 0943-822-3900;
Fax: 0943-822-3900
Linxia Economic Development Zone
Tel: 0930-638-3152

its history as a stop on the Silk Road. And in the Gansu town of Jiayuguan lies the western terminus of the Ming Dynasty-era Great Wall. The city government of Dunhuang is trying to strengthen the tourism industry and announced in 2000 that it was seeking domestic and overseas investment to build a new tourism economic zone near Dunhuang's Yitang Lake.

Politics

Gansu Communist Party Secretary Song Zhaosu rose through the political ranks of his native Henan, ultimately becoming vice governor in 1988 and deputy secretary of the Henan Communist Party from 1993 to 1998. Song served as acting governor and then governor of Gansu from 1998 to 2001, when he was appointed to his current position.

A Hebei native, Gansu Governor Lu Hao graduated from Lanzhou University with a degree in chemistry and has lived in Gansu ever since. Lu was named governor in January 2001, having served previously as Lanzhou's Party secretary.

WTO preparations

According to GTECO, the province is making efforts to adjust its government structure to create an environment, based on international practices, that is conducive to economic development. As part of this process, officials have instituted a mandatory World Trade Organization (WTO) basic-knowledge test; officials must pass the test to be eligible for annual salary increases. Gansu, GTECO says, is also in the process of improving its science and technology resources as well as its legal framework to improve its international competitiveness. 完

Gansu Contacts

Government and Party Leadership

Party Secretary: Song Zhaosu
Governor: Lu Hao
Vice Governors: Guo Kun, Cui Zhenghua (portfolio includes foreign trade and investment), Yun Xiaosu, Luosang Linzhiduojie, Wu Bilian, Li Zhongan

Government Offices

China Council for the Promotion of International Trade
Director: He Qianqing
Address: 280 Xiaoshaomenwai, Chengguan District, Lanzhou 730030
Tel: 0931-872-9168; Fax: 0931-884-4197
Liaison Department
Tel: 0931-883-0479; Fax: 0931-886-9483

Ministry of Foreign Trade and Economic Cooperation
Director: Mao Yusheng
Address: 386 Dingxi Rd., Lanzhou 730000
Tel: 0931-861-6321; Fax: 0931-861-8083
Foreign Investment Department
Tel: 0931-861-6321; Fax: 0931-861-8083

State Administration for Industry and Commerce
Address: 120 Gannan Rd., Lanzhou 730000
Tel: 0931-841-6086; Fax: 0931-882-5697
Enterprise Registration Department
Tel: 0931-841-5282; Fax: 0931-882-5697

State Development Planning Commission
Director: Zhao Kewen
Address: Zhongyang Guangchang, Lanzhou 730030
Tel: 0931-848-9851; Fax: 0931-848-4190
Foreign Capital Utilization Department
Tel: 0931-846-5581; Fax: 0931-848-4190

State Economic and Trade Commission
Director: Ren Jidong
Address: 1 Zhongyang Guangchang, Lanzhou 730030
Tel: 0931-846-2467; Fax: 0931-846-3087
Foreign Economics and Trade Department
Tel: 0931-846-2501; Fax: 0931-846-3087

Other Offices

Provincial Department of Finance
Address: 136 Jinning Rd., Lanzhou 730030
Tel: 0931-881-1297; Fax: 0931-882-9756

Gansu Foreign Business and Investment Promotion Joint Service Center
Address: 386 Dingxi Rd., Lanzhou 730000
Tel: 0931-861-6321, ext. 8239, 8293; Fax: 0931-862-3860

Gansu FIE Legal Consulting Center
Address: 386 Dingxi Rd., Lanzhou 730000
Tel: 0931-861-6321, ext. 8293, 8260; Fax: 0931-862-3860

Gansu FIE Complaint Center
Address: 1 Zhongyang Guangchang, Lanzhou 730030
Tel: 0931-848-0470

Gansu FIE Mediation Center
Address: 386 Dingxi Rd., Lanzhou 730000
Tel: 0931-848-0470; Fax: 0931-862-3860

Lanzhou, Gansu

Lanzhou GDP

GDP, RMB billion	Year
2.79	1996
2.95	1997
3.13	1998
3.33	1999
3.74	2000

Useful Websites

Lanzhou Government
www.lz.gansu.gov.cn
Lanzhou Window
www.lzvw.com.cn
Lanzhou Information Port
www.lzxxg.com

Located near the headwaters of the Yellow River at the geographic center of China, Gansu's capital city is fast becoming a major trade center for provinces in the north and west, such as Xinjiang and Qinghai. With four major national rail lines converging at Lanzhou, the city is a transfer center for containers being shipped along the Euro-Asian continental line, and the Lanzhou Western Railway Station is home to the largest cargo marshalling yard in China's Northwest. Already a petrochemical base, the city's oil and gas industry stands to benefit from the construction of the central government's west-to-east gas pipeline, which will pass through the city on its course from Xinjiang to Shanghai. Lanzhou is also a major physics research center, home to an advanced particle accelerator at the Heavy Ion Research Facility.

Lanzhou is not a pretty place. Arriving at the airport, about an hour's drive from the city center, one is struck by the bleakness of the landscape and the pollution—in fact, Lanzhou is generally considered to be one of the most polluted cities in China.

From a commercial point of view, however, Lanzhou is likely to be a pleasant surprise for the typical investor with low expectations. Indeed, the Lanzhou government is well aware of its shortcomings and in recent months has taken steps to cut down on pollution and position itself as a more attractive commercial destination, according to city officials. One of the more interesting decisions has been to take on the challenging task of ending local protectionist measures that have blocked trade with other provinces, with the goal of raising the volume of overall commerce and attracting service industries.

As an indication of local interest in this market, major Chinese chain stores are moving into Lanzhou at a rapid pace. Some foreign retailers have also indicated that, though other cities might have greater sales volumes, Lanzhou's relatively low costs allow for greater returns and higher profits. Lanzhou also compares favorably with higher-profile rival Xi'an, capital of Shaanxi, in ease of facility construction. For example, archeological discoveries often slow down construction efforts in Xi'an, whereas many foreign investors report that building projects in Lanzhou can be completed quickly and inexpensively.

Economy highlights

- In 2000, agriculture accounted for 5.1 percent of Lanzhou's GDP, while manufacturing and services accounted for 52.7 and 42.2 percent, respectively.
- Lanzhou's Dongbu general goods wholesale market is one of the largest of its kind in China and the 49th largest market overall, registering $525 million in 2000 turnover.

FDI

- By the end of 2000, Lanzhou's cumulative utilized FDI reached $340 million.
- In total FDI, Hong Kong's investment of $487 million leads the pack, followed by the

Lanzhou Contacts

Government and Party Leadership

Party Secretary: Wang Jun
Vice Mayor in charge of foreign trade and investment: Liu Yajun
Mayor: Zhang Zhiyin (acting)

Government Offices

China Council for the Promotion of International Trade
Director: Yang Yongzhong
Address: 699 E. Binghe Rd. 730030
Tel: 0931-843-5482; Fax: 0931-843-5482

Ministry of Foreign Trade and Economic Cooperation
Director: Qian Xiuwu
Address: 75, N. Xinchang Rd. 730030
Tel: 0931-883-4840; Fax: 0931-885-3143
Foreign Investment Department
Tel: 0931-883-2041

State Administration for Industry and Commerce
Director: Wang Xihu
Address: 135 Yongchang Zhong Rd. 730030
Tel: 0931-843-5140; Fax: 0931-843-5140
Foreign Investment Department
Tel: 0931-843-5192

State Development Planning Commission
Address: 509 E. Binghe Rd.
Tel: 0931-883-7057
Foreign Economic Department
Tel: 0931-886-1935

State Economic and Trade Commission
Director: Zhang Yixiang
Address: 244 W. Mingzhu Rd., Chengguan District
Tel: 0931-466-5121; Fax: 0931-466-0697

Lanzhou, 2000

Population: 2.93 million
Per capita GDP: $1,244 (+6.8%)
Average urban disposable income: $707 (+14.1%)
Average urban spending: $610 (+12.0%)
Average rural spending: NA
Urban-rural resident ratio: 66:34
Mobile phone users: 300,000+
Internet users: 40,000+

Lanzhou accounts for:

0.2% of China's total population
0.3% of China's total GDP
0.2% of China's total contracted foreign direct investment (FDI)
0.1% of China's exports
0.05% of China's imports

Lanzhou is home to:

8 administrative areas
1,301 foreign-invested enterprises (FIEs)
144 FIEs with US investment

Economy

GDP: $3.74 billion (+12.4%)
Fixed-asset investment: $1.86 billion (+10.4%)
Value-added industrial output: $2.12 billion (+7.9%)
Retail sales: $1.93 billion (+8.5%)
Government revenue: $0.33 billion (+9.9%)
Government spending: $0.26 billion (+8.7%)

FDI

Number of contracts: 56 (+12.0%)
Amount contracted: $97.2 million (+56.0%)
Amount utilized: $78.0 million
Top five investors (amount contracted):

1. United States	$45.2 million
2. South Korea	$17.2 million
3. Hong Kong	$13.6 million
4. Israel	$8.1 million
5. Canada	$5.1 million

Foreign Trade

Total trade: $403.5 million (+25.4%)
Exports: $281.2 million (+11.9%)
Imports: $122.4 million (+23.7%)
FIE exports: $33.9 million (12.1% of total exports)
Top five trade partners (total trade):

1. Japan	$60 million
2. South Korea	$30 million
3. United States	$25 million
4. Taiwan	$20 million
5. Singapore	$16 million

SOURCE: Lanzhou Foreign Economics Office, National Bureau of Statistics.
NOTE: All growth rates are compared to the same period in 1999 except where indicated.
NA = not available

United States and Taiwan, with $228 million and $204 million, respectively.

- Gansu's first logistics joint venture, worth half a million dollars, was set up in Lanzhou in late 2001 by Canadian Pacific Railway Co., which took a 50 percent stake, and the Lanzhou Railway Administration Container Transportation Co., the Container Transport Center of the Lanzhou Railway Administration Branch, the Container Transport Center of the Yinchuan Railway Administration Branch, and the Container Transport Center of the Xining Railway Administration Branch.

WTO preparations

The Lanzhou municipal government has begun to educate government officials and business leaders about WTO requirements. In early December 2001, a conference featuring WTO experts from various embassies and international agencies took place in Lanzhou. Experts explained what WTO membership will mean for China and what is expected from China to meet its WTO commitments.

Looking ahead: Environmental protection and Yellow River development

Lanzhou has enacted several measures to clean up its environment, including shifting to a greater reliance on natural gas. In December 2001, Lanzhou began operating a 930 km natural gas pipeline originating in neighboring Qinghai's Qaidam Basin.

In addition, the city has numerous plans for the Yellow River. Over the long term, Lanzhou plans to build 25 hydropower stations along the river with a total capacity of 15 million kW. Other plans call for re-foresting the banks of the river, renovating river tourist points, and dredging the river bed and reinforcing river banks to facilitate water transport. 完

Selected Business Hotels

Lanzhou Legend Hotel
Address: 599 Tianshui Rd., Lanzhou 730000
Tel: 0931-888-2876; Fax: 0931-888-7876
www.lanzhoulegendhotel.com

Hotel Savoy Lanzhou
Address: 788 Xijin West Rd., Qilihe District, Lanzhou 730050
Tel: 0931-256-6868; Fax: 0931-258-0668

Lanzhou Hotel
Address: 434 Donggang Rd. West, Lanzhou 730000
Tel: 0931-841-6321; Fax: 0931-841-8608

Lanzhou Indicators

McDonald's restaurants:	0
Kentucky Fried Chicken restaurants:	1
Jeans West stores:	3

Major American Investors:
US Lubrizol International Management Co. ($29.5 million)
Now International, Inc. ($10.4 million)

SOURCE: Lanzhou Foreign Economics Office

Major Development Zones

National-level zone:
Lanzhou State New and High-tech Industrial Development Zone
E-mail: gxqzsj@sina.com;
Tel: 0931-826-7574

Lanzhou Municipal Government's Sectors of Emphasis

- Ecological environmental construction
- Comprehensive agricultural development
- Energy, transportation, and telecommunication infrastructure
- New and high-tech industries
- Petrochemicals
- Medicines
- Building materials
- Exploitation of mineral products

Shenyang, Liaoning

Although its reputation has been marred in recent years by major corruption scandals, efforts over the past year to clean things up could make Shenyang one of China's more attractive foreign investment destinations, if not an obvious first choice. With its well-developed transportation links into Heilongjiang and Jilin provinces and Beijing, Shenyang—capital of Liaoning and China's fifth-largest city—is the largest commodity distribution center in northeast China and the retail center for the densely populated central Liaoning region. It is also a major manufacturing base for machinery, automobile production, pharmaceuticals, chemicals, and metallurgy.

Economy highlights

- Shenyang's unemployment rate soared—and jobless workers protested—in the late 1990s, as key state-owned enterprises laid off large numbers in a bid to reform traditional industries. Today, unemployment rates remain high, as they do throughout China's northeast rust belt, but

This city overview is an excerpt of a forthcoming US-China Business Council report.

Though not an obvious first choice, Shenyang has the potential to become an attractive foreign investment destination.

efforts are under way to improve the situation. Liaoning and Shenyang are in the midst of a three-year social welfare and pension reform program that began in summer 2001. If successful, the reform program will extend to the rest of China.

- Primary industry accounted for 6.4 percent of Shenyang's GDP in 2000, while secondary and tertiary industries accounted for 44.3 and 49.3 percent, respectively.
- Shenyang Jinbei Auto-making Co. manufactures the "Zhonghua" car, the first car for which China holds full intellectual property rights.
- Shenyang is home to nearly 100 software companies employing nearly 15,000 software developers.

Foreign direct investment

- By the end of 2000, 220 of Shenyang's 1,049 industrial enterprises were foreign-invested. Those FIEs contributed 24.1 percent of industrial output in 2000.
- Major foreign investors in Shenyang include The Boeing Co., Compaq Computer Co., and IBM Corp. General Motors Corp. is 50 percent owner in a $230 million sport utility vehicle production venture, Jinbei GM Automotive.
- Shenyang is home to the representative offices of Sumitomo Bank (Japan) and the Commercial Bank of Holland as well as one Sino-foreign insurance joint venture, Taikang Life, a life insurance venture with funding from China, Japan, Singapore, and Switzerland.
- Shenyang has made a concerted effort to attract overseas Chinese investment by establishing the Shenyang Overseas Chinese Incubation Park in the Hunnan Industrial Quarter of the Shenyang High-tech Industrial Development Zone. This zone attracted $550 million worth of foreign investment in contracts in 2000.

Politics

In the recent past, corruption severely stunted Shenyang's economic development. Charges of high-level bribery, gambling with public funds, and gang-related activities resulted in the conviction of the mayor and other high-level officials and the execution of a vice mayor. In early 2001, both Mayor Chen Zhengao, a former Liaoning vice governor, and Liaoning Governor Bo Xilai were appointed to head anticorruption efforts. President Jiang Zemin's fall 2001 visit to Shenyang signaled that these efforts were successful and that both the city and province were open for legitimate business.

WTO preparations

The Shenyang Municipal Government is in the process of reviewing and revising laws to ensure that they are World Trade Organization (WTO) compliant. Shenyang is also educating its government officials, business leaders, and citizens on WTO requirements and WTO-related challenges through regular newspaper segments as well as the publication of a book, *WTO and Shenyang.* 完

Shenyang, 2000

Population: 6.85 million
Per capita GDP: $1,968
Average urban disposable income: $707
Average urban spending: $616
Average rural spending: $241
Urban-rural resident ratio: NA
Mobile phone use: 16.7% of city population
Internet use: 3.4% of city population

Shenyang accounts for:

0.5% of China's total population
1.2% of China's total GDP
2.8% of China's total contracted foreign direct investment (FDI)
0.5% of China's exports
0.6% of China's imports

Shenyang is home to:

12 administrative areas
3,674 foreign-invested enterprises (FIEs)
214 FIEs with US investment
0 multinational research and development centers
2 representative offices of foreign banks
1 joint-venture insurance office
1 US consulate

Economy

GDP: $13.48 billion (+10.3%)
Fixed-asset investment: $3.17 billion (+9.2%)
Value-added industrial output: $5.33 billion (+11.2%)
Retail sales: $6.84 billion (+9.7%)
CPI: +0.1
Government revenue: $0.73 billion (+9.1%)
Government expenditure: $1.12 billion (+16.2%)

FDI

Number of contracts: 646
Amount contracted: $1.45 billion (+33.4%)
Amount utilized: $0.71 billion (+42.9%)
Top five investors (amount contracted):

1. UK Virgin Islands	$630 million
2. United States	$250 million
3. South Korea	$240 million
4. Hong Kong	$140 million
5. The Netherlands	$30 million

Foreign Trade

Total trade: $2.68 billion (+47.7%)
Exports: $1.30 billion (+62.3%)
Imports: $1.39 billion (+36.3%)
FIE exports: $0.86 billion (66.2% of total exports)
Top five trade partners:

1. United States
2. South Korea
3. Japan
4. Germany
5. The Netherlands

SOURCES: Shenyang Statistics Bureau, Shenyang Foreign Investment Promotion Bureau, and Shenyang China Council for the Promotion of International Trade (CCPIT)
NOTE: All growth rates are compared to the same period in 1999 except where indicated.
NA = not available

Looking Ahead

Top Infrastructure Projects

- Shenyang Commerce and Technology Mansion construction
- Western area sewage treatment plant project, worth $143 million
- Shenyang logistics base project, worth $12.8 million
- Hunnan trash-burning power plant project, worth $70.1 million
- Northeast area daily trash treatment center project, worth $59.2 million

Municipal Government Sectors of Emphasis

- Automobile industry
- Equipment manufacturing
- Pharmaceuticals and chemicals
- Information technology
- Environmental protection

Tenth Five-Year Plan (2001-05) Highlights

- Annual GDP increase of 9.2 percent
- Fixed-asset investment up 11 percent per year
- Industrial output up 17.2 percent per year
- Agricultural output up 4.4 percent per year
- Retail sales up 9 percent per year
- Foreign trade exports up 21 percent per year
- Consumer price index up 0.02 percent per year

SOURCE: Shenyang CCPIT

Shenyang Indicators

McDonald's restaurants:	6
Kentucky Fried Chicken restaurants:	10
Jeans West outlets:	7

Major Corporate Investors:

1. Shenyang Jinbei Passenger Vehicle Co.	($299 million)
2. Shenyang Hangtian-Mitsubishi Engine Manufacturing Co.	($264 million)
3. Jinbei-General Motors Automobile Co.	($231 million)
4. Shenyang Shenhai Thermal	($171 million)
5. Shenyang Huarun-Sanyo Condenser Co.	($159 million)

Top US Invested Projects

1. Jinbei-General Motors Automobile Co.	($231 million)
2. Kelaisite International Property	($89.6 million)
3. Shenyang Lido Hotel	($78.2 million)
4. Shenyang Holiday Mansion	($30.0 million)
5. Shenyang Green Organic Fertilizer Co.	($30 million)

SOURCE: Shenyang CCPIT

Shenyang Contacts

Government and Party Leadership

Party Secretary: Zhang Xingxiang
Mayor: Chen Zhenggao
Vice Mayors: Li Jia, Sun Xiangjian (portfolio includes foreign trade and investment), Lu Yihuan, Li Baoquan, Zhao Changyi

Government Offices

China Council for the Promotion of International Trade
Director: Li Huanian
Address: 55 Renao Rd., Shenhe District 110014
Tel: 024-2292-0972; Fax: 024-2292-0973
www.ccpit-sy.org.cn
Liaison Department:
Tel: 024-2292-0975; Fax: 024-2292-0973

Ministry of Foreign Trade and Economic Cooperation
Director: Song Qi
Address: 35 Qingnian Dajie, Shenhe District 110014
Tel: 024-2282-8050; Fax: 024-2272-4746
Foreign Investment Department:
Tel: 024-2272-4746; Fax: 024-2272-4746

State Administration for Industry and Commerce
Director: Gai Shilin
Address: 118 Nanguan Rd., Shenhe District 110016
Tel: 024-2401-1114; Fax: 024-2411-2911
Foreign Investment Department:
Tel: 024-2252-6500; Fax: 024-2252-6055

State Development Planning Commission
Director: Shen Wenbo
Address: 260 Shifu Dalu 110013
Tel: 024-2272-1604; Fax: 024-2272-0662
Foreign Investment Department:
Tel: 024-2272-1132; Fax: 024-2376-8009

State Economic and Trade Commission
Director: Gu Chunli
Address: 260 Shifu Dalu 110013
Tel: 024-2272-8904
www.syjmw.com

Other

Shenyang Foreign Investment Promotion Bureau
Tel: 024-2287-5200; Fax: 024-2287-5201
E-mail: syfipb@pub.sy.ln.cn

Selected Shenyang Business Hotels

Hotel Inter-continental
Address: 208 Nanjing North Street, Heping District 110001
Tel: 024-2334-1999; Fax: 024-2334-1199

Marriott
Address: 388 Qingnian Da Street, Heping District 110003
Tel: 024-2388-3456; Fax: 024-2388-0677

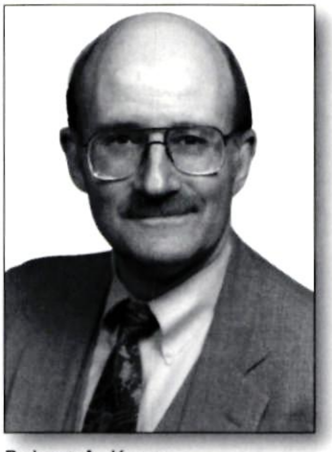
Sheraton Shenyang Lido
Address: 386 Qingnian Street, Heping District 110004
Tel: 024-2318-8888; Fax: 024-2318-8800

Shenyang GDP, RMB billion

1996	9.32
1997	10.28
1998	11.34
1999	12.24
2000	13.48

Useful Websites

Shenyang Municipal Government
www.shenyang.gov.cn
Shenyang Statistics Information Net
www.sysinet.gov.cn
Shenyang Foreign Investment Service Center
www.syfisc.gov.cn
A Window on Shenyang
www.shenyang.com.cn
Shenyang Government Procurement
www.sy-procurement.gov.cn



Robert A. Kapp

LETTER from the President of the US-China Business Council

Business, Economics, and Security

The US-China Security Review Commission's bold statement that trade and national security issues relating to China are inseparable is closer to the mark than most American businesses may realize.

The best thing to do with the recently published *Report of the United States-China Security Review Commission* (USCC) is probably to read the executive summary and move on.

In its unrelievedly grim view of China's modernization and the threats it poses to American economic and military security, the report offers few, if any, surprises. The exception was a dignified dissent by a lone commissioner, a former Commerce Department export control boss, who faulted the document for its one-sidedness and disingenuousness.

In fact, while the report can be criticized for its relentless, jackhammer-like concentration on the military and economic threats it believes China may pose to the United States—and for ignoring the impressive array of easily accessible information and expert opinion that did not conform to the widely publicized preconceptions of many commissioners—the remarkable thing about the document is how relatively bloodless most of its suggestions turned out to be. Various recommendations of the "guilty until proven innocent" variety will be highly unpalatable to those doing business in, or with, China and should not become US law or policy. The implicit premises of others (e.g., that Chinese students and scholars in the United States must be regarded as special security risks) are questionable or objectionable. But all in all, the report's recommendations are strangely bland, and a few—like the proposal for stronger federal support of Chinese-language study or for US support of rule of law programs in China—will cause no heartburn at all.

In and of itself, this document, and the accompanying gigantic compendium of contracted papers by researchers of predictably strong affinity to the outlooks of their commission patrons, will not prove to mark the moment when the United States and China finally head off to enlist in the new Cold War. As one colleague with a long, uniformed military background put it, "For the amount of time, money, and effort put into the USCC, this first report appears to be destined to be a minor footnote in the scheme of US-China relations."

But before this report is filed away, it is worth pointing out a few matters that US business should not lightly dismiss.

1 The report's bold opening statement that trade and national security issues relating to China are inseparable is closer to the mark than most American businesses may realize. It is already clear, in business sectors beyond the defense sector, that the complex security relationship between the United States and China cannot be pigeonholed or wished away by companies that "just want to do business."

2 The US-China security realm, already the home of a large and growing army of analysts, gamers, and congressional staffers on the US side and similar legions in China, is multidimensional. It grapples with technological change. It is beset by critical inadequacies of information that nurture unfettered speculation that sometimes feeds on itself.

3 The politically pregnant implication that because US economic engagement with China is beneficial to China it is bad for US security (leave aside that it is also good for the United States) is not going to go away, either. Those who take China's economic advancement as dangerous *per se* to the United States perceive thriving two-way business as a clear and present danger. They do not concern themselves any more today with the broader implications of its disruption than they did in the old days when they opposed Most Favored Nation or Permanent Normal Trade Relations on similar grounds.

4 Most of the research and analysis in this burgeoning field is unconcerned with US-China commercial and economic relations; primarily military, it sometimes touches on na-

tional economic strength as a strategic factor, but it does not spend time on the substance of US-China trade and investment, let alone on the benefits to the United States arising from that commerce.

5 Given the opacity of China's policymaking, politics, and military affairs to most American observers, creative speculation about China's ultimate motives and its most fundamental behavioral traits flourishes in this literature. This is the realm of pop Sinology, of high-sounding quotations from the fifth-century BC classic of military strategy the *Sunzi Bingfa*, of easy references to "Chinese culture." A typical example would be the familiar but unsupported assertion that China in the twenty-first century is bent on restoring the world-subduing grandeur of its imperial dynasties.

6 In the security dialogue, based as it seems almost always to be on the identification and assessment of threat, there is little analysis of the complex cycles of action and response between the United States and China that even a serious newspaper reader can discern. Analysis concentrates on what the other side does, with little acknowledgment of what the analyst's own side does. To their credit, some researchers have faulted such analyses for this very omission, but the habit of ignoring the interactive dimension of US-China (and US-Taiwan-China) security dilemmas persists.

7 In the United States, some of the security dialogue on China takes place in environments to which most business and other lay people have no access. But a lot of it is in the newspapers, the magazines, the think tank reports, and the Worldwide Web. In these publicly available materials, two characteristics stand out. First, duplication and repetition: one can read essentially the same article over and over again, especially if one stays within the closed circuit of analysts lashed to the same ideological moorings. Second, a paucity of authoritative consensus as to what the data mean and what the future holds. (One aspect of this is the divergence between the study of "capabilities" and the study of "intentions," in which some argue that, because intentions can always change from benign to malignant, only capabilities count, and others argue that all the hardware and software in the world won't amount to much if the political, administrative, and human resource systems behind them don't conduce to its effective use.)

8 This yields interesting results. Much of the security dialogue, including the USCC report for the most part, appears to take the form of conversations among the faithful: apocalyptic analyses cite the same experts as their sources, and are in turn cited by those experts in the next round of the cycle. Contrary argument, or testimony that fails to conform to the predispositions of the analysts, is ignored or disregarded. Looking in on this realm from the outside, one senses that before there are facts there is received truth. In that may lie genuine peril.

Does all of this mean that every US maker of plywood or tea kettles, or seller of auto insurance, or developer of office software should establish an in-house Department of US-China Security Research? Of course not. But on the basic question of the confluence of economic engagement and the national security debate, the very existence of the USCC report is a wake-up call.

The suggestion that American companies—whose $100-plus billion dollars' worth of annual merchandise trade alone is a central and fundamentally positive component in the overall US-China relationship—might have a legitimate interest not only in the outcome of the US-China security dialogue but in the way the dialogue is constructed will not be well received in many quarters, including some within business itself. It is a standard axiom in what I call "attack circles" that American companies, in the search for profits, will do *anything*—including disregarding US national security concerns—in order to make China's "bad actors" happy and to sell-sell-sell to them. The crisis of public confidence in corporate ethics in 2002 gives too-easy credence to that axiom, and opportunists have already seized on it.

At the same time, some polemicists and journalists will regard business expressions of concern, interest, or opinion on security topics as another "crossing of the Rubicon"—another case of business overstepping its bounds and trashing the barriers separating the commercial zone of legitimate concern from the non-commercial fields it has no right to inhabit.

But it is not business that has declared these demarcation lines null and void. While we should not inflate the significance of a single report that largely recapitulates hoary polemics, the broad policy issues at stake in US-China relations will endure indefinitely, and Americans in business have just as real a right to be concerned with them as do other Americans who make their livings measuring military sealift capacity or expounding on China's "Assassin's Mace Weapons," or deciding for the laity what the real size of China's opaque military budget is. If we are lay people on such topics, so be it; the issue is too important to be left to the priesthood alone. 完

Council Bulletin

Event Wrap-Up

Washington

July

Issues Luncheon: A Conversation with Lan Lijun, Newly Arrived Minister of the PRC Embassy

Meeting: Qinghai Province Governor and Delegation Featured Governor Zhao Leji and an 11-person delegation of senior officials from Qinghai Province, visiting the United States under the auspices of the America-China Economy and Cultural Cooperation Organization. Members of the delegation included An Pingsui, president, Board of Directors and general manager, Qinghai Salt Lake Industrial Group Co., Ltd.; Liu Guiyou, director, Information Office; Liu Ning, director, Foreign Affairs Office; Ma Haili, vice director, Financial Department; Miao Xiaolei, president, Qinghai Investment Group Co., Ltd.; Wang Dingbang, director, Government Affairs Office; Xie Xiaoping, director, Foreign Affairs Office; Xun Xingcai, secretary; Li Pengxin, governor, Haixi Autonomous Prefecture; Zhang Yijiong, mayor, Xining Municipal Government.

Meeting: Gansu Province Delegation Featured a 10-person delegation of Gansu Province director- and deputy director-level officials. Members of the delegation included Bo Yanjie, deputy director general, Department of Human Resources; Deng Zhitao, deputy director, Office of Policy Research and Analysis; Gao Ge, director, Television Art Center, Gansu Provincial Television Station; Huo Ronghui, deputy director general, Administration Office; Li Jianzhuang, deputy mayor, Baiyin City; Li Zhongyi, deputy director, Administration Office, Gansu Department of Trade and Economic Cooperation; Shi Guifang, deputy division chief, Personnel Department, Jiuquan Steel Group Co.; Song Qi, deputy division chief, Investment Department, Gansu Provincial Planning Commission; Wang Kai, director, Office of Legislative Services; Zhang Baojun, deputy director, Administration of Foreign Experts Affairs.

Meeting: Sharon Mann, US Department of Commerce (DOC) Featured Sharon Mann, director for market access and compliance at US DOC's new trade facilitation office in Beijing.

Meeting: William Lash, US DOC Featured William Lash, assistant secretary for market access and compliance.

Beijing

July

Luncheon talk by Dr. Kenneth Lieberthal Featured Kenneth Lieberthal, professor, Political Science and Business Administration, University of Michigan and former special assistant to the president and senior director, Asian Affairs, at the National Security Council.

Shanghai

July

Luncheon talk by Dr. Harry Harding Featured Harry Harding, dean, Elliott School of International Affairs and professor, Political Science and International Affairs, George Washington University.

Advertisers in this Issue

CHINA'S SECURITIES MARKETS OPEN TO FOREIGN INVESTMENT

WALTER HUTCHENS

Foreign investors are eager, but do China's capital markets bespeak caution?

Walter Hutchens is an assistant professor at the Robert H. Smith School of Business, University of Maryland.

The China Securities Regulatory Commission (CSRC) has enacted new rules that allow foreign financial firms to acquire stakes in PRC fund-management and securities companies. Both of the new rules, which took effect July 1, 2002, open the door to foreign investment in a sector that previously has been almost completely off-limits to foreign participation.

The Regulations on the Establishment of Fund-Management Companies with Foreign Equity comply with China's World Trade Organization (WTO) commitments, while the Regulations on the Establishment of Securities Companies with Foreign Equity accelerate the schedule for reform. China's WTO working party report does not mandate liberalization for securities companies until December 2004. However, PRC authorities will keep a firm grip on the industry through business scope restrictions.

A line at the door

China has been developing securities markets for more than a decade. Though not yet large when compared to such foreign markets as the Nasdaq National Market or the New York Stock Exchange, China's stock markets have grown rapidly. The country now has two stock exchanges—one in Shanghai and one in Shenzhen—1,178 listed companies, and total market capitalization of more than $500 billion. China also has more than 68 million brokerage accounts and in June 2002 trading turnover was $49 billion. Though each of these numbers can be qualified in important ways, they accurately suggest that much progress has been made in a relatively short time.

Foreign financial giants are enthusiastic about entering China's securities markets and have already signed a number of technical cooperation agreements and memoranda of understanding for joint ventures in anticipation of the new regulations (*see* Table).

Foreign fund managers are particularly enthralled with the prospect of providing fund-management services to millions of Chinese retail investors who currently speculate in, or "stir-fry" (*chao gu*), stocks directly. China has only five mutual funds—in contrast to more than 7,000 in the United States—and established them only within the last 11 months. (A sixth mutual fund has been approved but not yet established.)

Even if Chinese investors do not buy funds in large numbers, providing them with brokerage services could be lucrative. Underwriting also offers titillating possibilities—a comparatively small number of Chinese companies have accessed public markets thus far, so the potential seems enormous.

Ownership caps

The new rules do not throw the door to China's market wide open, however. Foreign investment in fund-management companies may not exceed 33 percent, and the cap will rise only to 49 percent by December 11, 2004. Foreign investment stakes in securities companies are limited to 33 percent. China is under no obligation to allow foreign ownership beyond these levels for either type of company in the future.

Even though foreign ownership in fund-management companies is currently limited to 33 percent, a foreign investor can be the company's largest shareholder. In contrast, the rules on securities companies make it clear that a single Chinese party must hold one-third of a company's shares, making outright control by a foreign investor impossible.

Investor qualifications

Chinese investors in foreign-invested fund-management and securities companies are subject to the same requirements as investors in domestic fund-management and securities companies. These include stringent capitalization requirements.

Foreign investors in fund-management and securities companies must meet additional, special requirements, and CSRC reserves the right to add any prudential requirements that it deems advisable. Both regulations require that foreign investors be

- located in a country that has "perfected" (*wanshan*) its securities law and supervision and whose securities regulatory authority maintains a cooperative relationship, and has a memorandum of understanding, with CSRC (as have the United States, Hong Kong, and other leading jurisdictions); and
- unsullied by major regulatory or judicial penalties imposed within the last three years.

China is seeking investment from foreign financial firms with industry experience, not from purely financial investors.

Sino-Foreign Fund Management Alliances

Foreign Partner	PRC Partner	Type	Date Established
ABN AMRO Bank (the Netherlands)	Changsheng Fund Management Co., Ltd.	Strategic alliance/Letter of intent	12/2001
Allianz AG (Germany)	Guotai Junan Securities Co., Ltd.	Applied for joint venture	06/2002
American International Group, Inc. (US)	Industrial and Commercial Bank of China	Strategic alliance	04/2001
Bank of Montreal (Canada)	Fullgoal Fund Management Co., Ltd.	Strategic alliance/Letter of intent	02/2001
BNP Paribas SA (France)	Changjiang Securities Co., Ltd.	Applied for joint venture	03/2002
BNP Paribas SA (France)	Shenyin & Wanguo Securities Co., Ltd.	Technical cooperation	06/2001
Commerzbank AG (Germany)	China Southern Securities Co., Ltd.	Technical cooperation	03/2001
Credit Lyonnais Securities Asia (France)	Xiangcai Securities Co., Ltd.	Applied for joint venture	07/2002
Daiwa Securities Group, Inc. (Japan)	Shanghai International Corp.	Technical cooperation	03/2002
Deutsche Bank AG (Germany)	Dacheng Fund Management Co., Ltd.	Technical cooperation	07/2001
Fortis NV (Belgium)	Haitong Securities Co., Ltd.	Strategic alliance/Letter of intent	11/2001
Franklin (Templeton) Resources, Inc. (US)	Guangfa Securities Co., Ltd.	Strategic alliance/Letter of intent	11/2001
HSBC plc (UK)	China Southern Fund Management Co., Ltd.	Technical cooperation	02/2001
ING Groep NV (the Netherlands)	China Communication Securities Co., Ltd.	Technical cooperation	10/2001
Invesco Funds Group, Inc. (US)	Penghua Fund Management Co., Ltd.	Technical cooperation	09/2000
JP Morgan Fleming Asset Management (US)	Hua'an Fund Management Co., Ltd.	Strategic alliance/Letter of intent	08/2000
Prudential plc (UK)	Jiashi Fund Management Co., Ltd.	Technical cooperation	01/2002
Prudential (Prumerica) Financial Inc. (US)	China Everbright Securities Co., Ltd.	Strategic alliance/Letter of intent	11/2001
Schroders plc (UK)	Huaxia Fund Management Co., Ltd.	Technical cooperation	03/2001
Schroders plc (UK)	China Galaxy Securities Co., Ltd.	Technical cooperation	03/2001
Société Générale Group (France)	Fortune Trust and Investment Co., Ltd.	Applied for joint venture	07/2002
UBS Warburg (Switzerland)	Guotai Fund Management Co., Ltd.	Technical cooperation	09/2001

SOURCE: Compiled by US-China Business Council staff from press reports

Foreign-invested securities companies may not engage in A-share brokerage business or proprietary trading of A or B shares.

A foreign investor in a fund-management company must also

- be a "financial institution" (*jinrong jigou*) in the country where it is located;
- have asset management qualifications and experience, if it is the largest shareholder; and
- have paid-in capital of no less than the foreign-currency equivalent of ¥300 million ($36.2 million).

CSRC also limits foreign investors to participation in only two fund-management companies, of which they may be the controlling shareholder of just one.

A foreign investor in a securities company must have

- a license to engage in the securities business in the country where it is based;
- at least 10 years of experience in the financial industry;
- a record of compliance with all risk control requirements of its home country during the previous three years; and
- a "good reputation and business record" in international securities markets.

These requirements reveal that China is seeking investment from foreign financial firms with industry experience, not from purely financial investors. This preference for strategic rather than financial investors has been the dominant pattern in China's reform era: China grants limited market access in exchange for capital, technology, and know-how that will help the country develop. (Under the new rules, capital contributions from foreign investors must be made in cash, though PRC commentators acknowledge that technology and knowledge transfer, particularly with respect to managing mutual funds, is part of what China hopes foreign investors will bring.)

Scope of business

Foreign-invested fund-management companies can provide the same services as domestic fund-management companies, namely, establishing and managing public securities investment funds (*zhengquan touzi jijin*). China issued separate rules on foreign investment in venture capital funds in September 2001 (*see The CBR*, July-August 2002, p. 30).

Foreign-invested securities companies, on the other hand, will not be allowed to do everything that purely domestic securities companies do, even though the new rules require them to have the minimum capitalization required to be a "comprehensive" (*zonghe xing*) securities company. In particular, foreign-invested securities companies may not engage in A-share brokerage business or proprietary trading of A or B shares. These have been key revenue sources for PRC securities companies, particularly since initial public offerings (IPOs) have slowed dramatically.

Foreign-invested securities companies may, however, engage broadly in underwriting stocks and bonds. They may underwrite both A- and B-share issues as well as overseas listings by Chinese companies (N, H, or L shares, as they are sometimes called, depending on whether they are listed in New York, Hong Kong, or London). They will also be permitted to underwrite and provide brokerage services for both government bonds and corporate bonds. Though barred from proprietary stock trading, foreign-invested securities companies can trade government and corporate bonds for their own account.

A spat with MOFTEC

The new rules require only CSRC approval to establish a foreign-invested fund-management or securities company. This is a change from earlier drafts of the rules, which had required a filing for the record (*bei an*) with the Ministry of Foreign Trade and Economic Cooperation (MOFTEC).

MOFTEC officials have already objected to being left out of the approval process, asserting that such investments are governed by China's joint venture laws, which require MOFTEC approval for the establishment of a joint venture. CSRC has retorted that it meant what it said in the new rules—only the Company Law and China's body of securities law will govern foreign-invested fund-management and securities companies.

Resolution of this issue will determine much more than who wins a bureaucratic turf war. Different legal rights inhere in different business forms. For example, joint ventures established under China's foreign investment legal regime provide certain minority shareholder protections and some flexibility regarding profit distribution relative to equity interest. The Company Law does not provide these features for a generic limited-liability company—which is the required form of foreign-invested fund-management and securities companies in the CSRC regulations.

Offshore holdings

Advisors to foreign investors in China often counsel them to create special-purpose offshore vehicles to hold particular PRC investments. This allows for greater flexibility on future transfers, since an offshore transfer may not require PRC approvals. The new rules do not explicitly prohibit such arrangements, but they may make them difficult. For example, the requirement that foreign investors' home countries have cooperative arrangements with CSRC will limit the choices available for offshore registration. And in the case of securities companies, the requirement that foreign investors have a 10-year track record would disqualify recently formed special-purpose vehicles.

CSRC has said that a subsidiary or parent of a financial institution can be the foreign shareholder of a fund-management company if it is qualified but the financial institution is not. This suggests that a special-purpose vehicle could rely on the "financial institution" credentials of its parent to avoid being tainted by findings of wrongdoing within the last three years. The direct shareholder would still have to be capitalized at the high level required under the new rules, however.

Fixation on registered capital

Qualified investors must provide at least ¥10 million ($1.2 million) in registered capital to es-

The "Special Characteristics" of China's Securities Markets

Although the slogan "socialism with Chinese characteristics" has heralded tremendous development, the reality of "stock markets with Chinese characteristics" may not be so salutary. Before accepting the invitation to become shareholders in PRC fund-management or securities companies, foreign investors should consider some of the special traits of China's securities markets.

PRC stock markets serve state-owned enterprises, not entrepreneurs

Under the PRC Company Law, no company may list without three years of continuous profitability. This means that promising start-ups often cannot access China's capital market. In addition, government priorities govern the approval process, so even companies meeting the objective requirements of the law are not always able to list. Almost none of the companies traded on China's stock exchanges are private enterprises. This system limits the potential clients available to underwriters and fund managers.

"Overhang" of unlisted shares

Listed companies in China are "publicly owned" not through their listed shares but through their *unlisted* shares. When a state-owned enterprise converts to a joint-stock company *(gufen youxian gongsi)* and lists, only about one-third of its shares are generally issued to public investors. The rest remain in government hands directly as state-owned shares *(guoyou gu)* or indirectly as legal-person shares *(faren gu)*. Because of this "overhang" of unlisted shares, PRC stock exchanges are not markets for corporate control.

Sealed off from world capital flows

China's currency is not freely convertible. Foreigners with hard currency cannot open an account to trade A shares, which are denominated in renminbi (RMB) and listed in Shenzhen and Shanghai. Chinese citizens cannot legally use RMB to buy overseas equities, such as shares listed on stock markets outside of mainland China or in Hong Kong. China's moribund B-share market (consisting of shares denominated in foreign currency and listed in Shanghai or Shenzhen), has attracted just over 100 issuers and offers little relief from this limitation on RMB convertibility. Though China was pleased to have its currency shield in place during the 1997 Asian financial crisis, the non-convertibility of the RMB on the capital account remains a high wall separating PRC equity markets from international capital flows.

Recent phenomenon

The promotion of stock markets was certainly not on the original agenda of the Chinese Communist Party (CCP). (Indeed, the platform adopted by Mao Zedong and others at the first CCP congress in Shanghai in 1921 called for the abolition of private property.) Even within the context of China's 23-year reform effort, the promotion of securities markets has been comparatively recent. The Shanghai and Shenzhen stock markets were only established in 1990. Key national laws are even more recent—the PRC Company Law came into effect in 1994 and the Securities Law in 1999. Many significant regulatory developments, such as the establishment of the first open-ended mutual funds, have occurred within the last 18 months.

Shifting regulatory environment

The China Securities Regulatory Commission (CSRC) and other government authorities have enacted a large body of regulation to govern China's securities markets, and new rules continue to pour forth. A draft investment fund law will probably be submitted to the National People's Congress this year. While no jurisdiction has a completely static securities law, in China the pace of change is remarkable.

Heavy government direction

When China established stock exchanges in the early 1990s, it aimed not only to enable share issuing and trading but also to *control* such activities (Carl Walter and Fraser Howie make this point in their helpful book *To Get Rich is Glorious: China's Stock Markets in the '80s and '90s*). The PRC government determines which companies can publicly issue stock, what interest rates can be paid on corporate bonds, how much commission brokerage companies may charge, and any number of other matters that might be set by market forces in other jurisdictions.

Corruption

As recent US scandals indicate, no securities regulatory regime can eliminate all fraud. However, most Chinese commentators acknowledge that corruption is rampant in China's emerging capital markets.

A cultural revolution

Stock market developments are at the vanguard of China's ongoing cultural, political, and economic evolution. Simply put, stock markets depend on the rule of law, transparency, and the interactions of private parties, whereas China has often relied on government fiat, secrecy, and personal connections. Developing strong securities markets in China thus entails enormous changes.

Anthropologist Ellen Hertz has noted that the "trading crowd" of stock market participants constitutes a new force in Chinese politics. A vibrant discourse about stock markets demonstrates that China's financial press can do much more than simply churn state propaganda. The magazine *Caijing*, in particular, has pushed the envelope in terms of policy discussion and investigative journalism. Not many articles in China endorse Falun Gong or Taiwan's independence, but many contain vociferous criticism of the government's stock market policies, including its clumsy efforts to sell off state-owned shares.

—Walter Hutchens

Foreign investors wishing to establish fund-management or securities companies under the new rules may face challenges in finding suitable and willing Chinese partners.

tablish a fund-management company and at least ¥500 million ($60.4 million) for a securities company. As noted above, investors in fund-management companies must have at least ¥300 million in paid-in capital, but investors in securities companies do not have a paid-in capital requirement.

The minimum paid-in capital requirement for shareholders in fund-management companies seems misguided. Although the ¥300 million threshold is the same for both foreign and Chinese investors, the real issue should not be how much capital investors ostensibly have but whether they are capable of adding value through investment of capital or expertise. In reality, several individual foreign asset-management companies already manage assets that exceed by many times the entire amount invested in the current PRC funds industry. Rather than requiring that the entity directly holding an investment in a fund-management company be over-capitalized, a more artful approach would be to require that a shareholder or its parent have a certain amount of assets under management.

Finding suitable partners

Foreign investment, as a general matter, is eagerly sought in China. But foreign investors wishing to establish fund-management or securities companies under the new rules may face challenges in finding suitable and willing Chinese partners.

Each Chinese partner in a fund-management company must have at least ¥300 million of paid-in capital, and the lead promoter of the company must be a trust and investment company (few of which remain, after waves of government clean up in the sector) or a securities company.

Moreover, qualified Chinese entities face significant disincentives to accept foreign investment. For example, domestic securities companies with foreign investment cannot earn lucrative brokerage commissions for A-share trading or income from proprietary trading of A and B shares. In addition, a fund-management or securities company that accepts foreign investment apparently cannot conduct an IPO, because the Company Law does not permit limited liability companies to list. If a domestic company remains a company limited by shares, however, it can raise additional capital through an IPO and avoid restriction on its business scope.

A Chinese securities firm that wants to list and continue lucrative A-share brokerage or proprietary A- and B-share trading businesses may establish a new securities company with foreign investors rather than convert the existing entity into one with foreign investment. However, the capital requirements for a new securities company and the prospect of creating a competitor (for underwriting business, at least) could discourage this option.

Foreign professionals

The new rules set no limits on foreign participation in the day-to-day operations of foreign-invested fund-management or securities companies. However, they do require that the board chair, the general manager, and other top-level officers be qualified to engage in the securities business under CSRC regulations. These qualifications include passing an industry exam in Chinese—a challenge for many foreign fund managers. CSRC has indicated that it may waive some of the normal personnel qualification requirements for foreign professionals in fund-management companies, but implementation remains unclear.

Other CSRC regulations concerning fund-management and security company officers may also affect foreign personnel. For example, existing regulations prohibit officers and directors of such companies from having other employment or from trading securities.

Joining a party in progress

The new rules are a welcome invitation for foreign investors interested in entering China's rapidly developing securities markets as shareholders in fund-management and securities companies. But the invitation is circumscribed by ownership caps, business scope restrictions, and a limited pool of qualified Chinese partners. Moreover, investors establishing ventures under the new rules will be joining a party already in progress. Foreign firms will have their work cut out for them in the PRC's turbulent and immature capital markets. 完

CORPORATE GOVERNANCE WITH CHINESE CHARACTERISTICS

STEVEN SHI AND DRAKE WEISERT

Chinese officials are addressing the widespread problem of ineffective and corrupt management and accounting in Chinese public companies

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China, like the United States, has weathered a number of its own financial scandals over the last year. As a result, PRC officials are examining more closely than ever the issue of corporate governance—the means by which various corporate participants, including managers, shareholders, and banks, share rights and responsibilities. Legislation has tackled many problems in recent years, including lack of transparent information disclosure, the need to separate enterprise from government control, and the need for independent board directors. This year the PRC government announced that local regulators would crack down on corporate and securities law violations, focusing on the relationship between listed and parent companies, the use of capital raised from markets, and the accuracy of financial data. Such initiatives, however well-intentioned, demonstrate that China's corporate culture is not yet entirely successful in fostering professional managerial behavior.

Early reform

Chinese officials have been studying corporate governance ever since they launched the Shanghai and Shenzhen stock exchanges in December 1990 and April 1991, respectively. Officials hoped the stock markets would put household savings to use as financing for listed companies, most of which were—and still are—profitable parts of state-owned enterprise (SOE) parents. They were also interested in separating SOE management from government. As China's capital market developed and SOE reform progressed, a string of SOEs were restructured into "shareholding" firms—a new structure for PRC enterprises—in the early 1990s. Some of these shareholding enterprises undertook initial public offerings (IPOs) and listed on the Shanghai and Shenzhen exchanges. To date, more than 1,100 companies have listed on the exchanges, according to China's regulatory body, the China Securities Regulatory Commission (CSRC), and numerous unlisted SOEs have turned into shareholding or limited liability entities.

PRC authorities that supported these economic reforms initially hoped the existence of capital markets could facilitate the introduction of a modern enterprise management system based on efficiency and transparency. They also hoped reforms would help overhaul ailing state-owned businesses without the social turbulence that they feared would result from massive bankruptcy in the SOE segment of the economy. Authorities focused on how to allocate controlling rights among corporate leaders and prevent excessive control by management; how to ensure that management maximizes investors' interests; and how to design and implement incentive mechanisms.

Current legal framework

The current legal framework for corporate governance is based primarily on the following national laws and regulations: the Certified Accountant Law (issued in 1993), Audit Law (1994), Company Law (1994), People's Bank of China Law (1995), Commercial Bank Law (1995), Securities Law (1998), and Accounting Law (1999). The key regulatory bodies involved in the lawmaking process are CSRC, the State Economic and Trade Commission, the Ministry of Finance, and the People's Bank of China.

According to the Company Law, there are three tiers of control over a company's operations: the shareholders' general meeting, the boards of directors and supervisors, and management. The general shareholders' meeting has final say over the key issues of the company, such as approval of the management strategy, the financial budget and key investment plans, and the nomination of the boards of directors and supervisors. The board of directors makes key investment plans and the board of supervisors oversees the decisionmaking process and performance of senior management and directors. And management is responsible for day-to-day operations and for implementing the decisions of the board of directors.

Problems from the outset

In practice, key managers sometimes gain control over the shareholders' general meeting so it functions mainly as a rubber stamp, giving green lights to decisions already made by senior management. Insiders have also occasionally won dominant positions on the boards of directors and supervisors and placed their cronies in board positions. In such cases, the boards of directors and supervisors merely serve the demands of controlling parties and their representatives. In some instances, managers diverted money from state and company coffers into their own pockets—actions that clearly ran counter to the goal of increasing the value of shareholders' investments.

Government and company efforts to build a corporate governance system during the 1990s thus existed largely on paper and ultimately contributed little toward an effective system. Both officials and academics were disappointed when most of these "modernized" enterprises failed to start earning profits. Beginning in 2001, a string of corporate scandals, most of which were spotted by accident (*see* p.42), not only put the buzz-words "corporate governance" (*gongsi zhili*) in newspaper headlines, but also prompted disillusioned investors to demand reform of the country's corporate governance structure for listed companies to revitalize China's sluggish stock market. CSRC issued a raft of new regulations and decrees and punished a number of listed companies, brokerages, accountants, and fund houses. The effect thus far on China's stock market has been minimal, however, and stock prices have not risen significantly since the decline of mid-2001, when the government raised the possibility of flooding the market with a selloff of its large shareholdings.

A string of corporate scandals, most of which were spotted by accident, not only put the buzzwords "corporate governance" *(gongsi zhili)* in newspaper headlines, but also prompted disillusioned investors to demand reform.

The lack of profitability and corruption scandals stemmed from the prevalence of structural distortions among China's listed companies, which have obstructed the development of a healthy corporate management system in China and have created an untrustworthy setting for long-term investors. The systemic problems among China's listed companies include:

- **Concentrated share ownership**

The largest shareholder stake in listed companies averages 44.9 percent, according to a July 2001 issue of *China Securities*. In contrast, the second-largest shareholder typically owns a mere 8.2 percent. Under such a scenario, majority shareholders can easily ignore minority investors and use information asymmetries—whereby board directors and senior managers have access to key information regarding a stock price before individual investors—to beautify the books and defraud new investors.

- **Considerable non-tradable shares**

More than 60 percent of listed companies' shares (both A and B shares) in China are not in circulation, according to CSRC. The considerable amount of non-tradable shares in the market makes management indifferent to the fluctuations in stock prices and the rights of minority shareholders. Meanwhile, external supervision by government industry regulators, and the media, remains limited.

- **The role of the state**

Since most listed firms emerged out of state-owned entities, the government in many cases owns more than half, and in some cases up to 80 percent, of a company's shares. Typically, however, the state does not exercise its rights as a shareholder to influence management effectively. In fact, majority government control of listed companies can make it difficult for systems managers to build healthy corporate governance systems and enhance profitability; state shares played a negative role in corporate governance among 434 firms surveyed in 2001 by Chen Chien-Hsun and Shih Hui-Tzu, research fellows at Taiwan's Chung-Hua Institution for Economic Research. For example, the Ministry of Agriculture, as the supervisory agency of Lantian Co. Ltd., was either unable or unwilling to point out the company's financial misconduct before it became public.

The government appears to be aware of this problem. As mentioned, CSRC worked out a scheme last year to sell off some state-owned shares, but the proposal caused turbulence in the market and drove individual investors—fearing a crash in stock prices from a massive sale of state shares—out of stocks. To maintain market stability, CSRC announced in mid-2002 that it would put the plan on hold.

- **A compromised regulator**

Though PRC regulations governing the relationship between the state and company management are adequate, they are not always implemented, in part because of inadequate resources. Listed companies in China report to multiple government institutions, with each institution exerting considerable influence over the company's management. For example, CSRC shared authority over Lantian with the Ministry of Agriculture and Hubei local authorities. CSRC also lacks independent enforcement authority; it must coordinate any effort to penalize rule breakers with the Ministry of Public Security.

- **Absence of incentive mechanisms for management**

Most listed companies in China lack an incentive mechanism that ties the management team's performance to its compensation. In addition, the absence of solid accounting and

China's Enrons

Since late July 2001, the China Securities Regulatory Commission (CSRC) has reprimanded a number of listed companies for violating provisions relating to financial reporting and management. A few of the highest-profile cases include:

- **Guangxia (Yinchuan) Industry Co. Ltd.**

Guangxia, a listed pharmaceutical company, falsified profits for several years to present itself as a fast-growing entity with sophisticated, state-of-the-art technologies. The company fabricated sales contracts and export figures and exaggerated its financial statements, reportedly inflating net profits by ¥745 million ($90 million). CSRC initiated an extensive probe of the company in August 2001, and the Ministry of Finance eventually stripped the accounting license of its long-standing auditor, leading observers to nickname Guangxia the "Chinese Enron."

- **Sanjiu Pharmaceutical Co.**

CSRC uncovered Sanjiu's troubles in mid-2001. The listed company, which was reportedly China's largest pharmaceutical group, had misappropriated ¥2.5 billion ($302 million) on behalf of a few major shareholders and related business partners without the consent of other shareholders or the public. These diversions amounted to 96 percent of the company's net assets, posing considerable threat to the company's operations.

CSRC reprimanded the senior principals, headed by former military serviceman Zhao Xinxian, and fined the company ¥150 million ($18.1 million). Major shareholders and related business partners had repaid ¥349 million ($42.2 million) to Sanjiu by March 2002. Zhao remains the company's legal representative and the company continues to operate, publishing a quarterly report for the first quarter of 2002.

- **Lantian Co. Ltd.**

Lantian listed on the Shanghai stock exchange in 1996 and was hailed as the first publicly listed Chinese ecological agricultural company. Immediately after its IPO, however, investors grew suspicious of the company's soaring share price and incredibly strong profit growth because its business lines, lake fisheries and lotus processing, were unlikely to generate profits at that level. In 2000, the company had reported ¥1.84 billion ($222 million) in sales income but only ¥8.5 million ($1 million) in accounts receivable—an impossible gap for a legitimate company. Lantian said that it had settled most of its transactions with cash. Analysts have estimated that the company fabricated 2000 net profits of up to ¥500 million ($60 million).

Liu Shuwei, a researcher at the Central University of Finance and Economics in Beijing, wrote a research paper in October 2001 questioning the company's financial safety and sent warnings to state bank officials urging them to reconsider their lending programs to Lantian. Banks stopped extending new loans to Lantian and the company's major creditors, Citic Industrial Bank and China Minsheng Banking Corp., filed lawsuits against the company. CSRC also launched an investigation of the company's connected transactions, suspicious accounts receivables, and inflated earnings.

- **Zhengzhou Baiwen Co. Ltd.**

Henan-based Baiwen, a state-owned retail firm, listed on the Shanghai Stock Exchange in April 1996. Exactly three years later it became one of the first companies that CSRC temporarily delisted, after it reported losses of ¥957 ($116 million) in 1999—the largest one-year loss by a listed PRC company. CSRC later found that the company had inflated profits by ¥19 million ($2.3 million) before its listing and by ¥144 million ($17.4 million) in the three years that it was listed. The company was reportedly found guilty of insider trading and publishing misleading annual reports. CSRC also fined Baiwen's accountants for falsifying audits. In mid-2002, leather products firm Sanlian Group finalized a purchase of 50 percent of the company.

- **Macat Optics and Electronics Co., Ltd.**

Guangdong-based Macat, a motorcycle and camera parts manufacturer, listed in Shenzhen in July 2000. CSRC began investigating the company in November 2000 and in September 2001 announced that the company had fabricated fixed assets of HK$91 million ($12 million) by falsifying imported capital equipment lease contracts; had inflated sales revenue by HK$301 million ($39 million) by issuing fake foreign trade receipts and forging sales contracts and customs documents and seals; and had exaggerated net profits by HK$93 million ($12 million). In January 2002, the local procuratory office indicted senior company executives, the external auditor, and the company's underwriter and asset appraisal agency for implication in fraud activities.

—Steven Shi and Drake Weisert

prevalence of information asymmetries boosts management's autonomy. Unfortunately, China's lack of an accounting culture, coupled with the widespread practice of reporting only good news to higher-ups, make the organic development of a fair incentive mechanism unlikely in the near future.

- **Lax screening for IPO selection**

Poor corporate governance in China begins before a company is approved for listing. Many analysts have highlighted the distortion caused by the government's role in selecting companies for listing. There is also a perception problem: the prevalent mindset among SOE managers is that capital raised from the financial markets is free money that can be squandered with impunity. This attitude has its roots in the era of the planned economy, when SOE managers would receive loans from state-owned banks with no obligation to repay them. In order to increase their chances to be selected for listing, companies have an incentive to inflate their figures and produce deceptive financial reports. Collusion with local governments and interest groups facilitates the circumvention of the minimal accounting rules China maintains.

Companies such as Lantian and Zhengzhou Baiwen Co. Ltd. were, in effect, phony entities even before their IPOs. And government officials showered praise on the companies after the IPOs, obscuring the companies' faults.

- **Underdeveloped capital market**

In many cases, stock prices in China do not reflect corporate performance or operational cycles because institutional investors, insiders, and the listed companies themselves manipulate figures. As a result, investor psychology is not that of "buy and hold" but rather "buy to trade." Chinese investors typically focus less on a company's basic performance when making investment decisions than on the names of the company's key institutional investors. Thus, managers in a Chinese listed company, unlike their Western counterparts, are under little pressure to improve performance and self-discipline.

A chorus for reform

Chinese academics and senior officials have published numerous empirical studies in newspapers and academic journals on the subject of corporate governance. Some of their recommendations are clearly receiving consideration by PRC lawmakers. Wu Jinglian, chief economist with the State Council's Development Research Center (DRC), has criticized excessive intervention from the government and parent SOEs and proposed that listed companies drop their state-owned stakes. Zhang Weiying, professor at Beijing University, has recommended that the government allow company shareholders to select corporate managers and that China privatize its state banks. Dai Yuanchen, an economist at the China Academy of Social Sciences (CASS), believes that more state industries should be opened to private investors.

Wu and CSRC Chairman Zhou Xiaochuan have stated that a crucial obstacle to successful corporate governance of listed companies is "insider control." Wang Guogang, vice director of CASS's Financial Research Institute, has recommended that companies move toward an institutionalized management system to alleviate undue influence by individuals. Wu and Dai proposed the introduction of independent board directorships to monitor the management of listed companies. And Zhang Chunlin, an economist at the World Bank, believes China should set up financial institutions to replace government agencies to monitor enterprise management.

The core of effective corporate governance lies in the creation of a fair and efficient competitive market environment, according to Lin Yifu, professor at Beijing University. Related to this, Zhang Weiying has emphasized the importance of property rights reform in future legislation. And CASS's Wang and the World Bank's Zhang believe that listed companies should replace stock issuances with bond issuances as primary sources of capital.

The prevalent mindset among SOE managers is that capital raised from the financial markets is free money that can be squandered with impunity.

The Code of Corporate Governance

The corporate scandals and capital flight cases that emerged in mid-2001 prompted officials at CSRC and other state regulatory bodies to put corporate governance at the top of their list of priorities for 2002. Reflecting this commitment, in January 2002 CSRC issued the Code of Corporate Governance of Listed Companies in China.

The new code aims to introduce solid corporate governance in listed companies by elevating requirements on accounting procedures and information disclosure, introducing independent directors' systems, and tightening the supervision of corporate management. CSRC officials who drafted the code, and other similar legislation in the past, used the US legal and regulatory systems as models. Though the code directly addresses many of the existing problems in China's financial sector, it will only prove effective if company managers honestly implement—and CSRC strictly enforces—its provisions.

Yet these provisions are promising. For example, the code expands the rights of shareholders. Article 2 states that minority shareholders should have equal status with other shareholders and Article 4 gives shareholders the right to protect their interests through civil litigation and other legal approaches. Article 8 requires that listed compa-

Chinese investors typically focus less on a company's basic performance when making investment decisions than on the names of the company's key institutional investors.

nies make a genuine effort to use modern telecommunications technologies in shareholders' general meetings to improve shareholder participation. And Article 11 gives institutional investors more weight in the decisionmaking process, including in the nomination of directors.

The code attempts to strengthen the roles of the boards of directors and supervisors. According to Articles 29 and 31, a listed company must establish transparent procedures to select the board of directors, and a listed company in which the controlling shareholder owns a stake in excess of 30 percent should adopt a cumulative voting mechanism to ensure the voting interests of minority shareholders. Article 49 requires listed companies to introduce independent directors who do not hold any other positions within the company. Articles 60 and 61 state that members of the board of supervisors must be permitted access to information related to operational status and be allowed to hire independent intermediary agencies for professional consultation, without interference from other company employees.

Finally, the code includes specific provisions on information disclosure. Articles 88 and 89 require the listed company to disclose promptly any information that may have a substantial impact on the decisionmaking of shareholders or associated parties. Articles 13 and 14 require the listed company to fully disclose prices of related party transactions and prohibit it from providing financial collateral to related entities. Article 92 requires the listed company to promptly release detailed information on controlling shareholders. And Articles 25 and 27 require controlling shareholders to honor the independence of the listed company and to avoid interfering or directly competing with the listed entity.

Building trust

China's officials and academics are clearly worried that weak corporate governance is endangering the country's economic reforms. And the problem is not limited to public companies, though private companies are hidden from scrutiny because they are not obligated to publish their financial data. New laws have addressed a number of the issues of greatest concern, including information disclosure and financial fraud, but effective enforcement is by no means assured. China would do well to learn from its own experience, and that of the United States, and work to improve public trust in its companies. 完

China Business

Sales and Investment

MAY 16 – JULY 15, 2002

Compiled by Collins Alt

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

Firms whose sales and other business arrangements with China do not normally appear in press reports may have them published in *The CBR* by sending the information to the attention of the editor.

Accounting and Insurance

INVESTMENTS IN CHINA

Ace International (US)

Purchased a 22.13% stake in Huatai Insurance Co., Ltd. of Beijing. $150 million. 05/02.

American International Assurance Co., Ltd., a subsidiary of American International Group, Inc. (US)

Won approval from CIRC to open a Beijing life insurance operation. 05/02.

OTHER

Munich Re Group (Germany)

Won approval from CIRC to set up a reinsurance venture in China. 06/02.

Tokio Marine & Fire Insurance Co. (Japan), Samsung Fire and Marine Co. (South Korea)/PICC

Will form strategic partnership to develop the Chinese insurance market. 06/02.

Advertising and Public Relations

INVESTMENTS IN CHINA

WPP Group plc (UK)/H-Line Worldwide Ltd. (Beijing)

Will form joint venture, H-Line Ogilvy Co., Ltd., to provide public relations services. (UK:65%-PRC:35%). 06/02.

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

Banking and Finance

OTHER

Korean Asset Management Corp. (South Korea)/CCB

Will cooperate to exchange information and training on handling nonperforming loans. 07/02.

Woori Bank, a subsidiary of Woori Financial Group (South Korea)/BOC

Will form strategic alliance to assist South Korean firms operating in China to obtain RMB-based loans. 07/02.

Allianz AG (Germany)/Guotai Junan Securities Co., Ltd. (Shanghai)

Will form joint venture fund-management company. (Germany:33%-PRC:67%). 06/02.

China UnionPay Co., Ltd. (Shanghai)

Will become a principal member of Visa International (US), allowing Chinese citizens to use their credit cards abroad and allowing Visa to open more outlets in China. 06/02.

Cho Hung Bank (South Korea)

Won license from PBOC to conduct RMB-related business in Tianjin. 06/02.

Hang Seng Bank, a subsidiary of HSBC Holdings plc (UK)

Won license from PBOC to conduct business in foreign currency in Shenzhen. 06/02.

Industrial Bank of Korea (South Korea)

Won license from PBOC to conduct RMB-related business in Tianjin. 06/02.

Korea Exchange Bank (South Korea)

Won license from PBOC to conduct RMB-related business in Tianjin. 06/02.

Chemicals, Petrochemicals, and Related Equipment

INVESTMENTS IN CHINA

Kao Corp. (Japan)

Will form WFOE chemical holding company, Kao Holding Co., to expand and manage previous investments in China. 07/02.

Sekisui Chemical Co., Ltd. (Japan)/Materic Construction System Co., Ltd., a subsidiary of Qingdao Construction Group (Shandong)

Will form joint venture, Sekisui Qingdao Plastic Co., Ltd., to manufacture plastic water pipes. (Japan:25%-PRC:75%). $6 million. 06/02.

Formosa Plastic Corp. (Taiwan)
Will set up WFOE to build PVC plastics factory in Ningbo, Zhejiang. $43 million. 05/02.

Consumer Goods

INVESTMENTS IN CHINA

Sanyo Electric Co., Ltd. (Japan)
Will form WFOE, Qingdao Sanyo Electric Co., Ltd., to manufacture and sell refrigerator compressors. $17 million. 07/02.

Carrefour SA (France)/Harbin Power Equipment Co., Ltd. (Heilongjiang), Liaoning Chengda Group
Will form three retail joint venture supermarkets in Heilongjiang. (France:65%-PRC:35%). 06/02.

DIA Group (Spain)/Beijing Shoulian Group
Will form retail joint venture that will set up discount food chain stores in Beijing. 05/02.

OTHER

Office 1 Superstore International (US)
Will open a 4,500m^2 general store in Shanghai in August. 05/02.

Electronics and Computer Software

CHINA'S IMPORTS

NCR Corp. Ltd. (Hong Kong), a subsidiary of NCR Corp. (US)
Won contract from CCB to provide Personas 84 and 86 machines for bill payment, web advertising, and smart card applications. $14.4 million. 07/02.

Microsoft Corp. (US)
Won contract from TCL Holdings Co. of Guangdong for use of Microsoft's mobile software standard for mobile phones and personal digital assistants. 05/02.

INVESTMENTS IN CHINA

Agilent Technologies Inc. (US)
Opened WFOE maintenance center for electrical measurement equipment in Shanghai. 07/02.

Dell Computer Corp. (US)
Will set up WFOE, Dell China Product R&D Center, in Shanghai. 07/02.

LG Group (South Korea)/Philips Electronics NV (the Netherlands)
Will form joint venture, LG Philips LCD Co., Ltd., to manufacture liquid crystal displays (LCDs) in Nanjing. (South Korea:50%, the Netherlands:50%). $100 million. 07/02.

LG Group (South Korea)/Shandong Langchao Cheeloosoft Co., Ltd.
Will form new joint venture to develop information technology applications, after Shandong Langchao buys outstanding 46% stake from parent Langchao Group. (South Korea:49%-PRC:51%). $6 million. 07/02.

Toshiba Corp. (Japan)
Will purchase remaining 5% of joint venture, Wuxi Huazhi Semiconductor Co., Ltd., from Huajin Electronics Group Corp. of Jiangsu to form WFOE, Toshiba Semiconductor Co., Ltd., which it will relocate, as part of an effort to expand production. 07/02.

TPV Technology Ltd. (Hong Kong)
Will build WFOE LCD factory in Fujian. 07/02.

Asia Vital Components Co., Ltd. (Taiwan), Furukawa Electric Co., Ltd. (Japan)
Will form joint venture, Furukawa Electric Suzhou Co., Ltd., to manufacture and market soldering machines for electric components. $600,000. 06/02.

Tata Consultancy Services Co. (India)
Will set up WFOE software R&D base in Shanghai. 06/02.

Achieva Ltd. (Singapore)/Beijing Stone Technology Co., Ltd.
Will form joint venture, Beijing Stone Computer Co., Ltd., to design and market computer peripherals, components, and software in China. 05/02.

Daifuku Co., Ltd. (Japan)
Set up WFOE, Daifuku Shanghai Co., to provide logistics services for equipment and software. 05/02.

Jabil Circuit Inc. (US)
Will purchase the manufacturing assets of Lucent Technologies of Shanghai, a subsidiary of Lucent Technologies Inc. (US). 05/02.

Motorola Inc. (US)
Will build an advanced integrated chip production base with Leshan-Phoenix Semiconductor Co., Ltd., a joint venture among Leshan Radio Corp. of Sichuan, Motorola Corp., and ON Semiconductor Corp. (US). $375 million. 05/02.

Olympus Optical Co., Ltd. (Japan)
Will invest $2.63 million in its existing facilities in Shenzhen to make digital camera lenses. 05/02.

Toshiba Corp. (Japan)
Will set up WFOE, Toshiba Information Equipment Co., Ltd., to produce IT products in Hangzhou, Zhejiang. 05/02.

Toshiba Corp. (Japan)/Guangzhou Baiyun Electrical Appliance Group Co., Ltd.
Will form joint venture to design and manufacture circuit breakers, electrical appliances, and load switches. (Japan:50%-PRC:50%). 05/02.

OTHER

IBM Corp. (US)/Shanghai Yidong Network Information Co., Ltd.
Formed an alliance to build integrated computer systems for Shanghai government. 06/02.

Microsoft Corp. (US)/SDPC
Will form the SDPC-Microsoft Cooperation Committee to invest in software R&D centers, education institutes, and various software joint ventures. $750 million. 06/02.

Shanghai Hua Hong NEC Electronics Co., Ltd., a joint venture of NEC Corp. (Japan) and Shanghai Hua Hong Group Co., Ltd.
Announced it will begin producing integrated circuits for PRC national ID cards. 06/02.

Engineering and Construction

INVESTMENTS IN CHINA

The Shaw Group, Inc. (US)/Yangzi Petrochemical Corp., a subsidiary of Sinopec
Will form joint venture to manufacture 12,000 tons of pipe in Nanjing New & High Technology Industry Development Zone. (US:50%-PRC:50%). 07/02.

Lafarge SA (France)
Will purchase 70% of Chongqing Cement Plant Co., Ltd. $30 million. 06/02.

Environmental Technology and Equipment

INVESTMENTS IN CHINA

Thames Water plc (UK), a subsidiary of RWE AG (Germany)
Purchased a stake in China Water Co., Ltd. (UK:48.8%-PRC:51.2%). $30.5 million. 06/02.

ThermoEnergy Corp. (US)/Shenzhen Fuhaoheng Investment Co., Ltd.
Will form joint venture to construct and operate wastewater treatment plants in China. 06/02.

Food and Food Processing

CHINA'S IMPORTS

BRL Hardy Ltd. (Australia)
Licensed Dragon Seal Wine Co., Ltd. of Beijing to be sole distributor of BRL Hardy wines in China. 06/02.

ONDEO-Degrémont, a subsidiary of Suez SA (France)
Won contract from the Government of Shandong to supply drinking water to the residents of Qingdao for 25 years. $30 million. 05/02.

INVESTMENTS IN CHINA

E. I. Du Pont de Nemours & Co. (US)/Henan Luohe Shineway Industry Group Co., Ltd.
Will form joint venture, Dupont Luohe Shuanghui Protein Co., Ltd., to produce soy protein additive in China. (US:65%-PRC:35%). 06/02.

H. J. Heinz Co. (US)
Purchased Guangzhou Meiweiyuan Foodstuffs Co., Ltd., Guangzhou Meiweiyuan Foodstuffs Factory Co., Ltd., and Panyu Jinmai Foodstuffs Factory Co., Ltd. to form WFOE, Heinz-Meiweiyuan Food Co., Ltd. 06/02.

Generale Des Eaux, a subsidiary of Vivendi Universal (France)
Bought stake in the Pudong branch of Shanghai Running Water Co. (France:50%-PRC:50%). 05/02.

Machinery and Machine Tools

CHINA'S IMPORTS

Rockwell Automation (US)/Beijing Hollysys Systems Engineering Co., Ltd.
Won contract from the Government of Shenzhen to supply automation systems for local subway project. 06/02.

INVESTMENTS IN CHINA

Hyundai Heavy Industry Co. (South Korea)/Beijing Jingcheng Machinery and Electronics Holdings Co., Ltd.
Will form joint venture to produce hydraulic pressure grabs and forklifts with an annual capacity of 5,100 units. (South Korea:60%-PRC:40%). $27.5 million. 06/02.

Medical Equipment and Devices

CHINA'S EXPORTS

Double Dove Group Co., Ltd. (Zhejiang)
Won contract from Retractable Technologies, Inc. (US) to market Double Dove syringes worldwide. 06/02.

Metals, Minerals, and Mining

CHINA'S IMPORTS

Sino Mining Ltd. (Australia)
Won contract from the Government of Guizhou to develop a gold mine at Qianxinan Buyi, Guizhou. 05/02.

CHINA'S INVESTMENTS ABROAD

Baosteel Group Corp. (Shanghai)/Hamersley Iron Pty. Ltd. (Australia)
Will form joint venture to mine iron ore in Western Australia. (Australia:54%-PRC:46%). $670 million. 07/02.

Baosteel Group Corp. (Shanghai)/Rio Tinto Group (Australia)
Will form joint venture to build and operate a mine in Pilbara, Western Australia, to ship 100 million tons of iron ore to Baosteel each year. $4 billion. 06/02.

INVESTMENTS IN CHINA

Mitsubishi Materials Corp. (Japan)
Will form WFOE to manufacture semiconductor gold wiring in Zhejiang. $3.65 million. 07/02.

Miscellaneous

INVESTMENTS IN CHINA

TMC International Holdings Ltd. (Singapore)/Xi'an Lighten Technology Group Co., Ltd. (Shaanxi)
Will form joint venture to provide education services and products in China. (Singapore:60%-PRC:40%). $145,000. 06/02.

Bally Total Fitness Holding Corp. (US)/China Sports Industry Co., Ltd. (Beijing)
Will form joint venture to set up Bally fitness clubs in China. 05/02.

Rosenbluth International (US)/China Comfort Travel Co., Ltd. (Beijing)
Will form joint venture, Rosenbluth-Comfort Business Travel Service Co., Ltd., to offer travel services in China. (US:49%-PRC:51%). 05/02.

OTHER

IMAX Corp. (US)
Set up Asia headquarters in Shanghai. 06/02.

Lamaze International (US)/Beijing Oriental BabyCare Consulting Co., Ltd.
Will form strategic alliance to introduce Lamaze pregnancy instruction in China. 06/02.

Petroleum, Natural Gas, and Related Equipment

CHINA'S IMPORTS

Nippon Oil Corp.
Won contract from Sinopec to provide heavy oil. 07/02.

US Hydrocarbon Technologies, Inc. (US)
Will license coal liquefaction technology and technical services to Shenhua Group Corp. 06/02.

Nippon Oil Corp. (Japan)
Won contract from PetroChina to export 250,000 kiloliters of fuel oil C for one year. 05/02.

INVESTMENTS IN CHINA

Xinao Gas Holdings Ltd. (Hong Kong)/Rizhao City Town Gas Co., Ltd. (Shandong)
Will form joint venture, Rizhao Xinao Gas Co., Ltd., to distribute piped natural gas in Rizhao, Shandong. (Hong Kong:80%-PRC:20%). 07/02.

BP plc (UK)
Will purchase Royal Dutch/Shell Group's 12 Guangdong gas stations. 06/02.

Hong Kong and China Gas Co. (Hong Kong)/Wuhan Municipal Gas and Heating Power Group Corp.
Will form joint venture to develop Wuhan gas project. $144.93 million. 05/02.

Pharmaceuticals

CHINA'S EXPORTS

Shenyang Sunshine Pharmaceuticals Co., Ltd.
Will license its products to ELPEN Pharmaceuticals Co., Inc. (Greece), and will cooperate with ELPEN in future investments. 07/02.

OTHER

Vital Living Inc. (US)
Will license AHI Management Co. (US) to market Vital Living cardiovascular nutraceuticals in China. 05/02.

Ports and Shipping

INVESTMENTS IN CHINA

Daewoo Construction Co. (South Korea)/Zhuanghe City Port Railway Construction Development Center (Liaoning)
Will cooperate to build port in Zhuanghe, Liaoning. $29.97 million. 06/02.

Power Generation Equipment

CHINA'S IMPORTS

BP plc (UK)/Beijing Kenuo Weiye Technology Co. Ltd.
Won contract from the Citizen Center of Shenzhen to provide a solar photovoltaic on-grid power system. 06/02.

Property Management and Development

CHINA'S IMPORTS

Boustead Singapore Ltd.
Won contract from the Wuxi Foreign Investment Bureau to develop an industrial park in Wuxi, Jiangsu. $27 million. 05/02.

INVESTMENTS IN CHINA

Rodamco Asia NV (the Netherlands)
Purchased 72% of Ascott Group Ltd.'s Somerset Grand Shanghai from CapitaLand Ltd. (Singapore). $23.1 million. 06/02.

OTHER

China Export and Import Bank
Signed agreement with Mauritian Development Bank to provide $12 million in loans to fund a housing project in Mauritius. 06/02.

Telecommunications

CHINA'S IMPORTS

Cisco Systems, Inc. (US)
Won contract from China Unicom to build national videoconferencing network. 07/02.

LM Ericsson AB (Sweden)
Won contract from TCL Mobile Communications Ltd. of Guangdong to supply platform technology for mobile phones. 07/02.

Nera ASA (Norway)
Won contract from Beijing Marine Communication and Navigation Co., Ltd. to set up an advanced land station gateway to provide satellite services. $3.7 million. 07/02.

P-Com, Inc. (US)
Won contract from Datang Telecom Technology Industry Group of Beijing to provide wireless communications equipment. $100 million. 07/02.

AsiaInfo Holdings, Inc. (US)
Won contract from Jiangxi Mobile, a subsidiary of China Mobile, to provide an integrated business and operation support system. 06/02.

Computer Associates International, Inc. (US)
Won contract from Sichuan Mobile, a subsidiary of China Mobile, to deploy Computer Associate's (CA) Unicenter, BrightStor, and eTrust IT solutions. 06/02.

Computer Associates International, Inc. (US)
Won contract from Shenzhen Unicom, a subsidiary of China Unicom, to deploy CA's eBusiness management solutions. 06/02.

LM Ericsson AB (Sweden)
Won contract from Shandong Mobile, a subsidiary of China Mobile, to expand GSM network. $135 million. 06/02.

LM Ericsson AB (Sweden)
Won contract from Guangdong Mobile, a subsidiary of China Mobile, to deploy a MPLS virtual private network in Guangdong. 06/02.

Motorola Inc. (US)
Won contract from China Mobile to expand GSM networks, provide infrastructure solutions, and offer IT services in Beijing, Tianjin, Hubei, and Yunnan. $100.8 million. 06/02.

Oy Nokia AB (Finland)
Won contract from Yunnan Mobile, a subsidiary of China Mobile, to expand GSM network. $75 million. 06/02.

Sewon Telecom Co., Ltd. (South Korea)
Won contract from Legend Group Ltd. (Hong Kong) for GSM mobile phones. $45.3 million. 06/02.

CommVerge Solutions Ltd. (Hong Kong)
Won contract from Zhejiang Unicom, a subsidiary of China Unicom, to supply and install a voice-quality enhancement system. 05/02.

Nortel Networks Ltd. (Canada)
Won contract from China Mobile to expand the GSM network in Hebei. 05/02.

Oy Nokia AB (Finland)
Won contract from Zhejiang Mobile, a subsidiary of China Mobile, to expand GSM network and to conduct Nokia MMS trials. $85 million. 05/02.

Shanghai Bell Alcatel Mobile Communication System Co., Ltd., a subsidiary of Alcatel SA (France)
Won contract from Jiangsu Mobile, a subsidiary of China Mobile, to expand GSM network. $114 million. 05/02.

Sierra Wireless Inc. (US)
Licensed Guangdong Isocreate Communications Co., Ltd. to distribute its wireless network card in China. 05/02.

INVESTMENTS IN CHINA

Pacific Century Cyberworks Ltd. (Hong Kong)/China Telecom
Will form joint venture to provide IT services to financial sector in China. 07/02.

SK Telecom Co., Ltd. (South Korea)/China Unicom
Will form joint venture to provide wireless Internet services. 07/02.

Telstra Corp. Ltd. (Australia)/Shanghai General Electronics Group
Will form joint venture to offer telecom services. 07/02.

Vodafone Group plc (UK)
Will purchase 1% of China Mobile's Hong Kong-listed arm. $750 million. 06/02.

Matsushita Communication Industrial Co., NEC Corp. (Japan)/Huawei Technologies Co., Ltd. (Guangdong)
Will form joint venture, Cosmobic Technology Co., to develop and market mobile phones in China and elsewhere. $8 million. 05/02.

OTHER

EC Founder Holdings Co., Ltd. (Hong Kong)/Tianjin People's Broadcasting Station Transportation Channel
Will cooperate to explore geographic information system (GIS)-based traffic conditions broadcasting system. 06/02.

Siemens AG (Germany)/Datang Telecom Technology Co., Ltd. (Beijing)
Won approval from the Government of the PRC to design and deploy a third-generation mobile network. 06/02.

Agere Systems Inc. (US)/Zhongxing Telecom Co. (Shenzhen)
Will cooperate to build R&D center in Shenzhen. 05/02.

Lionbridge Technologies Inc. (US)/Ningbo Bird Electronics Ltd. (Zhejiang)
Will cooperate to develop and market Java-enabled mobile phones. 05/02.

Transportation

CHINA'S EXPORTS

Tianjin Automotive Group
Won contract from American Automobile Network Holdings Inc. (US) to export 252 Xiali economy cars to the United States. 06/02.

INVESTMENTS IN CHINA

Delloyd Industries Sdn. Bhd., a subsidiary of Delloyd Ventures Bhd. (Malaysia)/Huadu District of Guangzhou
Will build plant to manufacture and assemble automotive parts. 07/02.

The Boeing Co. (US)/Shanghai Airlines Co., Ltd., Shanghai Airport Group Co., Ltd.
Will form joint venture to provide aircraft maintenance service in Shanghai. $80 million. 06/02.

Embraer-Empresa Brasileira de Aeronáutica SA (Brazil)/AVIC I
Will build an aircraft assembly and components factory in China. (Brazil:51%-PRC:49%). 06/02.

TNT Logistics Holding Co., a subsidiary of TPG NV (the Netherlands)/Shanghai Automotive Industry Group Corp.
Formed joint venture, Anji-TNT Automotive Logistics Co., Ltd., to provide management, training, storage, and transportation for automakers in China. 06/02.

DaimlerChrylser AG (Germany)/Beijing Automotive Industry Group Co.
Will extend their joint venture contract by 30 years until 2033. 05/02.

General Motors Corp.
Will purchase a 34% stake of SAIC Wuling Automobile Co., Ltd., a joint venture between Shanghai Automotive Industry Group Corp. and Liuzhou Wuling Automobile Co. Ltd., to produce minivans in Guangxi. $30 million. 05/02.

OTHER

BMW AG (Germany), Brilliance China Automotive Holdings Ltd. (Hong Kong)
Received approval from the PRC government to set up a car-manufacturing joint venture. 06/02.

DaimlerChrysler AG (Germany)/BOC
Will cooperate to offer auto financing options to Chinese consumers. 06/02.

PSA Peugeot Citroen SA (France)
Announced it will resume vehicle production in China by 2004. 06/02.

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short takes

English-language Legal Hotline

For the last three years, the Beijing Bureau of Justice has offered a phone service to foreigners in China seeking legal advice for business and related concerns. The bureau estimates that the service has helped more than half a million callers. This summer the service added an English-language option. Callers can dial (010) 160-0148 during weekday business hours.

Practical English Test for Chinese Business Professionals

China's WTO membership and 2008 Olympic commitments have compelled the State Economic and Trade Commission (SETC) to create a practical and conversational English test for Chinese business professionals as a part of its training initiative. Testing will begin in late 2003 or early 2004.

Educational Testing Service (ETS), based in Princeton, New Jersey, signed a $70 million contract with Beijing Topeak International Education Investment, Co., Ltd. to provide the standardized test over the next five years. ETS is currently responsible for managing several exams, such as the Graduate Record Exam and the Test of English as a Foreign Language, in China.

China Establishes Antidumping Service Centers

The Investigation Bureau of Industry Injury, under SETC, has approved the establishment of an antidumping consulting service center under the China Association of Automobile Manufacturers and a separate general antidumping center in Xiamen, Fujian. The centers will conduct research on antidumping, antisubsidy, and safeguard measures and will provide judicial consultation and training. They will also assist in investigative work on injury cases involving foreign imported products that are subject to antidumping, antisubsidy, or safeguard measures, and analyze the enforcement and impact of such cases.

Visa, MasterCard Announce Links to PRC ATM Network

Foreign travelers to Beijing are now able to withdraw cash from more outlets than the few Bank of China and other ATMs throughout the city. Since June 27, Visa International Service Association has linked up with the Industrial and Commercial Bank of China's (ICBC) 780 Beijing ATMs. Visa also announced a link-up with China UnionPay Co., a for-profit PRC company launched in March to integrate China's disparate banking card systems into one centralized, compatible network. MasterCard International Inc. quickly followed Visa in joining the UnionPay network and announced that ICBC ATMs would soon accept foreign currency cards bearing its logo.

In a related move, Visa announced that it is also planning to issue foreign-currency, tourist debit cards later this year to Chinese citizens through its partner Chinese banks. Chinese citizens hoping to use the card will be required to deposit foreign currency into the debit card account before using the card overseas. Neither of the two expanded operations signal a relaxation of strict State Administration of Foreign Exchange controls, as the operations do not involve conversion of renminbi to foreign currency, a process that involves documentation and approval.

Beijing Olympics Update

First Batch of Olympic Ownership Tenders Expected Mid-September

Plans for the release of tender documents for the main sports arena and facilities for Beijing's 2008 Olympics Games moved forward with an unofficial midsummer announcement that the first round of tenders for public bidding on key venues would be released in mid-September. The announcement was made by an outside consultant appointed by the Office for Beijing Olympics 2008 projects under the Beijing Municipal Development Planning Commission (BDPC).

BDPC and the Beijing Organizing Committee for the Olympic Games (BOCOG) are jointly preparing tender documents that will specify funding, design, building, and operation of the National Stadium, National Indoor Stadium, National Swimming Center, Olympic Village, a meeting and exhibition center, and several other commercial facilities. Final tender documents are not yet complete but the State Development Planning Commission is expected to approve them in mid-September.

Authorities appear to want to select winning bids by the end of 2002. The bid period would, in that case, only last two months. It may prove difficult for companies to design facilities, undertake feasibility studies, and make all necessary financial analyses in time to submit bids on projects.

The Beijing government appears to expect financing for these projects to come entirely from the private sector under a build-operate-transfer model, with a concession period of 30 years. There is no indication thus far whether Beijing will inject International Olympic Committee or Chinese government funds into these projects. The Beijing government is asking companies to form consortia of finance, design, engineering, and operations companies to make a single bid for each tendered project.

Foreign Firms Among First Winners

Earlier in the summer, China named two US companies as winners in its first 2008 Olympic Games project bid competitions. PricewaterhouseCoopers, one of five accounting firms invited to submit bids, will provide accounting services related to the development of Olympic venues.

Another US firm, San Francisco-based Sasaki Associates, Inc., teamed with the design firm Tianjin Huahui Architectural Design & Engineering Co., Ltd. to win the $250,000 international competition for conceptual planning and design of the Beijing Olympic Green. The Sasaki-Huahui team also won second prize in the Wukesong Cultural and Sports Center design competition—no first prize was awarded. Although there is no guarantee that the winning designs of the Sasaki-Huahui team will be used, the success of the two US companies is an encouraging sign that BOCOG will consider foreign firms and will honor its commitments to a public and transparent bidding process. Unfortunately, the winning and runner-up designs, now on public display in Beijing, have come under heavy media criticism for falling short of expectations.

The jury, consisting of six foreigners and seven Chinese, reportedly favored natural landscapes. "Green Olympics," one of the three themes of the Games—along with "High-Tech Olympics" and "People's Olympics"—is gaining popularity with the organizers. Jury members noted their preference for mountains and water, the two essential elements of traditional Chinese painting.

BOCOG Releases Activity Plan

BOCOG released its "Beijing Olympics Activity Plan" on June 13, which mirrors announcements released in the March 2002 "Olympic Action Plan." The five-part activity plan restates BOCOG's three-stage timeline for venue and Olympic-related infrastructure projects. Stage one includes preparations and leadership group organization (December 2001-June 2003), stage two involves venue and facility construction (July 2003-June 2006), and stage three includes completion and testing (July 2006-summer 2008). The plan emphasizes the correlation between the economic development of Beijing and the successful staging of the games as well as the successful integration of Olympic venues into the city's urban design plans. The plan also calls for Beijing to implement Euro II vehicle emission standards from January 1, 2003. For an English-language version of the plan see *www.beijing2008.org/new_olympic/eolympic/plan.htm.*

Olympics "Hot Sheet"

The Commercial Service office at the American Embassy in Beijing compiles news articles from the Chinese press on the 2008 Beijing Olympics in the form of a free online newsletter. Individuals interested in signing up for this newsletter can contact David Snodgrass via e-mail at David.Snodgrass@mail.doc.gov.

Planned Spending Rises

Chinese news media have reported that the budget for spending on environmental cleanup, infrastructure, and public works in advance of the Olympics will reach $6.9 billion, $150 million more than earlier estimates.

Olympics Slideshow

To view a 100-slide, 20-MB Flash presentation prepared by the Beijing Municipal Planning Commission on Beijing's Olympics plans, visit *www.bjghw.gov.cn/flash/guihua.swf.*

—US-China Business Council staff

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First Impressions

I visited China this summer for the first time in my life. This isn't so extraordinary except that I am second generation Chinese-American, and I and my friends and family—none of whom had been back to China since leaving more than 30 years ago—were curious about the land of my ancestors. Would I be impressed, overjoyed, shocked? None of Amy Tan's novels gave me a clue.

My parents came from a village in Guangdong. I was born in Washington, DC, and moved with my family out to the suburb of Alexandria, VA, when I was two. Since my parents spoke no English, I grew up speaking household Cantonese with a small number of other children whose parents were from the same Chinese village—an experience quite different from growing up in a large Chinatown such as those in New York and San Francisco.

In college, a friend of mine persuaded me to study Mandarin with her. I had a car to take us to Chinese classes at a nearby college, and thought vaguely that learning Mandarin would be useful. I studied it for a total of two years, taking a year off in between to study in Paris. Studying Chinese seemed fun then, but I never had occasion to use it—and not for a long time afterwards.

Years later, I find myself working for the US-China Business Council, and needing to travel to China as part of my responsibilities as business and marketing manager for *The China Business Review*. I took a language review class to refresh my rusty Mandarin. Yet my trip would be like that of the typical foreign businessperson: I would meet mostly with the foreign or English-speaking Chinese managers of foreign-invested enterprises in Beijing, Shanghai, and Hong Kong. I would not have time to visit the home village. While glad finally to make the trip east, I was a bit wary of traveling by myself in what was, to me, a foreign country.

My first stop—Beijing—was enjoyable and didn't seem too unfamiliar, although I thought it would have more neighborhoods. Perhaps this was because I stayed in a hotel in the central business district, and my excursions beyond that were by car. People told me Shanghai, my second stop, would be much different from Beijing—as New York differs from Washington. I found it to be more like a large Western city than Beijing, but I wasn't necessarily looking for Western on this trip. I was expecting to enter a Chinese city and see a charming and distinct Chinese culture. I didn't find that in either Beijing or Shanghai.

The hardest part of being in China was looking the part but not speaking the language. I'm sure other Chinese-Americans experience this, though I didn't happen to notice any other struggling Asians during my brief stay. In Beijing, a colleague asked me if I felt at home in China, with all the other Chinese around. No, I replied, I'm American—a response that seemed to puzzle him. Another day, I stopped into an American hotel to use the restroom. I walked up to an expatriate manager and asked him in English where the restrooms were located. He looked at me and responded in English that he didn't speak any Chinese. Well, I answered, neither do I; where's the restroom?

People were often amazed that I spoke so little Mandarin: You don't speak *any* Chinese? They would ask. Well, yes, I would say, but only household vocabulary for a dialect of Cantonese—that is, not the Hong Kong one. Usually, this took some time for me to explain and was still difficult for them to understand, so often I would just smile politely and shrug.

I was occasionally able to use Mandarin. Out to dinner one evening with two couples, I was the only Asian face in the group. I entered the restaurant, told the hostess we wanted a table for five people in a non-smoking section, asked the waitress for green tea, and then had to resort to English when she asked me which dishes we wanted. Though I understood her question, I had reached the limit of my vocabulary.

I had heard that Hong Kong was a sophisticated city, and that I would be able to get by on English. This was more or less true. The questions was, whose English? American, British—or Hong Kong? There was the time I directed the taxi driver to Pedder Street, which I pronounced as any American would—that is, just the way it is spelled. He was confused, so I spelled it for him, which didn't seem to help, and said it was by Queensway, which he seemed to understand. As we approached the street, he exclaimed, "Ah, Pedder (Peh-duh) Street!" Like I said....

Another time, I had dinner with a colleague, a Hong Kong native. She wasn't familiar with the region on the mainland where my parents used to live. In her enthusiastic attempt to teach me about Hong Kong and Chinese culture, she explained to me all of the dim sum dishes on our table, even though this was unnecessary—my parents had been in the restaurant business at one time. She told me she used a wok at home, spelled w-o-k. She was surprised when I told her that I regularly eat Cantonese food and other cuisines, too. It seemed amazing to her that people from America could have had such exposure.

I enjoyed my trip, despite the difficulties making myself understood. But I thought Beijing and Shanghai otherwise resembled many other large cities and I wish I could have experienced the parts of China that are less internationalized; then I could have returned with some real stories—and perhaps a better understanding of the country. I plan to challenge myself more on my next visit by traveling to the countryside. Meanwhile, I'll start preparing how to explain to even more people in China what it means (to me) to be Chinese-American.

—*Kattie Lee*

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